February 21 2022

Macro Weekly

Week 8/2022

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Highlights

The world around us

The Norwegian economy

Market charts & comments

Last week

- **The virus**
  - Hong-Kong and China have no easy way out as the zero tolerance policy is challenging with a very contagious Omicron virus around. In the rest of the world, at least in the well vaccinated Wester countries, the virus is on the retreat, at least as a serious health challenge. Restrictions are eased
- **China**
  - No **inflation** to be seen, the headline down to 0.7%, the core at 1.2%
- **USA**
  - As we assumed, the **minutes from the late Jan FOMC meeting** could not be more aggressive than market had already discounted, after a 67 bps lift in the Dec-22 Fed funds future rate since the meeting. The 'geopolitical situation' also helped rate expectations down most places. Still, the minutes confirmed majority of the FOMC members have changed their mind vs the need for monetary tightening the coming months
  - **Retail sales** recovered more than expected in January, following the surprisingly large decline in December. Sales are still well above a reasonable long term trend. In value terms, total sales are up 24% from Feb-20!
  - **Housing data** were in sum better than expected in Dec. Building permits rose. Existing home sales climbed sharply, and prices rose at the fastest pace since last April as the inventory of unsold homes is 'empty'. No signs so far of lower demand for new mortgages, even if the 30 y fixed rate is up 125 bps from the bottom, to 4.25% (BTW, think of a 4.25% mortgage rate in Norway, a revolution?)
  - **Manufacturing production** is heading steadily upwards, if not as fast as surveys have signalled until recently. Now, surveys are easing somewhat, and the first February **Fed manufacturing surveys** confirmed a weaker trend – even if the two surveys still signal growth above trend – and cont. price pressures
  - **Atlanta Fed's GDP nowcaster** suggests a 1.3 growth rate in Q1, down form 6.9% in Q4. **Conference Board's LEI** dropped to below zero in January
- **UK**
  - **Inflation** was higher than expected in January, both the total and the core as prices continued to increase by some 0.5% per month. **Unemployment** is trending down, the number of **vacancies** rose sharply in Q4, and **wage inflation** has been accelerating the recent months
- **Sweden**
  - **Annual core inflation** (CPIF x energy) accelerated much more than expected in January, to 2.5% from 1.7%, as prices rose 1.4% m/m (our seas. adj). Several goods and services contributed but some reversal must be expected the coming months. If not… The headline CPI fell due to a sharp decline in electricity prices, just like in Norway
- **Norway**
  - **Mainland GDP** contracted 0.4% in December, slightly more than expected but still grew 1.4% q/q in 4Q (5.8% annualised, and by 4.2% last year). Some services was of course hit by Covid restrictions in Dec, and activity was probably below par in these sectors until mid February. The downturn will probably be both shorter and milder than NoBa assumed in Dec. Cost inflation is moderate but so are price increases (x the energy sector). The Mainland business (x electr.) operating margin remains stable, at a low level
  - **Norges Bank's expectation survey** reported higher price & wage expectations, and nobody believes in the long term 2% inflation target anymore! The survey was conducted before inflation fell sharply in January, and before the official TBU (Technical committee on wage formation) published a moderate 2.6% 2022 inflation forecast. We assumed they would say 2.5%
  - **Norge Bank's outgoing governor Olsen** warned that too high wage growth would be met by a tighter monetary policy
  - **Oil and gas companies** are signalling a further decline in their investments in 2022 but more projects will be added due to the temporary tax relief, and investments will probably increase substantially in 2023. The **manufacturing sector** is planning a huge increase in investments in 2022, far above earlier f'casts, while investments in **power supply** is expected further down

The Calendar: Preliminary PMIs, US household spending, housing. Norwegian labour market

Time	Count.	Indicator	Period	Forecast	Prior
Monday Feb 21					
06:00	SW	Home-Price Index	Jan		
09:15	FR	Manufacturing PMI	Feb P	55.5	55.5
09:15	FR	Services PMI	Feb P	54.0	53.1
09:30	GE	Manufacturing PMI	Feb P	59.8	59.8
09:30	GE	Services PMI	Feb P	53.1	52.2
10:00	**EU**	**Manufacturing PMI**	**Feb P**	**58.7**	**58.7**
10:00	**EU**	**Services PMI**	**Feb P**	**52.1**	**51.1**
10:00	**EU**	**Composite PMI**	**Feb P**	**52.9**	**52.3**
10:30	UK	Manufacturing PMI	Feb P	57.0	57.3
10:30	UK	Services PMI	Feb P	55.5	54.1
Tuesday Feb 22					
10:00	GE	IFO Business Climate	Feb	96.5	95.7
15:00	US	S&P CoreLogic CS 20-City YoY	Dec	18.2%	18.3%
15:45	US	Manufacturing PMI	Feb P	56	55.5
15:45	**US**	**Services PMI**	**Feb P**	**53**	**51.2**
16:00	US	Conf. Board Consumer	Feb	110	113.8
Wednesday Feb 23					
11:00	EU	CPI YoY	Jan F	5.1%	5.0%
11:00	EU	CPI Core YoY	Jan F	2.3%	2.3%
Thursday Feb 24					
08:00	**NO**	**Unemployment Rate LFS/AKU**	**Dec**	**3.5%(3.5)**	**3.5%**
08:00	**NO**	**Payrolls, wages**	**Jan**		
08:00	NO	Population growth	Q4		
08:00	SW	Unemployment Rate SA	Jan	8.0%	8.0%
14:30	US	Chicago Fed Nat Activity Index	Jan		-0.15
14:30	US	Initial Jobless Claims	Feb-19	235k	248k
16:00	US	New Home Sales	Jan	807k	811k
14:30	US	GDP Annualized QoQ, final	4Q S	7.0%	6.9%
Friday Feb 25					
08:00	NO	Hotel guest nights	Jan		
09:00	SW	Economic Tendency Survey	Feb		110.1
09:00	SW	Consumer Confidence	Feb	90.0	90.1
10:00	**NO**	**Unemployment Rate NAV**	**Feb**	**2.4% (2.4)**	**2.6%**
11:00	EU	Economic Confidence	Feb	113	112.7
14:30	US	Personal Income	Jan	-0.4%	0.3%
14:30	**US**	**Personal Spending**	**Jan**	**1.5%**	**-0.6%**
14:30	**US**	**PCE Core Deflator MoM**	**Jan**	**0.5%**	**0.5%**
14:30	US	Durable Goods Orders	Jan P	0.9%	-0.7%
14:30	US	Cap Goods Orders Nondef Ex Air	Jan P	0.3%	0.3%
16:00	US	U. of Mich. Sentiment	Feb F	61.7	61.7

- **Preliminary February PMIs**
  - » The January PMIs were far weaker than expected most places. The decline in the global PMI equalled a cut in the global GDP growth rate to 2% from 4%. Most likely, the Omicron was to blame, but underlying growth is probably slowing as well. A partial recovery in February is expected all over the place – but Japan reported sharp decline this morning
- **USA**
  - » **Personal spending** must have recovered most of the December decline in January, witnessing the larger than expected increase in retail sales. Focus is still on prices, the PCE deflator is expected to follow the CPI path, upwards
  - » **Durable orders** are still on the way up, and a further increase is expected in January
  - » The **housing market** is tight, and existing home prices are still up 18% y/y (the Shiller index). Normally a good environment for **new home sales** (if not building cost have stop up too)
- **Sweden**
  - » Neither **house prices, unemployment** nor **consumer & business sentiment** will probably support the Riksbank's zero-until-H2-24 policy stance
- **Norway**
  - » Both **NAV and LFS (AKU) will report unemployment**. We expect a decline in the NAV unemployment rate, as covid restrictions were eased in mid-February. The Nov – Jan LFS unemployment rate was probably unchanged
  - » We expect a flattening of the **no. of employees** in January, as Covid restrictions still were in place. The risk may be at the downside, following a surprising strong growth in December. Monthly wage stats are too volatile to draw any conclusions
- **And we hope, not too disturbing news from the east front**
  - » Biden and Putin plans to meet again

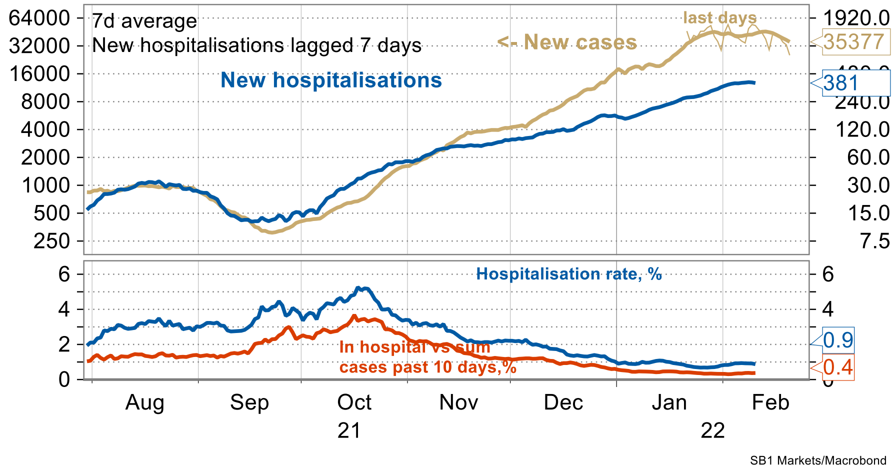
Sources: Bloomberg. SB1M est. in brackets. Key data are highlighted, **the most important in bold**

Covid-19

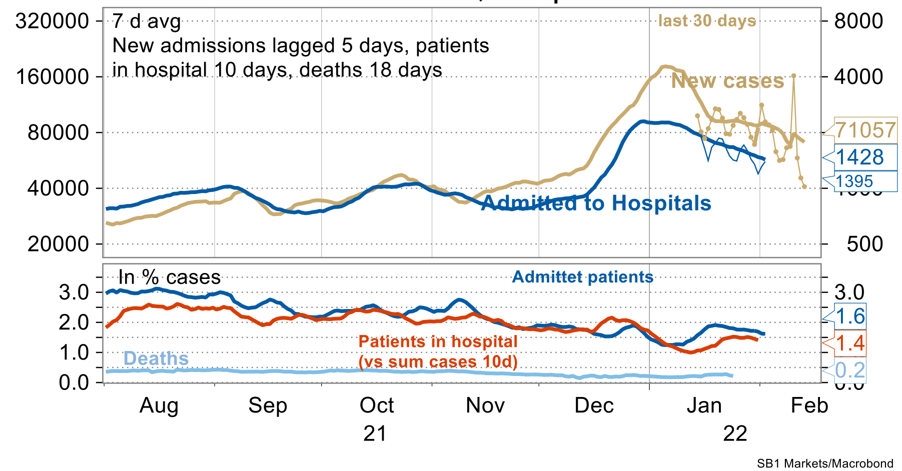
Case counting has become less relevant & reliable: But they are heading down

More new hospital admissions in Denmark but the peak is near? Still a very low level in Norway

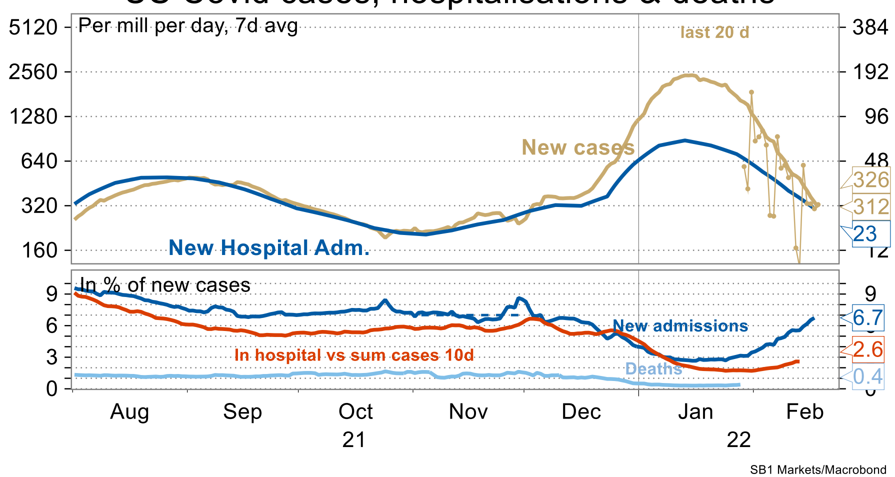
Denmark New Covid cases



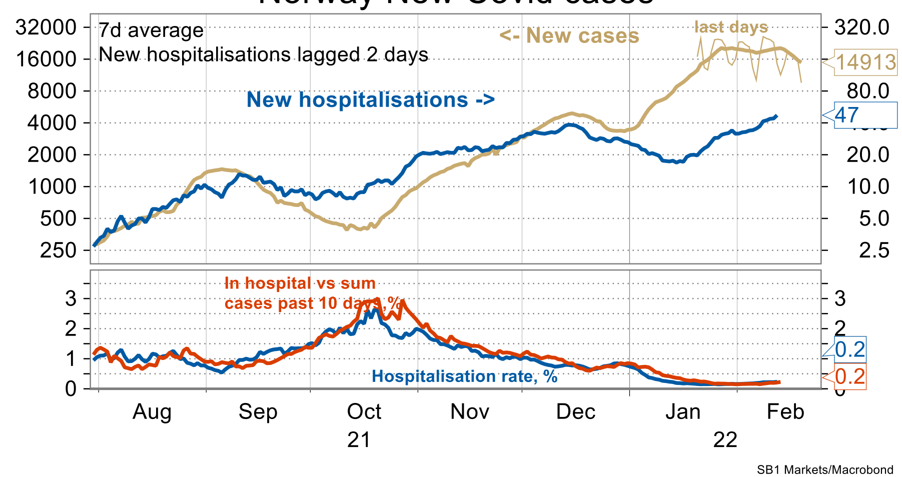
UK Covid-10 cases, hospitalisations



US Covid cases, hospitalisations & deaths

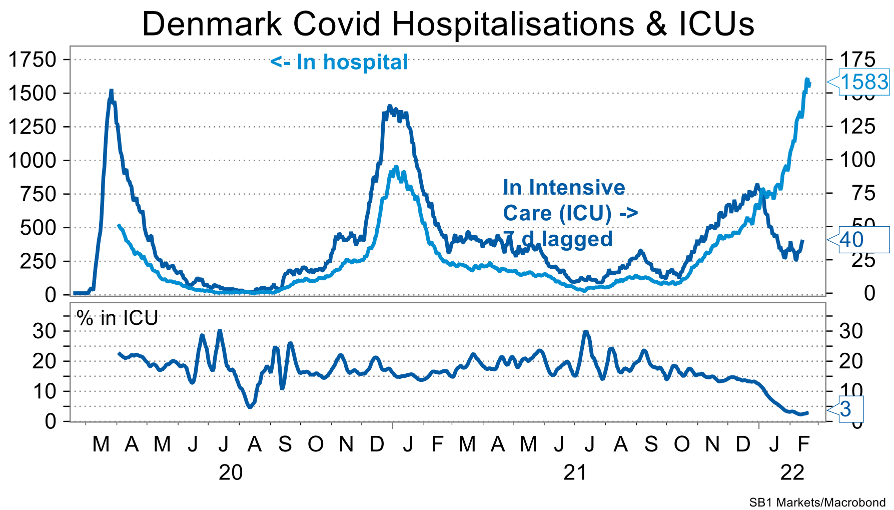


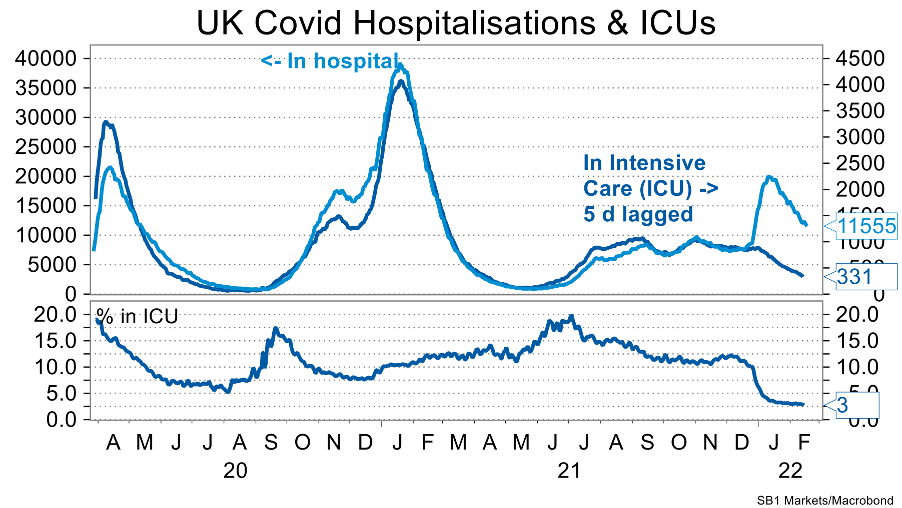
Norway New Covid cases

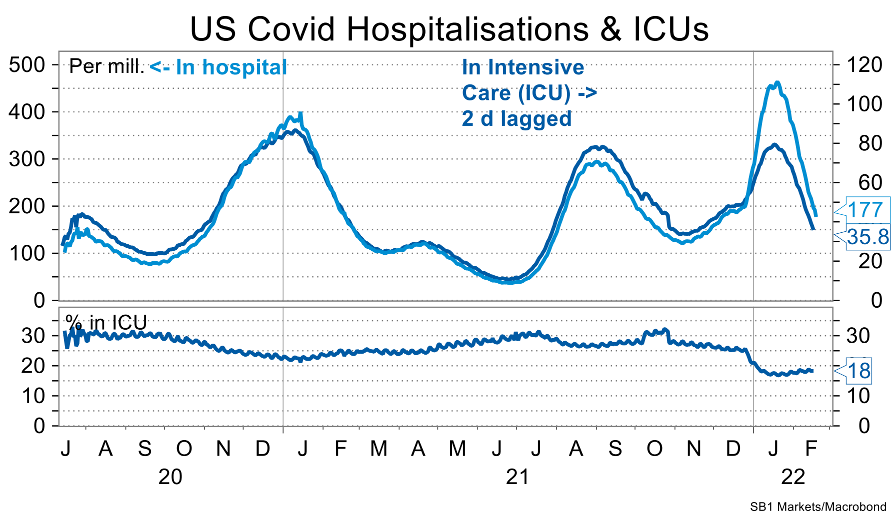


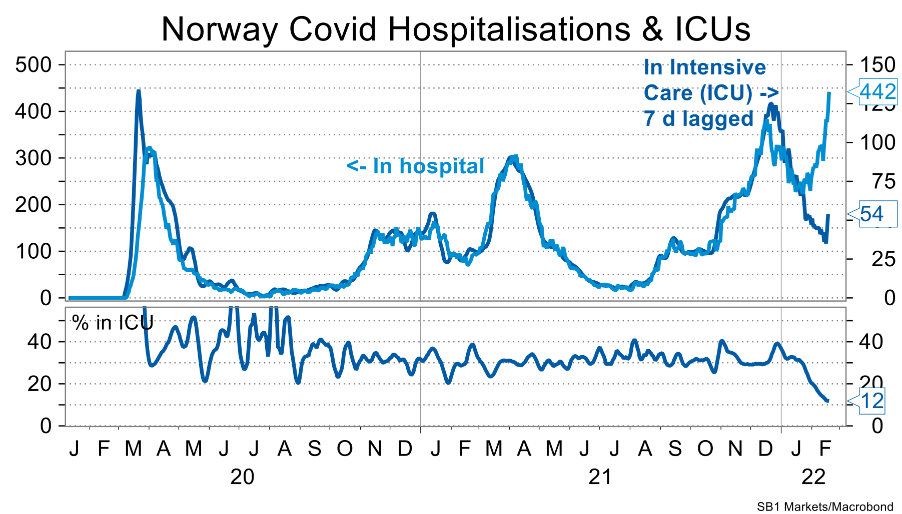
Hospital beds are filled up in Denmark & Norway but not in the ICUs

A steady decline in hospitalisations and ICU beds in UK & US.

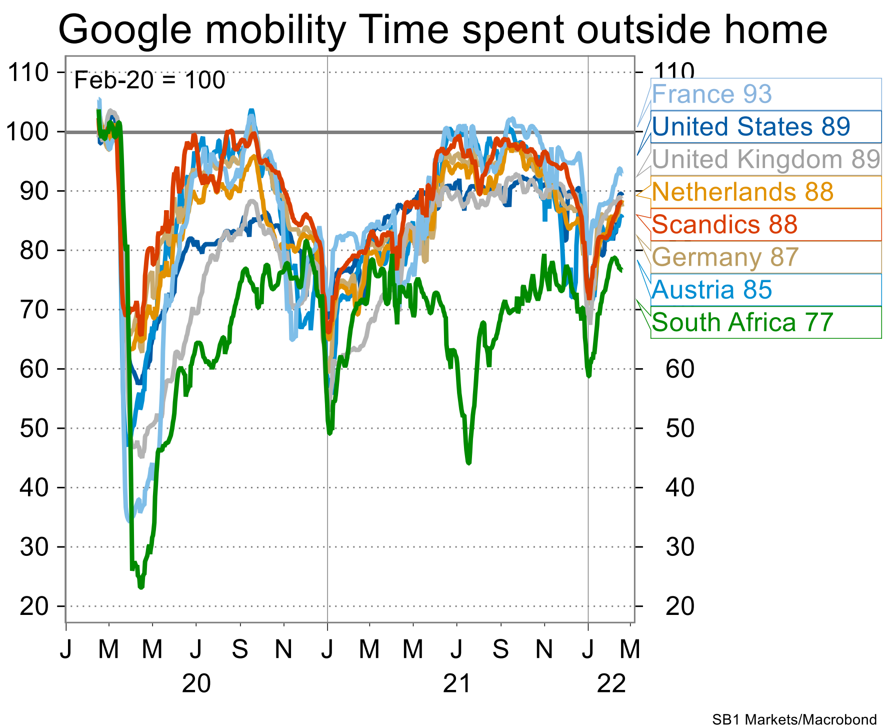


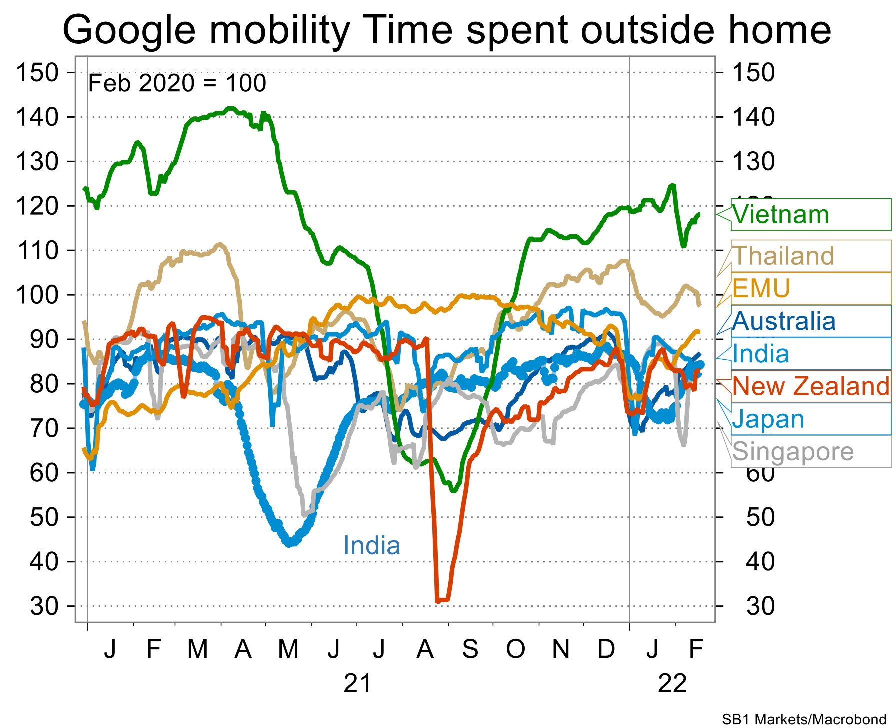






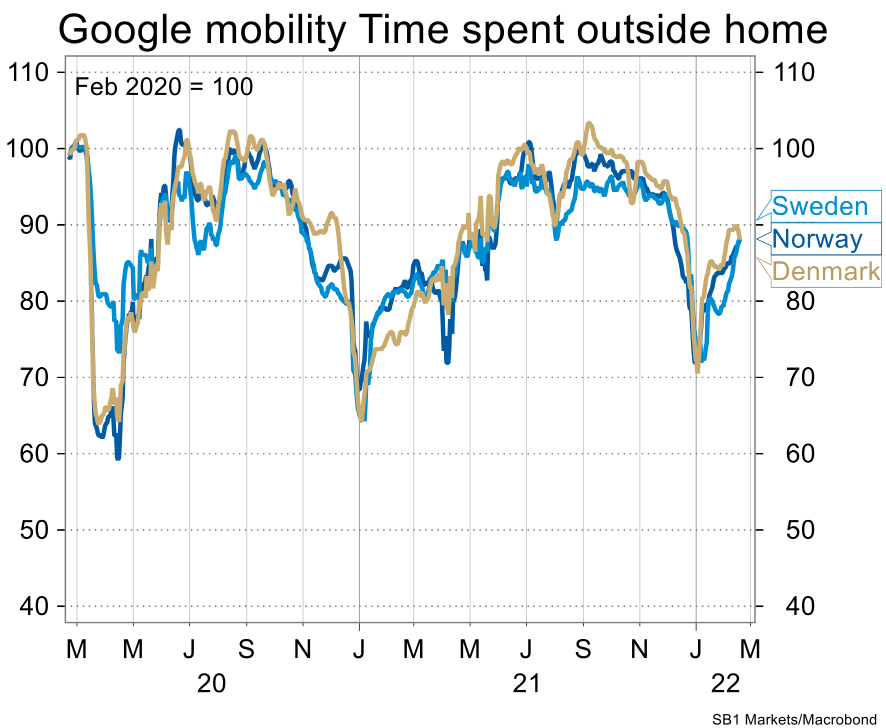
Mobility on the way up in the West, still some challenges in the East?

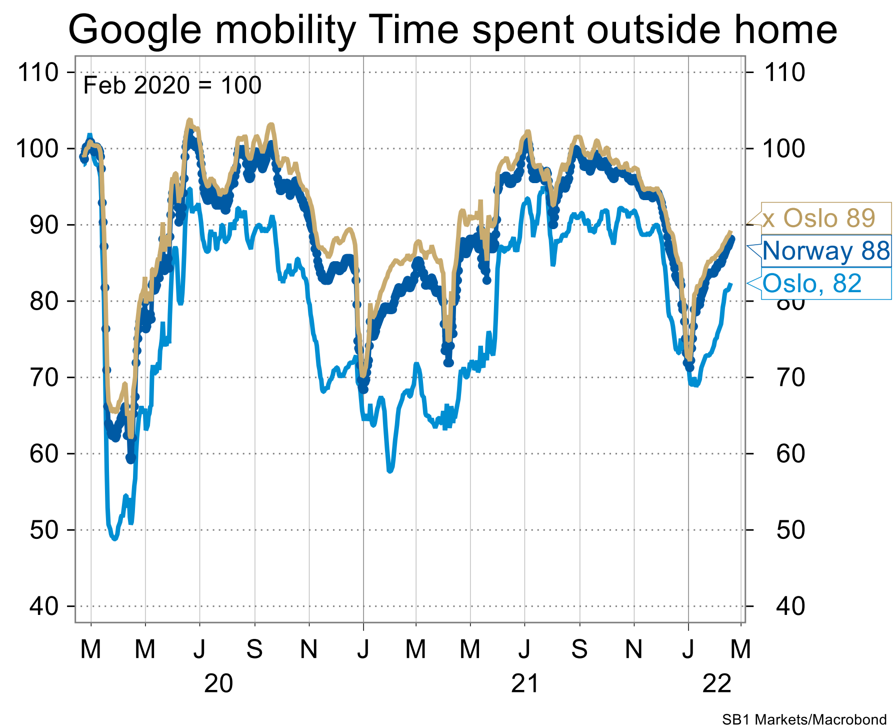




Mobility is on the way up in the Scandics, and in all parts of Norway

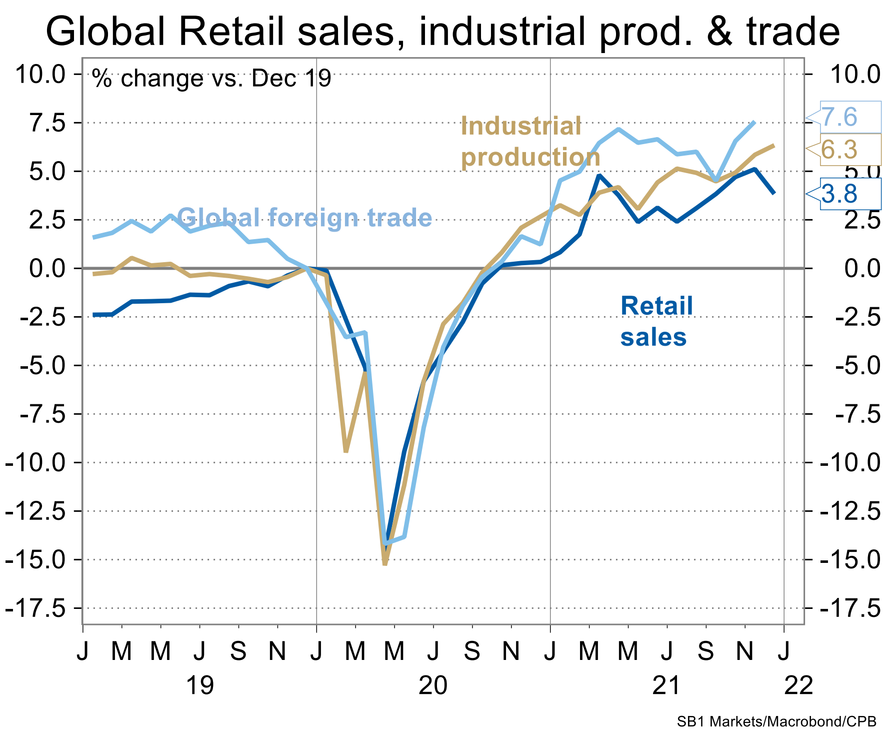
For good reasons

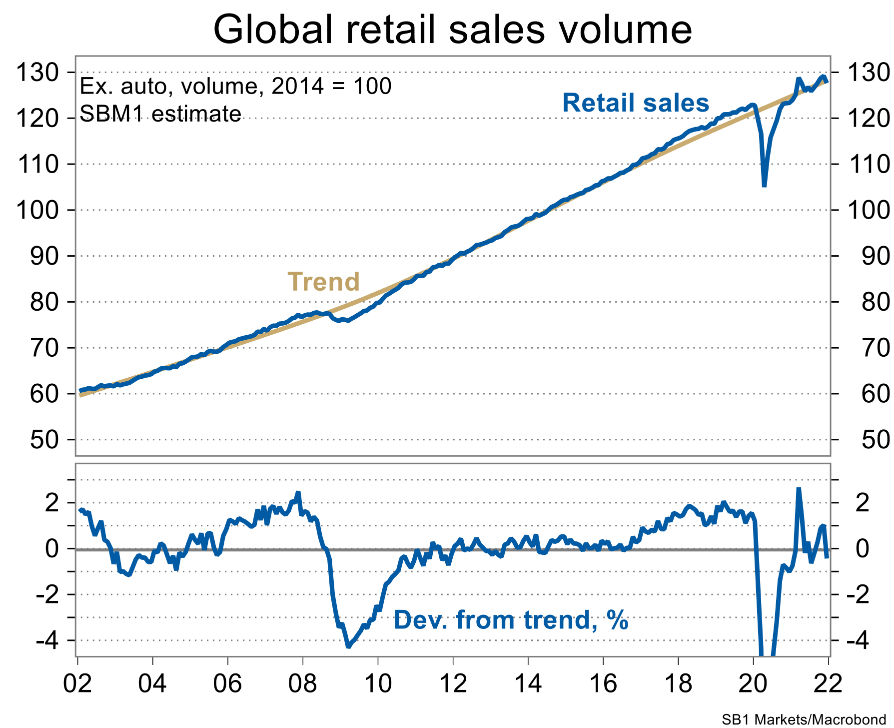




Global retail sales fell (at least) 1.2% in Dec, rich countries down 3%

Covid & high energy prices to blame? Manufacturing production kept up well

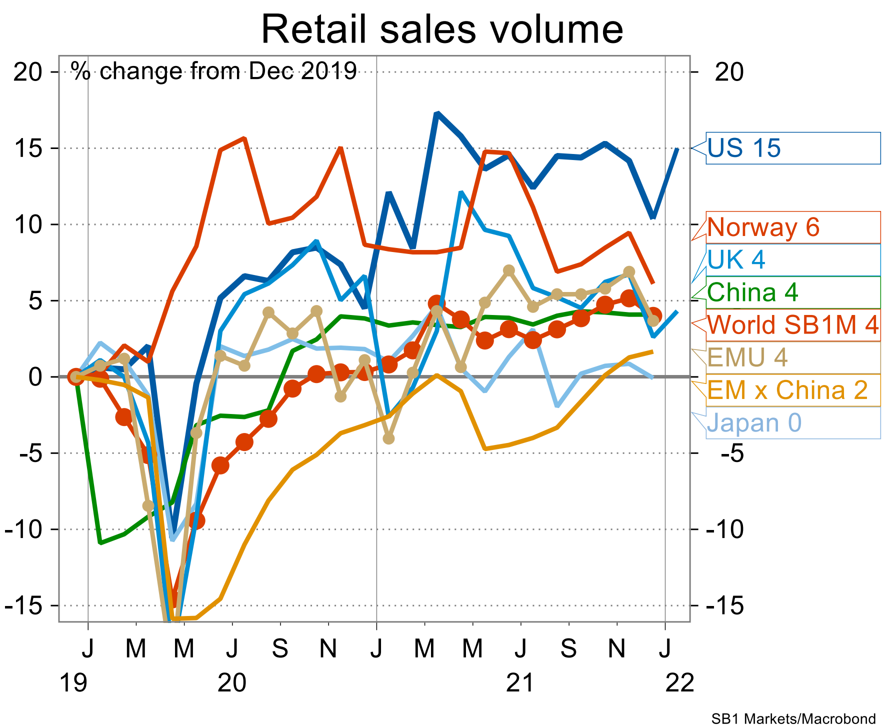


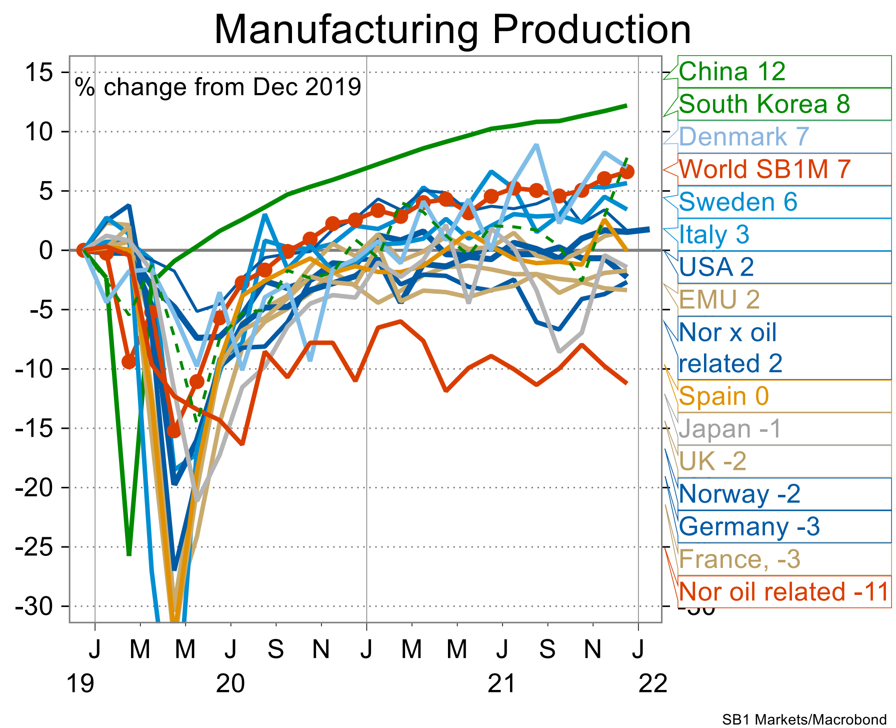


- **Global retail sales** very likely fell sharply in December, as sales fell some 3% in the rich part of the world – and unusually broadly. Omicron may explain some of the weakness, so may energy prices. However, the level has been too high as well, and one day sales will come back to earth. The global estimate is still uncertain as too few emerging markets have reported yet
- **Global manufacturing production** has recovered since the summer, and growth was through Q4
- **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

Retail sales recovered in January, from a weak December?

Still, the trend is very likely down in the rich part of the world? Manufacturing prod. still OK

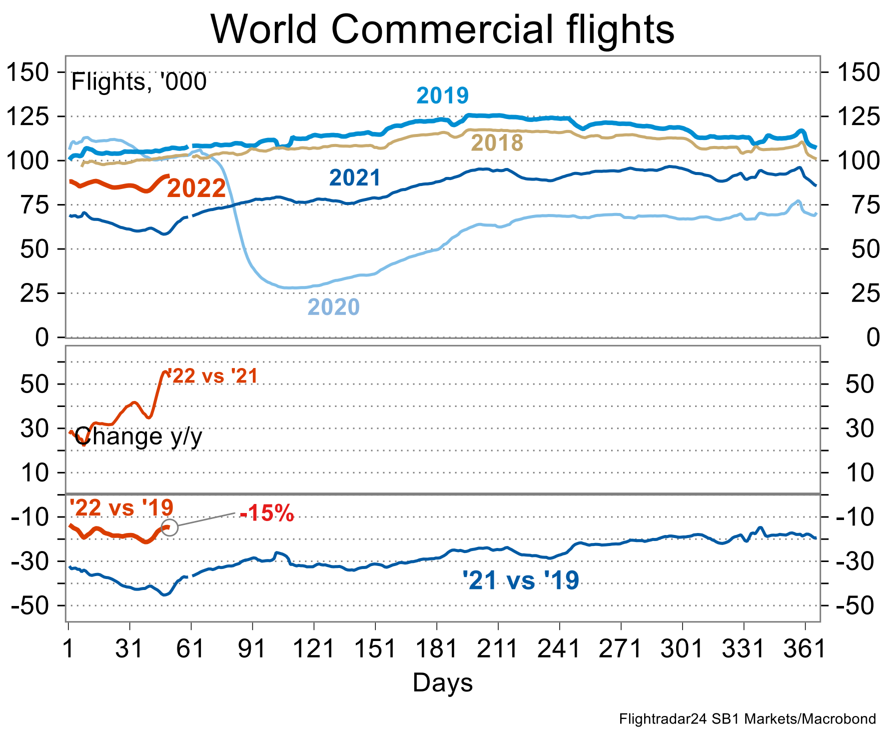


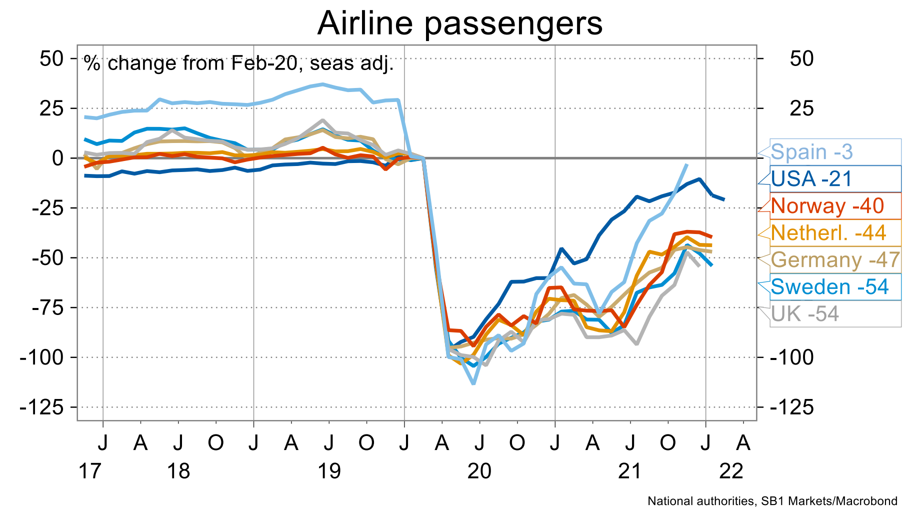


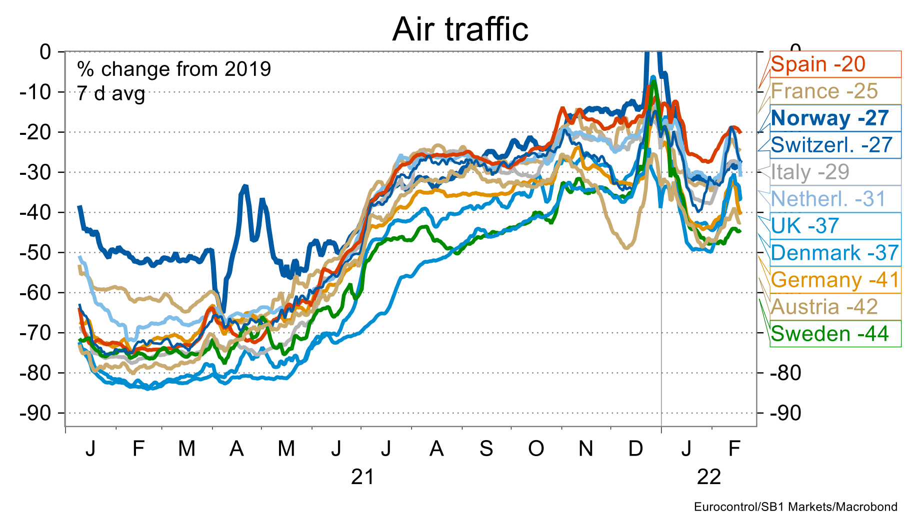
- **Retail sales** in Emerging Markets x China are recovering but is far below pre-pandemic trends. The Dec estimate is rather uncertain
- **Manufacturing production** has been hampered by a deep decline in auto production, but this sector is now recovering. The manufacturing PMIs are still strong, and delivery times very likely easing

Global airline traffic further up last week, now down ‘just’ 15% vs. 2019

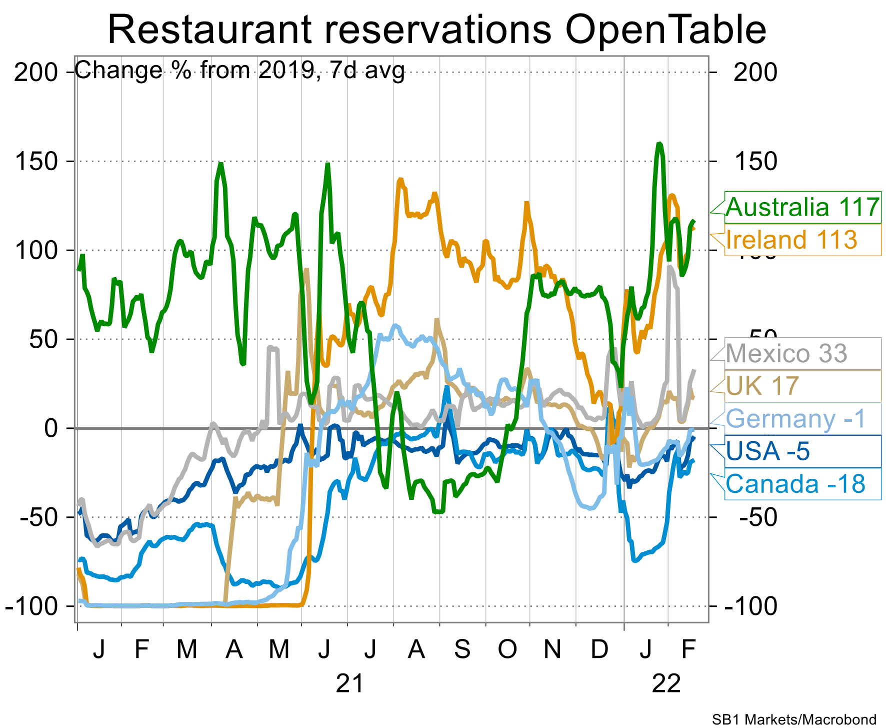
The fight against Omicron is won?

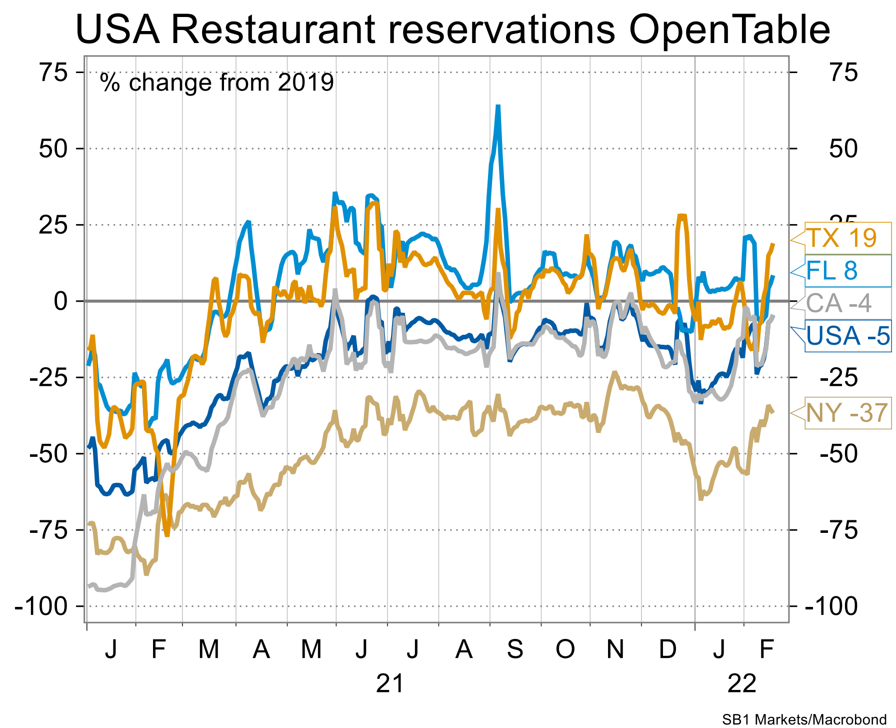






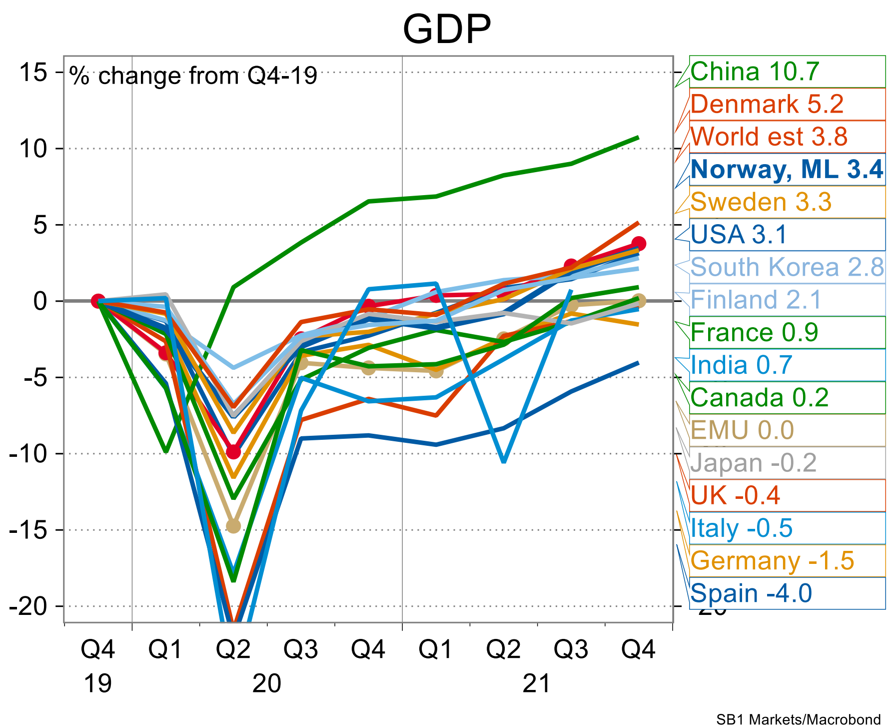
More restaurant guests most places?

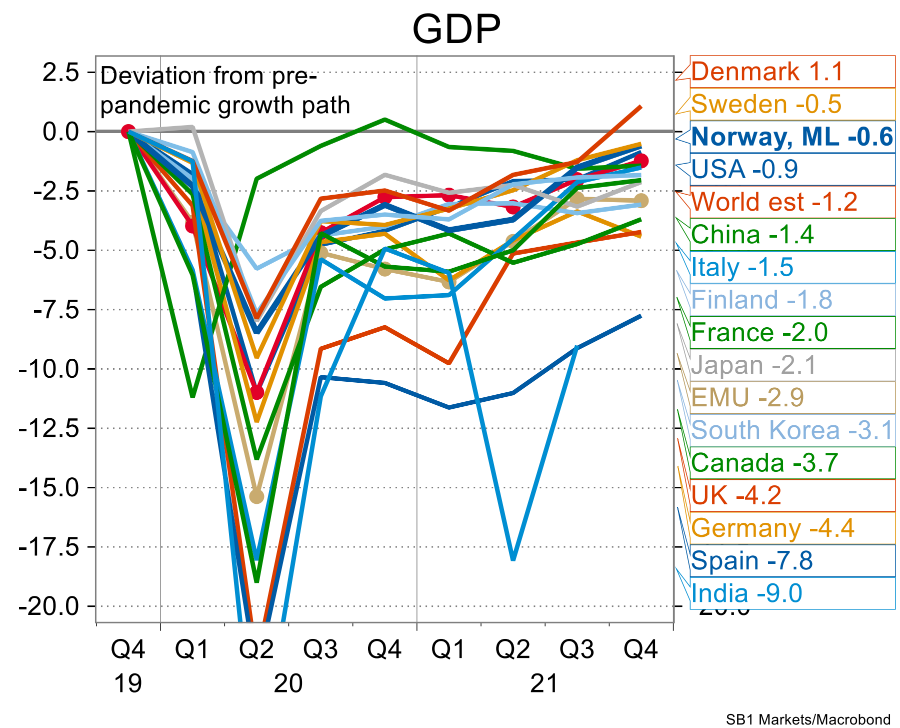




Strong growth in Q4 too, GDP is up 3.8% vs the pre-pandemic level

.. But still 1.2% below the p-p trend growth path



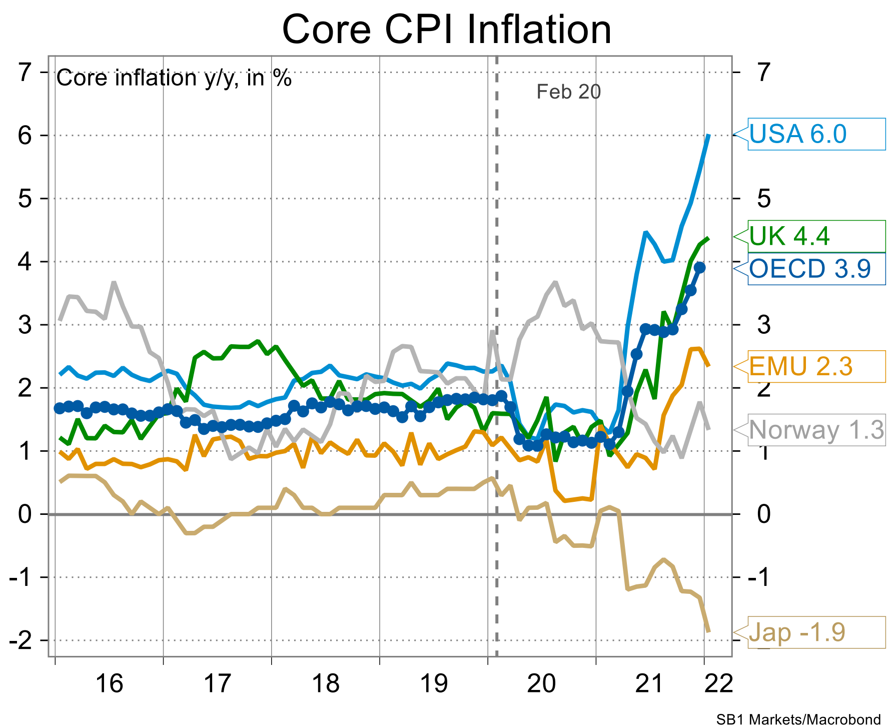


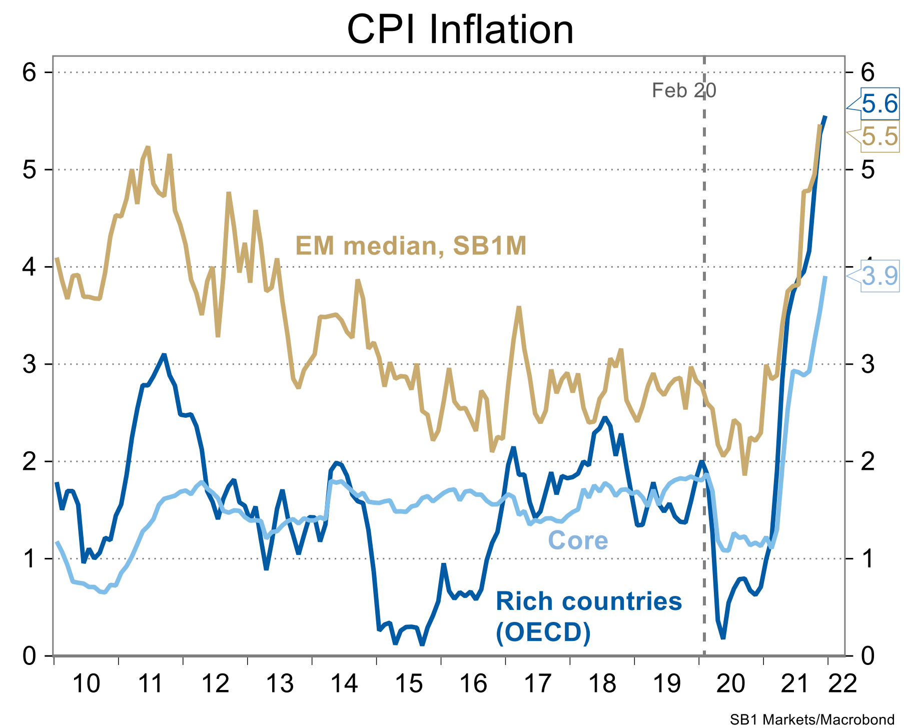
- Most countries have reported decent growth in Q4
- Some estimates are included at the charts above (but both Denmark and Finland are represented with their Q3 GDP data)

SpareBank 1 MARKETS

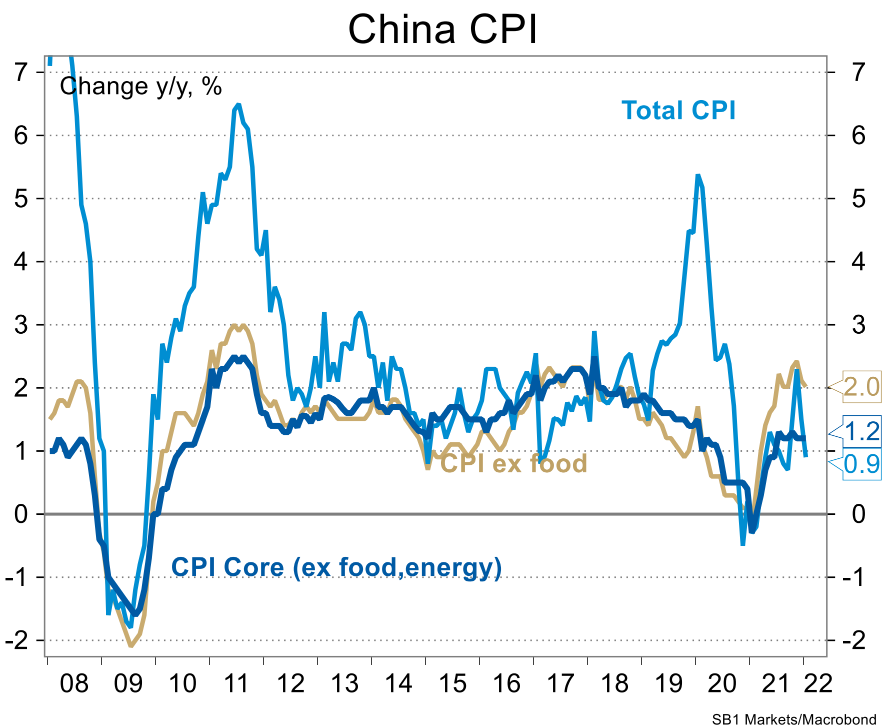
Inflation may be peaking ~~now~~ soon – at a high level

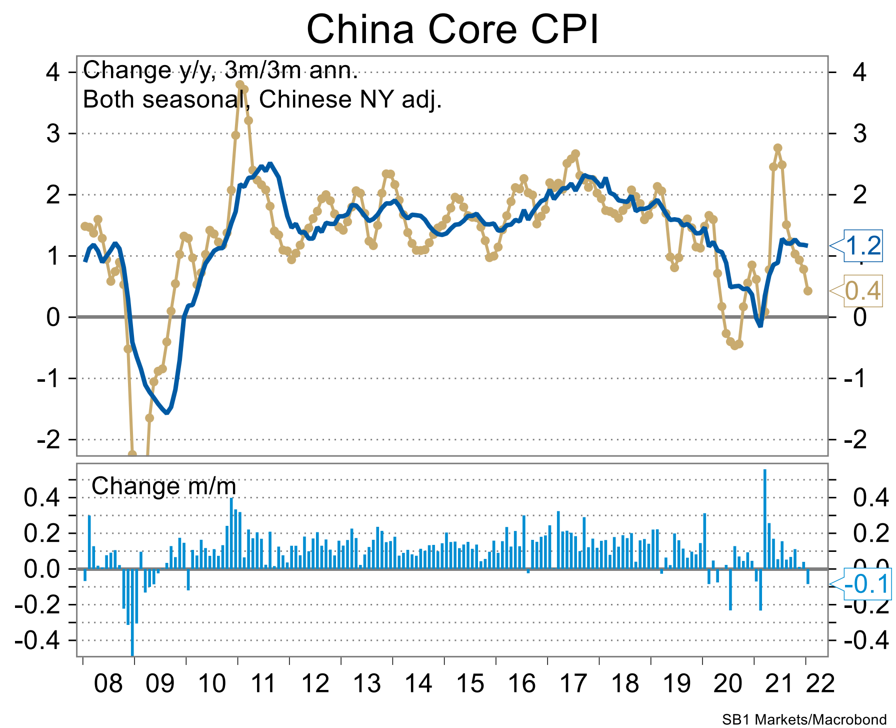
Energy prices the main culprit, but core inflation has turned up most places





No inflation in China, the headline up just 0.9% y/y, the core 1.2%

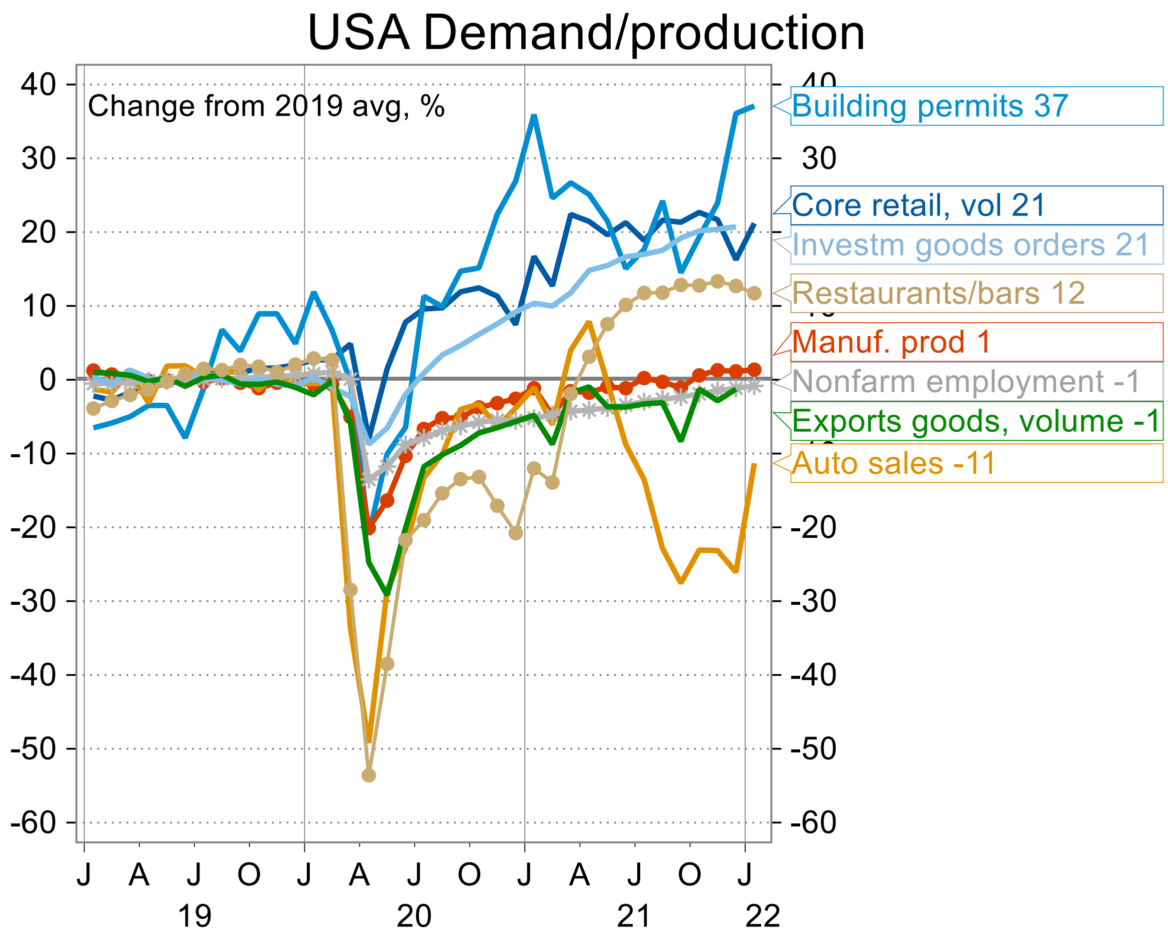




- **Total annual CPI** growth fell 0.6 pp to 0.9% in Jan – as prices fell 0.3% m/m. The annual rate was expected down to 1% - so no surprise
- **The core CPI (x energy, food)** was unch at 1.2% y/y. Prices fell 0.1% m/m. The 3m/3m rate fell to 0.4%
- **Food prices** rose marginally mm, and are still down 1.2% y/y, due to the normalisation of pork prices – even if vegetable prices rose sharply
- <u>Inflation is low</u>. **Monetary policy** will not respond to actual inflation data if inflation is not really high or low, <u>the real economy and the credit market is more important</u>

Big picture: Growth is slowing as the economy is ‘normalising’

The upside now: Auto production & exports

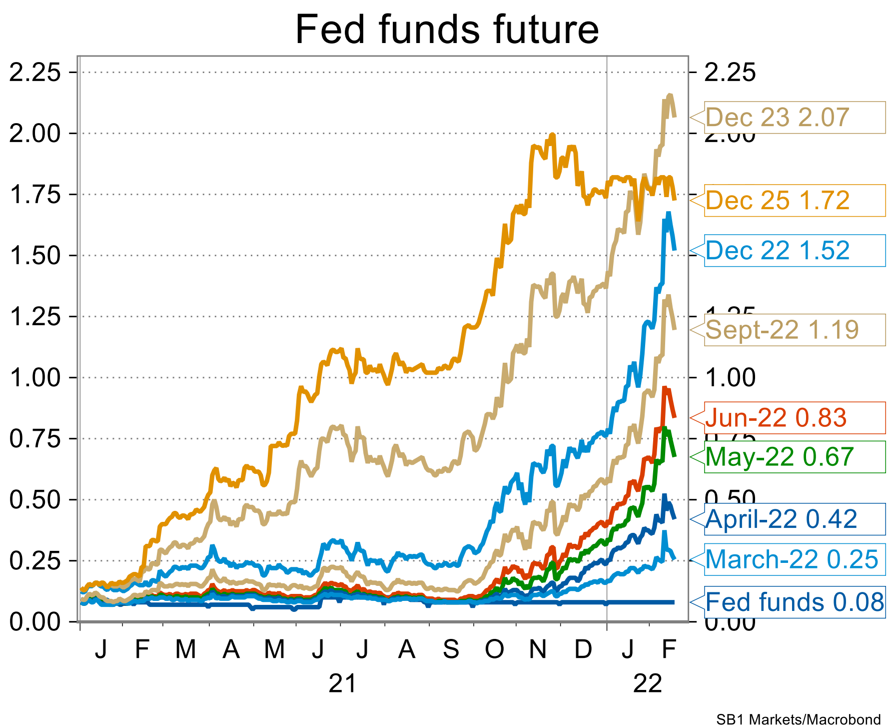


SB1 Markets/Macrobond

- Retail sales have peaked, but is still at a high level. Auto sales rose sharply in January
- Housing starts/building permits are are up recent months
- Manufacturing production is ‘too weak’ but supply constraints, exports have kept production in check
  - » Auto sales rose sharply in Februar, but the level is low, and the production way below normal level

FOMC minutes: not even more hawkish than expected (or James Bullard)

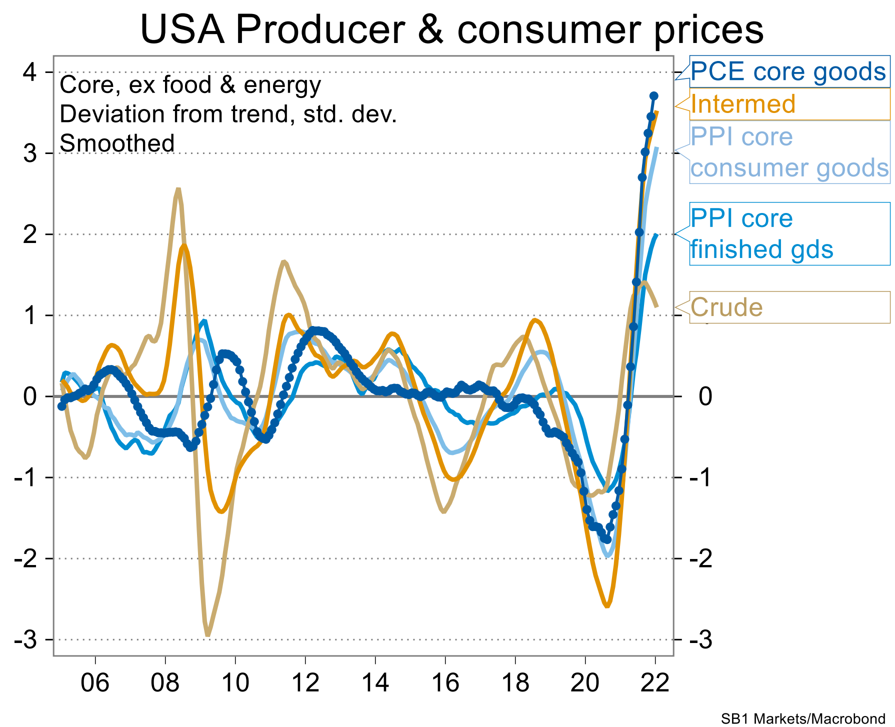
As we assumed the news was out, and discounted, and that minutes would not send rates up

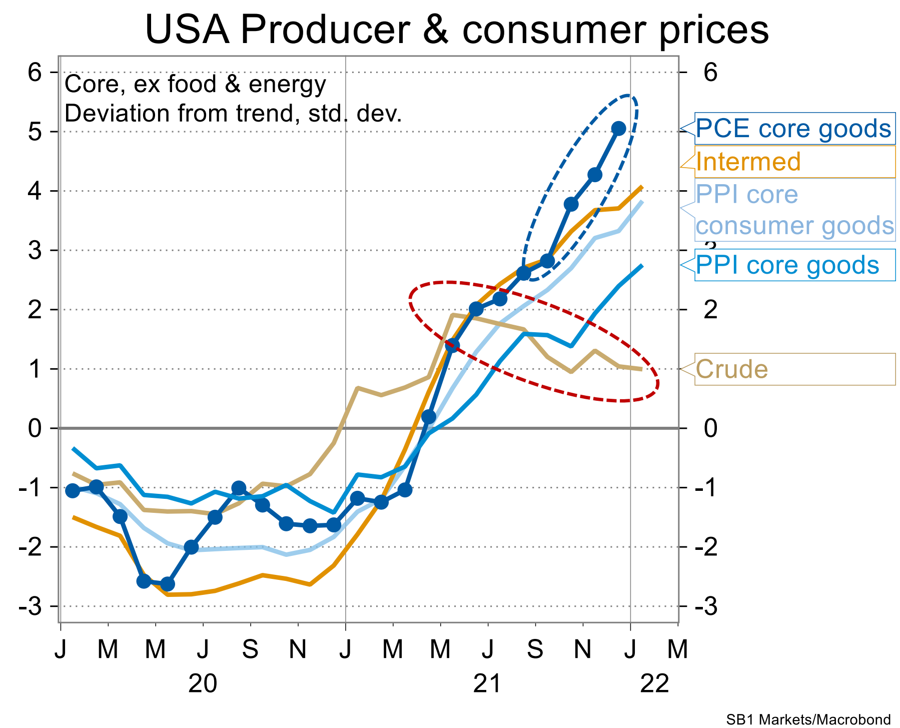


- **The two previous FOMC minutes** were significantly more hawkish than Powell's comments after these meetings. At the press conference after the late Jan meeting, Powell was much more hawkish than we have heard him before. After that, some FOMC members have dropped comments on the need for a more rapid monetary tightening, which together with a series of strong data have pulled rate expectations sharply up – the <u>Dec-22 Fed funds contract shot up 67 bps (!!!) since before the Jan 26 FOMC meeting</u>. We assumed that the minutes could not be even more aggressive than that – and they were not. They were just aggressive
  - » <u>Participants</u> agreed that uncertainty regarding the path of inflation was elevated and that risks to inflation were weighted to the upside (supply chains, geopolitical turmoil - energy prices, wage-price dynamic, unanchored inflation expectations)
  - » <u>Most participants</u> noted that, if inflation does not move down as they expect, it would be appropriate for the Committee to remove policy accommodation at a faster pace than they currently anticipate. <u>Some participants</u> commented on the risk that financial conditions might tighten unduly in response to a rapid removal of policy accommodation."
  - » <u>Thus, the majority is willing to take the risk of tightening too much</u>
- The FOMC also debated how to reduce the balance sheet, but no conclusion was drawn
- **Market reactions:** The Dec-22 contract fell 4 bps on Wednesday, and further on Thursday & Friday very likely due to war angst – stock prices fell too

Crude materials have peaked. But the pressure from supply chains is still strong

… However, core consumer prices have been rising earlier and more than normal vs. PPI prices

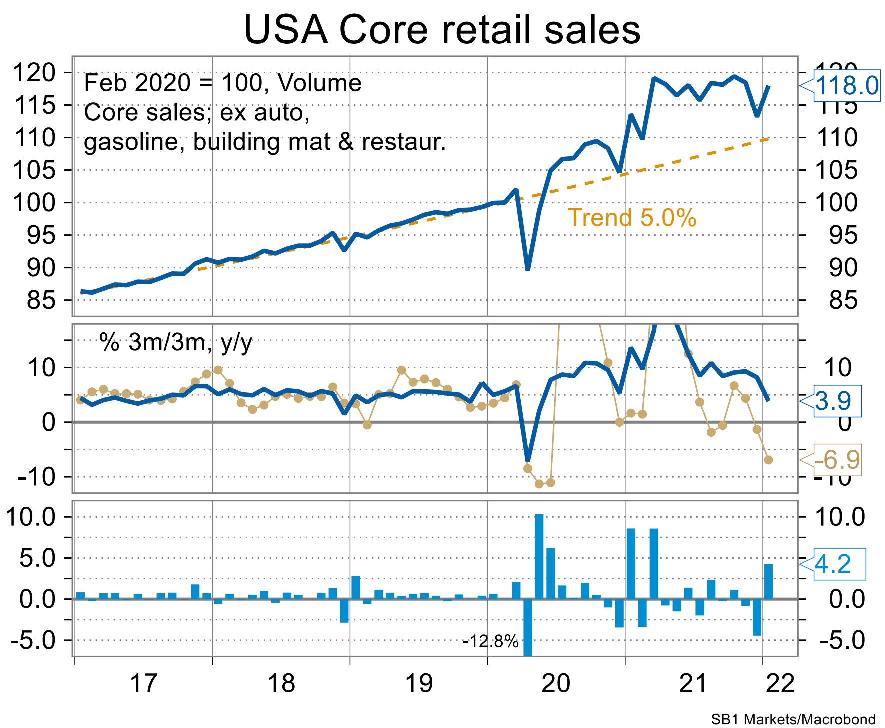


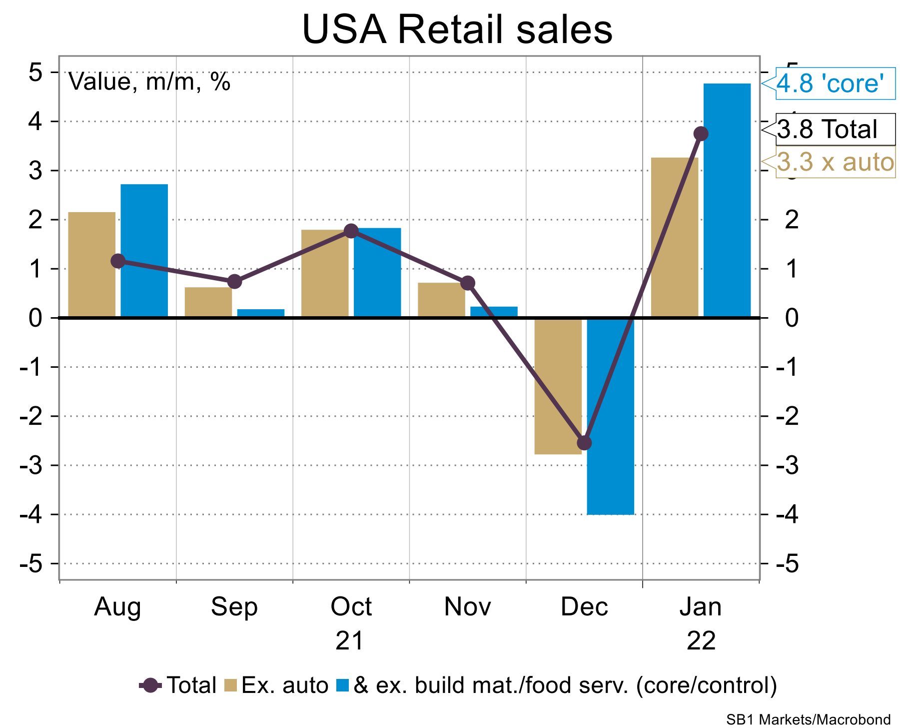


- **Crude goods prices** are leading intermediate goods prices by 4 months, and consumer prices by 12 months. Now, crude prices have clearly peaked (see the red ellipse on the chart to the right). However, **intermediate prices** have not yet yielded by much – and they will push finished goods prices further up the coming months
- Some more comfort: **Prices at the consumer level** (blue ellipse on the chart to the right) have responded earlier and more than normally vs the PPI core consumer goods index. That is very likely due to the unprecedented (and very likely not permanent) hike in 2^{nd} hand cars which are not a part of the PPI index. Thus the upside risk for the core goods component of the PCE may be limited the coming months

Retail sales recovered much better than expected in Jan, trend still just flat

… for core goods volumes, up 18% vs. Feb-20. Total sales are up 24% in nominal terms!

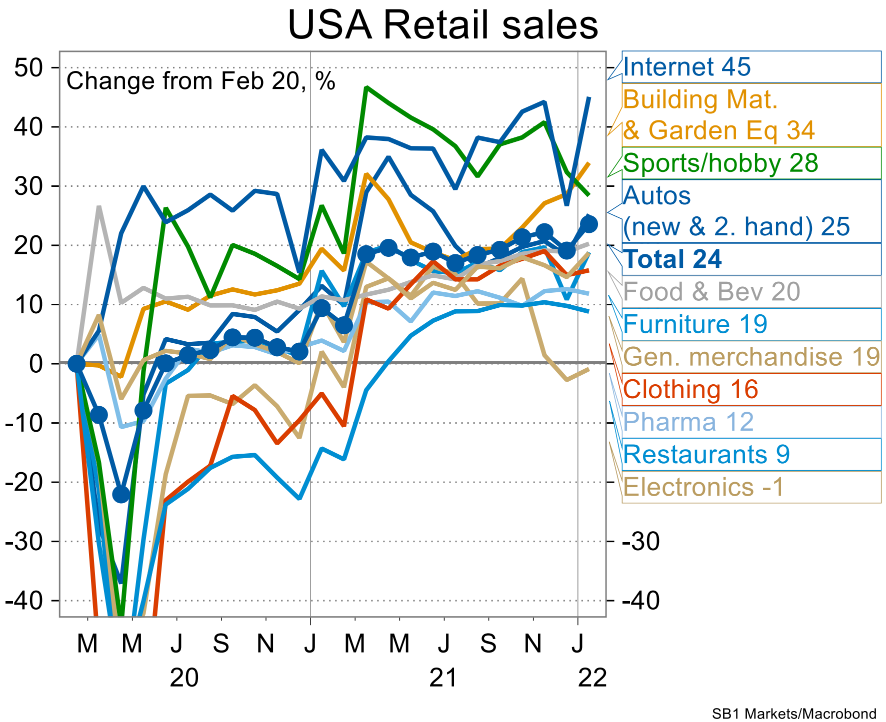


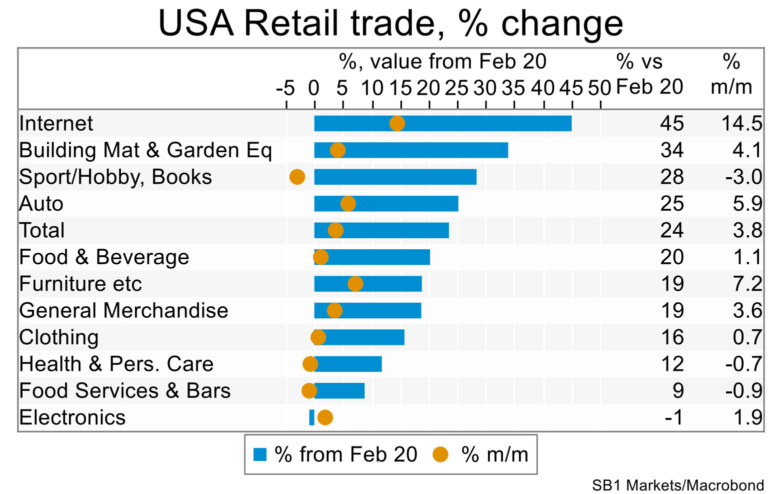


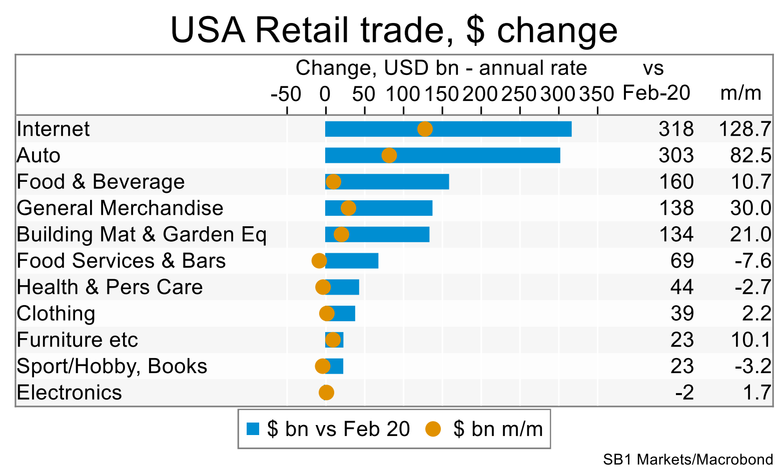
- **Total nominal sales** increased by 3.8% in January, following the 2.5% decline in December, revised from -1.9%, expected up just 1%. Thus, the level was far above expectations. Net sales rose sharply in Jan following the drop in Dec. Just 3 of 11 kind of stores reported a decline in sales in Jan
  - Total nominal sales are up 24% - twenty four per cent – vs. the Feb 2020 level!
- **Core sales of goods** (=control group, excludes autos, gasoline, building materials & restaurants) rose 4.8% in Jan, expected up 1%. Dec was revised down to -4.0 from -3.0%. We estimate a 4.3% monthly gain in January, measured in volume terms. Sale volumes are up 19% vs. the Feb-20 level, and 7% above a strong pre-pandemic 5% trend growth path
- **Consumption of goods** is very likely well above a sustainable level, and we still expect sales to decline the coming months/quarters – even if parts of the adjustment (vs. a long term growth path) already has taken place

Most sectors reported higher sales in January, following a weak December

Just sport/hobby (from a high level), restaurants (Omicron) and health down in January







Last month

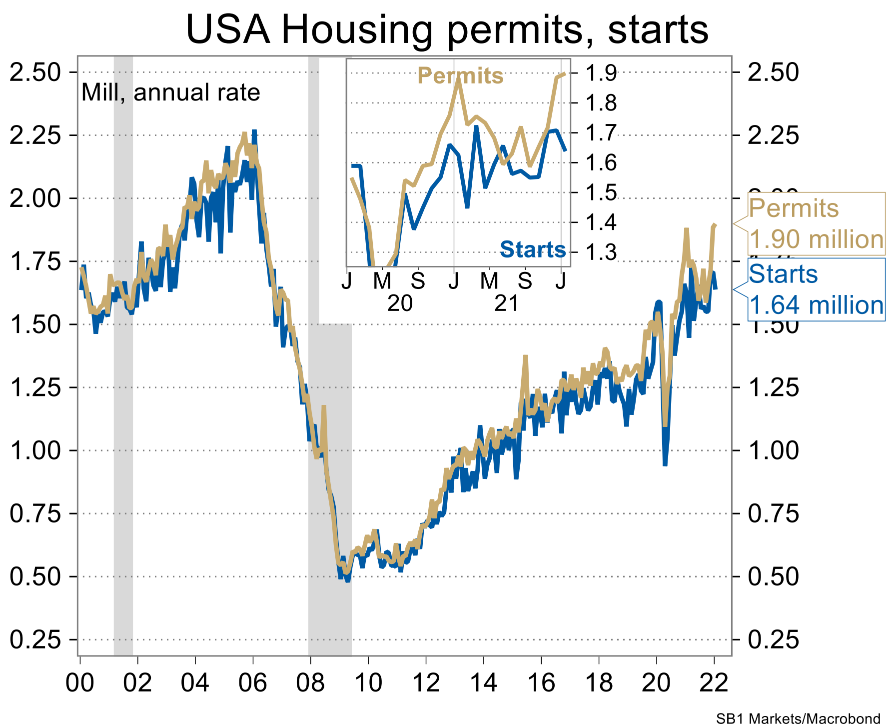
- 8 out of 11 main sectors reported higher sales in Jan, just 3 lower sales
- Net sales rose 14%, following a large decline in Dec

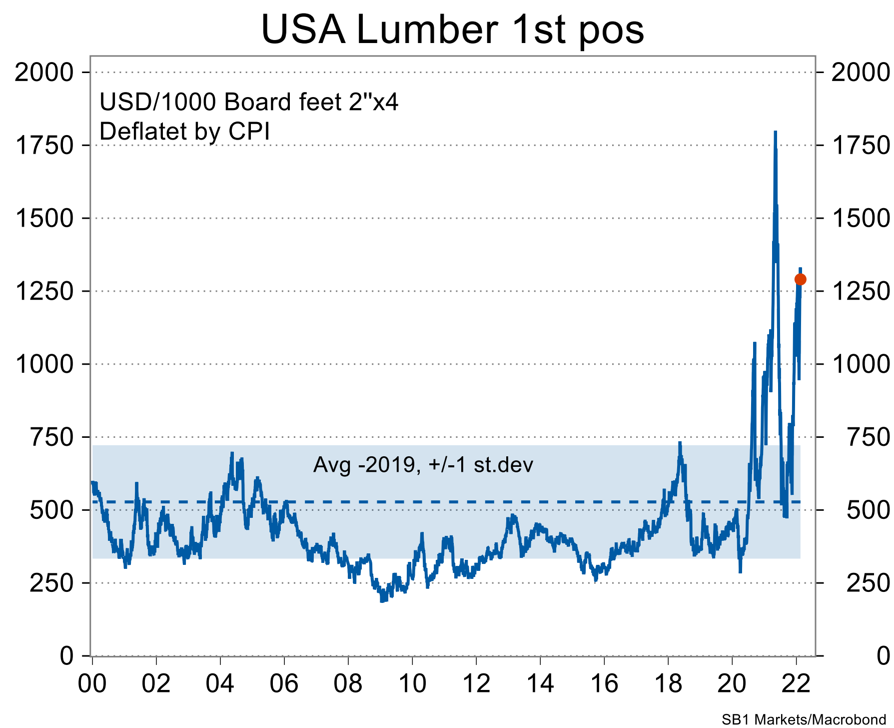
Since pre corona: Electronics down, all others are up

- **Net** sales are up 45%!

Housing starts down (weather/Omicron) but permits further up, best since 2006

... and the latter data point is the important one!

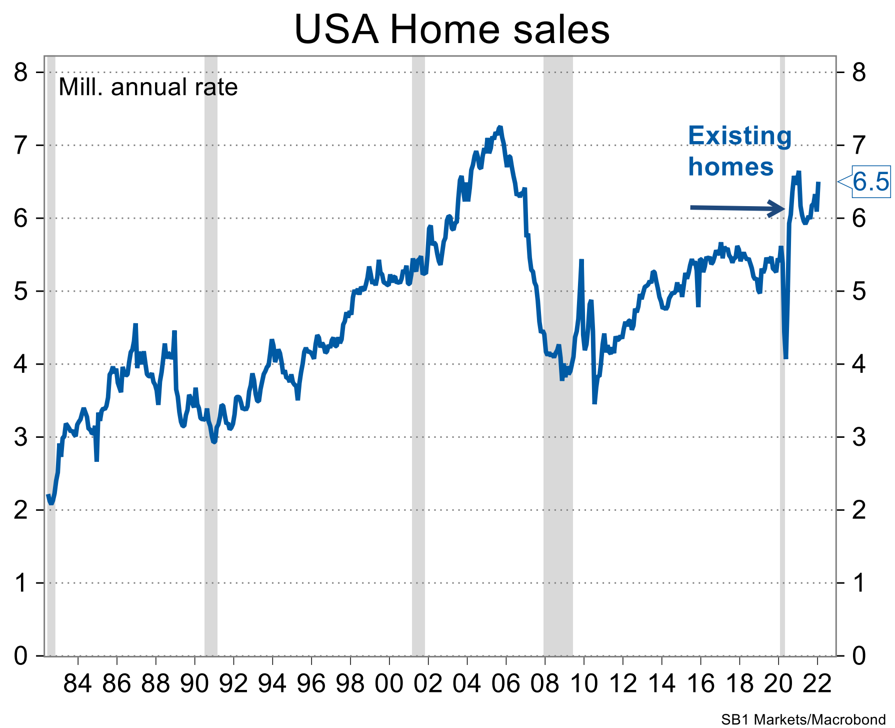


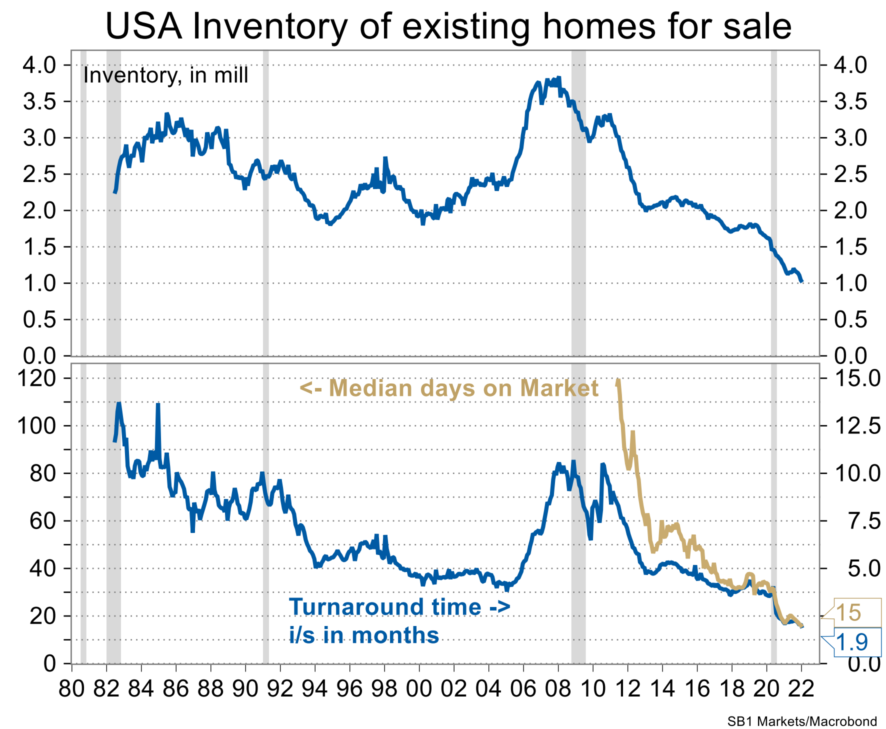


- **Housing starts** fell to 1.60 mill in Jan, from 1.71 mill in Dec, expected close to unch. Starts have been more or less flat through 2021 but the 3 past months are clearly up vs. the 2021 average
- **Building permits** rose to 1.90 mill, up from 1.89 in Dec, expected 7% down to 1.75. The Jan print is the highest since 2006!
- **Given the strong end of the year, the trend is still slightly up.** The level is some 10 – 15% above the pre-pandemic level. However, given the incredible strong existing home market, and soaring prices, starts should normally have strengthened further, amid still moderate mortgage rates and a recovering economy
- **Supply & capacity problems and higher cost** in the building sector may explain the lack of response. Lumber (2’’x4) prices are still unusually elevated, at 2.5 x the average price

Existing home sales sharply up in January, the inventory at ATL

Prices inflation has slowed but remains at 15.7% y/y

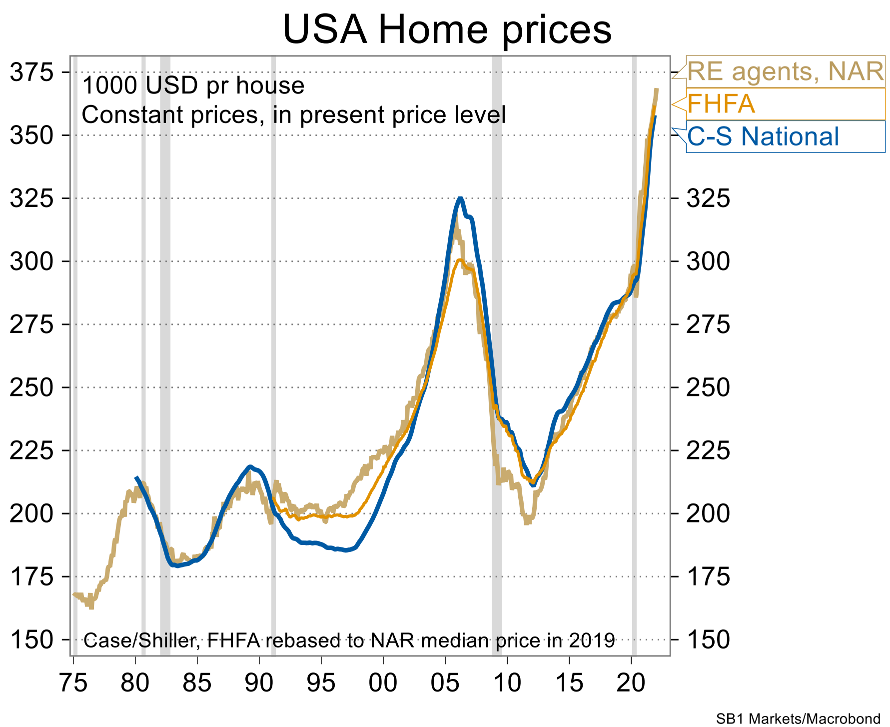


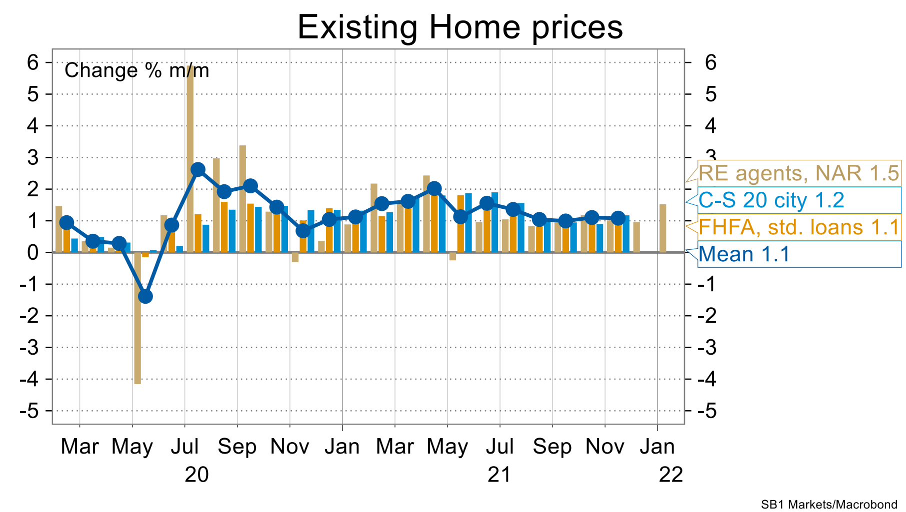


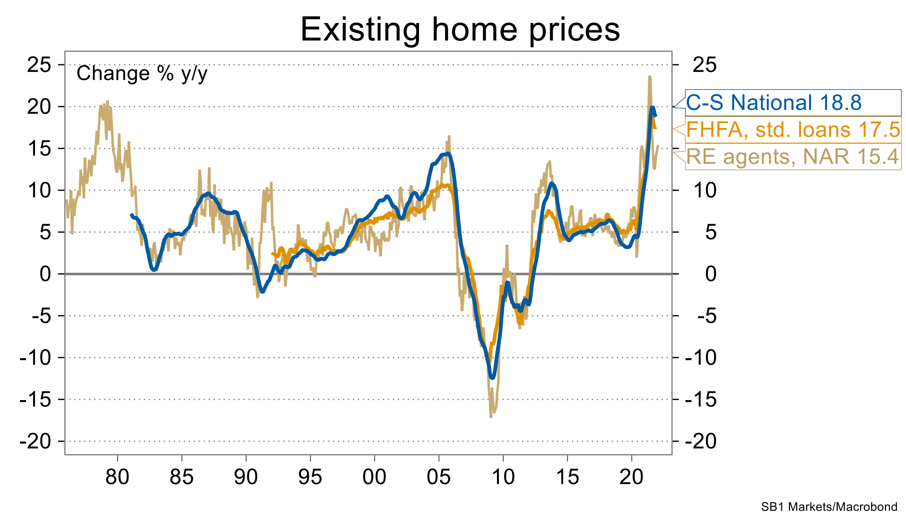
- Sales of **existing homes** climbed to 6.50 mill (ann. rate) in Jan, from 6.09'', expected 6.10'' (down from prev. reported 6.18''). Sales are down just 2% from the local peak in late 2020, and are 20% above the pre-pandemic level – and not that far below the ATH level at 7.26 mill in Sept 2005
- **The inventory of unsold homes** fell further in Jan, to another ATL.
  - The inventory equals 1.9 months of sales. During the 2005 boom, the i/s ratio was 4 months, in bad times it has been as high as 10 months
  - The median time on the market for those homes sold is just 15 days, down from 30 days before the pandemic (and 120 days in 2011!)
  - No doubt, the lack of supply keeps the number of transactions down
- **Prices** rose 1.2% m/m in Dec, up from 1.0% in Nov. The annual rate accelerated almost 1.7 pp to 15.7%. At the peak, prices were up 23% y/y

Existing home prices up 1.5% m/m in Jan, the fastest pace since last April

Peak inflation may still be behind us, after a 30% lift since before the pandemci



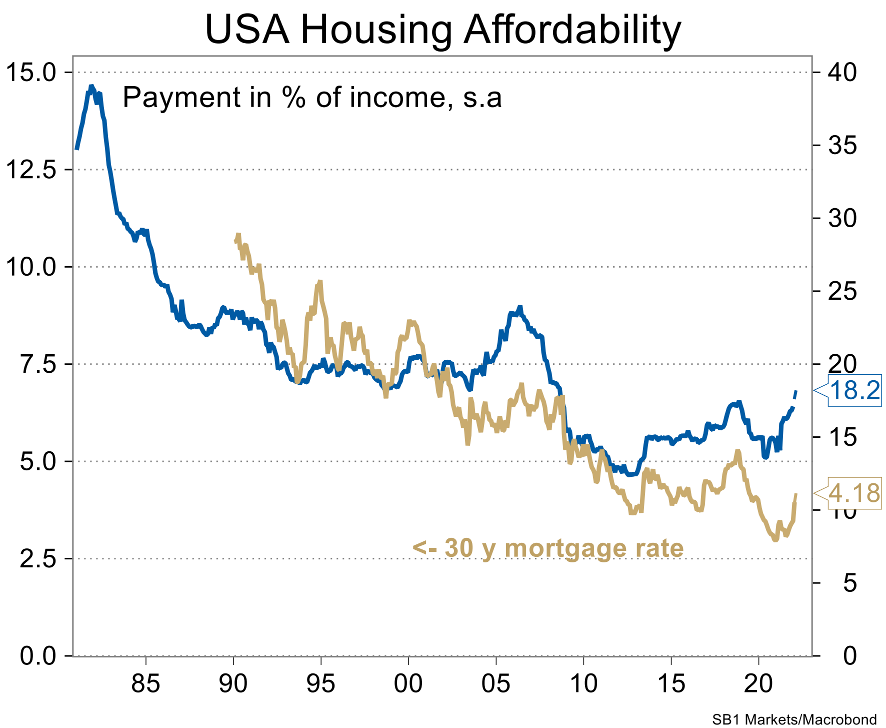


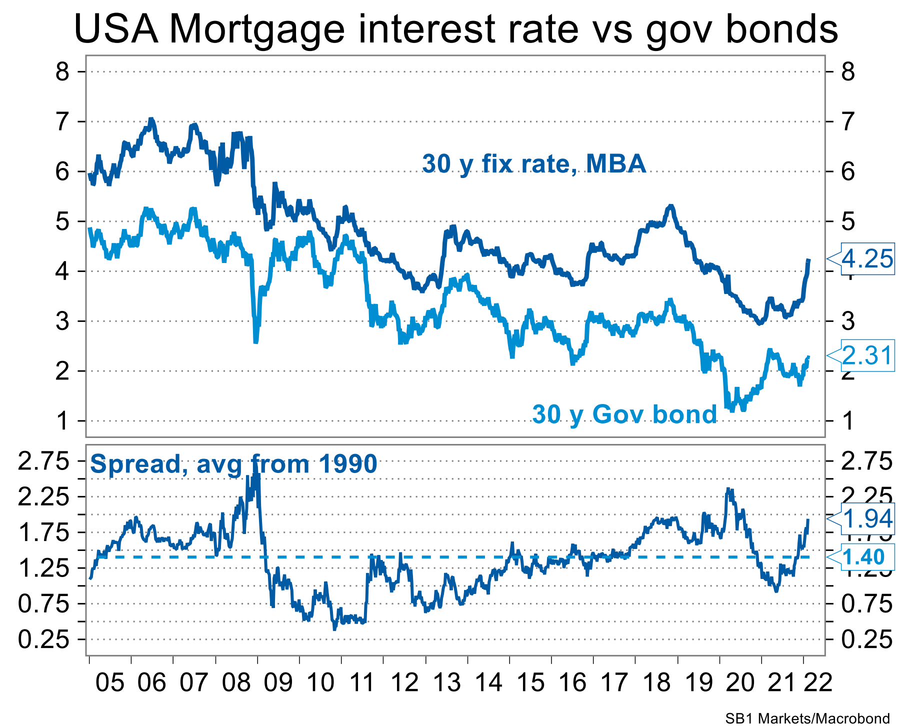


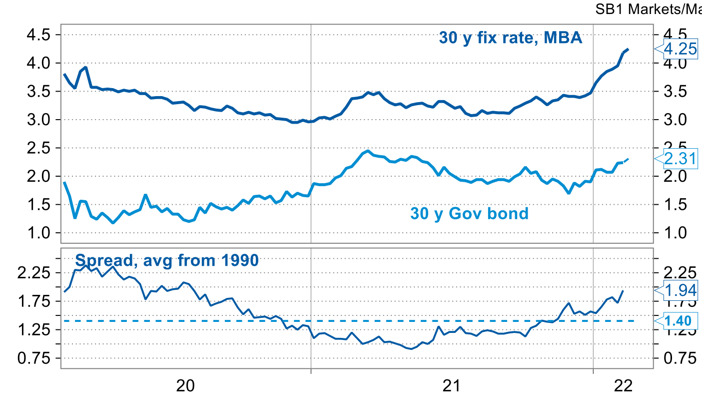
- **Prices** rose 1.5% m/m in Jan, according to the realtors – up from downward revised 1.0% in Dec. The annual rate rose to 15.4% from 14.7% (revised down 0.7 pp)
- **Other price indices** confirm a red hot housing market; prices are rising extremely fast – even if the peak rate of housing inflation is very likely behind us. Prices are up 30% vs. the pre-pandemic level – and the real price level is far above the 2005/6 peak

Prices are up 30% since before the pandemic, the mortgage rate is higher

So the affordability is not where it used to be. That is, it is still lower than anytime before 2008







- **The 30 y fixed mortgage rate** has climbed to 4.25% from 3.0% last summer
  - » **The** rate has increased MUCH more than the 30 y Gov bond rate. The spread has widened to 194 bps from 91 at the bottom last spring (and by more than 30 bps last month) and it is now above the 140 bps average
- The **Federal Reserve** is now rapidly tapering off its buying of mortgage backed bonds – and signals eagerness to reduce its holdings, which very likely explains the steep increase in the spread
  - » The central bank has funded most of the housing marked during the pandemic, at least until mortgage lending shot up through 2021

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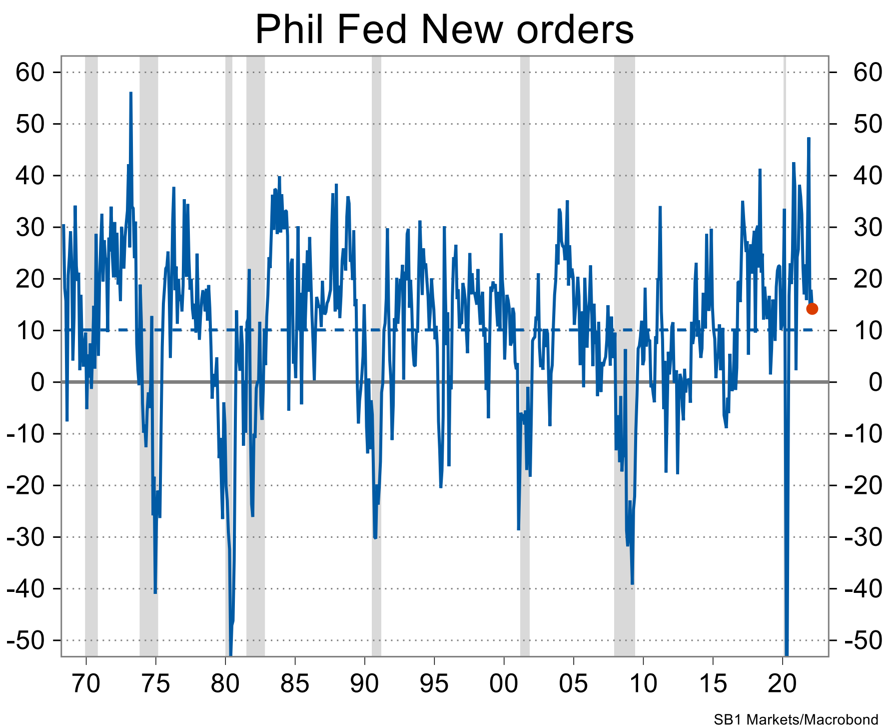
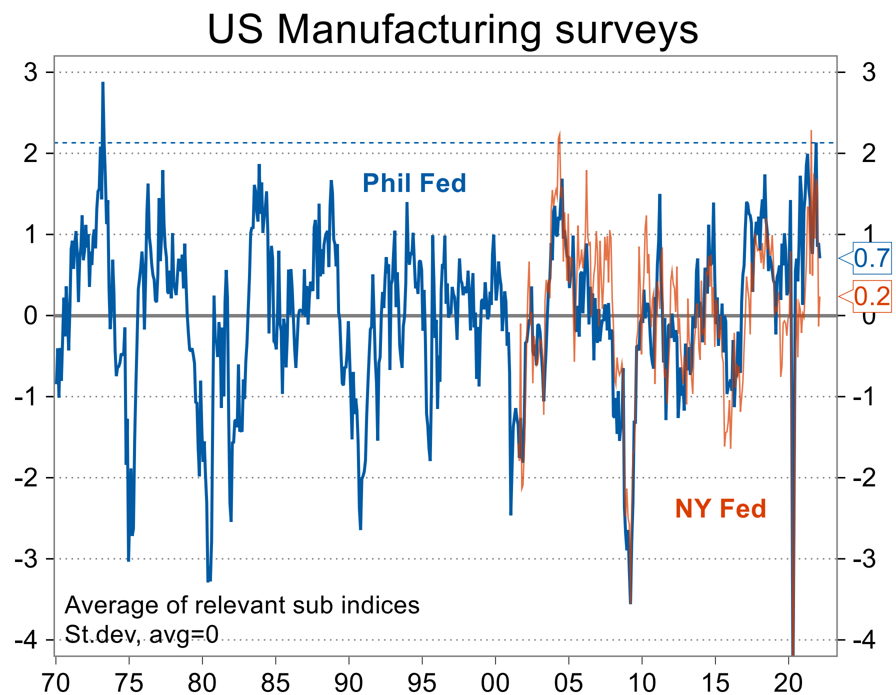
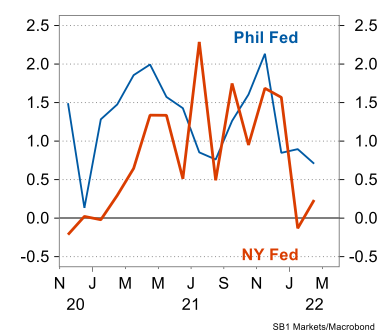
Both Philadelphia & NY Fed's manufacturing signal slower growth

Still, both are still reporting growth above average







- Phil Fed: 16 in Feb, down drom 23.2 in Jan, expected 20.0
- NY Fed: +3 in Feb, from -0.7 in Jan, expected up to 12
- No reason stated for the rather unusual decline in the NY Empire Manufacturing Survey January. However, optimism remained elevated

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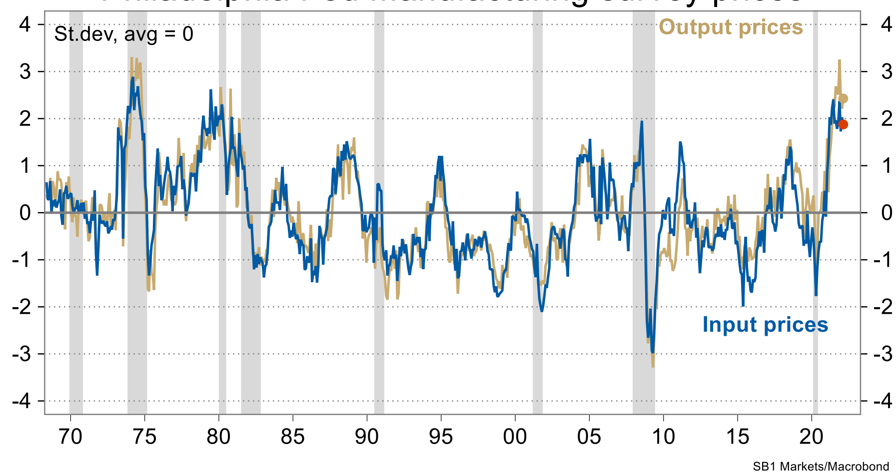
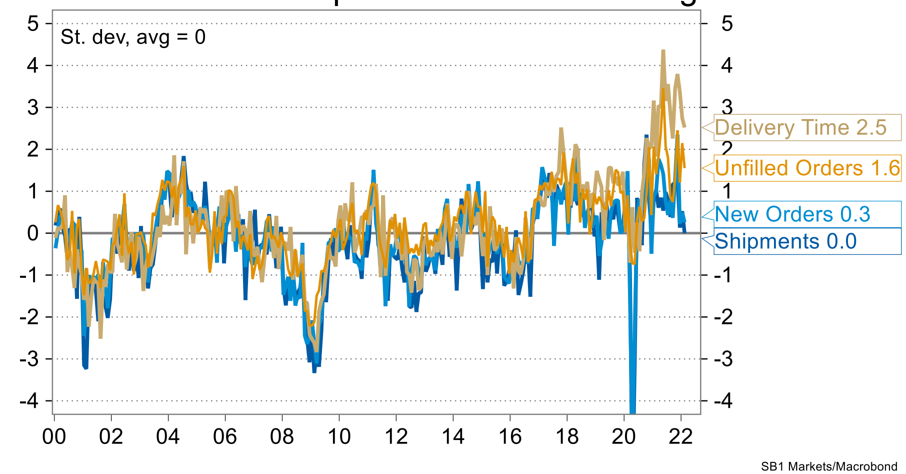
Phil Fed: Price pressures are very elevated – and are expected to remain so

… even if growth is expected to slow, and delivery times to ‘collapse’

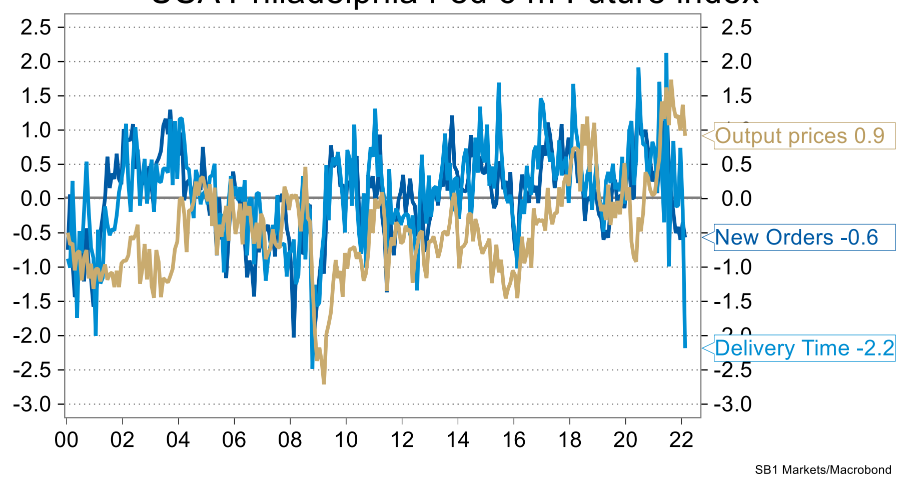
Philadelphia Fed Manufacturing survey prices



USA Philadelphia Fed Manufacturing index



USA Philadelphia Fed 6 m Future index



- The current prices increases are still very high, both input and output prices
- Order growth is slowing, so are actual shipments – but long delivery times (and lack of labour) may keep production in check, not demand – even if the new order component is weak too, the order reserve is still growing rapidly
- The outlook: Supply chains problems are expected to ease substantially but also the order inflow. Even so, output prices are expected to increase rapidly. A bit strange mix? Stagflation??

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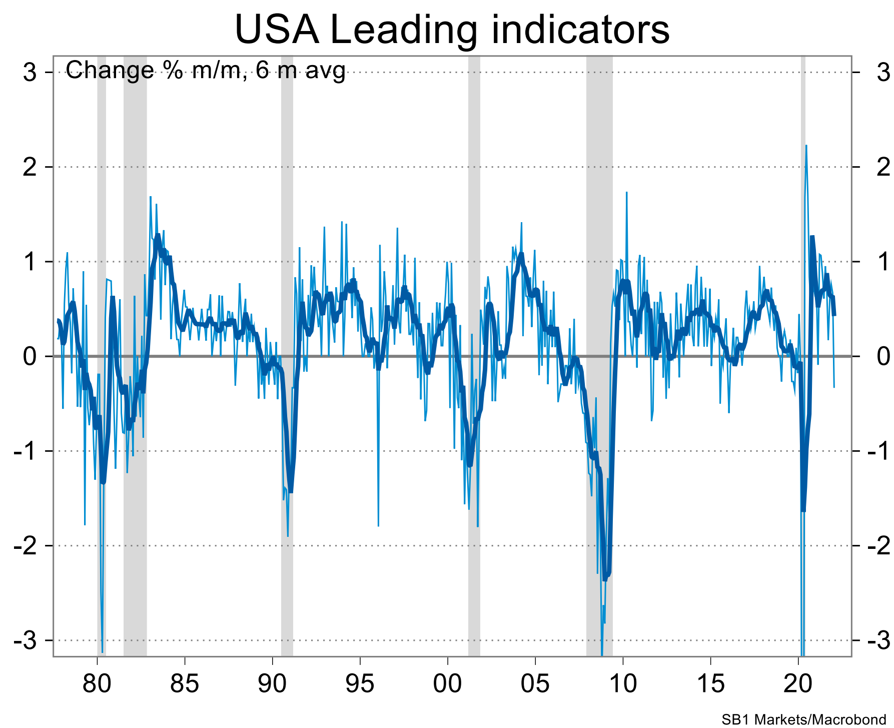
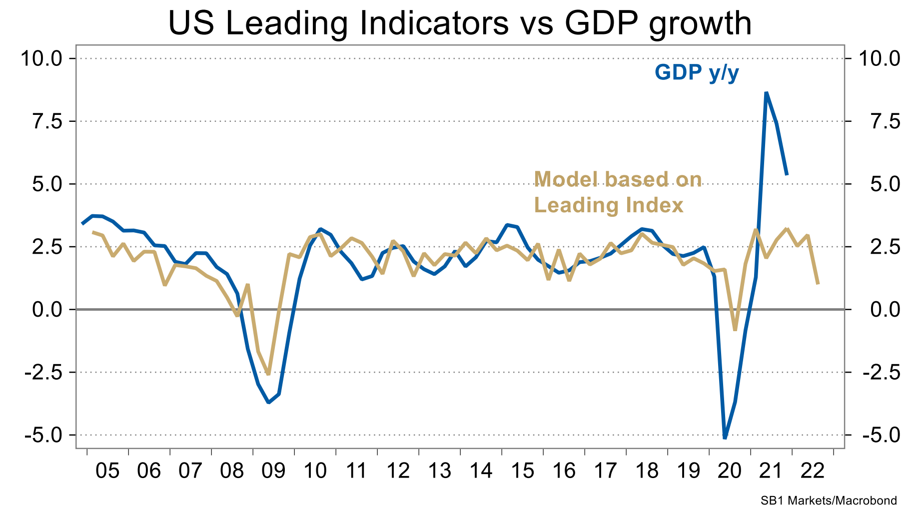
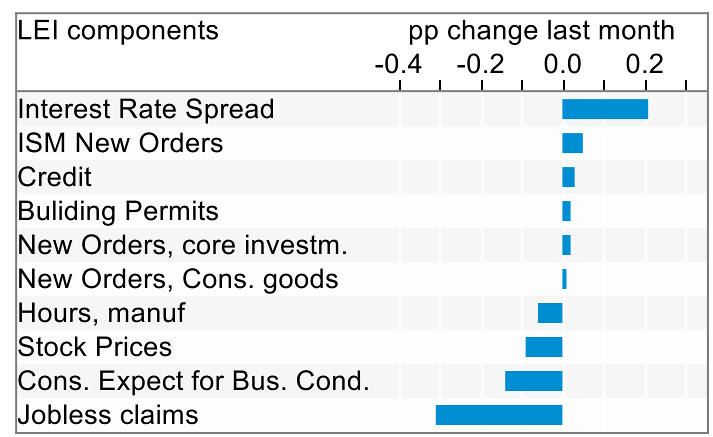
Leading indicators (Conference Board's LEI) in red in January

More jobless claims, weaker consumer confidence (vs businesses), and lower stock prices

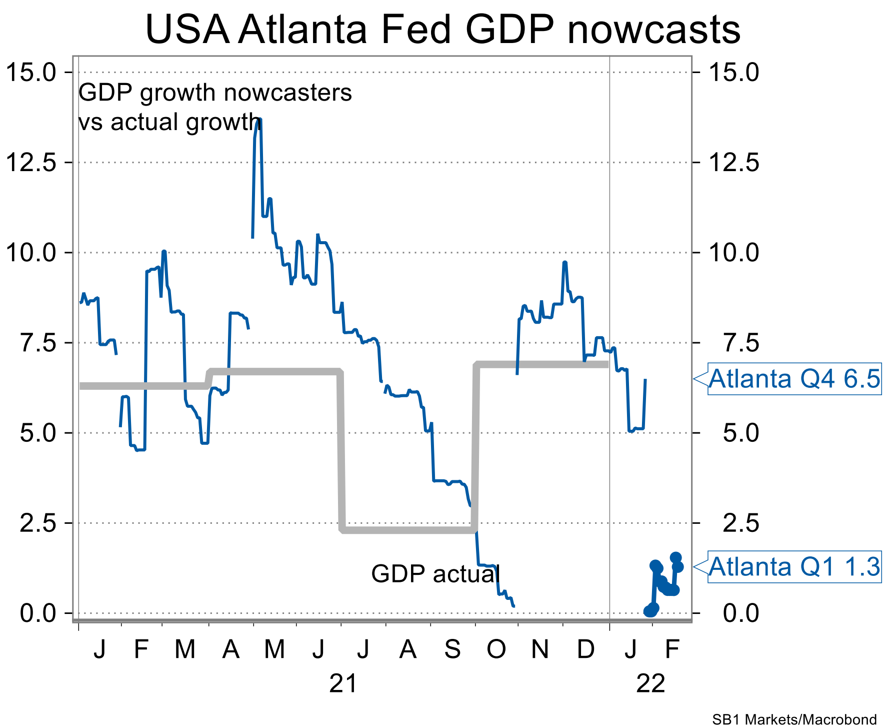


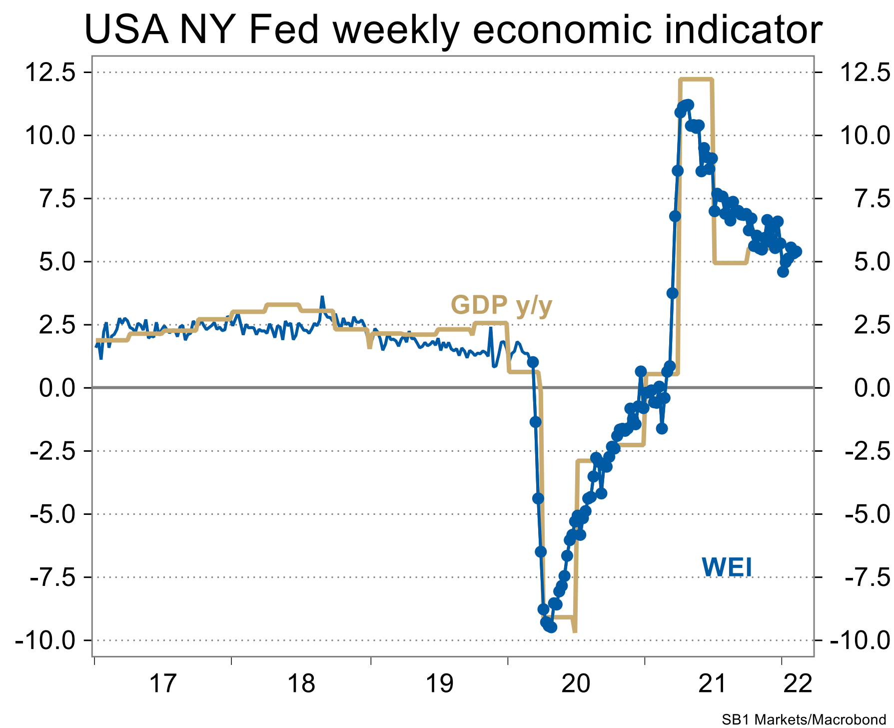


- The index fell 0.3% m/m in Jan, expected up 0.2%, even if all components already are published
- One negative print does not make an recession (the LEI has turned negative ahead of all recessions)



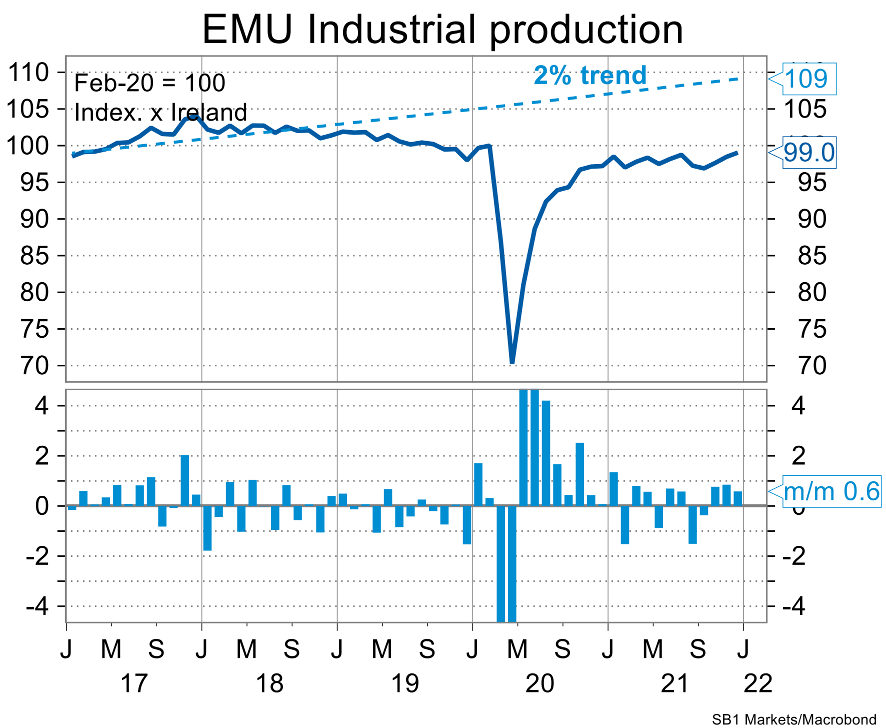
Atlanta Fed's nowcaster suggests 1% growth in Q1

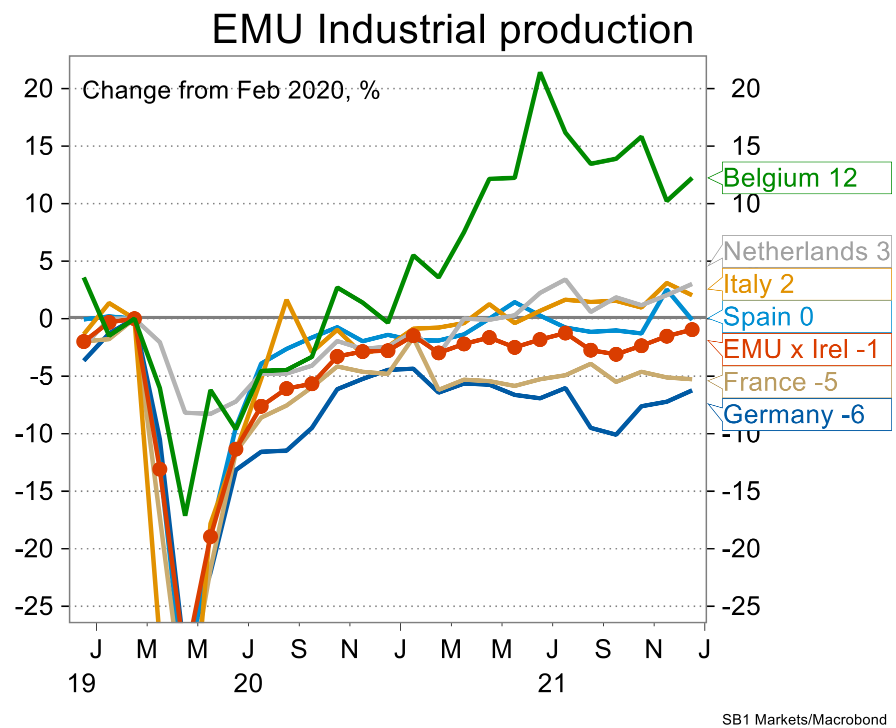




Industrial production up 0.6% in December, above expectations

Production 1% below the pre-pandemic level but the trend through 2021 was not that impressive





- **Officially,** production rose by 1.2% due to another hike in Irish production – which very likely will be reversed, as usual. The 'core' rose 0.6%
- **Germany** is still the laggard in EMU, due to the disastrous cut in auto production. Italy is in the lead among the big 4, 2% above the Feb-20 level
- However, **auto production** is finally recovering – and production rose by 7% m/m in December
- **Production in the EMU** has trended flat so far in 2021, even if surveys and new orders have signaled more than decent growth. The sharp setback in auto production explains much of the overall 'weakness'

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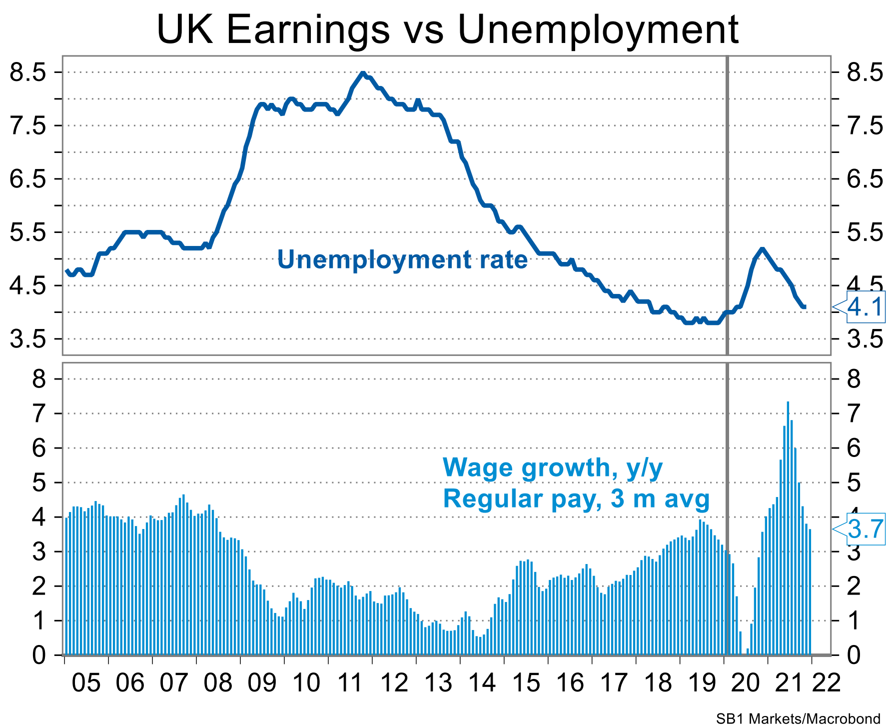
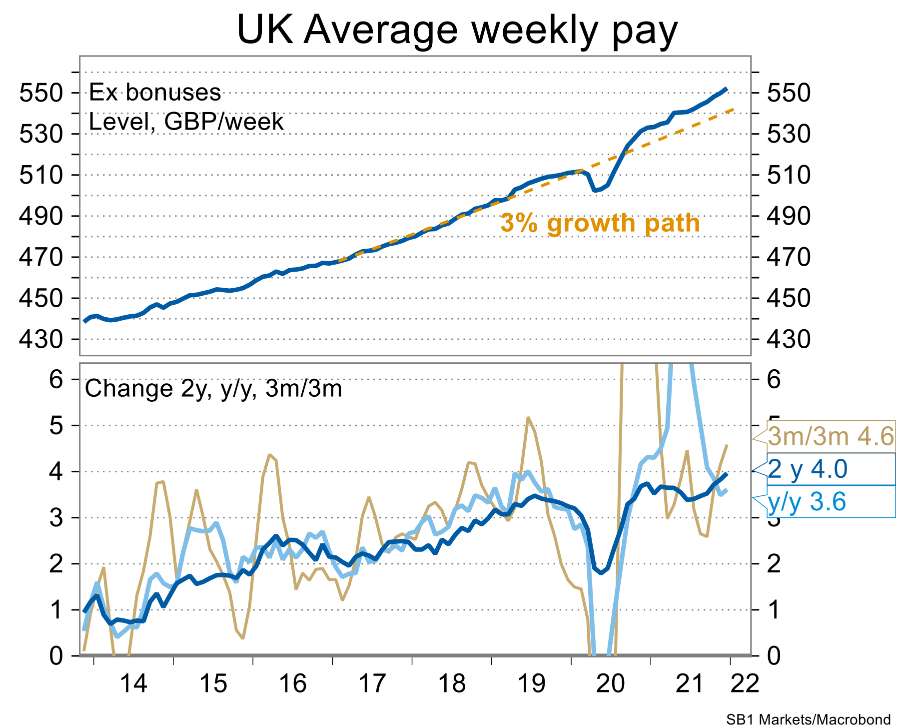
Unemployment is trending down - to just marginally above the pre-p level

Wage inflation is accelerating (even if annual growth rates are slowing)





- The **'LFS/ILO' unemployment rate was unuch at** 4.1% in December – but the trend is still down. The rate is just 0.1 pp higher than before the pandemic
- **Annual wage growth** (regular pay) decreased to 3.7% in Dec from 3.8% in Nov, expected down to 3.6 (the 3 m avg fell to 3.7% from 3.8%. Including bonuses, wages are up 4.3%, up from 3.8%
  - » Over the 2 past years, regular weekly pay is up 4.0% in average. Over the past 6 months (3m/3m) wages are up 4.6%, and both are accelerating
  - » When the pandemic hit, wage inflation was slightly above 3% – which was substantial higher than over the years before: at 1 – 2½ %

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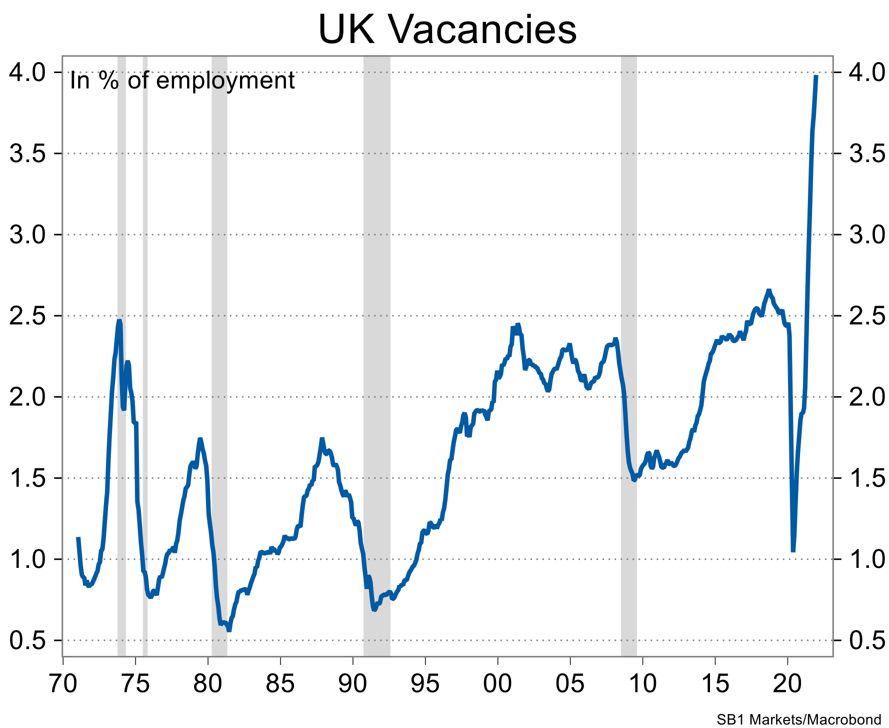
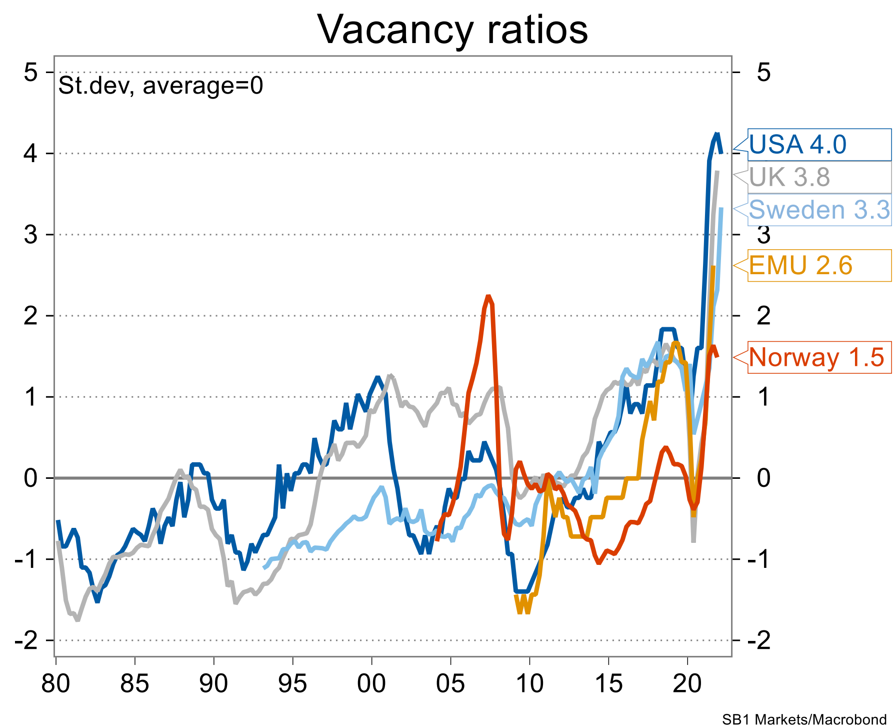
Vacancies shot further up in Q4, is approaching US levels!





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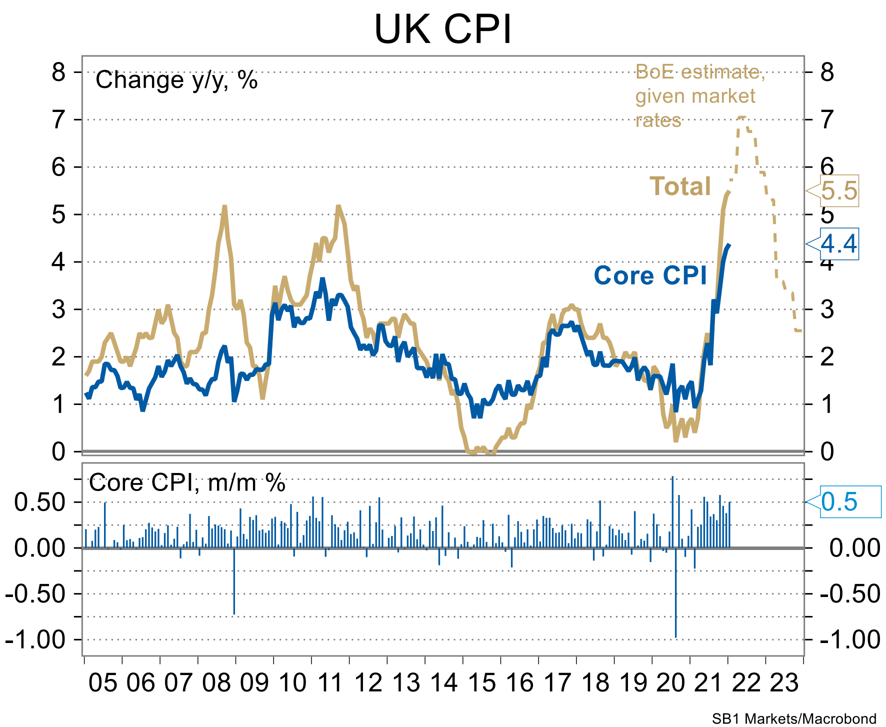
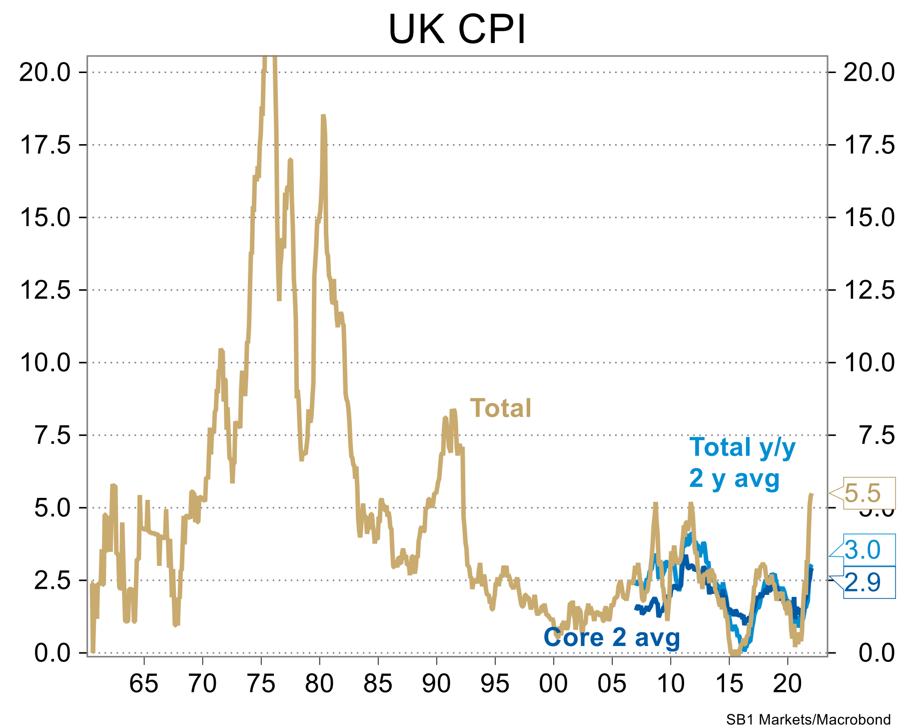
Inflation up to 5.5%, the core to 4.5%, slightly higher than expected

The core up 0.5% m/m, as is the 'new normal' these days

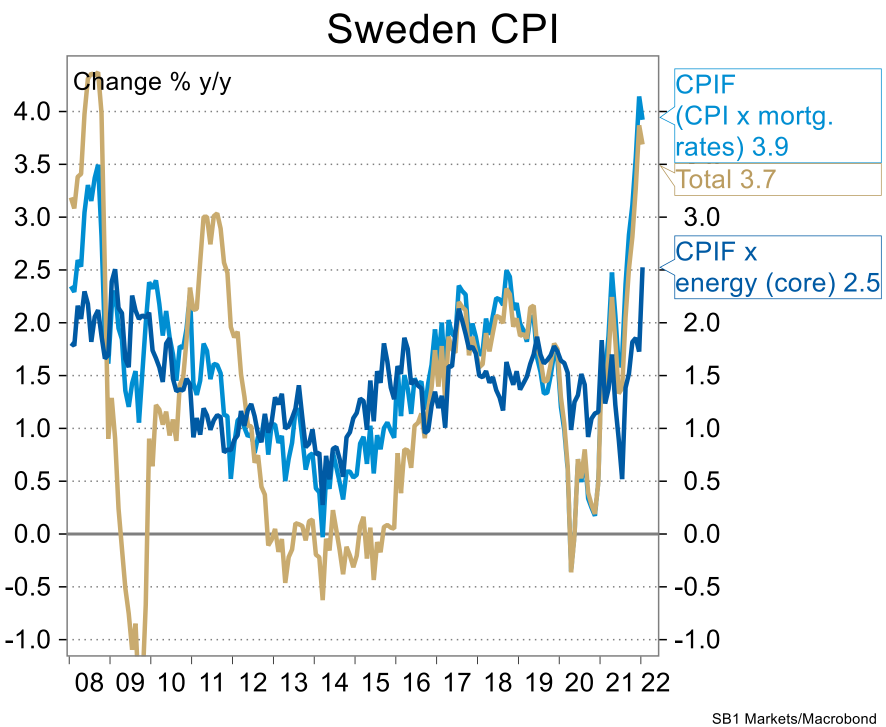


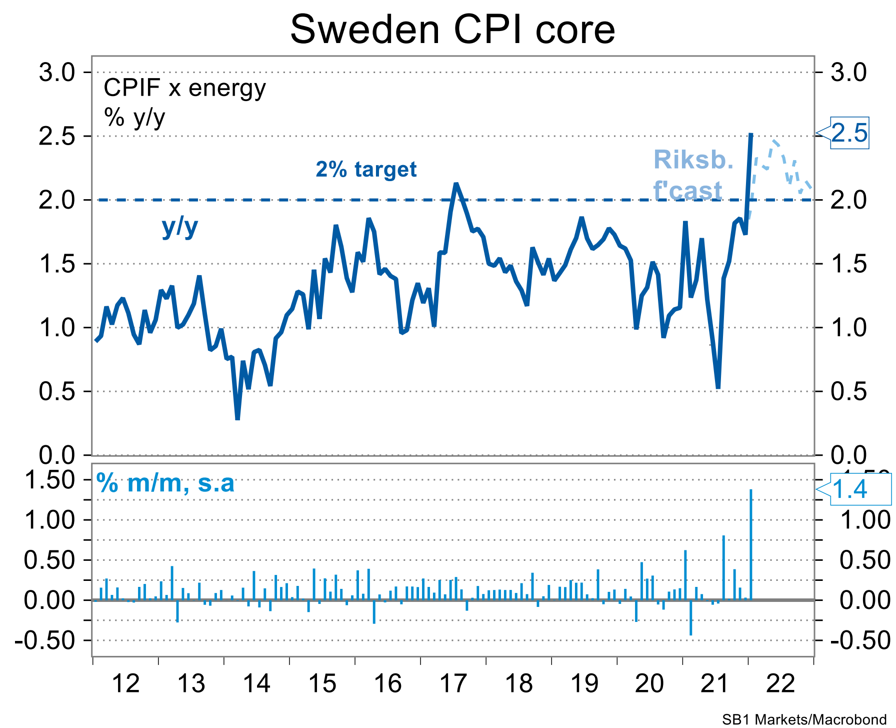


- **The total CPI** rose 0.4% m/m. The annual rates are the highest since the early 1990'ies. Measured over the past 3m/3m the core index is up more than 5%
- **Measured over 2 years**, headline is up 3.0%, and the core is up 2.9%, which illustrates the base effects on the present much higher y/y rates. Still, inflation is well above BoE's 2% target, anyway how we calculate it!
- **Transport** has lifted CPI by 1.6 pp. 2nd hand cars are sharply up, as are fuel prices
- **Housing, included energy**, has lifted the CPI by 1 pp. Still, there are many other contributors left…

Core inflation up 0.8 pp to 2.5%, 0.6 pp higher than expected

Headline inflation still down, as electricity prices fell sharply, like in Norway

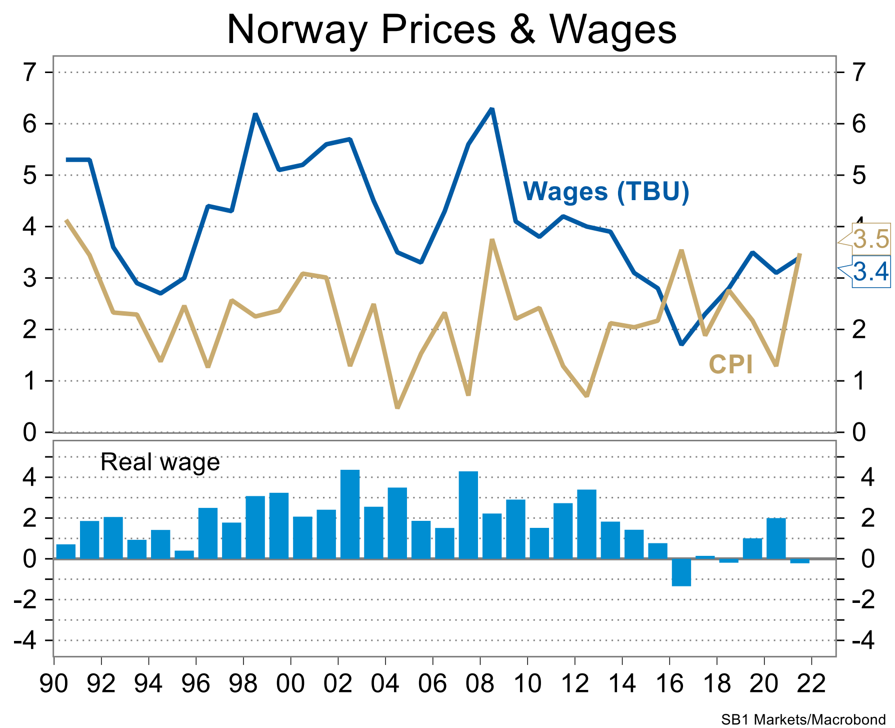




- **CPI-F x energy, the 'real core'** shot up by 1.4% m/m in January (seasonally adj), way above any forecast
  - » Prices actually rose 0.1% m/m, expected down 0.5%. The Riksbank expected a 0.5% decline too
  - » Prices rose by 0.7% (s.a) in Jan 2021, and thereafter retreated by 0.4% in February. If that trick is not repeated – and strengthened – this time around, the Riksbank will have to revise its inflation forecast sharply upwards. And if so, the Riksbank will have to revise its inflation forecast - and then to announce that the signal rate can be lifted before H2-2024. The market expect 1 hike in 2022, and 3 more in 2023 (rate expectations rose by 3 – 5 bps on Friday, following the CPI report
- **Headline inflation** slowed 0.2 pp to 3.7% y/y in Jan, expected down to 3.4%. Finally, electricity prices yielded

The TBU assumes 2.6% inflation in '22, lowering expectations of high wage increases

Wages rose 3.4% in the unionised part of the economy last year (3.5% overall). CPI was up 3.5%



- In the TBU, representatives from the Min. of finance and Min. of Labour, employers' associations' and trade unions together with SSB agree upon what has actually happened with wages last year, and they recognise a common price prognosis for the coming year (technically produced by SSB).

- The **Technical Committee** for clearing the ground for this spring's wage negotiations estimate last year's wage growth in the unionised part of the economy to 3.4%, as usual close to SSB's estimate of average wage growth for the overall economy, now estimated to 3.5%
  - » After last year's wage negotiations, the parties (and the TBU thereafter) estimated a 2.7% 2021 wage growth. Local adjustments and wage drift in a tight labour market turned out to become substantially higher than expected last spring
  - » In December **Norges Banks** assumed a 3.1%, after having revised up its forecast by 1.1 pp trough last year
  - » In Norges Bank's Q1 **expectation survey**, both employers' associations and trade unions thought wage rose 3.1 – 3.2% last year (the survey was conducted before SSB published its estimate)
  - » **Wage inflation** was somewhat lower in the public sector than in the private sector, and unions are now arguing for higher wage increases this year
    - However, looking back some few years, wage growth in the public sector has been higher than in the private sector. Still, there are potential for conflicts in the public sector wage negotiations this spring
- The **current 2.6% inflation forecast** is uncertain, both due to the global increase in inflation, and because the outlook for energy prices is uncertain. The forecast will be revised March 10, after the February CPI is published
  - » Electricity prices, as they are calculated in the CPI (and according to the SSB), are expected to rise by 2.5% in 2022, based on forward market prices. This outcome is somewhat strange, as future prices are heading straight down, signalling a substantial decline also in households' average electricity 2022 bill, following the steep rise in 2021
- 2022 wage expectations have shot recent months (check next page!) but the TBU report should calm down these expectations – at least vs the outcome in this spring's wage negotiations. However, the labour market is tight, and wage drift will probably propel wage growth through 2022, and through last year

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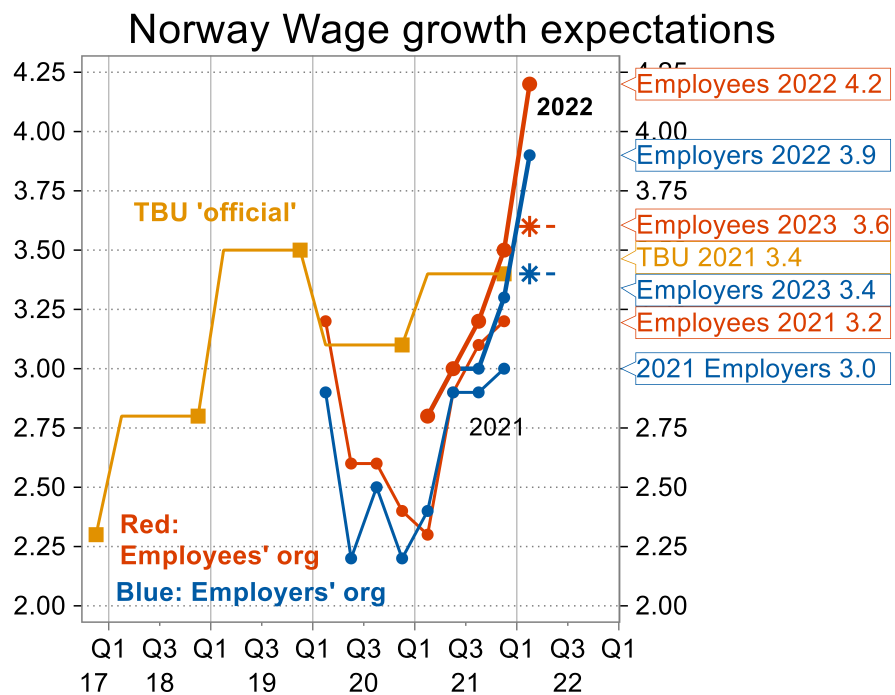
NoBa Expectation survey: Wages straight up in 2022, expectations up 0.6 – 0.7 pp

Are they aiming for 4%? A slowdown is expected in 2023, 'just 3.4 – 3.6% expected



SB1 Markets/Macrobond

2021 – wages rose faster than assumed by 'everybody'

- Wages rose 3.4% in the unionised part og the economy, according to TBU
- In Q4, leaders in the employers' organisations expected 3.0% and in the employees' organisations 3.2%, according to the Q4 NoBa expectation survey
- Norges Bank assumed 3.1% wage inflation in the Dec MPR
- In last spring's wage negotiations, a 2.8% wage increase was agreed upon

2022 – the largest upward revision ever!

- Leaders in employers' organisations lifted their forecast by 0.6 pp to 3.9% in Q1
- In the trade unions, leaders expect 4.2%, up 0.7 pp from Q3
- Norges Bank assumed a 3.2 % growth rate in the Dec MPR – and the bank will have to revise it's forecast sharply upwards
- We think wage inflation will approach 4% in 2020 but that will not be the outcome of the wage negotiations. The expectation survey was conducted before CPI inflation dropped to 3.2% in January from 5.3% in December

2003 – down to 3.5%. Well, that's not impossible but…

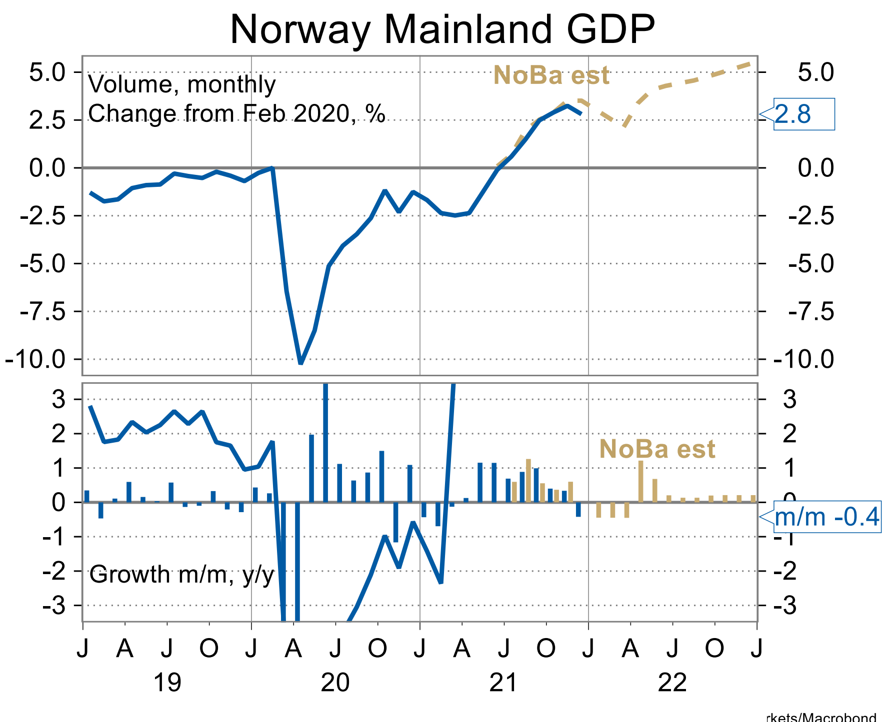
- Employers aim for 3.4%, the employees 3.6% as 2022 is assumed to be an exception, not the rule
- Given the current tight labour market, these forecasts seem to be on the low side

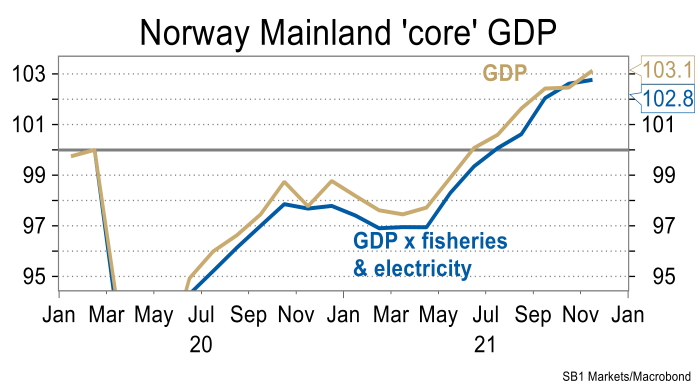
In sum

- We wrote 3 months ago: *'we expect further upward revisions the coming quarters as the labour market rapidly tightens'*
- Now, we are almost 'satisfied' with the 2022 forecasts, but the risk is still at the upside even if we do not think the wage negotiations this spring will yield a 4% outcome. However, actual wage inflation will probably climb to above 4%, due to the tight labour market
- Norges Bank will have to revise wage inflation up for both '21 and '22, by at least 0.5 pp in average in the March MPR

Mainland GDP down 0.4% in December, still +1.4% in Q4

November revised down, and Dec weaker than NoBa assumed but the recovery will start earlier

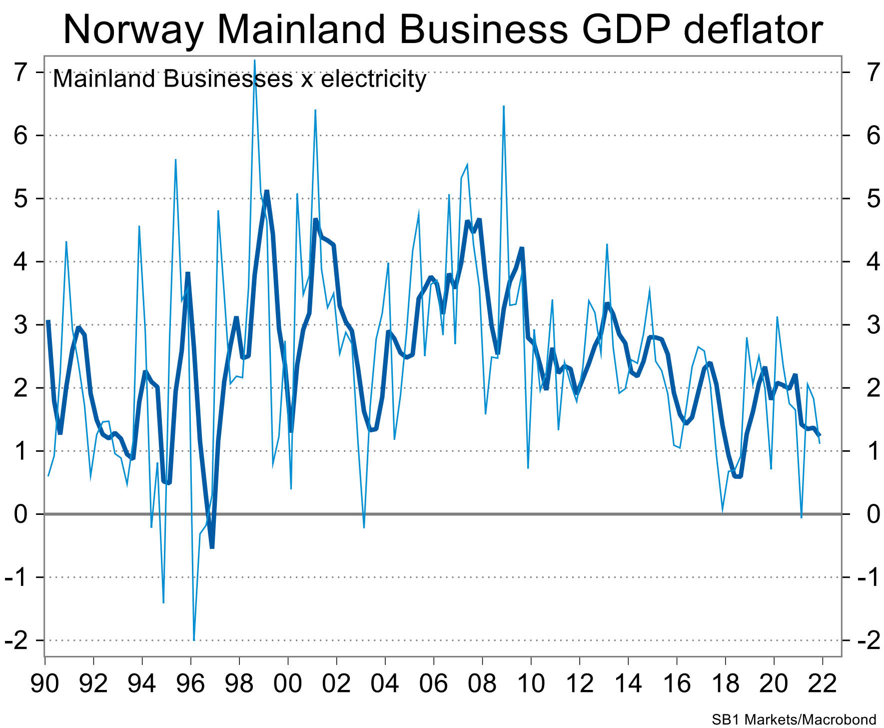


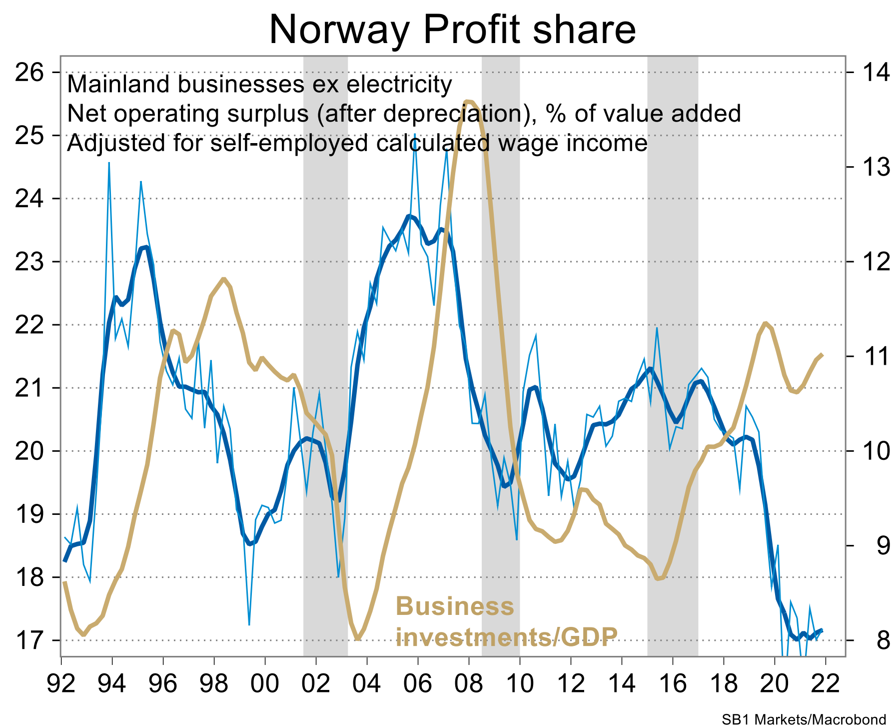


- **Mainland GDP** fell by 0.4% in Dec, Norges Bank expected unch, while consensus was for a 0.2% decline (we pencilled -0.3%). Growth in Nov was revised marginally down – but in total upwards
  - » **Production:** Detailed sector data are not available but activity in services fell by 1.8% m/m, as hotels & restaurants, culture was partially closed down.
  - » **Demand:** Norwegians' spending at home fell 2.7%, mostly due to a decline spending on services. Foreigners also reduce their spending, by 21%. Oil investments rose but history was revised unusually sharply down, by 10 pp while Mainland business investments rose sharply. Exports fell for the 2nd month in row
- **Mainland GDP is up 2.8% vs the Feb-20 level**
  - » **Production:** Services are back in black, even if production fell in December. Some sub-sectors are still below par, and more so in Dec. Manufacturing is down 1.2%. Other goods are sharply up, partly due to fisheries
  - » **Demand:** Norwegians' spending at home is up 7% from Feb-20, goods 13% (and now heading down), services are down 3% - but was trending rapidly up until December. Spending abroad is still down 56 %, and total household spending is up 1.4%. Oil investments are still in minus, revised sharply down (by 10%!). Mainland investments are finally in plus
- **The recovery was intact until December. We do not expect a recovery in January but February & March should be well into the black – as activity will start recovering 2 months earlier than Norges Bank assumed in December**

The profit share was under pressure, before corona – and still is

Operating margins have stabilised at a rather low level. Investments are exposed?

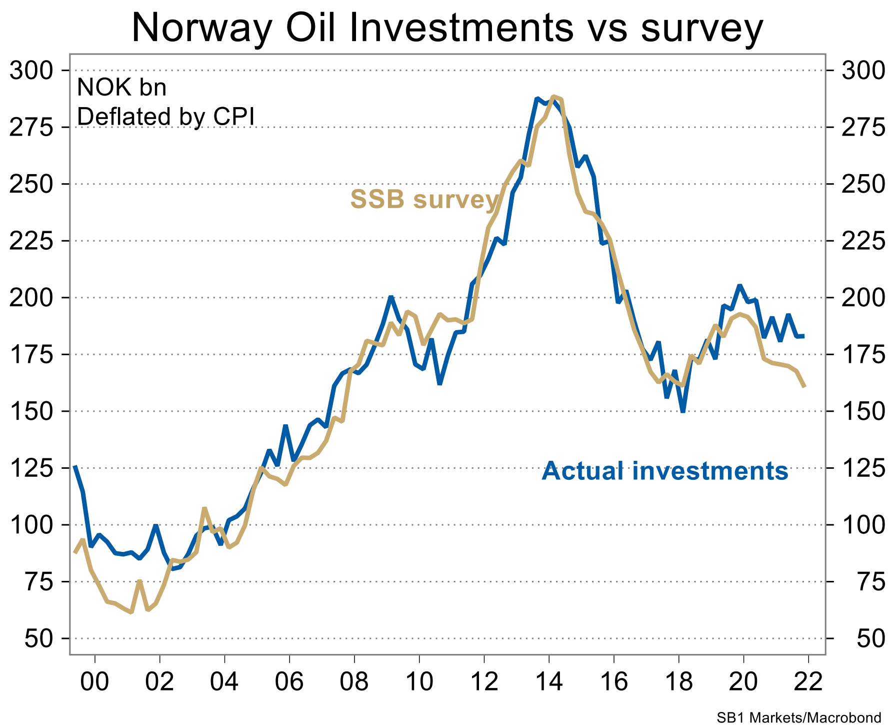


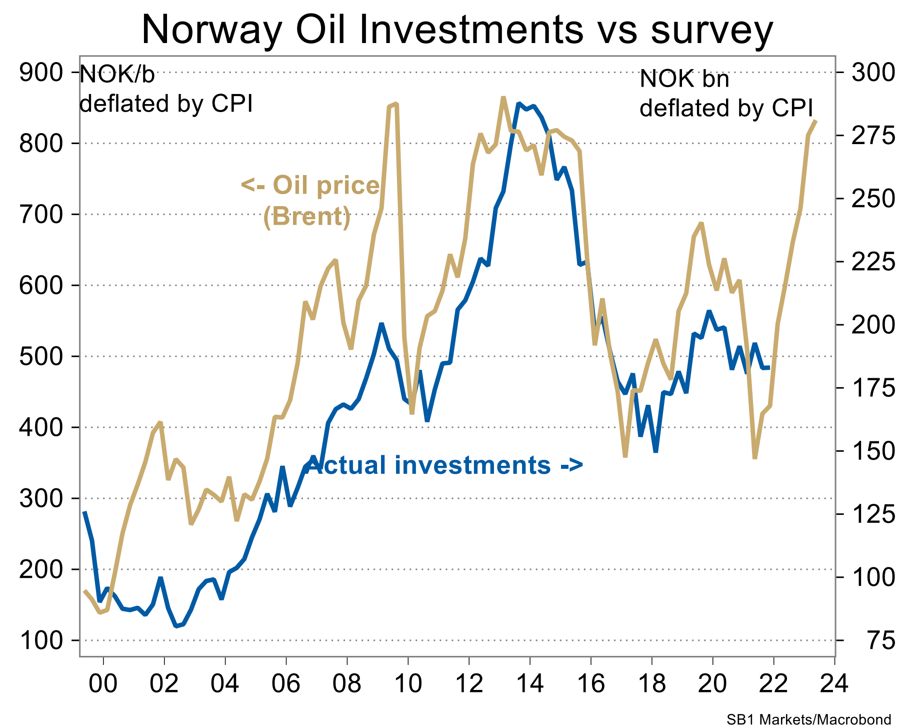


- The **Mainland business GDP price deflator** (ex the volatile electricity sector) has slowed to below 1.5%! There are huge differences between sectors. Manufacturing prices rose 0.4% last year (value added deflator)
- Unit labour cost (wage growth – productivity growth) is marginally higher (at 1.4%), and the gross margin is still slowly deteriorating
- The **Mainland business (ex electricity) gross margin** level is low – which signals some risk vs the above average investment ration

Oil investments: 2022 will be the local bottom

The temporary tax relief and high oil prices will lift investments substantially in 2023 (and '24+)

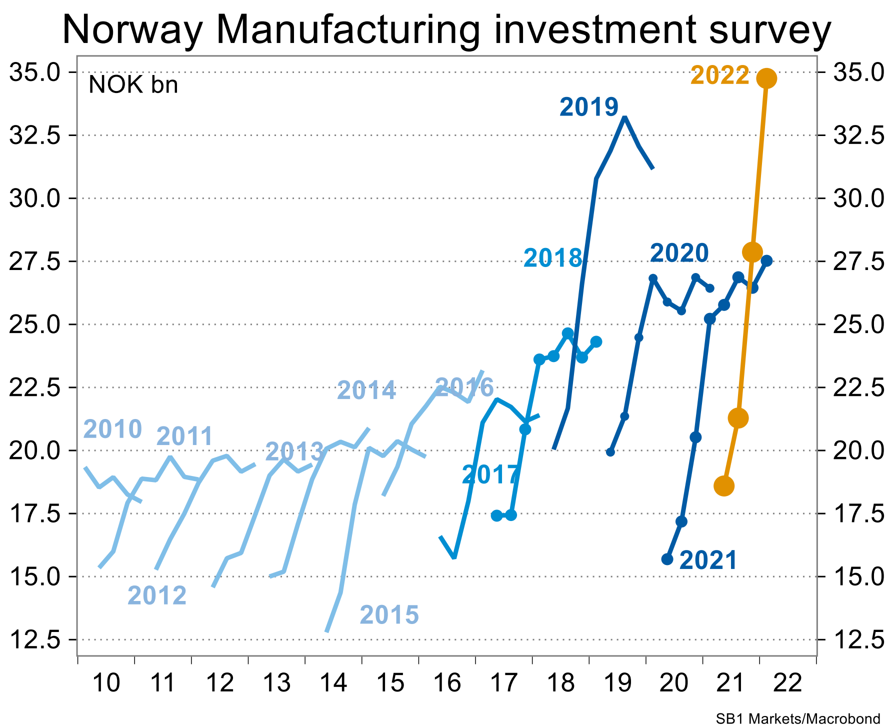


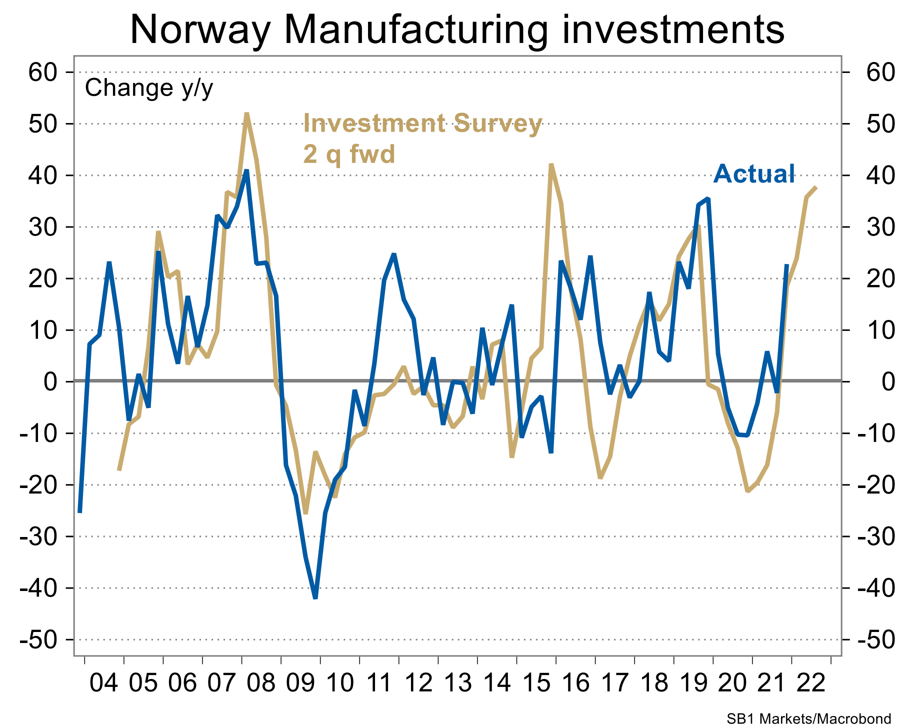


- Oil investments fell 3% in volume terms in **2021.** Nominal spending rose by 2%
- **Oil companies lifted their 2022 investment estimate** by 3% to 160 bn. The estimate is still 8% below the equivalent 2021 estimate. Several investment projects will be added to the list (a PDO delivered) before end of 2022in order to benefit from the temporary tax cuts decided in 2020 – and a higher oil price is also supportive. <u>Still, we expect another 4 - 6% drop in investment volumes in 2020</u>. In December, Norges Bank assumed a 6% volume decline next year
- <u>**The 2023 outlook** is far better, even if the first estimate is down as investment at a large no. of projects not yet included SSB's survey will be added the coming quarters</u>

WOW, manufacturing investments through the roof! Very strong growth signalled

The 2022 investment estimate revised up by 25% to Feb from Nov, the steepest rise since 1985!

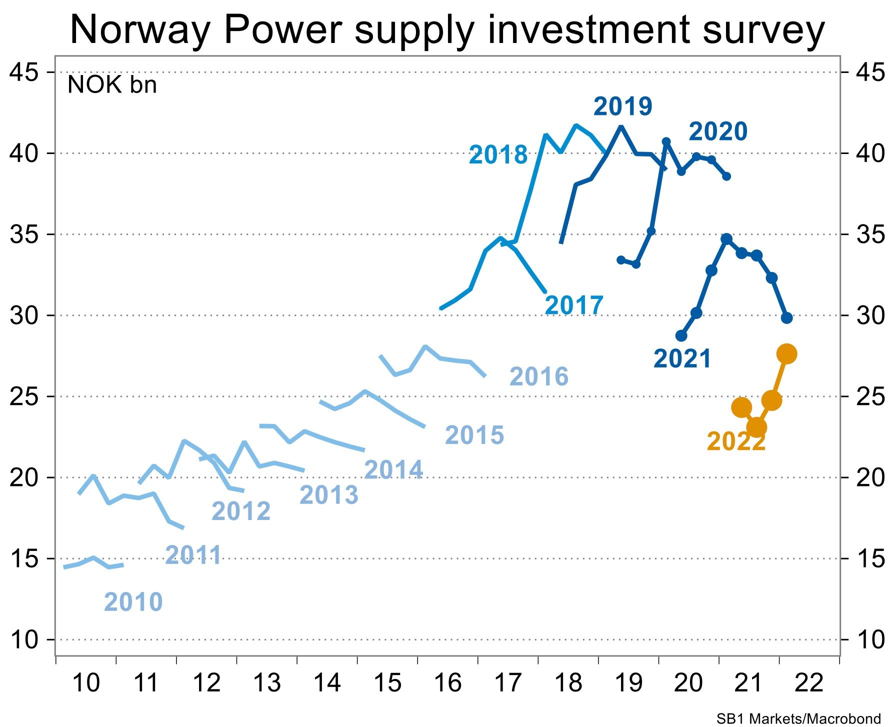


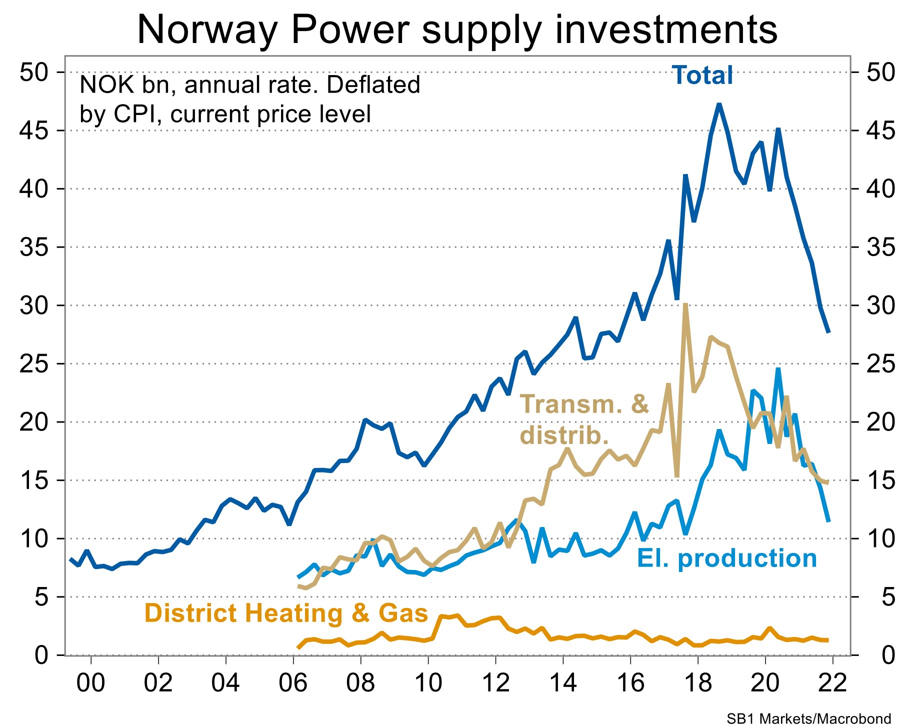


- Manufacturing companies report a 7% growth in **investments in 2021**, slightly better than we expected
- However, we do not expect the 25% lift in the **2022 forecast** to NOK 34.7 bn, following the 31% upgrade of the forecast 3 months ago – in sum 63% over 6 months, the 2nd largest upgrade ever (data from 1979). The increase from the equivalent 2021 forecast at 38% is the 3rd highest in history, just 1986 & 1995 were even stronger. A 30% growth in investments in volume terms in 2022 is not unlikely. Check chart 2 pages fwd
- **Computer/electrical equipment** contributed the most to the increase in the 2022 forecast vs the Q4 survey, and report investment plans at NOK 4.5 bn, up from 1.1 bn in 2021. Have couple of battery fabs been included?? Is it possible to spend that much money in 2022?
- **Non-ferrous metal industry** reports very aggressive 2022 investment plans too, NOK 6.5 bn vs 2.9 bn in 2021

Power supply: 2022 investments revised up, level still low

Investments fell 23% in 2021, and the 2022 f’cast signals a further substantial (15%) decline

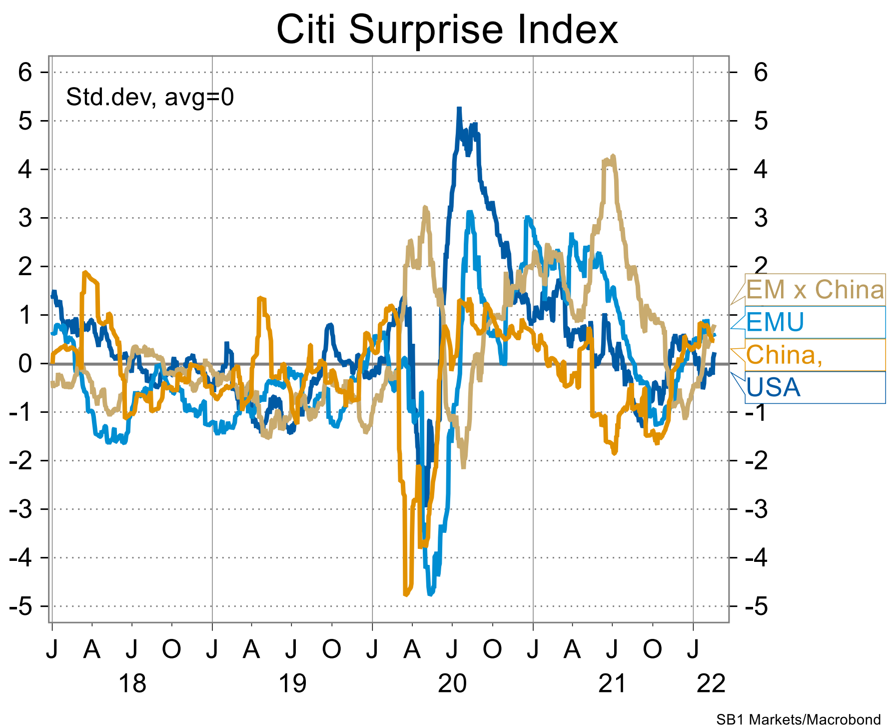


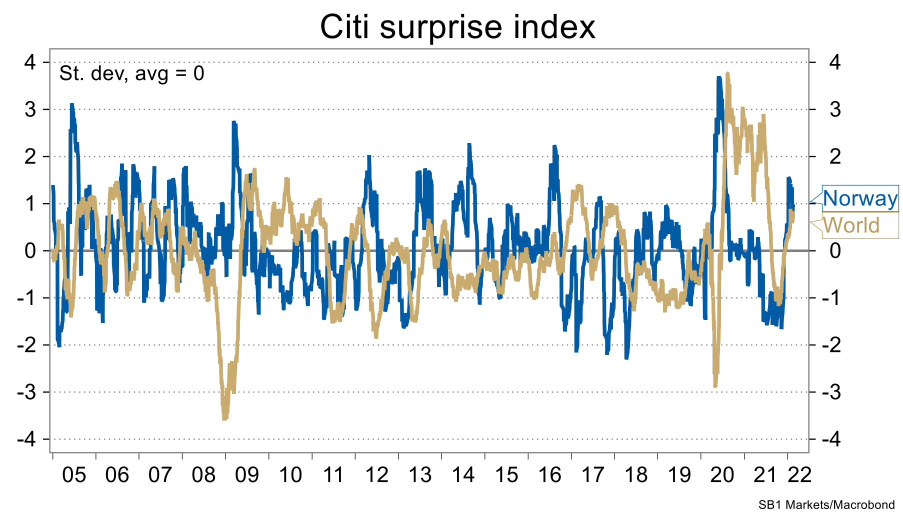


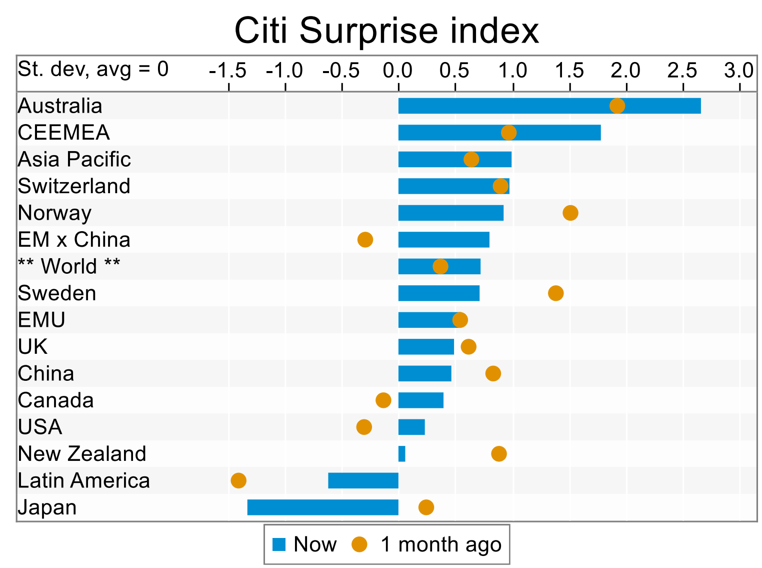
- **Power supply (production & distribution) companies** invested NOK 30 bn in 2021, down from 23% from the 38 bn level in 2020 (and 40 bn at the peak in 2018)
  - » Some big wind power projects were completed by the end of 2020, and few new projects have been added, contributing to the decline in 2021
- Companies lifted their **2022 investment** f’cast by 3 bn (12%) vs their Q4 prognosis, well above the 5% average revision in the Q1 survey. The estimate is 20% below the equivalent 2021 forecast (and 7% down vs. the final 2021 outcome. From the Q1 survey, estimates are normally revised down, by some 7% in average
- Until 2018, power supply investments had more than quadrupled since early 2000, by more than 10% p.a on average. The investment level as % of Mainland GDP was above 1%, the highest in decades. Both production & transmission have contributed. To 2022 from 2018, investments may decline by 36%, in nominal terms, and more in real terms. Will the green transition turn the tide? Quite likely

Almost all regions report growth above par

… almost everyhere!





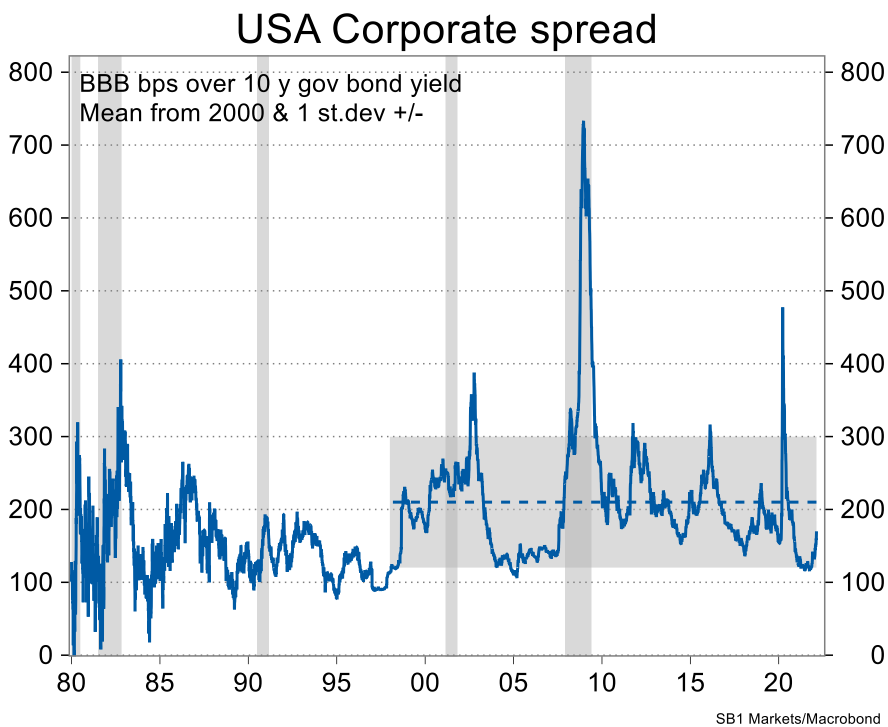


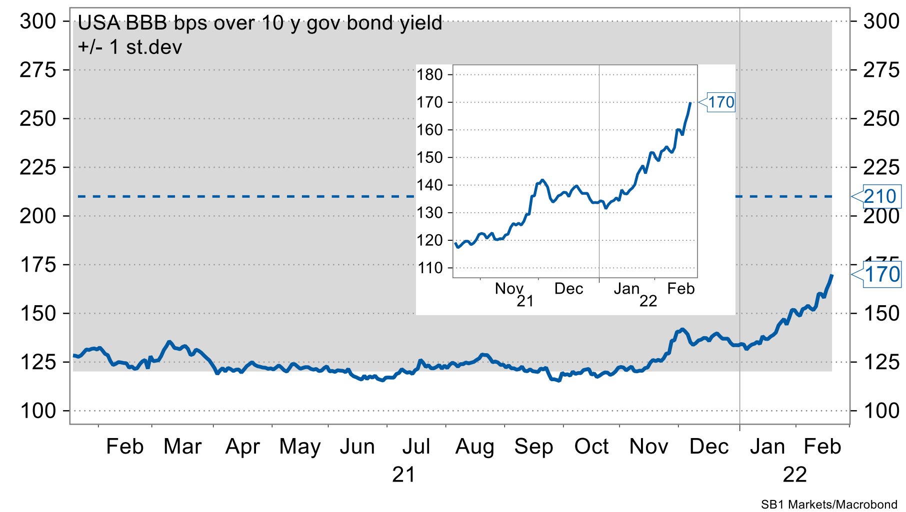
- **Norway** was surprising sharply on the downside through most of 2021, according to Citi. But in early December we crossed the zero line, and now we have suddenly moved up to the very upper part of the list

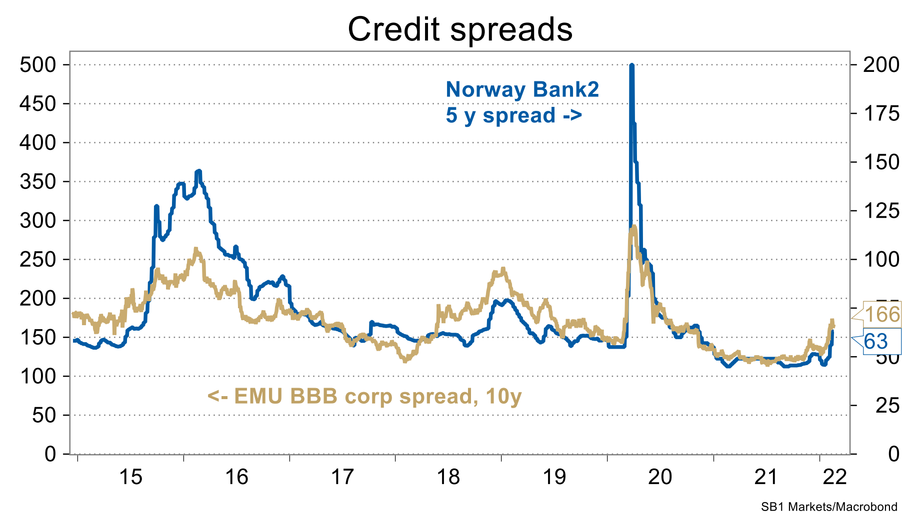
Surprise-indices measure the difference between economists' expectations and the actual outcome over a 3 month rolling window

The credit cycle has turned – and now even Norwegian banks have to pay up!

Higher bond yields, lower equity pricing is not the best environment for credit spreads



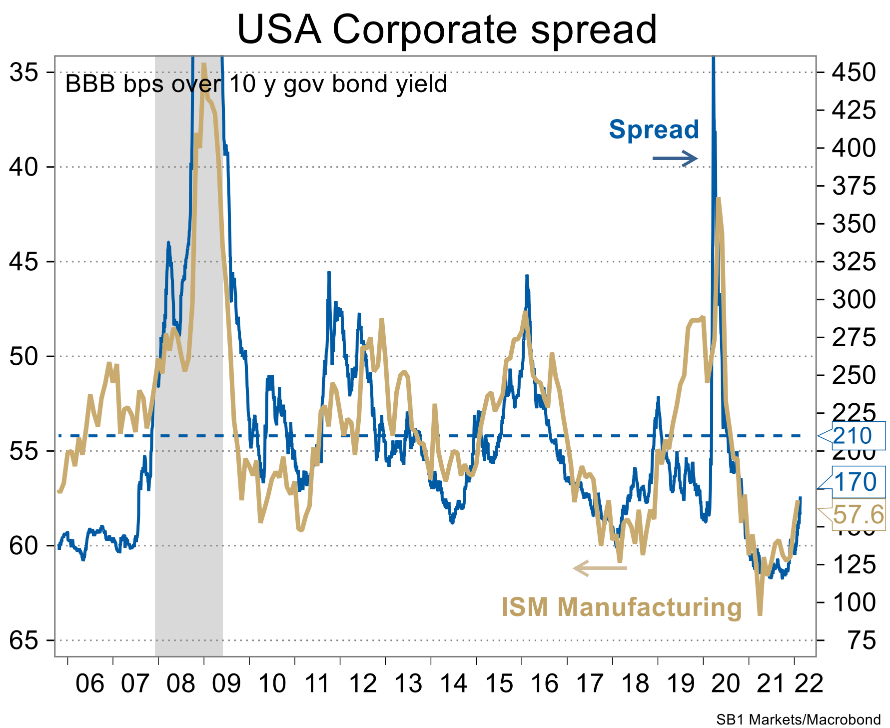




- The increase in US Corporate BBB spread now equals >0.5 st.dev, still just a fraction of a normal full credit cycle
  - » The credit cycle is often closely correlated to the economic cycle, check next page
- The NOK Bank 2, 5y spread widened 7 bps to 63 bp last week (and from below 50 two weeks ago), the highest spread in more than one year

It could be the economy, stupid

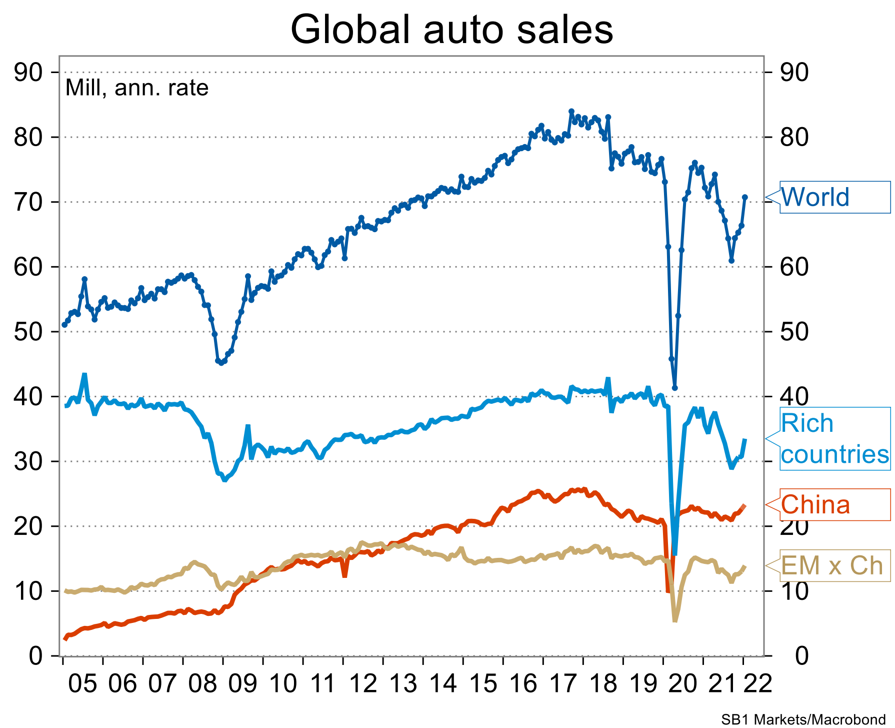
Growth has to be slowed to get inflation under control. If that happens…

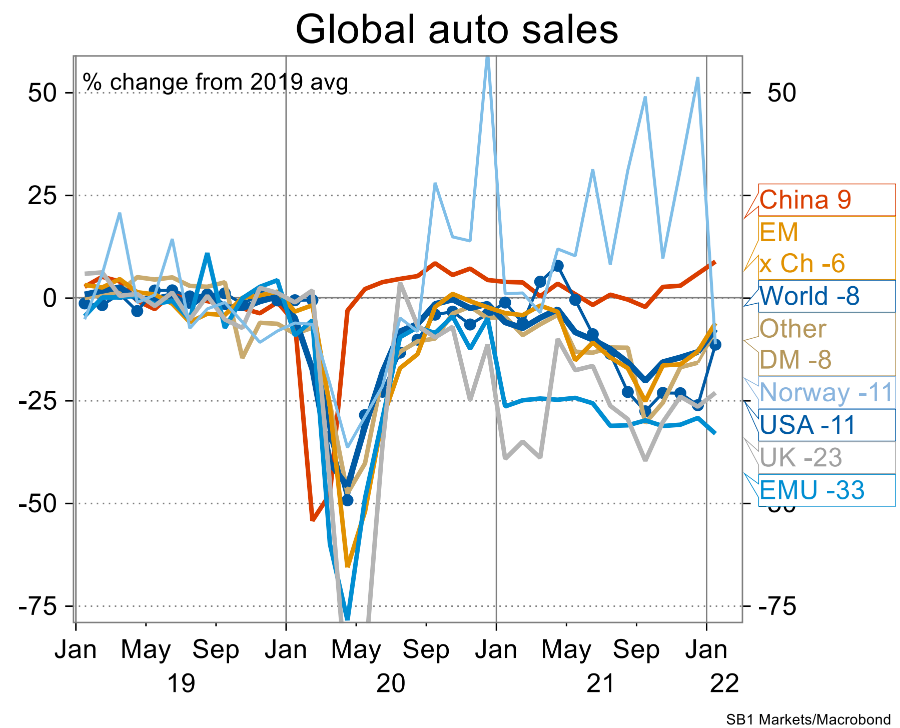


- Growth has already slowed somewhat, according to the US manufacturing ISM – and all other surveys

Auto sales are recovering, are 'just' 8% below the 2019 level

Sales rose sharply in the US, in EM x China, and probably in China as well





- **Global sales** rose by almost 6% m/m, according to our calculations (some few countries have not yet reported). Sales are down 8% vs. the average 2019 level, up from -21% at the bottom last September
- **US** contributed most at the upside, up to -11% vs. the '19 level. Sales in **EMU** fell again, and are down 33% vs. 2019
- Sales in **China** are trending slightly upwards, and preliminary data suggest a further increase in January – and sales may be 9% above the 2019 level
- Most other **Emerging markets** also reported stronger sales in January, we estimate 6% shortfall vs. '19
- **Norwegian** sales fell sharply following the record high level in December
- **Auto production** is now recovering, especially in Germany

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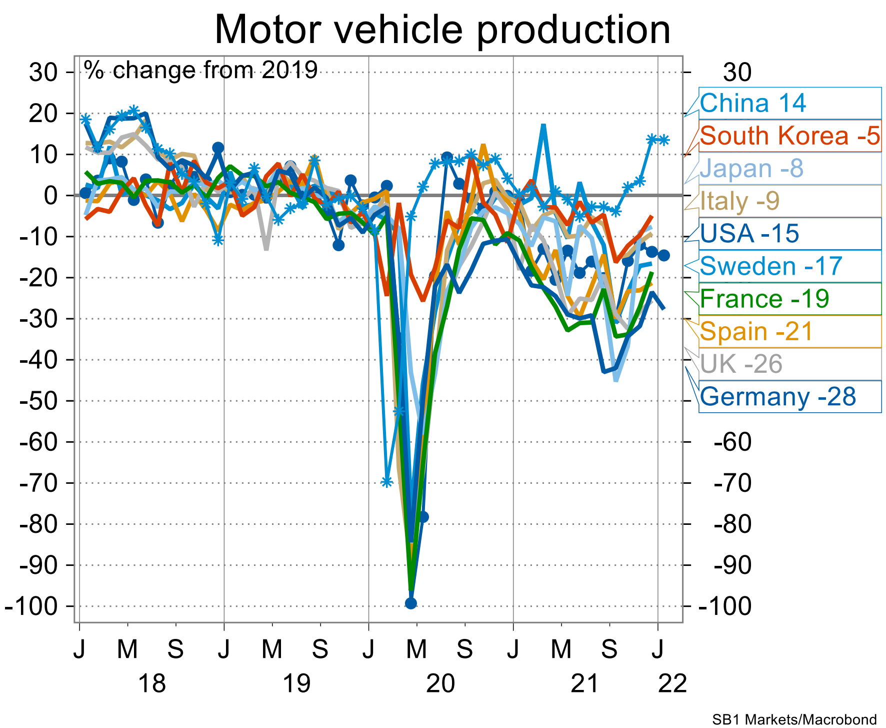
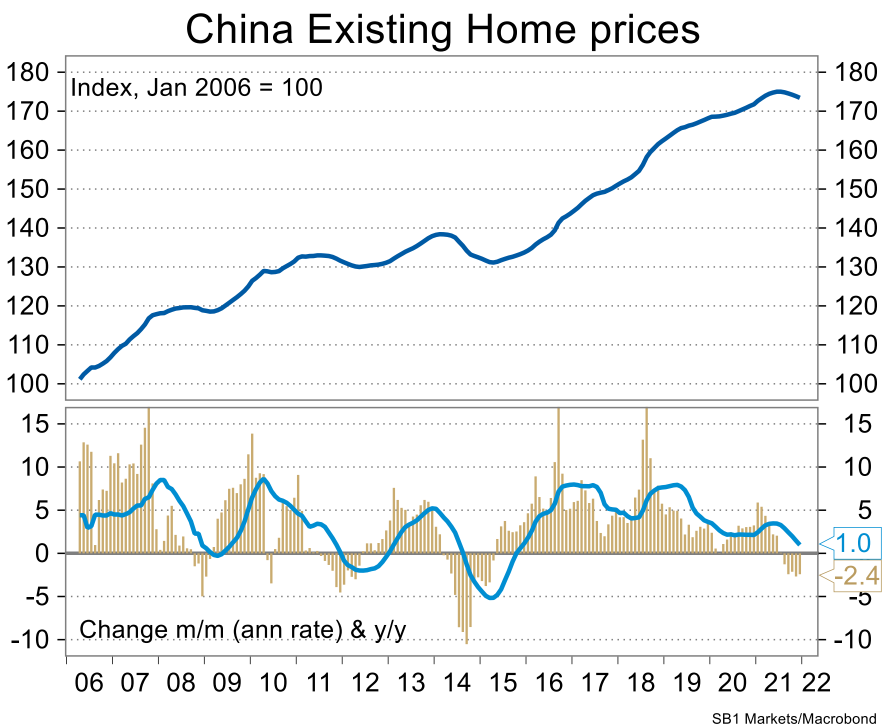
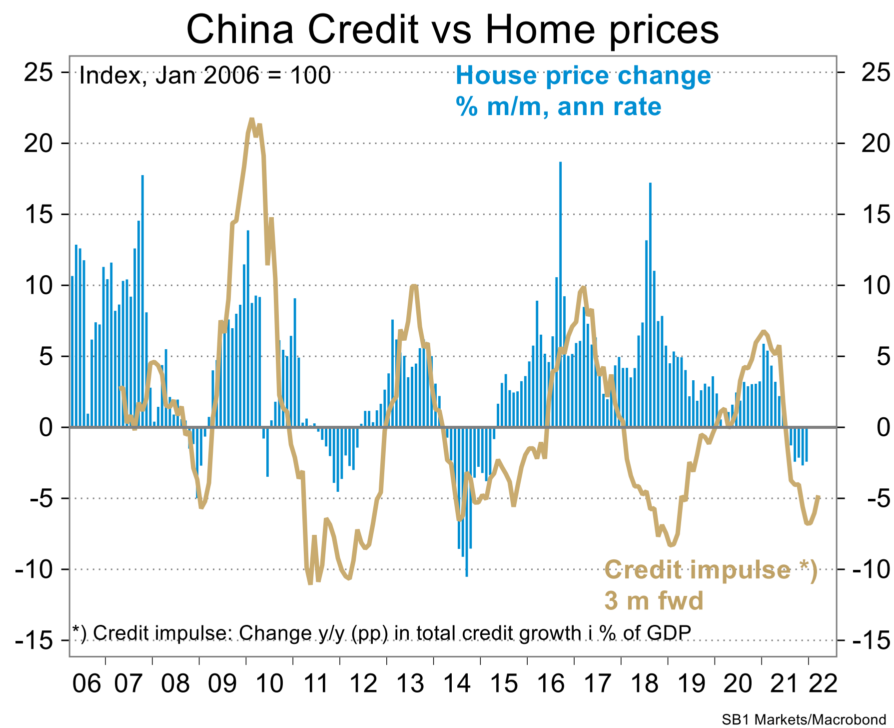
Auto production on the way up!



House prices turn south, so far at a measured pace – still the main Chinese risk?

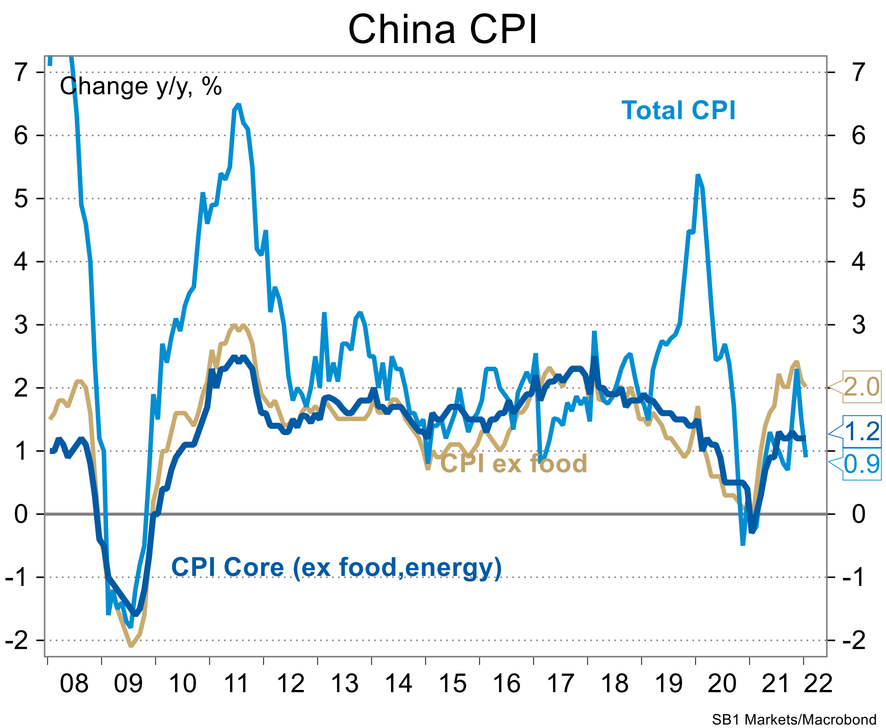
Prices fell for the 4th month in row but are still up 1% y/y

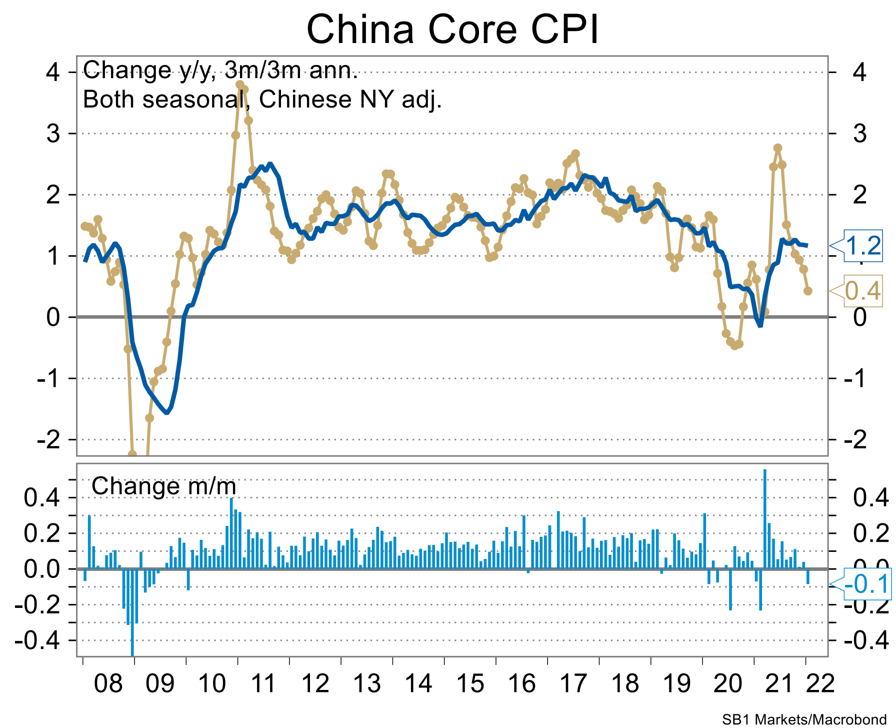




- **Existing home prices** peaked in July, and have fallen at a 2 – 2.5% pace since then – and by 2.4% annualised in Dec. Prices are still up 1.0% y/y
- **New home prices** peaked in August, and have fallen slower than existing home prices. So far, not any signs of distressed sales from 'bankrupt' property developers
- **Credit growth** accelerated marginally during last year, mostly due to increased borrowing from local governments
- **Several heavy indebted property developers** are struggling which surely poses a treat vs the housing market & construction activity. The builders may be restructured, with a helping hand from the authorities, who also can supply credit to bail out buyers, and support sales of buildings under construction
- We think the **main risk is** that home buyers at one stage loses confidence in housing – even in empty homes – as a safe and profitable investment. Several small setbacks in prices have so far not made a dent in the investment appetite, and the current modest setback in prices does not signal a buyers strike. Should that happen, a much harsher setback in construction activity would take place

No inflation in China, the headline up just 0.9% y/y, the core 1.2%

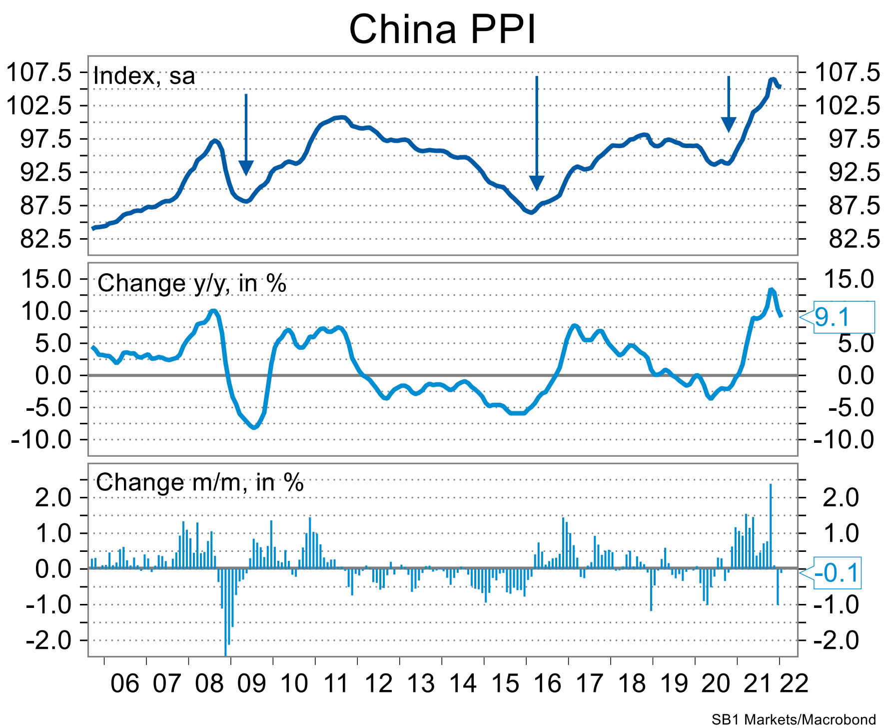


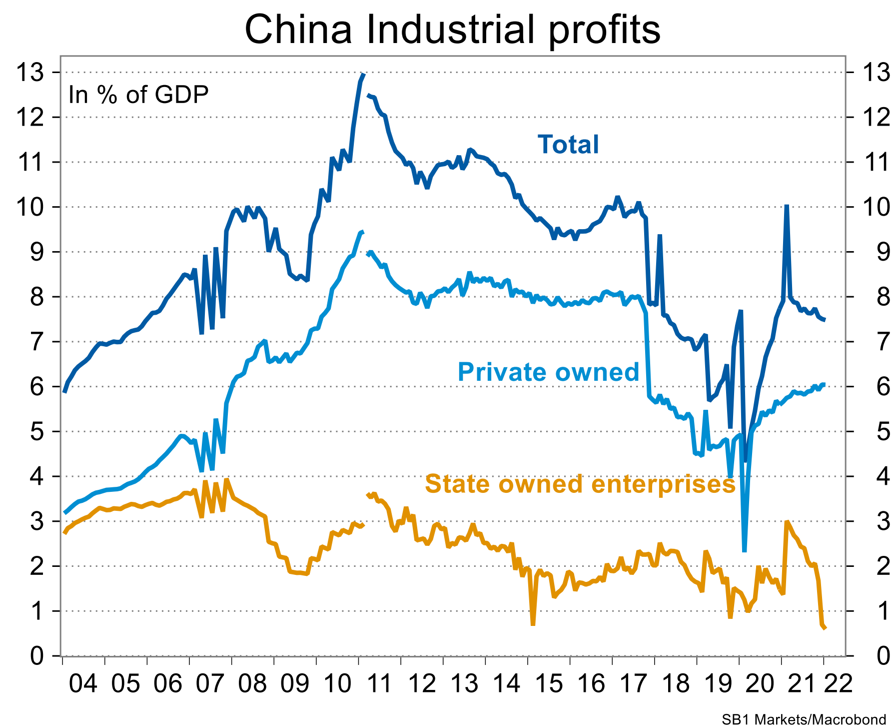


- **Total annual CPI** growth fell 0.6 pp to 0.9% in Jan – as prices fell 0.3% m/m. The annual rate was expected down to 1% - so no surprise
- **The core CPI (x energy, food)** was unch at 1.2% y/y. Prices fell 0.1% m/m. The 3m/3m rate fell to 0.4%
- **Food prices** rose marginally mm, and are still down 1.2% y/y, due to the normalisation of pork prices – even if vegetable prices rose sharply
- <u>Inflation is low</u>. **Monetary policy** will not respond to actual inflation data if inflation is not really high or low, <u>the real economy and the credit market is more important</u>

Peak PPI~~?~~ !

Prices fell 0.1% m/m in Jan, following the 1% drop in Dec. The y/y rate is 9.1%, it peaked at 13.5%

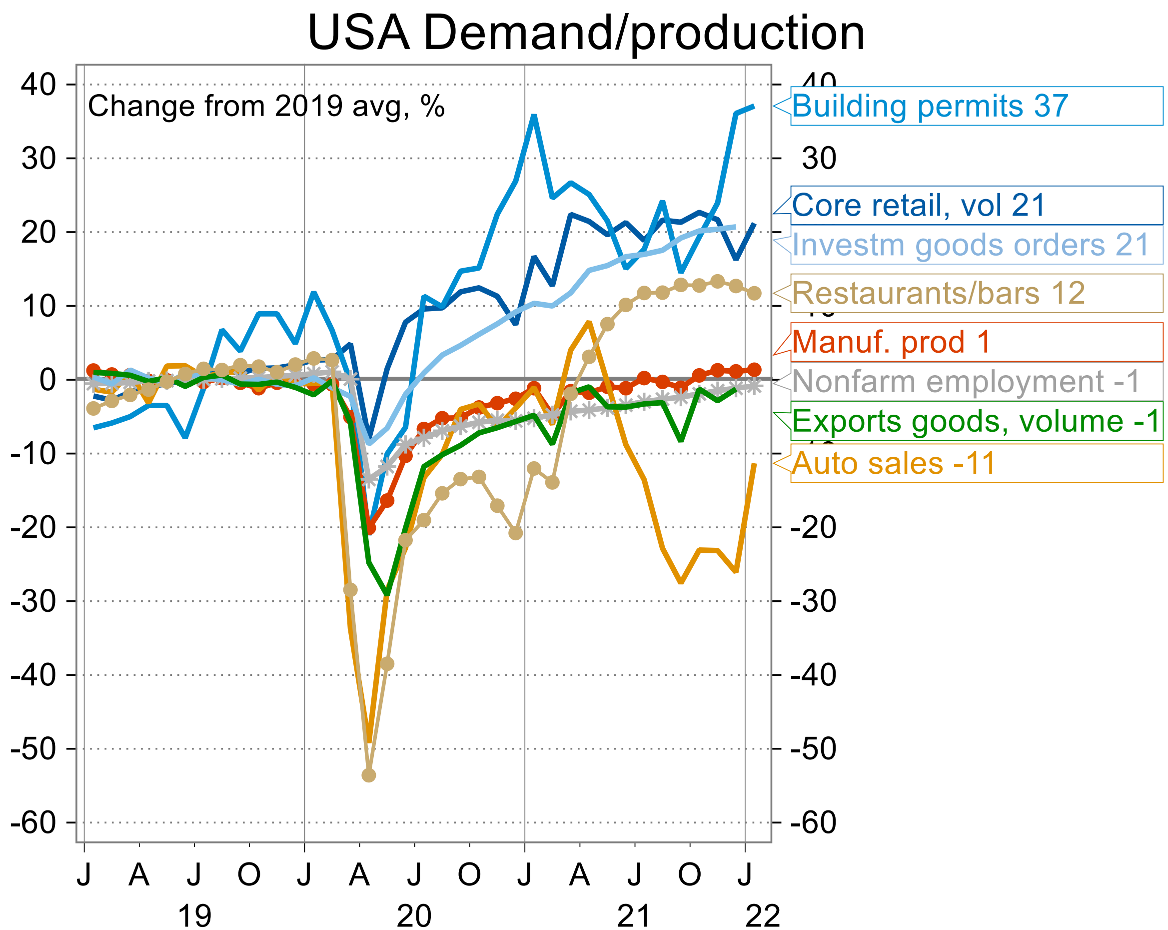




- **The PPI** has turned south the two past months, and the annual growth rate has slowed more than 4 pp. Raw material and intermediate prices have calmed down
  - Consumer goods are up 0.8%, durable consumer goods are up 0.6% y/y. The correlation between PPI and CPI in China is not impressive
- **Profits in privately owned industrial enterprises** fell by 50% in February ‘20. Profits rose to a normal level in April/May ‘20 – if we label the profit level in 2019 and early 2020 as normal – at 5% of GDP – and now it has climbed to 5.9%
- **Profits in state owned enterprises profits** have fallen sharply recent months – to a record low level

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

The upside now: Auto production & exports

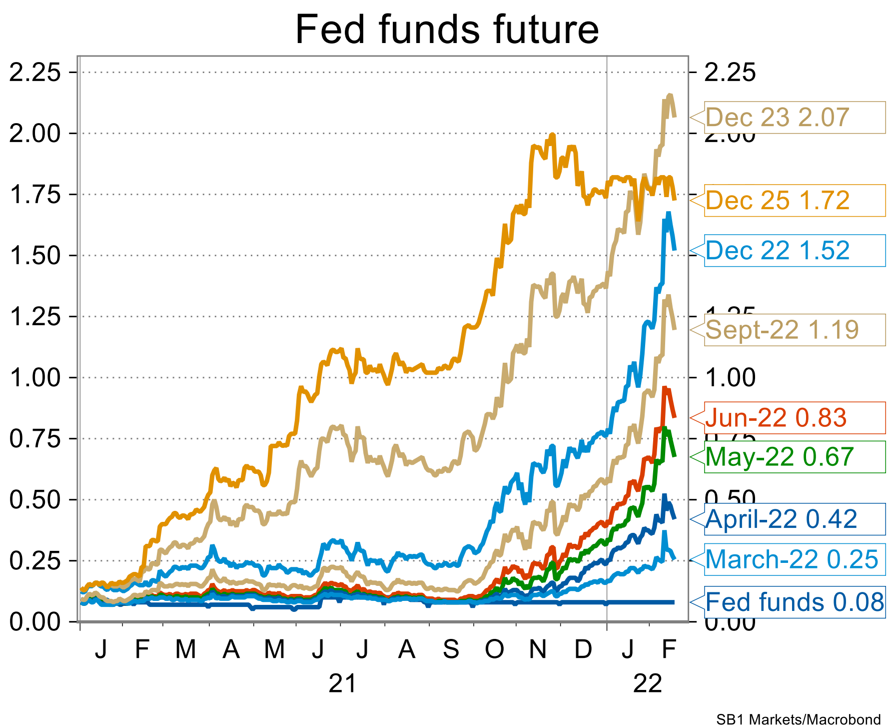


SB1 Markets/Macrobond

- Retail sales have peaked, but is still at a high level. Auto sales rose sharply in January
- Housing starts/building permits are are up recent months
- Manufacturing production is 'too weak' but supply constraints, exports have kept production in check
  - » Auto sales rose sharply in Februar, but the level is low, and the production way below normal level

FOMC minutes: not even more hawkish than expected (or James Bullard)

As we assumed the news was out, and discounted, and that minutes would not send rates up



- **The two previous FOMC minutes** were significantly more hawkish than Powell's comments after these meetings. At the press conference after the late Jan meeting, Powell was much more hawkish than we have heard him before. After that, some FOMC members have dropped comments on the need for a more rapid monetary tightening, which together with a series of strong data have pulled rate expectations sharply up – the Dec-22 Fed funds contract shot up 67 bps (!!!) since before the Jan 26 FOMC meeting. We assumed that the minutes could not be even more aggressive than that – and they were not. They were just aggressive
  - » Participants agreed that uncertainty regarding the path of inflation was elevated and that risks to inflation were weighted to the upside (supply chains, geopolitical turmoil - energy prices, wage-price dynamic, unanchored inflation expectations)
  - » Most participants noted that, if inflation does not move down as they expect, it would be appropriate for the Committee to remove policy accommodation at a faster pace than they currently anticipate. Some participants commented on the risk that financial conditions might tighten unduly in response to a rapid removal of policy accommodation."
  - » Thus, the majority is willing to take the risk of tightening too much
- The FOMC also debated how to reduce the balance sheet, but no conclusion was drawn
- **Market reactions:** The Dec-22 contract fell 4 bps on Wednesday, and further on Thursday & Friday very likely due to war angst – stock prices fell too

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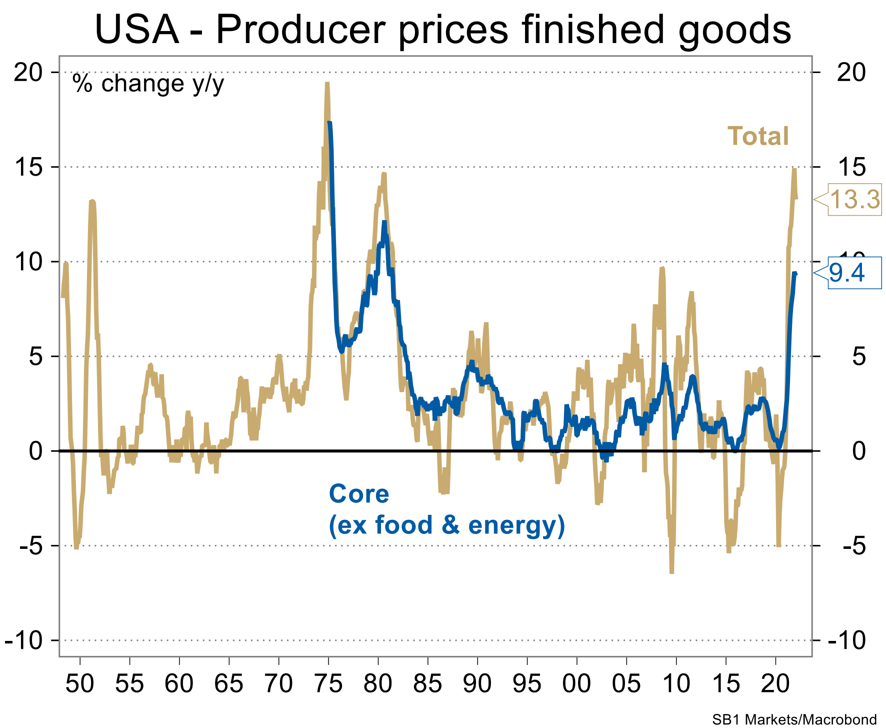
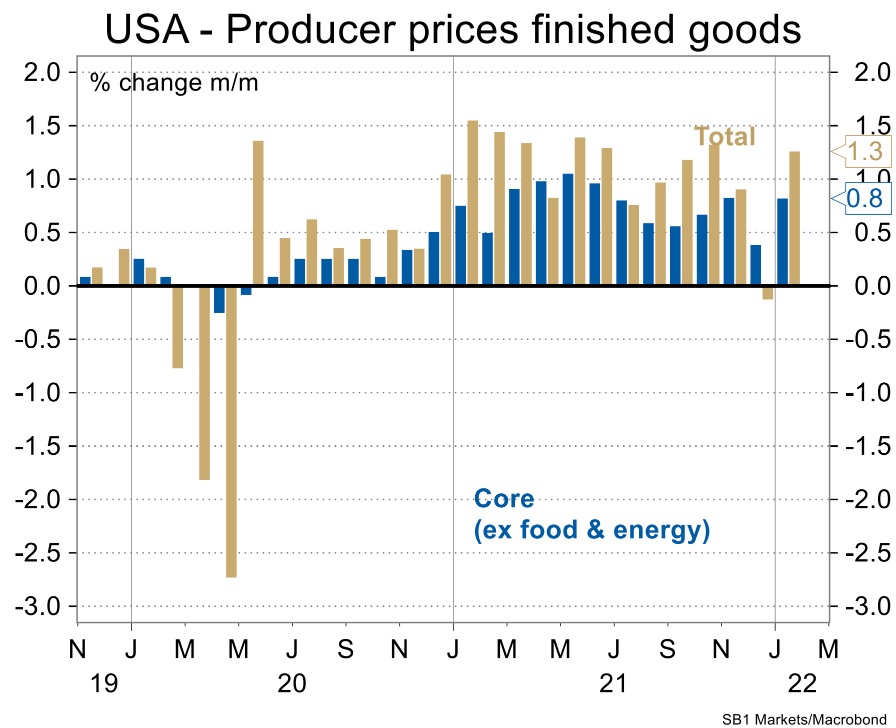
The PPI up 1.3% in January, and Dec revised up – up 13.3% y/y

However, crude materials (ex energy) are on the way down!

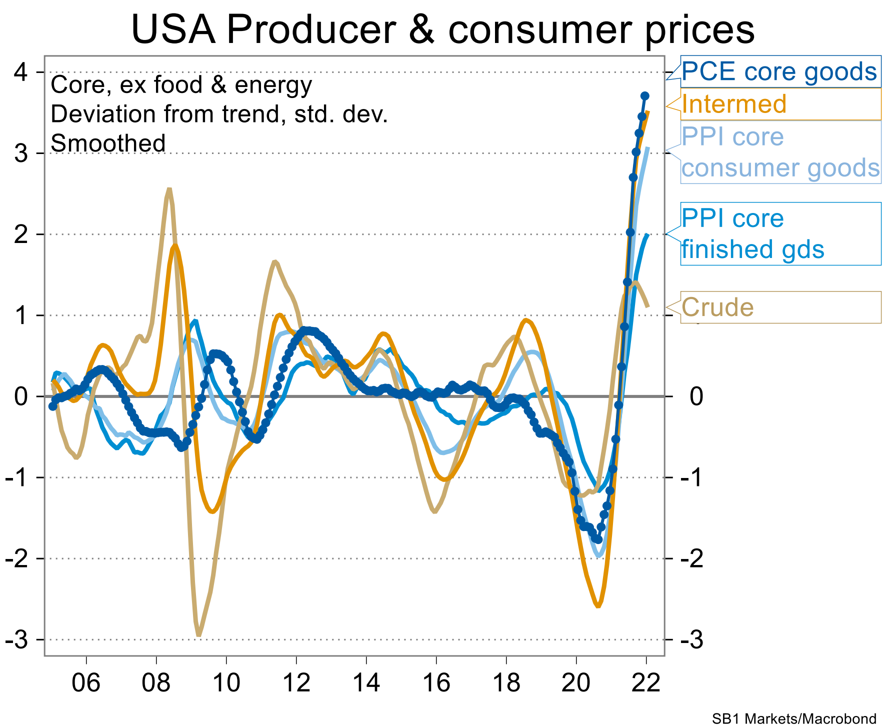


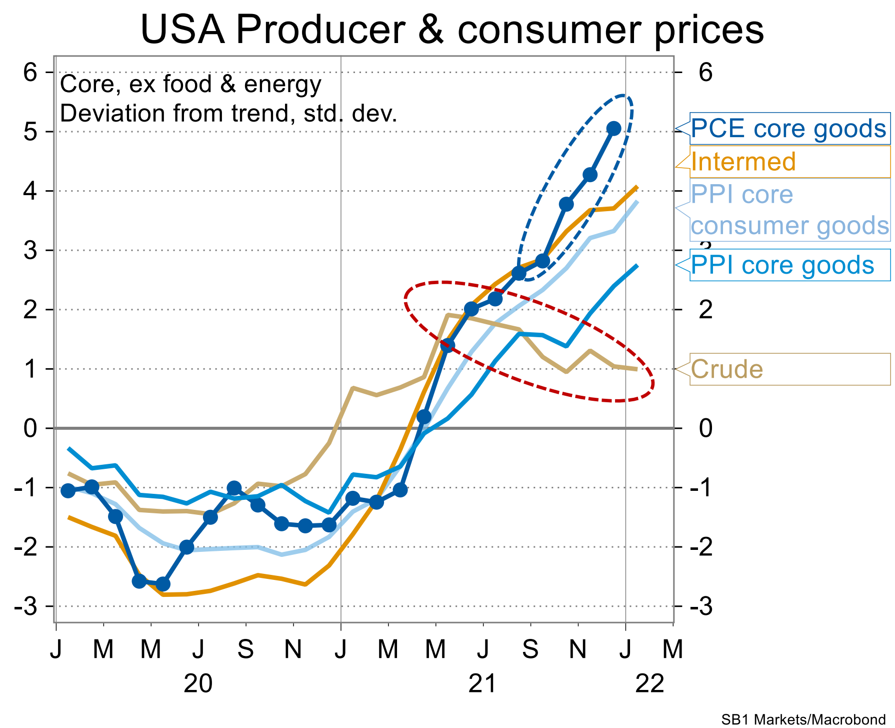


- **The headline finished goods PPI** shot up 1.3% in January, and Dec was revised up to -0.1% from -0.4%. The annual rate is slightly down from the peak, is still at 13.3%, the highest print since Jan 1975
- **Core finished goods x food & energy** PPI rose by 0.8%. The annual growth rate was unch at 9.4%, highest level since 1982
- The good news: **Crude material prices** are retreating. In addition, **core CPI goods prices** have already climbed more than usual vs. PPI prices (due to 2nd hand auto prices), limiting the upside risk
- **The 'official' total final demand PPI**, including **services**, rose by 1% and history was revised sharply up. The annual rate was 0.8 pp higher than expected, at 9.8%

Crude materials have peaked. But the pressure from supply chains is still strong

… However, core <u>consumer</u> prices have been rising earlier and more than normal vs. PPI prices

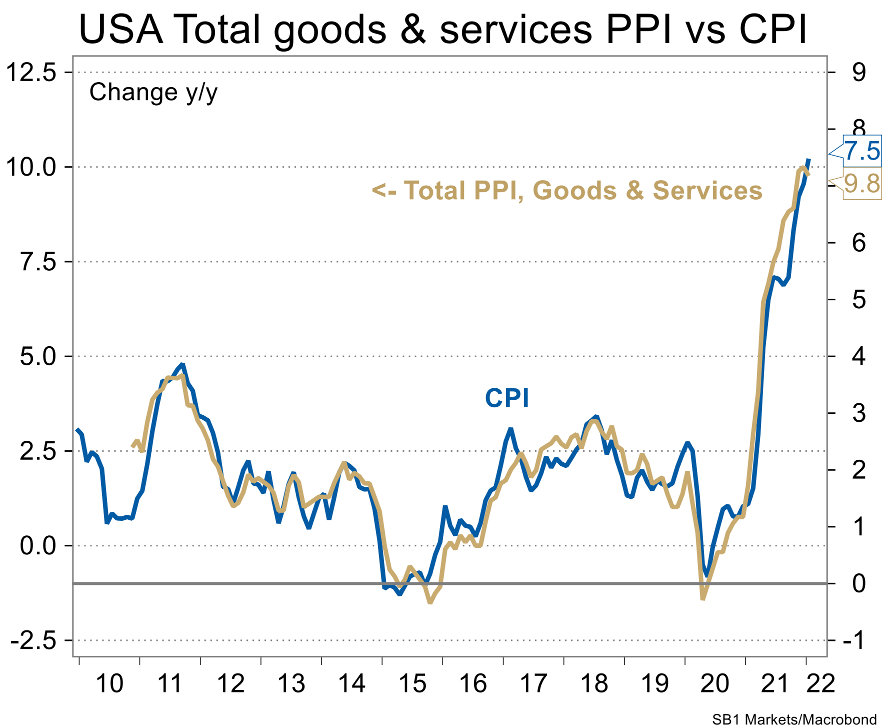


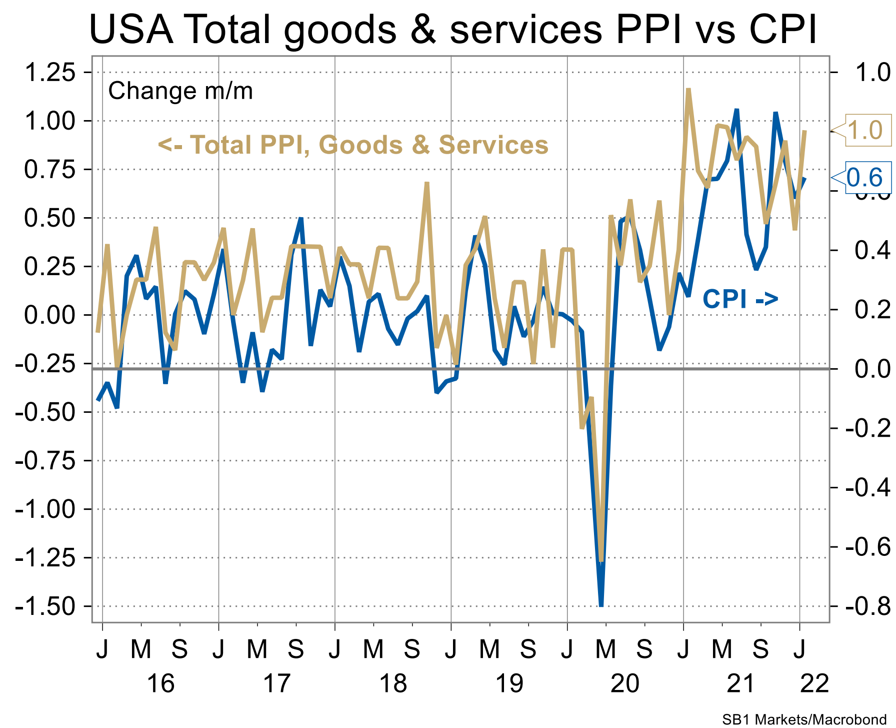


- **Crude goods prices** are leading intermediate goods prices by 4 months, and consumer prices by 12 months. Now, <u>crude prices have clearly peaked</u> (see the red ellipse on the chart to the right). However, **intermediate prices** have not yet yielded by much – and they will push finished goods prices further up the coming months
- Some more comfort: **Prices at the <u>consumer level</u>** (blue ellipse on the chart to the right) have responded <u>earlier and more than normally</u> vs the PPI core consumer goods index. That is very likely due to the unprecedented (and very likely not permanent) hike in 2nd hand cars which <u>are not a part of the PPI index</u>. Thus the <u>upside risk for the core goods component of the PCE may be limited the coming months</u>

Bottom line: Total PPI (services included) confirms 7.5 % CPI growth

The total PPI rose 1.0% m/m in Oct, expected 0.5%. Up 9.8% y/y, exp. 9.0% – the history revised up

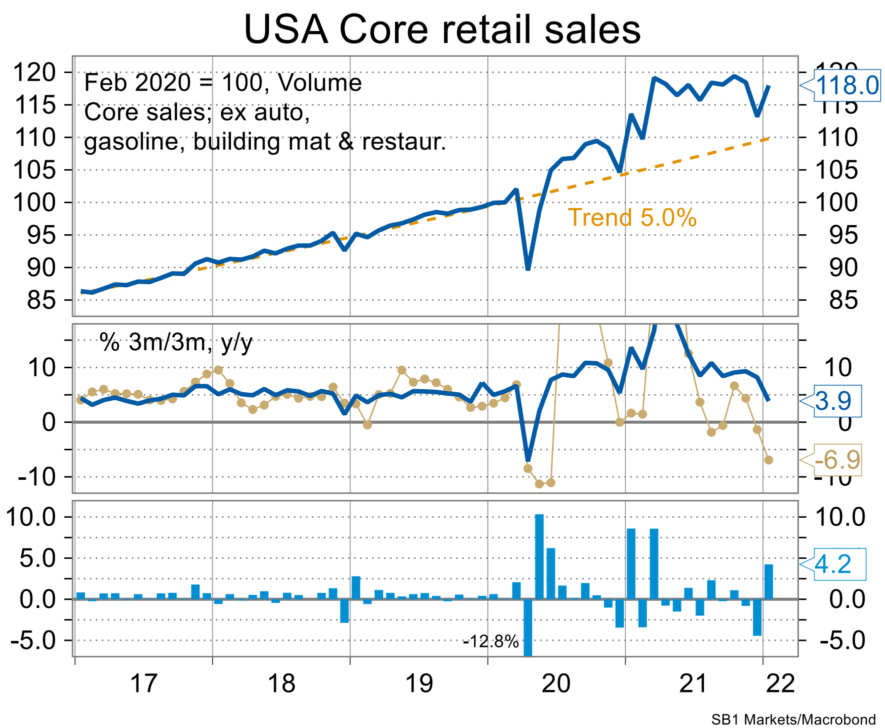


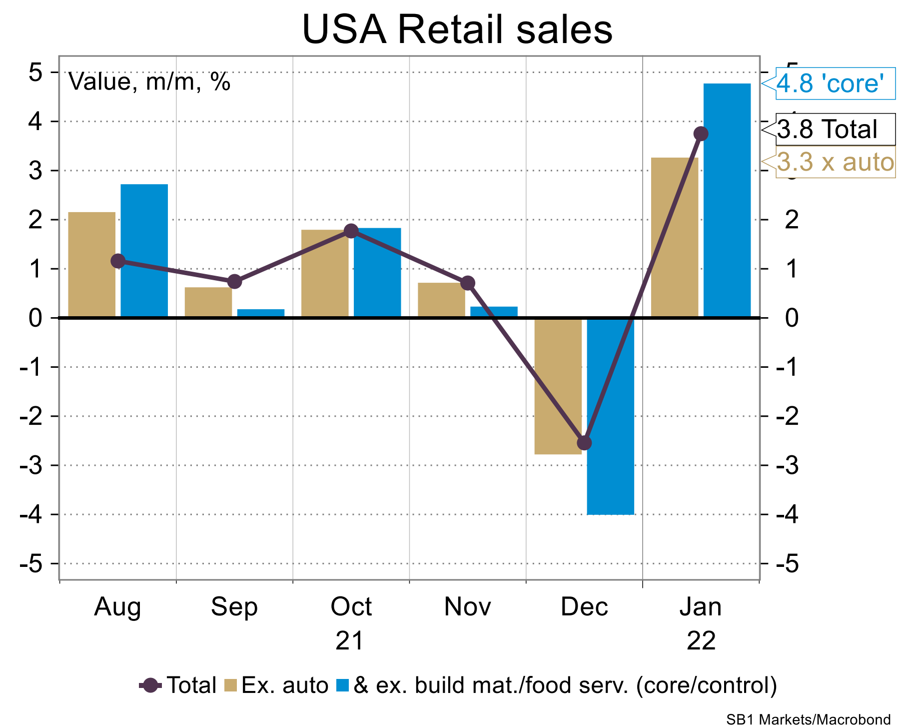


- The correlation between the 'new' total PPI, which includes all sort of services in addition to goods vs the CPI is pretty close. The current close to 10% annual growth rate in the PPI signals some 7.5% y/y growth rate in the CPI index. Which seems to be a precise estimate ☺

Retail sales recovered much better than expected in Jan, trend still just flat

… for core goods volumes, up 18% vs. Feb-20. Total sales are up 24% in nominal terms!

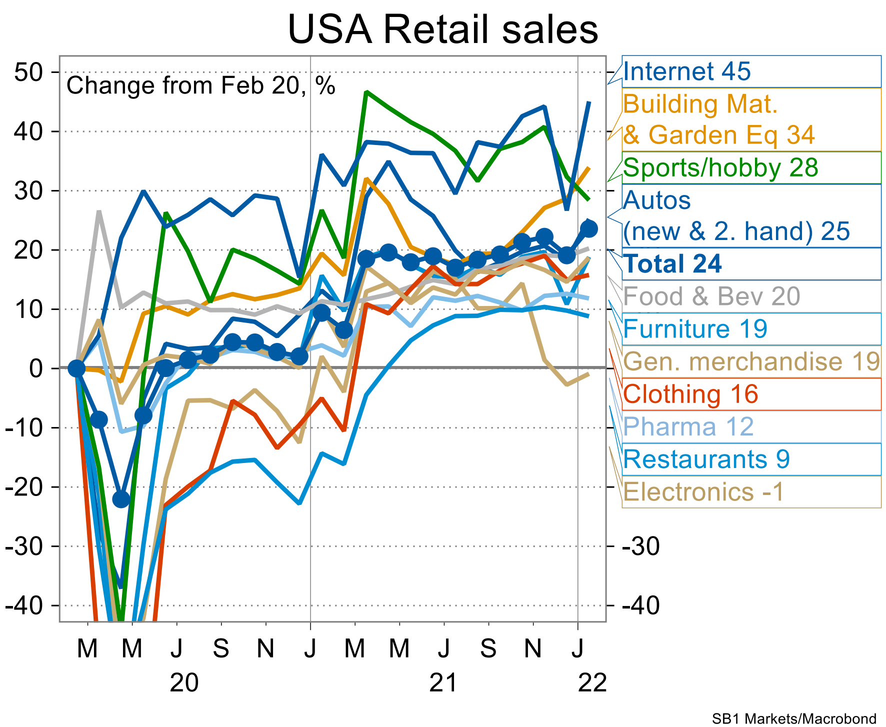


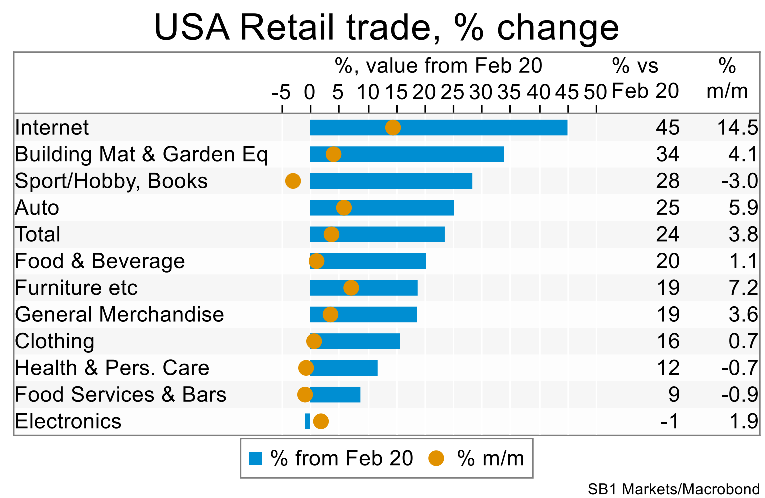


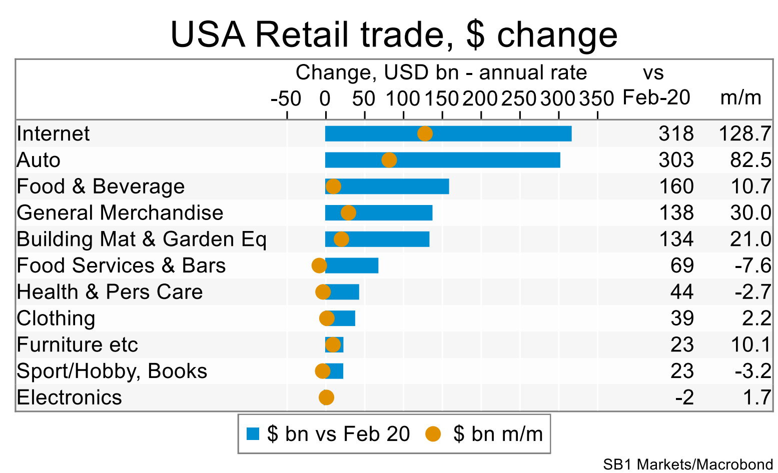
- **Total nominal sales** increased by 3.8% in January, following the 2.5% decline in December, revised from -1.9%, expected up just 1%. Thus, the level was far above expectations. Net sales rose sharply in Jan following the drop in Dec. Just 3 of 11 kind of stores reported a decline in sales in Jan
  - Total nominal sales are up 24% - twenty four per cent – vs. the Feb 2020 level!
- **Core sales of goods** (=control group, excludes autos, gasoline, building materials & restaurants) rose 4.8% in Jan, expected up 1%. Dec was revised down to -4.0 from -3.0%. We estimate a 4.3% monthly gain in January, measured in volume terms. Sale volumes are up 19% vs. the Feb-20 level, and 7% above a strong pre-pandemic 5% trend growth path
- **Consumption of goods** is very likely well above a sustainable level, and we still expect sales to decline the coming months/quarters – even if parts of the adjustment (vs. a long term growth path) already has taken place

Most sectors reported higher sales in January, following a weak December

Just sport/hobby (from a high level), restaurants (Omicron) and health down in January







Last month

- 8 out of 11 main sectors reported higher sales in Jan, just 3 lower sales
- Net sales rose 14%, following a large decline in Dec

Since pre corona: Electronics down, all others are up

- **Net** sales are up 45%!

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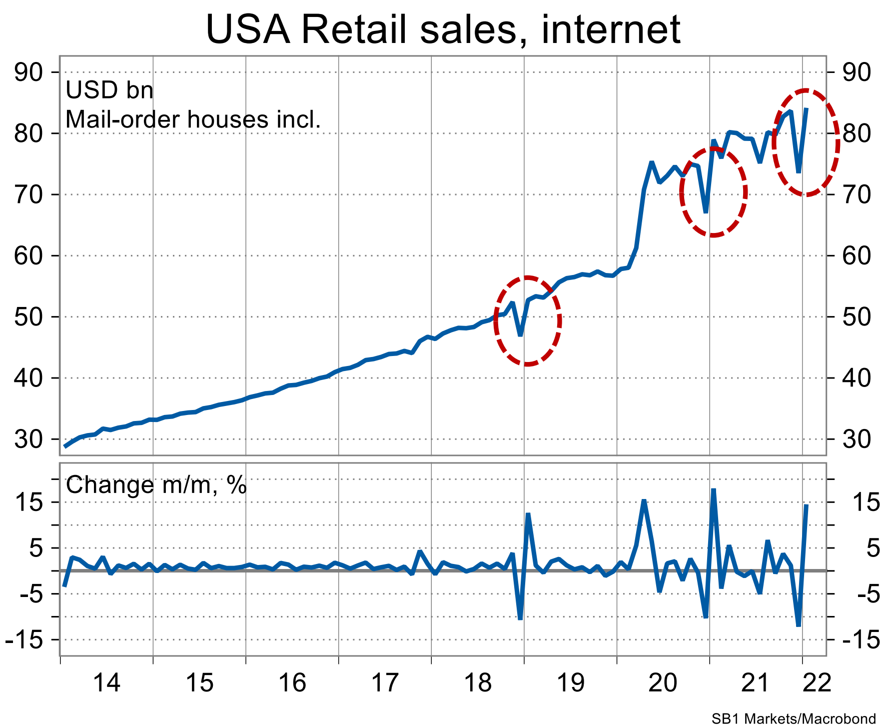
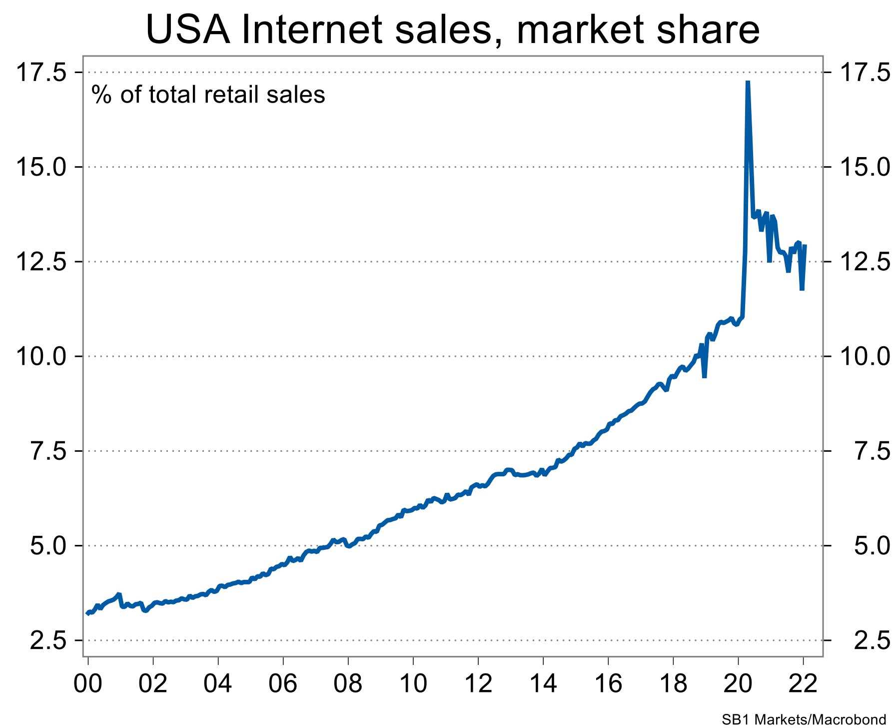
A new seasonal pattern underway in net sales? A ‘V’ in Nov-Jan 3 of 4 last years

As we expected one month ago, net sales recovered in January

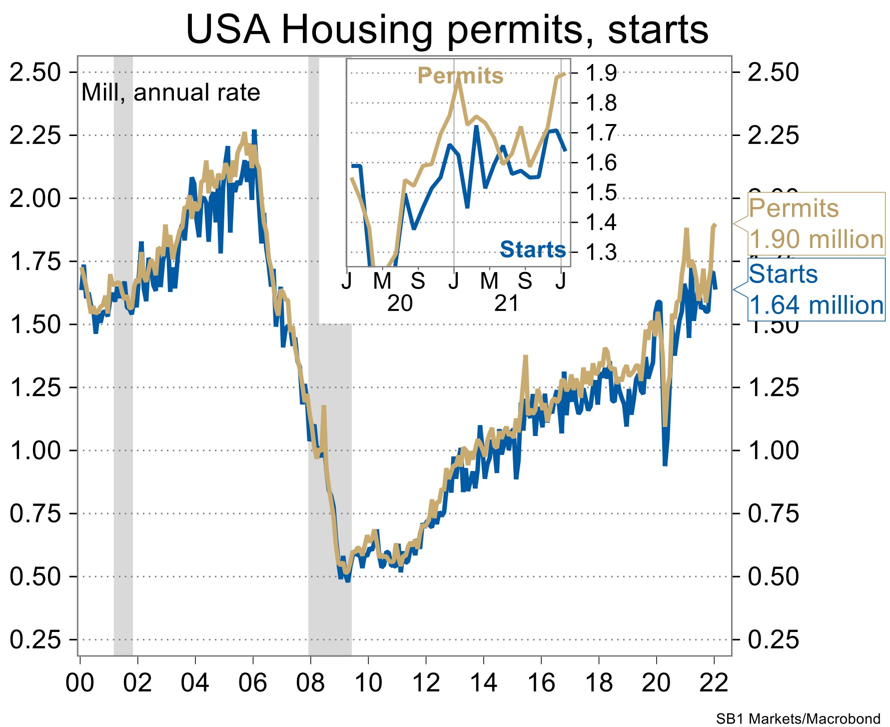


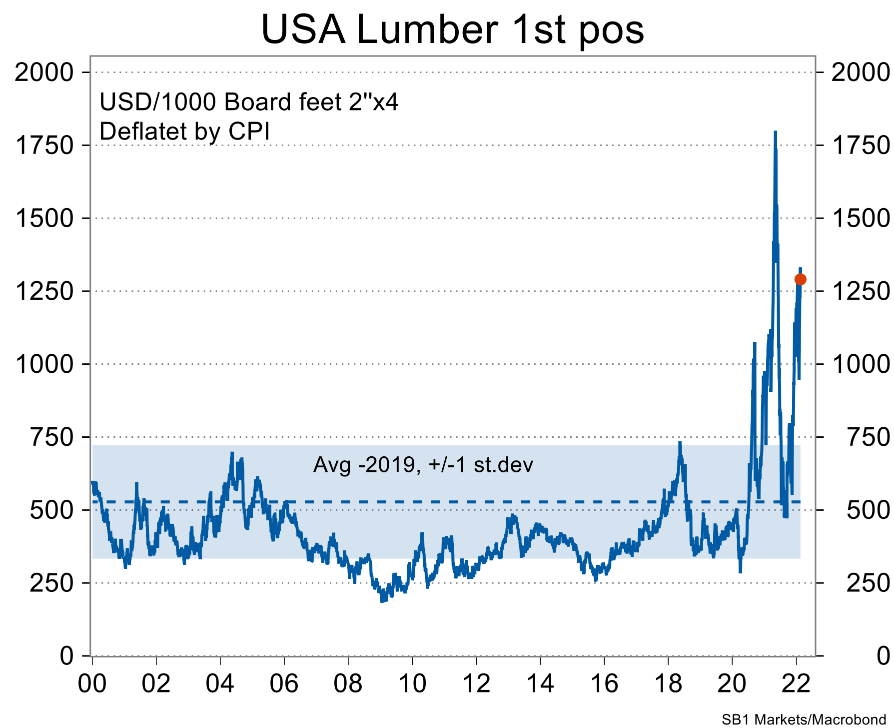


- Anyway, the internet sales market share (vs. total retail sales) has returned to the pre-pandemic trend growth

Housing starts down (weather/Omicron) but permits further up, best since 2006

… and the latter data point is the important one!

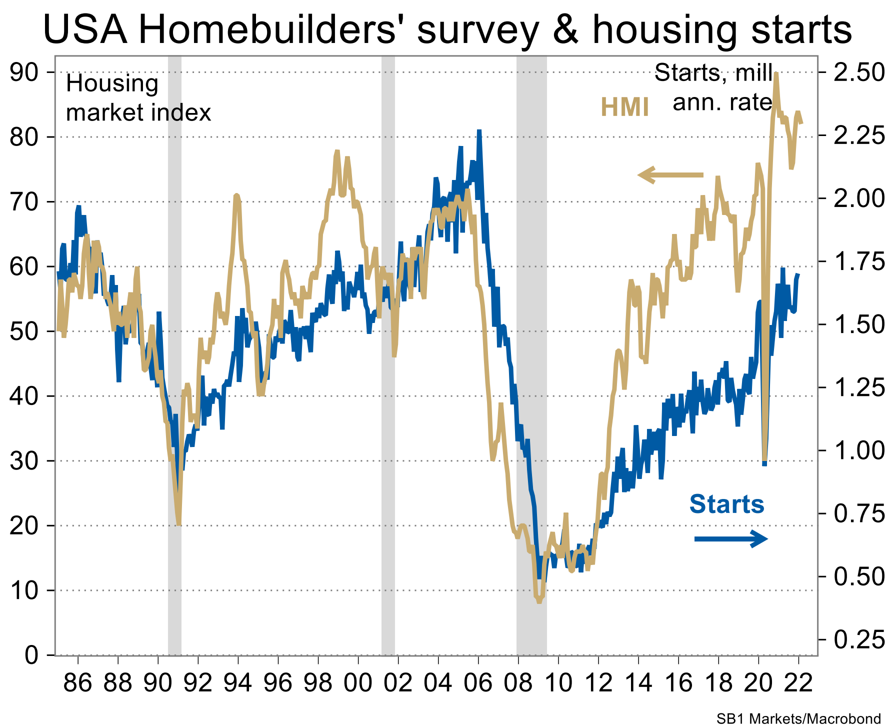


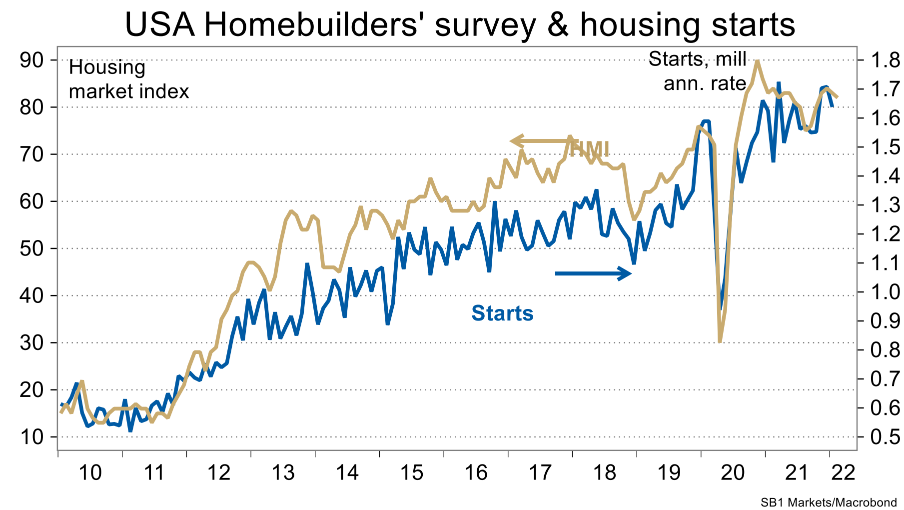


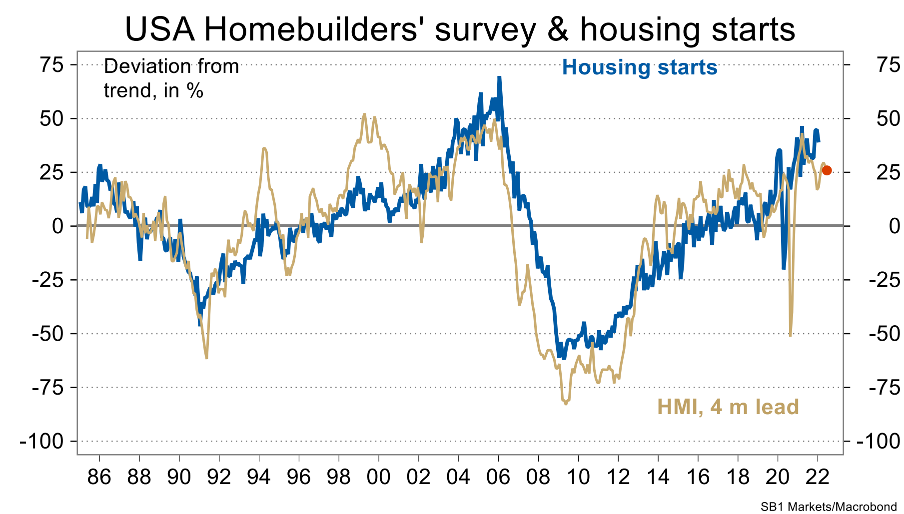
- **Housing starts** fell to 1.60 mill in Jan, from 1.71 mill in Dec, expected close to unch. Starts have been more or less flat through 2021 but the 3 past months are clearly up vs. the 2021 average
- **Building permits** rose to 1.90 mill, up from 1.89 in Dec, expected 7% down to 1.75. The Jan print is the highest since 2006!
- **Given the strong end of the year, the trend is still slightly up.** The level is some 10 – 15% above the pre-pandemic level. However, given the incredible strong existing home market, and soaring prices, starts should normally have strengthened further, amid still moderate mortgage rates and a recovering economy
- **Supply & capacity problems and higher cost** in the building sector may explain the lack of response. Lumber (2’’x4) prices are still unusually elevated, at 2.5 x the average price

Homebuilders' market index one more tick down, the level is high…

Still, the index does not signal an further increase in housing starts



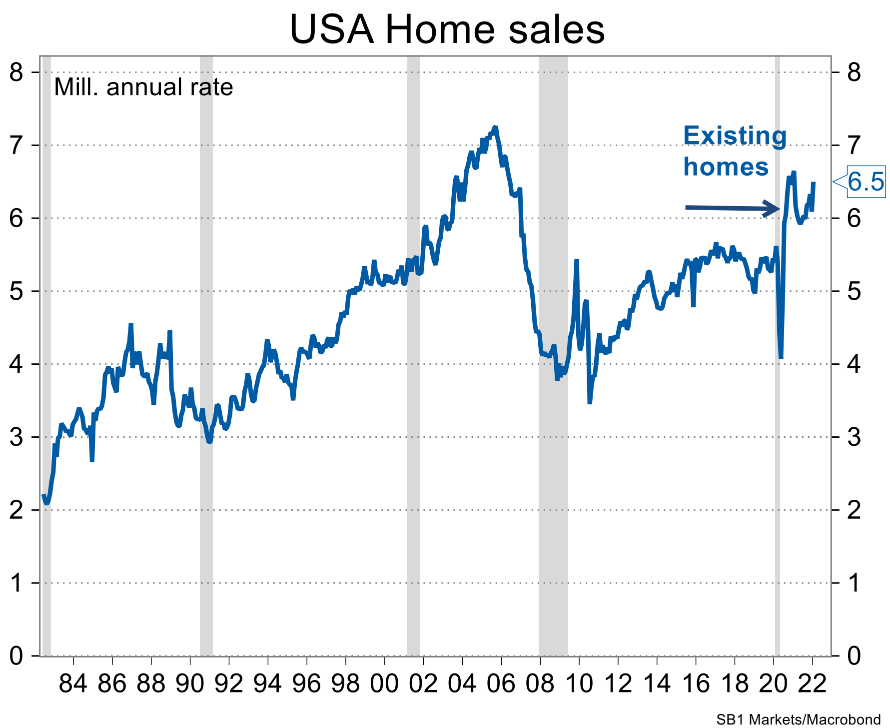


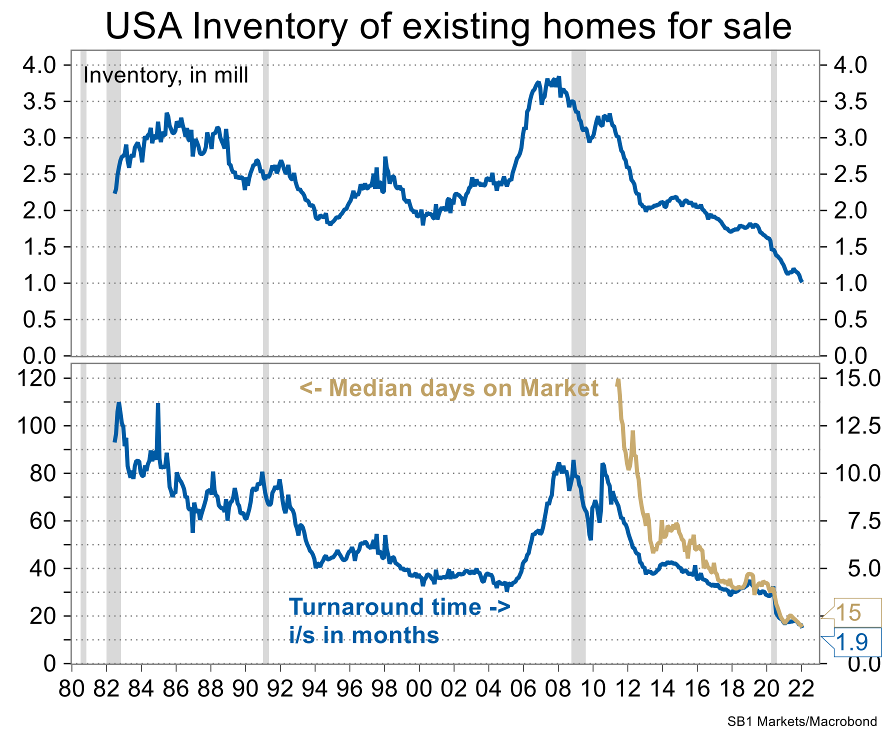


- **The Homebuilders' Housing Market Index** lost 1 p to 82 in February, expected unch. The level is high but still down from 90 last Nov. Traffic of prospective buyers and expected sales slowed somewhat
- **Rising material prices, supply chain and labour shortages are still** creating challenges for the home builders, according to the NAHB – but those shortages may have peaked (even of lumber prices are soaring again!)
- <u>Even if the index level is very high, the HMI does not signal higher housing starts, ref. the chart on the bottom right</u>

Existing home sales sharply up in January, the inventory at ATL

Prices inflation has slowed but remains at 15.7% y/y

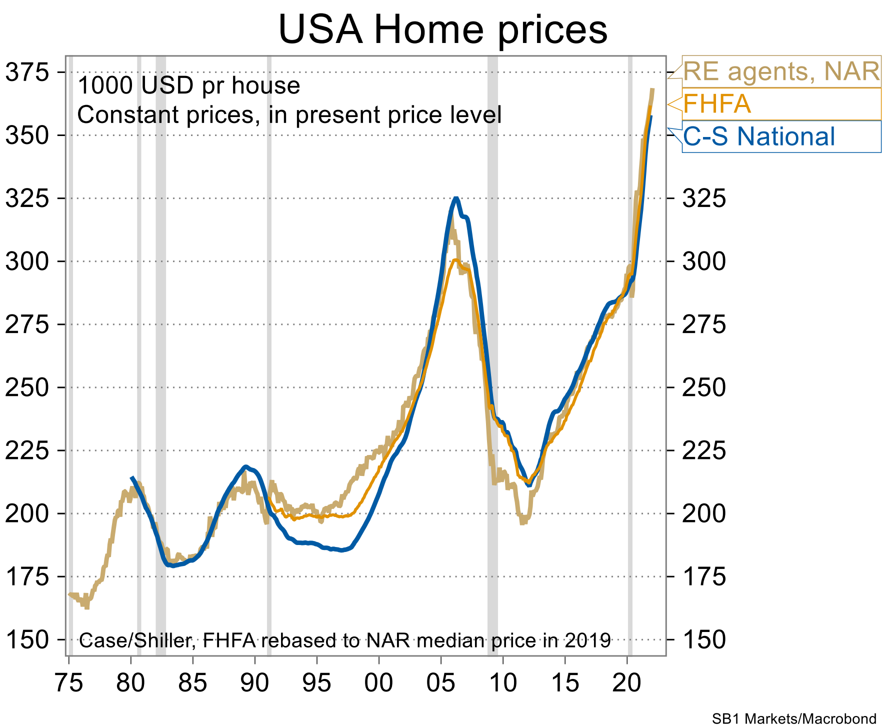


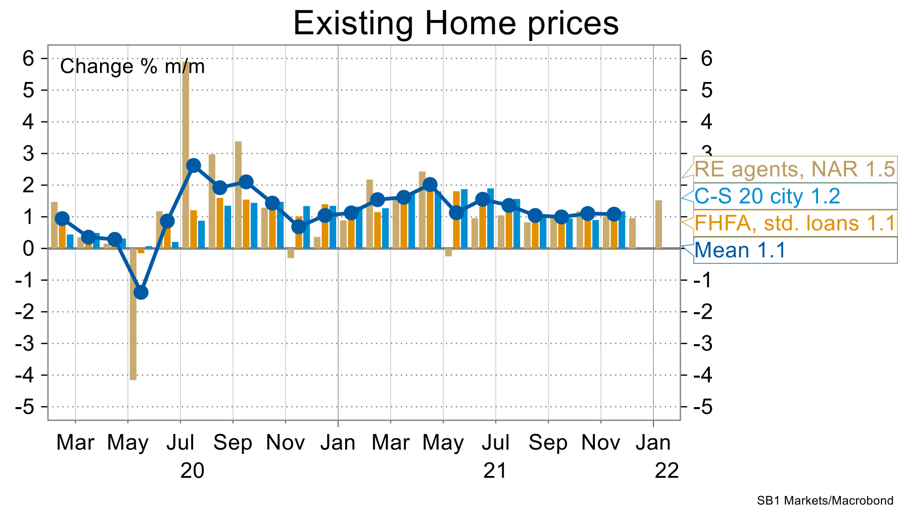


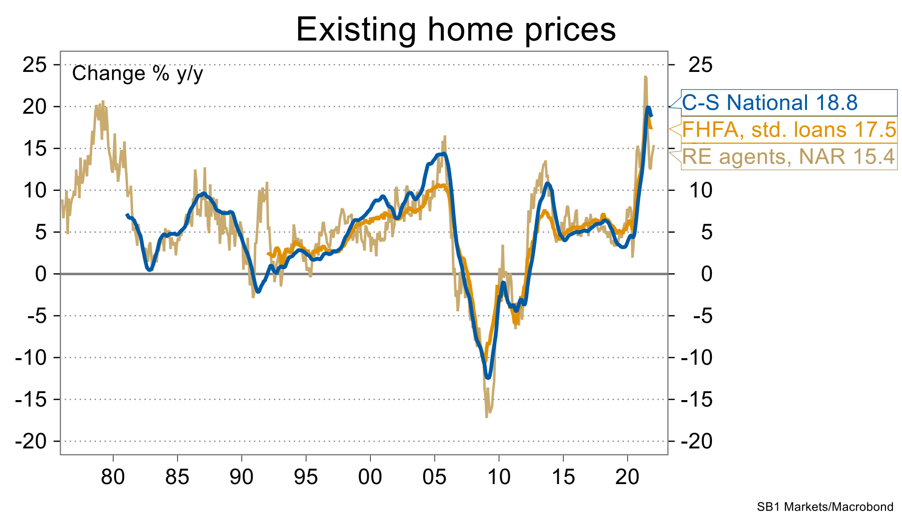
- Sales of **existing homes** climbed to 6.50 mill (ann. rate) in Jan, from 6.09'', expected 6.10'' (down from prev. reported 6.18''). Sales are down just 2% from the local peak in late 2020, and are 20% above the pre-pandemic level – and not that far below the ATH level at 7.26 mill in Sept 2005
- **The inventory of unsold homes** fell further in Jan, to another ATL.
  - The inventory equals 1.9 months of sales. During the 2005 boom, the i/s ratio was 4 months, in bad times it has been as high as 10 months
  - The median time on the market for those homes sold is just 15 days, down from 30 days before the pandemic (and 120 days in 2011!)
  - No doubt, the lack of supply keeps the number of transactions down
- **Prices** rose 1.2% m/m in Dec, up from 1.0% in Nov. The annual rate accelerated almost 1.7 pp to 15.7%. At the peak, prices were up 23% y/y

Existing home prices up 1.5% m/m in Jan, the fastest pace since last April

Peak inflation may still be behind us, after a 30% lift since before the pandemci



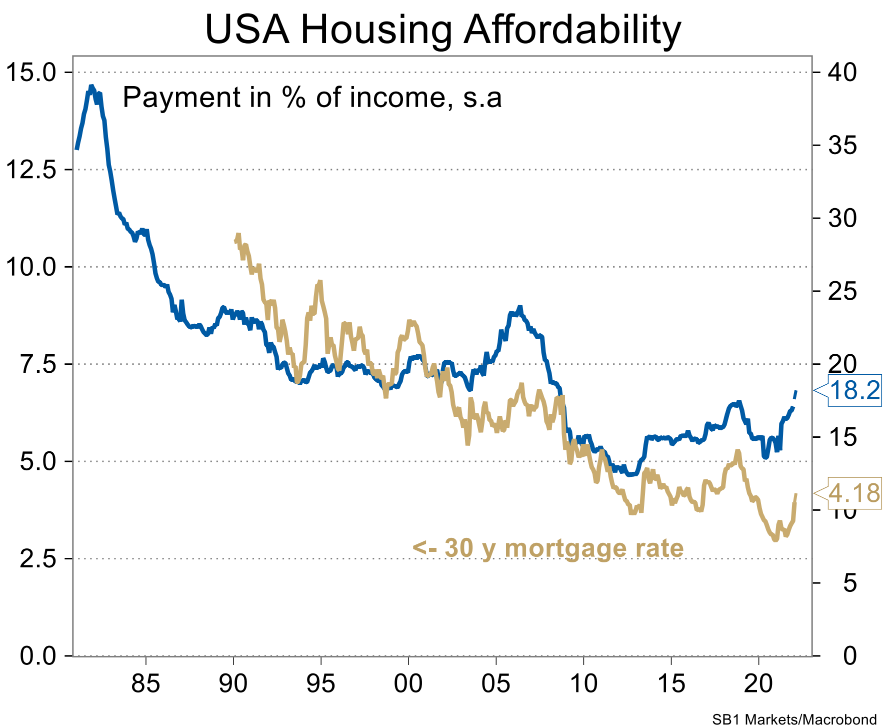


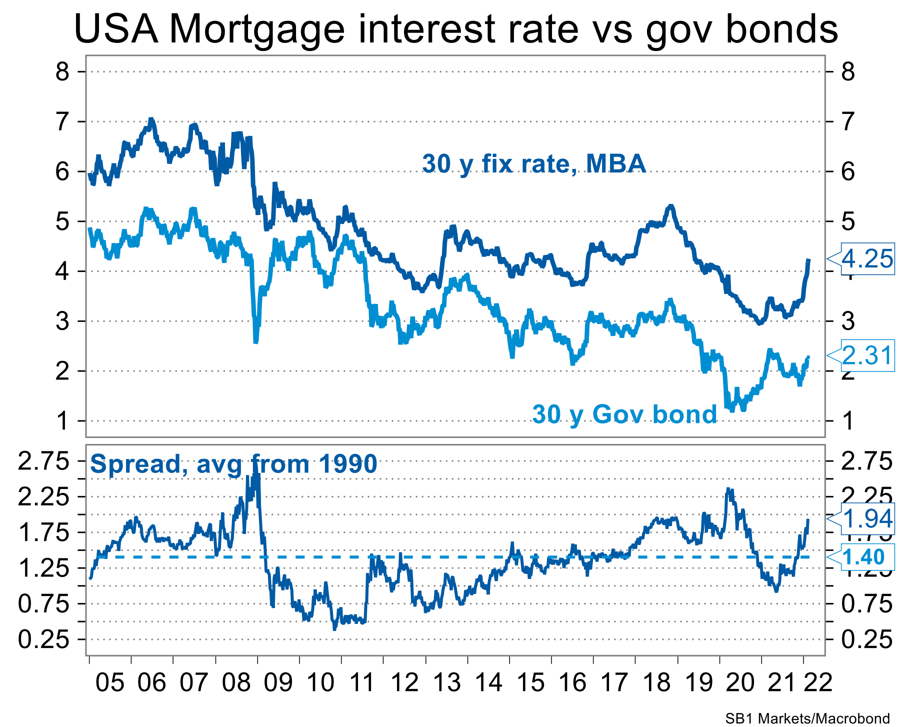


- **Prices** rose 1.5% m/m in Jan, according to the realtors – up from downward revised 1.0% in Dec. The annual rate rose to 15.4% from 14.7% (revised down 0.7 pp)
- **Other price indices** confirm a red hot housing market; prices are rising extremely fast – even if the peak rate of housing inflation is very likely behind us. Prices are up 30% vs. the pre-pandemic level – and the real price level is far above the 2005/6 peak

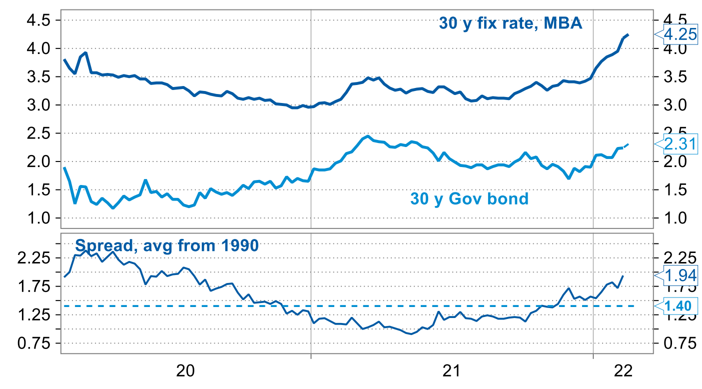
Prices are up 30% since before the pandemic, the mortgage rate is higher

So the affordability is not where it used to be. That is, it is still lower than anytime before 2008



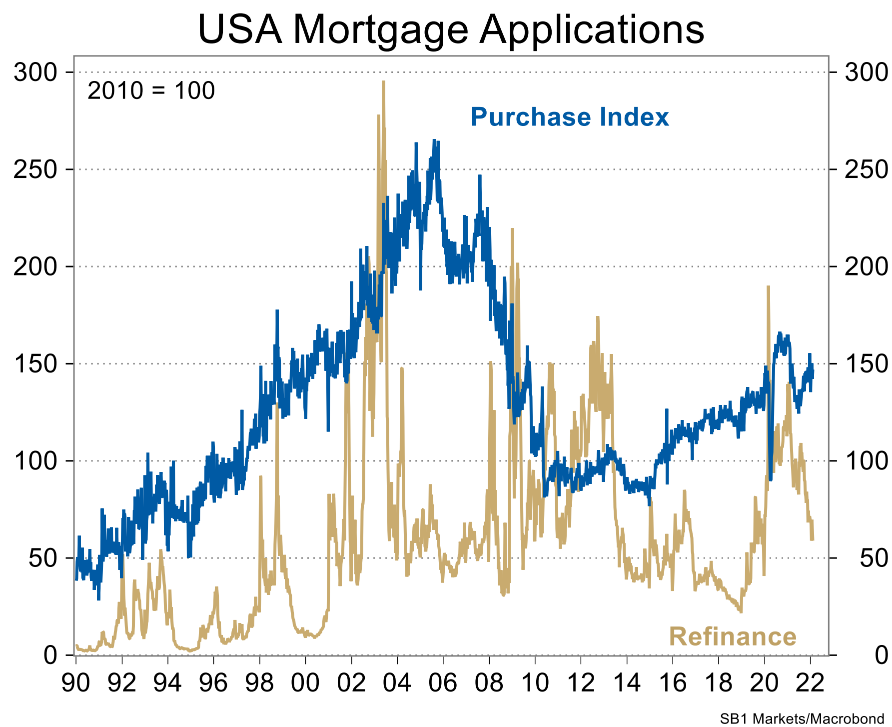


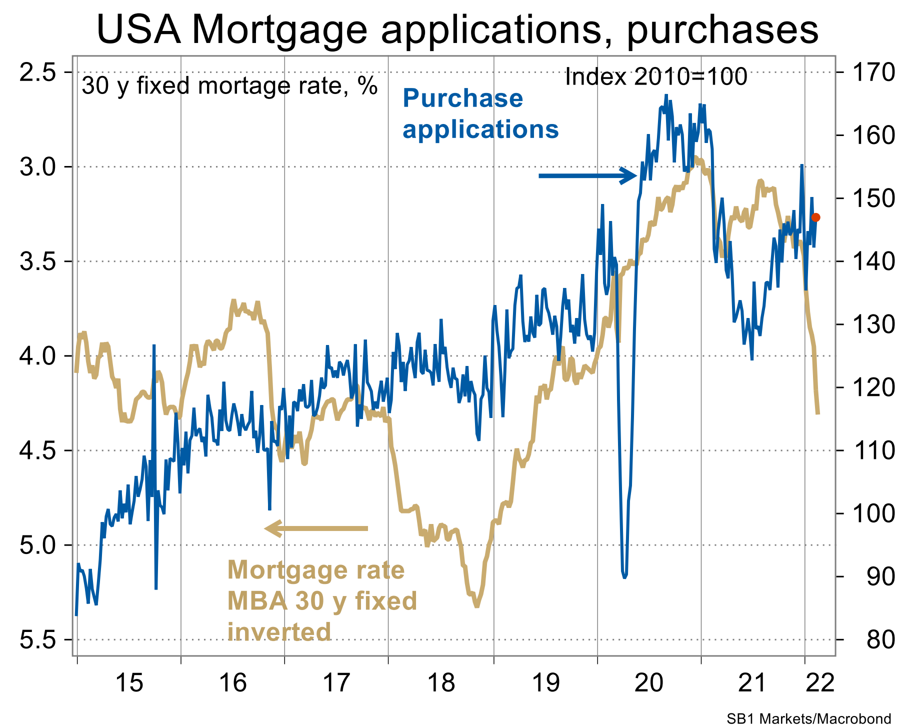
- **The 30 y fixed mortgage rate** has climbed to 4.25% from 3.0% last summer
  - » **The** rate has increased MUCH more than the 30 y Gov bond rate. The spread has widened to 194 bps from 91 at the bottom last spring (and by more than 30 bps last month) and it is now above the 140 bps average
- The **Federal Reserve** is now rapidly tapering off its buying of mortgage backed bonds – and signals eagerness to reduce its holdings, which very likely explains the steep increase in the spread
  - » The central bank has funded most of the housing marked during the pandemic, at least until mortgage lending shot up through 2021



Mortgage rates are up – but demand for new mortgages is still strong

So far, home buyers does not seem to be scared by the substantial lift in mortgage rates

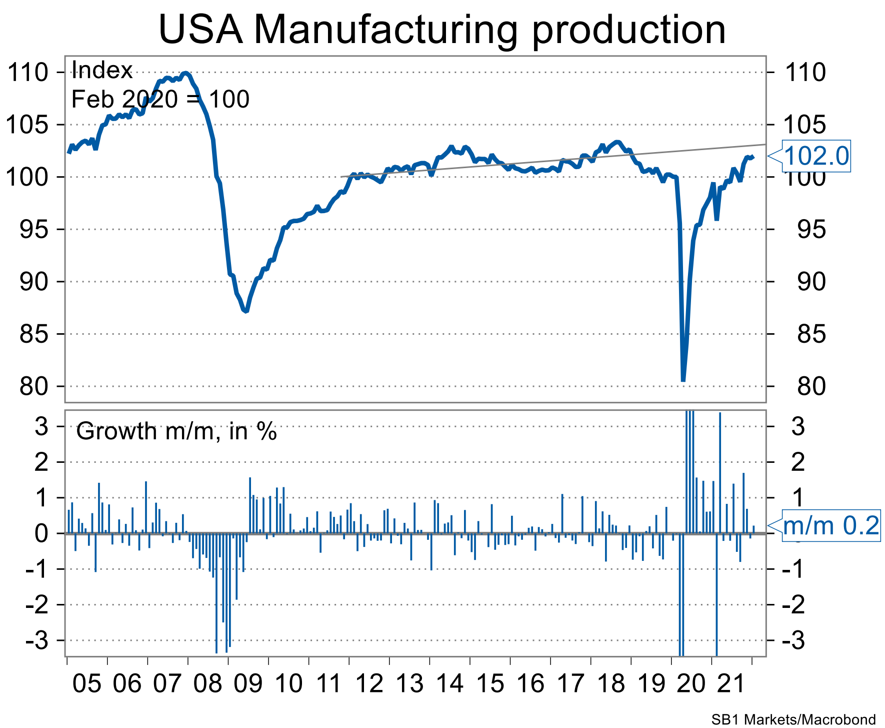


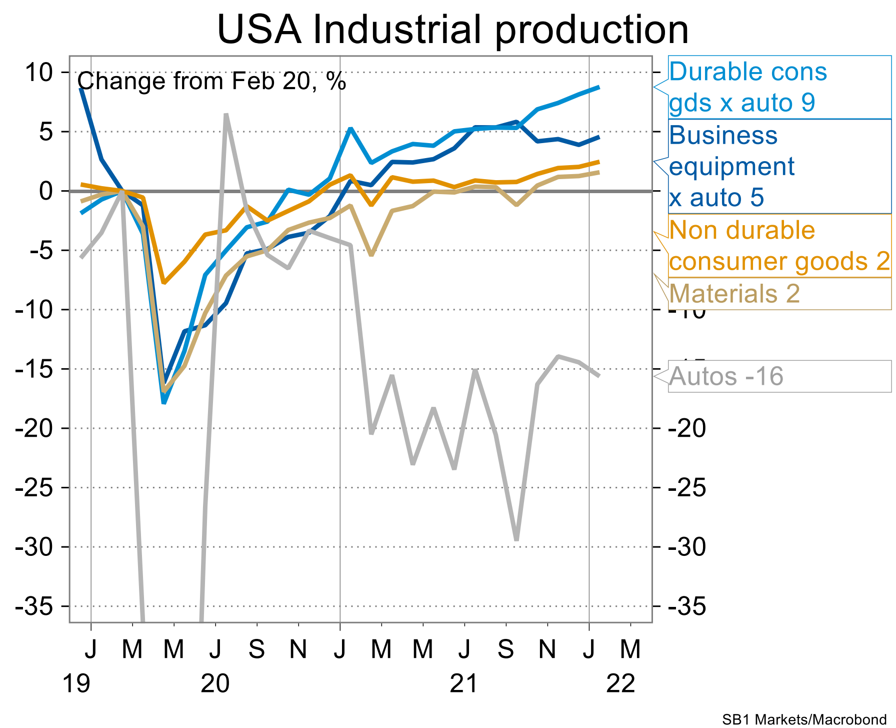


- Demand for new mortgages rose marginally last week but has not responded to the 40 bps decline in the 30-year mortgage rate since March – the no. of applications has fallen
- Demand for new mortgages (for buying, not refinancing) is not closely correlated to mortgage rates but the increase in demand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

Manufacturing production up 0.2% in January, up to 2% above the Feb-20 level

Auto production is still lagging, slightly down in both Dec & Jan

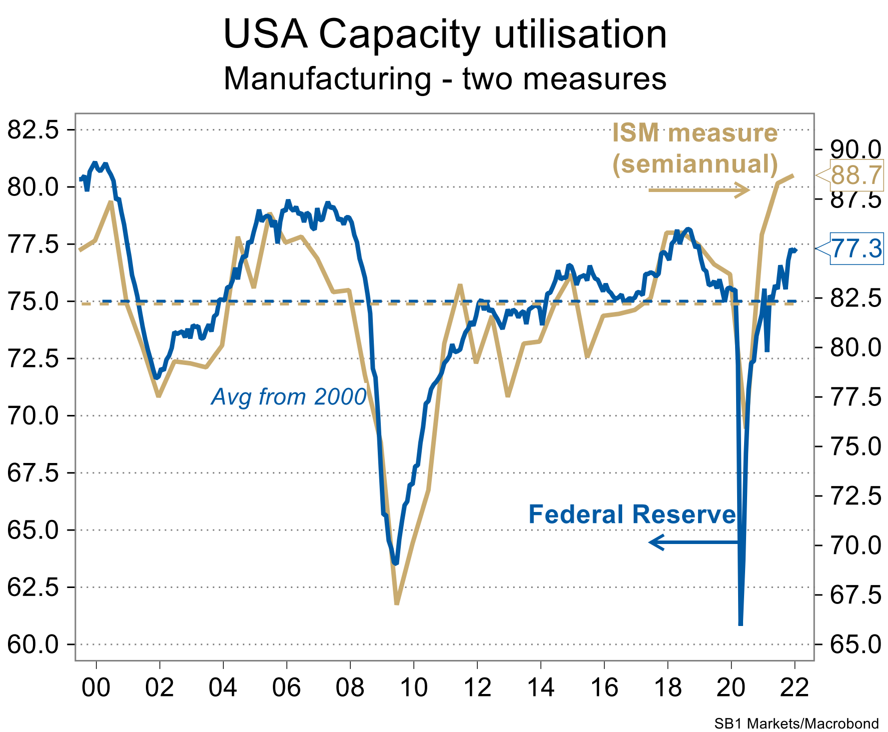




- **Manufacturing production** was expected up 0.3%. However, as Dec was revised up to -0.1% from -0.3%, the 2 last months were a tad better than expected
- **Manufacturing production** is trending upwards – but is still just 2% above the level before the pandemic. Surveys signal continued growth
  - » The steep decline in auto production has been a drag on overall production in 2021
- **Total industrial production**, including utilities, mines/oil production rose 1.4% m/m expected up 0.5%
- **PMI/ISM and all other surveys** signal a continued recovery
- **Capacity utilization** rose in January and is above average. The ISM survey reports a record high utilization, check next page

Capacity utilisation high or record high

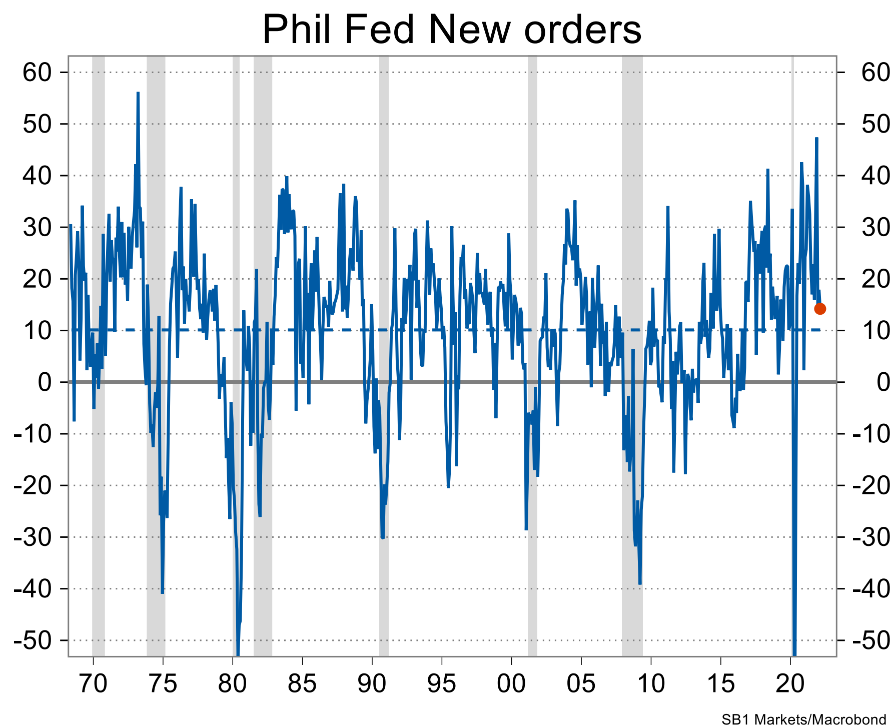
Not an irrelevant question

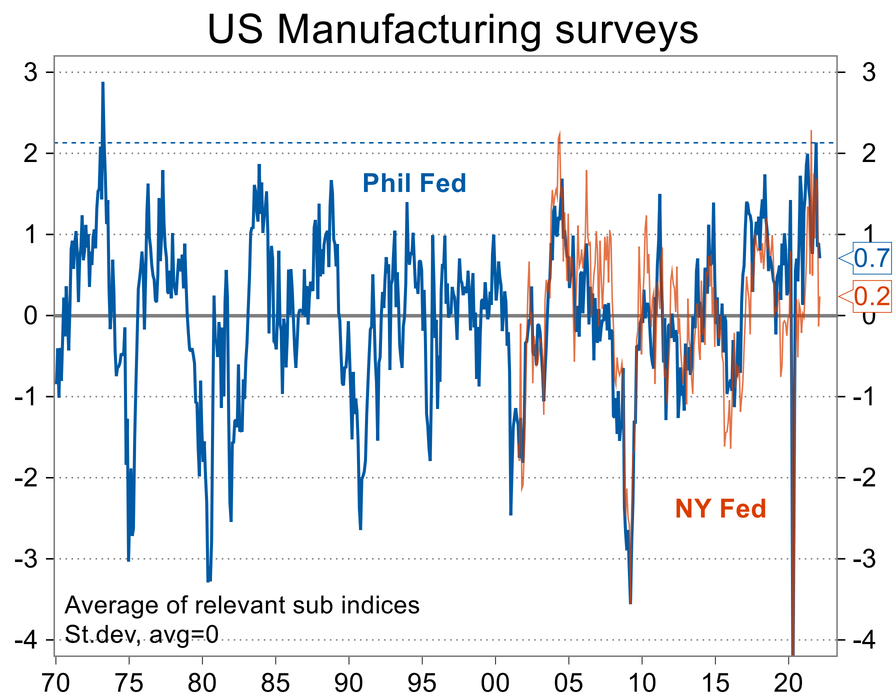


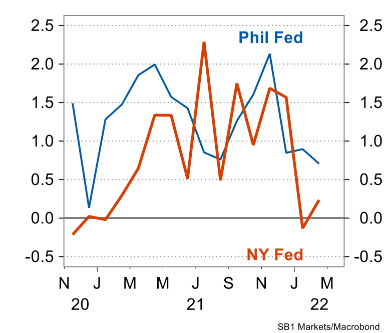
- **The Federal Reserve's** measure now yields a capacity utilisation at 77%, vs. the long term average at 75%
  - » 77 – 80 are booming times
- **ISM's semi-annual** survey reported a further increase H2/Dec, to another ATH at 88.7% vs the average at 82.5%
  - » These two measures have not been 100% correlated but the current discrepancy is large – and quite important when assessing the growth outlook
- The Fed's estimate is model based, while the ISM survey is based on companies assessment of their own capacity utilisation
- Given reports on labour shortages, material shortages, prices, the ISM survey seems to give the most reasonable result

Both Philadelphia & NY Fed's manufacturing signal slower growth

Still, both are still reporting growth above average







- Phil Fed: 16 in Feb, down drom 23.2 in Jan, expected 20.0
- NY Fed: +3 in Feb, from -0.7 in Jan, expected up to 12
- No reason stated for the rather unusual decline in the NY Empire Manufacturing Survey January. However, optimism remained elevated

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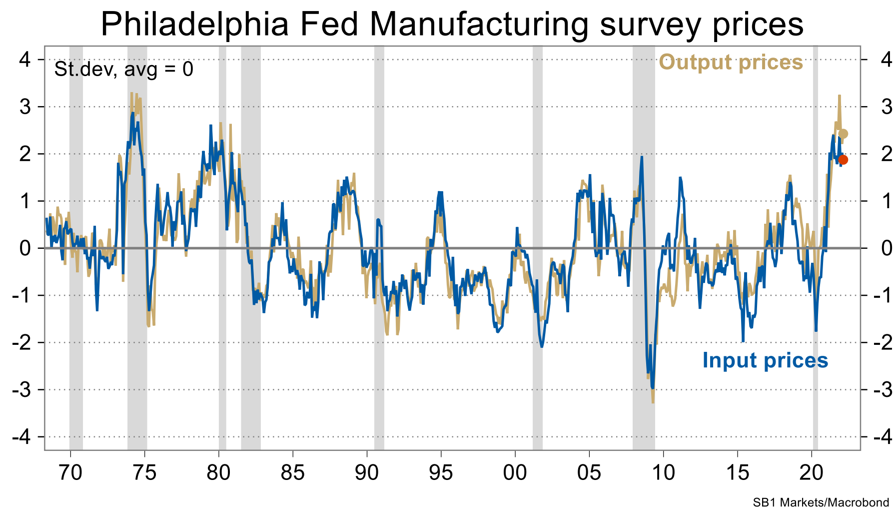
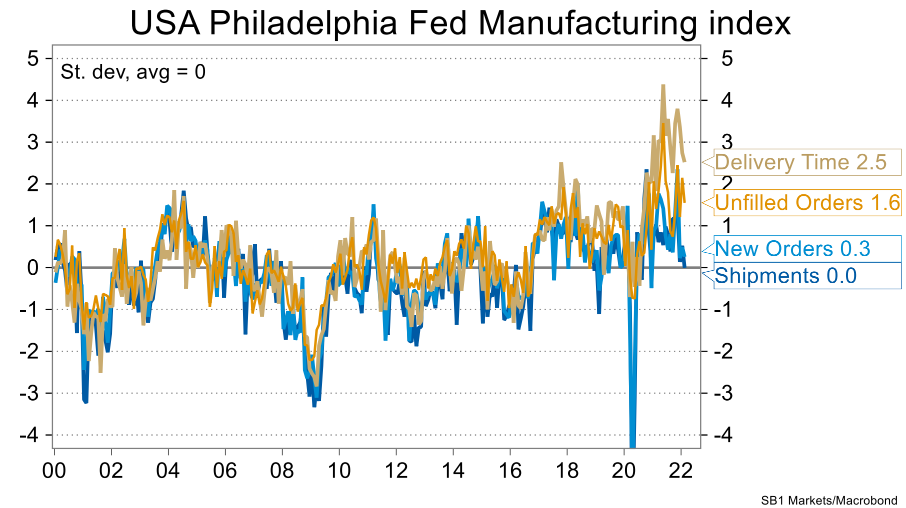
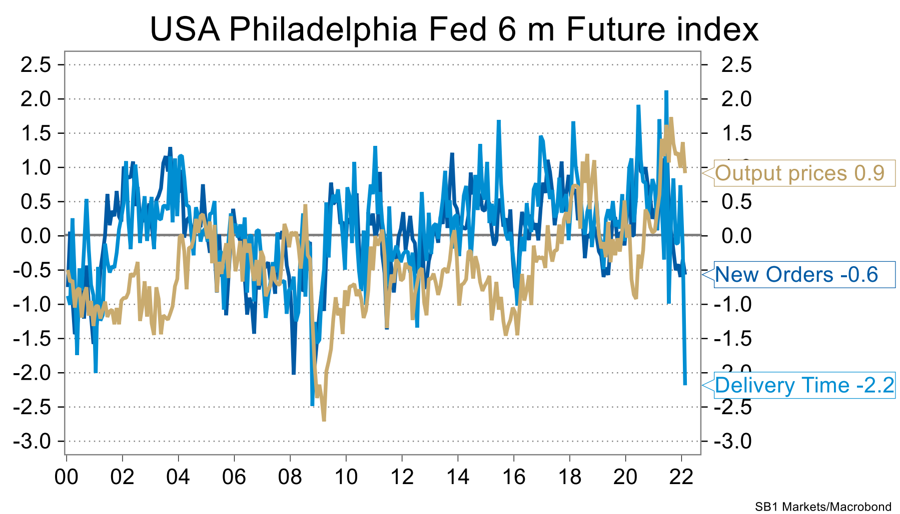
Phil Fed: Price pressures are very elevated – and are expected to remain so

… even if growth is expected to slow, and delivery times to 'collapse'







- The current prices increases are still very high, both input and output prices
- Order growth is slowing, so are actual shipments – but long delivery times (and lack of labour) may keep production in check, not demand – even if the new order component is weak too, the order reserve is still growing rapidly
- The outlook: Supply chains problems are expected to ease substantially but also the order inflow. Even so, output prices are expected to increase rapidly. A bit strange mix? Stagflation??

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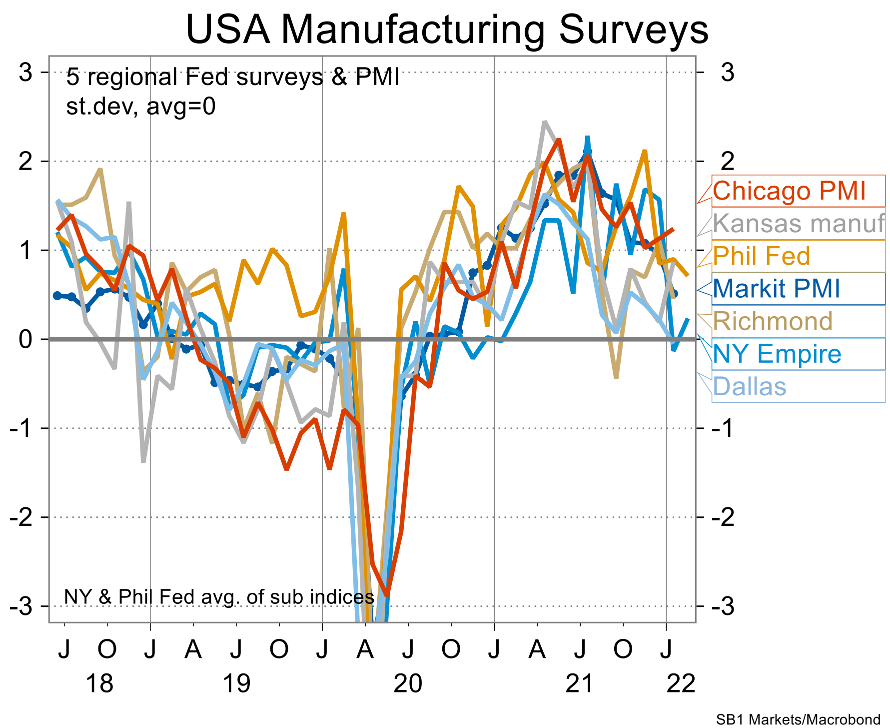
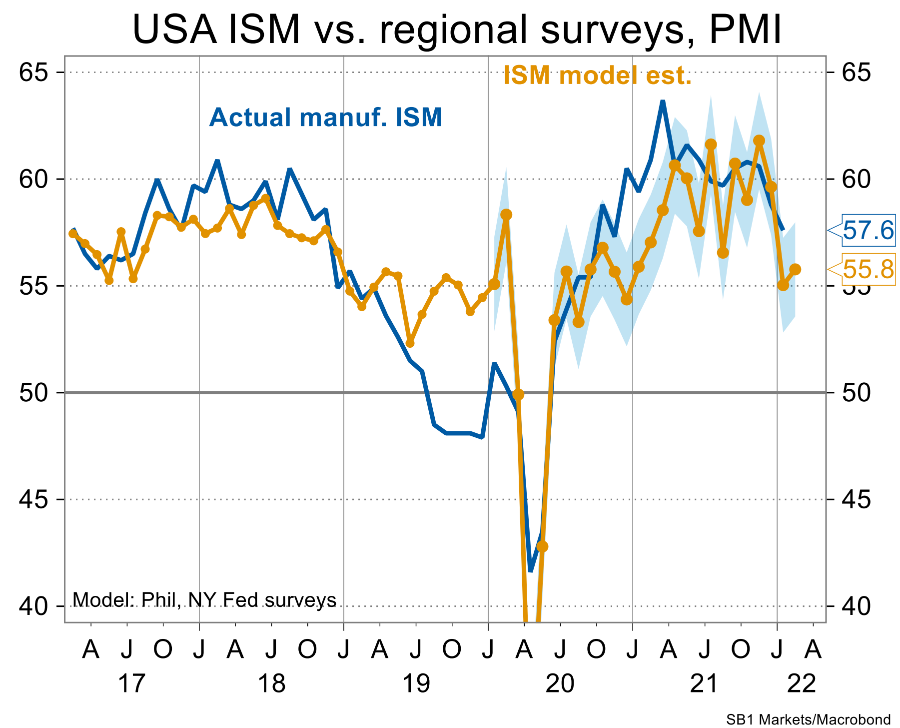
Manufacturing surveys so far in February: 1 up, 1 down.

The big picture: Surveys are heading down, growth is slowing





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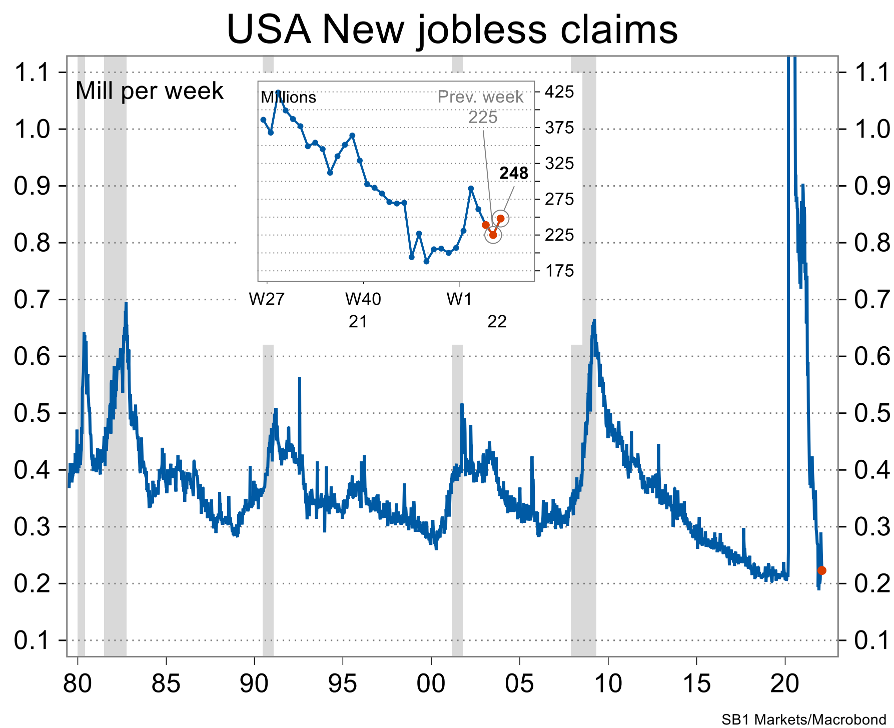
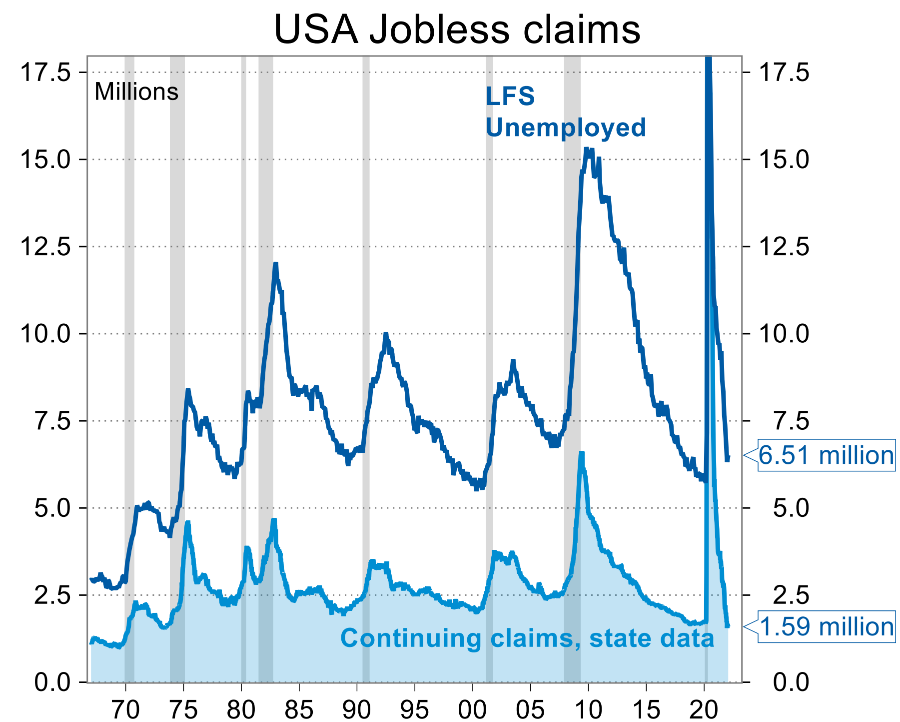
New jobless claims up last week but level still low

The level is still very low

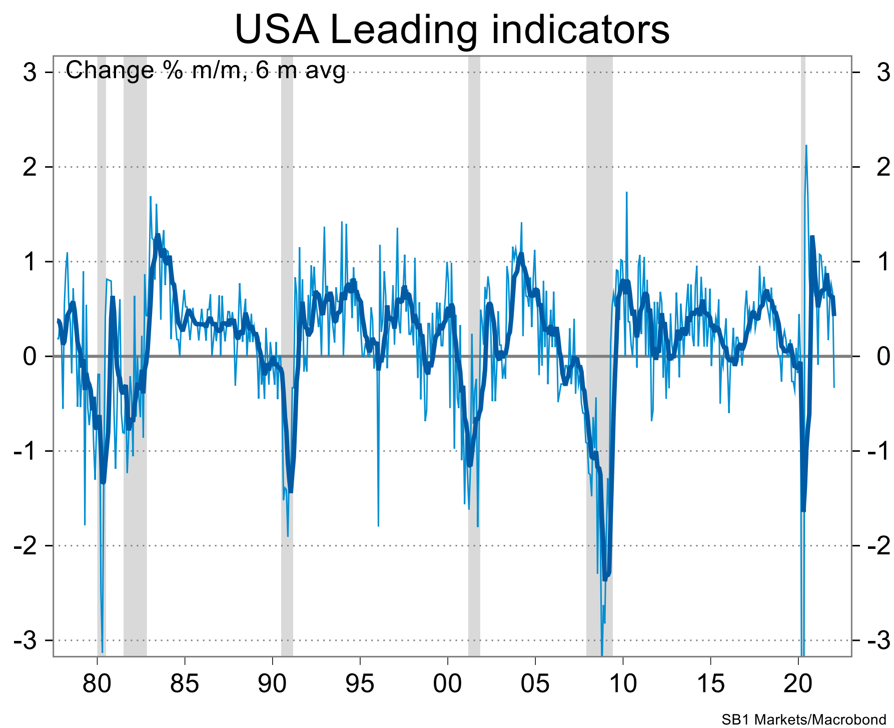




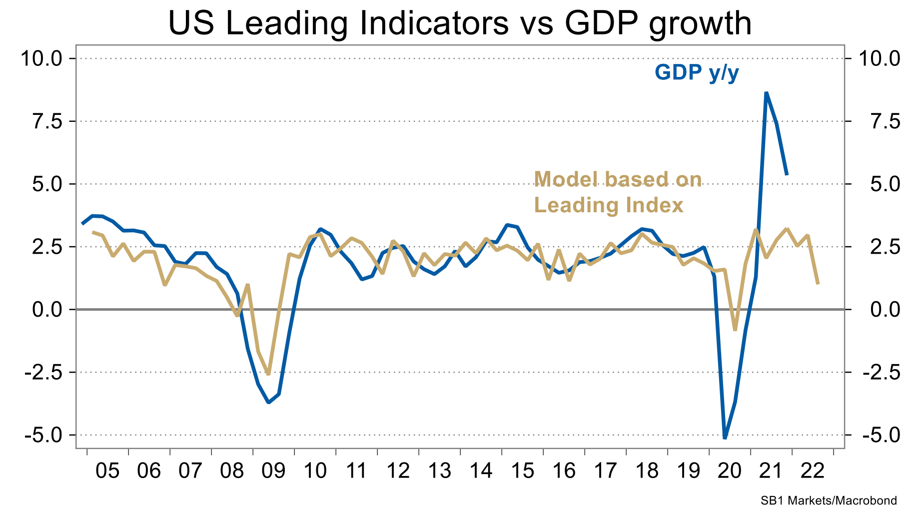
- **New jobless claims** increased 248' in week 6 from 225' the previous week. The inflow is still very low – but somewhat above the level last year
- **Ordinary continuing claims** fell by 0.2 mill in week 6, to the lowest level 1973!

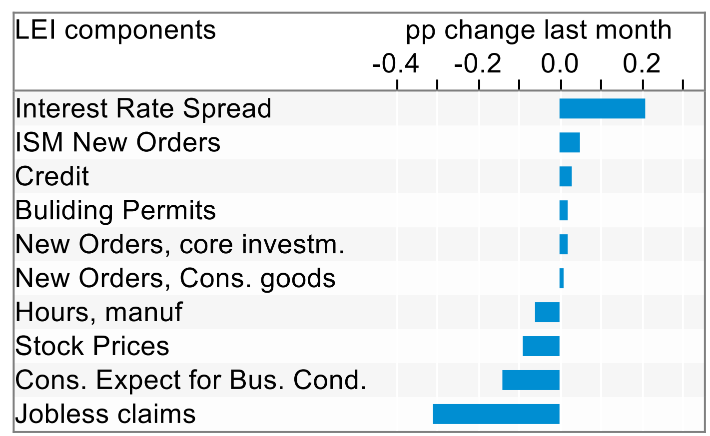
Leading indicators (Conference Board's LEI) in red in January

More jobless claims, weaker consumer confidence (vs businesses), and lower stock prices



- The index fell 0.3% m/m in Jan, expected <u>up</u> 0.2%, even if all components already are published
- One negative print does not make an recession (the LEI has turned negative ahead of all recessions)





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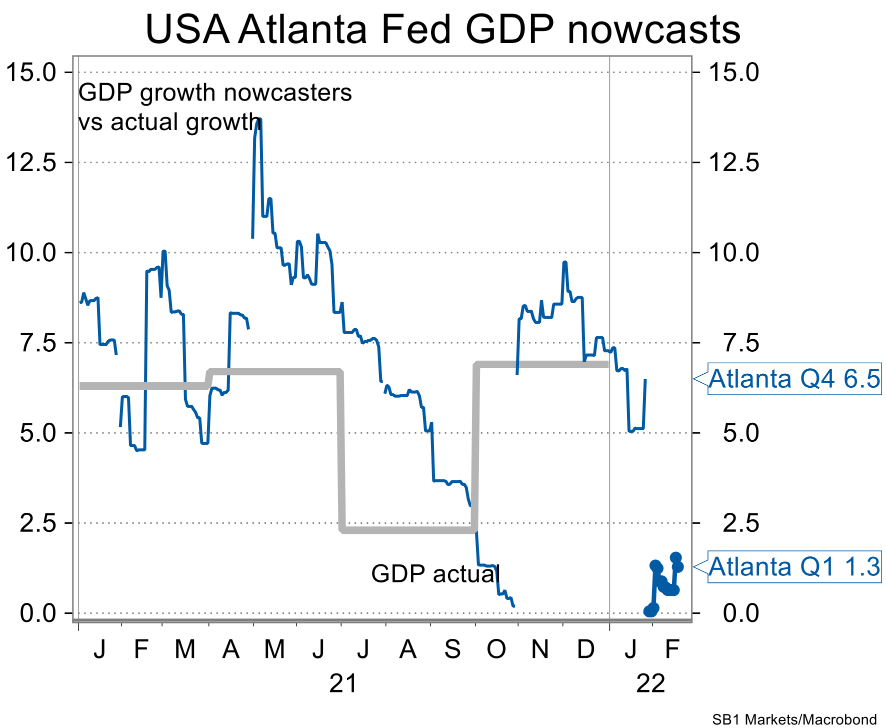
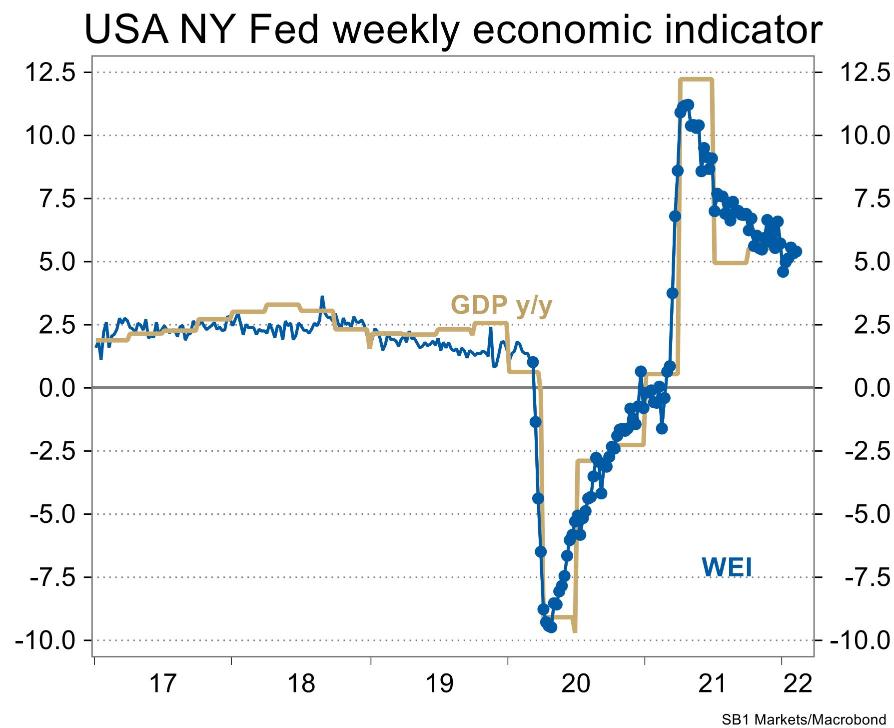
Atlanta Fed's nowcaster suggests 1% growth in Q1





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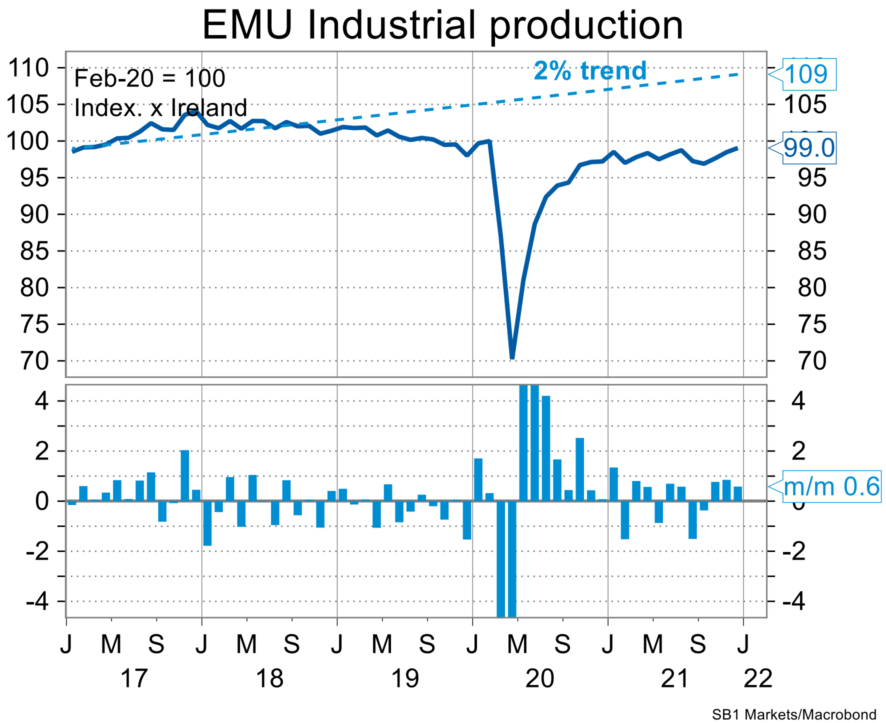
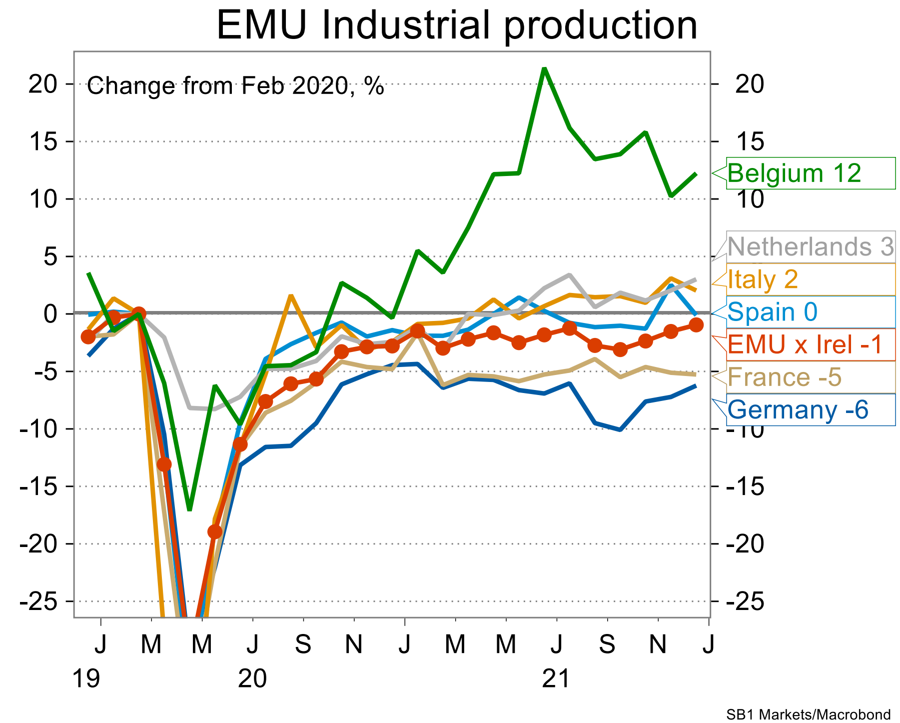
Industrial production up 0.6% in December, above expectations

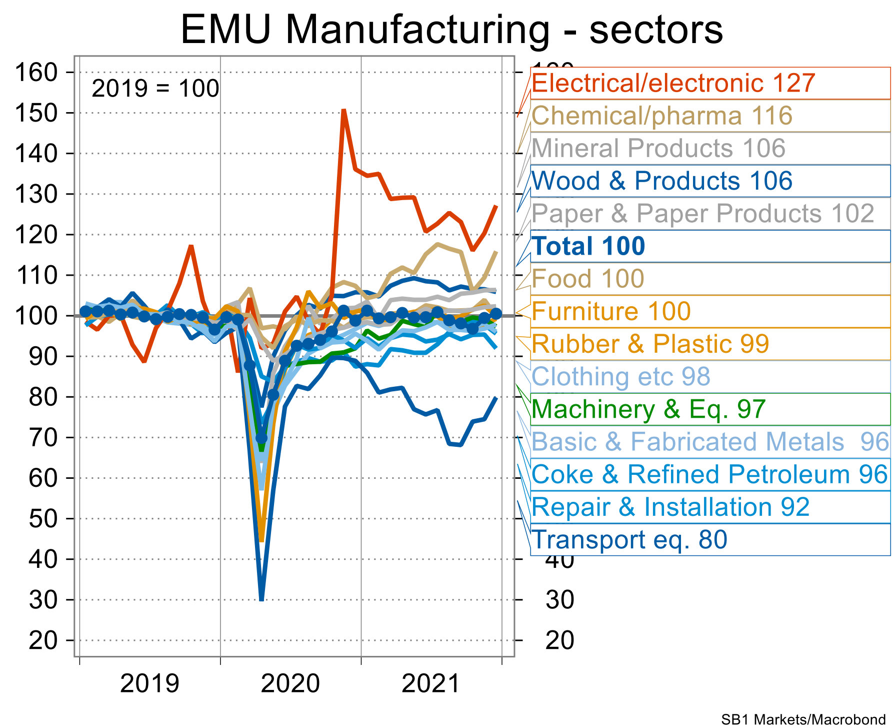
Production 1% below the pre-pandemic level but the trend through 2021 was not that impressive





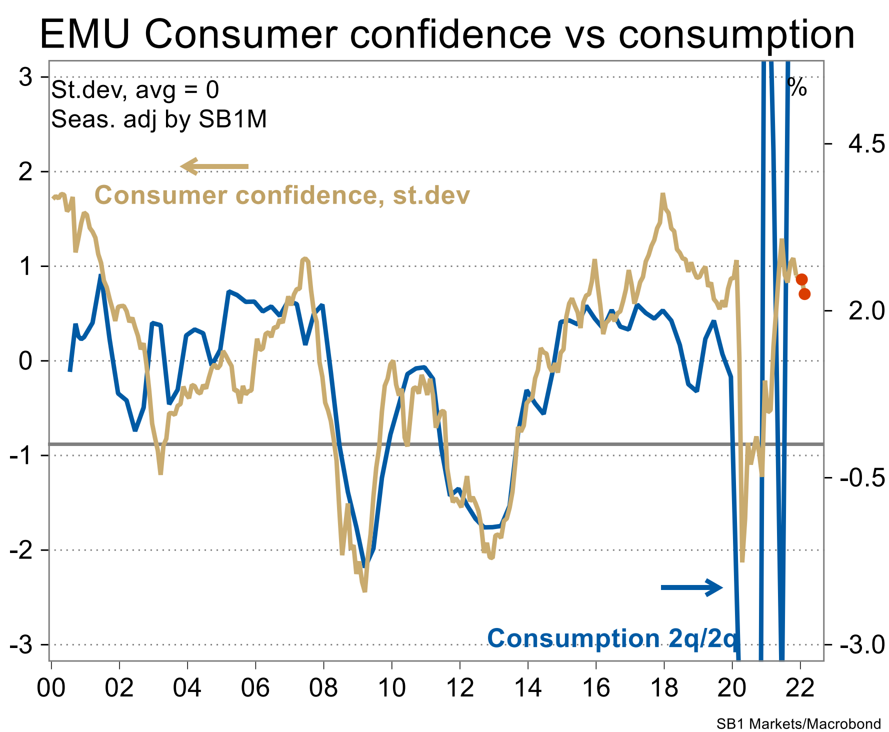
- **Officially,** production rose by 1.2% due to another hike in Irish production – which very likely will be reversed, as usual. The 'core' rose 0.6%
- **Germany** is still the laggard in EMU, due to the disastrous cut in auto production. Italy is in the lead among the big 4, 2% above the Feb-20 level
- However, **auto production** is finally recovering – and production rose by 7% m/m in December
- **Production in the EMU** has trended flat so far in 2021, even if surveys and new orders have signaled more than decent growth. The sharp setback in auto production explains much of the overall 'weakness'

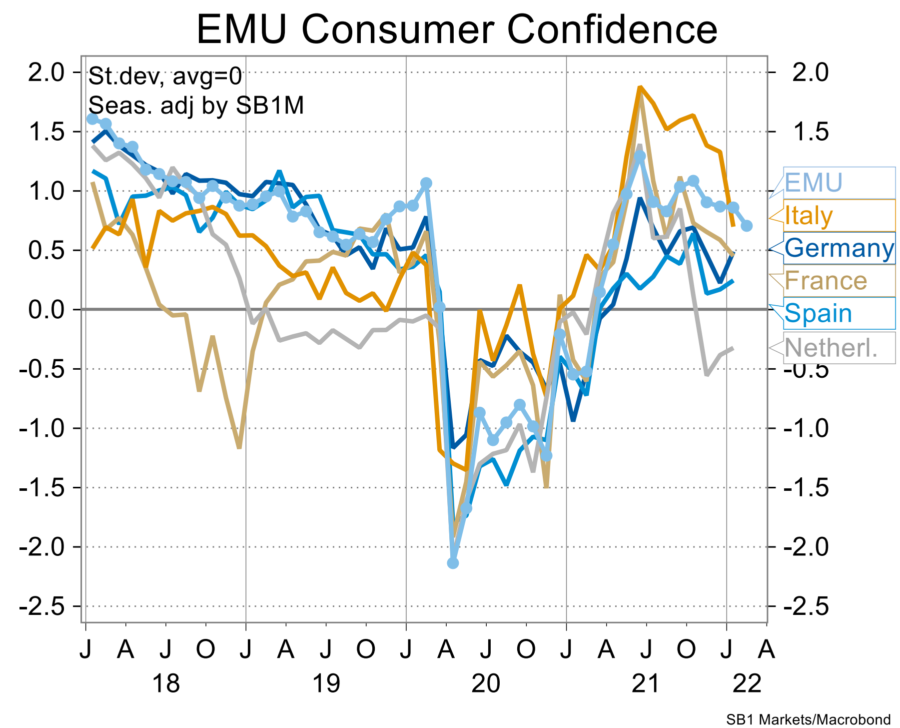
Auto production on the way back, still down 20%



The fight against the virus has not brought consumer confidence (much) down

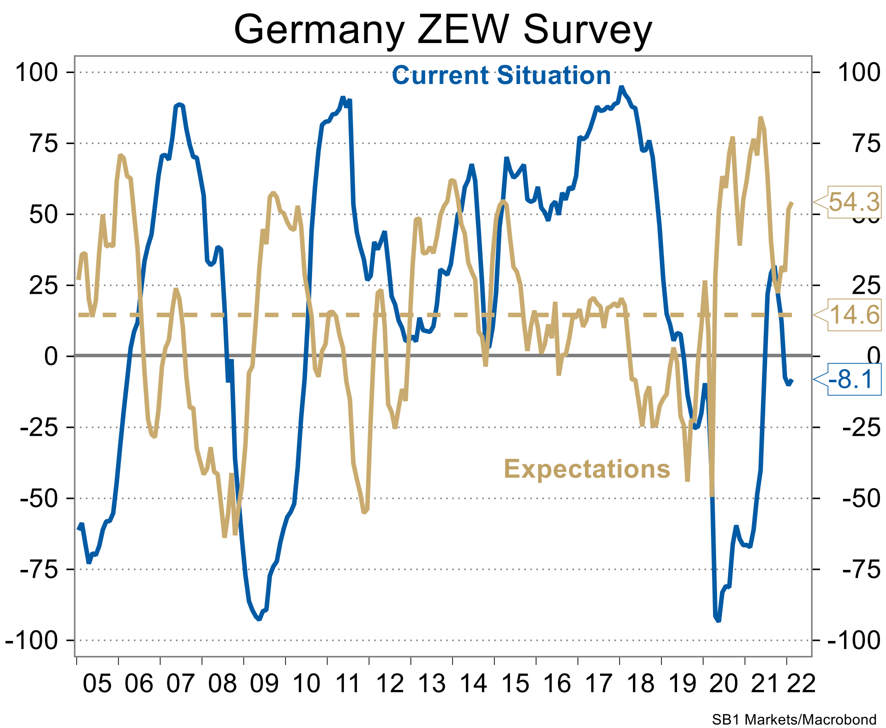
The level fell 0.2 st.dev to 0.7 st.dev above average. Households are not that worried





ZEW expectations further up in February – and the level is far above average

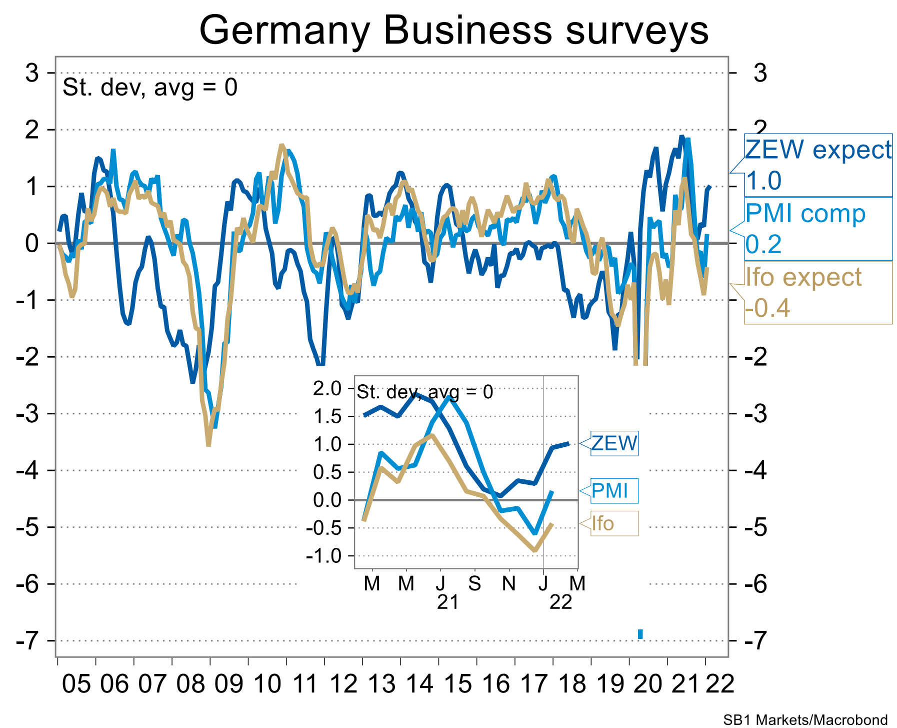
A strong light in the end of the tunnel, according to German analysts and investors



- The **ZEW expectation** climbed 2.6 to 54.3 in February, expected 55 – to 0.8 st.dev above average, following a steep increase in January
  - » The index signals GDP growth far above trend – some 3 – 4%
- **Assessment of the current situation** flattened – exactly at an average level
- **In sum:** Not that bad?

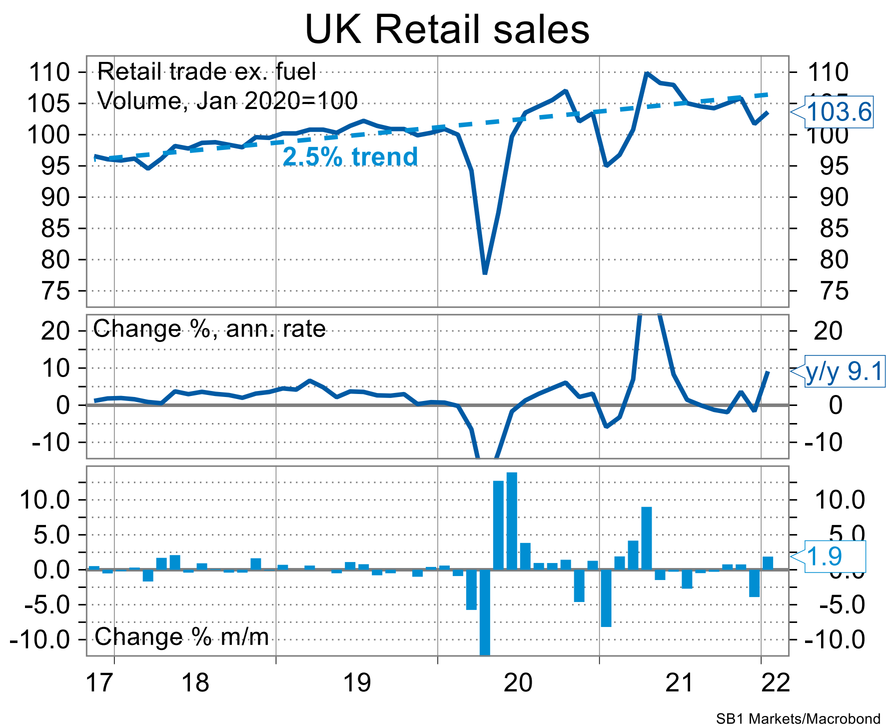
Just ZEW has reported Feb data but the two other main surveys also rose in Jan

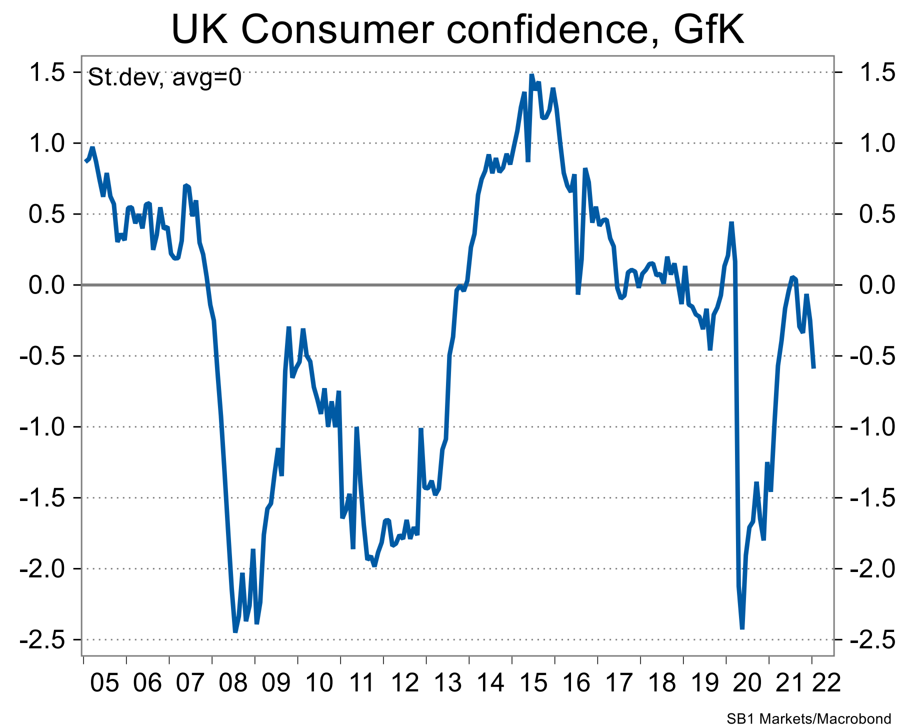
... and all three surprised at the upside



Retail sales recovered just some of the Dec loss in January

Sales up 1.9% following the 4% Dec drop, expected up 1.2%. More to go in Feb, 'after' Omicron?

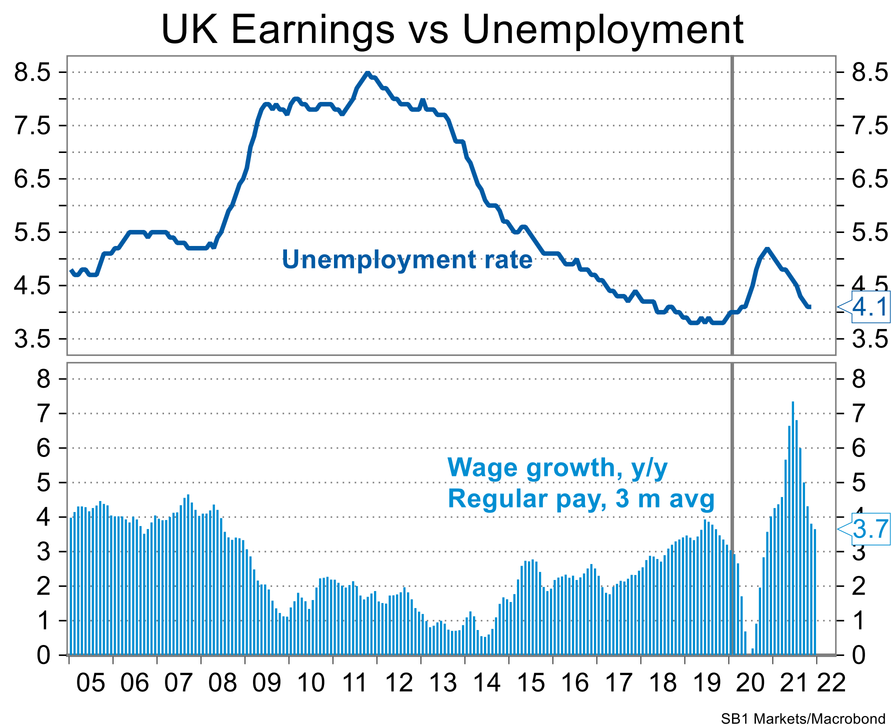


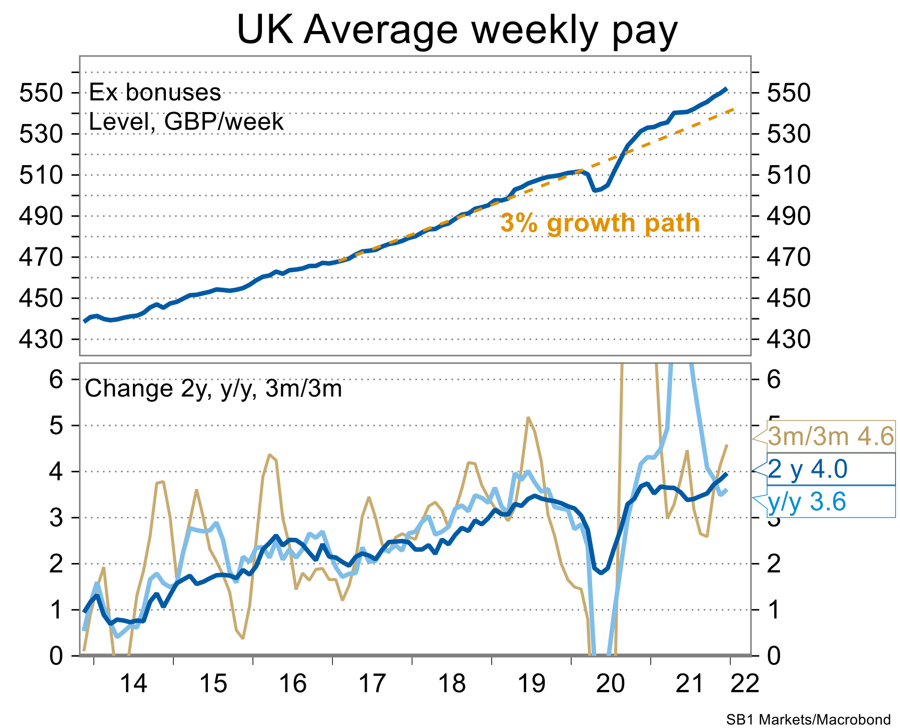


- **Retail sales** peaked in April, and the gradual decline brought sales down to the pre-pandemic 2.5% growth path – before falling below in December, when measures were taken to reduced the spread of Omicron. Sales just partially recovered in January but more than expected. In February all restrictions were lifted, and sales probably rose further
- **Consumer confidence** has fallen recent months to somewhat below average

Unemployment is trending down - to just marginally above the pre-p level

Wage inflation is accelerating (even if annual growth rates are slowing)

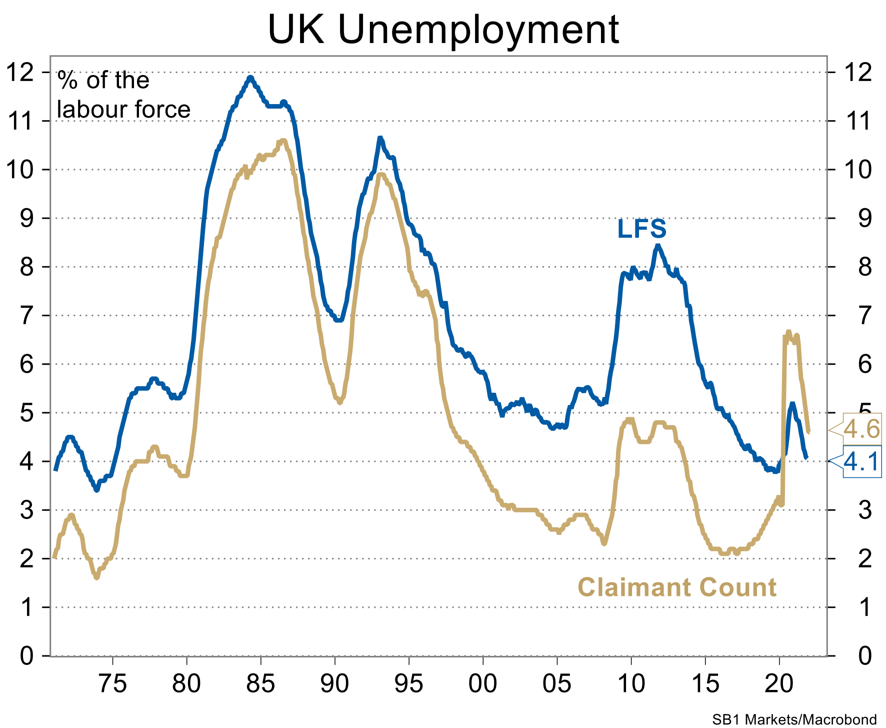


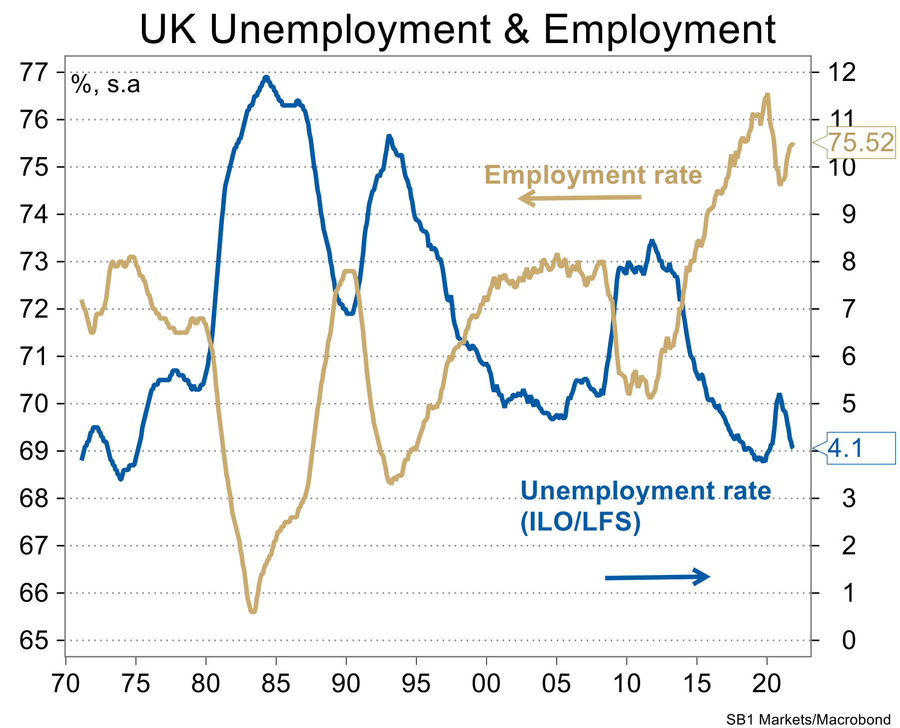


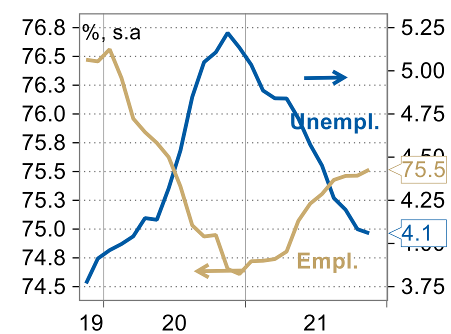
- The **'LFS/ILO' unemployment rate was unuch at** 4.1% in December – but the trend is still down. The rate is just 0.1 pp higher than before the pandemic
- **Annual wage growth** (regular pay) decreased to 3.7% in Dec from 3.8% in Nov, expected down to 3.6 (the 3 m avg fell to 3.7% from 3.8%. Including bonuses, wages are up 4.3%, up from 3.8%
  - » Over the 2 past years, regular weekly pay is up 4.0% in average. Over the past 6 months (3m/3m) wages are up 4.6%, and both are accelerating
  - » When the pandemic hit, wage inflation was slightly above 3% – which was substantial higher than over the years before: at 1 – 2½ %

‘Open’ unemployment at 4.6%, sharply down since the spring but still ‘high’

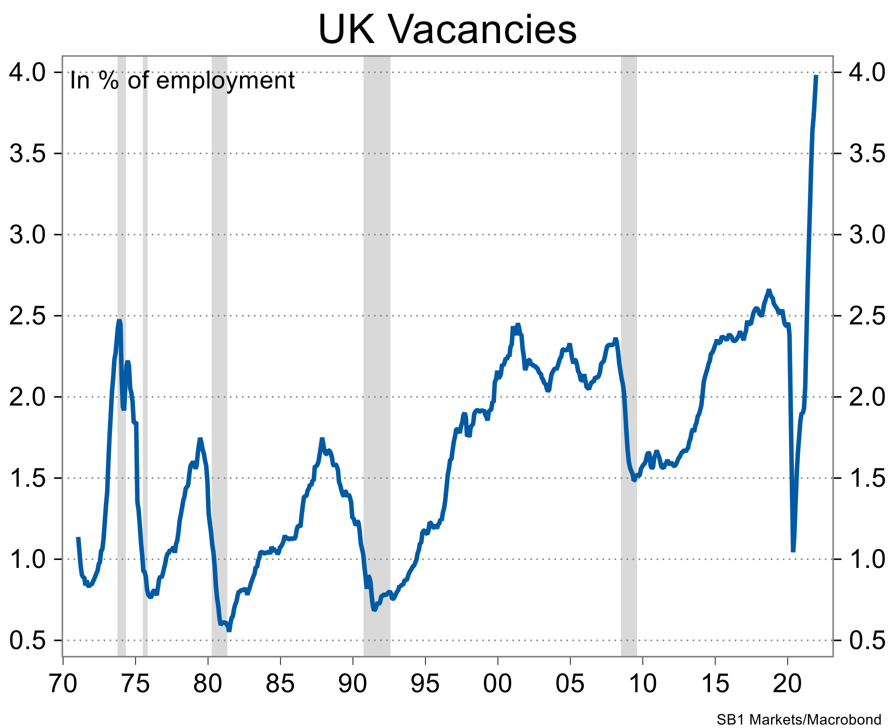
The employment rate is 1 pp down (1.2%) vs. Feb-20

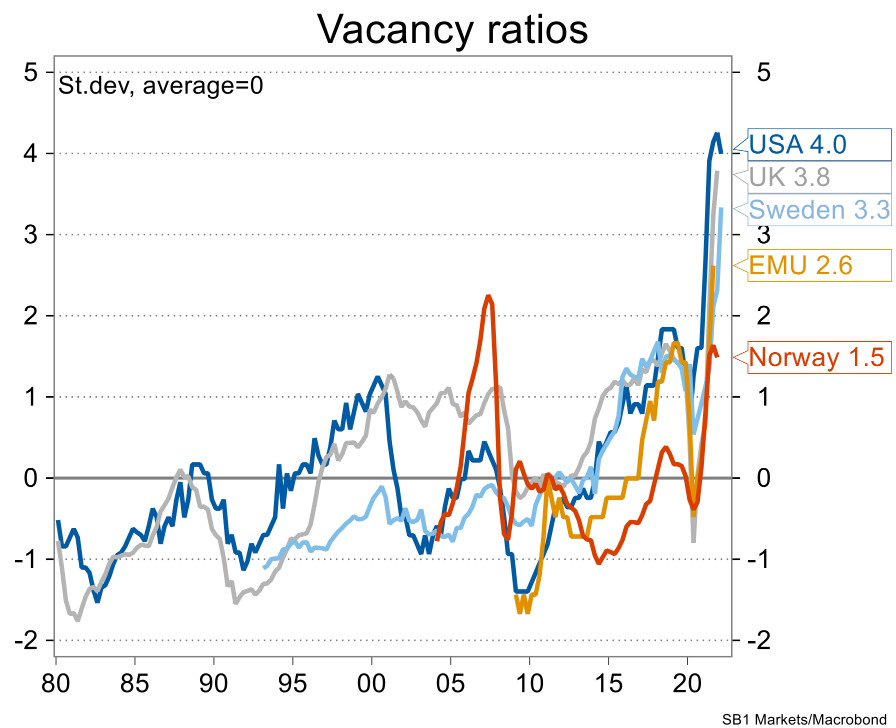






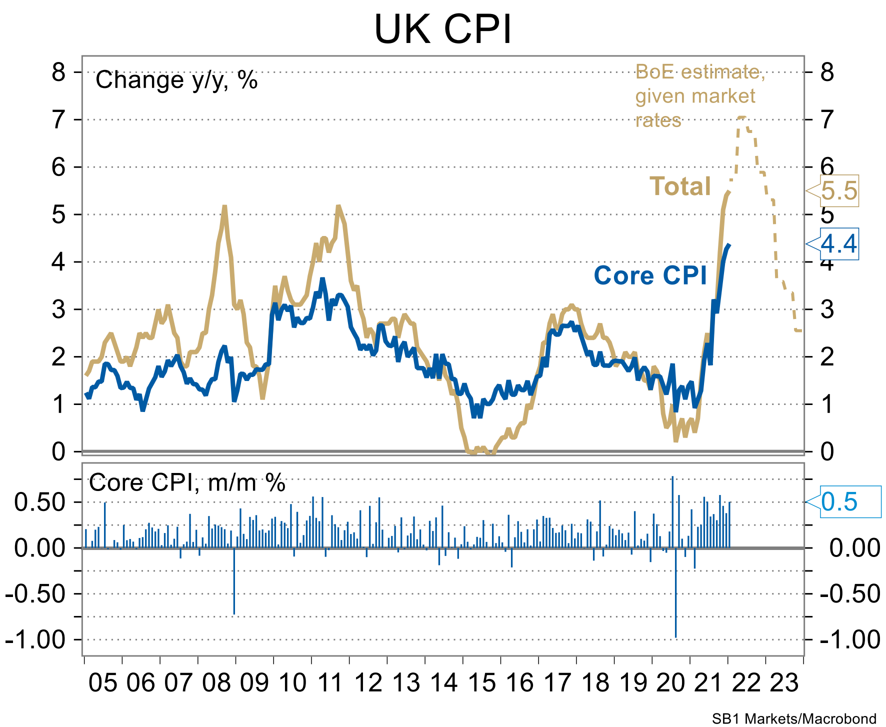
Vacancies shot further up in Q4, is approaching US levels!

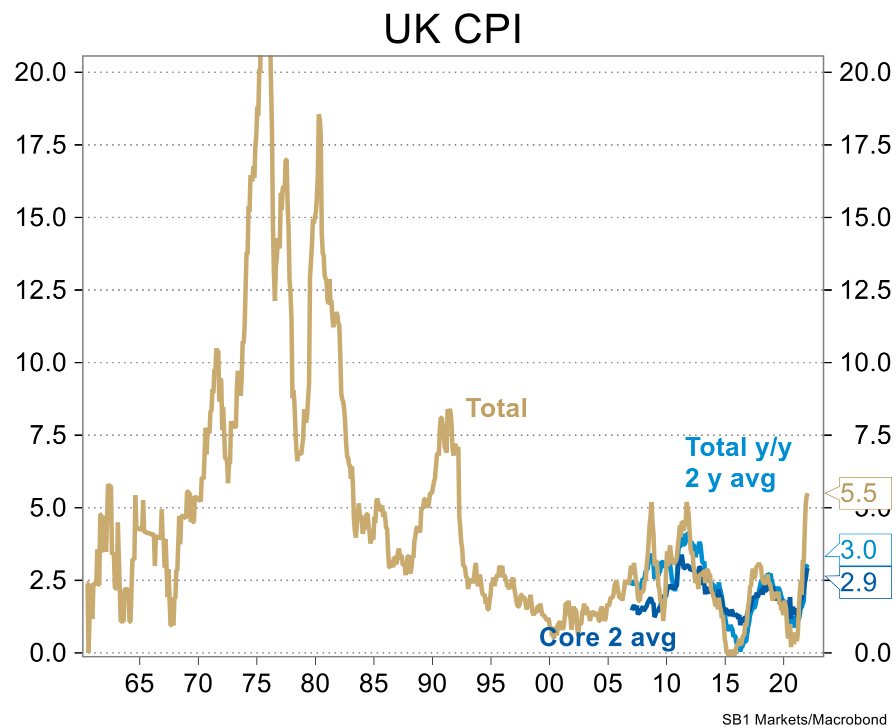




Inflation up to 5.5%, the core to 4.5%, slightly higher than expected

The core up 0.5% m/m, as is the 'new normal' these days





- **The total CPI** rose 0.4% m/m. The annual rates are the highest since the early 1990'ies. Measured over the past 3m/3m the core index is up more than 5%
- **Measured over 2 years**, headline is up 3.0%, and the core is up 2.9%, which illustrates the base effects on the present much higher y/y rates. Still, inflation is well above BoE's 2% target, anyway how we calculate it!
- **Transport** has lifted CPI by 1.6 pp. 2nd hand cars are sharply up, as are fuel prices
- **Housing, included energy**, has lifted the CPI by 1 pp. Still, there are many other contributors left…

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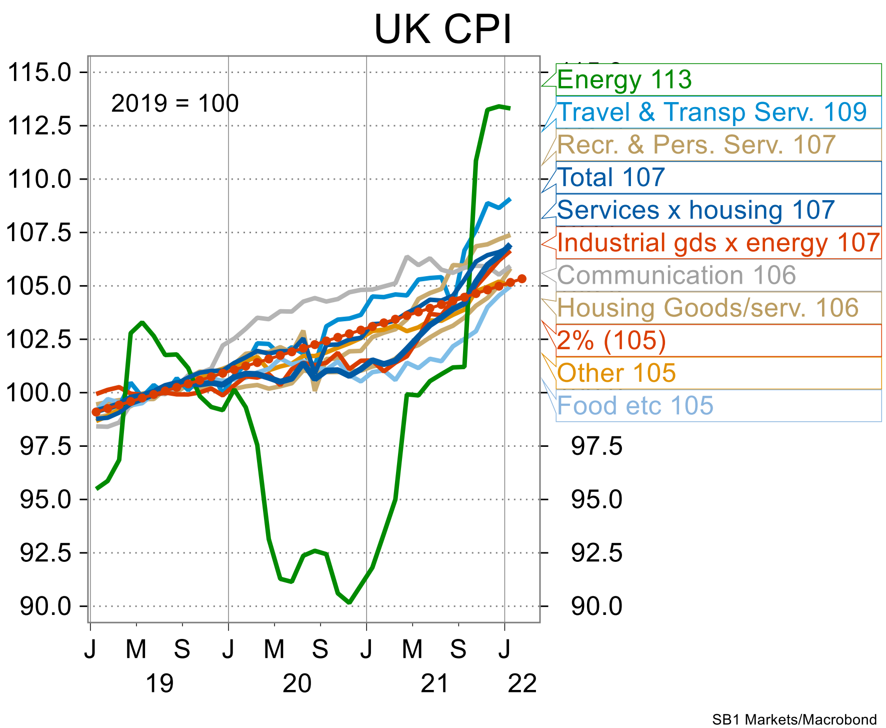
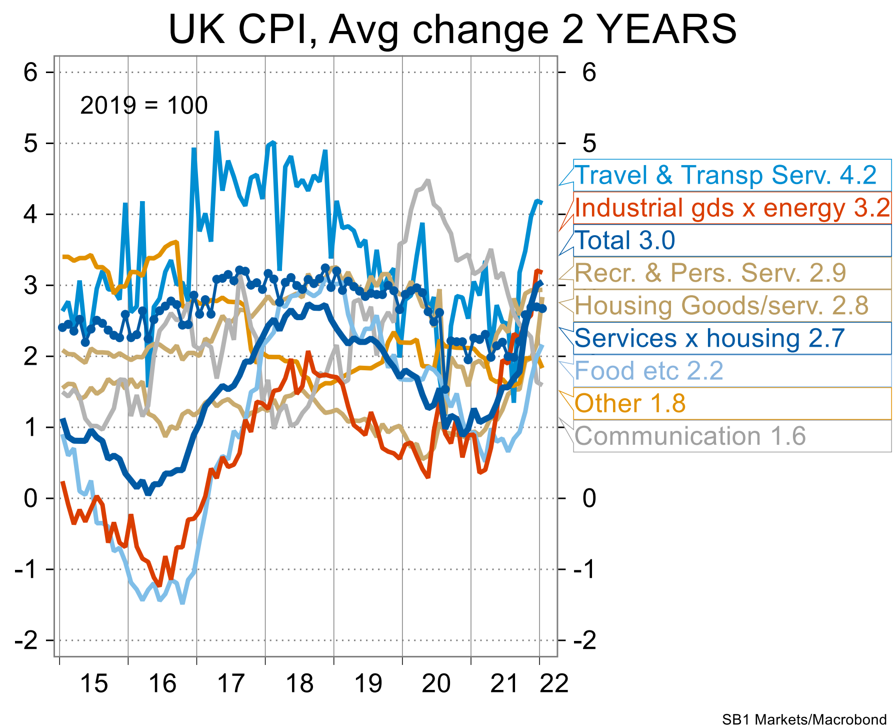
Energy a culprit but many prices are accelerating, now

Measured over 2 years, inflation is not that high – *but recent monts prices have been accelerating*





- **Energy prices** are up 23% y/y, rather modest vs. the lift in spot gas and electricity prices
- Almost all sectors are up more than 2% even measured over the past 2 years

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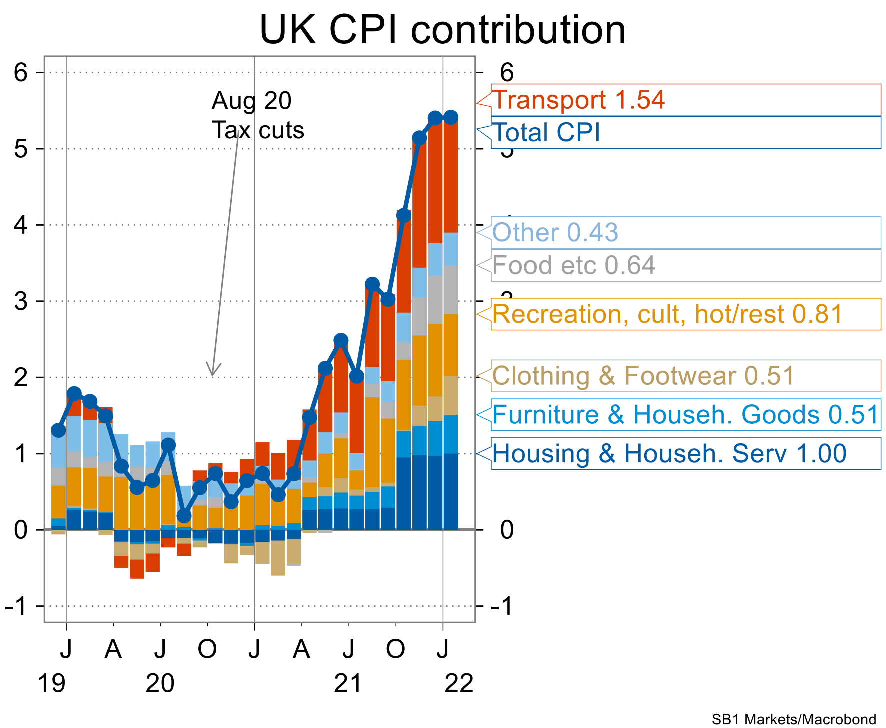
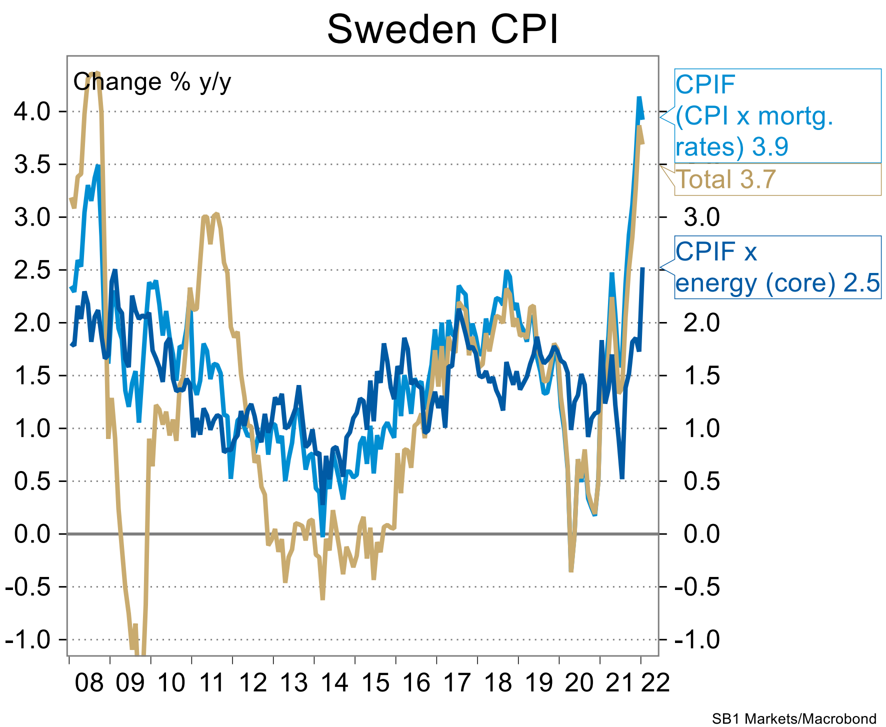
Transport, housing, recreation/hotels/restaurants the main contributors

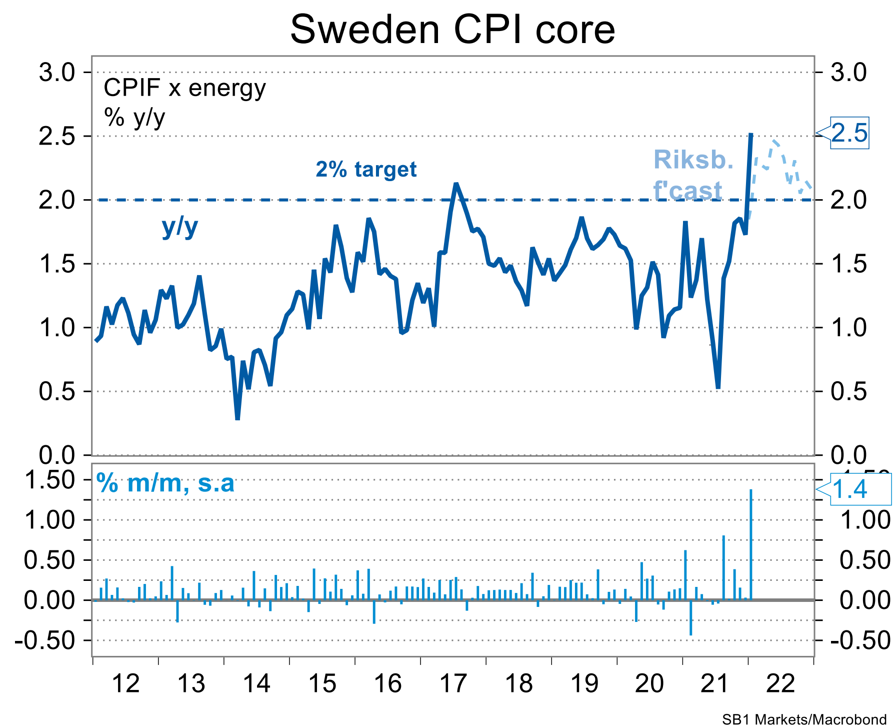
Within transport and housing, the energy component is the main culprit. But….



Core inflation up 0.8 pp to 2.5%, 0.6 pp higher than expected

Headline inflation still down, as electricity prices fell sharply, like in Norway



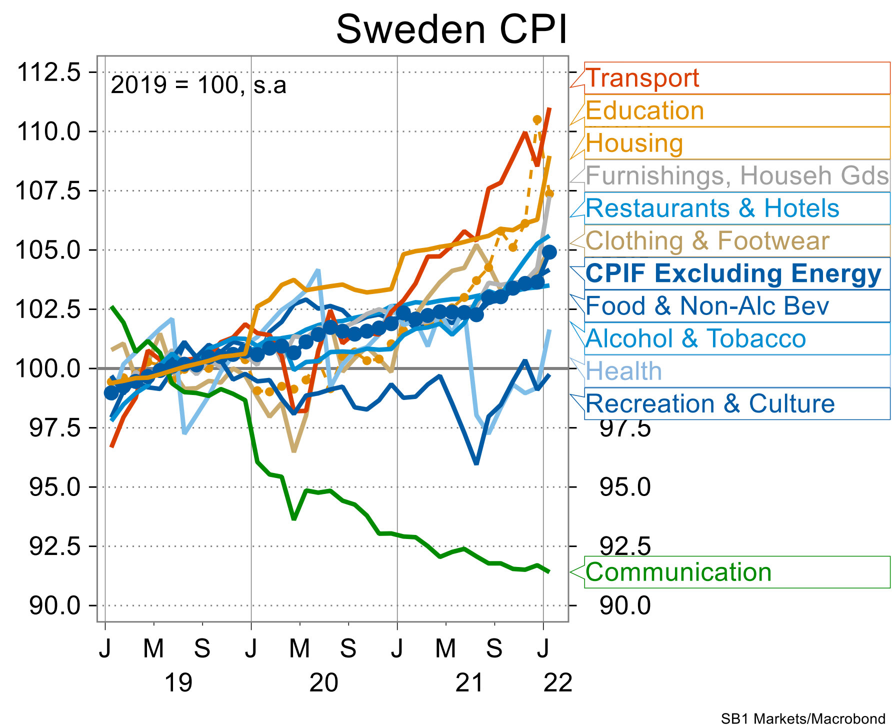


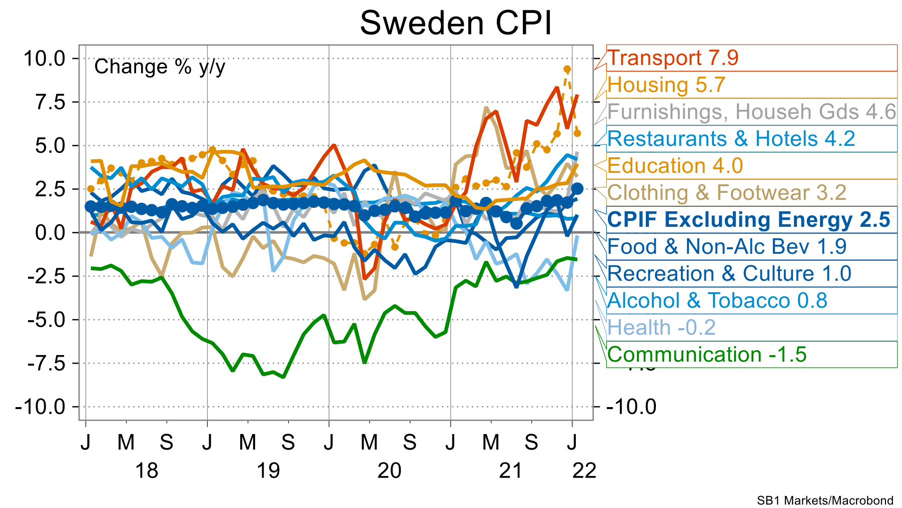
- **CPI-F x energy, the 'real core'** shot up by 1.4% m/m in January (seasonally adj), way above any forecast
  - » Prices actually rose 0.1% m/m, expected down 0.5%. The Riksbank expected a 0.5% decline too
  - » Prices rose by 0.7% (s.a) in Jan 2021, and thereafter retreated by 0.4% in February. If that trick is not repeated – and strengthened – this time around, the Riksbank will have to revise its inflation forecast sharply upwards. And if so, the Riksbank will have to revise its inflation forecast - and then to announce that the signal rate can be lifted before H2-2024. The market expect 1 hike in 2022, and 3 more in 2023 (rate expectations rose by 3 – 5 bps on Friday, following the CPI report
- **Headline inflation** slowed 0.2 pp to 3.7% y/y in Jan, expected down to 3.4%. Finally, electricity prices yielded

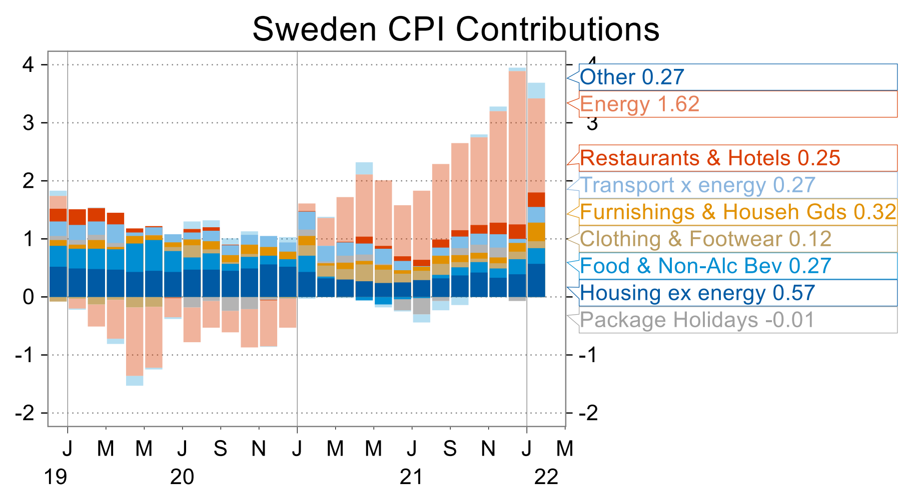
SpareBank 1 MARKETS

Inflation in Sweden: it's used to be just energy, but not so anymore

Energy prices fell in January, but suddenly other prices shot up



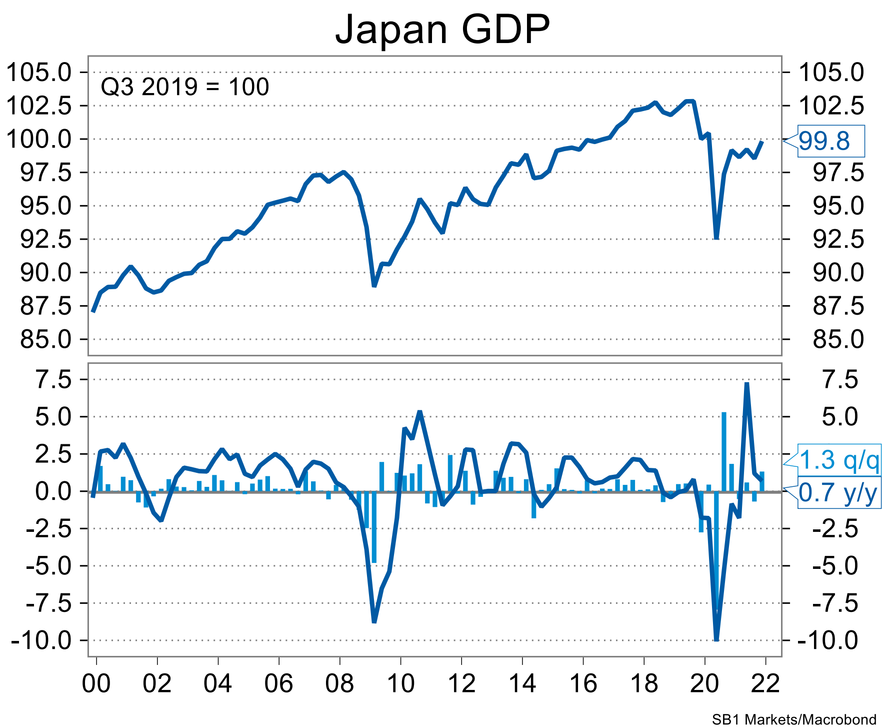


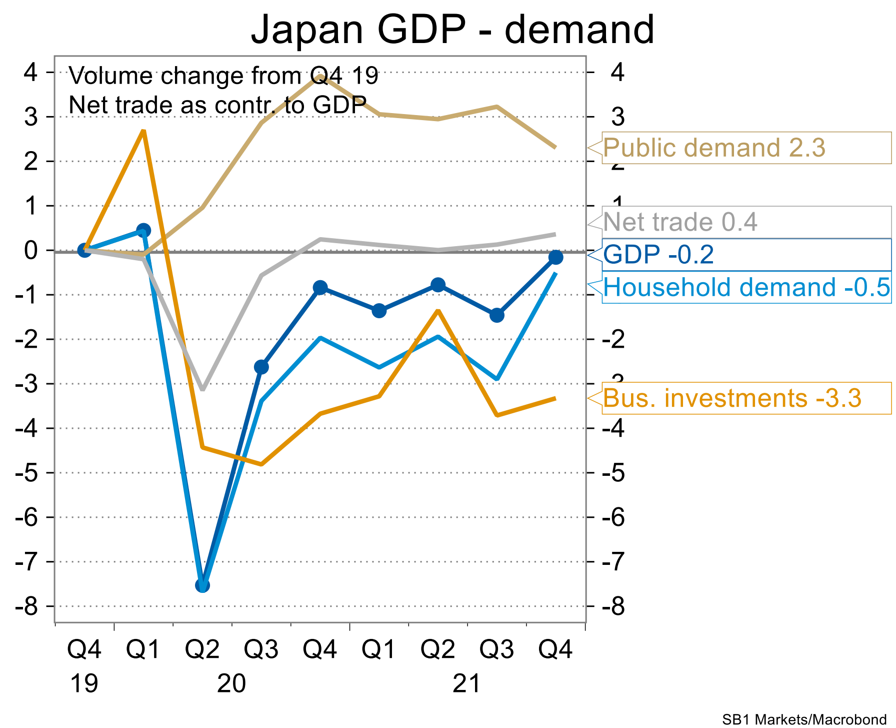


- Transport services, clothing furnishings & household equipment, health, package holidays, education all contributed significantly at the upside measured m/m
- I now remains to be seen if these price increases will be reversed or not in February or March

GDP up 5.3% in Q4 (1.3% not annualised), history significantly revised upwards

History was revised up by <u>1.5%</u> (vs. the Q4-19 level). Consumption did the heavy lifting in Q4

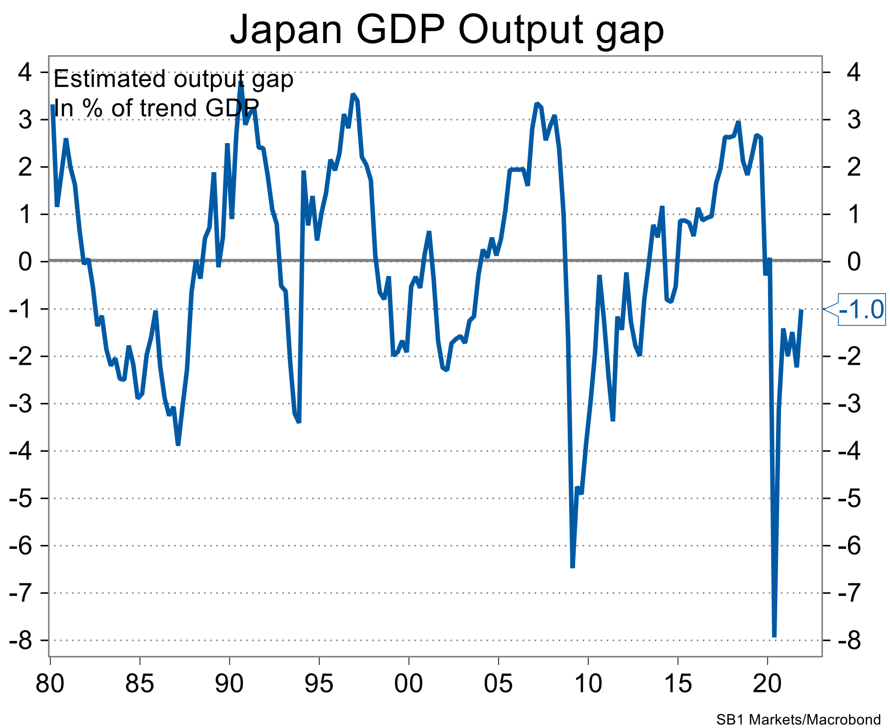


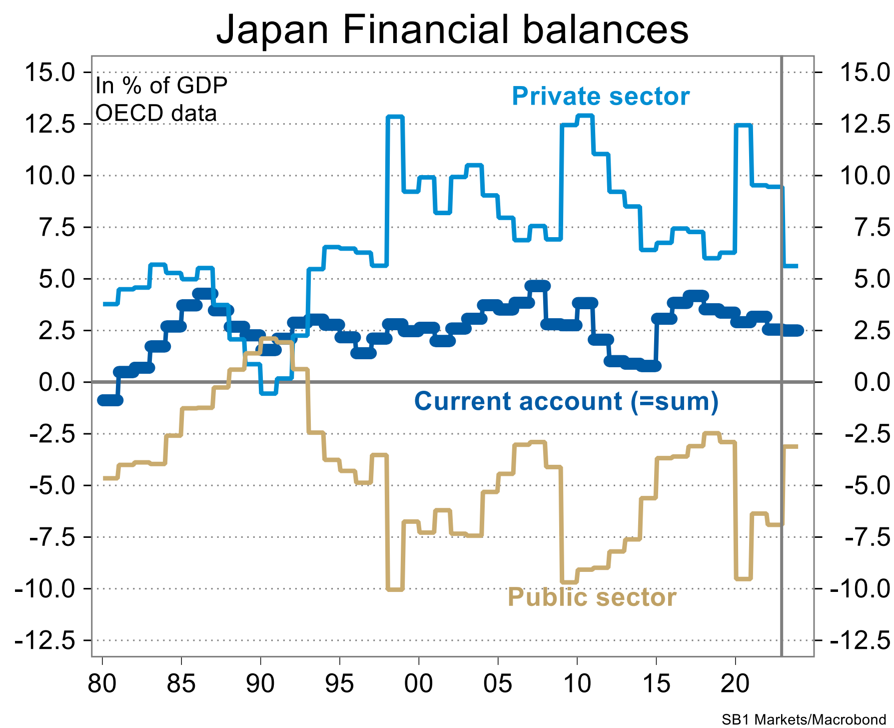


- All in all, a much better reported than expected, even if GDP grew a tad less than expected in Q4 (1.3% vs. 1.5%)
- GDP is now just 0.2% below the Q4-19 level – which was rather weak though (due to the VAT hike in Oct-19). GDP is more than 2.5% below the late 2018 level

SpareBank 1 MARKETS

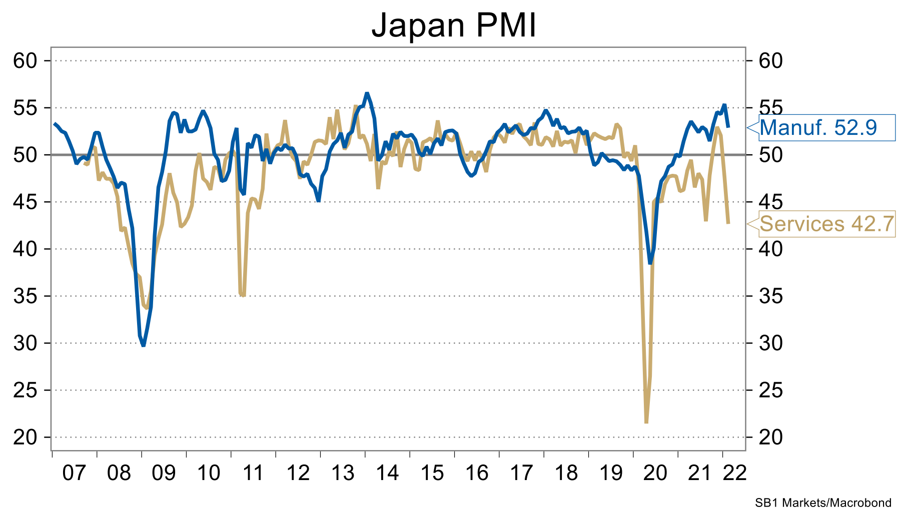
A deep downturn – but not that far up the pre-pandemic trend level

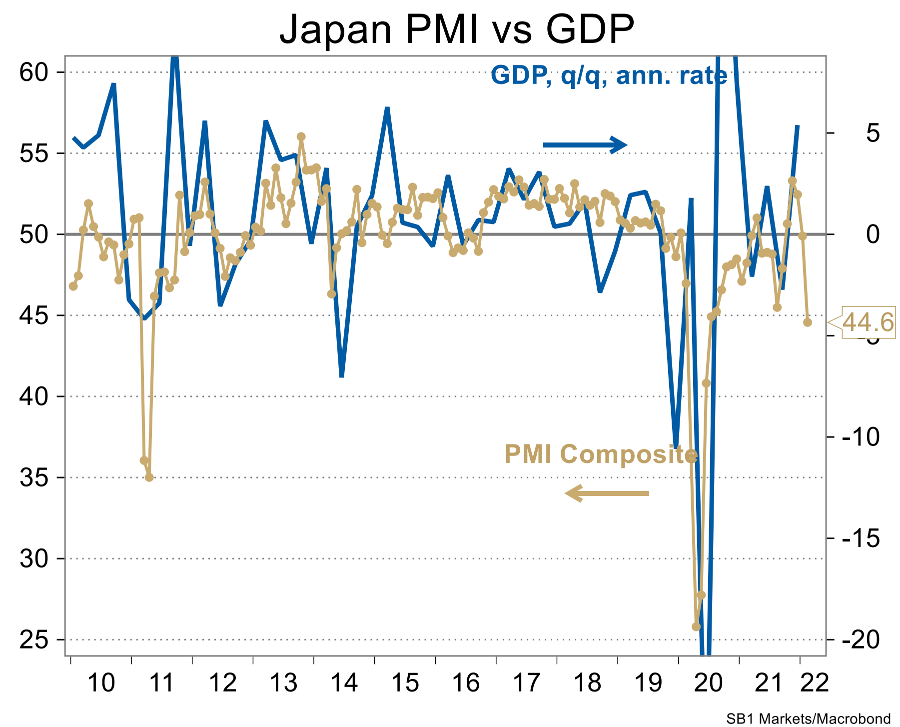


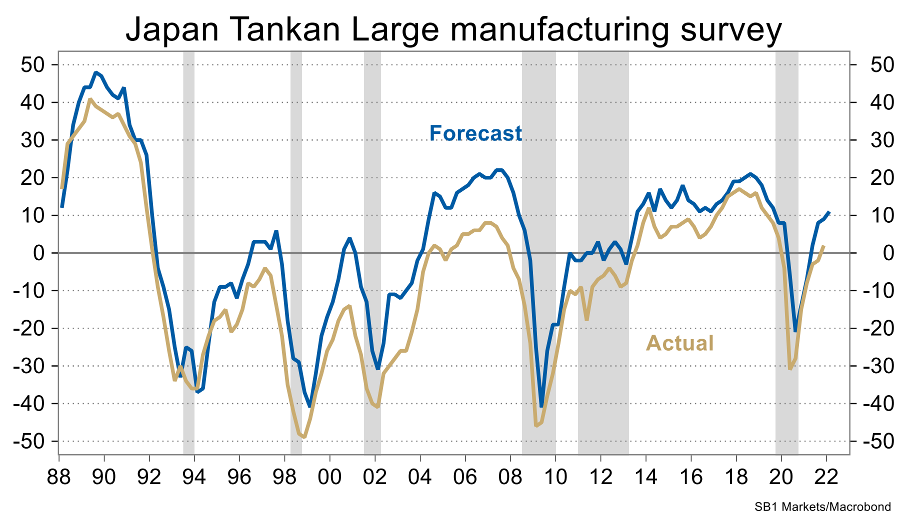


A further decline in the PMIs in February

The composite PMI fell by 5.3 p to 44.6, signalling a steep (a 4 – 5% pace) decline in GDP







Highlights

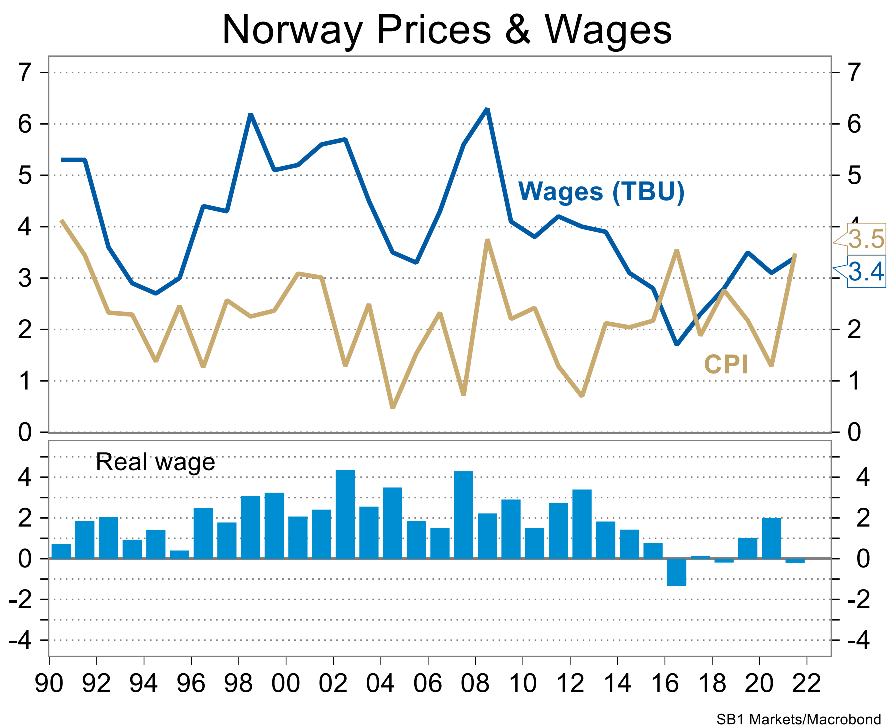
The world around us

The Norwegian economy

Market charts & comments

The TBU assumes 2.6% inflation in '22, lowering expectations of high wage increases

Wages rose 3.4% in the unionised part of the economy last year (3.5% overall). CPI was up 3.5%

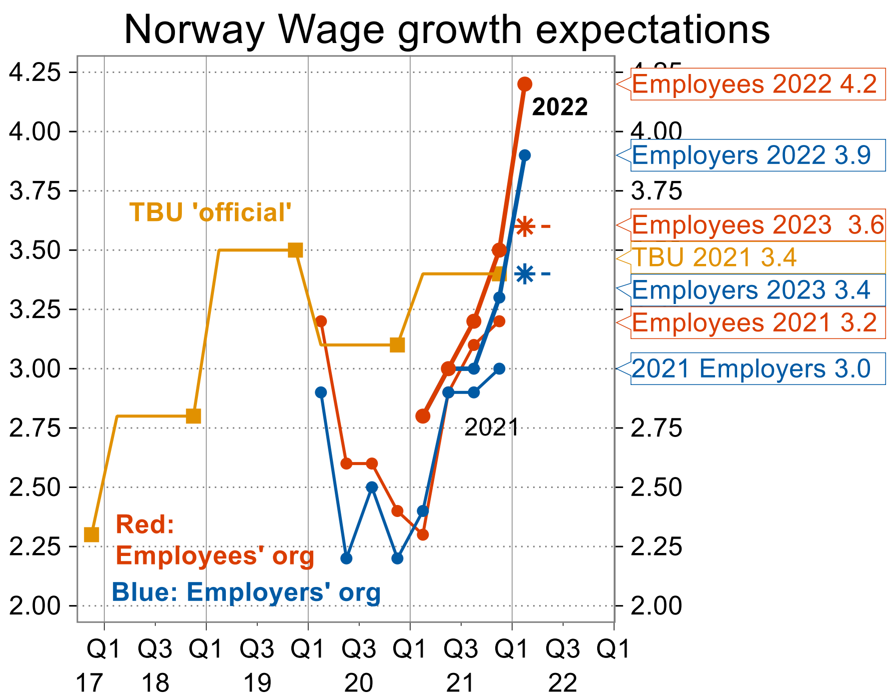


- In the TBU, representatives from the Min. of finance and Min. of Labour, employers' associations' and trade unions together with SSB agree upon what has actually happened with wages last year, and they recognise a common price prognosis for the coming year (technically produced by SSB).

- The **Technical Committee** for clearing the ground for this spring's wage negotiations estimate last year's wage growth in the unionised part of the economy to 3.4%, as usual close to SSB's estimate of average wage growth for the overall economy, now estimated to 3.5%
  - » After last year's wage negotiations, the parties (and the TBU thereafter) estimated a 2.7% 2021 wage growth. Local adjustments and wage drift in a tight labour market turned out to become substantially higher than expected last spring
  - » In December **Norges Banks** assumed a 3.1%, after having revised up its forecast by 1.1 pp trough last year
  - » In Norges Bank's Q1 **expectation survey**, both employers' associations and trade unions thought wage rose 3.1 – 3.2% last year (the survey was conducted before SSB published its estimate)
  - » **Wage inflation** was somewhat lower in the public sector than in the private sector, and unions are now arguing for higher wage increases this year
    - However, looking back some few years, wage growth in the public sector has been higher than in the private sector. Still, there are potential for conflicts in the public sector wage negotiations this spring
- The **current 2.6% inflation forecast** is uncertain, both due to the global increase in inflation, and because the outlook for energy prices is uncertain. The forecast will be revised March 10, after the February CPI is published
  - » Electricity prices, as they are calculated in the CPI (and according to the SSB), are expected to rise by 2.5% in 2022, based on forward market prices. This outcome is somewhat strange, as future prices are heading straight down, signalling a substantial decline also in households' average electricity 2022 bill, following the steep rise in 2021
- 2022 wage expectations have shot recent months (check next page!) but the TBU report should calm down these expectations – at least vs the outcome in this spring's wage negotiations. However, the labour market is tight, and wage drift will probably propel wage growth through 2022, and through last year

NoBa Expectation survey: Wages straight up in 2022, expectations up 0.6 – 0.7 pp

Are they aiming for 4%? A slowdown is expected in 2023, 'just 3.4 – 3.6% expected



2021 – wages rose faster than assumed by 'everybody'

- Wages rose 3.4% in the unionised part og the economy, according to TBU
- In Q4, leaders in the employers' organisations expected 3.0% and in the employees' organisations 3.2%, according to the Q4 NoBa expectation survey
- Norges Bank assumed 3.1% wage inflation in the Dec MPR
- In last spring's wage negotiations, a 2.8% wage increase was agreed upon

2022 – the largest upward revision ever!

- Leaders in employers' organisations lifted their forecast by 0.6 pp to 3.9% in Q1
- In the trade unions, leaders expect 4.2%, up 0.7 pp from Q3
- Norges Bank assumed a 3.2 % growth rate in the Dec MPR – and the bank will have to revise it's forecast sharply upwards
- We think wage inflation will approach 4% in 2020 but that will not be the outcome of the wage negotiations. The expectation survey was conducted before CPI inflation dropped to 3.2% in January from 5.3% in December

2003 – down to 3.5%. Well, that's not impossible but…

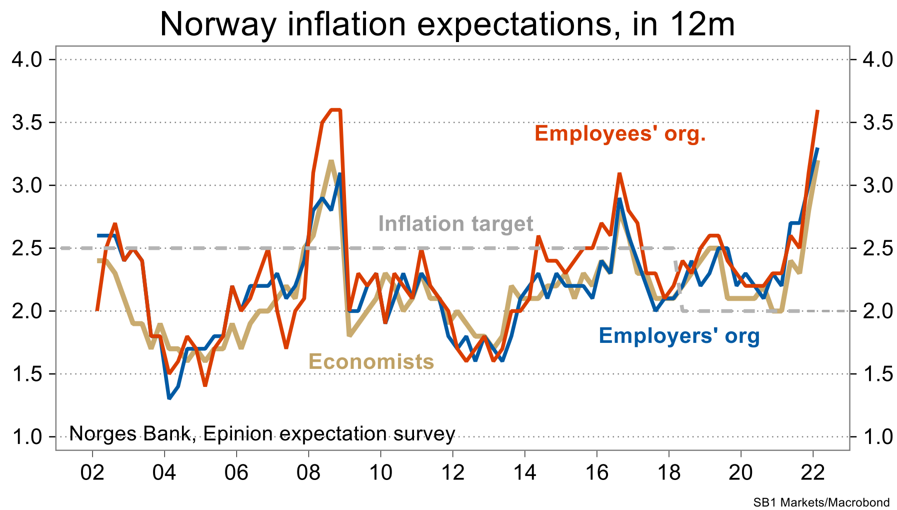
- Employers aim for 3.4%, the employees 3.6% as 2022 is assumed to be an exception, not the rule
- Given the current tight labour market, these forecasts seem to be on the low side

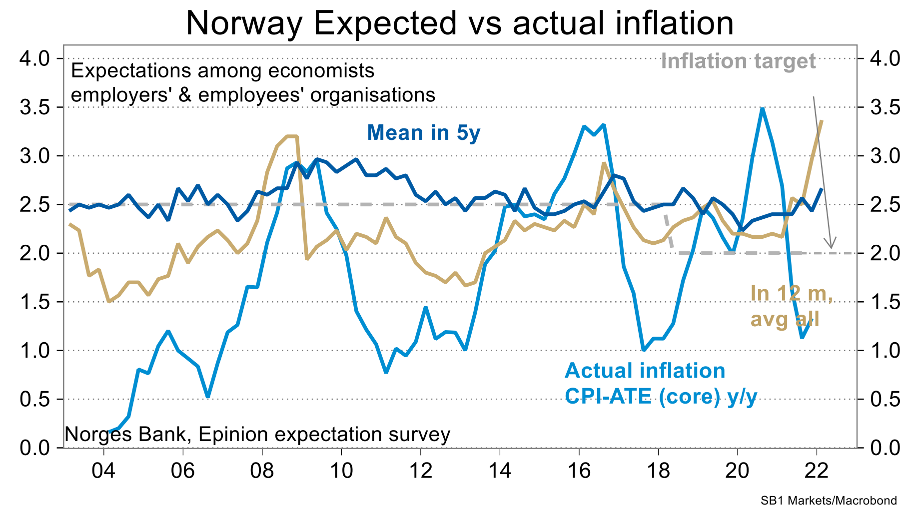
In sum

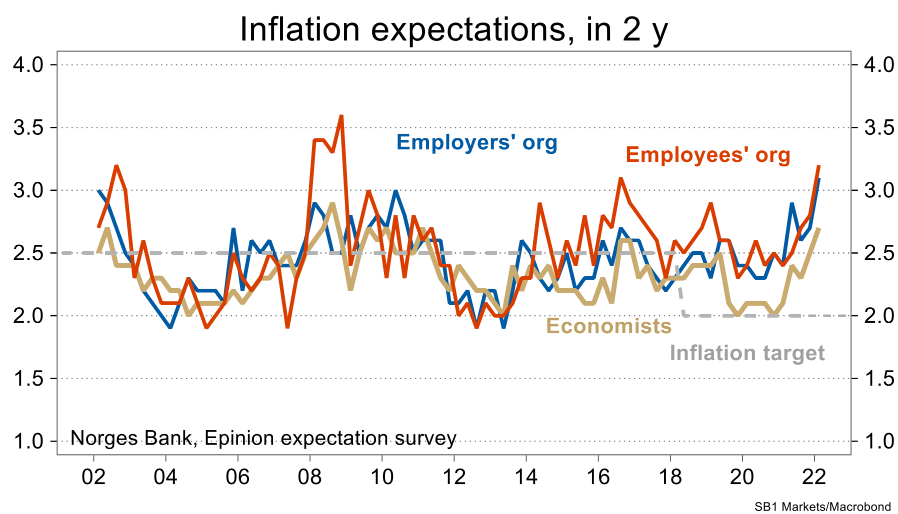
- We wrote 3 months ago: *'we expect further upward revisions the coming quarters as the labour market rapidly tightens'*
- Now, we are almost 'satisfied' with the 2022 forecasts, but the risk is still at the upside even if we do not think the wage negotiations this spring will yield a 4% outcome. However, actual wage inflation will probably climb to above 4%, due to the tight labour market
- Norges Bank will have to revise wage inflation up for both '21 and '22, by at least 0.5 pp in average in the March MPR

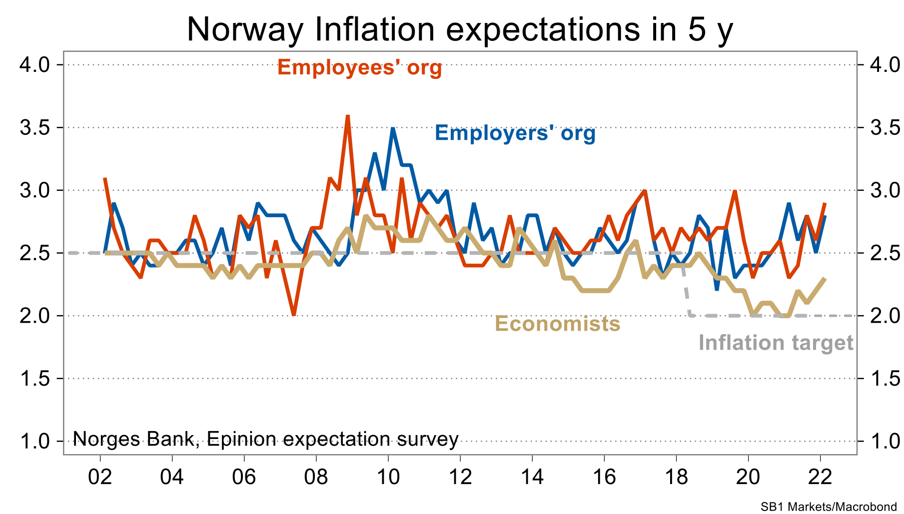
Short term inflation exp. further up, and nobody believes in 2% long term!!

Labour market organisations expect 2.8-2.9% inflation long term, even economist have given up the 2% target



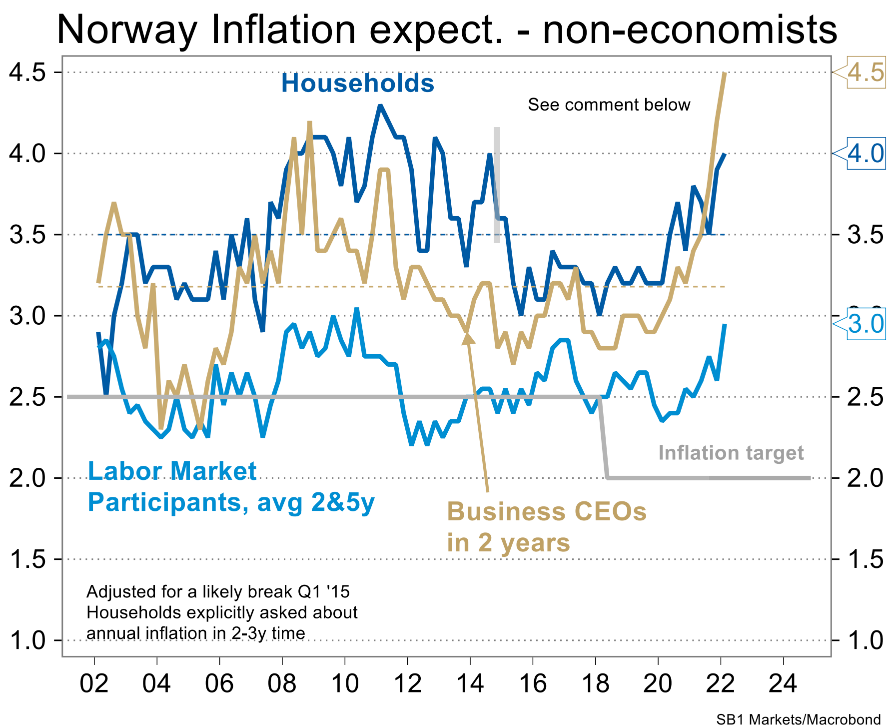






Household, business inflation expectation are not particularly well anchored

Businesses expect a 4.5% inflation rate in 2 years' time, households 4%



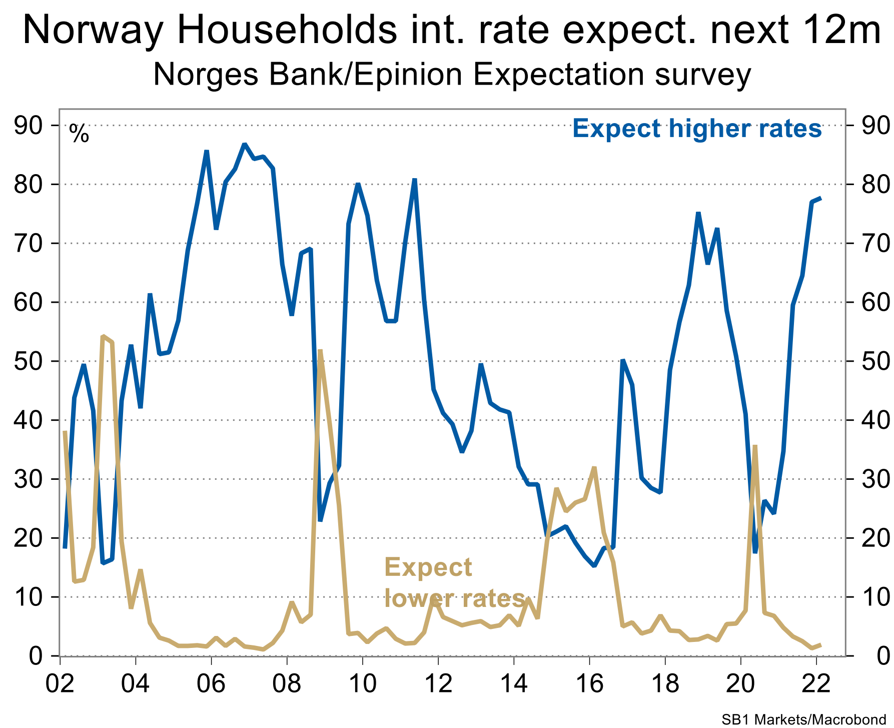
Business leaders' & households' expectations are rising sharply to above normal (very high) levels

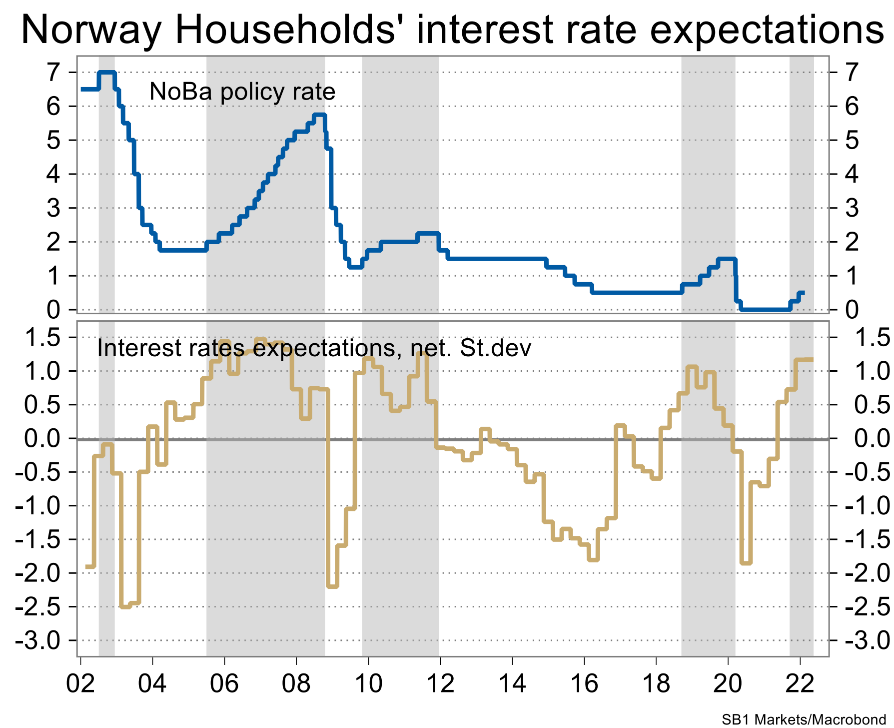
- **Labour market participants** (leaders in trade unions & employees' assoc.) are probably listening to their economists, but the still expect 3% long term inflation rate (2 y & 5 y avg). The cut in the inflation target to 2% in 2018 has not influenced inflation expectations at all
- **Business leaders** are expecting a 4.5% inflation rate in 2 years time – up 1.5 pp since before corona, and much higher than their average expectation (3.1%) (and no impact of the lower inflation target)
- **Households** have always expected incredibly high inflation going forward (even after an adjustment of data prior to Q1 '15, due to a clarification of 'inflation', see below) – on average 3.5%. Now, **they expect 4.0% in** 2 to 3 years time, up 0.2 pp from Q4, and 0.8 pp from before corona
  - » Should we just ignore these 'silly' expectations, or should we reflect on them?
  - » We should at least put some emphasis on the significant rise in inflation expectations – to above average levels
  - » **Perhaps we could even explain demand for credit from households by the 2 – 2.5 pp negative gap between mortgage lending rates and expected inflation?**

The questions regarding expected inflation in 2 or 2 – 3 years time for business leaders and households were slightly altered in Q1 2015 survey. Since then, they have been asked about the expected rate of annual inflation in 2/2-3 year time, not just 'inflation' which could have an unambiguous interpretation. Household revised their expectations down by 0.6 pp in the Q1 '15 vs the Q4 '14 survey due to this clarification. Business CEO's revised their expectations a tad upwards. Since there were no other major change in actual inflation or inflation expectations among other groups during these months, we have just revised households' expectations down by 0.6 pp pre Q4 '14 at the chart above

Households recognises that interest rates are on the way up

Households are often ahead of the curve when NoBa (well communicated) starts hiking

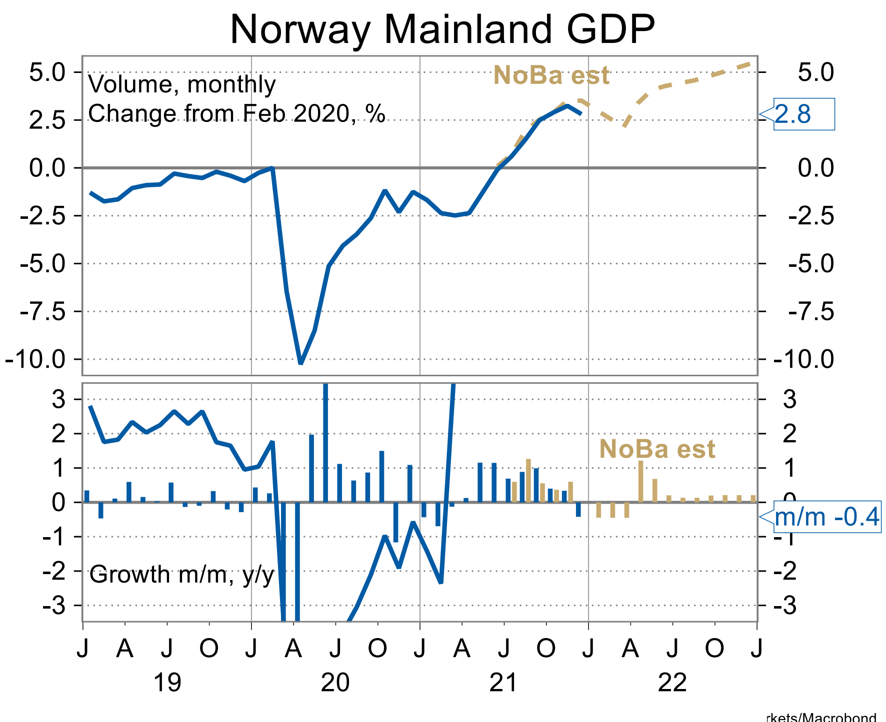


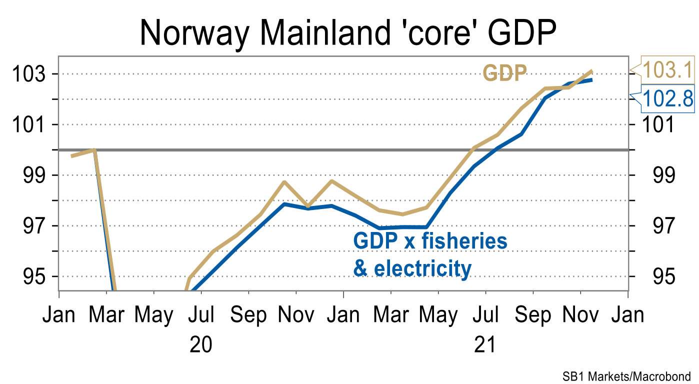


- 78% of households expect Norges Bank to hike the policy rate the coming 12 months, up from 65% 6 months ago, before NoBa started hiking. Still 20% are not sure (just 2% expect the banks to cut interest rates)

Mainland GDP down 0.4% in December, still +1.4% in Q4

November revised down, and Dec weaker than NoBa assumed but the recovery will start earlier

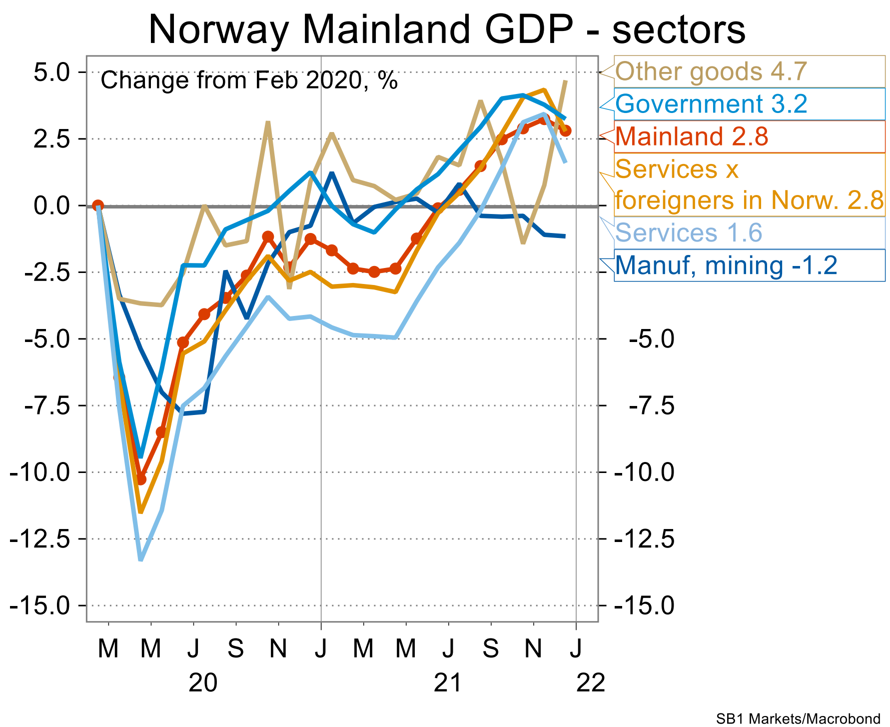


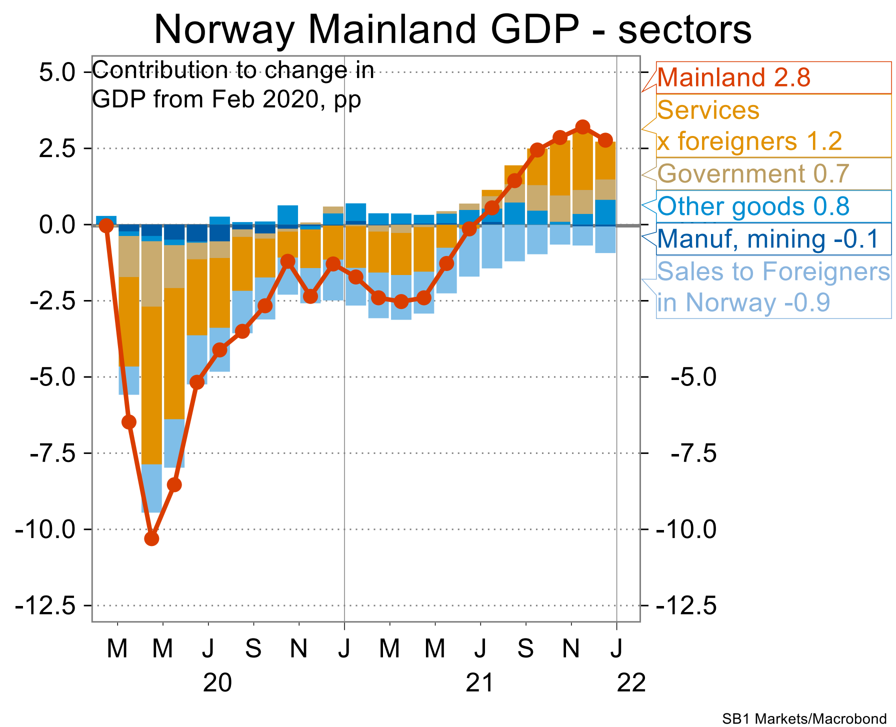


- **Mainland GDP** fell by 0.4% in Dec, Norges Bank expected unch, while consensus was for a 0.2% decline (we pencilled -0.3%). Growth in Nov was revised marginally down – but in total upwards
  - » **Production:** Detailed sector data are not available but activity in services fell by 1.8% m/m, as hotels & restaurants, culture was partially closed down.
  - » **Demand:** Norwegians' spending at home fell 2.7%, mostly due to a decline spending on services. Foreigners also reduce their spending, by 21%. Oil investments rose but history was revised unusually sharply down, by 10 pp while Mainland business investments rose sharply. Exports fell for the 2nd month in row
- **Mainland GDP is up 2.8% vs the Feb-20 level**
  - » **Production:** Services are back in black, even if production fell in December. Some sub-sectors are still below par, and more so in Dec. Manufacturing is down 1.2%. Other goods are sharply up, partly due to fisheries
  - » **Demand:** Norwegians' spending at home is up 7% from Feb-20, goods 13% (and now heading down), services are down 3% - but was trending rapidly up until December. Spending abroad is still down 56 %, and total household spending is up 1.4%. Oil investments are still in minus, revised sharply down (by 10%!). Mainland investments are finally in plus
- **The recovery was intact until December. We do not expect a recovery in January but February & March should be well into the black – as activity will start recovering 2 months earlier than Norges Bank assumed in December**

Production: Services down, other goods (than manufactured) sharply up in Dec

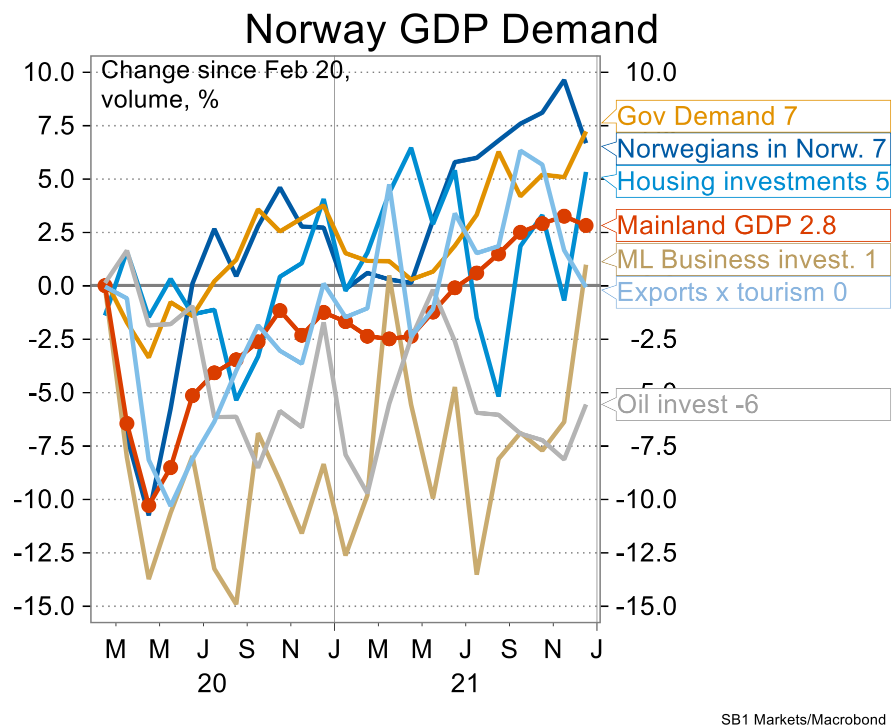
Services still start recovering again in March

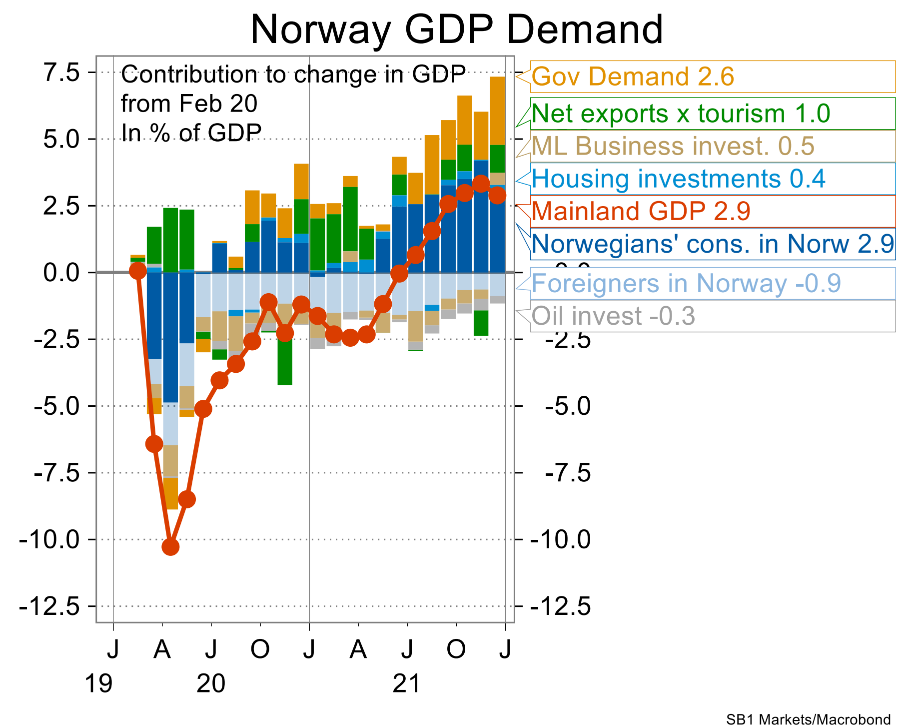




Demand: Household spending down in

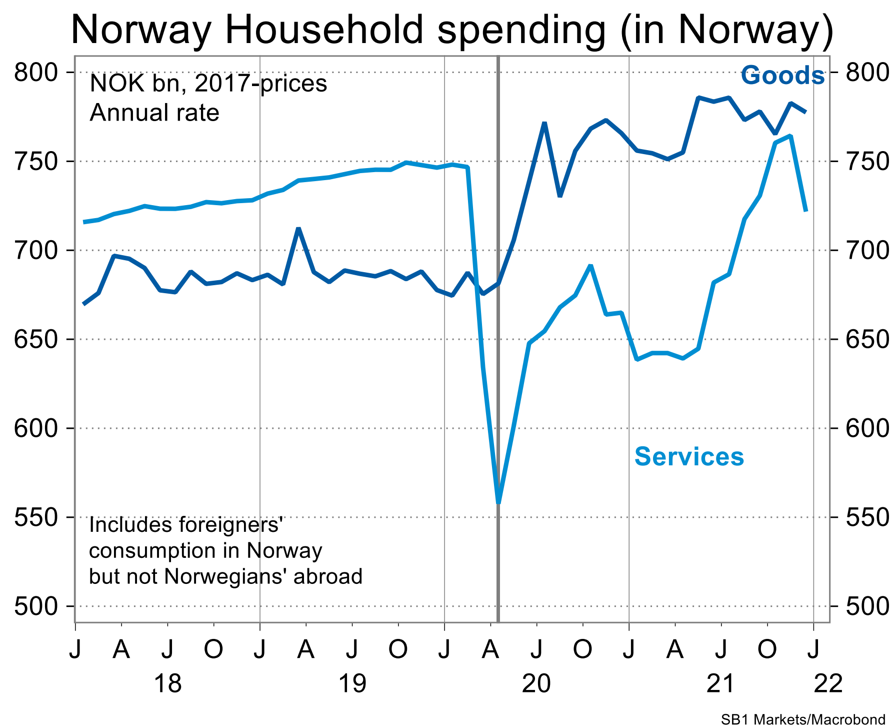
Oil investments have recovered, as are now Mainland business investments

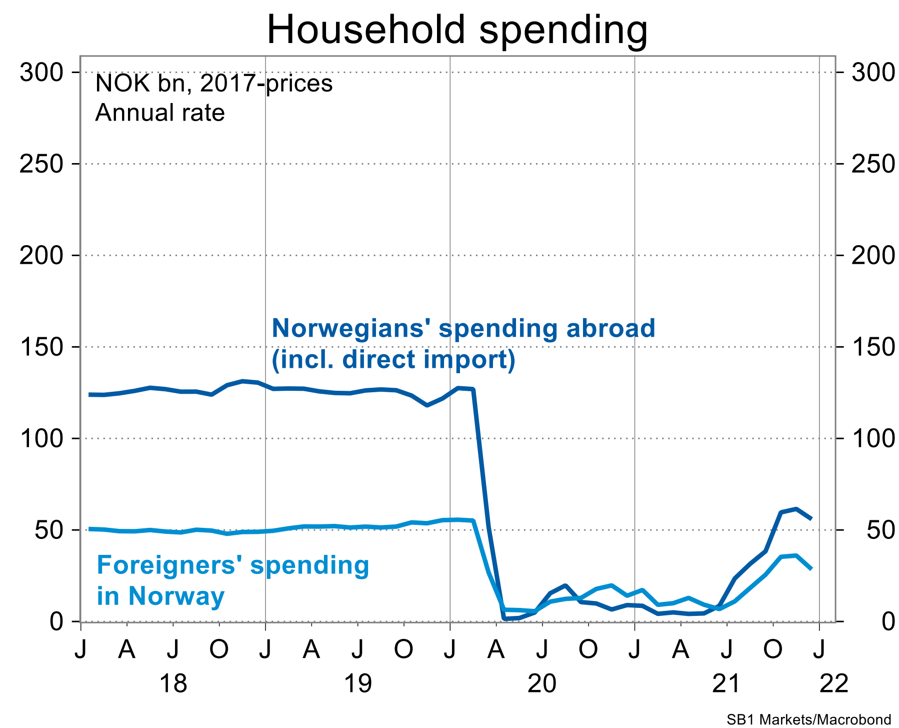




Services consumption in Norway finally above the Feb-20 level

A setback likely during the last (?) fight against the virus, thereafter at substantial upside

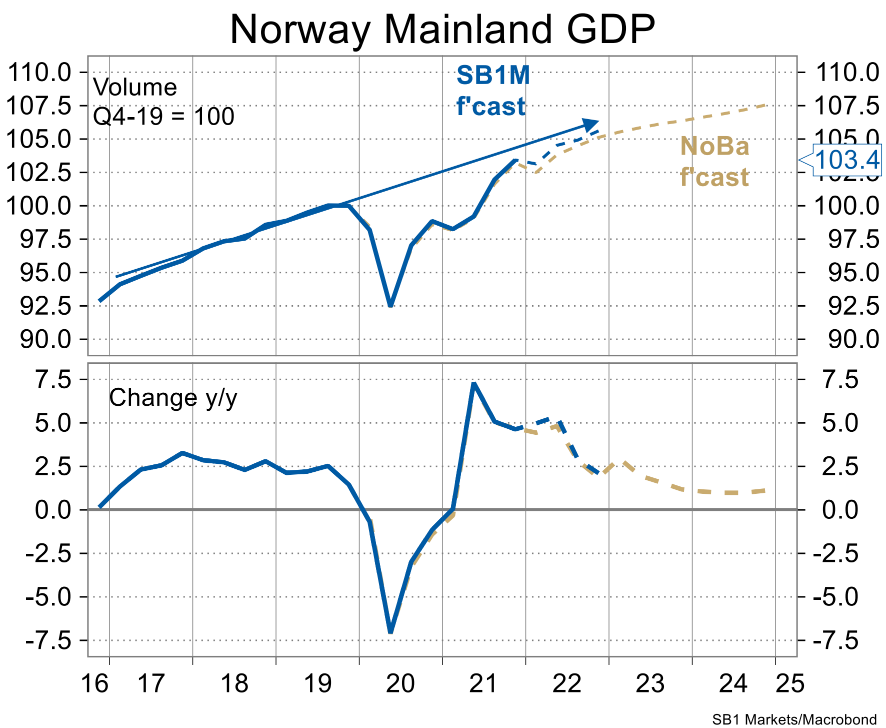




- Spending abroad is still muted, especially for Norwegians – foreign consumption in Norway has recovered far better!

Q4 GDP: Up 1.4% (5.8% annualized), and the level 3.4% above Q4-19

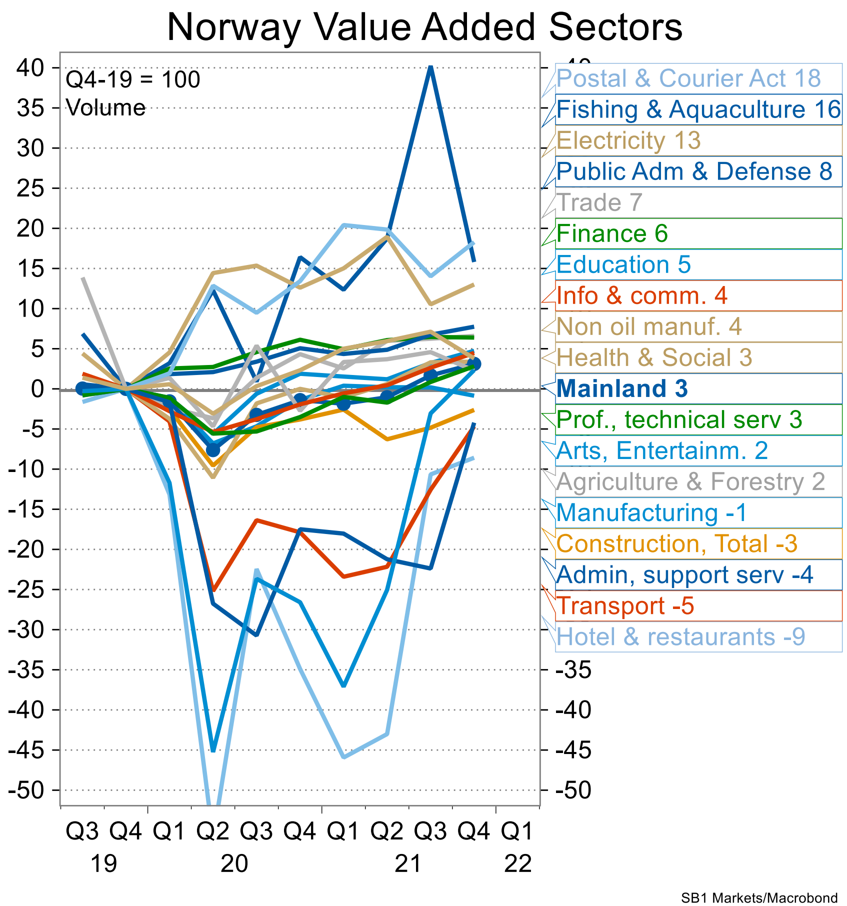
Activity is not far below the pre-pandemic trend, even if some services have not fully recovered

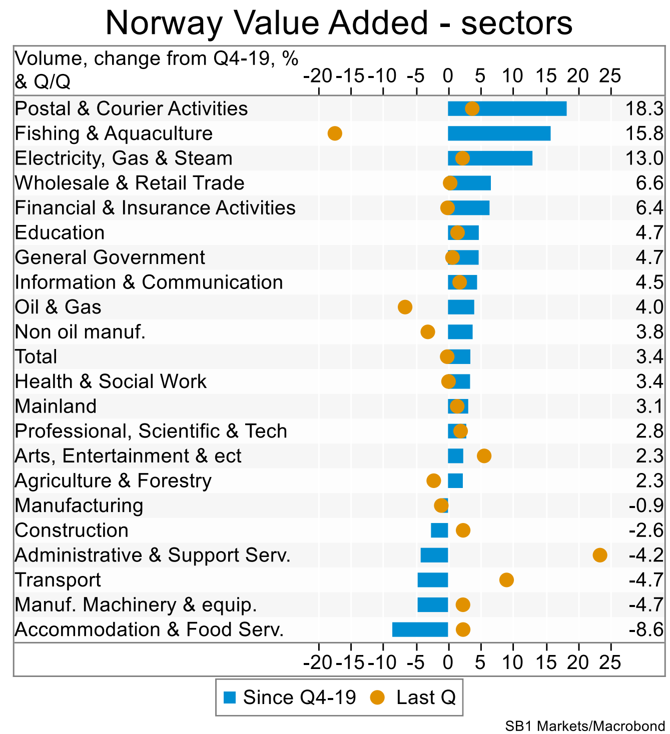


- **Mainland GDP up 1.4% in Q1 (, 4.2% in 2022**
  - » Norges Bank expected a 1.3% growth in Q4, and Q3 was revised slightly upwards
  - » Total GDP grew 3.8% q/q (16% annualised), 0.3 pp more than we expected. Oil and gas production (+shipping) added 10.7% q/q

Q4 Production: Growth in most sectors, even hotel/rest & culture

Some services are still down vs Q4-19 but we expect these gaps to be close in H1



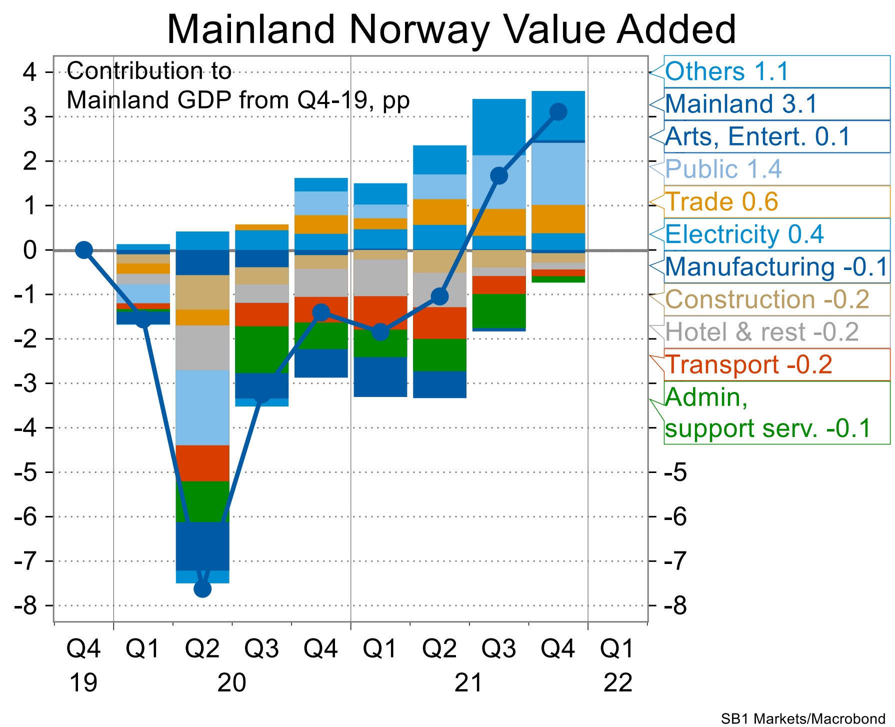


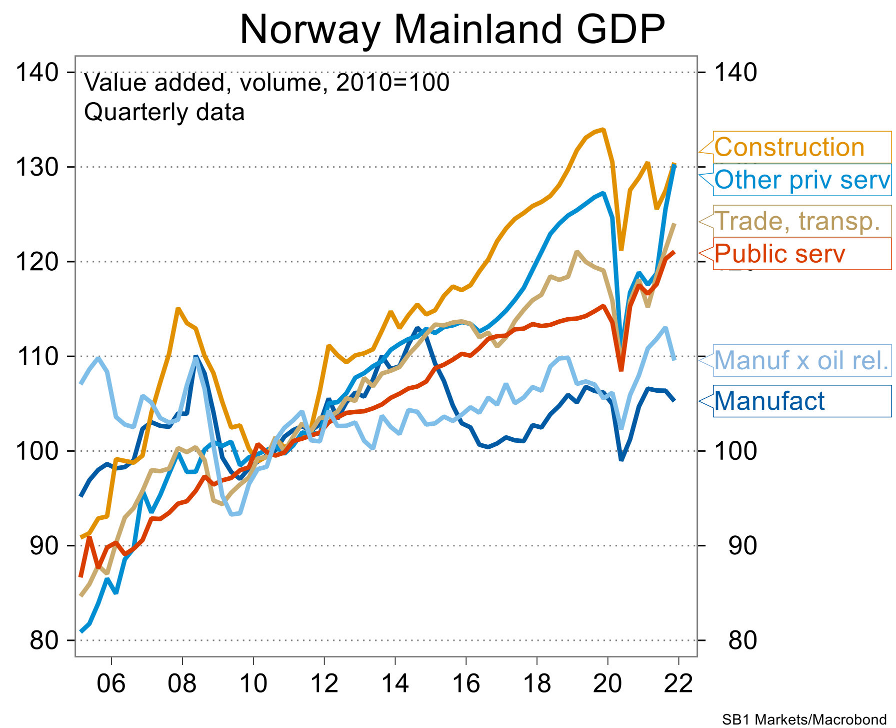
The Q3 data vs Q4-19 (some monthly aggregates at the previous page)

- **Hotels & restaurants** are down 10% vs Q4-19. Culture & Entertainment are up 3%
- **Administrative & support services** (like staffing & travel agencies, cleaning, canteens, leasing etc) are down 4%, following a tremendous growth in Q4, up almost 25%
- **Transport** -5%, due to personal transport (bus, trains, airlines), after a 9% growth in Q4
- **Construction** is far weaker than we have assumed, 3% down vs. Q4-19
- **Manufacturing** is down 1%, due to the decline in production in oil related industries, others are up 6% vs Q4 19
- **Postal & courier activities at the top of the list**, +18%. We have all seen them around – but growth is now slowing
- **Fisheries & Aquaculture** at no. 2, up 16%, even after a 18% decline in Q4 (due the early start of the mackerel fisheries

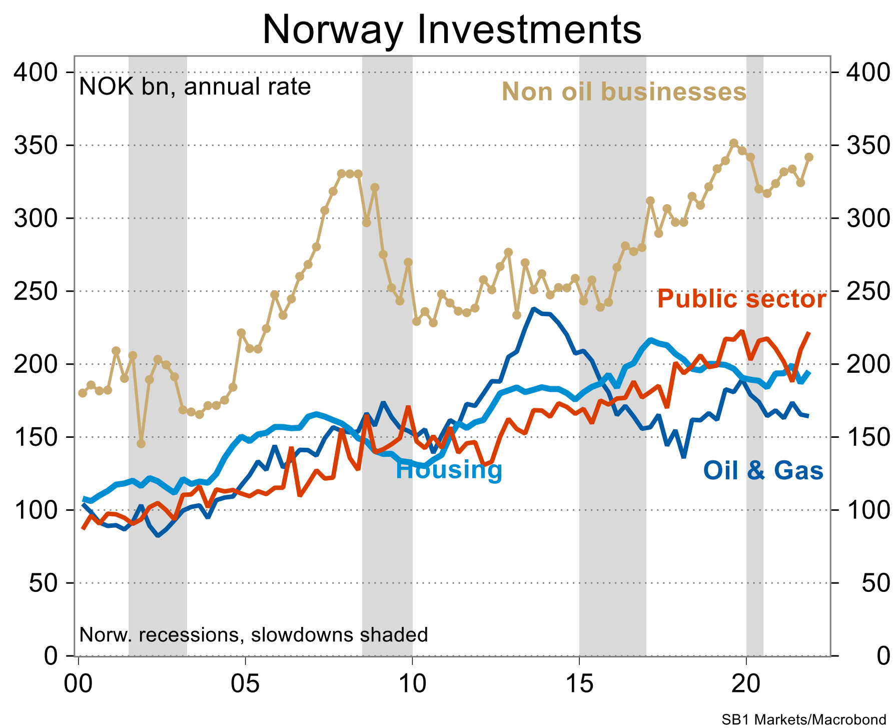
The hard-hit service sectors still a 0.5% drag on Mainland GDP in Q4

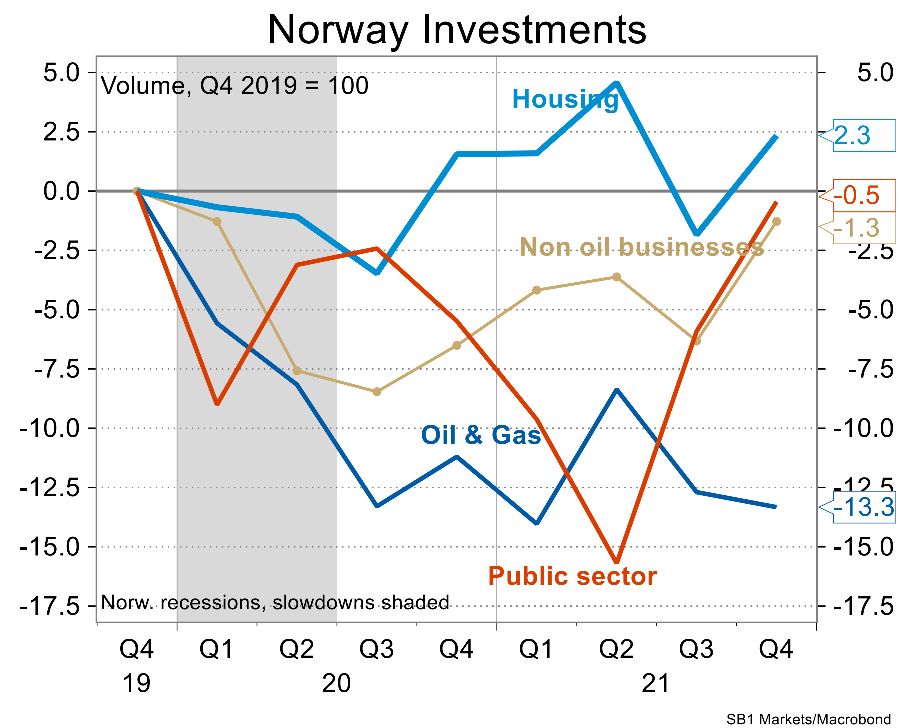
Construction is on the downside too





Investments mostly up in Q4, oil investments revised down

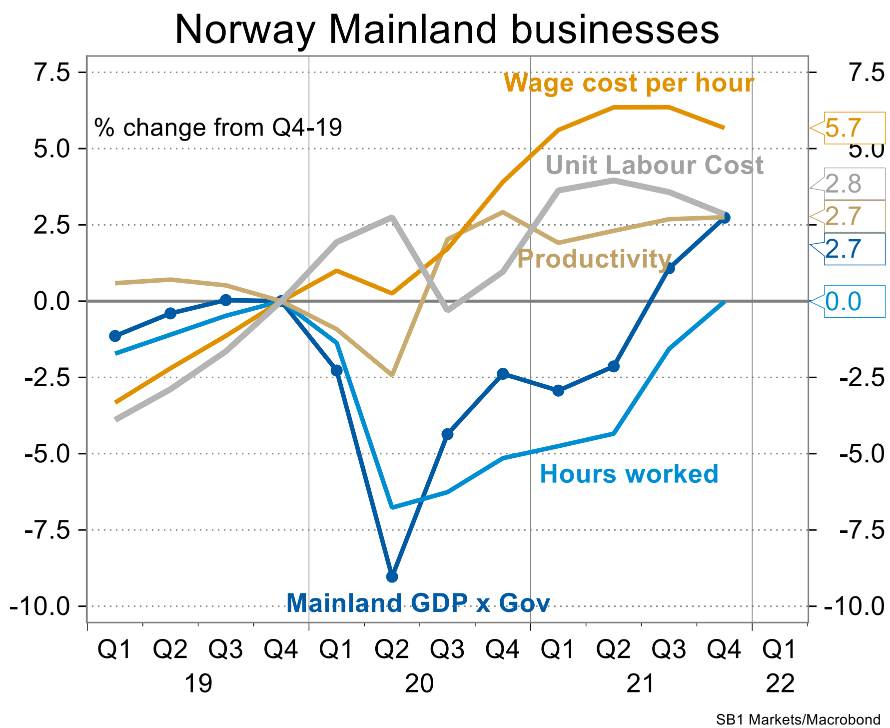


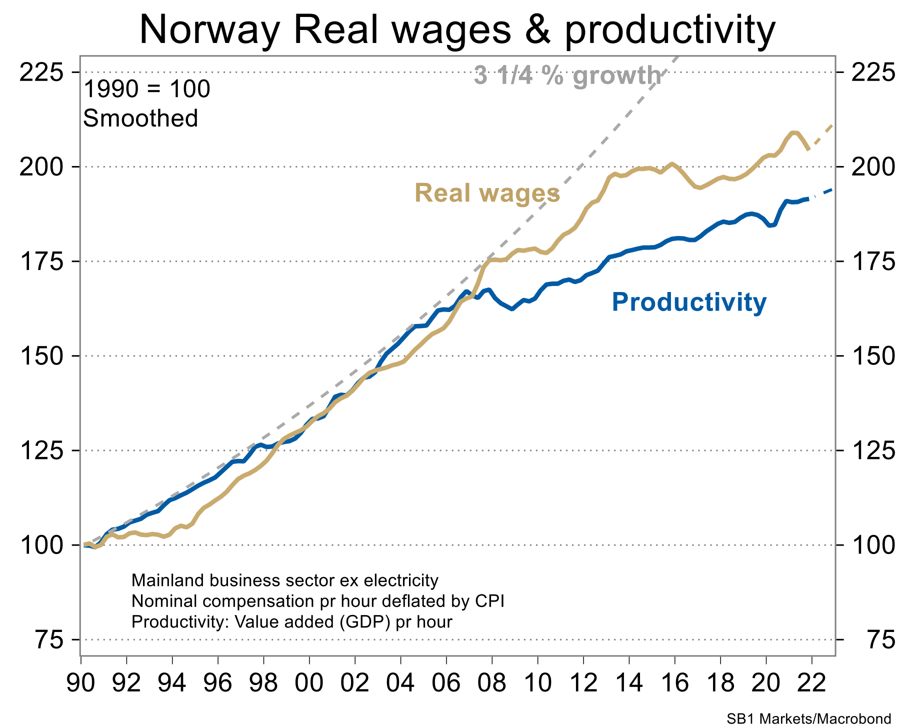


- Both Mainland business, housing, and oil sector investments were heading down before the corona virus hit as signaled by investment plans/surveys (manufacturing & oil)
- Housing has been rather strong through the pandemic, others fell significantly. Housing investments fell in Q3, to 1% below the Q4-19 level
- Oil investments have stabilised following a substantial downward revision of Q2 & Q3 – and investments fell again in Q4
- Public investments recovered sharply through H2

Unit labour cost inflation up a just a 1.5% pace since before the pandemic

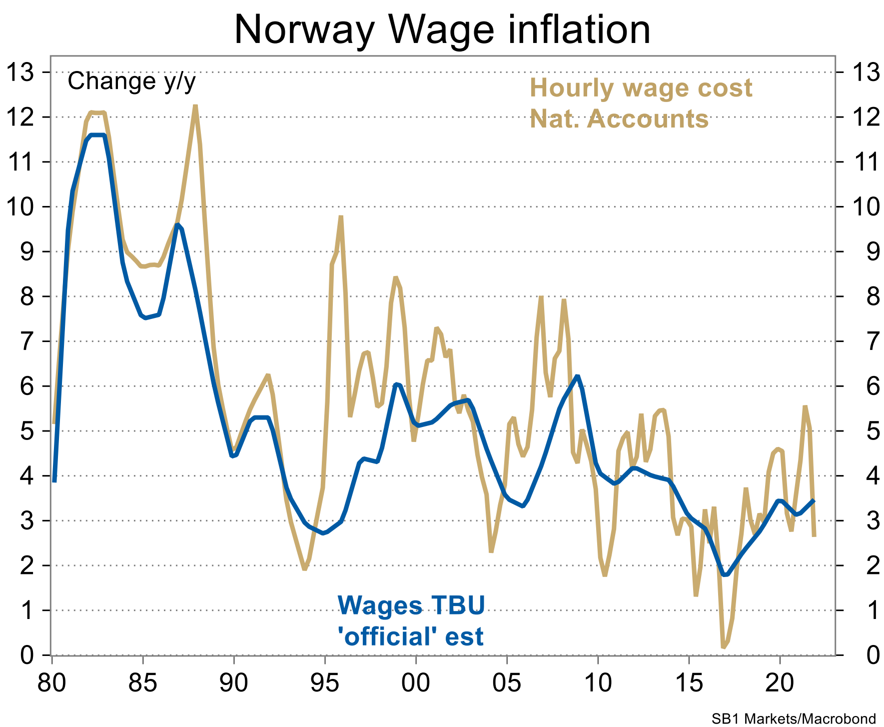
Wage inflation at 2.8% (in average in 2020 & 21)

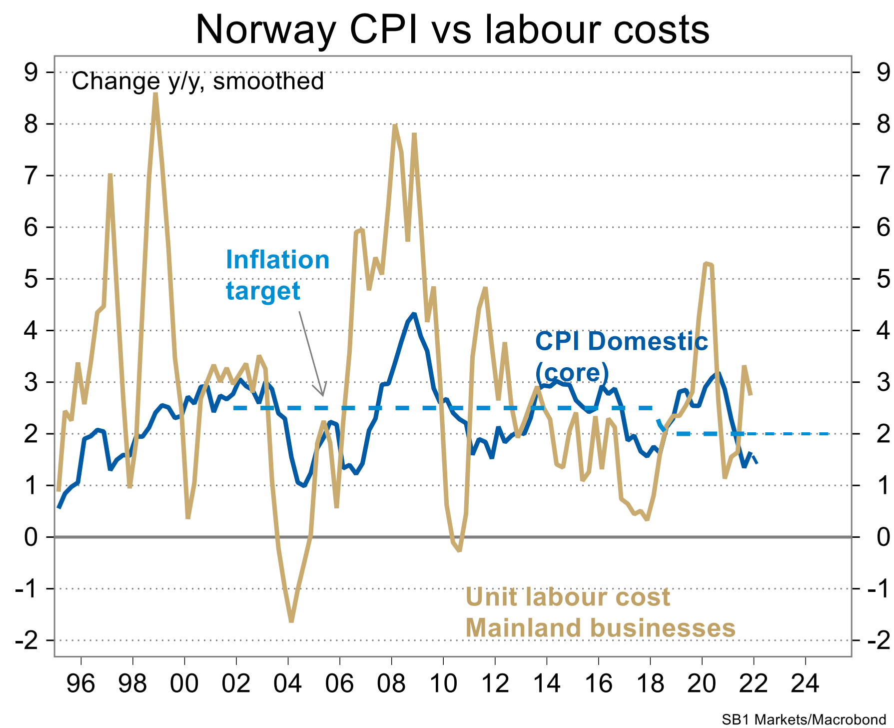




- The **average hourly wage cost** fell in Q4, and wage inflation is not that high, as measured in the National accounts, by 2.8%
- **Productivity** has increased at a 1.4% pace
- **Thus, Unit Labour Costs** have been increasing at a 1.4% pace
- **Real wages** fell in Q3/Q4 due to higher electricity prices

Cost inflation more or less in line with domestic core CPI inflation

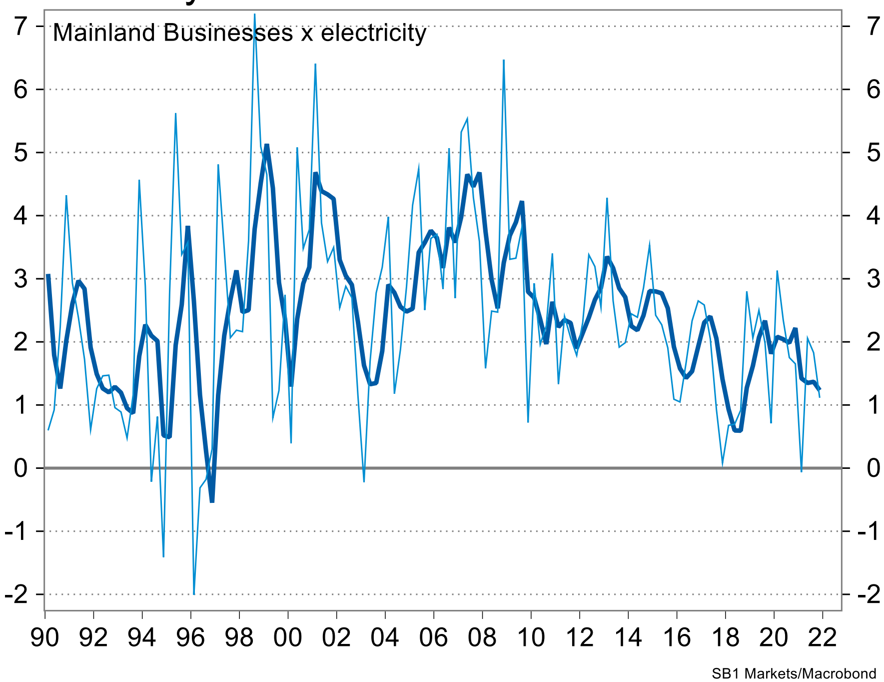




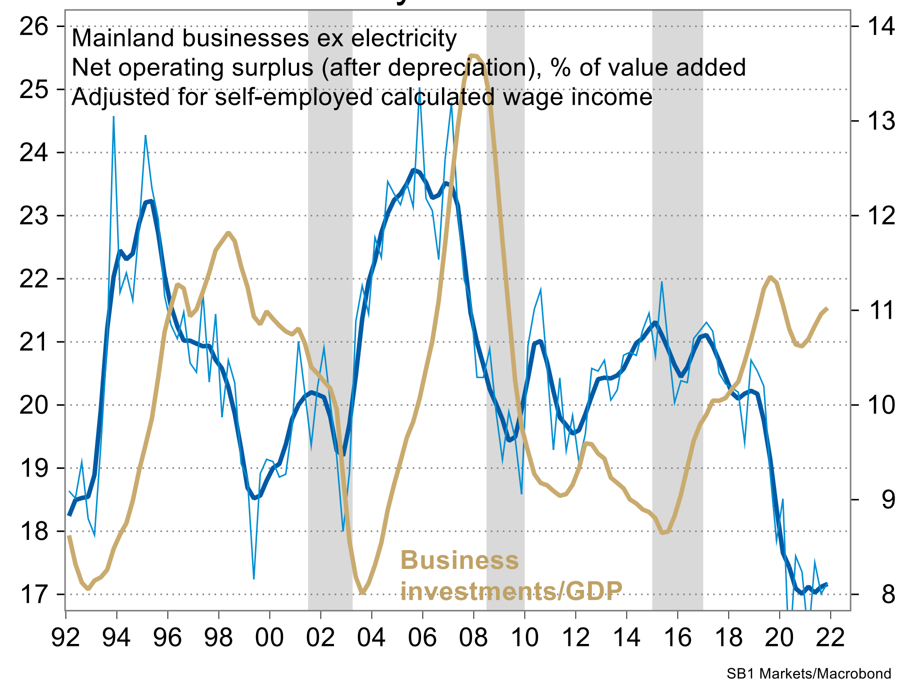
The profit share was under pressure, before corona – <u>and still is</u>

Operating margins have stabilised at a rather low level. Investments are exposed?

Norway Mainland Business GDP deflator



Norway Profit share

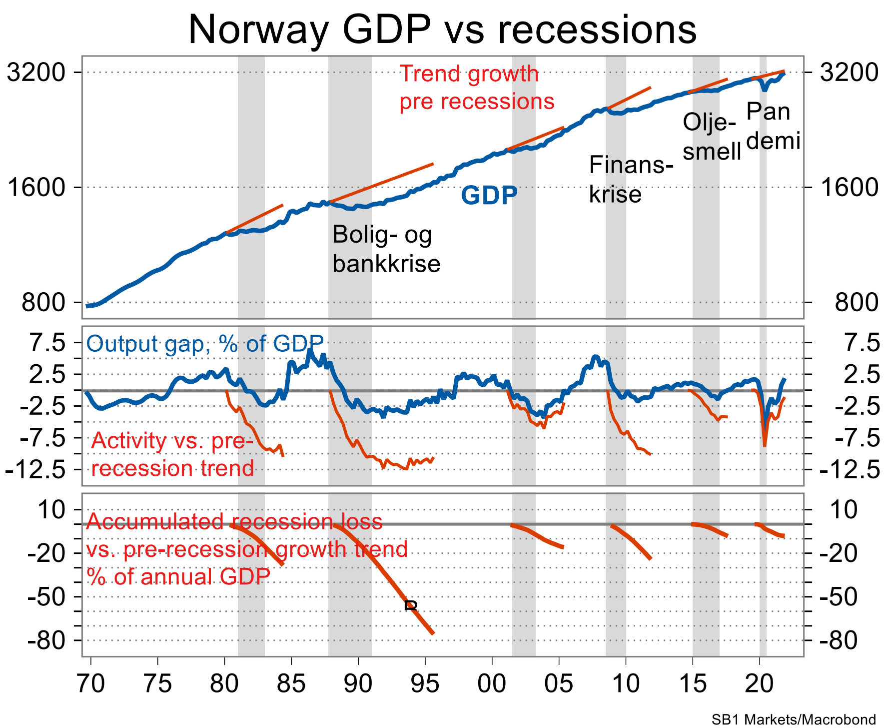


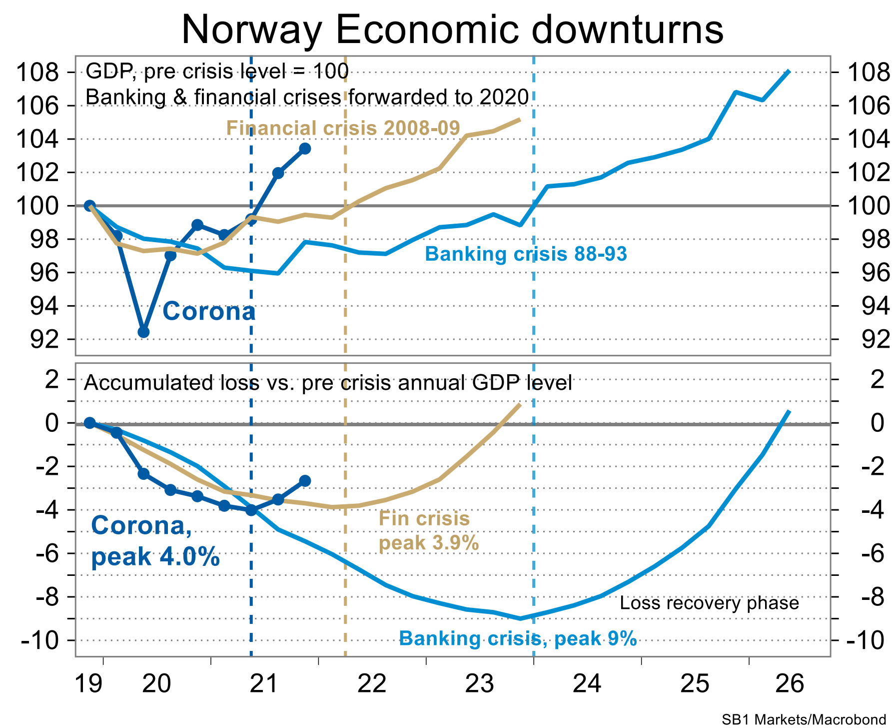
- The **Mainland business GDP price deflator** (ex the volatile electricity sector) has slowed to below 1.5%! There are huge differences between sectors. Manufacturing prices rose 0.4% last year (value added deflator)
- Unit labour cost (wage growth – productivity growth) is marginally higher (at 1.4%), and the <u>gross margin is still slowly deteriorating</u>
- The **Mainland business (ex electricity) gross margin** level is low – which signals some risk vs the above average investment ration

SpareBank 1 MARKETS

The Big Picture: Not a normal downturn, of course

The deepest and shortest downturn has not created large economic loses

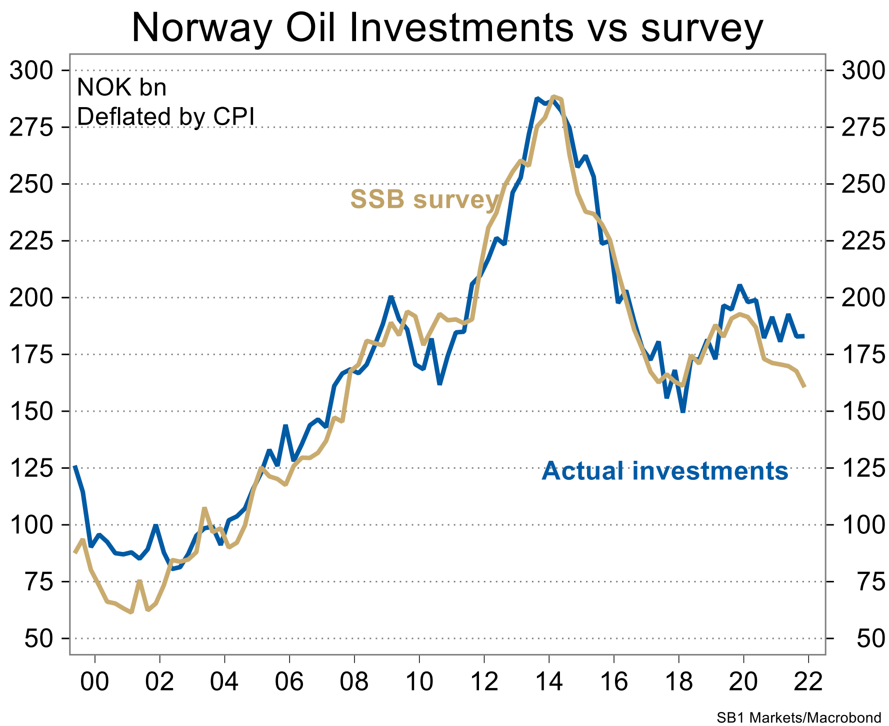


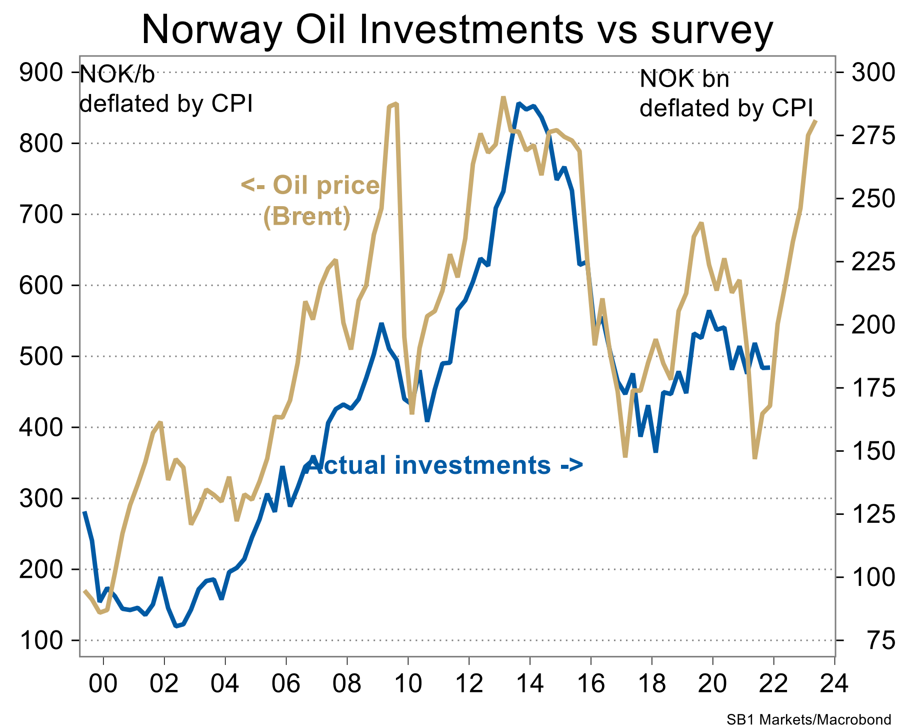


- A **pre-crisis growth trend** might be looked upon as a path that was expected among economic agents (household, companies, banks, market participants) before the crisis, based on their adaptive expectations. The loss vs this trend line is the economic/income loss vs. these expectations, a measure of the 'disappointment' (income, consumption, corporate earnings, etc)
- The accumulated loss vs the **pre-pandemic growth trend** is so far less than 10% of one year's GDP. The accumulated loss vs. the pre-pandemic GDP level peaked at 4%
- **The Banking Crisis** (88-93) created far longer and in sum much larger losses, in sum more than 70% of GDP (depending on when you stop counting, we do it rather arbitrary when our post the fact output gap is closed, in 1995). The loss vs. the pre Banking Crisis GDP level peaked at 9%
- The losses during and after the **Financial Crisis** (2008-2010) were substantial vs. the pre-crisis trend growth path, accumulated up to 25% of GDP before the output gap was closed in late 2011. However, the accumulated loss vs the pre FC GDP level was just 4% - in line with losses during the pandemic downturn
- GDP is now, vs. the starting point of these 2 earlier recessions, 4 – 5 ½ % ahead (upper panel to the right)

Oil investments: 2022 will be the local bottom

The temporary tax relief and high oil prices will lift investments substantially in 2023 (and ‘24+)

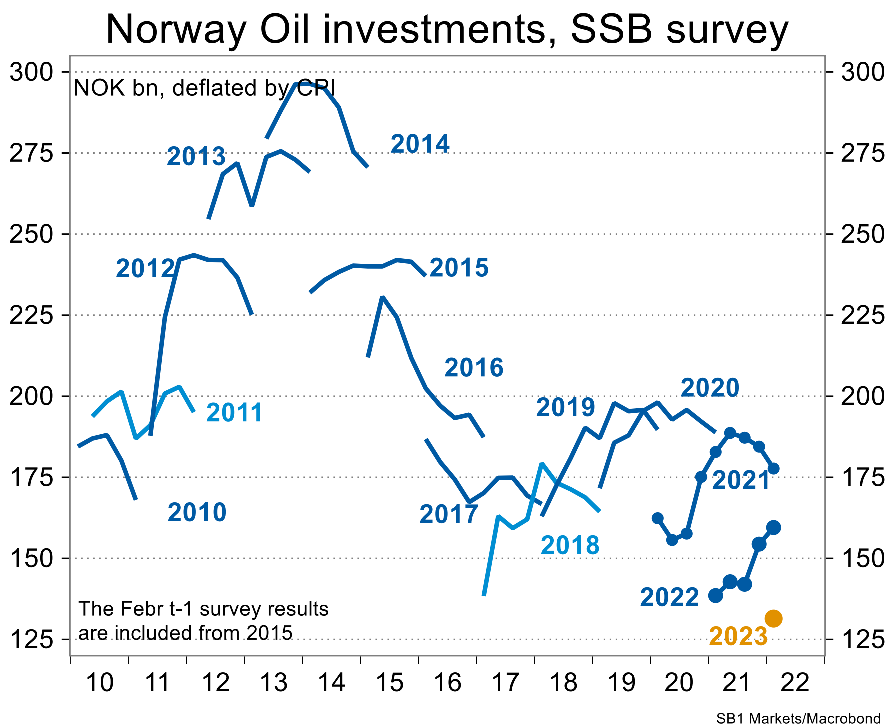




- Oil investments fell 3% in volume terms in **2021.** Nominal spending rose by 2%
- **Oil companies lifted their 2022 investment estimate** by 3% to 160 bn. The estimate is still 8% below the equivalent 2021 estimate. Several investment projects will be added to the list (a PDO delivered) before end of 2022in order to benefit from the temporary tax cuts decided in 2020 – and a higher oil price is also supportive. Still, we expect another 4 - 6% drop in investment volumes in 2020. In December, Norges Bank assumed a 6% volume decline next year
- **The 2023 outlook** is far better, even if the first estimate is down as investment at a large no. of projects not yet included SSB’s survey will be added the coming quarters

2022 oil investments revised up but probably still a decline next year

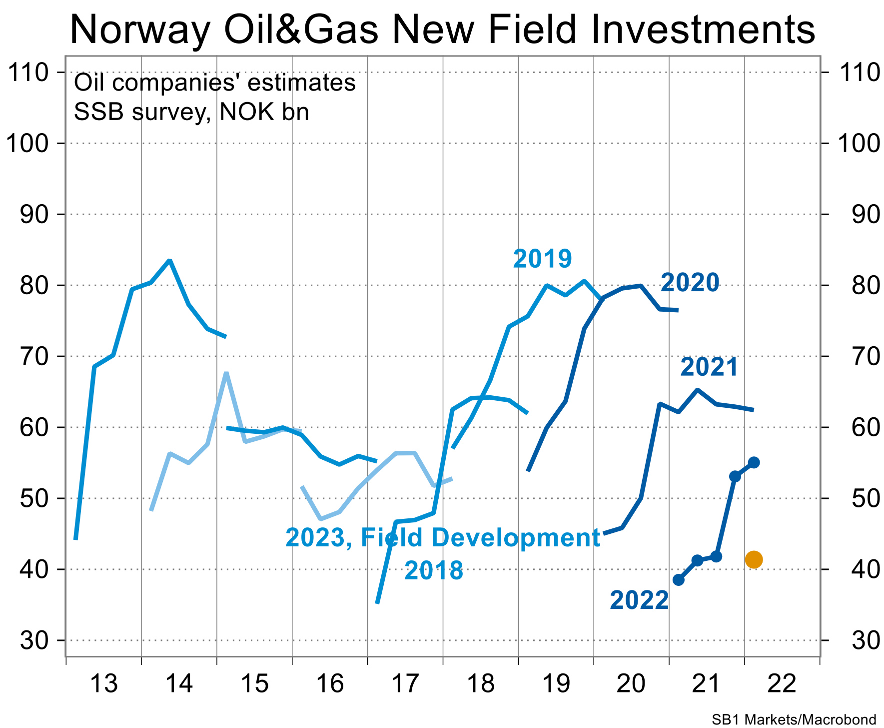
Even if more projects will be added due to the tax relief. The 2023 est. will be revised much more

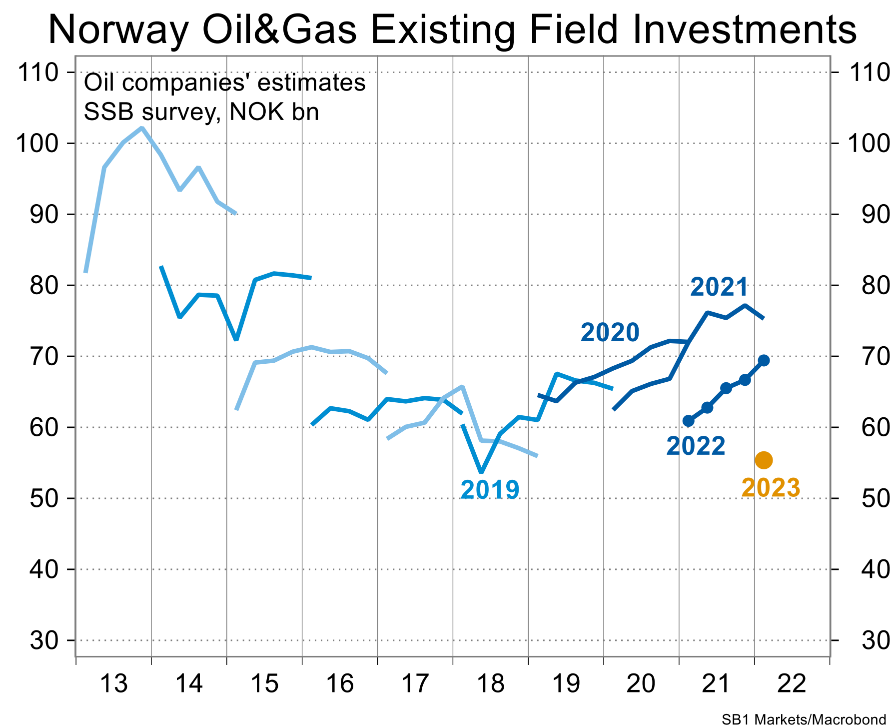


- In SSB's Q1 oil & gas investment survey, companies reported a small decline **<u>2021</u> investments to** NOK 178 bn. In volume terms, investments fell 3%, according to National Accounts
- **The 2022 investment estimate** was revised up by 3% to NOK 160 bn, still down 8% vs the equivalent '21 estimate, slightly below our expectations. A large number of projects will be added before the end of 2022 in order to benefit from the temporary cut in oil taxes, but we still assume a small decline in value terms y/y in 2002, or 5% in volume terms.
  - » Both investments in new and existing fields are expected down in 2022
- **The first 2023 estimate** was down 6% vs the initial 2022 forecast, at NOK 130 bn. However this estimate is rather irrelevant due to the temporary tax cut. 2023 spending on these projects will be added to the investment as soon as oil companies delivers their applications
  - » The increase in the oil price is also a good argument for expecting higher investments next year
- **Conclusion:** A short and shallow downturn in oil investments – then another boom, at least a mini boom

Companies lift their new field inv. ‘22 f’cast by NOK 2 bn to 55 bn, more to come?

Some projects will be added but probably not sufficient to prevent a decline in 2022

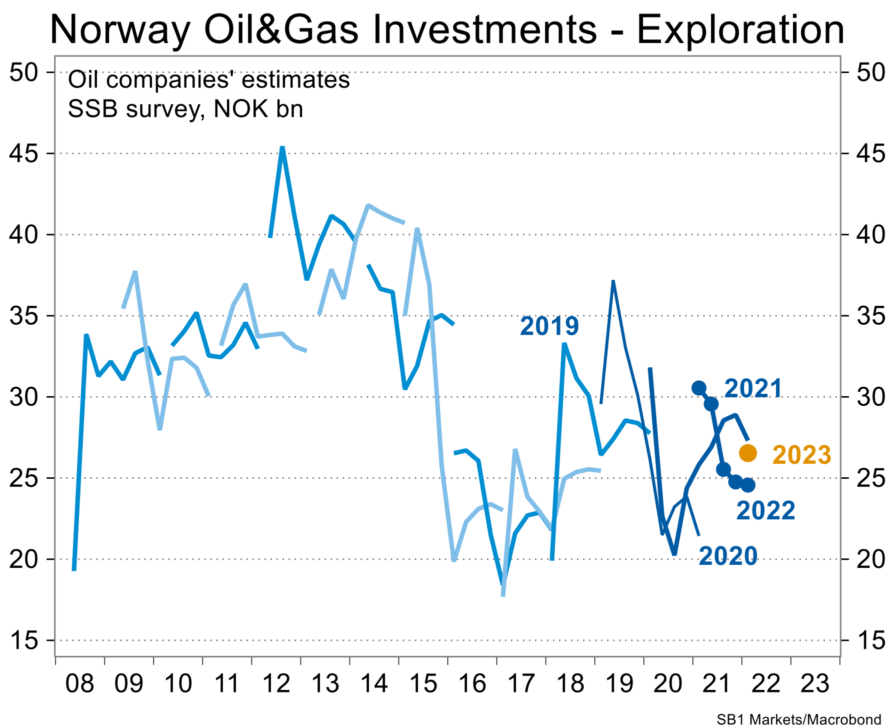


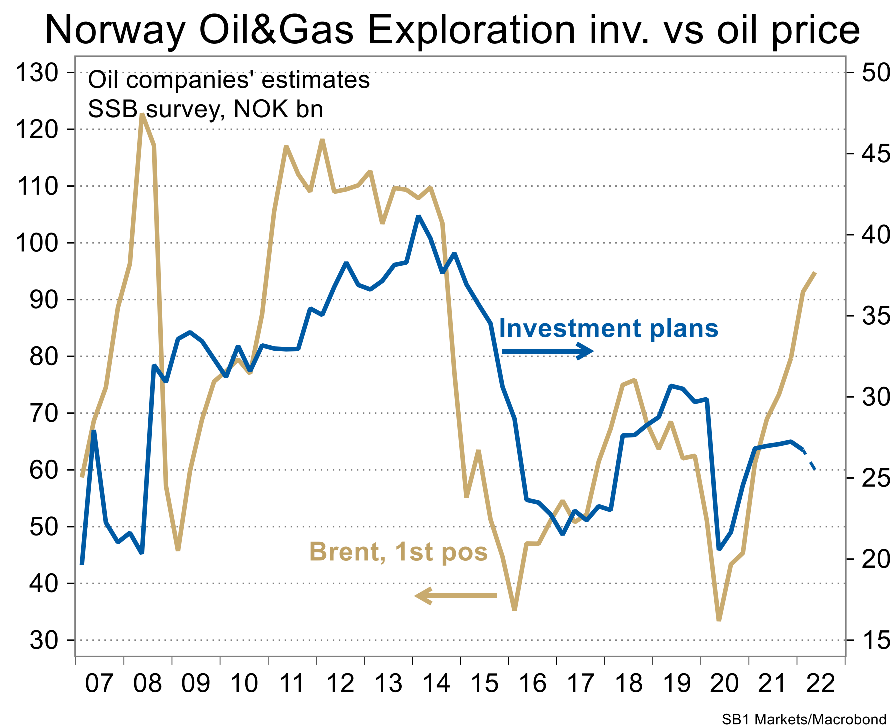


- **Investments in new fields**
  - » 2021: Oil companies report an 18% drop in 2021 spending vs 2020, as big projects were completed in 2020 (like Johan Sverdrup)
  - » The ‘22 forecast was revised slightly up (without any new projects added). The current estimate is down 12% vs. the 2021 outcome. In order to benefit from the temporary tax subsidies, companies will have to submit PDOs’ to the authorities before the end of the year, and a huge no. of projects will seek approval during the year. When the application is delivered, spending in 2022 will be revised up – and 2023 even more
- **Investments in fields on stream**
  - » The ‘22 forecast was revised upwards, in a normal manner. Companies signal a 8% decline vs. 2021

Spending plans for exploration & concept studies down in 2022

A bit surprising, given the rush for delivering PDOs before the end of the year. More spending in ‘23?





- More spending may be included when oil companies will deliver PDO’s for a large number of projects before end of 2022
- Anyway, the current ‘22 estimate is 10% down vs. the 21 estimate
- The first 2023 estimate is below the first 2022 forecast – above the current 2022 estimate

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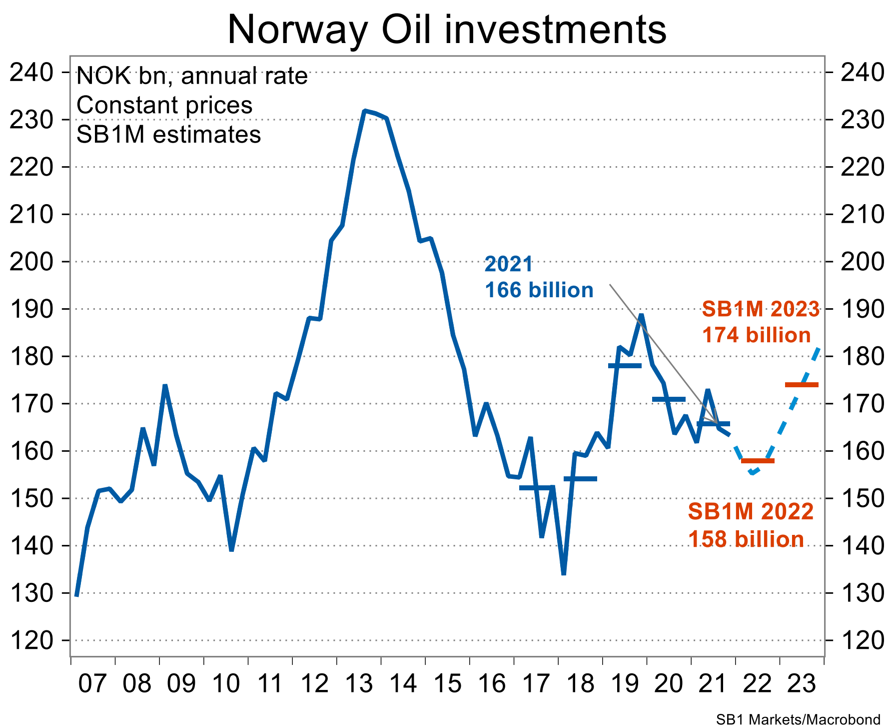
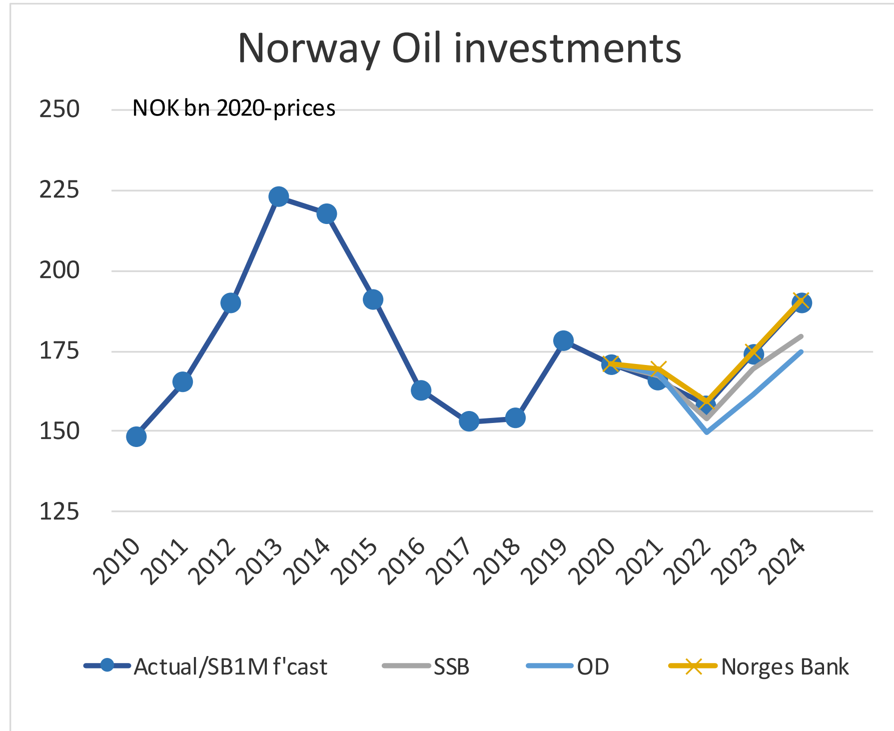
Oil investments probably further down in 2022 – before the next mini boom

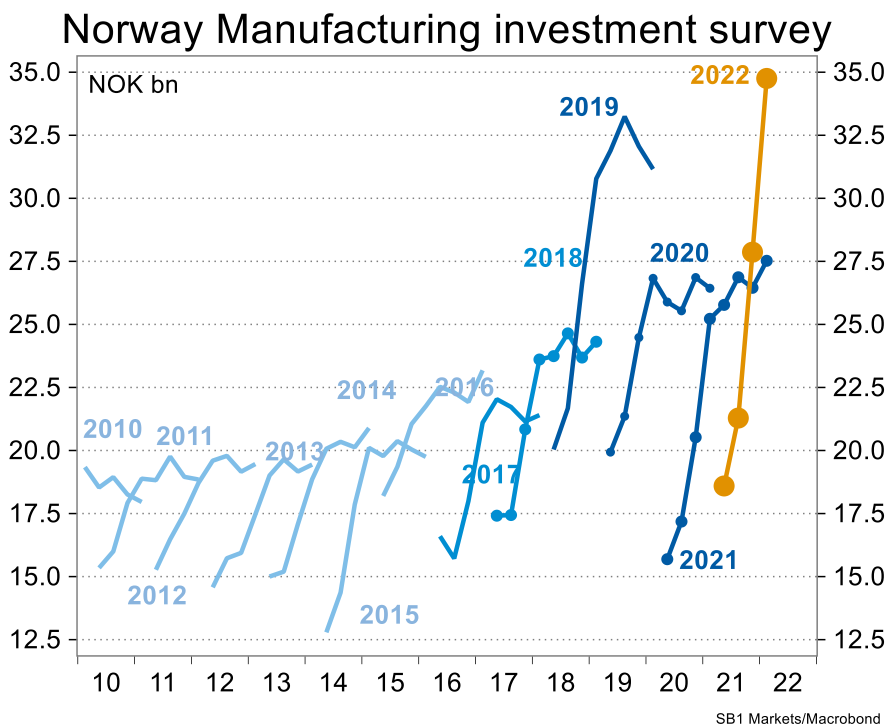
The surge will come later, from 2023

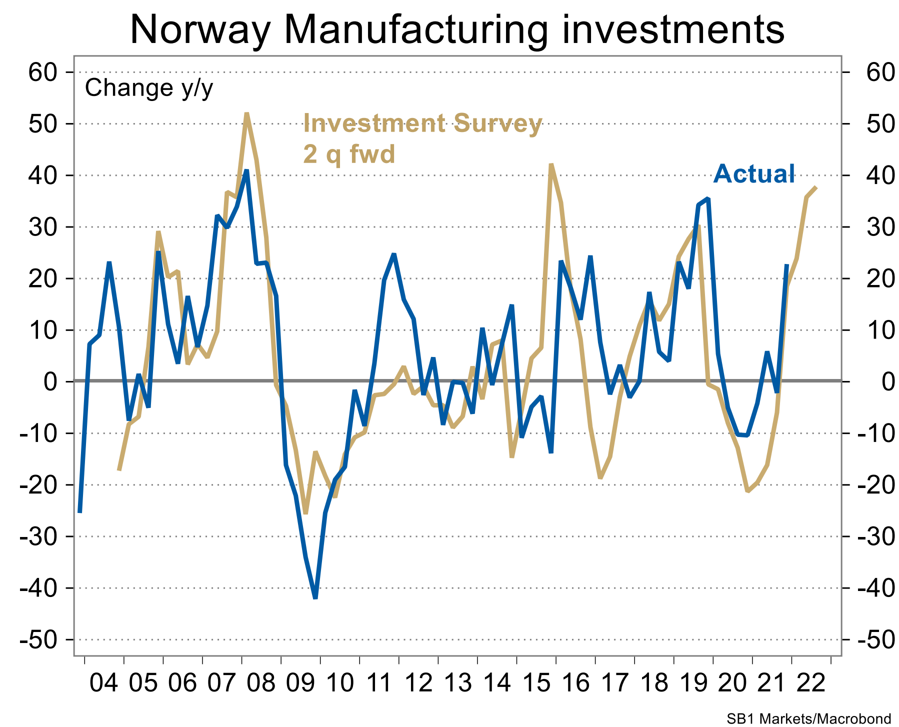




WOW, manufacturing investments through the roof! Very strong growth signalled

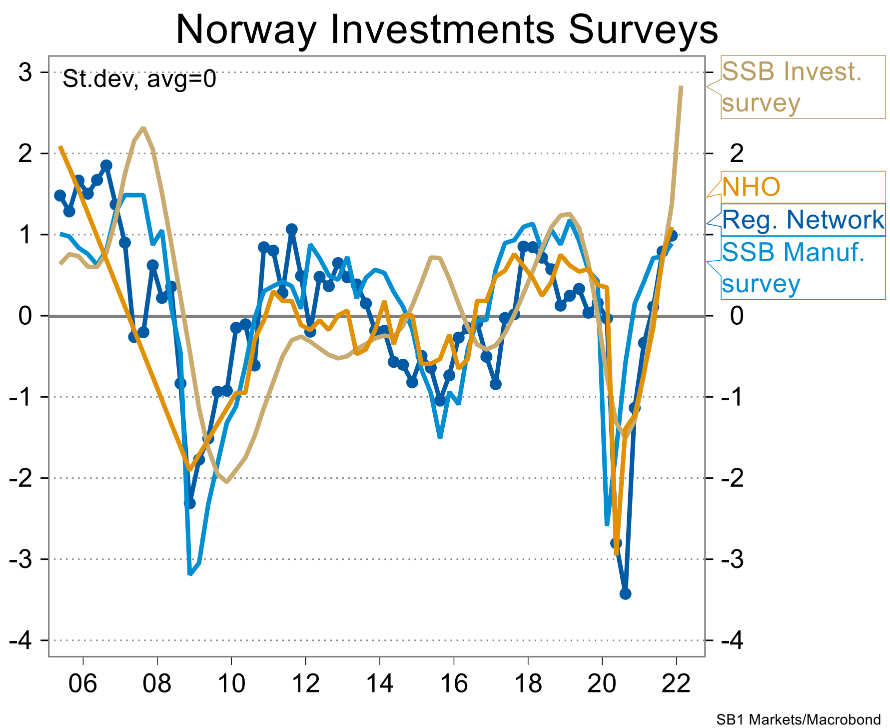
The 2022 investment estimate revised up by 25% to Feb from Nov, the steepest rise since 1985!





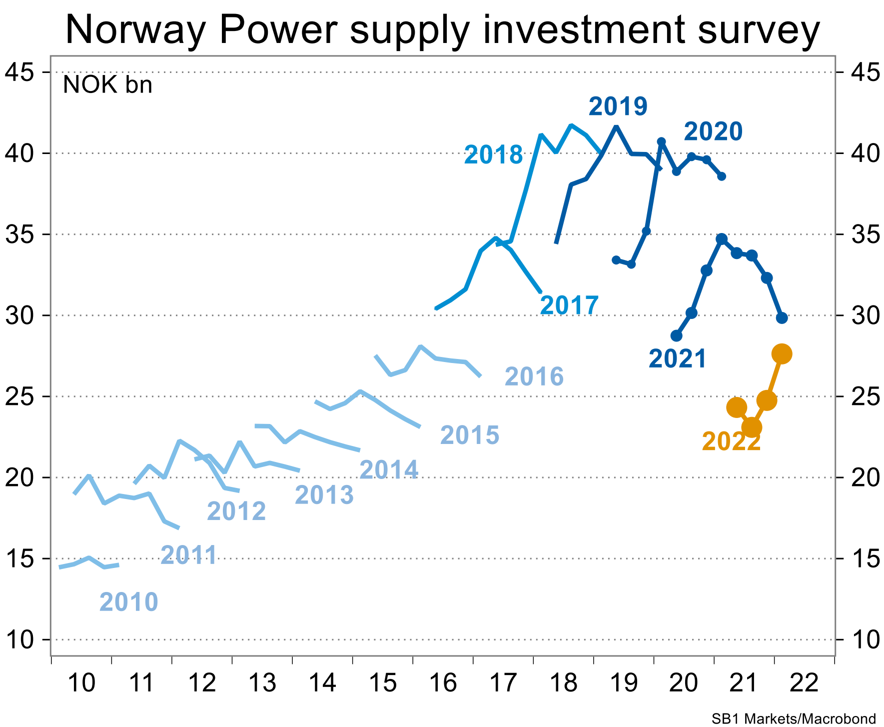
- Manufacturing companies report a 7% growth in **investments in 2021**, slightly better than we expected
- However, we do not expect the 25% lift in the **2022 forecast** to NOK 34.7 bn, following the 31% upgrade of the forecast 3 months ago – in sum 63% over 6 months, the 2nd largest upgrade ever (data from 1979). The increase from the equivalent 2021 forecast at 38% is the 3rd highest in history, just 1986 & 1995 were even stronger. A 30% growth in investments in volume terms in 2022 is not unlikely. Check chart 2 pages fwd
- **Computer/electrical equipment** contributed the most to the increase in the 2022 forecast vs the Q4 survey, and report investment plans at NOK 4.5 bn, up from 1.1 bn in 2021. Have couple of battery fabs been included?? Is it possible to spend that much money in 2022?
- **Non-ferrous metal industry** reports very aggressive 2022 investment plans too, NOK 6.5 bn vs 2.9 bn in 2021

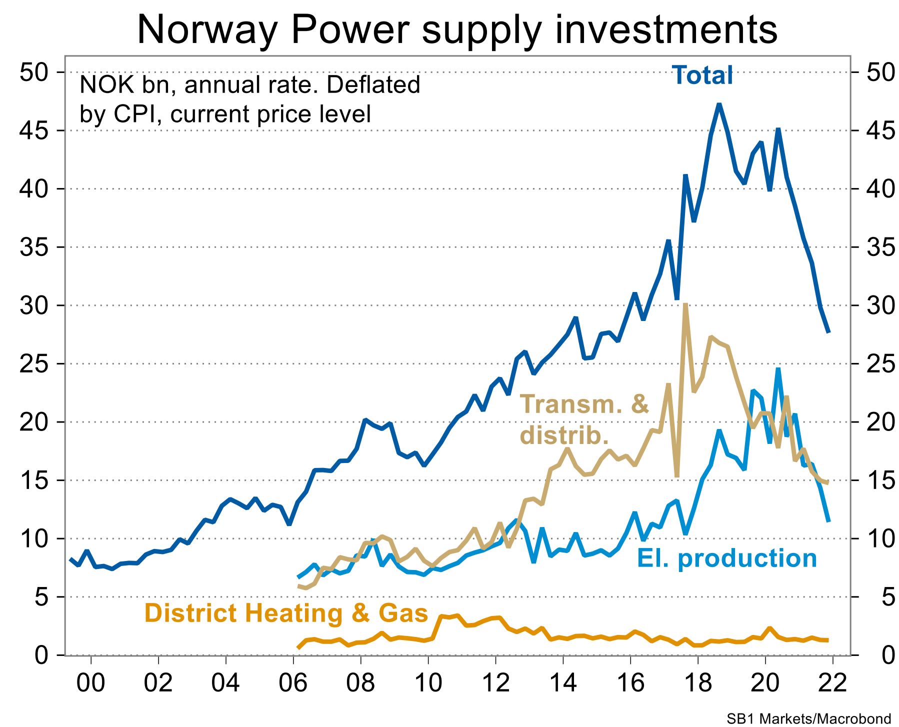
Other surveys are signalling strong growth in manufacturing investments



Power supply: 2022 investments revised up, level still low

Investments fell 23% in 2021, and the 2022 f'cast signals a further substantial (15%) decline

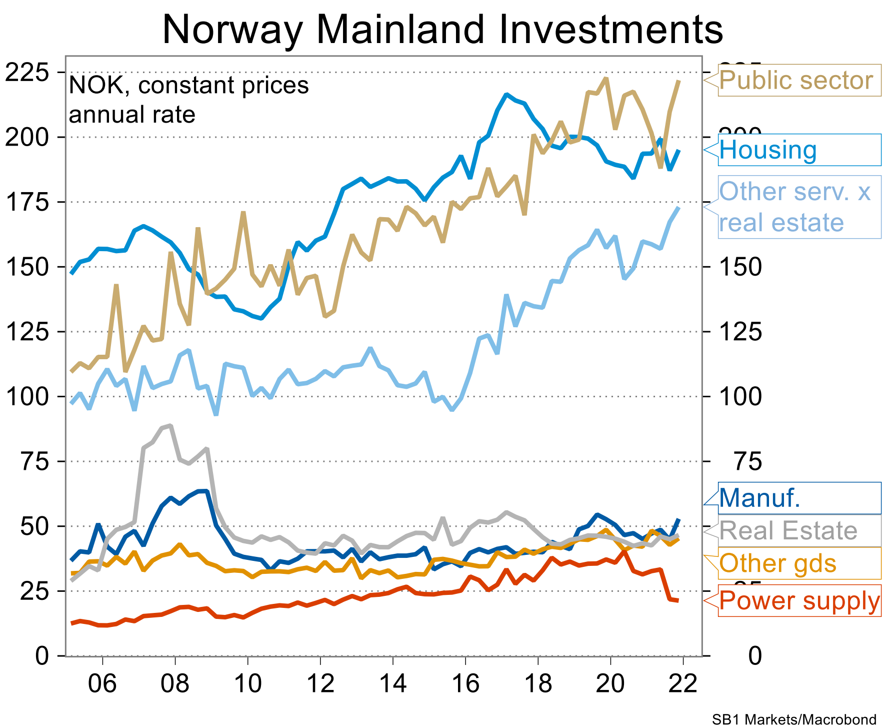


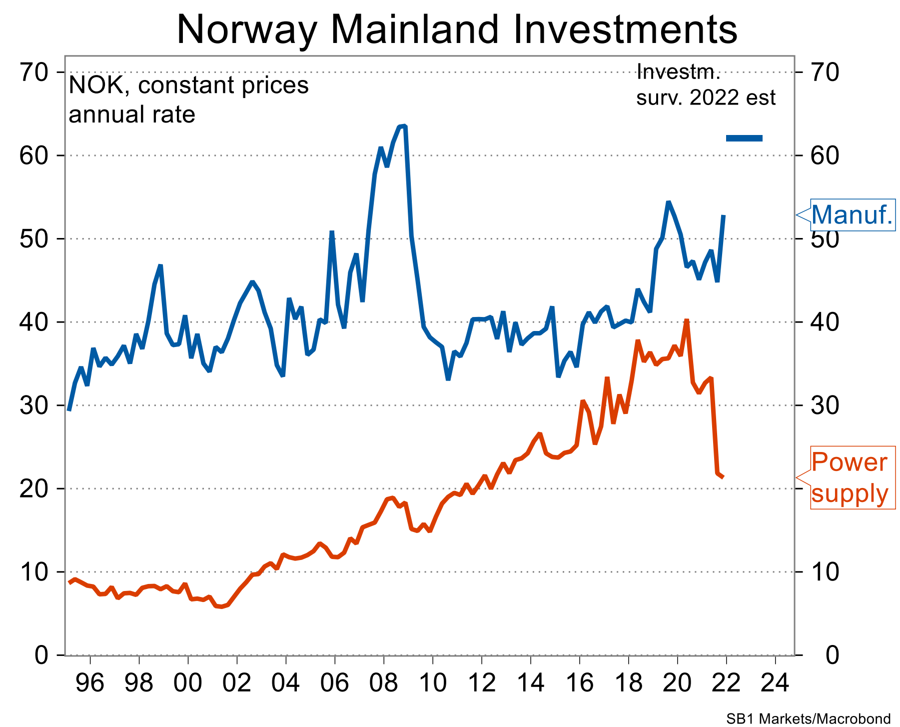


- Power supply (production & distribution) companies invested NOK 30 bn in 2021, down from 23% from the 38 bn level in 2020 (and 40 bn at the peak in 2018)
  - » Some big wind power projects were completed by the end of 2020, and few new projects have been added, contributing to the decline in 2021
- Companies lifted their 2022 investment f'cast by 3 bn (12%) vs their Q4 prognosis, well above the 5% average revision in the Q1 survey. The estimate is 20% below the equivalent 2021 forecast (and 7% down vs. the final 2021 outcome. From the Q1 survey, estimates are normally revised down, by some 7% in average
- Until 2018, power supply investments had more than quadrupled since early 2000, by more than 10% p.a on average. The investment level as % of Mainland GDP was above 1%, the highest in decades. Both production & transmission have contributed. <u>To 2022 from 2018, investments may decline by 36%</u>, in nominal terms, and more in real terms. <u>Will the green transition turn the tide? Quite likely</u>

Manufacturing and power supply investments are diverging sharply

Power supply investments were very low in both Q3 and Q4. Manuf. on the way up – to the sky??

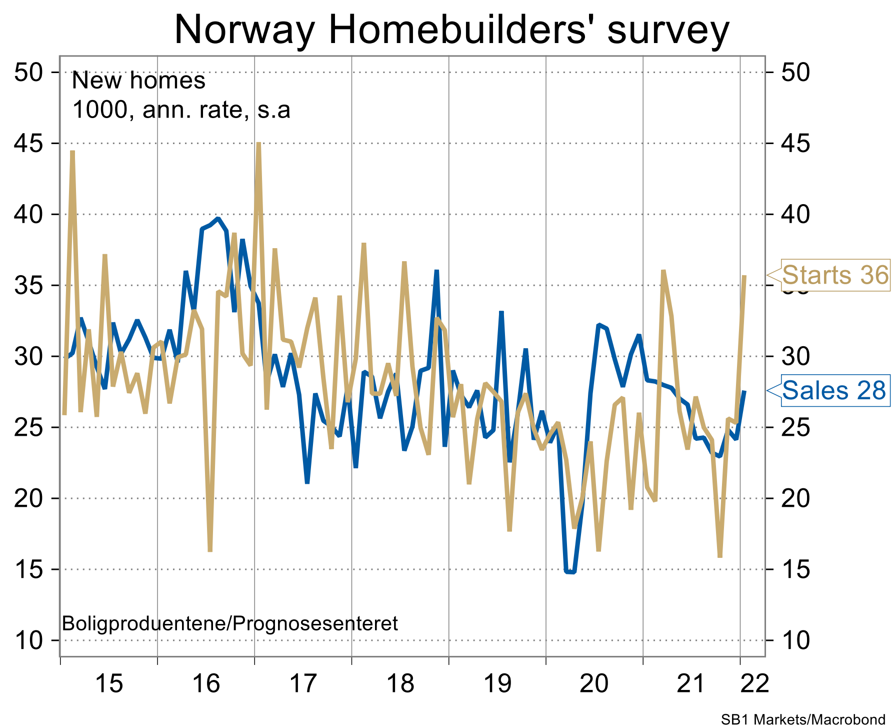


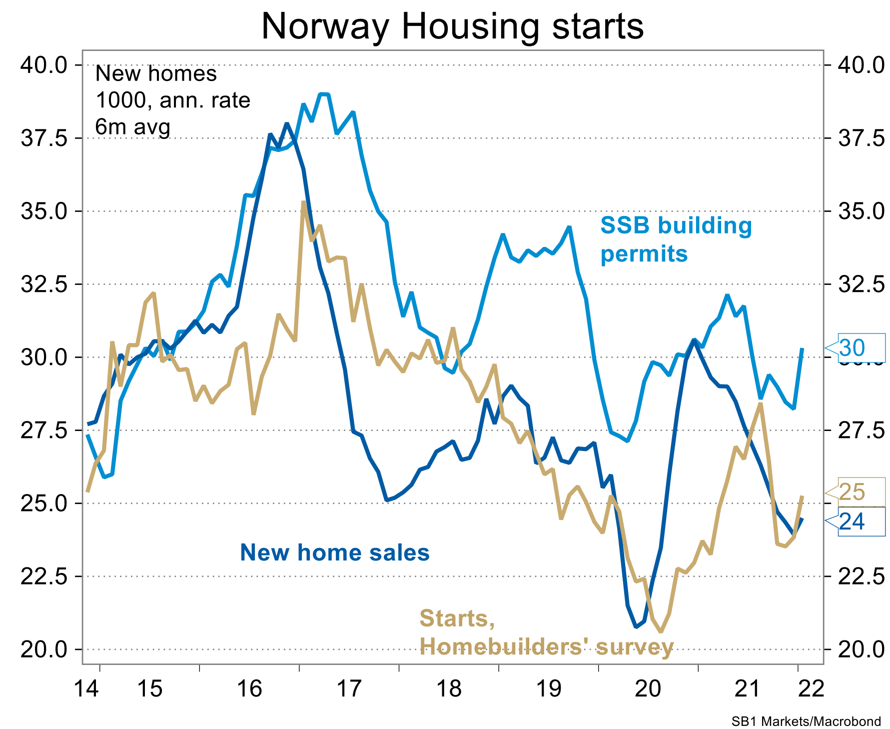


- SSB's investment survey signals a huge leap in manufacturing investments in 2022, + 30%, in volume terms to NOK 62 bn?

New home sales sharply up in January, starts even more

Sales/stars were on the weak side during H2-21 but recovered in January

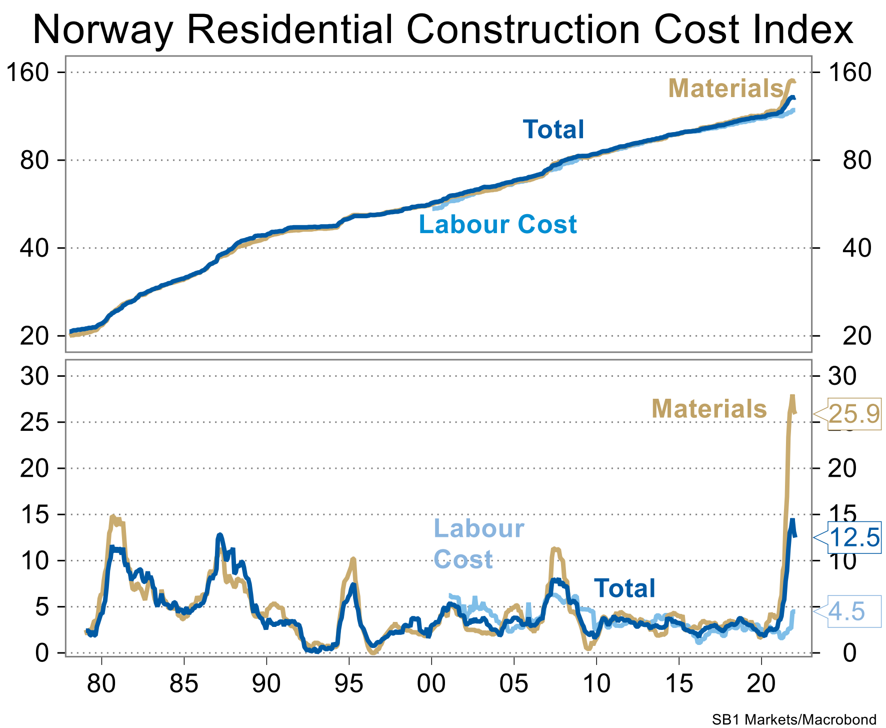


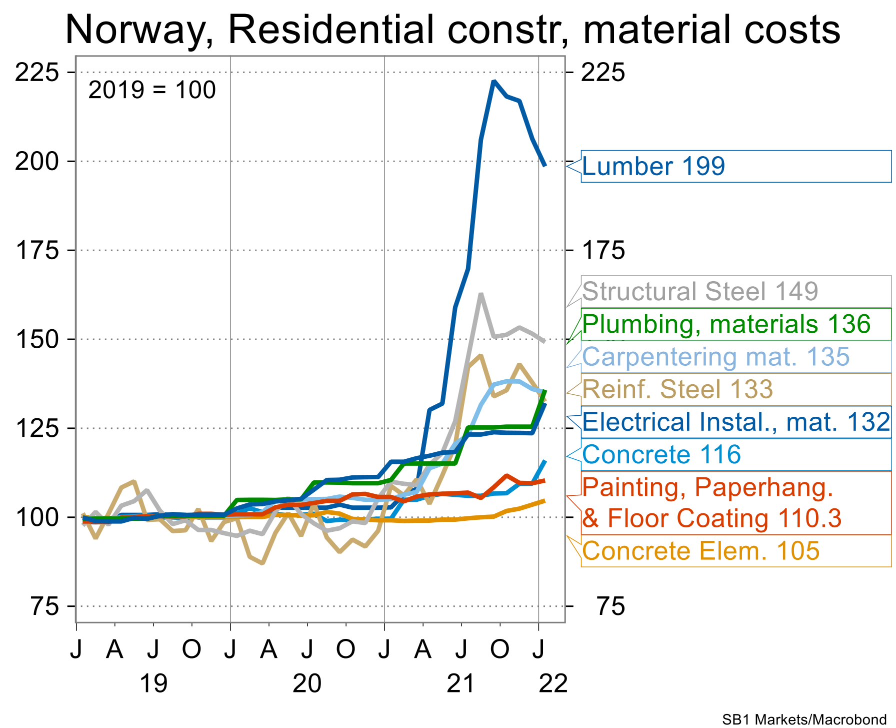


- **Boligprodusentene (Home builders)** has blamed higher material and land costs for the decline in sales, not an unreasonable hypothesis (but strangely enough, higher interest rates has not been mentioned). However, as existing home prices are substantially up over the past year, new homes are probably still competitive
- **SSB** also reported at decline in starts in (building permits) last year but the going rate during H2 was 30', which is not a low level
  - » The two stats for housing starts are far from identical. Many single home projects are not included in the Home builders' data. Nursing and student homes are not included either

Cost pressure in the construction sector has probably peaked. But..

Several pries rose further in January, like plumbing & electrical instal. materials, and concrete





- In total, **material prices** have flattened the past 3 months, as lumber prices have fallen 10%. The annual inflation rate has moderated slightly but remains at 25.9%! (The previous record was 15% back in 1980)
- **Labour cost inflation** accelerated to 4.5% y/y in Q4 from 2.6% in Q3, to the highest level since 2009 (Labour costs are calulcated just quarterly)
- Including labour costs, the **total building** cost index is up by 12.5%, down from the ATH at 14.6% at the peak in Oct

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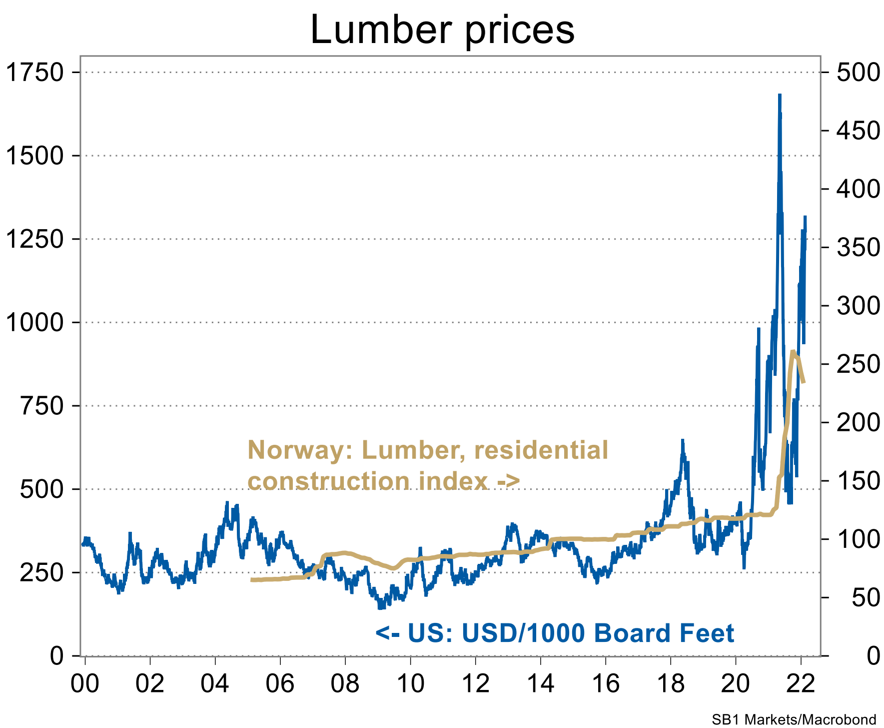
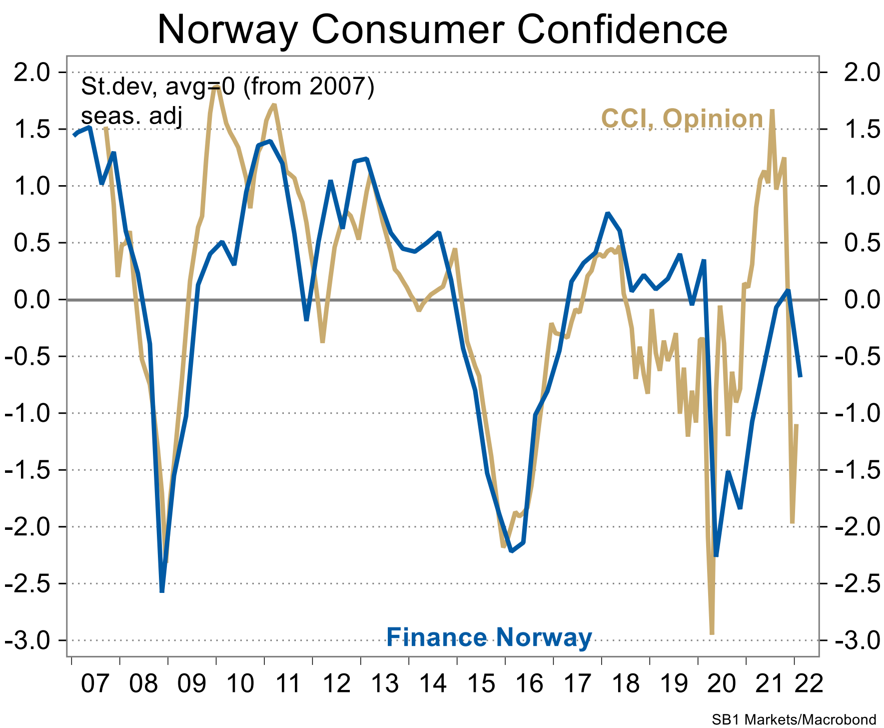
New warning: In the US, a 2nd lumber wave!

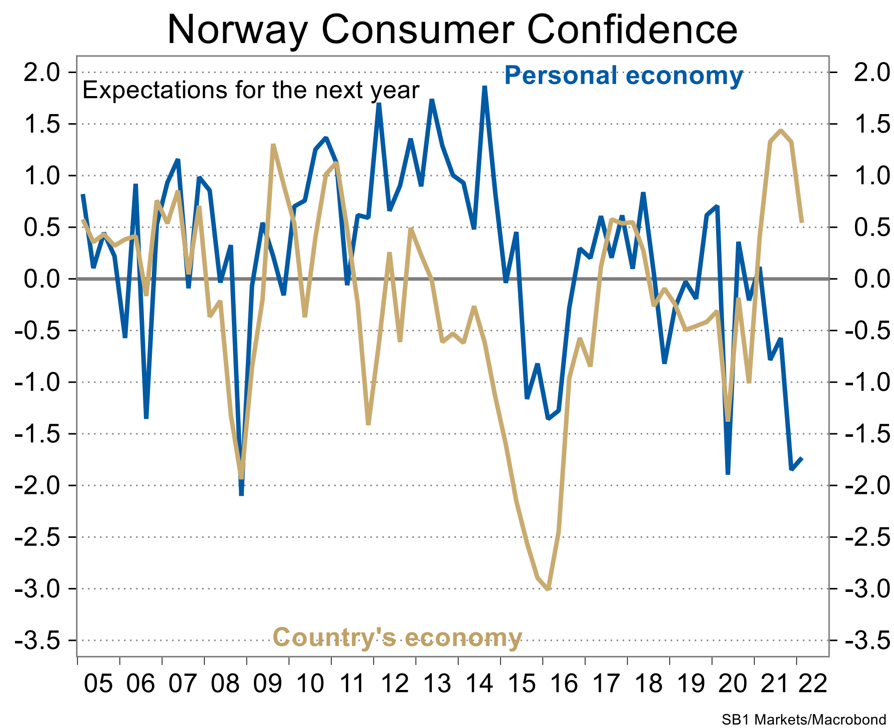
Lumber (2''x4'') prices have shot up again, to USD 1300/100 board feet, from USD 500



Finans Norges' Q1 consumer confid. down to below par

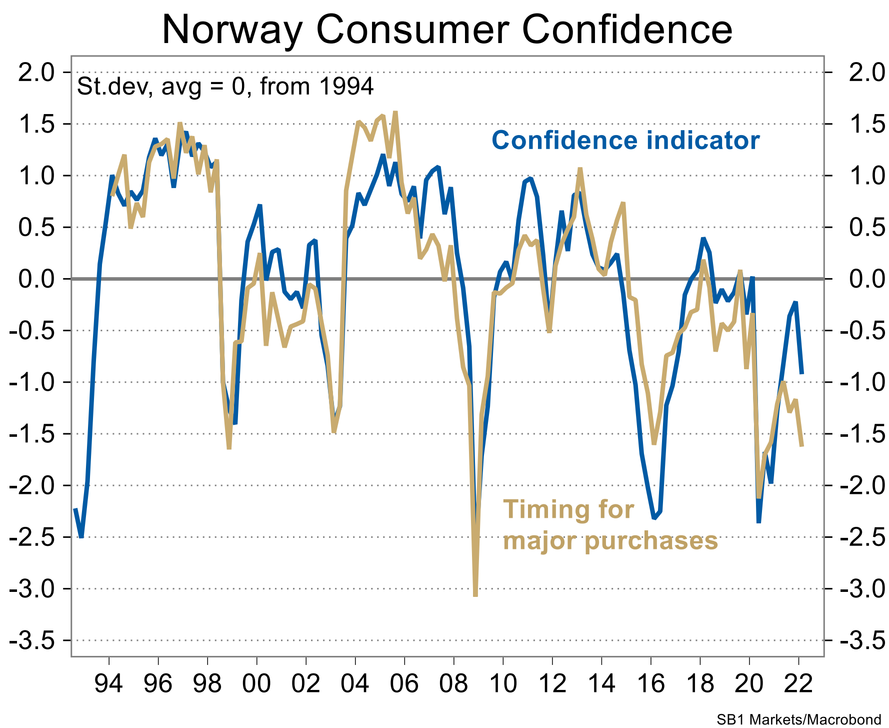
The index down 0.8 st.dev to -0.7 below avg, as household became less confident in the national ec.





- Finance Norway's quarterly **consumer confidence index** was weaker than we assumed in Q1
  - » However, a sign was given: the monthly CCI survey from Opinion fell sharply to 2 st.dev below par in Dec from +1.3 in Nov – and just partially recovered in Jan, to 1.1 st.dev below avg
- **Households' expectations** of their own economy stabilised at low level in Q1. The decline in Q4 must have been due to the 'electricity shock' and the recognition of higher interest rates. **Expectations for the country's economy** took the overall index down in Q1, but remains above average
- **Big item purchases** are still out of favour, as is travel. The only thing households want to 'spend' more money on: investments!

Still not the best timing for major purchases



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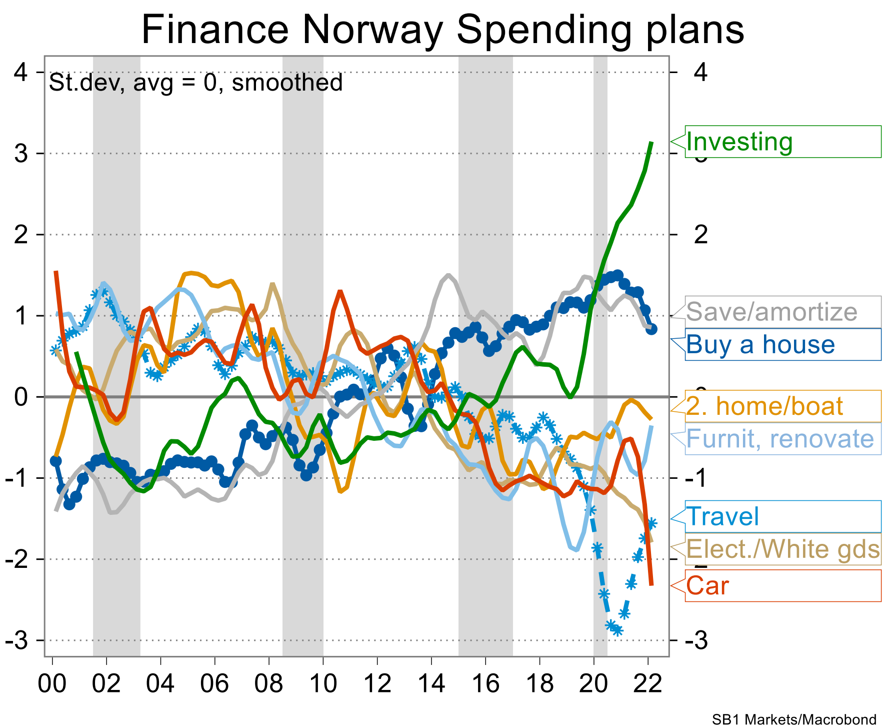
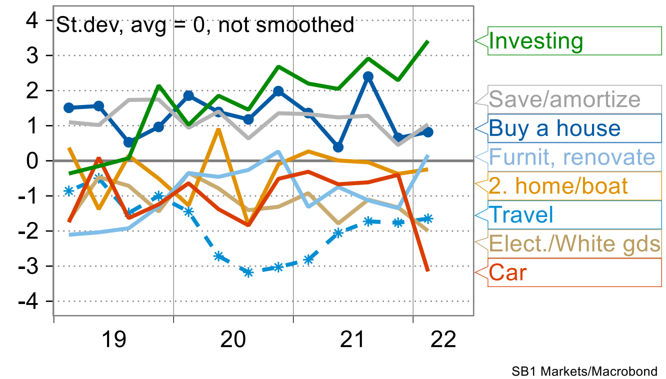
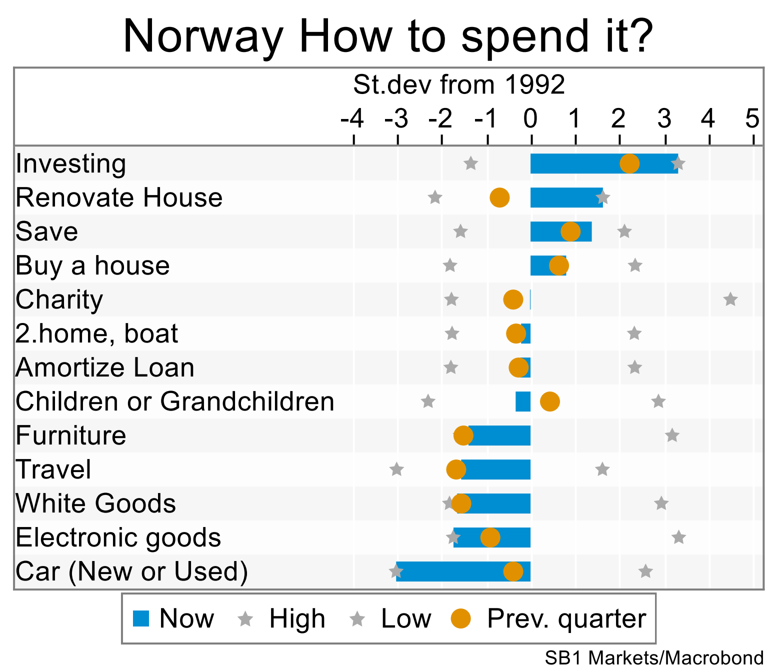
It's time for 'investing', like never before (with a P/B ratio at OSEBX 2.7??)

House buying plans have come down, still above par. No cars, and still less travel than normal



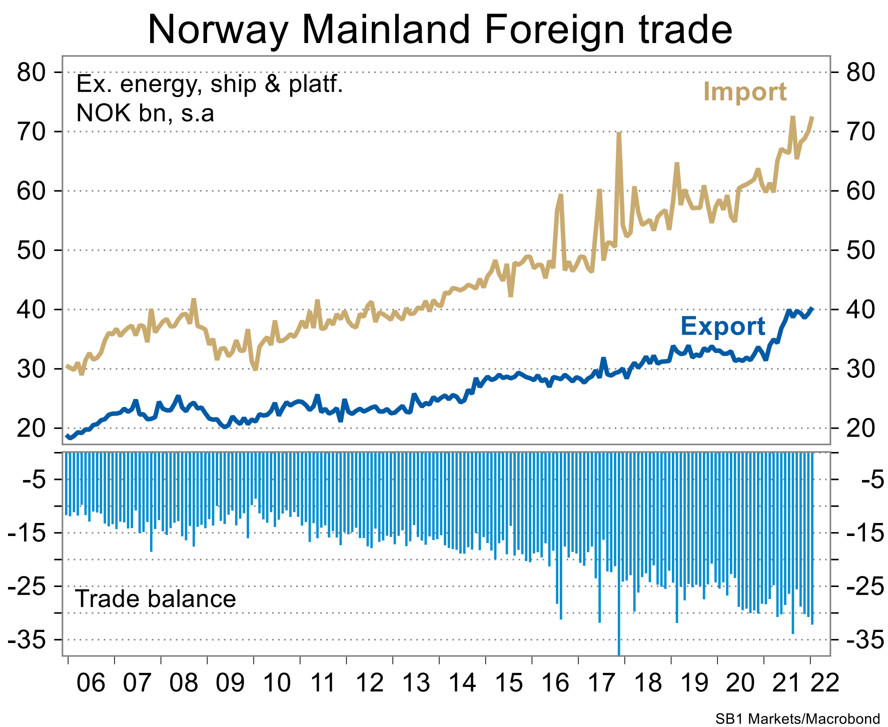


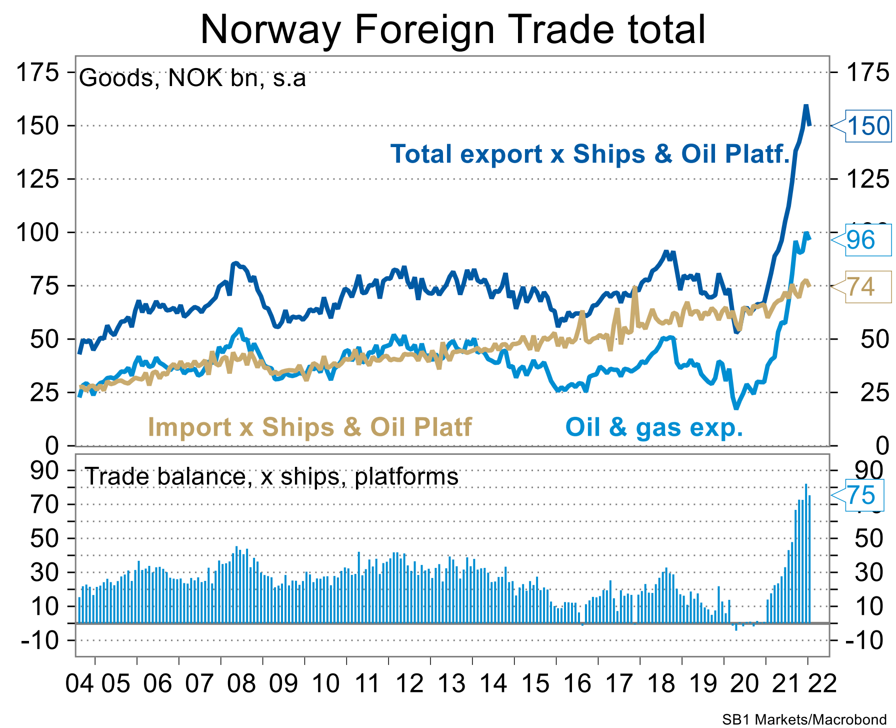


- **Home buying plans** flattened in Q4, and they have fallen significantly over the last year. Fear of higher interest rates?
- Demand for **2. homes and boats** is just close to average. **Car buying plans** suddenly fell sharply in Q1
- **Savings plans** are still above average, but now **"investing"** has become the highest ever, 3 st.dev above average!! We do not know what sort of investments households are referring too

The trade surplus down from ATH but still incredible large

Total surplus at NOK 75 bn in January, equalling 25% of GDP!

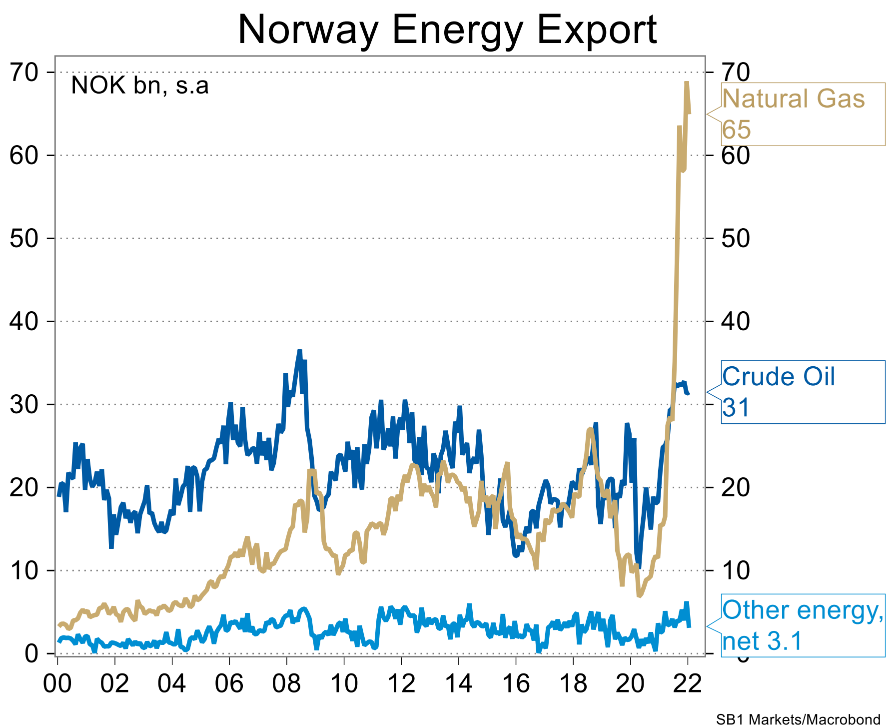


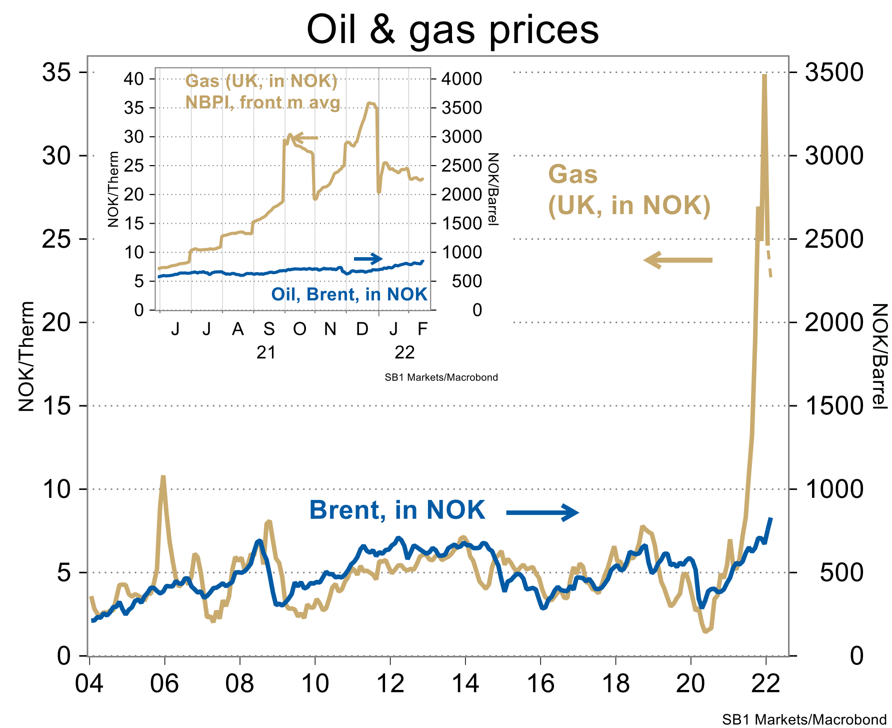


- **The <u>Mainland (non energy) trade deficit in goods</u>** rose marginally to NOK 32 bn
- **Non-energy exports** was record high in Jan but the trend recent months have been flattish. Exports are up more than 20% vs the level one year ago – and since before the pandemic – and the Jan level was record high
- **Imports** added some few bn and remain at 10% growth path
- **Both gas and oil exports** fell slightly due a decline prices – but petroleum exports way above anything seen before.
- **The trade surplus in goods** (ex ships/platforms) fell slightly to NOK 75, an enormous amount, 25% of Mainland GDP!
- **The government's <u>extra</u> revenues** from oil and gas exports (and direct ownership) the past 4 months may be some NOK 190 bn – transferred directly to oil fund

Gas exports marginally down – but still at NOK 65 bn, vs the 'normal' NOK 15 bn

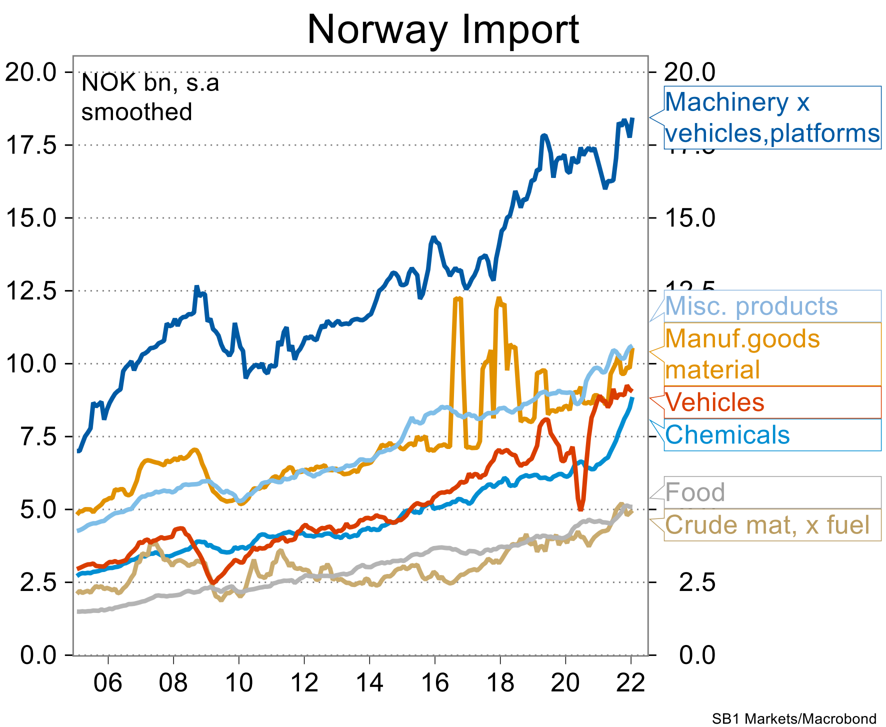
Gas exports equals more than 20% of Mainland GDP!

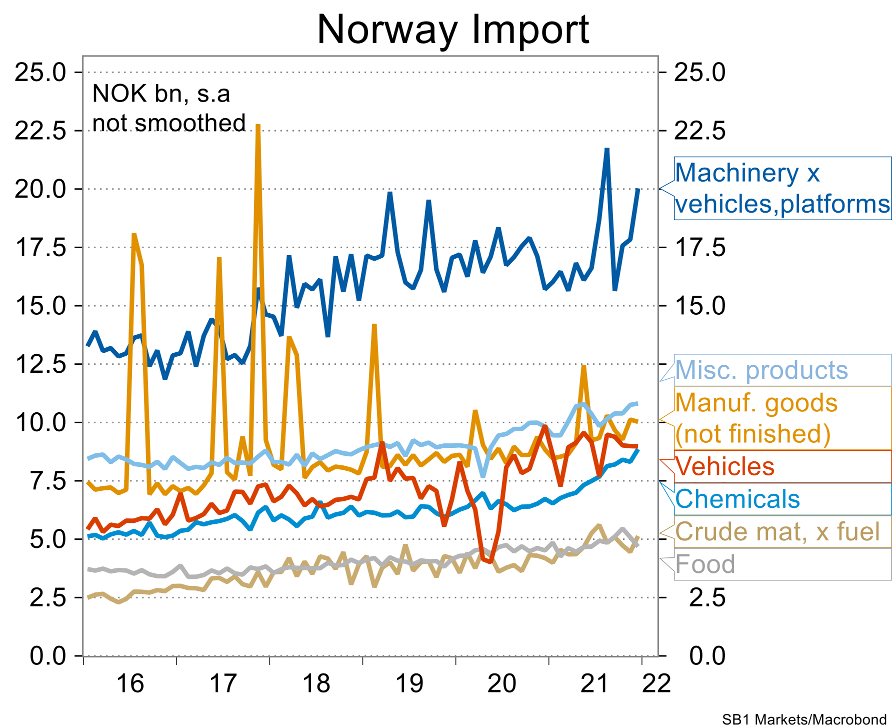




- **British gas** prises rose sharply in December, to another ATH, up 40% from November. (The NBPI at the charts to the right, the average for each month, calculated from the start of the month, the front month, check the small chart inserted). Prices fell sharply in January, by almost 30%. Prices are heading further down, so far in February but not by that much. The future market signals continued high prices
- Measured in NOK, the **oil price** is at a an ATH level, so far in February. Even so, **crude oil** exports fell marginally (in NOK bn, seasonally adjusted) – but remained at a high level

Most imports are trending upwards

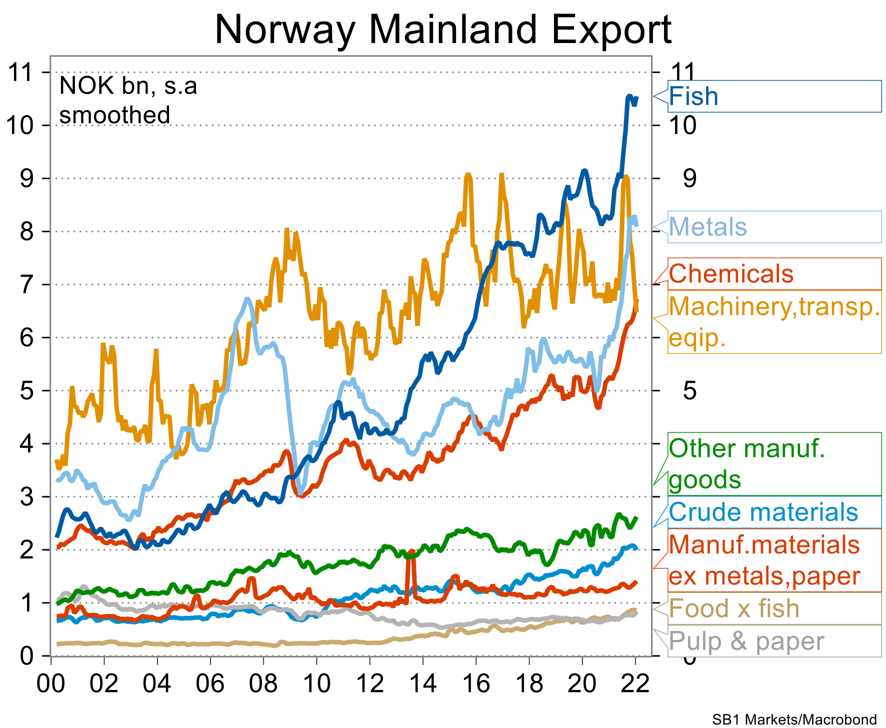


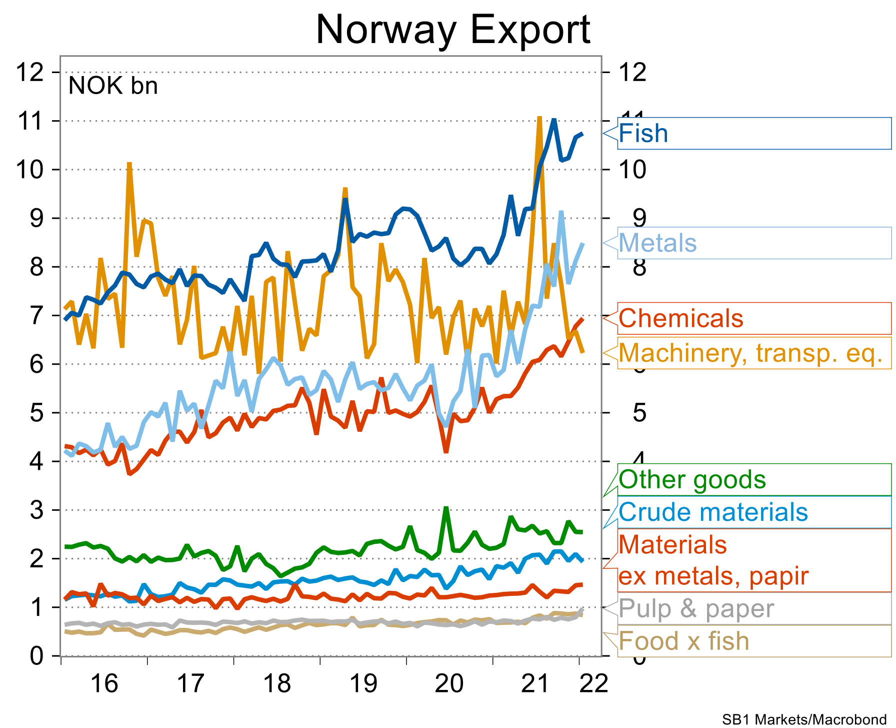


- The spikes in imports of manufactured goods are due to unfinished platforms or ships

Fish exports are surging, metals, chemicals sprinting upwards too

Exports of machinery & transport eq. sharply down recent months trend flattish since 2017





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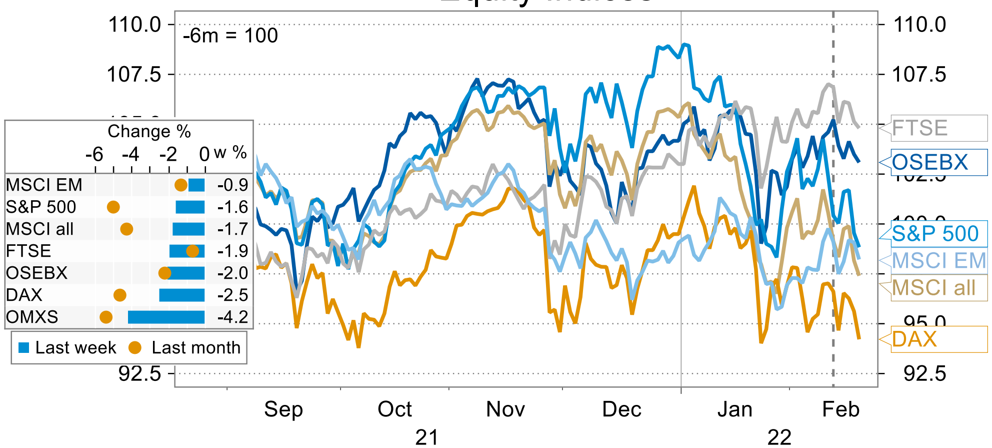
Stock markets down on increased war risk, bond yields fell to

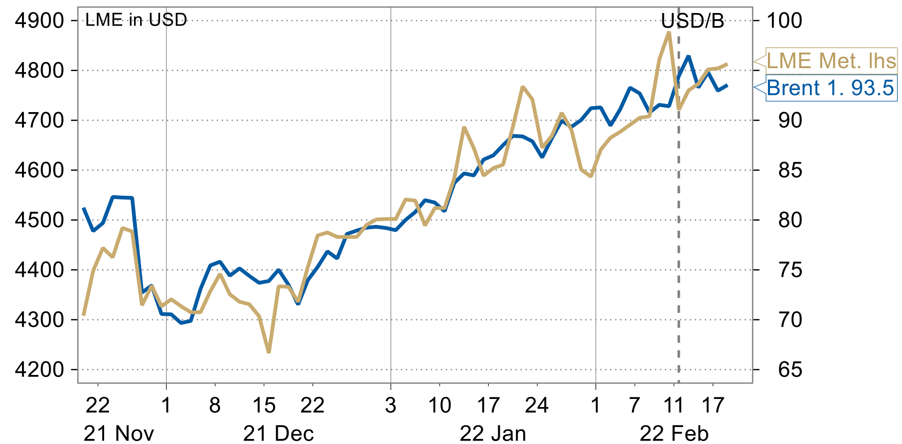
The oil price fell too (but most other commodity prices not) – and the NOK fell sharply

Equity Indices



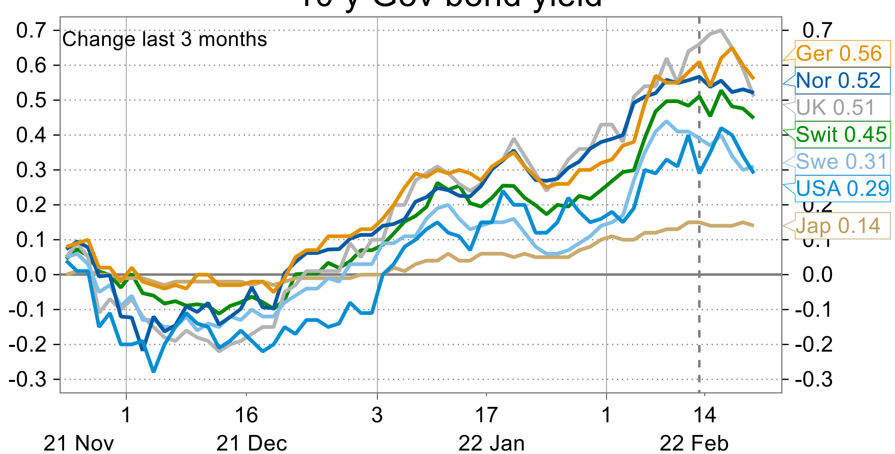
SB1 Markets/Macrobond

Oil vs. metals



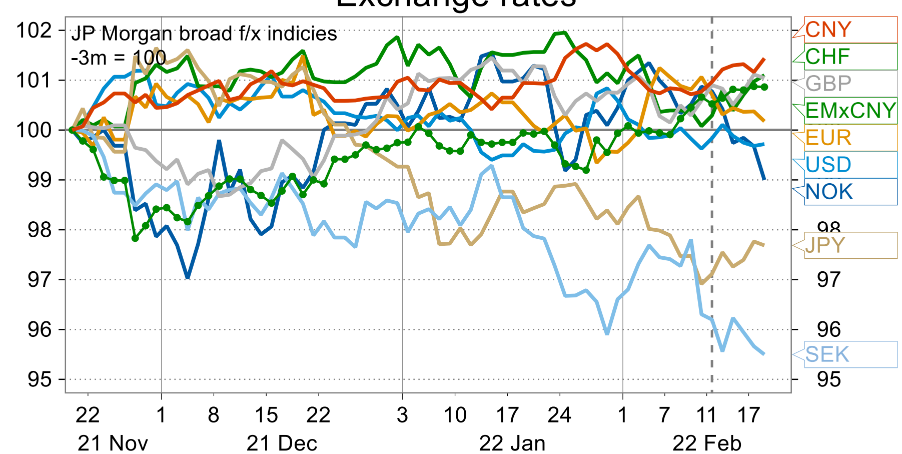
SB1 Markets/Macrobond

10 y Gov bond yield



SB1 Markets/Macrobond

Exchange rates



SB1 Markets/Macrobond

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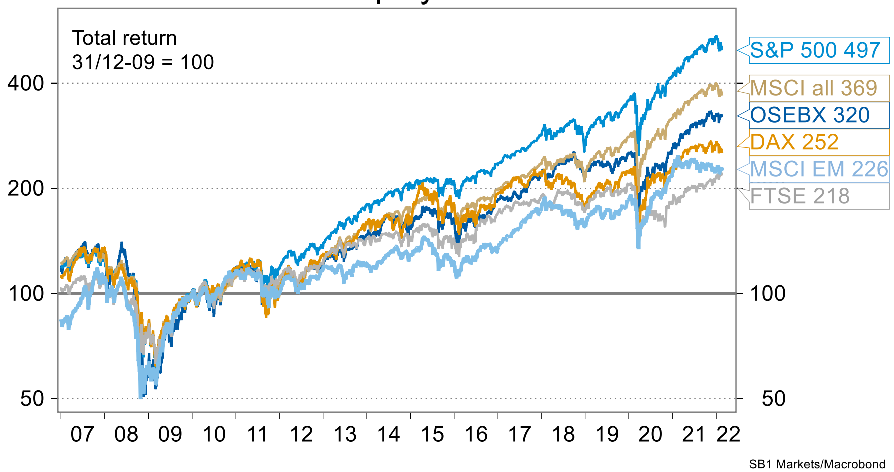
The big picture: Who were flying the highest?

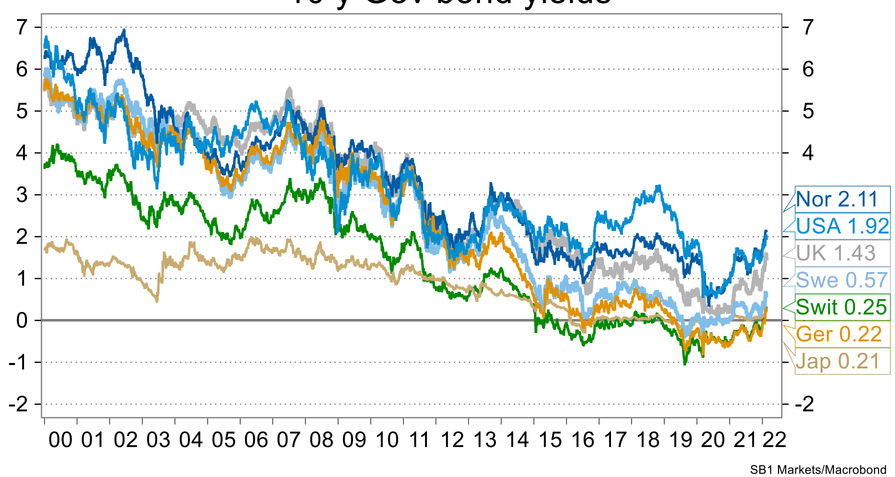
Bond yields are climbing rapidly everywhere, as have commodity prices

Equity Indices

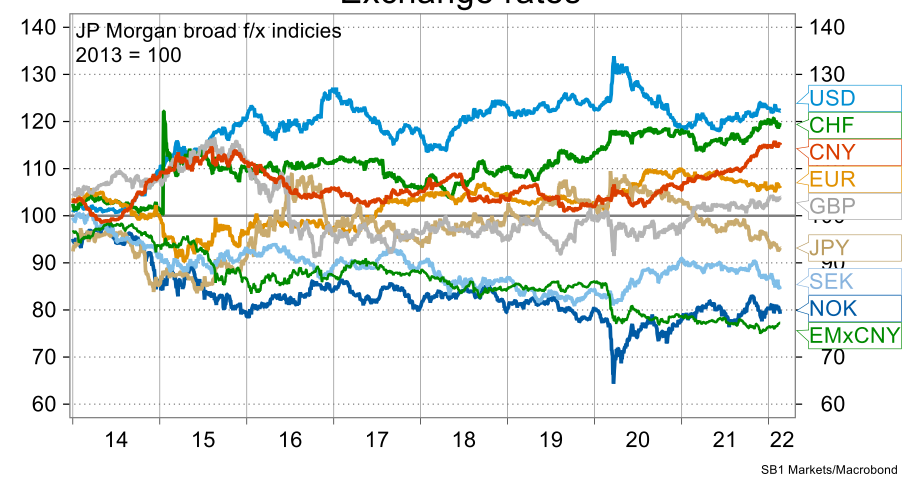


Oil vs. metals

10 y Gov bond yields



Exchange rates



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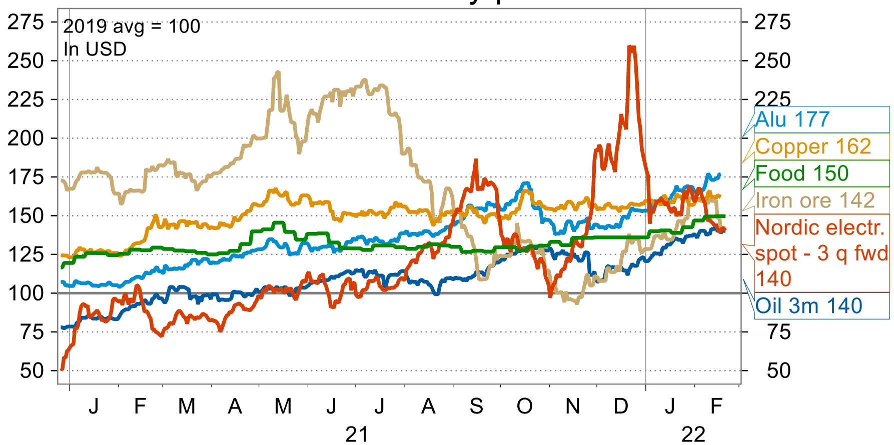
Iron ore prices sharply down (a Chinese attack?), oil slightly down

Other commodities flat/up

Commodity prices

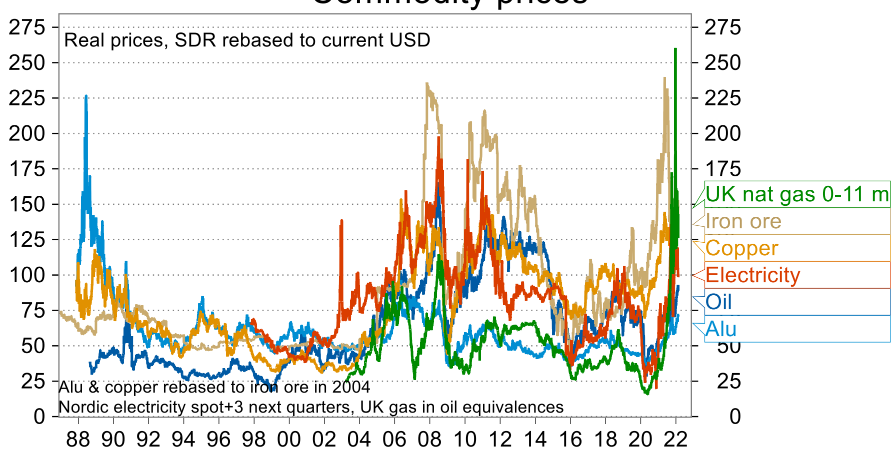


SB1 Markets/Macrobond

Brent oil, spot & Dec contracts

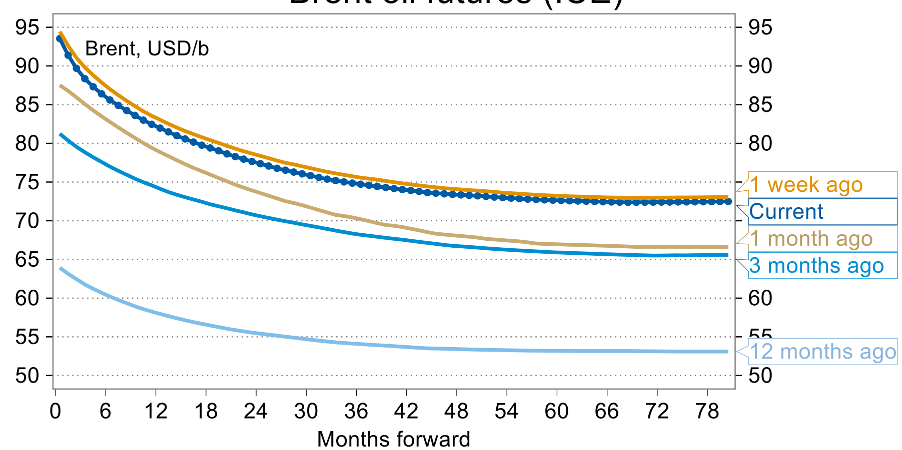
SB1 Markets/Macrobond

Commodity prices



SB1 Markets/Macrobond

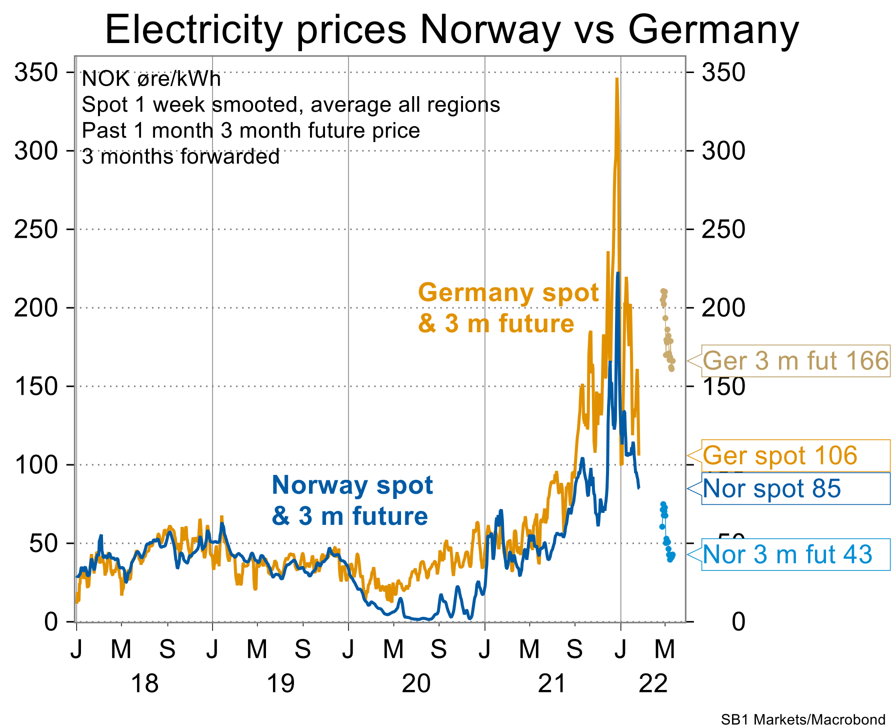
Brent oil futures (ICE)

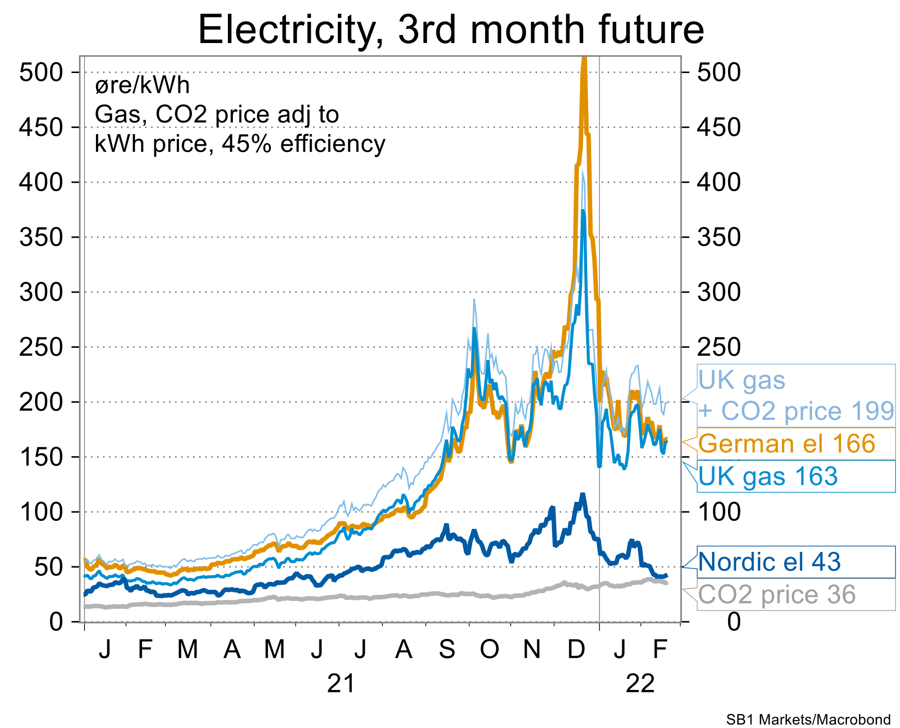


SB1 Markets/Macrobond

European energy prices are heading down, even if war angst is seen in other markets

The ‘Norwegian’ risk: European future electricity prices remain far above Nordic electricty prices

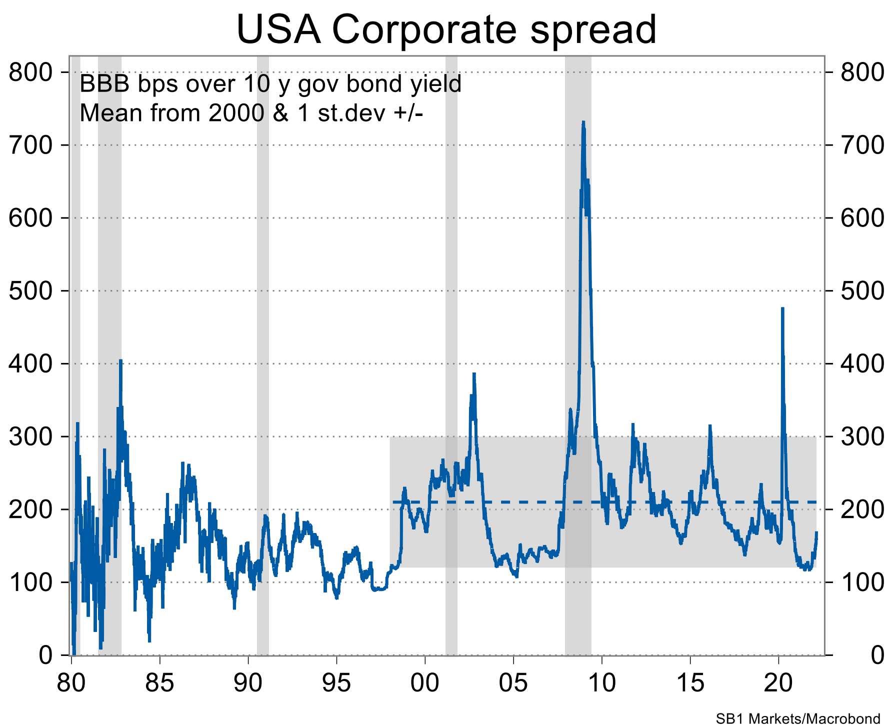


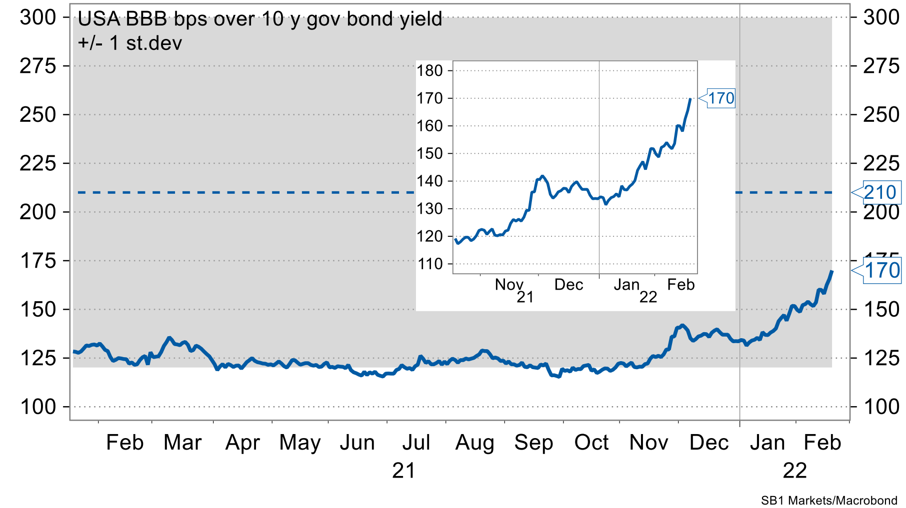


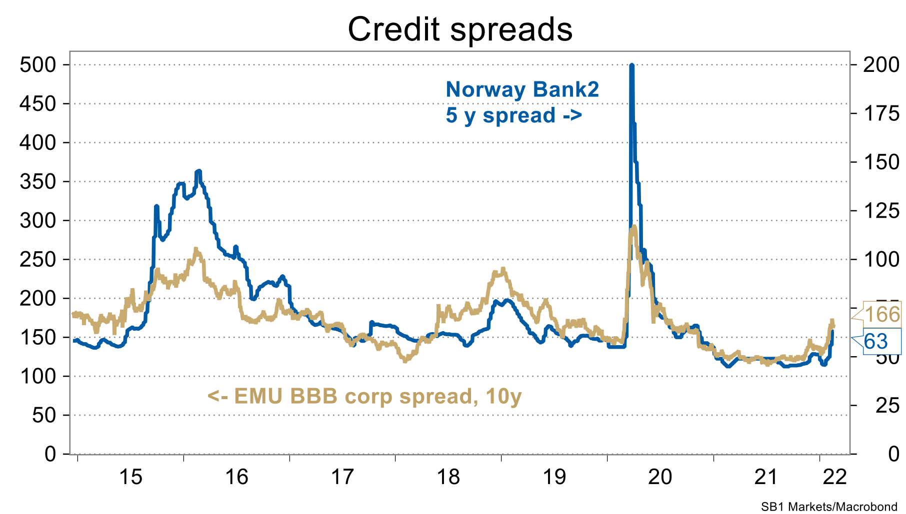
SpareBank 1 MARKETS

The credit cycle has turned – and now even Norwegian banks have to pay up!

Higher bond yields, lower equity pricing is not the best environment for credit spreads



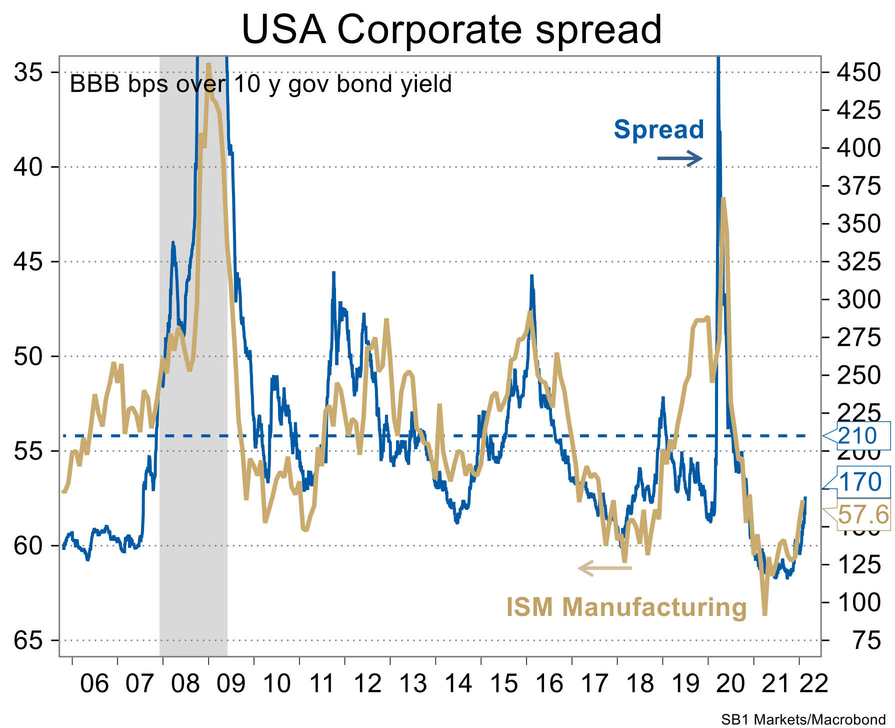




- The increase in US Corporate BBB spread now equals >0.5 st.dev, still just a fraction of a normal full credit cycle
  - » The credit cycle is often closely correlated to the economic cycle, check next page
- The NOK Bank 2, 5y spread widened 7 bps to 63 bp last week (and from below 50 two weeks ago), the highest spread in more than one year

It could be the economy, stupid

Growth has to be slowed to get inflation under control. If that happens…

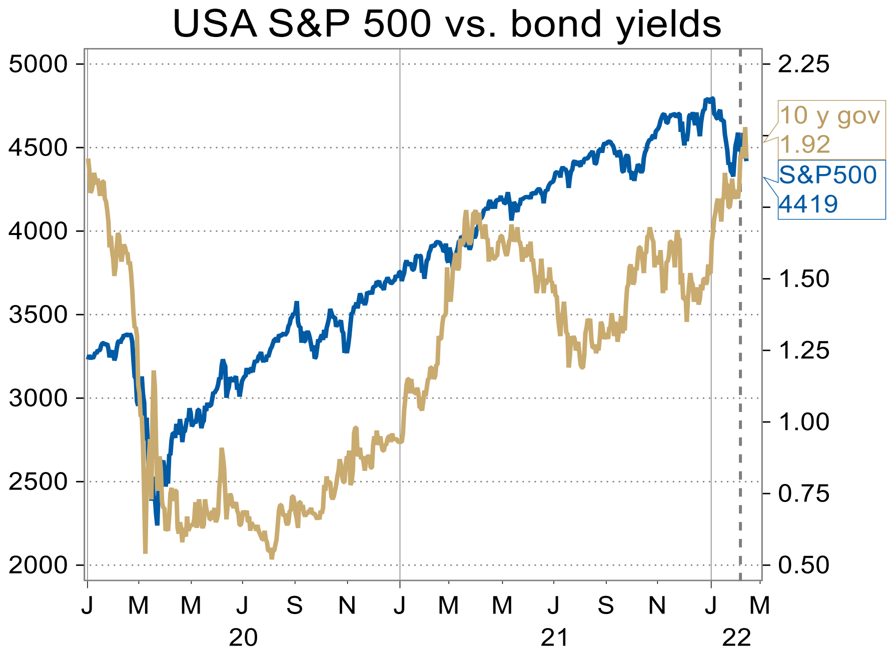


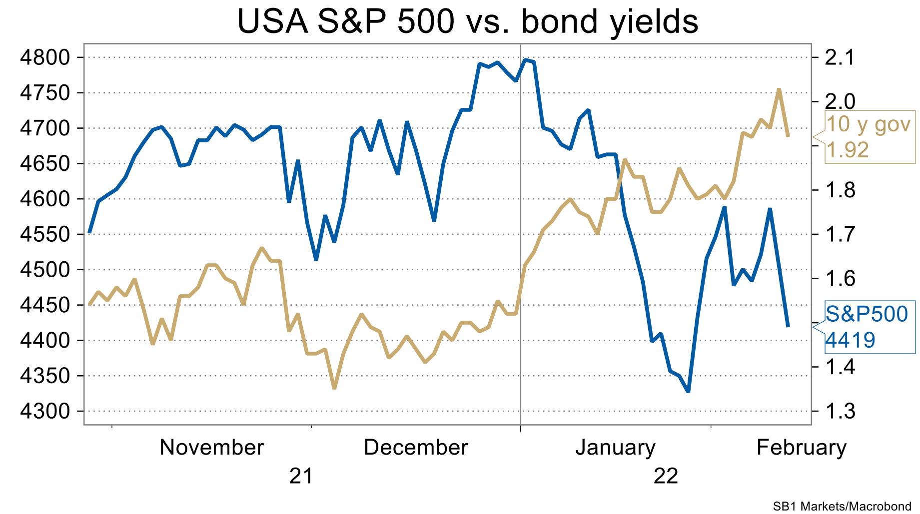
- Growth has already slowed somewhat, according to the US manufacturing ISM – and all other surveys

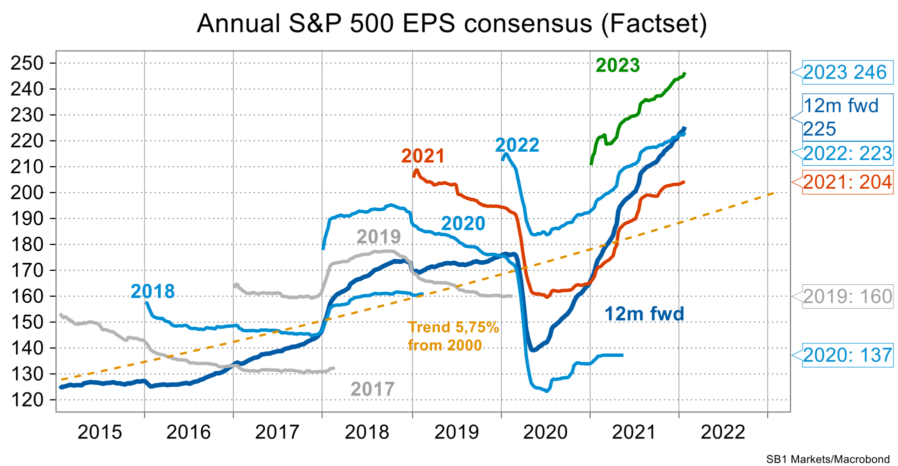
SpareBank 1 MARKETS

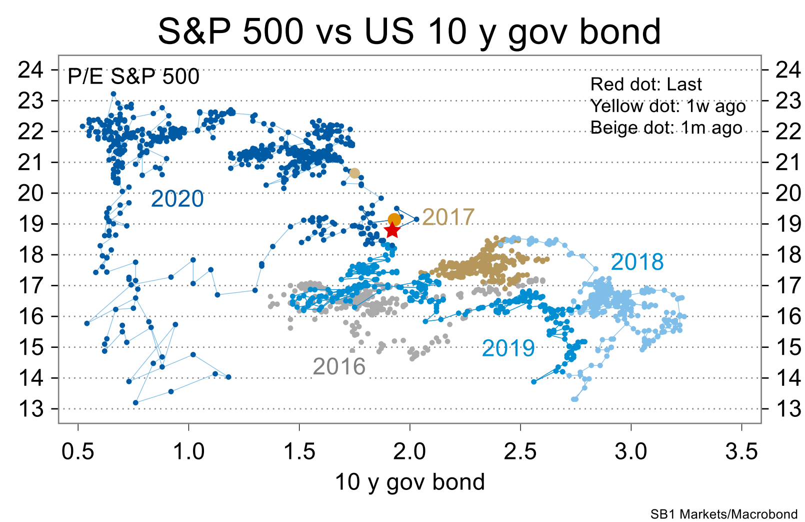
S&P 500 down 1.8%, due the Friday setback – which was due to war angst?

The 10 y was up 13 bps to 2.05% at Thursday but closed 1 pb down on the week, at 1.92%



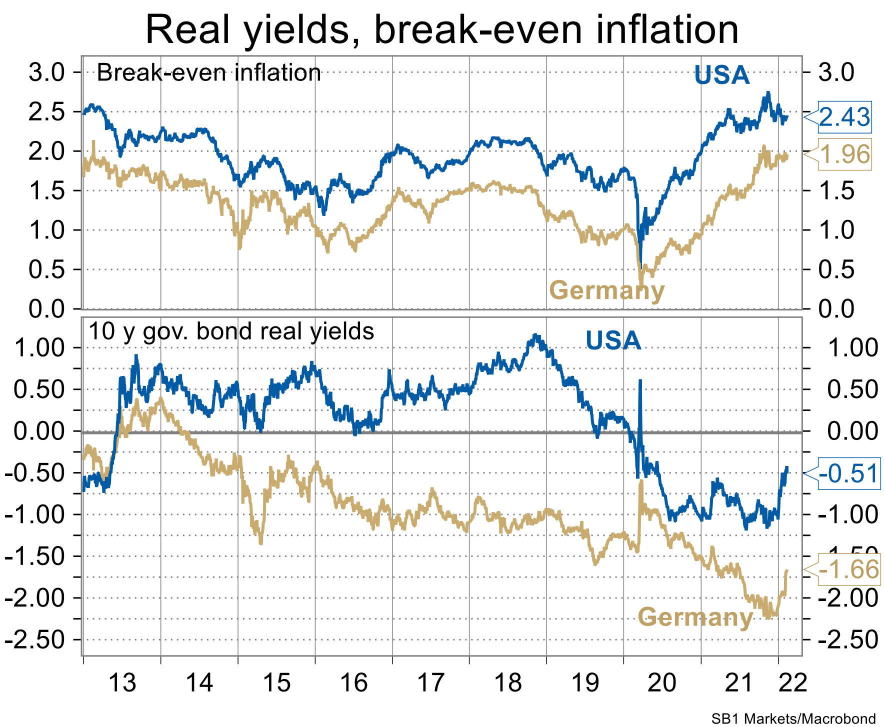


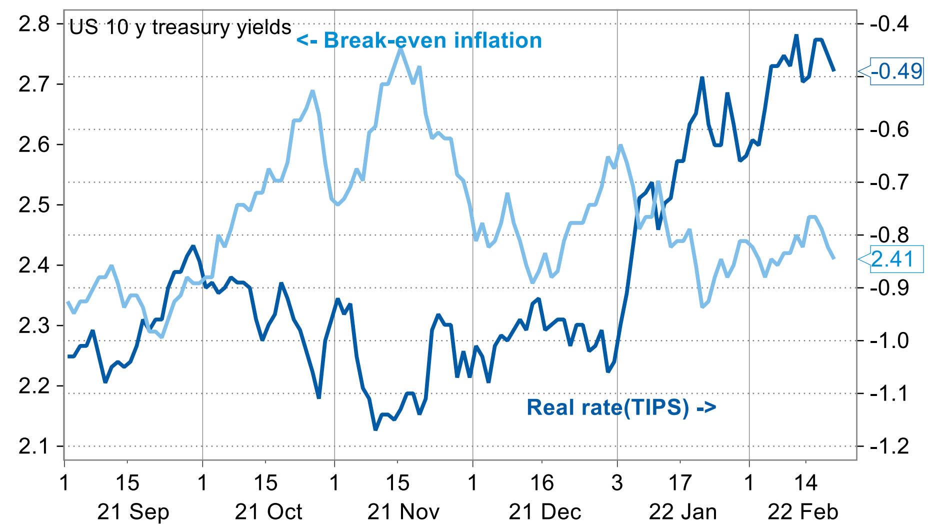




German real rates down, following the steep rise

No material changes in US last week





US & Germany 10 y Gov bond yield

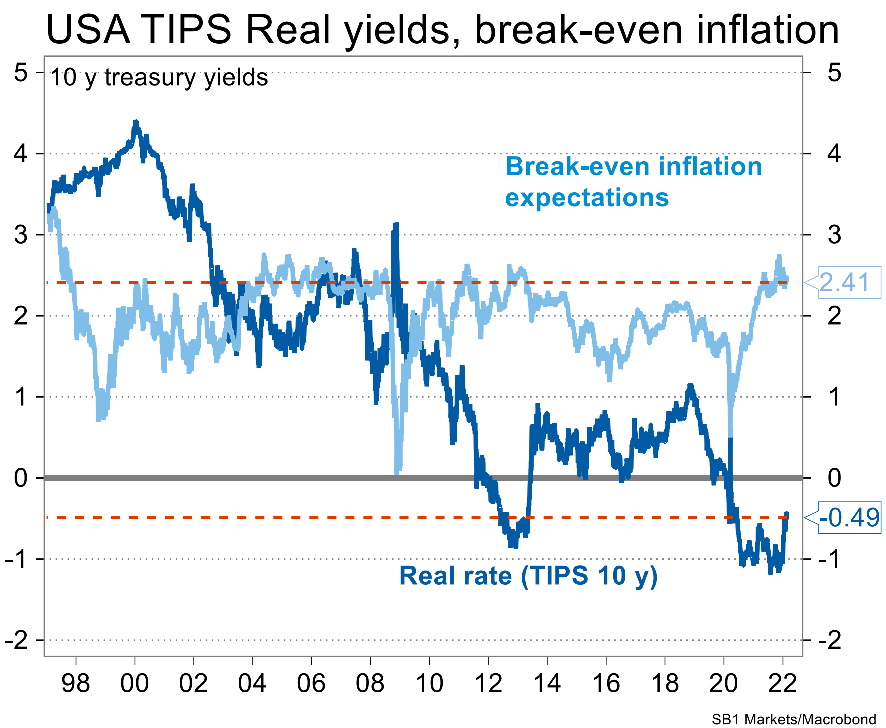
	Yield	Change 1w	Change 1m	Min since April-20
USA nominal treasury	1.92	-0.01	0.17	0.52
.. break-even inflation	2.43	0.02	-0.11	1.06
.. TIPS real rate	-0.51	-0.03	0.28	-1.19
Germany nominal bund	0.30	0.15	0.35	-0.65
.. break-even inflation	1.96	0.06	0.03	0.40
.. real rate	-1.66	0.09	0.32	-2.26

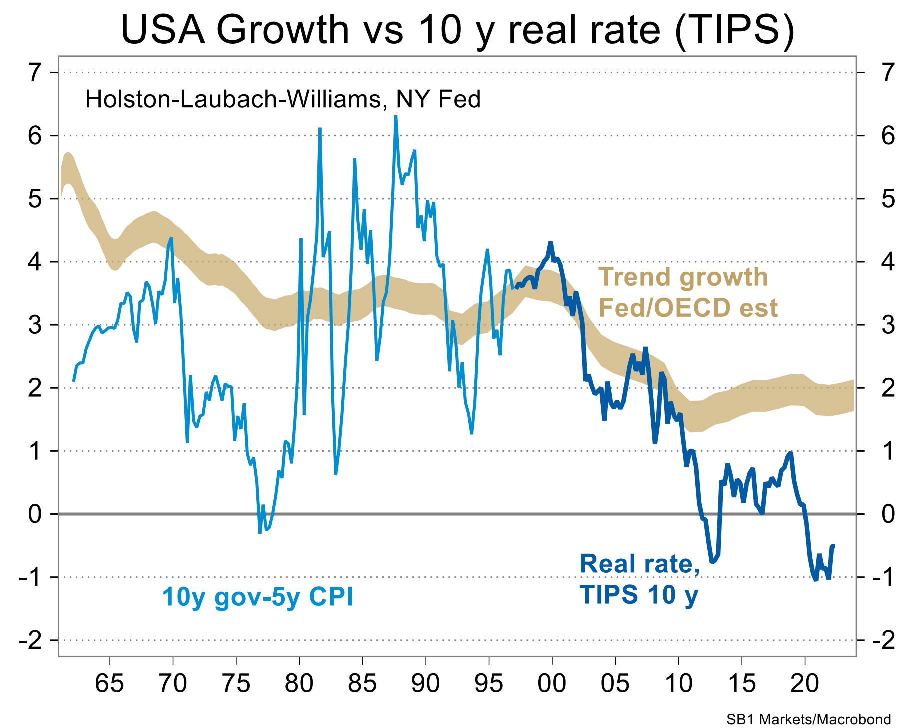
SB1 Markets/Macrobond

- US real rates are trending up, inflation expectations down
- German real rate are trending up, inflation expectations are flattish

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

Well, now it is happening – but the 'spread' is still far too large?

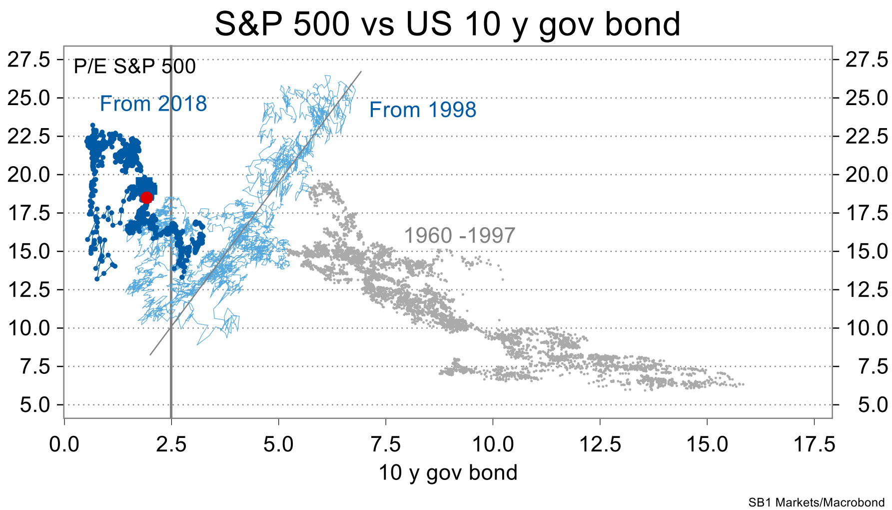


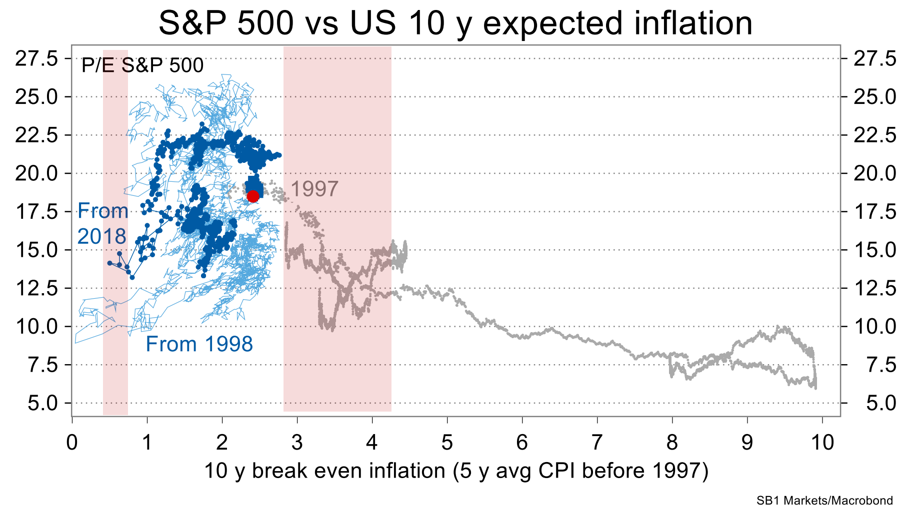


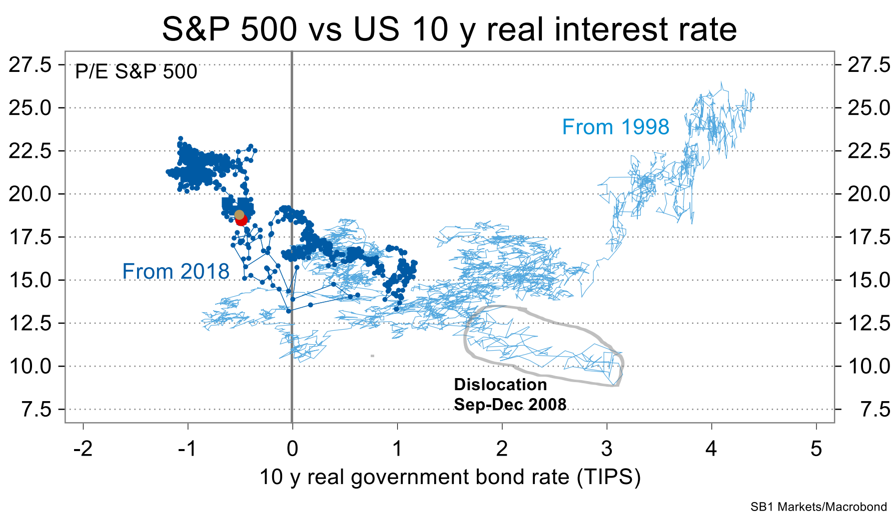
- Something is happening: The 10 y real TIPS rate is on the way up, now by almost 70 bps from the ATL last year

Bonds vs. equities: What's next?

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



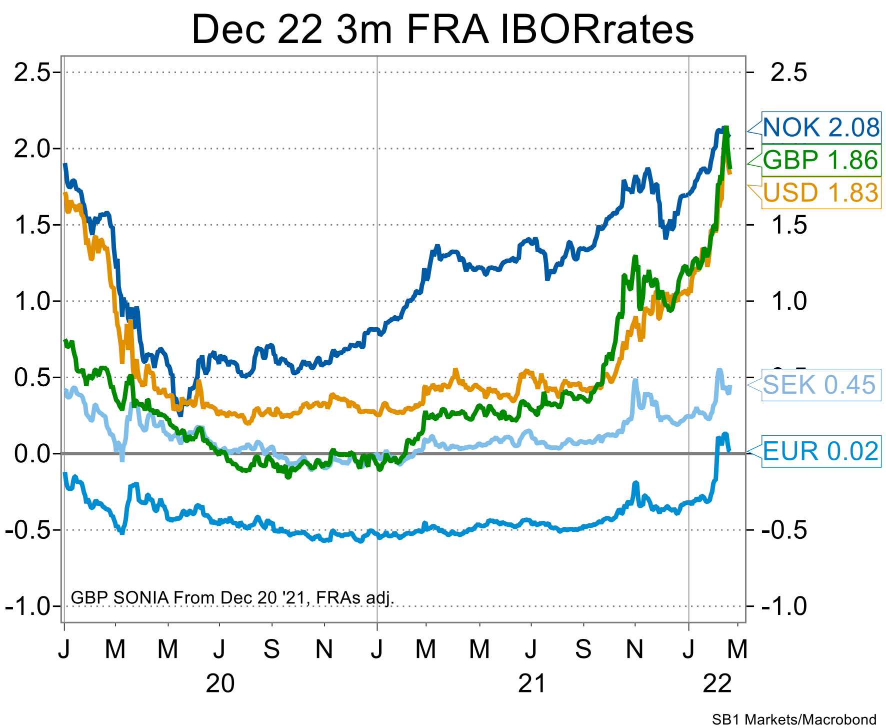


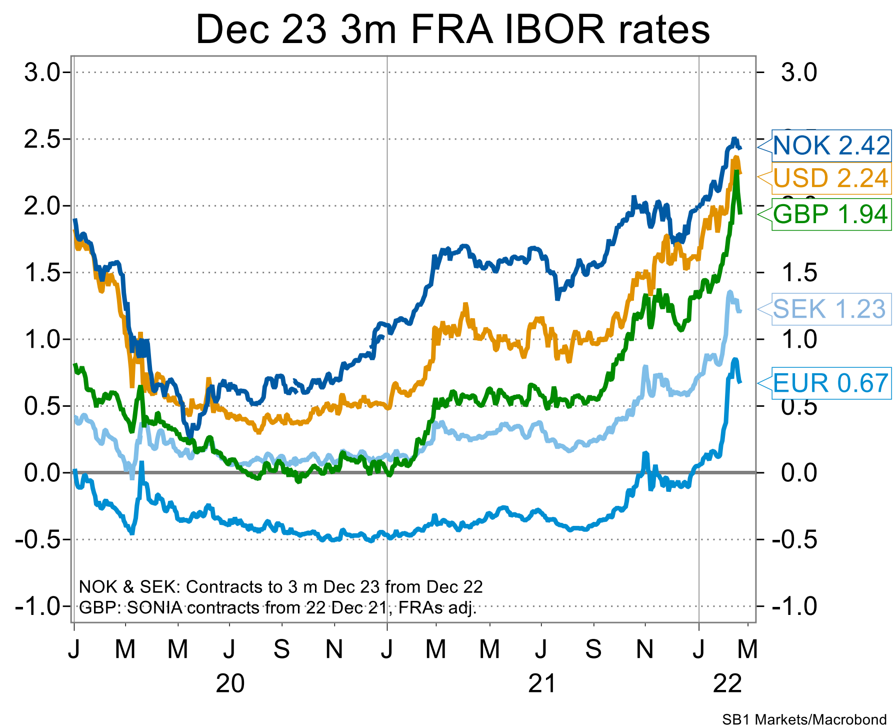


- **Expected inflation**
  - » ***If its not too low or too high: No problem***
    - 'Real' expected earnings are unaffected, higher inflation implies stronger growth in earnings, and vice versa
  - » ***If its too low or too high: A problem***
    - Something is rotten: Deflation or far too high inflation. 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 multiples? Luckily, multiples has come down quite a lot

Rate expectations lowered by risk of war + some milder FOMC comments

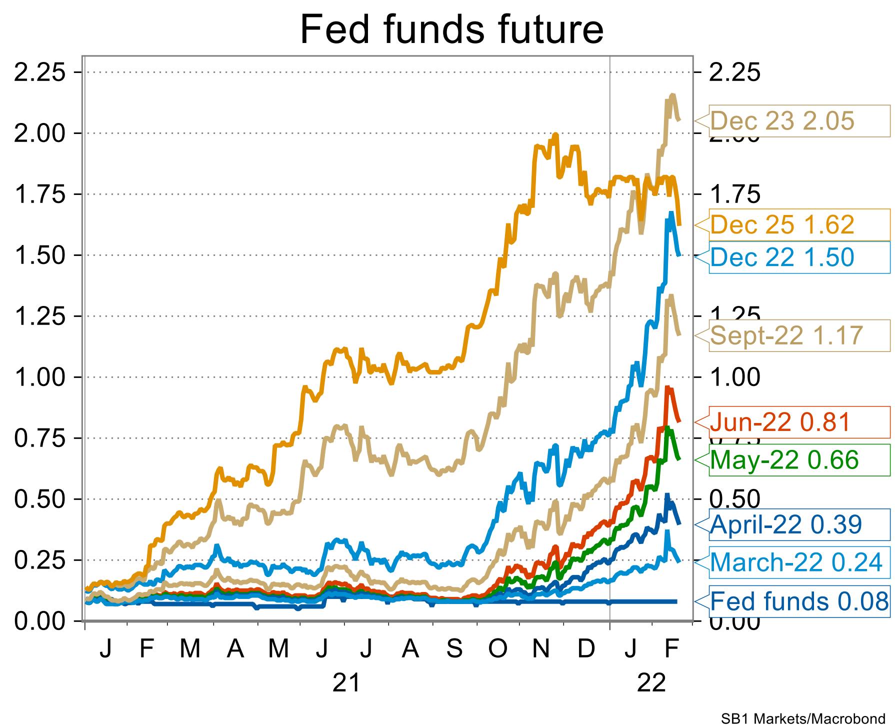
Last week's correction is not large vs. the lift in rate expectations recently

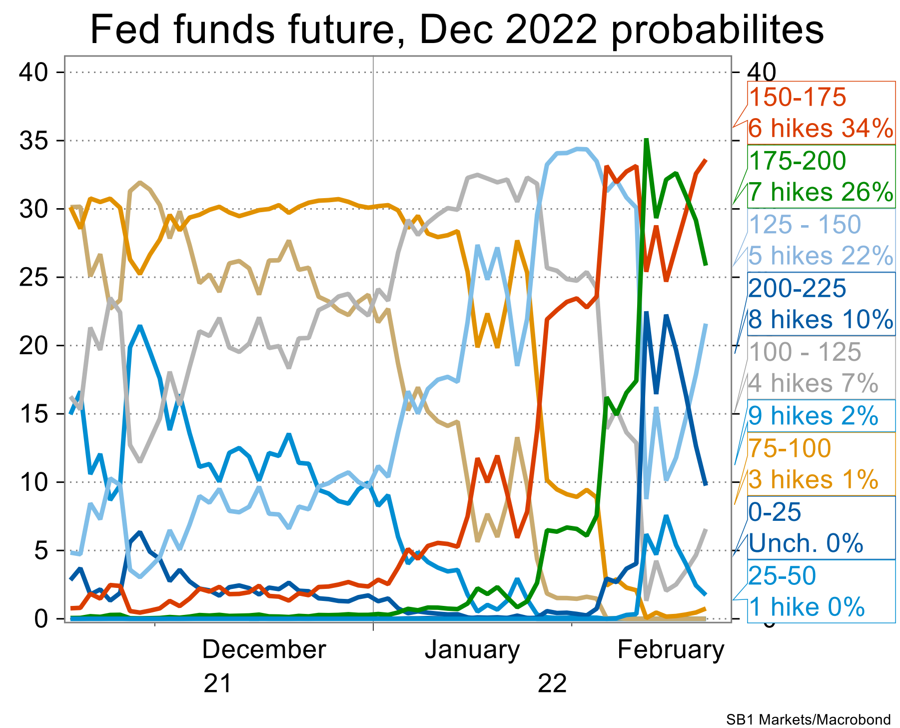




Less fear for 7 or more 2022 hikes, 6 the most likely

The FOMC minutes, oil prices – and angst for a war in Europe lowered rates last week

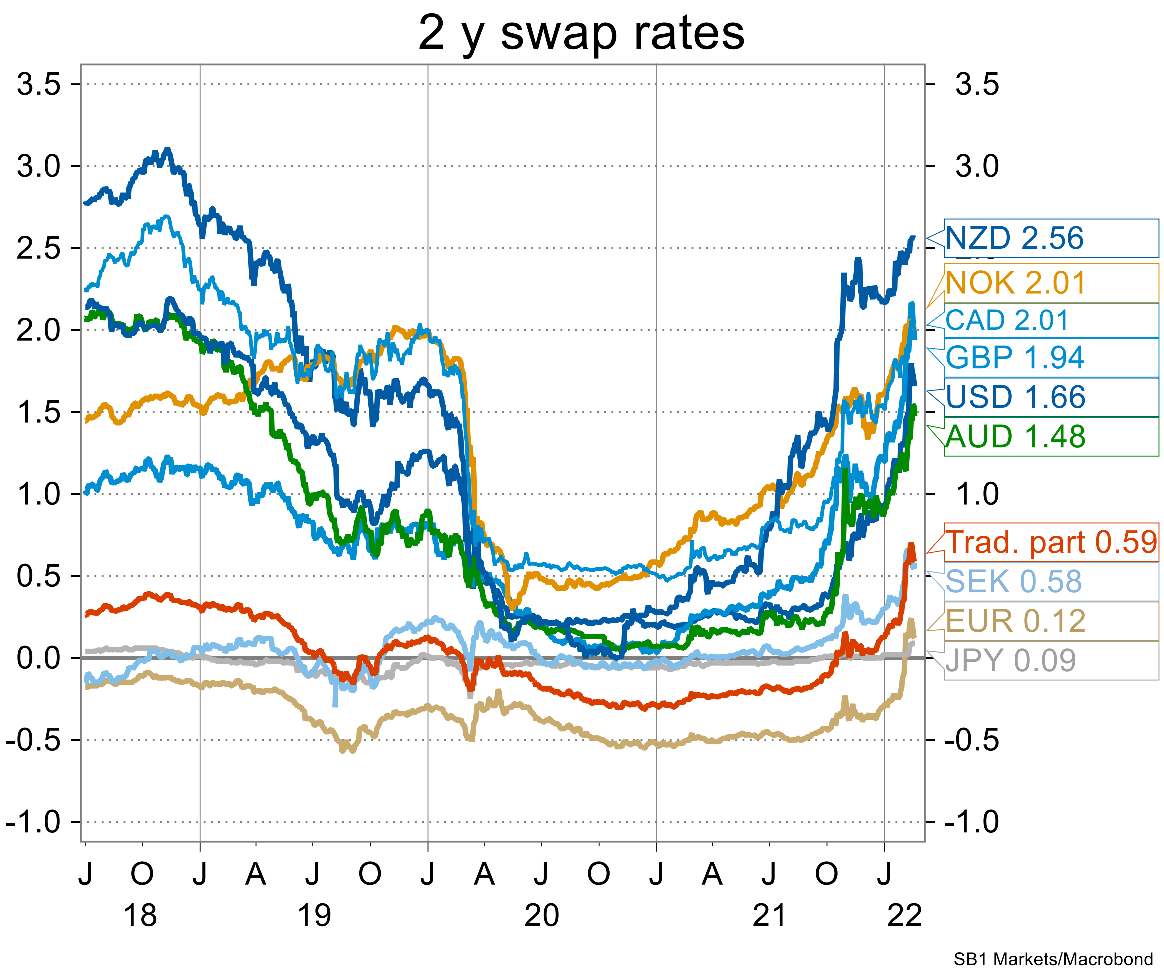


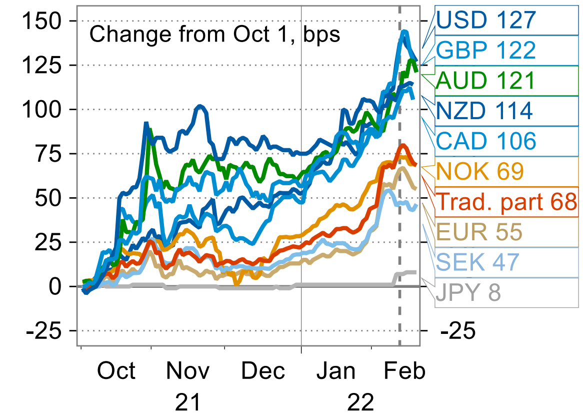


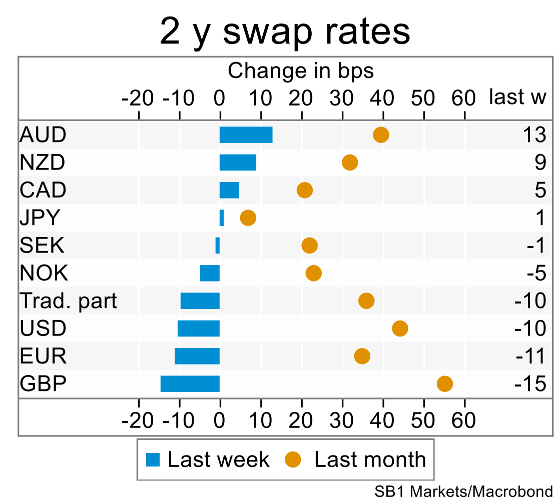
- A 50 bps March hike is now deemed to be far less likely than a 25 bps, 22% vs 78%. At Feb 10, the bet was 94% for a 50 bps hike

SpareBank 1 MARKETS

Geopolitics kept rates in check last week – our trading partners down 10 bps

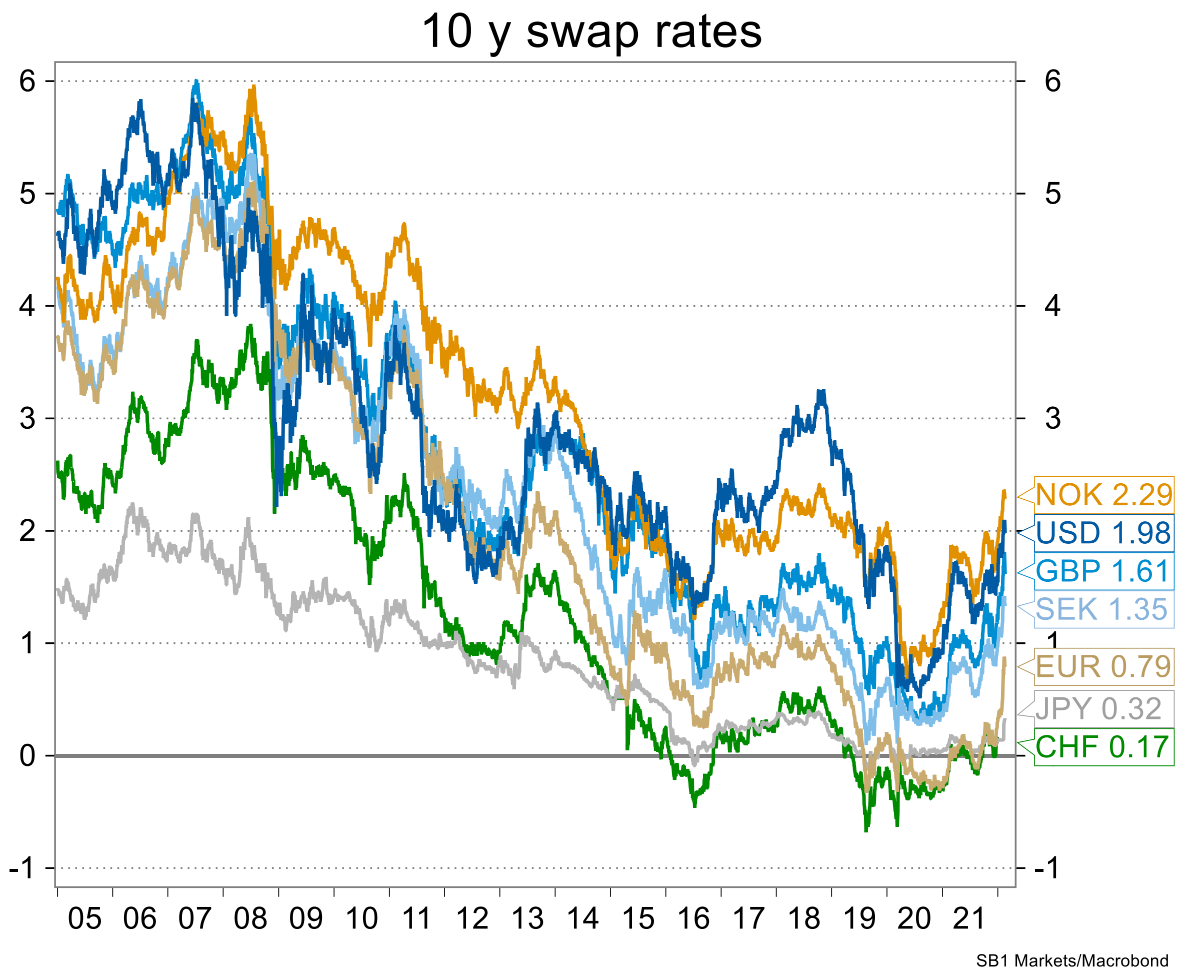


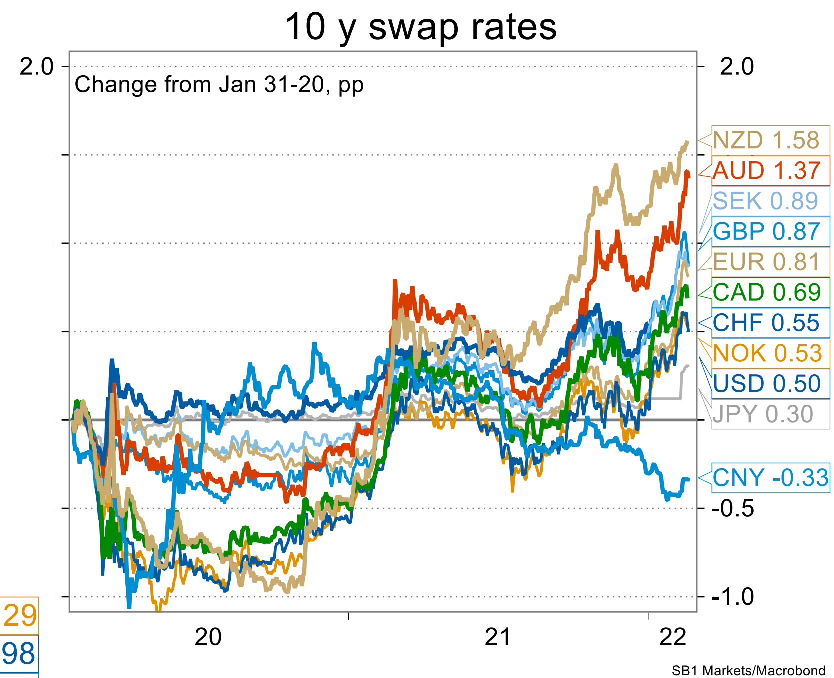


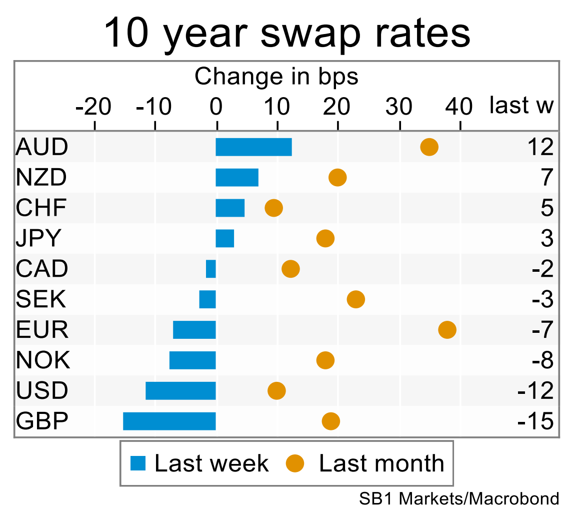


The trend seems to be up ☺.

… everywhere. Even if rates fell most places last week

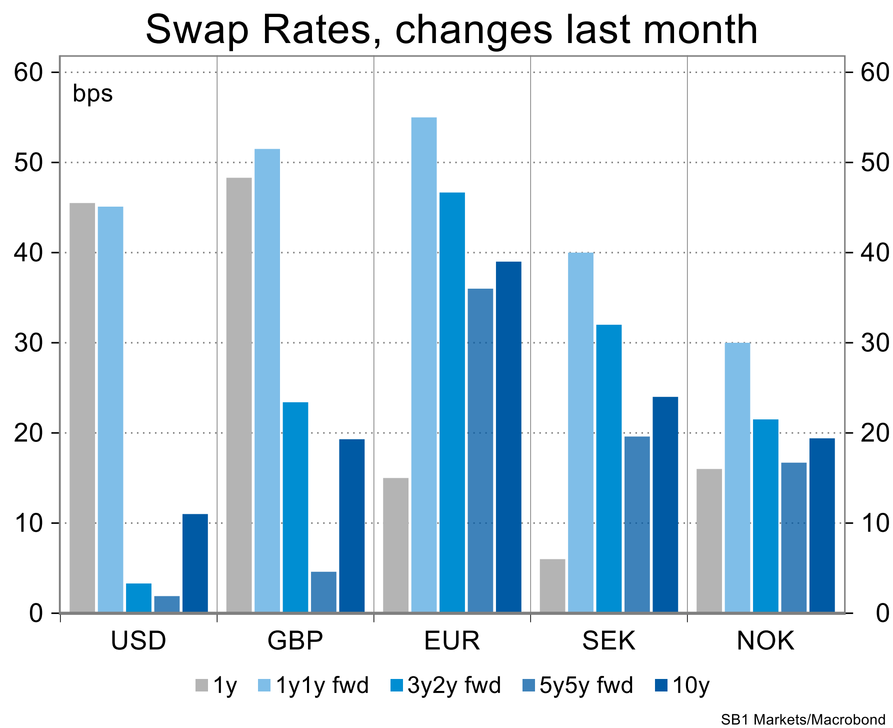


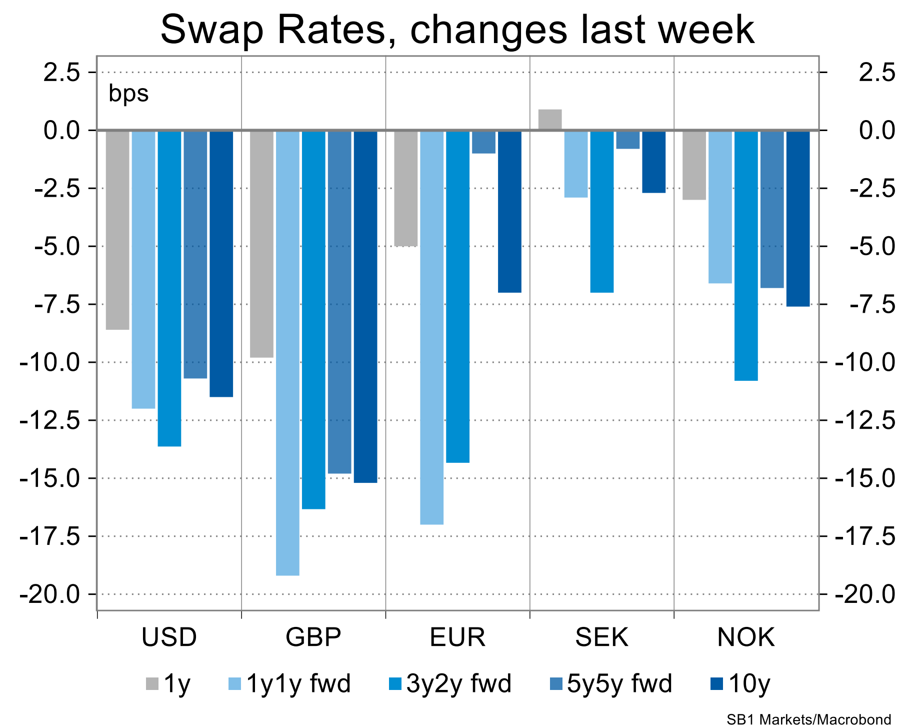




Finally, lower rates – the least in Sweden were CPI surprised at the upside

Still, the last weeks have been spectacular, especially in the short end





- Just the short end of the SEK curve up last week

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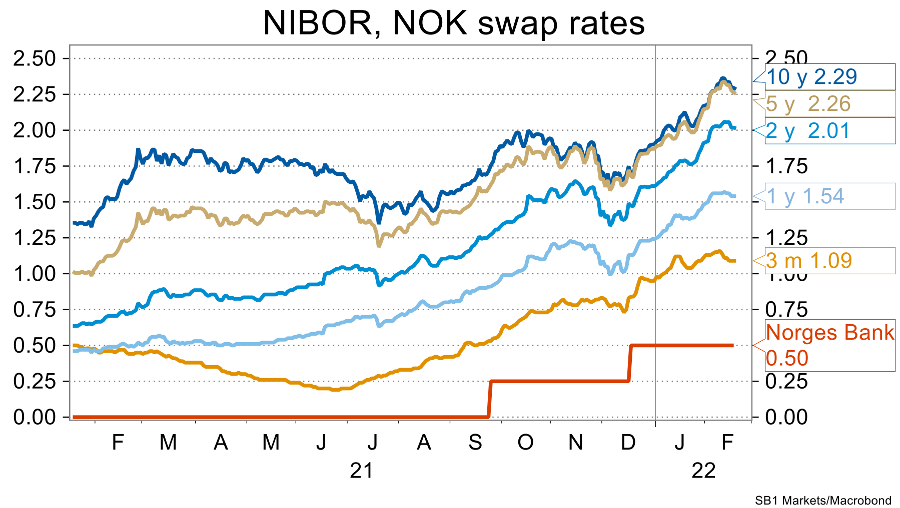
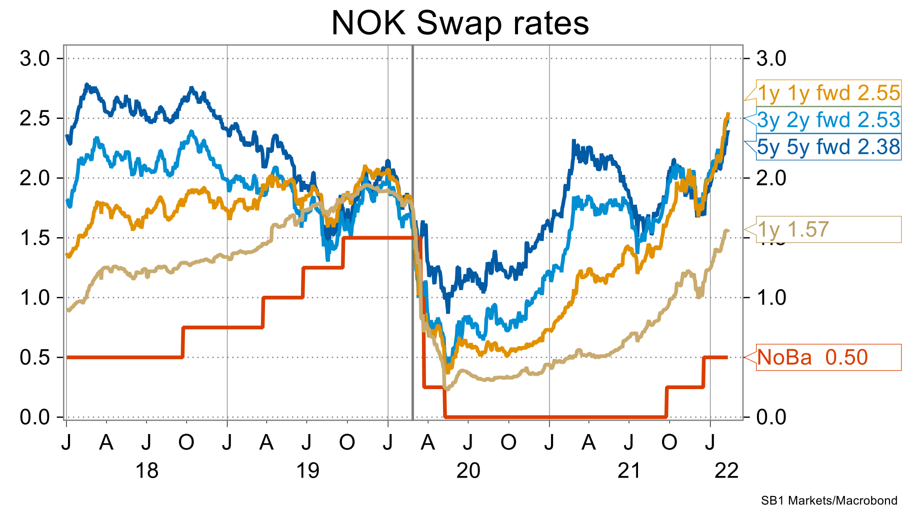
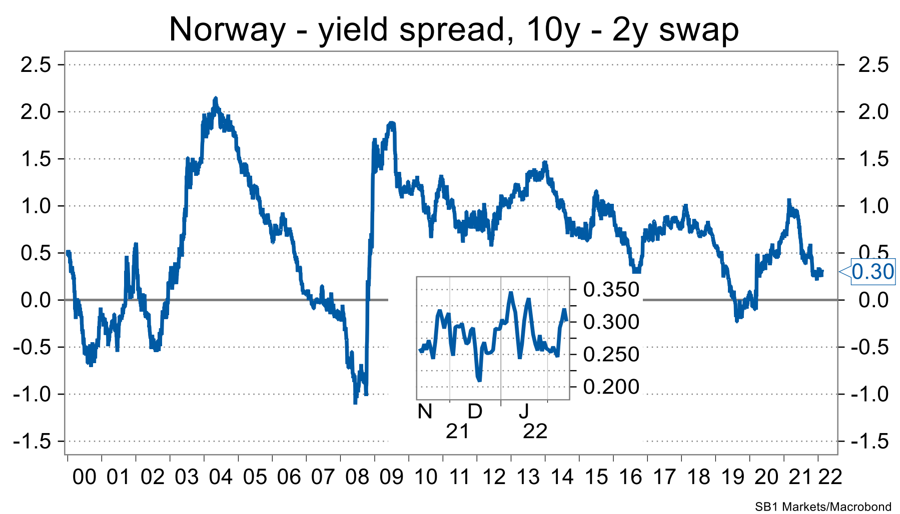
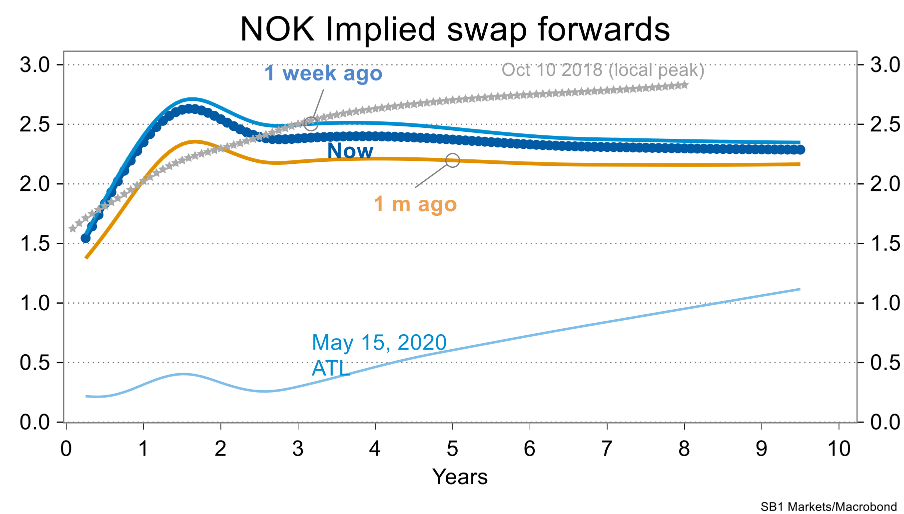
Up all along the curve last week, the 10 y down 6 bps to 2.29%!

The whole curve down last week – most at the mid-segement of the curve





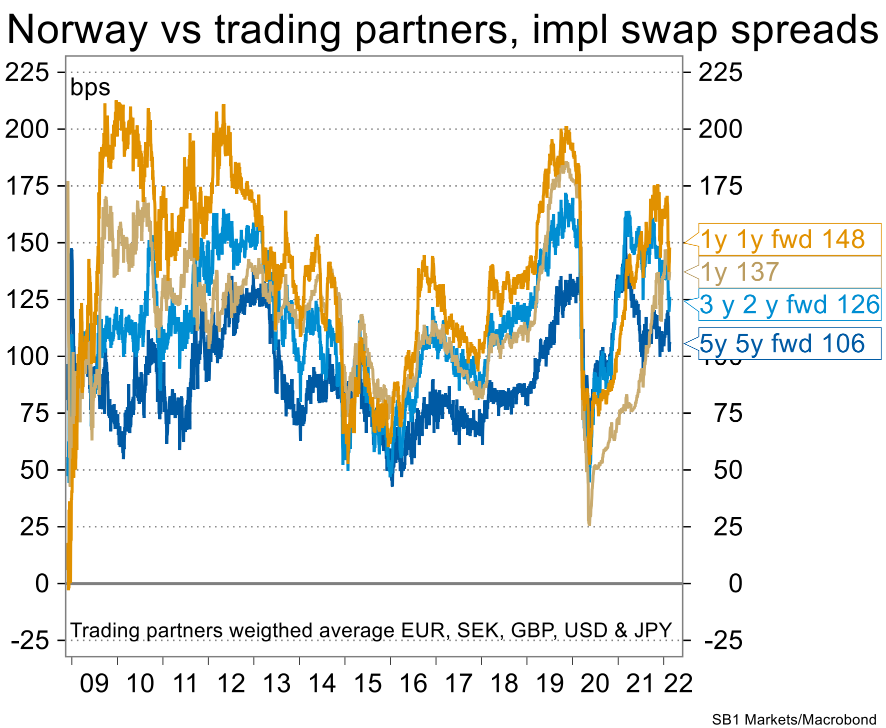


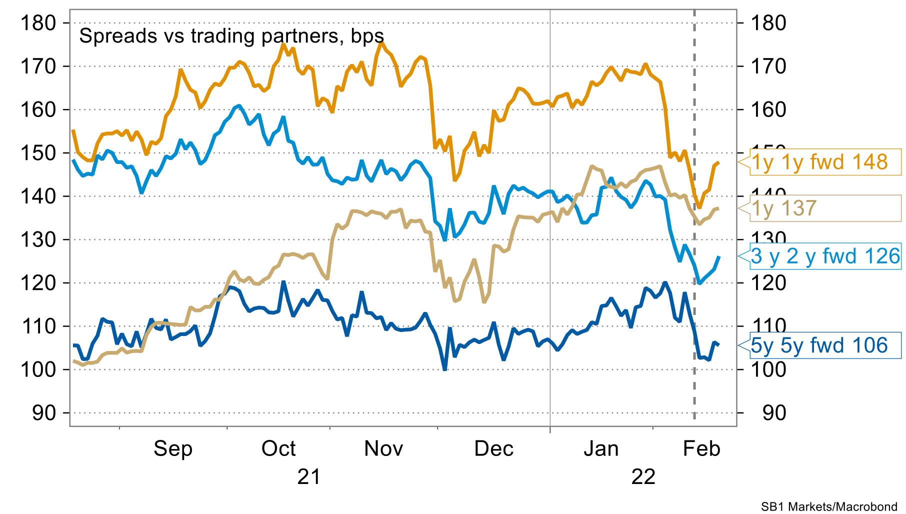


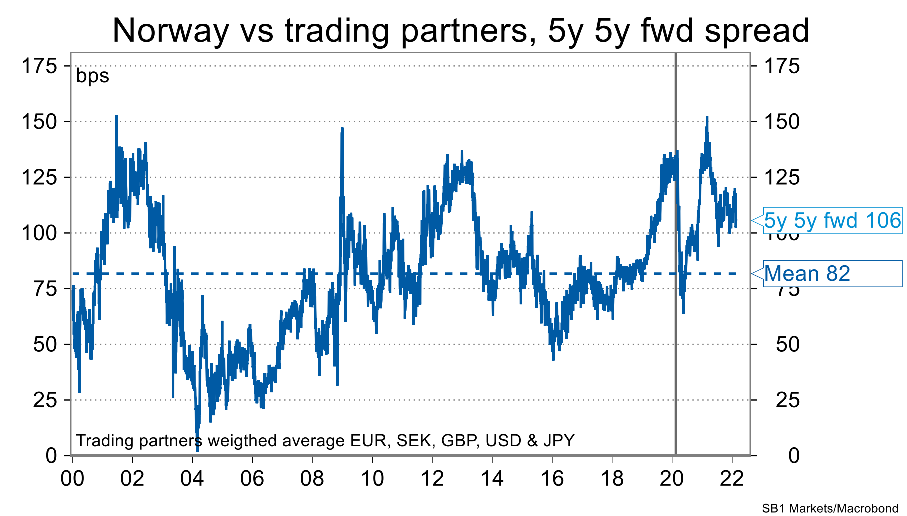
SpareBank 1 MARKETS

Spreads flattened – rose last week – rates fell more abroad than in Norway

Spreads are still at the high side



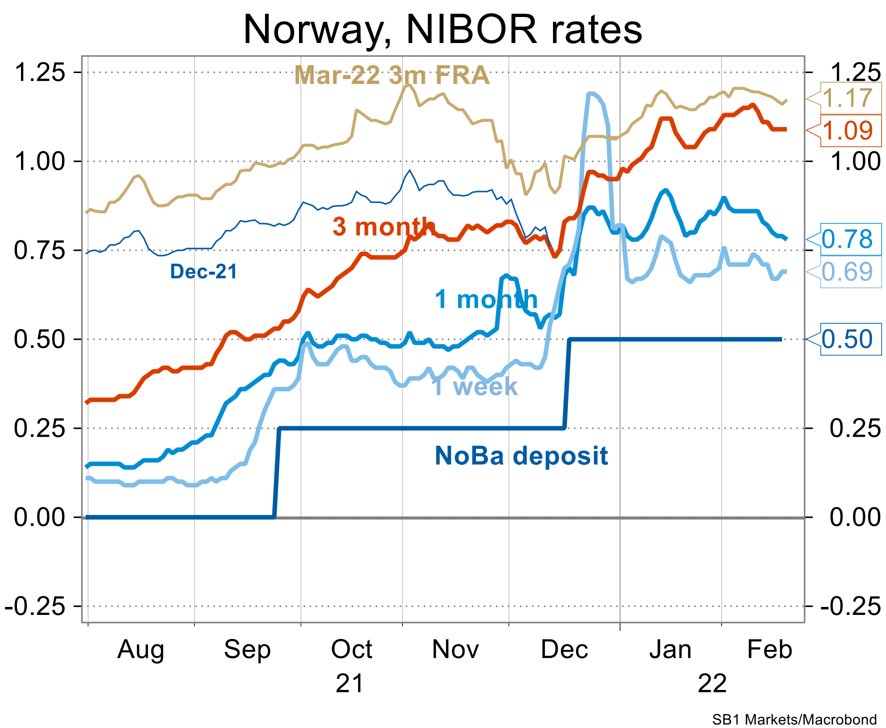


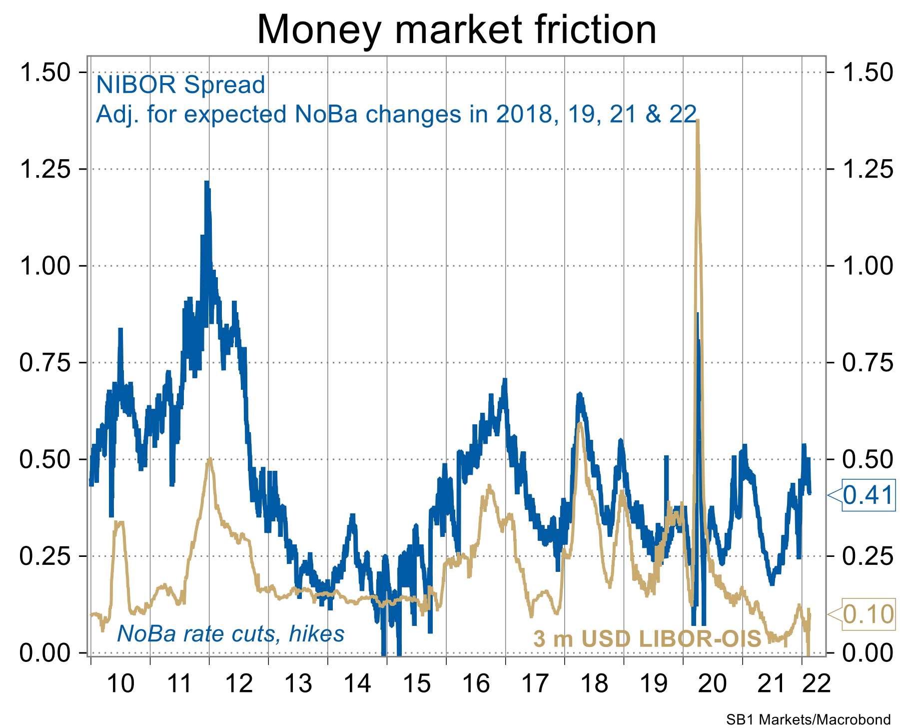


SpareBank 1 MARKETS

The 3m NIBOR down 2 bps to 1.09%

The NIBOR spread down 4 bps to 41 bps (if NoBa hikes ‘just’ 25 bps in March, and not further in May)

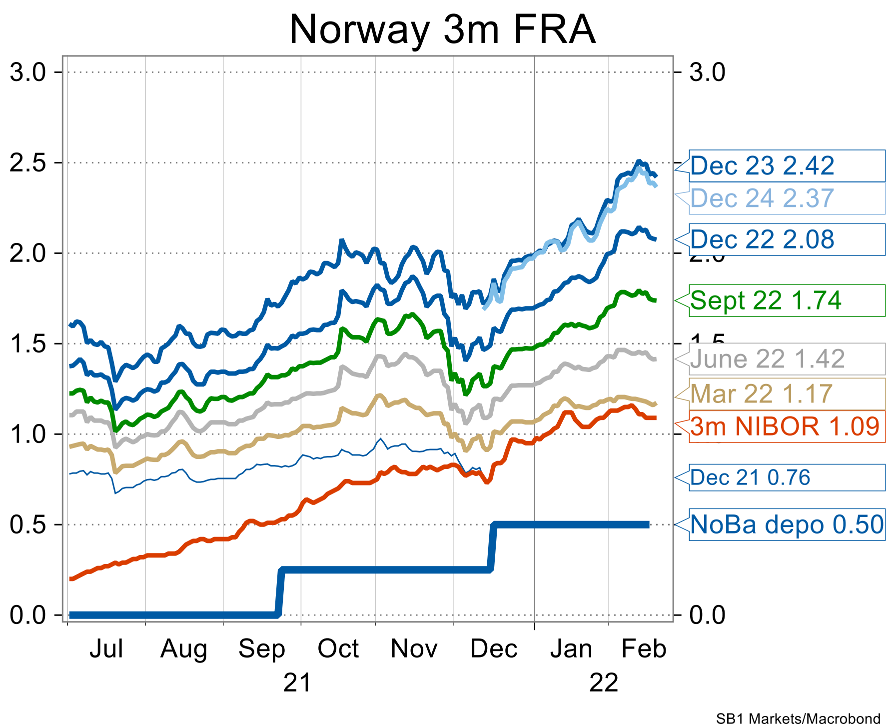


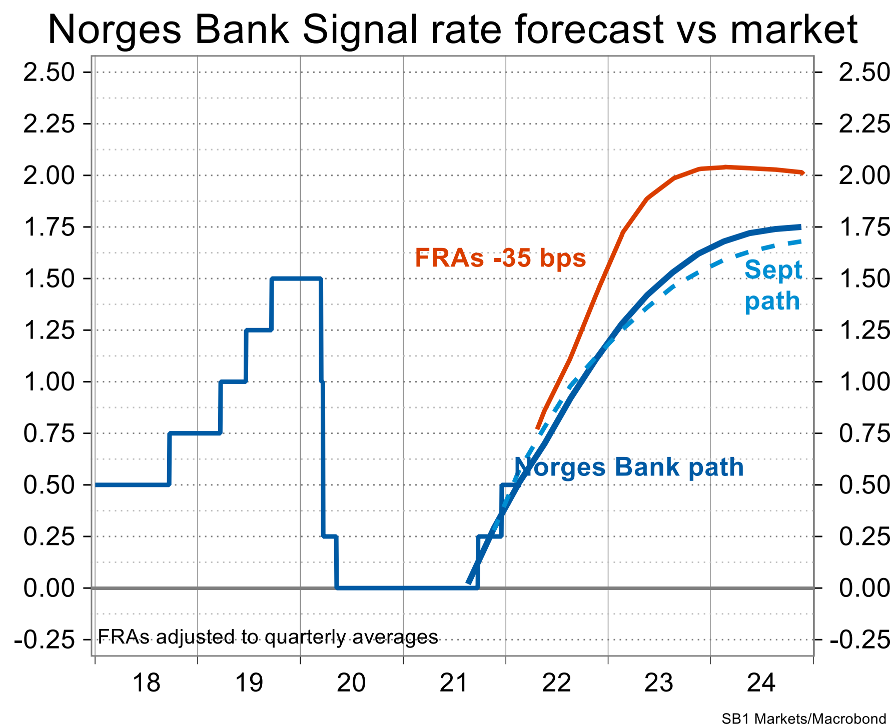


- The **3 m NIBOR** has been at elevated level recent weeks but the spread to a reasonable NoBA signal rate is narrowing somewhat
- The **USD LIBOR-OIS spread** at 10 bps is at the low side, but higher two weeks ago

A Ukrainian pause? FRAs down last week

Still, the FRA path is steeper than NoBa's rate path – for good reasons





- Market FRAs are now discounting a steeper interest rate path than NoBa presented in December – <u>or the expected NIBOR spread widened substantially – which we deem unlikely</u>
- If NoBa hikes March 24 (by 25 bps, and not in May), the average NoBa rate will be 0.73% in the March FRA period
- Thus, the **March-22 3 m** contract at 1.17% implies 100% probability for a 25 hike with a 44 bps NIBOR spread.
  - » If a 35 bps spread is assumed, almost a 40% probability for a 50 bps hike or if 25 bps in March, or an even higher probability for a May hike
  - » Most likely, the NIBOR spreads is expected be higher than 35 bps, but below 44 bps – and a the probability for a 50 bps March/25 May hike is well below 50%
- The June contract at 1.42% captures a lot of scenarios, including a small probability for a June signal rate at 1.25%
- The market expects 1.5 – 1.75 bps signal rate in December, at a peak at above 2% in late 2023

US vs. Norway: The need for as monetary policy tightening

Less need for tightening in Norway, and households' response to higher short term rates far stronger

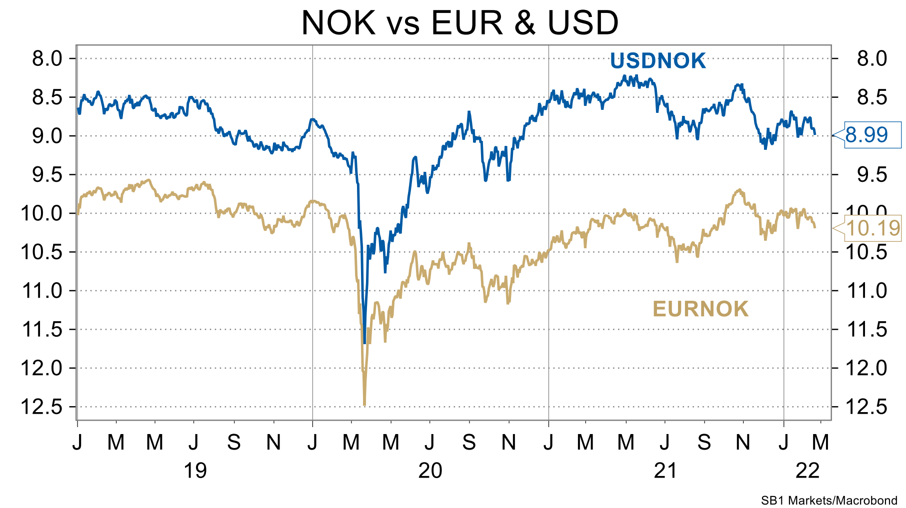
	USA	Norway
Inflation	Total 7.5%/core 6%	Total 3.2%, core 1.3%
Inflation expectations	Market 2.4%, households 3%+	Not higher (but probably not lower either)
Employment rate	Still below par	Well above the p-p level
Unemployment	Close to record low	Below average
Vacancies	Record high	High
Wage inflation	Accelerating rapidly	Accelerating slowly
House prices	Up 30% from Q4-19 Up 18% y/y now	Up 16% from Q4-19 Up 6% y/y now
Household debt	To 7% y/y from 3%	Unch at 5%
Househ. debt/inc. Ratio (vs. impact of higher short term rates)	>100%, from 135% in '08	246%, from 196% in '08
Floating or fixed mortgage rates	Fixed	Floating

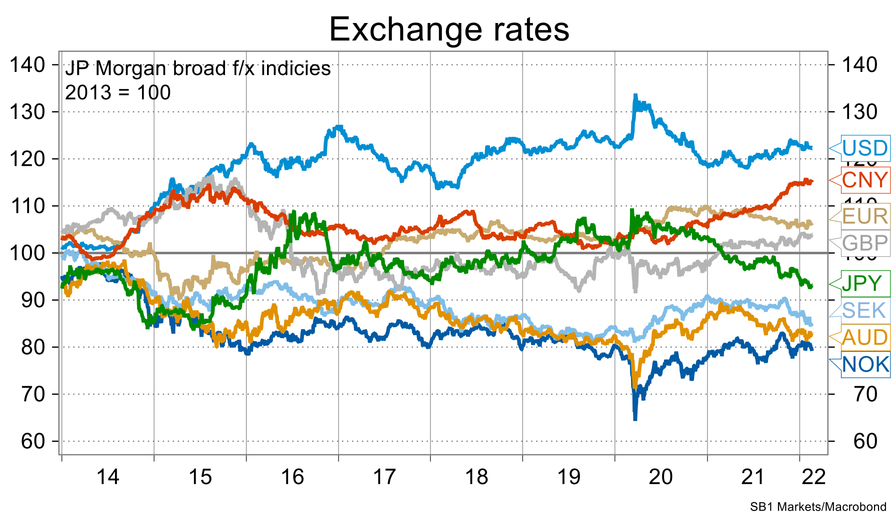
- US has a majority of the 'red' cells – in favour of a faster monetary thightening
  - » The economy is 'hotter'
  - » The impact of higher rates will be stronger in Norway than in the US

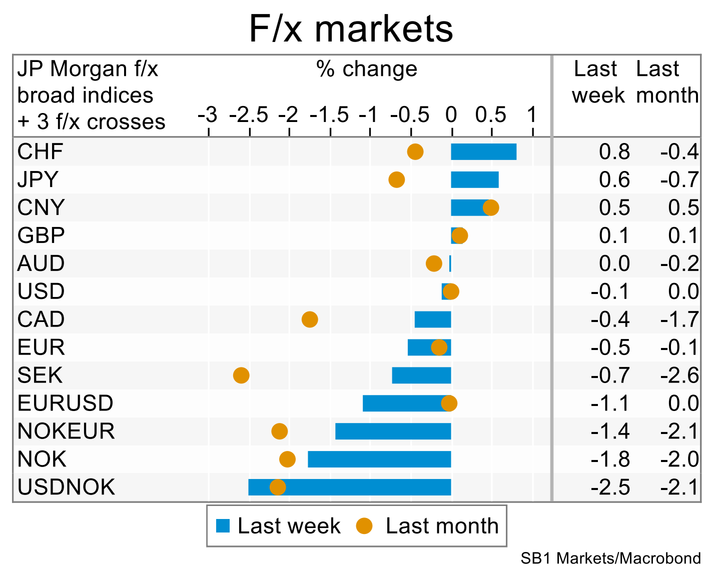
SpareBank 1 MARKETS

NOK the f/x loser last week, for no good reason?

The USD unch, the EUR down



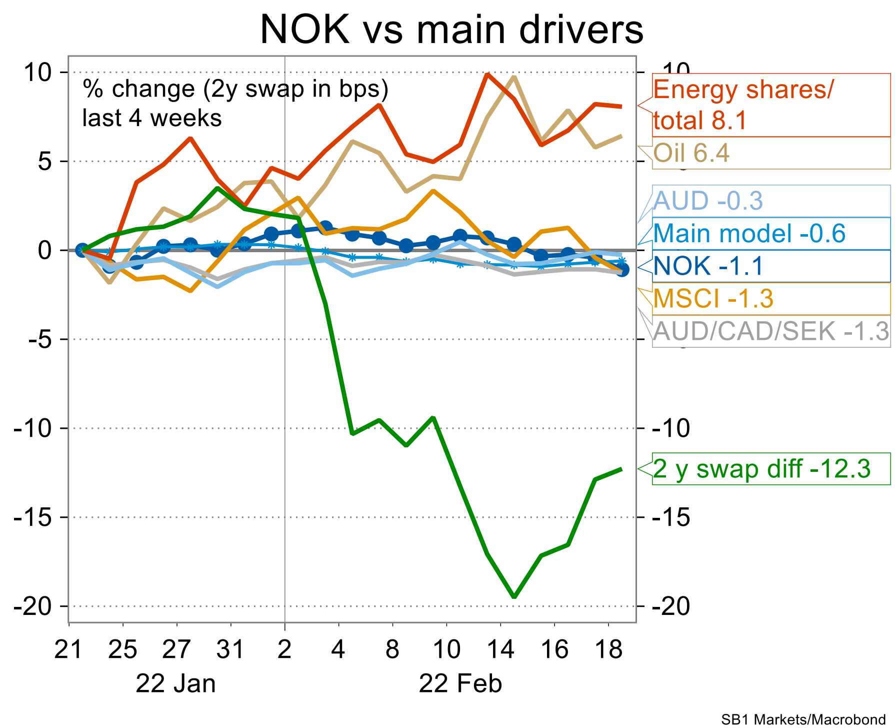


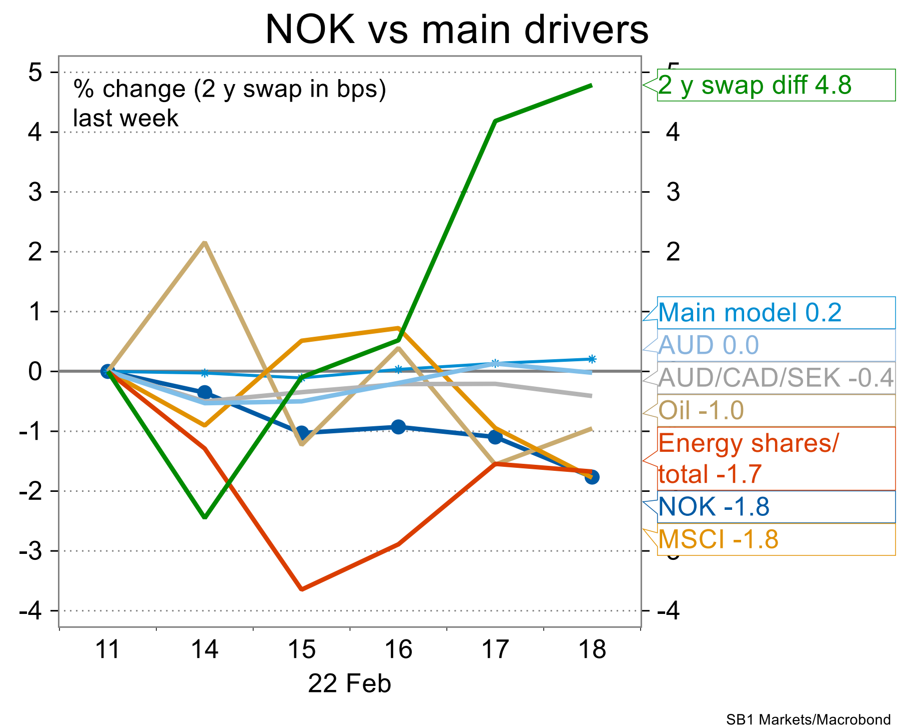


JP Morgan f/x broad indices + 3 f/x crosses	Last week	Last month
CHF	0.8	-0.4
JPY	0.6	-0.7
CNY	0.5	0.5
GBP	0.1	0.1
AUD	0.0	-0.2
USD	-0.1	0.0
CAD	-0.4	-1.7
EUR	-0.5	-0.1
SEK	-0.7	-2.6
EURUSD	-1.1	0.0
NOKEUR	-1.4	-2.1
NOK	-1.8	-2.0
USDNOK	-2.5	-2.1

NOK down 1.8% last week, without any support from our model

The oil price fell, as did global equities but the interest rate differential widened





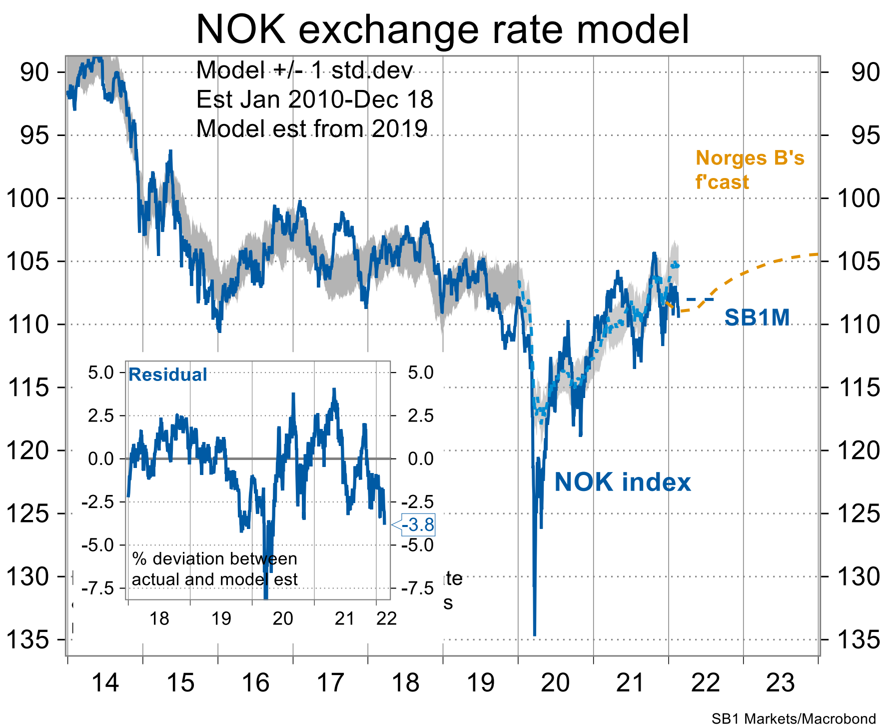
The status vs. the normal drivers down vs all of them:

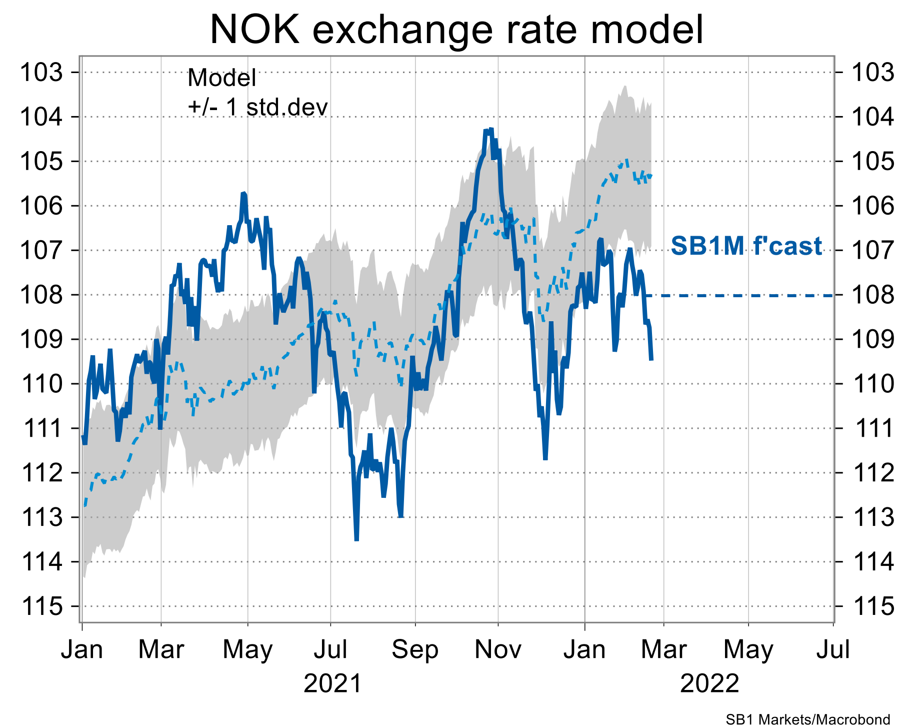
- ***The NOK unch - the level 4% below the model est (from - 2)***
- The NOK is 5% weaker than our AUD/CAD/SEK-model, our 'super-cycle peers', predicts (from 4)
- NOK is 2.7% stronger than a model which includes global energy companies equity prices (vs the global stock market), but less than last week (from 3.5%)

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

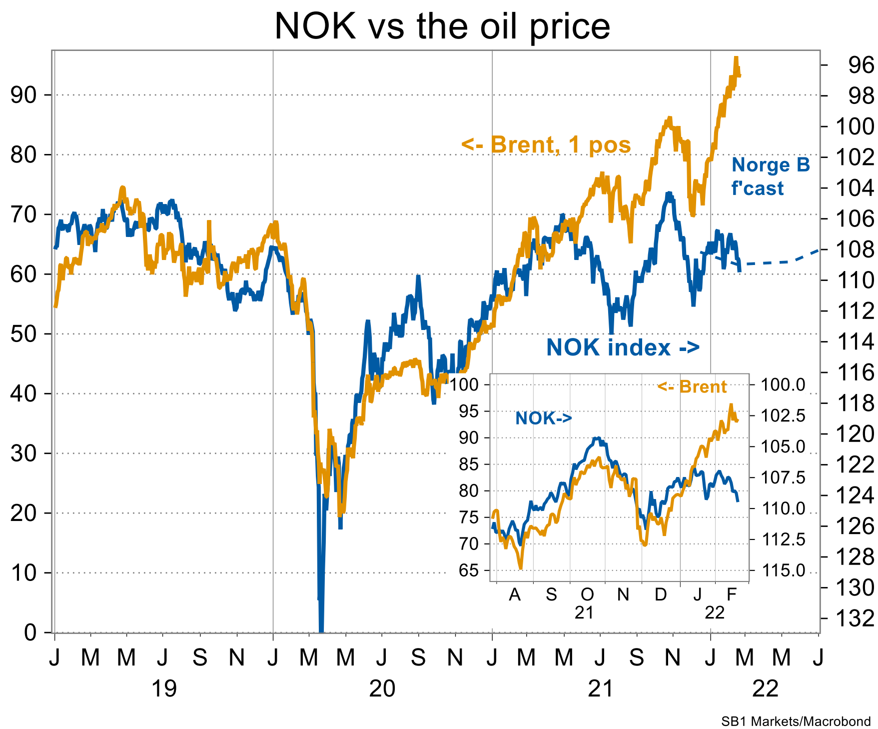
NOK lags our model by 4%

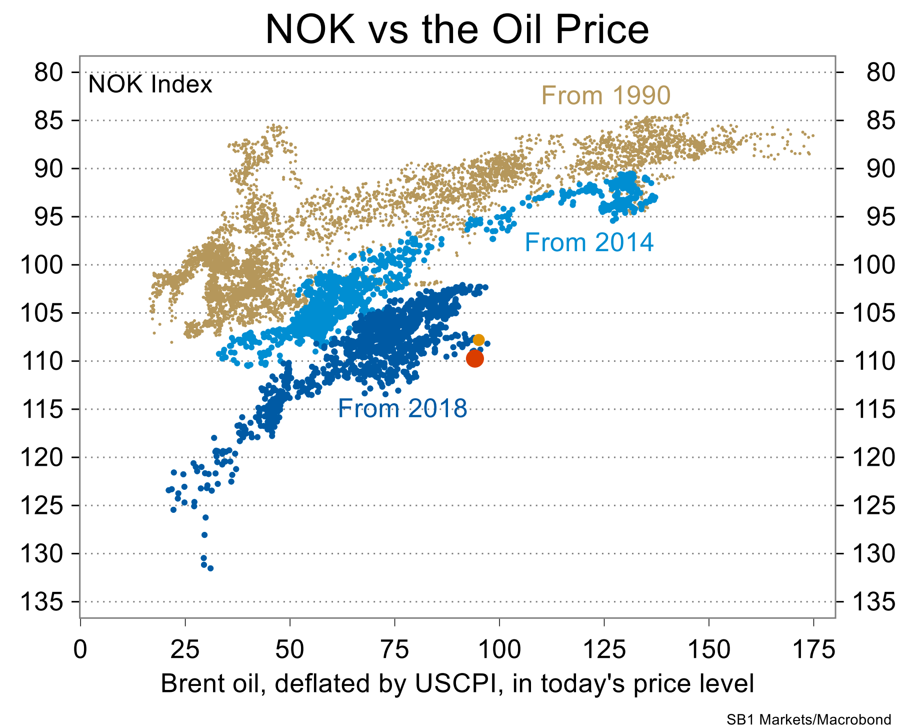
Time to buy?





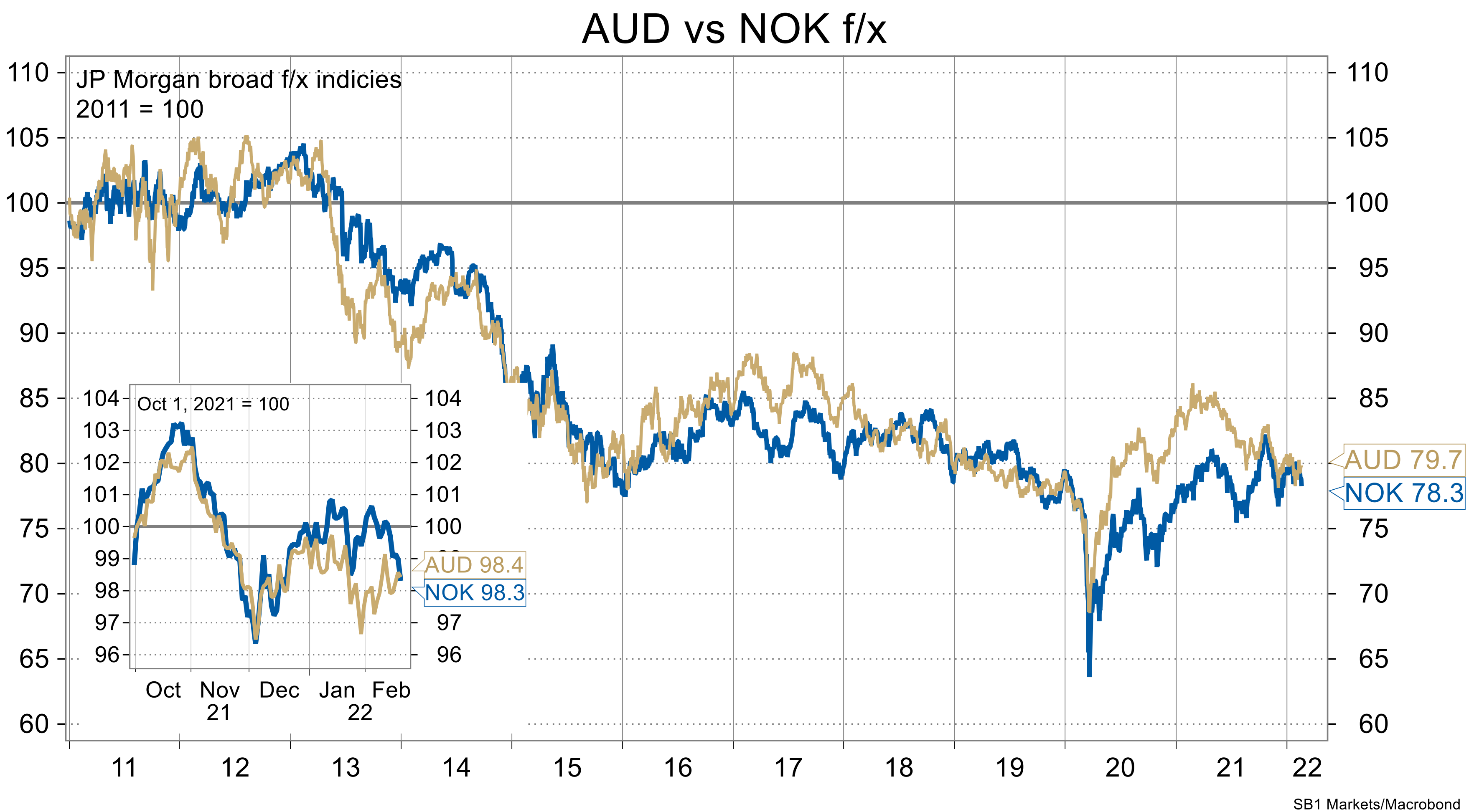
NOK down more than the oil price last week





- 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

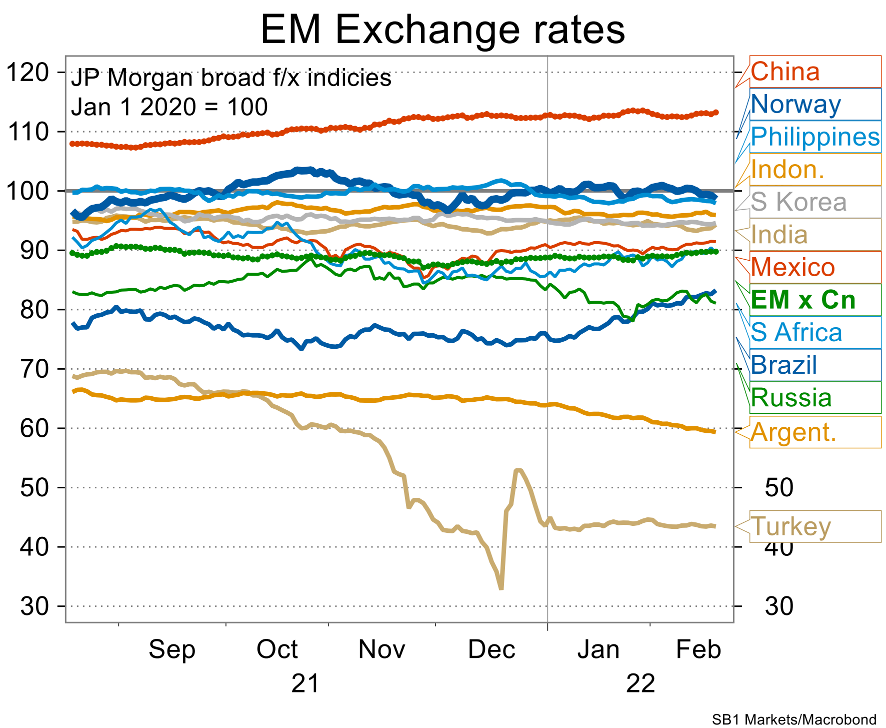
NOK down last week, the AUD was flattish

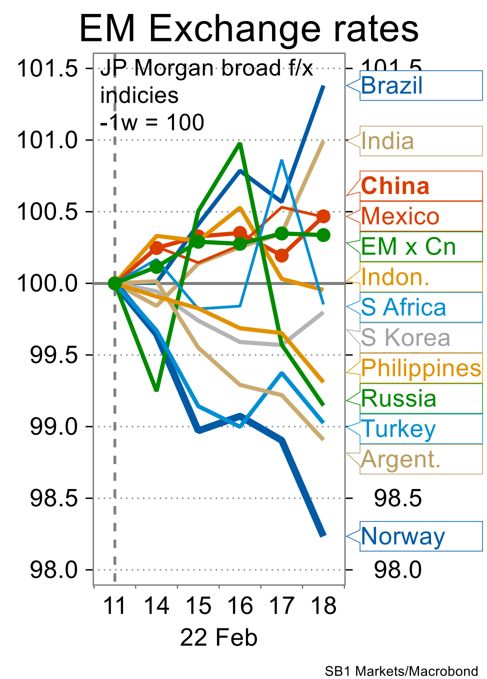


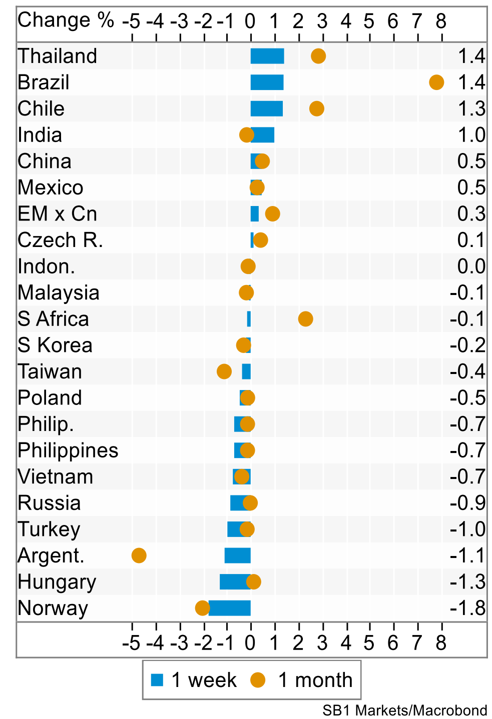
The two f/x indices are back to the 2011 parity (vs each other, from which they never since have deviated much)

The Russian rouble further down but not that weak (and NOK fell more…)

Mixed among other EM f/x. The CNY is slowly drifting upwards







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