March 28 2022

Macro Weekly

Week 13/2022

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Highlights

The world around us

The Norwegian economy

Market charts & comments

Last week, part I

- **The War/Sanctions**
  - » **Stalemate and more indiscriminate Russian bombardments** of civilian targets. Some positive news on peace talks, some negative. Russia may now be focusing on ‘rescuing’ the two eastern regions & Crimea, accepting that a full take-over of Ukraine has turned out to be impossible/far to expensive
  - » **Russia** wants to be paid in roubles for its gas exports. A strange position, the country will anyway receive f/x – and the roubles they can print themselves. Still, energy prices rose on the news
  - » **Raw material prices** mostly rose last week but most are down from the peaks just after the Russian invasion. **Food prices** are slowly sliding down; are the (likely) impacts of excessive hoarding fading? Sure, the upside risk is still substantial, if ‘everything’ goes wrong. More reports on component shortages in different sectors.
  - » **Sanctions** are still being tightened but the UK foreign minister have stated that many sanctions will be lifted if/when a reasonable peace deal is agreed upon
  - » **Expectation surveys** among **German investors** (ZEW) & **businesses** (Ifo), **EU and Norwegian consumers** <u>fell as never seen before in March, down to very low levels</u>. UK cons. confidence fell further too. In the **US**, sentiment fell just slightly but from an unusual low level (especially given the current state in the economy, except for inflation)
- **The virus**
  - » **China** is still struggling to keep the Omicron variant at bay, now it is Shanghai’s turn to be partially locked down. The zero tolerance strategy is challenging when the virus is as contagious as the current variant
  - » **In UK**, more new cases & hospitalisations again but few get really sick and few need an ICU bed
- **Preliminary March PMIs**
  - » These surveys kept up better than expected, signalling that so far, overall activity has not been harmed by much by war & sanctions. We estimate gain the global composite PMI gained 1.3 p to 54.7. However, it is far to early to expect the PMIs (which report changes in actual activity, not expectations) to report serious impacts from the war & sanctions. Still, there were some possibly impacts: delivery times rose in the EMU but fell further in the US and prices rose faster in Europe (and the global price indices probably rose). **US regional surveys** surprised at the upside, signalling a stronger ISM in March

Last week, part II

- **Inflation & monetary policy**
  - **Fed governor Powell** reiterated and strengthened his inflation worries at last Monday, 3 working days after the FOMC meeting – and interest rates shot up, once more – and by up to more 40 bps last week. In the market, the Fed funds rates is expected up by 50 bps in May and another 50 bps in June. Even so, the funds rate will be just 1.25%, half the assumed neutral rate, while the labour market is extremely tight, wage inflation is accelerating faster than ever – and inflation is at 8%. The 10 y gov bond rate approached 2,5%! Rates rose all over the curves everywhere
  - Even after **Norges Bank** lifted the interest rate path more than ever, by up to 80 bps, and up to 2.5% at the peak vs the 1.75% Dec forecast (we assumed 2.2%), and 'promised' 3 more hikes in '22 and 4 more hikes in 2003 (and hiked the signal rate to 0.75% of course), the 2 y swap rate rose less than among our trading partners! FRA rates rose by up to more than 40 bps last week, and the FRA curve is more than 50 bps above Norges Banks's new 'aggressive' path – and it is topping out above 3%
  - **In Sweden**, the market is pricing in 10 hikes before end of 2023. Until now, the Riksbank has stated it expect to conducts its ZIRP policy until H2 2024. We can hardly await the next MPR from the Riksbank, the board has a huge communication challenge!
  - **The Fed in US and the US economy is in even more dire straits**. We think risk markets substantially underestimates how the economy will look like, if inflation should be brought down towards the 2% target. We are not sure at all how much the Fed will have to hike, or how much long bond yields will have to increase (pushed up by QT, or QE in reverse) to get inflation down. However, we are confident that the Fed will not succeed before
    - growth in domestic demand and GDP has slowed substantially, squeezing corporate margins
    - the vacancy rate has fallen sharply, unemployment has started to increase, wage inflation has come substantially down
  - There is of course an obvious risk that US after a while could end up in a recession – as have been the usual outcome of monetary tightening campaigns. Even if the economy does not fall into a recession, the signs on growth, margins, unemployment, and thereafter wage growth are given
- **USA**
  - **Durable orders** were a tad weaker than expected in February but the trend is strong
  - Housing data are mixed. Is the close to 5% 30 y fixed mortgage rate putting a dent in demand? It's possible, pending home sales fell further in February, and new home sales sagged. However, until January price appreciation accelerated, and sales may be slowing due to an extreme lack for supply
- **EMU**
  - **Credit growth** is slowly accelerating among households, following substantial increases in home prices during the pandemic
- **Norway**
  - **Norges Bank:** Check above
  - **The LFS unemployment rate** fell further in January, and employment rose further. The participation rate has stagnated since last summer, signalling that the reserve on the labour market is exhausted
  - However, the no. of **employees** surprisingly fell the payrolls stats, measured in (mid) February. We are pretty sure a new trend is not established – and anyway the level is still high. The public sector was responsible for most of the decline in payrolls in February
  - **This morning:** Both February retail sales and credit growth was weaker than expected

SpareBank 1 MARKETS

This week: Besides War, Sanctions, Commodity Prices – US labour market, manuf. PMIs

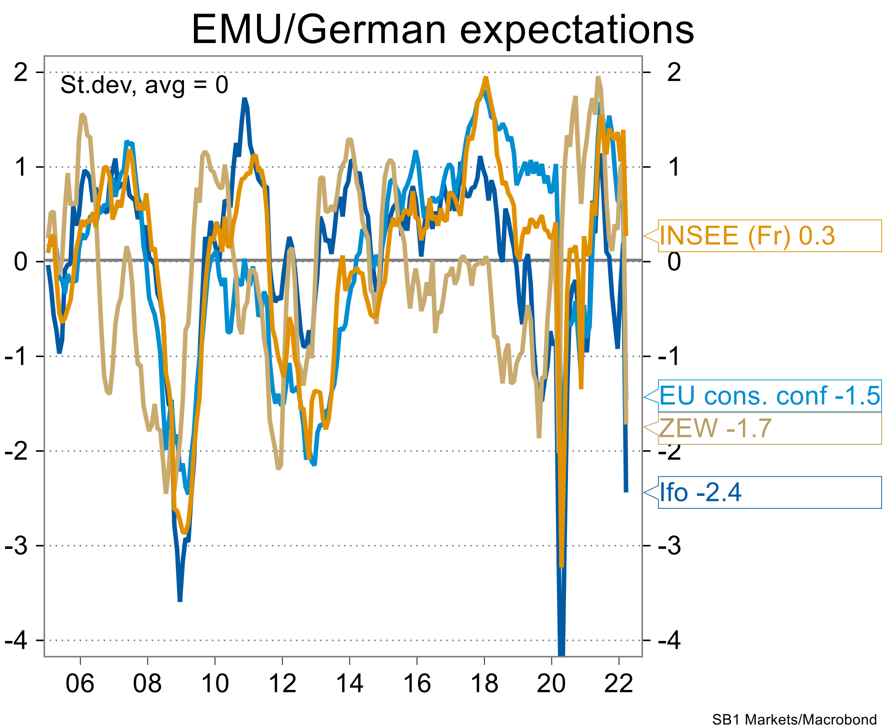
Time	Count.	Indicator	Period	Forecast	Prior
Monday March 28					
08:00	**NO**	**Retail Sales W/Auto Fuel MoM**	**Feb**	**0.1%(1%)**	**0.4%**
08:00	**NO**	**Credit growth (C2) YoY**	**Feb**	**(4.9%)**	**5.0%**
14:30	US	Advance Goods Trade Balance	Feb	-$106.6b	-$107.6b
Tuesday March 29					
08:00	SW	Retail Sales MoM	Feb		4.5%
15:00	US	S&P CoreLogic CS 20-City YoY	Jan	18.6%	18.6%
16:00	US	Conf. Board Consumer	Mar	107.0	110.5
16:00	**US**	**JOLTS Job Openings**	**Feb**	**11000k**	**11263k**
Wednesday March 30					
01:50	JN	Retail Sales MoM	Feb	-0.3%	-1.9%
09:00	SW	Economic Tendency Survey	Mar	110	113
09:00	SW	Consumer Confidence	Mar		88.9
11:00	**EU**	**Economic Confidence**	**Mar**	**109.4**	**114**
14:00	GE	CPI YoY	Mar P	6.1%	5.1%
14:15	US	ADP Employment Change	Mar	438k	475k
14:30	US	GDP Annualized QoQ	4Q T	7.1%	7.0%
Thursday March 31					
01:50	JN	Industrial Production MoM	Feb P	0.5%	-0.8%
03:30	CN	Manufacturing PMI, NBS	Mar	50.0	50.2
03:30	CN	Non-manufacturing PMI	Mar	50.6	51.6
08:00	GE	Retail Sales MoM	Feb	0.5%	2.0%
11:00	**EU**	**Unemployment Rate**	**Feb**	**6.7%**	**6.8%**
14:30	US	Personal Income	Feb	0.5%	0.0%
14:30	US	Personal Spending	Feb	0.5%	2.1%
14:30	US	PCE Core Deflator YoY	Feb	5.5%	5.2%
14:30	US	Initial Jobless Claims	Mar-26	200k	187k
Friday April 1					
03:45	CN	Manufacturing PMI, Caixin	Mar	50.0	50.4
08:30	SW	Manufacturing PMI	Mar	58.0	58.6
10:00	NO	Manufacturing PMI	Mar	54.8	55.9
10:00	EU	Manufacturing PMI	Mar F	57.0	57.0
10:00	**NO**	**NAV Unemployment Rate**	**Mar**	**2.1% (2.1)**	**2.3%**
11:00	**EU**	**CPI Estimate YoY**	**Mar**	**6.7%**	**5.8%**
11:00	EU	CPI Core YoY	Mar P	3.1%	2.7%
14:30	**US**	**Nonfarm Payrolls MoM**	**Mar**	**475k**	**678k**
14:30	**US**	**Unemployment Rate**	**Mar**	**3.7%**	**3.8%**
14:30	**US**	**Average Hourly Earnings MoM**	**Mar**	**0.4%**	**0.0%**
14:30	US	Average Hourly Earnings YoY	Mar	5.5%	5.1%
14:30	**US**	**Labor Force Participation Rate**	**Mar**	**62.4%**	**62.3%**
15:45	US	Manufacturing PMI	Mar F	58.5	58.5
16:00	US	Construction Spending MoM	Feb	1.0%	1.3%
16:00	**US**	**ISM Manufacturing**	**Mar**	**58.6**	**58.6**
17:00	**WO**	**Manufacturing PMI**	**Mar**	**53.8**	**53.6**
	US	Auto sales	Mar	13.95m	14.07m

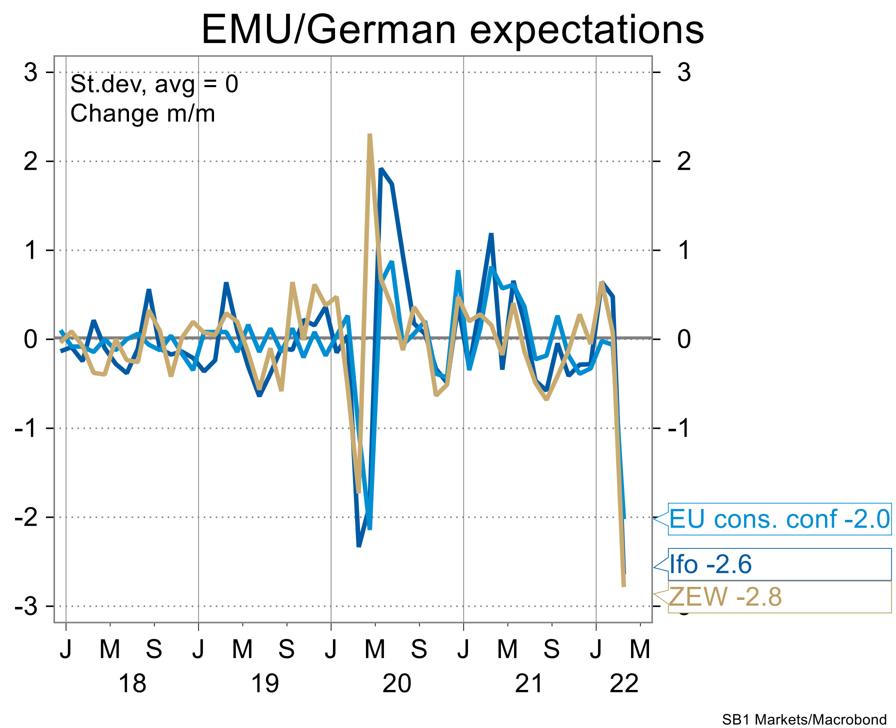
- **Manufacturing PMI**
  - » **Preliminary March PMIs** from EMU, Japan, UK & US were OK – but rather useless vs assessing consequences of the war/sanctions – it would be too early to expect large impacts in March besides the price changes – and increasing delivery times in Europe (but not in the US). All other countries report at Wed/Thursday, with China in focus. Some virus problems? The global manuf. index most likely rose. In the US, the manufacturing ISM is expected unch. The PMI & regional surveys suggest a small lift
- **USA**
  - » Growth in **employment** is expected to slow but **unemployment** to decline further, and **wage inflation** to accelerate again. The participation rate is expected one tick up, and the trend is now finally slowly upwards. The JOLTS survey will confirm an extremely tight labour market and large no. of unfilled vacancies. Small businesses will probably report than openings are hard to fill, and to report aggressive wage plans
  - » The Feb **household income & spending** report will report higher inflation, like the CPI has told us already. March **auto sales** are expected further down
  - » The last version of the **Q4 GDP** accounts will fill some black holes, like on corporate profits
- **EMU**
  - » **More business surveys** will be published but they are probably not relevant gauge the impact of was/sanctions. We already know that expectations have collapsed, like we have not seen before, both among households & businesses
  - » **HICP (CPI) inflation** is expected further up, while **unemployment** is expected further down from the lowest level since 1981
- **Norway**
  - » We expect the **NAV open unemployment rate** to decline further, also in seas. adj. terms, to 2.0%. A very low level indeed
  - » **Retail sales** are heading down vs. more normal levels but we expect a small uptick in February
  - » **Credit growth** may have slowed to below 5% in February

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

European expectations fell off the cliff in March, except for the French survey

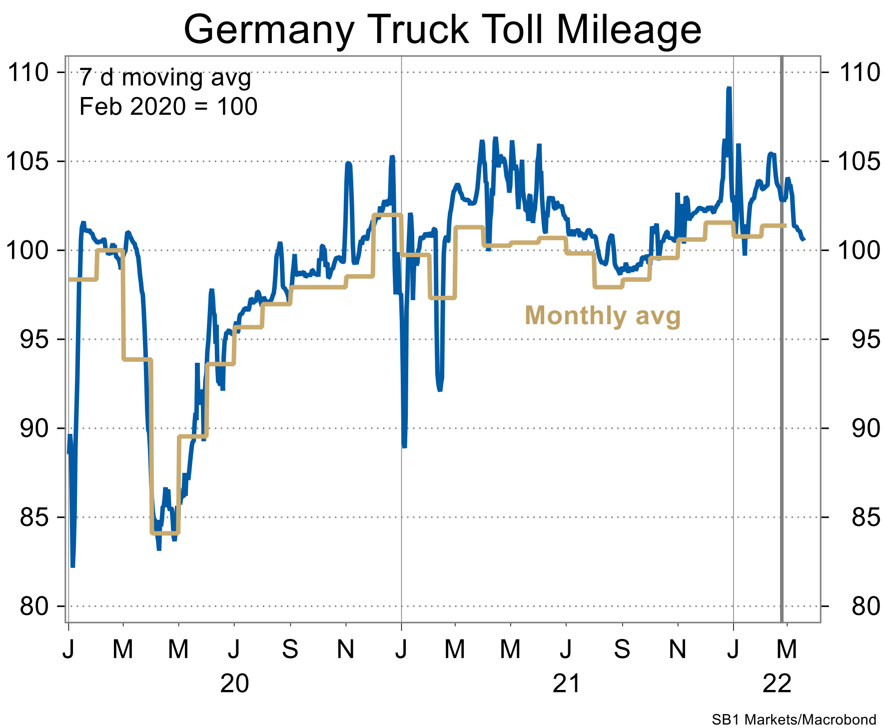
The largest decline ever, to low levels. For good reasons. Activity is probably not (yet) hit

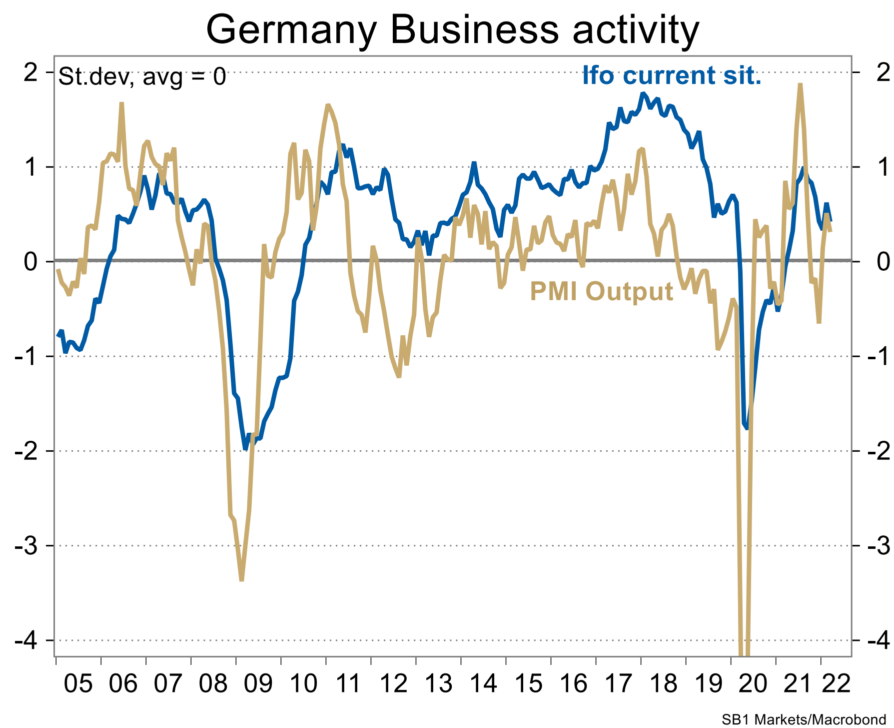




- Both EU consumer confidence, expectations in the German investor/analysts ZEW survey, and expectations in the IFO survey all 'collapsed' in March.
  - » At least the ZEW survey, but also a substantial part of the others were conducted in when the German stock market tanked, and oil og gas prices skyrocketed in the first two weeks after the Russian invasion
- The outlook index the French INSEE manuf. survey fell sharply too, but remained above avg. The French comp. PMI rose in March, while the German PMI fell
- Still, these surveys are of course warning signs

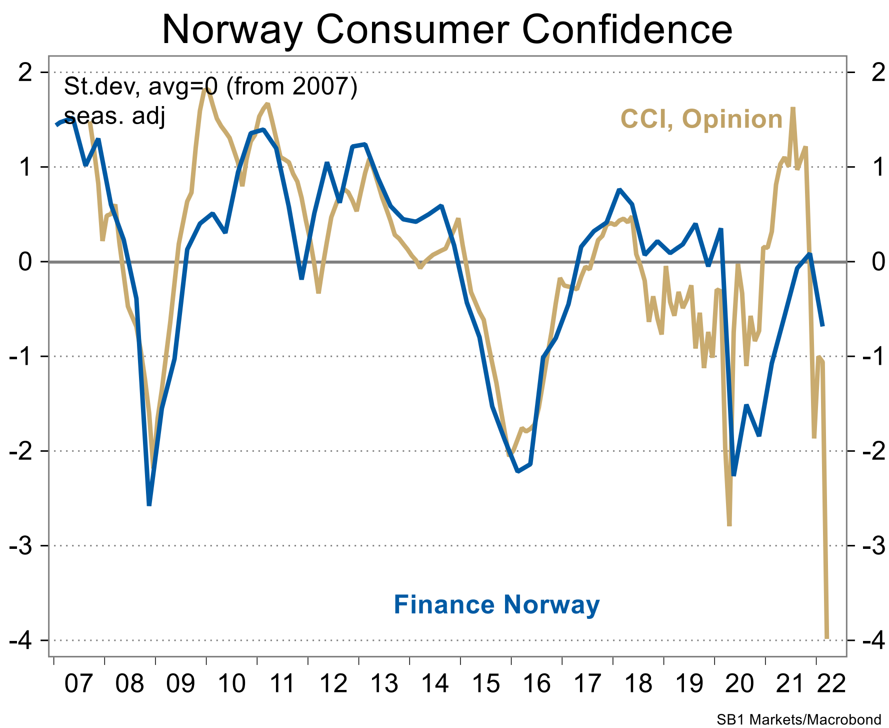
Actual activity probably not yet hurt, at least not by much





Consumer confidence collapsed in March, to ATL by far. Down 3 st.dev, to -4!!

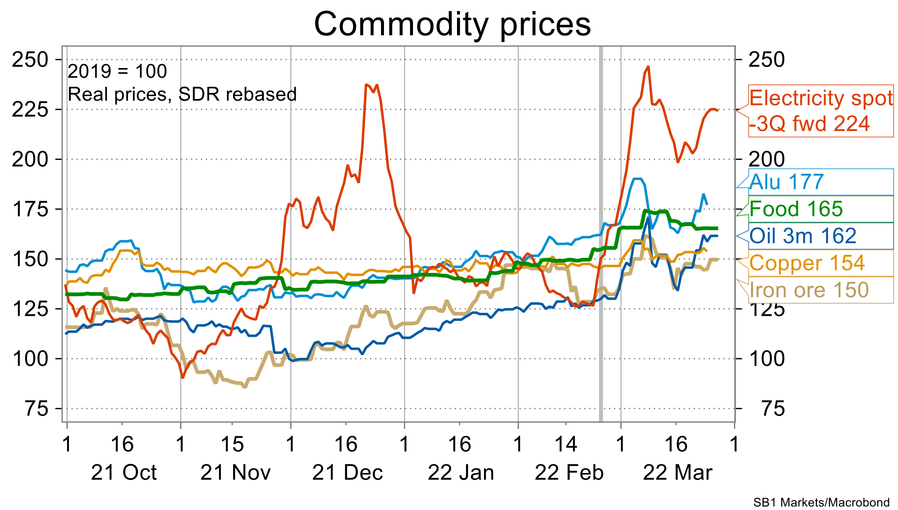
There is just one possible explanation: The War

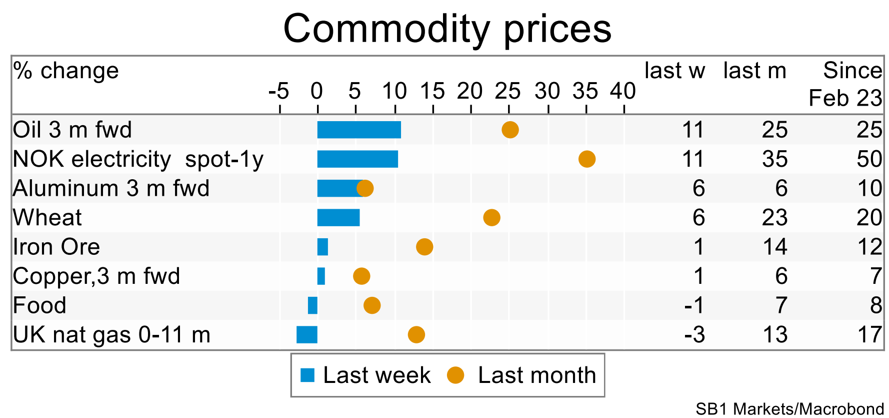


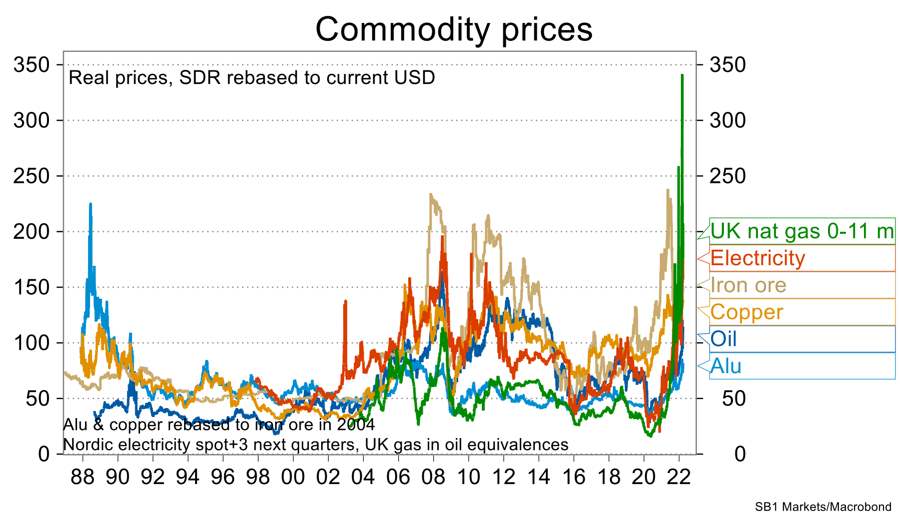
- **The decline in CCI** from Opinion was the largest one month drop ever, to the lowest lever ever – rather dramatic
- **The war in Ukraine** is the only news since the previous survey was conducted in March that can explain the unprecedented drop in confidence
  - » **Fear of higher inflation** – also present before the invasion – may also explain some the drop – and the level was well below average in both Dec, Jan & Feb, very likely due to the steep rise in electricity prices
  - » **Norges Bank's rate hike** last week – and the lift in the interest rate path – was announced after this survey was conducted
- Besides (exaggerated, most likely) fears of inflation, the economic situation is close to superb, strong growth in employment, low unemployment, low interest rates, a strong stock market, a stable housing market – and no more corona restrictions
- **Will consumption follow suit?** We doubt, and in no way at a scale suggested by the confidence index

Mixed commodity prices last week following 2 week's decline

Food prices fell for the 3rd week in row. Less hoarding? All prices are up since before the invasion



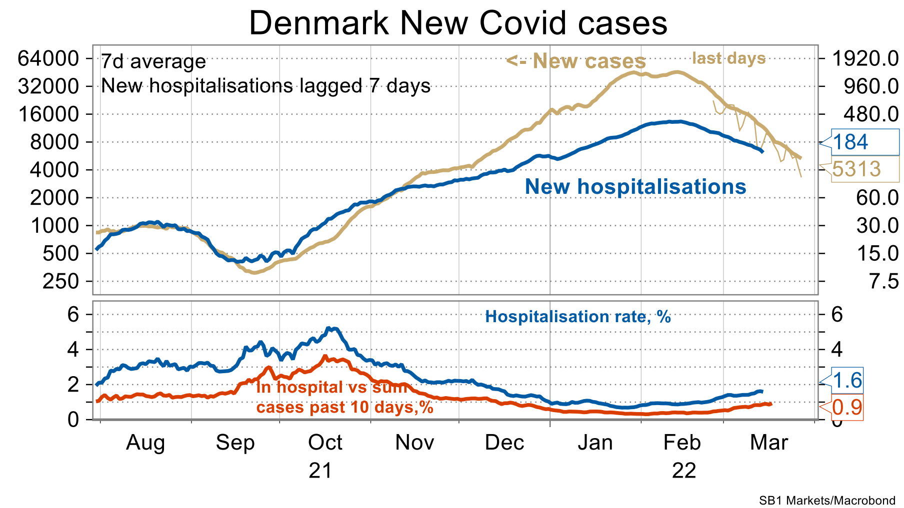


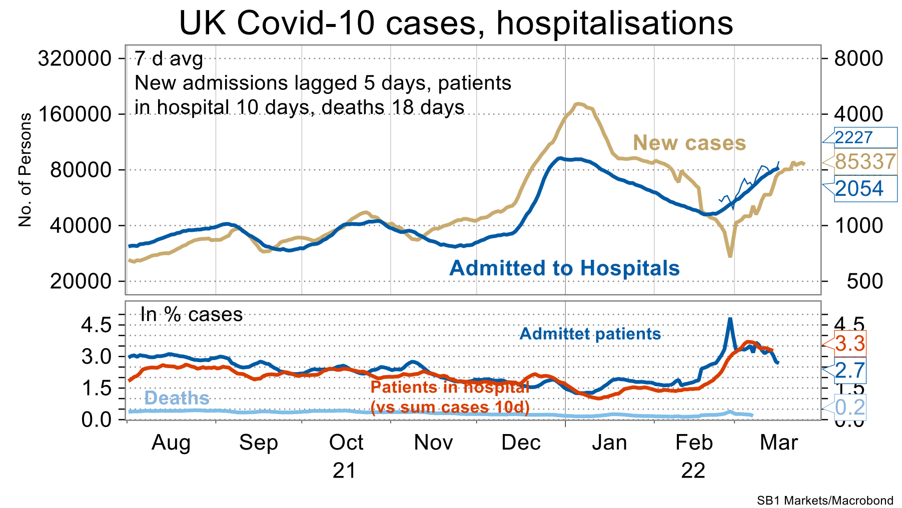


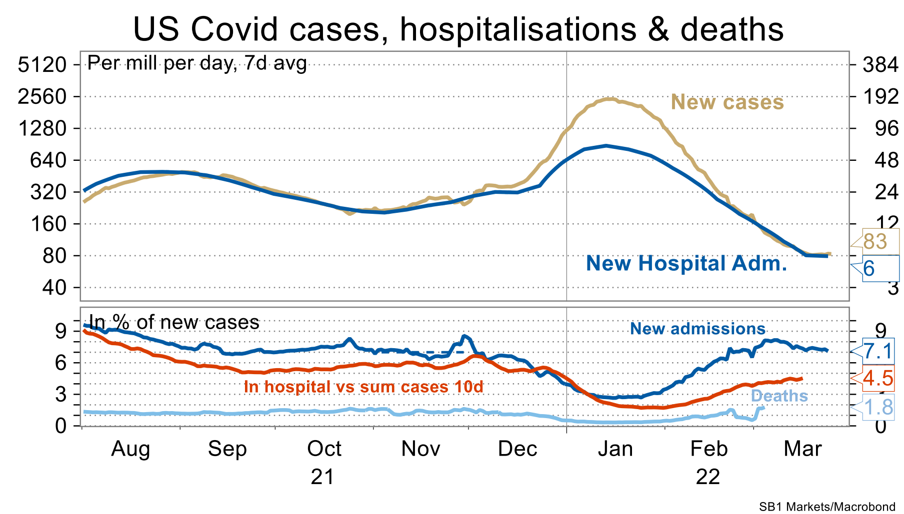
- Will **Russia be allowed to export** oil and gas, will buyers abroad buy the stuff or will **Russia turn the tap off**?
  - » There seems to be willing buyers of rebated Russian oil
  - » Russia is still pushing gas through the pipelines to Europe
- Will Russia/Ukraine sell grain – restrictions are introduced (as for many other goods)?

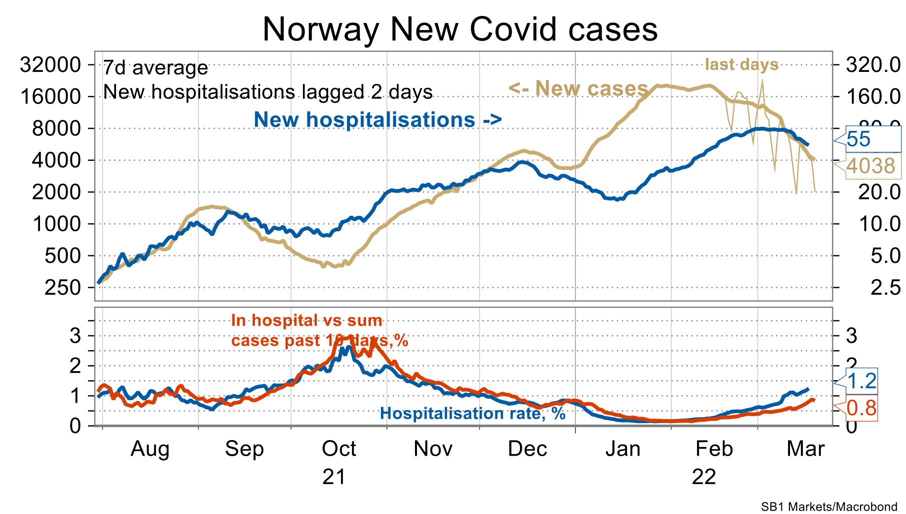
Covid recap: UK has some challenges with the BA.2 Omicron variant

More patients admitted but now hospital crisis – check next page. Elsewhere in the West, no problem



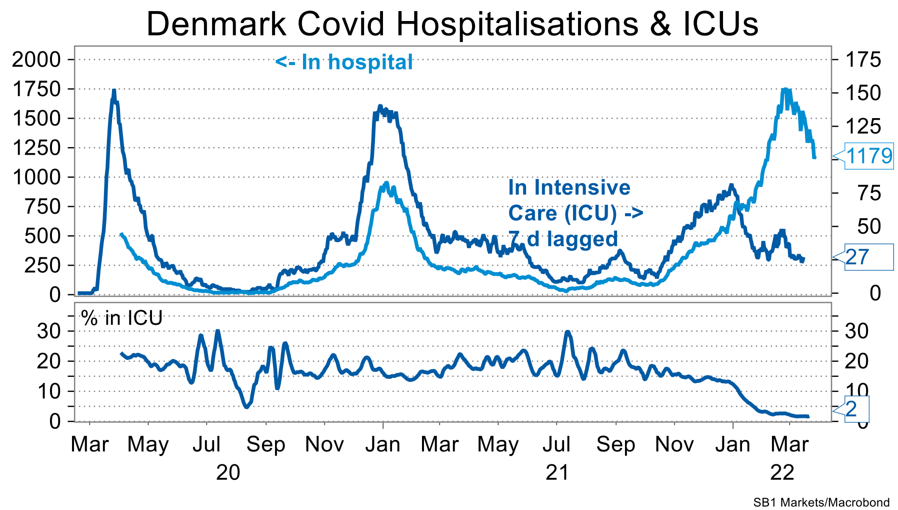


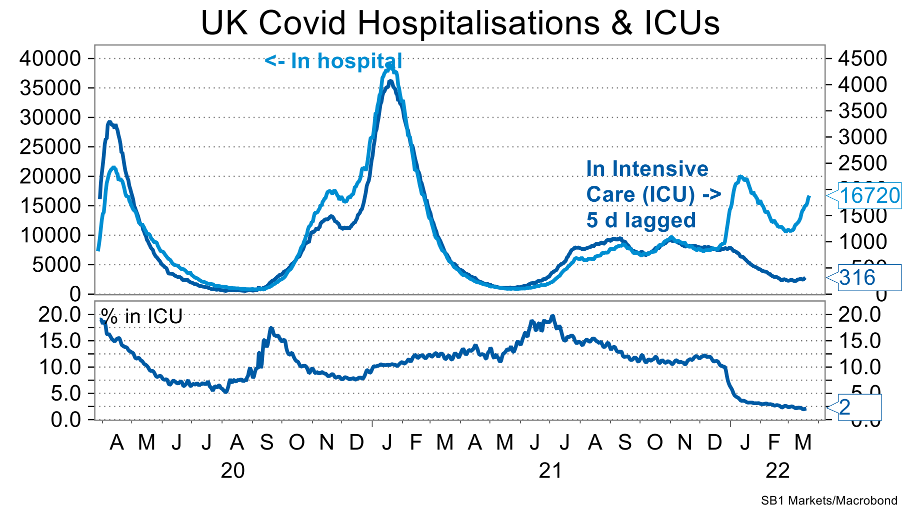


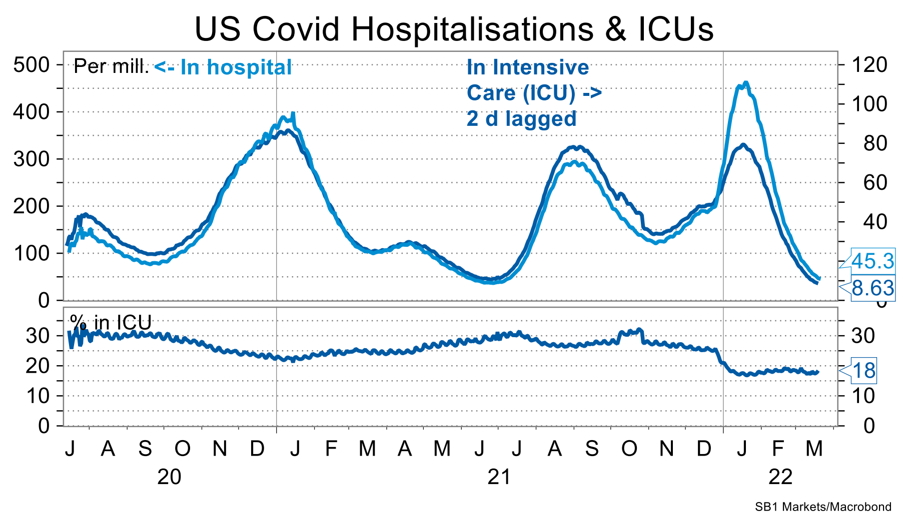


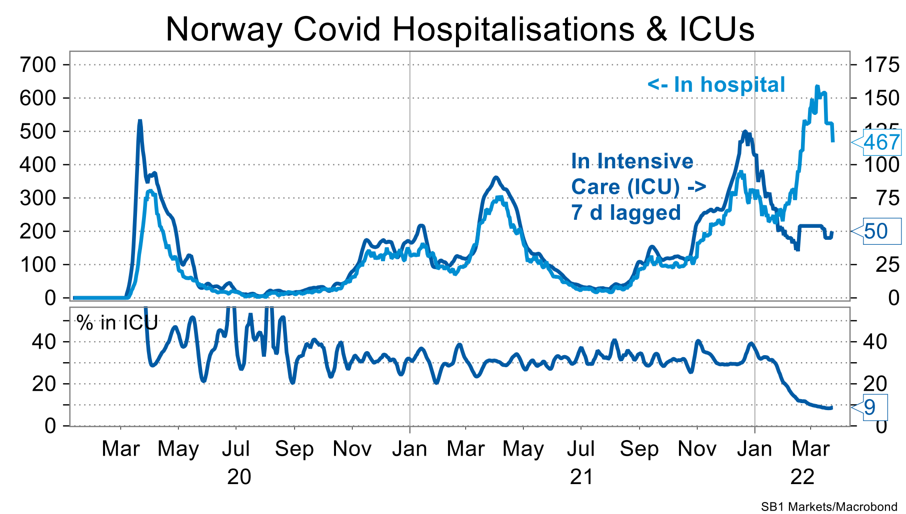
More patients in UK hospitals but no increase in the ICU usage

Good news from other countries

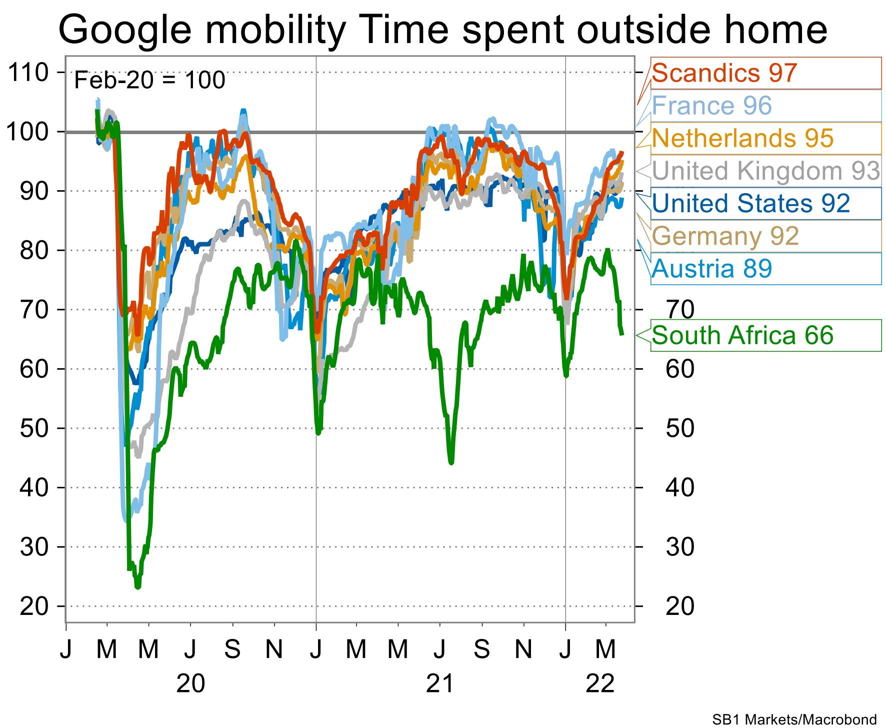


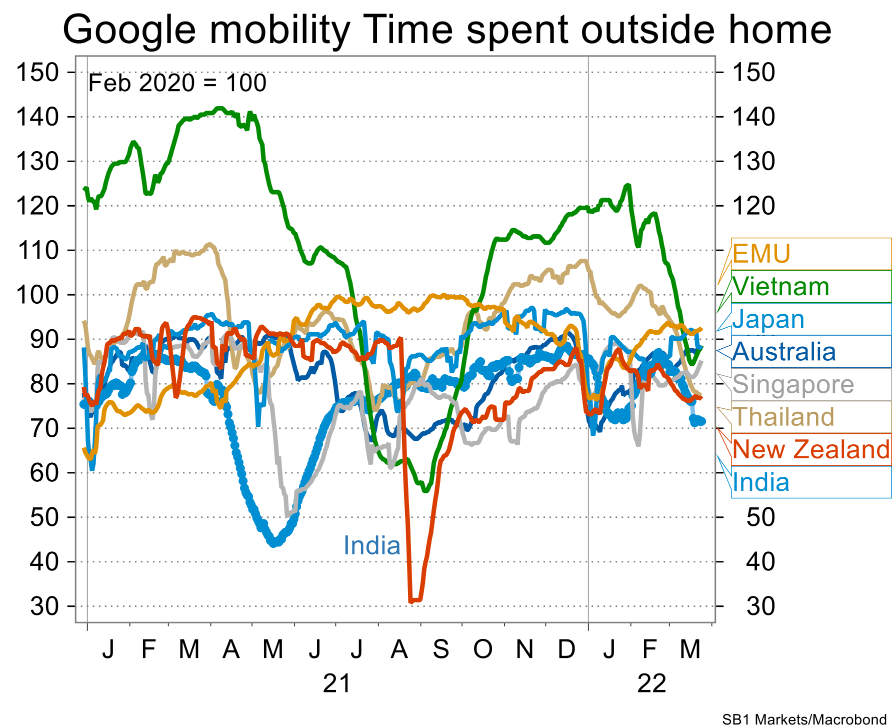






Mobility on the way up in the West, still some' challenges in the East (x Japan)

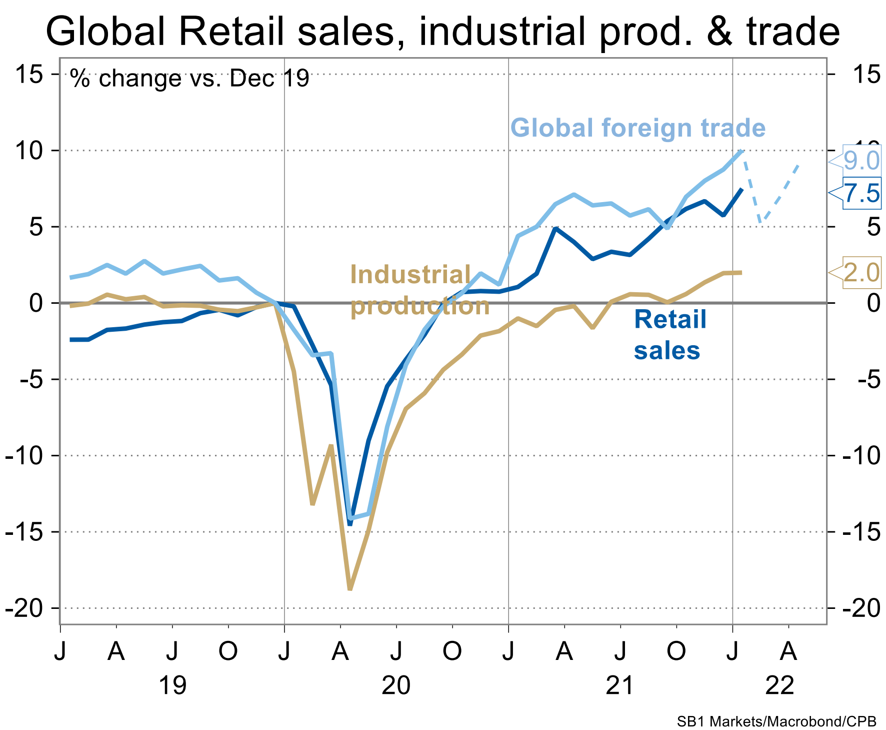


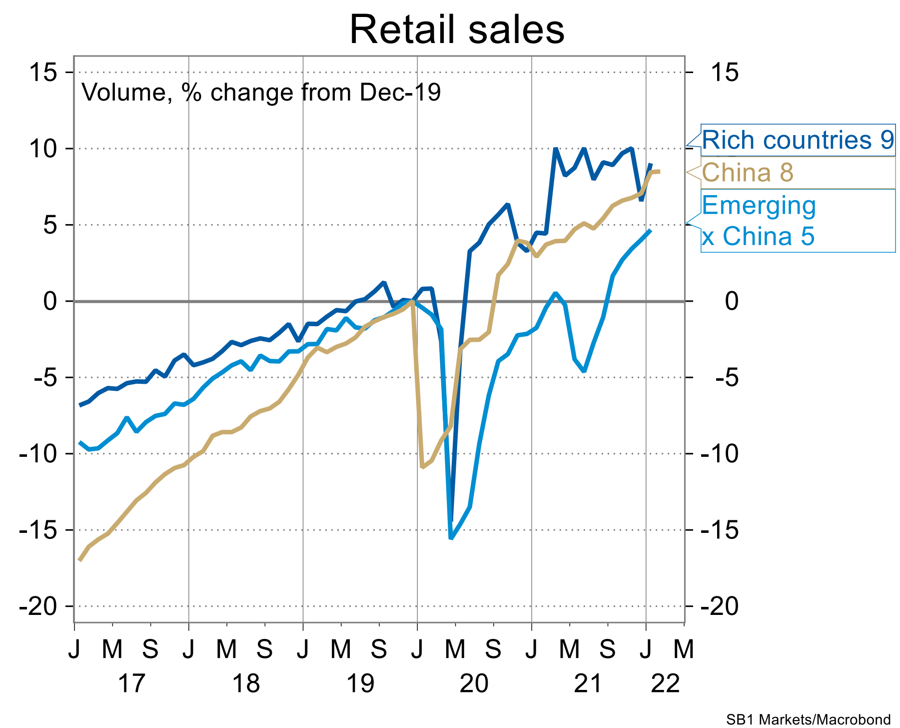


SpareBank 1 MARKETS

Global retail sales recovered in January. Probably down in Feb, trend strong

Chinese data have been revised up, lifting the global retail sales visibly

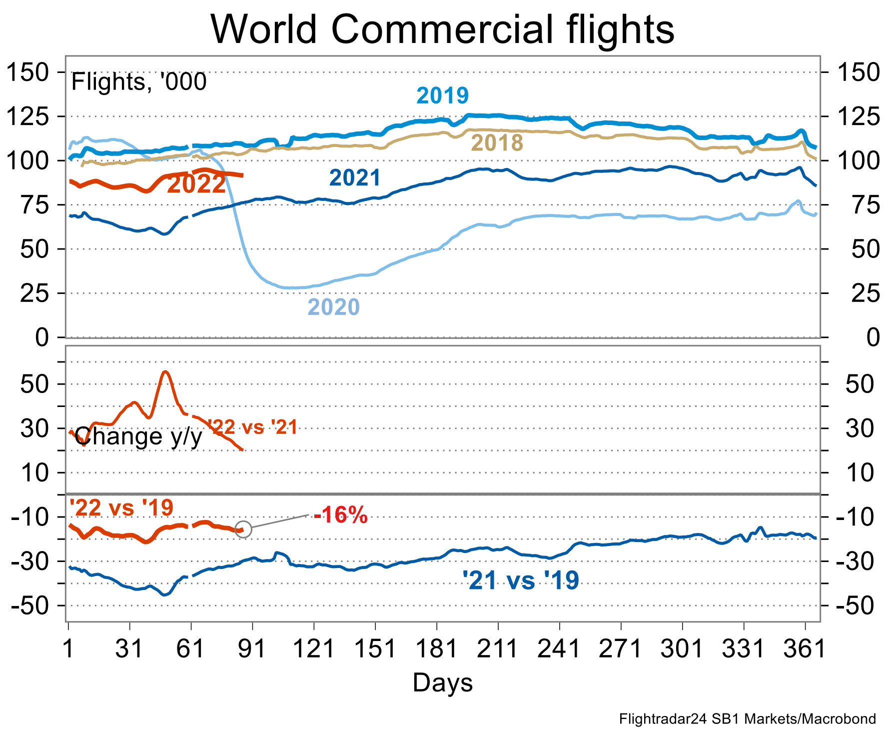


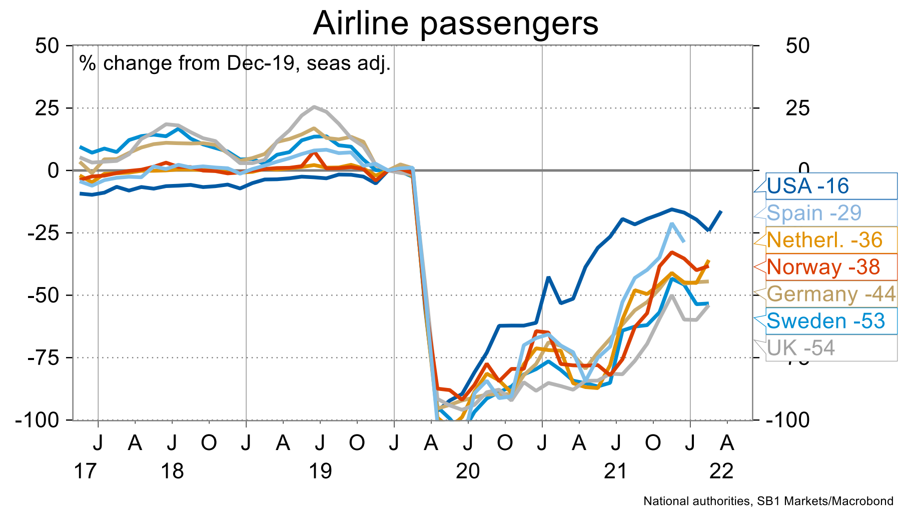


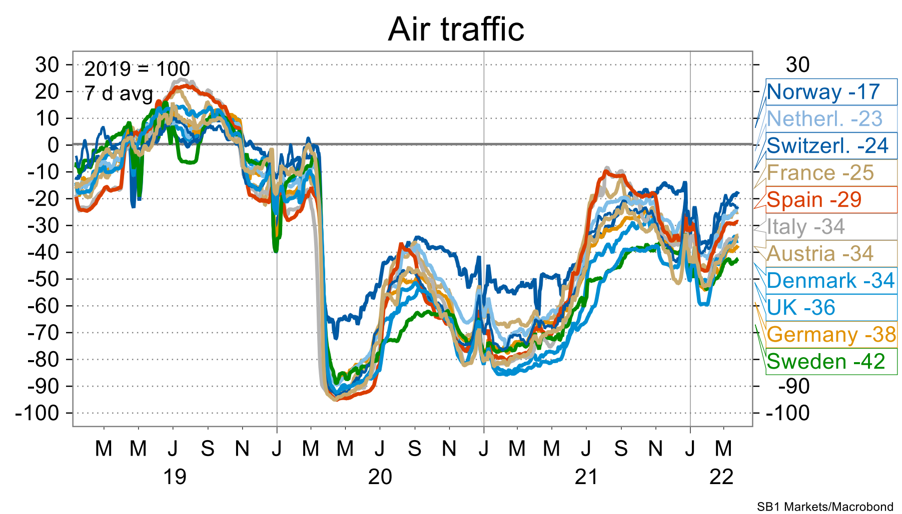
- **Global retail sales** recovered the December loss in January
- **Global manufacturing production** has recovered since the autumn, and growth continued into Q1
- **Global foreign trade** may have contracted in February (Feb, March and April estimates from Kiel Institute)

Global airline traffic is stalling? At least it is flying lower

Traffic has slowed marginally past two weeks, especially vs the normal growth at this time of the year

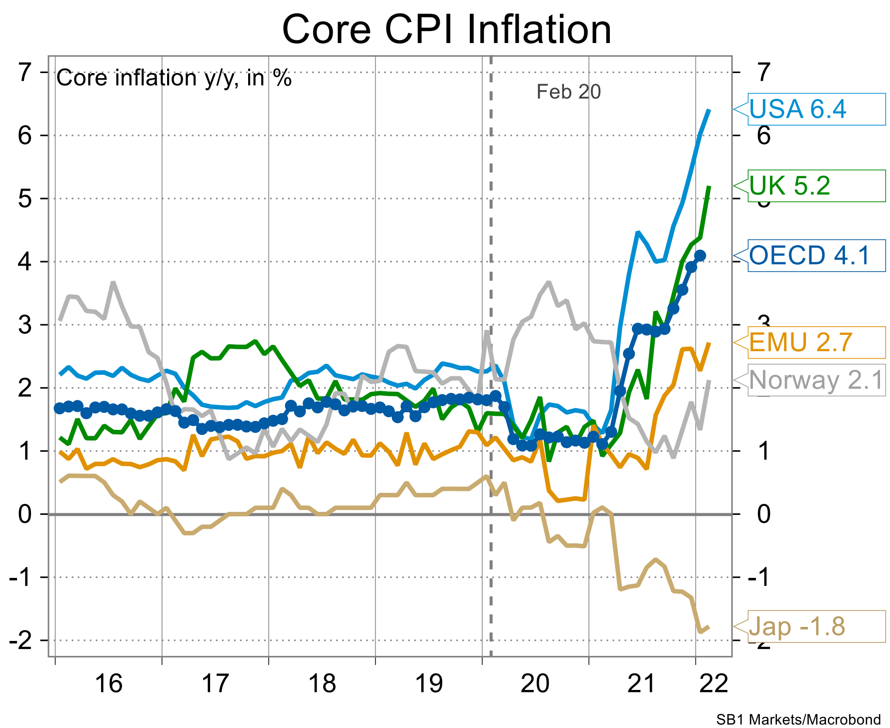


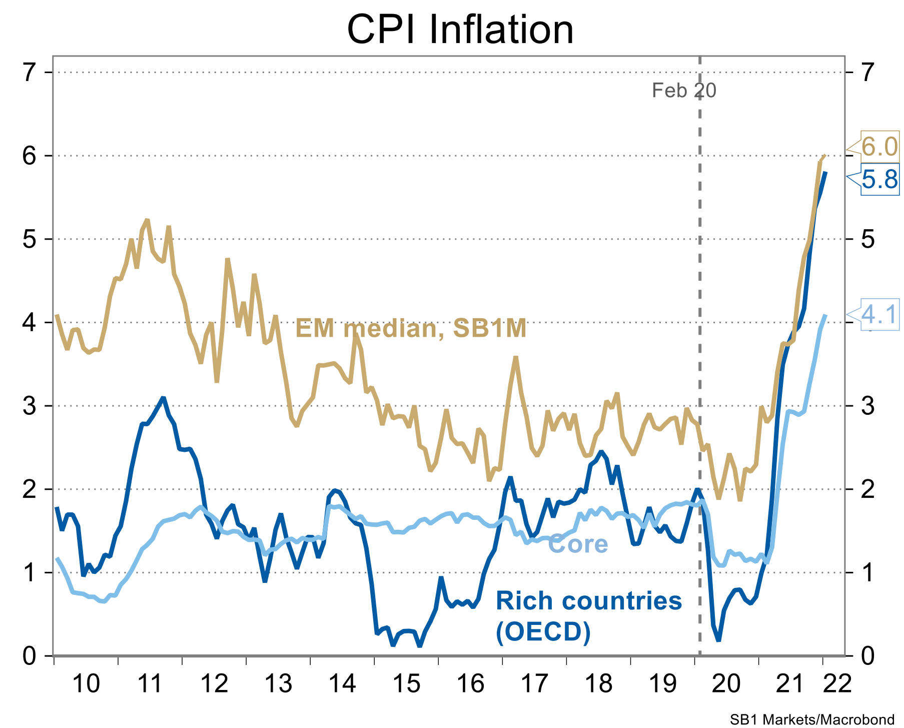




Inflation still rapidly on the way up

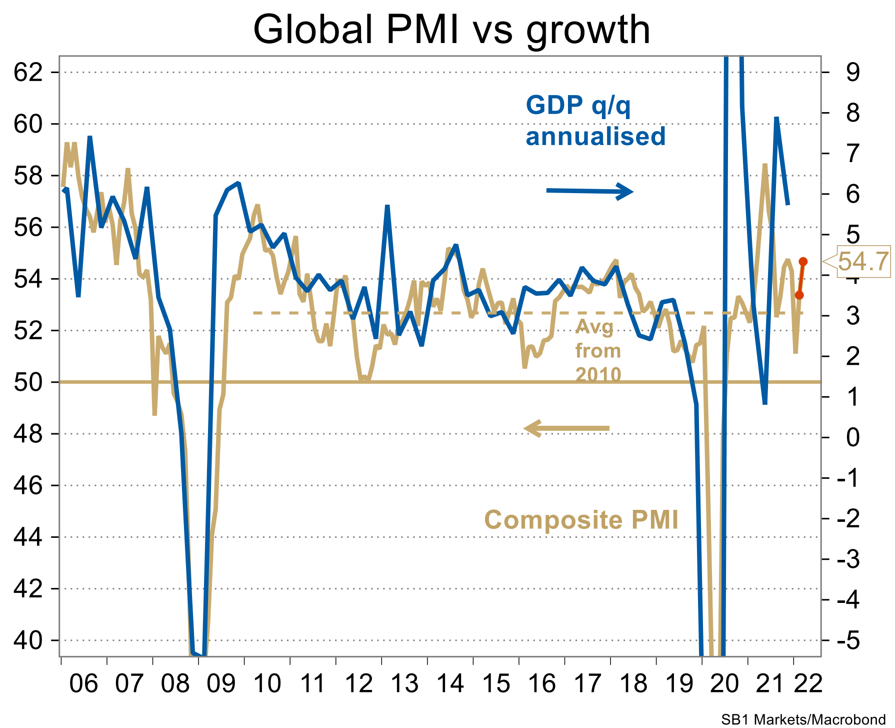
Energy prices the main culprit, but core inflation has turned up most places

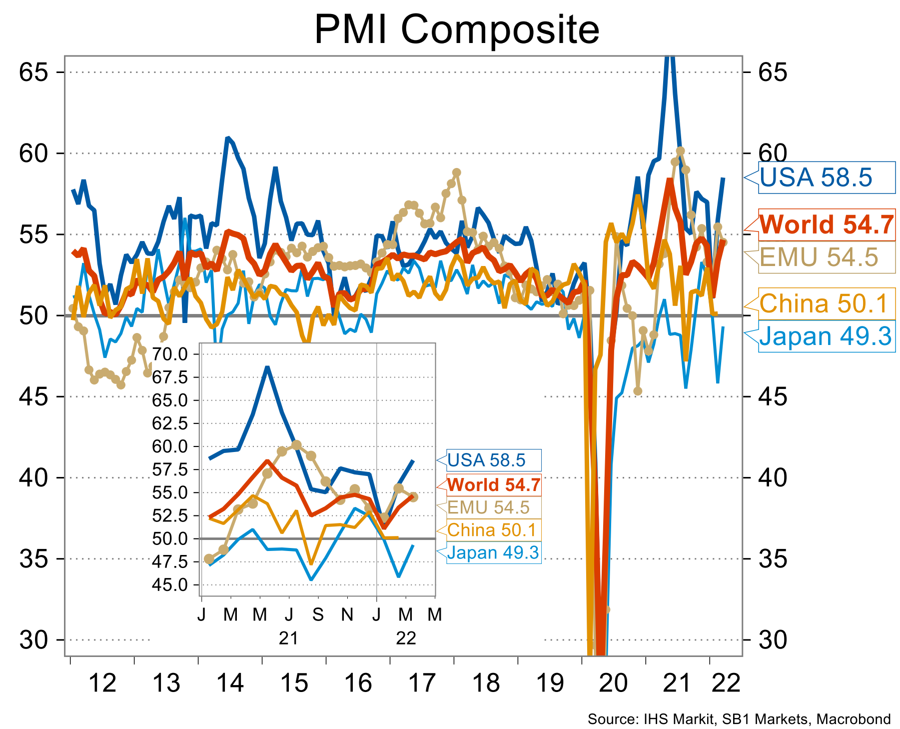




Wait-and-see PMIs up in March, EMU slightly down, US & Japan more up

We <u>estimate</u> +1.3p m/m to 54.7 →, 4%+ global GPD growth. Too early do judge the impact of the war



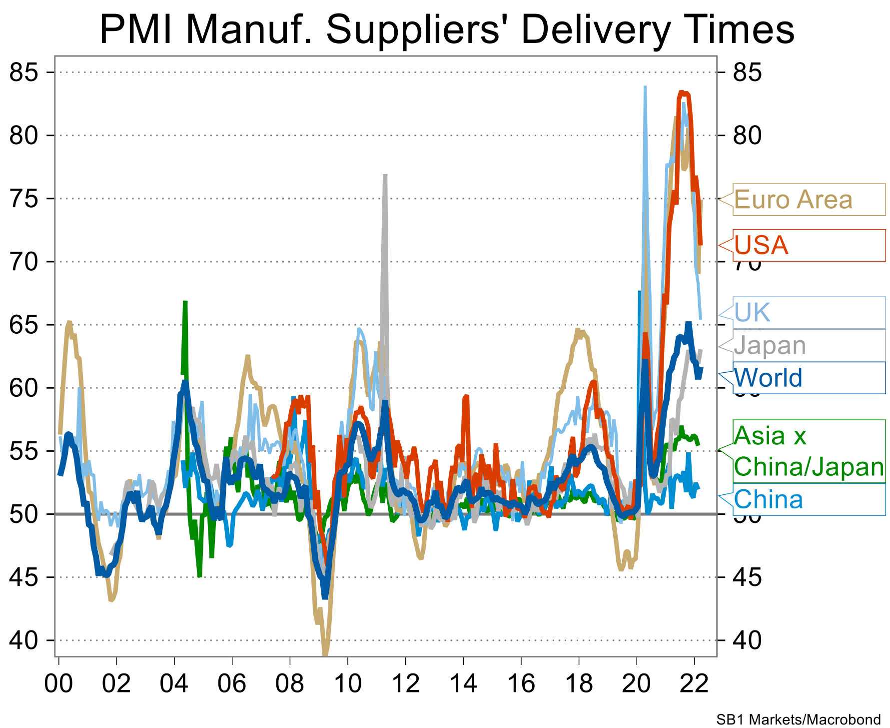


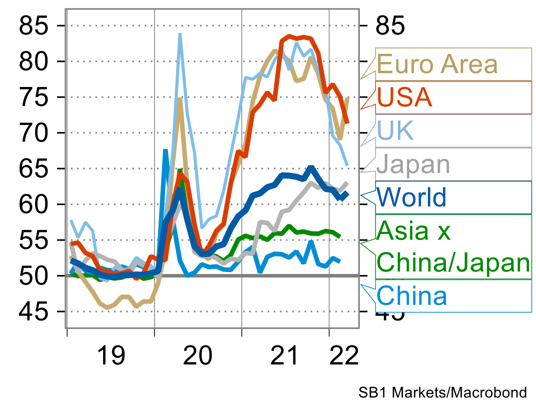
- **The PMIs** are not expectation surveys but a growth tracker where companies report whether orders, production, employment is up or down vs the previous month. While expectations surveys in Europe that so far a published collapsed in March, the PMIs kept up quite well – signalling than companies so far have not seen a deterioration of business condition
  - » Still, delivery times and prices rose in the EMU, and not in the US
- The lift in the global composite PMI (our estimate) was well above expectations (the PMIs were better than expected in both the US, UK as well as in the Euro Area

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

Delivery times up in EMU, down in US. By accident or due to the war/sanctions?

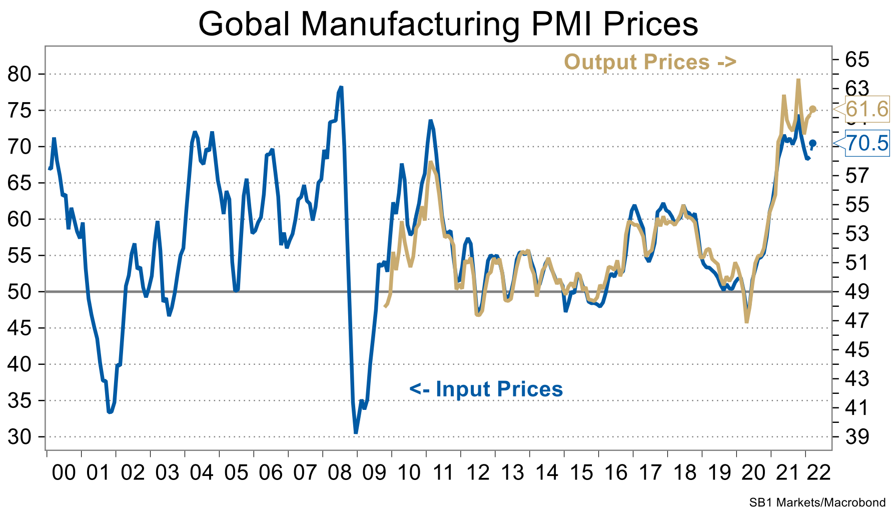
Global delivery times rose as well (our est) but the trend is still downwards

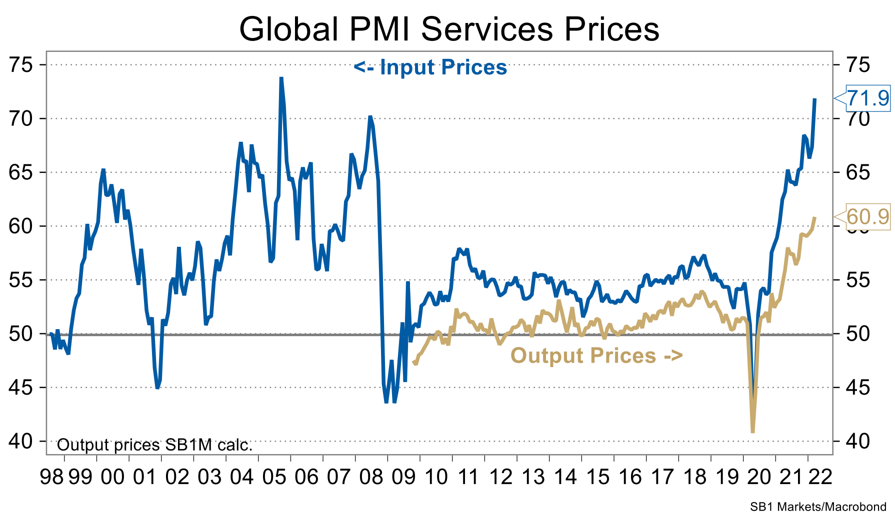




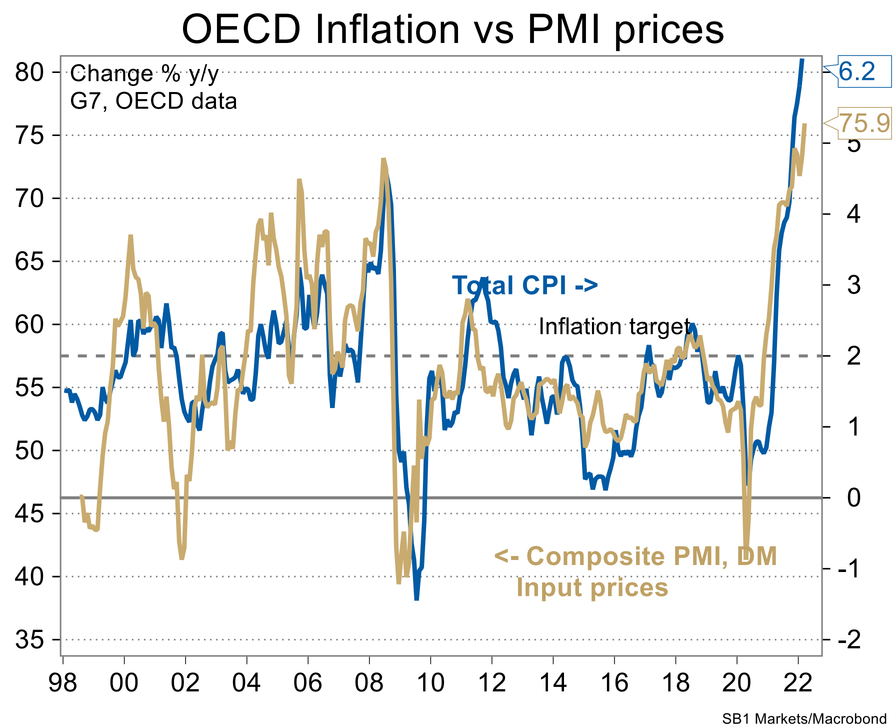
- **The global delivery times** PMI sub-index (changes in delivery times vs the previous month) has been inching down since the peak in October, including a likely further decline in February. The decline is broad among in The Western rich countries
- **The interpretation of this index is uncertain** – are companies really reporting changes in delivery times – which they are asked to do?
  - » This index as been above 50 most of the time (the past 20+ years), formally implying a continuous increase in delivery times. However, delivery times have surely not increased almost all the time – they have rather fallen! Companies may be reporting the level of delivery times. If so, delivery times are now contracting – while the index formally reports than delivery times are increasing at a marginally slower pace

Price indices up again, especially in services





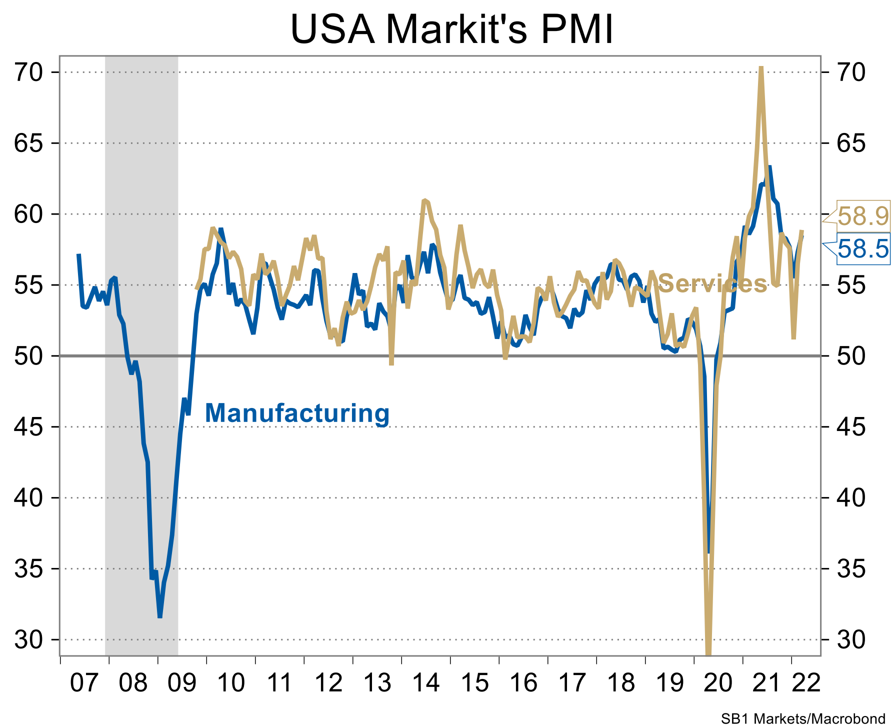
The last services PMI priced based on preliminary PMIs from EMU, Japan, UK, and the US

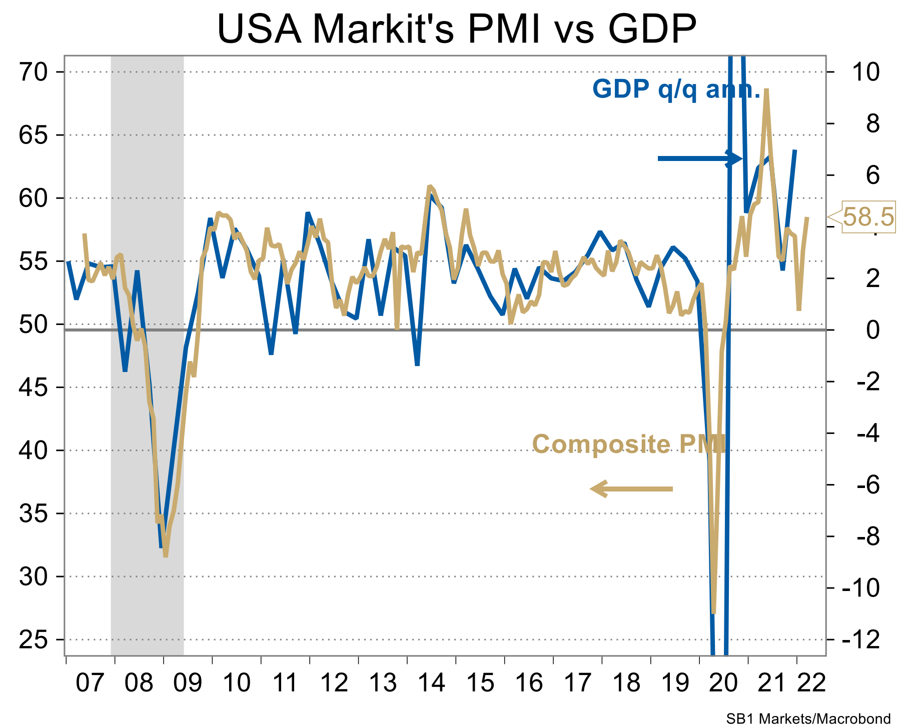


- In manufacturing, the price indices have peaked – at least until now, and prices rose faster again in March
- Prices have not yet eased in the service sector
- We are still much more concerned about wage inflation than the actual price inflation due to factors that most likely are transitory, like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

The PMIs further up in March

Both manuf. & services up, the composite +2.6 to 58.5, signalling 4% GDP growth

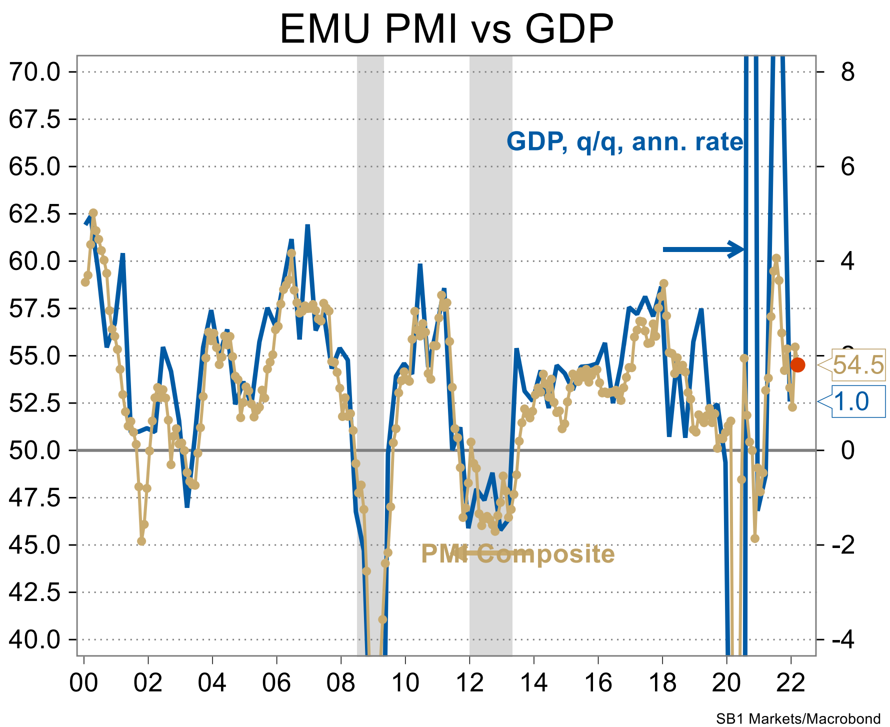


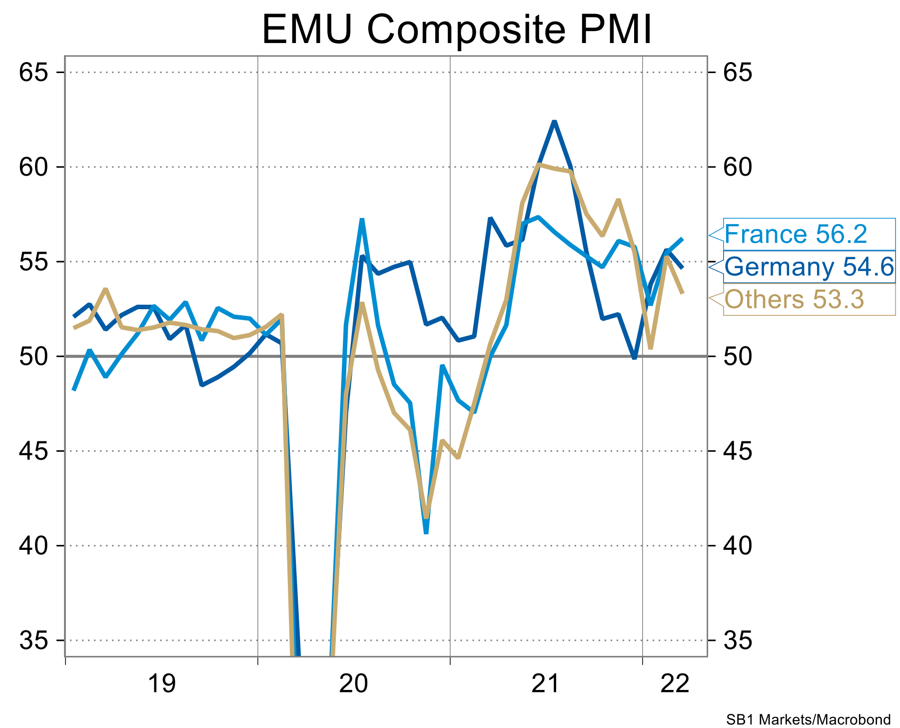


- **The composite PMI** fell sharply in January, due to a setback in services – but the index is now back on track
- **The price indices** was close to unch, at very high levels
- A positive sign: the **delivery times index** further – and it is trending down but remains at a high level. Orders were growing faster too
- Companies report that **employment** rose at a brisk pace in March too especially in the service sector

The composite PMI down 1 p to 54.5, no material impact from the war (yet)

The (nuclear powered) French PMI up, the (gas powered) German PMI down

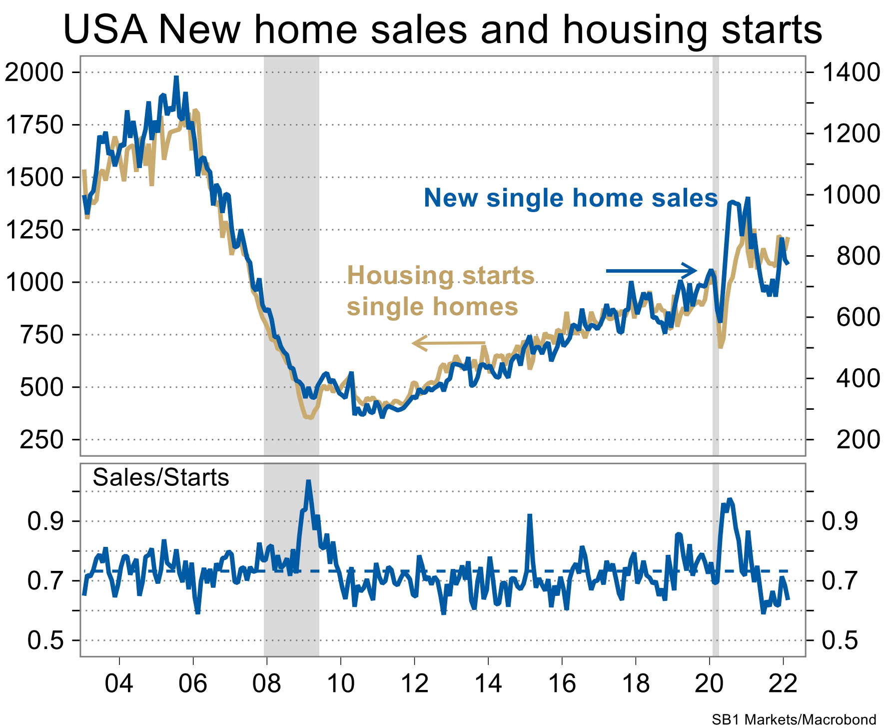


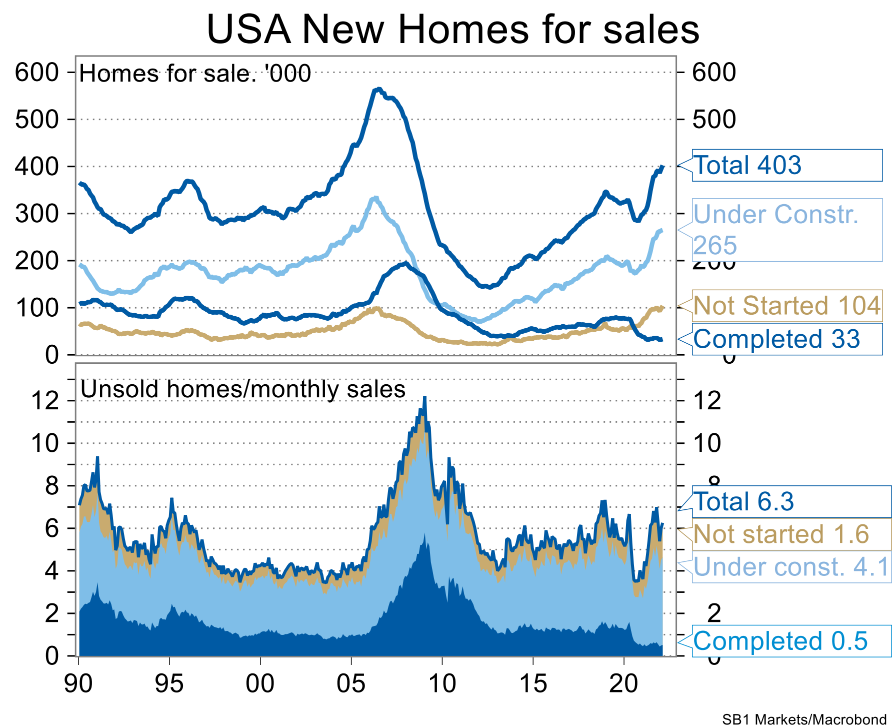


- **It is too early** to expect companies to report any large scale impacts of the war in Ukraine or sanctions. The respondents are asked about actual changes vs last month in new orders, production, employment etc. They are not asked about their expectations (except in an expectation part of the survey which is conducted in some countries)
- **The composite PMI** fell 0.7 p less than expected. The index signals a 2% GDP growth pace
- **The French** are less dependent in Russian gas, and are probably less worried about the energy bill

New home sales down in Feb, the total inventory of unsold homes on the way up

Prices have stagnated too. However, sales are still strong, and just few completed homes are for sale

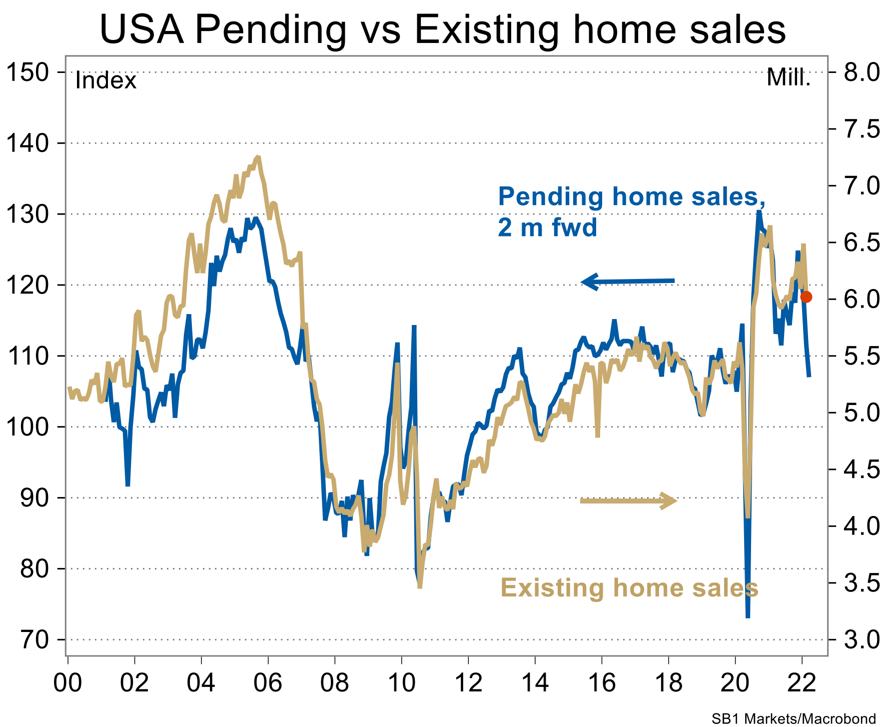


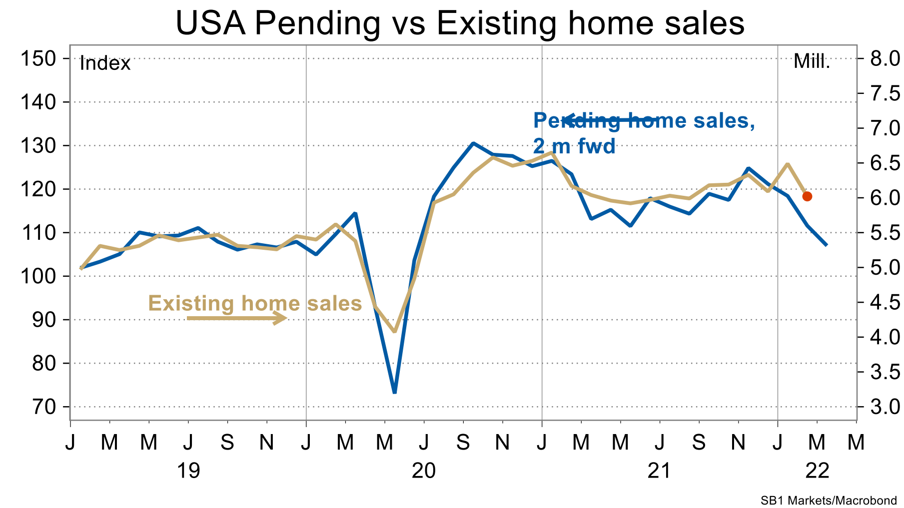


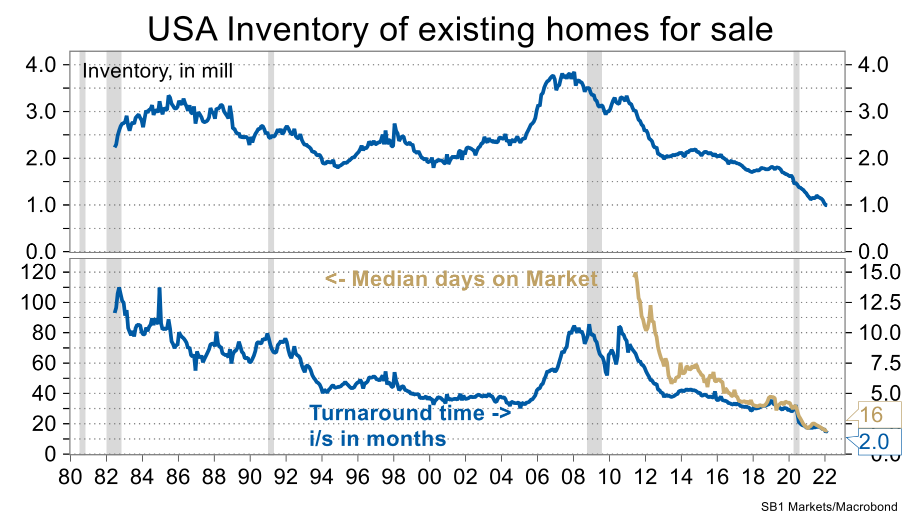
- **New single home sales** fell to 772'' (annualised rate) in Feb – from a slightly downward revised 788' in Nov, expected up to 810'. These monthly figures are often revised substantially and the last observation is close to useless
- **The big picture:** Following a 30% decline from January to June, sales were stable through H2 last year, at approx. the same level as before the pandemic – until the hike in Dec. Sales have been somewhat lower than normal vs. new single home starts (in avg. sales are 70%+ below starts, as may homes are built by homeowners themselves)
- **The inventory of unsold homes** has increased by 42% since Oct 2020, and the level is the highest since 2008. The inventory equals 6.3 months of sales, a bit higher than 'normal' – and up from the record low level at 3.5 months in Sept 2020
  - The increase in the inventory is not due to large increase in completed house for sale (the most 'effective' supply), and this inventory just equals 15 days of sale (1/3 of a normal level). However, the no. of projects not yet started (but for sale) has doubled, to the highest number ever, and the no. of new homes at the market but still under construction has climbed rapidly, to the highest level since 2007. So, there are lot of homes in the pipeline, and clearly a confirmation that the supply side is responding to the steep increase in demand. At one stage, combined with higher mortgage rates, that could change the housing market outlook

Pending home sales further down in February, mortgages rates start to bite?

No. of agreed transactions is down 14% from November





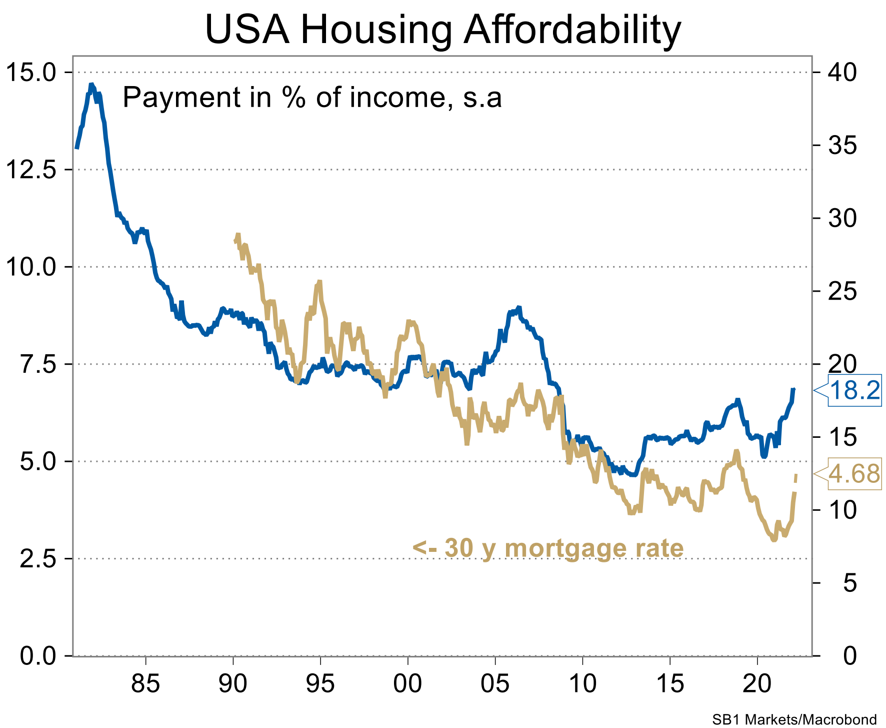


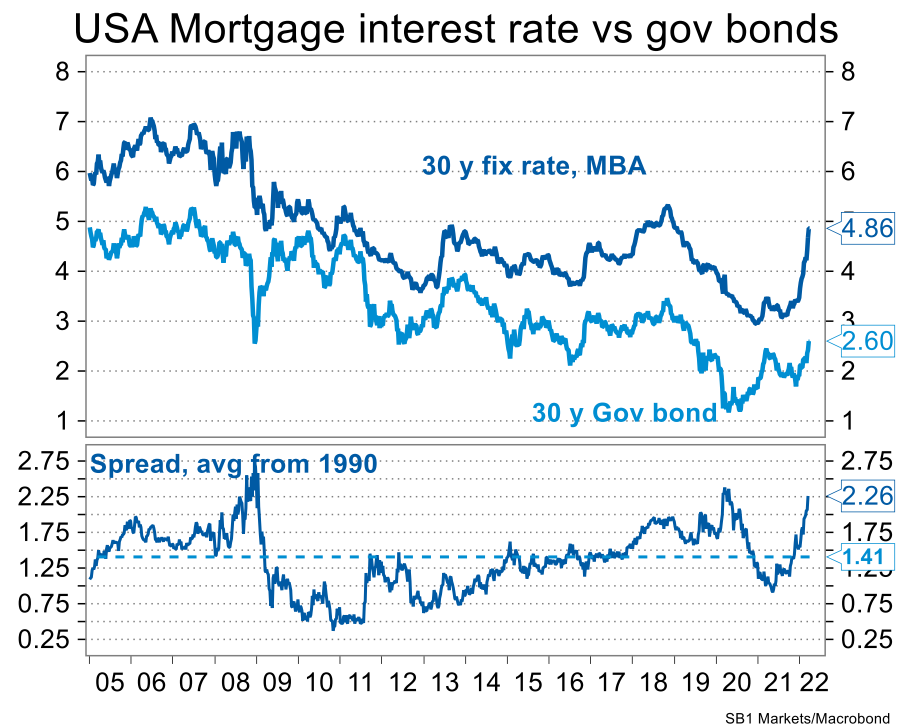
- The decline is significant – and important – as it signals that higher mortgage rates may slow down the housing market
- In December and January **existing home prices** rose faster than over the previous months, though based on deals signed in November and December (‘pending sales’). The inventory of unsold homes is at record low level, whatever measure we apply and sales may decline due to lack of available supply
- However, Since December, the 30 y fixed mortgage rate has climbed 130 bps to 4.8%, which of course may hamper demand!

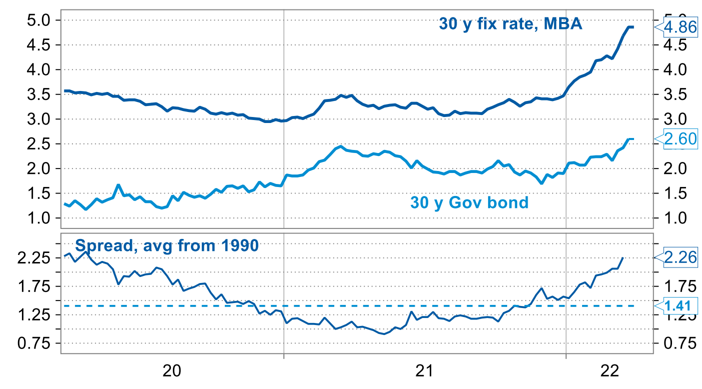
Pending home sales: Deals signed. Existing home sales: The actual transaction, typically 1 – 2 months after signing

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

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



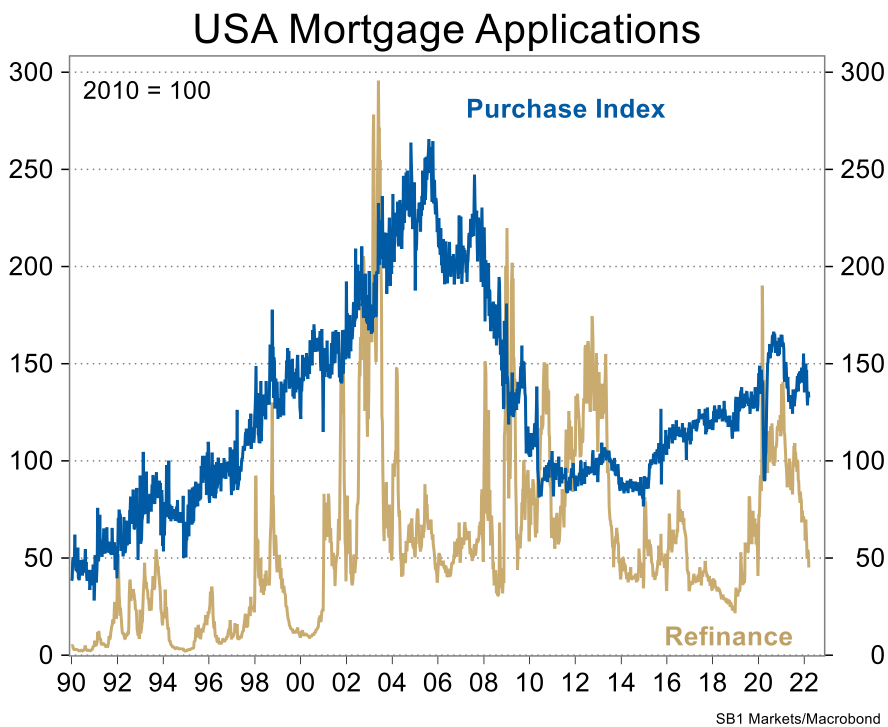


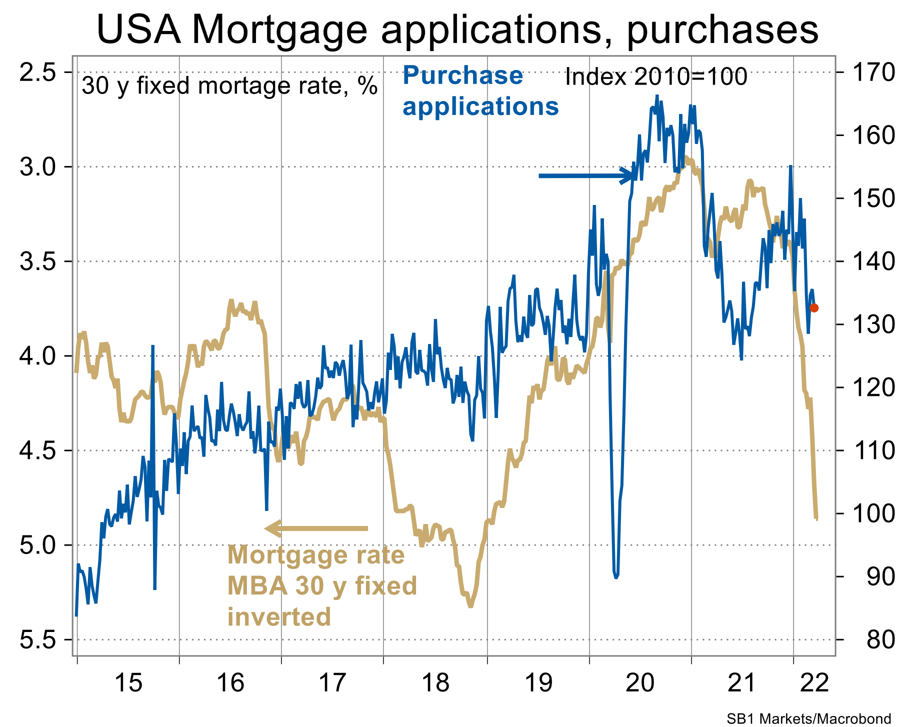


- **The 30 y fixed mortgage rate** has climbed to 4.8% (MBA, last week) from 3.0% last summer – and 3.5% by the end of last year
  - » The rate has increased MUCH more than the 30 y Gov bond rate. The spread has widened to 226 bps from 91 at the bottom last spring and it is far above the average at 140 bps
- 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 has not yielded by much

Demand for refinancing has fallen sharply but that is not a warning sign

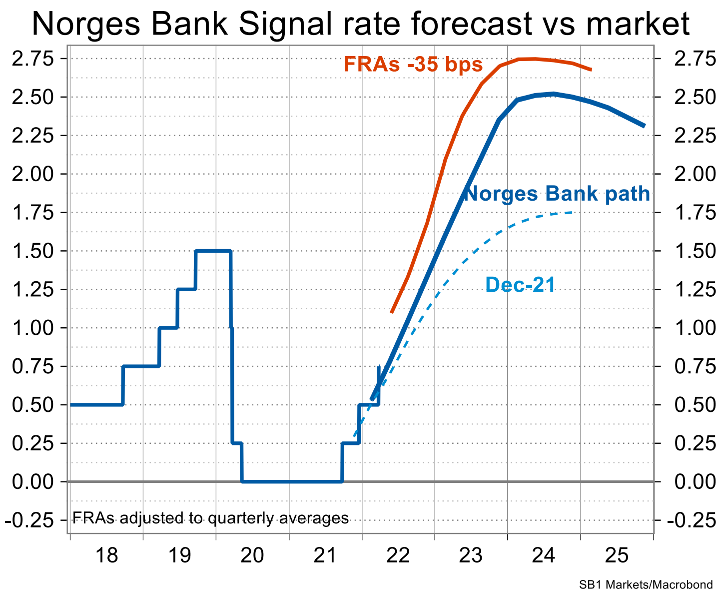




- The correlation between mortgage rates and existing home sales or prices are unstable

NoBa delivered the 3rd hike, and the path was revised up more than ever before

… and thereafter FRA-rates rose even more, by up to 25 bps – and is up to 50 bps above the new path



Interest rate paths

	NoBa Path 4-21	**NoBA Path 1-22**	**Change**	Fair FRA *) @IMM, NB	FRA** pre-meet	FRA** now	NoBa - FRA now
Q1 22	0.51	***0.53***	***0.02***	1.24		**-**	
Q2 22	0.70	***0.78***	***0.08***	1.46	1.63	**1.63**	-0.17
Q3 22	0.92	***1.05***	***0.13***	1.68	1.89	**1.97**	-0.29
Q4 22	1.11	***1.32***	***0.21***	1.90	2.25	**2.38**	-0.48
Q1 23	1.28	***1.59***	***0.31***	2.16	2.53	**2.70**	-0.54
Q2 23	1.42	***1.85***	***0.43***	2.41	2.71	**2.92**	-0.51
Q3 23	1.53	***2.10***	***0.57***	2.66	2.81	**3.04**	-0.38
Q4 23	1.62	***2.35***	***0.73***	2.81	2.85	**3.08**	-0.27
Q1 24	1.68	***2.48***	***0.80***	2.86	2.86	**3.10**	-0.24
Q2 24	1.72	***2.51***	***0.79***	2.87	2.85	**3.09**	-0.22
Q3 24	1.74	***2.52***	***0.78***	2.85	2.83	**3.07**	-0.22
Q4 24	1.75	***2.50***	***0.75***	2.82	2.79	**3.03**	-0.20
Q1 25		***2.47***		2.79	2.79	**3.02**	-0.23
Q2 25		***2.43***		2.73			
Q3 25		***2.37***		2.32			
Q4 25		***2.31***		2.26			

*) *Assuming the NIBOR spread gradually down to 35 from Q1-23, vs 50 bps in Q2*
**) Q4 FRAs adjusted for liquidity prem

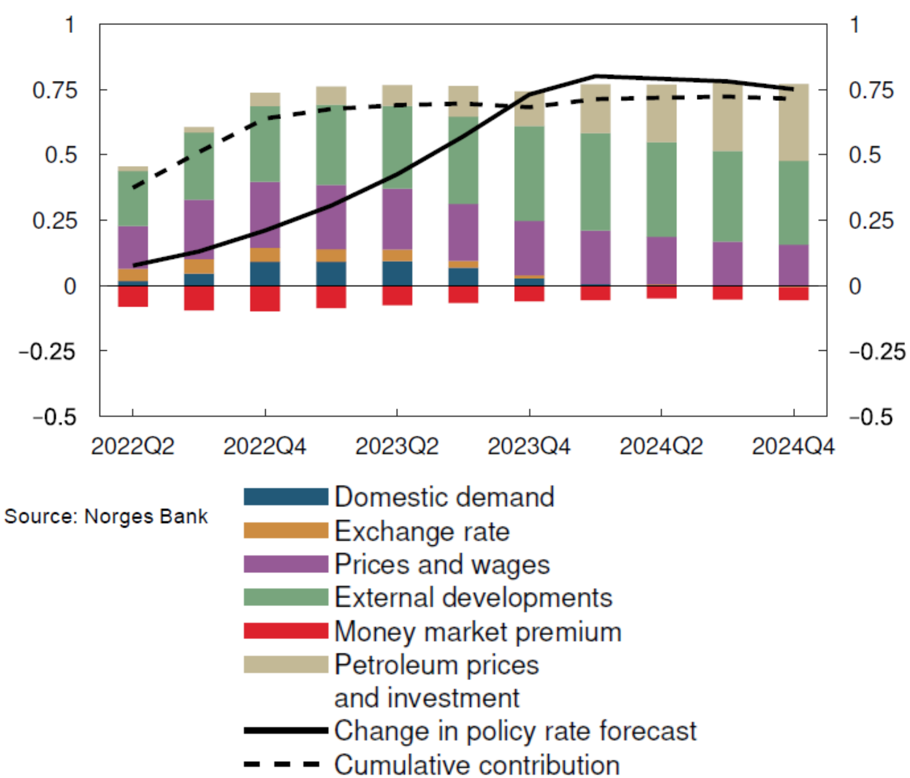
- **The signal (deposit)** was hiked by 25 bps, as expected
- **The policy rate path** was revised by up to 80 bps, an unprecedented quarterly change. The peak was lifted to 2.5% from 1.75% in the Dec MPR. We assumed a 50-bps lift, and a peak at 2.25%. Consensus was probably for something less than our f'cast
  - » However, our sum of the part analysis, based on expected changes in NoBa's forecasts but before deduction for 'adjustment and risk' signalled a 90 bps increase in the interest rate path
- The change in the interest rate path was the largest ever, by far. Higher interest rates abroad, the oil price, higher capacity utilisation, and significantly higher price- and wage inflation expectations contributed at the upside. Just an upward revision of the expected NIBOR spread contributed at the downside (see more next page).
- The Bank assumes core inflation will remain above the 2% target as long as the eye can see. At the same time, the output gap will remain positive too. NoBa defend its position by stating that high employment/low unemployment makes it worth 'breaking' the inflation target at the upside
- The new path implies 3 more hikes in 2022, with a 25% probability for a 4th hike, 4 hikes in 2023 (if 3 more in 2022), and the last hike to 2.25% in 2024. The next hike is supposed to be decided at the June meeting
  - » The new interest rate path implies that monetary policy will turn moderately restrictive from Q3 2023 as the signal rate will be lifted to above the assumed neutral rate at 1.75%
- **NoBa's new interest rate path was up to 35 bps below the FRA market (given a 35 bps NIBOR spread from Q4). Even so, FRAs rose sharply at Thursday and Friday, by 7 – 24 bps. The market discounts 5 more hikes in 2022 (vs. 3 in NoBa's main scenario). At the most, market expectations are 54 bps above NoBa's path (Q1-23), and they are signalling a 2.75% policy rate peak, 25 bps above NoBa's path**

Reasons for the rate path lift: Everything, except a wider NIBOR spread

The Banks data driven models argued for a 50-bps hike, and 4 more hikes in '22 (in sum '6' '22 hikes)

Chart 4.8 A number of factors pull up the rate path

Cumulative contribution. Percentage points



Source: Norges Bank

Our pre-meeting forecast was pretty close to the outcome until mid 2023 but thereafter NoBa was slightly more aggressive!

Upside contributions:

- Foreign rate expectations (-lower growth expectations, war & sanctions)
- Wage and cost inflation was revised sharply
- Domestic Mainland demand
- Petroleum prices, investments
- Even the NOK, even if the NOK has strengthened (but less than suggested by petroleum prices

Downside contributions:

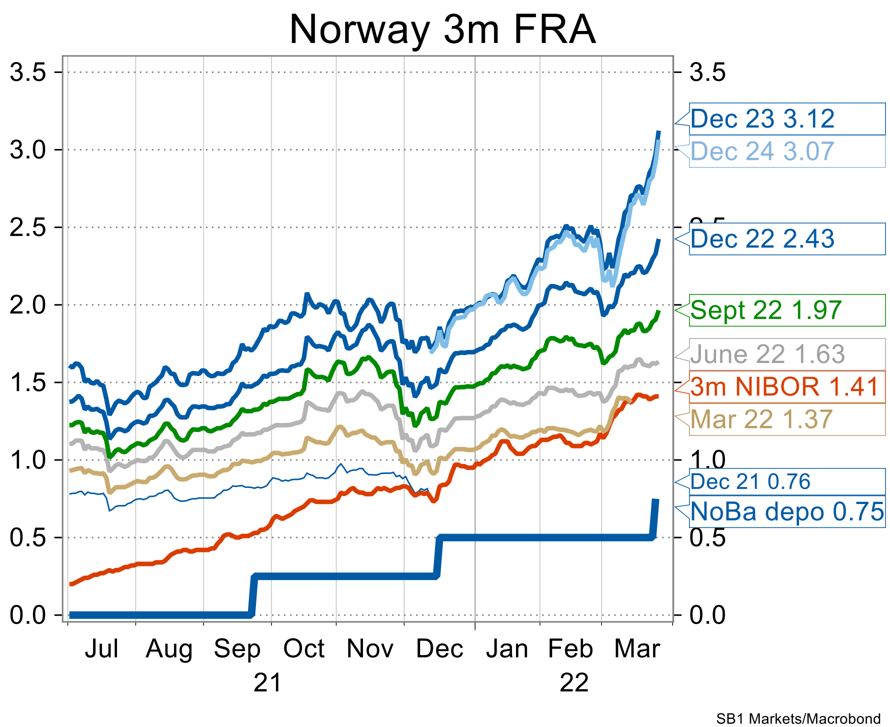
- Just a higher spread between NIBOR rates and the policy rate

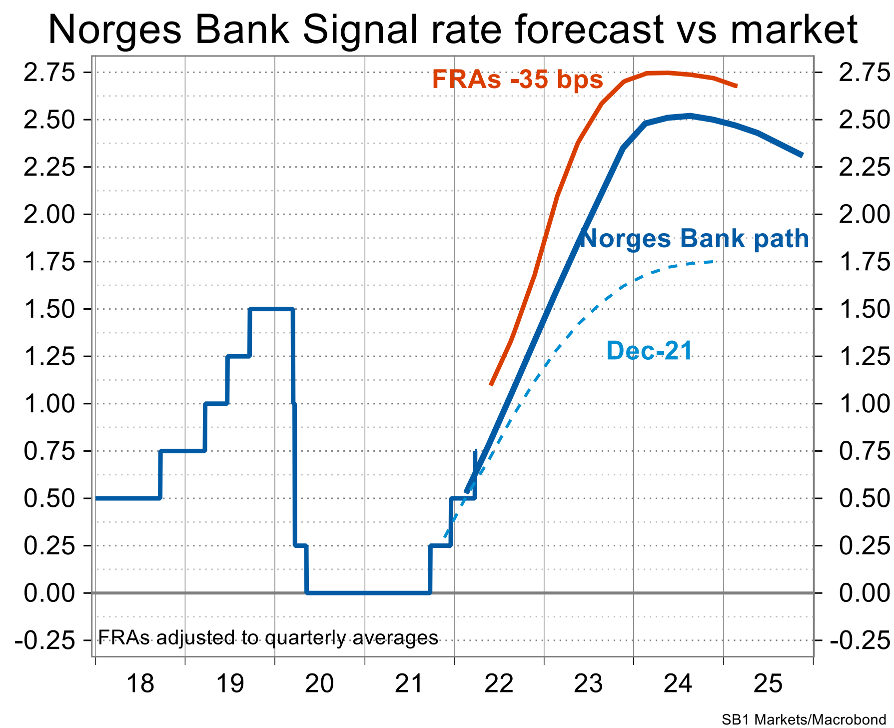
The board's (unprecedented) adjustment

- The data driven model suggested a 50-bps hike at this junction, and a lift in the interest path by 64 bps in Q4-22. The MPC decided to lift the path by 'just' 21 bps, a 43-bps discrepancy. We have never seen such a gap between 'data' and 'policy'
- The MPC still wanted to take a gradual approach as it is unsure how heavily indebted households will react to higher mortgage rates. Uncertainty regarding impacts of the war/sanctions also suggest more measured rate hikes, than the actual situation in the economy suggests

FRAs climbed after NoBa's message, to even further above the new path

It seem unreasonable to assume that markets discounts an even higher NIBOR spread

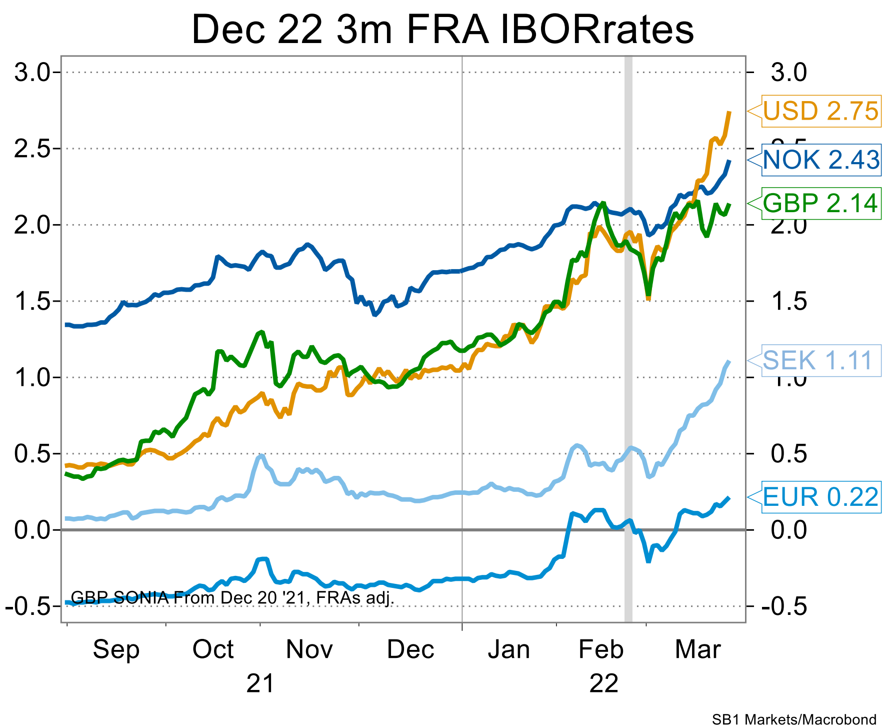


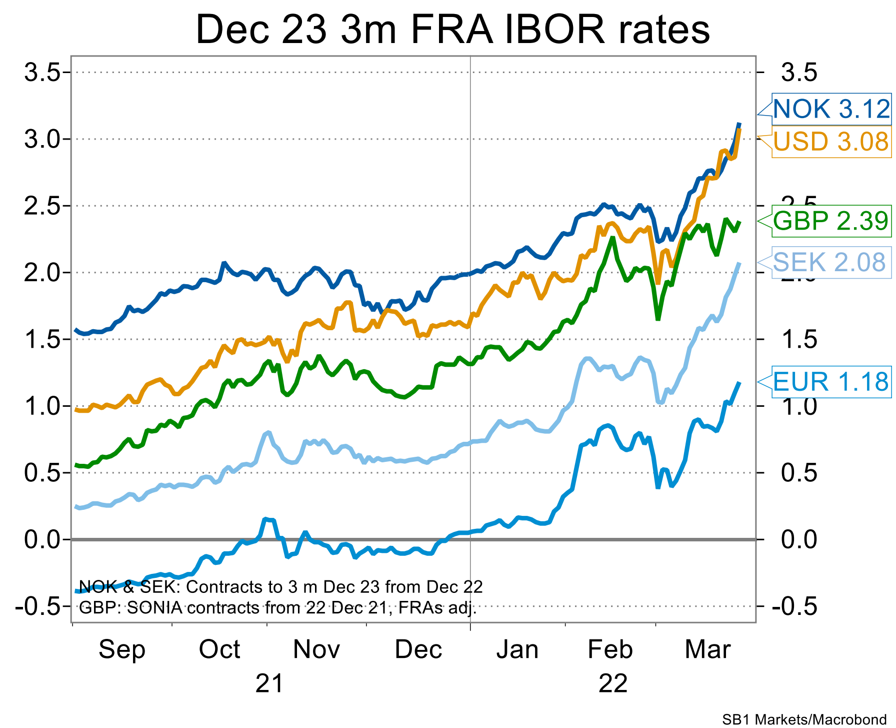


- … so these rate **expectations are 'the real thing'** – expectations of a more aggressive Norges Bank

Is just the sky the limit? Dec-22 FRAs up 10 – 40 bps, Dec-23 by 26 – 45 bps

US and Swedish rates moved the most

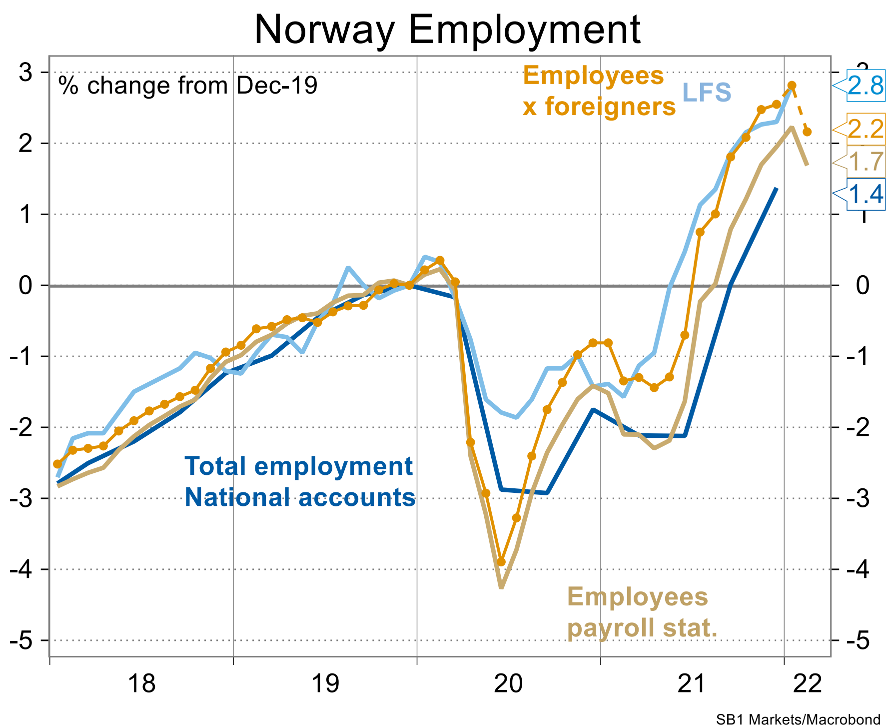




- We really look forward to the next Riksbank meeting! The Riksbank has until now insisted that the ZIRP will kept in place until H1-24. The market does not at all believe in that position. In fact, the market expects more than 10 hikes before that. We have never seen such a mis-match before between a central bank and the market before, at least not in a civilised country in recent times. Since the Riksbank's board cannot be ousted by the Government, the members should have taken the consequence themselves?

Payrolls cut by 0.5% in (mid) February, we expected a further growth

The no. of employees is still up 1.7% vs Feb-20. The LFS report further growth in total employment

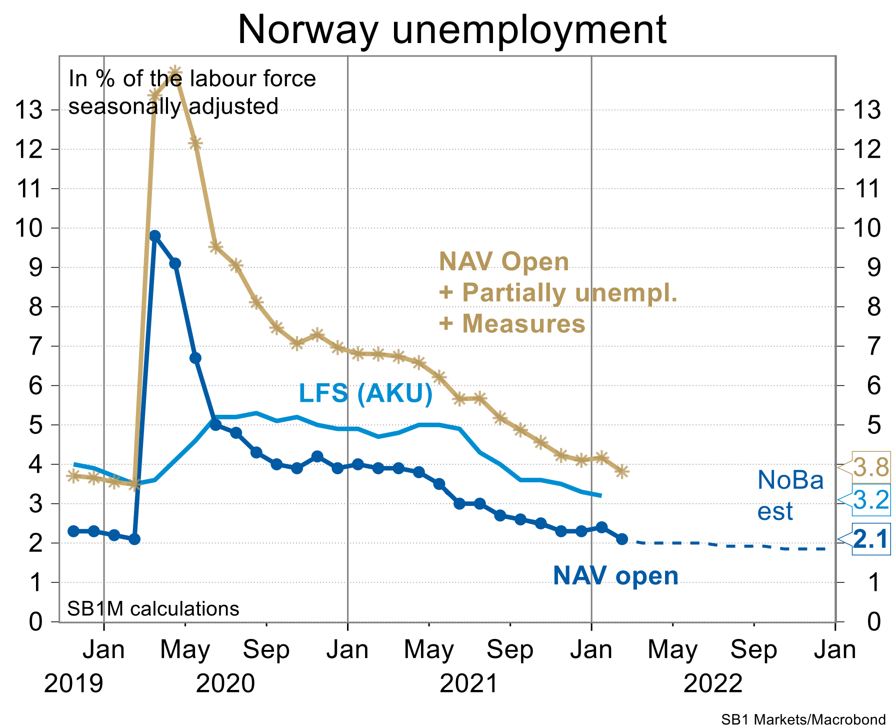


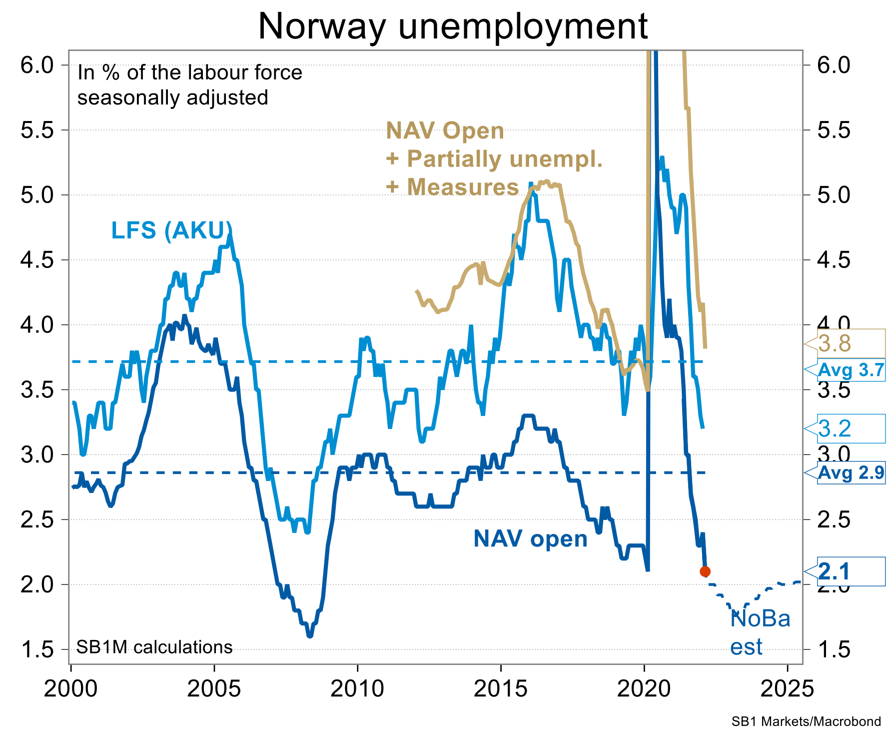
- The 14’ decrease in the **register-based no. of employees** to mid Feb from mid January was a surprise
- We expect employment growth to slow due to lack of available labour, not due to lack of demand

- **The LFS** (‘AKU’ survey) employment data (both employees and self-employed, with permanent residency in Norway) reported a 14’ (0.4%) growth in employment in Jan (avg Dec-Feb from avg Nov – Jan), and by a 2.6% pace over the past 3 months
  - » LFS employment is up 2.8% since before the pandemic, and both participation and employment rates are far above the pre-pandemic level – and the LFS unemployment rate has ‘collapsed’, now to 3.2%
- **National Accounts** reported a 1.4% growth in total employment in Q4 (5.5% annualised) – and the level is up 1.4% vs. Q4-19. These NA data includes foreigners on short-term stay

LFS unemployment down to 3.2% - to below the pre-pandemic level

Norges Bank revised its NAV unemployment forecast down last week, to 1.8% at the bottom

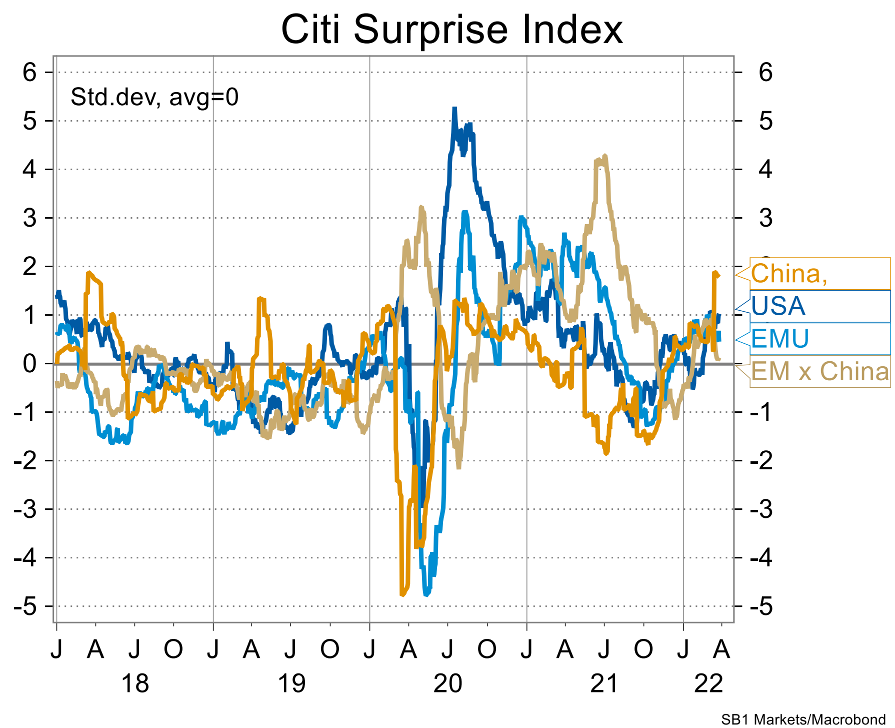


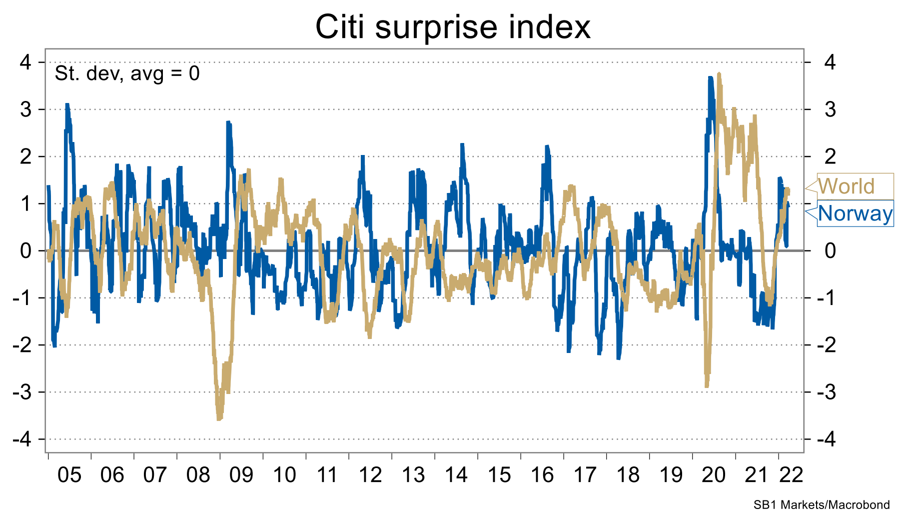


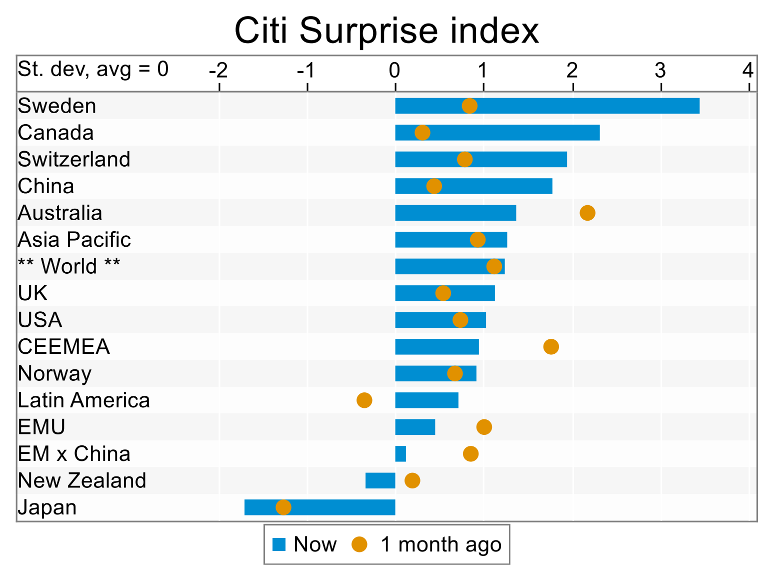
- However, given the speed of decline so far, 1.8% is not be that far away, check the chart to the left
- **The LFS (AKU) unemployment rate** fell 0.1 pp to 3.2% in Jan (Dec-Feb avg), from 3.3% a month earlier – expected unchanged (we expected 3.2%). The level is well below the 3.7% average

The world is surprising at the upside. At least so far…

China almost up to the top of the list on Jan/Feb data. Just Japan at the downside vs expectations







- **Norway** was surprising sharply on the downside through most of 2021, according to Citi. But in early December we crossed the zero line, and shot up in January – and we are still well above average

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

Highlights

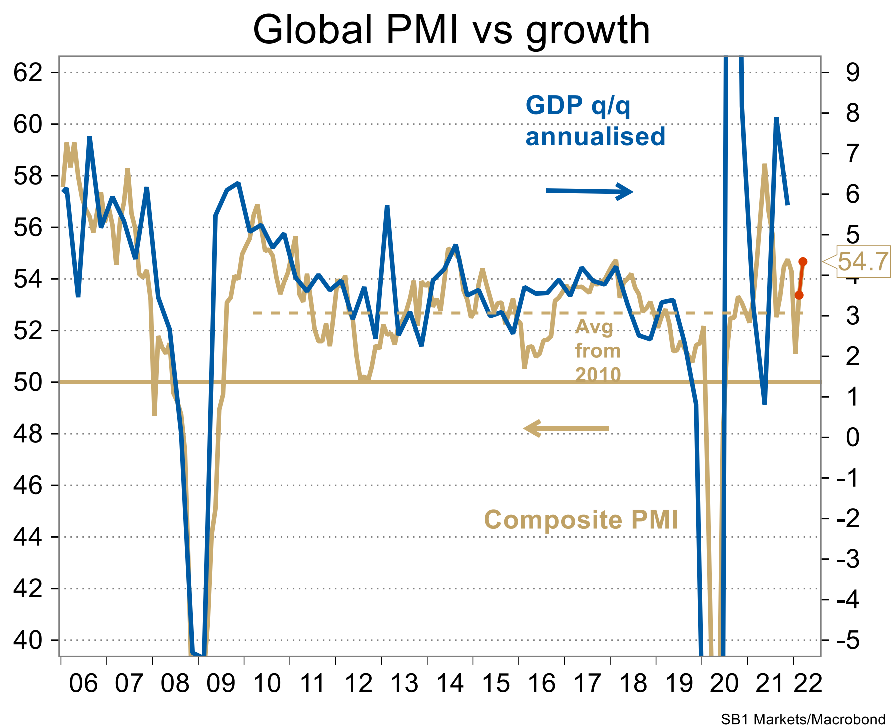
The world around us

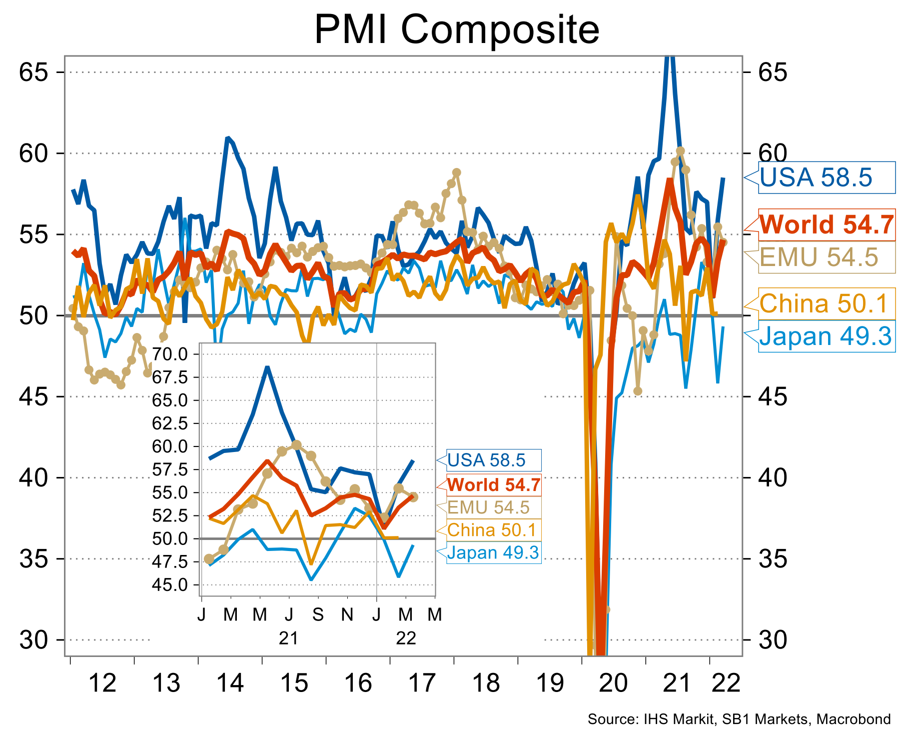
The Norwegian economy

Market charts & comments

Wait-and-see PMIs up in March, EMU slightly down, US & Japan more up

We estimate +1.3p m/m to 54.7 →, 4%+ global GPD growth. Too early do judge the impact of the war

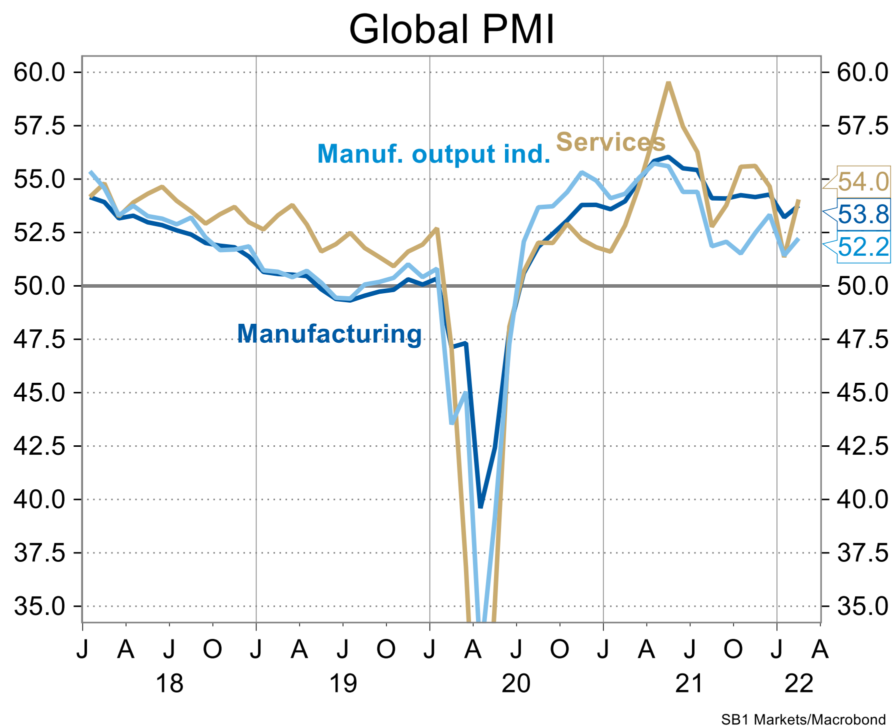




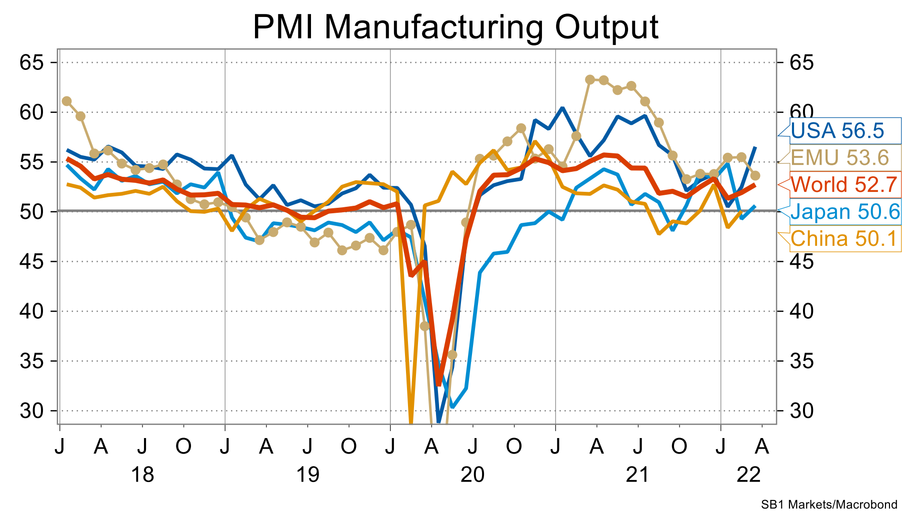
- **The PMIs** are not expectation surveys but a growth tracker where companies report whether orders, production, employment is up or down vs the previous month. While expectations surveys in Europe that so far a published collapsed in March, the PMIs kept up quite well – signalling than companies so far have not seen a deterioration of business condition
  - » Still, delivery times and prices rose in the EMU, and not in the US
- The lift in the global composite PMI (our estimate) was well above expectations (the PMIs were better than expected in both the US, UK as well as in the Euro Area

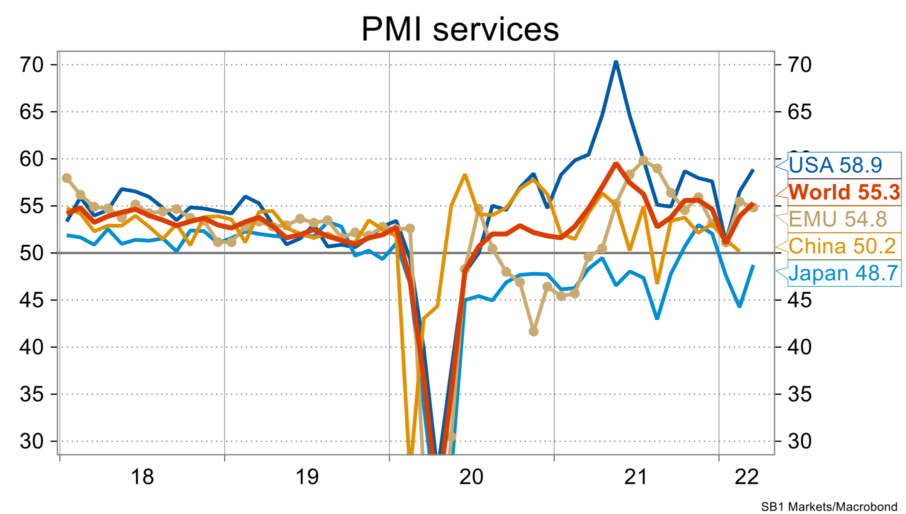
Our estimates are based on the preliminary PMIs from US, China, EMU, Japan UK, Australia. The estimates are uncertain, but usually by less than 0.5 p

Both manufacturing & services report higher growth



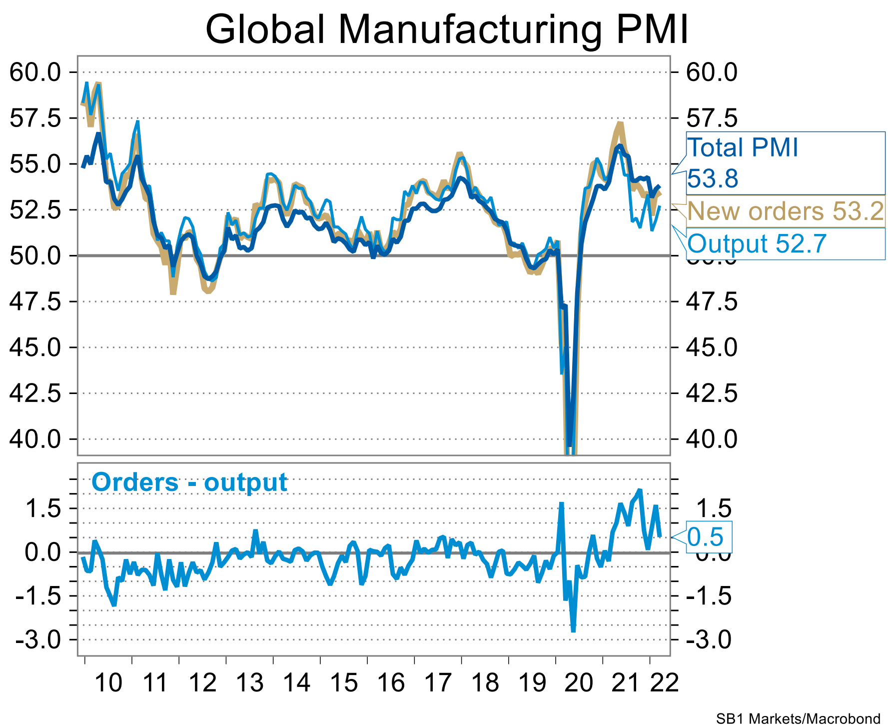
- Growth has very likely peaked, at least in the rich part of the world. Now, the war in Ukraine and economic war against Russia may create new challenges – even if 'geopolitics' normally are not important for the economic cycle

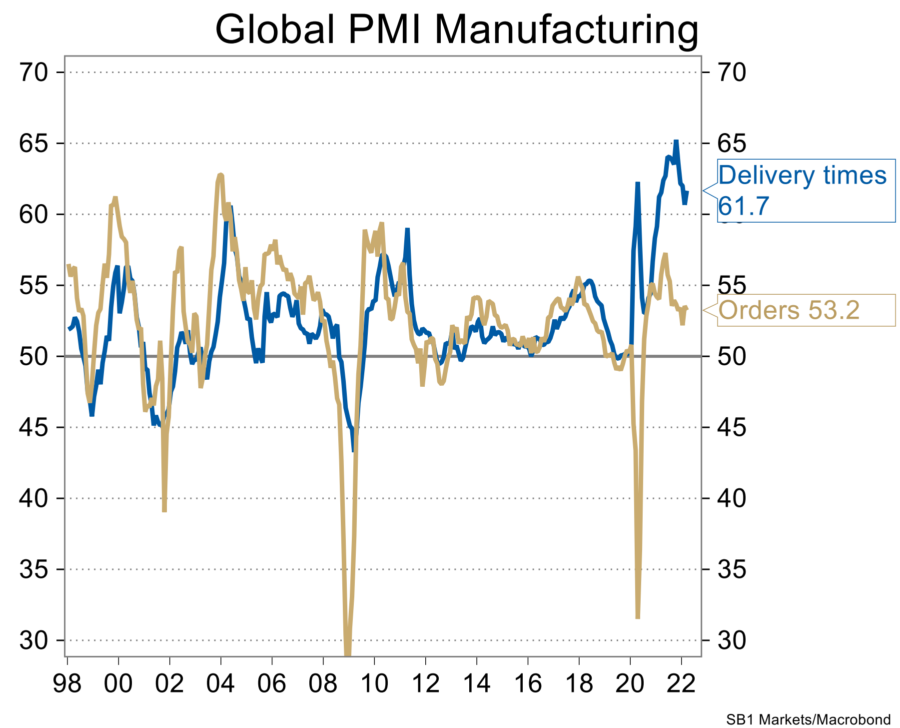




Growth in manufacturing at or above an average level

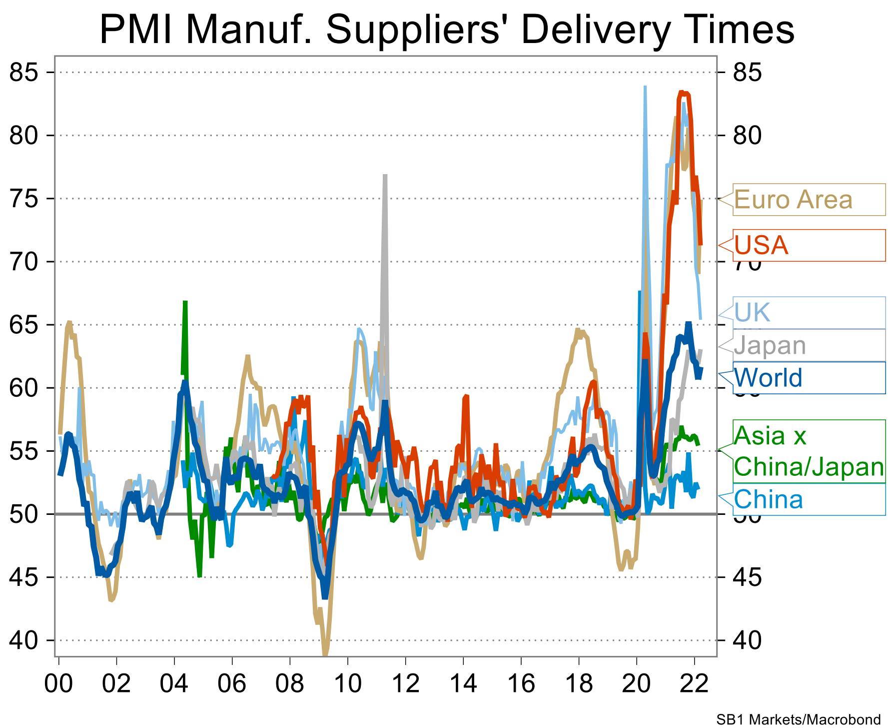
The delivery times index rose marginally in March

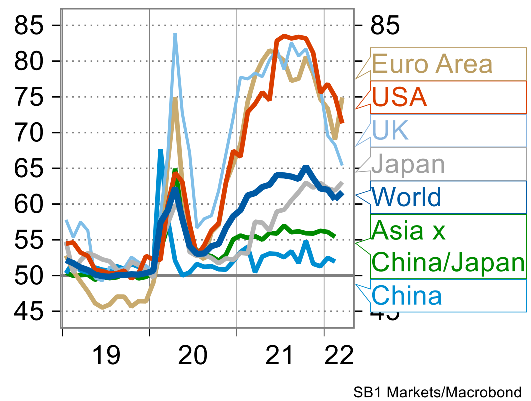




Delivery times up in EMU, down in US. By accident or due to the war/sanctions?

Global delivery times rose as well (our est) but the trend is still downwards



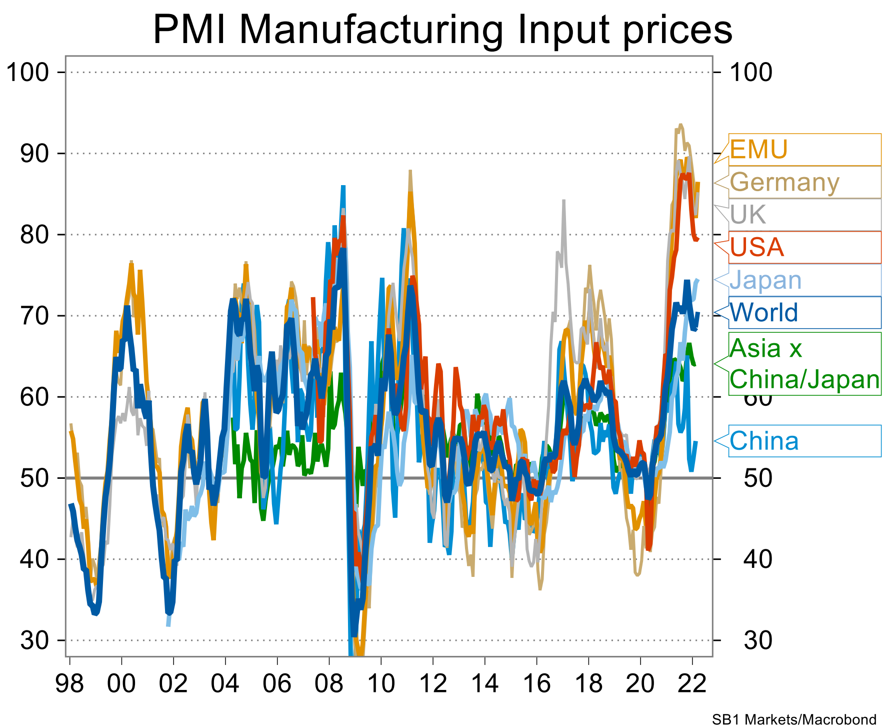


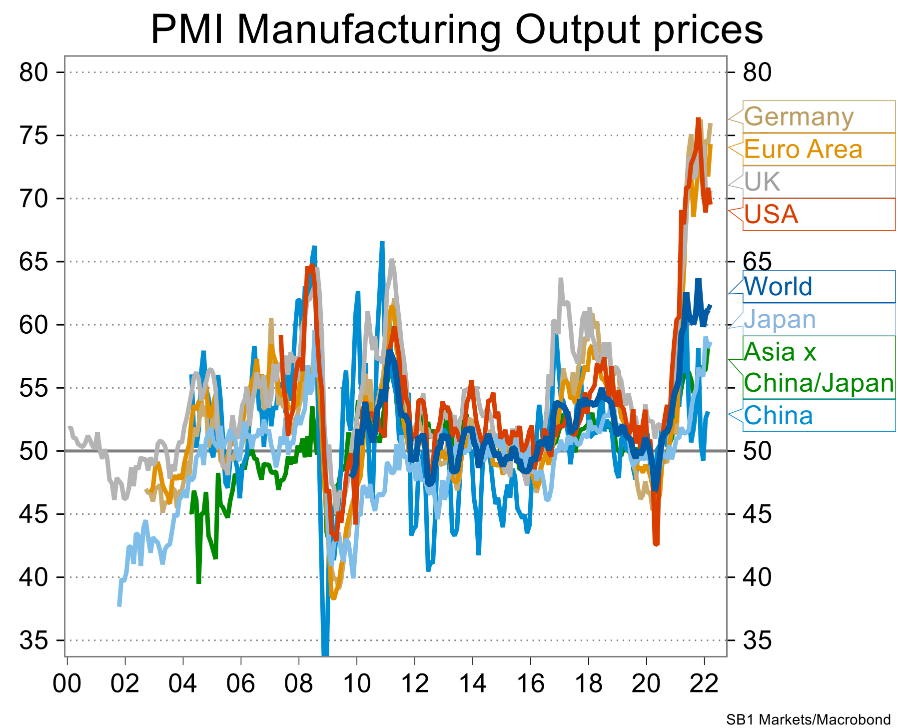
- **The global delivery times** PMI sub-index (changes in delivery times vs the previous month) has been inching down since the peak in October, including a likely further decline in February. The decline is broad among in The Western rich countries
- **The interpretation of this index is uncertain** – are companies really reporting changes in delivery times – which they are asked to do?
  - » This index as been above 50 most of the time (the past 20+ years), formally implying a continuous increase in delivery times. However, delivery times have surely not increased almost all the time – they have rather fallen! Companies may be reporting the level of delivery times. If so, delivery times are now contracting – while the index formally reports than delivery times are increasing at a marginally slower pace

SpareBank 1 MARKETS

EMU reported faster price increases (and longer delivery times), the US not

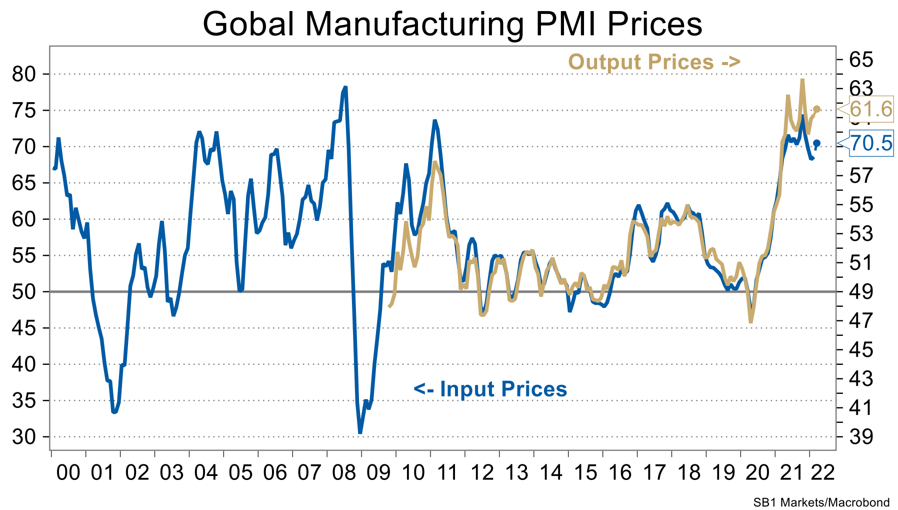
We may perhaps blame war/sanction related challenges – even in the first part of March

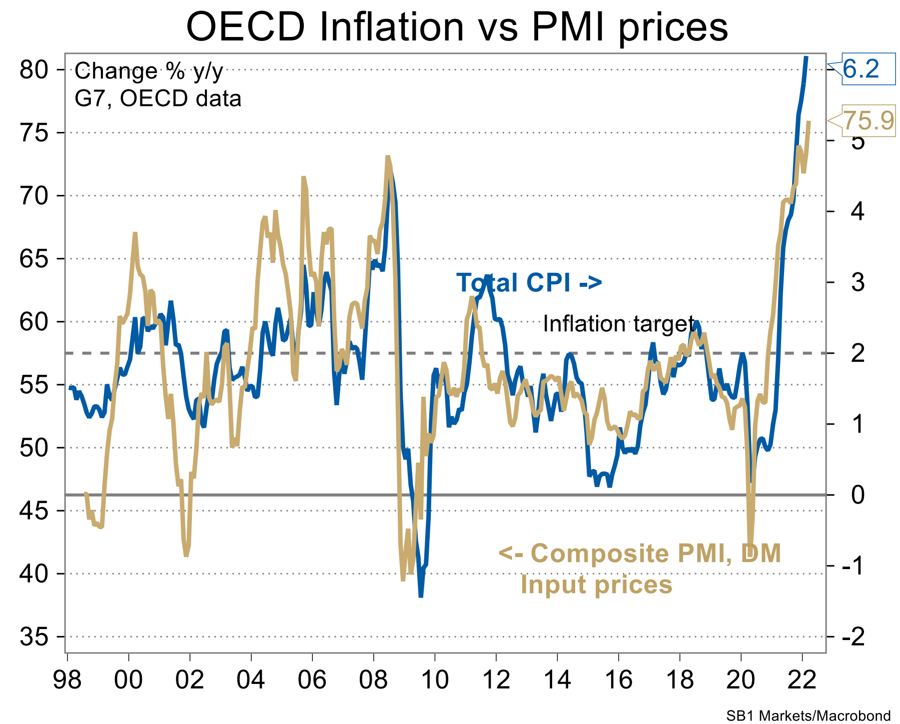


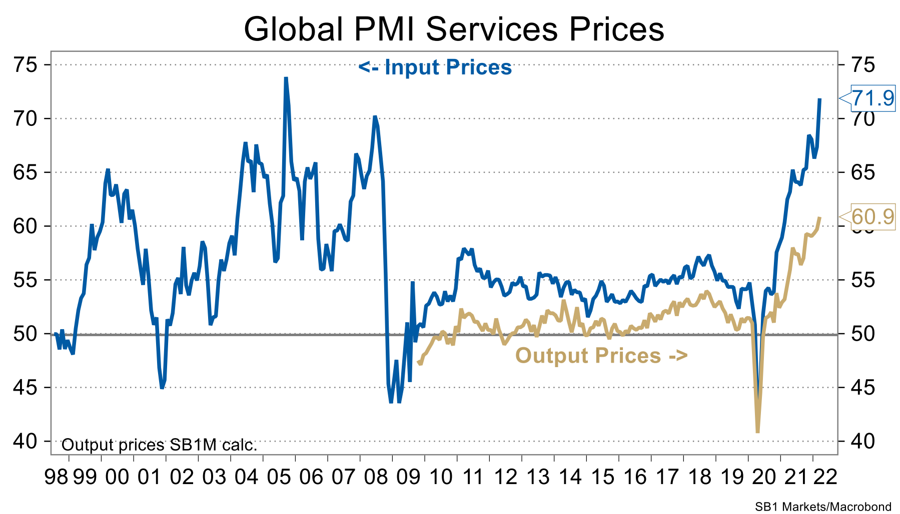


- Global input and output price indices rose in March – but both are somewhat below their peak levels

Price indices up again, especially in services





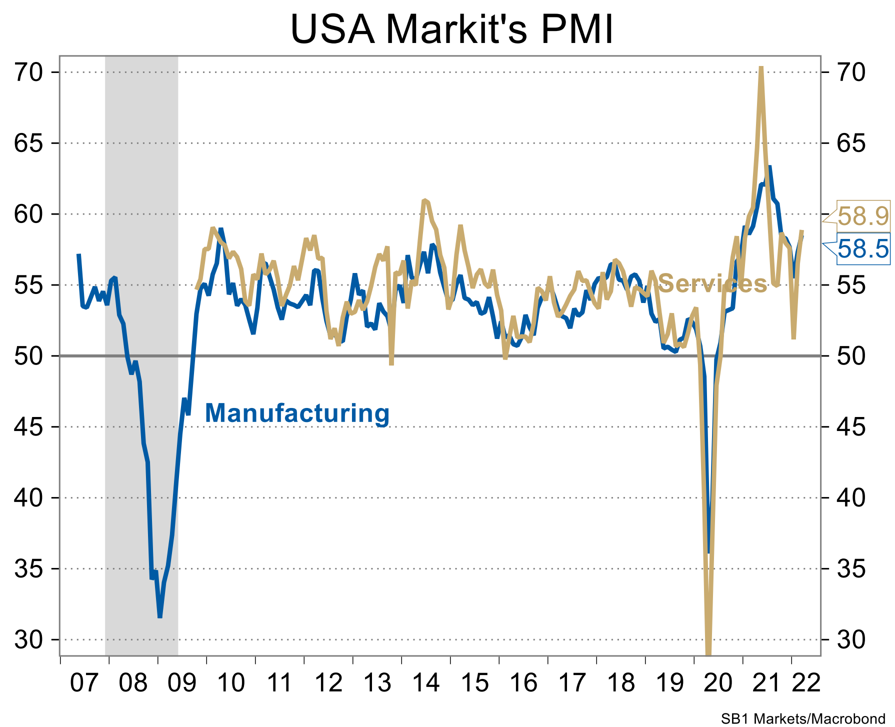


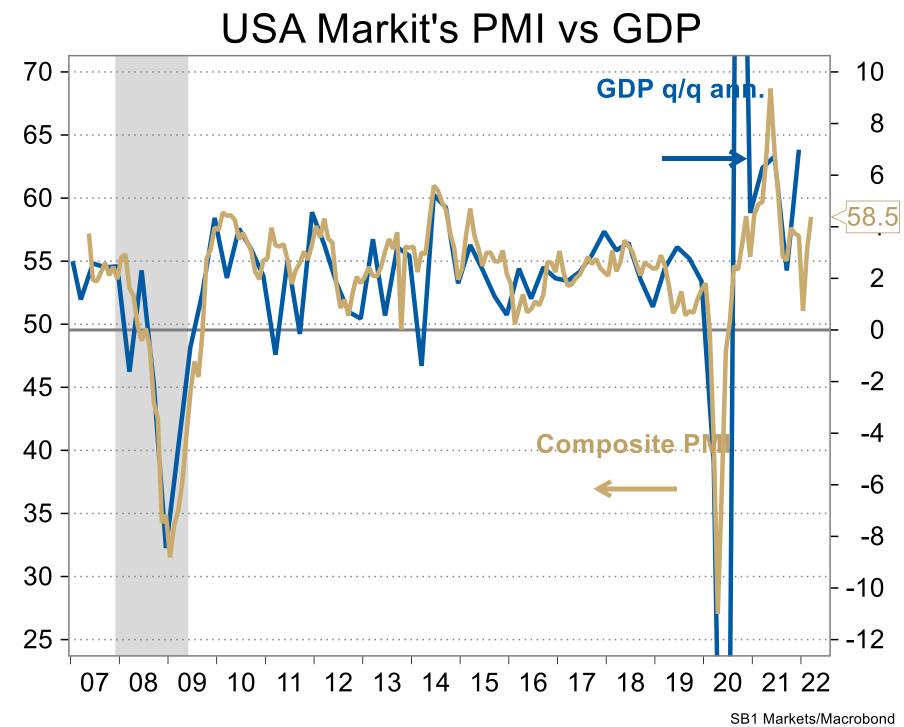
The last services PMI priced based on preliminary PMIs from EMU, Japan, UK, and the US

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

The PMIs further up in March

Both manuf. & services up, the composite +2.6 to 58.5, signalling 4% GDP growth

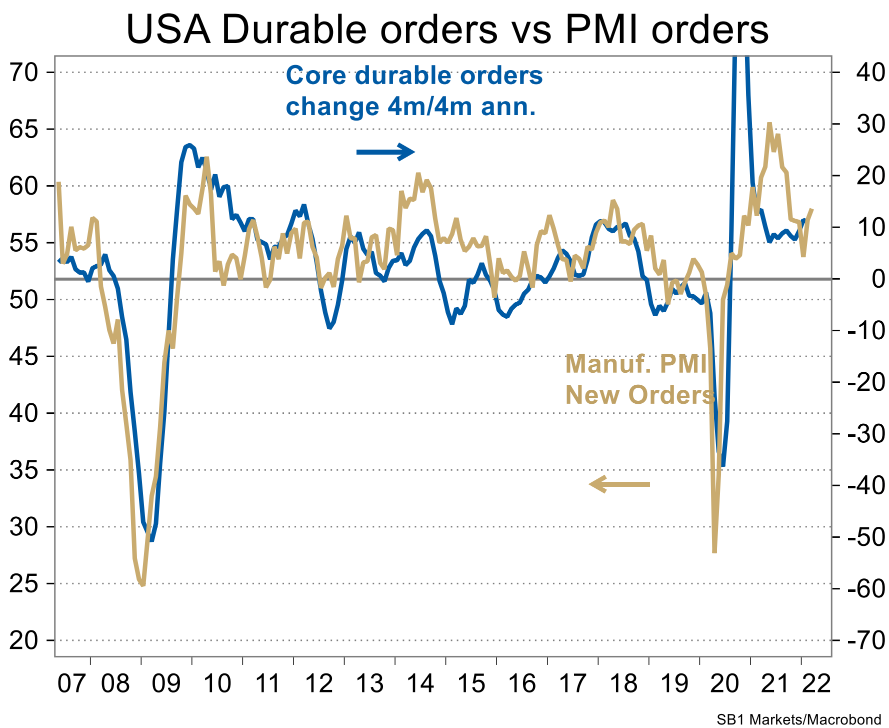


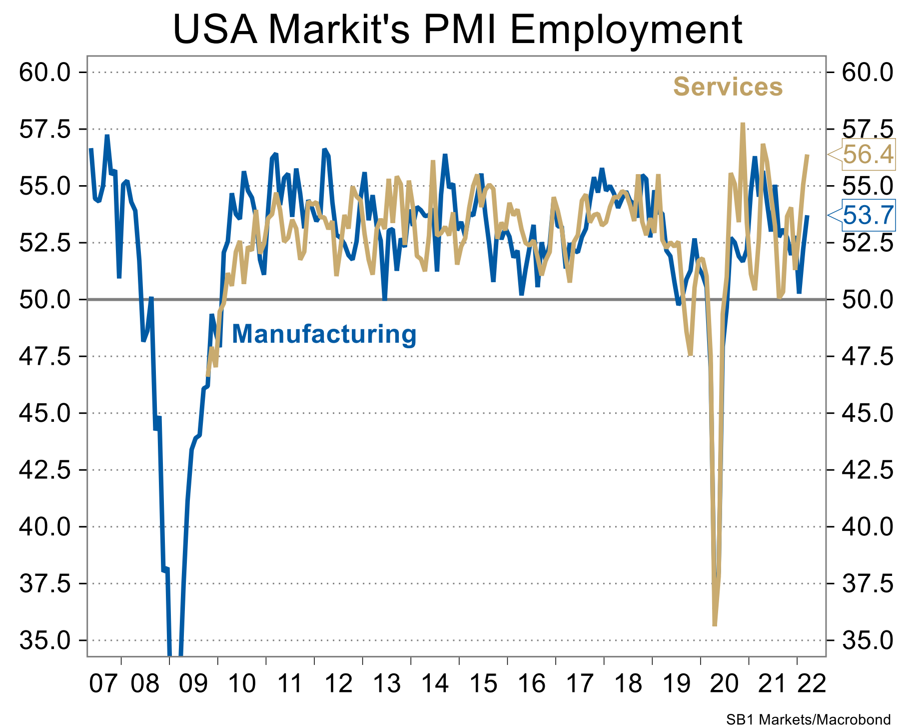


- **The composite PMI** fell sharply in January, due to a setback in services – but the index is now back on track
- **The price indices** was close to unch, at very high levels
- A positive sign: the **delivery times index** further – and it is trending down but remains at a high level. Orders were growing faster too
- Companies report that **employment** rose at a brisk pace in March too especially in the service sector

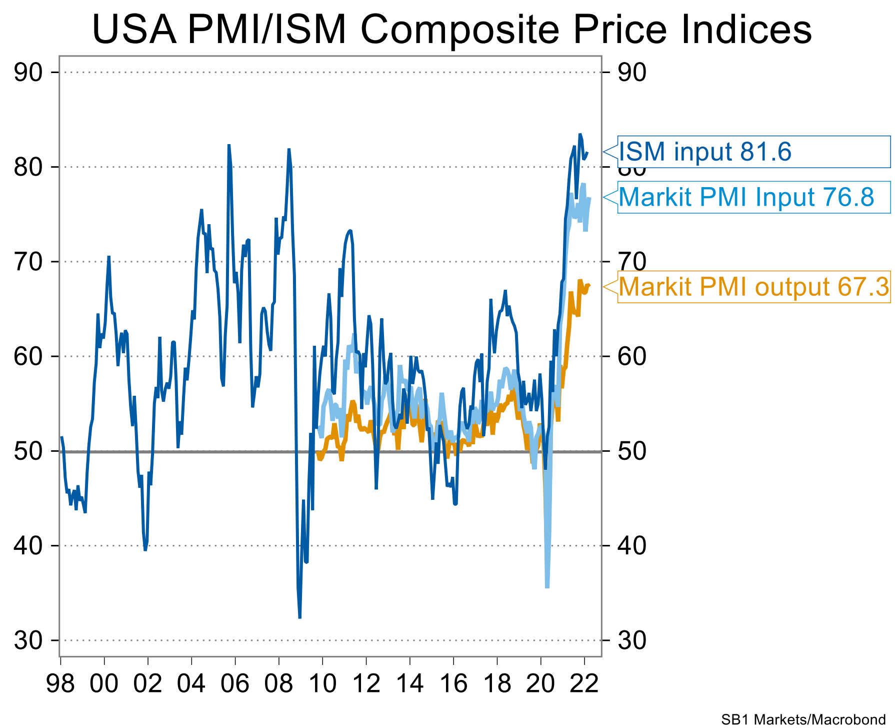
Manufacturing orders are growth well above trend, so is employment

Services report an unusual rapid growth in employment





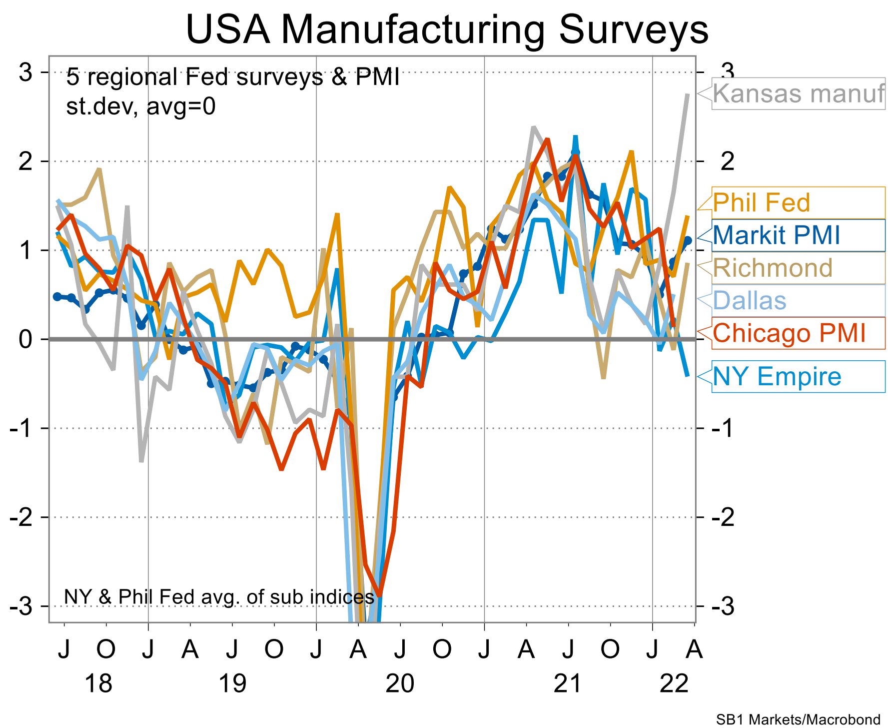
Peak price inflation? Well, not that convincing yet

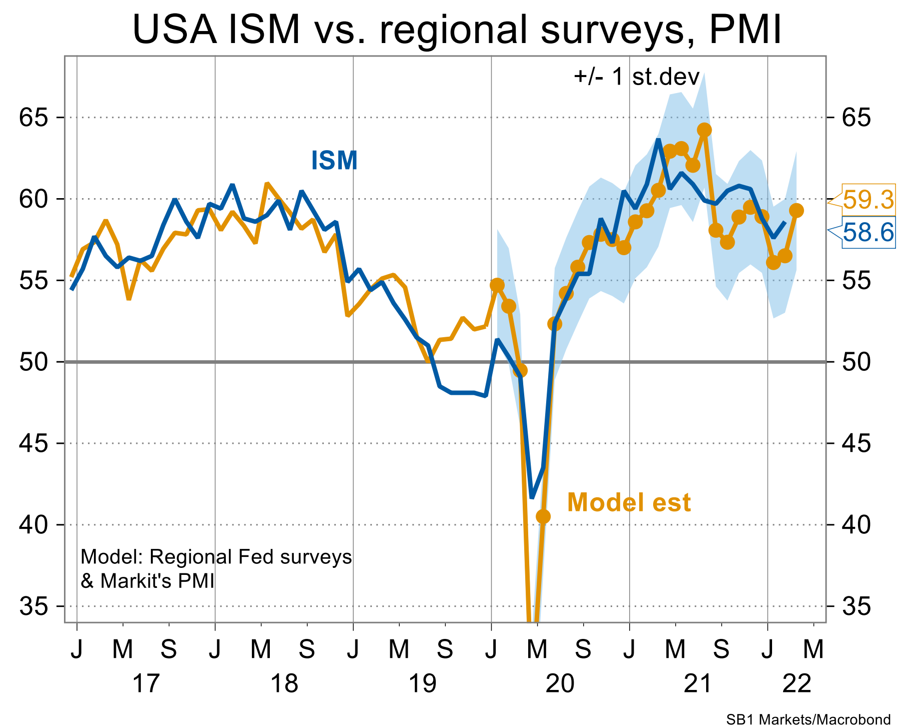


- ISM has not yet reported January data

4 out of 5 manufacturing surveys up in March, just NY Fed's down

Another lift in the ISM index. Anyway, the level is very high, not far below 60

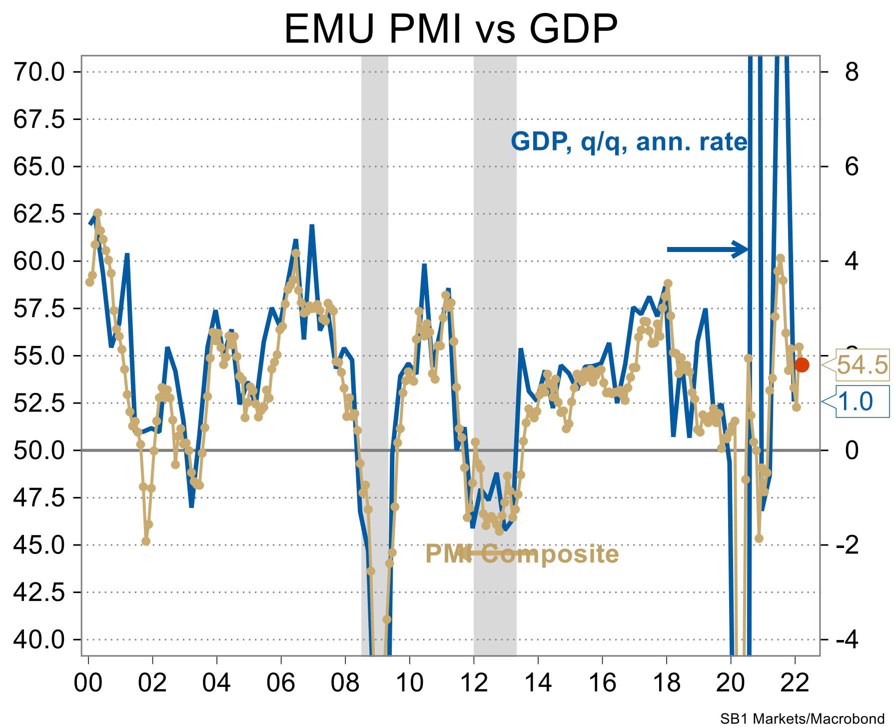


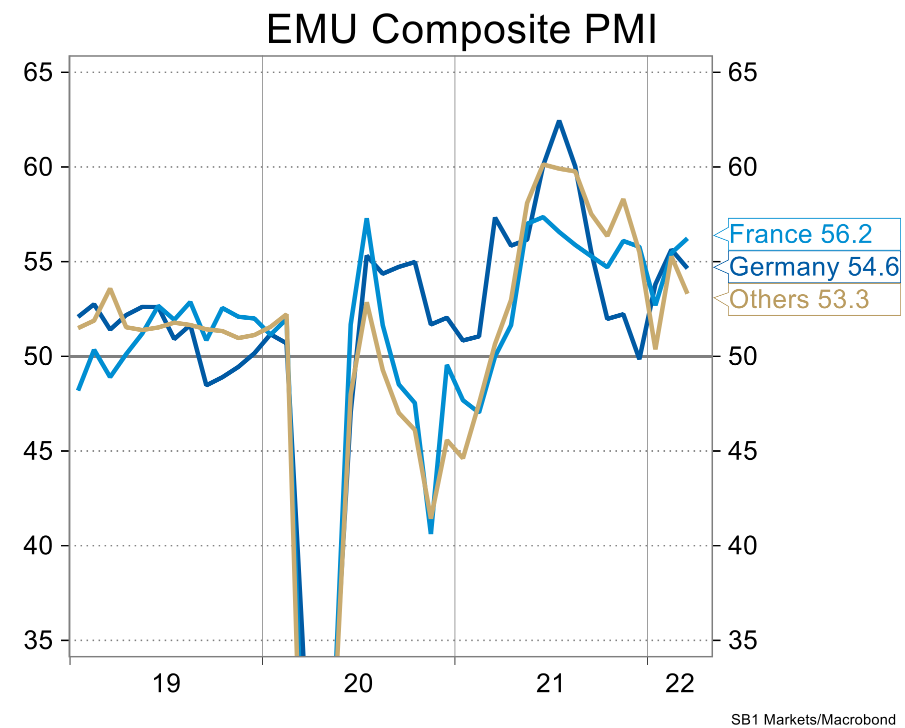


- Dallas Fed and Chicago PMI have not reported their manufacturing surveys yet

The composite PMI down 1 p to 54.5, no material impact from the war (yet)

The (nuclear powered) French PMI up, the (gas powered) German PMI down

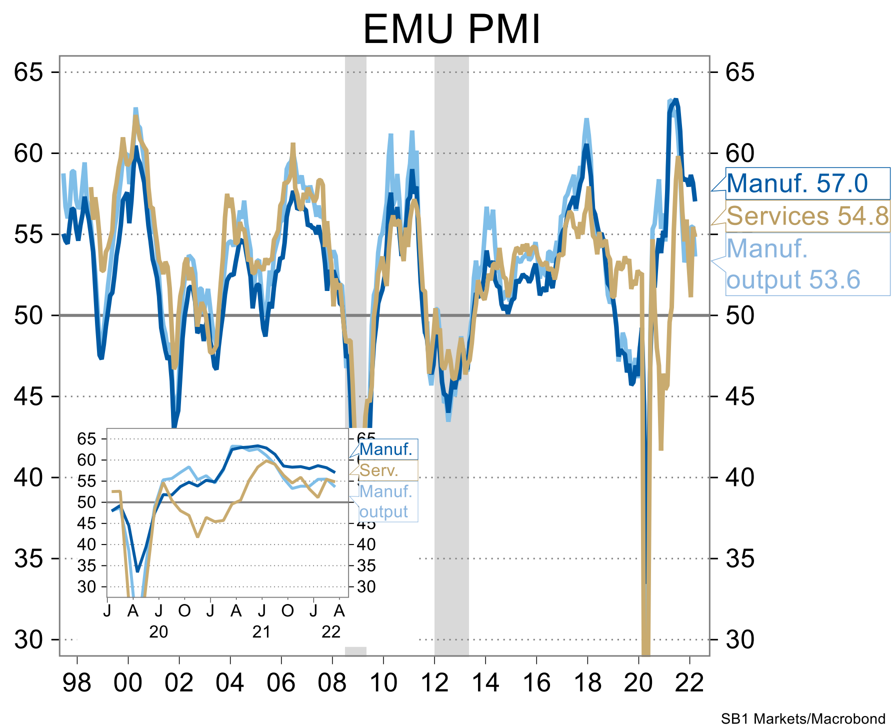


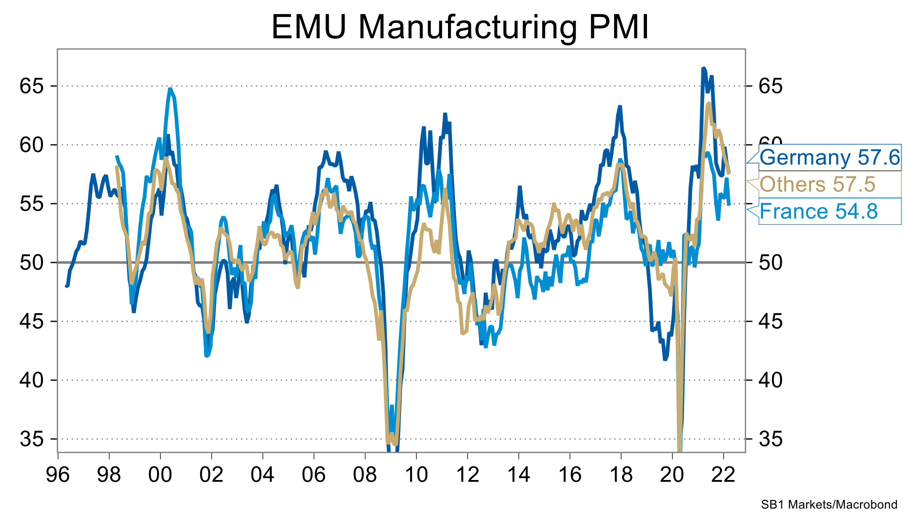


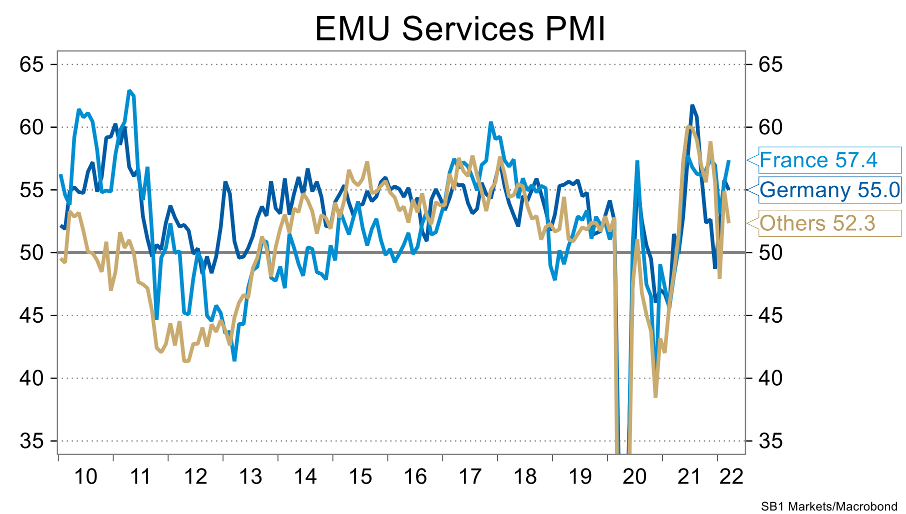
- **It is too early** to expect companies to report any large scale impacts of the war in Ukraine or sanctions. The respondents are asked about actual changes vs last month in new orders, production, employment etc. They are not asked about their expectations (except in an expectation part of the survey which is conducted in some countries)
- **The composite PMI** fell 0.7 p less than expected. The index signals a 2% GDP growth pace
- **The French** are less dependent in Russian gas, and are probably less worried about the energy bill

The manufacturing survey down, still strong

Services are reporting growth above trend too



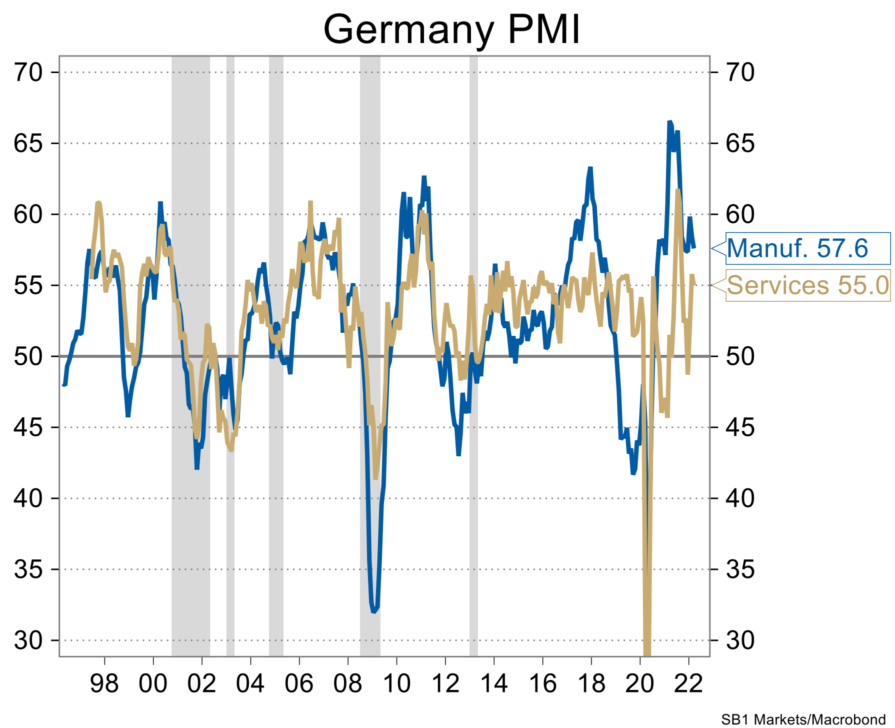


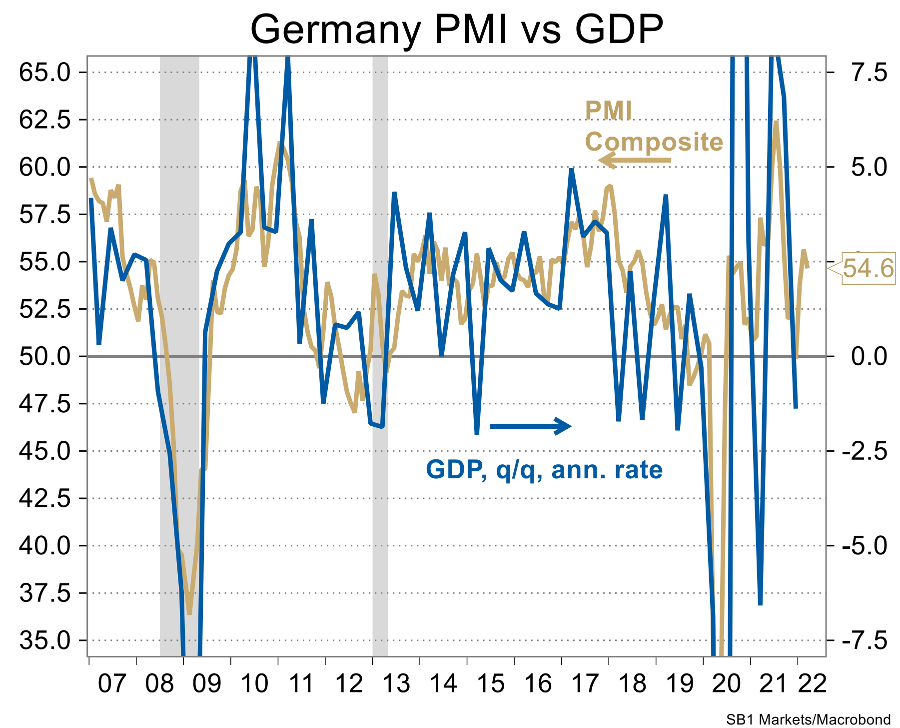


SpareBank 1 MARKETS

Germany: The PMIs just slightly down, activity kept up in the first part of March

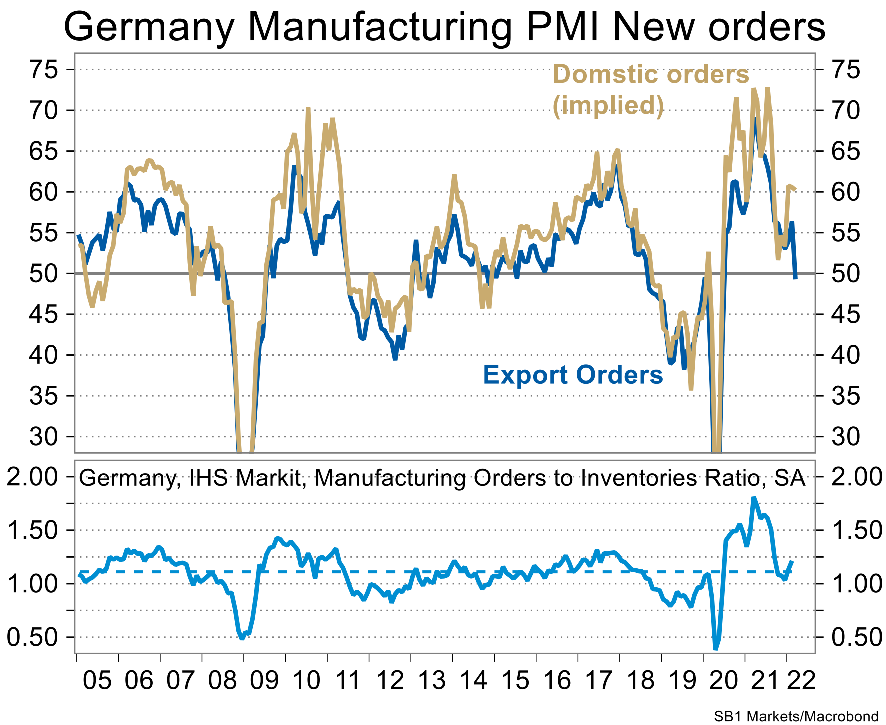
The composite PMI down 1 p to 54.6 → 2.5 % GDP growth





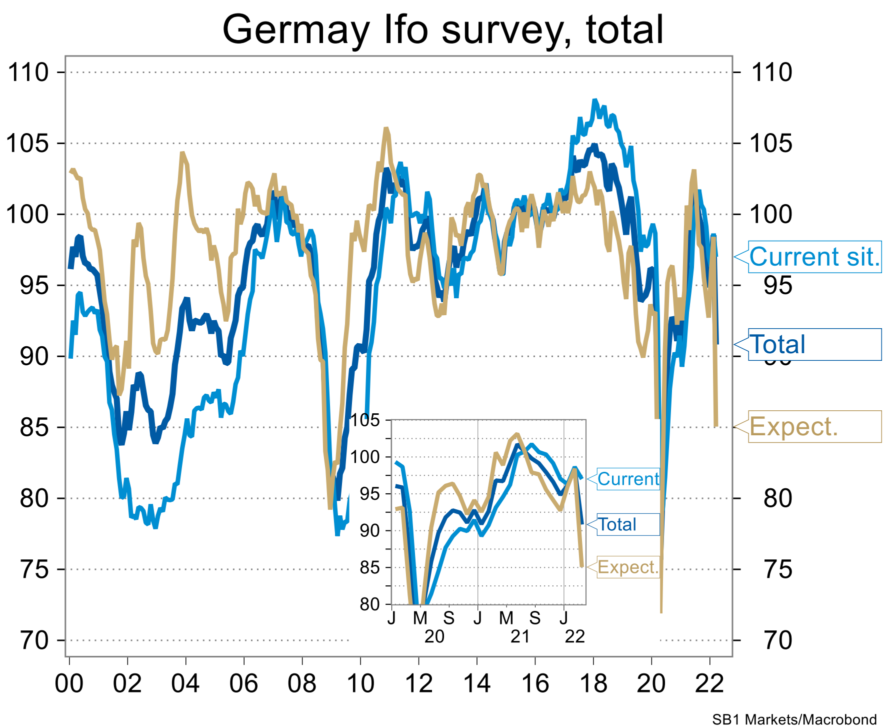
- **The war in Ukraine** has not yet created a sudden slowdown in orders but foreign orders slowed in early March
- **The composite PMI** was 0.8 p higher than expected
- **The manufacturing PMI** declined 0.8 p to 57.6, 1.6 p better than expected. The order component felt due a decline in export order index, while domestic orders (implicitly) kept up
- **The service sector PMI** fell 0.8 p, and was 1.3 p better than expected

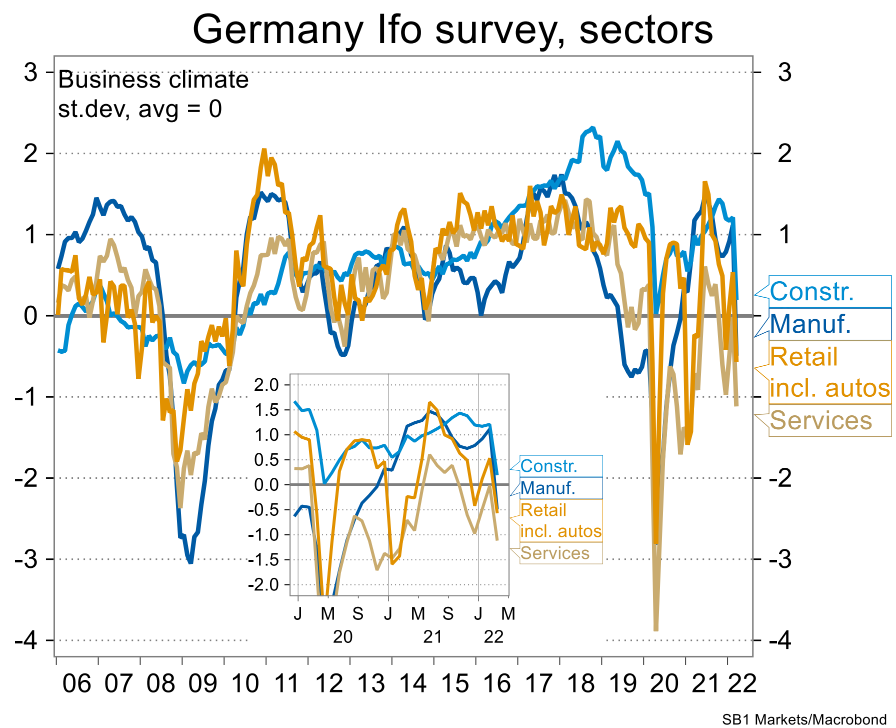
Export orders down in March



Ifo business expectations collapsed in March, the largest decline ever!

The index down 2.8 st.dev to -2.4, all sectors expect a sharp deterioration of business conditions

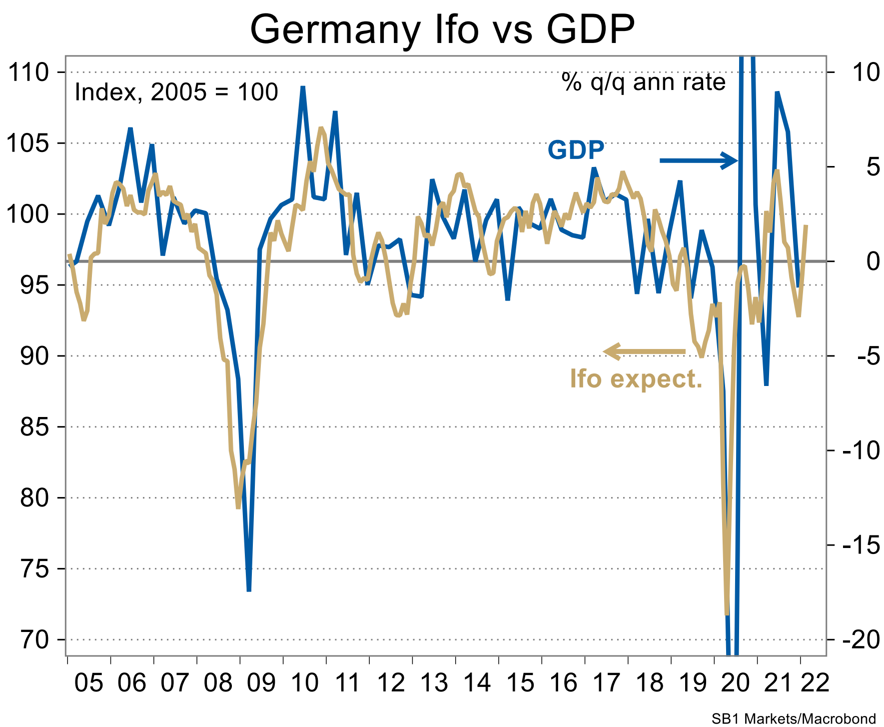


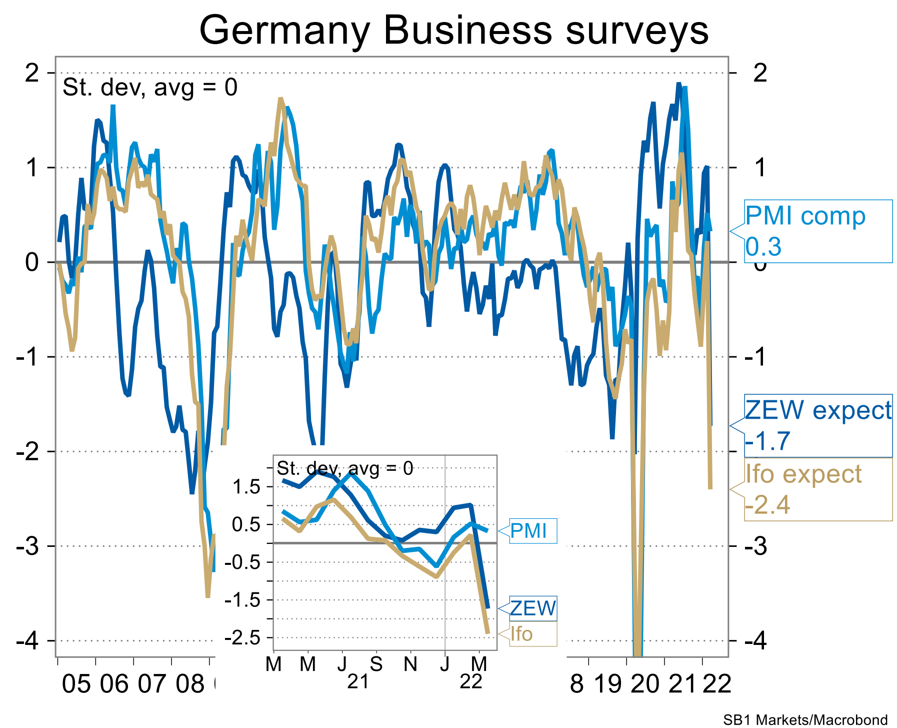


- **The expectation index** fell 13.4 p to to 85.1, expected down to 92. There is of course just one possible explanation, the war, sanctions & energy uncertainty
- The **assessment of the current situation** fell just 1.6 p, and remain well above an average level

Expectations down (ZEW & Ifo) activity still OK (PMI)

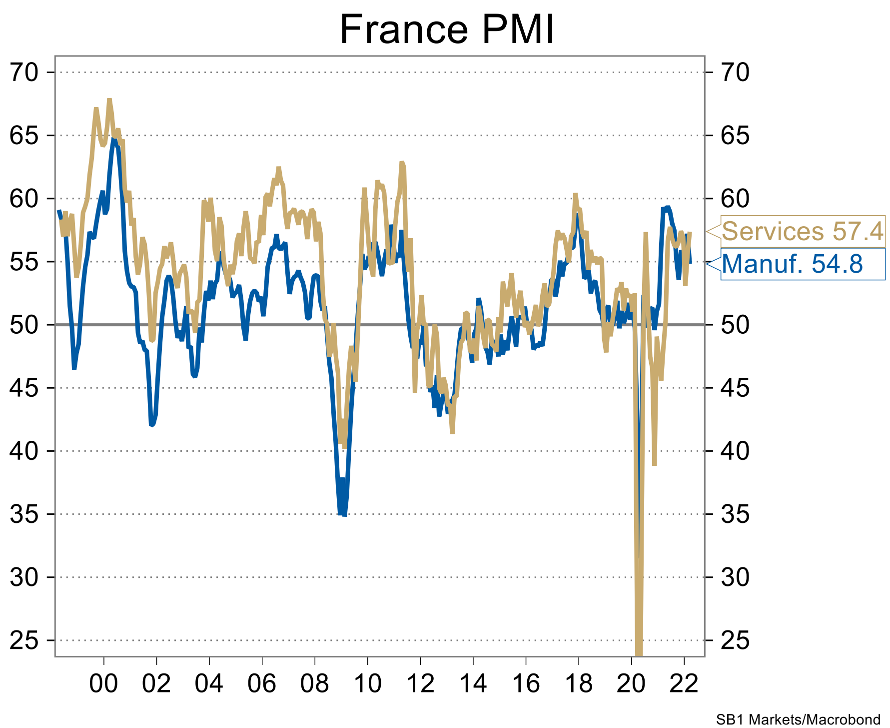
The coming months will be rather … interesting

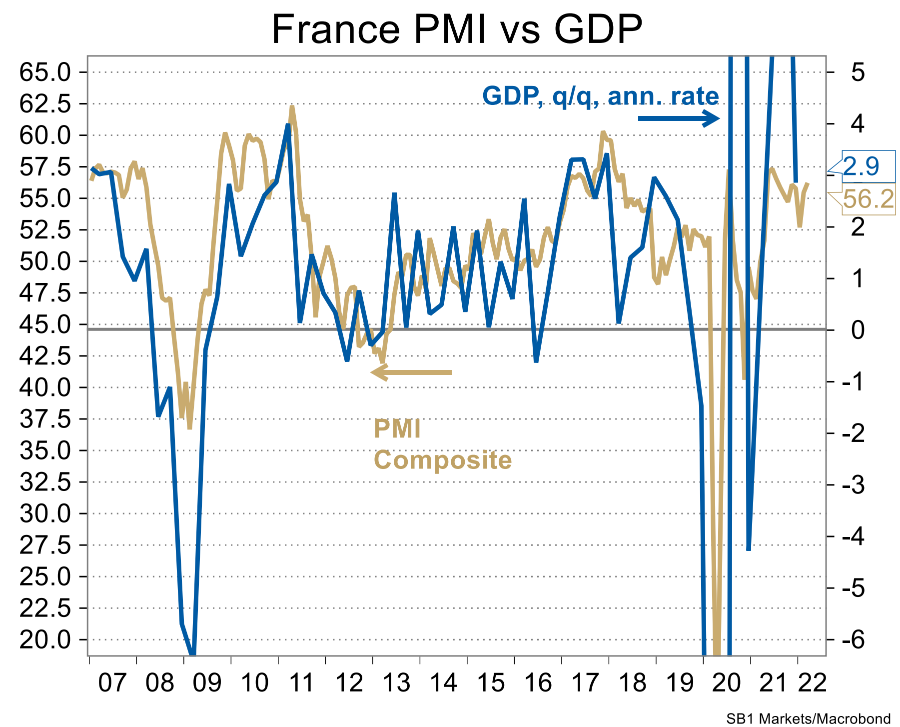




France: Services still going strong, manufacturing too

The composite up 0.7 p to 56.2 (expected down to 54.5) → 3% GDP growth is signalled

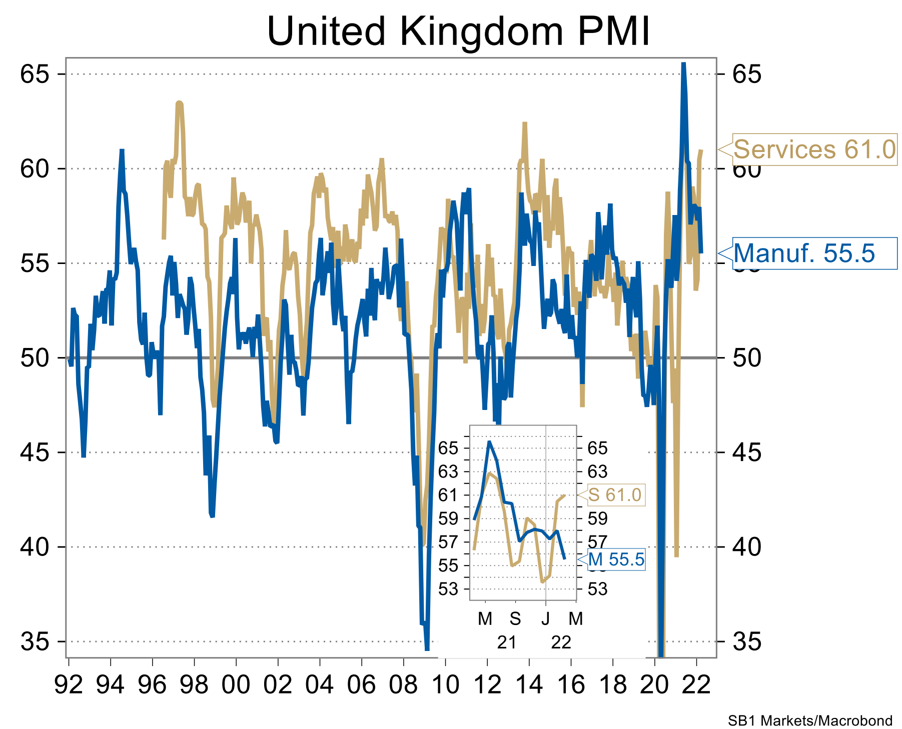


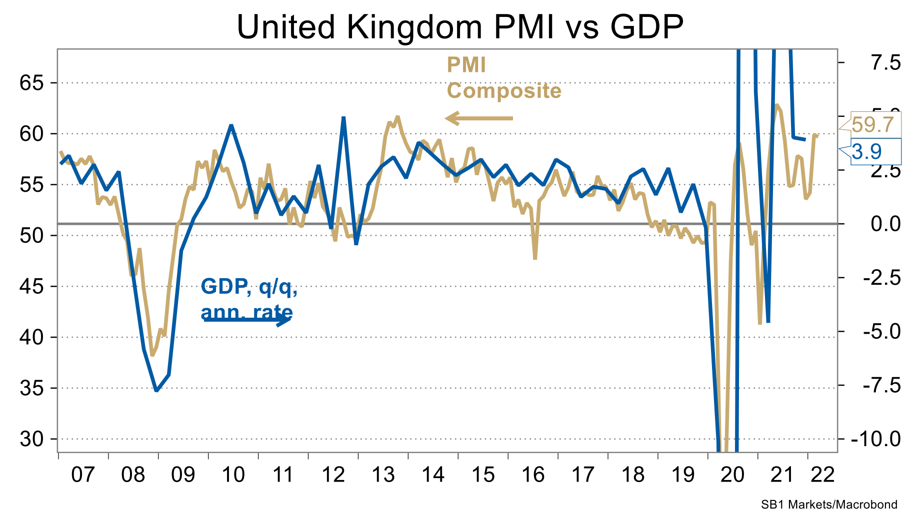


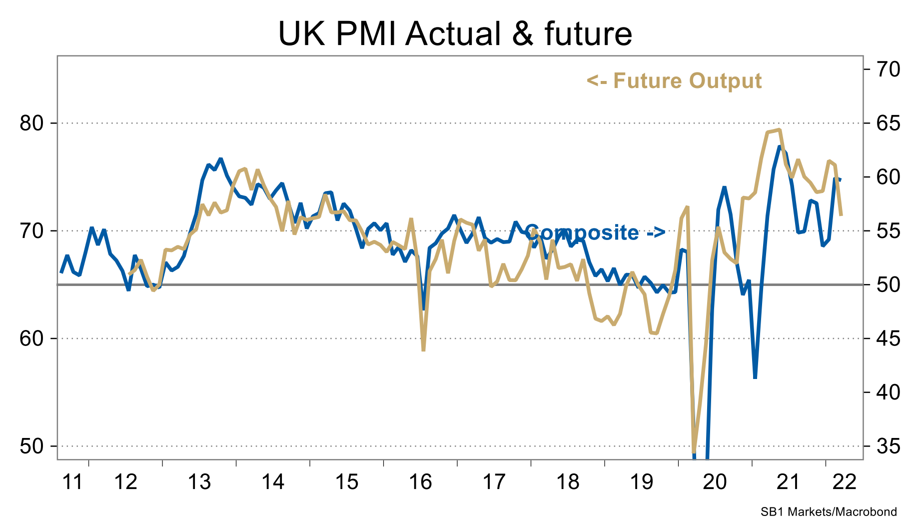
- The service sector PMI rose 2.4 p to 57.4

The PMIs further up in March: at 59.7 a post Omicron recovery confirmed

The manufacturing PMI declined but services are blooming



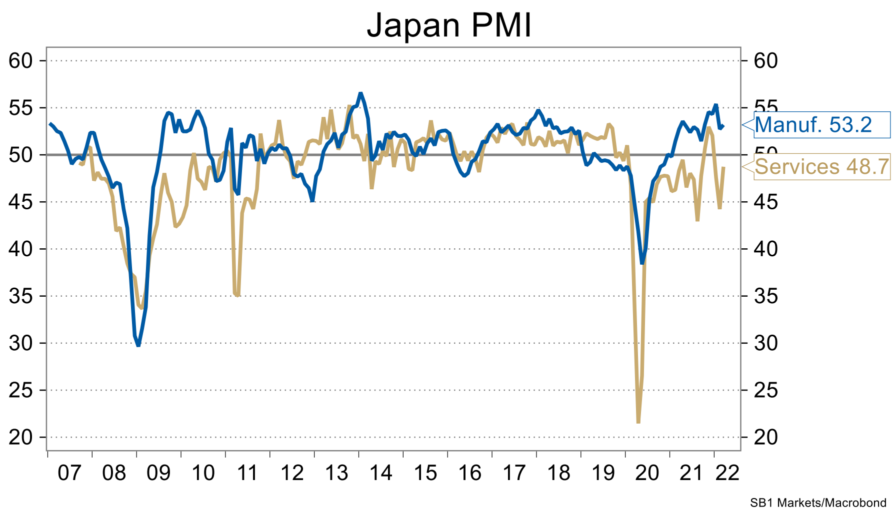


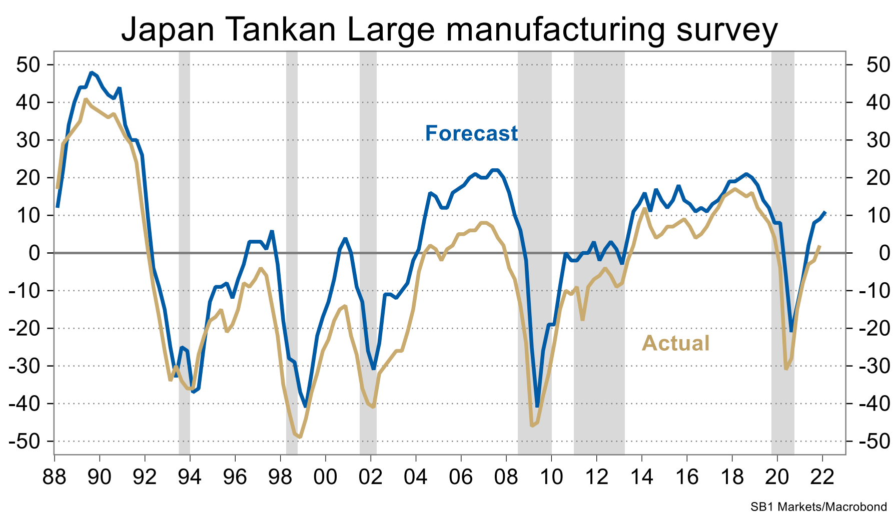


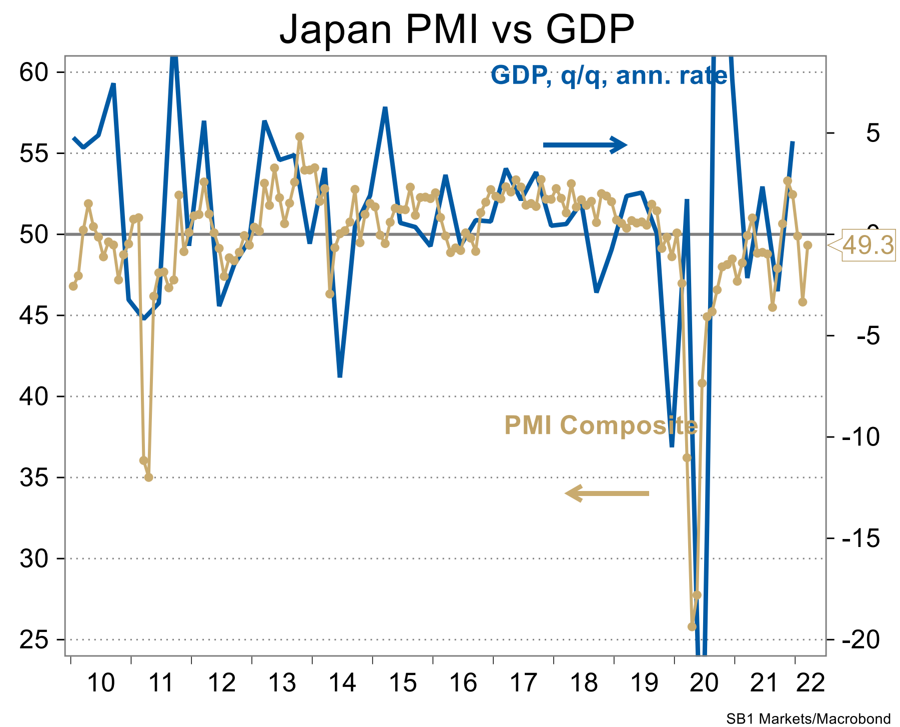
- **The manufacturing index** fell 2.5 p to 55.5. The output index fell 4.3 p to 52.6, which is not signalling growth above trend
- **The service sector** index rose rose further – and the composite index rose marginally
- **The future index** fell sharply however, very likely due to some concerns vs. the fallout of the war in Ukraine

The PMIs up in March, the composite still below 50, signalling no growth

The service sector PMI recovered, but remained below the 50 line. Manuf. at an OK level

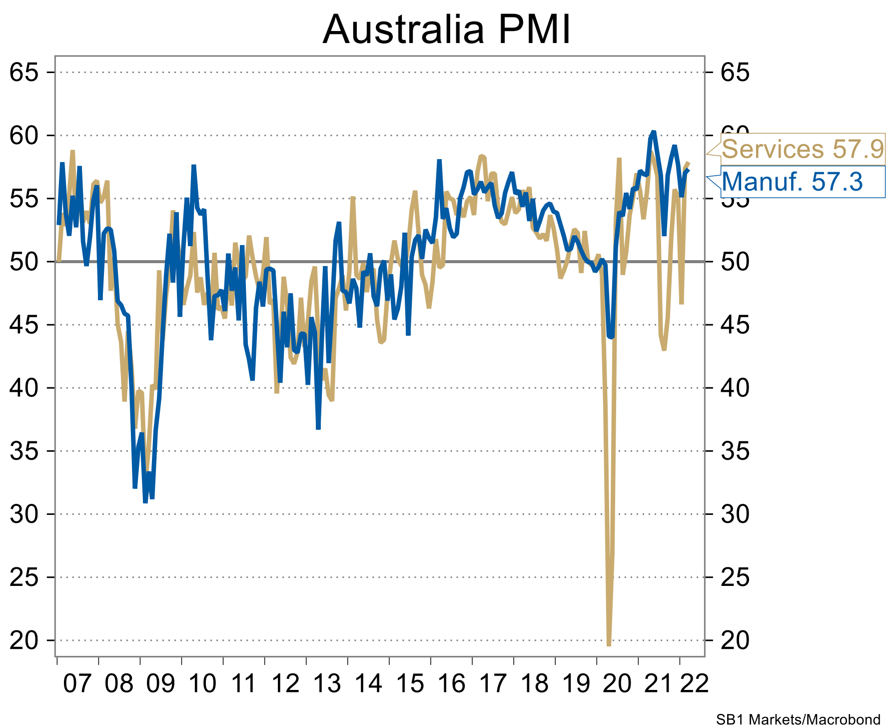


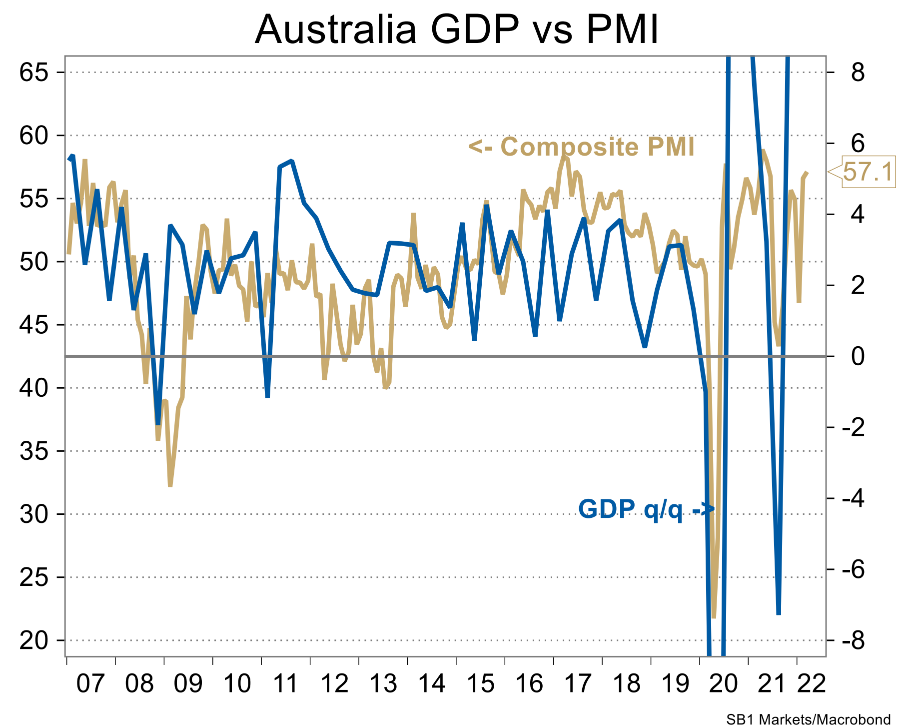




Full speed ahead in Australia, the both manuf. & services at the 57-level

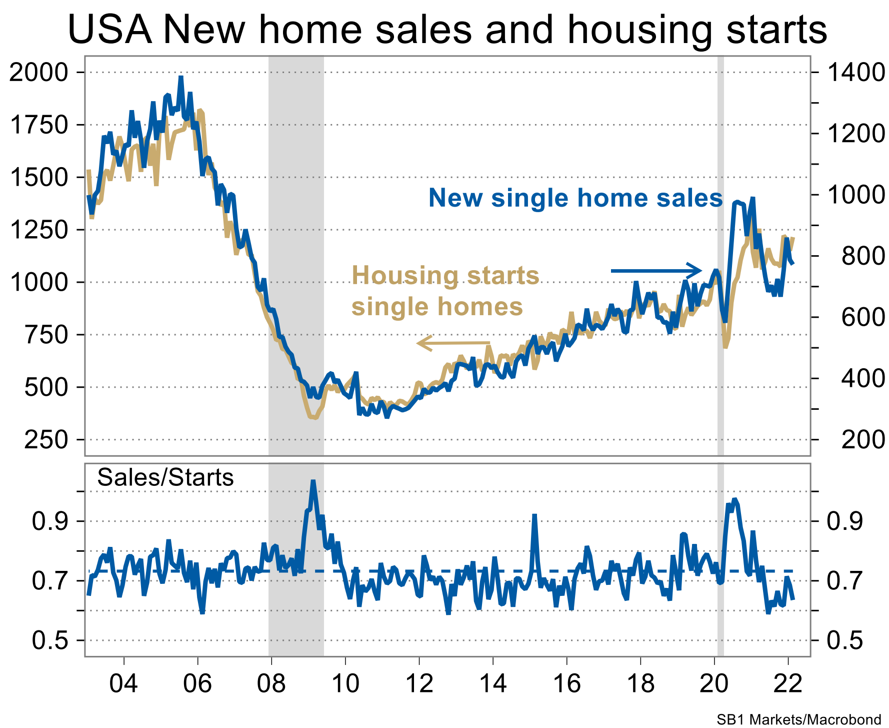
Which is not far below previous cycle peaks

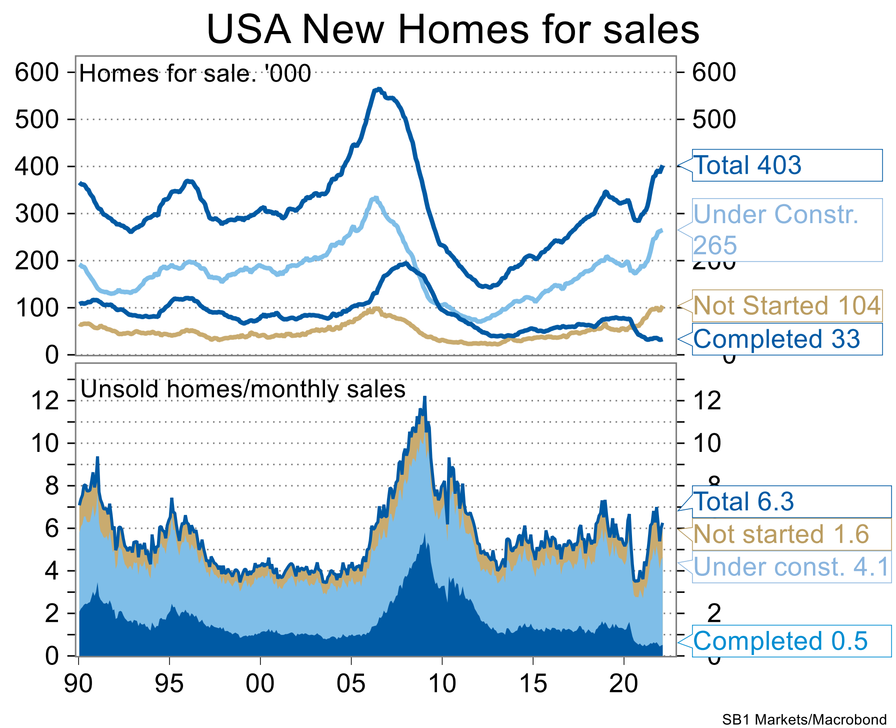




New home sales down in Feb, the total inventory of unsold homes on the way up

Prices have stagnated too. However, sales are still strong, and just few completed homes are for sale

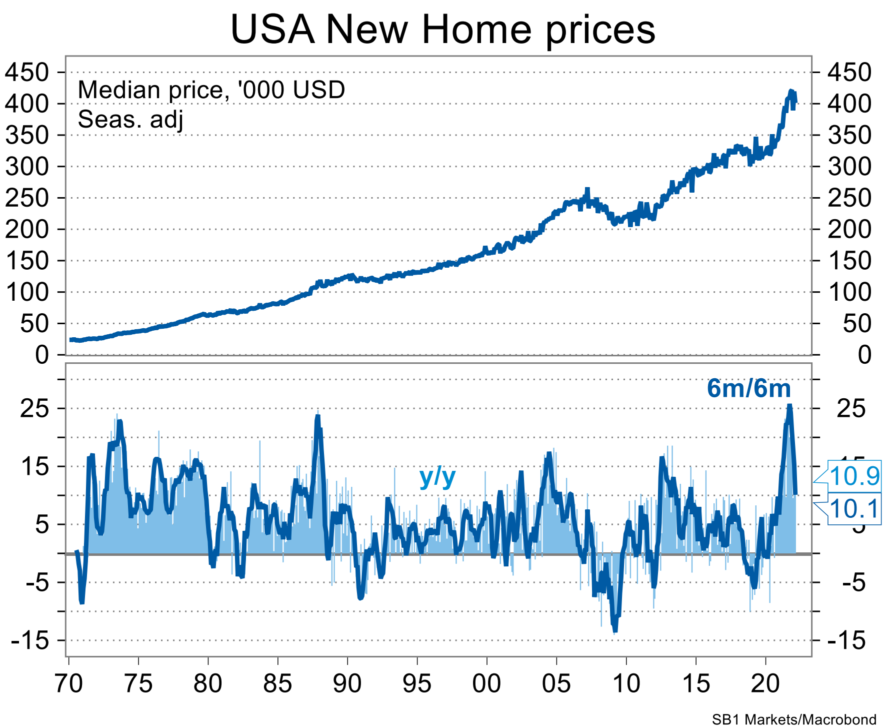


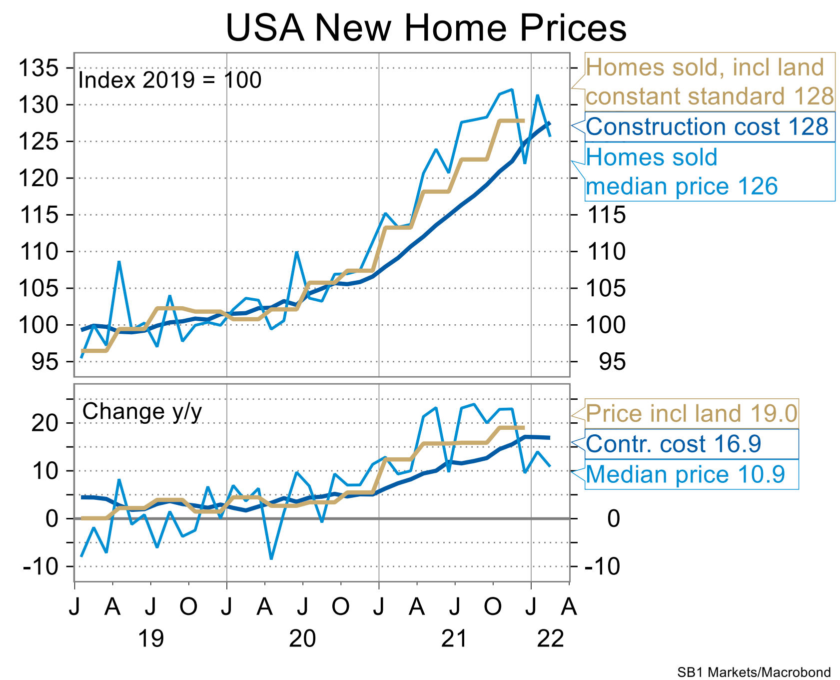


- **New single home sales** fell to 772'' (annualised rate) in Feb – from a slightly downward revised 788' in Nov, expected up to 810'. These monthly figures are often revised substantially and the last observation is close to useless
- **The big picture:** Following a 30% decline from January to June, sales were stable through H2 last year, at approx. the same level as before the pandemic – until the hike in Dec. Sales have been somewhat lower than normal vs. new single home starts (in avg. sales are 70%+ below starts, as may homes are built by homeowners themselves)
- **The inventory of unsold homes** has increased by 42% since Oct 2020, and the level is the highest since 2008. The inventory equals 6.3 months of sales, a bit higher than 'normal' – and up from the record low level at 3.5 months in Sept 2020
  - » The increase in the inventory is not due to large increase in completed house for sale (the most 'effective' supply), and this inventory just equals 15 days of sale (1/3 of a normal level). However, the no. of projects not yet started (but for sale) has doubled, <u>to the highest number ever,</u> and the no. of new homes at the market but still under construction has climbed rapidly, to the highest level since 2007. So, there are lot of homes in the pipeline, and clearly a <u>confirmation that the supply side is responding to the steep increase in demand. At one stage, combined with higher mortgage rates, that could change the housing market outlook</u>

New home prices has flattened? Prices are up 11% y/y, but flat since last summer

Construction costs are up 17% y/y, selling prices is up 19% as land prices are more up than constr. costs

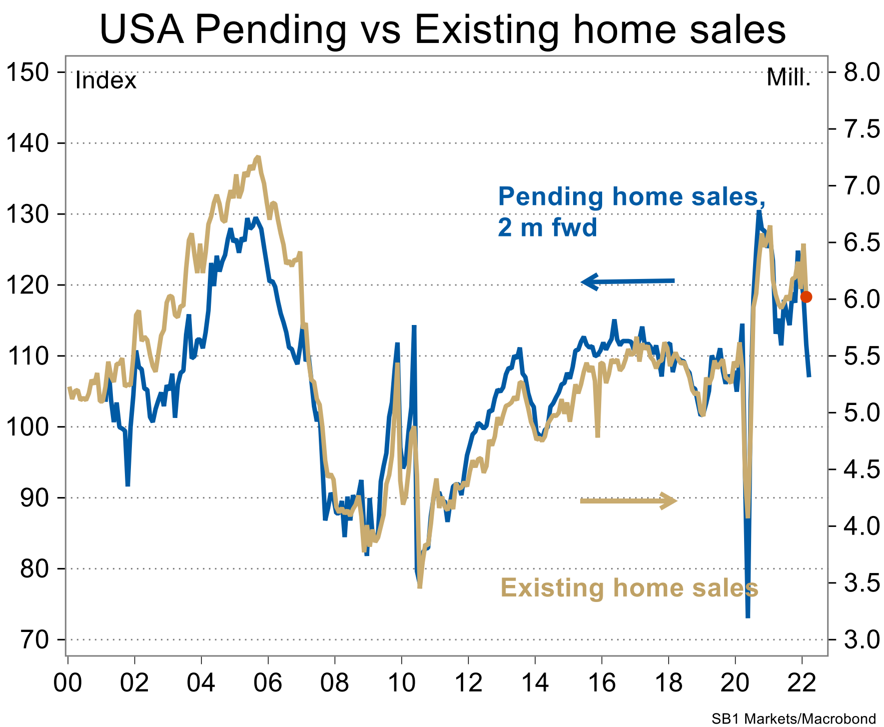


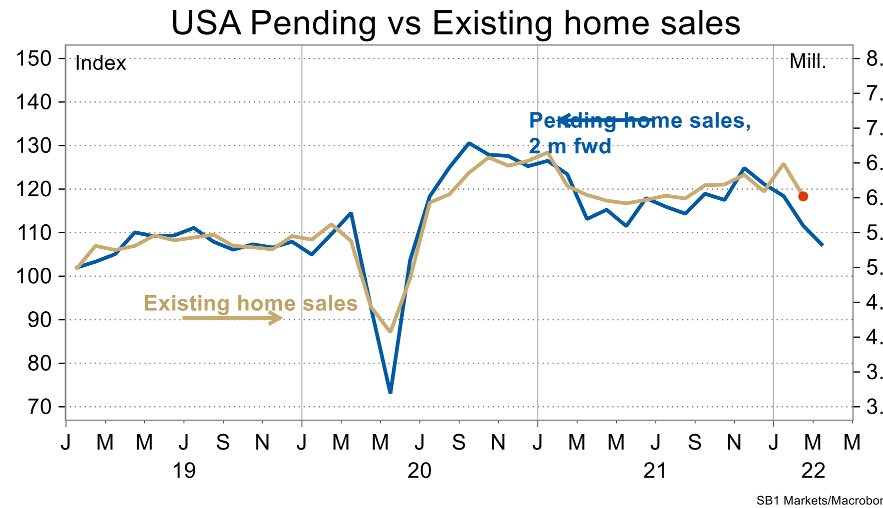


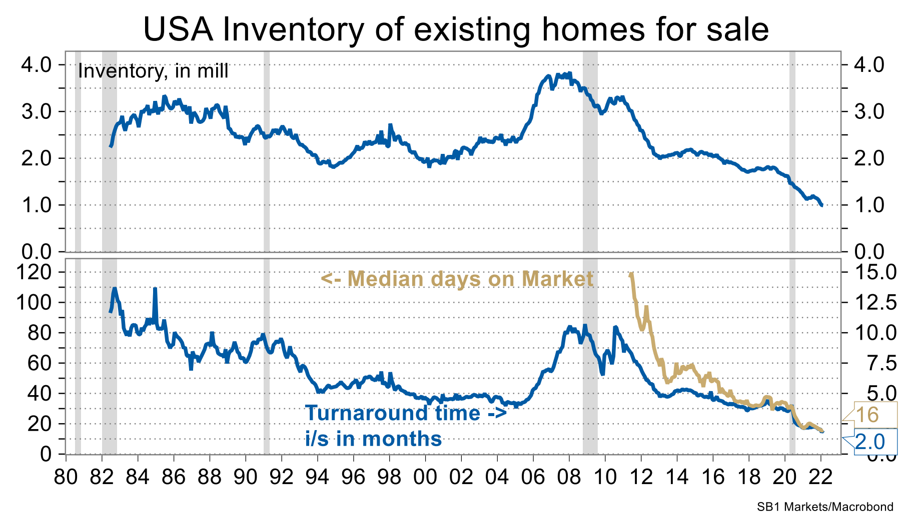
- Monthly **median new home sales prices** are <u>very</u> volatile, as these prices are not adjusted for changes in the mix of home sold
- The **construction price index** is adjusted for changes in standard & size, as is the **new homes sold price index**, which also includes cost of land: they are up by 17% and 19% resp., measured y/y in Feb/Q4
  - » As prices including land are still up more than the construction cost index (which of course is influenced by higher material costs), which implies an even faster increase in <u>land prices</u>. Thus, <u>demand must be the main driver for the hike in prices, not the construction cost (if demand was weak due to high prices, prices including land would have climbed less than construction costs)</u>

Pending home sales further down in February, mortgages rates start to bite?

No. of agreed transactions is down 14% from November





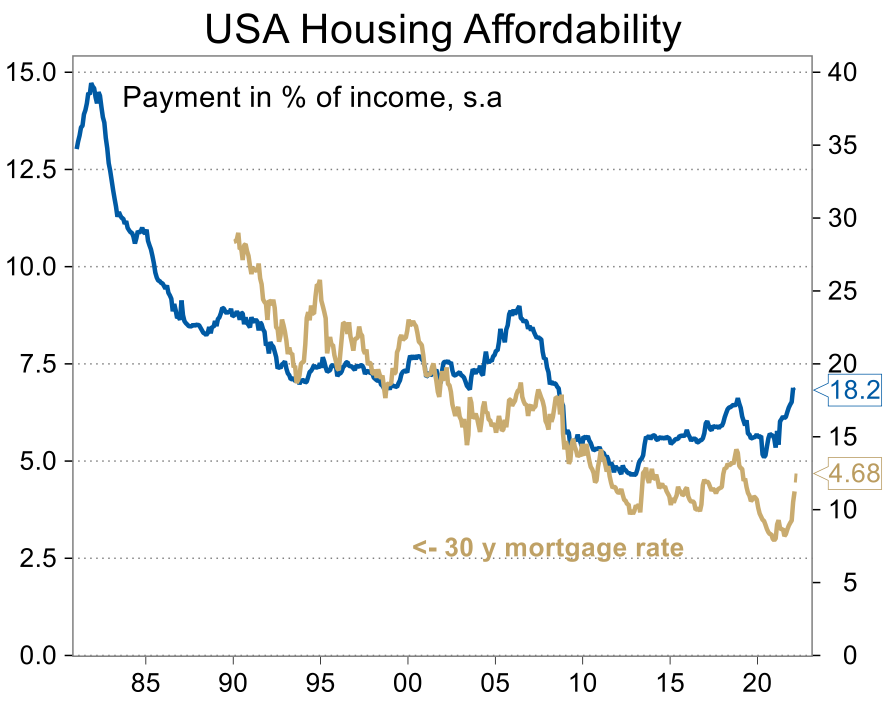


- The decline is significant – and important – as it signals that higher mortgage rates may slow down the housing market
- In December and January **existing home prices** rose faster than over the previous months, though based on deals signed in November and December ('pending sales'). The inventory of unsold homes is at record low level, whatever measure we apply and sales may decline due to lack of available supply
- However, Since December, the 30 y fixed mortgage rate has climbed 130 bps to 4.8%, which of course may hamper demand!

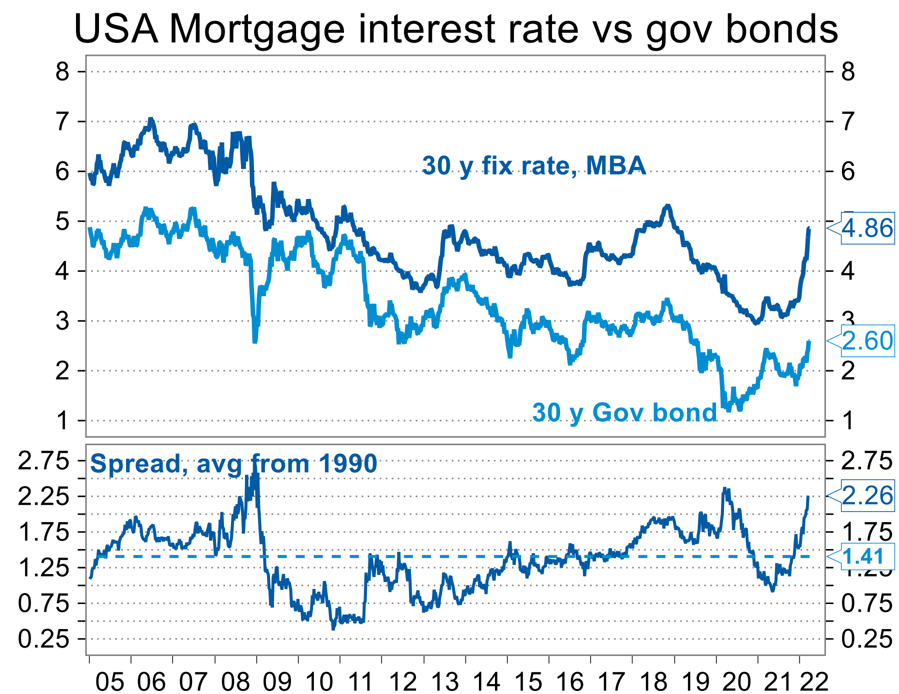
Pending home sales: Deals signed. Existing home sales: The actual transaction, typically 1 – 2 months after signing

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

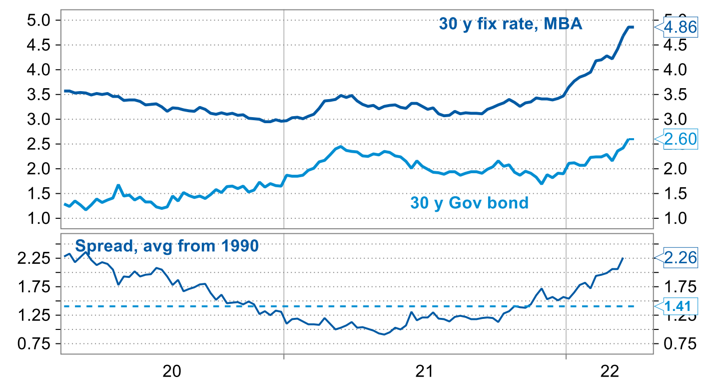
So the affordability is not what it used to be. That is, it is still lower than anytime before 2008



SB1 Markets/Macrobond



SB1 Markets/Macrobond

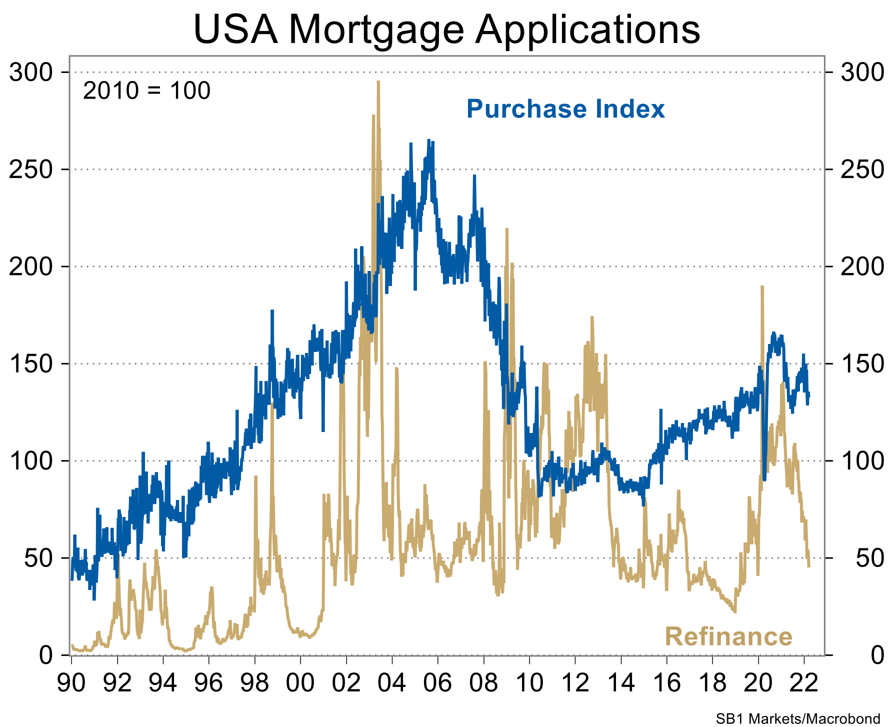


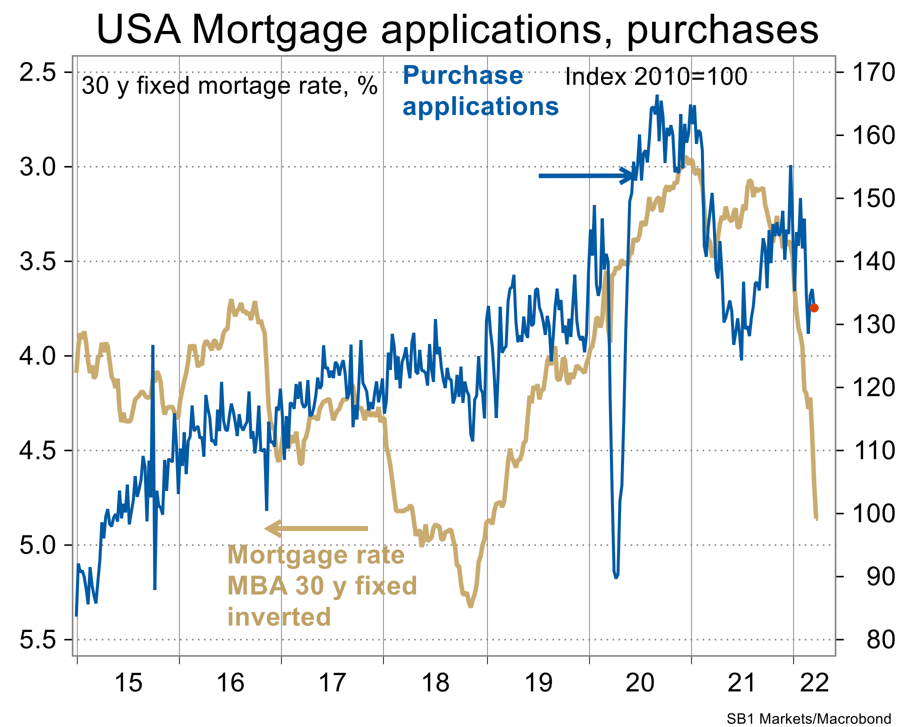
SB1 Markets/Macrobond

- **The 30 y fixed mortgage rate** has climbed to 4.8% (MBA, last week) from 3.0% last summer – and 3.5% by the end of last year
  - » The rate has increased MUCH more than the 30 y Gov bond rate. The spread has widened to 226 bps from 91 at the bottom last spring and it is far above the average at 140 bps
- 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 has not yielded by much

Demand for refinancing has fallen sharply but that is not a warning sign

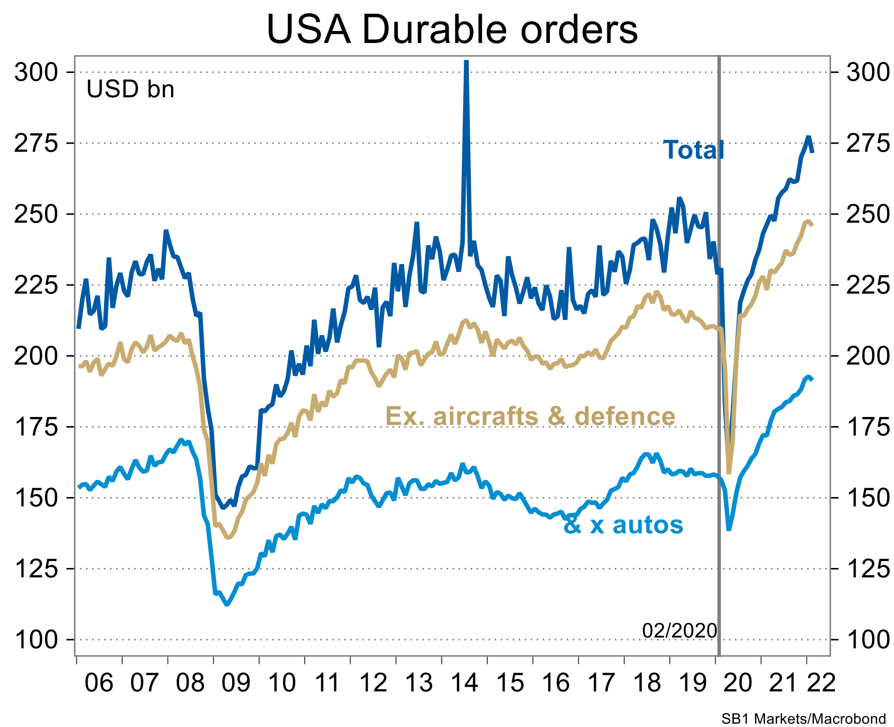


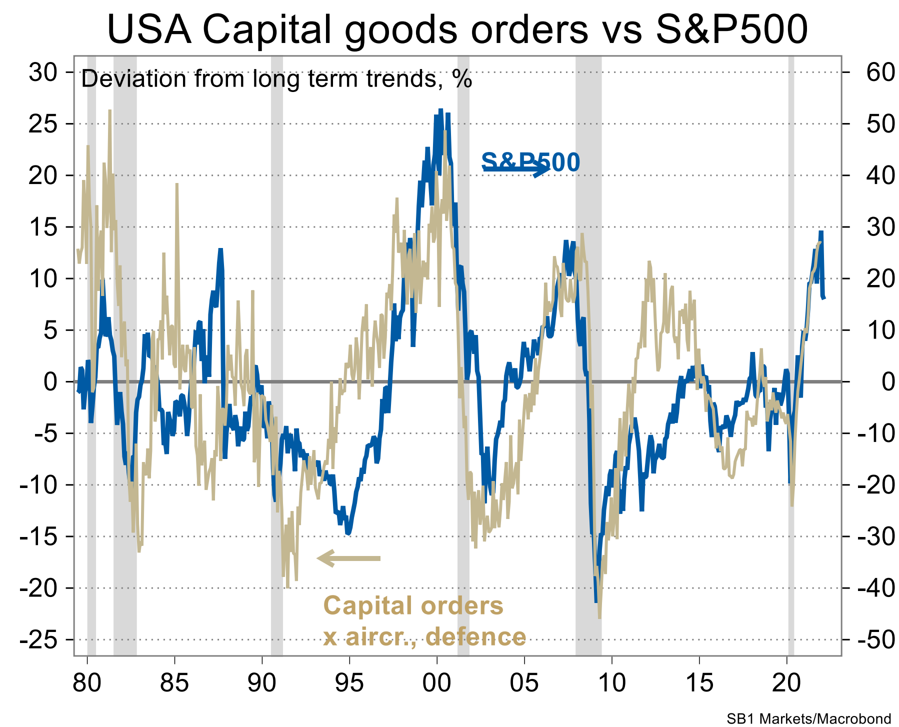


- The correlation between mortgage rates and existing home sales or prices are unstable

New orders down in February

However, investment orders may be slowing somewhat

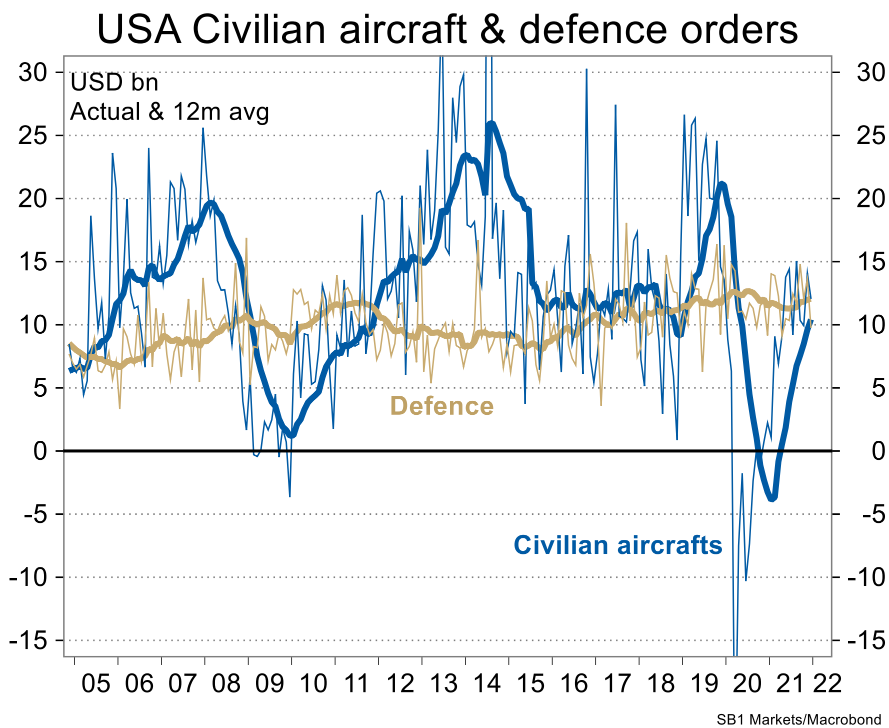


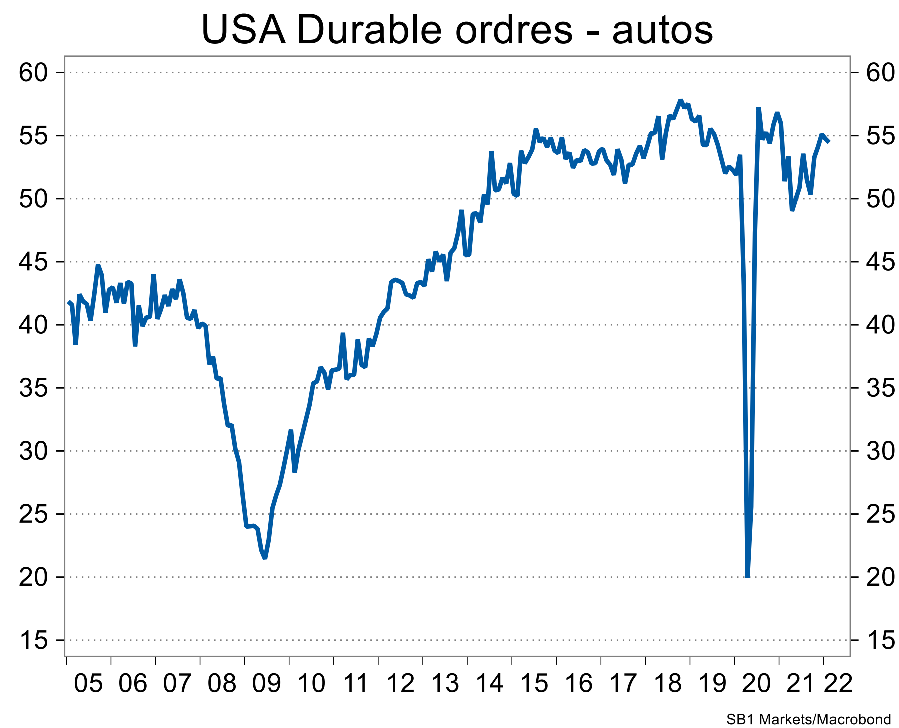


- **Total durable** orders fell by 2.2% in Feb, expected down 0.6%. Both the volatile aircraft & defence orders declined
  - » Ex these two components, the ‘core’ fell by 0.7%, also below expectations – but the trend is strong, as for total orders
- **Core <u>investment</u> goods orders** fell 0.3%, following an upward revised 1.3% lift in January. The trend is still straight up
- **Order inflow** is far above pre-pandemic levels, especially for investment good orders and surveys are still strongly hinting a further increase the coming months

Aircraft & defence orders down in October

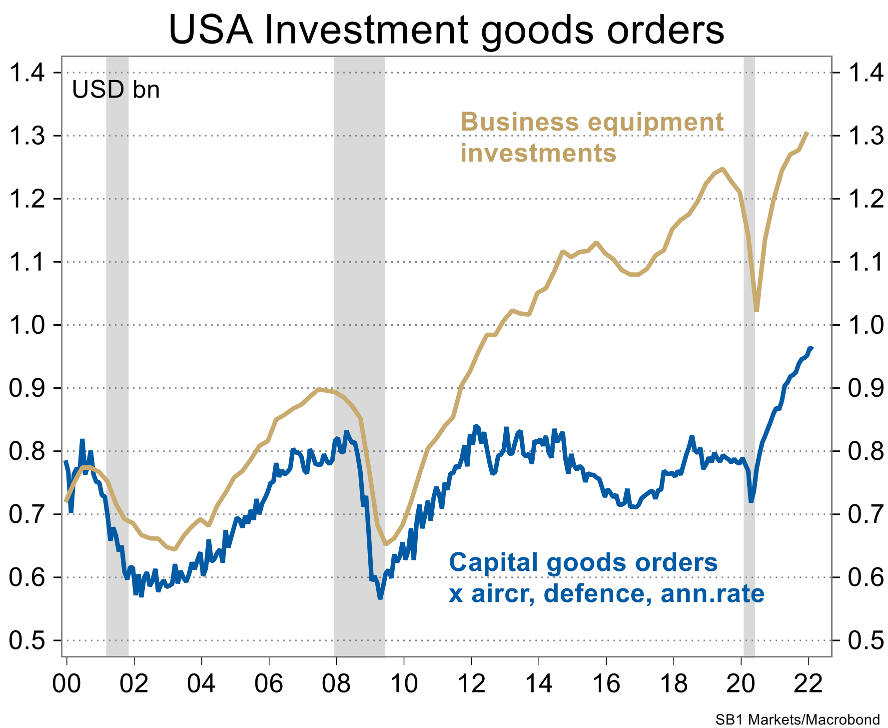
… while auto orders rose – and they are not at low level!

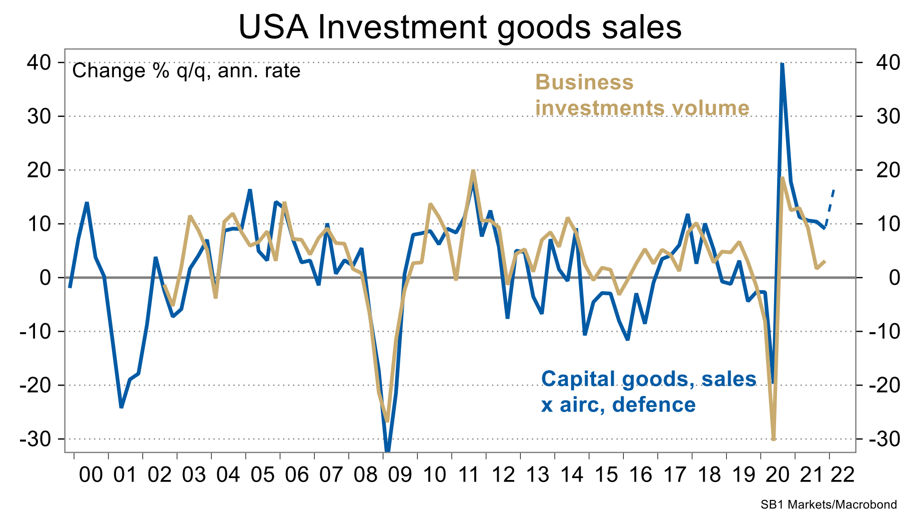




Core capital orders are still going strong

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

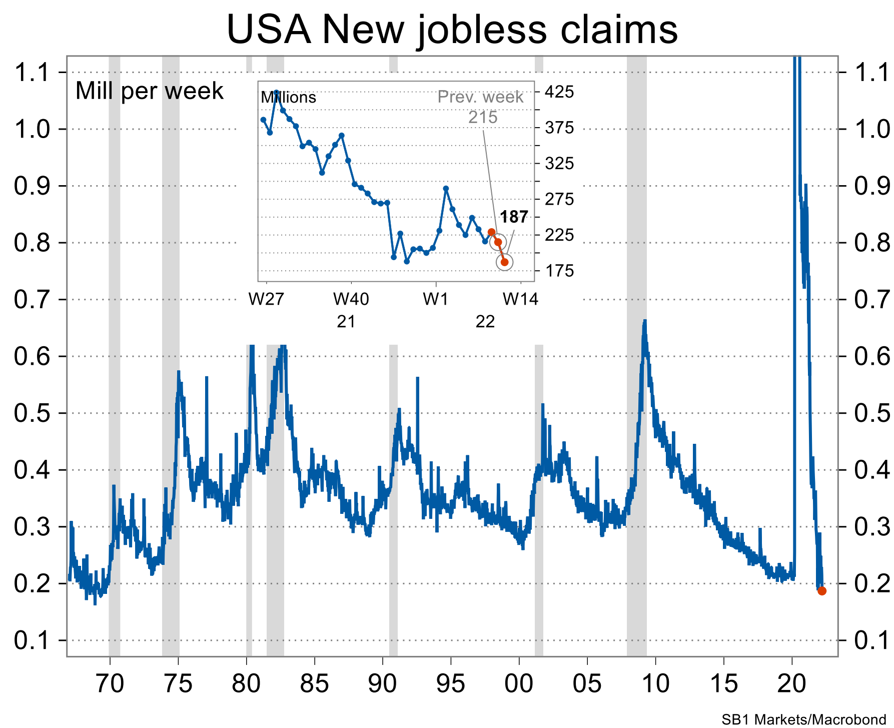


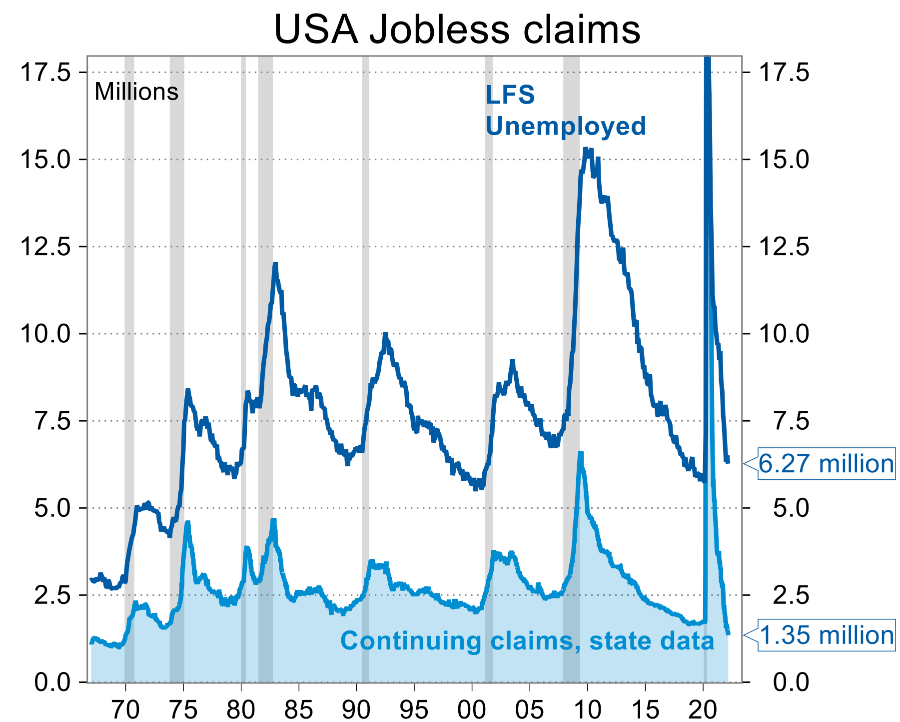


- **Core (x aircraft, defence) capital goods orders** are inching upwards at a 7% pace. Shipments were up 0.5% m/m. A decent growth in business investments is signalled (following a rather slow growth in Q3 and Q4)
- **The business investment** level is well above the pre-pandemic level – and not at low vs. a reasonable long term trend (see more data, comments here)

New jobless claims at the lowest level since 1969! Continued claims lowest too

(Well cont. claims the lowest since week 1 1970). ATL by far in % of the labour force, of course

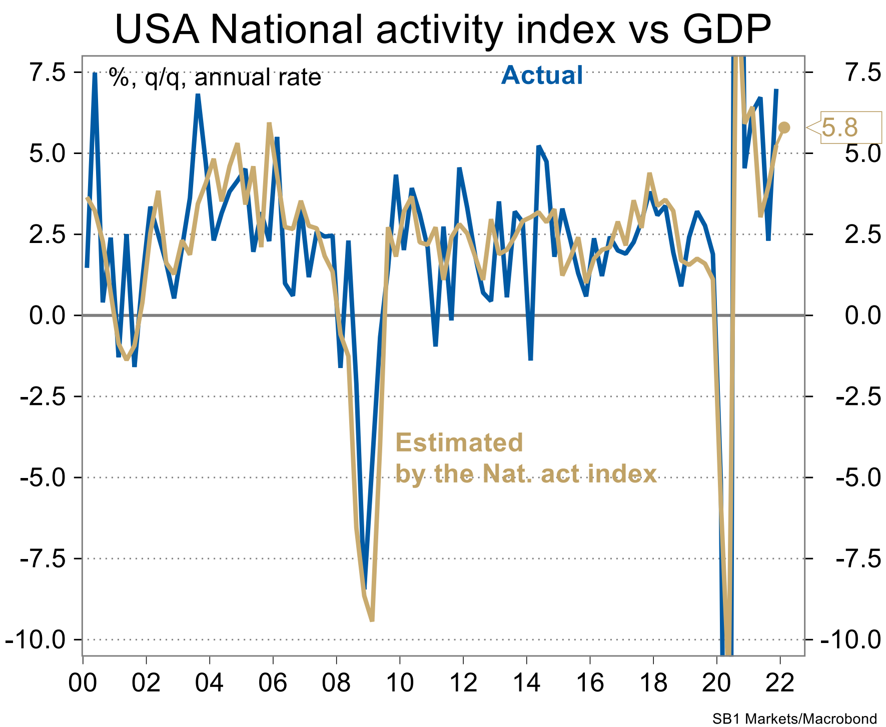


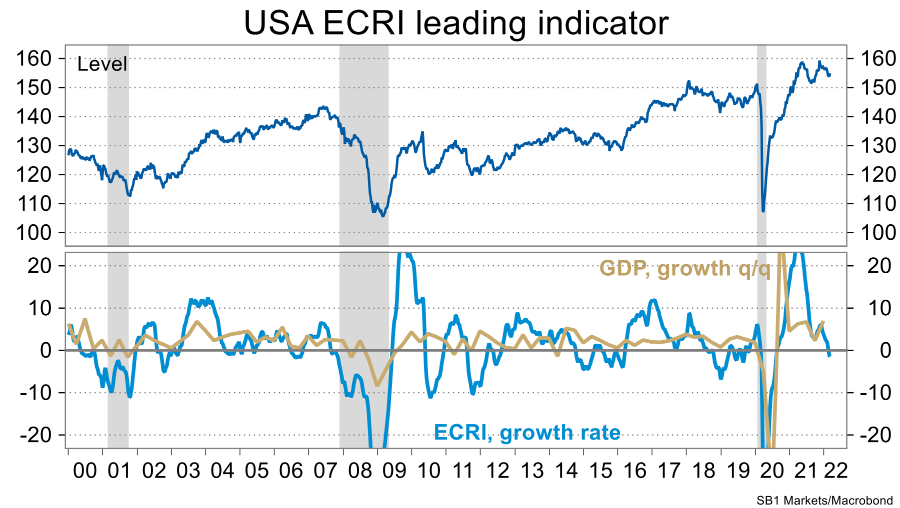


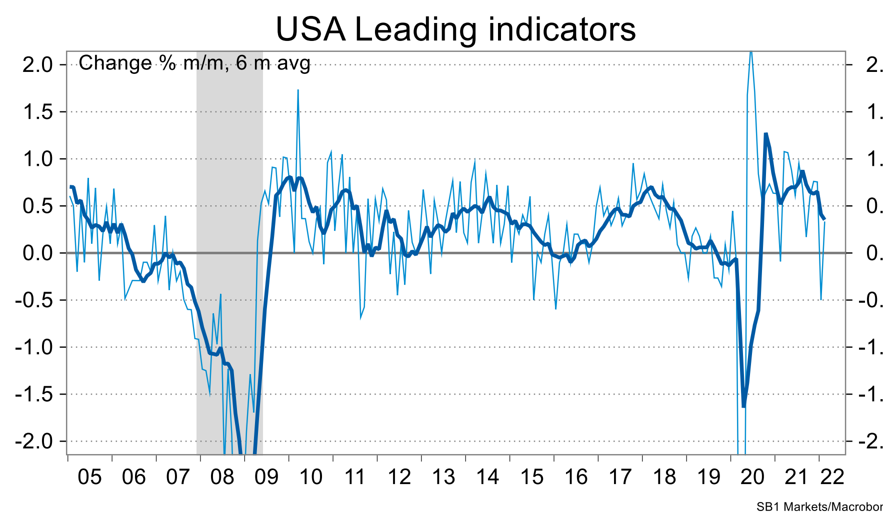
- **New jobless claims** fell 28’ in week 11 to 187’ the lowest inflow since late 1969 – where the labour force was 2 times larger than today
- **Ordinary continuing claims** fell 67’ in week 10, to 1.35 mill, to the lowest level since Jan 1970, and as share of the labour force, the lowest ever, by far

The national activity index signals decent growth in Q1

Other nowcasters are weaker, the ECRU indicator report growth close to zero, LEI growth at trend



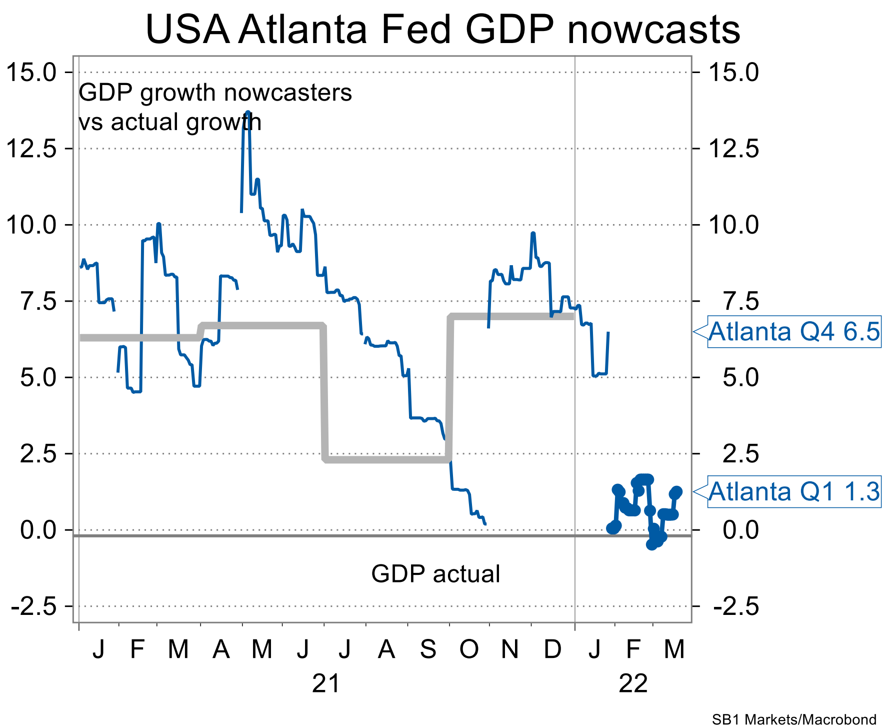


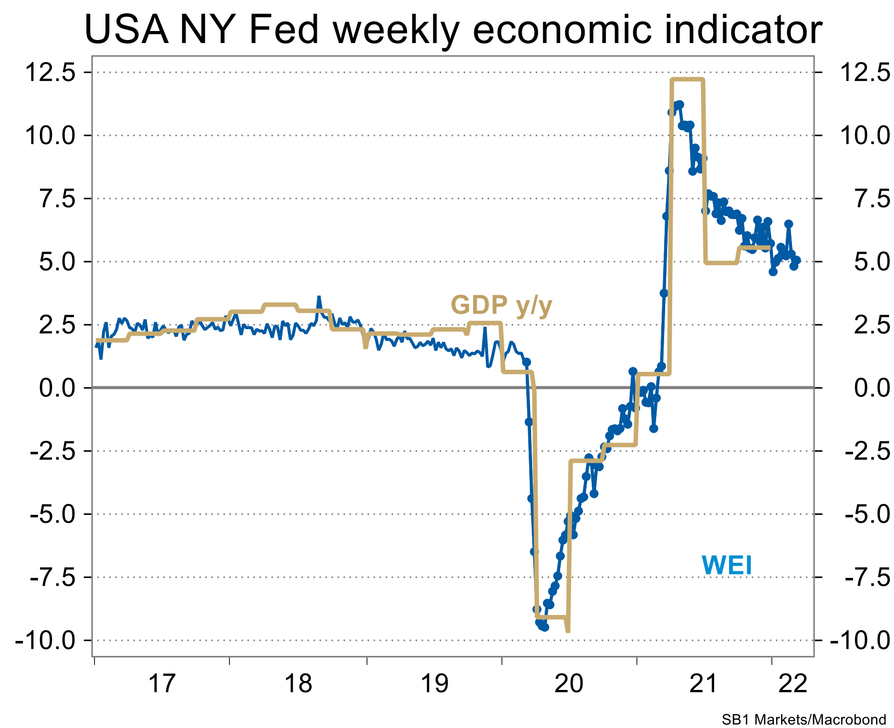


- The contrast to Atlanta Fed's nowcaster is unusual, check next page for the nowcaster

Atlanta Fed's nowcaster suggests 0.5% growth in Q1

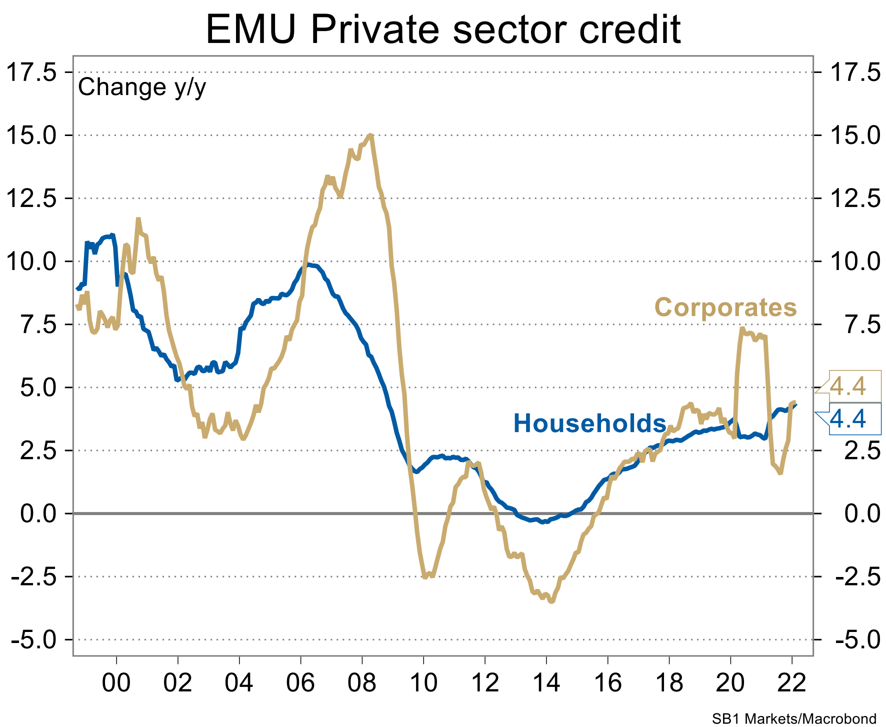
Net trade & inventories contributes at the downside, according to Atlanta Fed

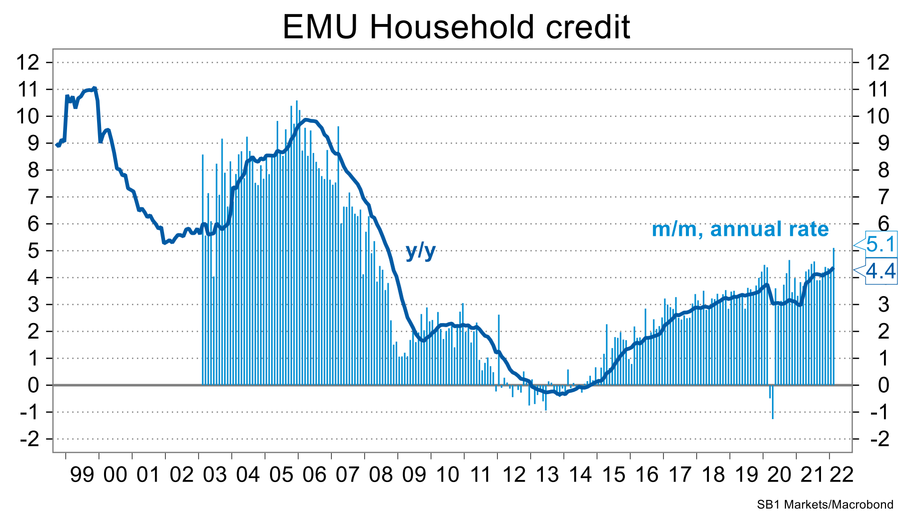


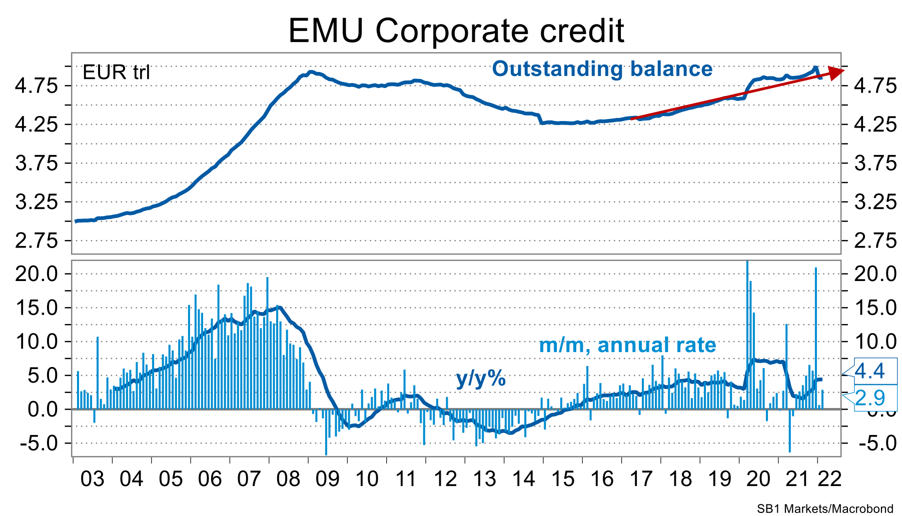


Credit growth is slowly accelerating, at least household debt

But no credit boom to be seen, growth rates still at 4.4% for both sectors





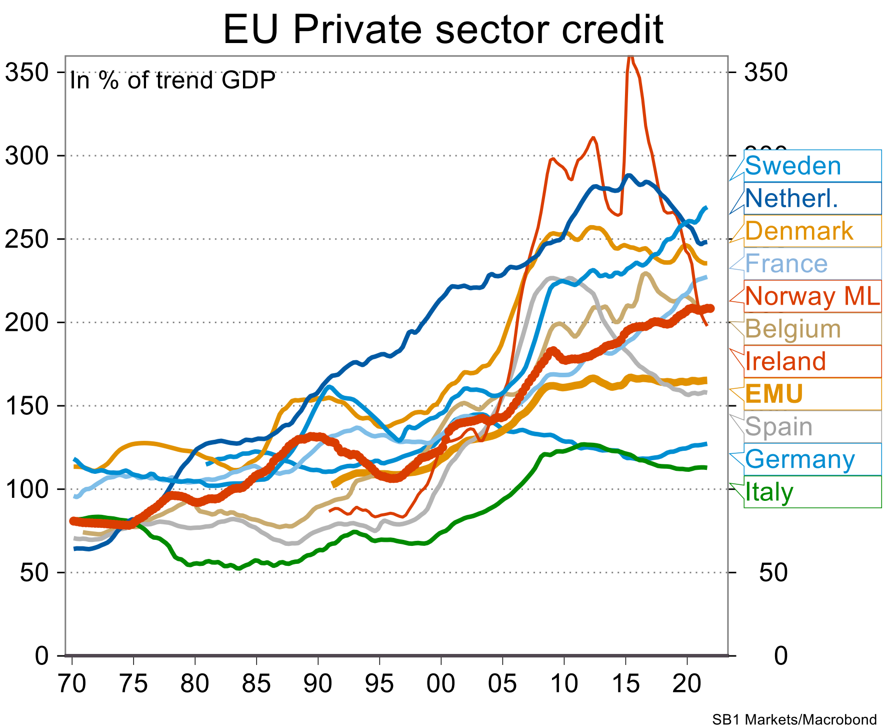


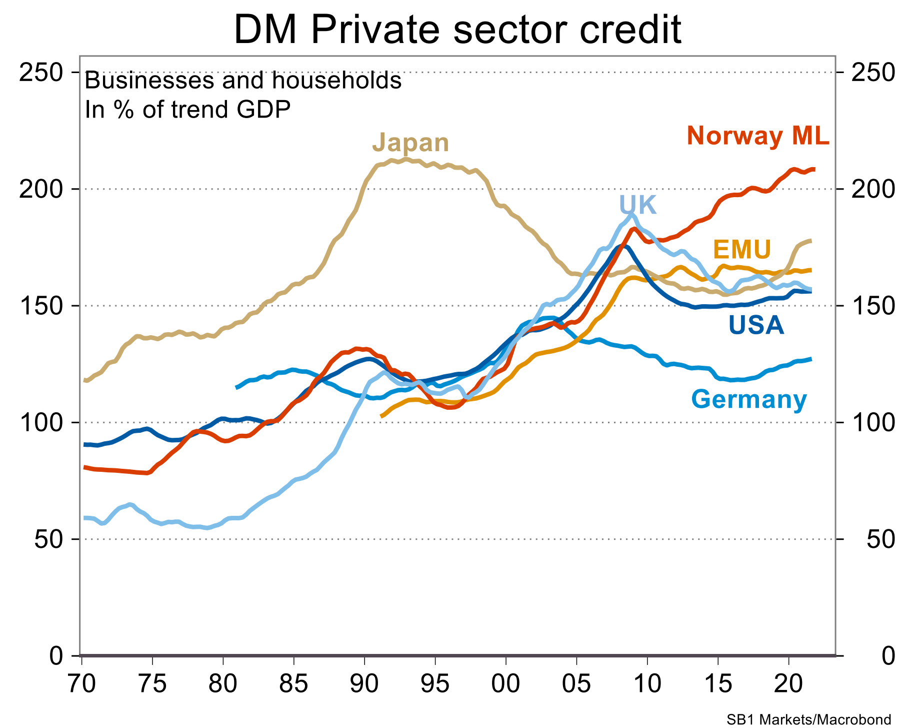
- The corporate debt level is back to the pre-pandemic trend growth path,
  - The credit volume is not higher than in 2008 in nominal terms – and sharply down in real terms or in % of GDP

SpareBank 1 MARKETS

The private sector has mostly been deleveraging since the Financial crisis

… and credit growth has been moderate during the pandemic, at least most places

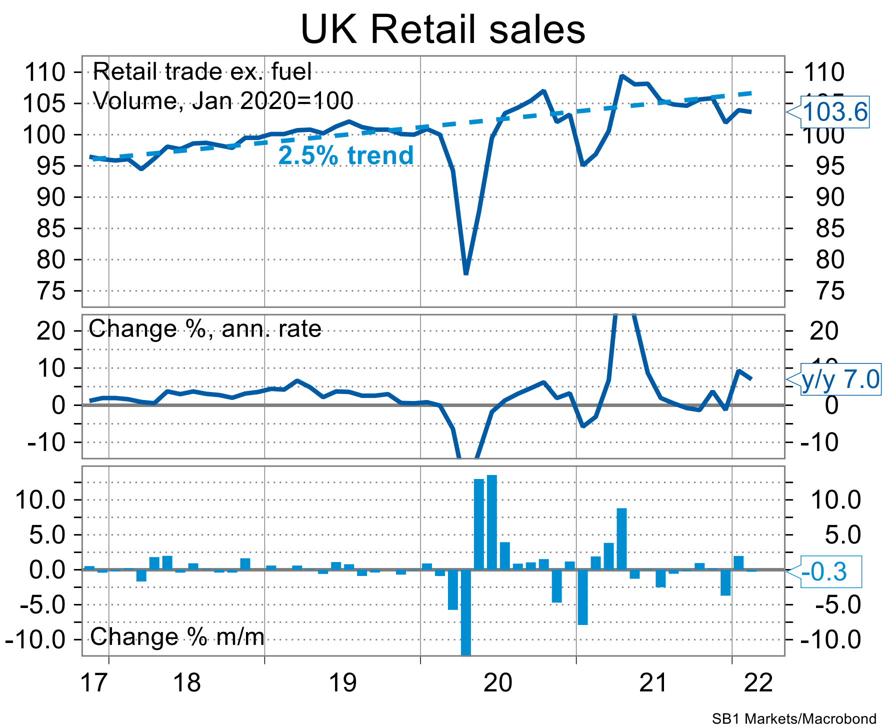


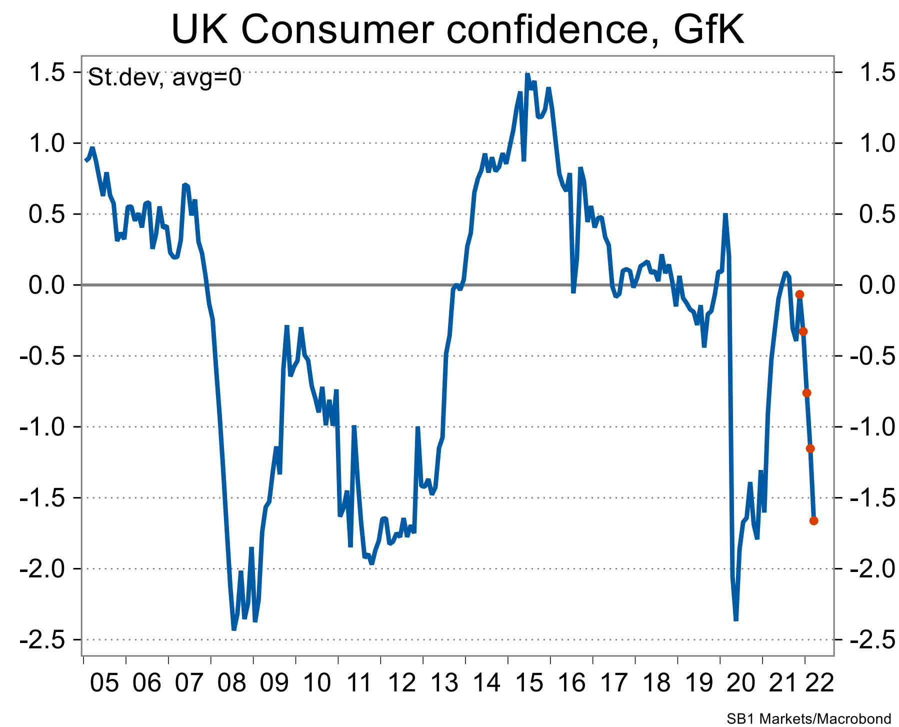


SpareBank 1 MARKETS

Retail sales are heading down, consumer confidence is falling rapidly

Sales down 0.3%, expected up 0.7%. Sales have fallen since November, and will decline in Q1

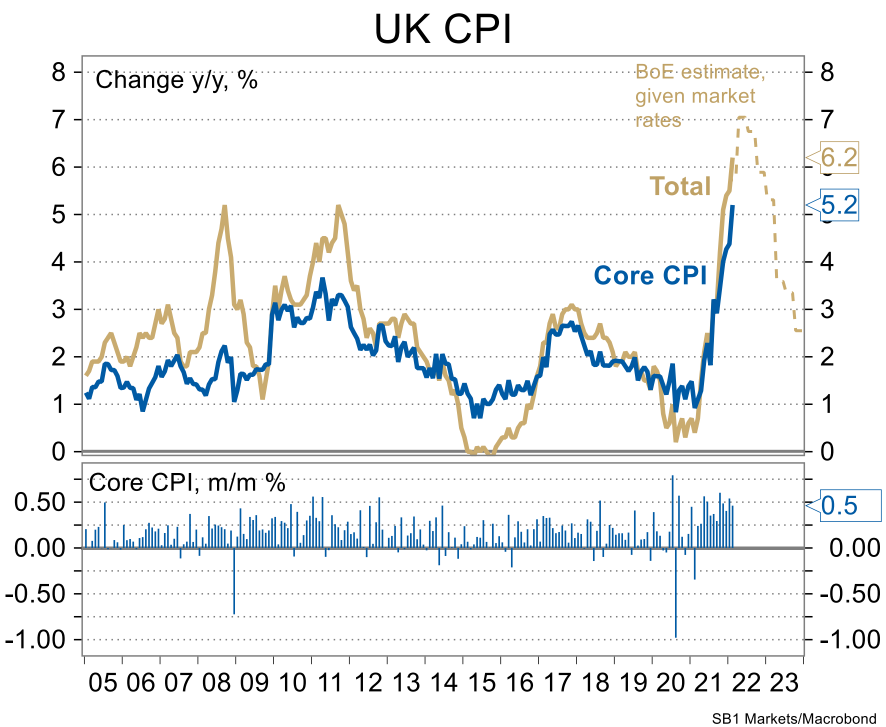


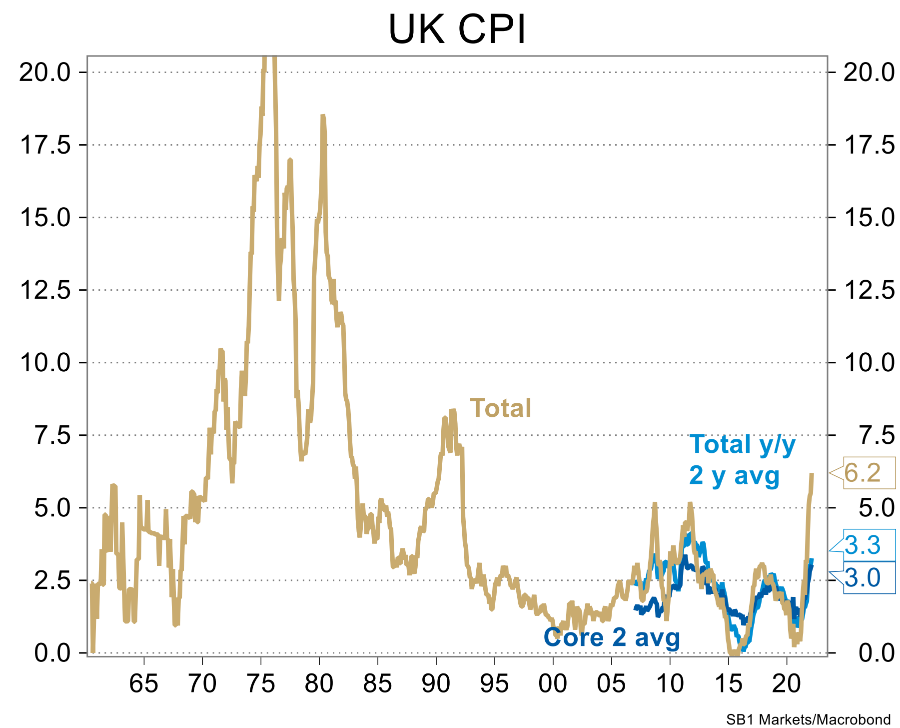


- **Retail sales** peaked last April, and the gradual decline brought sales down to well below the pre-pandemic 2.5% growth path. The Omicron wave hampered sales in December but sales remained low in both Jan & Feb, even if all restriction were lifted. Inflation is running high, and real incomes are declining
- **Consumer confidence** has fallen sharply since November (the first red dot at the chart to the right, at an average level), down to -1.2 st.dev below average in February and further down to 1.7 st.dev below in March. The decline in March may of course due to the war in Ukraine, but something had happened before that
  - » High inflation and declining real wages may be one reason. Beside that, the labour market is strong, and the unemployment rate is low

Inflation up to 6.2%, the core to 5.2%, both 0.3 pp above expectations

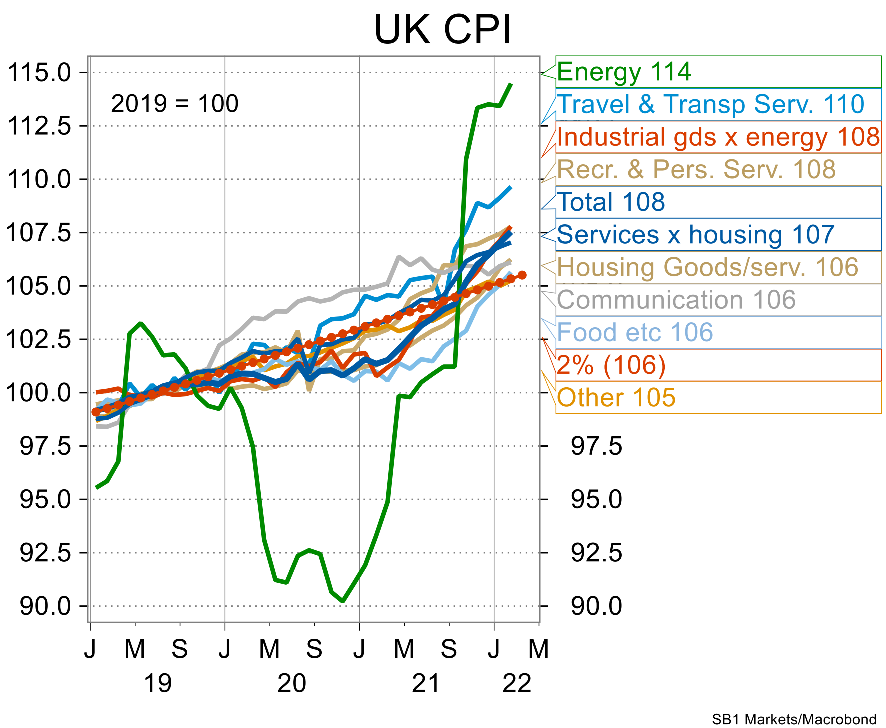
The core up 0.5% m/m, as is the 'new normal' these days

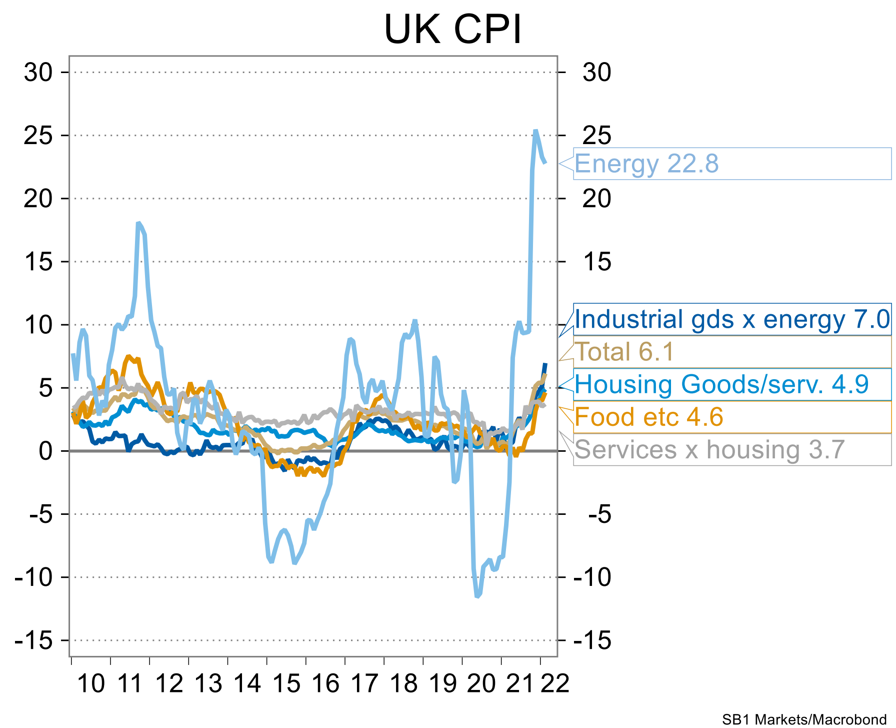




- **The total CPI** rose 0.5% m/m too. The annual rates are the highest since the early 1990'ies. Measured over the past 3m/3m the core index is up 6%
- **Measured over 2 years**, headline is up 3.3%, and the core is up 3.0%, which illustrates the base effects on the present much higher y/y rates. Still, 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…

Energy a culprit but many prices are accelerating

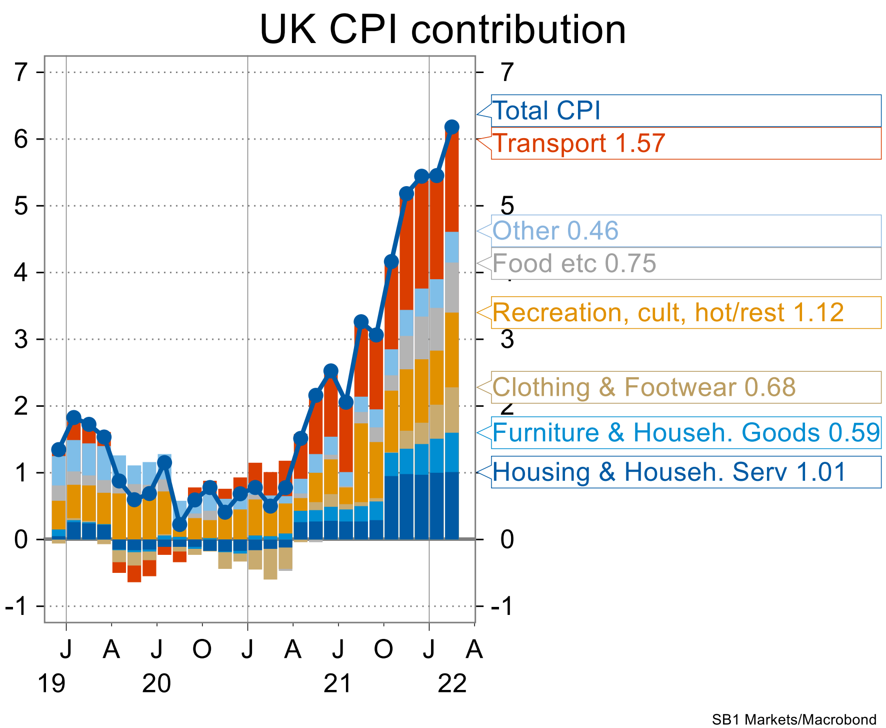




- **Energy prices** are up 23% y/y, rather modest vs. the lift in spot gas and electricity prices. Gas prices are regulated in UK, with caps

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

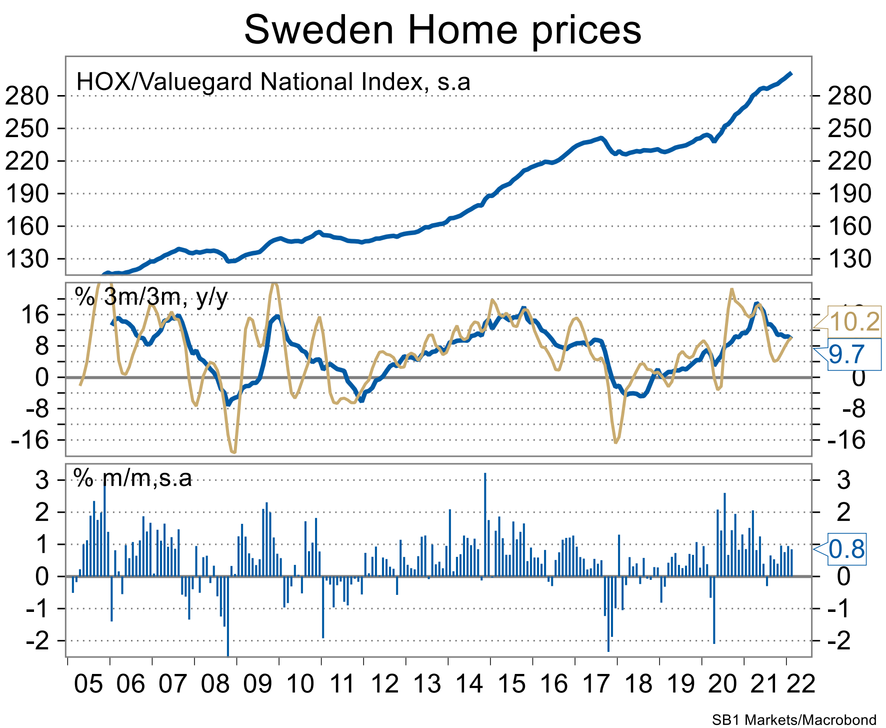
Within transport and housing, the energy component is the main culprit. But….

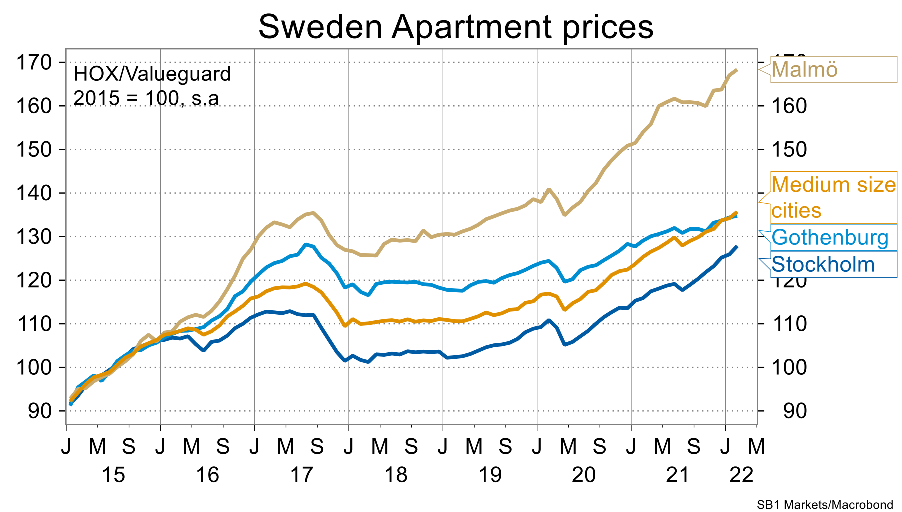


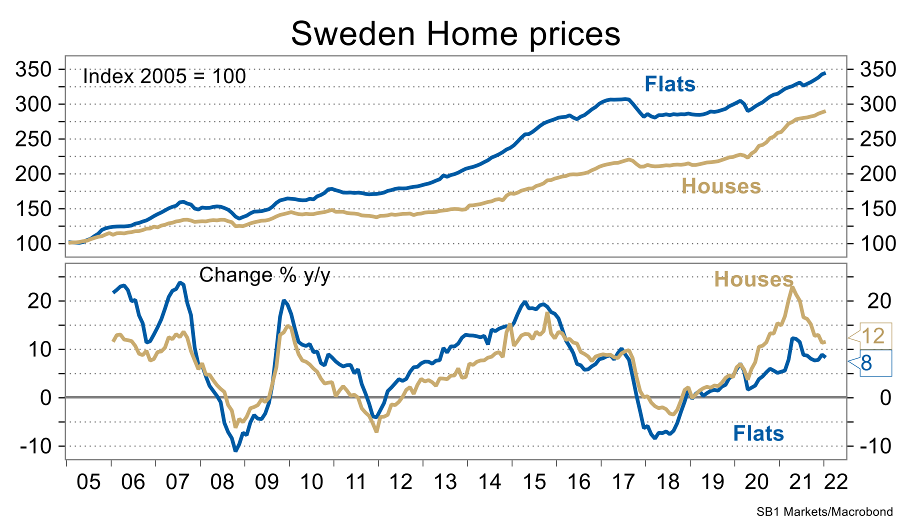
- Other sectors are reporting higher inflation too

Swedish house prices are accelerating again, prices up 0.8% m/m in February

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



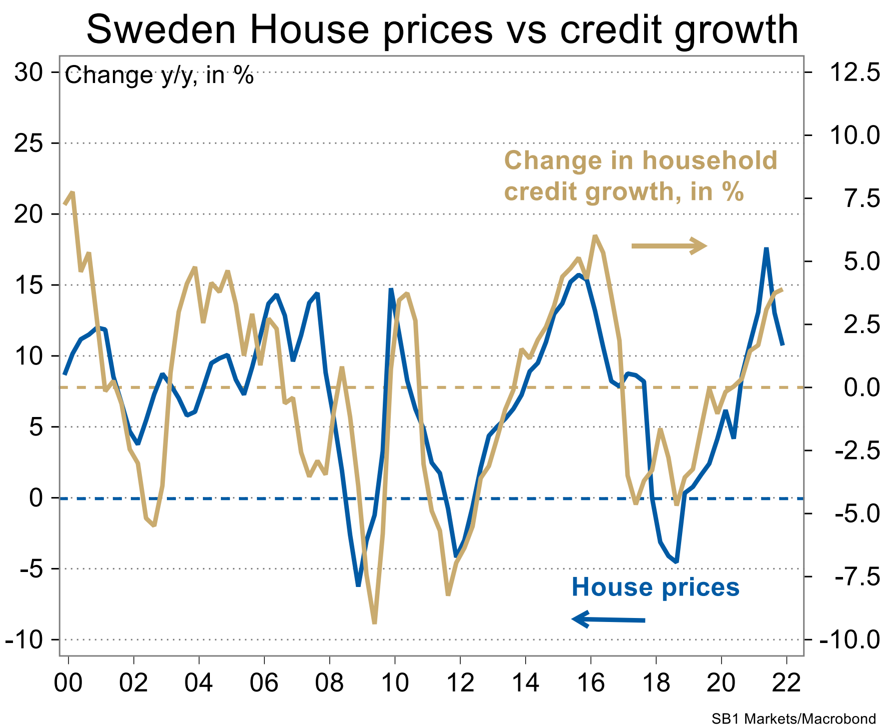


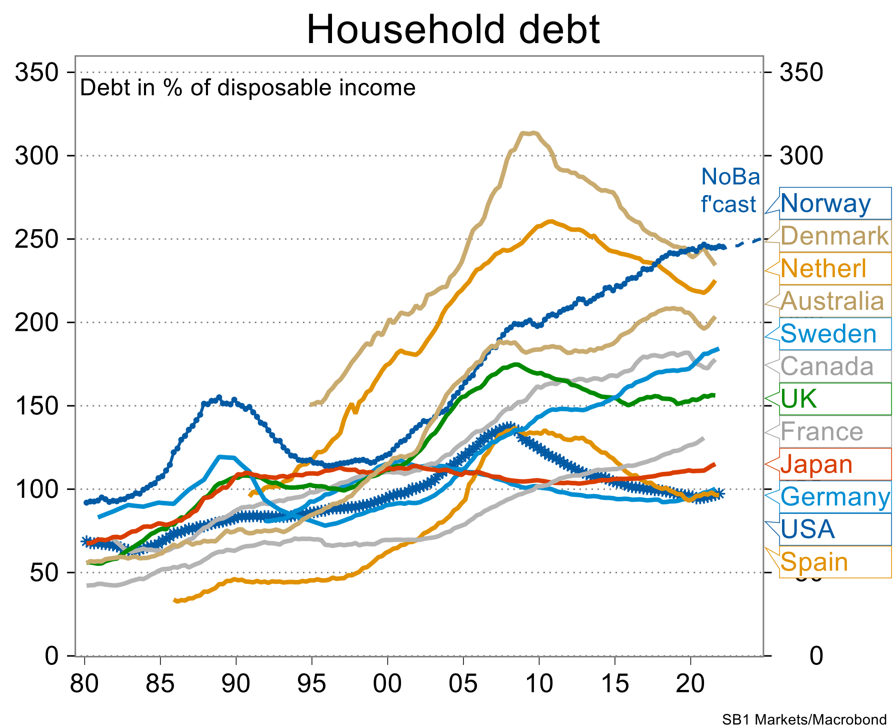


- The annual price inflation slowed 0.7 pp to 9.7% in February, and the trend is downwards – but price inflation is of course way above income growth
  - » The underlying price growth (3m/3m) has gained speed the past 4 months, and is at 10%, from 4% in October
- Malmö has reported a rapid price appreciation since October but price are drifting upwards in the all three main city regions
- From the peak, house price inflation has slowed more than flat prices, reversing some of the opposite movement last year but houses are still up 12% y/y, flats 8%

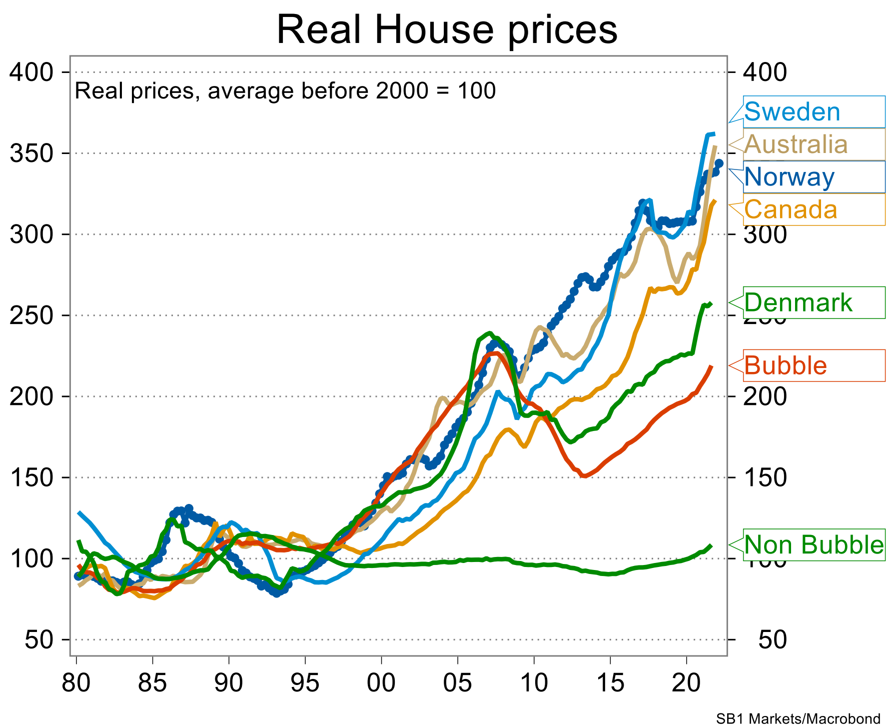
Credit growth is accelerating rapidly – and will for still a while

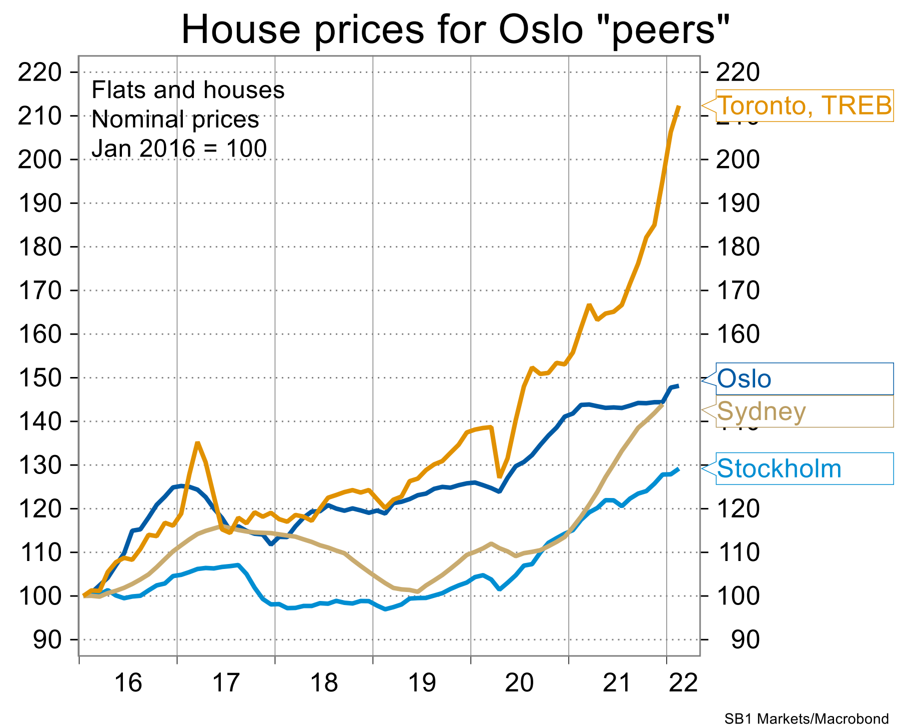
… and more than in most other rich countries, without cuts in (record low) mortgage rates





House prices have been on the way up during the pandemic

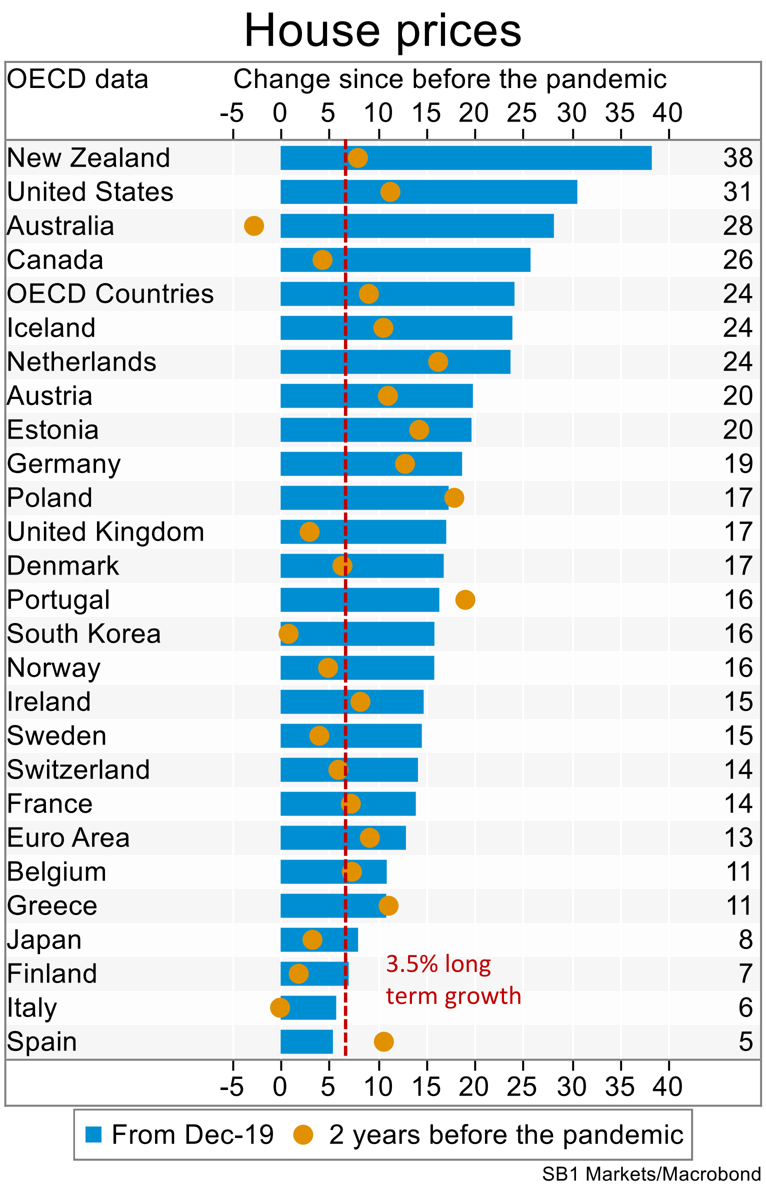




- Real house prices are at high levels in both Australia, Canada, Norway, and Sweden
- Home prices in the capitals in these countries are mixed recent months, as Oslo and Toronto have taken a break – but Sydney is probably still on the way up
- Other countries are following, like Denmark, New Zealand, US (check next page)

At the chart to the left: Bubble: US, UK, Spain, Netherlands, Ireland and several others. Non-bubble: Germany, Japan and some few others

House prices up everywhere, and have accelerated in 22 of 26 countries



Sweden (and Norway) not on the top of the list

- In average, house prices in the OECD area have appreciated by 24% since before the pandemic (Q4-19 to Q4 21)
  - » In the two years before the pandemic, prices rose 9%, or by 4.5% per year
  - » Long term, house prices may appreciate marginally more than inflation
- New Zealand, US, Australia & Canada is at the top of the list
- Spain has seen the largest deceleration since before the pandemic but prices are here too

OECD quarterly data, the last quarter Q2 or Q3-21

Highlights

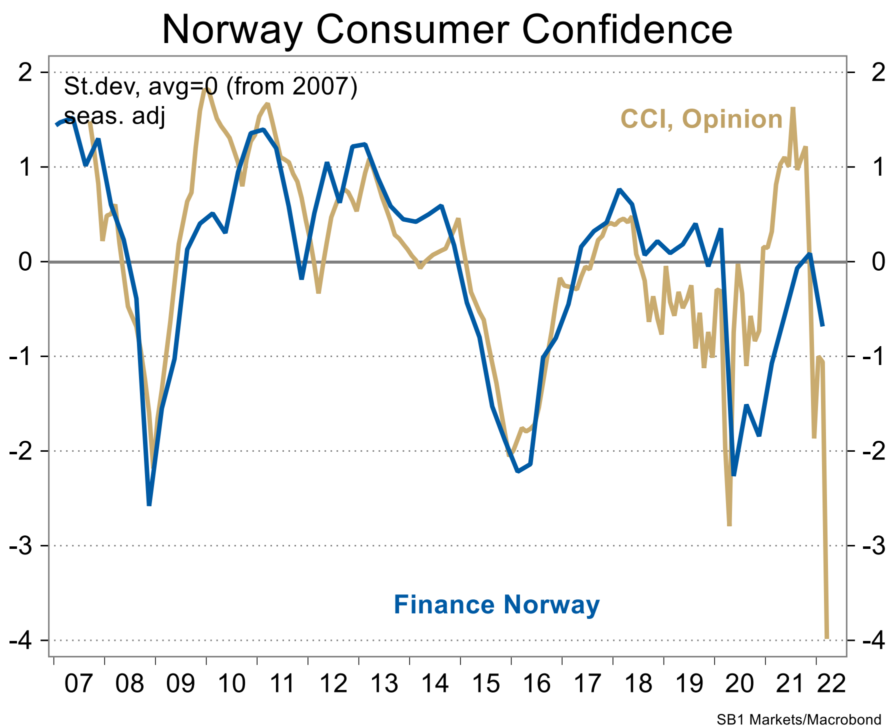
The world around us

The Norwegian economy

Market charts & comments

Consumer confidence collapsed in March, to ATL by far. Down 3 st.dev, to -4!!

There is just one possible explanation: The War

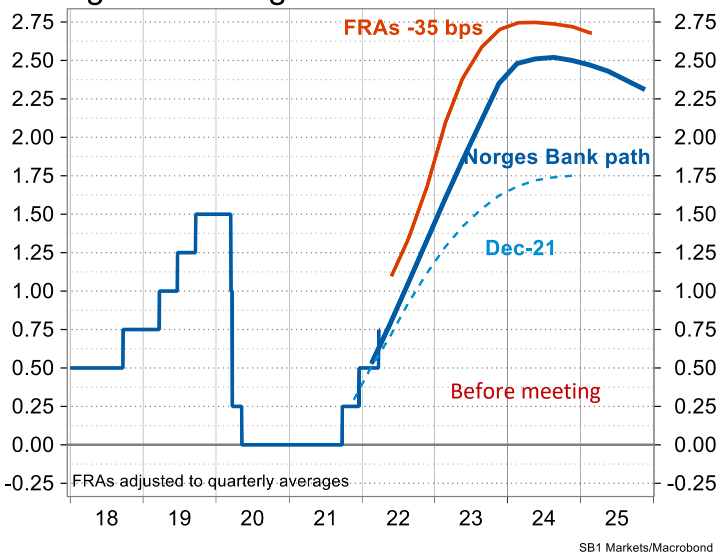


- **The decline in CCI** from Opinion was the largest one month drop ever, to the lowest lever ever – rather dramatic
- **The war in Ukraine** is the only news since the previous survey was conducted in March that can explain the unprecedented drop in confidence
  - » **Fear of higher inflation** – also present before the invasion – may also explain some the drop – and the level was well below average in both Dec, Jan & Feb, very likely due to the steep rise in electricity prices
  - » **Norges Bank's rate hike** last week – and the lift in the interest rate path – was announced after this survey was conducted
- Besides (exaggerated, most likely) fears of inflation, the economic situation is close to superb, strong growth in employment, low unemployment, low interest rates, a strong stock market, a stable housing market – and no more corona restrictions
- **Will consumption follow suit?** We doubt, and in no way at a scale suggested by the confidence index

NoBa delivered the 3rd hike, and the path was revised up more than ever before

… and thereafter FRA-rates rose even more, by up to 25 bps – and is up to 50 bps above the <u>new</u> path

Norges Bank Signal rate forecast vs market



Interest rate paths

	NoBa Path 4-21	NoBA Path 1-22	Change	Fair FRA *) @IMM, NB	FRA** pre-meet	FRA** now	NoBa - FRA now
Q1 22	0.51	***0.53***	***0.02***	1.24		-	
Q2 22	0.70	***0.78***	***0.08***	1.46	1.63	**1.63**	-0.17
Q3 22	0.92	***1.05***	***0.13***	1.68	1.89	**1.97**	-0.29
Q4 22	1.11	***1.32***	***0.21***	1.90	2.25	**2.38**	-0.48
Q1 23	1.28	***1.59***	***0.31***	2.16	2.53	**2.70**	-0.54
Q2 23	1.42	***1.85***	***0.43***	2.41	2.71	**2.92**	-0.51
Q3 23	1.53	***2.10***	***0.57***	2.66	2.81	**3.04**	-0.38
Q4 23	1.62	***2.35***	***0.73***	2.81	2.85	**3.08**	-0.27
Q1 24	1.68	***2.48***	***0.80***	2.86	2.86	**3.10**	-0.24
Q2 24	1.72	***2.51***	***0.79***	2.87	2.85	**3.09**	-0.22
Q3 24	1.74	***2.52***	***0.78***	2.85	2.83	**3.07**	-0.22
Q4 24	1.75	***2.50***	***0.75***	2.82	2.79	**3.03**	-0.20
Q1 25		***2.47***		2.79	2.79	**3.02**	-0.23
Q2 25		***2.43***		2.73			
Q3 25		***2.37***		2.32			
Q4 25		***2.31***		2.26			

**) Assuming the NIBOR spread gradually down to 35 from Q1-23, vs 50 bps in Q2*

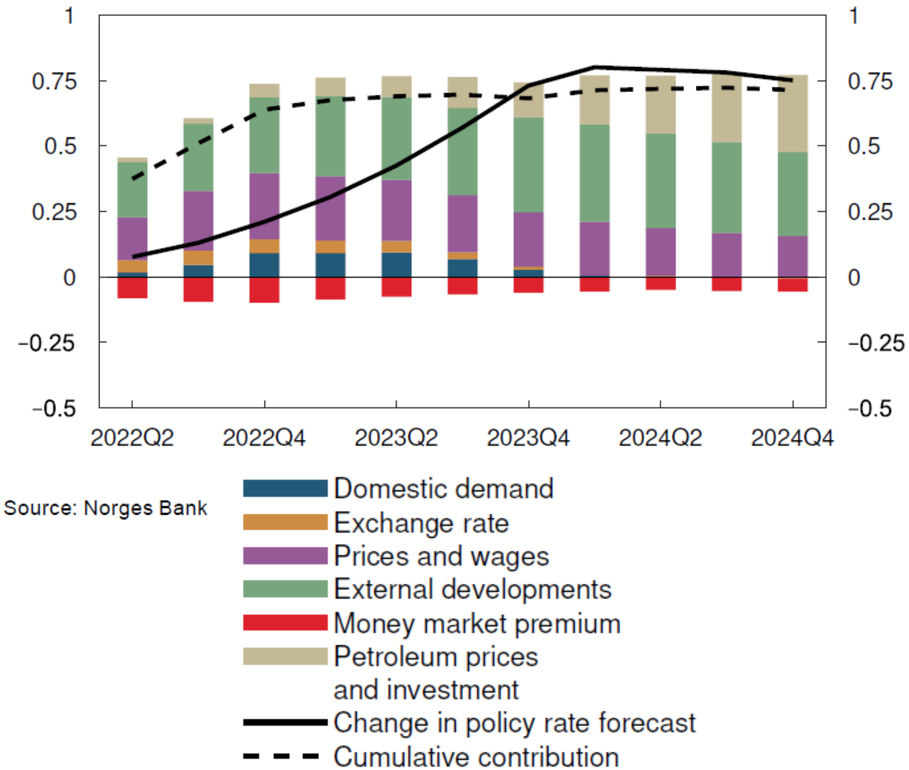
**) Q4 FRAs adjusted for liquidity prem

- **The signal (deposit)** was hiked by 25 bps, as expected
- **The policy rate path** was revised by up to 80 bps, an unprecedented quarterly change. The peak was lifted to 2.5% from 1.75% in the Dec MPR. We assumed a 50-bps lift, and a peak at 2.25%. Consensus was probably for something less than our f'cast
  - » However, our sum of the part analysis, based on expected changes in NoBa's forecasts but before deduction for 'adjustment and risk' signalled a 90 bps increase in the interest rate path
- The change in the interest rate path was the largest ever, by far. Higher interest rates abroad, the oil price, higher capacity utilisation, and significantly higher price- and wage inflation expectations contributed at the upside. Just an upward revision of the expected NIBOR spread contributed at the downside (see more next page).
- The Bank assumes core inflation will remain above the 2% target as long as the eye can see. At the same time, the output gap will remain positive too. NoBa defend its position by stating that high employment/low unemployment makes it worth 'breaking' the inflation target at the upside (STRATEGINOTATET)
- The new path implies 3 more hikes in 2022, with a 25% probability for a 4th hike, 4 hikes in 2023 (if 3 more in 2022), and the last hike to 2.25% in 2024. The next hike is supposed to be decided at the June meeting
  - » The new interest rate path implies that monetary policy will turn moderately restrictive from Q3 2023 as the signal rate will be lifted to above the assumed neutral rate at 1.75%
- **NoBa's new interest rate path was up to 35 bps below the FRA market (given a 35 bps NIBOR spread from Q4). Even so, FRAs rose sharply at Thursday and Friday, by 7 – 24 bps. The market discounts 5 more hikes in 2022 (vs. 3 in NoBa's main scenario). At the most, market expectations are 54 bps above NoBa's path (Q1-23), and they are signalling a 2.75% policy rate peak, 25 bps above NoBa's path**

Reasons for the rate path lift: Everything, except a wider NIBOR spread

The Banks data driven models argued for a 50-bps hike, and 4 more hikes in ‘22 (in sum ‘6’ ‘22 hikes)

Chart 4.8 A number of factors pull up the rate path
Cumulative contribution. Percentage points



Source: Norges Bank

Our pre-meeting forecast was pretty close to the outcome until mid 2023 but thereafter NoBa was slightly more aggressive!

Upside contributions:

- Foreign rate expectations (-lower growth expectations, war & sanctions)
- Wage and cost inflation was revised sharply
- Domestic Mainland demand
- Petroleum prices, investments
- Even the NOK, even if the NOK has strengthened (but less than suggested by petroleum prices

Downside contributions:

- Just a higher spread between NIBOR rates and the policy rate

The board’s (unprecedented) adjustment

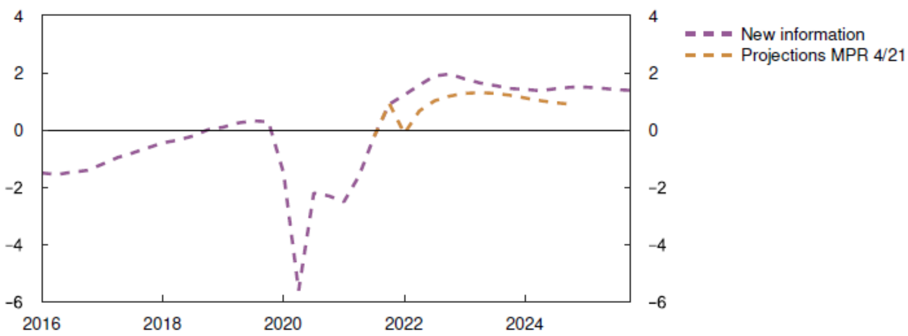
- The data driven model suggested a 50-bps hike at this junction, and a lift in the interest path by 64 bps in Q4-22. The MPC decided to lift the path by ‘just’ 21 bps, a 43-bps discrepancy. We have never seen such a gap between ‘data’ and ‘policy’
- The MPC still wanted to take a gradual approach as it is unsure how heavily indebted households will react to higher mortgage rates. Uncertainty regarding impacts of the war/sanctions also suggest more measured rate hikes, than the actual situation in the economy suggests

Higher capacity utilisation & higher CPI inflation

… and the inflation is assumed to stay above the target the in the whole forecast period (through ‘25)

Chart 4.3 Prospects for higher capacity utilisation

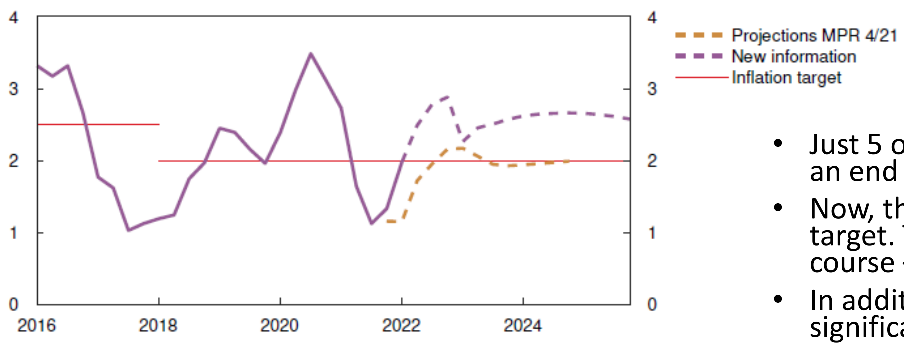
Estimated output gap. Conditioned on new information concerning economic developments and the policy rate forecast in MPR 4/21. Percent



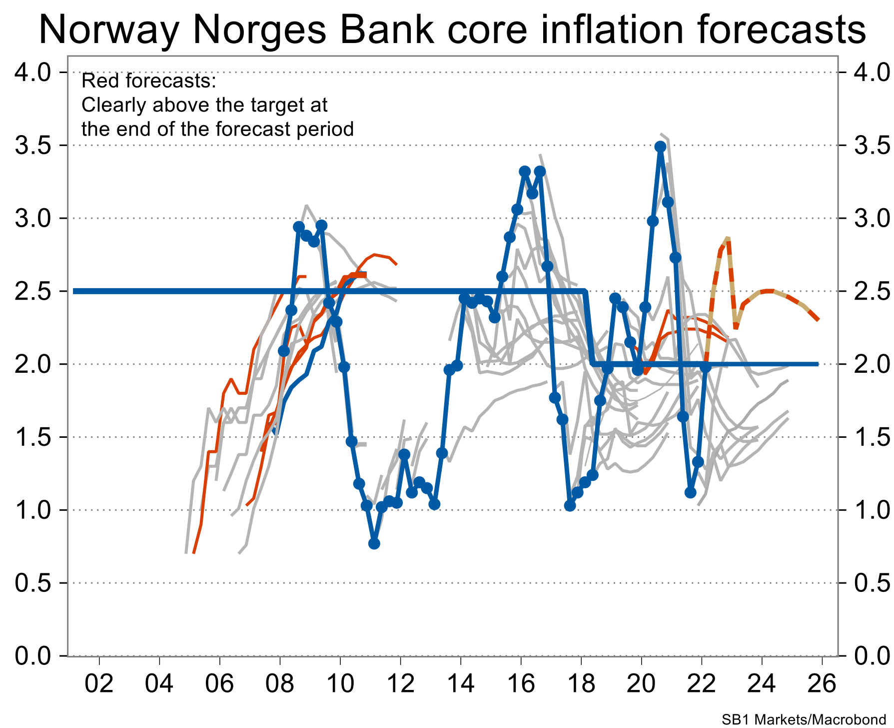
Source: Norges Bank

Chart 4.4 Prospects for higher inflation

CPI-ATE. Projections conditioned on new information concerning economic developments and the policy rate forecast in MPR 4/21. Four-quarter change. Percent



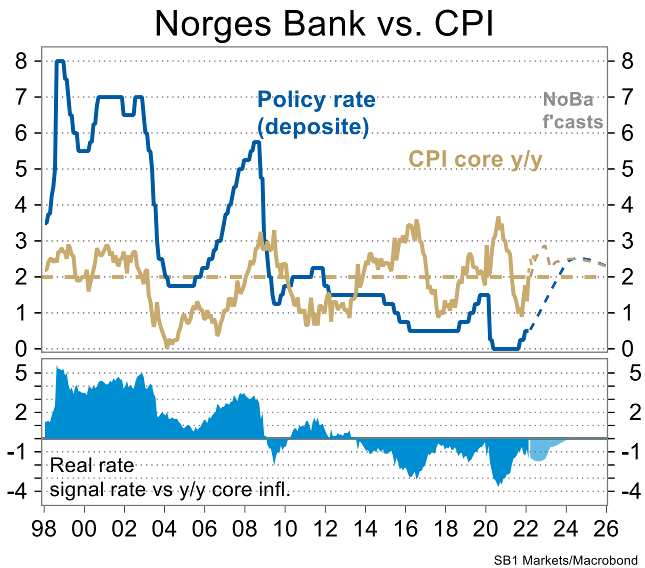
Sources: Statistics Norway and Norges Bank

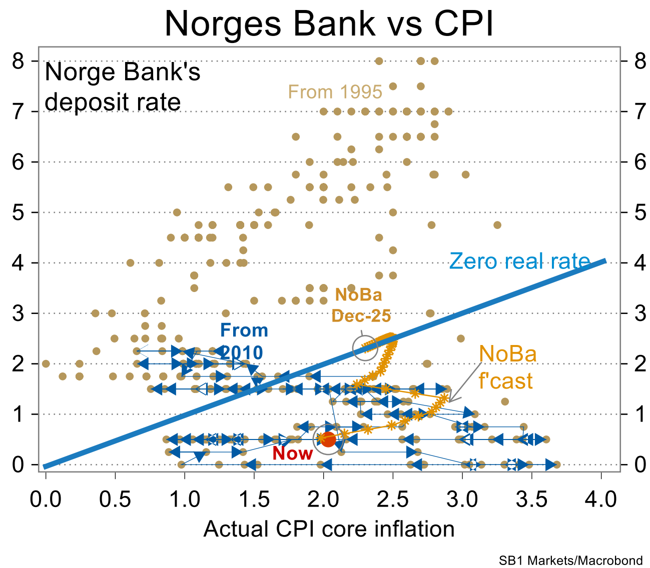


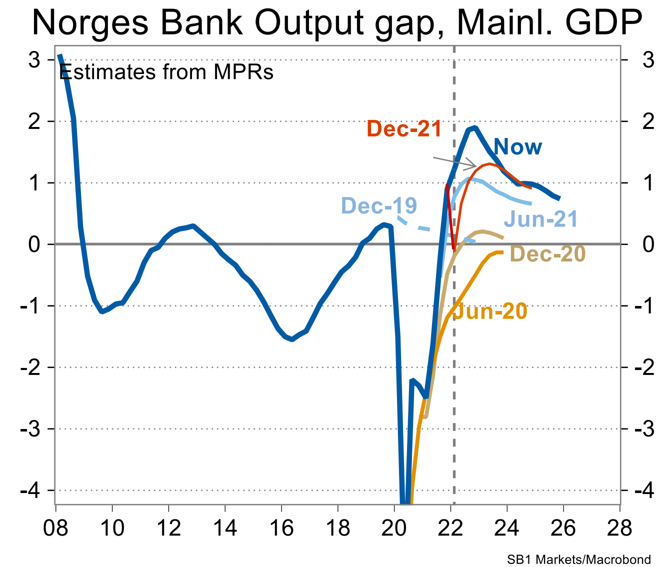
- Just 5 of the more than 60 inflation forecasts NoBa has publised since 2005 has had an end point above the inflation target at the time, and then by just 0.1 pp or 0.2 pp
- Now, the inflation forecast at the end of the forecast period is 0.3 pp above the target. The average miss is 0.4 pp (in sum 1.6 pp) – which is far from dramatic, of course – but still the highest average forecasted deviation ever
- In addition, the output gap was revised sharply up, and it is assumed to be significant above zero the coming 4 years. This mix is also unprecedented.
- **NoBa wants to let the economy run rather hot, even if it implies inflation marginally above target. However, should the labour market tighten further or wage inflation accelerate more than expected, more hikes are likely. And vice versa, of course**

More on the policy stance: The plan is to lift the real signal rate to zero

This time, rates are hiked because inflation is above target – and the output gap is positive

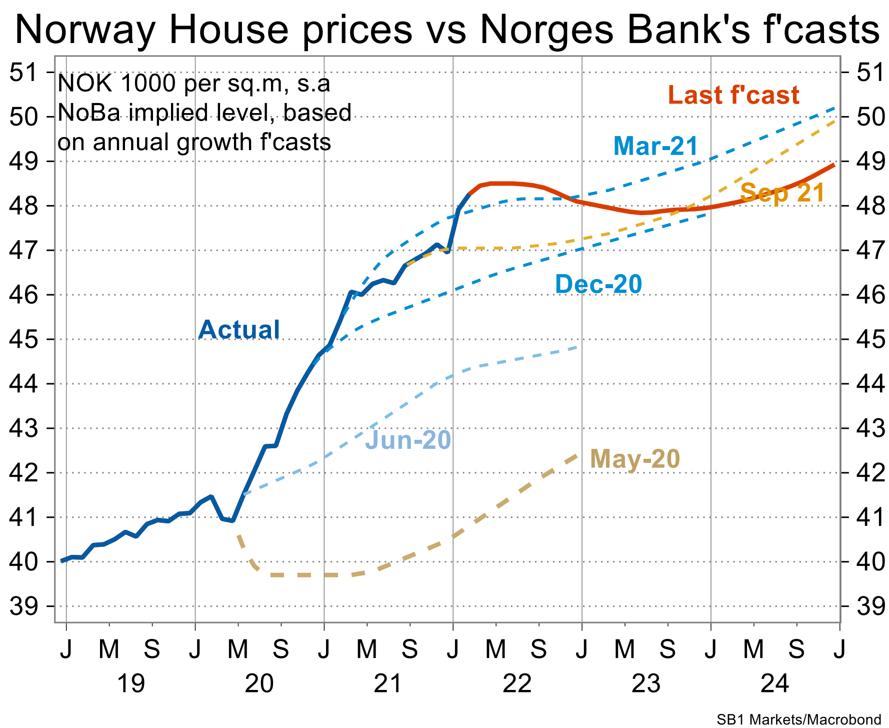






Norges Bank revised house prices up – and down. Exp. flat to Q3-24 from Q2-22

The starting point revised up due to price hikes in Jan/Feb, but then more rate hikes will start to bite?

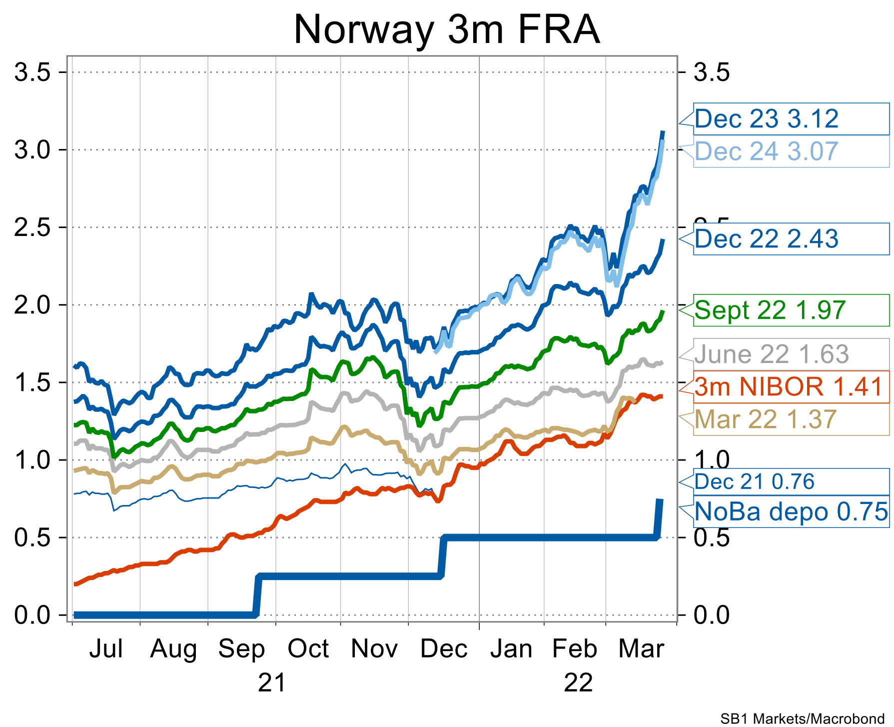


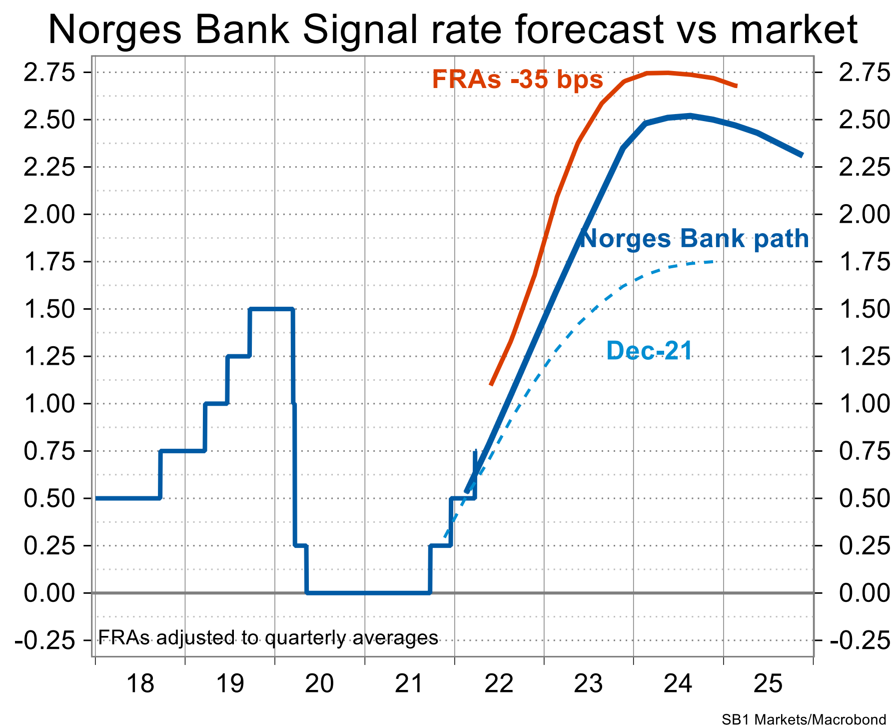
- NoBa expects house prices to appreciate less than income growth the coming years, at least until 2025, where interest rates are expected to be cut
- The bank expect house prices to turn down from Q2-22, and change tack upwards from Q3-23
- NoBa has published forecast all over the place since the beginning of the pandemic. And we to not blame the Bank!

- Prices are assumed to be below the Dec forecast from Q1-23 onwards

FRAs climbed after NoBa's message, to even further above the new path

It seem unreasonable to assume that markets discounts an even higher NIBOR spread

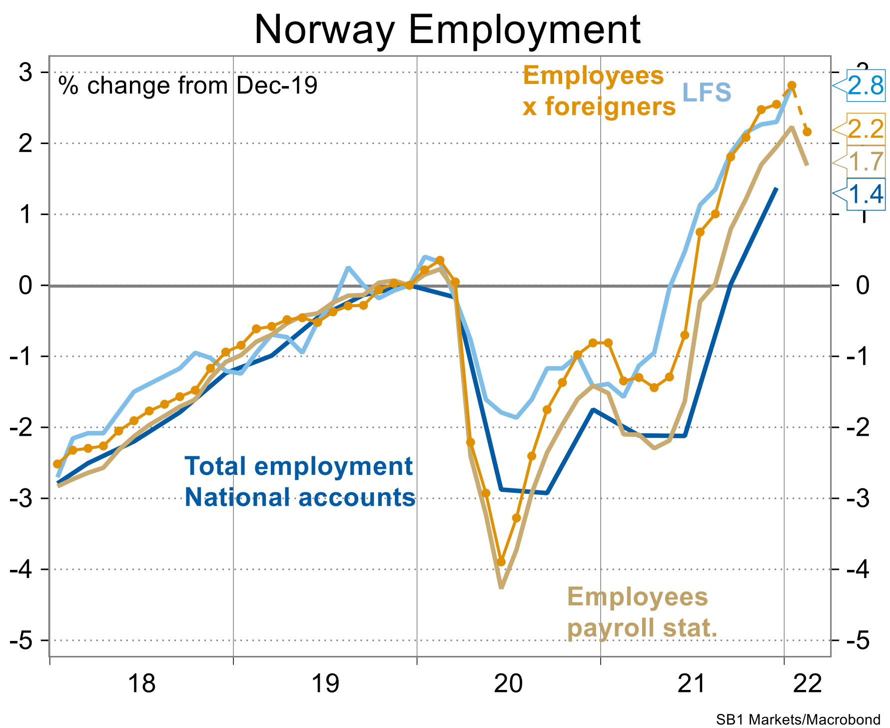




- … so these rate **expectations are 'the real thing'** – expectations of a more aggressive Norges Bank

Payrolls cut by 0.5% in (mid) February, we expected a further growth

The no. of employees is still up 1.7% vs Feb-20. The LFS report further growth in total employment

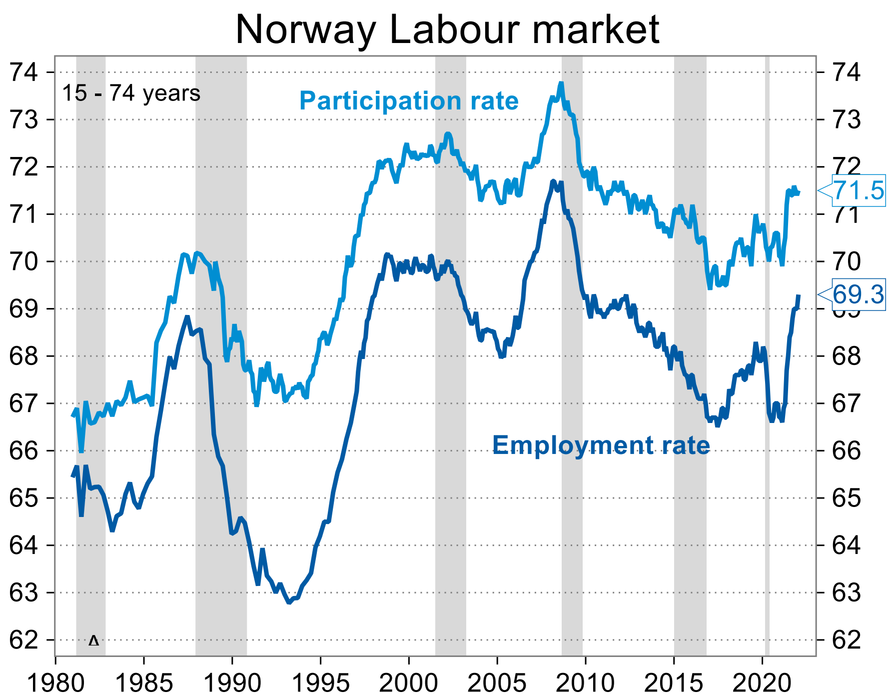


- The 14’ decrease in the **register-based no. of employees** to mid Feb from mid January was a surprise
- We expect employment growth to slow due to lack of available labour, not due to lack of demand

- **The LFS** (‘AKU’ survey) employment data (both employees and self-employed, with permanent residency in Norway) reported a 14’ (0.4%) growth in employment in Jan (avg Dec-Feb from avg Nov – Jan), and by a 2.6% pace over the past 3 months
  - » LFS employment is up 2.8% since before the pandemic, and both participation and employment rates are far above the pre-pandemic level – and the LFS unemployment rate has ‘collapsed’, now to 3.2%
- **National Accounts** reported a 1.4% growth in total employment in Q4 (5.5% annualised) – and the level is up 1.4% vs. Q4-19. These NA data includes foreigners on short-term stay

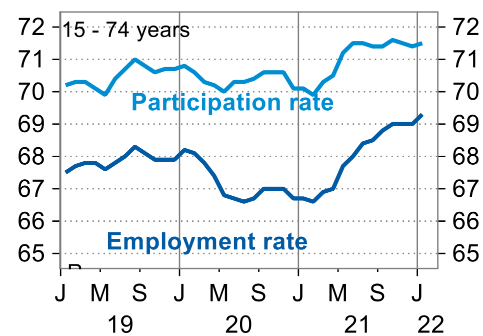
The participation rate has flattened since last summer

No further lift since last summer signals that the reserve is already engaged, no spare capacity left



SB1 Markets/Macrobond

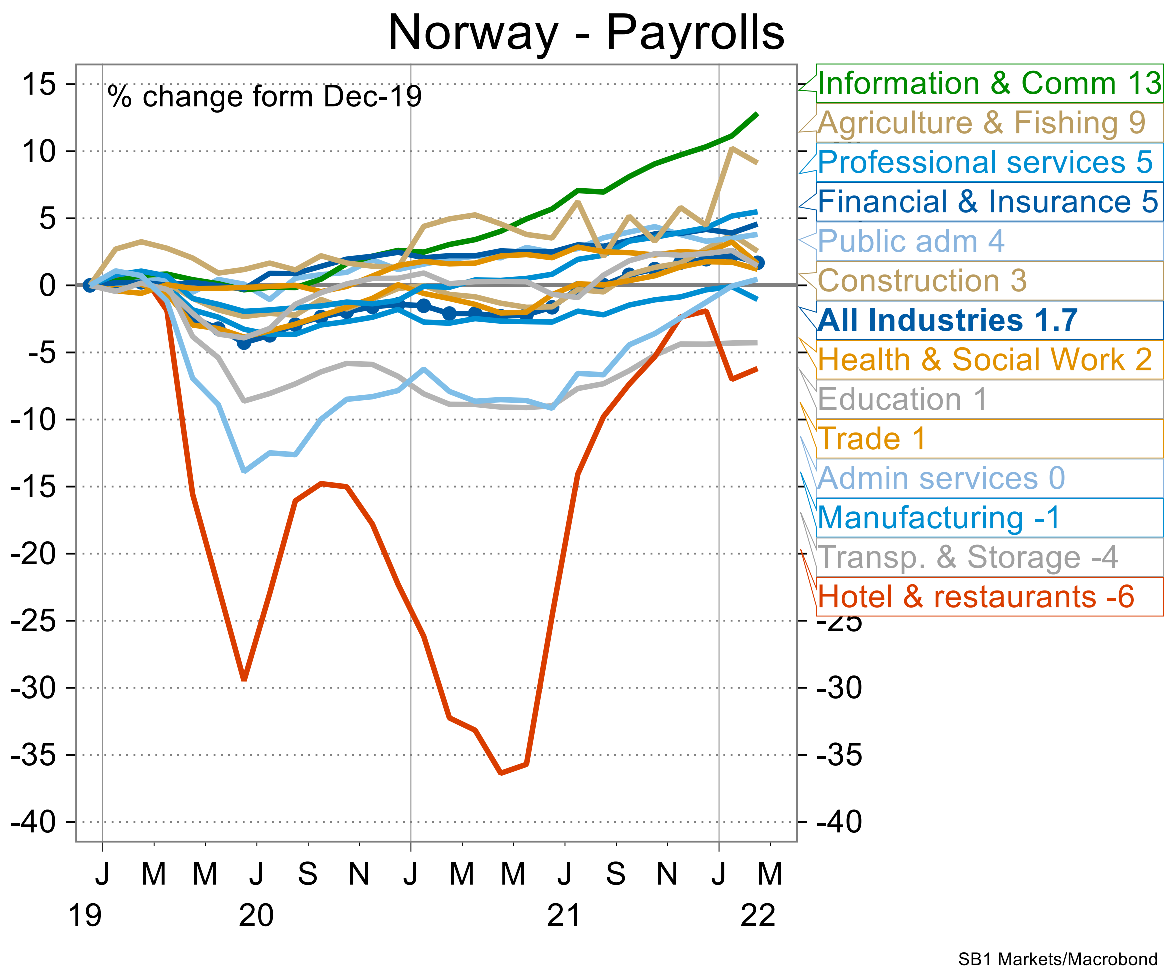
- **The employment rate** rose 0.3 pp to 69.3% in Jan
  - » Ahead of the pandemic the rate was 68.1 – 68.2, and it is up from the 66.4 through in early 2021 (and from the same level in 2017, after the 'oil crisis'). The employment rate is measured in % of the working age 15 - 74 y population
  - » The employment rate is the highest since 2012
- **The participation rate** gained 0.1 pp to 71.5% in Jan. This rate has been flat since last summer – at the highest level since 2012
- These monthly data are volatile but the flattening of the participation rate since the early summer even if demand for labour is still increasing <u>may indicate that the easy part of 're-engagement' is behind us</u>
- **Working age population** growth is 0.6% over the last year (Q4 est), in line with the moderate growth ahead of the pandemic

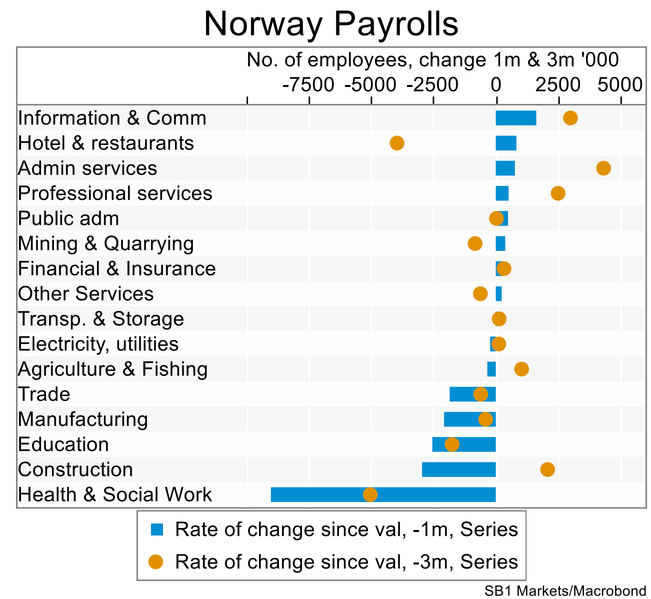


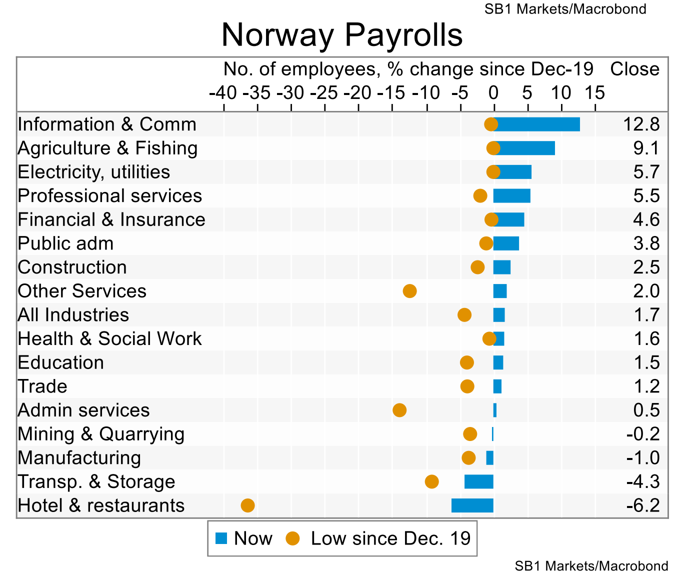
SB1 Markets/Macrobond

Public sector contributed at the downside in February (education & health)

Surely not a new trend! We expect payrolls to increase again in March – especially in hotels & rest!



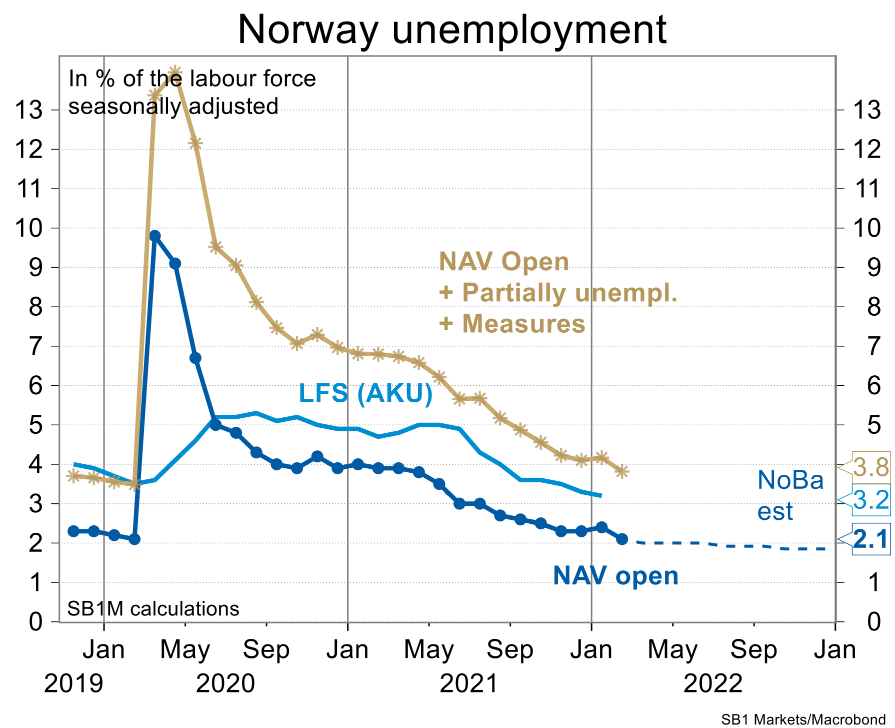


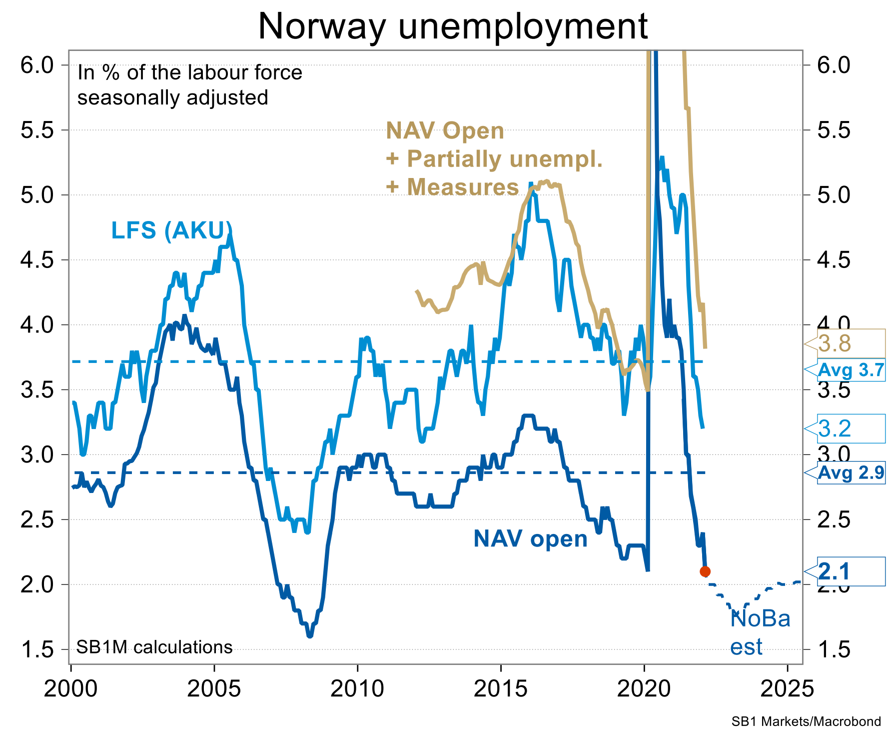


SpareBank 1 MARKETS

LFS unemployment down to 3.2% - to below the pre-pandemic level

Norges Bank revised its NAV unemployment forecast down last week, to 1.8% at the bottom



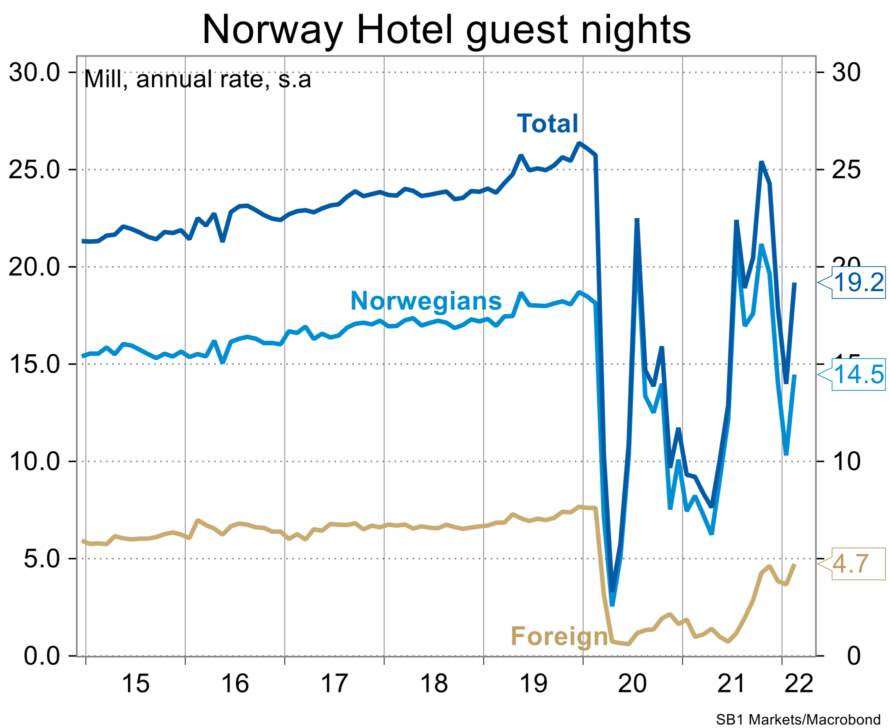


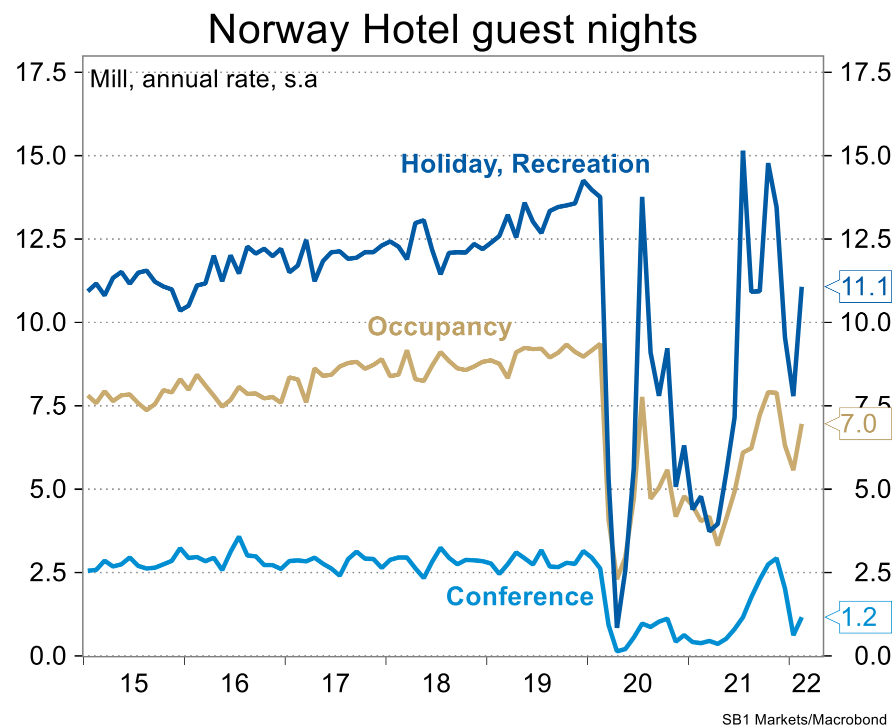
- However, given the speed of decline so far, 1.8% is not be that far away, check the chart to the left
- **The LFS (AKU) unemployment rate** fell 0.1 pp to 3.2% in Jan (Dec-Feb avg), from 3.3% a month earlier – expected unchanged (we expected 3.2%). The level is well below the 3.7% average

SpareBank 1 MARKETS

More hotel guest nights in February – and March will be even better

Almost half of the decline in no. of guest nights in Dec/Jan was reversed in February





- **The no. of guest nights** will very likely recover further in March

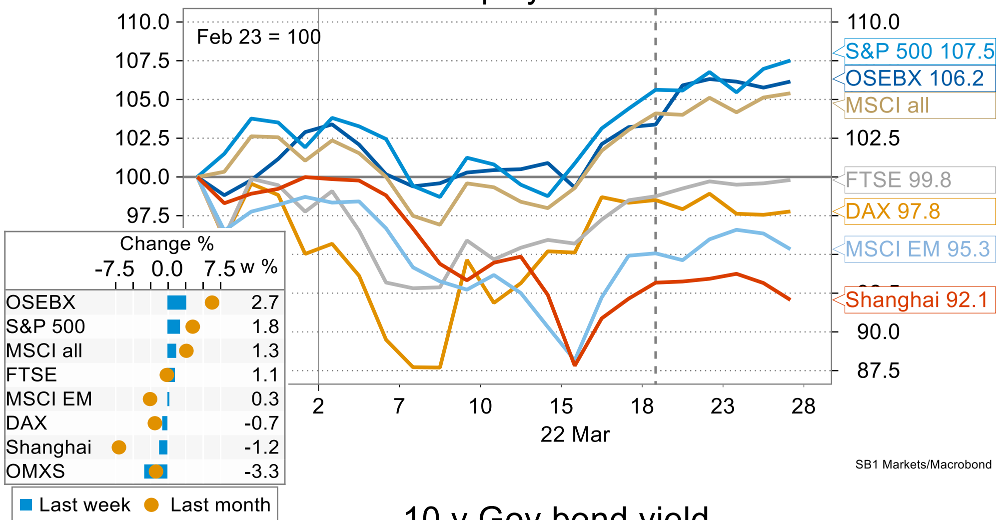
SpareBank 1 MARKETS

SpareBank 1 MARKETS

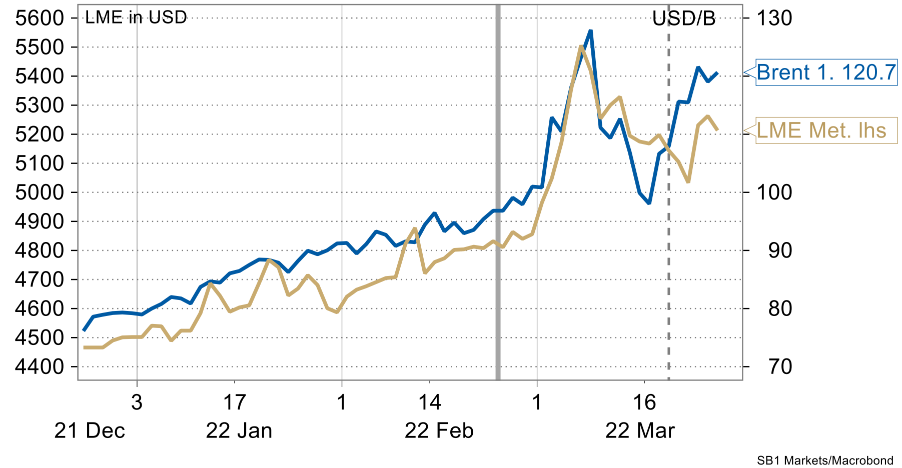
Most equity markets up, bond yields are surging, oil/metals up too

And NOK won the currency lottery last week (if we do not include the rouble)

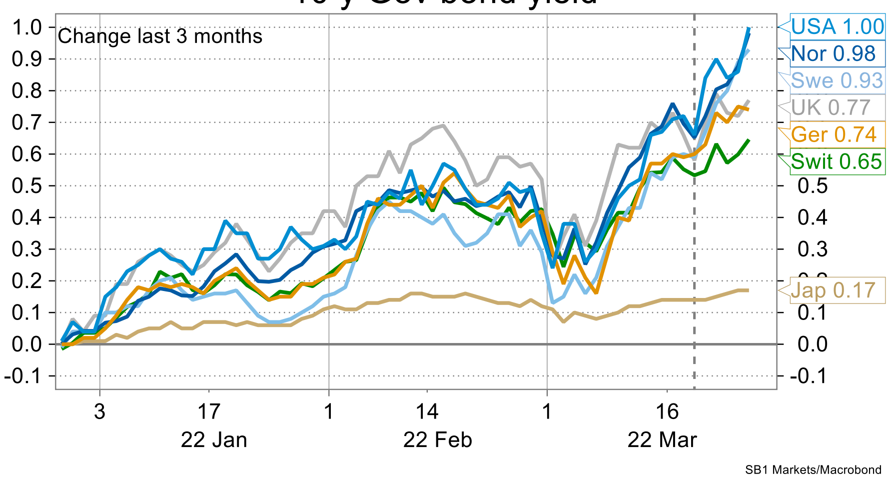
Equity Indices



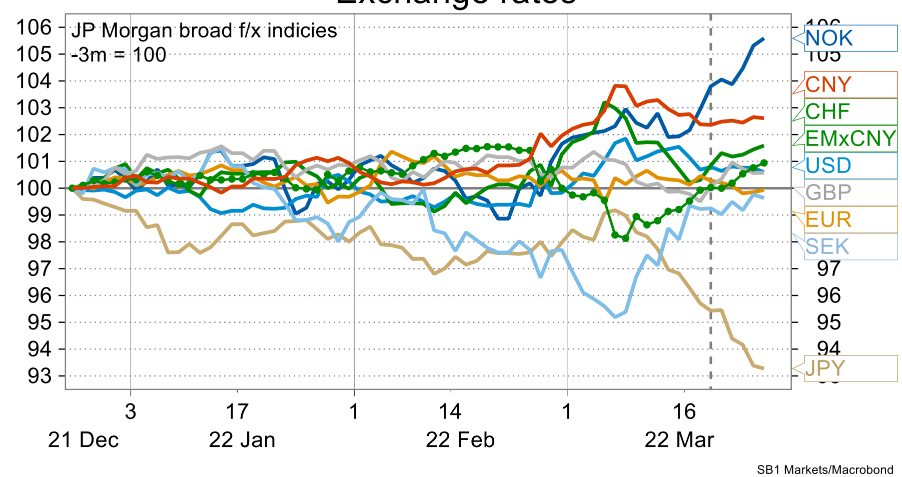
Oil vs. metals



10 y Gov bond yield

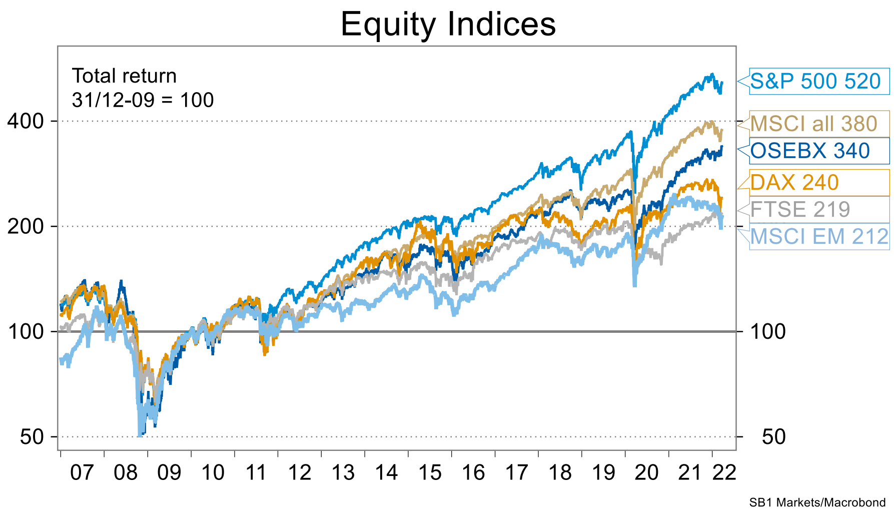


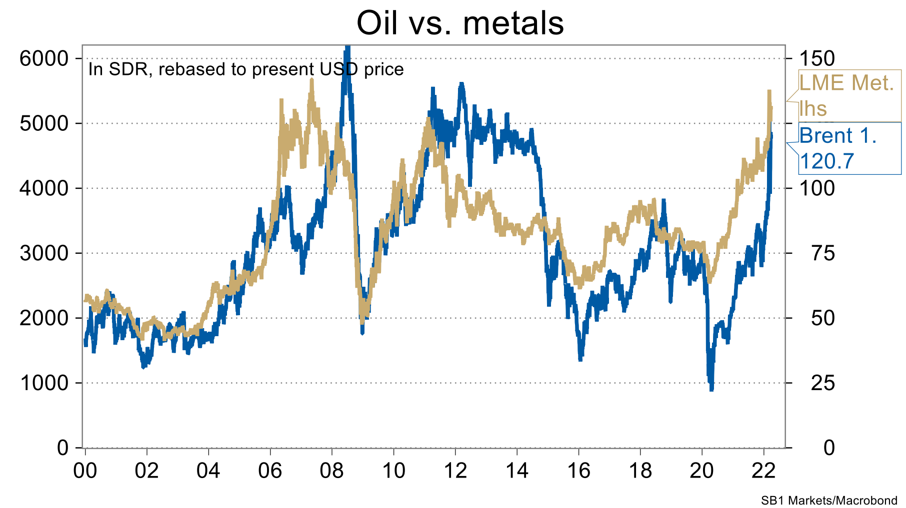
Exchange rates

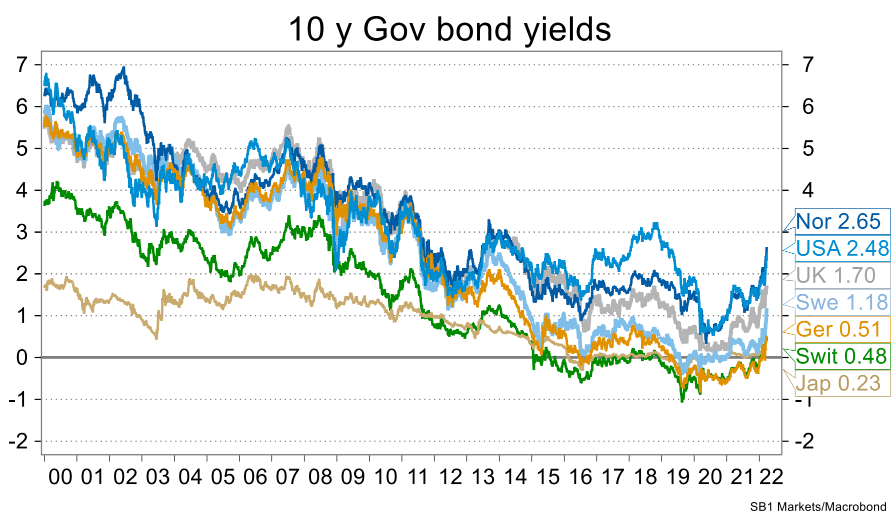


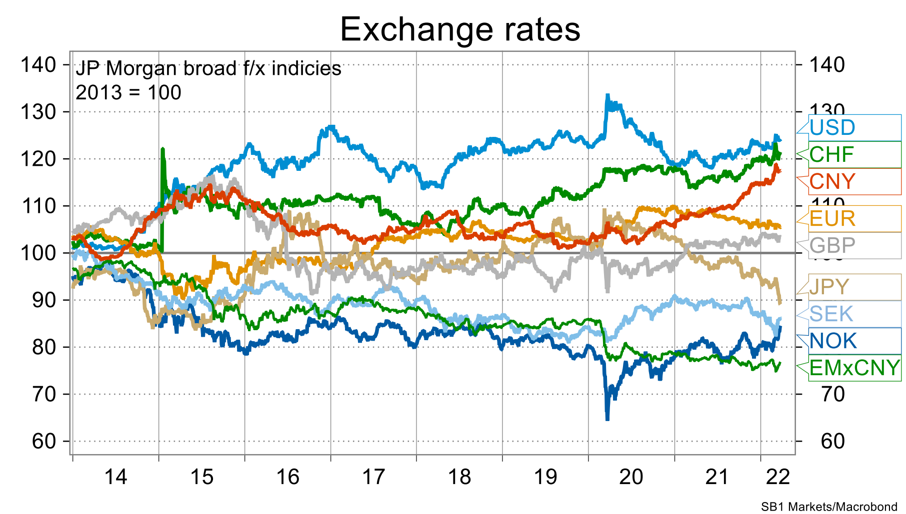
The big picture: Stock markets down, bond yields up

Commodities have taken a big step upwards





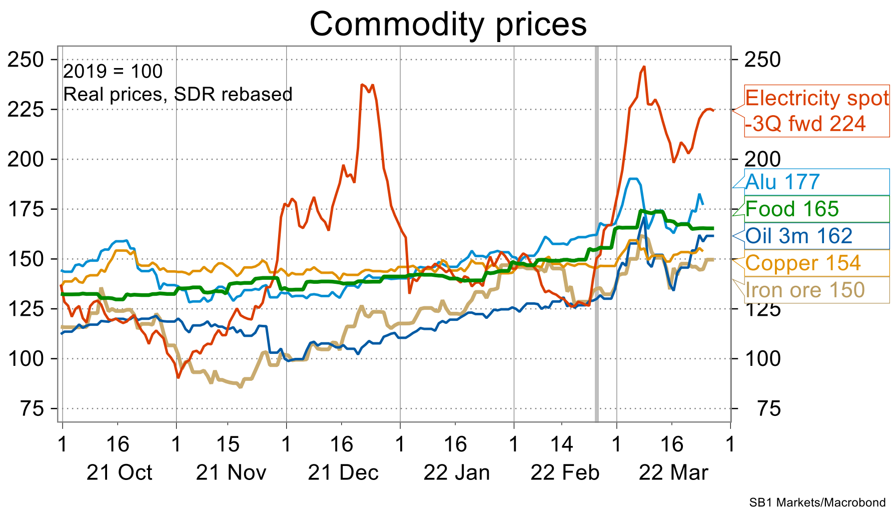


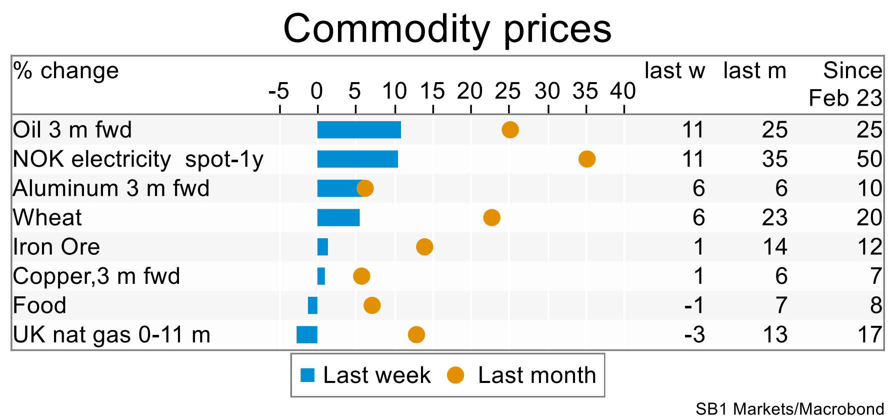


SpareBank 1 MARKETS

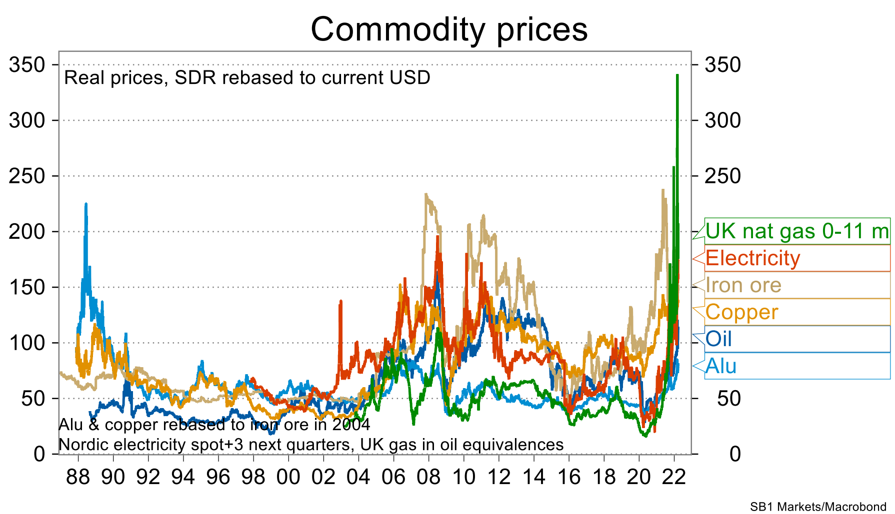
Mixed commodity prices last week following 2 week's decline

Food prices fell for the 3rd week in row. Less hoarding? All prices are up since before the invasion





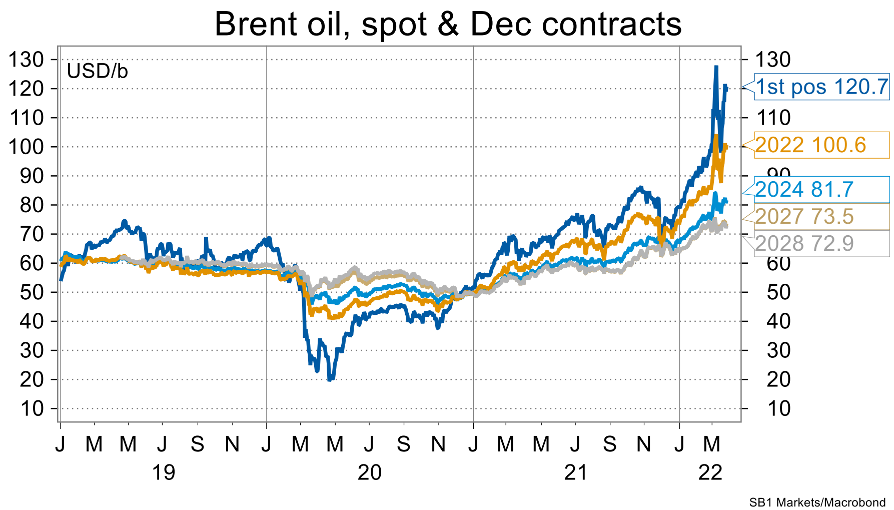
% change	last w	last m	Since Feb 23
Oil 3 m fwd	11	25	25
NOK electricity spot-1y	11	35	50
Aluminum 3 m fwd	6	6	10
Wheat	6	23	20
Iron Ore	1	14	12
Copper,3 m fwd	1	6	7
Food	-1	7	8
UK nat gas 0-11 m	-3	13	17

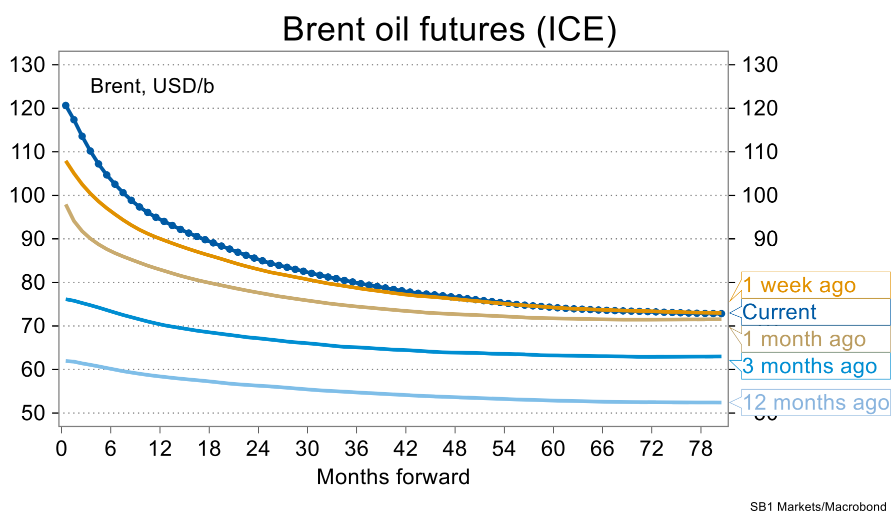


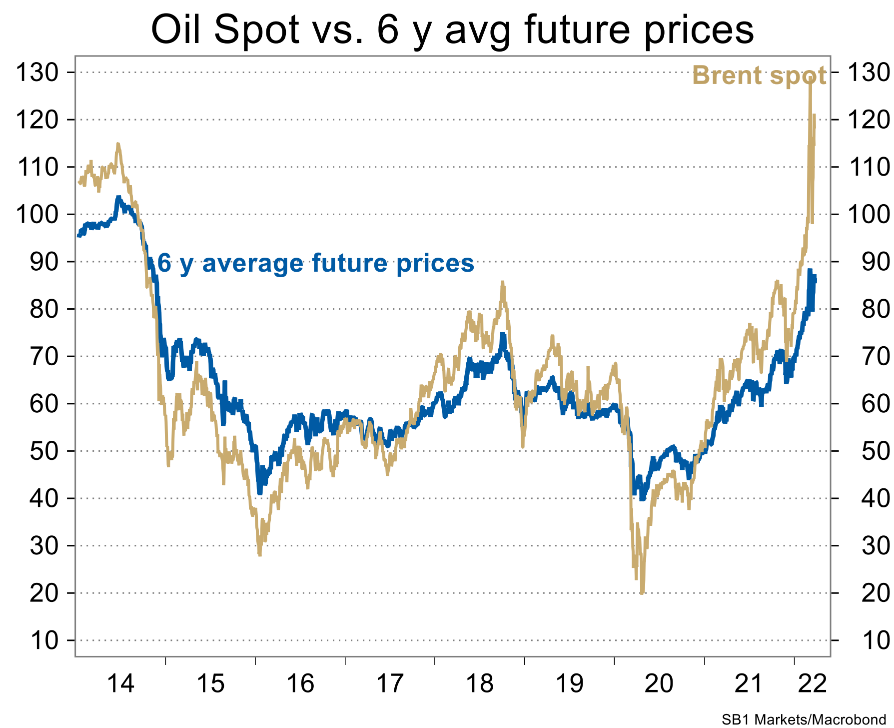
- Will **Russia be allowed to export** oil and gas, will buyers abroad buy the stuff or will **Russia turn the tap off**?
  - » There seems to be willing buyers of rebated Russian oil
  - » Russia is still pushing gas through the pipelines to Europe
- Will Russia/Ukraine sell grain – restrictions are introduced (as for many other goods)?

The oil price is still volatile – up to above USD 120 last week

Future prices have been much more stable than the short end of the curve – as usual



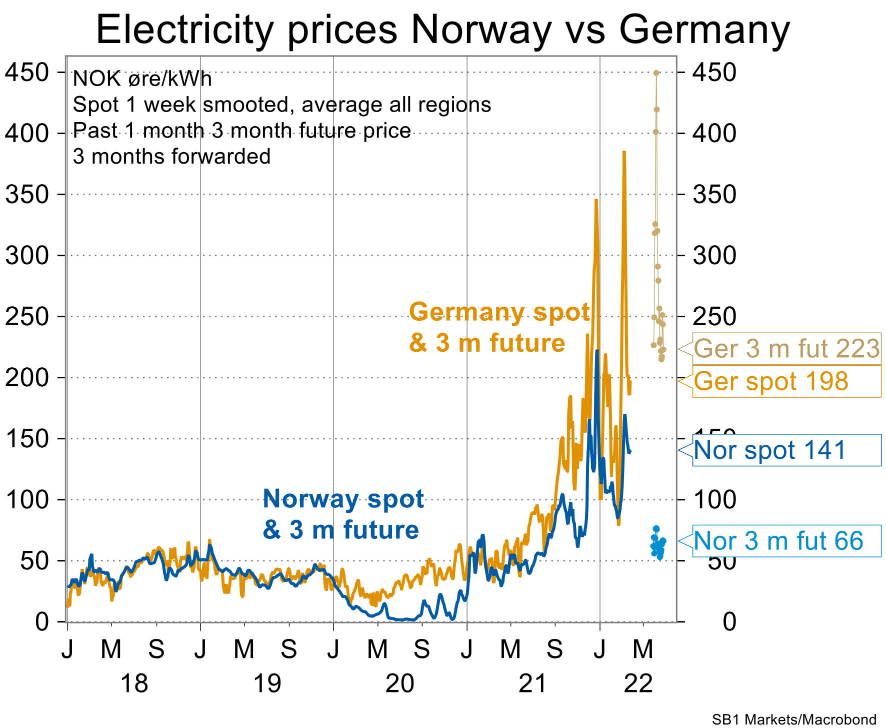


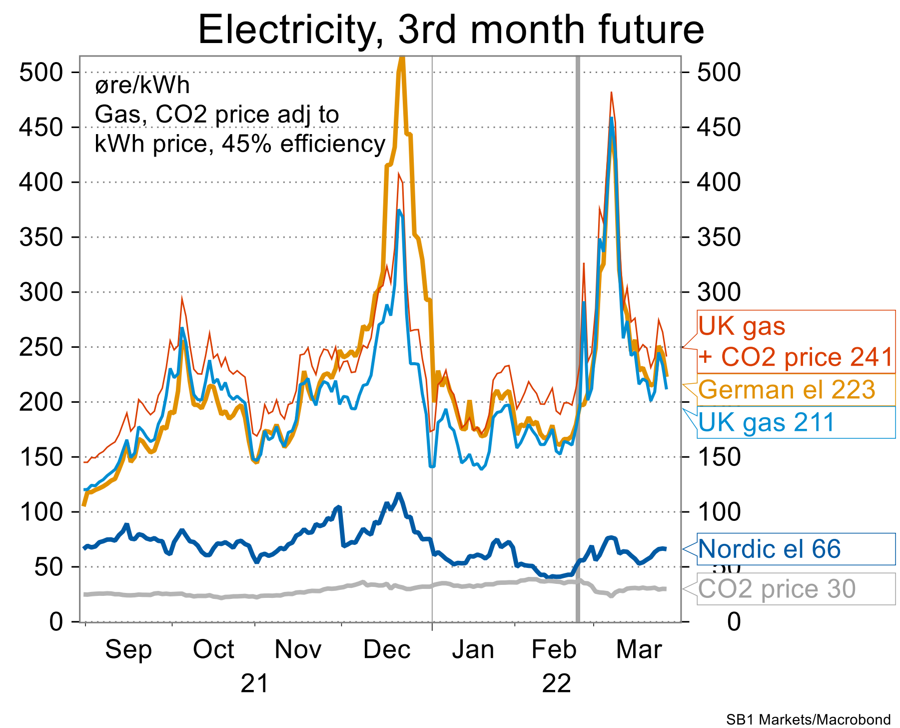


- Future prices have been lower than normal vs. the short end of the curve after the invasion – because markets assume that in the end, oil will flow

European gas & electricity prices are still trending down

Russia has so far supplied more gas to Europe – and Europe wants to buy it

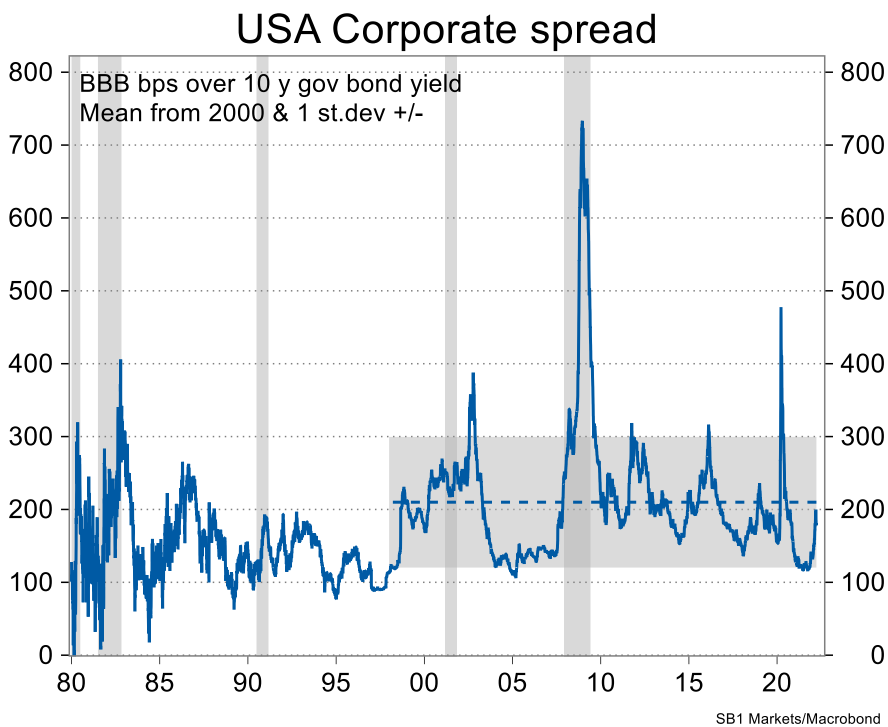


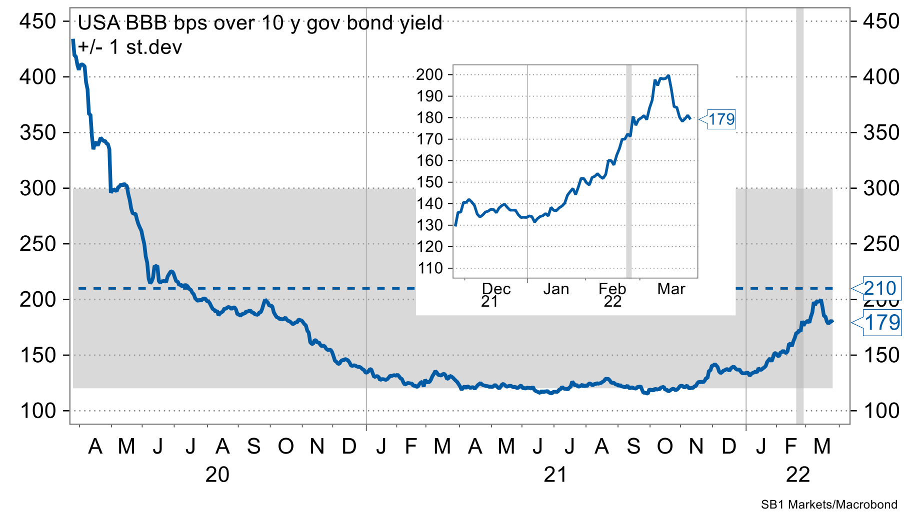


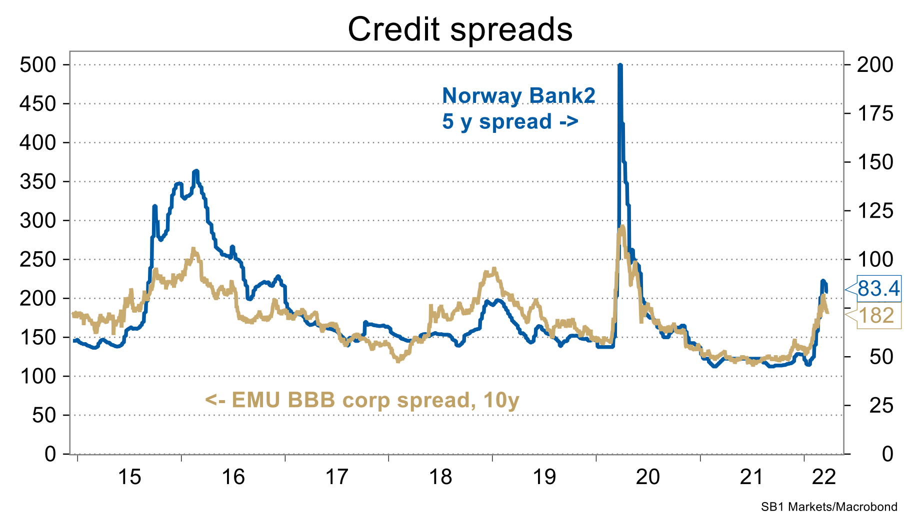
- **The 'Norwegian' risk**: Nordic future electricity prices remain far below European forward prices (even prices in the Oslo area)
- The Norwegian 2022 prices are up by approx. 35 øre/kWh since before the Russian invasion. At the CPI level (assumed continued subsidies, and still low prices in Mid/Northern Norway), this increase will lift the overall 2022 CPI by 0.4 pp. Still, the average electricity price will be lower in 2022 vs. 2021, and 2023 below the 2022 level
  - » The 80% subsidy for prices above 70 øre/kWh reduces the impact of higher electricity prices for Norwegian consumers substantially

Credit spreads further down last week but remain far above the local bottom

Norwegian bank spreads down too, as usual in tandem with spreads abroad

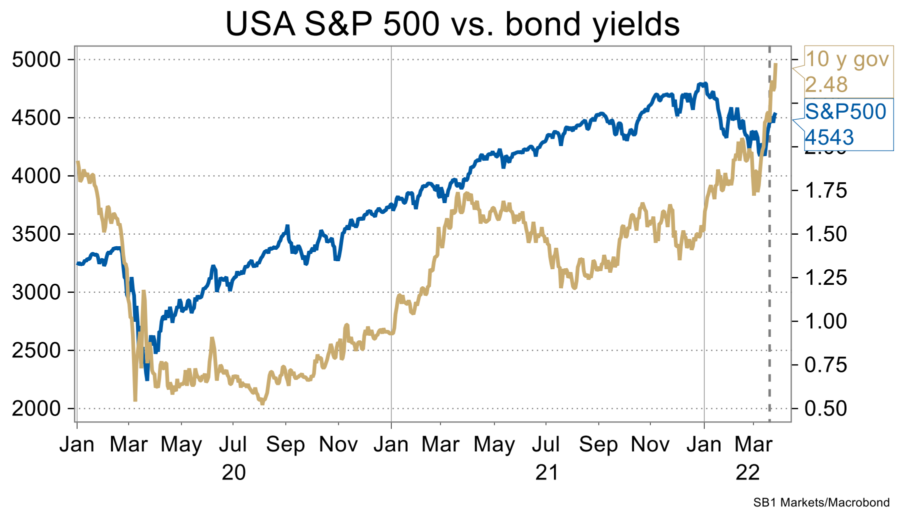


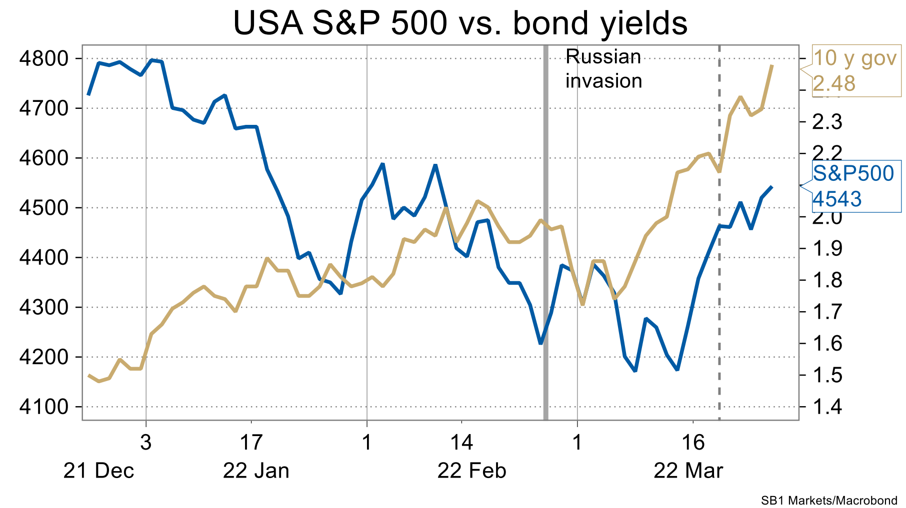


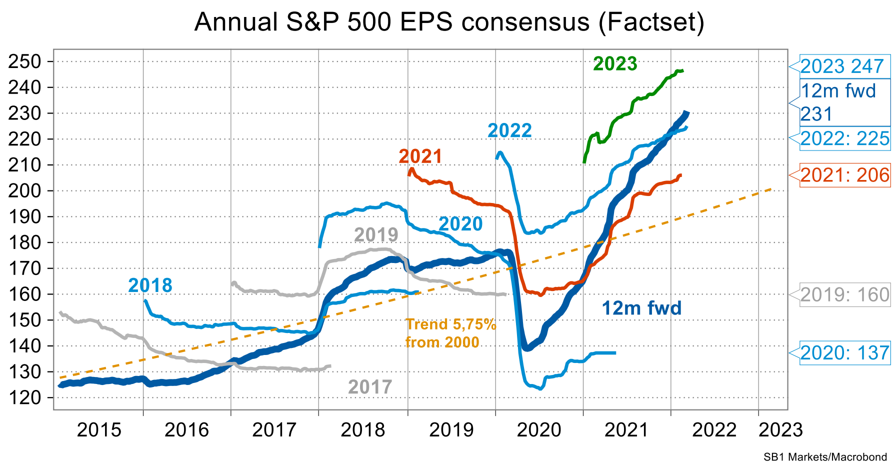


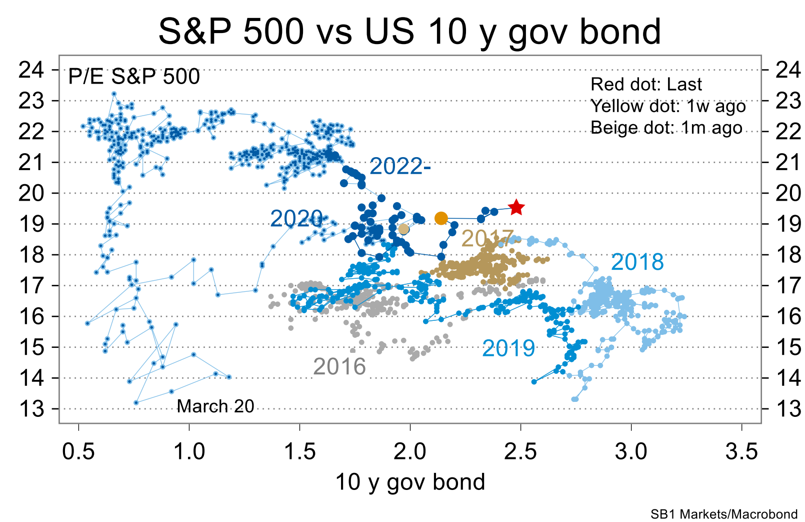
SpareBank 1 MARKETS

Bonds yields are surging but no (yet) a problem for the stock market



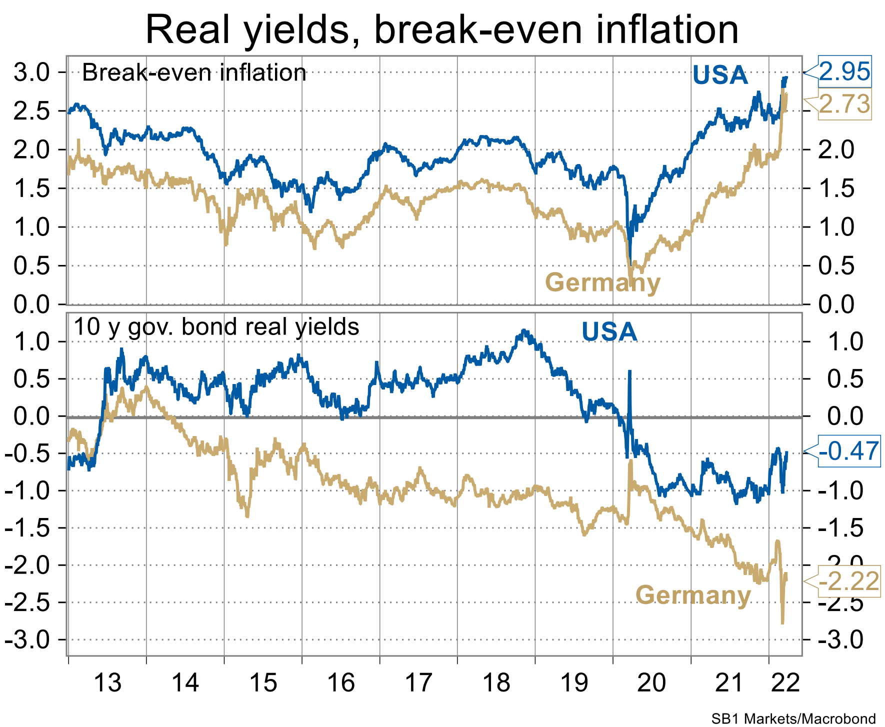


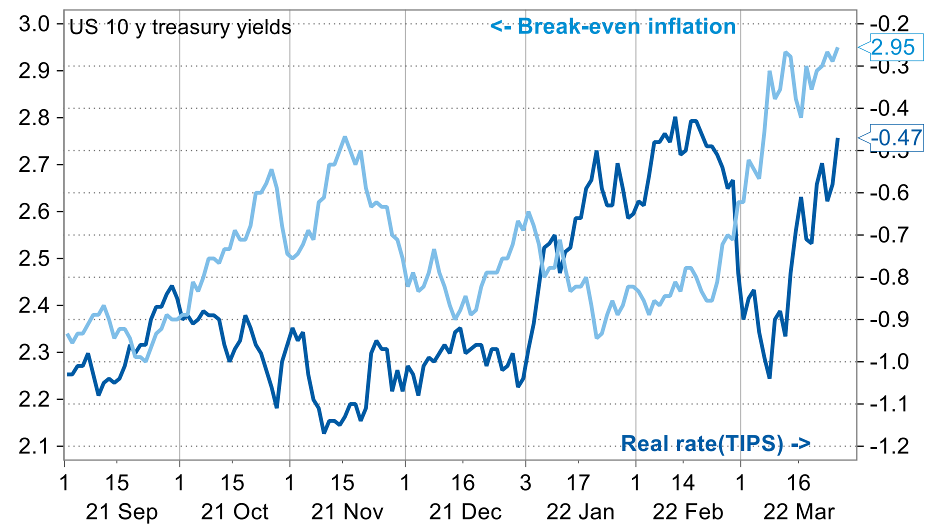




US real rates back up to the pre-war level. Inflation expectations are up 41 bps

Inflation expectations up in Germany too, by 75 bps but real rates are down 46 bps





US & Germany 10 y Gov bond yield

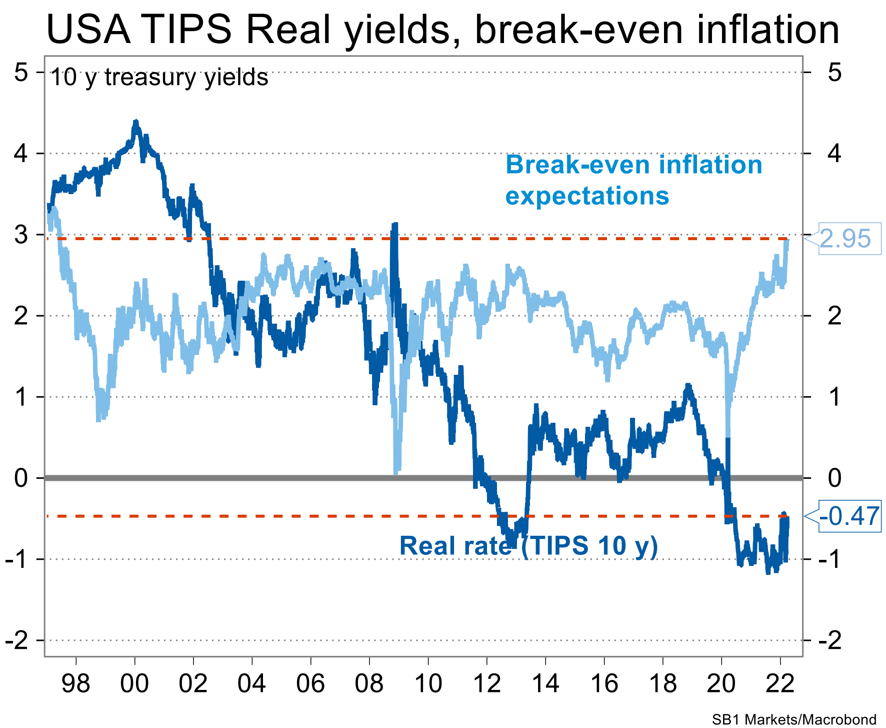
	Yield	Change 1w	Change 1m	Since Feb 18	Min since April-20
USA nominal treasury	2.48	0.34	0.51	0.56	0.52
.. break-even inflation	2.95	0.09	0.41	0.54	1.06
.. TIPS real rate	-0.47	0.25	0.10	0.02	-1.19
Germany nominal bund	0.51	0.14	0.34	0.29	-0.65
.. break-even inflation	2.73	0.18	0.51	0.75	0.40
.. real rate	-2.22	-0.04	-0.17	-0.46	-2.80

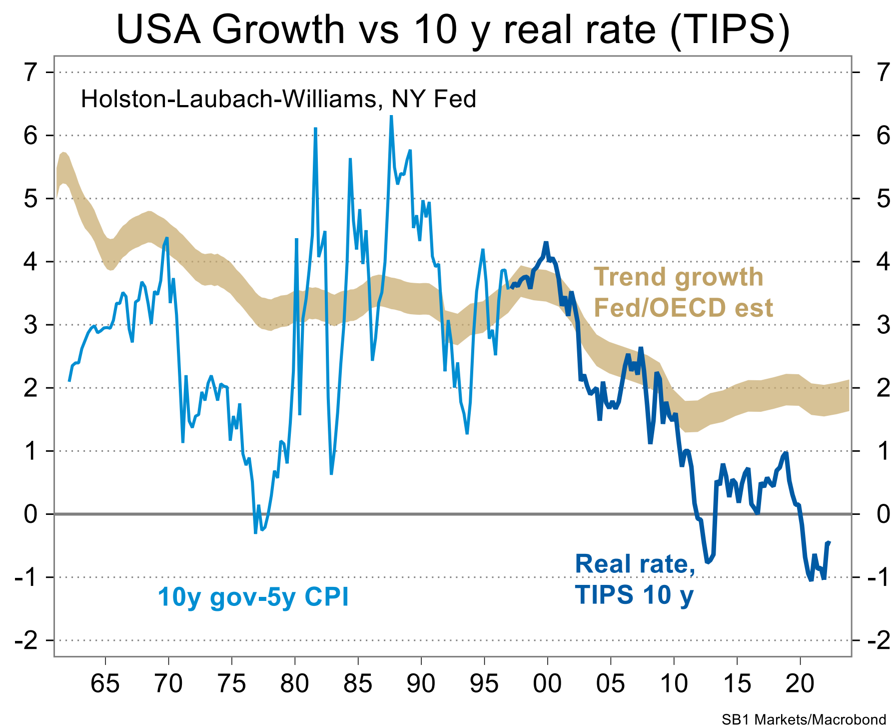
SB1 Markets/Macrobond

- **Real rates** are still very low, at least if growth keeps up in the US – or do not totally collapse in the EMU
- **Inflation expectations** are approaching levels that are signalling that markets have lost confidence in central banks' promises

What is the growth outlook?

If inflation is at 3%, and the real rate is at -1%, *we assume it is because the growth outlook is weak*

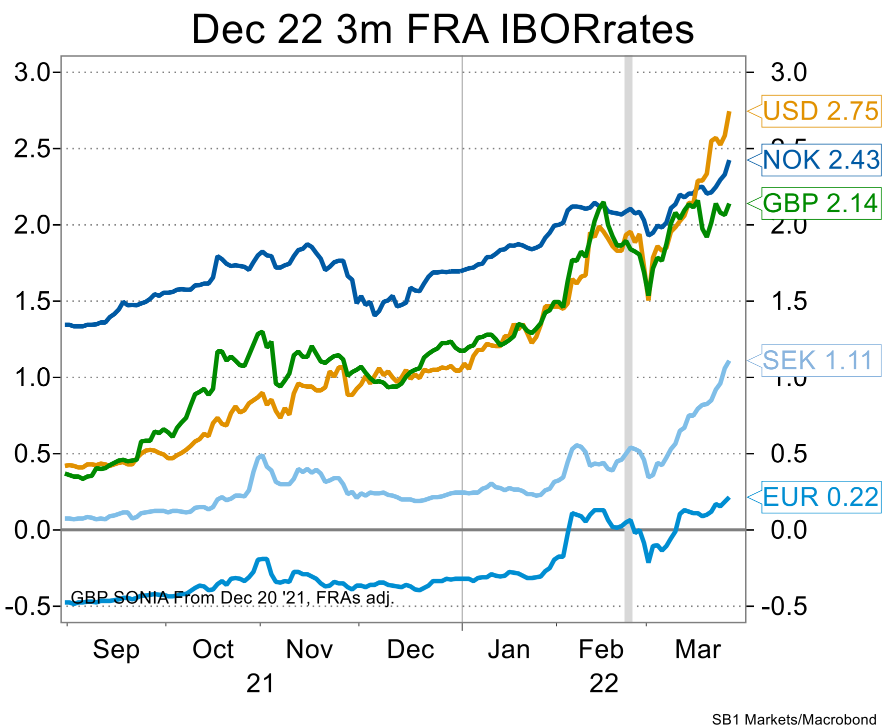


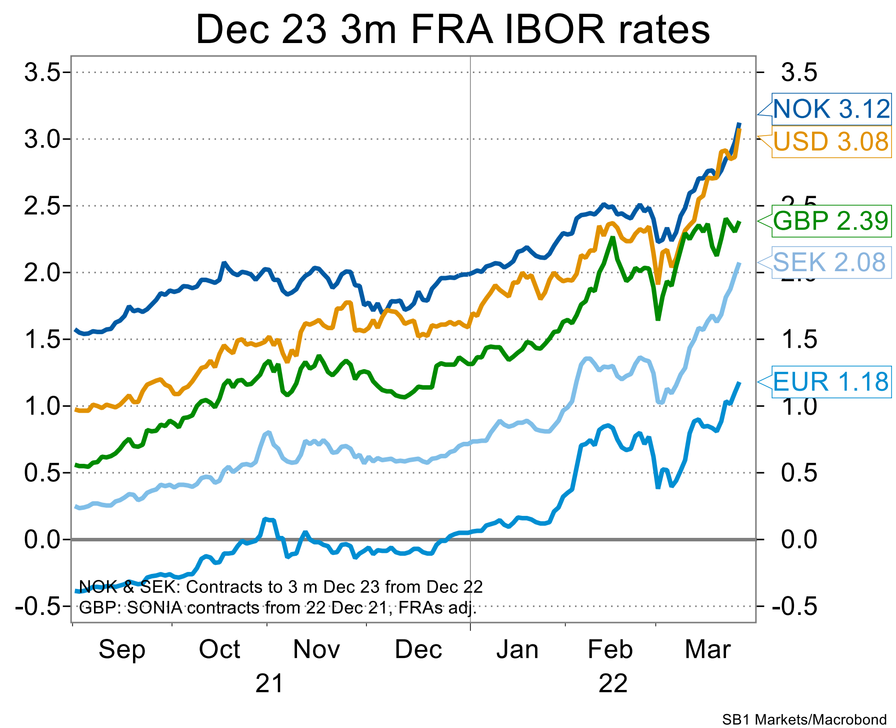


- If the economy is not really weak, we think central banks will tighten monetary policy by hiking rates, selling bonds in order to bring inflation by slowing the economy
- The big question: Has other markets discounted the bleak growth outlook that seems to be discounted in the bond market?

Is just the sky the limit? Dec-22 FRAs up 10 – 40 bps, Dec-23 by 26 – 45 bps

US and Swedish rates moved the most

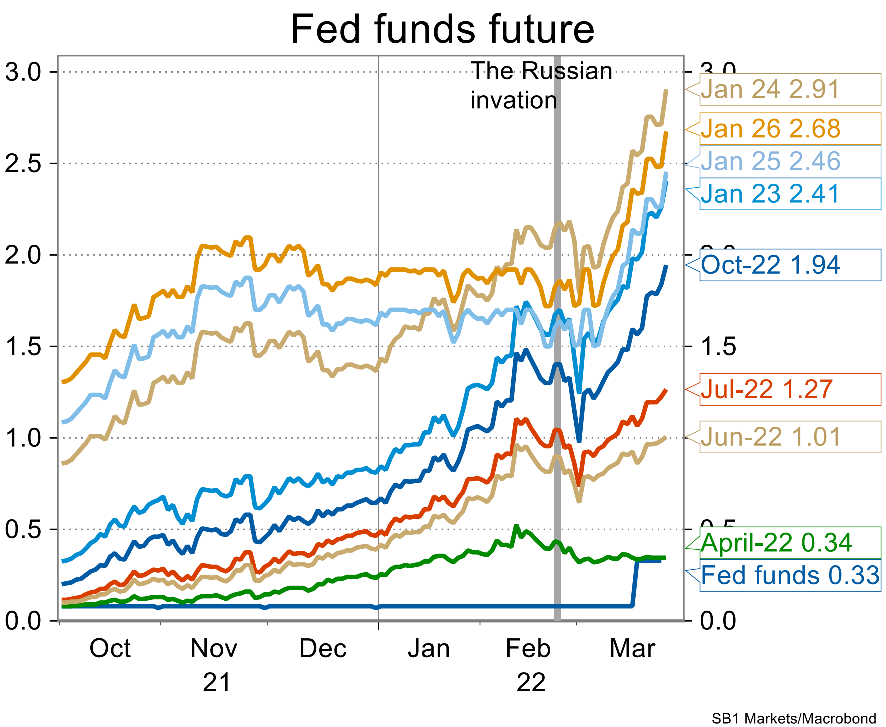


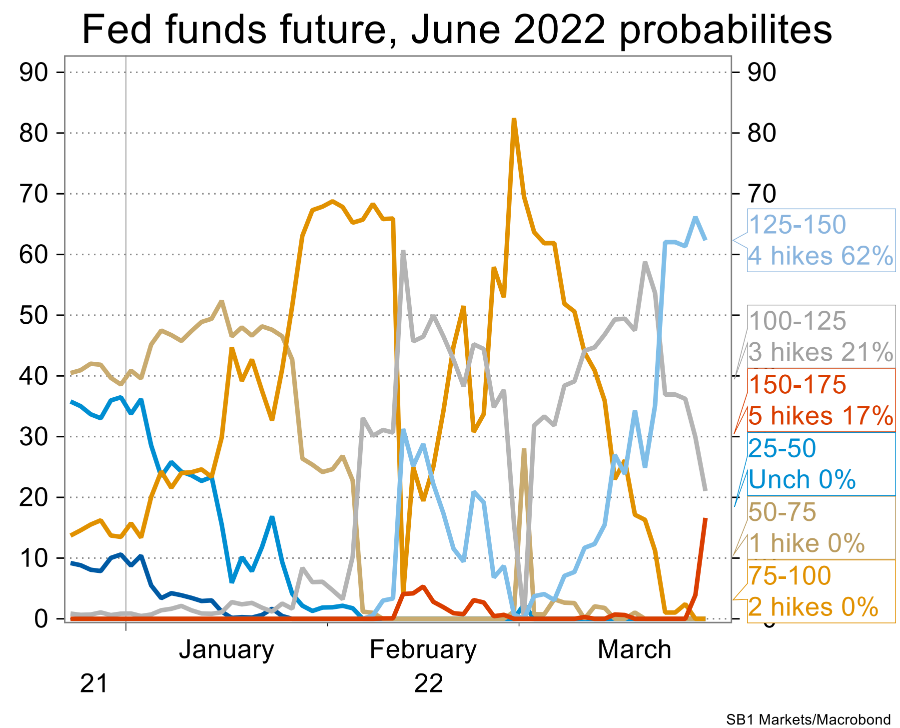


- We really look forward to the next Riksbank meeting! The Riksbank has until now insisted that the ZIRP will kept in place until H1-24. The market does not at all believe in that position. In fact, the market expects more than 10 hikes before that. We have never seen such a mis-match before between a central bank and the market before, at least not in a civilised country in recent times. Since the Riksbank's board cannot be ousted by the Government, the members should have taken the consequence themselves?

Fed funds future curve is steeping rapidly. +50 in May, and +50 in June is discount.

~~75~~ 100 more bps during Q2 is deemed to be the most likely outcome. 125 bps almost as likely as 75!!

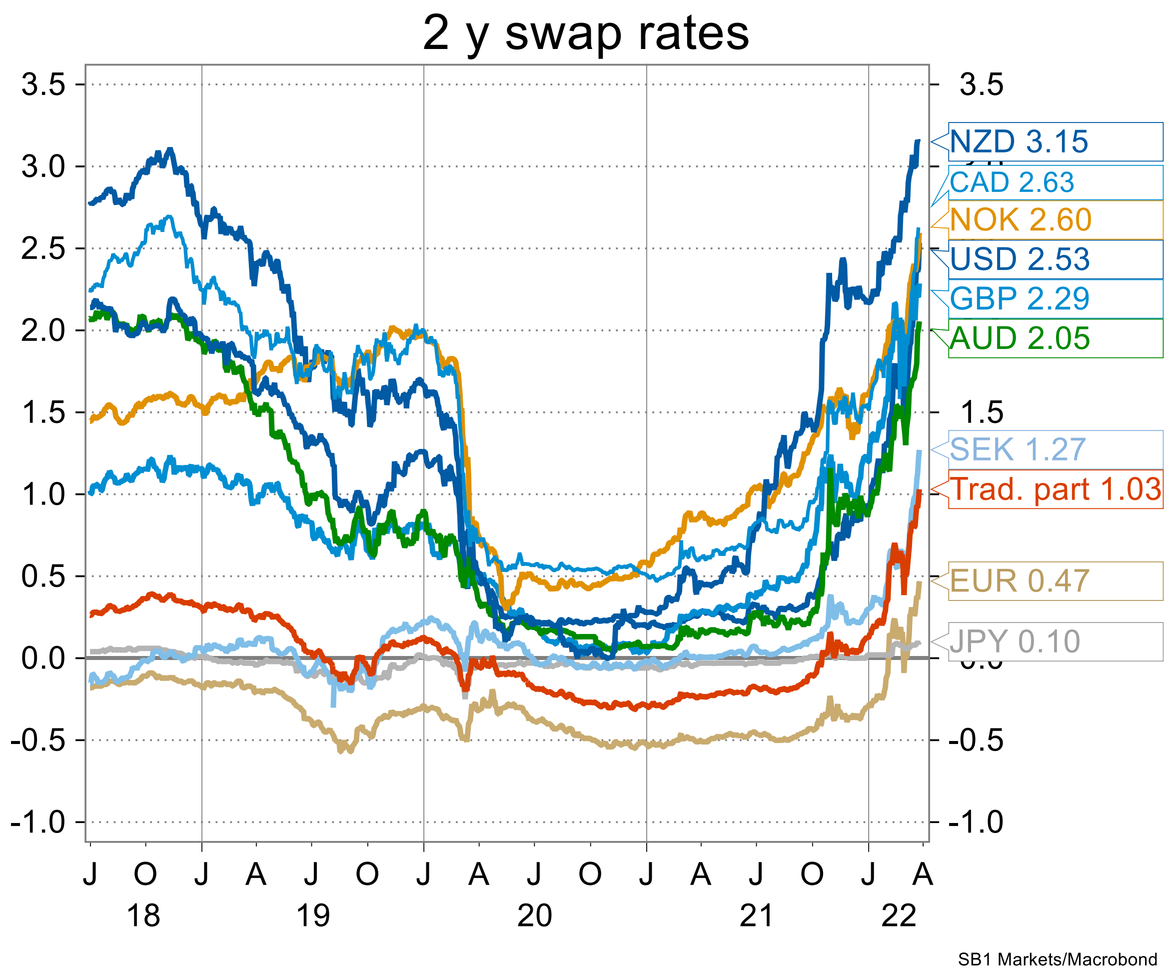


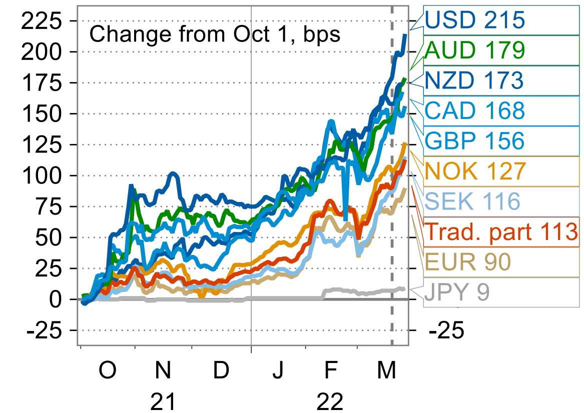


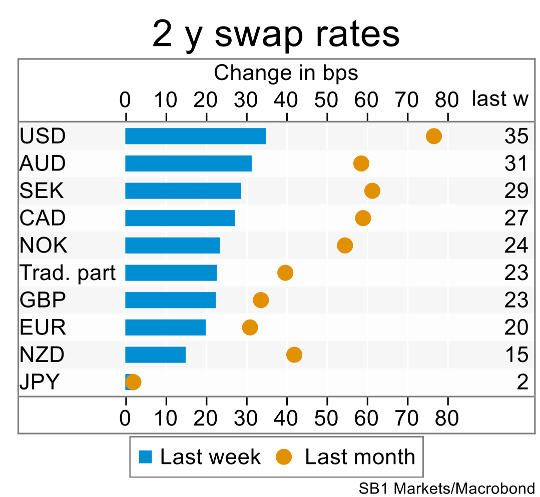
- Is the market going bananas? Well, the Fed has recognised that it is behind the curve, and the market expect the Fed to reach 1.25% in Q2 – which is still far below a neutral rate
- At last Monday, the 3rd working day after the FOMC meeting the previous week, Powell stressed the need for fighting inflation, and that more than 25 bps hikes could not be ruled out. His comments initiated a substantial hike in interest rate expectations, by some 20 bps. Towards the end of the week, rates shot up by the same amount, alongside higher oil prices

Powell talked up rates sharply, just 3 working days after the FOMC meeting!

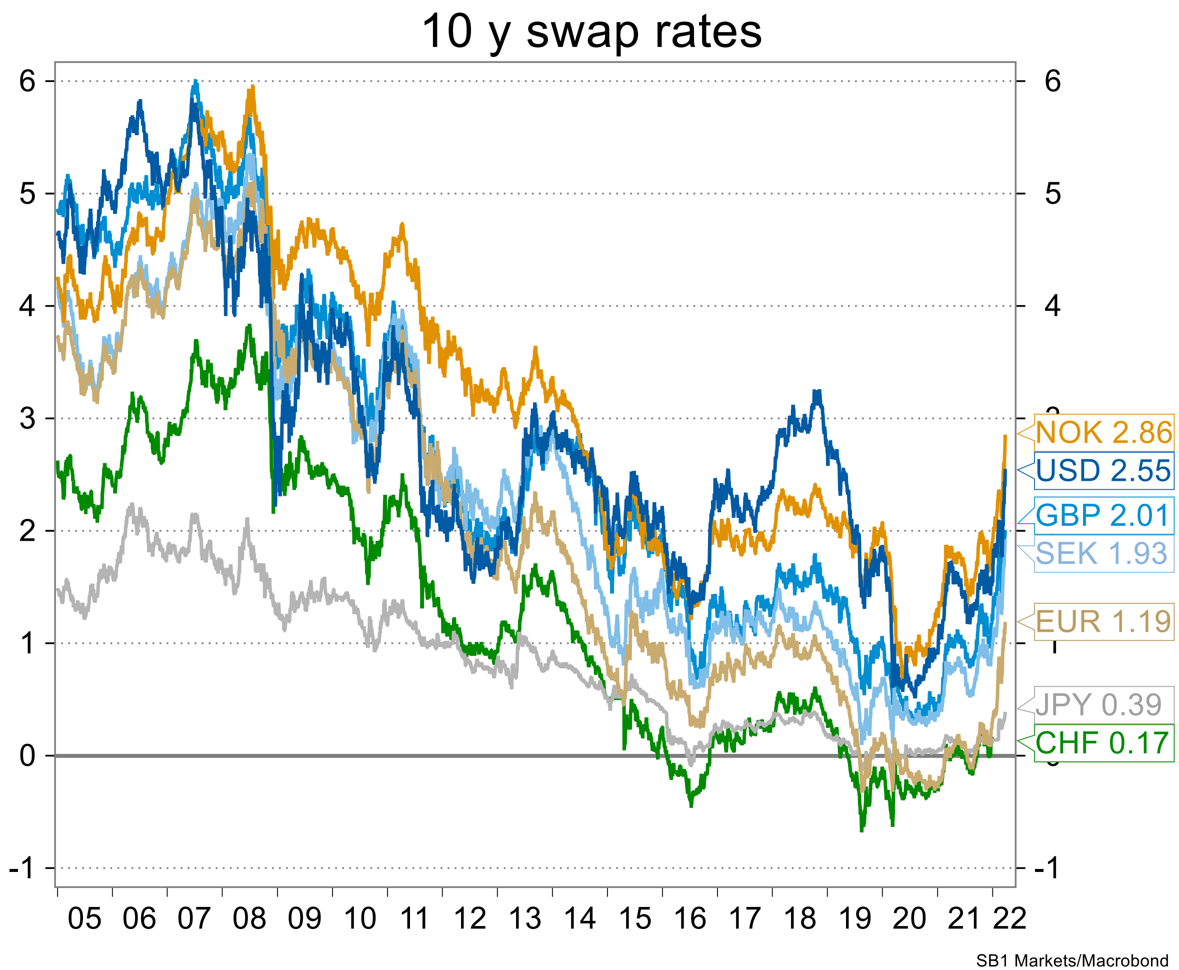
2 y rates shot up everywhere – and Norway in the middle of the group. Just JPY rates well anchored

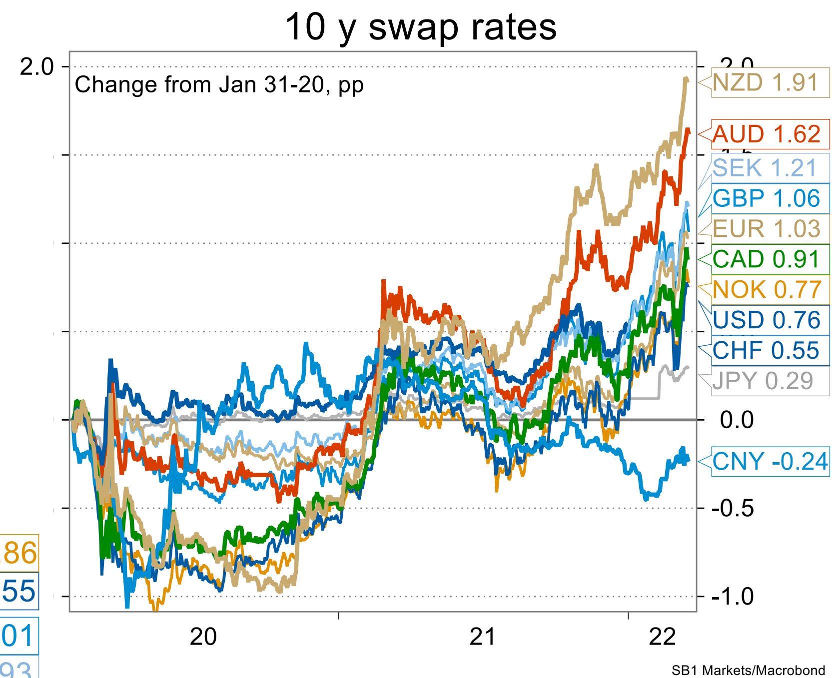


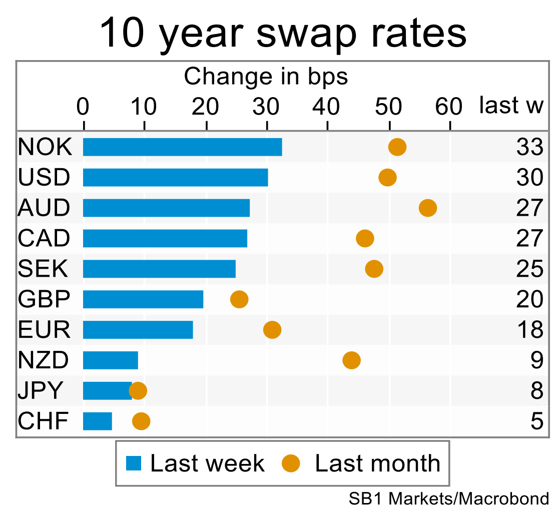




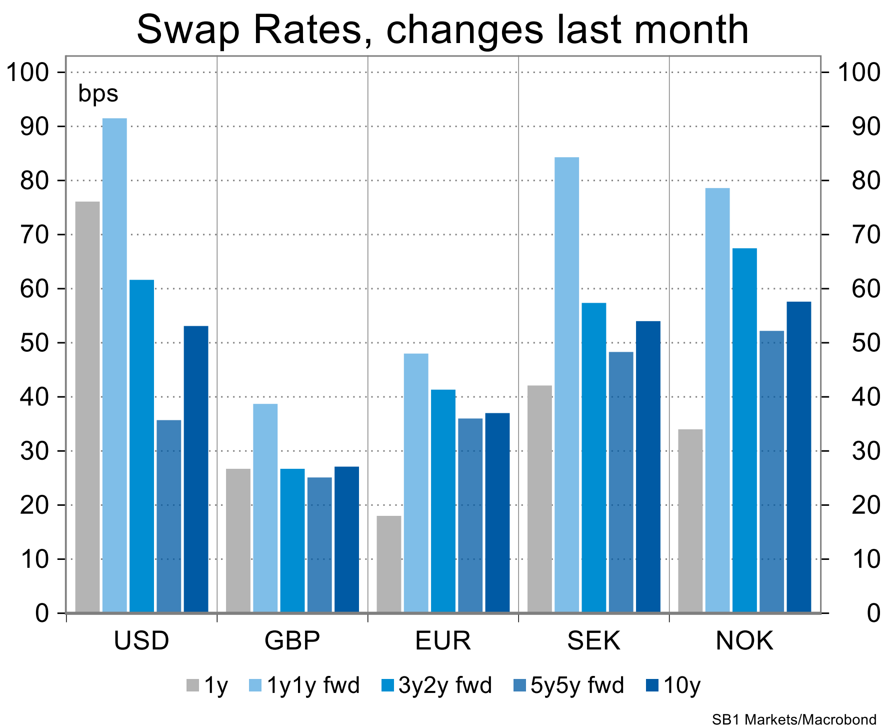
NOK in the lead, the others followed suit ☺

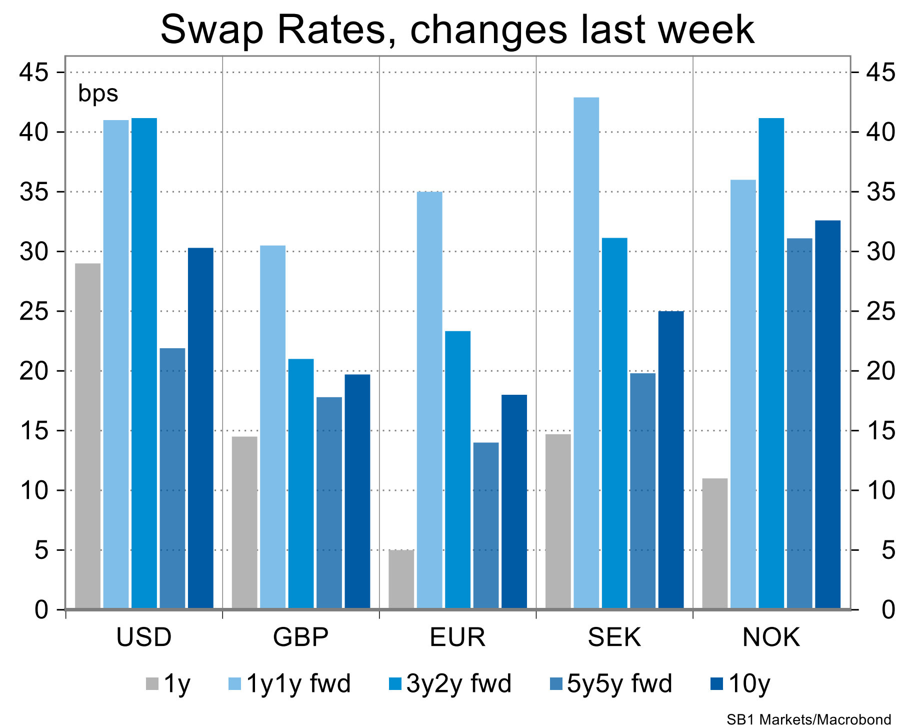






What a week! Rates up everywhere, all over the curve – and by substantial amounts





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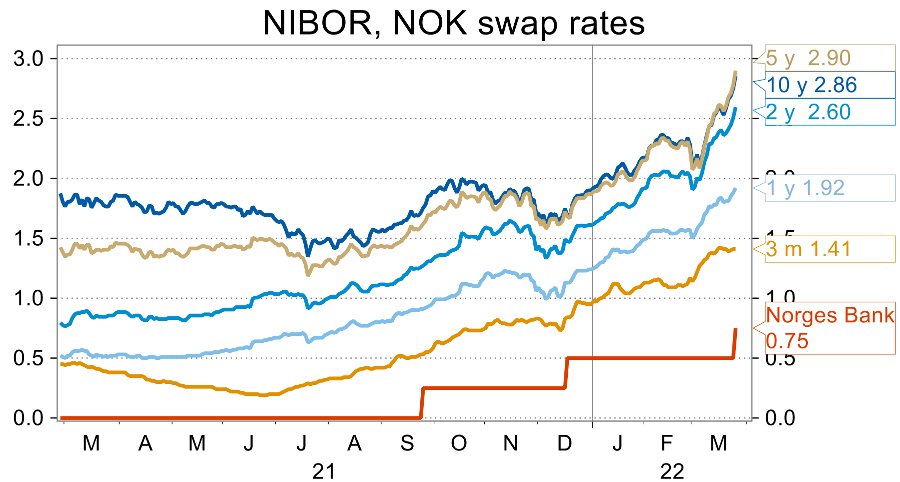
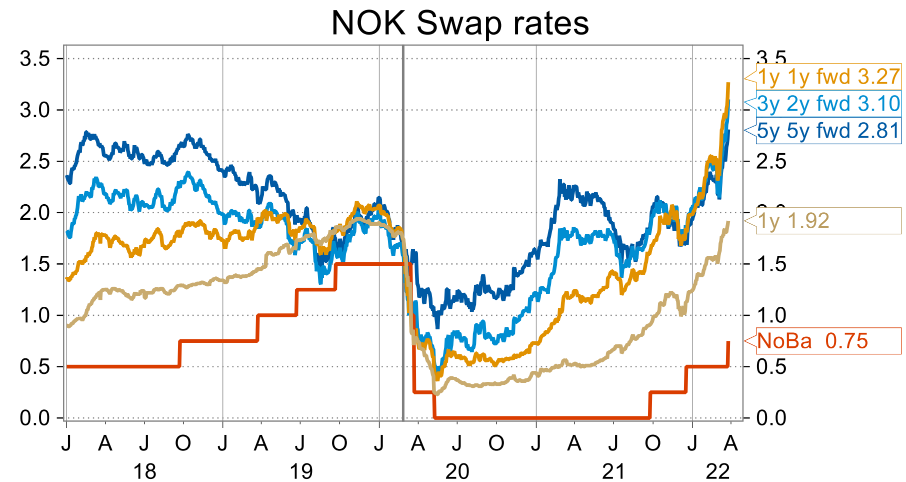
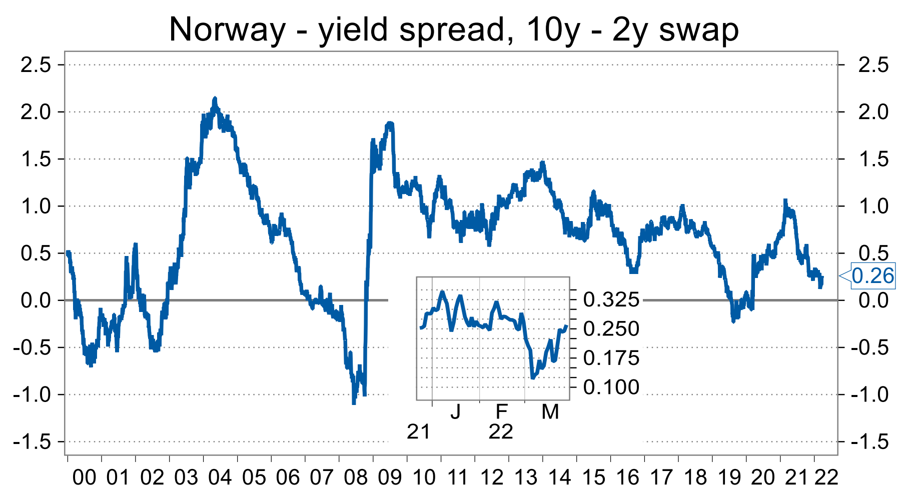
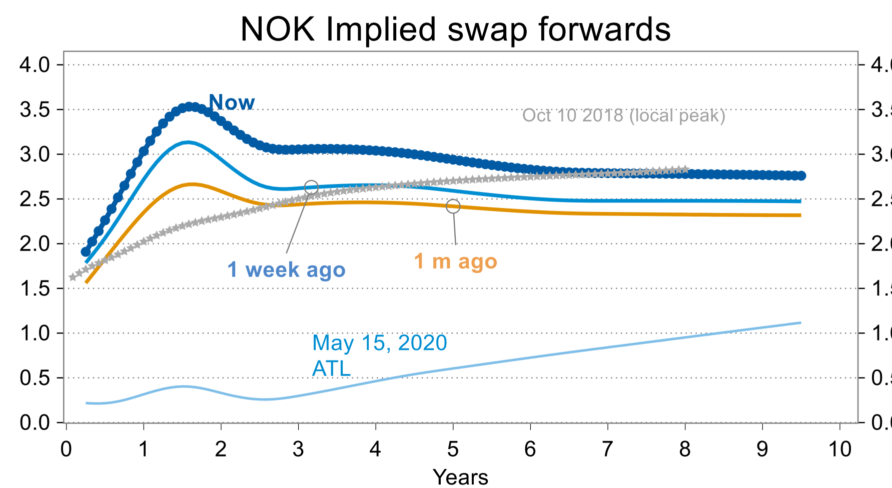
Long dated swaps are approaching 3%

The forward curve peaks at ~~3%~~ 3.5% at 1.5 y



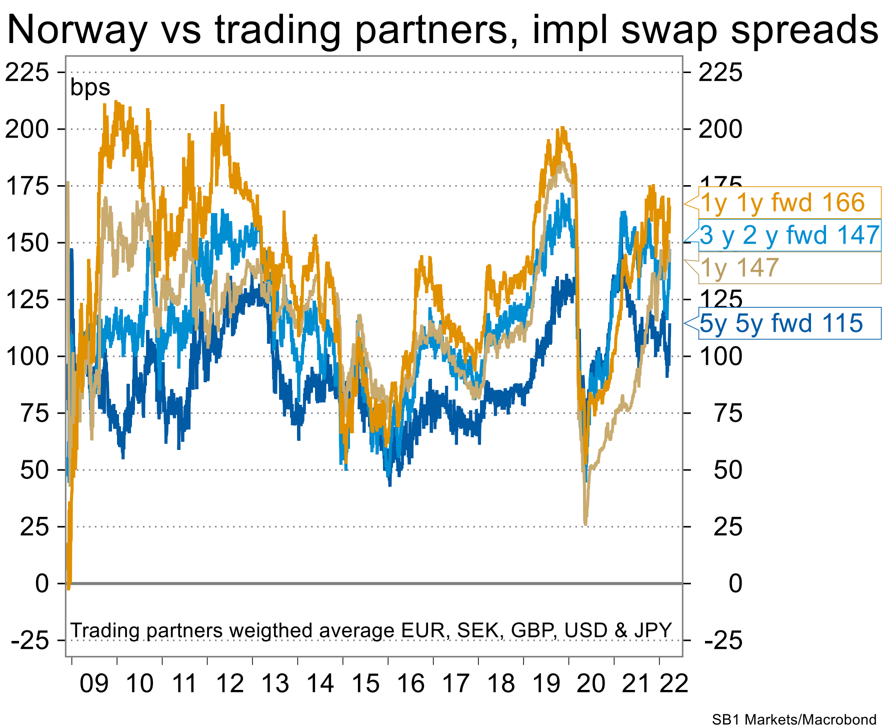


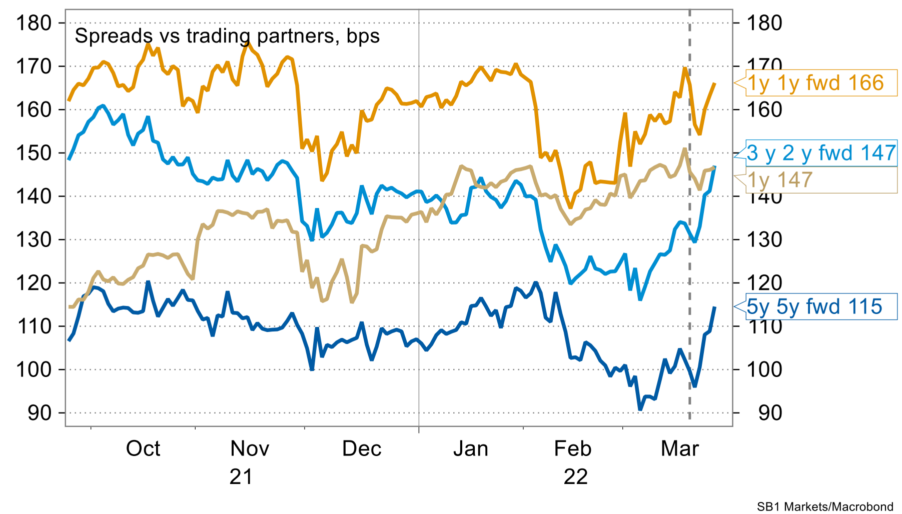


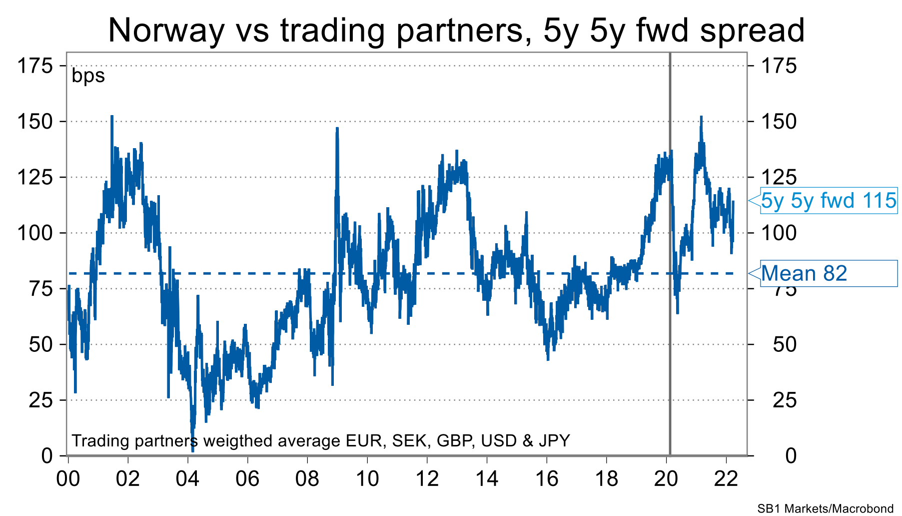


SpareBank 1 MARKETS

Spreads marginally down in the short end, sharply up further out on the curve

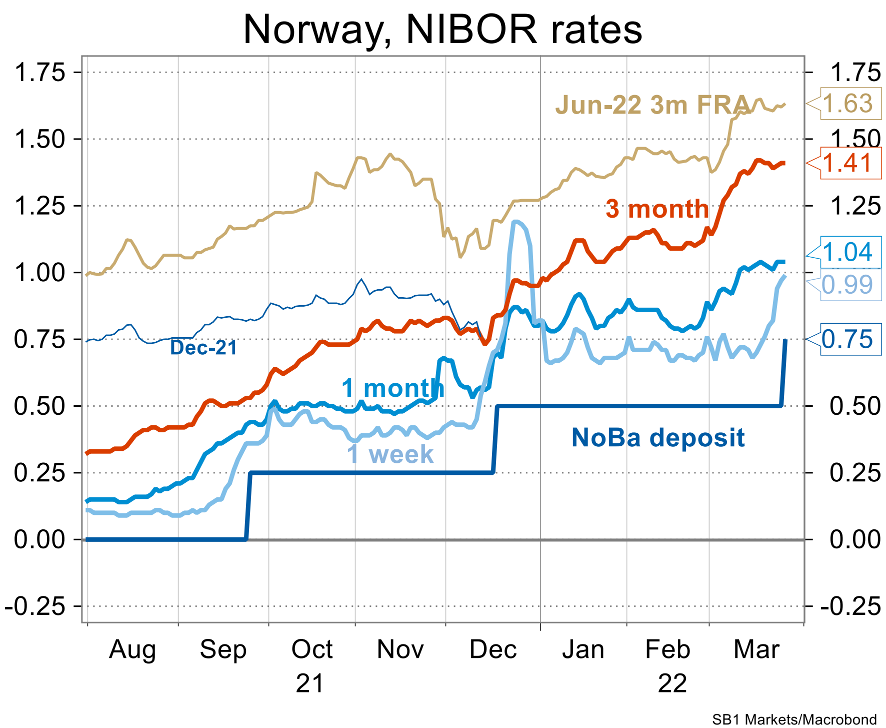


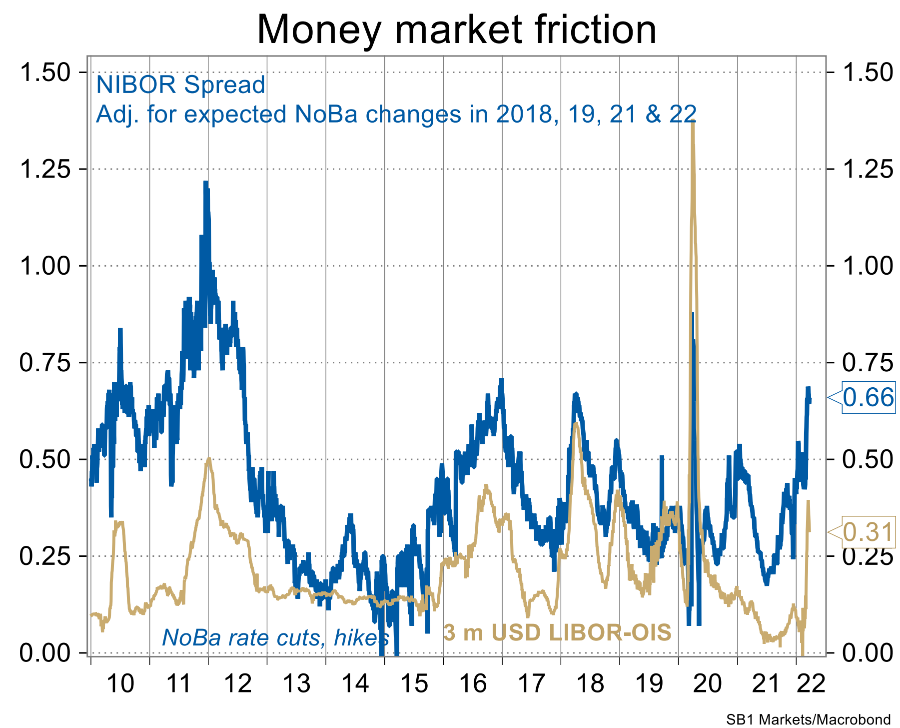




The 3m NIBOR FRAs stable, the NIBOR spread at 66 bps

… if NoBa does not hike in May too

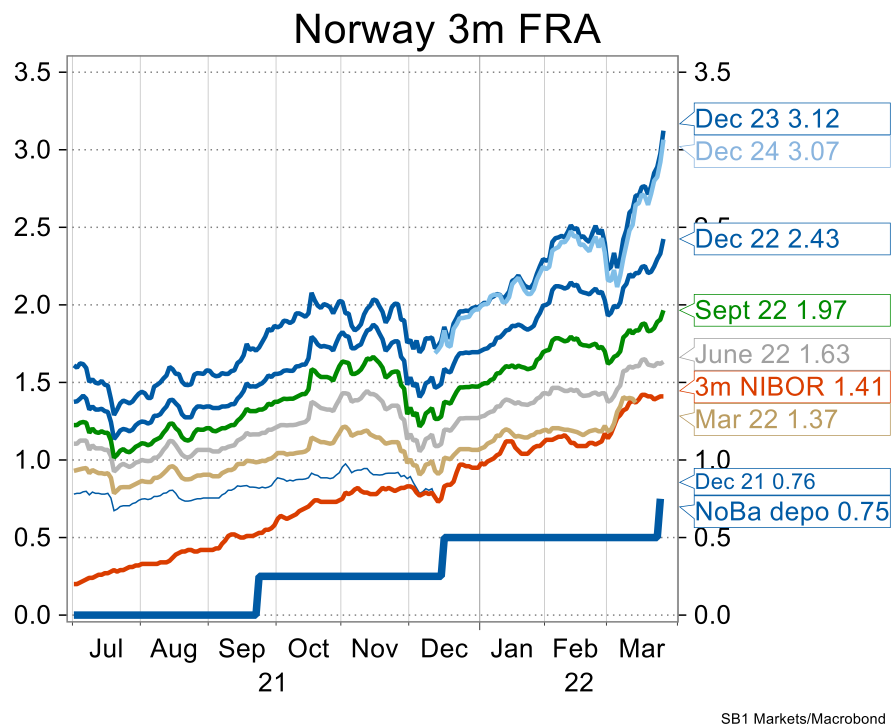


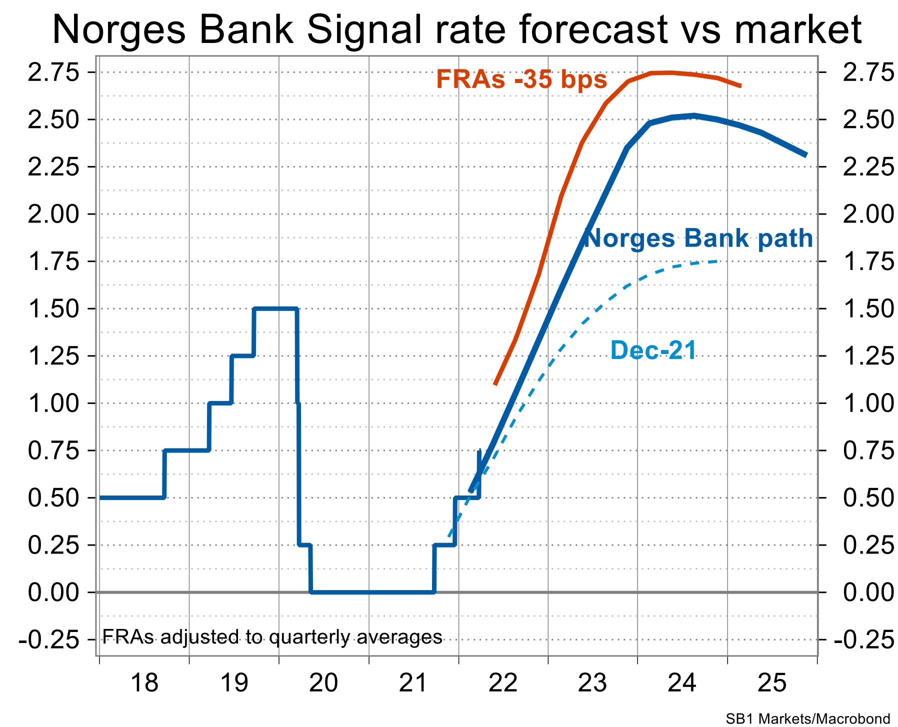


- The **USD LIBOR-OIS spread** declined 7 bps to 31 bps, which may signal some easing in NIBOR spreads as well
- Liquidity issues may follow sanctions – but most likely not, and in Norway, Norges Bank will have no problem countering them by offering banks more liquidity

FRAs shot up, by up to more than 40 bps, more than half after the NoBa meeting

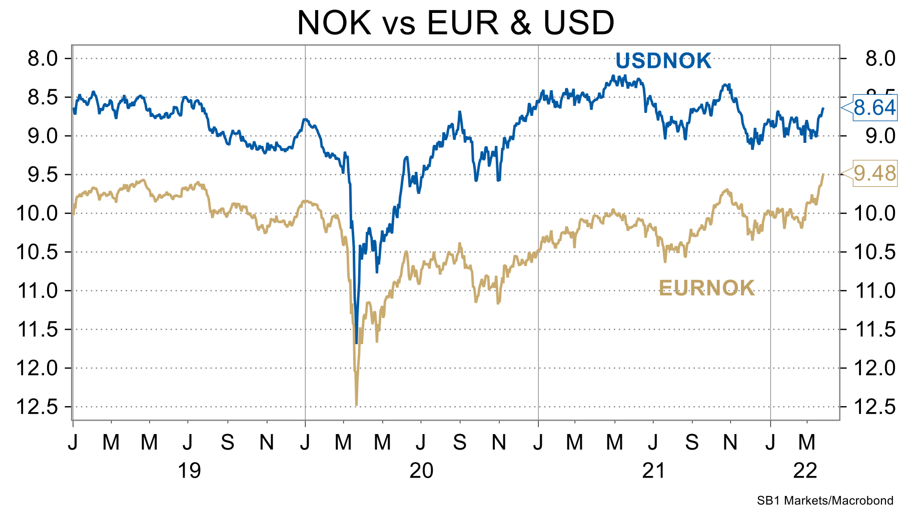
Market 3 m FRAs are up 90 bps above NoBa's path! Given a 'normal' spread, more than 50 bps!

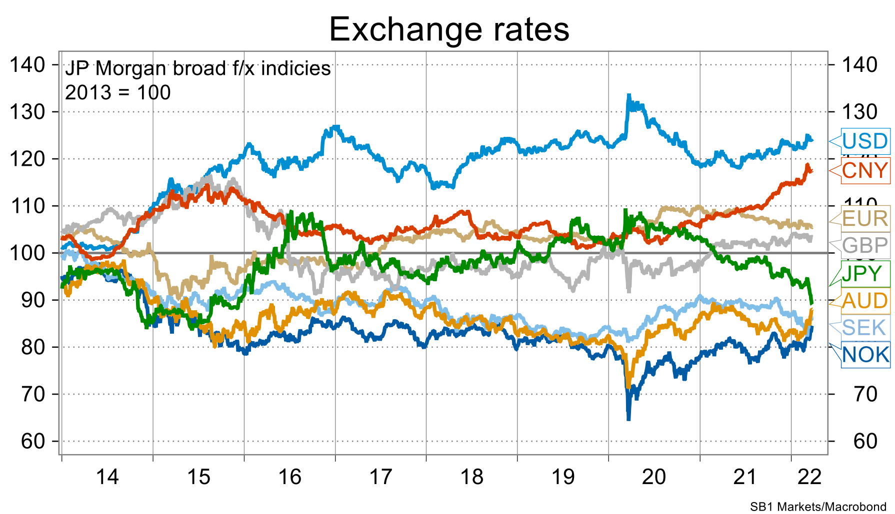


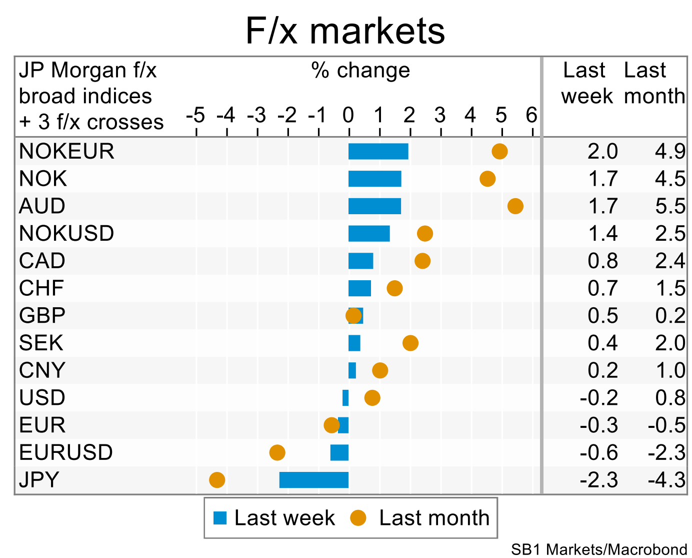


- Norges Bank almost ruled out a May hike in the MPR last week
- The June 3 m FRA contract at 1.63% implies:
  - A 100% probability for a 50 bp NoBa hike to 1.25% if the assumed Q3 NIBOR spread is 38 bps
  - A 50% probability for a 50 bp hike if the assumed Q3 NIBOR spread is 50 bps – as forecasted by NoBA in the MPR
  - A 100% probability for a 25 bp hike if the assumed Q3 NIBOR spread is 63 bps
  - A 88% probability for a 25 bp hike if the current 66 bps NIBOR spread remains in place
- Most likely, the expected spread is higher than 38 bps, but probably not much above 50 bps, given the normal spread volatility

NOK further up, together with AUD, CAD, SEK



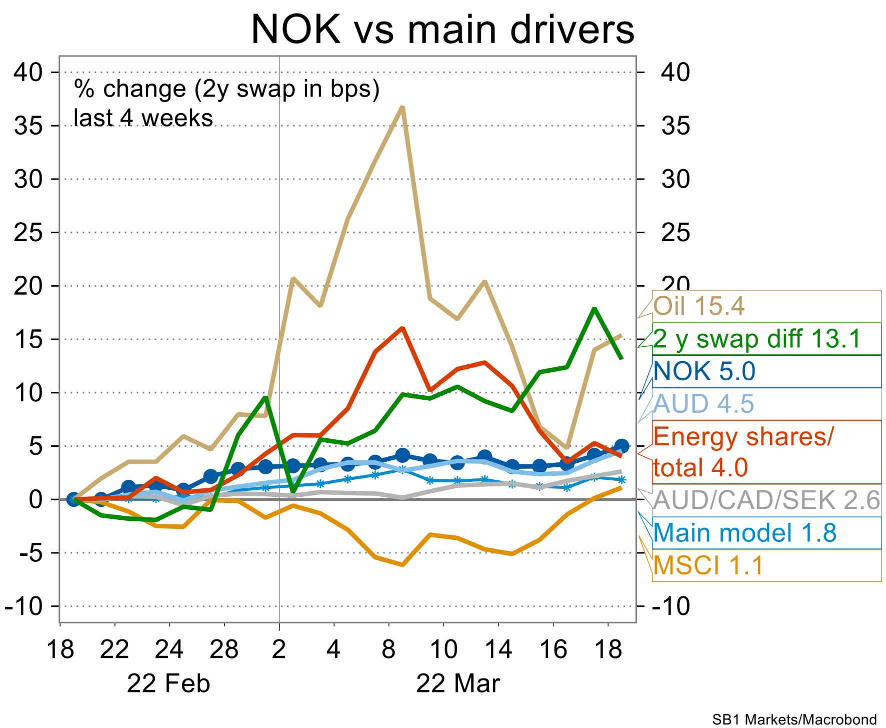


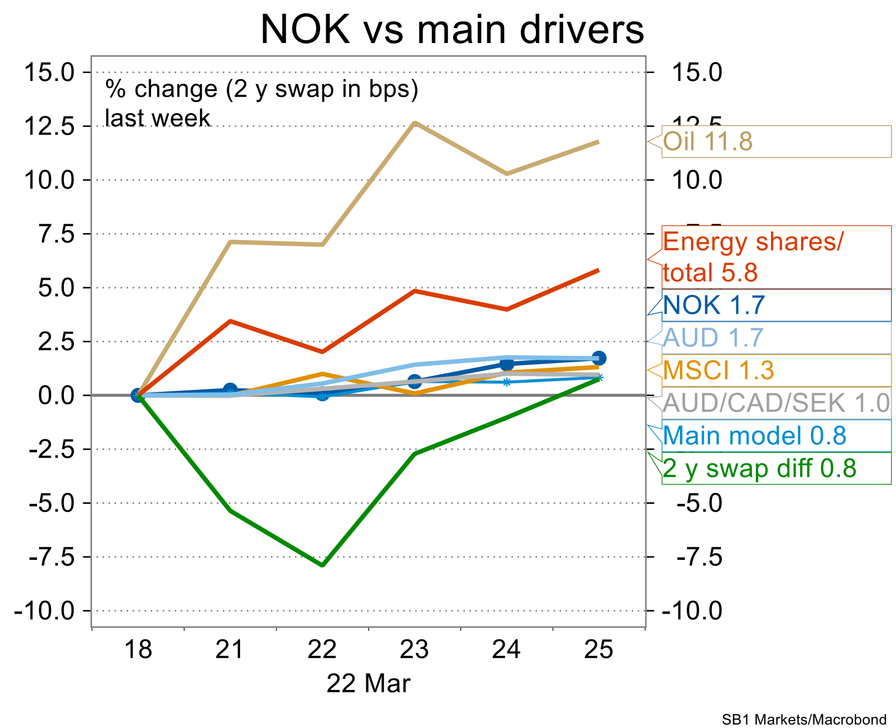


JP Morgan f/x broad indices + 3 f/x crosses	Last week	Last month
NOKEUR	2.0	4.9
NOK	1.7	4.5
AUD	1.7	5.5
NOKUSD	1.4	2.5
CAD	0.8	2.4
CHF	0.7	1.5
GBP	0.5	0.2
SEK	0.4	2.0
CNY	0.2	1.0
USD	-0.2	0.8
EUR	-0.3	-0.5
EURUSD	-0.6	-2.3
JPY	-2.3	-4.3

The oil prices ended down last week, the NOK still up 1.1%, from a 'low' level

Our model suggested an unchanged NOK



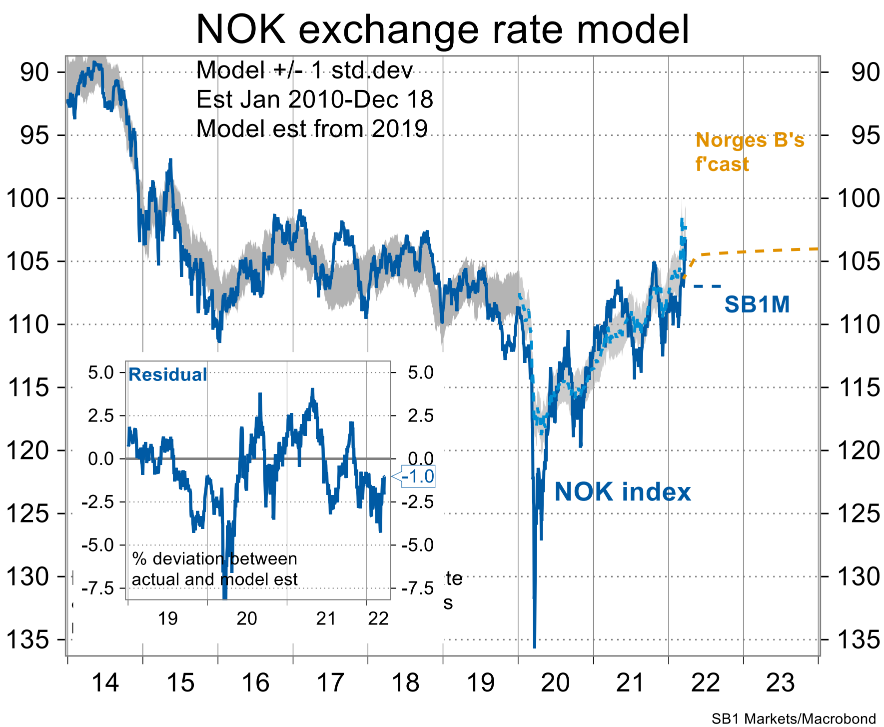


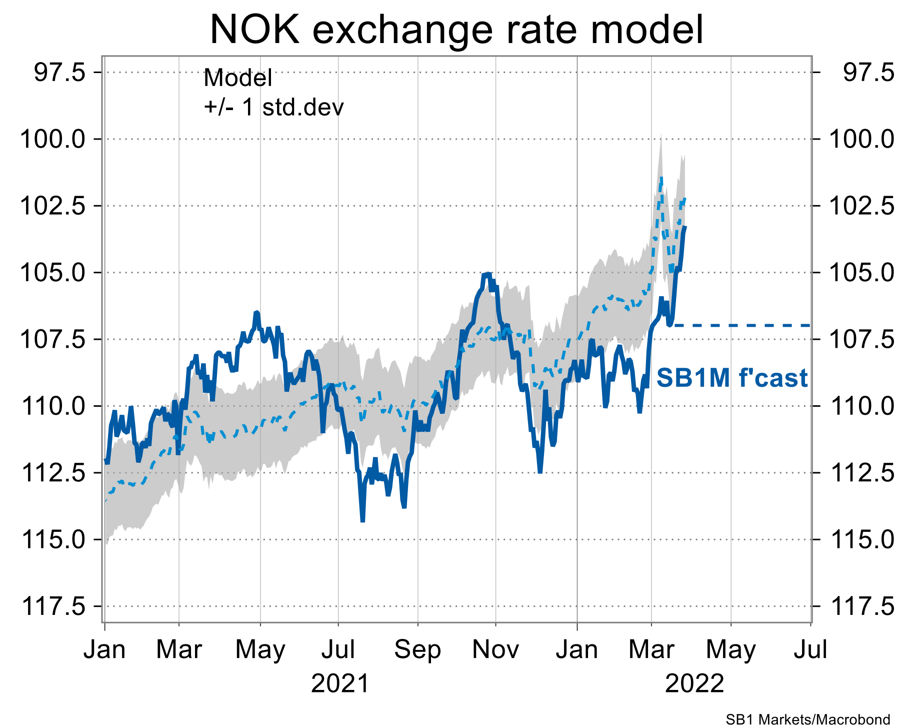
The status vs. the normal drivers:

- ***The NOK up 1.1% - and the NOK is just 1.1% below the model est (from -2.5%)***
- The NOK is 2% weaker than our AUD/CAD/SEK-model, our 'super-cycle peers', predicts (unch)
- NOK is 5% stronger than a model which includes global energy companies equity prices (vs the global stock market), but less than last week (from 3%)

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 just 1.1% from 4% two weeks ago

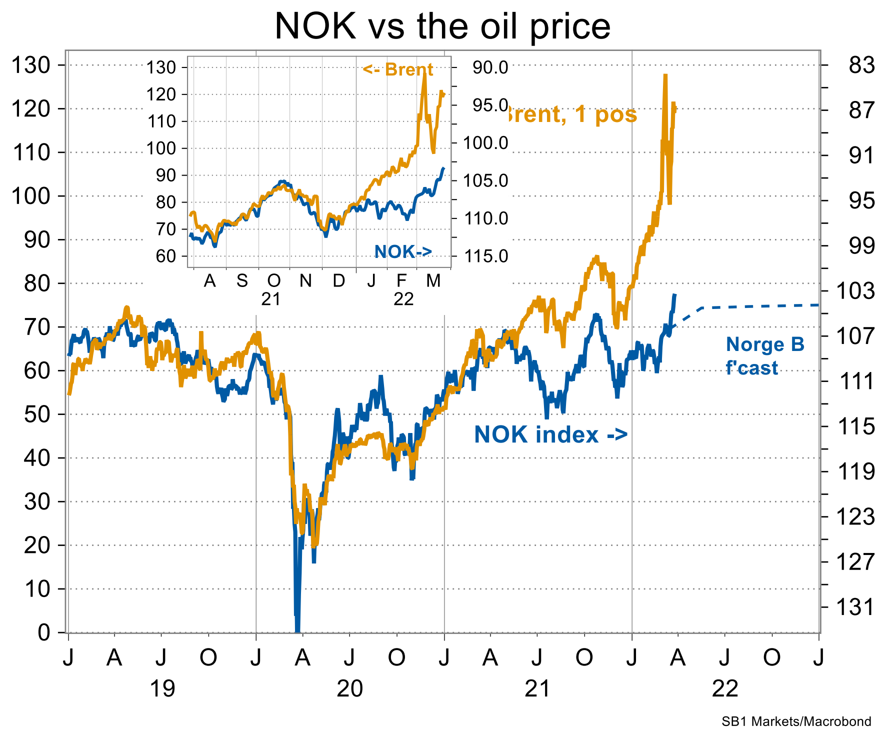


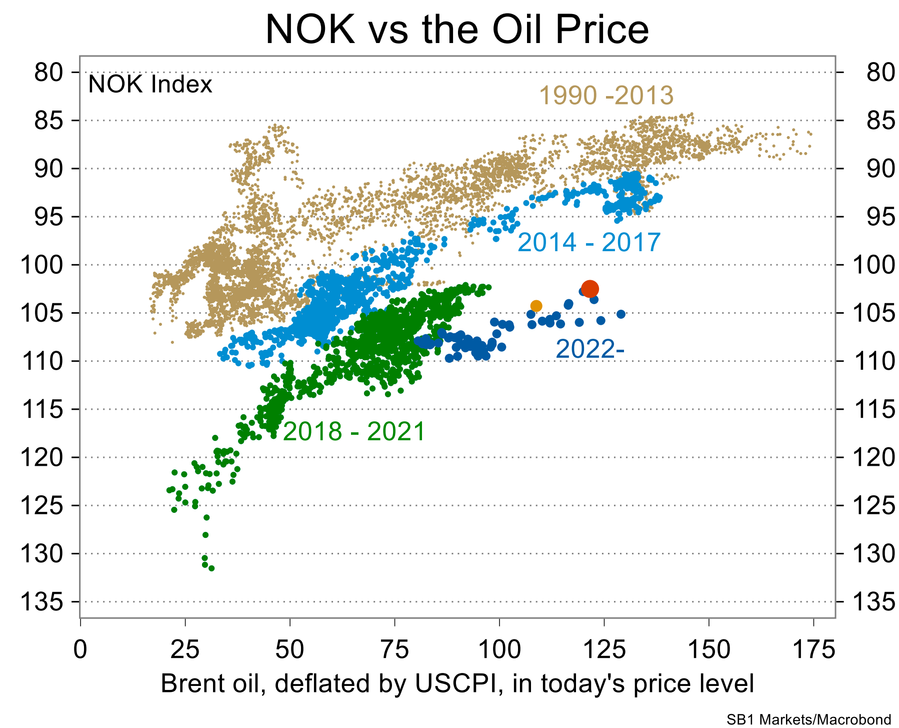


- Normally, the short end of the oil curve is most important for the NOK, not the ‘whole’ curve, which would have been more logic
- Gas prices are not included in our model either. Gas prices have been so closely correlated to the oil price, so it is not easy to estimate the impact of the gas price, historically

The oil price up, NOK up almost as it 'should'

NOK has <u>not</u> been particularly correlated to oil prices lately, at least not vs the short end of oil curve

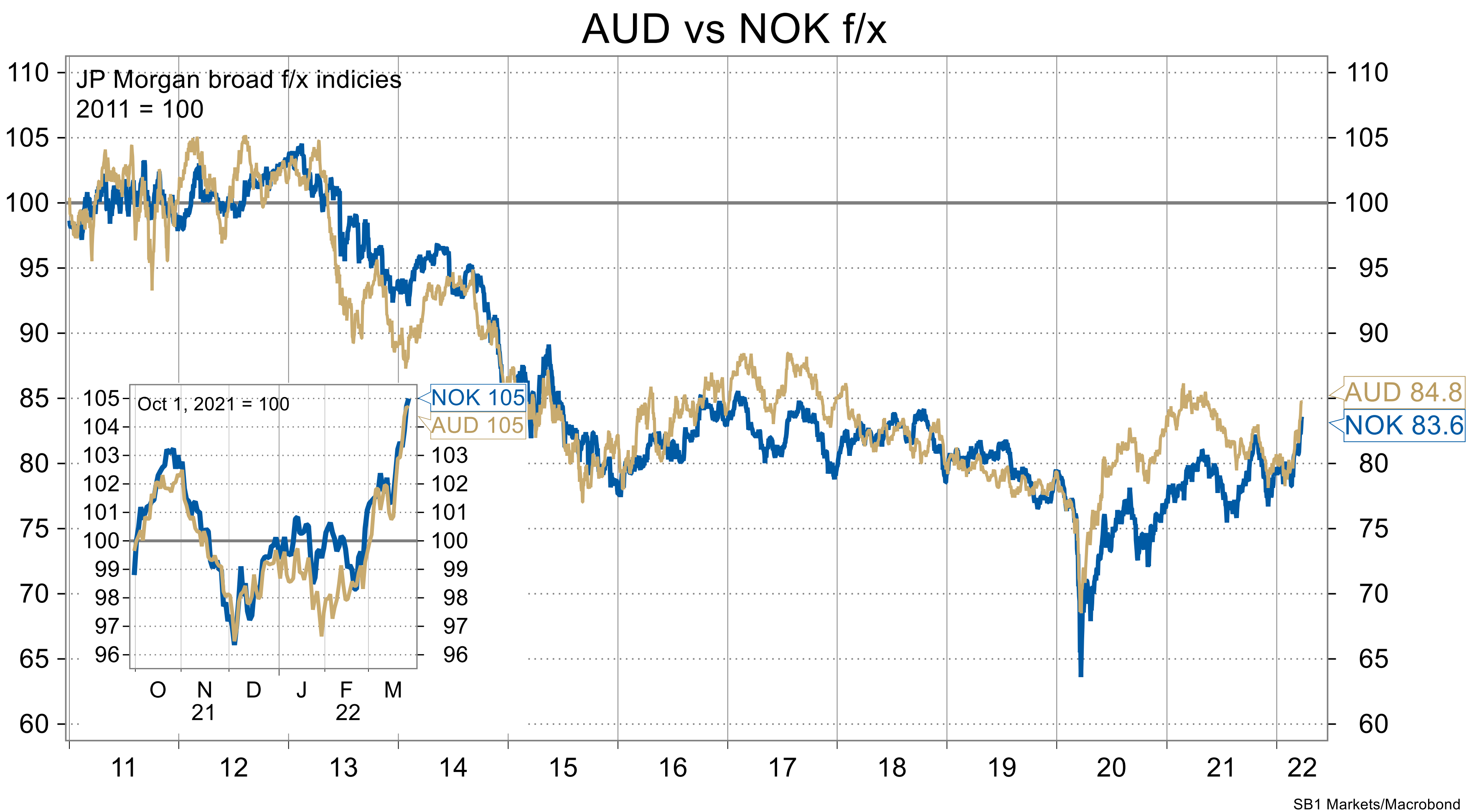




- NOK is normally correlating quite closely to the oil price but at a lower level than before 2018 – and now the NOK is weak even vs the past 3 years' (and now also the previous 6 month's relationship)
- A USD 10 drop in the oil price weakens the NOK by some 4%, as a partial effect.
  Within a broader model, the impact is substantially smaller

NOK is still dancing closely with the AUD

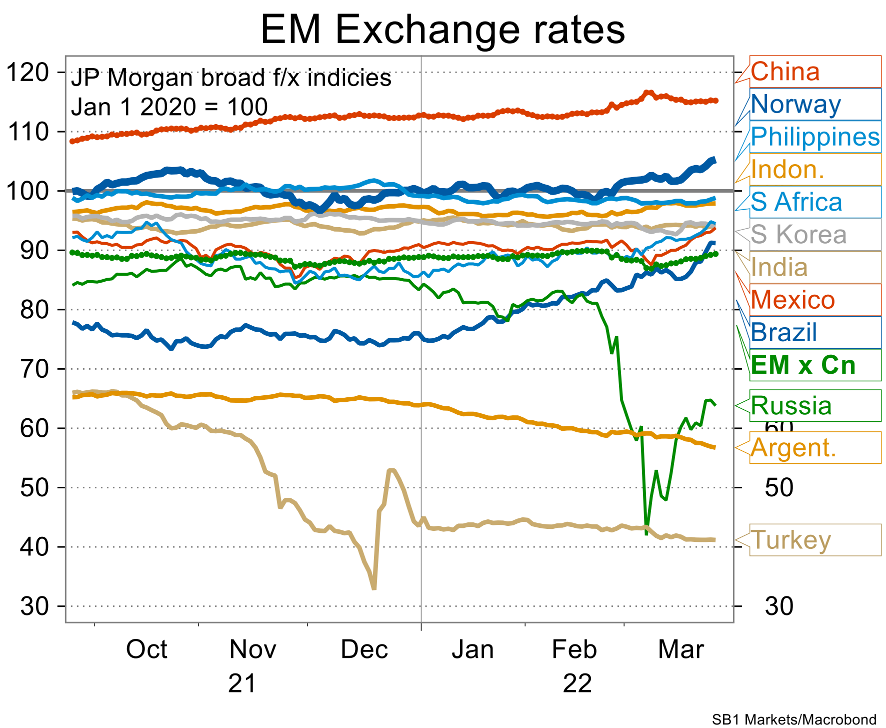
The surge in commodity prices is supporting both currencies

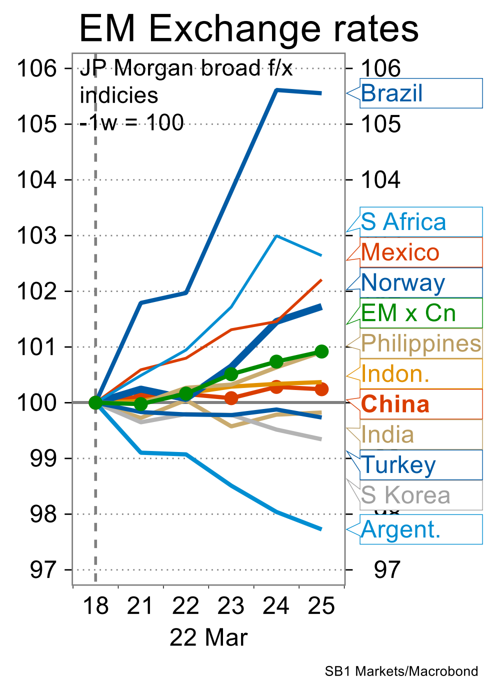


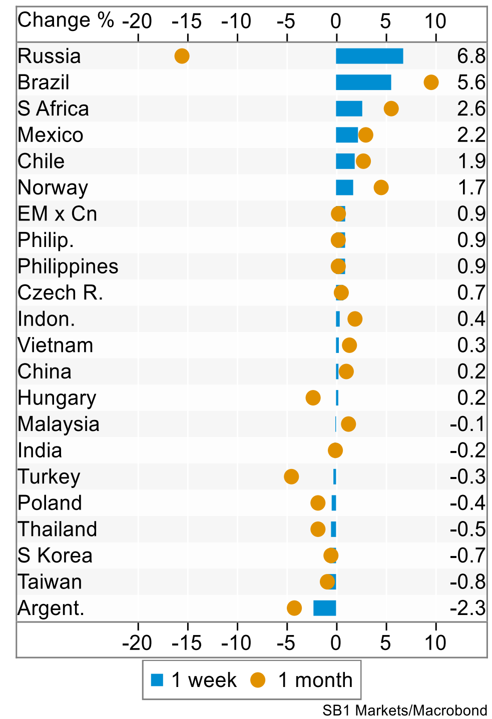
The two f/x indices are back to the 2011 parity (vs each other, from which they never since have deviated much)

The rouble recovered last week, just down 20% - in a real market??

A good week for other raw material producers too, NOK no exception







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