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Macro Weekly

Week 19/2022

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Highlights

The world around us

The Norwegian economy

Market charts & comments

Last week, part I

- **The War/Sanctions**
  - **No major news** from the East front, just a disastrous war going on – with no end in sight. (Today Putin may send a new message, and the Ukrainians of course want the war to come to an end)
  - **EU** has not finalised a decision to **end imports of Russian oil** by the end of 2022, as Hungary refuses to join. Biden says the G7 has agreed to stop buying Russian oil
  - **Other commodity prices** were mixed last week too. Oil prices rose (on fear of less Russian oil on the market), as did US gas prices (as European demand is increasing, we assume). However, metal prices fell further as did food prices
  - The **Russian rouble** has appreciated sharply recent weeks – and is now stronger than before the war. The country is still running a trade surplus, and capital is not allowed to leave the country (foreigners cannot sell their equities) reducing supply of RUB artificially. We are quite sure an open capital account would have lowered the RUB substantially. A strong RUB lowers domestic inflation. The central bank has already cut the signal rate by 6 pp to 14% (but it is still above the 9.5% pre-war level). The Russian PMIs recovered in April, but remain well below 50, implying a further contraction in economic activity
- **The virus**
  - In **Shanghai**, the lockdown was somewhat eased last week too, and activity has bottomed (but mobility is still close to the bottom). In Beijing mobility fell sharply last week, and the current zero tolerance policy is challenging for the economy, to put is mildly. Regrettably, the Chinese authorities will not utilise 'western' vaccines that are more effective than the Chinese versions (and many old Chinese have not been vaccinated)
  - **In South Africa, two new variants of Omicron**, BA.4 and BA.5, have led to a surge in new cases, an increase in hospitalisations, and some few deaths, as earlier infections but also vaccines gives less immunity then for other variants. Luckily, growth is already be slowing
- **PMIs/ISM**
  - The **global composite PMI** fell more than we assumed in April, by 1.7 p to 51.0 due to a steep decline in the service sector PMI in China. The Chinese manufacturing index fell sharply as well, both no doubt due to the Covid lockdowns in many cities. The downturn is still not as bad as in February 2020. In the rest of the world, the PMIs were in total close to unchanged. In the EMU the PMI gained more in April than it lost in March. The US PMIs fell, and the ISMs surprised at the downside too but as in the EMU, growth above trend is still reported. The Russian PMIs recovered but are still well below 50. The Hong Kong PMI shot up as Covid restrictions were eased. The Norwegian PMI rose to above 60 again (the 3rd best in the world). Delivery times rose, especially in China and price indices climbed again, 3 or the 4 global indices up to new ATH

Last week, part II

- **Central Banks**
  - **The Federal Reserve's FOMC** lifted the signal rate by 50 bps to 75 – 100 bps, as widely expected. The bank signalled further 50 bps hikes at the 2 upcoming meetings, which the stock market on Wednesday celebrated as a dovish sign (Powell said 75 bps hikes were not 'actively discussed'). In addition, Powell said a soft of softish landing was likely, as vacancies could be brought down (and then wage inflation) without lifting unemployment too much (and thus create a recession). On Thursday, stock market participants came to the opposite conclusion (which we think is the correct), and stocks tanked. Over the week, the S&P500 was close to unchanged, while the 10 y bond rate gained 23 bps to 3.12% (highest since late 2018), due to a 25 bps increase in the 10 y TIPS real rate to 0.26% (and from -100 bps in early March). Inflation expectations fell slightly. BTW, German rates climbed to well above 1%, for the first time since 2014. In the very short end of the curve, rates fell marginally. We still think the Fed will fight inflation by hiking rates until wage inflation is brought under control, and profit margins squeezed. The QT program (reducing bond holdings) will start in June, adding further pressure on yields
  - **Bank of England** lifted the bank rate by 25 bps to 100 bp, as expected. The Bank expect inflation to climb to 10% as regulated energy prices will be sharply lifted in April and October. The hike in the price level will lower real wages substantially. Consumption will be depressed, and the bank expects a decline in GDP in Q4 and in Q1 (a technical recession). Lower demand and a gradual reduction in energy prices will then bring inflation rapidly down. The market thought the Bank sounded somewhat dovish, and short term rates fell slightly. In the long end, GBP yields followed the global market up
  - **Norges Bank** reiterated that the signal rate will be hiked in June, and if anything the bank seem to put more emphasis on the upside risk vs wage and price inflation, than on the downside risk to growth
  - A **lot of other central banks** hiked their signal rates last week, like Iceland and Brazil by 1pp, Poland by 75 bps
- **China**
  - **Both exports and imports** were better than expected in April but both are down 7% in volume terms since January, no doubt due to the lockdowns
- **USA**
  - **Nonfarm payrolls** grew a tad faster than expected in April, but the **unemployment rate** did not fall further, and underlying **wage inflation** may have slowed marginally. However, **vacancies** soared in March, in April the SMEs still want **to hire**, are **not able to fill positions**, and the **plan to increase compensation** at a rapid pace. And wage inflation is anyway too high for comfort – and it is too high to bring inflation down to 2%. In Q1, **productivity** nosedived, and **unit labour costs** soared – no doubt an outlier. Still, underlying growth in productivity and ULC is far from reassuring
- **EMU**
  - **Unemployment** is trending down but at slower pace. The level is the lowest level since 1981!
  - **Retail sales** fell by 0.4% and the short term trend is flattish. Some money is transferred to spending on services, and there is a war going on in the backyard – and real wage are falling rapidly
- **Norway**
  - **Existing home prices** flattened in April, following the 4% surge in Q1. Prices rose further in most cities, including Oslo. Sales are still lower than during the pandemic but the inventory fell to a new ATL. No crisis, yet

The Calendar: US annual inflation down? Chinese April data. CPI & GDP in Norway

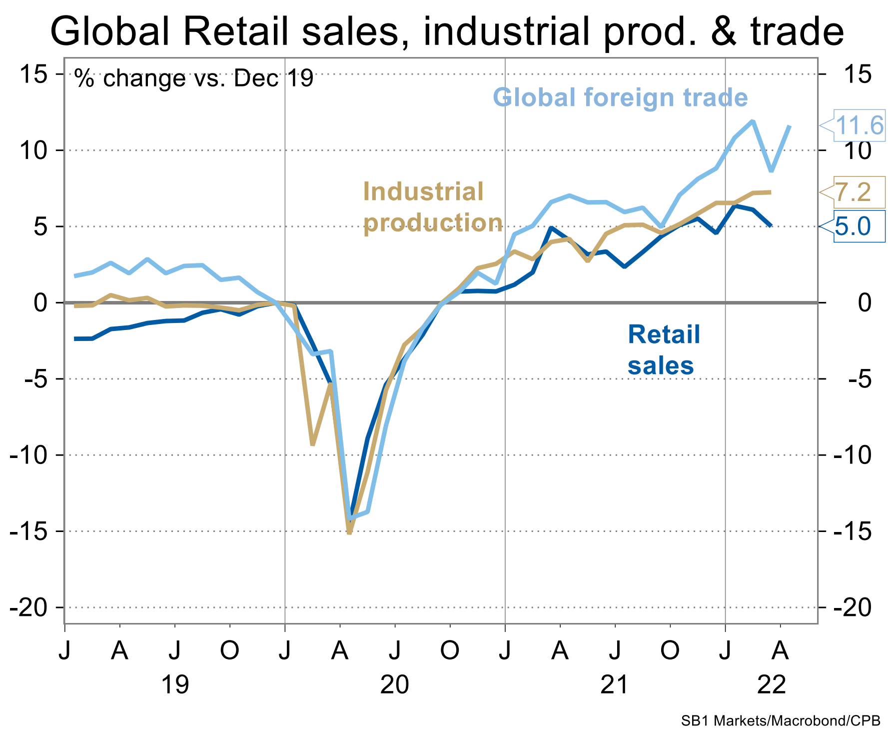
Time	Count.	Indicator	Period	Forecast	Prior
Monday May 9					
08:00	NO	Payrolls, wages	Q1		
08:00	NO	Ind Prod Manufacturing MoM	Mar	(1.5%)	-2.1%
Tuesday May 10					
08:00	**NO**	**CPI YoY**	**Apr**	**4.7%**	**4.5%**
08:00	**NO**	**CPI Underlying YoY**	**Apr**	**2.4%**	**2.1%**
11:00	GE	ZEW Survey Expectations	May	-42.5	-41
12:00	US	NFIB Small Business Optimism	Apr	92.9	93.2
Wednesday May 11					
03:30	CN	PPI YoY	Apr	7.8%	8.3%
03:30	CN	CPI YoY	Apr	1.9%	1.5%
14:30	US	CPI MoM	Apr	0.2%	1.2%
14:30	US	CPI Ex Food and Energy MoM	Apr	0.4%	0.3%
14:30	**US**	**CPI YoY**	**Apr**	**8.1%**	**8.5%**
14:30	**US**	**CPI Ex Food and Energy YoY**	**Apr**	**6.0%**	**6.5%**
20:00	US	Monthly Budget Statement	Apr	$220b	-$193b
Thursday May 12					
08:00	NO	Vacancies	Q1		
08:00	NO	Construction cost index, YoY	Apr		11.9%
08:00	SW	CPI YoY	Apr	6.2%	6.0%
08:00	SW	CPIF Excl. Energy YoY	Apr	4.5%	4.1%
08:00	UK	Monthly GDP (MoM)	Mar	0.0%	0.1%
08:00	UK	GDP QoQ	1Q P	1.0%	1.3%
08:00	UK	Manufacturing Production MoM	Mar	0.0%	-0.4%
14:30	US	PPI Final Demand YoY	Apr	10.7%	11.2%
14:30	US	Initial Jobless Claims	week	190k	200k
Friday May 13					
08:00	**NO**	**GDP Mainland MoM**	**Mar**	**(0.7%)**	**0.5%**
08:00	NO	GDP Mainland QoQ	1Q	-0.5%(0.7)	1.4%
11:00	EU	Industrial Production SA MoM	Mar	-1.8%	0.7%
14:30	US	Import Price Index ex Petroleum	Apr	1.2%	1.1%
16:00	US	U. of Mich. Sentiment	May P	64.0	65.2
During the week					
	CN	Aggregate Financing CNY	Apr	2200b	4650b
	CN	New Yuan Loans CNY	Apr	1550b	3130b
Monday May 16					
04:00	**CN**	**Industrial Production YoY**	**Apr**	**0.5%**	**5.0%**
04:00	**CN**	**Retail Sales YoY**	**Apr**	**-6.1%**	**-3.5%**
04:00	CN	Fixed Assets Ex Rural YTD YoY	Apr	7.0%	9.3%
04:00	CN	Property Investment YTD YoY	Apr	-1.5%	0.7%
04:00	CN	Residential Property Sales YTD	Apr		-25.6%

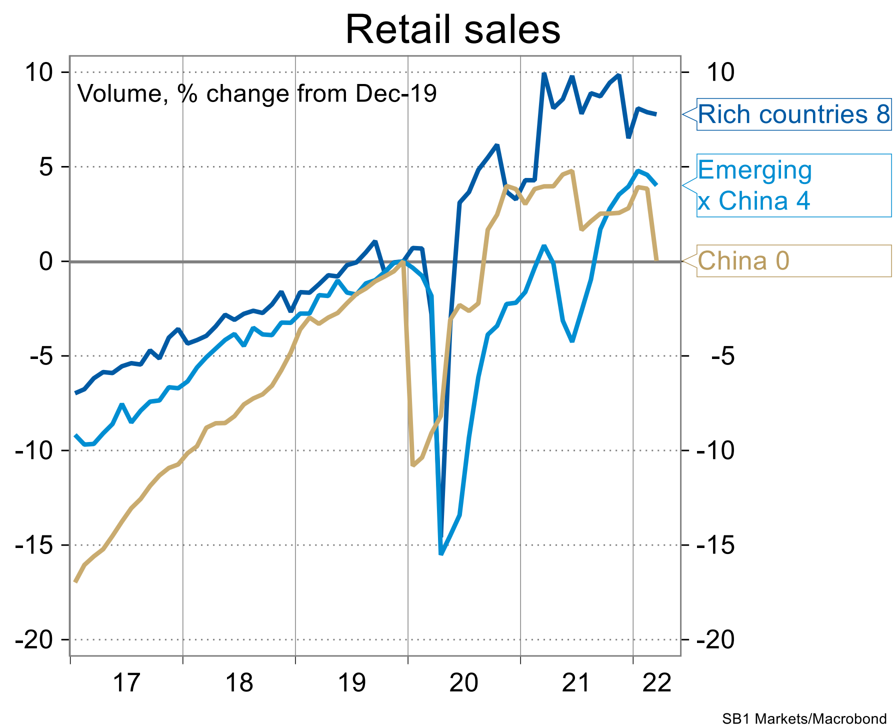
- **Global auto sales**
  - » **USA** has reported an visible uptick in auto sales in April, while sales in **EMU** remained close to unchanged following the large drop in March. In March sales also fell sharply in **China**, and in **Russia**, and may have fallen further in April. So far other **EMs** have reported small changes in April sales
- **China**
  - » **How bad was 'lockdown' April?** Expectations are not upbeat, for good reasons. Surveys were dismal. However, whatever data may turn out to be, they are not relevant if we do assume that the fight against the virus will be fought the same way for a long period of time (which is not unlikely, but we think is not the most likely outcome either)
- **USA**
  - » **Peak inflation!** Annual CPI inflation (both headline & the core) will very likely decline in April as prices surged m/m last April, and no such price hike are likely in April this year. Lower inflation is of course anyway good news but the longer-term outlook (and Fed's policy response over time) is far more decided by wage inflation
  - » **Atlanta Fed** will report its **median wage** estimate at Thursday or Friday
- **EMU**
  - » **Industrial production** probably fell sharply in March
- **Sweden**
  - » **CPI inflation** is expected further up
- **Norway**
  - » **CPI inflation** will probably accelerate in April. Market electricity prices fell slightly but the tax returned to a normal level, in sum close to unch. Gasoline prices fell slightly. However, we expect the core inflation rate to reverse the decline last month – lifting the annual rate 0.3 pp 2.4% and the headline rate by 0.2 pp to 4.6%
  - » **Mainland GDP** very likely grew at a decent pace in March, as the recovery in services continued. Retail trade shot up as well – but manufacturing production contributed at the downside

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

Global retail sales remained strong in February. Emerging markets on the way up

Industrial production on the right track too – probably global foreign trade too

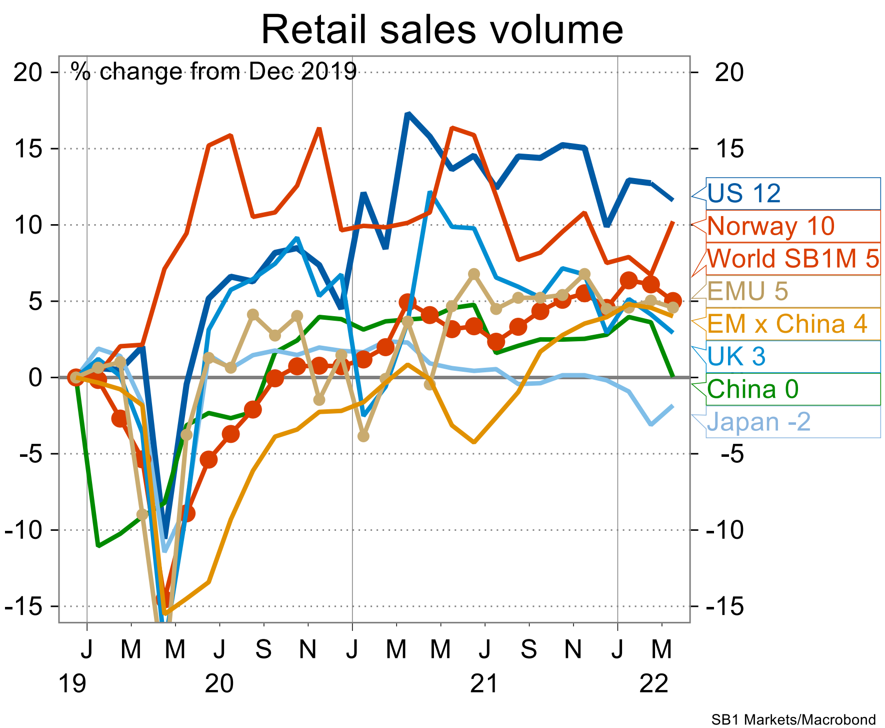


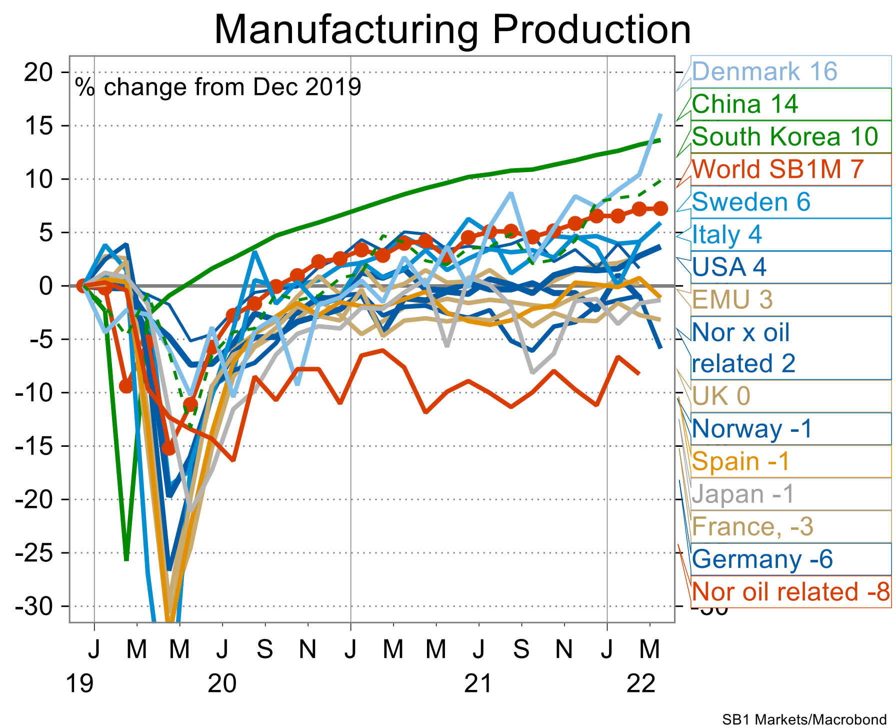


Global trade: The last months are estimates from the Kiel Institute

Retail sales down in March too, industrial production probably further up

The retail sales trend is very likely down in the rich part of the world. Manufacturing prod. still OK

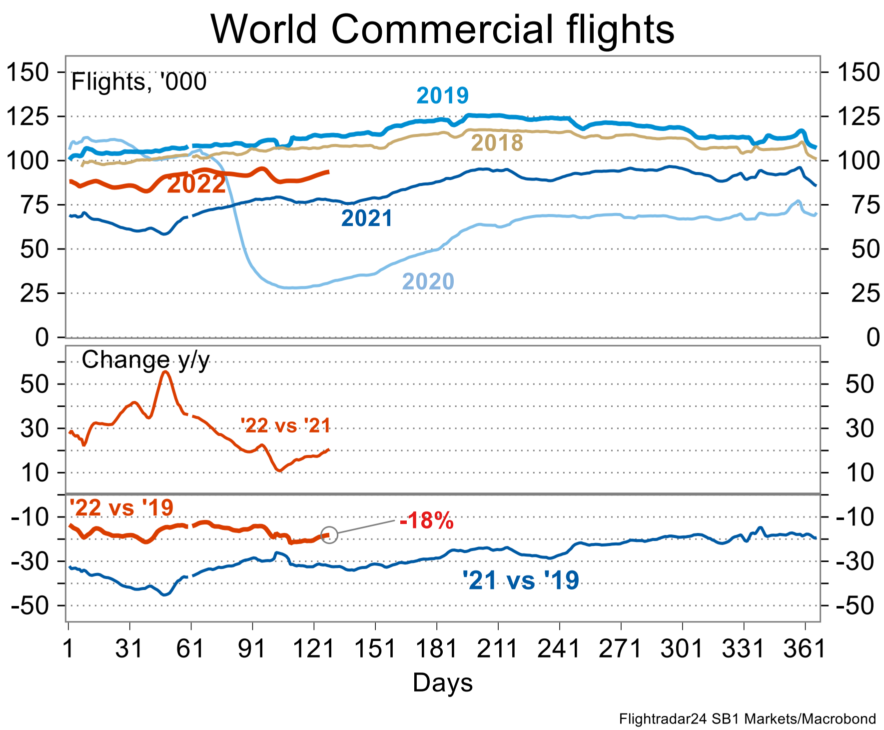


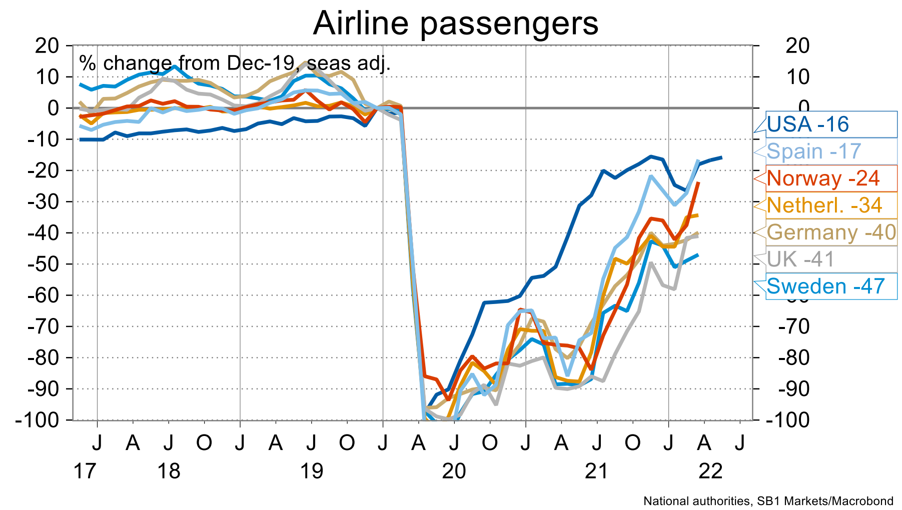


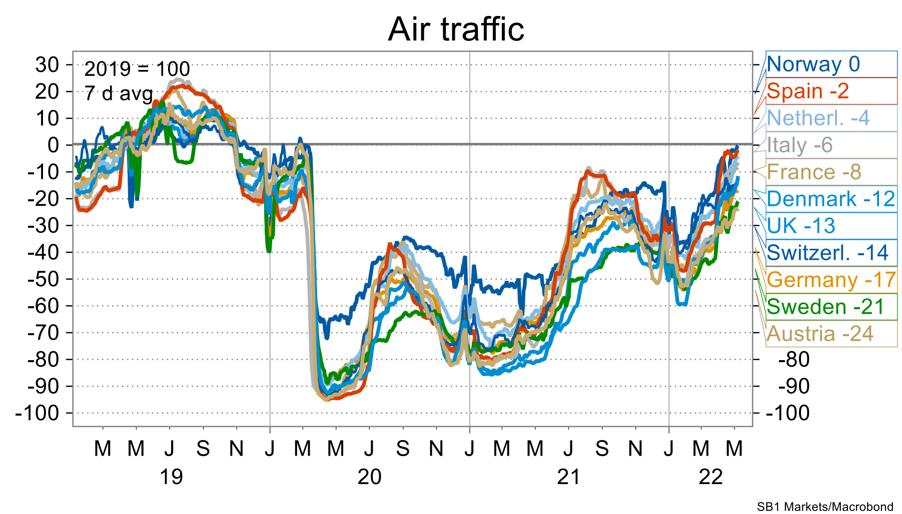
- **Retail sales** in Emerging Markets x China are recovering but is far below pre-pandemic trends
- **Manufacturing production** has been hampered by a deep decline in auto production. The manufacturing PMIs are down from the peak but are still signalling growth above trend

Global airline traffic up last week – still 18% down from 2019

Geopolitics? Trouble in China? Western Europe & US on the way up



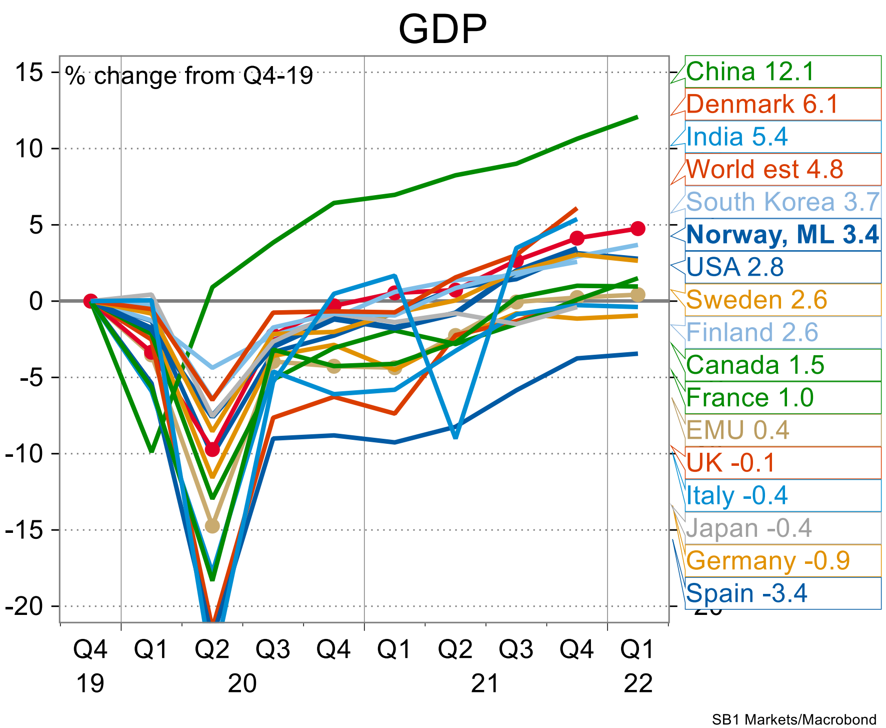


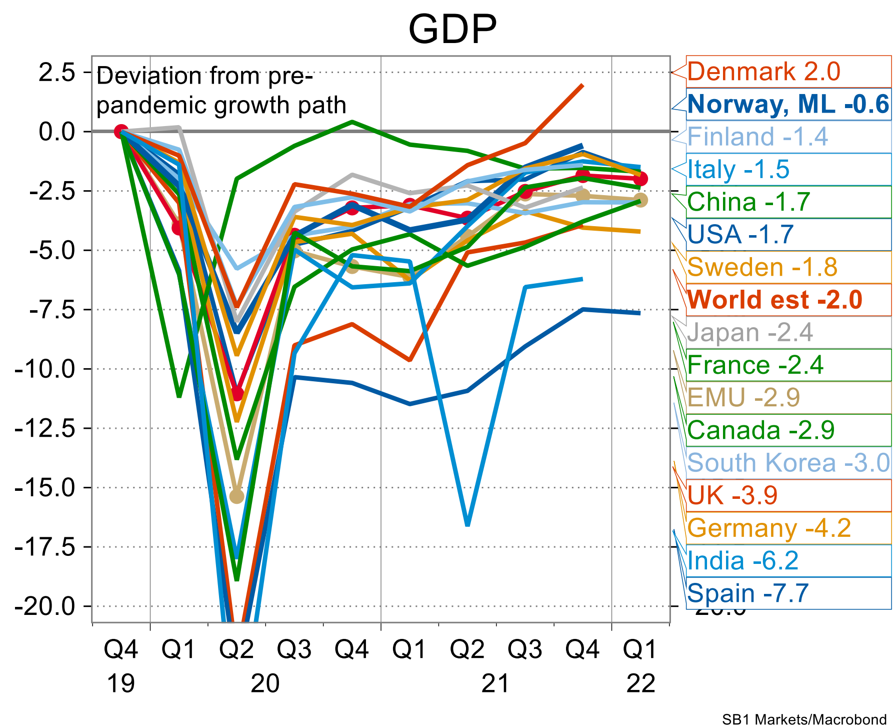


Global trade: The last months are estimates from Kiel Institute

GDP slowed in Q1, to 0.6% (2.4% annualised) from 1.4% (5.7%) in Q4

GDP is still below the pre-pandemic growth path, some 2%

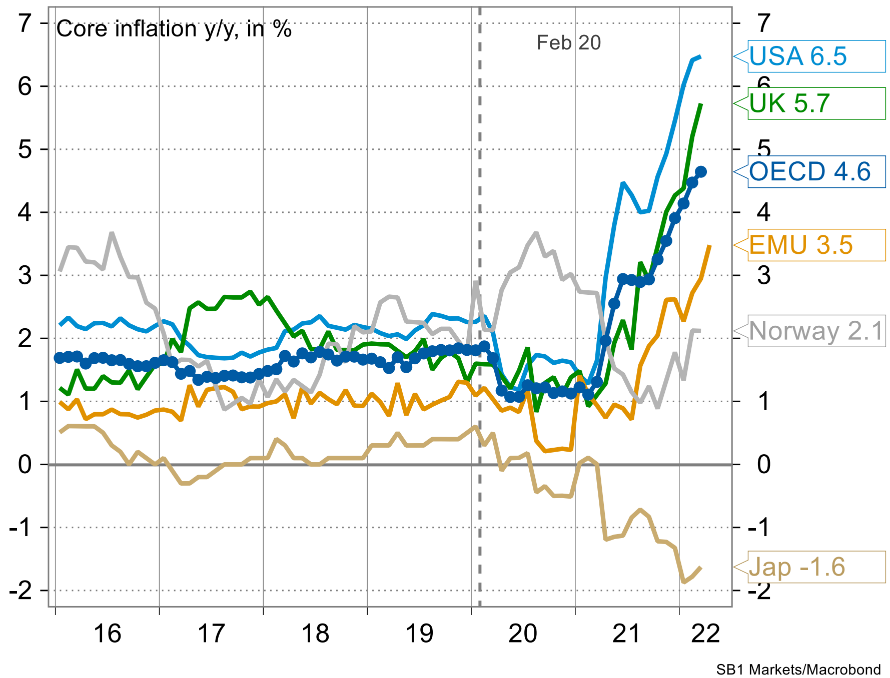




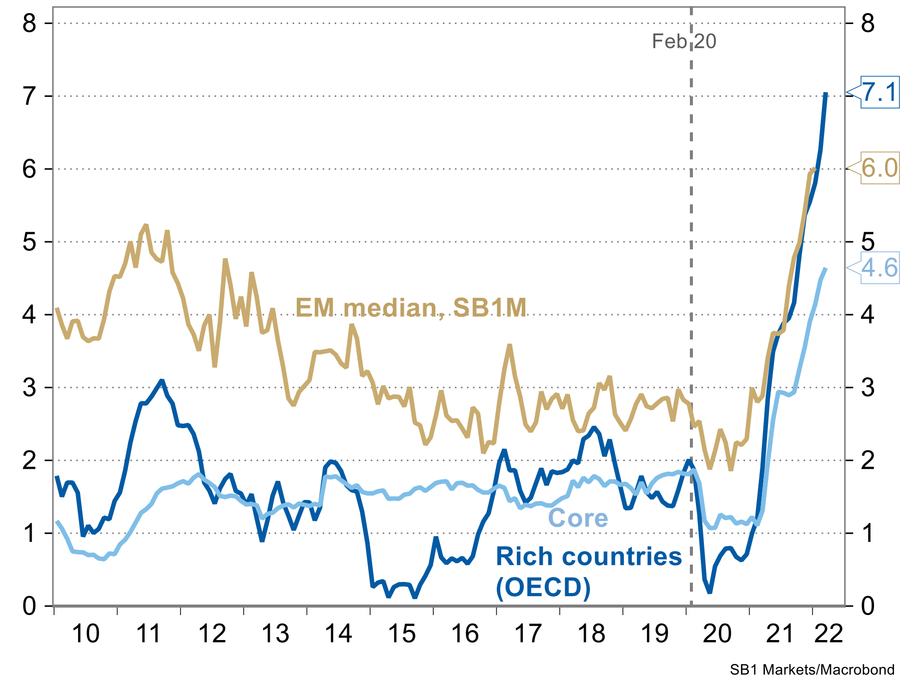
Inflation still rapidly on the way up

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

Core CPI Inflation

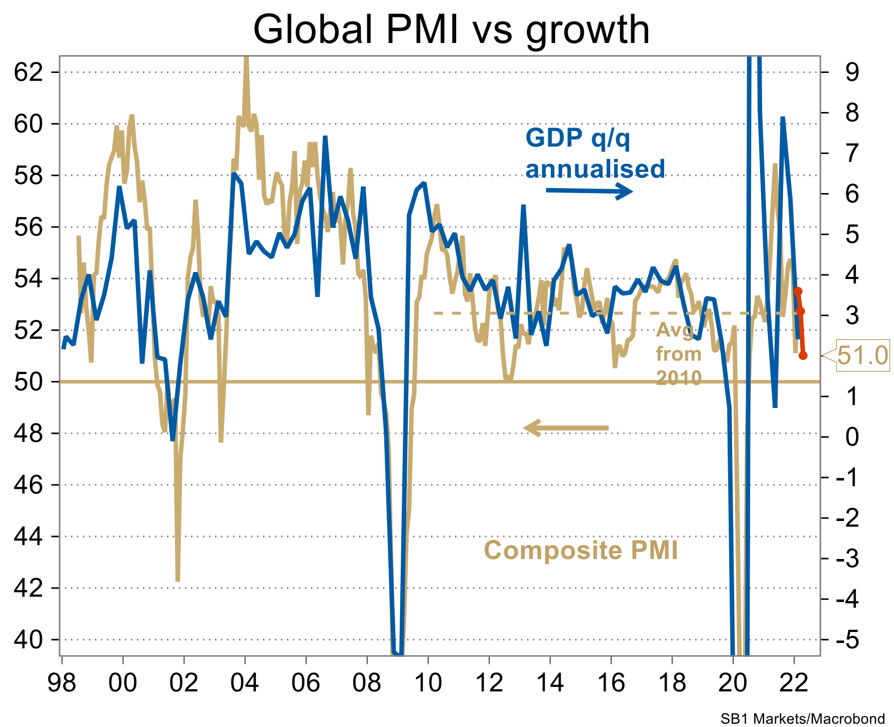


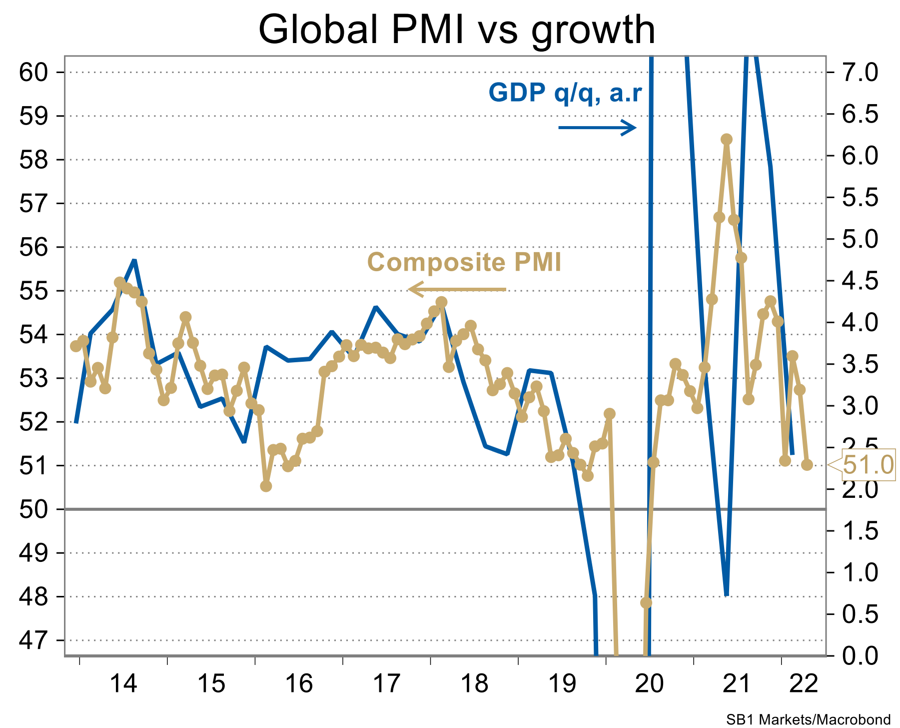
CPI Inflation



The global economy slowed further in April – almost entirely due to China

The global index fell 1.7 p to 51.0, the weakest level in 2 years

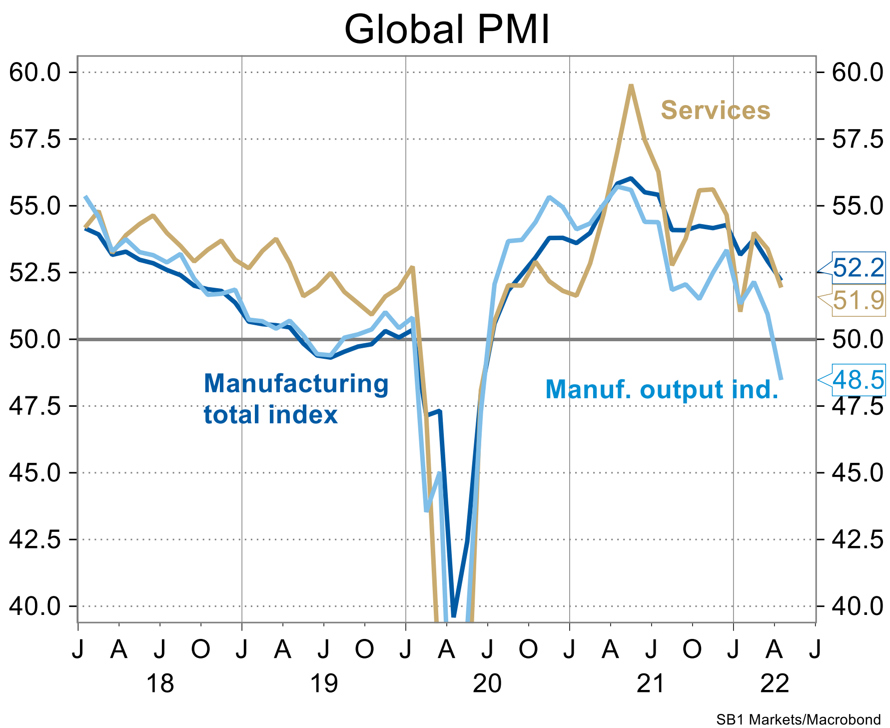


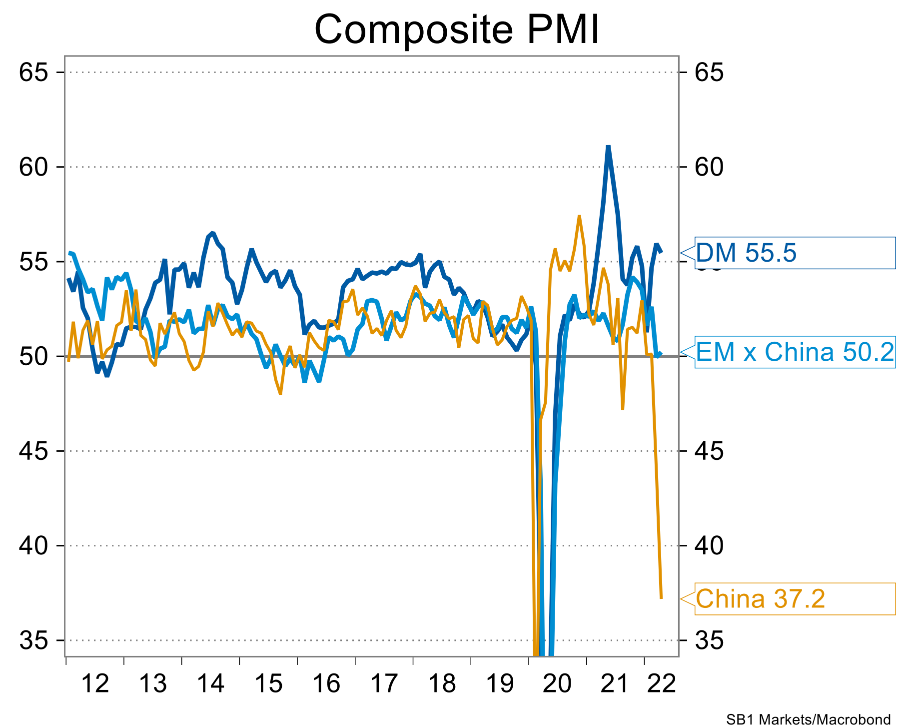


- A large, further decline in the service sector PMI in China in April, led to a larger decline in the global composite PMI than we assumed
- However, barring the decline in the Chinese PMIs (the manufacturing output index also 'collapsed'), the global index was just marginally down, with an uptick in EM ex China (India and Hong Kong contributed) and in the EMU. The EMU PMI was above the February level in April!
- **Delivery times** rose – and all **price indices** rose – and most to new ATH. So war & sanctions (and Chinese lockdowns) have some impacts…

The manufacturing output straight down – but stable ex China!

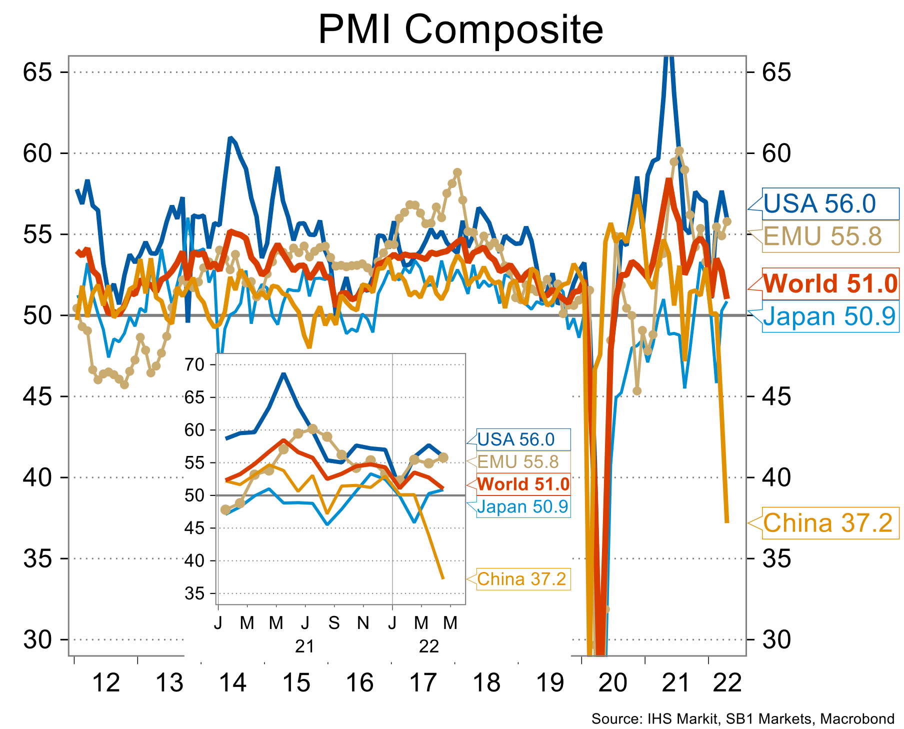
The service sector PMI also just marginally down ex China

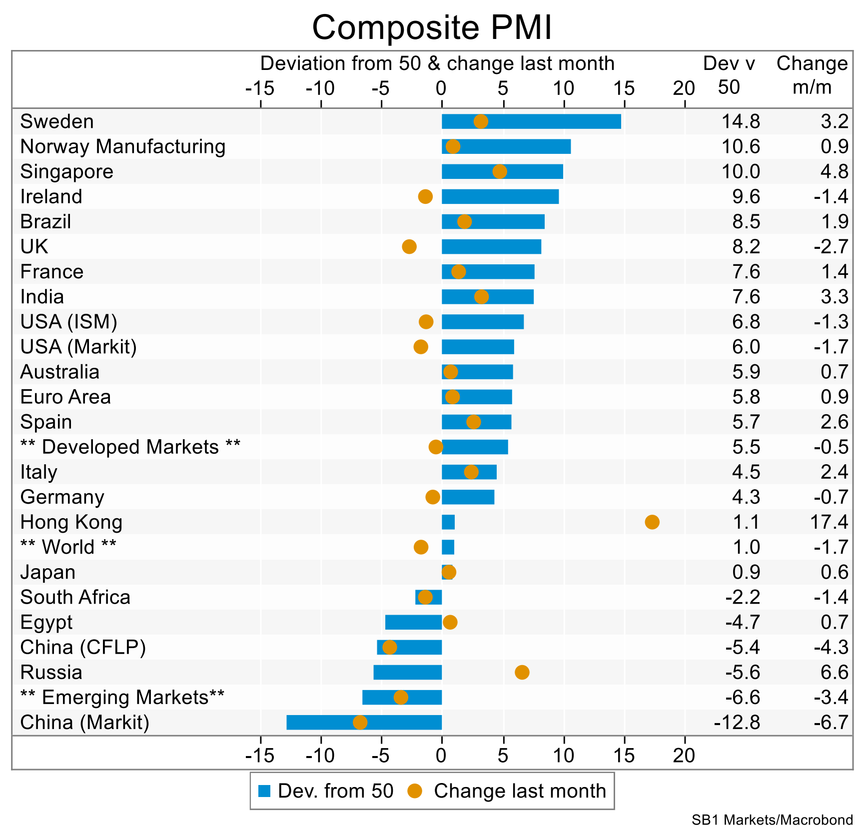




The global composite PMI down, mostly due the lockdown setback in China

The total down 1.7 p to 51.0, more than we assumed, China contributed by 1.3 p

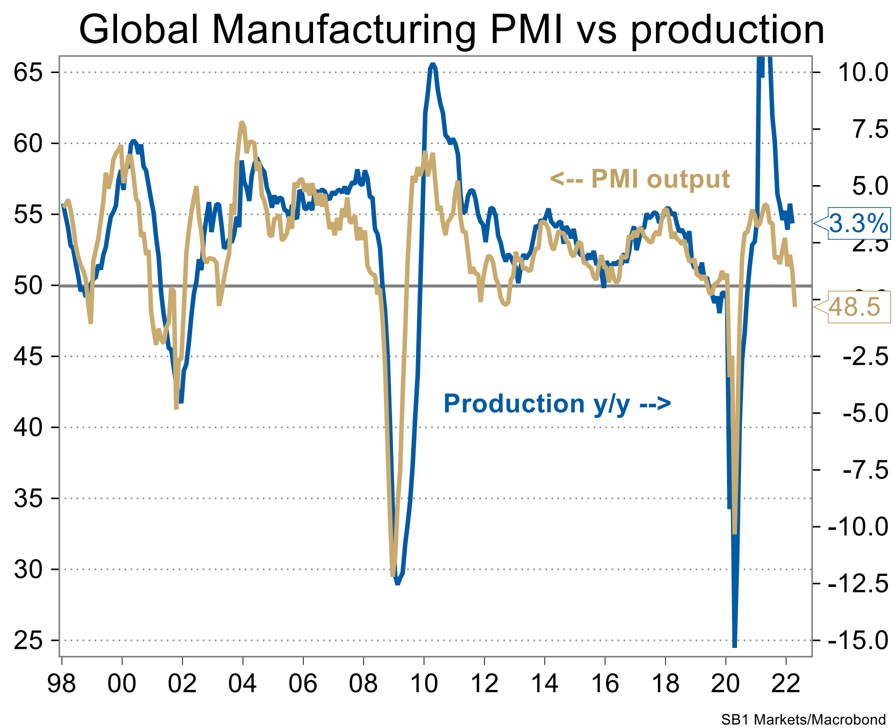


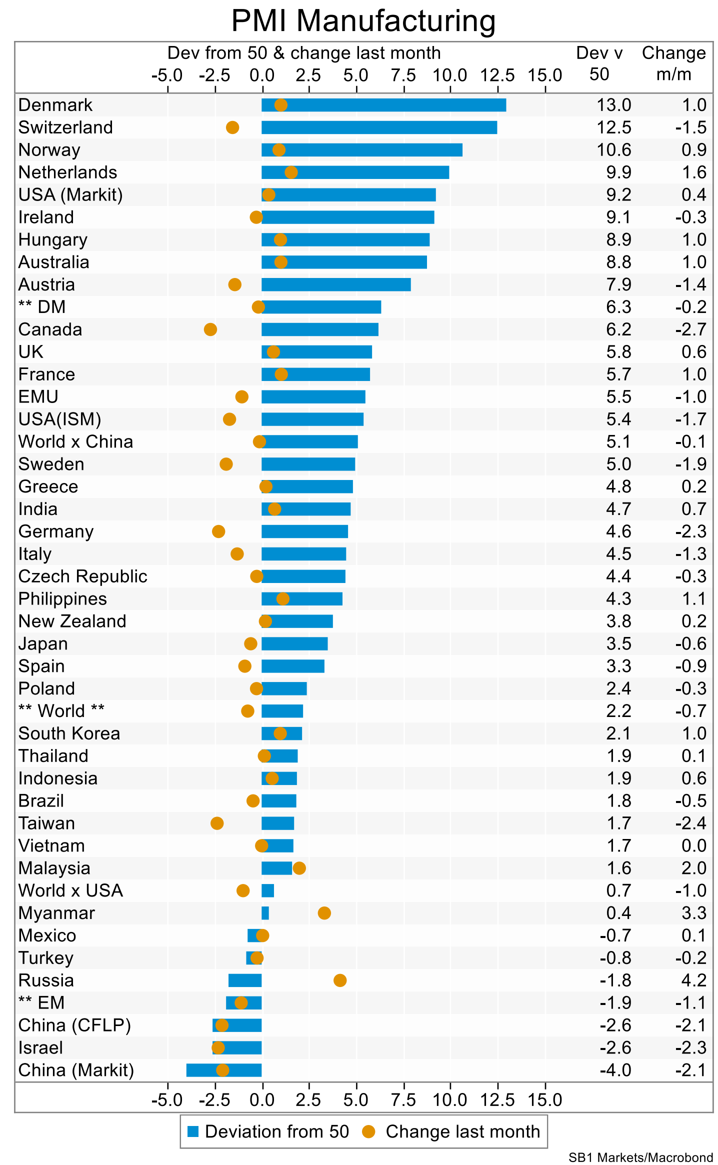


- 14 countries/regions up in March (down from 7), and 11 down (from 15)
- **The declines in Russia and China** in March and April have been harsh, even if the Russian PMIs recovered in April. War & sanctions are hurting the Russian economy brutally, according to businesses. China is fighting the virus with its 'impossible' zero tolerance policy. The Hong Kong PMIs were terribly depressed, but recovered by 17.4 p to 51.1. Regrettably, vaccination is far lower in China than in H-K, especially among the elderly
  - » Other EMs OK: Brazil rose further, as did India
- **The rich countries (Developed Markets, DM) PMI** declined 0.5 p due to a 1.7 p drop in the **US,** while EMU gained 0.9 p, <u>more than the decline in March</u>
- **Sweden** still has the pole position, ahead of Singapore, and Ireland)
- (**Norway** does not compete here, we just have a manufacturing PMI. The level would have yielded a 2nd place in the composite race)

Manufacturing headline PMI down 0.7 p to 52.2, and the output index to 48.5

7 of 43 surveys below 50. <u>Europe at the top, China at the bottom, Russia close to the bottom</u>



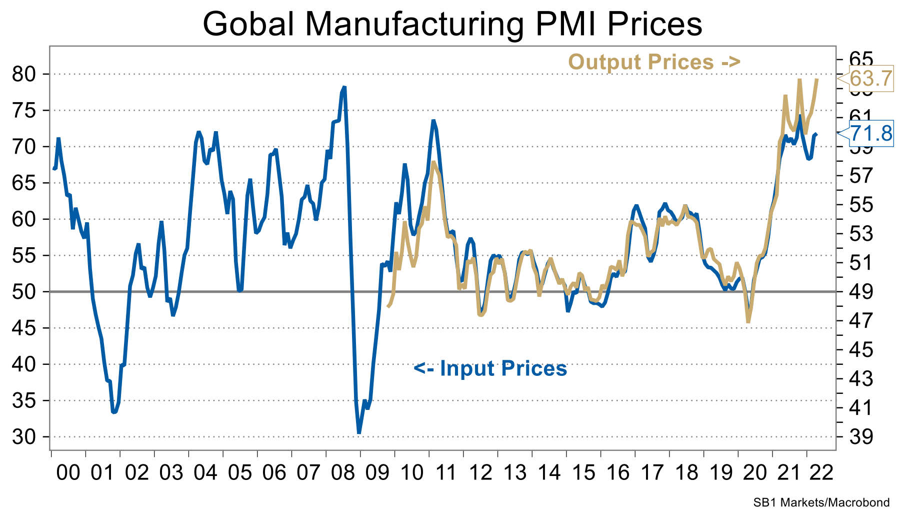


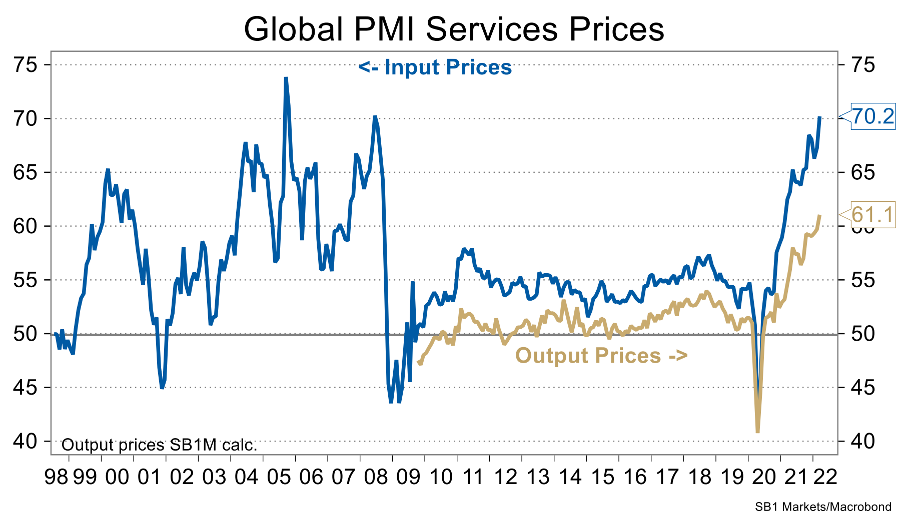
	Dev v 50	Change m/m
Denmark	13.0	1.0
Switzerland	12.5	-1.5
Norway	10.6	0.9
Netherlands	9.9	1.6
USA (Markit)	9.2	0.4
Ireland	9.1	-0.3
Hungary	8.9	1.0
Australia	8.8	1.0
Austria	7.9	-1.4
** DM	6.3	-0.2
Canada	6.2	-2.7
UK	5.8	0.6
France	5.7	1.0
EMU	5.5	-1.0
USA(ISM)	5.4	-1.7
World x China	5.1	-0.1
Sweden	5.0	-1.9
Greece	4.8	0.2
India	4.7	0.7
Germany	4.6	-2.3
Italy	4.5	-1.3
Czech Republic	4.4	-0.3
Philippines	4.3	1.1
New Zealand	3.8	0.2
Japan	3.5	-0.6
Spain	3.3	-0.9
Poland	2.4	-0.3
** World **	2.2	-0.7
South Korea	2.1	1.0
Thailand	1.9	0.1
Indonesia	1.9	0.6
Brazil	1.8	-0.5
Taiwan	1.7	-2.4
Vietnam	1.7	0.0
Malaysia	1.6	2.0
World x USA	0.7	-1.0
Myanmar	0.4	3.3
Mexico	-0.7	0.1
Turkey	-0.8	-0.2
Russia	-1.8	4.2
** EM	-1.9	-1.1
China (CFLP)	-2.6	-2.1
Israel	-2.6	-2.3
China (Markit)	-4.0	-2.1

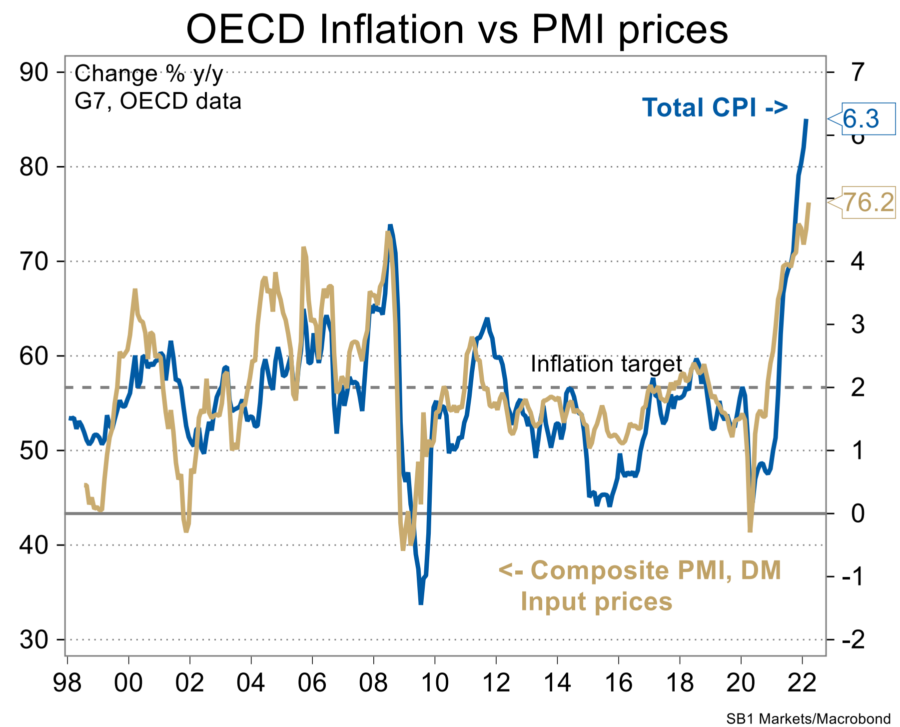
- The **manufacturing output index** fell 2.4 p to 48.8, in line with our forecast based on preliminary data for DMs and China
  - 46% of countries/regions reported higher total PMIs last month, up from 35% in March
  - **European countries** still dominate the top of the list. Norway is no. 3
  - The Chinese indices fell sharply. Rest of EM Asia was broadly up, as was Brazil
  - Russia reported a solid uptick from a very low level in March, but is still well <50
  - **Norway** reported a minor decline – and the level is well above average, at 60.6

All aggregated price indices up in April – and 3 of 4 up to ATH

Which of course does not signal a rapid decrease in monthly inflation rates

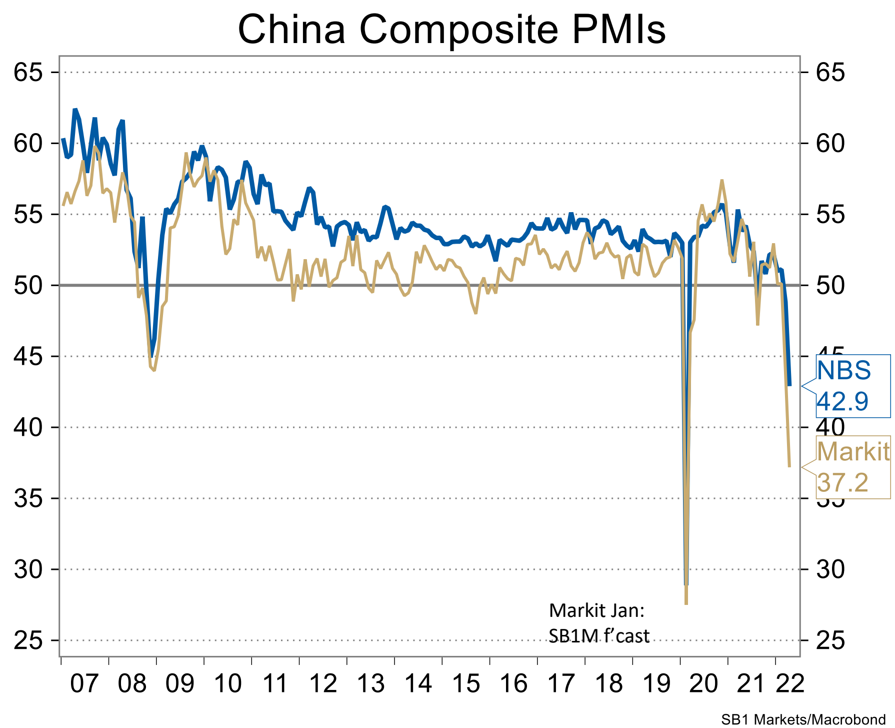


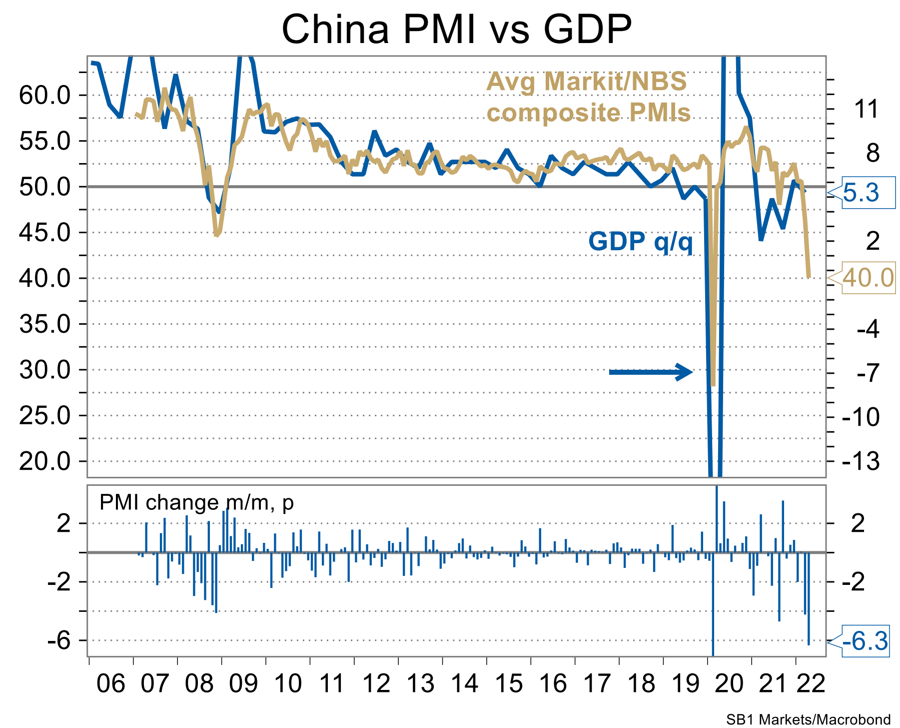




Both PMI data sets fell sharply in April, and Markit's even more than we assumed

The composite average declined 6.3 p to 40, the 2nd lowest ever, as lockdowns reduced economic act.

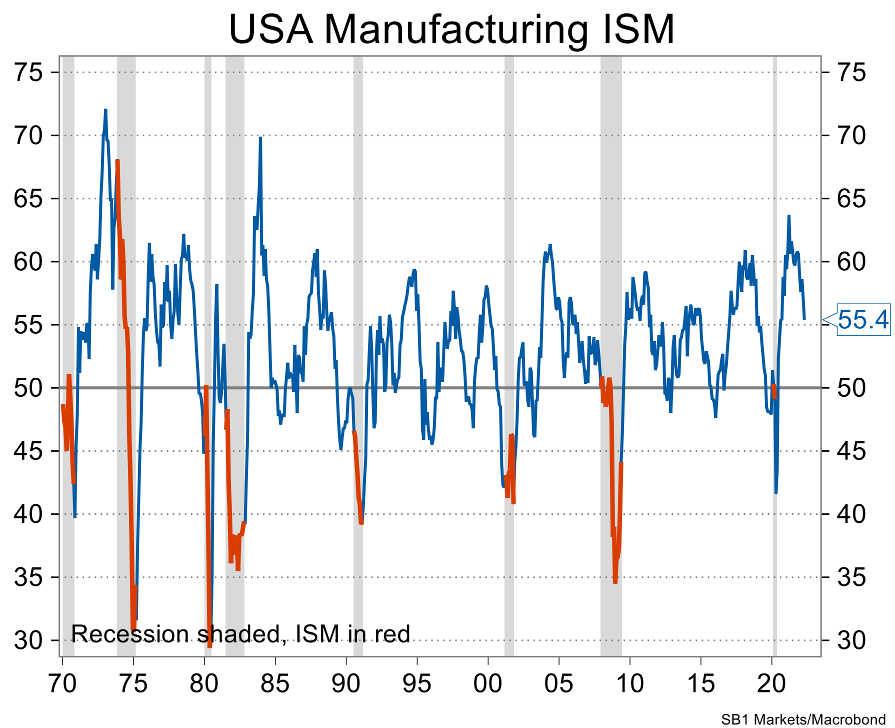


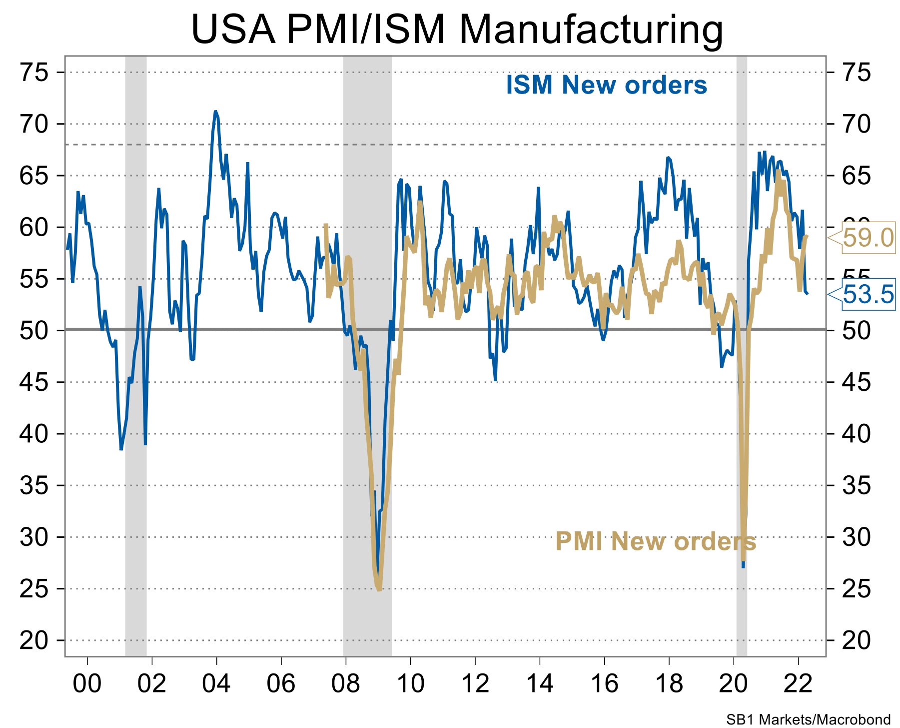


- **Markit's** service sector PMI declined almost 6 p, following the 8 p drop in March, down to 36.3 – expected down 1 p to 41. The composite index fell 6.7 p to 37.2, the 2nd lowest ever, just Feb-20 was worse
- The **CFLP/NBS composite PMI** nosedived 5.9 p to 42.9, also the 2nd weakest. **The average of the two PMI data sets** declined to 40.0, signalling zero growth in the Chinese economy – but the calibration is far from perfect
- The PMIs are signalling that the lockdowns have hurt the economy badly, but as they are less rigorous (on average, for the whole country), the economic impact is less than during the first lockdowns in February 2020. The impact will of course be felt in many global supply chains, even if restrictions are now gradually eased in some cities

Manufacturing ISM headed down, and will continue downwards?

The total index fell 1.7p to 55.1, expected up to 57.8



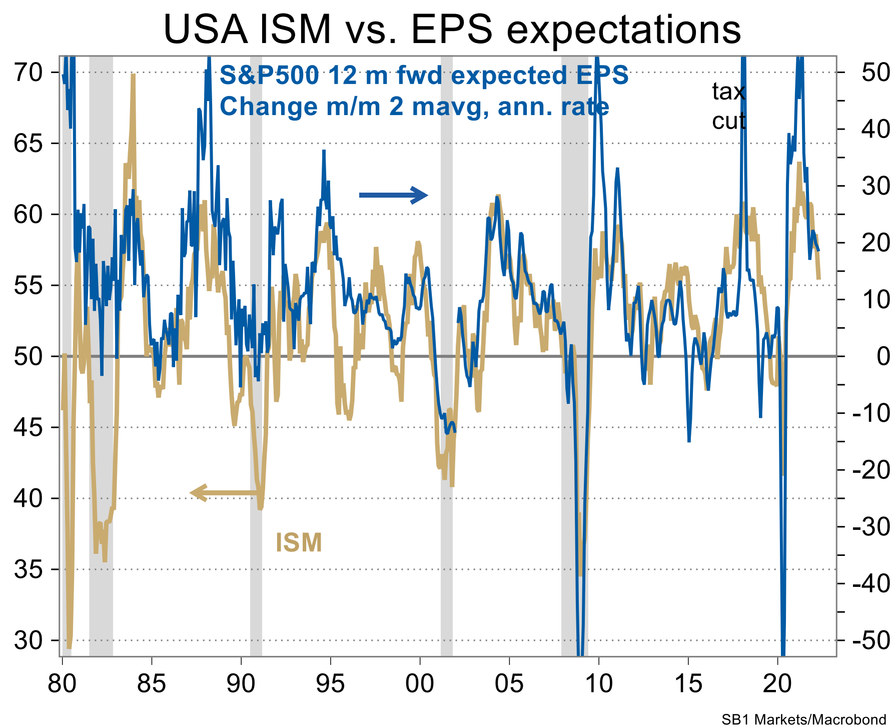


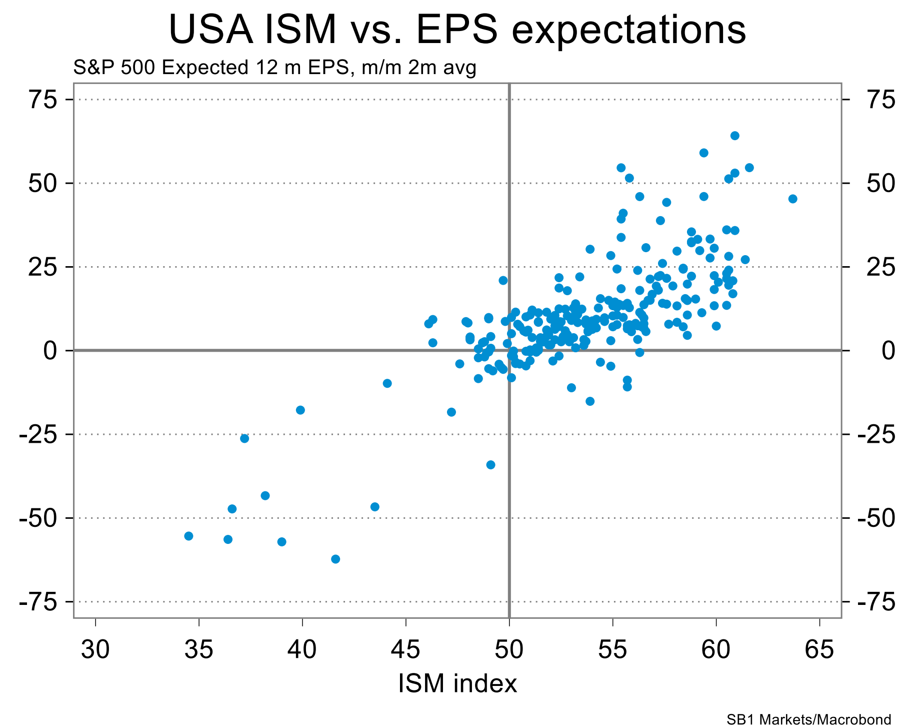
The **ISM manufacturing index is trending down but not yet at low level. However, at the current speed of decline, we are soon there**

- Last month, 17 of 18 manufacturing sectors reported growth (15 the prev. month), just 1 sector report a decline (Petroleum & Coal products, down from 2 sectors last month)
  - » The **new orders** index fell just 0.3 p to 53.5 – but it was above 60 in February
- 36 commodities saw **price increases** (from 43, at the peak 56 commodities). Just natural gas prices were reported as falling (strange, they actually rose)
- 18 commodities were reported in **short supply,** down from 24 (and far below the peak at 50 commodities a few months ago)
- **In their comments**, companies still report supply chain issues, now due to China (and not the war in Ukraine) – but some easing is reported

When the ISM turns south, growth in expected earnings always join

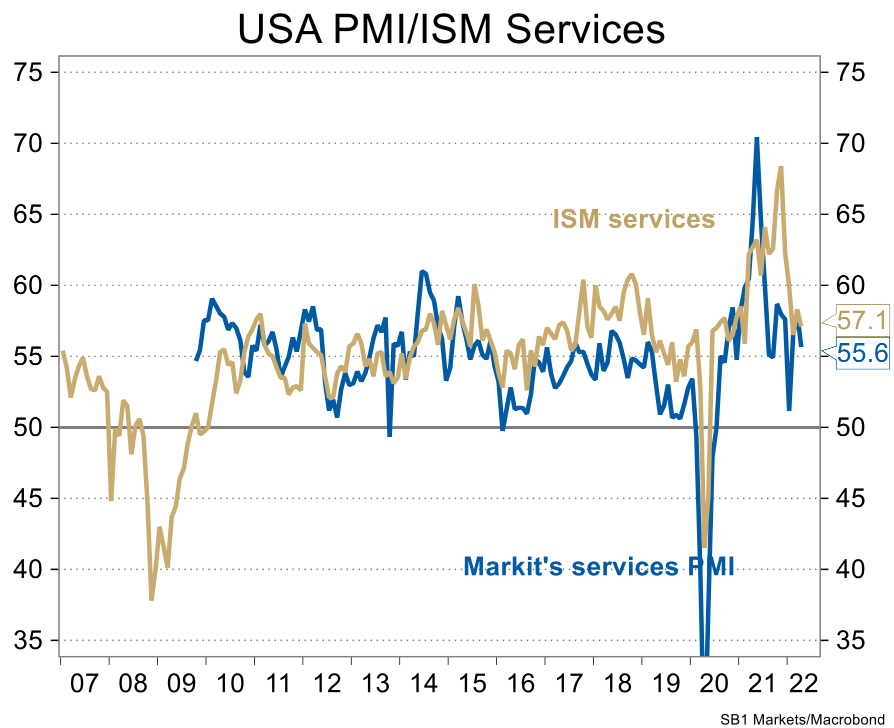
At 55, decent earnings growth is normally assumed. But not at 50

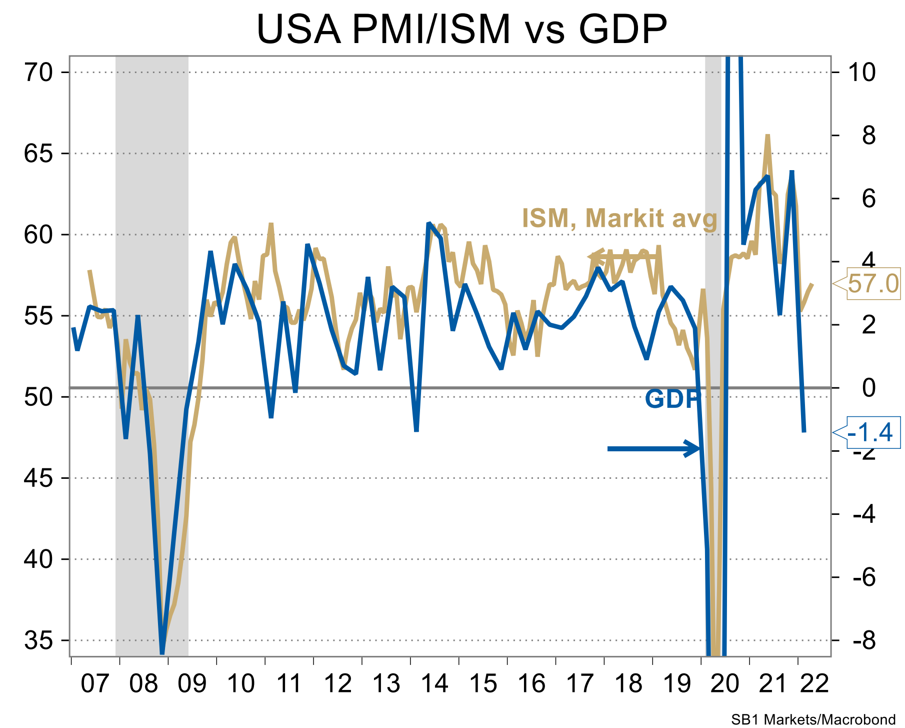




Services ISM down but still at a high level at 57.1

Markit's services PMI confirmed down. The grand PMI/ISM total at 57.0, signals growth above trend

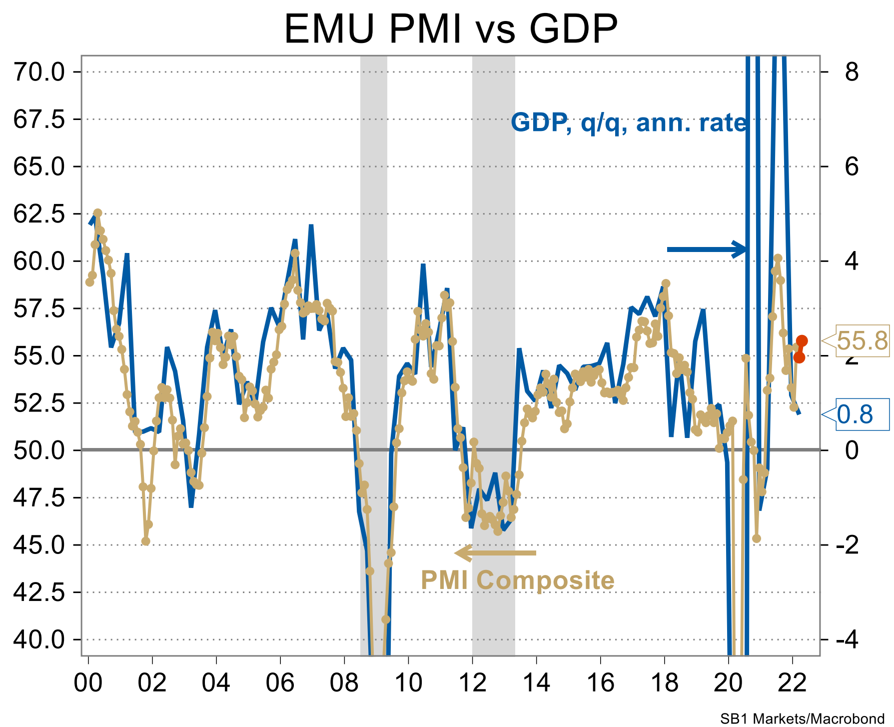


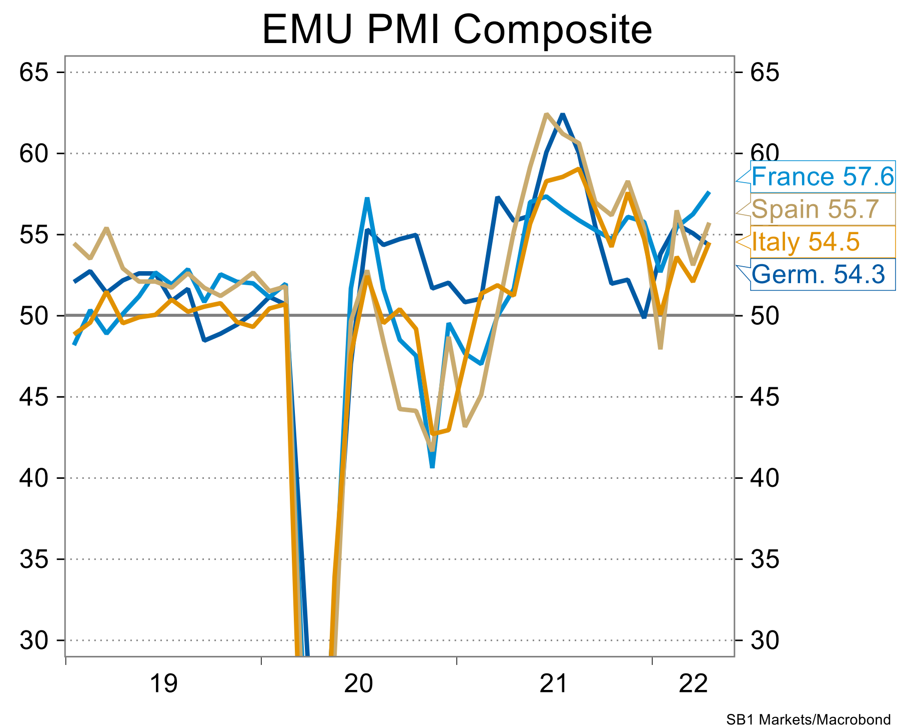


- **The ISM services index** lost 1.2 p to 57.1 in April, expected up 0.2 p. The level is well below the re-opening spikes but above average, signalling growth above trend
- The price index rose marginally to 84.6, an ATH – like the other price indices in the PMI/ISM data set, check next page
- Together with their manufacturing indices, the **PMI/ISMs** signal a 3% GDP growth rate

PMI stronger in April thanks to solid growth in services

The composite PMI up 0.9 to 55.8, in line with the preliminary estimate

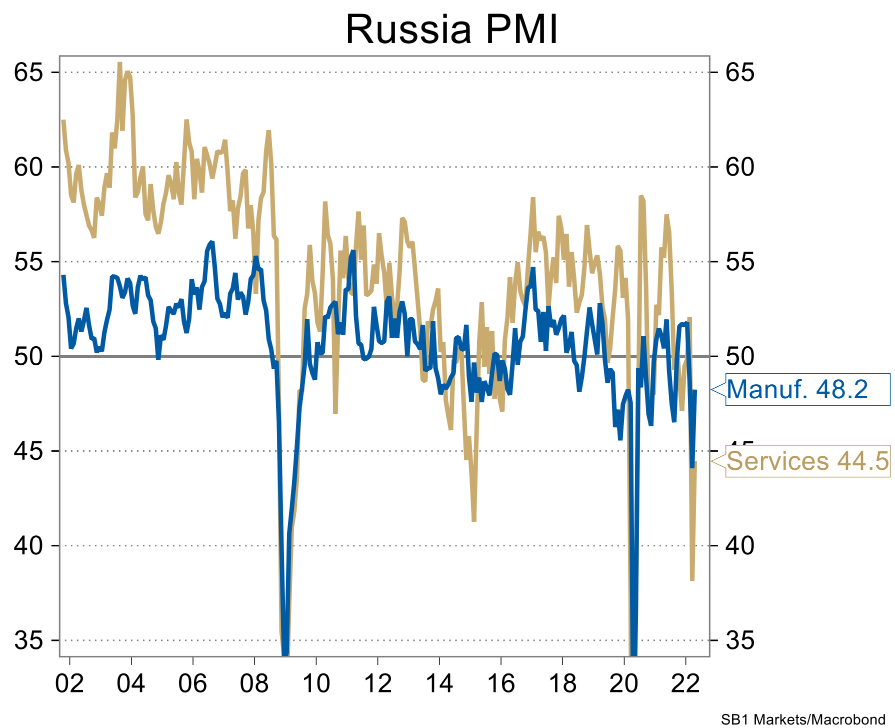


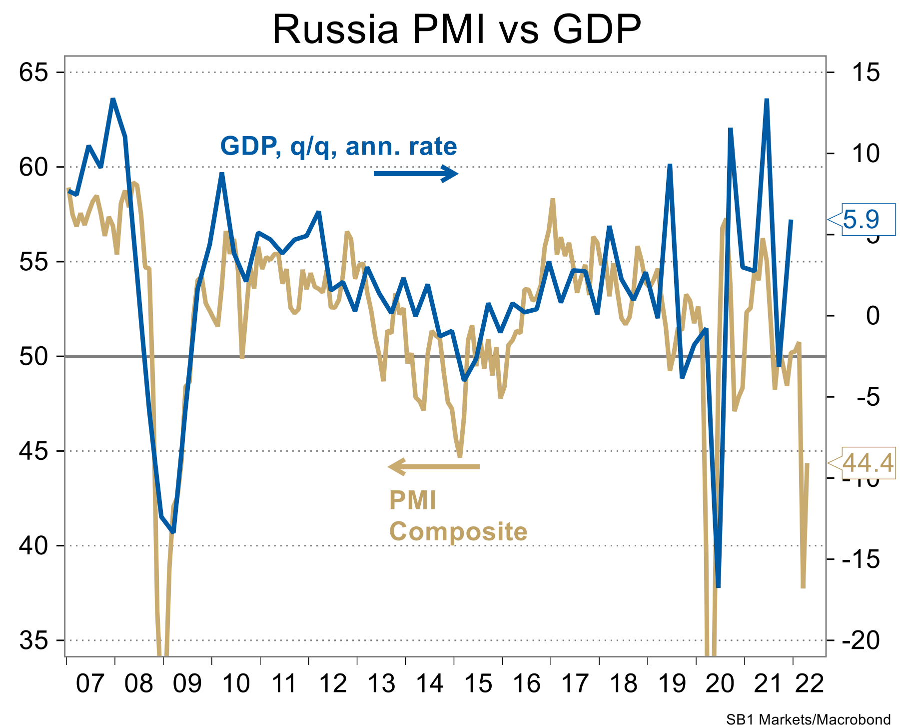


- While growth in manufacturing stalled in April, the service sector showed stronger growth as remaining restrictions were eased further
  - » However, the war in Ukraine and ever increasing purchasing prices give causes for concern in the manufacturing sector
  - » Could it also be that the pent up demand in the service sector has reached the top?
- The final **composite PMI** at 55.8 signals growth at 2.3%, well above trend
- The German PMI fell, while the other big 3 reported an increase

A continued but slower decline in both manufacturing and services

The composite PMI recovered 6.6 p to 44.4, still signalling a huge decline in GDP (almost 10%)

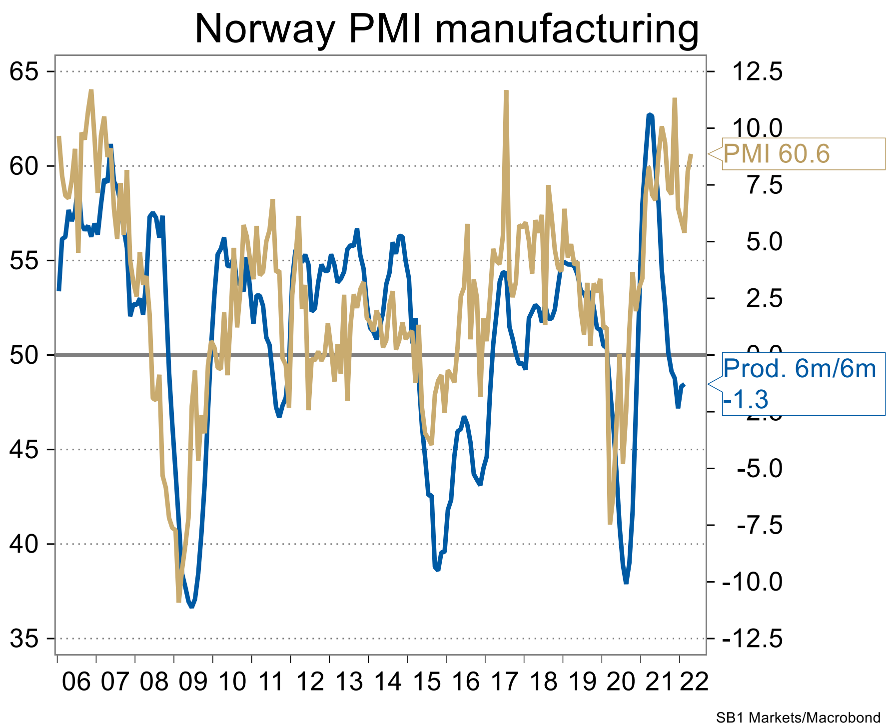


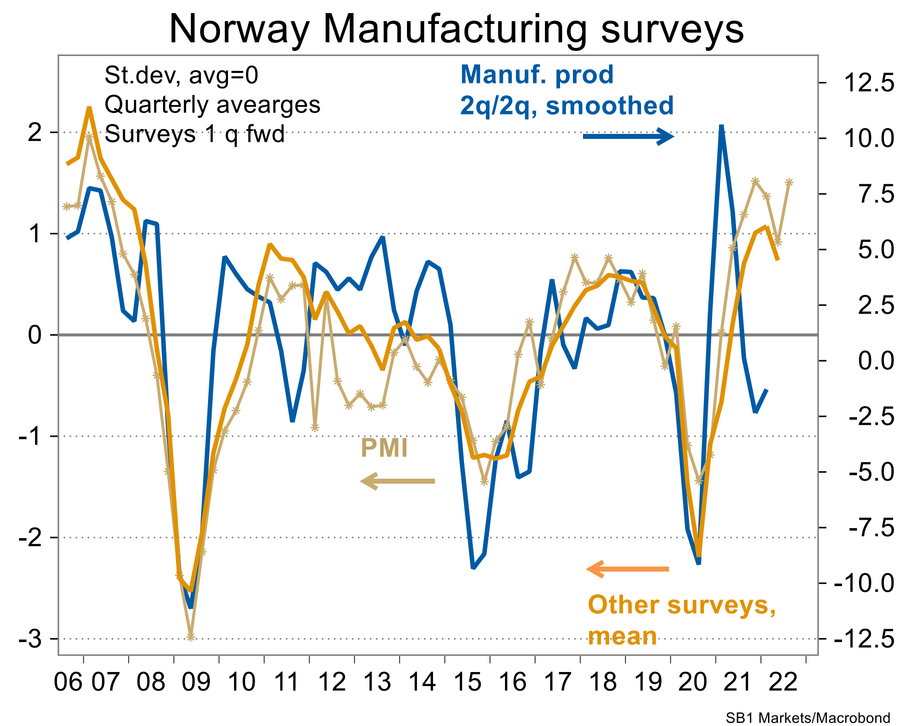


- **The service sector PMI** fell 6.3 p to 44.5
- **The output component in the manufacturing index** fell sharply too (a part of the composite index), while the total index just fell 4.5 p to 44.1
- There is of course just one possible explanation for this abrupt contraction in activity in April: The special operation in Ukraine and Western sanctions
- **A reminder:** The PMIs are not sentiment surveys – respondents are asked about in changes in actual activity (new orders, output, employment, inventories) from the previous month

The manufacturing PMI up 0.9 p to 60.6 in April, better than we expected (again)

The uptick was 'for real', both new orders & production up. Input prices are climbing rapidly, of course

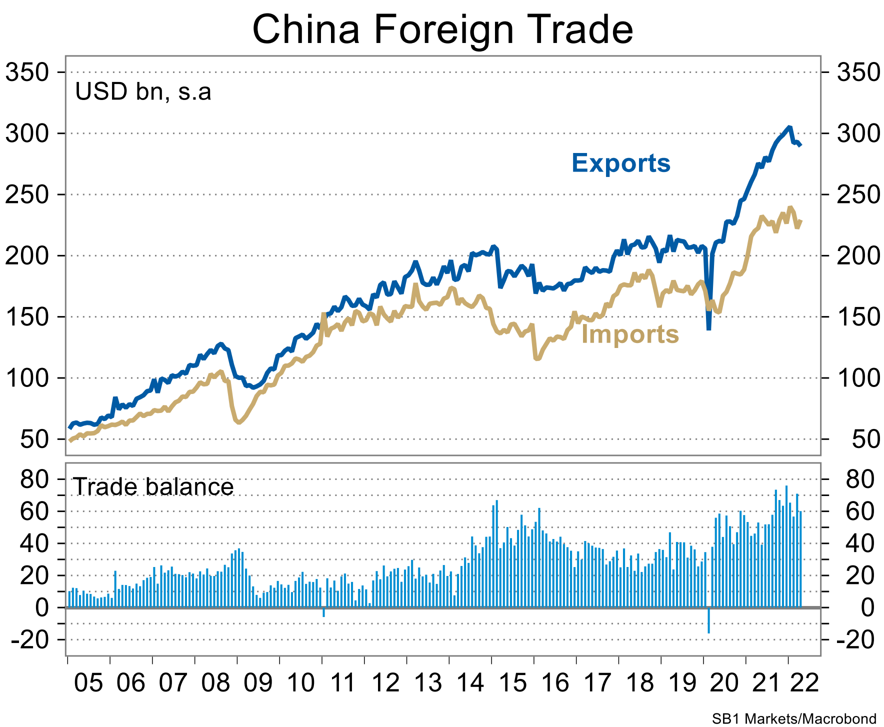




- The **manufacturing PMI index** climbed for the 2nd month in a row – to a very high level
- Other **manufacturing surveys** are mixed, but SSB's quarterly survey was also strong in Q1
- Even if surveys have been reporting growth, **actual production** has fallen slightly since last April

Exports down in April, but just by 1%, imports up 3%, both better than expected

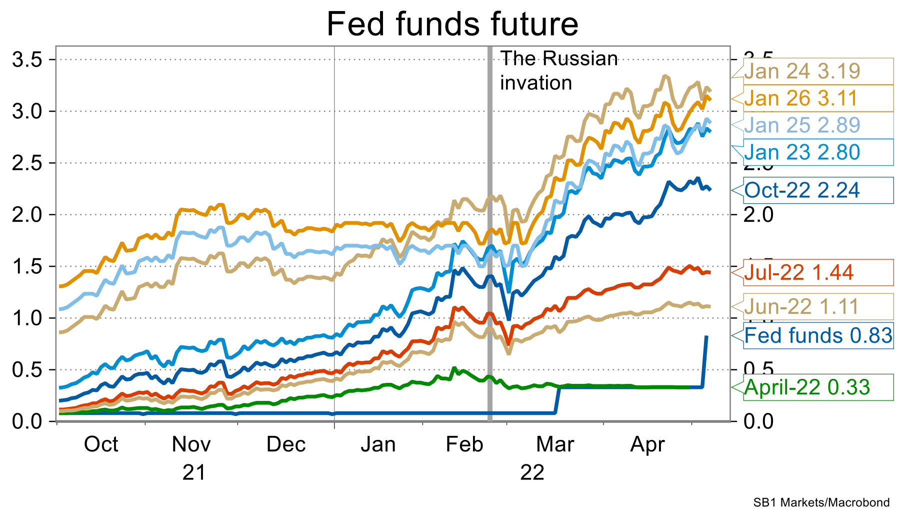
Still, both export & import volumes are down 7% from January, and just exports above the p-p trend

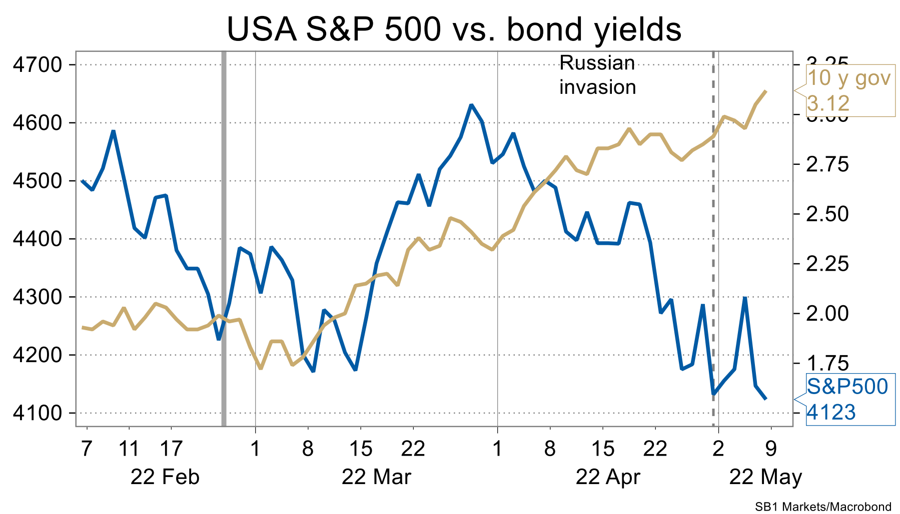


- **Exports fell by** grew by 1% in USD terms in April (our seas adj), and are up 4% y/y, down from 15% in March, 1 pp better than expected. Export volumes probably fell slightly too, adding to the decline in Jan, Feb & Mar. Export volumes are down 7%, are down 6% y/y – still up 13% from before the pandemic, and 4% above the pre-pandemic trend path
- **Import** values gained 3% m/m in April, and are flat y/y, like in March, 3 pp better than expected. Import volumes very likely rose too, we assume a smell price decline in April. Volumes are down 7% from January, and by 10% y/y, and are some 4% below the pre-pandemic trend. XXX Oil imports have flattened, coal and iron ore imports are down. In value terms, electric & electronics goods imports are still increasing rapidly
- The **trade surplus** at USD 51 bn was as expected and down USD 10 bn to USD 60 bn seas. adj.
- <u>Lockdowns have hurt foreign trade but so far not dramatically. Underlying slower growth in domestic demand recent quarters probably explain the decline in imports until the recent 'lockdown' drop</u>

What did the governor say? (A confused) Powell confused the (confused) markets

Some ups and downs in the markets last week but stocks were close to unch, the 10 y +23 bps, 3.12%



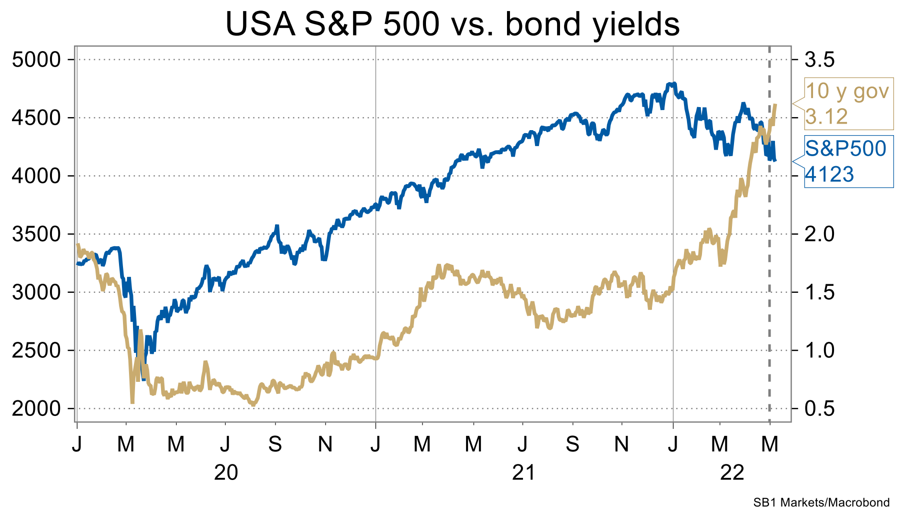


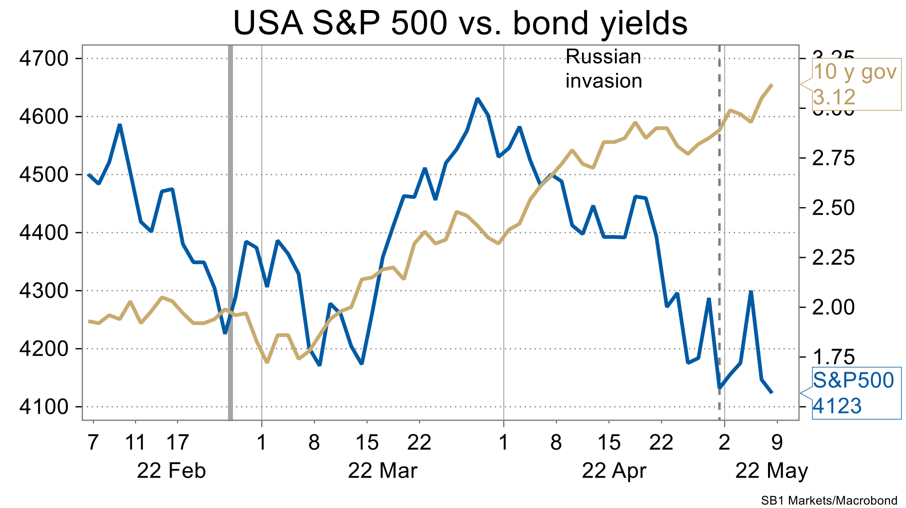
- **The press release** from the FOMC meeting on Wednesday did not change much: The signal rate was lifted by 50 bps as was widely expected and discounted in the market. The initiation of the QT process had been well communicated as well. The stock market was flat and bond yields rose marginally
- ... That is, until Powell started to talk at the press conference
- The FOMC had not 'actively discussed' a 75 bps hikes at this meeting or that 75 bps could be needed at the upcoming meetings. A 50 bps hike in June and July was signalled
- Then Powell said there is a path by which the unprecedented high level of vacancies could be brought substantially down without unemployment going up materially. Then wage and price inflation would come down, without the economy falling into a recession. There is a good chance of a soft or softish landing, he said.
- We assume there are some other 'not unlikely' paths too, but the stock marked shot up (and yields declined), as Powell was dovish vs rates (no 75 bps hikes) and assumed a recession would be a avoided. At least that was the conclusion at the marketplace. On Wednesday
- Of course, the next day, investors came to the **opposite conclusion**: stock markets tanked completely and yields rose
- Still, looking back, no big drama: Stock markets are back to where they came from ahead of the meeting. The short end of the curve is marginally lower (-3 to 12 bps), as 75 bps hikes are now deemed to be less likely. But no doubt, 50+50+... (pick your number of hikes) will be sufficient to achieve whatever is needed to bring inflation down. Last week the 10 y bond yields rose by 23 bps to 3.12%, due to a 26 bp lift in the TIPS real rate to 0.26%, and a small decline in break-even inflation expectations. The bond market did not think the FOMC was dovish, in the end
- **... and neither did we**: the FOMC has NOT become über-dovish vs. inflation. Yes, their inflation path is too high but we think the bank is willing to do what's needed to bring inflation down, almost whatever cost for the real economy – as the alternative would be even worse even if the FOMC hopes and prays for soft (GDP) landing. A soft landing is possible, but far from the most likely outcome. Thus, growth expectations, earnings expectations are very exposed. Most likely stock market multiples, and credit spreas too

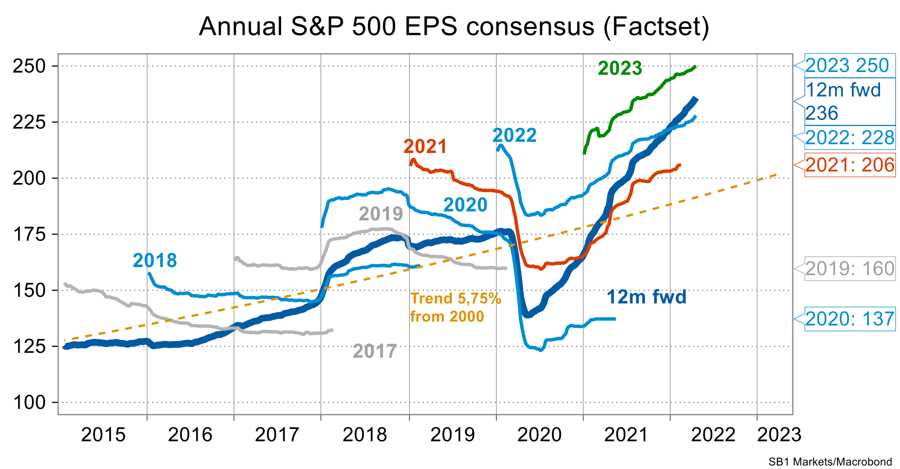
SpareBank 1 MARKETS

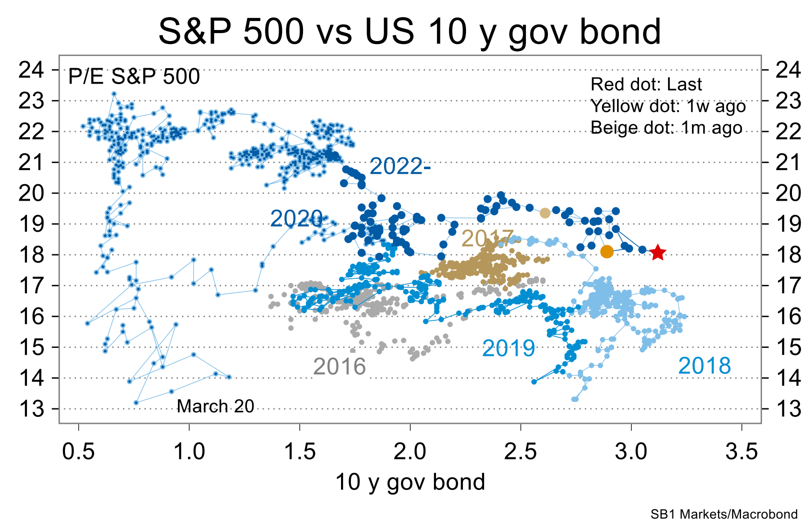
The 10 y gov bond up 23 bps to 3.12%. The S&P500 down 0.2, 14% from the peak

The next shoe to drop: Growth in expected earnings will soon fall sharply





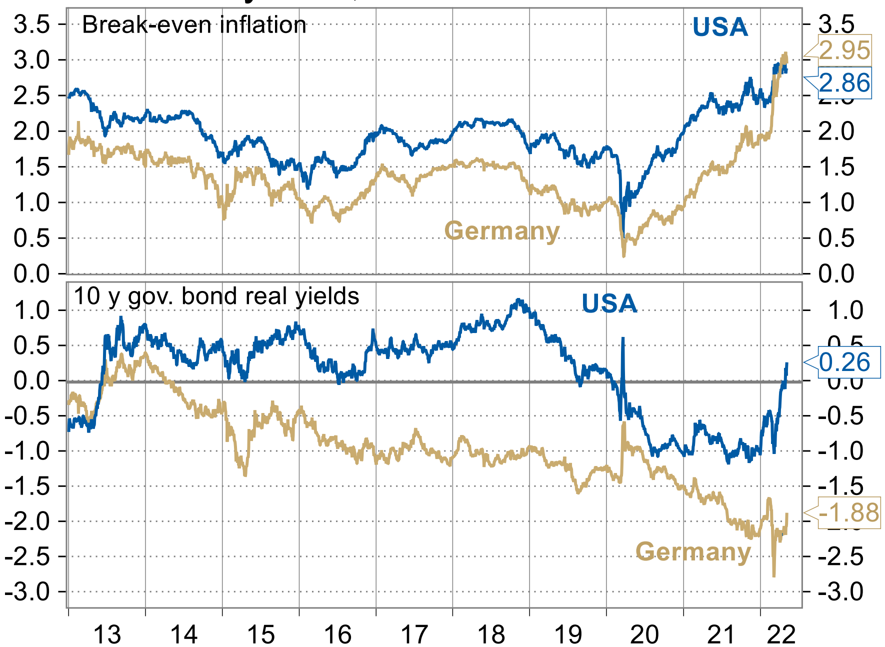




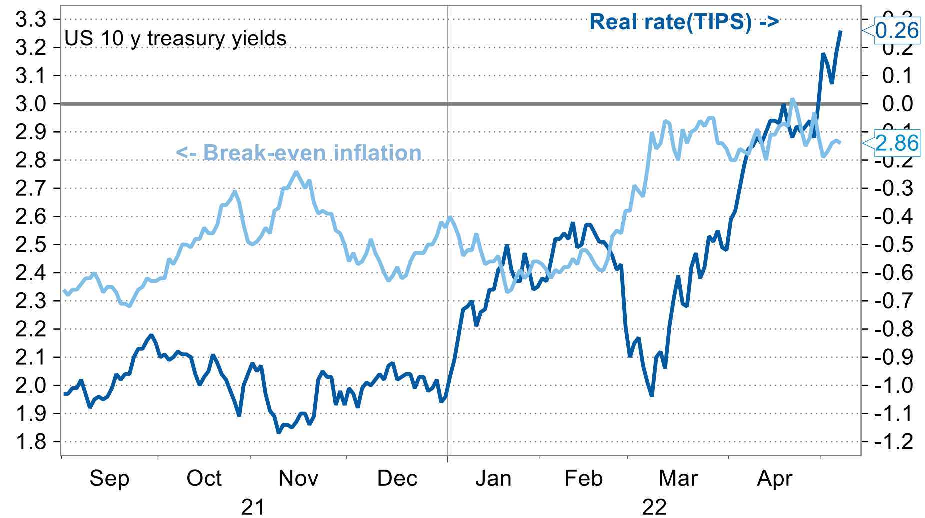
US 10 y TIPS real rate up 25 bps to +0.26. The German peer up 28 bps, still at -1.88%

Inflation expectations flat/down and close to 3% at both side of the Atlantic. Nominal at 3.12%, 1.07%!!

Real yields, break-even inflation



SB1 Markets/Macrobond



US & Germany 10 y Gov bond yield

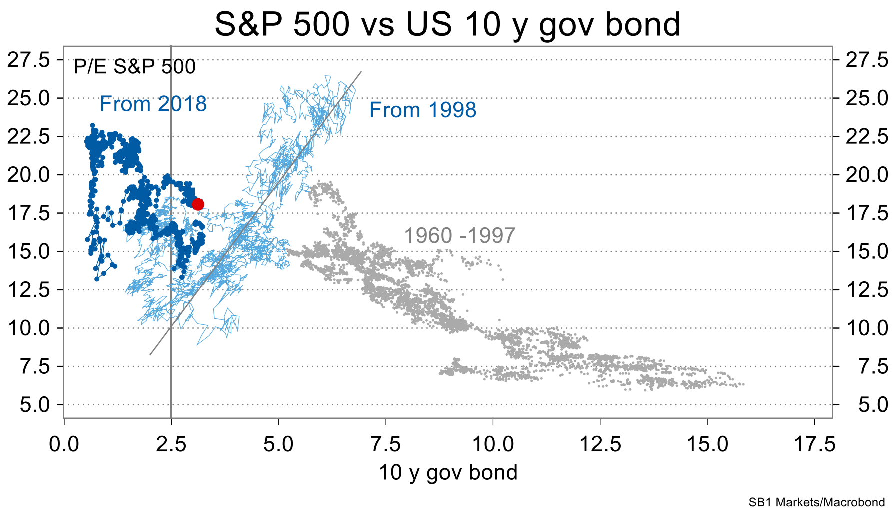
	Yield	Change 1w	Change 1m	Since Feb 18	Min since April-20
USA nominal treasury	3.12	0.23	0.51	1.20	0.52
.. break-even inflation	2.86	-0.02	0.03	0.45	1.06
.. TIPS real rate	0.26	0.25	0.48	0.75	-1.19
Germany nominal bund	1.07	0.17	0.42	0.85	-0.65
.. break-even inflation	2.95	-0.11	0.04	0.97	0.40
.. real rate	-1.88	0.28	0.38	-0.12	-2.80

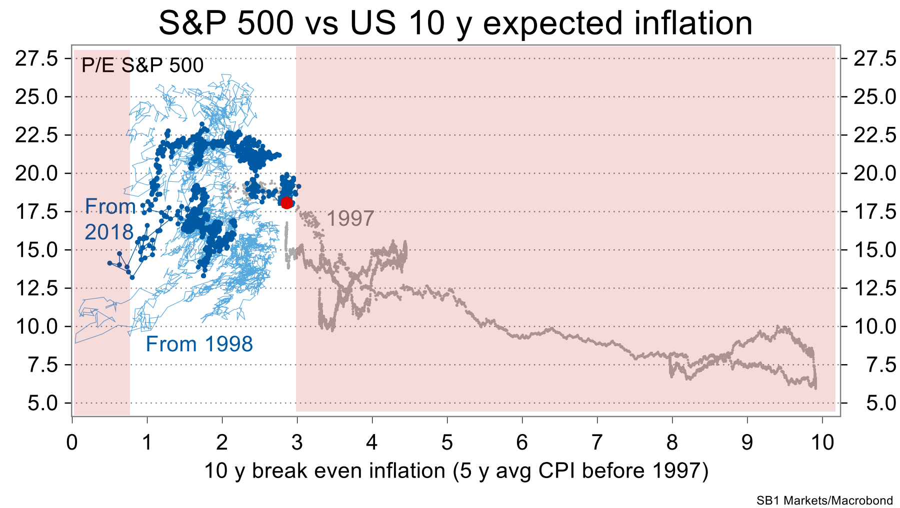
SB1 Markets/Macrobond

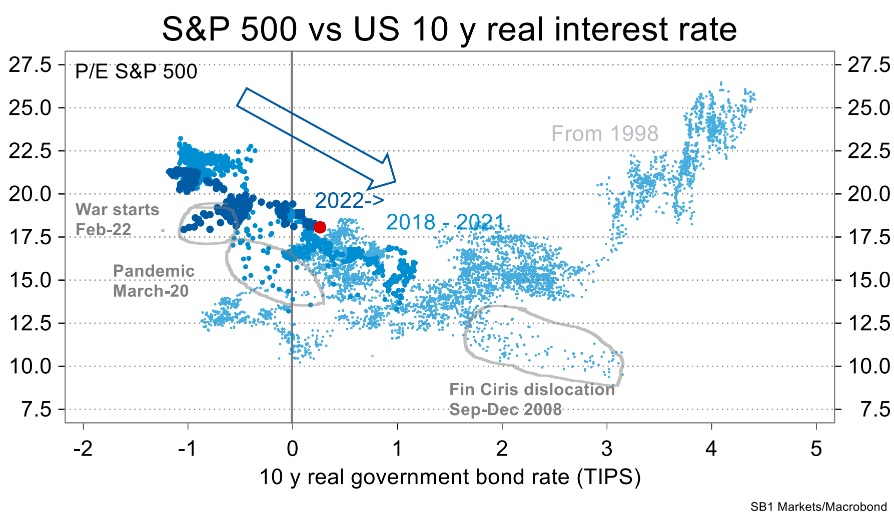
- **Nominal 10 y bond yields** are above 3% in the US and above 1% in Germany, the highest since late 2018 and late 2014 (!) resp.
- **Real rates in the US** fell to 1.03% after the Russian invasion in Ukraine, down from -0.42%. Now it is at +0.26%!!
- **The 10 y inflation expectations** are just below 3% in both the US and in Germany, at least vs. face value discounted at the bond market
- **Real rates in Germany** rose sharply last week but are still at -2.18%. The spread to the US 10 y real yield is close to record high

Bonds vs. equities: What's next? Central banks are now fighting inflation!

... And they will probably succeed. But at a price: Higher real rates + 'some' earnings surprises



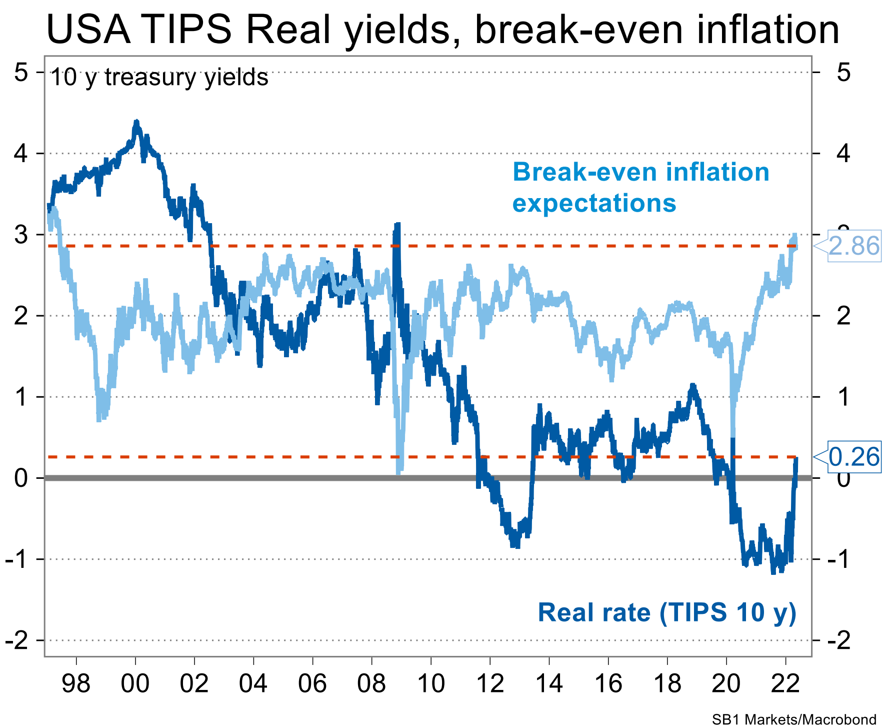


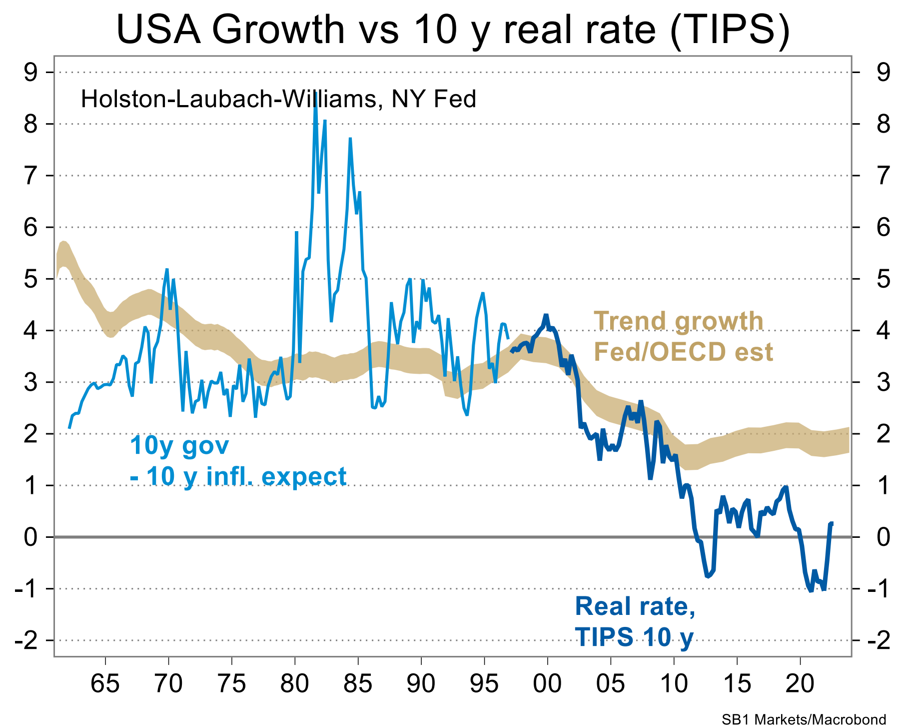


- **Expected inflation**
  - » ***If its not too low or too high: No problem***
    - 'Real' expected earnings are unaffected, higher inflation implies stronger growth in earnings, and vice versa
  - » ***If its too low or too high: A problem***
    - Something is rotten: Deflation or far too high inflation. The economy is not stable. Risk are increasing, earnings are exposed.
  - » Now: Infl. expectations at close to 3% - on the border to become a problem?
- **Expected long term real interest rates**
  - » ***Low real rates normally not good news, high rates were OK***
    - Real rates were low when the economy was weak, the outlook uncertain
    - High real rates when the economy was booming, with high P/Es
  - » **2018-21:** real rates have been low even if the economic outlook has been OK
    - Central banks wanted to lift growth, inflation was anyway not a problem – we entered the 'Goldilocks' corner'
  - » **Now:** Central banks engaged in a HUGE policy shift, to contain inflation. The risk: A further increase in REAL rates, at the same time as growth expectations slows!

Mind the gap: It's rapidly closing!

Real rates are rapidly on the way up from levels that were far to low if the growth outlook was OK

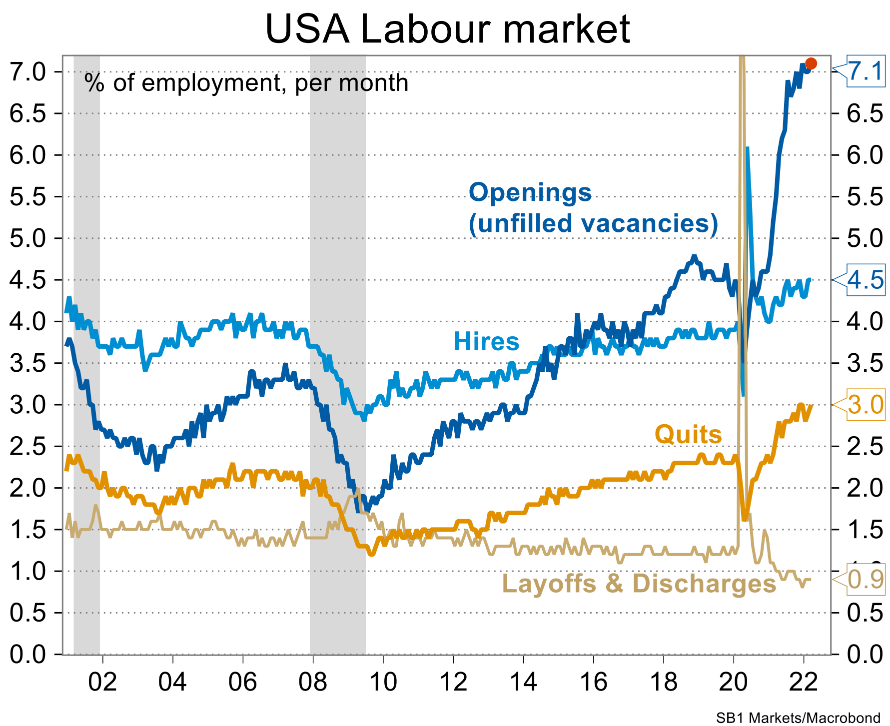




- There is now reason to believe that the current surge in real rates is due to an equivalent increase in growth expectations. It is of course the opposite: At least the short to medium-term outlook is now weakening as central banks finally enters the fights against inflation by at least bring growth down to below trend growth
  - » Profit margins are VERY exposed
  - » Demand for labour will slow too, and unemployment will increase – in order to get wage inflation down
- The USD 10 trl question: Are all risk markets really discounting this scenario?

The vacancy rate up to a new ATH. Quits & hires at ATH too

'Nobody' is laid off. The labour market is still extremely tight

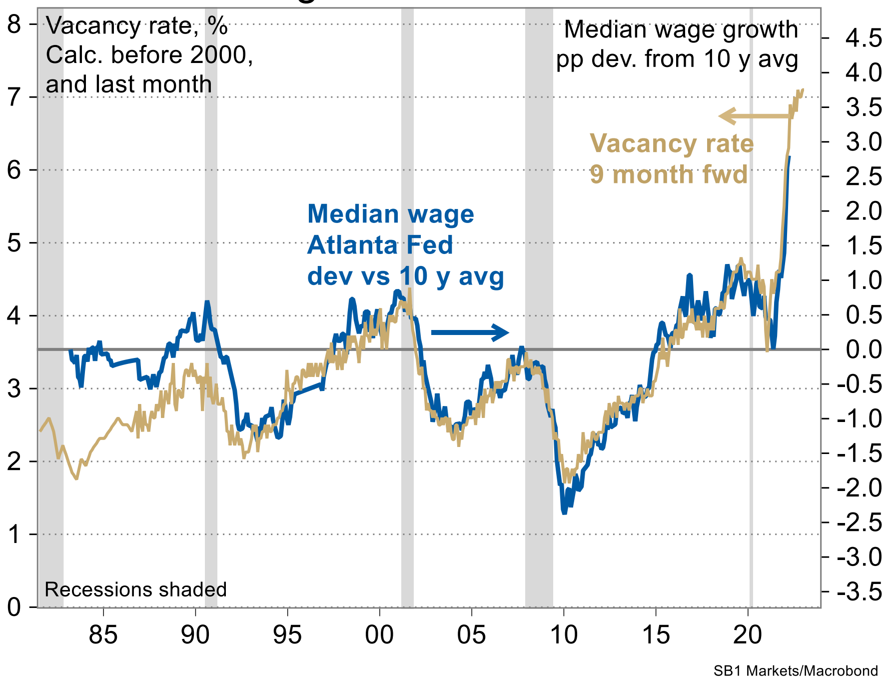


- The number of **unfilled vacancies** rose 0.2 mill to ATH at 11.6 mill in March, expected down to 11.0 mill. The rate gained 0.1 pp to 7.1%, ATH too (at the 2nd decimal)
  - » The highest print ever before the pandemic was 4.7%, and the rate was 4.5% just before the pandemic hit
  - » **The SMBs (NFIB survey)** reported an unch. – and close to record high – share of companies that were not able to fill open positions in April. These two series are very closely correlated – and both have been at levels never seen before since early last year
- **New hires** declined 0.1 mill to 6.7 mill persons from an upward level in February, equalling 4.5% of the employment level (unch., revised up by 0.2 pp), in line with previous ATHs
- The number of **voluntary quits** rose by 0.2 mill to 4.5 mill, or up 0.1 pp to 3.0% of the no. of employed, also in line with ATH late last year. As with unfilled vacancies, quits are closely correlated to wage inflation – for obvious reasons
- **Layoffs** were unchanged at 0.9%, a very low level
- **In sum:** The report data confirm an extreme tight labour market

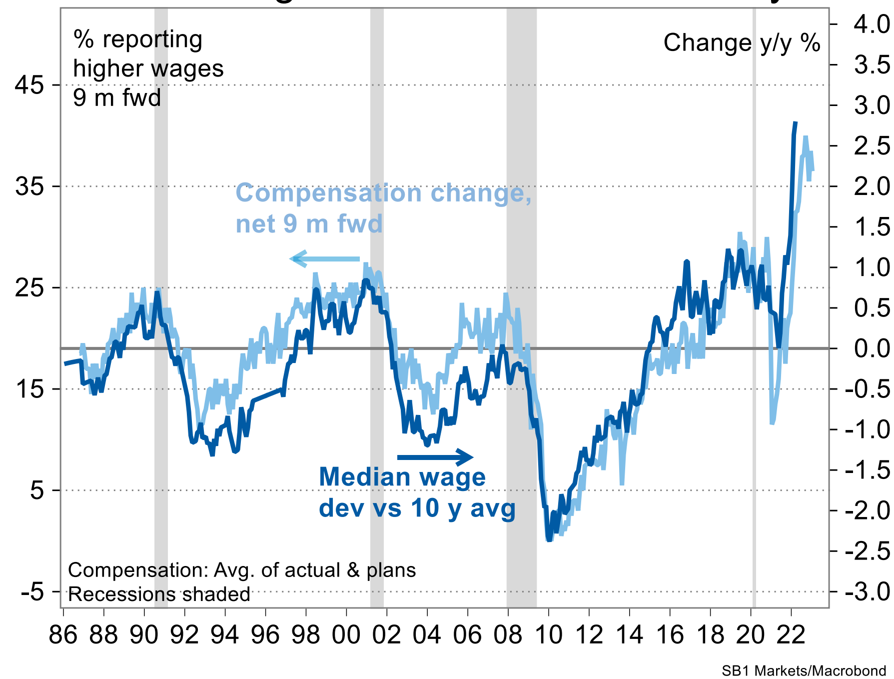
There seems to be some connections here?

The correlation between the vacancy rate and changes in median wage growth is <u>extremely</u> tight

USA Wage inflation vs vacancies



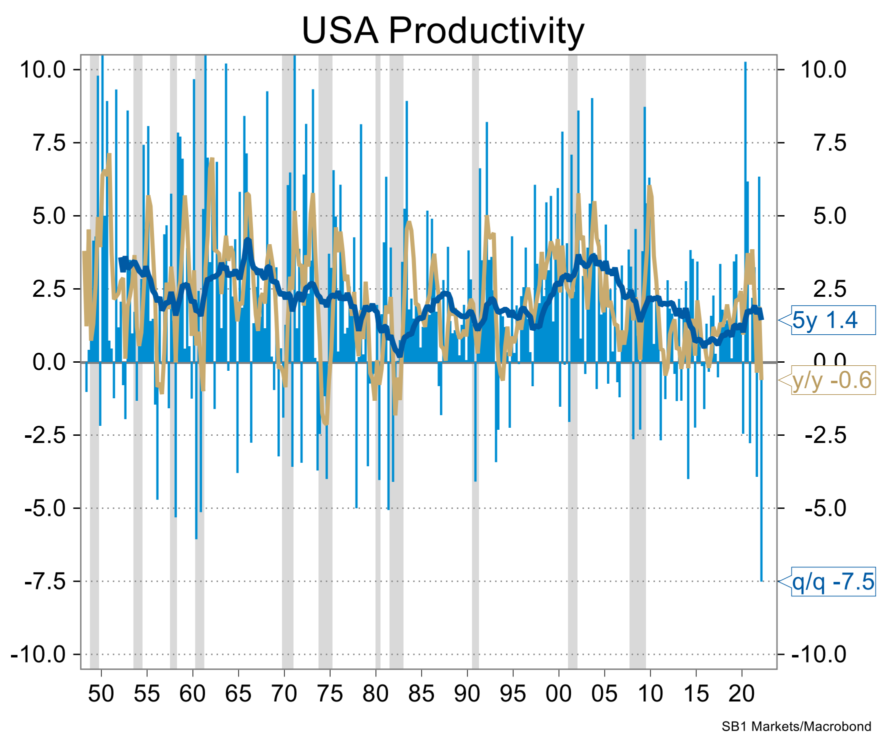
USA Wages - Actual vs NFIB survey

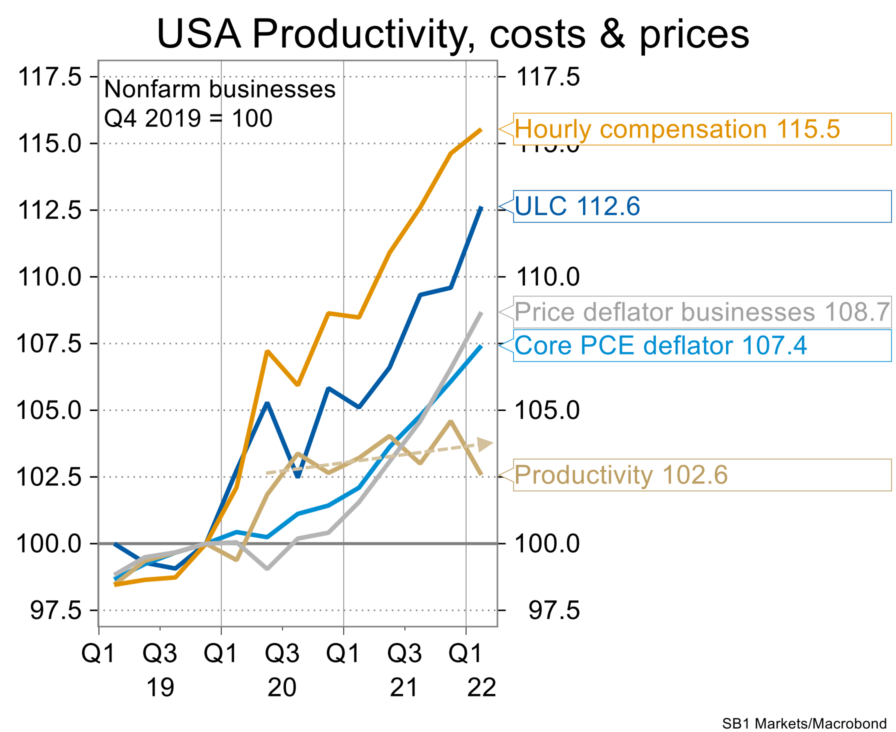


- Our 'Phillips curve' based in the vacancy rate signal a further increase in wage inflation the coming quarters, as the vacancy rate leads changes in wage inflation quite consistently by 3 quarters
- Companies (SMEs) compensation plans (see more next page) signal continued high wage inflation but not faster than the current
- Wage inflation has already accelerated by 2.5 – 3 pp vs the 10 y average (Atlanta Fed median) and cannot impossibly generate a 2% price inflation rate over time. <u>This is Fed's main headache. And it will be the stock owners' headache too, of course…</u>
- <u>Check under which circumstances wage inflation slows on the charts above (hint: find the shaded areas, follow the wage line ☺</u>

A Q1 productivity outlier – but the real problem is a dismal trend. ULC up >>5%

An unprecedented 7.5% drop in Q1 (exp. 4.5), and down 0.6% y/y. Underlying trend < 1%

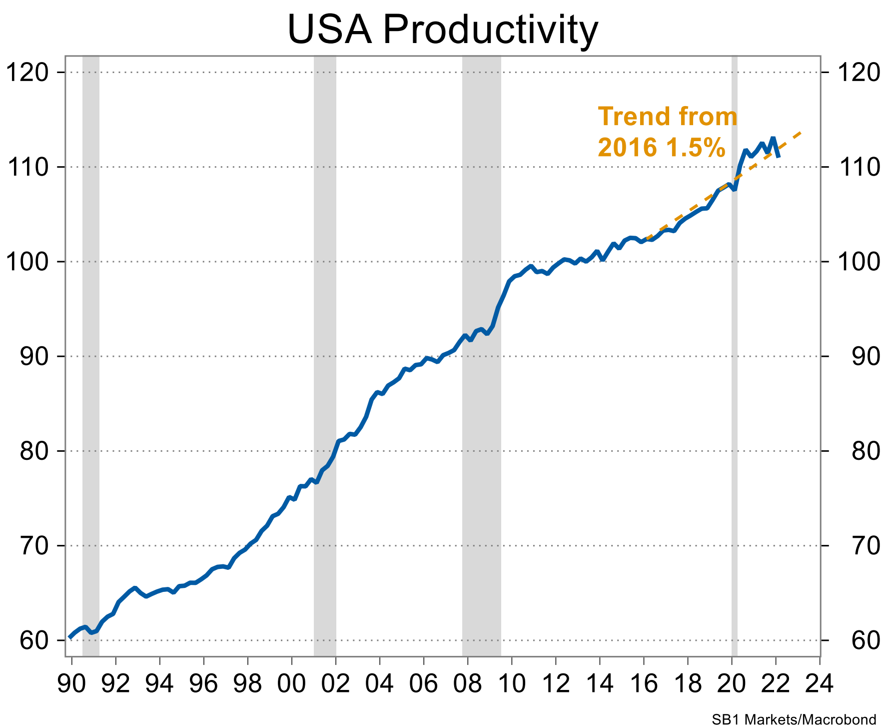


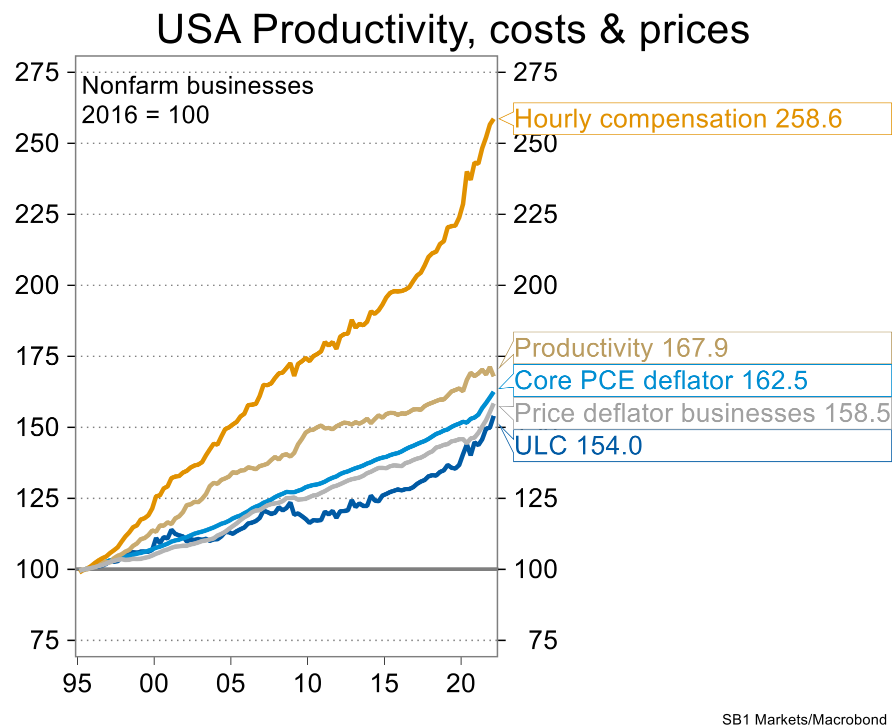


- **Productivity data** are still all over the place. In Q4, nonfarm business productivity surged 6.3% (but fell 3.9% in Q3). Hours worked rose much more than we assumed (and much more than the nonfarm payroll report has indicated). Output fell by 2.4%
- Still, the problem is a weak **underlying trend**. Productivity is up at a 1.1% pace since before the pandemic, and well below 2% since mid 2020. The trend since 2015 is though at 1.5%, perhaps a fair underlying trend estimate. (BTW we still think the Q1 GDP data were suspectedly weak, and productivity may be revised up)
- **Hourly compensation (wages ++)** grew at just a 3.2% pace in Q1, but the annual rate still accelerated to 6.5% from 5.5%. Since Q4-19 hourly compensation has grown at a 6.6% pace, way above the pre-pandemic level
- **Unit labour costs** (hourly compensation – productivity) grew by 11.6% in Q1 (expected 7.9%), up 7.2 y/y, the highest since 1982. Since Q4-19, ULC has grown at a 5.4% pace, far above a normal level – which of course is totally incompatible vs the 2% inflation target

No impressive lift in productivity during the pandemic

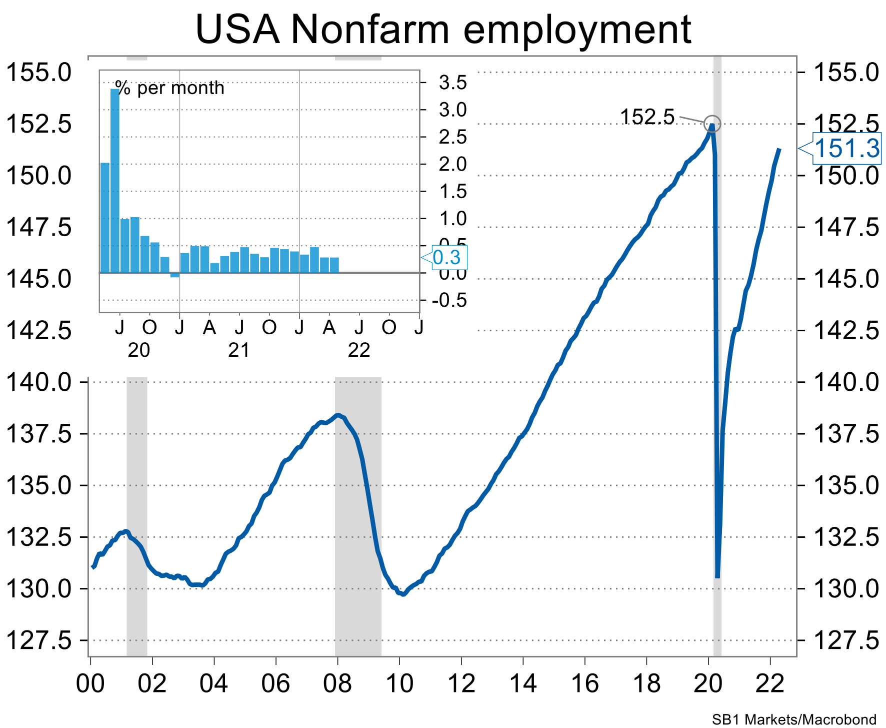
However, a quite impressive lift in hourly compensation…

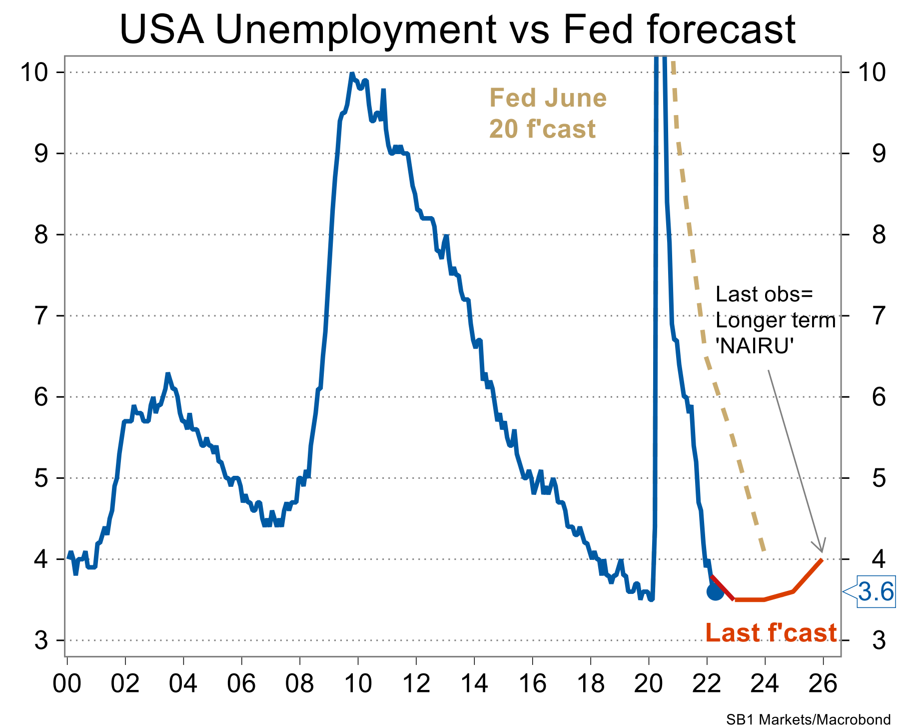




Stable growth in nonfarm payrolls, unempl. flat at 3.6%, wage infl. 'just' 0.3%

The participation rate fell, signalling limited reserves left

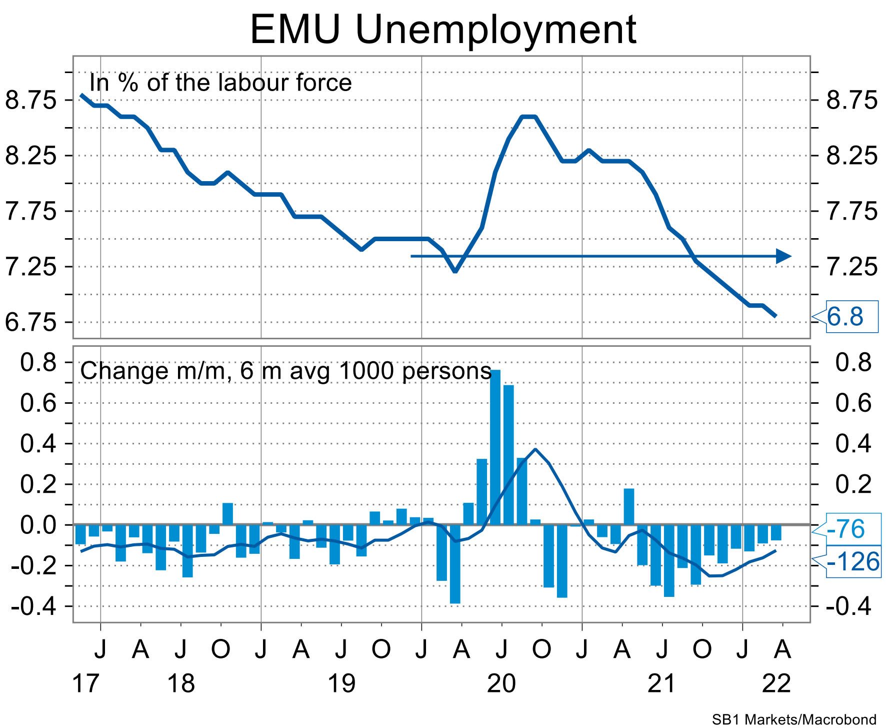


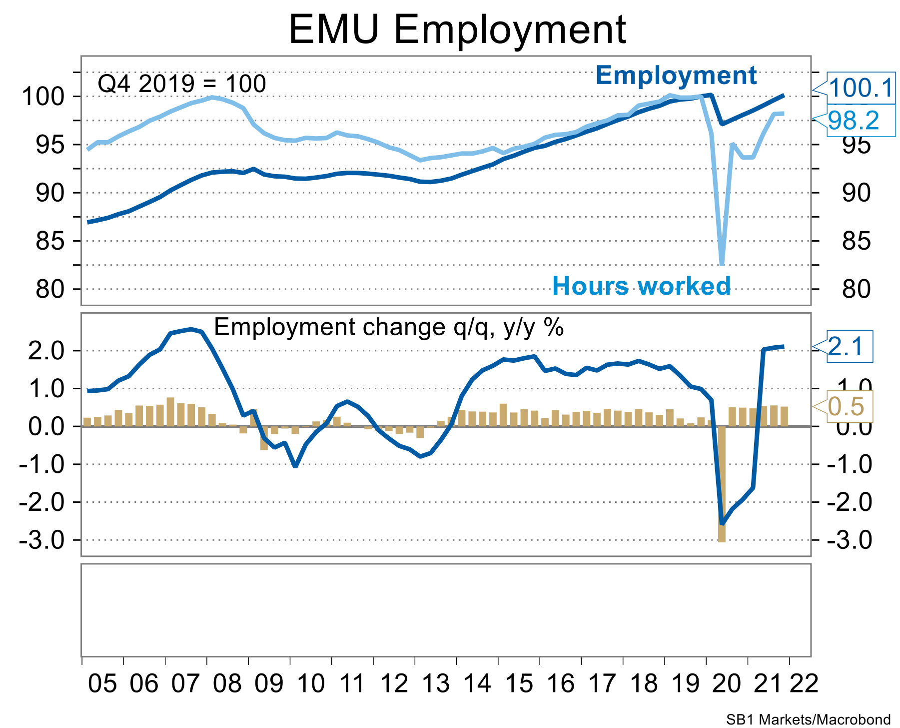


- **Nonfarm payrolls** rose by 428' in April, like in March, and 50' above expectations. The past 2 months were revised down by in sum 39'. Payrolls are still down 1.2 mill vs. Feb-20 or by 0.8%. The LFS employment declined by 353'. This number is much more volatile from month to month. The employment rate fell 0.1 pp. Average hours worked is trending down but remains well above the pre-pandemic level
- **The participation rate** surprisingly fell 0.2 pp to 62.2%. The trend is still probably up, but slowly vs. the still brisk demand for labour. Including those outside the labour marked due to Covid related reasons, the rate is 62.4% as very few now states Covid as a reason for not working/searching work
- **The unemployment rate** was stable at 3.6%, 0.1 pp higher than expected. The rate is now just 0.1 pp above Fed's estimate end of '22 estimate – and 0.4 pp below Fed's estimate of the long term NAIRU. In March, the unfilled vacancies equalled 6.8% of the labour force (7.1% of employment)
- **The average wage** rose 0.3%, 0.1 pp less than expected but growth in March was revised up by 0.1 pp to 0.5%. The annual rate is 5.5%, as expected, up from 3¼ before the pandemic – and not compatible with 2% CPI inflation over time
- **Maximum employment:** Even if the participation may be trending slowly up, the supply side is obviously the bottleneck at the labour market. For the time being, maximum employment is reached – and wage inflation is well above a sustainable level

Unemployment on the way down, the rate is the lowest since 1981

The unemployment rate (for the 3rd time…) down 0.1% to 6.8%. The speed of decline is abating

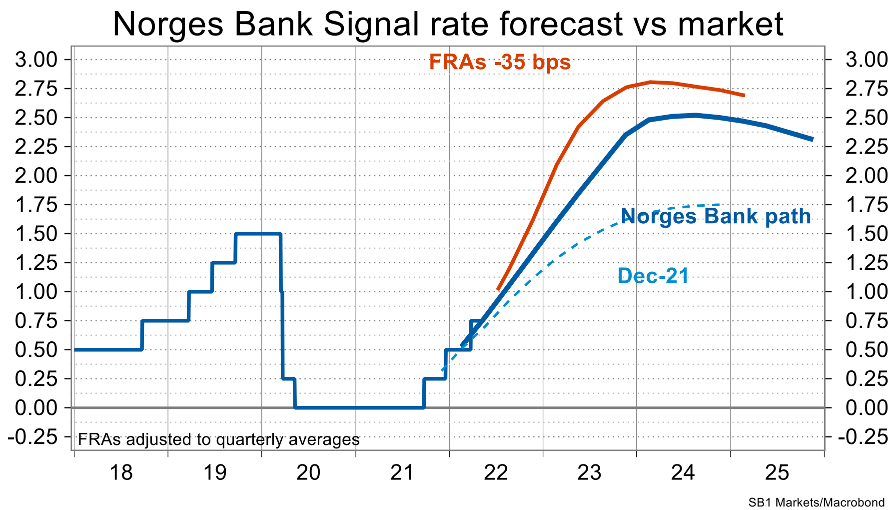


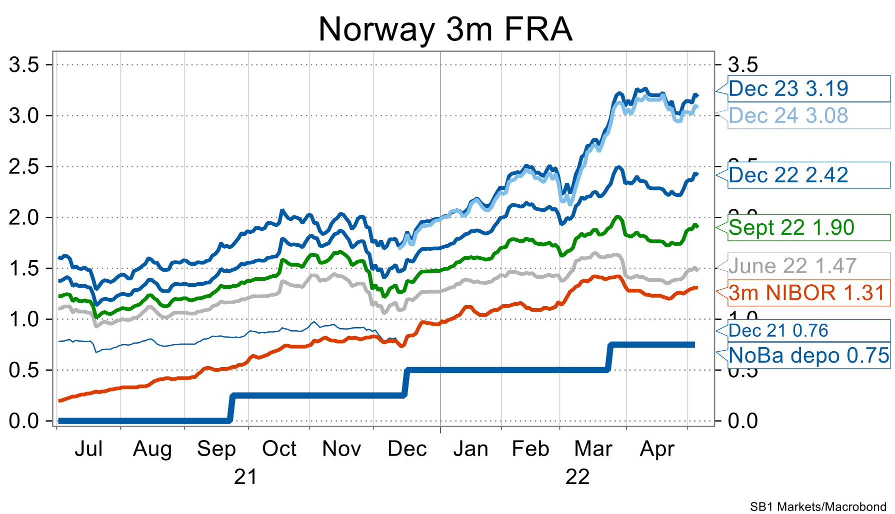


- **Unemployment** has been falling rapidly since last spring. In March, the unemployment level fell by 0.1 pp, as expected, but from an upward revised level in February (like what was the case one month ago)
- **Employment** rose by 0.5% in Q4, as in the previous 4 quarters, and the level is 0.1% above the pre-pandemic level
  - » However, the best proxy for **demand for labour**, is the number of **hours worked**. In Q4, hours worked was unch., and were down 1.8% vs the pre-pandemic level, as average working hours have fallen
- The number of **unfilled vacancies** has soared to the highest level ever, by far

Norges Bank confirmed the plan, a next hike in June

The tone was still on the hawkish side, the bank repeats the domestic price/wage inflation risk

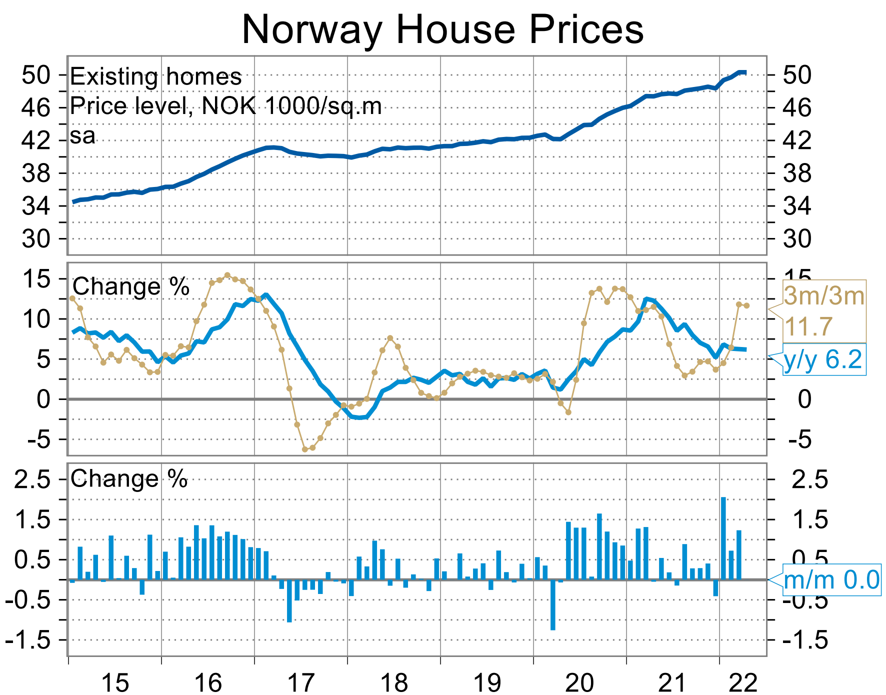




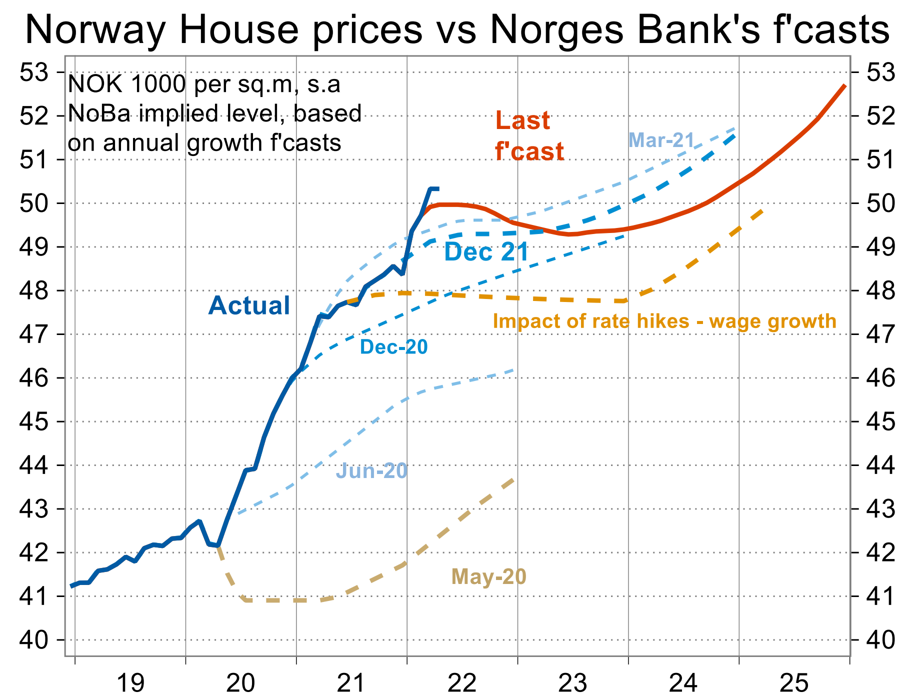
- **Key policy rate** was kept unchanged at 75 bps, as everybody expected
- Monetary policy is still expansionary, and there are not signals that the March MPR interest rate path is outdated
- The risks – both on the up- and downside
  - » Higher inflation and lower growth abroad due to the war in Ukraine
  - » Higher interest rates abroad may slow growth
  - » Risk of accelerating price and wage inflation in Norway. If there are prospects of persistently higher inflation, the policy rate may be raised more than quickly than indicated in the March MPR
- FRA-rates climbed last week, but not when NoBa published the press release from this 'mid' meeting
  - » The market probably discounts a small chance for a 50 bps hike in June or a hike at the August meeting
  - » The market is discounting a signal rate at close to 2% at the end of the year, well above NoBa's 1.5% f'cast, with a small probability for 1.75%

Finally, house prices flattened, but no. of transactions remained low, the inventory at ATL

Prices stabilised in April, following the 4% surge in Q1



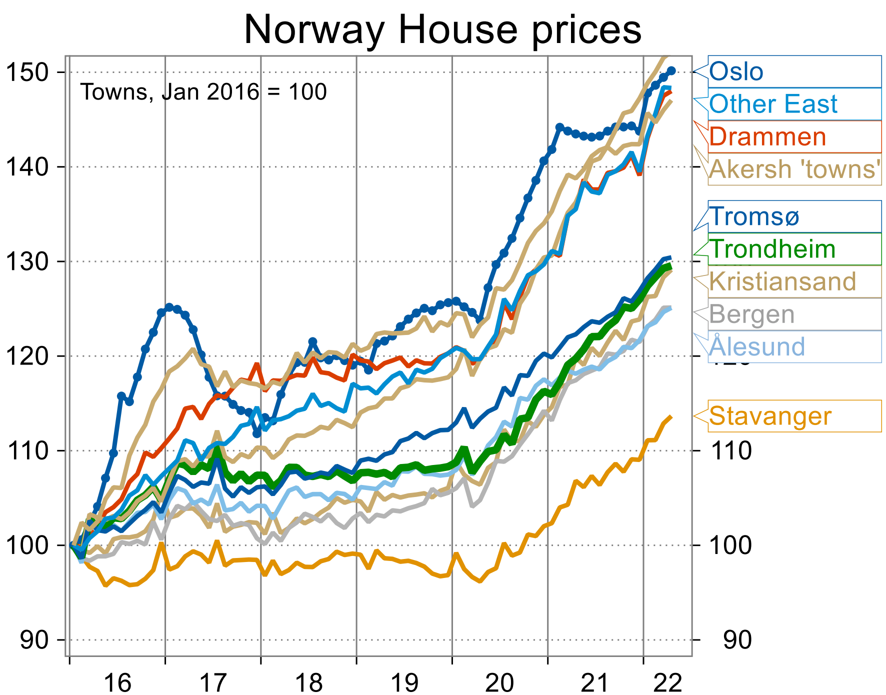
SB1 Markets/Eiendom Norge/Finn/Eiendomsverdi AS



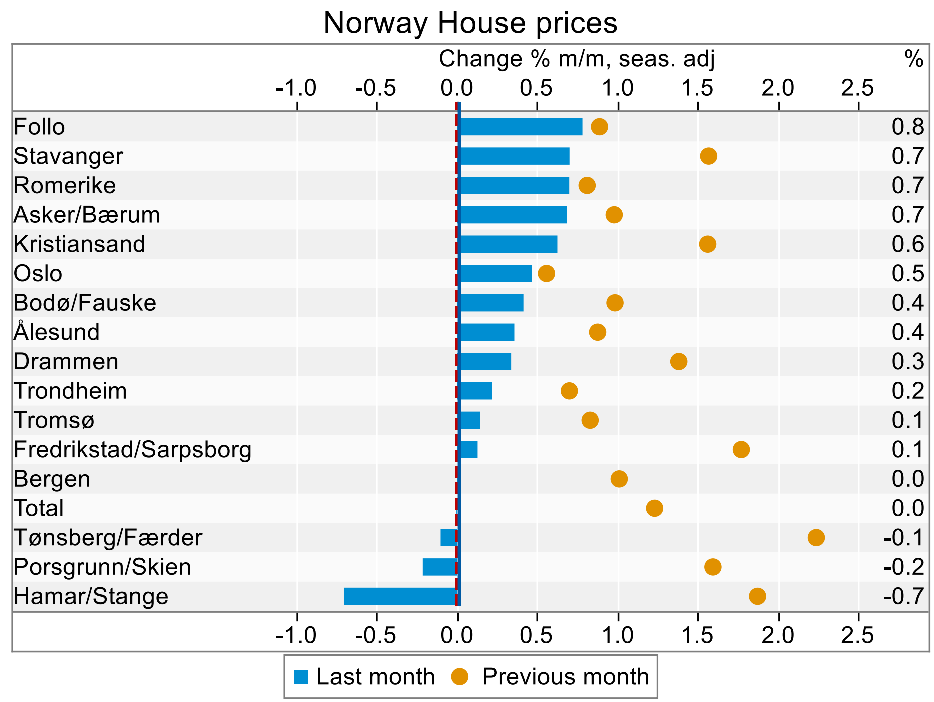
SB1 Markets/Macrobond

- **House prices** were unchanged in April (seas. adjusted., +0.3% unadj.), as we expected, following the 1.2% lift in March (revised from 1.0%). Norges Bank expected a 0.1% lift in April (and 0.4% in March). The number of transactions fell, is lower than 'normal', and the inventory is record low
  - » The surge in prices in Q1 was probably mostly due to lack of supply as a new law put up stricter requirements for technical valuation reports etc and thus fewer new homes for sale reached the market. Now, supply is gradually inching back to a normal level
- **Norges Bank** expects prices to flatten from here, and to decline marginally from Q3, before turning up again in H2 2023. In Q3 2024 prices are expected back to the H1-22 level.
- The impact on house prices from a 25 bps hike in the signal rate per quarter from Q3 last year adjusted for actual/expected growth in incomes, is illustrated at the chart to the right: the rate impact more or less equals the income impact, until the signal rate is assumed to flatten in 2024
  - » A 4% price elasticity vs. the interest rate is assumed, the coefficient is derived from NoBa's main forecast model. Wage growth 4%

Most cities reported higher prices in April, just Hamar really declined



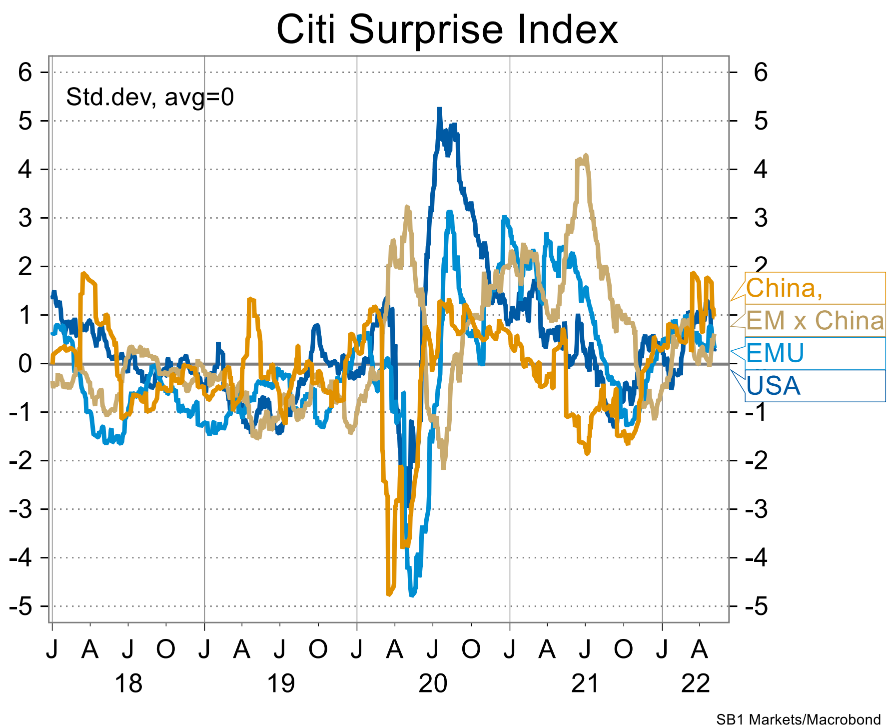
SB1 Markets/Eiendom Norge/Finn/Eiendomsverdi AS

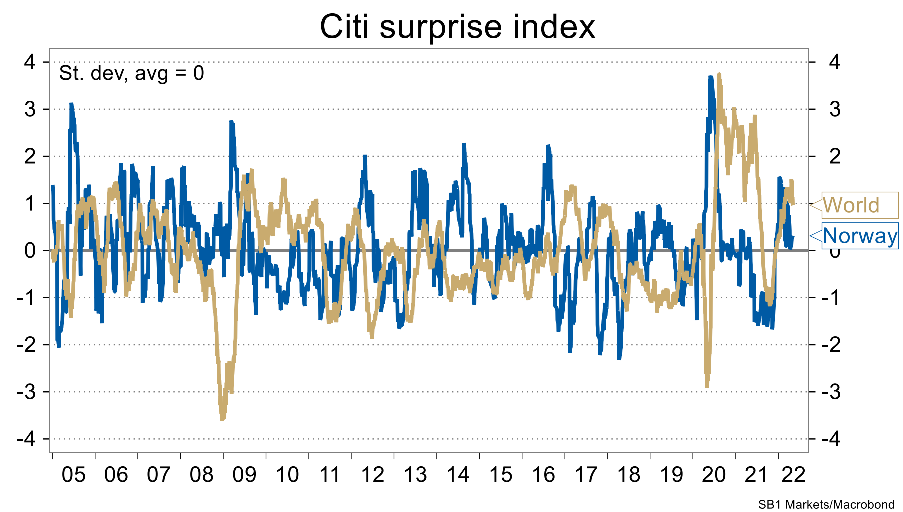


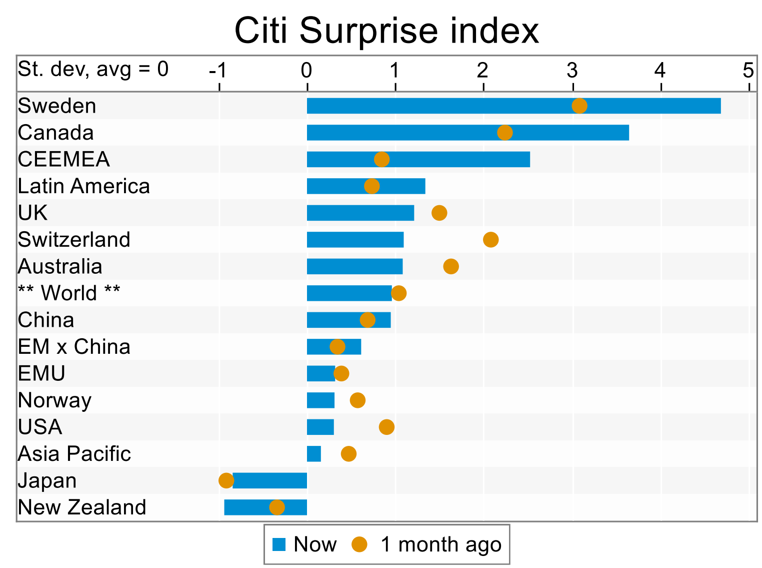
SB1 Markets/Eiendom Norge/Finn/Eiendomsverdi AS

The world is still surprising at the upside but less so last week

Weaker Chinese PMI took China down. US is also less convincing at the upside







- **Norway** is surprising marginally at the upside, according to Citi
- **Sweden** is still at the top

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

SB1 Markets/Macrobond

Highlights

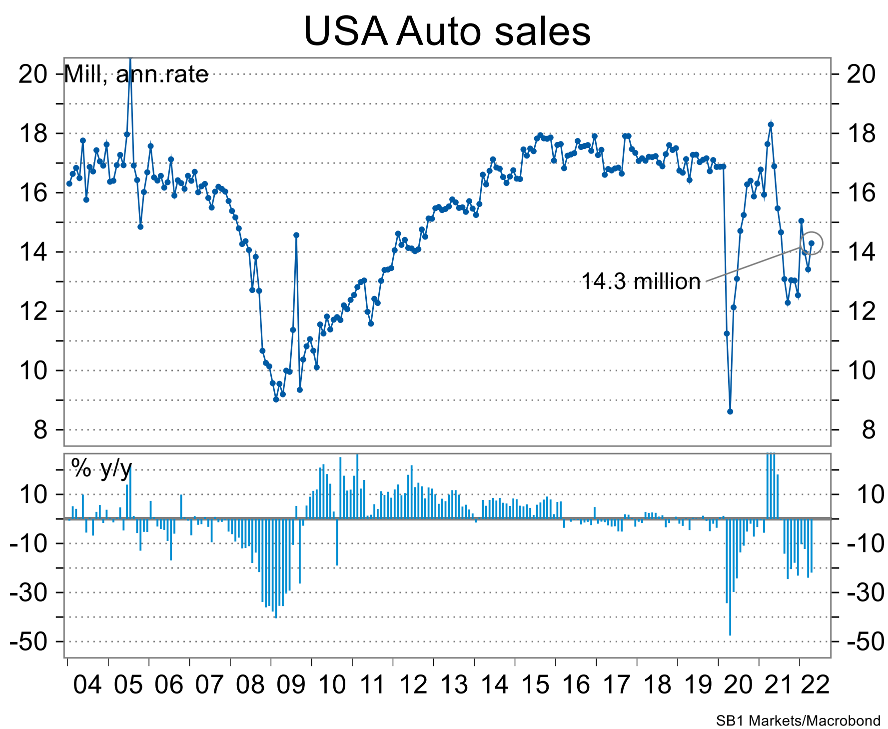
The world around us

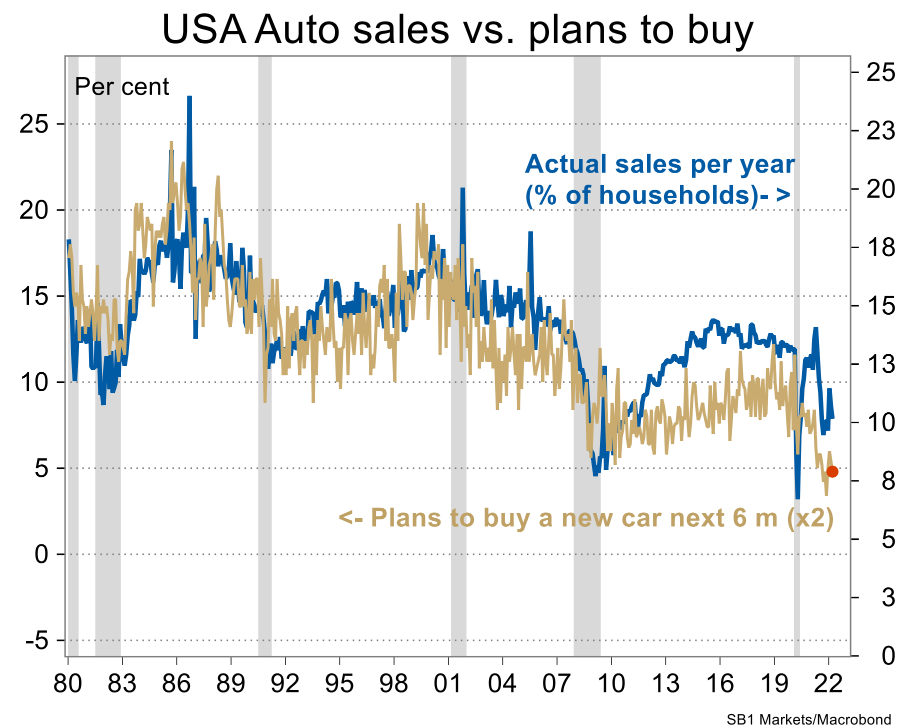
The Norwegian economy

Market charts & comments

US auto sales up 0.9 mill to 14.3 mill in April

Sales are down 16% vs. the 2019 level, entirely due to lack of supply

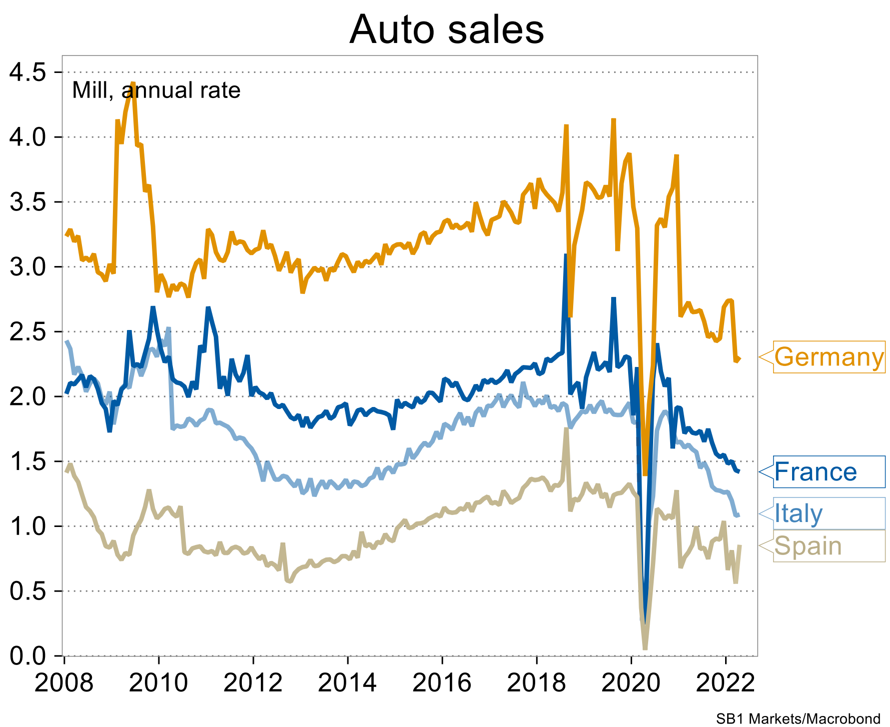


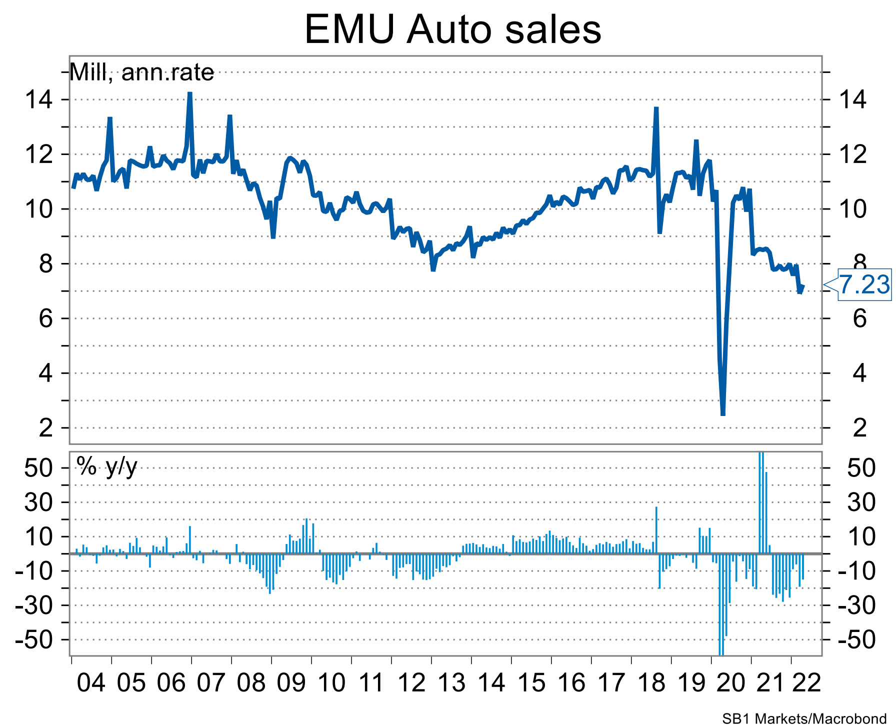


- Households revised down their **plans for buying a new car** substantially through last year as they probably have observed that there are delivery 'challenges'. In addition, prices are rising sharply (for identical cars), and more expensive models are prioritised by car producers (or rather cars with the highest margins
- **Demand for cars** is still strong, as the second-hand market is 'emptied', and used-car prices have soared 50% – 60% (but prices fell slightly in February)

Spanish sales up in April but no cheers elsewhere in the European Union

Total sales likely rose just marginally vs the huge (12%) setback in March. The trend is weak, level low

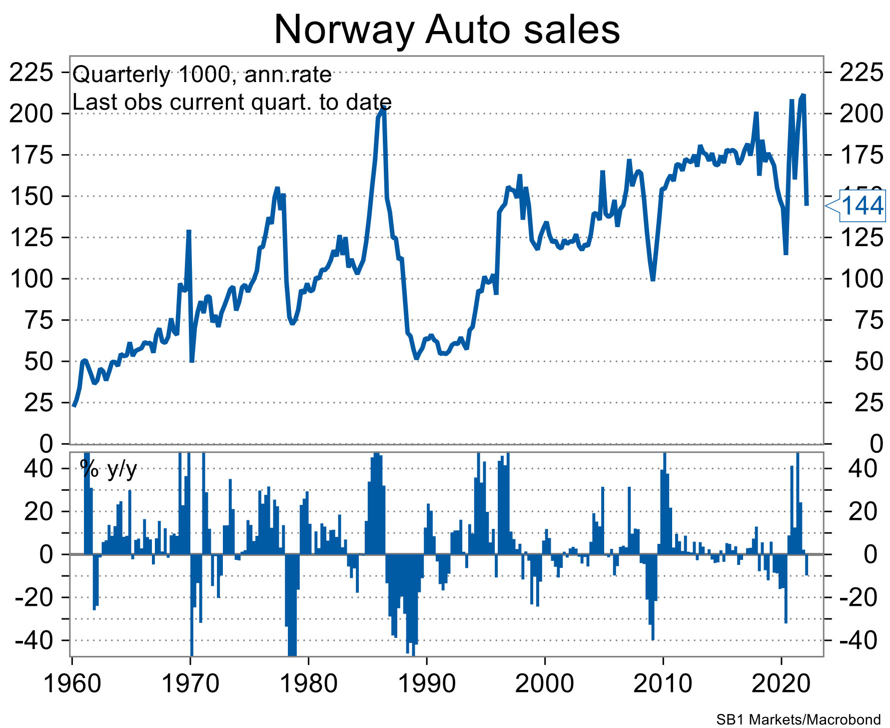


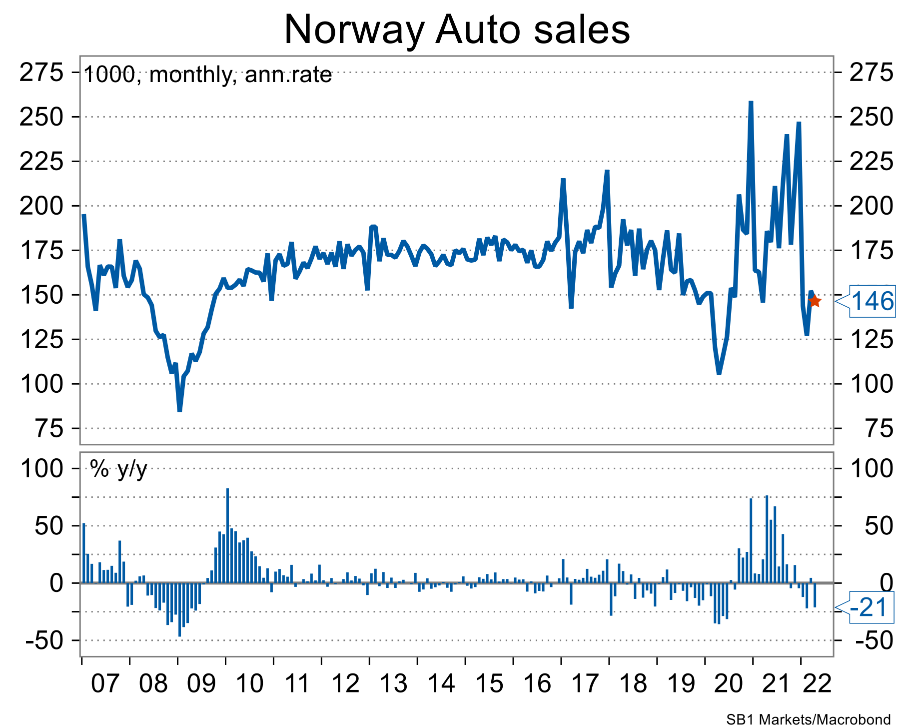


- All markets have reported substantial decline in auto sales since early 2021 – delivery problems is the main culprit, but some demand weakness as well?
- The coming months will be very challenging. The supply chains are exposed, once more – and German production nosedived in March

Norway: Auto sales 'slow' in both March and April – 9% below the 2019 level

Only China (of the 'big' countries) report smaller cuts in autos sales than Norway



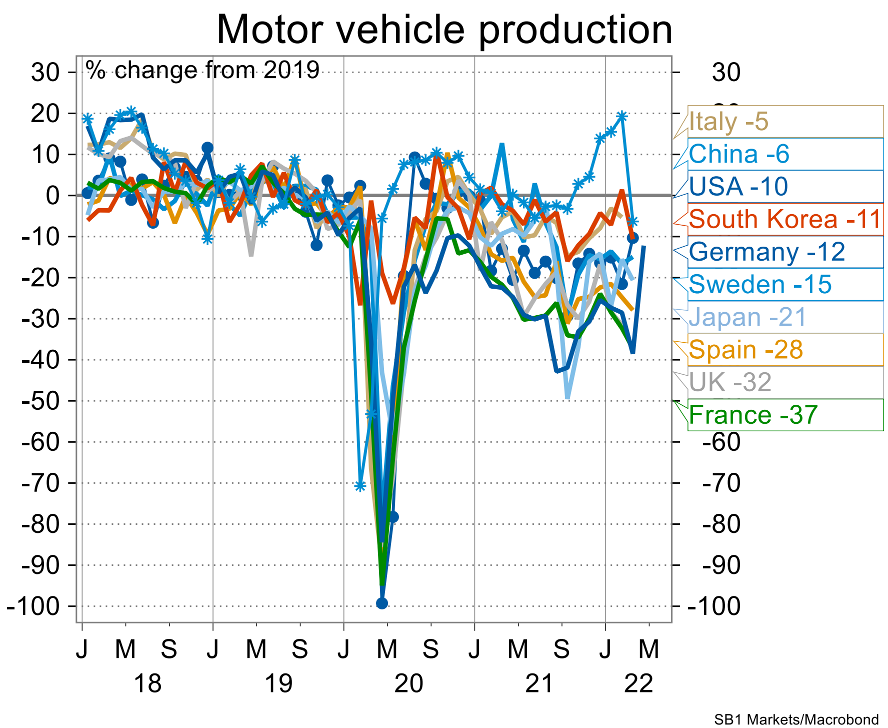


- Sales were stable at close to 150' in April
- Sales fell sharply in Q1, from an ATH level in Q4-21
- Last year, 192' autos were first-time registered –above the previous ATH at 185' in 2017 – and before that 173' in 2006!
  - » Sales have been much stronger than in any other rich country. Even the Q1-22 level is 'only' 10% below the 2019 level, 'just' because global sales were down 22%

SpareBank 1 MARKETS

German auto production reported sharply up in April – from a weak March

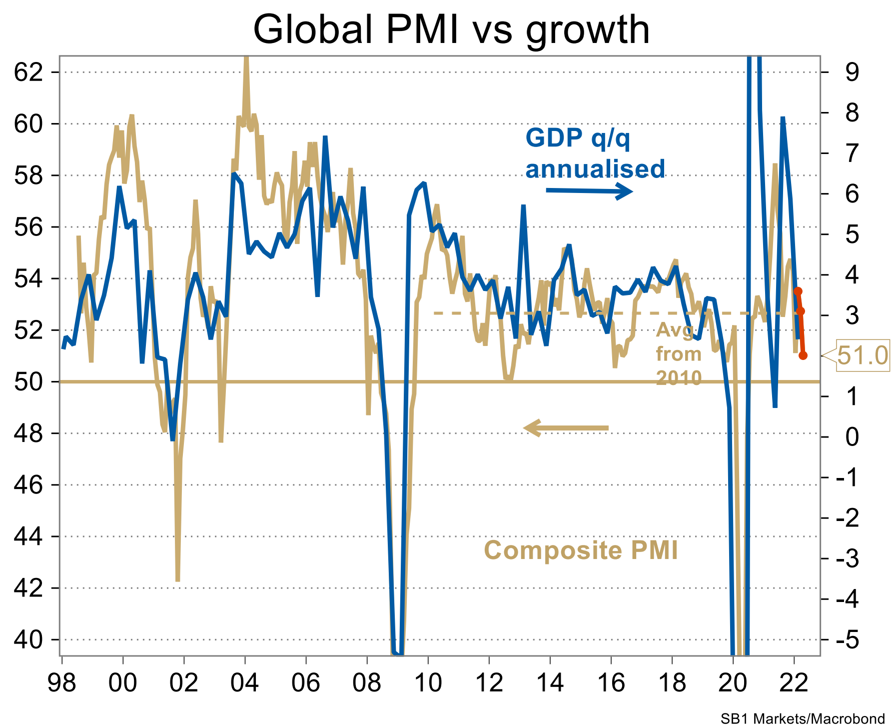
Chinese auto production fell sharply in March, very likely due to lockdown problems

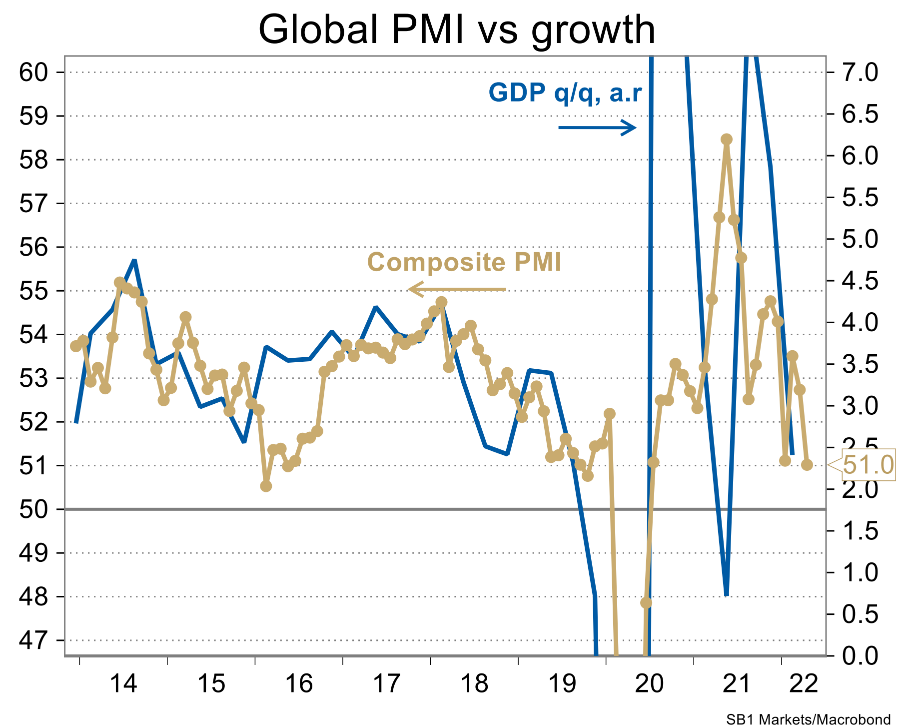


- The war in Ukraine may lead to more supply chain challenges for the auto industry, like lack of Ukrainian neon gas for semiconductor production or car parts from Ukraine

The global economy slowed further in April – almost entirely due to China

The global index fell 1.7 p to 51.0, the weakest level in 2 years

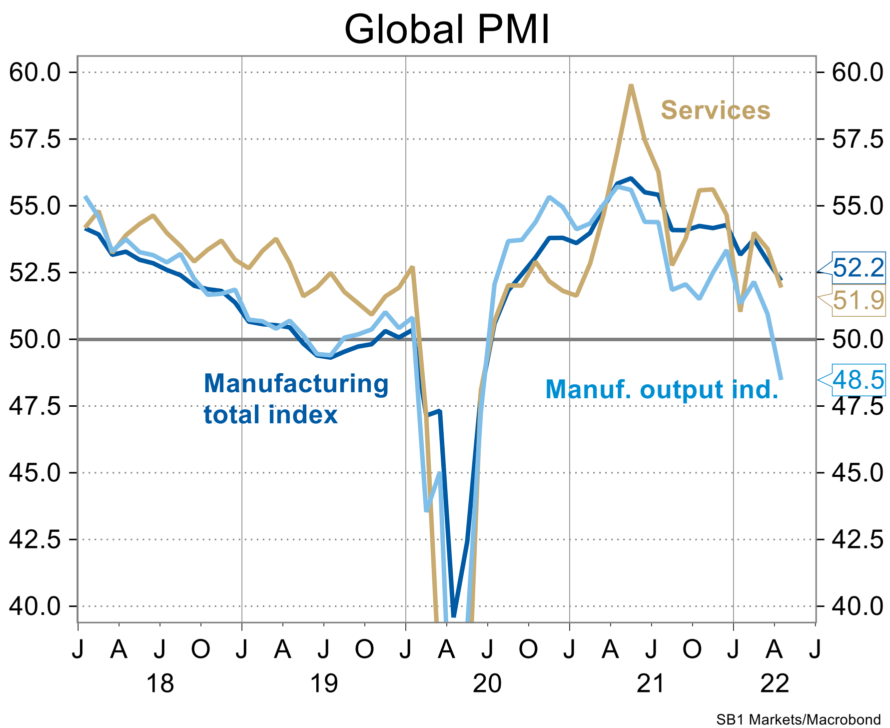


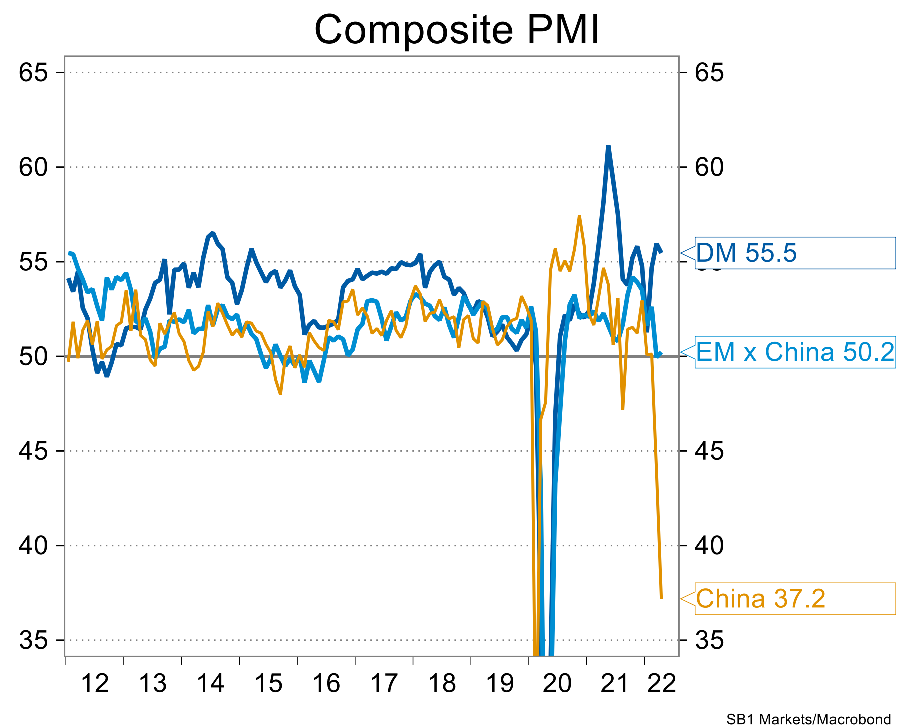


- A large, further decline in the service sector PMI in China in April, led to a larger decline in the global composite PMI than we assumed
- However, barring the decline in the Chinese PMIs (the manufacturing output index also 'collapsed'), the global index was just marginally down, with an uptick in EM ex China (India and Hong Kong contributed) and in the EMU. The EMU PMI was above the February level in April!
- **Delivery times** rose – and all **price indices** rose – and most to new ATH. So war & sanctions (and Chinese lockdowns) have some impacts…

The manufacturing output straight down – but stable ex China!

The service sector PMI also just marginally down ex China





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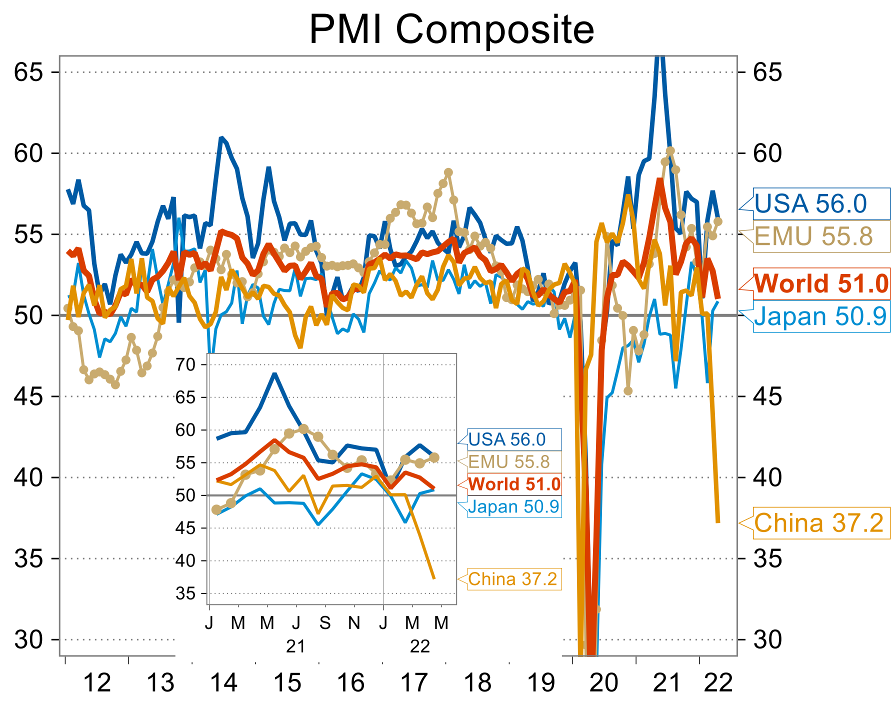
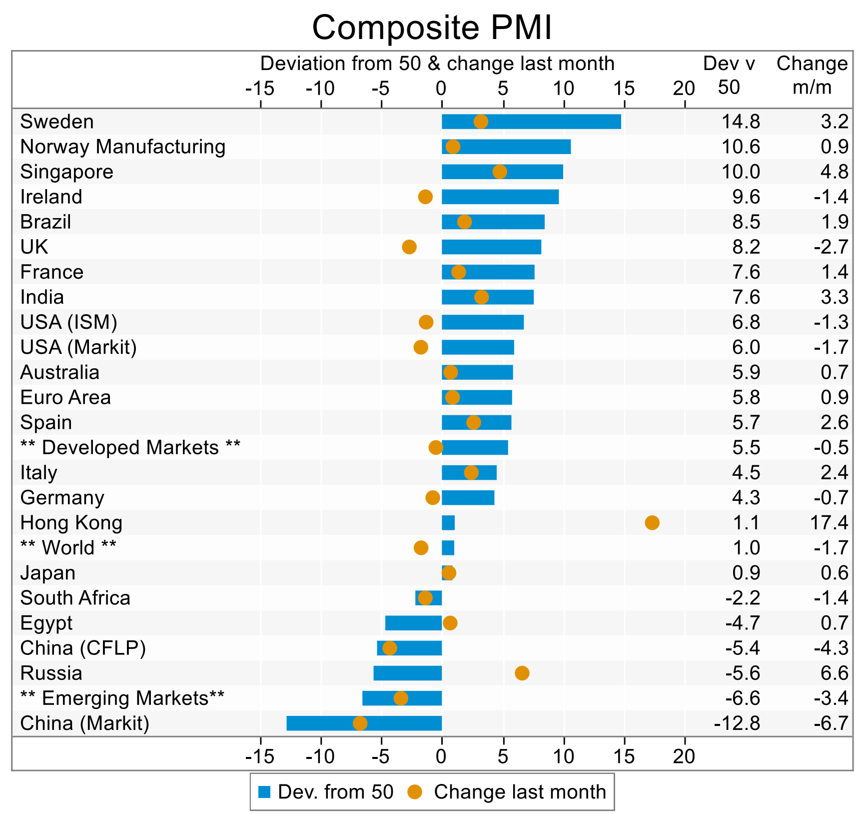
The global composite PMI down, mostly due the lockdown setback in China

The total down 1.7 p to 51.0, more than we assumed, China contributed by 1.3 p



Source: IHS Markit, SB1 Markets, Macrobond

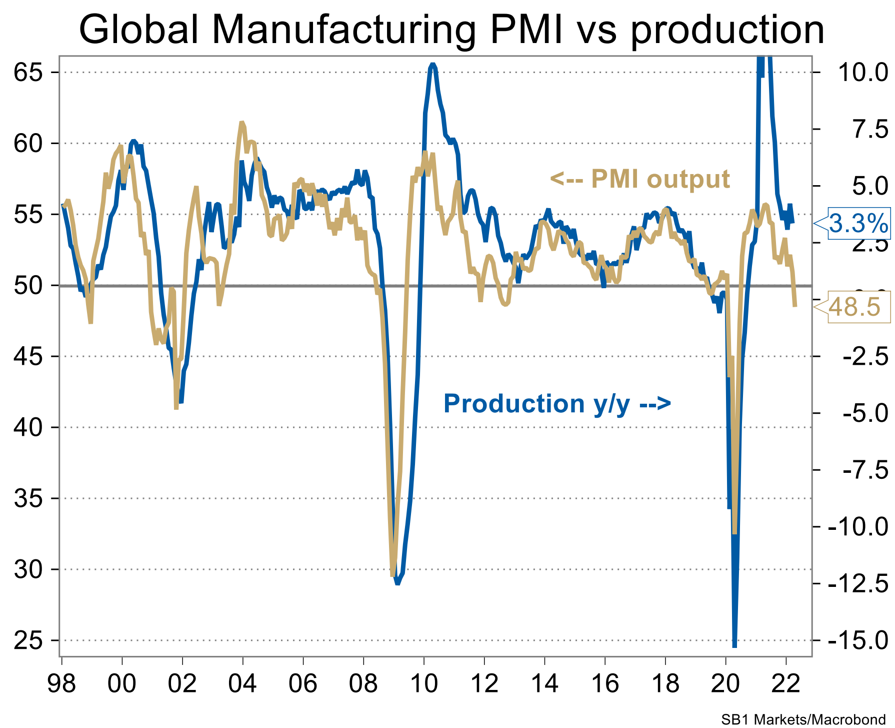


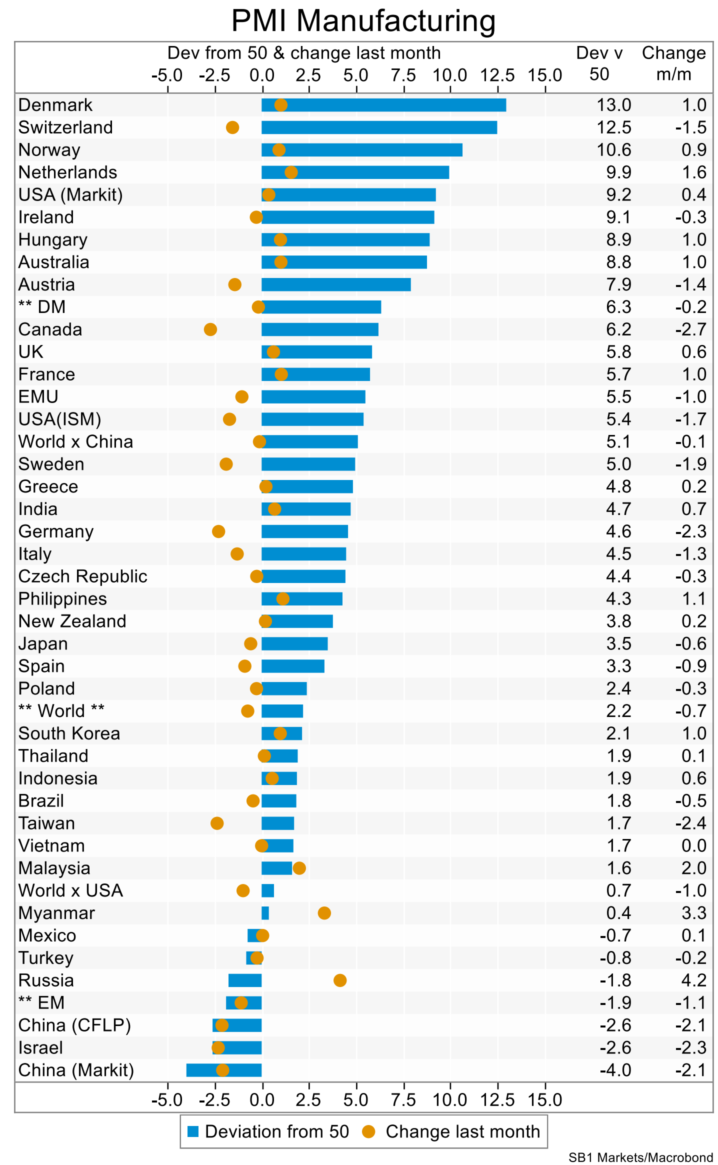
SB1 Markets/Macrobond

- 14 countries/regions up in March (down from 7), and 11 down (from 15)
- **The declines in Russia and China** in March and April have been harsh, even if the Russian PMIs recovered in April. War & sanctions are hurting the Russian economy brutally, according to businesses. China is fighting the virus with its 'impossible' zero tolerance policy. The Hong Kong PMIs were terribly depressed, but recovered by 17.4 p to 51.1. Regrettably, vaccination is far lower in China than in H-K, especially among the elderly
  - » Other EMs OK: Brazil rose further, as did India
- **The rich countries (Developed Markets, DM) PMI** declined 0.5 p due to a 1.7 p drop in the **US,** while EMU gained 0.9 p**,** more than the decline in March
- **Sweden** still has the pole position, ahead of Singapore, and Ireland)
- (**Norway** does not compete here, we just have a manufacturing PMI. The level would have yielded a 2nd place in the composite race)

Manufacturing headline PMI down 0.7 p to 52.2, and the output index to 48.5

7 of 43 surveys below 50. <u>Europe at the top, China at the bottom, Russia close to the bottom</u>

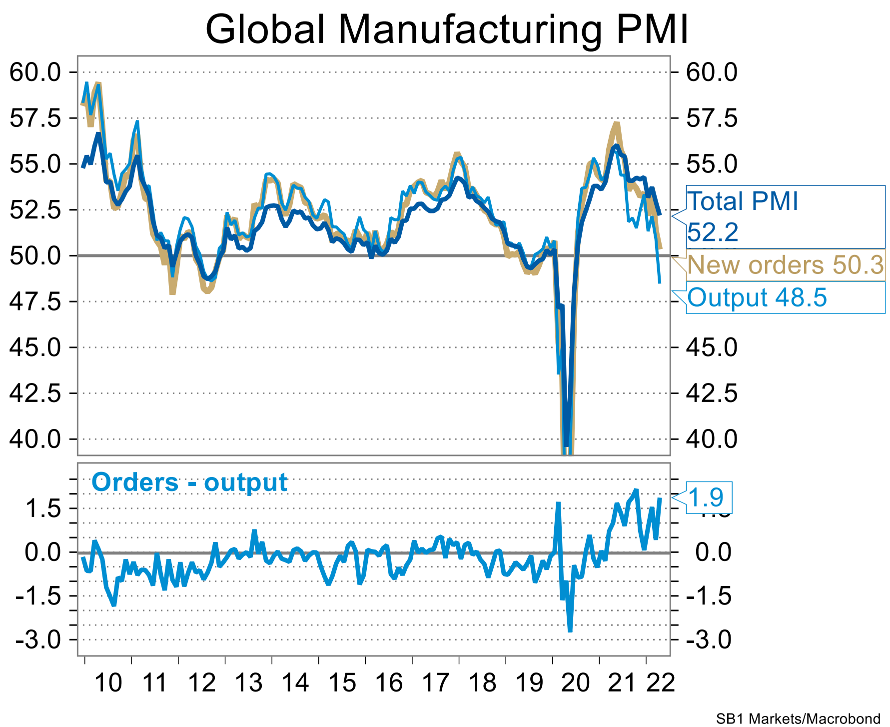


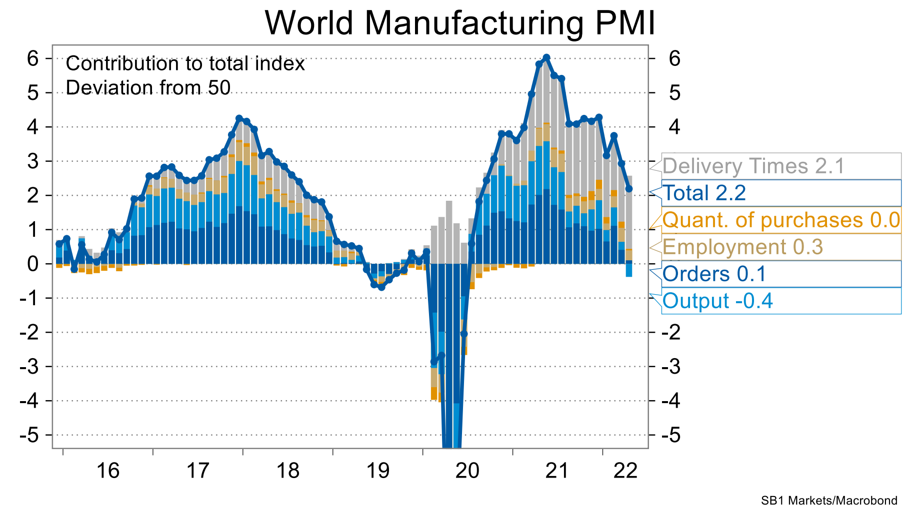


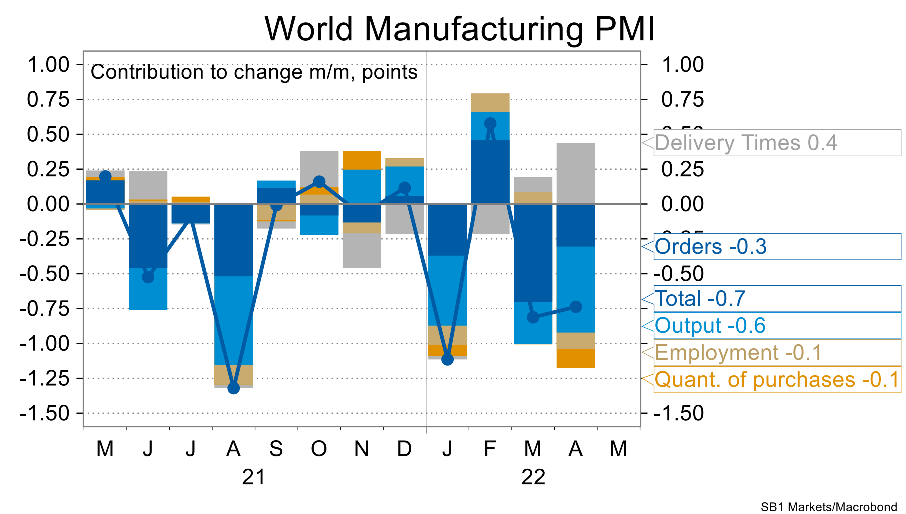
- The **manufacturing output index** fell 2.4 p to 48.8, in line with our forecast based on preliminary data for DMs and China
  - » 46% of countries/regions reported higher total PMIs last month, up from 35% in March
  - » **European countries** still dominate the top of the list. Norway is no. 3
  - » The Chinese indices fell sharply. Rest of EM Asia was broadly up, as was Brazil
  - » Russia reported a solid uptick from a very low level in March, but is still well <50
  - » **Norway** reported a minor decline – and the level is well above average, at 60.6

Manuf. delivery times up, other parts of the PMI down, both orders and output

Not a favourable mix. New orders close to 50 and the output index is well below

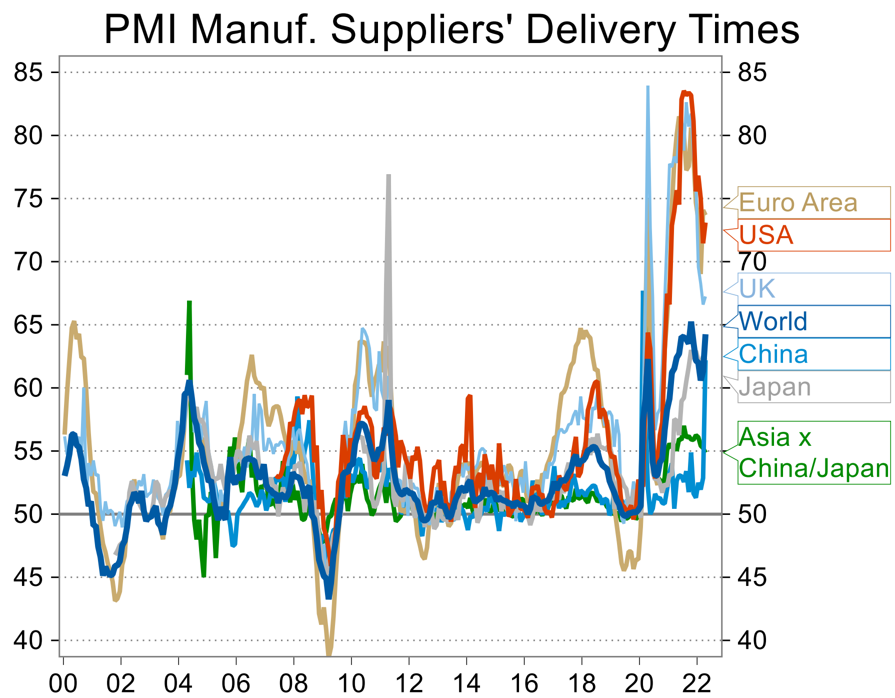




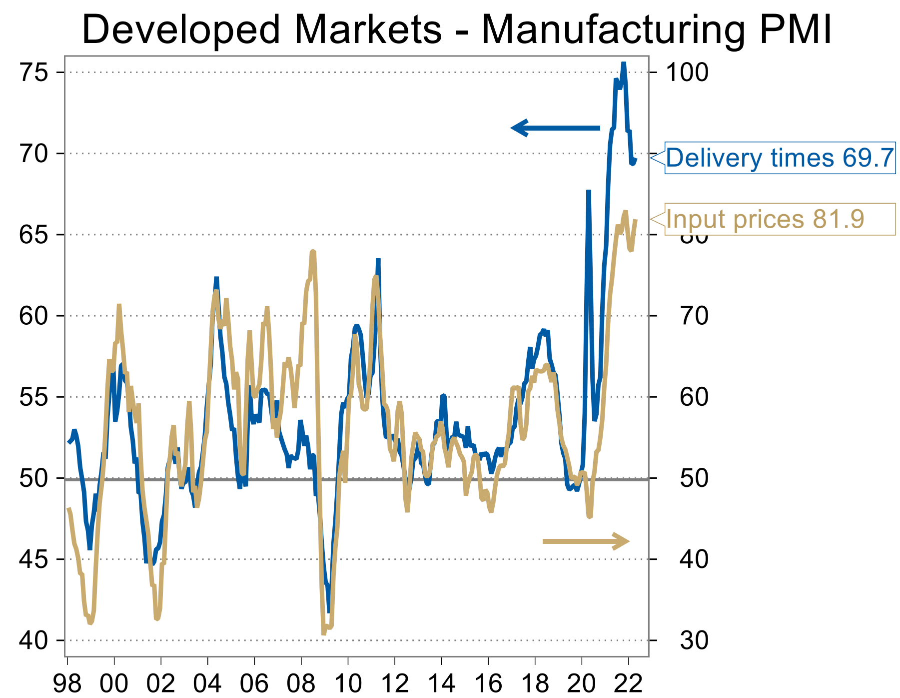


Delivery times straight up in China (and not due to stronger demand…)

Mixed elsewhere – and the trend is down



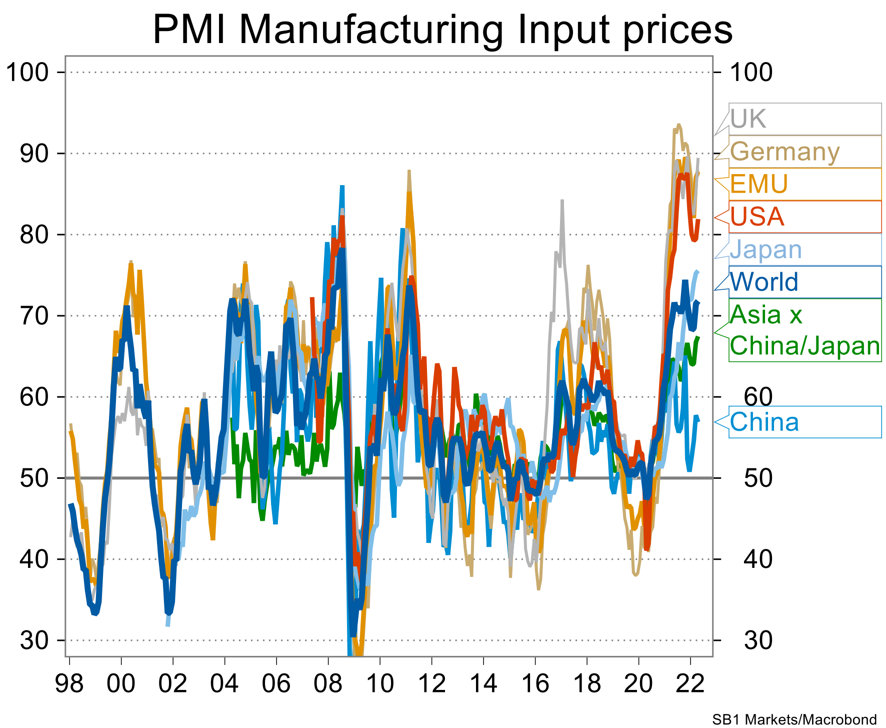
SB1 Markets/Macrobond

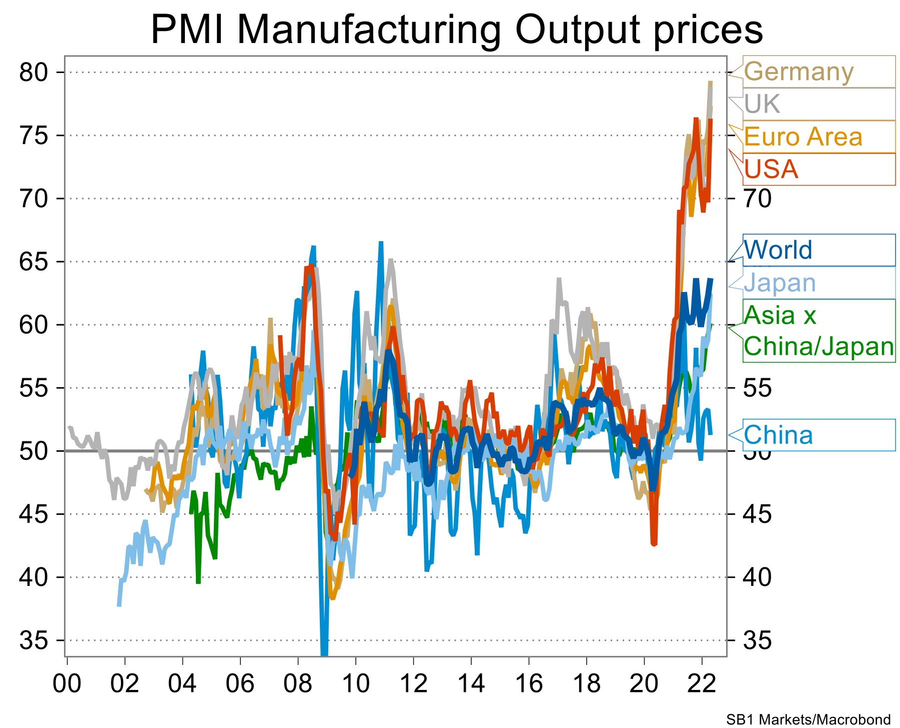


SB1 Markets/Macrobond

Manufacturing input prices rose faster in April, output prices at new ATH

Price increases have been the rich man’s problem – because demand has been strong here

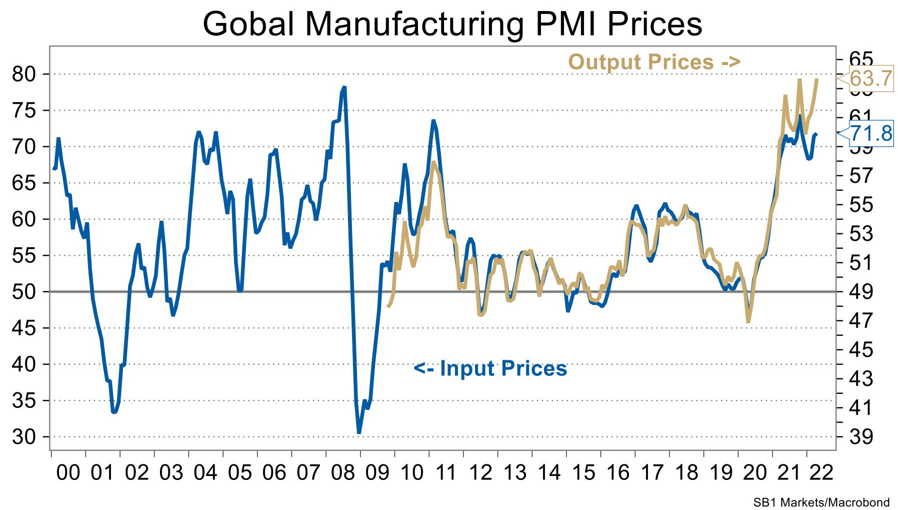


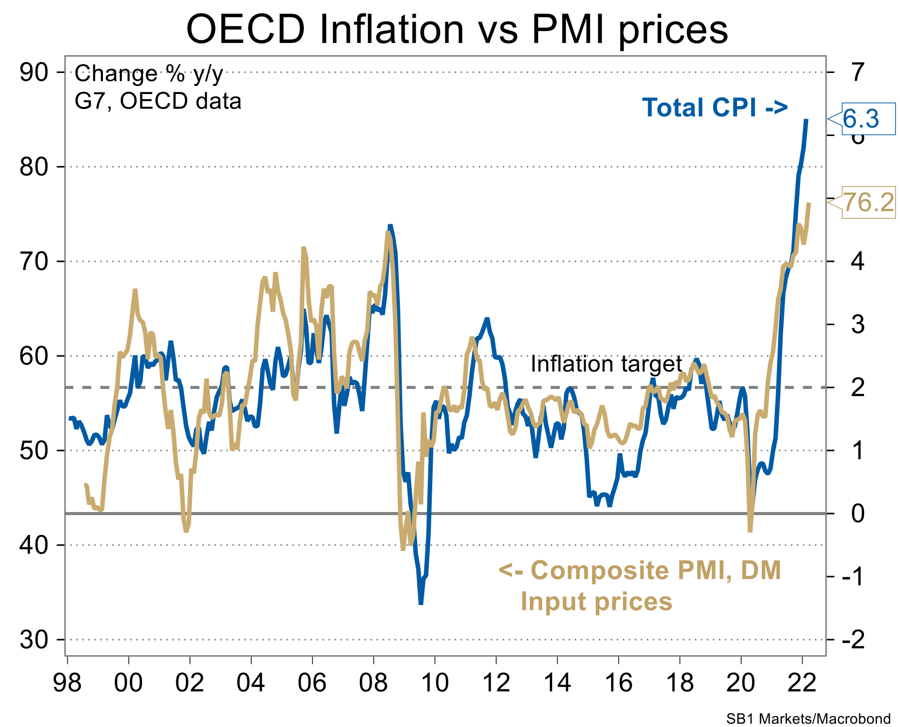


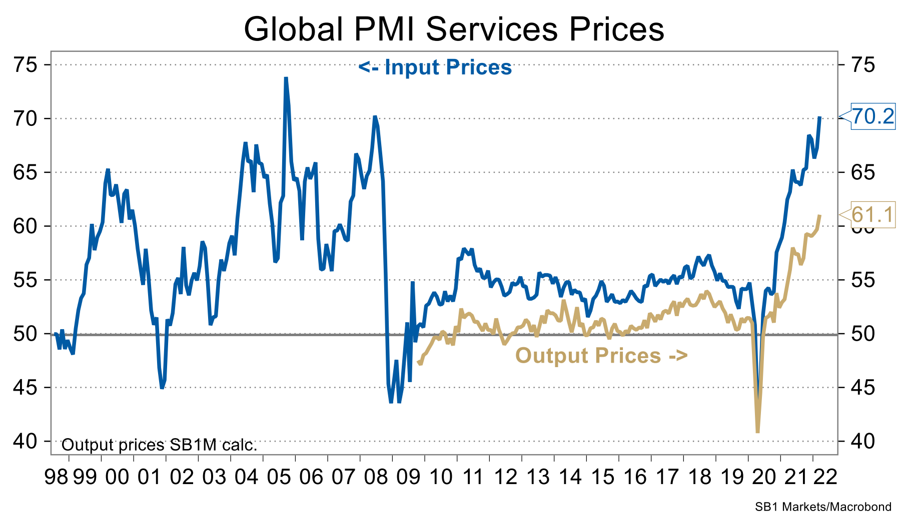
- Germany, UK and Japan reported the fastest growth in output prices ever, the US close to fastest
- Chinese output prices slowed

All aggregated price indices up in April – and 3 of 4 up to ATH

Which of course does not signal a rapid decrease in monthly inflation rates

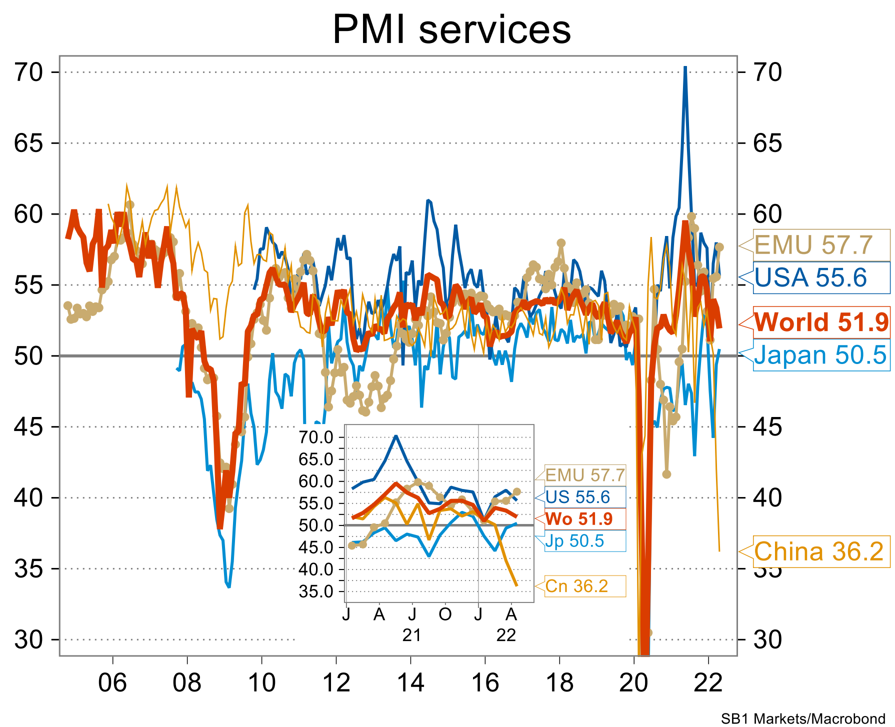


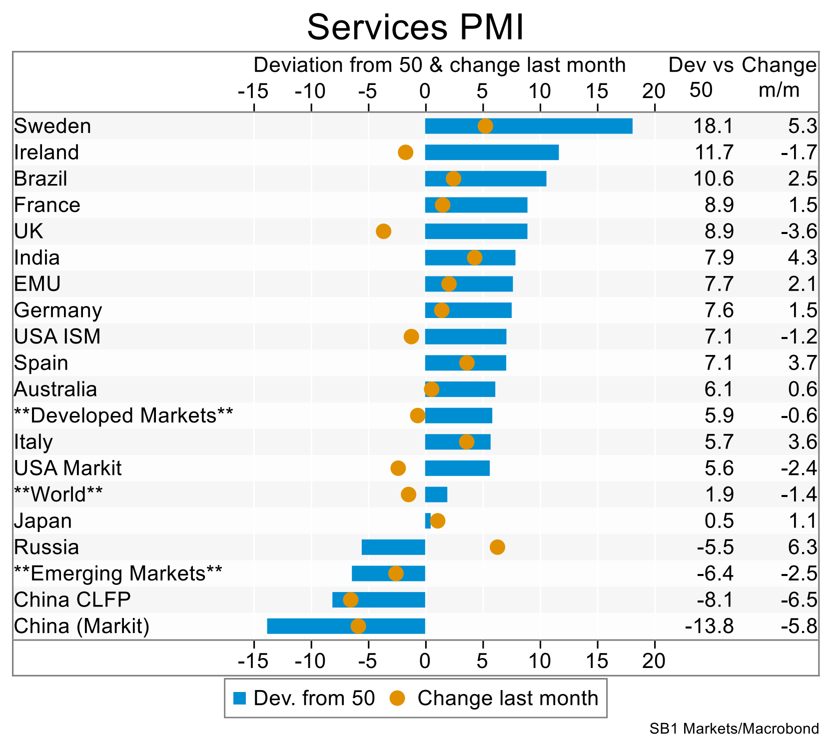




In services, only Russia and China below par. China the most down in April

The global index down by 1.4 p to 51.9. Developed markets at 55.9. EMU +2.1 p to 57.7! Sweden on top

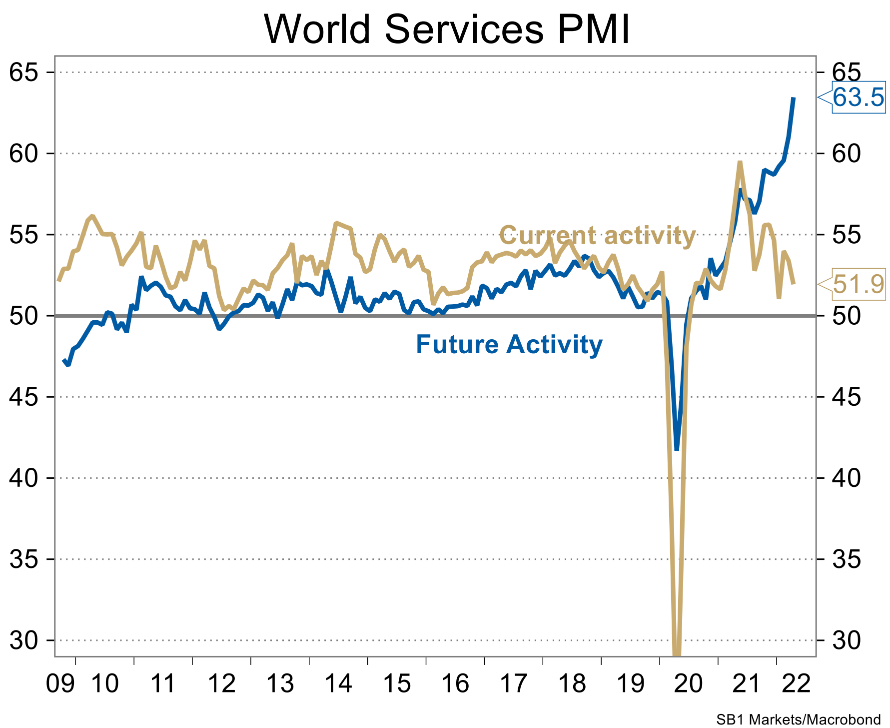


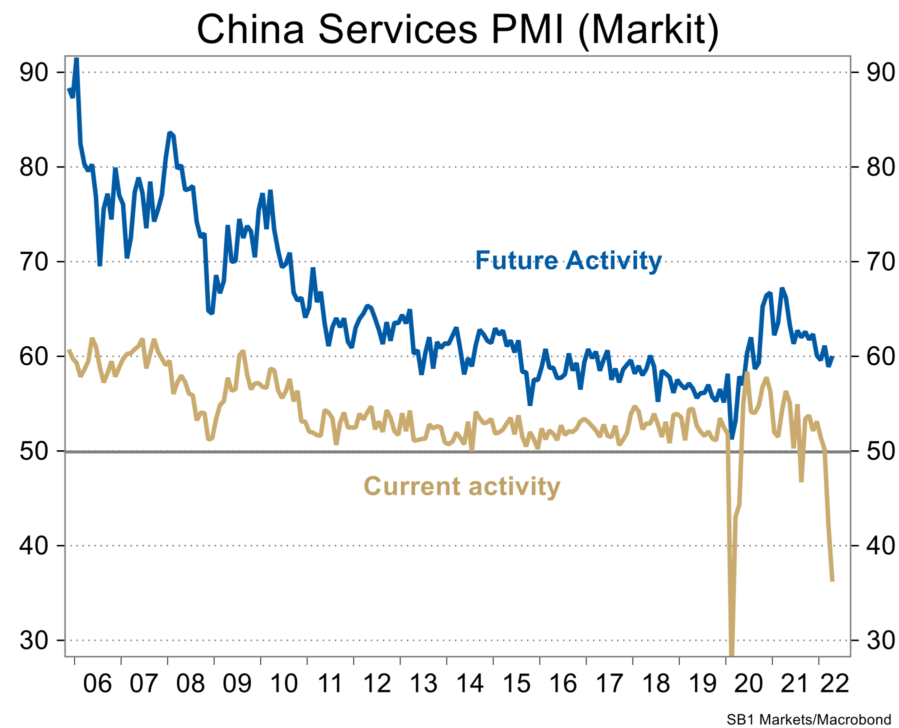


- **The global service sector PMI** declined slightly more than we assumed. China surprised on the downside, but others on the upside
- **The March and April setbacks in Russia and China are dramatic.** In Russia, a steep decline in activity is signalled by a 44.5 PMI (though up 6.3 p!). Chinese services are reporting a steep decline in activity due to the corona lockdown

The service sector expects better times ahead than ever before

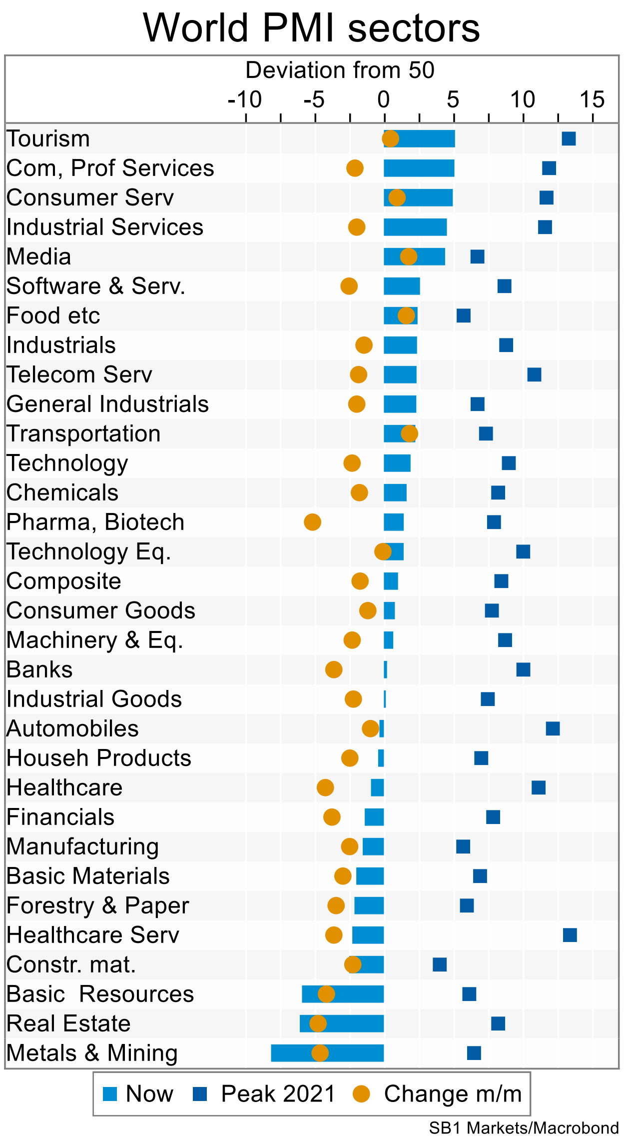
At least outside China – but even services in China are still rather upbeat

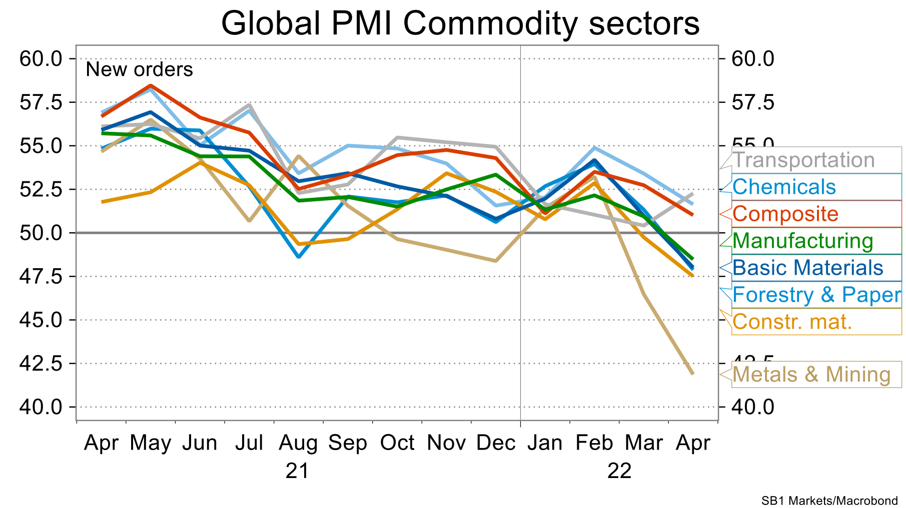


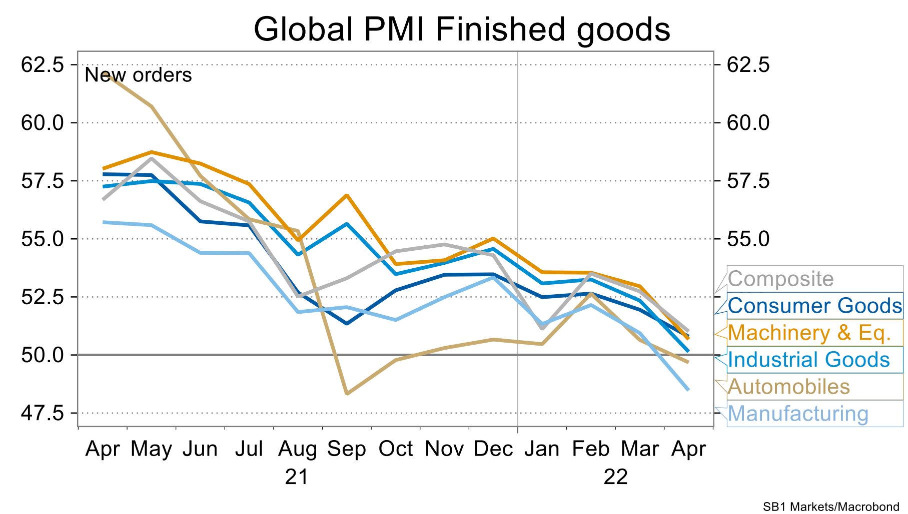


Almost all sectors reported slower growth in April. Basic materials/metals <50

5 sectors up, 17 down. 12 sectors are below the 50-line, 20 are still above



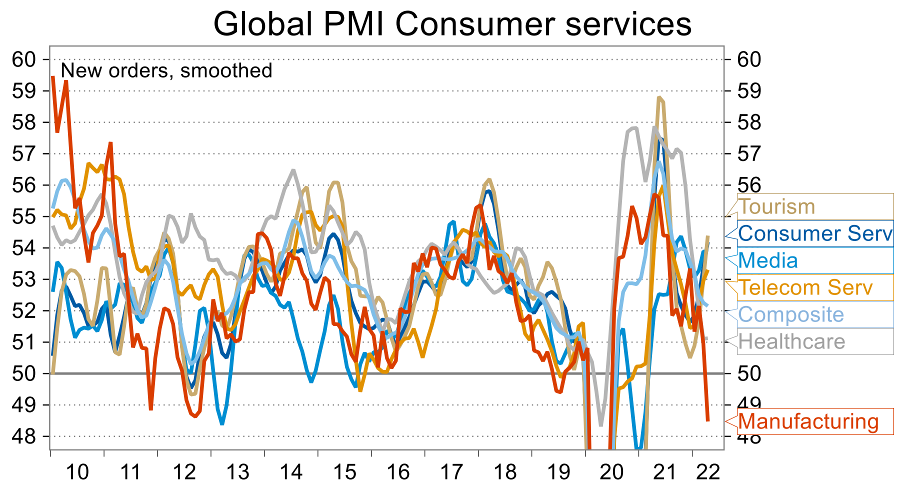


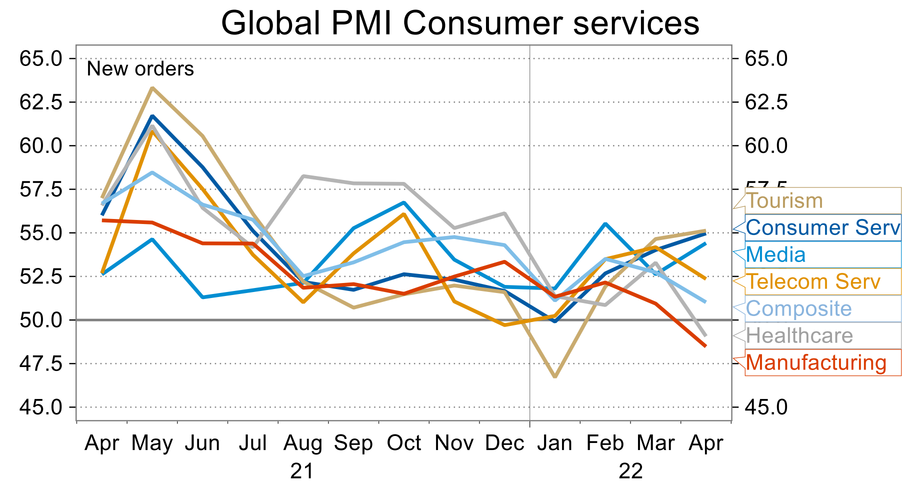


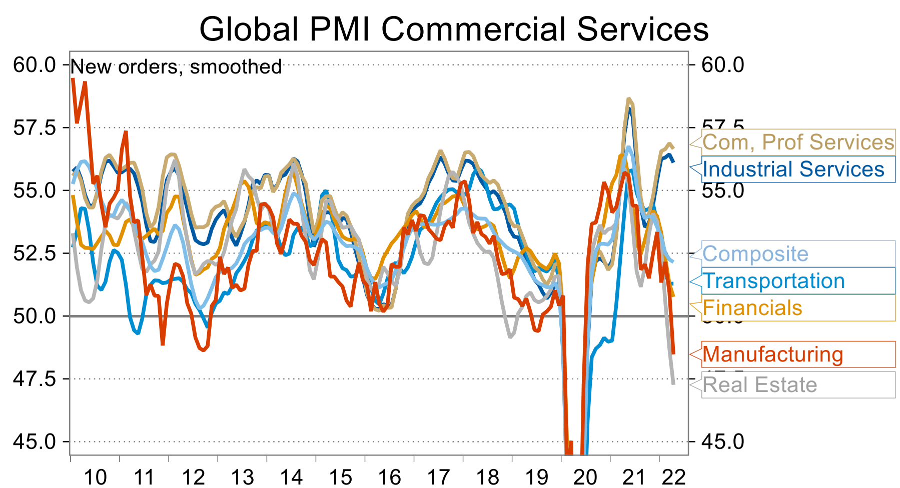
SpareBank 1 MARKETS

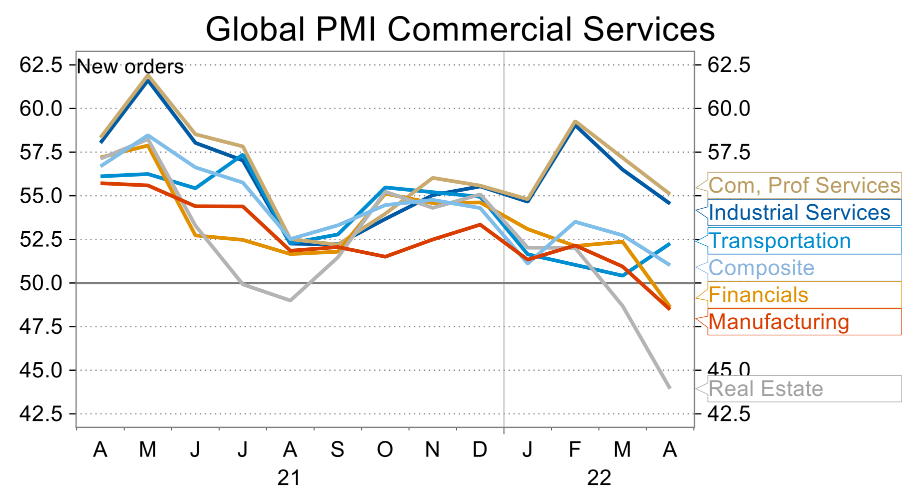
Services are reporting growth, but most sectors slowed down in March

Beware real estate: A sharp decline in April



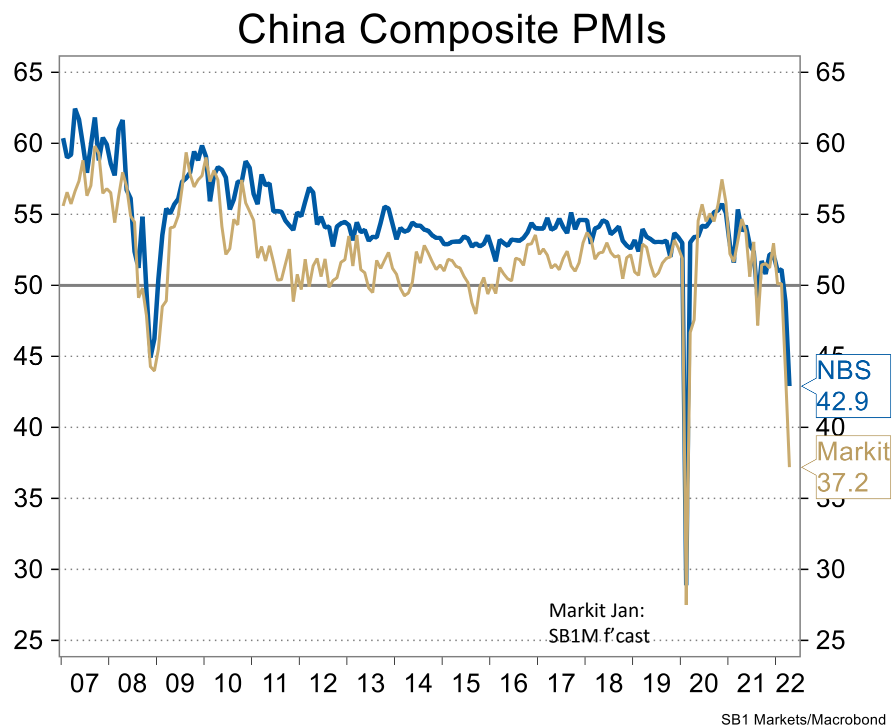


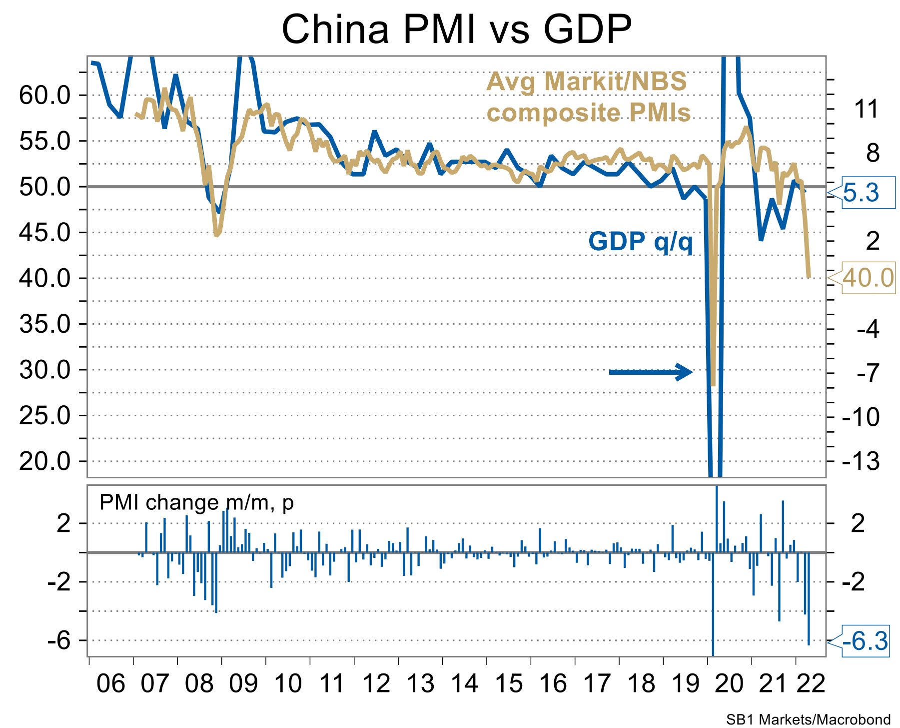




Both PMI data sets fell sharply in April, and Markit's even more than we assumed

The composite average declined 6.3 p to 40, the 2nd lowest ever, as lockdowns reduced economic act.

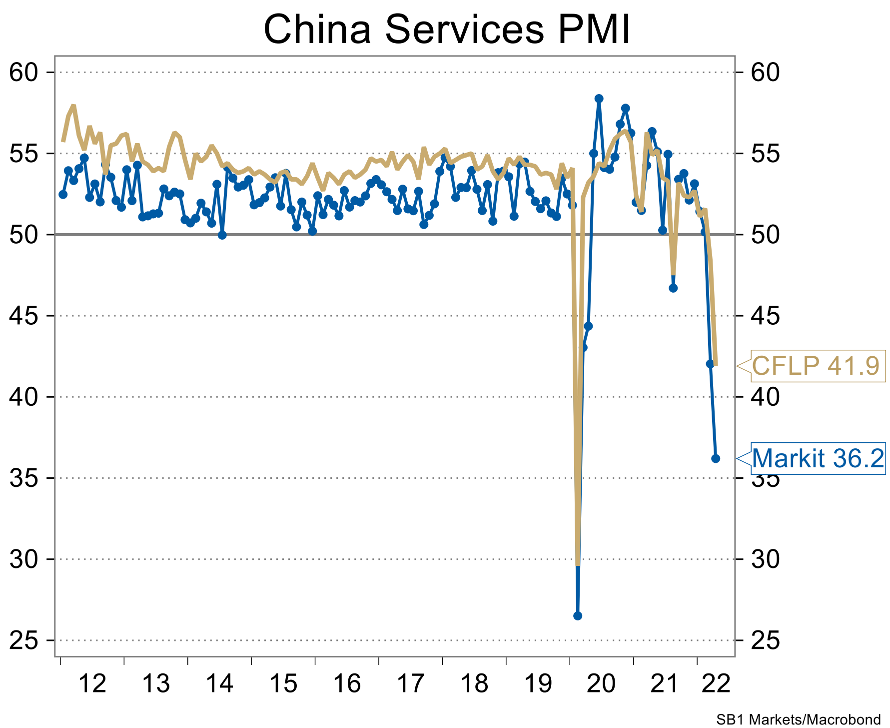


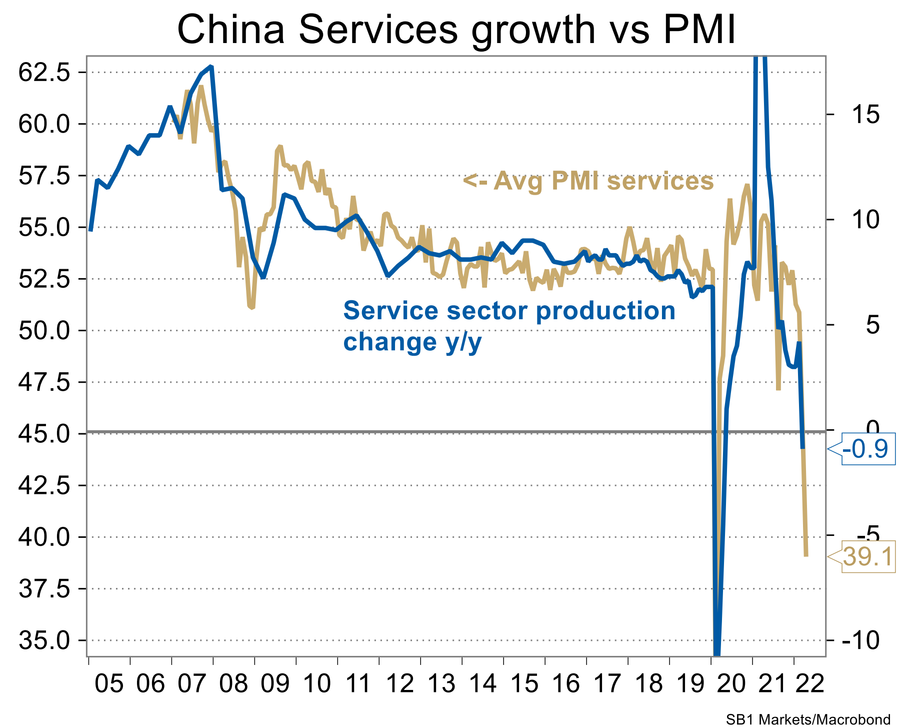


- **Markit's** service sector PMI declined almost 6 p, following the 8 p drop in March, down to 36.3 – expected down 1 p to 41. The composite index fell 6.7 p to 37.2, the 2nd lowest ever, just Feb-20 was worse
- The **CFLP/NBS composite PMI** nosedived 5.9 p to 42.9, also the 2nd weakest. **The average of the two PMI data sets** declined to 40.0, signalling zero growth in the Chinese economy – but the calibration is far from perfect
- The PMIs are signalling that the lockdowns have hurt the economy badly, but as they are less rigorous (on average, for the whole country), the economic impact is less than during the first lockdowns in February 2020. The impact will of course be felt in many global supply chains, even if restrictions are now gradually eased in some cities

Markit's services also fell further in April, by 5.8 p!

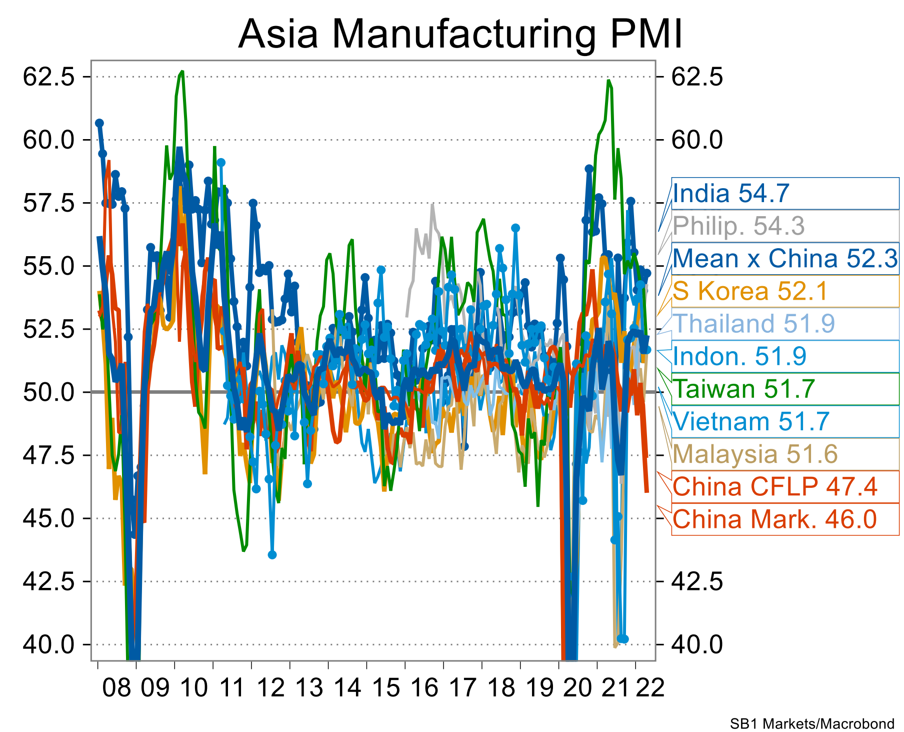
Both service sector PMIs are at the 2nd lowest level ever, confirming the high cost of the lockdowns

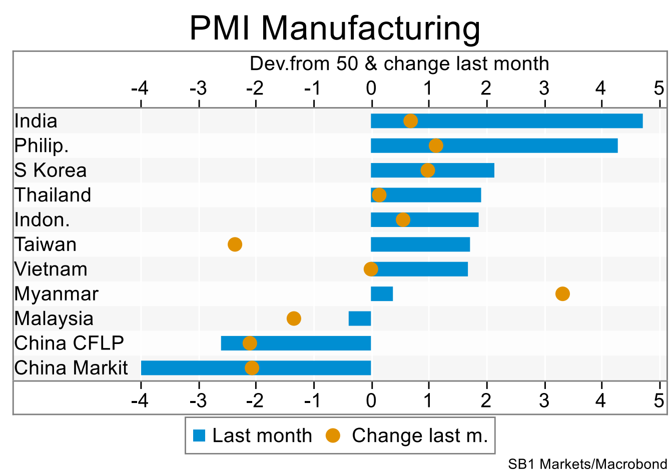


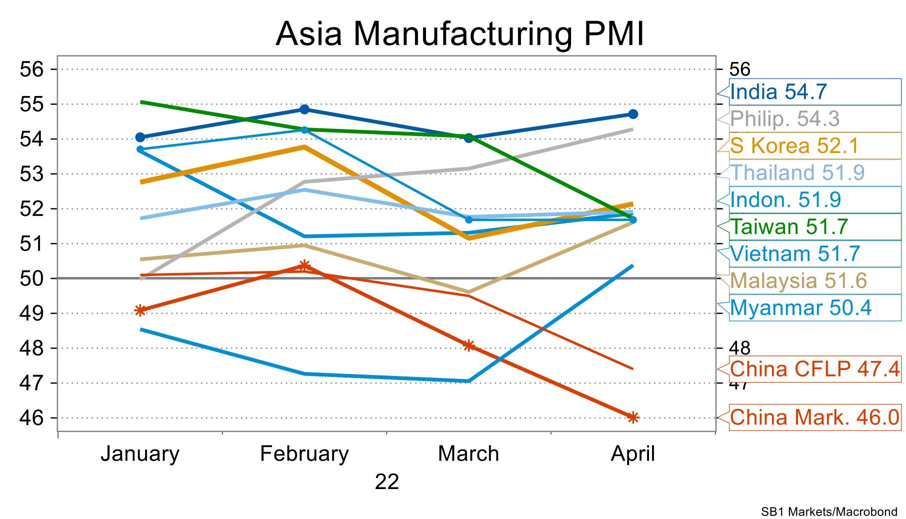


EM Asia: More up than down in April – but China is struggling, Taiwan slowing

All but the Chinese PMIs are above the 50 line, and all but China & Taiwan reported an uptick in April!





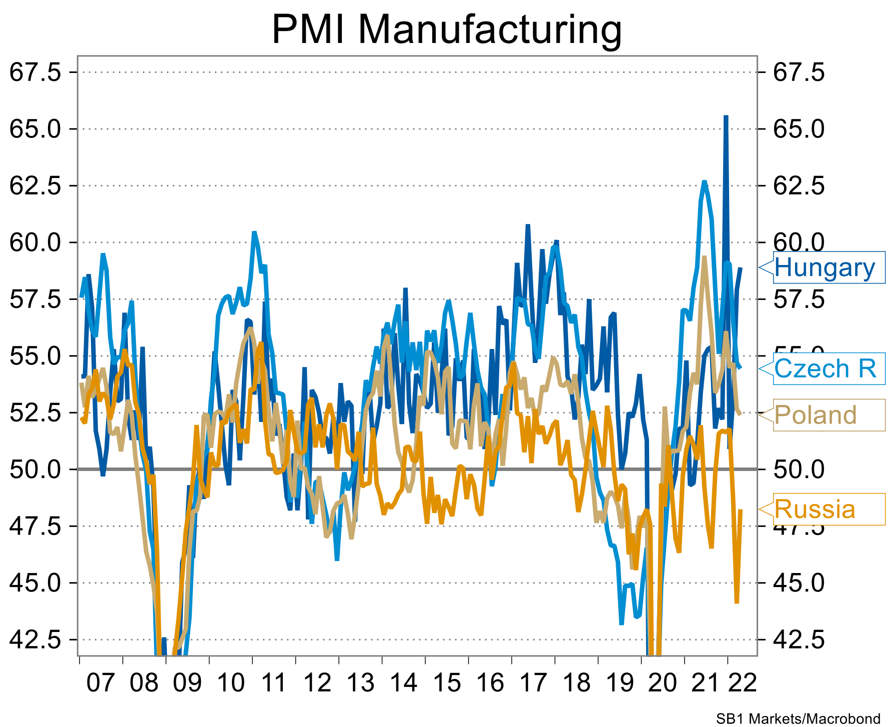


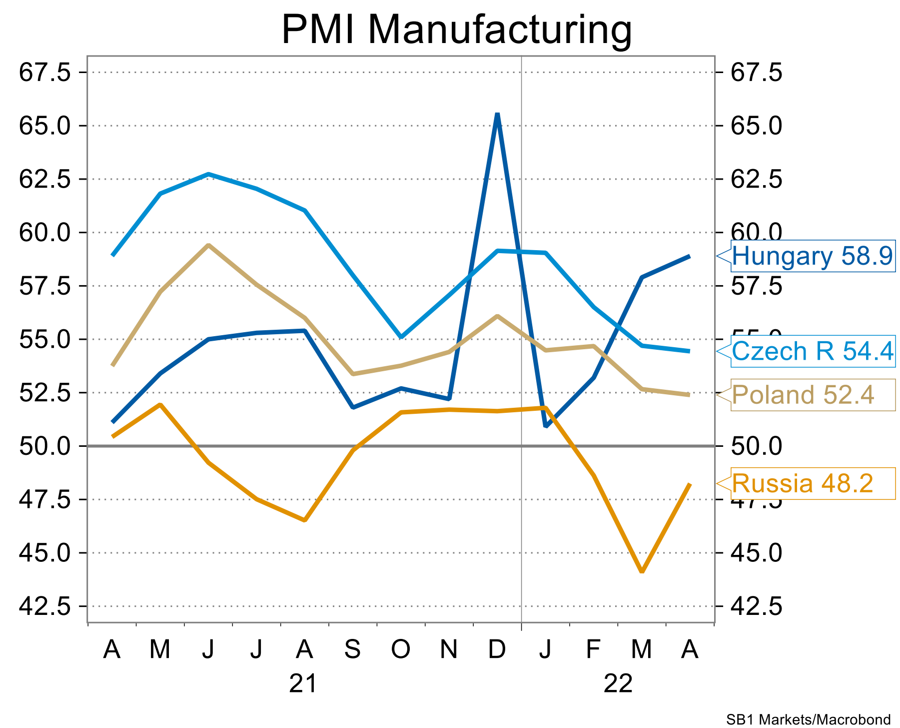
- So far, a Chinese problem – with some impact in Taiwan as well

SpareBank 1 MARKETS

No abrupt halt in Eastern Europe – and the Russian manuf. PMI rose in April

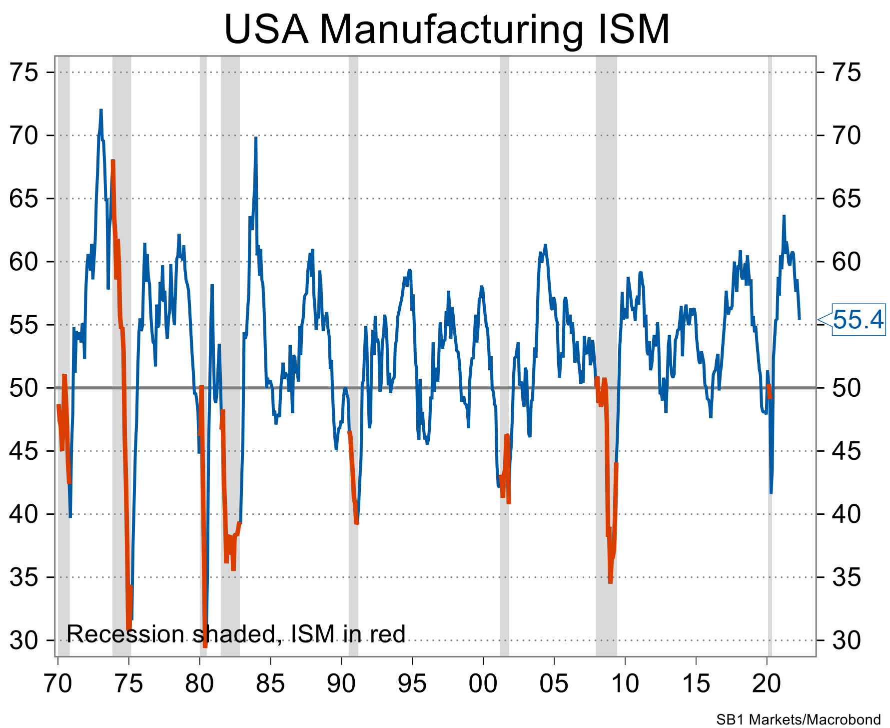
Activity in the Russian manufacturing sector is still contracting but at a slower pace

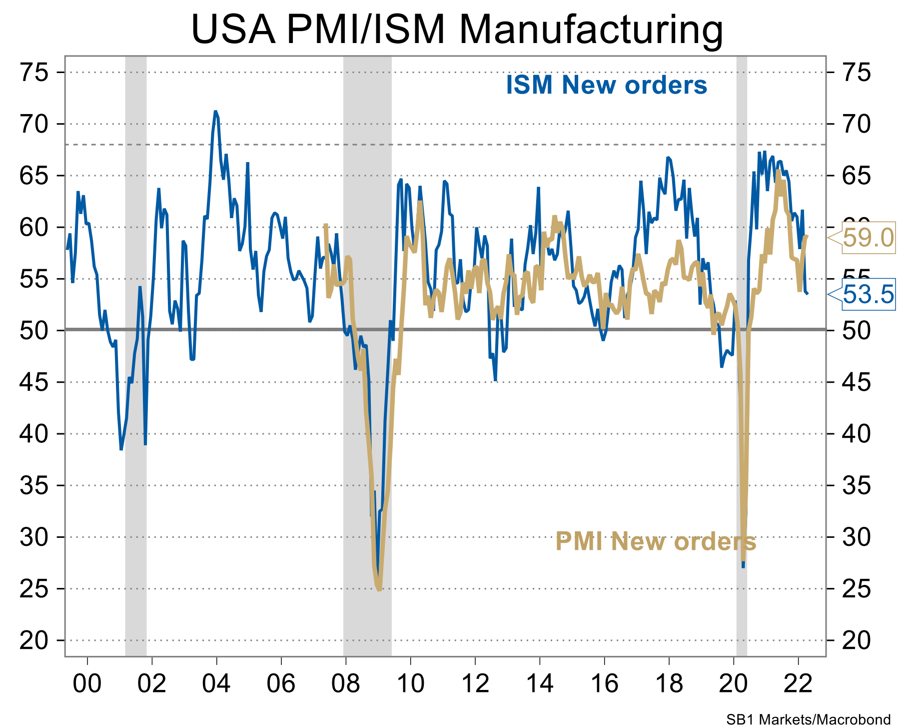




Manufacturing ISM headed down, and will continue downwards?

The total index fell 1.7p to 55.1, expected up to 57.8



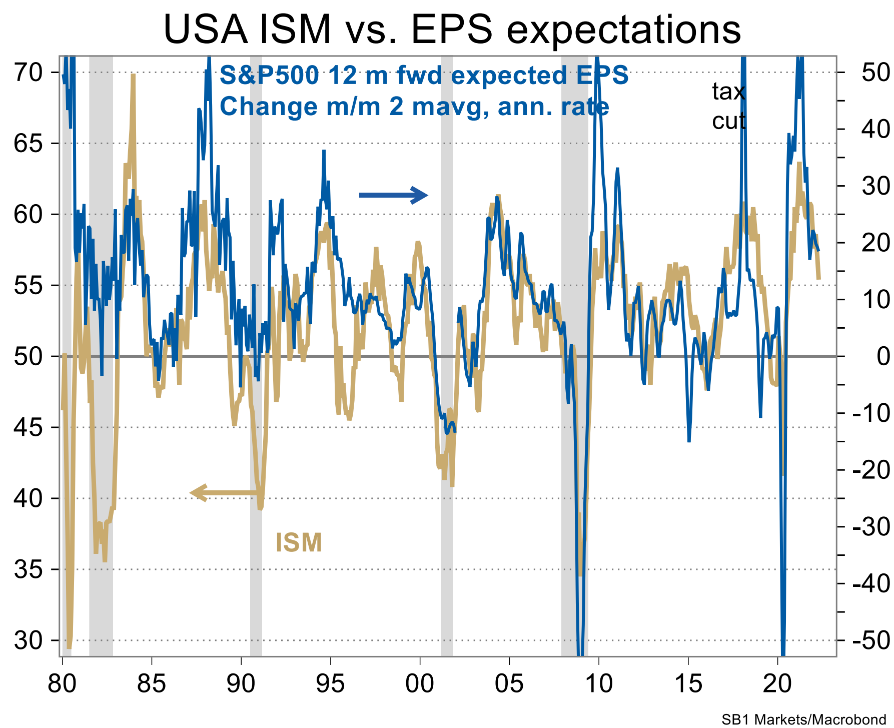


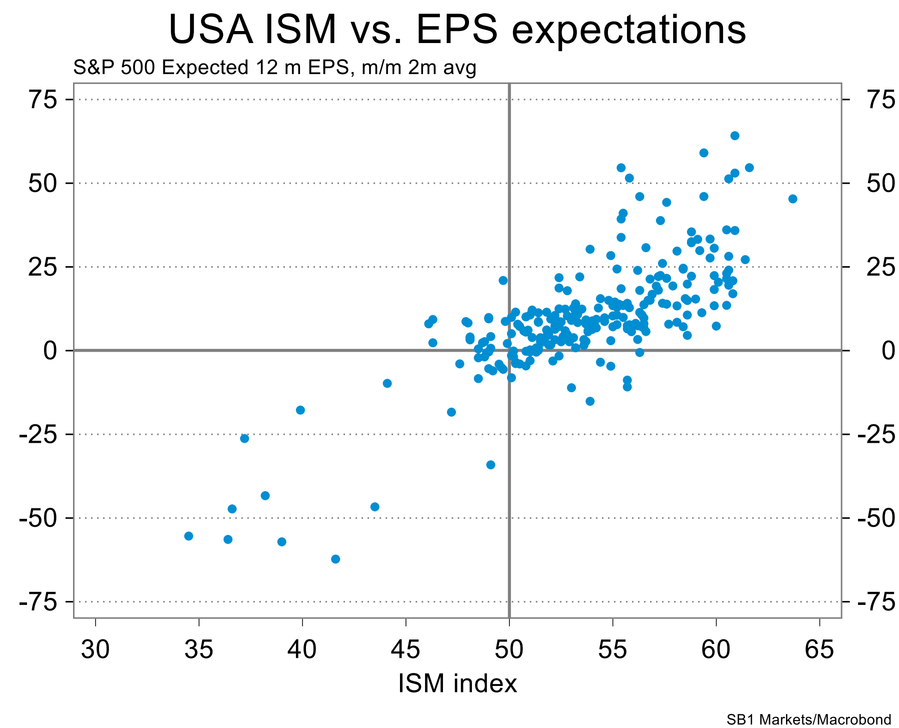
The **ISM manufacturing index is trending down but not yet at low level. However, at the current speed of decline, we are soon there**

- Last month, 17 of 18 manufacturing sectors reported growth (15 the prev. month), just 1 sector report a decline (Petroleum & Coal products, down from 2 sectors last month)
  - » The **new orders** index fell just 0.3 p to 53.5 – but it was above 60 in February
- 36 commodities saw **price increases** (from 43, at the peak 56 commodities). Just natural gas prices were reported as falling (strange, they actually rose)
- 18 commodities were reported in **short supply,** down from 24 (and far below the peak at 50 commodities a few months ago)
- **In their comments**, companies still report supply chain issues, now due to China (and not the war in Ukraine) – but some easing is reported

When the ISM turns south, growth in expected earnings always join

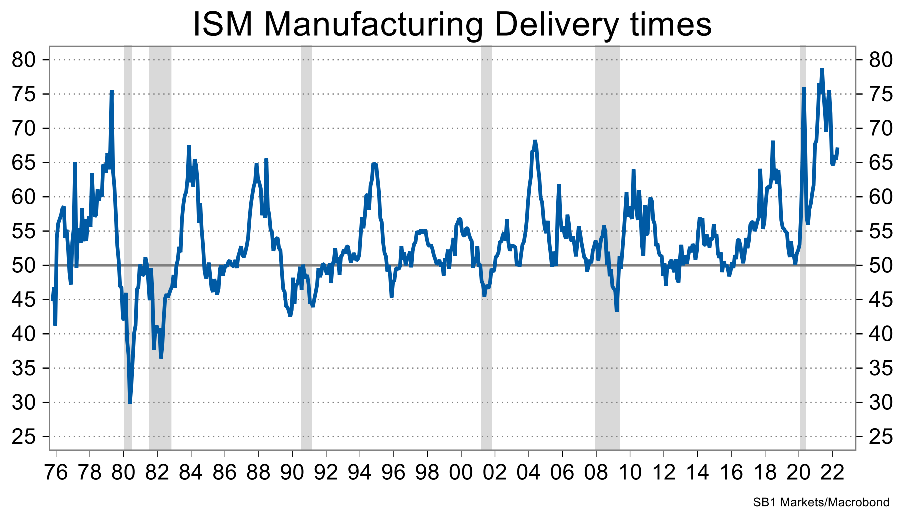
At 55, decent earnings growth is normally assumed. But not at 50

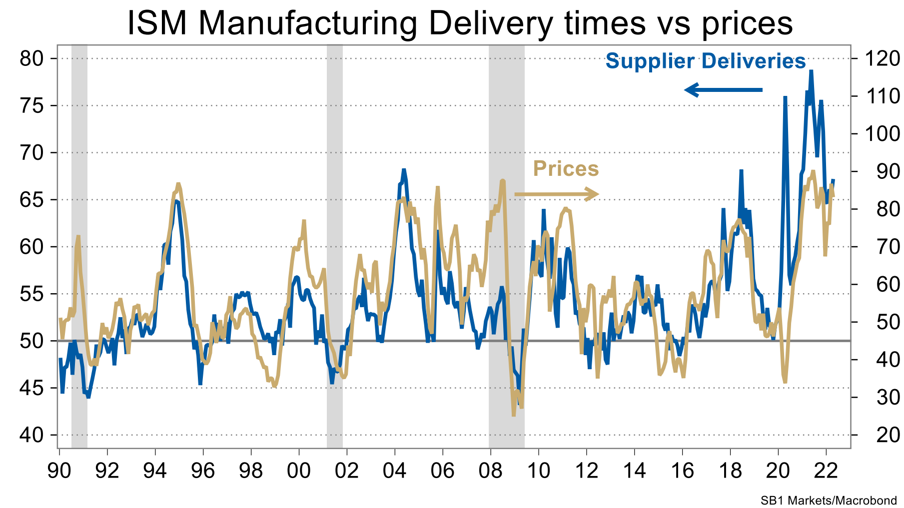


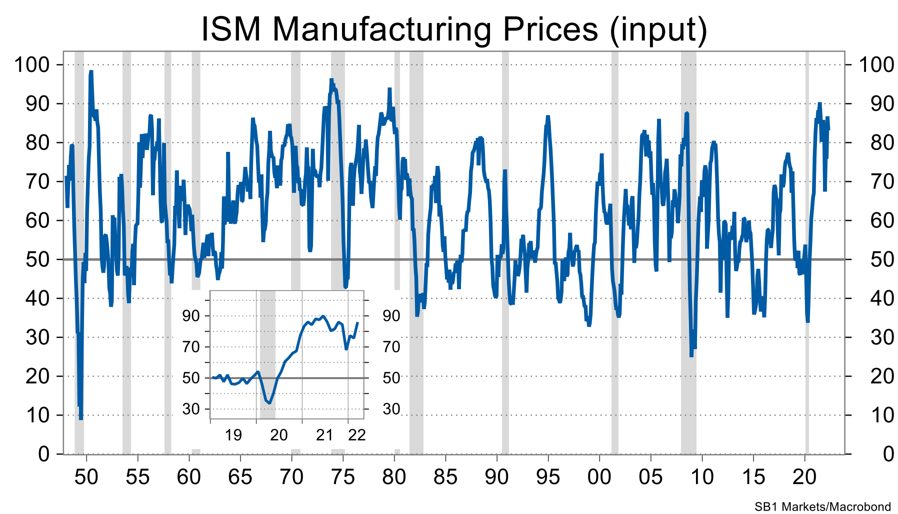


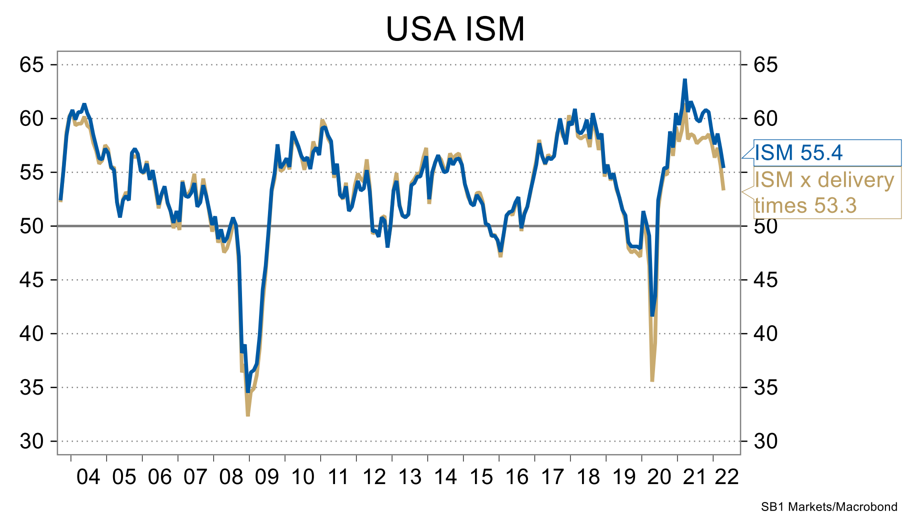
The delivery index still at a high level, and input prices rose fast in April too

A high delivery times index is not necessarily a sign of strength. 'Real' ISM is weaker than total index









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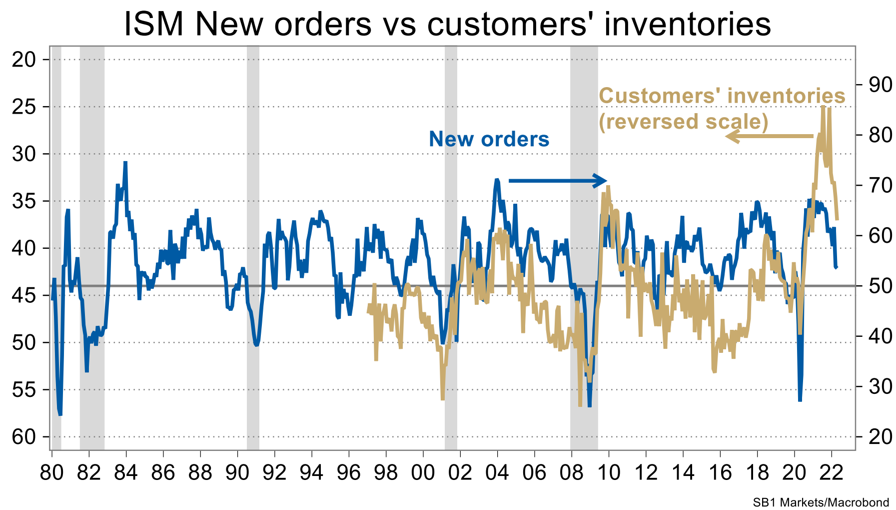
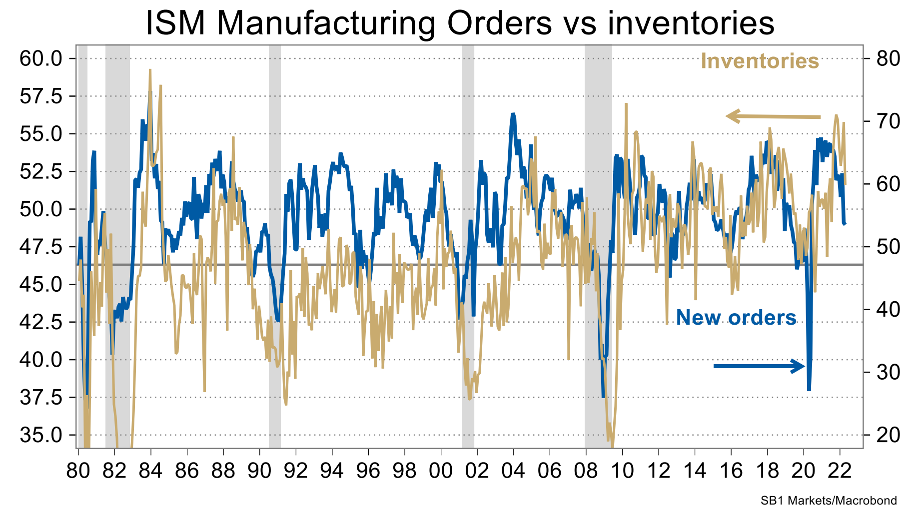
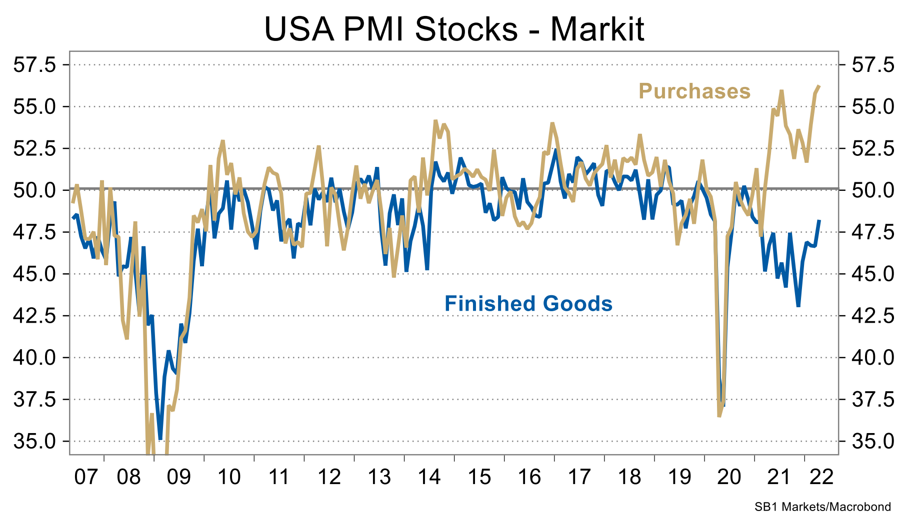
Growth in new orders is slowing, and inventories of purchases are growing

Customer's inventories are still declining, but slower. Signals a slowdown in activity the coming mos.





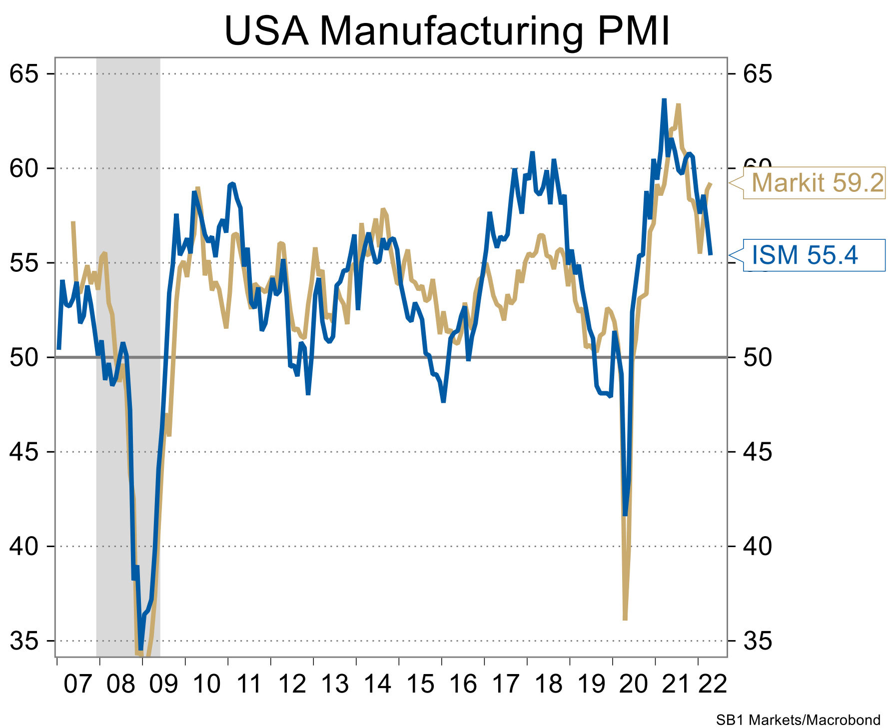


- Growth in manufacturers' **own inventories** (of purchases, not finished goods) is still higher than normal. Inventories must be pretty rich:
  1) Production is running slower than expected, due to weaker demand or due lack of some components, labour, transport services etc.
  2) Companies have been hoarding materials, just to be sure to have them at hand (and if so they will stop doing it soon)

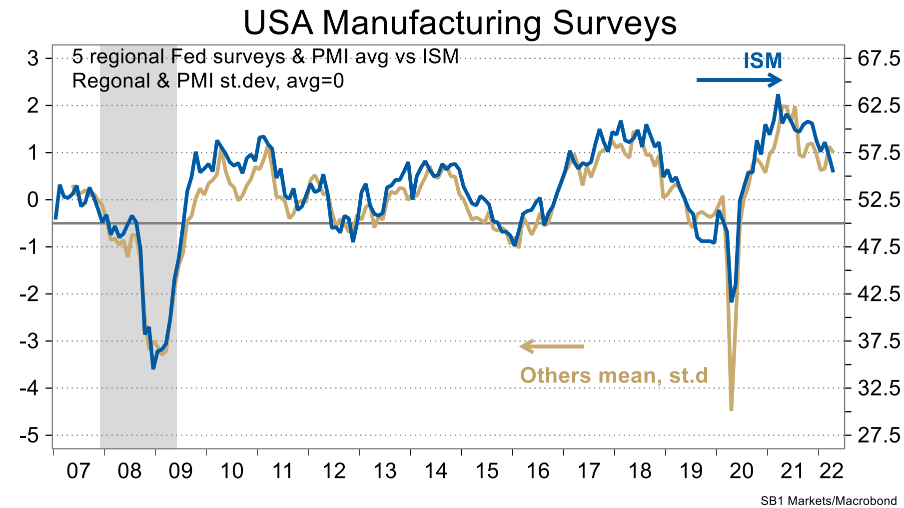
  Probably elements of both – but hoarding has probably been an element in the supply chain stress
- **Inventories of finished goods** (in Markit's report) are still on the way down, according to the PMI, which supports the hoarding explanation (which is good news vs the outlook)

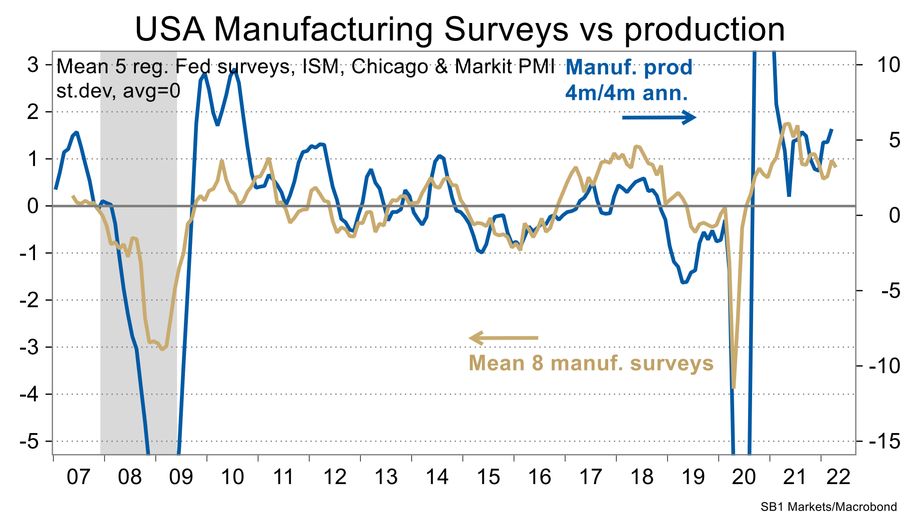
Sum of manufacturing surveys: Marginally down – and the trend is down

Growth is still signalled to be well above trend – but growth is most likely slowing



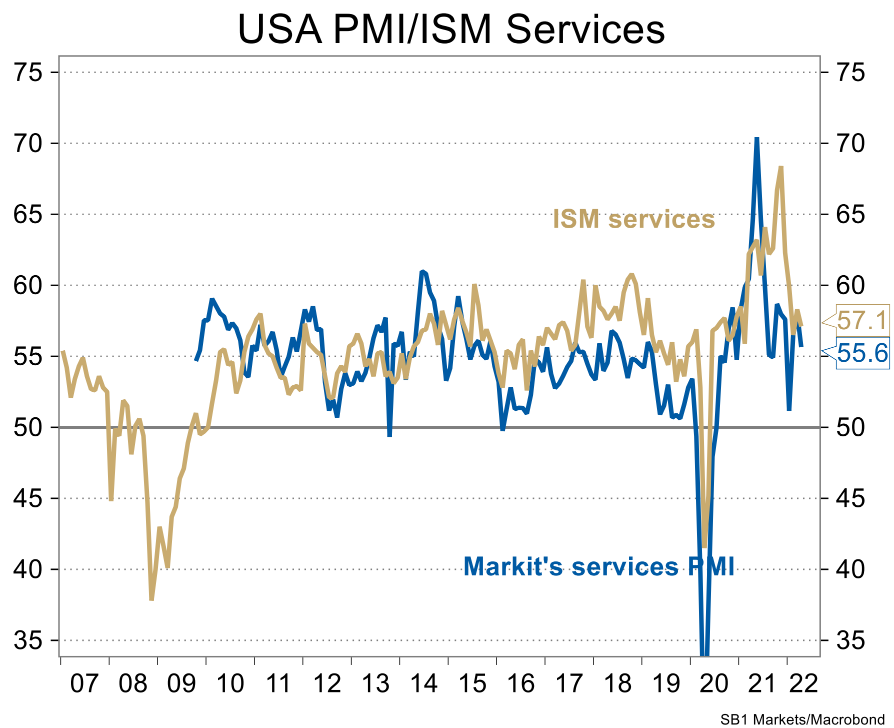
- Actual manufacturing production is on the recovery track and it is finally above the pre-pandemic level
- We expect a continued growth the coming months, but at a slower pace
  - » Investments will probably climb further while goods consumption in the US will have to normalise at a lower level than the current

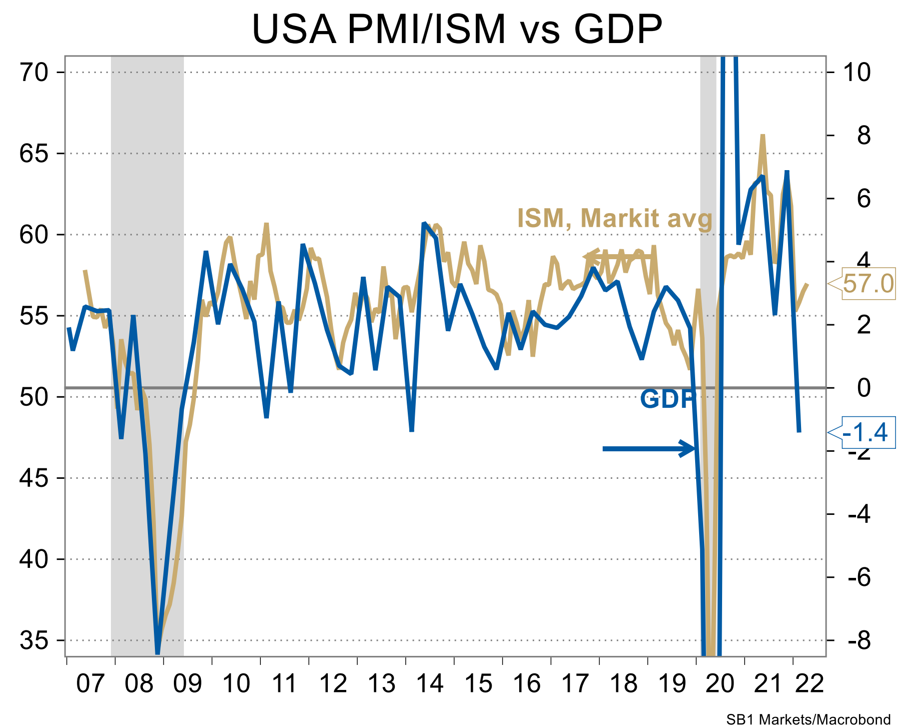




Services ISM down but still at a high level at 57.1

Markit's services PMI confirmed down. The grand PMI/ISM total at 57.0, signals growth above trend





- **The ISM services index** lost 1.2 p to 57.1 in April, expected up 0.2 p. The level is well below the re-opening spikes but above average, signalling growth above trend
- The price index rose marginally to 84.6, an ATH – like the other price indices in the PMI/ISM data set, check next page
- Together with their manufacturing indices, the **PMI/ISMs** signal a 3% GDP growth rate

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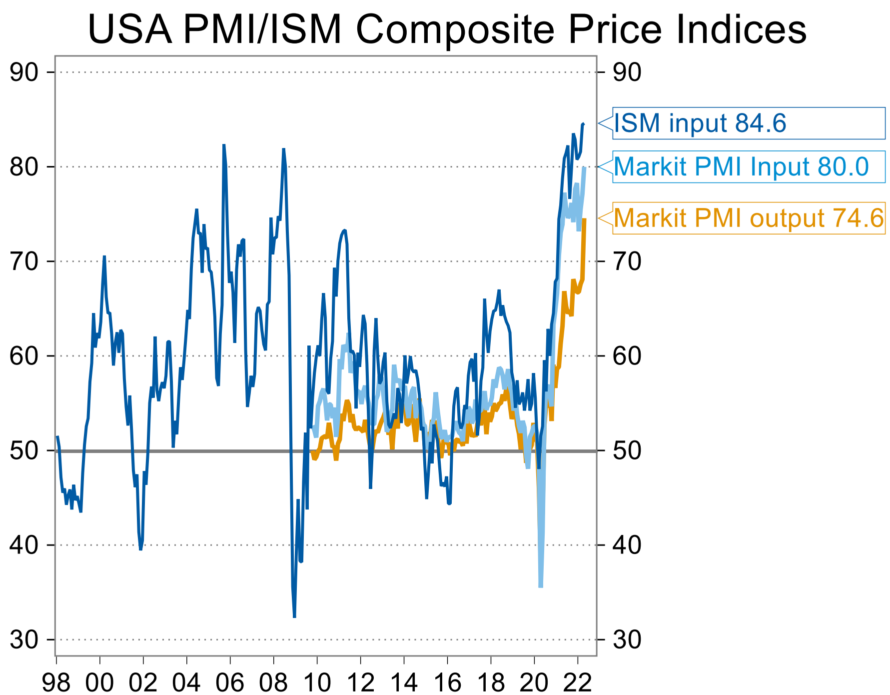
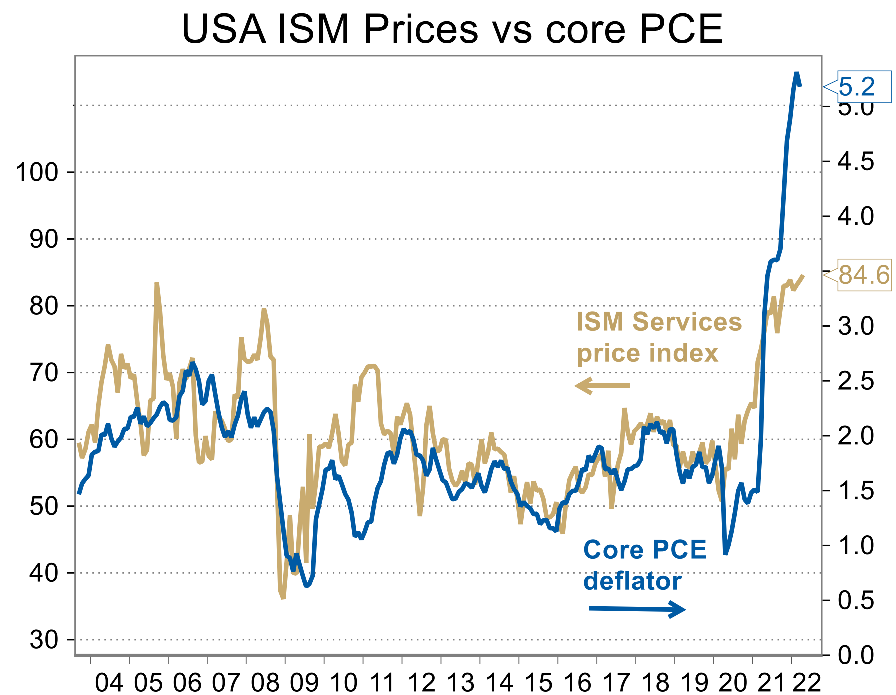
ISM input prices reported faster up than ever before

… but actual inflation (at least the core) has accelerated more than the PMI/ISMs have signalled



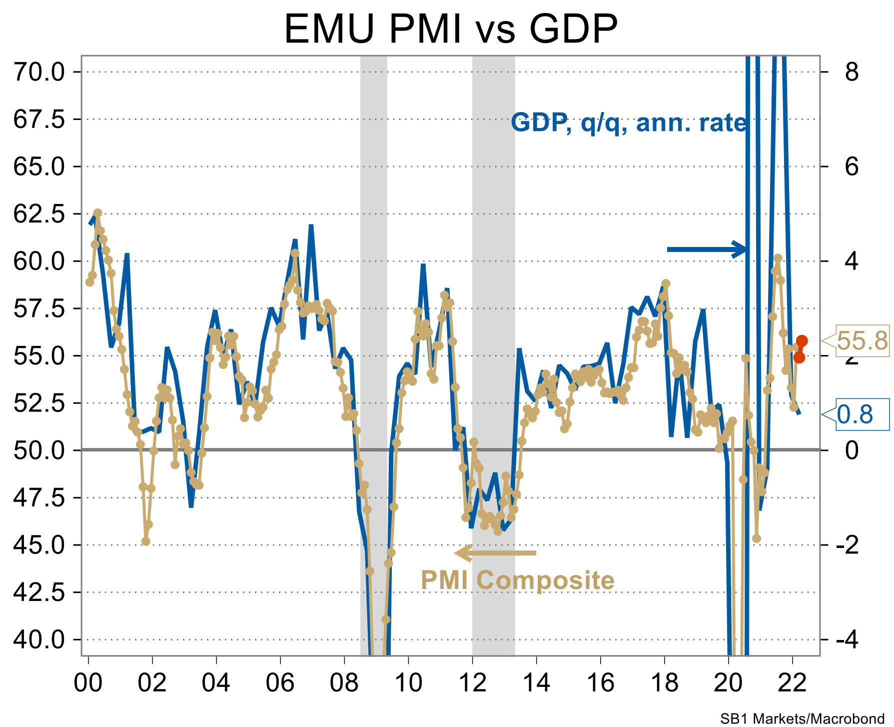
SB1 Markets/Macrobond

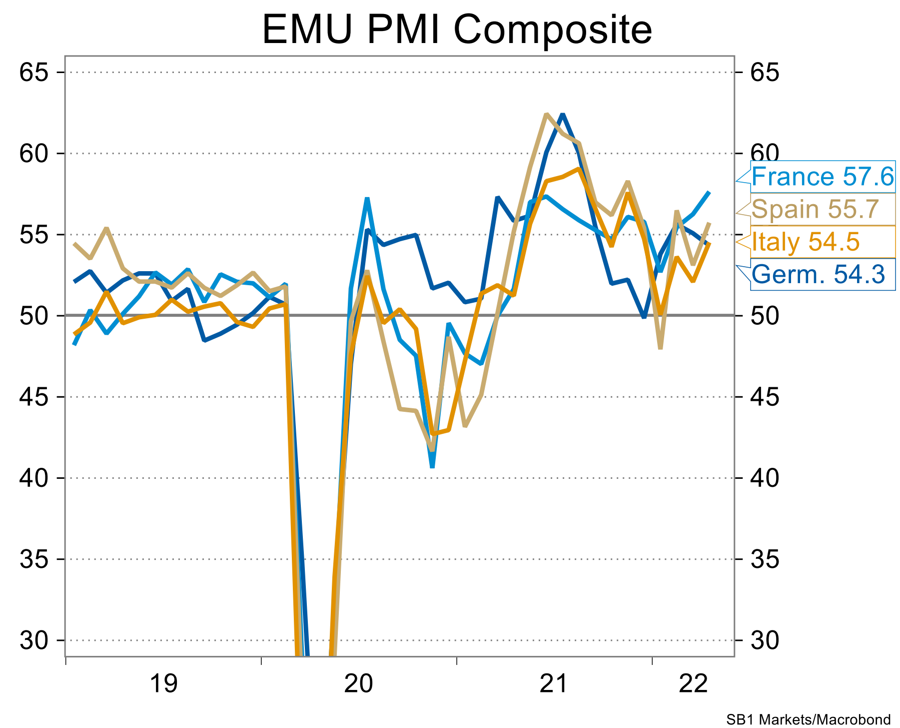


SB1 Markets/Macrobond

PMI stronger in April thanks to solid growth in services

The composite PMI up 0.9 to 55.8, in line with the preliminary estimate

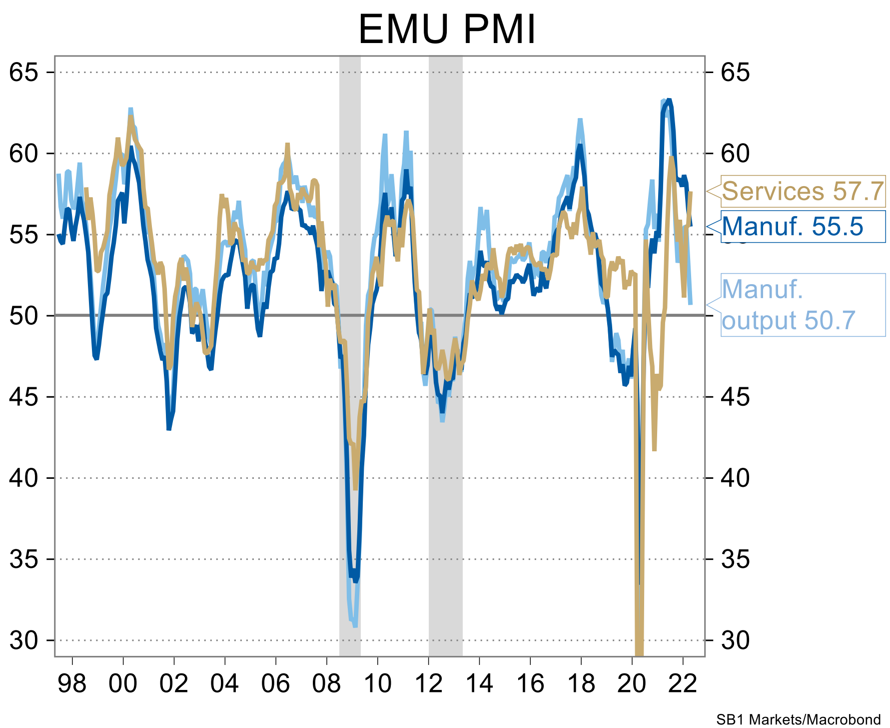


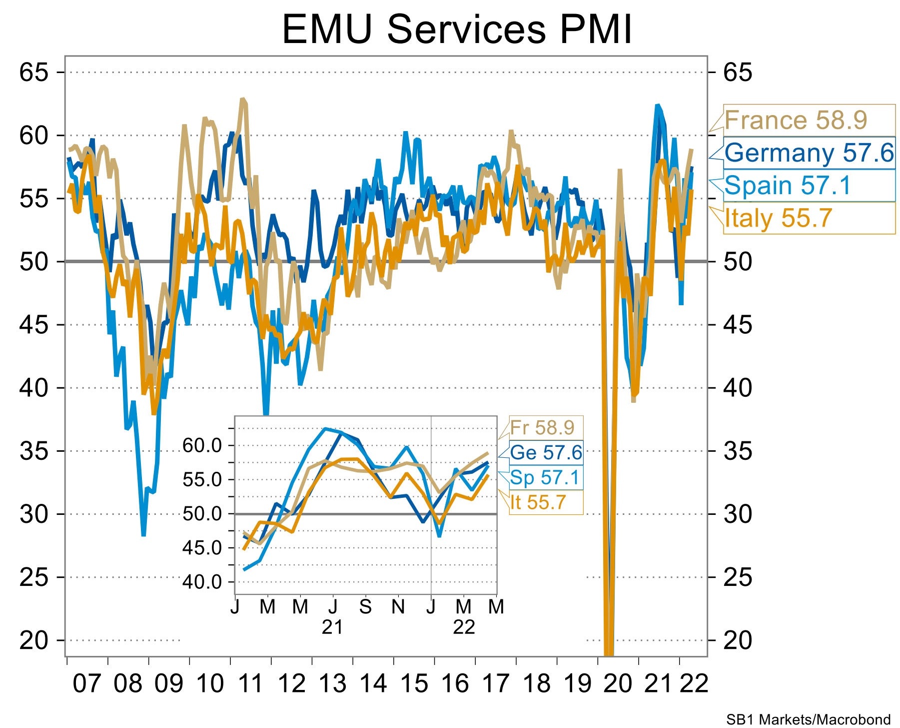


- While growth in manufacturing stalled in April, the service sector showed stronger growth as remaining restrictions were eased further
  - » However, the war in Ukraine and ever increasing purchasing prices give causes for concern in the manufacturing sector
  - » Could it also be that the pent up demand in the service sector has reached the top?
- The final **composite PMI** at 55.8 signals growth at 2.3%, well above trend
- The German PMI fell, while the other big 3 reported an increase

Manufacturing report slower growth, services still very upbeat

Manufacturing sector still expanding, but affected by supply-chain disruptions

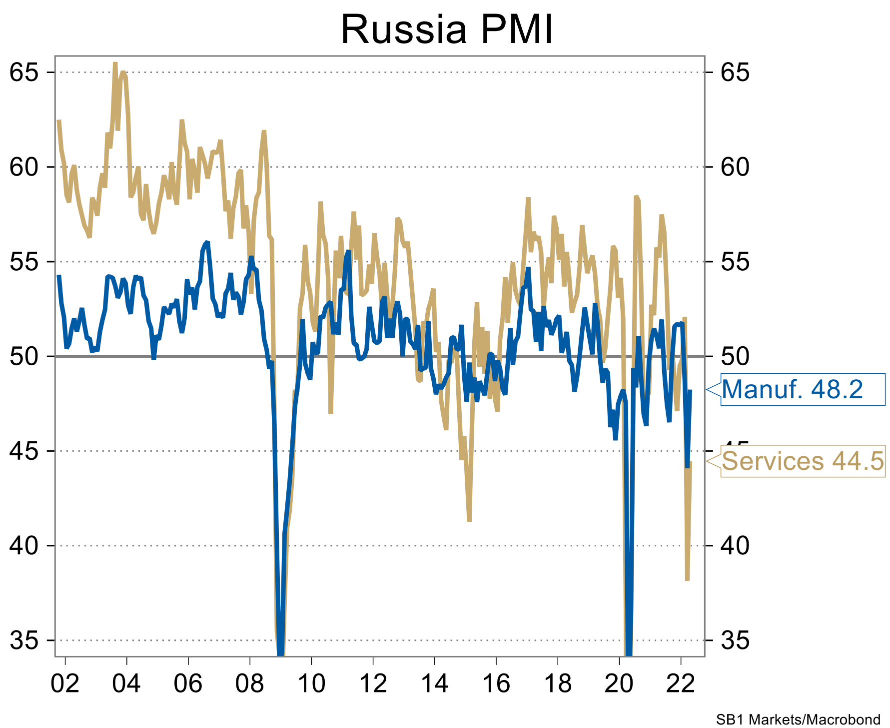


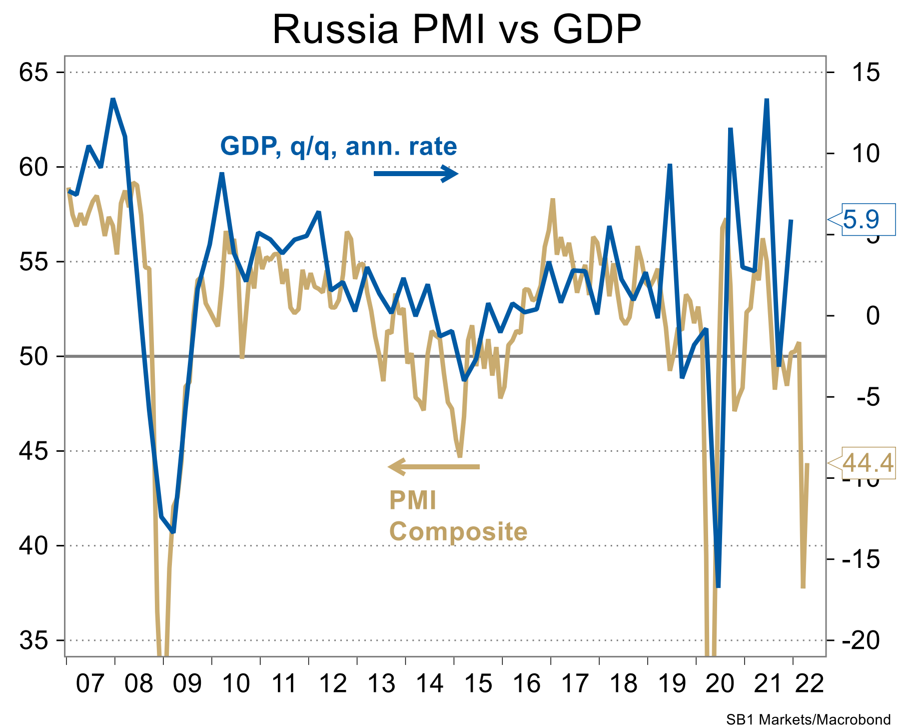


- The EMU **manufacturing PMI** fell to 55.5 in April from 55.3, and while 0.2 p above the initial estimate, the print is the lowest since January last year. The war in Ukraine, supply-side challenges, rising input prices, and another round of lockdowns in China weigh on sentiment
- The **services PMI** came in at 57.7, in line with the flash estimate and up 2.1 p from March as Covid restrictions were further eased across the EMU

A continued but slower decline in both manufacturing and services

The composite PMI recovered 6.6 p to 44.4, still signalling a huge decline in GDP (almost 10%)

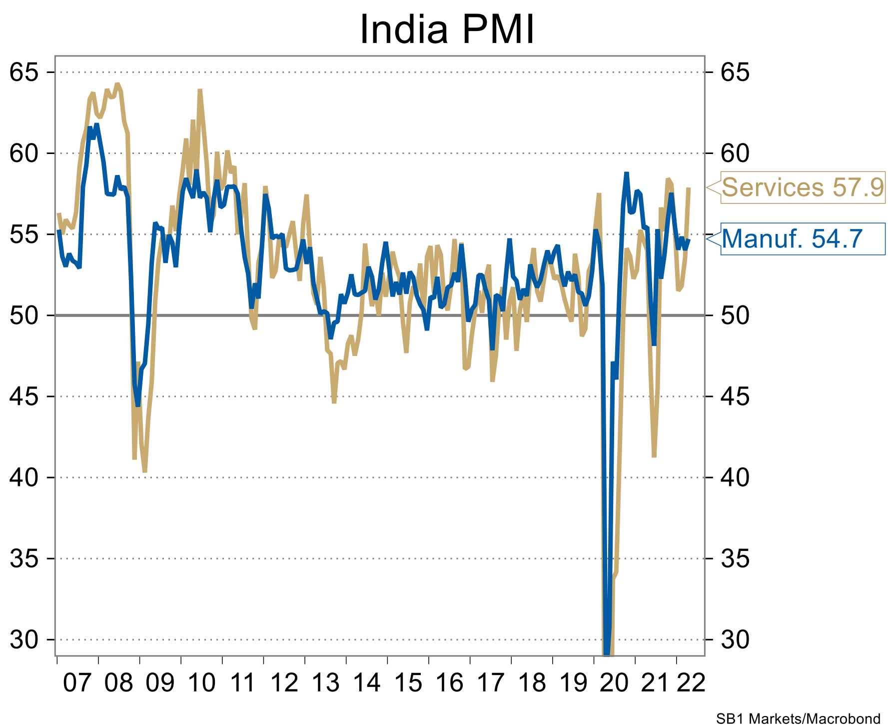


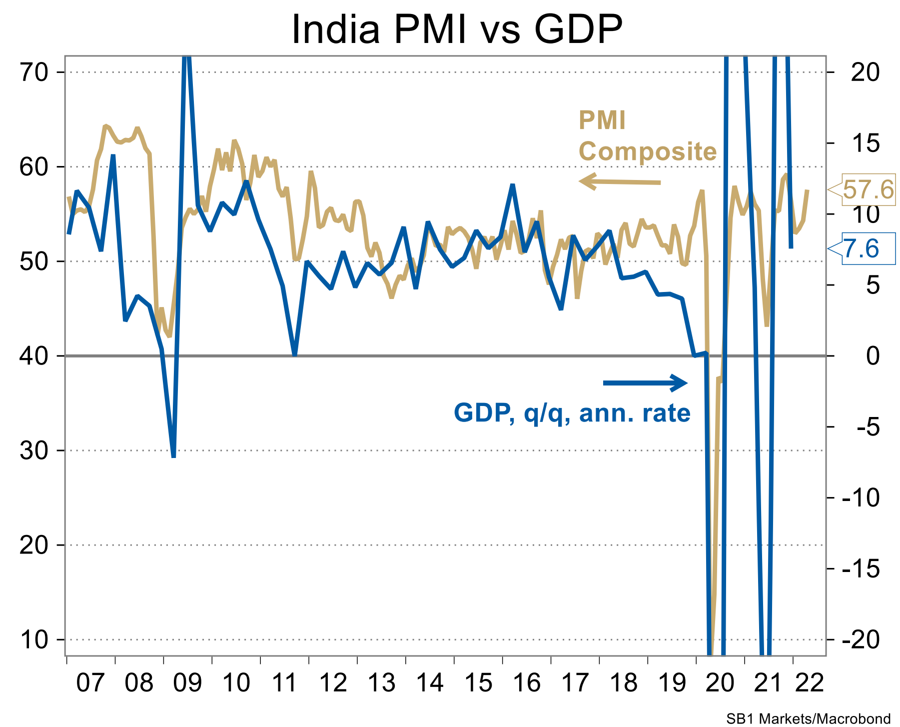


- **The service sector PMI** fell 6.3 p to 44.5
- **The output component in the manufacturing index** fell sharply too (a part of the composite index), while the total index just fell 4.5 p to 44.1
- There is of course just one possible explanation for this abrupt contraction in activity in April: The special operation in Ukraine and Western sanctions
- **A reminder:** The PMIs are not sentiment surveys – respondents are asked about in changes in actual activity (new orders, output, employment, inventories) from the previous month

The PMIs up in April, especially in the service sector. Strong growth ahead?

The composite PMI gained 3.3 p to 57.6, one of the best prints on record in the past 10 years

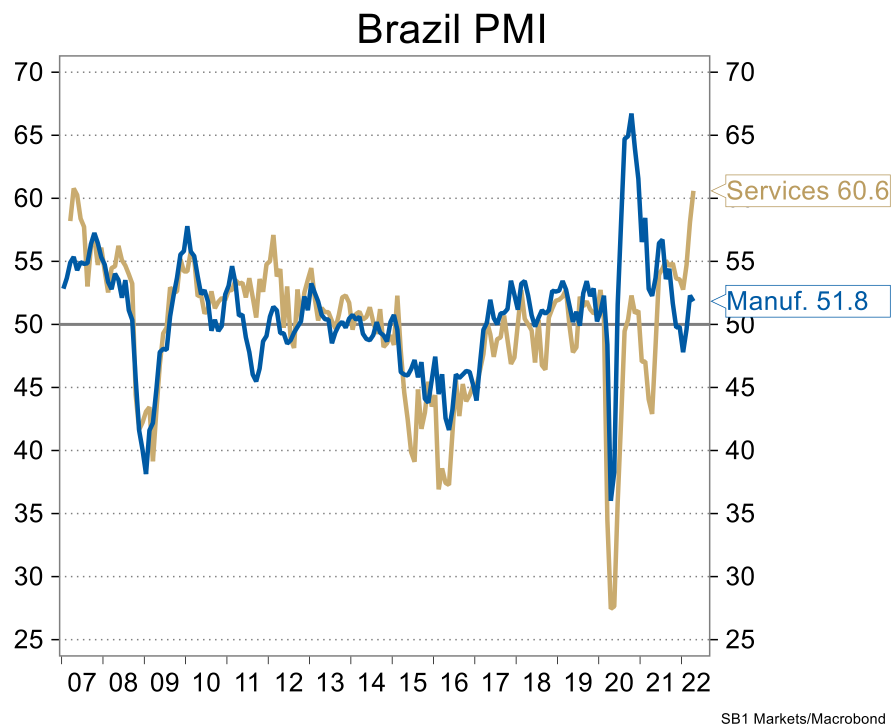


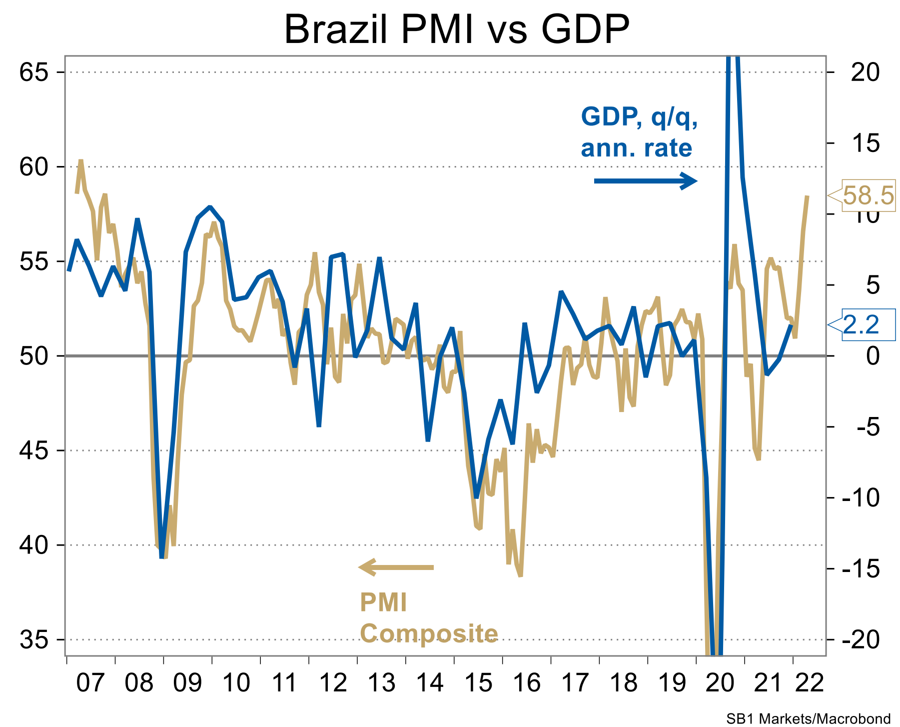


- **In Q4, Indian GDP** grew at 7.6% pace, and the PMI signals growth at least at this level
  - However, the correlation between the PMIs and GDP is rather weak – and due to the pandemic, growth rates have been all over the place the past 2 years

The service sector PMI further up – and the composite to the best level since '07

The composite index gained 1.9 p in April, following the 5.7p lift in Feb/March. No more pandemic!

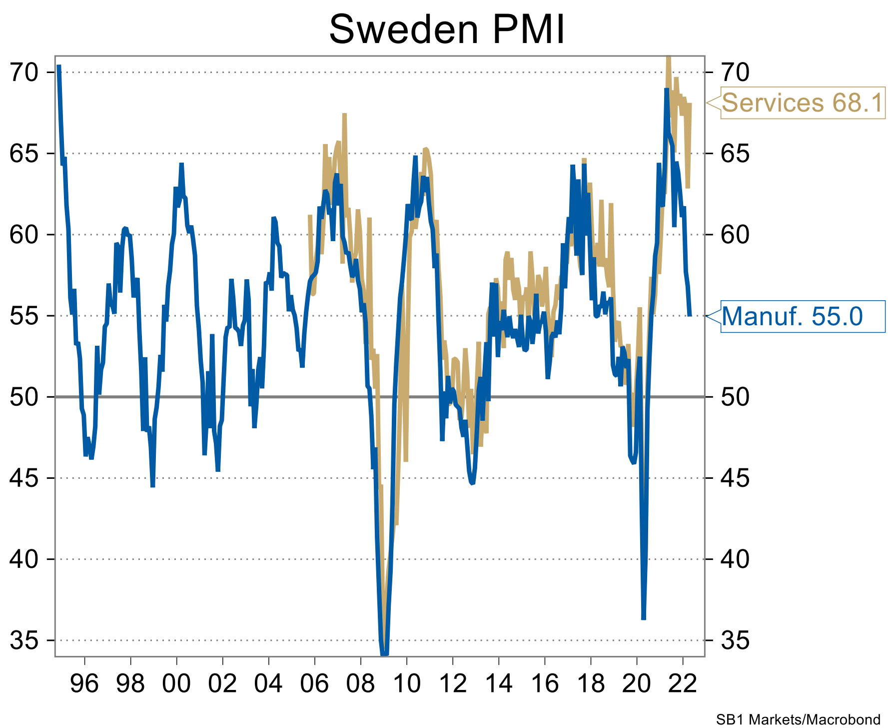


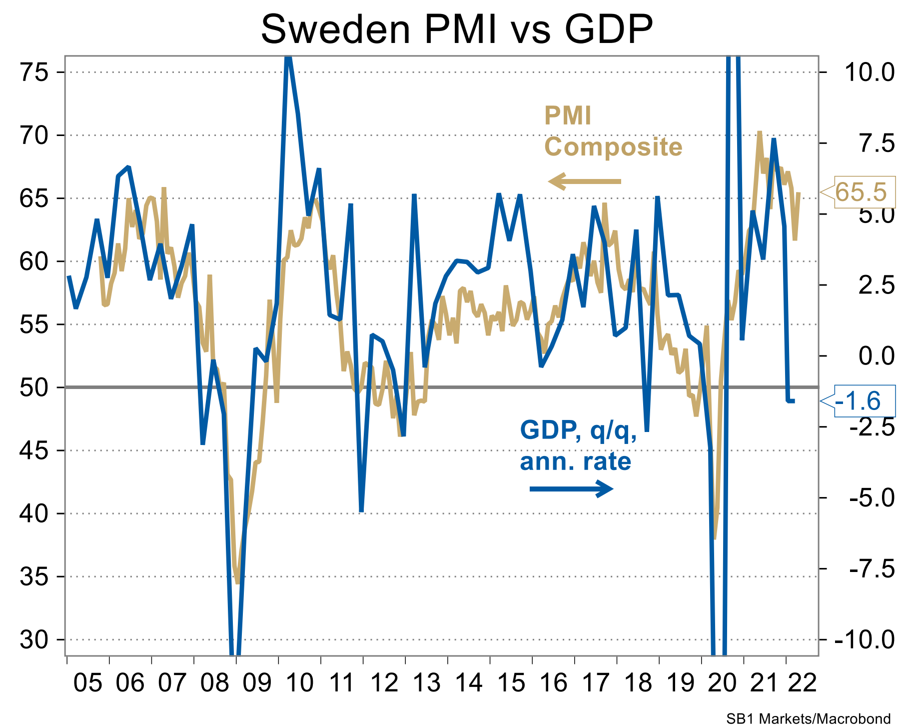


- GDP growth has been weak the previous 3 quarters as the country has experienced serious covid challenges. A brisk recovery is now under way

Services full speed ahead again in April, manufacturing reports slower growth

Both manufacturing and services reported faster – and very fast – growth!

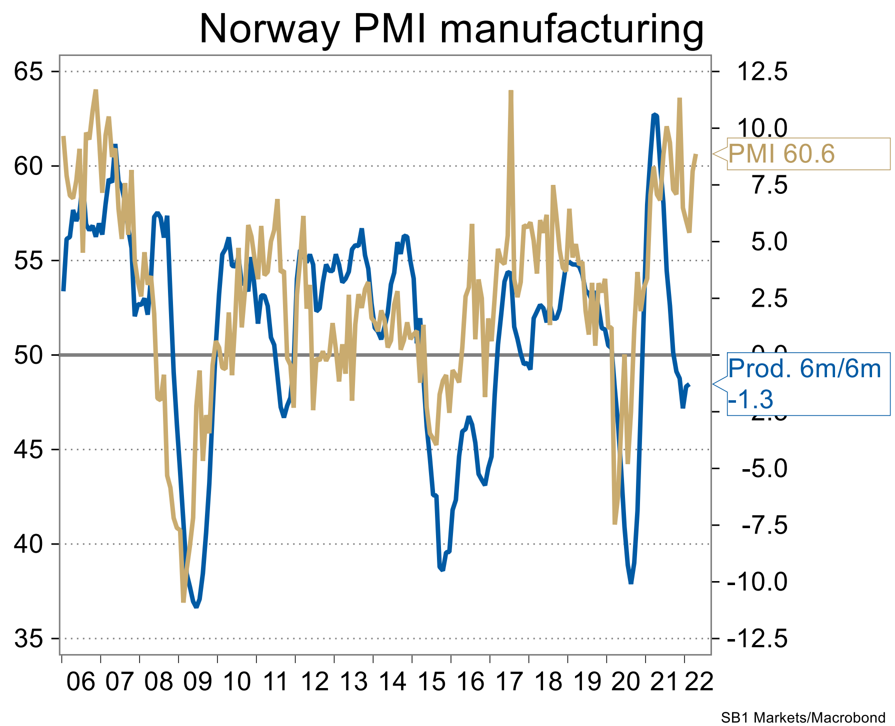


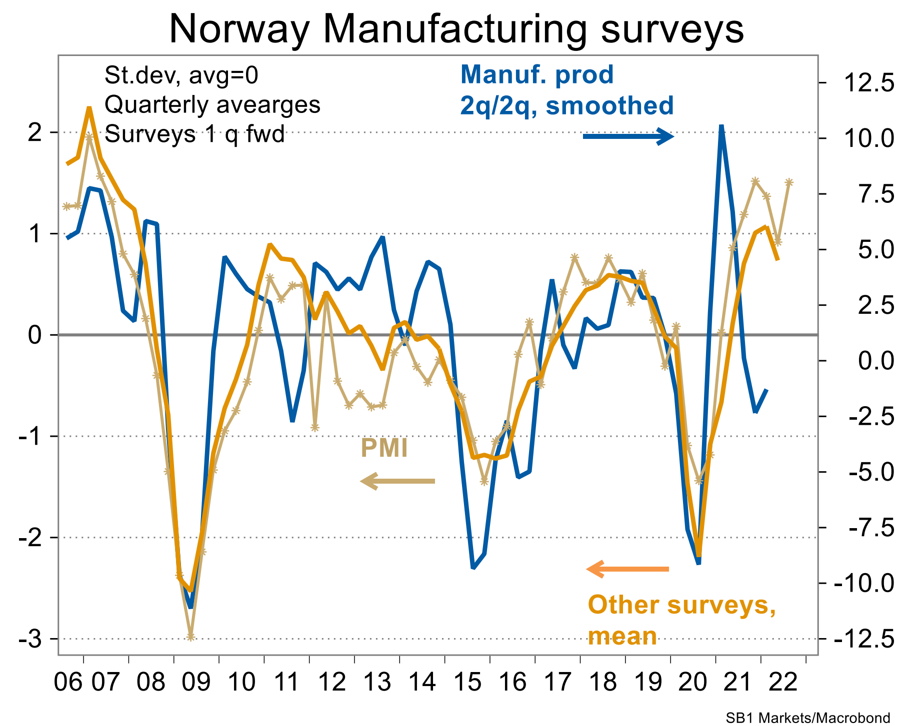


- In Q1, **GDP** fell at a 1.6% pace, due to the Omicron slowdown in some services (which BTW was not captured by the service sector PMI)
- Two weeks ago the **Riksbank** yielded and lifted the signal rate by 25 bps to 0.25%, signalled further hikes and lifted the interest rate path by almost 150 bps at the most. Market rates are 100 bps above the bank's new path!

The manufacturing PMI up 0.9 p to 60.6 in April, better than we expected (again)

The uptick was 'for real', both new orders & production up. Input prices are climbing rapidly, of course





- The **manufacturing PMI index** climbed for the 2nd month in a row – to a very high level
- Other **manufacturing surveys** are mixed, but SSB's quarterly survey was also strong in Q1
- Even if surveys have been reporting growth, **actual production** has fallen slightly since last April

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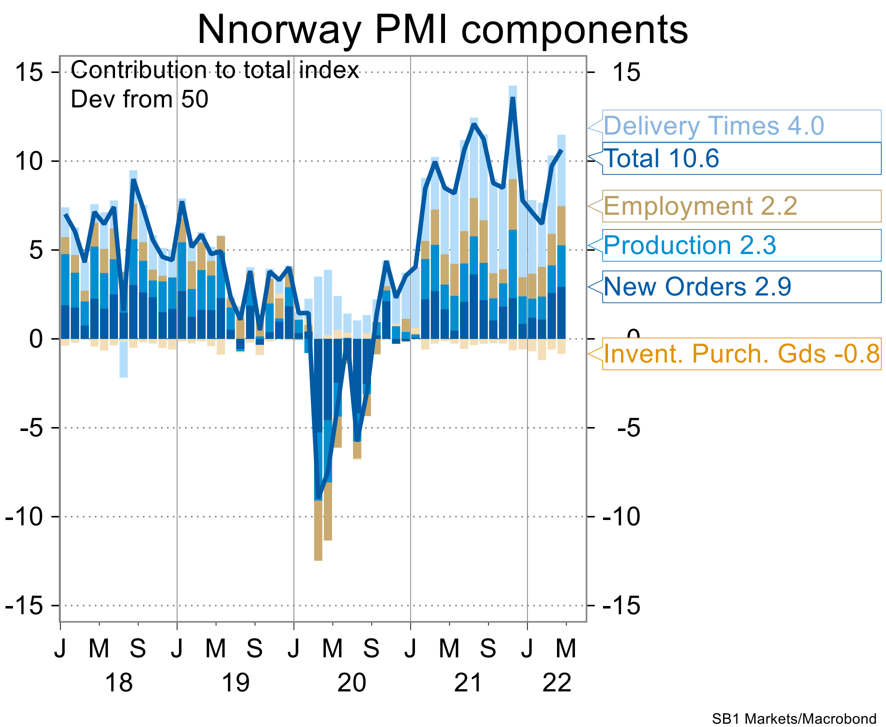
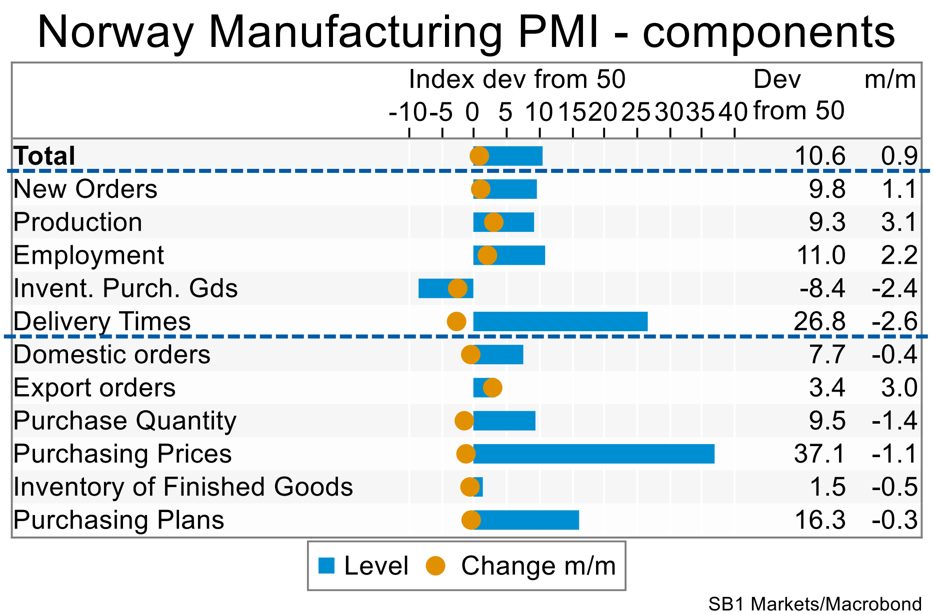
The delivery times index still lifts the headline PMI ‘artificially’, but less so in April

The delivery index lifts the PMI by 4 p – but other components rose in April, especially production





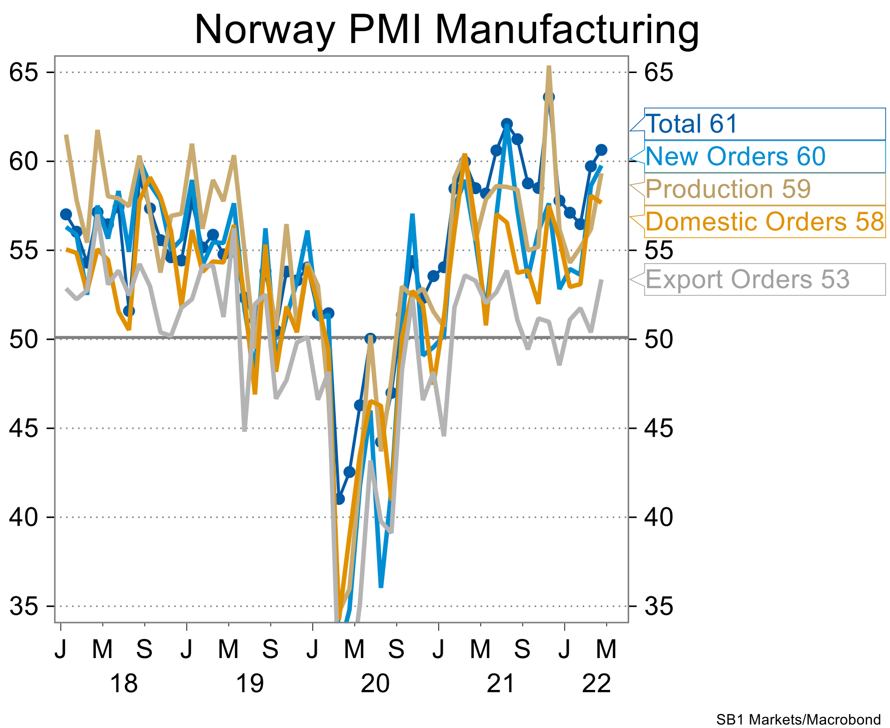
The total index is a weighted average of the first 5 sub-indices

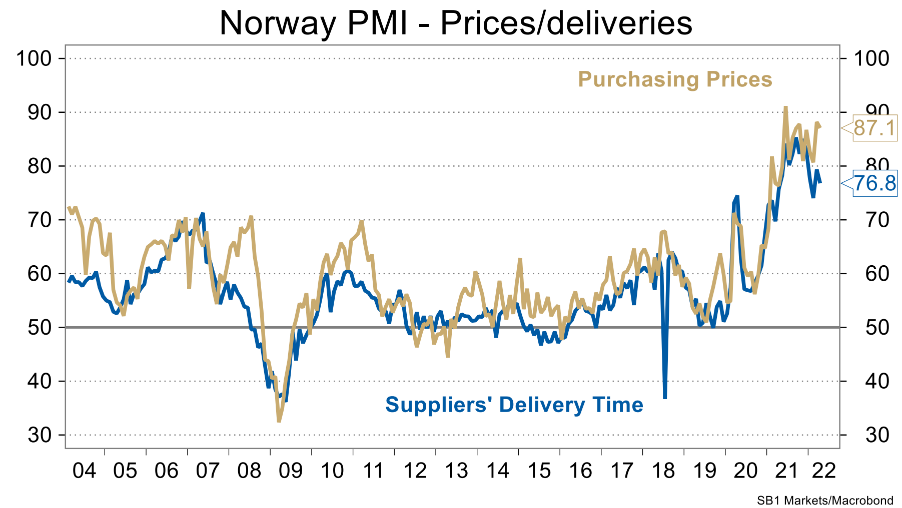
- Normally, the **delivery times index** has not had any significant impact on the total PMI index as the delivery times index has been quite closely correlated other components in the headline index. Now, it makes a substantial difference, by 4 pp to the total index
- **Prices** are still rising at a fast pace, albeit slower than in January when the index shot up 7.5 p to 88.1!

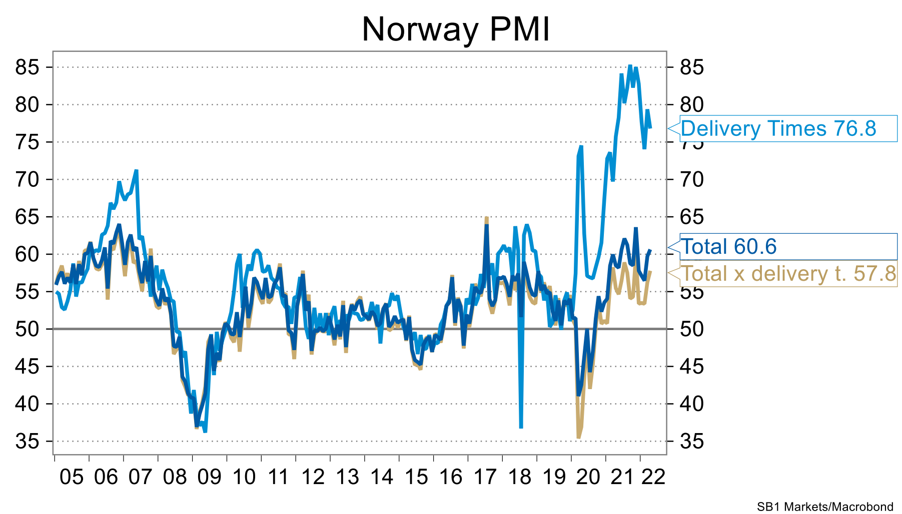
The total PMI index is a weighted index of new orders, production, employment, inventory of purchased goods, and delivery time. The 6 next sub indices at the table to the right are not included in the total index calculus

April a strong month, broad based

A total index ex. delivery times rose 2.8 p to 56.0, as orders and production indices climbed sharply



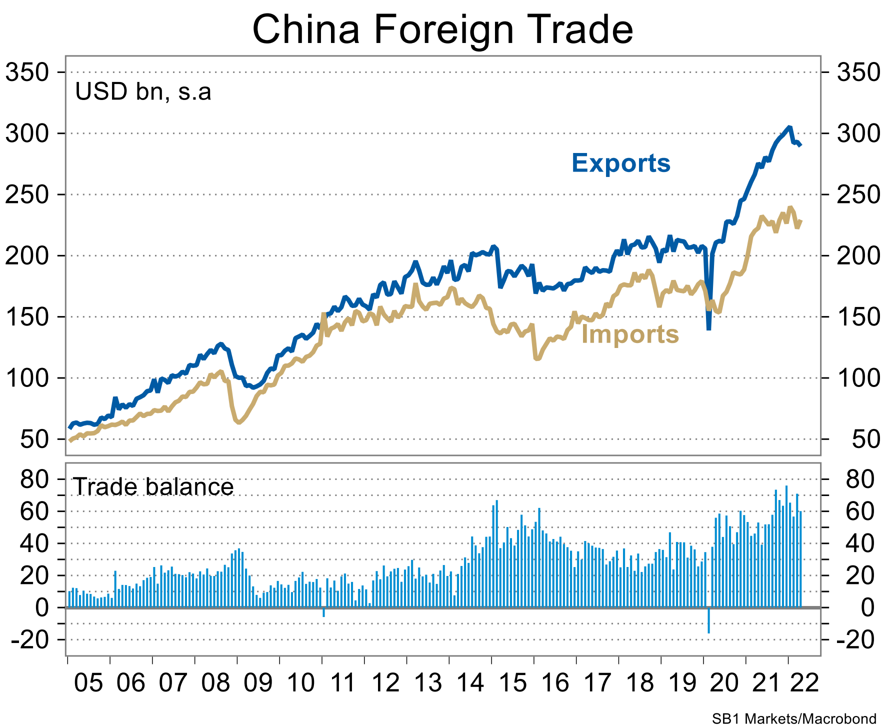




- **Prices** are still rising at a very fast pace

Exports down in April, but just by 1%, imports up 3%, both better than expected

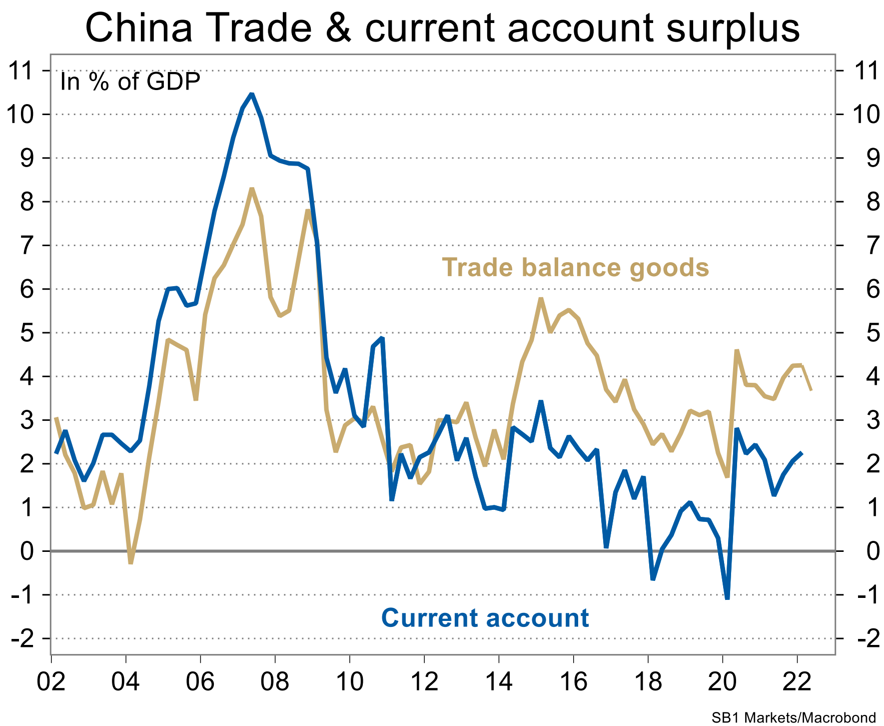
Still, both export & import volumes are down 7% from January, and just exports above the p-p trend

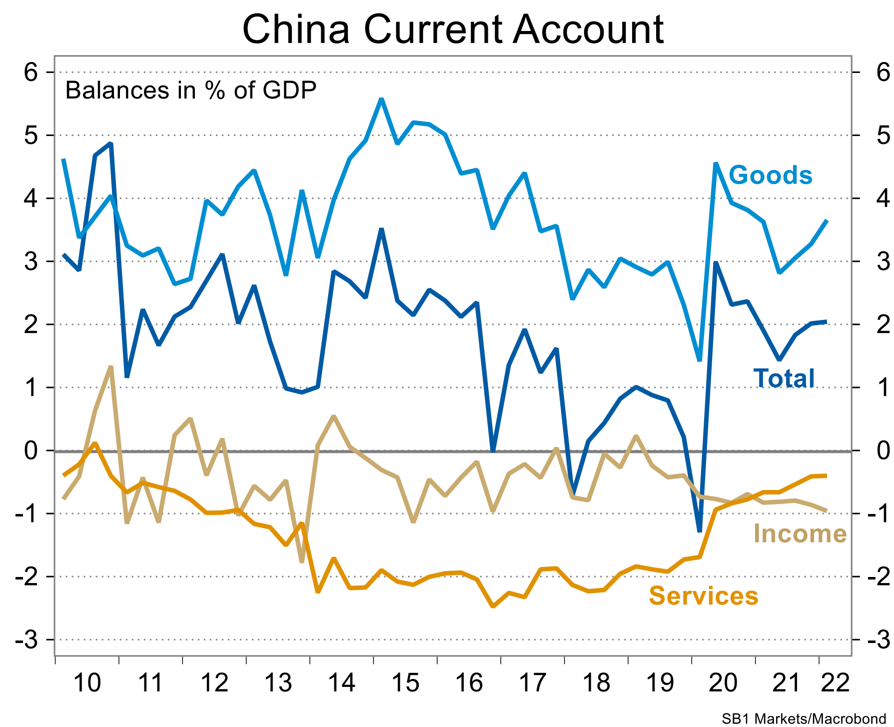


- **Exports fell by** grew by 1% in USD terms in April (our seas adj), and are up 4% y/y, down from 15% in March, 1 pp better than expected. Export volumes probably fell slightly too, adding to the decline in Jan, Feb & Mar. Export volumes are down 7%, are down 6% y/y – still up 13% from before the pandemic, and 4% above the pre-pandemic trend path
- **Import** values gained 3% m/m in April, and are flat y/y, like in March, 3 pp better than expected. Import volumes very likely rose too, we assume a smell price decline in April. Volumes are down 7% from January, and by 10% y/y, and are some 4% below the pre-pandemic trend. XXX Oil imports have flattened, coal and iron ore imports are down. In value terms, electric & electronics goods imports are still increasing rapidly
- The **trade surplus** at USD 51 bn was as expected and down USD 10 bn to USD 60 bn seas. adj.
- Lockdowns have hurt foreign trade but so far not dramatically. Underlying slower growth in domestic demand recent quarters probably explain the decline in imports until the recent 'lockdown' drop

The trade surplus has stabilised at 4% of GDP, the current account at some 2%

... up from 3% and 1% resp. before the pandemic

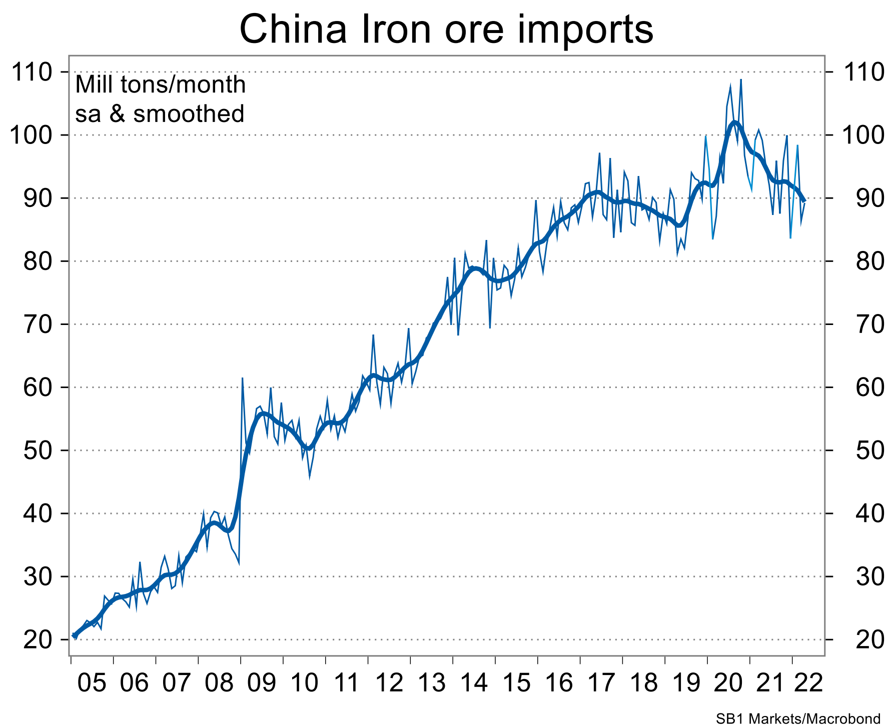


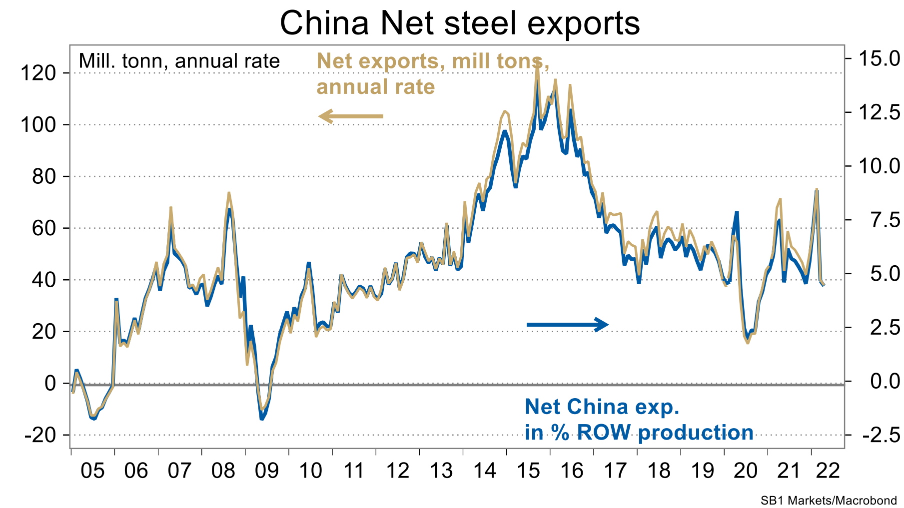


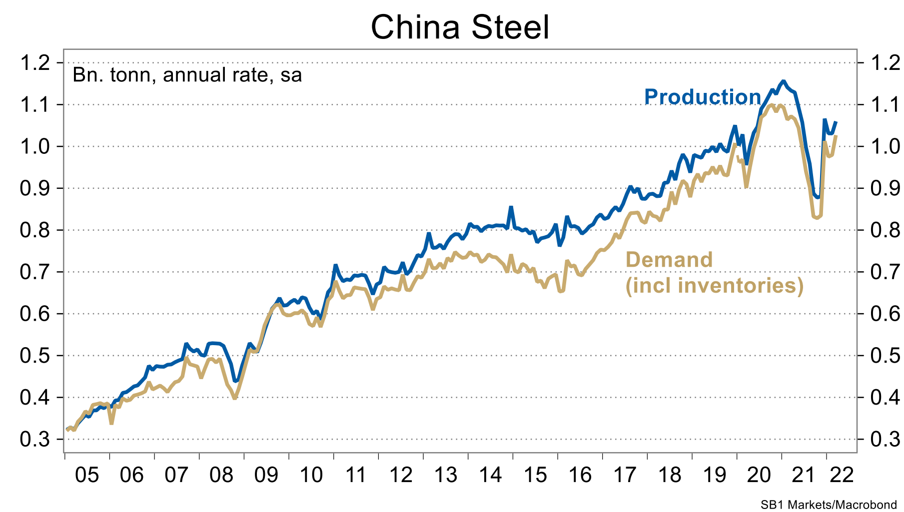
- In services, China runs a deficit, but not that large anymore, in Q4 less than -0.5% of GDP, from -2% before the pandemic
- China runs a deficit in net (mostly capital) income from abroad, even if the country has a huge net positive financial position
  - » China has invested much in low yielding US government bonds (and other low yielding investments); foreigners have been investing in profitable production capacity in China. US investments should soon yield larger returns

Iron ore imports are still trending down, -10% since late 2020

Steel production has stabilised, although almost 10% below the peak in early 2021



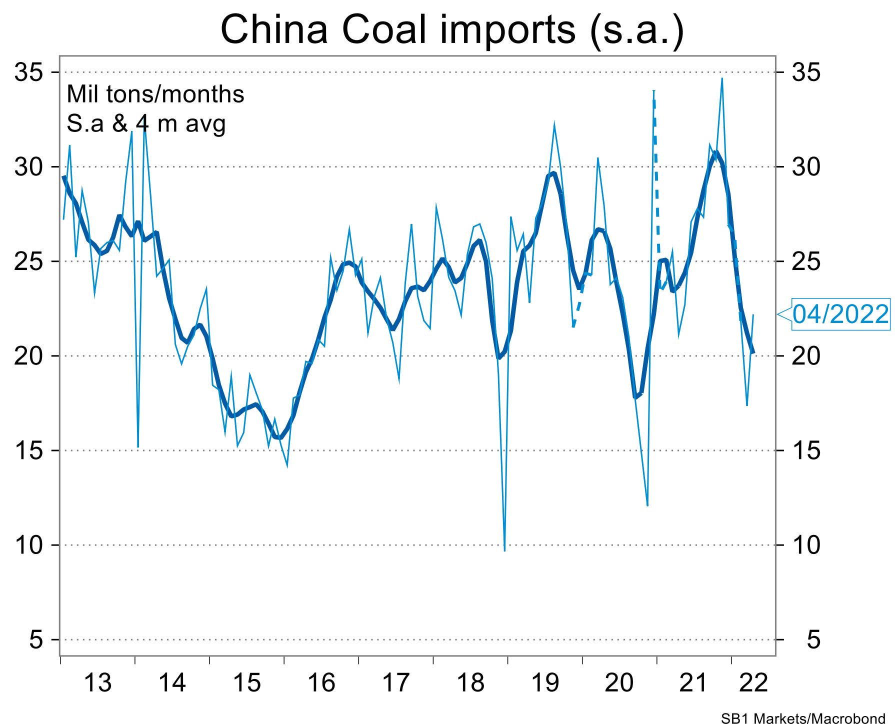


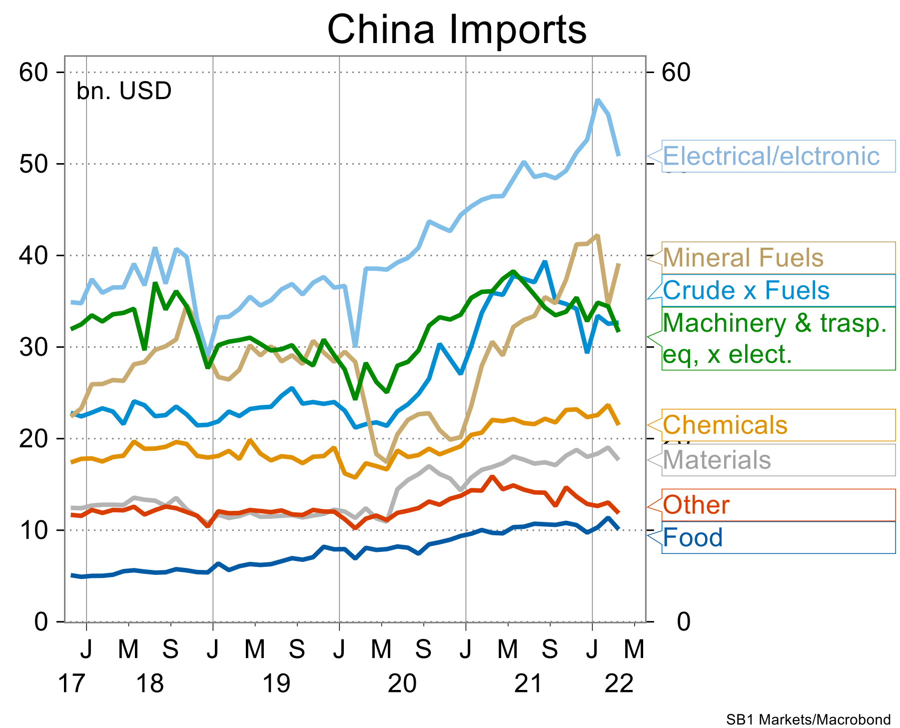


- **Production and domestic demand** (incl. inventories) fell sharply in Q2-Q3 last year – by 25% – due to public regulations and probably the setback in the construction sector
- Activity recovered sharply in December – and was stable through Q1

Coal imports up in April but are still below a 'normal' level

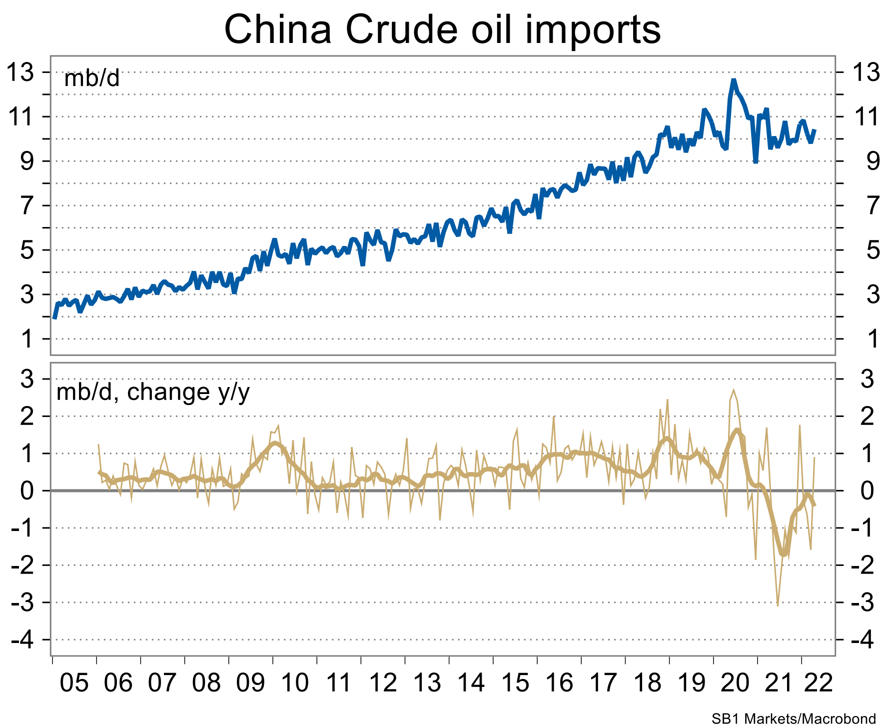
Imports of most goods fell m/m in March

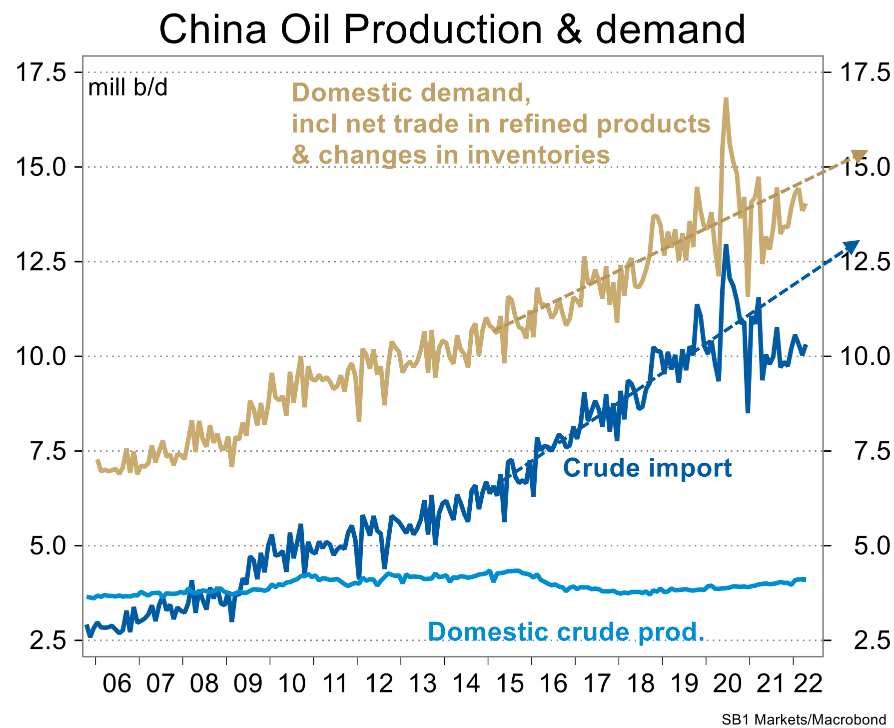




Oil imports have flattened

Domestic demand has more or less flattened too (but domestic production is slowly increasing)

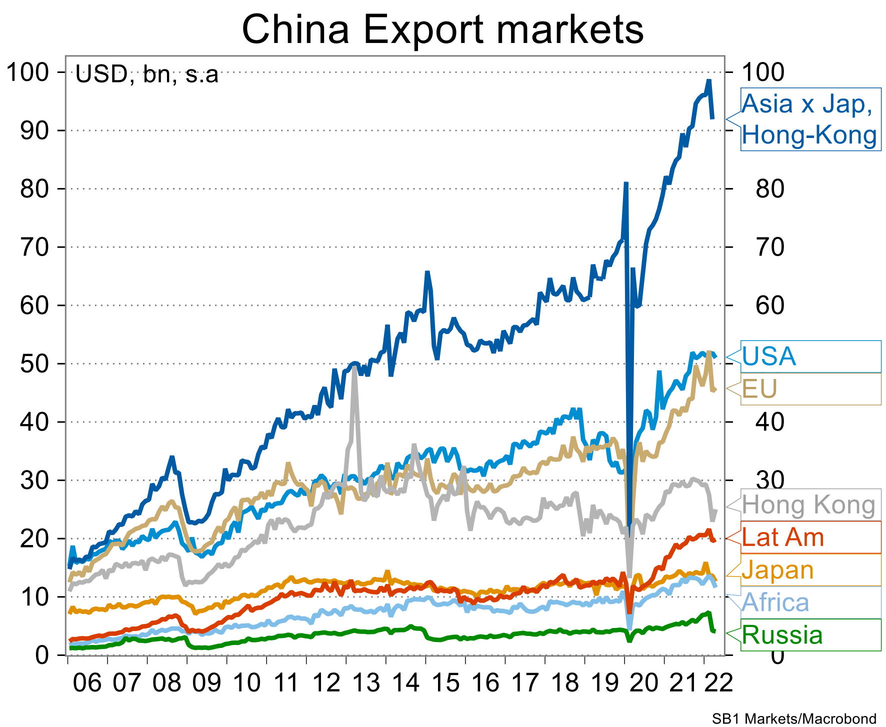




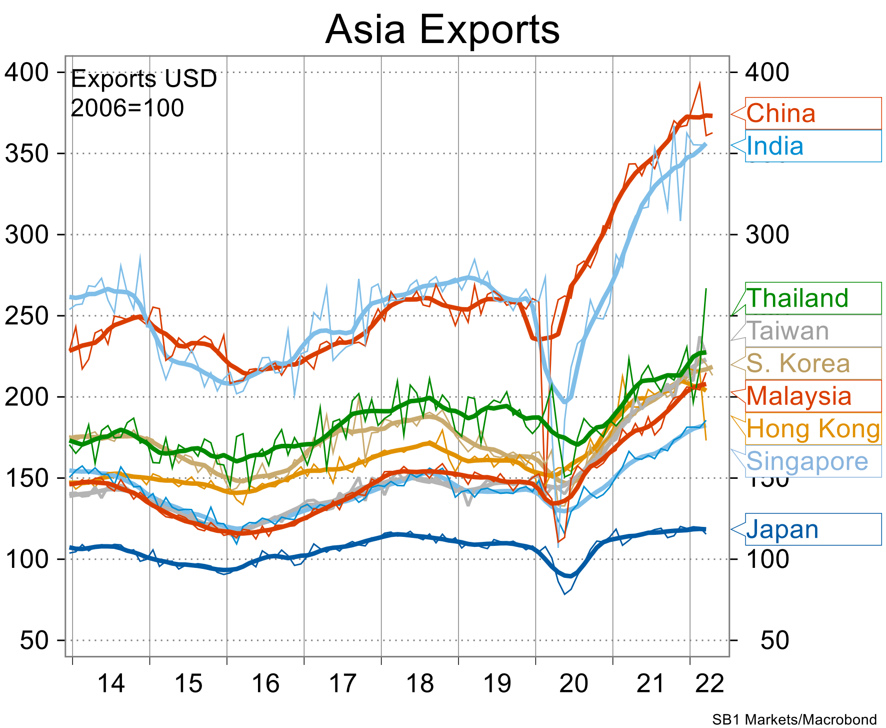
- 4 years without growth in oil import or domestic demand is rather surprising?
- Some inventory/reserve building/drawdowns may explain short term deviations but not the stabilisation since 2018

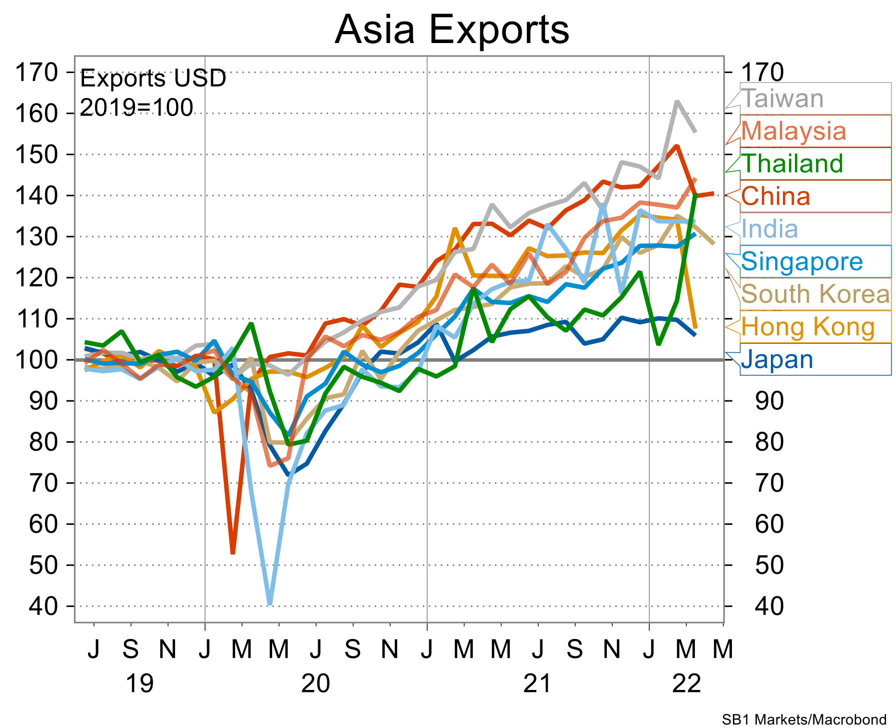
Chinese exports to Russia remained at very low level in April

The decline in exports so far in 2022 has been broad, except exports to the US



Exports from other Asian counties are in sum slowing – at high levels





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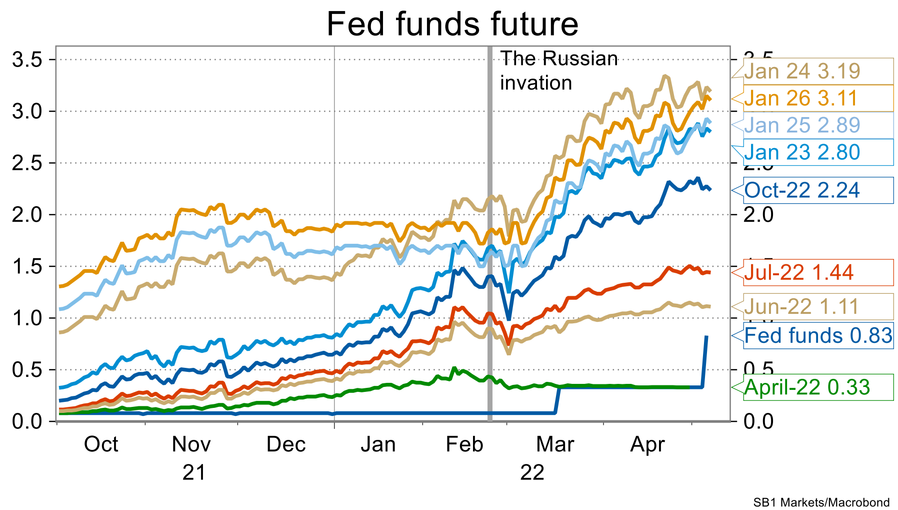
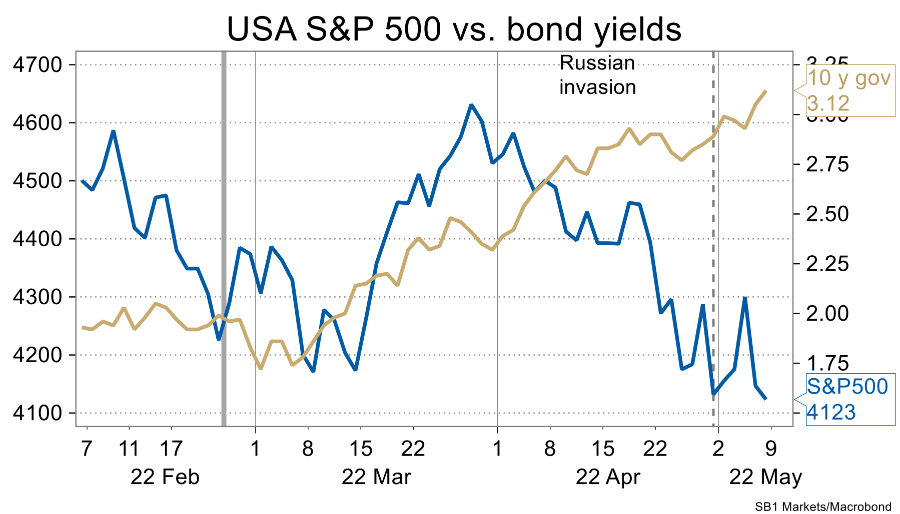
What did the governor say? (A confused) Powell confused the (confused) markets

Some ups and downs in the markets last week but stocks were close to unch, the 10 y +23 bps, 3.12%

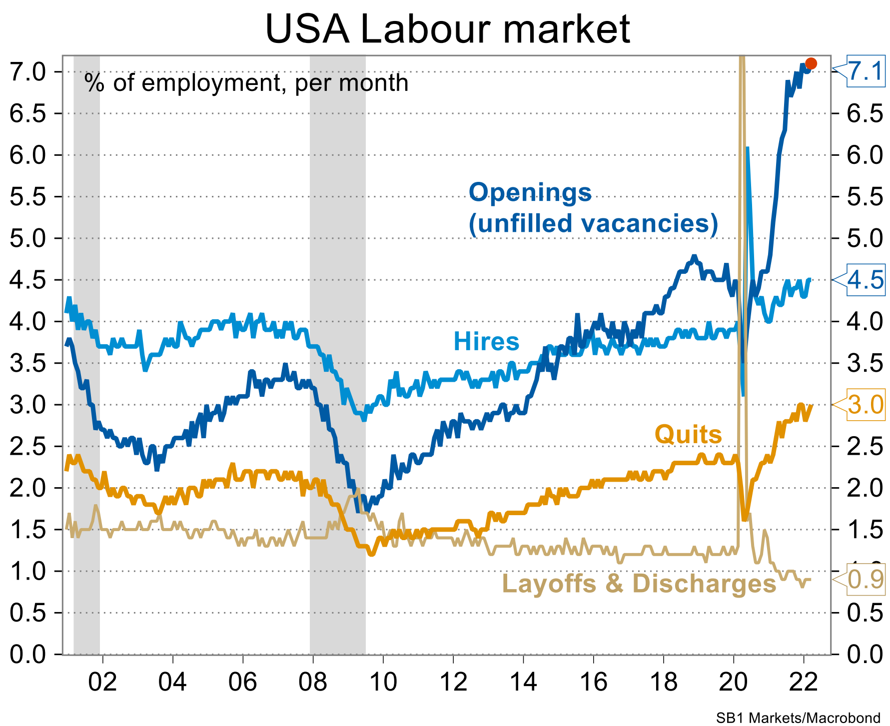




- **The press release** from the FOMC meeting on Wednesday did not change much: The signal rate was lifted by 50 bps as was widely expected and discounted in the market. The initiation of the QT process had been well communicated as well. The stock market was flat and bond yields rose marginally
- ... That is, until Powell started to talk at the press conference
- The FOMC had not 'actively discussed' a 75 bps hikes at this meeting or that 75 bps could be needed at the upcoming meetings. A 50 bps hike in June and July was signalled
- Then Powell said there is a path by which the unprecedented high level of vacancies could be brought substantially down without unemployment going up materially. Then wage and price inflation would come down, without the economy falling into a recession. There is a good chance of a soft or softish landing, he said.
- We assume there are some other 'not unlikely' paths too, but the stock marked shot up (and yields declined), as Powell was dovish vs rates (no 75 bps hikes) and assumed a recession would be a avoided. At least that was the conclusion at the marketplace. On Wednesday
- Of course, the next day, investors came to the **opposite conclusion**: stock markets tanked completely and yields rose
- Still, looking back, no big drama: Stock markets are back to where they came from ahead of the meeting. The short end of the curve is marginally lower (-3 to 12 bps), as 75 bps hikes are now deemed to be less likely. But no doubt, 50+50+... (pick your number of hikes) will be sufficient to achieve whatever is needed to bring inflation down. Last week the 10 y bond yields rose by 23 bps to 3.12%, due to a 26 bp lift in the TIPS real rate to 0.26%, and a small decline in break-even inflation expectations. The bond market did not think the FOMC was dovish, in the end
- **... and neither did we**: the FOMC has NOT become über-dovish vs. inflation. Yes, their inflation path is too high but we think the bank is willing to do what's needed to bring inflation down, almost whatever cost for the real economy – as the alternative would be even worse even if the FOMC hopes and prays for soft (GDP) landing. A soft landing is possible, but far from the most likely outcome. Thus, growth expectations, earnings expectations are very exposed. Most likely stock market multiples, and credit spreas too

The vacancy rate up to a new ATH. Quits & hires at ATH too

‘Nobody’ is laid off. The labour market is still extremely tight

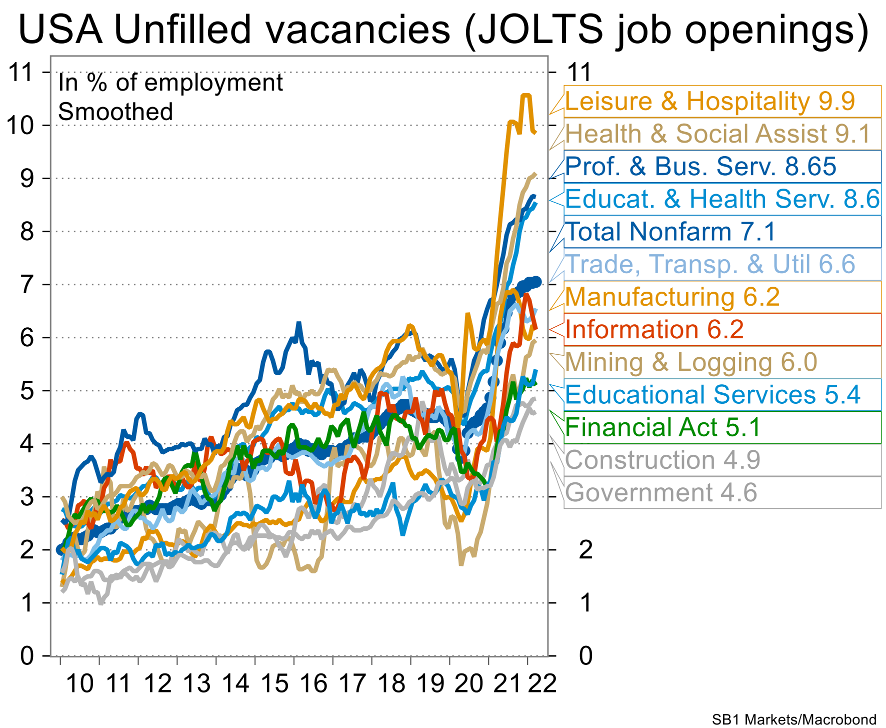


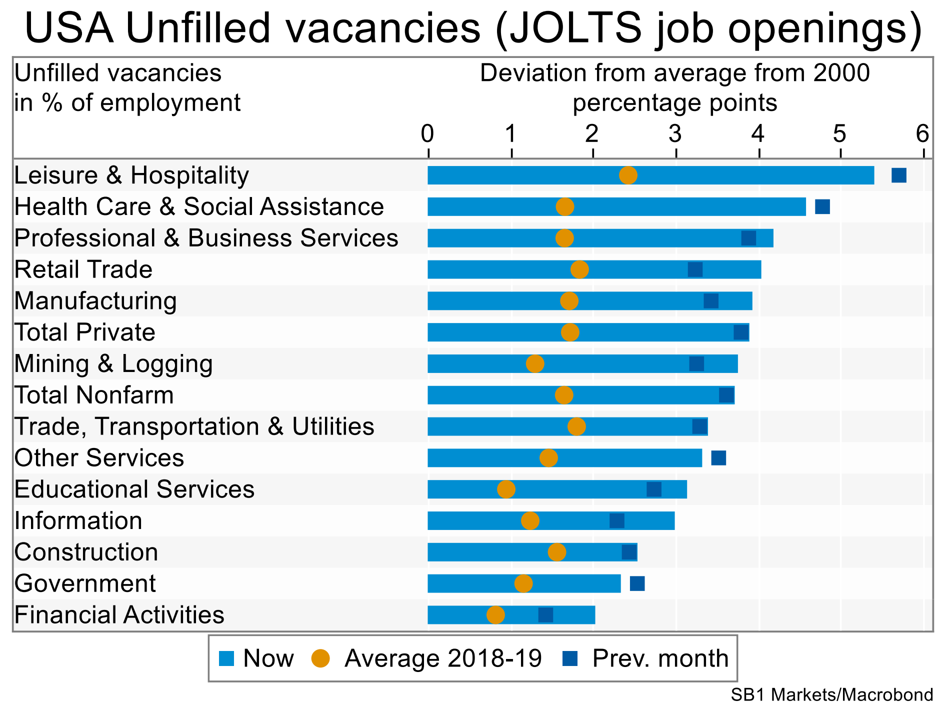
- The number of **unfilled vacancies** rose 0.2 mill to ATH at 11.6 mill in March, expected down to 11.0 mill. The rate gained 0.1 pp to 7.1%, ATH too (at the 2nd decimal)
  - » The highest print ever before the pandemic was 4.7%, and the rate was 4.5% just before the pandemic hit
  - » **The SMBs (NFIB survey)** reported an unch. – and close to record high – share of companies that were not able to fill open positions in April. These two series are very closely correlated – and both have been at levels never seen before since early last year
- **New hires** declined 0.1 mill to 6.7 mill persons from an upward level in February, equalling 4.5% of the employment level (unch., revised up by 0.2 pp), in line with previous ATHs
- The number of **voluntary quits** rose by 0.2 mill to 4.5 mill, or up 0.1 pp to 3.0% of the no. of employed, also in line with ATH late last year. As with unfilled vacancies, quits are closely correlated to wage inflation – for obvious reasons
- **Layoffs** were unchanged at 0.9%, a very low level
- **In sum:** The report data confirm an extreme tight labour market

SpareBank 1 MARKETS

All sectors are reporting more vacancies than before the pandemic

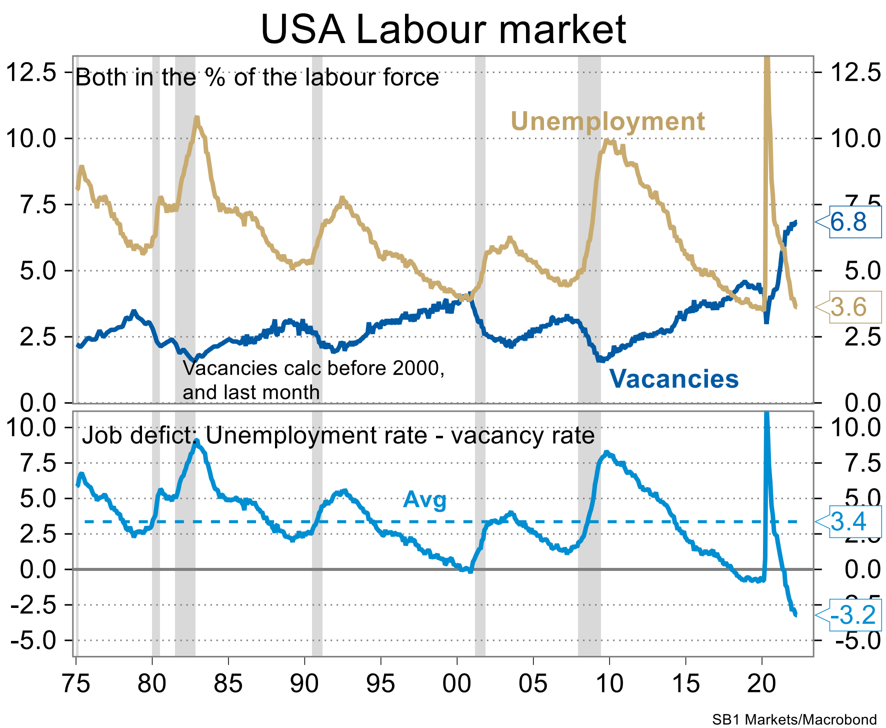
.. And most sectors are still trending upwards

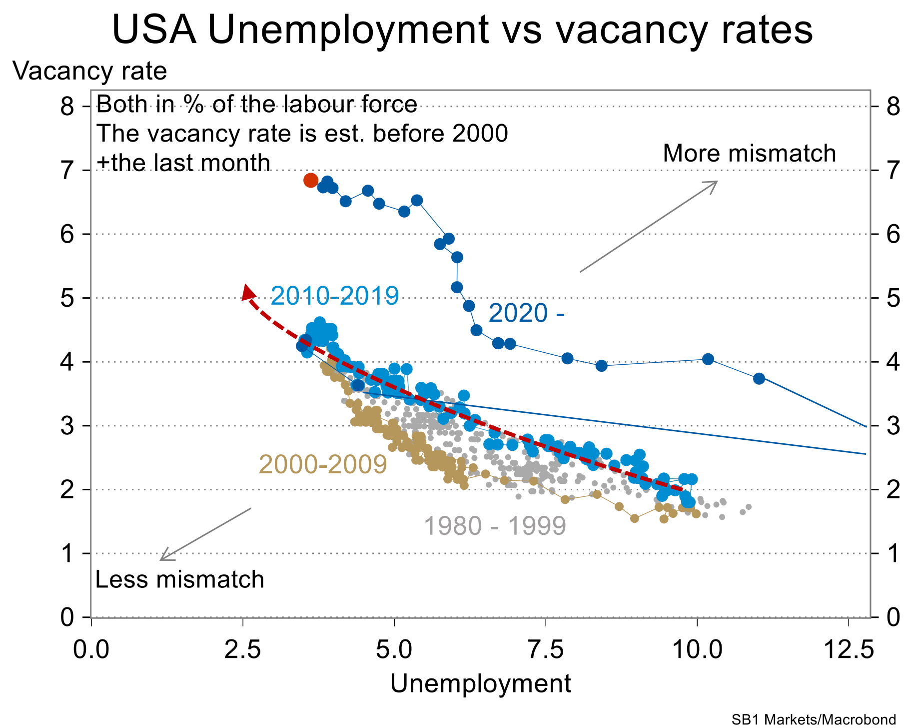




An unprecedented tight labour market – and still a large mismatch

5.8 mill were unemployed in March, and at the same time there were 11.6 mill unfilled job openings!

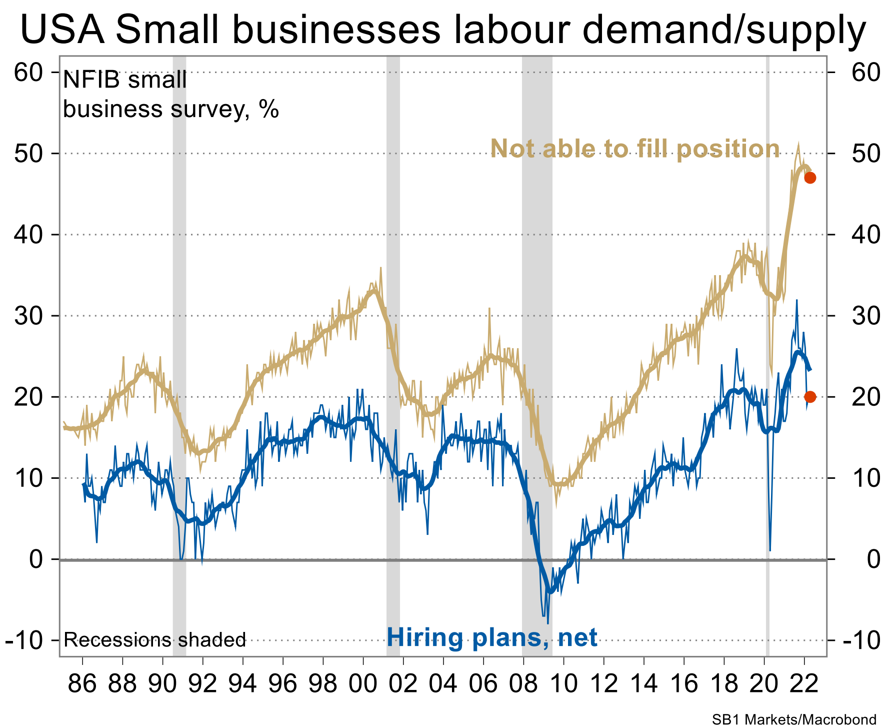


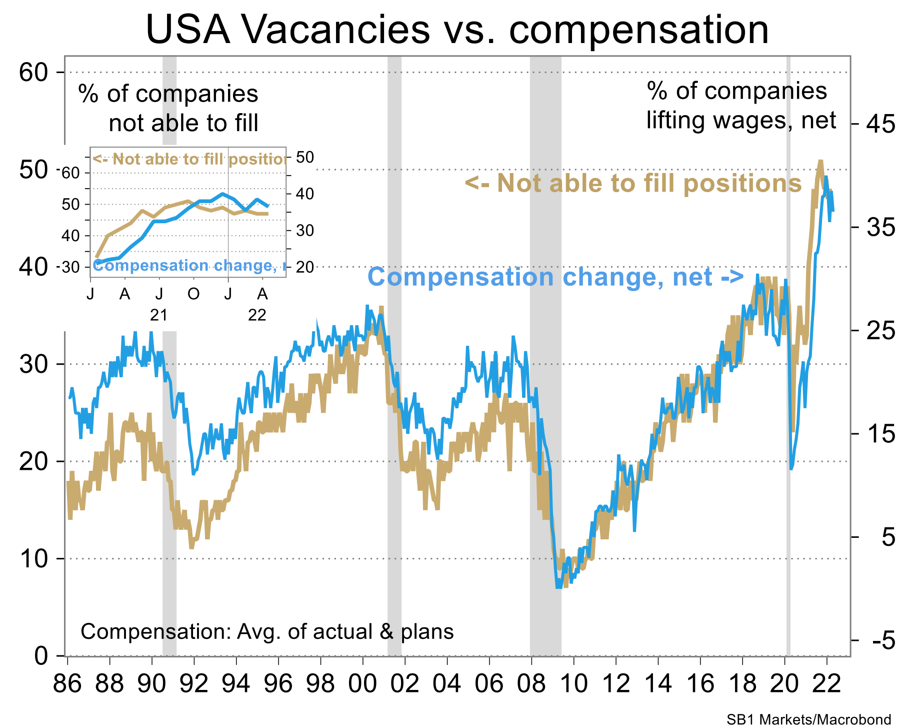


- We have never seen a 'jobs gap' like this before!
- **The Unemployment - Vacancy-curve** (UV, Beveridge curve) is still moving in the north-west direction, also signalling <u>a gradually tighter labour market</u>. The only silver lining may be that unemployment is falling faster than the vacancy rate increases, signalling that the <u>mismatch</u> in the labour market may be easing <u>somewhat – it is just tighter than ever before</u>

Fewer companies have hiring plans and fewer are not able to fill positions

... but levels are still very high, especially the vacancy index. Compensation plans are still aggressive

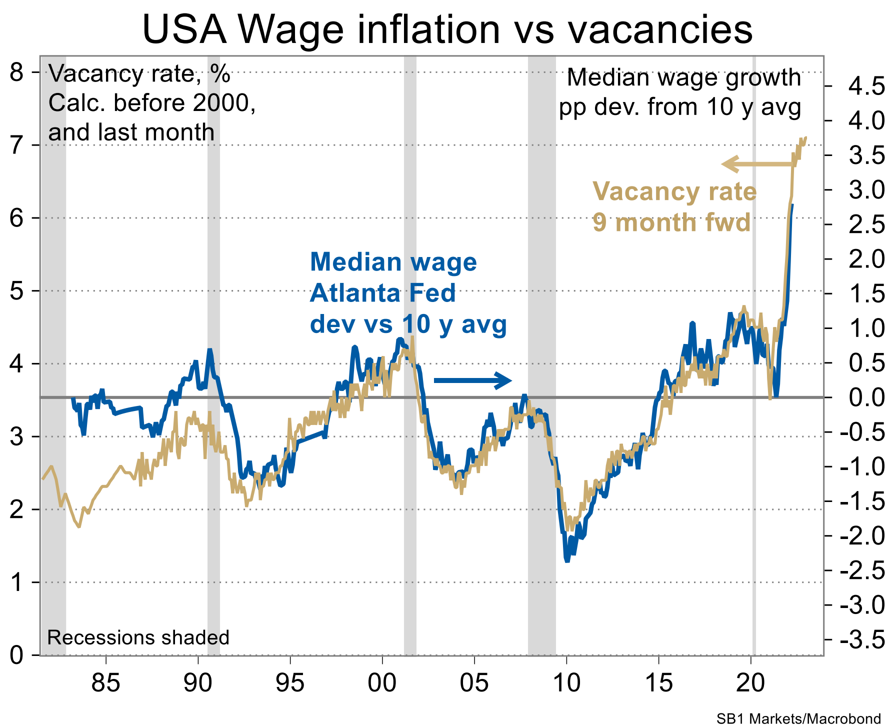


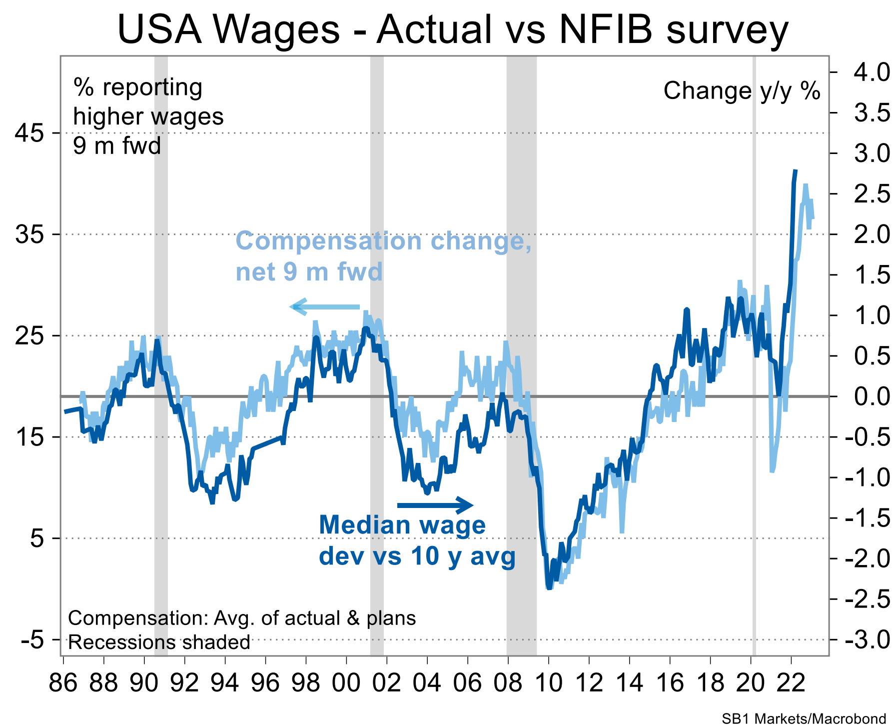


- **SMB's hiring plans** fell in March but stabilised in April, at a pretty high level
- The share of companies that report they are **not able to fill open positions** was stable in April but is slightly down from the peak in October last year. However, the level is far above anything we have seen before
- So is the share of companies that report **plans to lift compensation**. The proportion is just slightly down from the ATH in last December but is still signalling a rapid increase in wage inflation

There seems to be some connections here?

The correlation between the vacancy rate and changes in median wage growth is <u>extremely</u> tight

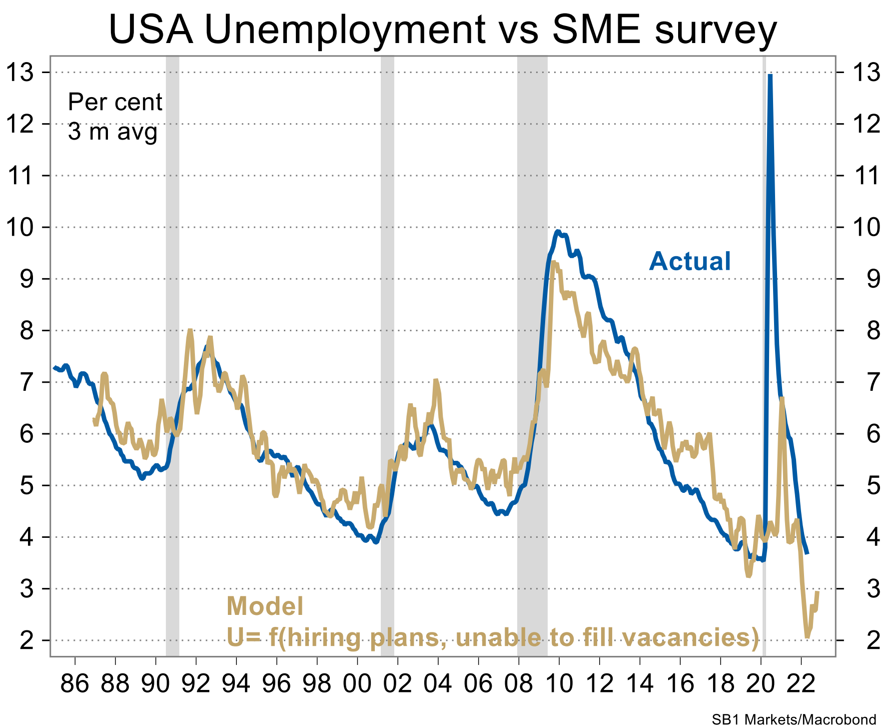




- Our 'Phillips curve' based in the vacancy rate signal a further increase in wage inflation the coming quarters, as the vacancy rate leads changes in wage inflation quite consistently by 3 quarters
- Companies (SMEs) compensation plans (see more next page) signal continued high wage inflation but not faster than the current
- Wage inflation has already accelerated by 2.5 – 3 pp vs the 10 y average (Atlanta Fed median) and cannot impossibly generate a 2% price inflation rate over time. <u>This is Fed's main headache. And it will be the stock owners' headache too, of course…</u>
- <u>Check under which circumstances wage inflation slows on the charts above (hint: find the shaded areas, follow the wage line ☺</u>

The tide may be turning

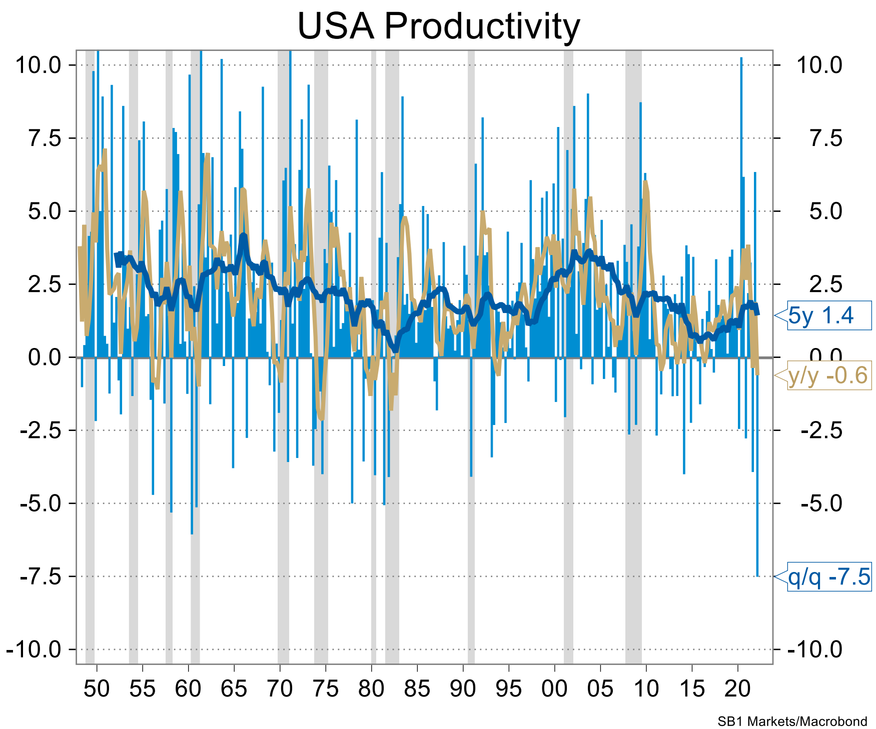
The ‘real’ tightness of the labour market can be described in many ways

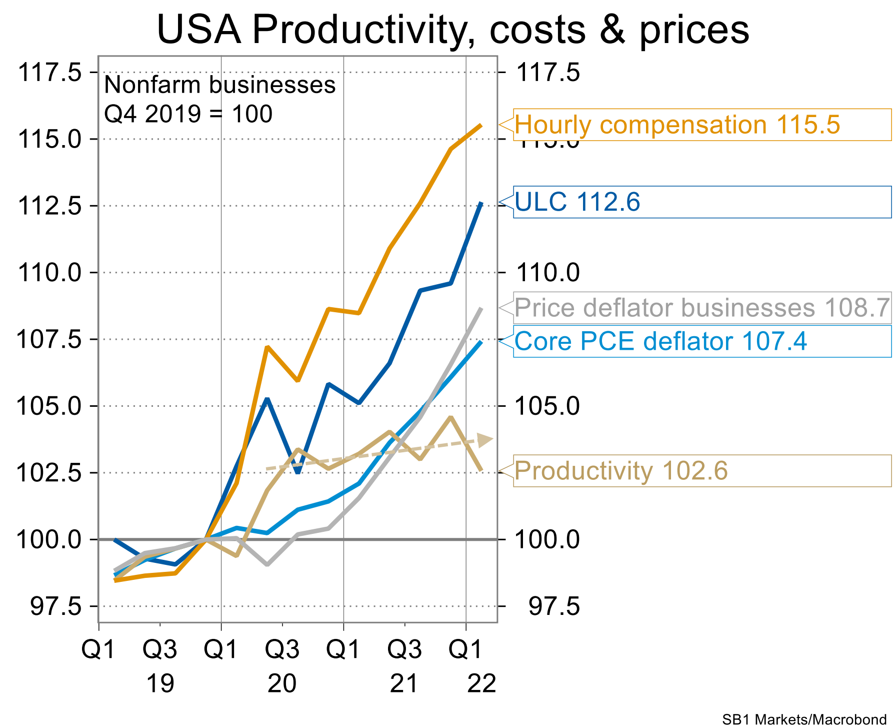


- Demand for labour and reported problems filling open positions in the SME survey correlates well to the official unemployment rate. The survey is leading unemployment rate by 6 – 8 months
- During the recent boom, the survey – as well as the official number of unfilled vacancies – signal a far tighter labour market than the current 3.6% official unemployment rate, explaining why wages have shot up faster than what can be explained by the unemployment rate itself (which is well explained by the vacancy rate)
- However, since last autumn, the SMEs report somewhat less aggressive hiring plans, and somewhat fewer businesses report that they are not able to hire. Still, they are signalling a 3% unemployment rate, which very likely not bring the vacancy rate or the wage inflation down to a sustainable level

A Q1 productivity outlier – but the real problem is a dismal trend. ULC up >>5%

An unprecedented 7.5% drop in Q1 (exp. 4.5), and down 0.6% y/y. Underlying trend < 1%

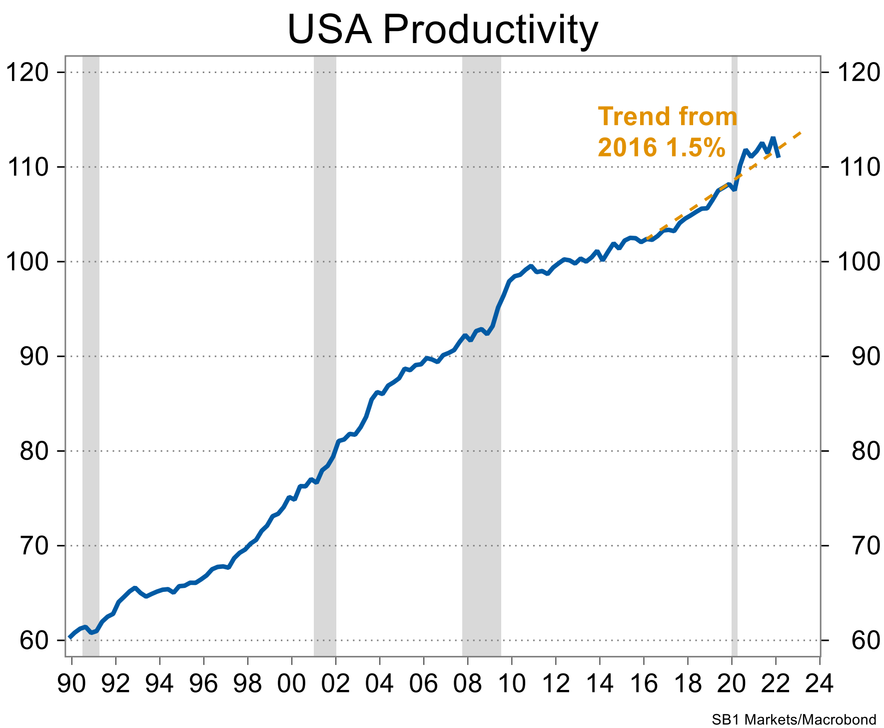


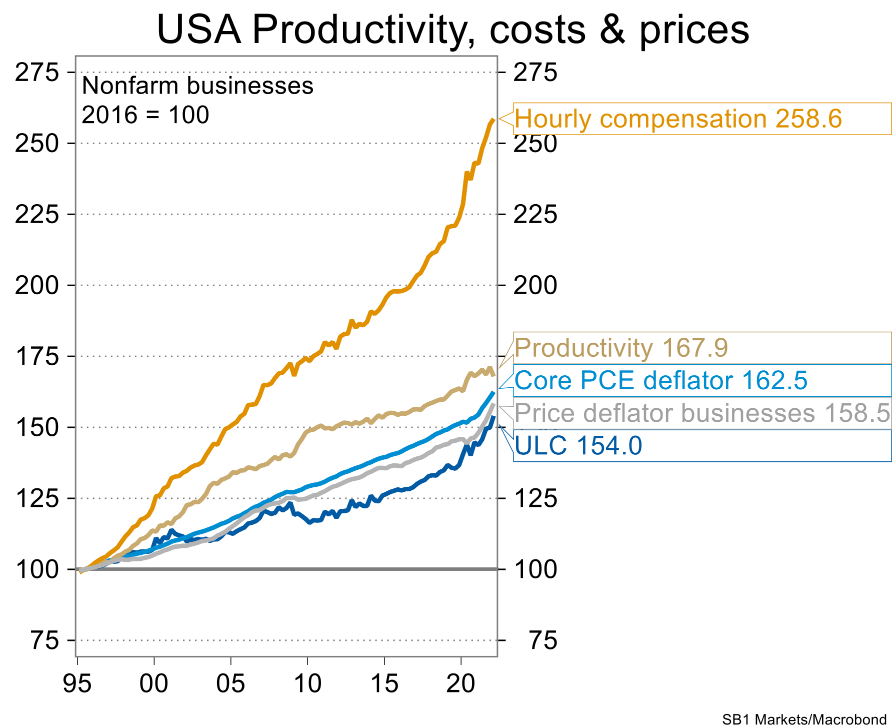


- **Productivity data** are still all over the place. In Q4, nonfarm business productivity surged 6.3% (but fell 3.9% in Q3). Hours worked rose much more than we assumed (and much more than the nonfarm payroll report has indicated). Output fell by 2.4%
- Still, the problem is a weak **underlying trend**. Productivity is up at a 1.1% pace since before the pandemic, and well below 2% since mid 2020. The trend since 2015 is though at 1.5%, perhaps a fair underlying trend estimate. (BTW we still think the Q1 GDP data were suspectedly weak, and productivity may be revised up)
- **Hourly compensation (wages ++)** grew at just a 3.2% pace in Q1, but the annual rate still accelerated to 6.5% from 5.5%. Since Q4-19 hourly compensation has grown at a <u>6.6% pace, way above the pre-pandemic level</u>
- **Unit labour costs** (hourly compensation – productivity) grew by 11.6% in Q1 (expected 7.9%), up 7.2 y/y, the highest since 1982. Since Q4-19, <u>ULC has grown at a 5.4% pace, far above a normal level – which of course is totally incompatible vs the 2% inflation target</u>

No impressive lift in productivity during the pandemic

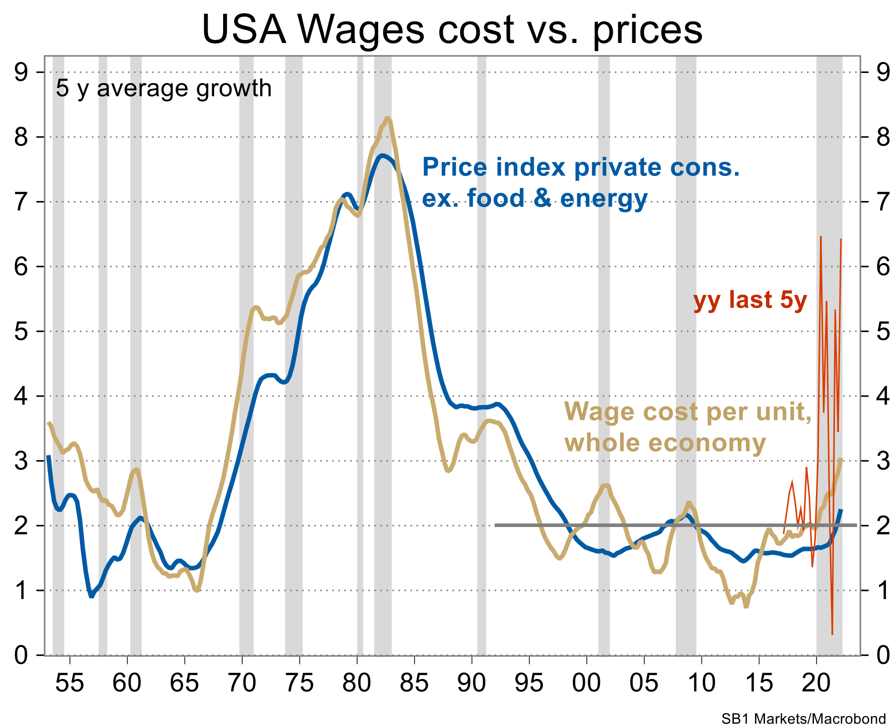
However, a quite impressive lift in hourly compensation…

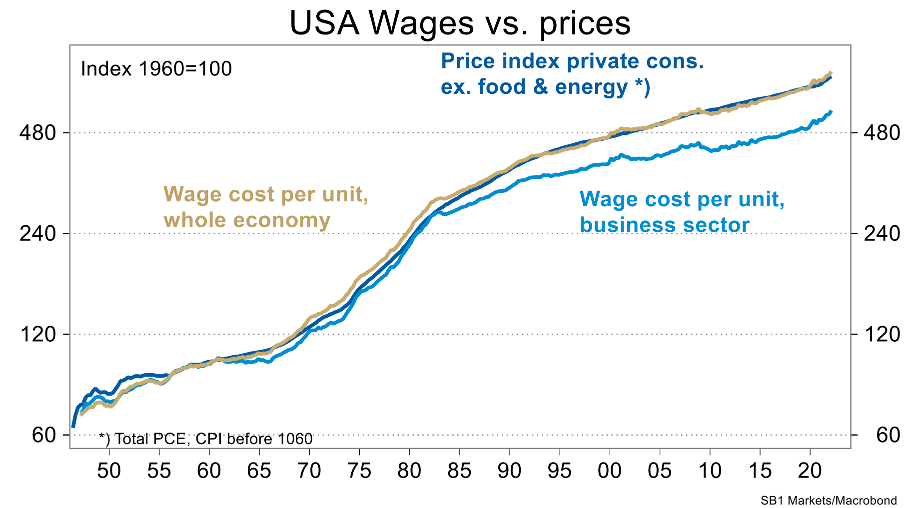


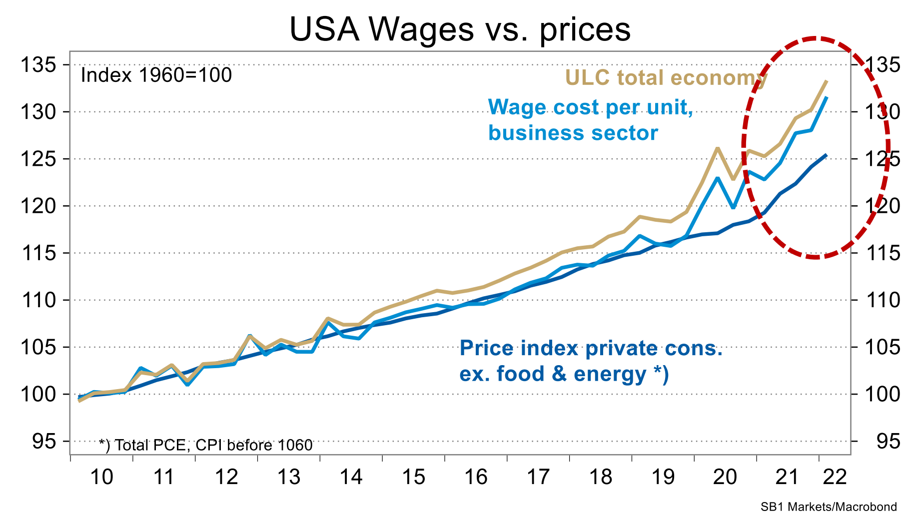


Wage inflation is the main risk, not raw materials/energy/corp. margins

Still risk vs core inflation even without faster wage inflation from here



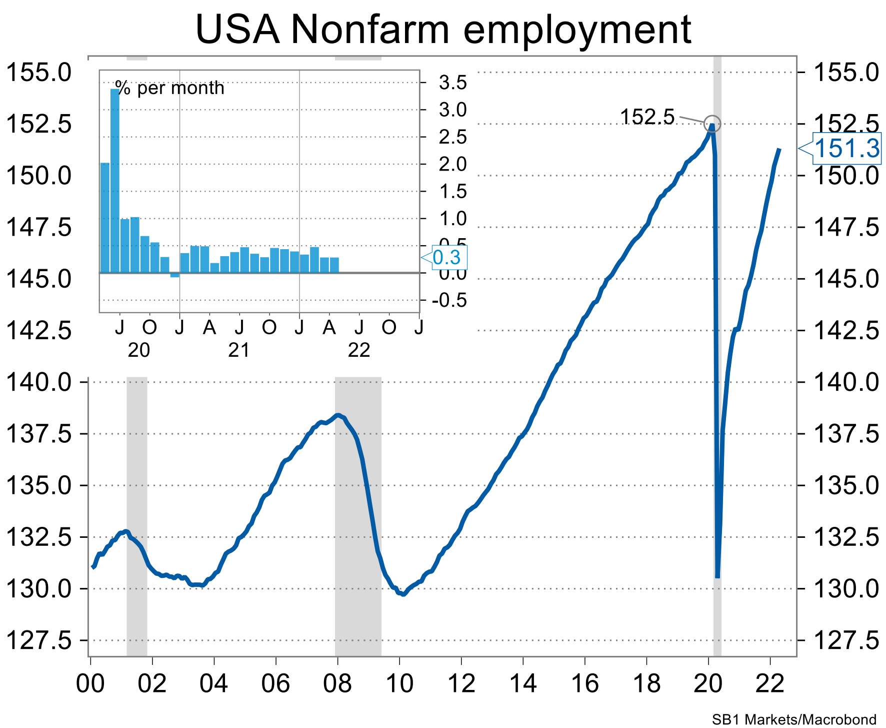


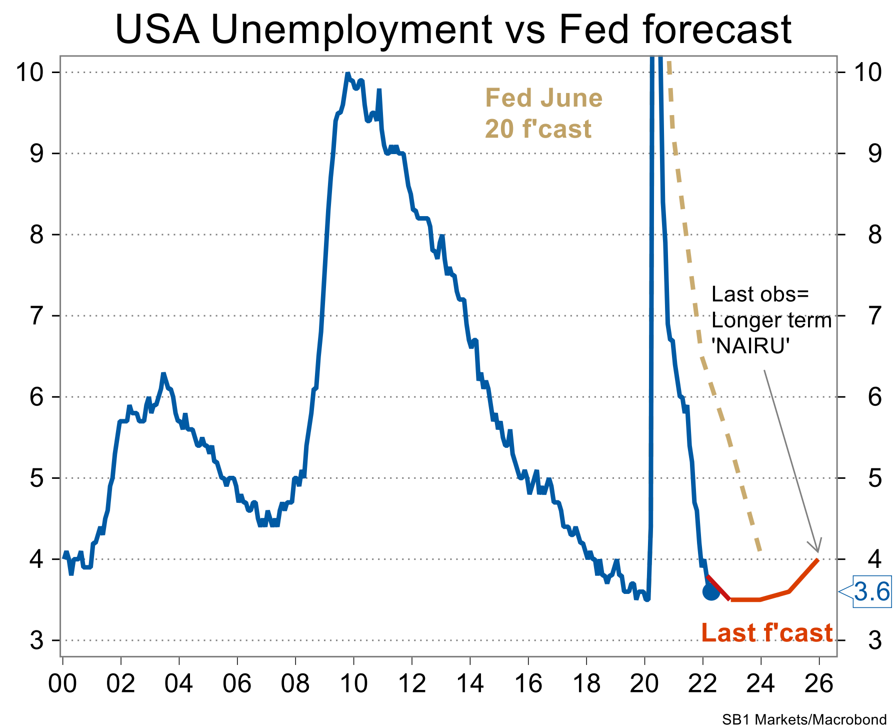


- Costs have climbed faster than core prices since before the pandemic

Stable growth in nonfarm payrolls, unempl. flat at 3.6%, wage infl. ‘just’ 0.3%

The participation rate fell, signalling limited reserves left



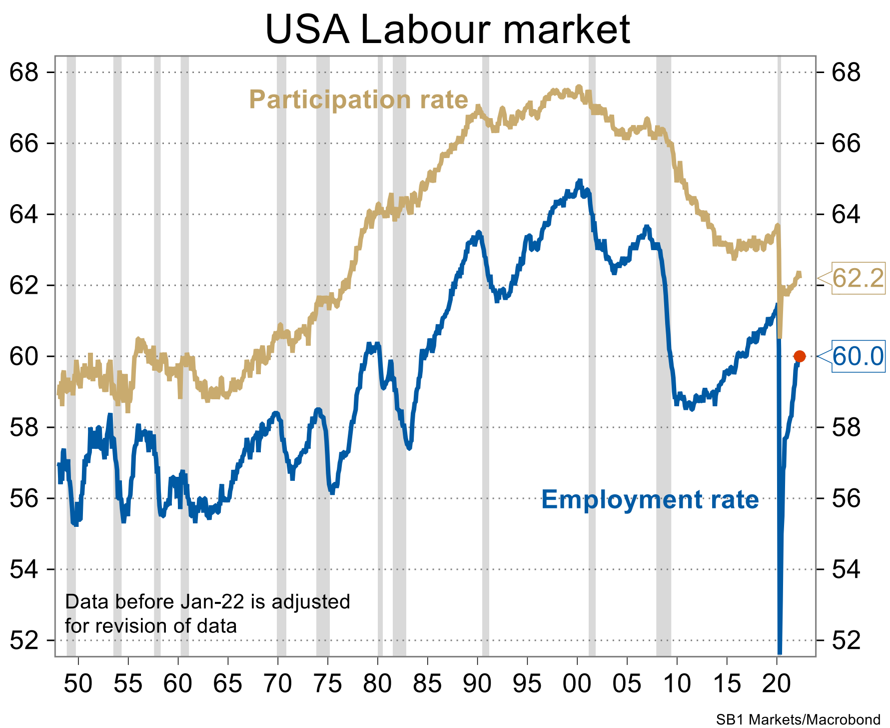


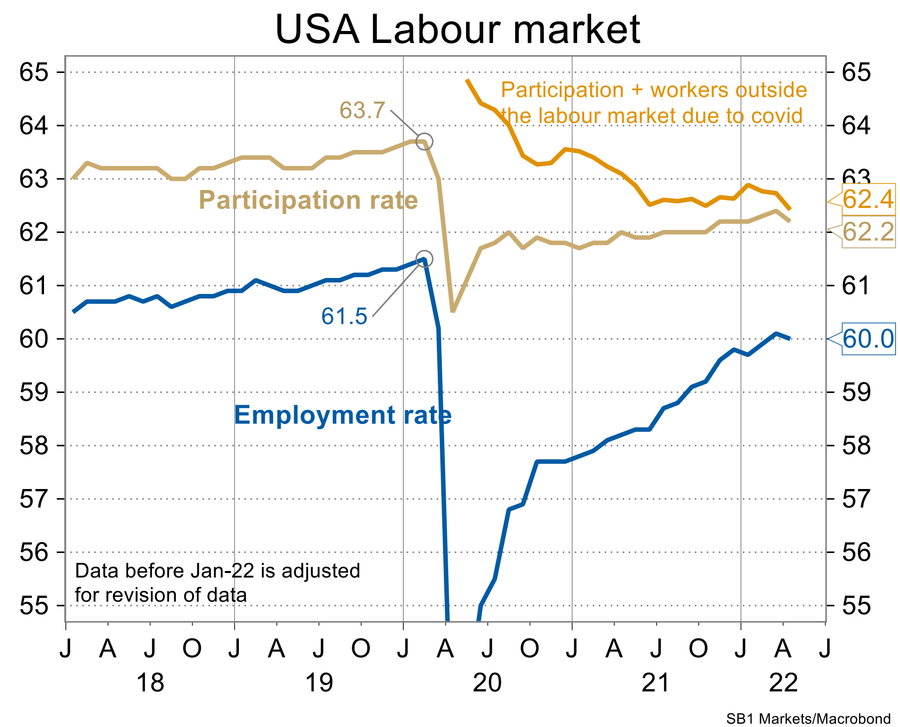
- **Nonfarm payrolls** rose by 428’ in April, like in March, and 50’ above expectations. The past 2 months were revised down by in sum 39’. Payrolls are still down 1.2 mill vs. Feb-20 or by 0.8%. The LFS employment declined by 353’. This number is much more volatile from month to month. The employment rate fell 0.1 pp. Average hours worked is trending down but remains well above the pre-pandemic level
- **The participation rate** surprisingly fell 0.2 pp to 62.2%. The trend is still probably up, but slowly vs. the still brisk demand for labour. Including those outside the labour marked due to Covid related reasons, the rate is 62.4% as very few now states Covid as a reason for not working/searching work
- **The unemployment rate** was stable at 3.6%, 0.1 pp higher than expected. <u>The rate is now just 0.1 pp above Fed’s estimate end of ‘22 estimate – and 0.4 pp below Fed’s estimate of the long term NAIRU.</u> In March, the unfilled vacancies equalled 6.8% of the labour force (7.1% of employment)
- **The average wage** rose 0.3%, 0.1 pp less than expected but growth in March was revised up by 0.1 pp to 0.5%. The annual rate is 5.5%, as expected, up from 3¼ before the pandemic – and <u>not compatible with 2% CPI inflation over time</u>
- **Maximum employment:** Even if the participation may be trending slowly up, the <u>supply side is obviously the bottleneck at the labour market</u>. For the time being, maximum employment is reached – and wage inflation is well above a sustainable level

SpareBank 1 MARKETS

The participation rate down in April, still trending slowly up

... but remains low vs. the pre-pandemic level. Very few Covid-related outsiders left

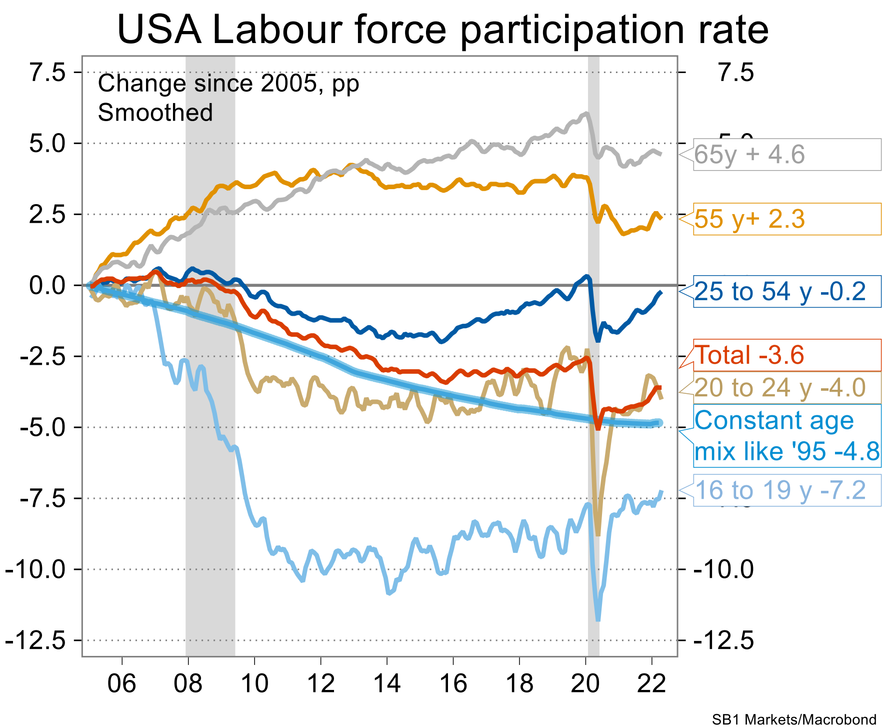


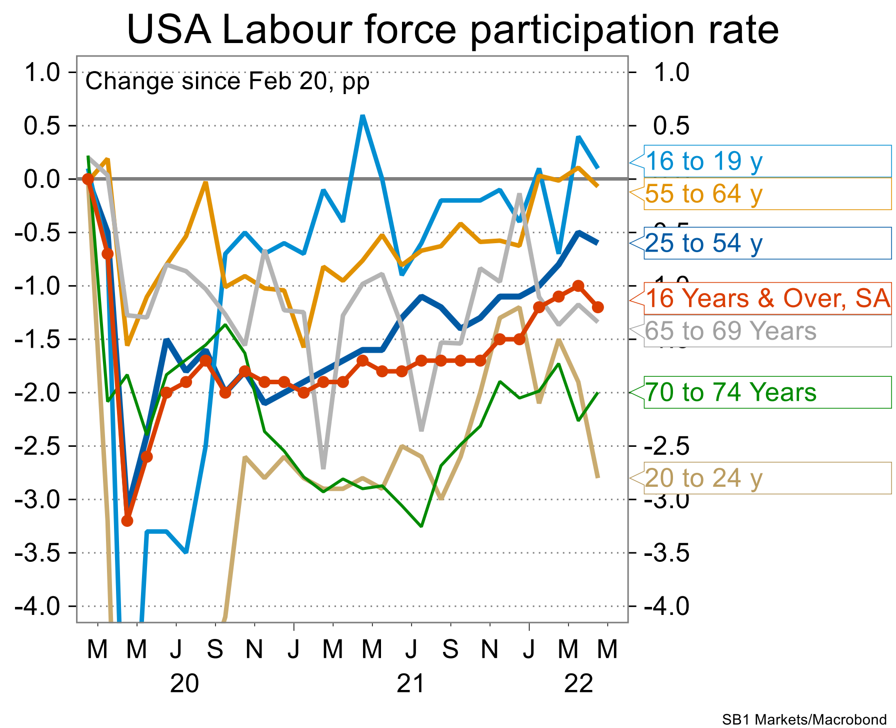


- **The labour force participation rate** surprisingly fell by 0.2 pp to 62.2% (of the working age population, 16 y +). The trend is slightly positive but not impressive given the increase in the employment rate (and the decline in the early part of the pandemic)
  - » The participation rate is down 1.5 pp (vs the working age population) vs the pre pandemic level, equalling 2.3% or 3.6 mill persons
  - » In April, 0.6 mill persons responded that they did not search for work (and thus were excluded from the work force) for Covid-19 related reasons, down from 0.9 mill in March (and 1.8 mill in Jan, 3.5 mill a year ago). Of the 0.6 mill, just 0.2 mill say they want a job. The reduction in no. of 'outsiders' has not led to an equivalent increase in the labour force. The 'covid outsider rate' has fallen by 0.9 pp (to just 0.2%) the past 12 months, while the participation rate has increased just 0.2 pp. This indicates that the reservoir of available labour supply is very limited
- **The employment rate** declined 0.1 pp to 60.0%. LFS employment fell by 353' following the 736' lift in March. Over time, the payrolls stats and the LFS report the same growth rates, but they may differ substantially from month to month. The employment rate is down 1.5 pp vs. Feb 20, equalling 2.4% or 3.9 mill persons

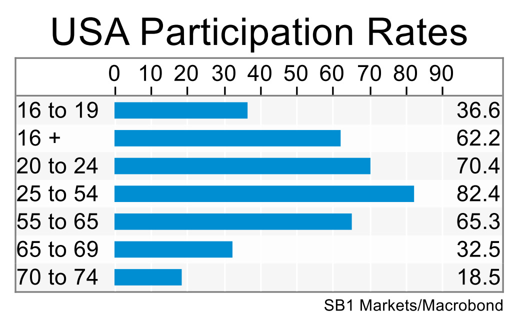
Participation rates: Core age groups soon back to pre-Covid & pre-GFC levels

Thus, the core reserve may be declining rapidly. The really old >64 seem hard to get back



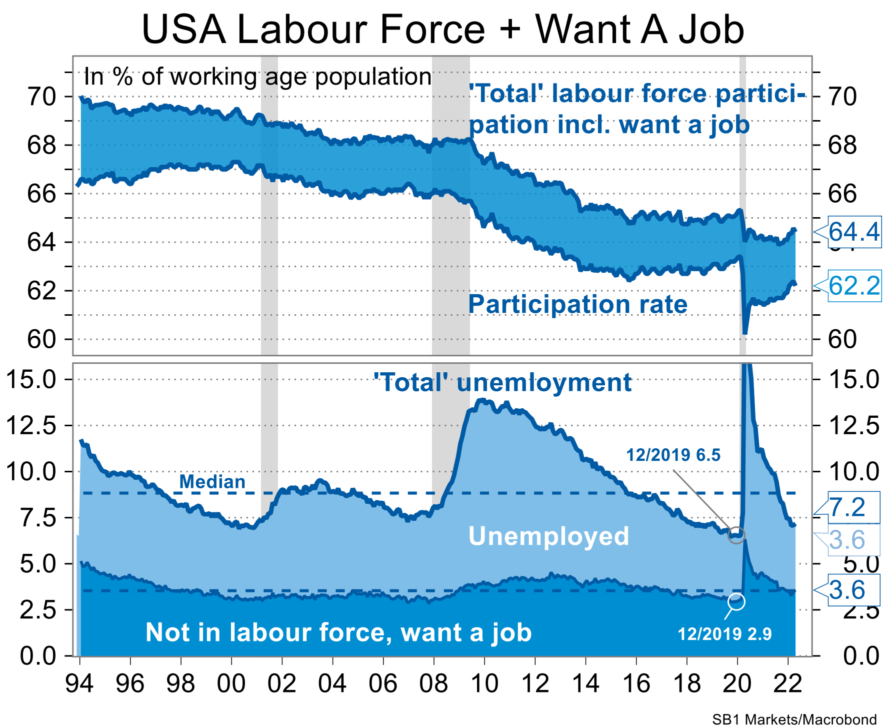


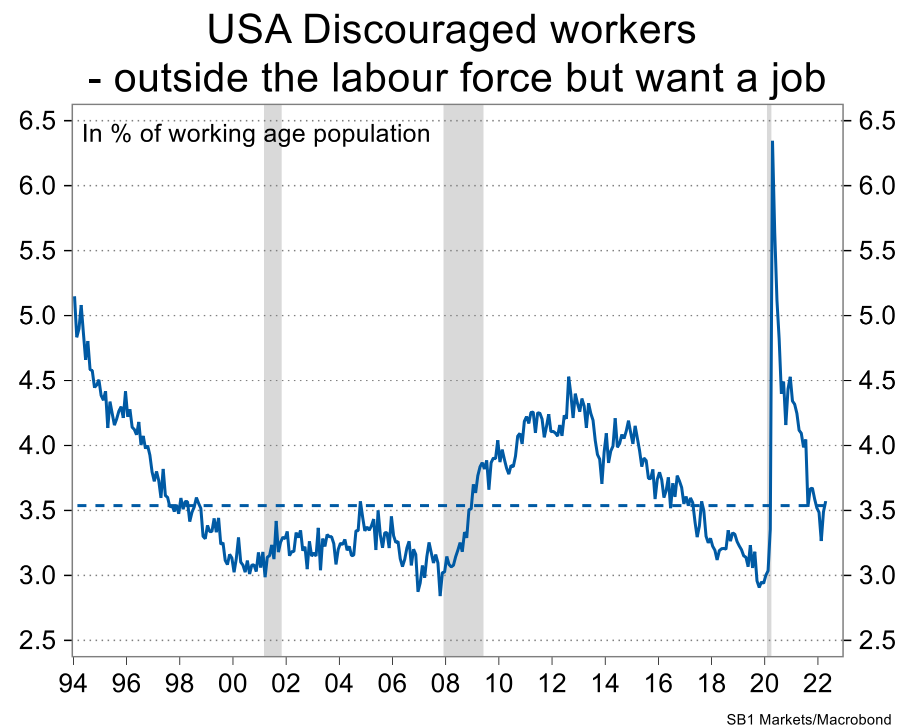
- The participation rate among the 25 – 64 y group is now back to the level from before the pandemic. The 20 – 24 y part of the population remains well below
- As the US population is aging, and a decline in the average participation rate over time is no surprise. The chart above illustrates the impact. The thick light blue line illustrates the participation rate if each group kept their participation rate at the 2005 level. The decline is due to the larger old cohorts



Not that many outside the labour force say they want a job

These outsiders equal 3.6% of the labour force, at the historical average

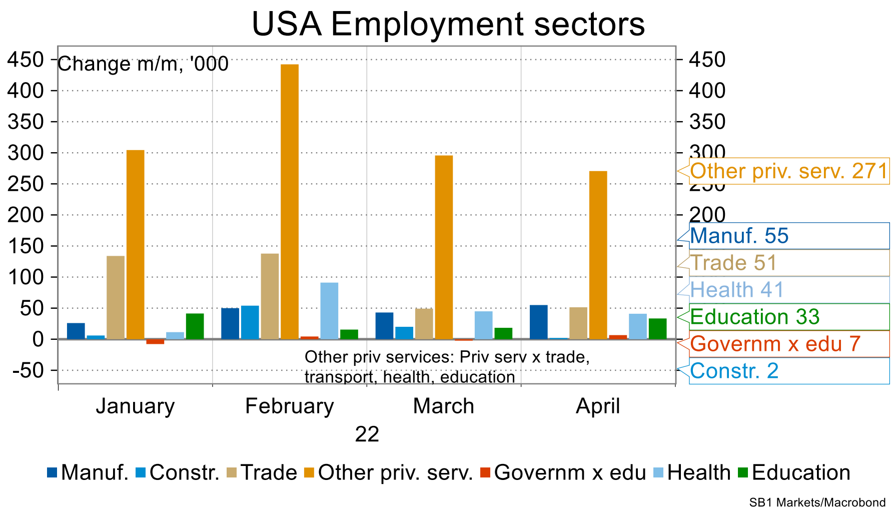


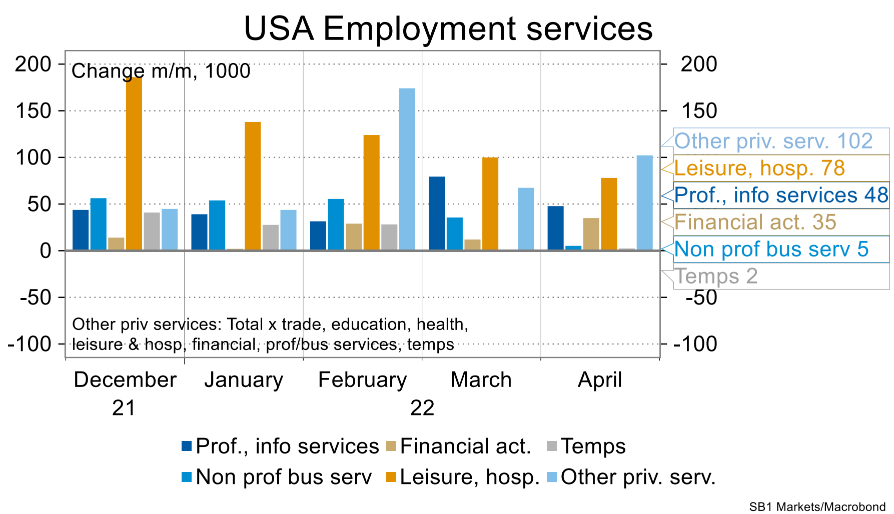


- Normally, the 'discouraged workers' rate is lower than average in booming times – and it 'should' have been below average. Those who sat they cannot work due covid now constitutes just a small fraction of the 3.6% rate

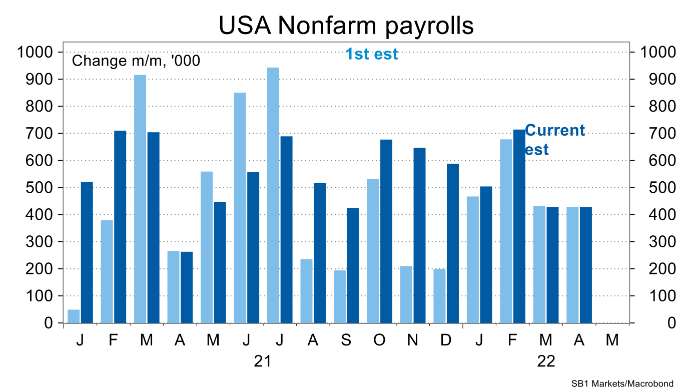
In April: Steady growth in most sectors

Still, slower growth in most sectors in March

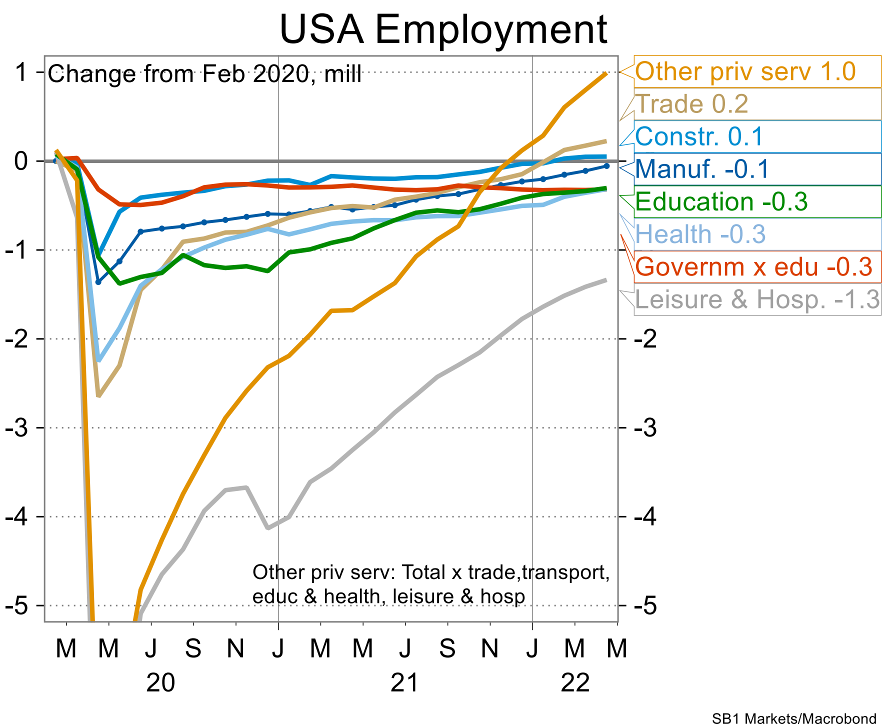


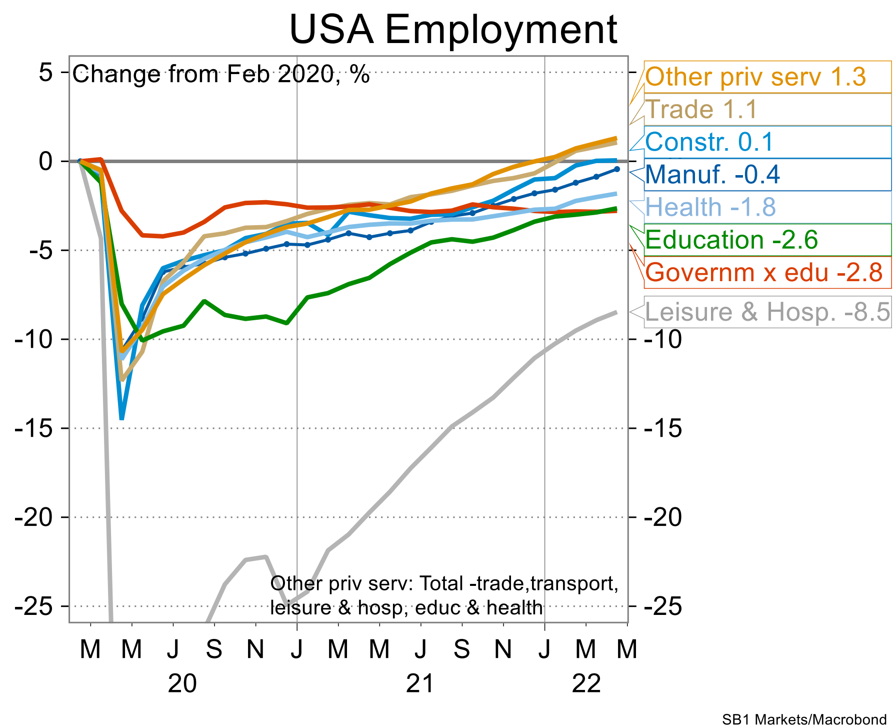


- **Last month:**
  - **Leisure & hospitality** (restaurants ¾ of the total, hotels, parks, gambling, arts++) added 78' jobs. Growth is now slowing, even if the no. of employed is still well below the pre-Covid level
  - **Trade** added 51' jobs – and the trend is steady upwards
  - A broad increase in payrolls in other **private services**
  - **Manufacturing** added 55', a still above average growth over time
  - **Construction** sector employment up by just 2', less than normal
  - **Education** (private & public) up by 33'
  - Employment in **government** (ex education) up by 7'



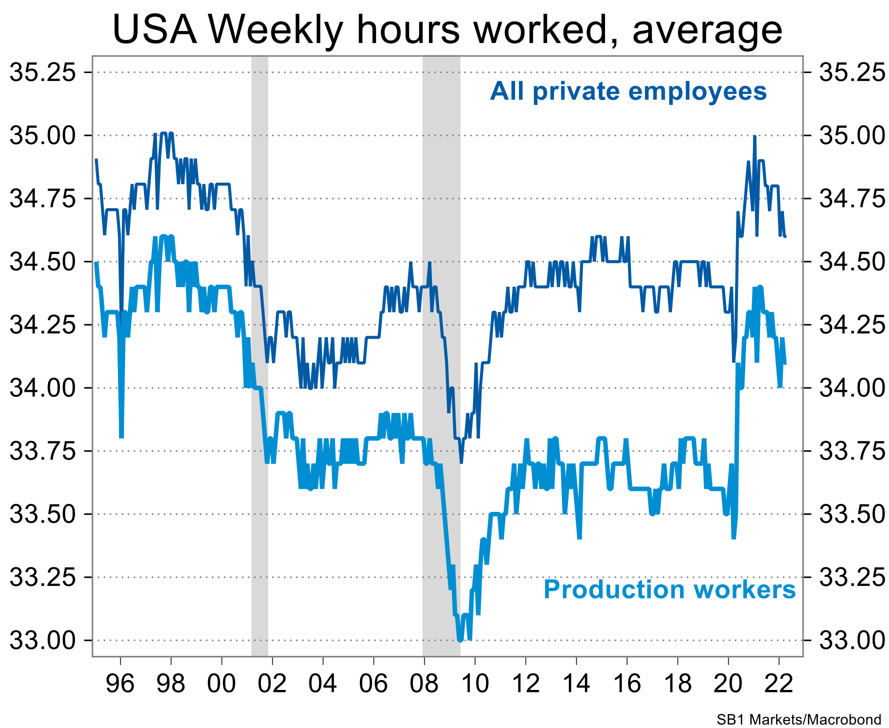
Vs. Feb-20: Several private services are up, but leisure/hospitality still down 8.5%

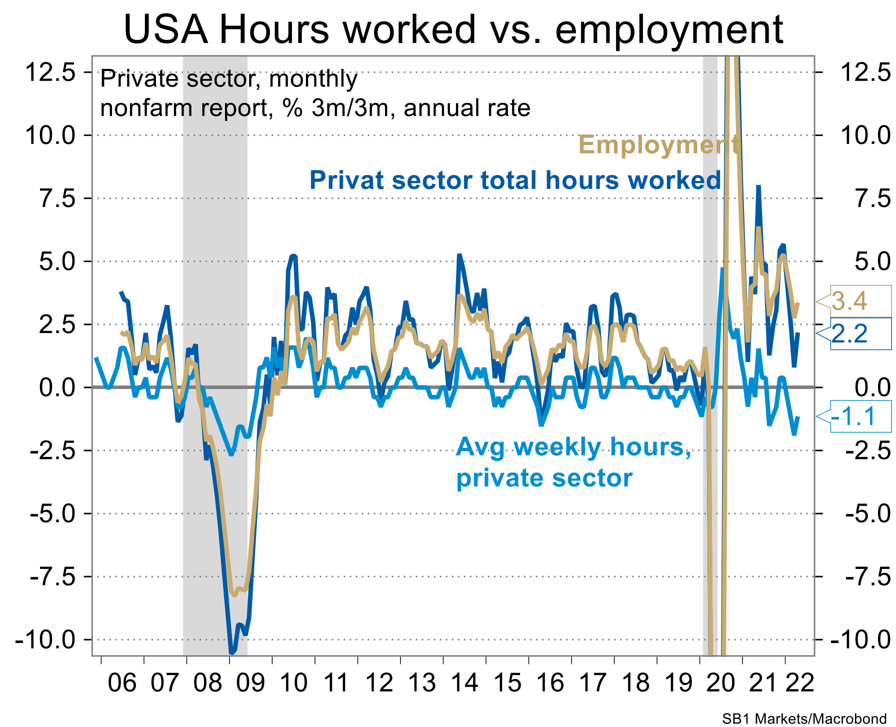




Average weekly hours flat in April but are trending down

The level is higher than before the pandemic. Part-time workers are probably returning now

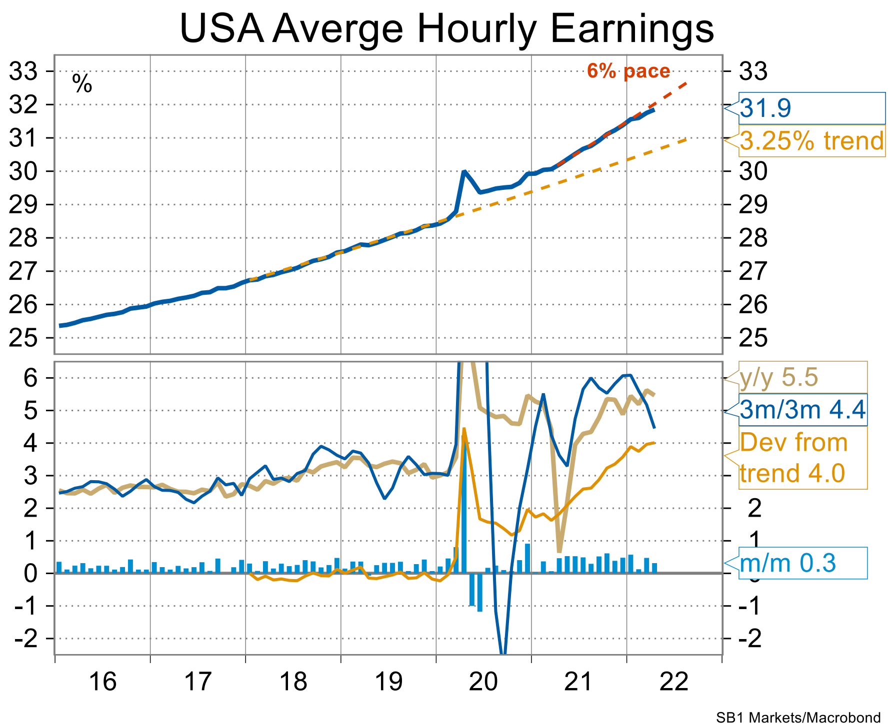




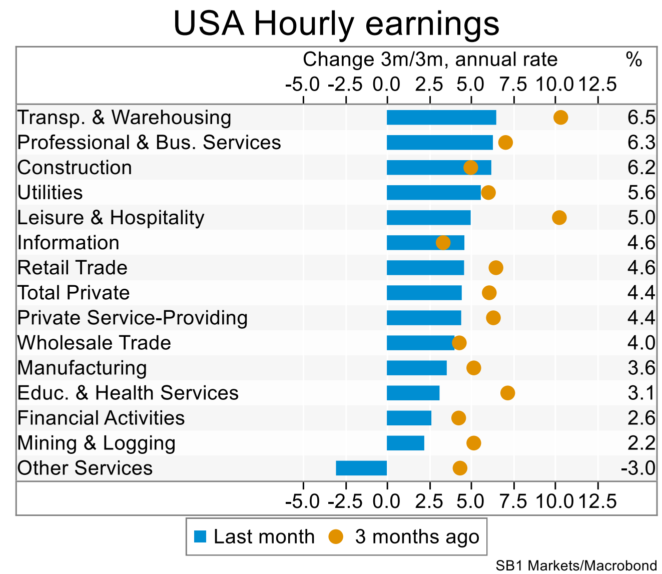
- 1.7 mill workers in the LFS reported that they have been unable to work or have worked fewer hours because their employer had closed or lost business due to the pandemic – down from 2.5 mill in March and 4.5 mill in February
- Underlying growth in total hours worked in the private sector is above 2% (In the Q1 productivity report, hours worked in nonfarm businesses are reported up 5.5% in, far above the estimate obtained from the payrolls report (0.8%) – an unusual discrepancy

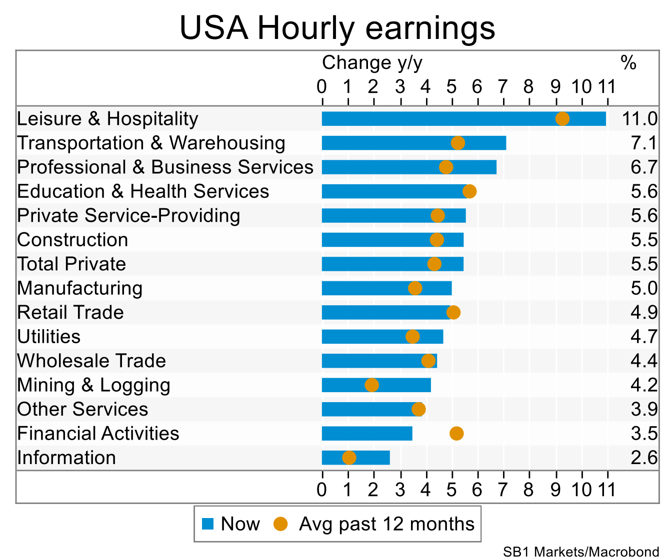
Wage growth may be slowing somewhat – but remains too high

The decline is broad based but not significant given the normal volatility in monthly data



- The **average wage** rose 0.3% in April, 0.1 pp less than expected, but March was revised up by 0.1 pp to 0.5%. **The annual rate** slowed 0.1 pp to 5.5%, as expected
- Underlying (3m/3m) growth has slowed to 4.4% from 6% in January
- Before the pandemic, wage inflation was at approx. 3¼%
- These monthly wage data are not adjusted for the change in employment mix between sectors or within sectors

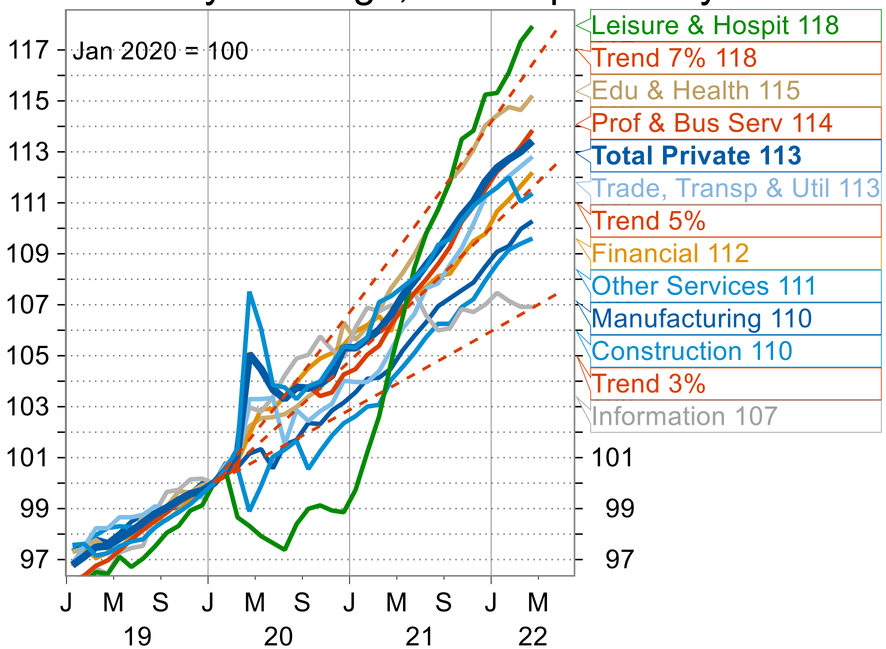




Wages are climbing at 4% – 7% growth pace, the average at 6%

… And well above the pre-pandemic growth path in all sectors

USA Hourly earnings, non-supervisory workers

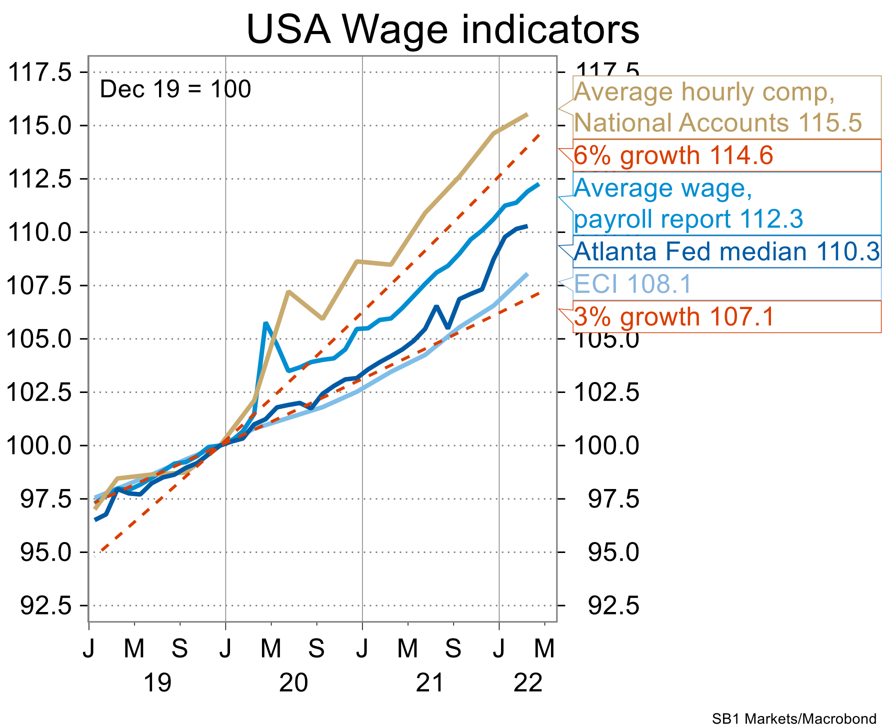


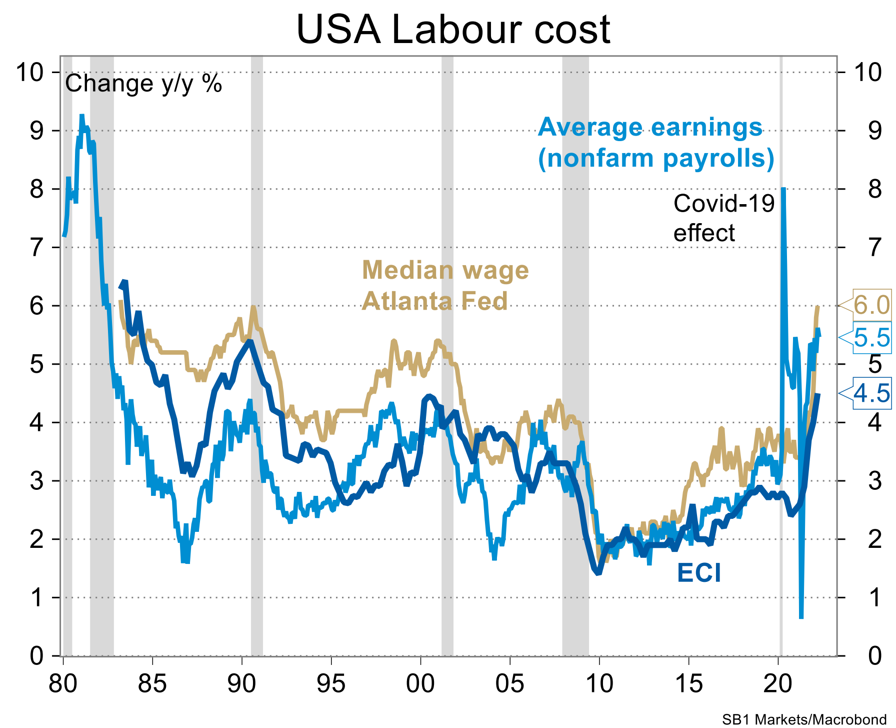
SB1 Markets/Macrobond

Memo: On the chart to the left above, wages for non-supervisory workers are shown. When all employees are included, growth is slightly lower in most sectors

Wage indicators agree: Growth has accelerated, to substantially > the 10y avg

… which yielded 2% inflation (or more). Productivity has not accelerated

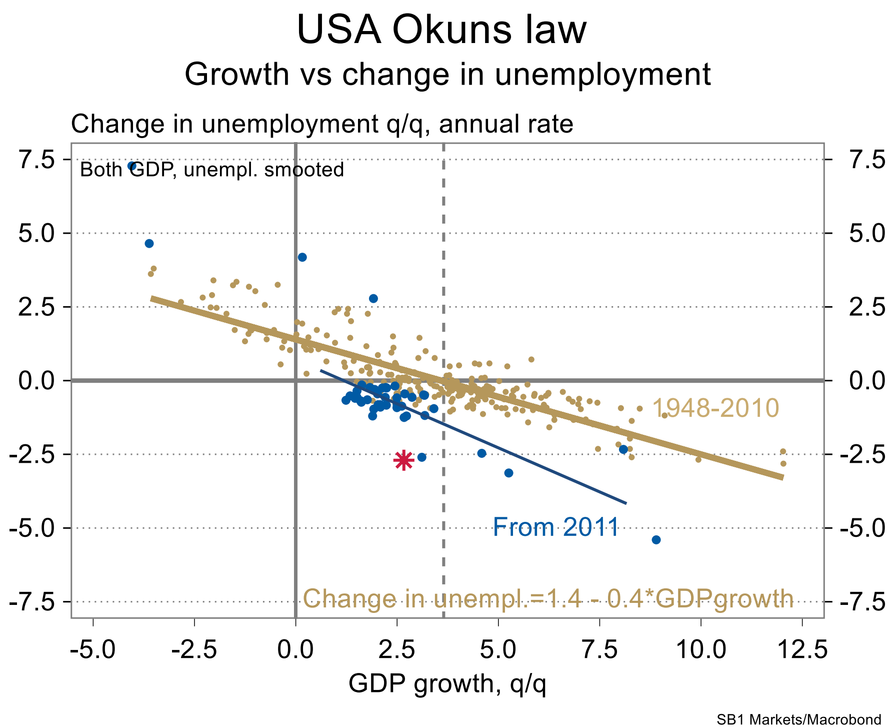




- **All wage indicators** are reporting faster wage growth, and all reporting wage growth well above the average recent years, also if we apply a 2-year average growth rate, to exclude the impact of changes during the first part of the pandemic (chart to the right)
- Growth in wage/earnings/compensation indicators are up 1.5 – 3.5 pp vs the their respective 10 y averages. There is an obvious risk that wage inflation will accelerate further (check the following pages) – probably until the next recession hits as the labour market is extremely tight
- Over the past 10 years, inflation has been close to 2%, and well above 2% if calculated over a shorter period
- It will be a 'challenge' to keep inflation at 2% if wage inflation remains at 5% - 6 %. Productivity growth has not accelerated. Profit margins may take a beating – and they very likely will – but probably not sufficient to bring inflation down. Wage inflation will probably not slow by much before demand for labour weakens – and unemployment increases

Uemployment will not stop falling before growth slows substantially

In the good ol' days, some 2.5% – 3% growth was sufficient to stabilise unemployment



- Now, growth will probably have to slow well below 2% in order to prevent unemployment for falling further
  - » But we have not seen normal cycles recent years, from 2010 to 2019 a just a continuous decline in the unemployment rate

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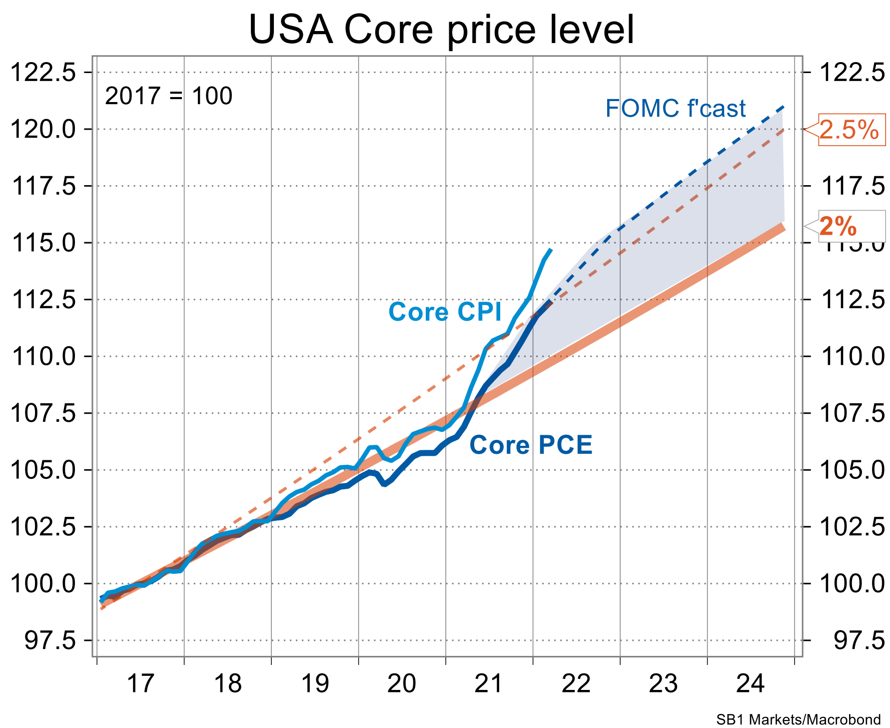
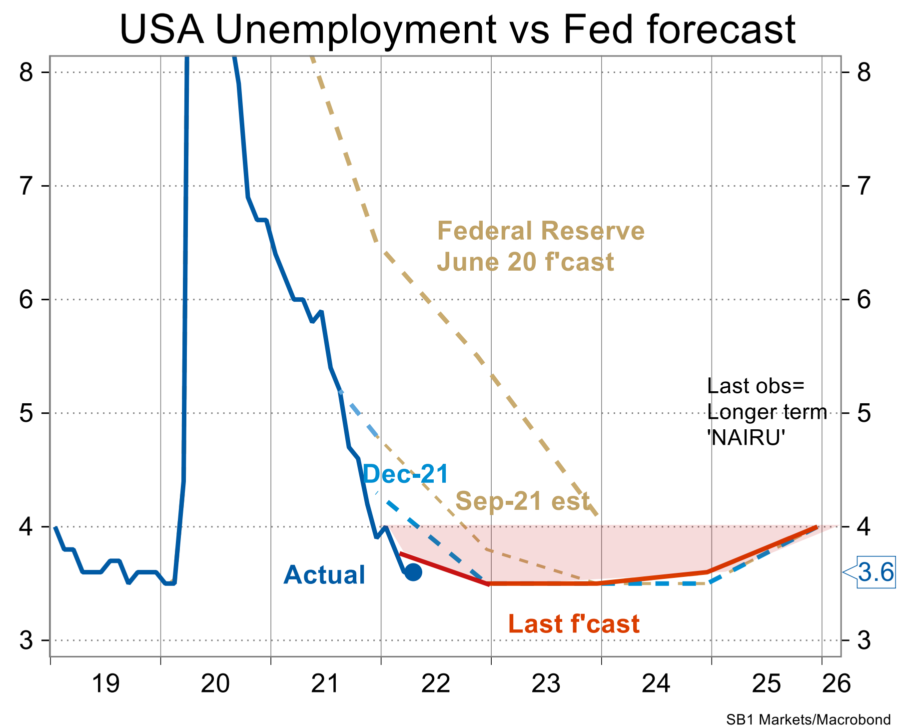
Fed's challenge: Neither the inflation target nor the employment target is met

Both inflation and xxemployment are at too high levels, and are expected to remain too high

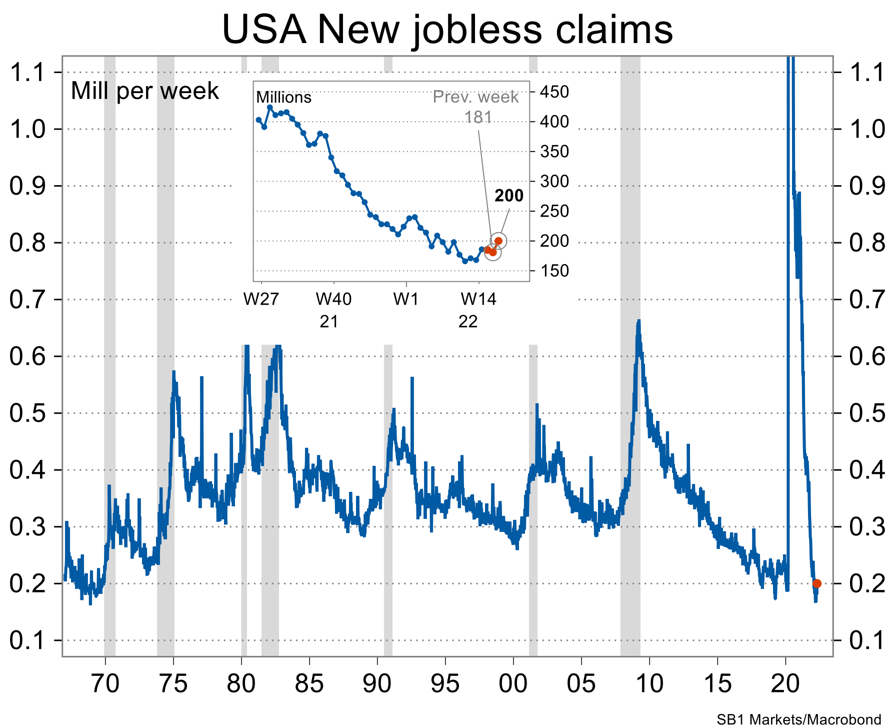


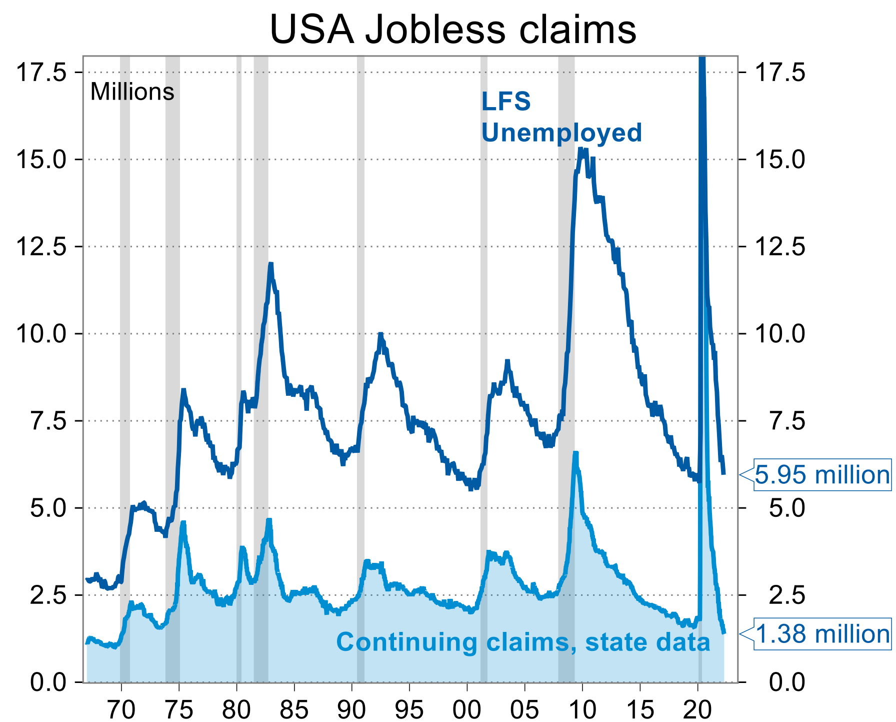


- The price level in late 2024 is expected to be 4.6% higher than implied by the 2%-over-time price-level path, 'promised' by the Federal Reserve
- At the same time, unemployment is expected to remain below the 4% assumed long term equilibrium rate the coming 3 years, at 3.5% from the end of 2022. The current unemployment rate is 3.6%
- To prevent the unemployment rate from falling further, GDP growth will have to slow sharply, NOW

New jobless claims increased up to 200', the very short trend up?

Continued claims fell further – to the lowest level since early 1970s

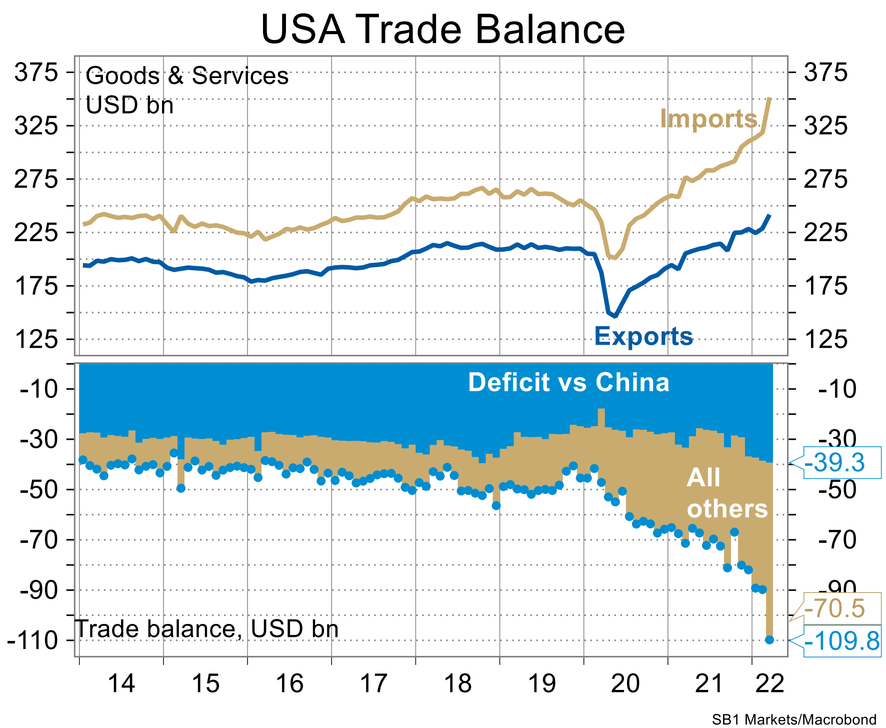


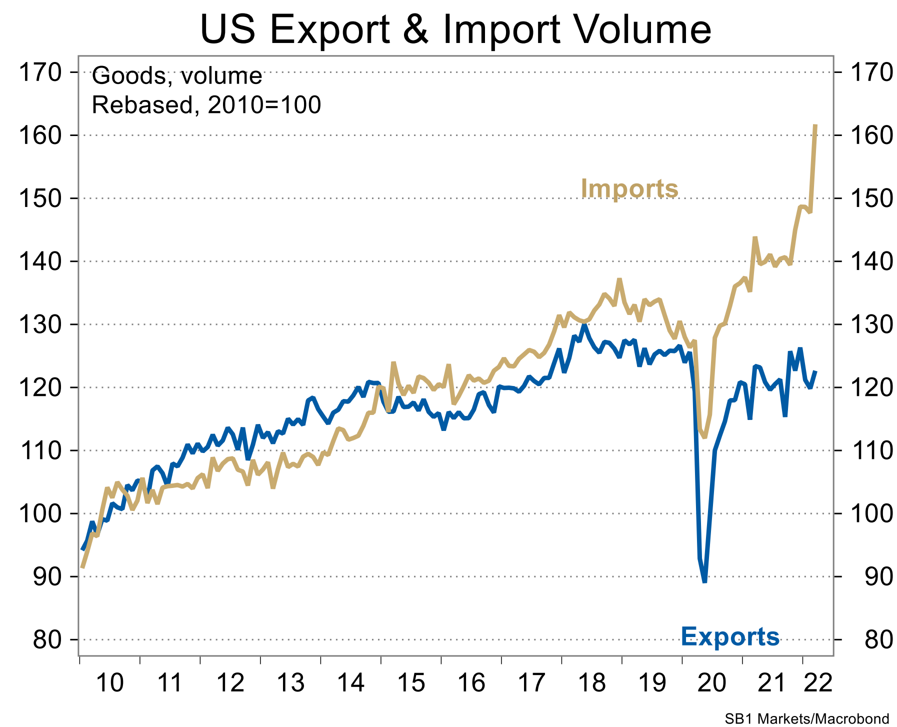


- **New jobless claims** grew by 19' in week 17 to 200'. Recent weeks, the inflow has increased marginally. Still, the inflow is close to the lowest level since 1968, when the labour force was 2 times larger than today
- **Ordinary continuing claims** declined by 19' to 1.41 mill in week 16, not seen since January 1970
- Another confirmation that the **labour market** is extremely tight

The trade deficit rose to ATH in March, by a wide margin

Import volumes are sky-rocketing, export volumes are still bleak, below the pre-pandemic level

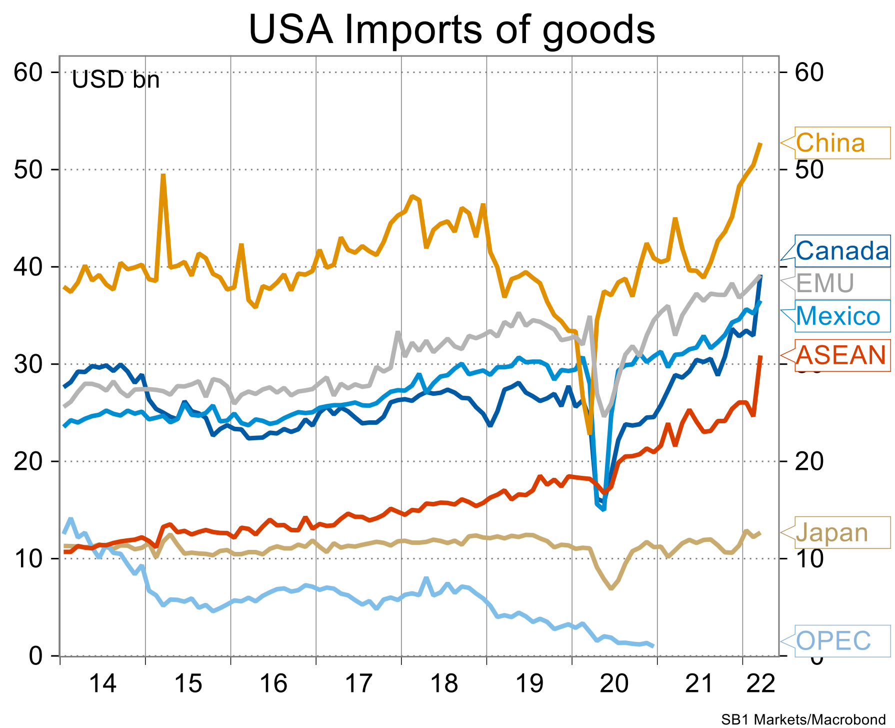


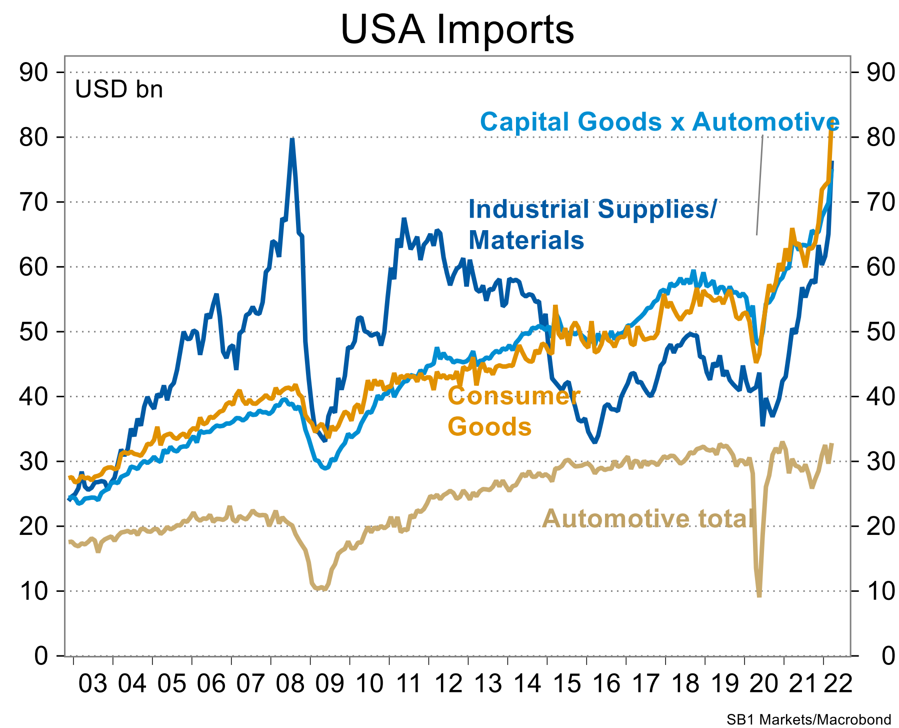


- **Imports** rose by 10% m/m in March and are 40% (!) above the Feb 2020 level. In volume terms, the imports of goods rose 9.5% m/m, to 26% above the Feb-20 level! Demand for goods has been strong during the pandemic, driving imports – even if auto imports have been low. We expect US households' demand for goods to slow the coming quarters, from the present very high level – dampening demand for imports too
  - » All sorts of imports rose, from everywhere. Imports from China rose to the highest level ever – and China is US' largest trading partner
- **Exports** rose 6% m/m in March. Export volumes gained 5%, but are still down 2% from Feb-20. We expect many of the US' trading partners to increase their demand for US goods, and one day even for services (like travelling into US)
- **The trade deficit surged to USD 110 bn from the previous** ATH at USD 89 bn, far above expectations before preliminary trade data were published tow weeks ago. The trade deficit is at 5.6% of GDP, not far below the ATH before the financial crisis

Higher imports driven by everything, and now even autos!

Consumer goods are up more than 50 % (in value) from before the pandemic!

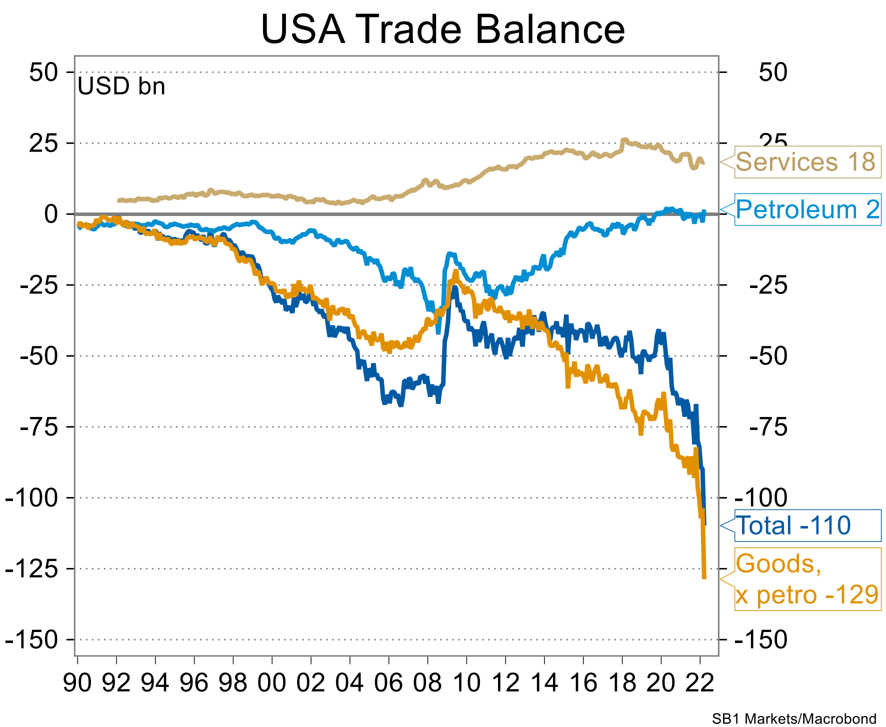


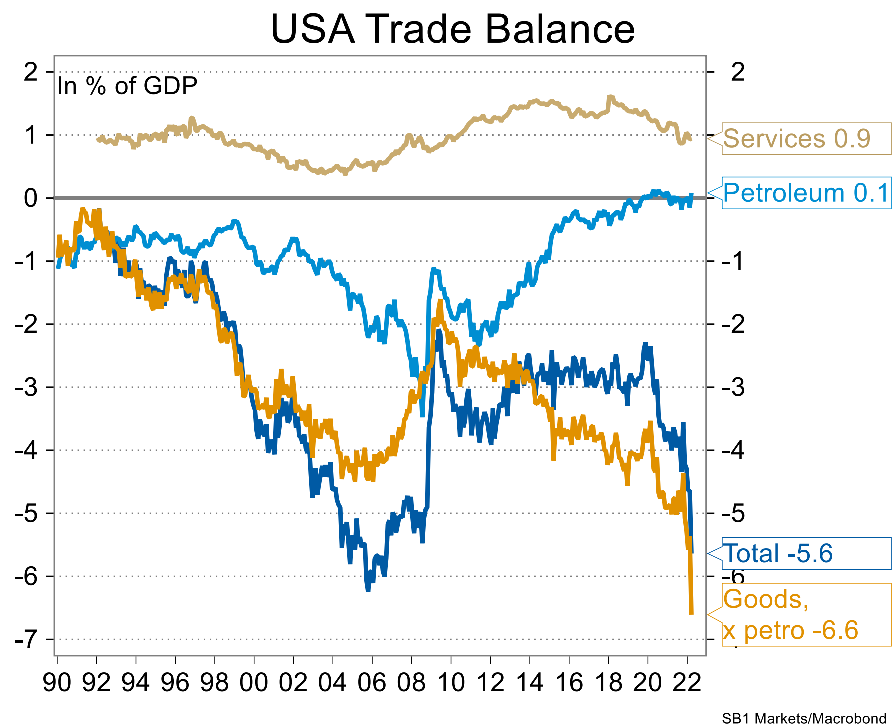


- **Imports from regions:**
  - » Imports from China are at an ATH – and is the largest counterpart vs. imports into the US
  - » Imports from ASEAN (the minor Asians) are trending sharply up – as are imports from Canada – and both spiked in March
  - » Imports from the EMU has been growing rapidly during the pandemic, but has flattened recently
- **Imports by type of goods:**
  - » Consumer goods imports are surging, but so is imports of capital goods (up >40% vs the pre-pandemic level, and industrial supplies are up more than 80% (all figures in value terms))

Goods x petroleum deficit very high, even in % of GDP

Surplus in services keeps narrowing

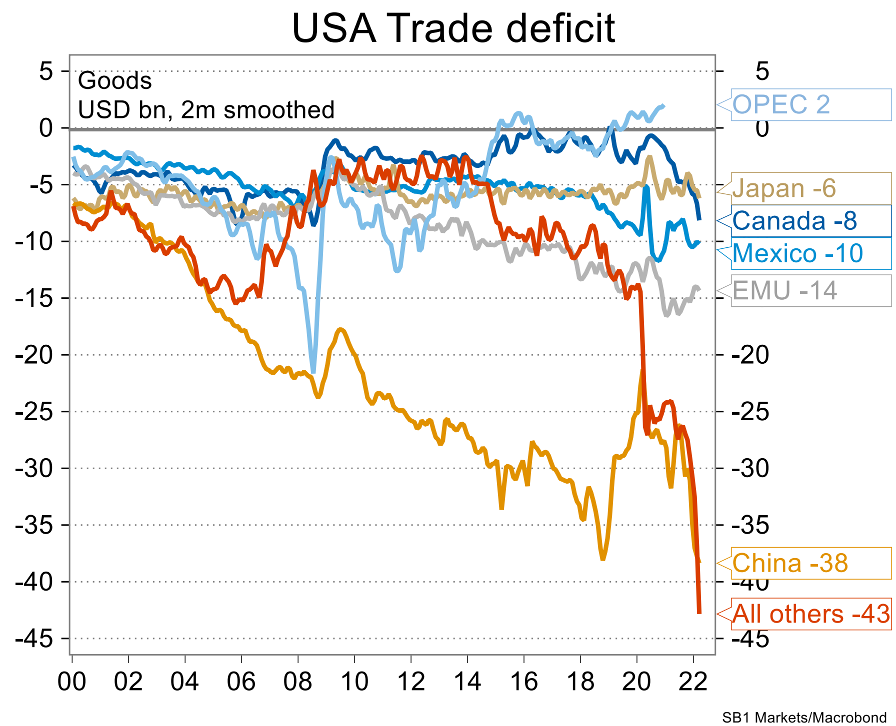




- The **total trade <u>deficit</u>** at USD 110 bn equals 5.6% of GDP, still below the record at 6.2% in late 2005, thanks to the shale oil revolution. The deficit has widened from 2.5% in early 2020 – as domestic demand has been stronger in the US than abroad
- **The US runs a <u>surplus</u> in services** at USD 18 bn, equalling 0.9% of GDP, but it is trending down (and the downturn started <u>well before Covid</u>)

The deficit vs. China is widening rapidly again, to ATH

The deficit is increasing in most directions



- The US deficit in goods (no services in these country stats) vs China equals more than 43% of the total deficit in goods, still lower than before the trade war started
- The deficit vs EMU has flattened during the pandemic – at a record high level
- The balance vs 'others' rose sharply in 2020

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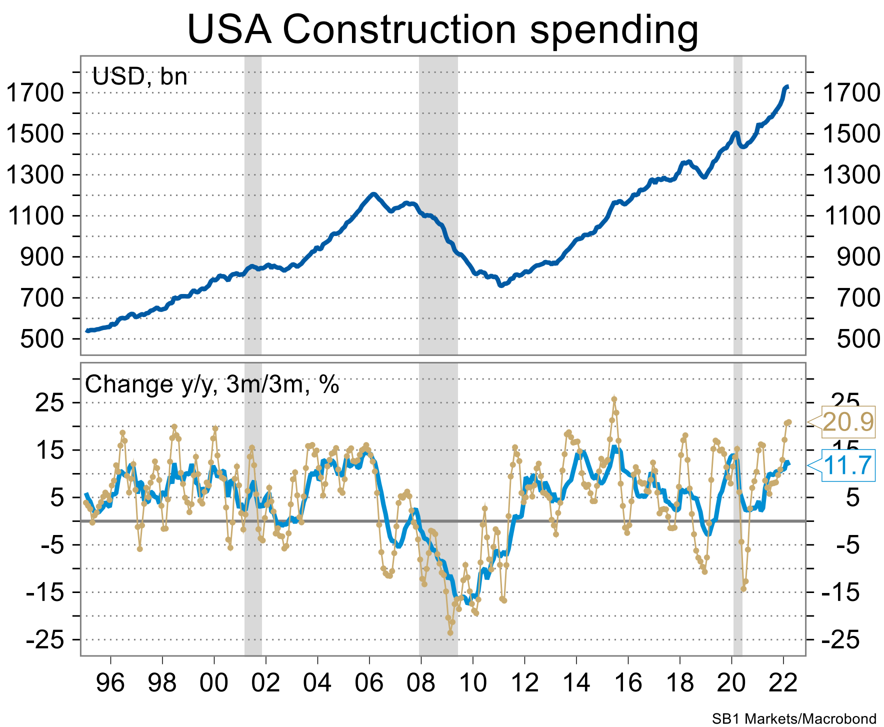
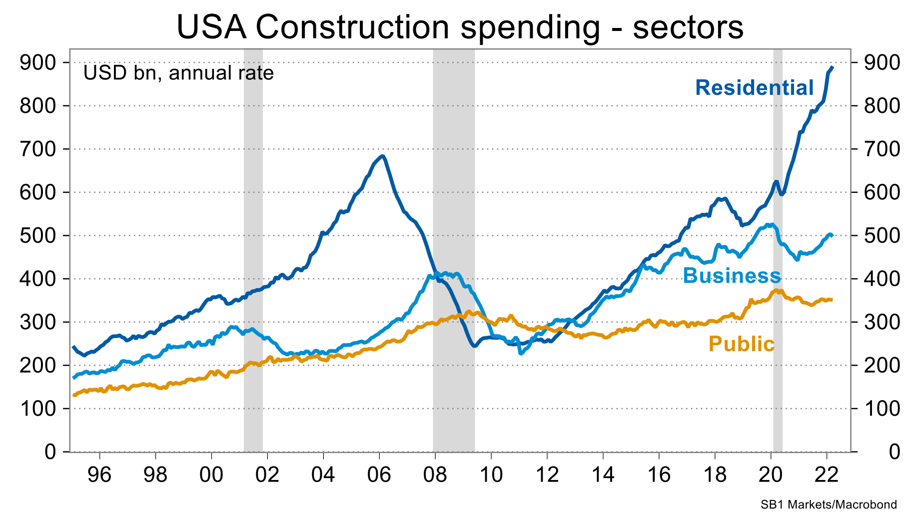
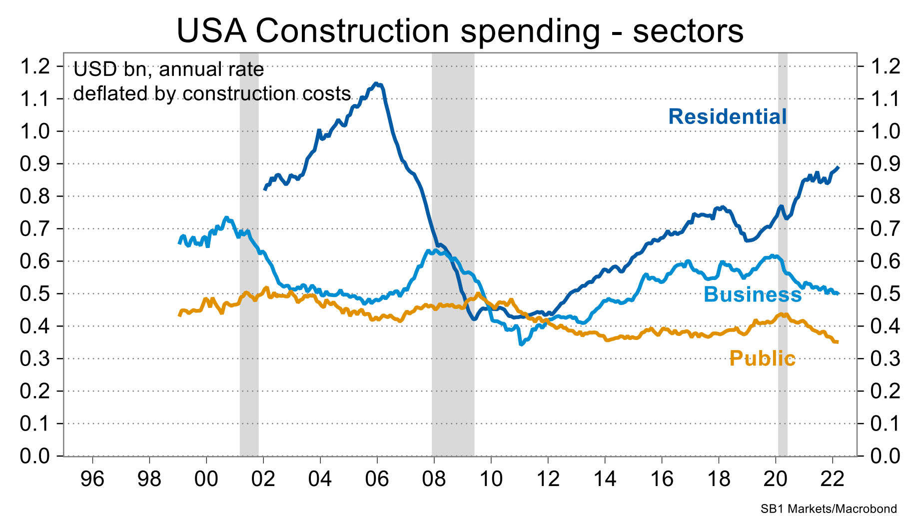
USA construction spending is growing rapidly, but not in real terms

Residential investments are surging in nominal terms, and are growing in real terms too



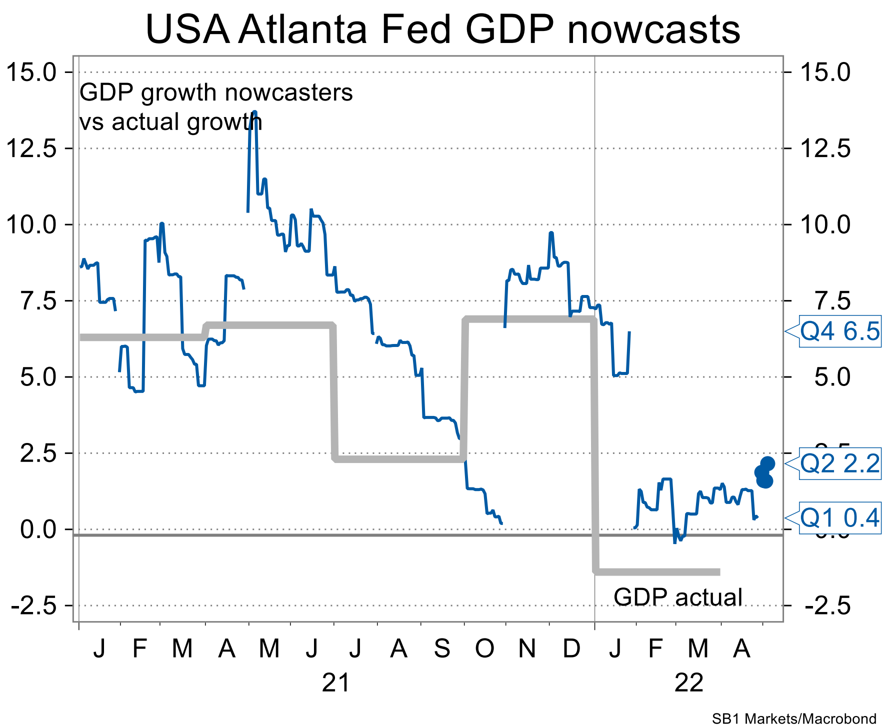


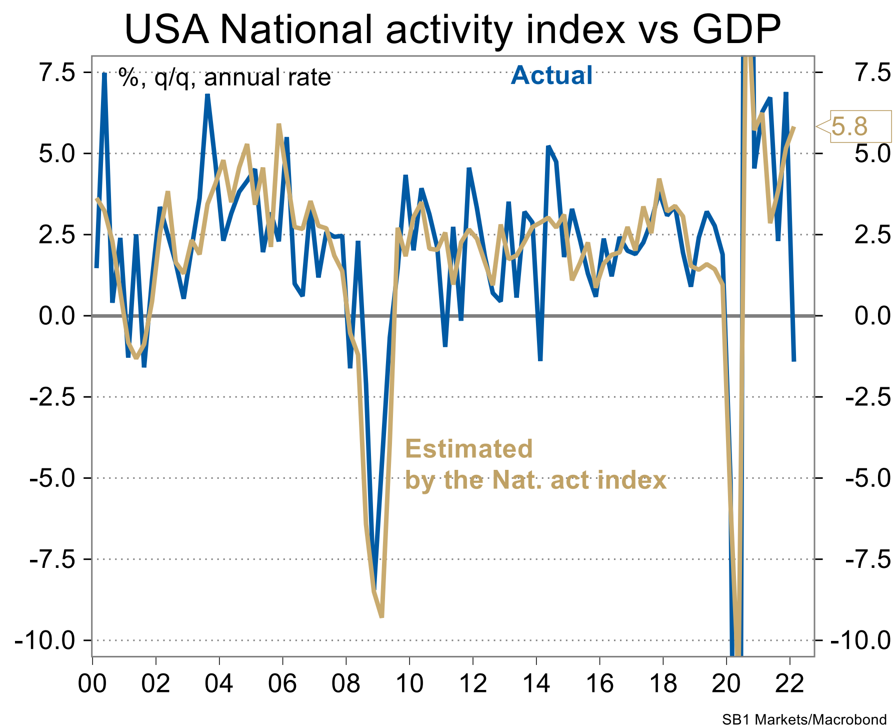


- Underlying growth is some 20% in nominal terms recent months but construction cost inflation is at the same level – and construction investments are trending down, at least business & public sector investments

Atlanta Fed's nowcaster suggests 2.2% growth in Q2, the Nat. Activity index 6%

Q1 was far weaker than expected and signalled by other data

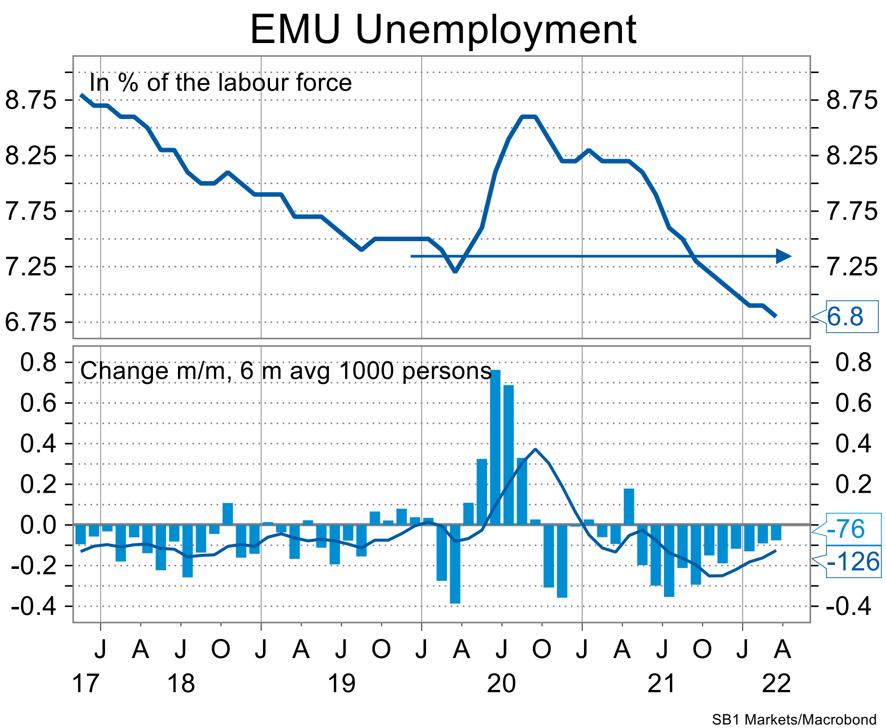


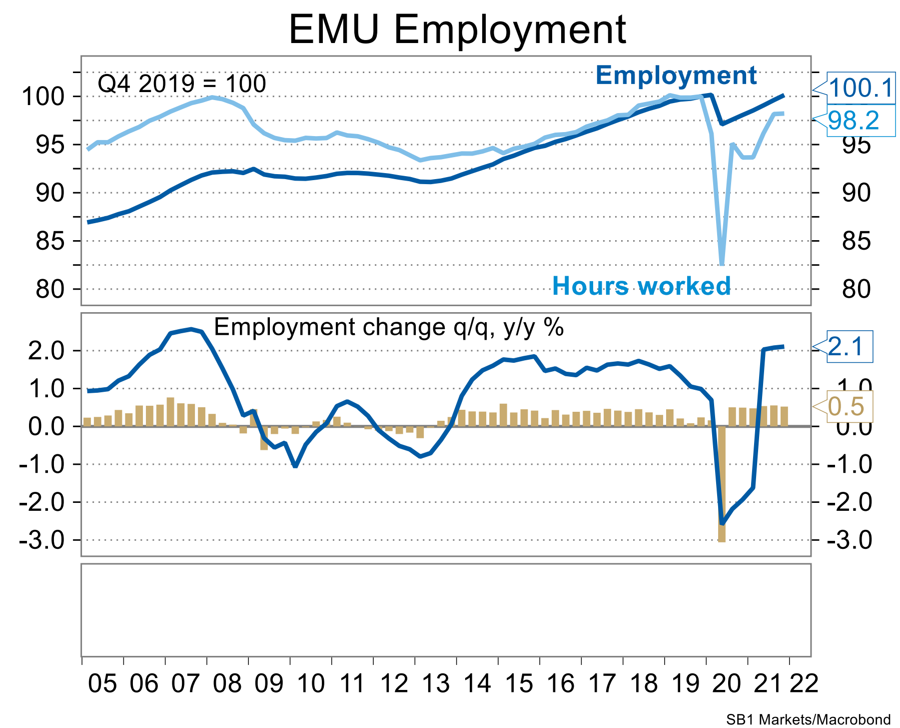


- **The National Activity Index** reported strong growth in Q1, a 5.8% pace – and growth was more than OK in March too, signalling substantial growth into Q2

Unemployment on the way down, the rate is the lowest since 1981

The unemployment rate (for the 3rd time…) down 0.1% to 6.8%. The speed of decline is abating

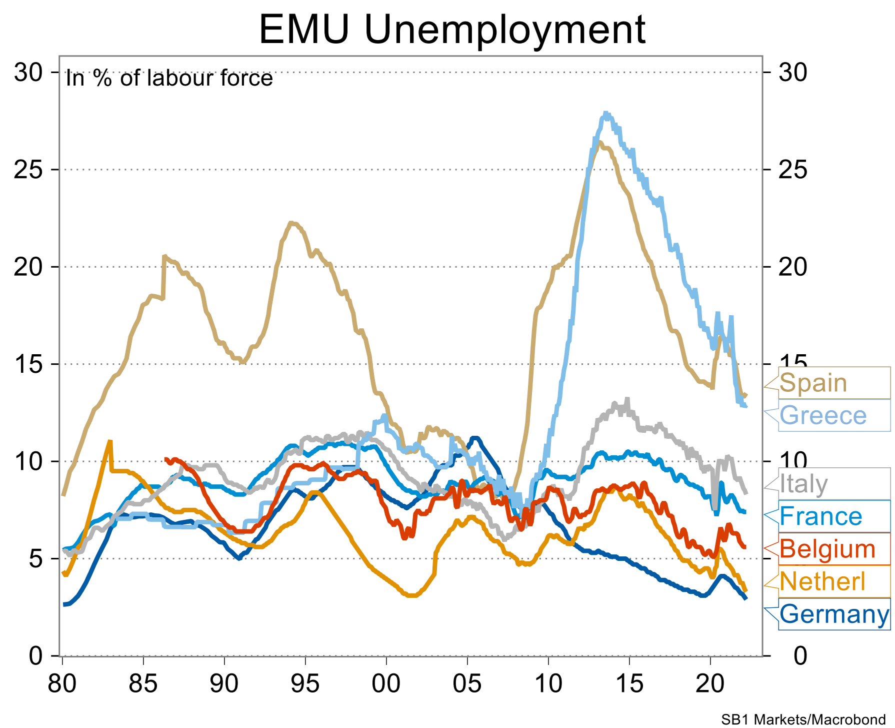


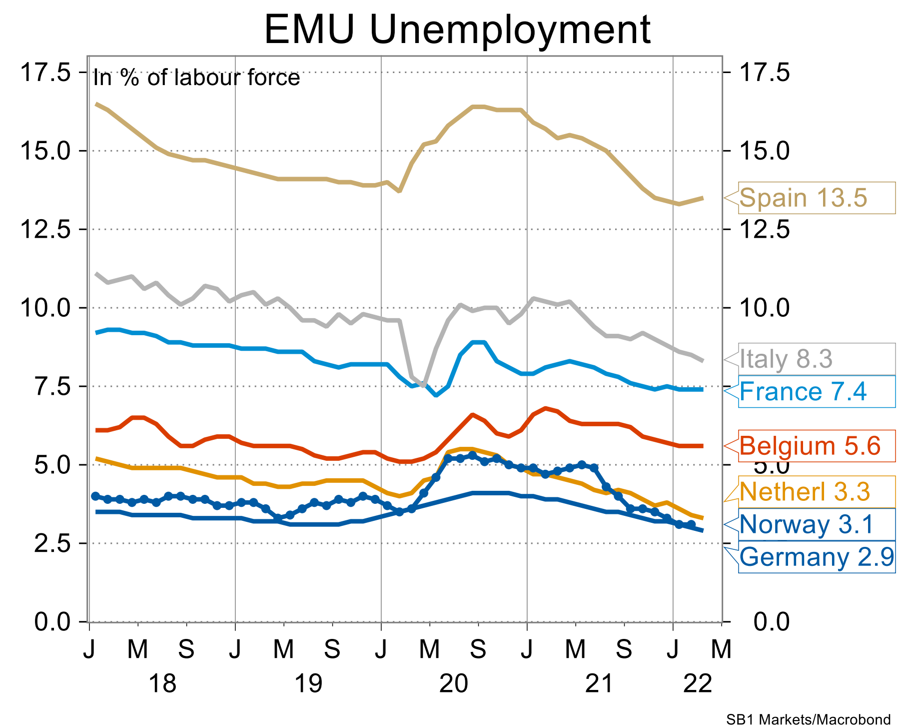


- **Unemployment** has been falling rapidly since last spring. In March, the unemployment level fell by 0.1 pp, as expected, but from an upward revised level in February (like what was the case one month ago)
- **Employment** rose by 0.5% in Q4, as in the previous 4 quarters, and the level is 0.1% above the pre-pandemic level
  - » However, the best proxy for **demand for labour**, is the number of **hours worked**. In Q4, hours worked was unch., and were down 1.8% vs the pre-pandemic level, as average working hours have fallen
- The number of **unfilled vacancies** has soared to the highest level ever, by far

Unemployment is declining all over the region…

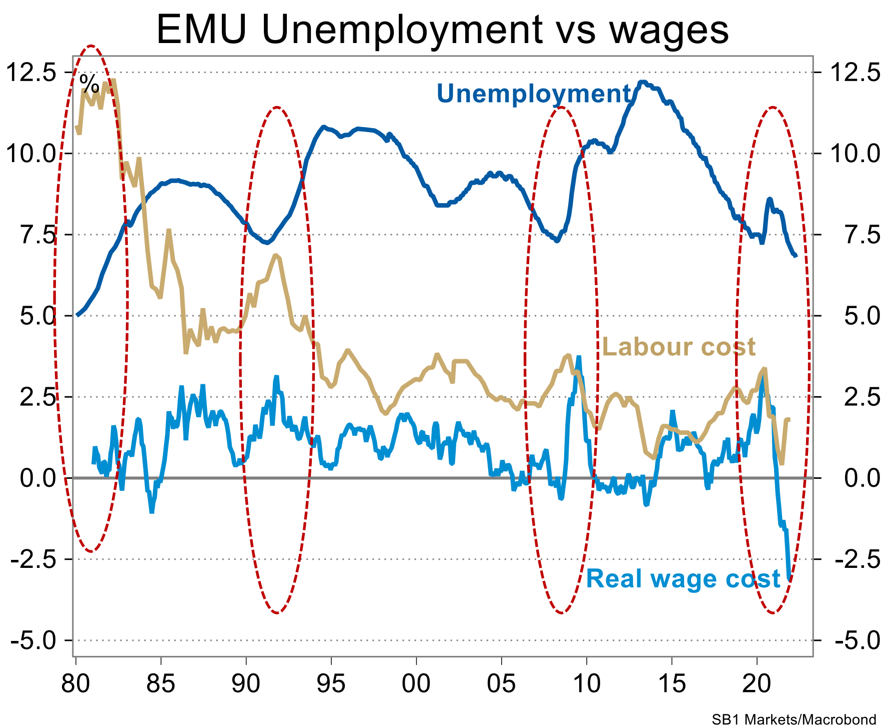
… But not in Spain over the past 2 months!

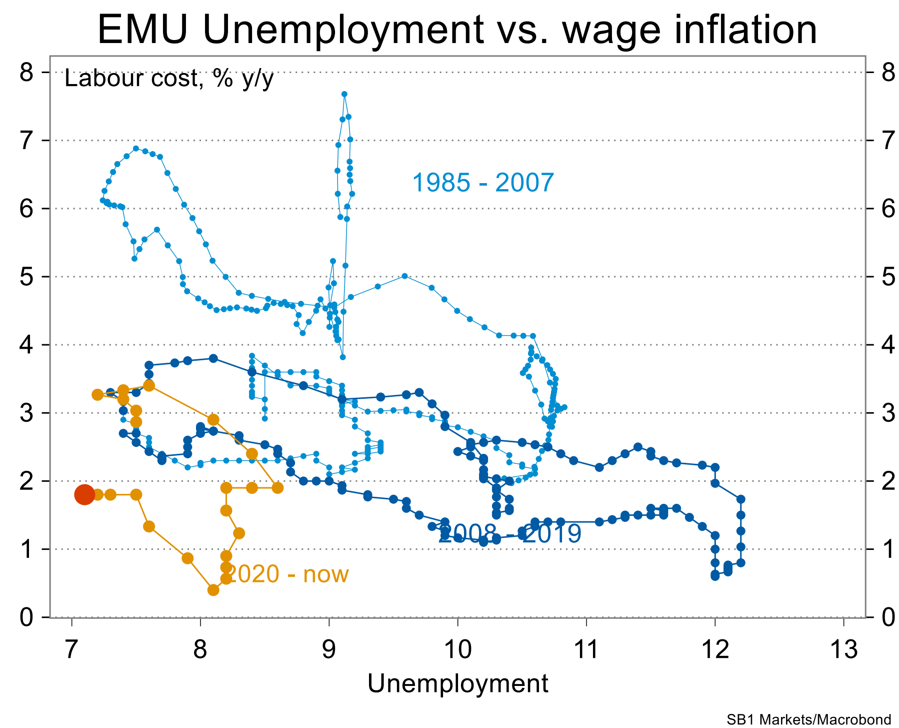




Unemployment is the lowest since 1981, vacancies are at ATH

There may be some wage inflation risk in the EMU too? So far, nothing is seen, wage inflation at 2.0%

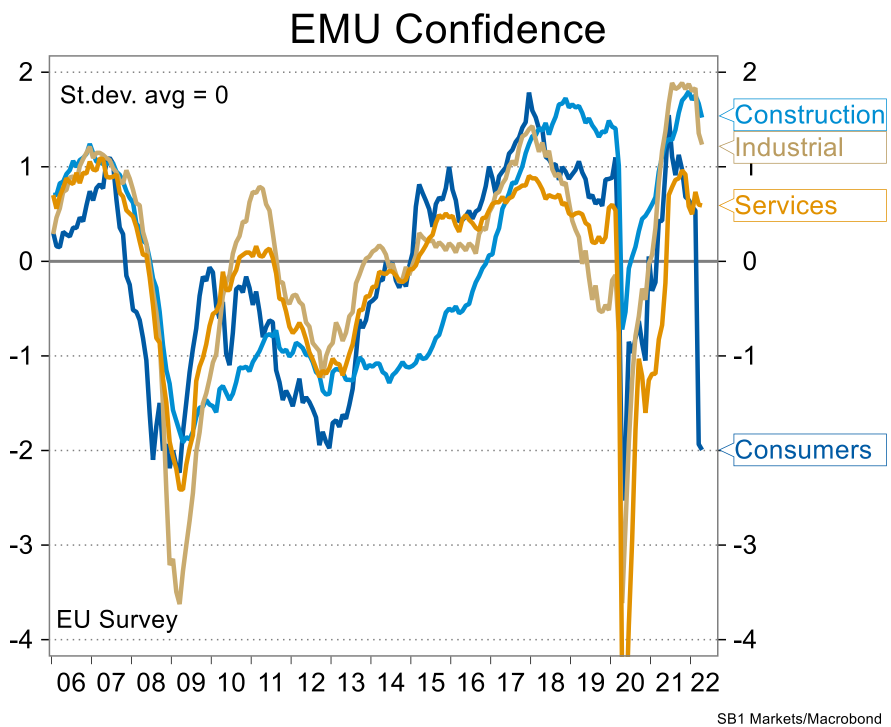


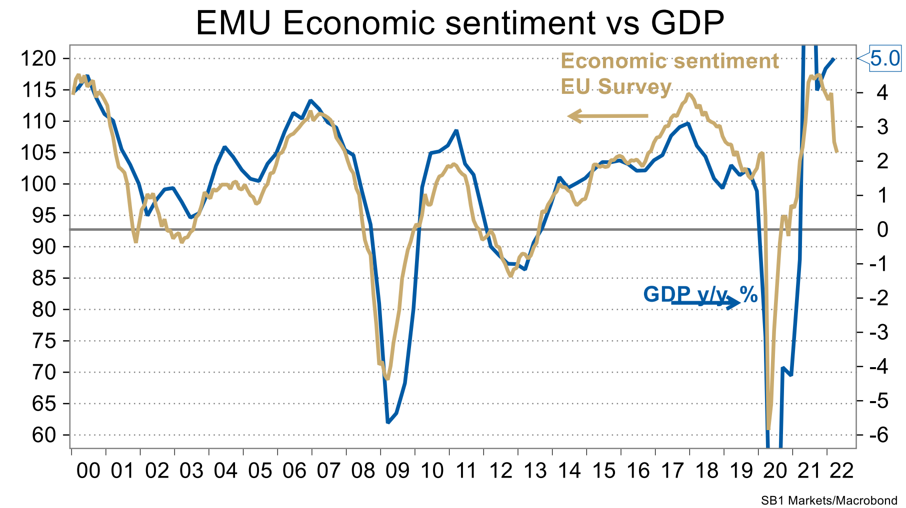


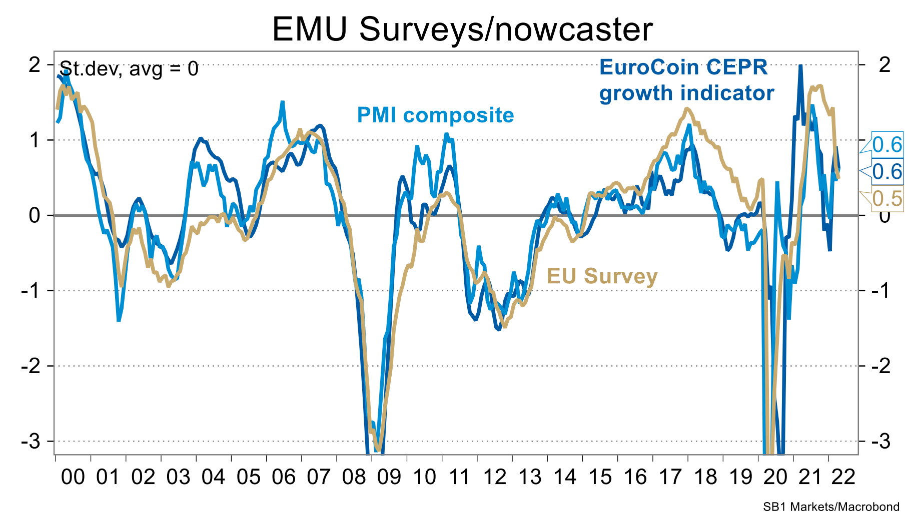
- A problem for the wage-earners: Wages are up 2%, while inflation is 7.5% - and real wages are collapsing

Households are still terribly negative, businesses sentiment down but not weak

EMU economic sentiment fell 0.5 st.dev, but remains 0.8 above avg, signalling 3% growth



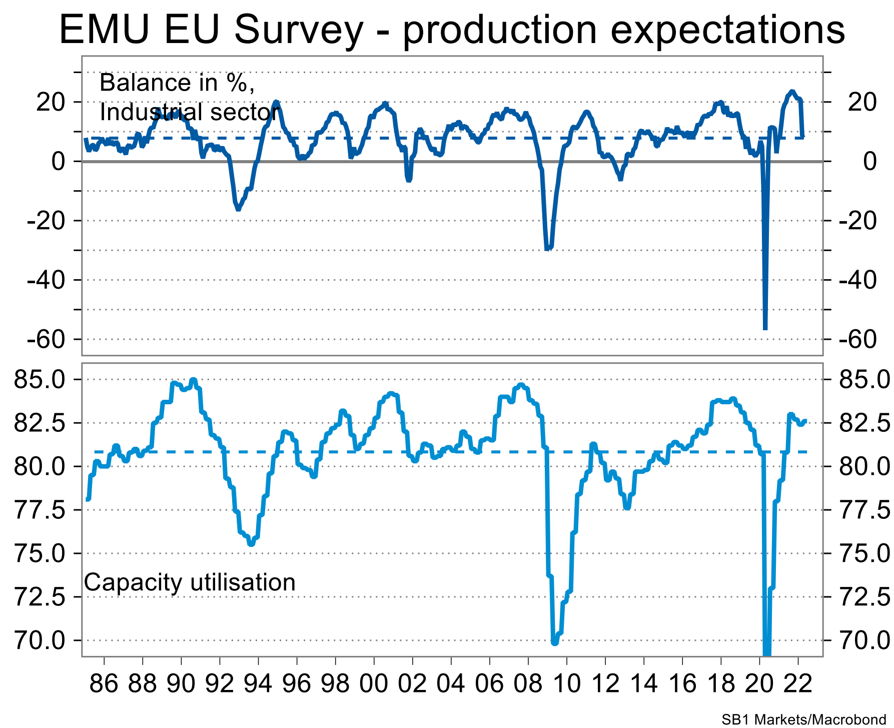


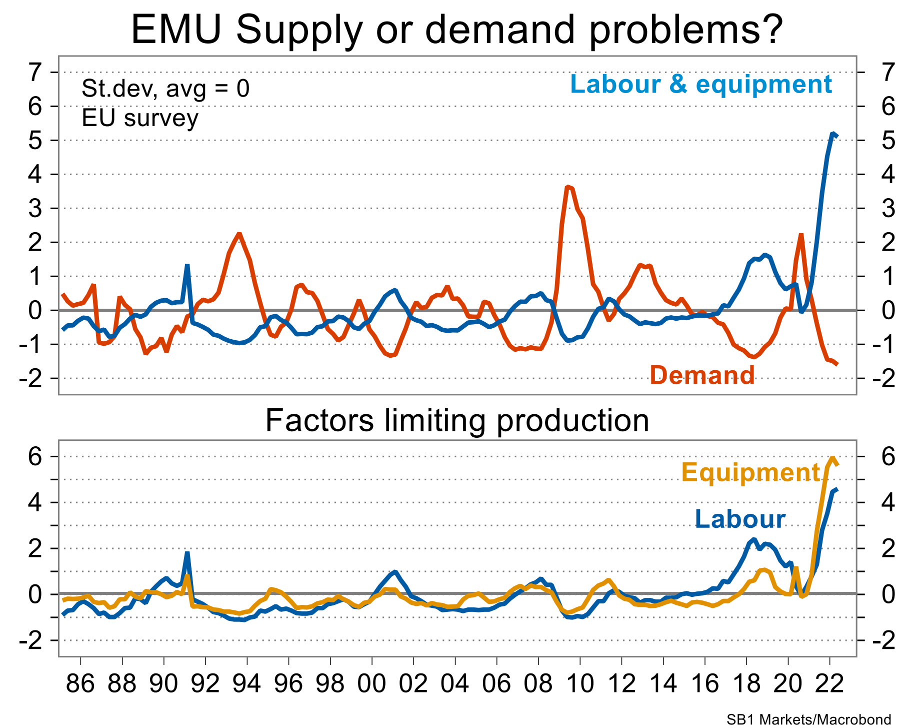


- **EU's confidence survey for the Euro area** declined 1.7p to 105.0, from a 2 pp downward revised level in March, expected down 0.5 p. The level is 0.5 st.dev above average, signalling a GDP growth above average, at some 2½%
  - » **Household confidence** was initially reported up in April vs March, but the final outcome was a further decline, to 2.0 st.dev below avg.
  - » **The industrial sector** reported a decline, but not by much, **construction** yielded, and **services** fell marginally, <u>and all remain well above a normal level</u>
  - » <u>Thus, war & sanctions have not yet scared businesses much at all</u>
- **The EuroCOIN GDP nowcaster** signals slower growth in line with EUs survey, as do the **PMI reports** – and all report growth above trend

Production expectations further and sharply down in April

Capacity utilisation well above average – and 'nobody' says demand limits production





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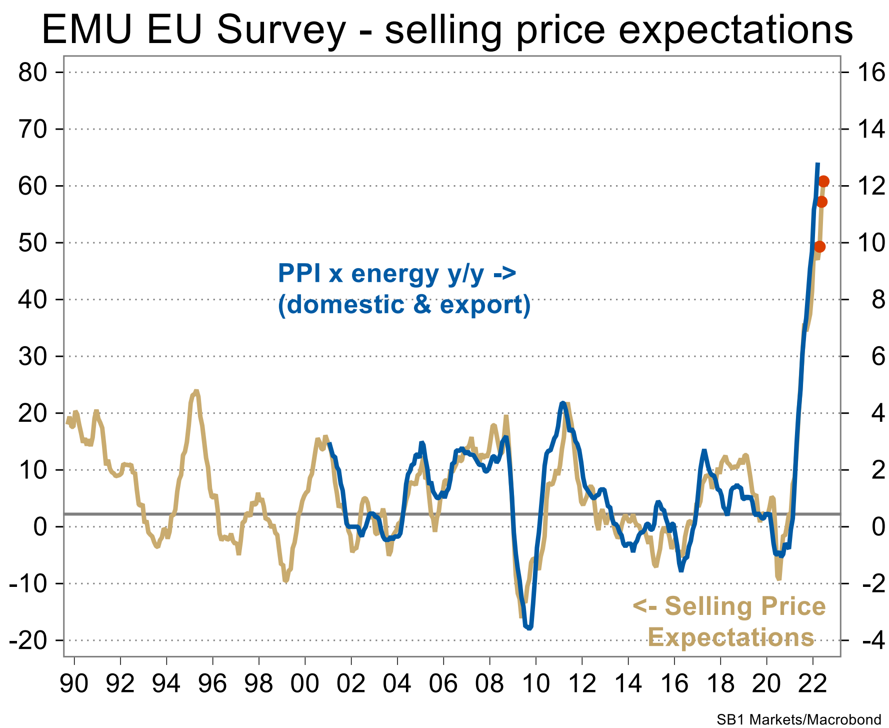
Companies report even steeper selling price increases

As cost pressures are building, and demand is still strong



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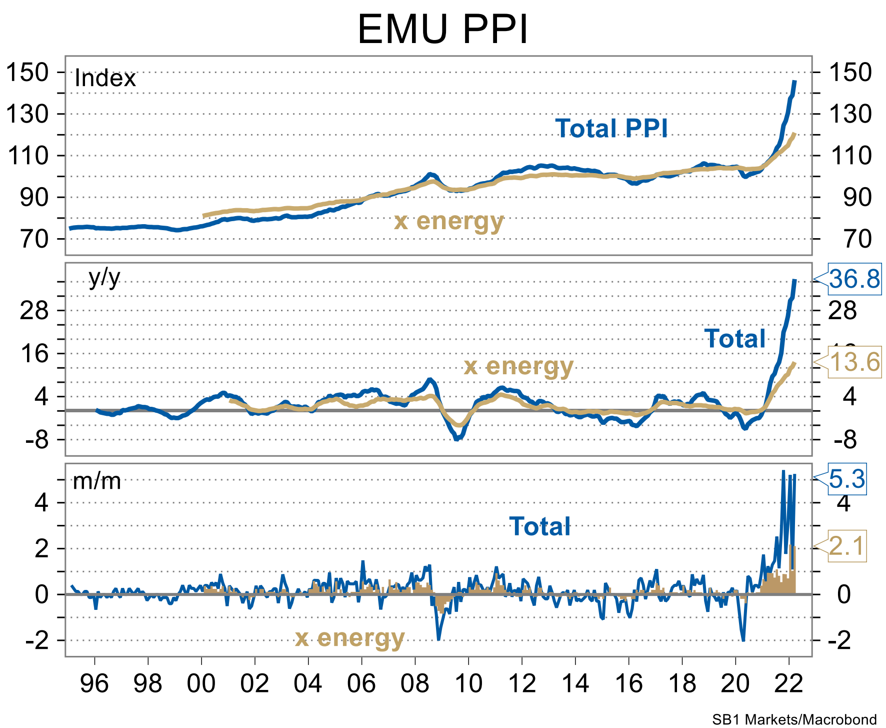
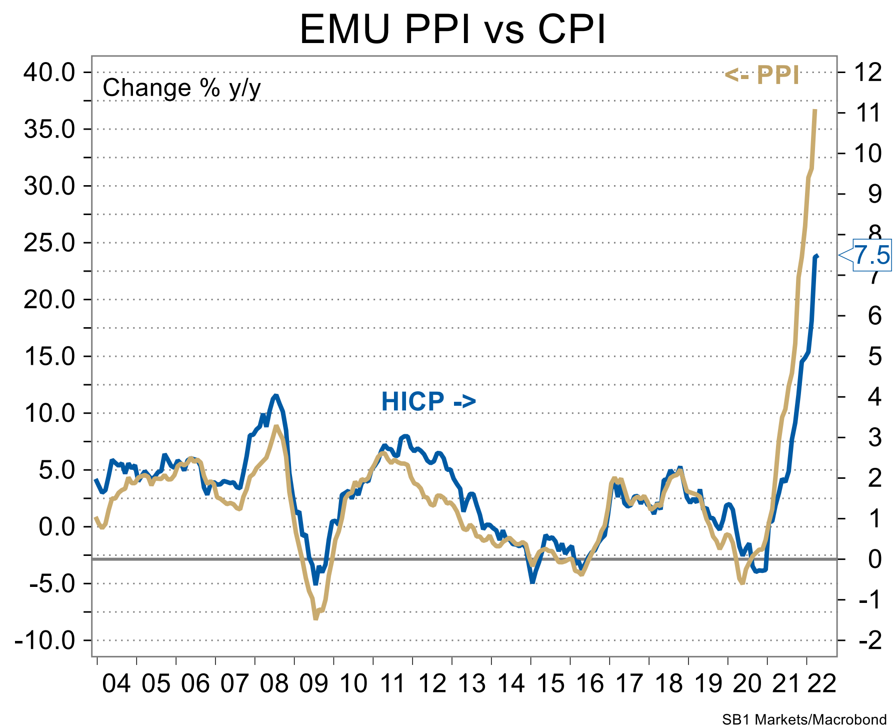
Producer prices up 37% y/y, all included. And 14% x energy

The total PPI rose 5.3% m/m in March, the core index added 2.1%, to the 2nd highest ever!

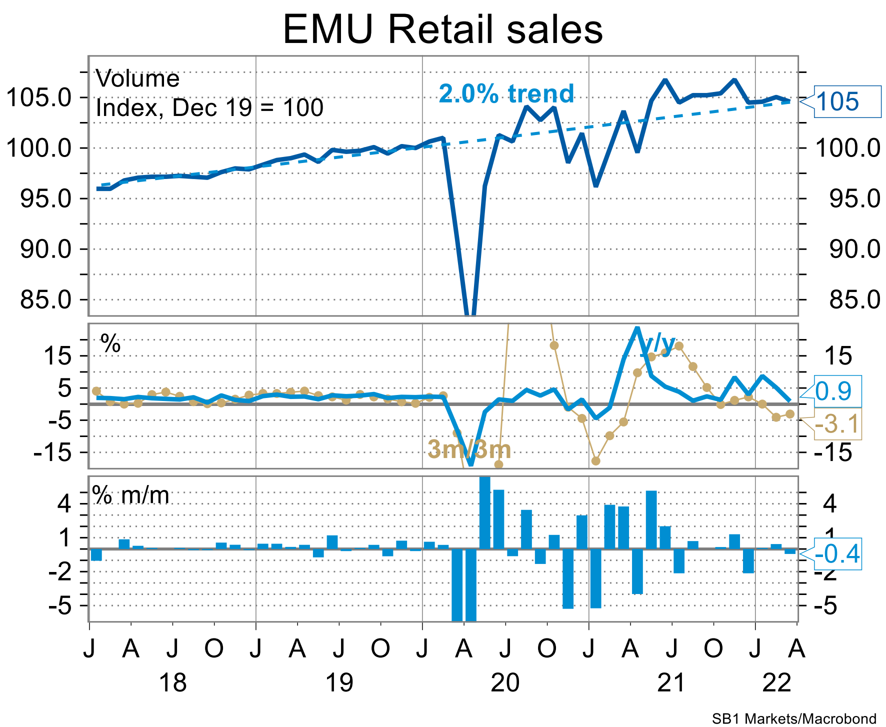


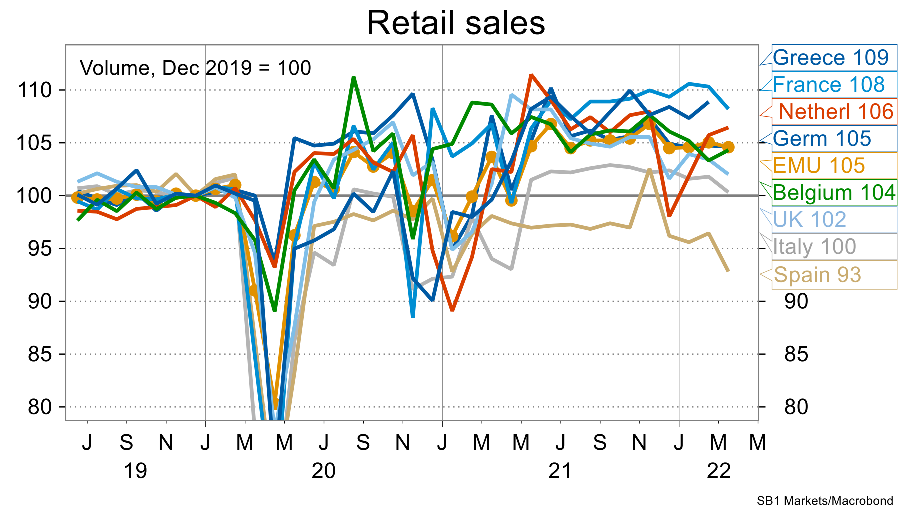


- No signs of lower inflation pressures here

Retail sales down 0.4% in March. Due to transfer of demand to gains in services?

Or fear of war? Spain the big loser, sales down in France as well. Sales flat in Germany

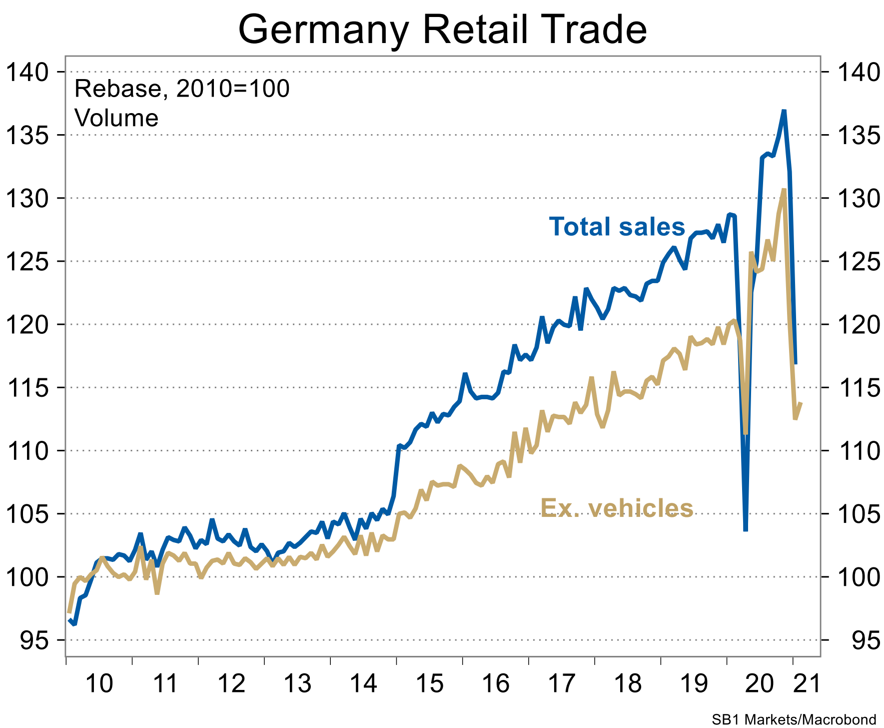


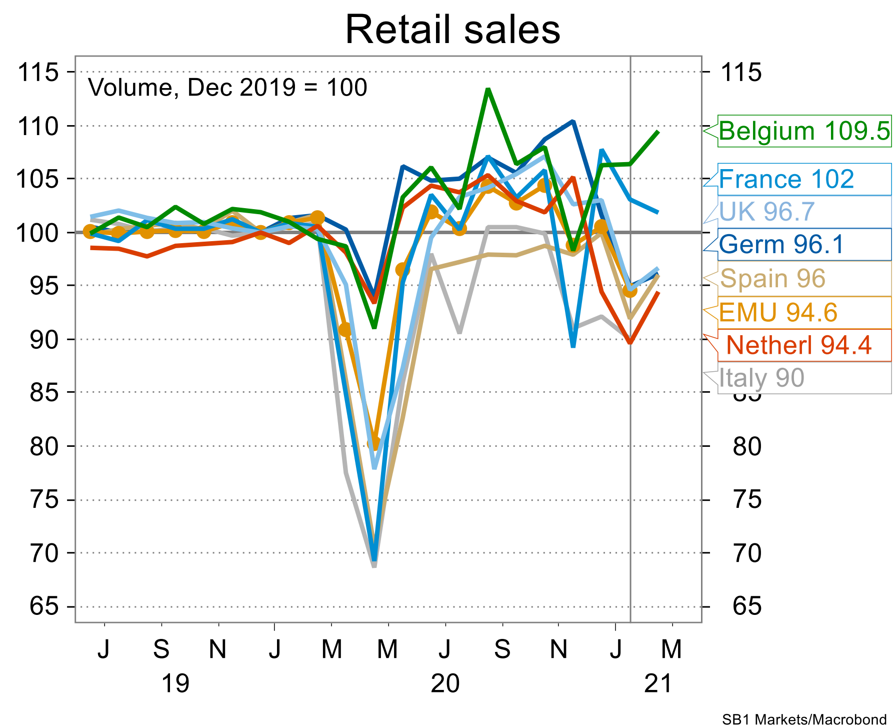


- Sales were expected down 0.1%
- Since before the pandemic: Sales are up 5%, and the level is close to the pre-pandemic growth path – signalling a limited downside risk (barring external chocks – and there are some around, like energy prices and war/sanctions

Retail sales up in February, but still very low during the last lockdown

Sales rose by 1.2% in Feb, expected +2%, following the almost 14% decline from Nov

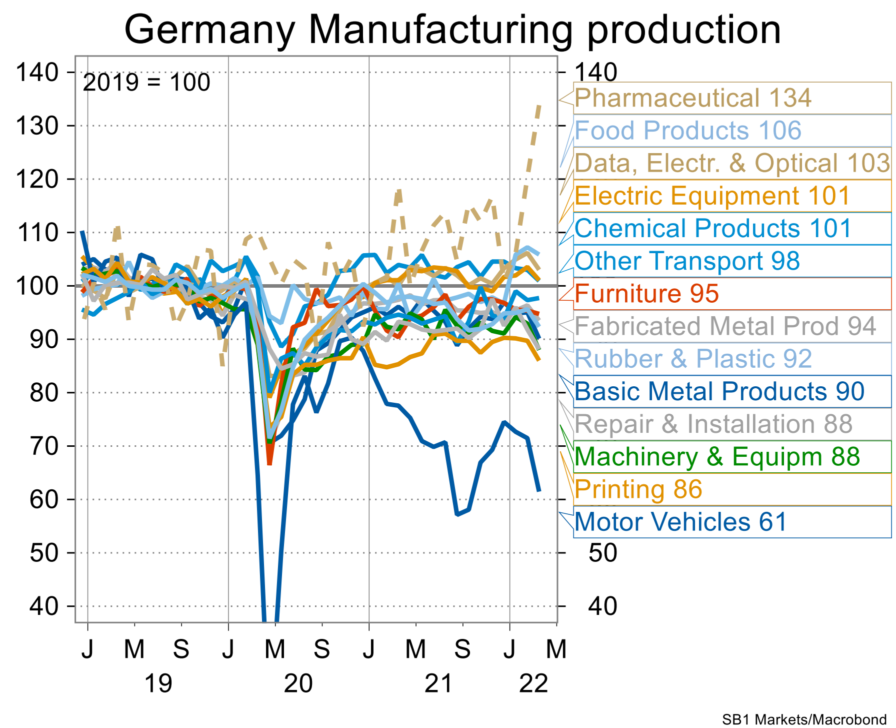




- The recent setback in sales is larger than during last spring – in Germany. Most other EMU countries were harder hit last year than they are now, as is the total Euro area

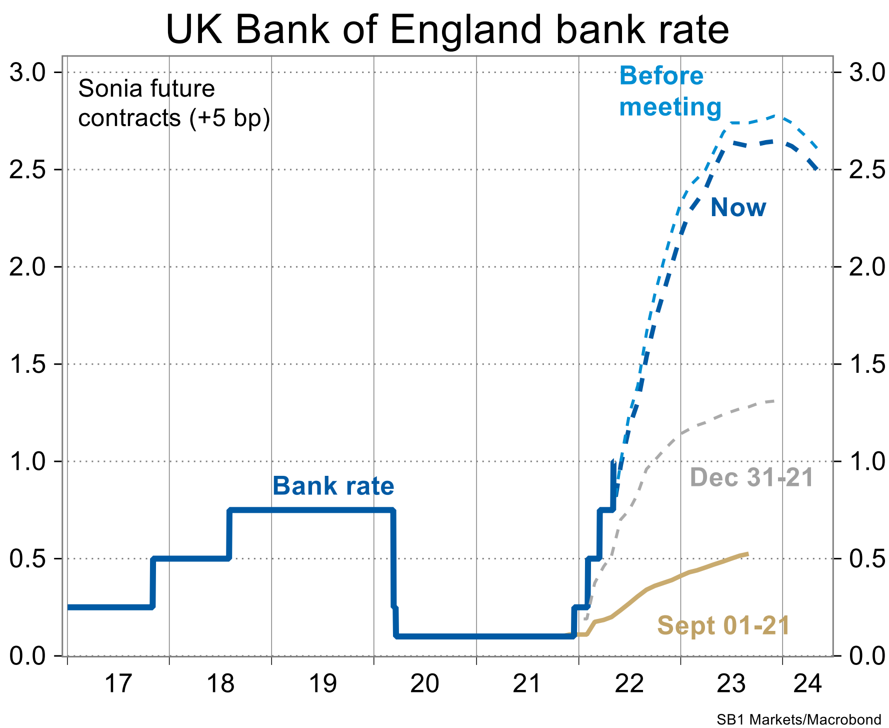
German factory orders down in March, alongside production

The auto sector is still the main drag – but the decline in March was rather broad, in sum 4.6%!



Bank of England: the 4th hike. Inflation may reach 10%. And then a recession?

The BoE once more less hawkish than expected: Still more hikes to come



- The bank rate was lifted by 25 bps to 1.00%, as widely expected
  - » 3 of 9 member voted for a 50 bps hike
- The Bank is in a squeeze: It expects inflation to accelerate further, though mostly due to higher energy prices that gradually feeds into the CPI though the semi-annual 'Ofgem' price cap adjustments, up to 10% in late 2022, 2 pp higher than the March forecast. The surge in inflation will reduce disposable income sharply, and the bank expects 'a very sharp slowdown' with a decline in GDP in Q4-22/Q1-23 (aka 'a recession'). Unemployment will increase from the current 3.8% (close to the lowest level since 1975) to 5½% in 3 years' time, and the output gap will turn negative
- After the current surge, <u>inflation is expected to decline to 2%</u> in two years' time, and to 1.3% in 3 years
- Still, the Bank hiked the signal rate, and expect some further hikes. On the other hand, the tone was somewhat dovish (a 'recession' was mentioned) and interest rate expectations fell slightly
- **QT:** BoE decided to start building down its holding of assets the bank built up during the QE programs (from August or later)
- The GBP fell 1.6% last week

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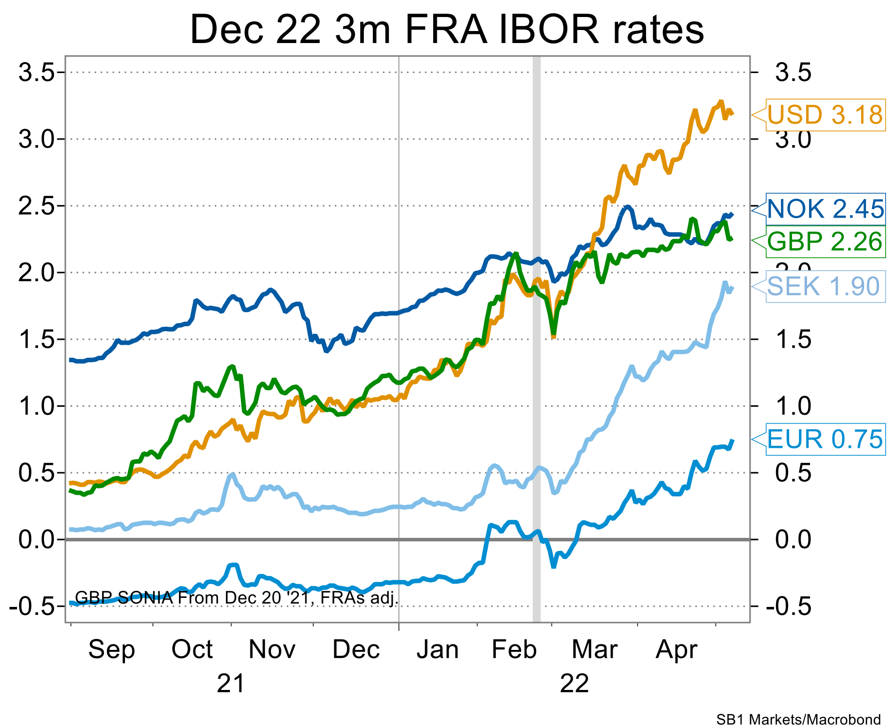
GBP FRA rates have flattened recently, while most others still are on the way up

The BoE lowered expectations slightly late last week



SpareBank 1 MARKETS

Highlights

The world around us

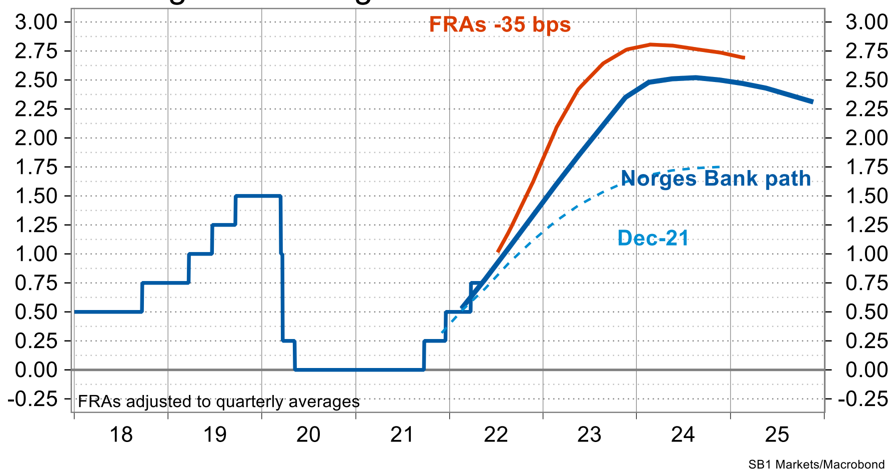
The Norwegian economy

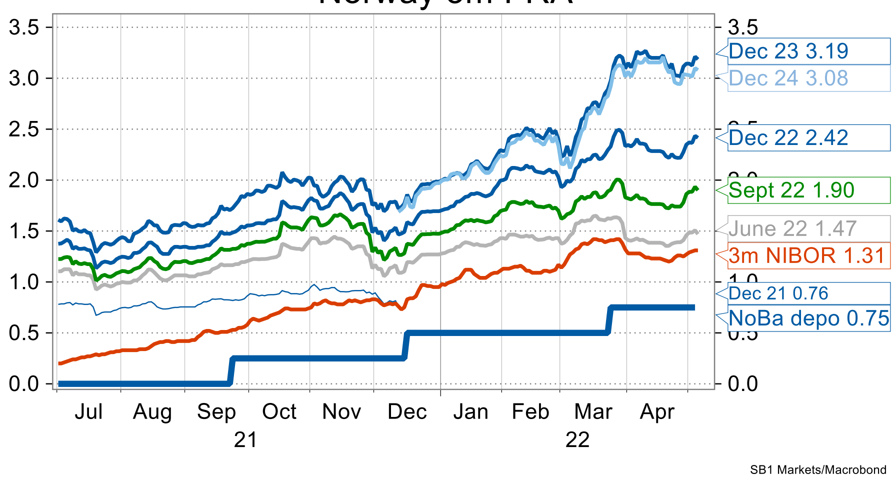
Market charts & comments

SpareBank 1 MARKETS

Norges Bank confirmed the plan, a next hike in June

The tone was still on the hawkish side, the bank repeats the domestic price/wage inflation risk





- **Key policy rate** was kept unchanged at 75 bps, as everybody expected
- Monetary policy is still expansionary, and there are not signals that the March MPR interest rate path is outdated
- The risks – both on the up- and downside
  - » Higher inflation and lower growth abroad due to the war in Ukraine
  - » Higher interest rates abroad may slow growth
  - » Risk of accelerating price and wage inflation in Norway. If there are prospects of persistently higher inflation, the policy rate may be raised more than quickly than indicated in the March MPR
- FRA-rates climbed last week, but not when NoBa published the press release from this 'mid' meeting
  - » The market probably discounts a small chance for a 50 bps hike in June or a hike at the August meeting
  - » The market is discounting a signal rate at close to 2% at the end of the year, well above NoBa's 1.5% f'cast, with a small probability for 1.75%

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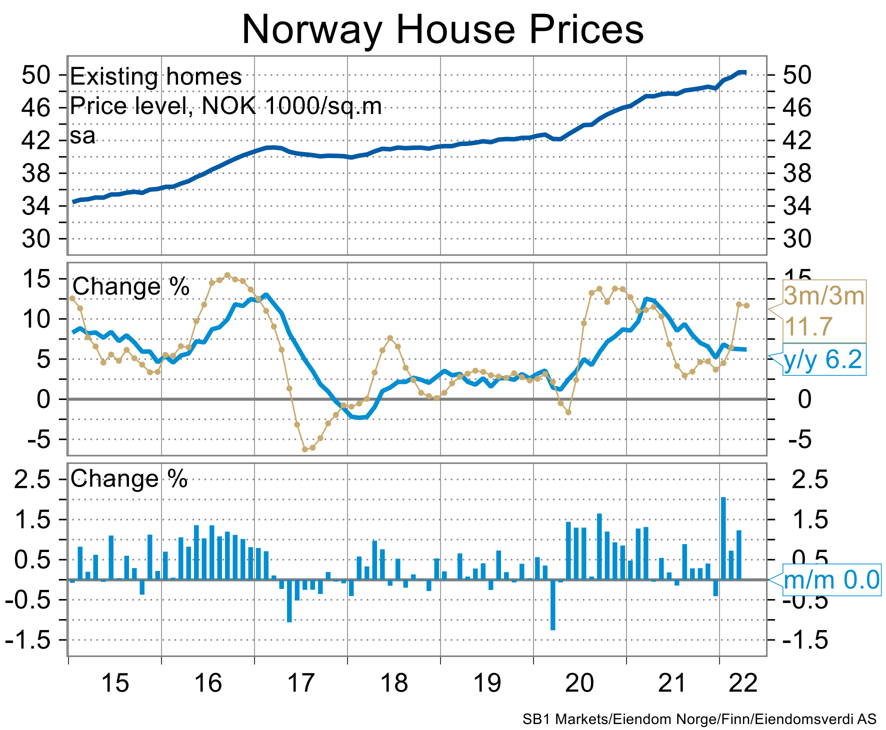
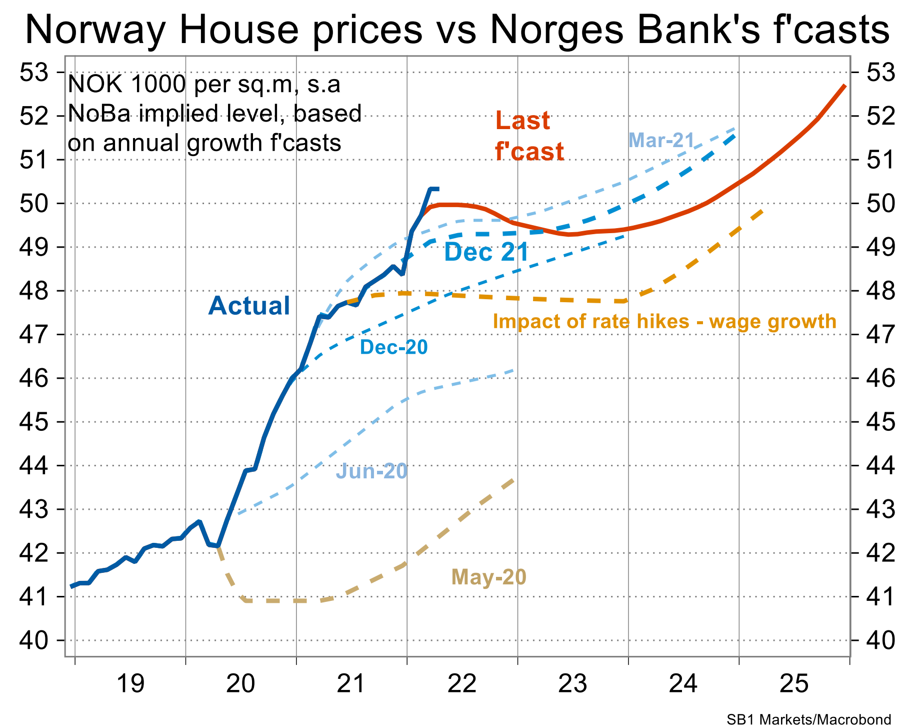
Finally, house prices flattened, but no. of transactions remained low, the inventory at ATL

Prices stabilised in April, following the 4% surge in Q1

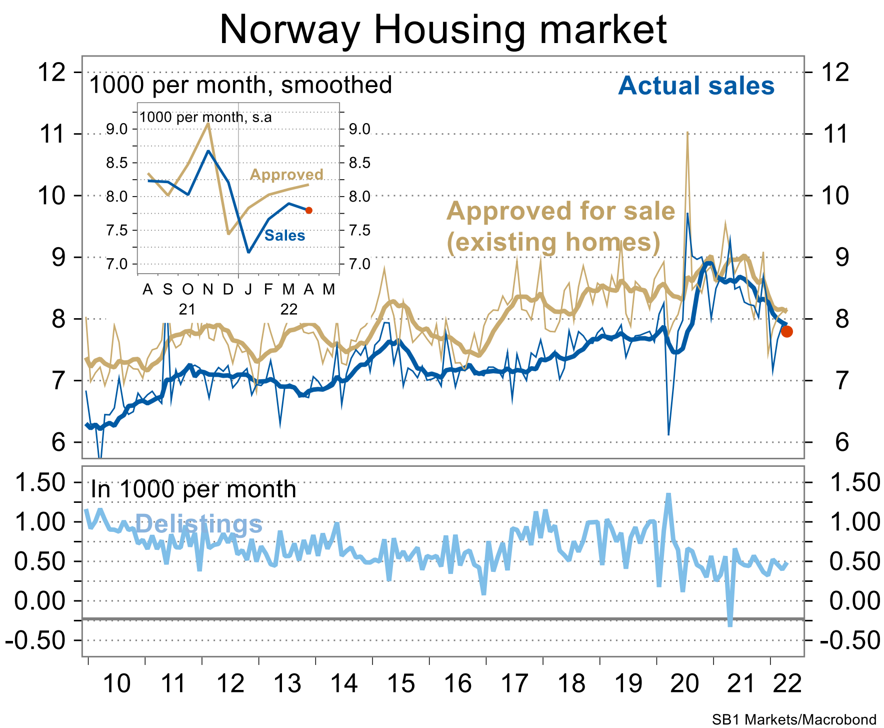


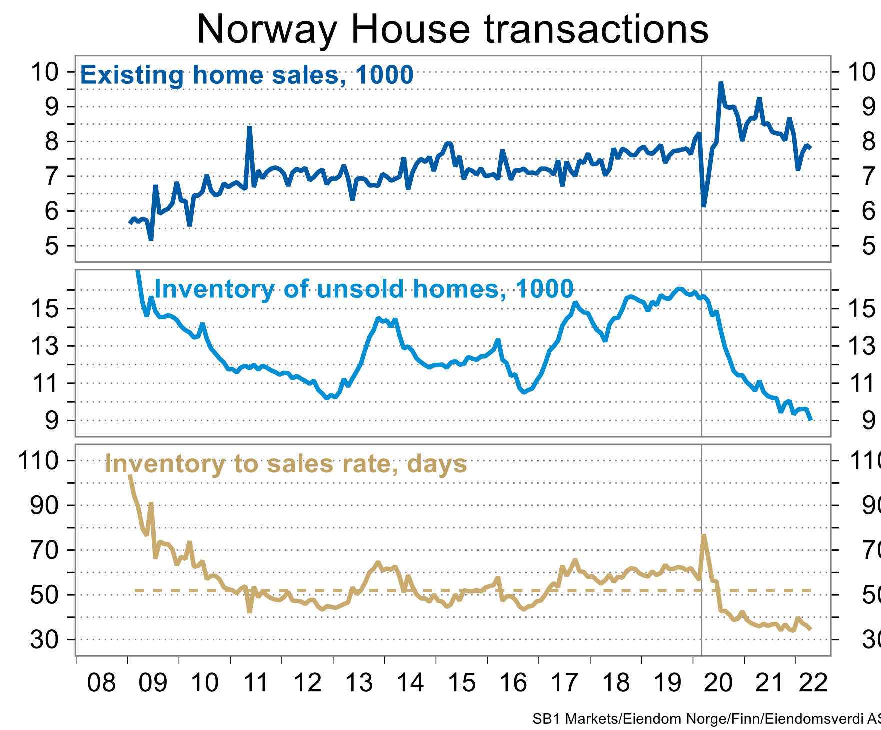


- **House prices** were unchanged in April (seas. adjusted., +0.3% unadj.), as we expected, following the 1.2% lift in March (revised from 1.0%). Norges Bank expected a 0.1% lift in April (and 0.4% in March). The number of transactions fell, is lower than 'normal', and the inventory is record low
  - » The surge in prices in Q1 was probably mostly due to lack of supply as a new law put up stricter requirements for technical valuation reports etc and thus fewer new homes for sale reached the market. Now, supply is gradually inching back to a normal level
- **Norges Bank** expects prices to flatten from here, and to decline marginally from Q3, before turning up again in H2 2023. In Q3 2024 prices are expected back to the H1-22 level.
- The impact on house prices from a 25 bps hike in the signal rate per quarter from Q3 last year adjusted for actual/expected growth in incomes, is illustrated at the chart to the right: the rate impact more or less equals the income impact, until the signal rate is assumed to flatten in 2024
  - » A 4% price elasticity vs. the interest rate is assumed, the coefficient is derived from NoBa's main forecast model. Wage growth 4%

The number of transactions down in April, more homes were approved

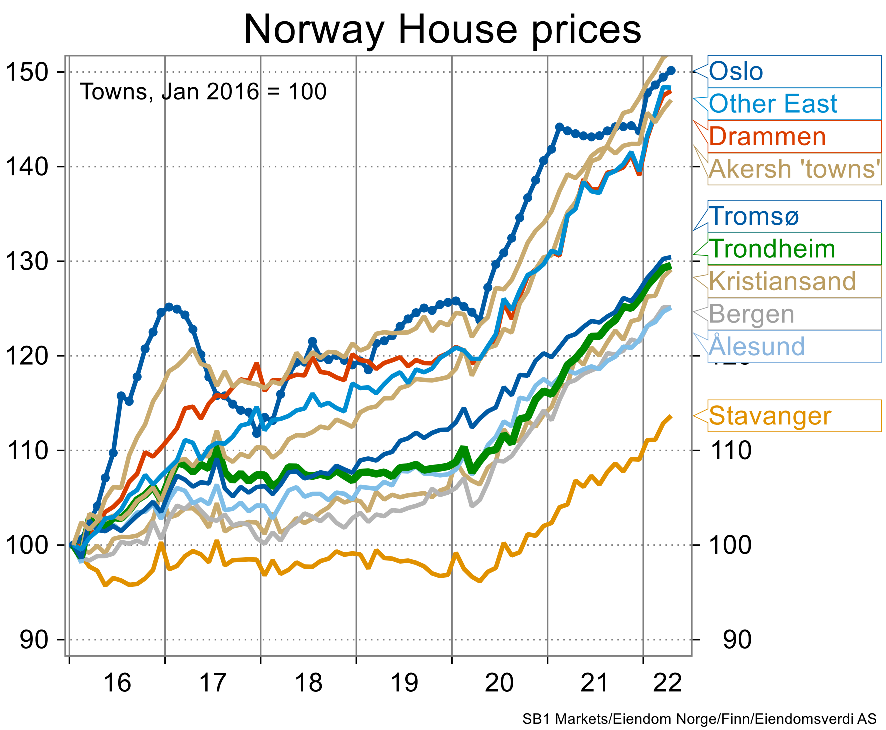
Still, the inventory of listed homes fell further, to ATL

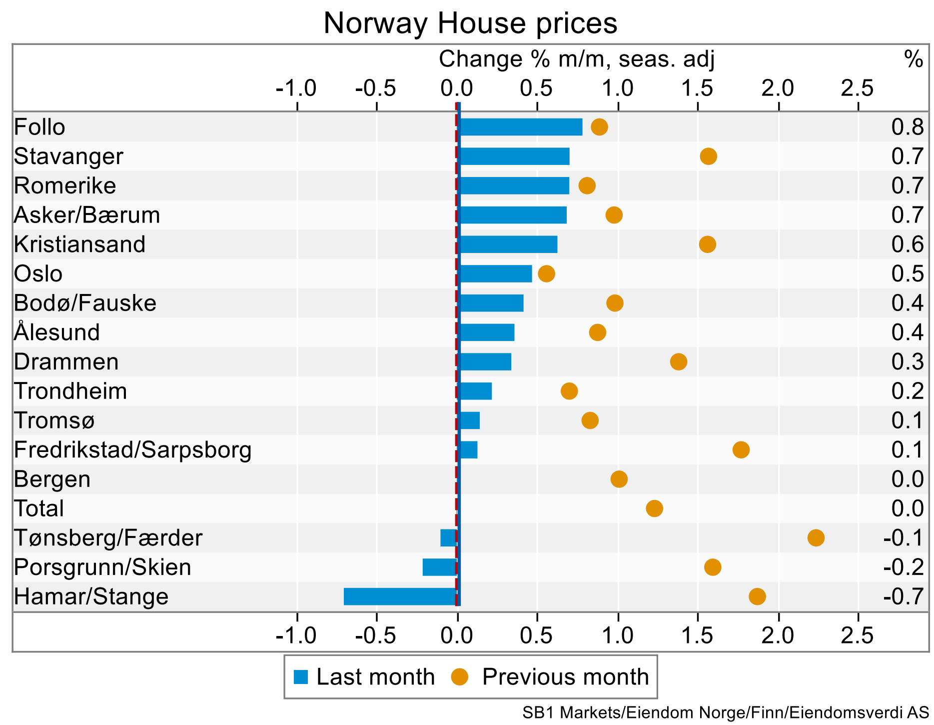




- **The number of transactions** has recovered somewhat following the large decline in January (new documentation requirements) but the level is still below normal, at least the normal during the pandemic
- The **supply of new existing homes for sale (approvals)** bottomed in December, and rose further in April. Still at a ‘low’ level
- The **inventory of unsold homes** declined in April, to the lowest level ever (since 2009, measured by this stats)
- The **inventory/sales ratio** declined 2 days to 34 days, vs an average at 52 days
- The **actual time on market** for those homes sold was unch. at 32 days, the fastest pace in almost 10 days (average 42 days)

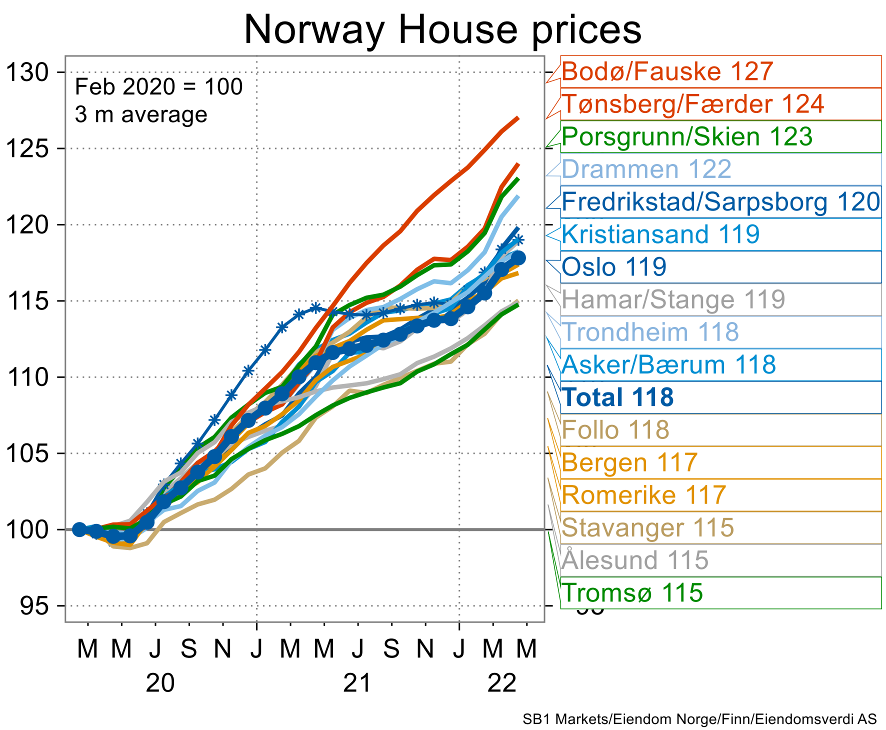
Most cities reported higher prices in April, just Hamar really declined

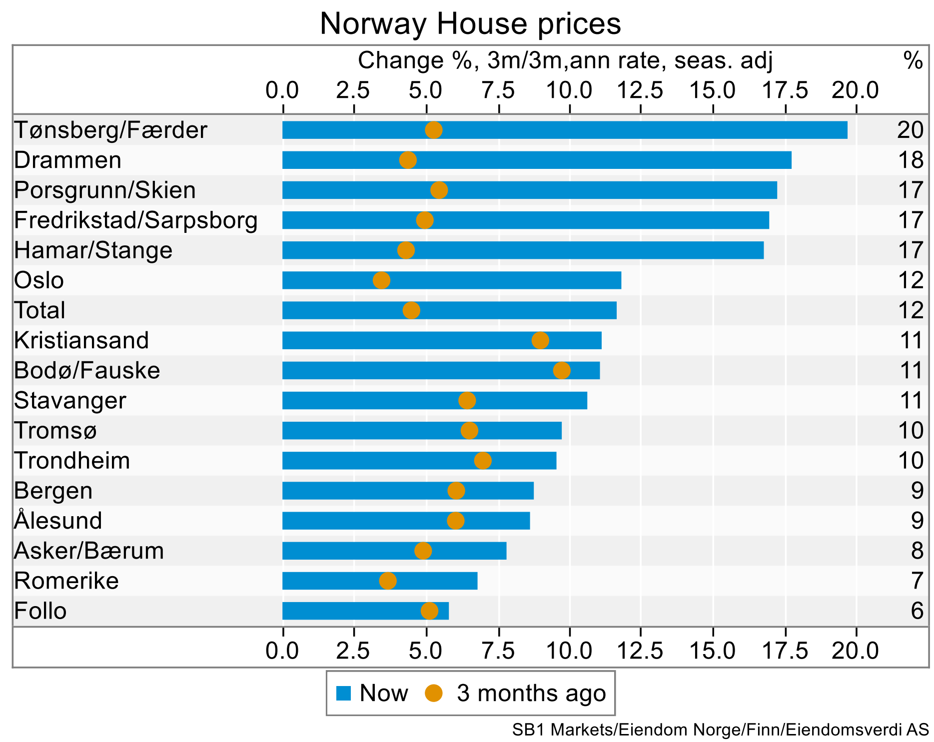




The big picture: Bodø still in the pole position but more cities are coming up

Bodø has lost some momentum vs. the rest of the country

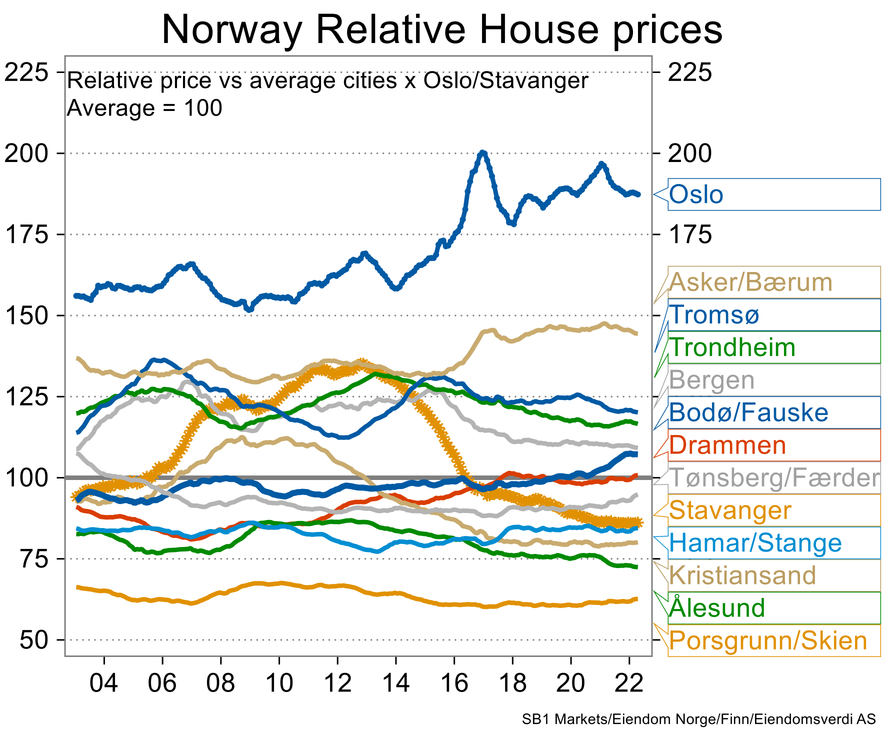


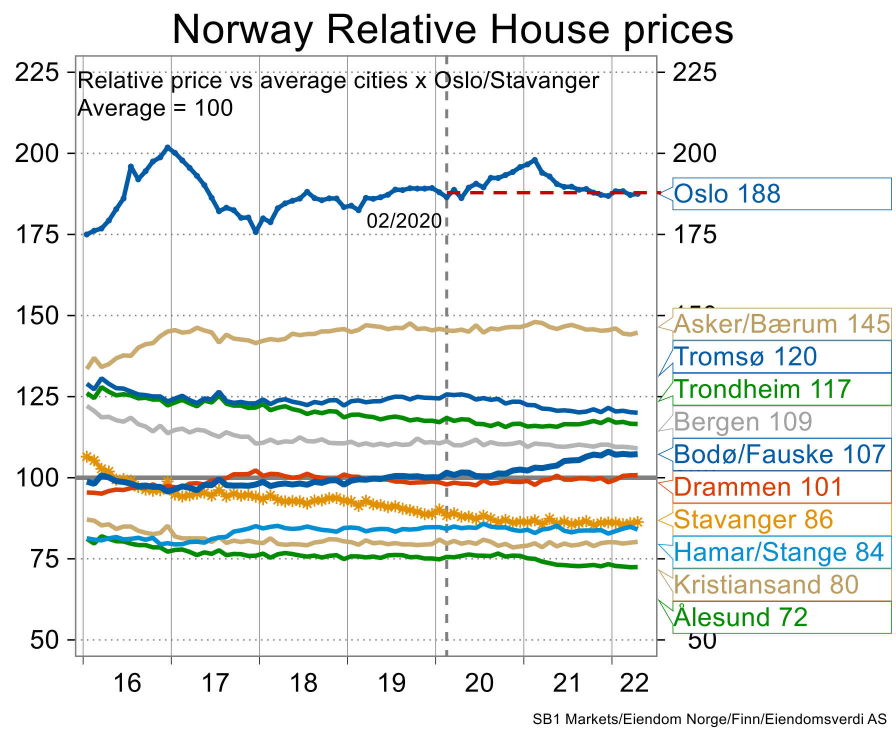


- Bodø the winner both since 2016 and early 2020
- After Bodø, eastern towns have been the winners since the start of the pandemic, Tønsberg, Porsgunn/Skien, Drammen and Fredrikstad/Sarpsborg, and prices are still climbing the fastest here
- Bergen, Stavanger, Ålesund and Tromsø at the bottom of the list (vs. early 2000)

Oslo relative prices close to the pre-pandemic level

Stavanger is still sliding down, as is Ålesund. Bodø the big winner, of course

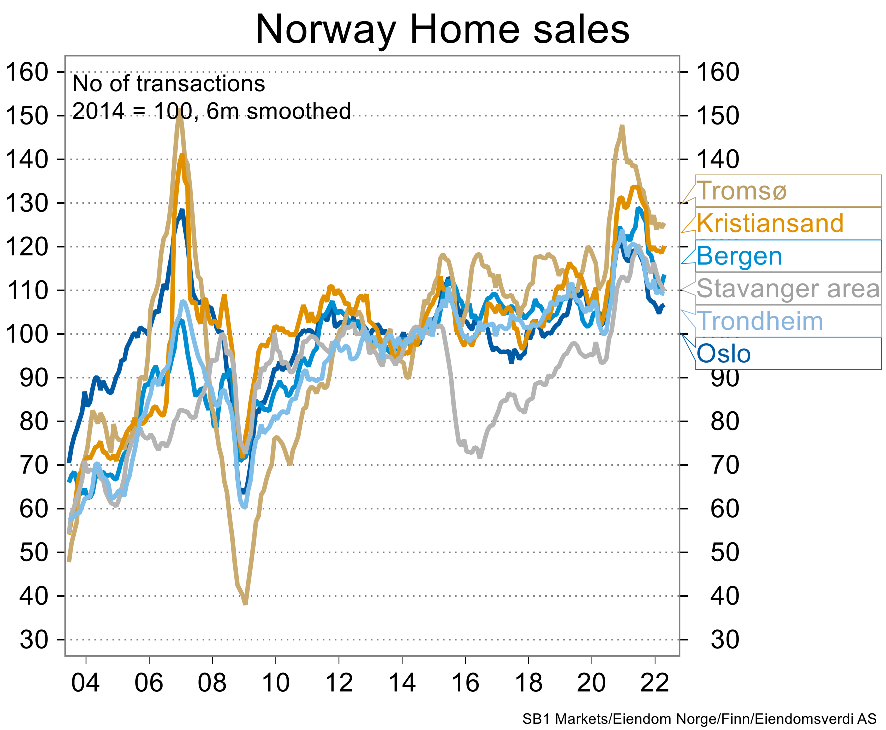


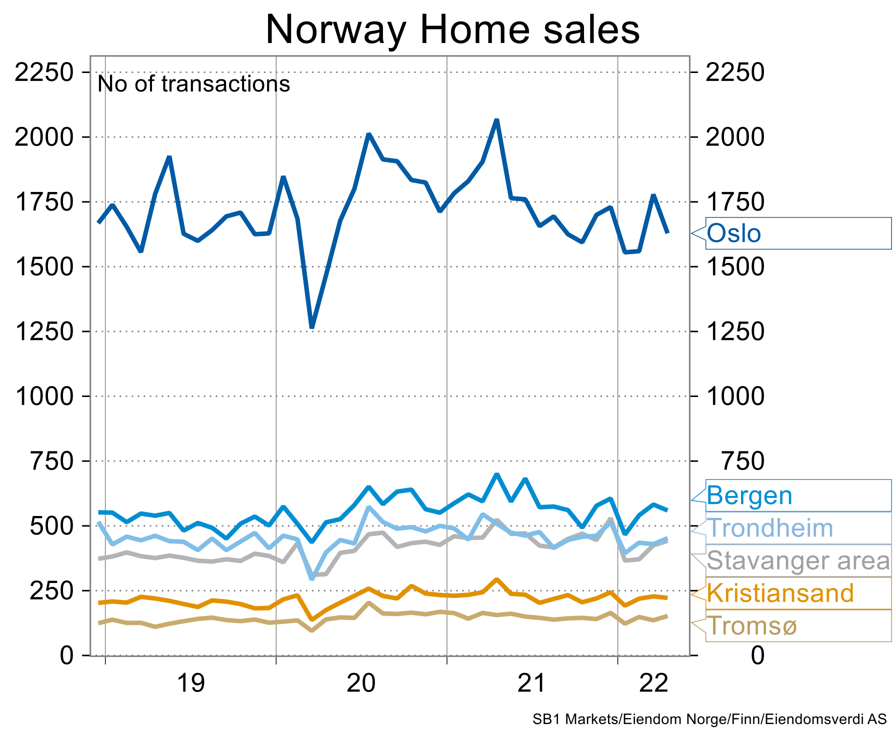


- Housing starts in Stavanger/Rogaland are still not lower than normal. It is still profitable to build, even at 'Hamar/Stange' prices! And why shouldn't it??

Number of transactions up in most cities in April

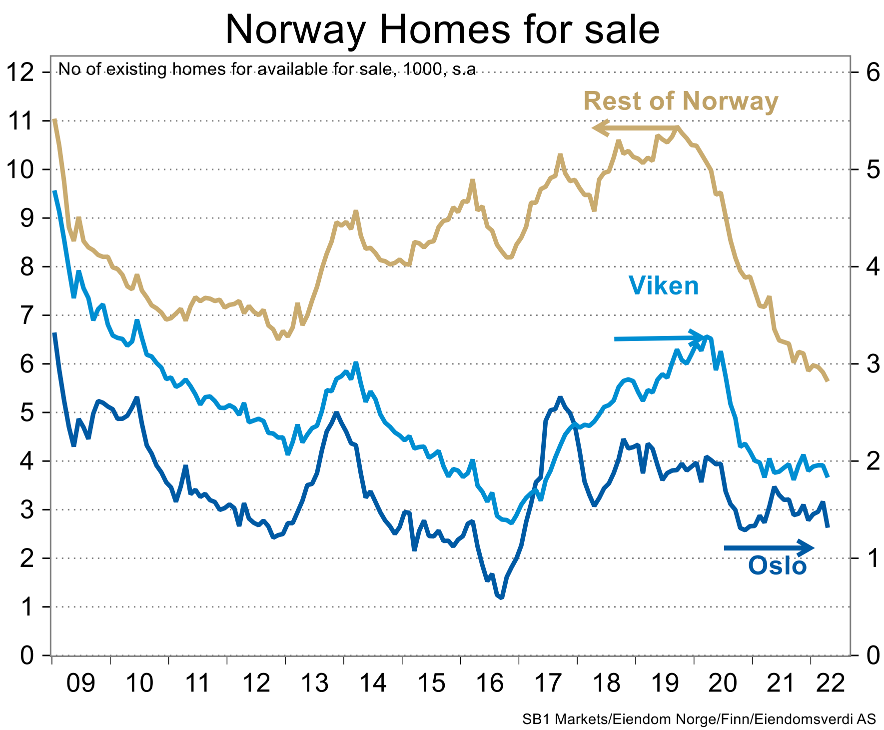
However, recent months have been lower than the previous everywhere

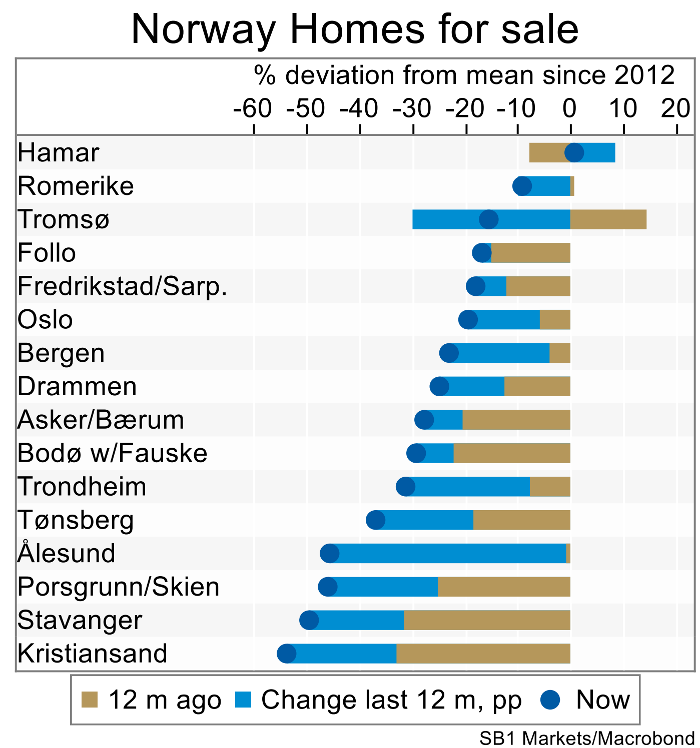




The inventory is lower than normal everywhere (except at Hamar)

..and it is falling everywhere (except at Hamar)

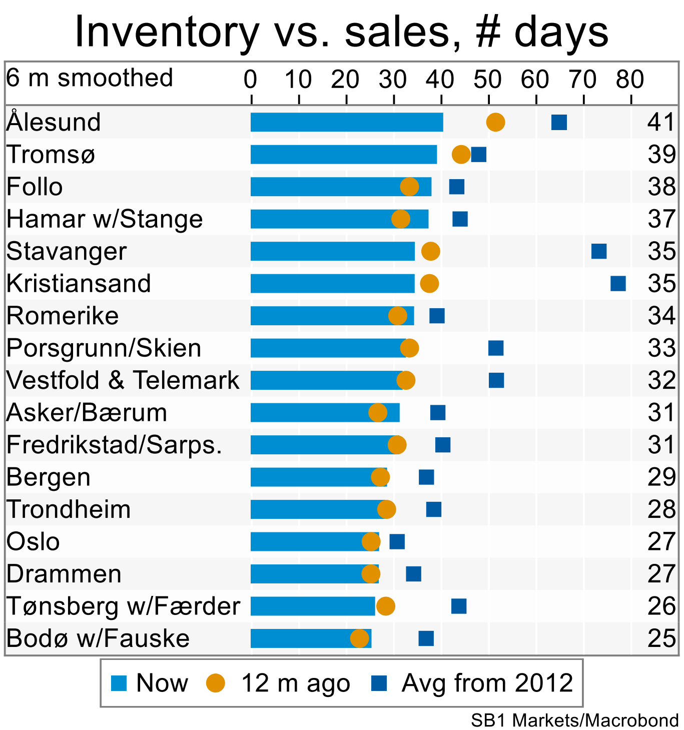




- Ålesund and Tromsø are reporting the steepest decline in homes for sale

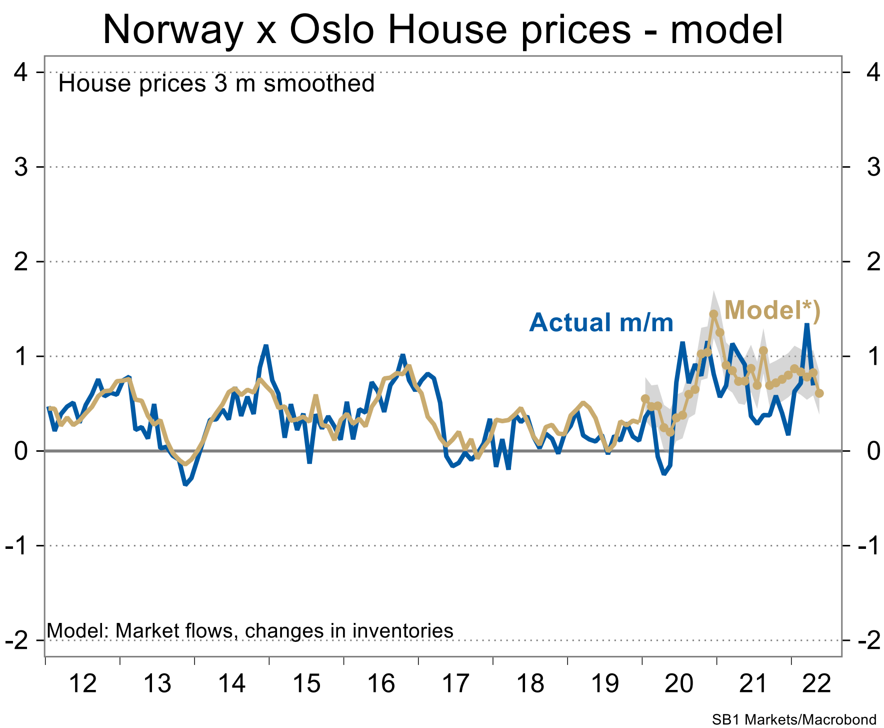
The inventory is turned around faster than normal everywhere

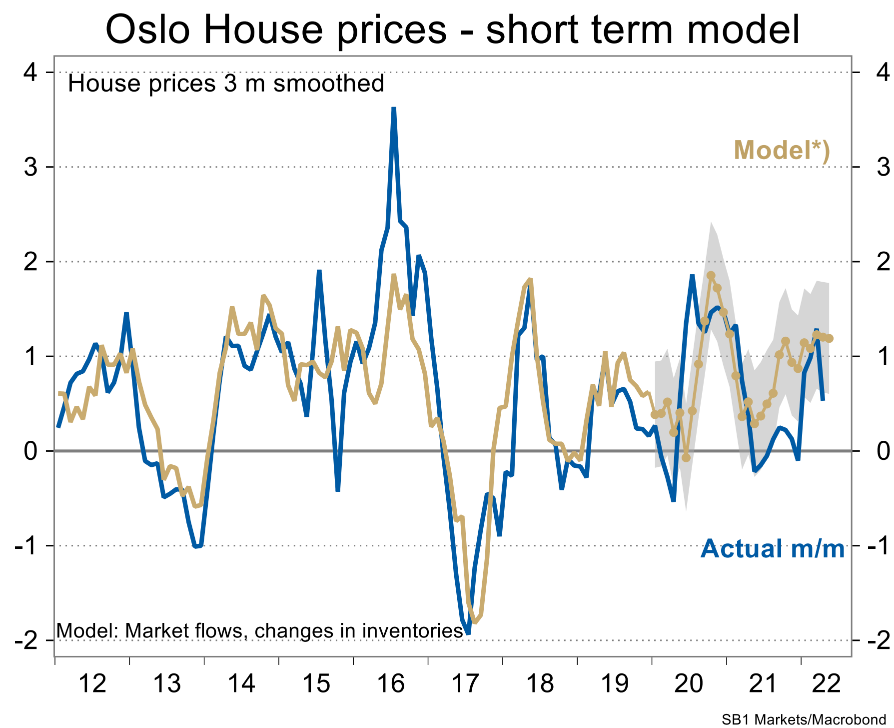
Though with substantial regional differences



- In average, the i/s ratio has fallen the past 12 months

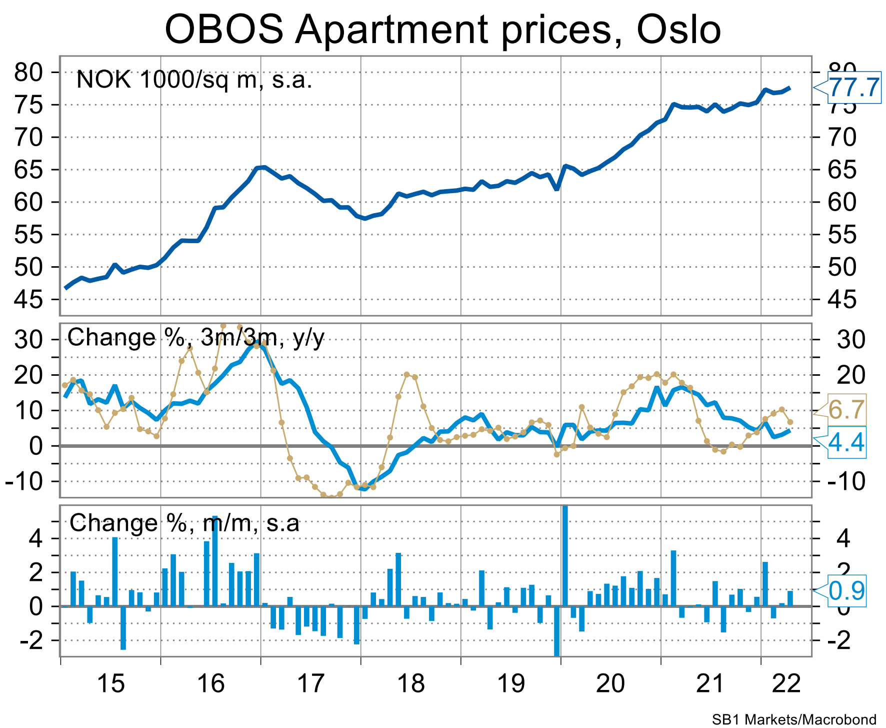
Short term market flows suggest decent price growth

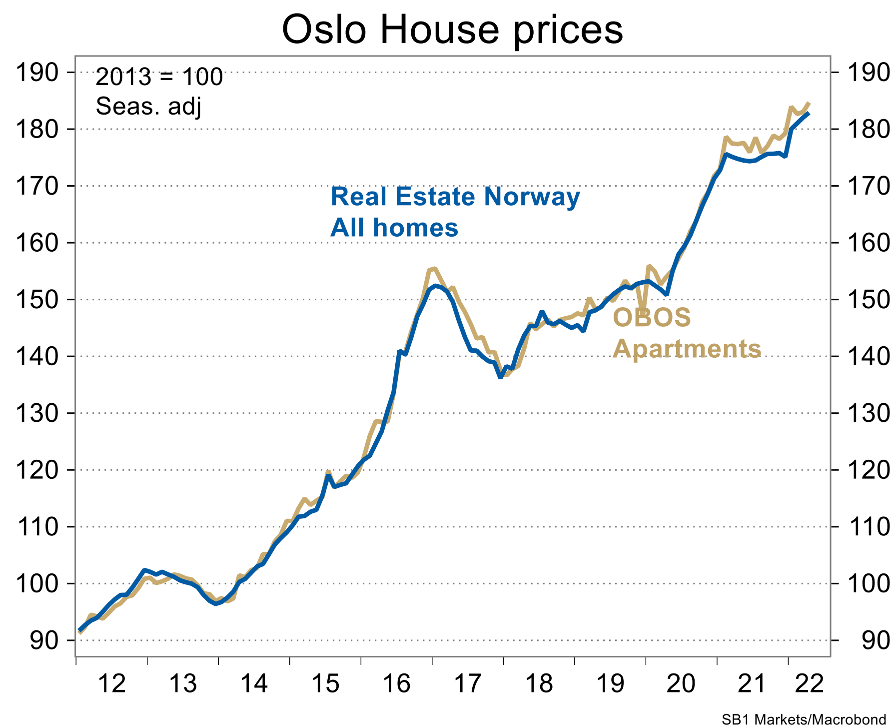




- Our **national x Oslo model** based on flows and the inventory signals a 0.6% growth in house prices per month, marginally below the 0.7% rate past 3 months
- Our **Oslo model** signals slightly above 1% growth, above the 0.5%% lift per month the past 3 months
- **Mortgage rates** are not included in these short-term market models, because they have not consistently added to the models' performance. Still, over time, mortgage rates and credit growth are important driver for house prices, and now rates are on the way up
- *These models are not long-term price models, just short-term models based on flows of (existing) houses approved for sale, actual sales and changes in inventories – which are normally correlated to prices*

OBOS apartment prices up 0.9% in April, up 4.4 y/y





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

Highlights

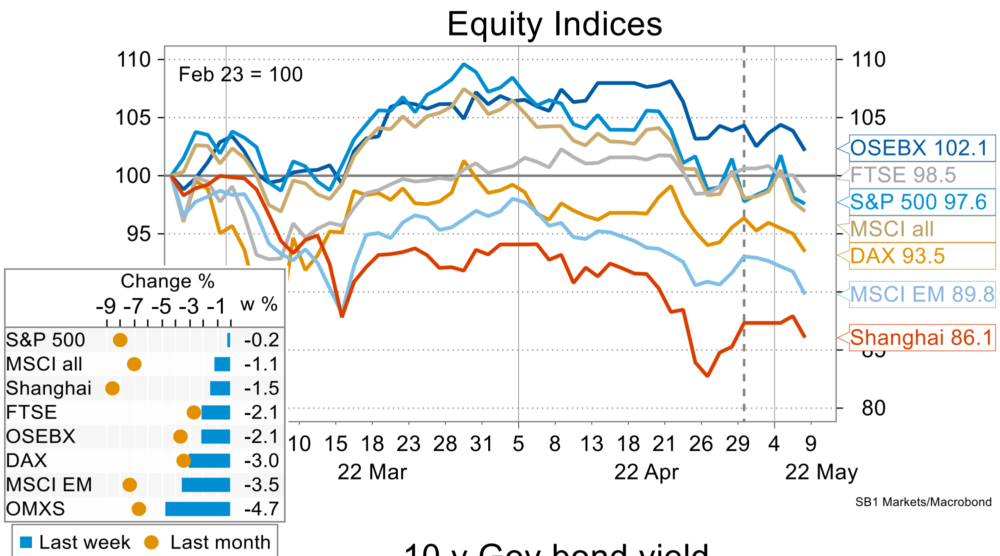
The world around us

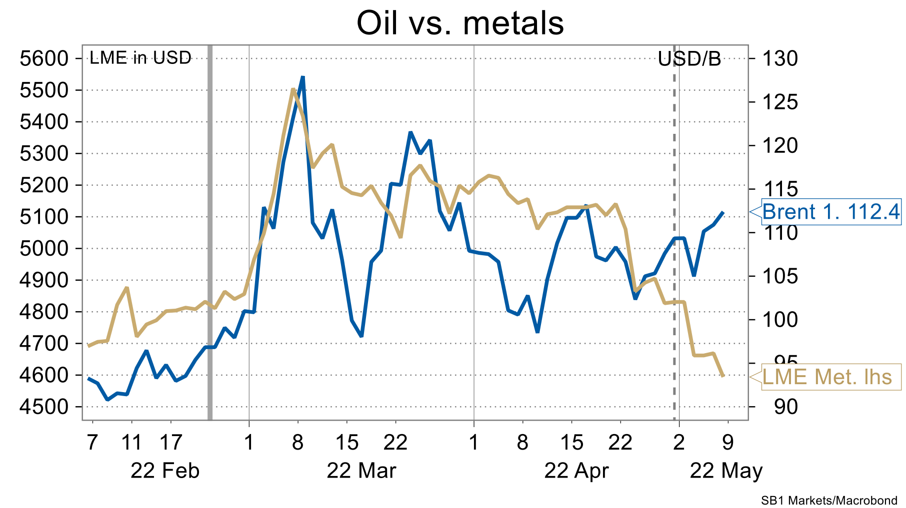
The Norwegian economy

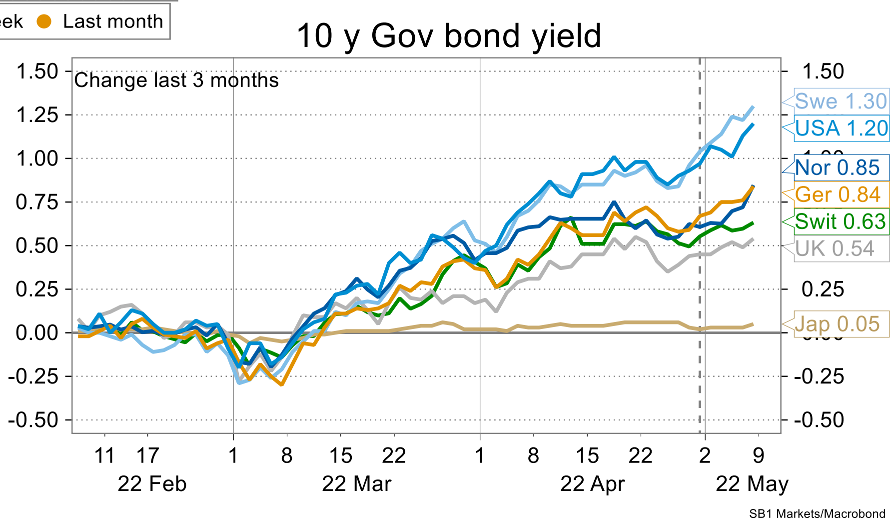
Market charts & comments

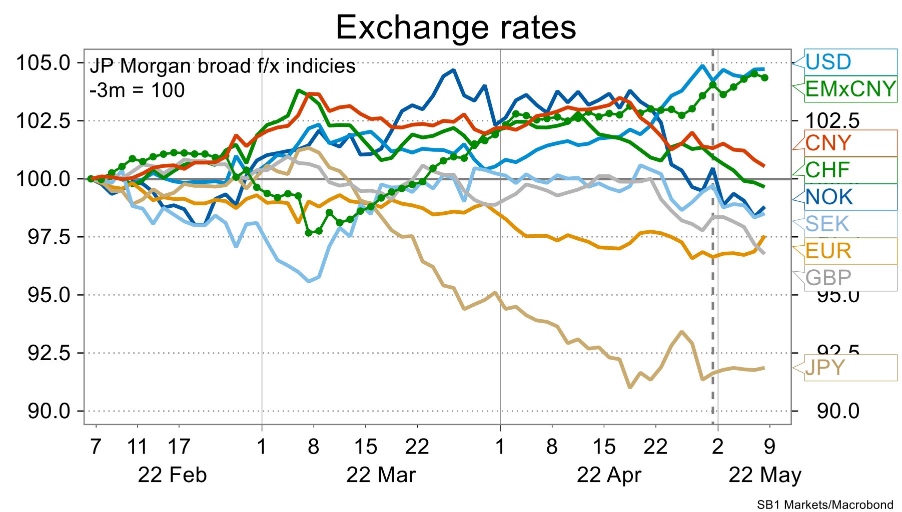
Volatile stock markets down, the US market the least

Oil prices up on supply concerns, metals further down. Bond yields sharply up. NOK, SEK, CNY down. EUR up



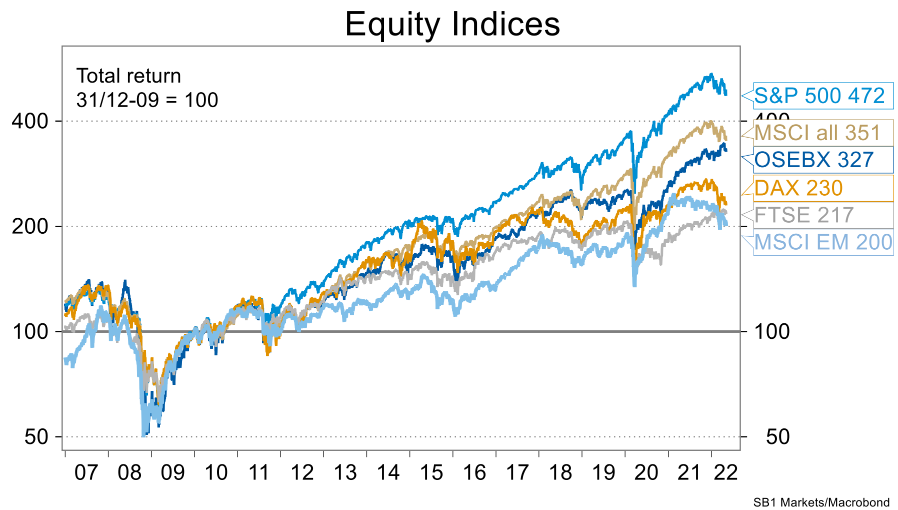


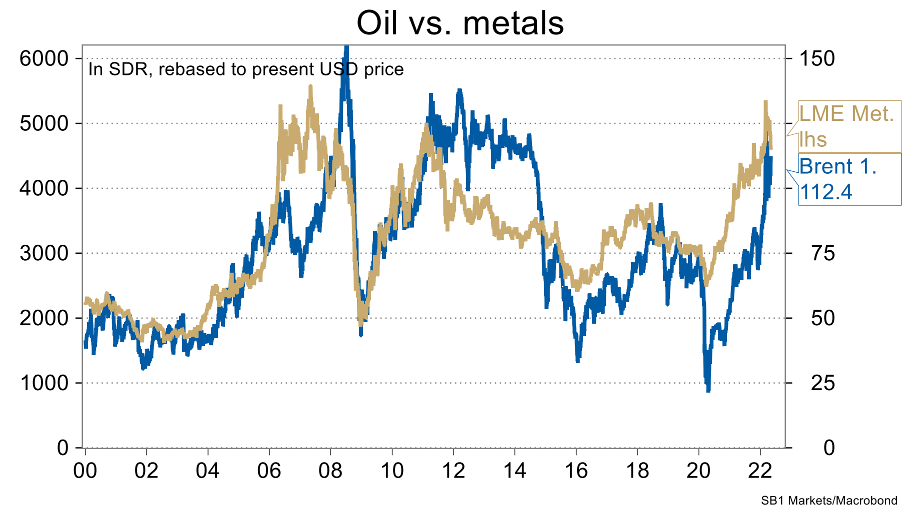


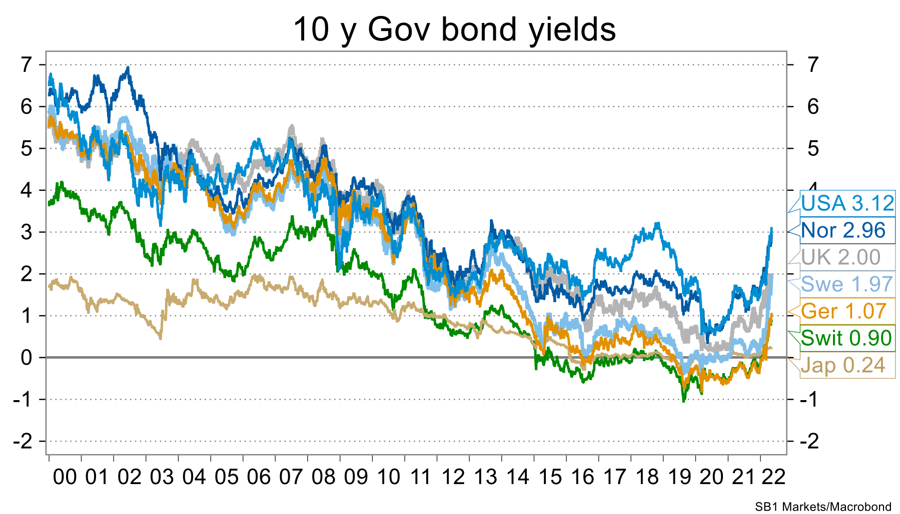


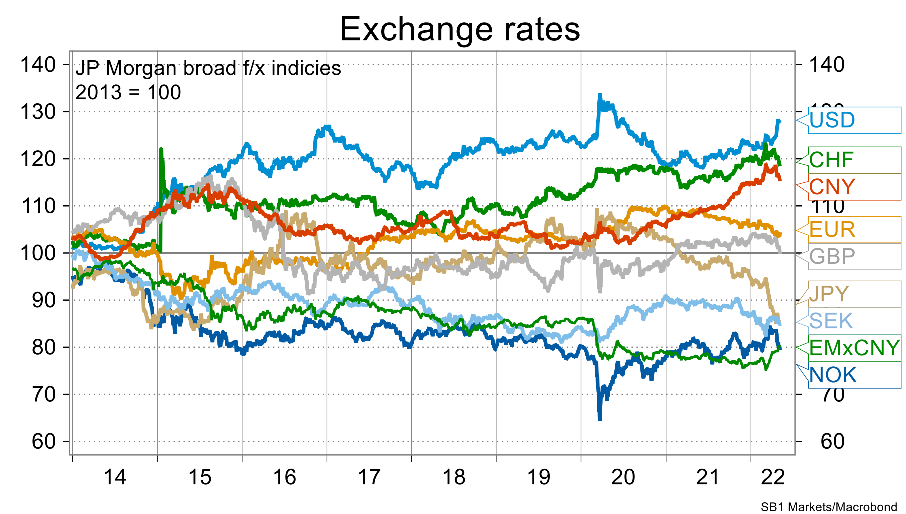
The big picture: Stock markets down (-oil rich OSEBX, FTSE), bond yields up

Commodities have taken a big step upwards, until early March. NOK, USD trend up; EUR, JPY down





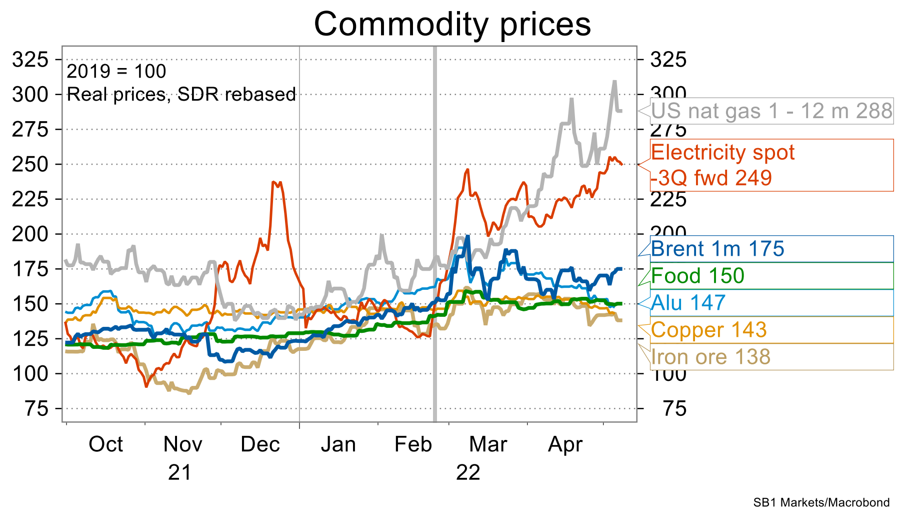


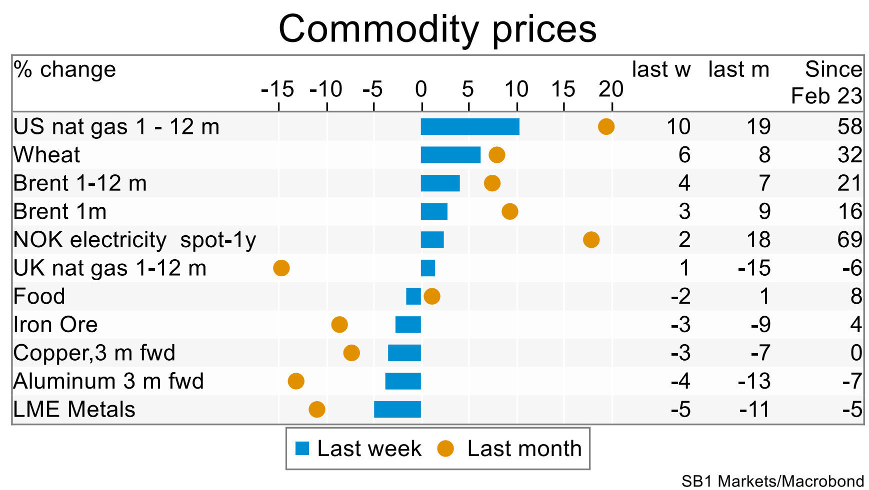


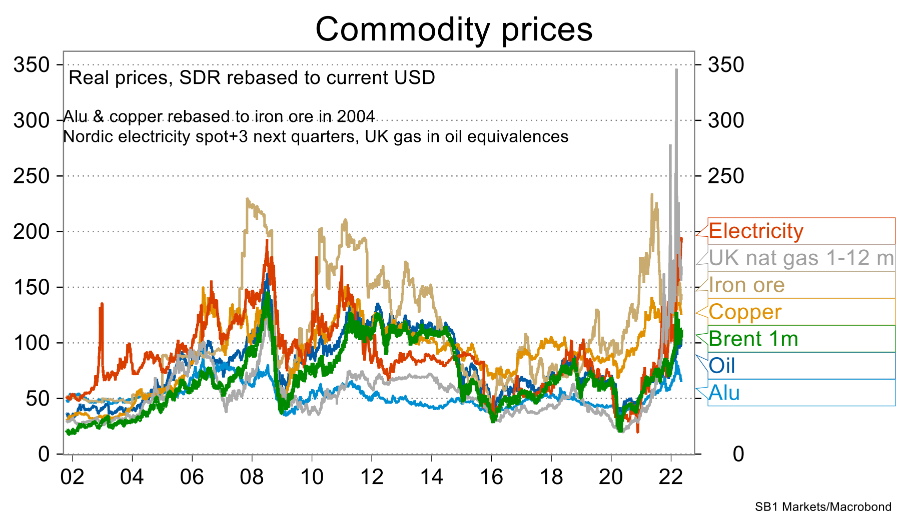
SpareBank 1 MARKETS

Mixed commodity prices, US nat. gas surges, oil and wheat up too. Metals down

Food prices marginally down last week too. Prices are up 50% since 2019, 8% from the war started



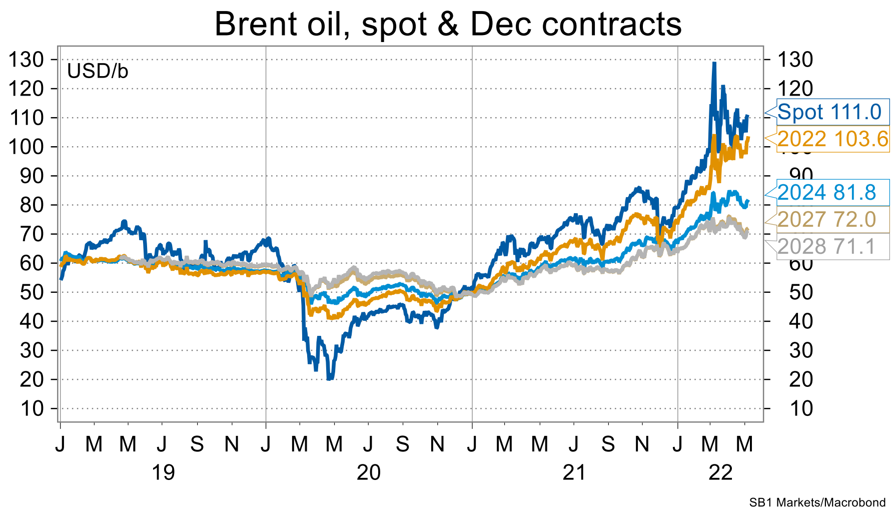


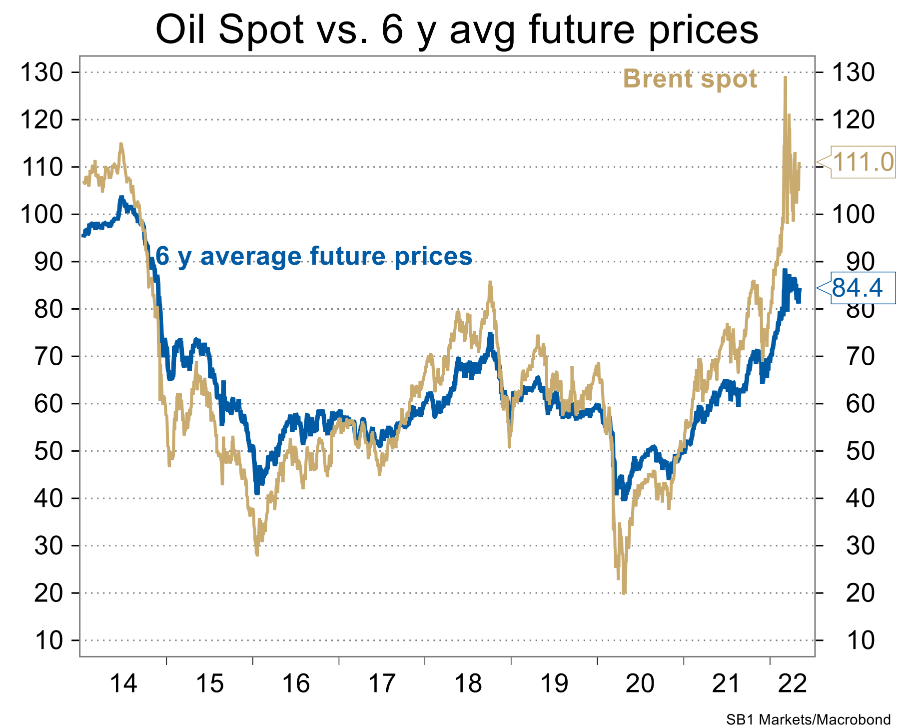


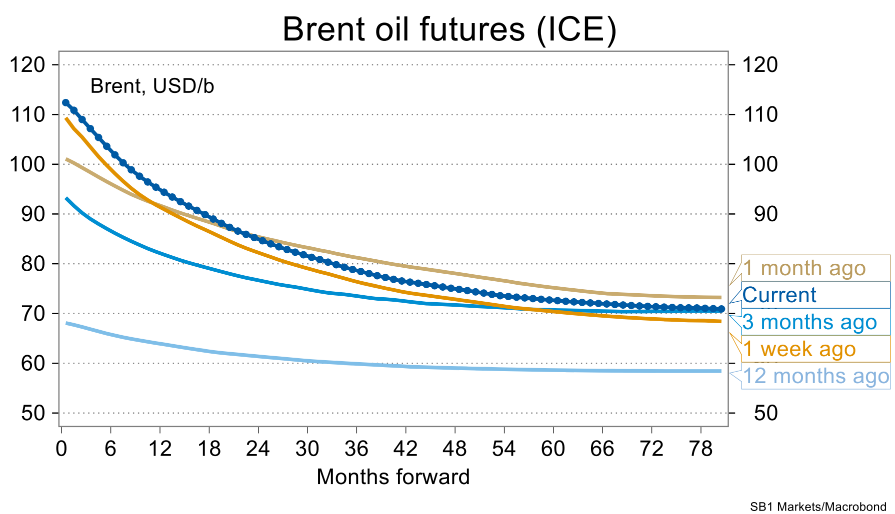
- UK natural gas prices are 6% down since before the invasion
- US natural gas prices are up 58%!
- Norwegian electricity prices are up 69%
- The oil price rose as EU will (more or less) stop buying Russian oil before the end of the year

The whole oil price curve shifted upwards last week

Oil up, as the EU seemed to not be willing to buy Russian oil (but Hungary balked during the weekend)



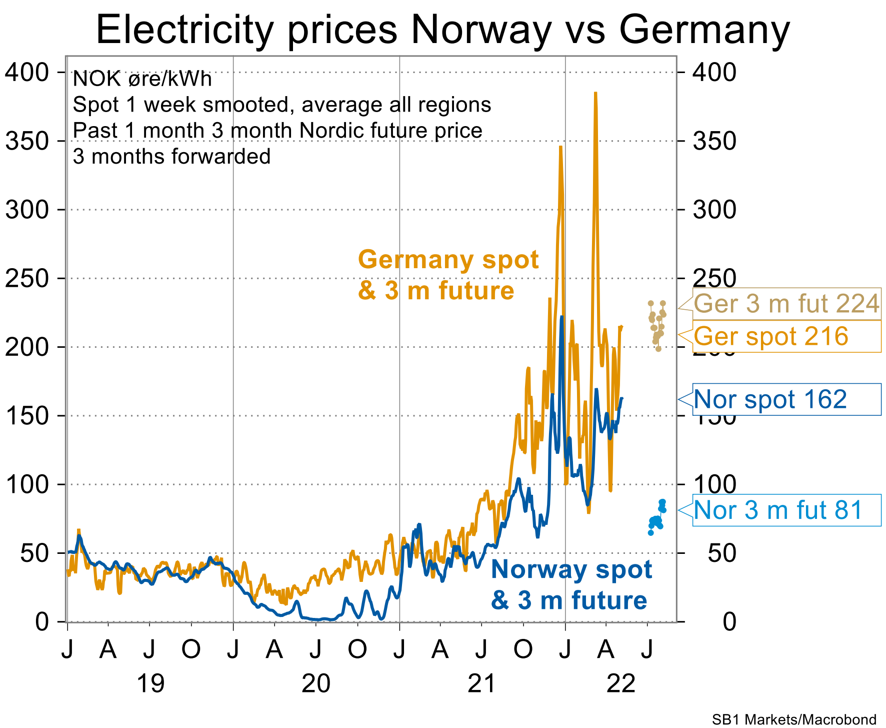


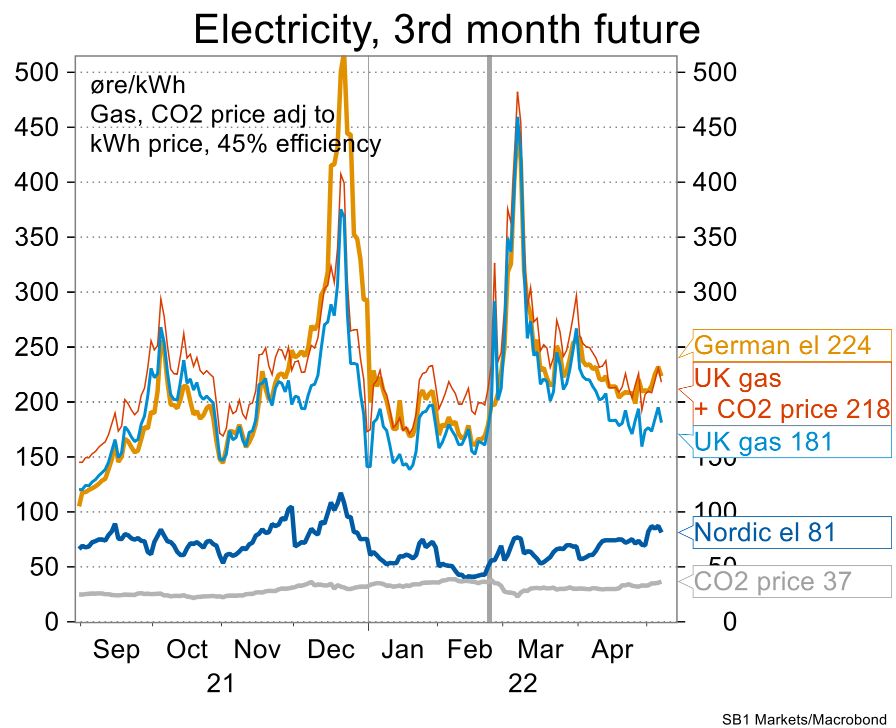


- Biden says the G7 has agreed to stop buying Russian oil – but the EU did not reach an agreement as Hungary refused to join
- Future prices have been lower than normal vs. the short end of the curve after the invasion – because markets assume that in the end, oil will flow

European energy prices up last week, most not higher than before the war

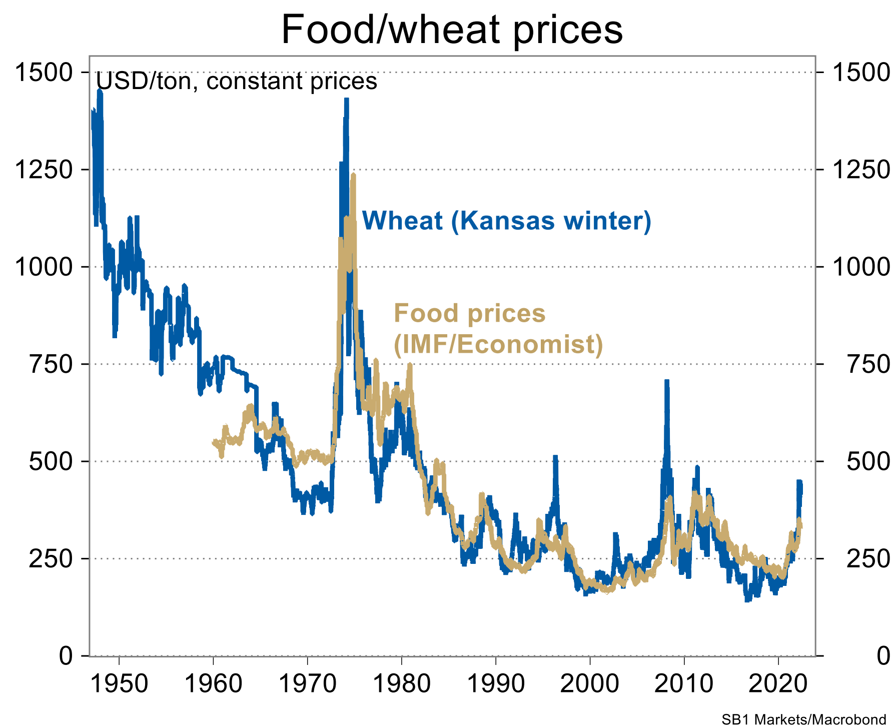
European energy prices have been drifting downwards since early March (but not Norw. el. prices)

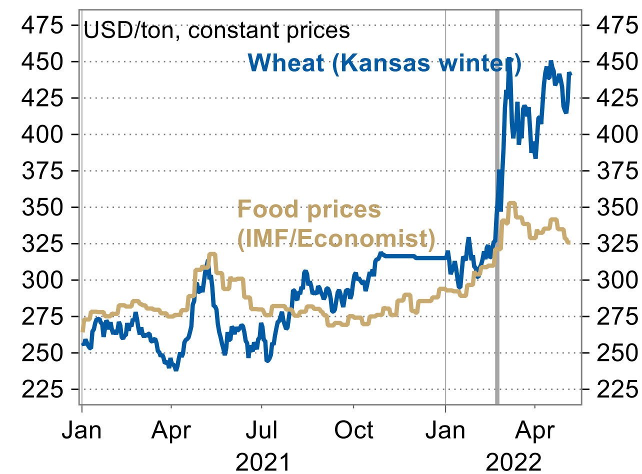




Wheat prices up, but food commodities in average further down

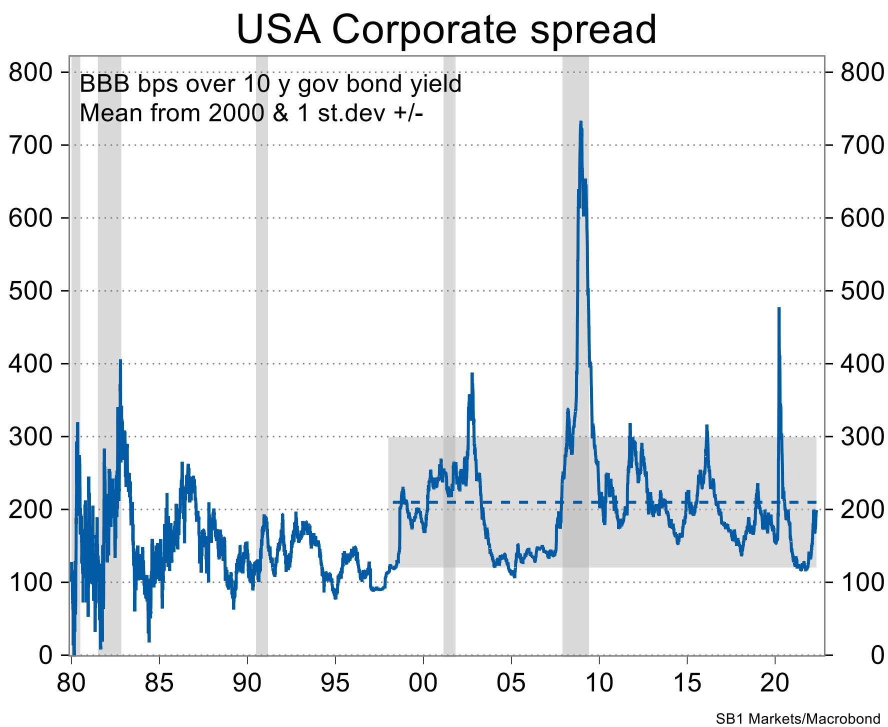
No end of the war in sight: how much wheat, sunflower + fertilisers will get out of Russia/Ukraine?

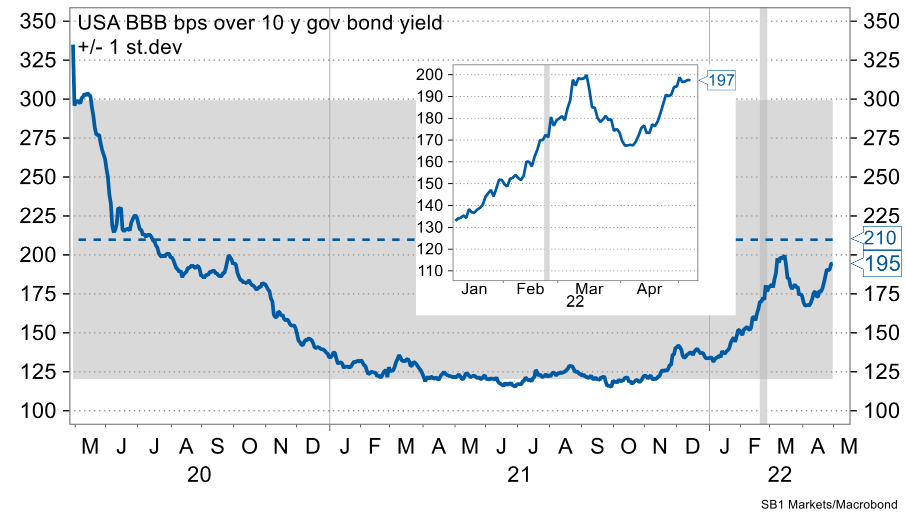


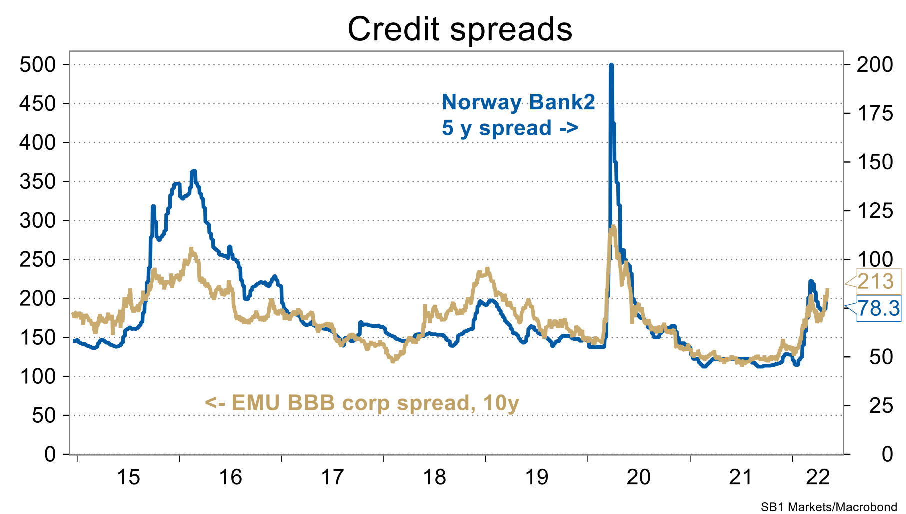


SpareBank 1 MARKETS

Credit spreads on the way up again, risk off, as at equity markets

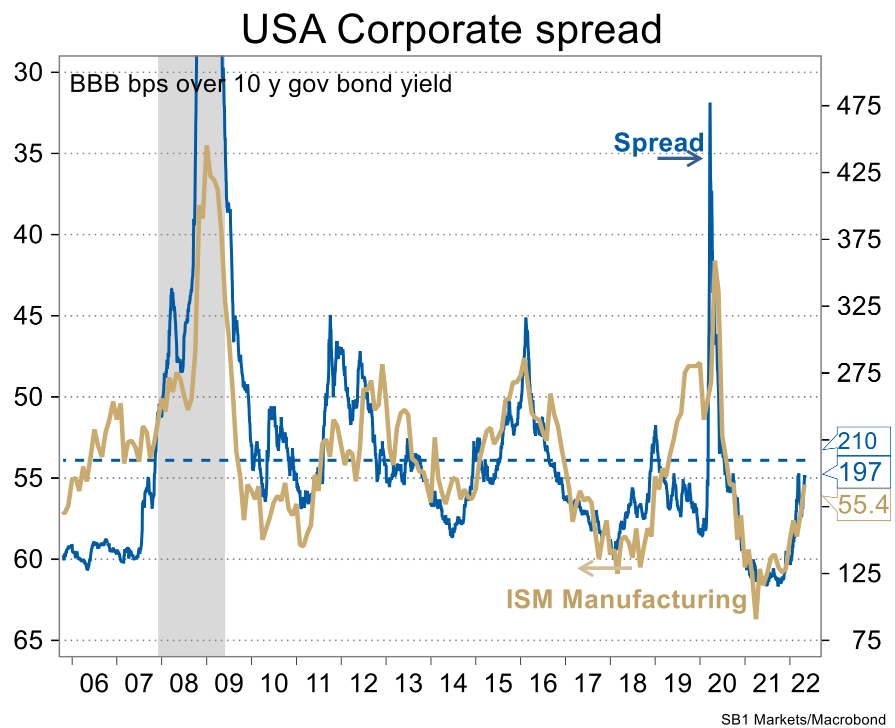


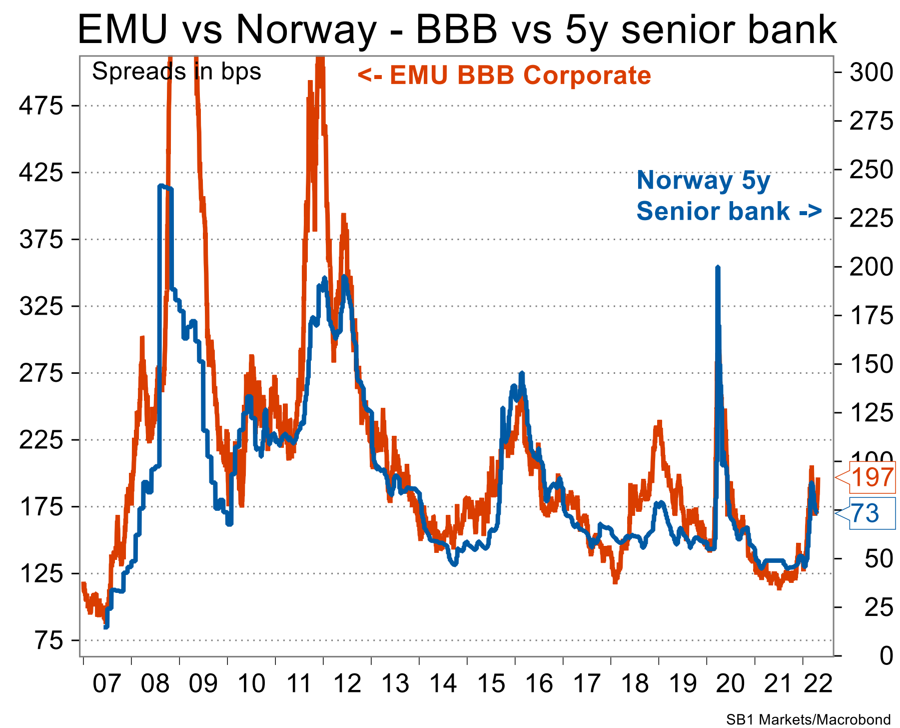




Why are credit spreads widening? Could it be the slowing economy?

What do you think is the most likely: An ISM at 50 or 60 in 6 months time?

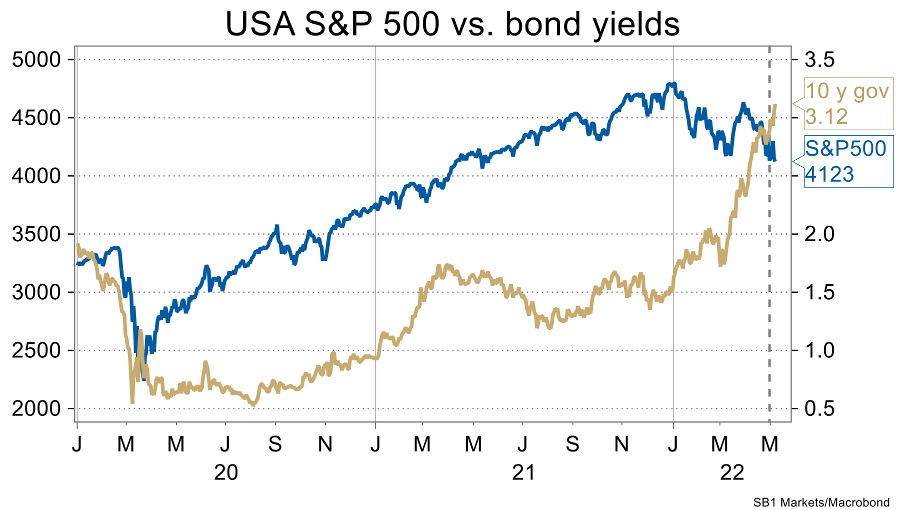


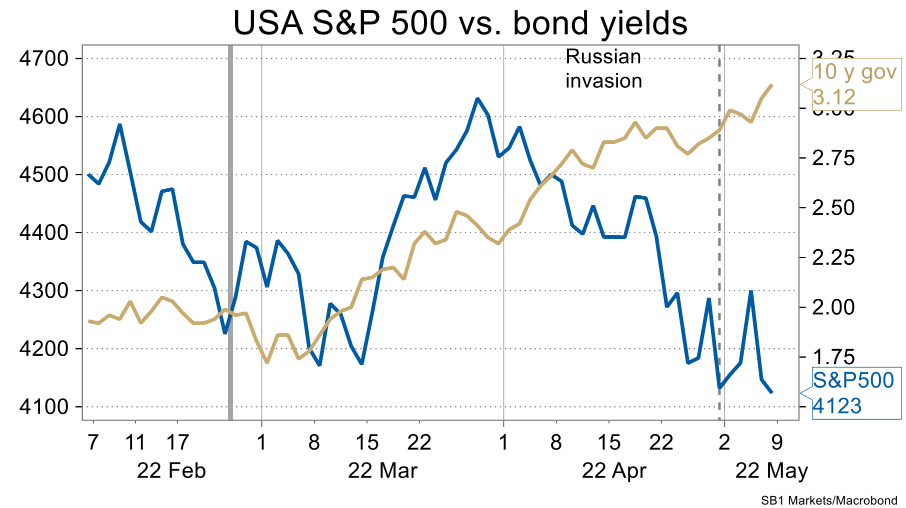


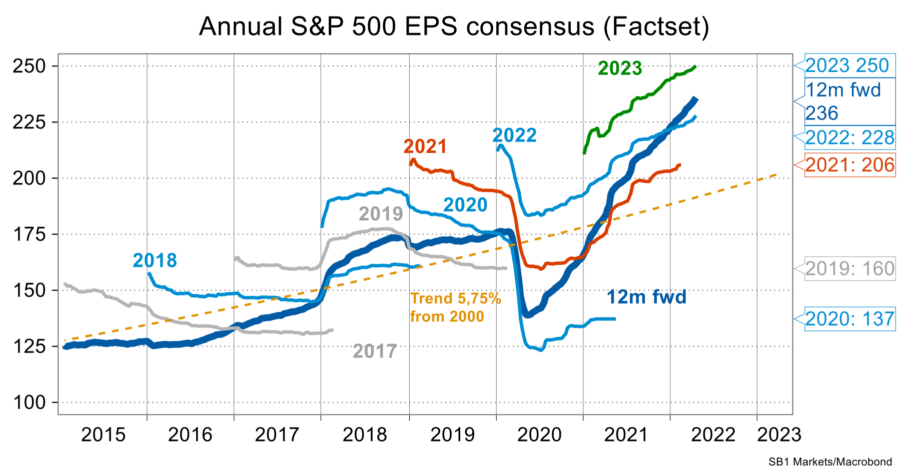
SpareBank 1 MARKETS

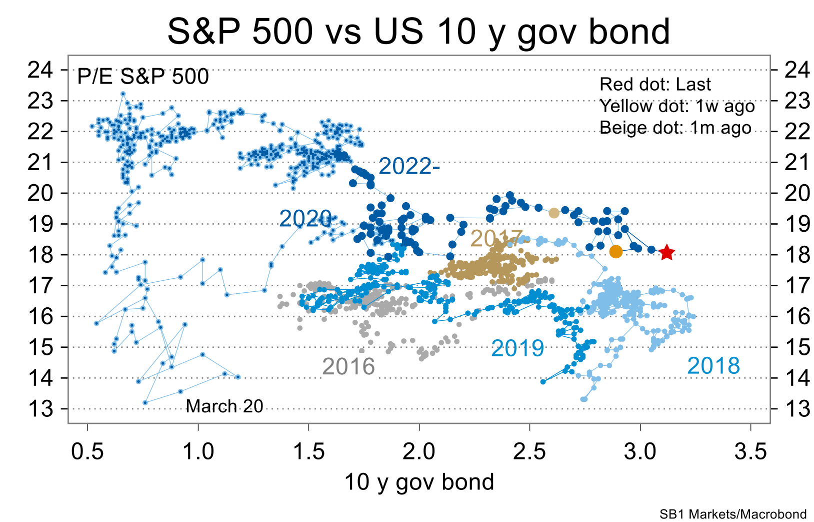
The 10 y gov bond up 23 bps to 3.12%. The S&P500 down 0.2, 14% from the peak

The next shoe to drop: Growth in expected earnings will soon fall sharply



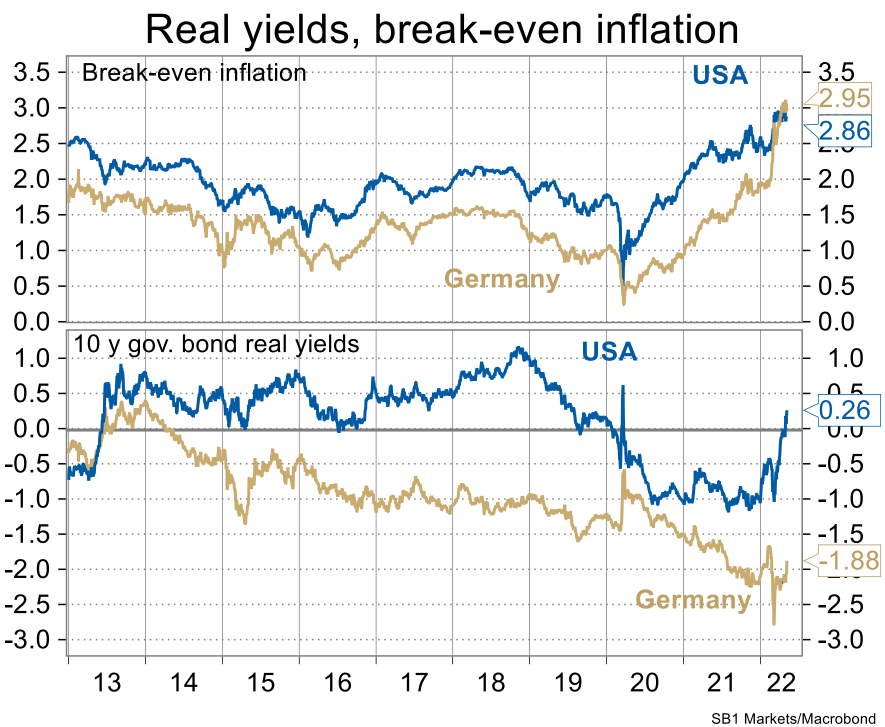


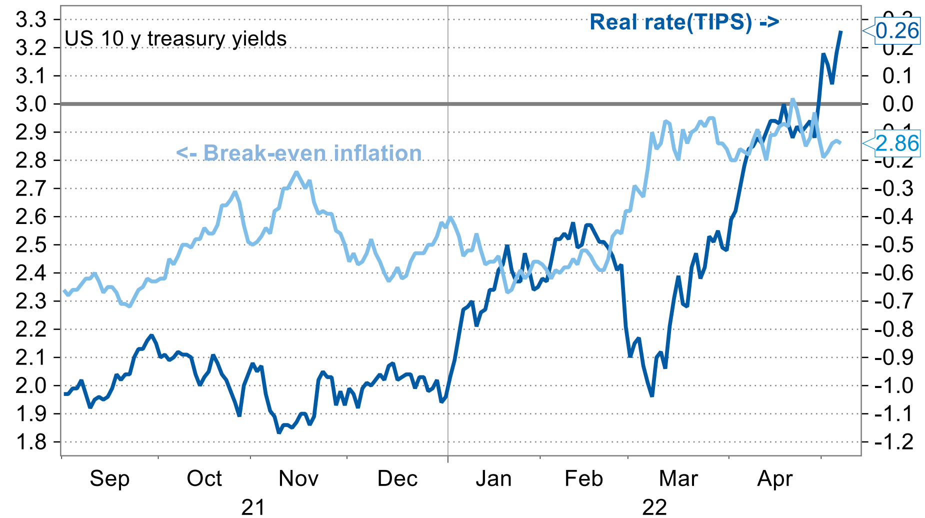




US 10 y TIPS real rate up 25 bps to +0.26. The German peer up 28 bps, still at -1.88%

Inflation expectations flat/down and close to 3% at both side of the Atlantic. Nominal at 3.12%, 1.07%!!





US & Germany 10 y Gov bond yield

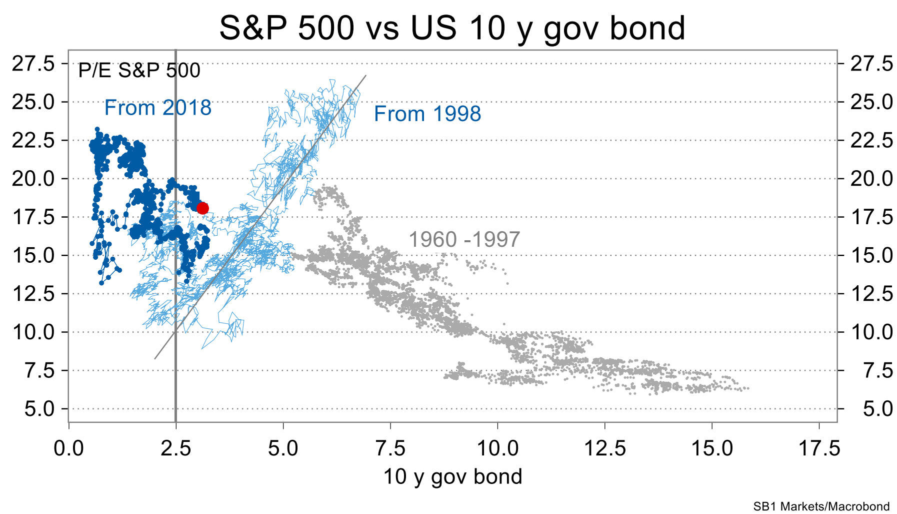
	Yield	Change 1w	Change 1m	Since Feb 18	Min since April-20
USA nominal treasury	3.12	0.23	0.51	1.20	0.52
.. break-even inflation	2.86	-0.02	0.03	0.45	1.06
.. TIPS real rate	0.26	0.25	0.48	0.75	-1.19
Germany nominal bund	1.07	0.17	0.42	0.85	-0.65
.. break-even inflation	2.95	-0.11	0.04	0.97	0.40
.. real rate	-1.88	0.28	0.38	-0.12	-2.80

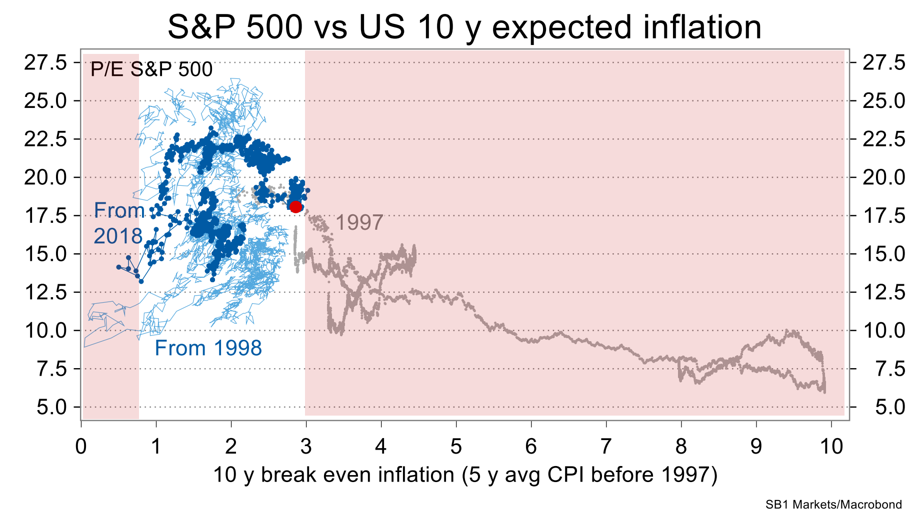
SB1 Markets/Macrobond

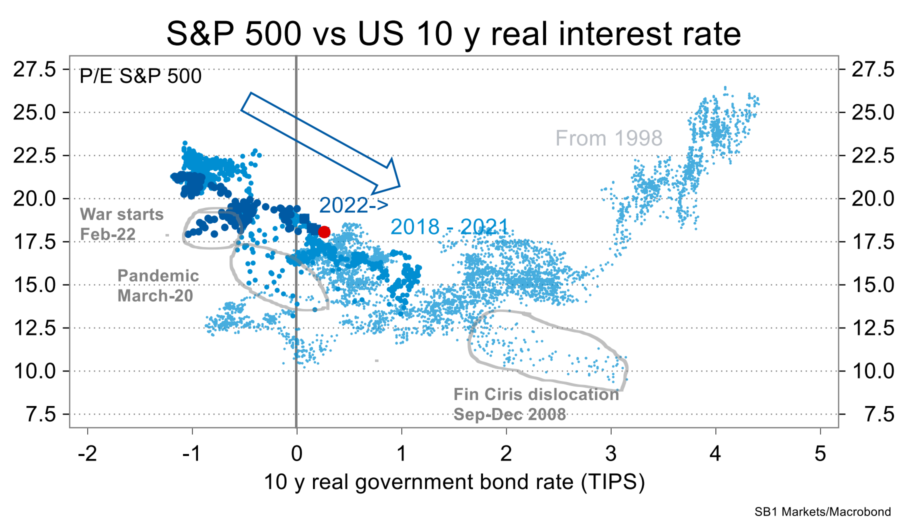
- **Nominal 10 y bond yields** are above 3% in the US and above 1% in Germany, the highest since late 2018 and late 2014 (!) resp.
- **Real rates in the US** fell to 1.03% after the Russian invasion in Ukraine, down from -0.42%. Now it is at +0.26%!!
- **The 10 y inflation expectations** are just below 3% in both the US and in Germany, at least vs. face value discounted at the bond market
- **Real rates in Germany** rose sharply last week but are still at -2.18%. The spread to the US 10 y real yield is close to record high

Bonds vs. equities: What's next? Central banks are now fighting inflation!

... And they will probably succeed. But at a price: Higher real rates + 'some' earnings surprises



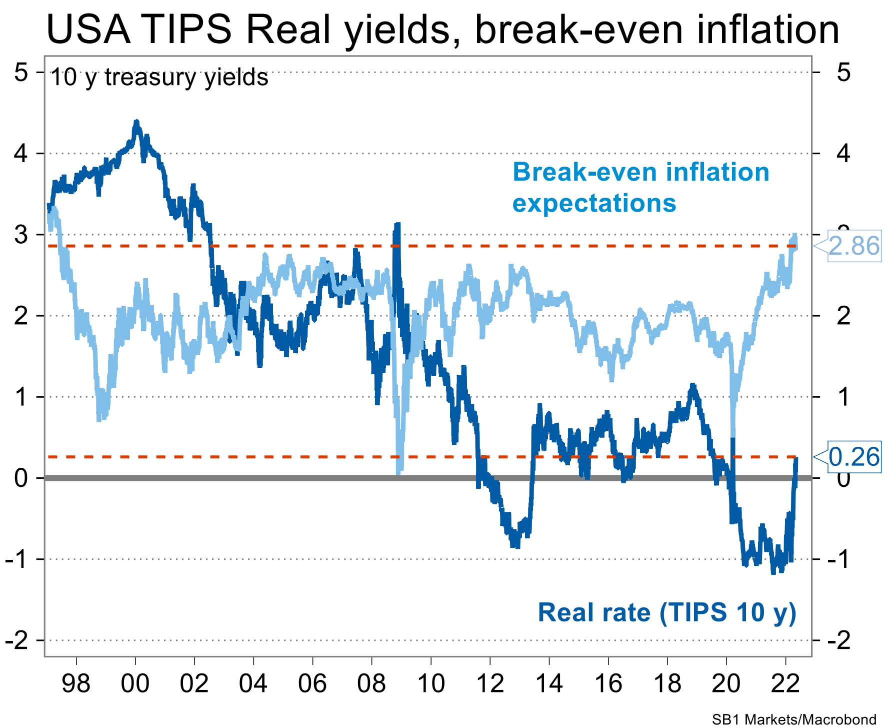


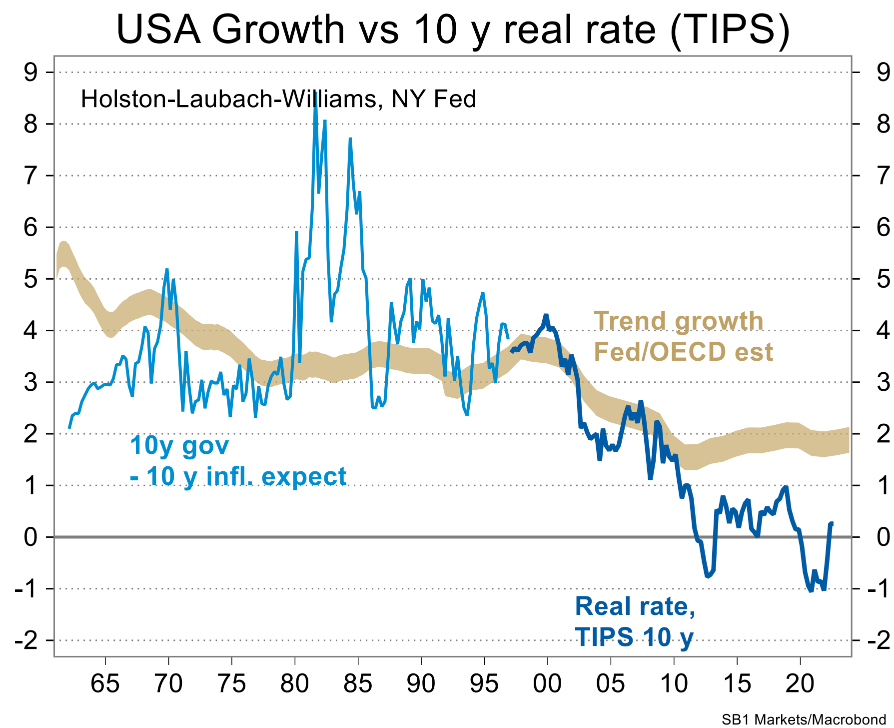


- **Expected inflation**
  - » ***If its not too low or too high: No problem***
    - 'Real' expected earnings are unaffected, higher inflation implies stronger growth in earnings, and vice versa
  - » ***If its too low or too high: A problem***
    - Something is rotten: Deflation or far too high inflation. The economy is not stable. Risk are increasing, earnings are exposed.
  - » Now: Infl. expectations at close to 3% - on the border to become a problem?
- **Expected long term real interest rates**
  - » ***Low real rates normally not good news, high rates were OK***
    - Real rates were low when the economy was weak, the outlook uncertain
    - High real rates when the economy was booming, with high P/Es
  - » **2018-21:** real rates have been low even if the economic outlook has been OK
    - Central banks wanted to lift growth, inflation was anyway not a problem – we entered the 'Goldilocks' corner'
  - » **Now:** Central banks engaged in a HUGE policy shift, to contain inflation. The risk: A further increase in REAL rates, at the same time as growth expectations slows!

Mind the gap: It's rapidly closing!

Real rates are rapidly on the way up from levels that were far to low if the growth outlook was OK

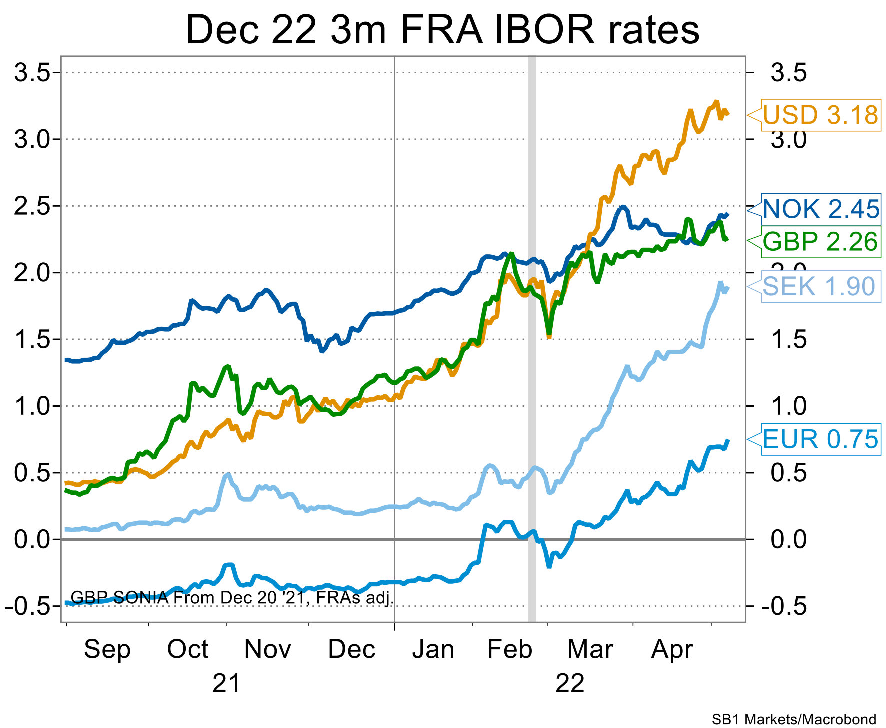


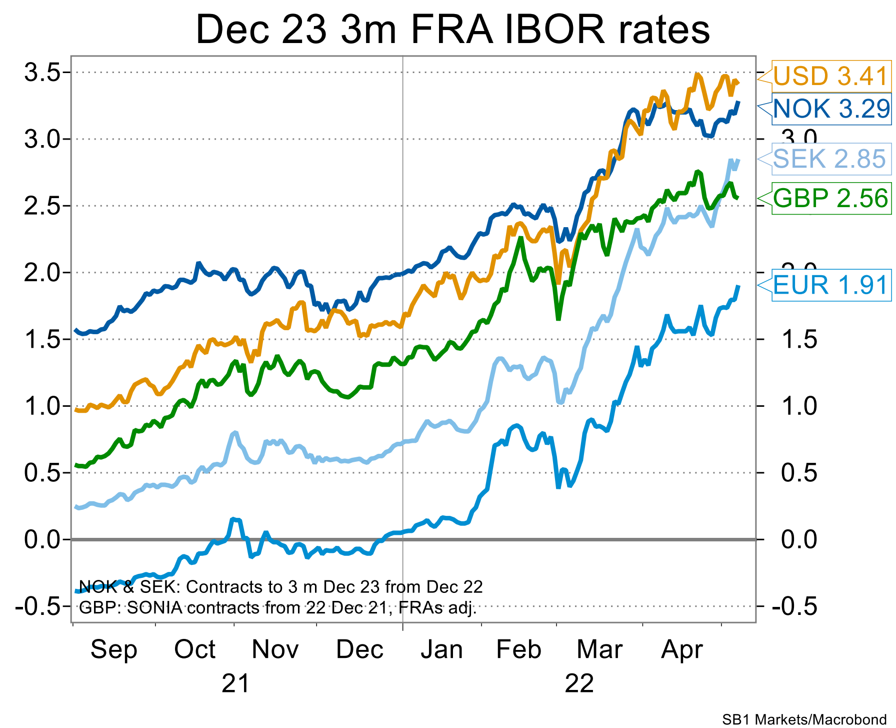


- There is now reason to believe that the current surge in real rates is due to an equivalent increase in growth expectations. It is of course the opposite: At least the short to medium-term outlook is now weakening as central banks finally enters the fights against inflation by at least bring growth down to below trend growth
  - » Profit margins are VERY exposed
  - » Demand for labour will slow too, and unemployment will increase – in order to get wage inflation down
- The USD 10 trl question: Are all risk markets really discounting this scenario?

SEK FRAs sharply up last week too, NOK & EUR up too but less

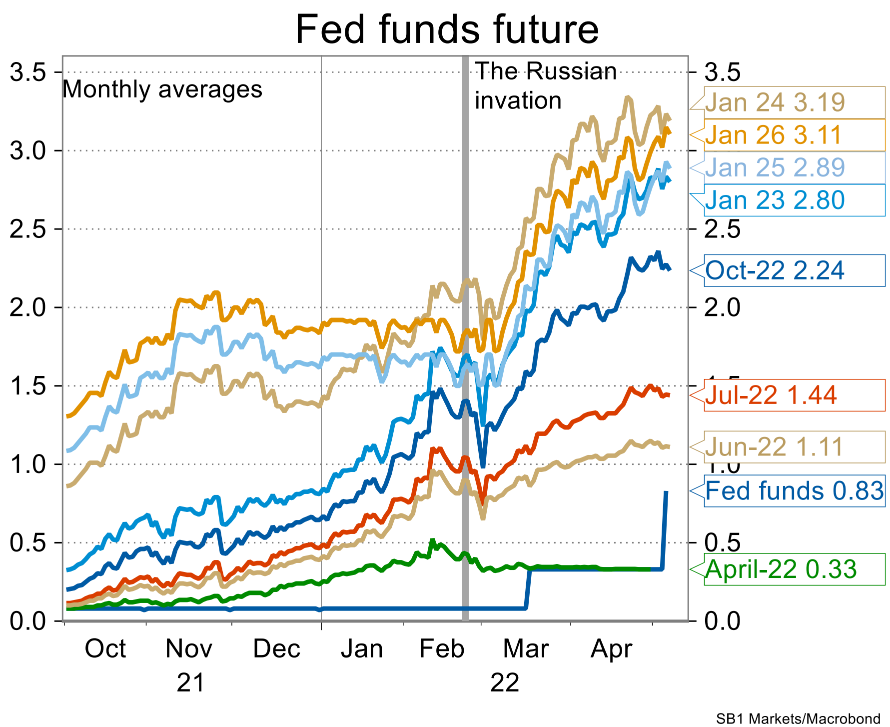
SEK FRAs up >40 bps after the Riksbank hike, market is 120 bps above the bank's 150 bps' lifted path

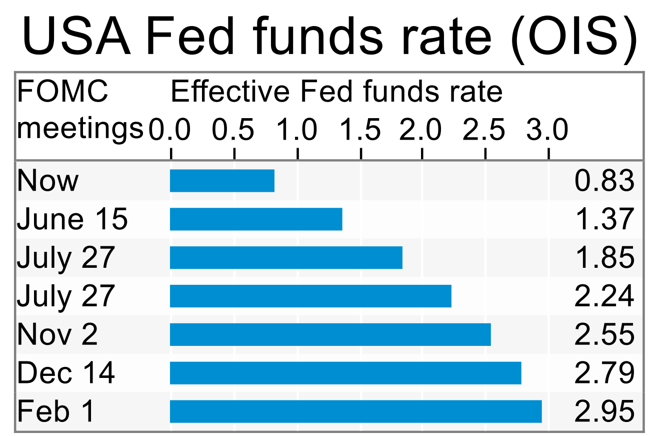




- The short end in US marginally down as Powell took 75 bps off the table (for now) but the Dec-23 contract rose

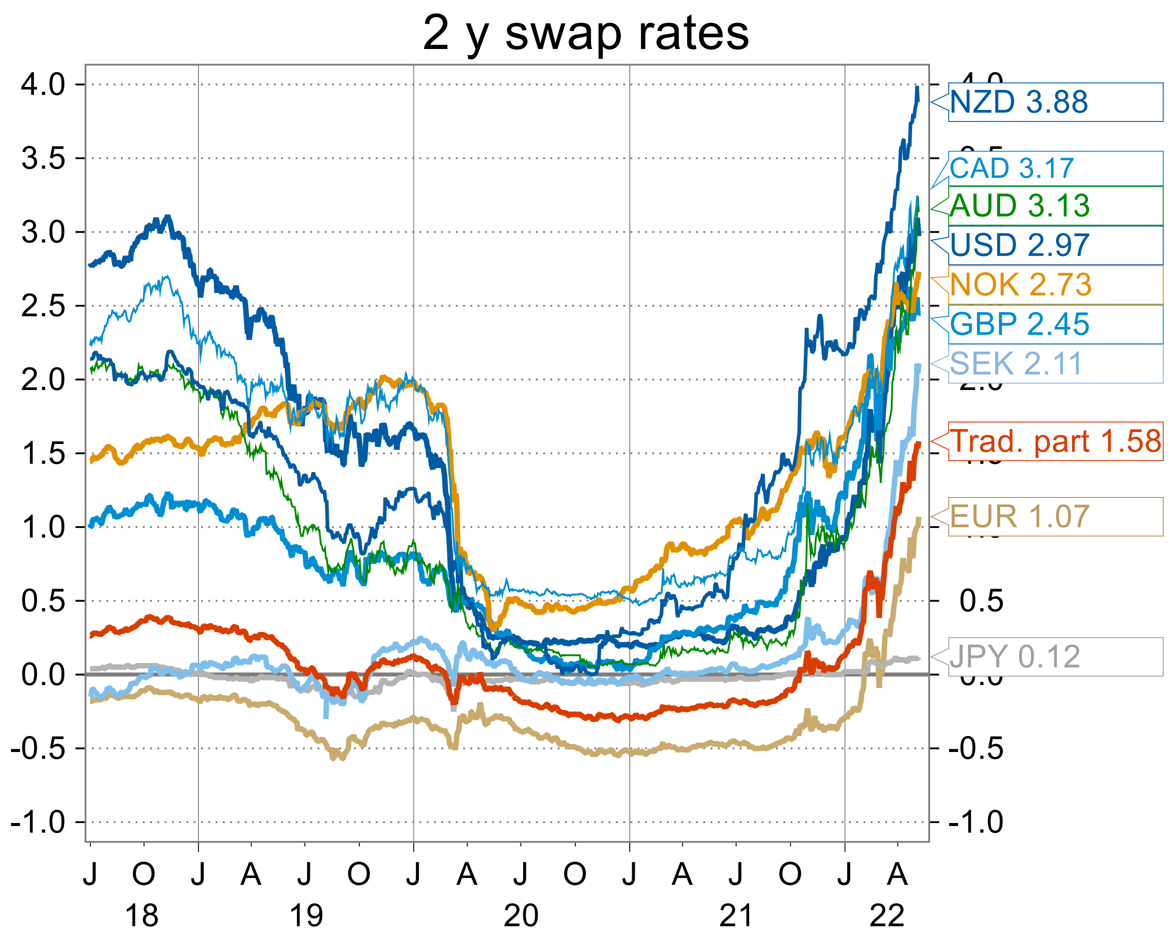
The Fed funds rate up 50 x 2, then (almost) 25 x 3, up to 2.70% in December



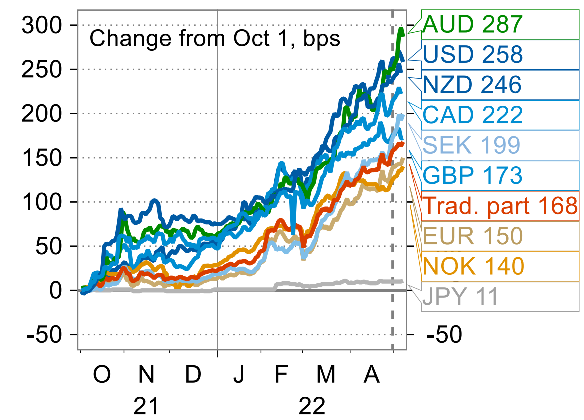


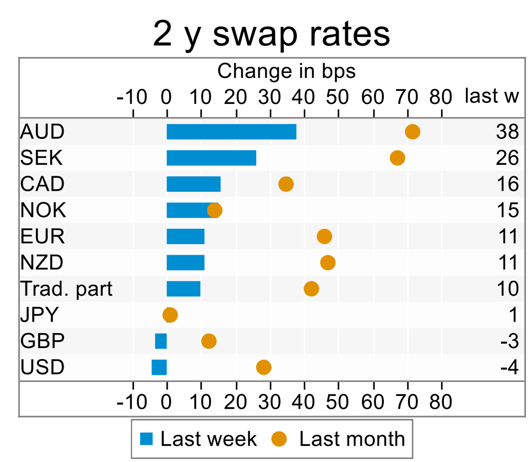
The Reserve Bank of Australia surprised the marked by the 1st 25bp hike

And then the 2 y swap shot up 38 bps, to 3.13%! So 'some' more hikes are expected. Most others up



SB1 Markets/Macrobond

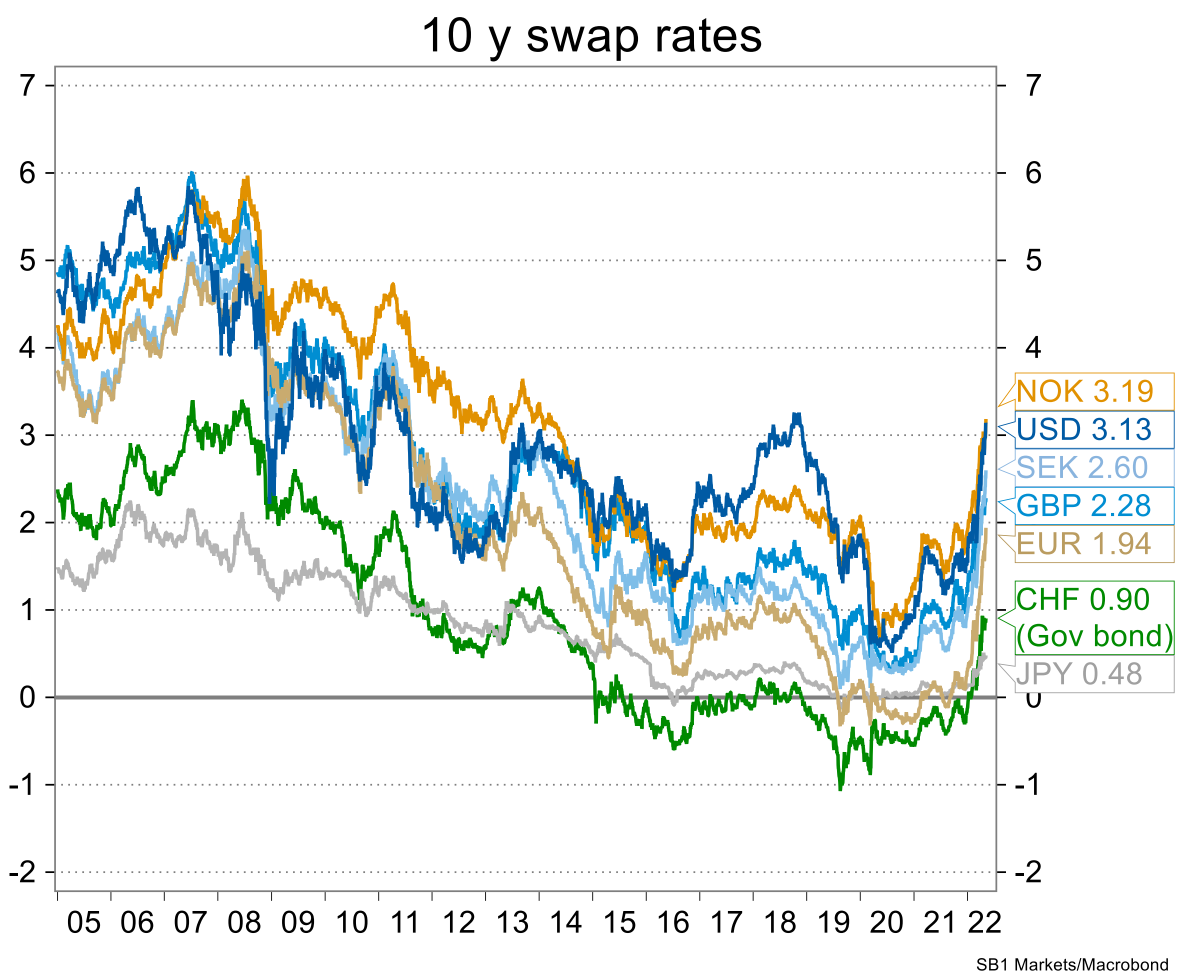


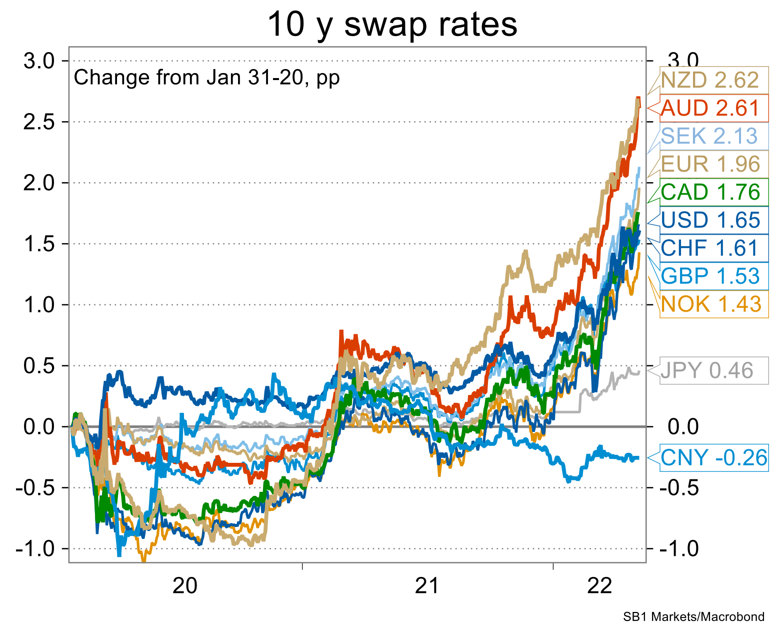


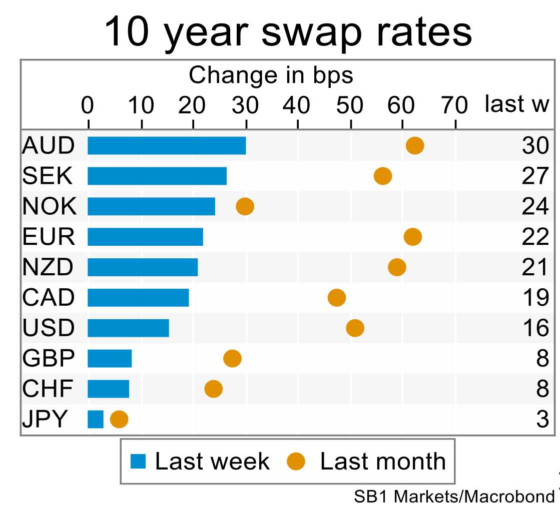
SB1 Markets/Macrobond

NOK recovered the throne, we are at the top again, at 3.19%

Well, that's because NZD (4.05%), AUD (3.76%), CAD (3.48%) are not included at our chart





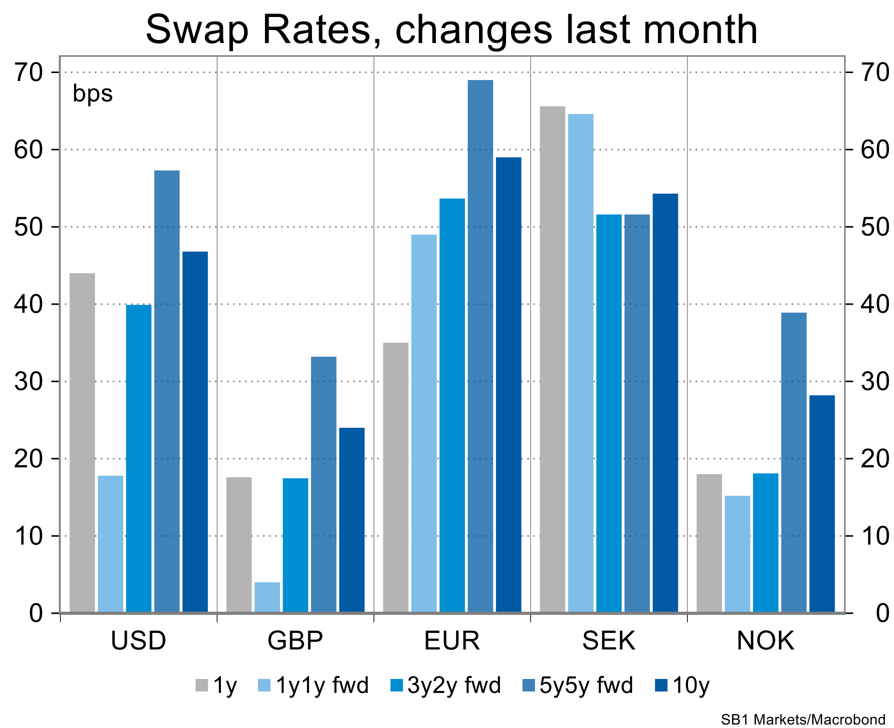


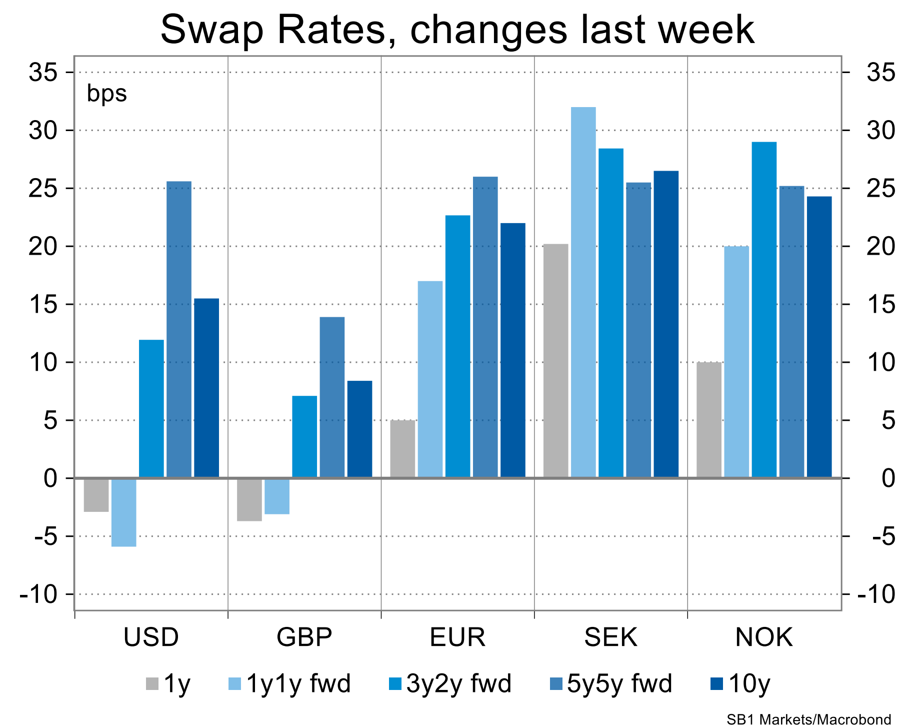
REAL ESTATE: TAKE CARE. YIELDS WILL HAVE TO RISE SHARPLY!

CHF: 10 y government bond yield

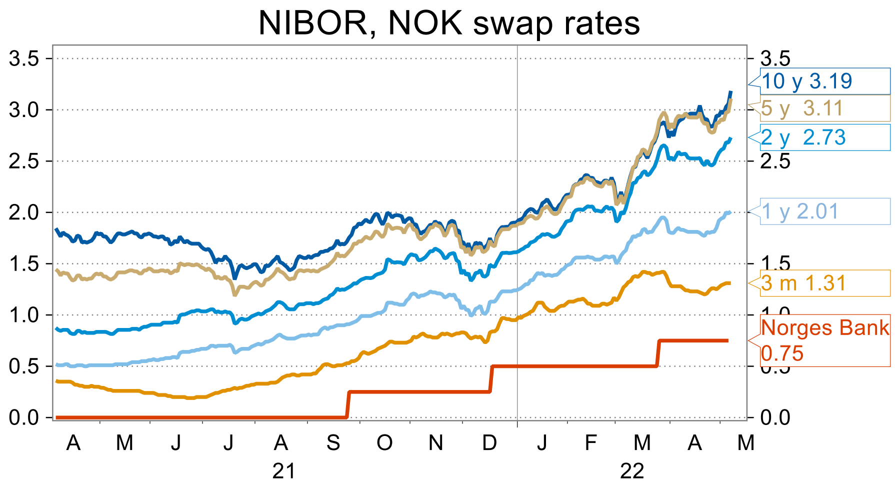
The short end in US, UK down on soft (or perceived soft) central banks. Others UP!

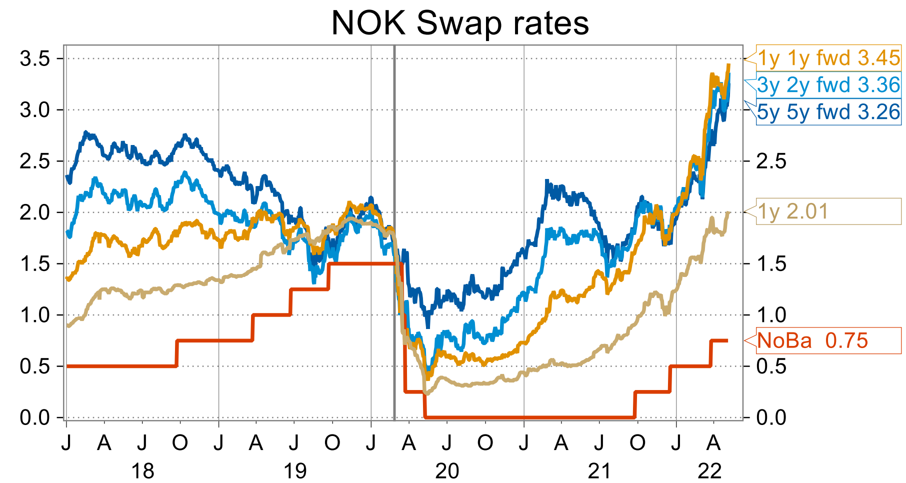
A huge lift in interest rate expectations in SEK, NOK and EUR (in that order)

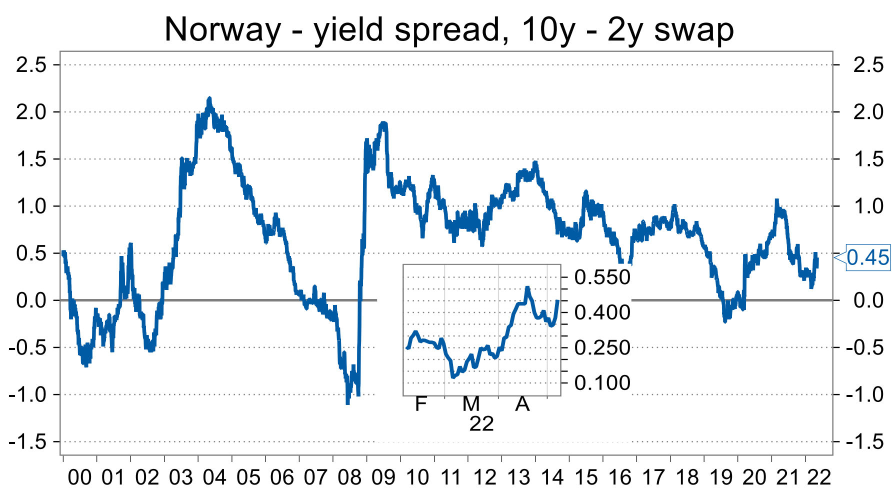


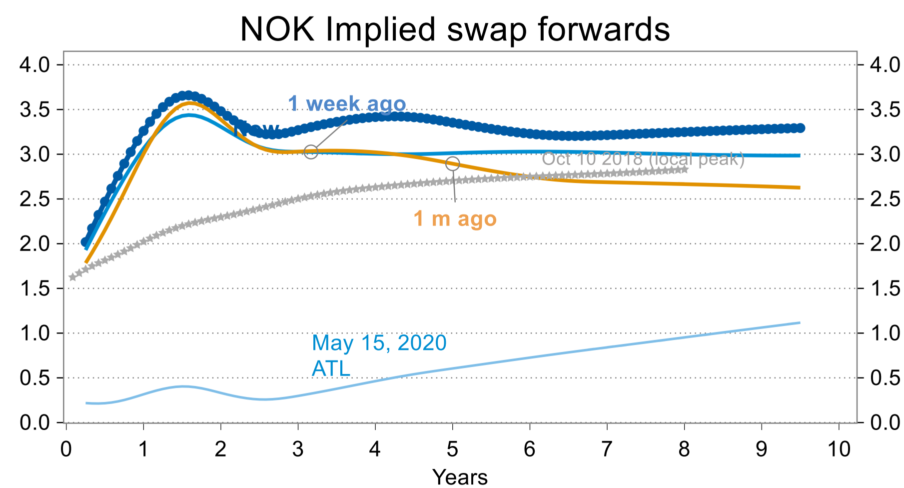


Rates up all over the curve, the most in the long end



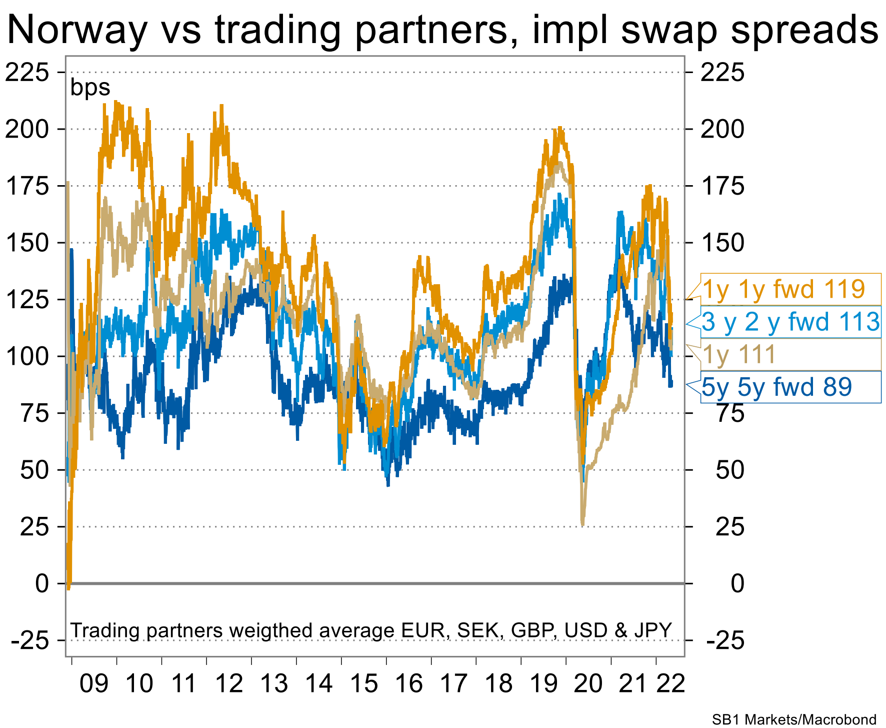


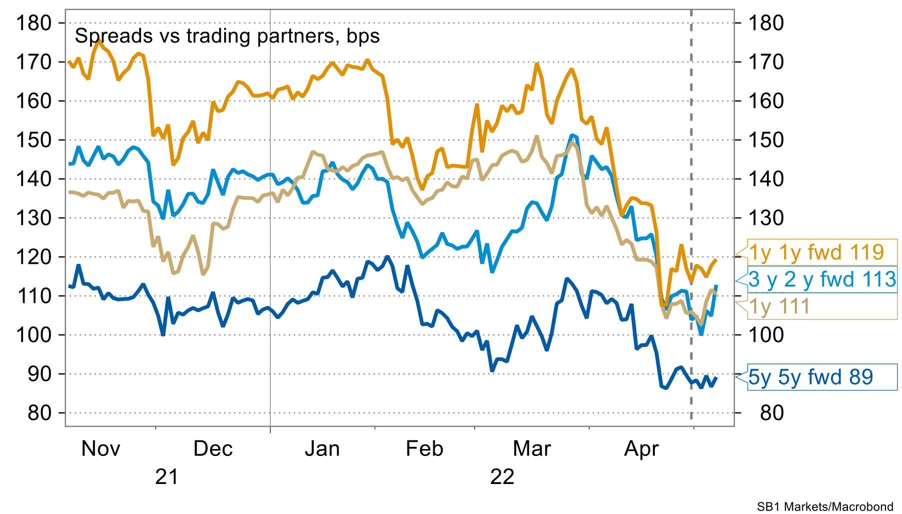


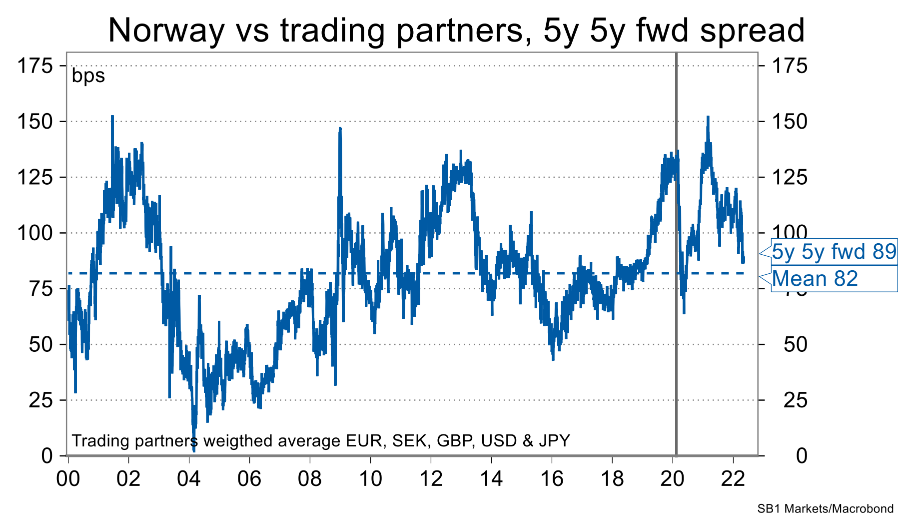


Spreads just slightly up as rate surged abroad too

Spreads are not far from levels following the rapid narrowing recent weeks



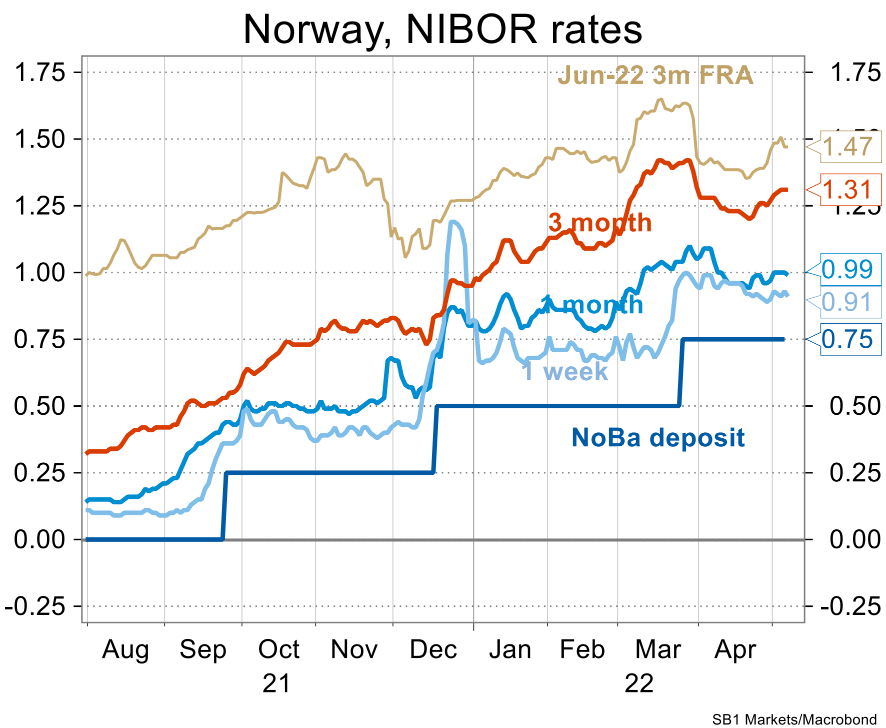


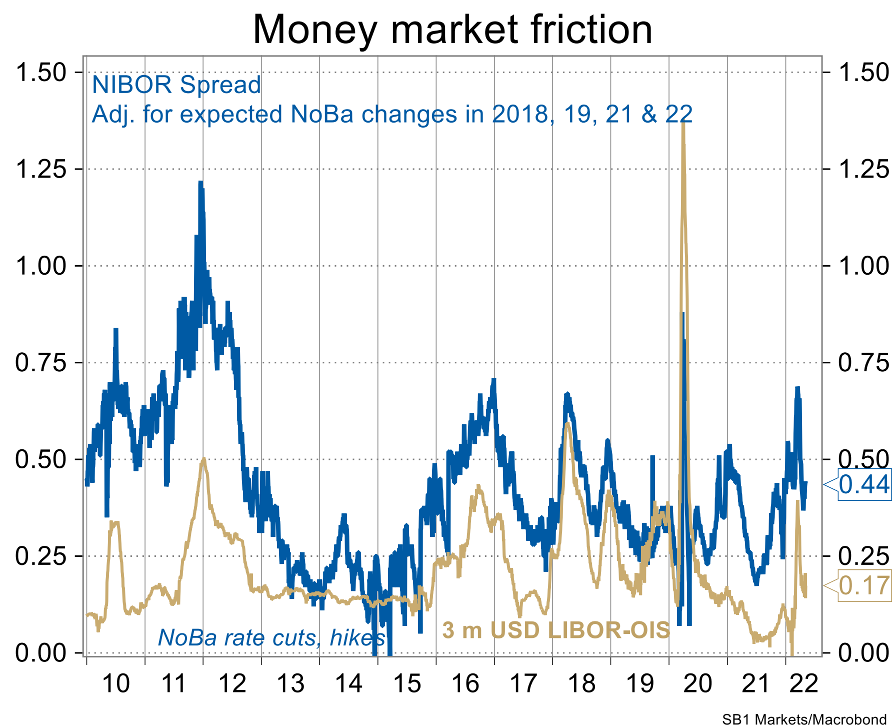


SpareBank 1 MARKETS

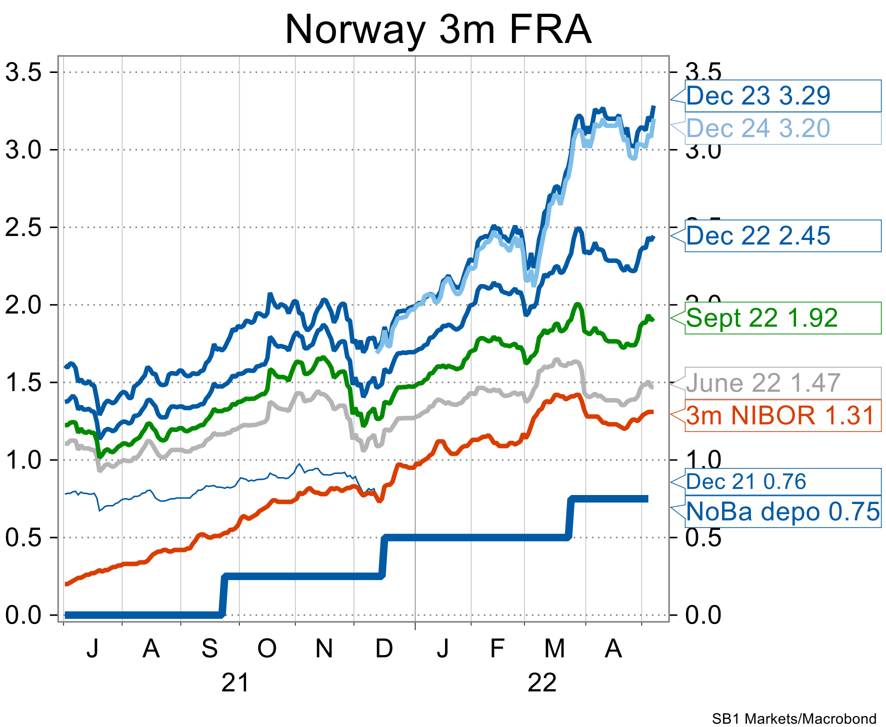
The 3m NIBOR up 4 bps to 1.31%, the NIBOR spread up 3 bps to 44 bps

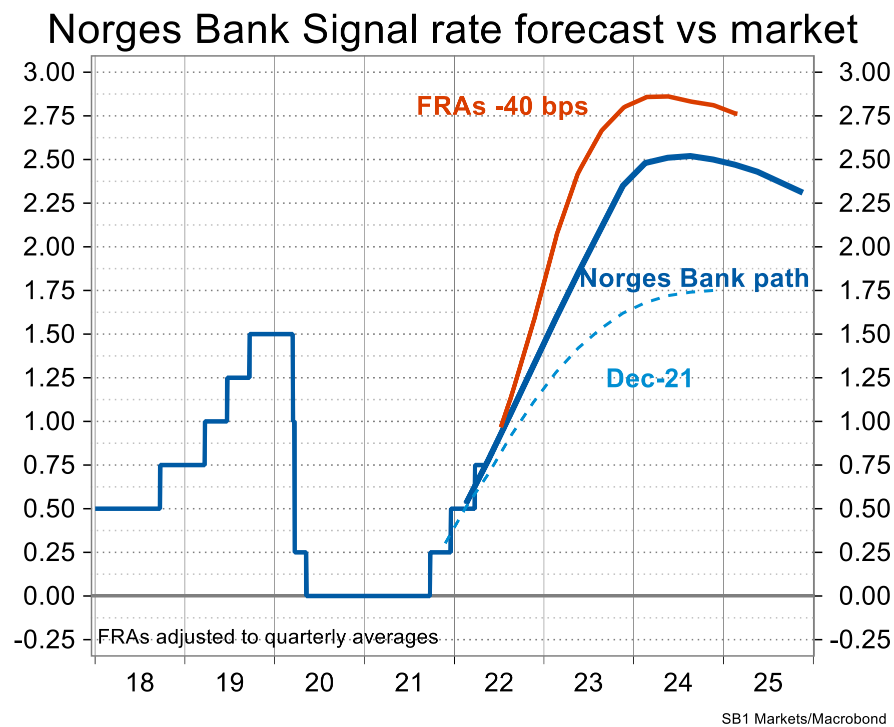
The USD LIBOR-OIS spread up 2 bps to 44





FRAs up, alongside the 3 m NIBOR. A higher NIBOR spread at least partly to blame





- The **June 3 m FRA** rose 1 bps to 1.47% last week, and the Sep contract added 6 bps to 1.92% (and Dec 10 bps to 2.45%)
  - » If NoBa hikes by 25 bps to 1% at June the 23 meeting (and no hike in August), the average deposit rate in the duration of the June 3 m FRA contract will be 0.98%
    - A 100% probability for a 25 bp hike if the assumed Q3 NIBOR spread is 49 bps. We doubt the spread is assumed to be that high. A 50 bps cannot be ruled out
    - However, as the Sept 3 m FRA at 1.92 is 45 bps above the June contract, a hike in both August and September is also an alternative
- The FRA market now discounts a 1.75% (30%) or a 2.00% (70%) signal rate in Q4 (assuming a general 40 bps NIBOR spread + a 5 bps Q4 liquidity premium)

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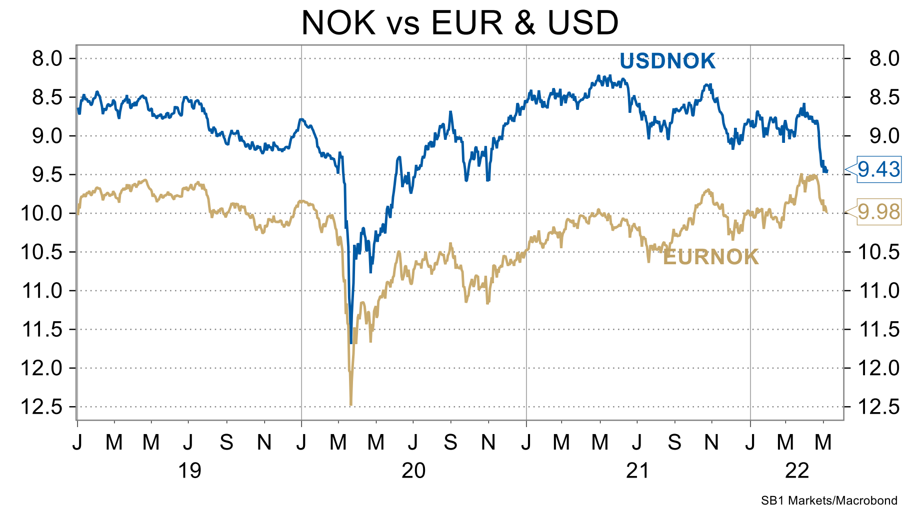
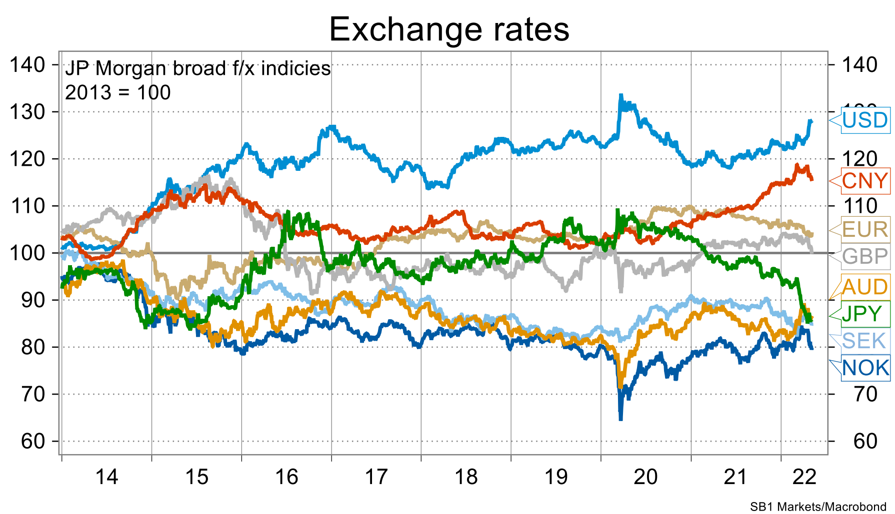
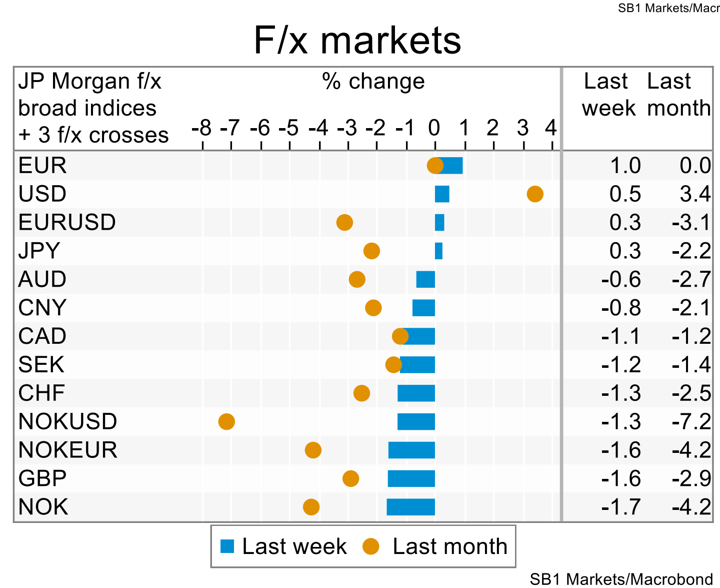
NOK lost another 1.7% last week, in spite of a higher oil price

The EUR at the top slot, after several weeks at the downside. The USD up too





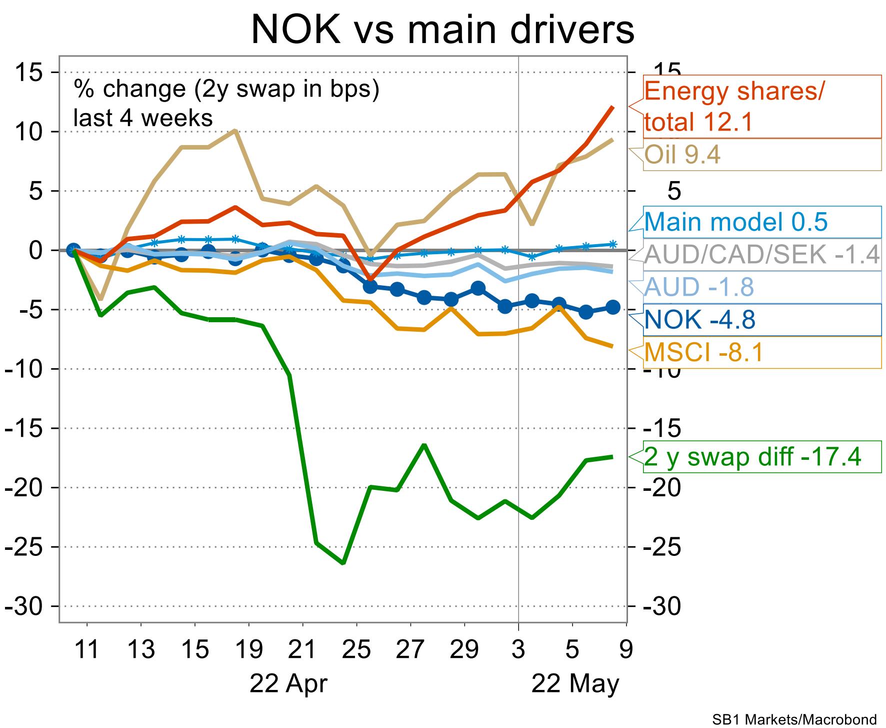


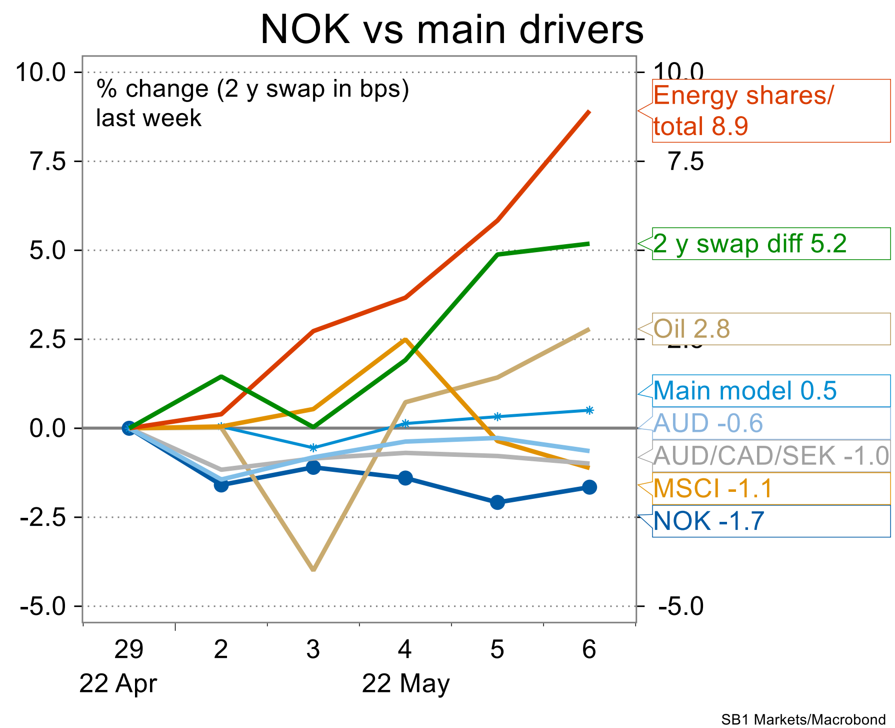
JP Morgan f/x broad indices + 3 f/x crosses	Last week	Last month
EUR	1.0	0.0
USD	0.5	3.4
EURUSD	0.3	-3.1
JPY	0.3	-2.2
AUD	-0.6	-2.7
CNY	-0.8	-2.1
CAD	-1.1	-1.2
SEK	-1.2	-1.4
CHF	-1.3	-2.5
NOKUSD	-1.3	-7.2
NOKEUR	-1.6	-4.2
GBP	-1.6	-2.9
NOK	-1.7	-4.2

SpareBank 1 MARKETS

What's up (or rather down) with the NOK?

NOK is falling even if the oil price, oil companies, and the interest spread is up. The MSCI to blame?





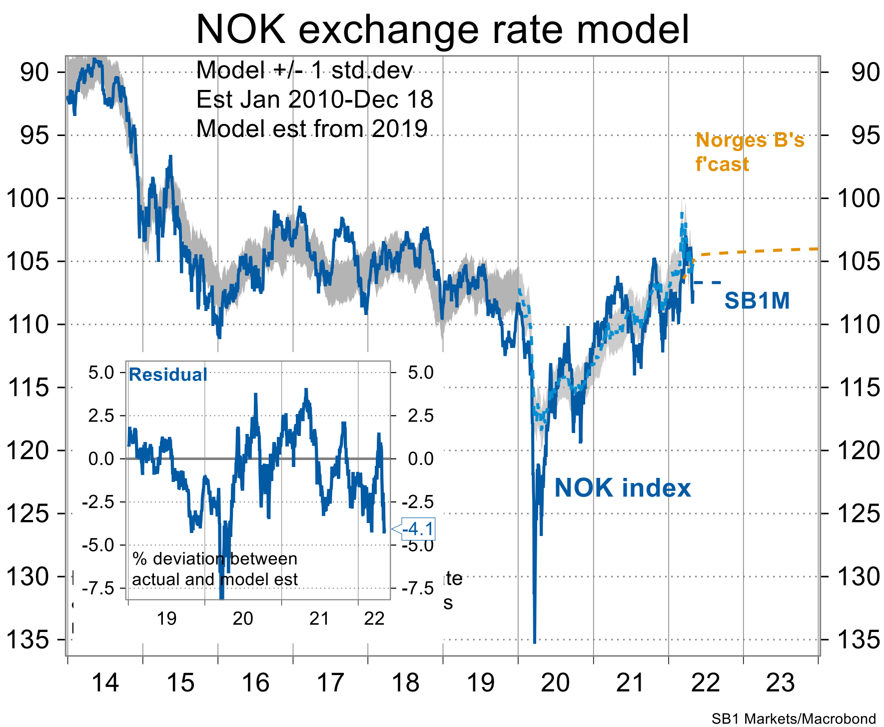
The status vs. the normal drivers – NOK the only loser

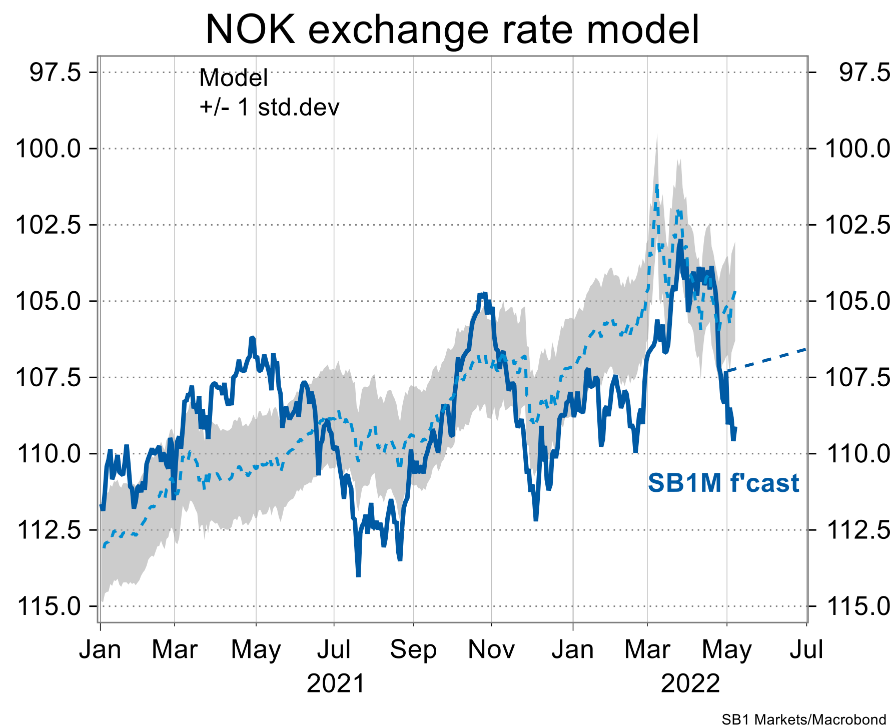
- ***The NOK -4.0% - and the NOK 2% below our main model estimate (from +1.9%)***
- The NOK is 6% weaker than our AUD/CAD/SEK-model, our 'super-cycle peers', predicts (from 5%)
- NOK is 1 % stronger than a model which includes global energy companies equity prices (vs the global stock market) (from 3)

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

The NOK suddenly down 4% vs our standard model estimate

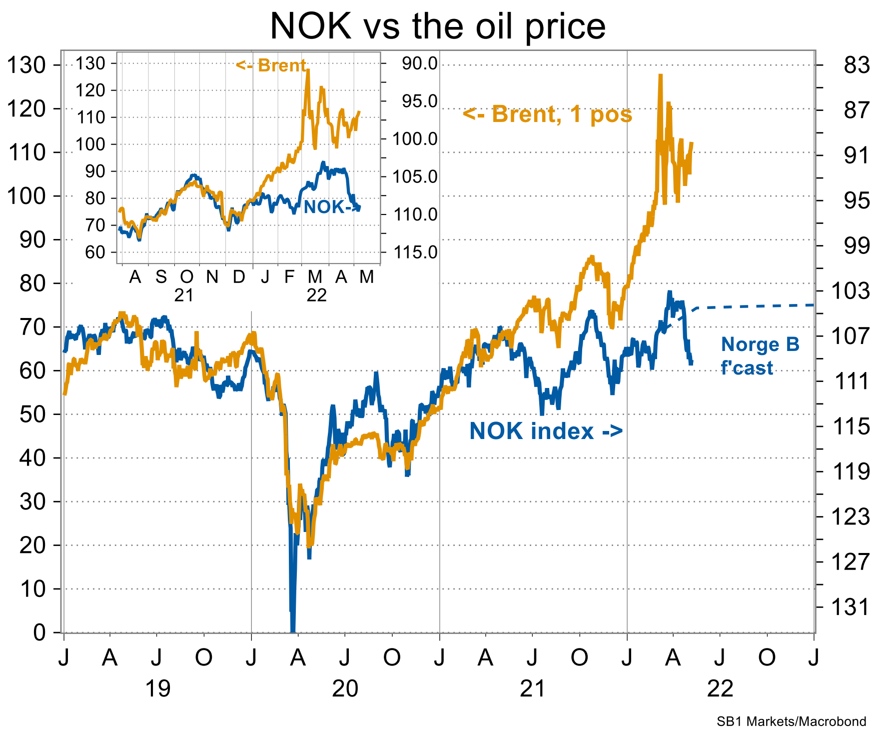
Rather unusual…

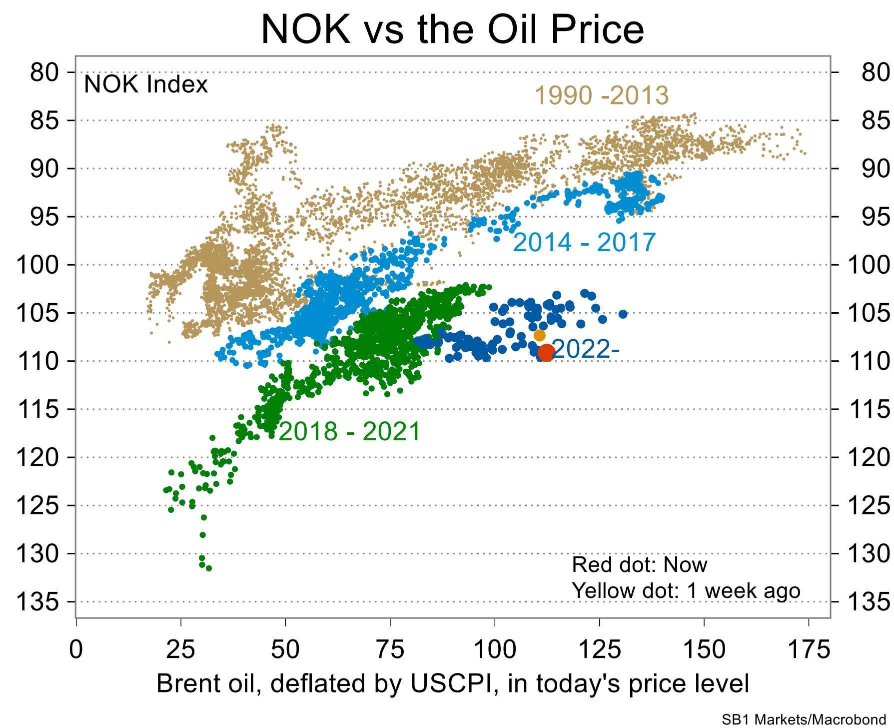




Oil up, NOK down. For the 2nd week in row!

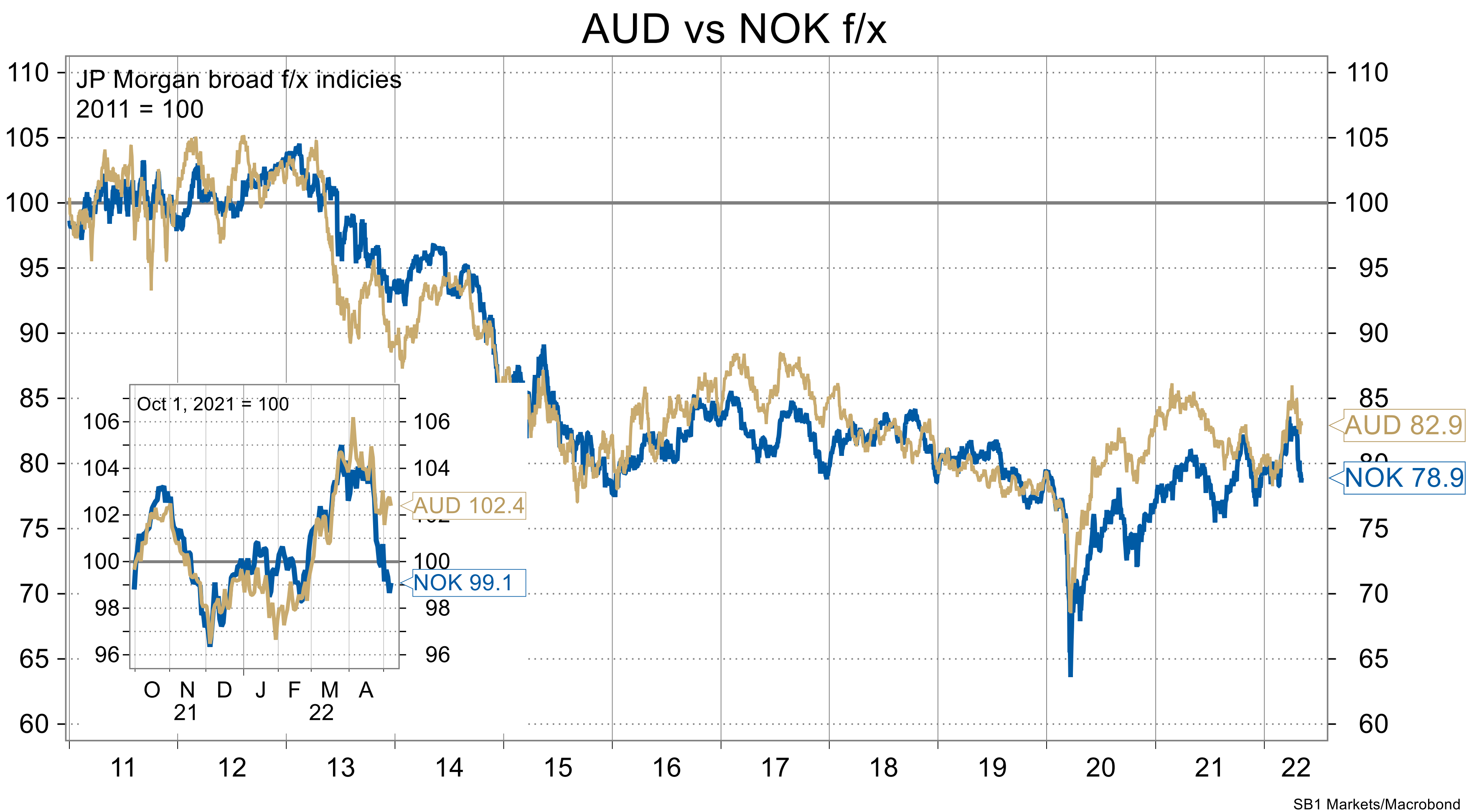
Oil & NOK have not been closely correlated so far in 2022





The NOK suddenly lost 3.5% vs. the AUD

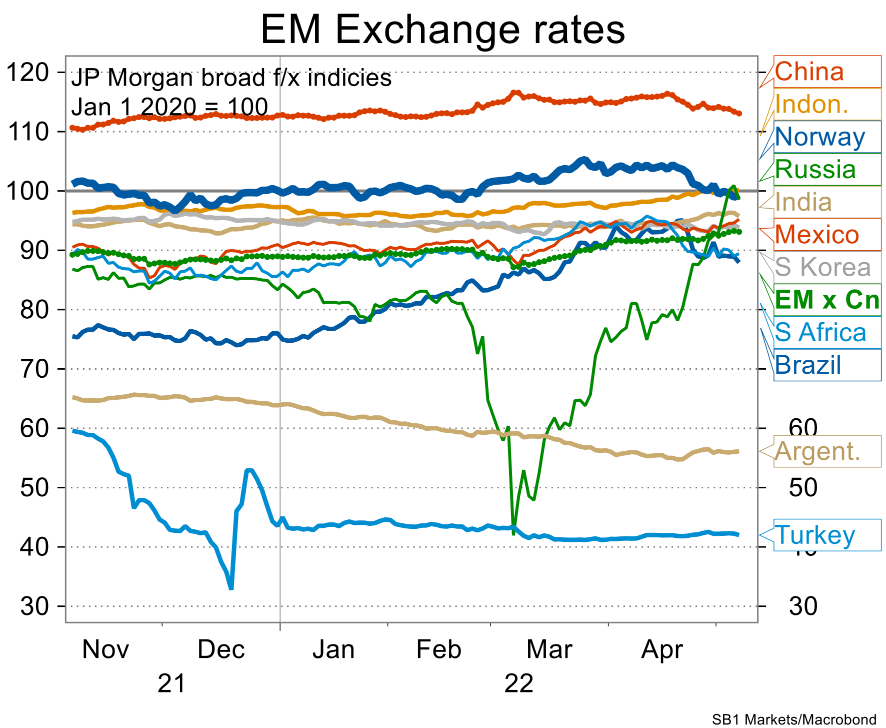
Even if the oil price are up, and metal prices fell. The RBA surprised markets with the first hike

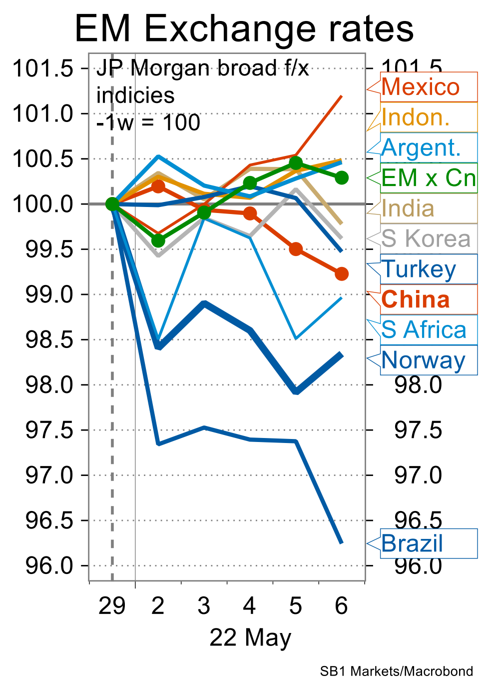


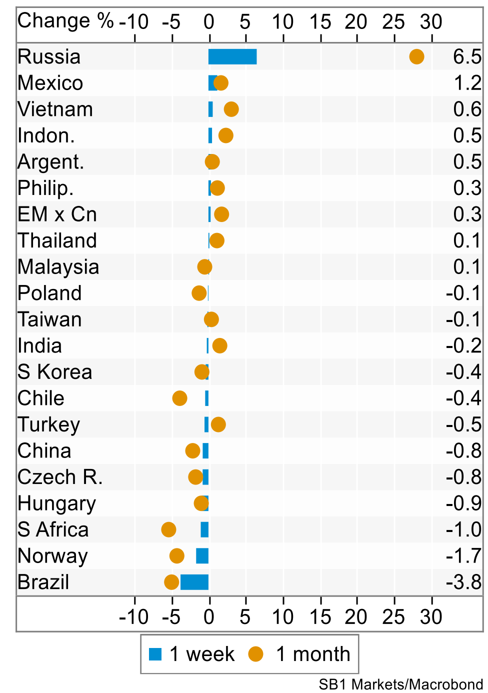
Usually, interest rate differentials have not been important for the NOK/AUD relative strength/weakness
It not usually the case but NoBa's NOK 2 bn daily selling vs. f/x for the Oil fund may weaken the NOK

The Brazilian real down, even if the economy is OK, and the central b. hiked 1 pp

Other EM currencies more up than down last week, the Russian RUB climbed 7%, up 138% vs bottom







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