July 26, 2022

Macro Weekly – Summer edition II

July 2022

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Last week

- **The War/Sanctions**
  - A **war stalemate** in south/east Ukraine, and the parties do not seem to heading for peace negotiations
  - An agreement on **exports of Ukraine grains** have been reached, which is good news. (But the loss of Ukraine supplies may have been exaggerated, just some 2% of global wheat demand is covered by Ukrainian exports)
  - **Most commodity prices** fell further last week –and they have been on the retreat since March/April. A bleaker growth outlook and probably less hoarding may explain the decline in prices. However, European natural gas prices rose again last week, even if Russian gas exports were partly restarted after the maintenance pause
- **Preliminary PMIs**
  - **The composite PMIs in the US and EMU** fell below the 50-line in July, as both were far weaker than expected. In the US, services surprised the most on the downside, in Europe the manufacturing sector (and Germany). Delivery times and prices are easing but both indices remain elevated. At the same time, new orders are contracting at both sides of the Atlantic, in a way just seen in recessions. Other US manufacturing surveys also reported a continued, and faster contraction in new orders
- **USA**
  - **Conference Board's leading economic indicators** fell more than expected in June. The 6 m average signals that the US economy is close to or into a recession with a high probability: Since 1970 a LEI at the current level has signalled all 8 of the 8 recessions, and only sent one half-false positive signal, in 2006, one year ahead of the Great recession (but then again a new signal in 2007). No false negatives either, barring the 1960 recession
  - **Housing** data confirms are further weakening of the housing market but the downside is still large vs. the warning from Homebuilders the previous week. House prices are still appreciating, but the peak is very likely near – and the downside is substantial following the 40% price lift since before the pandemic
  - **New weekly jobless claims** are on the way up. The current increase (in the 8 week average) at 1.7 pp of the labour force does not guarantee a recession but the likelihood is rather high
- **EMU**
  - **The ECB hiked** the signal rate by 50 bps, to zero. Some days before the meeting a 25 bps hike was expected by the economists but hints about a 50 bps hike made the 'double hike' more likely – and markets had anyway almost discounted it. Just as important, the ECB abolished it's forward guidance, and the next steps will be taken according to the data flow. That's what central banks do anyway, and their guidance have probably not been that helpful. FRA rates fell last week – and are well down from the peak
  - As expected, the **ECB established a new support program** (TIP) for exposed bond markets (like Italia's), with a lot of strings attached but none formalised
- **Sweden**
  - Swedish house prices fell even faster in June, by 2.1% seasonally adjusted, and at the fastest rate in Stockholm, which is now down more than 6% from the peak. Almost before any mortgage rate is lifted…
- **Norway**
  - **SSB's quarterly manufacturing survey** fell a tad more than we expected, to slightly below average. Oil related industries are still reporting growth, others a substantial weakening – like we see among our trading partners. Still demand is strong and prices will be lifted – and companies report widespread lack of labour

The Calendar: Another 75 bps Fed hike. US & EMU GDP. EMU CPI. Norw. unempl.

Time	Count.	Indicator	Period	Forecast	Prior
Tuesday July 26					
15:00	US	S&P CoreLogic CS 20-City YoY	May	20.6%	21.2%
16:00	US	Conf. Board Consumer	Jul	97.2	98.7
16:00	**US**	**New Home Sales**	**Jun**	**660k**	**696k**
Wednesday July 27					
10:00	EU	Credit growth, M3	Jun		
14:30	US	Advance Goods Trade Balance	Jun	-$103.2b	-$104.3b
14:30	US	Durable Goods Orders	Jun P	-0.4%	0.8%
14:30	US	Cap Goods Orders Nondef Ex Air	Jun P	0.2%	0.6%
16:00	**US**	**Pending Home Sales MoM**	**Jun**	**-1.0%**	**0.7%**
20:00	**US**	**FOMC Rate Decision**	**Jul-27**	**2.50%**	**1.75%**
Thursday July 28					
	GE	Retail Sales MoM	Jun		0.6%
08:00	**NO**	**Unemployment Rate AKU**	**May**	**(3.1)**	**3.2%**
08:00	NO	No. of Employees	Jun		
08:00	SW	GDP Indicator SA MoM	Jun		0.7%
08:00	SW	GDP Indicator SA QoQ	2Q	0.70%	-0.4%
08:00	SW	Retail Sales MoM	Jun		-0.6%
09:00	SW	Economic Tendency Survey	Jul	104.0	105.9
11:00	EU	Economic Confidence	Jul	102	104
14:00	GE	CPI YoY	Jul P	7.4%	7.6%
14:30	**US**	**GDP Annualized QoQ**	**2Q A**	**0.4%**	**-1.6%**
14:30	US	Initial Jobless Claims	Jul-23	250k	251k
Friday July 29					
01:50	JN	Retail Sales MoM	Jun	0.2%	0.6%
01:50	JN	Industrial Production MoM	Jun P	4.2%	-7.5%
07:30	FR	GDP QoQ	2Q P	0.2%	-0.2%
10:00	**NO**	**NAV Unemployment, not SA**	**July**	**1.7%**	**1.6%**
10:00	GE	GDP SA QoQ	2Q P	0.1%	0.2%
11:00	**EU**	**GDP SA QoQ**	**2Q A**	**0.2%**	**0.6%**
11:00	**EU**	**CPI Estimate YoY**	**Jul**	**8.7%**	**8.6%**
14:30	**US**	**Employment Cost Index**	**2Q**	**1.2%**	**1.4%**
14:30	US	Personal Spending	Jun	0.9%	0.2%
14:30	US	Real Personal Spending	Jun	0.0%	-0.4%
14:30	US	PCE Core Deflator MoM	Jun	0.5%	0.3%
Monday, August 1					
03:45	CH	Manufacturing PMI Caixin	Jul	51.5	51.7
08:30	SW	Manufacturing PMI	Jul		53.7
10:00	EC	Manufacturing PMI	Jul F		49.6
10:00	NO	Manufacturing PMI	Jul		56.4
10:30	UK	Manufacturing PMI	Jul F		52.2
11:00	EC	Unemployment Rate	Jun		6.6%
15:45	US	Manufacturing PMI	Jul F		52.3
16:00	US	Construction Spending MoM	Jun	0.4%	-0.1%
16:00	**US**	**ISM Manufacturing**	**Jul**	**52.6**	**53.0**

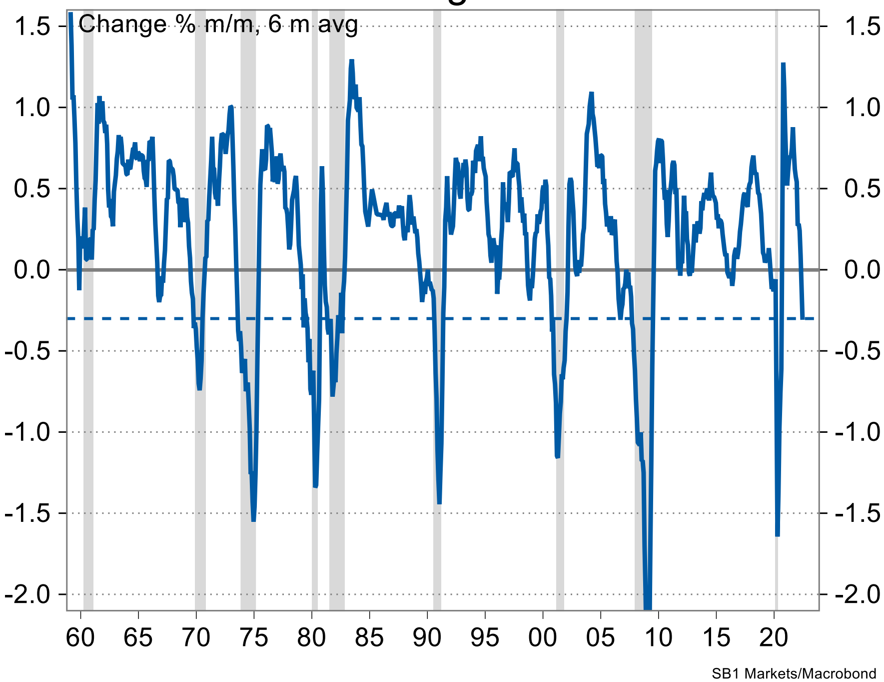
- **USA**
  - » **The Fed Reserve** will lift the signal rate by another 75 bps, barring a stock market crash before the meeting. A 100 bps hike has been on the table but given signs of slowdown in the economy, we think that is rather unlikely. We think the forward guidance will be nuanced, as economic activity is weakening – but the labour market remains extremely thigh, wage inflation is far too high – as is inflation too, of course
  - » **GDP** is expected up by 0.4% in Q2 (one week ago, the forecast was 0.8%).The nowcasters are all over the place. Atlanta Fed's gauge suggests a 1.6% decline, which seems rather pessimistic
  - » **More housing data**: New home sales and house prices. Sales have fallen substantially already but prices are still on the way up, they are lagging, as the normally do. But the peak is probably near, after the 40% lift in prices during the pandemic
  - » Perhaps the most important data point: **The Employment cost index**. A slowdown is expected in Q2 but a close to 5% growth rate is still too high to reach 2% price inflation over time
- **EMU**
  - » **GDP** probably grew in Q2. A 0.8% growth rate is expected vs. 2.4% in Q2 (or 0.2 vs. 0.6% not annualised)
  - » **HICP (CPI) inflation** will remain at very high levels. Electricity prices rose further and core inflation is way above the price target (albeit far lower than in the US)
- **Norway**
  - » **LFS unemployment** was revised up in April but the trend is down – and we expect a further reduction in May as demand for labour remains brisk
  - » **NAV registered unemployment** has fallen steadily too, but we expect the seasonal adjusted rate to remain at 1.7% in July (due to rounding)
  - » Even if Mainland GDP fell in both April and May, the **no. of employees** rose further, and we expect a further lift in June

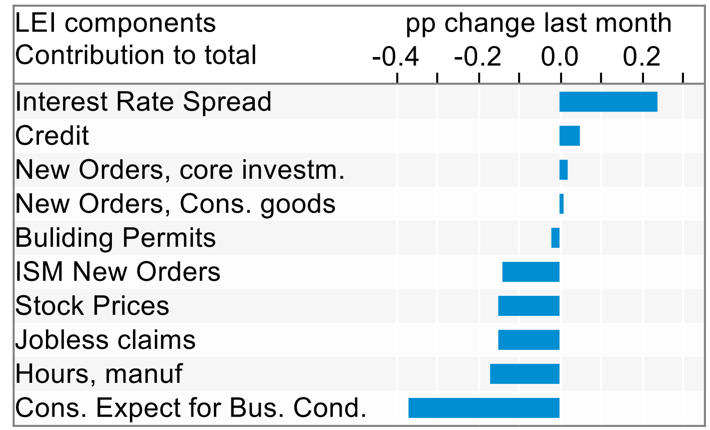
Sources: Bloomberg. SB1M est. in brackets. Key data are highlighted, **the most important in bold**

The Leading Economic Indicators suggest US is in or close to a recession

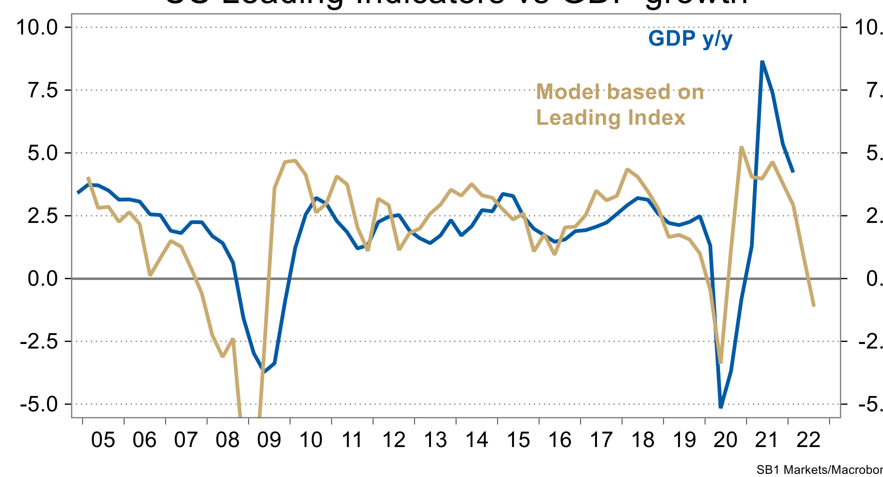
A 6-month avg at June's -0.3% level detected 8 of the 8 past recessions, just ½ false positive, 1 false neg.

USA Leading indicators





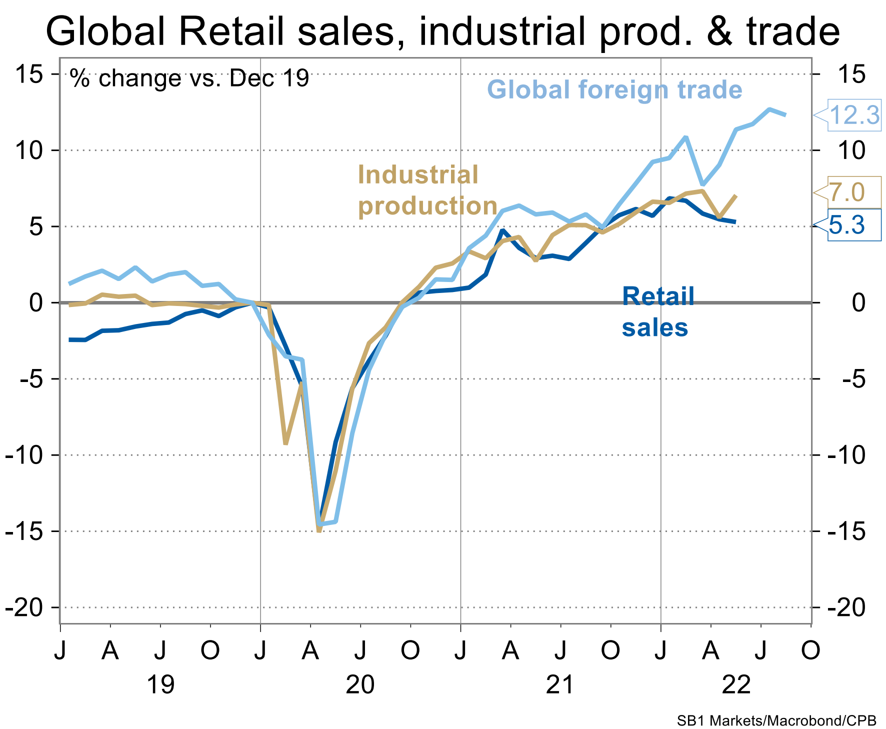
US Leading Indicators vs GDP growth

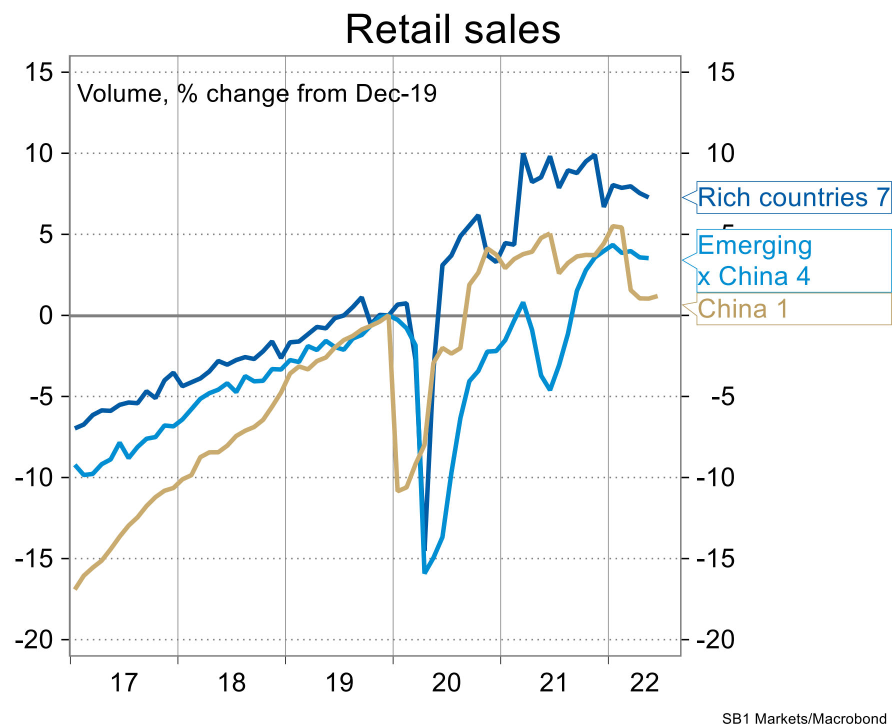


- The LEI fell 0.8% in June, 0.3 pp more than expected
- The 6 m average fell to -0.3%. The LEI has fallen to this level 9 times since 1959
  - » On 8 these occasions the US economy was very close to or had entered a recession, the 9th took place 1 year before the 2007-recession started (a ½ false positive)
  - » Thus, the LEI 6 m avg at -0.3 'detected' all 8 recessions since 1970, and barring the 2006-signal, no false positives
  - » In 1960, US entered a recession without any clear warning sign from the LEI, the only false negative

Global manufacturing production up in May, thanks to China – but is flattening?

Retail trade is trending down. China at the bottom



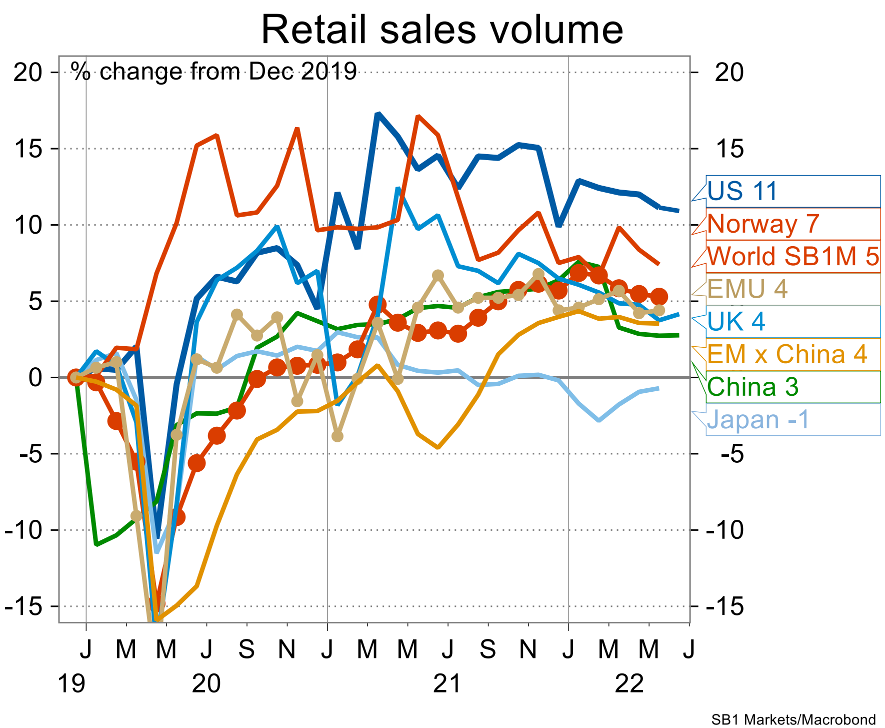


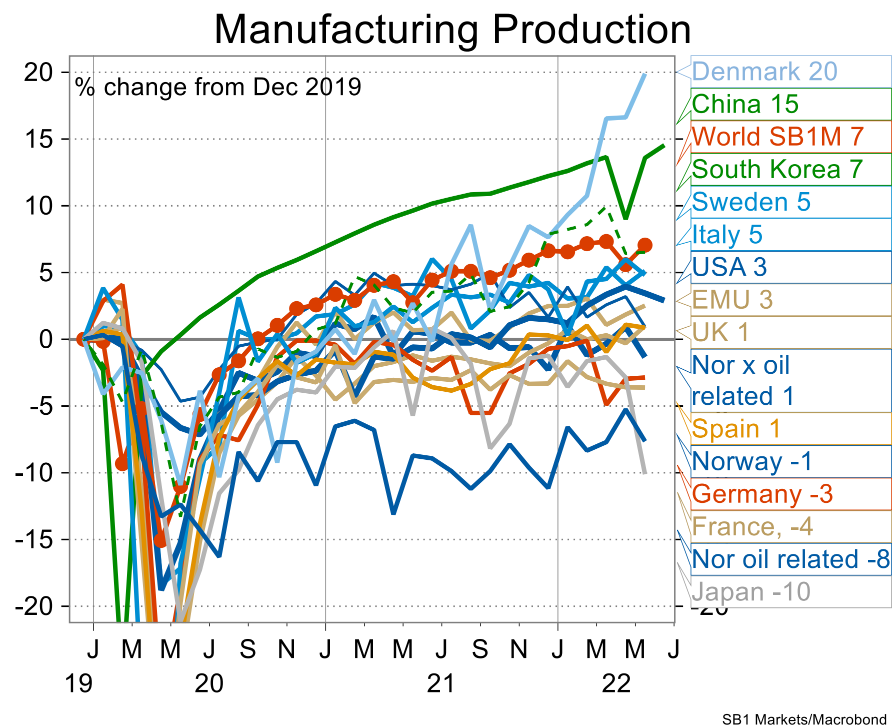
- Global foreign trade is still trending upwards

Global trade: The last months are estimates from the Kiel Institute, they are also making a prognoses for the next month based on shipping activity etc.

The decline in retail sales is broad based.

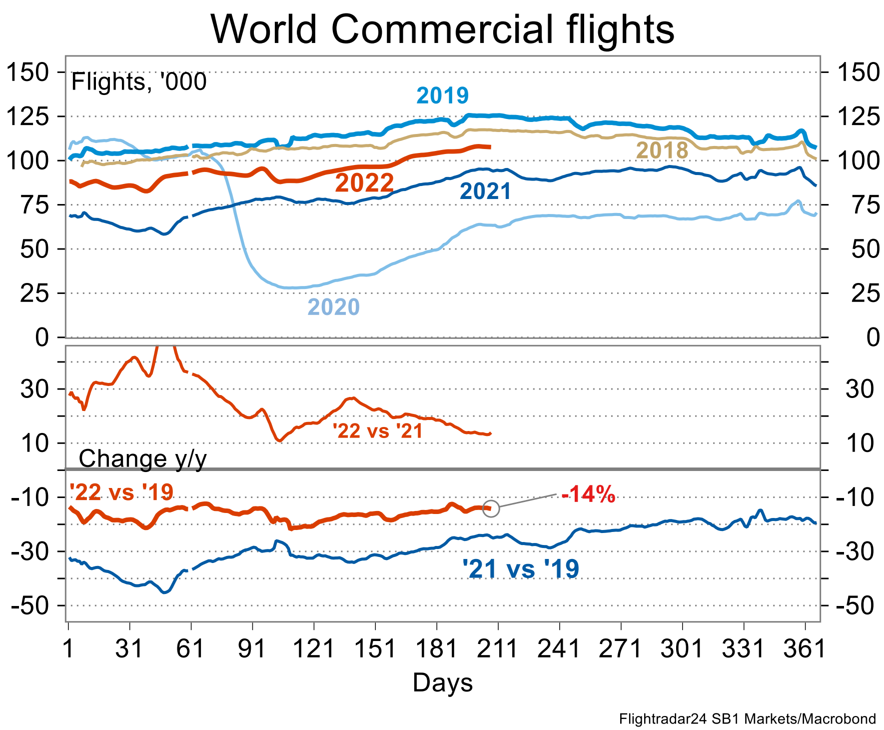
Manufacturing production is trending upwards – and is exposed?

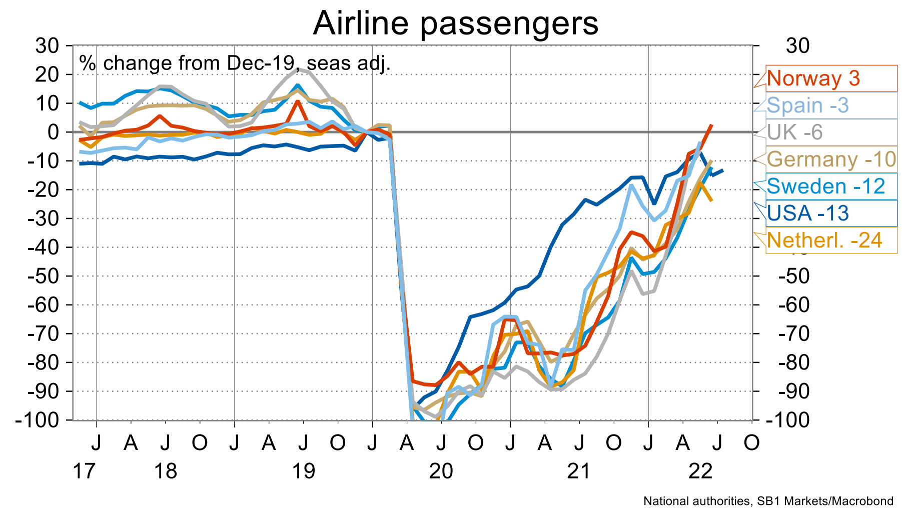


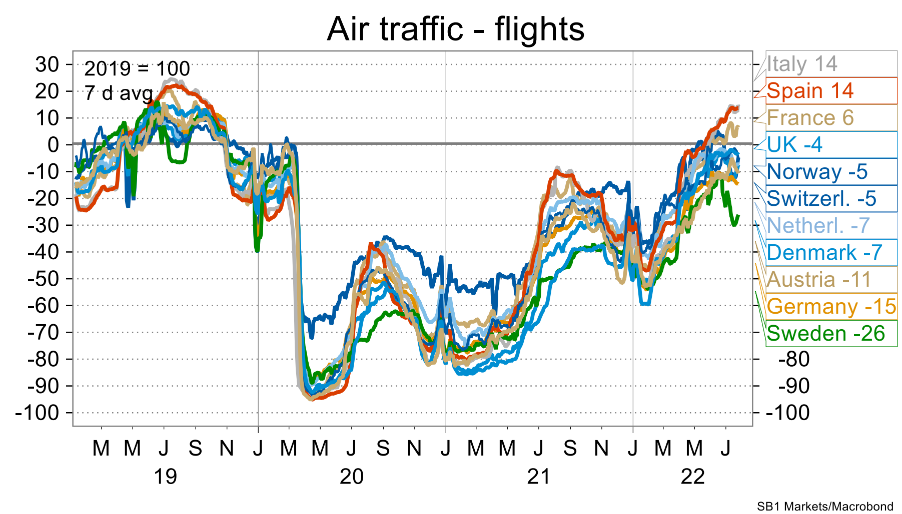


Global airline traffic has flattened recently, still down 14% vs. 2019

and finally marginally more than the seasonal normal



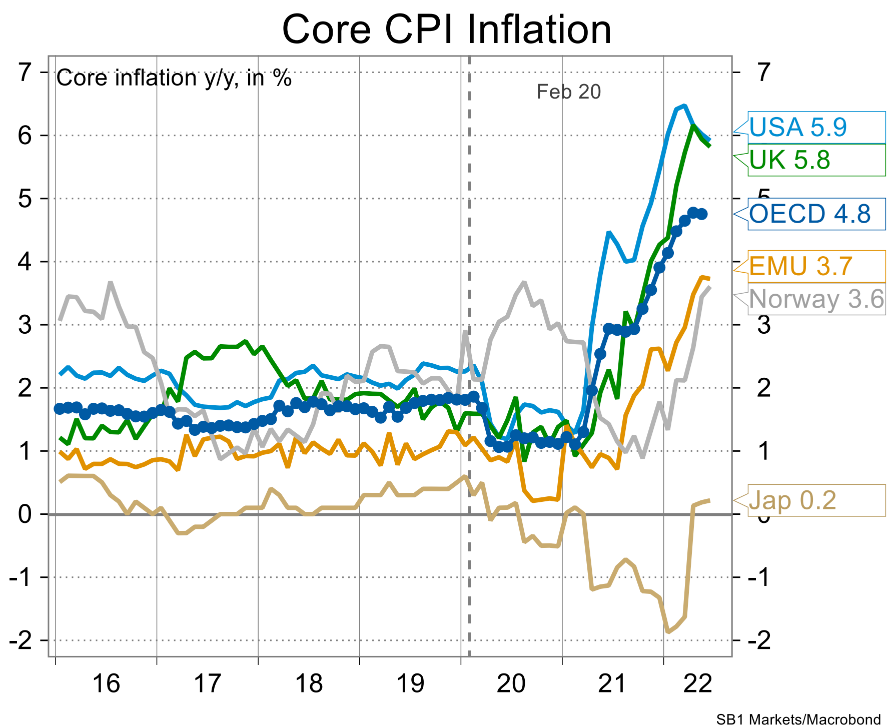


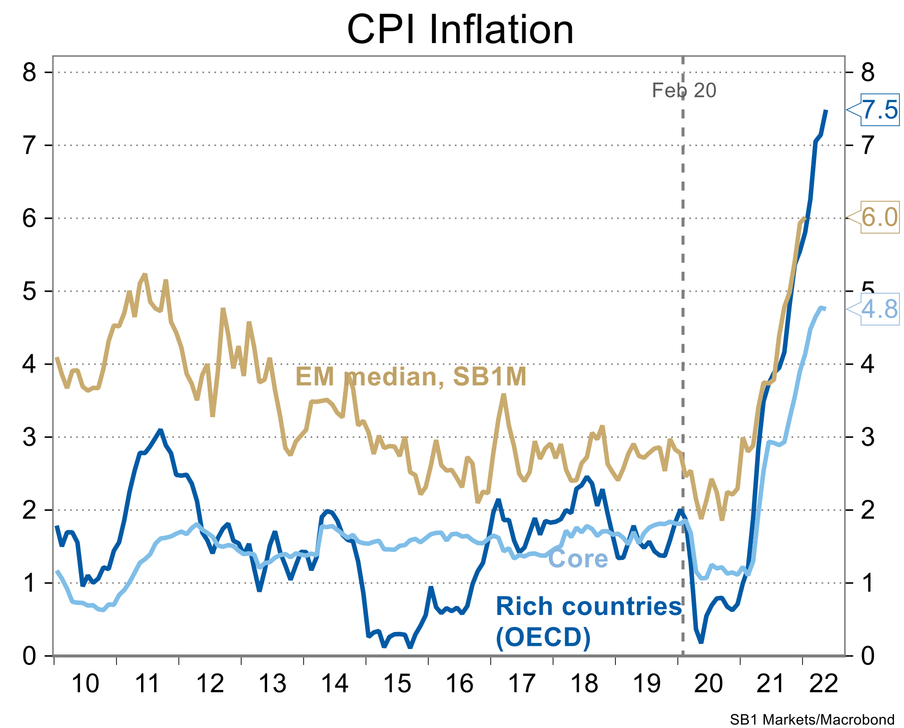


Global trade: The last months are estimates from Kiel Institute

Inflation still the main challenge most places

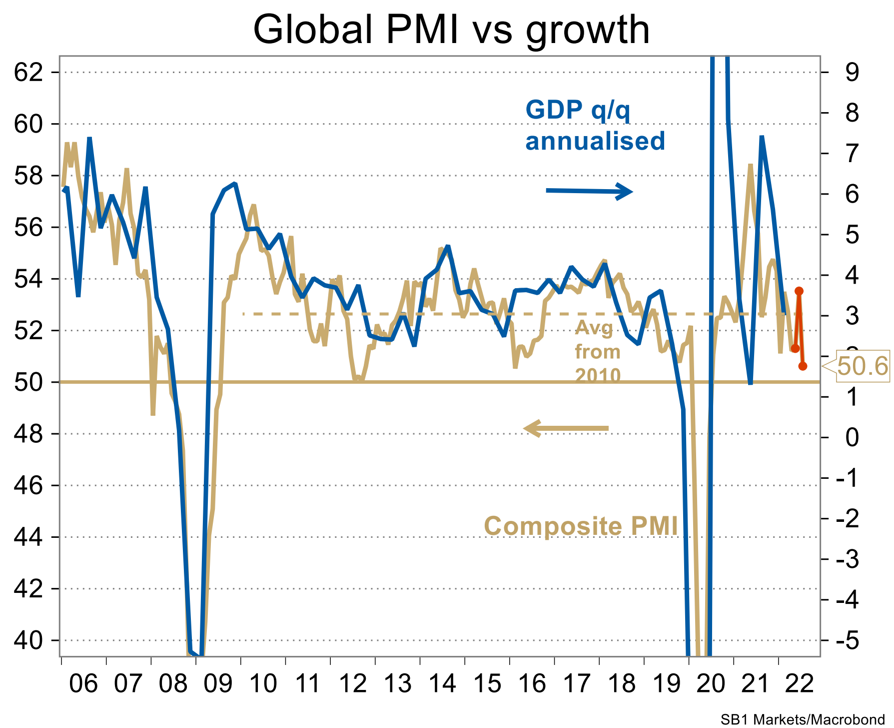
Energy prices the main culprit, but core prices are also contributing. However, some peaks are seen?

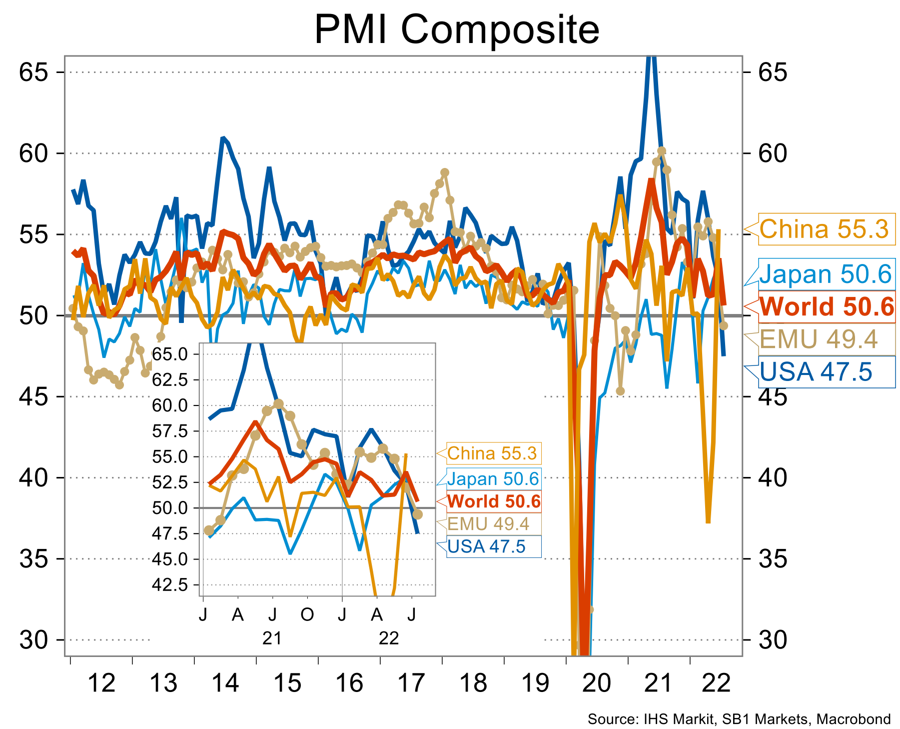




The composite PMI very likely sharply down, the US and the EMU PMIs < 50

Our uncertain preliminary global estimate is for a decline at almost 3 p to 50.6, the lowest since 2016



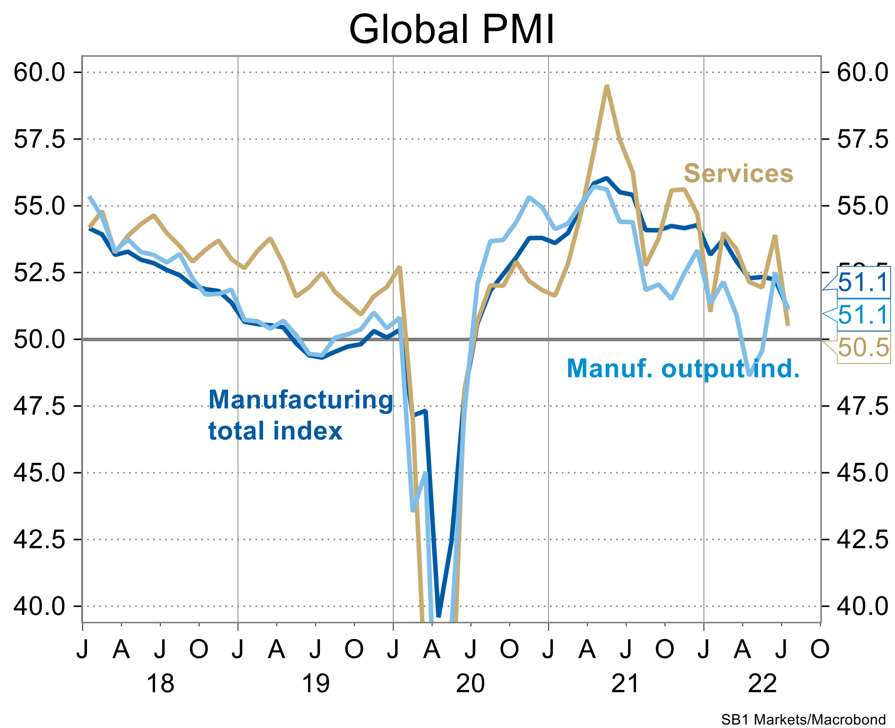


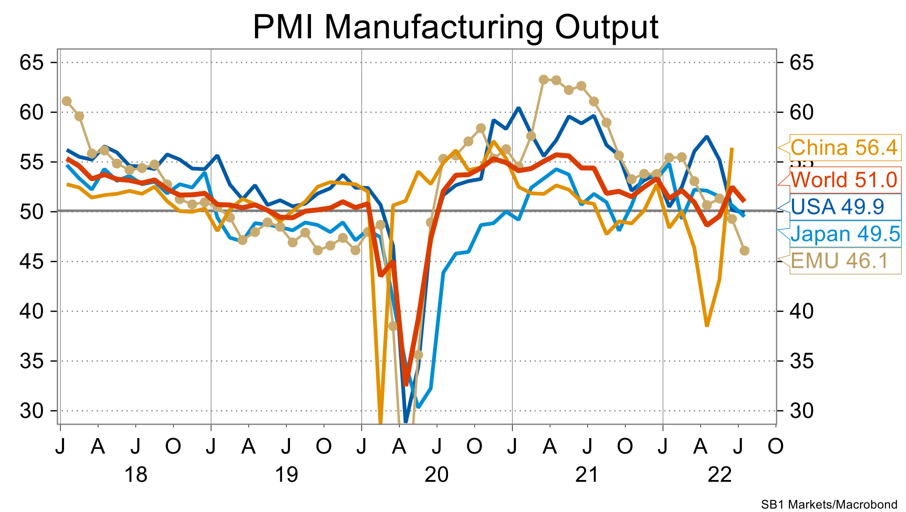
- The composite PMIs fell sharpy in both the US and in the EMU, and declined in Japan and the UK as well. The level signals a global GDP growth rate at less than 2%, which is often referred to as a global recession
- The US index is now at the bottom of the league, at 47.5, down 4.8 p, expected down 0.2 p to 52.1!
- The Eurozone PMI also fell sharply, by 2.6 p to 49.4, expected down 1 p to 51.0

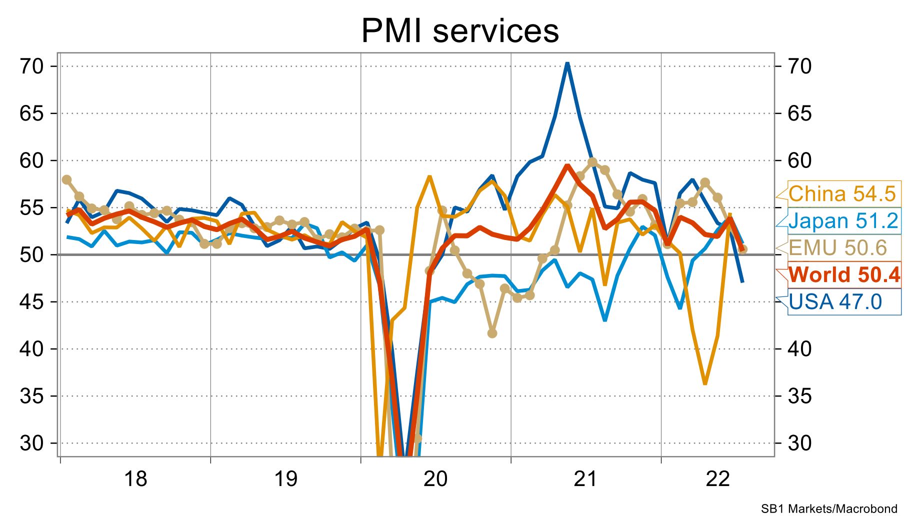
Our estimates are based on the preliminary PMIs from US, EMU, Japan UK, Australia. The estimates are uncertain, but usually by less than 0.5 p if the Chinse PMI does not change too much

EMU manufacturers and even more US services hit the wall in July

Both global manufacturing & services PMIs are trending down, and services fell the most in July



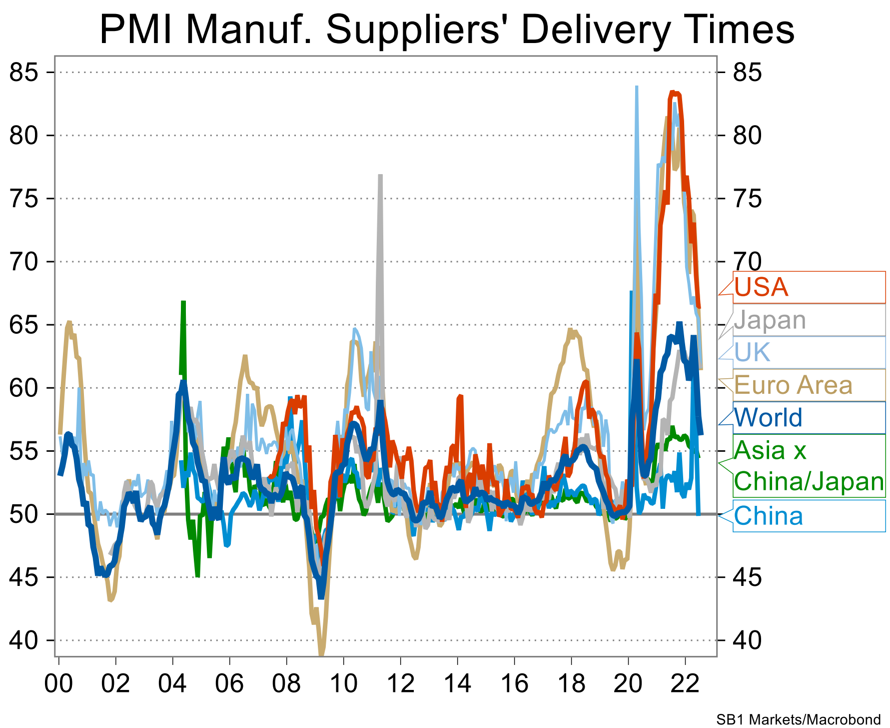


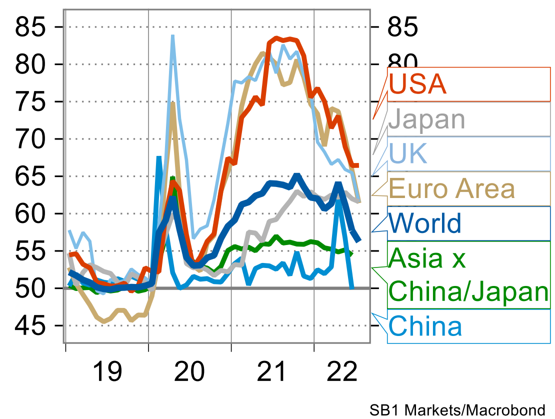


- We assume that the global service sector PMI stayed above the 50-line in July, following a 3 ½ drop. The manufacturing output index fell some 1.5 p to 51. Both fell more than expected
- The EMU manufacturing output index fell to 46.1, and the US service sector index to 47.9, both the weakest since the start of the pandemic

Delivery times index probably further down in June

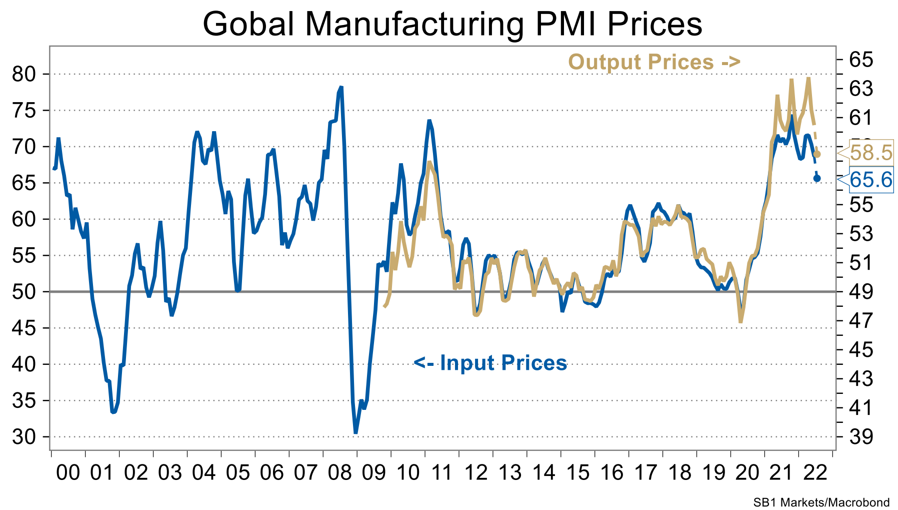
However, delivery times index was unch. in the US

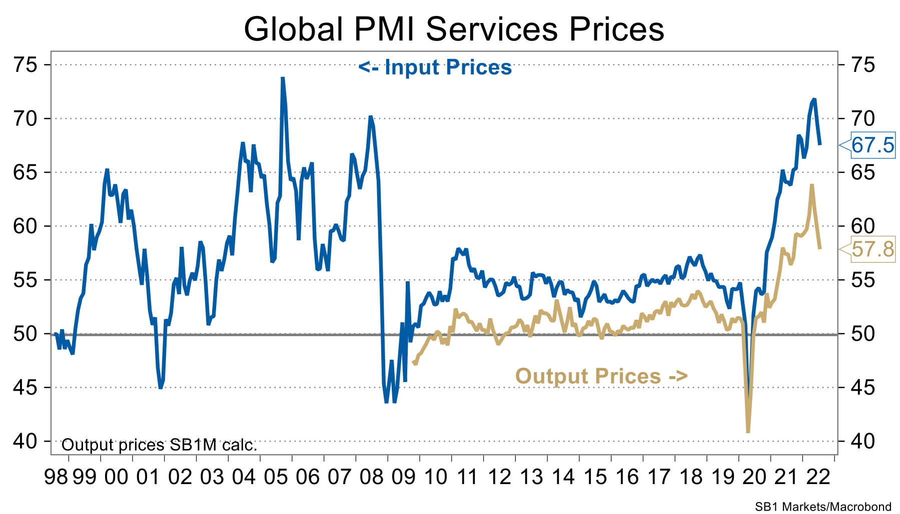


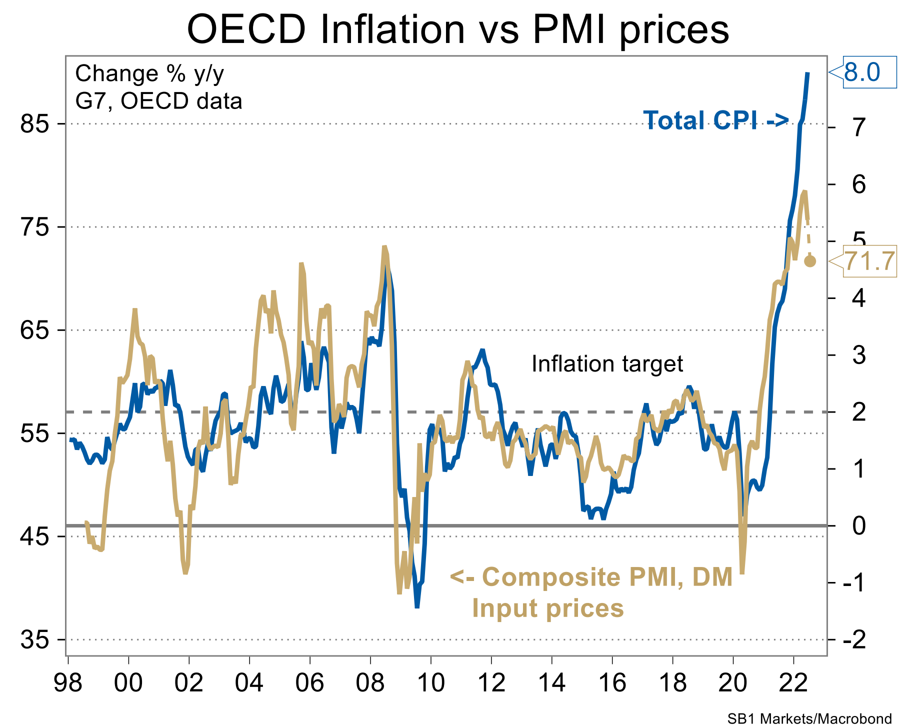


- **The global delivery times** PMI sub-index (changes in delivery times vs the previous month) has been inching down since the peak last October. The decline is broad among the Western rich countries
- **The interpretation of this index is uncertain** – are companies really reporting <u>changes</u>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

Price indices have peaked but are still reporting rapid price increases







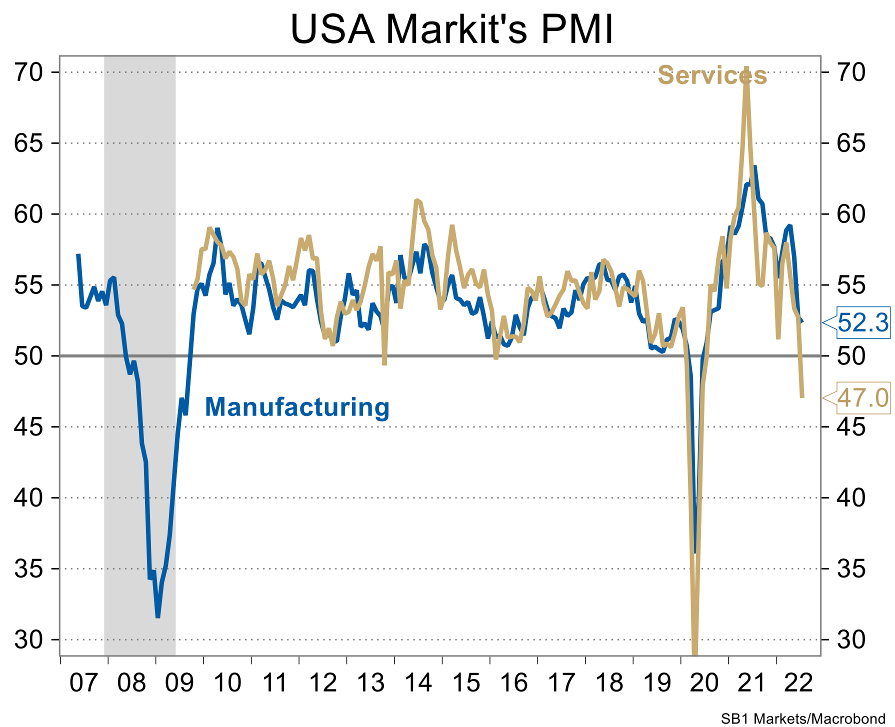
- These PMIs signal a substantial price pressure the coming months
- We are still much more concerned about wage inflation than the actual price inflation due to factors that are most likely transitory, like hikes in raw material prices, freight cost or short lived margins expansion when demand is surprisingly strong

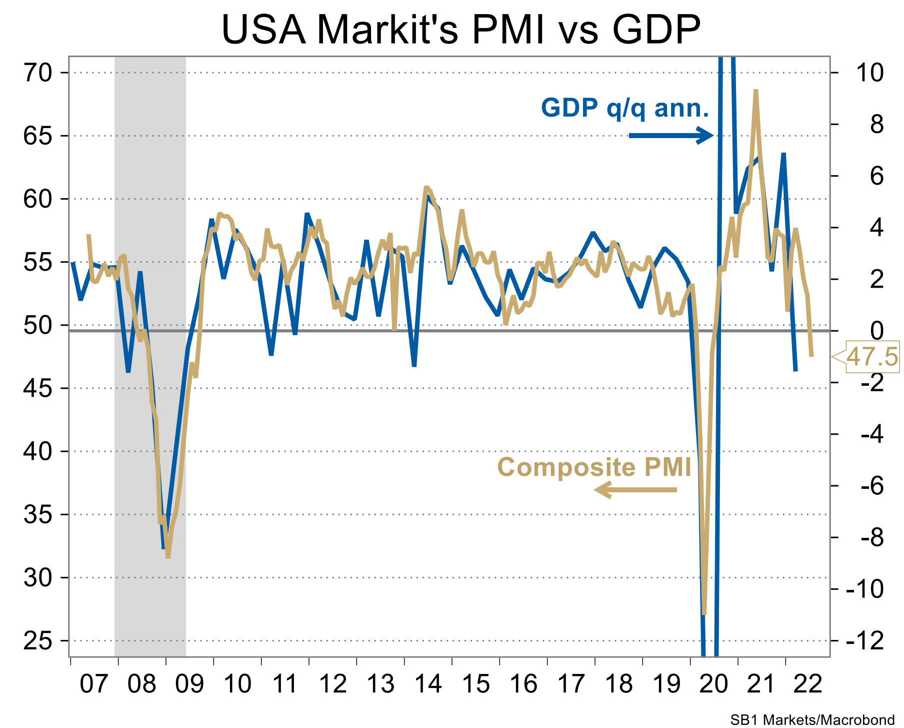
Last obs. based on preliminary PMIs from EMU, Japan, UK, and the US

SpareBank 1 MARKETS

Services & composite down in negative territory in July, manuf. slows further

The composite nosedived by an highly unusual 4.8 p to 47.5, signalling a GDP contraction, aka ….



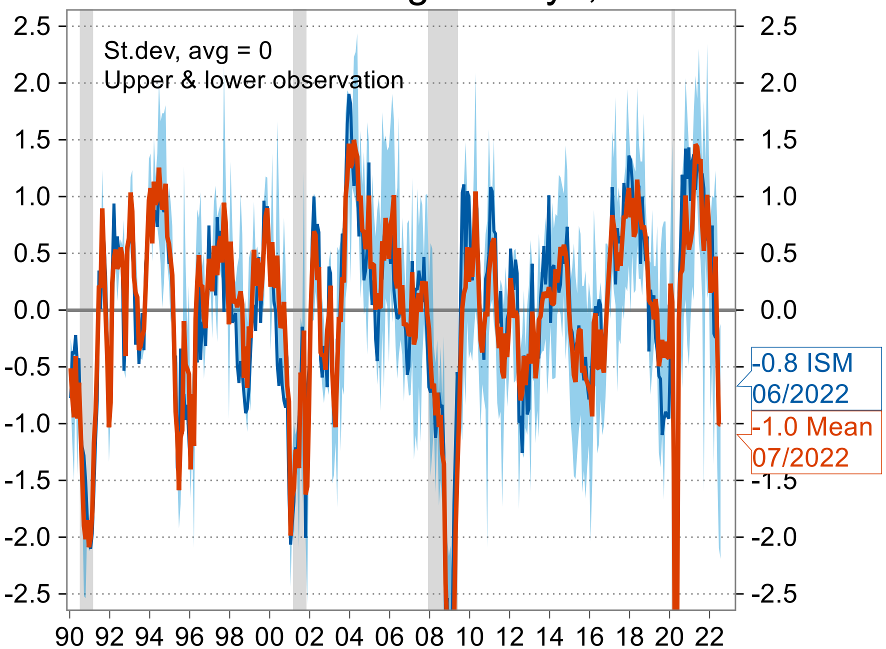


- **The composite PMI** has fallen sharply past two months, and fell below 50 for the first time since the outbreak of the pandemic
  - » The decline was due to a 5.7 p setback in services to 47.0 (expected down 0.2 p to 52.5!), and…
  - » … a decline in the output component of the manufacturing PMI by 0.3 p to 49.9. The total index fell by 0.4 p to 52.3
- **The price indices** fell sharply but are still reporting rapid price increases
- **The delivery times index** flattened, somewhat surprisingly
- **Household demand** was reported weaker due to high inflation and lack of buying power

New orders are slowing rapidly

Something hit US manufacturers in June, and so far July indices remained at the same low level

USA Manufacturing surveys, new orders

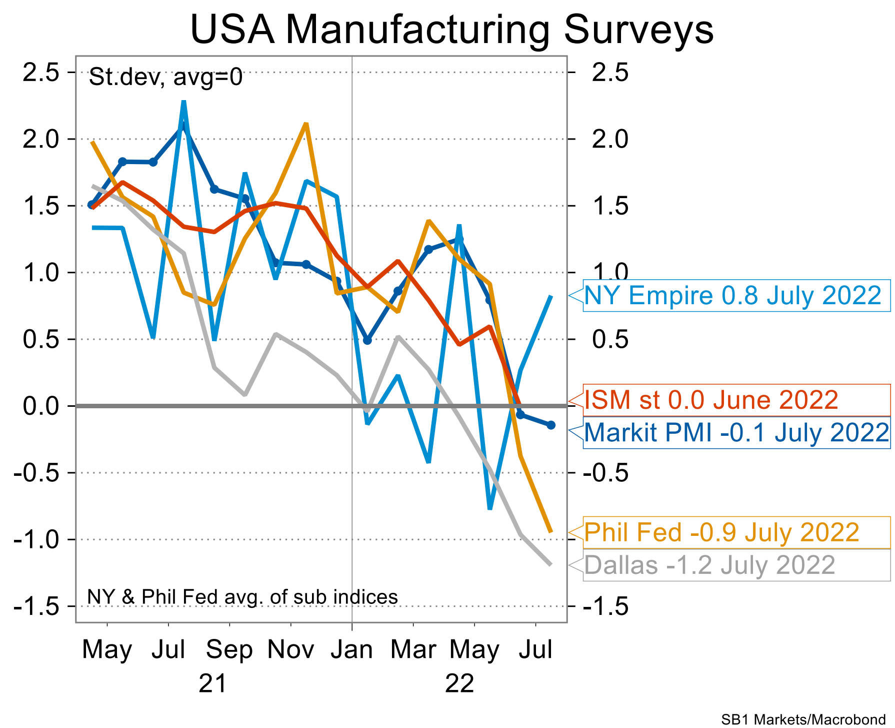


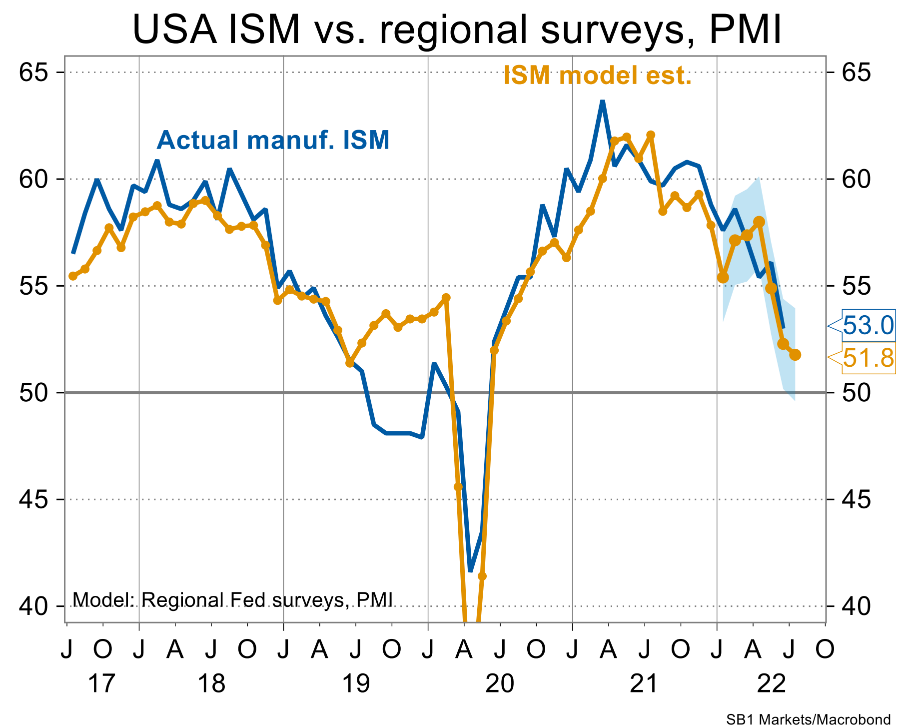
SB1 Markets/Macrobond

- Recessions have started with better new order data than these
- .. But ordre inflow indices have been even weaker, without a recession too
- On the other hand: Leading indicators sent a rather clear signal in June, check some few pages forward

NY Fed's survey against the flow, further up in July, Phil, Dallas Fed down

Markit's PMI fell marginally. In sum – and so far – the manuf. ISM signalled somewhat further down

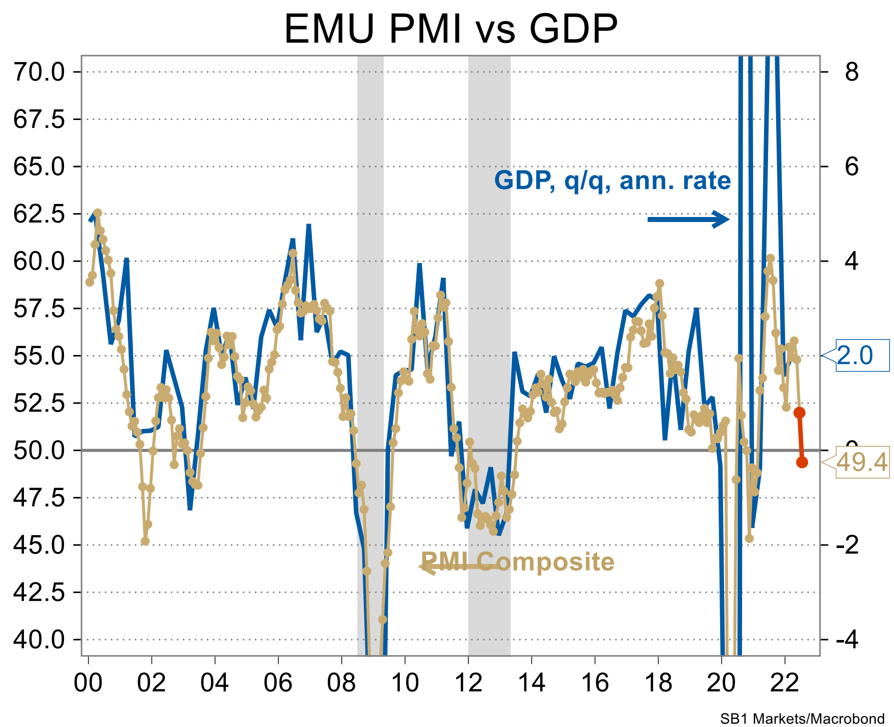


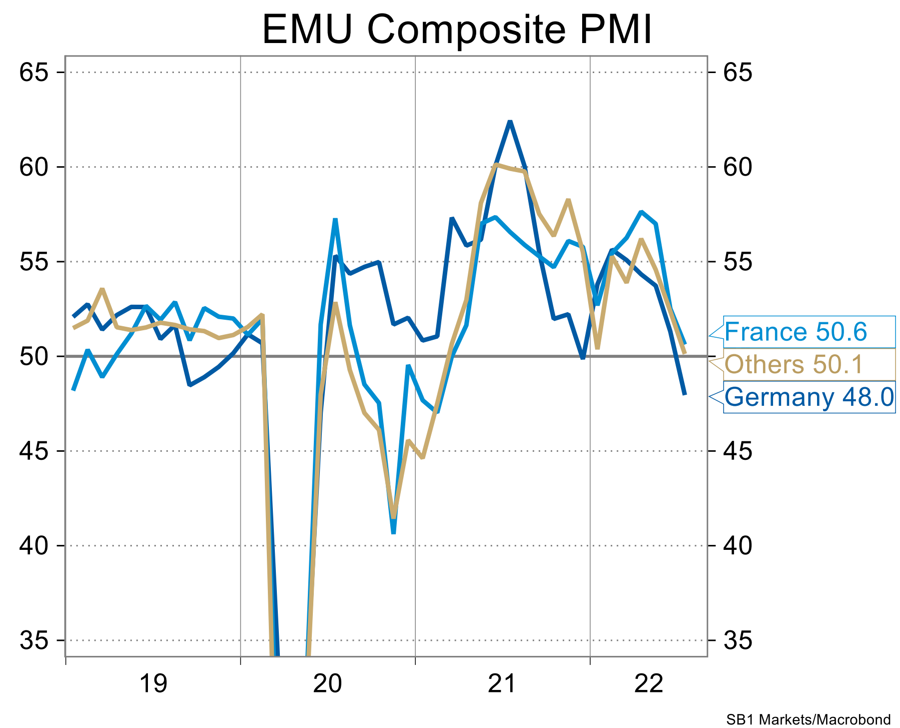


- Big picture: Growth is slowing sharply but manufacturing indices do no signal that the economy has entered a recession (even if the order indices are really worrisome)

The PMIs fell more than expected everywhere, and the composite to below 50

The German PMI fell to 48, the rest just marginally above the 50-line. How much is 'left' for the ECB?

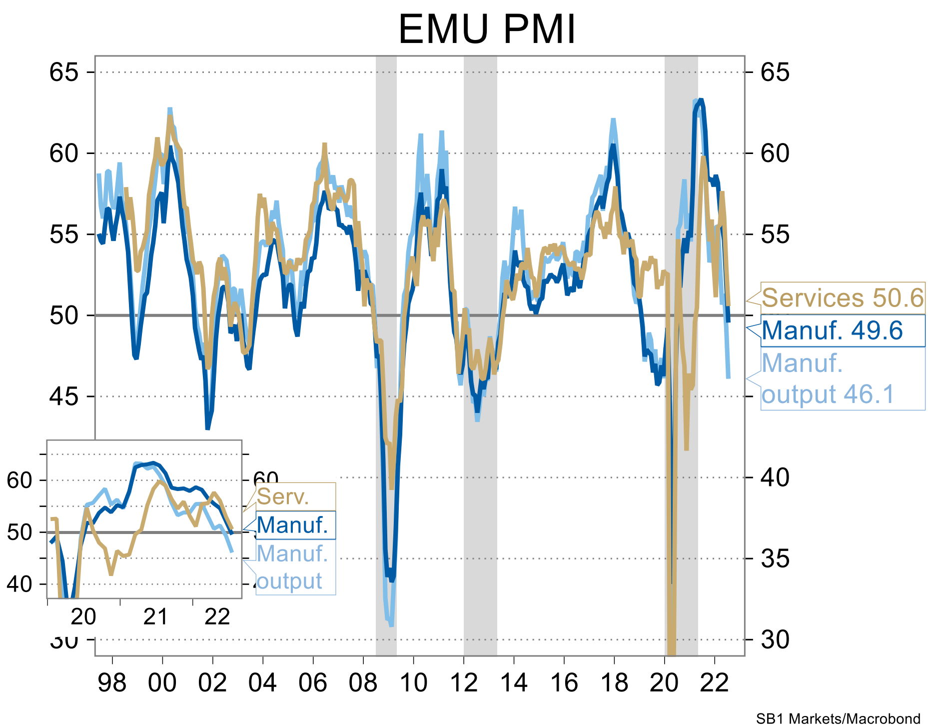


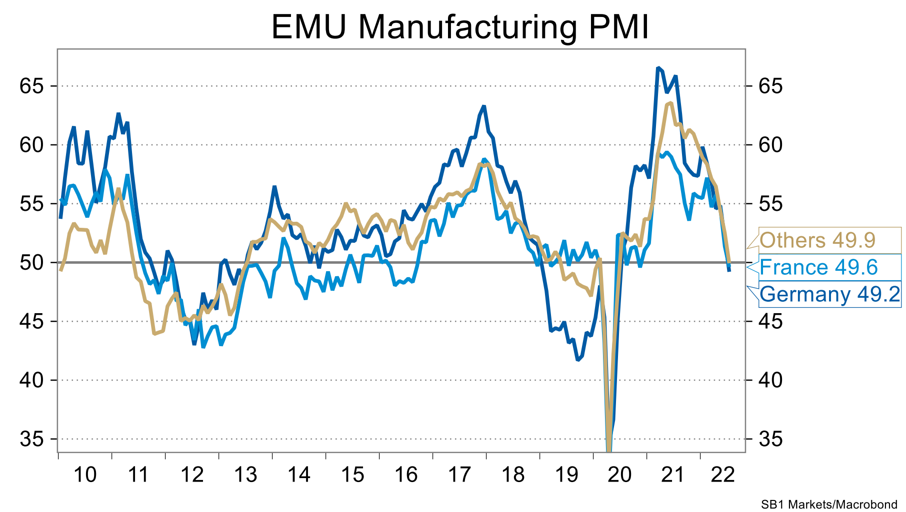


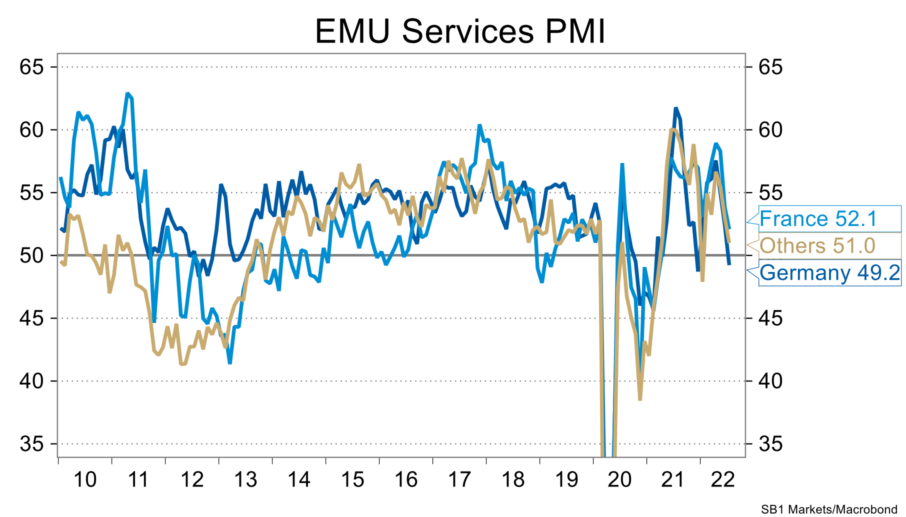
- **The composite PMI** declined 2.6 p in July, to 49.4, well below the 1 pp expected retreat to 51. The level signals a contraction in GDP
- **Services** reported much slower growth, the index fell by 2.4 p to 50.6, 0.4 p below the consensus forecast
- Manufacturing also slowed, the PMI fell 2.5 p to 49.6, 1.4 p below consensus. The output index fell 3.1 p to 46.1, and the new order index fell to 42.6 – a very weak print!
- **The delivery times** and price indices both fell substantially but still remain higher than normal. However, as new orders and production are both is declining, supply chains problems and pricing power will very likely be further reduced the coming months
- If the PMIs and other surveys continues down at the current pace, the pressure on (and within) the ECB to hike rates rapidly will no doubt fade. It is already taking place. The short/medium-term peak on the FRA curve has fallen to 1.4% (mid 2023), from 2.65% (late 2023) at the peak in mid June, following a substantial decline last week too, even if ECB hiked by 50 bps

Manufacturing has probably entered the contraction zone?

The output index fell well below the 50-line. Services are also reporting slower growth

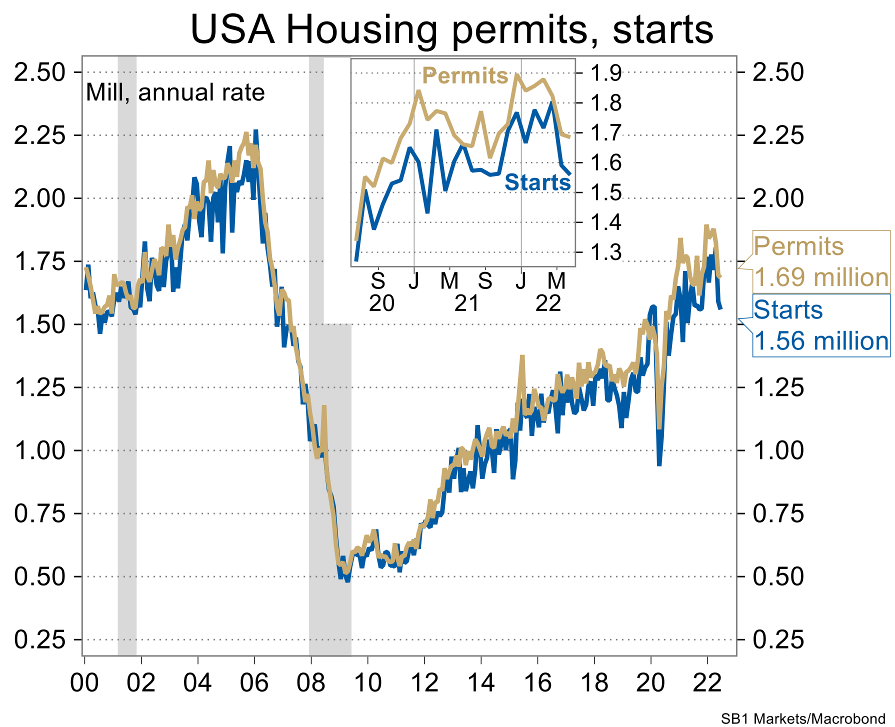


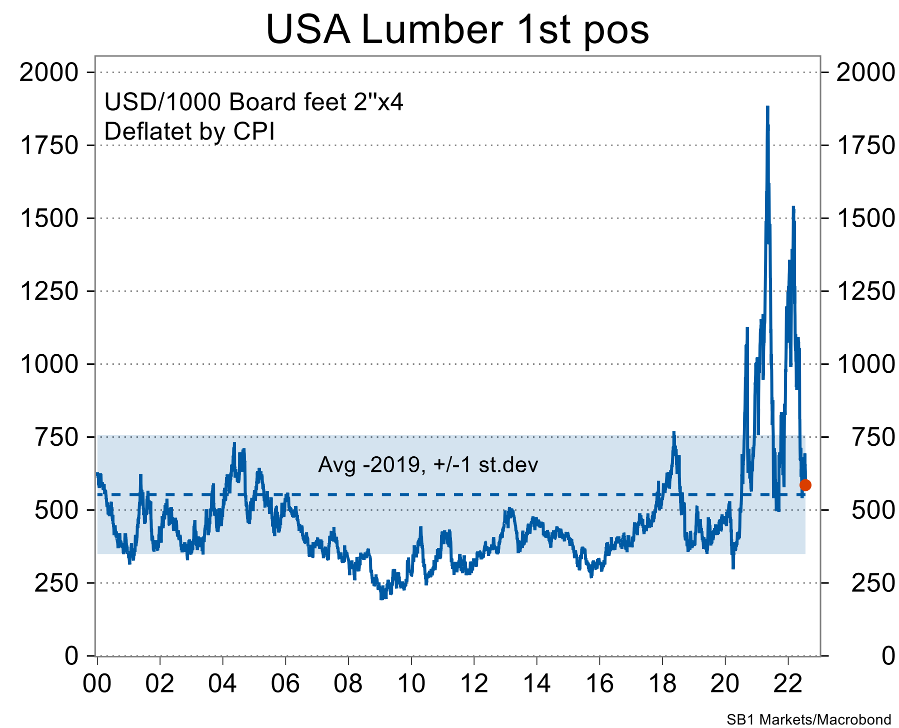




Housing starts/building permits are trending downwards

But the decline in June was not that large





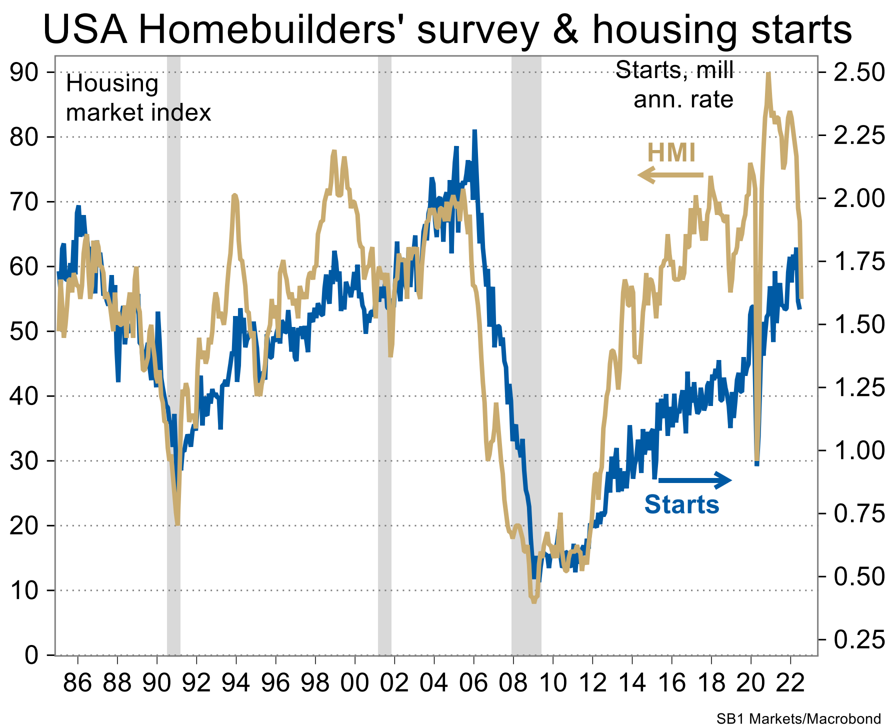
- **Housing starts** fell to 1.56 mill in June from 1.59 (revised from 1.55), expected 1.60 mil. **Building permits** landed at 1.69 mill, expected 1.68 mill, from 1.70 mill in May. Levels are still high but the tide has turned: The Housing market index shows the way, check next page
- Building <u>**material**</u> **cost inflation** has come to a sudden halt. **Lumber prices** have 'collapsed' recent weeks and are <u>now back to a normal level, steel prices are falling rapidly too</u>

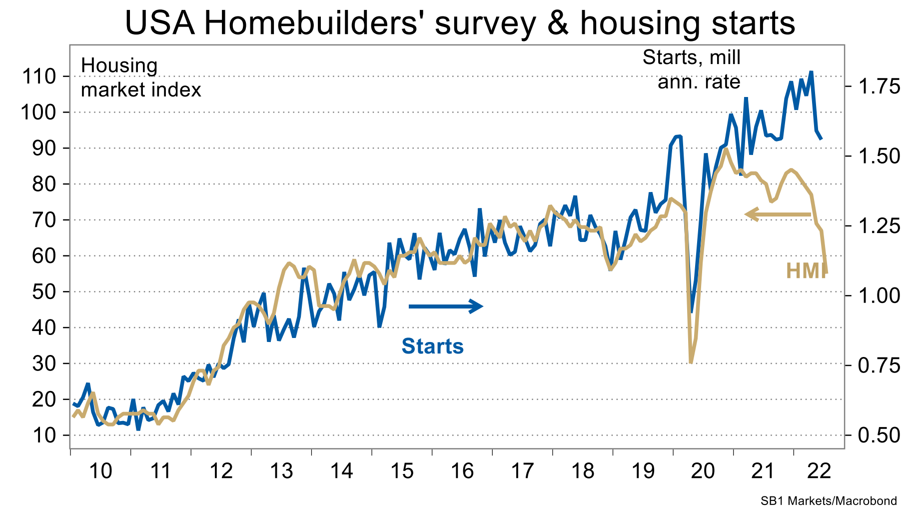
Reprint from last week's report, but still very relevant

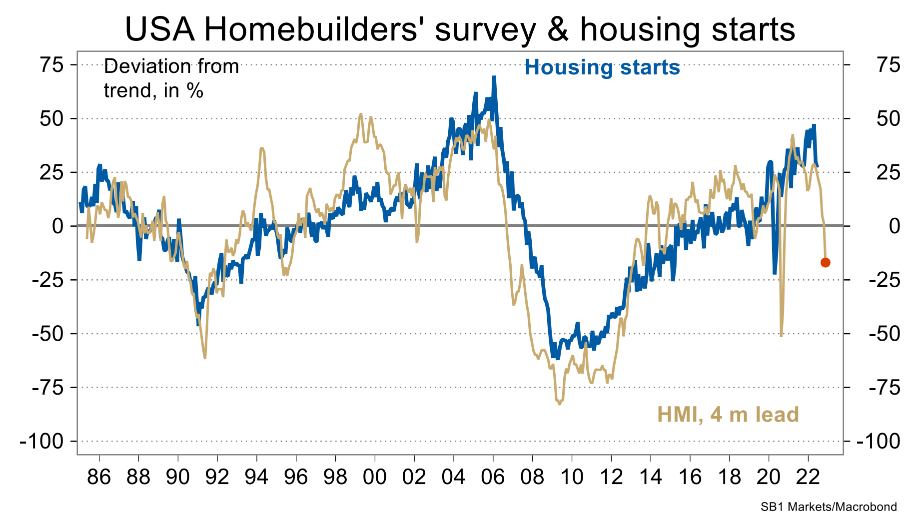
SpareBank 1 MARKETS

Homebuilders' index straight down in July: a further, steep decline in starts ahead

The HMI down 12 p to 55, the 2nd largest decline ever (after April-20). Starts down



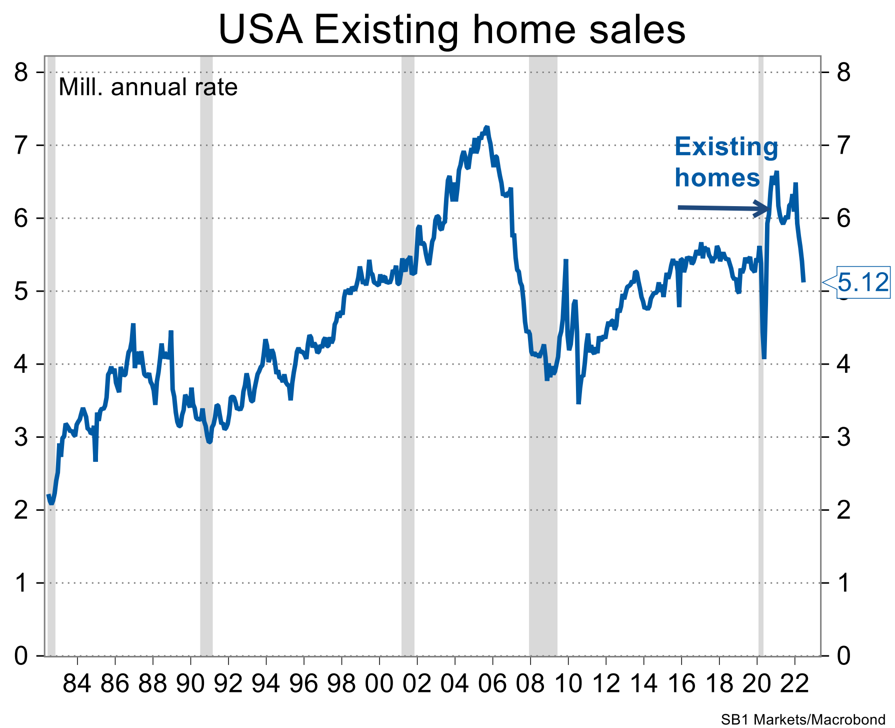


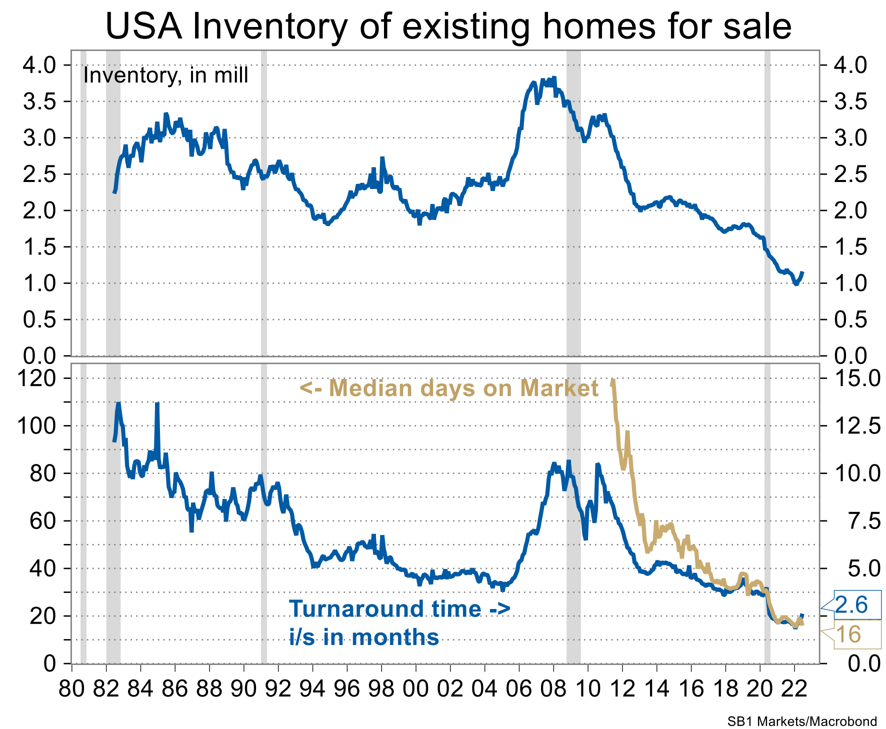


- **The Homebuilders' Housing Market Index (HM)** lost 12 p to 55 in July, expected down just 1 p! The monthly setback is unprecedented, ex. April-20 (as is the decline over the past 3, 6 or 8 months)
  - Affordability is still the challenge, due to higher mortgage rates, and soaring new home prices (at least until now)
- The decline in the index recent months signal more than a 1/3 decline in housing starts – which already has fallen by 14% - in sum a 50% setback

Existing home sales further down in June, and price inflation almost down to 0

The inventory is still very low – but has increased marginally the past 4 months

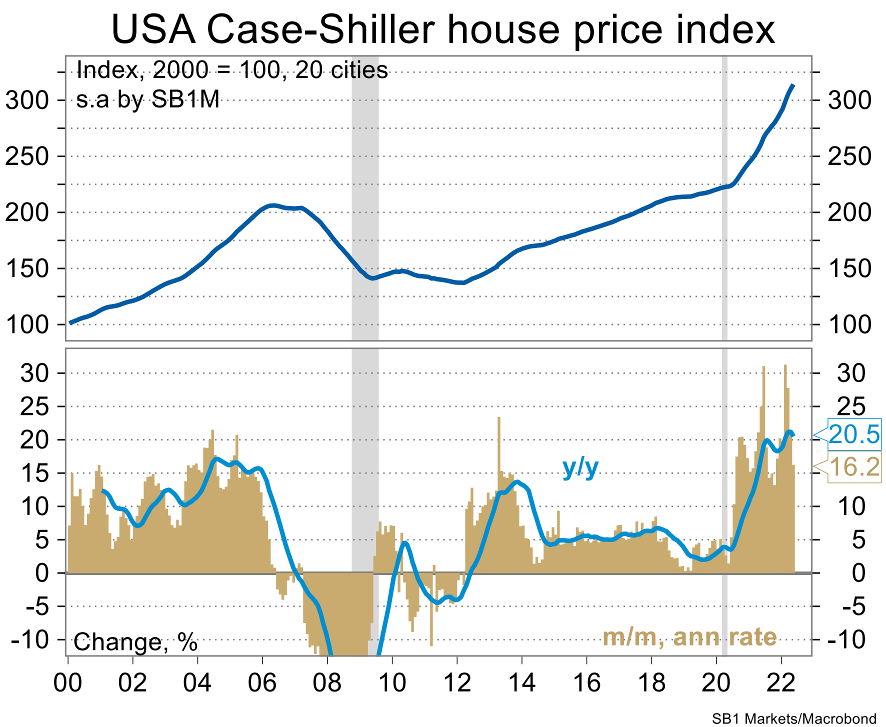


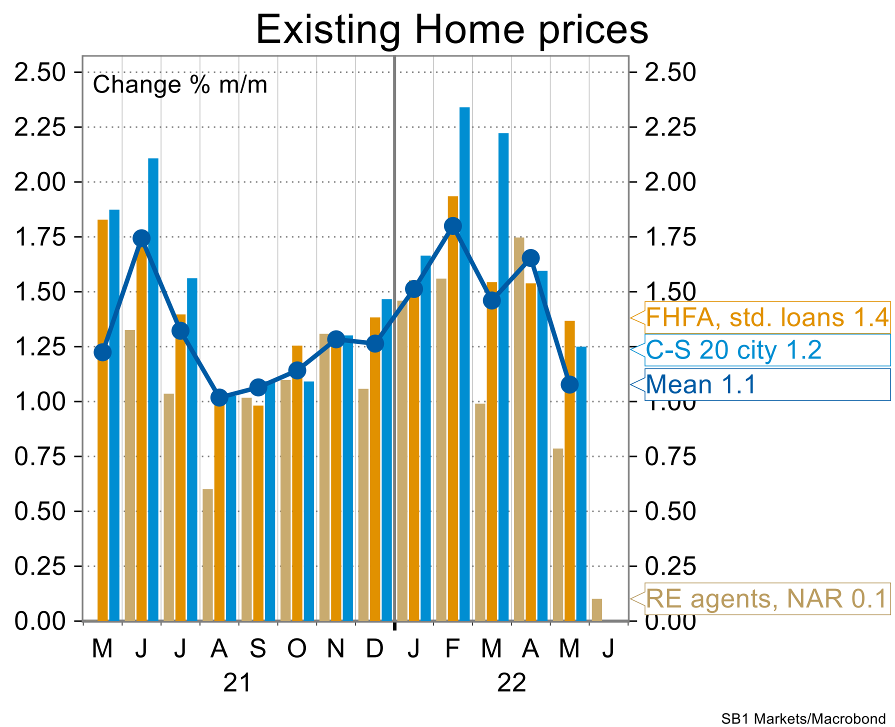


- Sales of **existing homes** fell to 5.12 mill (annualised rate), from 5.41 mill in May, expected close to unch. Sales have fallen by 21% from local peak in January. **Pending sales** signals a further decline in actual transactions in July
- **The inventory of unsold homes** rose marginally in June, as during the previous months – from at ATL in February
  - The inventory equals 2.6 months of sales (up from 2.4 last month). During the 2005 boom, the i/s ratio was 4 months, in bad times it has been as high as 10 months
  - Still, the median time on the market for those homes actually sold is just 16 days (down from 18 last, and close to ATL). Before the pandemic the time on market was at 30 days (and 120 days in 2011!)
- **Prices** rose 0.1% m/m in June, *check more next page*
- **Mortgage rates** have fallen recent weeks but remain far higher than over the previous years – and the high price level (up close to 40% since before the pandemic) has crushed affordability – and the impact is now very visible

House price inflation is slowing but Case/Shiller still reported a 1.2% lift in May

Realtors reported 0.1% price increase in June

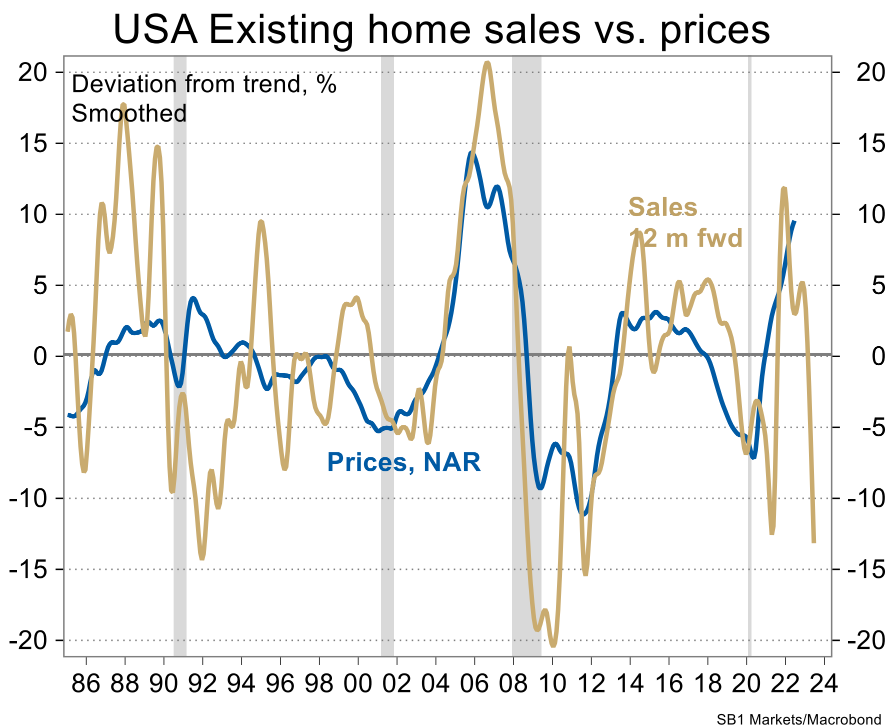


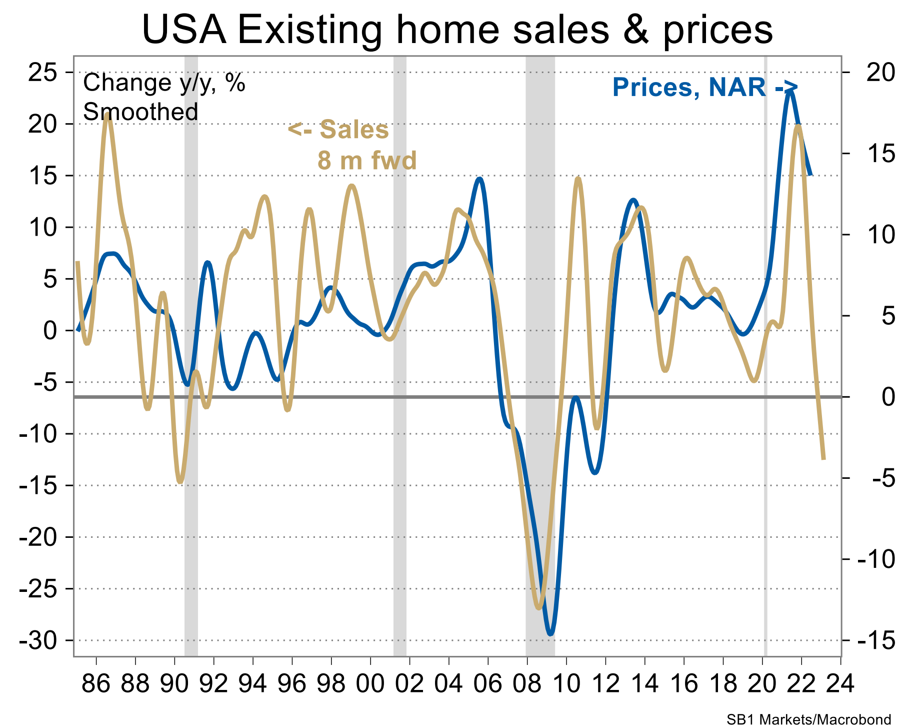


- **S&P's Case/Shiller's 20 cities** price index rose 1.2% m/m in May (April - June avg, our seas. adj) equalling a 16% annualised pace, well down from the recent peaks but still a very rapid price appreciation. A 1.5% increase was expected. The annual rate fall marginally to 20.5%. The national index is up by 19.7%
- **The FHFA** (Federal Housing Financing Agency) price index, which covers homes with loans guarantied by the government sponsored Fannie Mae or Freddie Mac ('Husbankene', has a countrywide coverage), rose 'just' 1.4% in May, and are up 18.3 y/y!
- **Realtors** reported a 0.1% lift in June, prices are up 13.5% y/y
- <u>However, even if prices cover transactions closed up to June (included in the April-June average), those deals were mostly agreed upon in May (as for the realtors index)</u> – and 'something' might have happened since May. Anyway, <u>we still expect prices to yield substantially the coming months, following the unprecedented 40% lift since before the pandemic</u>

When home sales turn south, prices follow. Normally after a while

Thus, a focus on transactions is justified – even if prices are the ‘real thing’

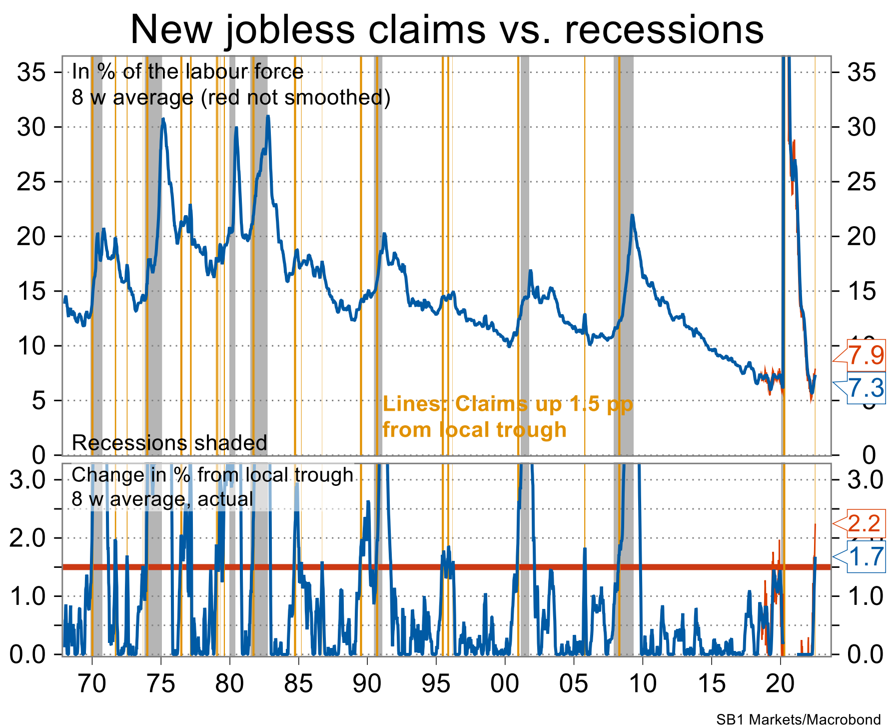


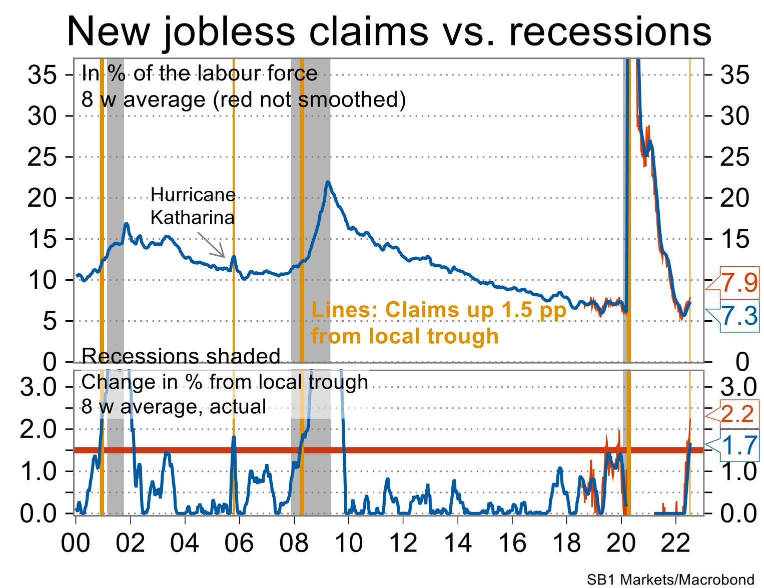


- Sales peaked in Jan-21 but probably mostly due to lack of supply – and prices have not yet yielded. The recent decline in sales, which started in Feb-22, is no doubt due to a softening demand, signalling a substantial downside risk for prices, especially given the unprecedented 2 y surge during the pandemic

A yellow warning line is drawn:

The lift in the 8-week average has crossed an important threshold

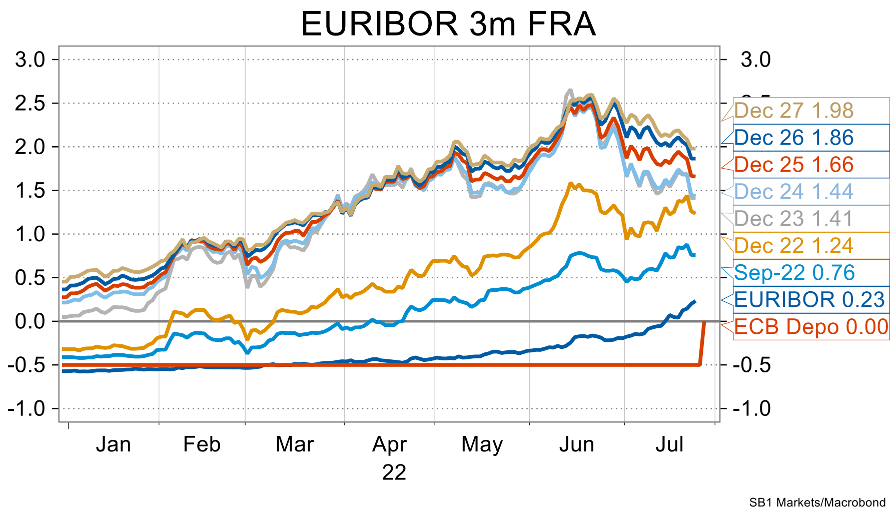


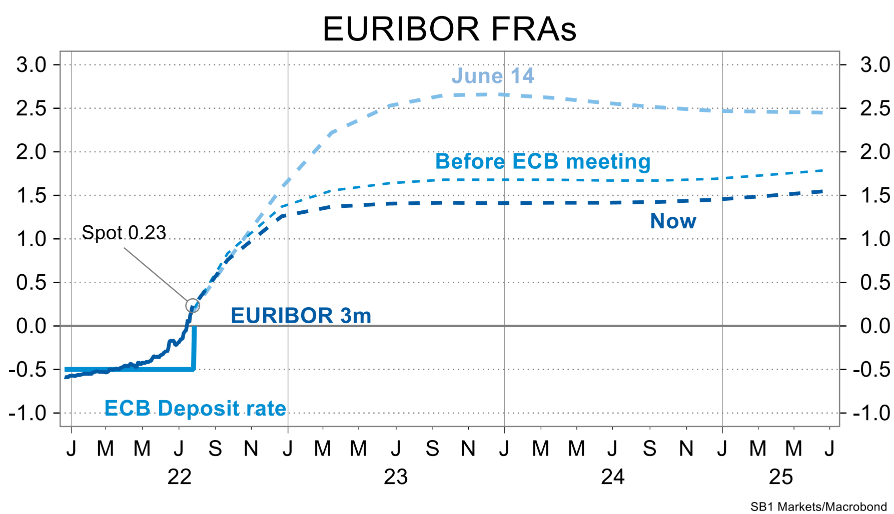


- The yellow lines: New jobless claims (8-week average) up 1.5 pp vs. the labour force
- Now, the average is up 1.7 pp, from 1.5 pp the previous week. Thus, a yellow line is now drawn at the charts above, for the first time since 2005 (Hurricane Katharina), without a recession around the corner (the lines in 2008, 2020), and before that in 1996
- Our recession signal model based on new jobless claims has sent several false signals (false positives), and even the correct signals often comes too late for a real time conclusion. Even so, the inflow of new unemployed persons is tightly correlated to the economic cycle – and the cycle is now weakening (Lifting the threshold to say 2% would strengthen the signal/noise ratio substantially. We may be there pretty soon)

ECB hiked 50 bps but the outlook is cloudy, no forward guidence given

Rate expectations ended the week sharply down. 'Italy' got a new QE program (if it behaves)

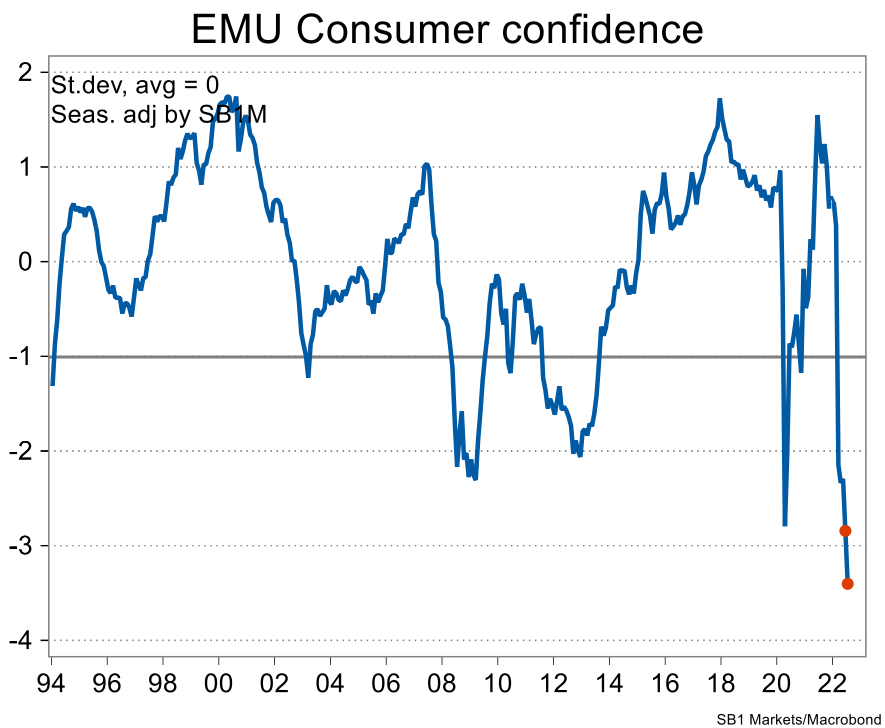


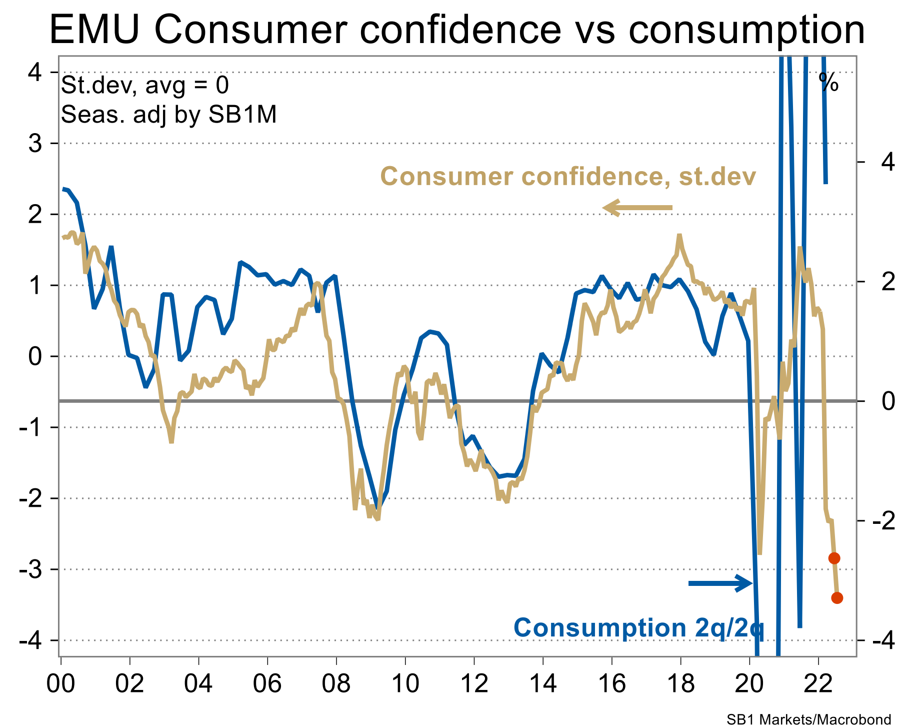


- **The 50 bps hike** was not expected by the majority of economist some days before the meeting but following hints about a 50 bps hike, a 'double hike' was not that surprising, especially not in the market, the 3 m EURIBOR rate rose by just 2 bps. The repo rate was then lifted to zero
- The bank acknowledge that the **economic outlook is clouded** but high inflation was sufficient to lift the signal rate out of the negative territory
- At the same time, the bank did **not give any forward guidance**. Given the bank's own experience, and even more lack of consistency in Federal Reserve's communication and actions, and the uncertainty about the development in the economy, it is reasonable to state the obvious: The ECB is data dependant
- As expected, a new program aimed at keeping bond market spreads in check was introduced. A **Transmission Protection Instrument (TPI)** was established (unanimously, Lagarde stressed)
  - » The formal argument was make sure that ECB's monetary policy works, by preventing that unwarranted, disorderly market dynamics which make monetary policy inefficient.
  - » Several strings were attached but no formal numbers – discretion over rule.
  - » Soon, a test may come: What if Italian spread widens after a new government decides to weaken the budget, and scrap economic reforms? Will the ECB still support the Italian bond market?
- **Short term market rates** rose just after the announcement but then fell back – and during last week especially longer date EURIBOR FRAs have fallen sharply as the growth outlook rapidly deteriorates. From mid June, the assumed peak for EURIBOR rates have fallen to less than 1.5% from 2.5%. Still, more than 100 bps hikes are discounted before the end of 2022
- *Check next page for European bond spreads*

Consumer confidence in uncharted territory, down and way below expectations

Inflation and a war is more important than the lowest unemployment rate since 1980

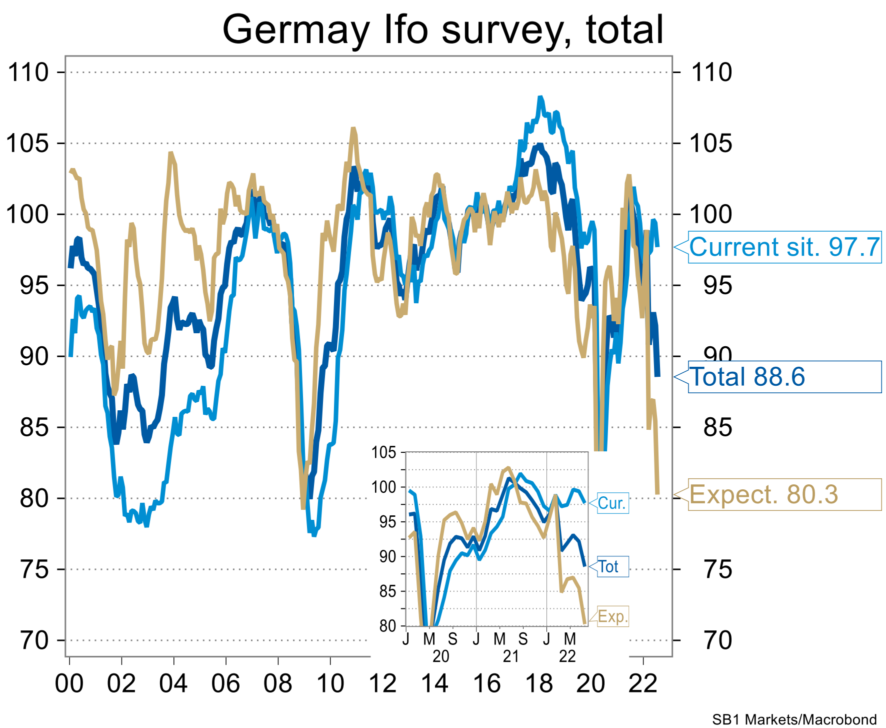


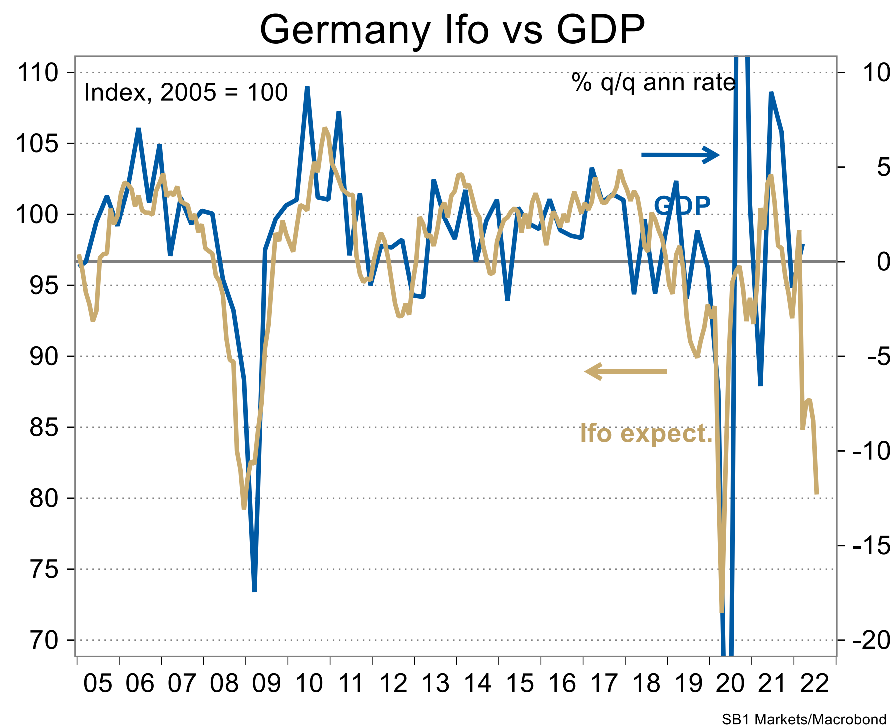


- **The confidence index** fell 3.2 p to -27 in July, expected down to 24.5, according to the preliminary estimate. The decline equals 0.6 st.dev, and the level in June is -3.4 st.dev below avg –a level not seen before, data though back just to 1994…
- **The war** has been around for 5 months, at most likely it does not constitute an even larger negative drag on the sentiment. Thus, **inflation** is probably to blame. **Interest rates** are now being hiked – and the rest of the yield curve has taken big leaps upwards, at least until mid June. Now rate expectations have fallen substantially – and sentiment is plummeting
- Usually, consumer confidence is tightly correlated to growth in household demand. If that's the case now as well…

Ifo expectations further down in July, to a very low level:A deep setback signalled

The index fell by 1 st.dev to -3.2 sd below avg! The current situation just marg. down, at +0.4 st.dev



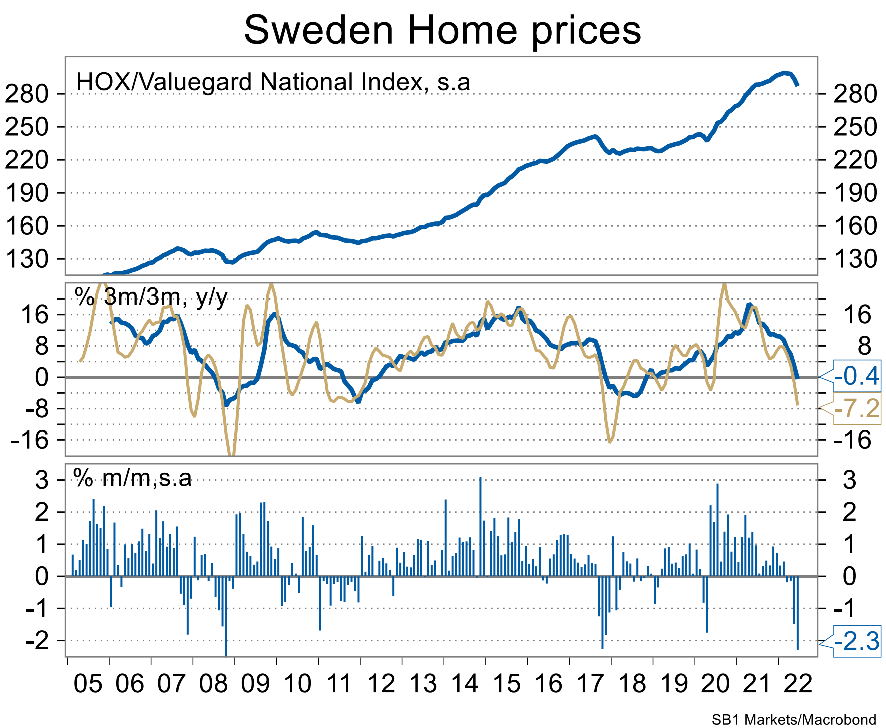


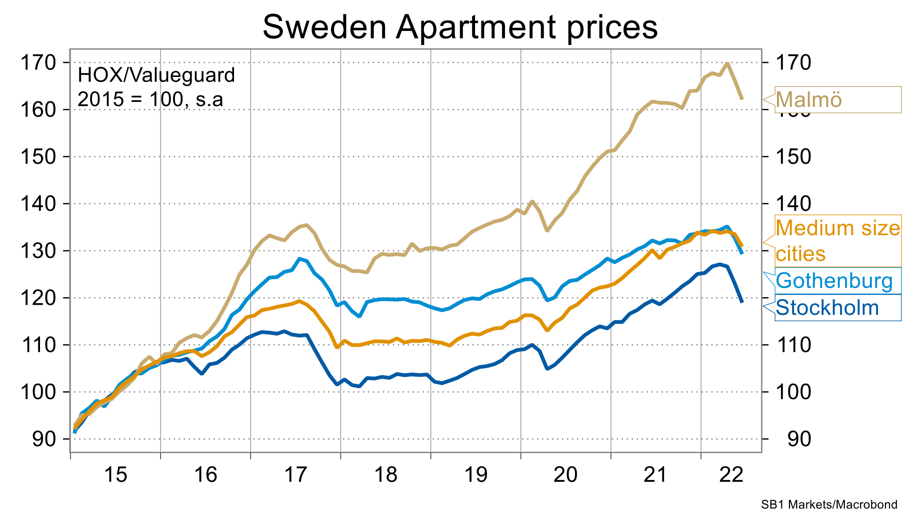
- **The expectation index** fell 5.2 p to 80.2, close to 3 p lower than expected. The level is very low, at -3.2 st.dev below average, almost down to the lowest level during the financial crisis. The correlation to GDP is not perfect but a huge decline in GDP is signalled, at a 10+ pace!
- The **assessment of the current situation** fell 1.7 p to 97.7, in line with expectations. The level is still above average, at 0.6 st.dev
- The total Ifo business climate index fell by 3.6 p to 88.6, well below expectations

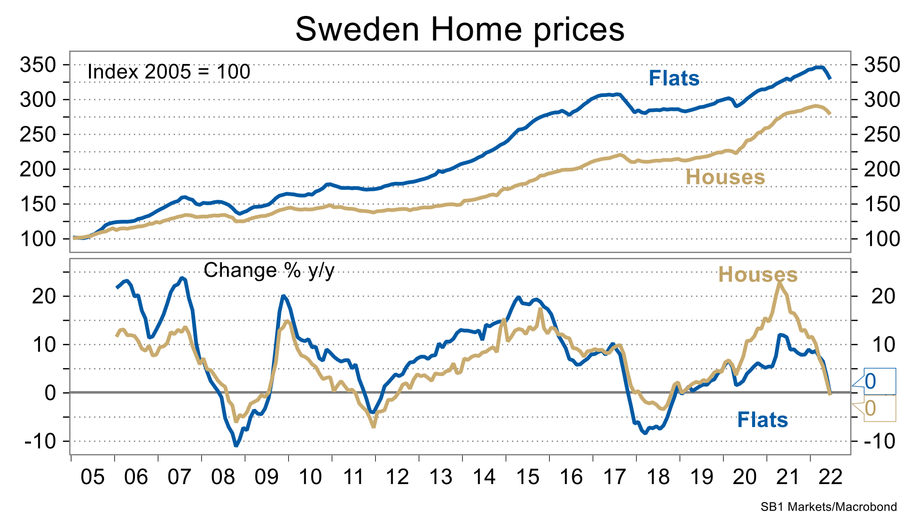
Business climate: the average of the current situation and expectations

Look to Sweden: House prices are falling rather rapidly

Prices fell 2.3% in June, the 4th decline in row, prices are down y/y. Stockholm in the lead



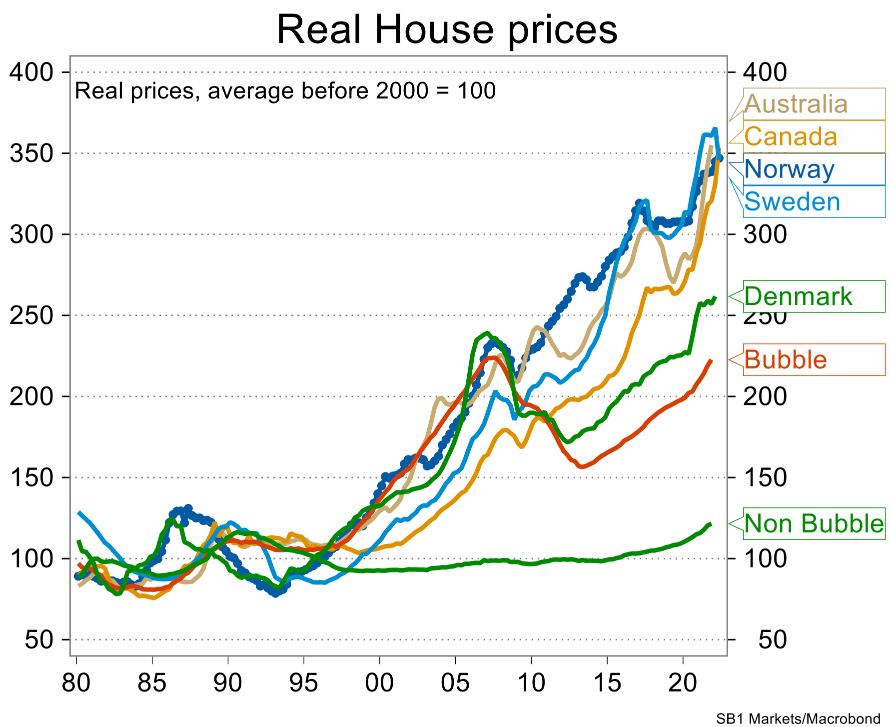


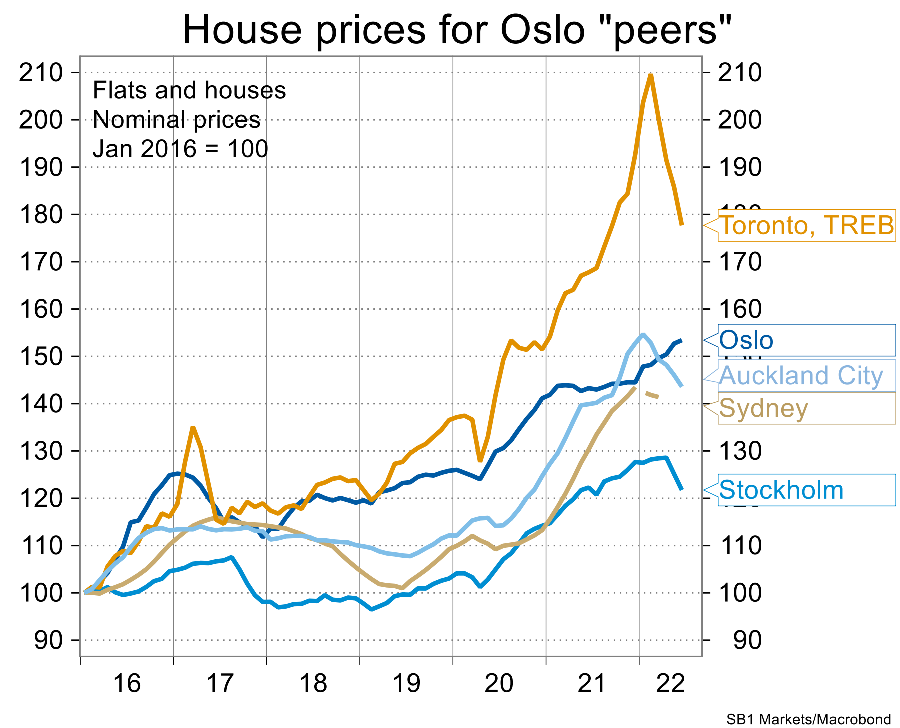


- **Prices are down** 4% from the peak in February. In Stockholm, apartment prices are down 6.4% from the peak
  - In June prices in Stockholm fell by 3.3% (4.5% not seas. Adj
  - Prices are down in all the major cities as well
- **The annual rate** declined to 2.9% from 6.2% in April
  - The underlying price growth (3m/3m) suddenly turned negative
- The **Riksbank's** abrupt change of tack in late April has no doubt hit the housing market hard, as the bulk of the decrease in prices so far took place in May and June

Just Oslo on the way up; Toronto, Sydney, Auckland & Stockholm have peaked

Very likely, Oslo will soon follow suit

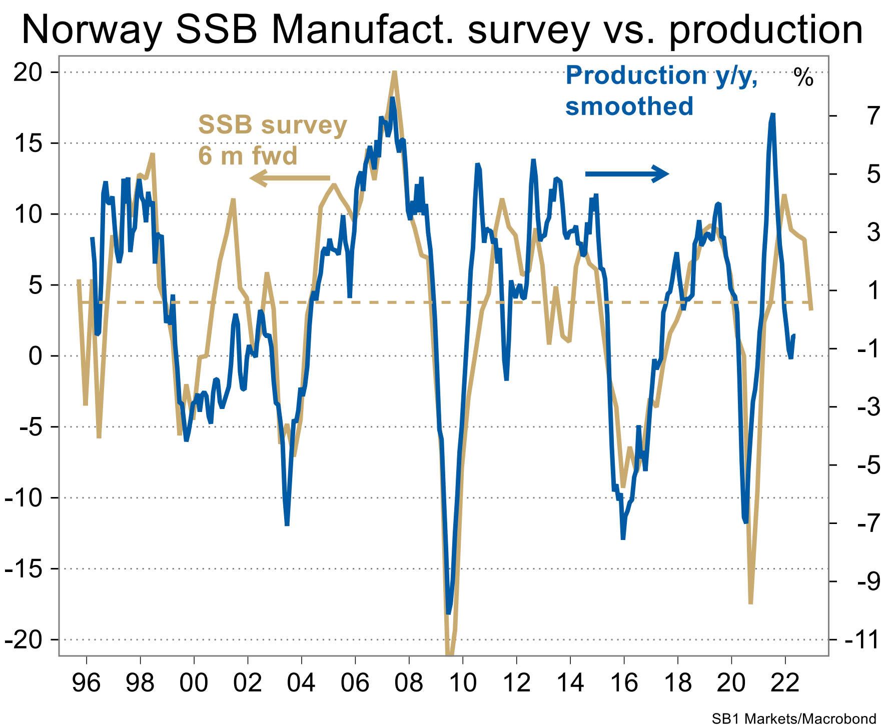


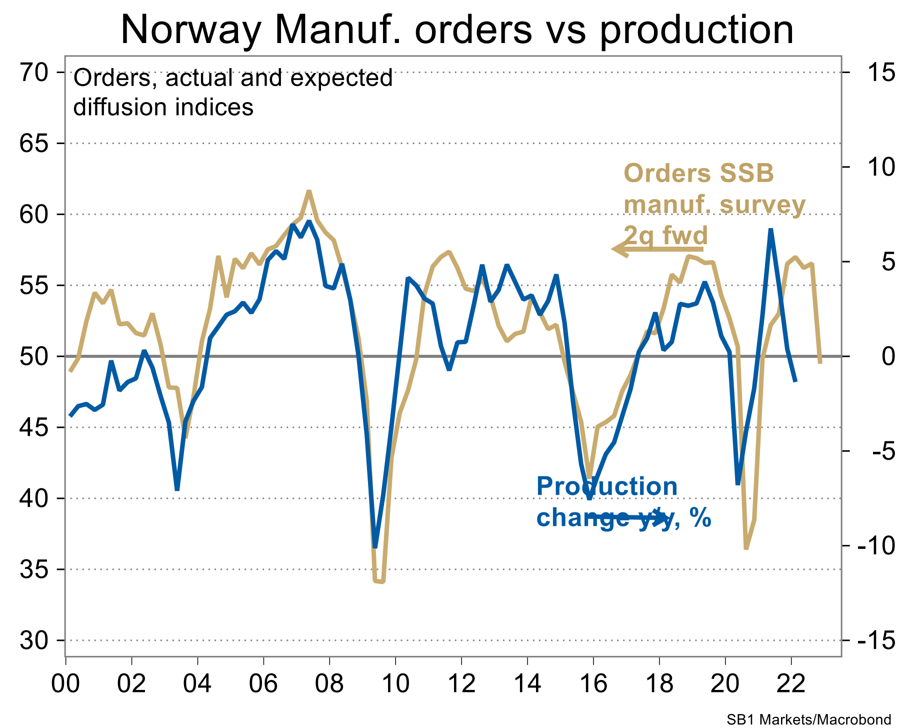


- Real house prices are at high levels in both Australia, Canada, Norway, and Sweden
- Now, the capital cities may signal a change is underway. Except for Oslo, of course, where prices never can decline.

SSB's manufacturing survey down to below average in Q2

The oil sector report continued growth, others do not – <u>the tide has turned</u>

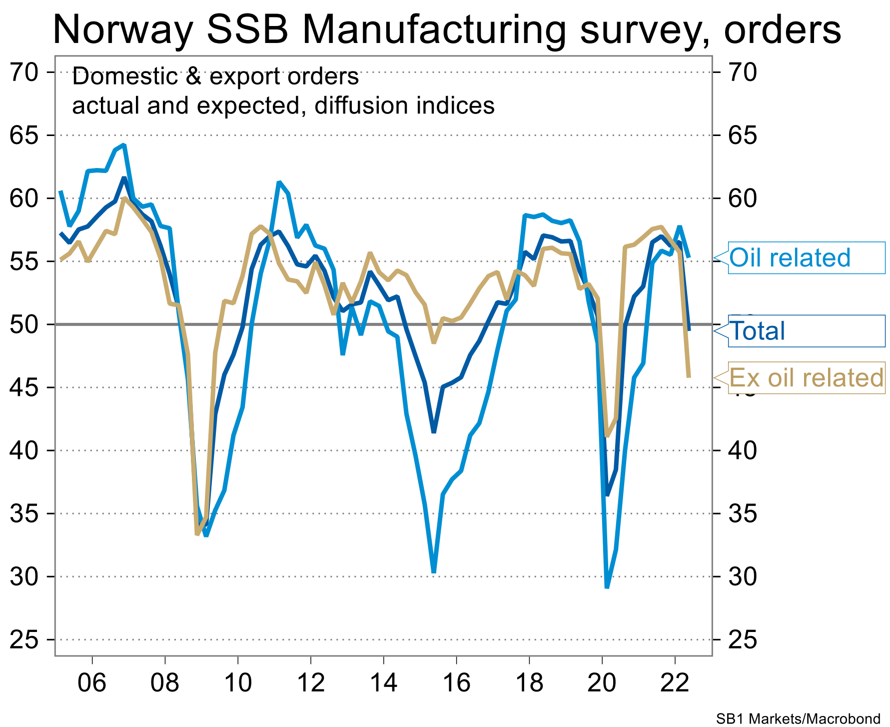


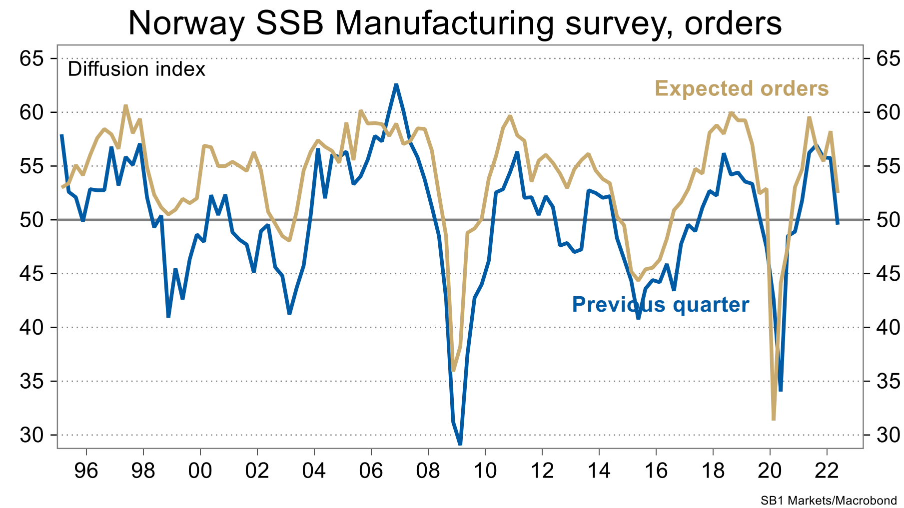


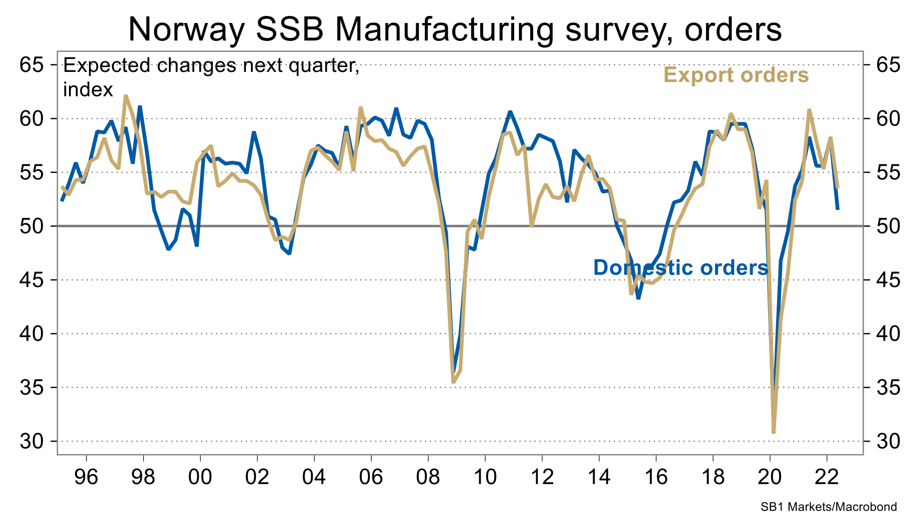
- The **composite index ('confidence')** in SSB's manufacturing survey fell to 3.2 p in Q2, which is marginally below and average level. We expected a decline to 4 (no consensus). Oil related sectors report a still strong outlook (like order expectations), other sectors fell to well below average
  - » The index signals trend growth, somewhat less than 3% GDP growth and – together with the oil price, a impressive 62% growth in 12 m forward expected corporate (OSEBX) earnings, though below analyst's current 89% growth estimate
- **Supply constraints** eased marginally (not for labour), but are still the most serious since 2008. **Demand/competition** is far less of a problem than normal
- Fewer companies reported they plan to lift prices – but the share is still was off anything seen before (barring the recent quarters)

Oil related manufacturers kept the pace up, other sectors not

Both domestic & export orders are slowing sharply, in sum

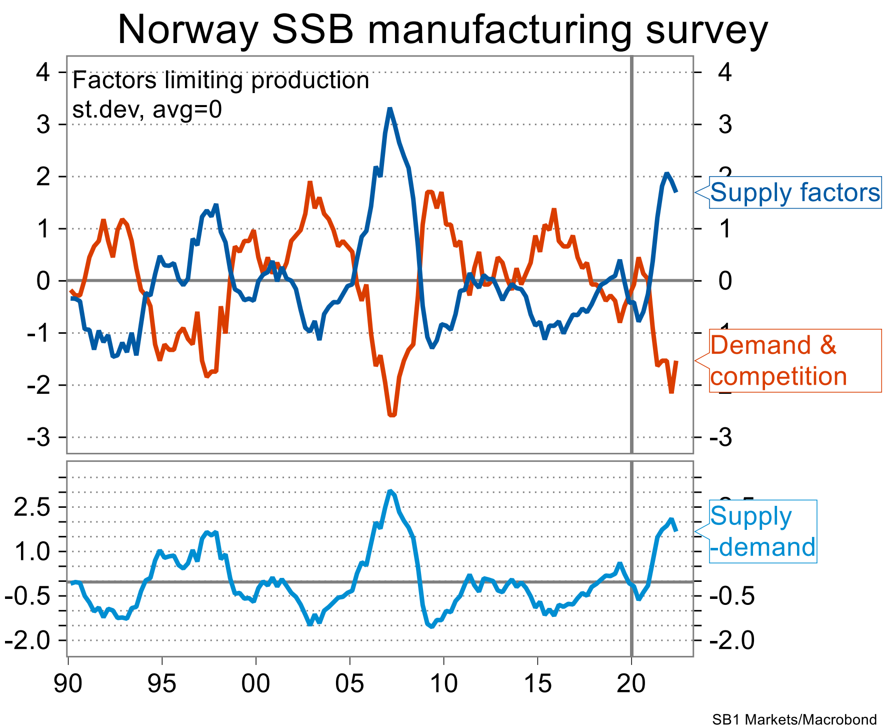


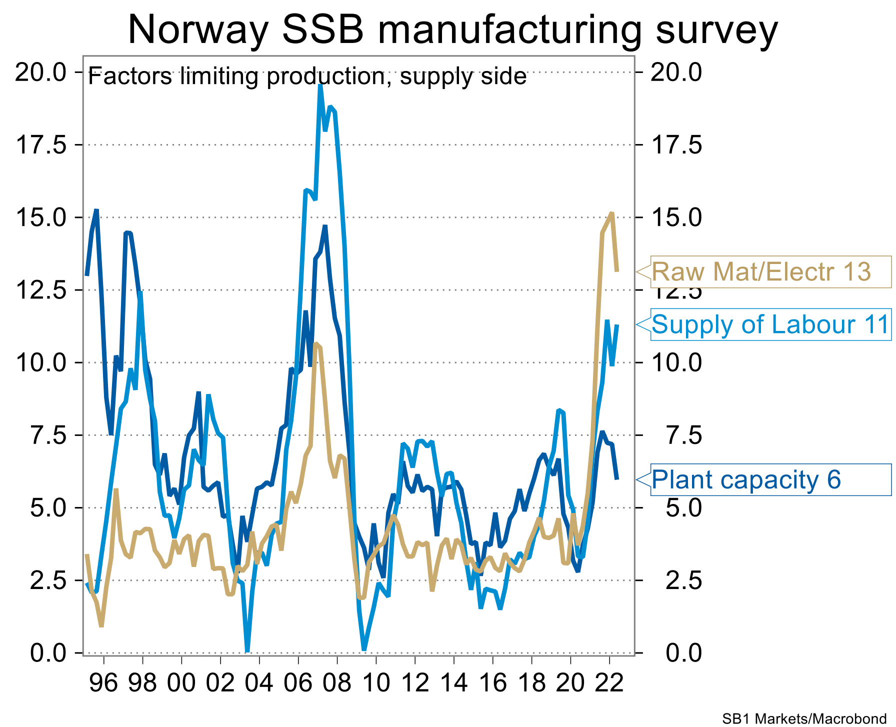




Limiting production: Supply factors far above average, demand far below

However, in Q2 the gap between the two narrowed somewhat

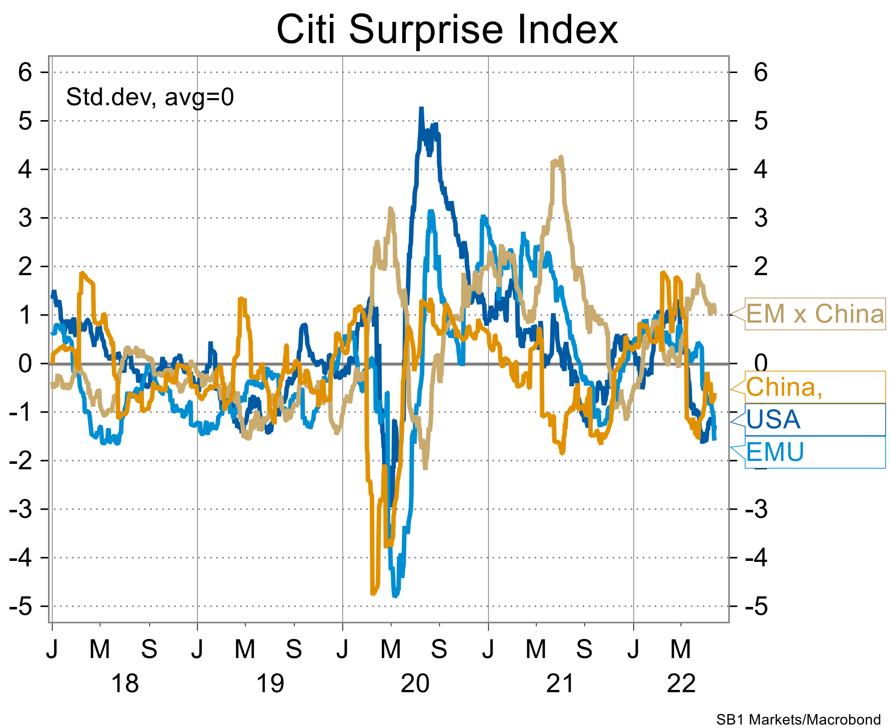


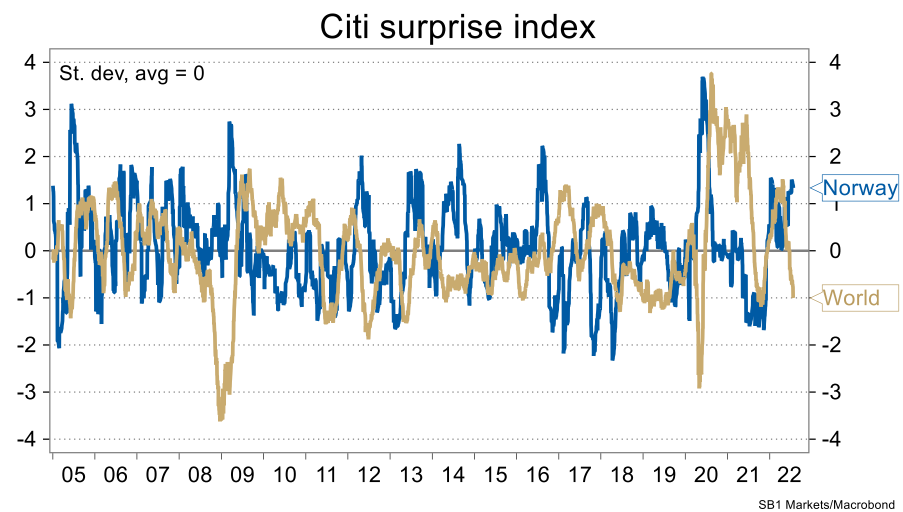


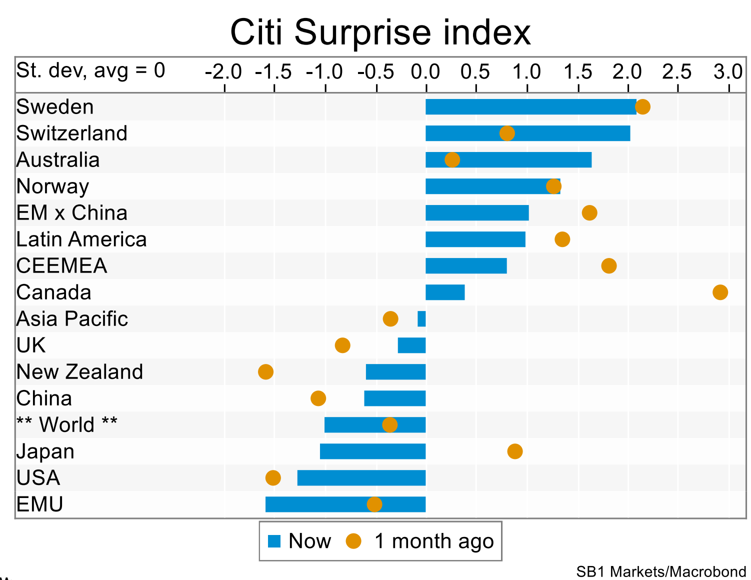
- Fewer companies reported supply side factors as limiting production, except for labour
  - » Raw materials/electricity is still the most important constraints, but problems eased a little in Q2. Plant capacity also were reported less of a problem
- More companies reported lack of demand or competition as limiting factors, but the share is still unusually low
- ***No demand crisis – and it never was during the pandemic***

EMU surprises the most on the downside – but US and China also below par

… as is the world







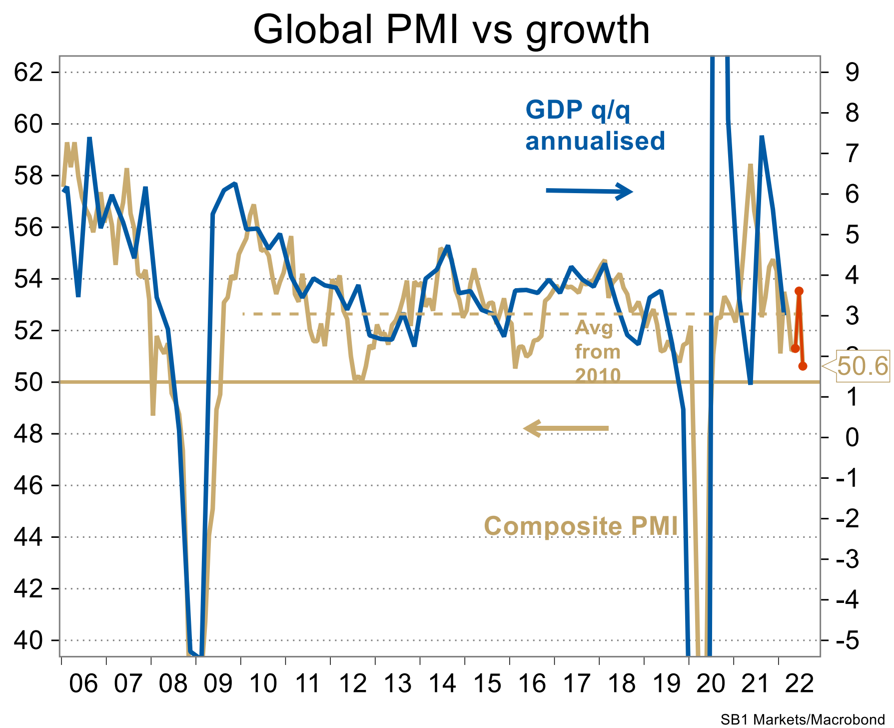
- **Emerging markets** x China are still delivering better results than excepted
- **Norway** is surprising significantly on the upside, according to Citi
- **Sweden** are still at the top

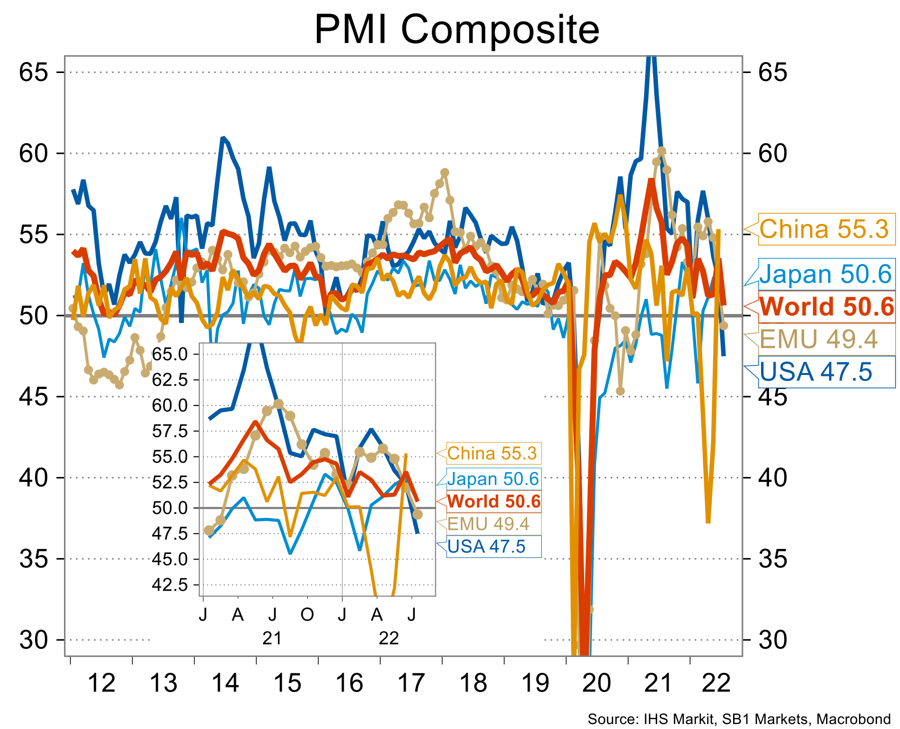
Surprise-indices measure the difference between economists' expectations and the actual outcome over a 3-month rolling window

SpareBank 1 MARKETS

The composite PMI very likely sharply down, the US and the EMU PMIs < 50

Our uncertain preliminary global estimate is for a decline at almost 3 p to 50.6, the lowest since 2016



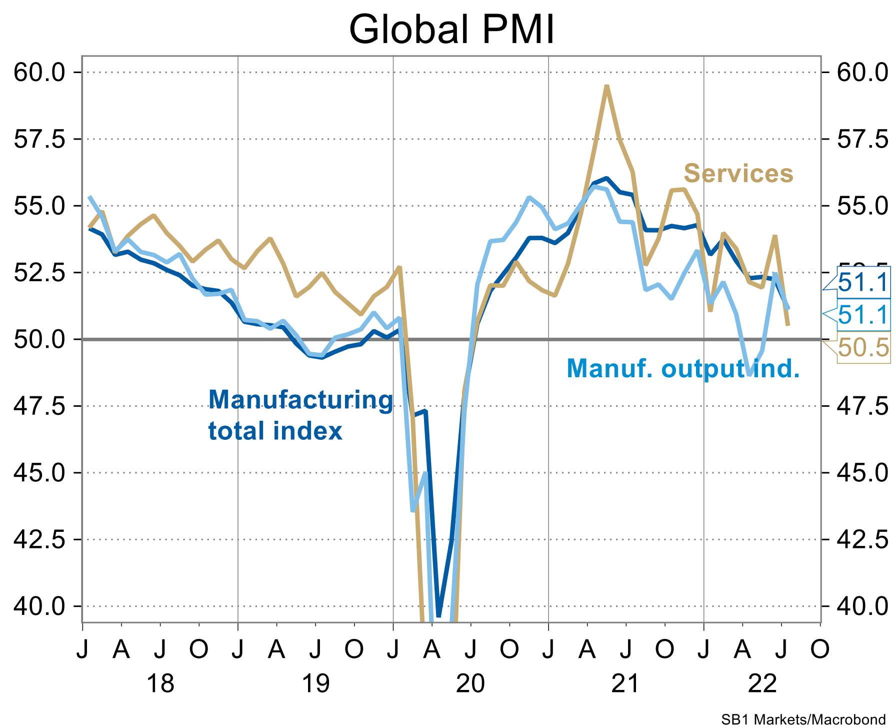


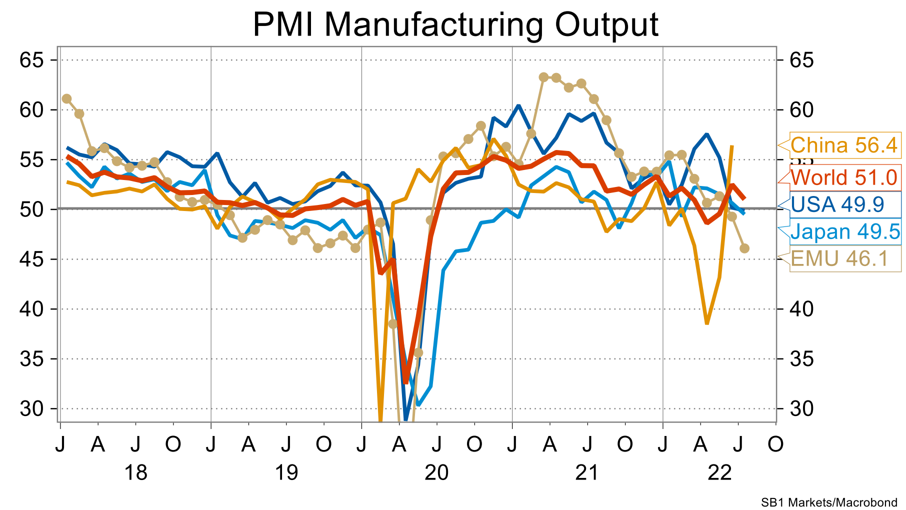
- The composite PMIs fell sharpy in both the US and in the EMU, and declined in Japan and the UK as well. The level signals a global GDP growth rate at less than 2%, which is often referred to as a global recession
- The US index is now at the bottom of the league, at 47.5, down 4.8 p, expected down 0.2 p to 52.1!
- The Eurozone PMI also fell sharply, by 2.6 p to 49.4, expected down 1 p to 51.0

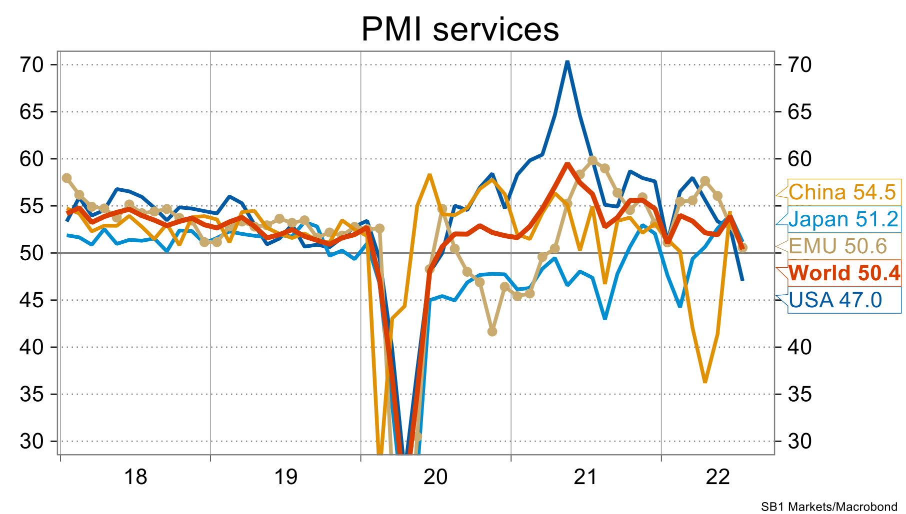
Our estimates are based on the preliminary PMIs from US, EMU, Japan UK, Australia. The estimates are uncertain, but usually by less than 0.5 p if the Chinse PMI does not change too much

EMU manufacturers and even more US services hit the wall in July

Both global manufacturing & services PMIs are trending down, and services fell the most in July



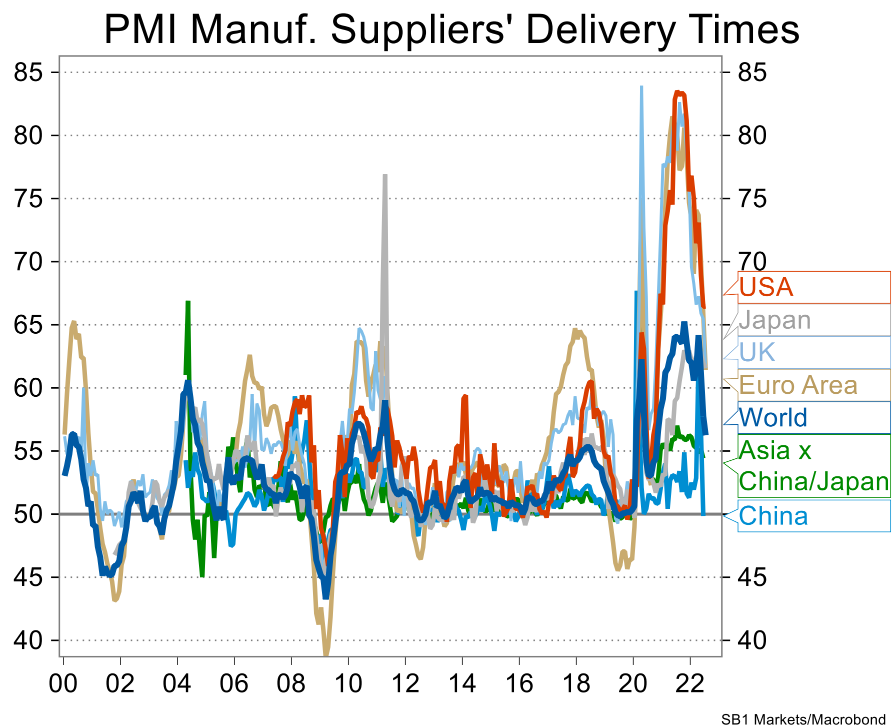


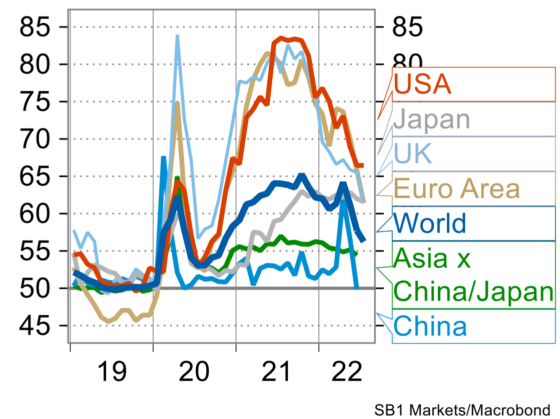


- We assume that the global service sector PMI stayed above the 50-line in July, following a 3 ½ drop. The manufacturing output index fell some 1.5 p to 51. Both fell more than expected
- The EMU manufacturing output index fell to 46.1, and the US service sector index to 47.9, both the weakest since the start of the pandemic

Delivery times index probably further down in June

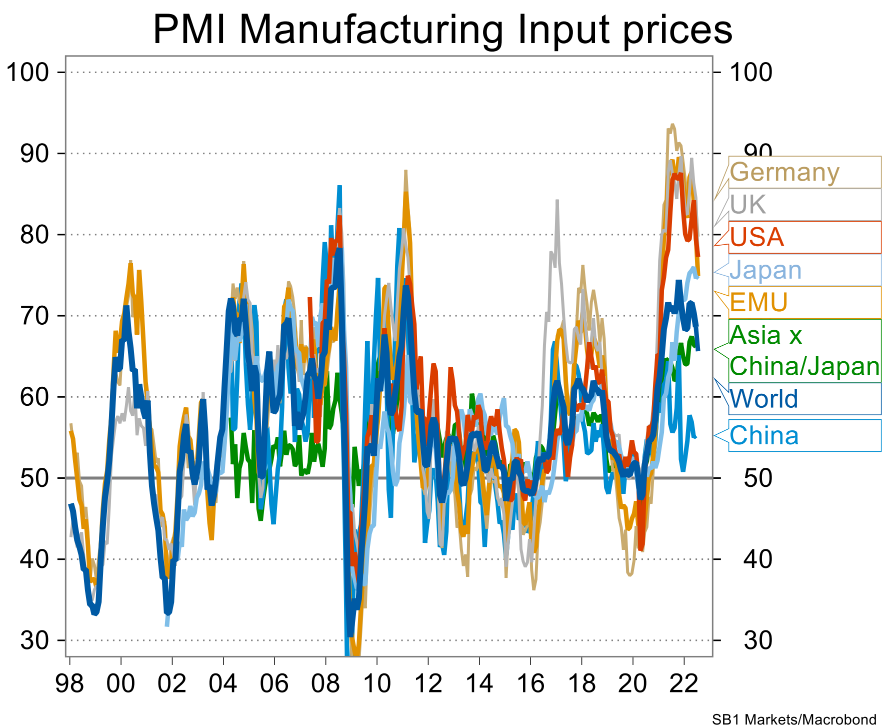
However, delivery times index was unch. in the US

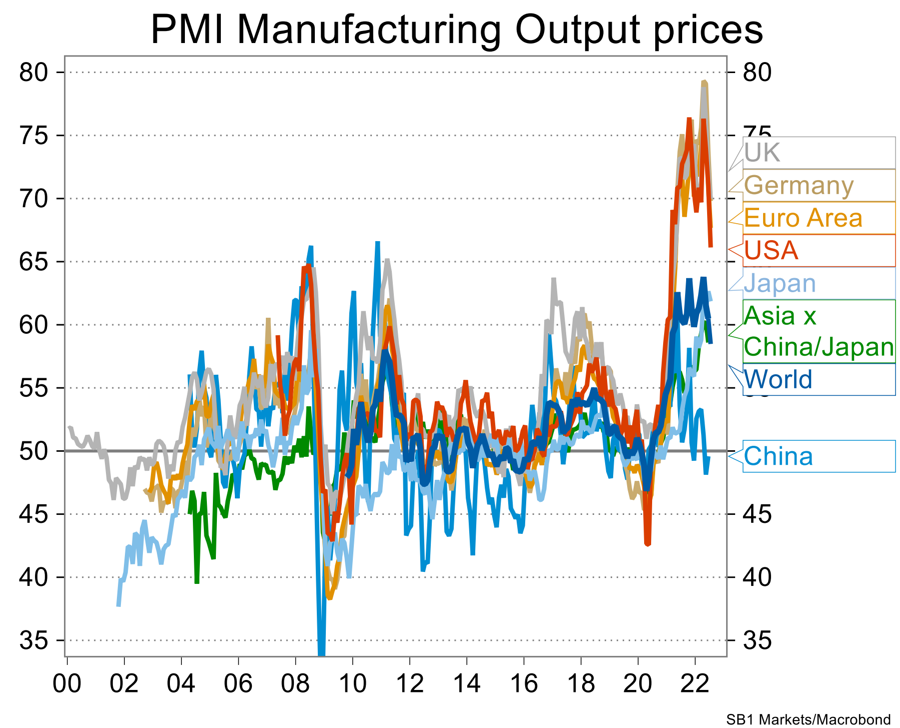




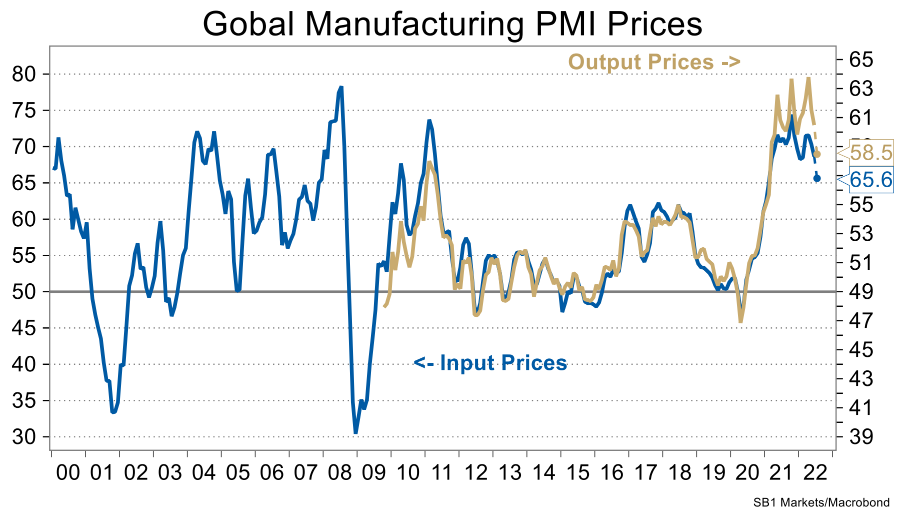
- **The global delivery times** PMI sub-index (changes in delivery times vs the previous month) has been inching down since the peak last October. The decline is broad among the Western rich countries
- **The interpretation of this index is uncertain** – are companies really reporting changes in delivery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

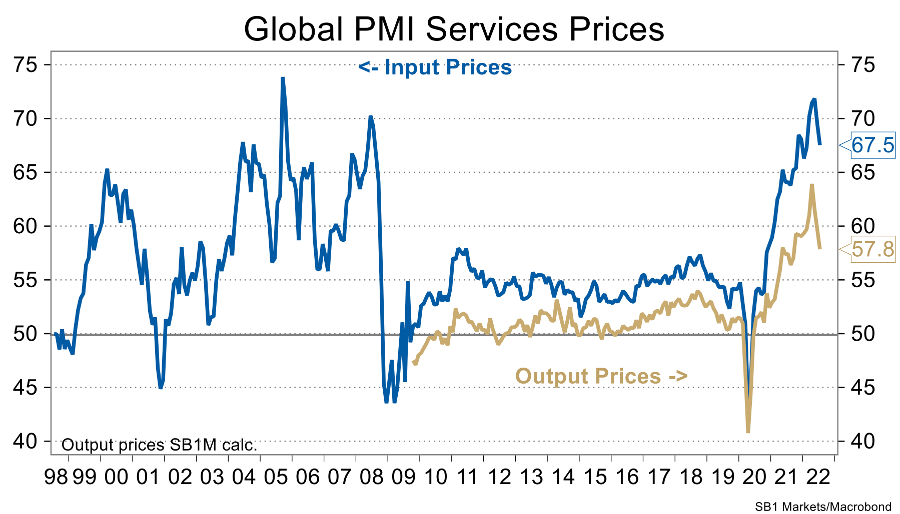
Manufacturing price inflation is heading downwards but remains elevated

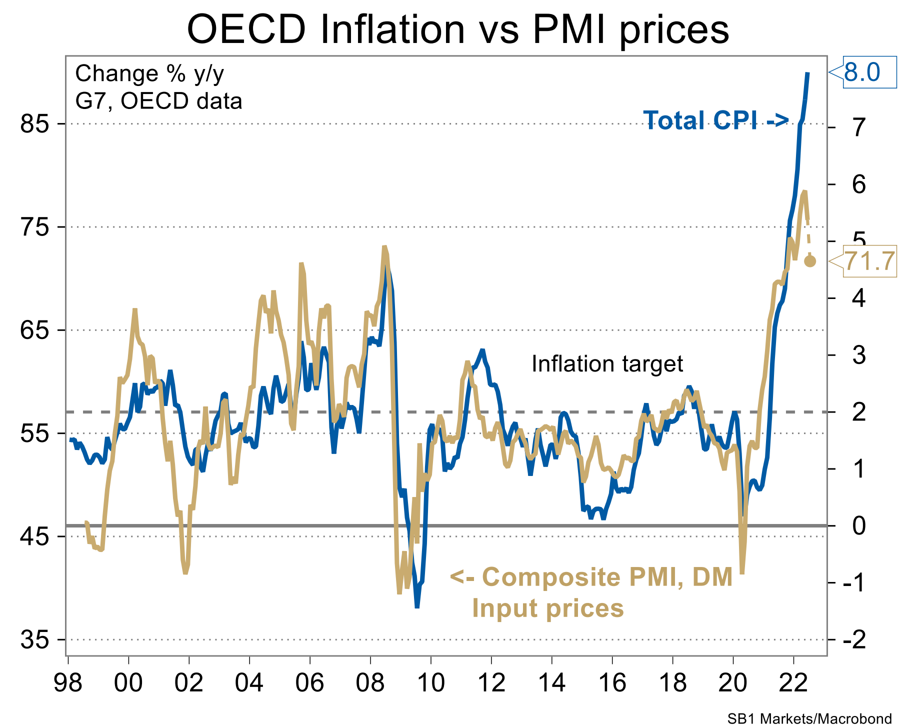




Price indices have peaked but are still reporting rapid price increases





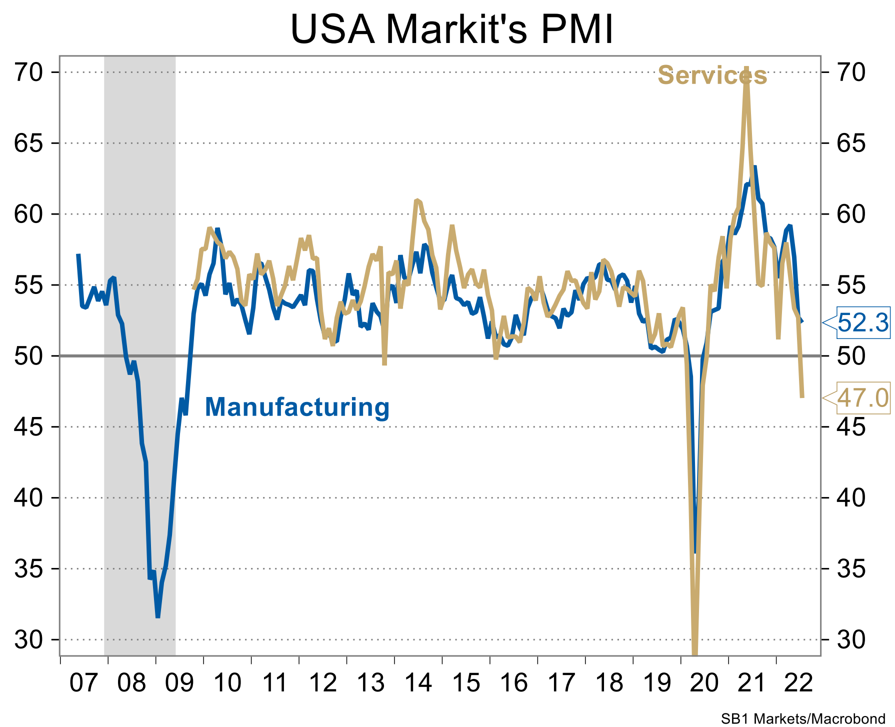


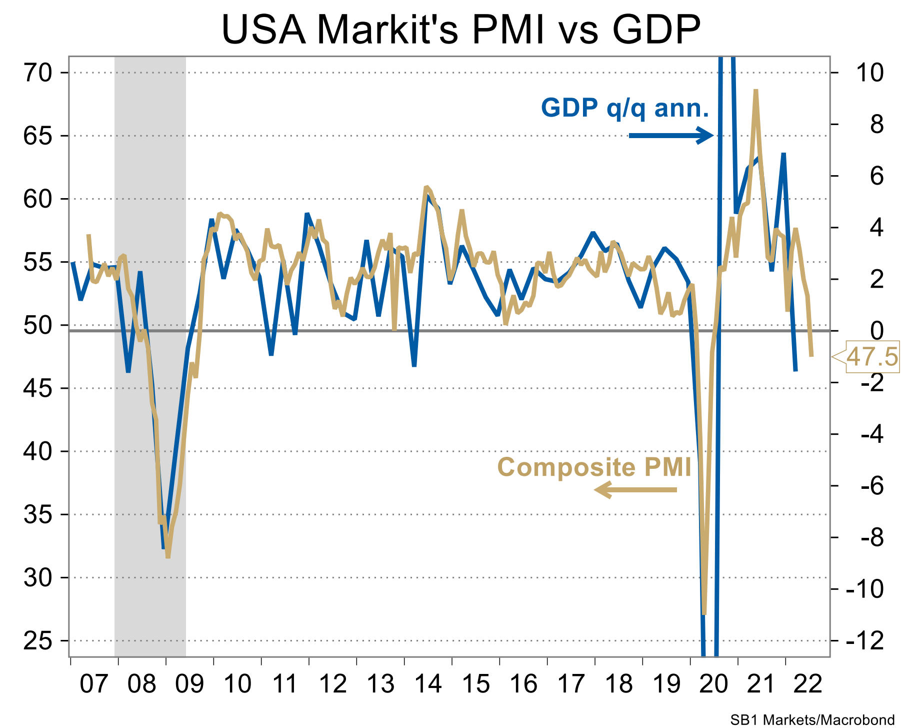
- These PMIs signal a substantial price pressure the coming months
- We are still much more concerned about wage inflation than the actual price inflation due to factors that are most likely transitory, like hikes in raw material prices, freight cost or short lived margins expansion when demand is surprisingly strong

Last obs. based on preliminary PMIs from EMU, Japan, UK, and the US

Services & composite down in negative territory in July, manuf. slows further

The composite nosedived by an highly unusual 4.8 p to 47.5, signalling a GDP contraction, aka ….

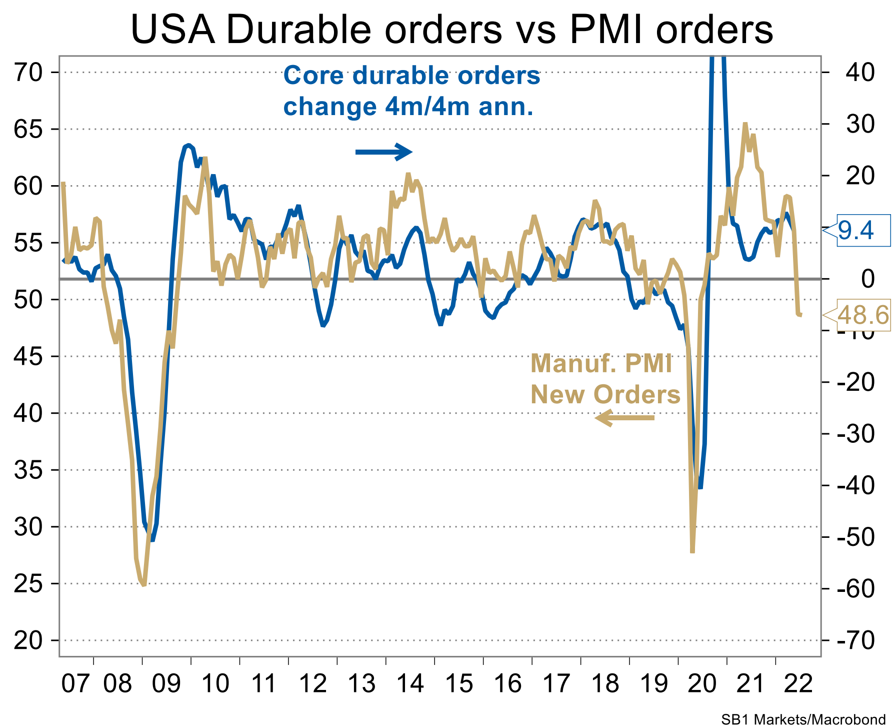


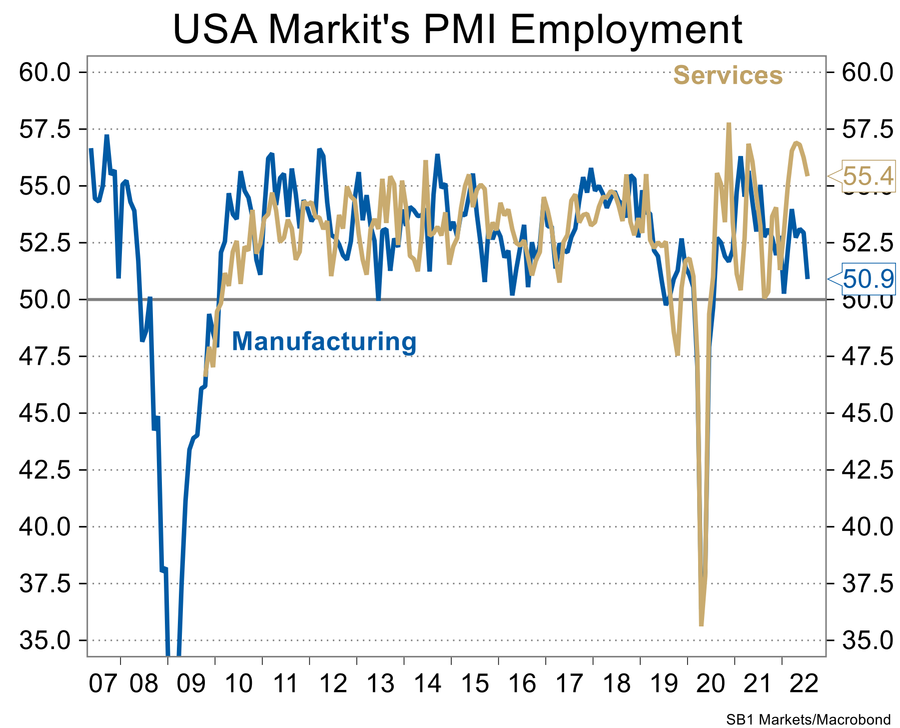


- **The composite PMI** has fallen sharply past two months, and fell below 50 for the first time since the outbreak of the pandemic
  - » The decline was due to a 5.7 p setback in services to 47.0 (expected down 0.2 p to 52.5!), and…
  - » … a decline in the output component of the manufacturing PMI by 0.3 p to 49.9. The total index fell by 0.4 p to 52.3
- **The price indices** fell sharply but are still reporting rapid price increases
- **The delivery times index** flattened, somewhat surprisingly
- **Household demand** was reported weaker due to high inflation and lack of buying power

Manufacturing orders fell in July too, the PMI says

The new order index fell marginally to 48.6, signalling a contraction in actual orders



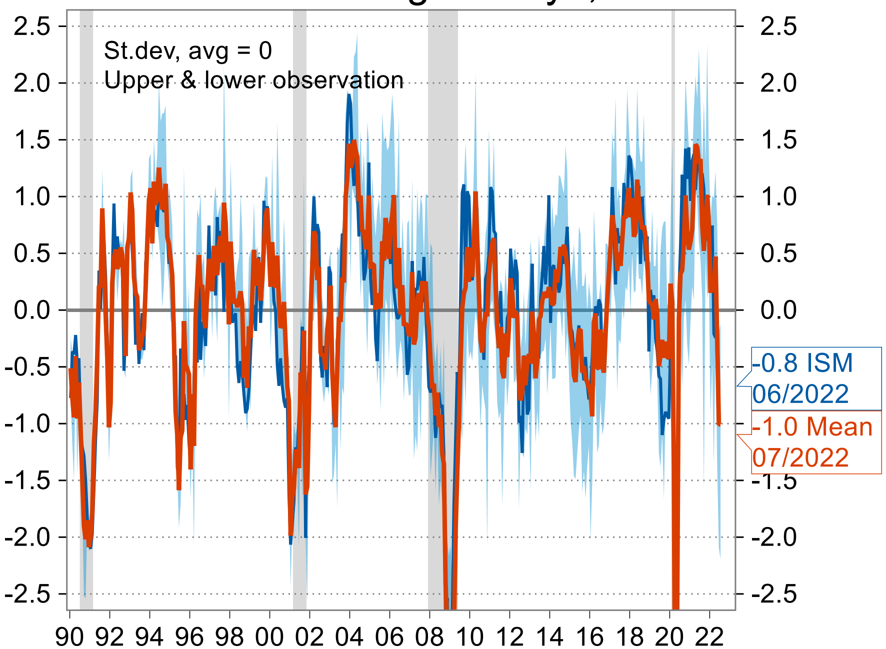


- All other manufacturing surveys are on the weak side vs. orders, see next page
- Employment, which is lagging, is still on the way up at a faster pace than normal

New orders are slowing rapidly

Something hit US manufacturers in June, and so far July indices remained at the same low level

USA Manufacturing surveys, new orders



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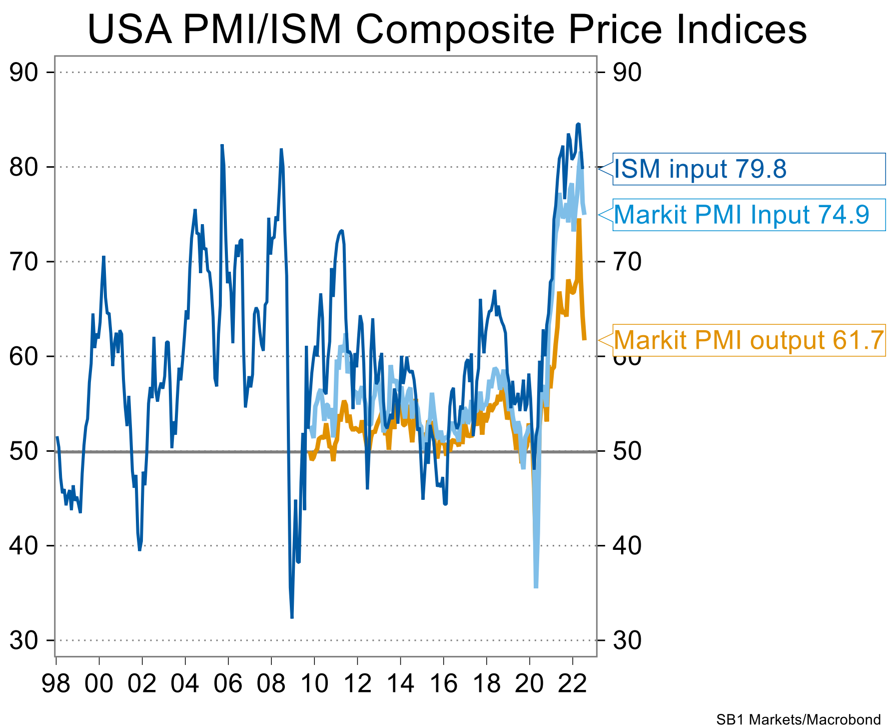
- Recessions have started with better new order data than these
- .. But ordre inflow indices have been even weaker, without a recession too
- On the other hand: Leading indicators sent a rather clear signal in June, check some few pages forward

Peak price inflation? Companies are reporting slower price increases in July

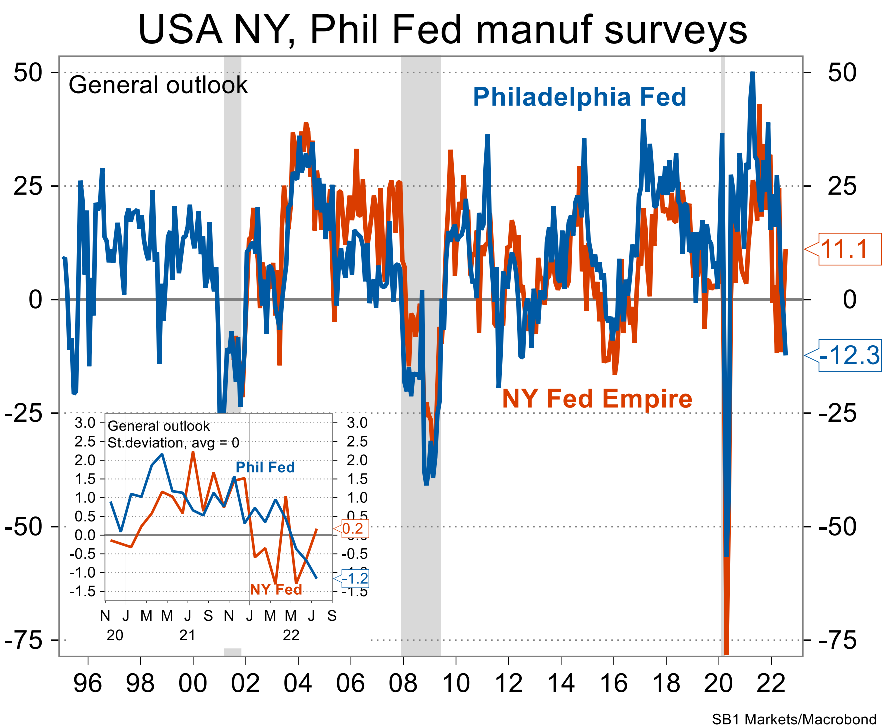
But far from slow

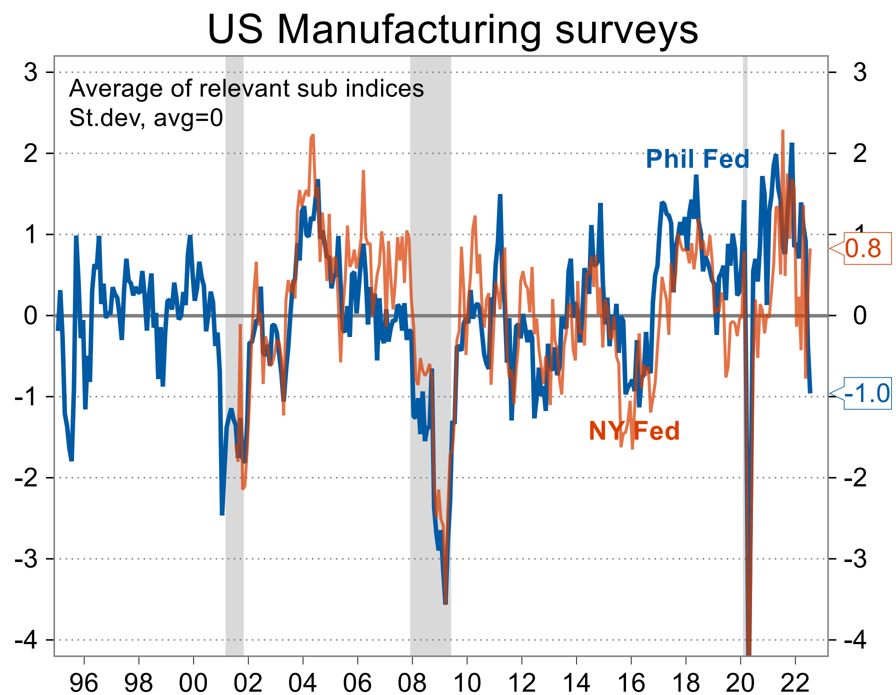


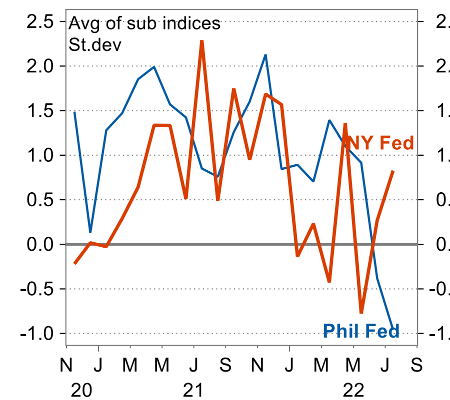
- ISM has not yet reported July data

The Philadelphia Fed survey fell further in July, while NY Fed's gauge rose again

The headline index in Phil Feds index does not suggest a recession, but orders are very weak



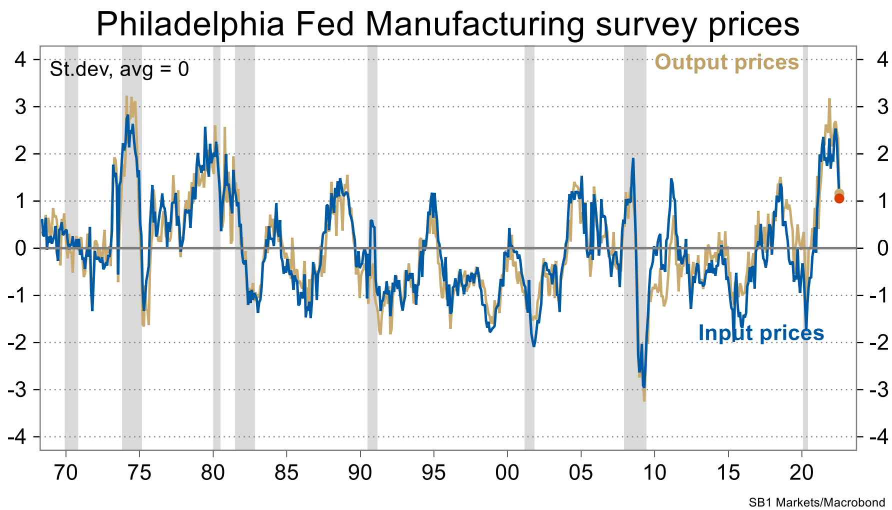


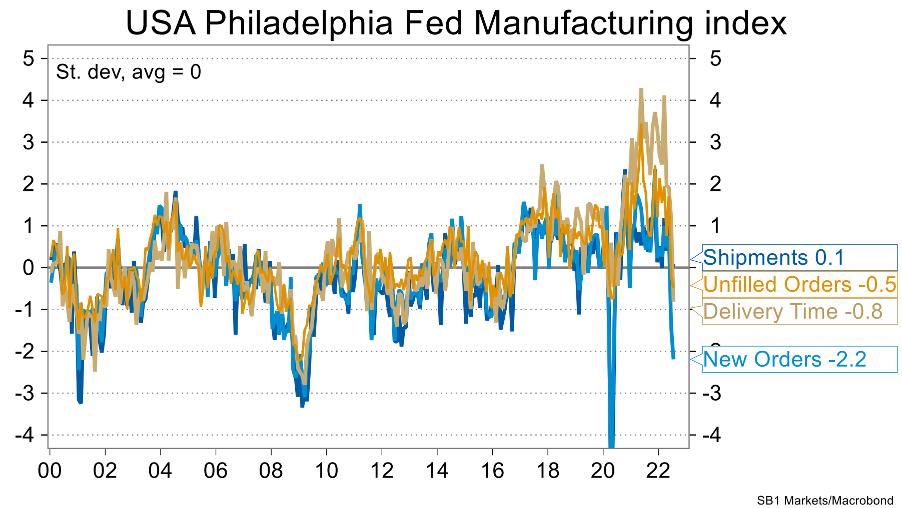


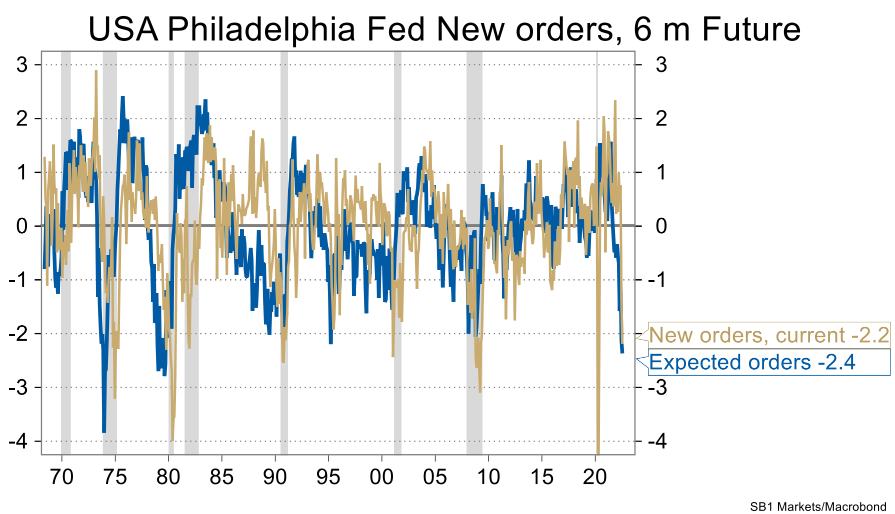
- **Philadelphia Fed's manufacturing index** fell to -12.3 from -3.3, expected UP to 0.5 (equalling 1.2 st.dev <u>below</u> avg)
  - » The outlook index (6 m future) fell further to, and the new orders index collapsed, to far into levels just seen in recessions (during 9 of the 9 recent recessions, since 1960)
- **NY Fed Empire State manufacturing index** rose continued upwards, to 11.1 in July from -1.2 in June, expected down to -2 (equalling 0.2 st.dev <u>above</u> avg. This index has been rather volatile lately, but is also trending down
- **In sum** not a recession signal but a gradual weakening of the cycle is confirmed, and the order inflow is very weak

Phil Fed: Assessment of actual orders and expectations fell further

Both are at levels seen only just before or in recessions. Price inflation is slowing rapidly



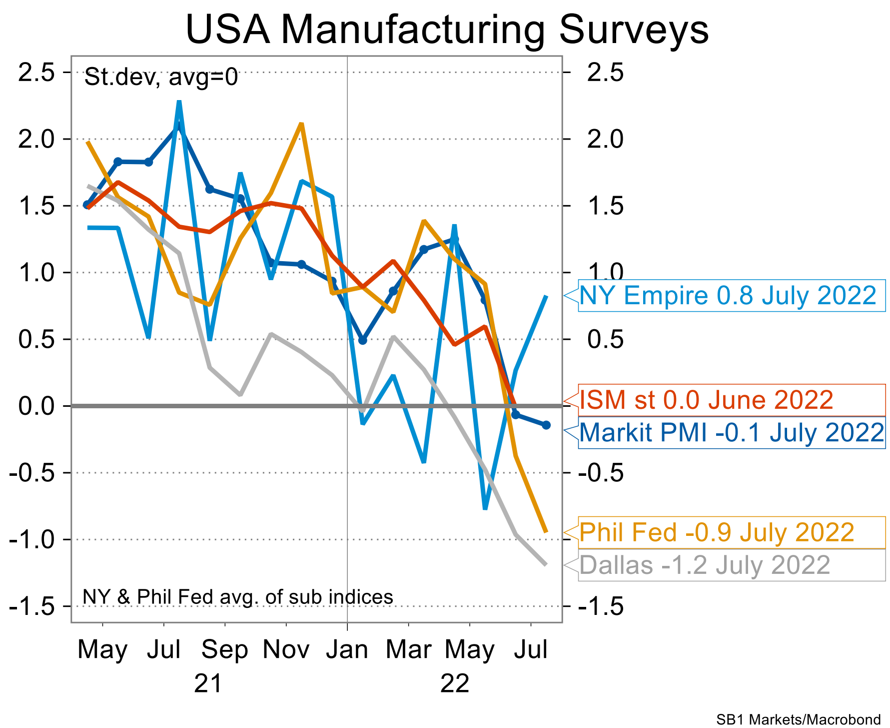


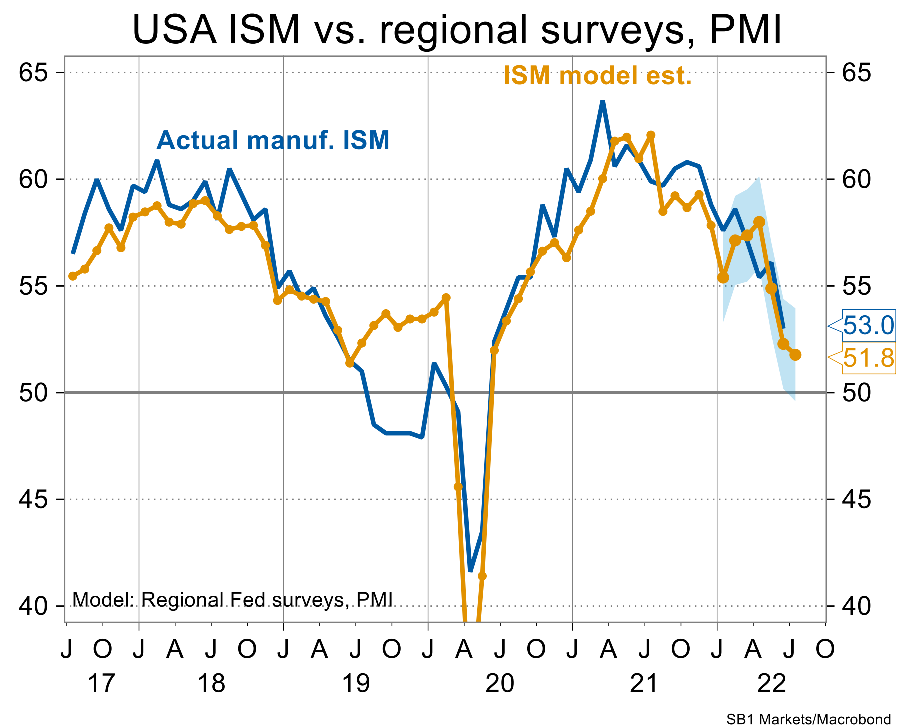


- The **current price** increases are still very high, for both input and output prices – and the delivery times index is still higher than normal – but it is falling rapidly, we assume mostly due to weakening demand
- **The new orders** index has fallen almost 3 st.dev past two months, down to -2.2 below average in July, which so far has only (and always) taken place during recessions
- **The outlook:** The new orders expectation index also fell further in July, down to -2.4 st.dev, the lowest level since 1979

NY Fed's survey against the flow, further up in July, Phil, Dallas Fed down

Markit's PMI fell marginally. In sum – and so far – the manuf. ISM signalled somewhat further down



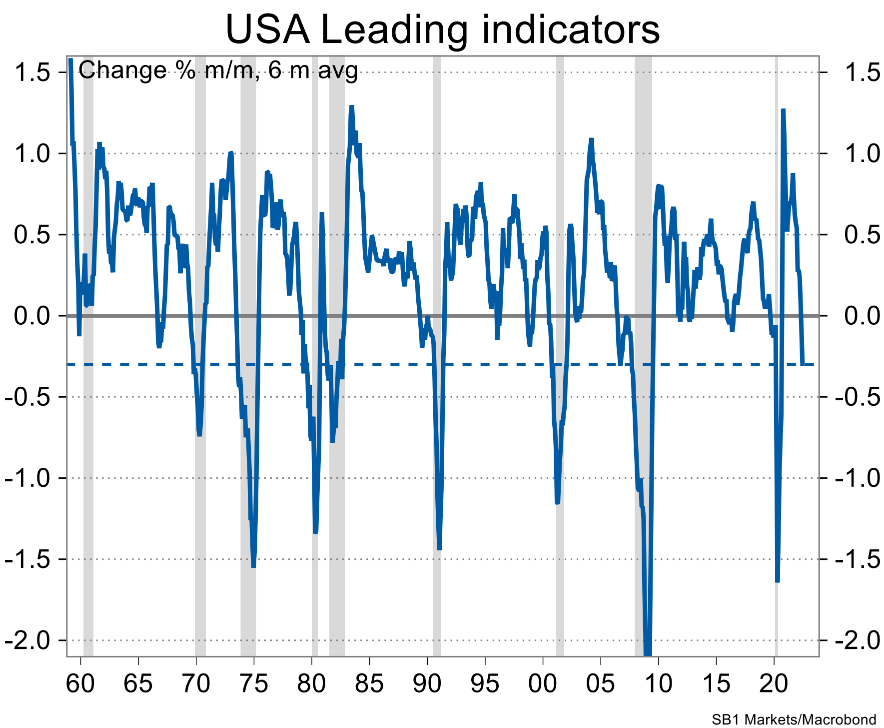


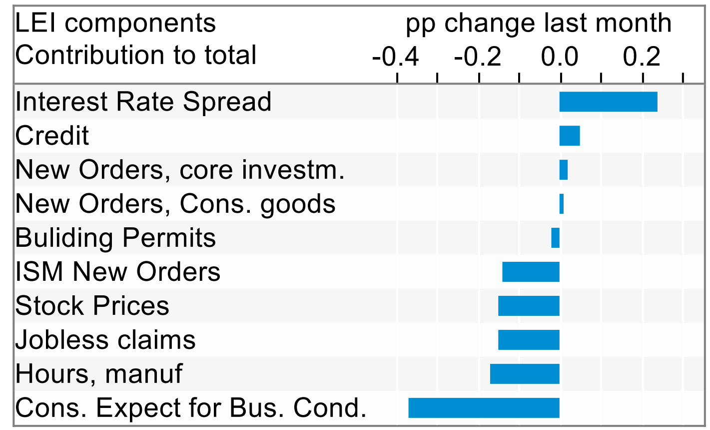
- Big picture: Growth is slowing sharply but manufacturing indices do no signal that the economy has entered a recession (even if the order indices are really worrisome)

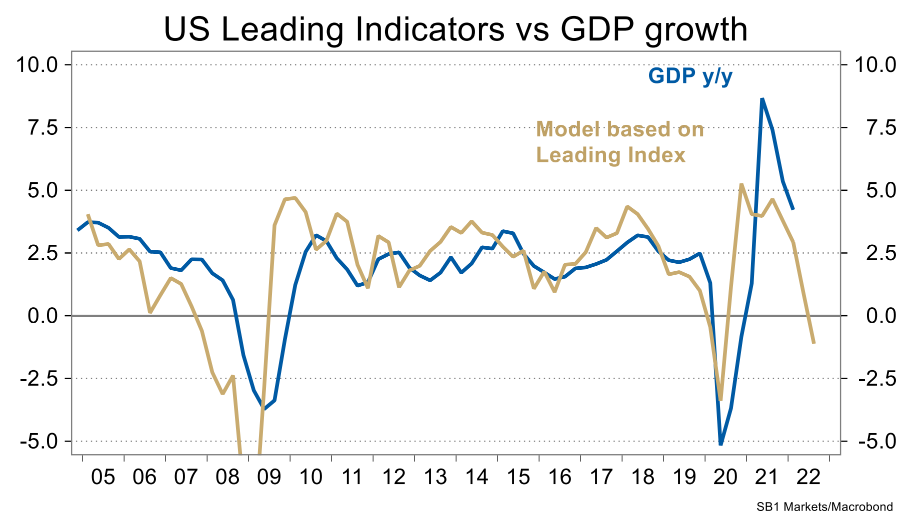
SpareBank 1 MARKETS

The Leading Economic Indicators suggest US is in or close to a recession

A 6-month avg at June's -0.3% level detected 8 of the 8 past recessions, just ½ false positive, 1 false neg.





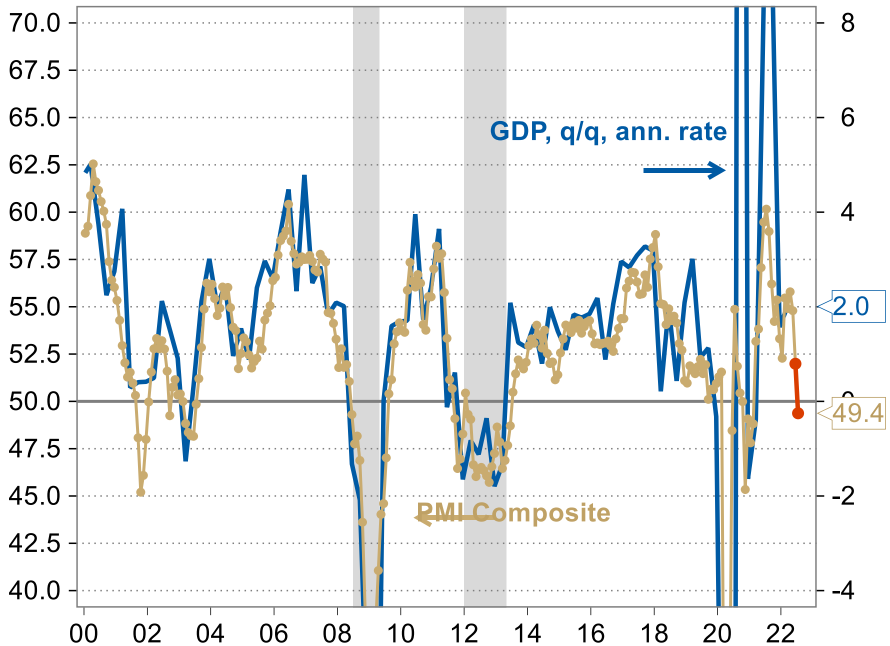


- The LEI fell 0.8% in June, 0.3 pp more than expected
- The 6 m average fell to -0.3%. The LEI has fallen to this level 9 times since 1959
  - » On 8 these occasions the US economy was very close to or had entered a recession, the 9th took place 1 year before the 2007-recession started (a ½ false positive)
  - » Thus, the LEI 6 m avg at -0.3 'detected' all 8 recessions since 1970, and barring the 2006-signal, no false positives
  - » In 1960, US entered a recession without any clear warning sign from the LEI, the only false negative

The PMIs fell more than expected everywhere, and the composite to below 50

The German PMI fell to 48, the rest just marginally above the 50-line. How much is 'left' for the ECB?

EMU PMI vs GDP



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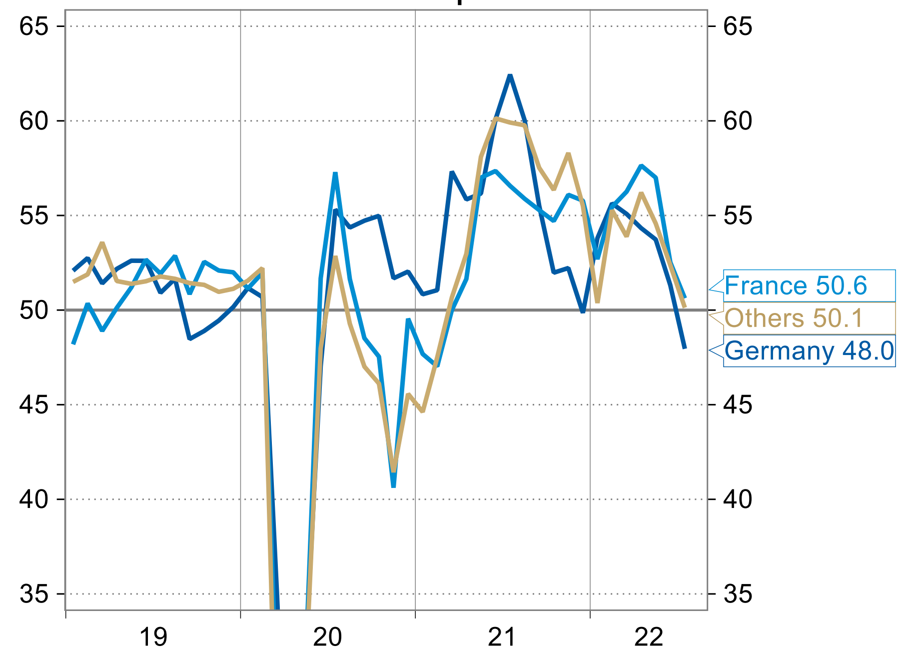
EMU Composite PMI



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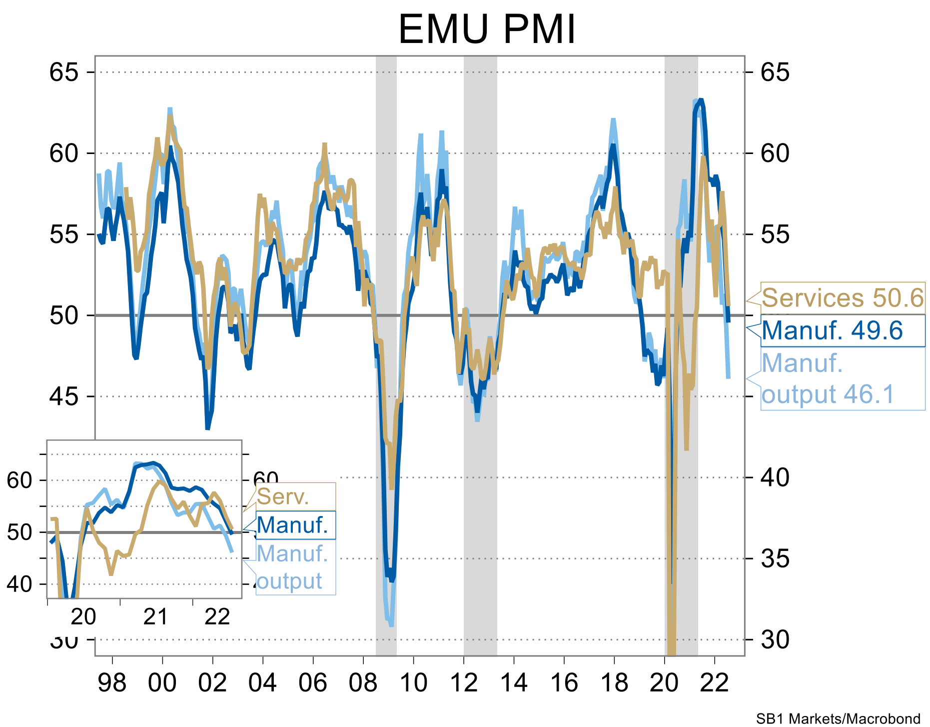
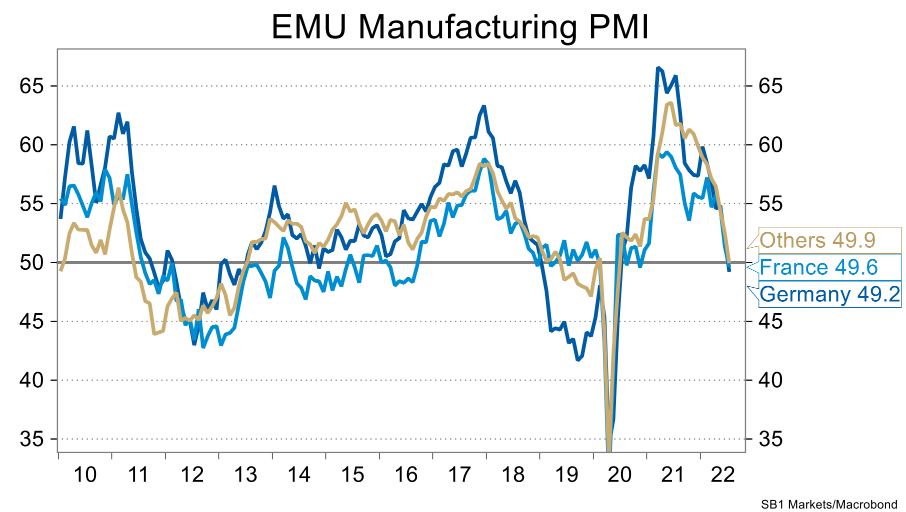
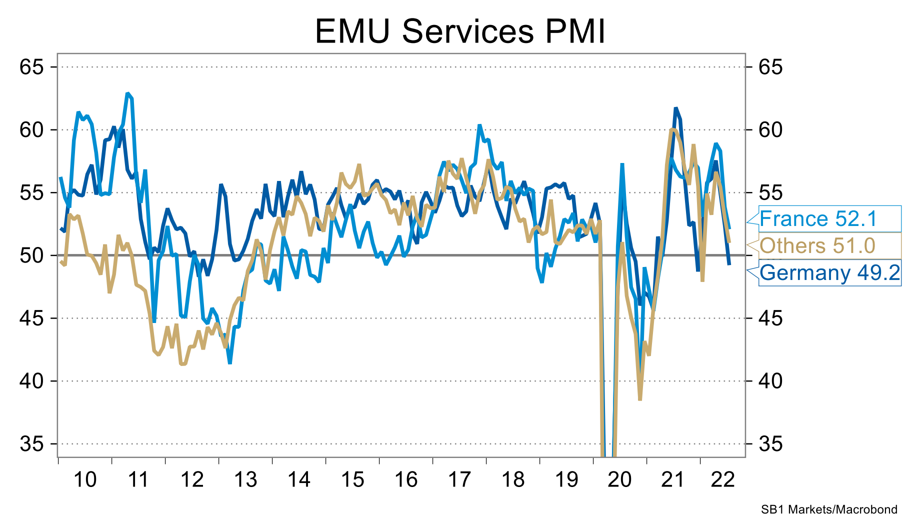
- **The composite PMI** declined 2.6 p in July, to 49.4, well below the 1 pp expected retreat to 51. The level signals a contraction in GDP
- **Services** reported much slower growth, the index fell by 2.4 p to 50.6, 0.4 p below the consensus forecast
- Manufacturing also slowed, the PMI fell 2.5 p to 49.6, 1.4 p below consensus. The output index fell 3.1 p to 46.1, and the new order index fell to 42.6 – a very weak print!
- **The delivery times** and price indices both fell substantially but still remain higher than normal. However, as new orders and production are both is declining, supply chains problems and pricing power will very likely be further reduced the coming months
- If the PMIs and other surveys continues down at the current pace, the pressure on (and within) the ECB to hike rates rapidly will no doubt fade. It is already taking place. The short/medium-term peak on the FRA curve has fallen to 1.4% (mid 2023), from 2.65% (late 2023) at the peak in mid June, following a substantial decline last week too, even if ECB hiked by 50 bps

Manufacturing has probably entered the contraction zone?

The output index fell well below the 50-line. Services are also reporting slower growth

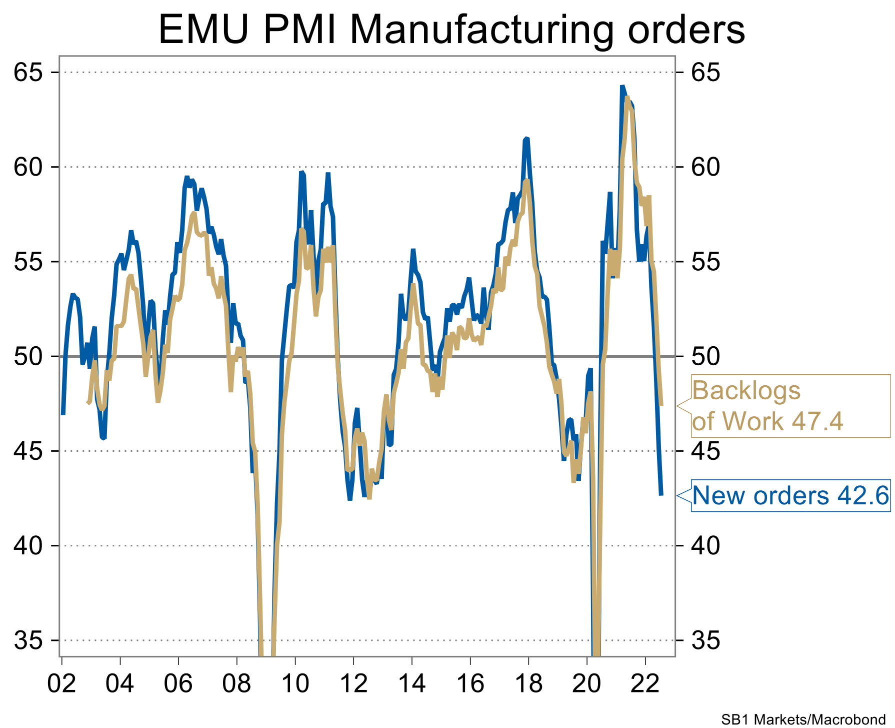


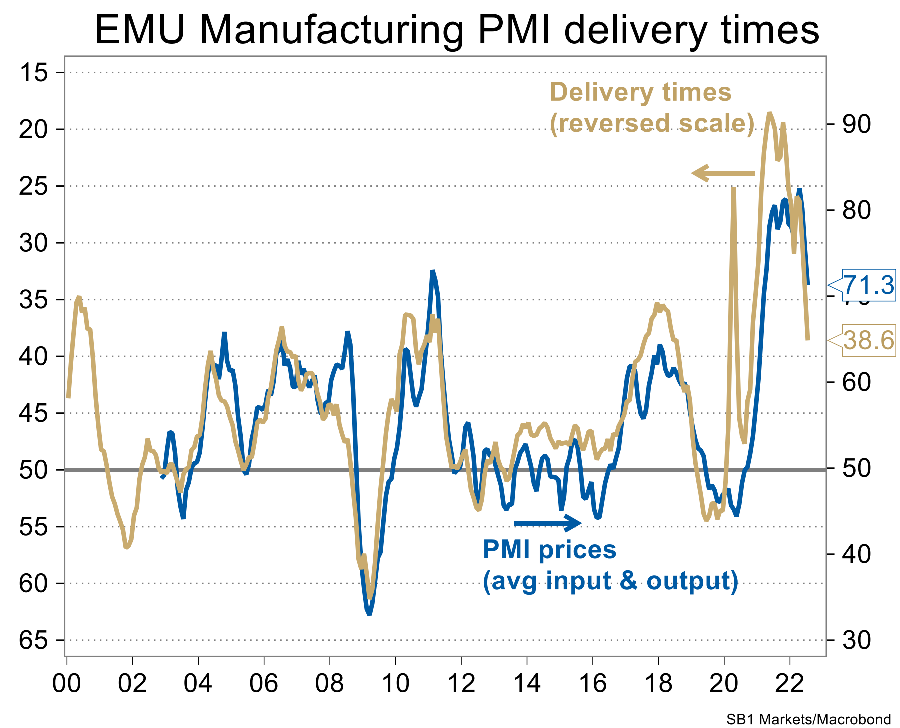




New orders sharply down, and even the backlog is contracting

Both the delivery times and price indices are falling rapidly, signalling less prices pressures

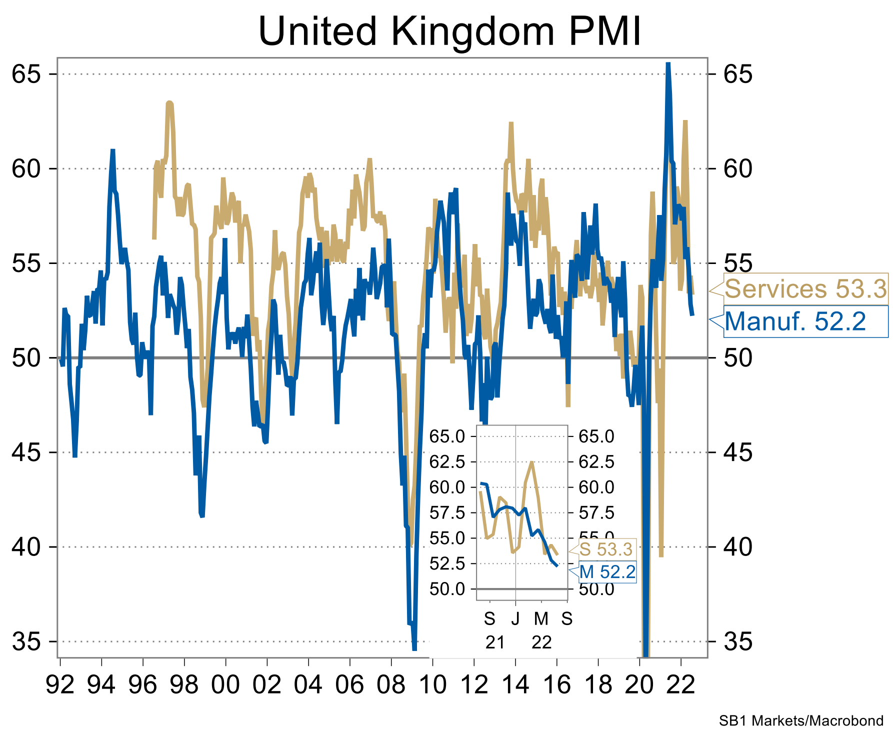


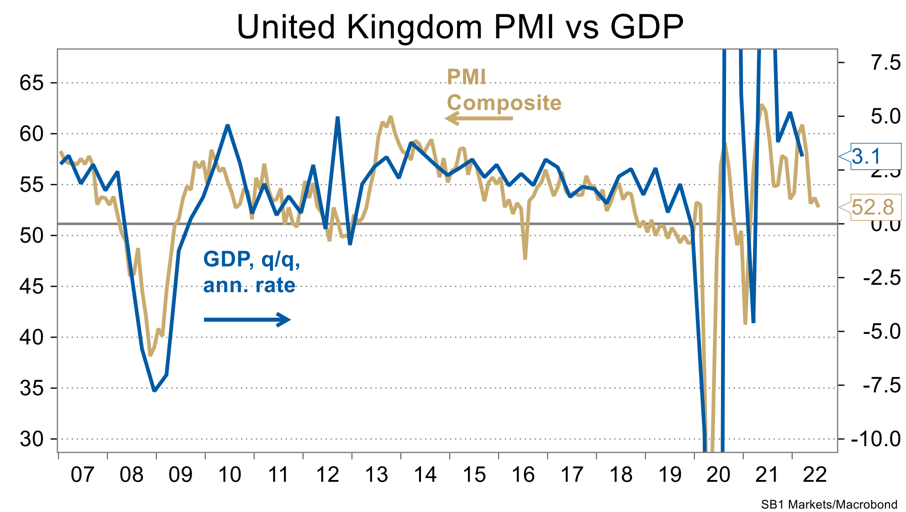


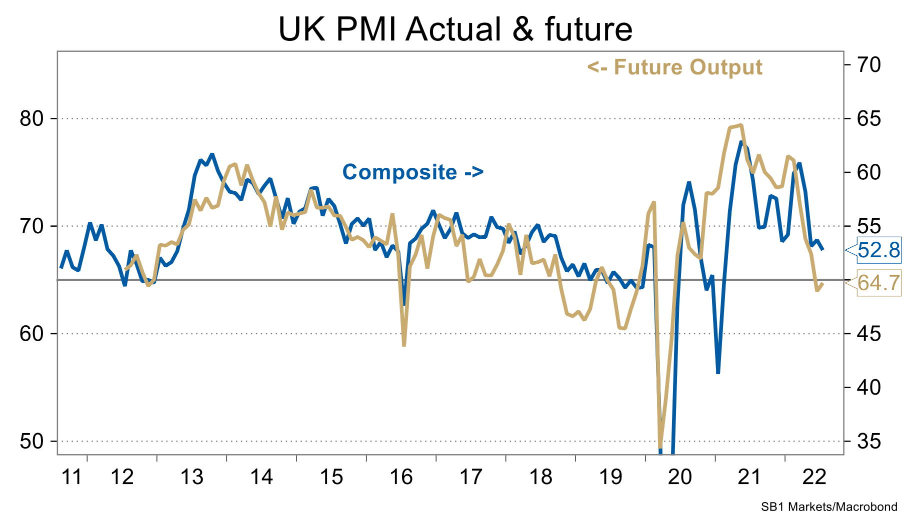
- However, companies are still reporting unusual widespread price increases!

The composite index just marginally down in July, at 52.8 signalling 1% growth

These days, not that bad. Both manufacturing and services contributed on the downside in July



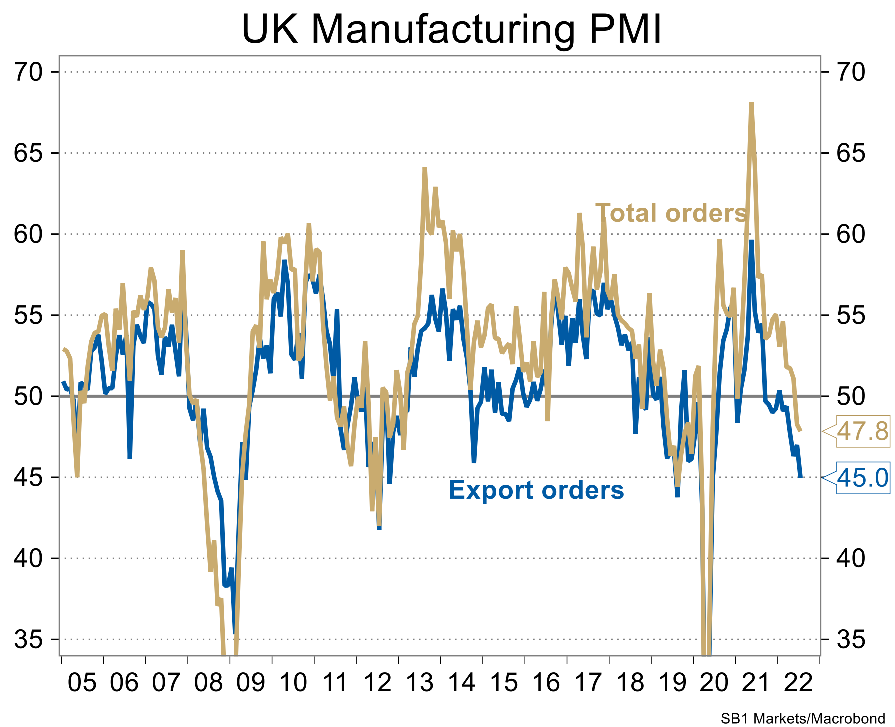


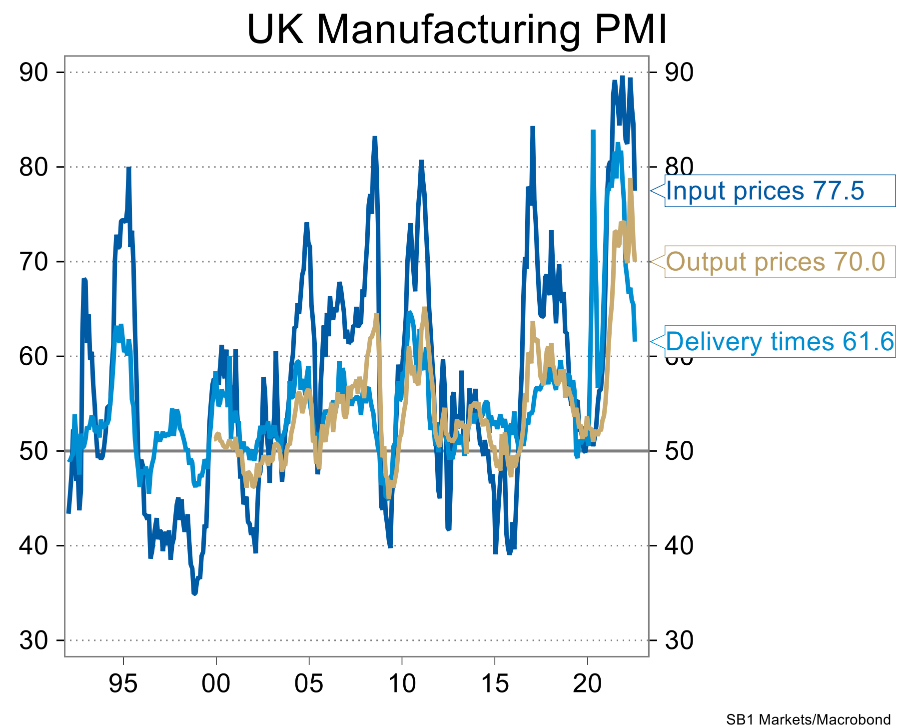


- The UK composite index fell 0.9 p but was 0.3 p stronger than expected – while both rest of Europe and the US surprised significantly on the downside

Order growth has turned negative, while delivery times slows

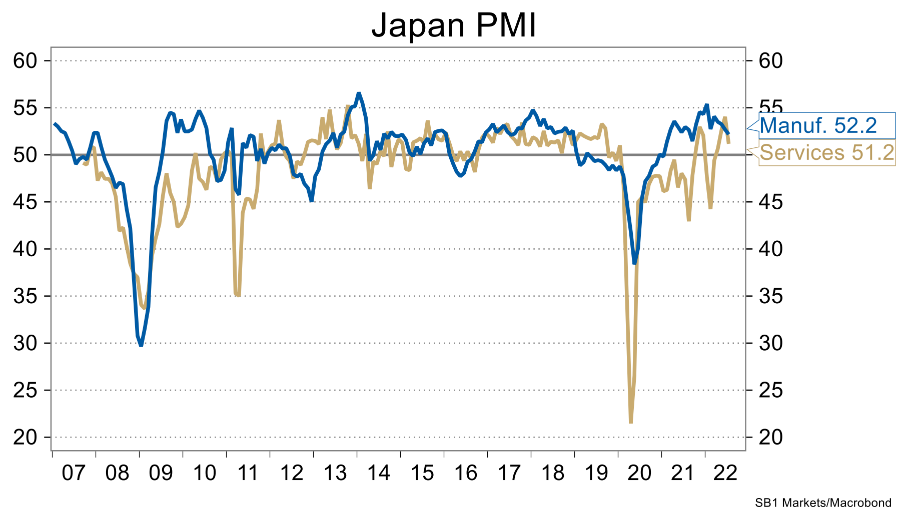
The price indices fell sharply as well but are still above normal levels, especially the price indices

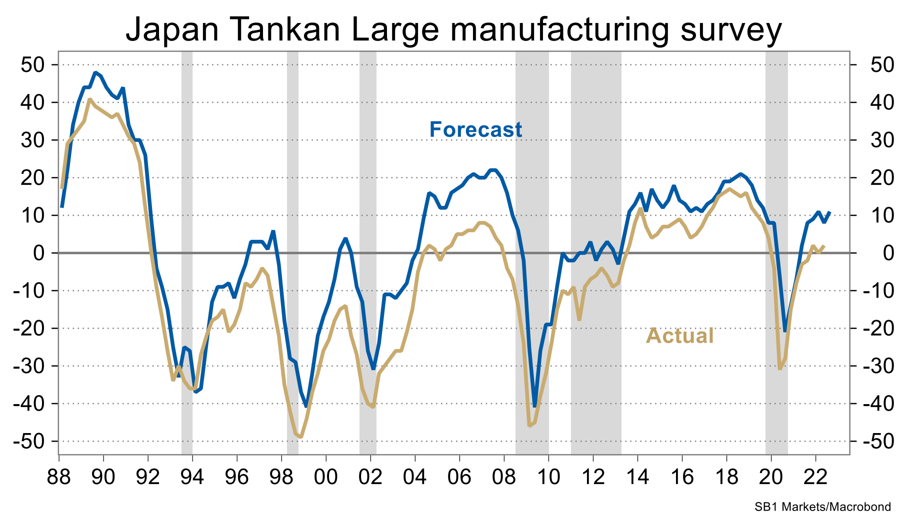


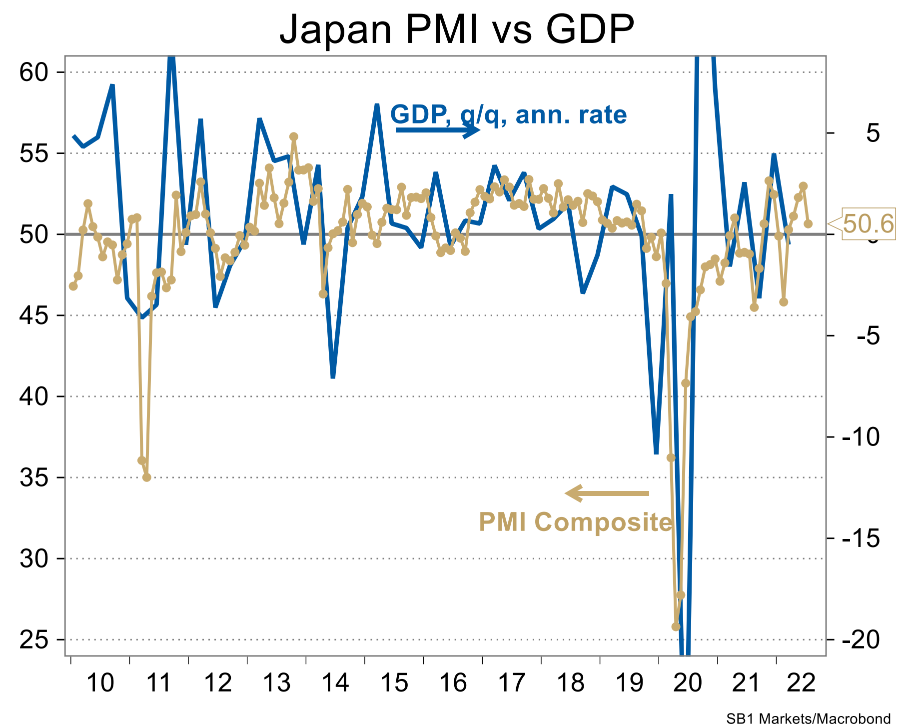


The service sector PMI fell back to 'normal' level in July. Zero GDP growth?

The manufacturing index continued downwards, but is still well above the 50-line



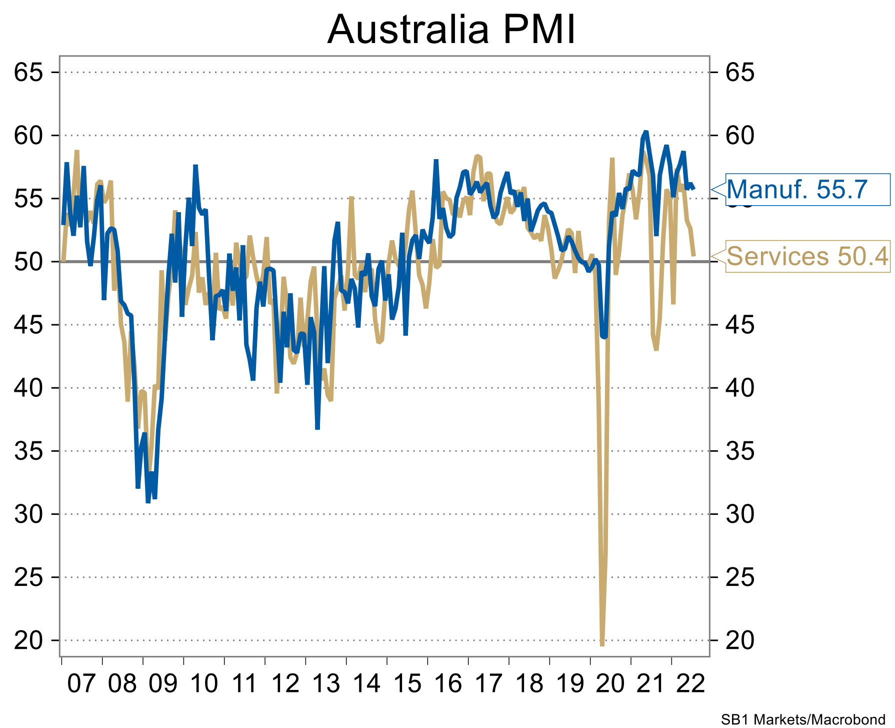


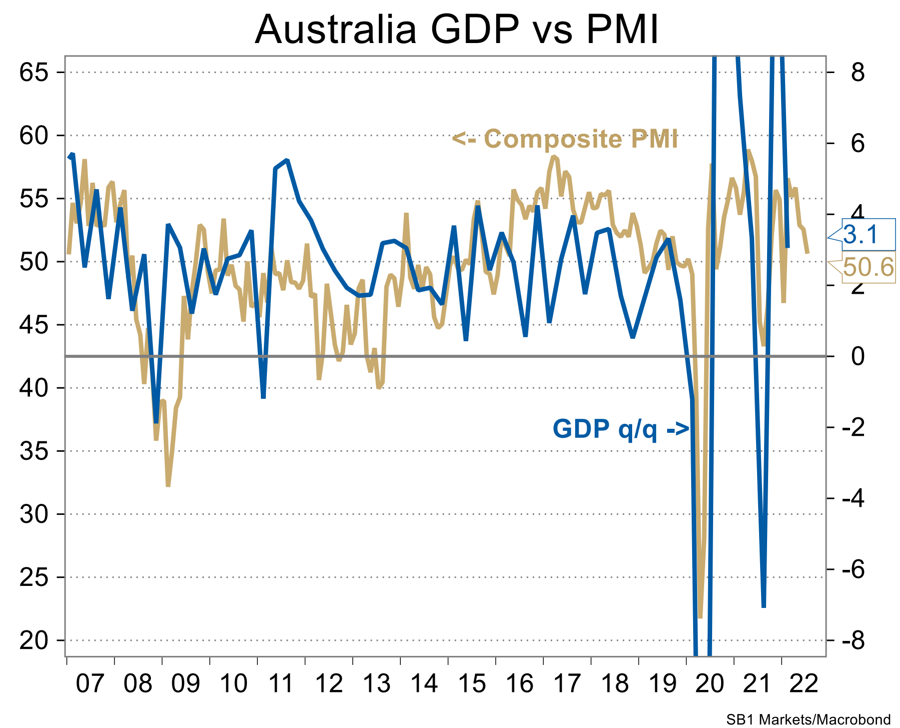


- Most of the positive reopening effects for the service sector have probably already taken place

Services are slowing down, even if the manufacturing sector is still going strong

The composite index at 50.6 is not impressive by itself, but in Australia normally signalling OK growth

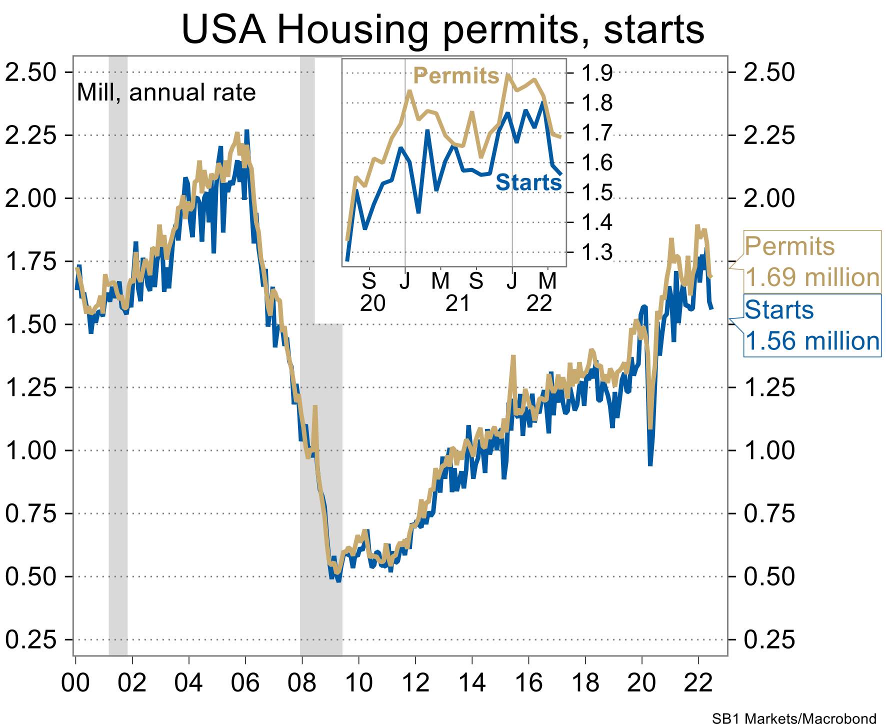


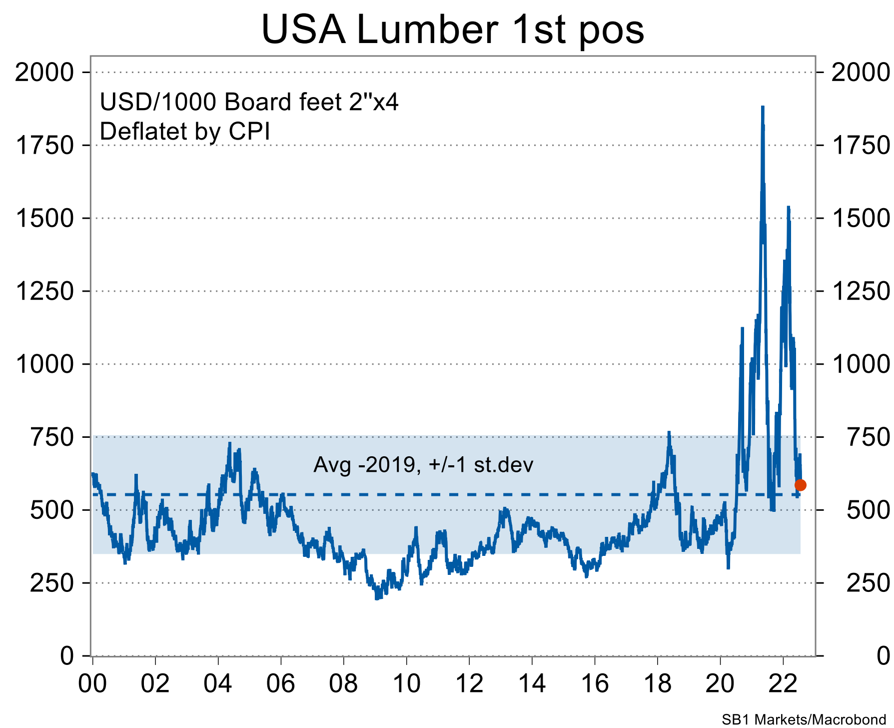


- Disclaimer: The correlation between the PMIs and actual GDP growth is not that impressive
- The manufacturing sector has not been hurt by the temporary lockdown setback in China

Housing starts/building permits are trending downwards

But the decline in June was not that large



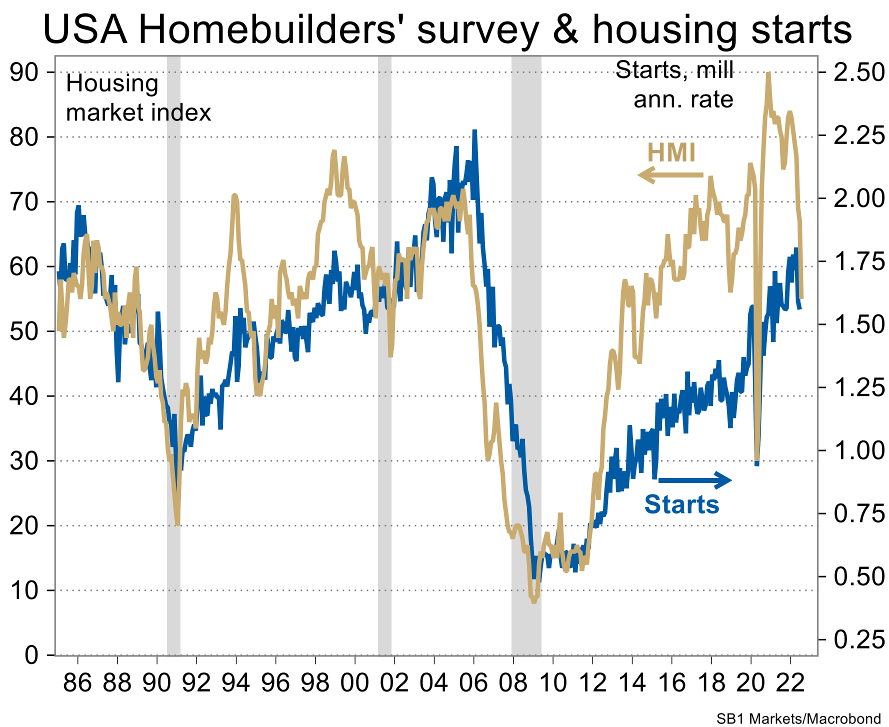


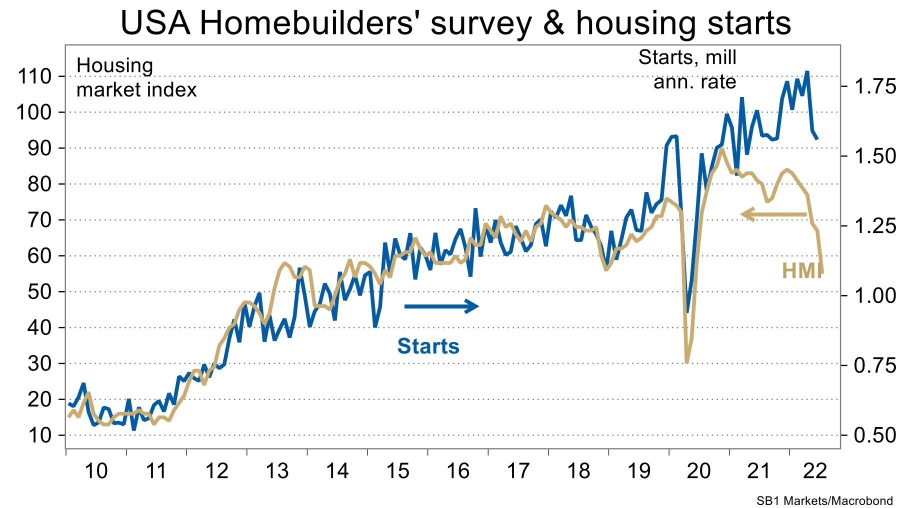
- **Housing starts** fell to 1.56 mill in June from 1.59 (revised from 1.55), expected 1.60 mil. **Building permits** landed at 1.69 mill, expected 1.68 mill, from 1.70 mill in May. Levels are still high but the tide has turned: The Housing market index shows the way, check next page
- Building **material cost inflation** has come to a sudden halt. **Lumber prices** have 'collapsed' recent weeks and are now back to a normal level, steel prices are falling rapidly too

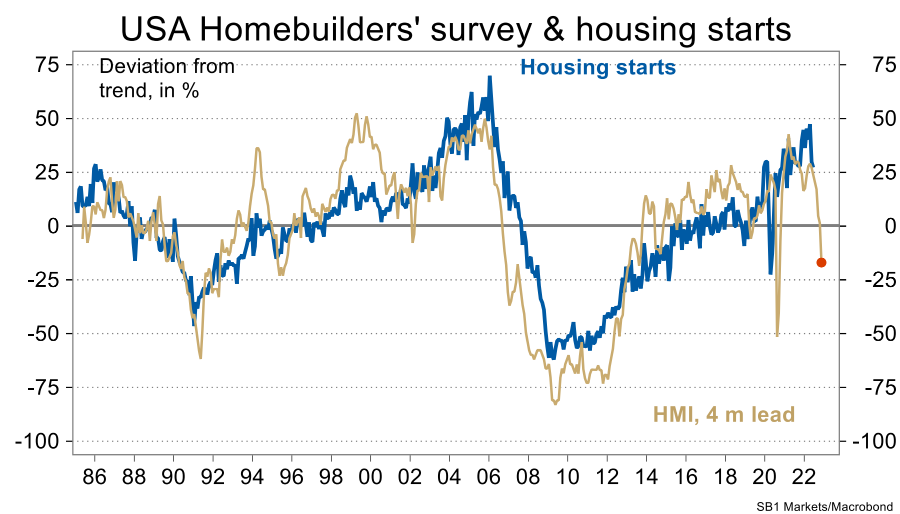
Reprint from last week's report, but still very relevant

Homebuilders' index straight down in July: a further, steep decline in starts ahead

The HMI down 12 p to 55, the 2nd largest decline ever (after April-20). Starts down



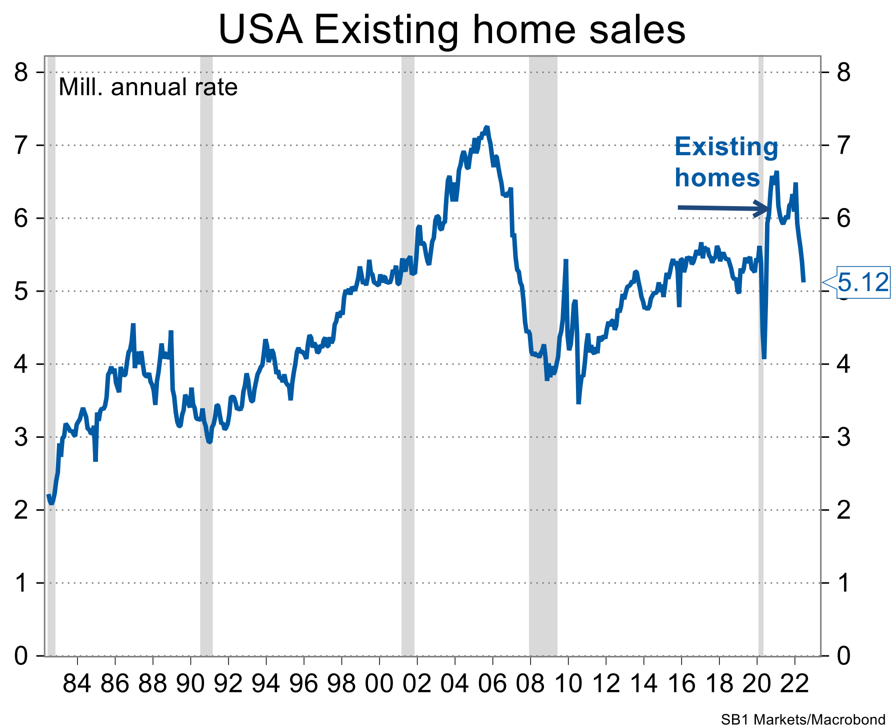


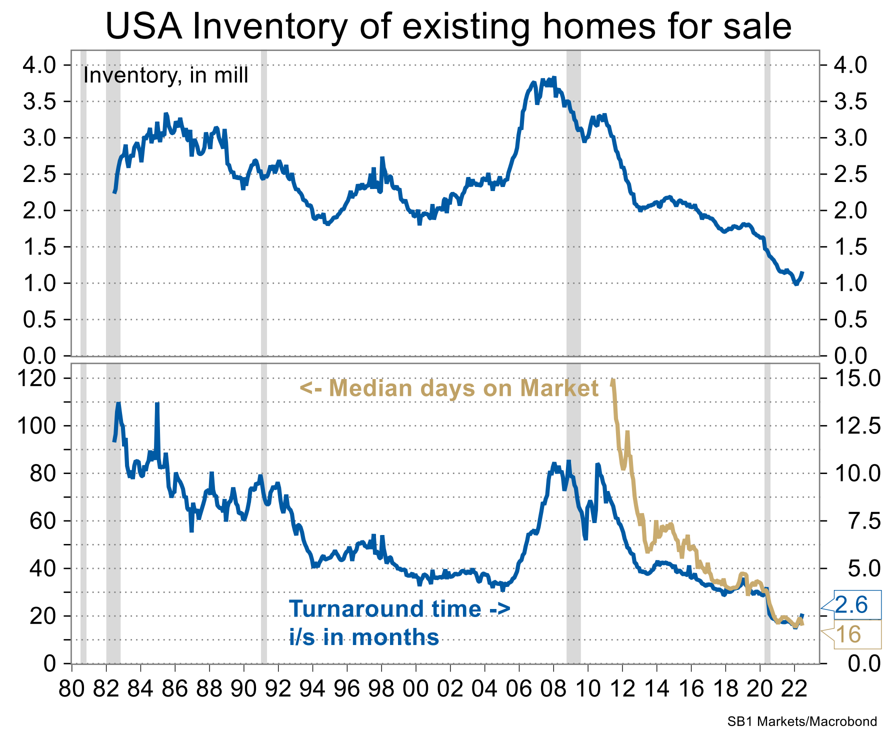


- **The Homebuilders' Housing Market Index (HM)** lost 12 p to 55 in July, expected down just 1 p! The monthly setback is unprecedented, ex. April-20 (as is the decline over the past 3, 6 or 8 months)
  - » Affordability is still the challenge, due to higher mortgage rates, and soaring new home prices (at least until now)
- The decline in the index recent months signal more than a 1/3 decline in housing starts – which already has fallen by 14% - in sum a 50% setback

Existing home sales further down in June, and price inflation almost down to 0

The inventory is still very low – but has increased marginally the past 4 months

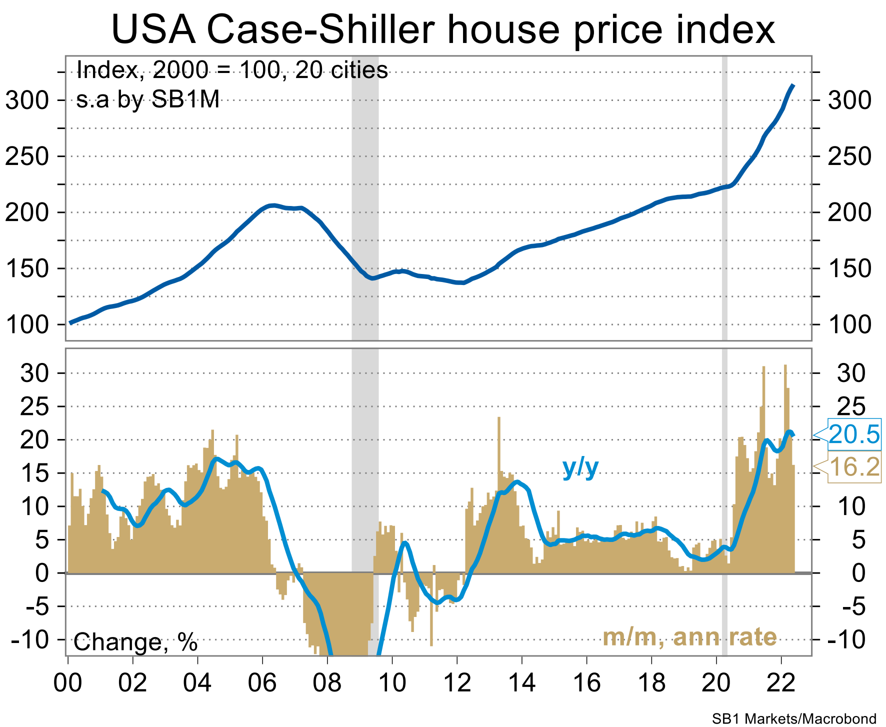


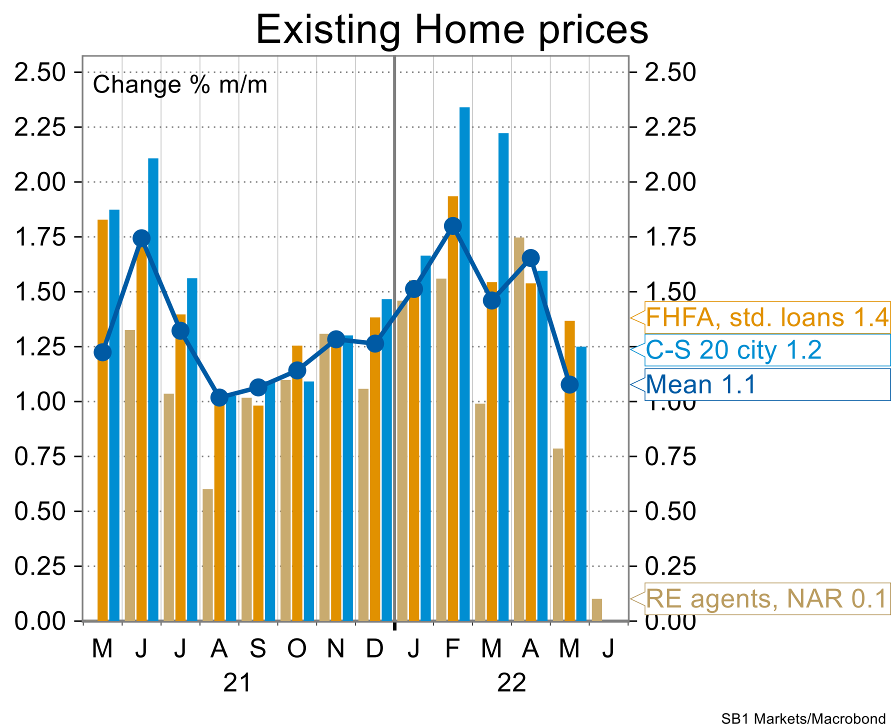


- Sales of **existing homes** fell to 5.12 mill (annualised rate), from 5.41 mill in May, expected close to unch. Sales have fallen by 21% from local peak in January. **Pending sales** signals a further decline in actual transactions in July
- **The inventory of unsold homes** rose marginally in June, as during the previous months – from at ATL in February
  - » The inventory equals 2.6 months of sales (up from 2.4 last month). During the 2005 boom, the i/s ratio was 4 months, in bad times it has been as high as 10 months
  - » Still, the median time on the market for those homes actually sold is just 16 days (down from 18 last, and close to ATL). Before the pandemic the time on market was at 30 days (and 120 days in 2011!)
- **Prices** rose 0.1% m/m in June, *check more next page*
- **Mortgage rates** have fallen recent weeks but remain far higher than over the previous years – and the high price level (up close to 40% since before the pandemic) has crushed affordability – and the impact is now very visible

House price inflation is slowing but Case/Shiller still reported a 1.2% lift in May

Realtors reported 0.1% price increase in June

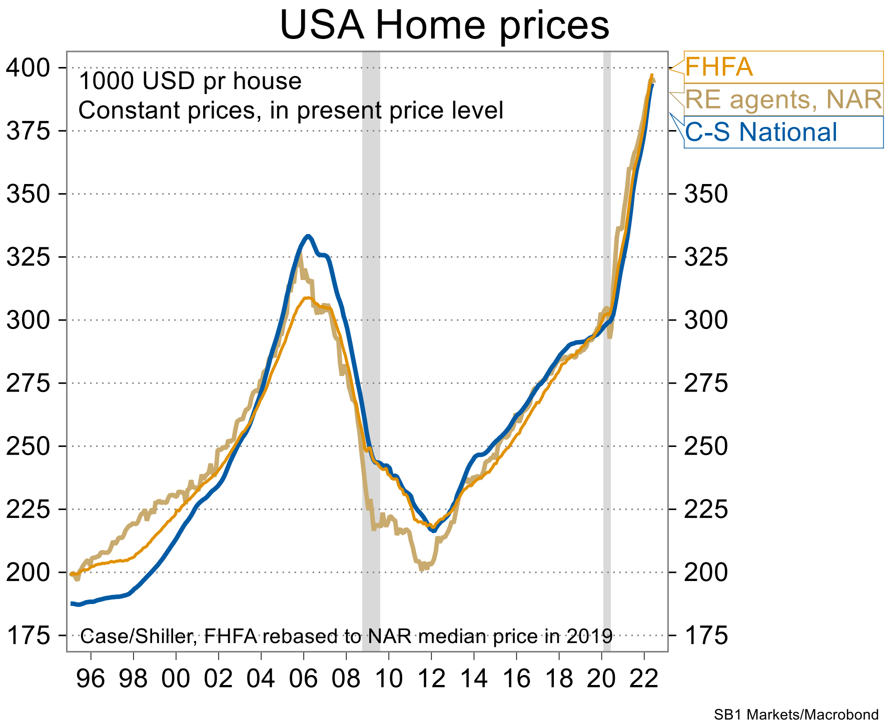


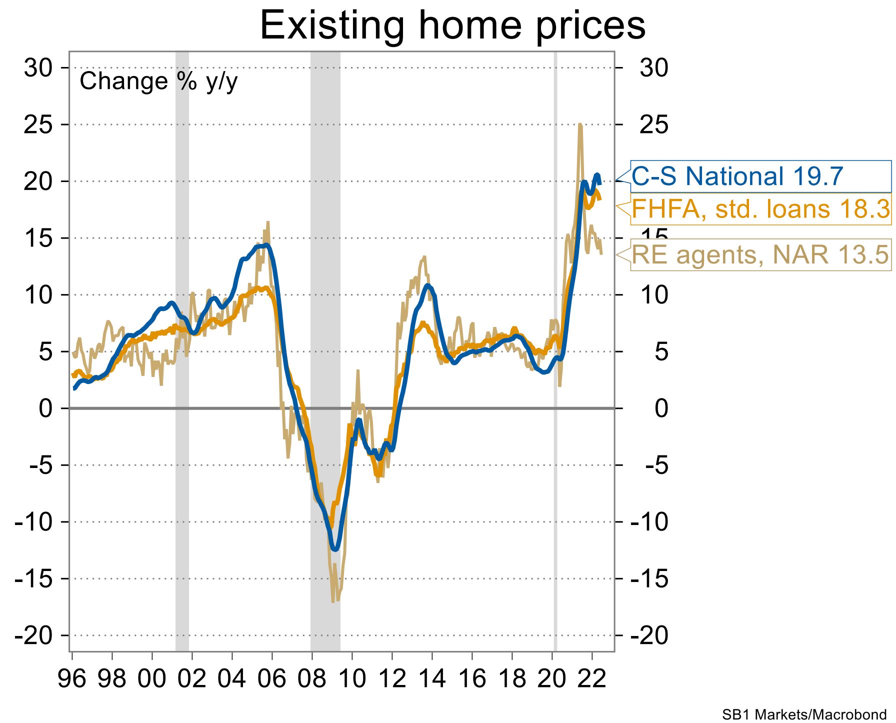


- **S&P's Case/Shiller's 20 cities** price index rose 1.2% m/m in May (April - June avg, our seas. adj) equalling a 16% annualised pace, well down from the recent peaks but still a very rapid price appreciation. A 1.5% increase was expected. The annual rate fall marginally to 20.5%. The national index is up by 19.7%
- **The FHFA** (Federal Housing Financing Agency) price index, which covers homes with loans guarantied by the government sponsored Fannie Mae or Freddie Mac ('Husbankene', has a countrywide coverage), rose 'just' 1.4% in May, and are up 18.3 y/y!
- **Realtors** reported a 0.1% lift in June, prices are up 13.5% y/y
- <u>However, even if prices cover transactions closed up to June (included in the April-June average), those deals were mostly agreed upon in May (as for the realtors index)</u> – and 'something' might have happened since May. Anyway, <u>we still expect prices to yield substantially the coming months, following the unprecedented 40% lift since before the pandemic</u>

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

Real prices are 17% – 26% above the pre-financial crisis peak

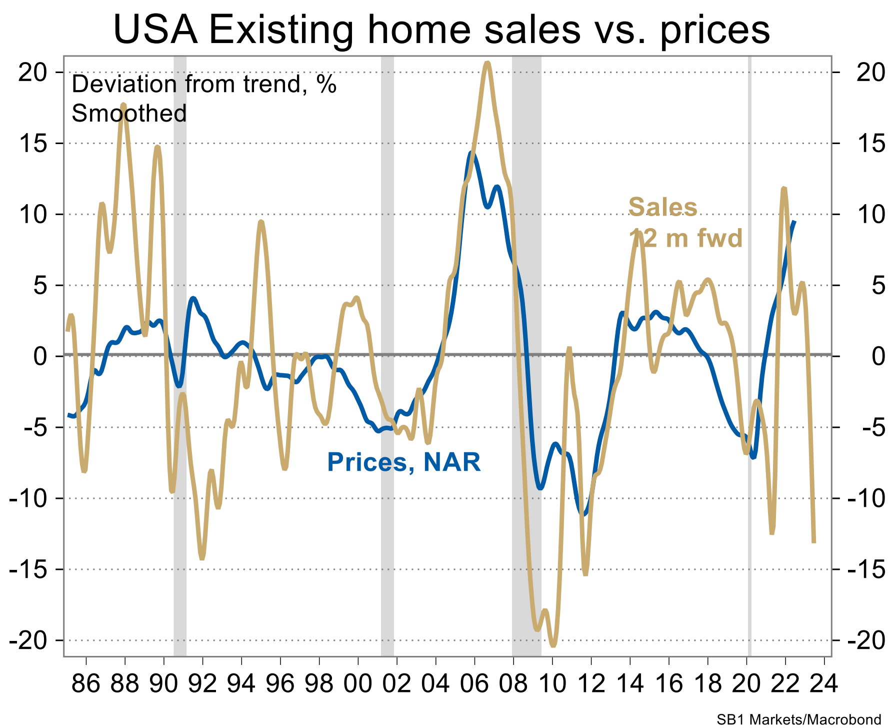


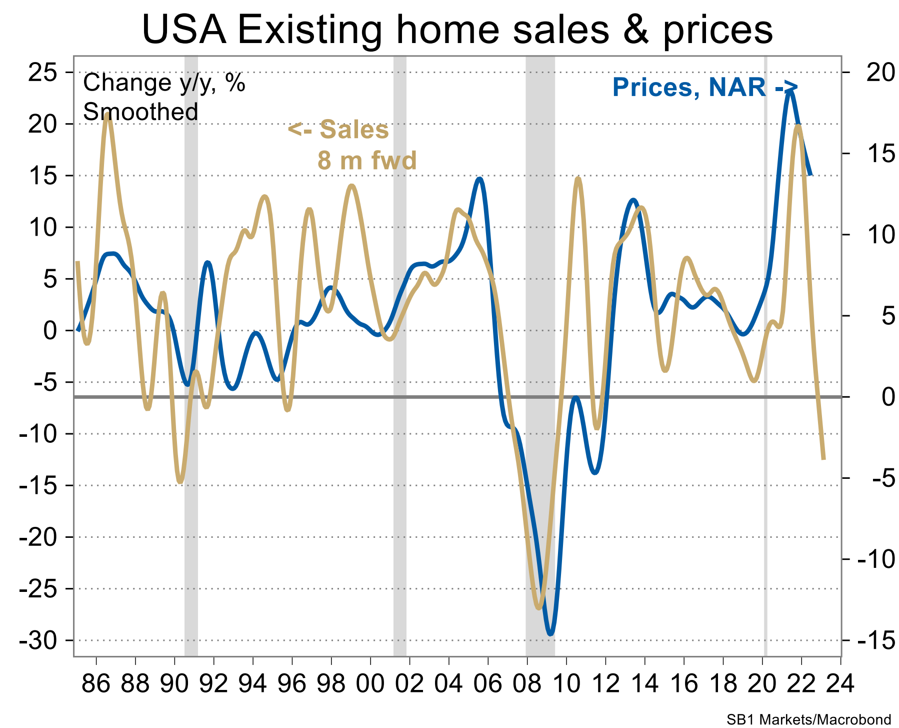


- Both the Case-Shiller National index, FHFA's index for homes with government sponsored mortgages (which includes most homes), and the realtors' price index have been reporting the highest house price appreciation ever (or since 1948) during the past months
- Real prices are far above the 2006 peak, by some 17% – 26%
- There are still some big differences vs the mid 2000 housing bubble
  - **Housing starts** are at a lower level. The **inventory** of 2nd homes for sale is still low (vs high 15 – 16 years ago). However, the inventory of new homes for sale is climbing rapidly
  - Households average **debt/income ratio** has fallen sharply since the peak before the financial crisis, and their cash positions have soared (on average) to above debts. However, credit growth has accelerated rapidly during the pandemic
  - The **savings rate/net financial investments rate** has now fallen to well below the pre-pandemic level – but the ratios are far above the level in 2005

When home sales turn south, prices follow. Normally after a while

Thus, a focus on transactions is justified – even if prices are the 'real thing'

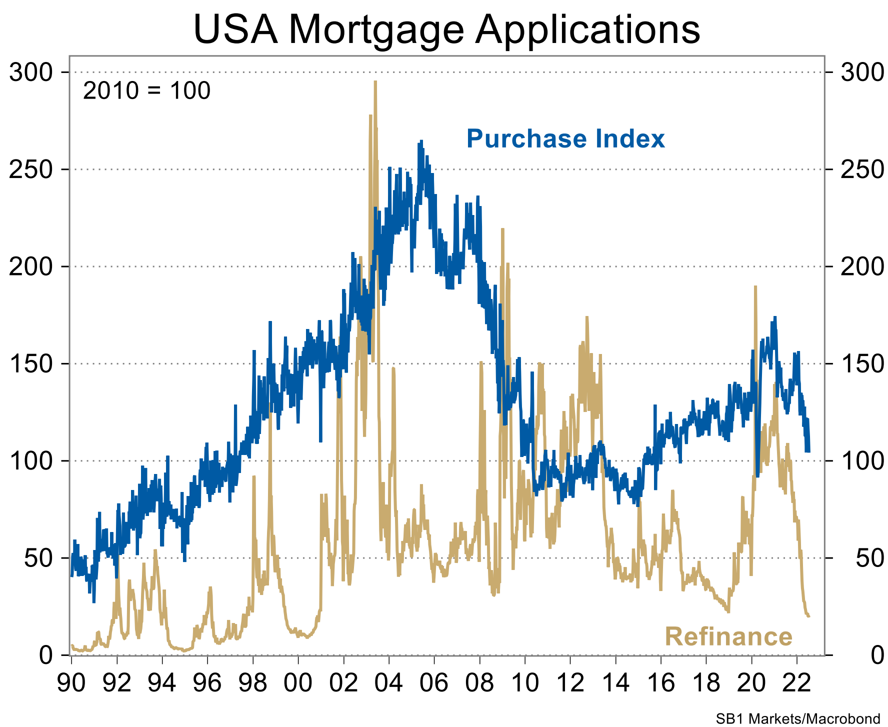


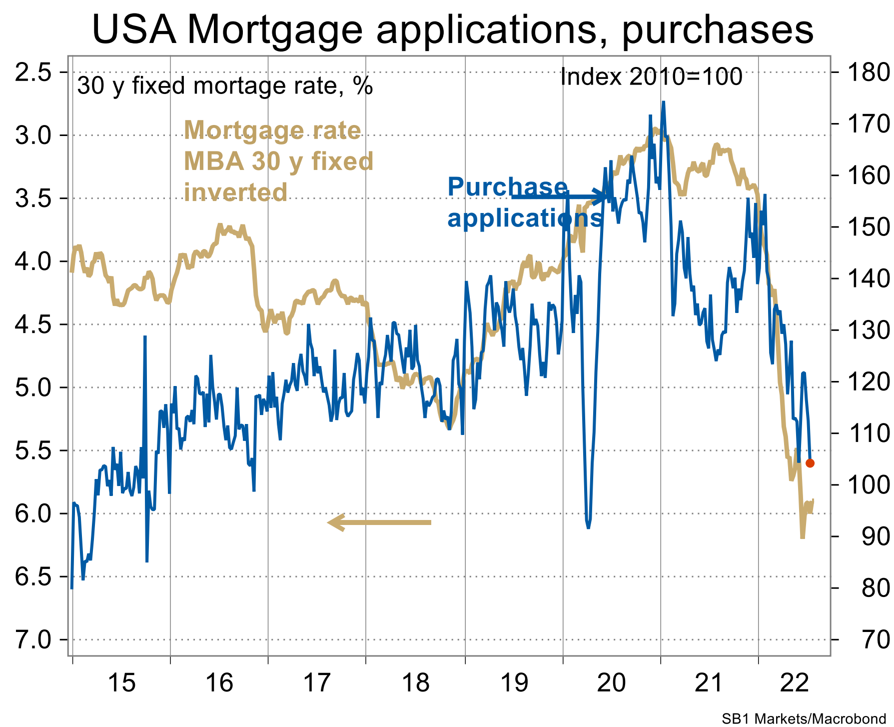


- Sales peaked in Jan-21 but probably mostly due to lack of supply – and prices have not yet yielded. The recent decline in sales, which started in Feb-22, is no doubt due to a softening demand, signalling a substantial downside risk for prices, especially given the unprecedented 2 y surge during the pandemic

Mortgage applications are rapidly on the way down, for good reasons

Applications for new loans are down by 1/3 from the local peak in January

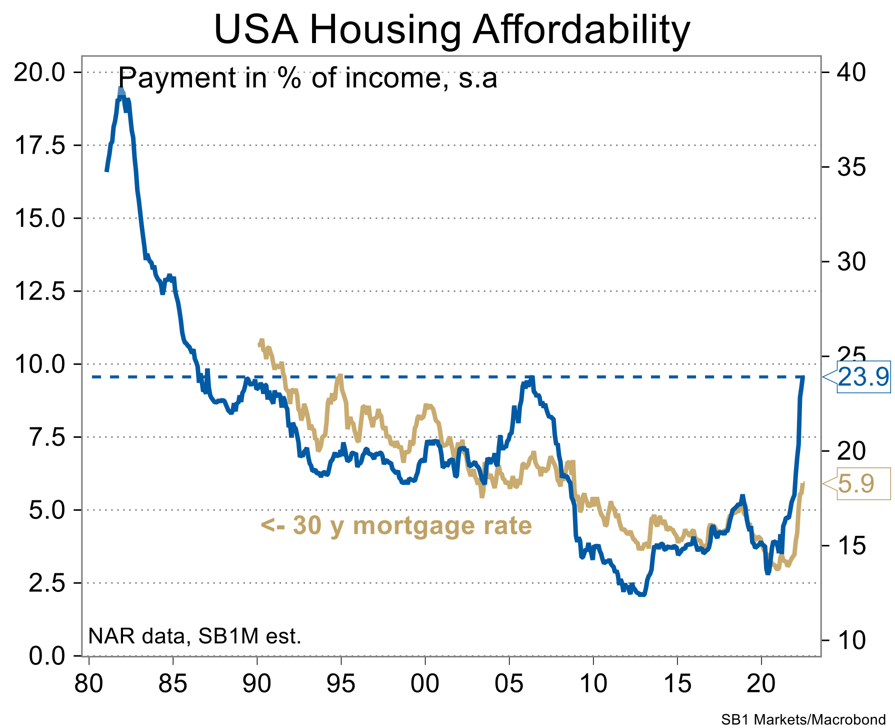


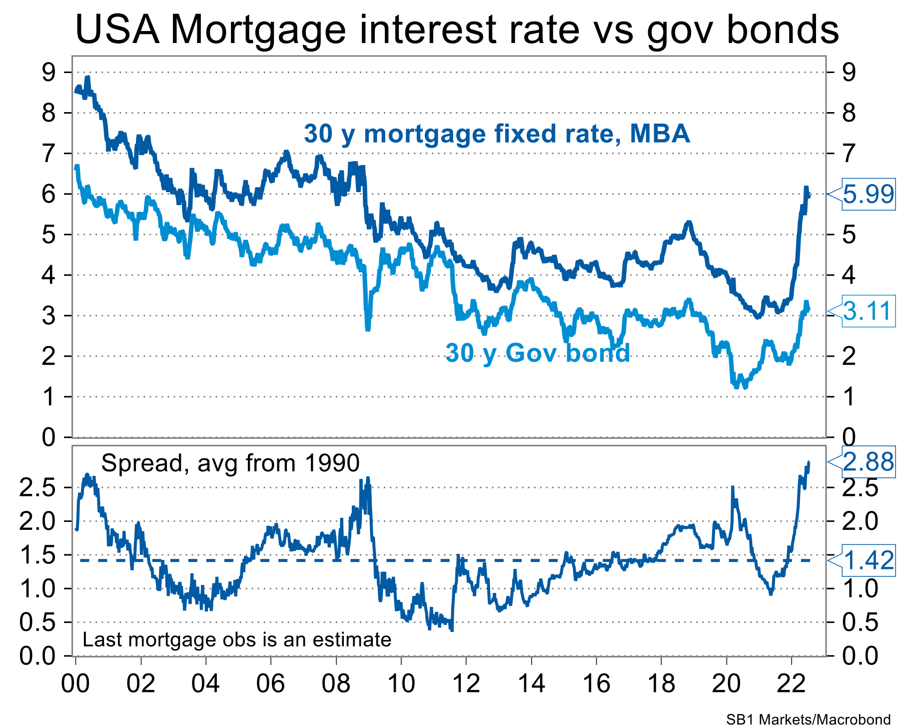


- Demand is not yet extremely low – and the level is ‘just’ 20% below the pre-pandemic level

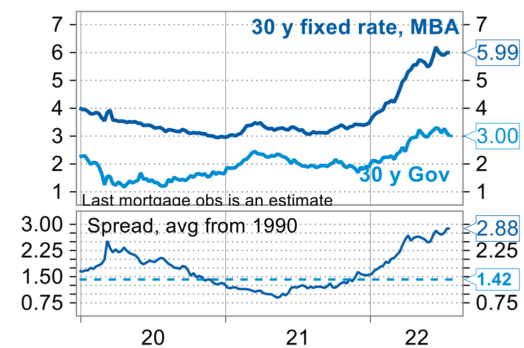
The least affordable housing market since 2008 (almost since 1987)

Prices are up 37% since before the pandemic, the mortgage rate is up 50%. In sum….



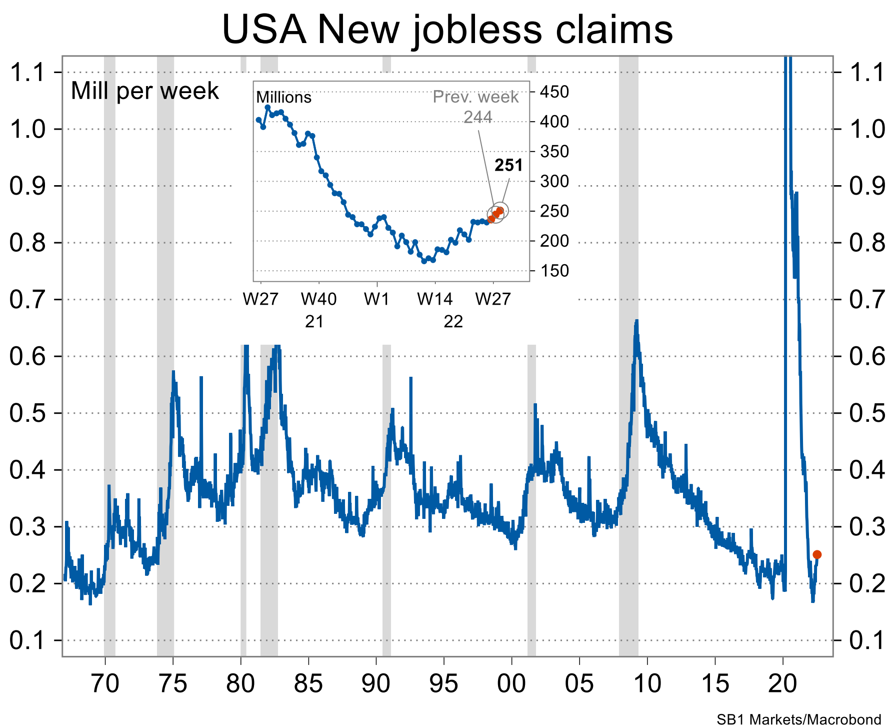


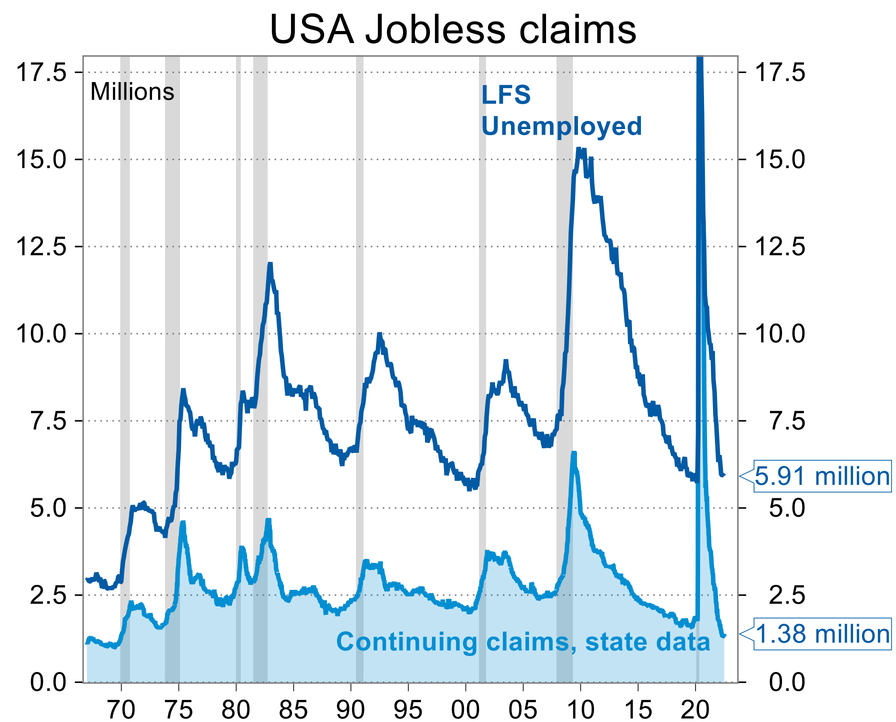
- **The 30 y fixed mortgage rate** has climbed to 5.96% (effective rate) from 3.0% last summer, from 3.5% at the start of 2022. Before the pandemic, the rate was 4.0%
- The **Federal Reserve** concluded its mortgage backed bonds buying campaign in March - <u>and has now start reducing its holdings. No doubt, this shift explains the surge in the spread, to 2.66 pp, way above the average at 1.41 pp</u>



New jobless claims are sending a warning signal: A recession not unlikely at all

Check the charts at the next page

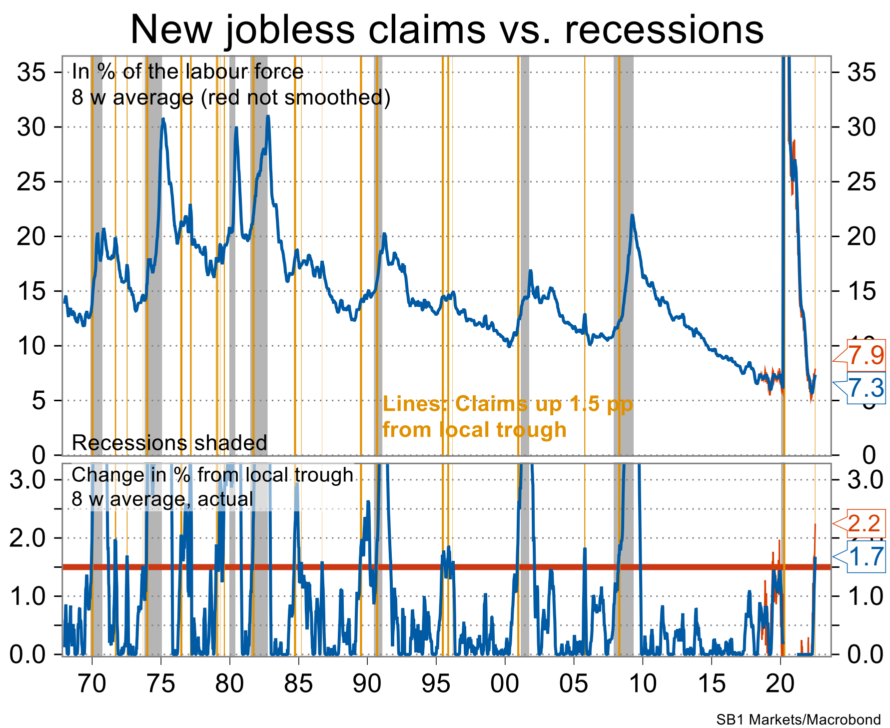


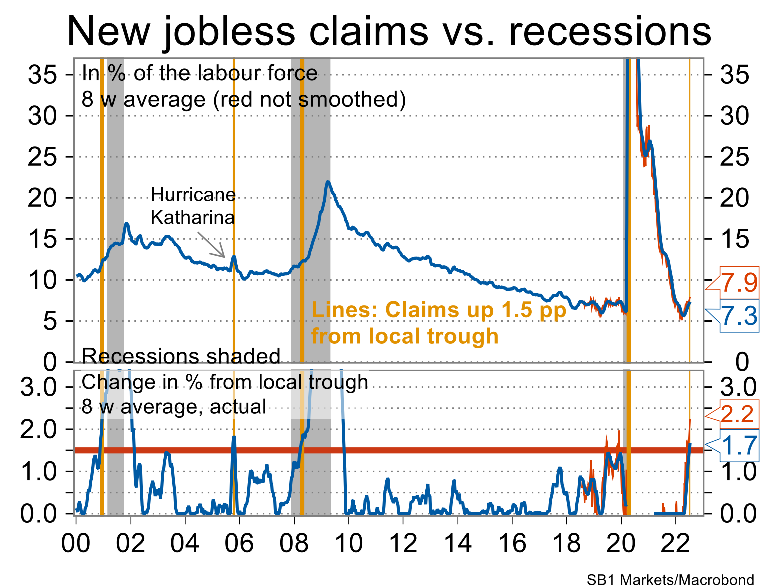


- **New jobless claims** rose 7’ to 251’ in week 28. Since the bottom in week 11 in mid-March, the weekly inflow has increased by 85’, from 166’ – which was the lowest since 1969. Measured
- **Ordinary continuing claims** fell 51’ to 1.38 mill in week 27, a very low level – but have probably also bottomed

A yellow warning line is drawn:

The lift in the 8-week average has crossed an important threshold

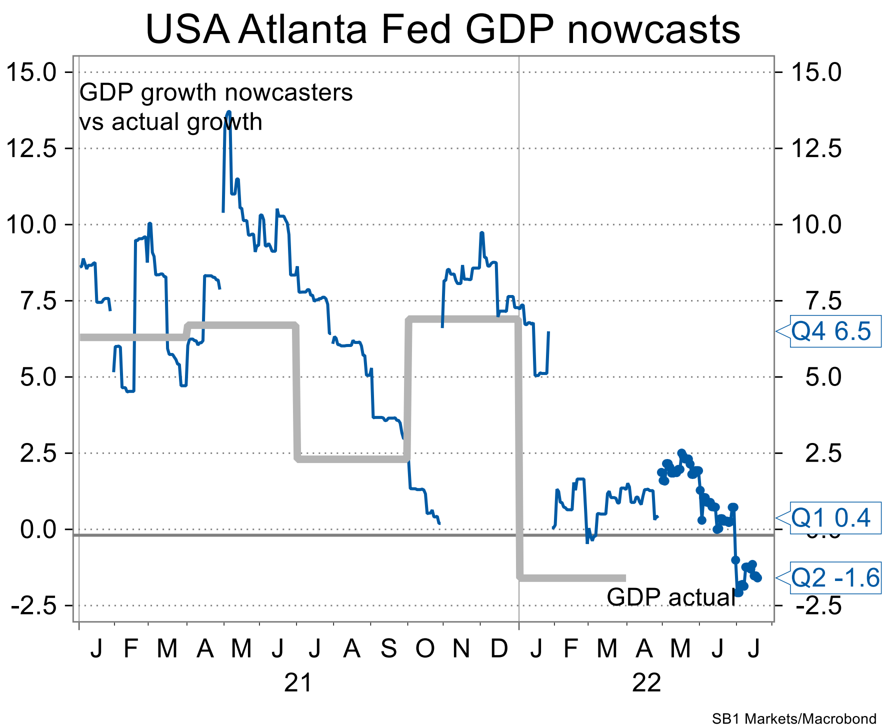


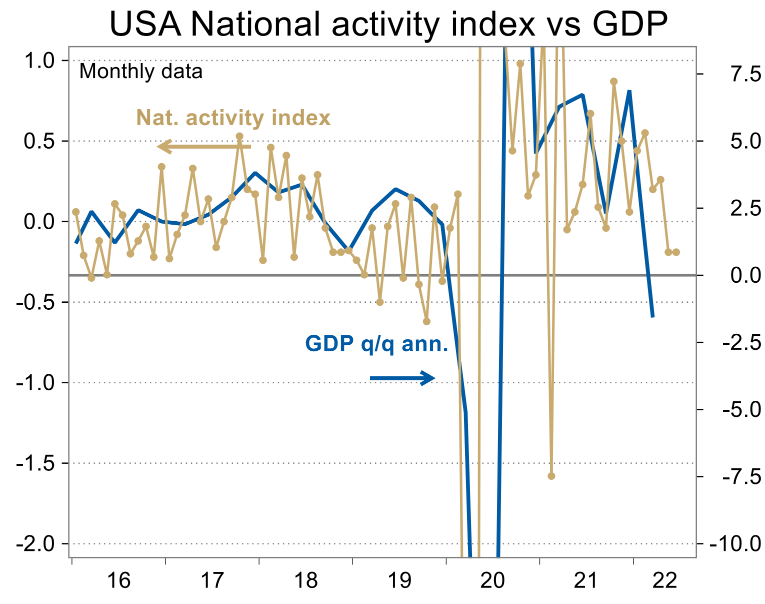


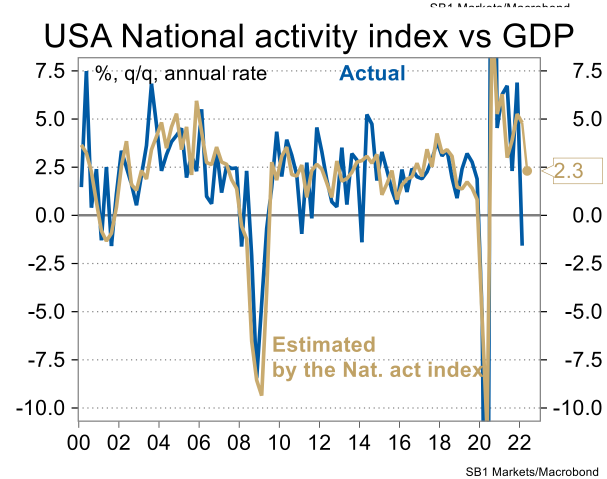
- The yellow lines: New jobless claims (8-week average) up 1.5 pp vs. the labour force
- Now, the average is up 1.7 pp, from 1.5 pp the previous week. Thus, a yellow line is now drawn at the charts above, for the first time since 2005 (Hurricane Katharina), without a recession around the corner (the lines in 2008, 2020), and before that in 1996
- Our recession signal model based on new jobless claims has sent several false signals (false positives), and even the correct signals often comes too late for a real time conclusion. Even so, the inflow of new unemployed persons is tightly correlated to the economic cycle – and the cycle is now weakening (Lifting the threshold to say 2% would strengthen the signal/noise ratio substantially. We may be there pretty soon)

Atlanta Fed's nowcaster suggests GDP fell at a 1.6% pace in Q2

The Nat. activity index says +2.3%. Economists go for +0.8%. The first official estimate out this week



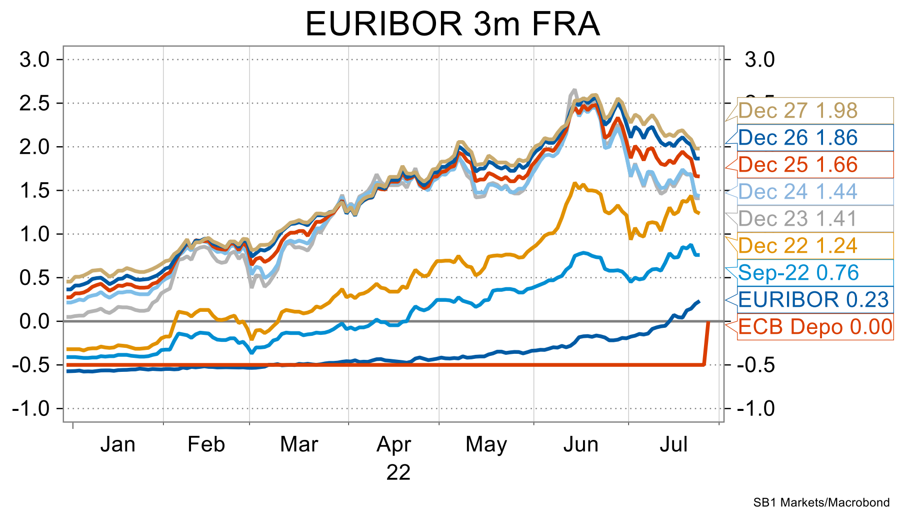


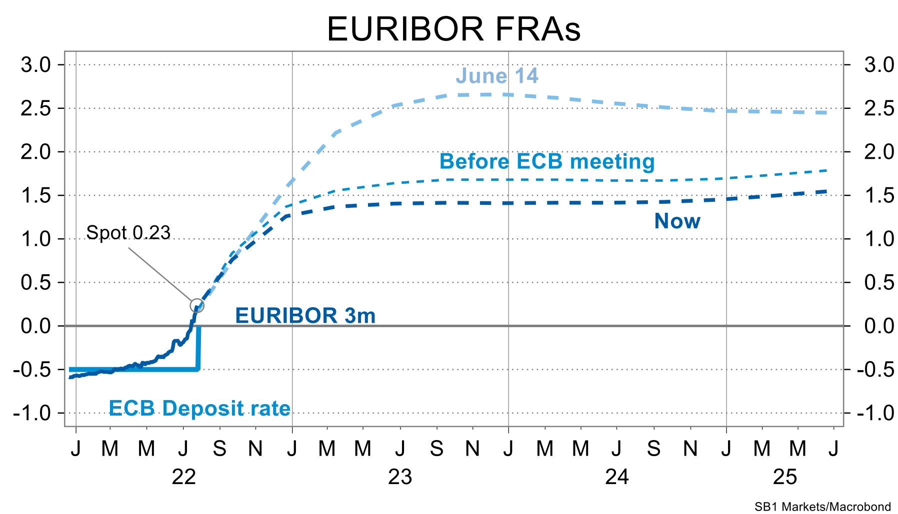


- **In a quarterly model**, the Activity index suggested a 2.3% growth pace in Q2, way above any other forecast – but a slowdown to well below 1% in May and June (and the latter was weaker than expected)
- **In Q1 GDP** fell 1.6%

ECB hiked 50 bps but the outlook is cloudy, no forward guidence given

Rate expectations ended the week sharply down. 'Italy' got a new QE program (if it behaves)





- **The 50 bps hike** was not expected by the majority of economist some days before the meeting but following hints about a 50 bps hike, a 'double hike' was not that surprising, especially not in the market, the 3 m EURIBOR rate rose by just 2 bps. The repo rate was then lifted to zero
- The bank acknowledge that the **economic outlook is clouded** but high inflation was sufficient to lift the signal rate out of the negative territory
- At the same time, the bank did **not give any forward guidance**. Given the bank's own experience, and even more lack of consistency in Federal Reserve's communication and actions, and the uncertainty about the development in the economy, it is reasonable to state the obvious: The ECB is data dependant
- As expected, a new program aimed at keeping bond market spreads in check was introduced. A **Transmission Protection Instrument (TPI)** was established (unanimously, Lagarde stressed)
  - » The formal argument was make sure that ECB's monetary policy works, by preventing that unwarranted, disorderly market dynamics which make monetary policy inefficient.
  - » Several strings were attached but no formal numbers – discretion over rule.
  - » Soon, a test may come: What if Italian spread widens after a new government decides to weaken the budget, and scrap economic reforms? Will the ECB still support the Italian bond market?
- **Short term market rates** rose just after the announcement but then fell back – and during last week especially longer date EURIBOR FRAs have fallen sharply as the growth outlook rapidly deteriorates. From mid June, the assumed peak for EURIBOR rates have fallen to less than 1.5% from 2.5%. Still, more than 100 bps hikes are discounted before the end of 2022
- *Check next page for European bond spreads*

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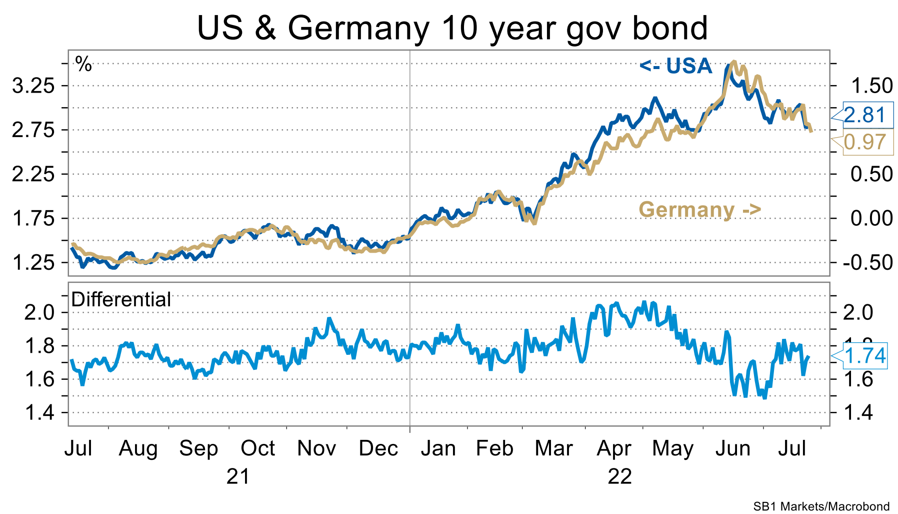
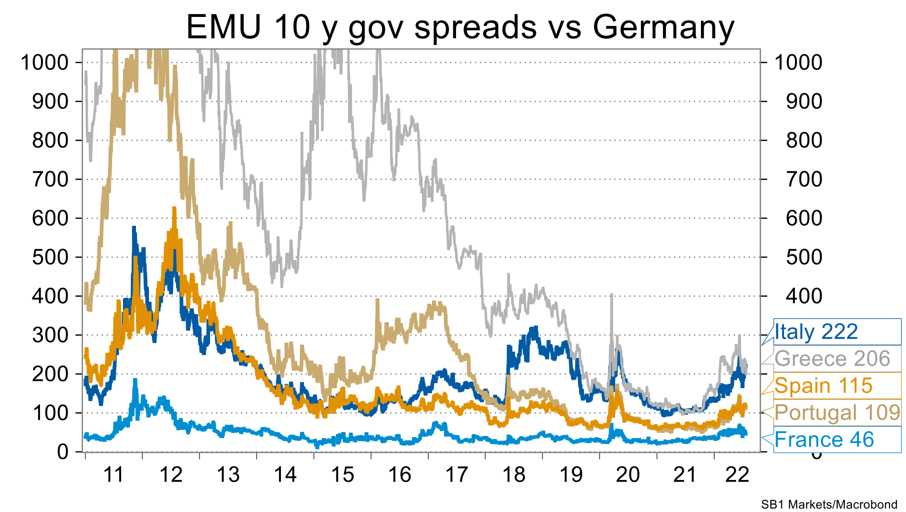
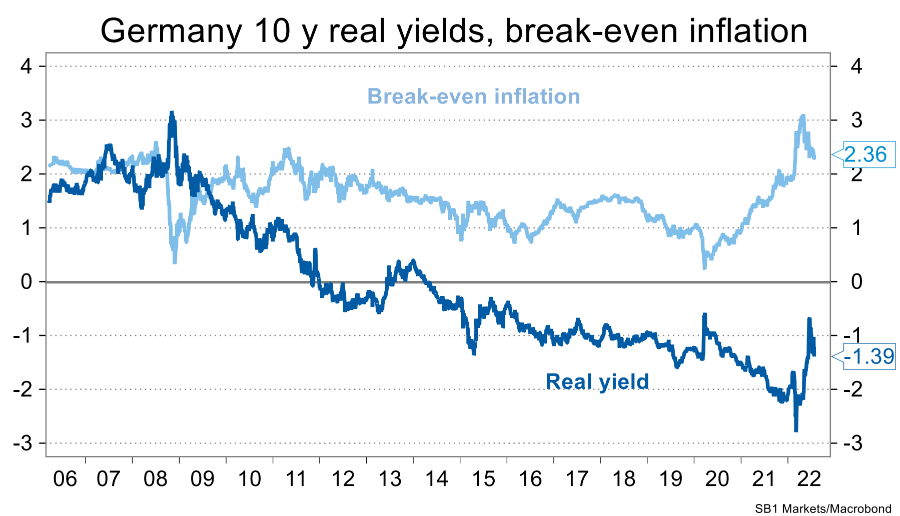
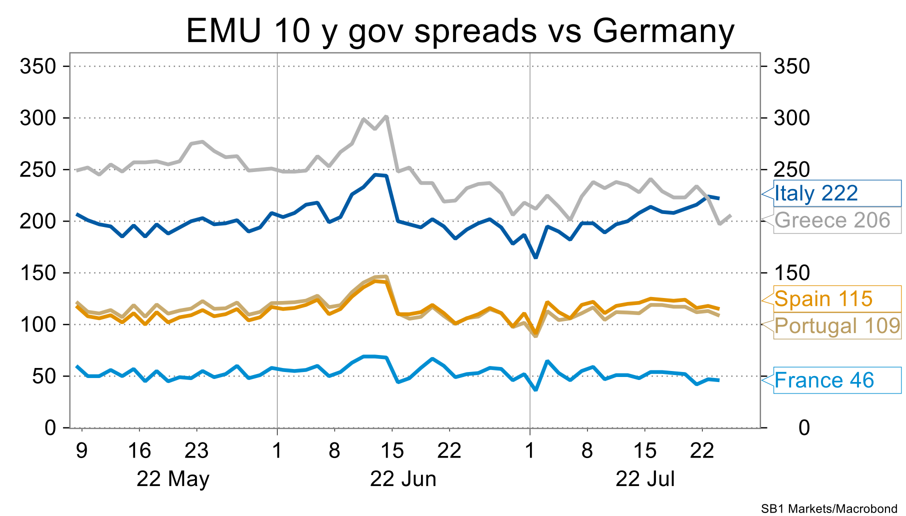
European bond market quite well-behaved, even if spreads have widened

Limited bond market reactions to Draghi's exit. The promise of a new support program was helpful?



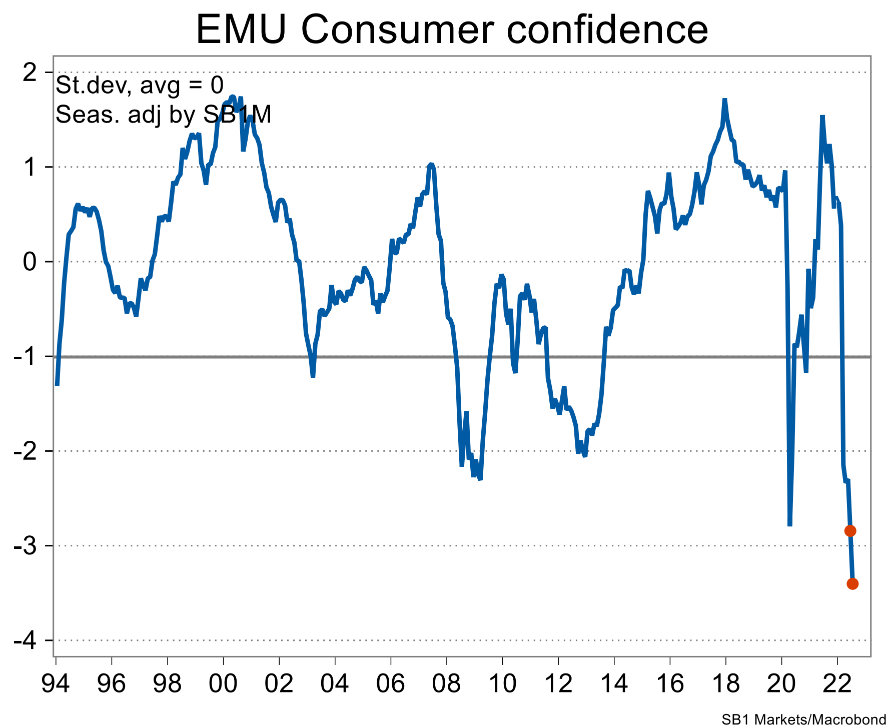


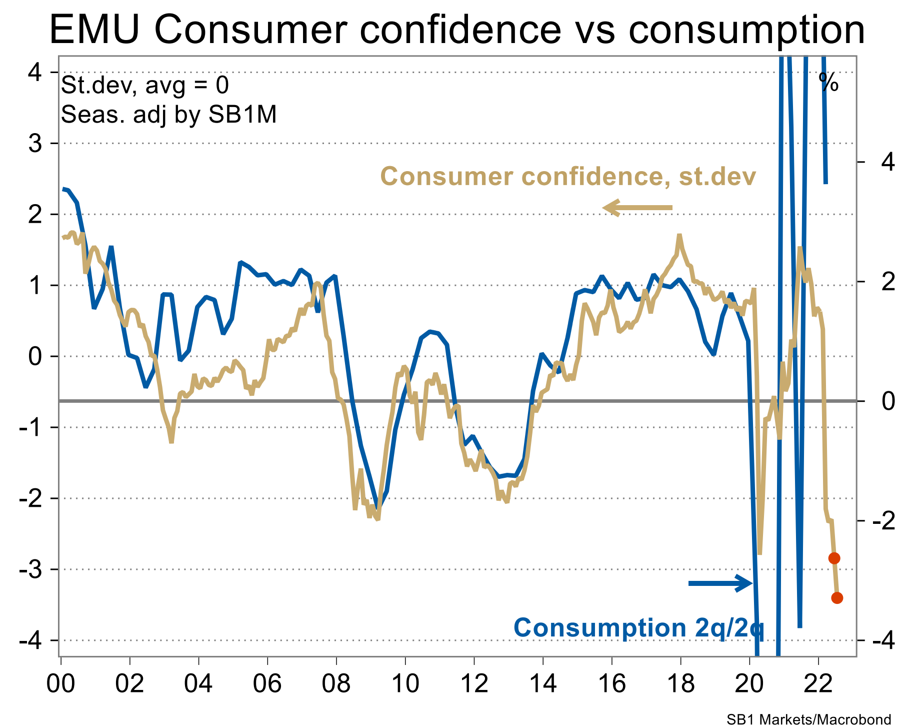




Consumer confidence in uncharted territory, down and way below expectations

Inflation and a war is more important than the lowest unemployment rate since 1980

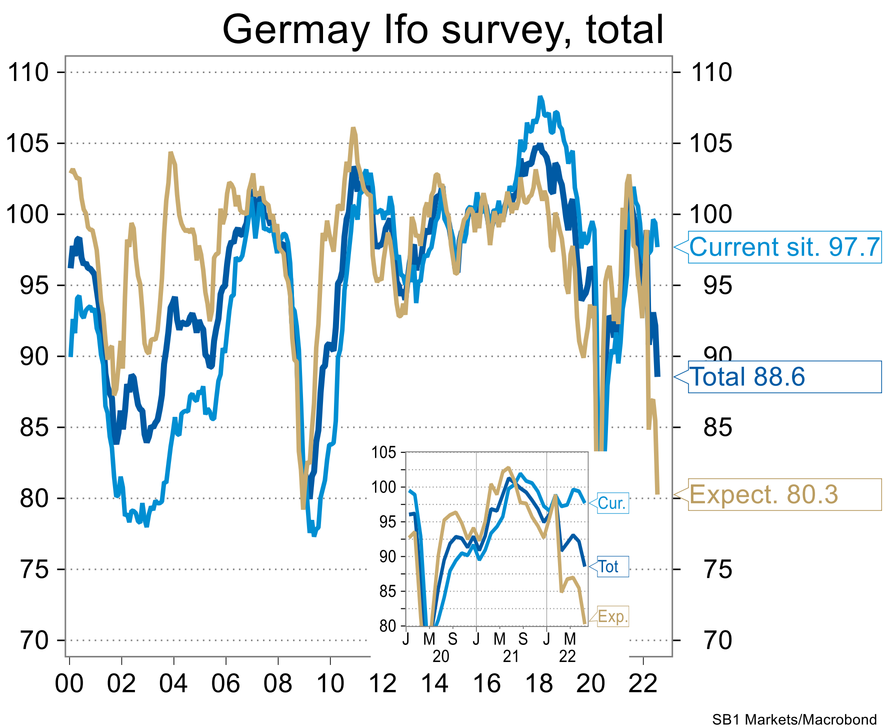


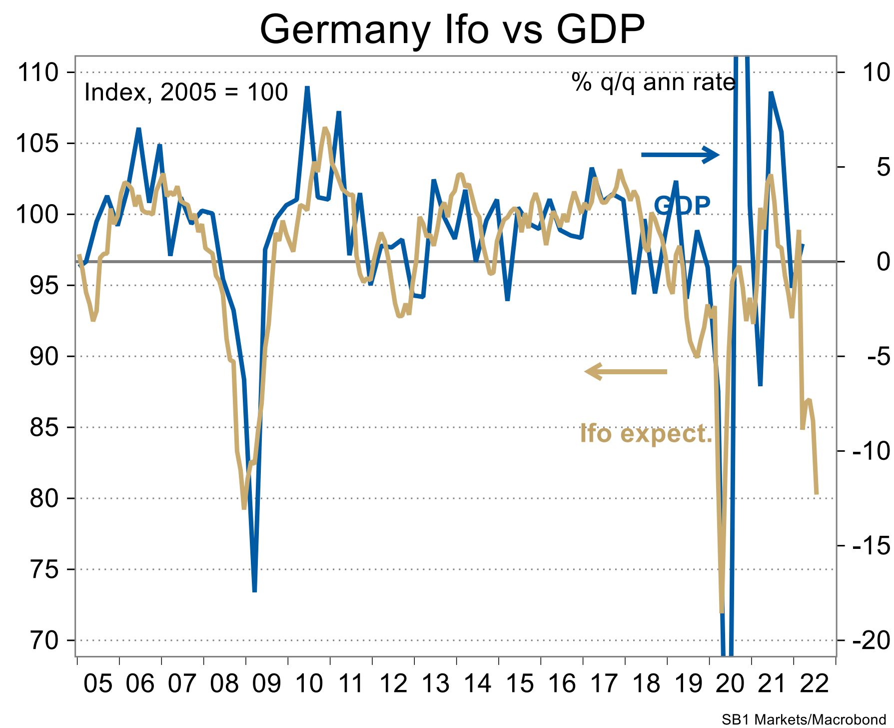


- **The confidence index** fell 3.2 p to -27 in July, expected down to 24.5, according to the preliminary estimate. The decline equals 0.6 st.dev, and the level in June is -3.4 st.dev below avg –a level not seen before, data though back just to 1994…
- **The war** has been around for 5 months, at most likely it does not constitute an even larger negative drag on the sentiment. Thus, **inflation** is probably to blame. **Interest rates** are now being hiked – and the rest of the yield curve has taken big leaps upwards, at least until mid June. Now rate expectations have fallen substantially – and sentiment is plummeting
- Usually, consumer confidence is tightly correlated to growth in household demand. If that's the case now as well…

Ifo expectations further down in July, to a very low level:A deep setback signalled

The index fell by 1 st.dev to -3.2 sd below avg! The current situation just marg. down, at +0.4 st.dev



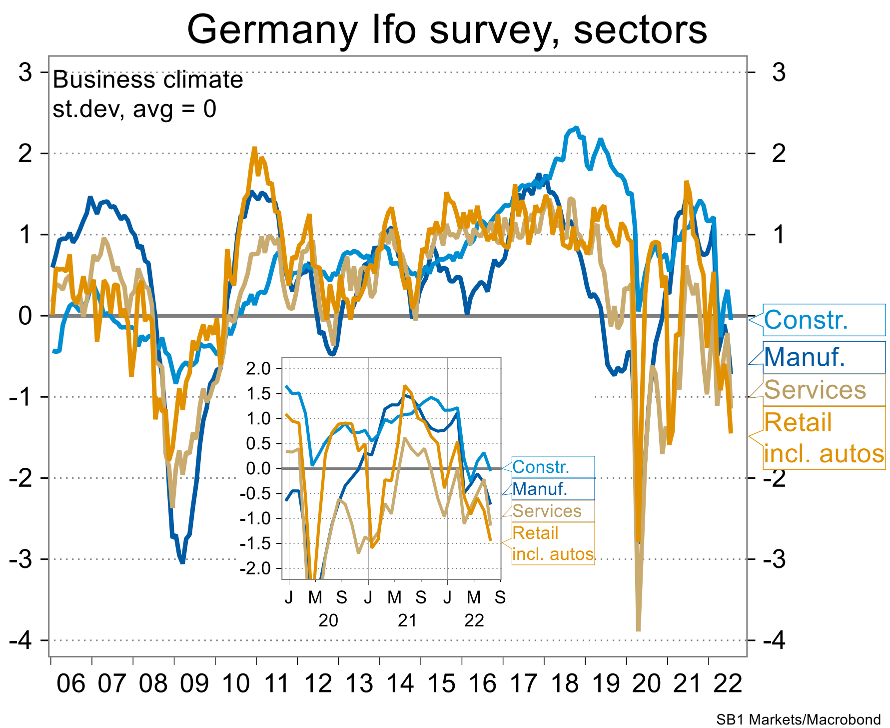


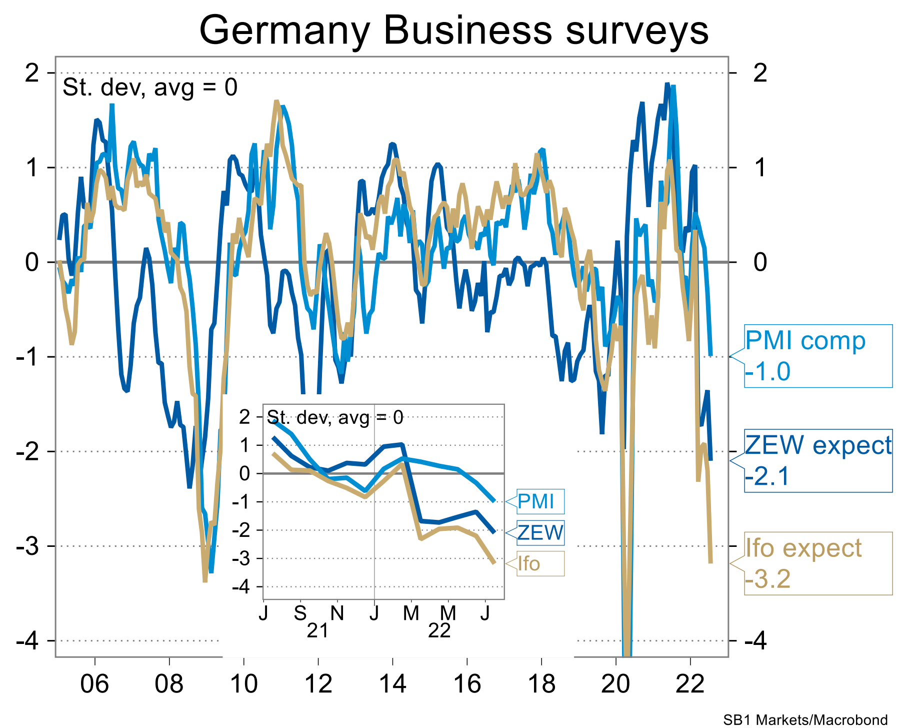
- **The expectation index** fell 5.2 p to 80.2, close to 3 p lower than expected. The level is very low, at -3.2 st.dev below average, almost down to the lowest level during the financial crisis. The correlation to GDP is not perfect but a huge decline in GDP is signalled, at a 10+ pace!
- The **assessment of the current situation** fell 1.7 p to 97.7, in line with expectations. The level is still above average, at 0.6 st.dev
- The total Ifo business climate index fell by 3.6 p to 88.6, well below expectations

Business climate: the average of the current situation and expectations

All sectors reported a weaker business climate in July

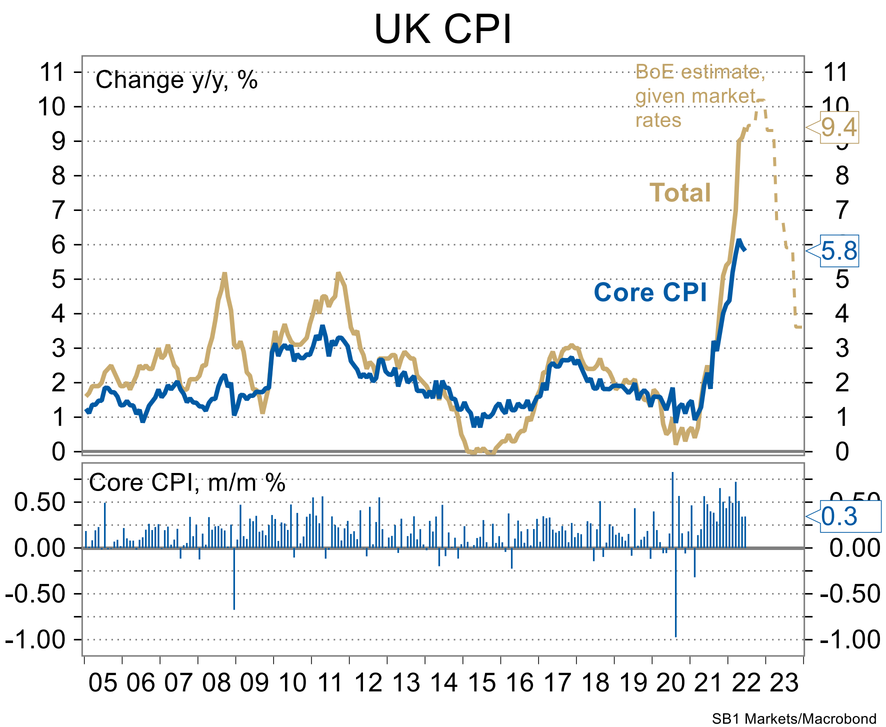
Other surveys have also surprised at the downside in July

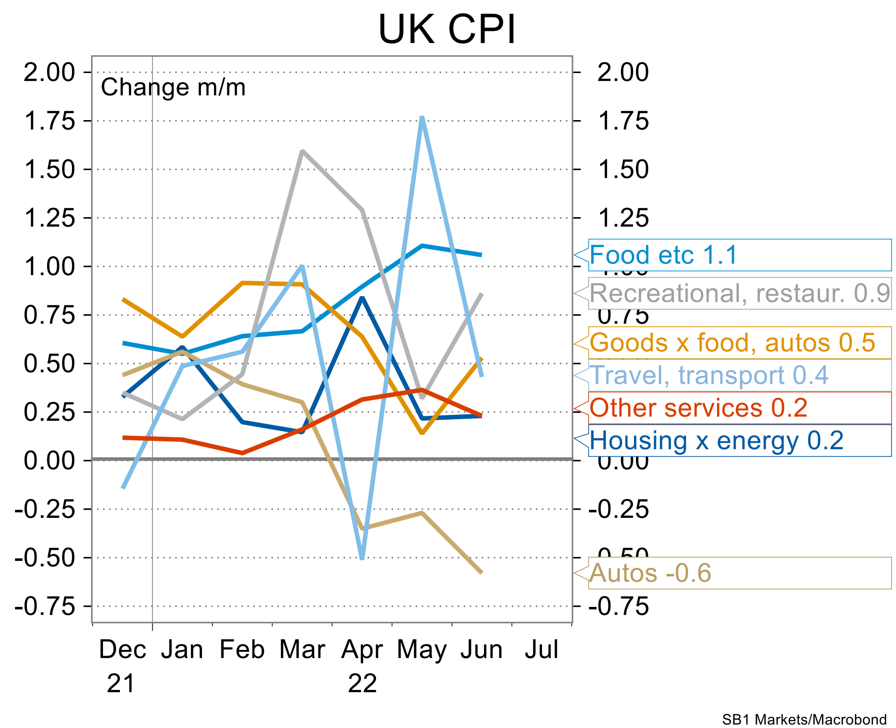




Headline inflation up to 9.4%, the core down 0.1 pp to 5.8%, as expected

Inflation will very likely soon peak but it is still broadening

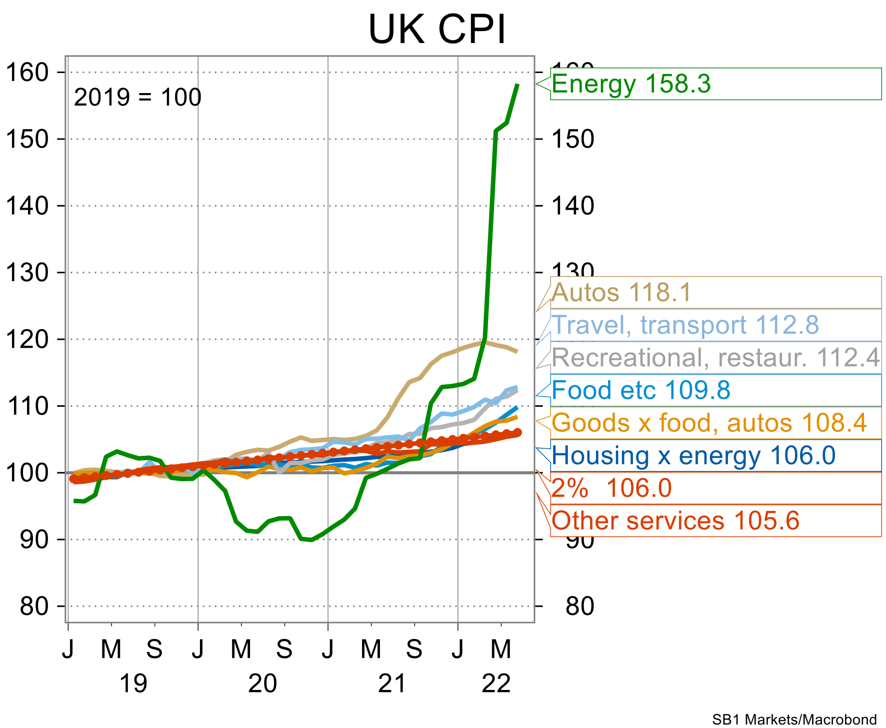


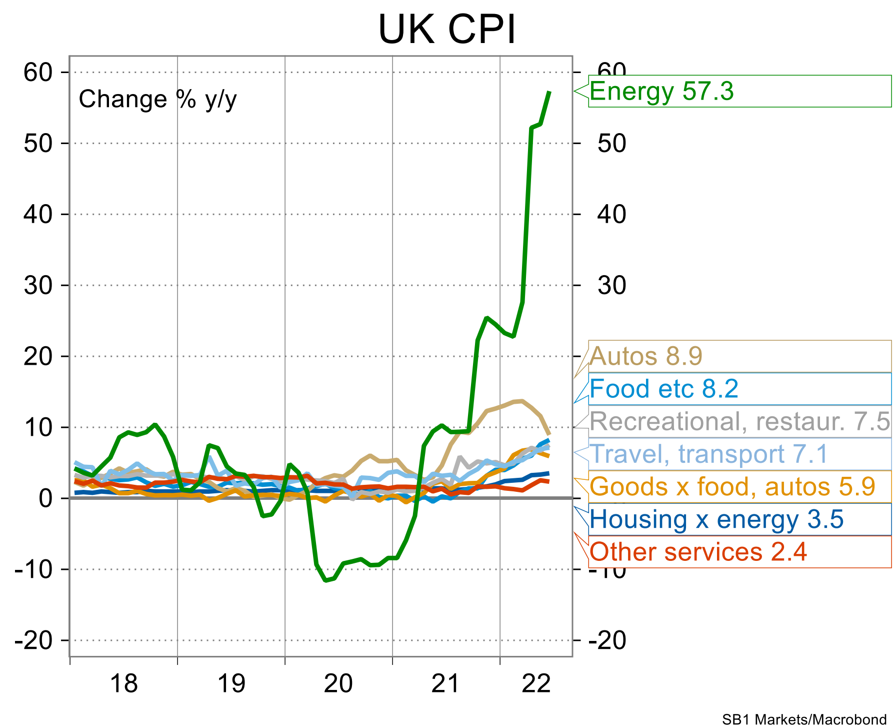


- **The total CPI** rose 0.8% m/m in June. The annual rate rose 0.3 pp to at 9.4% (as expected), the highest since 1982
- **Energy** has lifted the headline y/y rate by 3.8 pp. The regulated price cap for energy was lifted substantially in April (a semi-annual adjustment, the next in October)
- **Food prices** rose 1.1% in June, and they are up 8.2% y/y, lifting the headline by 1.4 pp!
- The **core CPI** (ex food and energy) rose 0.3% m/m, as in May, well below the norm recent months. The core is up 5.8% y/y, down from 5.9%, as expected
- **Auto prices** have fallen the past 3 months, and price increases for goods x autos & food have slowed too (if not in June). However, service prices are on the way up
- **All major sectors** are reporting growth above 2%, and almost all are above a 2% since before the pandemic

Energy is a main culprit

… but most main components are above the 2% growth path





- **Energy prices** are up 57% y/y, much of it due to the 26% m/m surge in April, when semi-annual price cap adjustments were undertaken (the next adjustment is scheduled for October)

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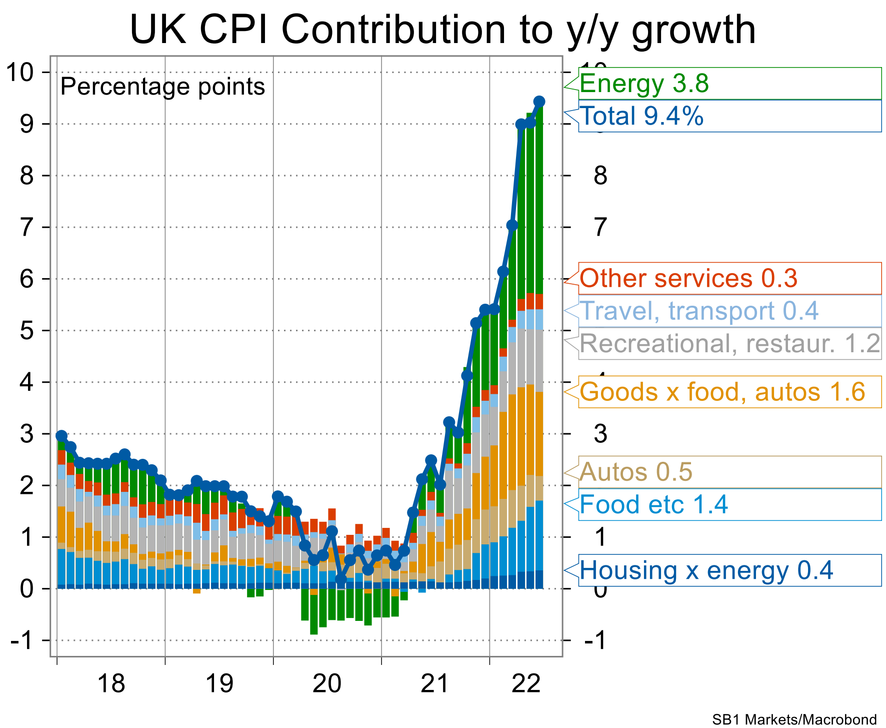
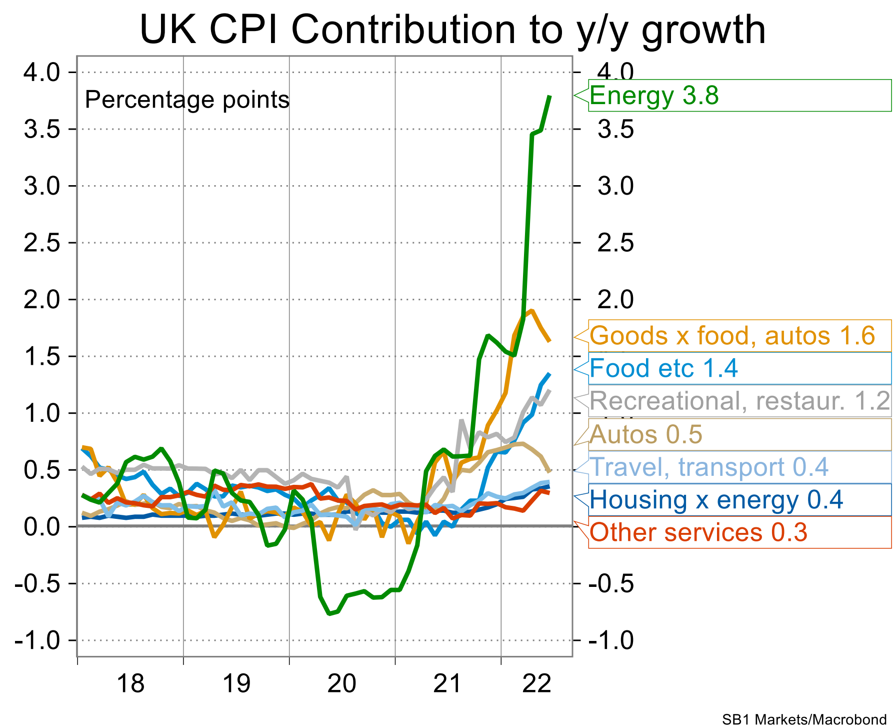
Energy is important, but several components contribute as well

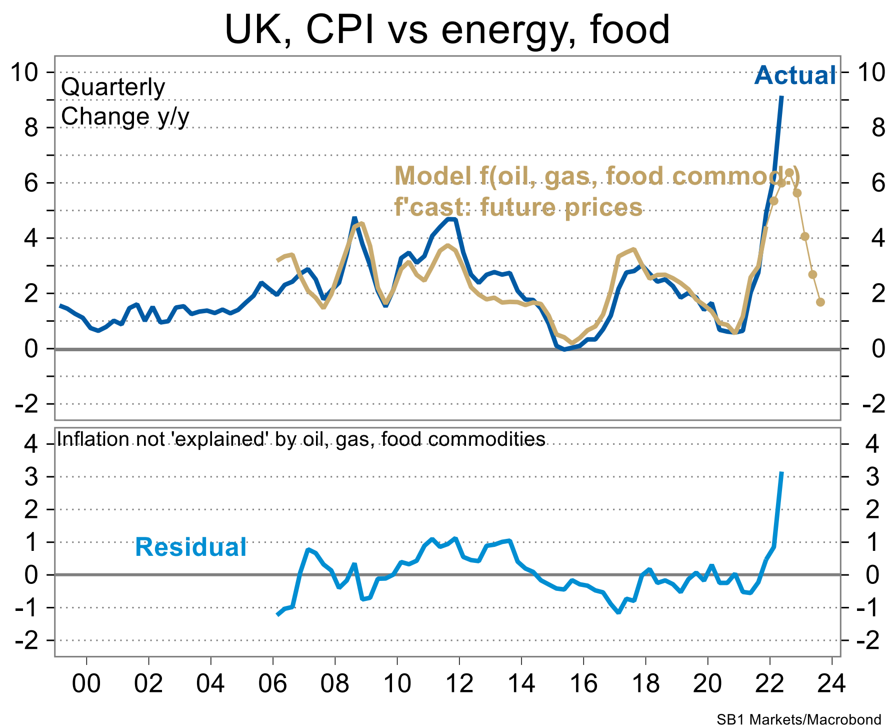
Goods x food & autos prices have shot up, as have recreational services/restaurants, foods, autos

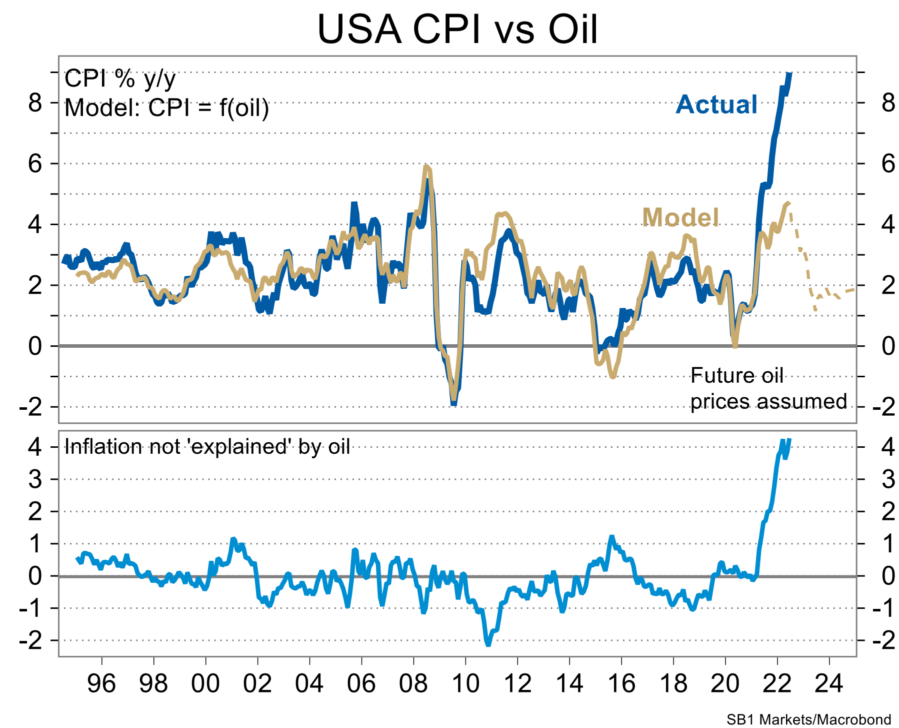




Oil, gas, food prices explain quite a lot but now other factors are contributing too

6 pp of the 9% lift in CPI may be explained by energy & food commodity prices. Still 3 pp left





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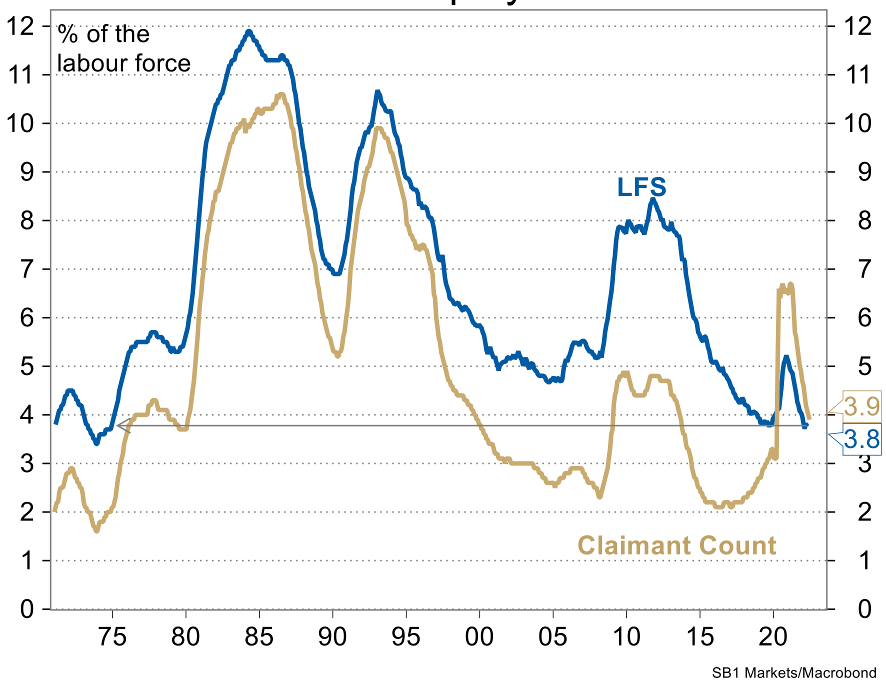
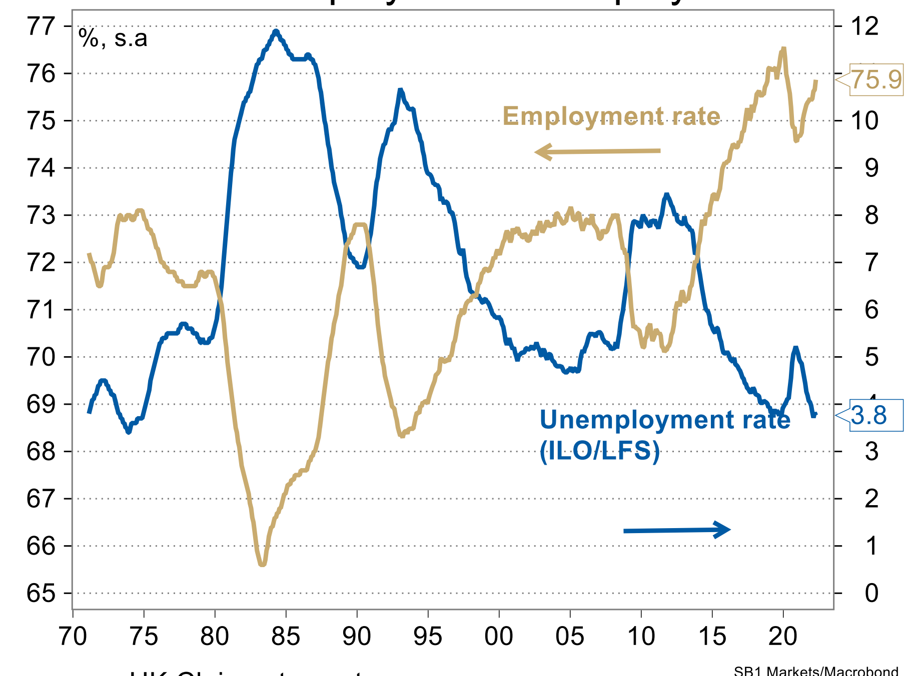
Unemployment flat at 3.8% in May, expected one tick up

The employment rate further up, still below the pre-pandemic ATH level

UK Unemployment

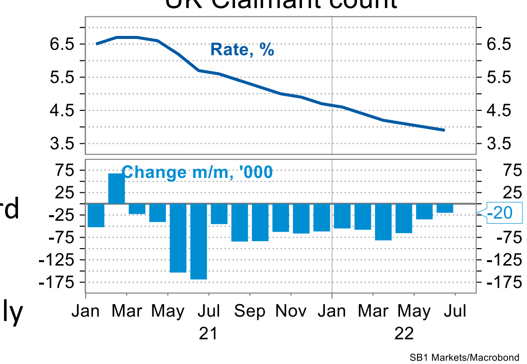


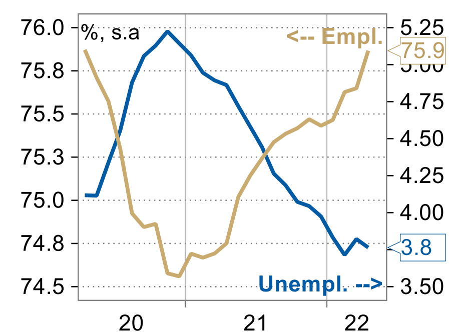
UK Unemployment & Employment



- ILO/LFS ('AKU') unemployment is at the lowest level since 1975
- The employment rose further in May
- The claimant count at labour market offices fell by 20' in June, expected -40', and less than the normal decline recently. However, the count fell, and the rate declined 0.1 pp to 3.9%. Given the record high level of vacancies, the claimant count 'should' have fallen further. More mismatch in the labour market?
- The no. of unfilled vacancies is record high and still increasing rapidly

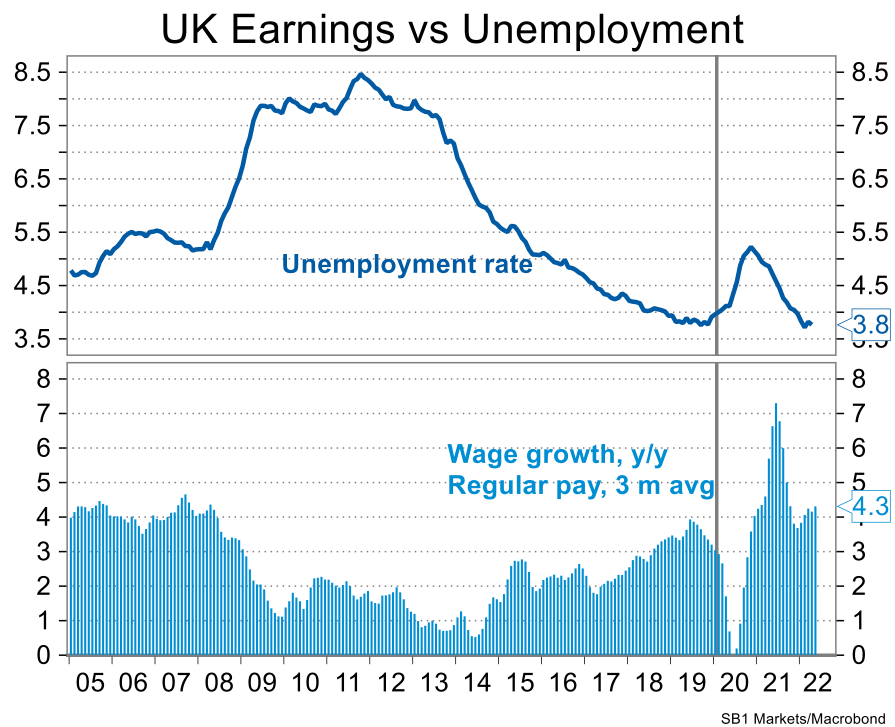
UK Claimant count

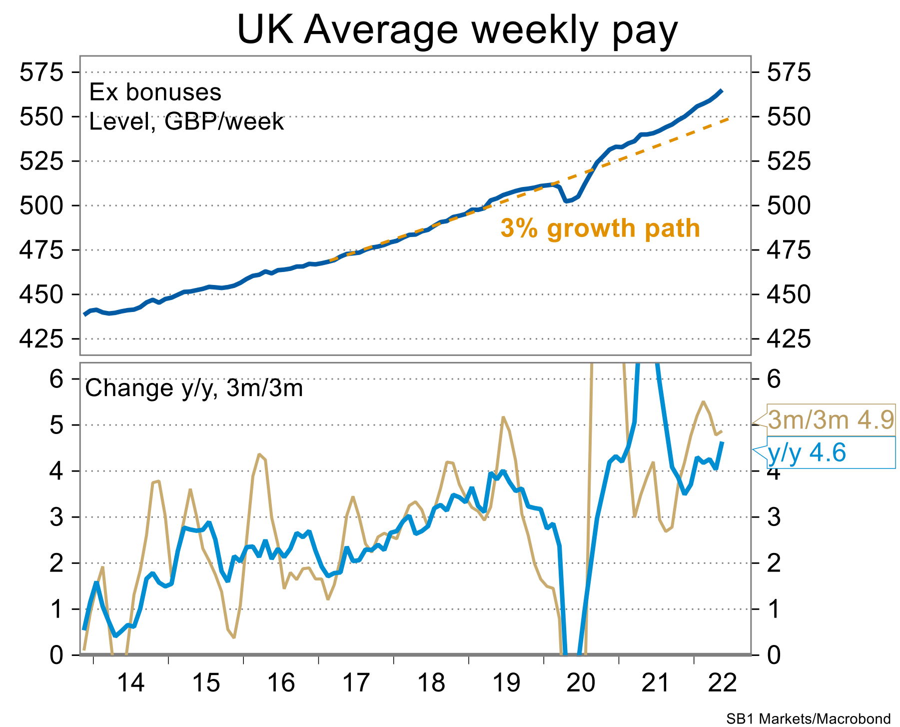




Unemployment has fallen to a low level – and wage inflation on the way up

… wages ex. bonuses up 4.3% 3m/3m, up from the pre-pandemic level at 2 – 3½%





- **Annual wage growth** (regular pay, 3 m avg) accelerated 0.1 pp to 4.4% in May, as expected. Not smoothed, wages were up 4.6%, the highest since . The underlying 3m/3m rate retreated marginally to 4.8%
- **Including bonuses**, total wages are up 6.3% y/y (3 m avg), but the annual rate in May fell to just 3.9% as wages have more or less flattened recent months
- Just before the pandemic, wage inflation was approx. 3% (total pay) to 4% (regular pay) – but just between 2% and 3% the preceding years. Thus, the current wage inflation rates are well above the British 'norm'
- Some unions in the UK have lifted their ambitions substantially recent months – as inflation is approaching 10% - and BoE expect more to come. Wage claims in the same territory have now been aired, not surprisingly in a very tight labour market

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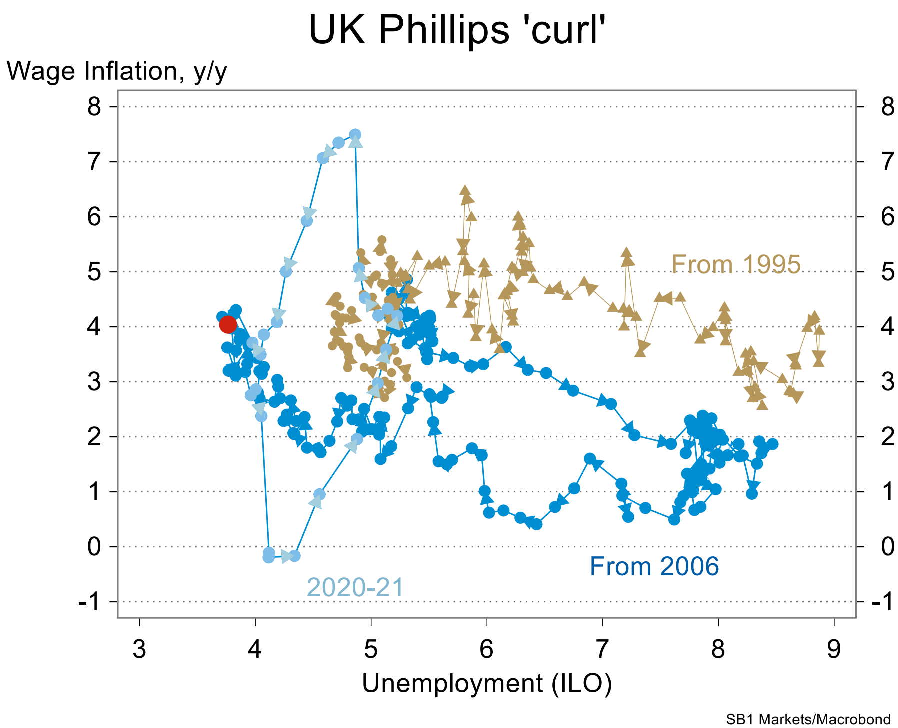
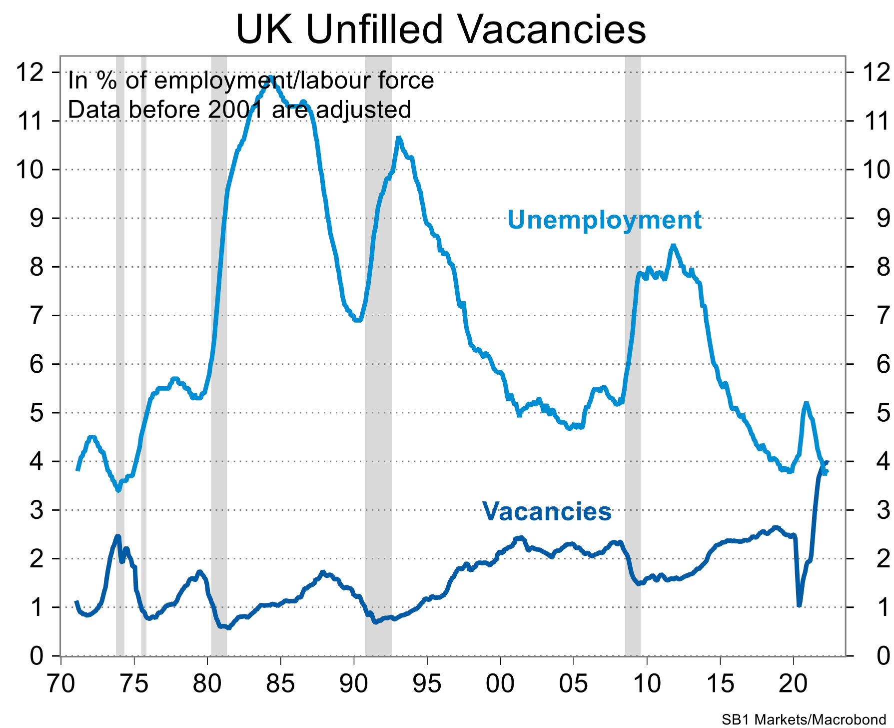
A tight labour market – perhaps the tightest ever due to the vacancy rate

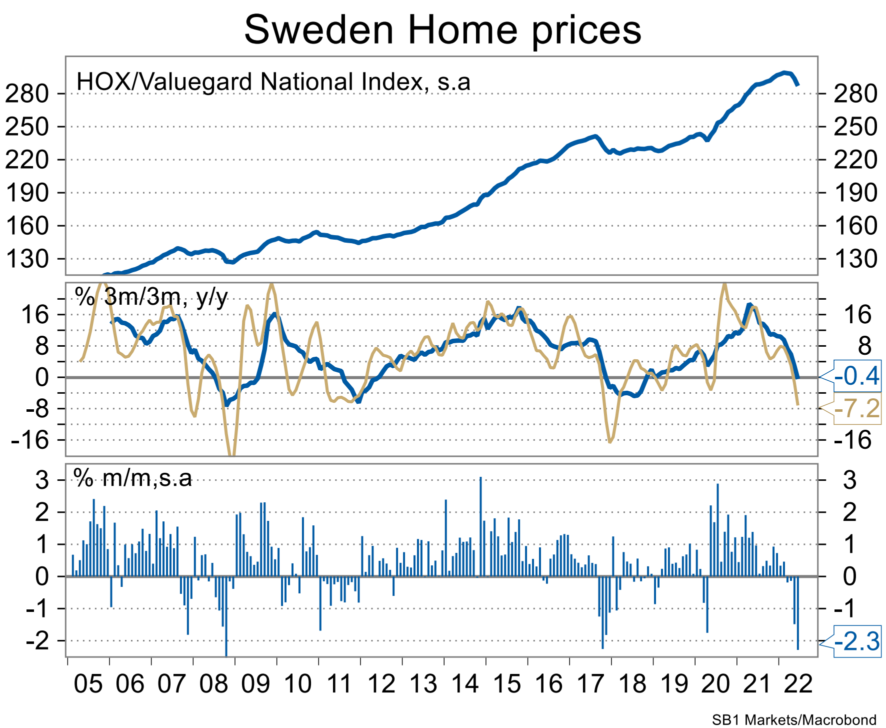
And wages are on the way up alongside something that looks like a Phillips curve

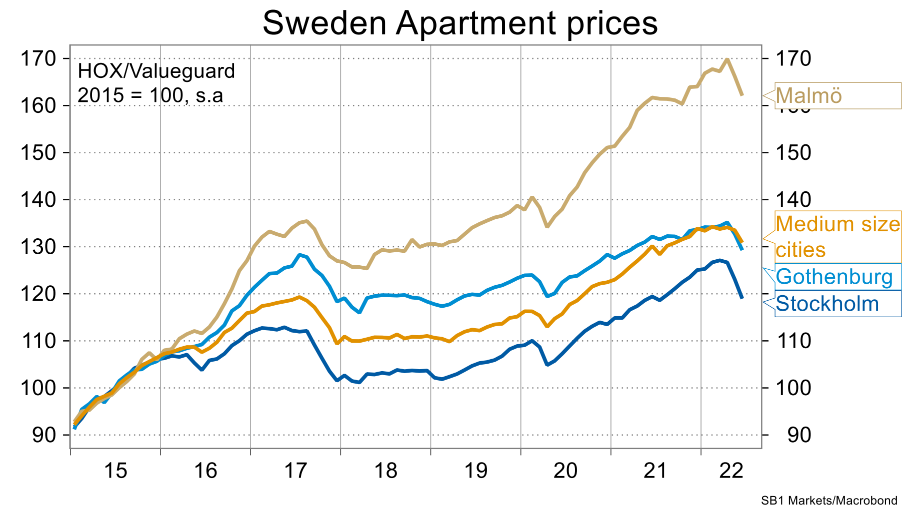


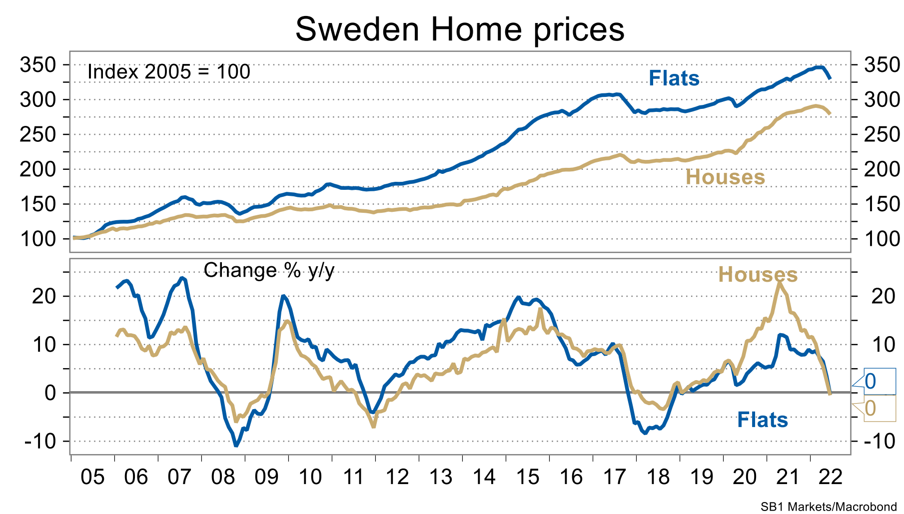


Look to Sweden: House prices are falling rather rapidly

Prices fell 2.3% in June, the 4th decline in row, prices are down y/y. Stockholm in the lead



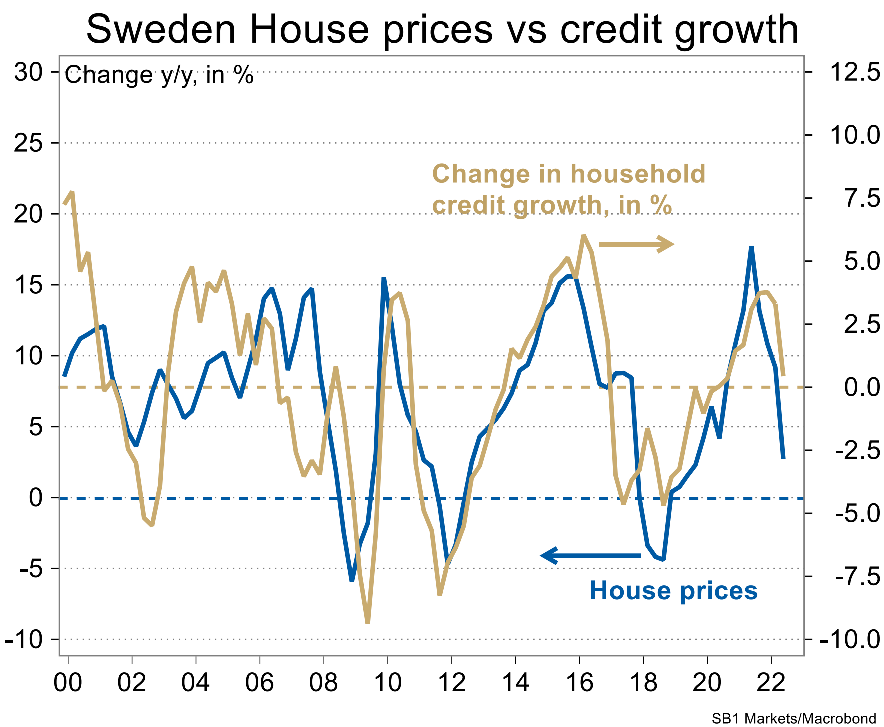


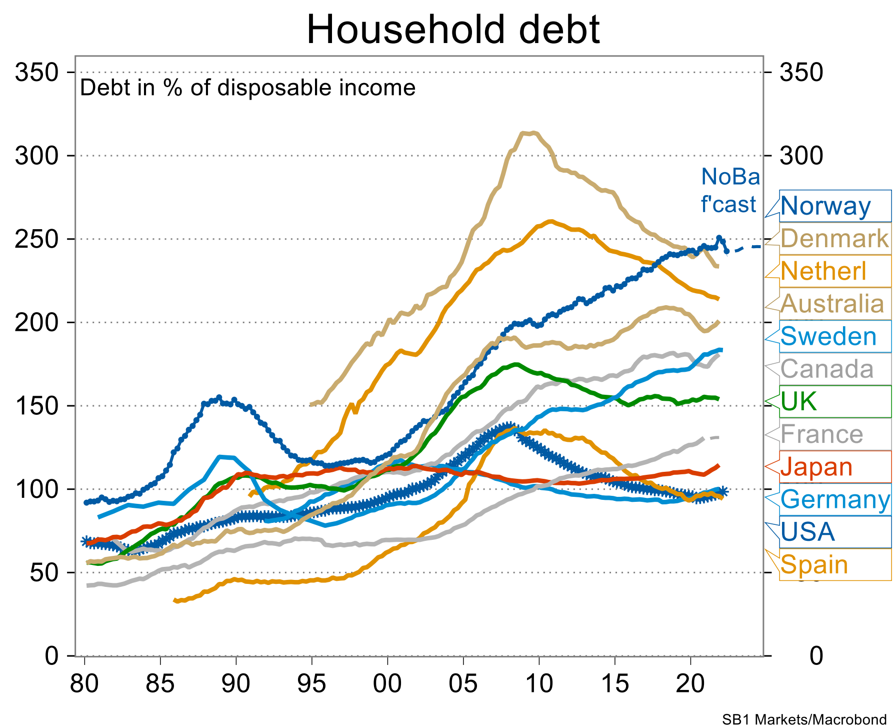


- **Prices are down** 4% from the peak in February. In Stockholm, apartment prices are down 6.4% from the peak
  - In June prices in Stockholm fell by 3.3% (4.5% not seas. Adj
  - Prices are down in all the major cities as well
- **The annual rate** declined to 2.9% from 6.2% in April
  - The underlying price growth (3m/3m) suddenly turned <u>negative</u>
- The **Riksbank's** abrupt change of tack in late April has no doubt hit the housing market hard, as the bulk of the decrease in prices so far took place in May and June

Credit growth is slowing too, as always when the housing market calms down

And more slowing is in the cards as house prices very likely will decline further





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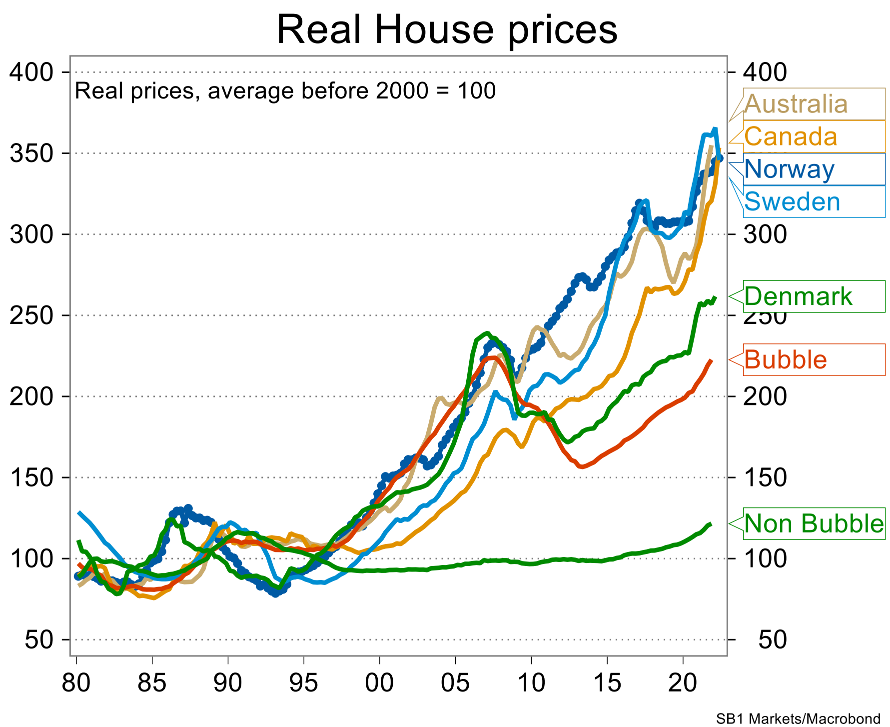
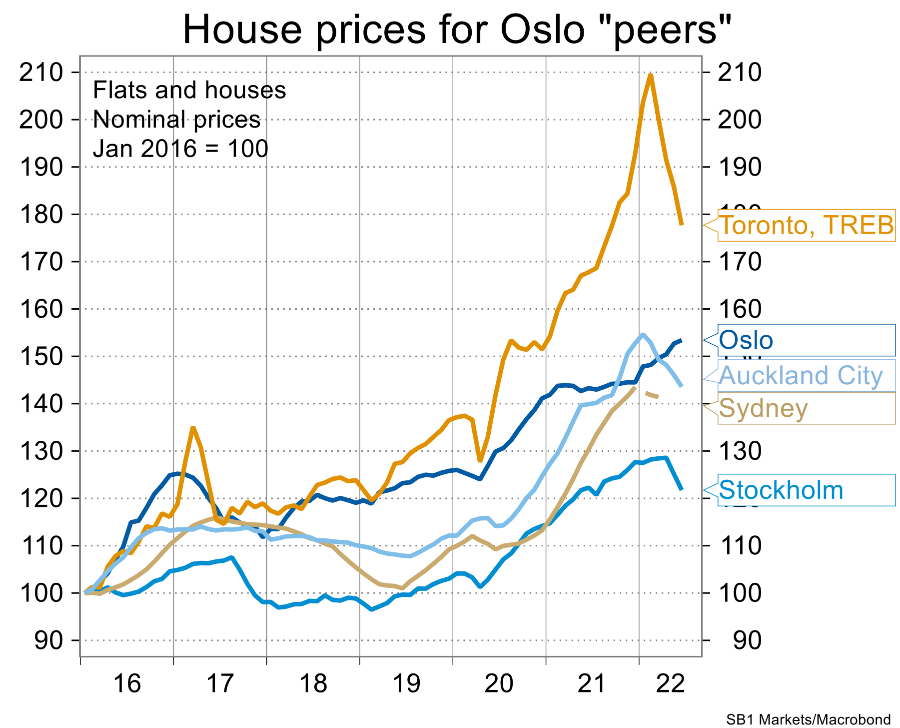
Just Oslo on the way up; Toronto, Sydney, Auckland & Stockholm have peaked

Very likely, Oslo will soon follow suit





- Real house prices are at high levels in both Australia, Canada, Norway, and Sweden
- Now, the capital cities may signal a change is underway. Except for Oslo, of course, where prices never can decline.

Highlights

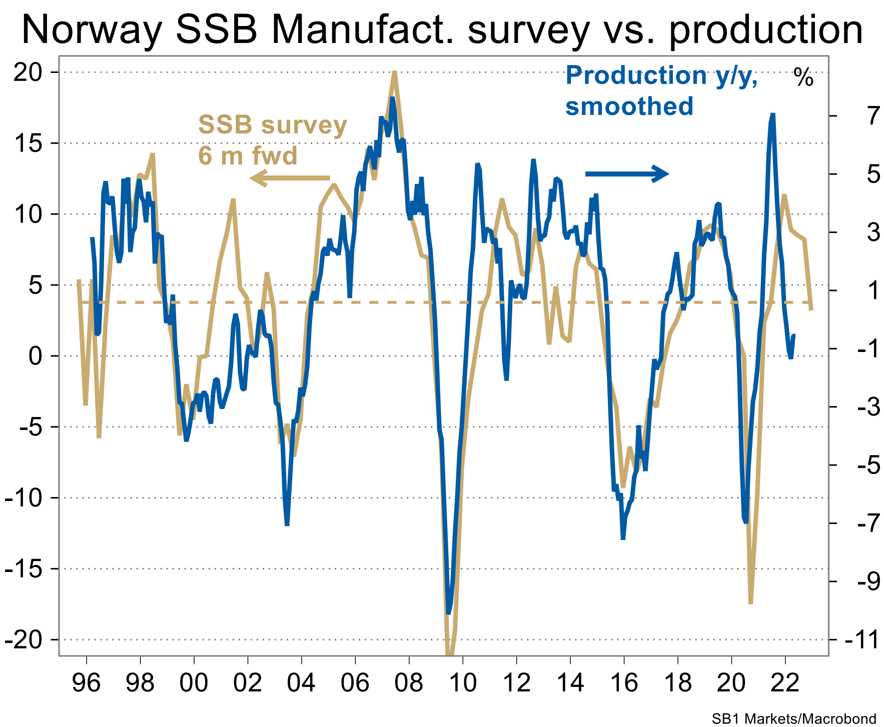
The world around us

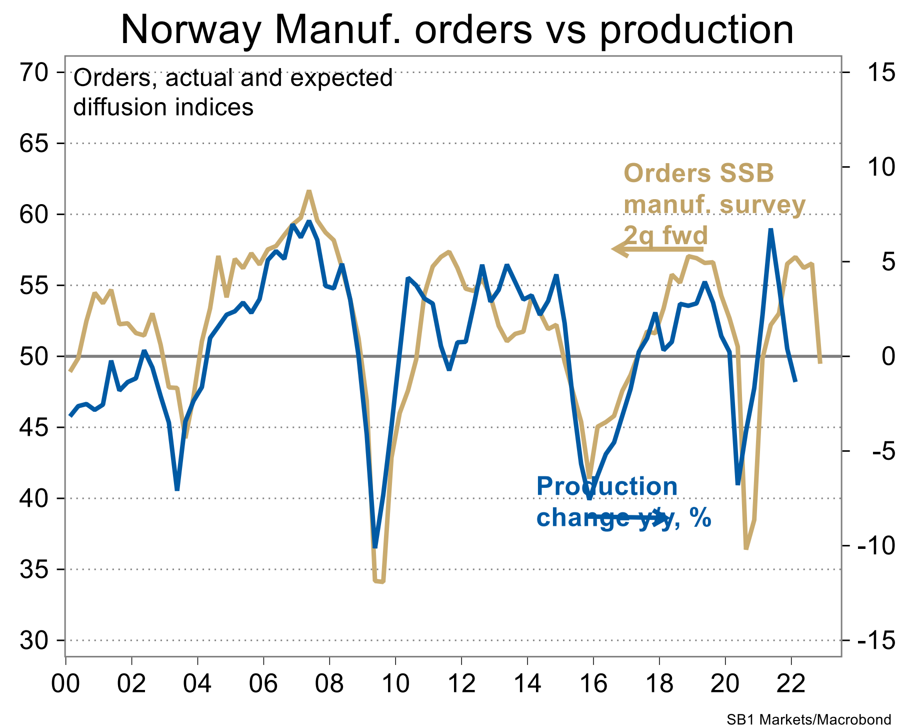
The Norwegian economy

Market charts & comments

SSB's manufacturing survey down to below average in Q2

The oil sector report continued growth, others do not – <u>the tide has turned</u>

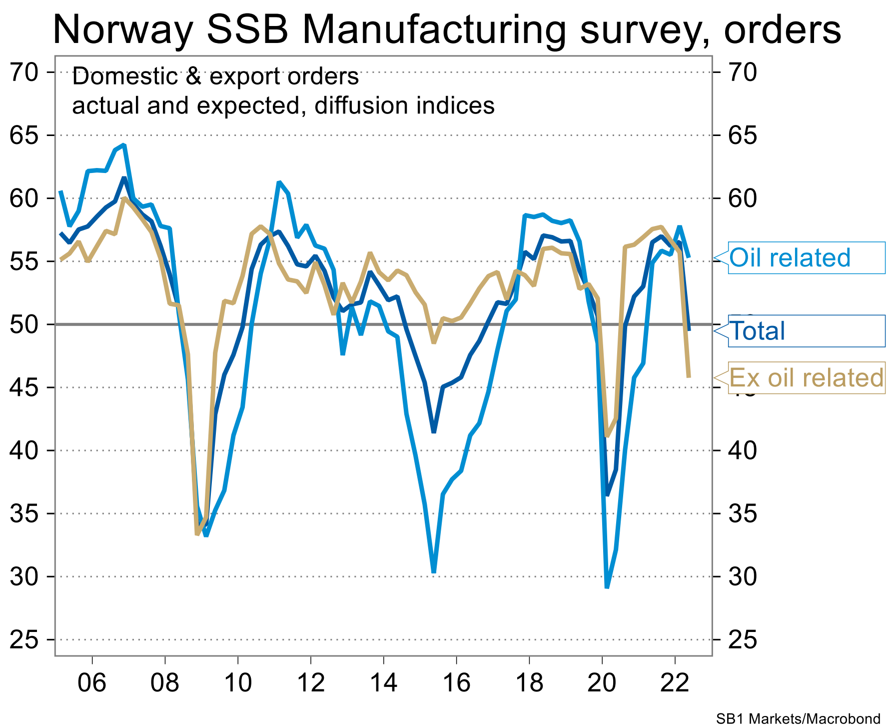


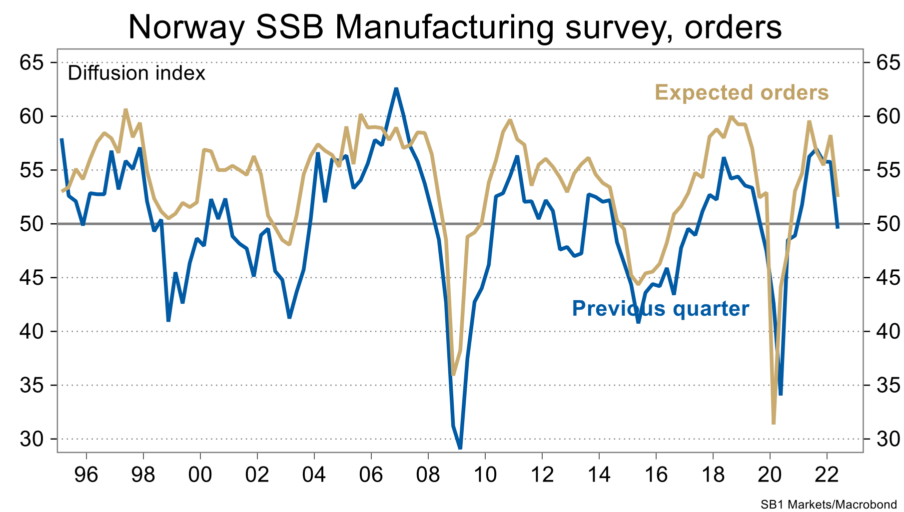


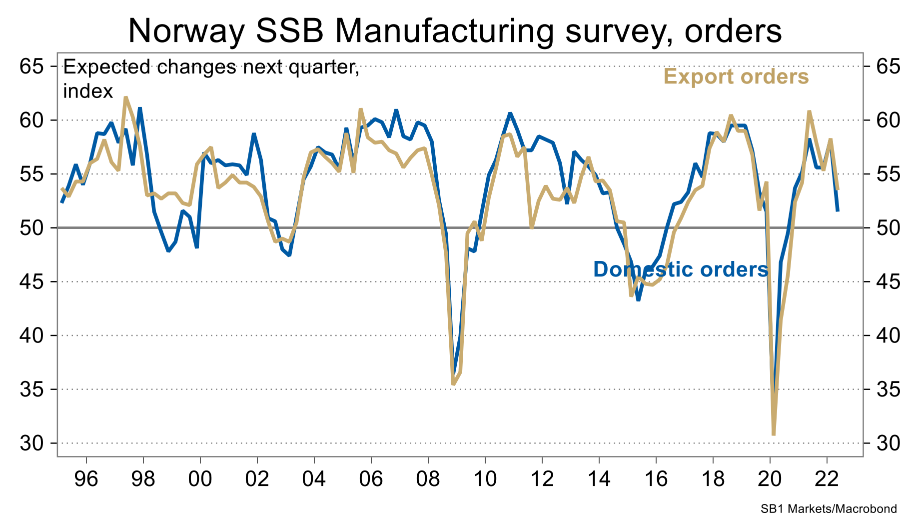
- The **composite index ('confidence')** in SSB's manufacturing survey fell to 3.2 p in Q2, which is marginally below and average level. We expected a decline to 4 (no consensus). Oil related sectors report a still strong outlook (like order expectations), other sectors fell to well below average
  - » The index signals trend growth, somewhat less than 3% GDP growth and – together with the oil price, a impressive 62% growth in 12 m forward expected corporate (OSEBX) earnings, though below analyst's current 89% growth estimate
- **Supply constraints** eased marginally (not for labour), but are still the most serious since 2008. **Demand/competition** is far less of a problem than normal
- Fewer companies reported they plan to lift prices – but the share is still was off anything seen before (barring the recent quarters)

Oil related manufacturers kept the pace up, other sectors not

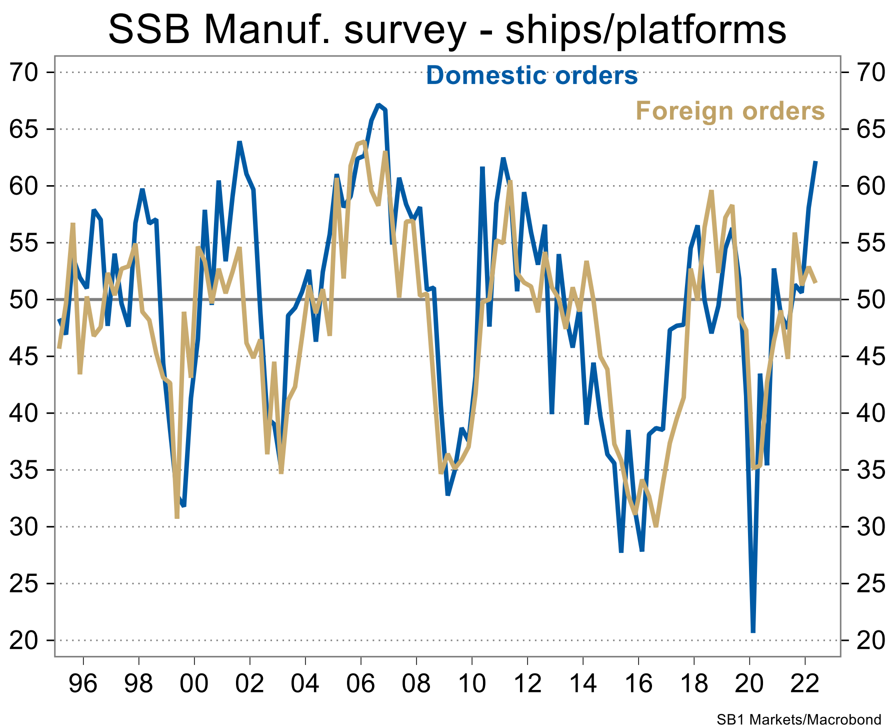
Both domestic & export orders are slowing sharply, in sum





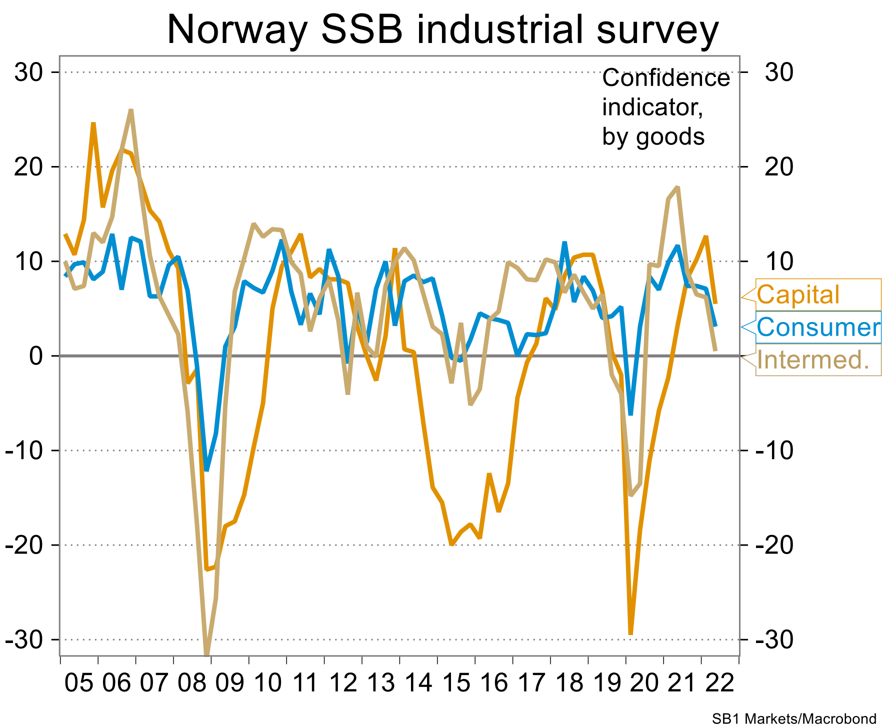


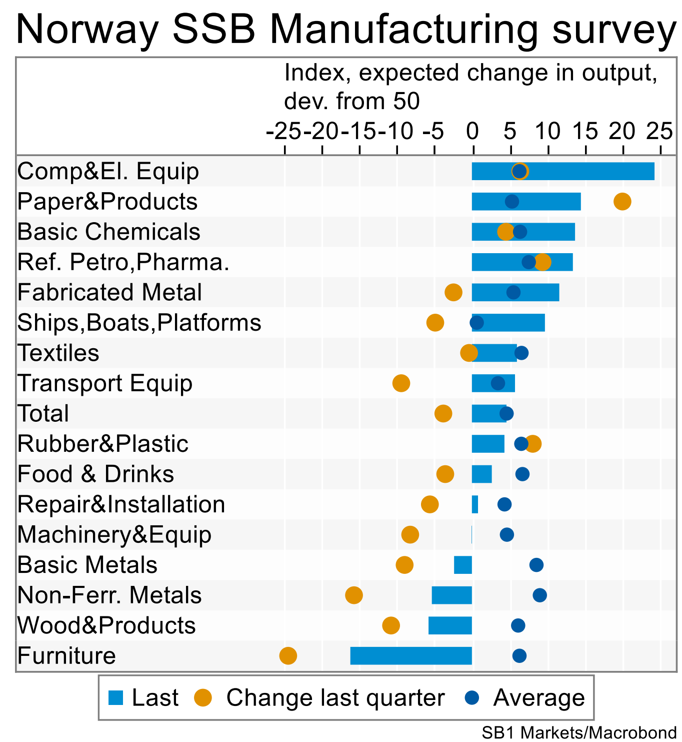
Ships/platforms: Order inflow on the way up (domestically, that is)



A majority of sectors report slower growth, and growth below trend in Q2

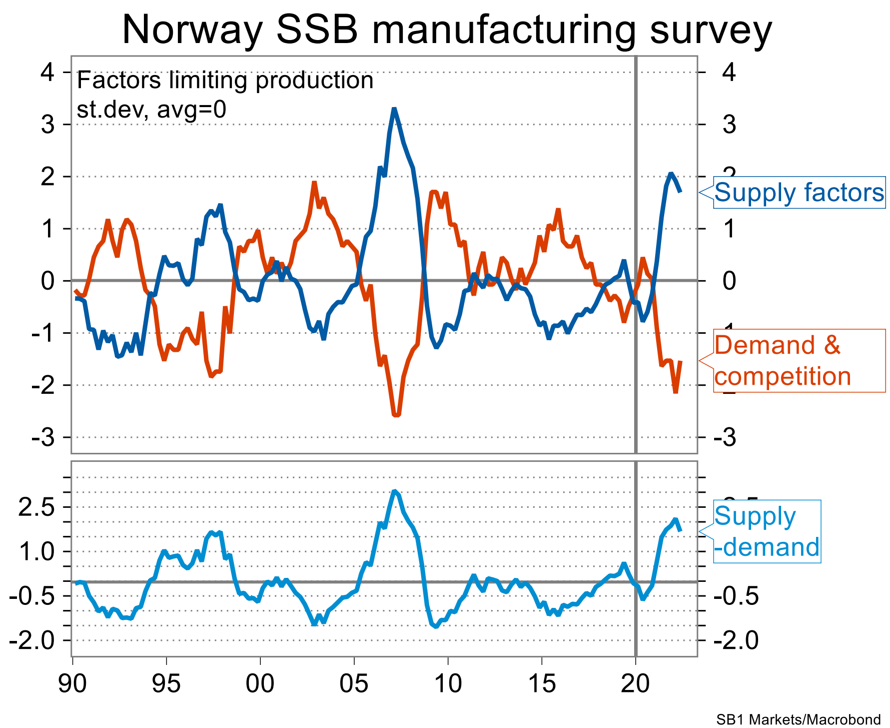
Metals, wood products, furniture at the bottom; Computers, paper, chemicals at the top of the list

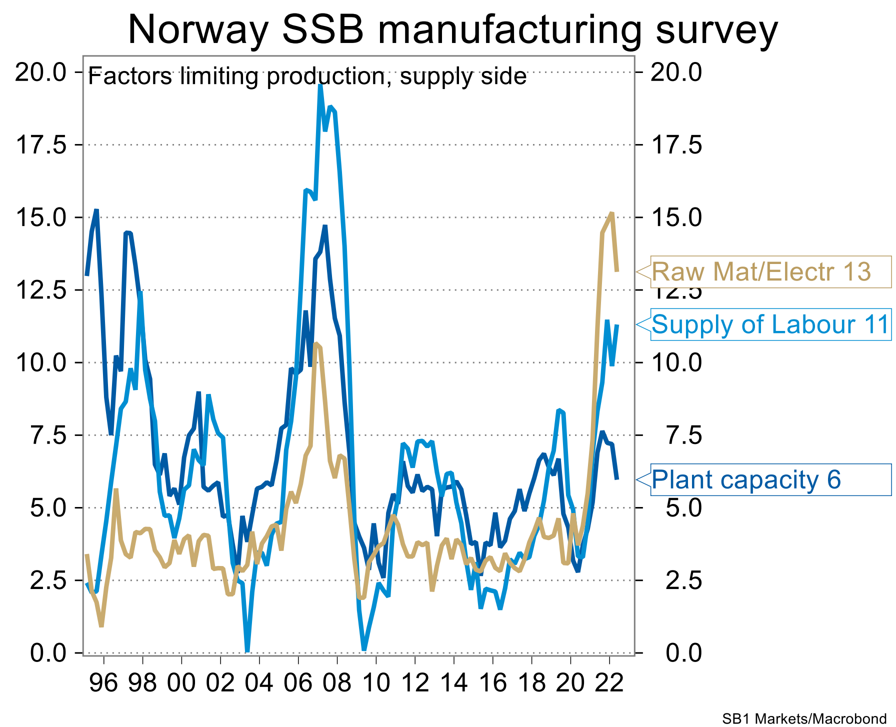




Limiting production: Supply factors far above average, demand far below

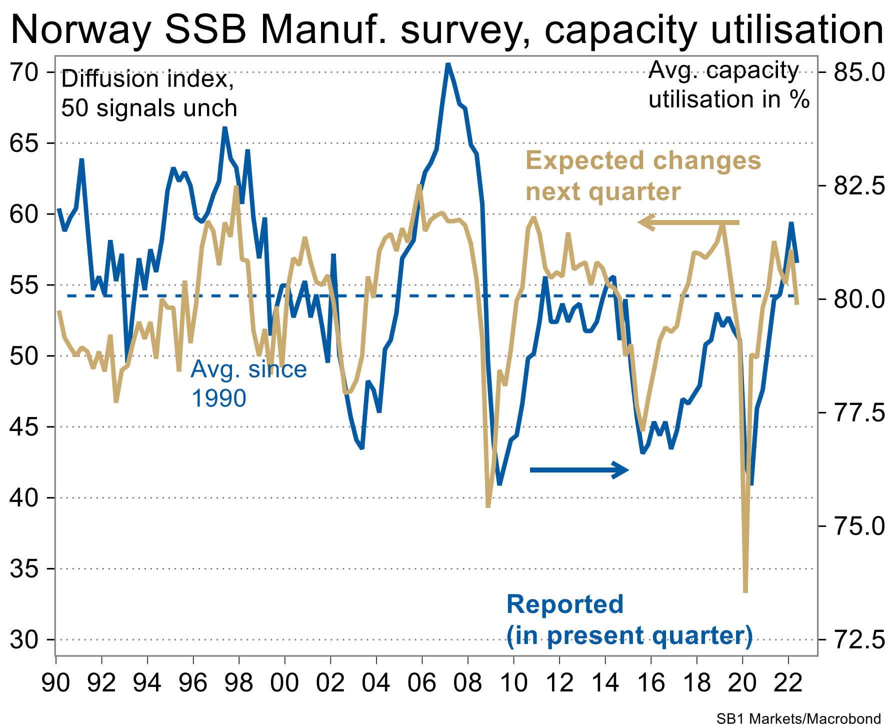
However, in Q2 the gap between the two narrowed somewhat

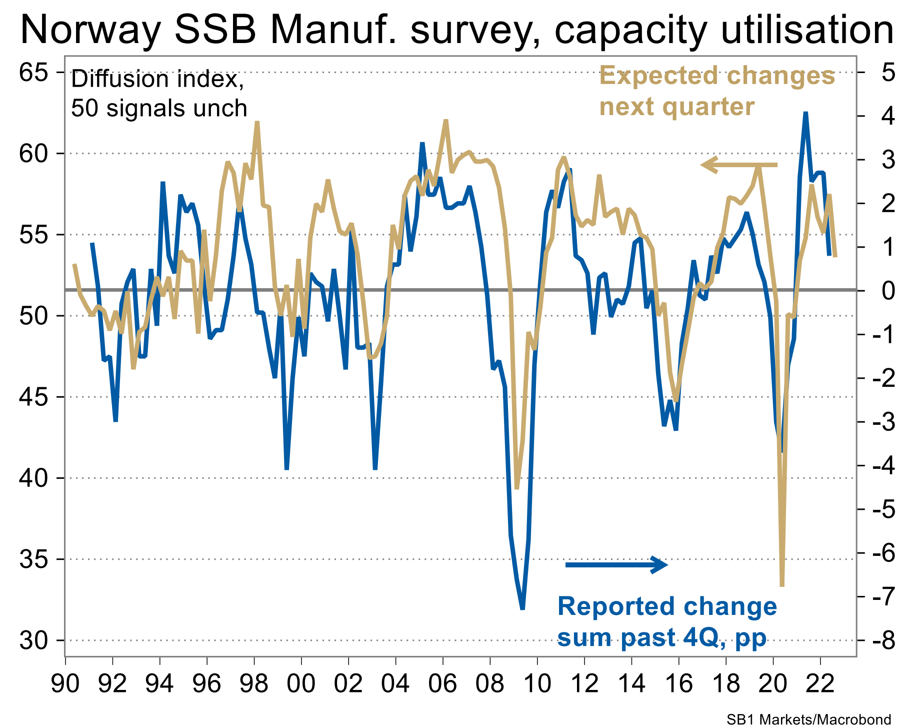




- Fewer companies reported supply side factors as limiting production, except for labour
  - » Raw materials/electricity is still the most important constraints, but problems eased a little in Q2. Plant capacity also were reported less of a problem
- More companies reported lack of demand or competition as limiting factors, but the share is still unusually low
- ***No demand crisis – and it never was during the pandemic***

Reported capacity utilisation down – and is expected further down

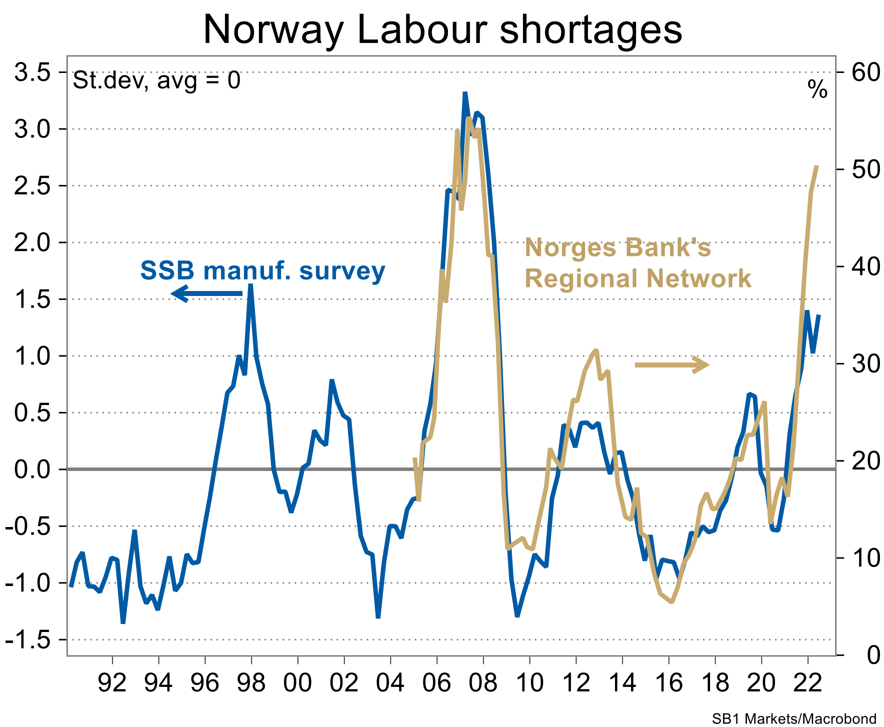


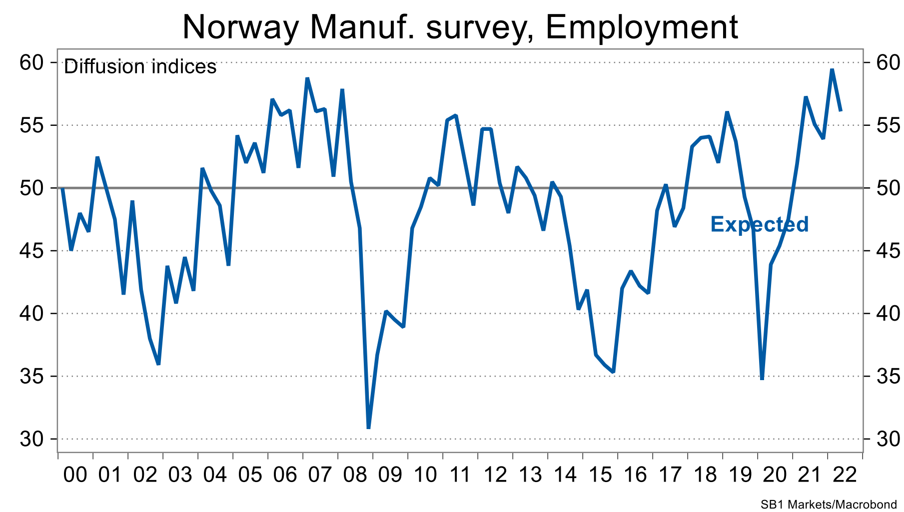


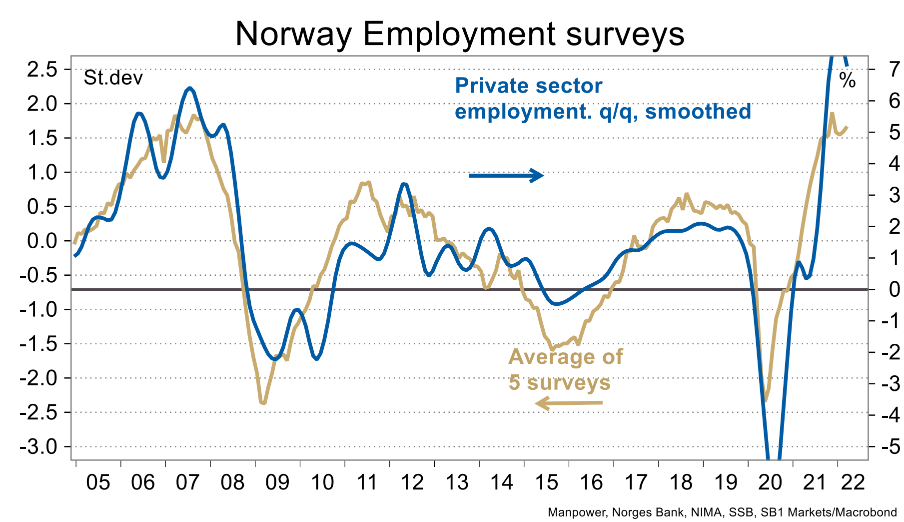
- The lift in capacity utilisation recent quarters has been impressive – from a low level early in the pandemic

Labour shortages still widespread, though not as in 2006-08

Manufacturers and other sectors reports very aggressive hiring plans

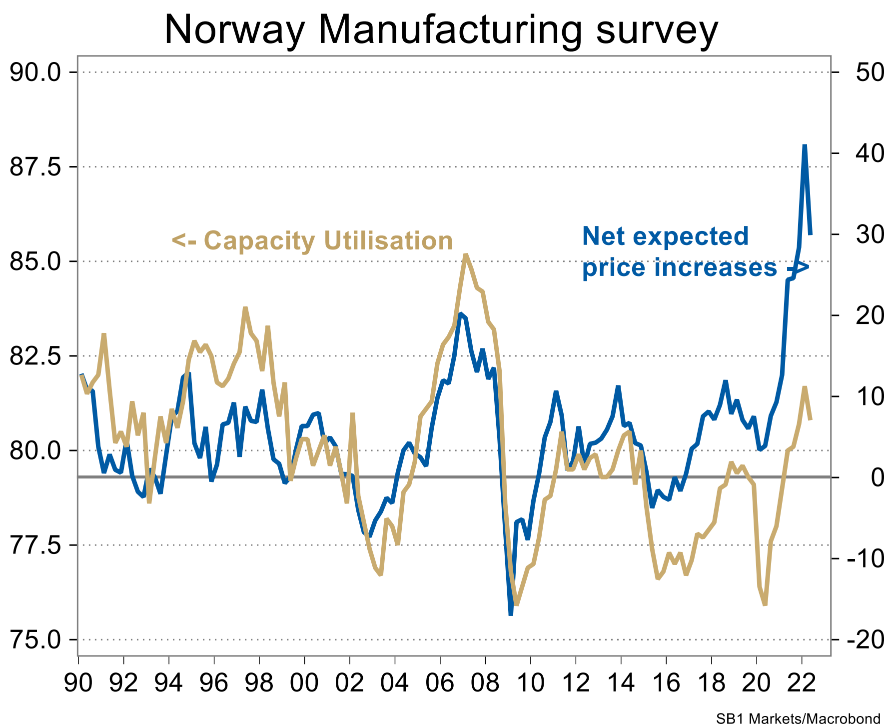






- Employment surveys are signalling a substantial acceleration of employment growth – which is not possible at unemployment rate is close to record low, and immigration from abroad at a huge scale is not likely, there are labour shortages everywhere

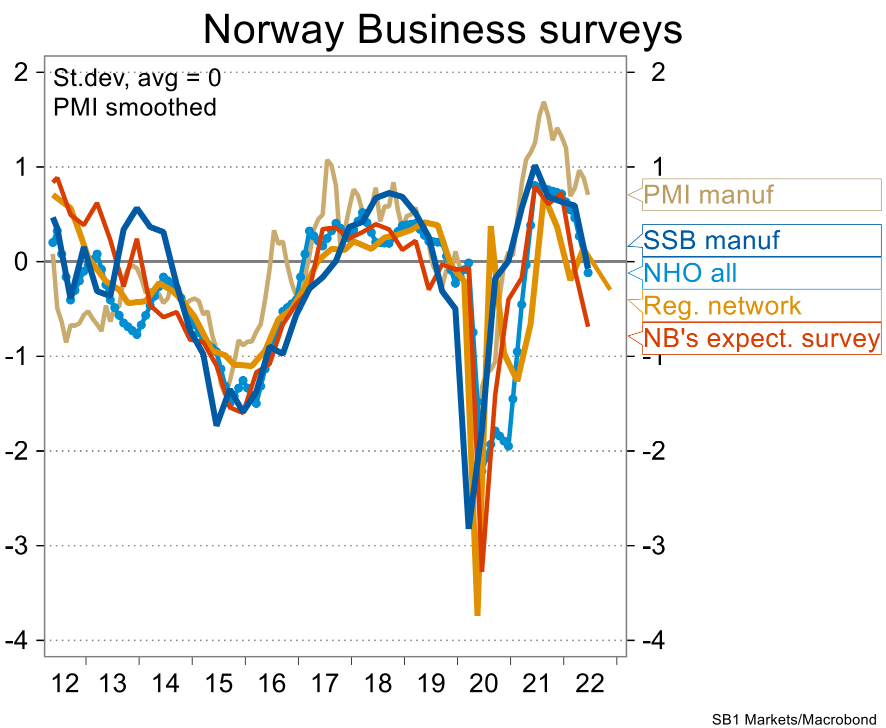
Planned price increases slowed but remains extremely high

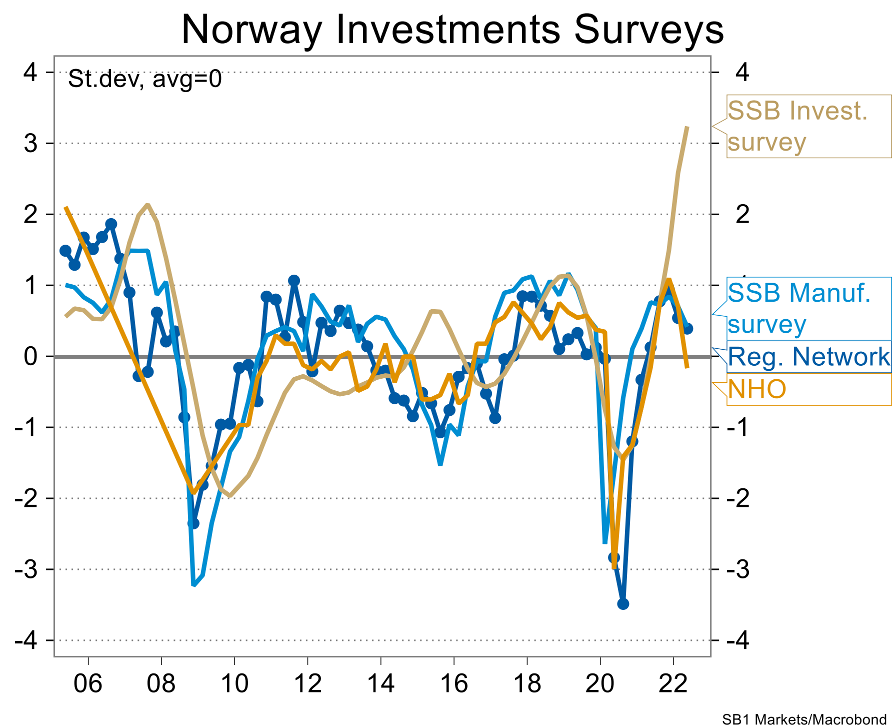


- Prices are expected up far more than suggested by the reported capacity utilisation

Surveys: Peak growth is behind us, average growth is signalled (in average)

Investments surveys are still above average, also the current SSB survey

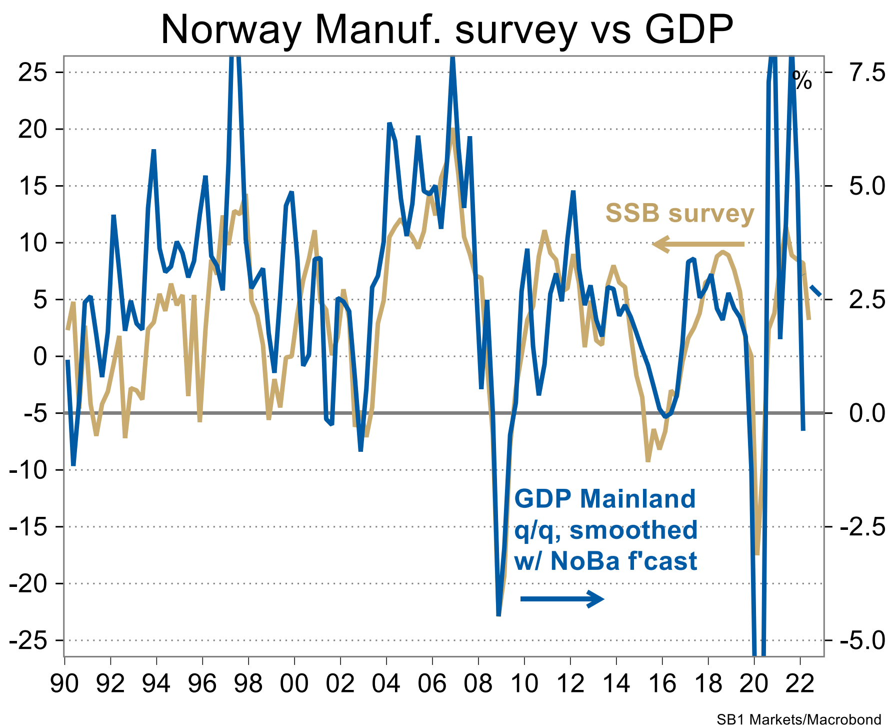


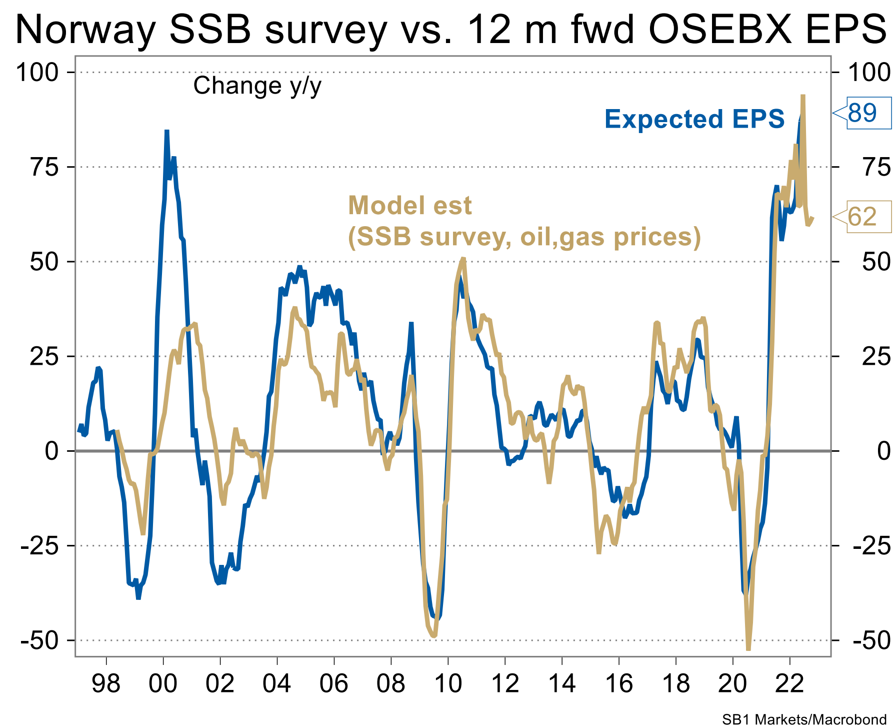


- In the **current manufacturing SSB survey**, companies revised their **investment plans** further down, still indicating growth well somewhat above average
- **Norges Bank's regional survey** agree. NHO' survey is below avg, while **SSB's investment survey** from May reported very strong growth in manufacturing investments

SSB's manufacturing survey signals 2% GDP growth, and still strong EPS growth

… but lower growth than the current 12 m EPS f'cast (where oil & gas prices are added in the model)





- The manufacturing survey is quite closely correlated the Mainland GDP cycle
- The survey is closely correlated to the OESEBX earnings cycle too – and even better if oil & gas prices are added in the equation

SpareBank 1 MARKETS

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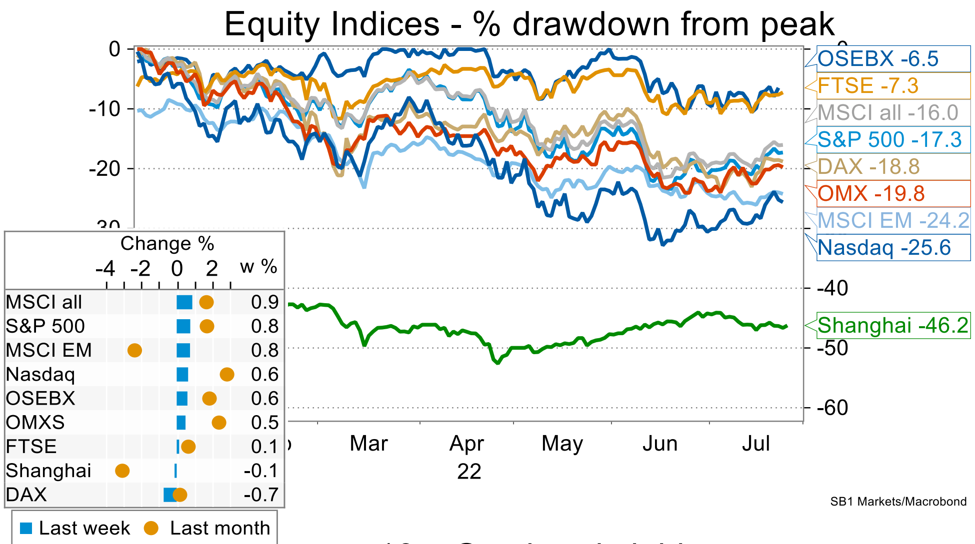
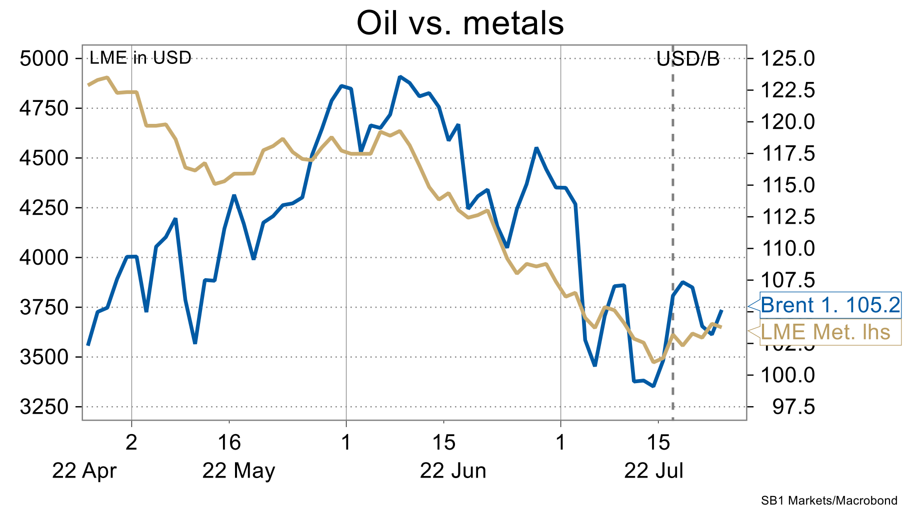
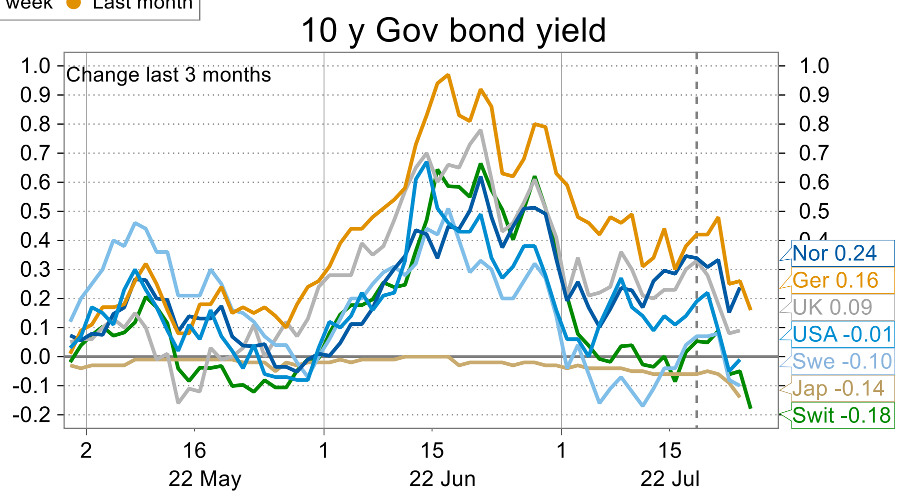
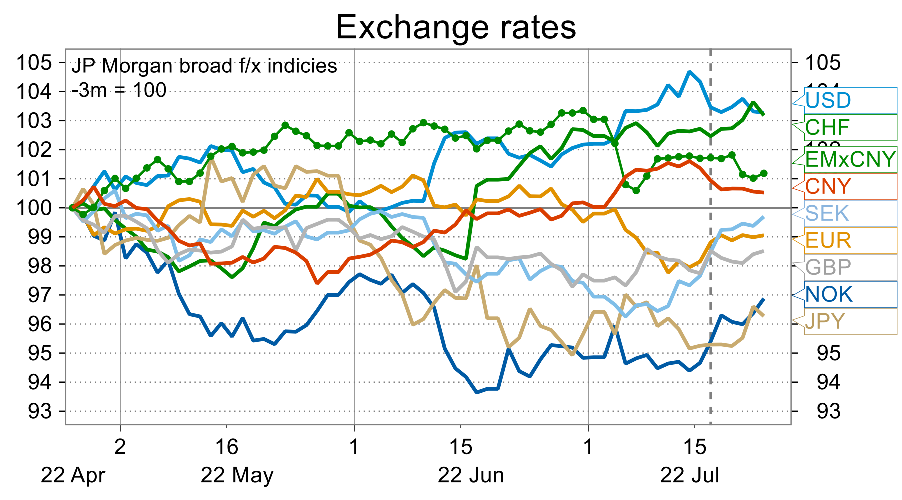
Equity markets mostly up last week. Oil, metals are heading down

Bond yields fell sharply last week (and over the last month) – as the growth outlook deteriorates



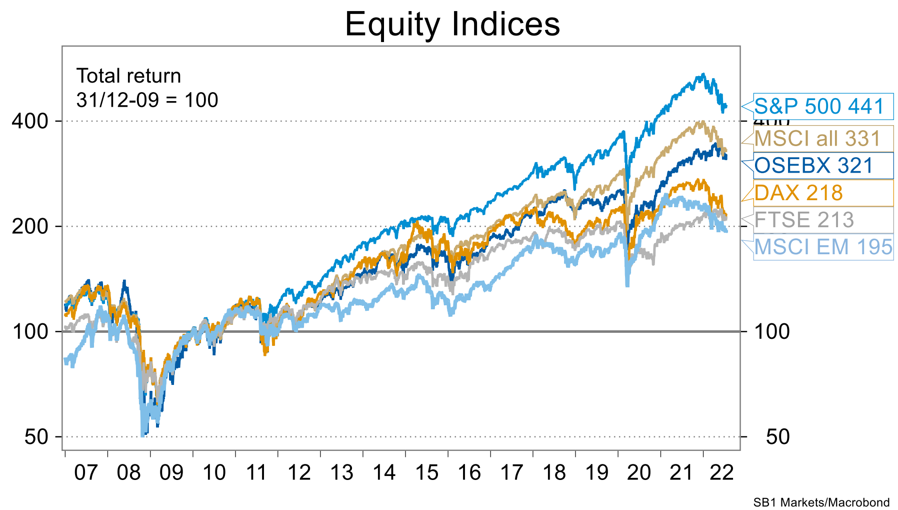


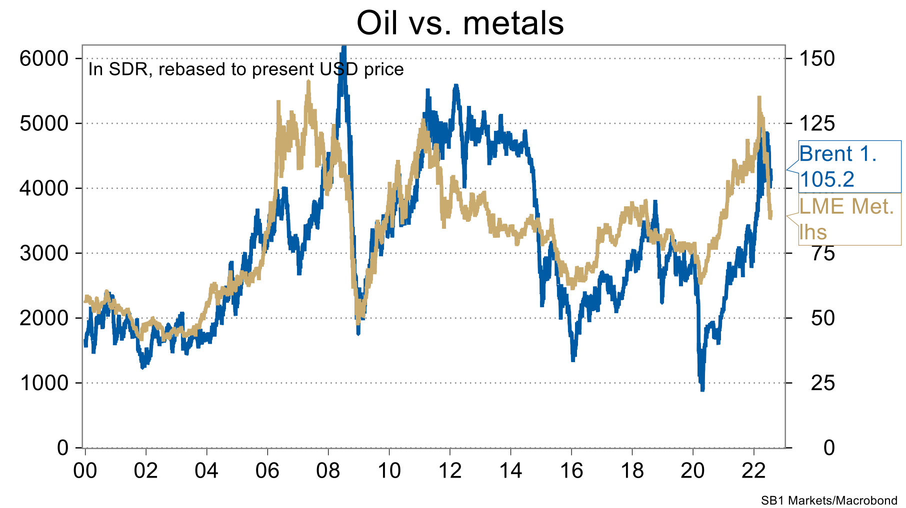


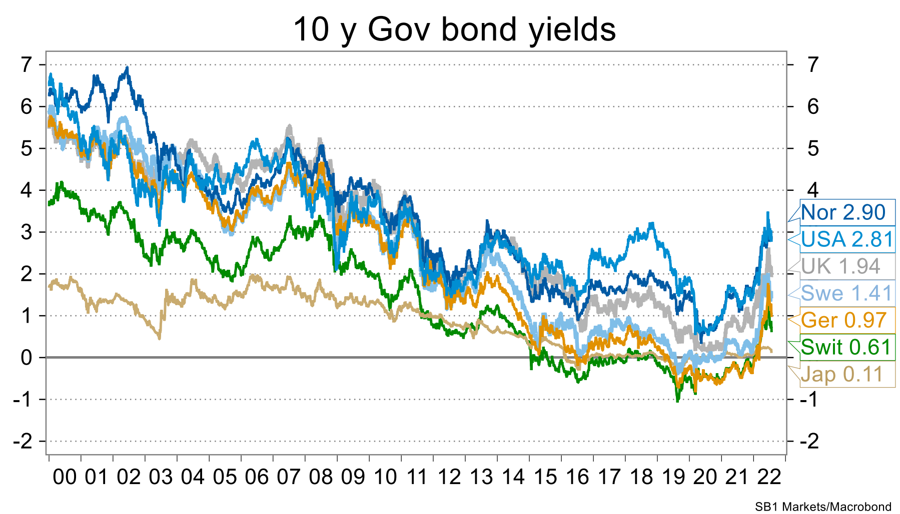


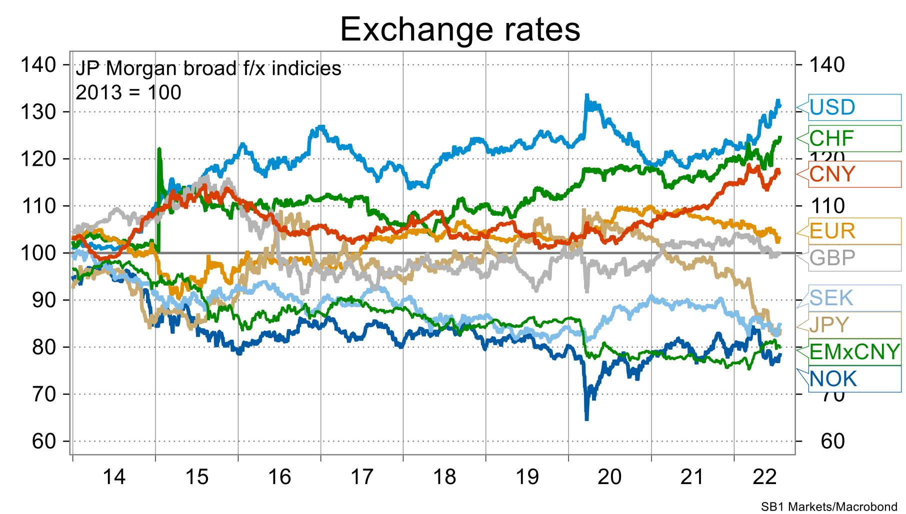
The big picture: Stock markets down, bond yields up

Commodities are on the way down again









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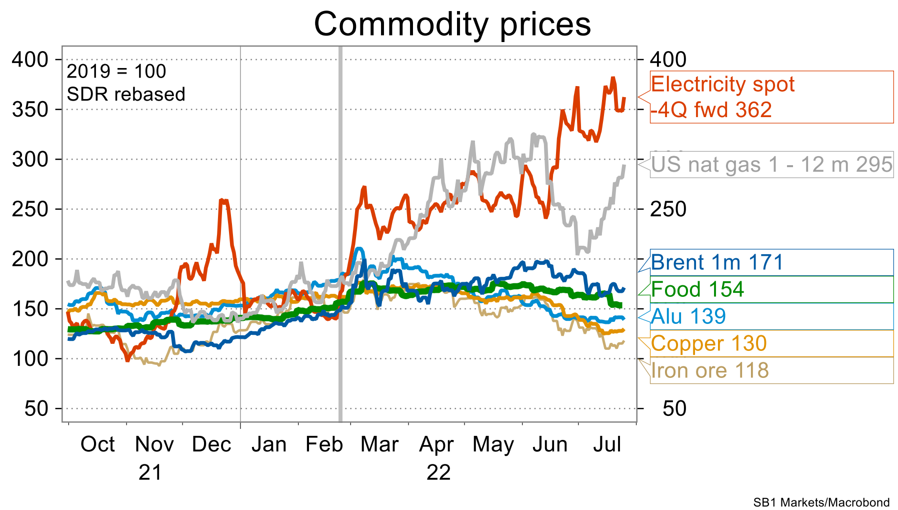
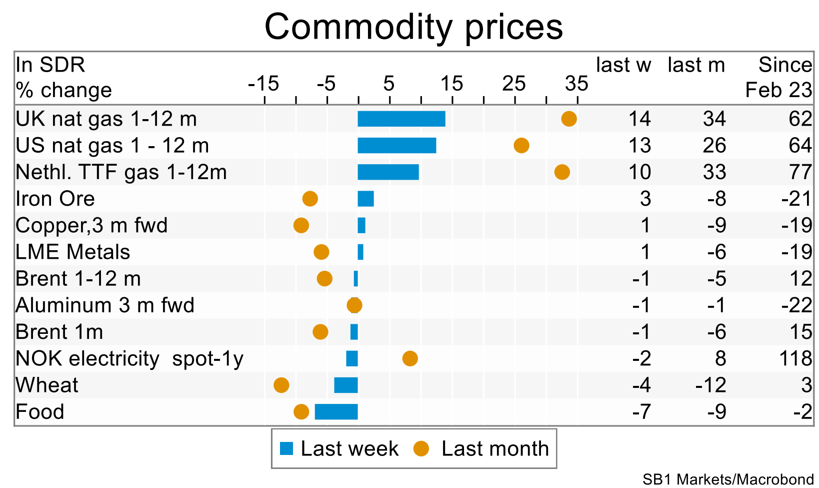
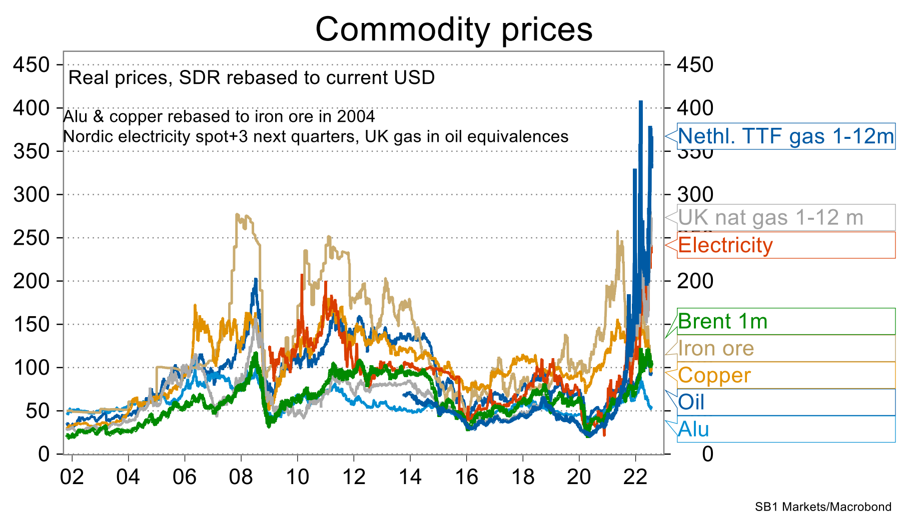
Most commodity prices are on the way down, except European gas/el prices

Food prices fell sharply last week, perhaps supported by an agreement on exports of Ukrainian grains







- Oil prices have stabilised, following the decline
- European natural gas prices rose further last week
- US natural gas prices rose again and are not far below the recent peak
- The Economists food commodity index fell sharply last week, by 7%, and they are lower than before the war started
- Metal prices are on the way down too

SDR: IMF's Special Drawing Rights – a 'global currency'

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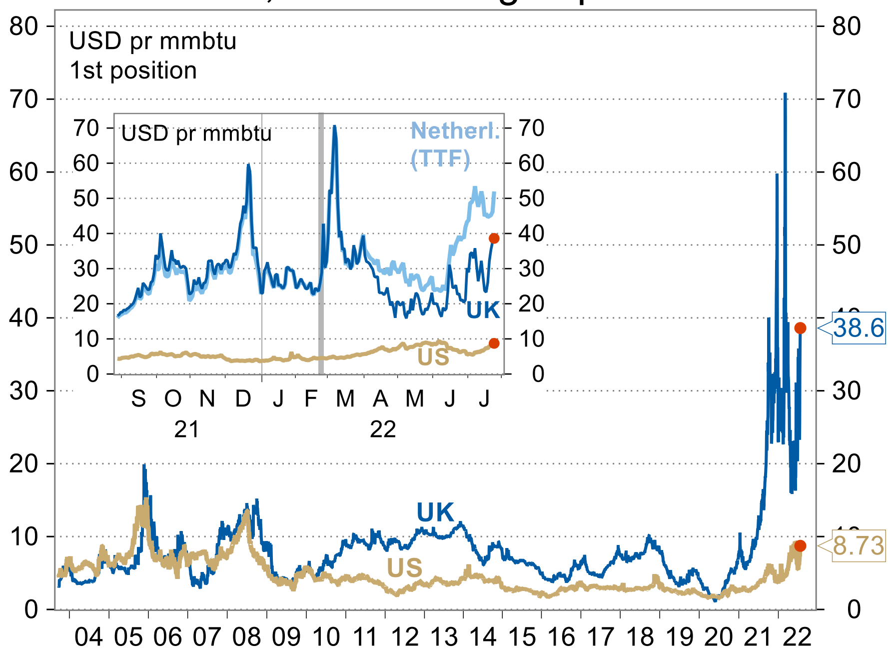
European natural gas prices further up last week

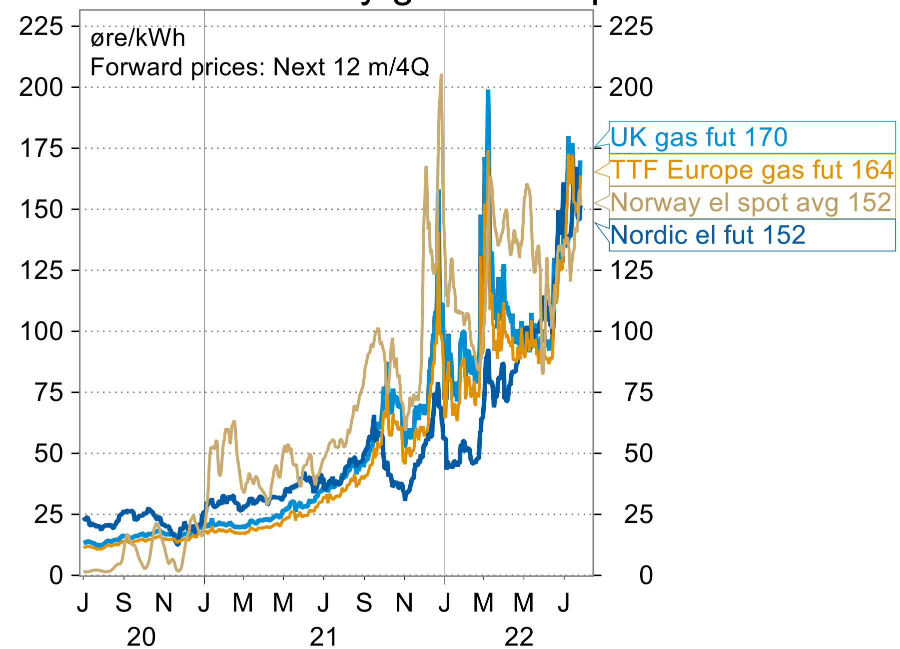
A partial reopening of Nord Stream I was not sufficient to bring prices down

UK, US natural gas prices



SB1 Markets/Macrobond

Electricity/gas future prices



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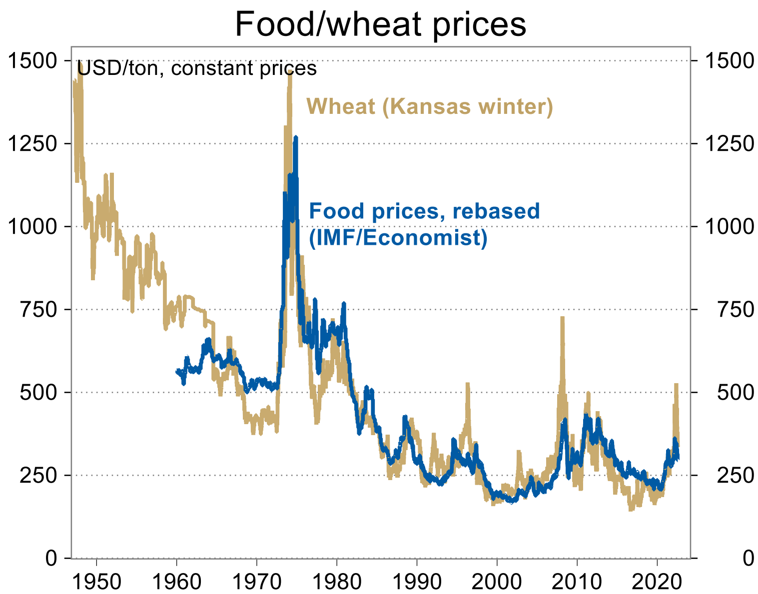
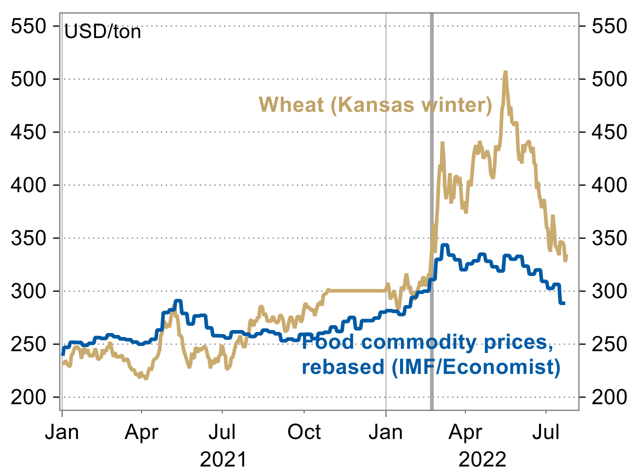
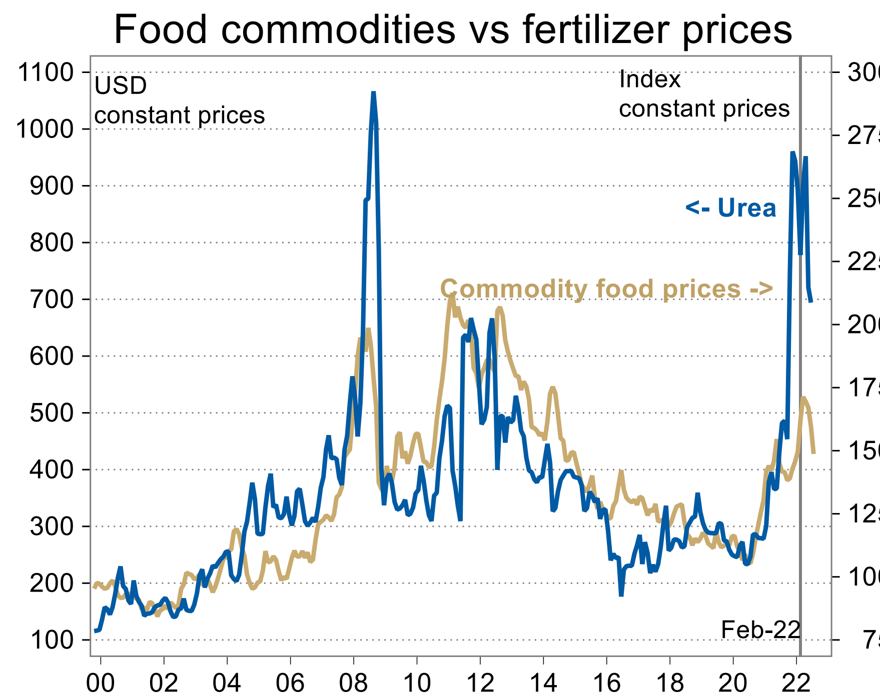
- Continental gas prices are twice as high as UK gas prices in the short end of the price curve, due to lack of transfer capacity, and risk for restrictions on UK gas exports to Europe
- However, for the coming 4 quarters, future prices are similar – and close to Nordic electricity prices

Food prices are trending downwards

Wheat prices are falling rather rapidly and are up just 6% from before the war, from +60% at the top







SB1 Markets/Macrobond

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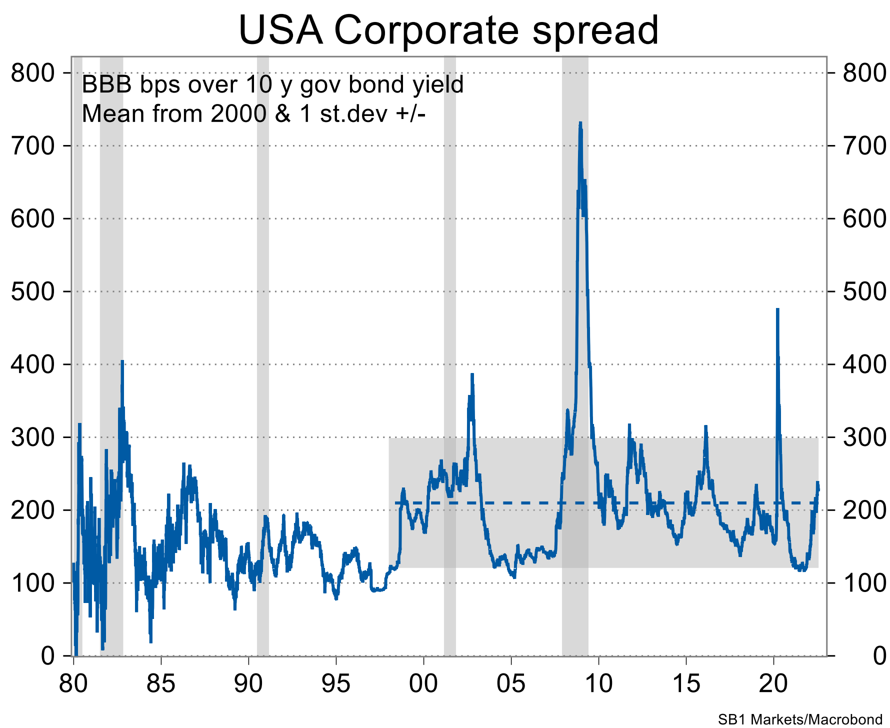
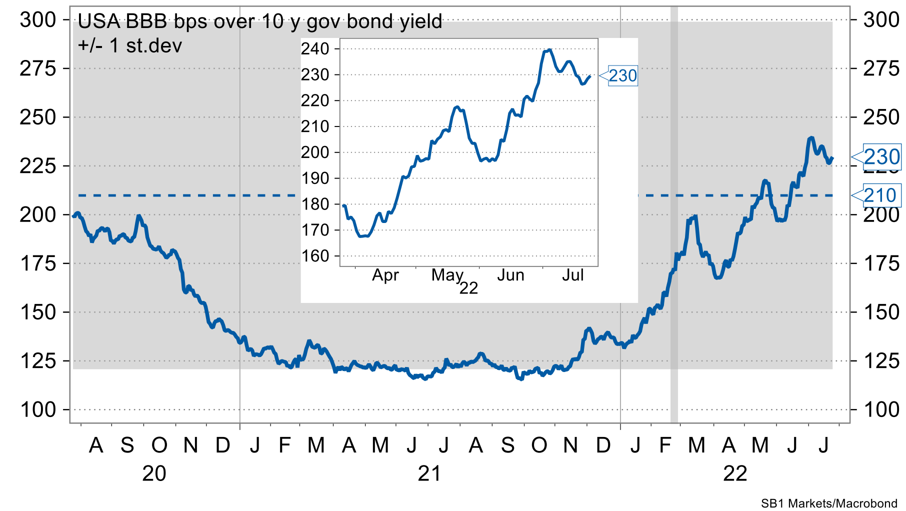
Credit spreads have climbed to above average – and has fallen margianlly

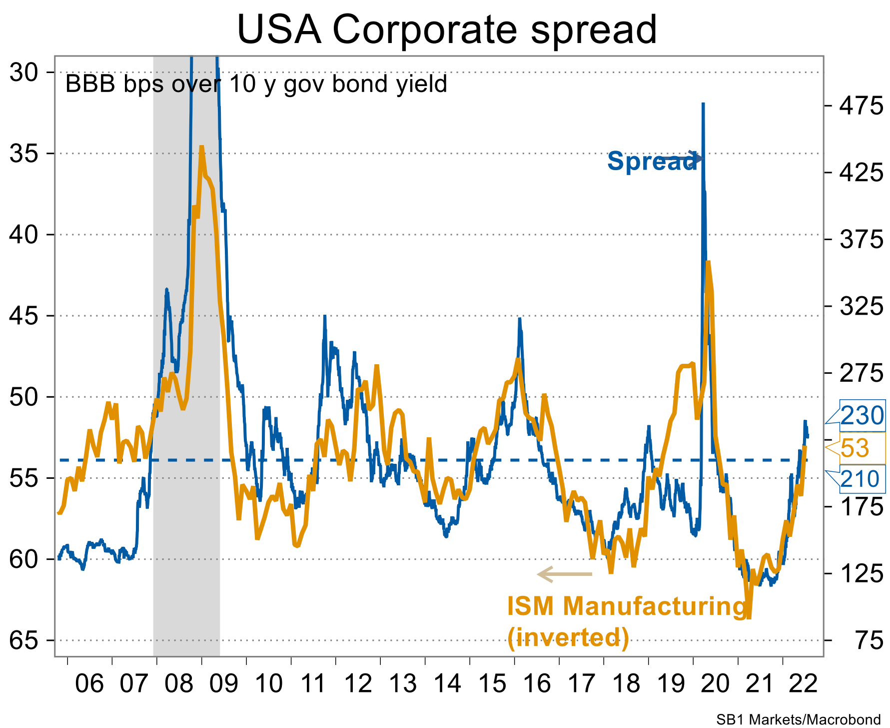


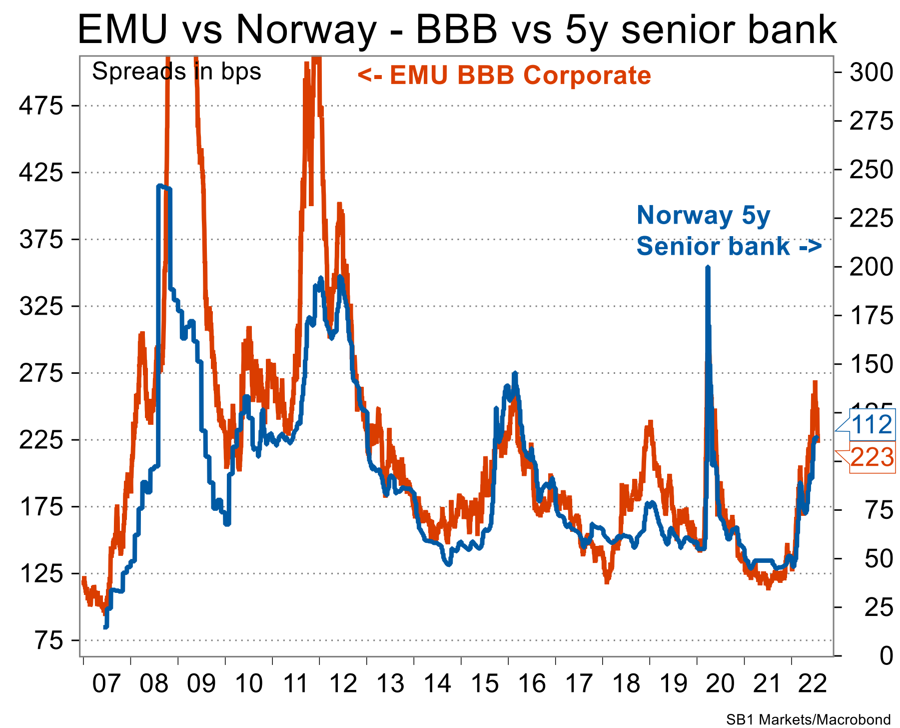


- The US BBB spread is up 110 bps from the bottom last autumn, more than a doubling

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

What do you think is more likely: An ISM at ~~50~~ 45 or 60 in some few months time? We are quite sure..

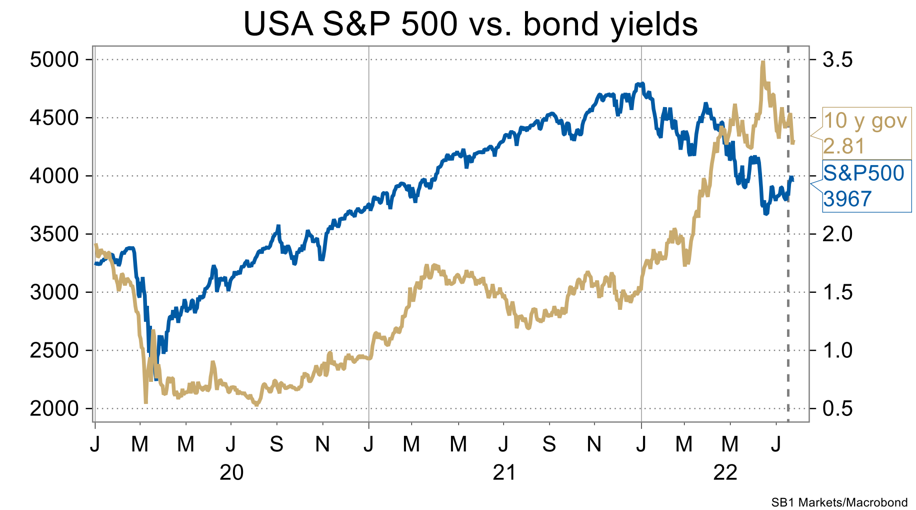


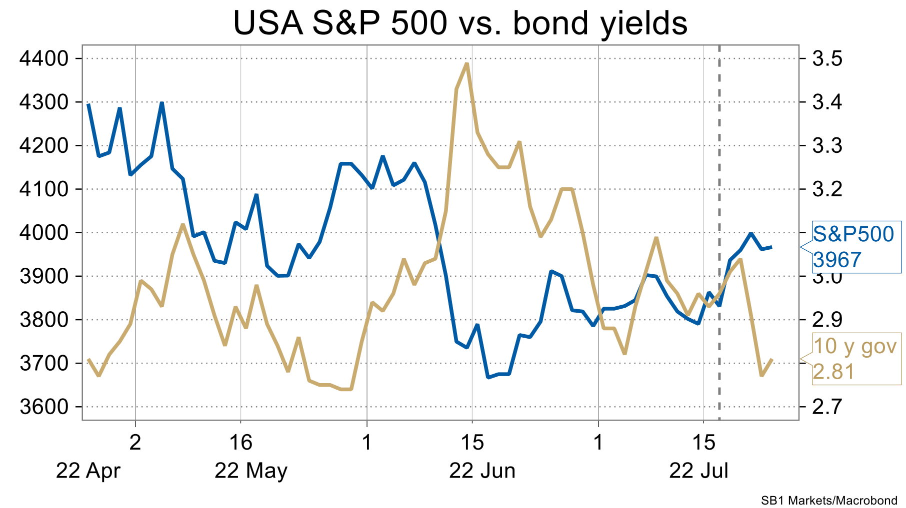


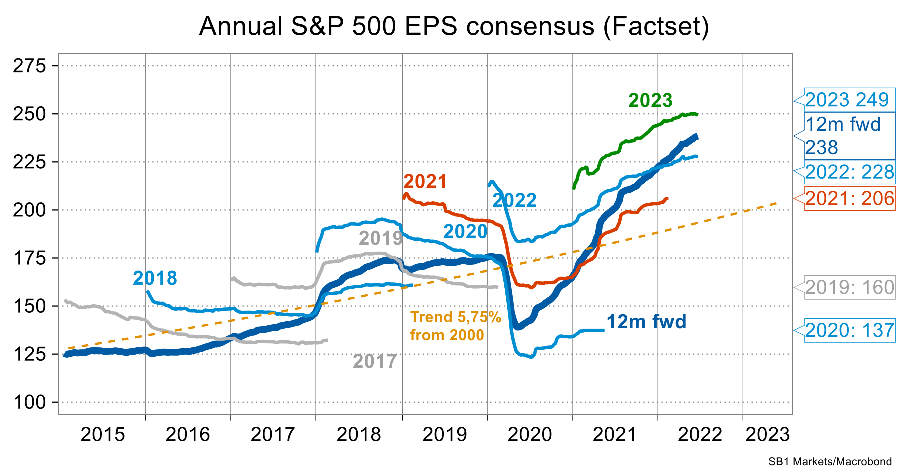
- The answer is not irrelevant for your view on the outlook for spreads, we think
- And do you think Norwegian spreads will be influenced by changes in the global credit market?

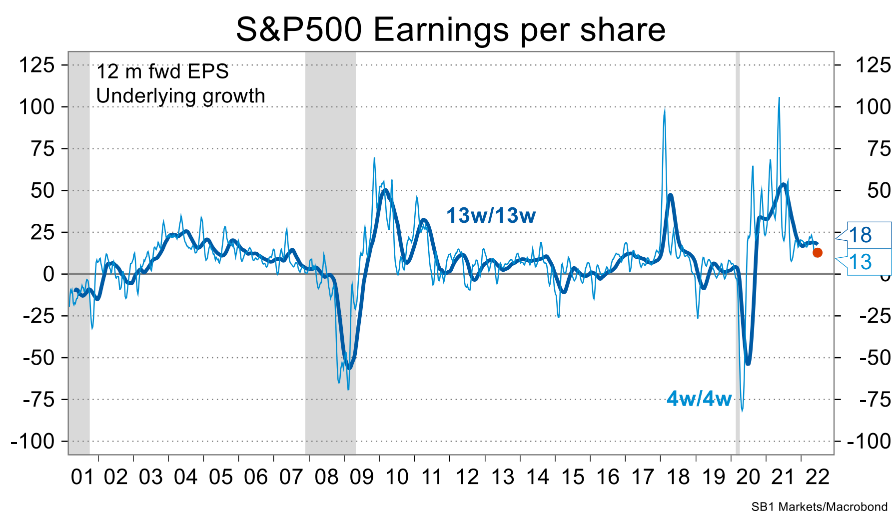
The S&P 500 has been trending slowly upwards since mid June

… but the longer-term trend is still down. No trend in long bond yields. The next shoe to drop: EPS!



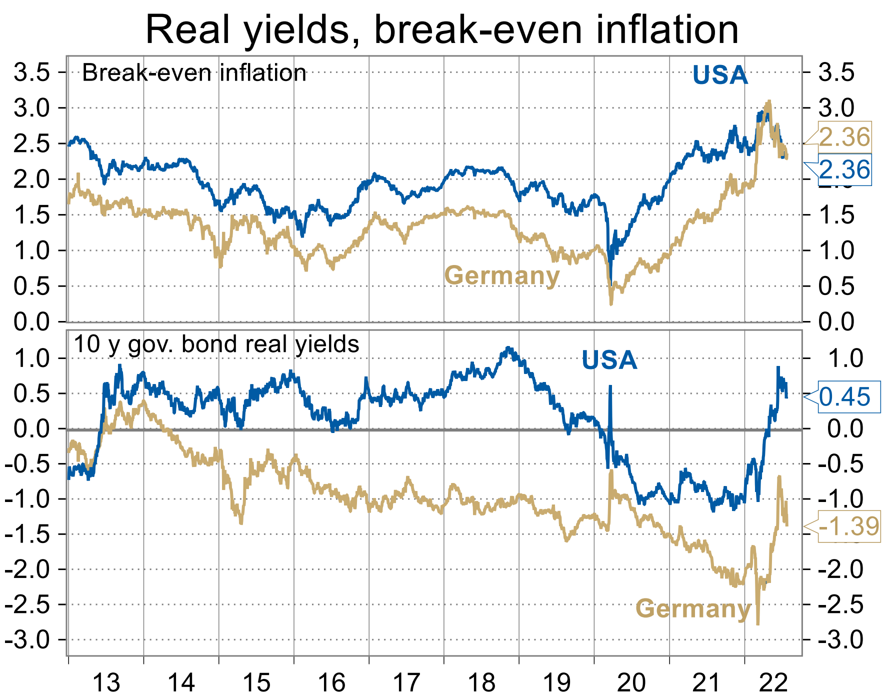


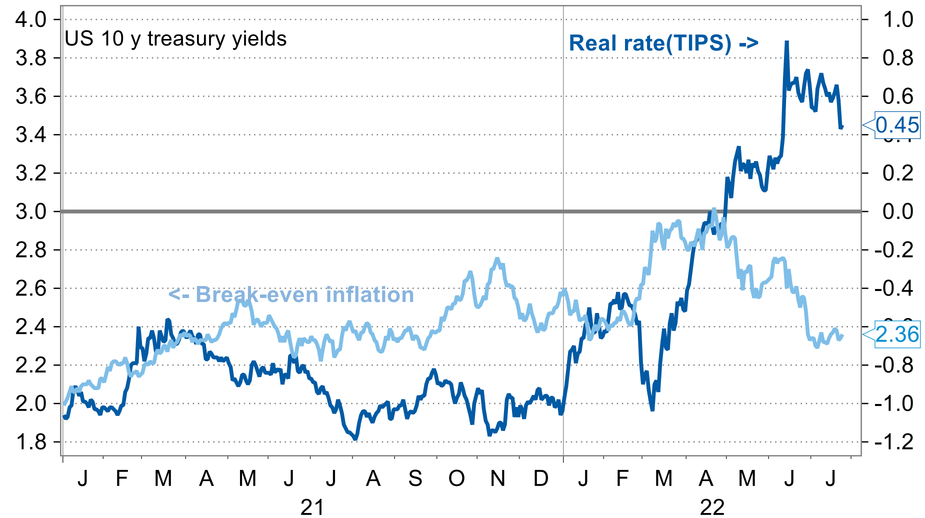




Real rates down last week, more than inflation expectations

Still, the lift in bond yields in 2022 is just due to higher real rates – while inflation expectations are down





- .. at least in the US

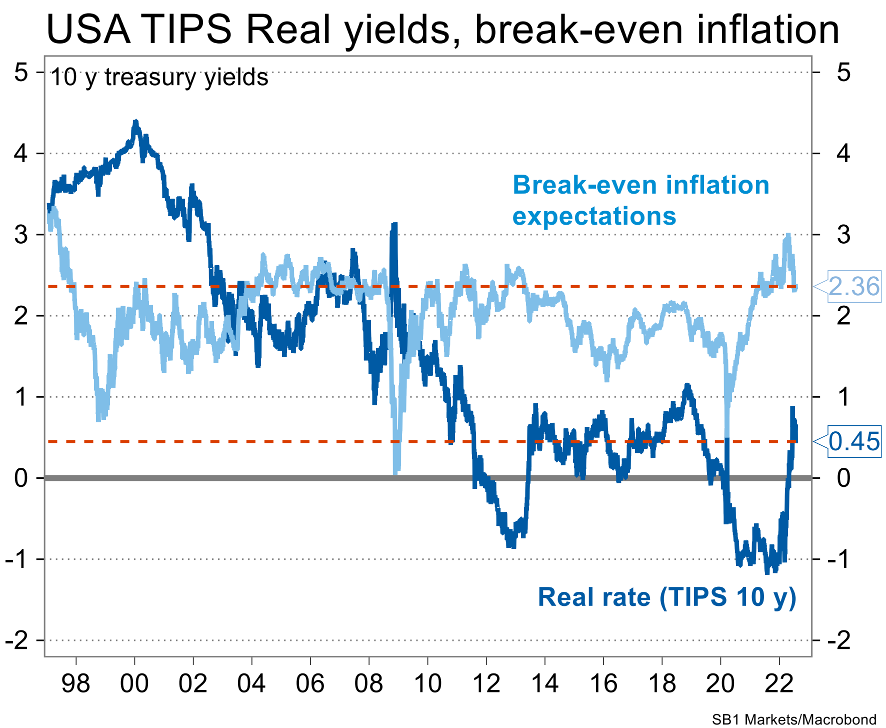
US & Germany 10 y Gov bond yield

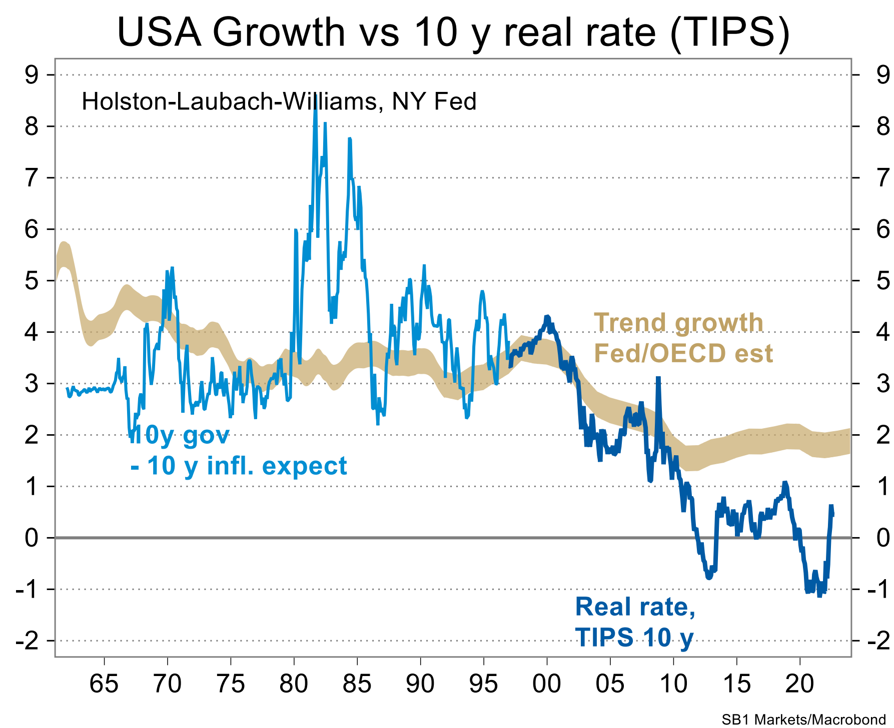
	Yield	Change 1w	Change 1m	Since Feb 18	Min since April-20
USA nominal treasury	2.81	-0.15	-0.32	0.89	0.52
.. break-even inflation	2.36	-0.01	-0.20	-0.05	1.06
.. TIPS real rate	0.45	-0.14	-0.12	0.94	-1.19
Germany nominal bund	0.97	-0.26	-0.46	0.75	-0.65
.. break-even inflation	2.36	-0.07	-0.02	0.38	0.40
.. real rate	-1.39	-0.19	-0.44	0.37	-2.80

SB1 Markets/Macrobond

Mind the gap: It's rapidly closing!

Real rates have returned to a more normal level – while short term growth expectations are falling

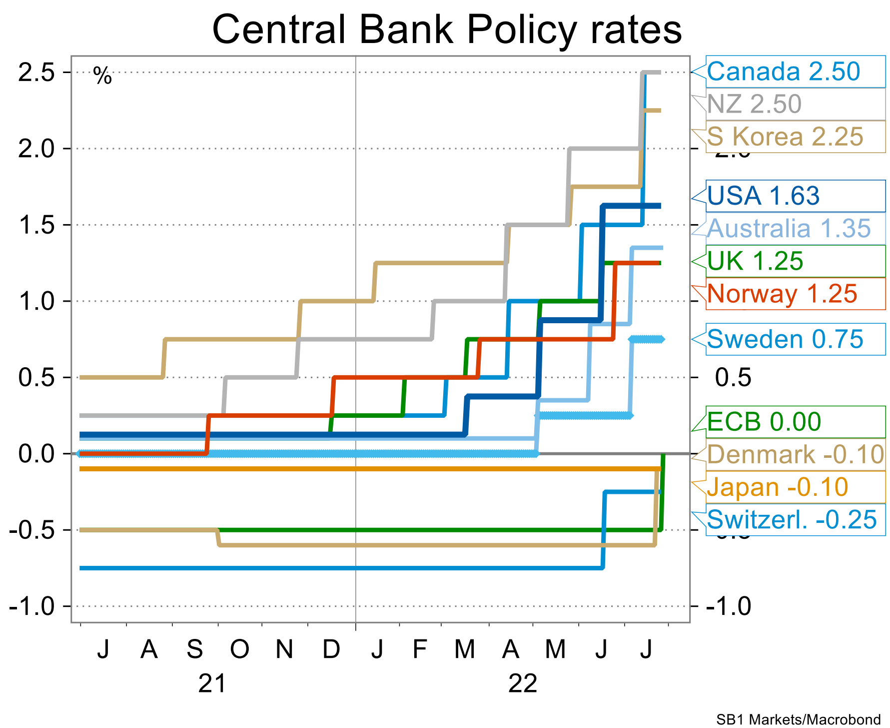


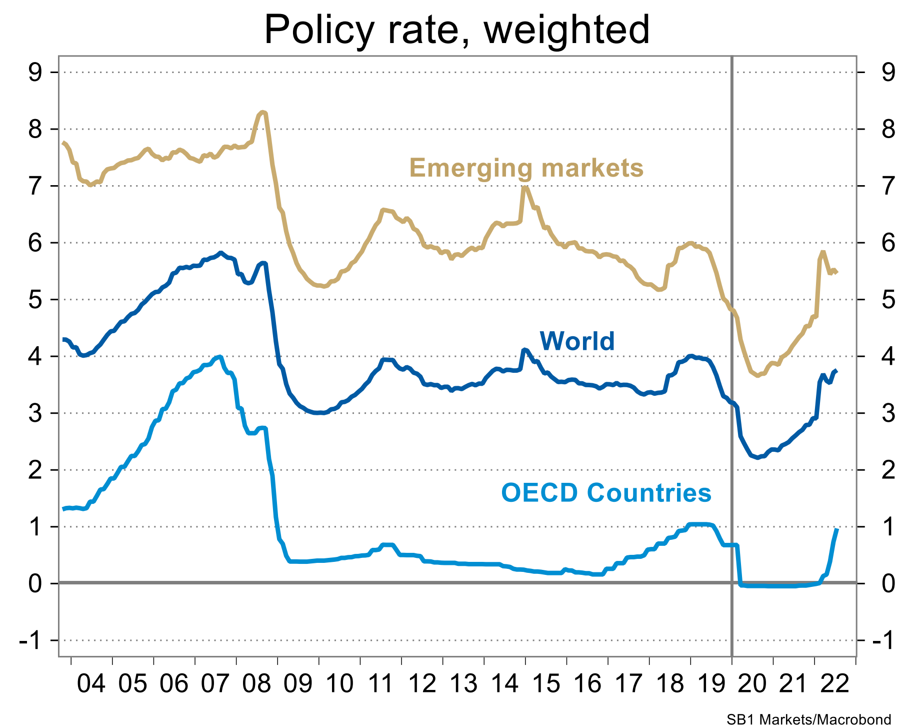


- There is no reason to believe that the current surge in real rates is due to an equivalent increase in growth expectations. It is of course the opposite: At least the short to medium-term outlook is now weakening as central banks finally enter the fight against inflation by at least bringing growth 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?

Central banks on the move

Norway is now at split 6th position among rich countries.





- In addition to rate hikes, central banks (x Japan and the Riksbank) have abolished their QE buying programs (well, the ECB established a new program last week)
- The EM average policy rate has come down due to the Russian cuts – but the trend is straight up

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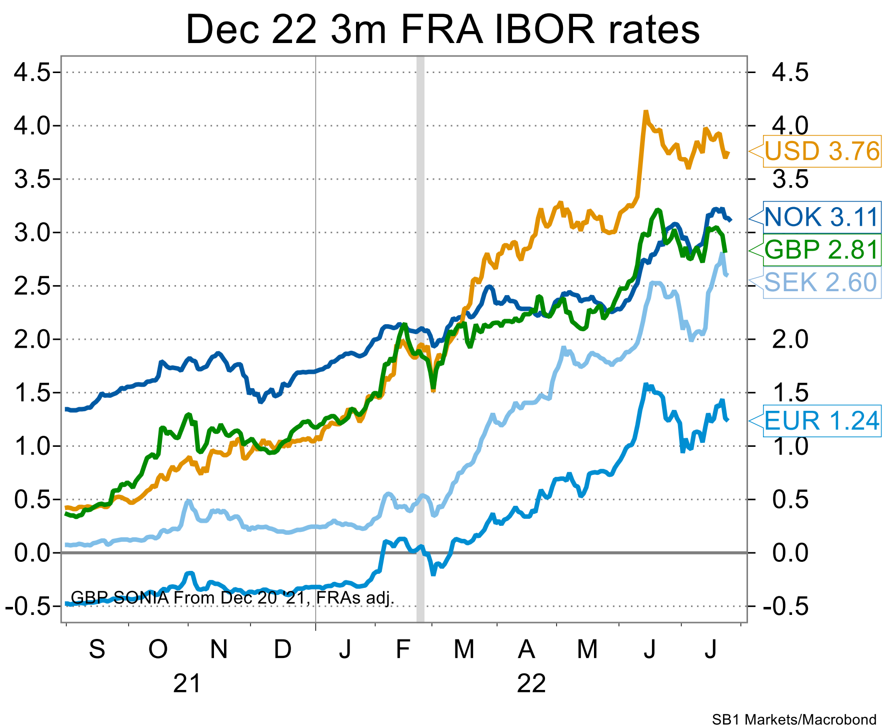
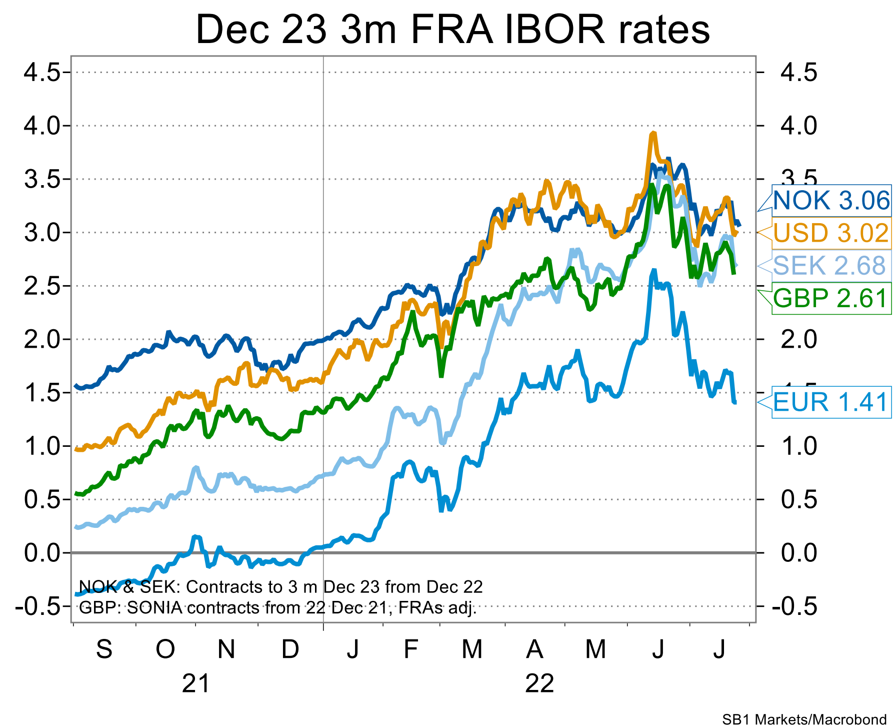
A forceful frontloading is expected – but longer dated FRAs are falling sharply





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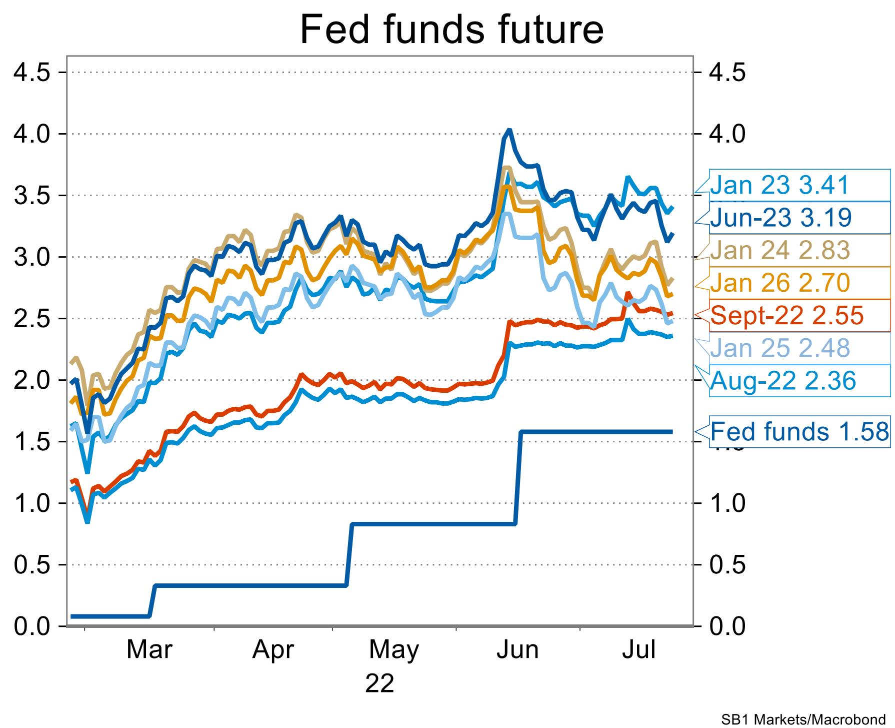
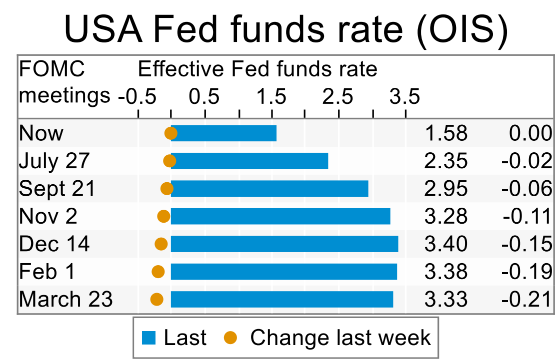
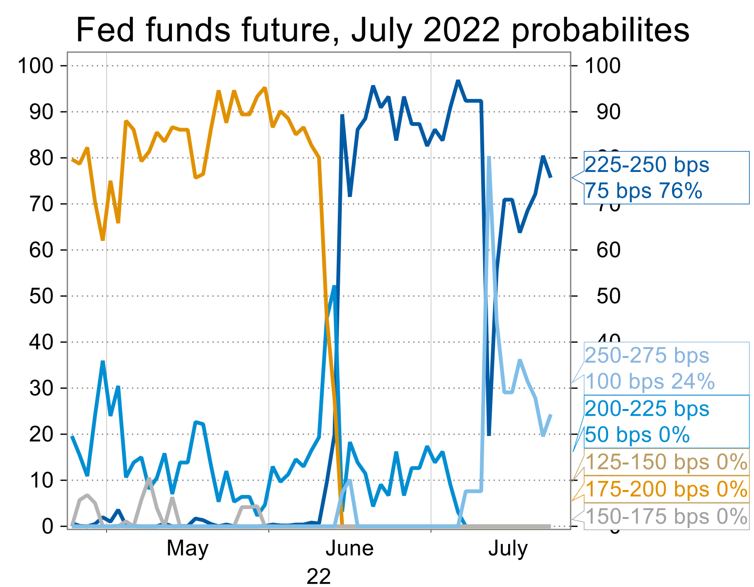
A 75-bps hike tomorrow is fully discounted. But what will the Fed say?

Take an ECB - and admit they do not have a clue (which has been the case for a while…)

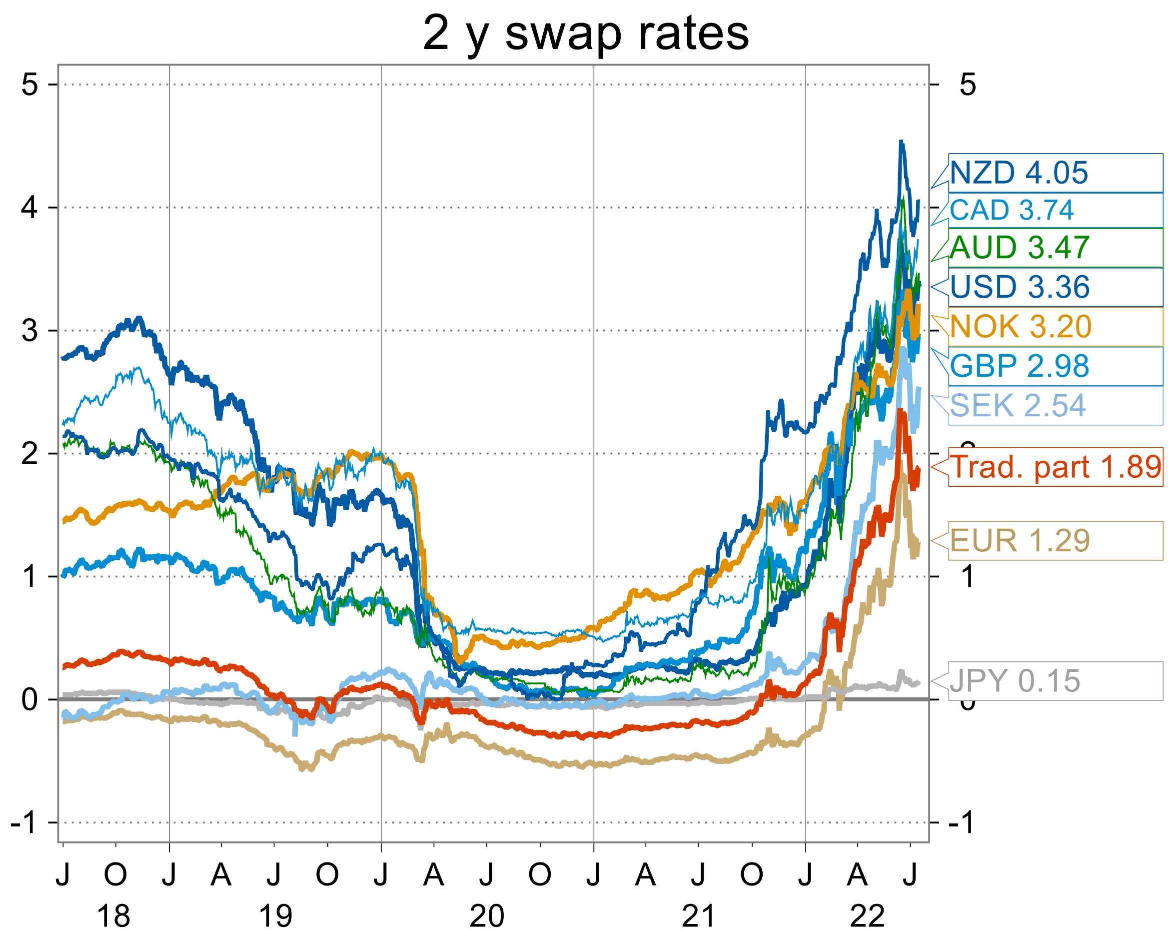




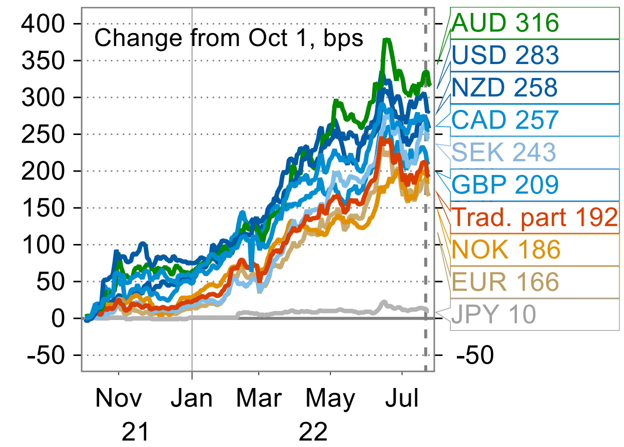


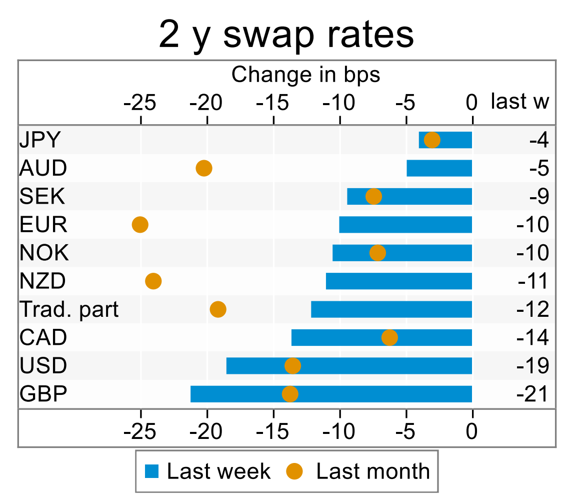
- FRAs – except the very shortest – are heading down, like everywhere else
- For September, the market is split between a 50 and 75 bp hike

A broad decline in 2 y swaps as the economic cycle weakens most places



SB1 Markets/Macrobond

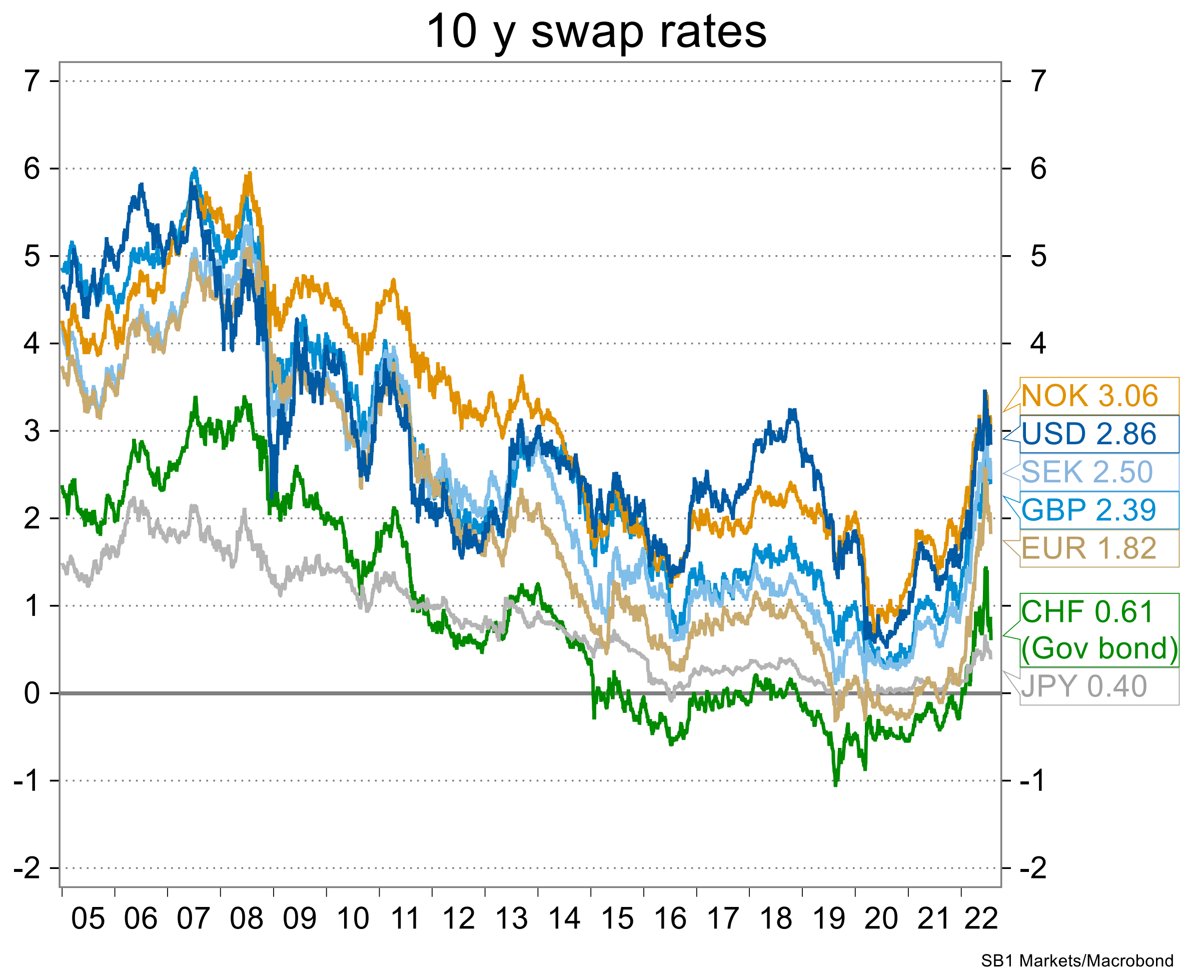


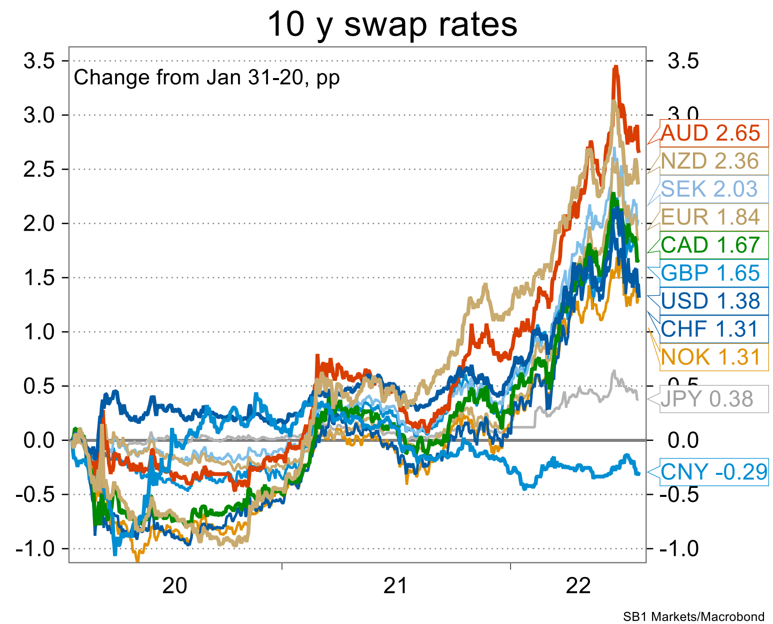


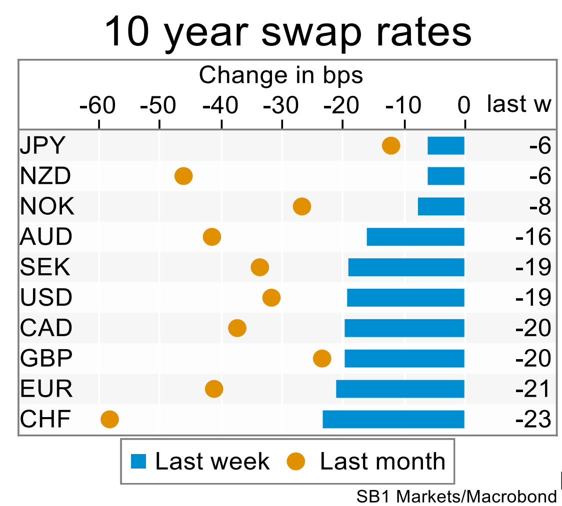
SB1 Markets/Macrobond

10 y swaps down everywhere – the economic cycle is turning south

Winter (aka recession) is coming



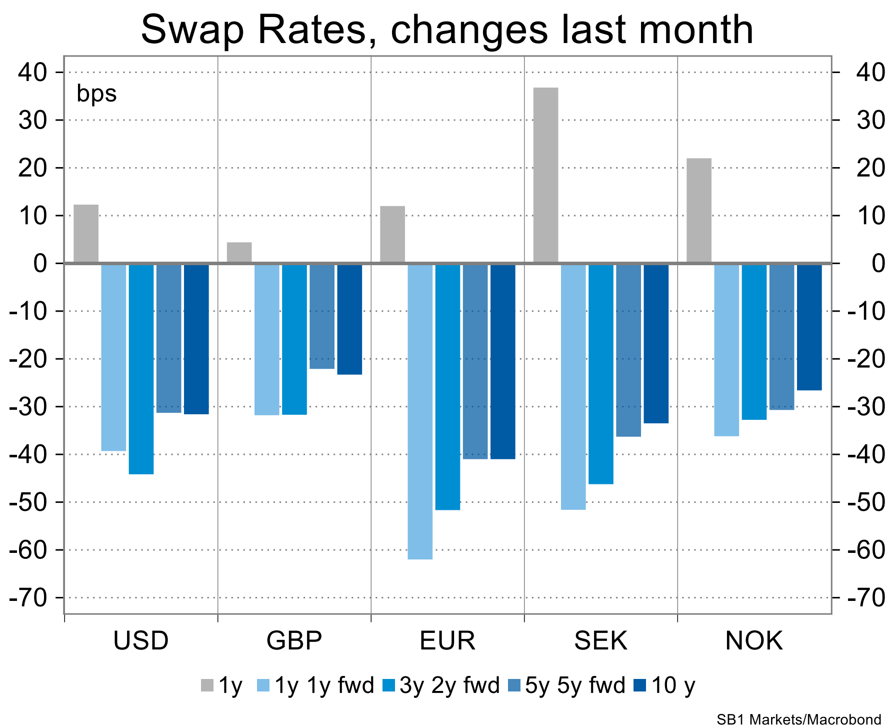


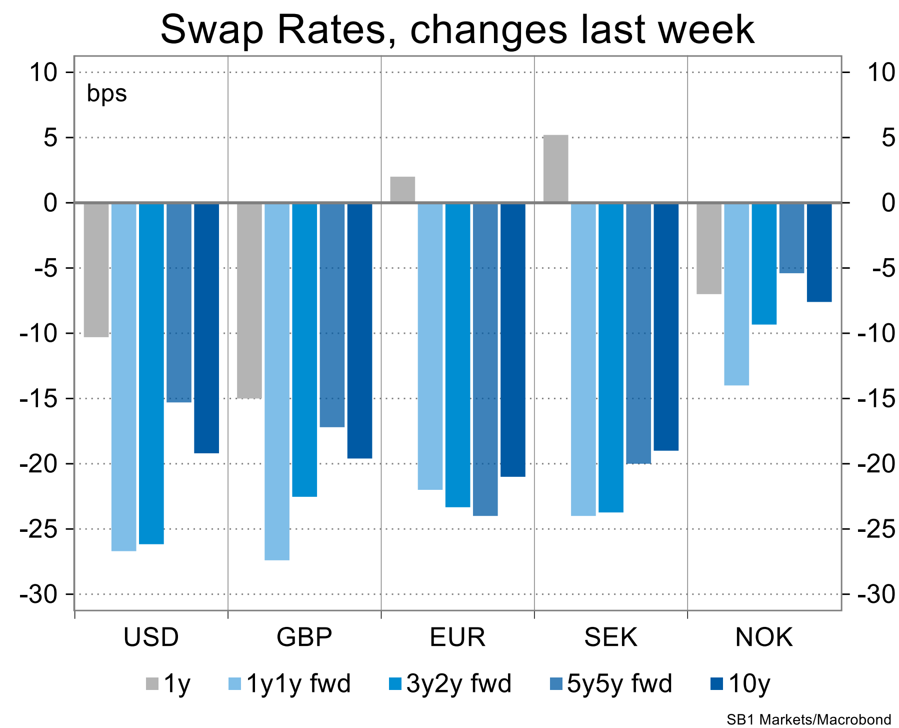


CHF: 10 y government bond yield

The short end is resilient but longer dated yields are all sharply down

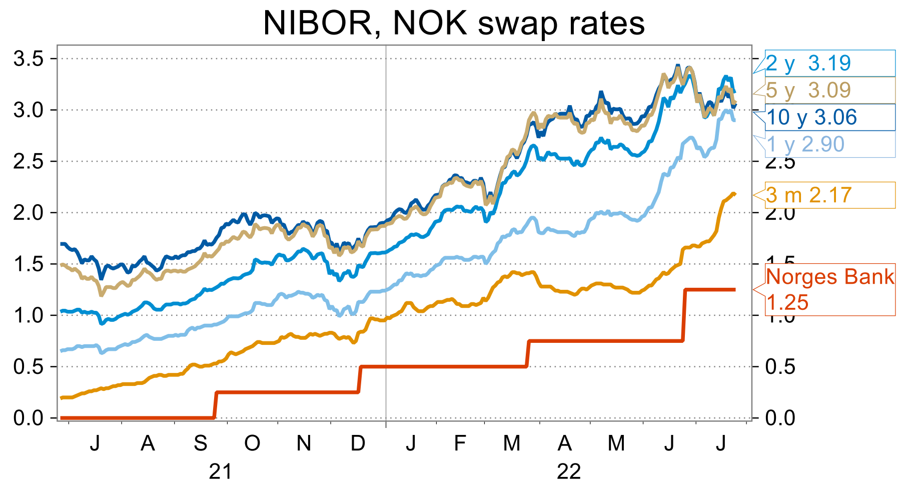
Winter (aka recession) is coming

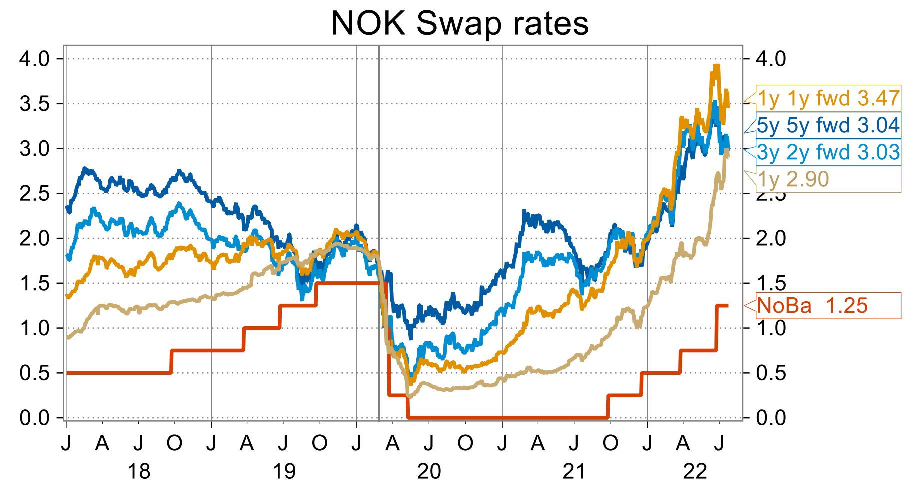


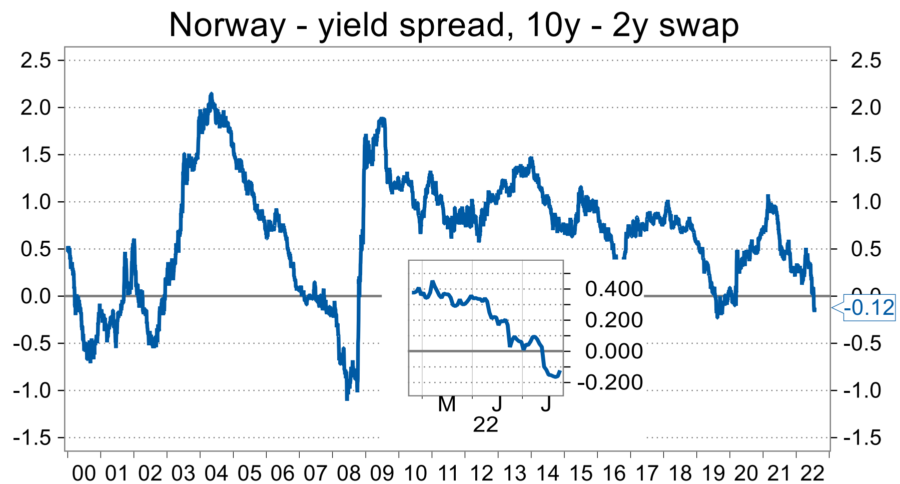


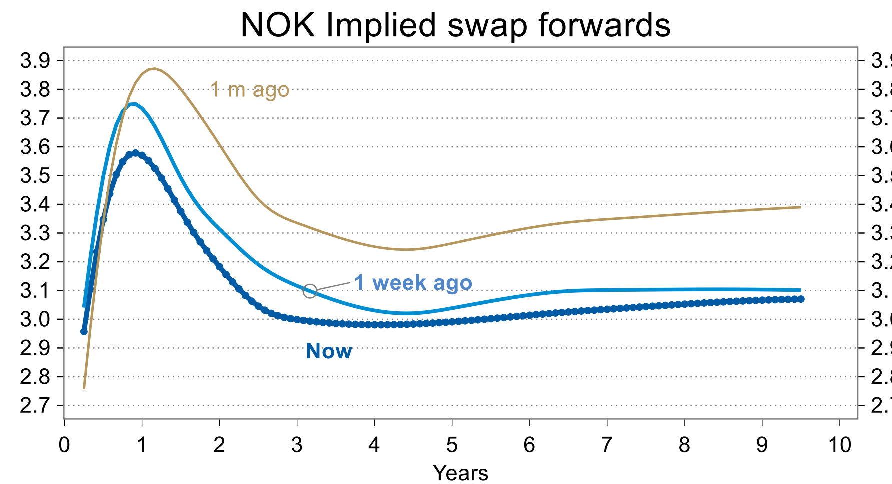
Rates down all over the curve

The 10 - 2y is finally inverted

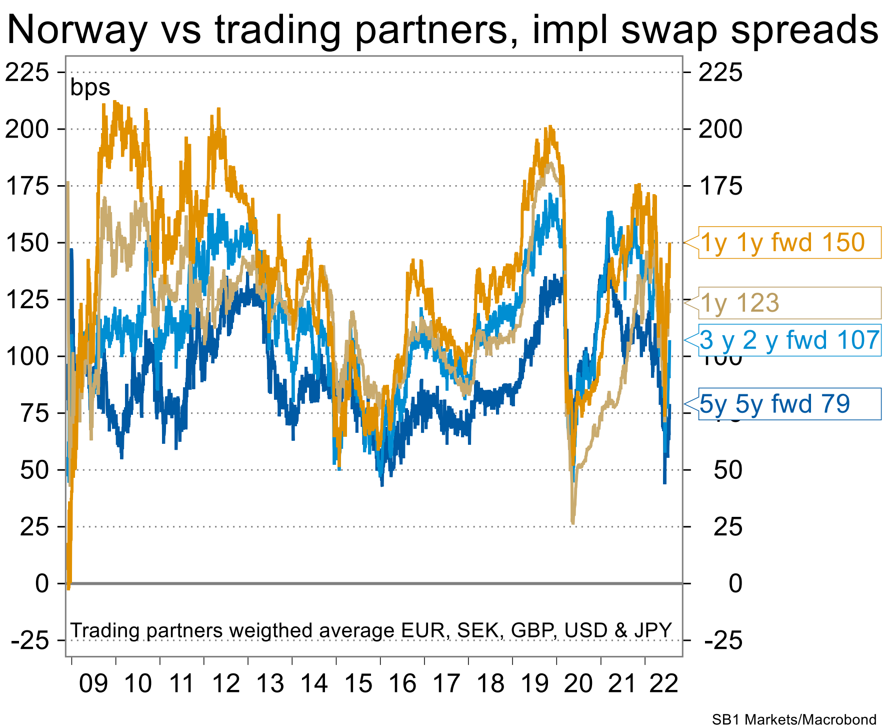


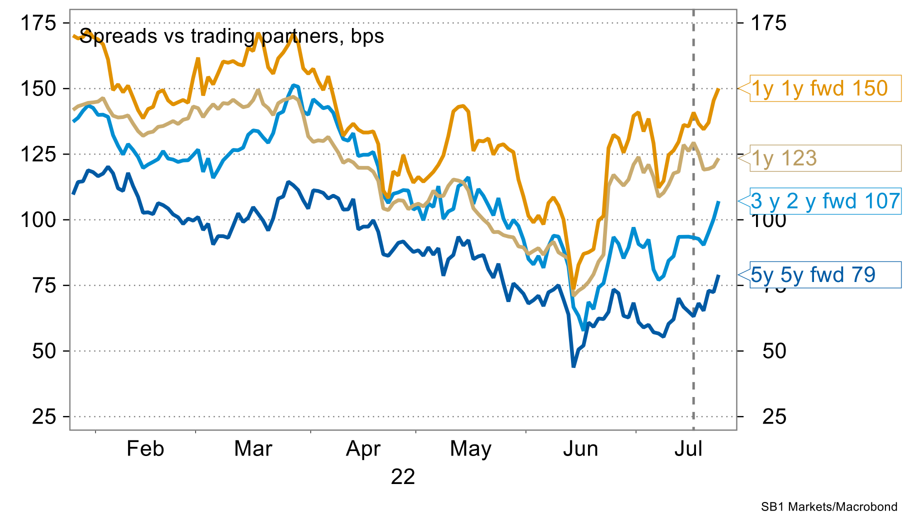


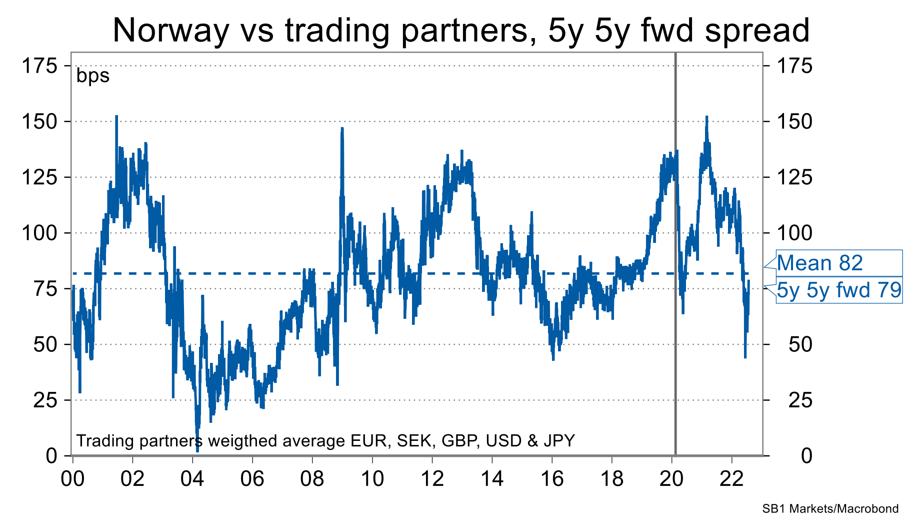




Spreads out all over the curve, barring the very short end







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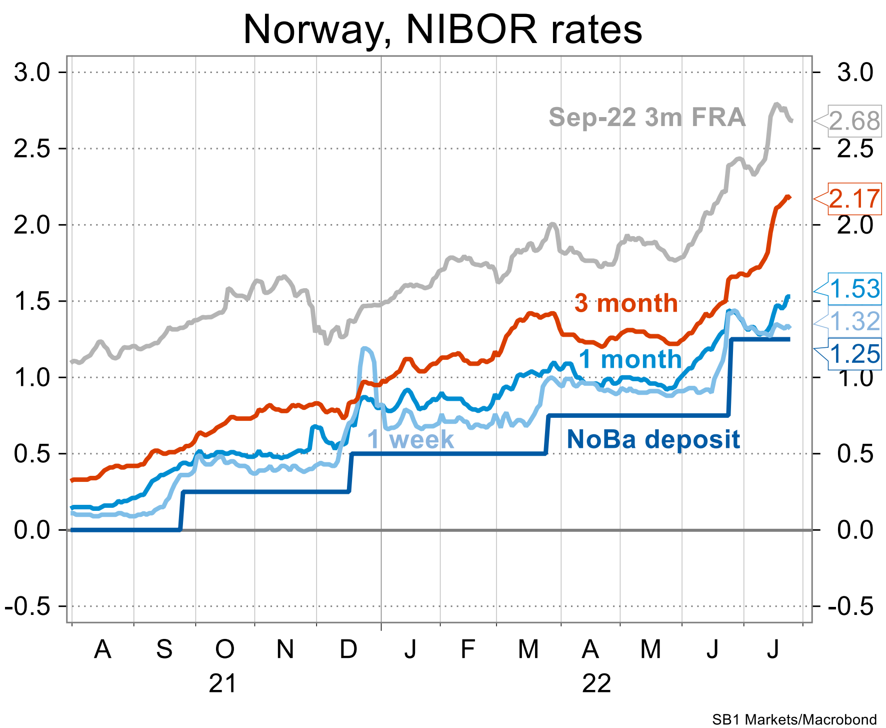
The 3m NIBOR up to 2.17% as 50 bps NoBa hikes in both Aug and Sept is discount.



- The USD LIBOR-OIS spread fell 3 bps to 10 bps last week – which is a low level!

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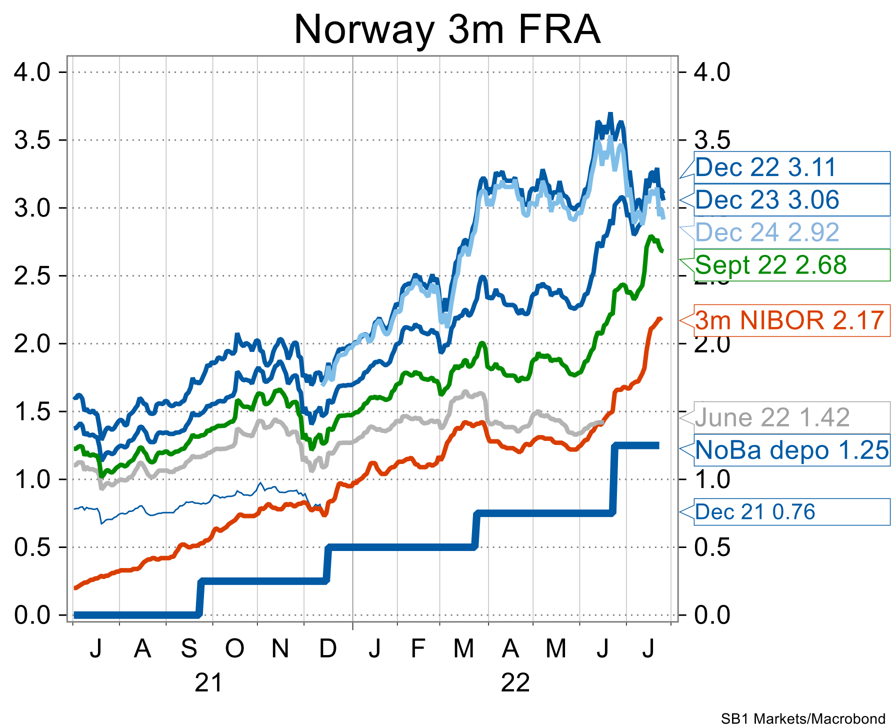
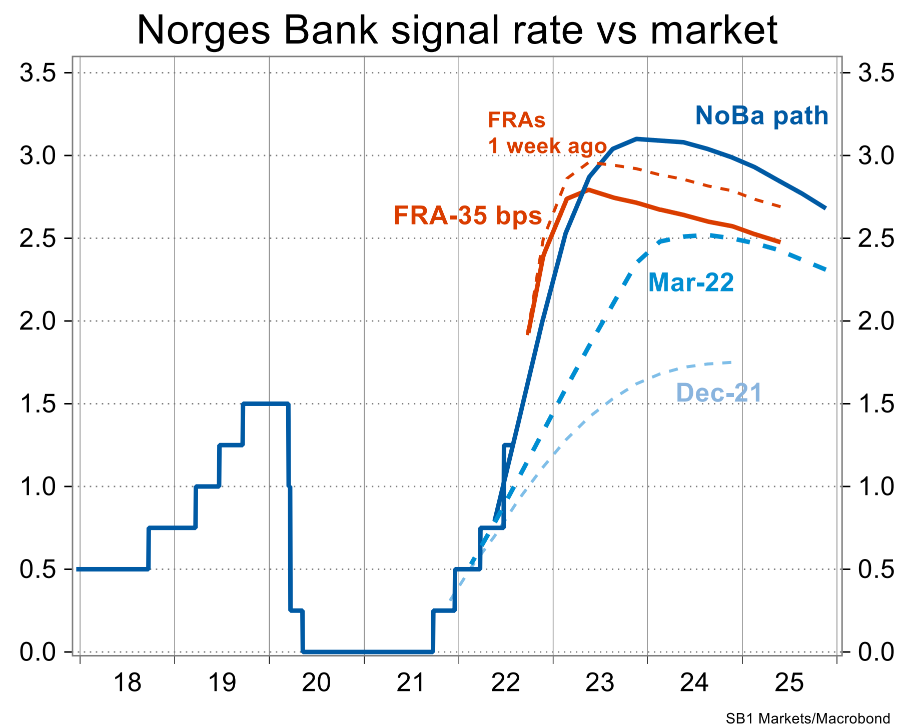
Rate expectations down from early 2023, but first +150 bps up to 2.75% in Dec

50 bps hike in both August and September, and then 25 bps in both Nov and Dec still discounted

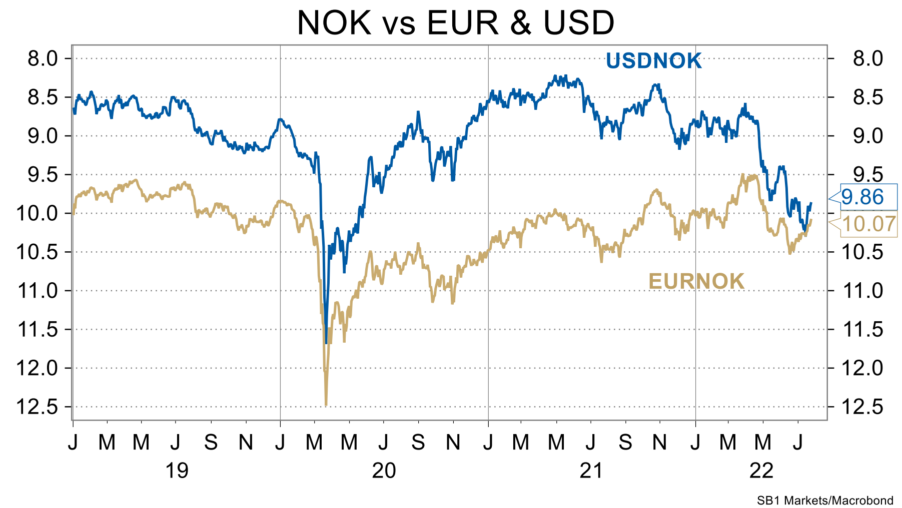


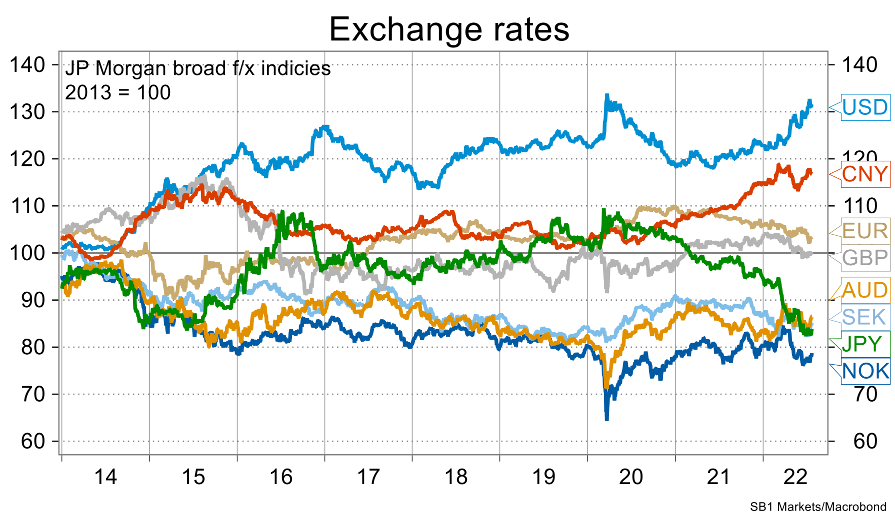


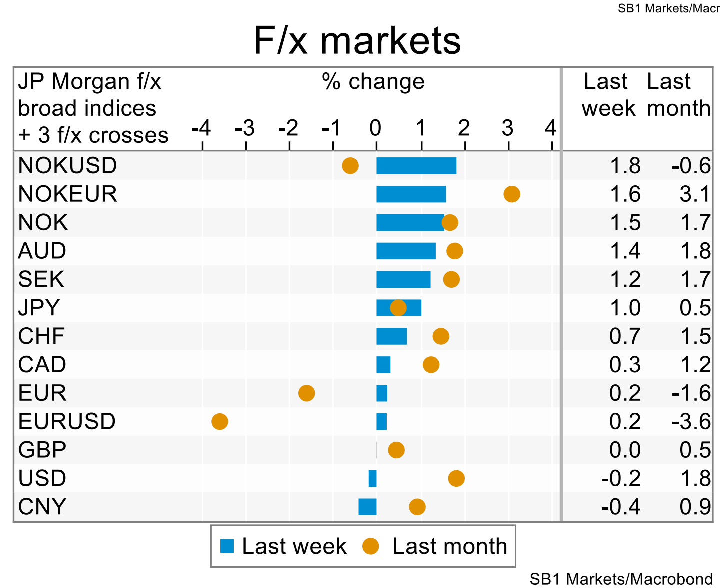
- **If NoBa hikes by 25 bps** in August and September, which was clearly signalled in the June MPR, the average signal rate would be 1.53% the coming 3 months. The current 3m NIBOR is at 2.17%, and the Sept 3 m FRA is at 2.68%. If not money market spreads have exploded, 50 bps hikes in both August and September is discounted – and further 25 bps hikes in November, December – up to 2.75%
- Thus, the market now expects a frontloaded but shorter hiking process, with a 35 bps lower peak level than NoBa assumed in June – and far earlier, just as in the world around us
- *We think the 50 + 50 bps hikes in August and September are more aggressive than Norges Bank will deliver,* we said last week
  - » FRA rates fell significantly but most after the initial 2 x 50 bps, which is still discounted
  - » **We still think the risk at the upside is less than the risk at the downside vs. current market expectations, at the short end of the curve**

NOK last week's winner, from a low starting point

EUR & USD clos to unchanged (trade weigthed)







JP Morgan f/x broad indices + 3 f/x crosses	Last week	Last month
NOKUSD	1.8	-0.6
NOKEUR	1.6	3.1
NOK	1.5	1.7
AUD	1.4	1.8
SEK	1.2	1.7
JPY	1.0	0.5
CHF	0.7	1.5
CAD	0.3	1.2
EUR	0.2	-1.6
EURUSD	0.2	-3.6
GBP	0.0	0.5
USD	-0.2	1.8
CNY	-0.4	0.9

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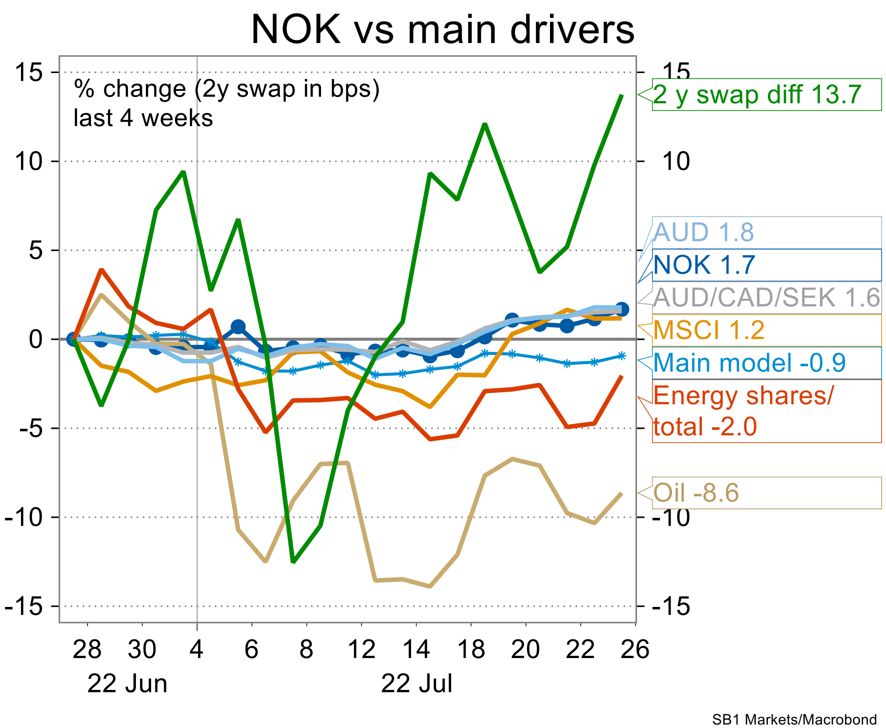
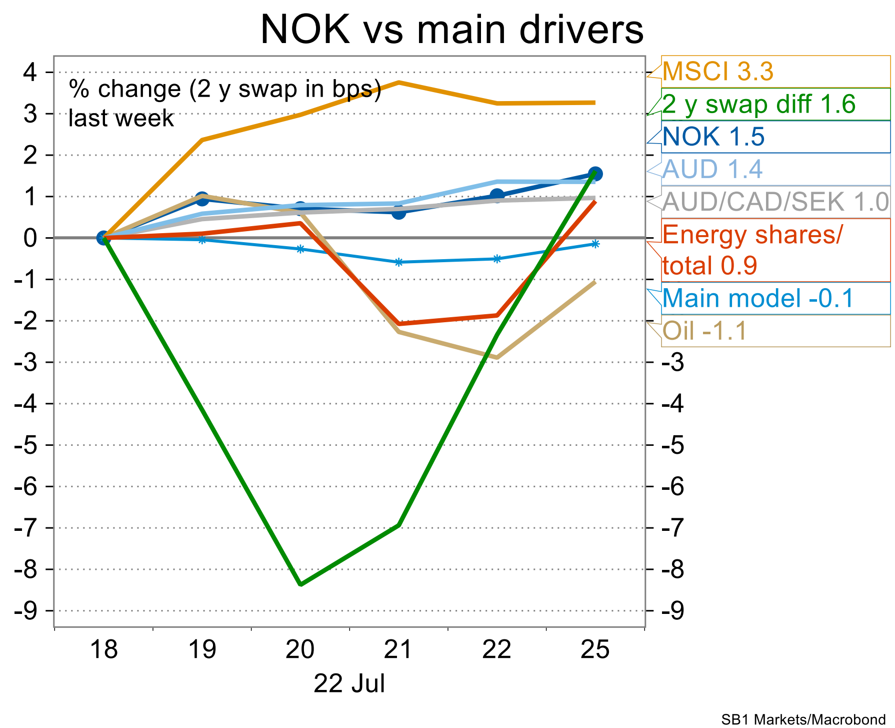
NOK up 1%, our model said 0.4%. Oil was flat vs. last week, NOK int. rates up

NOK is far below our model estimate, and NOK is weak vs other commodity currencies, energy shares





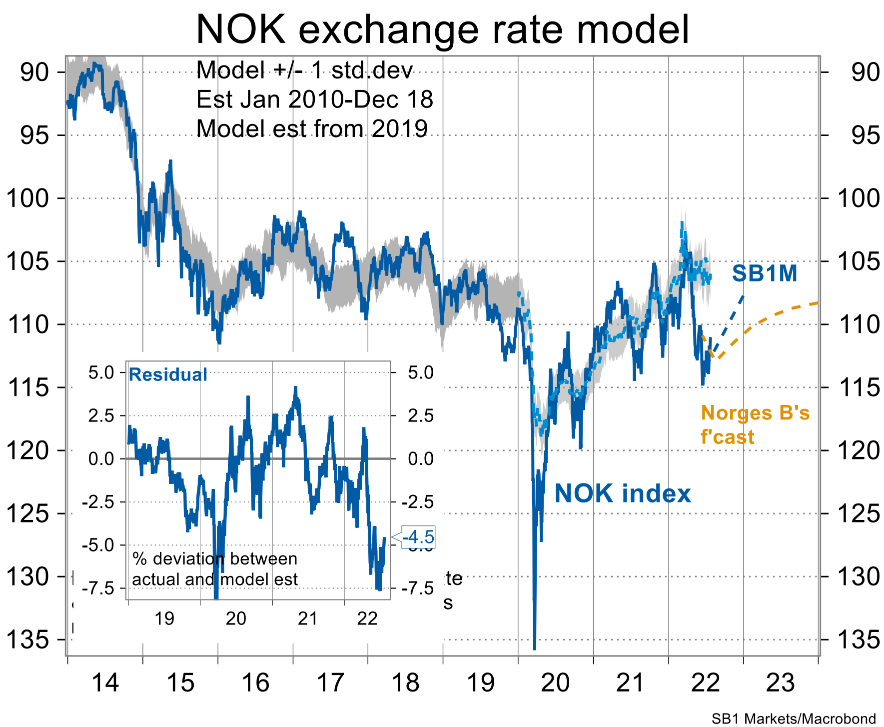
Gaps vs. out model estimates are extremely wide

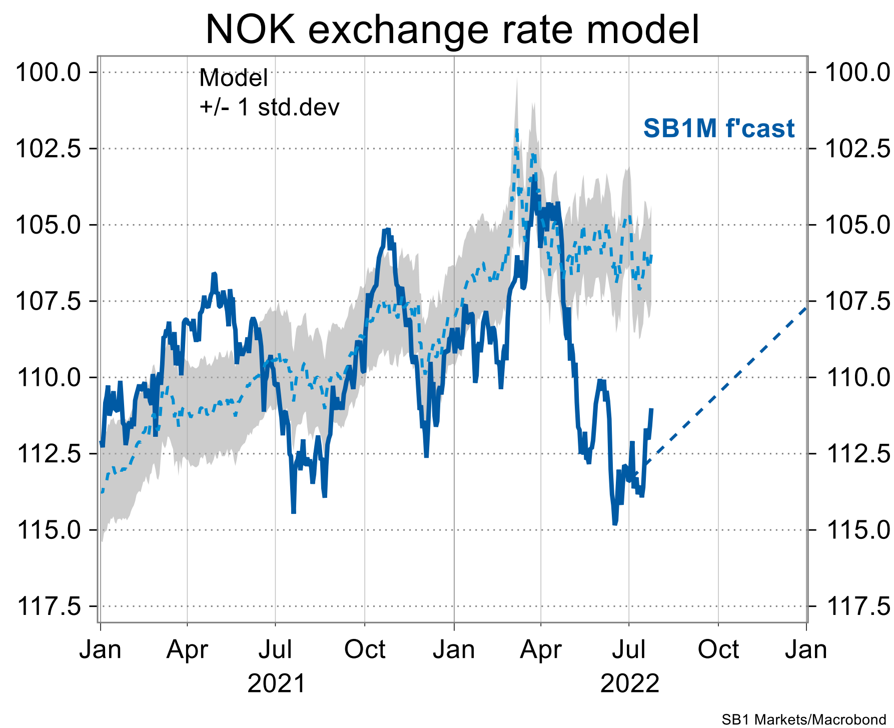
- ***The NOK +1.5%, our main model said -0.9% - and NOK is 4.5% below our main model estimate (from –6.9%)***
- The NOK is 9% weaker than our AUD/CAD/SEK-model, our 'super-cycle peers', predicts (from 10)
- NOK is 2.5% weaker than a model which includes global energy companies equity prices (vs the global stock market) (from 4)

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 is 4.5% below our model est – but finally above our (early July) f'cast

The NOK has recovered somewhat but is still weak vs the oil price/our models





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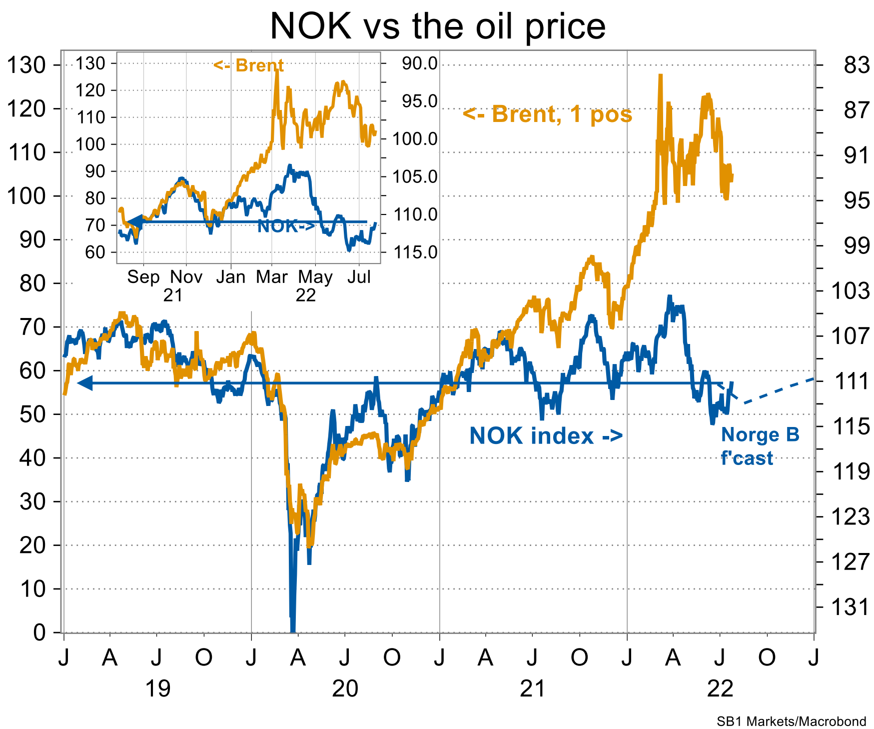
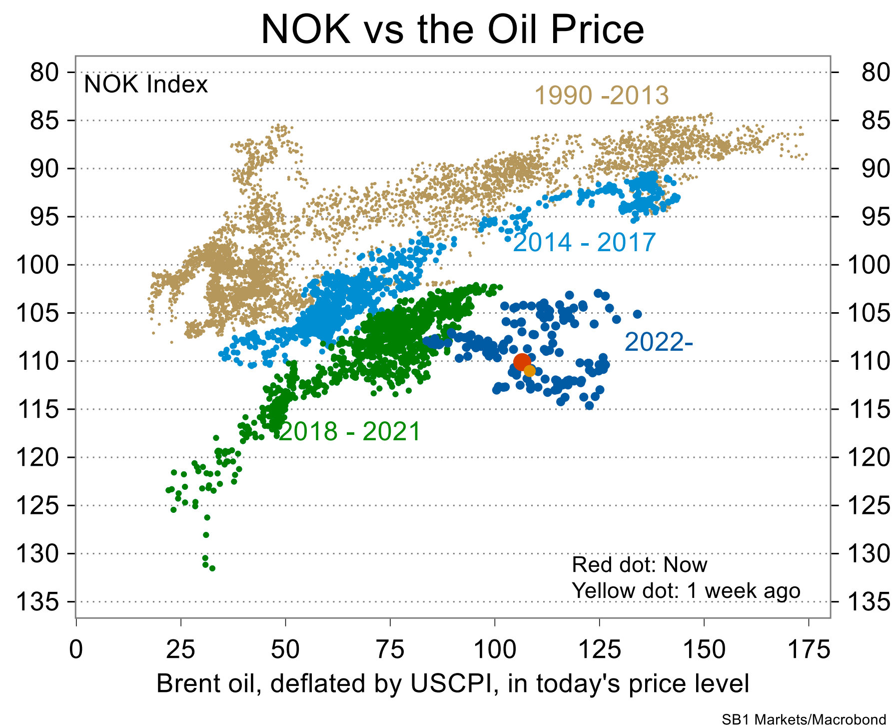
Oil slightly down last week, NOK up 1.5%, Still the NOK is weak vs oil

.. as if the oil price was USD 70/b (rebased to early Jan) or USD 55/b (rebased to May-21)

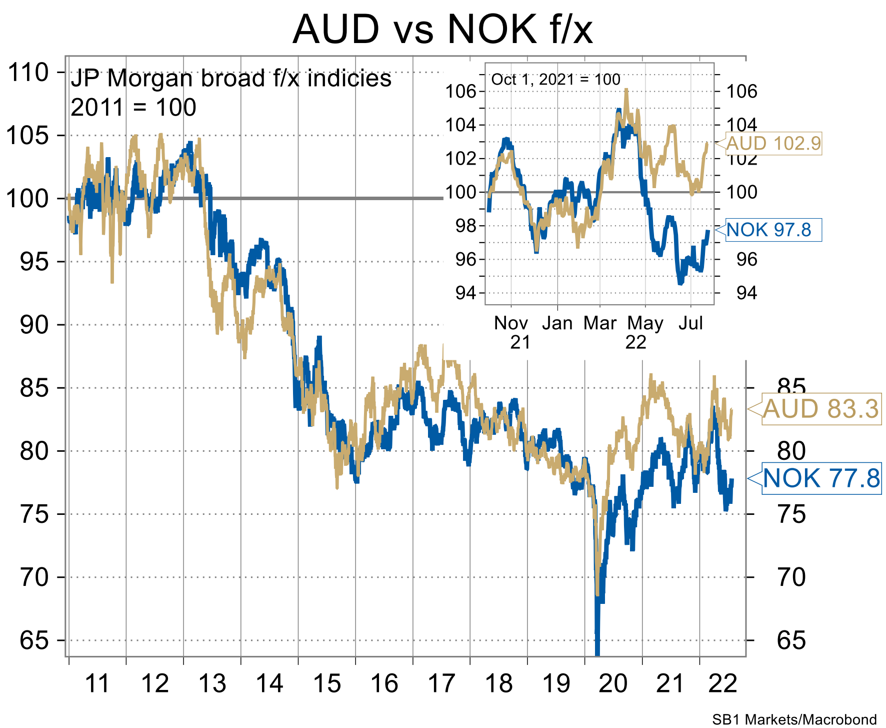


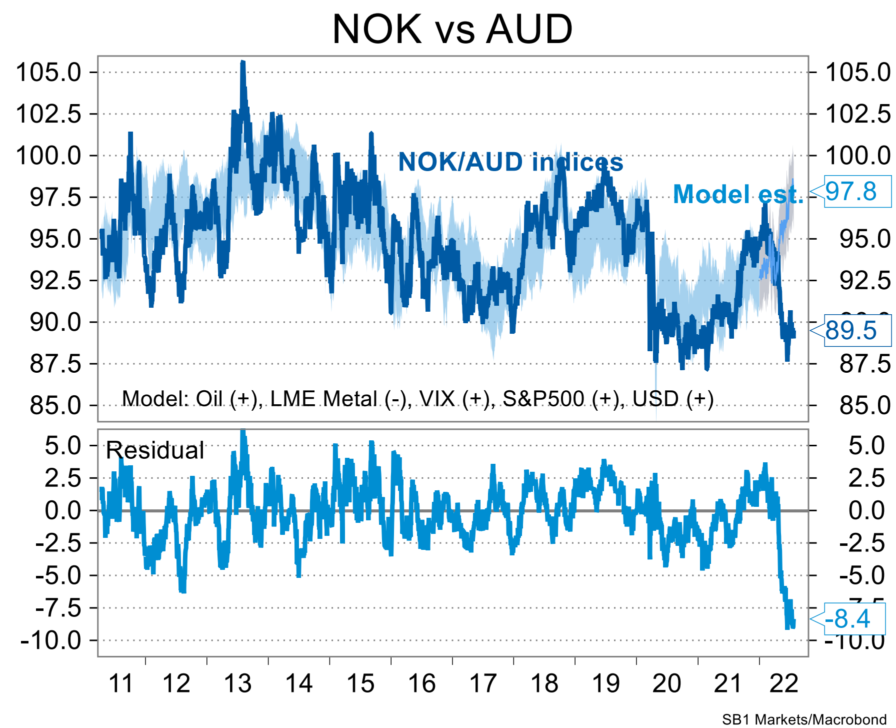


- The NOK has never before been as weak as the recent weeks, given the oil price

AUD and NOK up last week too – but NOK is too weak vs. the AUD?

The gap is now among the largest, even if metal prices have been falling for a while, oil & gas not

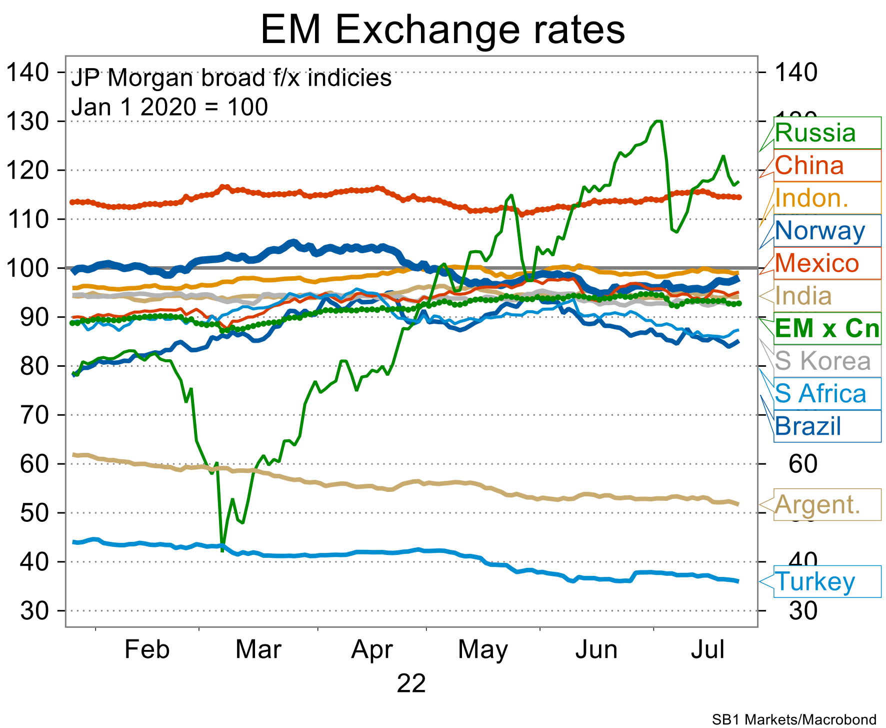


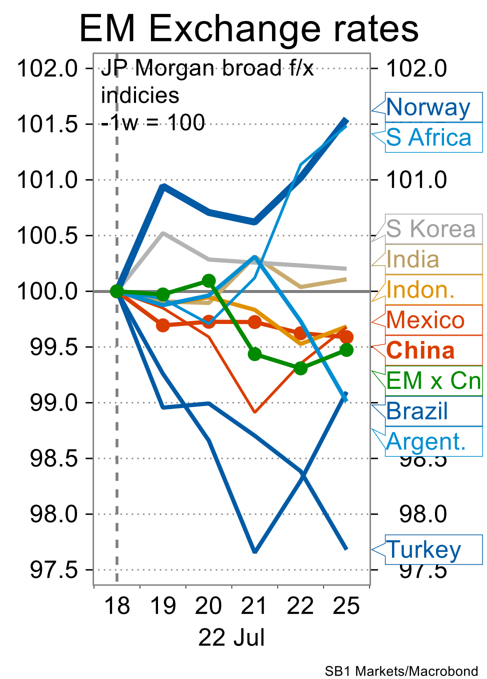


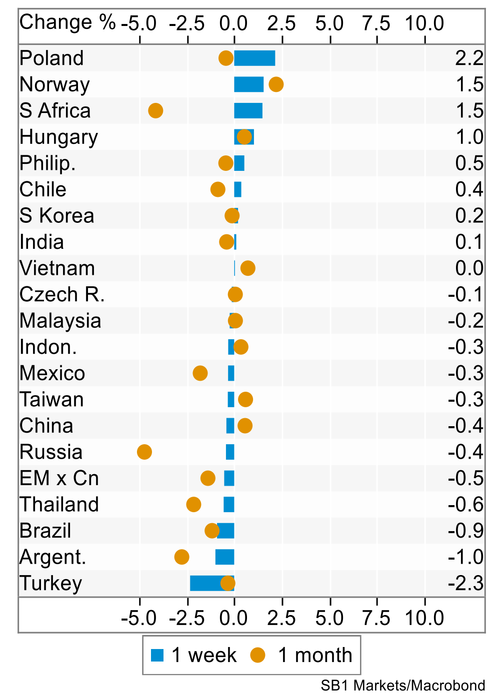
- The discrepancy between the NOK and AUD is highly unusual, given the normal factors that decide the limited gap
- Normally, NOK strengthens vs the AUD when the oil prices rises vs. the LME metal index, when VIX, and the S&P500 index increases, and the USD index appreciates. Seem like we need a new model. Until we find it, buy the NOK index (and short the AUD index)

EM f/x mixed: More down than up last week

But the EM space has not been weak in aggregate recent months, even if rich countries are hiking rates







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