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Macro Weekly

Week 40

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Last week, I

- **The War/European Energy/Commodities**
  - **Russia** has annexed 15% of Ukraine's land, which it is just partially holding – and still losing parts of it to the Ukrainian army. Ukraine is not willing to negotiate. Putin's position has clearly weakened recent weeks both on the ground in Ukraine, domestically and internationally. The risk for desperate actions has increased
  - **The sabotage against the two Nord Stream gas pipelines** in the Baltic Sea may represent a treat of escalation, at least if the Russians are responsible – which so far is not proven. Are other pipelines exposed??
  - **Gas prices** rose on the news of the sabotage but ended the week flattish, at least for the coming 12 months on average. This week, **Opec+** will meet and probably decide production cuts to bolster oil prices. Not really what the world economy needs now
  - **Commodity prices** mostly fell last week, but some metals were supported by discussions on sanctions on Russian metal exports
- **China PMIs**
  - **The NBS 'official' PMI** fell due to a weak service sector print, while the **Caixin manufacturing PMI** fell sharply. In sum, growth below par is signalled (but Caixin service sector PMI is not yet published)
- **USA**
  - **New home** sales rose sharply, and unexpectedly, in August – but the trend is down, and the **inventory of homes for sale** is climbing rapidly. **New home prices** have flattened recent months. The **'official' existing home price indices** (Case/Shiller & FHA) both unexpectedly reported a decline in July, and history was revised down. Mortgage rates exploded last week, to above 7%. We expect home prices to fall sharply the coming months, following the 40%+ lift through the pandemic
  - **PCE inflation** was revised up and rose more than expected m/m in August, the core by 0.6%, one of the highest on record. Still, peak inflation is probably behind us, but underlying inflation is high and broad
  - **Consumption** rose 0.1% in real terms in August, as expected, but growth in July was revised down (even if the level was revised up as a part of the annual GDP revision). Income grew 0.1% in real terms, as expected. The saving rate was unchanged, but July was revised down by 1.5 pp to 3.5%, to 4 pp below the pre-pandemic level – a rather low level as excess savings through the pandemic now funds 'expensive' consumption
  - **Conference Board's consumer confidence** index rose in September, to 0.5 st.dev above average. Inflation expectations are on the way down, as in all other surveys – and market expectations
  - **Durable goods orders** are still heading upwards, and are far stronger than signalled by manufacturing surveys
  - The **annual GDP revision** revealed that growth was been higher since before the pandemic, and GDP is up 3.5% vs Q4-19, revised from 2.5%. Almost all of the adjustment was due to higher service sector production, and higher private consumption. Business investments were weaker. The savings rate was revised down by 1.5 pp – to 3.5% now. Unit labour cost inflation was revised marginally down, which is just fine for the Federal Reserve – but it is still far too high

Last week, II

- **UK**
  - » The **Bank of England** had to intervene in the gilt market on Wednesday to prevent government bond yields to run completely out of control, which would have created huge problems for the pension funds' positions in derivative markets. The bank promised to do whatever needed to keep yields in check – while the long-term strategy still is to reduce its bond holdings. Still, long bond yields/swap rates ended the week up, and we have never seen such an increase in rates since the early 80s – and bond prices have never before fallen as much as over the past two (or 8) weeks. The GBP also gyrated wildly, and ended the week up following a larger decline the previous week. Such market volatility is not good news
  - » The very **expansionary fiscal policy** suggested by the Truss government is of course at odds with the BoE's ambitions to get inflation down by dampening demand. Still, we think market expectations for a close to 6% bank rate is far too aggressive on the top of the unprecedented decline in real income due to the surge in inflation. UK households mortgages have a rather short duration. The only risk on the upside for interest rates: A full breakdown in the currency (and in the UK political system)
- **EMU**
  - » **CPI inflation** rose more than expected in September, the headline up to 10.0%, and the core to 4.8%. We repeat that labour cost inflation remains reasonable in check, even after adjusting for slow underlying growth in productivity. The contrast to the US is substantial. Whether the ECB recognises that, is uncertain. The main longer term risk: A wage-price spiral if unions should try to recover the loss in real income
  - » **Unemployment** was unchanged at 6.6%, the lowest level since 1981 but the monthly decline in approaching the zero line
  - » **Business sentiment** fell in September but remains <u>above</u> average, according to the EU survey. The German Ifo survey was far weaker, especially the expectation component
- **Sweden**
  - » **Retail sales** fell in further in August, and is now below the pre-pandemic trend
  - » **Business sentiment** fell to 0.9 st.dev below average in September, signalling zero GDP growth. In May, the survey sent a 5% GDP growth signal…
  - » **Consumer confidence** fell further in September, to another ATL
- **Norway**
  - » **Retail sales** rose in August, but the trend is downwards, and total consumption of goods (ex electricity) is below the pre-pandemic trend. If not for high inflation and loss of buying power and rapidly increasing interest rates, the downside risk would have been limited. Now parts of retail sales are still exposed the coming months/quarters
  - » **NAV unemployment** fell just marginally in September, as we expected, but August was slightly revised upwards, and the level was marginally above expectations. The rate stands at 1.6% as expected, which may well may become be the bottom in the cycle. The inflow of new vacancies is on the way down but remains at a very high level, and the labour shortage index in Norges Bank's Regional Network just fell marginally from a very high level
  - » **Opinion's CCI** consumer survey fell further in September, to another ATL
  - » The **NOK** fell sharply Friday as Norges Bank surprised the market by lifting the amount of f/x buying for the Oil fund, from NOK 3.5 bn/day in Sept, to 4.3 bn in Oct. In the FRA market expectations of aggressive hikes are calming down but they still remain too high, we think

The Calendar: PMI/ISM, US labour market; The 2023 budget, home prices & GDP here

Time	Count.	Indicator	Period	Forecast	Prior
Monday August 3					
08:30	SW	PMI Manufacturing	Sep		50.6
10:00	EA	PMI Manufacturing	Sep F	48.5	48.5
10:00	NO	PMI Manufacturing	Sep		52.3
15:45	US	PMI Manufacturing	Sep F	51.8	51.8
16:00	US	Construction Spending MoM	Aug	-0.2%	-0.4%
16:00	**US**	**Manufacturing ISM**	**Sep**	**52.3**	**52.8**
17:00	WO	PMI Manufacturing	Sep	49.7	50.3
	US	Auto sales	Sep	13.50m	13.18m
Tuesday August 4					
11:00	EA	PPI YoY	Aug	43.2%	37.9%
16:00	**US**	**JOLTS Job Openings**	**Aug**		**11239k**
Wednesday August 5					
08:30	SW	PMI Services	Sep		59.4
08:45	FR	Manufacturing Production MoM	Aug		-1.6%
10:00	EA	PMI Services	Sep F	48.9	48.9
10:00	EA	PMI Composite	Sep F	48.2	48.2
11:00	**NO**	**Home prices**	**Sep**	**-0.5%**	**0.6%**
14:15	US	ADP Employment Change	Sep	205k	132k
14:30	US	Trade Balance	Aug	-$68.1b	-$70.7b
15:45	US	PMI Services	Sep F	49.2	49.2
15:45	US	PMI Composite	Sep F	49.3	49.3
16:00	**US**	**ISM Services**	**Sep**	**56.0**	**56.9**
17:00	**WO**	**PMI Composite**	**Sep**	**50.4**	**49.3**
Thursday August 6					
08:00	**NO**	**Budget proposal, key data**	**2023**		
08:00	SW	GDP Indicator SA MoM	Aug		0.0%
10:00	NO	Budget proposal	2023		
11:00	EA	Retail Sales MoM	Aug	-0.4%	0.3%
14:30	US	Initial Jobless Claims	Oct-01	205k	193k
Friday August 7					
06:00	SW	Home prices Maklarstatistik	Sep		
08:00	GE	Industrial production	Aug	-0.5%	-0.3%
08:00	NO	GDP MoM	Aug		0.3%
08:00	**NO**	**GDP Mainland MoM**	**Aug**	**0.4%**	**-0.3%**
08:00	NO	Ind Prod Manufacturing MoM	Aug	-1.0%	1.4%
14:30	**US**	**Change in Nonfarm Payrolls**	**Sep**	**250k**	**315k**
14:30	**US**	**Unemployment Rate**	**Sep**	**3.7%**	**3.7%**
14:30	**US**	**Average Hourly Earnings YoY**	**Sep**	**5.1%**	**5.2%**
14:30	US	Labor Force Participation Rate	Sep	62.4%	62.4%
21:00	US	Consumer Credit	Aug	$250b	$24b
Saturday August 8					
03:45	CN	Caixin China PMI Services	Sep	54.5	55.0

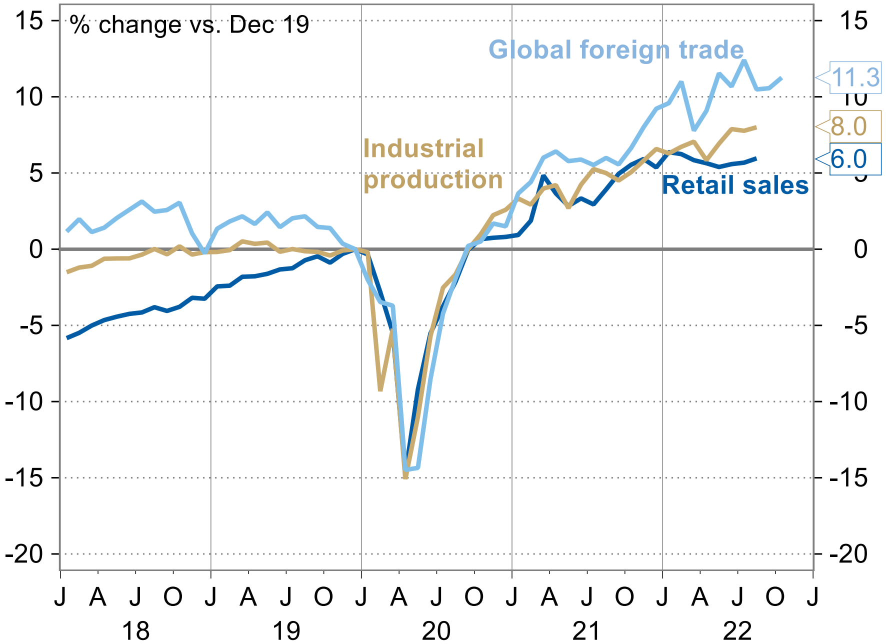
- **September (final) PMIs, ISM**
  - The preliminary PMIs from the rich part of the world together with the Chinese PMI, signal a decline in the global manufacturing PMI to below the 50-line, with both new orders and output sub-indices well below 50. The global service index will recover, almost entirely due to a correction upwards from a strangely low US service sector PMI in August. Emerging markets x China PMIs have so far kept up well, in spite of the steep decline in the PMIs in the rich part of the world. The US ISMs are expected just slightly down. Regional surveys signal a lower ISM level
- **September auto sales**
  - **Global sales** have been impressive past months, mainly due to strong sales in China and in EM x China (and x Russia). **US sales** are expected slightly up
- **USA**
  - We still think the **labour market and wage inflation** is more important than the headline (or even the core) CPI. Employment growth is slowing, and unemployment has probably bottomed. Wage inflation is well above pre-pandemic level (and other surveys report higher growth than in the monthly payrolls report). **Unfilled job openings** is perhaps just as important, as it is very closely correlated to the wage inflation. The **NFIB small business survey** will also report labour shortages and hiring and wage plans
- **EMU**
  - Several countries will report **retail sales** and **industrial production**. August was probably not a strong month – and the impact of energy shortages/high prices will very soon become visible. Still, aggregate EMU surveys do not signal a sharp slowdown, at least not yet. And the unemployment rate is the lowest since the beginning of the 80s
- **Sweden**
  - **GDP** has so far been strong but will probably slow the coming months. August data out this week
  - The first September **home price** indicators that are already published signals sharp price decline, on Friday the first broad index will be published, from the realtors
- **Norway**
  - **National budget:** The Government has promised to deliver a tight budget. We assume a cut in the non-oil structural 2023 budget to 9.7% of Mainland GDP from 10.3% in 2022, that is a 0.5 pp fiscal tightening. The deficit (=transfer from the oil fund) should equal 2.7% of the Oil fund, down from 2.9% in 2022, equalling 1% of GDP less than the long term budget rule ('handlingsregelen'). The risk should be on the downside vs. our estimates. Higher rent based taxes for hydropower electricity generation and new rent taxes for wind farms as well for the fish farming industry will alone cut the budget deficit by almost 1% of GDP. At the expenditure side: Defence, electricity subsidies, Ukraine refugees, and we expect some promises for supporting Ukraine after the war. The overall budget surplus will be enormous, the largest in any rich country ever
  - We expect August **Mainland GDP** data to confirm just a modest upward drift in Mainland GDP
  - **Home prices** surprised at the upside in August but we expect a significant decline in September (or if not then, in October) as the rapid increase in interest rates will dampen demand substantially. The buying power is sharply reduced

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

Retail sales are still soft, manufacturing production recovered still strong

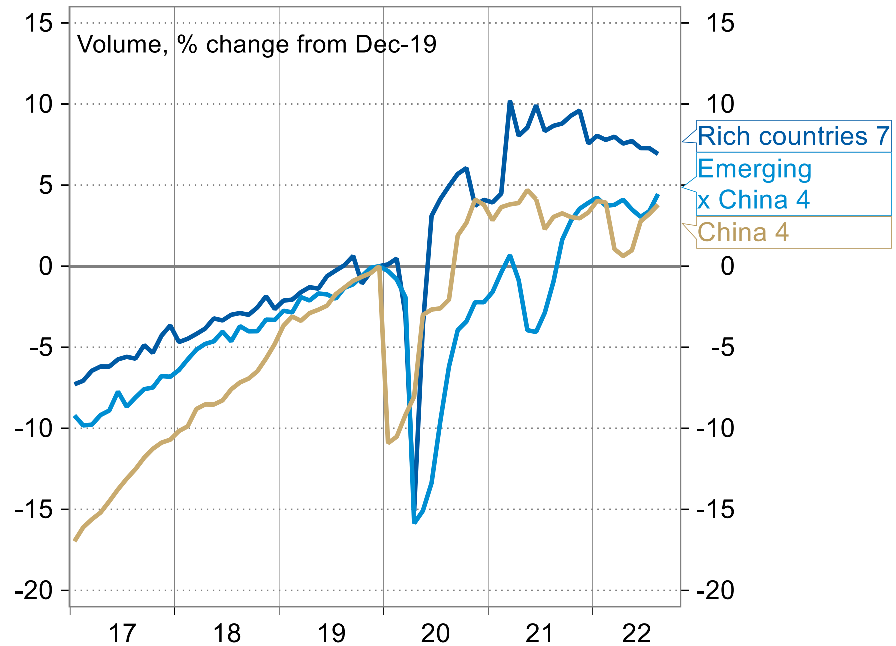
Global foreign trade may have flattened. Both manuf. prod. & trade exposed to lower retail sales

Global Retail sales, industrial prod. & trade



SB1 Markets/Macrobond/CPB

Retail sales



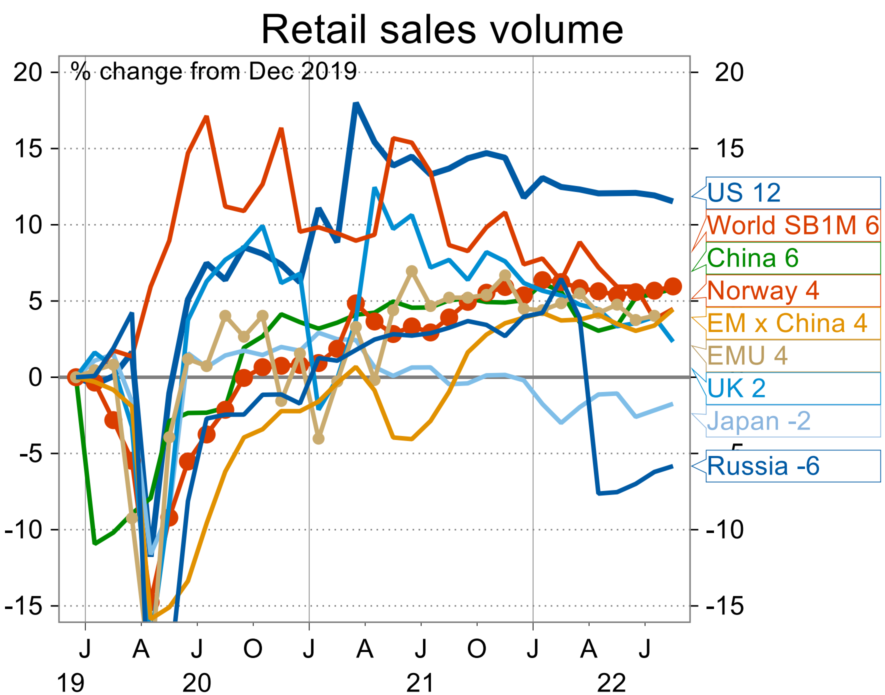
SB1 Markets/Macrobond

Global foreign 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.

SpareBank 1 MARKETS

A broad slowdown of retail sales, at least in the rich part of the world

Is manufacturing exposed? Surveys, like the August PMIs send a warning sign too



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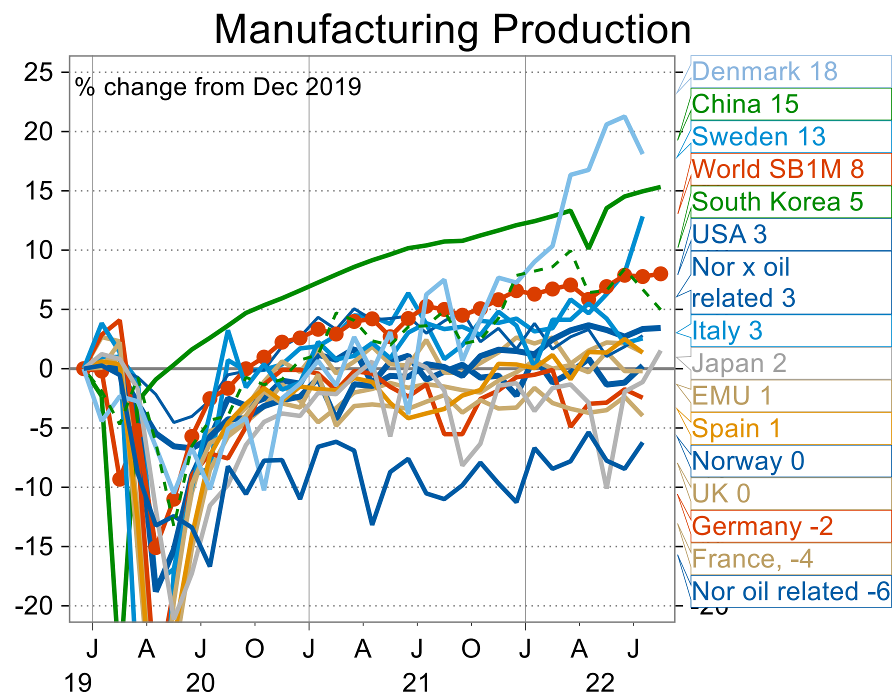

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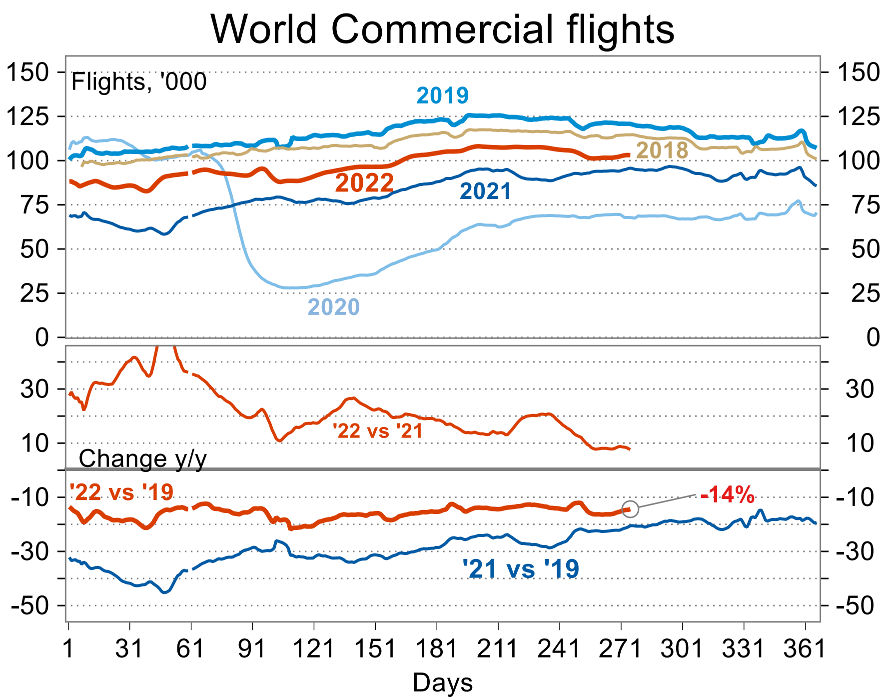
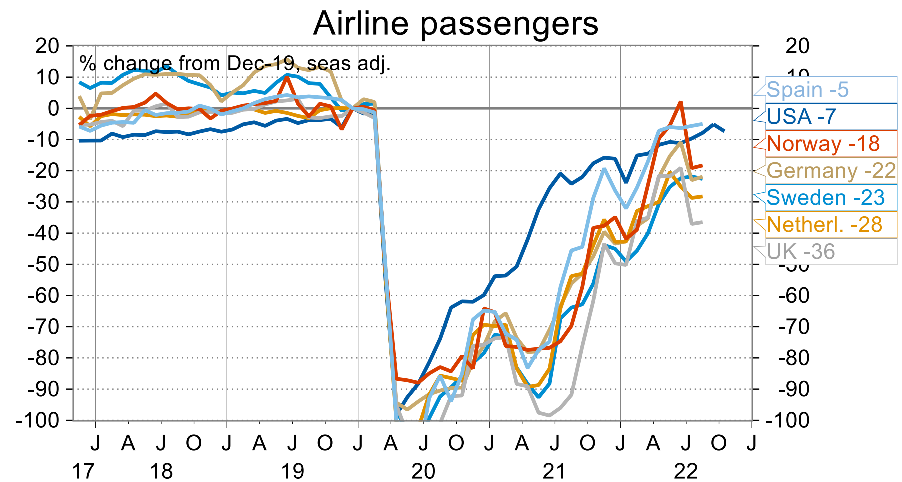
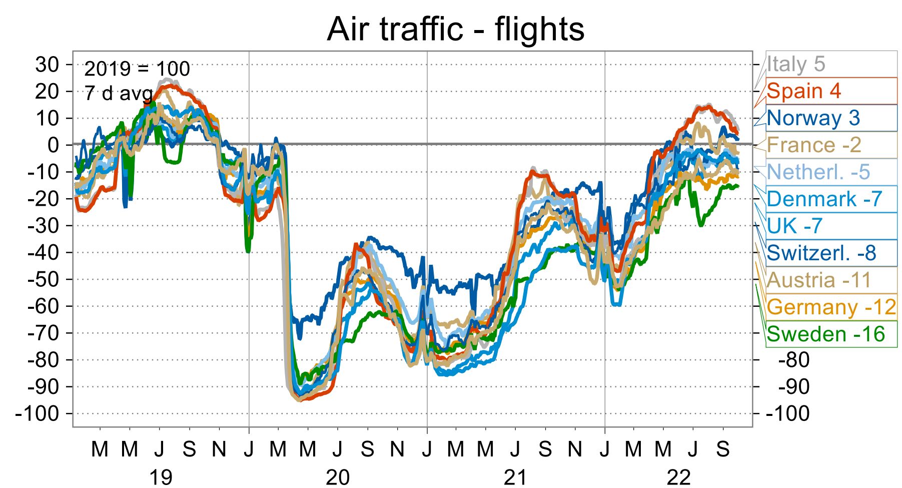
Global airline traffic down slightly up, still down 14% vs. 2019 level



Flightradar24 SB1 Markets/Macrobond



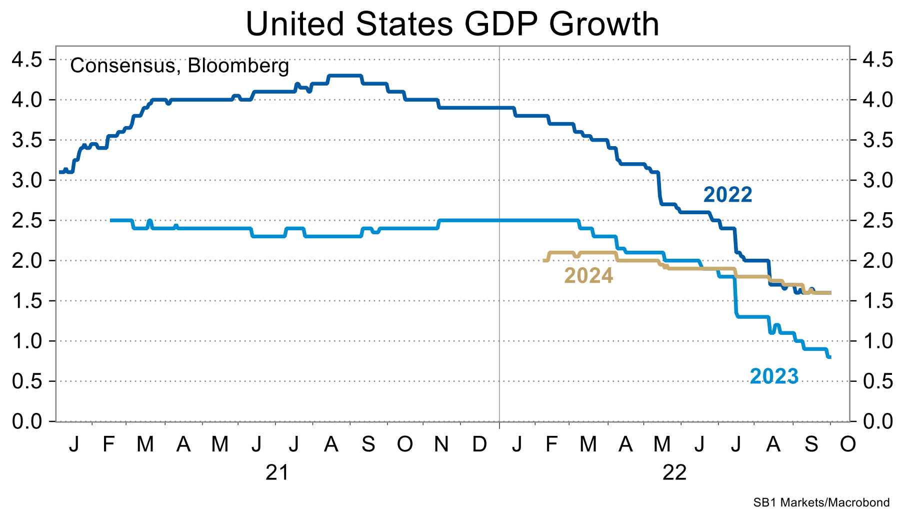
National authorities, SB1 Markets/Macrobond

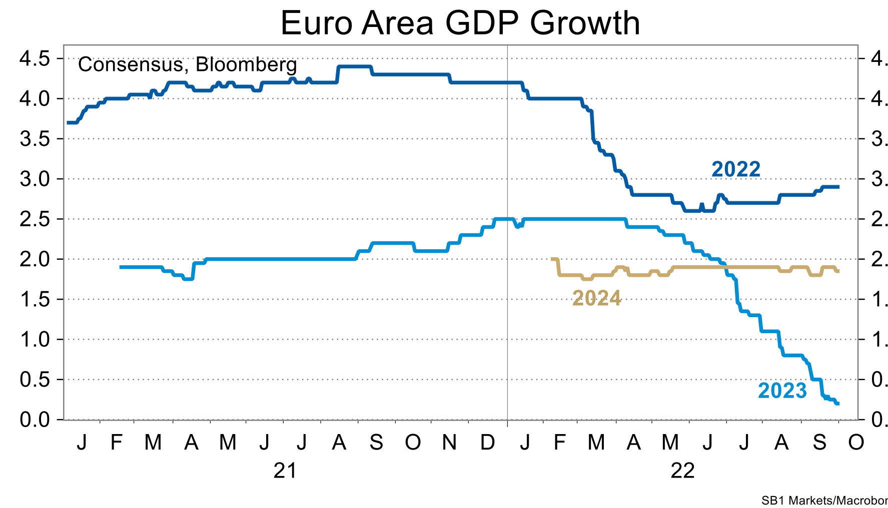


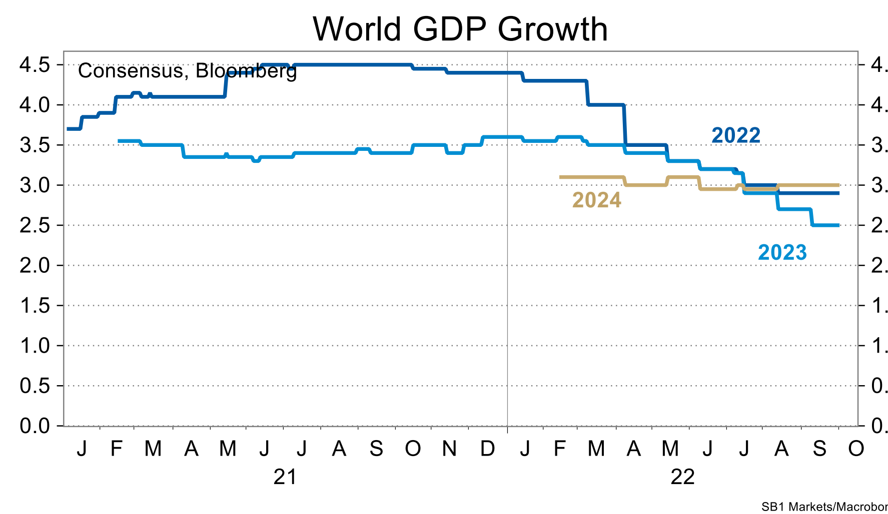
SB1 Markets/Macrobond

Global trade: The last months are estimates from Kiel Institute

GDP growth expectations: 2023 forecasts are sliding down, and fast in the EMU

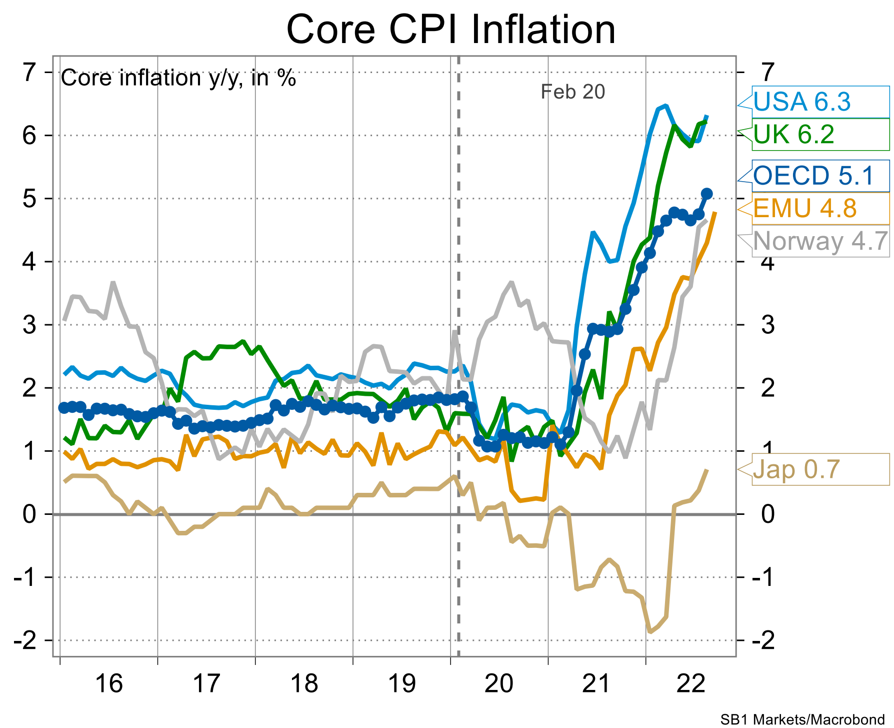


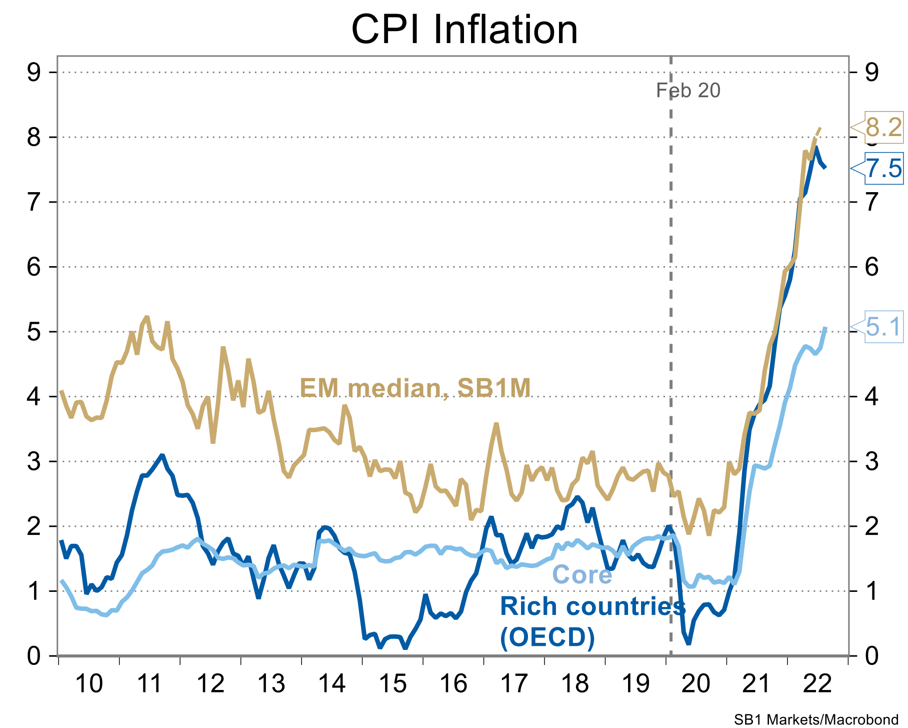




Peak inflation? Data are not that obvious anymore

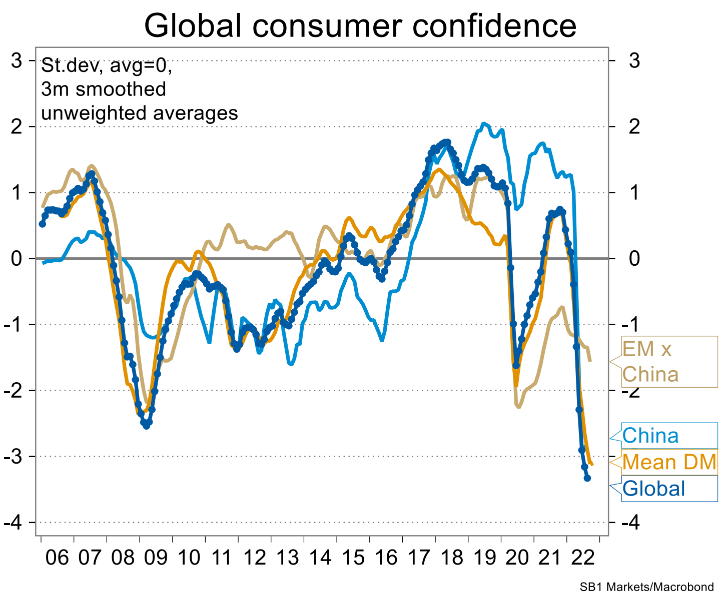
The going rate is 8% headline inflation, and 5% core inflation

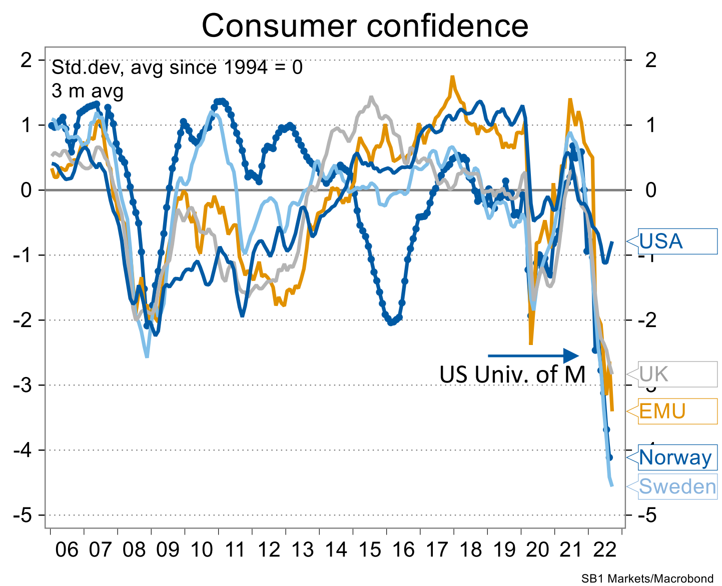




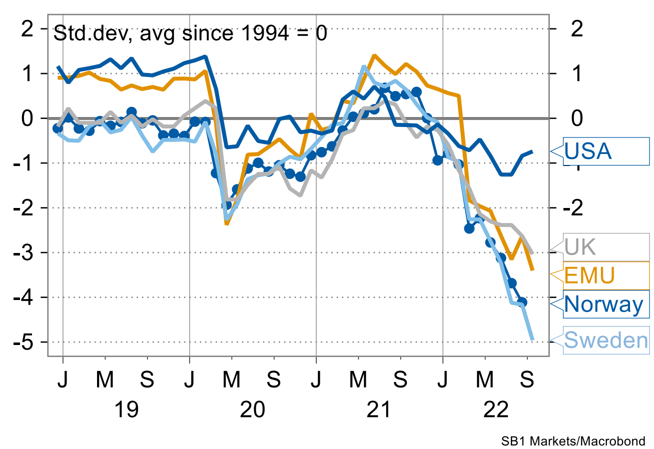
Consumer confidence further down almost everywhere

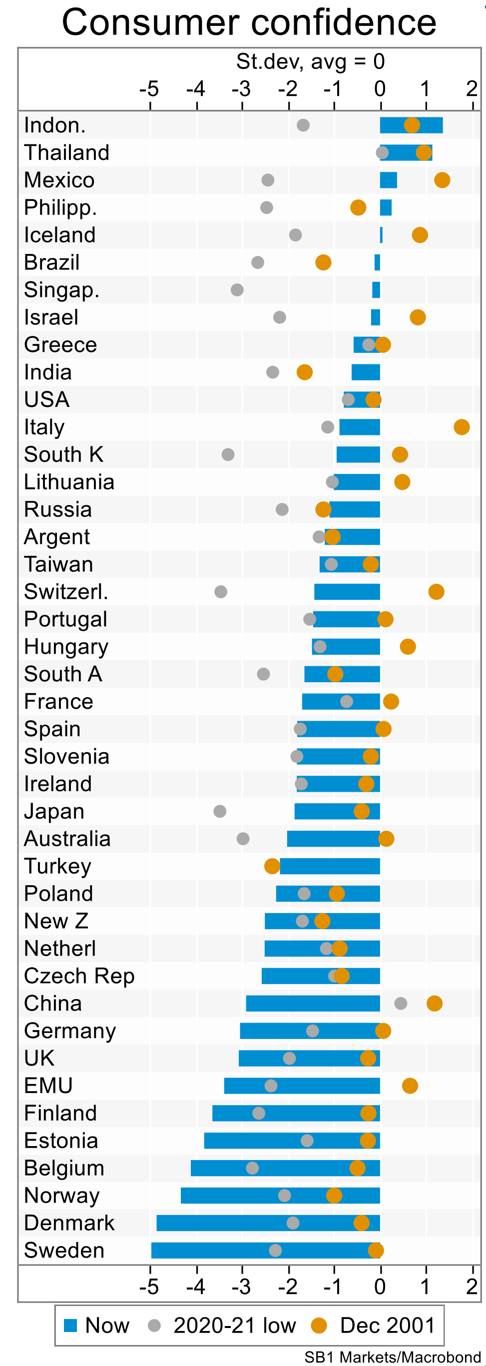
The Nordics at the bottom, rest of Europe close to. US a tad up past 2 m!





- Most countries are reporting a significant lower confidence level than late last year. Just 4 countries are above average, 35 are below, many at ATL
- In most **rich countries** inflation and higher interest rates may to blame, while the collapse in the sentiment in **China** is very likely due the Covid measures (or also the souring housing market?)
- **Emerging markets ex China** has not fallen that much recently, but the level is low

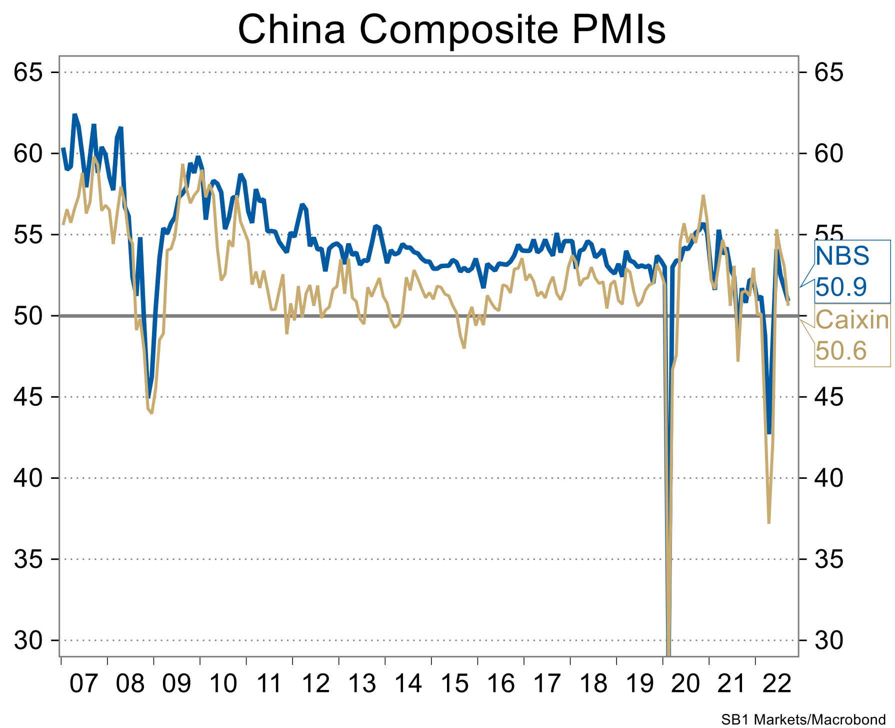


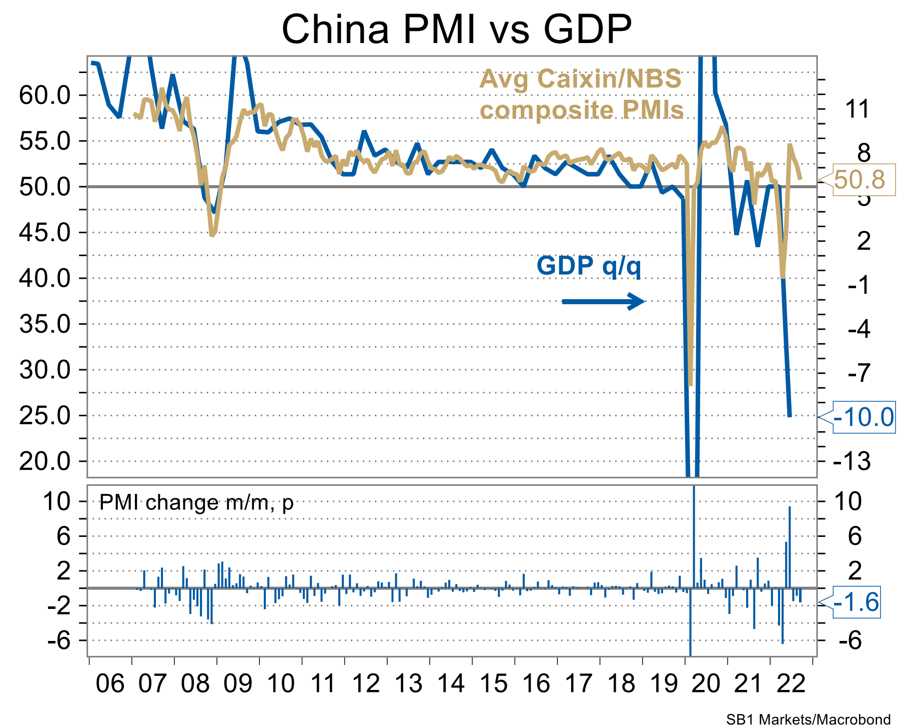


Norway is the average of Finans Norge & Opinion

The NBS PMI down as services slowed, the Caixin manufacturing survey also down

In sum, the PMI reports (probably) signal modest growth in Q3. We think the outcome will be better

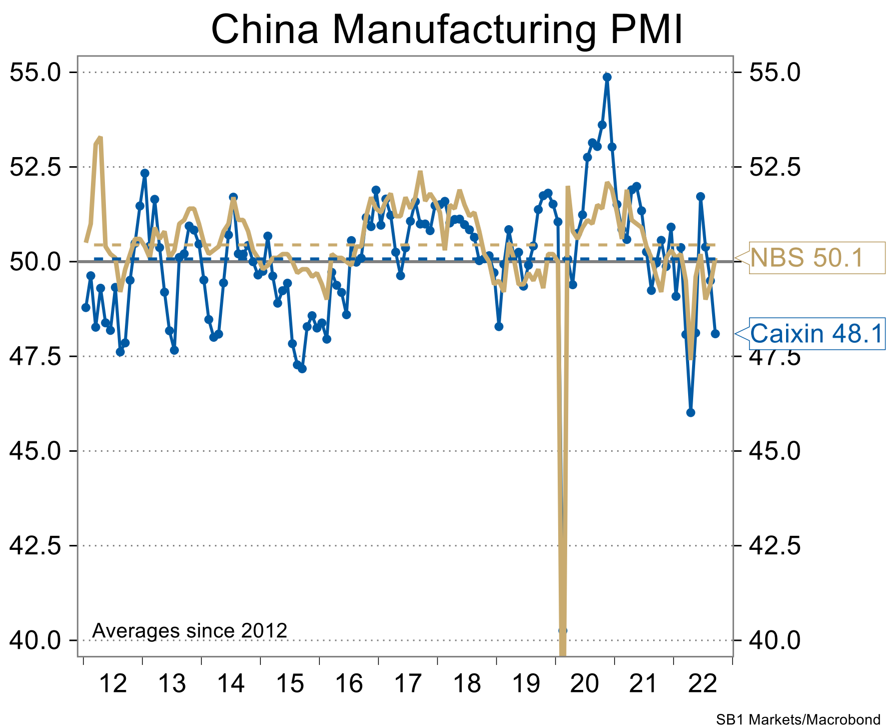


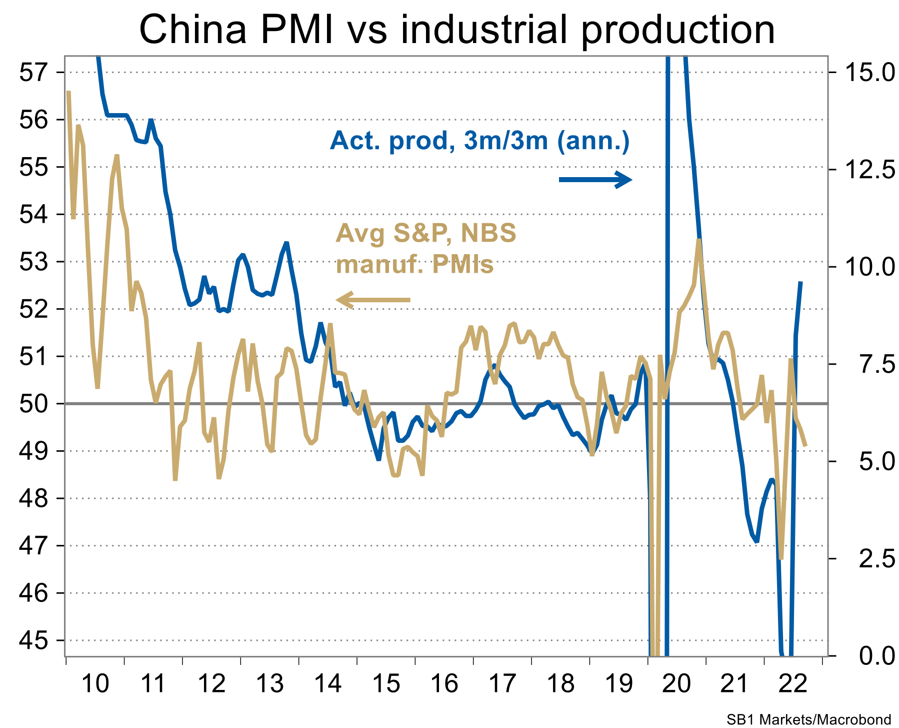


- … following the 10% setback in Q2 (2.6% not annualised), during the lockdowns. The **two PMI data sets** will probably (services data from Caixin is not yet published) signal growth below par, at a level around 50.8
- The **NBS/CFLP composite PMI** fell by 0.5 p to 50.9, expected close to unchanged. The service sector reported a further slowdown to well below trend growth. The manufacturing sector reported higher growth, at almost a normal pace of expansion
- The **Caixin manufacturing index** fell 1.5 to 48.1, expected unchanged. The level is well below par, but since NBS reported a far stronger index, it is hard to draw any conclusions
  - » Caixin has not yet reported its service sector survey, we assume a moderate decline our estimate for the composite index

Caixin's manuf. PMI further into contractionary territory – NBS/CFLP PMI was up

Both are below average and signal growth below trend, but still no decline in production



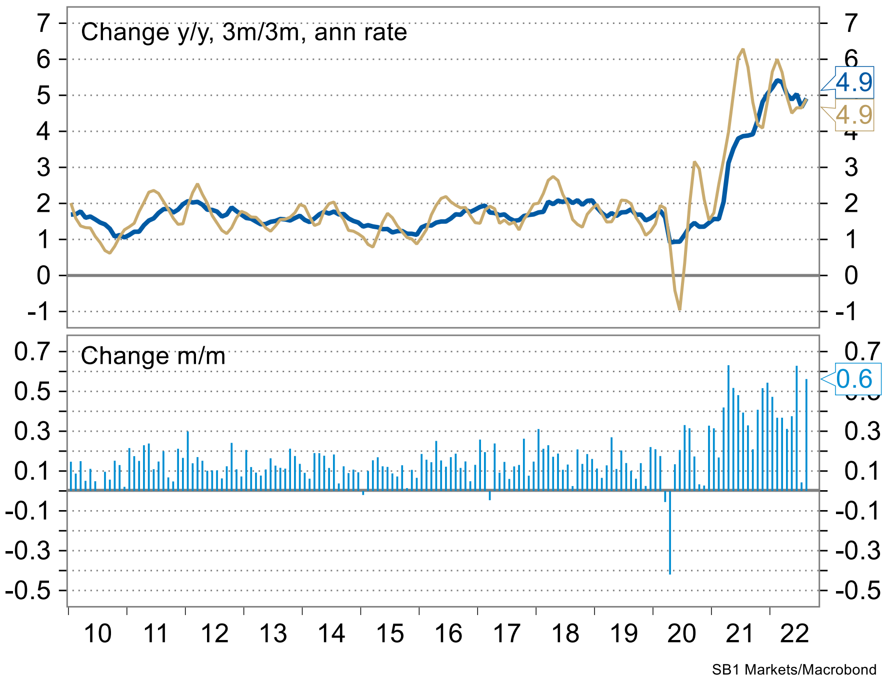


- Actual production rose sharply in May, and further the next three months

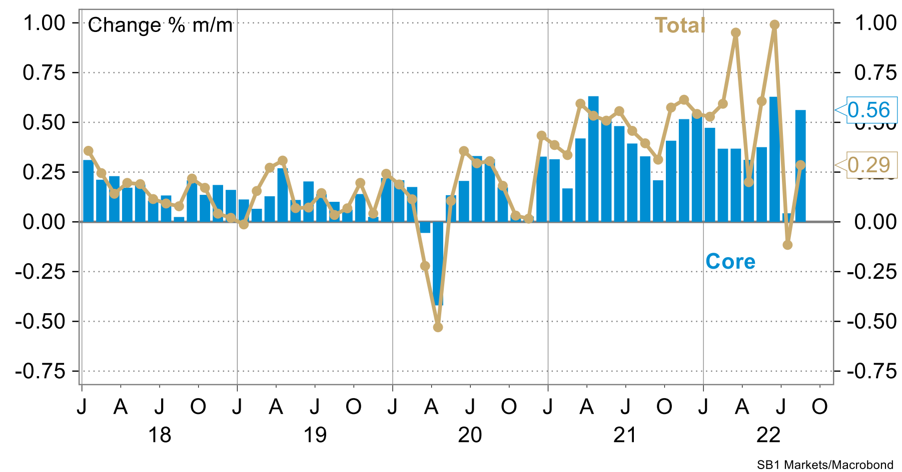
Core inflation revised up m/m – and higher than expected in August

The core PCE deflator rose by 0.6%, and is up 4.9% y/y, 0.1 – 0.2 pp higher than expected

USA Core PCE deflator

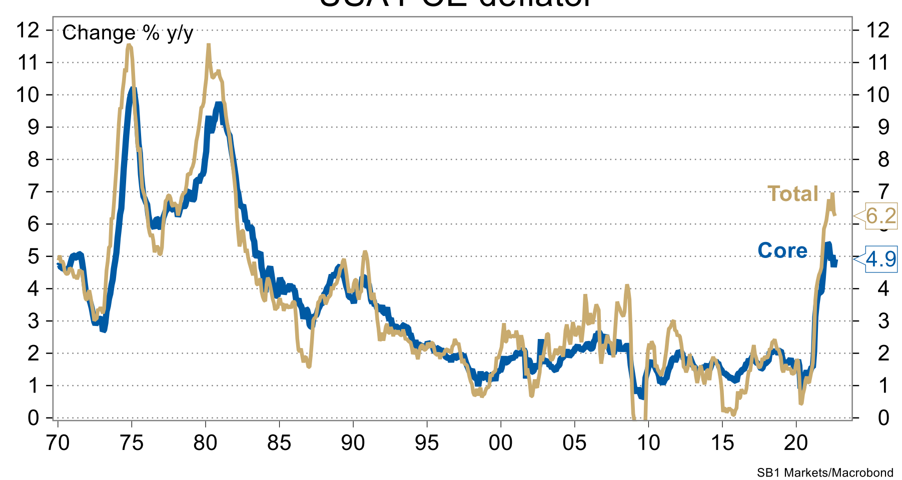


USA PCE deflator



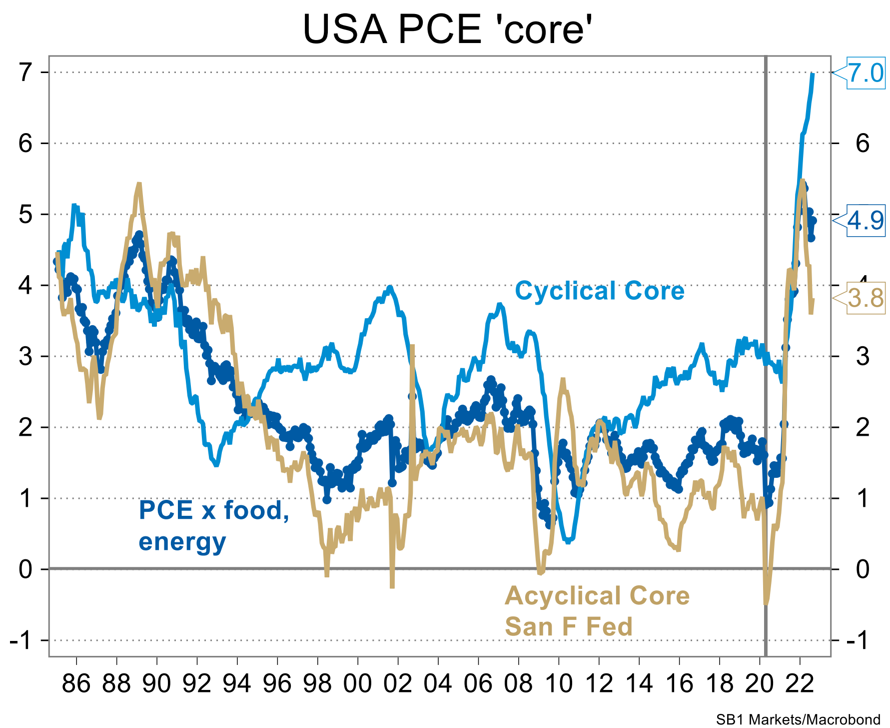
- **The total PCE deflator** also rose more than expected in August, up 0.3% and 6.2% y/y, both 0.2 pp higher than expected

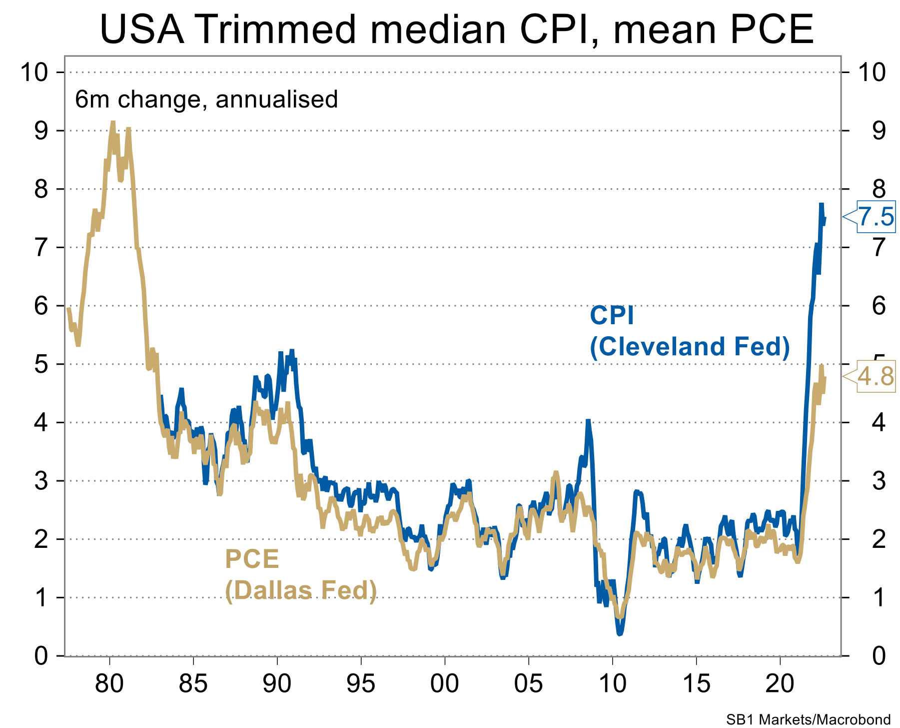
USA PCE deflator



Inflation has peaked but remains high – and broad

A couple of months of ‘better’ data is not going to cut it for the Fed. Anyway, wages are more import.

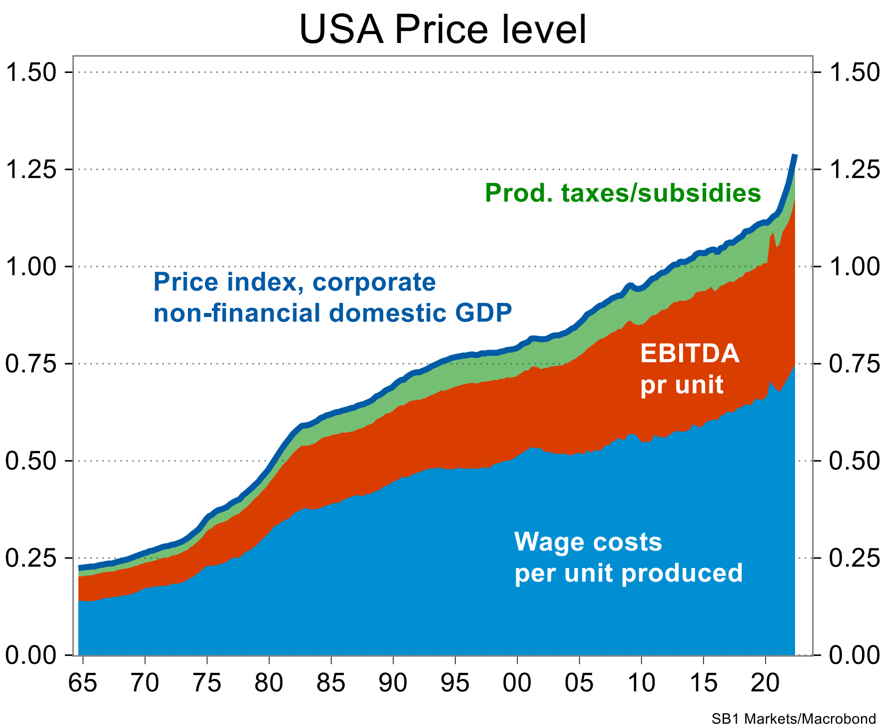


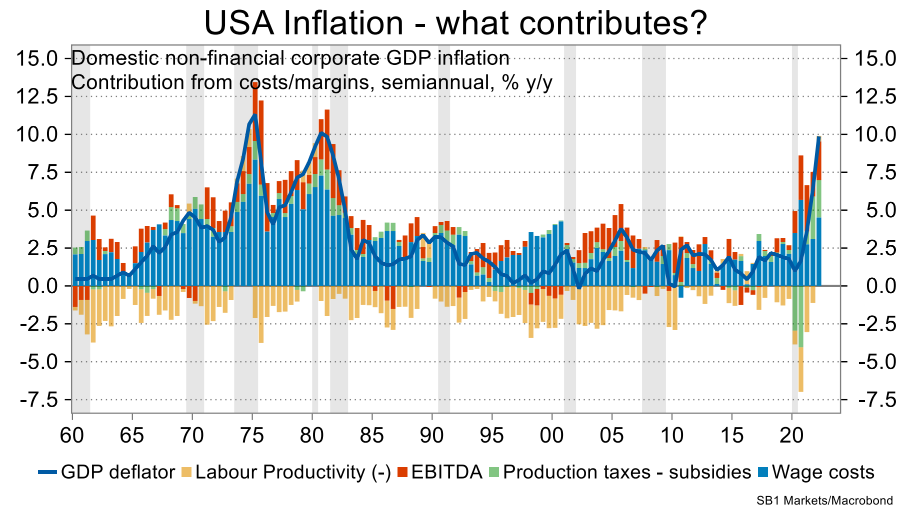


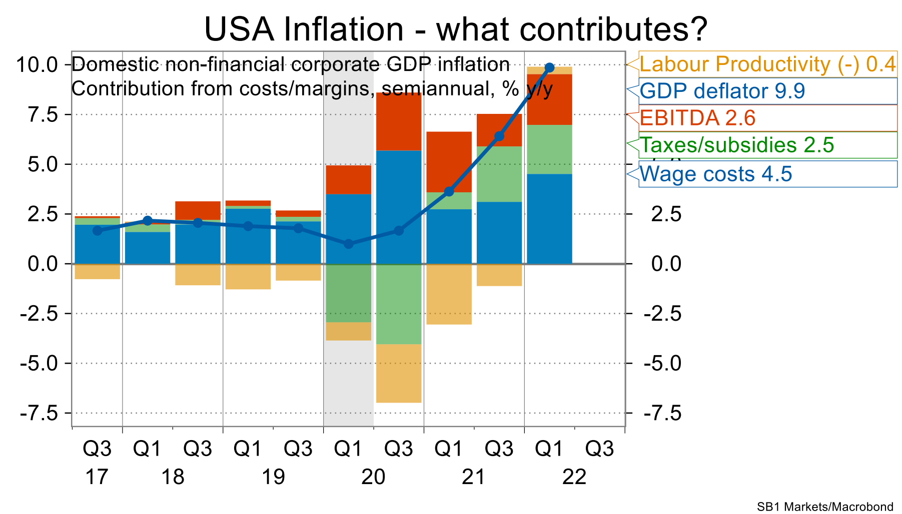
- The **trimmed PCE mean** (Dallas Fed) accelerated 0.5 pp to 4.8% (measured over the past 6 months). The peak was at 6% in June (revised up from 4.8%)
- **The trimmed median CPI (Cleveland Fed)** is up 7.5% over 6 months
- **Core cyclical and acyclical PCE** prices are up 7.0% – 3.8% resp., and the cyclicals are still on the way up
- Other measures of underlying inflation are also still among the highest levels in 30 – 40 years

Margin expansion a main driver for high inflation

Prices are up 10% for goods/services produced in US businesses. Higher margins explains ¼



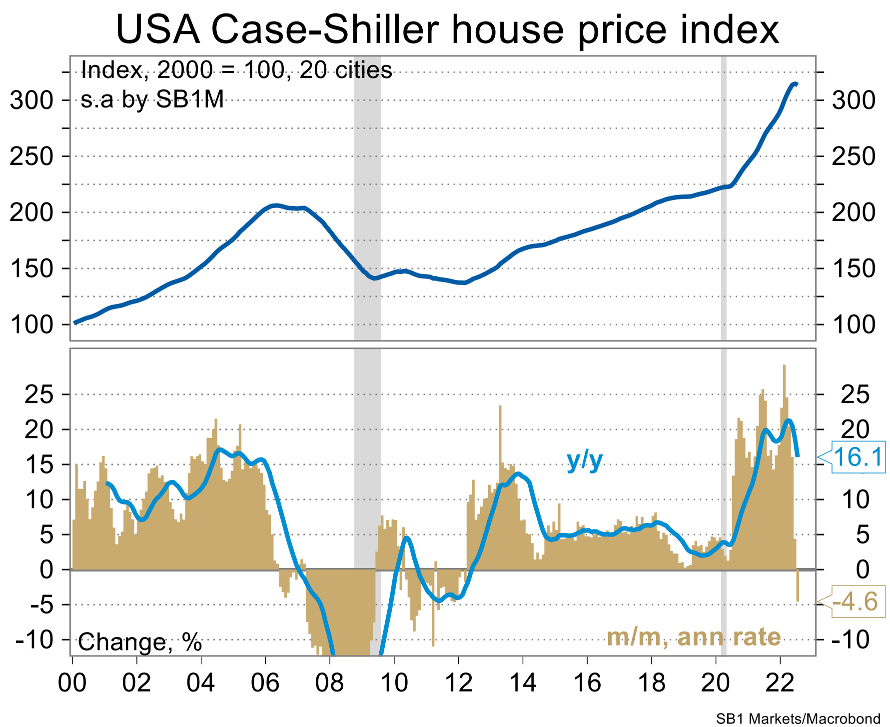


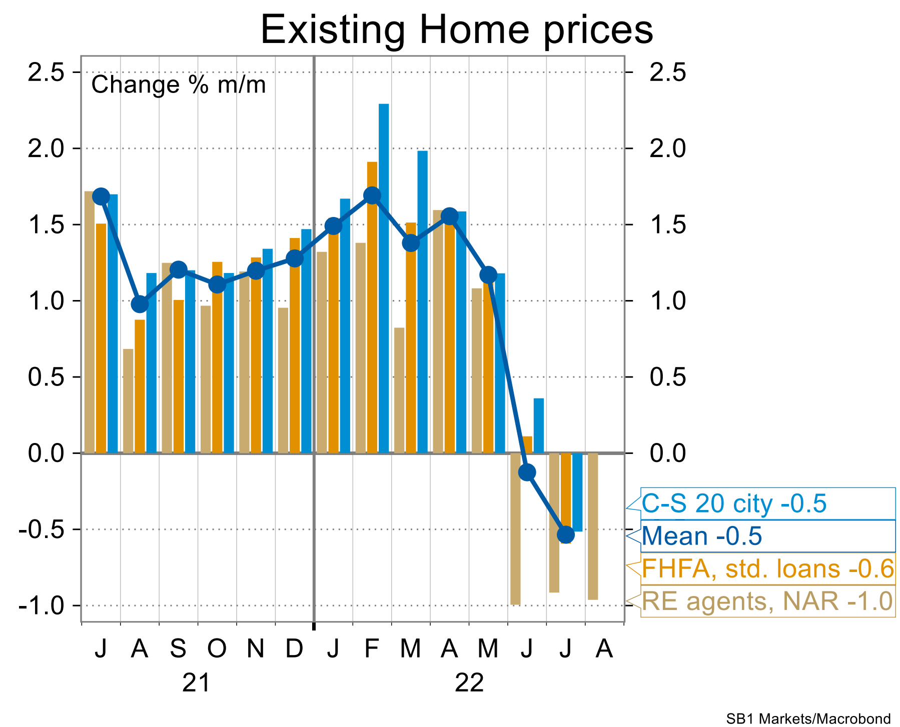


- The main contributor is – as it should be – higher wage costs. However, the 4.5% contribution due to higher wages is far more than what is sustainable vs the 2% price target. In addition productivity has fallen y/y, pushing Unit Labour Costs further up. Net taxes/subsidies are also up as covid support programs are scaled back (but as profits rose when they are distributed, it would not have been surprising if profits were normalised when they were abolished – but profits rose further

Now it is 'official': *House prices are falling*, as the realtors have told us

Case/Shiller reported a 'surprising' 0.5% fall in prices in July



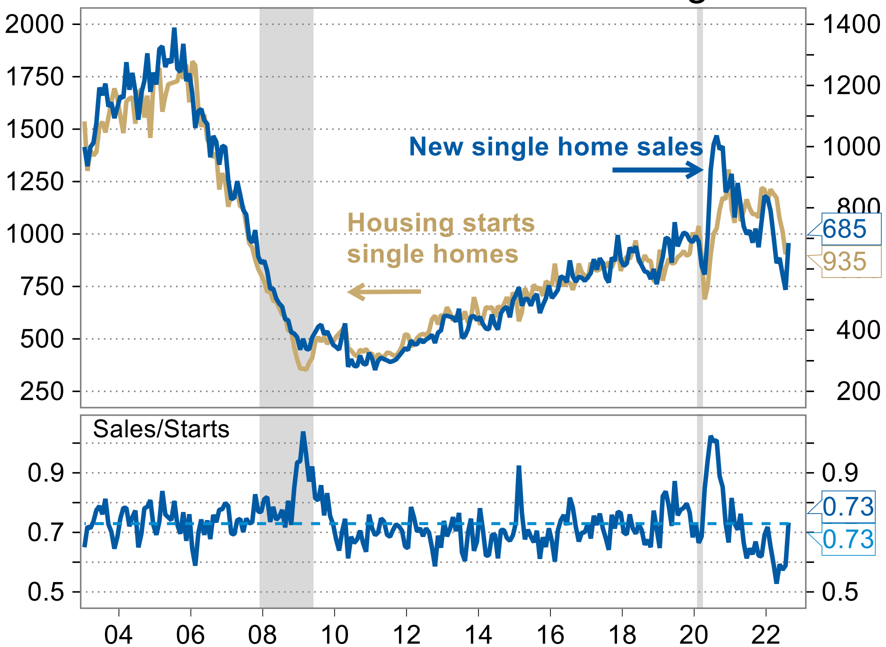


- **S&P's Case/Shiller's 20 cities** price index fell by 0.4% m/m in July (June - Aug avg., our seas. adj, 0.5% by the 'official' seasonal adjustment) equalling a -4.6% annualised pace – A 0.2% increase was expected. Thus, the outcome was 0.7 pp lower than expected, for the 3-month average. Something must have happened in the last month! The index is still up 16.1% - down from 18.6% in June, and 1 pp lower than expected!
- **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), was down 0.6% in July, and is up close to 14% y/y
- **Realtors** reported a 1% decline in August, following a 0.9% drop in July and 1% drop in June. Prices are still up 7.9% y/y– but the annual rate is now 'collapsing'
- We still expect prices to yield substantially the coming months, following the unprecedented 40% lift since before the pandemic, and the surge in mortgage rates, up to 6.5% (30 y fixed), from 4% before the pandemic

New home sales suddenly up almost 30% - but very likely just a one-off

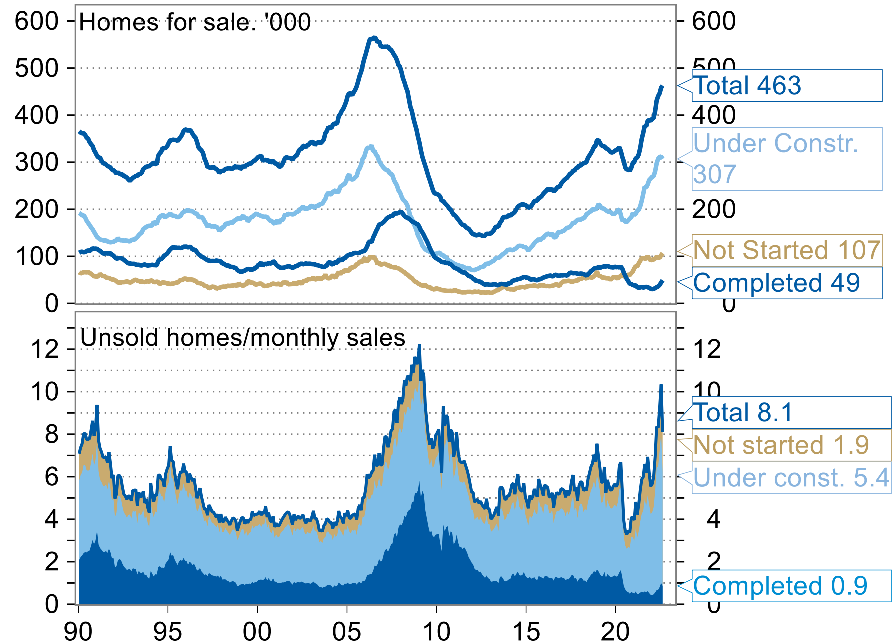
Sales are trending rapidly down and homebuilders have reported further decline in sales

USA New home sales and housing starts



SB1 Markets/Macrobond

USA New Homes for sales

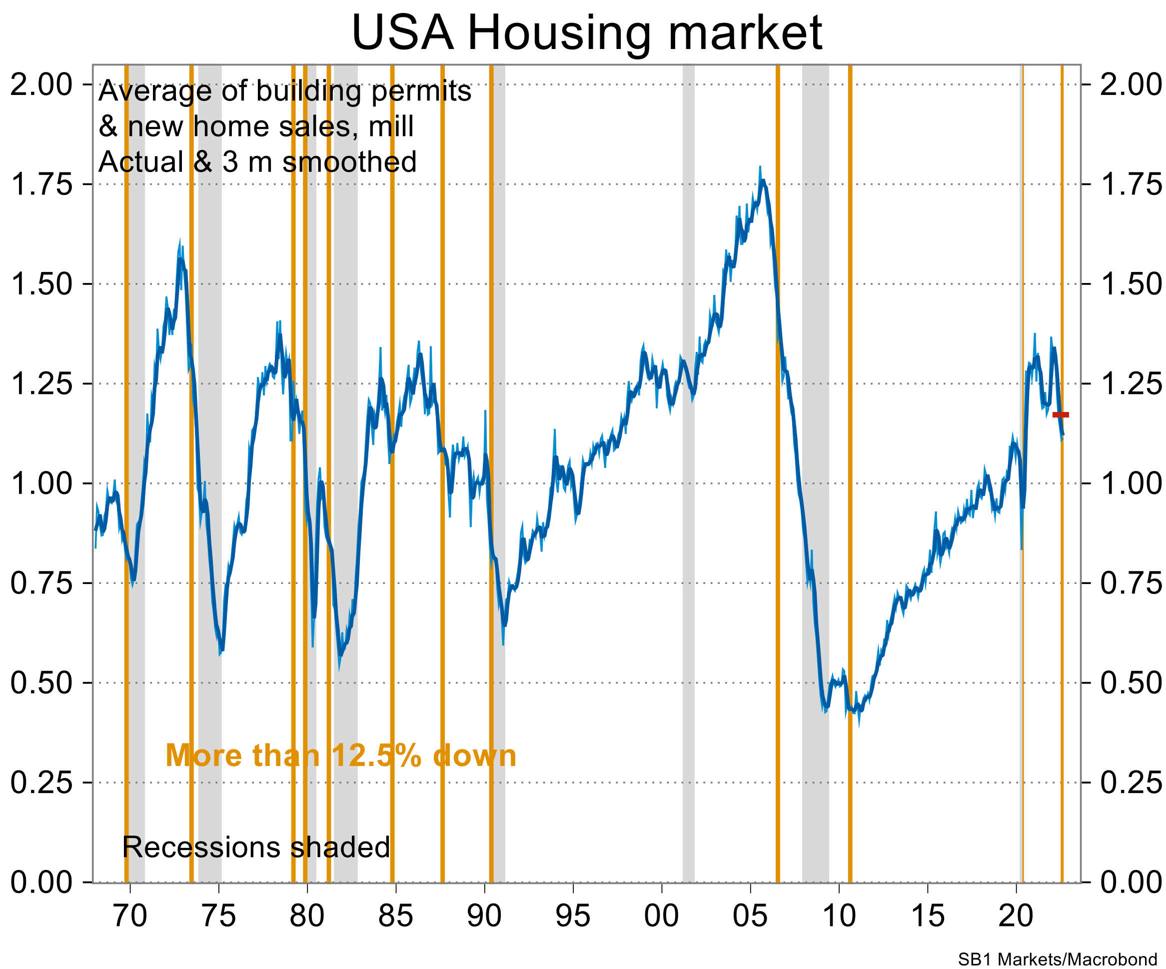


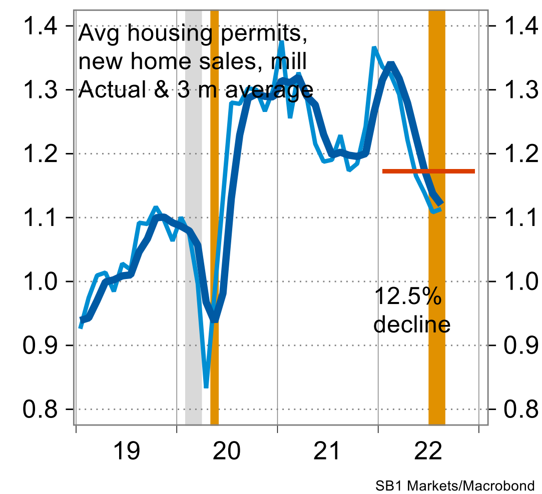
SB1 Markets/Macrobond

- **New single home sales** shot up 685' August, from 532' in July, expected down to 500' from previously reported 511' (annual rate). Even if sales surprised sharply on the upside, the decline the previous months with the setback in building permits sends a clear recession signal (*check 2 pages forward*)
- **The inventory of unsold homes** rose further in August to 463' units, up from below 300' in Aug-20. Measured in month's of sales, inventories equal 8.1 months, from the record low at 3 months in Aug-20. Most of the inventory is 'for real', either completed homes (but the level in this category is still very low) or under construction (and these homes will be completed) – as the supply side responded to the strong increase in demand & prices. A steep increase in number of homes for sales that are not yet started, also confirms the strength of the potential supply side (but most of these projects will very likely not be started as at least the housing market has entered a recession)
- Prices increased slightly in July but prices are now on the way down, the peak was in April. Still, prices are up 8% y/y

Housing vs. recessions: We have crossed the red line!

The combined decline in new home sales & building permits has <u>crossed</u> a recession warning line

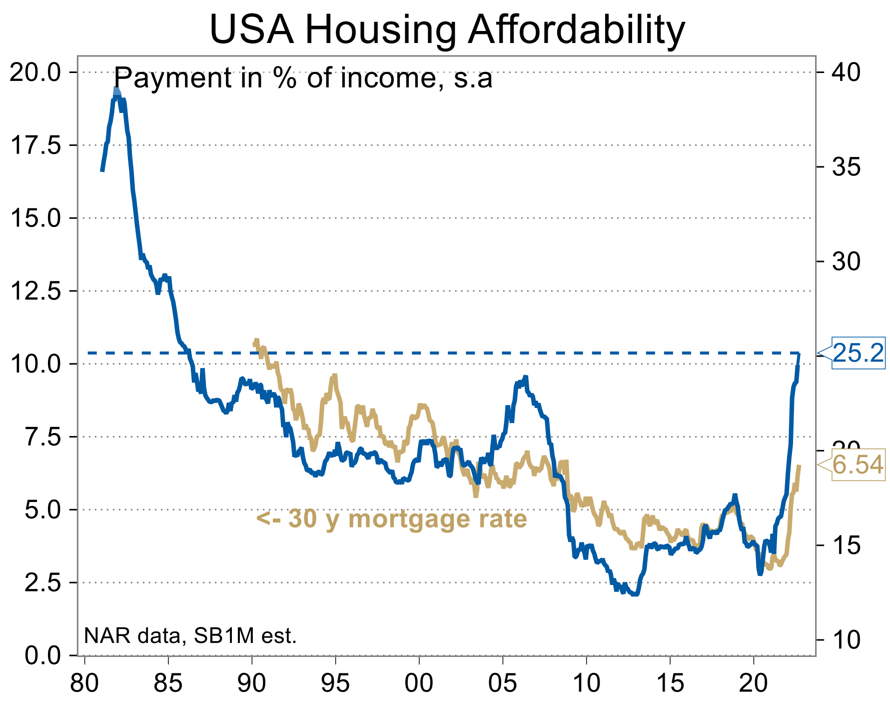


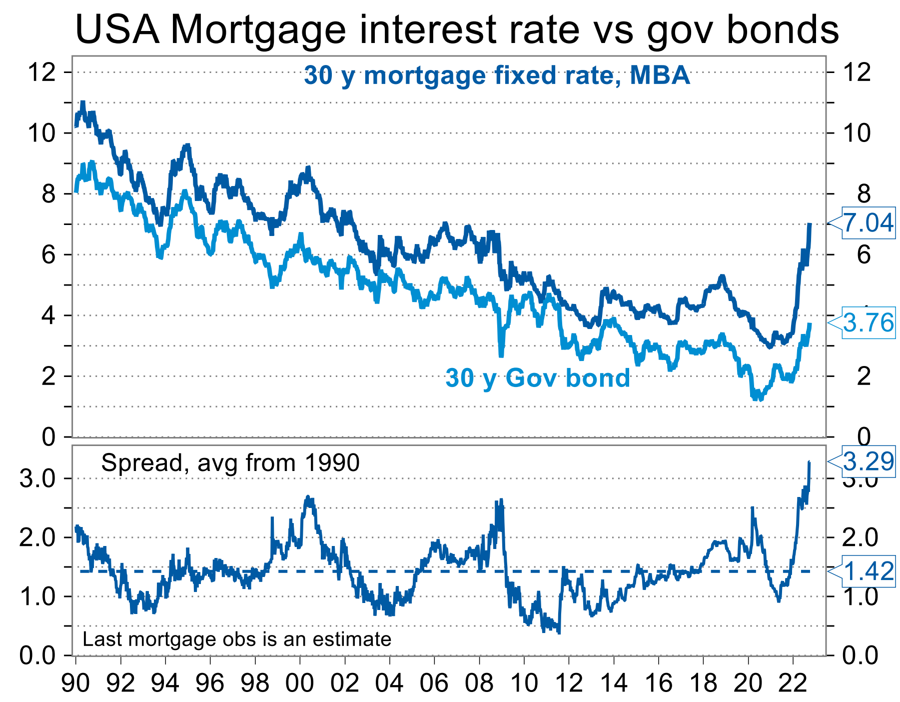


- Most recessions are 'housing recessions' as demand for housing and residential investments decline substantially ahead of and during recessions
  - » The only exception in recent decades was the 'Nasdaq' recession in 2001
  - » In addition, the pandemic recession was not caused by a setback in the housing market
- On the charts, we have marked declines of more than 12.5% in the 3 m average of the average of building permits and new homes sales vs. the recent 12 m peak with a yellow line
  - » 1984 and 1987, where interest rates were hiked, and a soft landing (and no recession) followed even if housing sent a signal (The 2010 decline was just after the GFC)
  - » The other 7 lines: A recession followed

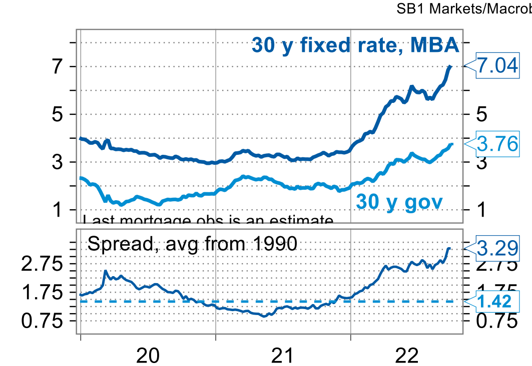
A mortgage market meltdown, the margin to 30 y gov bond unprecedented!

The effective mortgage crossed the 7% line last week. Will the Fed be forced to do a 'BoE'?



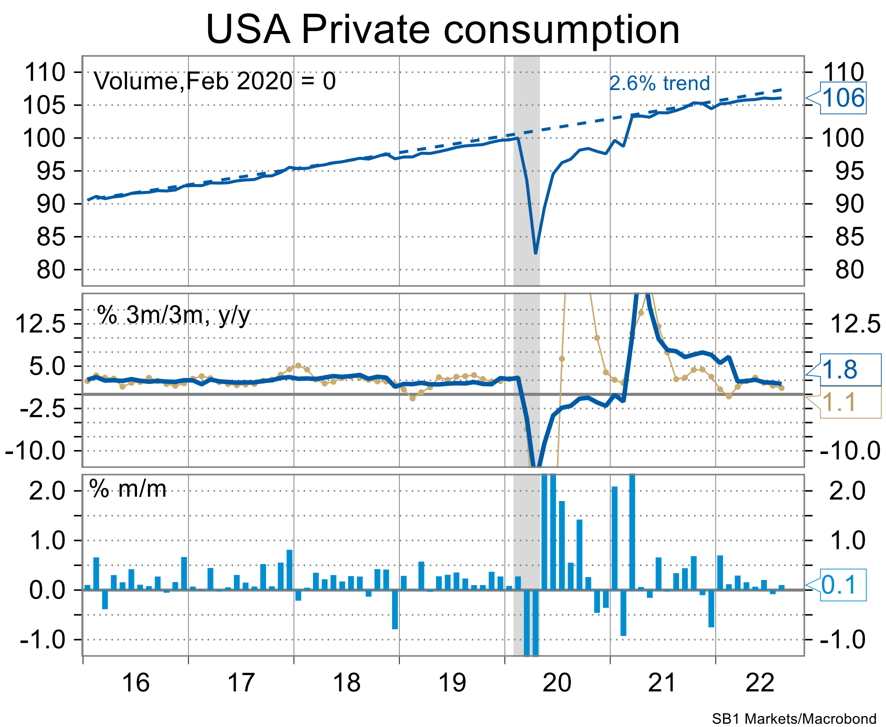


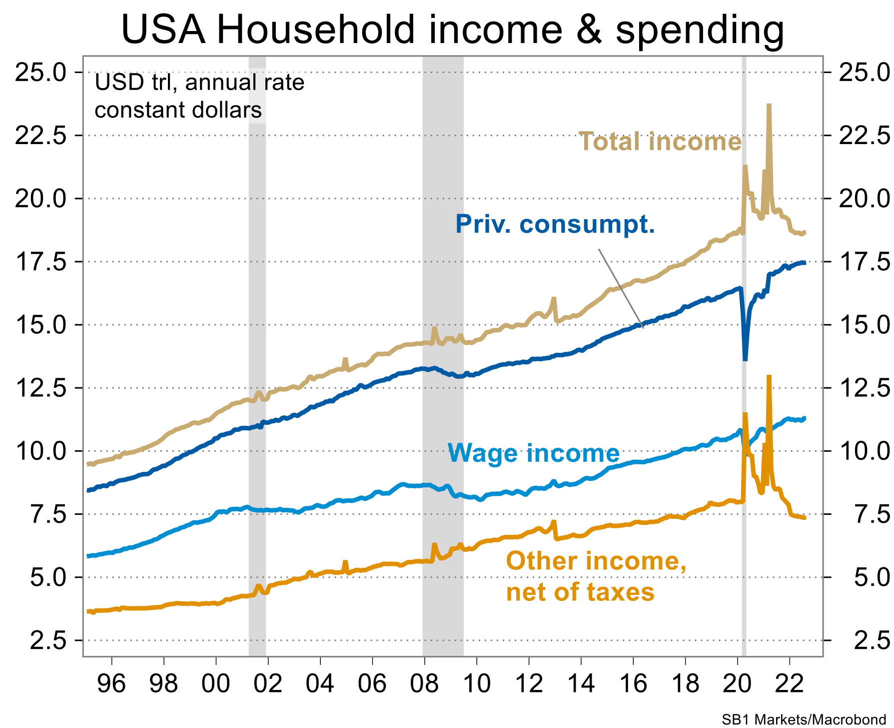
- The 30 y fixed mortgage rate shot up last week as the 30 y treasury bond yield rose sharply, and the spread has widened dramatically recent weeks, to levels we have not seen before (data from 1990). The spread was 0.9 pp at the bottom when the Federal Reserve snapped up all net mortgage bond issuances even if prices rose 20% y/y. Now the Fed is selling mortgage backed bonds, and the spread is above 3%
- At which stage will the Fed decide that the market is not working, and that is has to start buying bonds again, just like the Bank of England had to do in order to prevent a completely meltdown in the UK gilt market last week? We think that we are not that far away, probably far less than 100 bps
- <u>Housing affordability (house price x mortgage rate/income) is the deteriorating by the day – to the worst level since 1986!</u>



Consumption is flattening

Consumption grew 0.1% in August, as expected. Real incomes are trending down, as prices soar

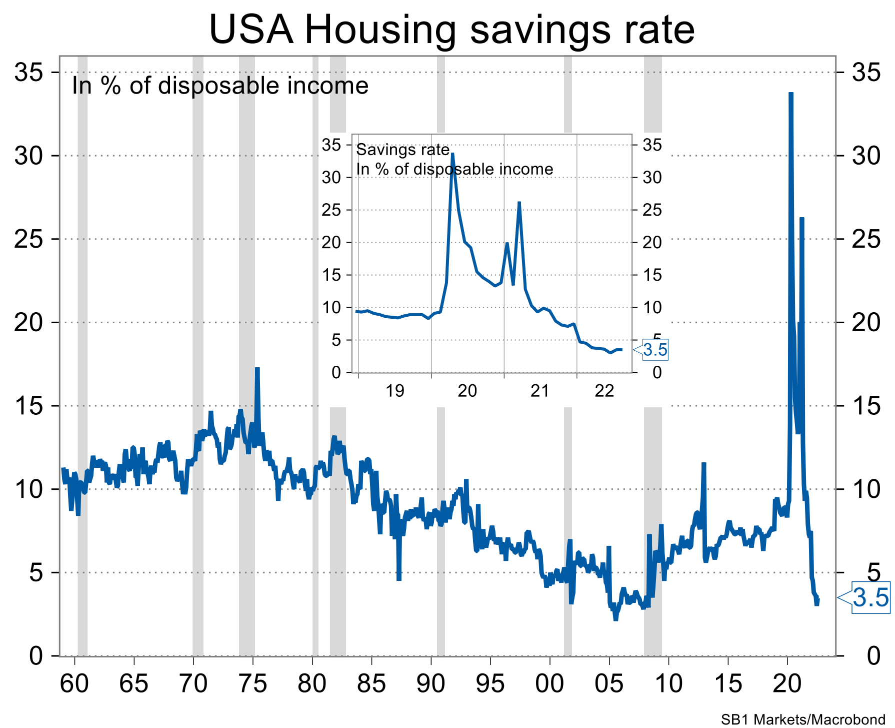


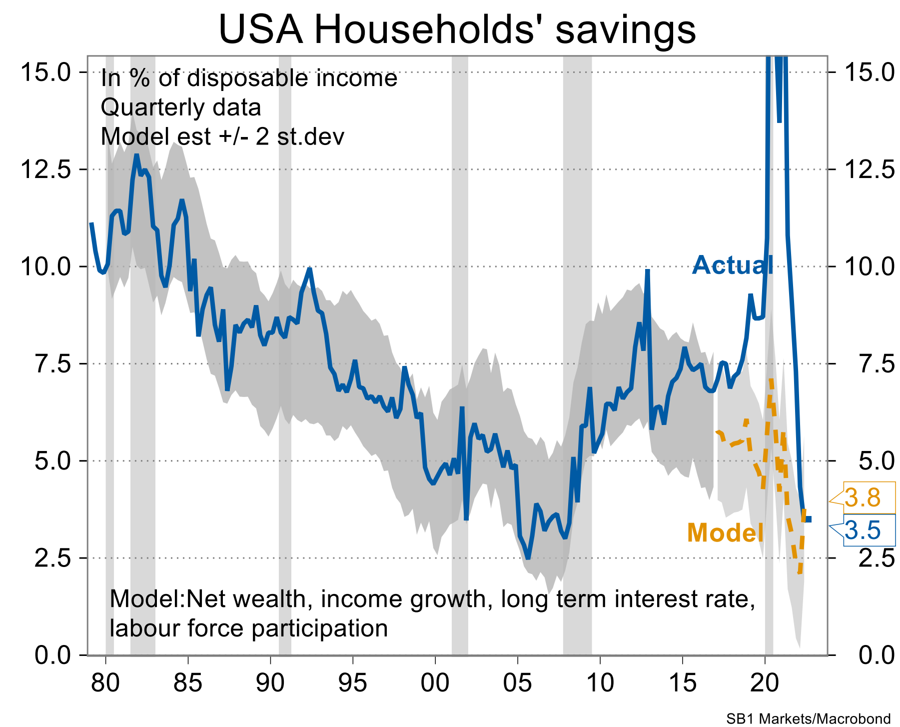


- **Private consumption** rose 0.1% in real terms in August, as expected, but growth in July was revised down by 0.3 pp to -0.1%. Nominal spending rose 0.4%, expected 0.2%. Prices rose 0.3%, 0.2 pp more than expected
  - » Consumption of goods fell, services are still on the way up
  - » History was revised slightly up since late 2020
- **Personal nominal disposable income** gained 0.4% in August, and was up by 0.1% in real terms. Real disposable income is trending down, due to normalisation of transfers, and higher taxes – and very high inflation
- **The savings rate** was flat at 3.5%, following a 1.5 pp downward revision – and is now some 4% below the pre-pandemic level. However, even if the accumulated extraordinary savings through the pandemic is now run down, most of the Wall of Money is still intact which may make it possible for households to keep up the level of spending (at least for those who saved…)

The savings rate revised down 1.5 pp, and 3.5% is not that impressive

The savings rate was revised down from mid 2021 (and for 2019)

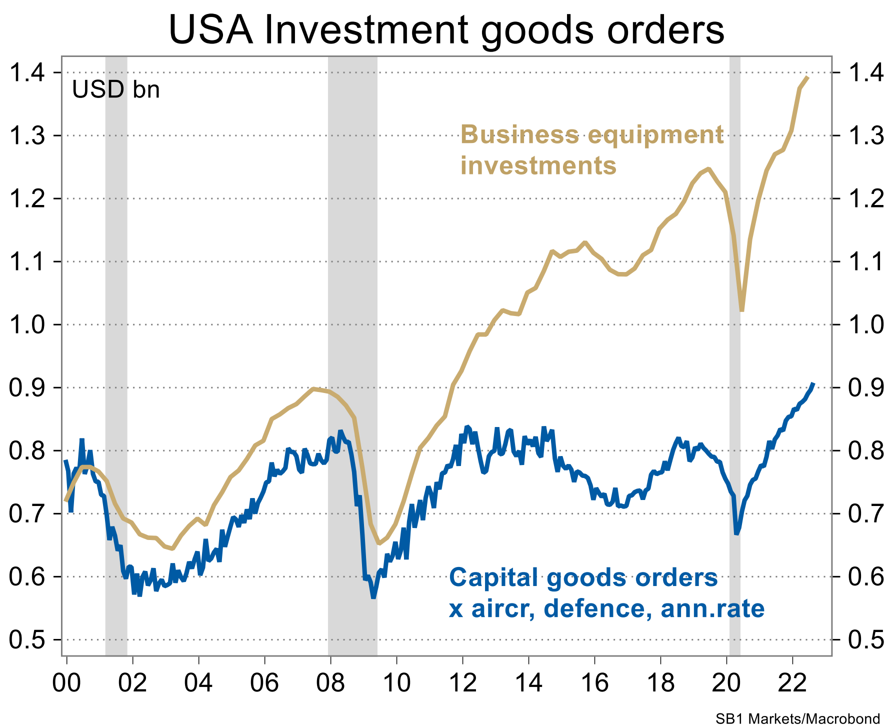


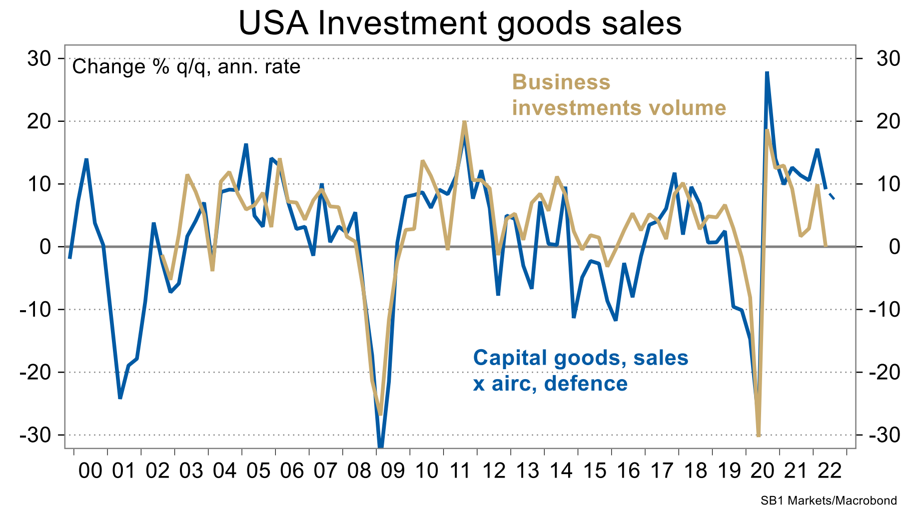


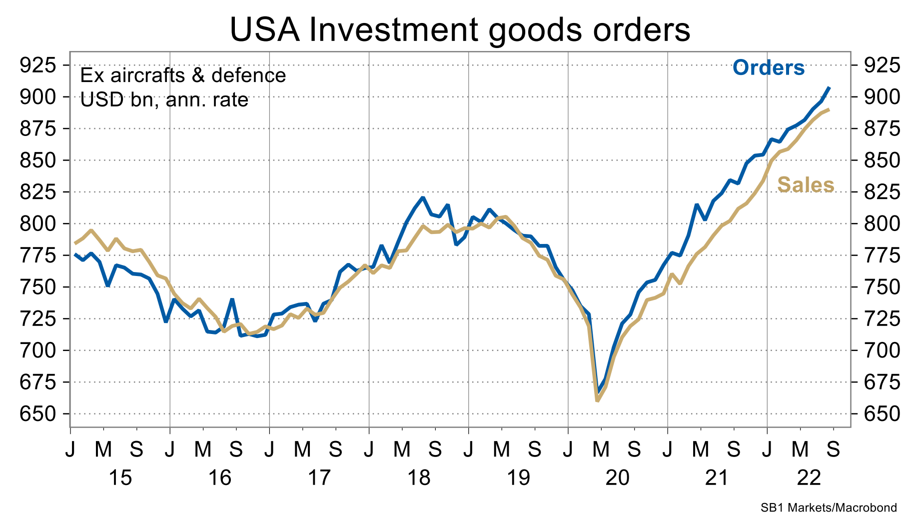
- The **savings rate** was unch. at 3.1% in August (July was revised down by 1.5 pp)
- Households are now dipping into 'normal' savings in order to keep consumption up, as their real incomes are not keeping up, due to the high rate of inflation. The savings rate is now 4 pp lower than before the pandemic
  - » However, household have saved much more than normal during the pandemic, equalling to some 13% of disposable income – on average for all households, that is. This 'Wall of Money' is now shrinking at a 4 pp pace per year, if the savings rate stabilises at 3.5%
- Our old savings model, yielded a 2.8% savings rate in Q2. During the 2016 – 2019 period our model has underestimated the savings rate systematically by some 2 pp, but the gap is now closed (as the sign may change in Q3, due to the decline at the stock market – and thereafter by lower oil price, and higher interest rates

Core capital orders are still growing well above trend

Signal decent growth in business investments in Q3 (at least in nominal terms)



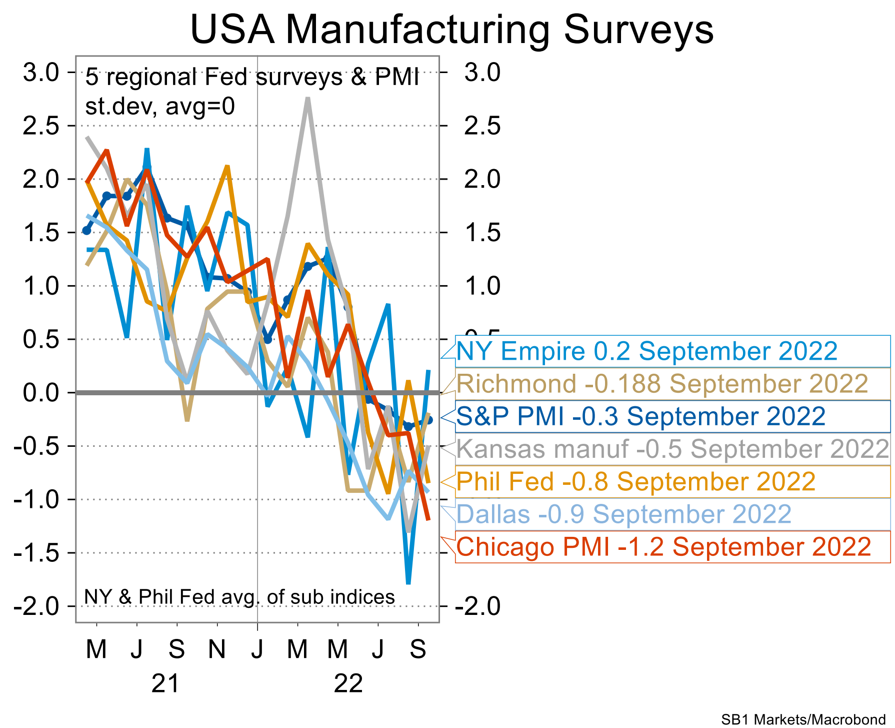


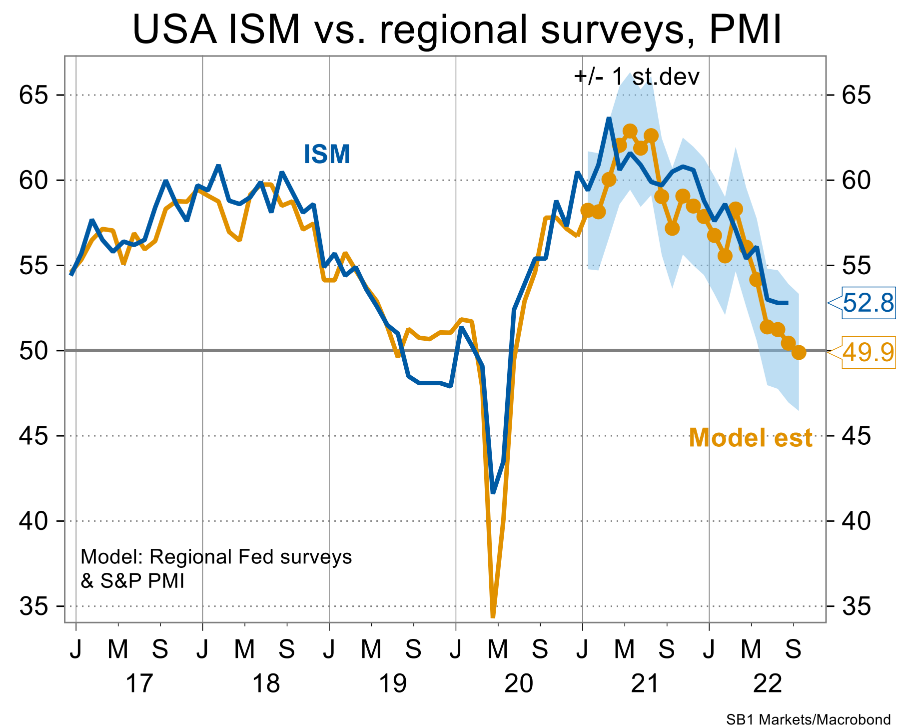


- **Core (x aircraft, defence) capital goods orders** grew by 1.3% in Aug, far above expectations at 0.2%. July data was revised up 0.4 pp to 0.7%. Shipments were up 0.3% m/m. All data are in nominal terms
- **The business investment** level is well above the pre-pandemic level – and not low vs. a reasonable long term trend (both in nominal and volume terms)

The trend is set – but September surveys were mixed

The ISM risk: The level is substantially stronger than the average of other surveys



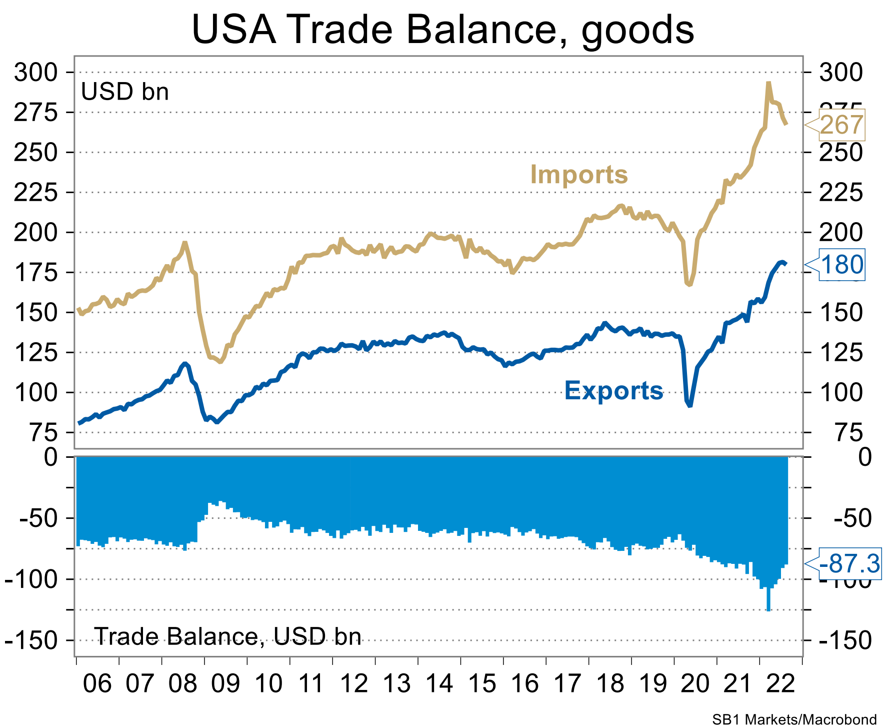


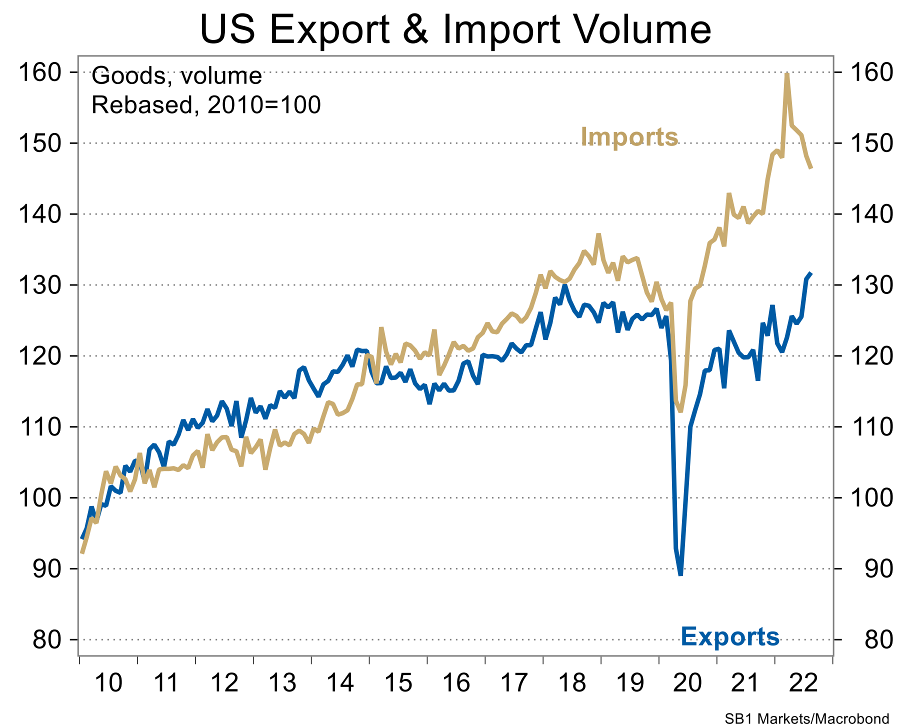
- Big picture: Growth is slowing sharply but manufacturing indices do not signal that the economy has entered a recession (even if order indices are really worrisome)

SpareBank 1 MARKETS

The trade deficit is shrinking, even in volume terms. Will support growth in Q3

The trade deficit in goods narrowed by USD 2 bn to 89 bn in Aug, marginally better than expected

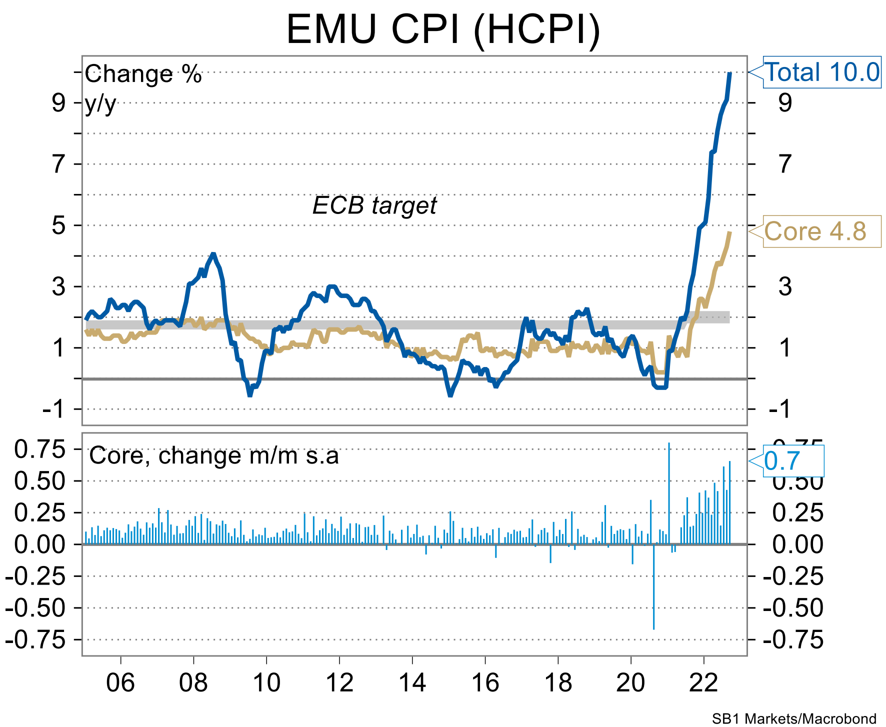


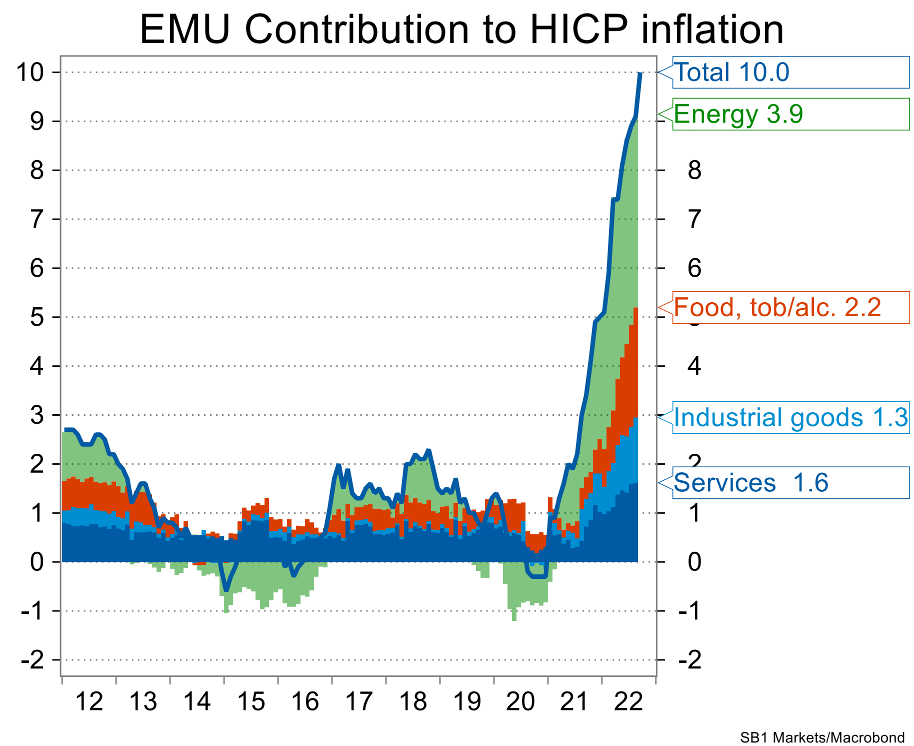


- The trade balance in goods has been falling rapidly recent months, as imports are declining rapidly, from a very high level
- In addition, growth in exports have been rather impressive, even in volume terms. Export volumes are up some 5% from before the pandemic. Imports have fallen sharply from the March peak, by 8% - but imports are still up 15% from early 2020. The slowdown in import volumes is due to weaker domestic demand, probably also a destocking
- If export and import volumes are unchanged in Sept, exports of goods will be up 21% in Q3, while imports will be down 12%. If so, a 4 pp (four) contribution to GDP growth in Q3! Inventories will very likely be run down, so the net impact will be smaller – but still very likely positive

Inflation surged in September – headline inflation hits 10%, core at 4.8%

Both higher than expected, again. Energy prices the main culprit but inflation is broadening, here too

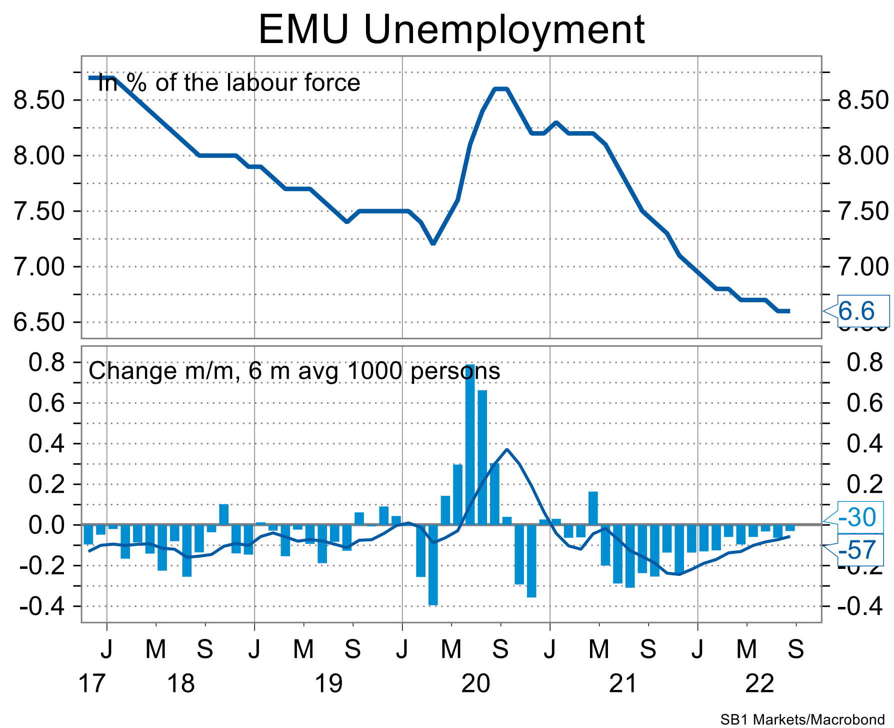


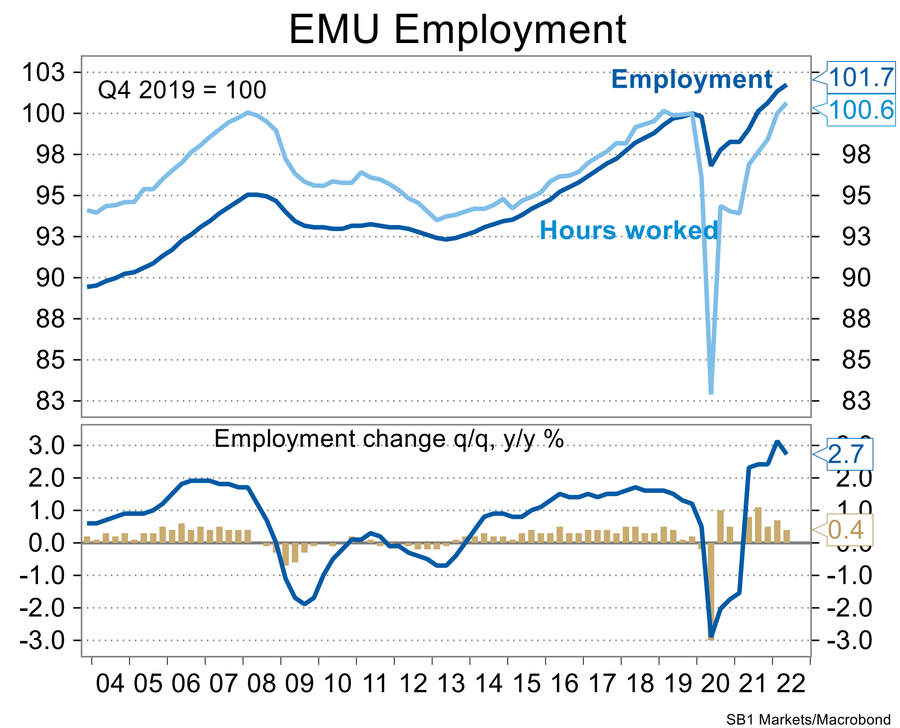


- The **total HICP** rose 1.2% m/m Sept (1.1% seas adj), 0,3 pp above expectations… again
  - » Energy prices rose 2.5% m/m, they are up 40%, and contributes with close to 4% to the headline rate. Food prices rose 1.2% - and the latter is up 11.8% y/y, contributing more than 2 pp to overall CPI growth (all data at the chart to the right is not updated)
- **The core** rose 0.7% m/m, 0.1 pp more than expected. Both goods and services contributed. The annual rate accelerated 0.5 pp to 4.8%, the highest ever, of course
- The **ECB** is no doubt in fighting mode and will hike the signal rate further this week. However, as long as wage cost inflation remains moderate, the medium-term threat against price stability is not that large. The current lift in profit margins will not be sustained if the economy slows. The main risk is that the current inflation shock will push wage inflation up due to compensation claims from the unions

Unemployment flat at the lowest level since 1980 at 6.6% in Aug, as expected

The no. of unemployed fell marginally – and will soon turn up?

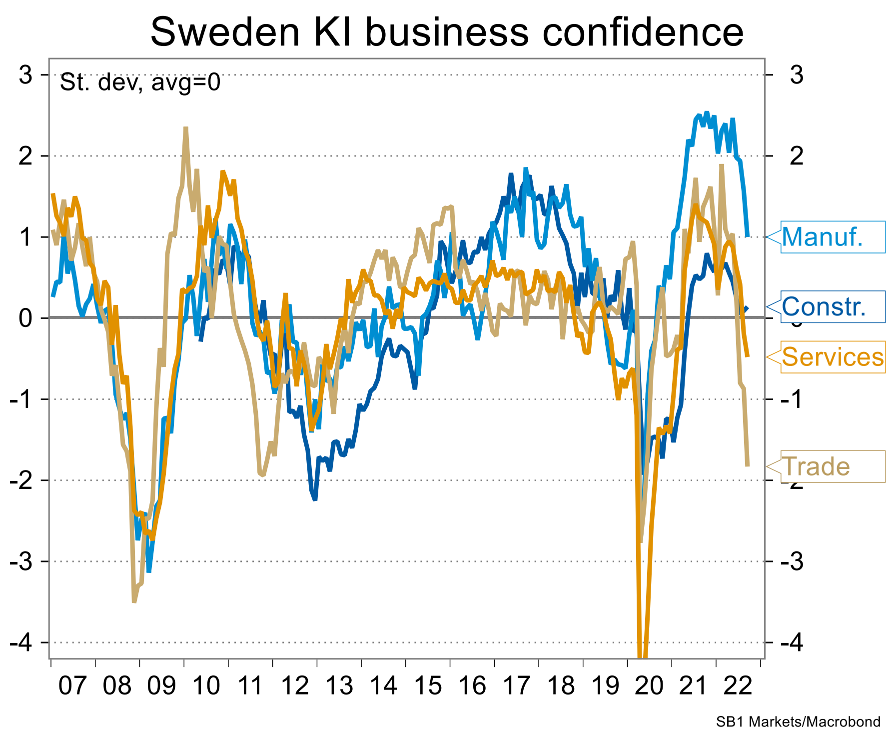


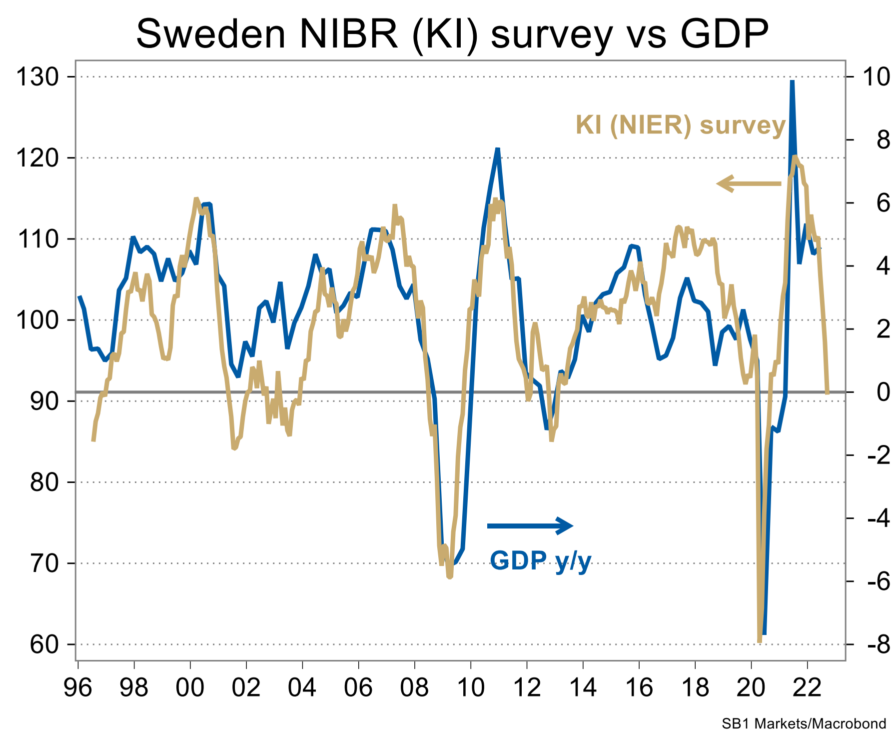


- **The number or unemployed declined in August**
- **Employment** grew by 0.4% in Q2 (not annualised), and hours worked grew too
  - » The employment level & the employment rate is higher than before the pandemic
- The number of **unfilled vacancies** soared to the highest level ever in Q2, by far
- The labour market is no doubt still very tight – until further notice
- **Wage cost inflation** has not accelerated but a slowdown in productivity growth has pushed labour cost per produced unit upwards, to somewhat above 2%

Business confidence deteriorated sharply in September, zero growth signalled!

Confidence in the manufacturing sector fell, but is still strong at 1 st.d. above average

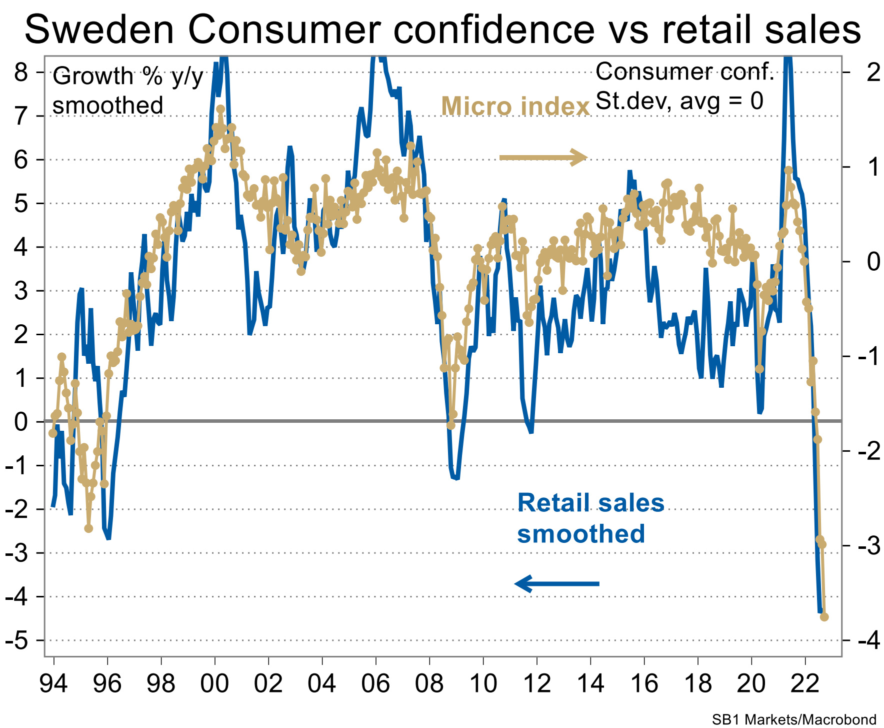


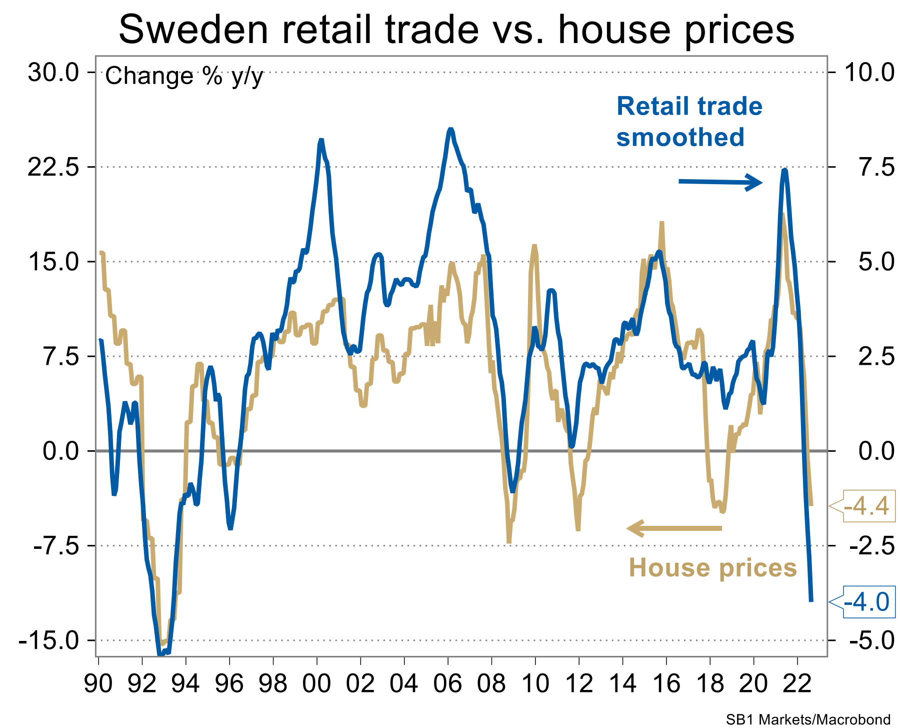


- **The composite index** fell to 90.8 in September from 97.2 in August. The decline equals a 0.7 st.dev decline to 0.9 st.dev below average. The index signals zero GDP growth, down from +2% in August. The Riksbank expects a small increase in GDP in Q3 (q/q) but then a 0.9% (total) decline in Q4 and Q1
- **3 out of 4 main sub-sectors** are reporting declining confidence
  - » The **trade sector confidence plummeted** in Sept, and is now 1.8 st.dev under water
  - » The **manufacturing sector sentiment** has declined over the past three months, however, manufacturing sector sentiment still remains strong
  - » Sentiment in **the construction sector improved** in Sept, and is now 0.1 st.dev above par

Consumers are not just saying they are pessimistic: They walk the walk

House prices and retail sales down in tandem with consumer confidence

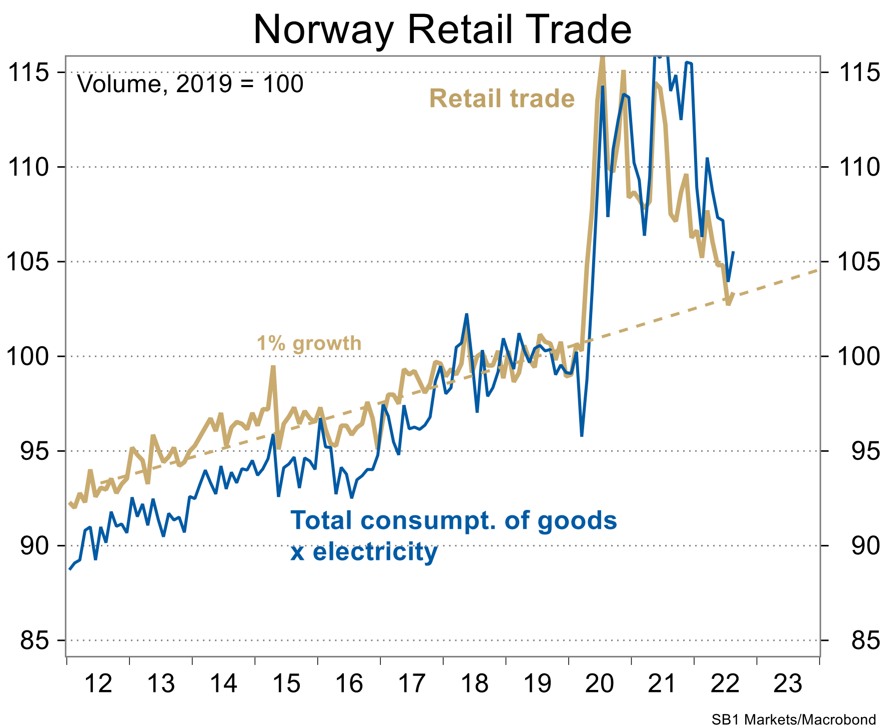


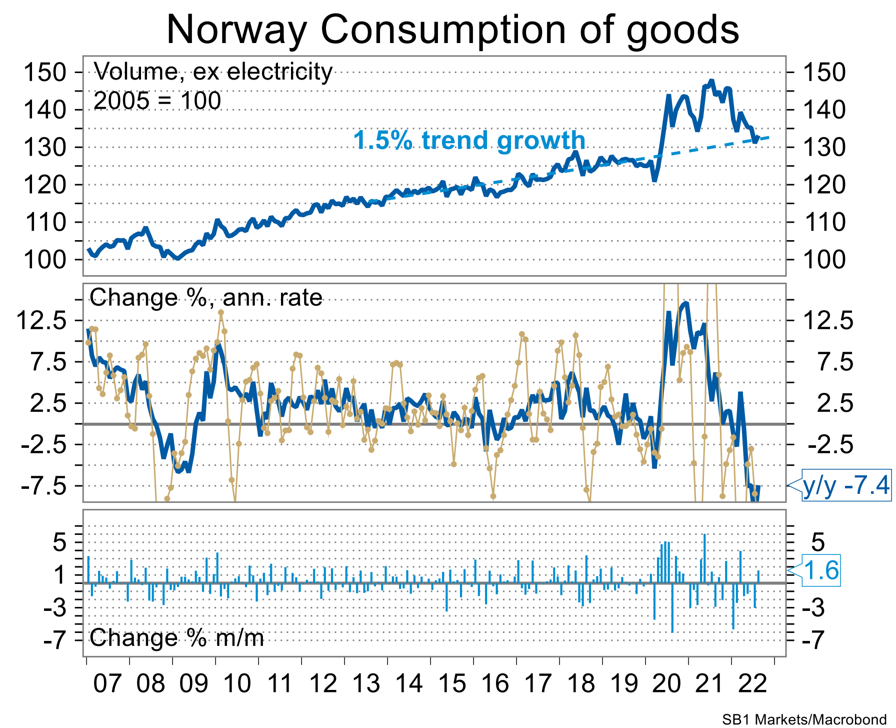


- **Consumer confidence** (the micro index)) fell 11.1 p to 41.2 in Sep from 52.3 in Aug (revised down from 56.3) – which is rather depressing, at 3.6 st.dev below average! The **macro index** was also down, to 2.4 st.dev below average from 1.9 st.dev below average, resulting in a total confidence index that fell to 3.6 st.dev. below average from 2.9 st.dev below average the month before
- Both **retail sales** and **house prices** have fallen alongside the decline in consumer confidence – higher rates and high inflation is softening both sentiment and ultimately demand - the outlook is rather bleak

Retail sales stronger than expected in August, but the trend is down

Retail sales were up 0.7% (expected -0.5%); total consumption of goods was up 1.6%

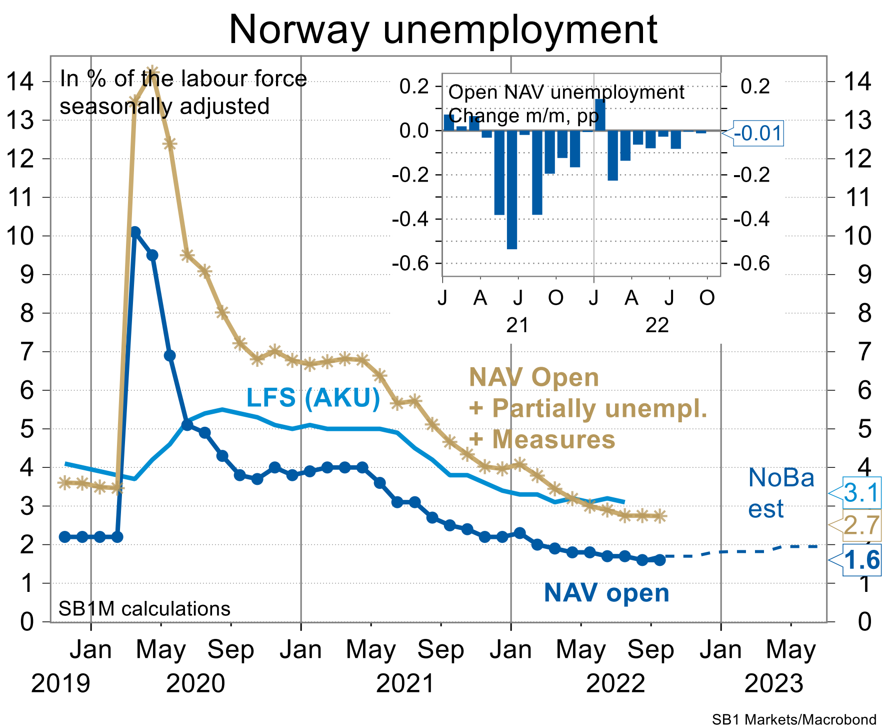


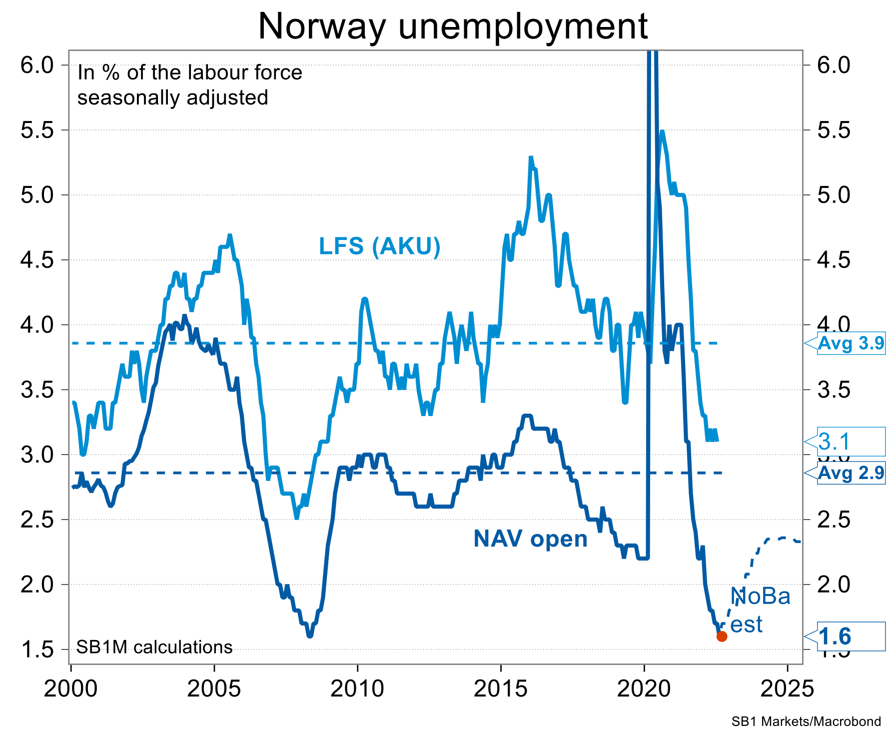


- **Retail sales** have been far more volatile than normal during the pandemic, and monthly data have been close to useless. Sales have been trending down since early 2021, like in many other rich countries, from levels that were miles above pre-pandemic trend growth path. **Total consumption of goods** gained 1.6% in August
- The lift in inflation and higher interest rates seem to have aided sales back down to the pre-pandemic trend – and we expect sales to fall below the trend the coming months/quarters
- Both household equipment (building materials) and food store sales contributed on the upside in August (both were down in July)

NAV unemployment marginally down in September – which will be the bottom?

Open unemployment unch. at 1.6%, as expected – but 0.1 below NoBas f'cast



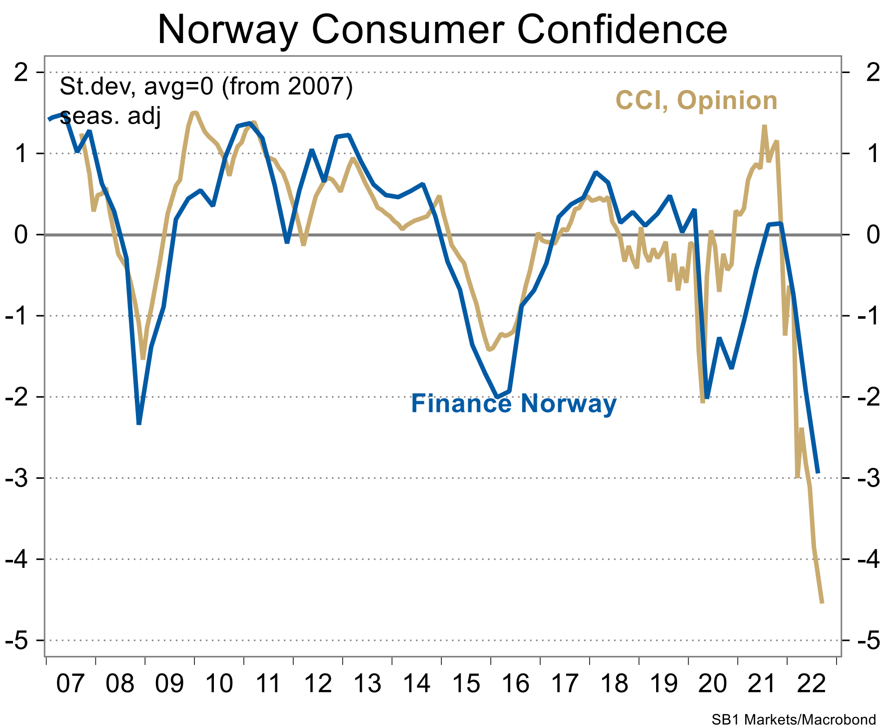


- **The 'full time' open NAV unemployment**, fell by some 300 persons in Sept (seas. adj) to 47.6'. The change was as we assumed, but Aug was marginally revised upwards. The rate at 1.6% (s.a) is equal to the lowest level before the financial crisis in 2008, and almost the lowest level since 1980, and +0.1 pp below NoBa's estimate in the MPR. Unadjusted the rate was unch. at 1.6% (1.57%), expected down to 1.5%
- Including labour market measures, unemployment fell by 700' persons, and the rate is at 2.0%
- The inflow of **new job seekers** have bottomed but is still at very low level. The **inflow of new vacancies** fell in September, and the trend is down, from the peak before the summer. Even so, the level remains very high. The decline is broad, except for the public sector.
- **The LFS (AKU) unemployment rate** declined 0.1 pp to 3.1% in July. **Employment growth** is slowing – or fallen to zero (LFS)

SpareBank 1 MARKETS

Consumer confidence down to ATL in ~~May~~ ~~July~~ ~~August~~ September…

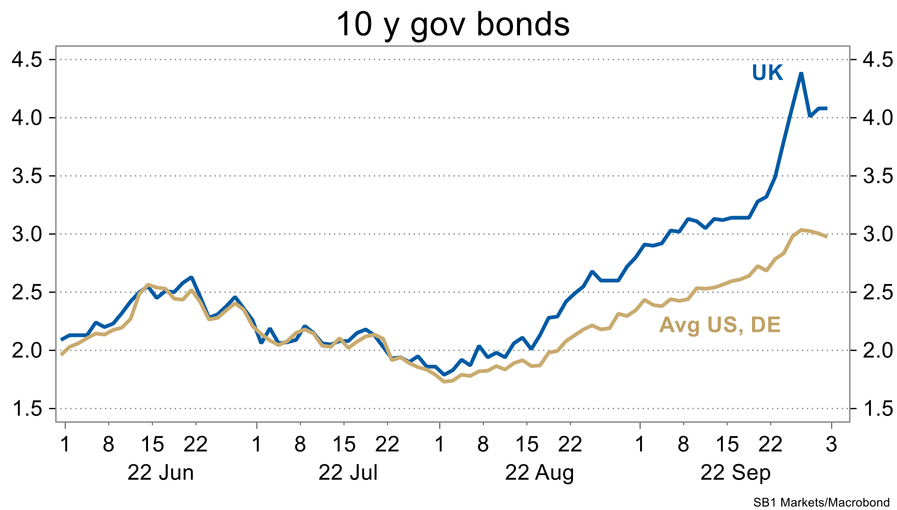
… and more than 'twice as weak" as when the corona first attacked

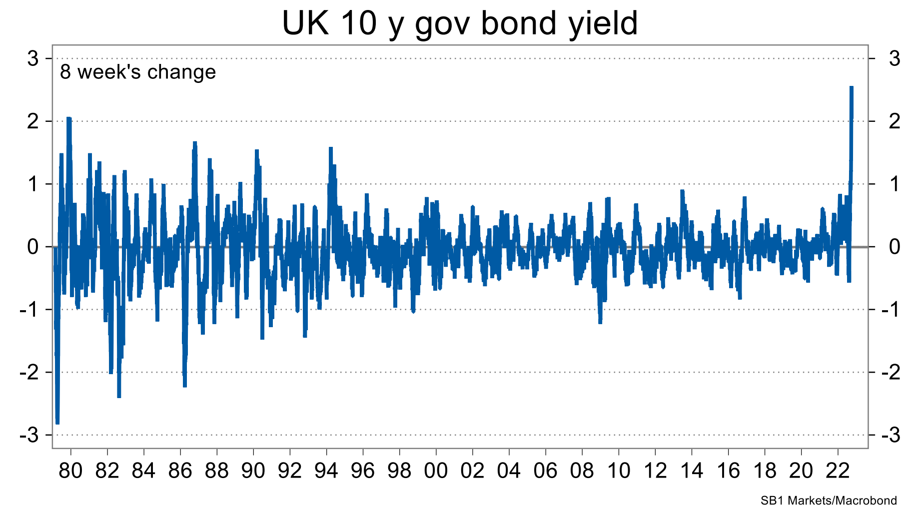


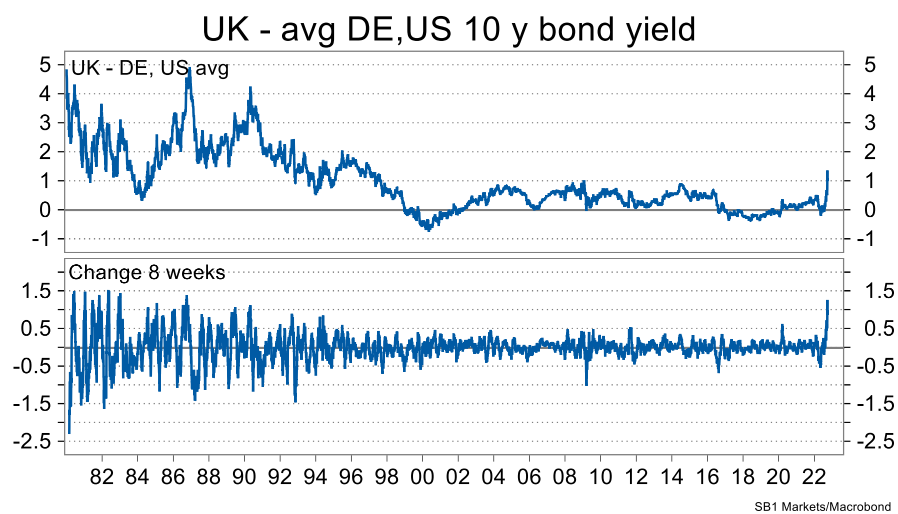
- **The CCI print** from Opinion in September was the lowest ever recorded – high inflation and higher interest rates are no doubt biting
- The index recovered somewhat in April, but fell again in May - Aug, and is now 4.4 st.dev below average. The bottom during the pandemic was 2.0 st. dev. below average
- **Will households stop spending or retreating from the housing market?** So far, the housing market has held up well, while retail sales volumes have been falling sharply but from a level way above trend
- The **net share of optimists** is almost -30%. Given inflation and the hikes in interest rates + some geopolitical uncertainty, this share could easily have been larger
- On the other hand, even if a large share of the population recognises that their own economy will be hurt, it does not imply that they all plan to cut spending sharply. Even so, the decline in confidence is of course worrisome

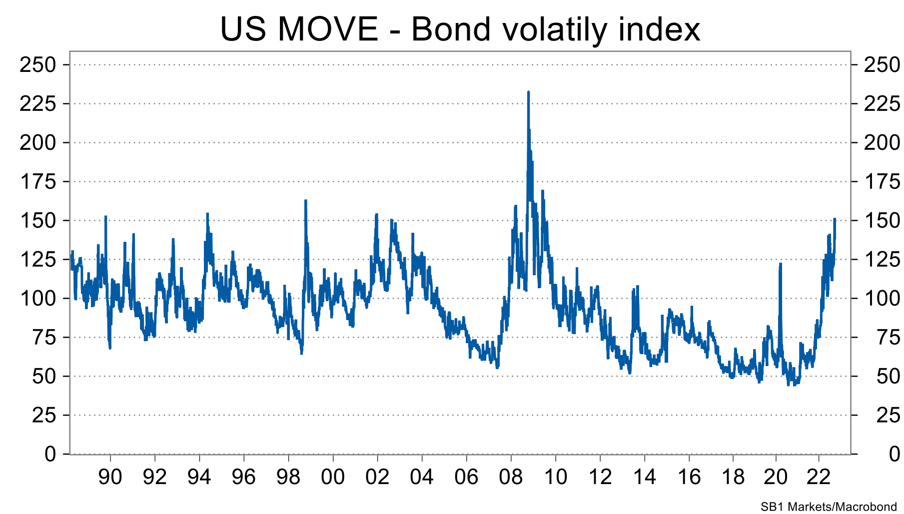
Some though weeks for the UK! BoE had to save the gilt market!

The Bank of England had to intervene at Wednesday, and fired a bazooka: Will keep yields in check



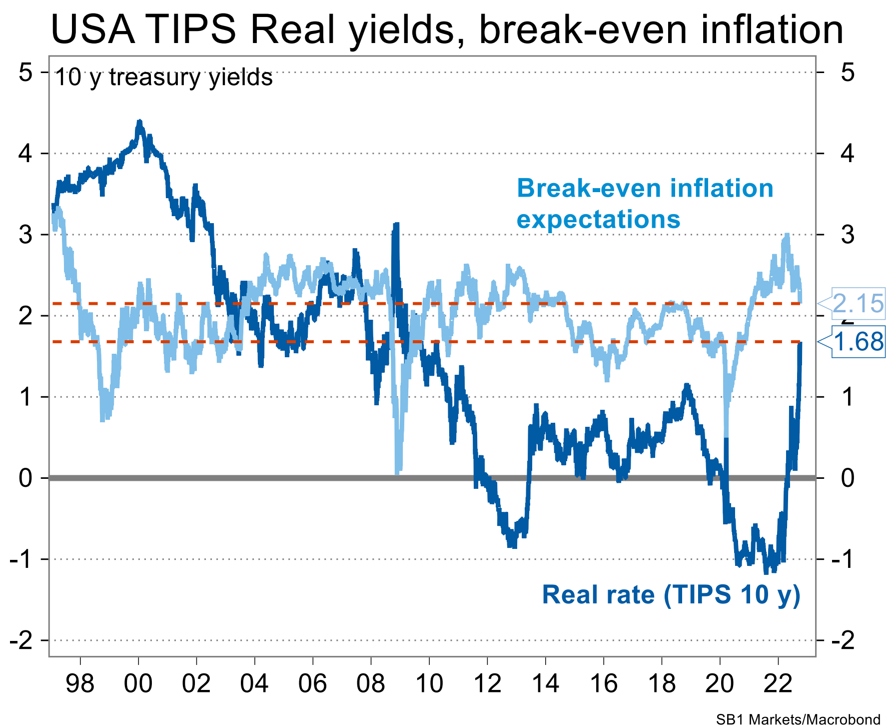


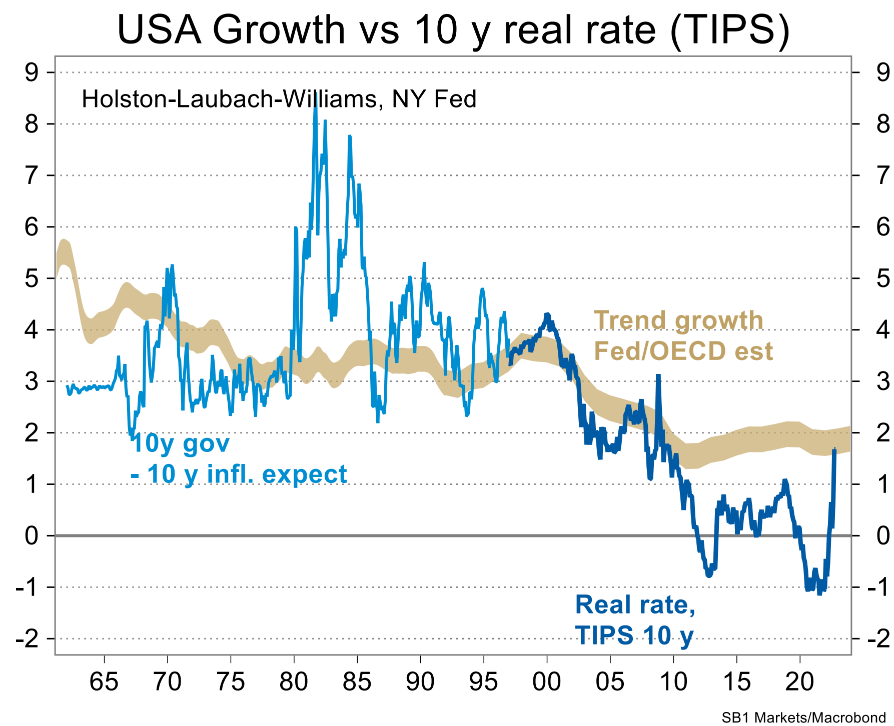




Growth vs real rates: Mind the missing gap, it has closed!

Real rates are up, while short/medium-term growth expectations are below trend growth

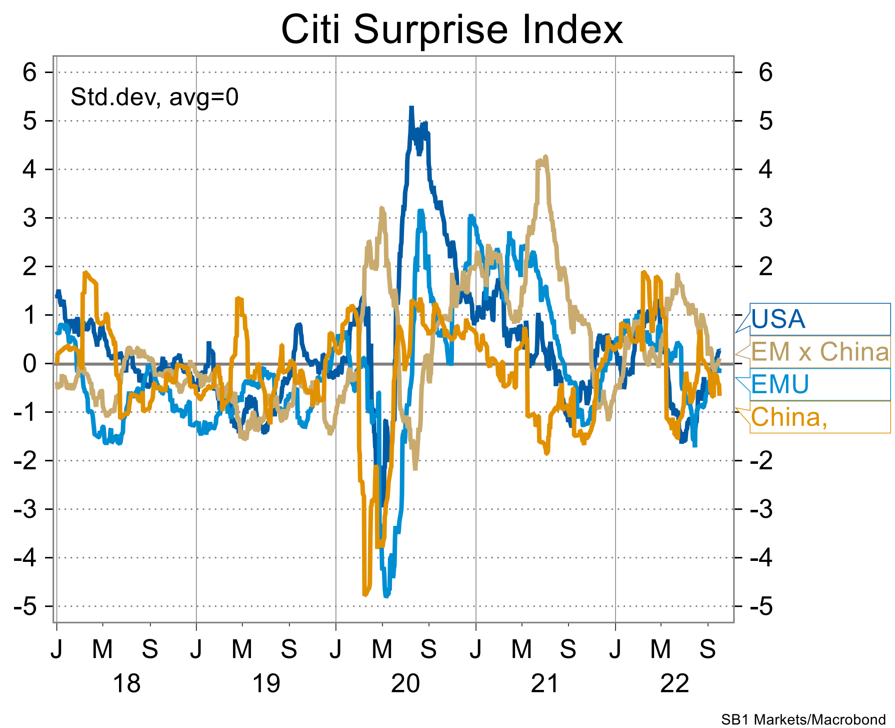


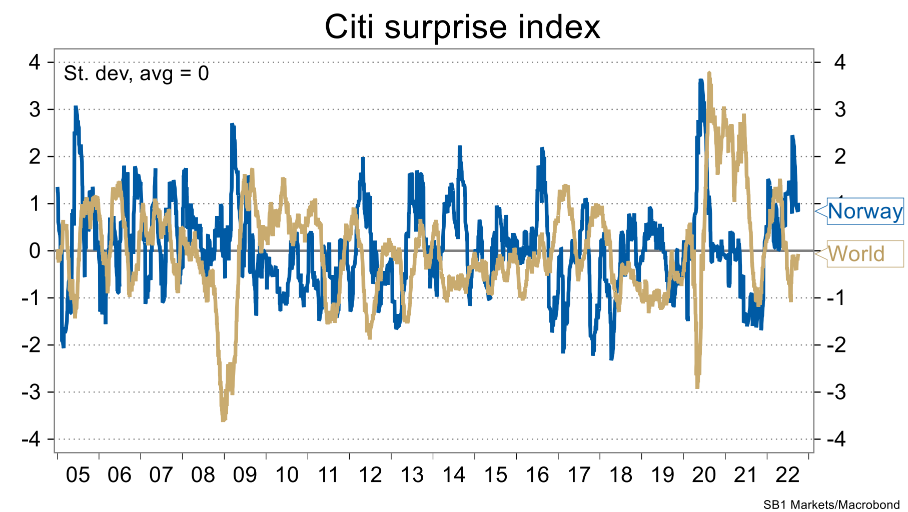


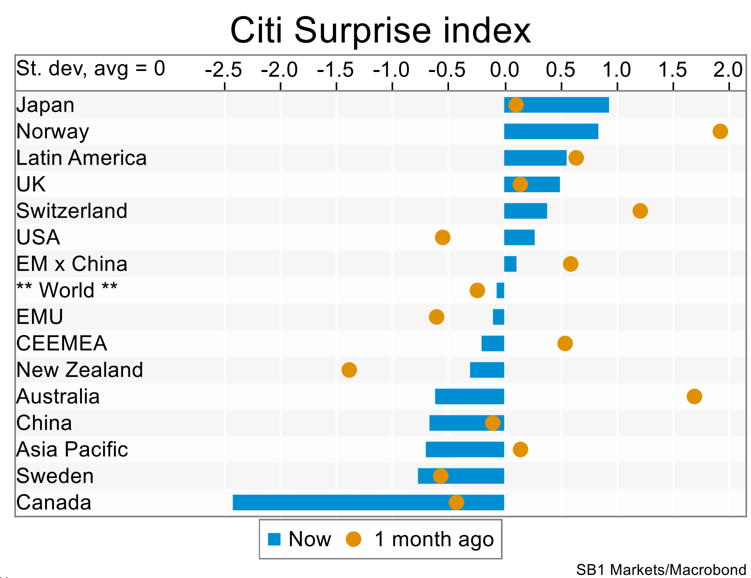
- Long term inflation expectations are 'collapsing', down 85 bps from the peak

Data still slightly on the downside but most countries/regions close to neutral

US data surprised on the upside last week, China still on the downside.







- **Norway** no. 2 on the list, according to Citi
- … even if our super-cycle friends Australia, Canada, Sweden & NZ all are close to the bottom of the list. Strange, will that discrepancy last?

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

Highlights

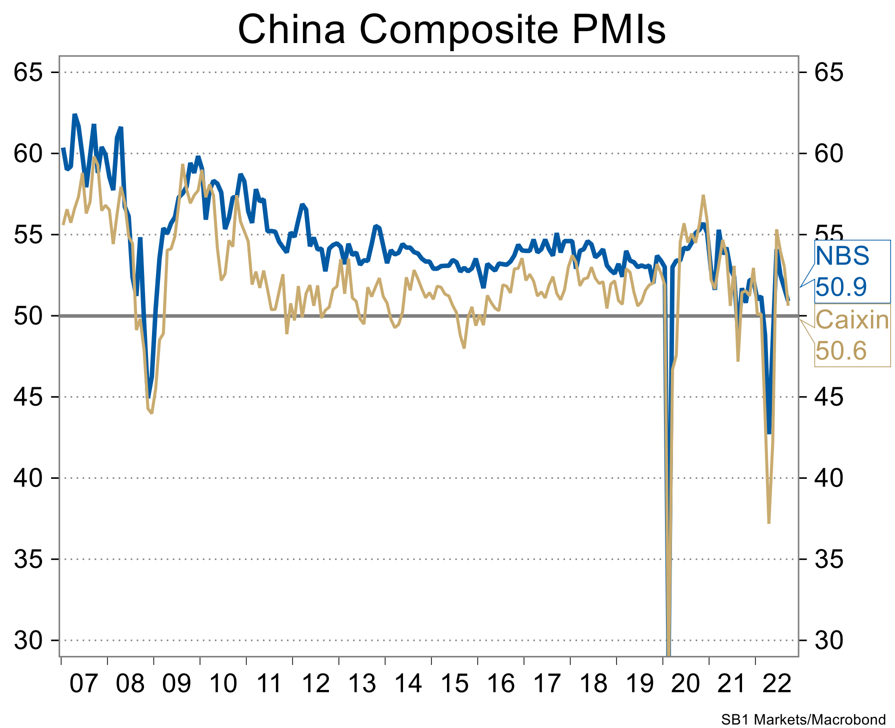
The world around us

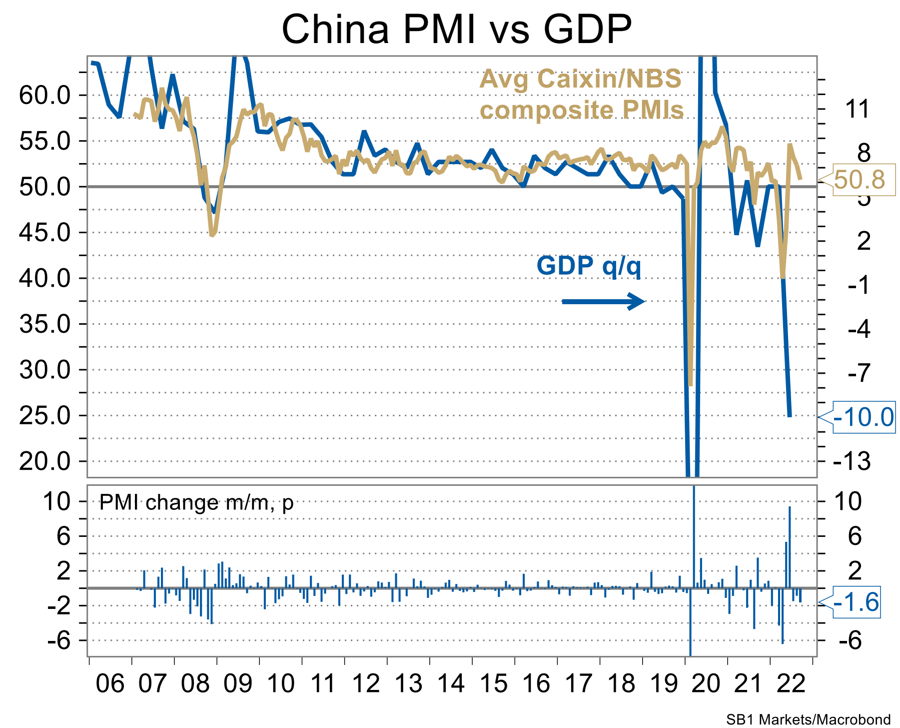
The Norwegian economy

Market charts & comments

The NBS PMI down as services slowed, the Caixin manufacturing survey also down

In sum, the PMI reports (probably) signal modest growth in Q3. We think the outcome will be better

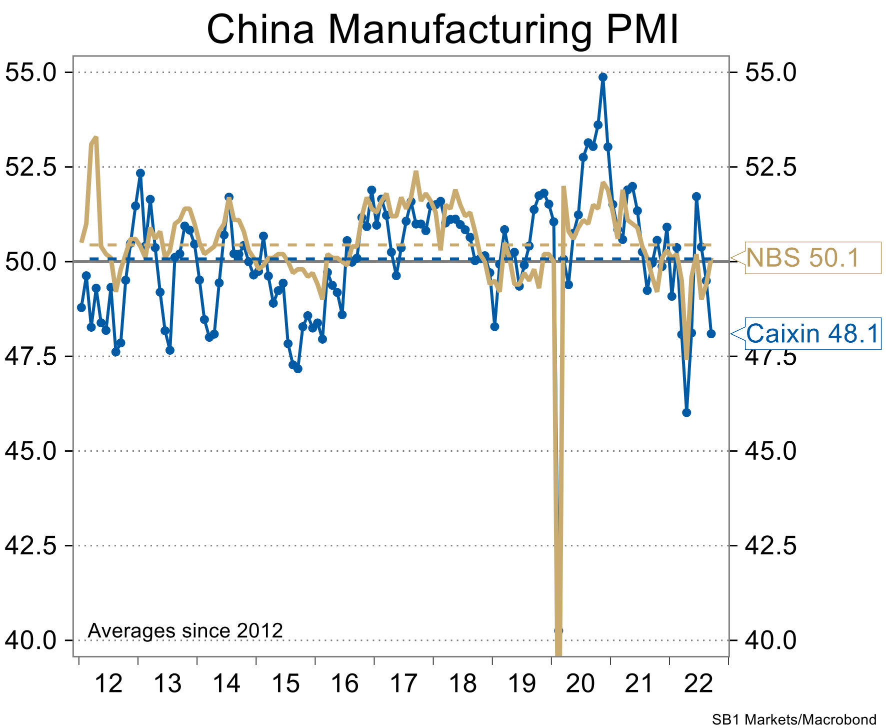


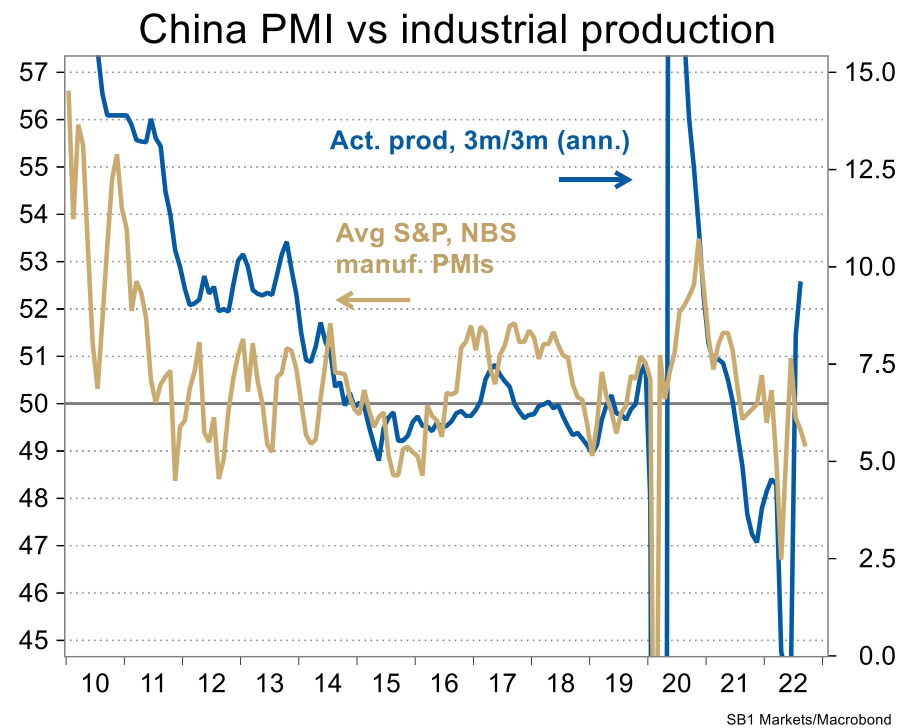


- … following the 10% setback in Q2 (2.6% not annualised), during the lockdowns. The **two PMI data sets** will probably (services data from Caixin is not yet published) signal growth below par, at a level around 50.8
- The **NBS/CFLP composite PMI** fell by 0.5 p to 50.9, expected close to unchanged. The service sector reported a further slowdown to well below trend growth. The manufacturing sector reported higher growth, at almost a normal pace of expansion
- The **Caixin manufacturing index** fell 1.5 to 48.1, expected unchanged. The level is well below par, but since NBS reported a far stronger index, it is hard to draw any conclusions
  - » Caixin has not yet reported its service sector survey, we assume a moderate decline our estimate for the composite index

Caixin's manuf. PMI further into contractionary territory – NBS/CFLP PMI was up

Both are below average and signal growth below trend, but still no decline in production

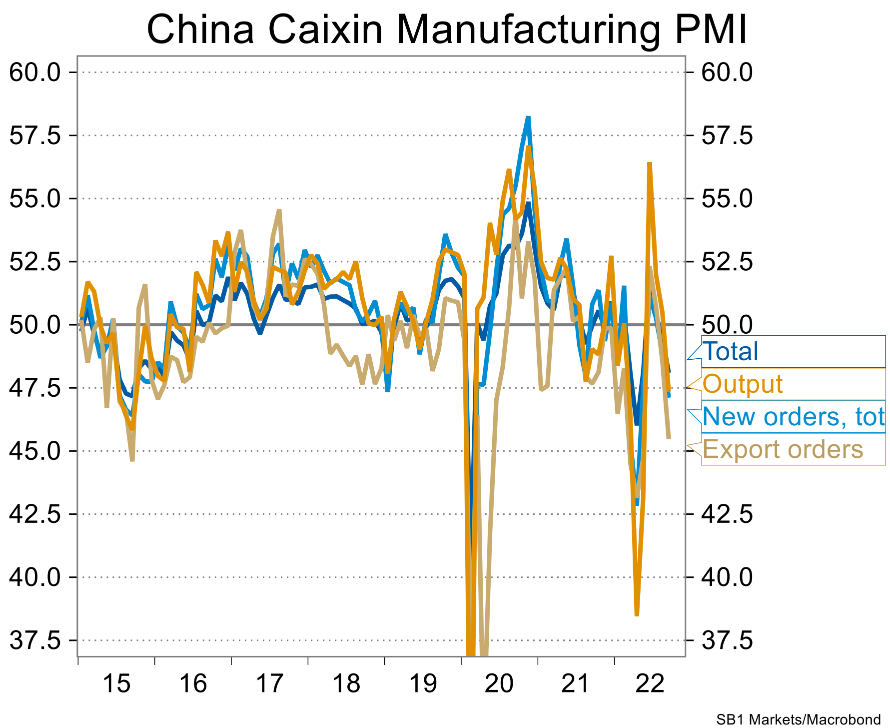


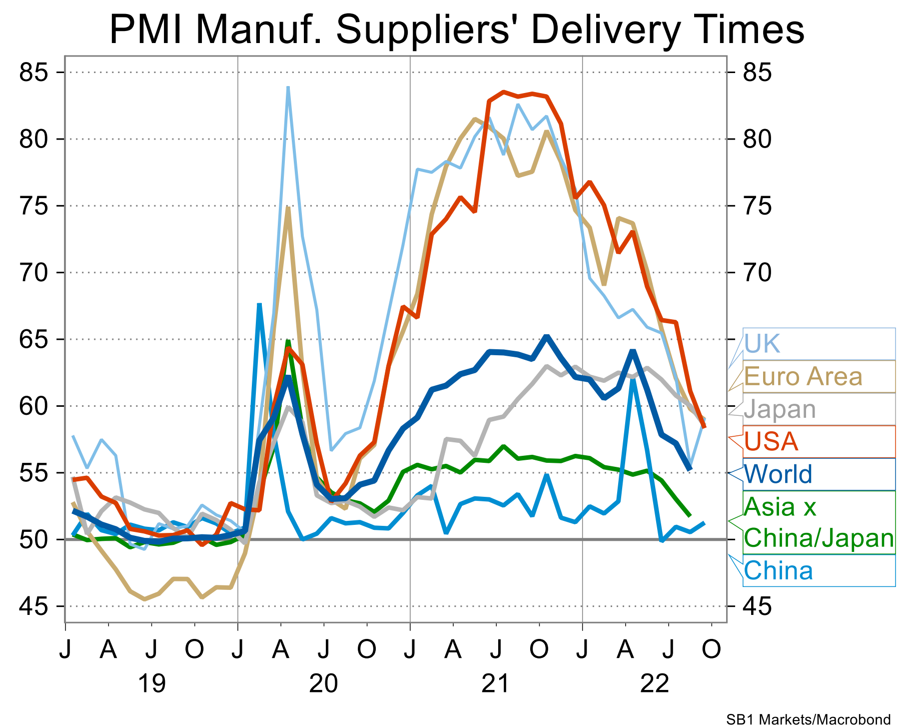


- Actual production rose sharply in May, and further the next three months

Limited lockdowns probably not to blame for a setback in export orders

Global demand for goods is probably slowing

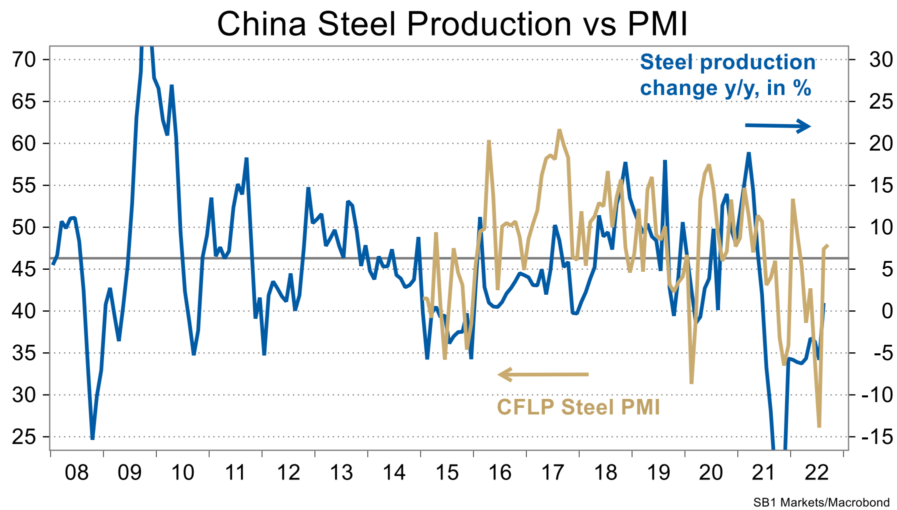


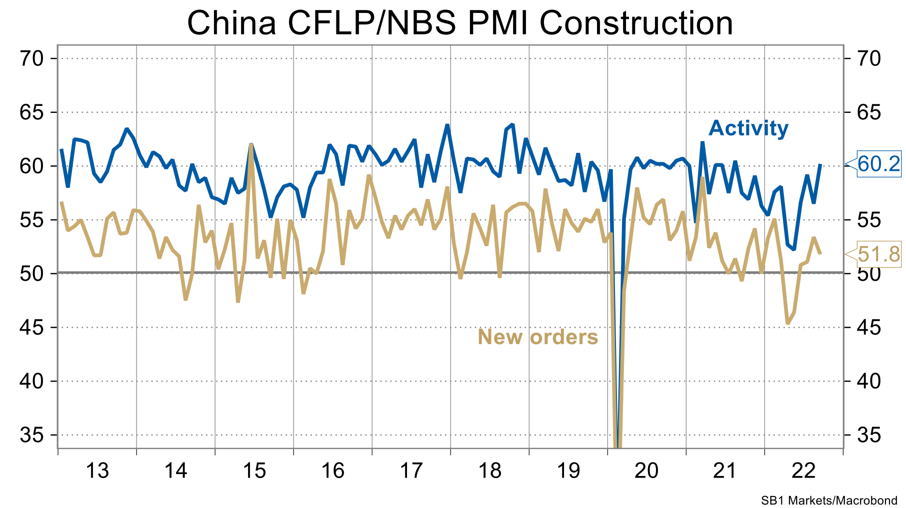


- The decline in Caixin's PMI & its sub-components are rather similar to the lockdown halt in April. Now, covid restrictions are far less widespread, and they are very likely not the reason for the current setback
- The **output sub-index** fell to 47.4 from 50.5 in September, suggesting a contraction in output
- Delivery times have 'normalised'

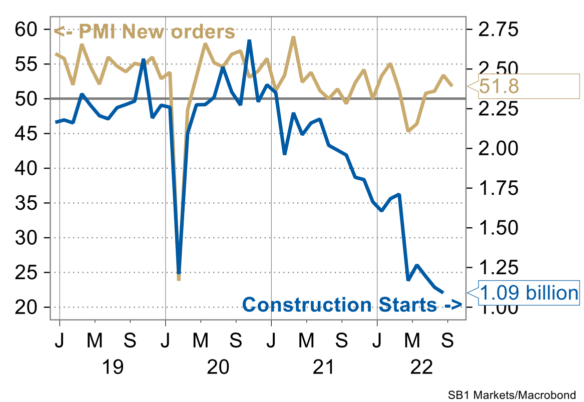
The steel sector PMI increased in September, rather remarkable

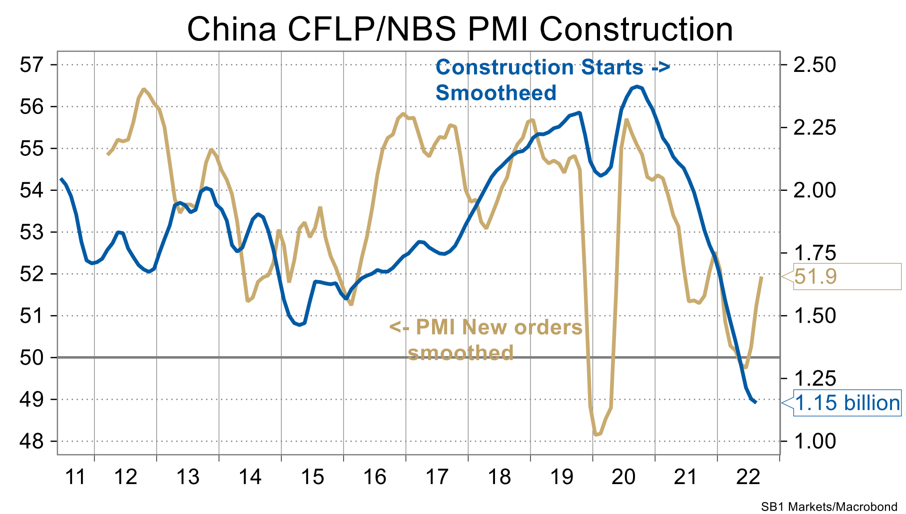
Order inflow to the construction was a tad lower in September, but orders are still growing





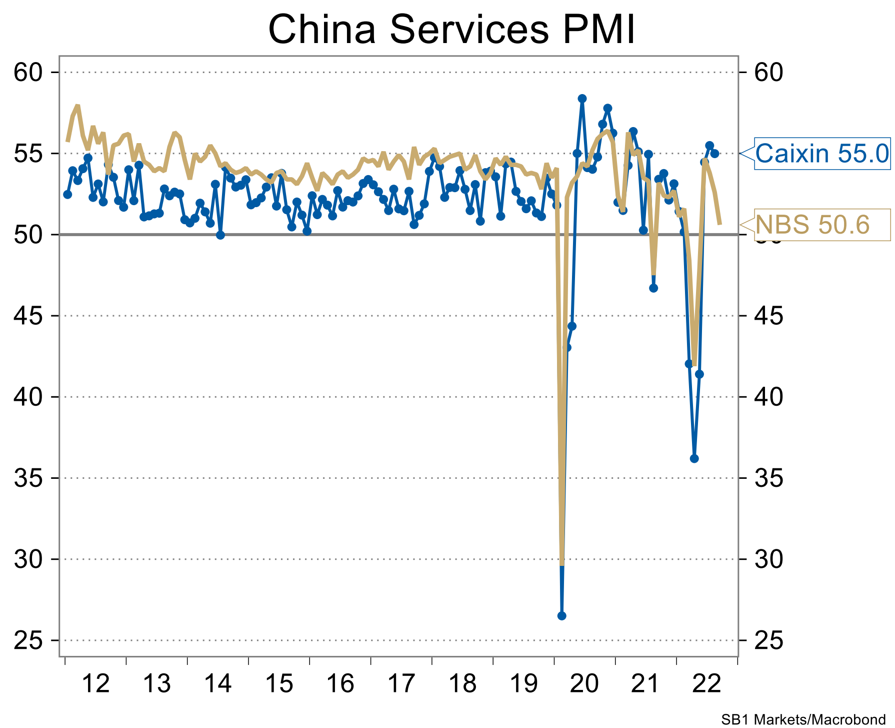
- Construction starts have continued downwards after the major lockdowns during the spring, and prices are falling. Thus, the fall in orders in Sept makes sense

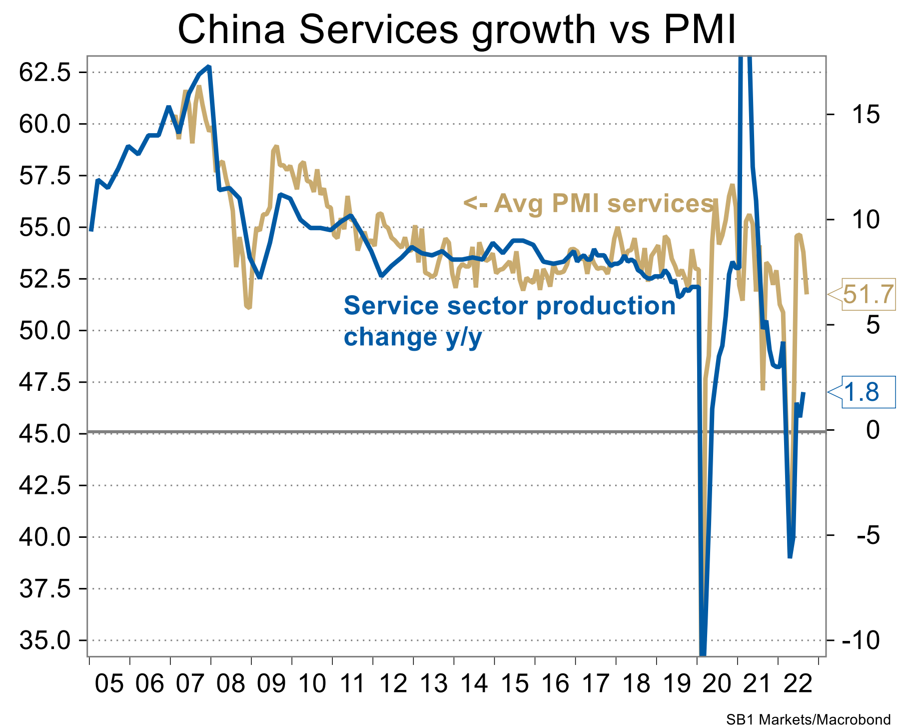




China's 'national' service sector PMI closing in on the 50-line in September

The CFLP services PMI came in a 50.6, down 2 p from August

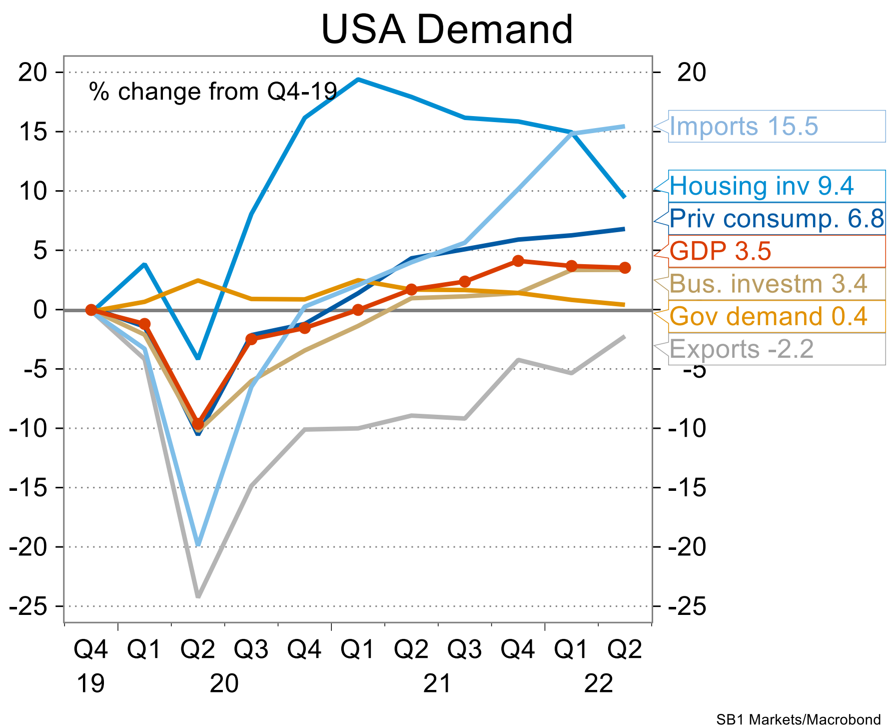




- S&P has not reported yet

GDP growth revised up, due to higher consumption and higher exports

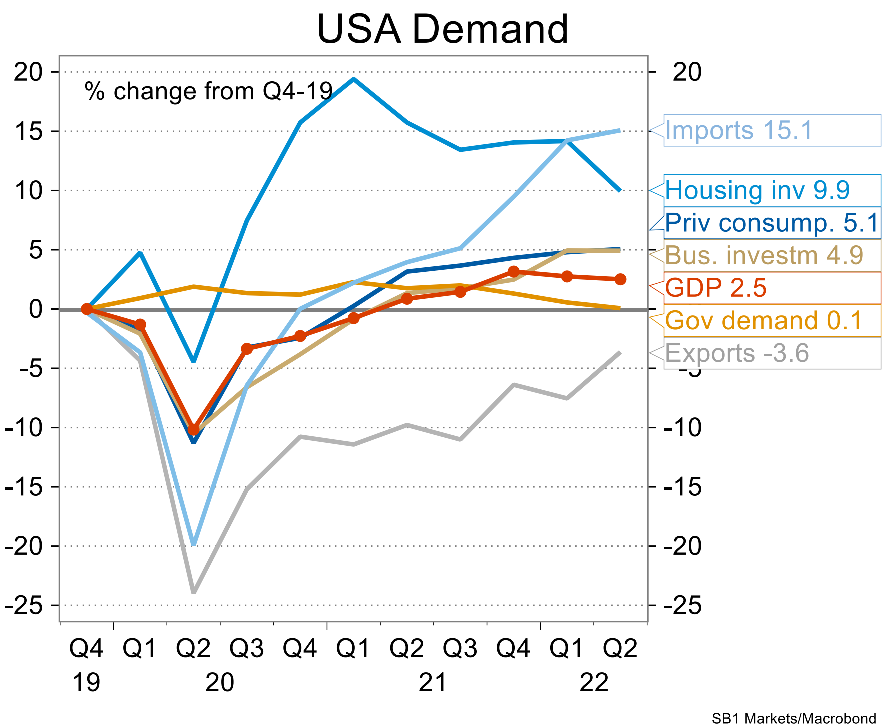
Business investments are revised down in the annual revision. The savings rate is revised visibly down



Hint: Flip between this page and the next

- Since before the pandemic:
  - GDP up 3.5%, up from previously reported 2.5%
  - Household consumption up 6.8% from 5.1%
  - Housing investments unchanged
  - Business investments down to 3.4% from 4.9%
  - Exports have fallen slightly less than assumed
  - Government demand up 0.4% vs prev. reported 0.1%
  - Household income close to unchanged but wage income growth has been slightly lower than assumed
  - Service sector production was revised upwards equalling 0.9% of GDP, goods production was upped equalling 0.1% of GDP
  - The savings rate was revised down by 1.5 pp and is now just at 3.5%
  - Price deflators (inflation) was revised up by 0.2 – 0.3 pp last year
  - The wage cost pressure is slightly less than previously assumed (wage inflation down, productivity has been growing slightly faster)
  - The recovery has been stronger than assumed, but at the same time with somewhat slower growth in costs
- Implications
  - In sum probably on the upside vs. Federal Reserve's view on the need for monetary tightening

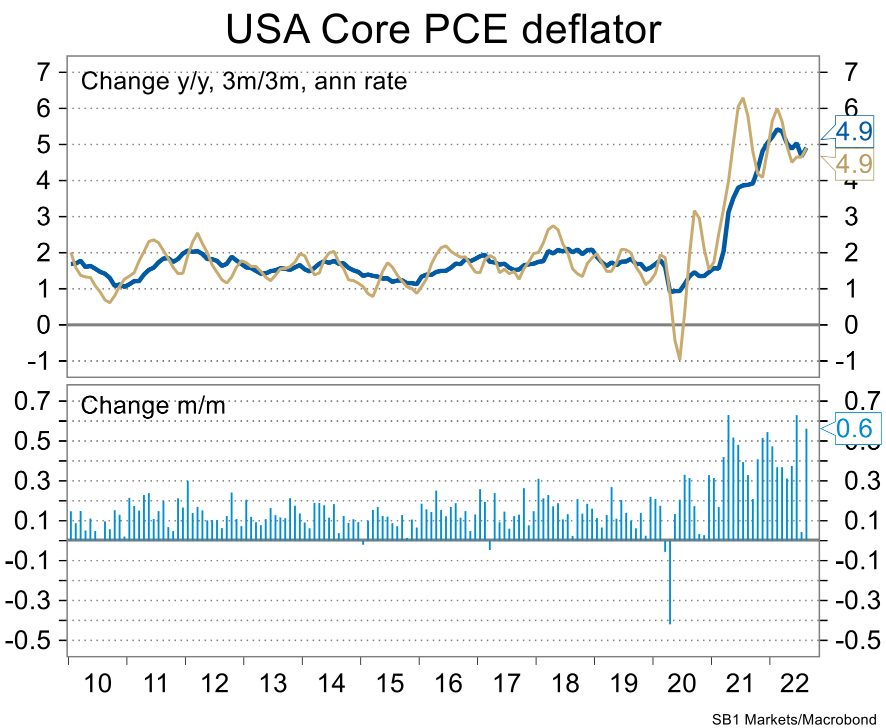
The main demand components before the revision:

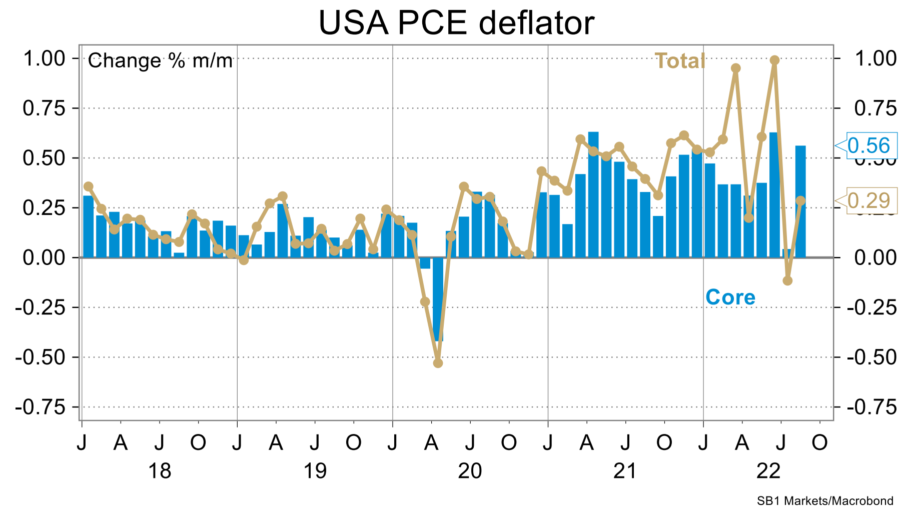


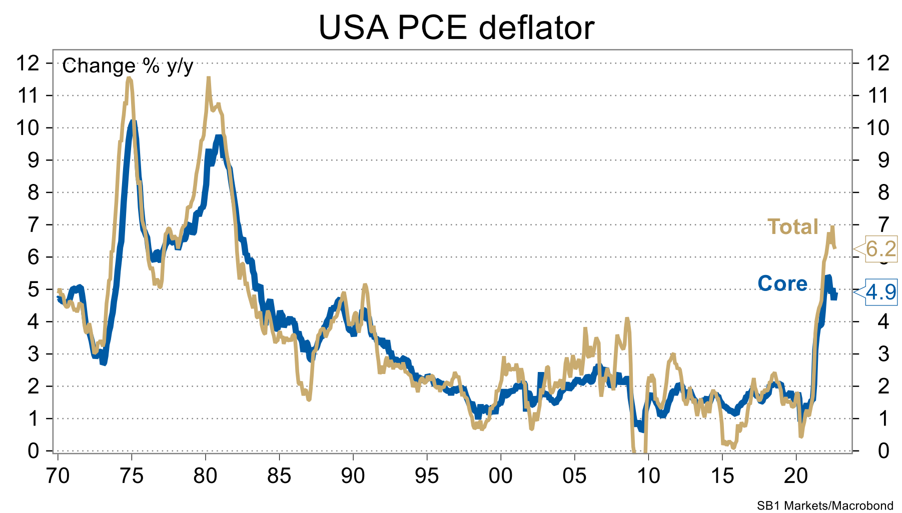
We have shaded the 'hard' pandemic quarters at the chart on the top

Core inflation revised up m/m – and higher than expected in August

The core PCE deflator rose by 0.6%, and is up 4.9% y/y, 0.1 – 0.2 pp higher than expected



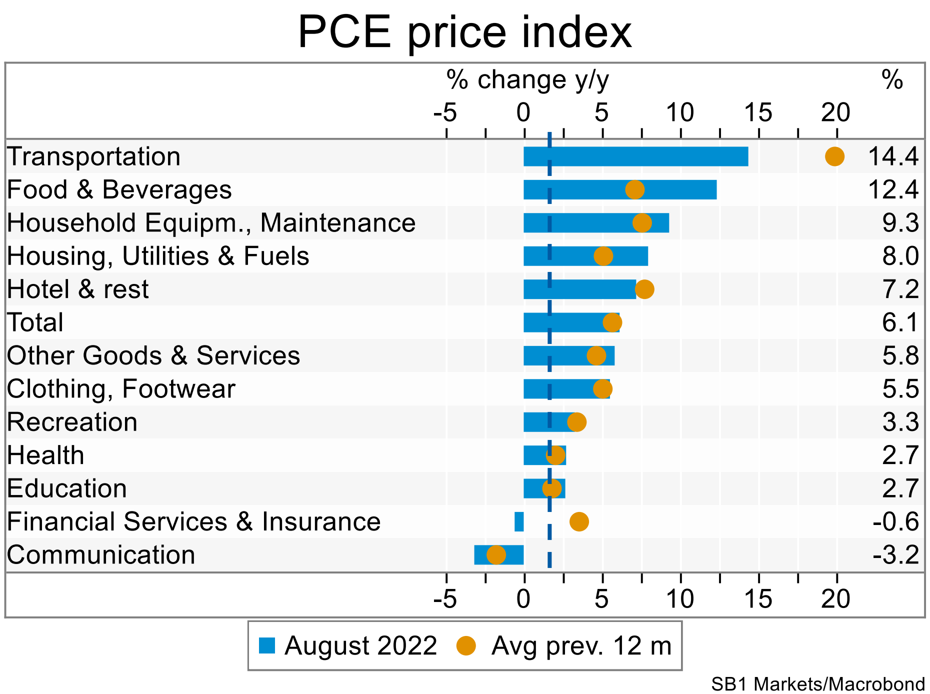


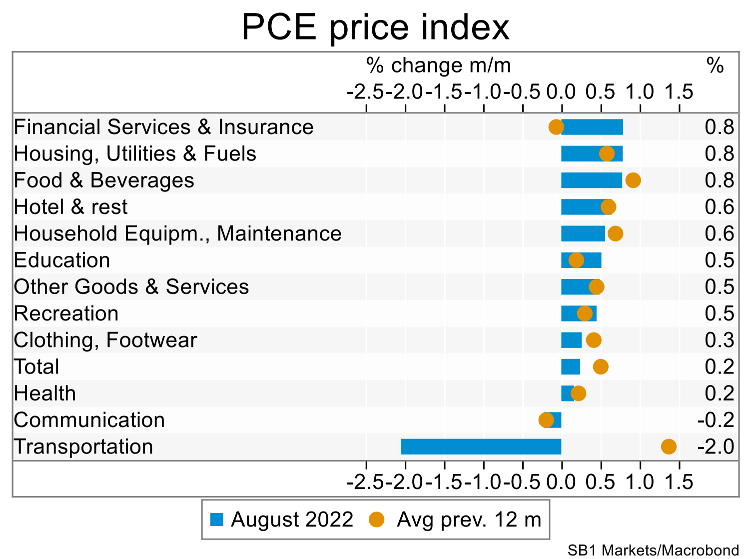


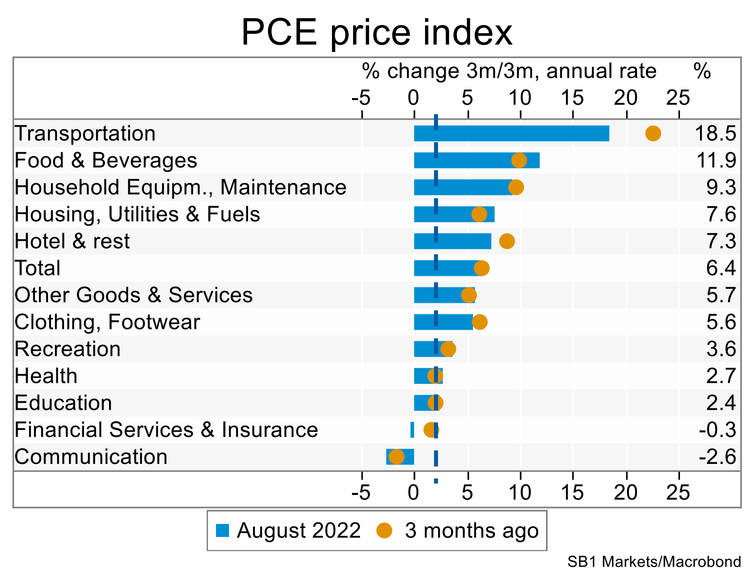
- **The total PCE deflator** also rose more than expected in August, up 0.3% and 6.2% y/y, both 0.2 pp higher than expected

PCE by main sectors: All but 2 sectors report >2% annual growth

… and all but 2 are up more than 2% measured 3m/3m, the total is up 6.4%

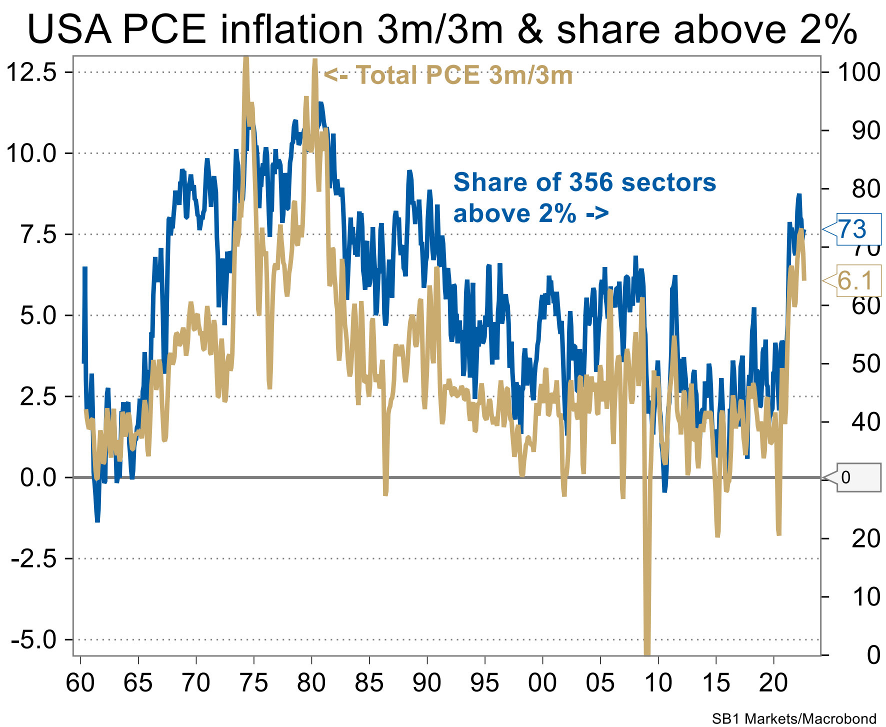


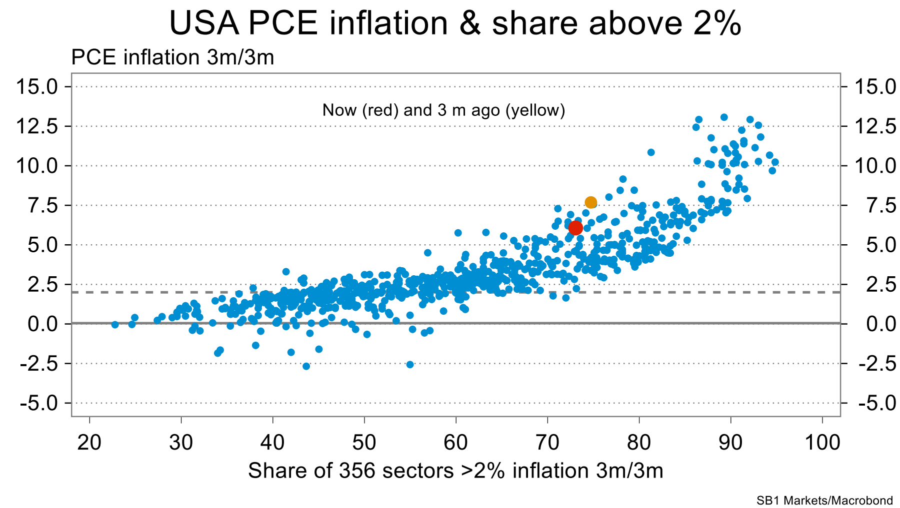


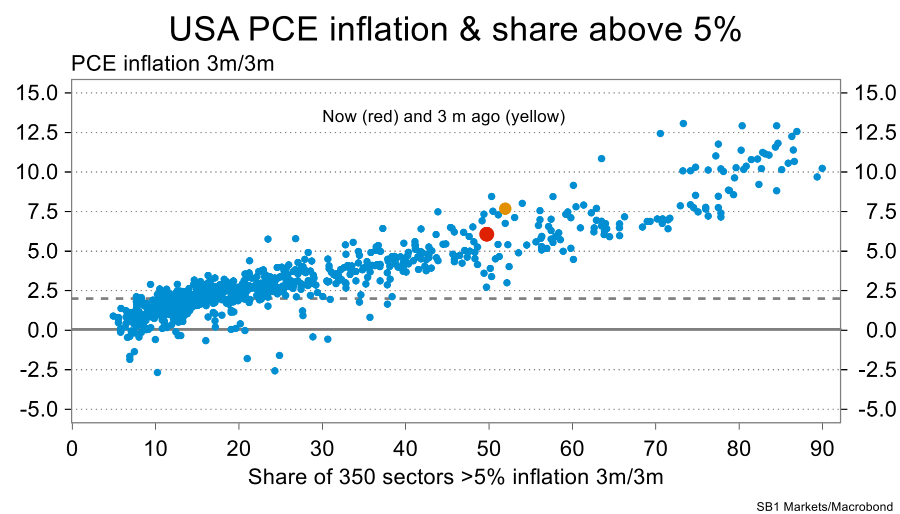


- Still, the momentum may be slowing as most sectors report somewhat lower growth 3m/3m than 3 months ago
- Transportation prices fell in August (gas & airfare tickets)

Inflation is still high and broad based – but it has peaked

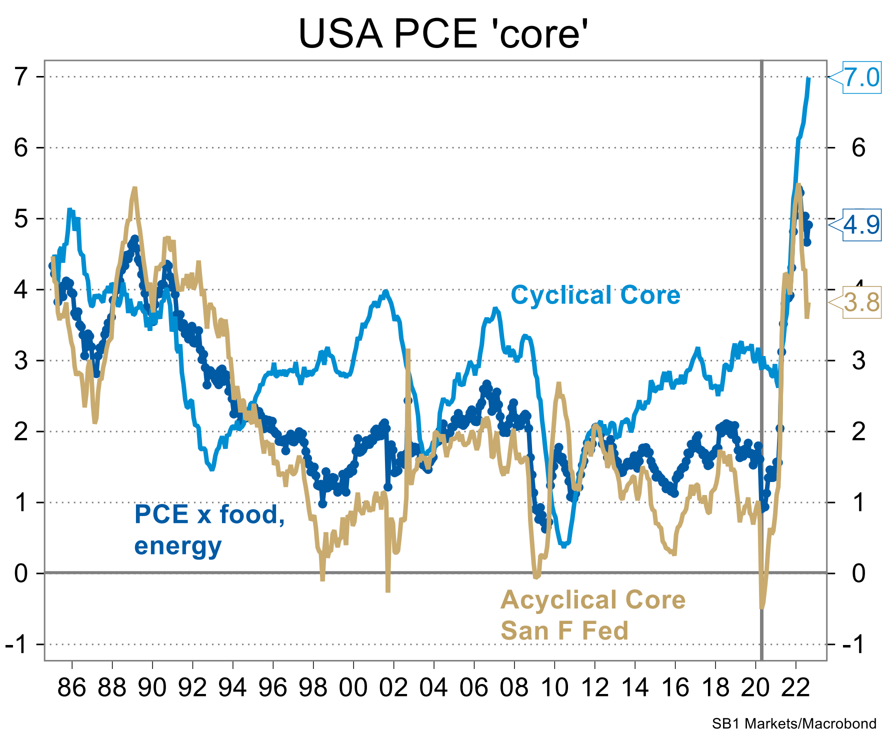


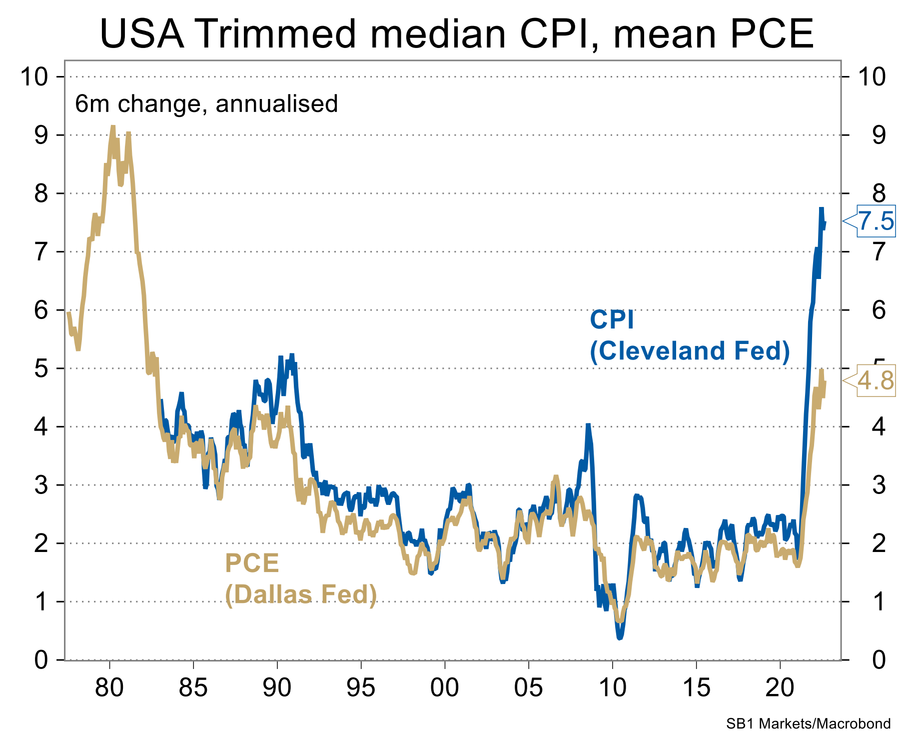




Inflation has peaked but remains high – and broad

A couple of months of ‘better’ data is not going to cut it for the Fed. Anyway, wages are more import.

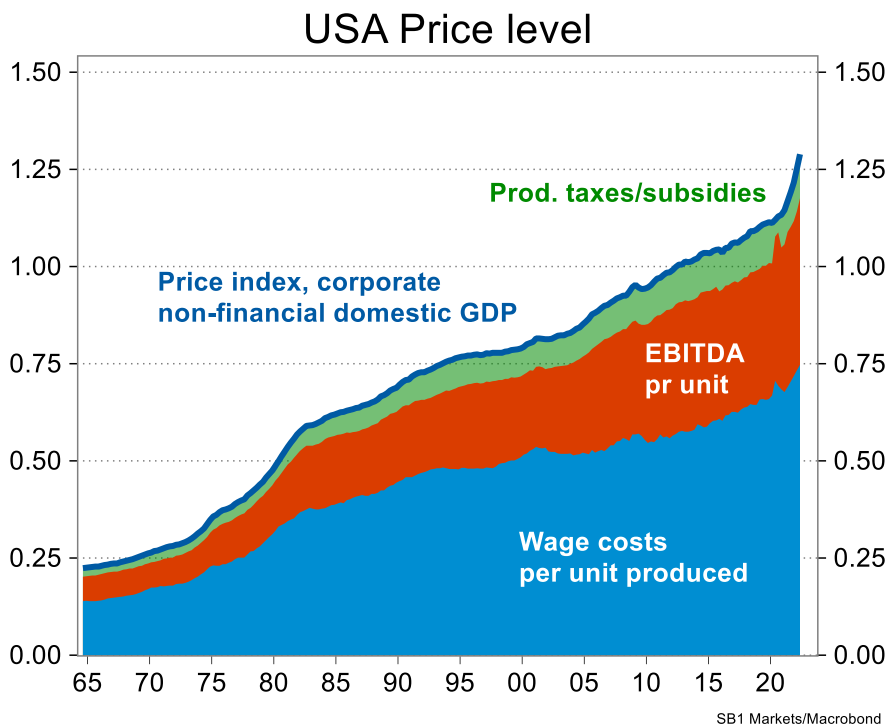


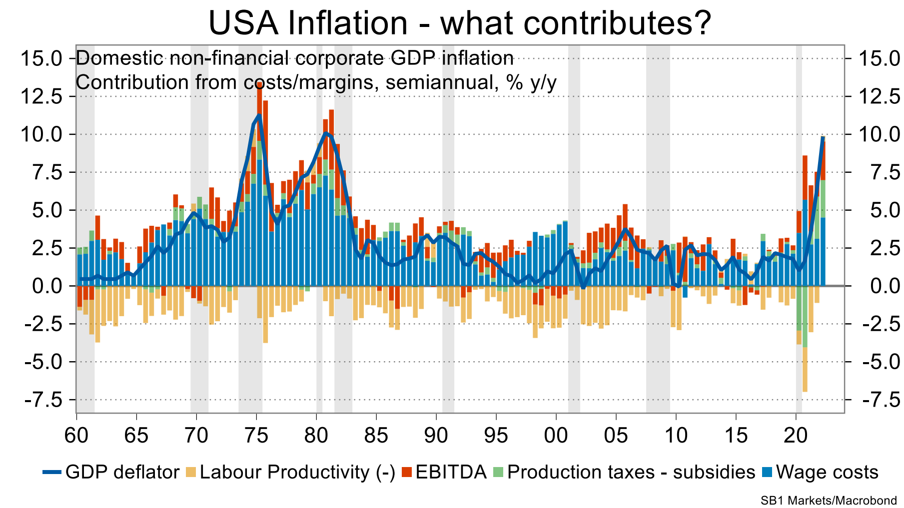


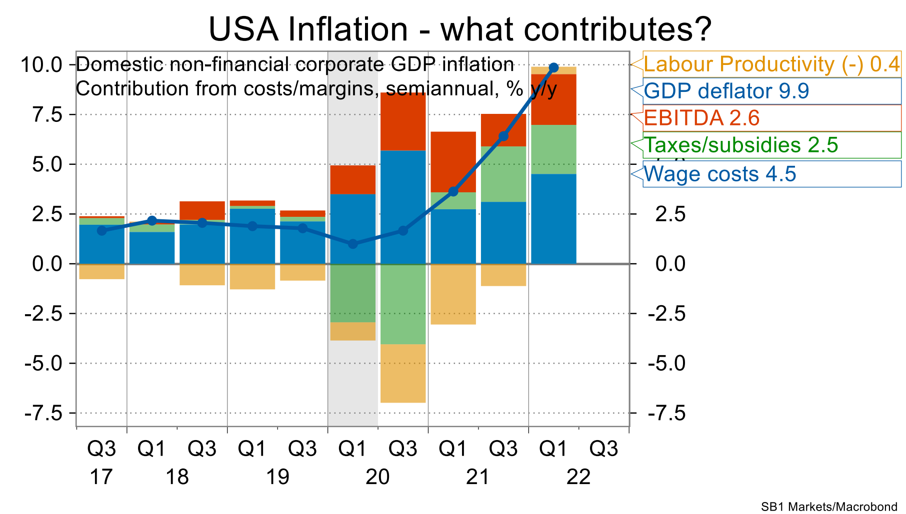
- The **trimmed PCE mean** (Dallas Fed) accelerated 0.5 pp to 4.8% (measured over the past 6 months). The peak was at 6% in June (revised up from 4.8%)
- **The trimmed median CPI (Cleveland Fed)** is up 7.5% over 6 months
- **Core cyclical and acyclical PCE** prices are up 7.0% – 3.8% resp., and the cyclicals are still on the way up
- Other measures of underlying inflation are also still among the highest levels in 30 – 40 years

Margin expansion a main driver for high inflation

Prices are up 10% for goods/services produced in US businesses. Higher margins explains ¼



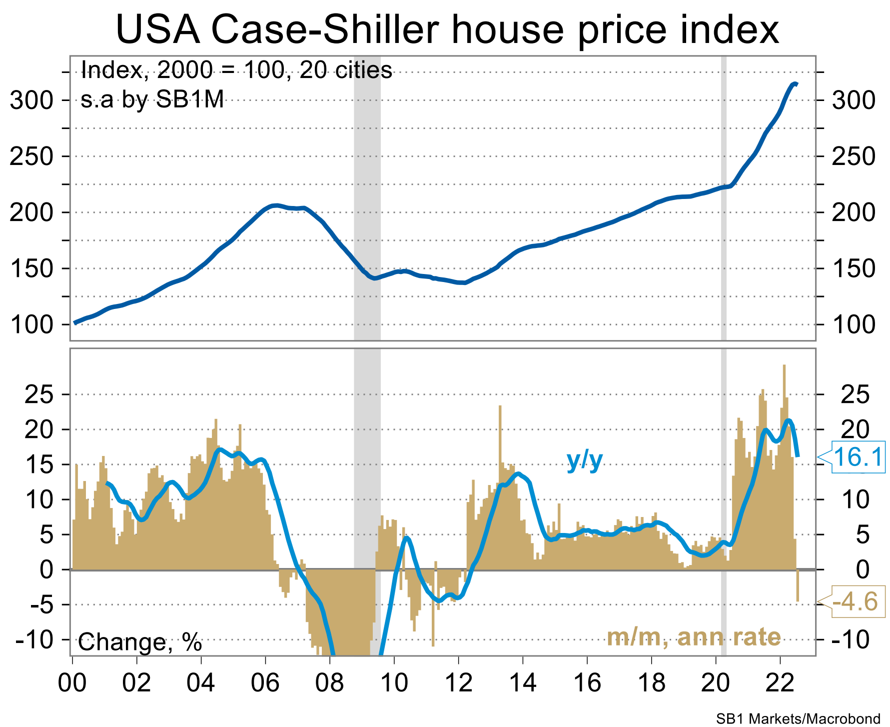


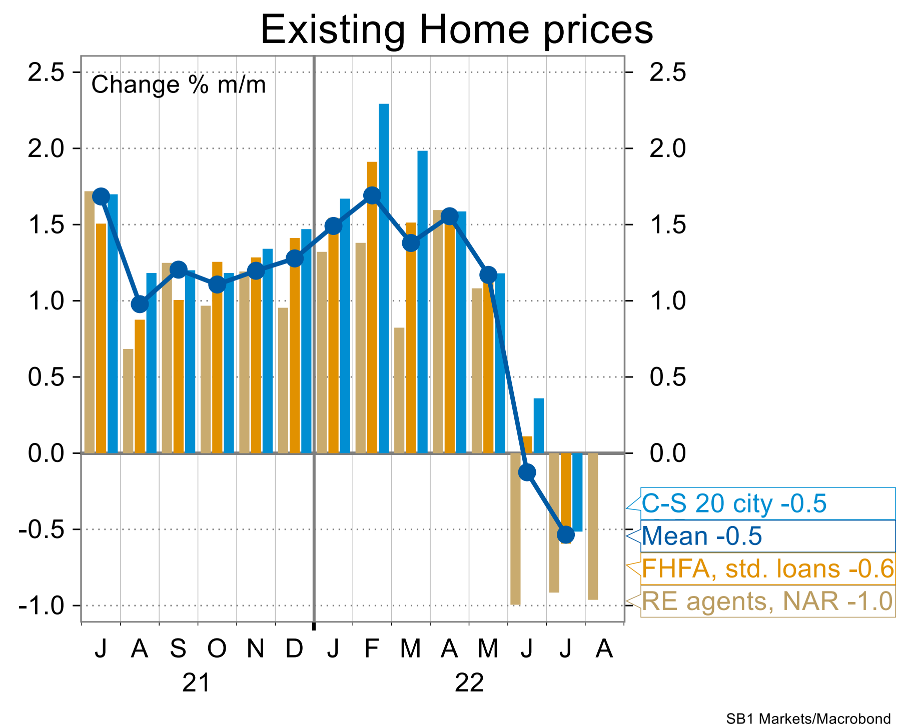


- The main contributor is – as it should be – higher wage costs. However, the 4.5% contribution due to higher wages is far more than what is sustainable vs the 2% price target. In addition productivity has fallen y/y, pushing Unit Labour Costs further up. Net taxes/subsidies are also up as covid support programs are scaled back (but as profits rose when they are distributed, it would not have been surprising if profits were normalised when they were abolished – but profits rose further

Now it is ‘official’: *House prices are falling*, as the realtors have told us

Case/Shiller reported a ‘surprising’ 0.5% fall in prices in July

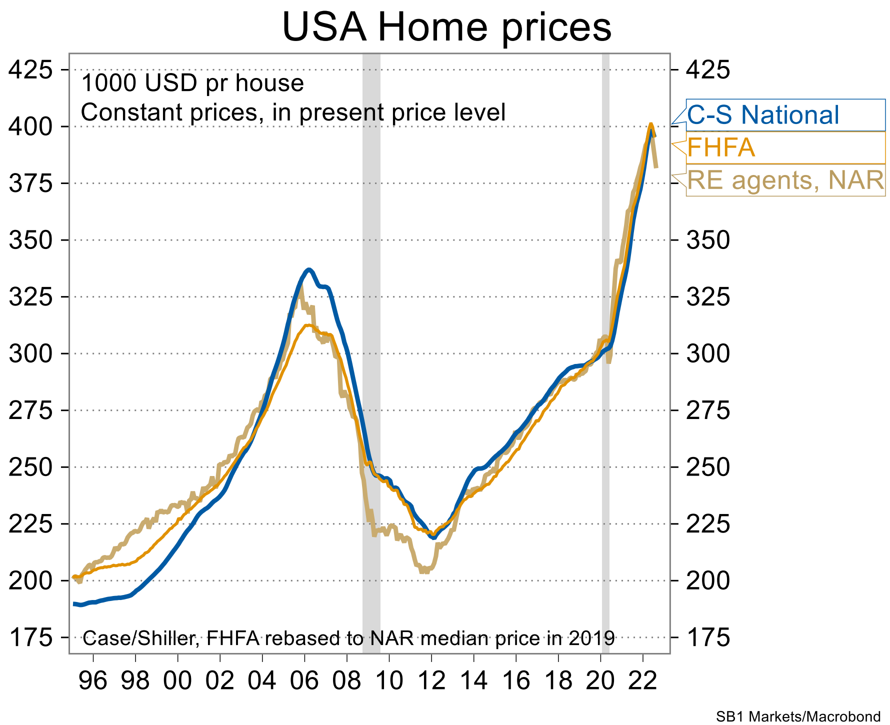


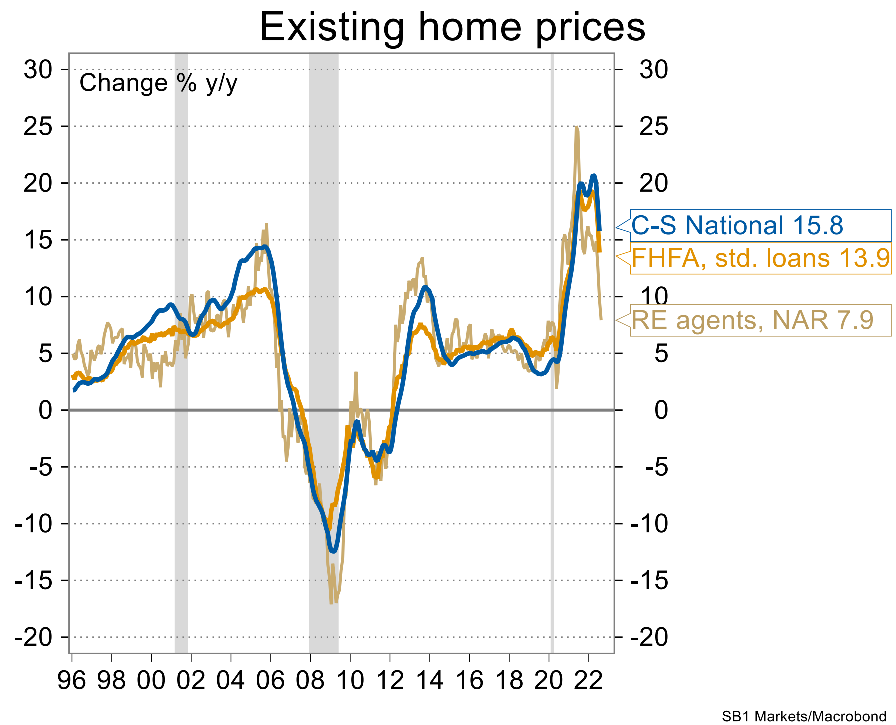


- **S&P’s Case/Shiller’s 20 cities** price index fell by 0.4% m/m in July (June - Aug avg., our seas. adj, 0.5% by the ‘official’ seasonal adjustment) equalling a -4.6% annualised pace – A 0.2% <u>increase</u> was expected. Thus, the outcome was 0.7 pp lower than expected, for the 3-month average. Something must have happened in the last month! The index is still up 16.1% - down from 18.6% in June, and 1 pp lower than expected!
- **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), was down 0.6% in July, and is up close to 14% y/y
- **Realtors** reported a 1% decline in August, following a 0.9% drop in July and 1% drop in June. Prices are still up 7.9% y/y– but the annual rate is now ‘collapsing’
- <u>We still expect prices to yield substantially the coming months, following the unprecedented 40% lift since before the pandemic, and the surge in mortgage rates, up to 6.5% (30 y fixed), from 4% before the pandemic</u>

The downside is HUGE, following the 40%+ house price appreciation from Feb-20

Were real house prices too low before the pandemic? Probably not. Can they fall back? Not unlikely

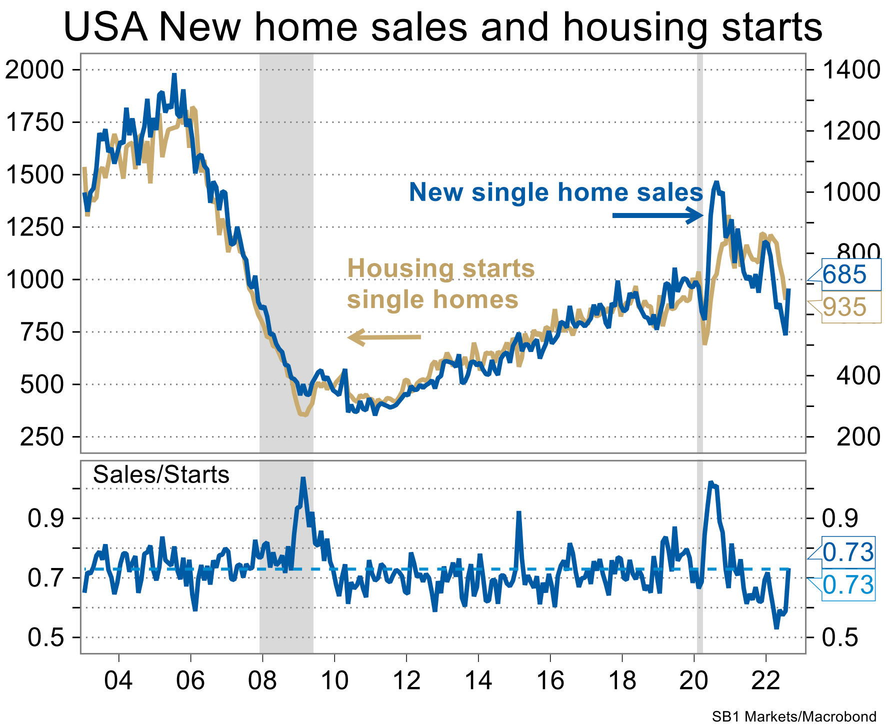


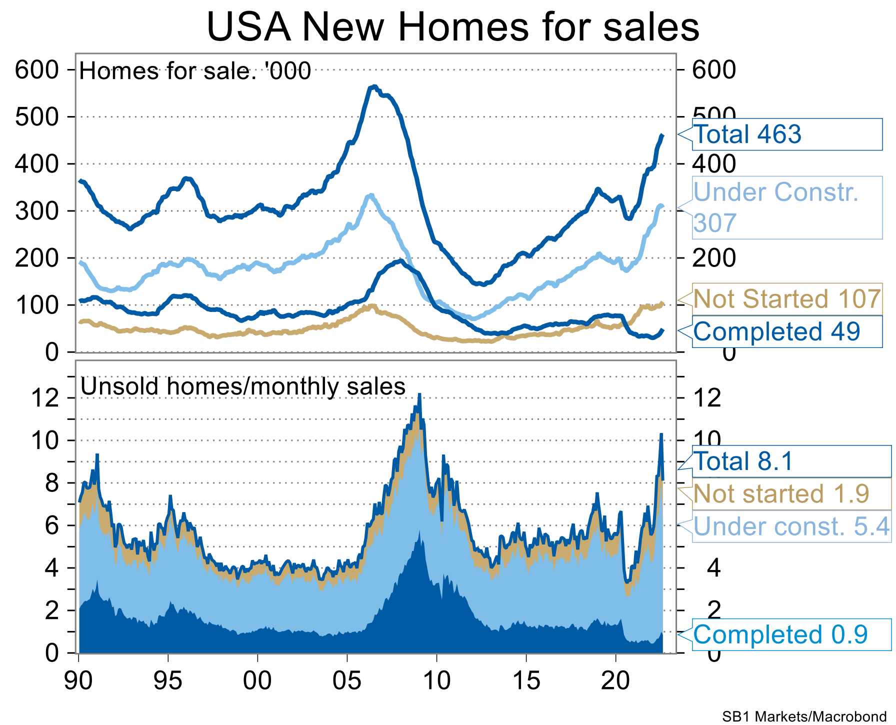


- Real prices are far above the pre-financial crisis level too
- There are still some big differences vs the mid 2000 housing bubble
  - » **Housing starts** are at a lower level. The **inventory** of second-hand homes for sale is still close to record low (vs high 15 – 16 years ago). However, the inventory 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, and housing affordability is far below the 2006 level
  - » The **savings rate/net financial investments rates** have now fallen to well below the pre-pandemic level – but the ratios are above the level in 2005

New home sales suddenly up almost 30% - but very likely just a one-off

Sales are trending rapidly down and homebuilders have reported further decline in sales



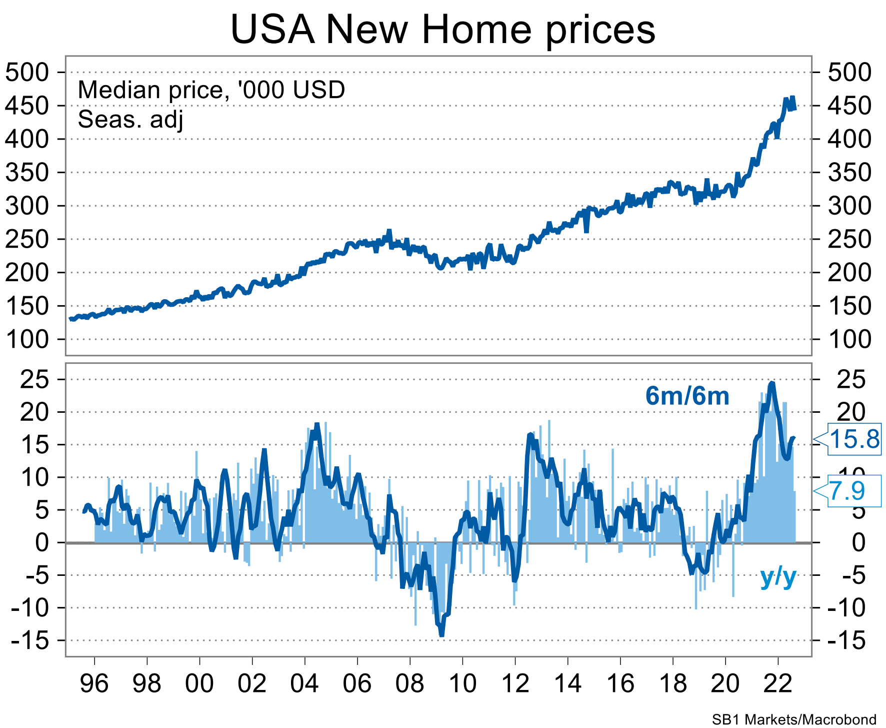


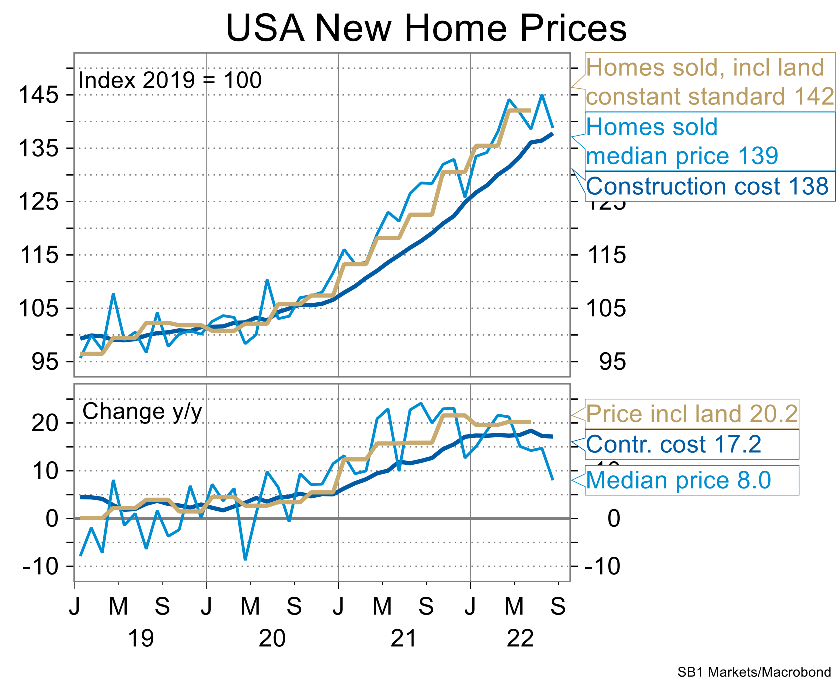
- **New single home sales** shot up 685' August, from 532' in July, expected down to 500' from previously reported 511' (annual rate). Even if sales surprised sharply on the upside, the decline the previous months with the setback in building permits sends a clear recession signal (*check 2 pages forward*)
- **The inventory of unsold homes** rose further in August to 463' units, up from below 300' in Aug-20. Measured in month's of sales, inventories equal 8.1 months, from the record low at 3 months in Aug-20. Most of the inventory is 'for real', either completed homes (but the level in this category is still very low) or under construction (and these homes will be completed) – as the supply side responded to the strong increase in demand & prices. A steep increase in number of homes for sales that are not yet started, also confirms the strength of the potential supply side (but most of these projects will very likely not be started as at least the housing market has entered a recession)
- Prices increased slightly in July but prices are now on the way down, the peak was in April. Still, prices are up 8% y/y

SpareBank 1 MARKETS

New home prices have flattened. Soon they will start declining? Very likely

The median price index is volatile and badly constructed – but something seems to be underway

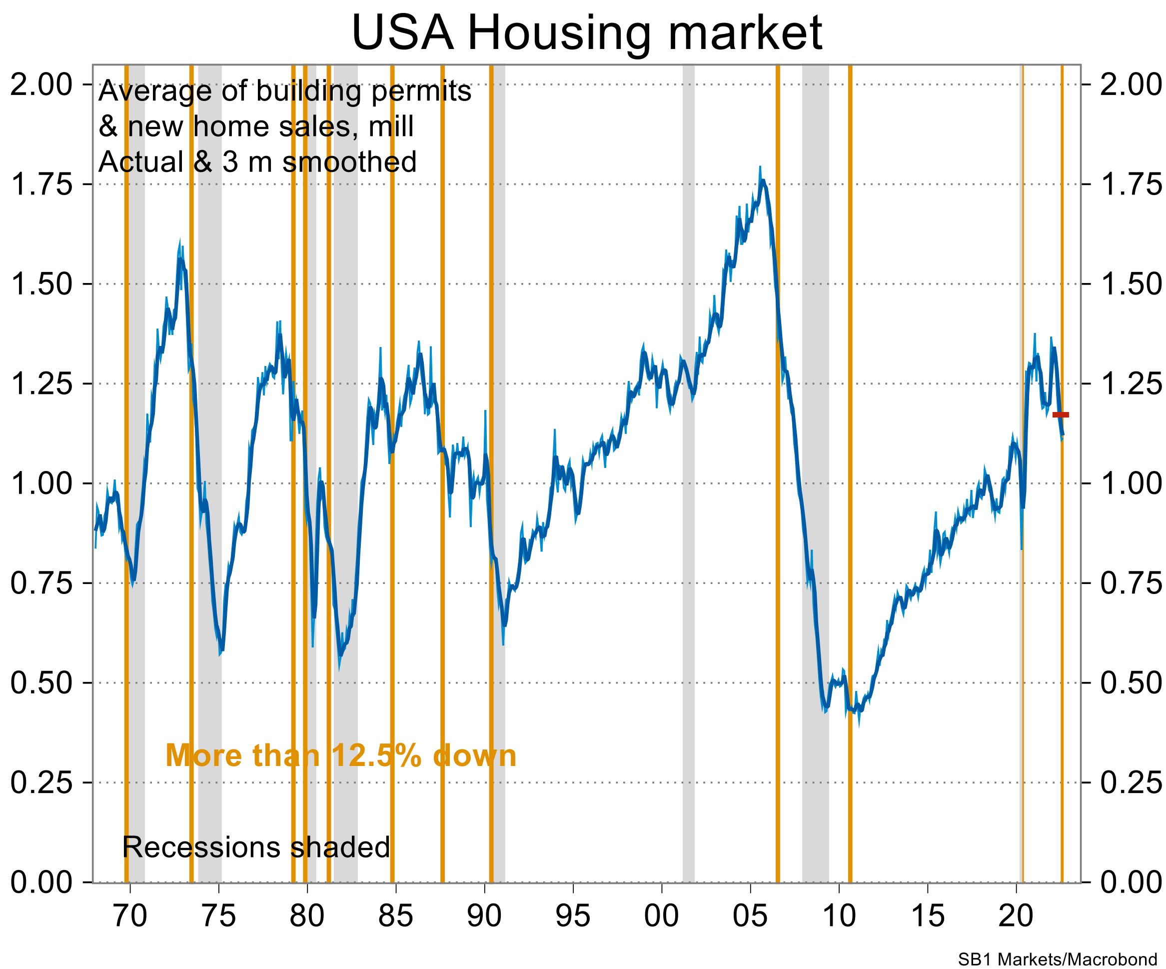


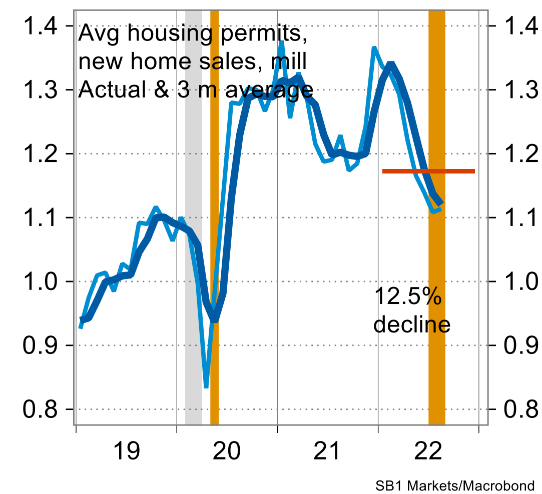


- The monthly **median new home sales prices** are very volatile, as they are not adjusted for changes in the mix of homes sold. In August, prices were up 7.9% y/y, down from above 20% at the peak
- The **construction price index** is adjusted for changes in standard and size, as is the **new homes sold price index**, which also includes cost of land: they are up by 17% (in August) and 20% (Q2) resp. Construction cost inflation is very likely peaking now, as material prices are nosediving
  - » Prices incl. land is still growing faster than construction costs, signalling strong demand for new homes. We expect the sign to change soon, as land prices should ease more than construction cost if demand for housing eases

Housing vs. recessions: We have crossed the red line!

The combined decline in new home sales & building permits has crossed a recession warning line

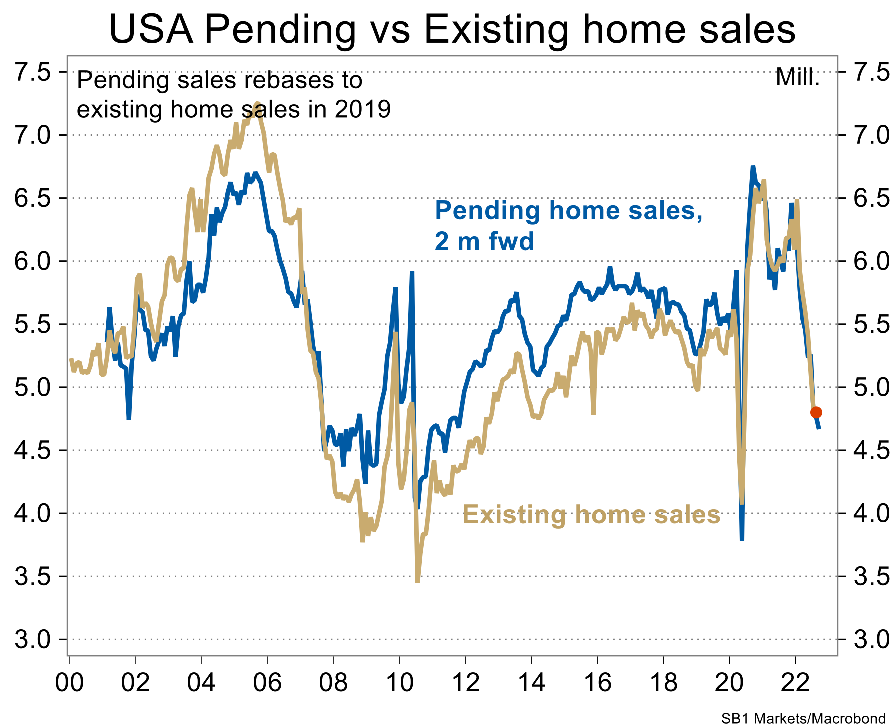


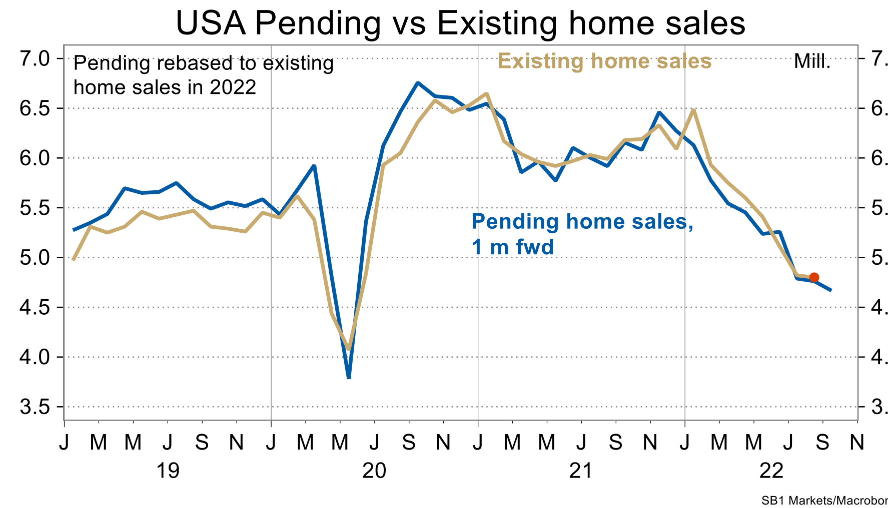


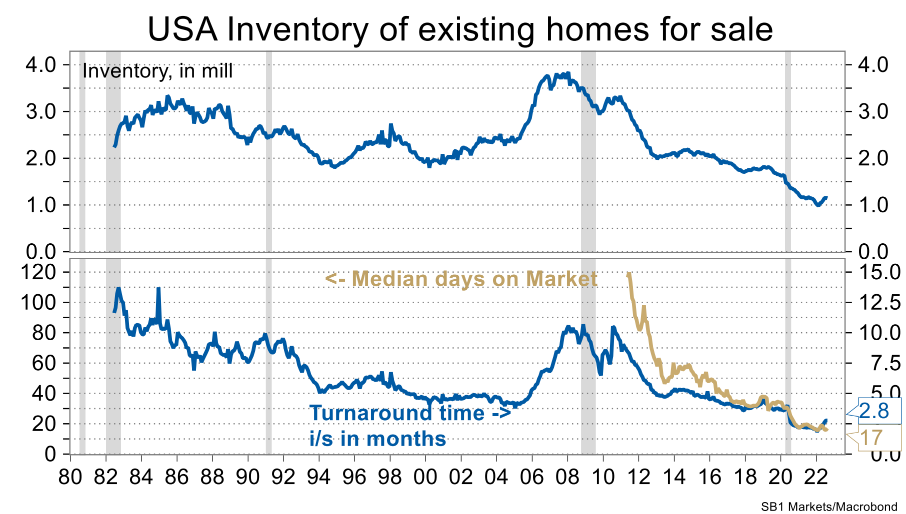
- Most recessions are 'housing recessions' as demand for housing and residential investments decline substantially ahead of and during recessions
  - » The only exception in recent decades was the 'Nasdaq' recession in 2001
  - » In addition, the pandemic recession was not caused by a setback in the housing market
- On the charts, we have marked declines of more than 12.5% in the 3 m average of the average of building permits and new homes sales vs. the recent 12 m peak with a yellow line
  - » 1984 and 1987, where interest rates were hiked, and a soft landing (and no recession) followed even if housing sent a signal (The 2010 decline was just after the GFC)
  - » The other 7 lines: A recession followed

Pending home sales further down in August

No. of agreed transactions fell 2%, and is down 28% from last November, a substantial decline







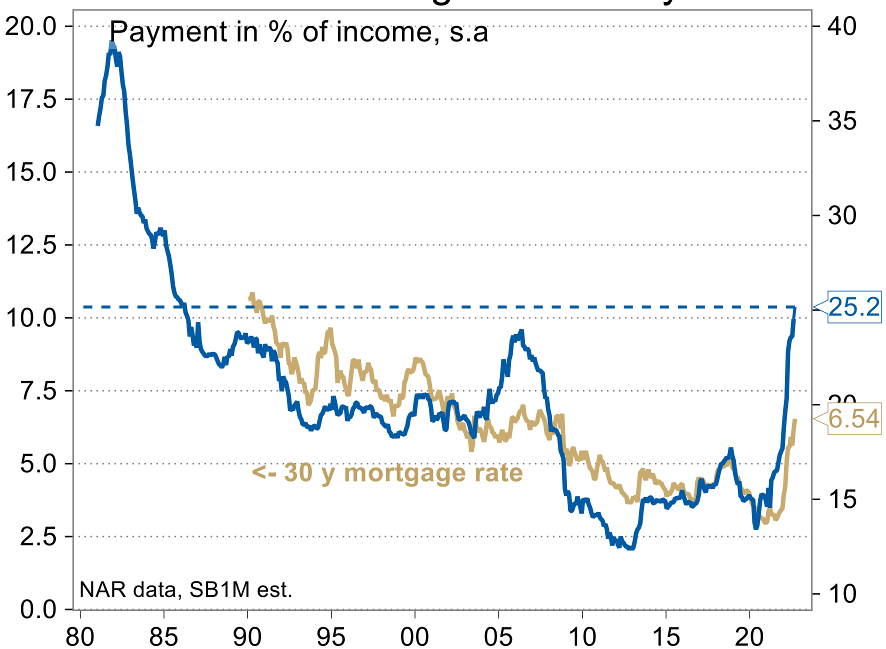
- The decline in June was slightly larger than expected (1.4%) – and the trend is straight down
- The decline confirms that higher mortgage rates <u>are</u> slowing the housing market

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

A mortgage market meltdown, the margin to 30 y gov bond unprecedented!

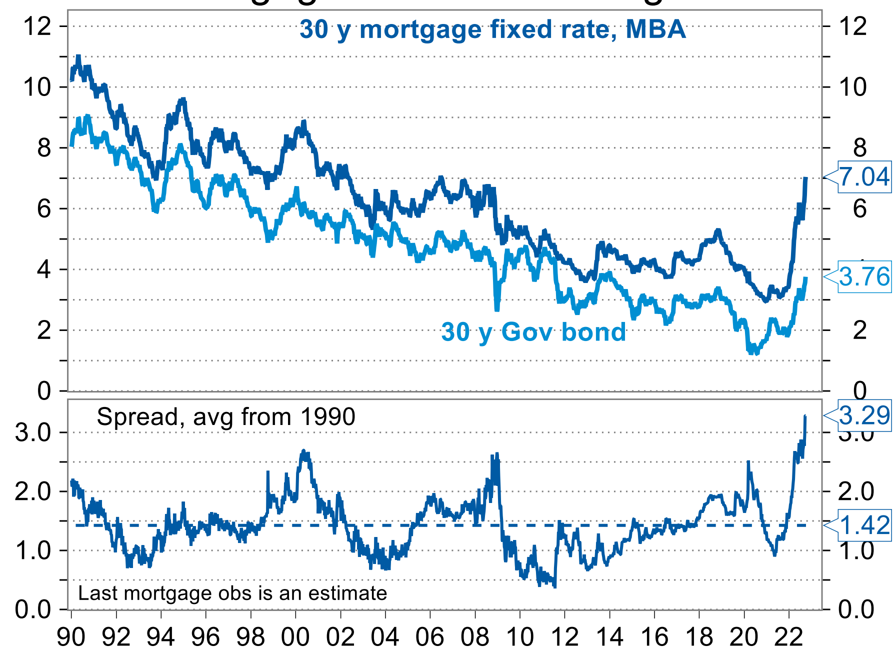
The effective mortgage crossed the 7% line last week. Will the Fed be forced to do a 'BoE'?

USA Housing Affordability



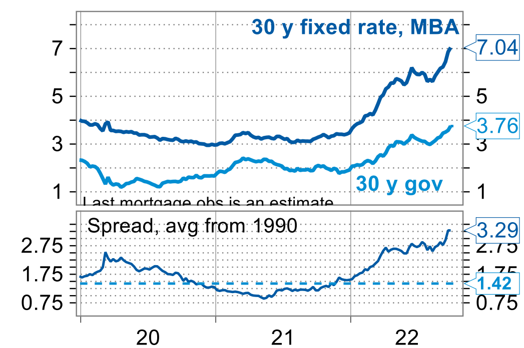
SB1 Markets/Macrobond

USA Mortgage interest rate vs gov bonds

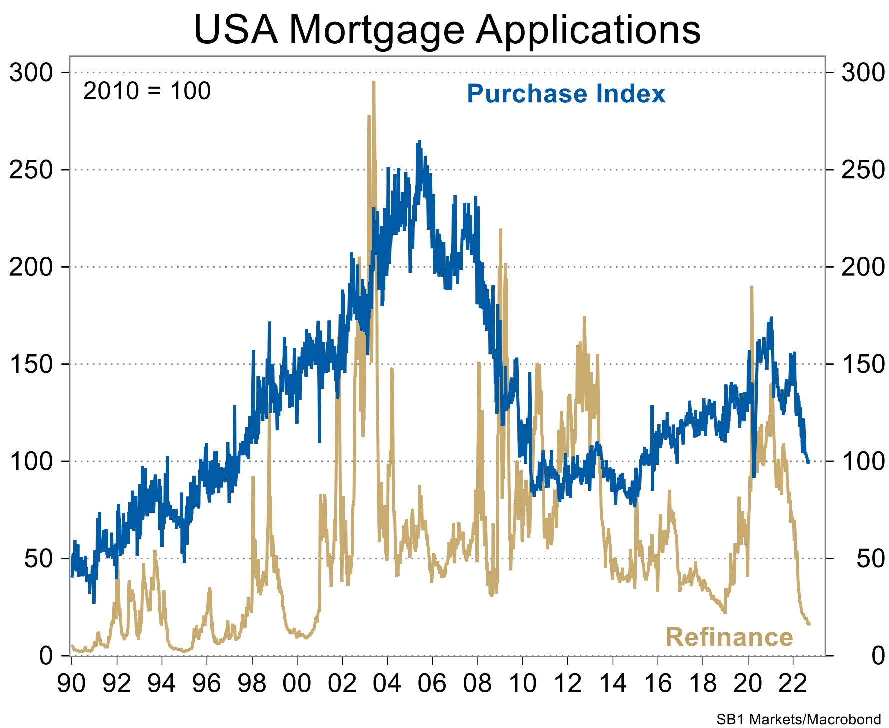


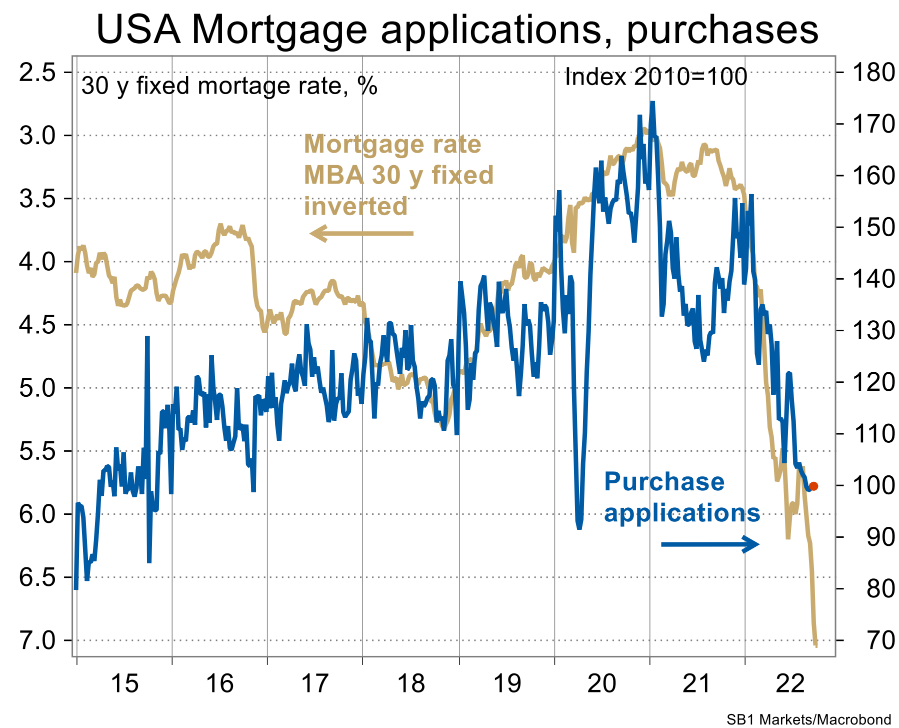
SB1 Markets/Macrobond

- The 30 y fixed mortgage rate shot up last week as the 30 y treasury bond yield rose sharply, and the spread has widened dramatically recent weeks, to levels we have not seen before (data from 1990). The spread was 0.9 pp at the bottom when the Federal Reserve snapped up all net mortgage bond issuances even if prices rose 20% y/y. Now the Fed is selling mortgage backed bonds, and the spread is above 3%
- At which stage will the Fed decide that the market is not working, and that is has to start buying bonds again, just like the Bank of England had to do in order to prevent a completely meltdown in the UK gilt market last week? We think that we are not that far away, probably far less than 100 bps
- Housing affordability (house price x mortgage rate/income) is the deteriorating by the day – to the worst level since 1986!



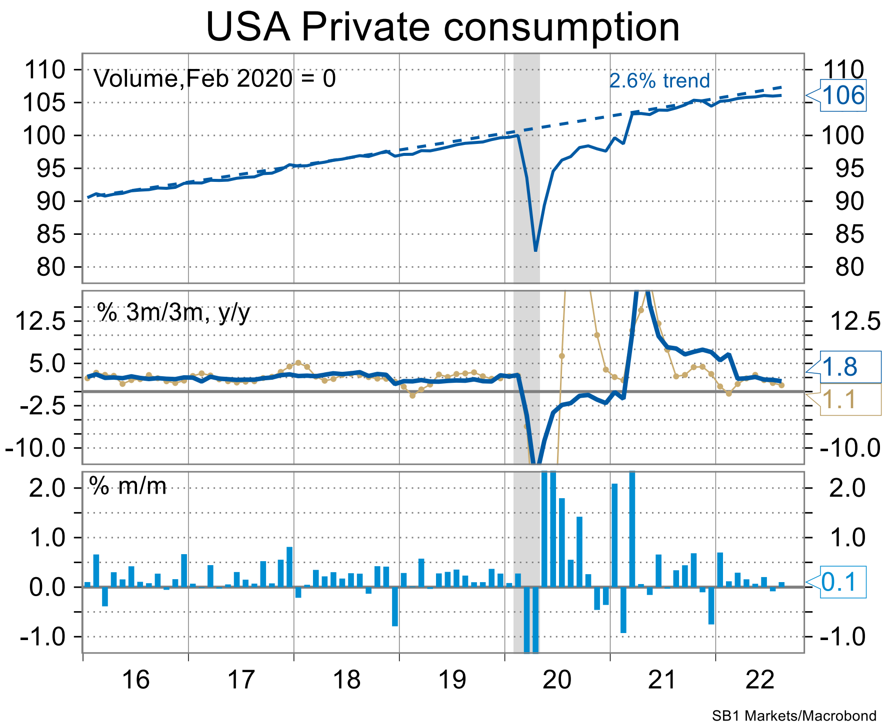
Demand for new mortgages will no doubt take a new hit

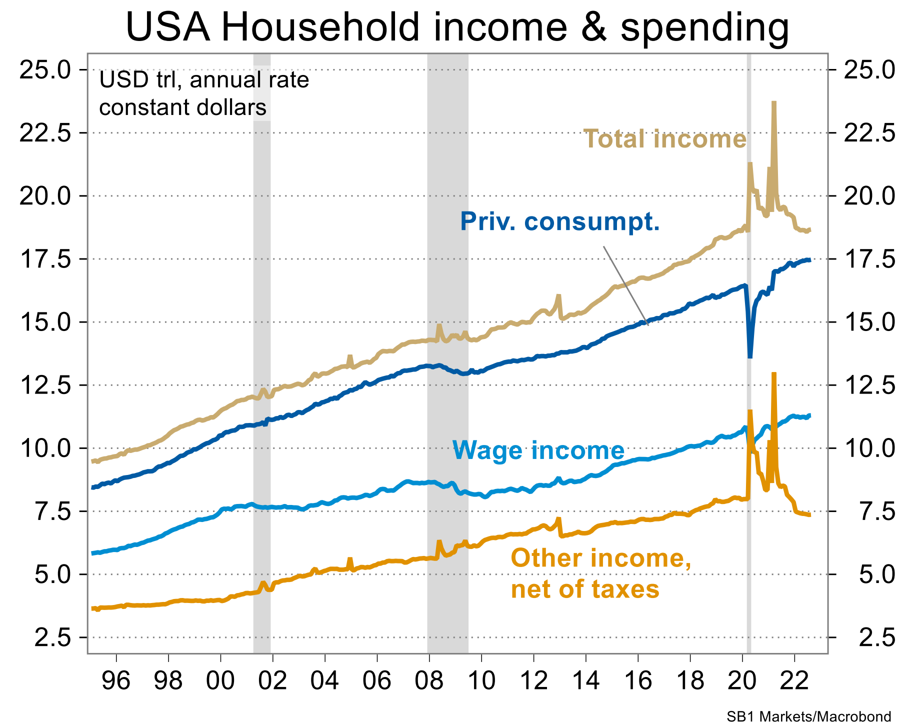




Consumption is flattening

Consumption grew 0.1% in August, as expected. Real incomes are trending down, as prices soar

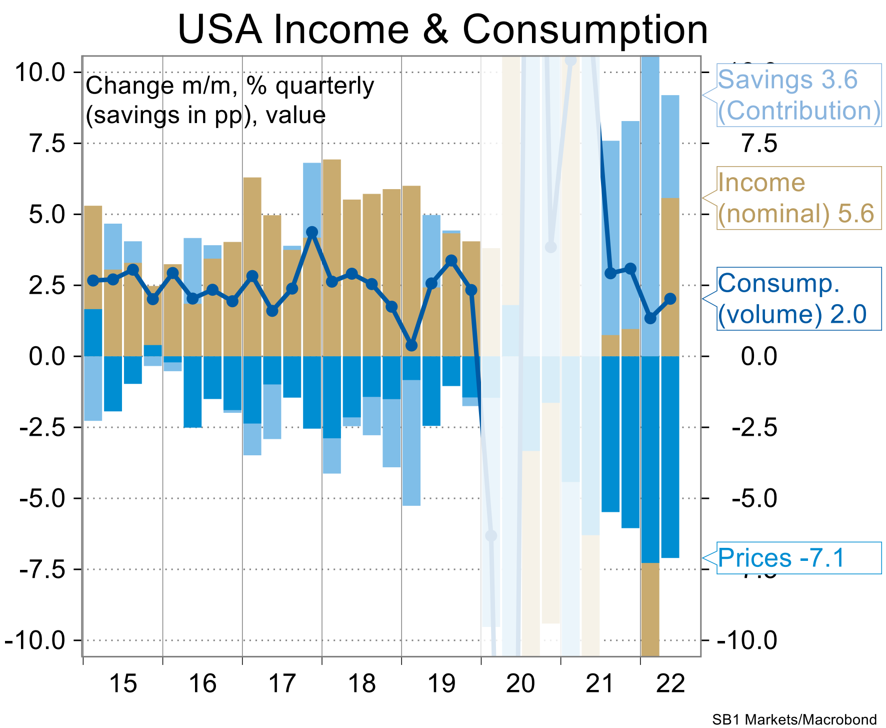


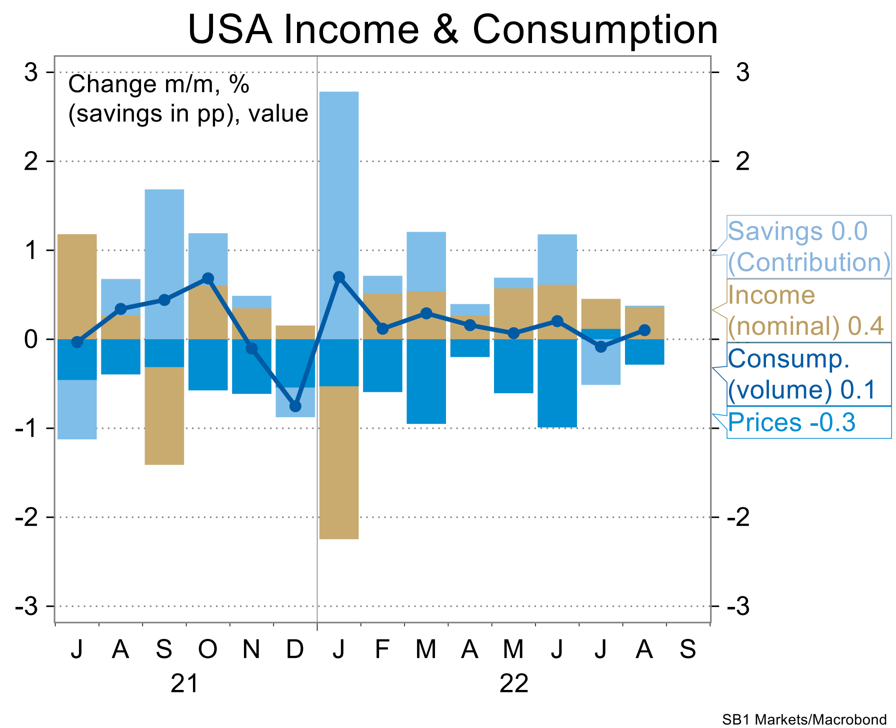


- **Private consumption** rose 0.1% in real terms in August, as expected, but growth in July was revised down by 0.3 pp to -0.1%. Nominal spending rose 0.4%, expected 0.2%. Prices rose 0.3%, 0.2 pp more than expected
  - » Consumption of goods fell, services are still on the way up
  - » History was revised slightly up since late 2020
- **Personal nominal disposable income** gained 0.4% in August, and was up by 0.1% in real terms. Real disposable income is trending down, due to normalisation of transfers, and higher taxes – and very high inflation
- **The savings rate** was flat at 3.5%, following a 1.5 pp downward revision – and is now some 4% below the pre-pandemic level. However, even if the accumulated extraordinary savings through the pandemic is now run down, most of the Wall of Money is still intact which may make it possible for households to keep up the level of spending (at least for those who saved…)

Prices rose 0.3% in August, and consumption gained 0.1%

Nominal income growth was strong in Q2, but as slowed somewhat in July/August

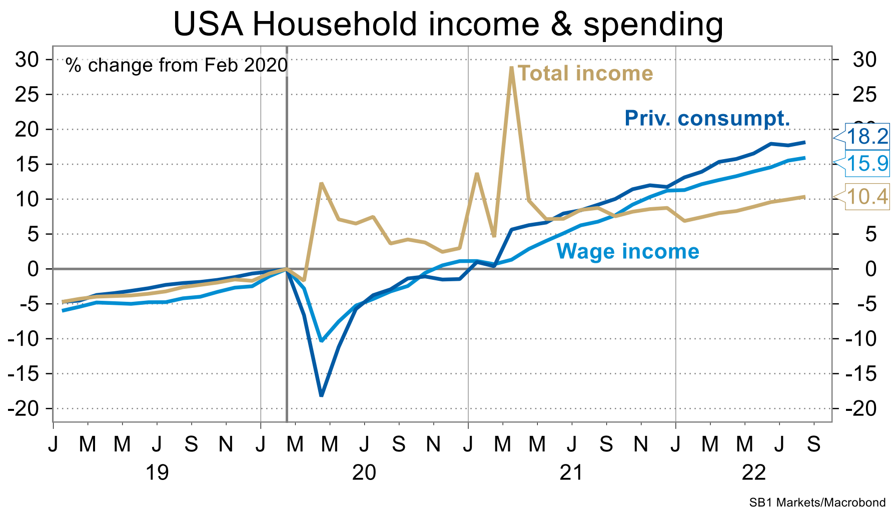


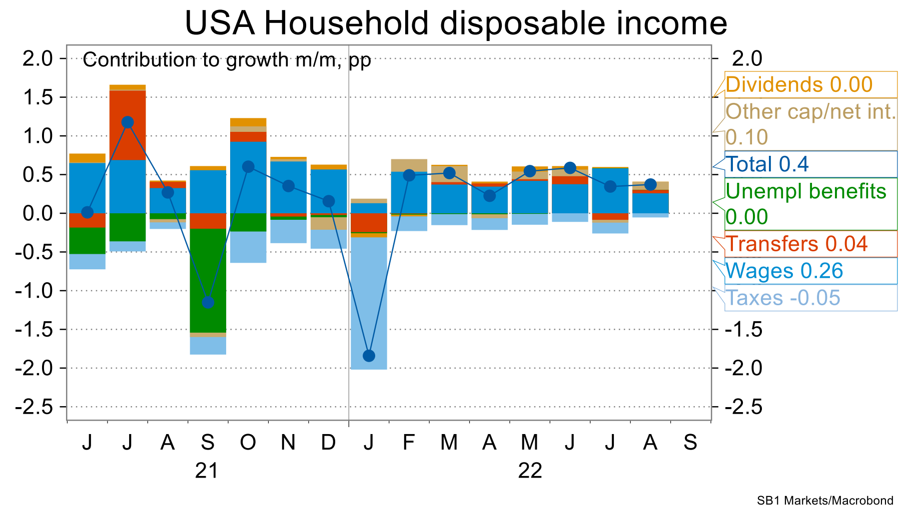


We have shaded the 'hard' pandemic quarters at the chart to the left

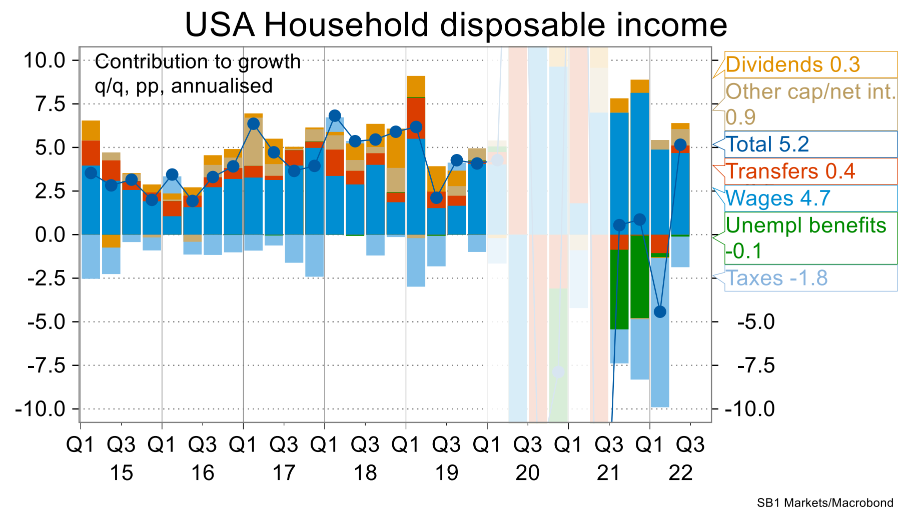
Income growth still higher than normal, nominally – by some 0.4% per month

Wage revenues continue upwards, but less transfers, and other income weaker



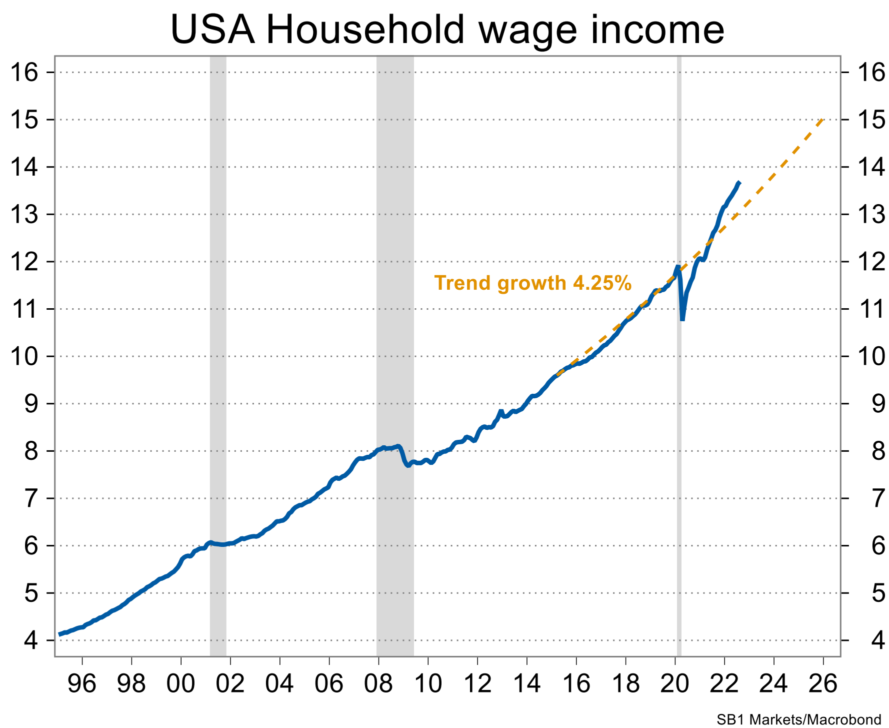


- **Total household disposable income** flattened from the spring in 2021 to early 2022 but has been trending upwards since January. Household income fell in Q1 due to higher tax payments but rose sharply again in Q2
- **Total wage income** is growing rapidly and the level is far above the pre-pandemic growth path at 4.25%, even if employment & hours worked remain below the pre-pandemic level (check the chart on the next page). The reason is of course the sharp increase in wage inflation. Wage growth was revised somewhat down in the annual revision



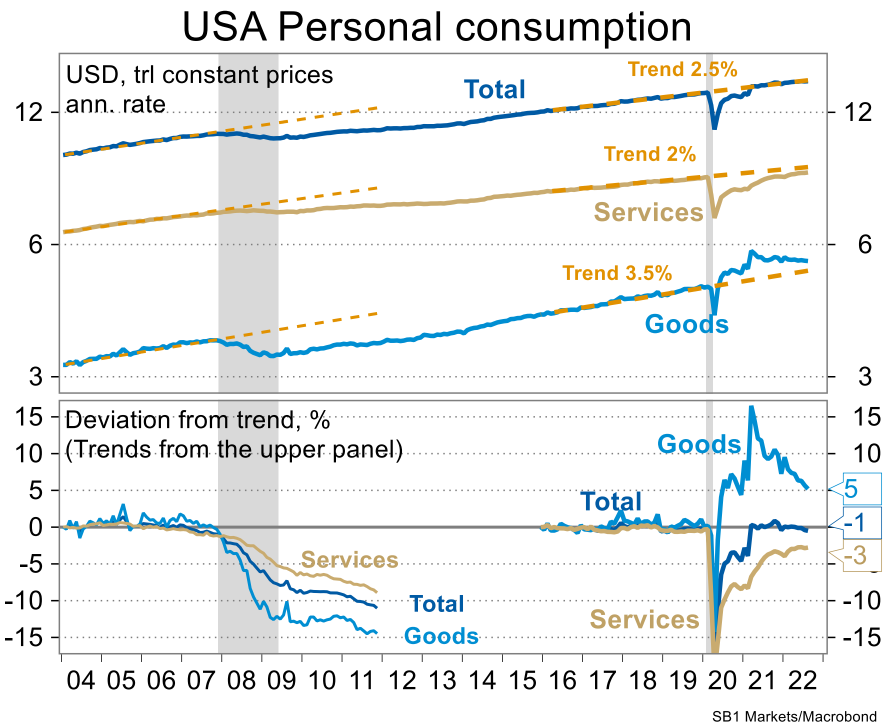
We have shaded the 'hard' pandemic quarters at the lower right chart, as these data make no sense now

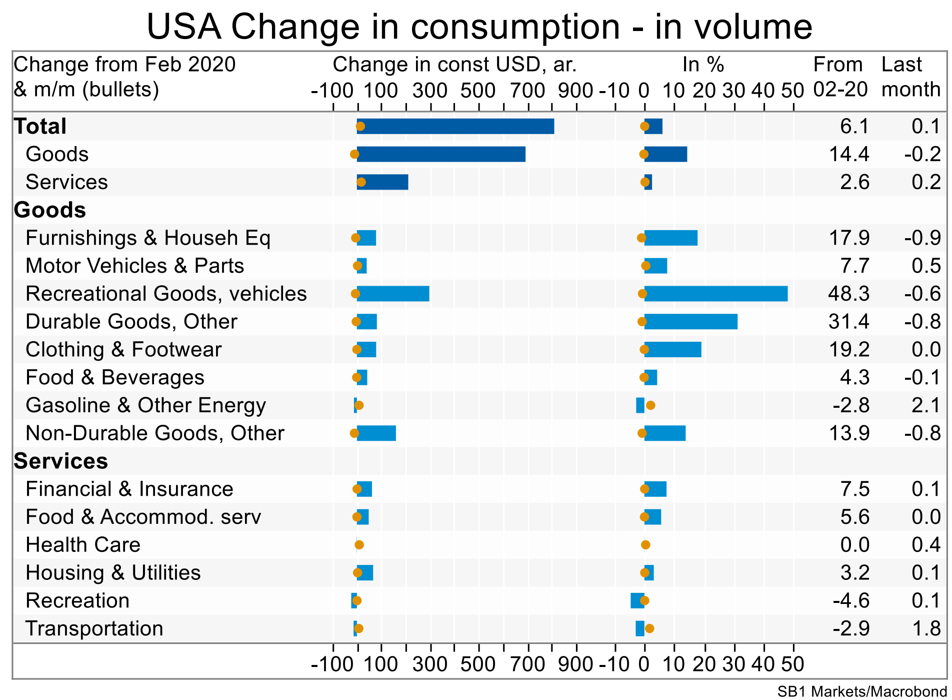
Something is happening with wage revenues (=wage costs for others…)



Services are 2.6% above the pre-pandemic level; goods are still 14% above

Spending on services is still 3% below the pre-pandemic trend, spending on goods are 5% above!

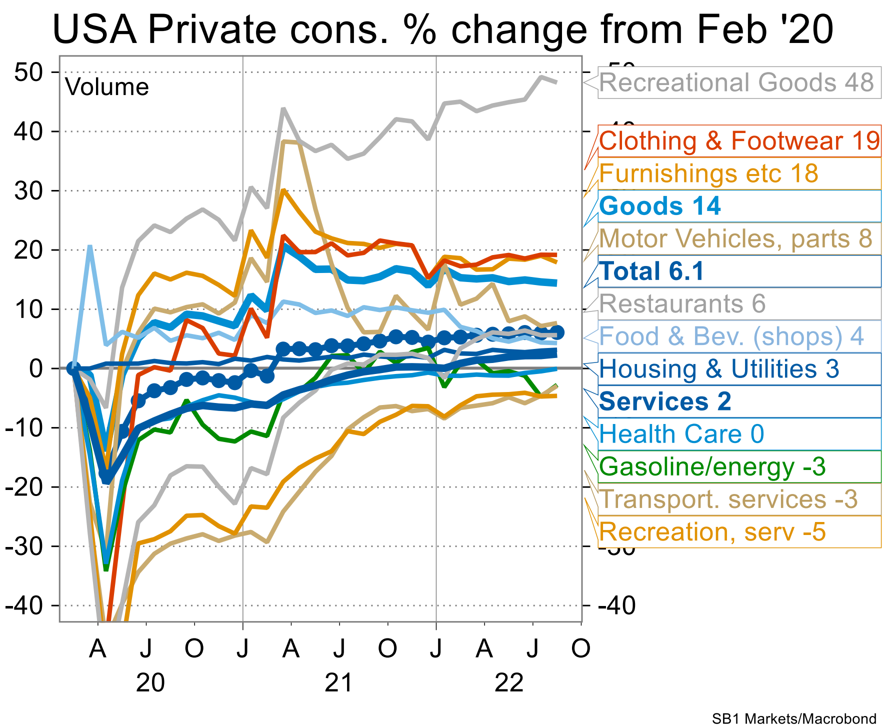


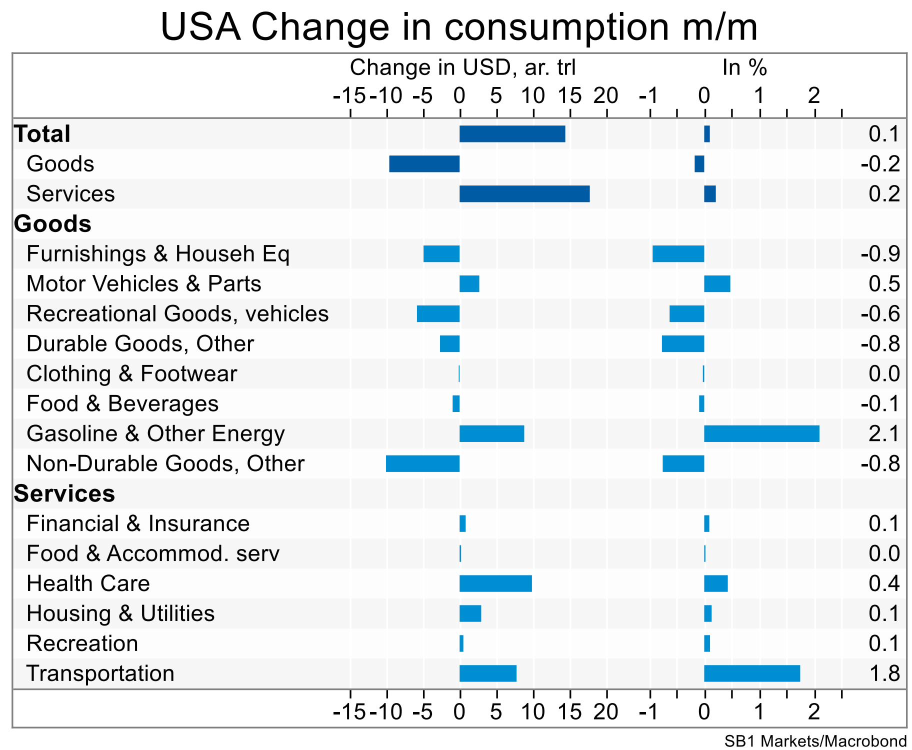


- Both consumption of goods and even more service consumption was revised up in the annual GDP revision

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

Mixed July consumption data, goods down, services up

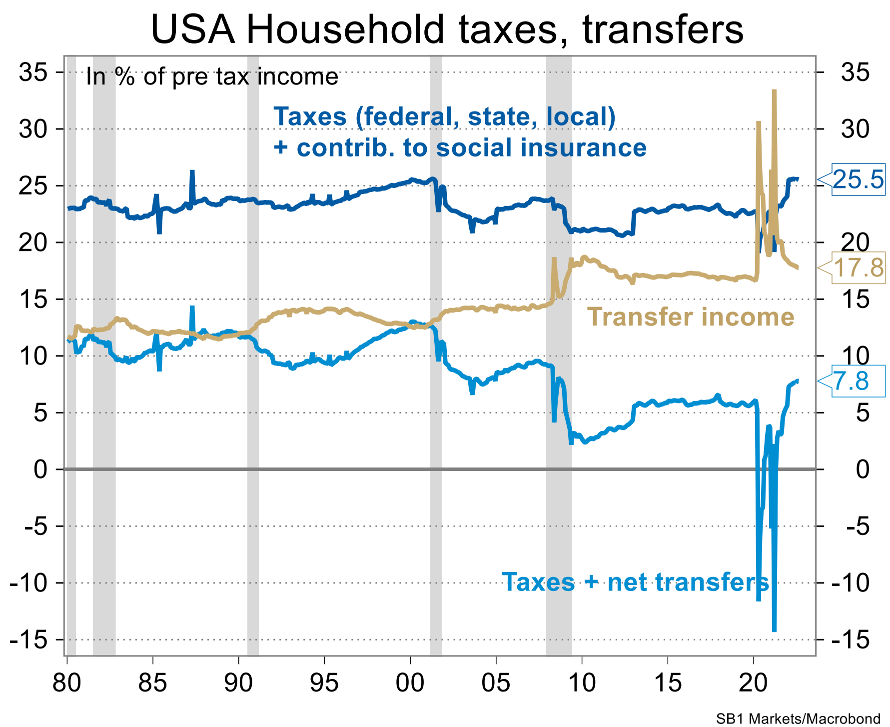


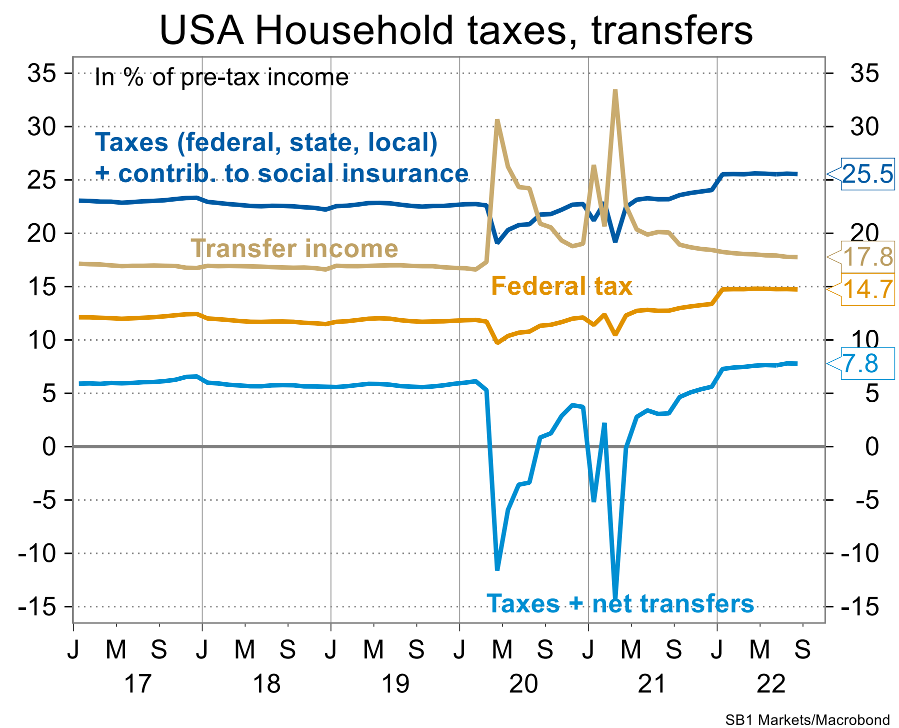


SpareBank 1 MARKETS

Households contribute more to the Federal coffers than before the pandemic!

Net taxes up to 7.8% of pre-tax income, best since 2009. Gross taxes at 25.5% equal to the 2001 ATH!

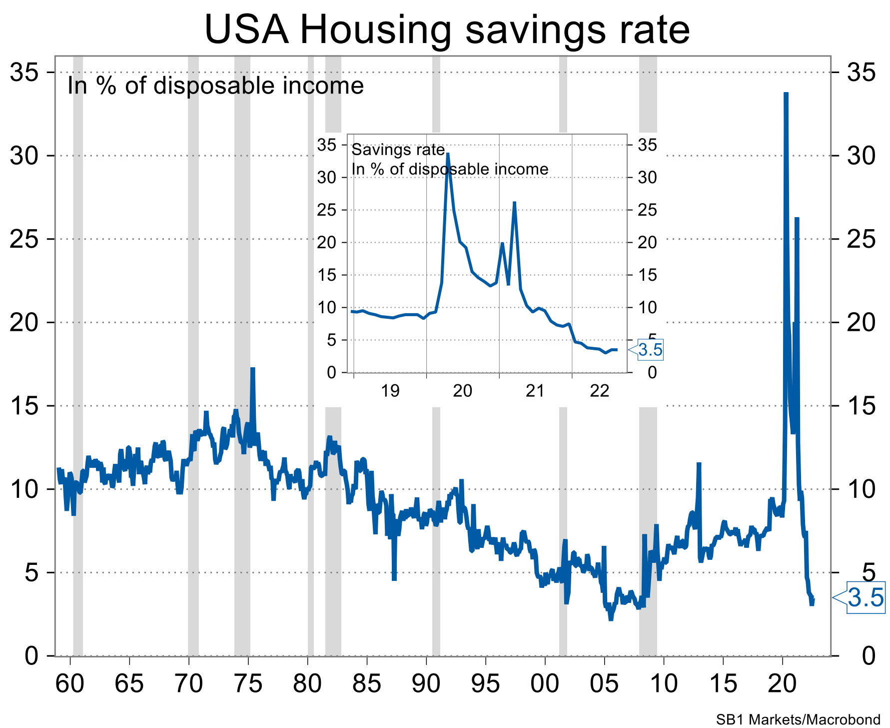


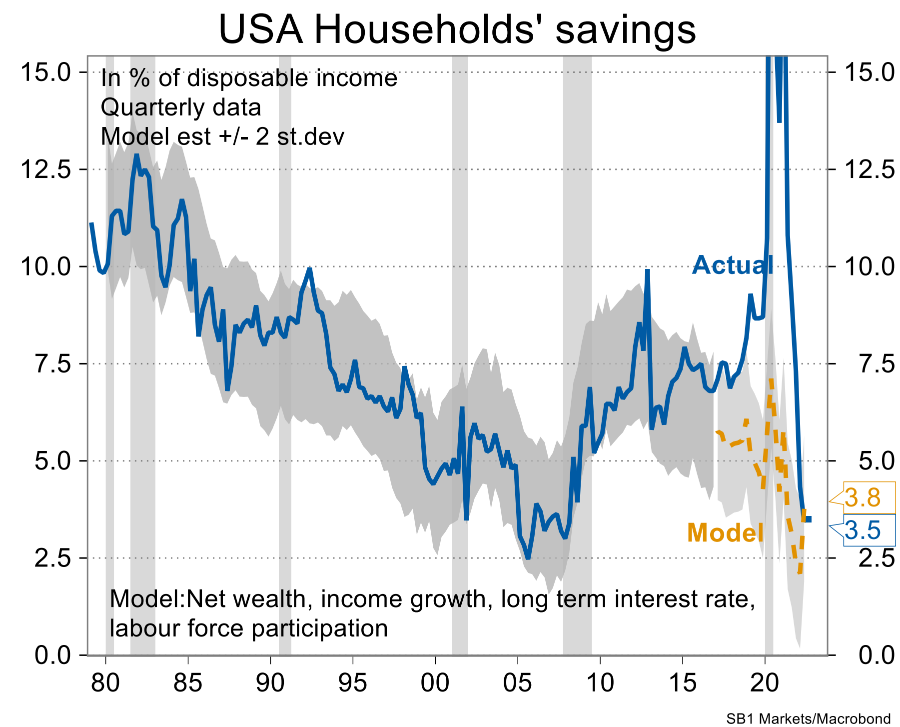


- Transfers are trending down but are still higher than before the pandemic (vs total pre-tax income). However, the total tax rate is climbing faster. The total gross federal income tax rate at 25.5% of pre-tax disposable income is equal to the ATH in 2021!
- Thus, the net tax rate is on the way up, and has recovered to 7.8%, above the 6% pre-pandemic level – but far below the 10% – 12% from before year 2000 – as the transfer rate is at 18%, up from below 15% from before the Financial Crisis

The savings rate revised down 1.5 pp, and 3.5% is not that impressive

The savings rate was revised down from mid 2021 (and for 2019)

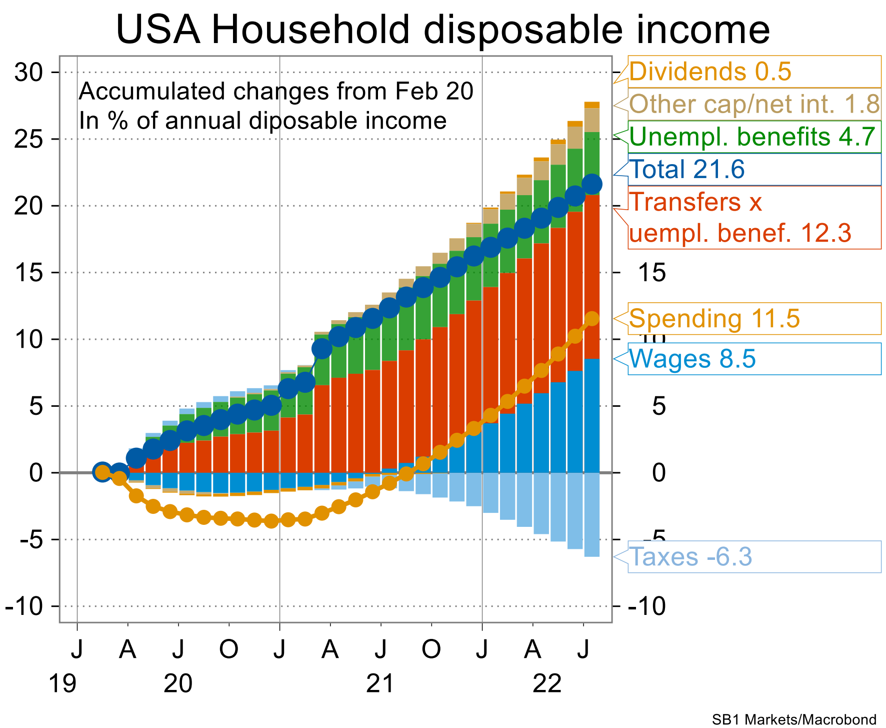


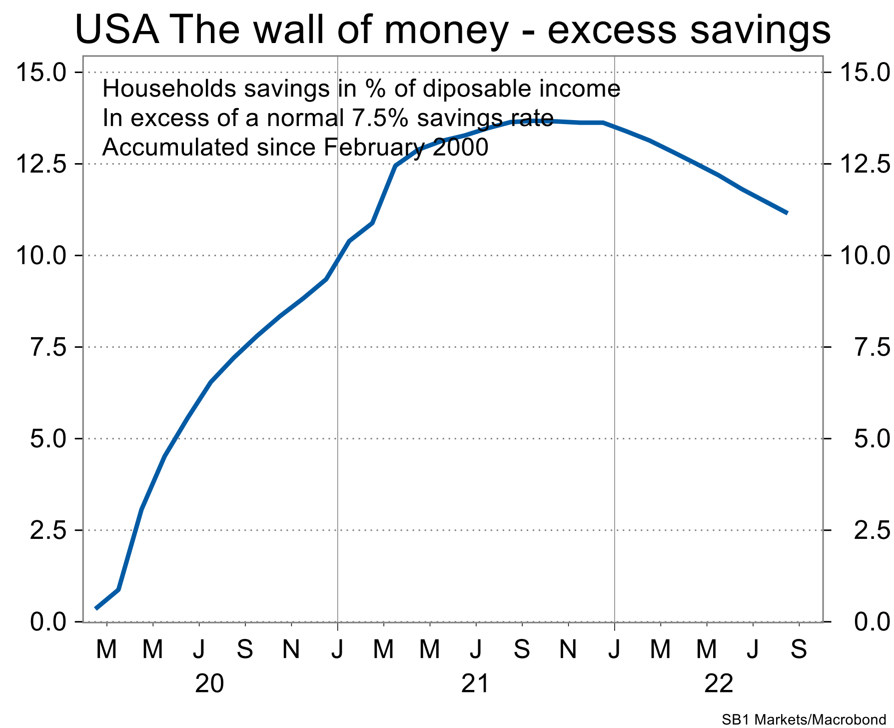


- The **savings rate** was unch. at 3.1% in August (July was revised down by 1.5 pp)
- Households are now dipping into 'normal' savings in order to keep consumption up, as their real incomes are not keeping up, due to the high rate of inflation. The savings rate is now 4 pp lower than before the pandemic
  - » However, household have saved much more than normal during the pandemic, equalling to some 13% of disposable income – on average for all households, that is. This 'Wall of Money' is now shrinking at a 4 pp pace per year, if the savings rate stabilises at 3.5%
- Our old savings model, yielded a 2.8% savings rate in Q2. During the 2016 – 2019 period our model has underestimated the savings rate systematically by some 2 pp, but the gap is now closed (as the sign may change in Q3, due to the decline at the stock market – and thereafter by lower oil price, and higher interest rates

The Wall of Money is coming down faster than previously assumed

The sum of 'excess savings' through the pandemic is still substantial

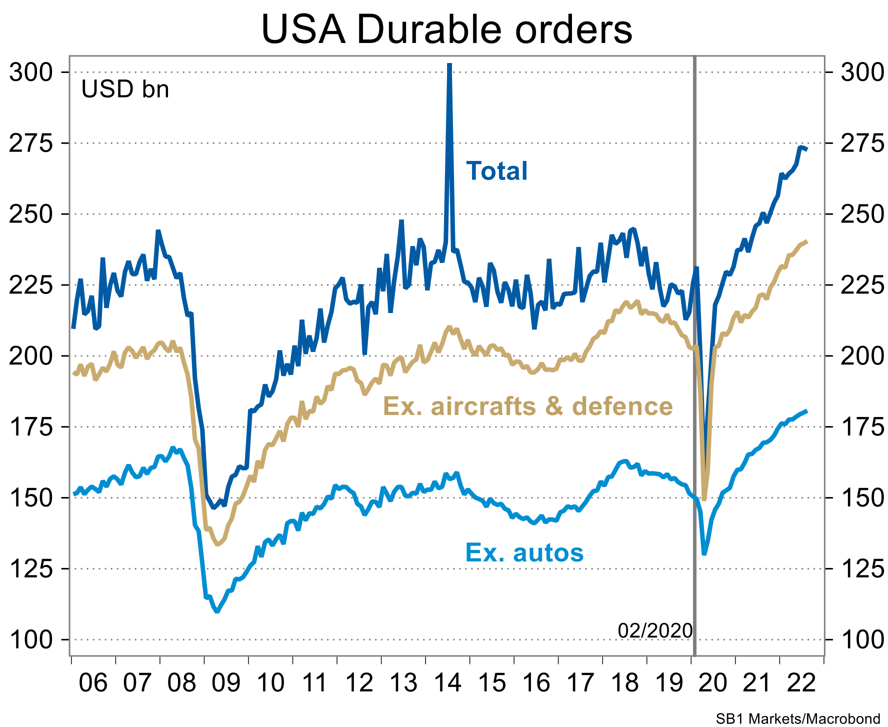


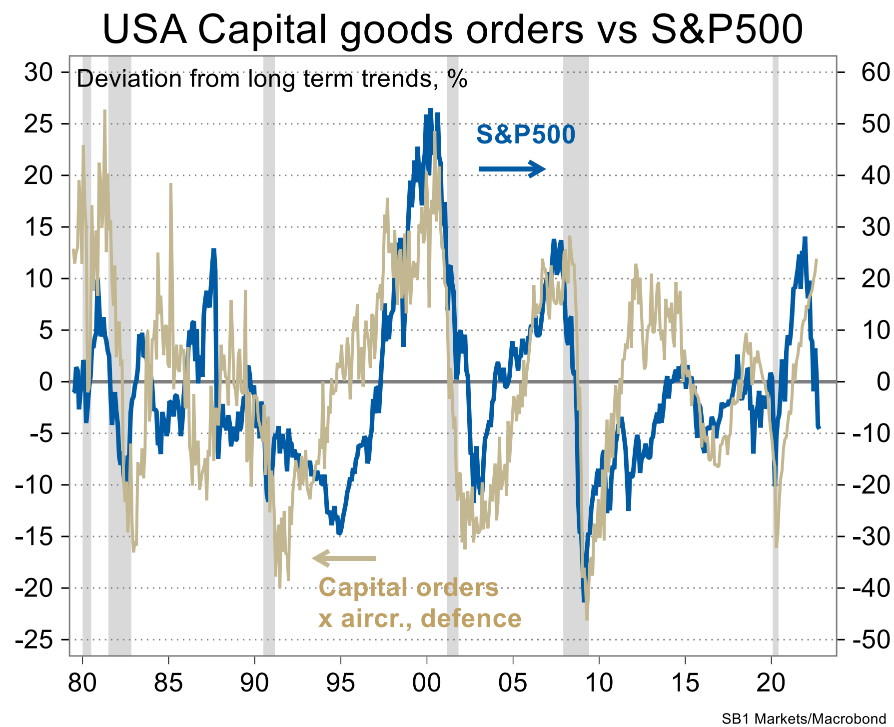


- Transfers from the government and low spending (on services) explained the lift in savings - but now spending is coming back, and the savings rate is now lower than before the pandemic

Durable goods orders still decent – core up 1.3% in August

No signs of a recession here

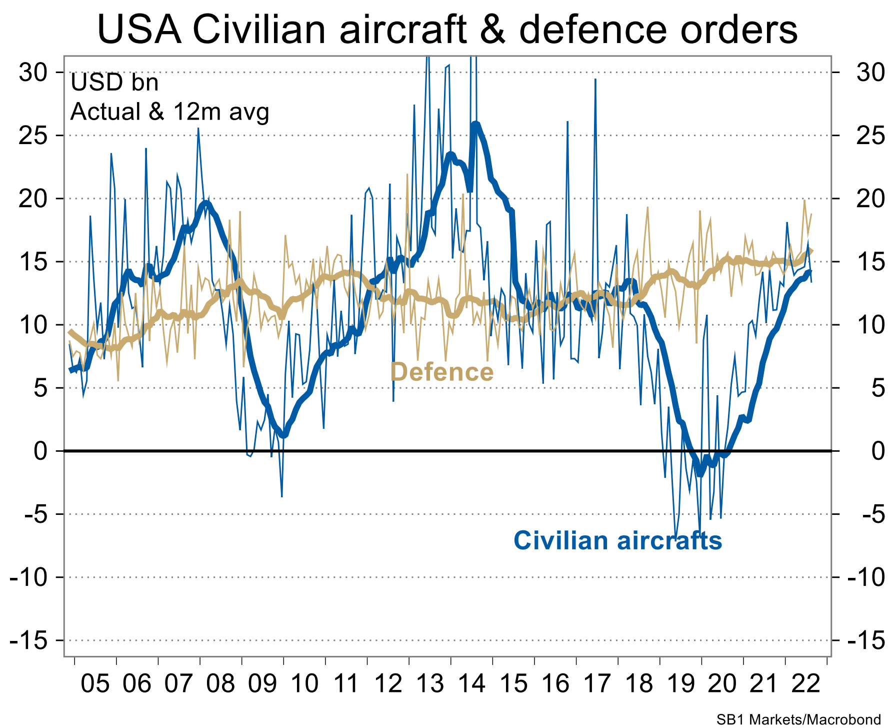


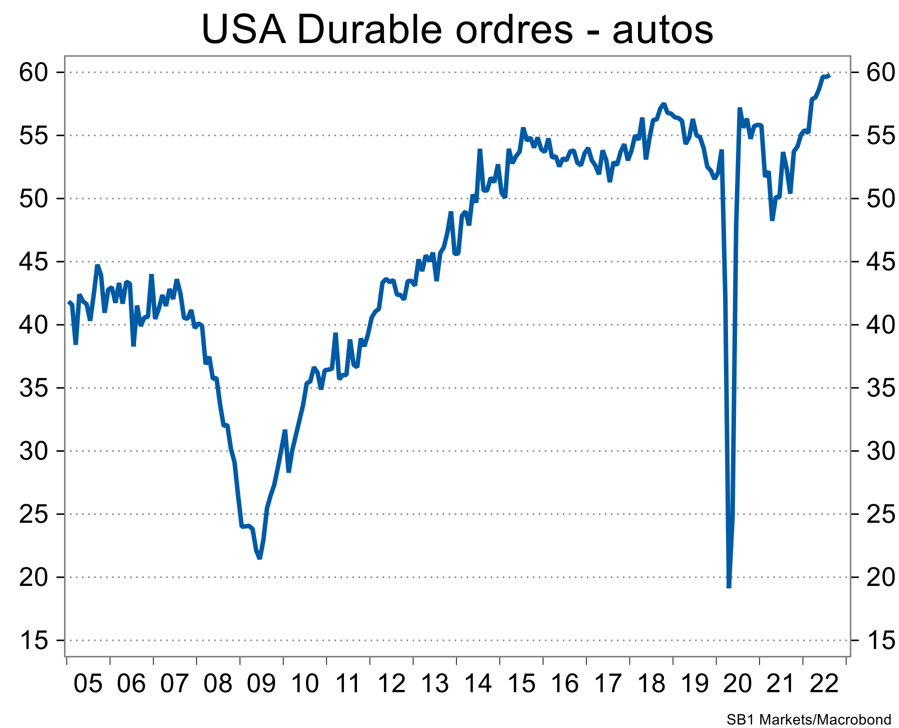


- **Total durable** orders were down 0.2% in August, down from -0.1% in July, expected down 0.4%
- The volatile aircraft & defence orders rose marginally, and **other orders** (our core concept) were up 0.2%
- **Core investment goods orders** grew 1.3%, expected up 0.2%. Underlying growth is slowing but remain well above trend
- **Order inflow** is far above pre-pandemic levels, especially for investment good orders, but surveys have now turned the tide and are still in the negative, but we haven't witnessed a sharp decline in orders this far

Aircraft & defence orders at normal levels

… while auto orders rose in August from a downward revised July print

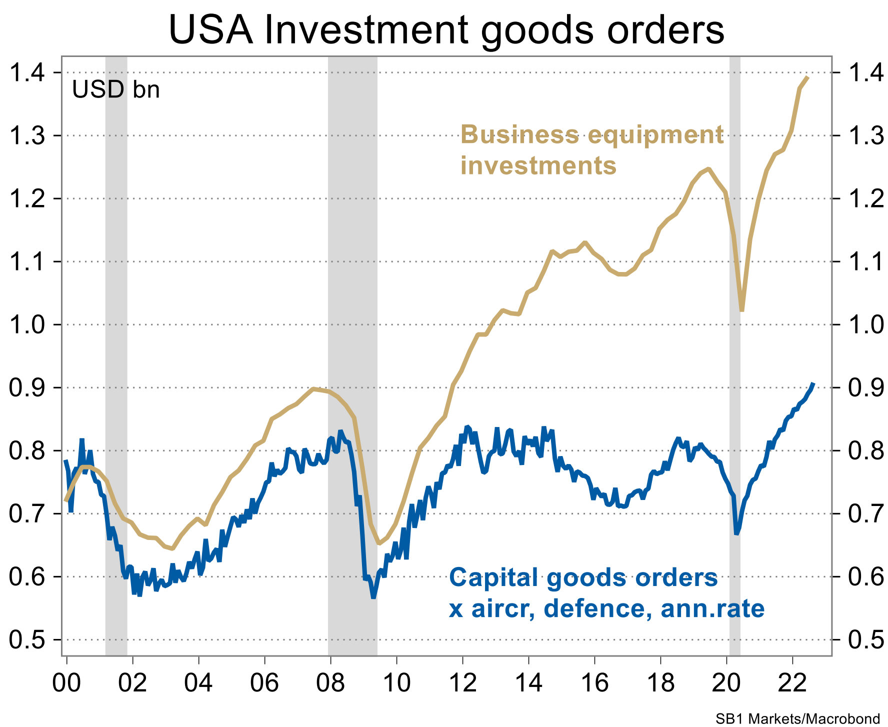


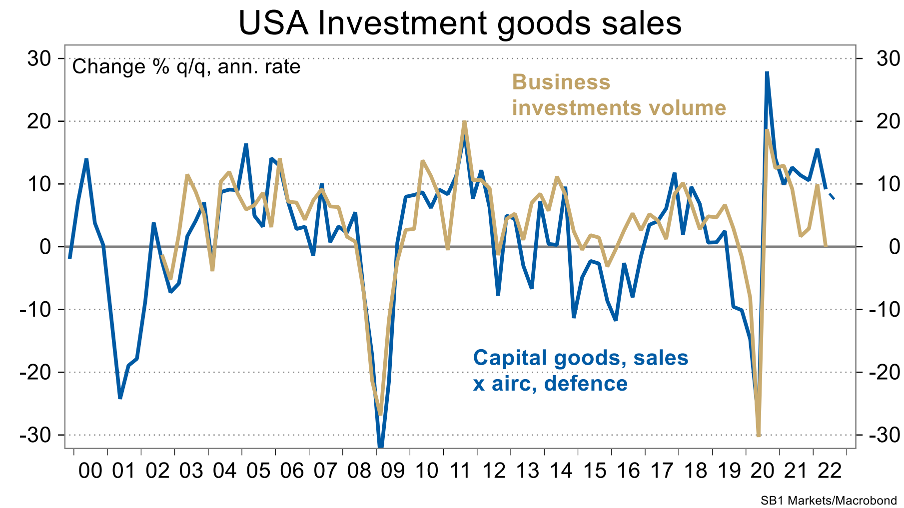


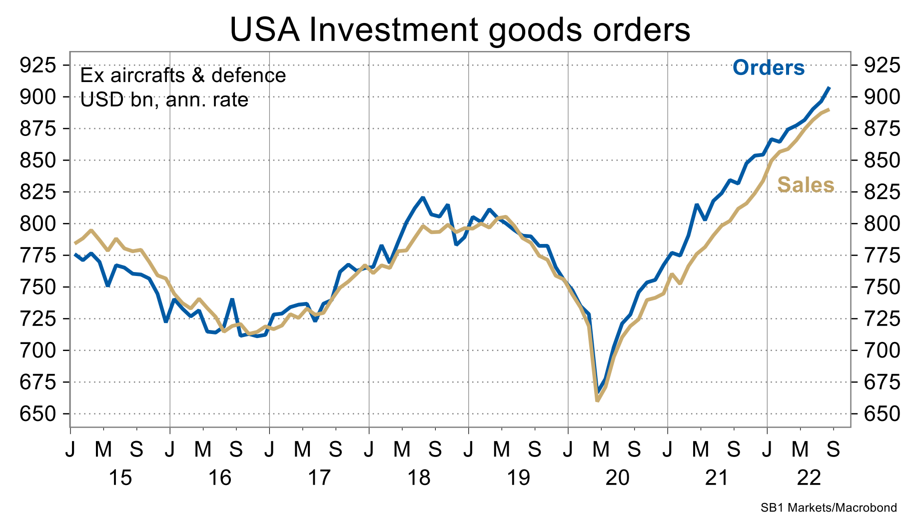
- Aircraft orders were down 18% m/m (these orders are very volatile), while auto orders were up 0.3%
- Memo: New aircraft orders during the pandemic have been heavily revised but the level now is not adjusted

Core capital orders are still growing well above trend

Signal decent growth in business investments in Q3 (at least in nominal terms)



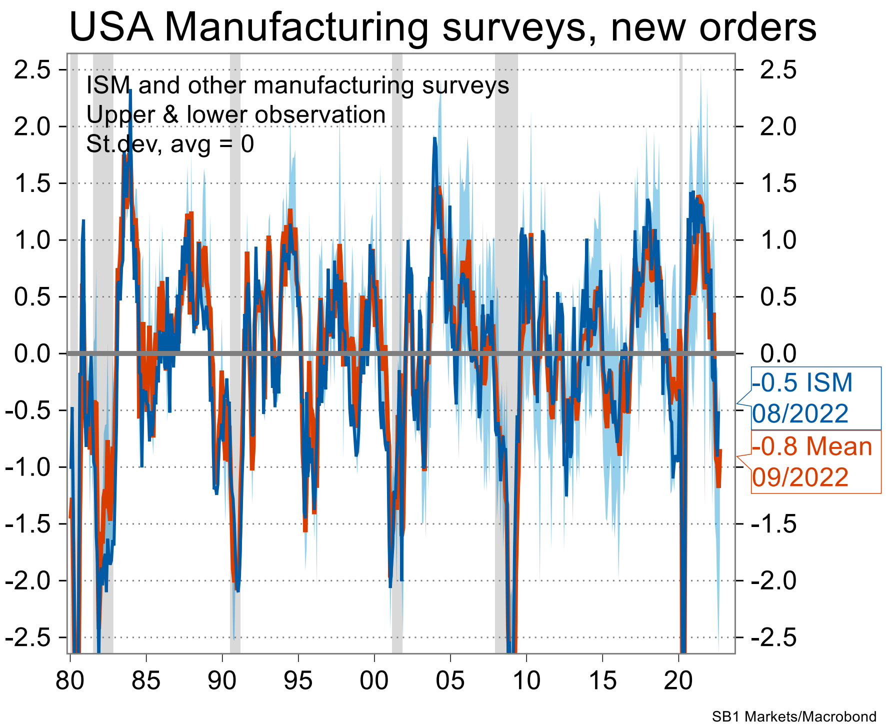




- **Core (x aircraft, defence) capital goods orders** grew by 1.3% in Aug, far above expectations at 0.2%. July data was revised up 0.4 pp to 0.7%. Shipments were up 0.3% m/m. All data are in nominal terms
- **The business investment** level is well above the pre-pandemic level – and not low vs. a reasonable long term trend (both in nominal and volume terms)

Surveys are signalling a steep decline in new orders

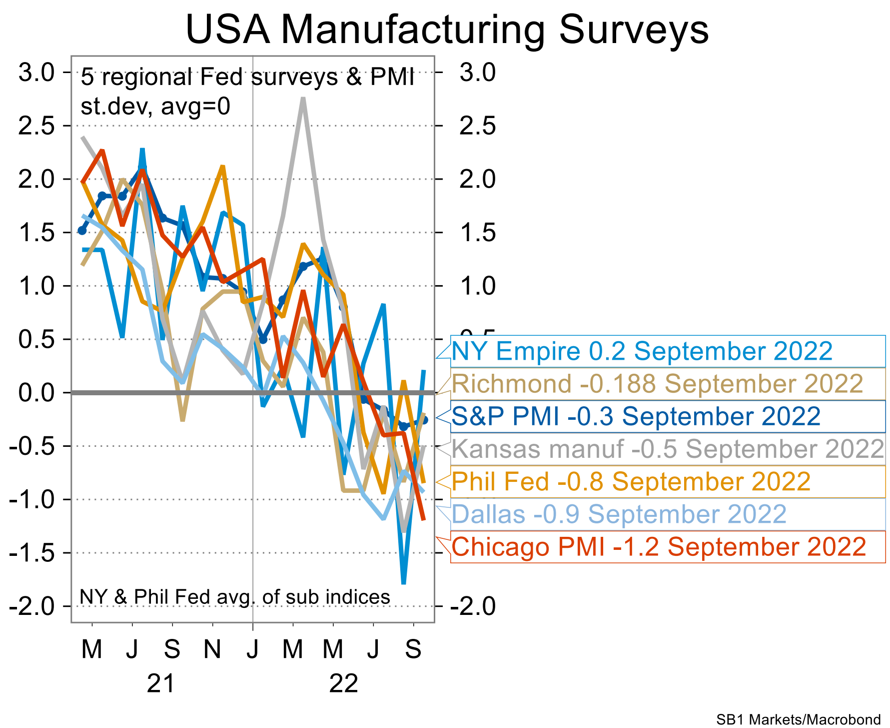
… which so far has not materialised… but surveys are less bad than a month ago

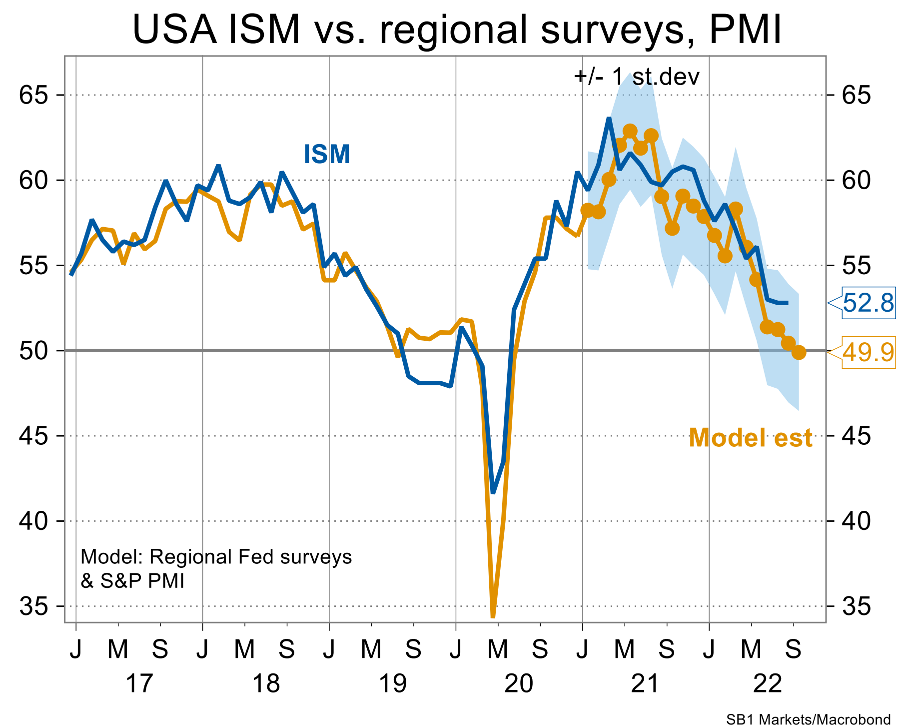


* The ISM order index is

The trend is set – but September surveys were mixed

The ISM risk: The level is substantially stronger than the average of other surveys

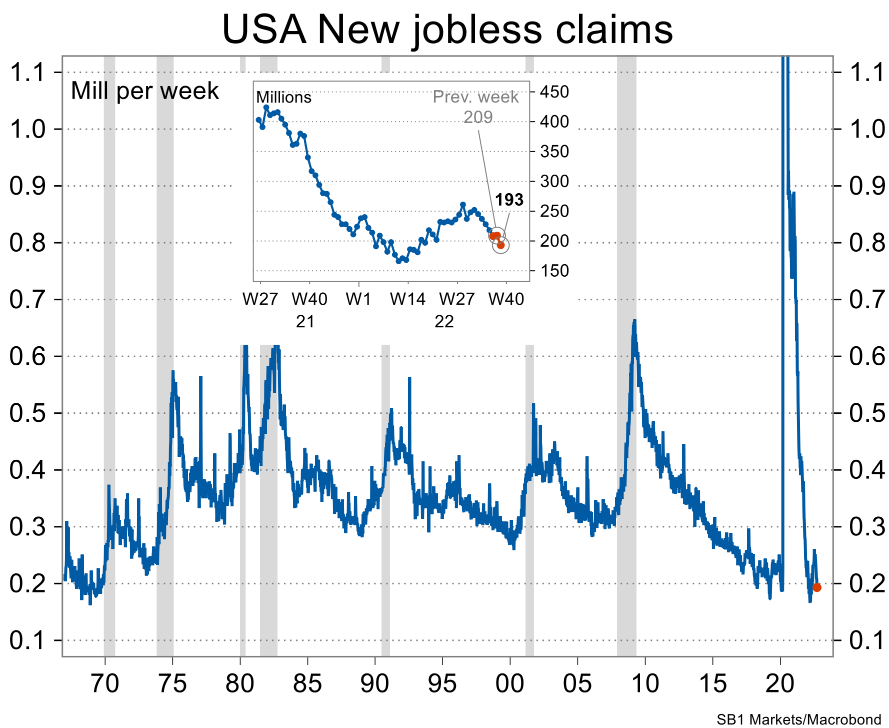


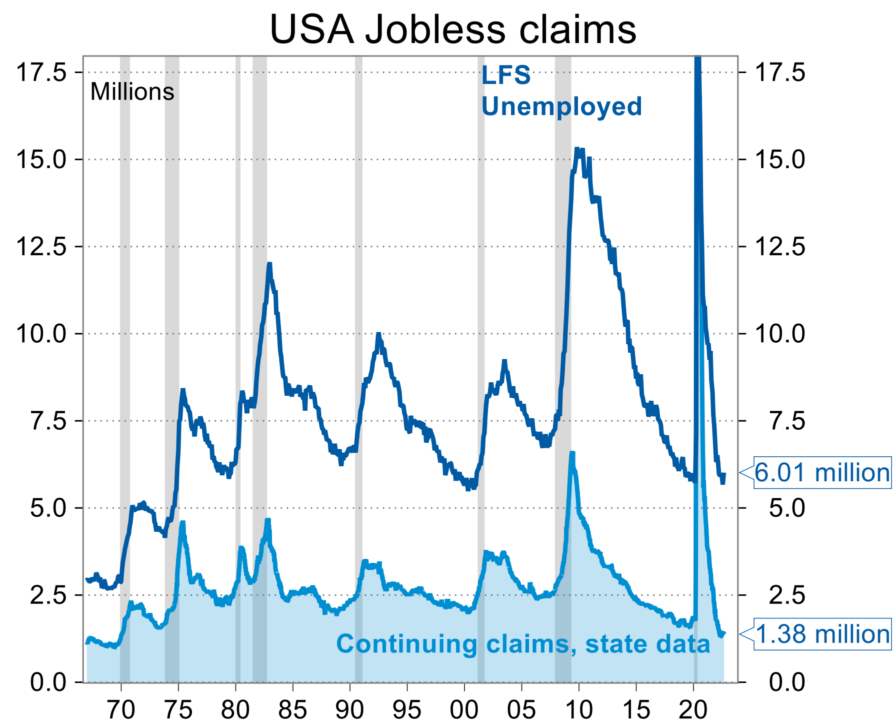


- Big picture: Growth is slowing sharply but manufacturing indices do not signal that the economy has entered a recession (even if order indices are really worrisome)

The labour market is <u>extremely</u> tight. Somebody has to do something!

New jobless claims fell sharply last week – to the lowest level since the spring

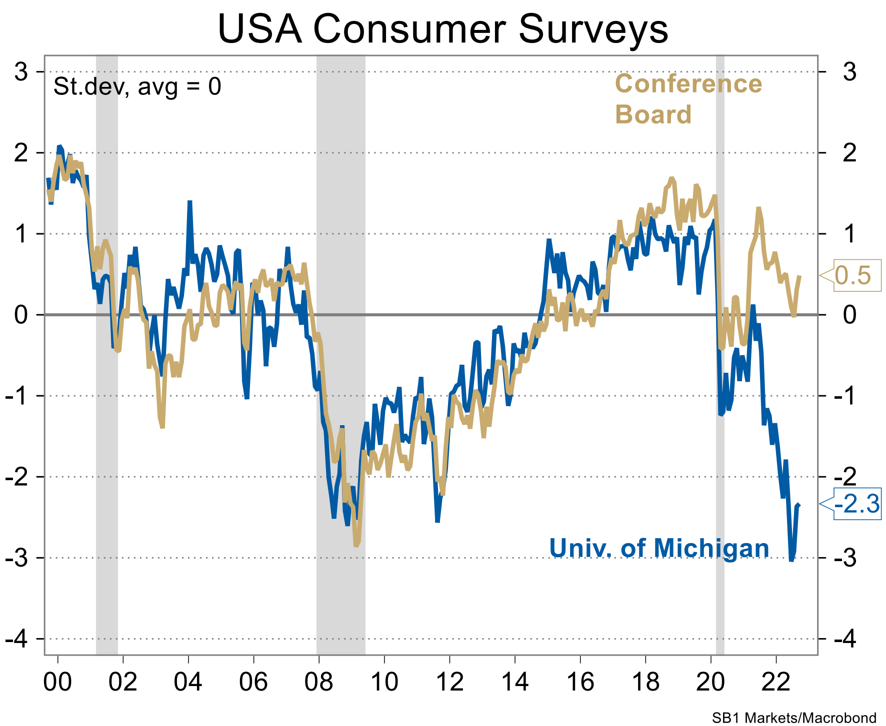




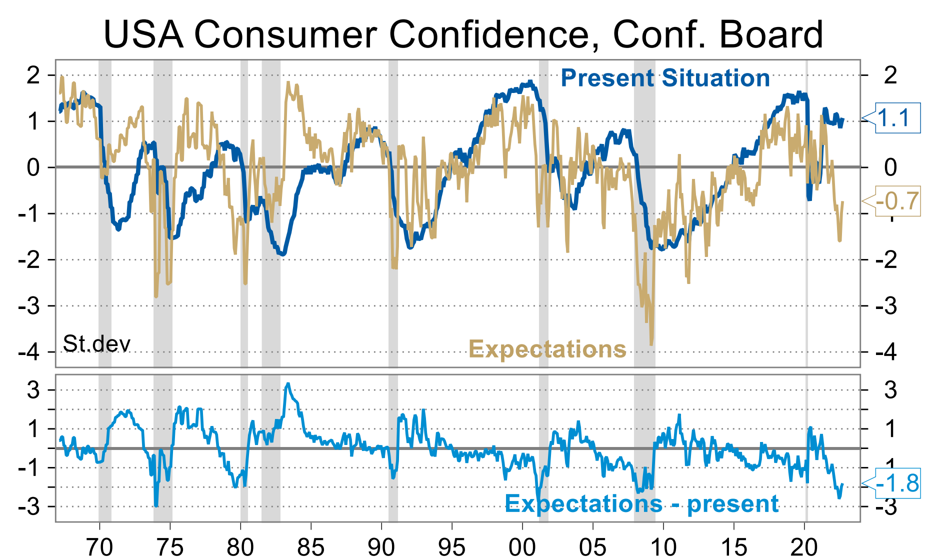
- **New jobless claims** all of a sudden dropped to 193' from 209' last week (revised from 213'), expected up to 220'. New claims have fallen by 68' from 8 weeks ago, and the level is just 27' above the bottom during the spring – which has the lowest level since 1969 (in number of persons, the lowest ever in % of the labour force)
- **Continuing claims** fell by 29' in week 37, also below expectations

Conference Board's Consumer confidence survey further up in September

However, expectations are still below average, normally a warning sign. Inflation expectations down



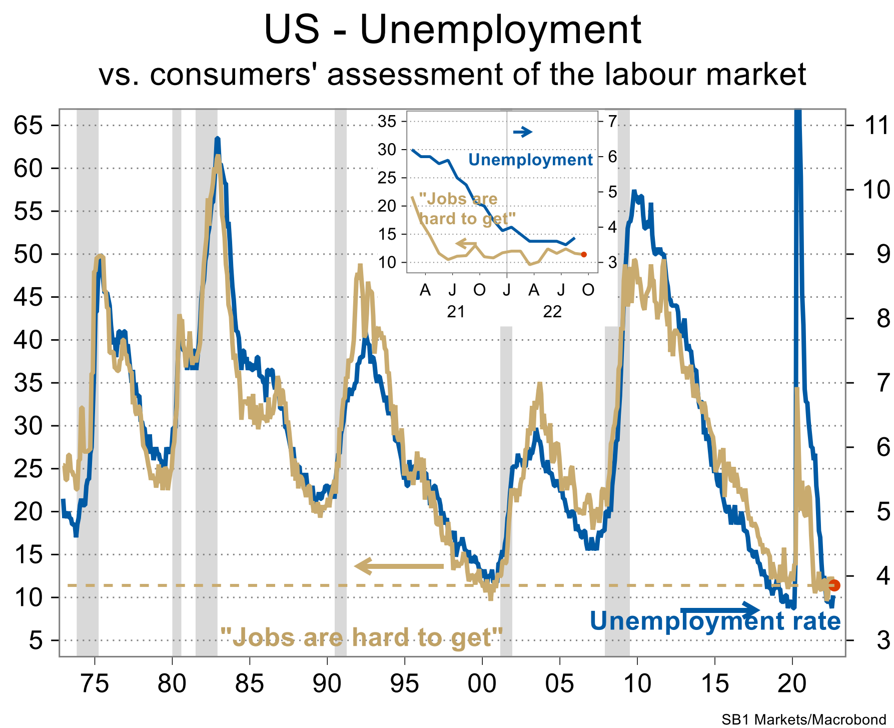
- **The main index** rose to 108 is Sept, up from 103.6 in Aug, expected up to 104.5. Households assessment of the future expectations rose the most
  - » The increase in the main index equalled 0.2 st.dev, up from an average level
  - » **Expectations** are weak, 0.7 st.dev below average, which is normally seen in recessions (but not only)
  - » **The difference** between households assessment of the present situation is at -1.8. The gap is always the largest just before or when a recession hit, check the chart below

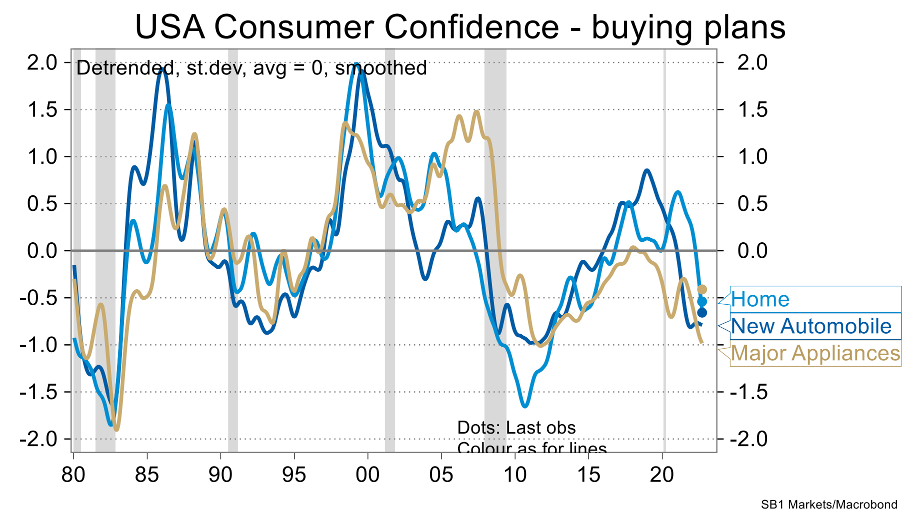


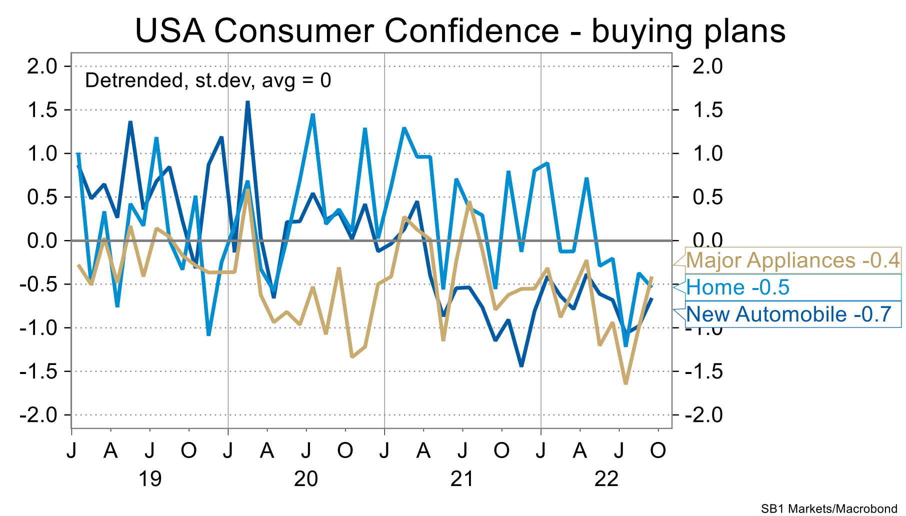
- **The other consumer** surveys we follow are on another planet (even if sentiment was up in all surveys in Jul/Aug/Sept). University of Michigan's sentiment was revised slightly from the first estimate, but is still at -2.3 st.dev below avg – which is a very low level
  - » Two other confidence surveys, from IBD/TPP and Univ. Florida are not much better than the UM survey – and Conf. Board's survey is an outlier

Buying plans up in September, apart from housing of course…

… but plans are still well below average

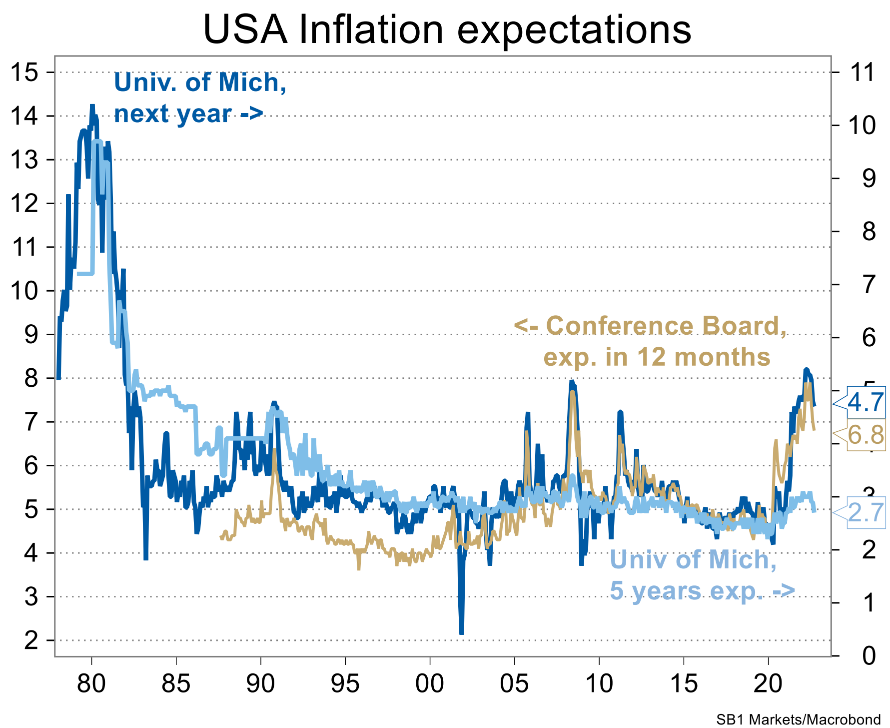


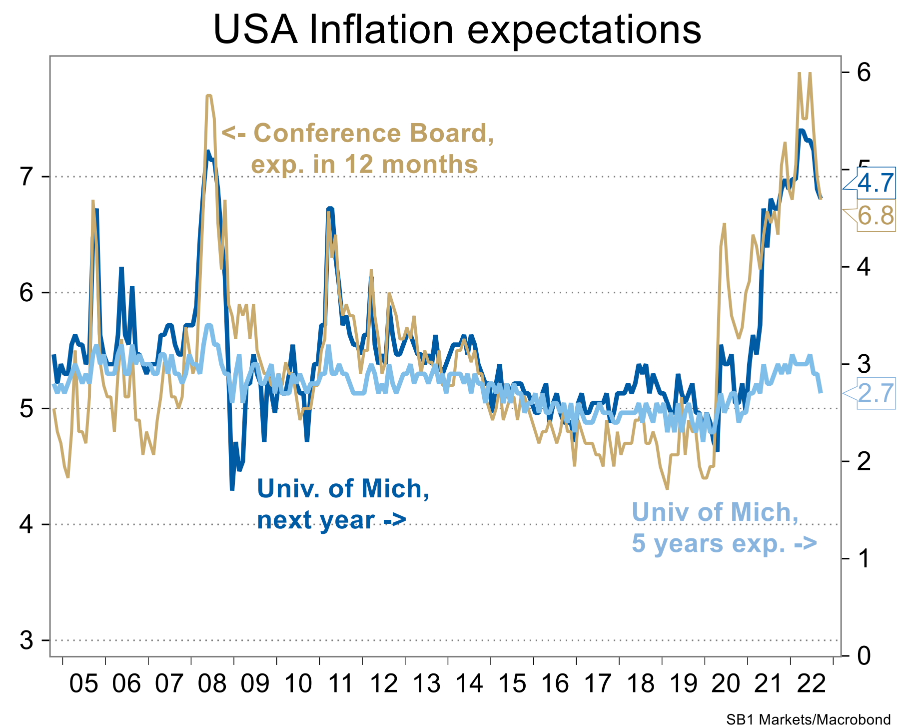




- **Household spending plans** are volatile, but the decline since the spring is significant, especially for homes and major appliances, despite the September increase
- Jobs are still very easy to come by, according to the conference boards – and as witnesses by plenty of other data as well

Inflation expectations are heading down, both according to Conf. B & Univ of M

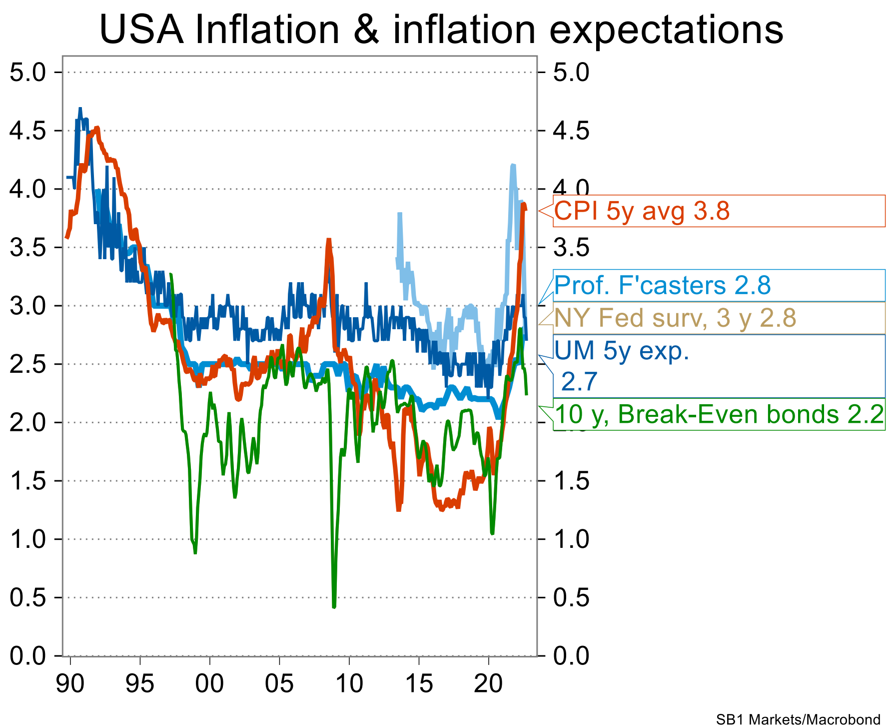


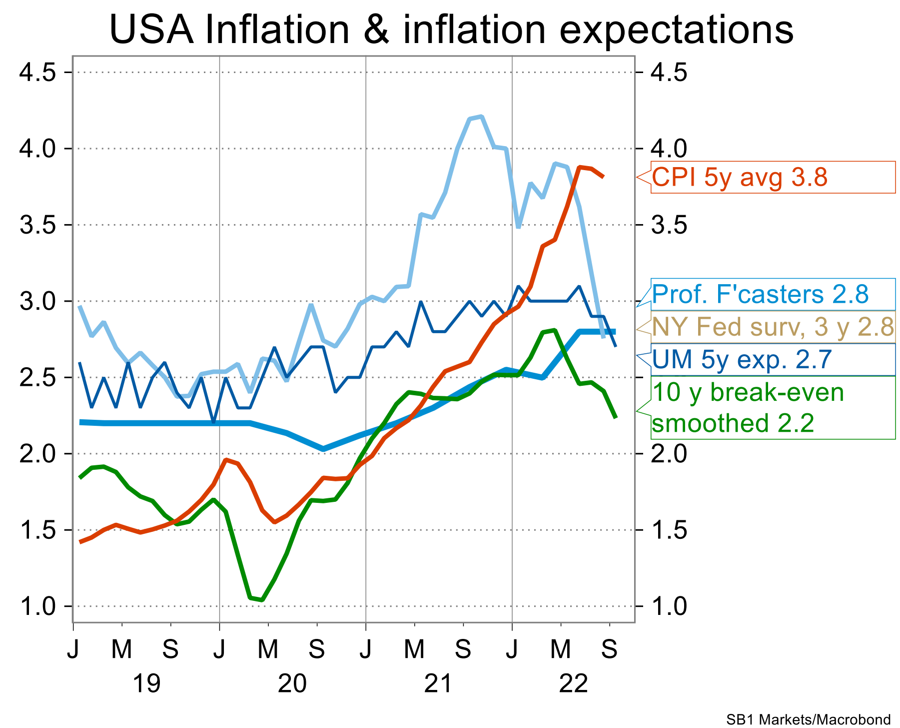


SpareBank 1 MARKETS

Inflation expectations are heading down, according to other surveys too

All surveys are signalling low inflation expectations

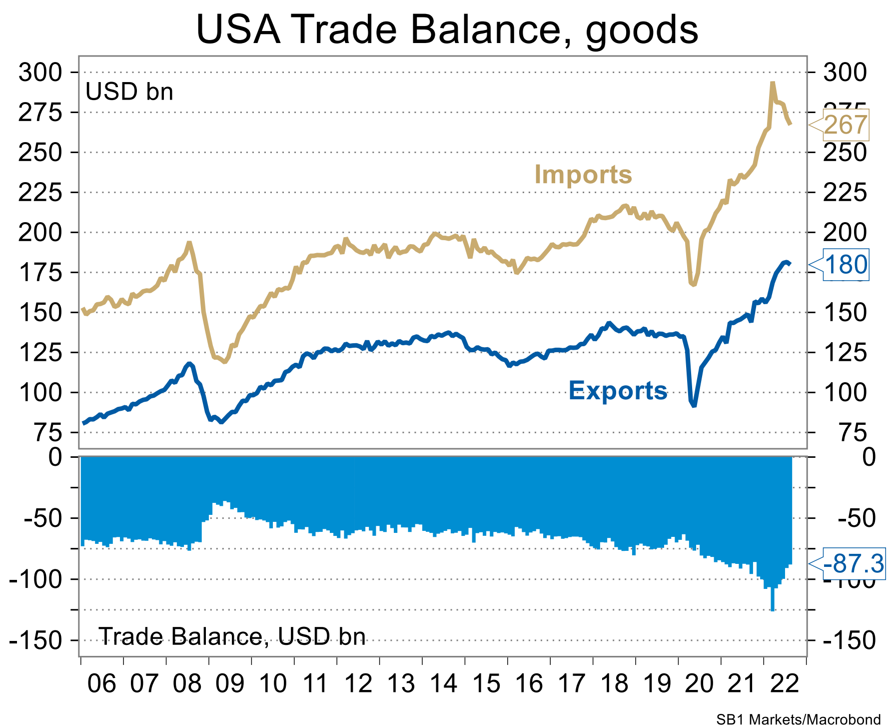


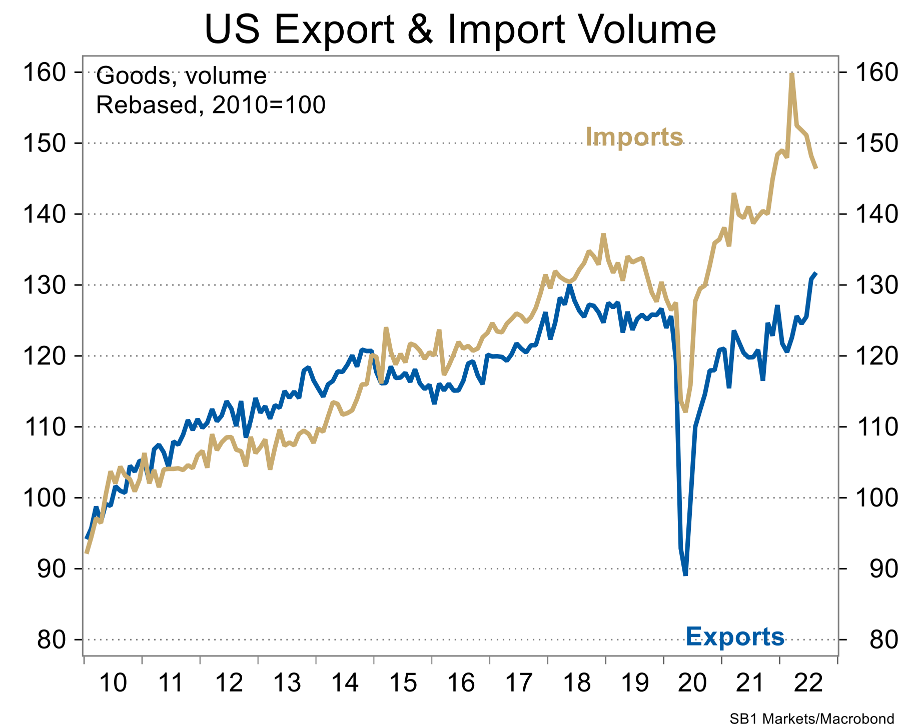


USA

The trade deficit is shrinking, even in volume terms. Will support growth in Q3

The trade deficit in goods narrowed by USD 2 bn to 89 bn in Aug, marginally better than expected

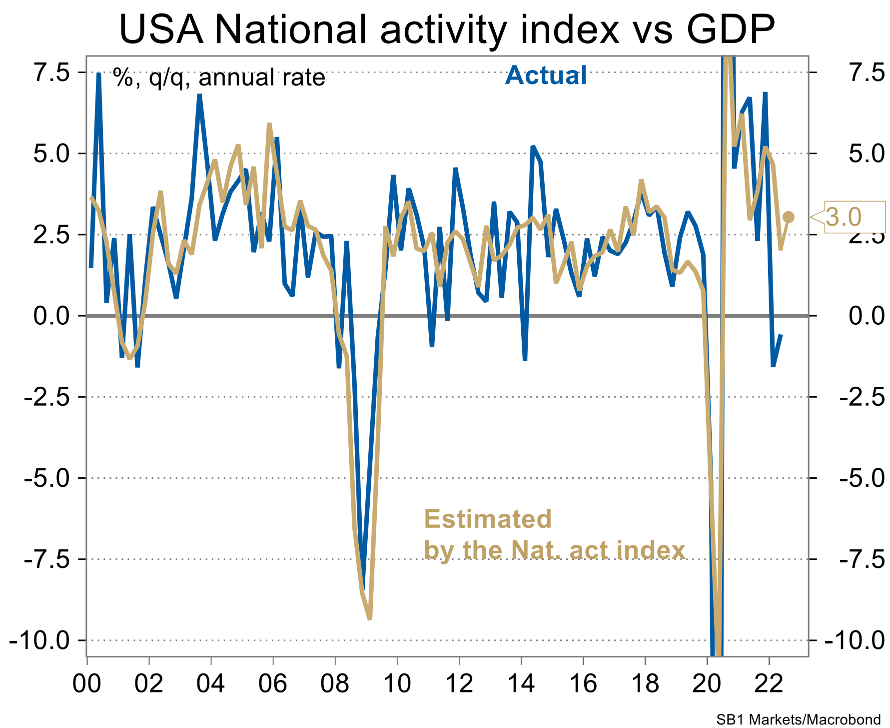


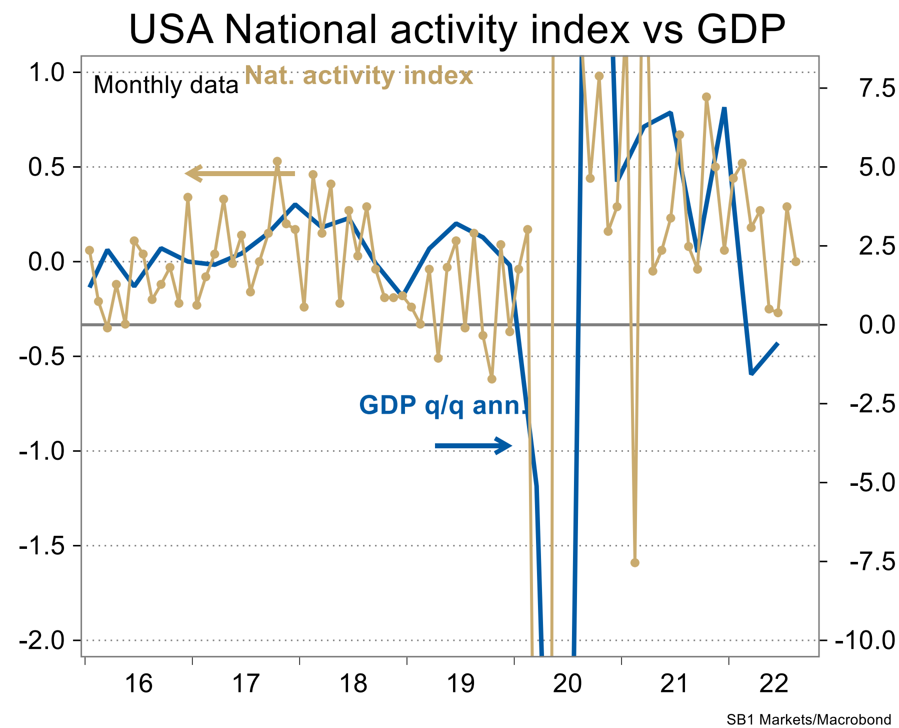


- The trade balance in <u>goods</u> has been falling rapidly recent months, as imports are declining rapidly, from a very high level
- In addition, growth in exports have been rather impressive, even in volume terms. Export volumes are up some 5% from before the pandemic. Imports have fallen sharply from the March peak, by 8% - but imports are still up 15% from early 2020. The slowdown in import volumes is due to weaker domestic demand, probably also a destocking
- If export and import volumes are unchanged in Sept, exports of goods will be up 21% in Q3, while imports will be down 12%. If so, a 4 pp (four) contribution to GDP growth in Q3! Inventories will very likely be run down, so the net impact will be smaller – but still very likely positive

The National activity index signals a 3% growth pace in Q3. Optimistic, we think

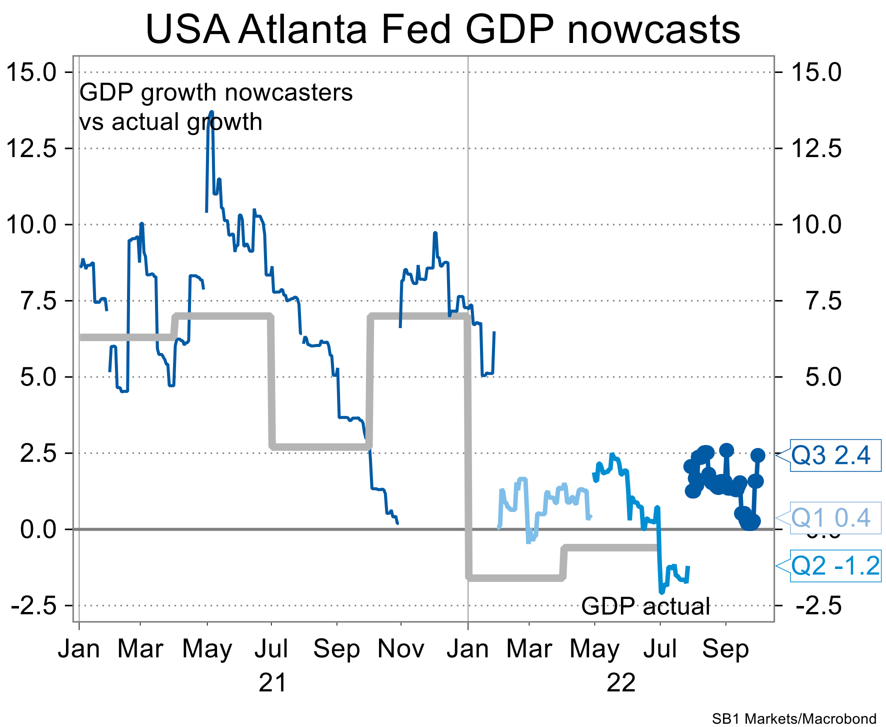
The sum of 80-some indicators lower in September from a slightly upward revised August print

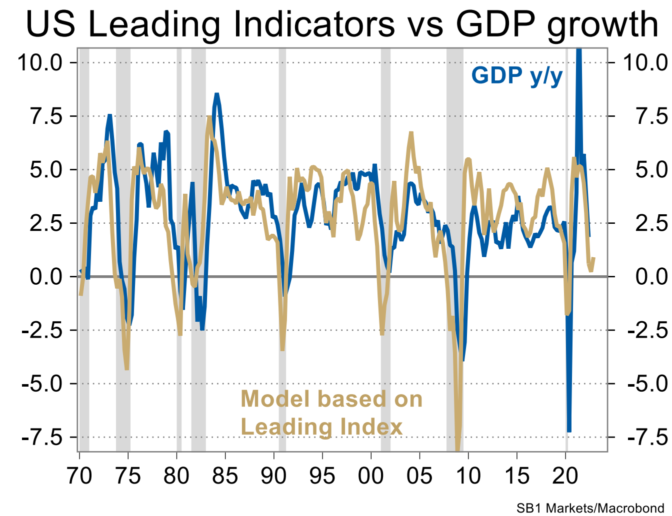




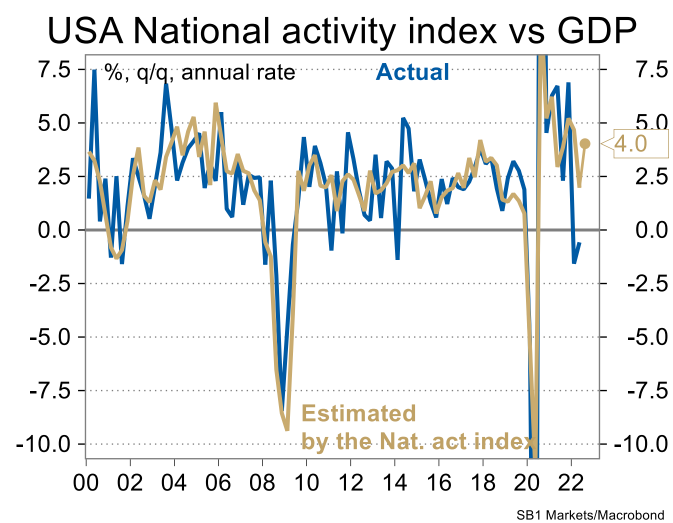
Atlanta Fed's Q3's forecast up 2 pp to 2.4%, due to net exports, the GDP revision

Sure, these measures are volatile but trade data were strong. Inventories the uncertain element now





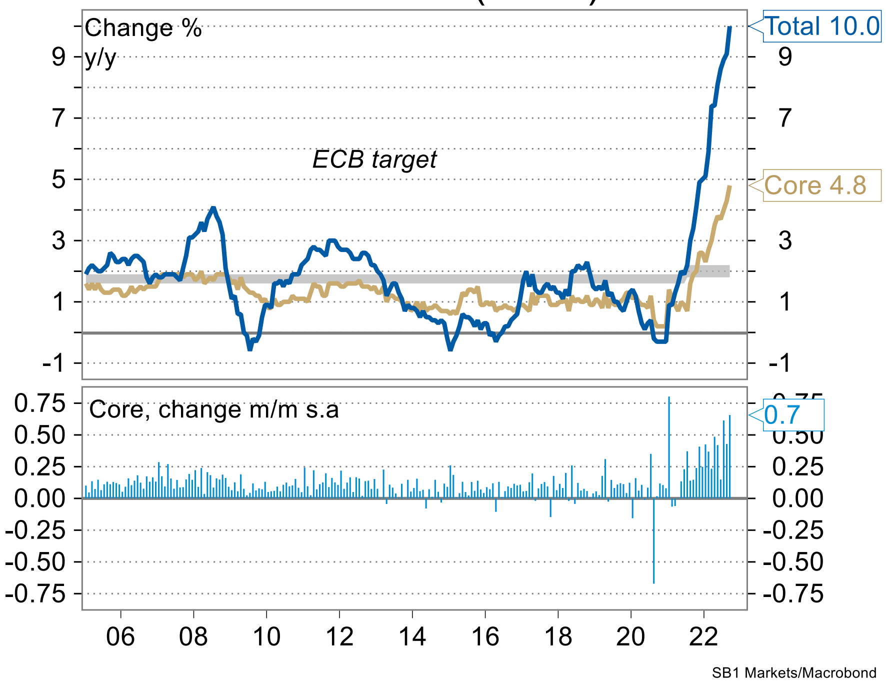
- National Activity index suggests 4% (the July pace). Leading indicators say zero!
- **Q2 GDP** fell 0.6%, revised up from -0.9%



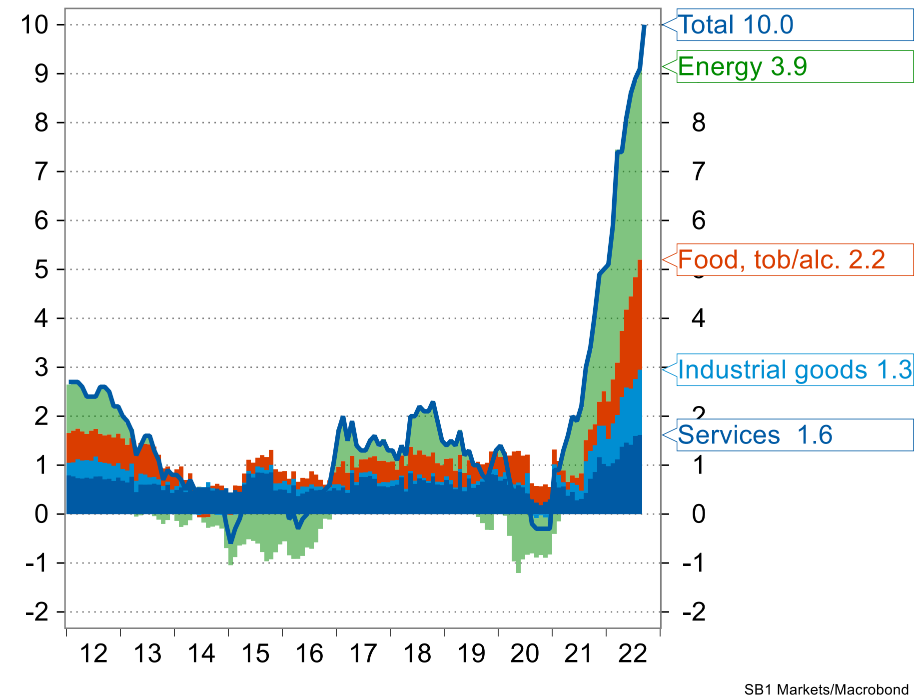
Inflation surged in September – headline inflation hits 10%, core at 4.8%

Both higher than expected, again. Energy prices the main culprit but inflation is broadening, here too

EMU CPI (HCPI)



EMU Contribution to HICP inflation

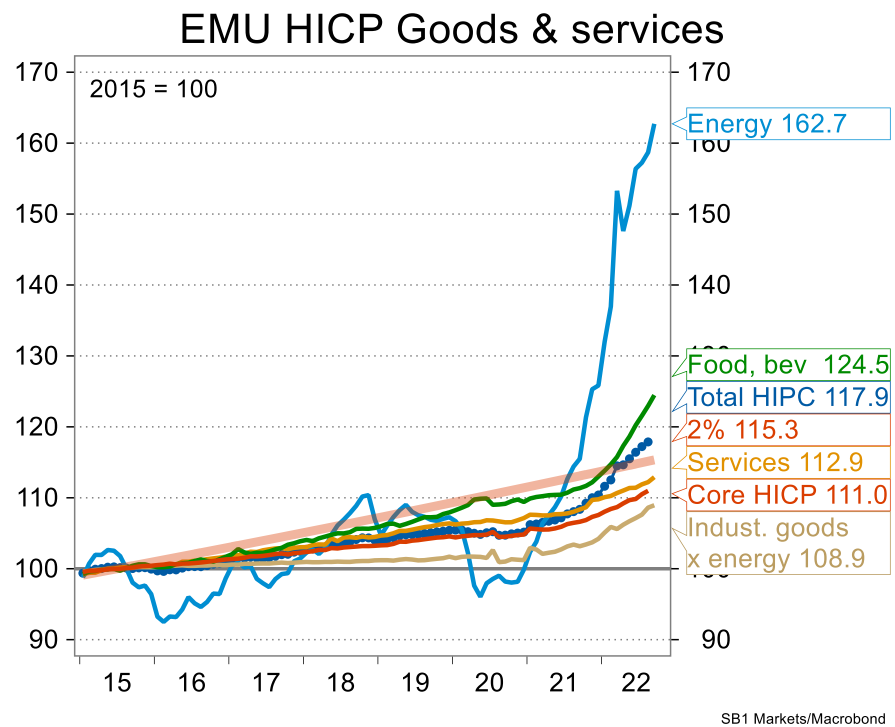


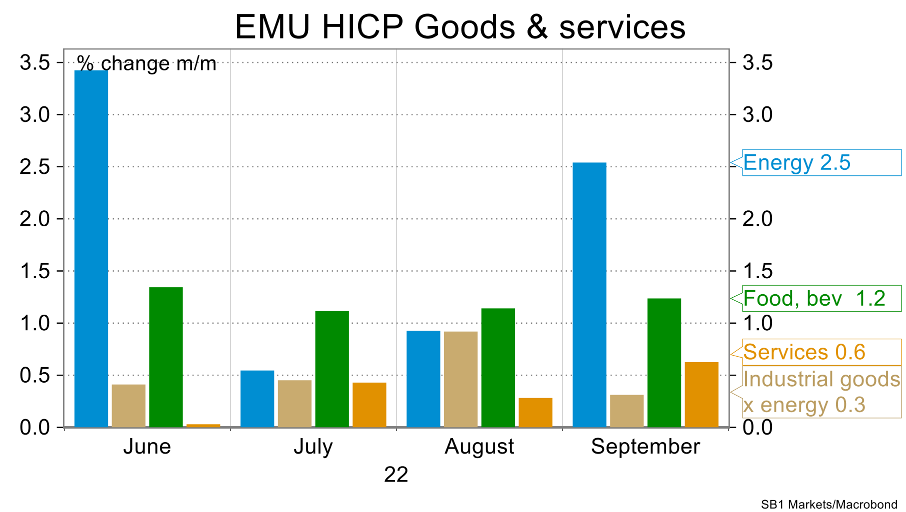
- The **total HICP** rose 1.2% m/m Sept (1.1% seas adj), 0,3 pp above expectations… again
  - » Energy prices rose 2.5% m/m, they are up 40%, and contributes with close to 4% to the headline rate. Food prices rose 1.2% - and the latter is up 11.8% y/y, contributing more than 2 pp to overall CPI growth (all data at the chart to the right is not updated)
- **The core** rose 0.7% m/m, 0.1 pp more than expected. Both goods and services contributed. The annual rate accelerated 0.5 pp to 4.8%, the highest ever, of course
- The **ECB** is no doubt in fighting mode and will hike the signal rate further this week. However, as long as wage cost inflation remains moderate, the medium-term threat against price stability is not that large. The current lift in profit margins will not be sustained if the economy slows. The main risk is that the current inflation shock will push wage inflation up due to compensation claims from the unions

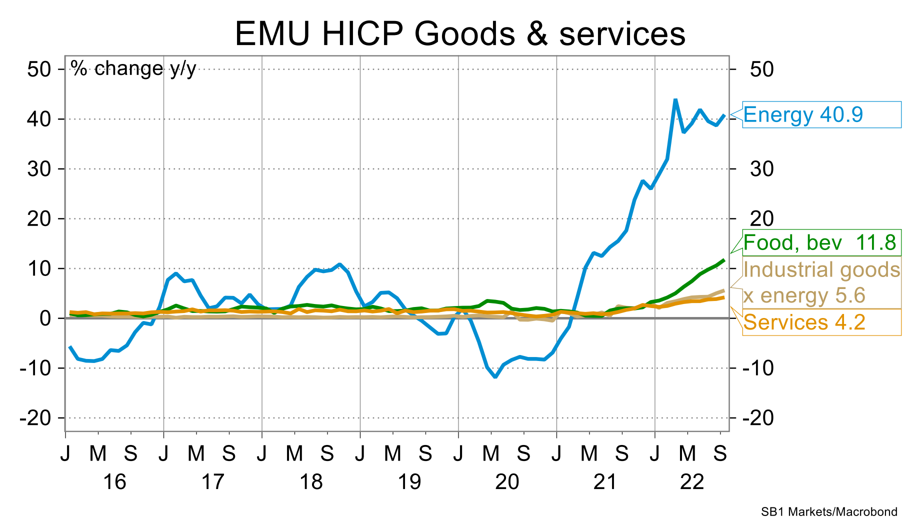
SpareBank 1 MARKETS

Energy prices rose 2.5% in Sept, and food prices added another 1.2%!

Energy prices are up 40.9% y/y



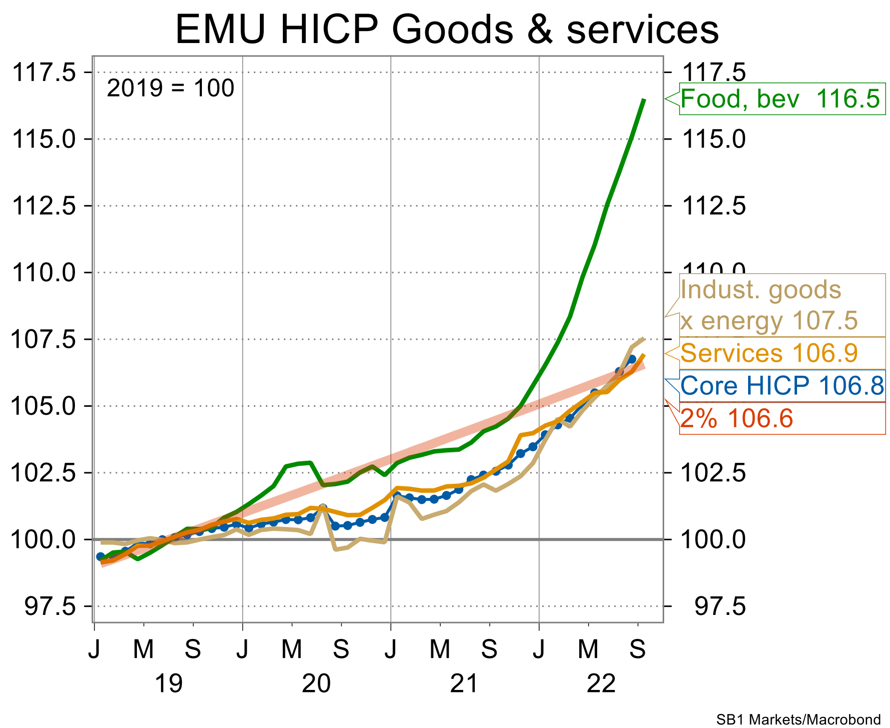


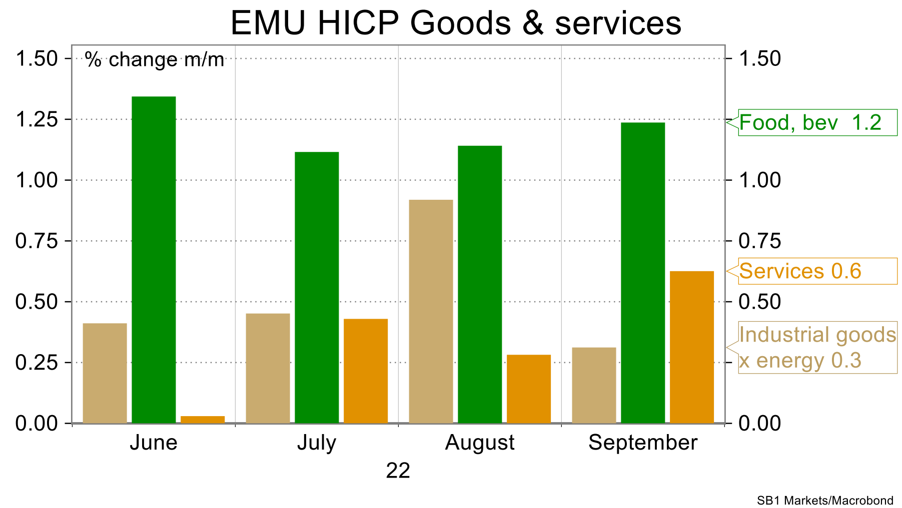


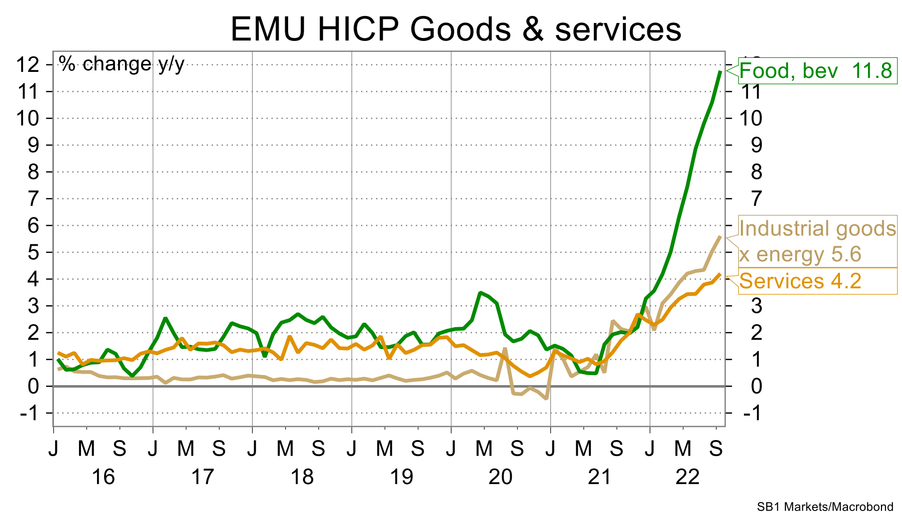
- Food prices rose 1.2% in Sept, more or less in line with price hikes recent months – and they are up 11.8% m/m
- Gas prices have come down somewhat recently and might bring headline inflation down…

Inflation is broad based – everything is above a 2% path since 2019!

Food inflation at 11.8%, industrial goods x energy at 5.6%, and services 4.2%. The target? 2%...



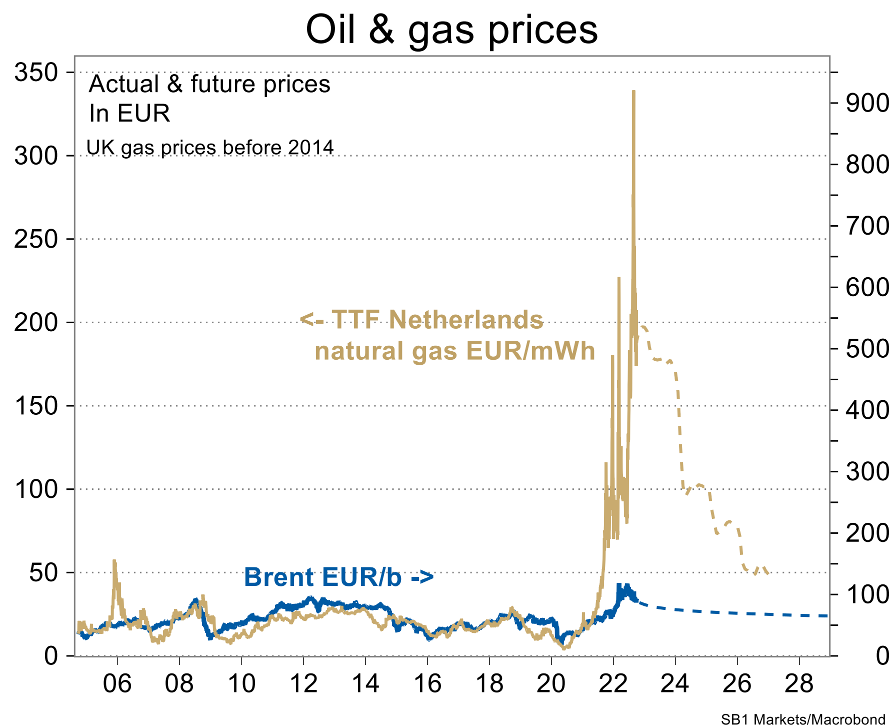


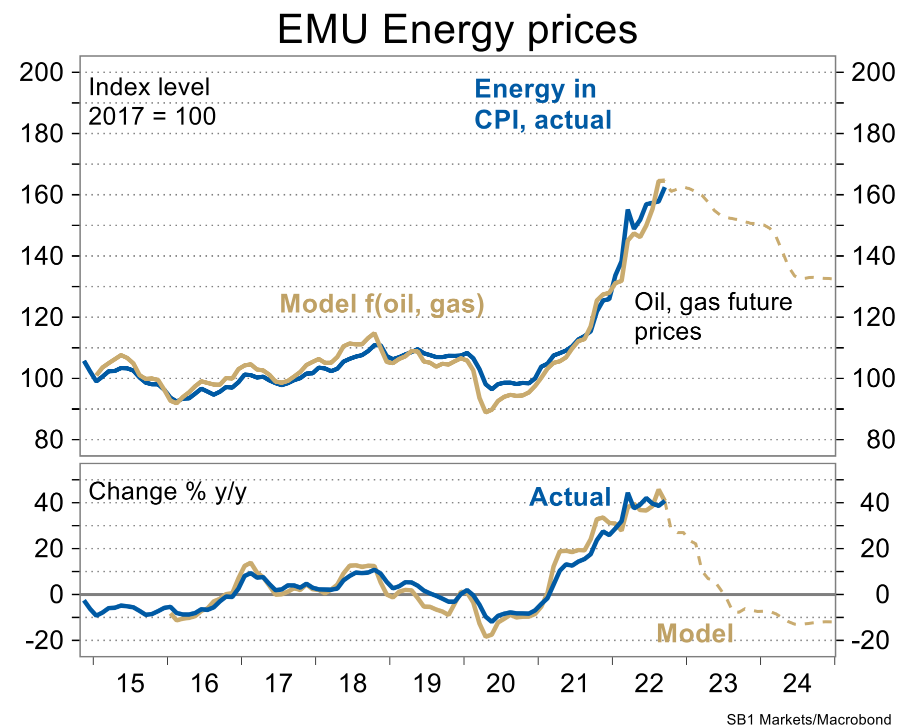


- **Industrial goods** prices increased 0.3% in Sept, and are up 5.6% y/y. And now, these prices are finally above a 2% path since 2019
- **Services prices** gained 0.6% in Sept, and these prices are also above a 2% path vs the 2019 level – and they are up 4.2% y/y. Transport and hotels/restaurants have contributed on the upside last year (but no detailed data for Sept yet)
- (No further details in the preliminary HICP report)

Gas, oil prices have lifted 'energy CPI inflation' up to 40% but....

…if futures markets are correct (this time…), annual energy inflation is close to the peak

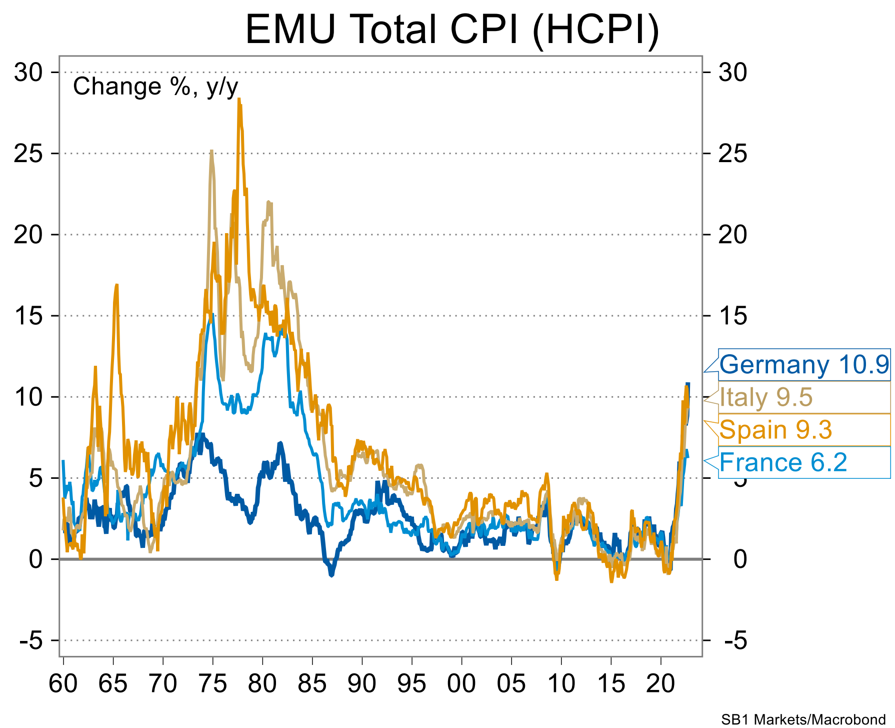


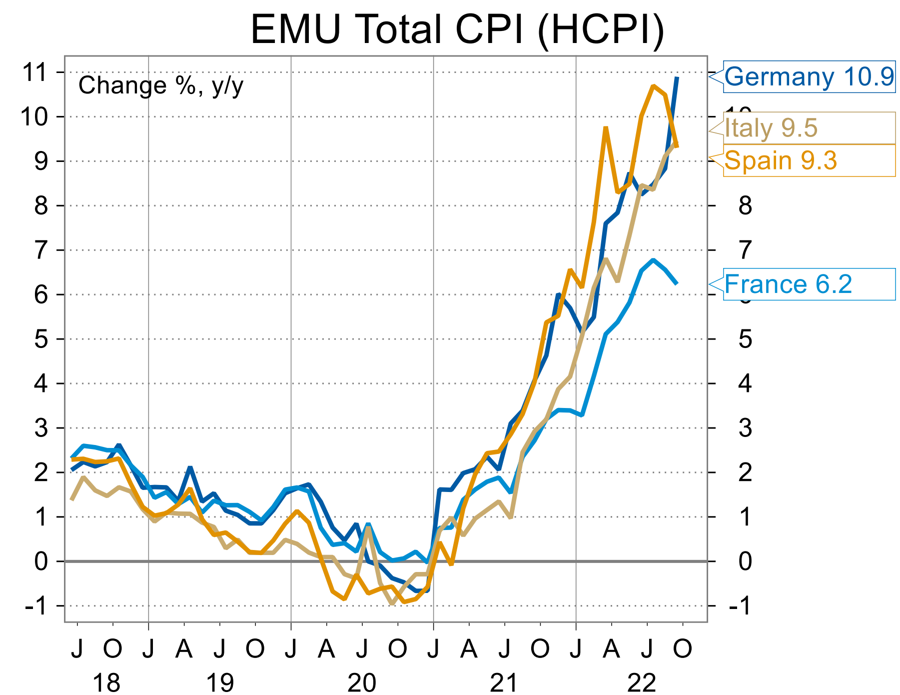


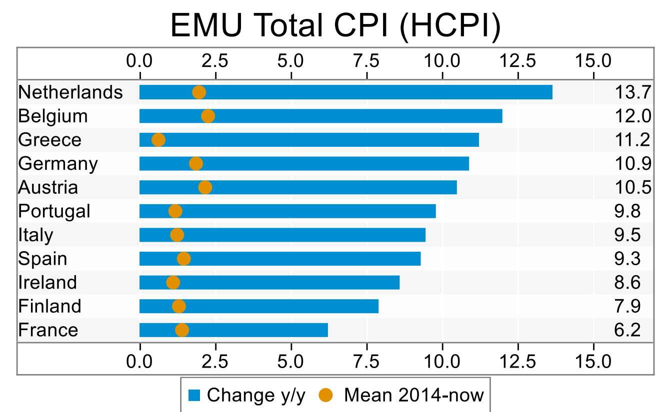
- Futures prices have come down from the top, even if prices in the short end of the curve rose post the gas pipe sabotage
- Early next year, energy prices will be down, measured y/y – even after the current surge. If the market this time is right

Inflation is high across the union

But the inflation in France and Spain are down from the peak



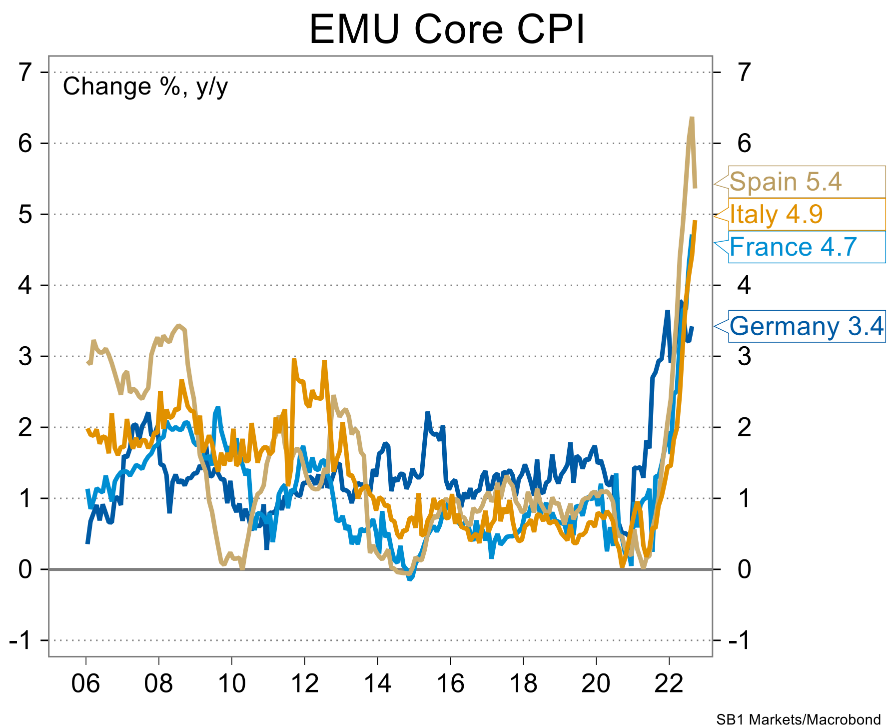


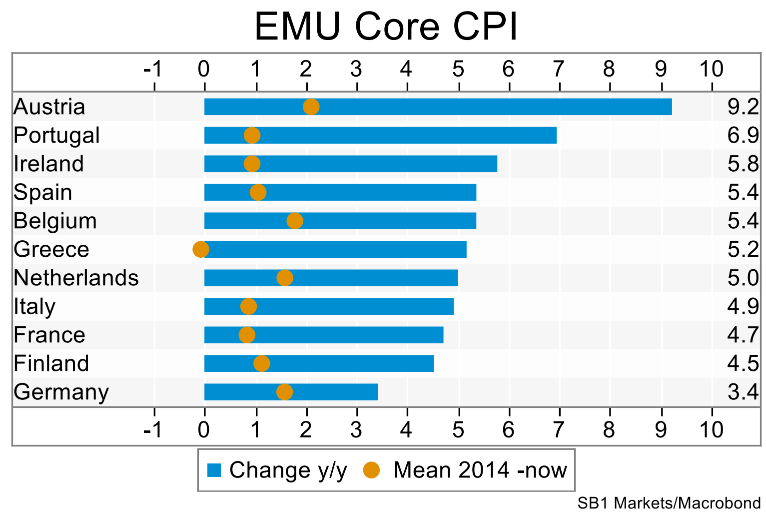


- In fact, the Spanish CPI (HICP) fell m/m and surprised on the downside in September (as did the French index)
- In the biggest EMU economy, Germany, however inflation surprised on the upside – increasing 2.4% m/m, twice as much as expected, bringing the y/y rate to 10.9% - the highest since 1949 – and then back to the early 1920s, during the Weimar Republic

Core inflation is, of course, above the 2% target everywhere as well

...putting pressure on the ECB

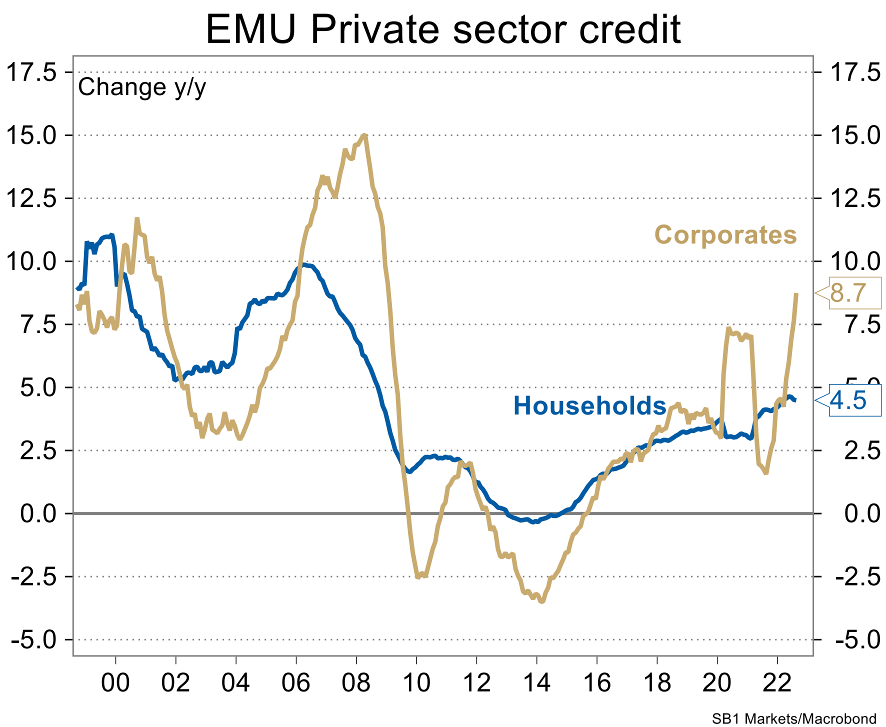


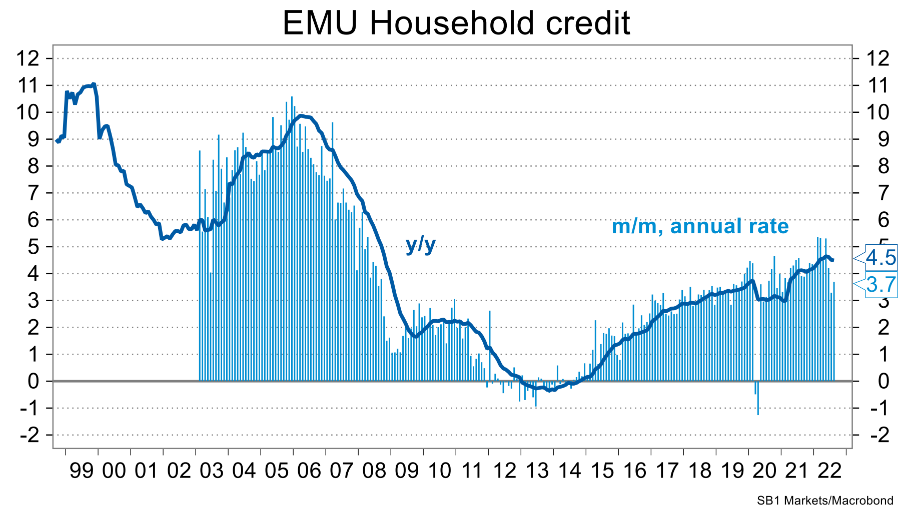


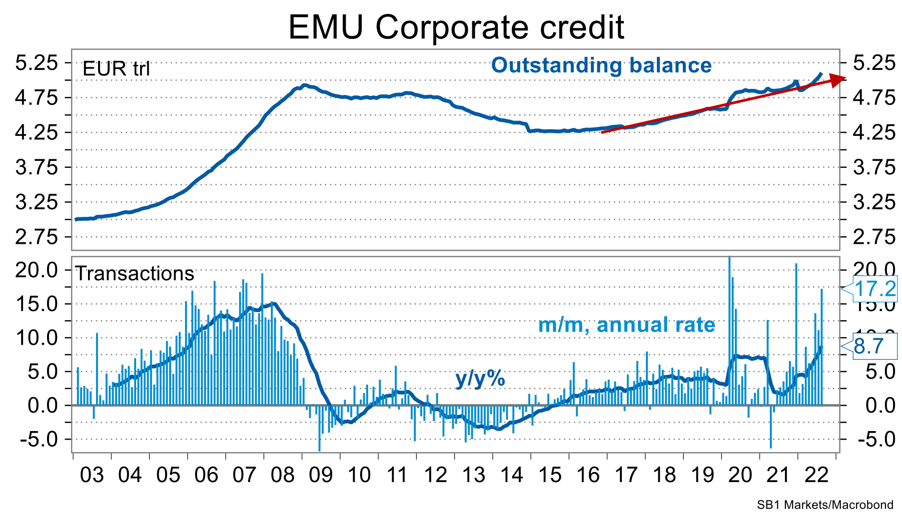
SpareBank 1 MARKETS

Corporate credit growth has accelerated. Households slowing?

Growth in household debt increased slightly in Aug, but the y/y rate is coming down



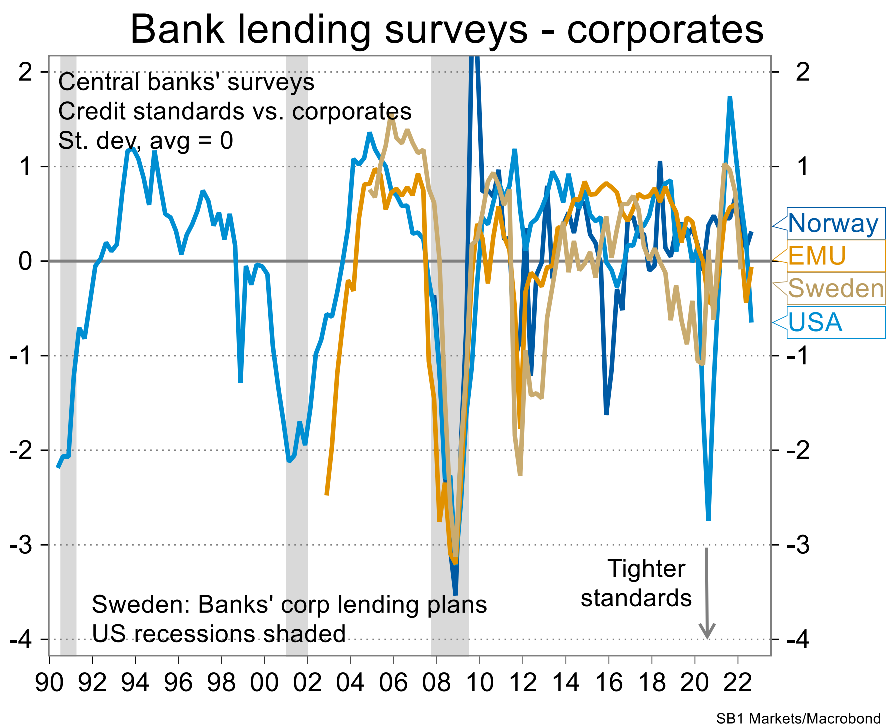


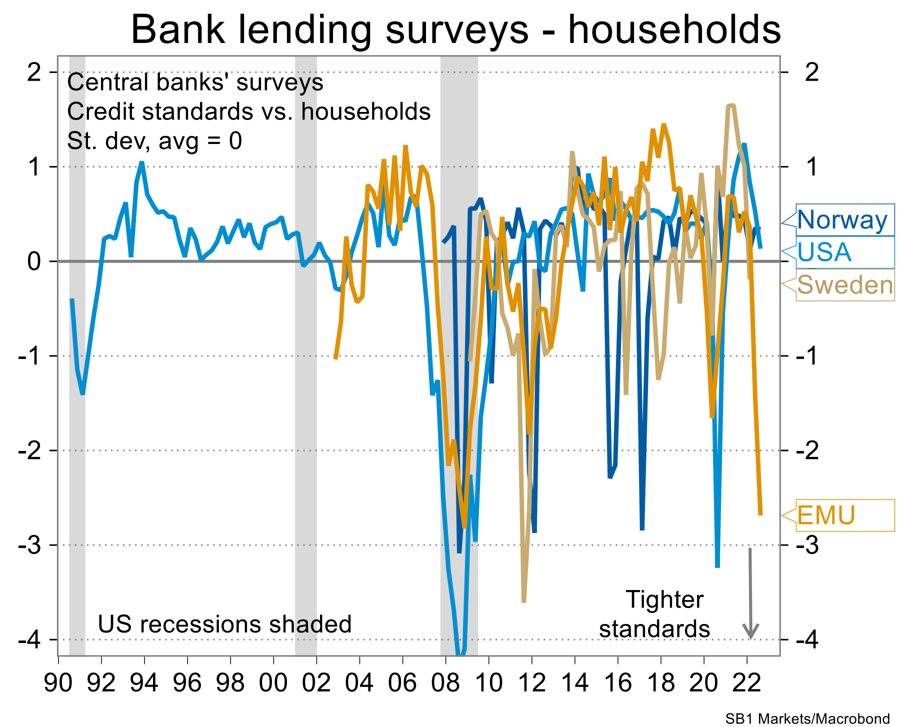


- **Annual growth rates** at 4.5% – 8.7% are well above normal nominal income growth. Now, incomes are growing much faster due to high inflation (=income for the corporate sector) and strong growth in employment, out of the pandemic
  - » The **corporate debt** level is above the pre-pandemic trend growth path, as is **household debt**
- Household credit growth has slowed significantly since June. A warning sign?
- The last **banking survey** was mixed, check next page

European banks report tighter standards vs. households

EMU banks have not reported such a tightening of standards vs. households since the GFC

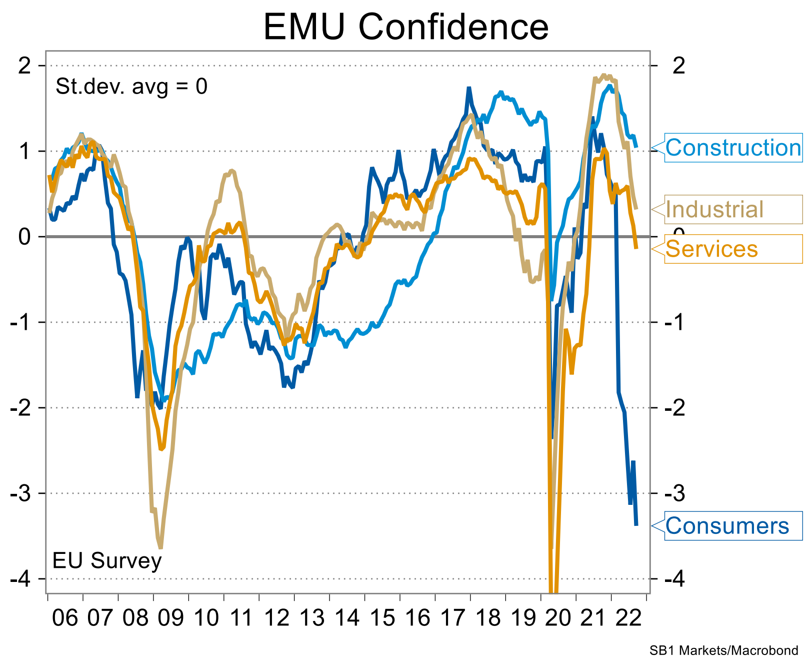


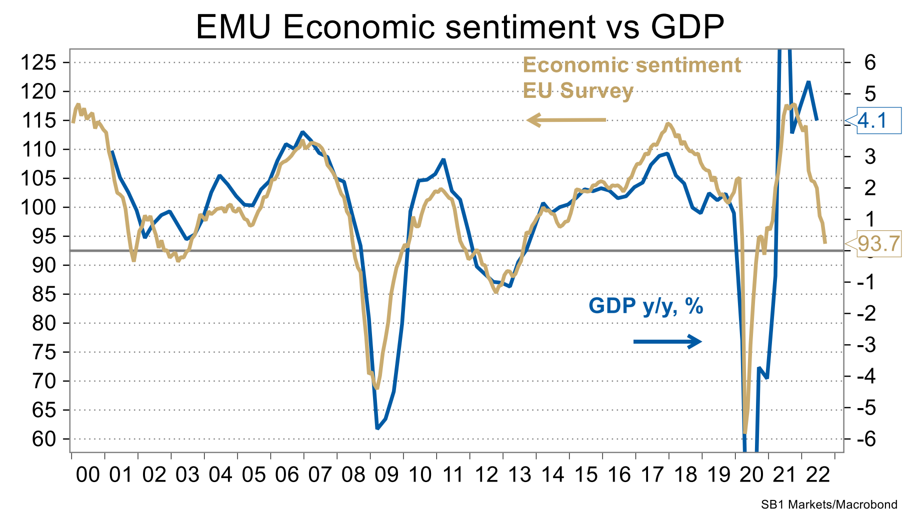


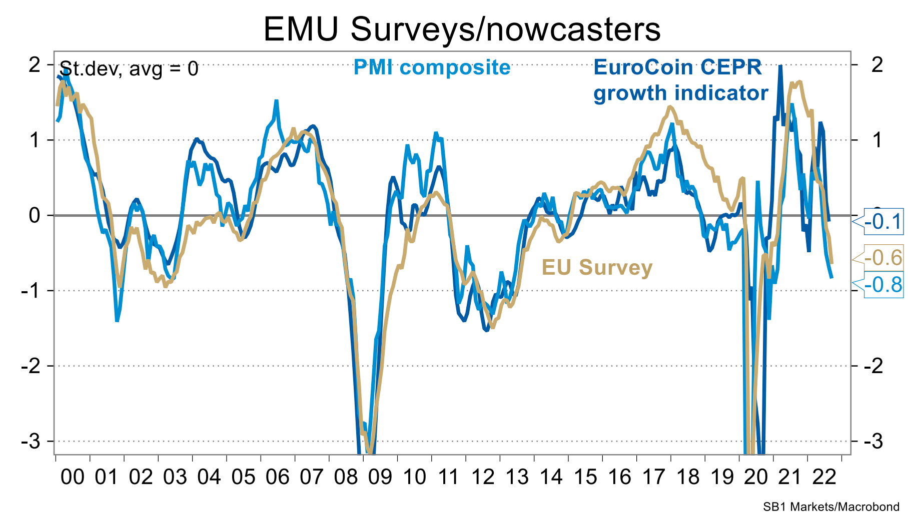
- However EMU banks are not yet reluctant to offer loans to the businesses
- **US banks** are signalling tighter lending standards vs corporate sector but not vs households
- **Norwegian banks** are close to neutral, at least they were in early Q3. We assume some tightening is taking place, especially in vs the commercial real estate sector

Economic sentiment further down in Sept, and services are now in the neg.

The overall index fell 3.6 p to 93.7, expected 95. Still, businesses are reporting growth > trend!





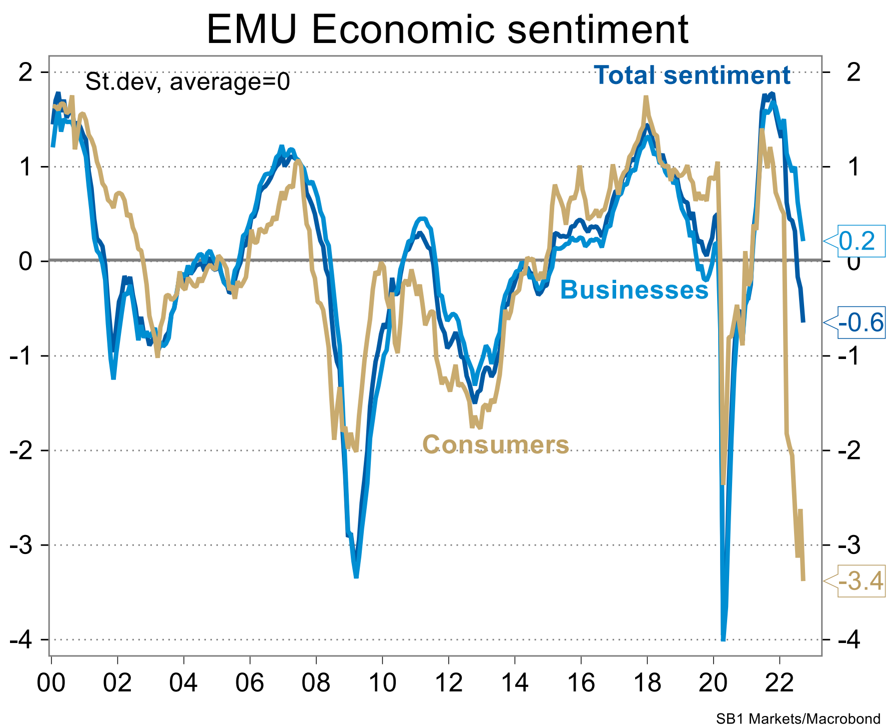


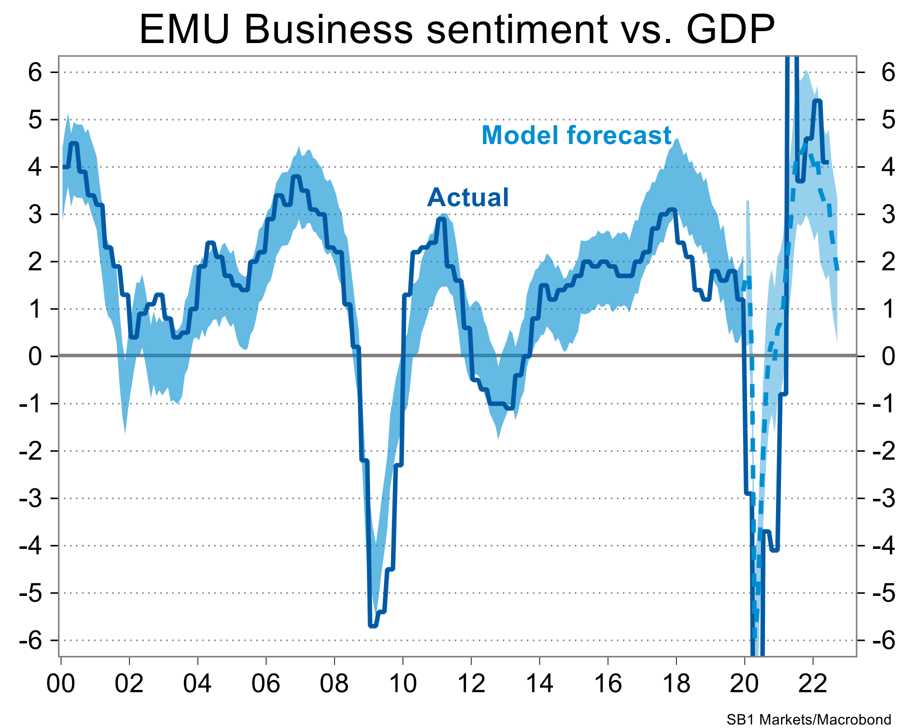
- **The Economic sentiment index** is 0.6 st.dev below average, with a large contribution from households. Businesses are in average above (+0.2 st.dev) – but surely rapidly on the way down, and the service index fell below average
- Thus, even if there is war nearby, inflation is surging, businesses are still reporting growth above trend. Consumers are pessimistic but historically their views on the economy has been irrelevant vs. GDP growth, just businesses tell us something relevant (more next page)
- **All of the surveys we follow are now signalling growth below trend,** or an outright recession (like the German Ifo survey)

SpareBank 1 MARKETS

Businesses are still reporting growth above average, rather surprisingly

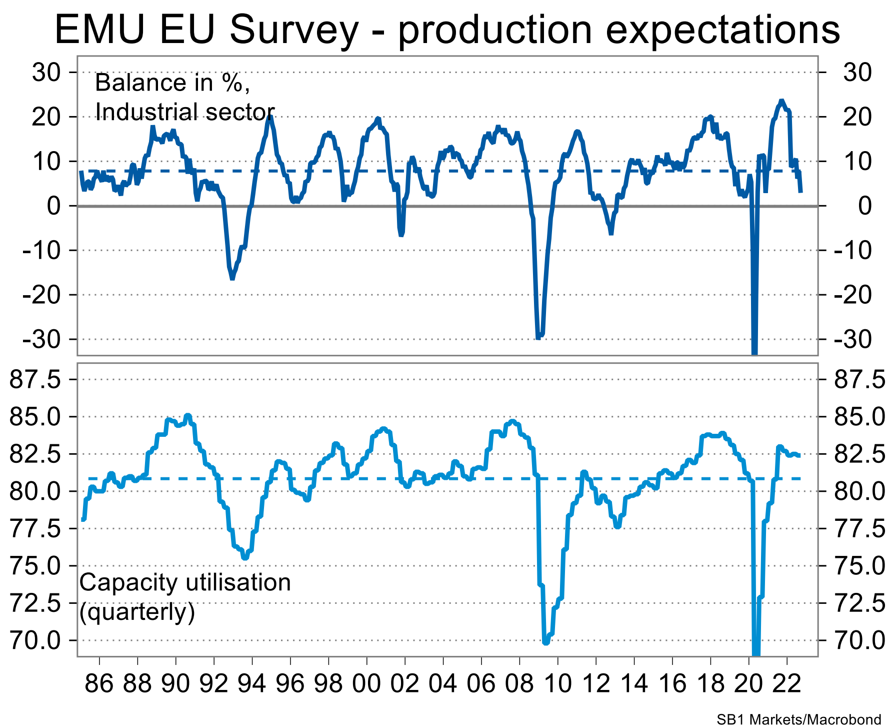
Historically, no contribution to the GDP forecast from households, just from businesses

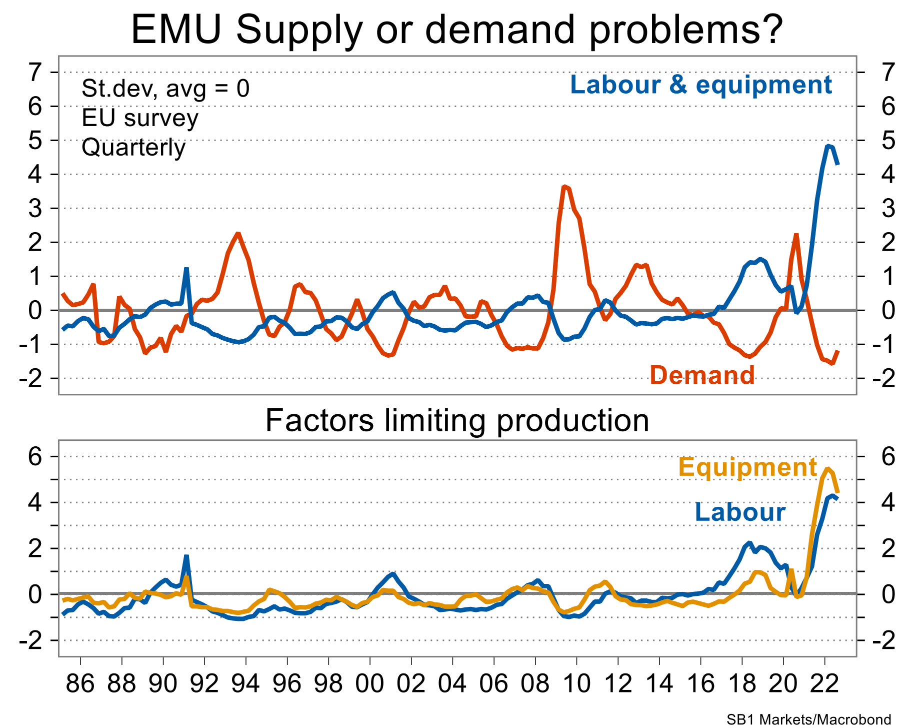




Production expectations down to below average

Capacity util. well above average. A few more complain about sales, fewer about supply shortages

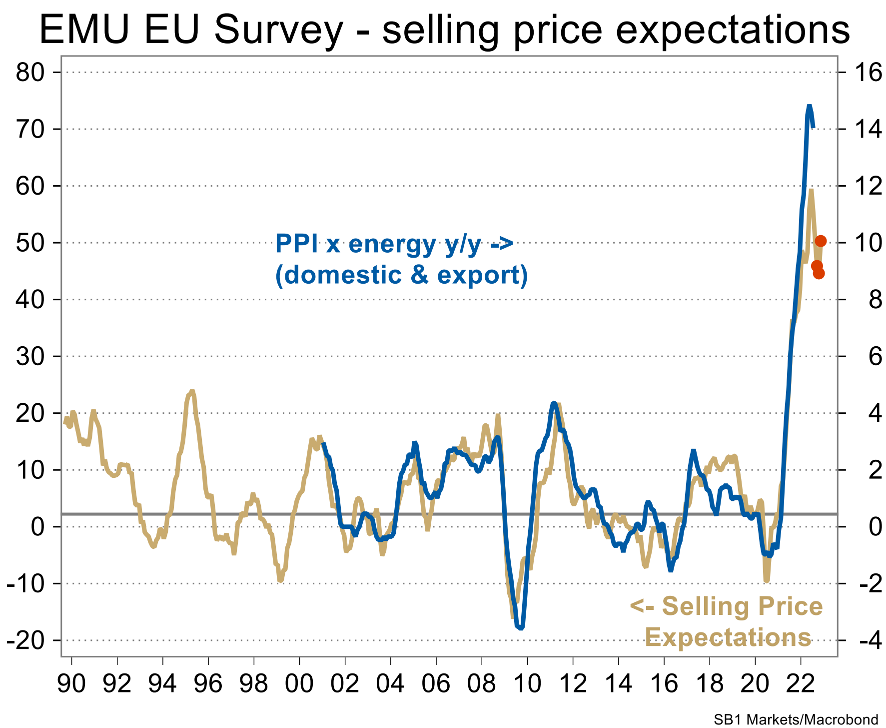




- However, supply shortages, primarily labour and equipment, are fare more wide-spread than normal. At the same time, even if the share rose marginally in Q3, close to record few companies complain about demand
- Even if the economy is now clearly slowing, the business part of this survey, and the record low unemployment rate, give the ECB arguments for hiking the signal rate further this week

Companies report faster growth in selling prices

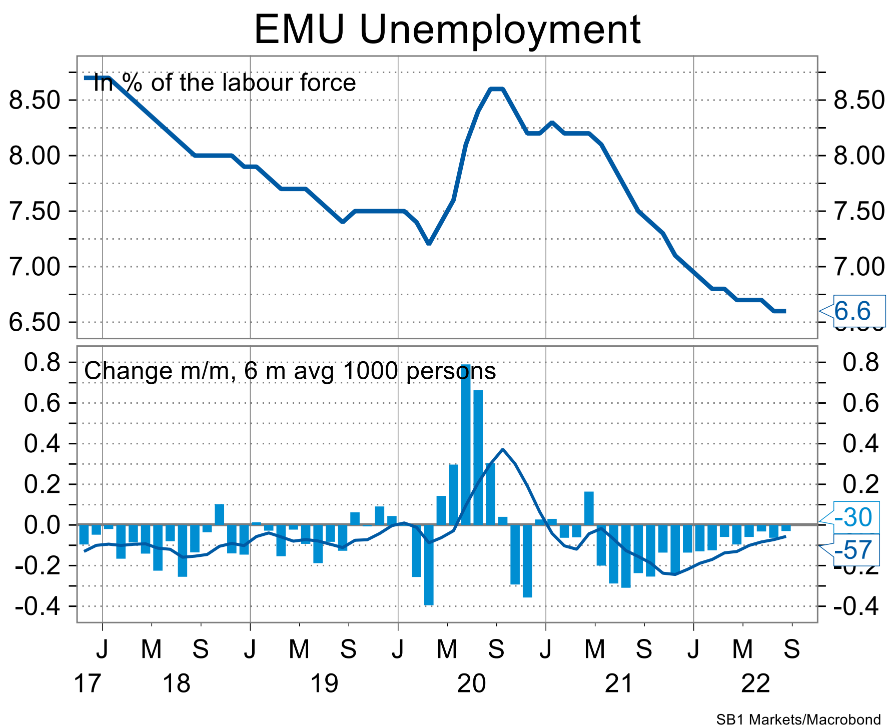
Quite surprising – and not encouraging

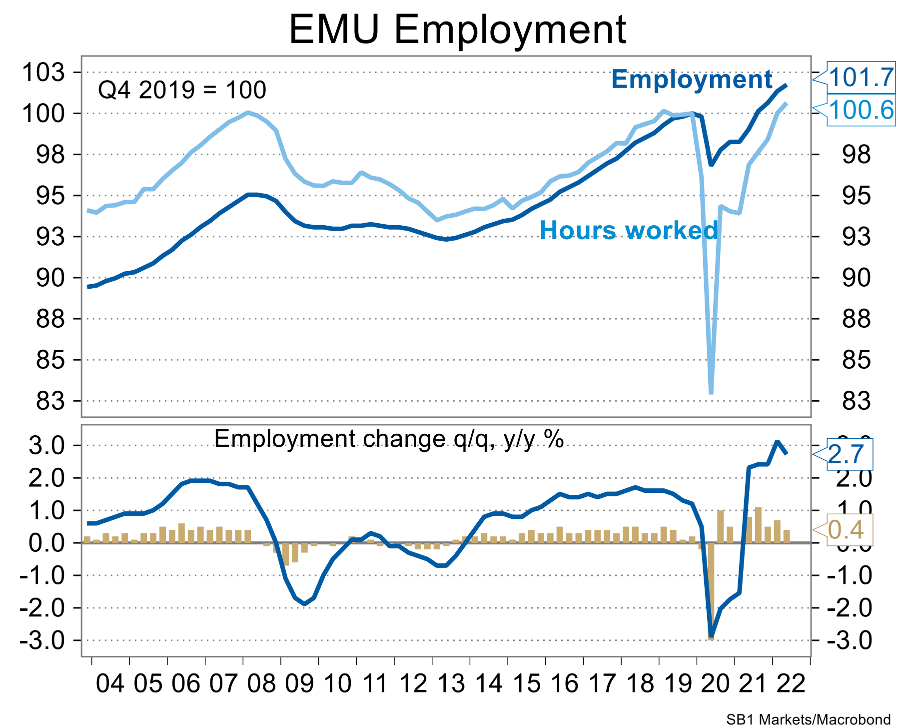


SpareBank 1 MARKETS

Unemployment flat at the lowest level since 1980 at 6.6% in Aug, as expected

The no. of unemployed fell marginally – and will soon turn up?

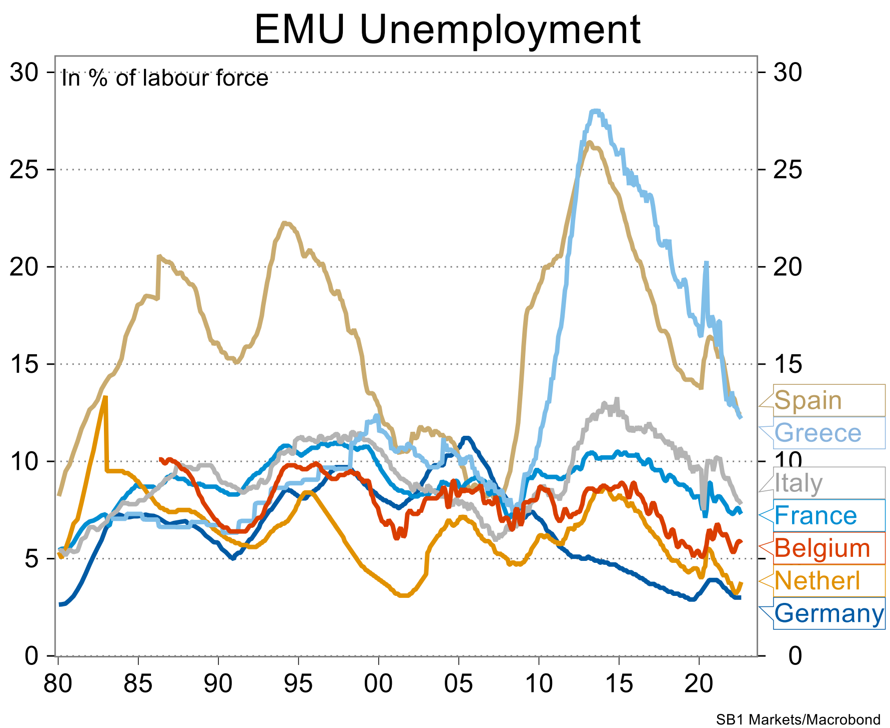


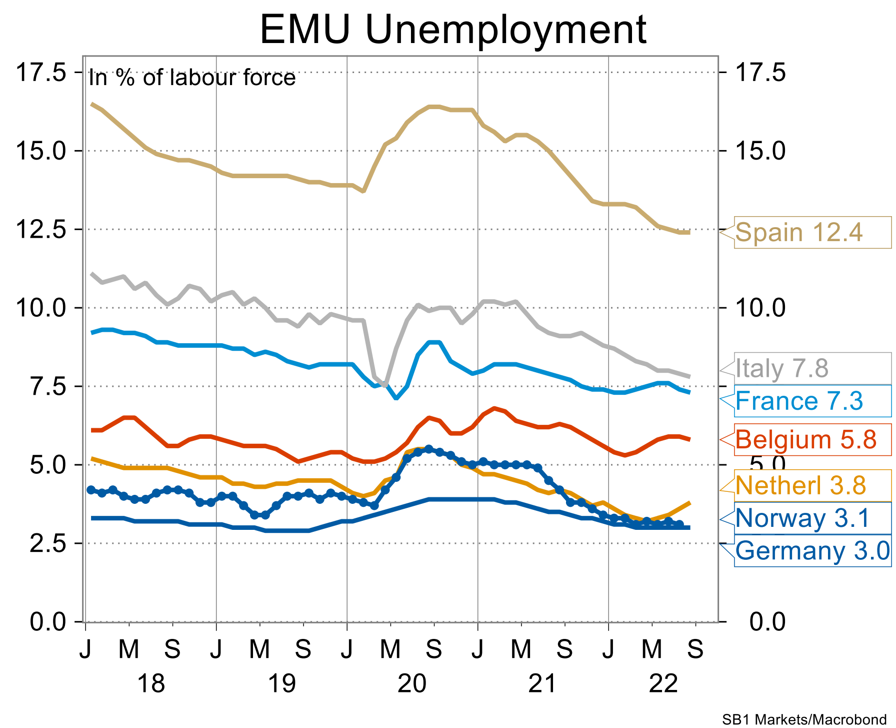


- **The number or unemployed declined in August**
- **Employment** grew by 0.4% in Q2 (not annualised), and hours worked grew too
  - » The employment level & the employment rate is higher than before the pandemic
- The number of **unfilled vacancies** soared to the highest level ever in Q2, by far
- The labour market is no doubt still very tight – until further notice
- **Wage cost inflation** has not accelerated but a slowdown in productivity growth has pushed labour cost per produced unit upwards, to somewhat above 2%

Unemployment is lower than average everywhere

Belgium has been marginally on the way up – and now the Netherlands has followed suit

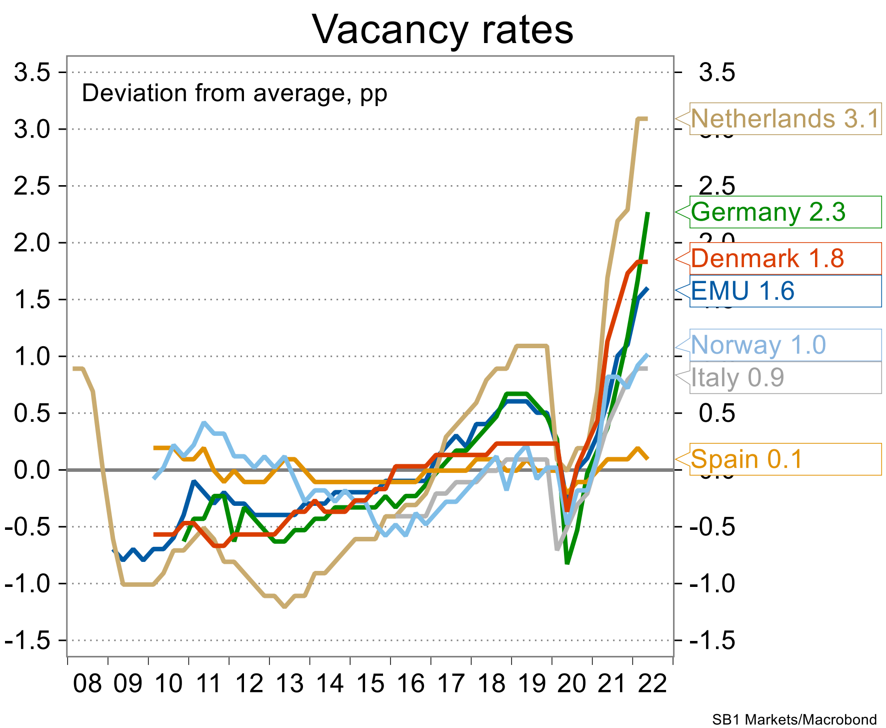


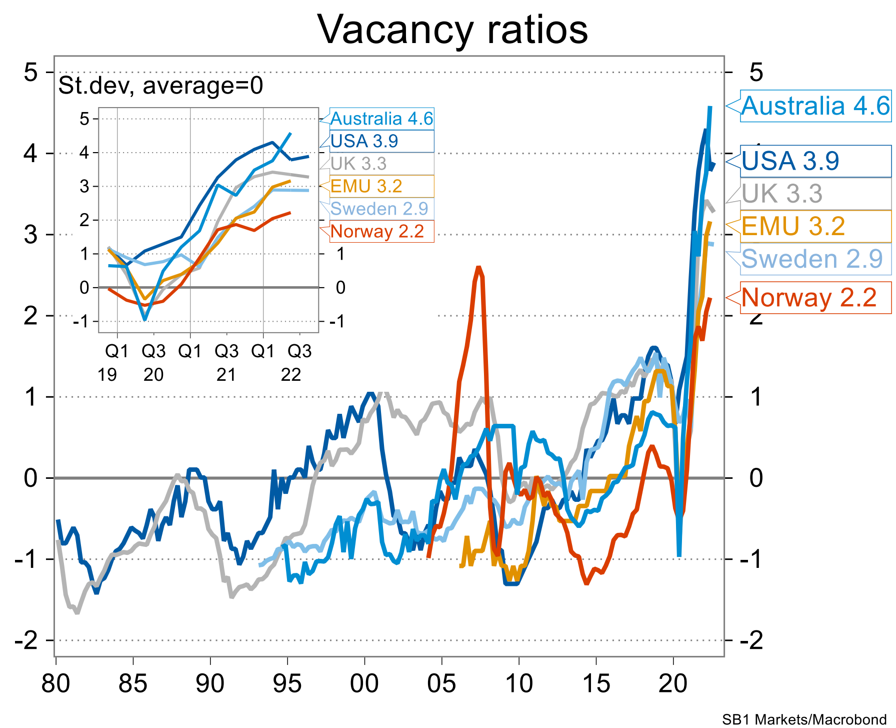


SpareBank 1 MARKETS

Vacancies record high almost everywhere

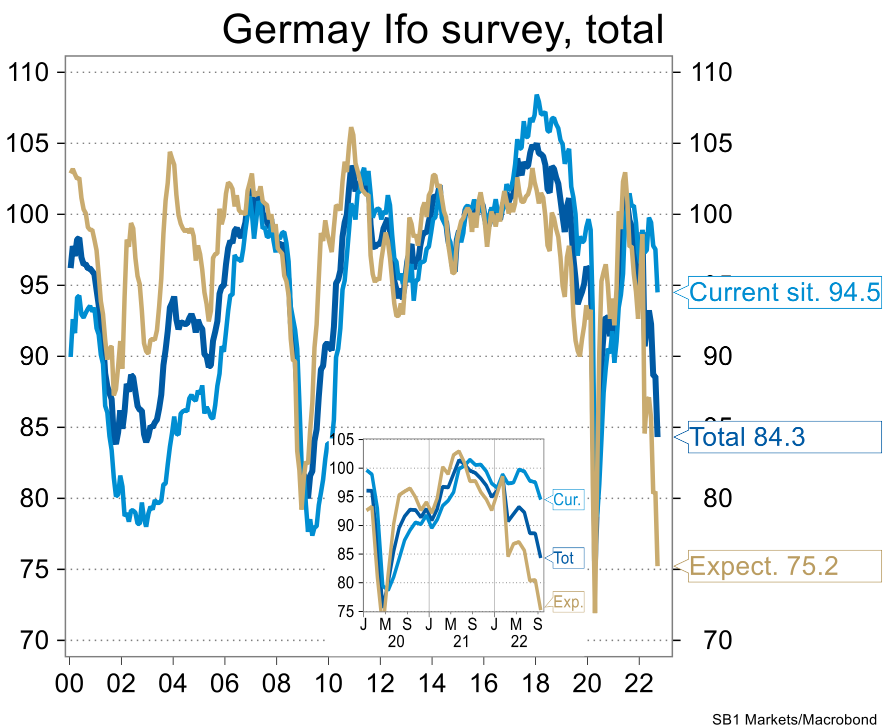
However several countries outside EMU have peaked

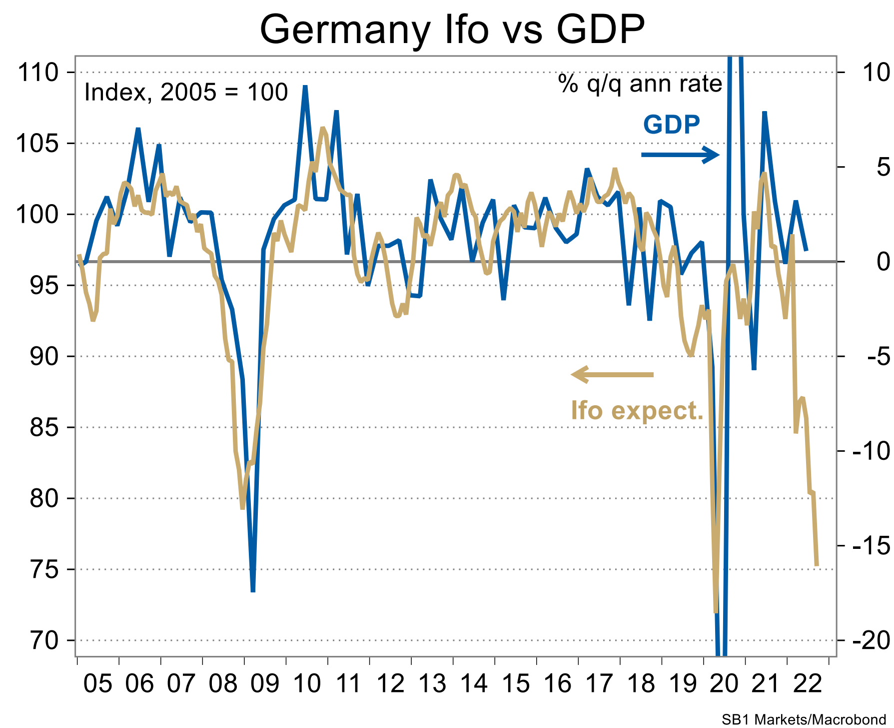




Ifo expectations plummeted in September – sentiment is dire

The index fell 5.3 p to 75.2, and signals a substantial fall in GDP. Market expectations were at 79



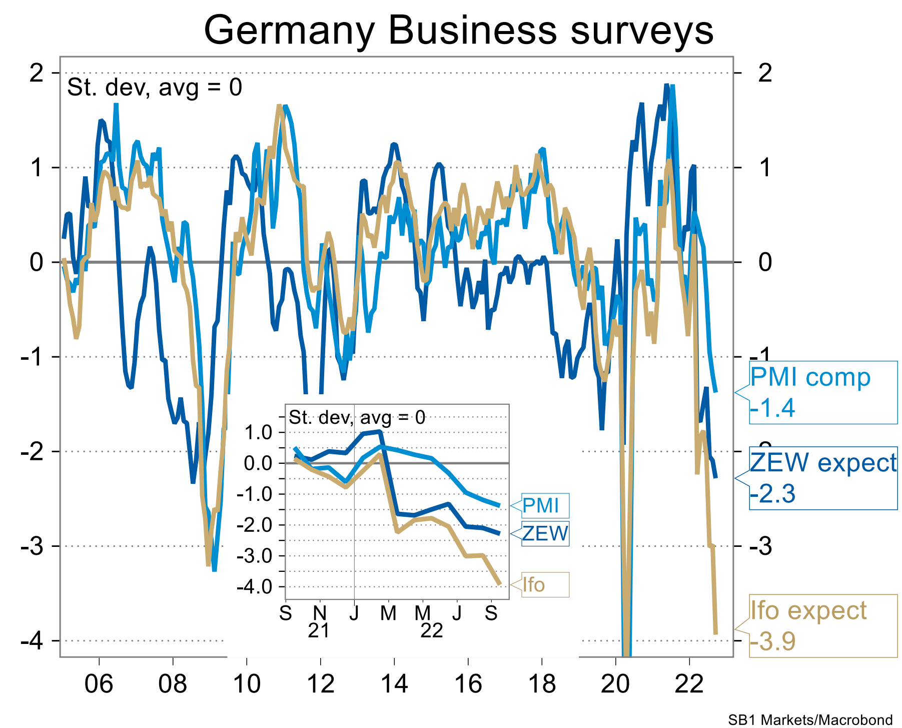


- **The expectation index** fell 5.3 p to 75.2, 4.8 p lower than expected. The level is very low, at 3.9 st.dev below average, lower than the lowest print during the financial crisis. The correlation to GDP is not perfect but a huge decline in GDP is signalled, at a 16% pace! The energy crisis is no doubt the main reason for the sharp deterioration of business sentiment
- The **assessment of the current situation** fell 3 p to 94.5, 1.5 p below expectations. The level around average – signalling a normal growth rate. The problem is the expectations
- The **total Ifo business climate index** fell by 2.3 p to 84.3; expected 87

Business climate: the average of the current situation and expectations

All sectors report of weaker business climate in September

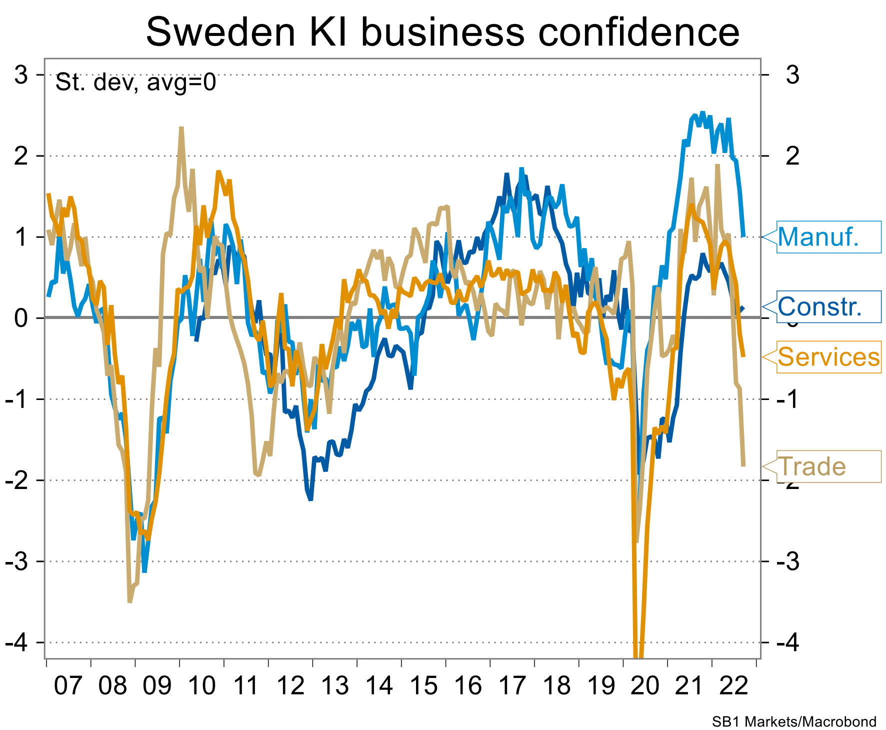
And all sector indices are below average

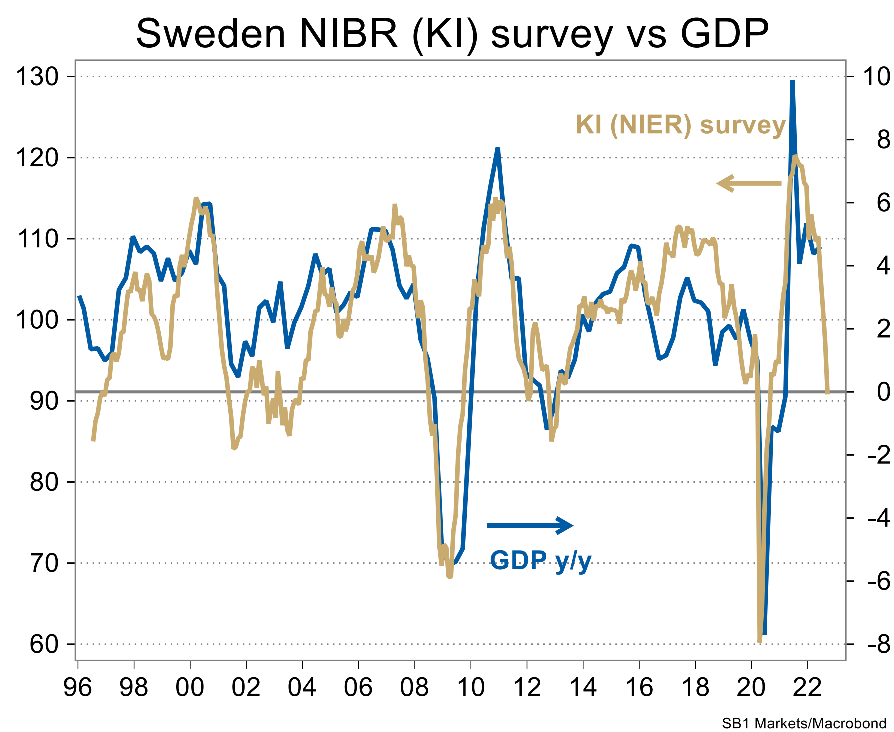


- Other surveys are also well into negative territory, signaling slower growth/fall in output in the coming months

Business confidence deteriorated sharply in September, zero growth signalled!

Confidence in the manufacturing sector fell, but is still strong at 1 st.d. above average

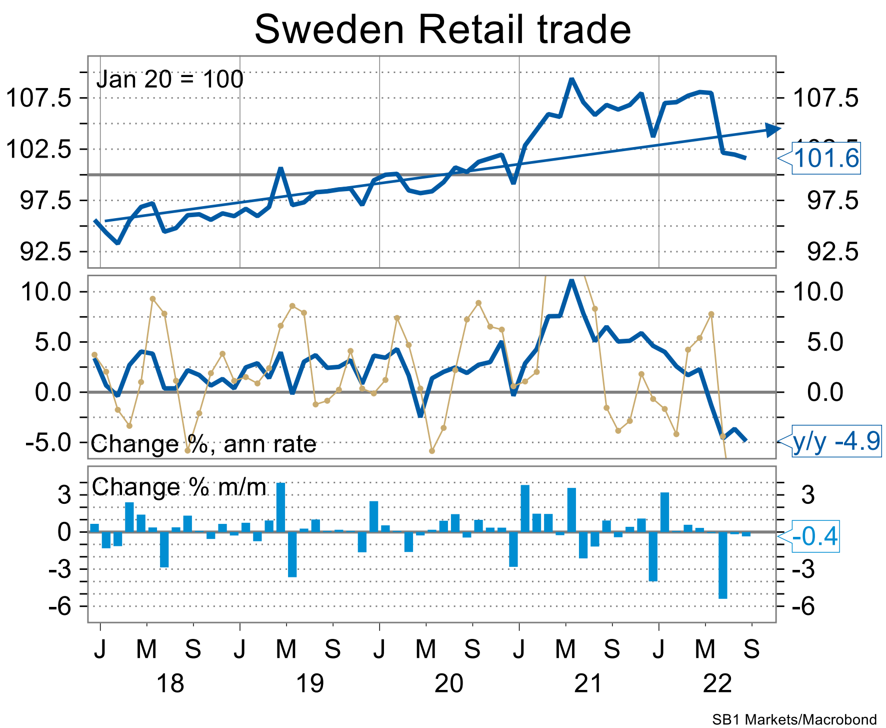


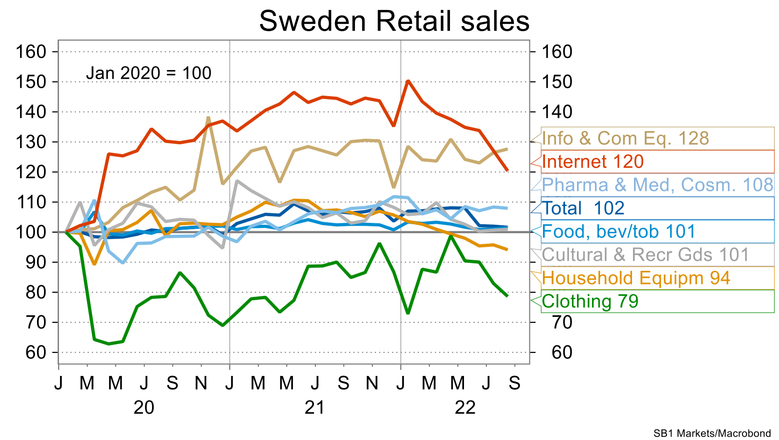


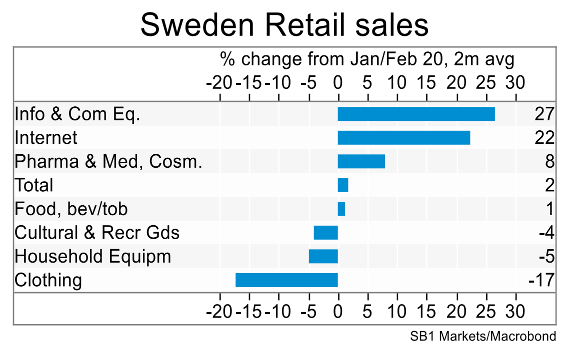
- **The composite index** fell to 90.8 in September from 97.2 in August. The decline equals a 0.7 st.dev decline to 0.9 st.dev below average. The index signals zero GDP growth, down from +2% in August. The Riksbank expects a small increase in GDP in Q3 (q/q) but then a 0.9% (total) decline in Q4 and Q1
- **3 out of 4 main sub-sectors** are reporting declining confidence
  - » The **trade sector confidence plummeted** in Sept, and is now 1.8 st.dev under water
  - » The **manufacturing sector sentiment** has declined over the past three months, however, manufacturing sector sentiment still remains strong
  - » Sentiment in **the construction sector improved** in Sept, and is now 0.1 st.dev above par

Retail sales down for the 4th month in August, down 4.9% y/y

Sales are now ‘just’ 1.1% higher than before the pandemic, and below the pre-pandemic trend



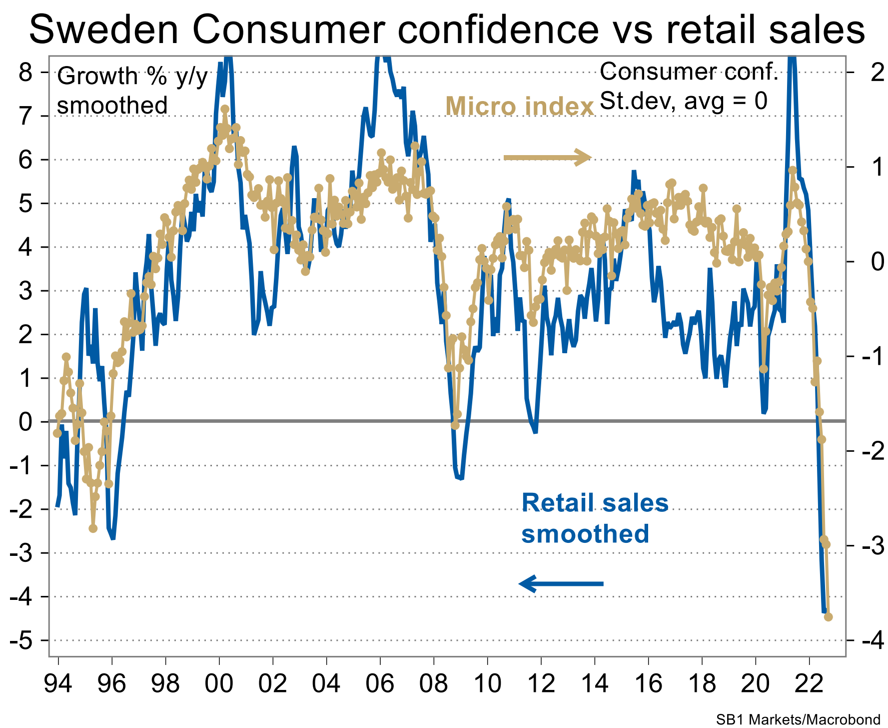


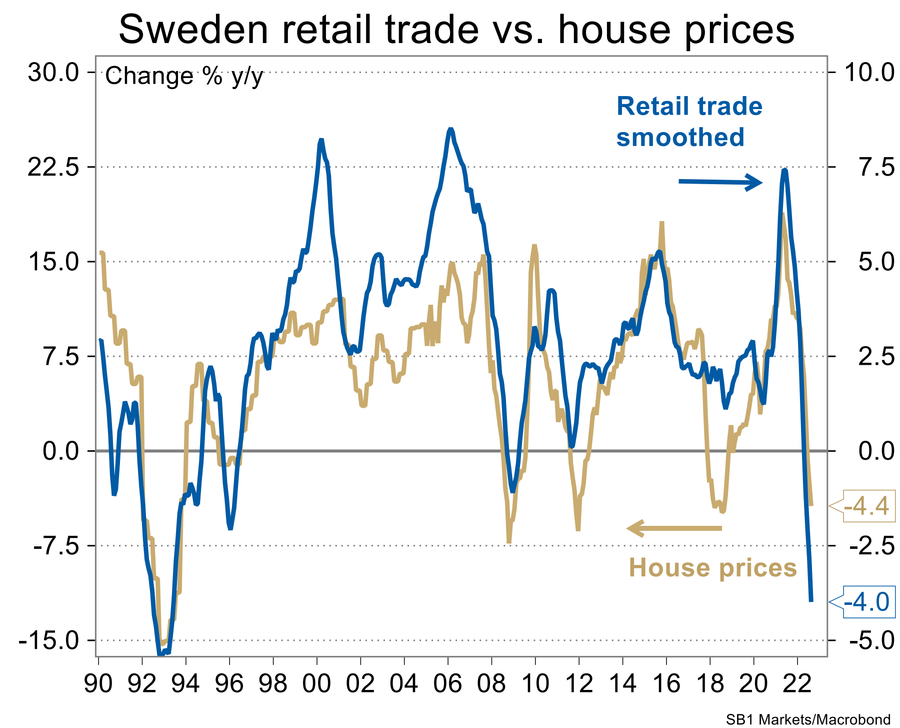


- **Sales fell 0.4% m/m in August**, following the 0.2% drop in July (revised up from -0.6%). Sales are down 6% from the peak last spring – and the underlying trend is down
- **The fall in retail sales was broad**: information and com. equipment sales fell by 12% m/m, clothing -10%, internet sales -6%, and food & beverage sales were down by 2%

Consumers are not just saying they are pessimistic: They walk the walk

House prices and retail sales down in tandem with consumer confidence

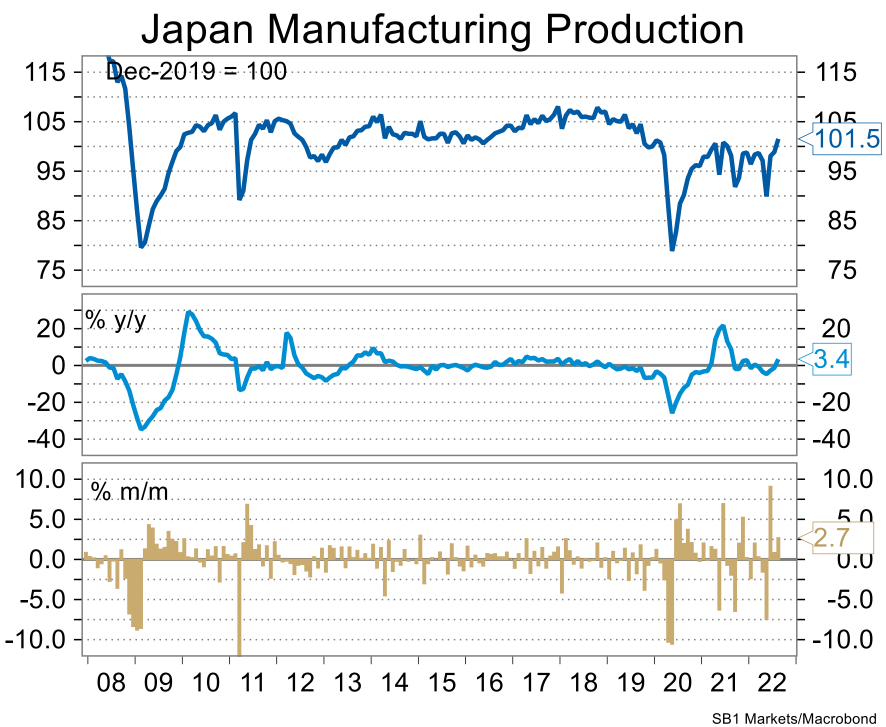


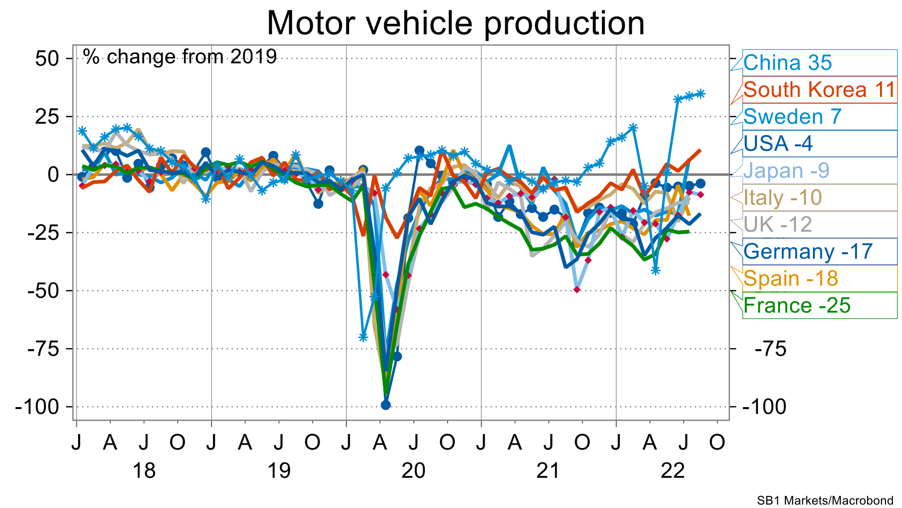


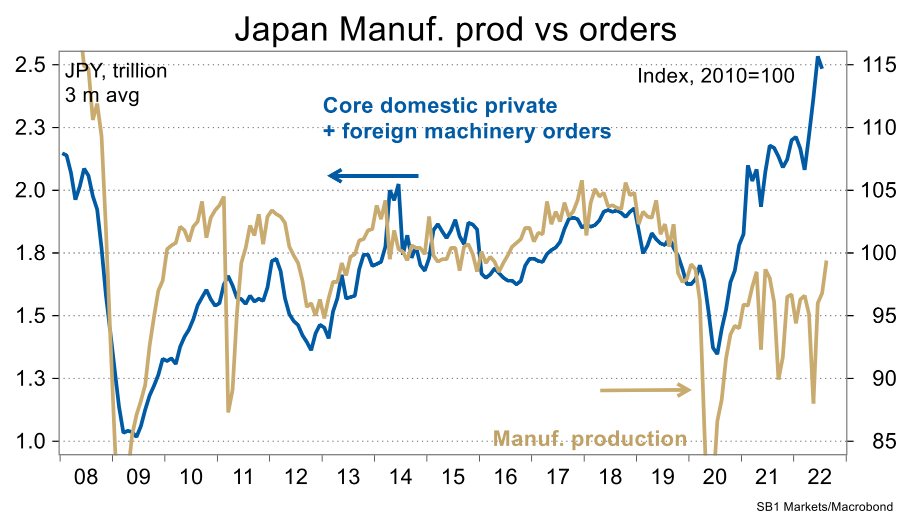
- **Consumer confidence** (the micro index)) fell 11.1 p to 41.2 in Sep from 52.3 in Aug (revised down from 56.3) – which is rather depressing, <u>at 3.6 st.dev below average</u>! The **macro index** was also down, to 2.4 st.dev below average from 1.9 st.dev below average, resulting in a total confidence index that fell to 3.6 st.dev. below average from 2.9 st.dev below average the month before
- Both **retail sales** and **house prices** have fallen alongside the decline in consumer confidence – higher rates and high inflation is softening both sentiment and ultimately demand - <u>the outlook is rather bleak</u>

Manufacturing production further up in August

Production rose 2.7% m/m, expected +0.2%



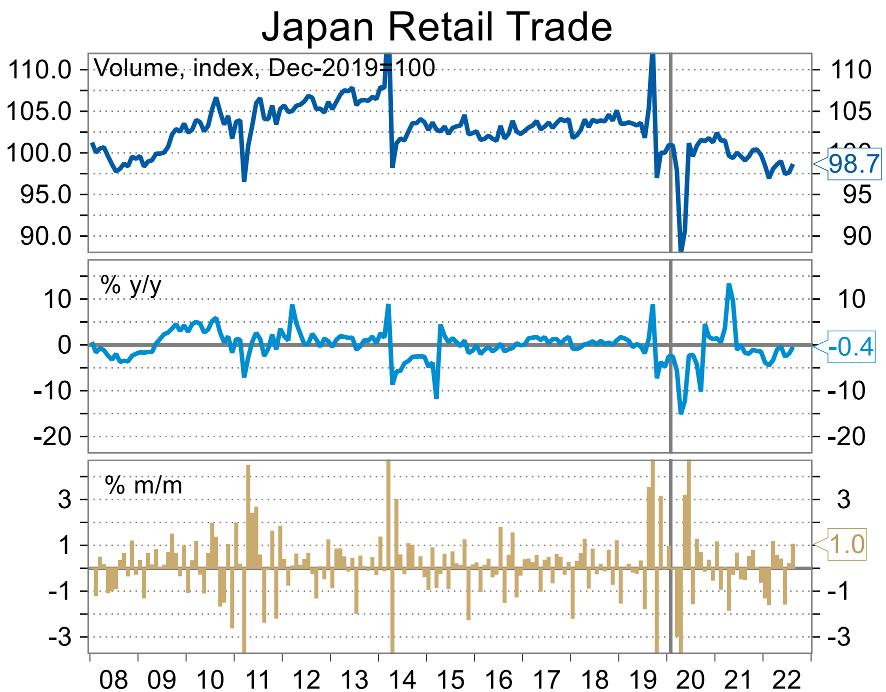




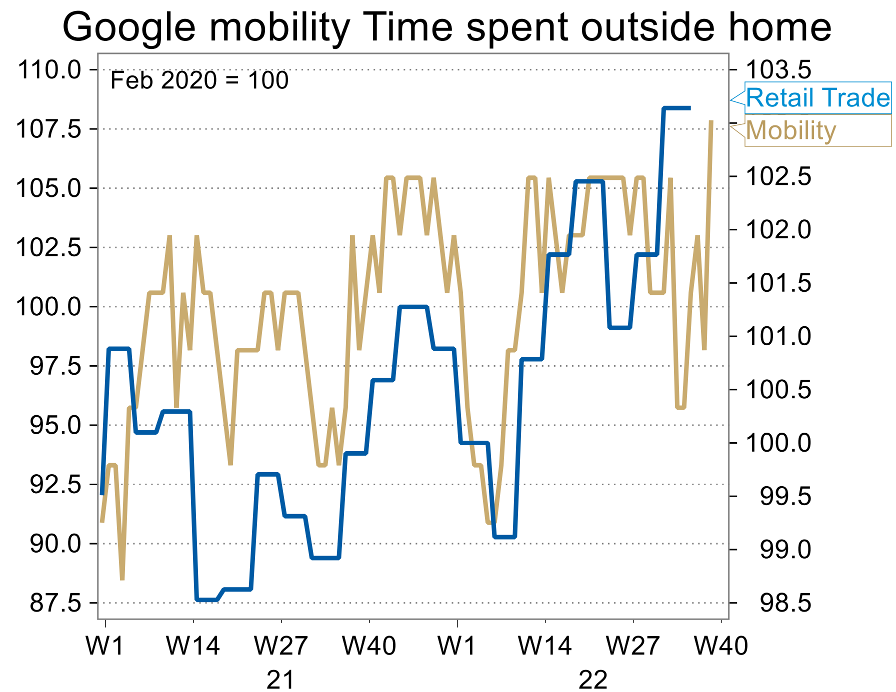
- **Production** fell due to a Covid wave and imposed restrictions in May but has since recovered, and is now back to the level before the lockdown. Disruptions due to lack of supplies from China is reported to have contributed to the temporary setback
- **Overall order inflow** has strengthened substantially through 2021, and into 2022. The declining JPY explains at least part of the increase, probably also higher prices

Retail sales rose in August – the trend since the spring is flat

… and the level is low



SB1 Markets/Macrobond



SB1 Markets/Macrobond

- **Retail sales** have been quite closely correlated to mobility (time spent outside home) recent months. However in August, mobility fell quite noticeably, but retail sales were up, likely due to the holidays. In September, mobility increased again, which could point to further growth in retail sales?

Highlights

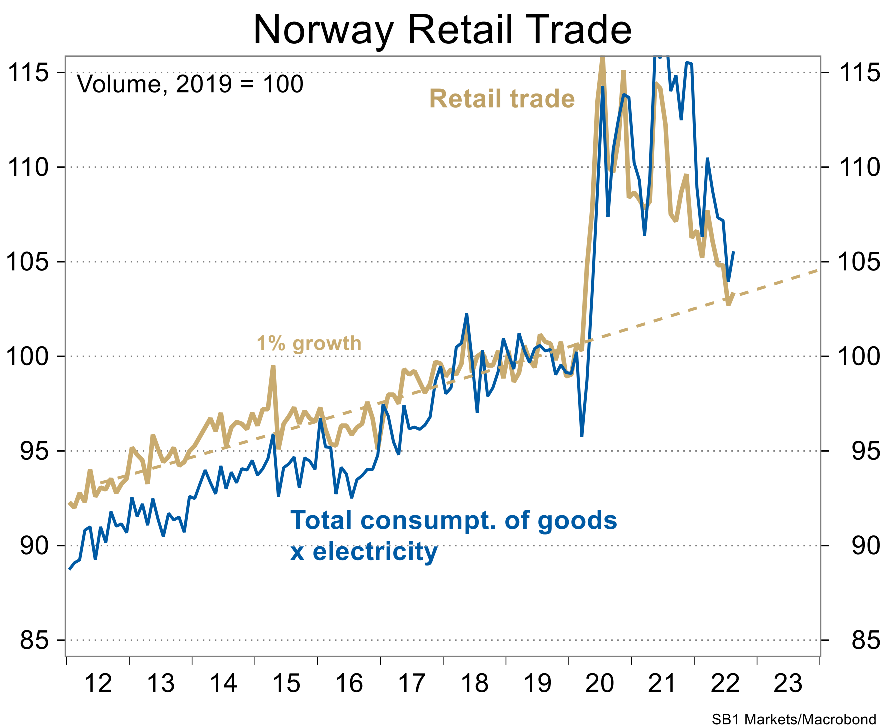
The world around us

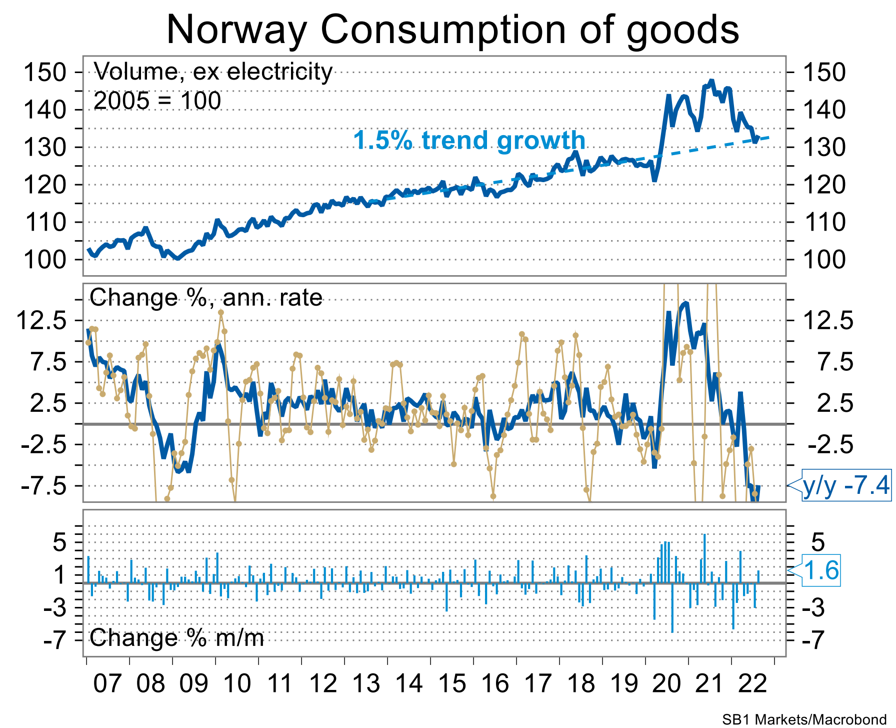
The Norwegian economy

Market charts & comments

Retail sales stronger than expected in August, but the trend is down

Retail sales were up 0.7% (expected -0.5%); total consumption of goods was up 1.6%

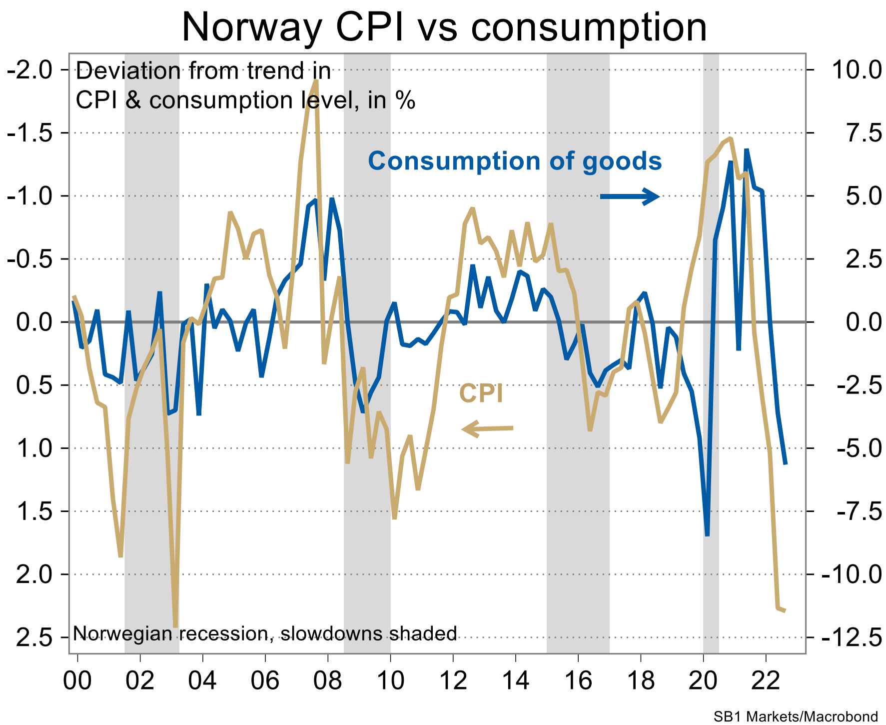




- **Retail sales** have been far more volatile than normal during the pandemic, and monthly data have been close to useless. Sales have been trending down since early 2021, like in many other rich countries, from levels that were miles above pre-pandemic trend growth path. **Total consumption of goods** gained 1.6% in August
- The lift in inflation and higher interest rates seem to have aided sales back down to the pre-pandemic trend – and we expect sales to fall below the trend the coming months/quarters
- Both household equipment (building materials) and food store sales contributed on the upside in August (both were down in July)

Higher consumer prices contribute to lower consumption

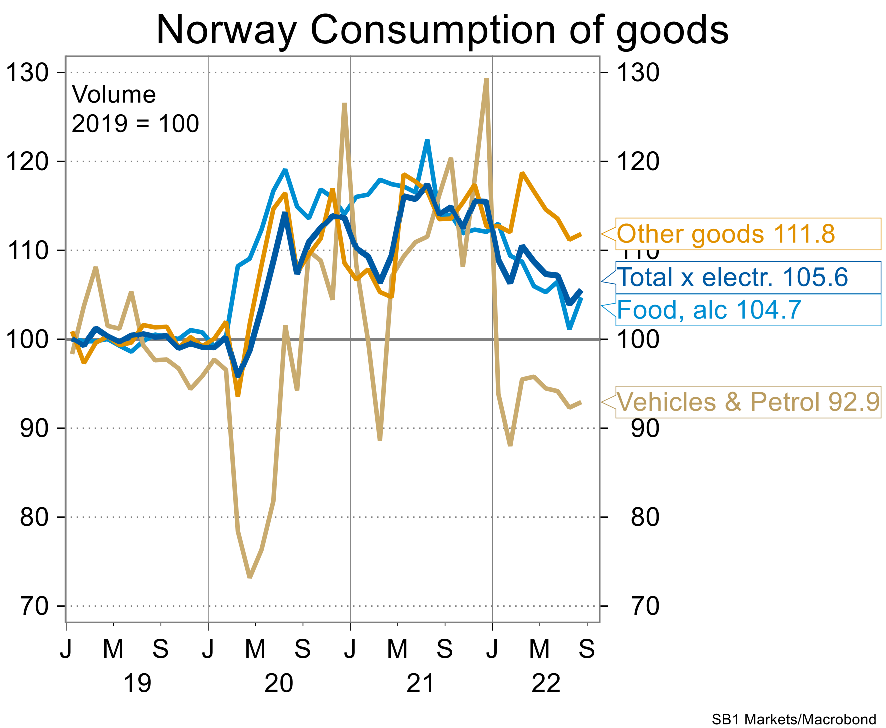
Consumption of goods (volume) are negatively correlated to changes in consumption prices

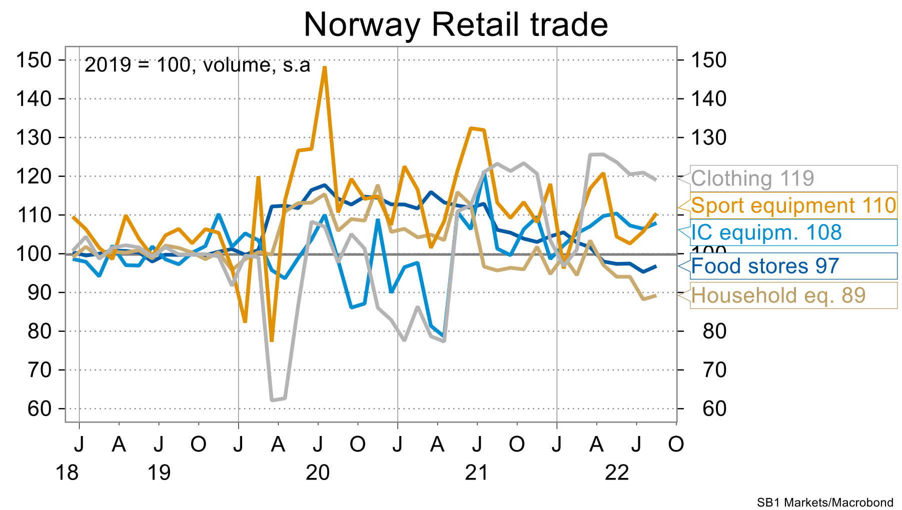


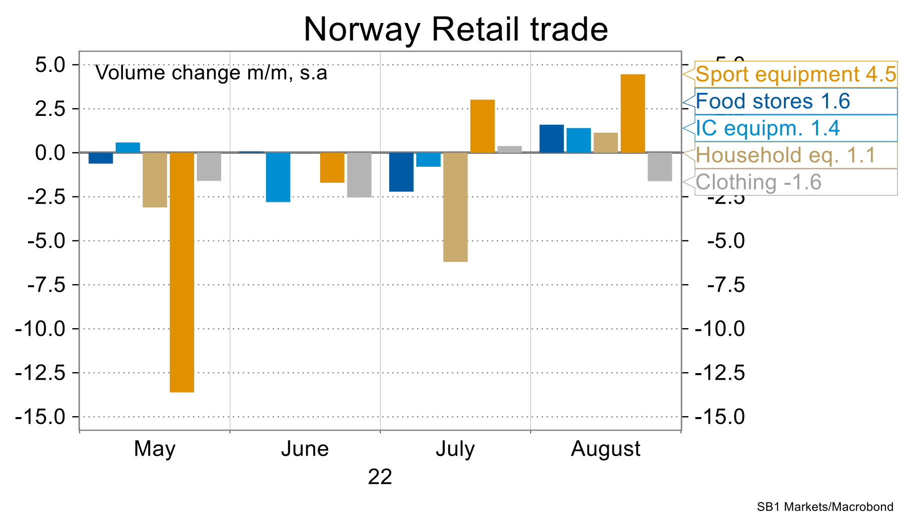
- The elasticity for consumption of goods vs. changes in headline CPU is some -2, probably as consumption of services normally are more stable than goods – and because high prices normally are associated with a weak Norwegian economy (like oil prices down, NOK weaker, higher imported inflation)
- This time too, consumption of goods has come down as the level of inflation has remained elevated – in conjunction with most of the pent-up demand after the pandemic seems to have dissipated
- In addition, interest rates are rapidly on the way up

Household equip. up 1.1%; Food sales up 1.6%; Sports equip. up 4.5% (in volume terms)

Household equipment sales are trading down, so are food store sales



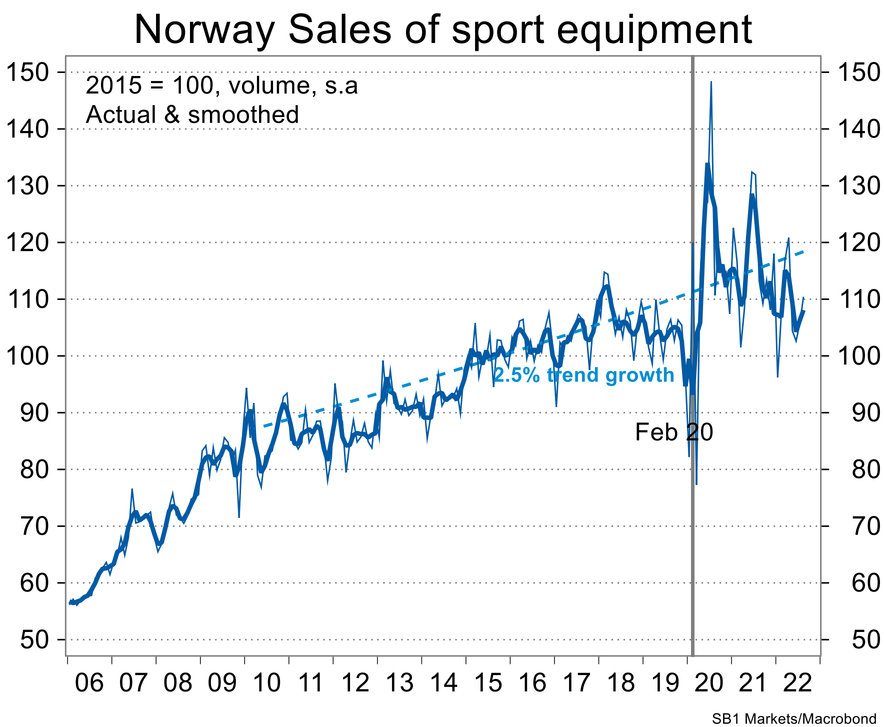




SpareBank 1 MARKETS

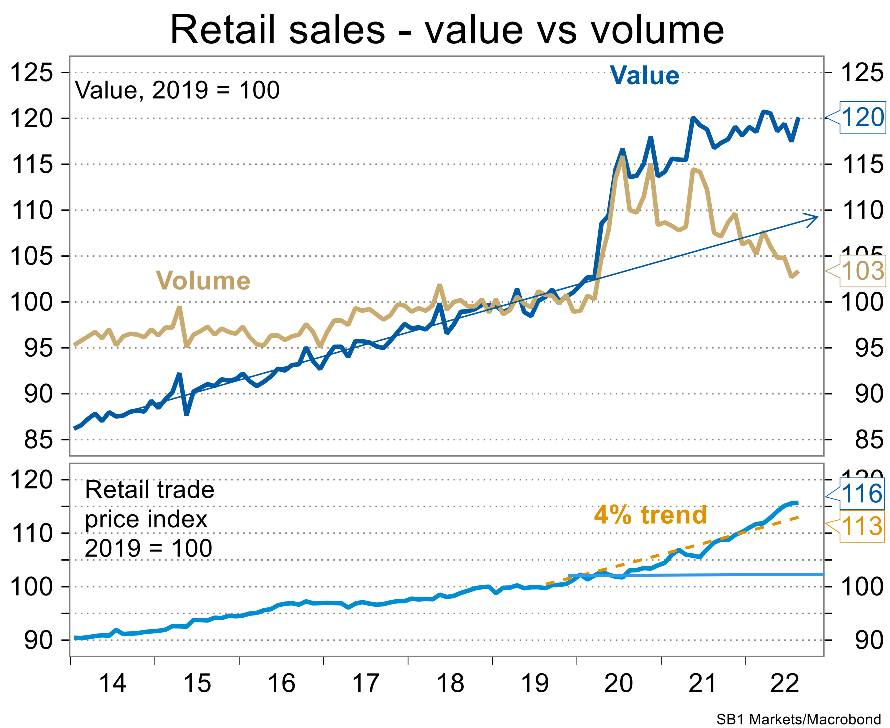
Sports equipment sales: Up 4.5% in September, but still below a normal level

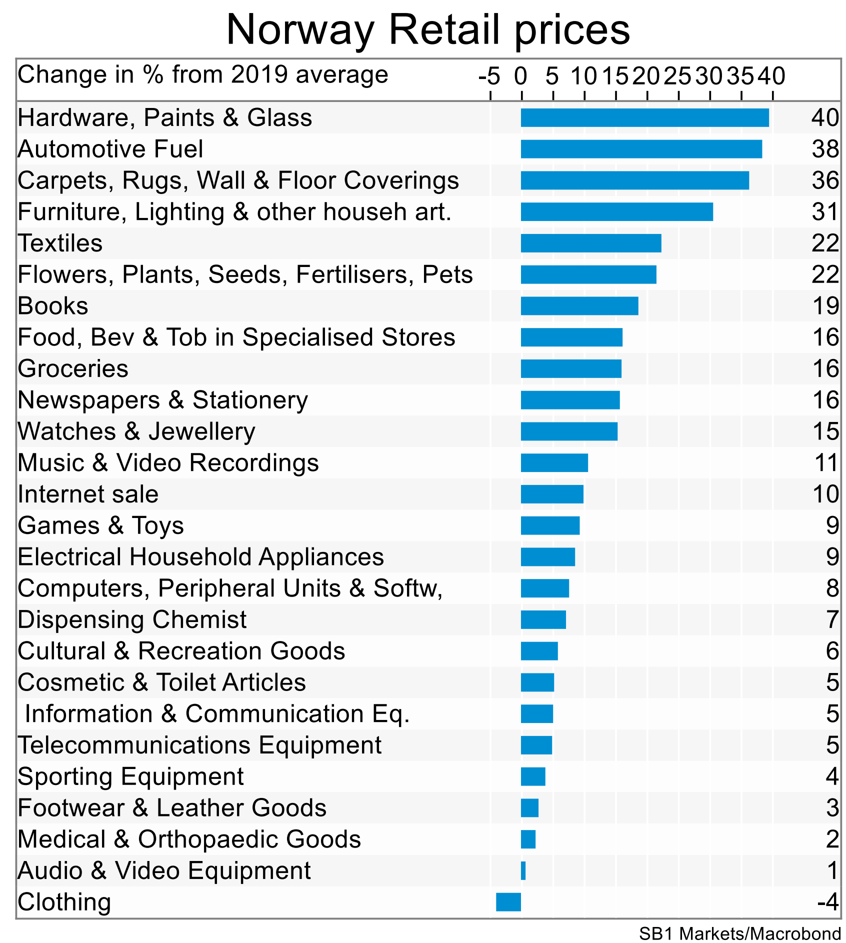
…and still some upside? Or will higher interest rates/high inflation keep sales at a lower level?



Retail sales value vs. volume – and what's between

Retail prices have been increasing at well above 4% pace since 2019, in sum by 16%!

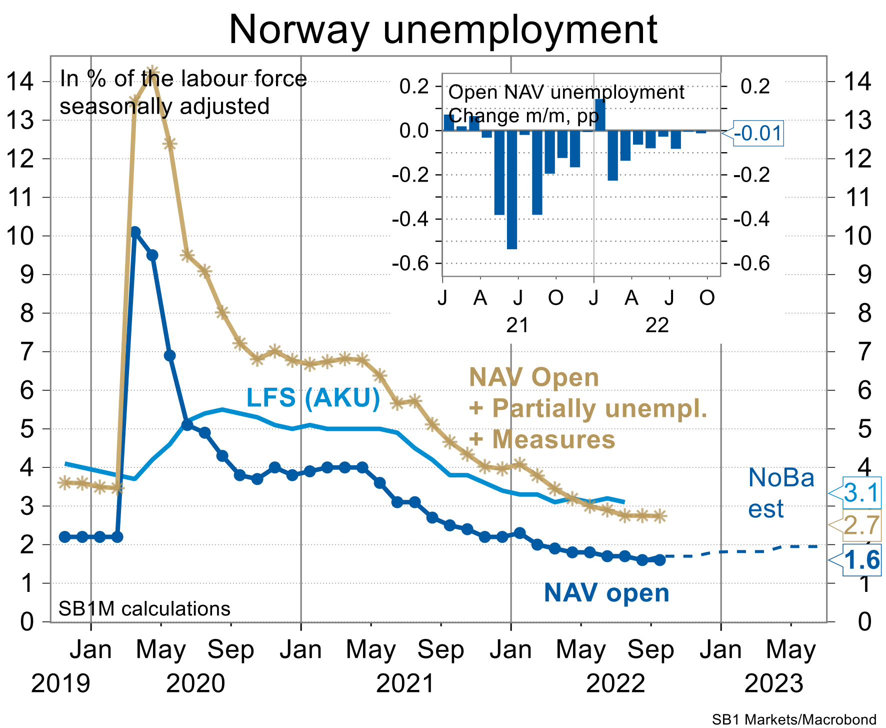


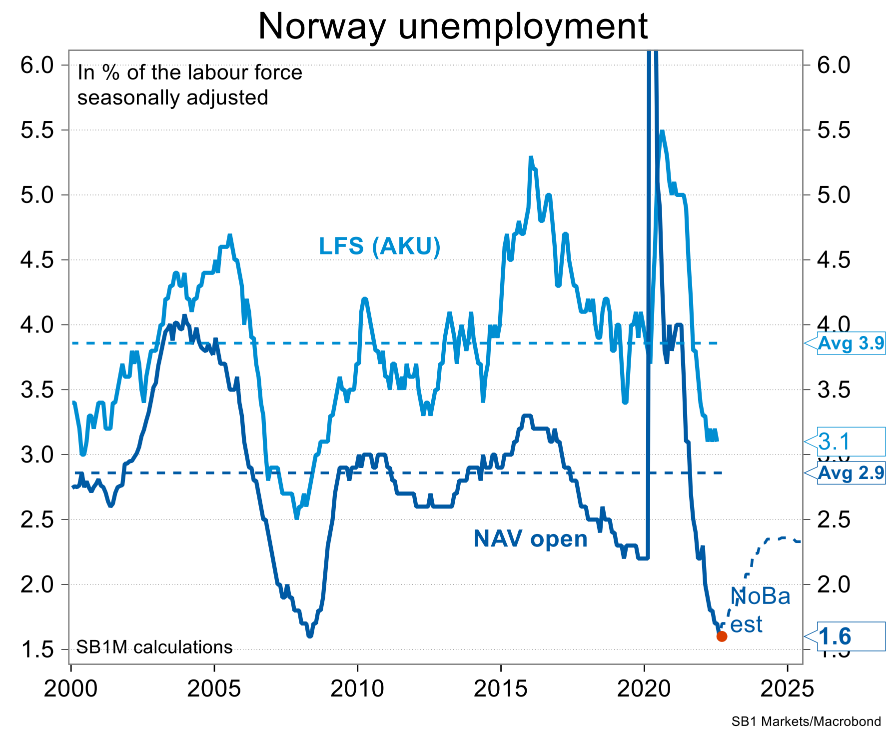


- Retail sales, measured in value terms, are 18% above the 2019 level and close to 10% above the pre-pandemic trend
- Huge differences is **price changes**:
  - » Gasoline up 38%, floor coverings, hardware (building materials) are up 38% – 40%, furniture 31%
  - » Close to the bottom of the list: Sport equipment prices are up just 4% and clothing is down 4%!

NAV unemployment marginally down in September – which will be the bottom?

Open unemployment unch. at 1.6%, as expected – but 0.1 below NoBas f'cast

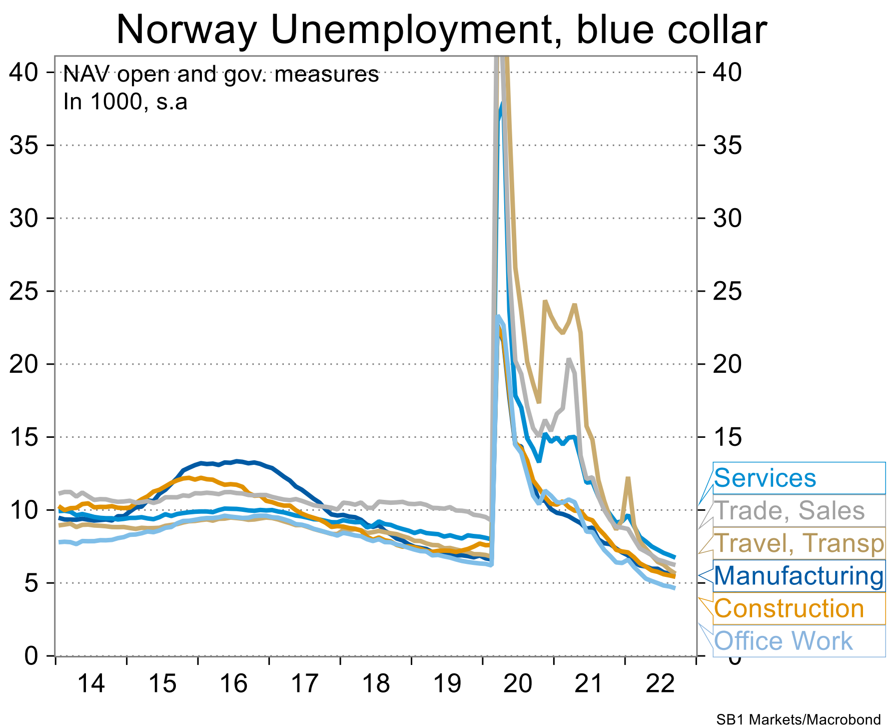


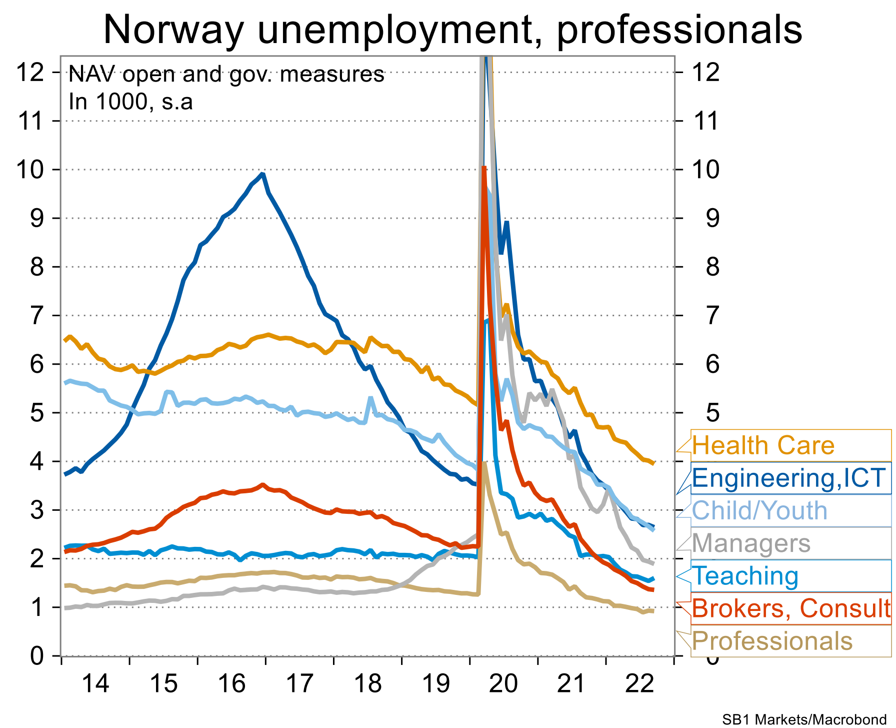


- **The 'full time' open NAV unemployment**, fell by some 300 persons in Sept (seas. adj) to 47.6'. The change was as we assumed, but Aug was marginally revised upwards. The rate at 1.6% (s.a) is equal to the lowest level before the financial crisis in 2008, and almost the lowest level since 1980, and +0.1 pp below NoBa's estimate in the MPR. Unadjusted the rate was unch. at 1.6% (1.57%), expected down to 1.5%
- Including labour market measures, unemployment fell by 700' persons, and the rate is at 2.0%
- The inflow of **new job seekers** have bottomed but is still at very low level. The **inflow of new vacancies** fell in September, and the trend is down, from the peak before the summer. Even so, the level remains very high. The decline is broad, except for the public sector.
- **The LFS (AKU) unemployment rate** declined 0.1 pp to 3.1% in July. **Employment growth** is slowing – or fallen to zero (LFS)

SpareBank 1 MARKETS

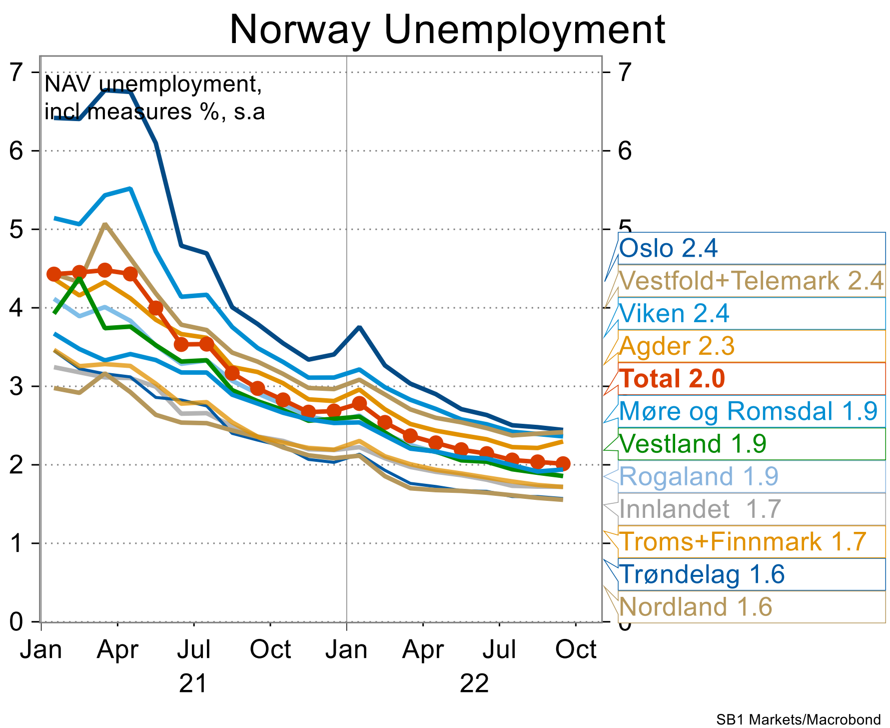
Unemployment is declining for all sorts of labour

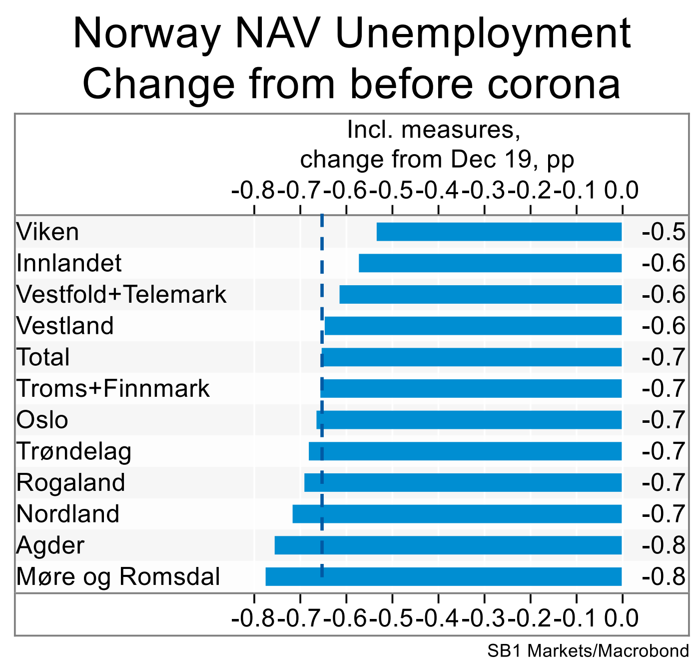




Unemployment is falling everywhere – and to well below pre-pandemic levels

Unempl. is declining at almost the same speed in all regions – and is well below avg. everywhere





- The unemployment rate rose marginally in September in Vestfold & Telemark, Agder, and Møre & Romsdal
- Nordland and Trøndelag at the bottom – Oslo at the top, as usual

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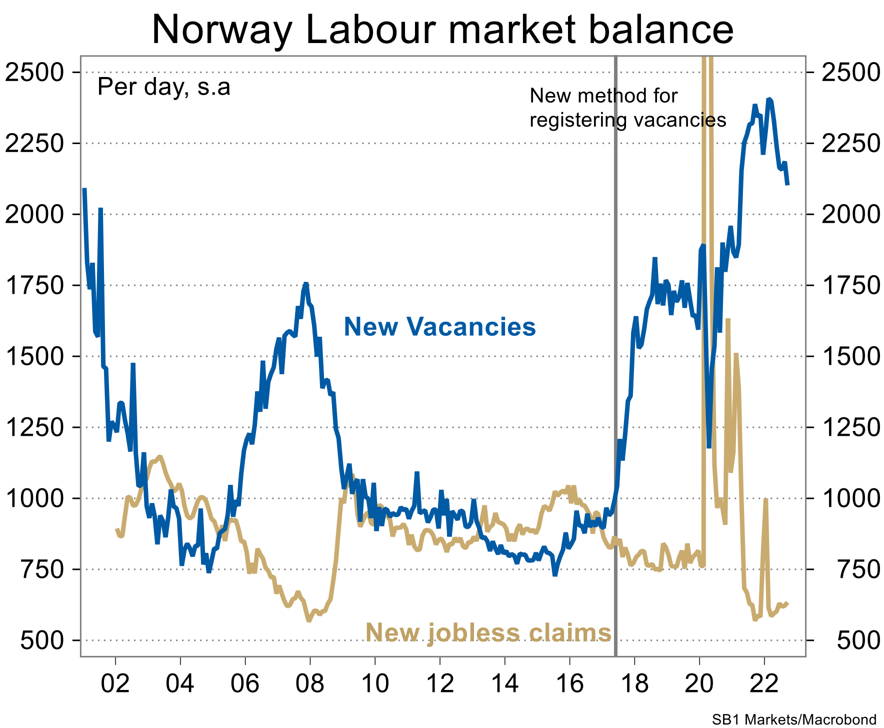
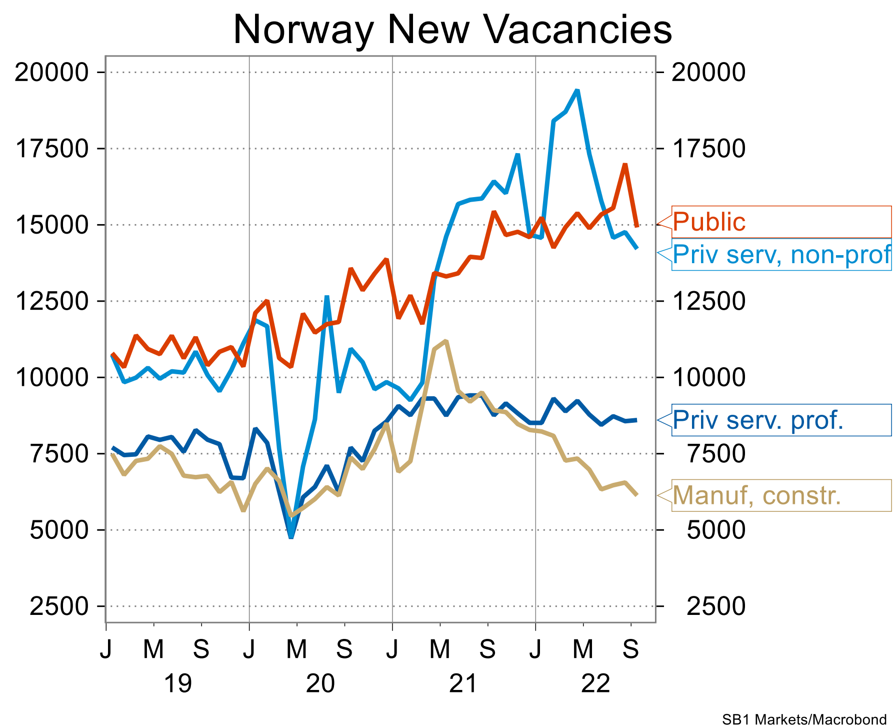
New job openings on the way down, but still at a high level

More vacancies in the private sector but demand form the private sector on the way down, broadly



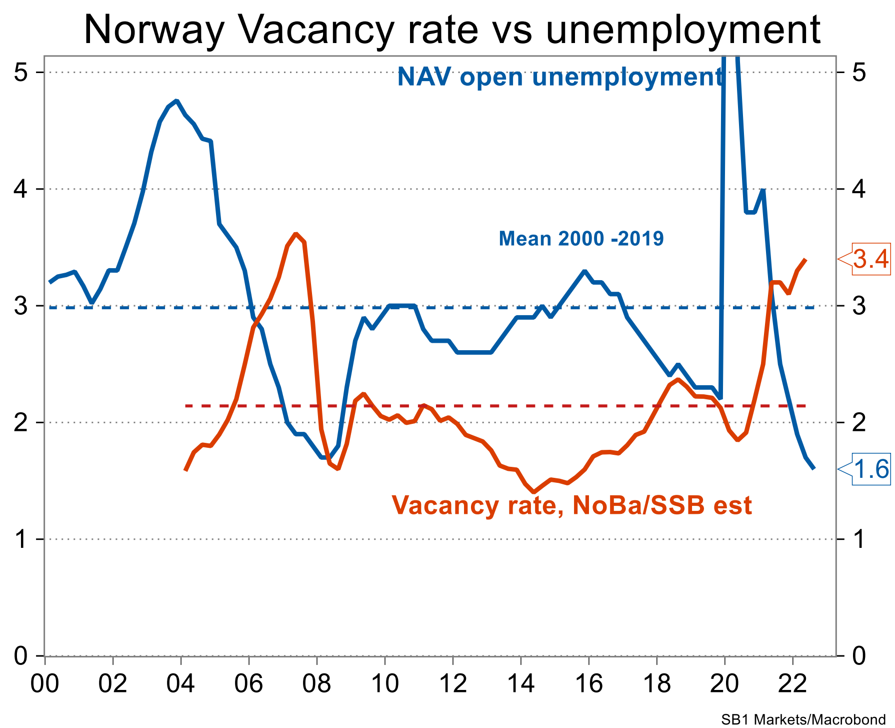


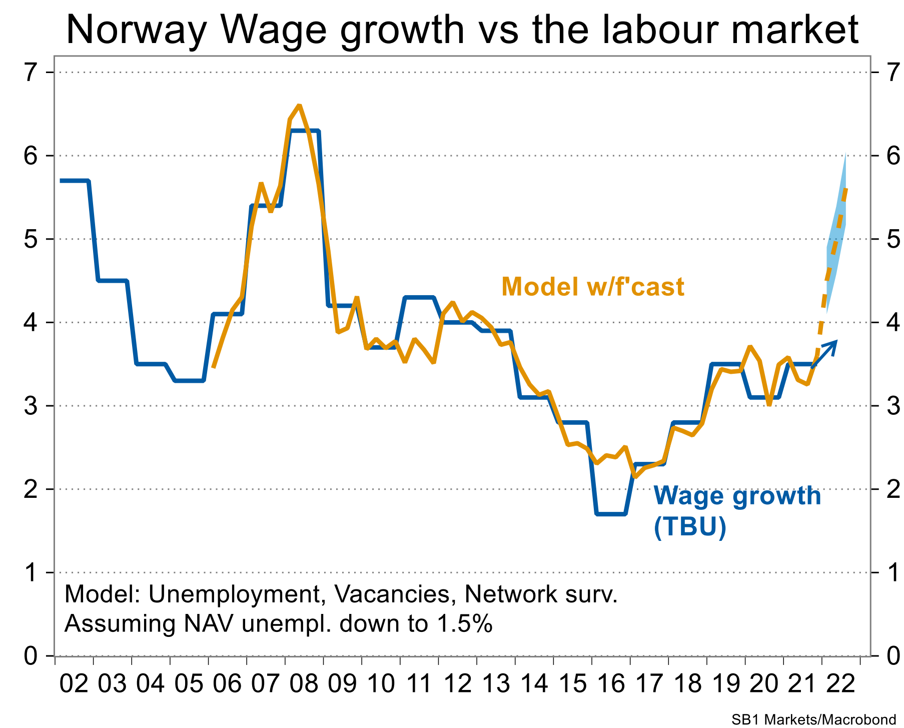
- The no. of new vacancies fell in September, and the trend is clearly down
- Most sectors have announced somewhat fewer new vacancies recently, most pronounced in the construction sector
- The no. of new jobless claims have probably bottomed at a very low level

SpareBank 1 MARKETS

Can wage inflation climb further? Our simple model suggests it would

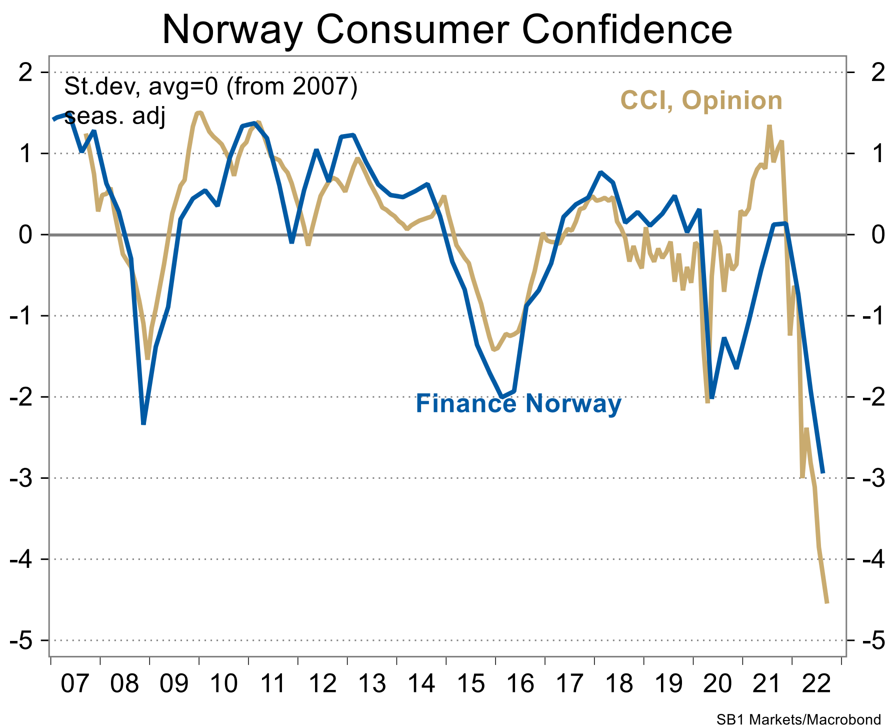
… if nothing is done in order to weaken the labour market. But somebody is doing something now





Consumer confidence down to ATL in ~~May~~ ~~July~~ ~~August~~ September…

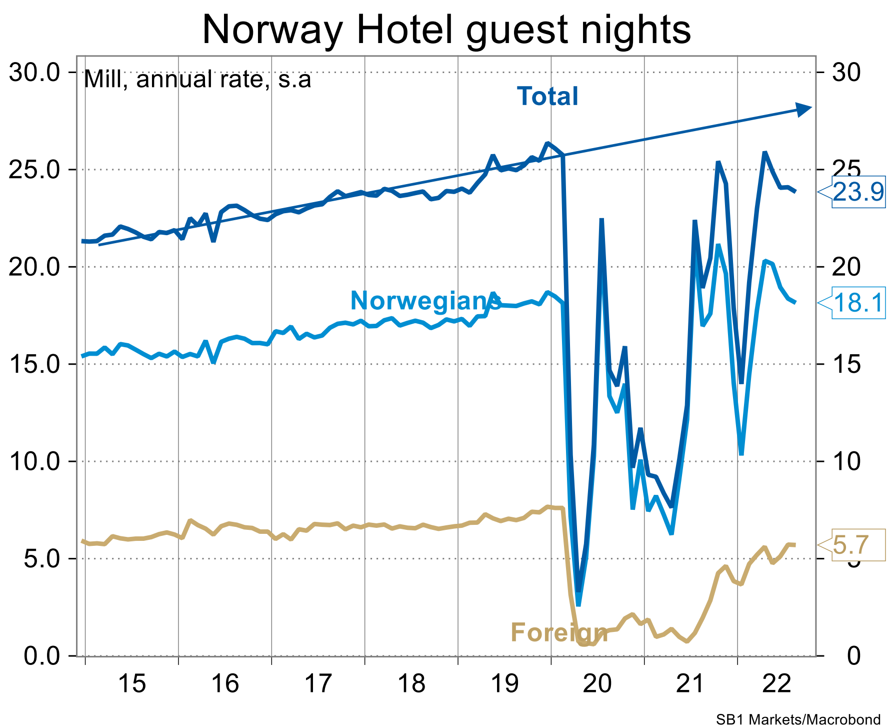
… and more than 'twice as weak" as when the corona first attacked

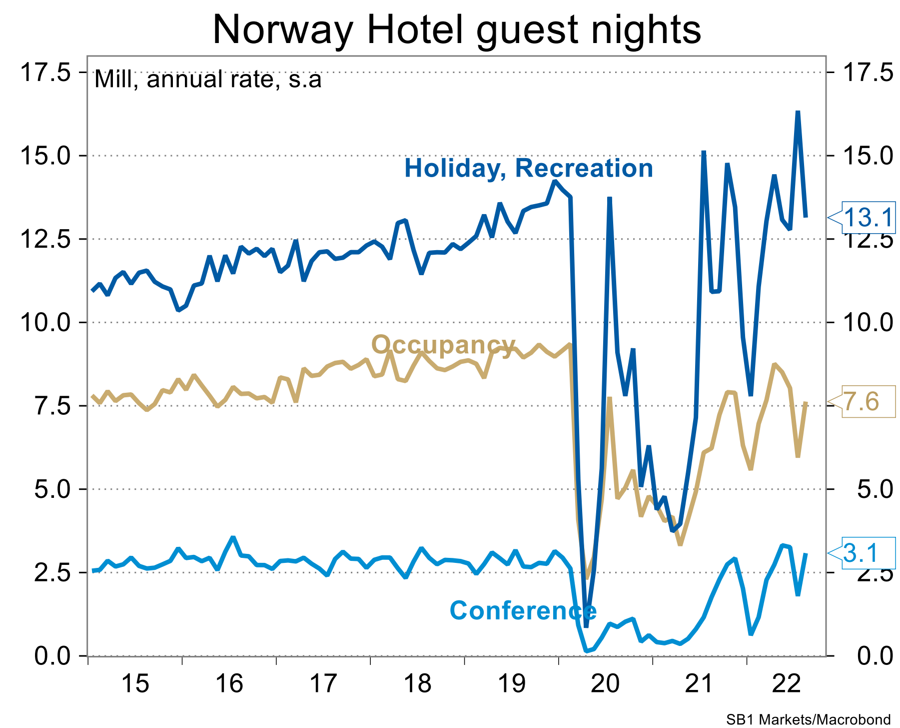


- **The CCI print** from Opinion in September was the lowest ever recorded – high inflation and higher interest rates are no doubt biting
- The index recovered somewhat in April, but fell again in May - Aug, and is now 4.4 st.dev below average. The bottom during the pandemic was 2.0 st. dev. below average
- **Will households stop spending or retreating from the housing market?** So far, the housing market has held up well, while retail sales volumes have been falling sharply but from a level way above trend
- The **net share of optimists** is almost -30%. Given inflation and the hikes in interest rates + some geopolitical uncertainty, this share could easily have been larger
- On the other hand, even if a large share of the population recognises that their own economy will be hurt, it does not imply that they all plan to cut spending sharply. Even so, the decline in confidence is of course worrisome

A marginal decrease in hotel guest nights in Aug, less recreational traffic

Conferences and other business related guest nights up. Foreign guest nights are still down 25% vs pp

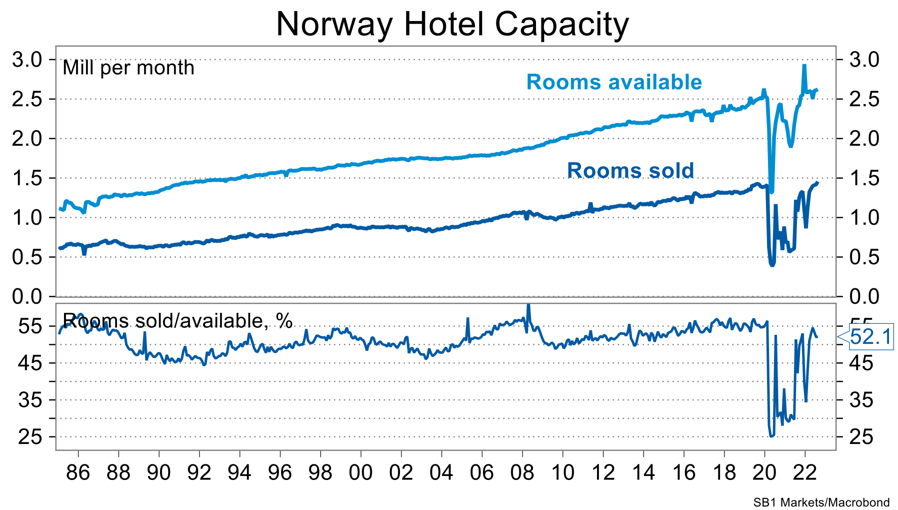


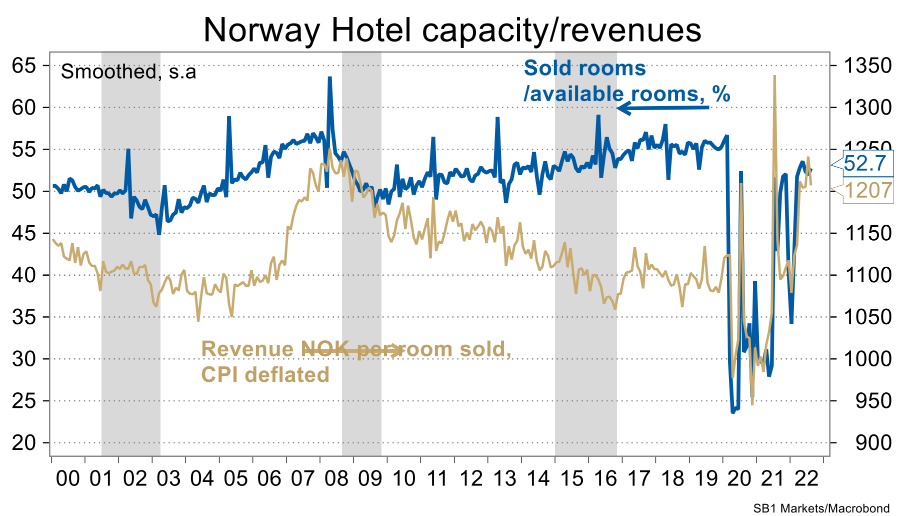


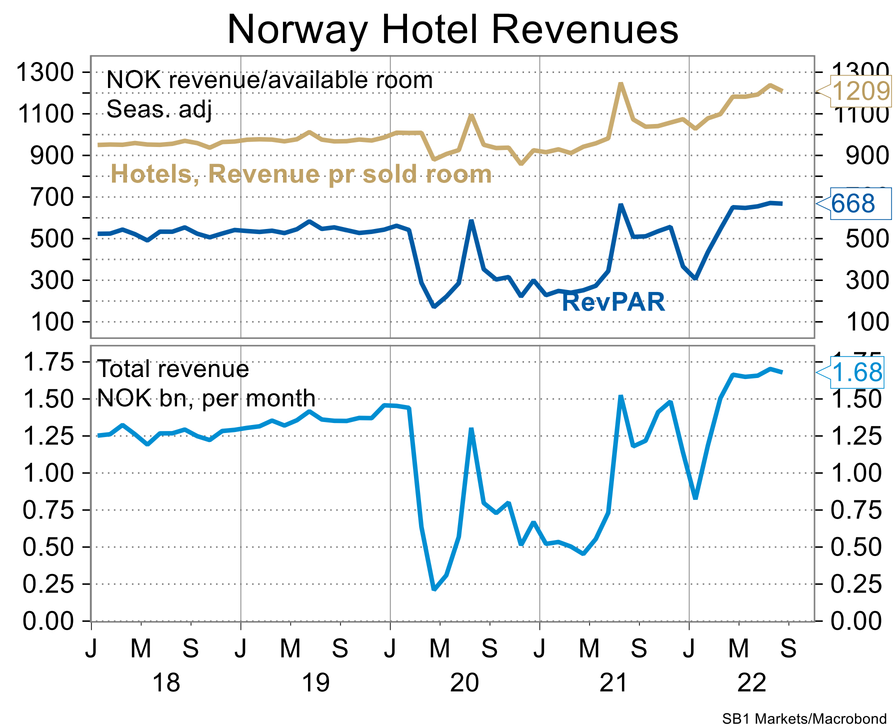
- Recreational demand is back to a normal level, even if the total number of foreigners are still down 25% vs the pre-pandemic level
- The conference market is back the pre-pandemic level – it took just some few weeks after restrictions were lifted
- Other business guest nights are some 10% –15 % below the pre-pandemic level (monthly date are volatile, even after seas. adj.)
- The no. of guest nights is still below the pre-pandemic trend growth path, by some 10% and just due to fewer foreigners

Capacity utilisation still not back to normal but prices are up 20% since Feb-20…

… RevPAR is higher than ever before too, as are total revenues







- **Capacity utilisation** (room sold vs. rooms available) was 52.7% in July, somewhat below the normal level ahead of the pandemic
- **Revenue per sold room** is up 20% from the Feb-20 level, a substantial increase (aka inflation)
- **RevPAR** (revenue per available room) is also far above the pre-pandemic level, 16%

SpareBank 1 MARKETS

Highlights

The world around us

The Norwegian economy

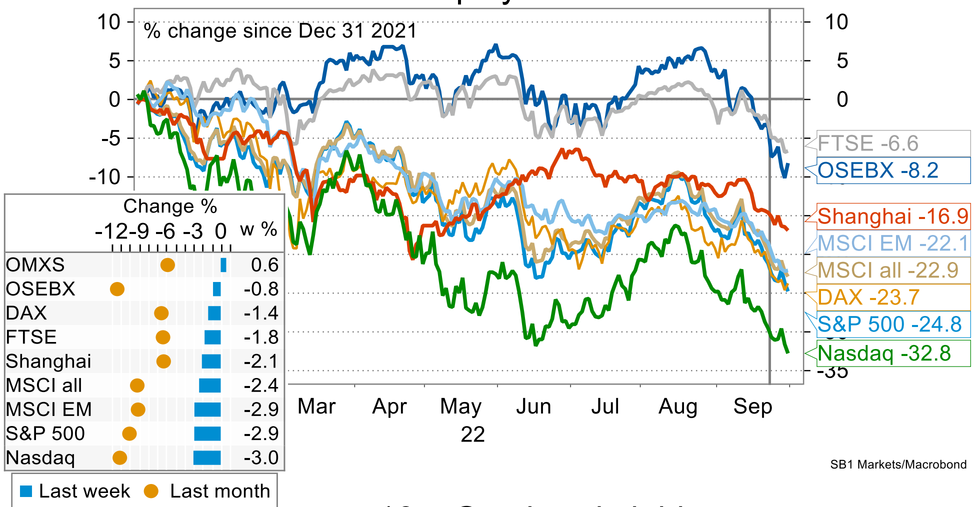
Market charts & comments

SpareBank 1 MARKETS

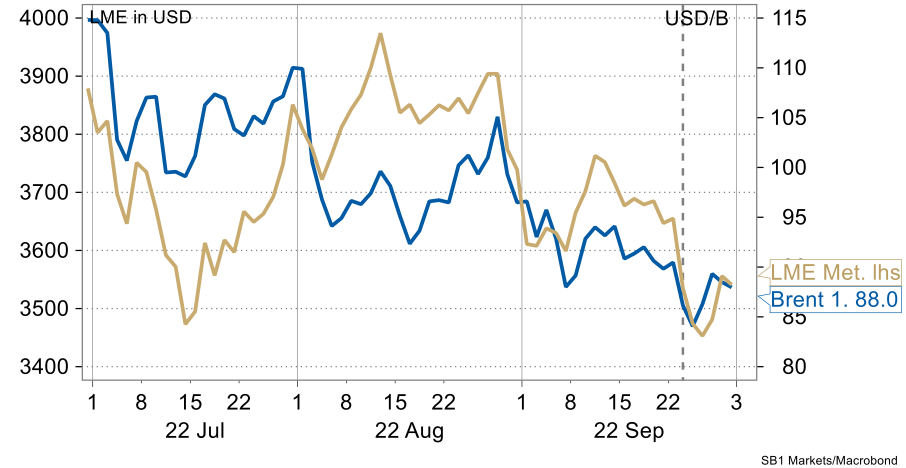
Risk off, volatile bond yields mostly up. BoE will buy bonds again

Metal prices up on discussions about further sanctions on Russian exports – but the trend is down, as for oil

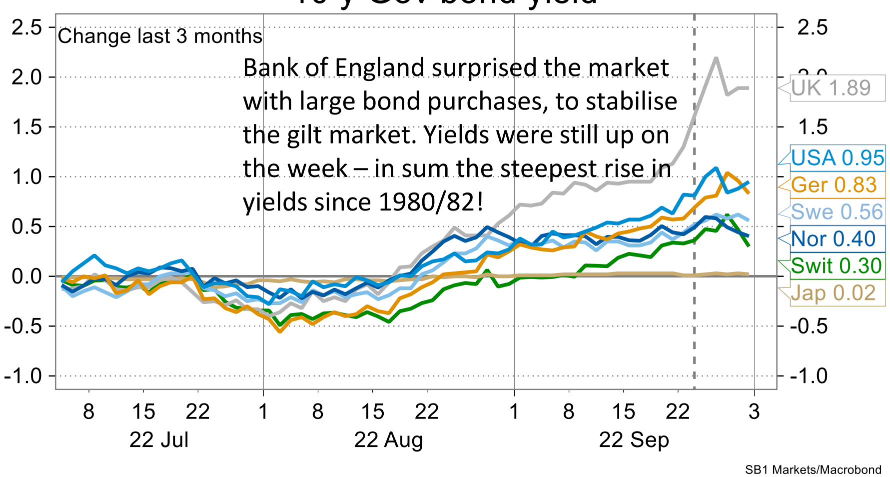
Equity Indices



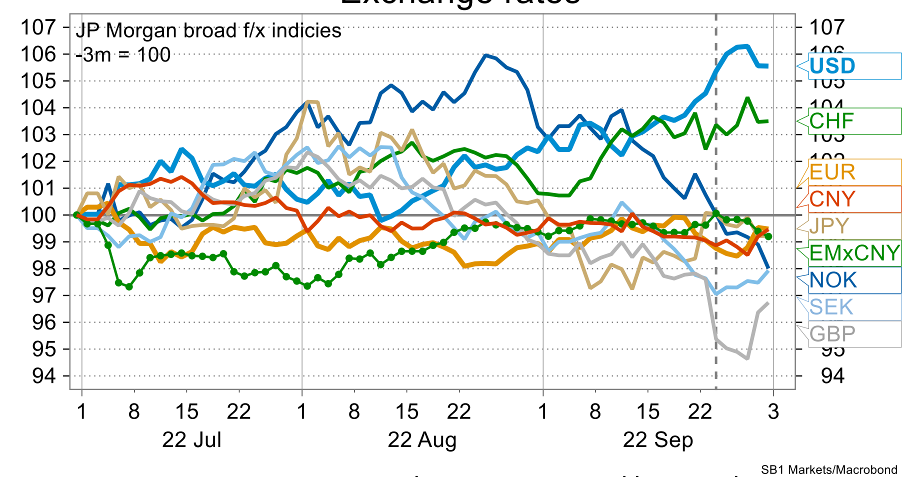
Oil vs. metals



10 y Gov bond yield



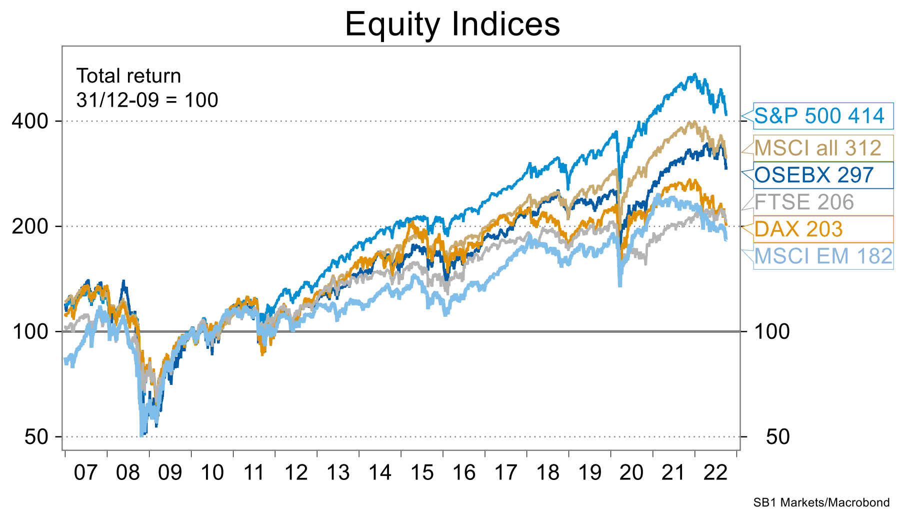
Exchange rates

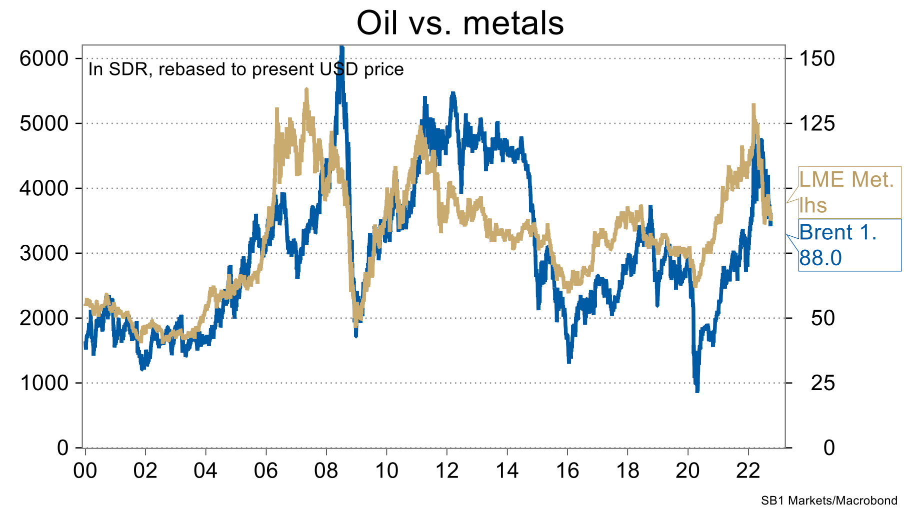


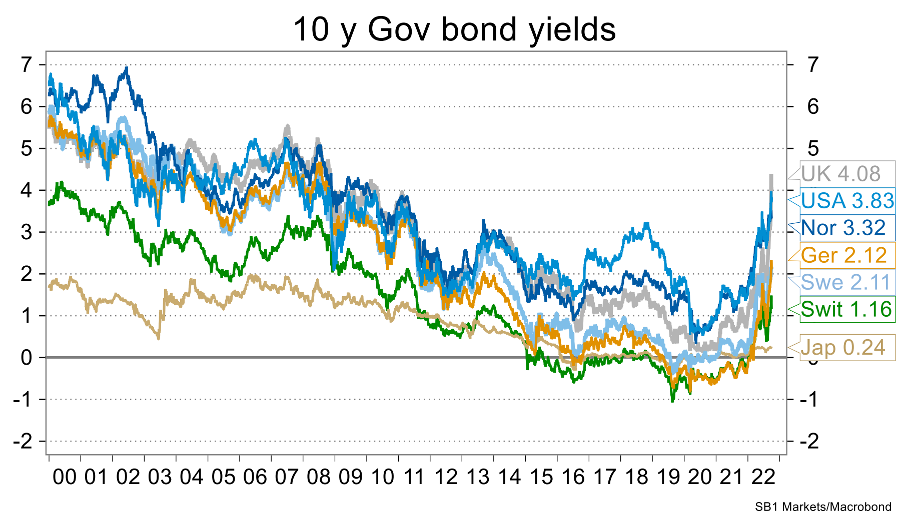
The GBP recovered last week

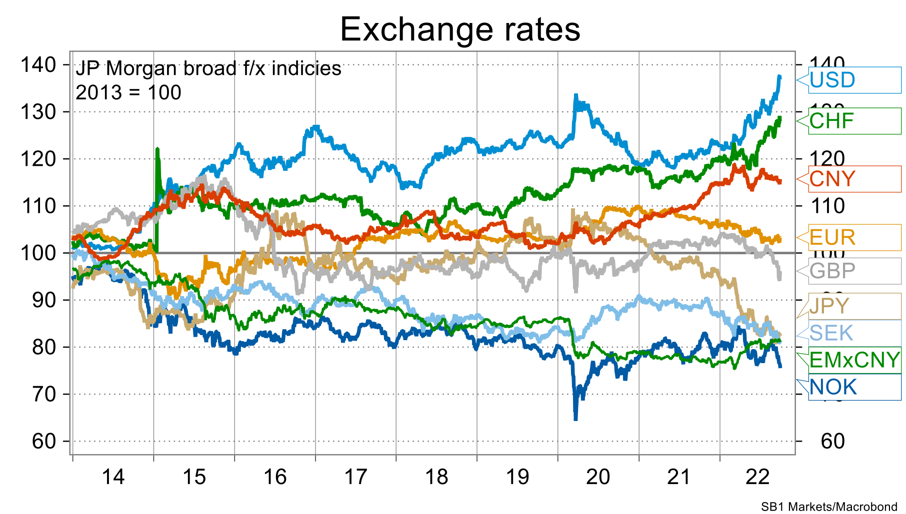
The big picture: Stock markets down, commodities down, bond yields up

The USD is very strong, most other DMs are slipping, NOK including



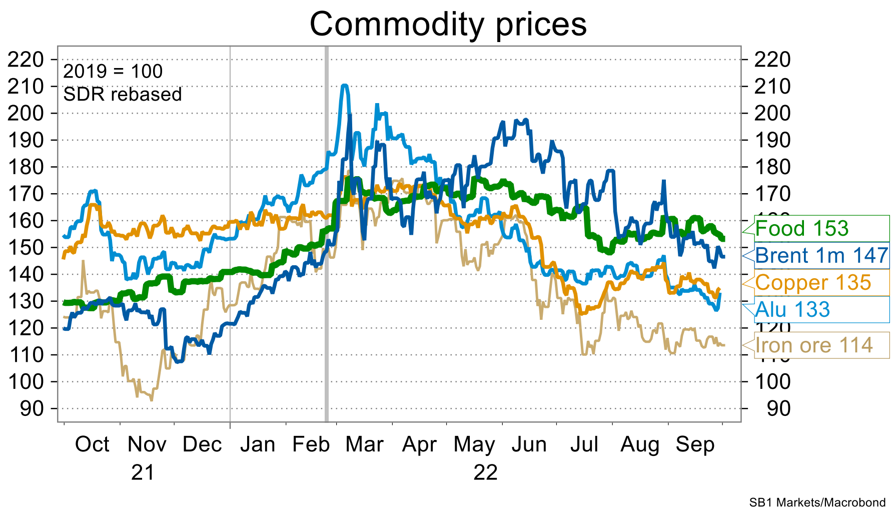


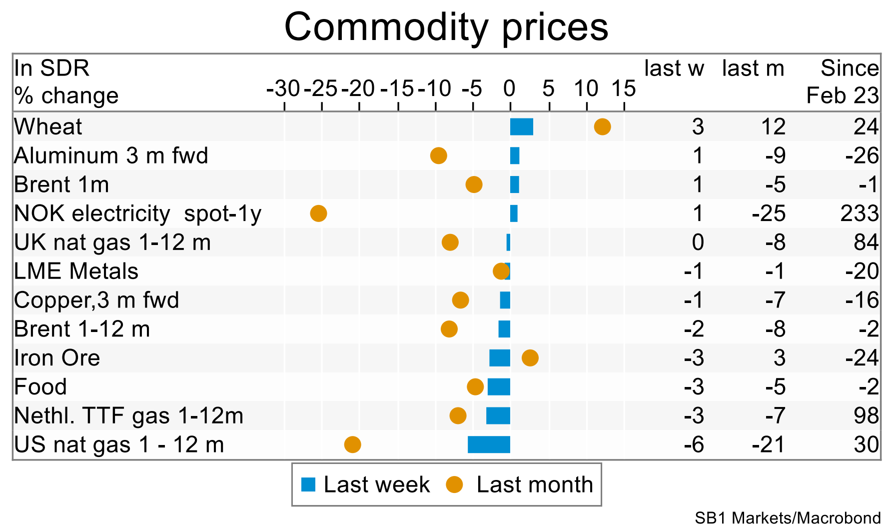




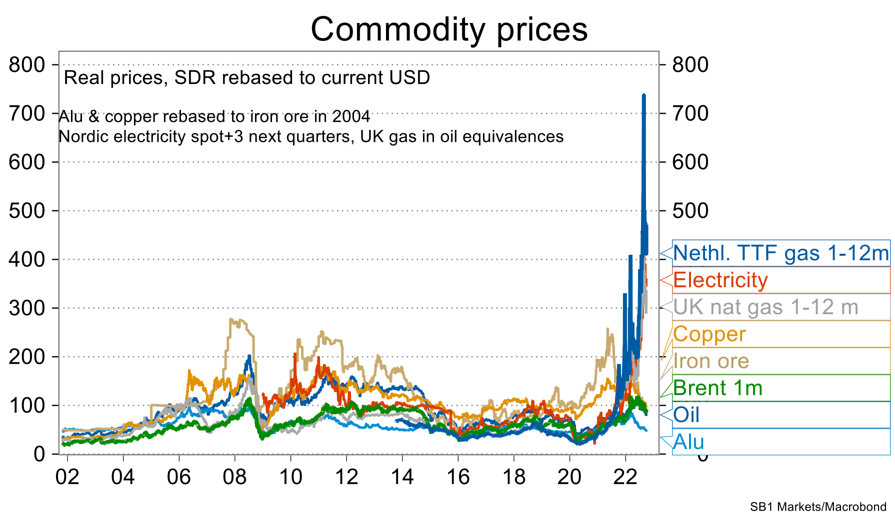
SpareBank 1 MARKETS

All commodities but wheat were down last month. Most down last week too





In SDR % change	last w	last m	Since Feb 23
Wheat	3	12	24
Aluminum 3 m fwd	1	-9	-26
Brent 1m	1	-5	-1
NOK electricity spot-1y	1	-25	233
UK nat gas 1-12 m	0	-8	84
LME Metals	-1	-1	-20
Copper,3 m fwd	-1	-7	-16
Brent 1-12 m	-2	-8	-2
Iron Ore	-3	3	-24
Food	-3	-5	-2
Nethl. TTF gas 1-12m	-3	-7	98
US nat gas 1 - 12 m	-6	-21	30



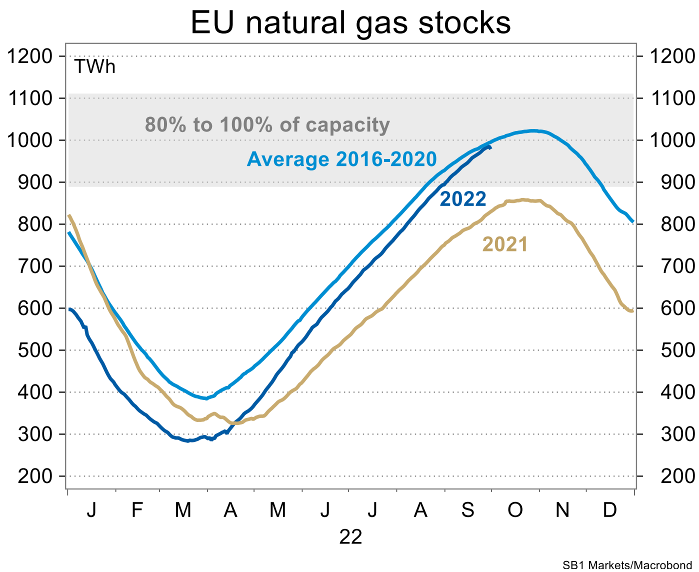
Last week

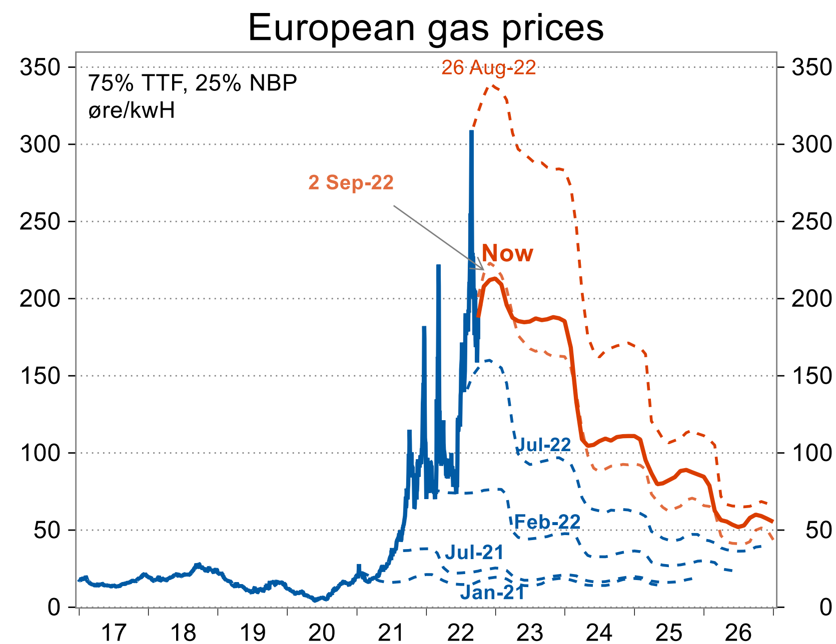
- **European natural gas** has more or less flattened following the steep decline late August/early September. The sabotage of Nord Stream 1 and 2 did not shock the market that much, the Dutch gas price fell last week
- **Oil prices** close to unchanged on the week, but are trending down
- The Economist's **food commodity inched down 3% last week** (in SDRs), and are down 5% last month
- Most **metal prices** were mixed. Some were supported by discussions on more sanction on Russian exports, including metals

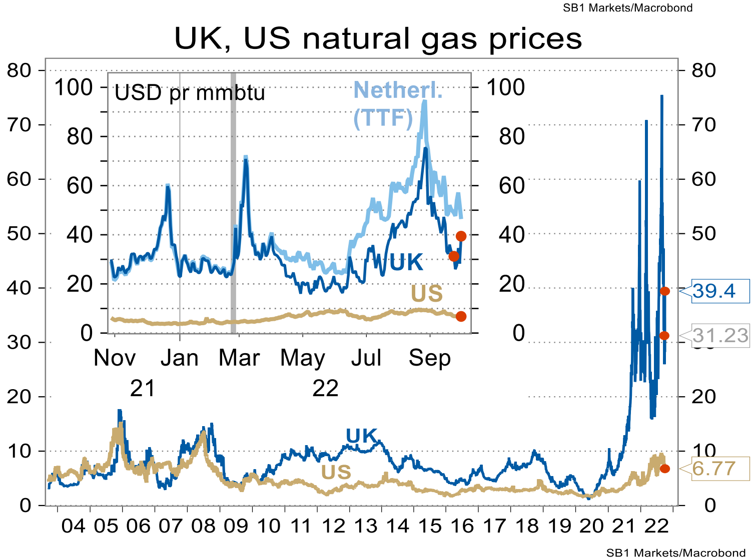
SDR: IMF's Special Drawing Rights – a 'global currency'

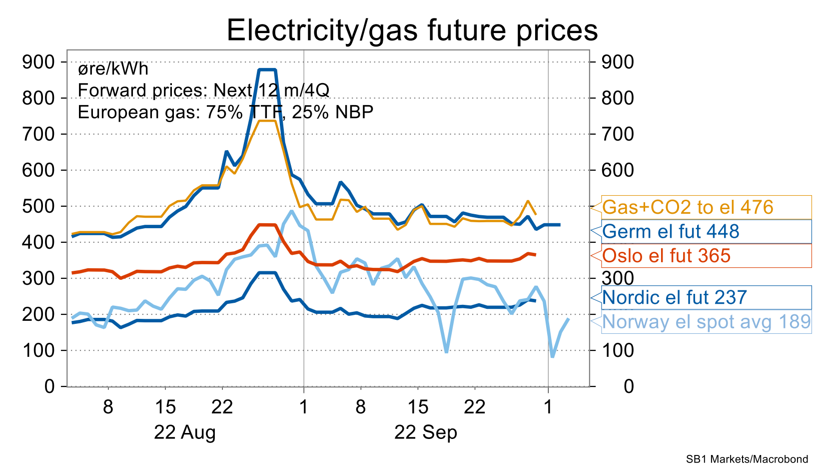
European gas/electricity prices have stabilised, as gas stock are well filled

The sabotage against the two Nord Stream pipe lines did not shock the market



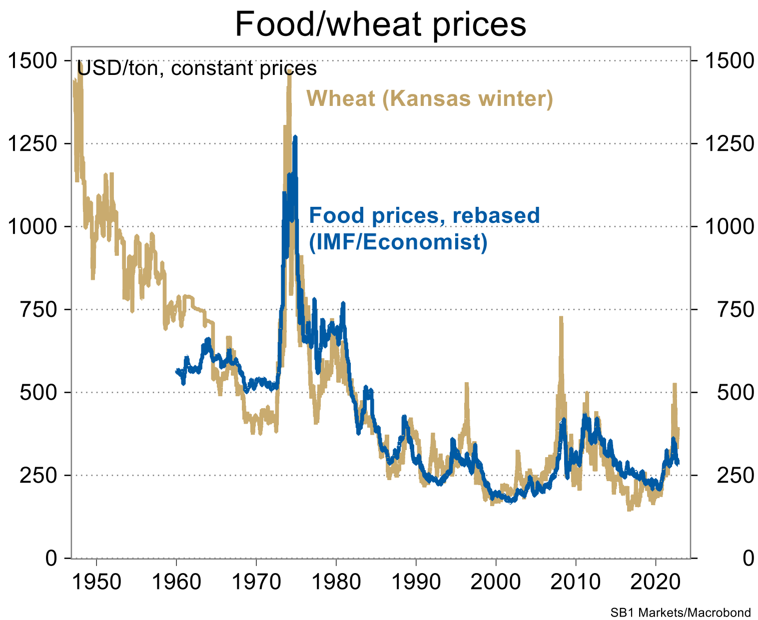


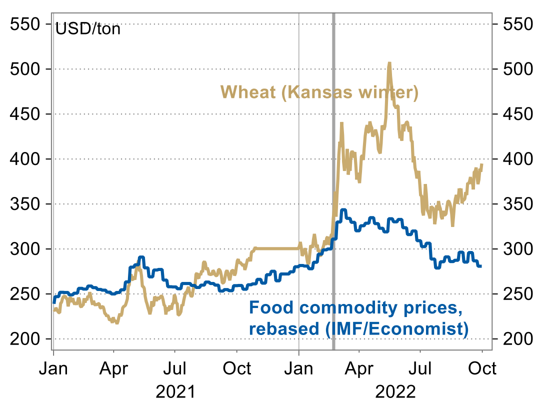


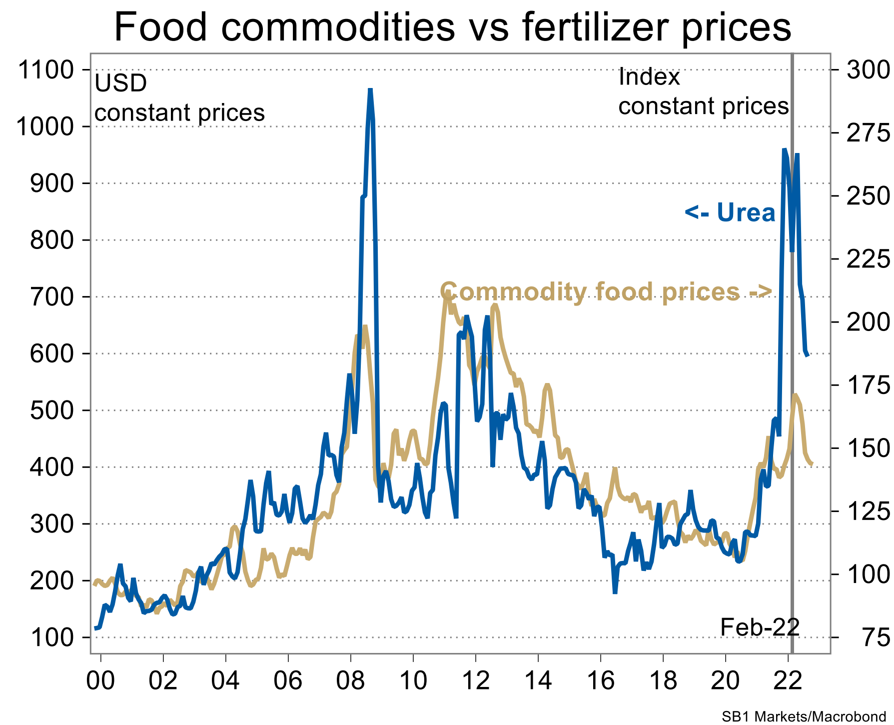


Food prices down last week & are trending down in spite of higher wheat prices

The real price level is not that high, *and close to the 10 y average. A global food crisis??*

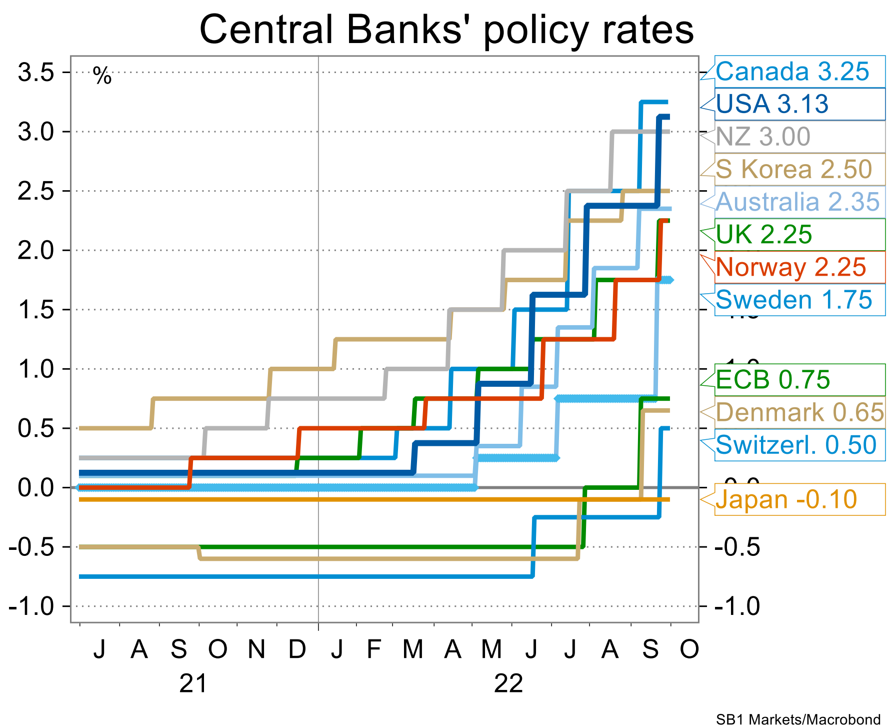


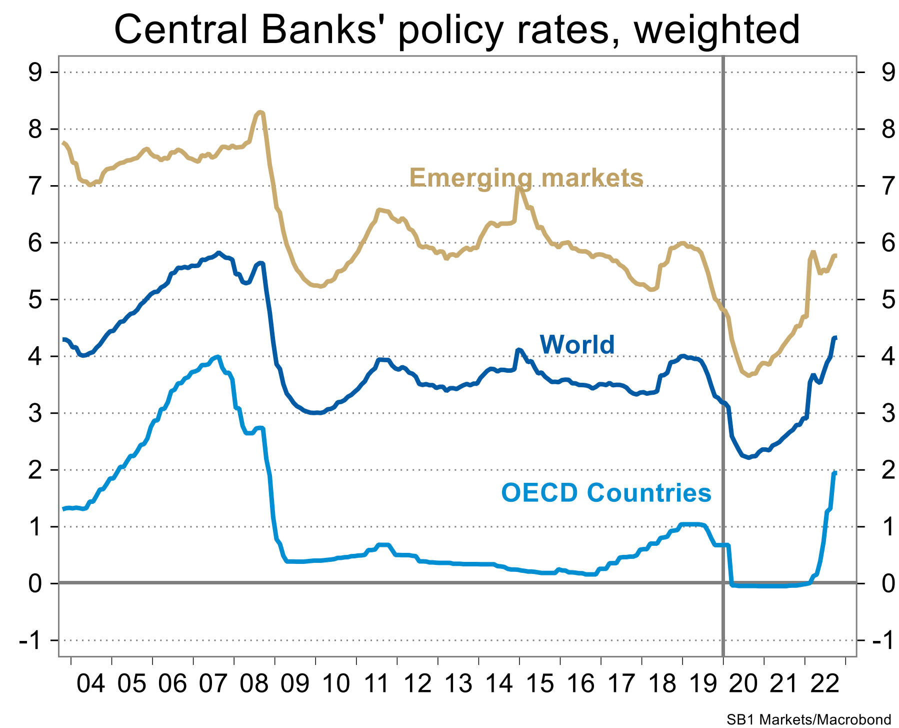




Urea prices are falling rapidly too (but are not low vs. food prices)

Signal rates were kept in check last week (But not all other rates)



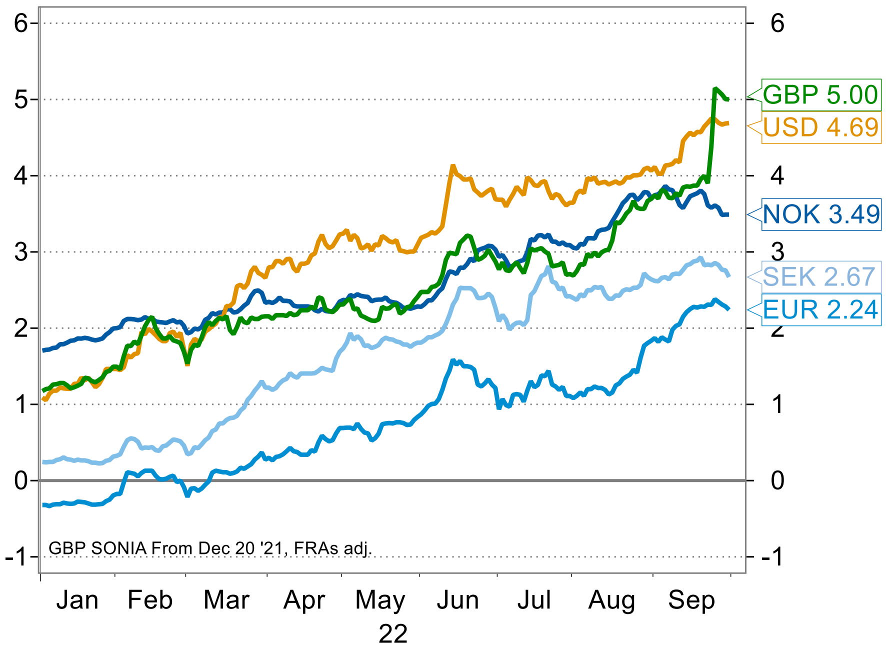


- Central banks are hiking rates even if they expect growth to slow (US) or the economy to contract (Sweden, UK, Norway) because inflation is way above target (including all measures of underlying inflation, partly also costs) and is expected to remain above target for several years
- The EM average policy rate has come down due to the Russian cuts – but the average is on the way up again
- In addition to rate hikes, most central banks have ended their QE buying programs. Some banks will start reducing their holdings, moving into the QT zone. US ramped up its QT program (doubled the pace) from the beginning of September

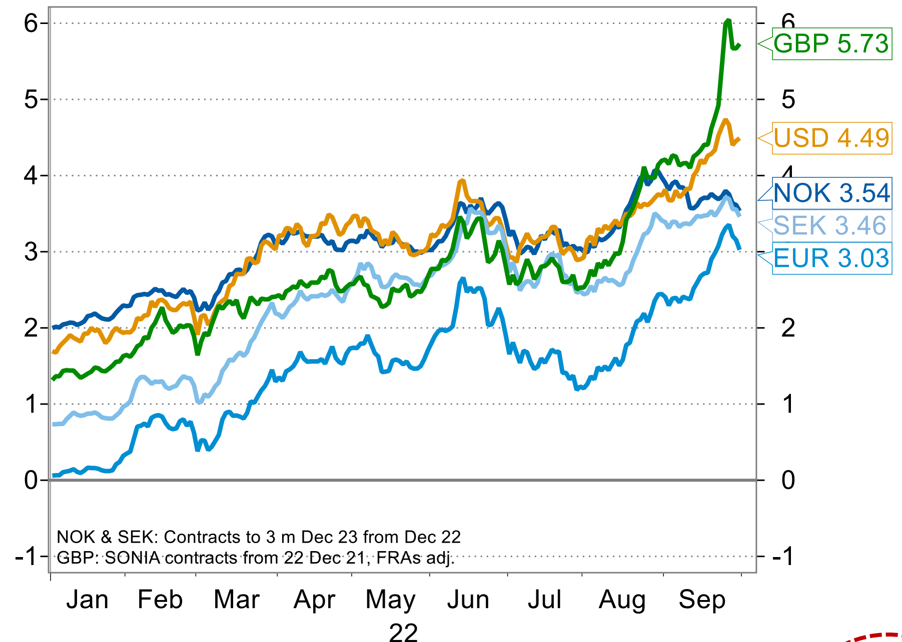
GBP FRAs rose further last week – but fell after BoE's bond market intervention

UK rate expectations are too aggressive, the UK economy will be 'killed' by such rates. NOK FRAs down

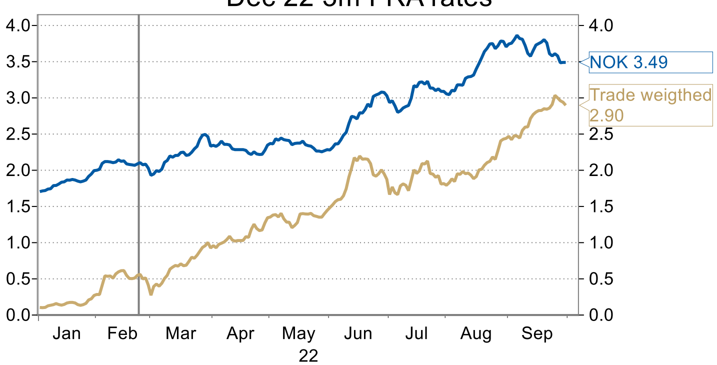
Dec 22 3m FRA IBOR rates



Dec 23 3m FRA IBOR rates



Dec 22 3m FRA rates



Dec 23 3m FRA rates

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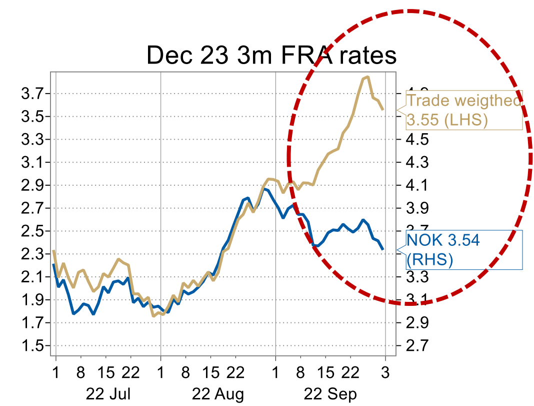
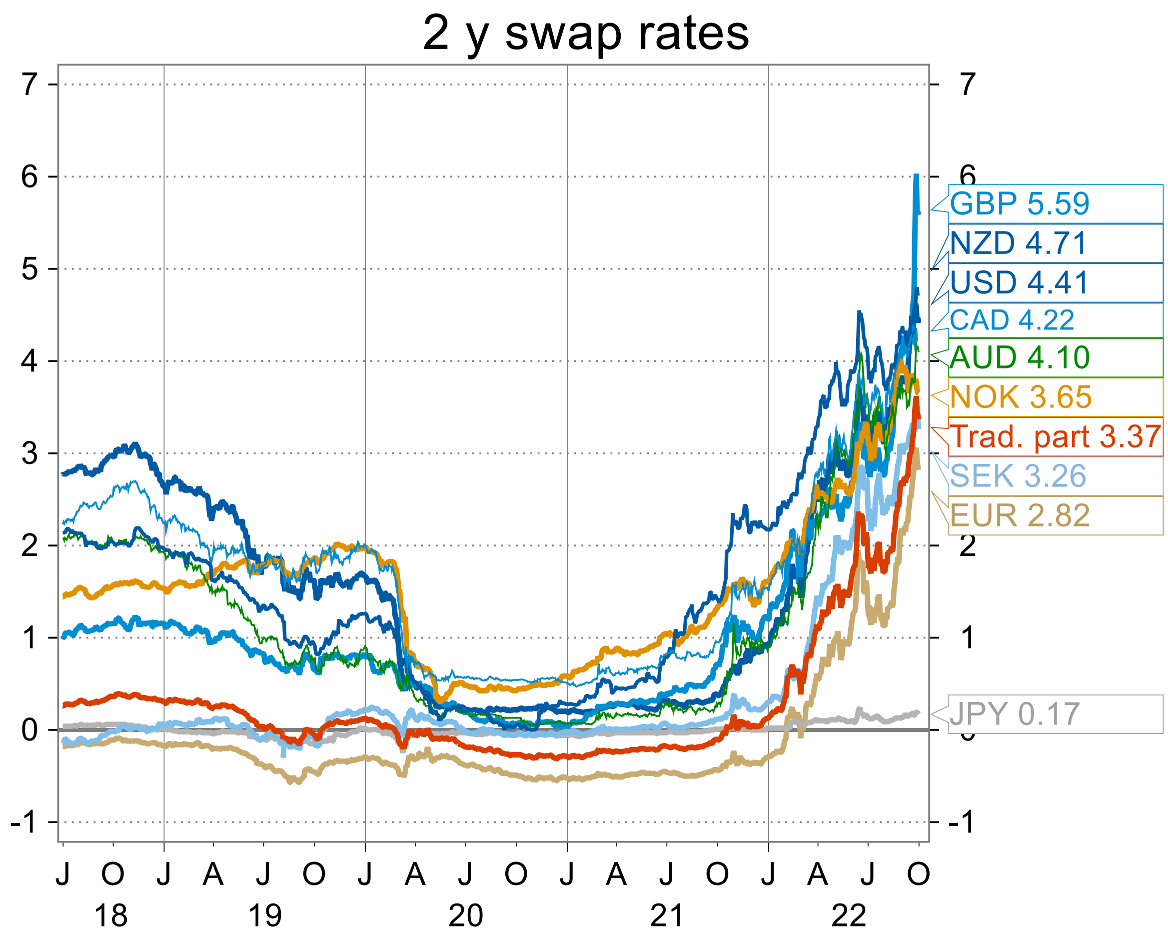
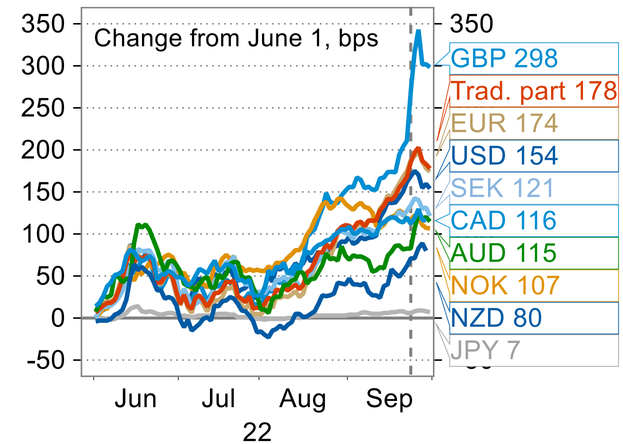
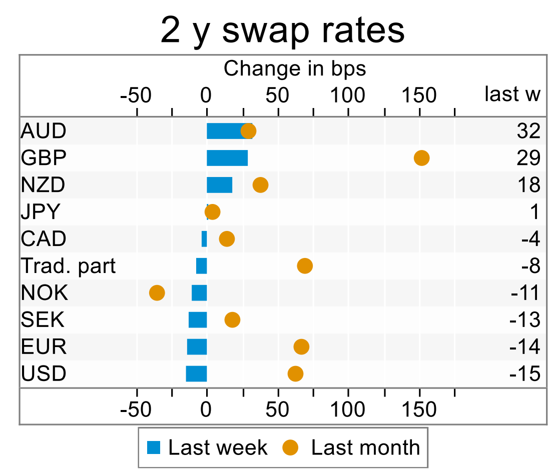


Most 2 y swap rates down but GBP rates rose further

NOK rates have fallen past 4 weeks, foreign rates have climbed. AN UNPRECEDENTED SPREAD DECL!

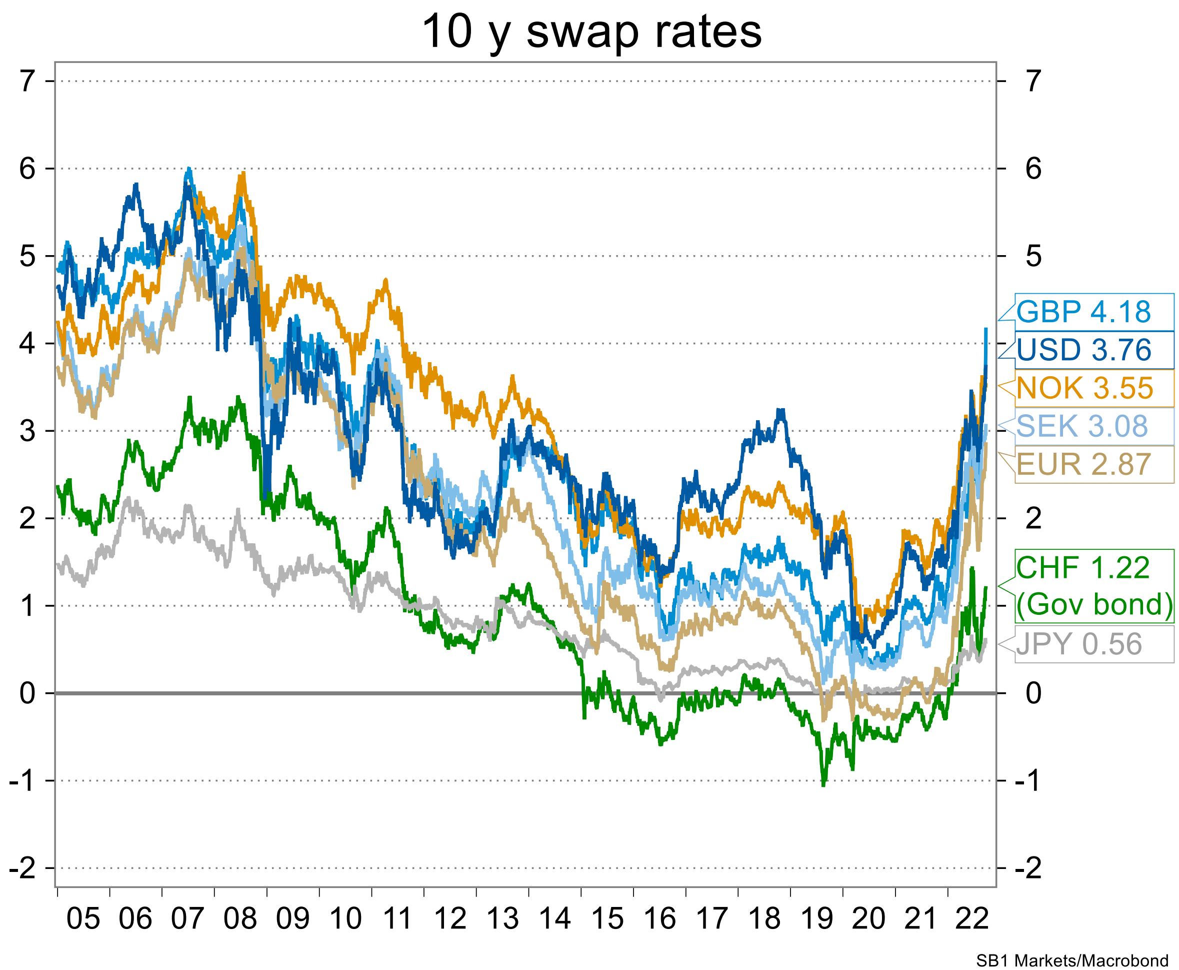


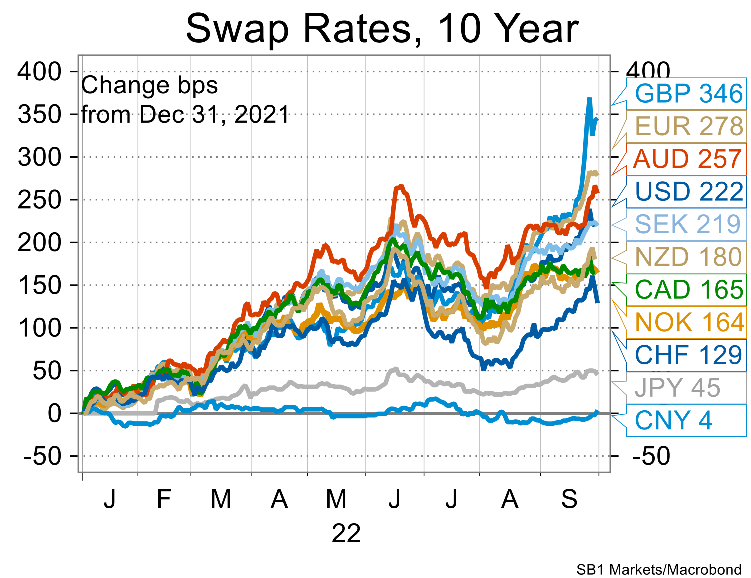


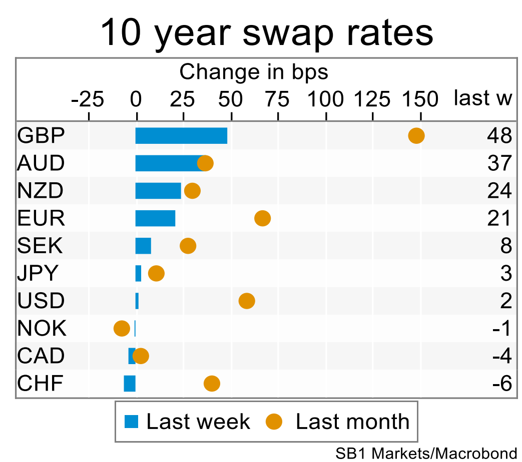


The long end of the curve further up in UK, even if the BoE are buying bonds again

EUR rates up too, while USD, NOK rates decreased





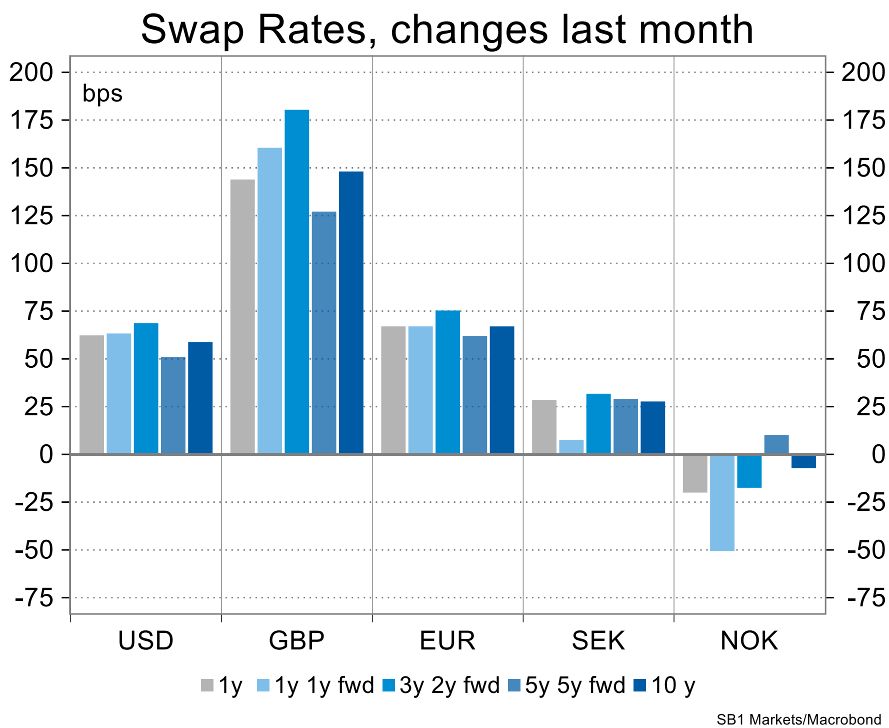


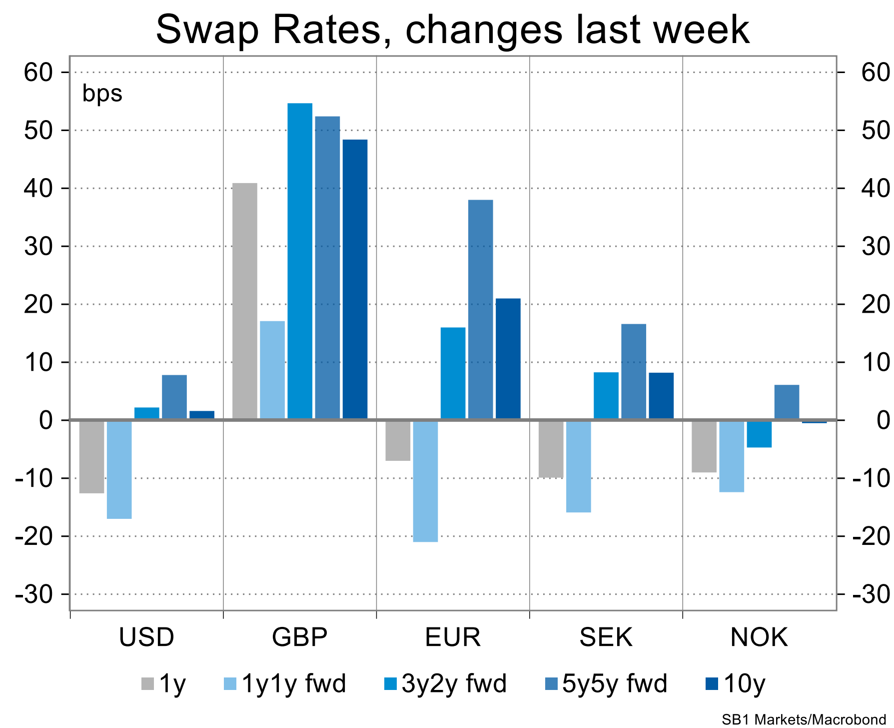
CHF: 10 y government bond yield

SpareBank 1 MARKETS

Look to England (if you want to create trouble for yourself)

Keep Calm and Carry On: NOK rates are unusually insulated from the surge in rates abroad



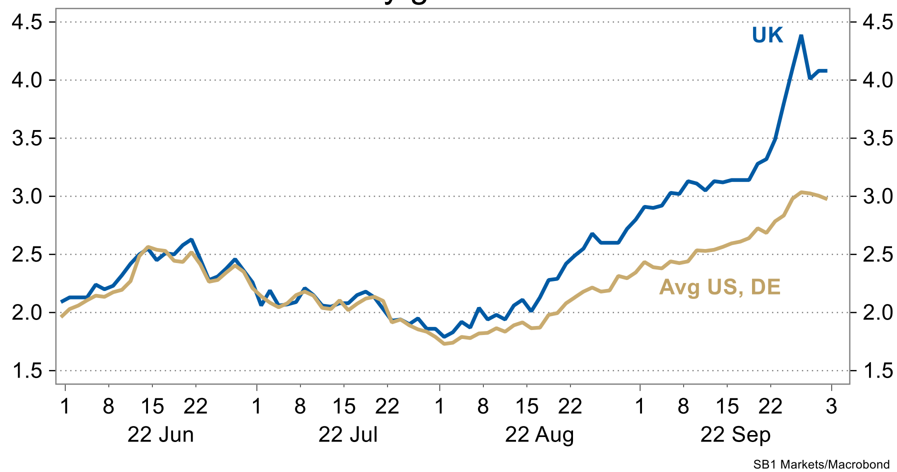


- The UK interest rate shock is unprecedented, at least since 1980 and 1982 measured by the change in bond yield, and the largest ever if measured by the bond price. Volatility was extreme last week both before and after Bank of England's draconic decision to start buying bonds, at least for some weeks – and signalled that it could buy whatever needed to prevent yields from rising too much
- The short end calmed down everywhere else

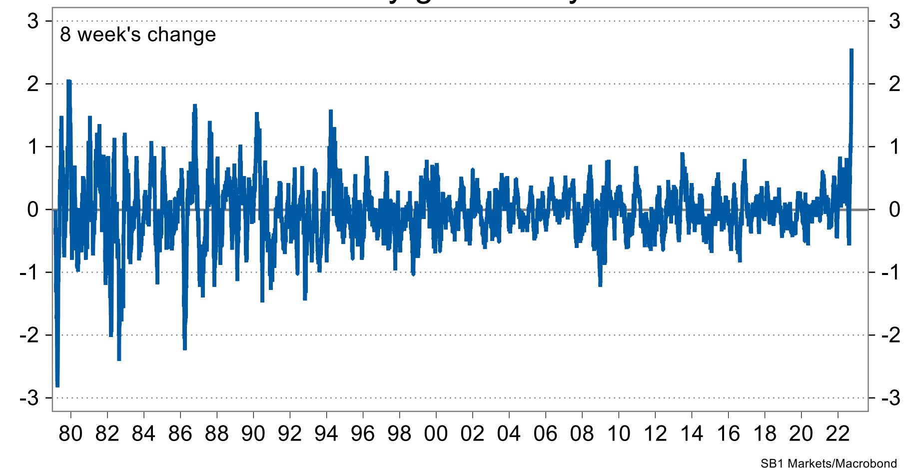
Some though weeks for the UK! BoE had to save the gilt market!

The Bank of England had to intervene on Wednesday, and fired a bazooka: Will keep yields in check

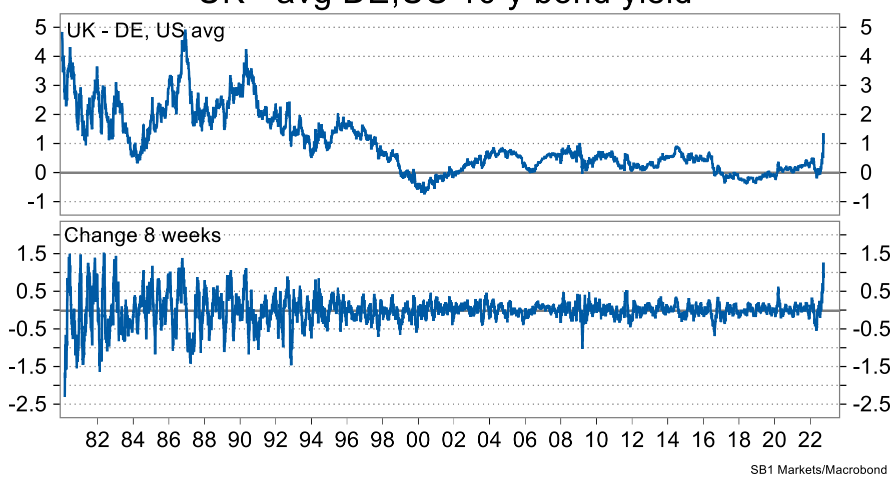
10 y gov bonds



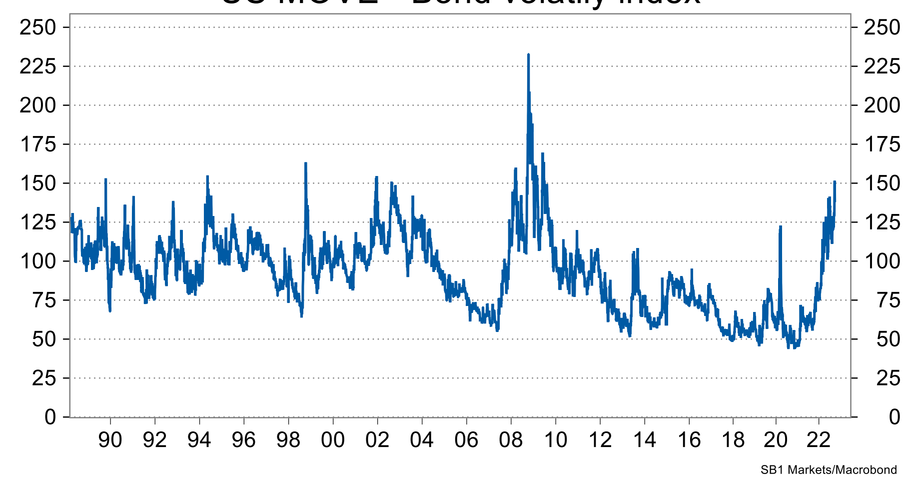
UK 10 y gov bond yield



UK - avg DE,US 10 y bond yield

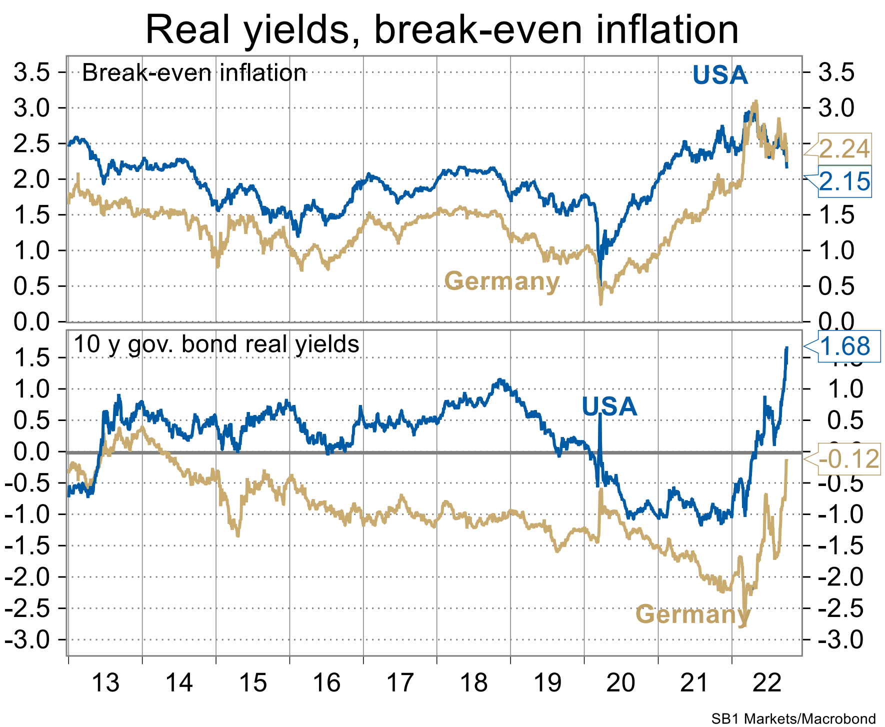


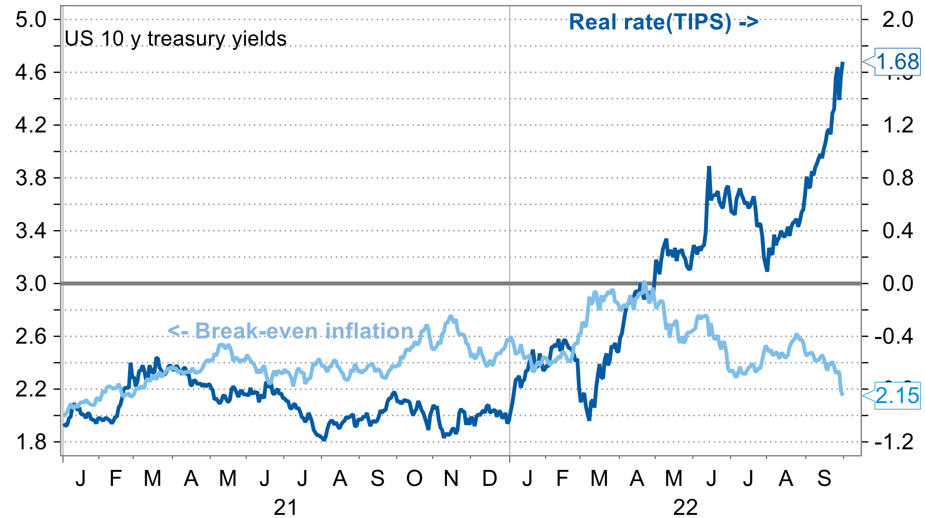
US MOVE - Bond volatily index



Real rates are shooting up, inflation expectations are falling rapidly!

10 y real rates up 36 bps (US) to 48 bps (German), as inflation expectations are down 22 – 34 bpd!





US & Germany 10 y Gov bond yield

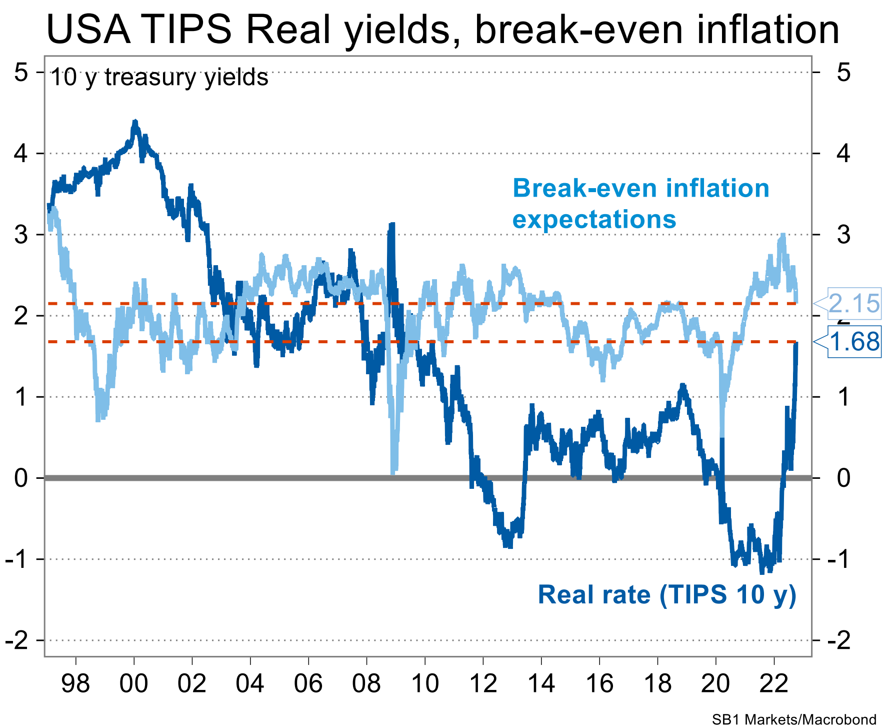
	Yield	Change 1w	Change 1m	Since Feb 18	Min since April-20
USA nominal treasury	3.83	0.14	0.72	1.91	0.52
.. break-even inflation	2.15	-0.22	-0.40	-0.26	1.06
.. TIPS real rate	1.68	0.36	1.12	2.17	-1.19
Germany nominal bund	2.12	0.14	0.64	1.90	-0.65
.. break-even inflation	2.24	-0.34	-0.45	0.26	0.40
.. real rate	-0.12	0.48	1.09	1.64	-2.80

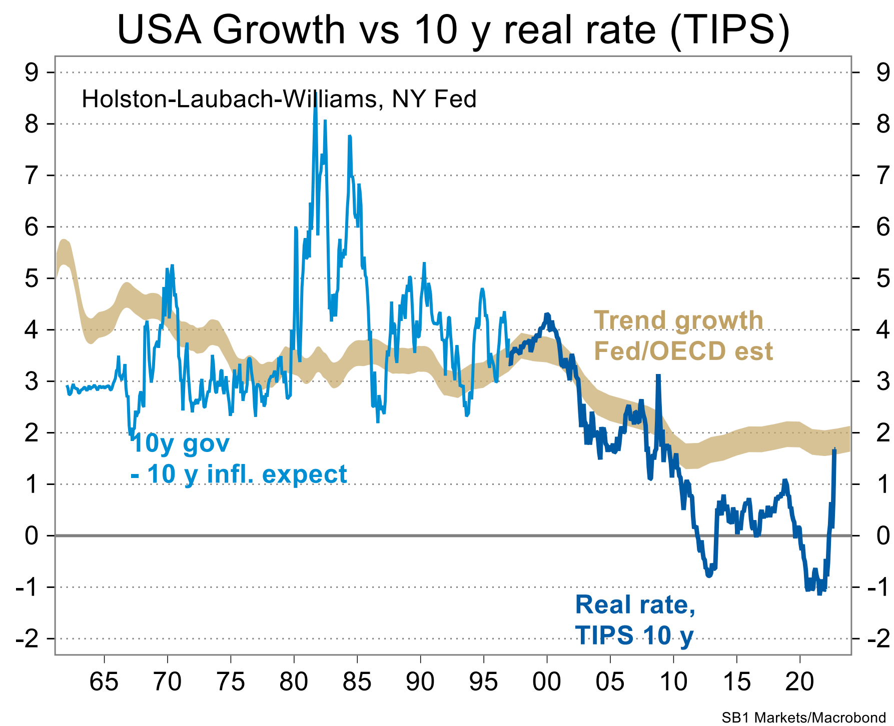
SB1 Markets/Macrobond

- These movements are for the history books!
- No signs of war angst or flight to safety
- No signs of fear of QE measure (a la BoE's gilt stunt) creating more inflation
- In the US, a 10 y CPI expectation at 2.15% is on the low side vs Fed's 2% target for the PCE-deflator (which in average is some 0.3 pp below CPI inflation)
- xxHeader right graph

Growth vs real rates: Mind the missing gap, it has closed!

Real rates are up, while short/medium-term growth expectations are below trend growth

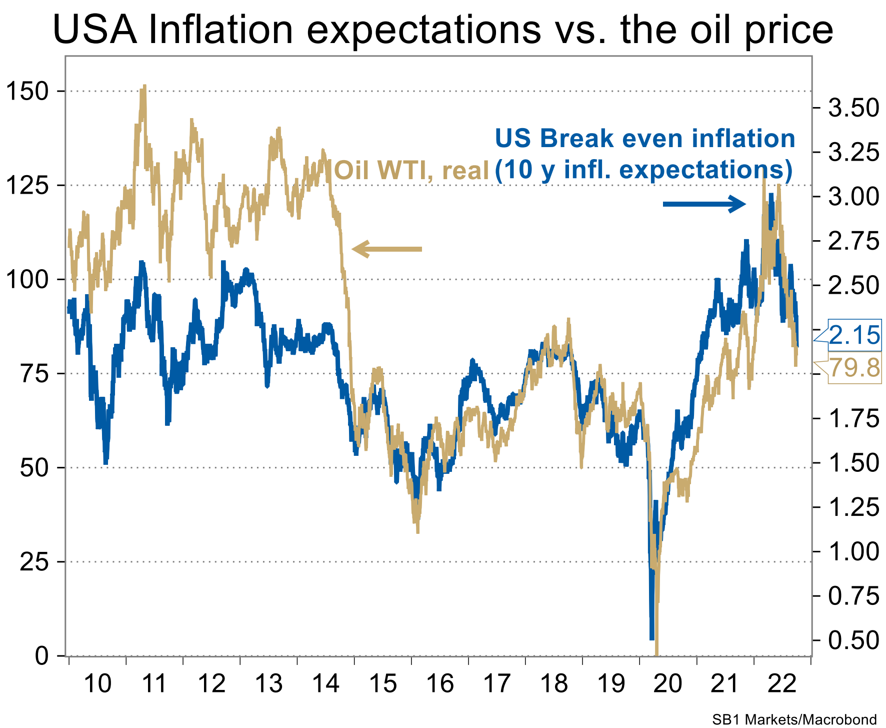


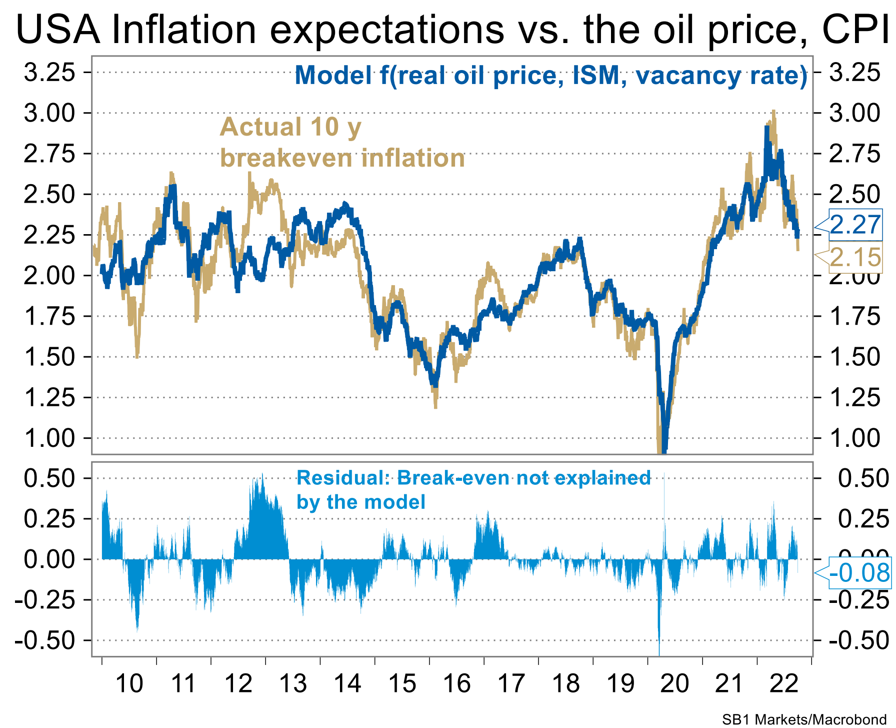


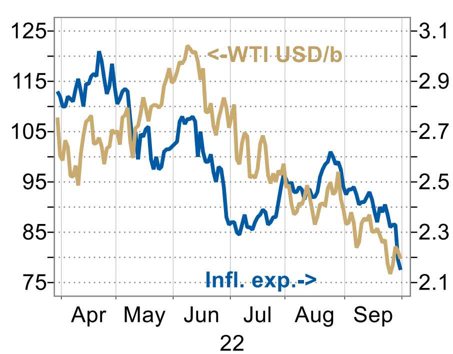
- Long term inflation expectations are ‘collapsing’, down 85 bps from the peak

(Longer-term) Inflation expectations are trending down, as our model suggests

If the economy slows – and the oil price does not surge – inflation exp. should come further down

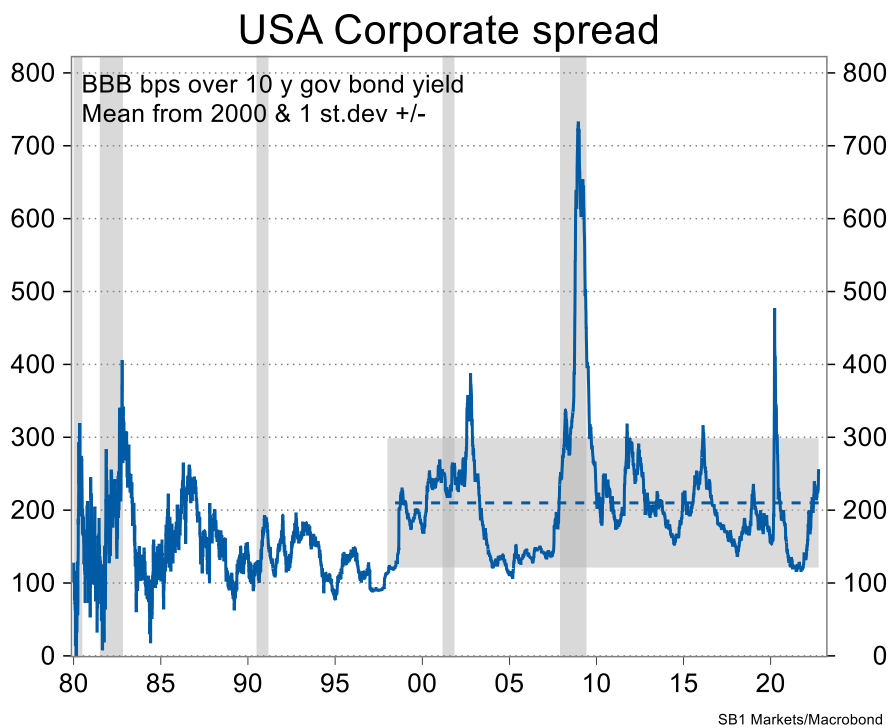


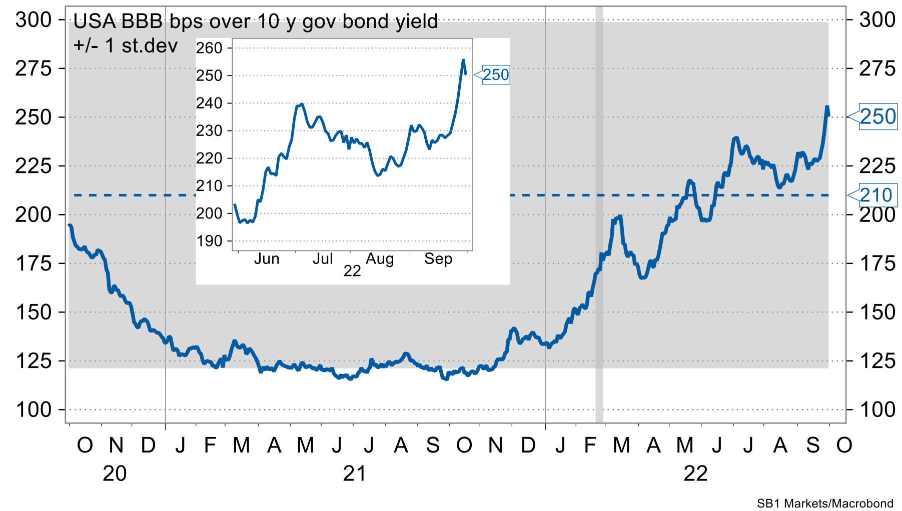




- A simple model including the <u>spot</u> oil price, the <u>current</u> ISM and the <u>current</u> vacancy rate pretty well explains the <u>long-term</u> breakeven inflation expectation in the bond yield curve
- What now? We are uncertain about the oil price, but rather confident that both the ISM, and the vacancy rate will decline. Impact vs the 10 y break-even expected inflation rate
  - -5 ISM points: -12 bps
  - -3 vacancy pts, (to 3.6% from 6.6%): -36 bps
  - - 10 USD/b: -10 bps

Risk on: Credit spreads up, alongside a weaker stock market



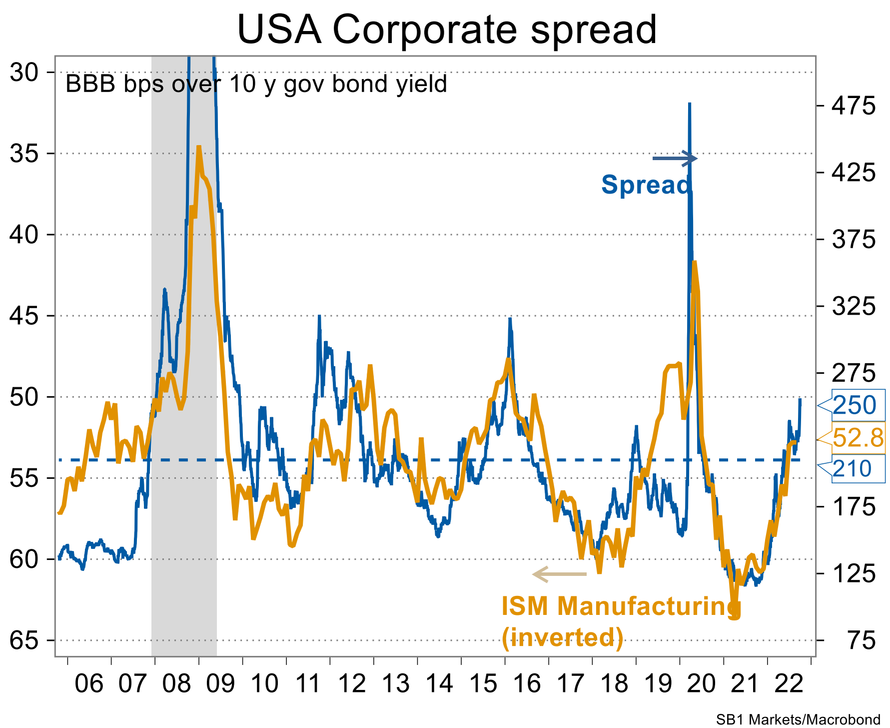


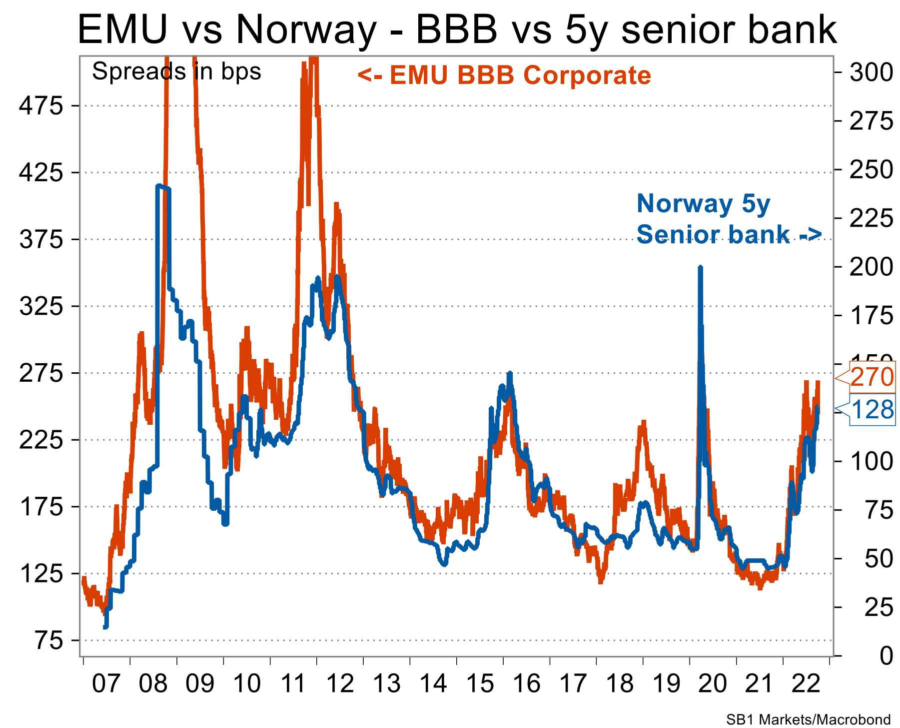
- The US BBB spread is up more 130 bps from the bottom last autumn, almost a doubling
- In addition, real rates have increased by more than 250 bps since late last year
- Thus, the basis for all valuation metrics has changed dramatically, check the chart two pages forward!

SpareBank 1 MARKETS

Why have credit spreads widened in 2022? Could it be the slowing economy?

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

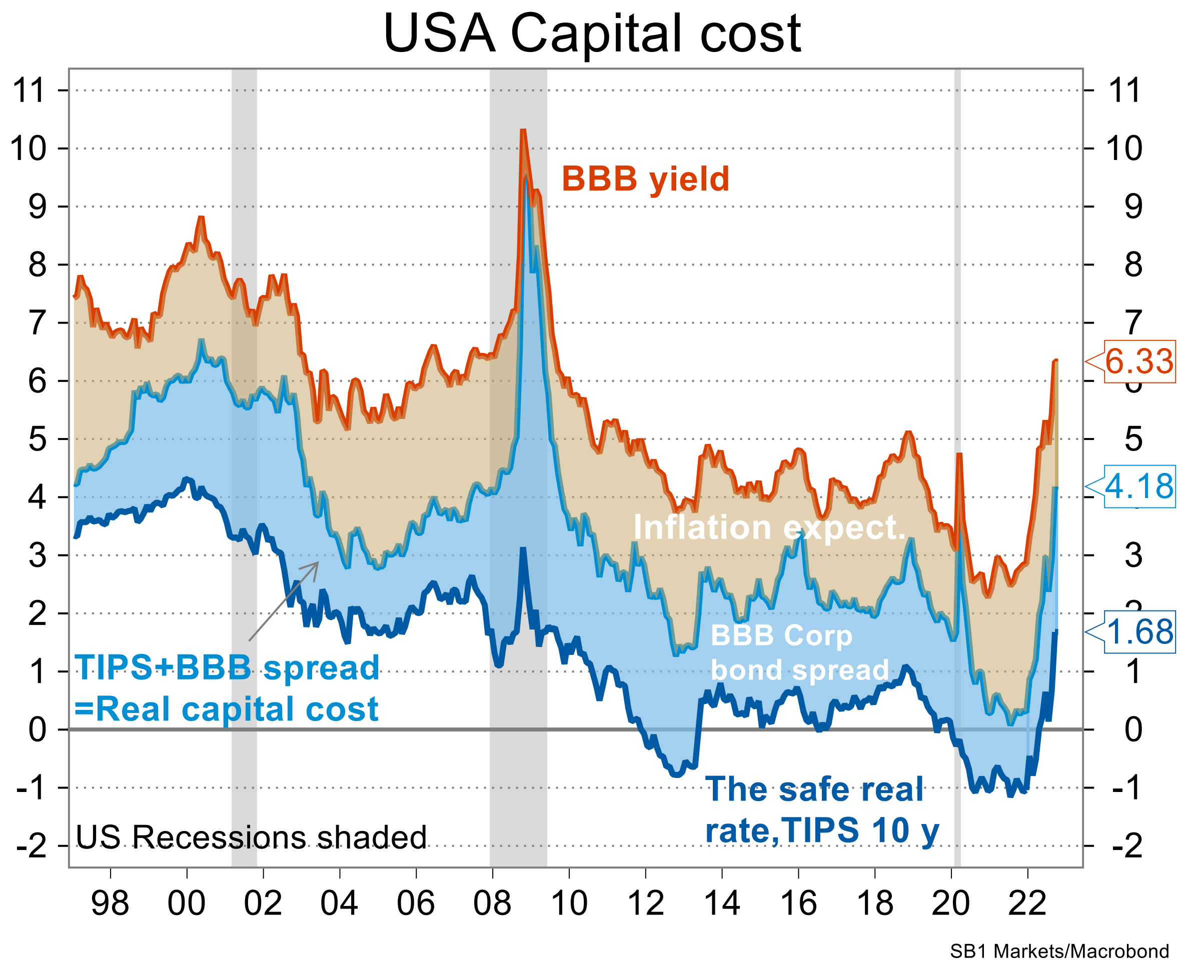




- The answer is not irrelevant for your view on the outlook for spreads, we think
- And do you think Norwegian spreads will be influenced by changes in the global credit market?
- Last week: Norwegian credit spreads rose in sympathy with higher spreads abroad the previous week
- The good news: The recent hike in spreads have made these credit instruments far more attractive, at least from a hold to maturity perspective

The cost of capital is not what it was some few months ago

All valuation metrics have changed dramatically. *As have all calculations of return on capital*

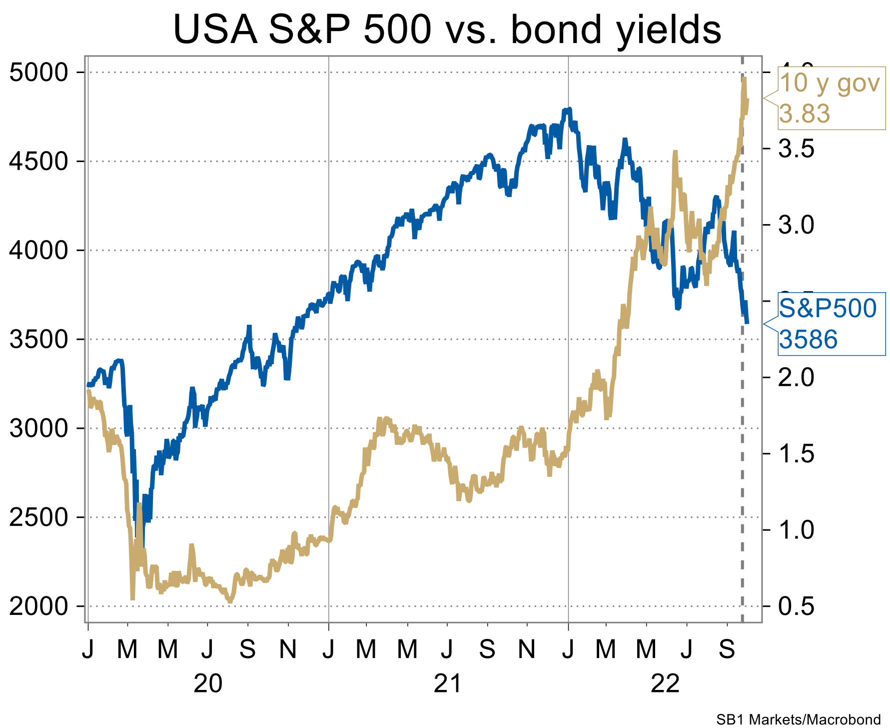


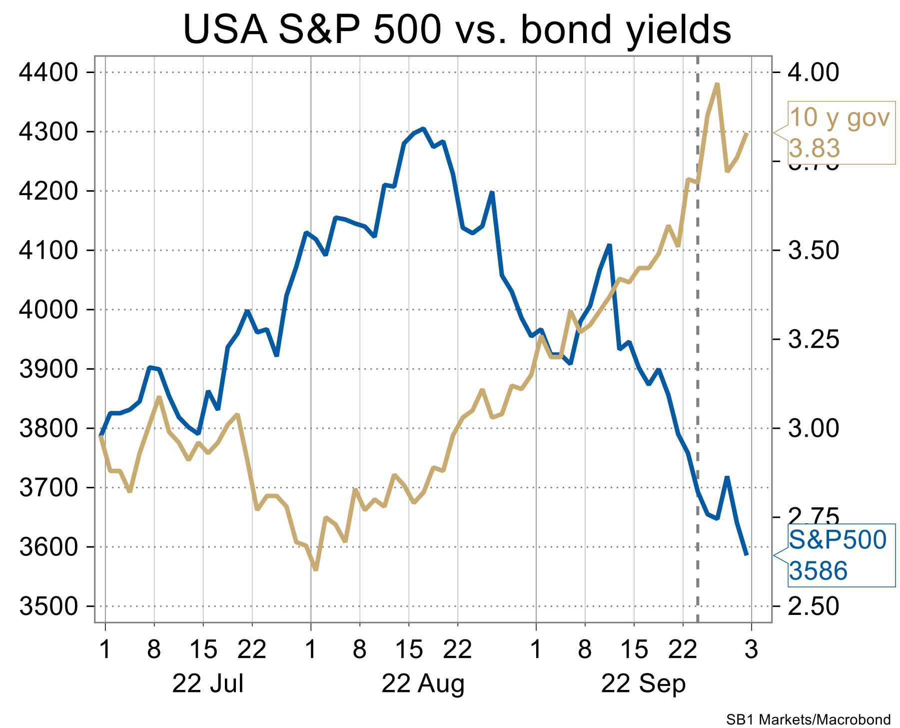
- The total real borrowing cost for a BBB company has increased to 4.2% bps from zero by the end of last year:
  - The TIPS real rate is up from -100 to + 168 bps
  - The BBB corporate investment grade spread is up from 120 bps to 250!
- Add on modest inflation expectations, the nominal borrowing cost has increase from well below 3% to above 6%

SpareBank 1 MARKETS

And last week it was… higher-than-expected inflation? And UK gilts, of course

The S&P fell below the June through – 10 y treasury yield rose 14 bps to 3.83%, but w/extreme vol!





- The 10 y gov briefly crossed the 4%-line before rapidly falling back to 3.70% in sympathy with the huge decline in British yields, following BoE bazooka-message & actual government bond purchases on Wednesday

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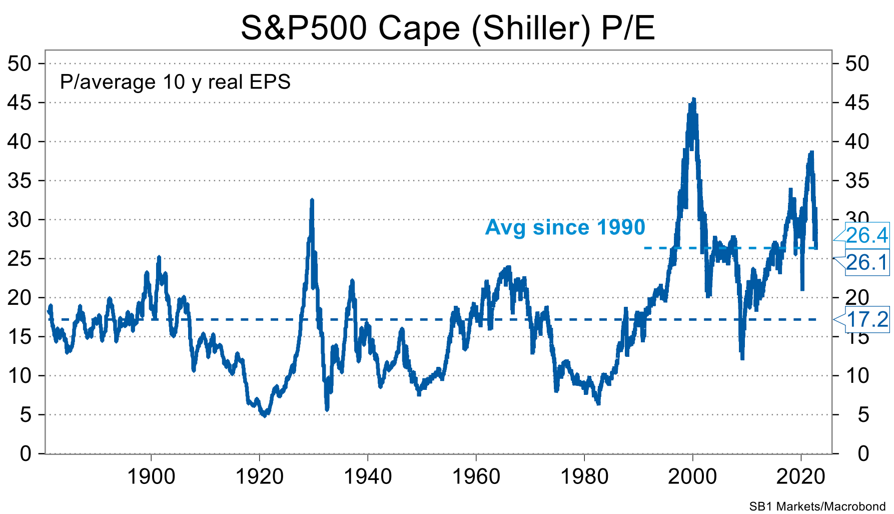
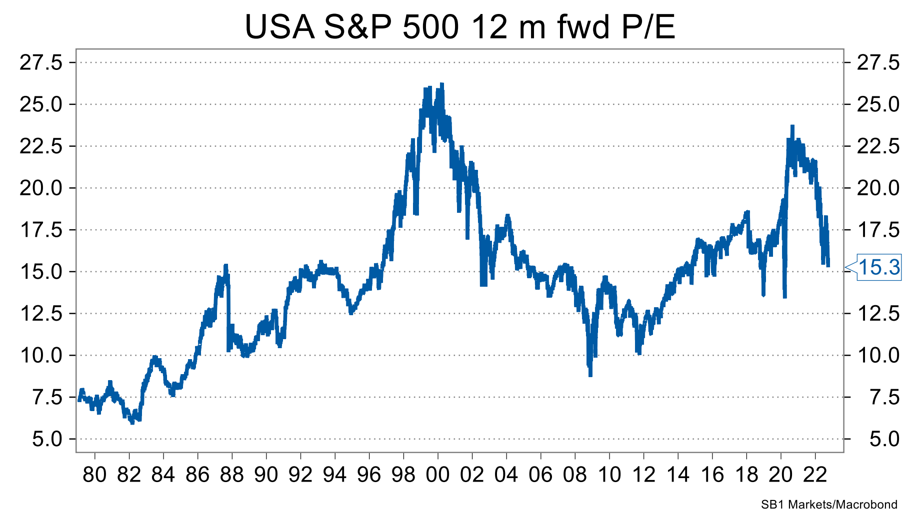
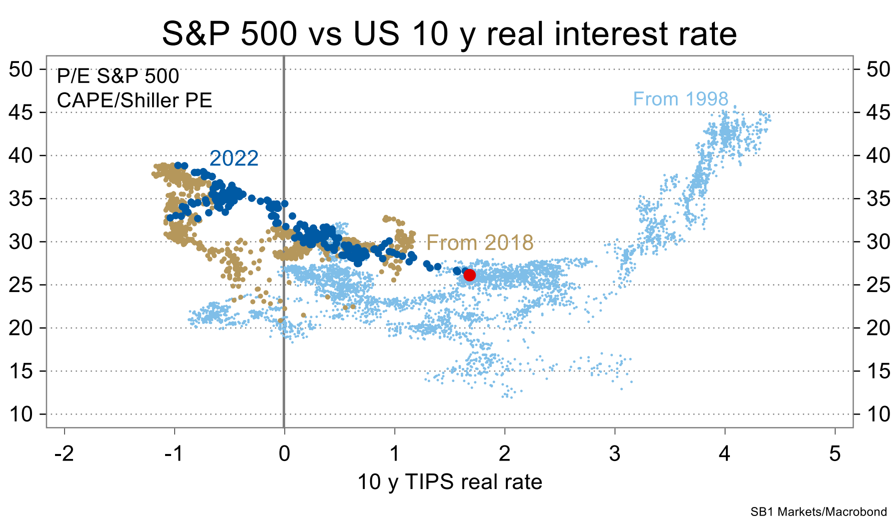
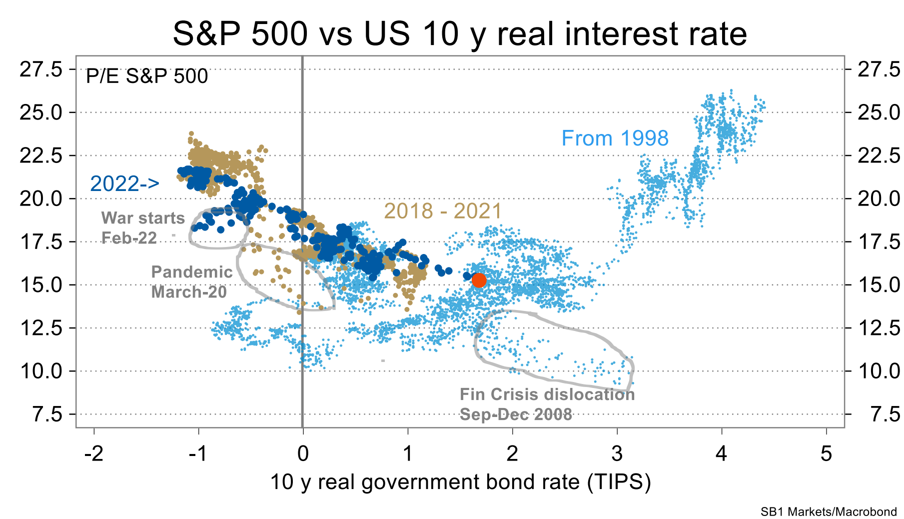
4 valuation charts: Check the extreme tight correlation between real rates, P/E

The TIPS real rate has been the main driver for the P/E since 2018. And it still probably is





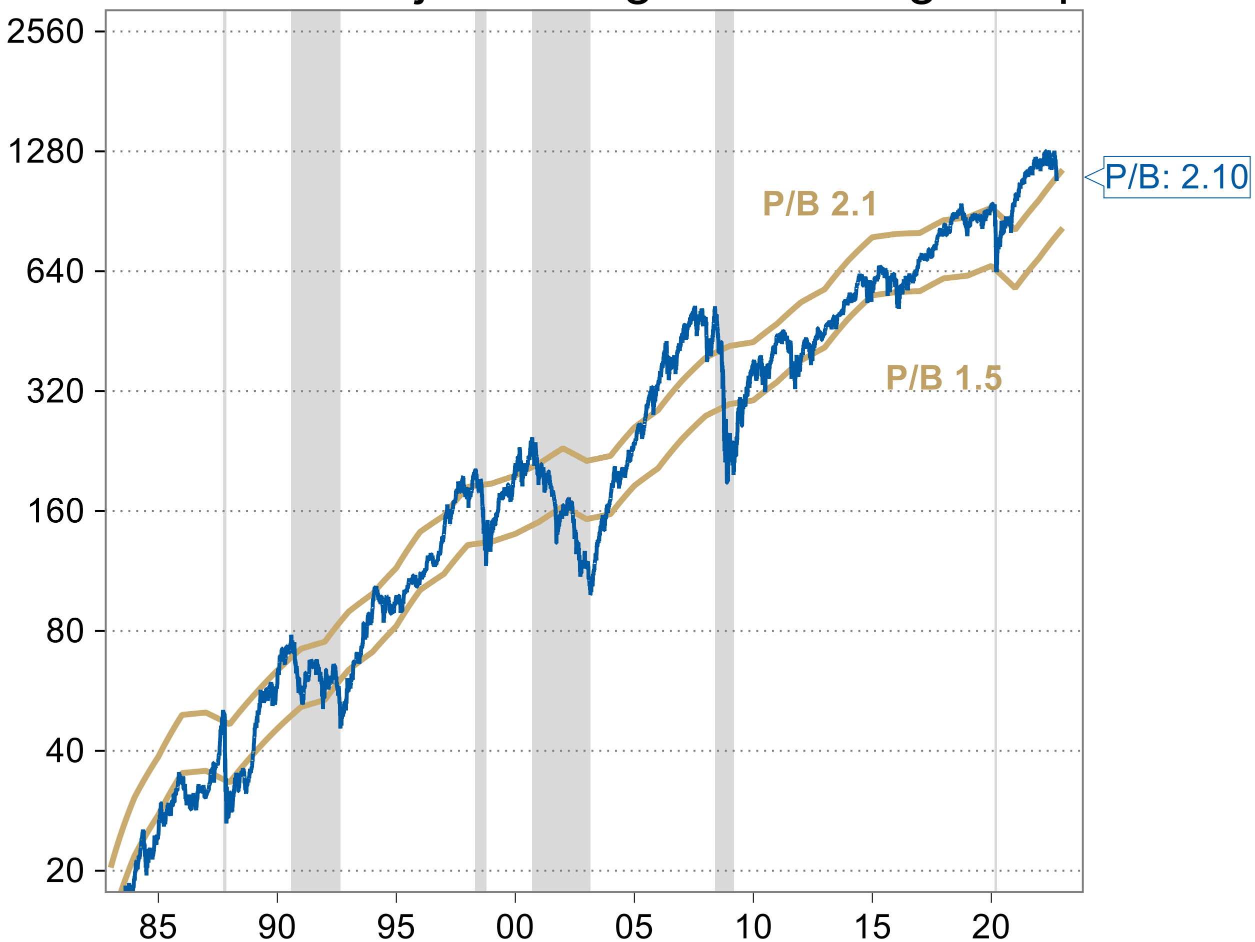


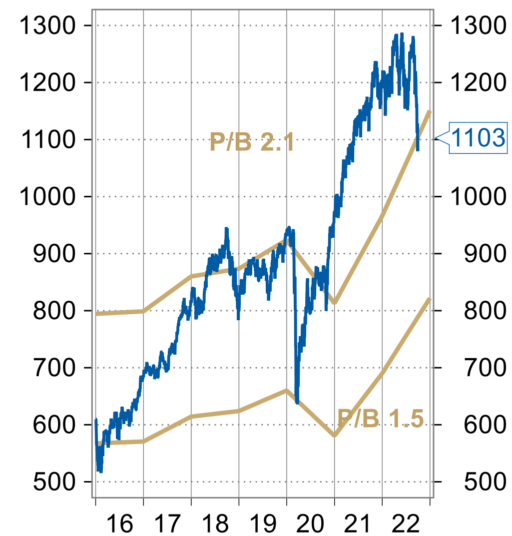


Finally, OSEBX almost hit the upper band of the 1.5/2.1 Price/Book corridor

Thus, it is just 29% down the lower (1.5) band, at 800! A <u>very</u> safe bottom at 500 (P/B=1)

Oslo Børs - aksjeverdi og verdi av egenkapitalen



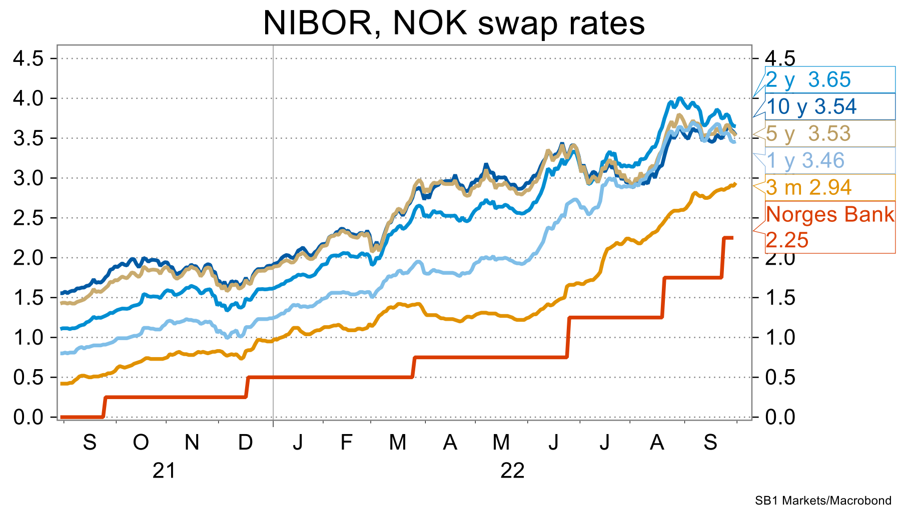


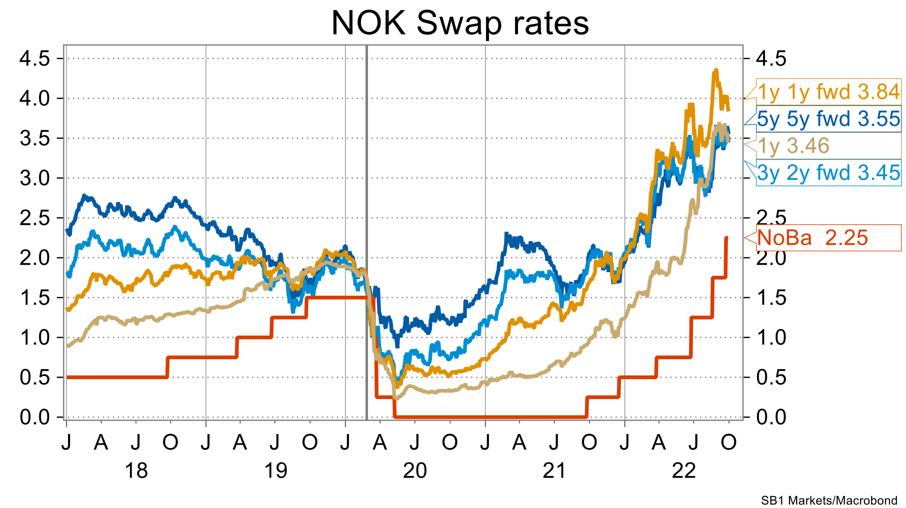
Source: Oslo Børs, Vital, Bloomberg, SB1 Markets, Macrobond.

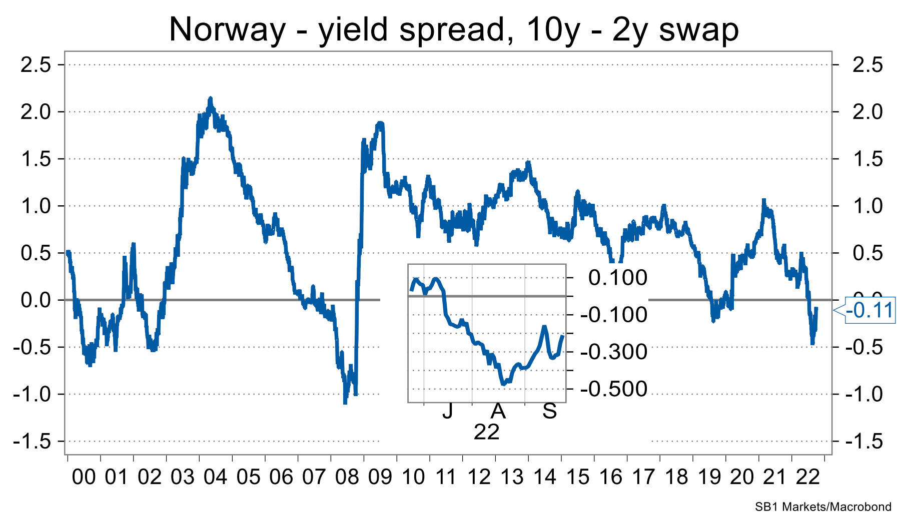
Source: Oslo Børs, Vital, Bloomberg, SB1 Markets, Macrobond.

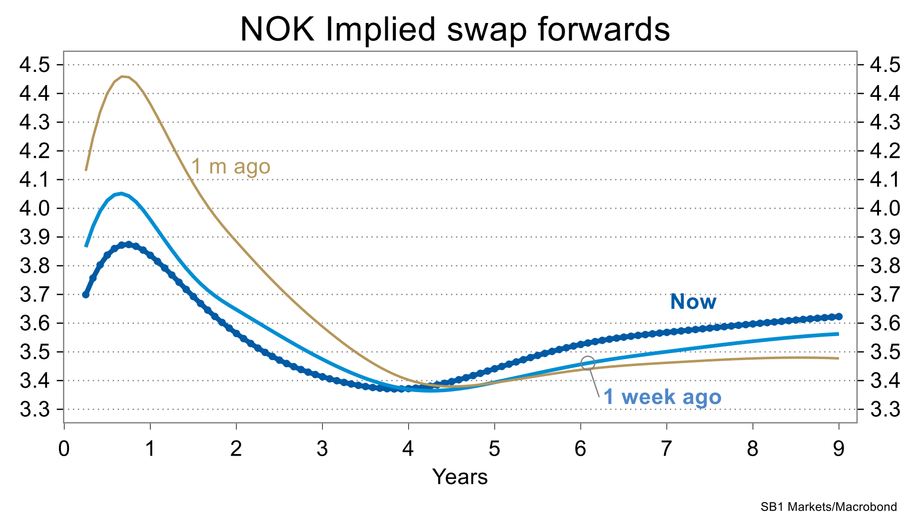
Norwegian swaps down in the short end, up in the long end (implied)

The 3m NIBOR up to 2.94%



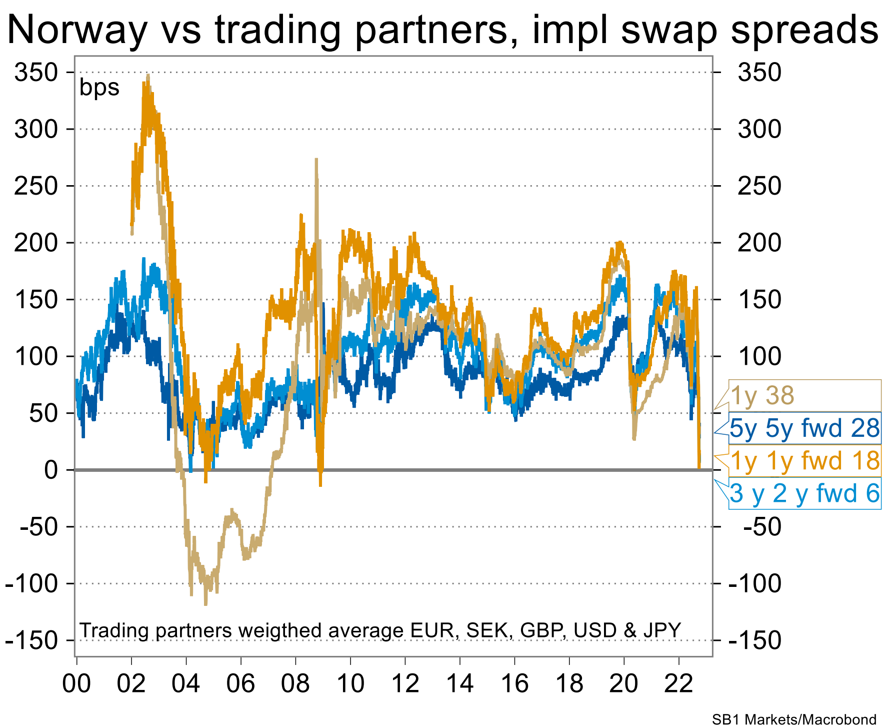


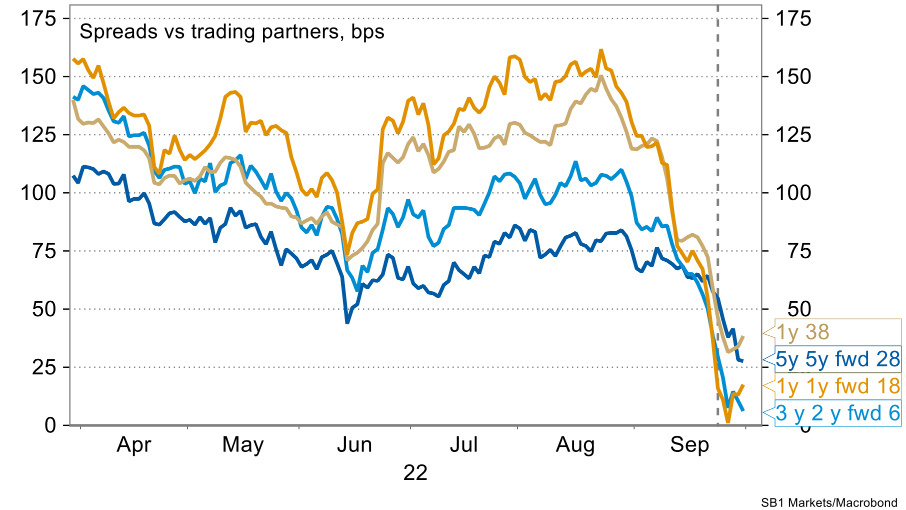




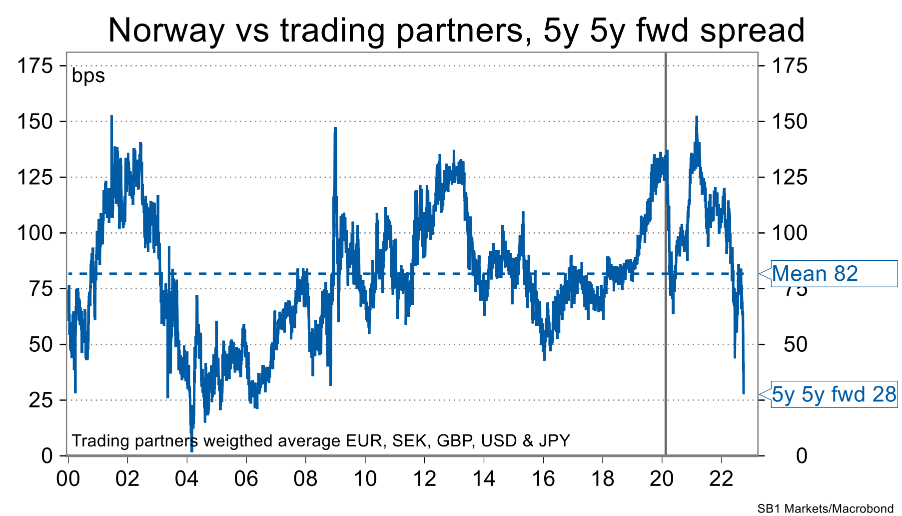
Spreads vs trading partners are collapsing, much faster than we expected

Implied spreads have fallen to low levels all over the curve



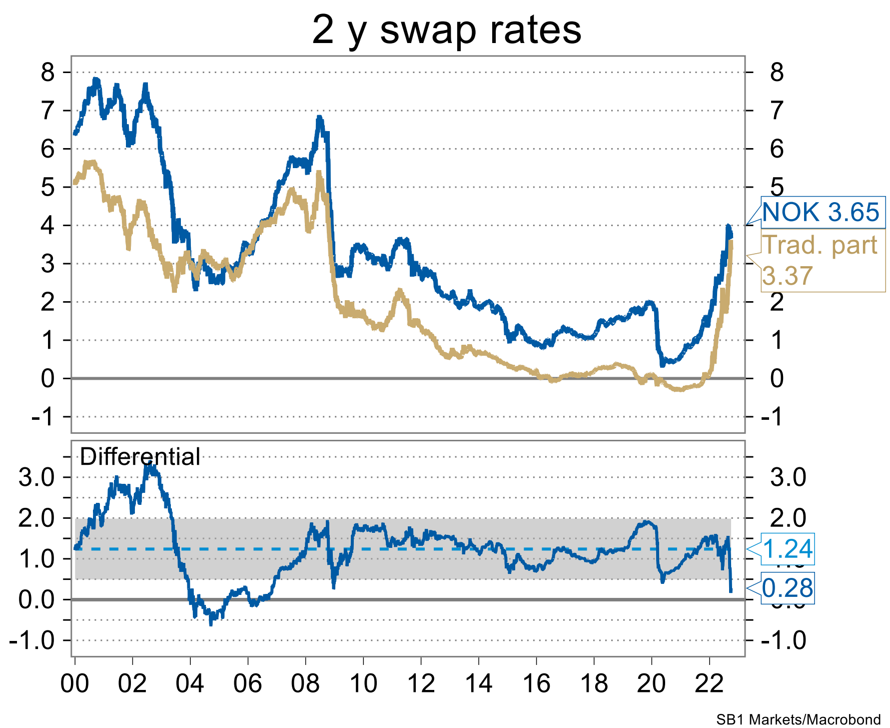


- NOK rates are still above the average level among our trading partners – but the margins were sharply reduced last week. We have long argued that NOK rate expectations were too high vs. our trading partners but did not expect such a rapid decline
- XXXX TEKST HER XXXX
- However, the 'structural' low rates in the Euro Area (compared to the Anglo Saxon countries) may take the 'trading partner' average too far down
- **Now, there is still some downside potential in the short end, given the still rather aggressive NOK FRA-rate path (check next page)**

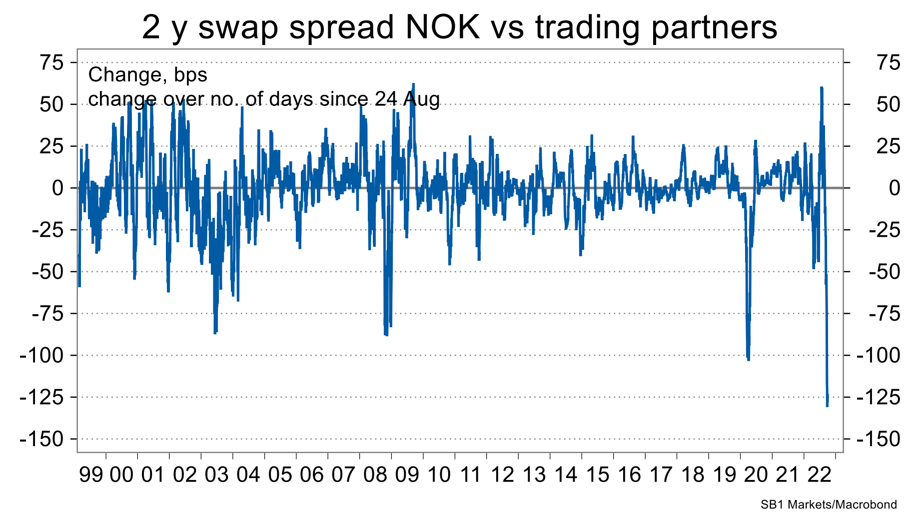


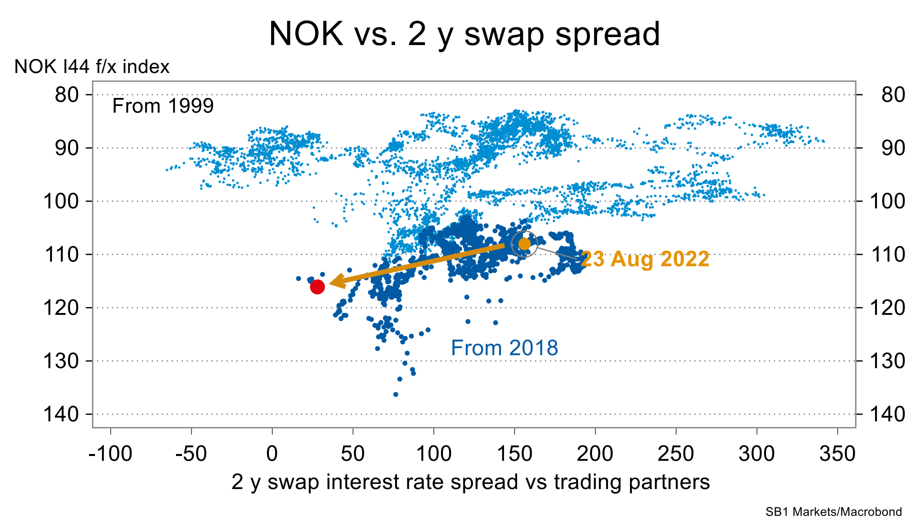
The largest decline in NOK 2 y interest rates vs. trading partners, ever!

The largest decline ever over 5 weeks, to the lowest level since 2007



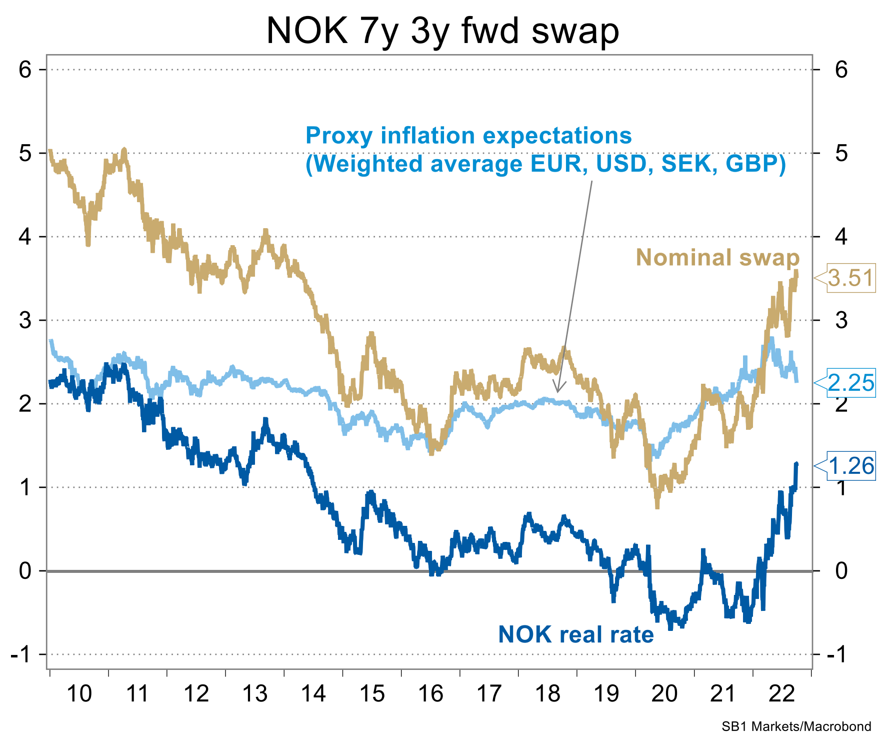
- Rates abroad have surged further, while Norwegian rates have fallen. NOK rates are still higher than among our trading partners, but by just 28 bps
- The NOK has fallen, but not by much (confirming the weak correlation between NOK and the interest rate differential) – and the oil and gas prices have fallen too

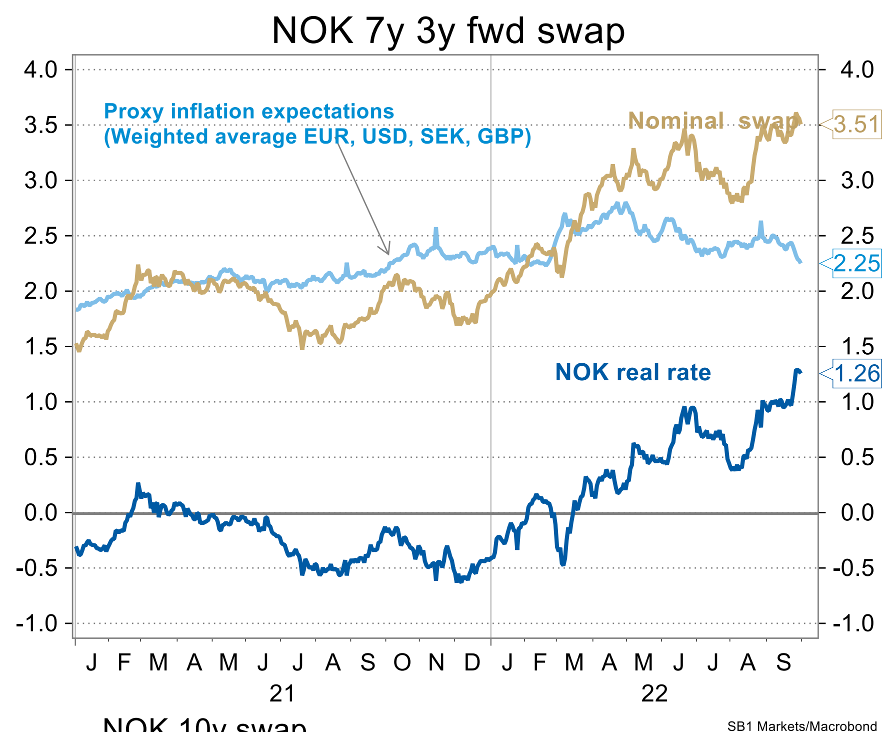


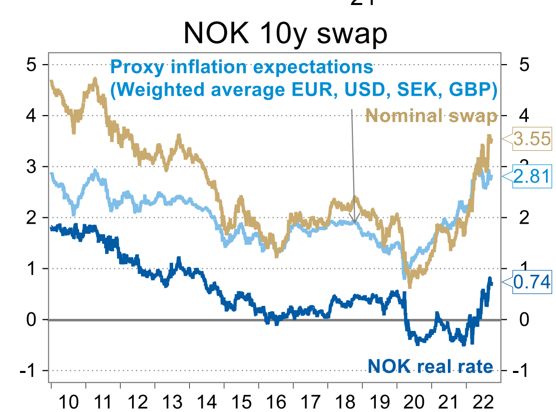


Norway: NOK inflation expectations very likely down, as in the rest of the world

If so, real rates rose sharply in Norway too last week – and the trend is straight upwards







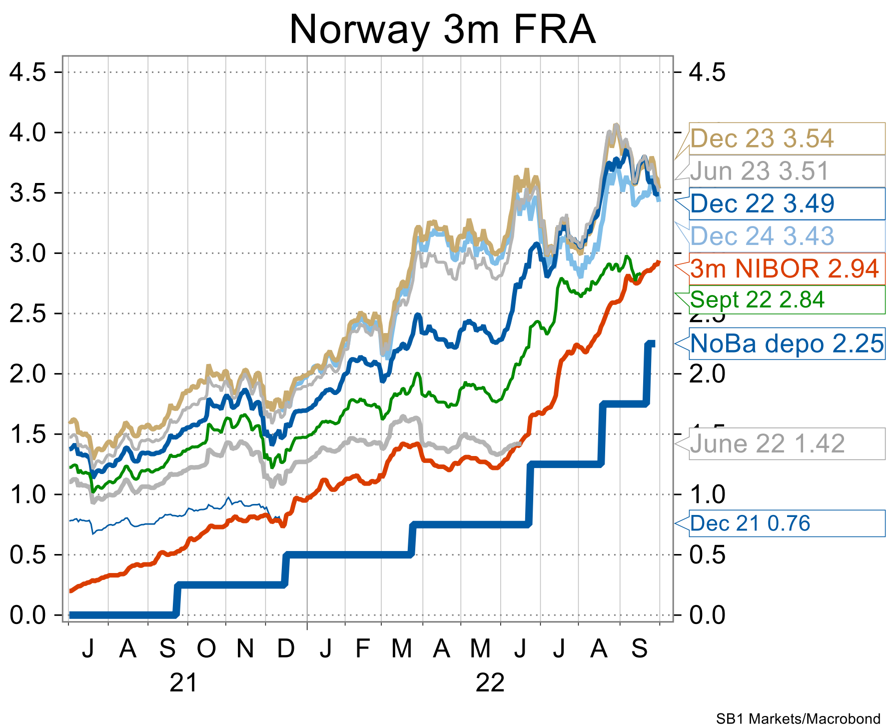
- The lift in nominal swap rates recent months is due to higher real rate expectations, while inflation expectations are trending down

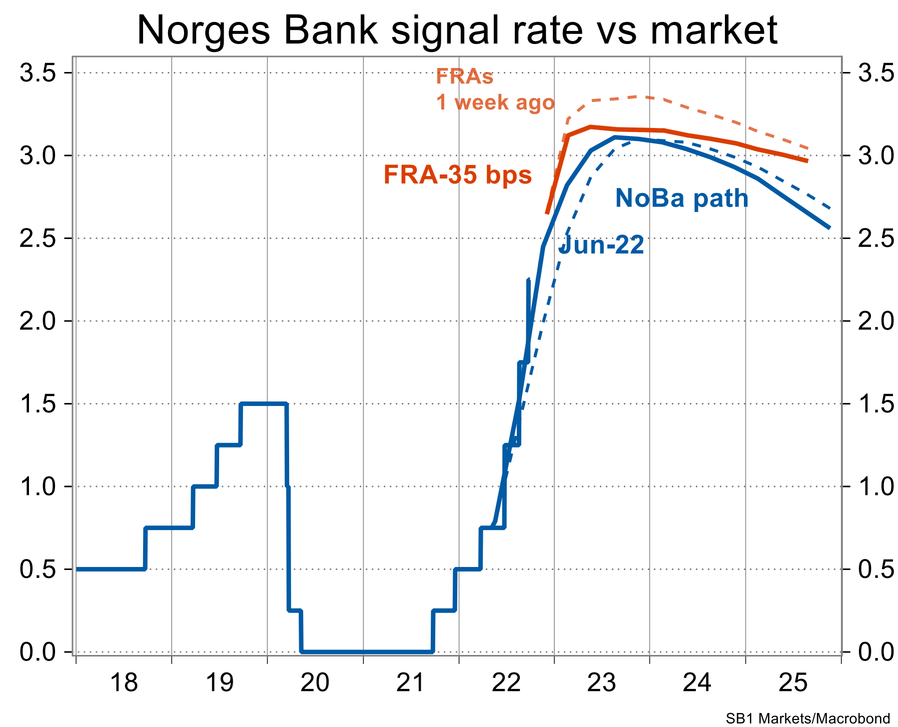
Memo: Our NOK inflation expectation proxy is a weighted average of EUR, SEK, GBP, and USD inflation swaps, cross-checked vs historical inflation differentials and inflation expectations from surveys

SpareBank 1 MARKETS

The FRA market is calming down, still above NoBa's interest rate path

The FRA rates are still too high, at least in the short end





- **The 3 m NIBOR** added 9 bps to 2.94% last week. Even so, FRA rates fell, from 3 m Dec-22 -9 bps, via Dec-23 -19 bps to -4 bps in far end
- **NoBa** signalled +25 bps in Nov and +25 bps in Dec. The **FRA market** assumes 50 bps in November, and a 60% for another 50 bps in December (given 25 bps as the alternative)
- **Market expectations** are still too aggressive. Given the average debt level, as well as the proportion of households within the 'fat tail to the right' (the proportion who have borrowed a lot vs. income), household demand will hurt too much, and house prices could fall faster and more than is needed to take the inflationary pressure out of the Norwegian economy. Real wages are under pressure as well, as there are few signs of higher nominal wage inflation. In addition, the momentum in the economy is weakening, and a decline in activity is rather likely. However, capacity utilisation is high, and there is still excess demand for labour. Thus, some further tightening is probably warranted but the risk may well be on the downside vs. NoBa's path, than on the upside

SpareBank 1 MARKETS

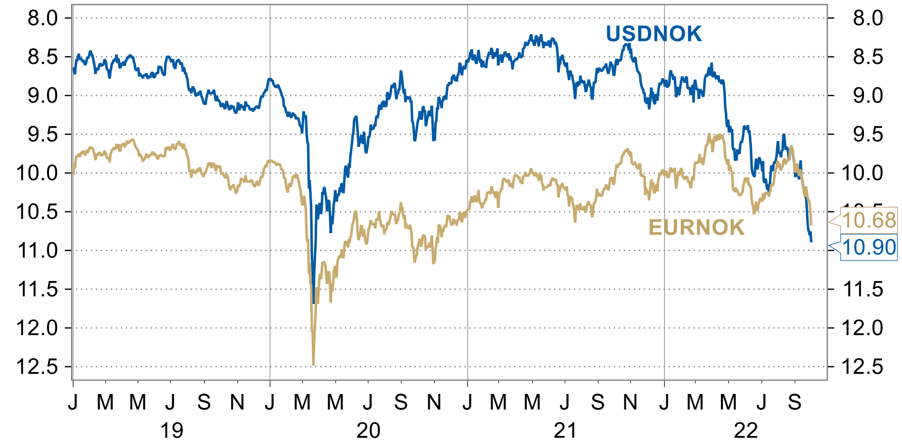
The GBP recovered most of the previous week's losses. King Dollar further up

NOK fell further. The JPY returned to the downward path, after the previous week's f/x intervent.

EURUSD

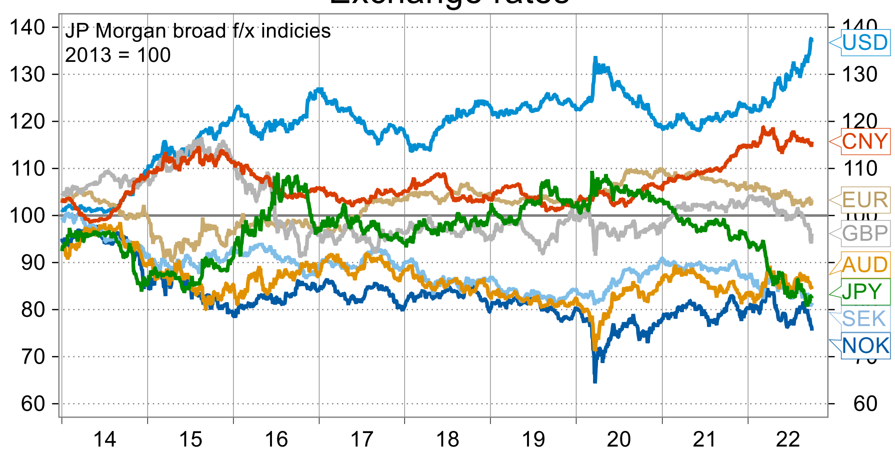
SB1 Markets/Macrobond

NOK vs EUR & USD



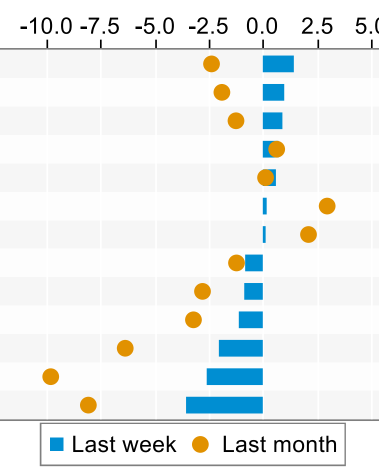
SB1 Markets/Macrobond

Exchange rates



SB1 Markets/Macrobond

F/x markets



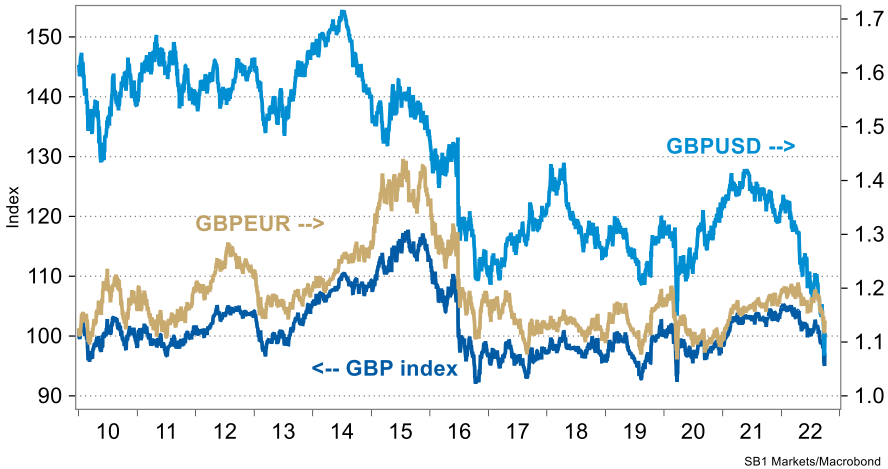
JP Morgan f/x broad indices + 3 f/x crosses	Last week	Last month
GBP	1.4	-2.4
EURUSD	1.0	-1.9
SEK	0.9	-1.2
EUR	0.7	0.6
CNY	0.6	0.1
USD	0.2	3.0
CHF	0.1	2.1
JPY	-0.8	-1.2
AUD	-0.9	-2.8
CAD	-1.1	-3.2
NOK	-2.0	-6.4
NOKUSD	-2.6	-9.8
NOKEUR	-3.5	-8.1

SB1 Markets/Macrobond

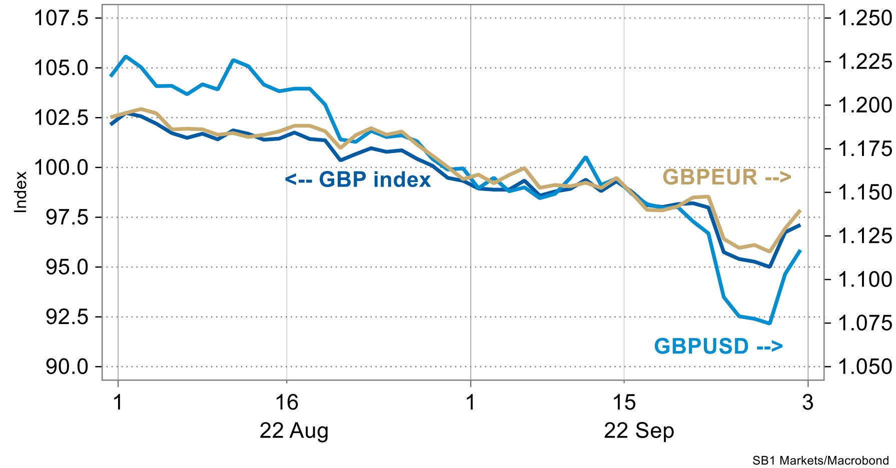
The pund ran into trouble but recovered most of the loss last week

The decline in the GBPUSD rate was mostly due to a strong USD, not a weak pound

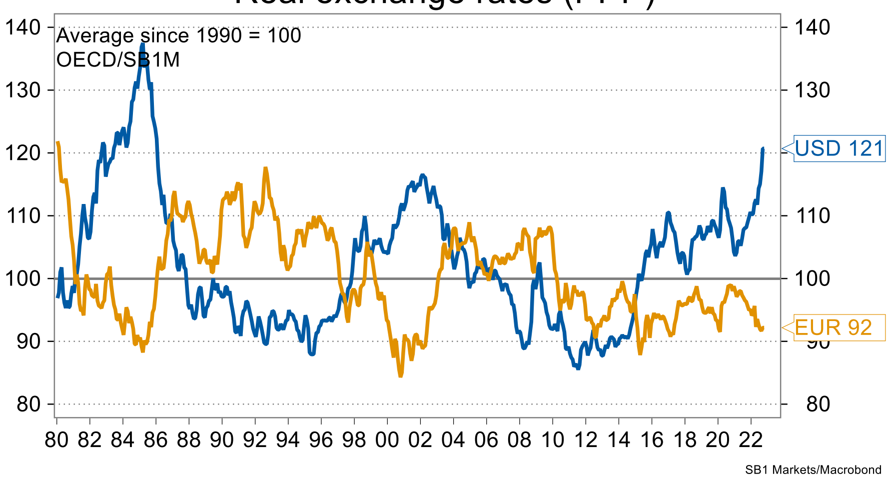
GBP vs USD, EUR & the GPB index



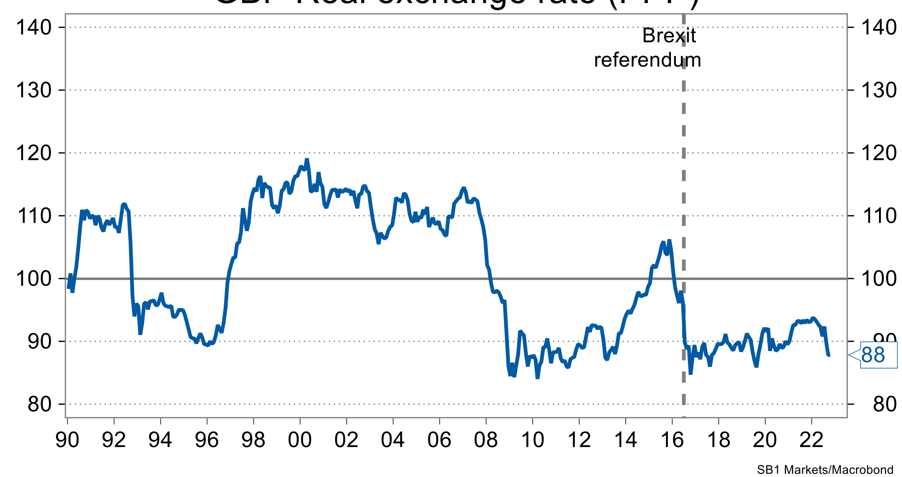
GBP vs USD, EUR & the GPB index



Real exchange rates (PPP)



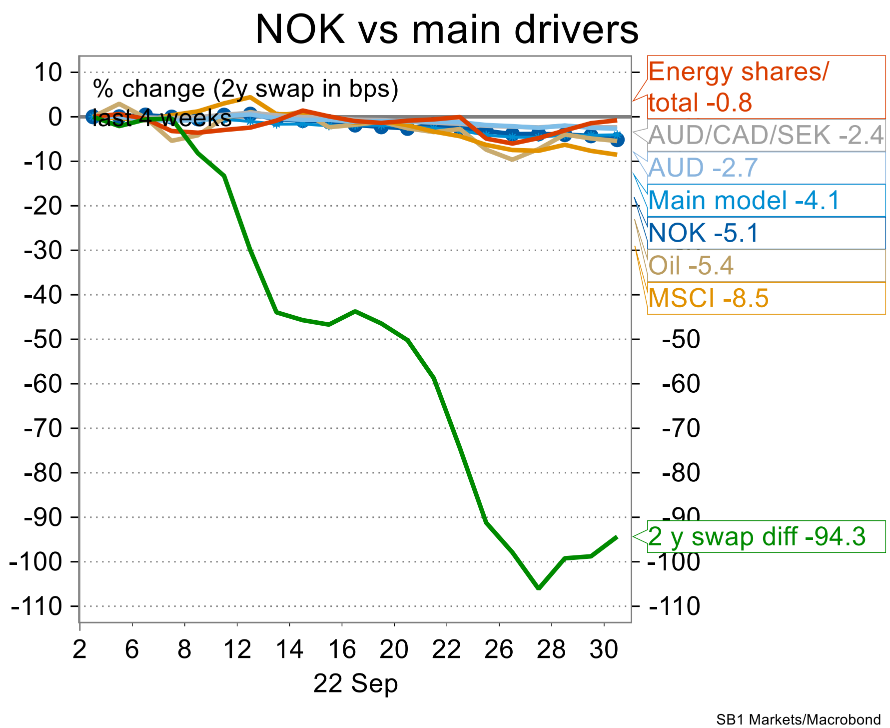
GBP Real exchange rate (PPP)

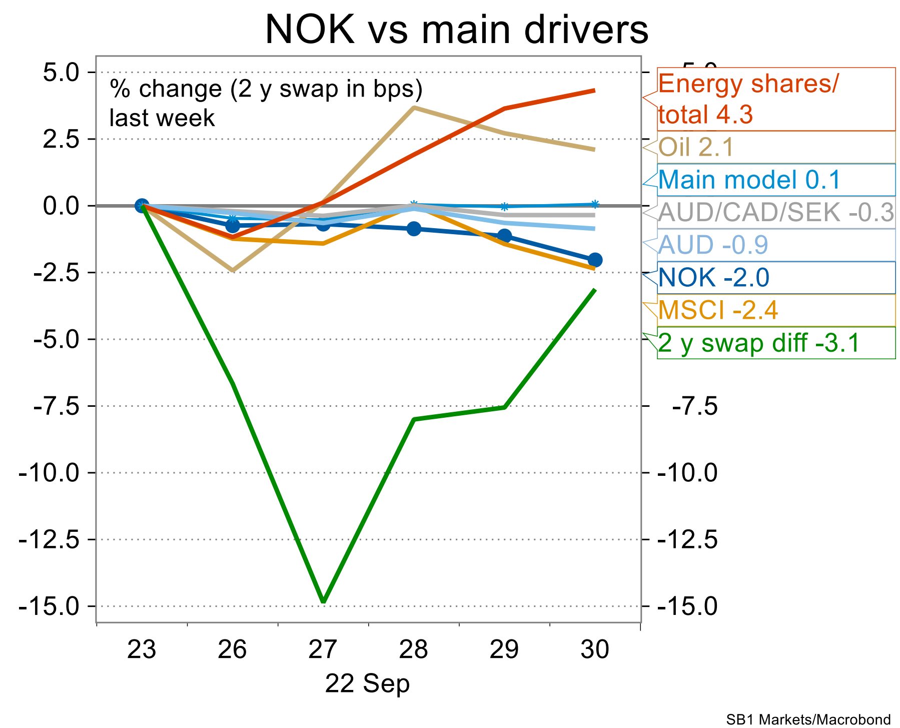


SpareBank 1 MARKETS

NOK down 2%, our model suggested unch. The oil price slightly up

The decline in NOK interest rates vs. our trading partners slowed to a trickle, after an unprecedented drop





Gaps vs. out model estimates narrowed

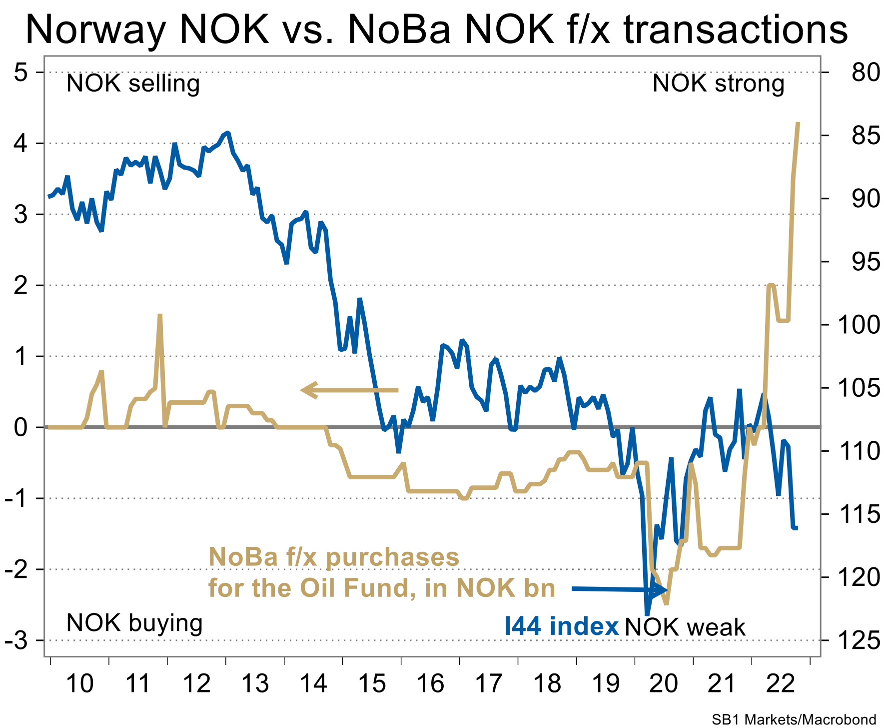
- ***NOK is 2.5% <u>below</u> our main model estimate (from –0.5%)***
- The NOK is 10% <u>weaker</u> than our AUD/CAD/SEK-model, our 'super-cycle peers', predicts, a substantial weakening (from -7%)
- NOK is 3% weaker than an estimate from a model that includes global energy companies equity prices (vs the global stock market) (from -0.5%)

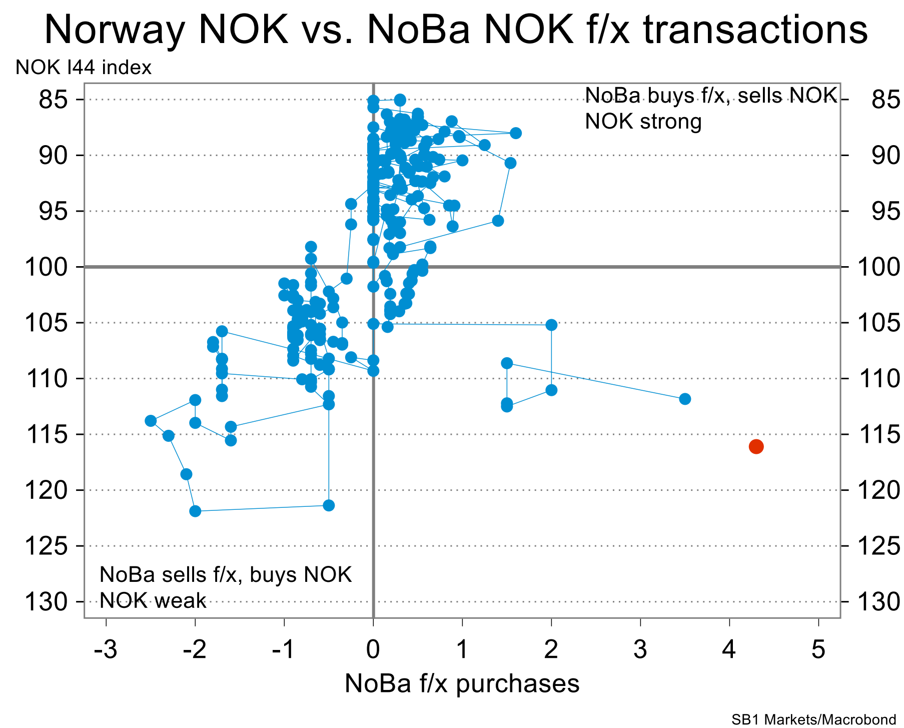
Why was NOK so weak last week? Most of the decline took place on Friday, when Norges Bank surprisingly announced that it increased its daily f/x purchases for the Oil fund to an amount equalling NOK 4.3 bn/day in October, up from 3.5 bn/day in September

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

NoBa will buy even more f/x for the Oil Fund, up to NOK 4.3 bn/day, from 3.5 bn

The lift probably contibuted to NOK decline on Friday – even if the 'real' correlation is the opposite



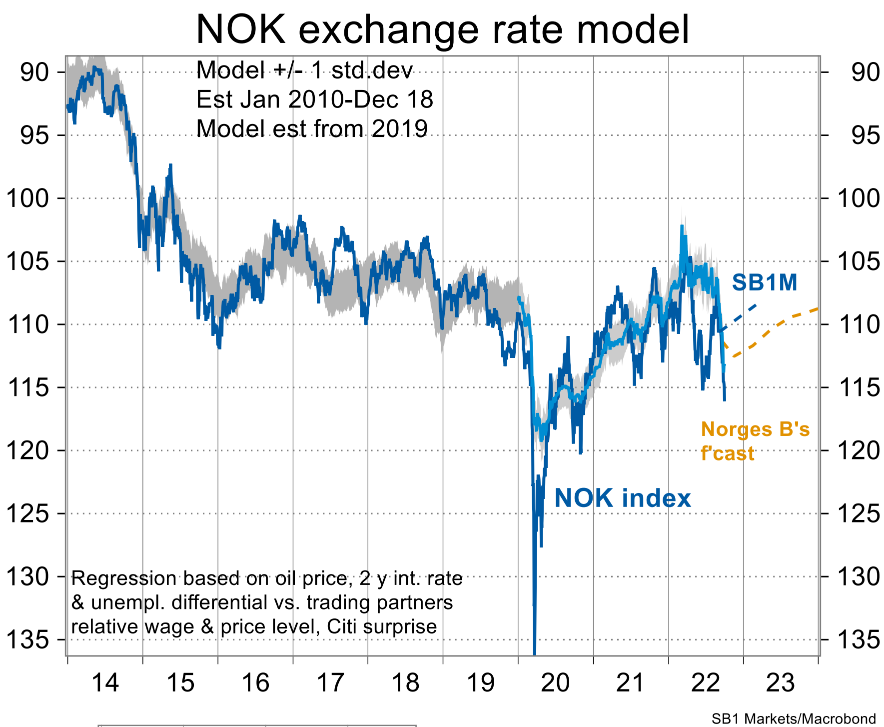


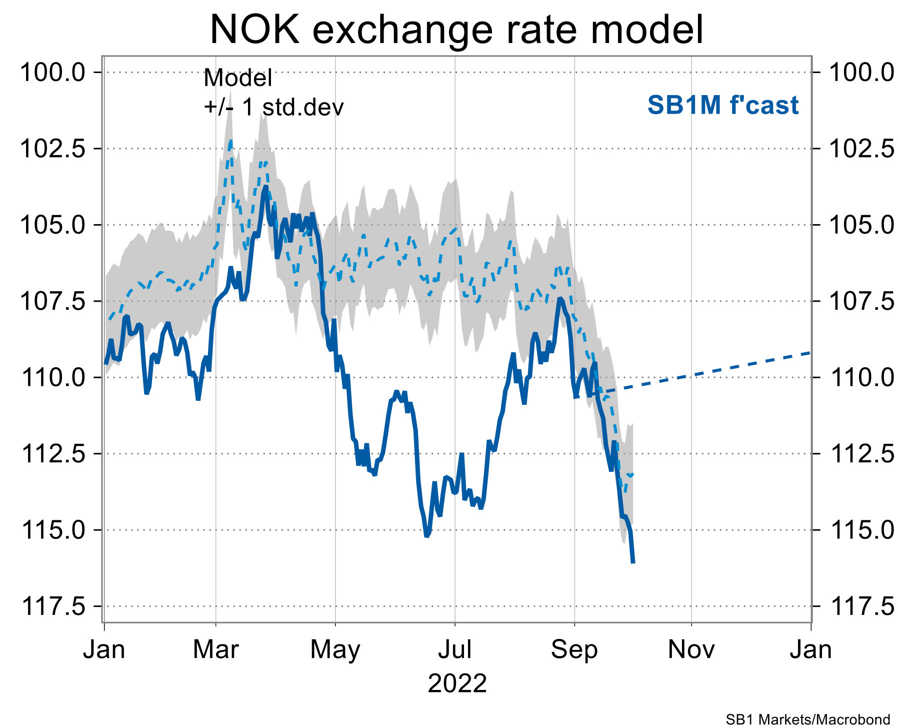
- … because Norges Bank sells NOK when oil/gas prices ares high! And the oil prices dominated completely, over the cash flow impact of NOK selling 'afterwards'
- Even in a full model, the partial effect of NOK sales has the wrong sign!
- Still, last week the market was surprised by the increased buying of NOK, consensus was for an unchanged amount

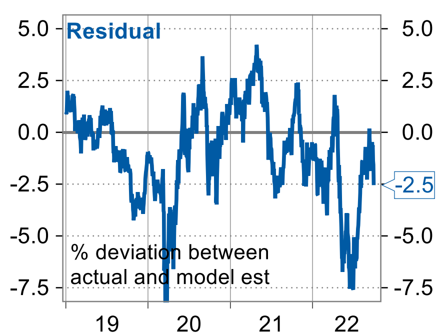
SpareBank 1 MARKETS

The NOK 2.5% below the model estimate

Both are heading down of course



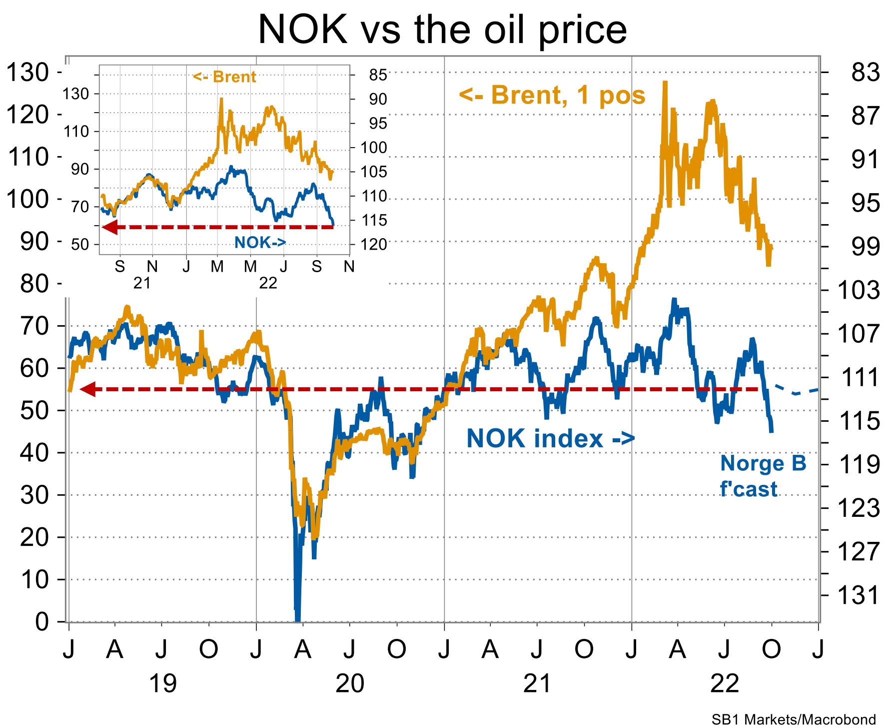


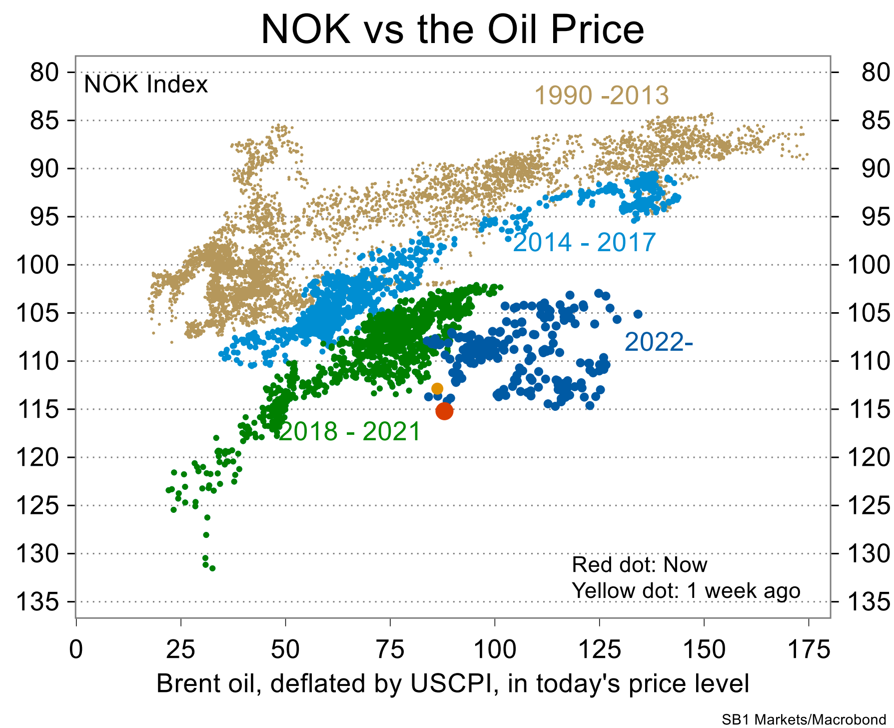


SpareBank 1 MARKETS

NOK is heading downwards in tandem with the oil price

... but last week it was just the NOK that fell

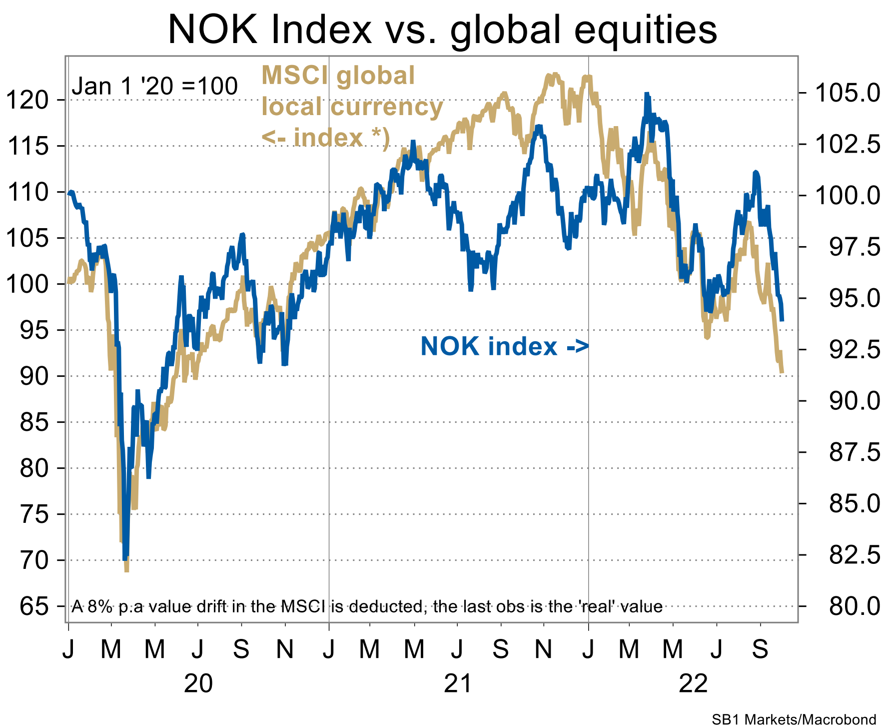


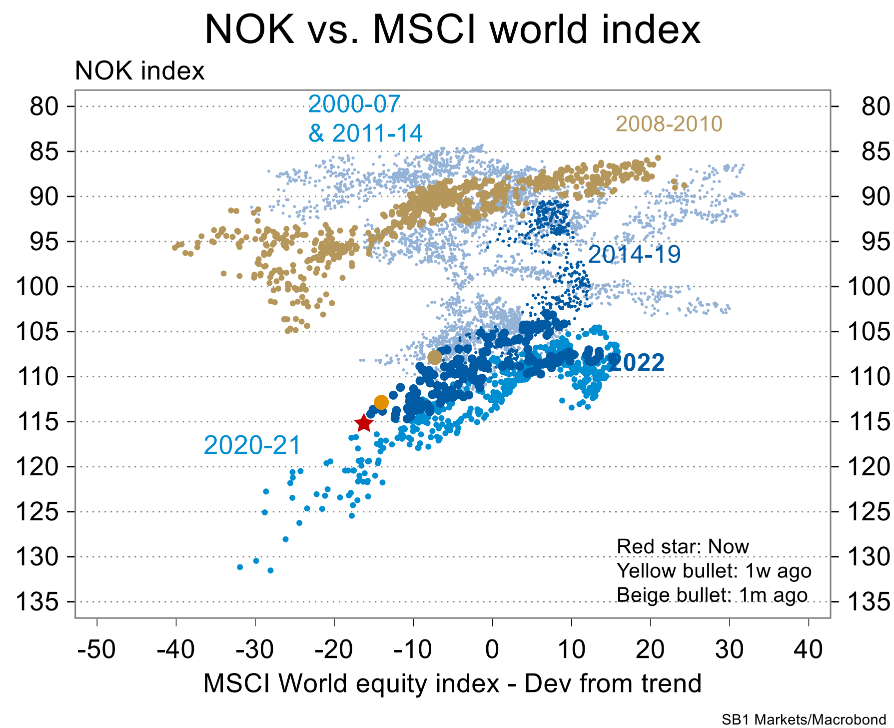


- The correlation between the NOK and the oil price has been non-existent since the start of 2022

The NOK has joined global stock markets, downwards

The NOK has been more in sync with stock markets than normal since April

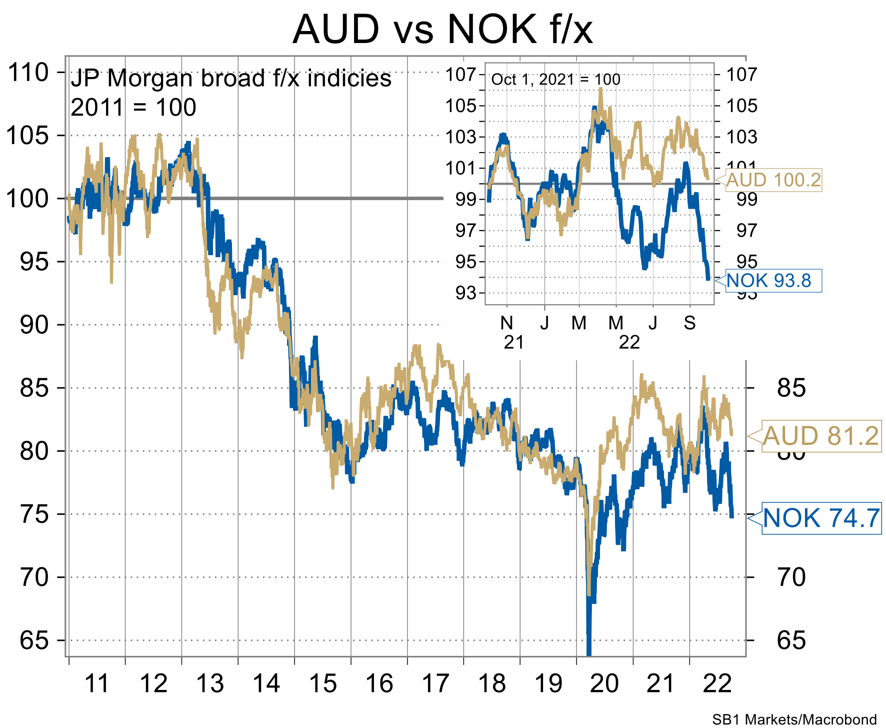


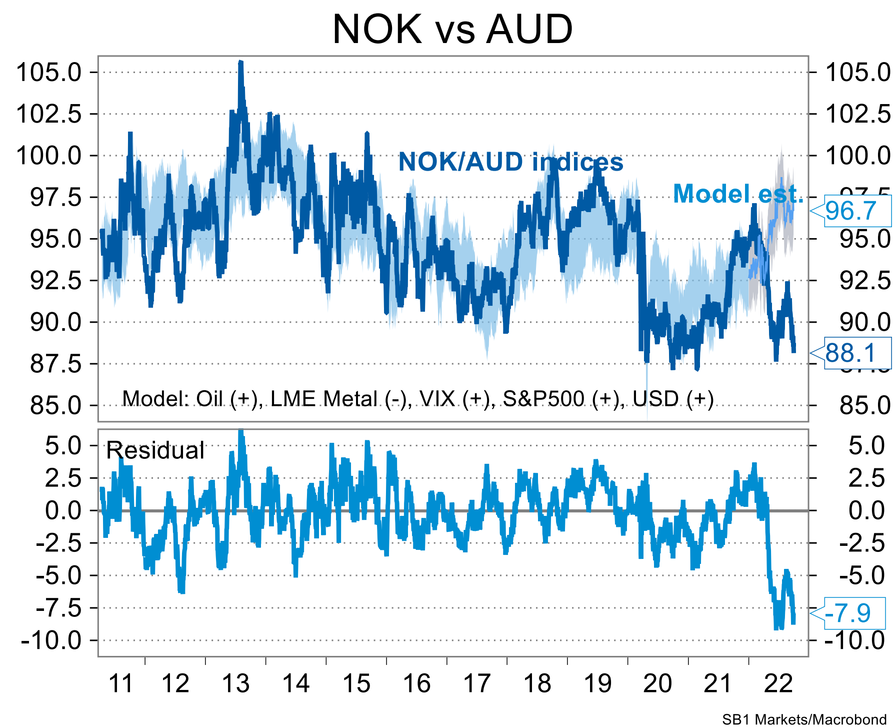


- There is no stable correlation over time, and when it is, the oil price is normally the real driver. Not so now

AUD down, NOK even more. Again.

NOK is 8% below our model f'cast vs AUD, even if the gas price is <u>not</u> included





- The discrepancy between the NOK and AUD is unusual, given the normal factors that normally has explained the limited gap between the two
- Normally, NOK strengthens vs the AUD when the oil price 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)

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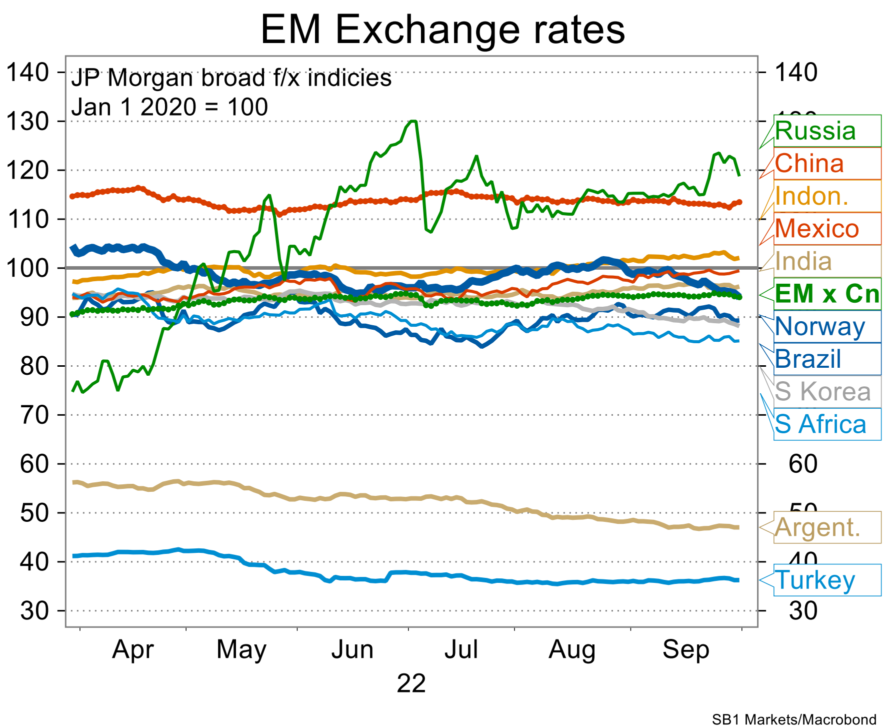
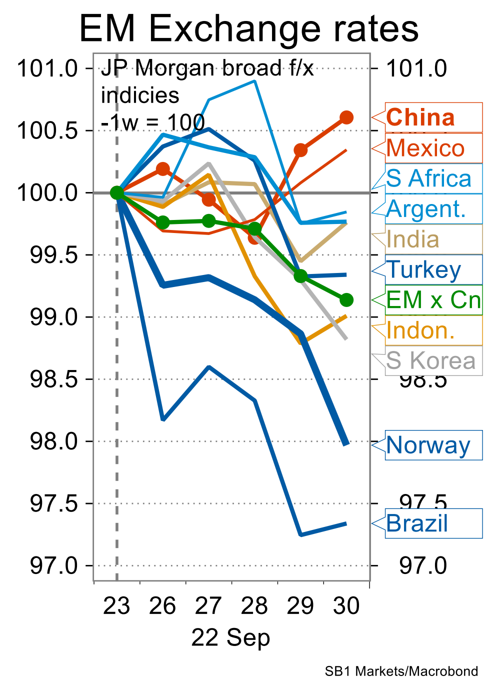
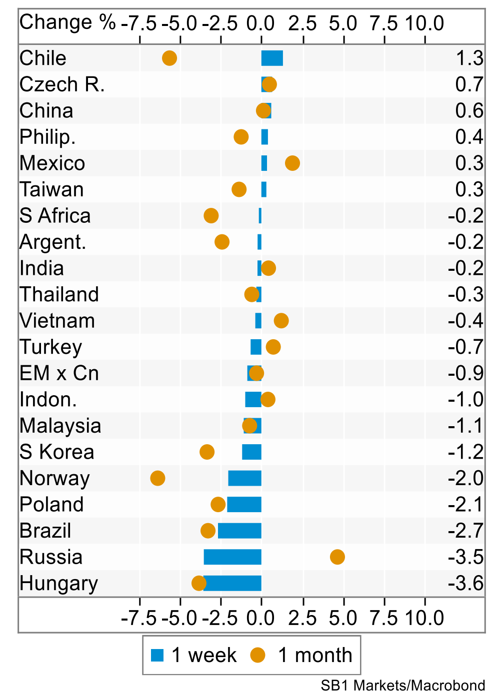
EM f/x (x China) mostly on the downside, risk off & liquidity uncertainties

Contagion to Emerging markets from a candidate member in trouble (aka UK)?







- The CNY has been slightly on the weak side recent weeks but recovered last week. The weakness vs. the USD is due to a strong USD, not a very weak CNY, trade weighted

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