November 7, 2022

Macro Weekly

Week 45

Harald Magnus Andreassen
Phone : (+47) 24 13 36 21
Mobile : (+47) 91 14 88 31
E-mail : hma@sb1markets.no

Tina Norden
Phone : (+47) 24 13 37 48
Mobile : (+47) 93 22 62 24
E-mail : tina.norden@sb1markets.no

SpareBank 1 Markets
Phone : (+47) 24 14 74 00
Visit address : Olav Vs gate 5, 0161 Oslo
Post address : PO Box 1398 Vika, 0114 Oslo

Last week, I

- **The War/European Energy/Commodities**
  - **The war** goes on and on, no end in sight. Russia re-joined the deal regarding **exports of Ukraine grains** – but food prices still rose last week
  - **European gas and electricity prices** fell further last week, all over the curve. **Other commodities** rose significantly, at least partially on hopes of an end to the restrictive Chinese Covid policy, and more investment stimulus
- **October PMIs**
  - **The global PMI** fell less than we assumed, due to a smaller decline than we expected in the Chinese surveys, as well as upward revisions from both side of the Atlantic. Still, the global PMI fell, and at 49,0, it signals just some 1% growth in the global GDP. **Rich countries** are at bottom of the list but China is even weaker. **Emerging markets x China** are still reporting the fastest growth rates. In Developed Markets, new manufacturing orders are especially weak and explains why delivery times are rapidly normalising. In the US manufacturing ISM, prices are reported down, the delivery times index is far below an average level! The service sector ISM fell but is still reporting decent growth while the service PMI still is well below the 50-line (and it is probably too weak vs. reality). The (volatile) Norwegian manufacturing PMI surprised at the upside in October, up 3 p to 53.1, but the trend is down, and other surveys are definitively at the weak side - while the Swedish manufacturing survey fell sharply, to 46.8. However, services are doing better in Sweden, and decent GDP growth is still reported
- **Auto sales**
  - **US** reported a significant lift in auto sales in October, and sales are just 12% below the 2019 level (in May it was -21%). **UK** sales rose sharply too. Sales in **EMU** probably fell marginally, following some better months. Sales are anyway down 23% vs. 2019 – and weaker demand may be an explanation. Norwegian sales is still among the best in class in the rich part of the world. More countries will report this week
- **USA**
  - **The FOMC** lifted the Fed funds rate by 75 bp, for the 4th time in row, to 3.75 – 4.00%, as everybody expected. When deciding future increases in the policy rate, the committee says it will take into account the cumulative tightening of monetary policy, the lags, and economic and financial developments, signalling that pace of tightening will slow. At the same time, Powell stated that the FOMC members believe they have ways to go to achieve a sufficient tightening, and that the terminal (peak rate in this cycle) most likely will be lifted in December, from the 4.6% f'cast given in September. The market had already discounted a 5% terminal rate (for next spring) and was not shocked by Powell's comments, but the market acknowledged that the Fed would keep rates higher for longer. Stock market disliked this signal. The market now expects a 50-bps hike in Dec (62%), the alternative being the 5th 'triple' hike (38%). Should incoming data be on strong side and/or financial markets should take another 'October' party, the Fed will hike by 75 bps, even if the rate than would be lifted close to the expected terminal rate (we assume the December dot plot (rate path) will signal 5.1% as the peak)
  - **Mixed news from the labour market**: The **unfilled vacancy rate** was expected down to 5.9% in September but ascended to 6.5%. The SMEs still report they are not able to **fill job openings**, and a significant larger share of companies planned to **increase compensation** the coming months. **Nonfarm employment** is still growing more than expected. On the other hand, employment growth is slowing, and the LFS survey reports a decline in both **participation and employment rates**, and the **unemployment rate** rose 0.2 pp to 3.7%. **Wage inflation** is slowly slowing but remains too high. **Labour productivity** was close to flat in Q3 and is <u>down</u> 1.4% y/y as lower productive (and lower paid) service sector workers returned to the labour market. Still, labour productivity was revised sharply up (following the upward revision of GDP), and **unit labour costs** were revised down. Even so, ULC are up 6% y/y, and the current rate of growth can not deliver 2% price inflation over time. That's Fed real inflation problem

Last week, II

- **China**
  - » **Exports** have flattened, at a very high level – due to weaker demand from the West. **Imports** are well down from the peak but has stabilised recent months. The trade surplus remained at a very high level in October
- **EMU**
  - » **October CPI** 'surprised' sharply on the upside (but that was now surprise after country data were published late the previous Friday). The 10.7% headline, 5.0% core rate are is anyway really bad news, for the economy as for the ECB. Inflation is broad, if not as broad in the US, as energy explains much more of the headline rate of inflation in EMU than in the US. <u>In addition, the underlying inflation machine (the Unit Labour Cost) is up a tad more than in 2% in the EMU, 1/3 of the rate in the US</u>!
  - » **Q3 GDP also** 'surprised' on the upside (but that was no surprise after country data were published the previous Friday), up at a 0.7% (annualised) pace, expected 0.4%. Germany surprised most at the upside. However, surveys do not signal a strong Q4, to put it mildly
  - » **Unemployment** remained at 6.6%, the lowest level since early 80s, as the number of unemployed fell further
- **UK**
  - » **Bank of England** hiked the bank rate by 75 bps to 3.00%, as expected. The bank expects the economy to fall into a recession, but inflation is far too high, also due to domestic factors. However, the bank signalled that the market's expectations were too aggressive – but the FRAs did not respond but the GBP fell again
- **Norway**
  - » **Norges Bank** lifted the signal rate by 25 bps to 2.5%, as we and some ½ of the economists expected. We assumed the market was more positioned for a 50-bps hike but market responses in the short end of the curve were muted – and the 3 NIBOR rose sharply, which could only be explained by a much wider NIBOR spread. The bank signalled that another 25-bps hike was on the table for the December meeting, which we also think is the most likely outcome. The current Dec 3 FRA at 3.53% must be a good investment
  - » **Home prices** fell 0.8% in October, well below our -2% forecast (but an 0.3 pp upward revision of the Sept decline to 0.9% reduced the distance vs our expected price level in Oct). Prices are now declining in a large majority of cities, the most in Oslo (-1.9%), where the debt level is the highest. The inventory of unsold homes have shot up twice as fast over 4 moths as anytime before, and faster than ever m/m also in October. Market flows indicate a further and large decline in prices, especially in Oslo
  - » **Credit growth** was lower than we expected in October, up 5.1% y/y, as the Mainland corporate sector reduced its debts, though following the unprecedented surge in September. The trend for households is marginally downwards – and we expect more to come, as signalled by the lending survey and the surge in mortgage rates

The (short) Calendar: US CPI & election. Chinese credit & CPI. Norwegian CPI, vacancies

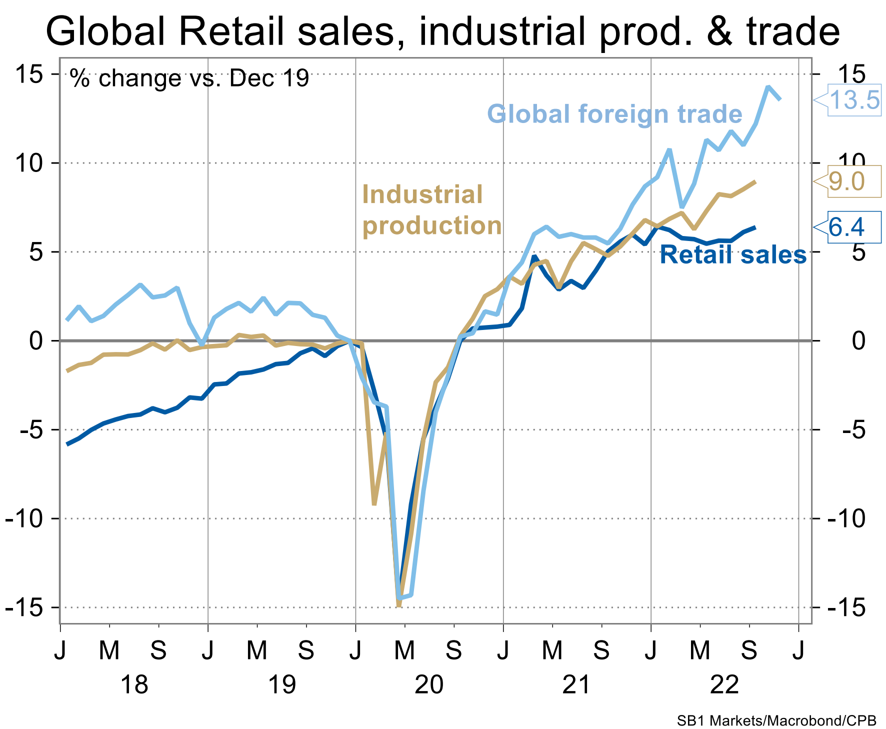
Time	Count.	Indicator	Period	Forecast	Prior
Monday Nov 7					
08:00	GE	Industrial Production SA MoM	Sep	0.2%	-0.8%
08:00	NO	Ind Prod Manufacturing MoM	Sep	(0.0%)	-1.0%
21:00	US	Consumer Credit	Sep	$32.5b	$32.2b
Tuesday Nov 8					
06:00	SW	House Prices, Maklarstatistik			
11:00	EMU	Retail Sales MoM	Sep	0.4%	-0.3%
12:00	US	NFIB Small Business Optimism	Oct	91.5	92.1
Wednesday Nov 9					
02:30	CN	PPI YoY	Oct	-1.6%	0.9%
02:30	CN	CPI YoY	Oct	2.4%	2.8%
08:00	**NO**	**Unfilled vacancies**	**Q3**	**(3.2%)**	**3.4%**
10:00	NO	Norges Bank Financial stab. rep.			
13:00	US	MBA Mortgage Applications	Nov-04		-0.5%
Thursday Nov 10					
08:00	**NO**	**CPI YoY**	**Oct**	**7.1%(6.3)**	**6.9%**
08:00	**NO**	**CPI Underlying YoY**	**Oct**	**5.5%(5.5)**	**5.3%**
14:30	US	CPI MoM	Oct	0.6%	0.4%
14:30	US	CPI YoY	Oct	8.0%	8.2%
14:30	US	CPI Ex Food and Energy YoY	Oct	6.5%	6.6%
14:30	**US**	**CPI Ex Food and Energy MoM**	**Oct**	**0.5%**	**0.6%**
14:30	US	Initial Jobless Claims	Nov-05	220k	217k
20:00	US	Monthly Budget Statement	Oct		-$429.7b
Friday Nov 11					
08:00	UK	Monthly GDP (MoM)	Sep	-0.4%	-0.3%
08:00	UK	GDP QoQ	3Q P	-0.5%	0.2%
08:00	UK	Manufacturing Production MoM	Sep	-0.8%	-1.6%
16:00	US	U. of Mich. Sentiment	Nov P	59.5	59.9
During the week					
	CN	Aggregate Financing CNY	Oct	1600b	3530b
	CN	New Yuan Loans CNY	Oct	800b	2470b

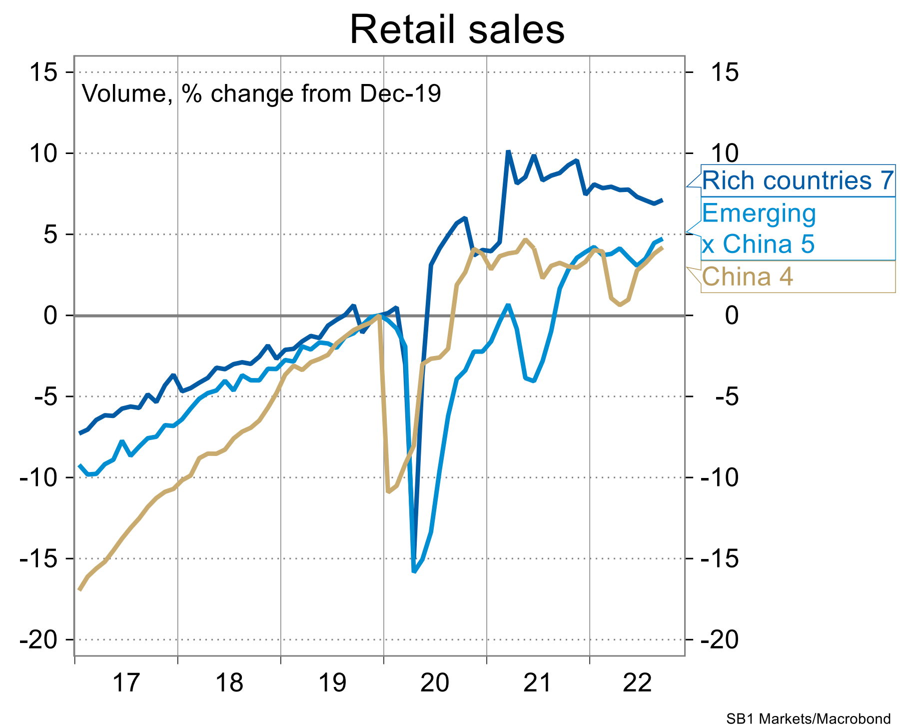
- **China**
  - » **Credit growth** has slowed somewhat past 3 months, as local governments have borrowed less than during the previous months. The central government has 'ordered' local governments to borrow more to fund infrastructure investments and housing projects that have run into trouble, while at the same time trying to prevent local government from 'selling' property to their investment vehicles, and letting these 'invisible' companies borrow. Local governments are struggling because an important income source, sale of publicly owned land, has fallen sharply as construction starts have nosedived by more than 50%. **CPI and PPI** are also reported
- **USA**
  - » **CPI monthly inflation** is expected to remain very high in October too, even if raw material prices are falling, alongside used car prices. Rents are still on the way up, and food prices have not yielded. Gasoline prices rose slightly in October, following the decline in Sept. A core rate at 0.5% m/m is way above Fed's ambitions (0.2%) – and the annual growth rates are extremely high
  - » … and that's why the **Democrats** will lose their majority in the **House** and possible even in the **Senate** at Thursday – and Biden will become a lame duck the last two years of his presidency
  - » Atlanta Fed's median wage tracker slowed marginally in September but is still reporting high wage inflation
- **EMU**
  - » **Retail sales** surprised on the upside in September but the outlook is not the best
- **UK**
  - » **September and Q3 GDP** are both expected down, the latter at least partly due to the Queen's funeral. Bank of England expect a further contraction, and for real, the next quarters
- **Sweden**
  - » The first, broad October **house price** indicator, from the realtors, is out this week. According to this index, prices rose slightly in Sept. It will surprise us if prices did not turn down again in Oct
- **Norway**
  - » We expect the **headline CPI** to decline substantially due to the decline in electricity prices in October, to 6.3% from 6.9% in September. (Electricity prices have been very low so far in November as well). However, **core price inflation** very likely moved in the opposite direction, we expect 5.5% vs. 5.3% in September, even if our m/m estimate is modest, up 0.3% seasonally adjusted
  - » Look up for the **unfilled vacancy statistics**! The rate rose further in Q2, but during Q3, the number of new vacancies fell somewhat, and we expect the unfilled vacancy rate to decline moderately – and thus remain at a very high level

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

Retail sales up in September, due to Emerging markets – and even rich countries

Industrial production rose as well. Recent global trade data may be too upbeat?



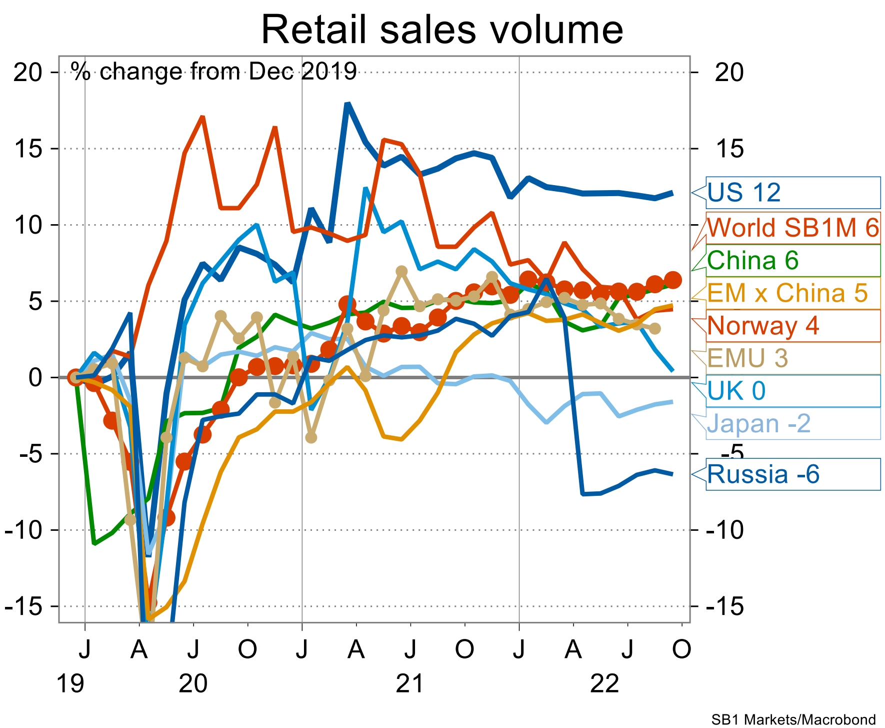


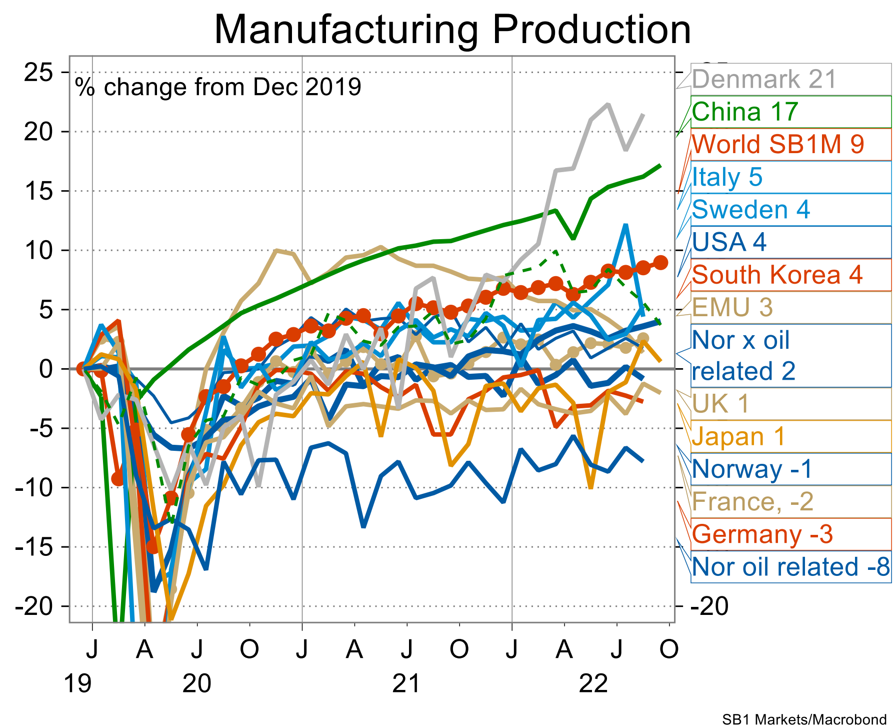
- So far, not all countries have reported September data, so these are our final estimates

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.

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

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

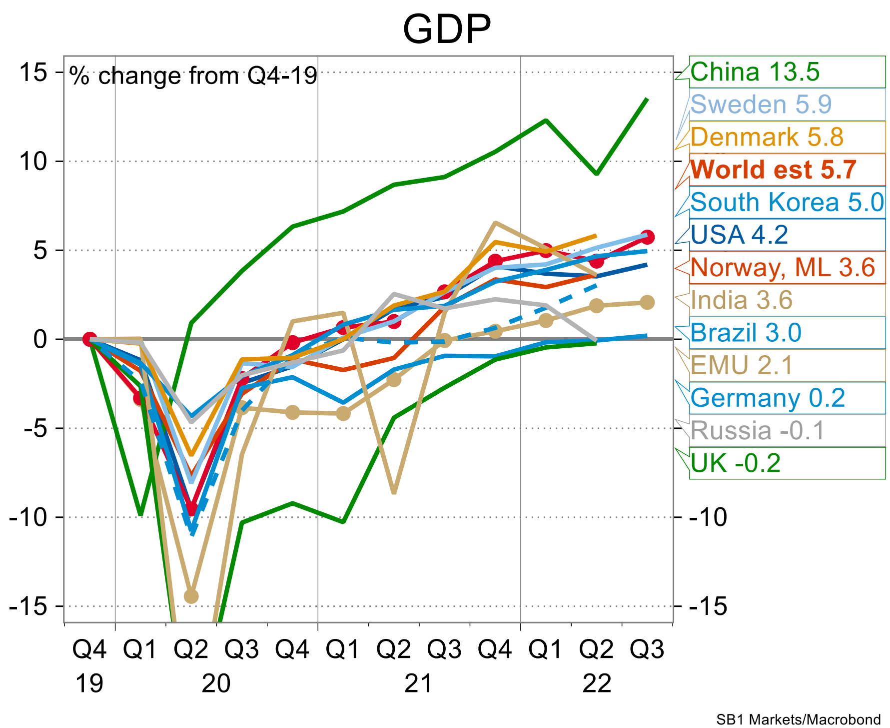


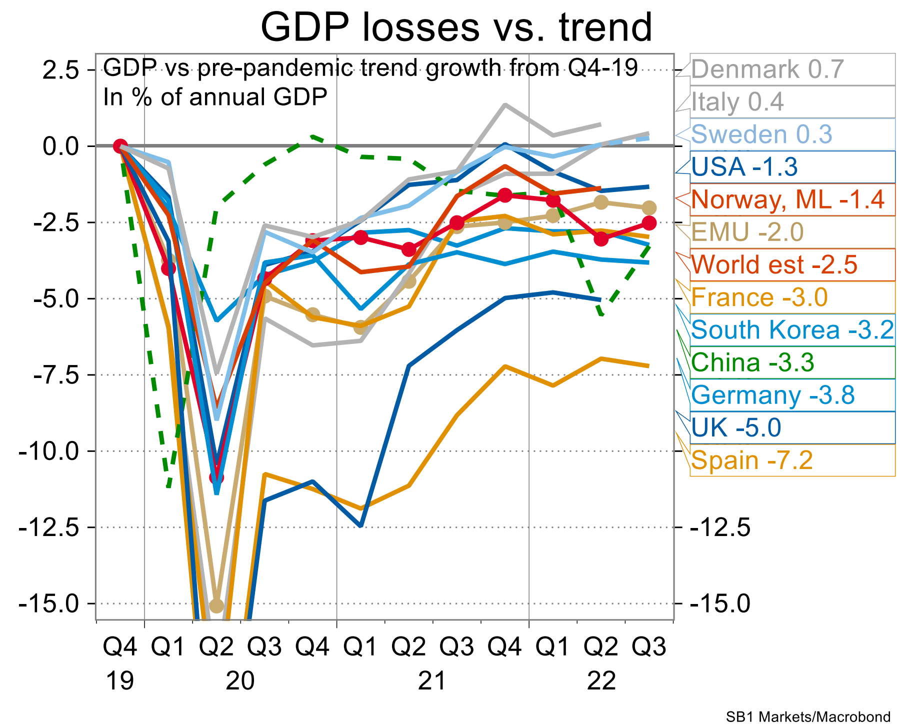


US retail sales: Personal consumption of goods, ex auto & energy

Global GDP recovered in Q3, mostly thanks to China, but with help from the US

… and the EMU! Up 1.3%, from -0.6% in Q1. Global GDP is still 2.5% below the pre-pandemic trend path

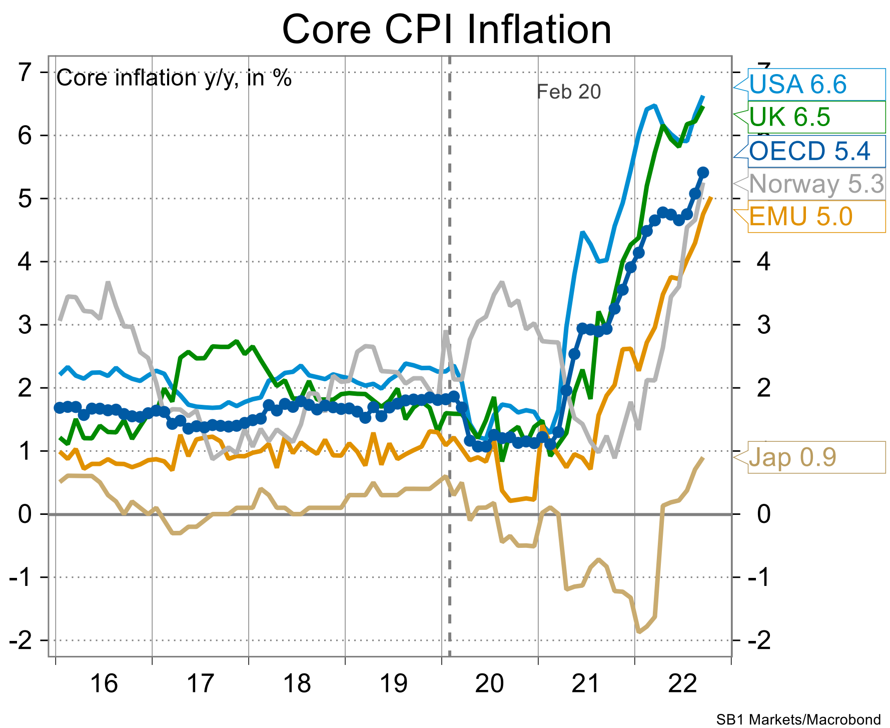


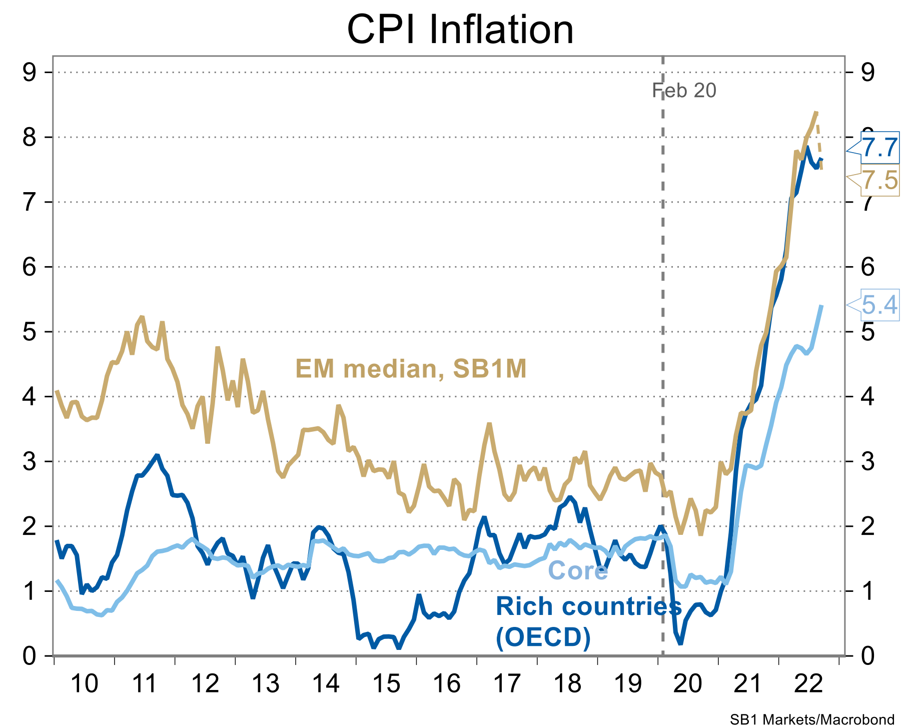


- … even if unemployment, at least in the rich part of the world is ‘zero’, and employment rates are record high almost everywhere
- Most countries have not yet reported Q3 data

Peak inflation? Data are not that obvious anymore

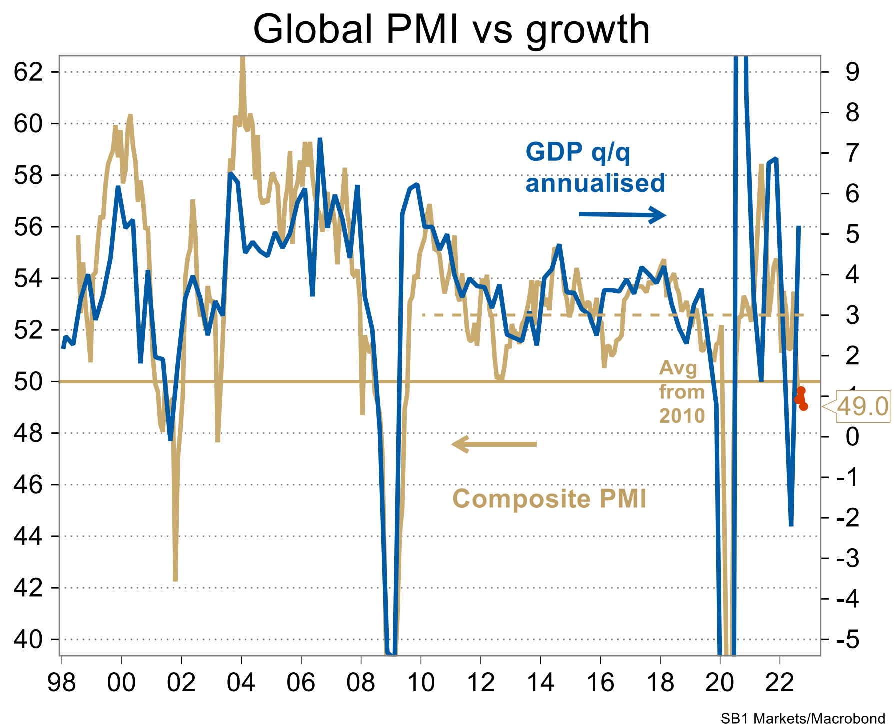
The going rate is 8% headline inflation, and 5% core inflation, and the latter is still on the way up

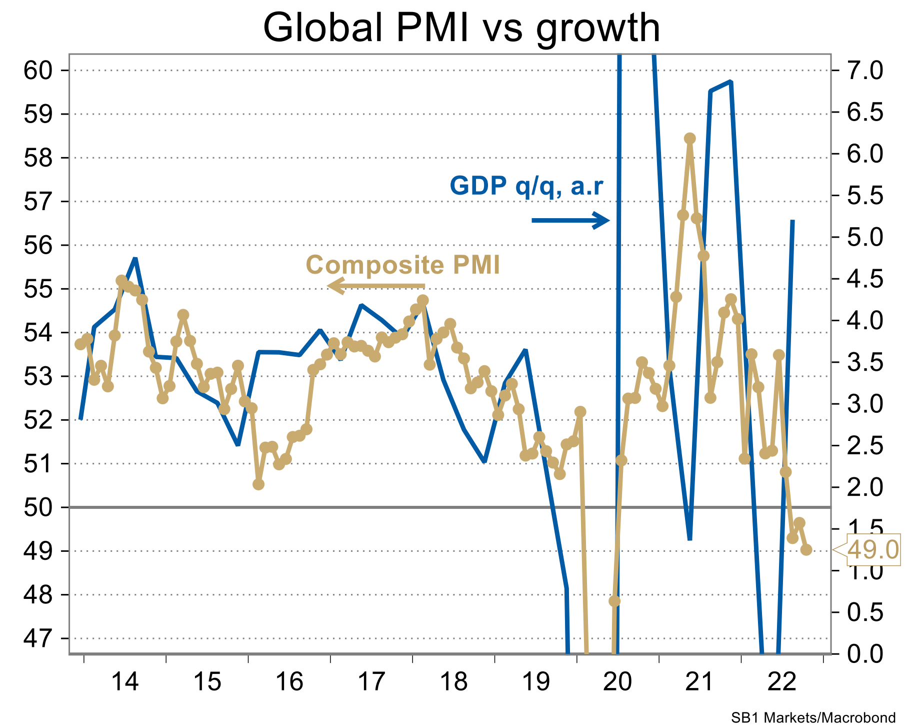




The global PMI down in October, signals just some 1% global GDP growth

The global index fell by 0.6 p to 49.0, we expected -1 p. Both manuf. & services slowed further

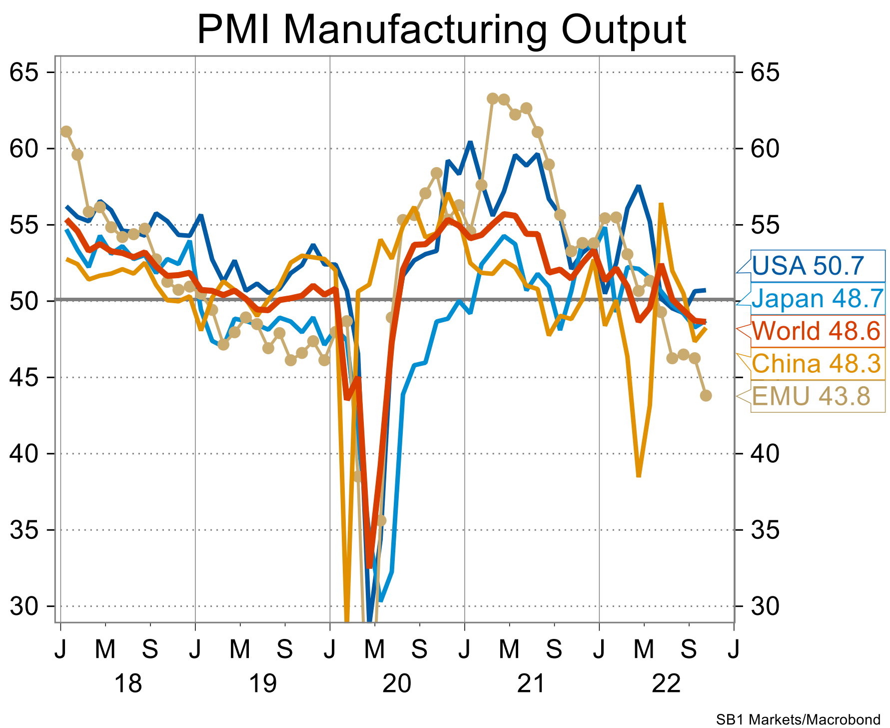


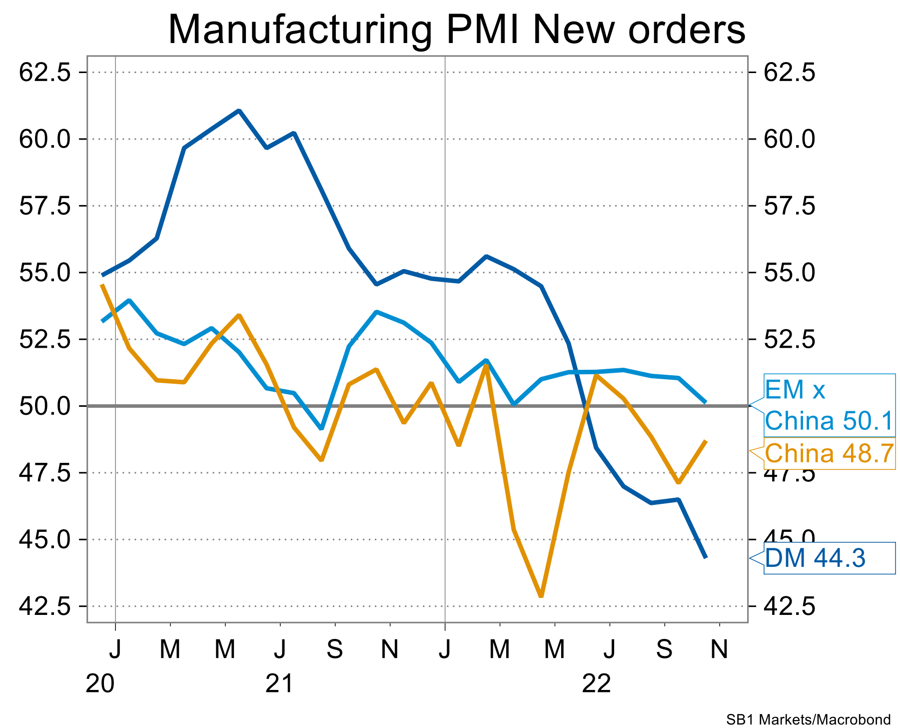


- The composite PMIs are weak in the US (S&P/Markit), the UK, and in the EMU as well, while Caixin's China PMI fell less than we assumed – but remains well below the 50-line
- The German index is at the bottom of the league, as both the manufacturing and the service sector PMIs are very weak.
- The US S&P PMIs are below par too; the ISMs is in sum far better, due to the service sector ISM
- New orders are weak across the EMU, and are declining the US as well

New orders and output are slowing in developed markets; not in EM x China

European manufacturers report an steep decline in new orders, taking the DM average down

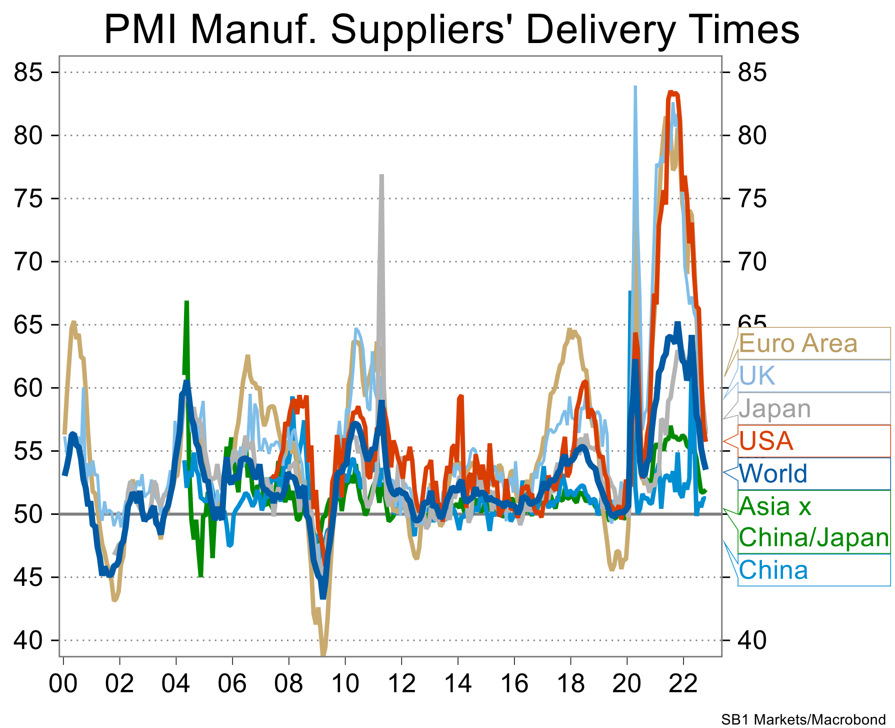


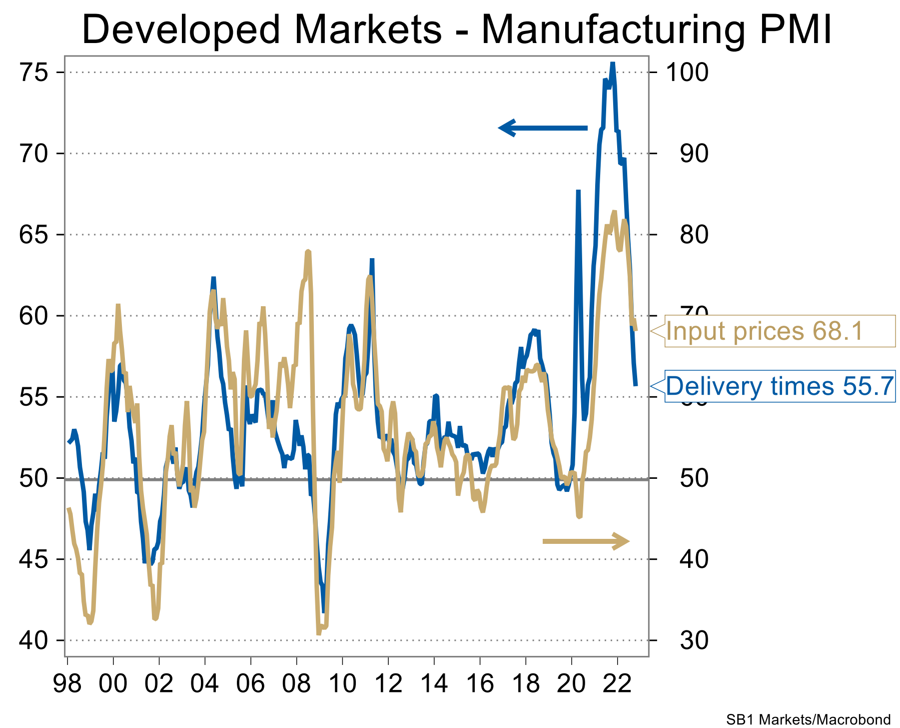


- The US index has stabilised recent months, are is still above the 50-line

SpareBank 1 MARKETS

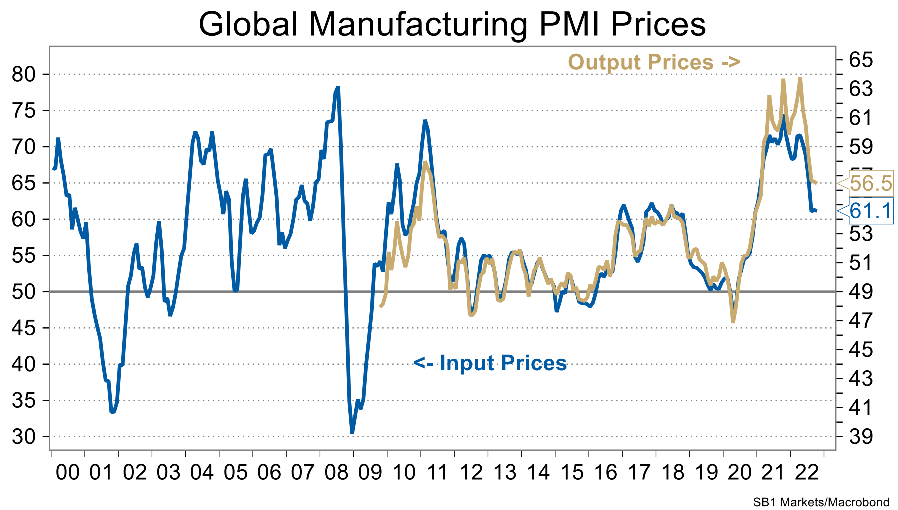
Delivery times and price indices are coming down rapidly, both still above avg.

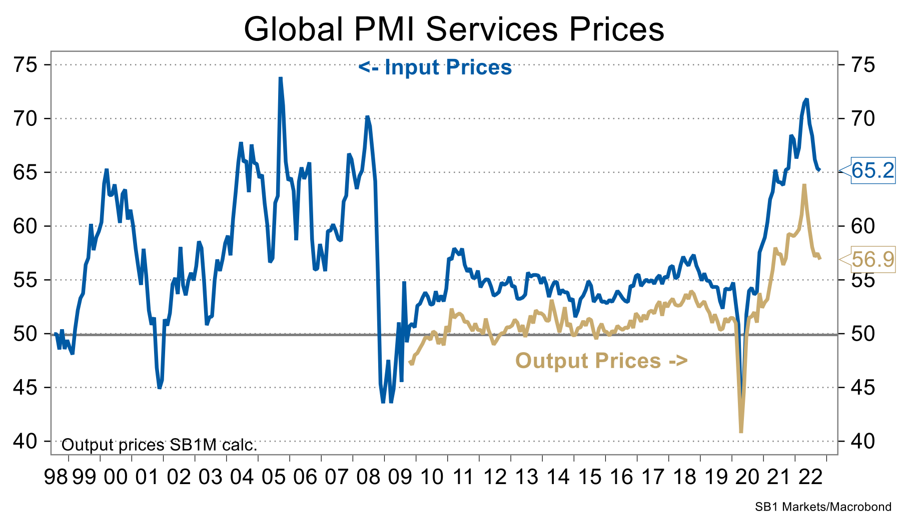


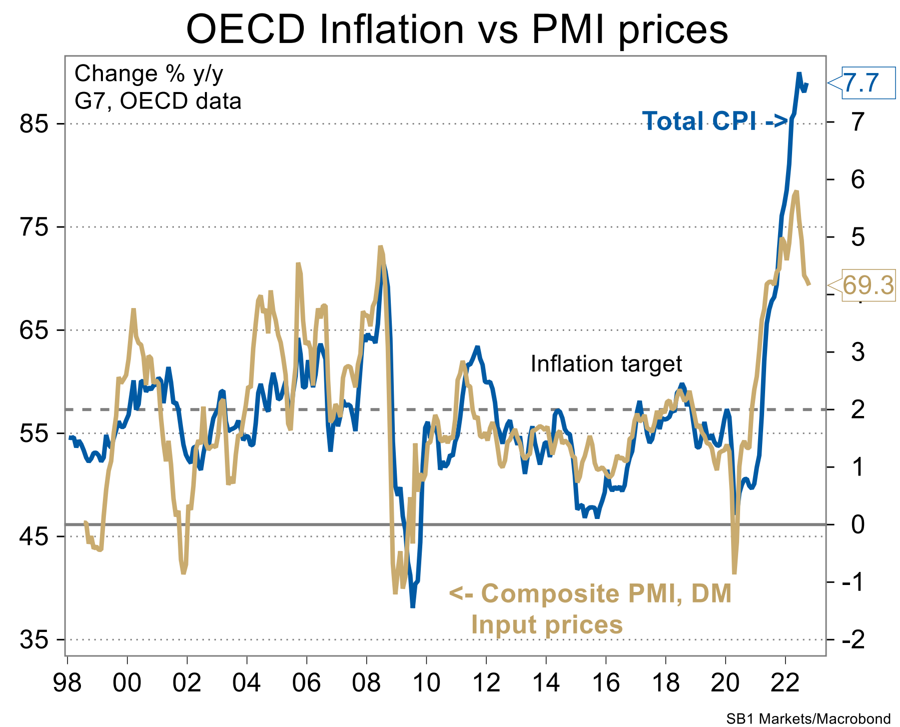


Price increases are slowing, according to the PMIs

All price indices remain at high or very high levels though (like service sector input prices)

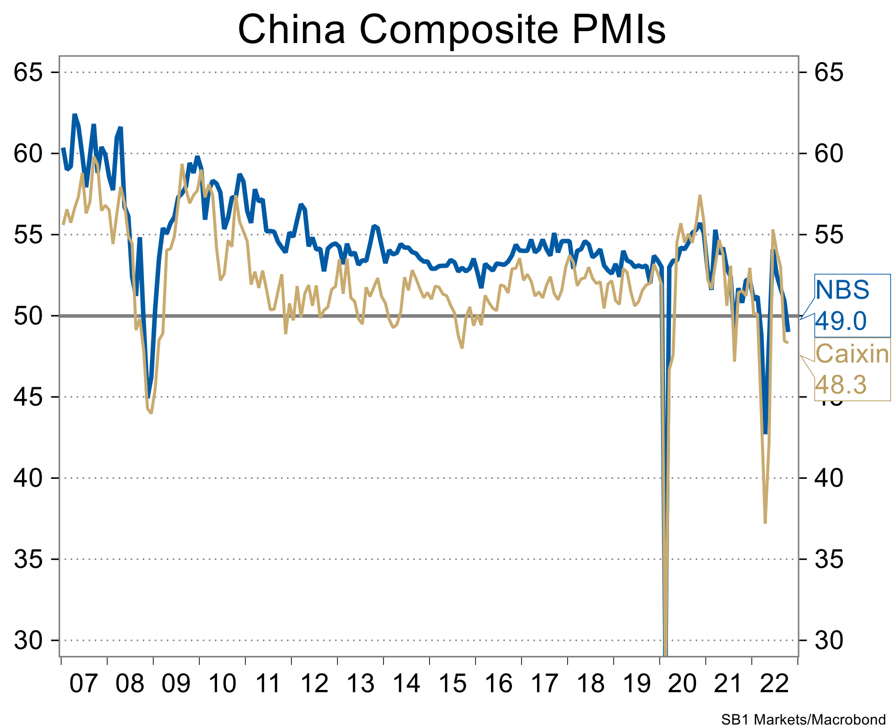


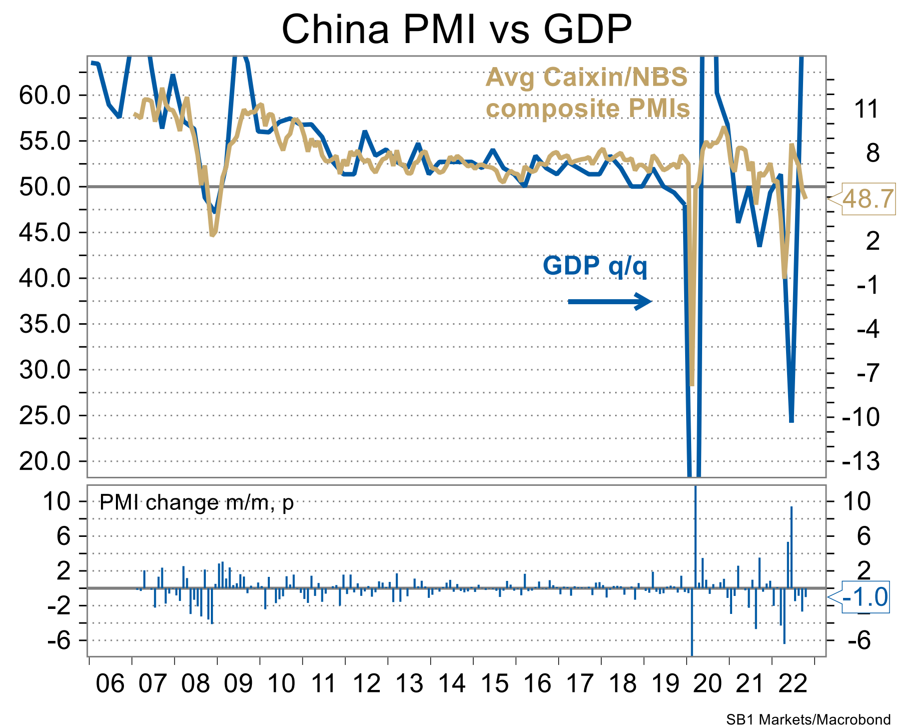




Both PMI data sets down in October – services the main drag

In sum, the PMIs signal modest growth in Q4

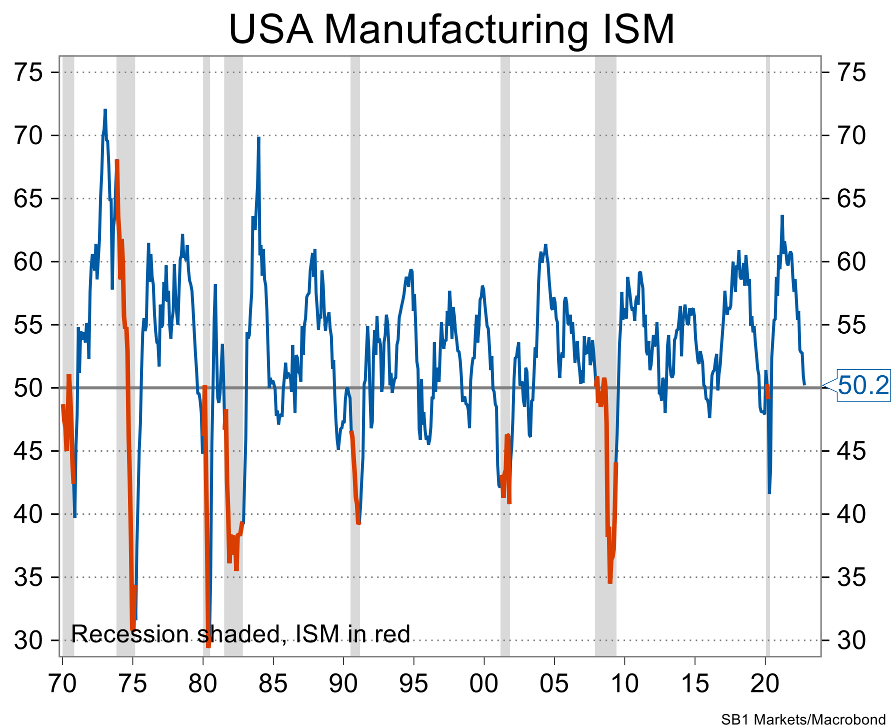




- **GDP** recovered from the weak lockdown Q2, and better than expected in Q3. The October PMI signals far lower growth in Q4
- The **Caixin composite index** fell by 0.3 p to 48.3, expected up 0.4 p. Services surprised on the downside
- The **NBS/CFLP composite PMI** fell by 1.9 p to 49.0, expected just marginally down. The service sector reported a further slowdown to well below trend growth. The manufacturing PMI sector also fell below 50 in October

The manufacturing ISM fell further in October, but details not that bad

The index fell 0.7 p to 50.2, expected 50, and the survey remain stronger than other manuf. surveys



The **ISM manufacturing survey** confirms a gradual slowdown in the US economy, but not as much as the average (and median) of other surveys

- In October, 8 of 18 manufacturing sectors reported **growth** (down from 9 in Sept), 10 sectors reported a decline (up from 7)
- The **new orders** index was up 2.1 p, even if exports orders fell faster. The total new orders index remained contractionary territory at 49.2. 12 of 18 sectors reporting declining orders, which is one less than last month, but still very weak. Other surveys agree. The **order backlog** is also declining rapidly
- The **production** index rose 1.7 p to 52.3, which is slightly below an average level. The **employment** index rose 1.3 p to 50 in October, after falling 5.5 p in September. Labour demand is still softer than at the peak and the ISM reports that more companies are implementing hiring freezes
- So why did the total index decline? The **delivery times** index fell sharply, by 5.6 p to 46.8 as **supply chain** issues are dissipating: 9 commodities saw **price increases** (from 15 last month and 40 in May, and 56 at the peak). 17 were down in price, like aluminium, steel, and lumber. This is up from 16 in September. 9 commodities were reported in **short supply**, up from 7 in Sept (but far below the peak at 50 commodities a few months ago)
- In addition, the **inventory** index fell 3 p, which is not necessarily bad news. Taken together, deliveries and inventories lowered the ISM total index by 1.7 p. The order components contributed on the upside
- The input **price** index fell sharply to 49.4, signalling falling prices!
- **Comments** are mixed – many are still reporting that labour is a scarce commodity, but several are acknowledging a slowdown in demand, and that competition is increasing

SpareBank 1 MARKETS

A warning sign: At the current pace of contraction in new orders…

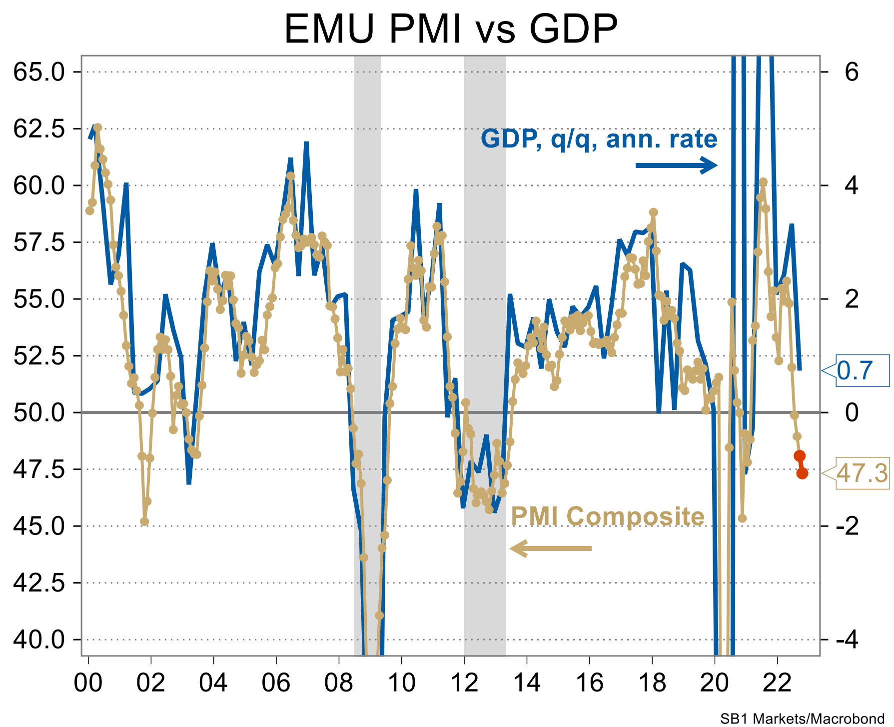
…a recession usually follows. The '95 soft landing is the only exception.

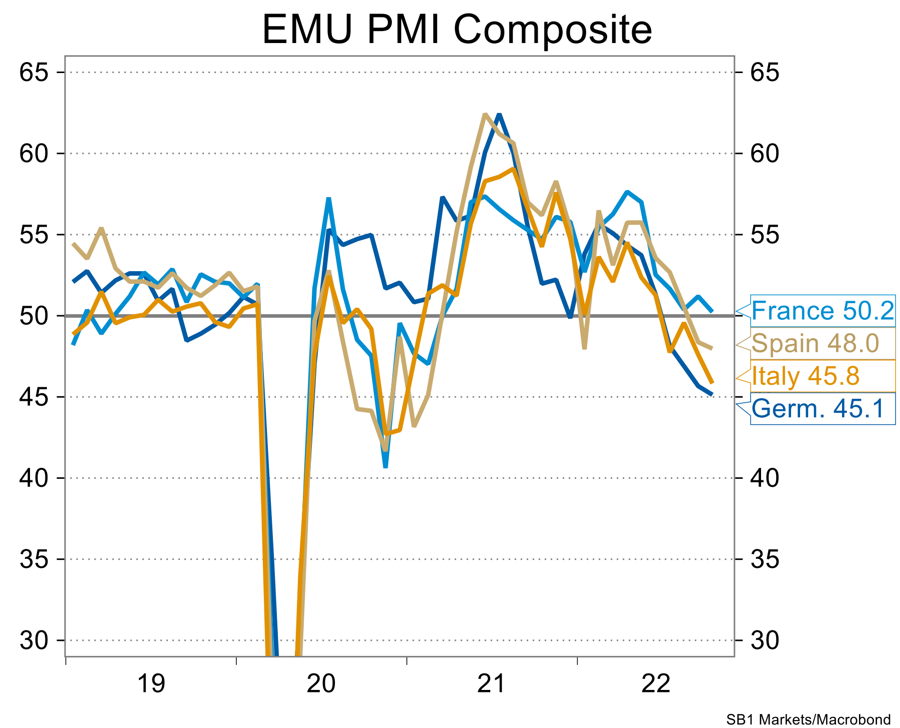
The other 6 contractions are the past 6 recessions

SpareBank 1 MARKETS

The Eurozone final PMIs confirmed in contractionary territory, but no full crisis

The composite down 0.8 p to 47.3; data weaker everywhere but the German & Spanish service sectors

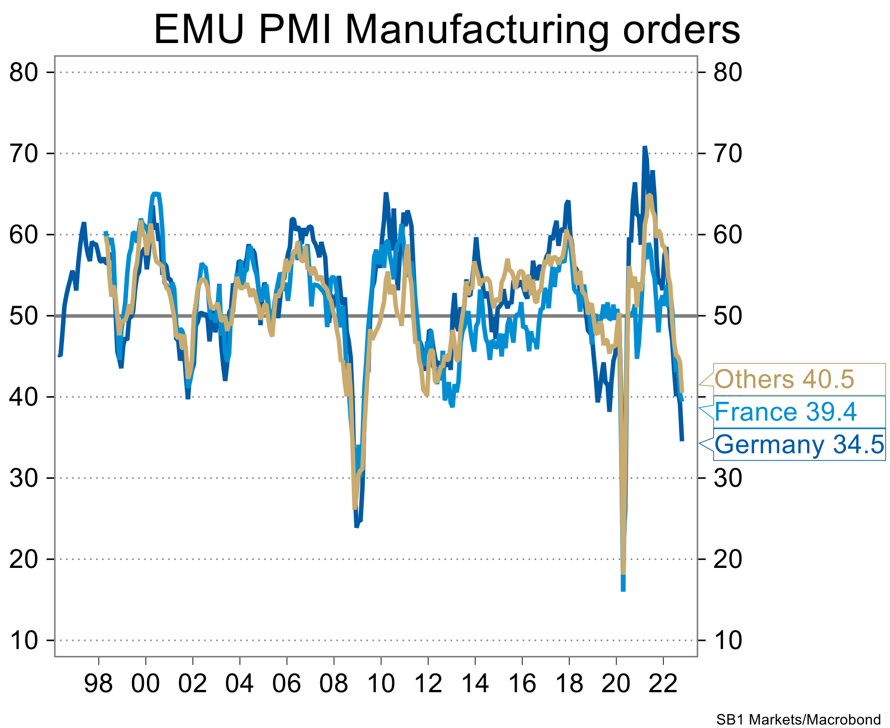


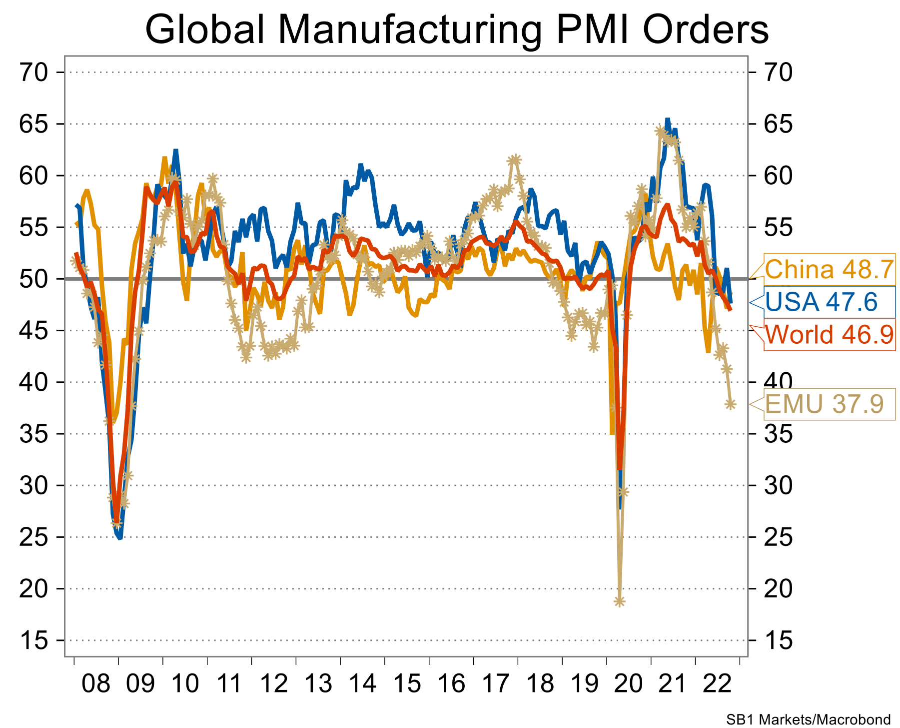


- The EMU composite PMI was 0.2 p higher than the flash estimate, but down from September. The Italian service PMI, and the German and Spanish manufacturing PMIs fell the most. However, the French and German service sector PMIs were stronger than initially reported. Apart from France, the PMIs are all weak though
- The **service PMI**, **manufacturing PMI** and the **manufacturing output** index all fell in October
- The sum of the parts for the Eurozone points to around a 1% contraction in GDP. In Q3, GDP grew 0.7%
- The October PMIs, like the previous month, bear sign of higher energy costs and higher interest rates, as well as lower global demand, as demonstrated by the lower new order indices, also from export markets

European new orders are falling very rapidly

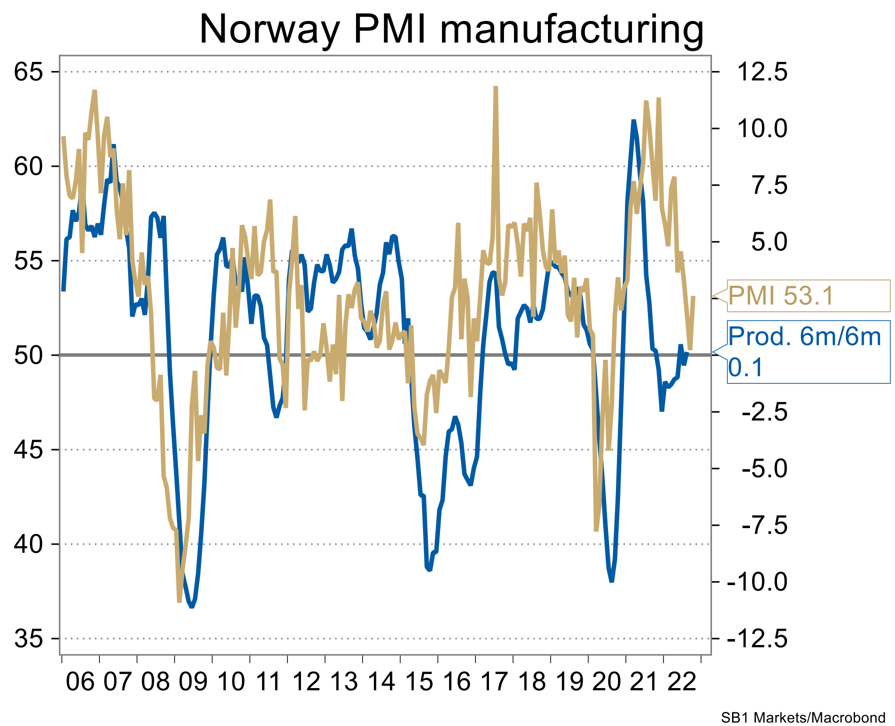
No doubt, the manufacturing sector in EMU is heading for a deep downturn, Germany in the lead

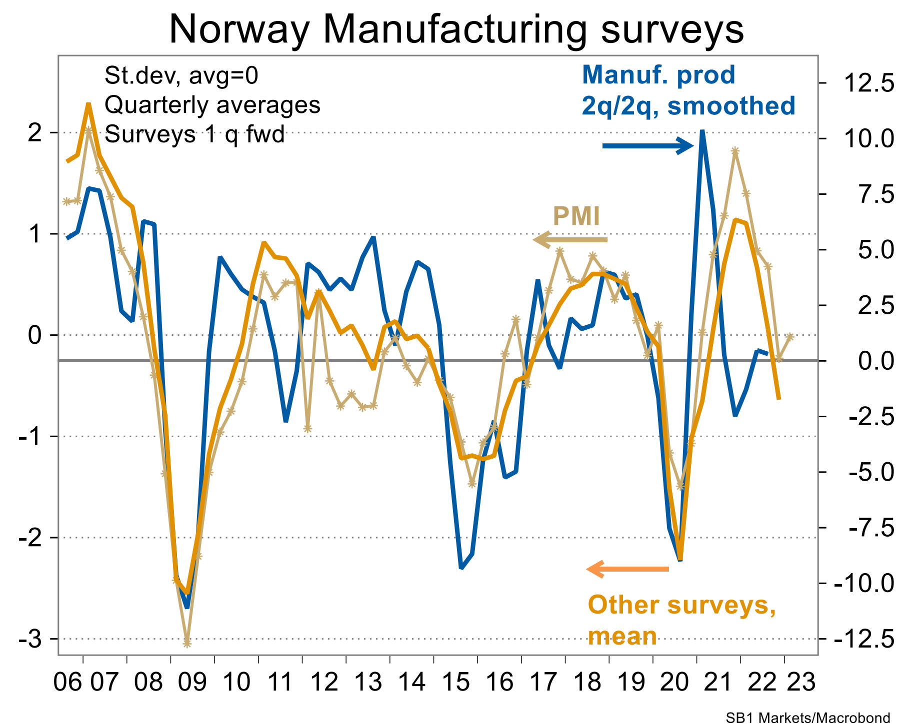




The volatile Norwegian manufacturing PMI up in Oct – all sub-indices stronger

Production, orders, employment all increased, so did delivery times, while inventories decreased



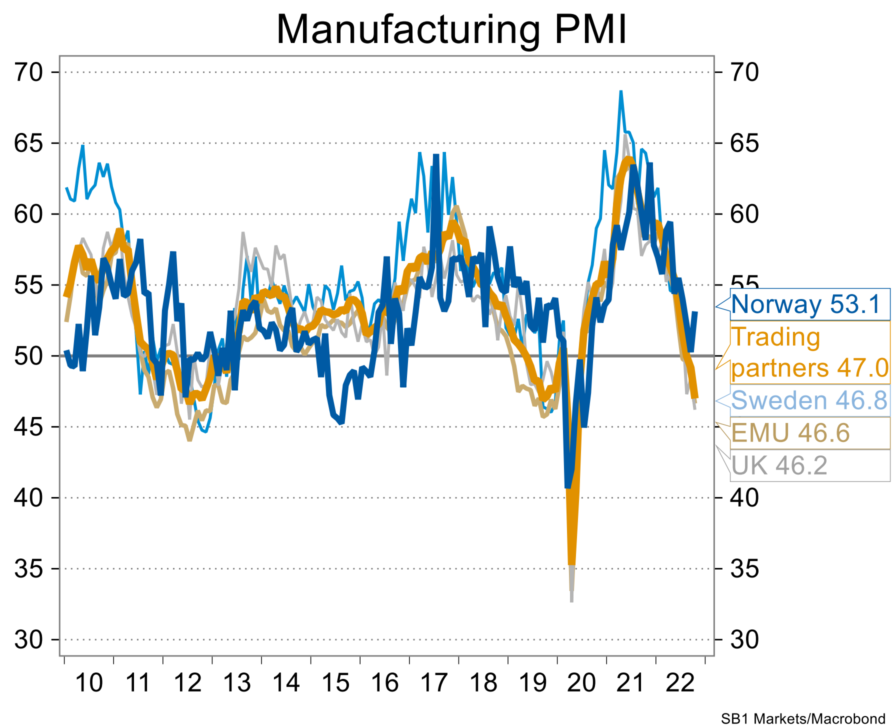


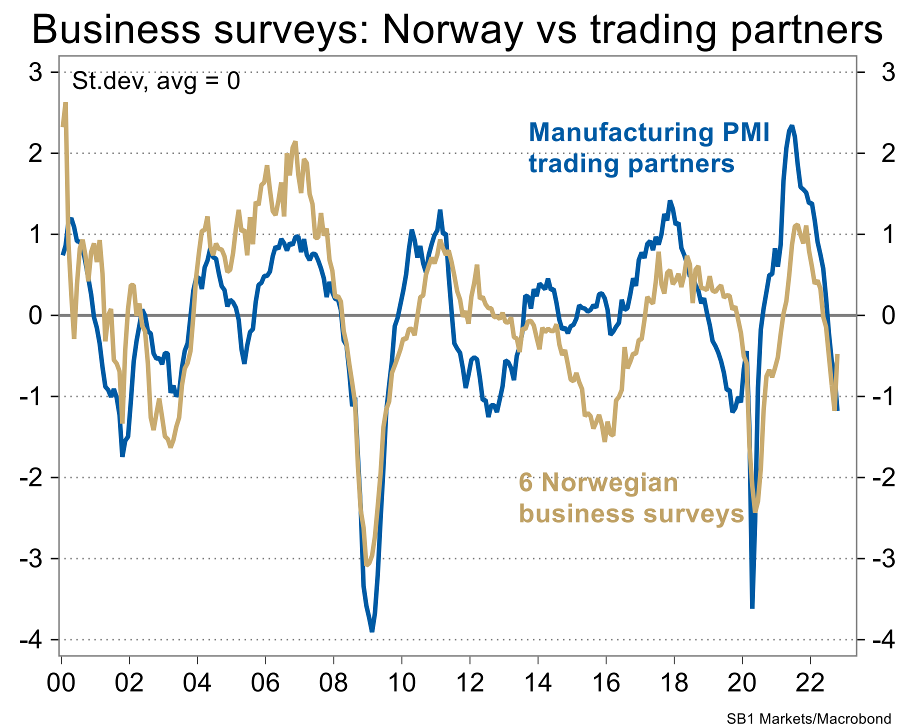
- The **manufacturing PMI index** rose 2.9 p to 53.1 in October (September was revised up by 0.3 p), but the trend is down
- Other **manufacturing surveys** on the other hand are on the weak side, like the SSB survey, NHO and Norges Banks' Regional Network
- **Actual production** has been trending down since early 2021, and has – at best – stabilised recent months (September will be reported today)

SpareBank 1 MARKETS

Norwegian manufacturers normally follow the rest of the world

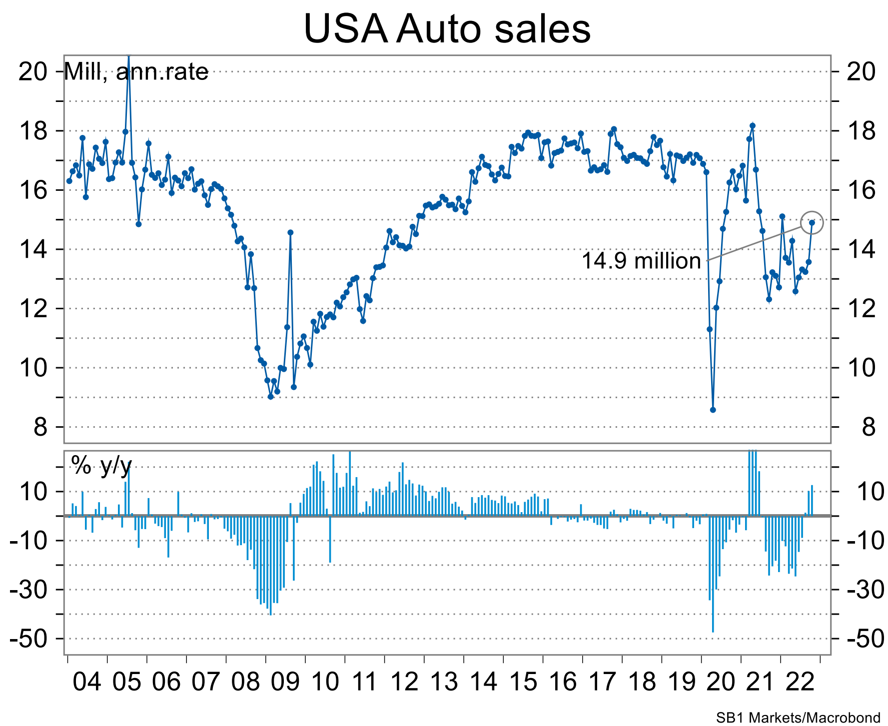
The October observation is odd, right?

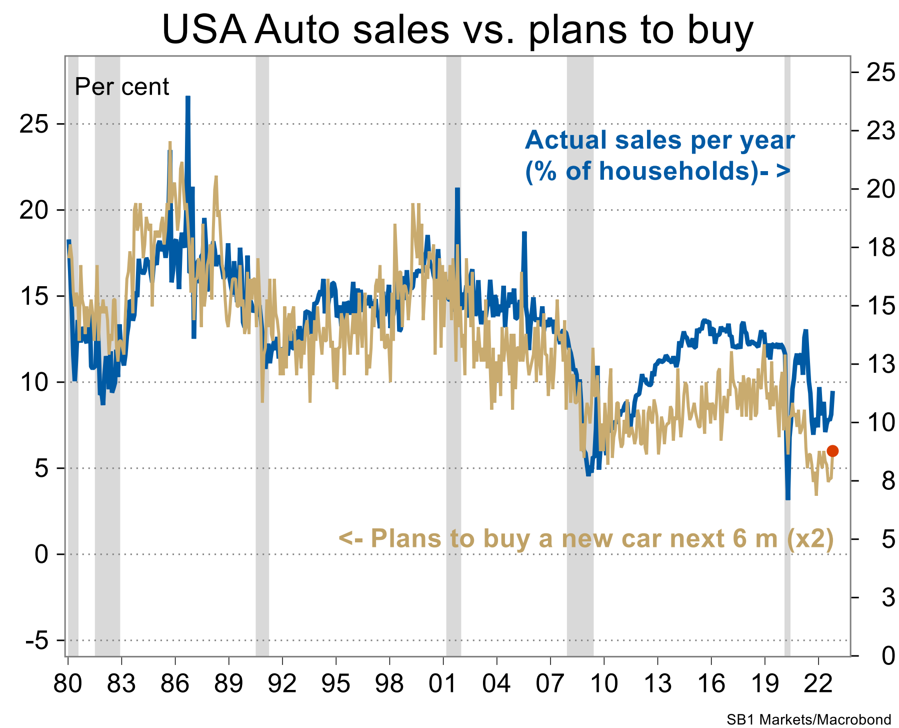




US auto sales sharply up in October, as delivery problems eased

Sales up 13.6 mill to 14.9 mill, 0.4 mill above expectations – and 'just' 12% below the 2019 average

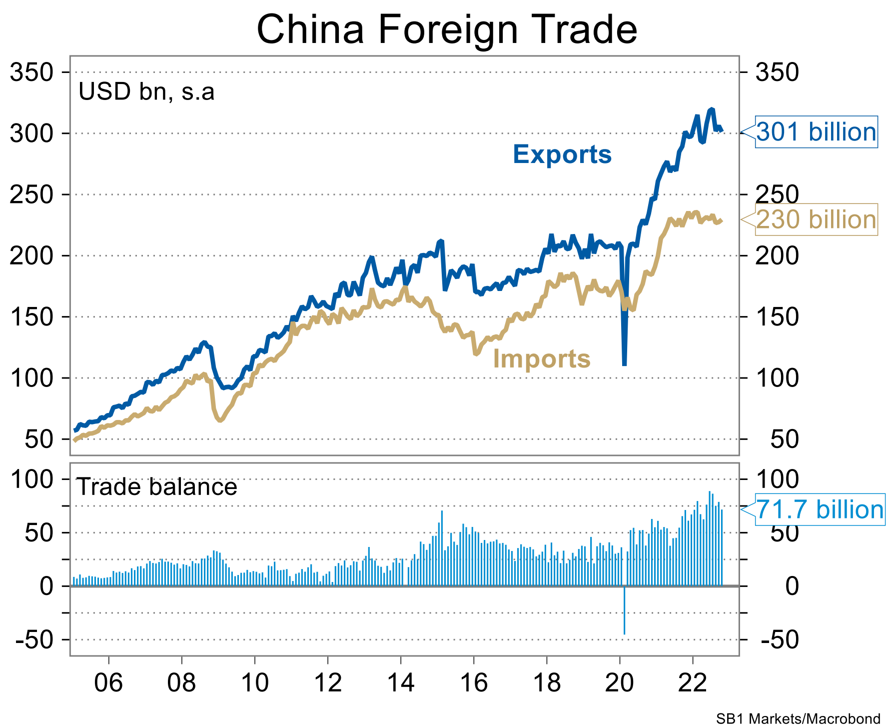


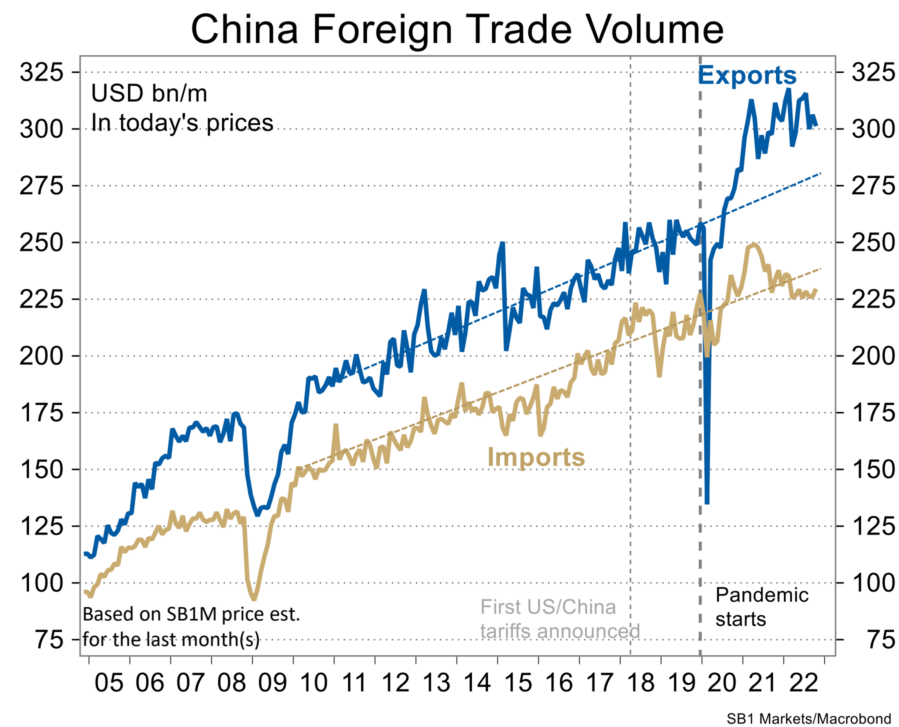


- Plans for buying a new car has been stable at a record-low level over the past year – but has bottomed
- Some demand slowing: Prices for second hand cars are declining rapidly and inventories of new cars are increasing

Exports are flattening, at a very high level, imports are trending slowly down

Exports down 2% m/m in Oct, imports up 1%. Exports flat y/y (exp +4.5%), imports -1% y/y (exp. flat)

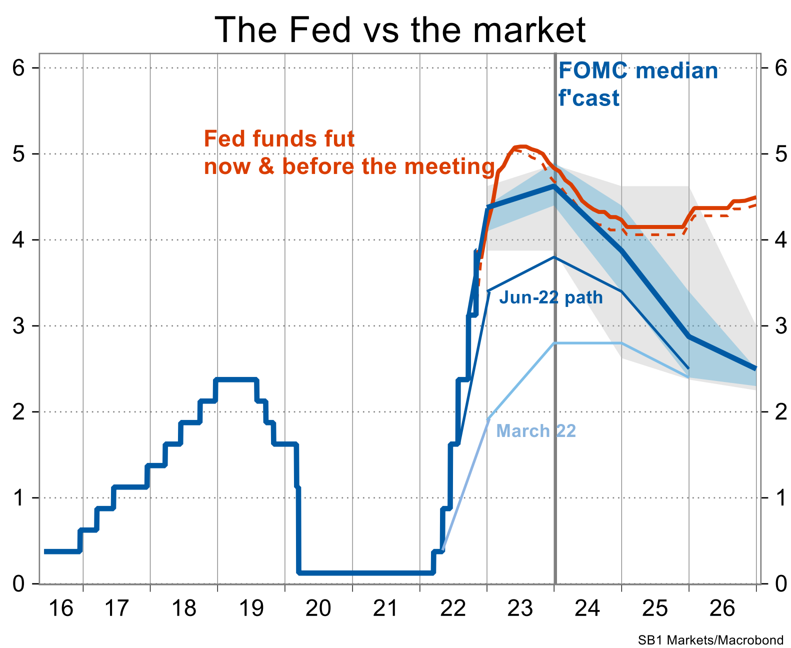




- In volume terms, we assume small changes m/m in October, exports marginally down, imports slightly up (no price indices available yet)
- Exports have more or less flattened recent months following the impressive surge through the pandemic – no supply chains issues to be seen. The current flatting corresponds with flattening demand for goods in the rich part of the world
- Imports have been trending slowly down, in volume terms, and significantly in volume terms, since April 2021 – we assume due to lower domestic demand, both due to weak retail sales and the decline in construction activity. The former has probably been hampered by Covid restrictions. However, since March, import volumes have flattened
- The trade surplus remains very high – and not far below ATH

Another 75 bps now, and the 'terminal rate' will be higher, but the pace will slow…

… at some point, or "in the next meeting or the one thereafter", as Powell said

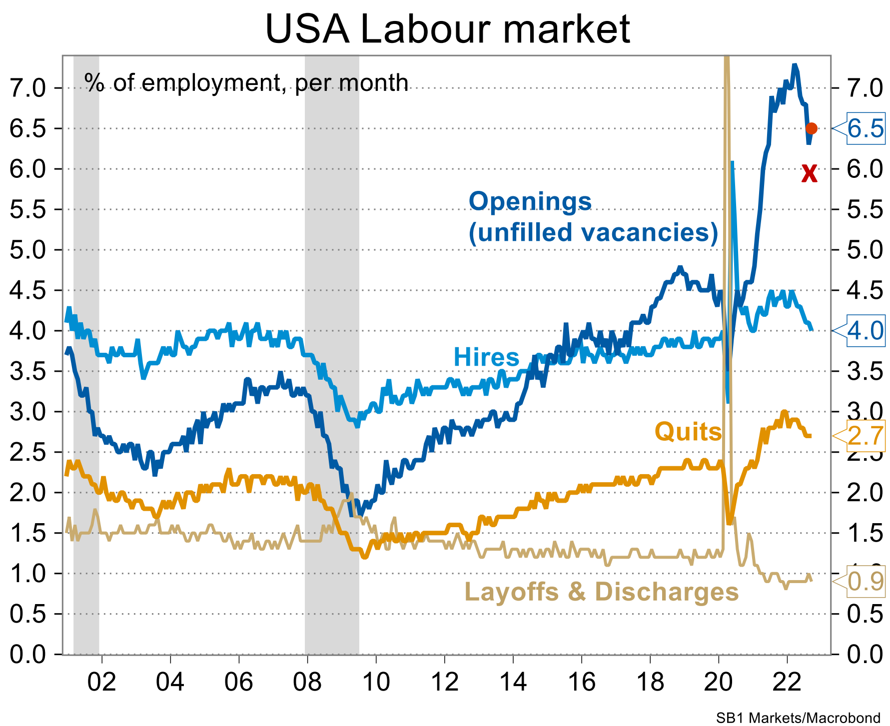


- **Market reactions: Volatile, and mixed**
  - The short end of the curve ended marginally up, as did the long end of the curve
  - Still, equity markets fell sharply, as Powell sounded more hawkish than the press release?

- As expected by the market and previously communicated, the FOMC hiked the **Fed funds rate by 75 bps to 3.75% – 4.00%**
- In the statement, the bank said that the terminal rate will be higher than previously expected, and that the pace of increases will slow at some point, but Powell also stated that *"We think that we have a ways to go, we have some ground to cover with interest rates before we get to that level of interest rates that we think is sufficiently restrictive".*
- The policy stance remains firm, but the bank added a new paragraph in the November report: "In determining the pace of future increases in the target range, the Committee will take into account the cumulative tightening of monetary policy, the lags with which monetary policy affects economic activity and inflation, and economic and financial developments." In other words, the Fed does not want to break the economy's back, and more importantly, it is not about how fast to go, but how far to go (and the Fed is going further than previously communicated). The market has since early October anticipated a higher terminal rate than the FOMC September dot plot signalled, a 4.6 peak. In fact, the market did not revise its expectations much up after receiving the messages from Powell
- However, Powell also reiterated his previous comment that **the risk of tightening too little outweighs the risk of tightening too much** – and he also added that should the Fed go too far, they have the tools to support the economy
- Taken together, another 75-bps hike in December was not taken off the table, even if the FOMC in September signalled a 50 bps Dec hike. The market pricing implies that a 50-bps hike is sufficient, given that the terminal rate is not that far away, and market rates did not move by much last Wednesday, in the short end or the curve, or with regards to the terminal (peak) rate in this cycle (*check next page*). However, longer dated contracts are higher than before the FOMC meeting
- But sure, the bank's decision is, like any other central bank's, data dependent…

Seems like the Fed has its job cut out for them: Vacancies increased in September

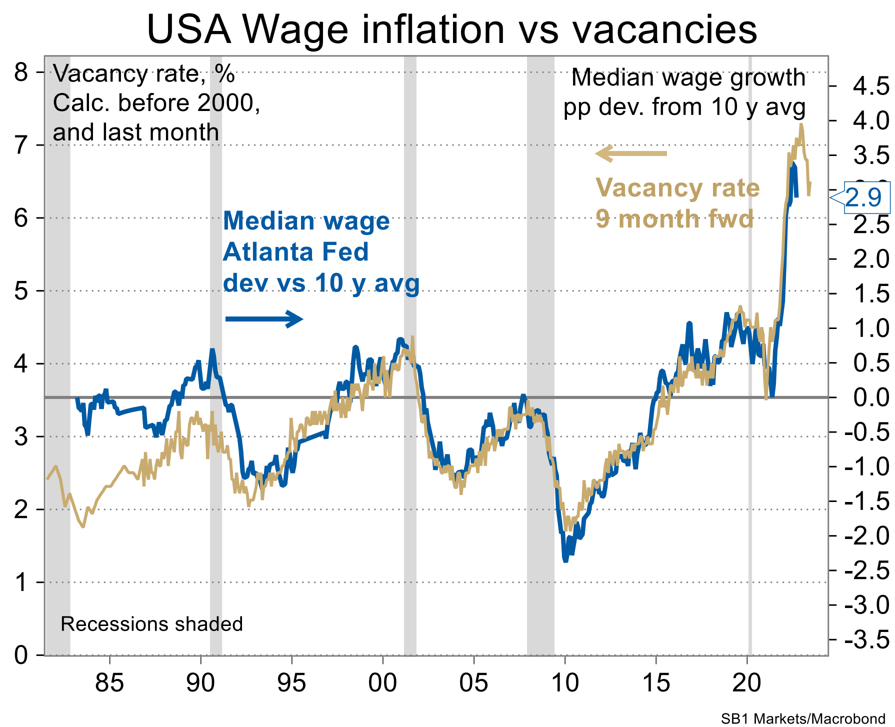
The vacancy rate increased by 0.3 pp to 6.5%, was expected down to 5.9%!

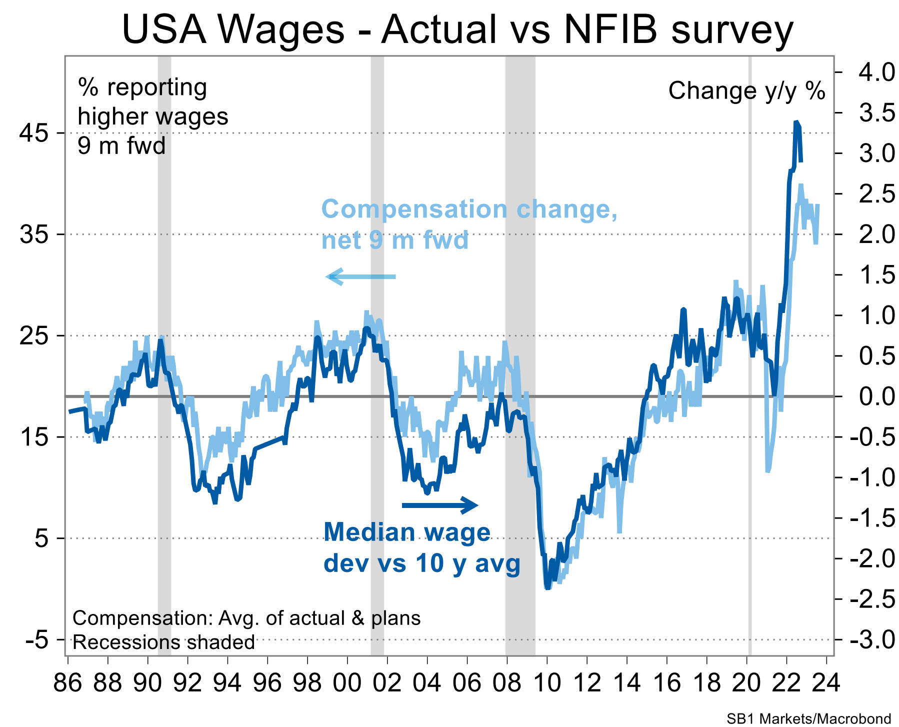


- The number of **unfilled vacancies rose by 0.44** mill to 10.7 mill in Sept (Aug vacancies revised up by 280'), expected down to 9.75 mill. The rate (vs no. of employed) rose 0.2 pp to 6.5%, while it was expected down to 5.9% (the red cross at the chart to the left)!
  - » Vacancies are still down from the peak in March (7.3%), but the September JOLTs survey indicates that it may be more tricky to restore balance in the labour market than what has been laid out by the Fed
  - » The highest print ever before the pandemic was 4.7%, and the rate was 4.5% just before the pandemic hit – the current level is still very high – even if the tide has turned
- **The SMBs (NFIB survey)** reported that 46% of companies were not able to fill positions in October, unch. from Sept, which is close to record high. Hiring plans were down by some 3 pp, but remains high – and the share saying that they are increasing compensation rose, and is again close to record high
- **New hires** fell by 0.2 mill to 6.1 mill in Sept, equalling 4.0% of the employment level. This is indicating an easing of the labour market, but the level is, of course, still high
- The number of **voluntary quits** fell 0.1 mill to 4.1 mill, leaving the rate to employment unch. at 2.7%. The trend is down, signalling that workers have become somewhat more cautious leaving their current jobs – but the quit level is still higher than anytime before the post pandemic surge
- **Layoffs** equalled 0.9% of employment in September, down 0.1 pp from August – still not signalling any take-off in downsizing
- **In sum:** The tide has turned, but the labour market is still very tight, and it is unlikely that wage inflation will come down to a sustainable level without a substantial further weakening. Job openings may be stickier that what the Fed has hoped for, and are leading unemployment by some few months, though not by a stable lag (but the correlation is high). Actual unemployment rose by 0.2 pp to 3.7% in October but new jobless claims, which leads the unemployment rate has not turned up

Both the vacancy rate as well as SME's compensation plans have peaked

And wage inflation may have peaked too, but the level is still way above what will return 2% CPI infl.

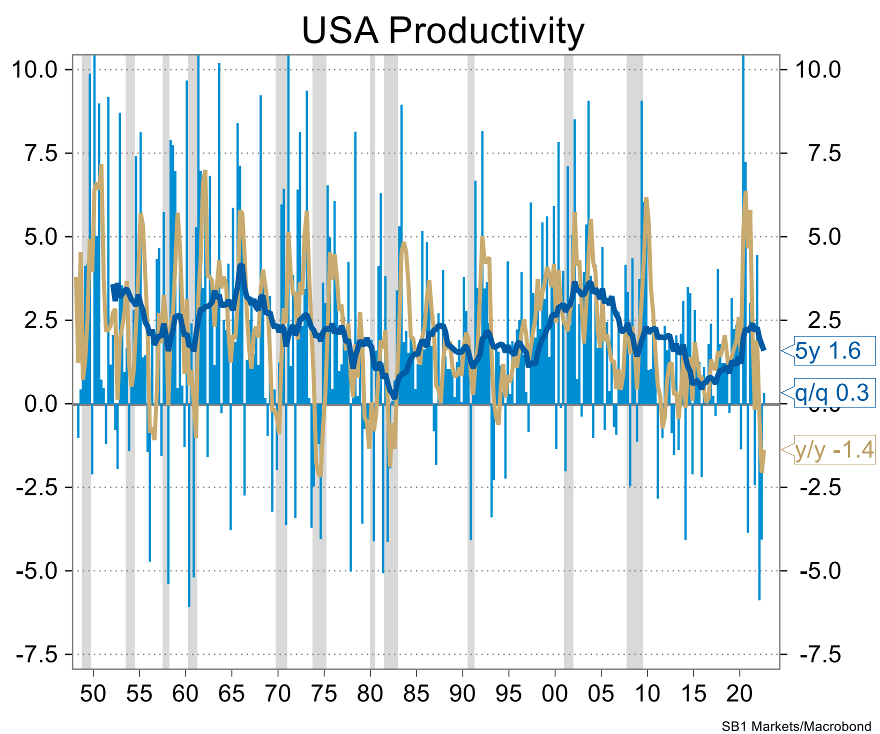


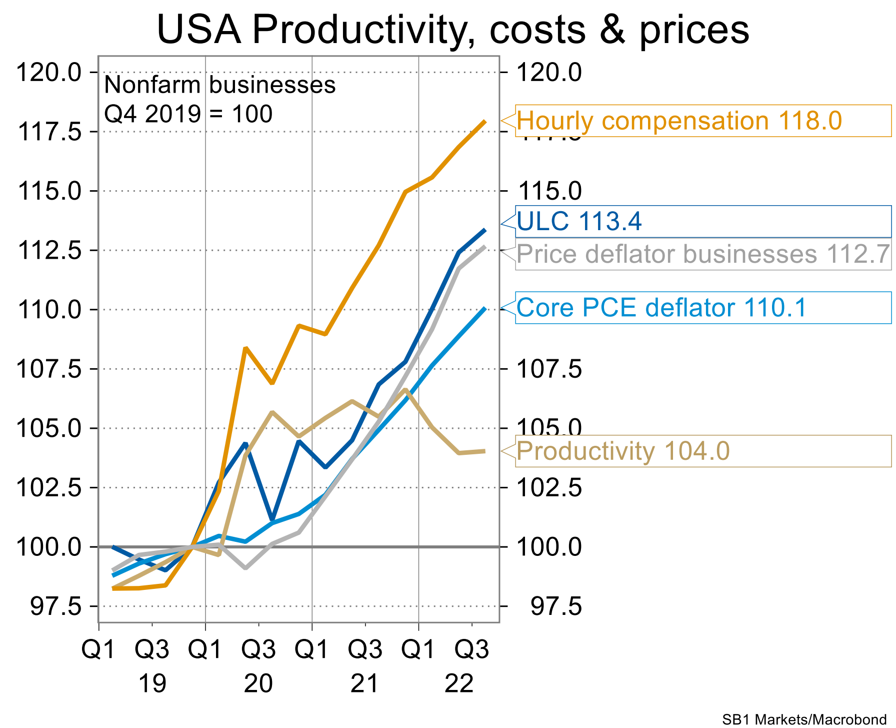


- **Our 'Phillips curve'** based on the vacancy rate signals a further increase in wage inflation the coming quarters even if vacances may have peaked, as the vacancy rate leads changes in wage inflation quite consistently by 3 quarters. However, we would not be surprised if the current extraordinary high wage already has peaked
  - » Companies (SMEs) compensation plans signal continued high wage inflation but not faster than the present
- **Wage inflation** has already accelerated by almost 2.9 pp vs the 10 y average (Atlanta Fed median), and cannot possibly generate a 2% price inflation rate over time. <u>This is Fed's main headache, not the current high CPI inflation print. And it will become the stock owners' headache too, of course</u>
- **Demand for labour has to be reduced sharply in order to get wage inflation back to a sustainable level!**
  - » <u>Check under which circumstances wage inflation slows on the charts above (hint: find the shaded areas, follow the blue wage line - as well as the vacancy rate or the wage hike plans ☺). Fed will not be able to control inflation if demand for labour is not cut sharply. Exactly what Powell told us at the recent press conferences!</u>

No growth in productivity in Q3 but growth past 3 years revised up by 0.8 pp/y!

Unit labour cost is revised down by the same amount, still climbing far too fast

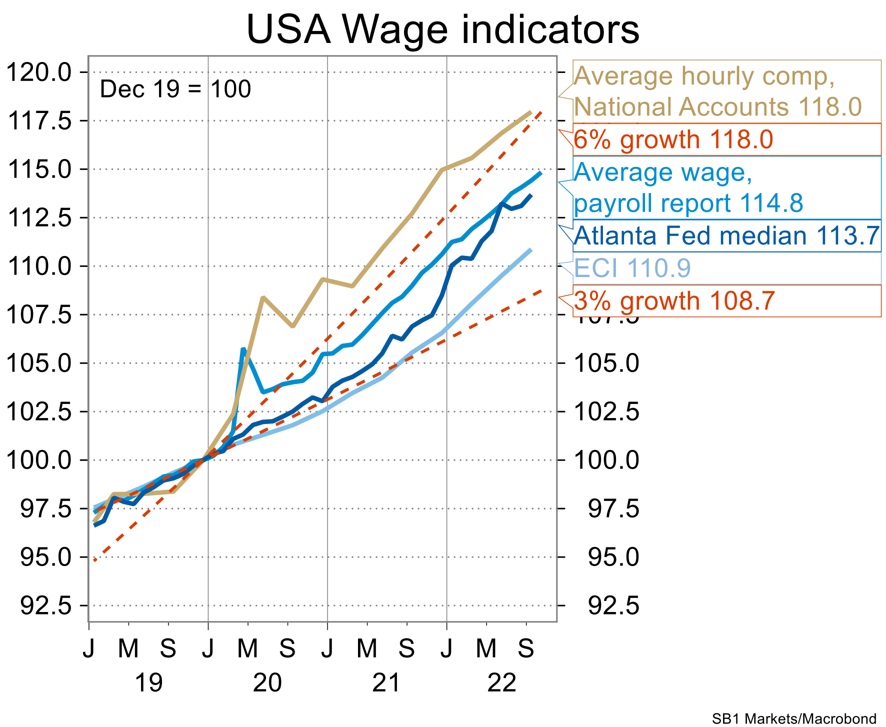


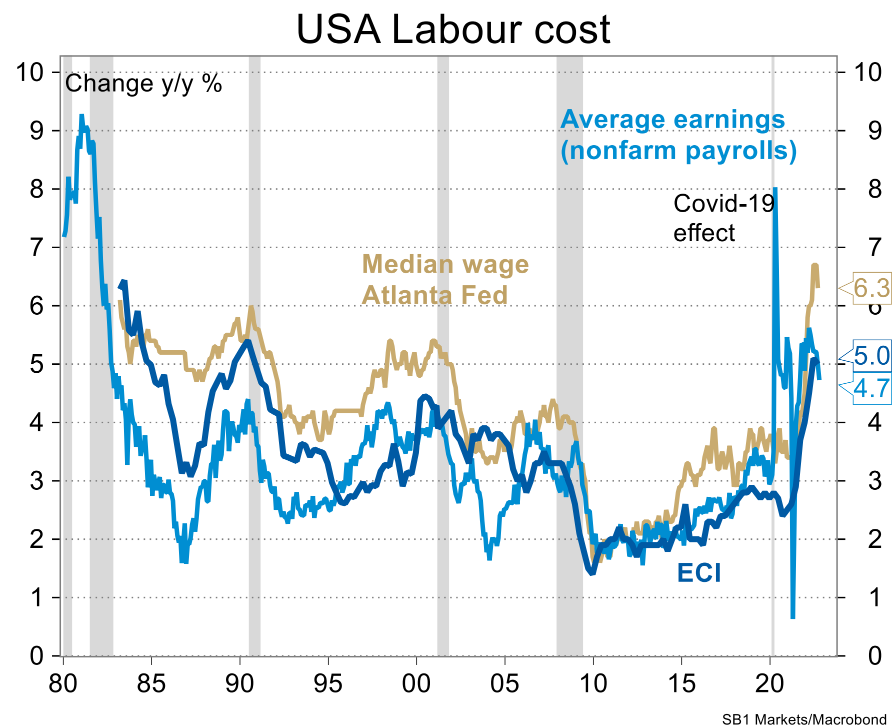


- **Productivity** rose by 0.3% in Q3 (annualised), expected up by 0.6%, after the unusual steep decline during H1. Over the past 4 quarters, productivity has fallen by 1.4%, as less productive (and less paid) service sector workers have returned to their jobs after the pandemic). However, following the upward revision of GDP growth since 2019 (in the annual revision, published some weeks ago), productivity growth was revised substantially upwards, from a 0.6% average pace to a 1.4% average pace! That's still not impressive, but in line with recent history (check the two following pages)
- **Hourly compensation (wages ++)** grew at a 3.8% pace in Q3, and the annual rate is 4.7%. Average growth since Q4-19 is 6.2%. Growth is slowing somewhat, but not convincing as lower paid service sector workers have returned to work, taking the average wage down
- **Unit labour costs** (hourly compensation – productivity) grew by 3.5% in Q2, up 6.1% y/y. Since Q4-19, ULC has grown at a 4.7% pace, revised down from 6.4% but still far above a normal level – which of course is incompatible vs the 2% inflation target

All indicators combined: some signs that wage inflation may have peaked

However, all are reporting much higher wage inflation than pre Covid: 2% price inflation 'impossible'



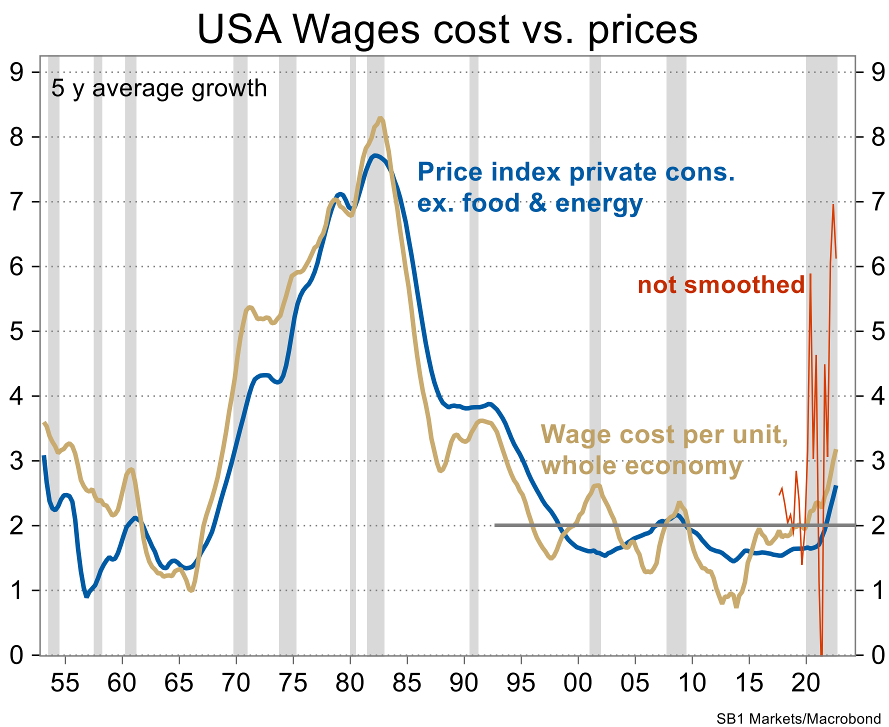


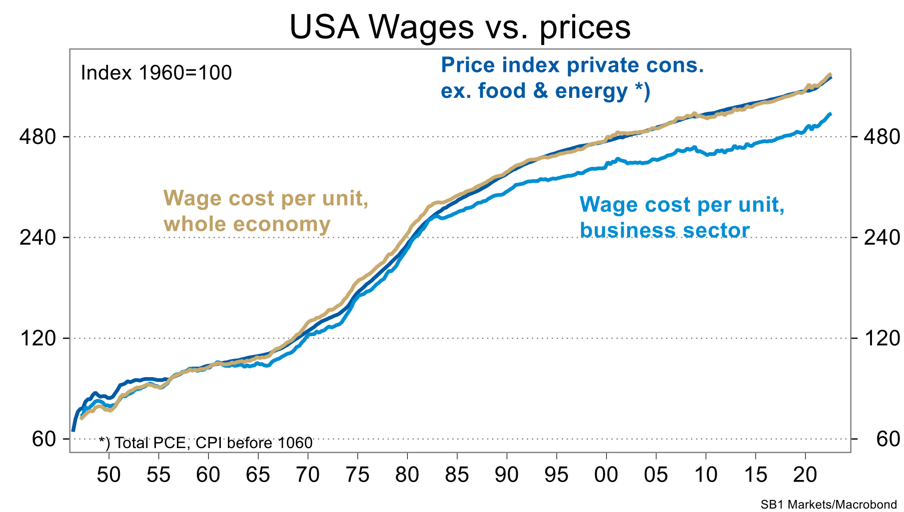
- **All wage indicators** are reporting faster wage growth, and all reporting wage growth well above the average recent years. More on hourly earnings in Q3 here
- Growth in wage/earnings/compensation indicators are up 2.5 – 4 pp vs the their respective 10 y averages before the pandemic
- Over the past 10 years, inflation has been close to 2% (before the pandemic, that is)
- It will be a impossible to keep inflation at 2% if wage inflation remains at the current levels. Productivity growth has not accelerated. Profit margins may take a beating – and they no doubt will – but not sufficient to bring inflation down to acceptable levels on their own. Wage inflation will probably not slow by much before demand for labour weakens – and unemployment increases

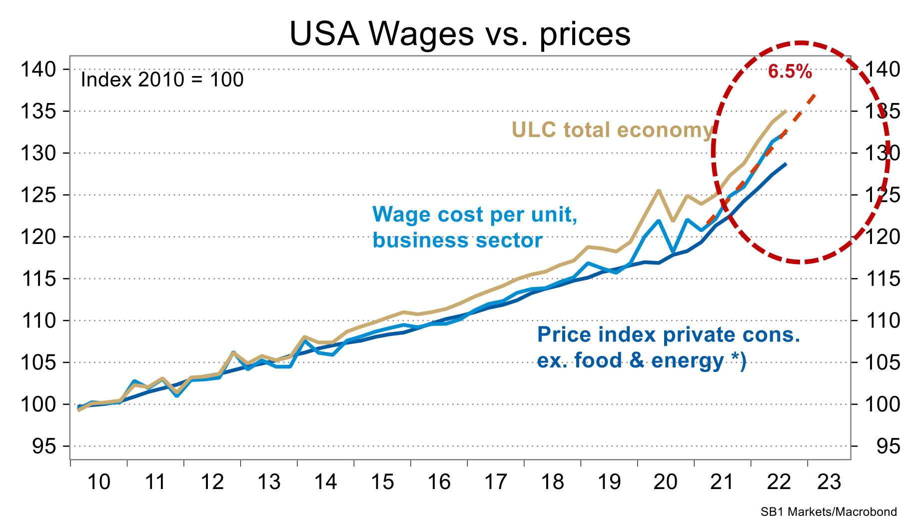
SpareBank 1 MARKETS

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

Core inflation will be hard do get down, given the cost surge recent quarters



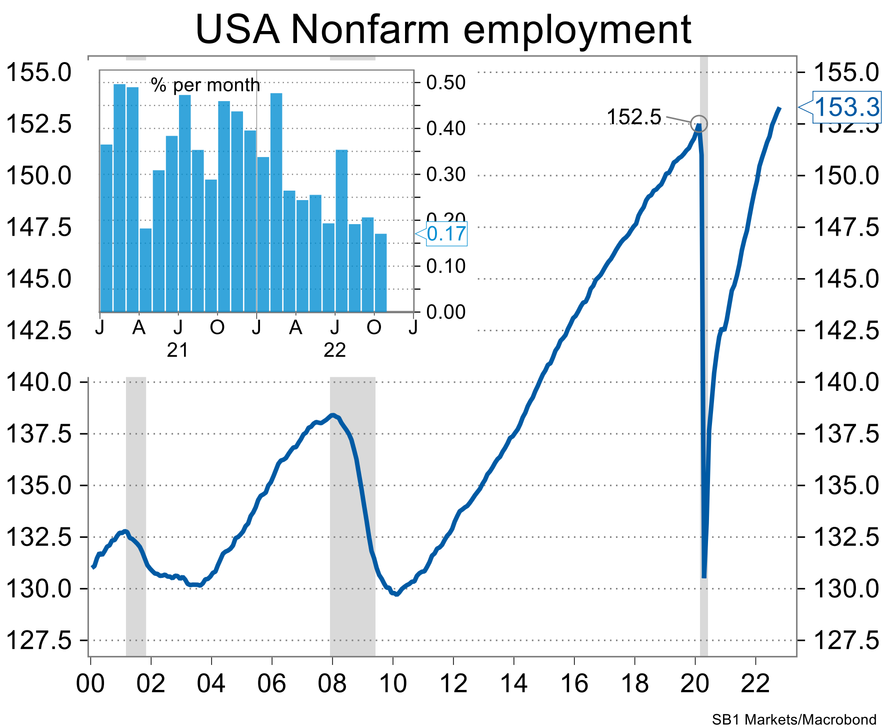


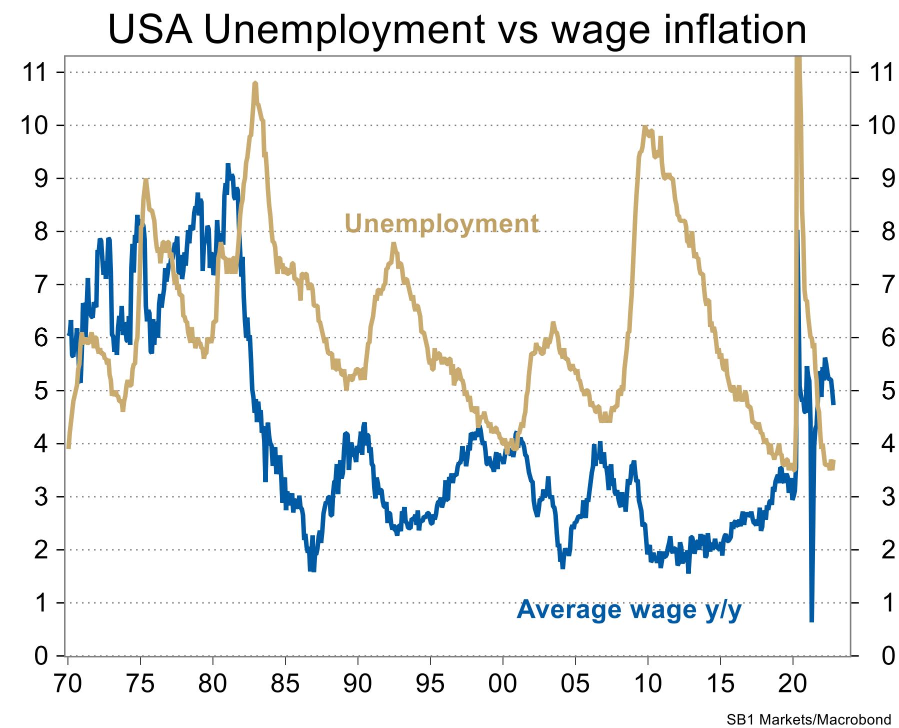


SpareBank 1 MARKETS

Employment growth is slowing, and unemployment rose in October

In addition, wage inflation may be slowing – but it remains too high, according to the labour report



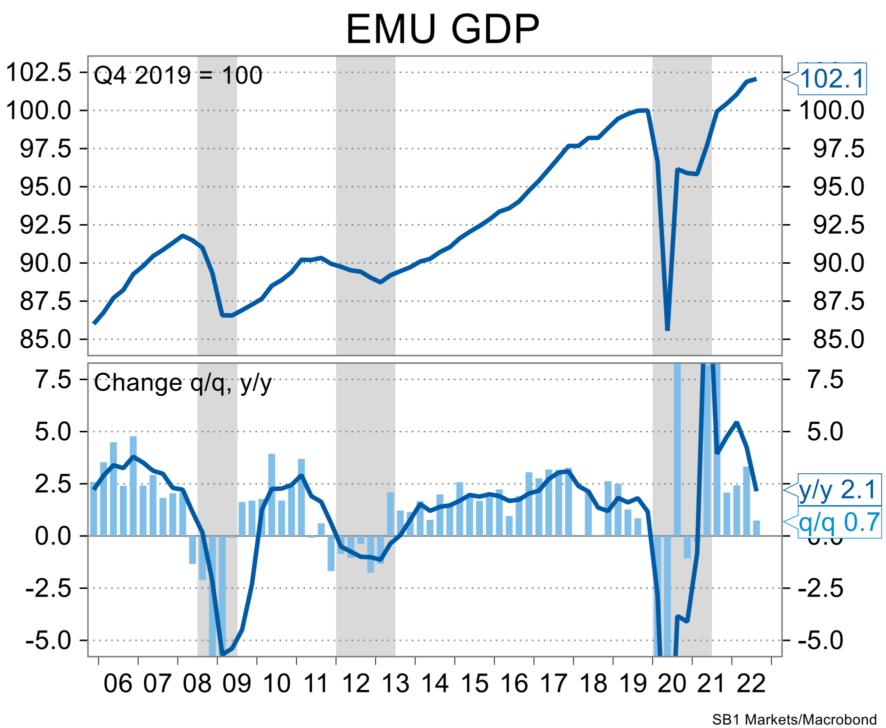


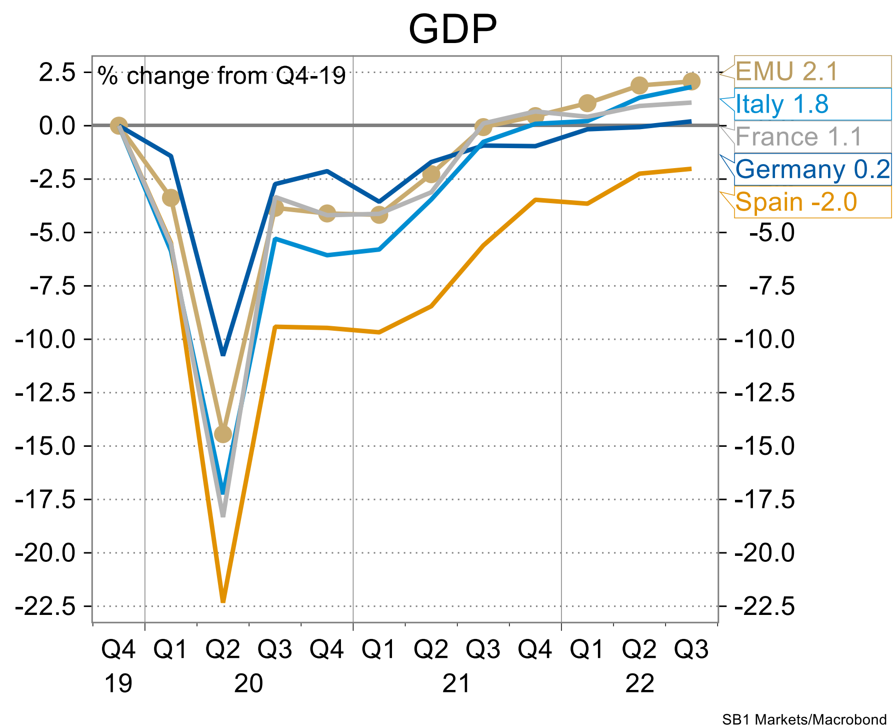
- **Nonfarm payrolls** rose by 261' in October, expected 200' (Sept data was revised up by 52' to 315') but growth is gradually slowing. The LFS employment fell by 0.2% and the **employment rate** was down 0.1 pp to 60.0%. The employment rate has flattened since March – surely not a signal of strength
- **The participation rate** decreased by 0.1 pp to 62.2%, and the level has been flat so far this year. The unemployment rate still rose by 0.2 pp to 3.7%, expected up to 3.6%. The FOMC Q4 forecast at 3.8% is not far away, but one month's data is not sufficient to ease anyone's nerves
- **Wages** rose 0.4% in Oct, 0.1 pp more than expected and than the Sept increase. Measured 3m/3m, wages are up 4.4%, and clearly declining! The annual rate fell 0.3 pp to 4.7%, as expected. Still, wage inflation is well above par; Average wages rose by 3¼% in 2019, and well below 3% in the years before (and other and better wage indicators signals higher wage growth)
- The unemployment rate is still too low, and wage inflation is too high. <u>The next month's data will be crucial if the FOMC should comfortably ease the pace of rate hikes to 50 bps</u>

SpareBank 1 MARKETS

No recession yet: Eurozone GDP expanded at 0.7% (annualised) pace in Q3

The market expected a 0.4% growth pace

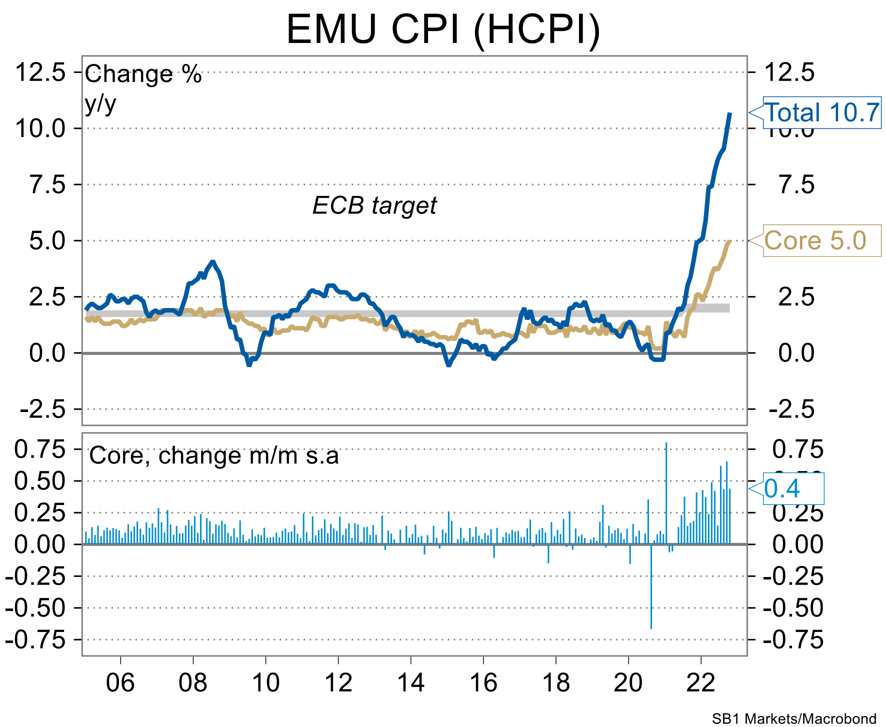


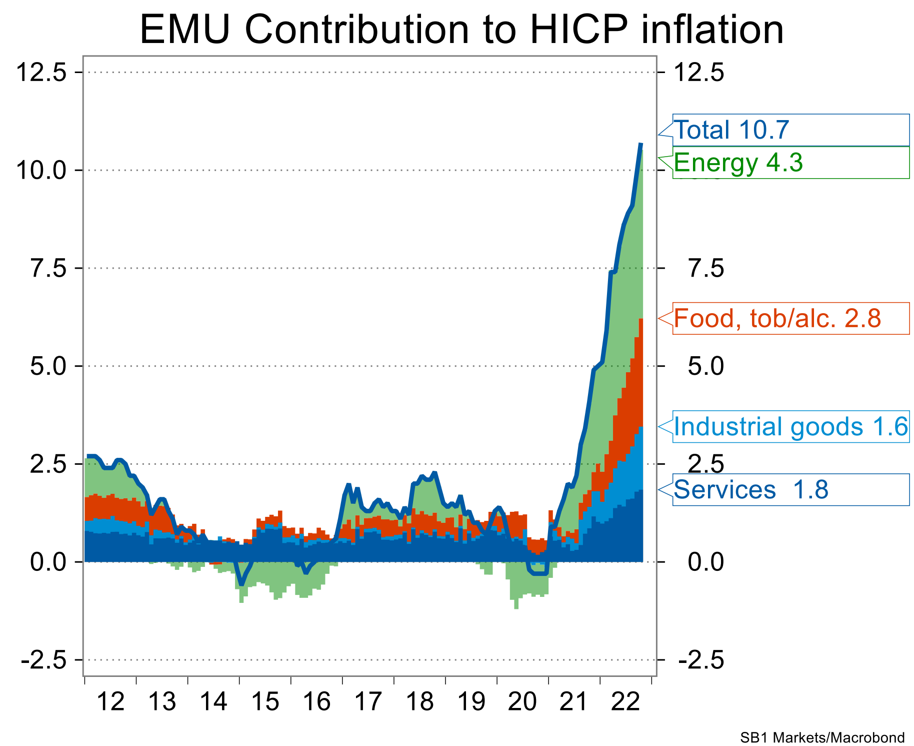


- GDP grew 0.2% in Q3 (not annualised), expected 0.1% - and is up 2.1% y/y and 2.1% above the Q4-19 level
- Italian GDP grew rapidly in Q3, up 0.5%, expected +0.3%
- German GDP was up 0.3% (not annualised), expected -0.3%; France + 0,2%, as expected; and Spain +0.2%, below the expected 0.3%
- *Details will follow in a fortnight*

Inflation higher than expected in October too, as headline inflation hits 10.7%

Core inflation up 0.2 pp to 5% y/y, expected unch.

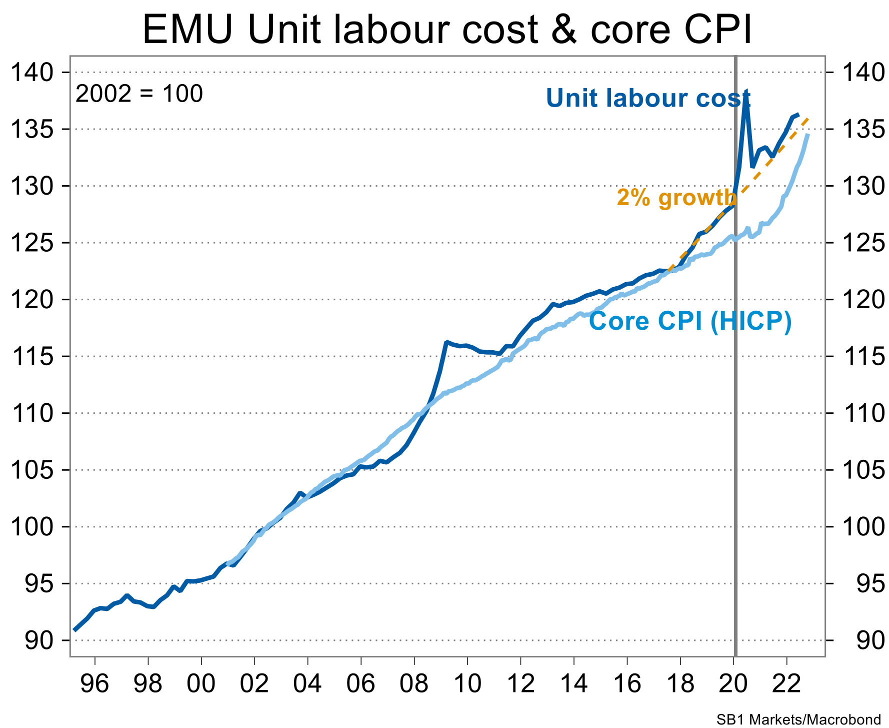




- The **total HICP** rose 1.4% m/m in Oct (seas adj), and 10.7% y/y, which was 0.5 pp above expectations (however, national data that came out Friday the previous week revealed that the forecast was far too low)
  - » Energy prices rose 3.7% m/m, they are up 41% y/y (unch.), and contribute by 4.3 pp to the headline rate. Food prices rose 1.4% m/m - and the latter is up 13% y/y, contributing 2.8 pp to overall CPI growth
- **The core** rose 0.4% m/m. Both goods and services contributed. The annual rate accelerated 0.2 pp to 5%, the highest ever, again…
- The **ECB** hiked rates by 75 bps last week and reiterated that their job is to control inflation. However, the bank's statement with regards to further hikes was softer, and they can afford to be – 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. So far, they have not succeeded

Unit labour cost inflation suggests limited risk to inflation, over time

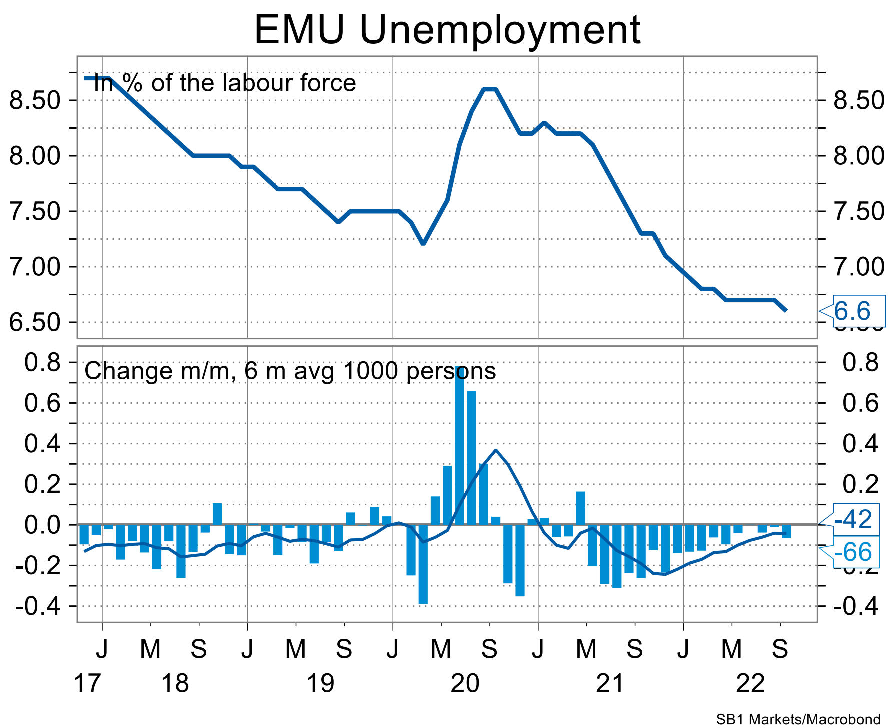
Wage inflations is moderate, and ULC is up at a pace just marginally above 2%

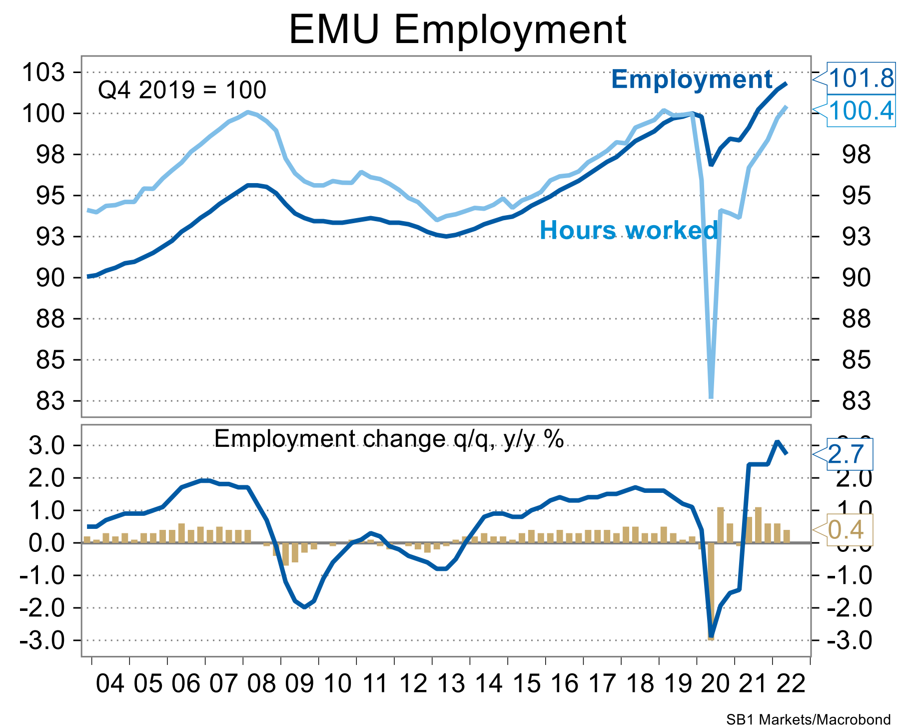


- **Unit labour cost** (labour cost per unit produced = wage cost/production volume, growth in UCL= wage growth – productivity growth) has jumped up during the pandemic as productivity fell because employment was not cut (as in the US)
- On the other hand, in the 3 years before the pandemic – and through the pandemic so far – ULC has accelerated to 2% from 1%. The 1% growth in unit cost corresponded to the long term growth in core rate of inflation at 1%, well below ECB's 2% target – and a 2% ULC inflation will over time yield a 2% CPI inflation

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

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



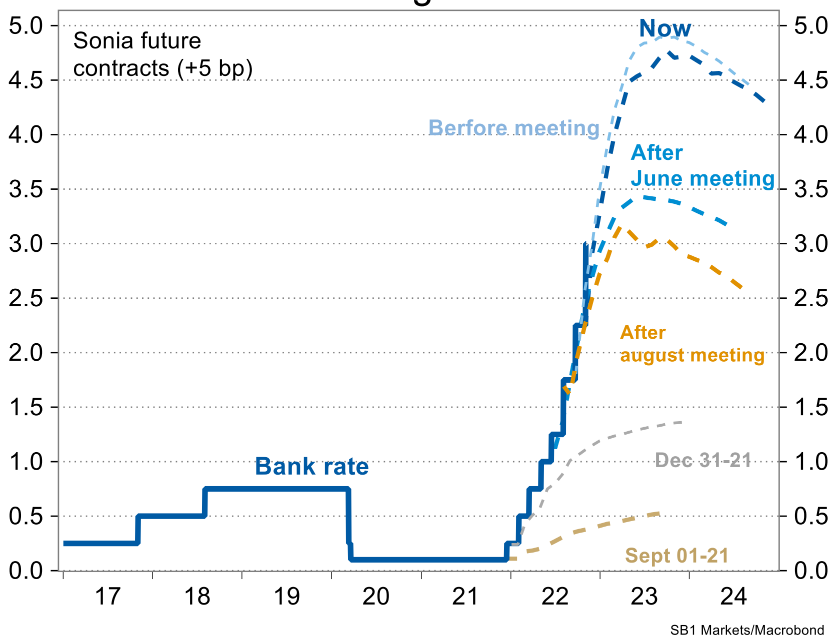


- **The number or unemployed** declined further in September
- **Employment** grew by 0.4% in Q2 (not annualised), and hours worked grew too
  - » The employment level & the employment rate is higher than before the pandemic
- The number of **unfilled vacancies** soared to the highest level ever in Q2, 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%

Bank of England raises rates by 75 bps - largest hike since 1989

…and forecasts a longer recession

UK Bank of England bank rate

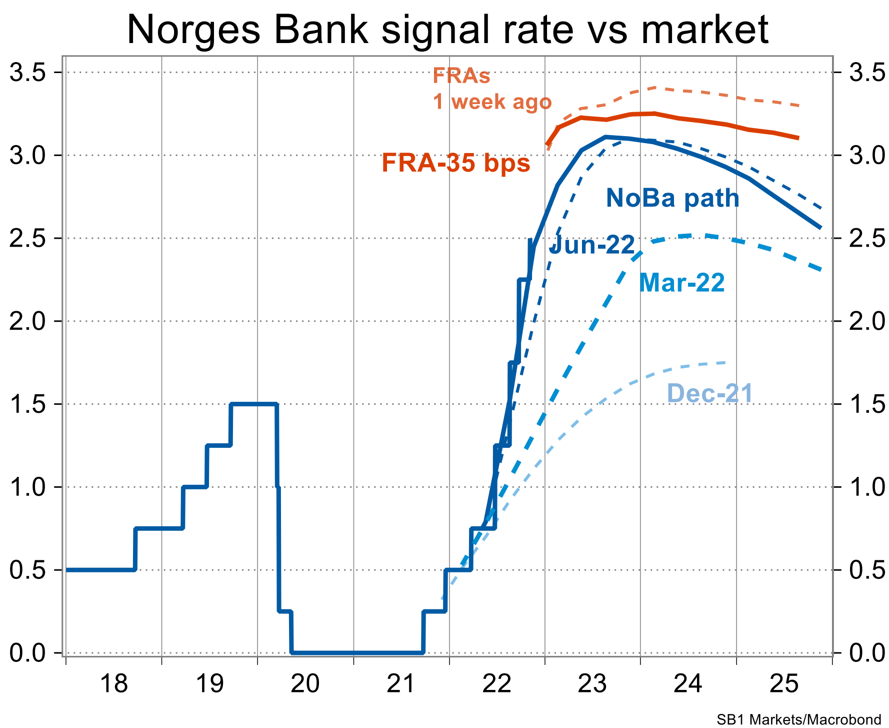


- **The policy rate** was lifted by 75 bps to 3%, as widely expected
  - » 7 of 9 members voted for a 75 bp hike, while 1 member preferred a 50 bp hike, and 1 member voted for 25 bps
  - » The Bank was clearly front loading rate hikes in order to prevent it from risking an extended tightening later
  - » In its statement, the bank projects a contraction in GDP for 5 - 8 quarters, depending on the terminal rate (3% vs. 5.25%), but signalled that the bulk of the rate hikes is behind us, but that some further increases are needed to bring inflation back to the target of 2%. However, the governor stated that the projected terminal rate is closer to today's rate than the peak markets predictions in Oct.
  - » Peak inflation is now expected at 11% in Q4 this year, which is down from 13% in the last MPR due to the Energy Price Guarantee. Unemployment is forecasted to reach just under 6.5% (from the current 3.5%) and that there will be a negative output gap of 3%

- The **short end of the UK curve** kept sliding at the bank stated that most of the rate hikes are in the past. Predictions of a prolonged recession, on the other hand, sent the GBP tumbling yet again, and the pound is down 2.6% for the week

Norges Bank raised by 25 bps to 2.50%

The bank is acknowledging that the economy is cooling, and we are yet to see full effect of hikes



The policy rate was raised by 25 bps to 2.50%, as expected by both us and some half of the economist. The market was also split, but the market response was smaller than we expected

The bank also signaled that **the rate will likely be hiked further** in December (by 25 bps, they said in Sept)

According to the statement and the governor, the underlying data suggests that the rate could have been hiked by more than 25 bps. GDP growth and inflation have surprised at the upside, and unemployment at the downside. However, the bank sees signs of a slowdown in the economy, and it acknowledges that monetary policy works with a lag – the rate is already in restrictive territory.

Given the households debt level, almost entirely floating, the impact could be substantial. In addition, Norway does not have a wage inflation problem and the risk of overreaching is clearly present – in other words: the bank can afford to wait and see

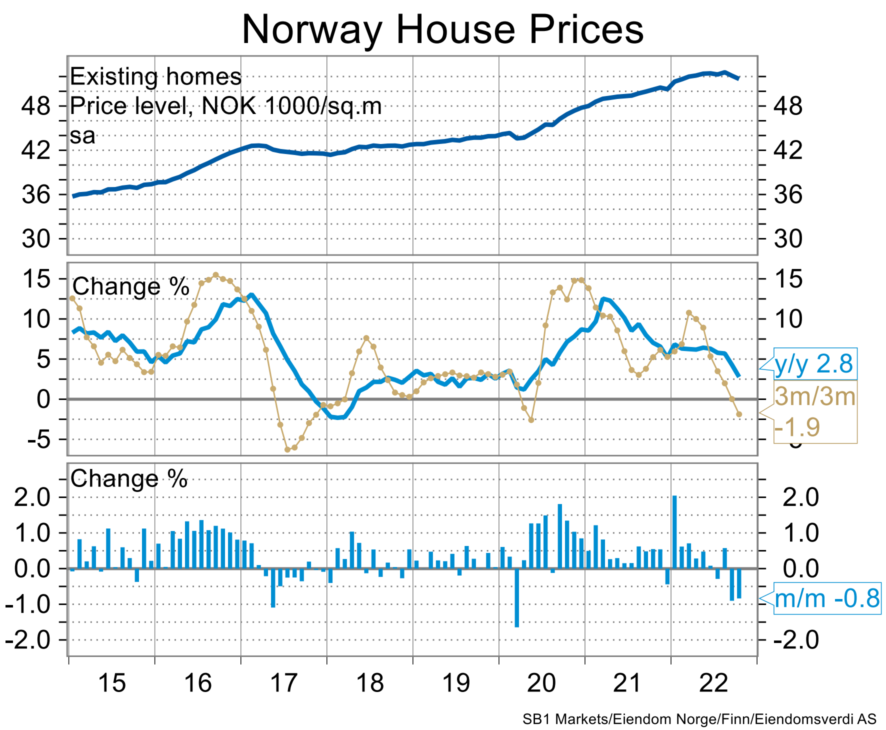
Market reaction

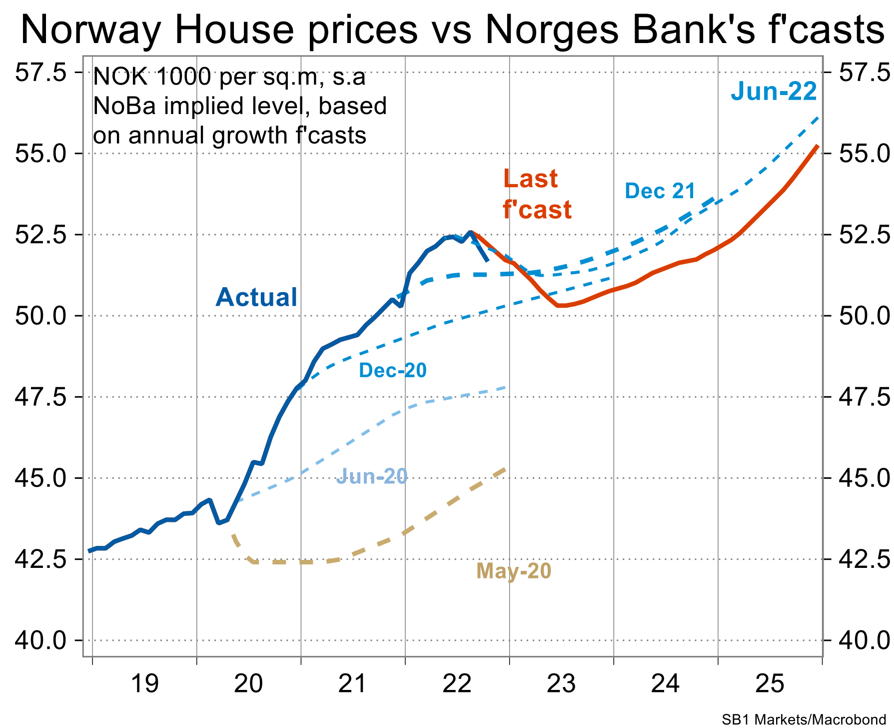
- » The **Dec-3 FRA** fell 4 bps, but rest of the curve rose. The Dec-3 FRA at 3.53% is far to high if NoBa hikes by just 25 bps or even 50 bps in December.
    - ▪ However, the NIBOR spread has very likely widened substantially, the 3 m NIBOR is at 3.40%, implying NIBOR spreads at 76 bps if NoBa hikes by 25 bps in December, and 62 bps if NoBa hike by 50 bps in Dec! The 'normal spread is some 40 bps in (35 bps + the normal Q4 liquidity year end premium at 5 bps)
- » The **NOK** depreciated 1% just after the announcement, but has strengthened thereafter, no doubt supported by a higher oil price

SpareBank 1 MARKETS

Winter is coming, house prices down 0.8% in Oct; Sept print revised down

Prices are falling faster than NoBa assumed, almost ½ of the assumed decline already executed



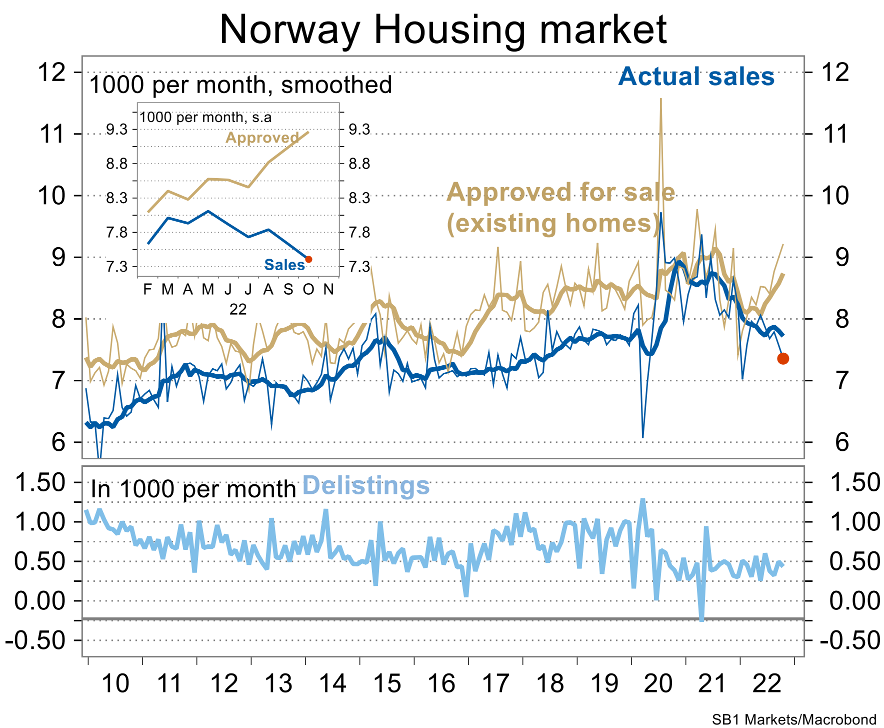


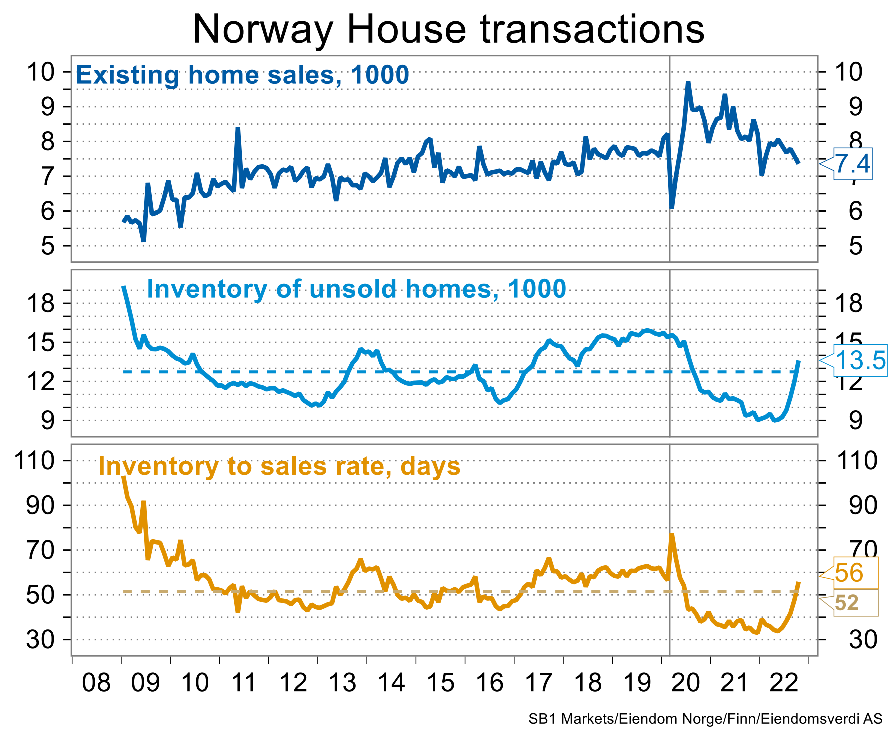
- **House prices** declined 0.8% in October, we thought even 2% was likely (which was close to the 1.9% drop in Oslo). September was revised down by 0.3 to -0.9%. Barring the price fall at the start of the pandemic, we have to go back to 2017 to find a greater fall in prices. Norges Bank expected a 0.4% decline. Prices are now down 1.9% measured 3m/3m – but are still up 2.8% y/y. Prices fell in 11 of 16 cities, and the most in Oslo. Underlying (3/3m) are up in 3 cities, down in 13
- **Existing home transactions** fell further, to 7.6' which is 15% below the peak during the pandemic but still just back to the average 2019 level. However, no. of **homes approved for sale** rose further, and is clearly above a normal level.
- **The inventory of unsold homes** rose by 1.6' units in September, the steepest increase ever (the two previous months were last ATHs!), to 13.5', which is above avg. Since June, the inventory has shot up twice as fast than anytime before! Still, the time on market for those homes actually sold remains low
- **Norges Bank** expects a 4% price decline from August till next summer. Now prices have declined by 1.7%. The risk is no doubt on the downside

SpareBank 1 MARKETS

A record rapid pace of inventory accumulation as sales slow rapidly as well

The inventory is increasing twice as fast as ever before, and the inventory is above average

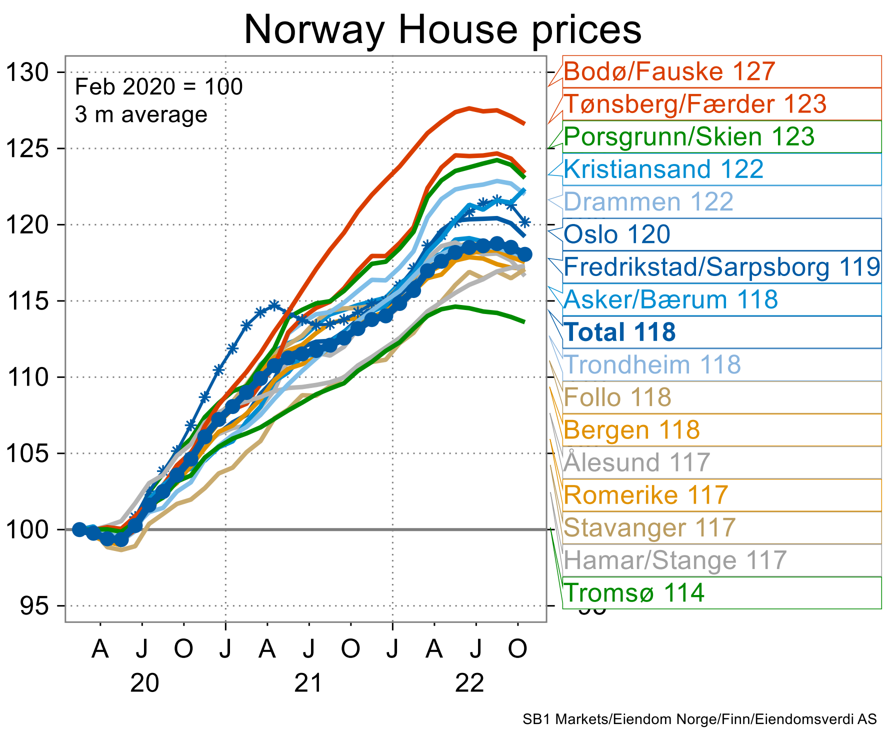


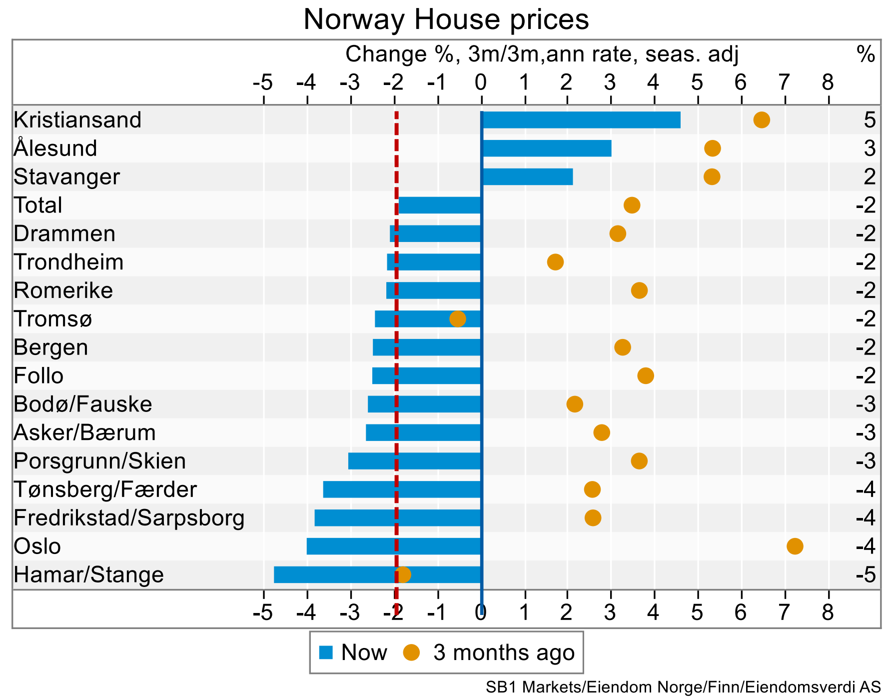


- The **number of transactions** fell in further in October and is now slightly below a normal (2019) level (7.3')
- The **supply of new existing homes for sale (approvals)** rose further and to way above a normal level in October (9.2')
- The **inventory of unsold homes** rose by 1.6', the fastest increase ever (August and September were also ATHs ☺). The lift over the past 4 months is twice as fast as ever seen before, up to 13.5 from 9.1' in June, or almost 50%)
- The **inventory/sales ratio** added 10 days to 56 days, vs an average at 52 days – and the ratio is still not high
- The **time on market** for those homes actually sold was unchanged at 32 days (average 42 days) – so there is not yet any buyer's strike for homes which are 'correctly' priced. However, if all those homes not sold should have been sold, substantial price cuts would very likely have been needed

The big picture: Prices are now turning down most places

Prices measured 3m/3m are still up in Kr.sand, Ålesund and Stavanger, but down in 11 of 16 cities

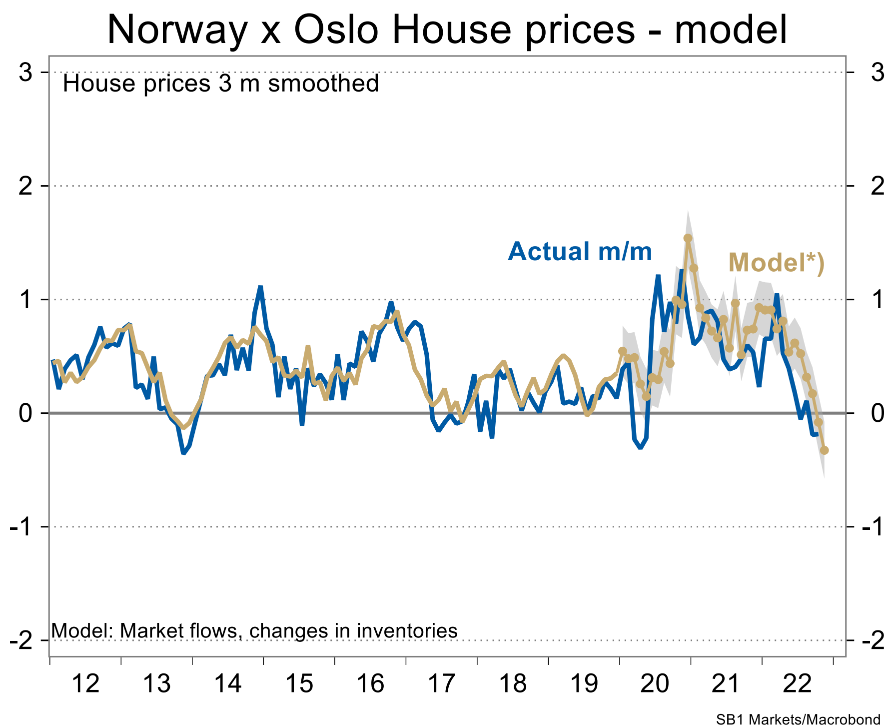


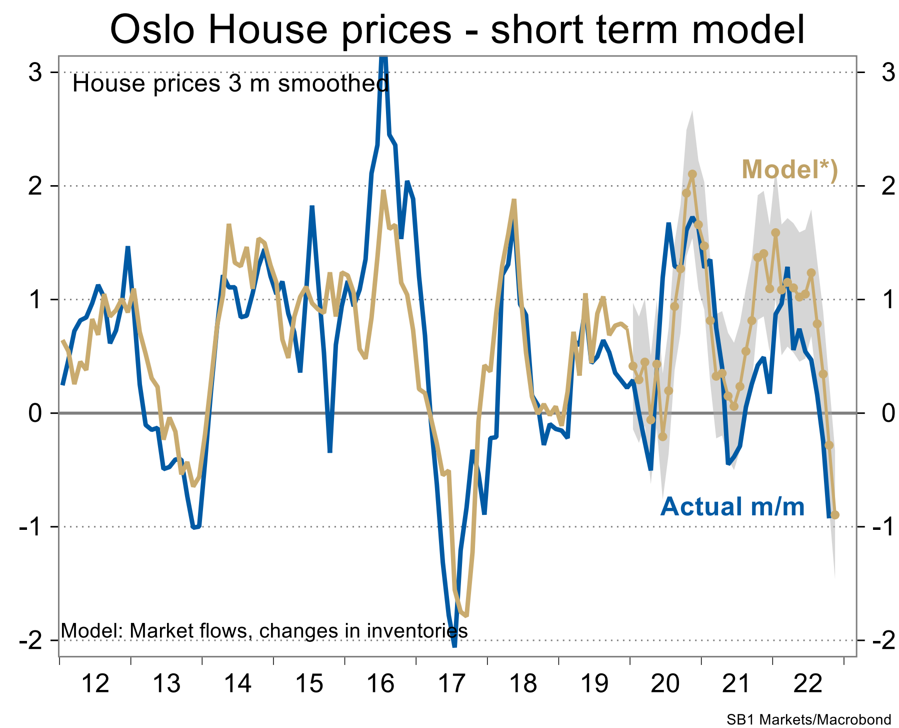


- Bodø the winner through the pandemic (and since 2016). Recent months, prices in Bodø have been falling but now Oslo is speeding up too
- After Bodø, south-eastern towns have been the winners since early 2020; Tønsberg, Porsgunn/Skien, Drammen, Oslo, and Fredrikstad/Sarpsborg. Prices are now seem to have turned most places
- Tromsø, Hamar, Stavanger, and Romerike are at the bottom of the list (vs. early 2020)
- Now: Prices are falling most places, even smoothed 3m/3m. 13 'cities' are down, while just 3 still are up measured 3m/3m. 3 months ago, just 2 cites were reporting underlying decline in prices

Short term market flows suggest continued price fall, especially in Oslo

Higher mortgage rate will also contribute to a slowdown coming months

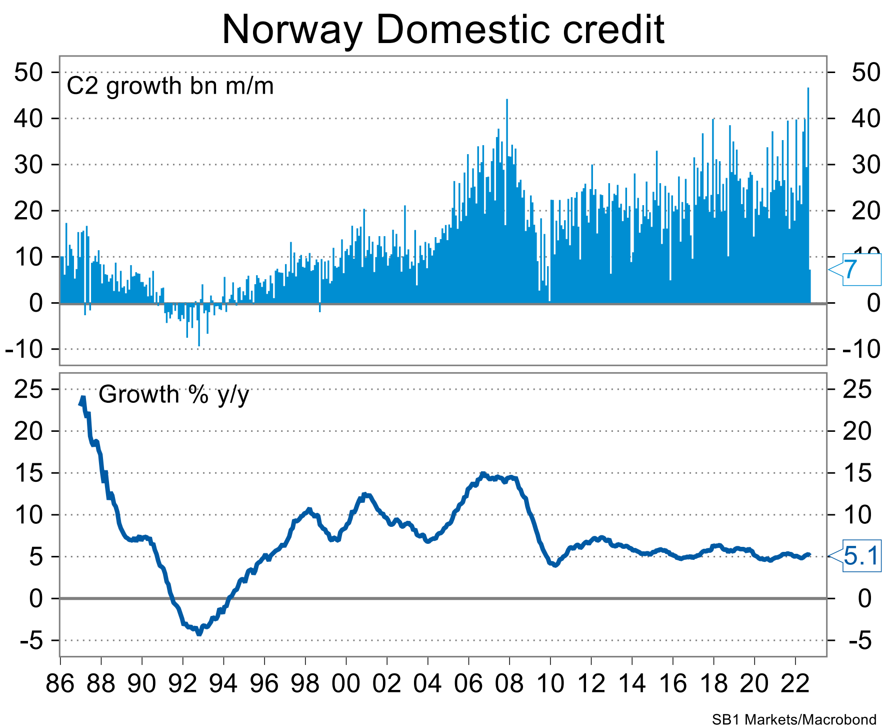


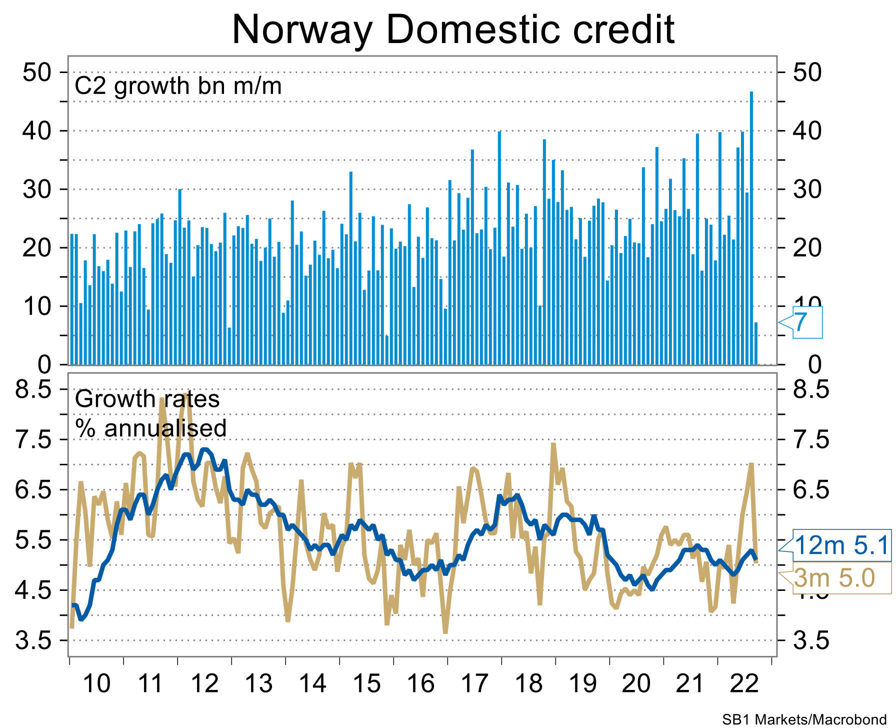


- Our **national x Oslo model** based on flows and the inventory signals a 0.3 fall in house prices (in comparison, prices in Norway x Oslo fell by 0.5% in October)
- Our **Oslo model** signals a further fall in prices and more than in the rest of the country
- **Mortgage rates** are not included in these short-term market models, because they have not consistently added to the models' performance. Still, over time, mortgage rates and credit growth are important driver for the flows at the housing market, and now rates are rapidly on the way up
- *These models are not long-term price models, just short-term models based on flows of (existing) houses approved for sale, actual sales and changes in inventories – which are normally correlated to prices*

After the August borrowing spree, payback time in September

Growth in household debt is gradually slowing, and is now slightly under the NoBa estimate from September

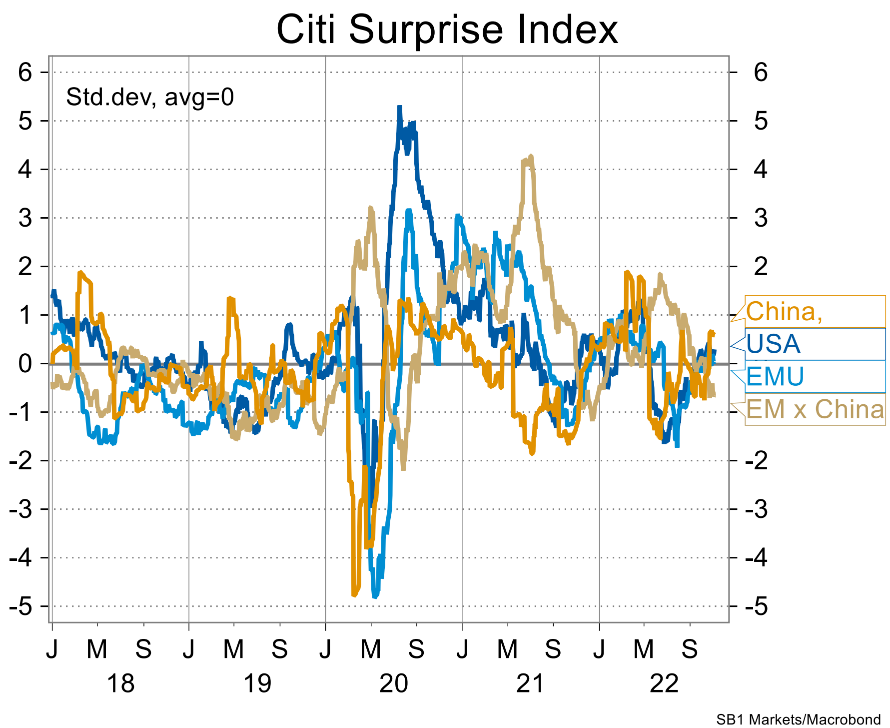


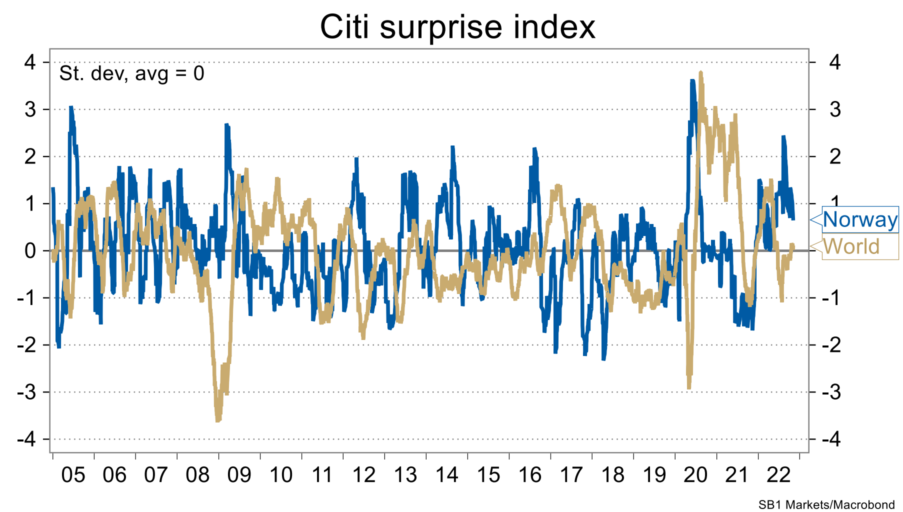


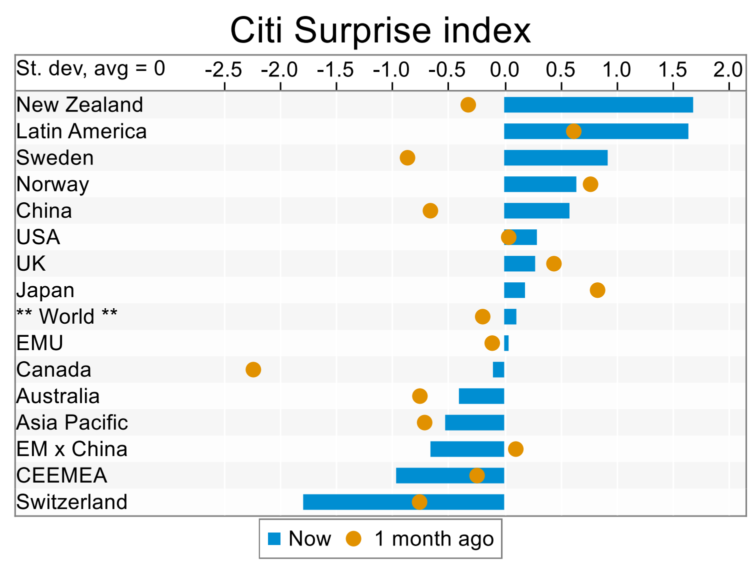
- **Total domestic debt** (C2) rose by NOK 7 bn in Sept, down from 45 bn in Aug, we expected 19 bn. The annual growth rate fell 0.2 pp to 5.3%, we expected an uptick from the prev. reported 5.2% to 5.3%! The 3m/3m growth rate fell to 5% from 7%. What happened?
- **Corporate C2 credit** contracted by NOK 10 bn, following the unprecedented 31 bn lift in Aug, and the annual rate fell by 0.7 pp to 7%. For Mainland companies, the annual rate fell 0.3 pp to 8.6%, way above NoBa's estimate. The unusual swing is probably due to transfers of debt from abroad
- **Household credit** rose by NOK 14 bn in Sept, 1 bn more than we expected (and up 1.5 bn form Aug). The annual rate was unch. at 4.3%, as we expected. NoBa estimated 4.4%. We expect a further slowdown as higher interest rates and falling house prices curb demand for debt
- **Local governments** added NOK 4 bn in Sept, 0.5 bn more than we expected. The annual growth rate gained 0.5 pp to 4.3%. Last summer the rate was 8%! Finally, local gov's are not increasing their debt/income ratio

Data close to expectations, according to the Citi surprise index

Both US, EMU and China delivers as expected







- **Emerging markets x China** is somewhat below par
- **Norway** no. 4 on the list, according to Citi, behind Sweden

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

Highlights

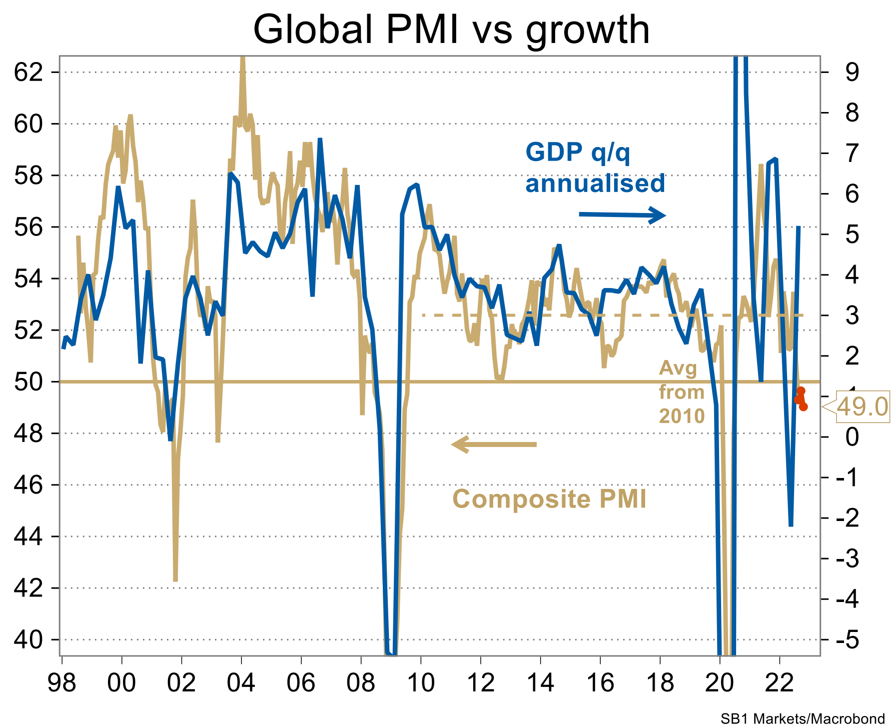
The world around us

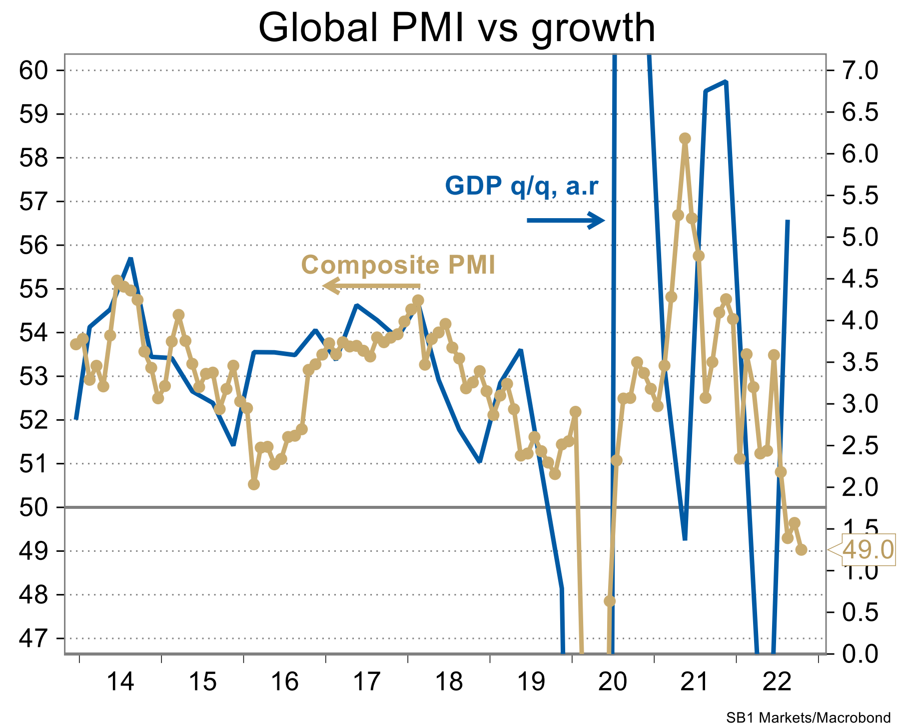
The Norwegian economy

Market charts & comments

The global PMI down in October, signals just some 1% global GDP growth

The global index fell by 0.6 p to 49.0, we expected -1 p. Both manuf. & services slowed further

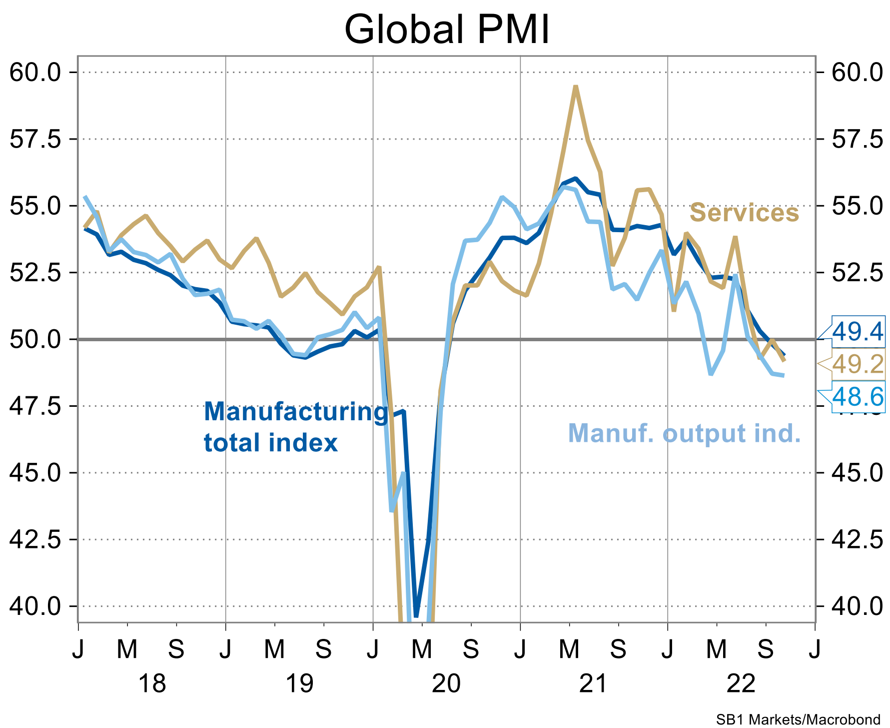


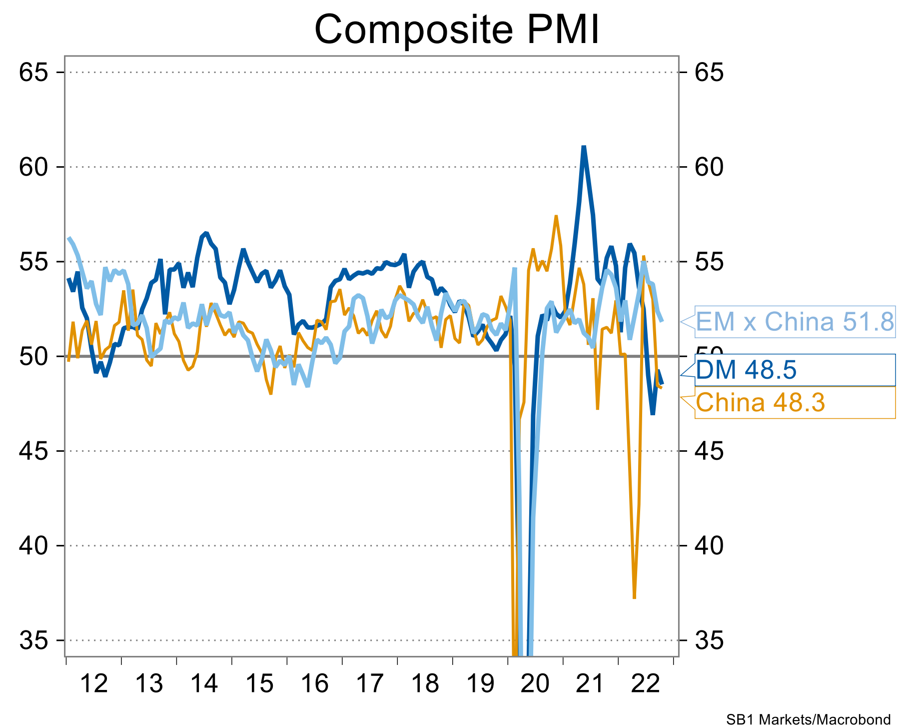


- The composite PMIs are weak in the US (S&P/Markit), the UK, and in the EMU as well, while Caixin's China PMI fell less than we assumed – but remains well below the 50-line
- The German index is at the bottom of the league, as both the manufacturing and the service sector PMIs are very weak.
- The US S&P PMIs are below par too; the ISMs is in sum far better, due to the service sector ISM
- New orders are weak across the EMU, and are declining the US as well

Emerging Markets x China down but still at 51.8. China & rich countries below 50

Both manufacturing and services down in October, and below 50

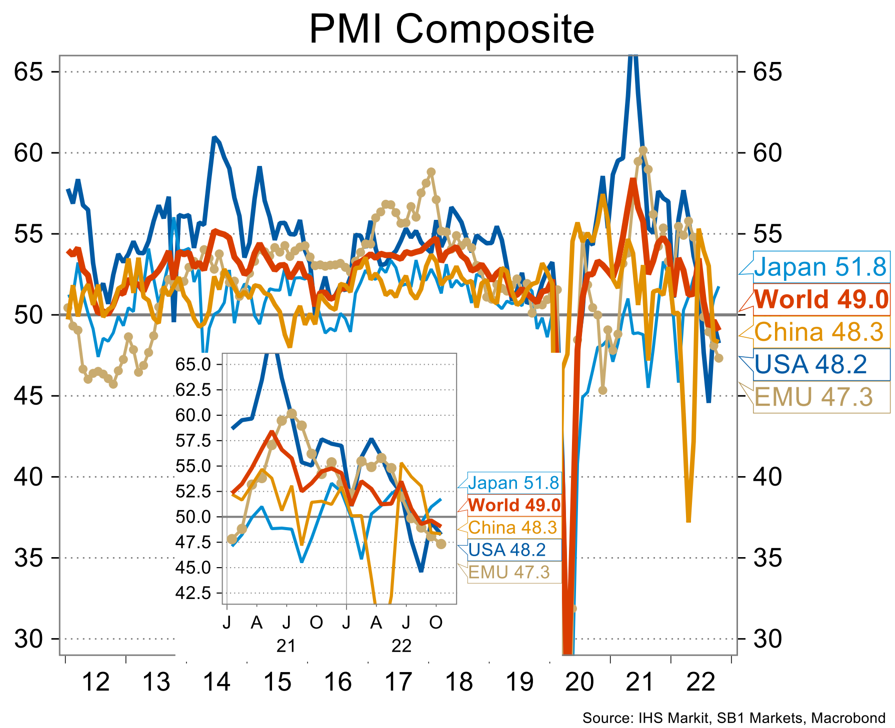


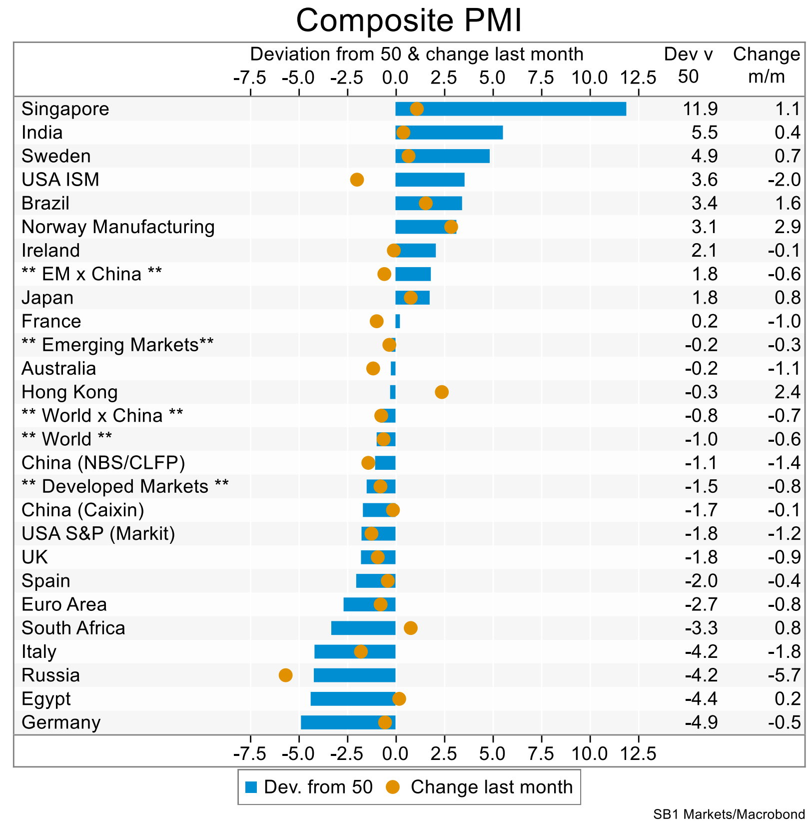


- The output index in manufacturing fell just 0.1 p, to 48.6

20 countries/regions down, 9 up in October

17 countries/regions below the 50 line (including China, EMU, UK, US); 10 are above

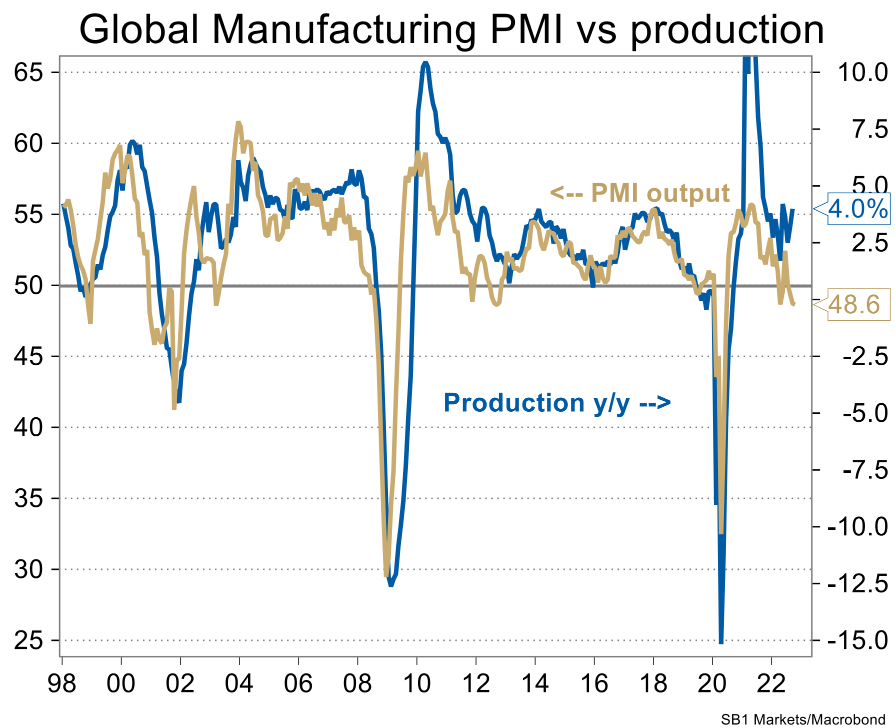


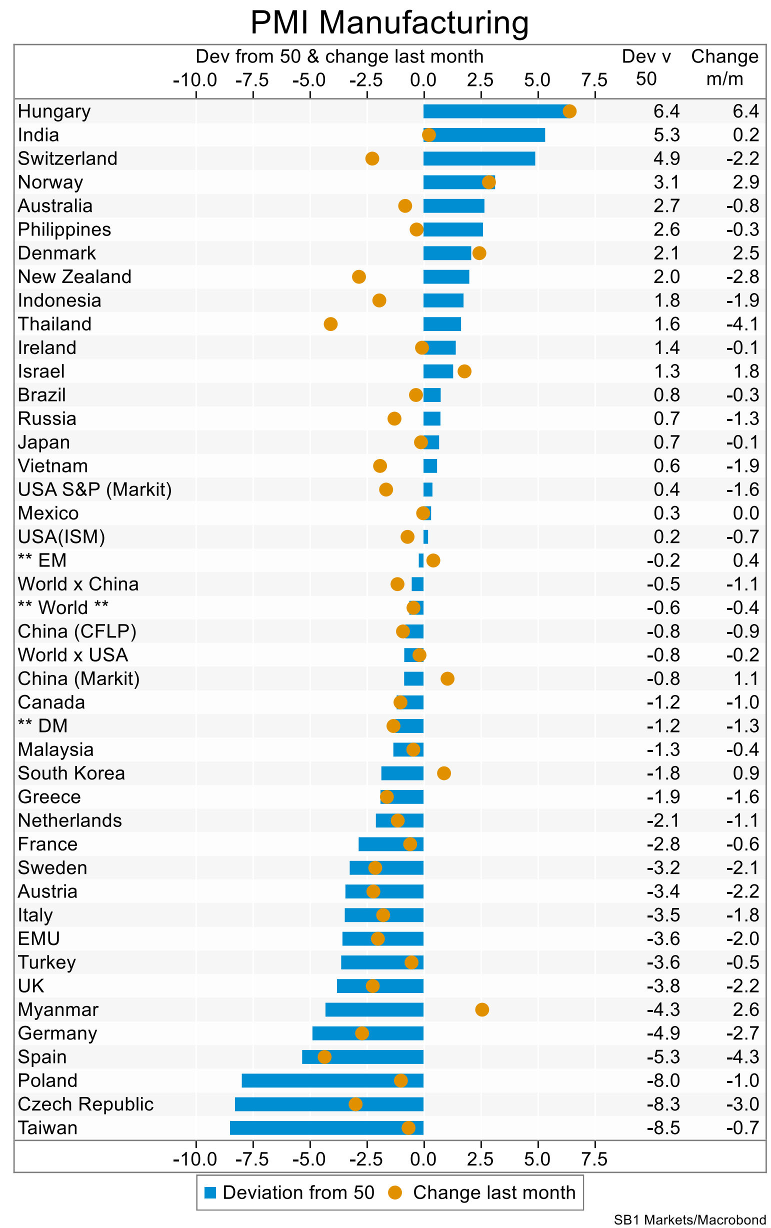


- **The rich countries'** (Developed Markets, DM) PMIs remain well below the global average
  - » A couple of exceptions: The French and Swedish composite PMIs are still above 50 due to strength in the service sector – and the ISM 'composite' is even stronger, for the same reason
  - » The Chinese Caixin PMI fell just 0.1 p to 48.3, we assumed a larger decline
- The **ISM survey** is far better than **S&P's (Markit) US survey** – the ISM 'composite' declined 2.0 p to 53.6, while S&P's PMI fell 1.2 p, but is far weaker, at 48.2. This discrepancy is more than strange – and is entirely due to the diverging service sector indices (ISM covers mostly larger companies)
- (**Norway** does not compete in this league, we just have a manufacturing PMI. The Oct index would have yielded a 6th place in the composite race)

The global PMI signals a decline in manufacturing production, down 0.4 p to 49.4

80% of the PMIs down, and 53% are below the 50-line

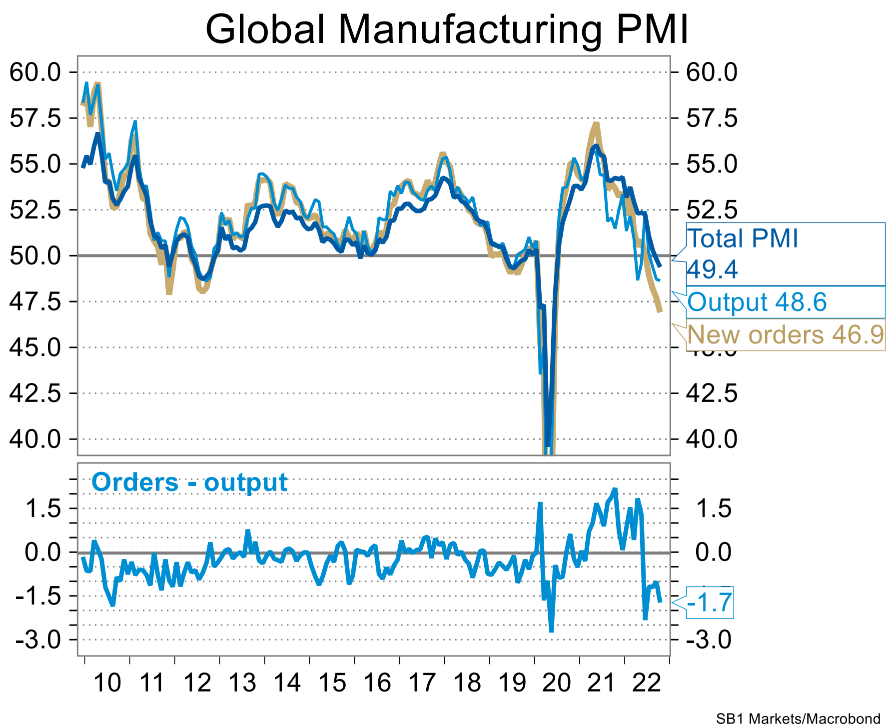


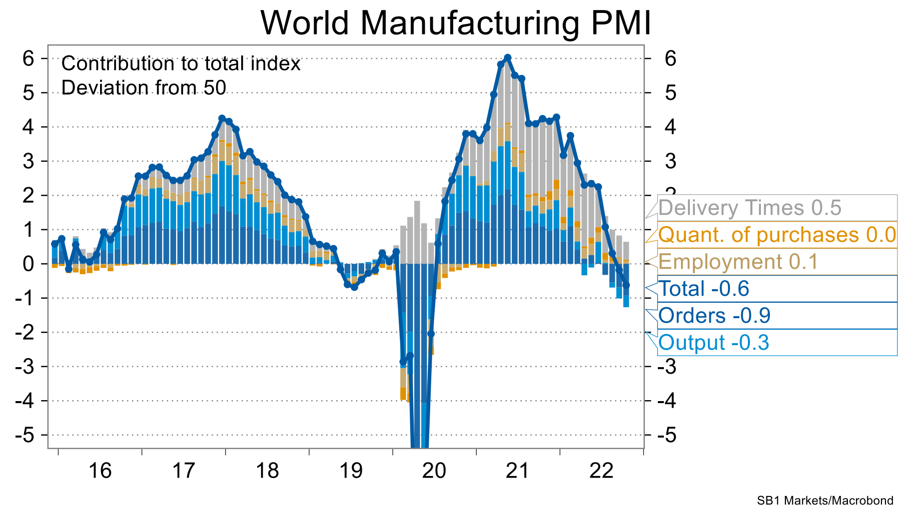


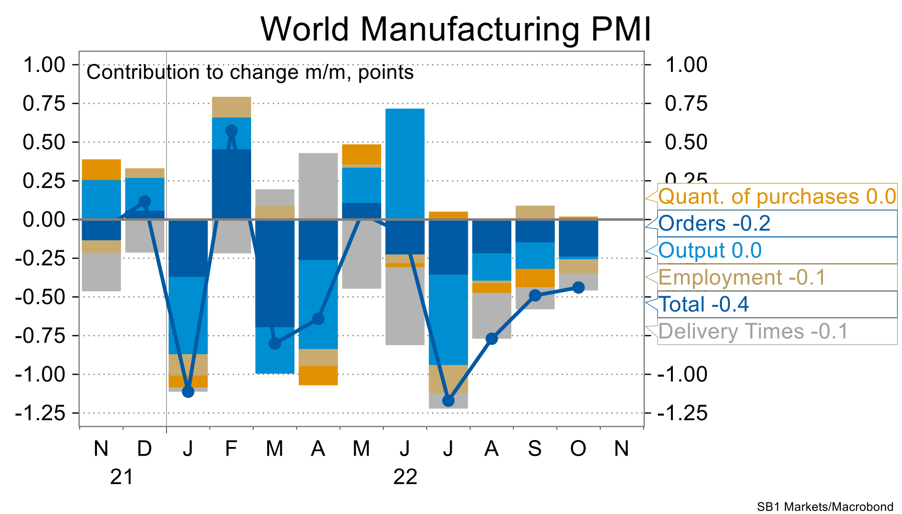
- **The manufacturing** output index fell 0.1 p to 48.6
- **Rich countries are weaker the** Emerging Markets, measured by the total index. Also measured by the new order index, EM x China at 50.1 (and trending flat) are ahead of DM, which 'collapsed' to 44.3!
- **Norway** recovered in October, we believe it is temporary– up to the 4th position globally – with a 53.1 p!
- **Sweden** has fallen rapidly recent months, and further in Oct, by -2.1 p to 46.8

All sub-components of the total index down in Oct

Easing supply problems are good news, but the only reason is waning demand & activity!

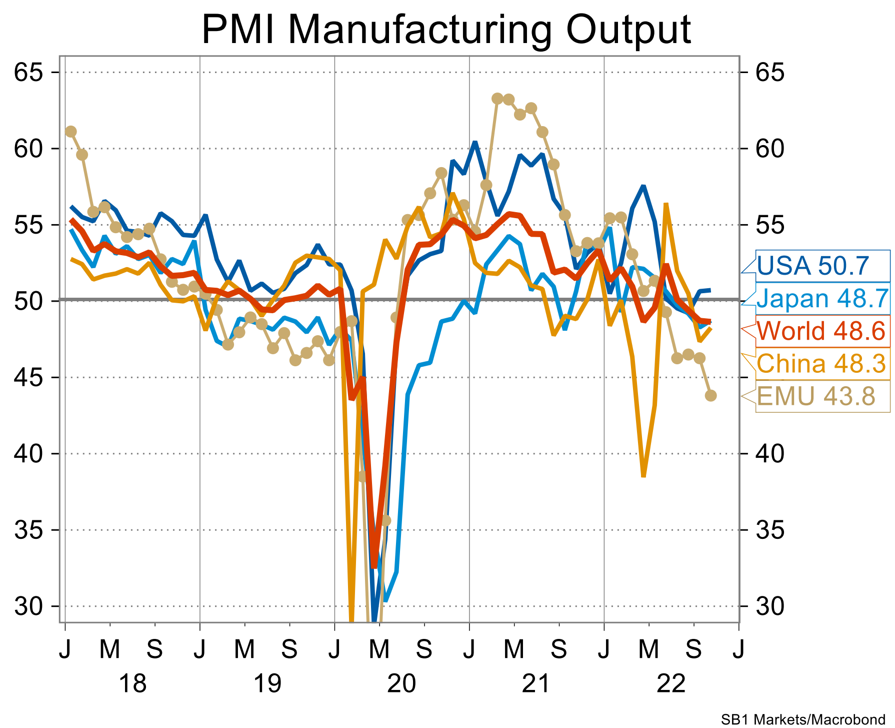


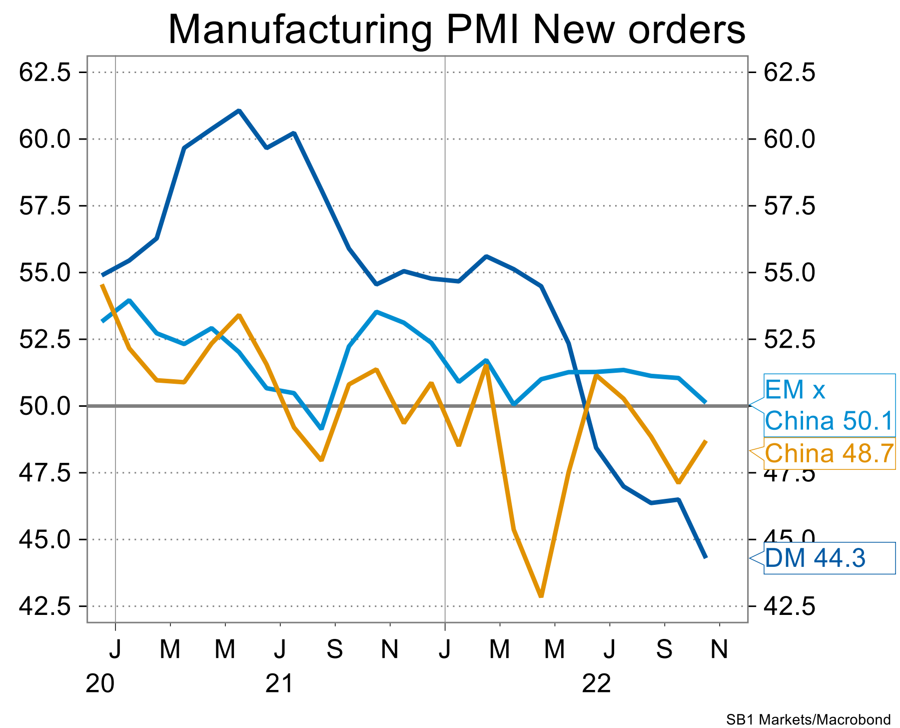




New orders and output are slowing in developed markets; not in EM x China

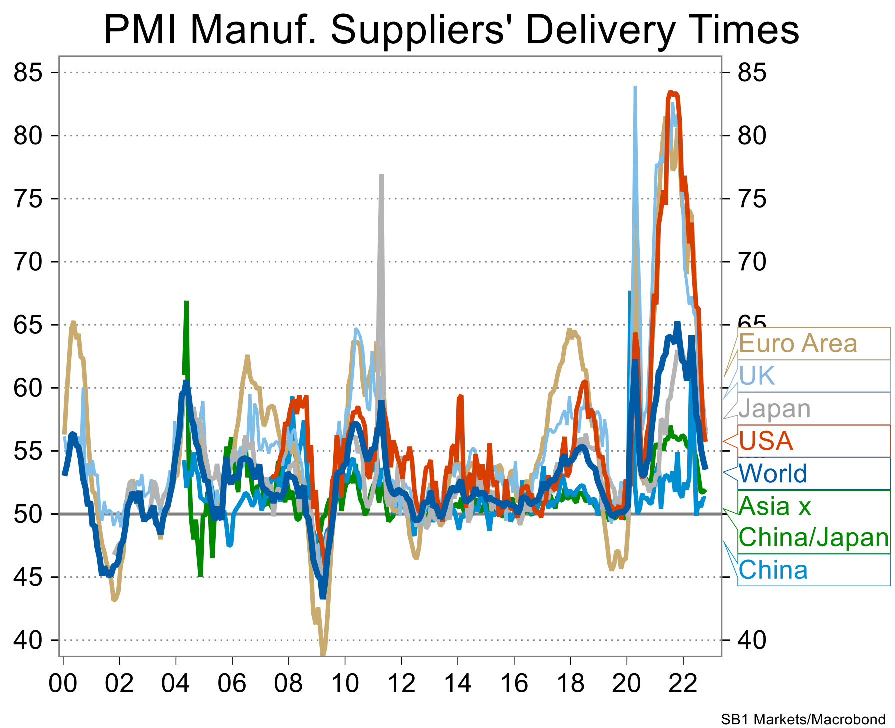
European manufacturers report an steep decline in new orders, taking the DM average down

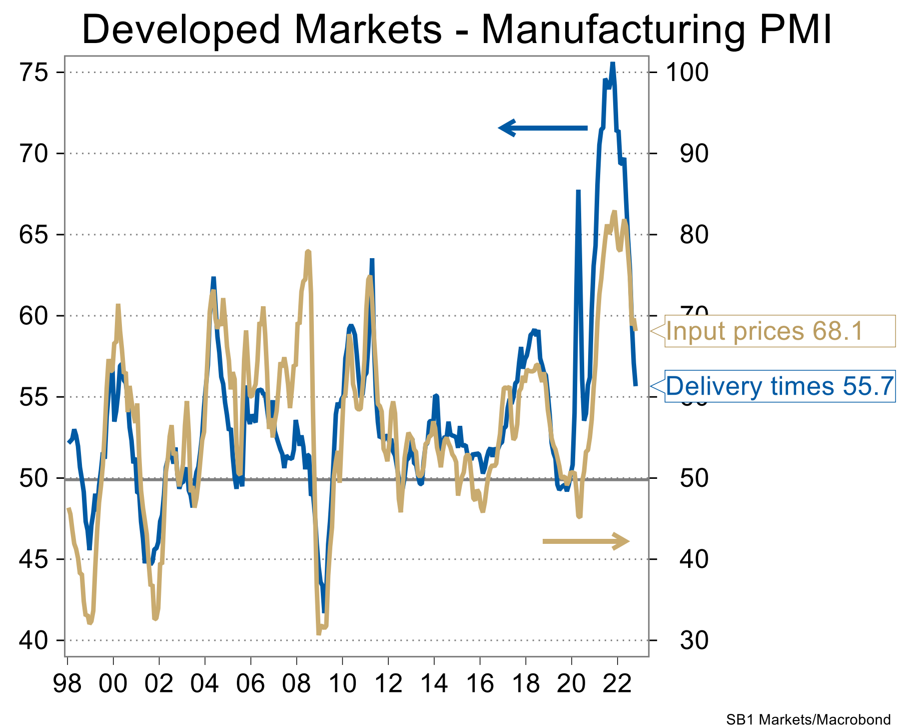




- The US index has stabilised recent months, are is still above the 50-line

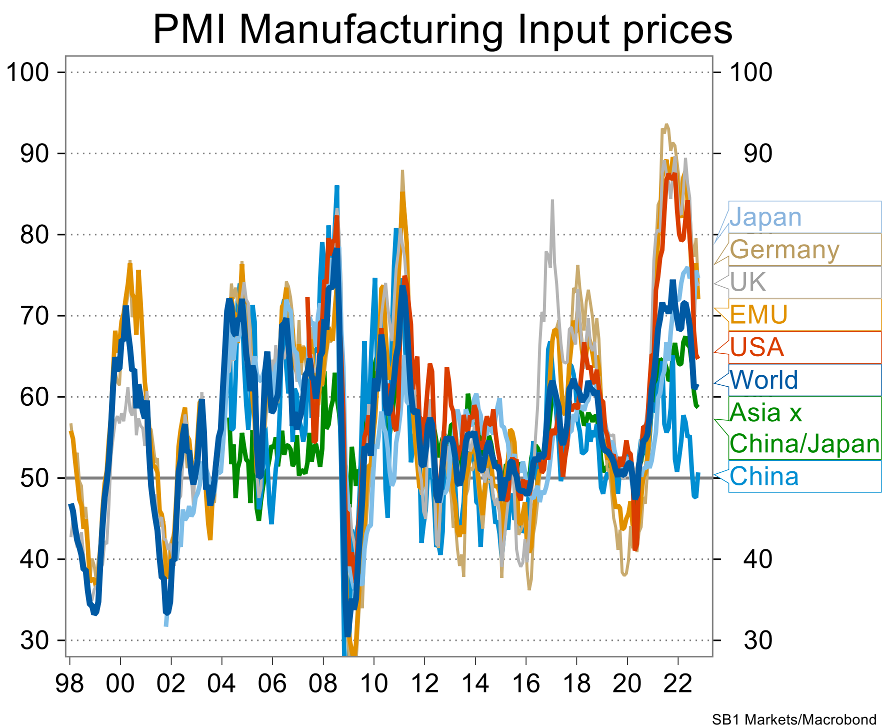
Delivery times and price indices are coming down rapidly, both still above avg.

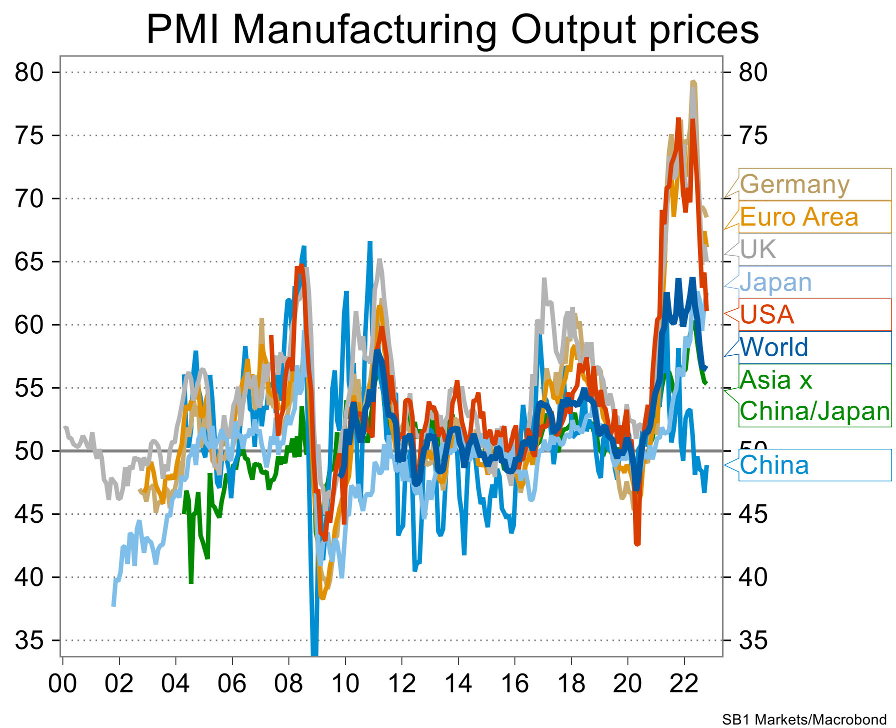




Small changes in price indices in October – and the remain higher than normal

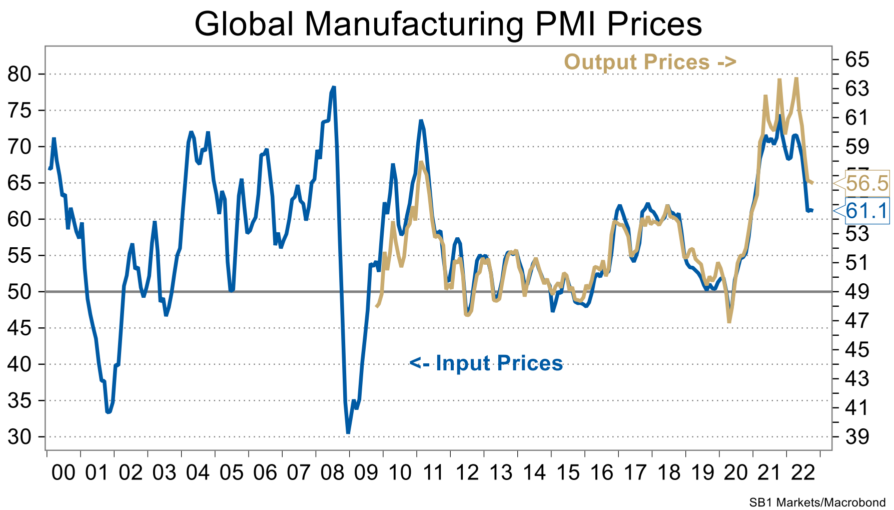
At least ex. China. German/Euro Area output prices are still soaring, companies report. For how long?

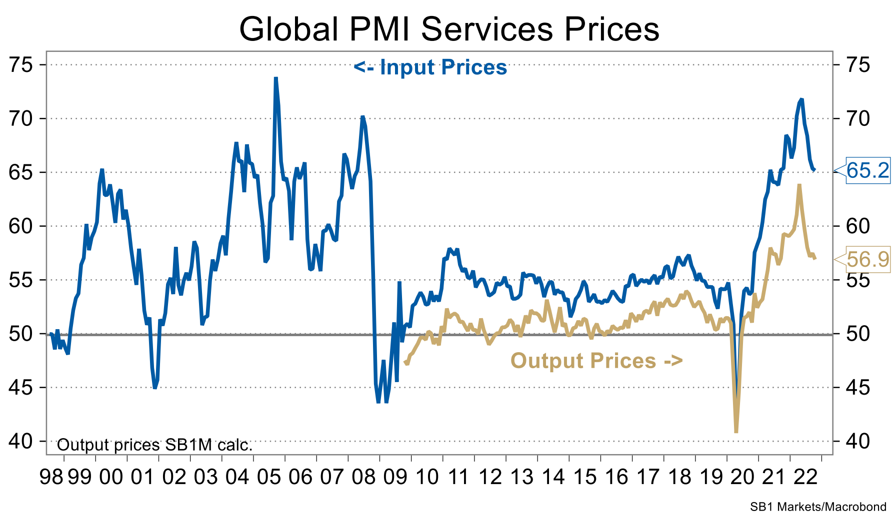


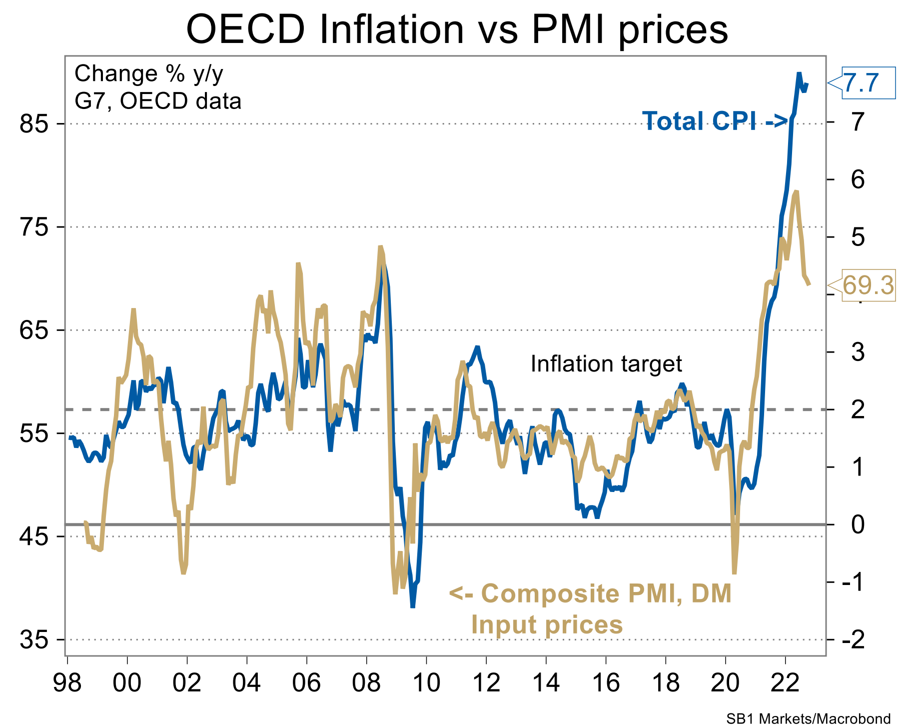


Price increases are slowing, according to the PMIs

All price indices remain at high or very high levels though (like service sector input prices)

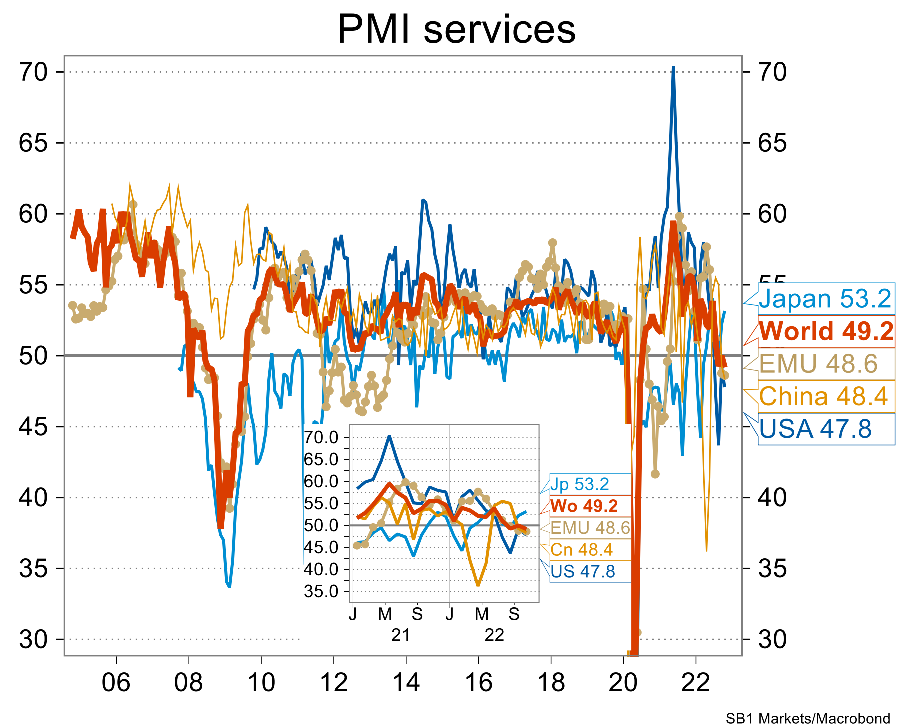


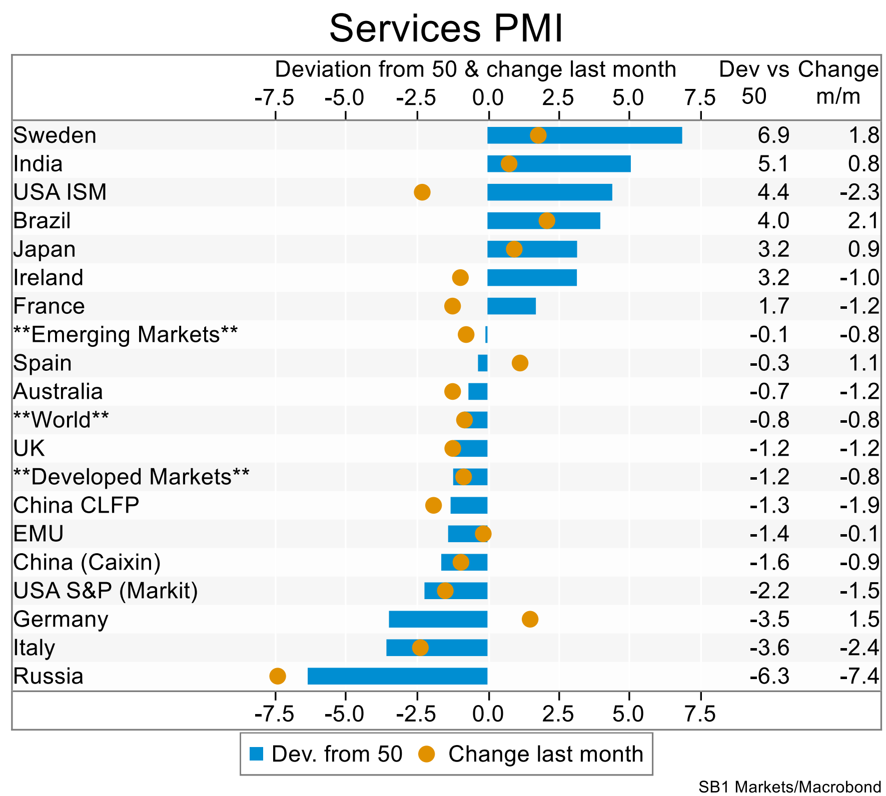




Services PMI down 0.8 p to 49.2, all main regions below the 50-line

Both China, EMU and US below the 50-line

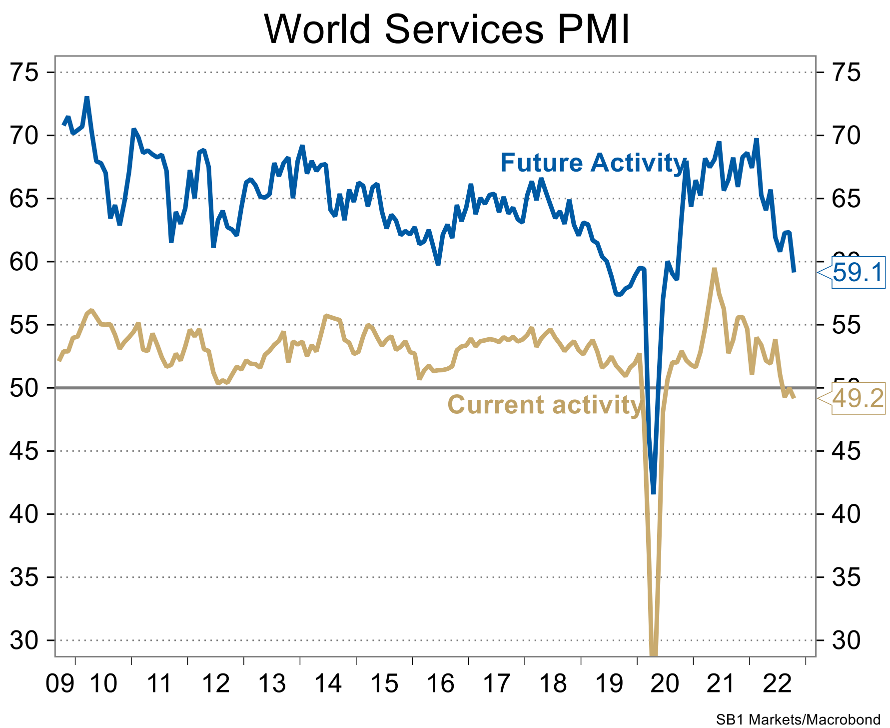


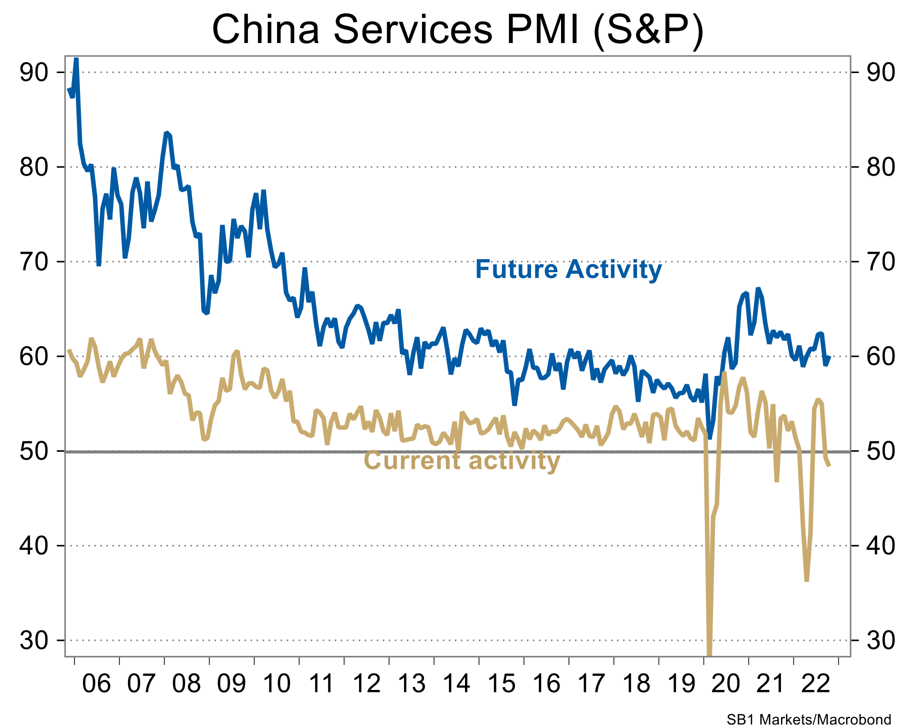


- The Russian index sharply down in October, to the bottom of the list

Future activity aspects in the service sector sharply down

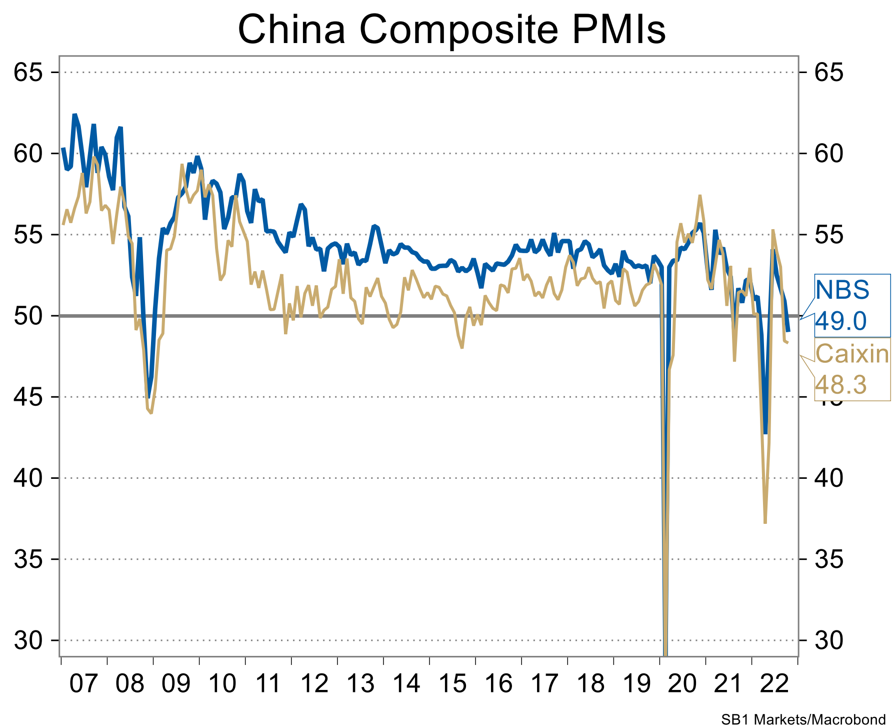
Not far above the lowest level, barring the pandemic trough

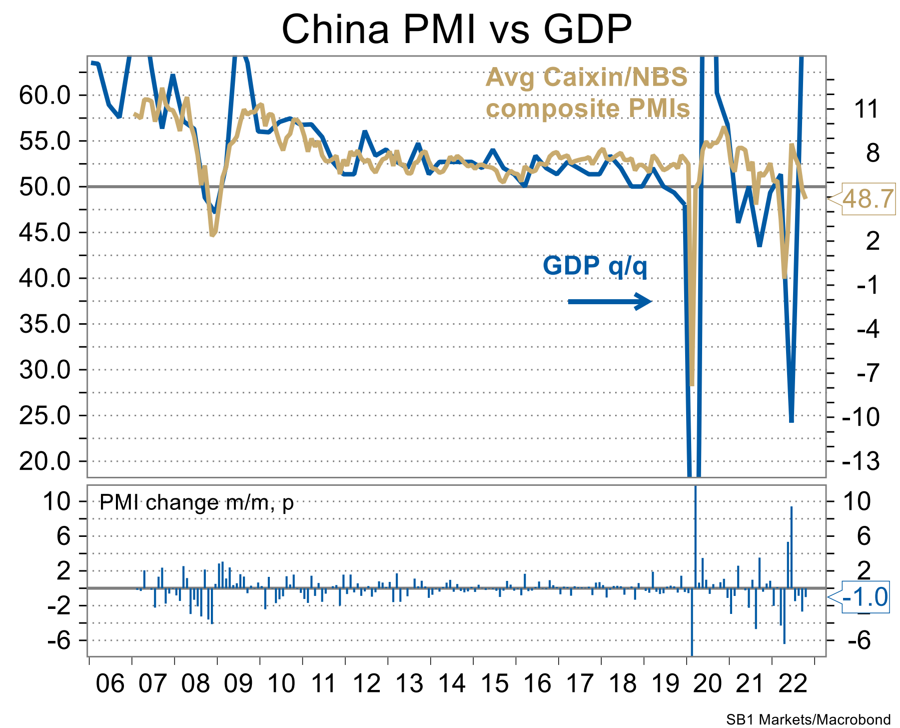




Both PMI data sets down in October – services the main drag

In sum, the PMIs signal modest growth in Q4

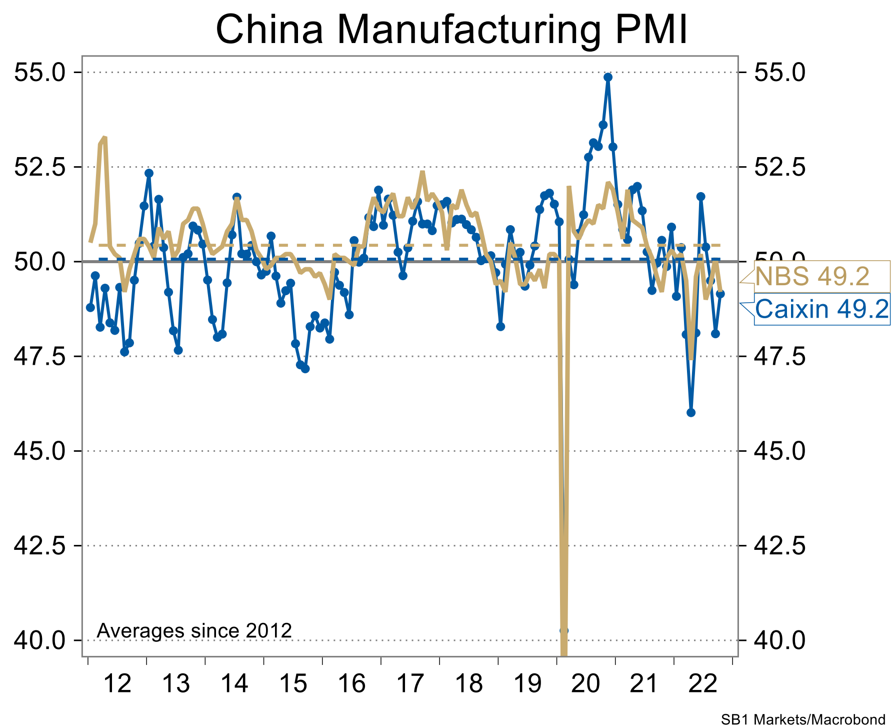


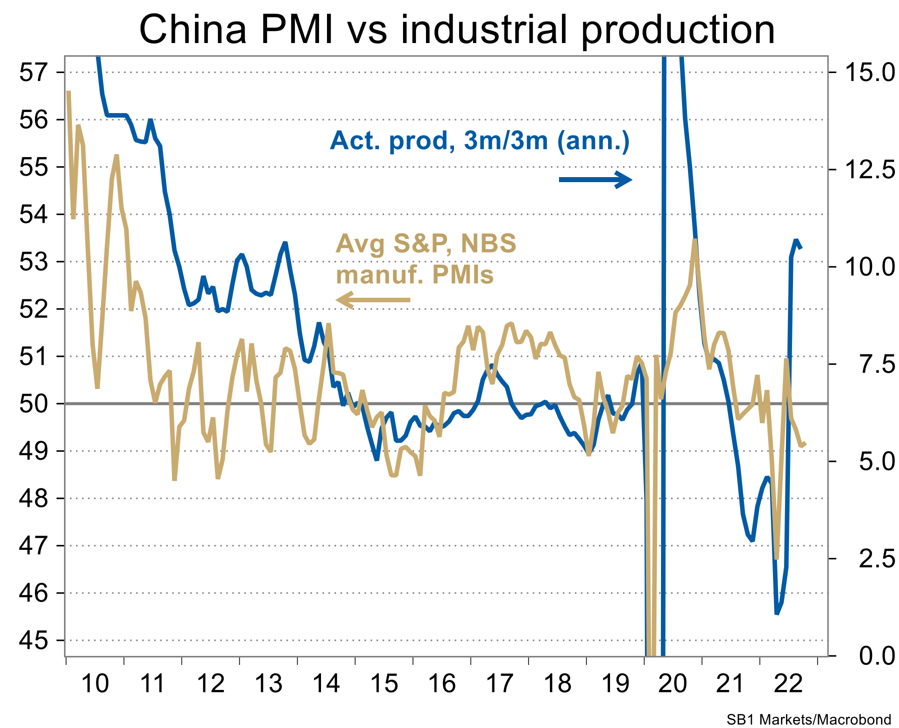


- **GDP** recovered from the weak lockdown Q2, and better than expected in Q3. The October PMI signals far lower growth in Q4
- The **Caixin composite index** fell by 0.3 p to 48.3, expected up 0.4 p. Services surprised on the downside
- The **NBS/CFLP composite PMI** fell by 1.9 p to 49.0, expected just marginally down. The service sector reported a further slowdown to well below trend growth. The manufacturing PMI sector also fell below 50 in October

Both manufacturing data sets equal and below 50, but on average slightly up

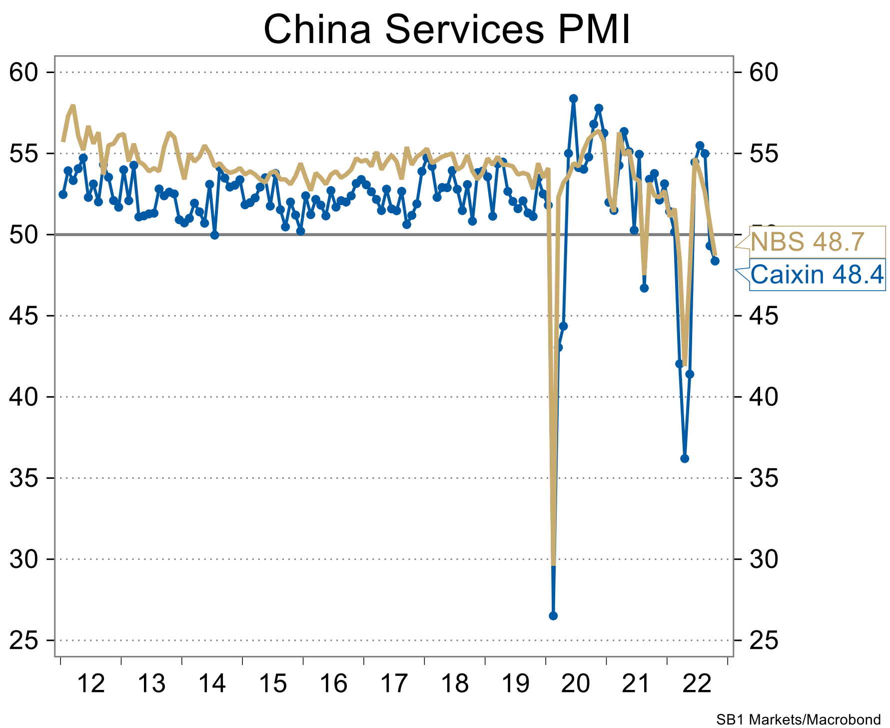
Signals growth below trend

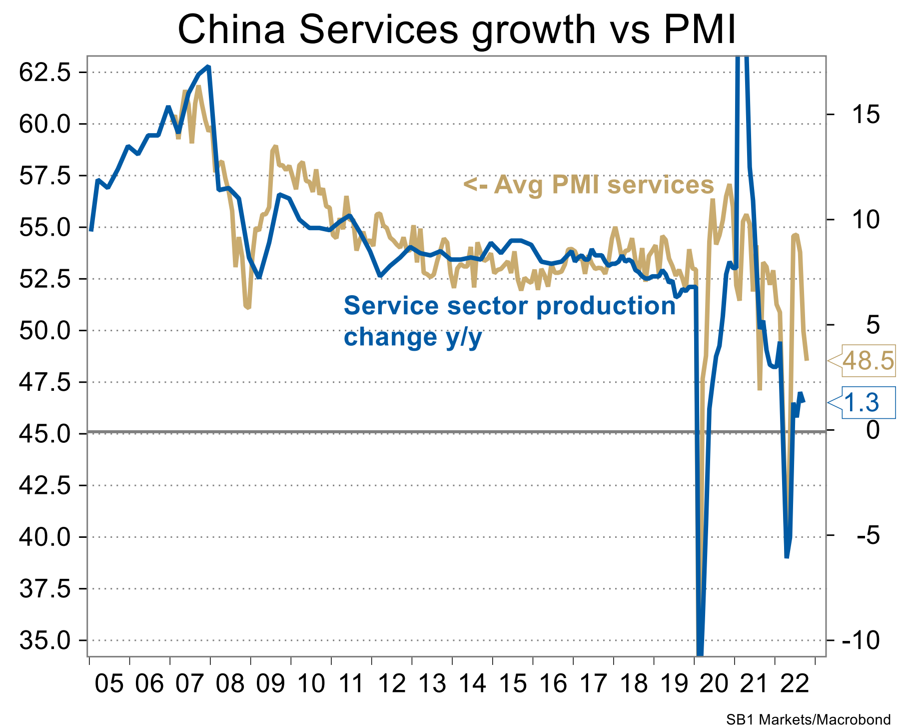




- Actual production rose sharply in May, then grew at a slower pace during the summer and accelerated again in September. The production level is above the growth trend before the lockdowns in the spring

The service sector PMIs were down, and are now well below average



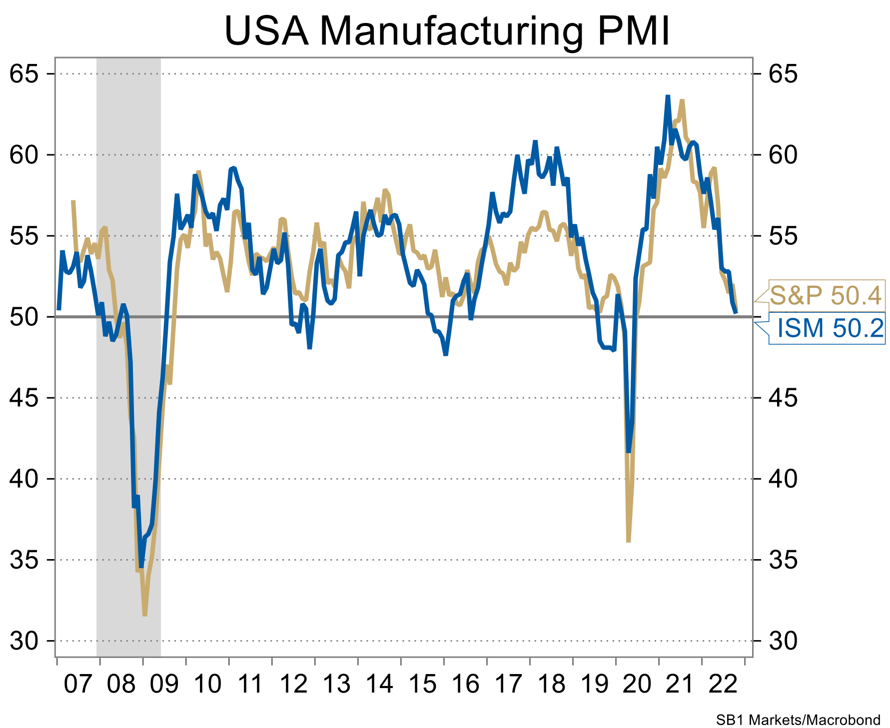


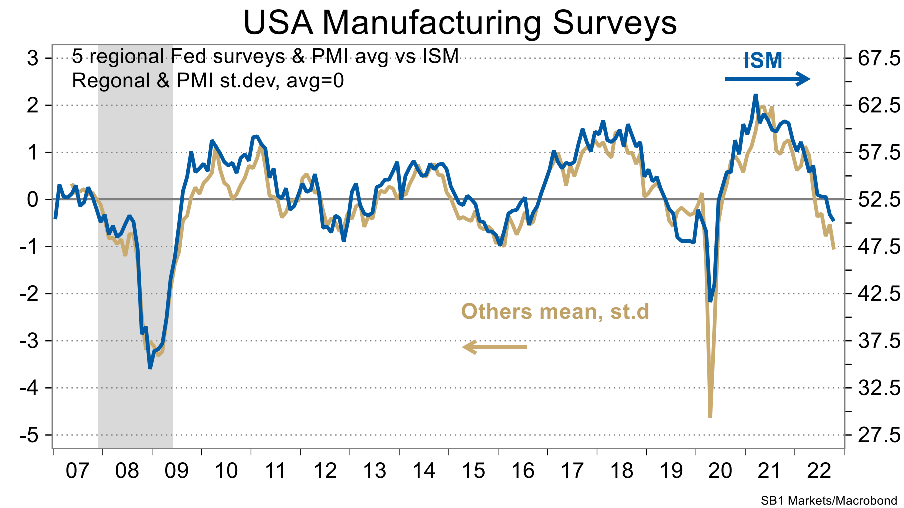
- There were some Covid restrictions in October, and subway transport fell in some few large cities (Guangzhau, Wuhan) but not in Beijing or Shanghai

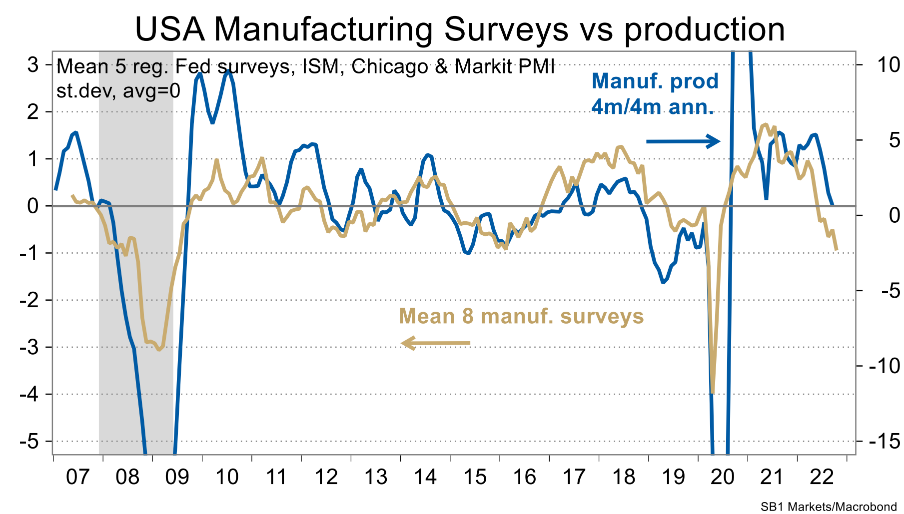
SpareBank 1 MARKETS

Manufacturing surveys: Below average, but sector is still expanding, albeit slowly

The ISM -0.7 p to 50.2, S&P's PMI -1.6 p to 50.4 (but revised up 0.5) – both above expectations



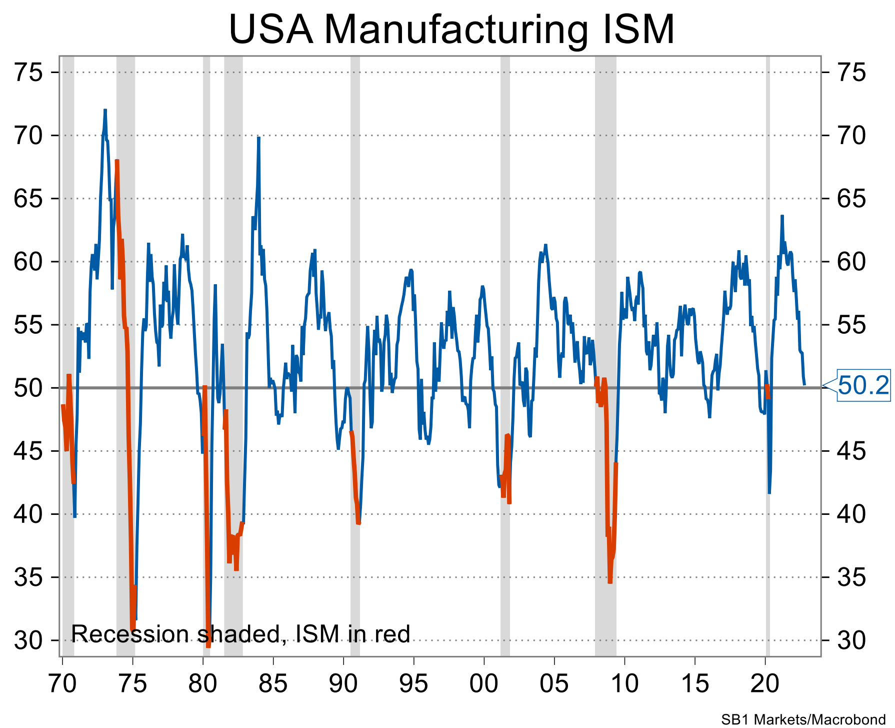




- The trend is clearly down and growth in actual manufacturing production is on the way down too
  - » Other surveys are on average weaker than the PMI & ISM, at a level equalling 47.5
- We expect a continued slowdown the coming months, as orders are unusually weak (if not deep into a recession)

The manufacturing ISM fell further in October, but details not <u>that</u> bad

The index fell 0.7 p to 50.2, expected 50, and the survey remain stronger than other manuf. surveys



The **ISM manufacturing survey** confirms a gradual slowdown in the US economy, but not as much as the average (and median) of other surveys

- In October, 8 of 18 manufacturing sectors reported **growth** (down from 9 in Sept), 10 sectors reported a decline (up from 7)
- The **new orders** index was up 2.1 p, even if exports orders fell faster. The total new orders index remained contractionary territory at 49.2. 12 of 18 sectors reporting declining orders, which is one less than last month, but still very weak. Other surveys agree. The **order backlog** is also declining rapidly
- The **production** index rose 1.7 p to 52.3, which is slightly below an average level. The **employment** index rose 1.3 p to 50 in October, after falling 5.5 p in September. Labour demand is still softer than at the peak and the ISM reports that more companies are implementing hiring freezes
- So why did the total index decline? The **delivery times** index fell sharply, by 5.6 p to 46.8 as **supply chain** issues are dissipating: 9 commodities saw **price increases** (from 15 last month and 40 in May, and 56 at the peak). 17 were down in price, like aluminium, steel, and lumber. This is up from 16 in September. 9 commodities were reported in **short supply**, up from 7 in Sept (but far below the peak at 50 commodities a few months ago)
- In addition, the **inventory** index fell 3 p, which is not necessarily bad news. Taken together, deliveries and inventories lowered the ISM total index by 1.7 p. The order components contributed on the upside
- The input **price** index fell sharply to 49.4, signalling falling prices!
- **Comments** are mixed – many are still reporting that labour is a scarce commodity, but several are acknowledging a slowdown in demand, and that competition is increasing

SpareBank 1 MARKETS

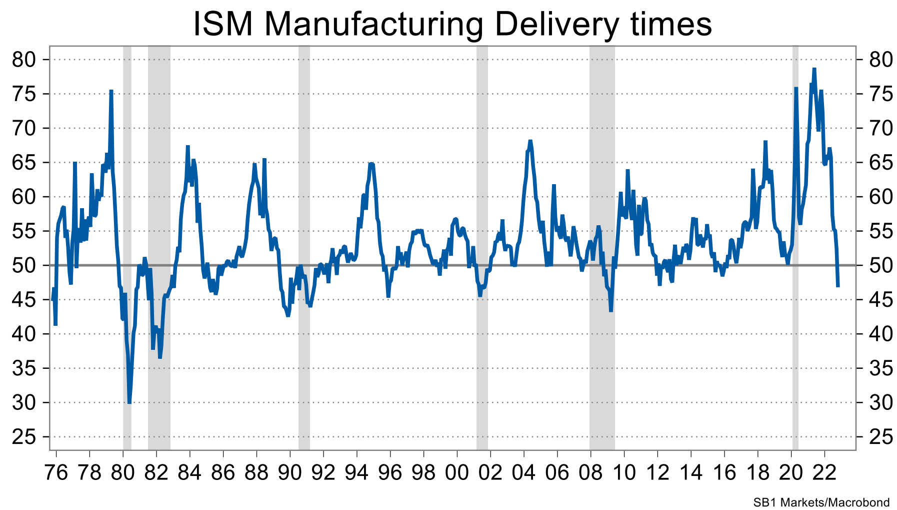
A warning sign: At the current pace of contraction in new orders…

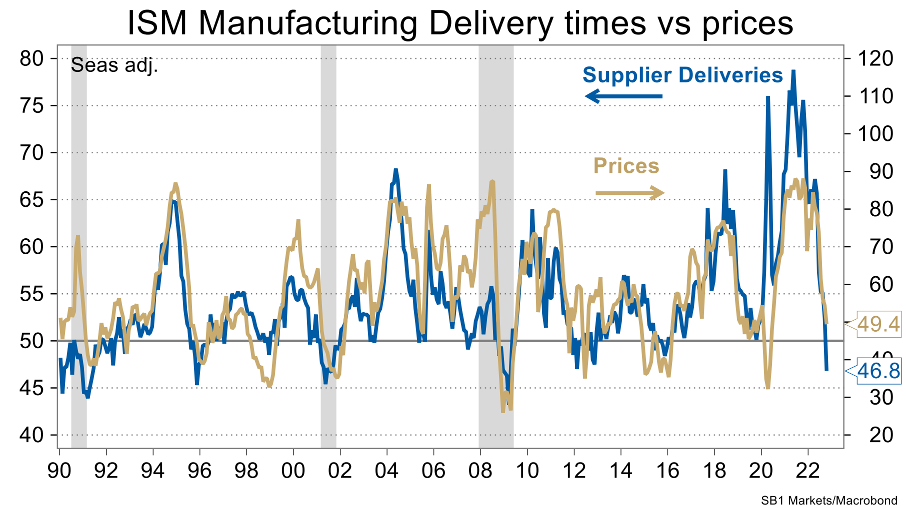
…a recession usually follows. The '95 soft landing is the only exception.

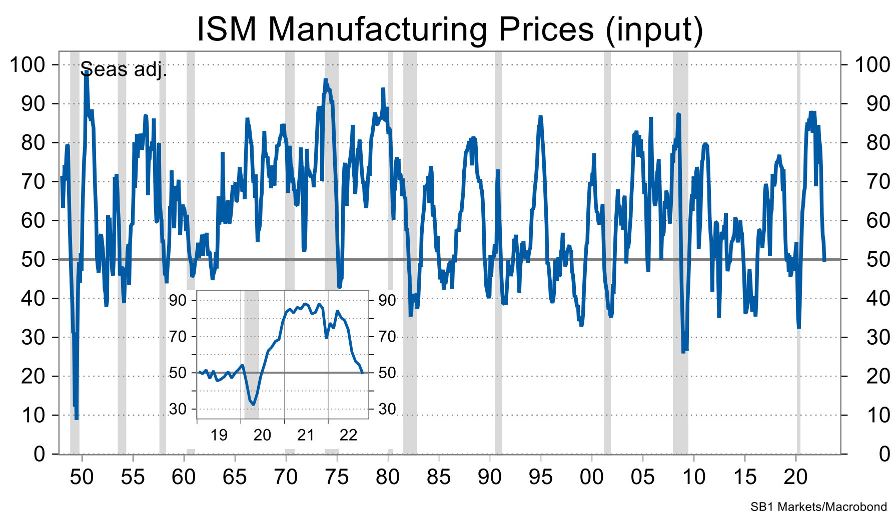
The other 6 contractions are the past 6 recessions

The delivery times index and the input price index are both below average

The price index is now at 49.4, and the delivery index at 46.8!





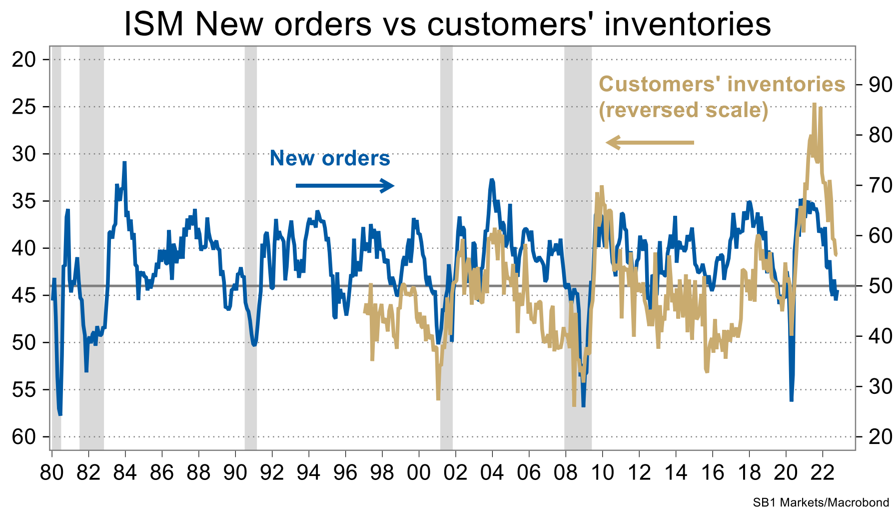


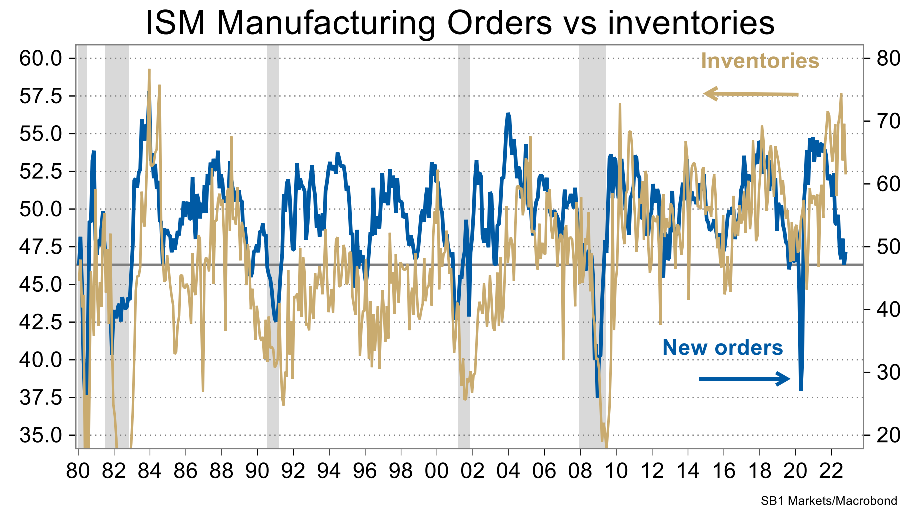
- No more price increases!
- The supplier deliveries index has fallen to 47 in October from 67 in April, implying shorter delivery times and supply-side issues seem to be history – because demand has slowed sharply

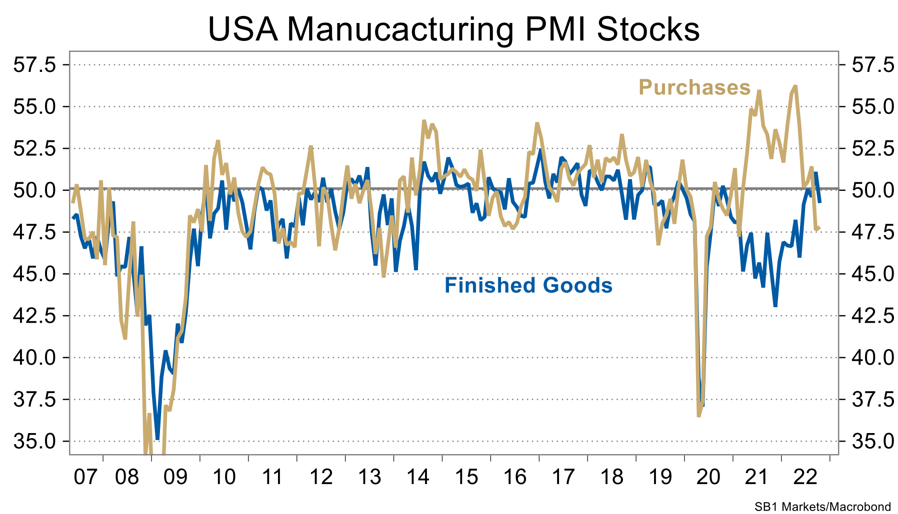
SpareBank 1 MARKETS

Customers' stocks are decreasing but slower, says the manufacturers

.... Implying far faster growth in orders than the current new order index implies







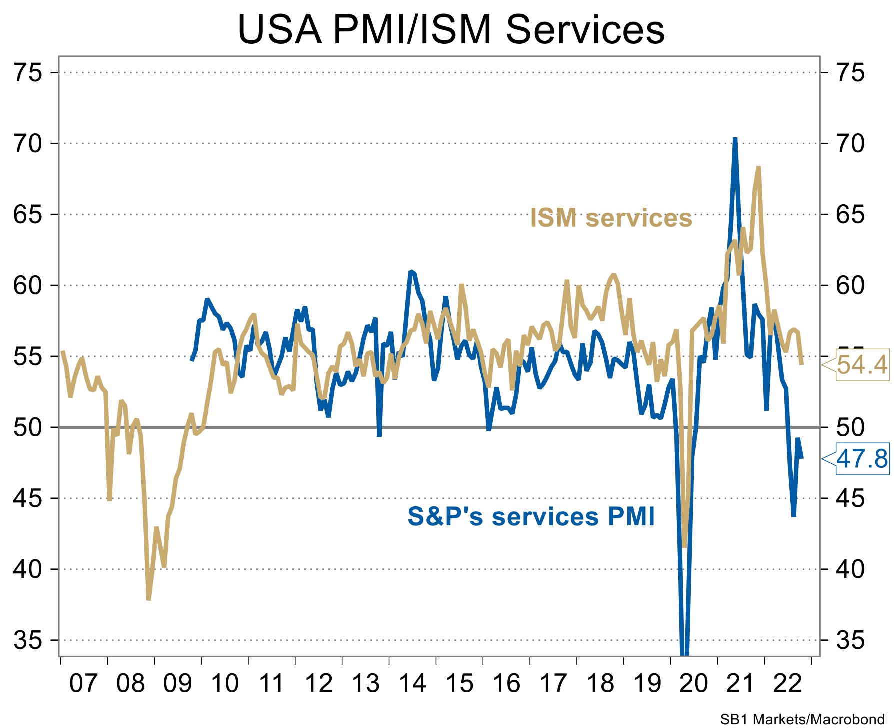
Mixed on own inventories

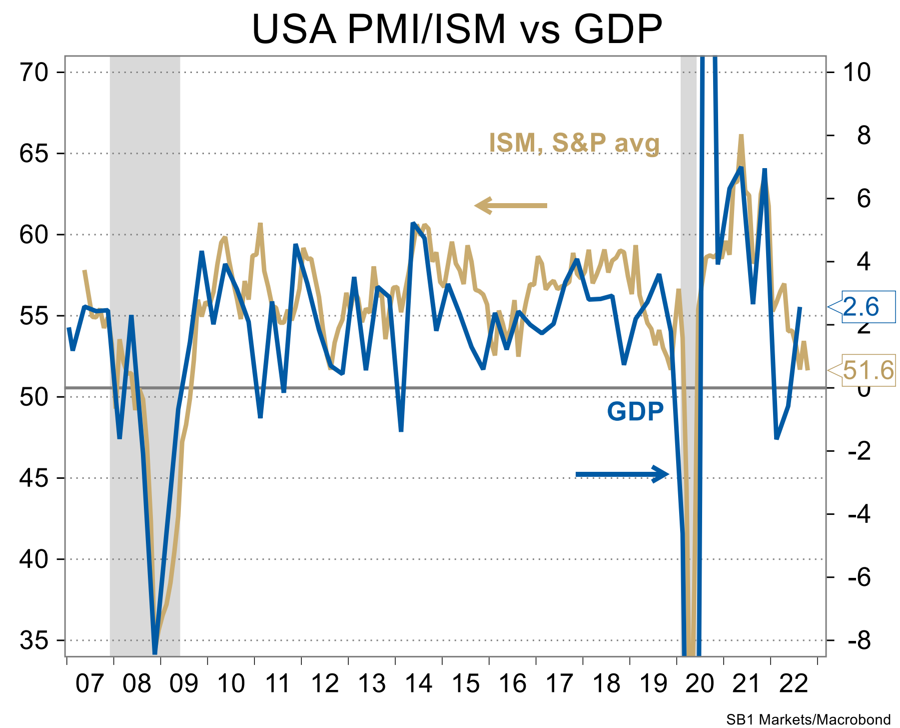
- ISM reports lower growth in inventories of purchases in the manufacturing sector in October, but still much faster growth than normal. Most likely, companies will cut back on purchases, to bring growth in purchases down. However, the PMI tells another story:
- The PMI survey (S&P/Markit) reports falling inventories of purchases, and close to unchanged finished goods inventories

SpareBank 1 MARKETS

Mind the gap: S&P says services are contracting, while the ISM reports OK growth

In average, slow growth is signalled – also if manufacturing surveys are included



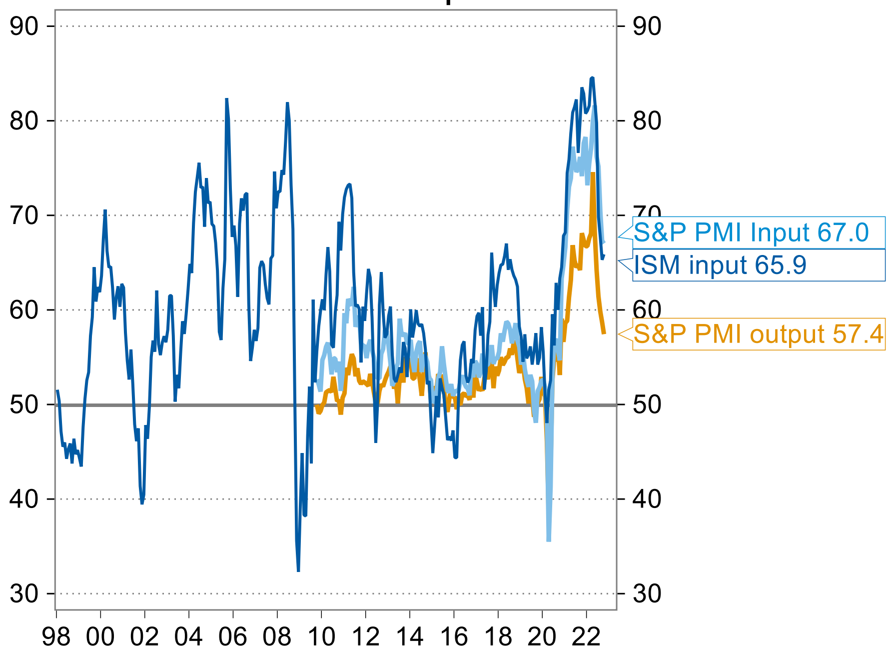


- The history of the two surveys are too similar and too short to judge which one is better
- But so far, the ISM seems to be more correct, the service sector has not been contracting the recent months
- The **ISM services** index was down 2.3 p to 54.4, expected down to 55.5. This survey is tilted towards the larger companies compared to the S&P survey. Even if the new order index was down 4.1 p, the 56.5 level signals decent growth. Input prices are increasing a little faster according to the ISM, and slower than reported by the S&P index, which still reports very fast price increases
  - » Comments were in general much weaker than signalled by the actual index numbers
  - » 16 sectors reported growth, just 2 a decline: Management & support services, and Real estate
- **S&P's services PMI** (aka Markit's) was higher than the preliminary PMI, but remained below 50
- The **average** of the composite ISM and PMI fell 1.8 p to 51.6, the lowest since the start of the pandemic – which implies less than 1% GDP growth

PMI reports slower growth in prices, the ISM not

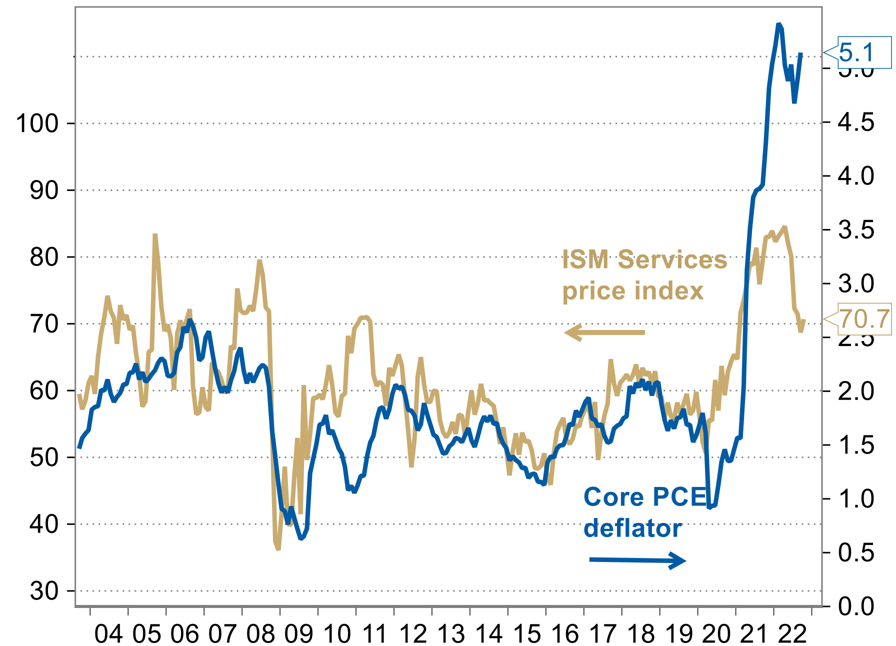
However, the ISM is still reporting slower price growth than the PMI

USA PMI/ISM Composite Price Indices



SB1 Markets/Macrobond

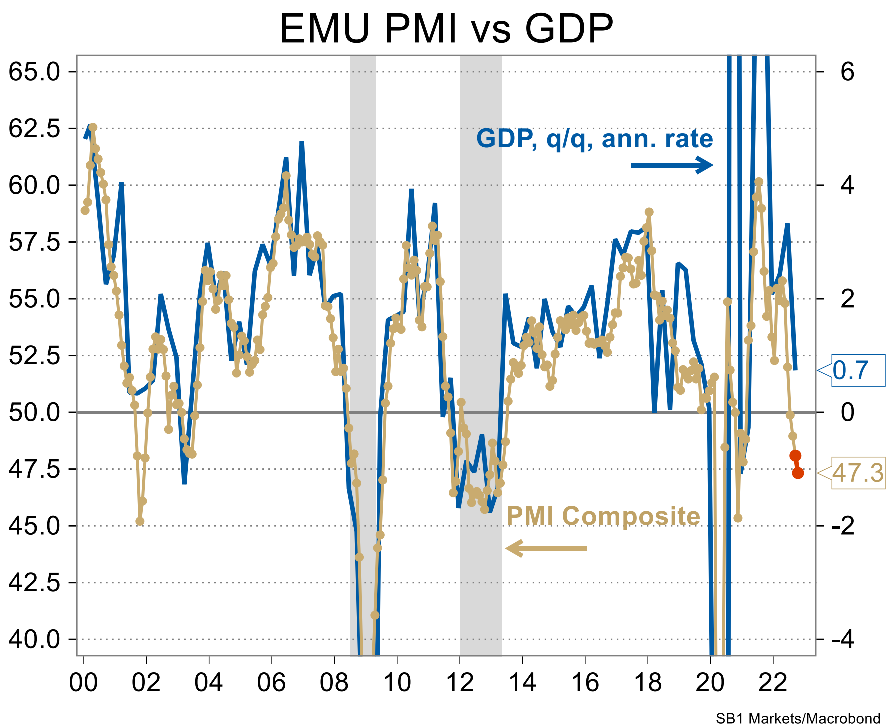
USA ISM Prices vs core PCE

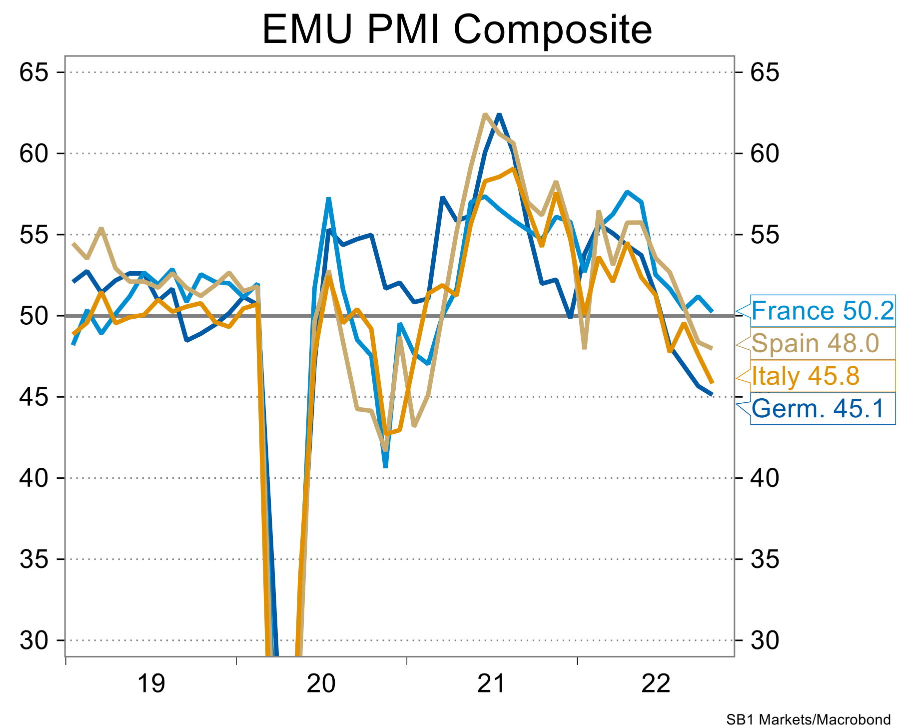


SB1 Markets/Macrobond

The Eurozone final PMIs confirmed in contractionary territory, but no full crisis

The composite down 0.8 p to 47.3; data weaker everywhere but the German & Spanish service sectors

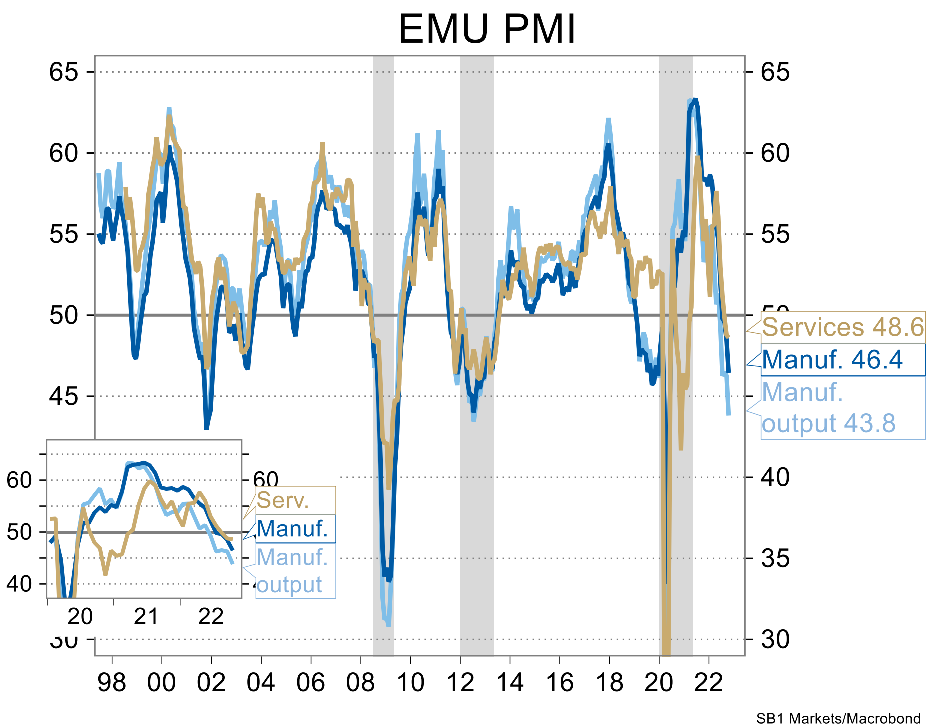




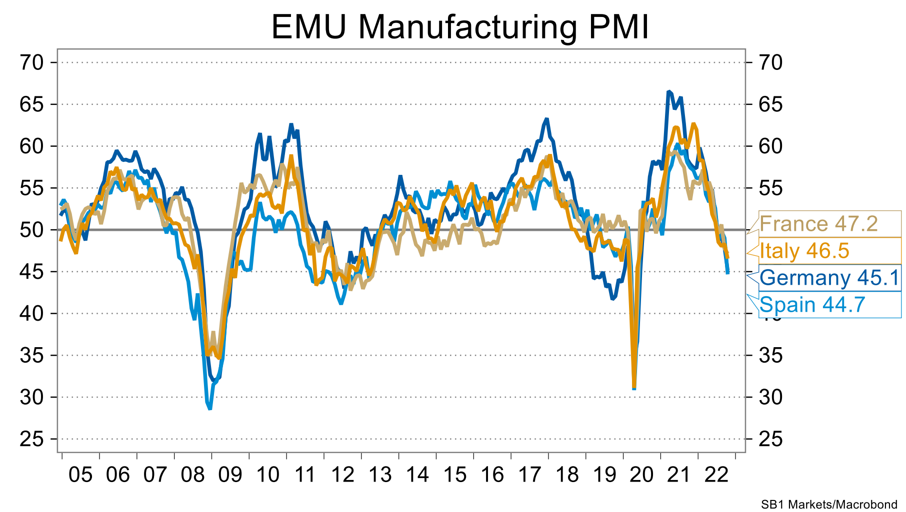
- The EMU composite PMI was 0.2 p higher than the flash estimate, but down from September. The Italian service PMI, and the German and Spanish manufacturing PMIs fell the most. However, the French and German service sector PMIs were stronger than initially reported. Apart from France, the PMIs are all weak though
- The **service PMI**, **manufacturing PMI** and the **manufacturing output** index all fell in October
- The sum of the parts for the Eurozone points to around a 1% contraction in GDP. In Q3, GDP grew 0.7%
- The October PMIs, like the previous month, bear sign of higher energy costs and higher interest rates, as well as lower global demand, as demonstrated by the lower new order indices, also from export markets

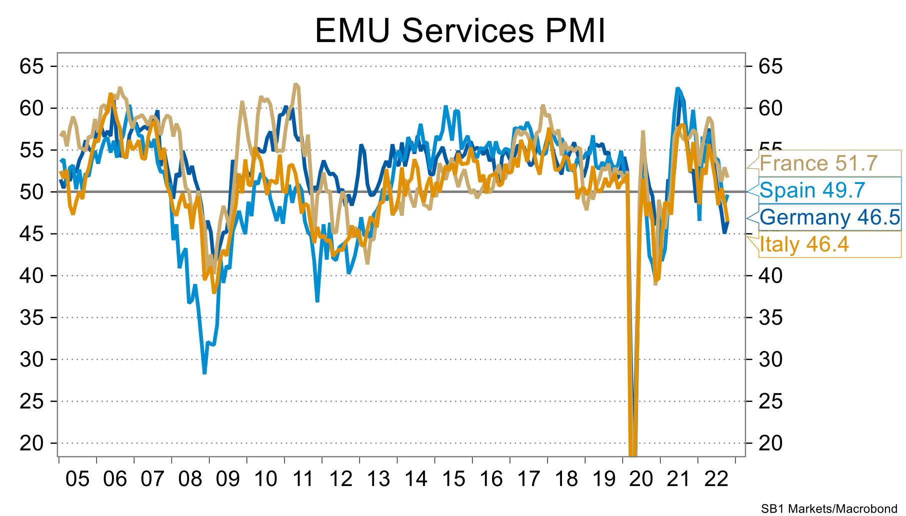
Manufacturing and services PMIs further down in the Eurozone

Manufacturing below 50 in all of the big 4 – Services above 50 only in France



- The manufacturing output component is a warning sign. And even more the order index (which fell to the lowest level since April-09 (barring the prints during the pandemic)

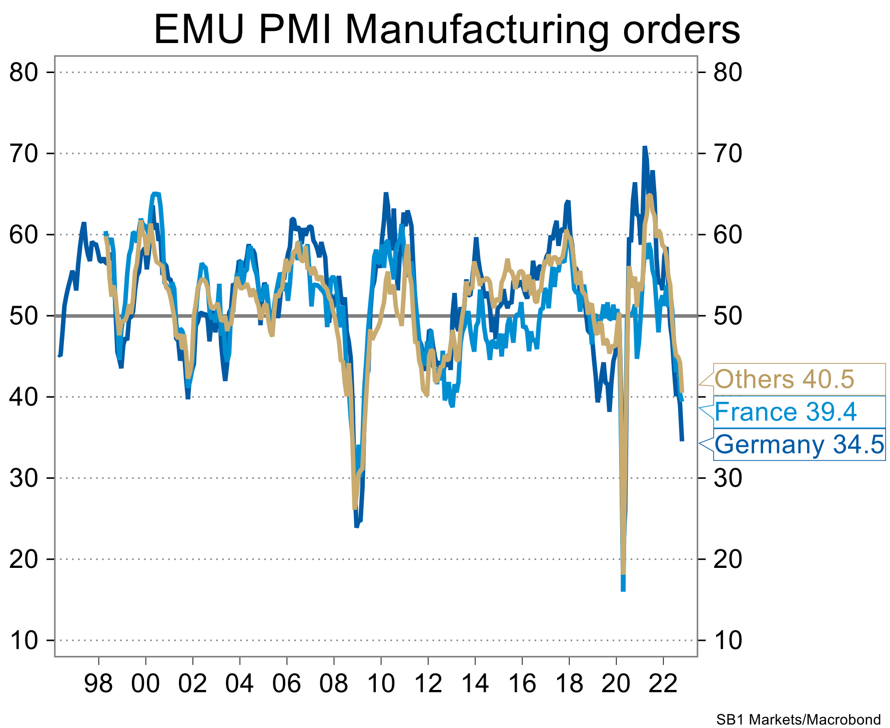


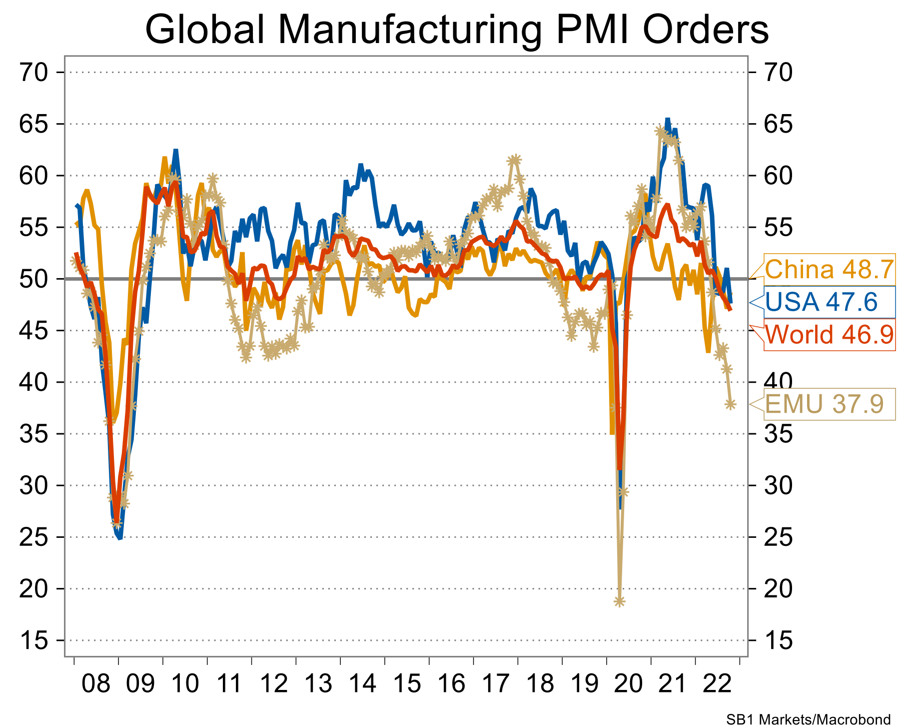


SpareBank 1 MARKETS

European new orders are falling very rapidly

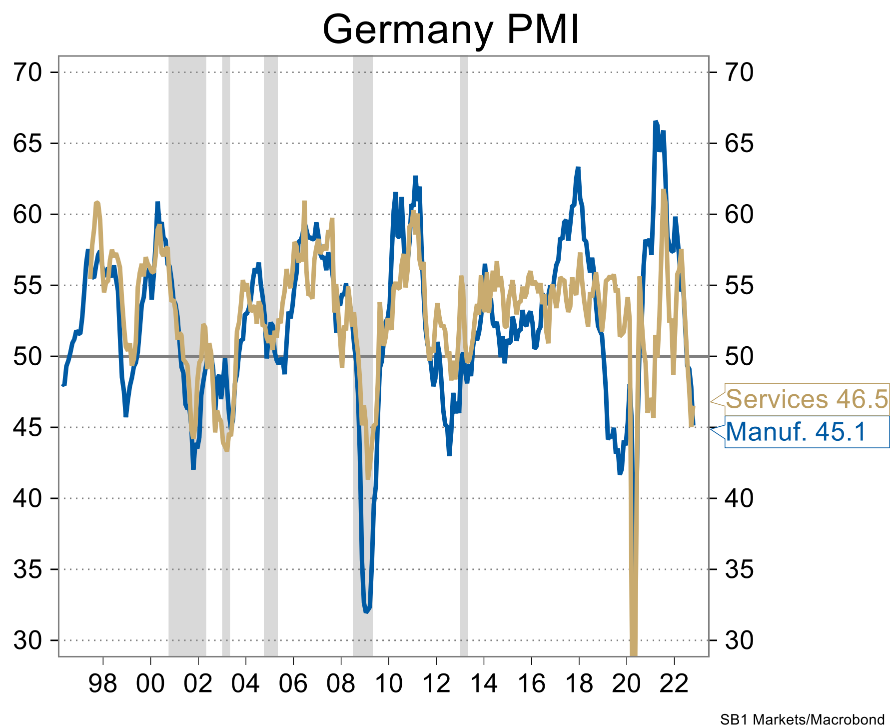
No doubt, the manufacturing sector in EMU is heading for a deep downturn, Germany in the lead

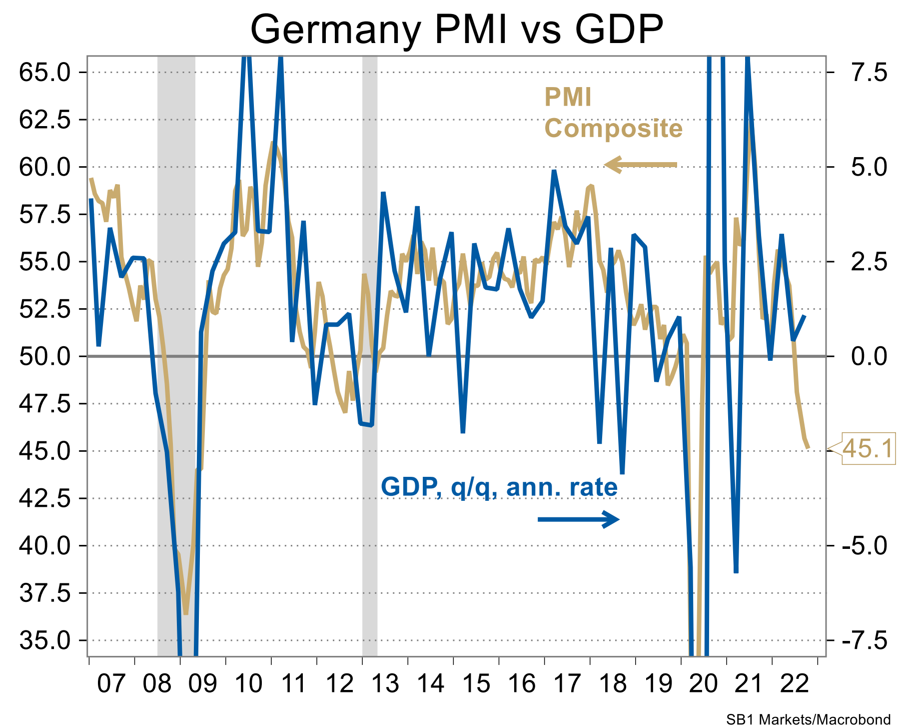




Germany: The composite PMI now signals some 2.5% fall in GDP

Services came in far better than the flash estimate but still low, of course

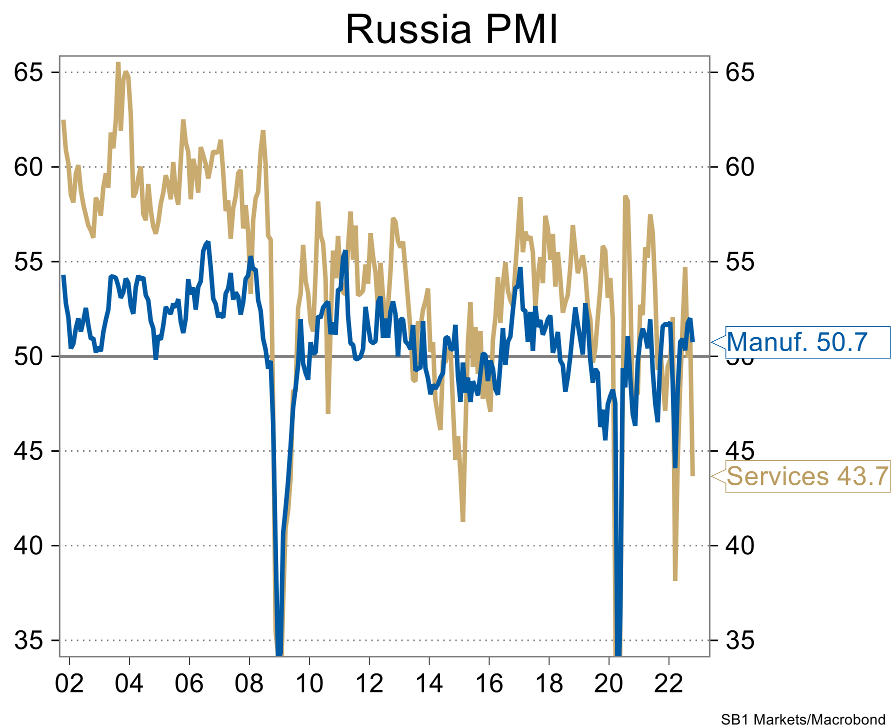


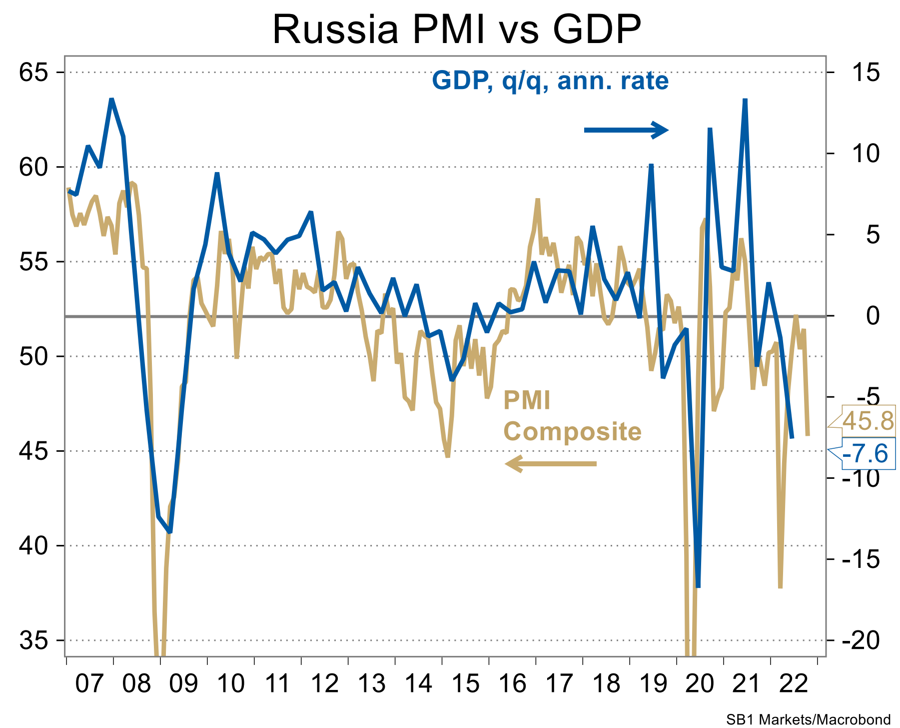


- The composite PMI is down 0.6 p to 45.1 in October, which is 1 p higher than the preliminary print
  - » The service sector PMI rose by 1.5 p to 46.5, vs 44.9 in mid October. High inflation, higher interest rates, and an uncertain outlook (war & energy prices) in dampening demand
  - » The manufacturing sector PMI fell 2.7 p to 45.1, which is the lowest level since June-20. The fall was driven by a sharp fall in new orders and higher input prices (mainly energy)

Russian PMI down the drain in October

The service sector PMI was particularly weak and fell 7.4 p to 43.7; manuf. PMI was down 1.3 p

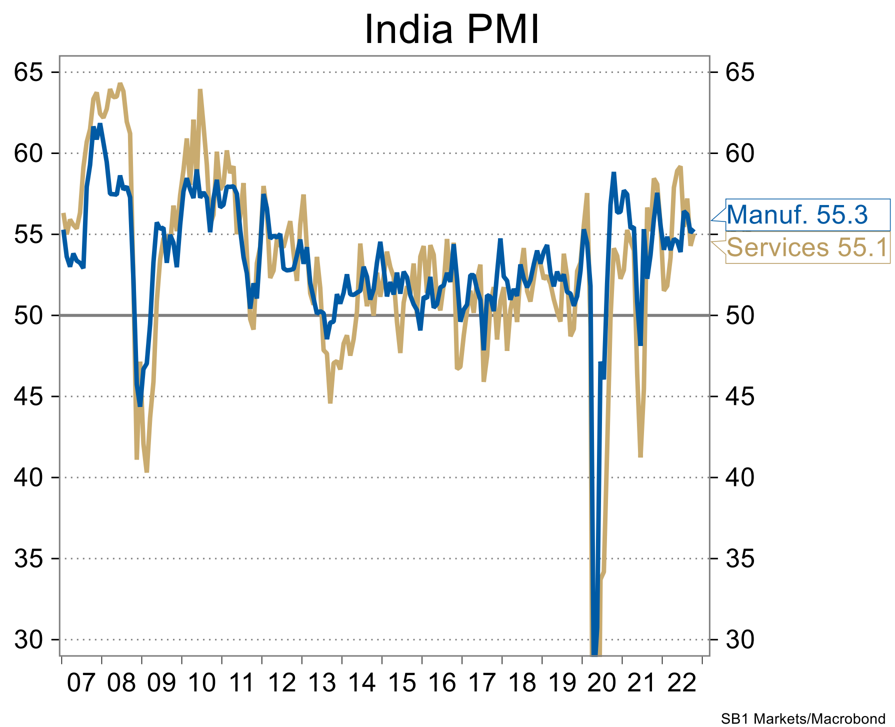


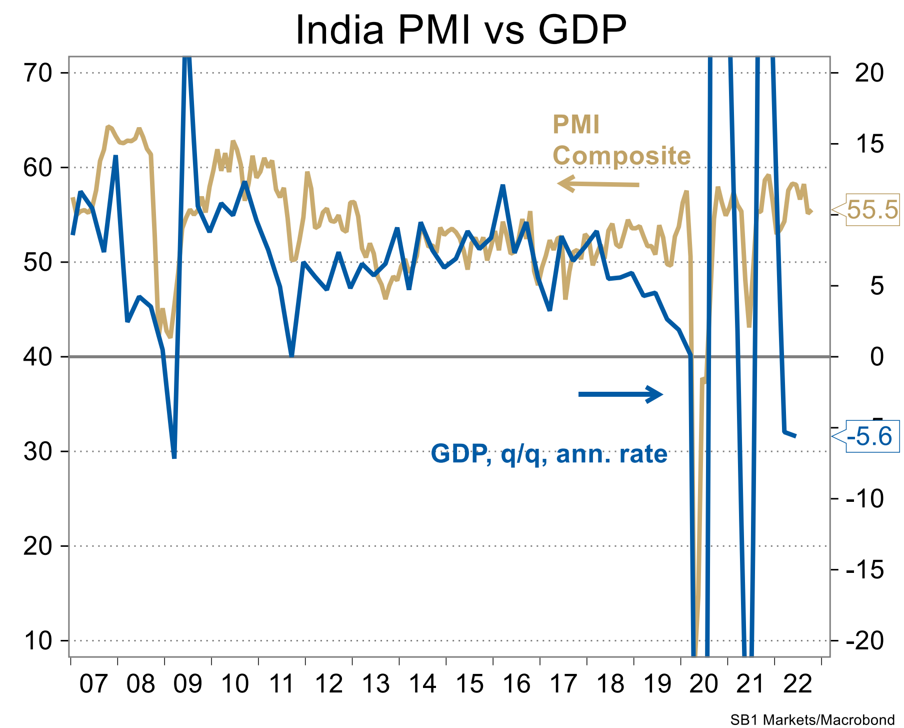


- **The composite PMI** was down 5.7 p to 45.8, which signals a contraction in GDP at a 7.5% pace in Q4
- **Reliable data from Russia** are in short supply these days. What we have? Retail sales are down 12%, auto sales are down 70%, imports have fallen sharply (based on export data from other countries). Still, industrial production is down just 4% since February even if oil and gas production is included. GDP fell by 7.6% (-2% not annualised) in Q2, far less than assumed when the war started
- **A reminder:** The PMIs are not sentiment surveys – respondents are asked about in changes in actual activity (new orders, output, employment, inventories) from the previous month

The composite PMI up 0.4 p to 55.5, as both services and manufacturing rose

…and both sector PMIs are very strong. 10% GDP growth??

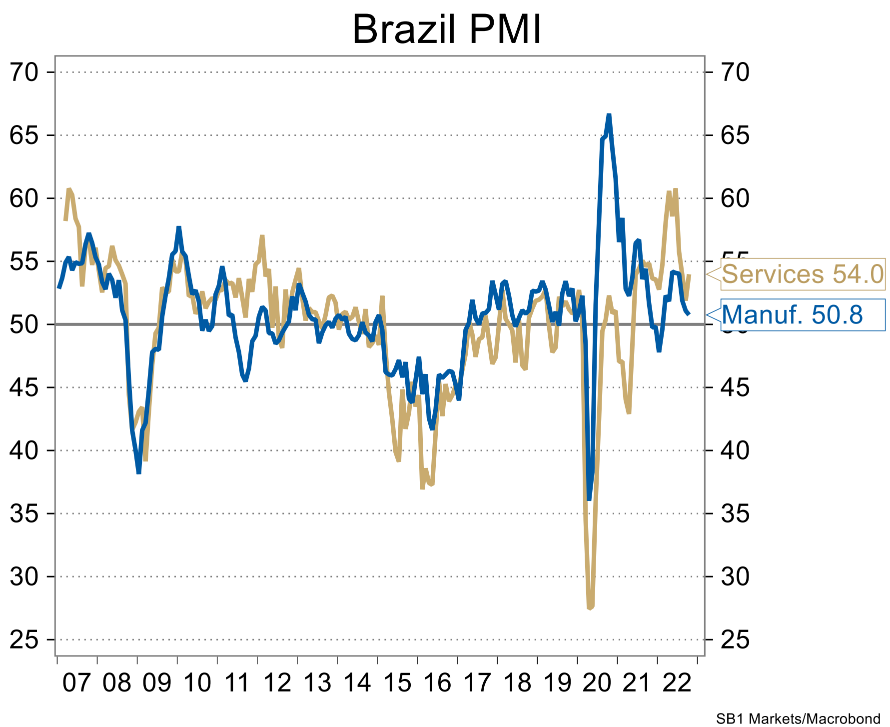


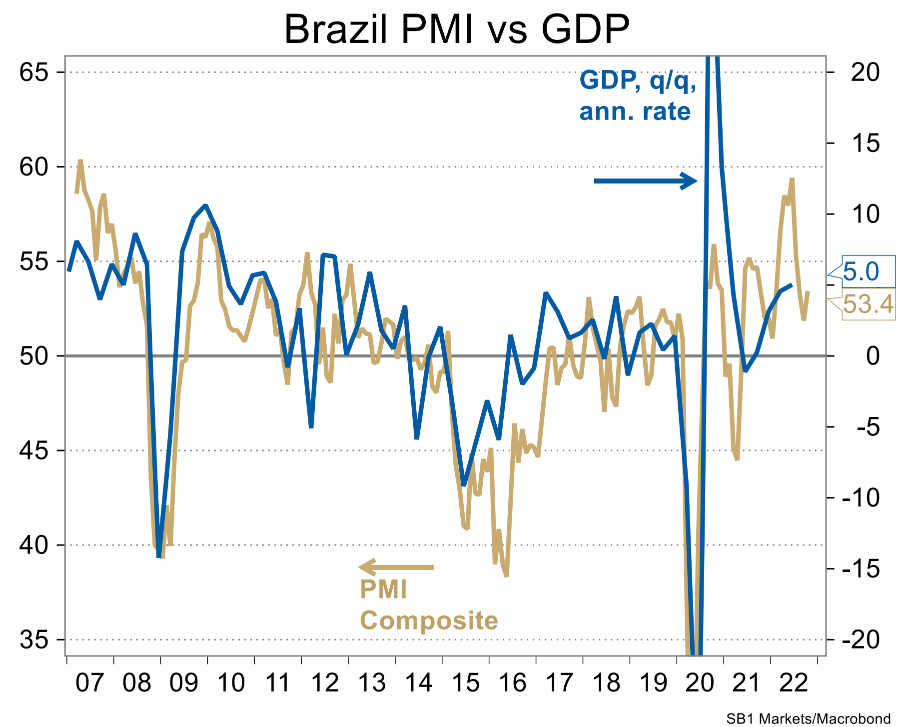


- So far in 2022, GDP has contracted! In Q2, **Indian GDP fell** at a 5.6% pace, close to the decline in Q1. The PMI signals a 10%+ quarterly growth rate in Q4 – which it has been doing for a while, at the same time as GDP growth was negative…
  - » The correlation between the Indian PMIs and its GDP has always been weak – and has been even worse during the pandemic
  - » Just for the record: Measured y/y GDP was still up in 13% y/y in Q2, up from 3.6% % in Q1

The manuf. PMI down, services more up, and the composite signals 5% growth

The composite rose 1.6 p to 53.4

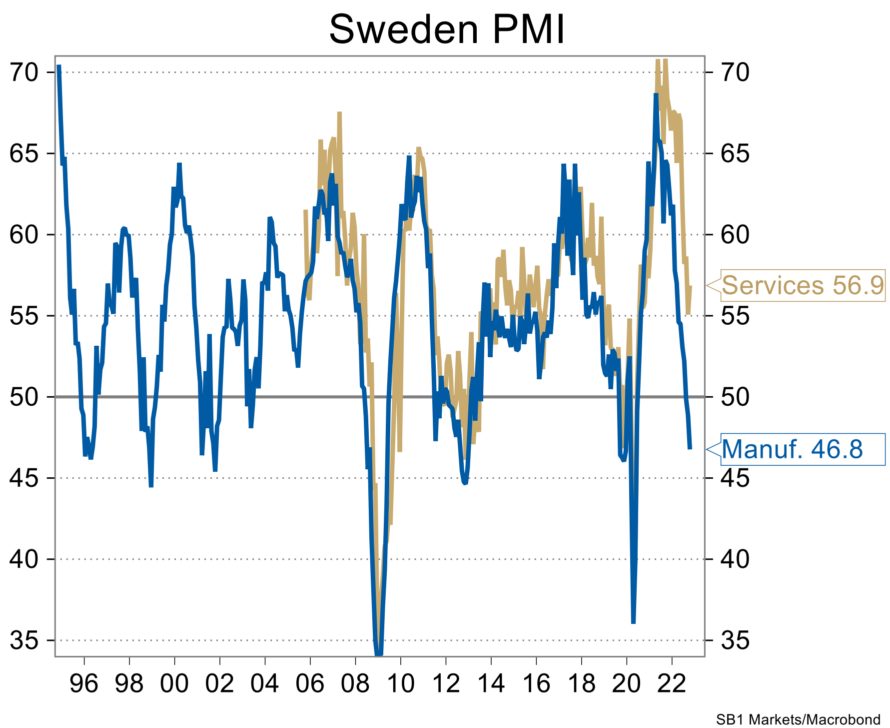


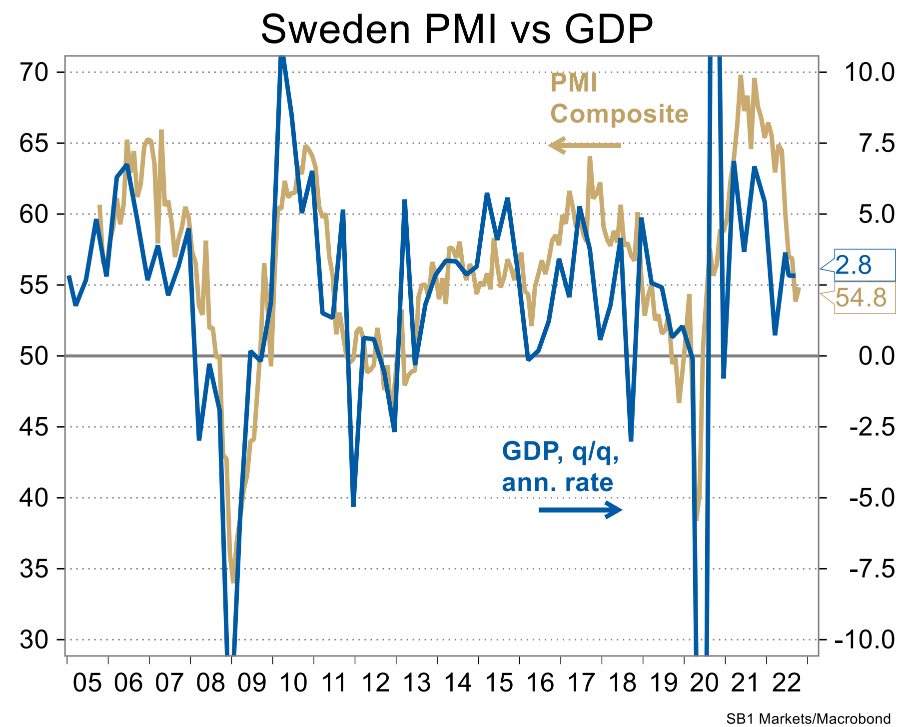


- The correlation to actual GDP growth is not impressive
- Actual GDP growth has picked up some steam the past 3 quarters

Manufacturing sector contracting at a faster pace – but services turned up again!

The service sector PMI rose 1.8 p to 56.9 in October, while the manuf. PMI fell 2.1 p to 46.8

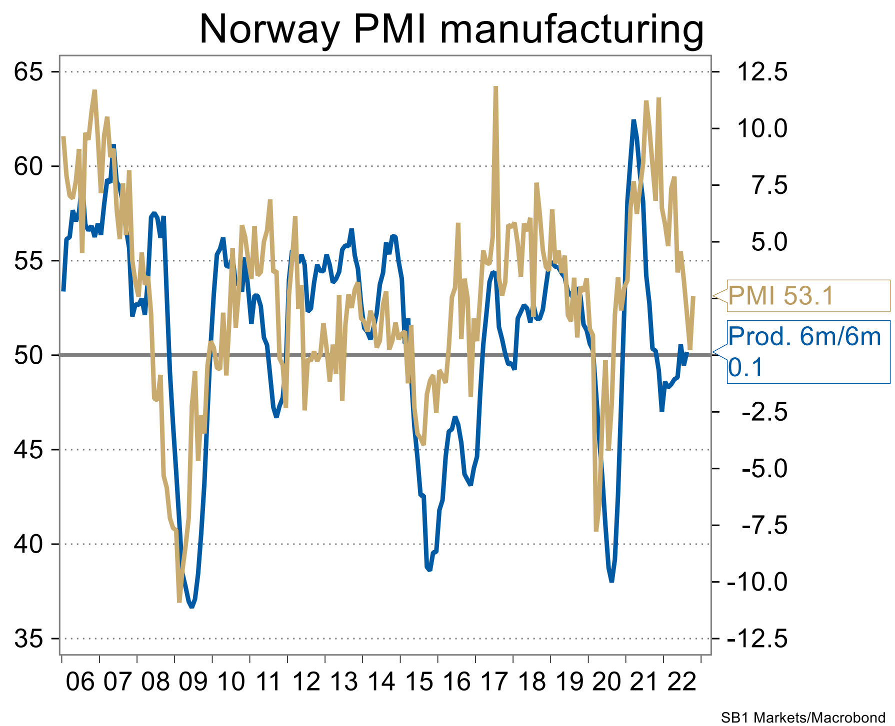


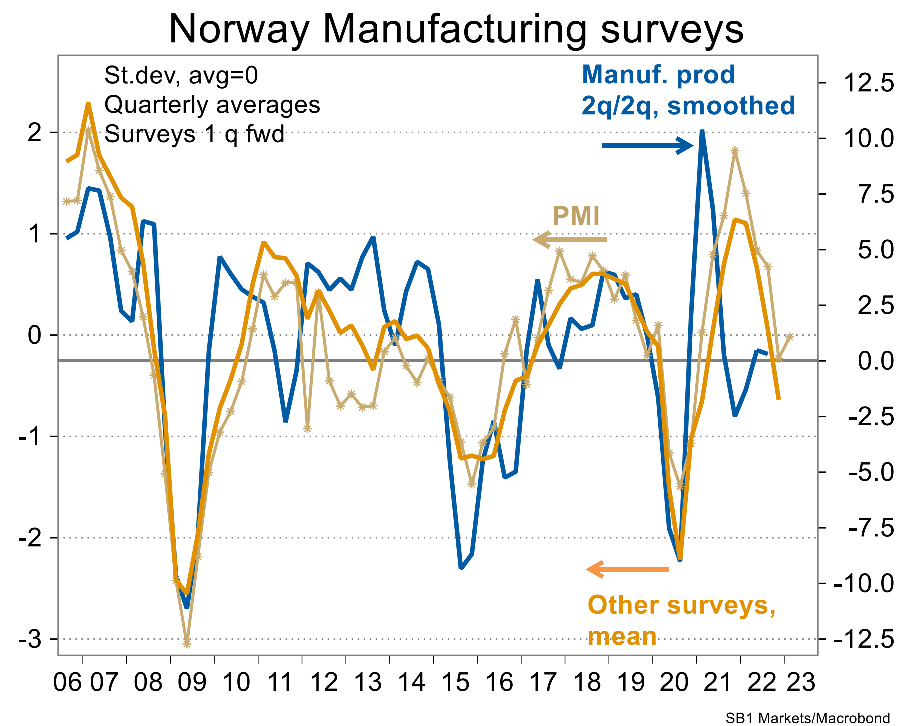


- **The composite** index rose 1 p to 54.8. The service sector still looks incredibly strong. The manufacturing PMI kept falling, as all sub-indices fell, and the production, employment and delivery times indices fell the most
- In Q3, **GDP** grew at 2.8% pace (0.7% not annualised). At current levels, the composite PMI is signalling a GDP growth at around 2%. KI's survey, which is tracking GDP closer, indicate a similar contraction

The volatile Norwegian manufacturing PMI up in Oct – all sub-indices stronger

Production, orders, employment all increased, so did delivery times, while inventories decreased

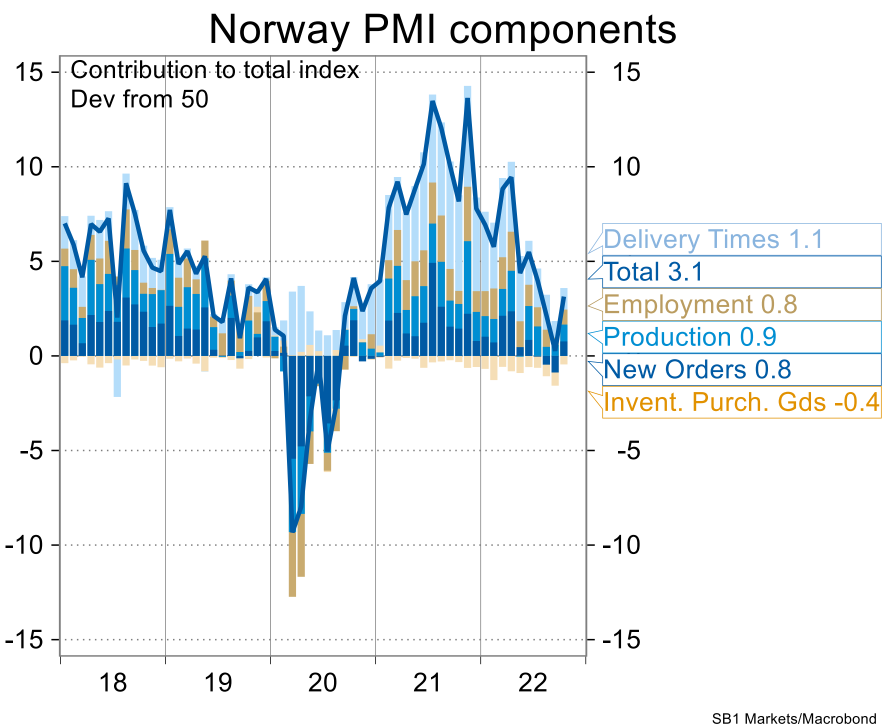


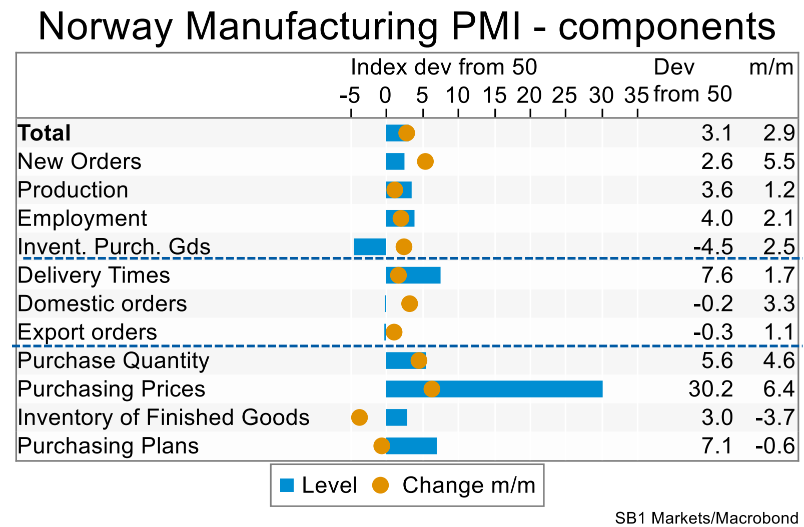


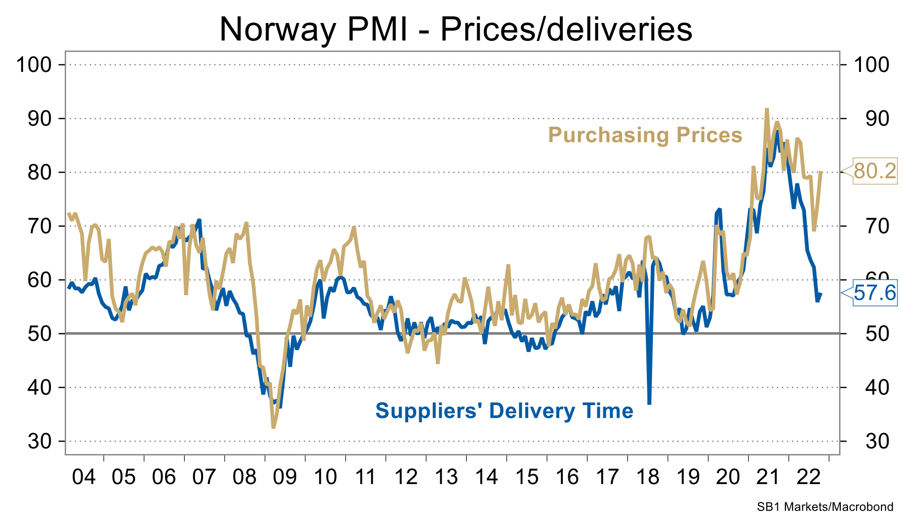
- The **manufacturing PMI index** rose 2.9 p to 53.1 in October (September was revised up by 0.3 p), but the trend is down
- Other **manufacturing surveys** on the other hand are on the weak side, like the SSB survey, NHO and Norges Banks' Regional Network
- **Actual production** has been trending down since early 2021, and has – at best – stabilised recent months (September will be reported today)

Orders are up and inventories are falling – doesn’t sound like a cooling economy

… and input prices are still rising, and faster in October



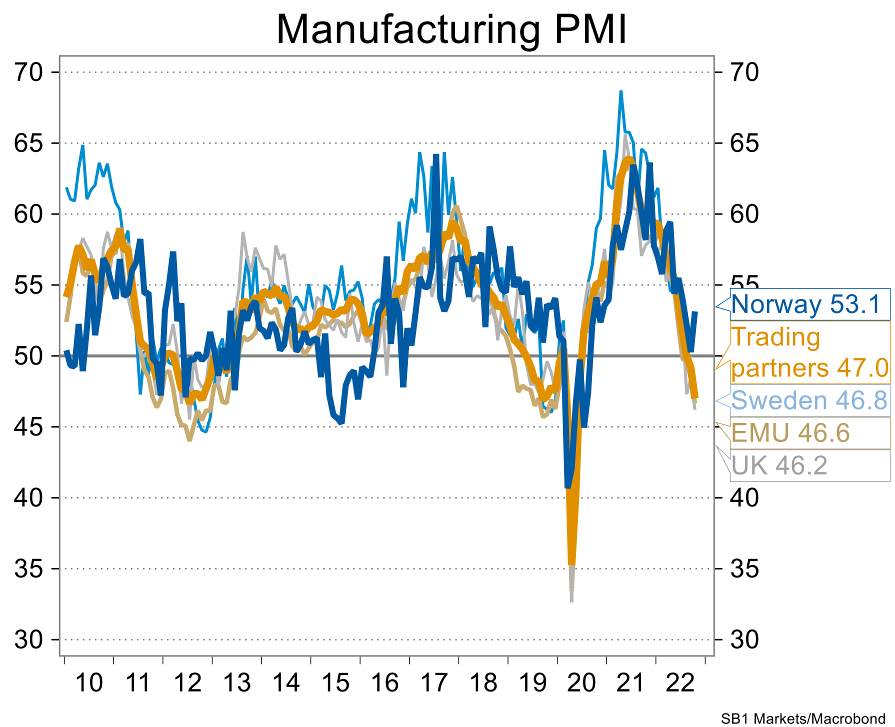


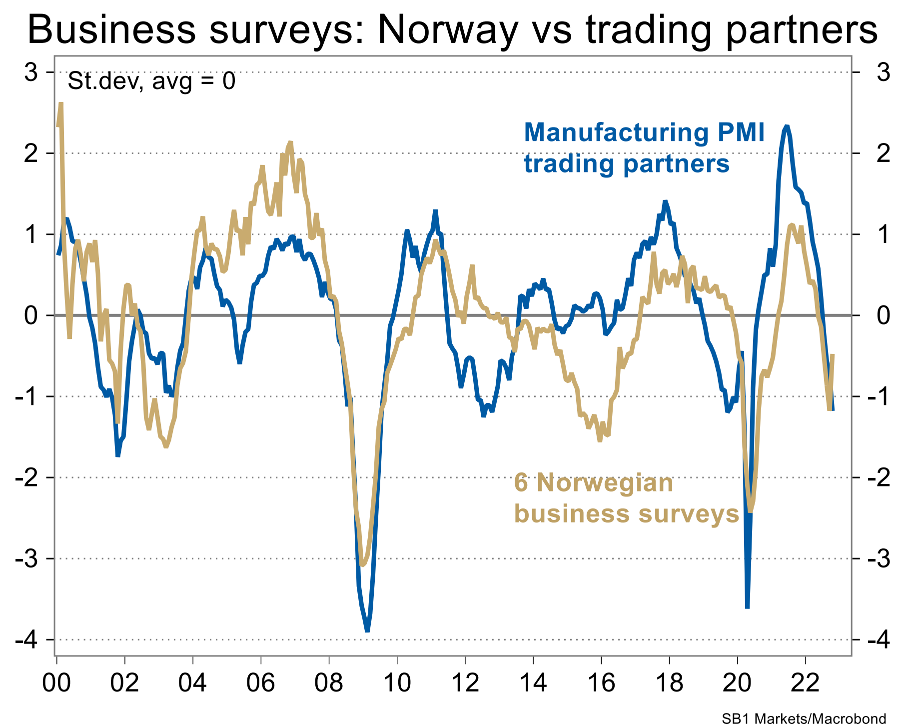


The total PMI index is a weighted index of new orders, production, employment, inventory of purchased goods, and delivery time. The 6 next sub indices at the table to the right are not included in the total index calculus

Norwegian manufacturers normally follow the rest of the world

The October observation is odd, right?

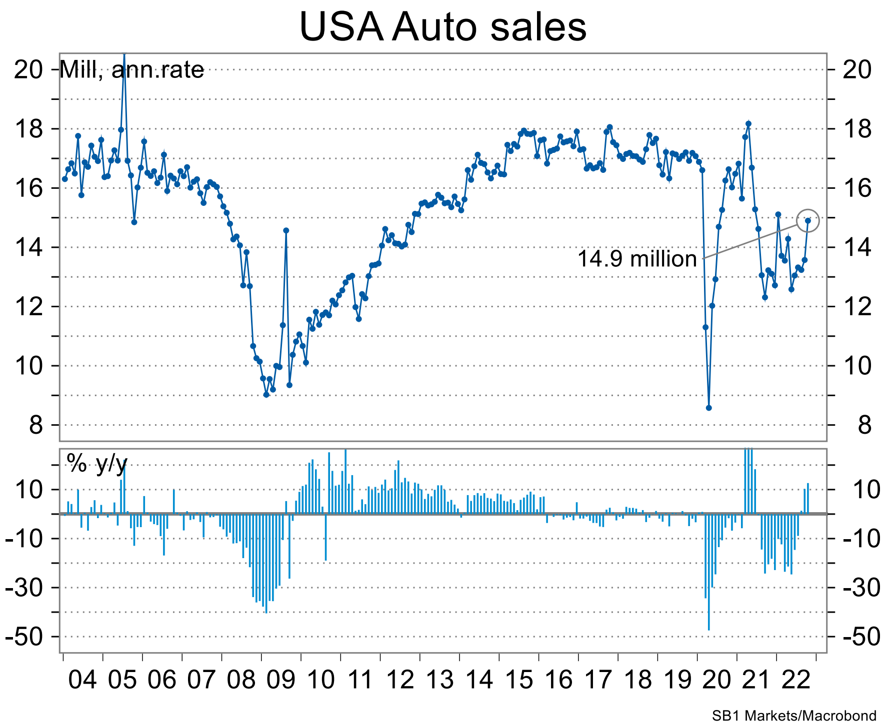


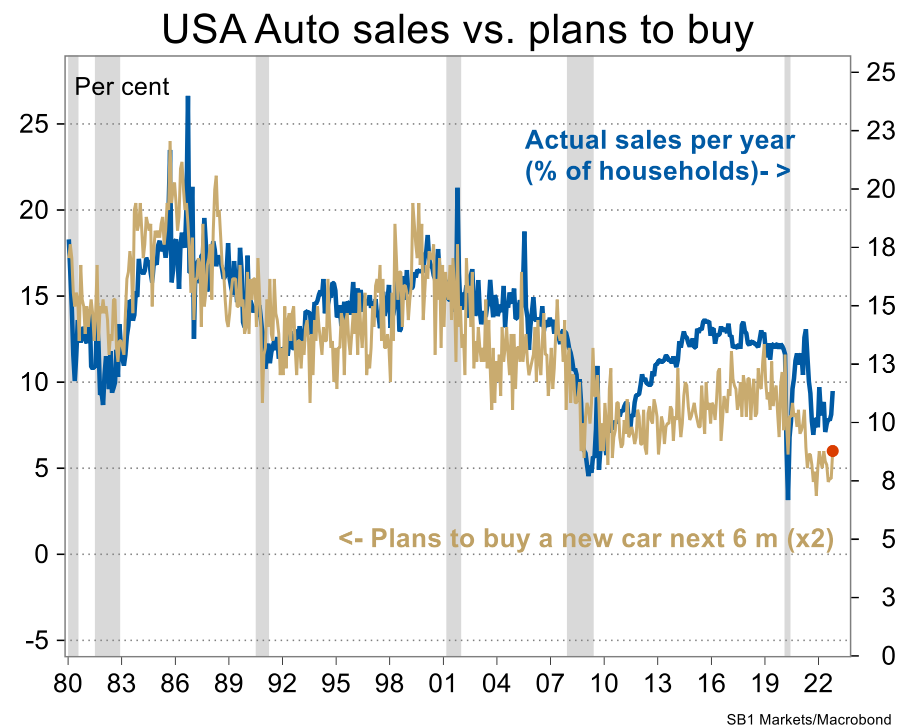


SpareBank 1 MARKETS

US auto sales sharply up in October, as delivery problems eased

Sales up 13.6 mill to 14.9 mill, 0.4 mill above expectations – and 'just' 12% below the 2019 average



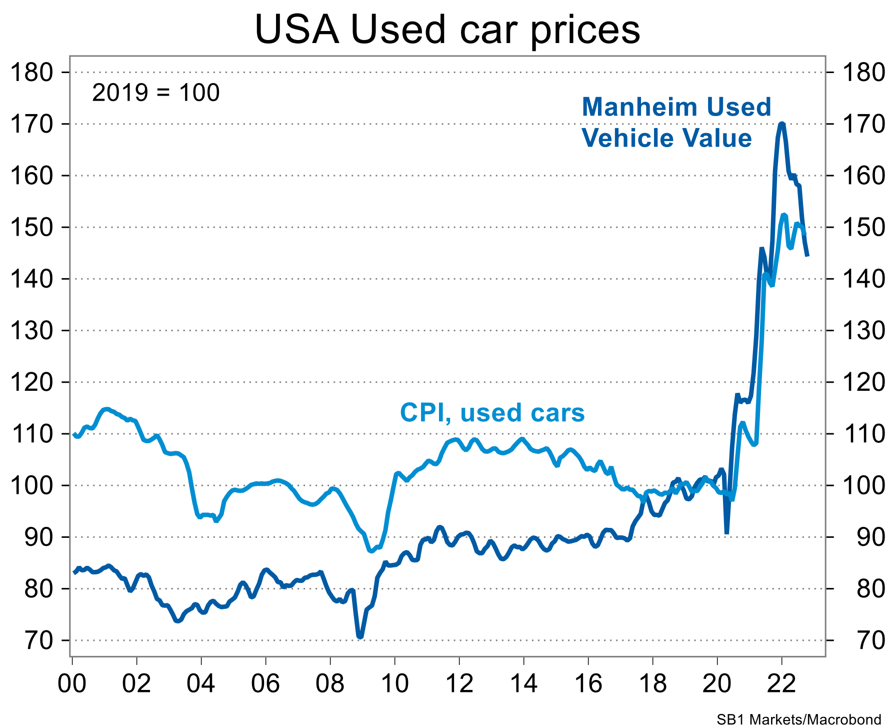


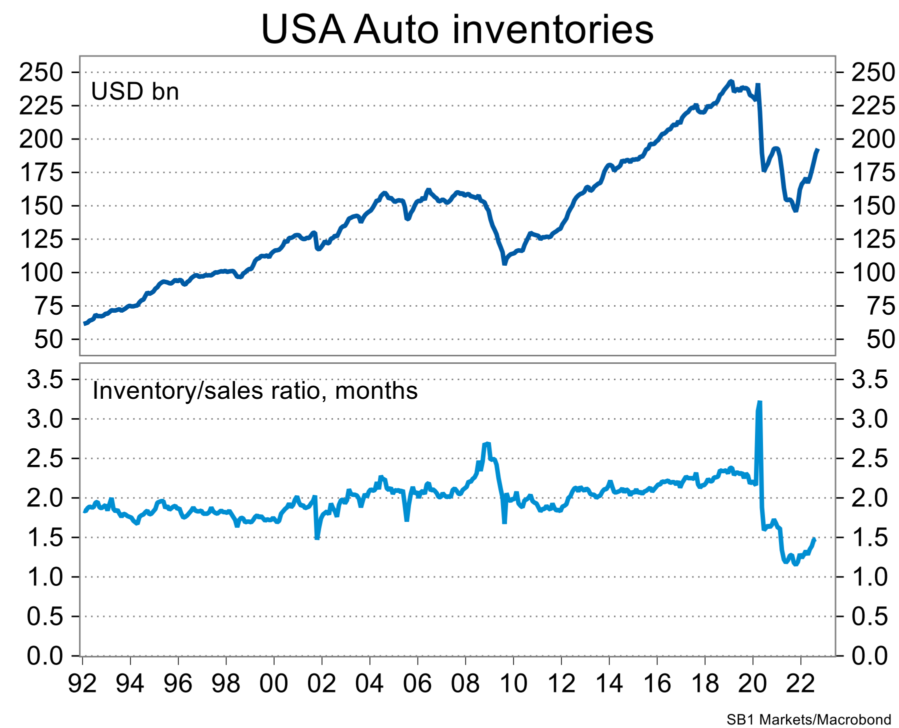
- Plans for buying a new car has been stable at a record-low level over the past year – but has bottomed
- Some demand slowing: Prices for second hand cars are declining rapidly and inventories of new cars are increasing

SpareBank 1 MARKETS

Used car prices are heading down, and auto inventories are slowly recovering

Signs of less tight auto market – but still a long way to go

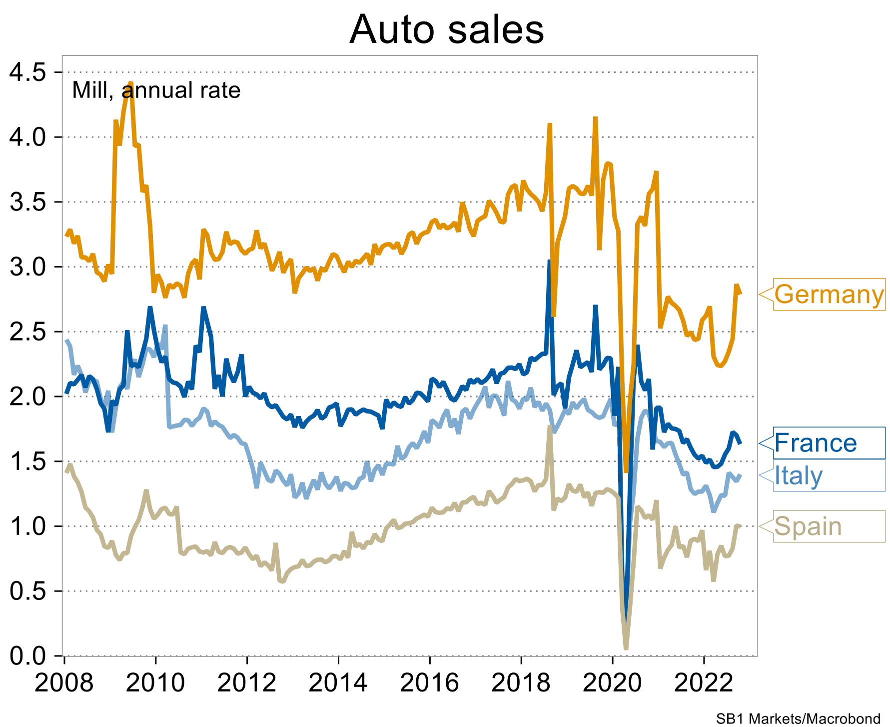


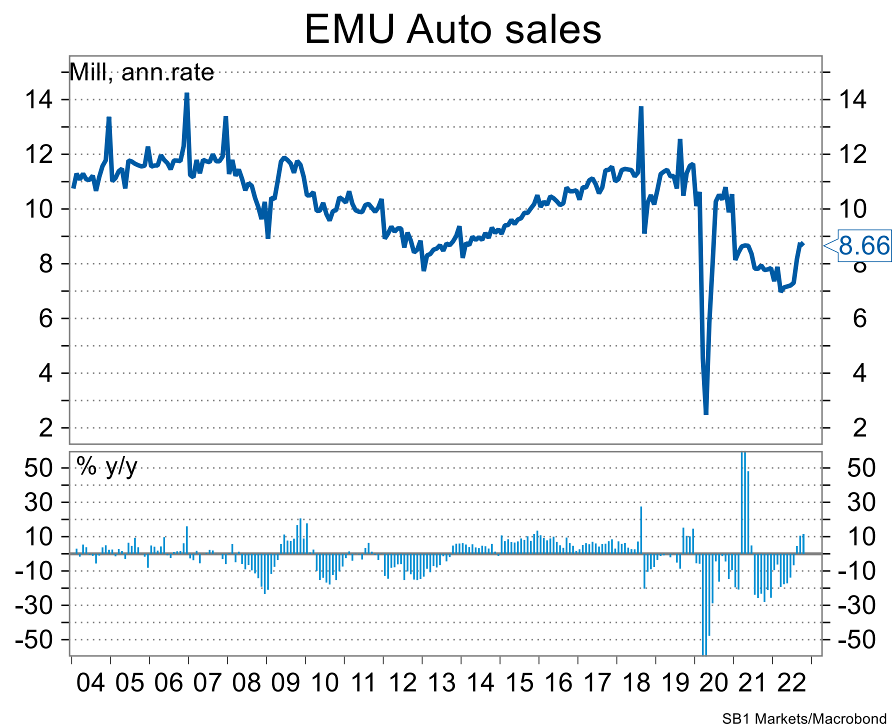


SpareBank 1 MARKETS

EMU: Sales probably slightly down in October, following some ‘strong’ months

Sales in Italy rose marginally, the other big 3 reported a small decline. Sales are still up 20% since July

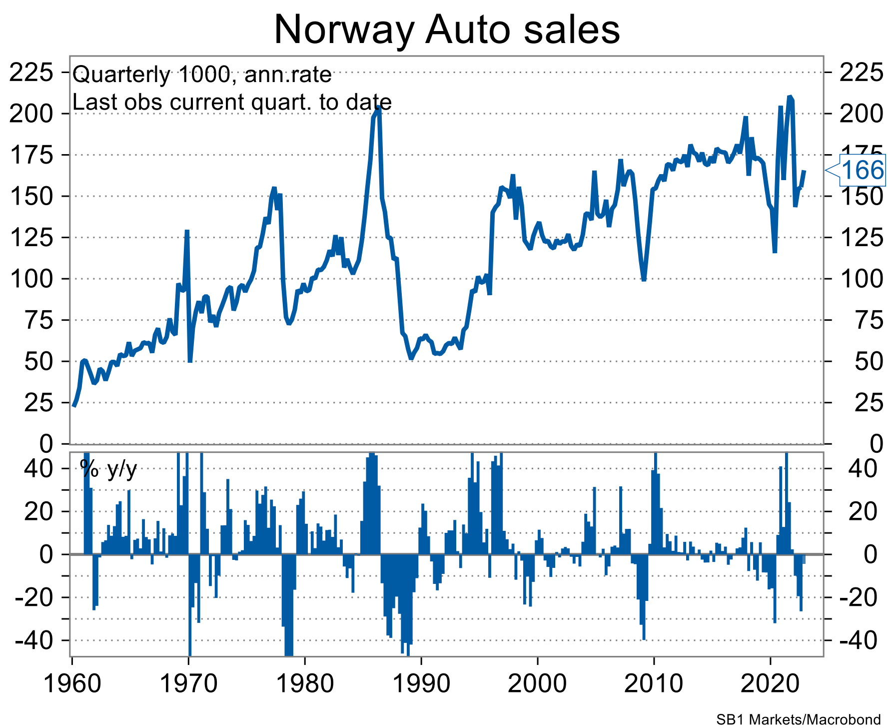


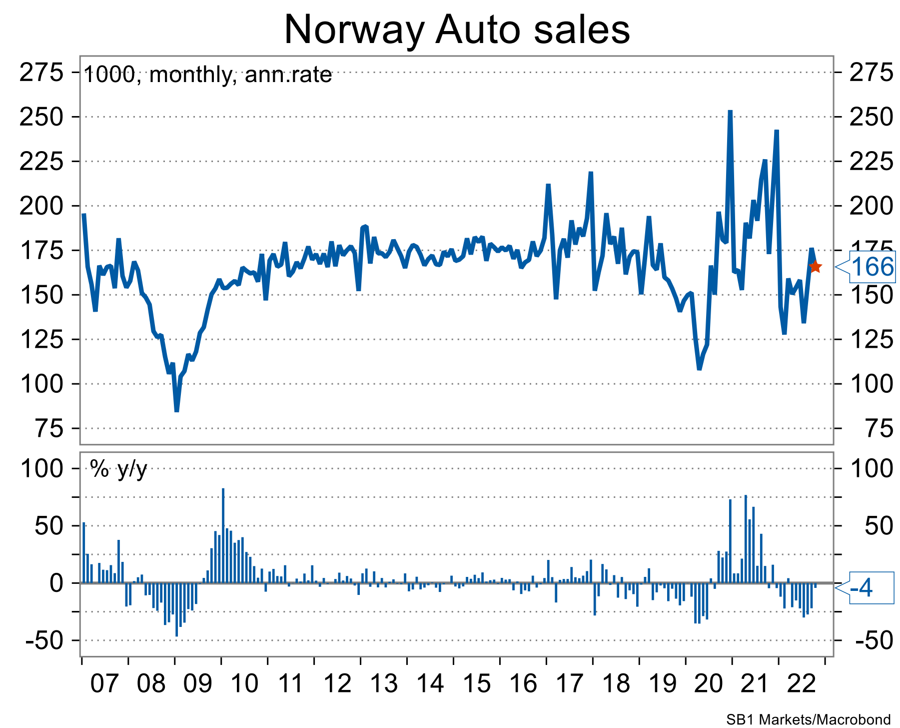


- *Total EMU sales are our estimate*

Norway: More new registrations slightly down in October

Still higher than the average level so far in 2022 but slightly below the average level since 2010

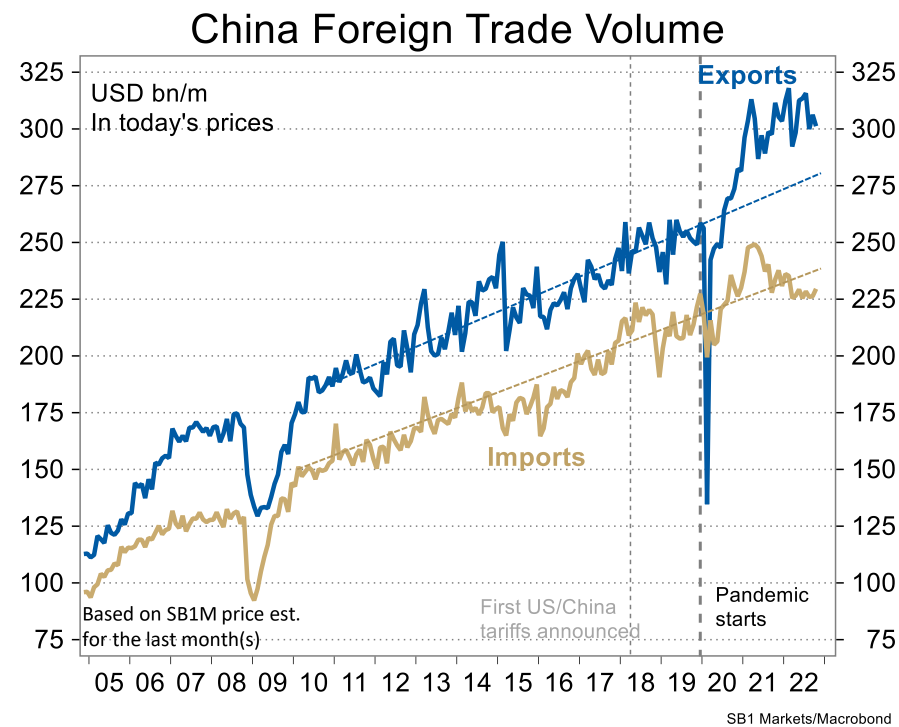




- New registrations down to 166' from 177' in Sept

Exports are flattening, at a very high level, imports are trending slowly down

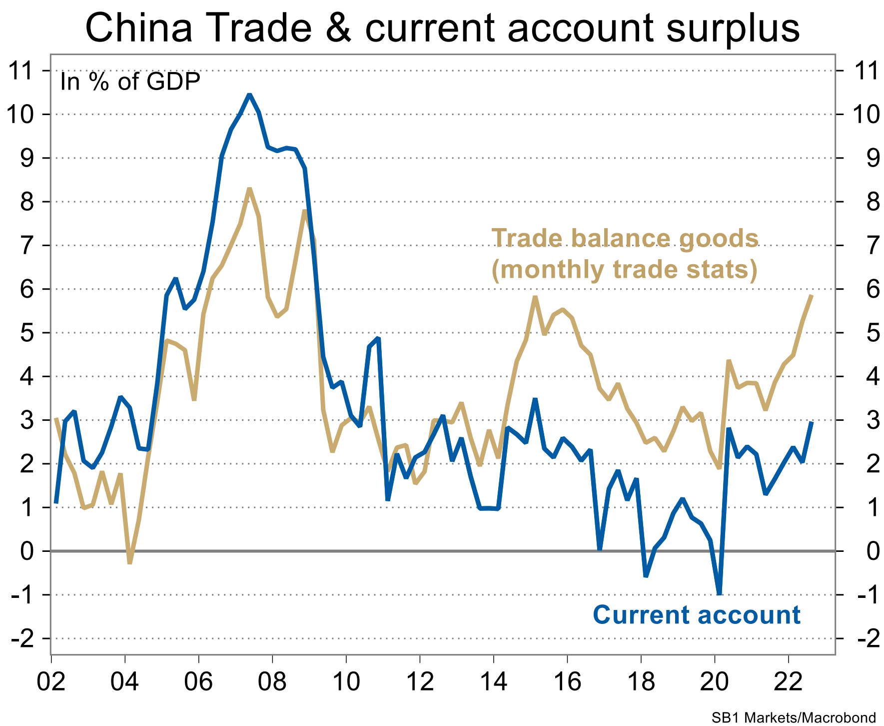
Exports down 2% m/m in Oct, imports up 1%. Exports flat y/y (exp +4.5%), imports -1% y/y (exp. flat)

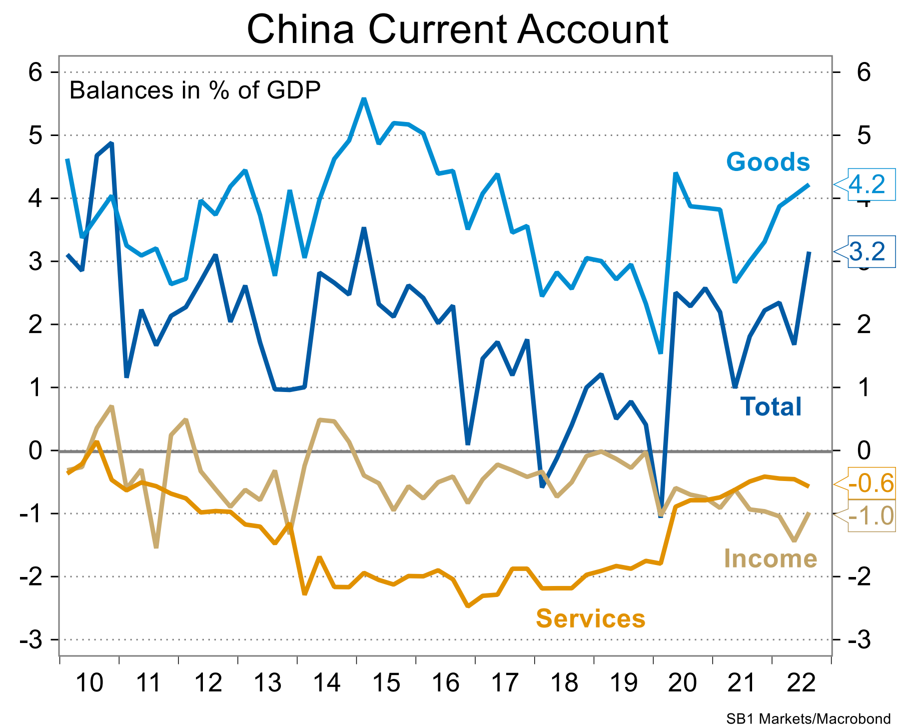


- In volume terms, we assume small changes m/m in October, exports marginally down, imports slightly up (no price indices available yet)
- Exports have more or less flattened recent months following the impressive surge through the pandemic – no supply chains issues to be seen. The current flatting corresponds with flattening demand for goods in the rich part of the world
- Imports have been trending slowly down, in volume terms, and significantly in volume terms, since April 2021 – we assume due to lower domestic demand, both due to weak retail sales and the decline in construction activity. The former has probably been hampered by Covid restrictions. However, since March, import volumes have flattened
- The trade surplus remains very high – and not far below ATH

The trade surplus is trending upwards again, even in % of GDP

The current account is solid in plus too (3%), as the Chinese are not travelling abroad anymore

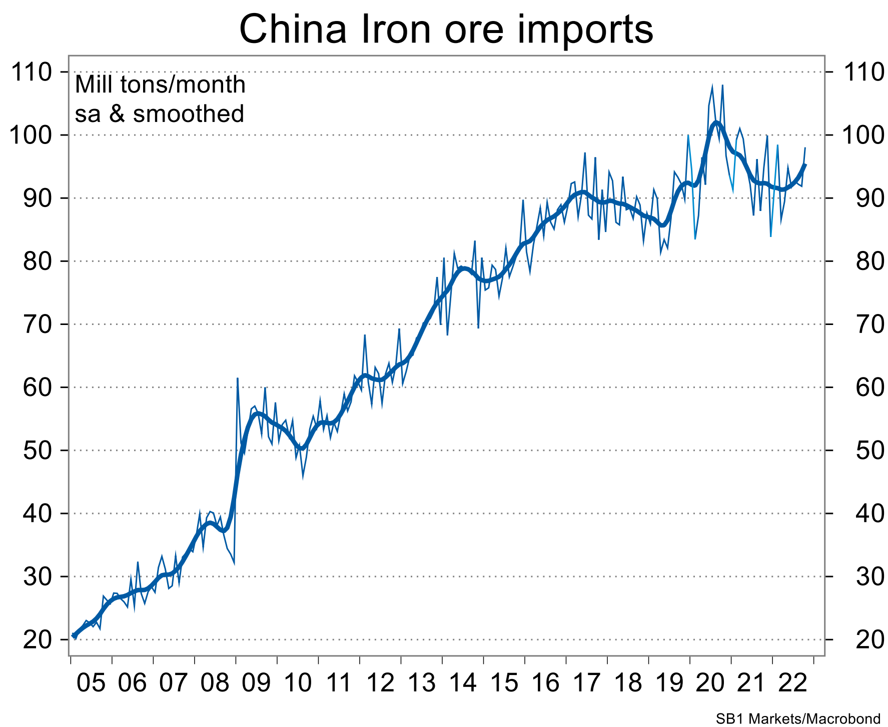


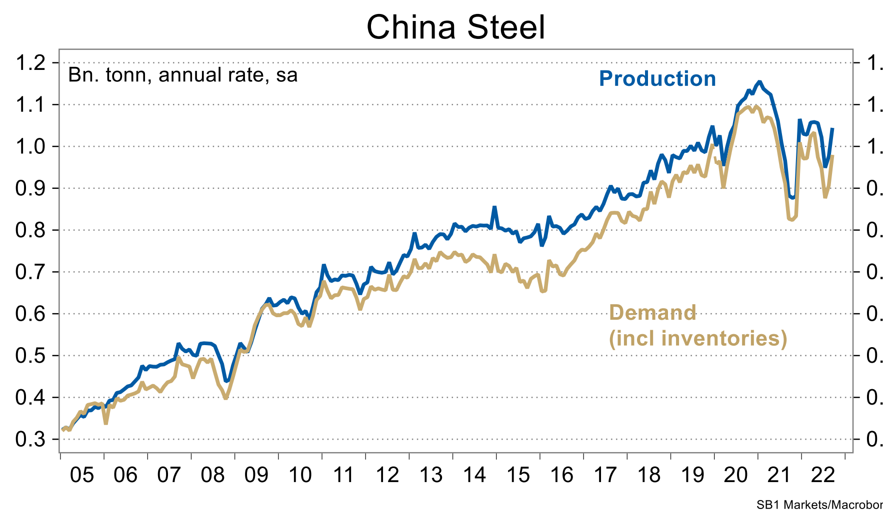


- China runs a deficit in net (mostly capital) income from abroad, even if the country has a huge net positive financial position
  - » China has invested much in low yielding US government bonds (and other low yielding investments); foreigners have been investing in profitable production capacity in China. Now, China's investments in the West may get somewhat better return?

Iron ore imports up in October, still well below the peak in 2020

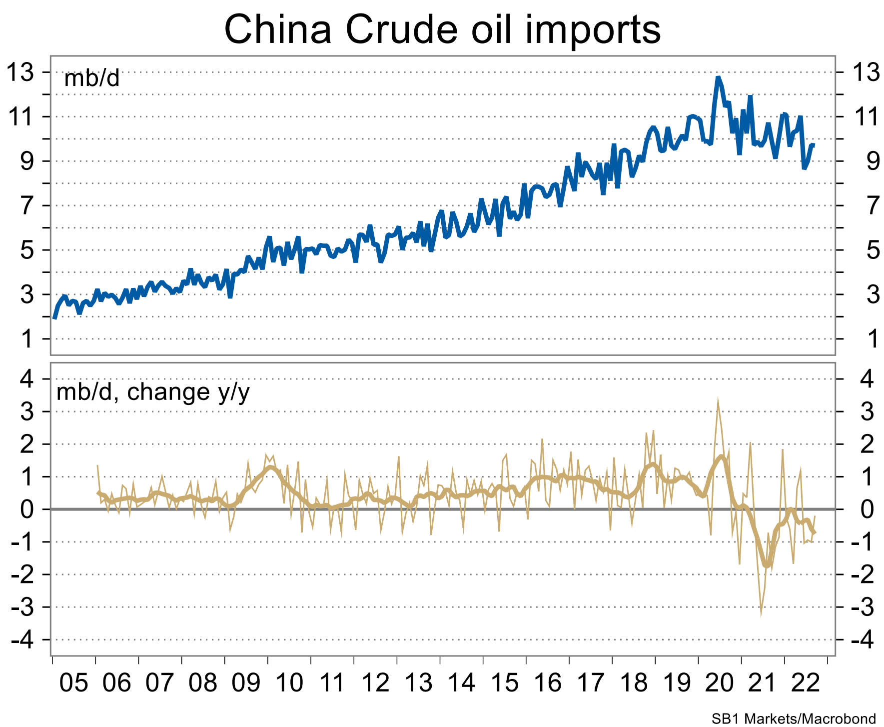
Steel production was also higher in September, rather surprising given the decline in construction star

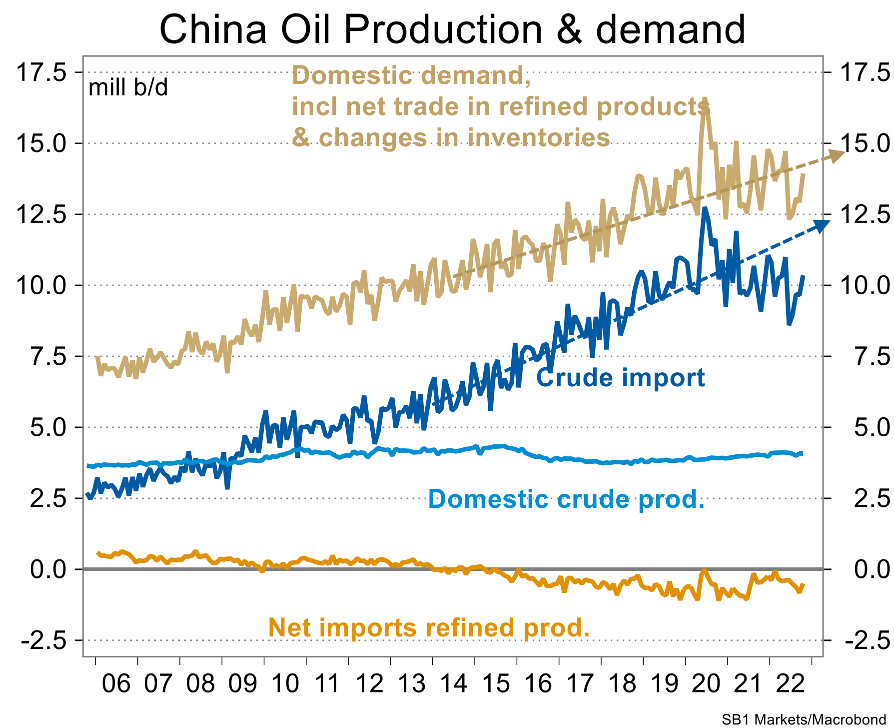




- **Steel production and domestic demand** (incl. inventories) fell sharply in Q2-Q3 last year – by 25% – due to public regulations and probably the setback in the construction sector
- Production recovered last December and has remained fairly stable in 2022, though with a dip in June, and an uptick in August/September.

Crude oil imports up in October, trend is weak

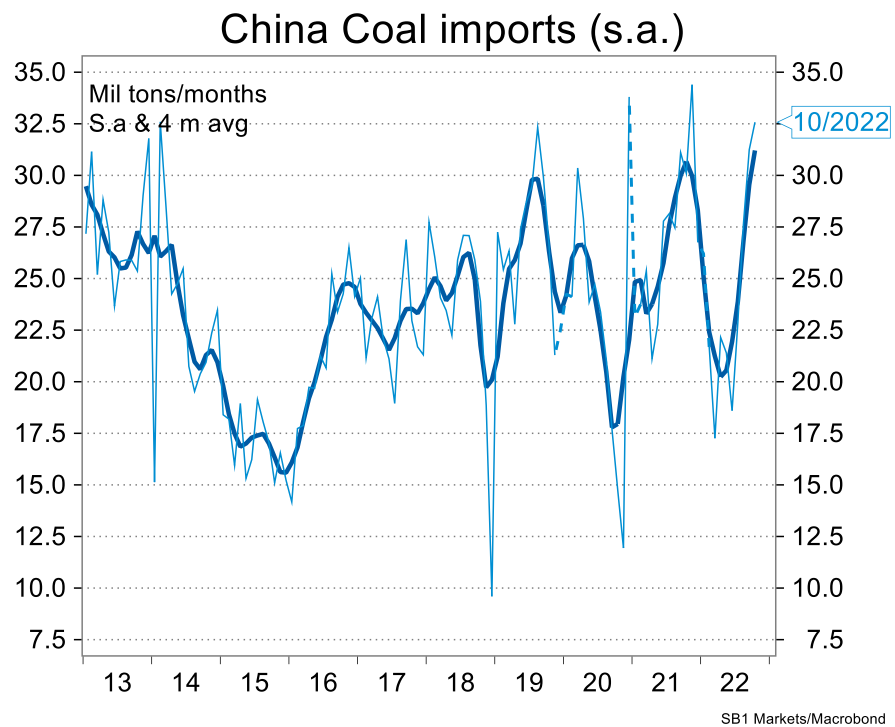


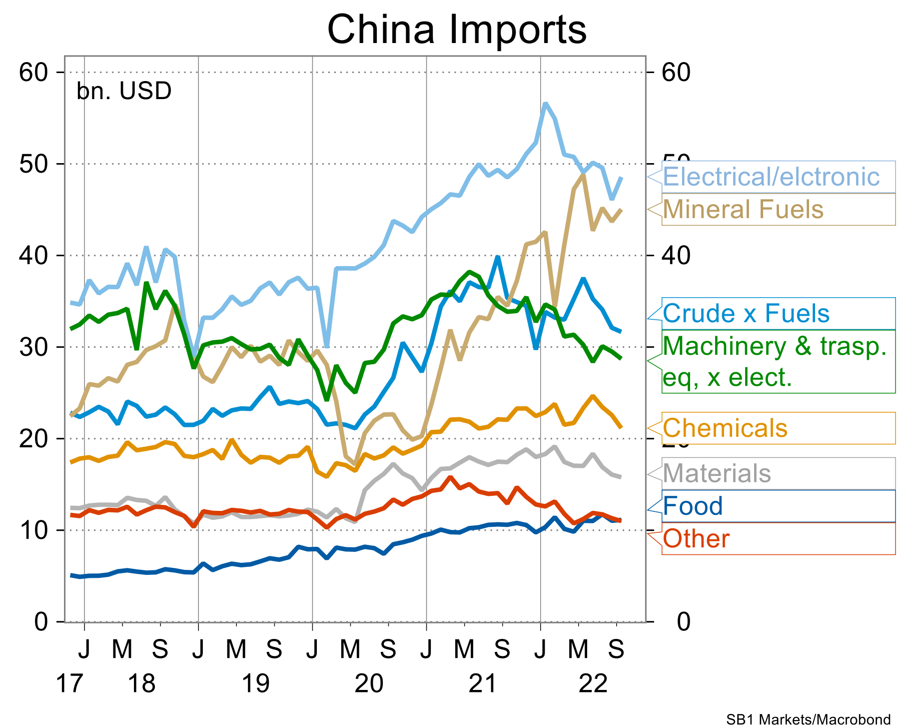


- 4 years without growth in **crude oil** import or domestic demand is rather surprising?
- However, higher net imports of **refined products** since early 2020 (almost 1 mb/d) and a small increase in domestic crude production have partly compensated for the flattening in crude imports - implying that domestic demand for oil/oil products is still increasing – but still at a slower pace
- Some **inventory/reserve building/drawdowns** may explain short term deviations but probably not the whole slowdown in apparent domestic demand

Coal imports further up in October, close to record high

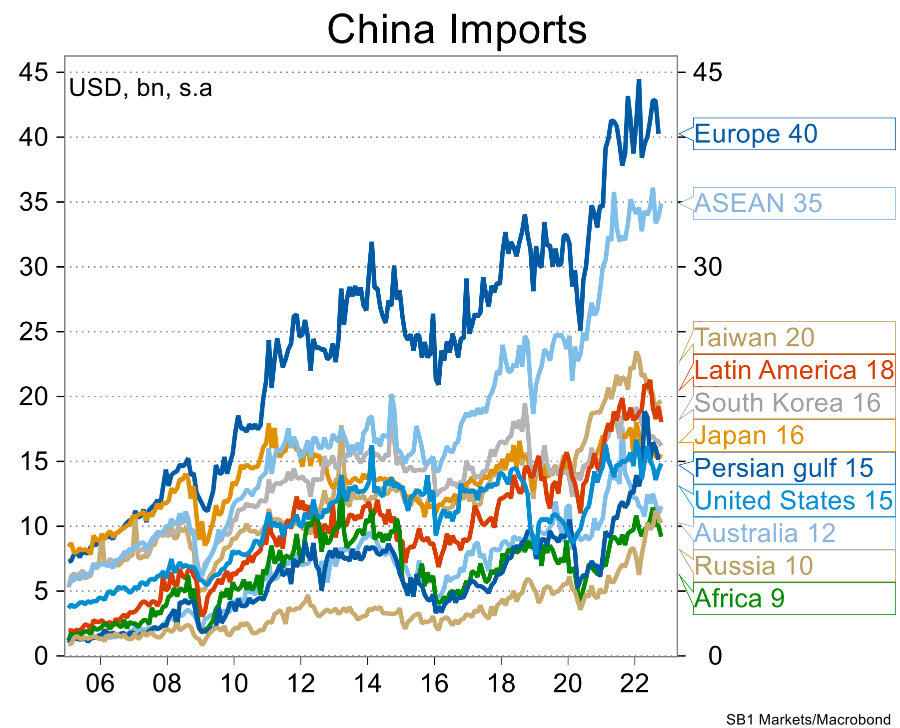
Imports of most goods are heading down (data are lagging one month)





Imports from Russia are surging (Russian oil has found a new market)

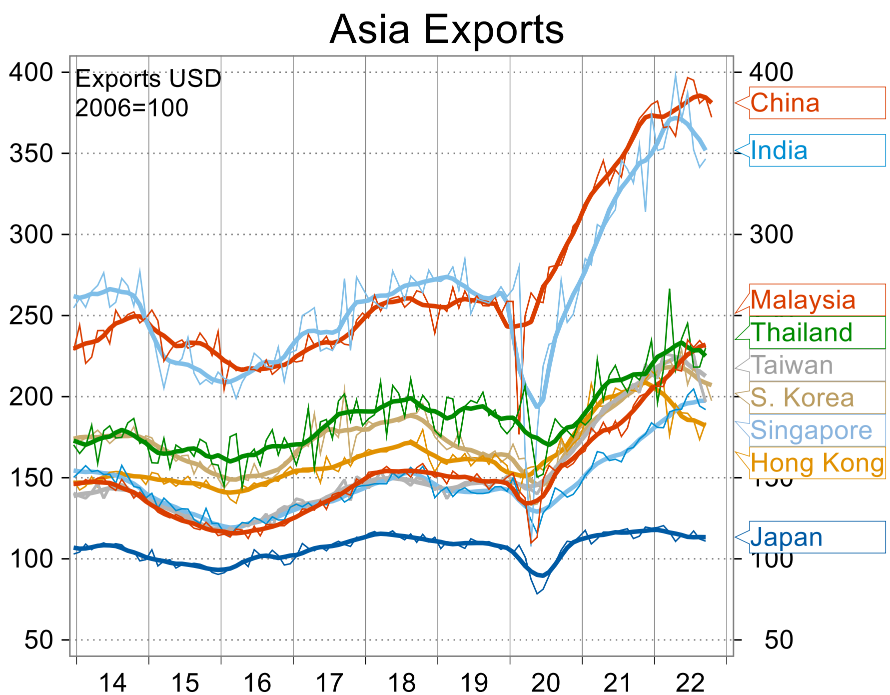
Exports to Russia have also picked up recent months –but is not that high…



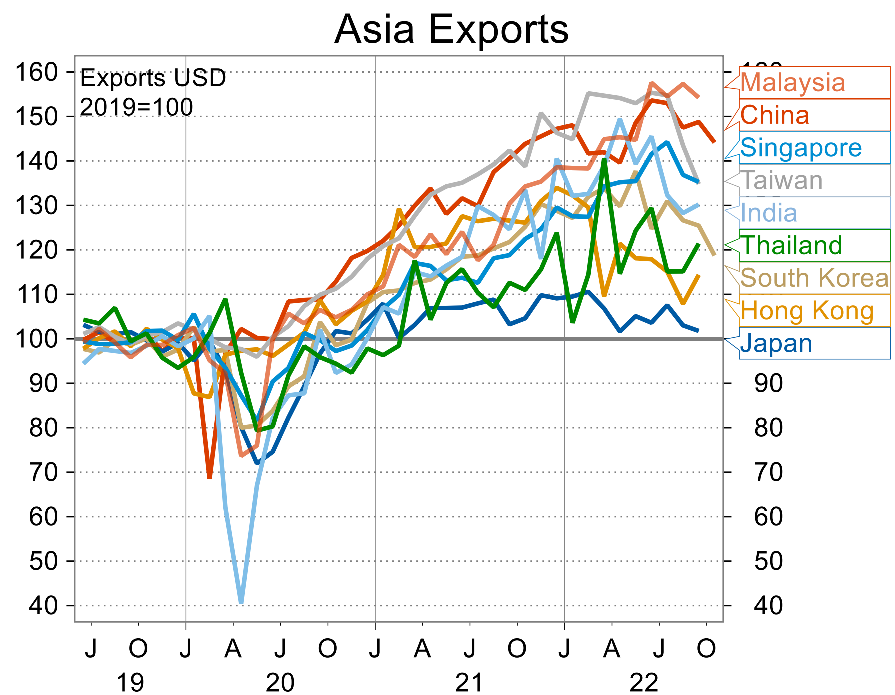
- Exports to the West have fallen somewhat recent months, especially to the US, we doubt due to trade/tech restrictions
- Imports from the US have also fallen – but not from Europe

Exports from other Asian countries on the weak side recent months

South Korea, Taiwan, Hong Kong, Japan are all trending down



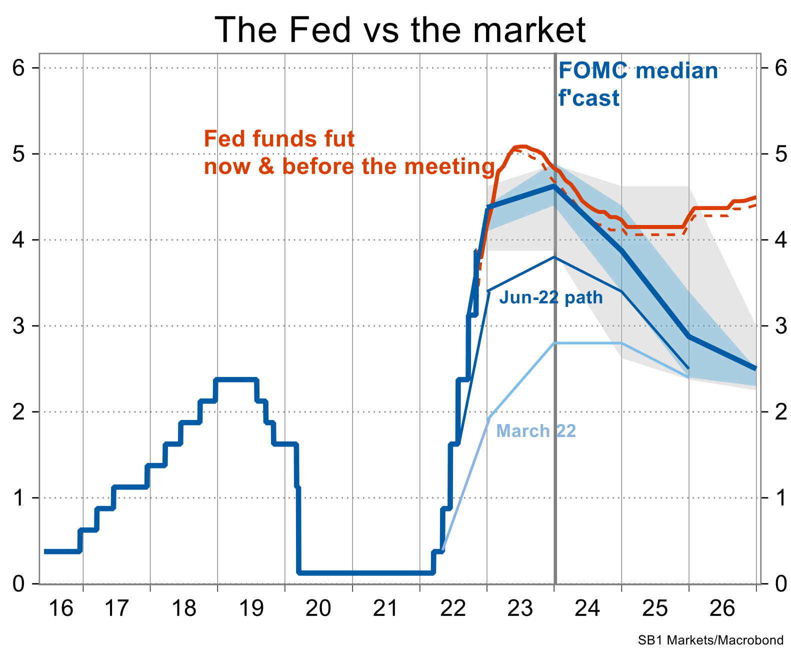
SB1 Markets/Macrobond



SB1 Markets/Macrobond

Another 75 bps now, and the 'terminal rate' will be higher, but the pace will slow…

… at some point, or "in the next meeting or the one thereafter", as Powell said



- **Market reactions: Volatile, and mixed**
  - » The short end of the curve ended marginally up, as did the long end of the curve
  - » Still, equity markets fell sharply, as Powell sounded more hawkish than the press release?

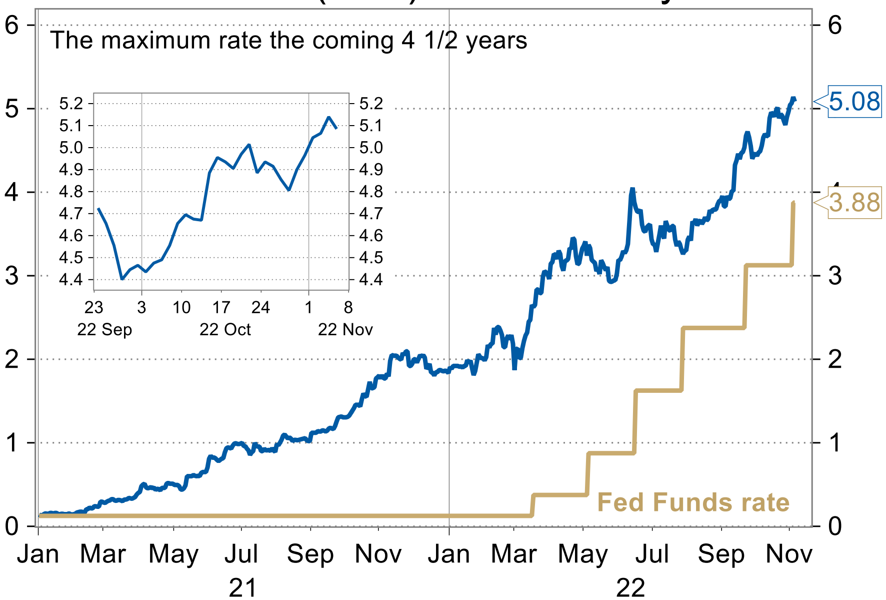
- As expected by the market and previously communicated, the FOMC hiked the **Fed funds rate by 75 bps to 3.75% – 4.00%**
- In the statement, the bank said that the terminal rate will be higher than previously expected, and that the pace of increases will slow at some point, but Powell also stated that *"We think that we have a ways to go, we have some ground to cover with interest rates before we get to that level of interest rates that we think is sufficiently restrictive".*
- The policy stance remains firm, but the bank added a new paragraph in the November report: "In determining the pace of future increases in the target range, the Committee will take into account the cumulative tightening of monetary policy, the lags with which monetary policy affects economic activity and inflation, and economic and financial developments." In other words, the Fed does not want to break the economy's back, and more importantly, it is not about how fast to go, but how far to go (and the Fed is going further than previously communicated). The market has since early October anticipated a higher terminal rate than the FOMC September dot plot signalled, a 4.6 peak. In fact, the market did not revise its expectations much up after receiving the messages from Powell
- However, Powell also reiterated his previous comment that **the risk of tightening too little outweighs the risk of tightening too much** – and he also added that should the Fed go too far, they have the tools to support the economy
- Taken together, another 75-bps hike in December was not taken off the table, even if the FOMC in September signalled a 50 bps Dec hike. The market pricing implies that a 50-bps hike is sufficient, given that the terminal rate is not that far away, and market rates did not move by much last Wednesday, in the short end or the curve, or with regards to the terminal (peak) rate in this cycle (*check next page*). However, longer dated contracts are higher than before the FOMC meeting
- But sure, the bank's decision is, like any other central bank's, data dependent…

SpareBank 1 MARKETS

The Fed will keep at it, until the Fed funds rate reaches 5%?

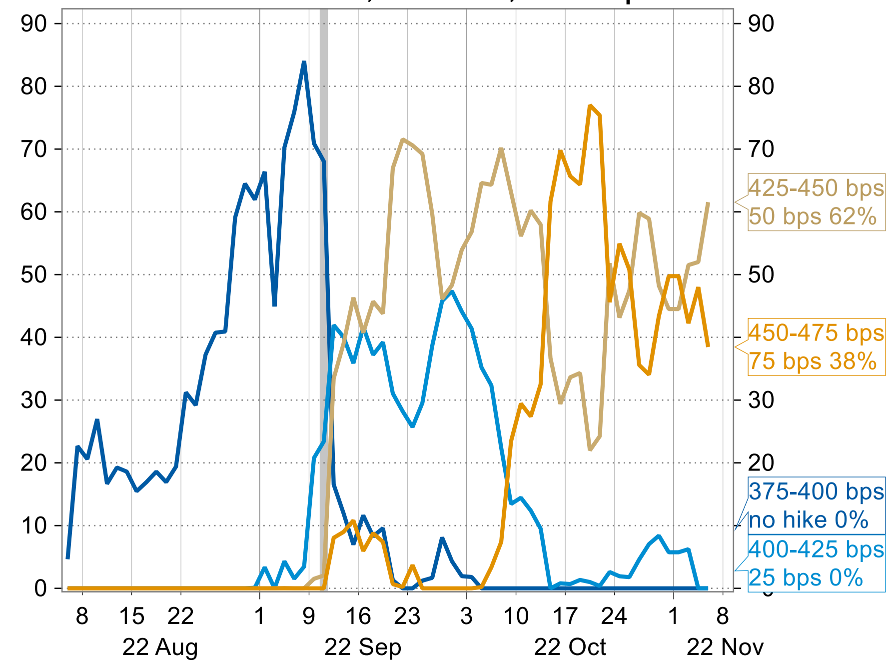
Powell's comments did not shock the market, the terminal (expected peak) rate rose just marginally

USA Fed funds futures, terminal (max) rate in this cycle



SB1 Markets/Macrobond

Fed funds future, Dec 14, 2022 probabilites

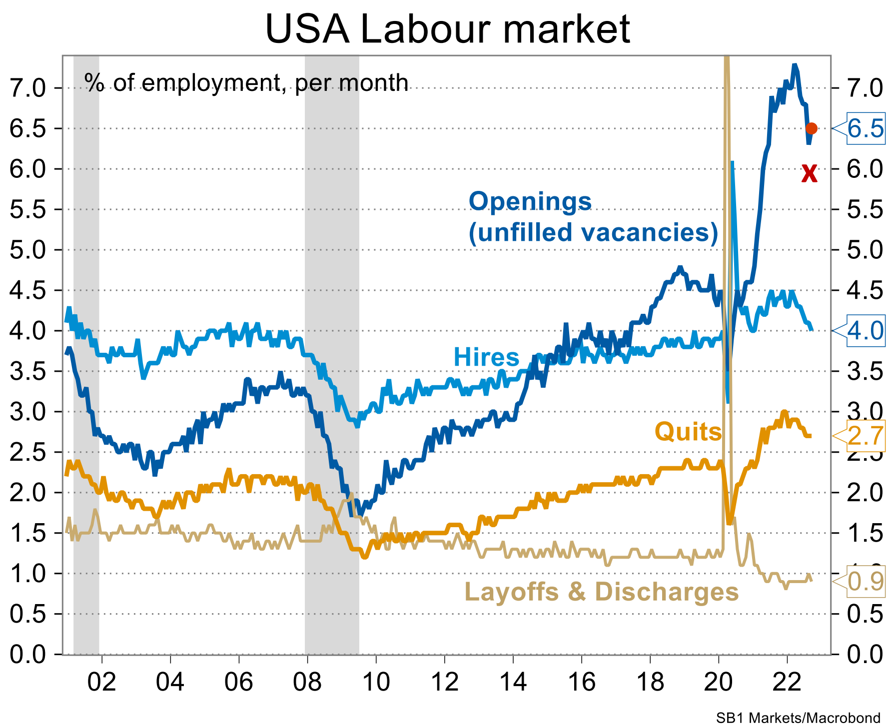


SB1 Markets/Macrobond

- In September, the FOMC signalled at cycle peak at 4.6%. Powell said the estimate of the termial rate would be lifted in Dec, we assume up to 5.1%. There is were the market is now, following a small lift last week (and almost nothing on Wednesday
- The market deems a 50 bps hike the most likely outcome on the December meeting (62%), the alternative being the 5th 'triple' hike in row (38%)

Seems like the Fed has its job cut out for them: Vacancies increased in September

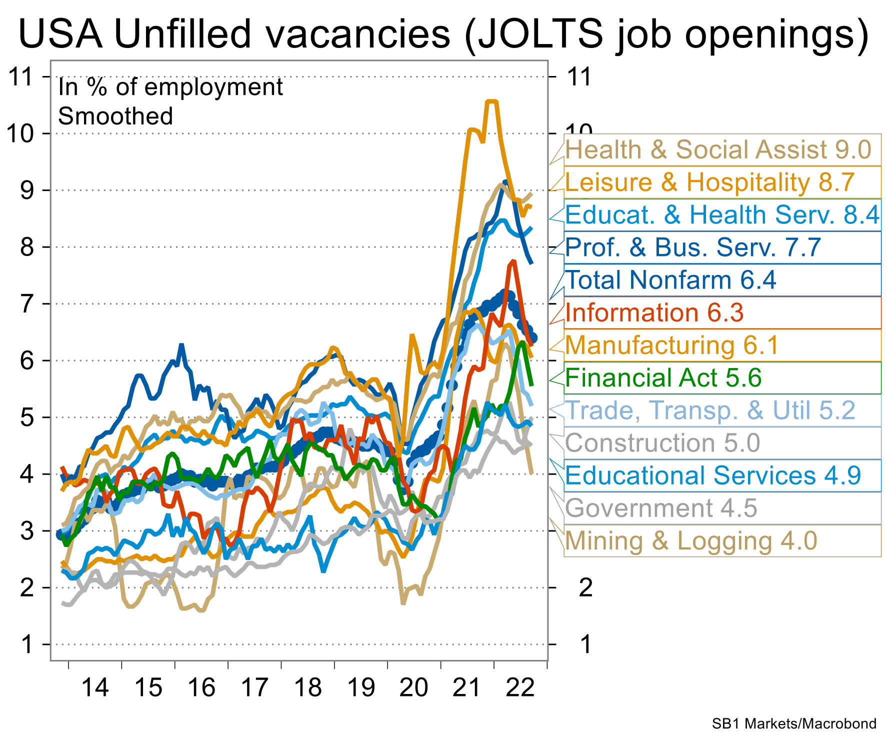
The vacancy rate increased by 0.3 pp to 6.5%, was expected down to 5.9%!

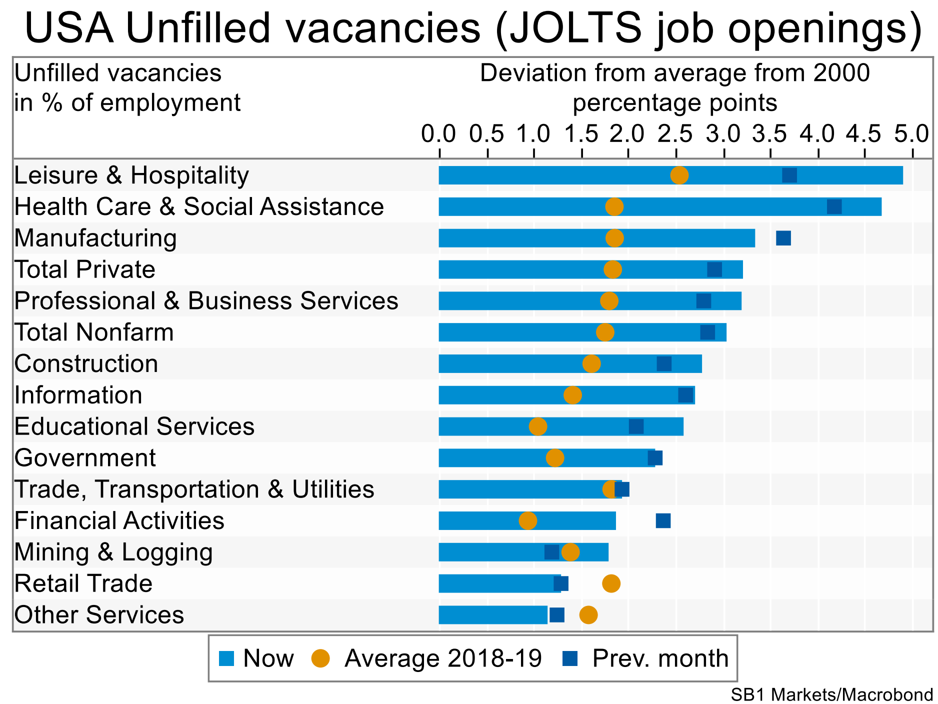


- The number of **unfilled vacancies rose by 0.44** mill to 10.7 mill in Sept (Aug vacancies revised up by 280'), expected down to 9.75 mill. The rate (vs no. of employed) rose 0.2 pp to 6.5%, while it was expected down to 5.9% (the red cross at the chart to the left)!
  - » Vacancies are still down from the peak in March (7.3%), but the September JOLTs survey indicates that it may be more tricky to restore balance in the labour market than what has been laid out by the Fed
  - » The highest print ever before the pandemic was 4.7%, and the rate was 4.5% just before the pandemic hit – the current level is still very high – even if the tide has turned
- **The SMBs (NFIB survey)** reported that 46% of companies were not able to fill positions in October, unch. from Sept, which is close to record high. Hiring plans were down by some 3 pp, but remains high – and the share saying that they are increasing compensation rose, and is again close to record high
- **New hires** fell by 0.2 mill to 6.1 mill in Sept, equalling 4.0% of the employment level. This is indicating an easing of the labour market, but the level is, of course, still high
- The number of **voluntary quits** fell 0.1 mill to 4.1 mill, leaving the rate to employment unch. at 2.7%. The trend is down, signalling that workers have become somewhat more cautious leaving their current jobs – but the quit level is still higher than anytime before the post pandemic surge
- **Layoffs** equalled 0.9% of employment in September, down 0.1 pp from August – still not signalling any take-off in downsizing
- **In sum:** The tide has turned, but the labour market is still very tight, and it is unlikely that wage inflation will come down to a sustainable level without a substantial further weakening. Job openings may be stickier that what the Fed has hoped for, and are leading unemployment by some few months, though not by a stable lag (but the correlation is high). Actual unemployment rose by 0.2 pp to 3.7% in October but new jobless claims, which leads the unemployment rate has not turned up

Most sectors are reporting more vacancies than in August

…and all but 2 sectors report more vacancies since before the pandemic (retail, other services)

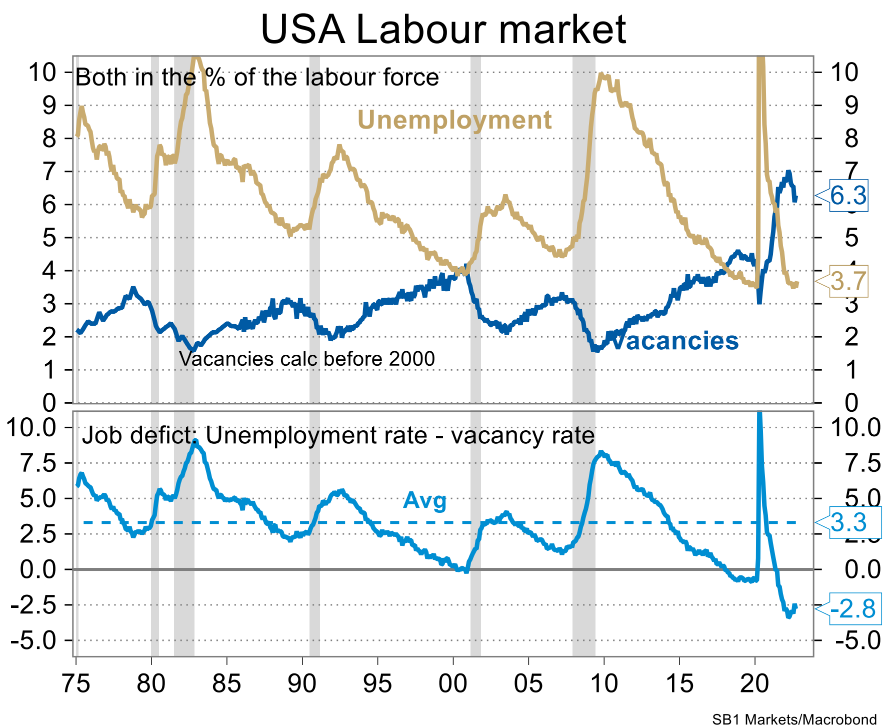


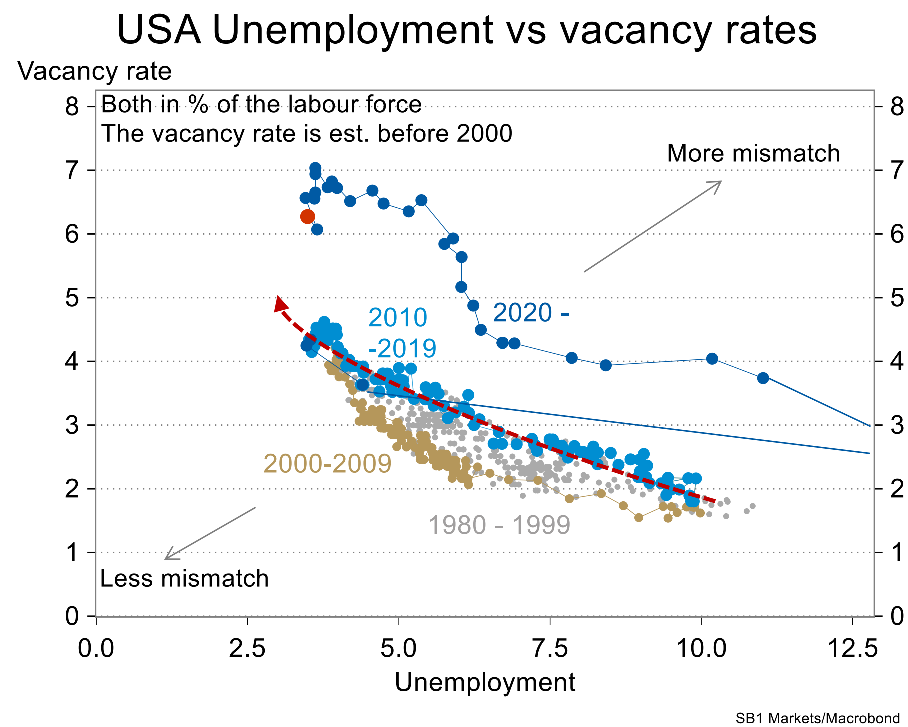


- Only four sector reported fewer vacancies than in the previous month: The financial sector, manufacturing, government, and other services

Unemployment up 0.2 pp to 3.7%. Is the tide turning?

Will vacancies return to a normal level without an increase in unemployment (= a recession?)

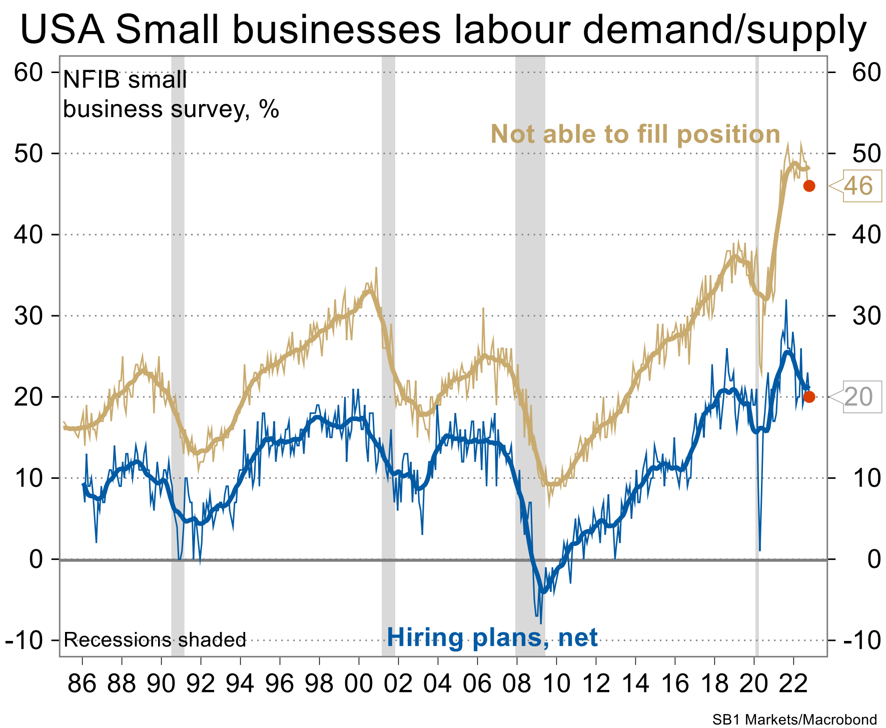


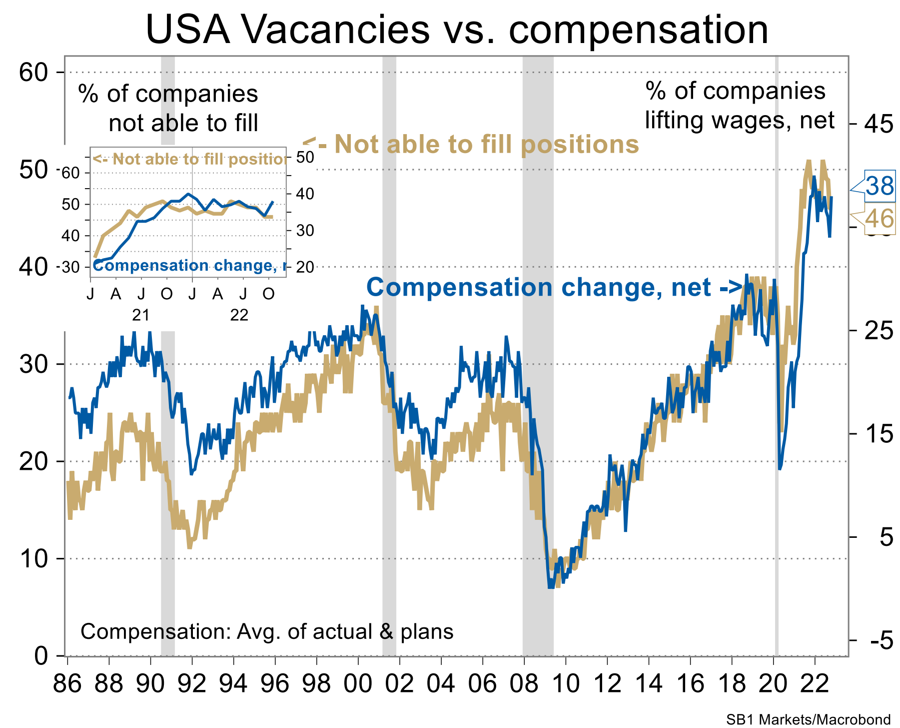


- In principle **vacancies may be reduced without pushing the unemployment rate** up (aka recession), as the vacancy rates is so much higher than normal, but we think it would be hard to achieve, over time. The September tally shows that unemployment was down, while layoffs rose, the latter was not a move in the right direction for the Fed. In October, the unemployment rate rose back up to 3.7% again
- An economy that reduces overall demand for goods and services, and thus demand for labour, will hit both companies that have vacancies, and those which do not. The labour market is not so flexible that redundant labour in one company will seamlessly be transferred to fill still vacant positions in other companies/sectors/regions. <u>If such a transfer had been easy, it would have taken place already, and the unemployment rate would have been lower</u>

SMEs have moderated their hiring plans, but still find it difficult to fill vacancies

Some <u>more</u> companies are planning to lift wages, and more than anytime before (x prev. months)



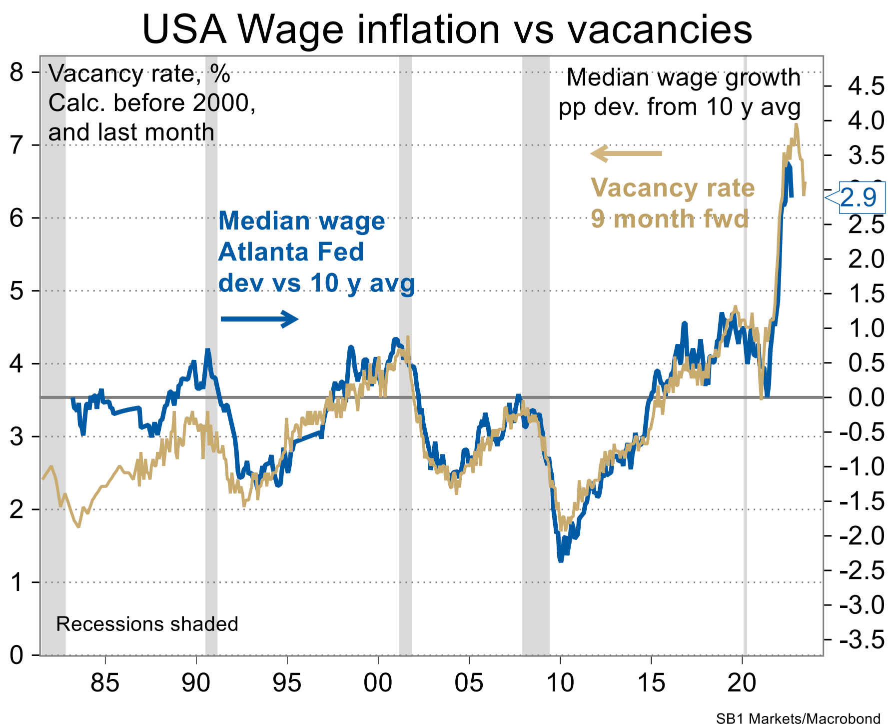


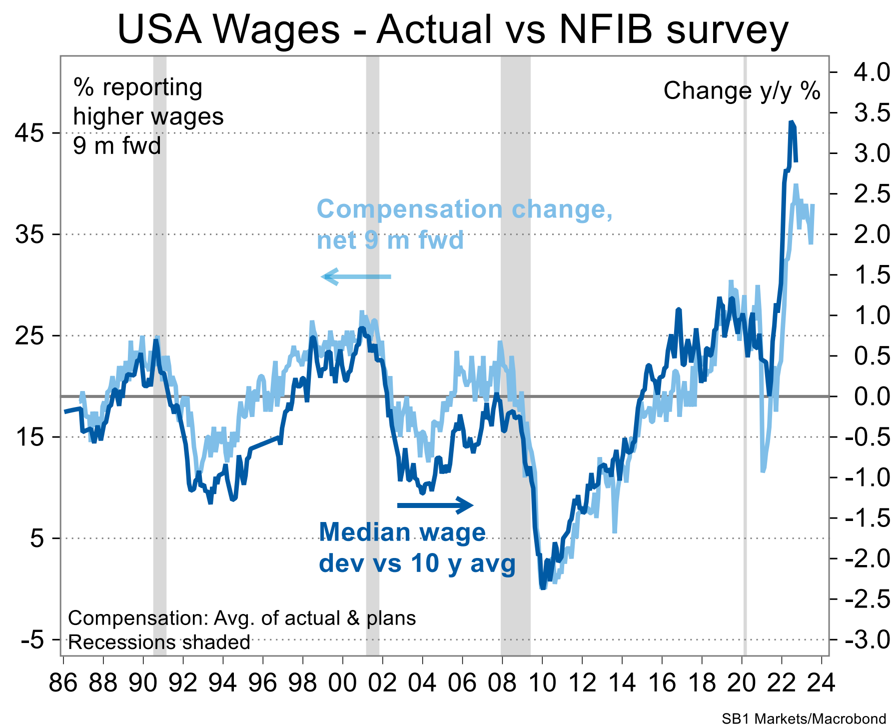
- 46% of SME's report they are **not able to fill open positions** in October, unch. from September. The share remains close to the peak level
- 20% of companies **plan to hire**, down 3 pp from Sept, and well below the 32% at the peak in Aug-21. The trend is down but the level is still unusually high, at the highest level ever seen before the pandemic
- 38% of companies report that they **plan to lift compensation** in the coming months, up from 34% in September. The peak was at 40% last December. Before that, the ATH was at 27%, while the average – signalling no acceleration in wage growth – has been at some 20%
- <u>There is still a ways to go…</u>

SpareBank 1 MARKETS

Both the vacancy rate as well as SME's compensation plans have peaked

And wage inflation may have peaked too, but the level is still way above what will return 2% CPI infl.



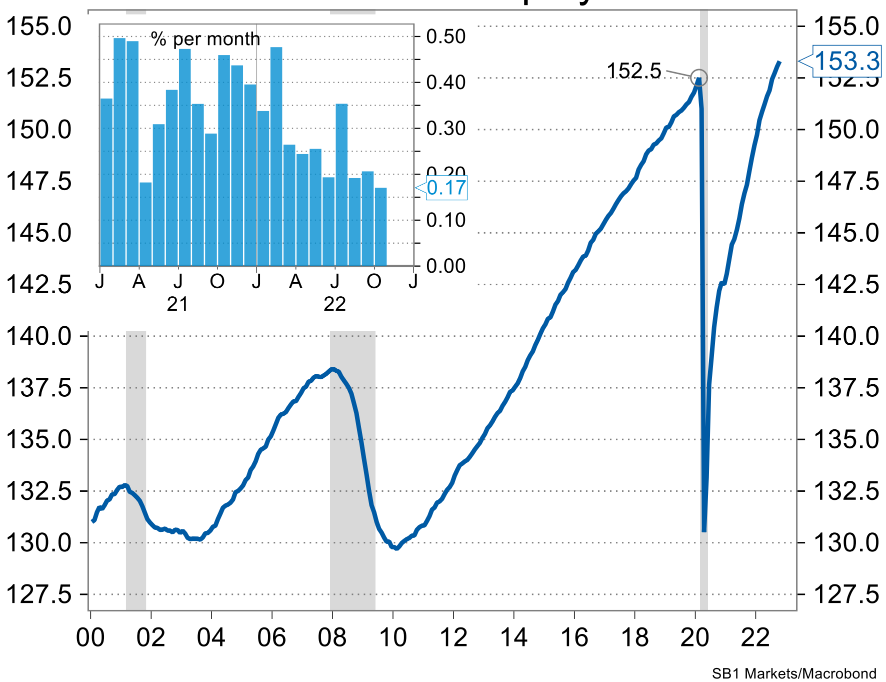


- **Our 'Phillips curve'** based on the vacancy rate signals a further increase in wage inflation the coming quarters even if vacances may have peaked, as the vacancy rate leads changes in wage inflation quite consistently by 3 quarters. However, we would not be surprised if the current extraordinary high wage already has peaked
  - » Companies (SMEs) compensation plans signal continued high wage inflation but not faster than the present
- **Wage inflation** has already accelerated by almost 2.9 pp vs the 10 y average (Atlanta Fed median), and cannot possibly generate a 2% price inflation rate over time. This is Fed's main headache, not the current high CPI inflation print. And it will become the stock owners' headache too, of course
- **Demand for labour has to be reduced sharply in order to get wage inflation back to a sustainable level!**
  - » Check under which circumstances wage inflation slows on the charts above (hint: find the shaded areas, follow the blue wage line - as well as the vacancy rate or the wage hike plans ☺). Fed will not be able to control inflation if demand for labour is not cut sharply. Exactly what Powell told us at the recent press conferences!

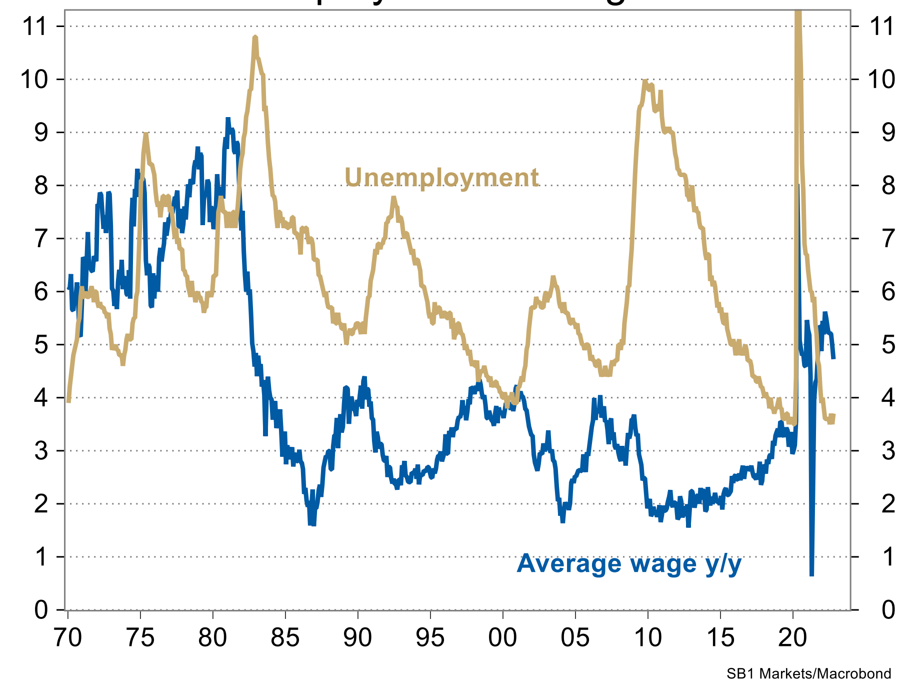
Employment growth is slowing, and unemployment rose in October

In addition, wage inflation may be slowing – but it remains too high, according to the labour report

USA Nonfarm employment



USA Unemployment vs wage inflation

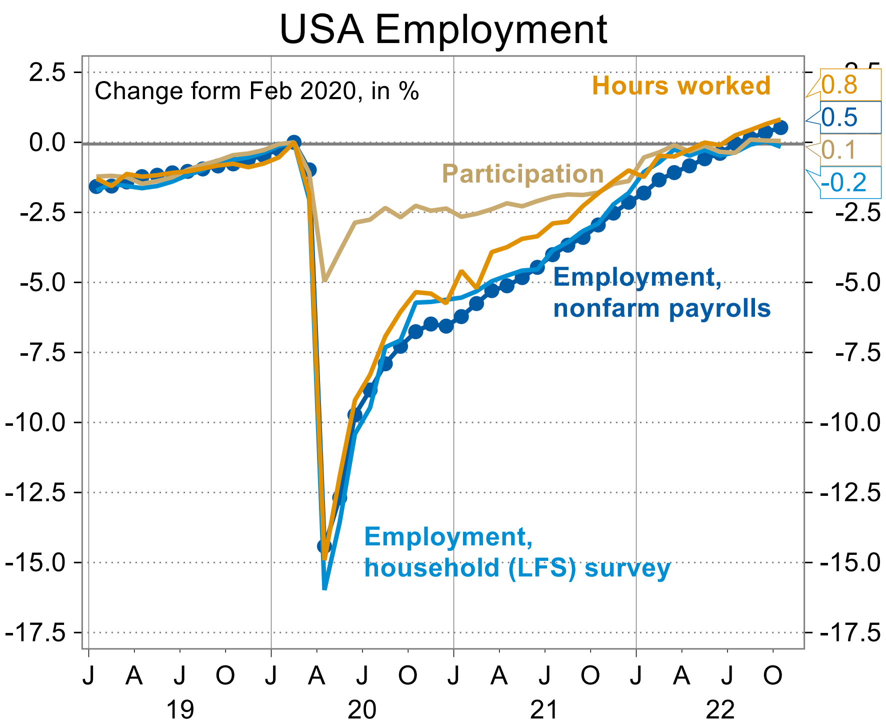


- **Nonfarm payrolls** rose by 261' in October, expected 200' (Sept data was revised up by 52' to 315') but growth is gradually slowing. The LFS employment fell by 0.2% and the **employment rate** was down 0.1 pp to 60.0%. The employment rate has flattened since March – surely not a signal of strength
- **The participation rate** decreased by 0.1 pp to 62.2%, and the level has been flat so far this year. The unemployment rate still rose by 0.2 pp to 3.7%, expected up to 3.6%. The FOMC Q4 forecast at 3.8% is not far away, but one month's data is not sufficient to ease anyone's nerves
- **Wages** rose 0.4% in Oct, 0.1 pp more than expected and than the Sept increase. Measured 3m/3m, wages are up 4.4%, and clearly declining! The annual rate fell 0.3 pp to 4.7%, as expected. Still, wage inflation is well above par; Average wages rose by 3¼% in 2019, and well below 3% in the years before (and other and better wage indicators signals higher wage growth)
- The unemployment rate is still too low, and wage inflation is too high. <u>The next month's data will be crucial if the FOMC should comfortably ease the pace of rate hikes to 50 bps</u>

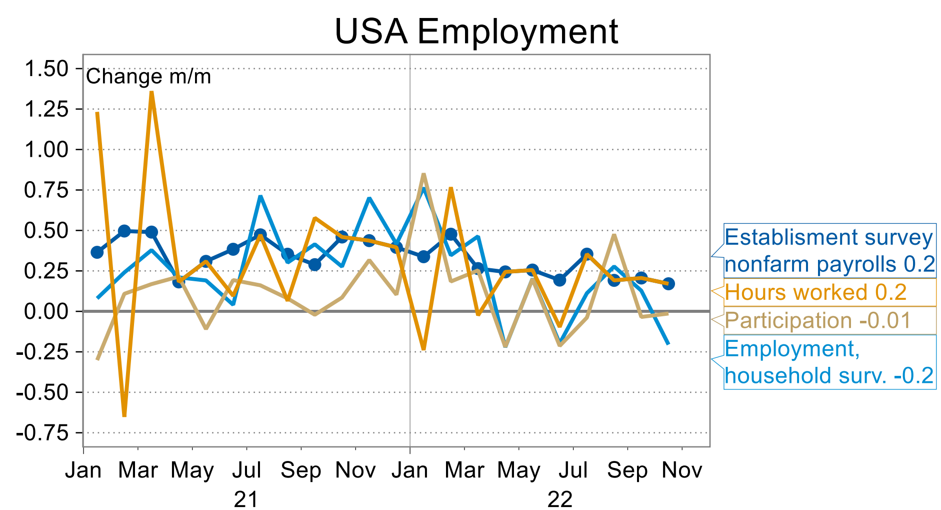
SpareBank 1 MARKETS

Employment (and hours worked) now above the pre-pandemic level

... Before we adjust for growth in population since early 2020



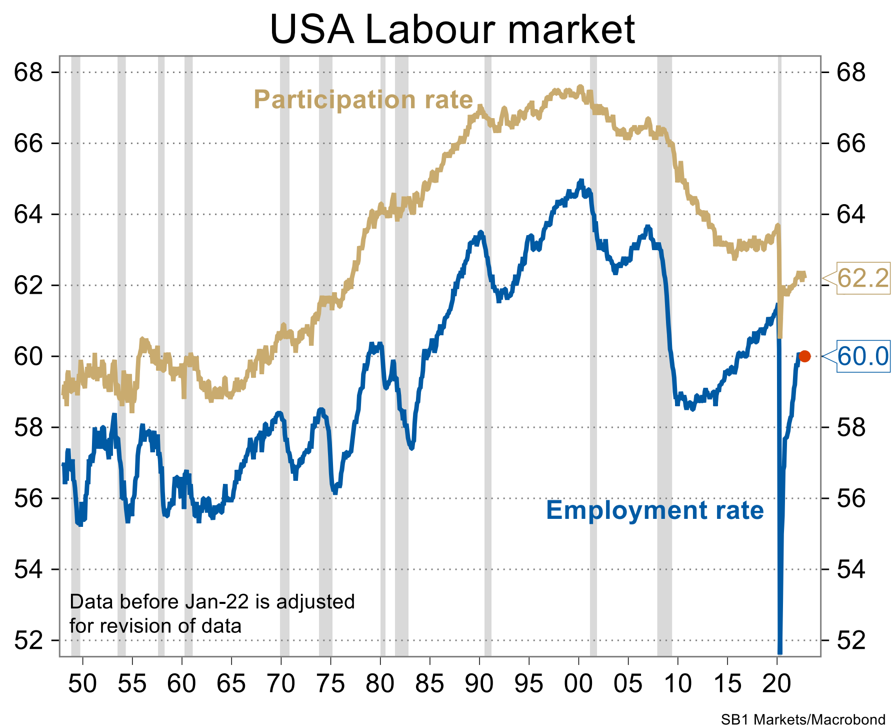
- **Nonfarm payrolls** (employees) are now 0.5% above the Feb '20 level, while **total employment** measured by the **household survey** (LFS/'AKU') is down 0.2%, and it has flattened since Q1. The survey data are more volatile the payrolls stats, but the two measures are quite similar over time. The **employment rate** is 0.2% below the pre-pandemic level
- **Labour market participation** is 0.1% above the Feb-20 level. **The participation rate** was reported down by 0.1 pp to 62.2%, and it is still down 1.5% vs the pre-pandemic level
- **Aggregate hours worked in private sector** gained 0.2% in October, due to the increase in employment

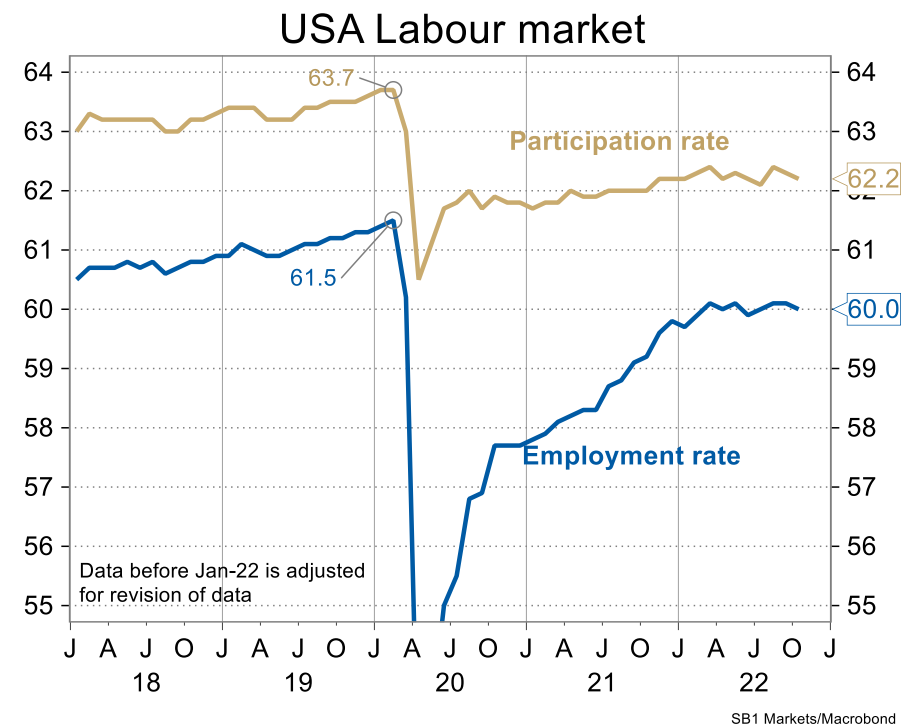


SB1 Markets/Macrobond

Labour force survey: The participation rate down, flattish in 2022

The employment rate also marginally down in October

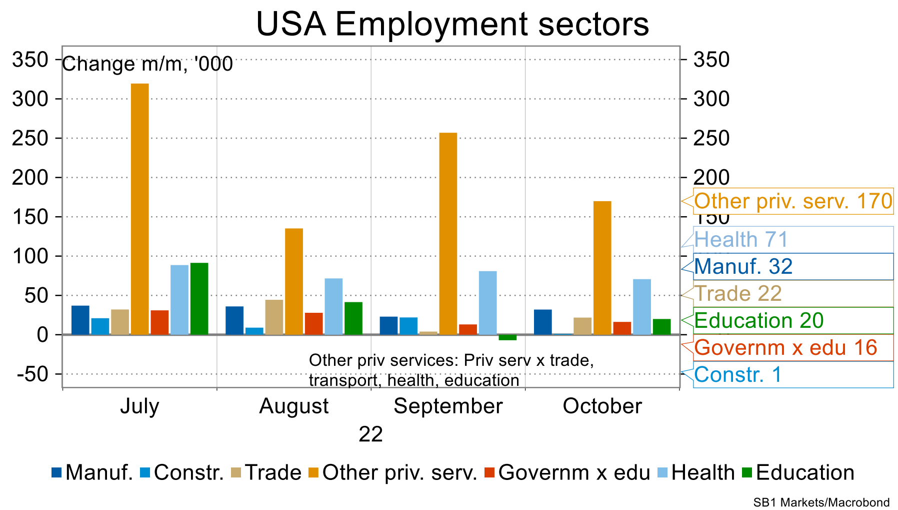


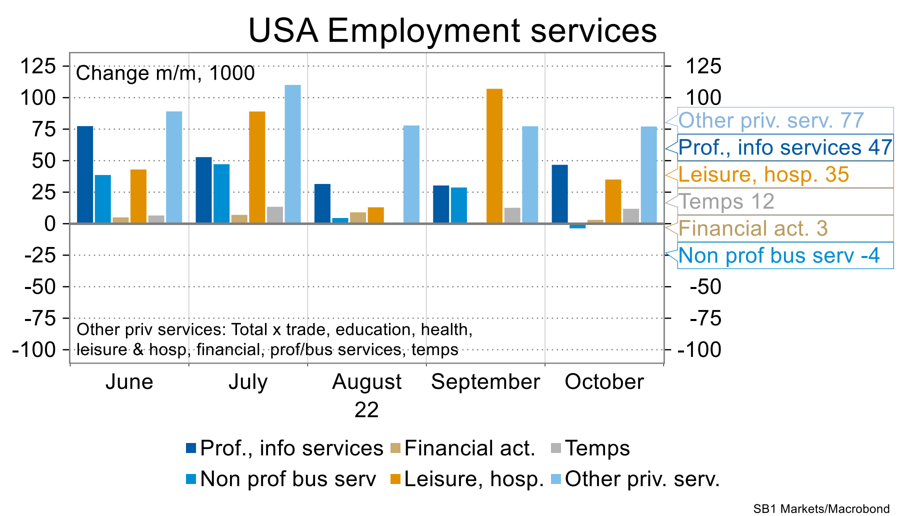


- In October, **the labour force participation rate** declined 0.1 pp to 62.2%. The participation rate has not climbed further in 2022, even if demand for labour has been – and still is strong. The participation rate is 1.5 pp (2.6%) below the pre-pandemic local peak – which again was way below the pre-IT bubble peak, in year 2000 – as the population ages
- **The employment rate** also fell by 0.1% to 60.0%. The short term trend is flat too, as growth in employment has slowed. This rate is 1.5 pp below the pre-pandemic local peak

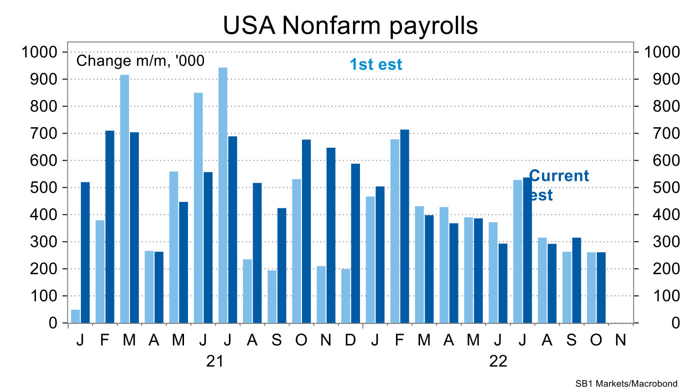
In October: Solid growth in most sectors, services in the lead – as usual

The financial sector, and education the only main sectors down



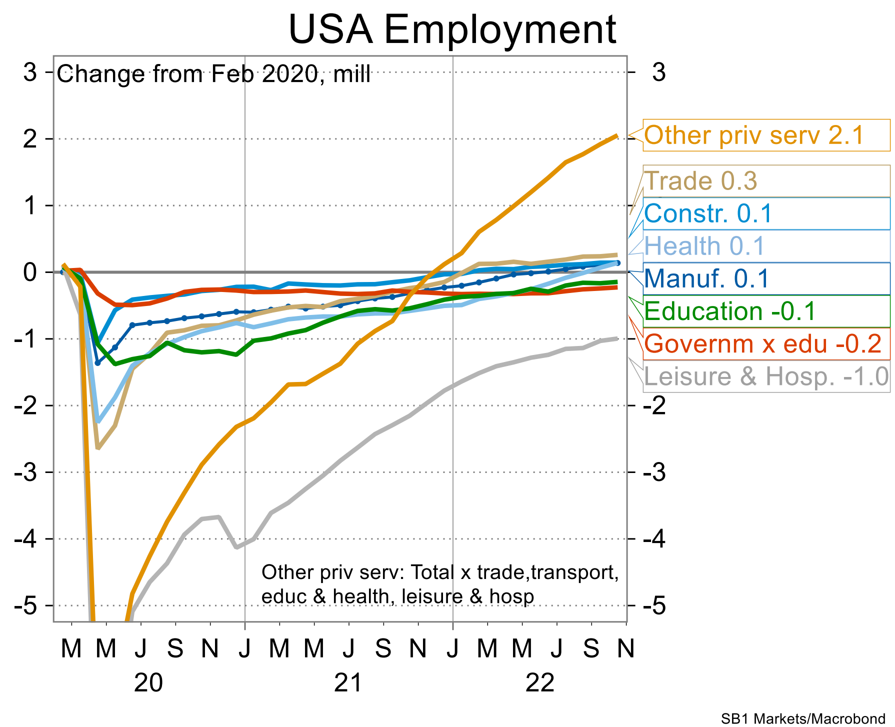


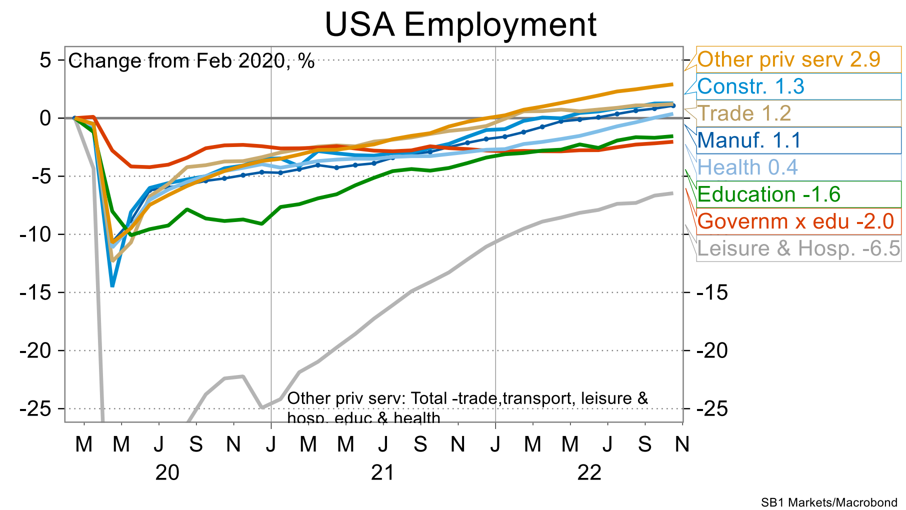
- **Last month:**
  - » **Leisure & hospitality** (restaurants ¾ of the total, hotels, parks, gambling, arts++) added 35' jobs
  - » **Trade** added 22' jobs but growth will likely, alongside flattening retail sales of goods, come down
  - » A broad increase in payrolls in other **private services**
  - » **Manufacturing** added 32'; growth is slowing but it is still higher than normal
  - » **Construction** sector employment up by 1', far less than normal, but still better than the decline in construction activity suggests. A decline in employment is quite likely
  - » **Education** (private & public) up by 20'
  - » Employment in **government** (ex education) rose by 16', better than normal – and growth has turned positive recently



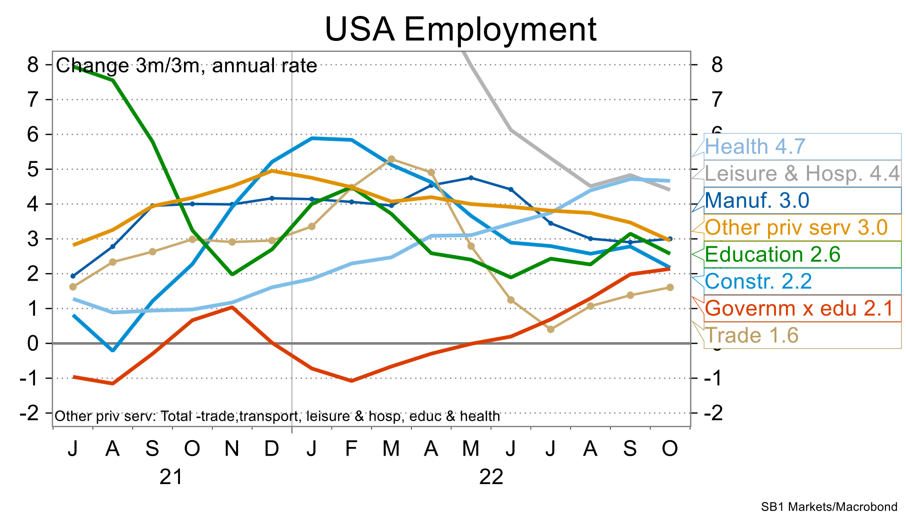
Vs. Feb-20: Several private services are up, but leisure/hospitality still down 6.5%

Trade, manufacturing and construction are back to their pre-pandemic levels



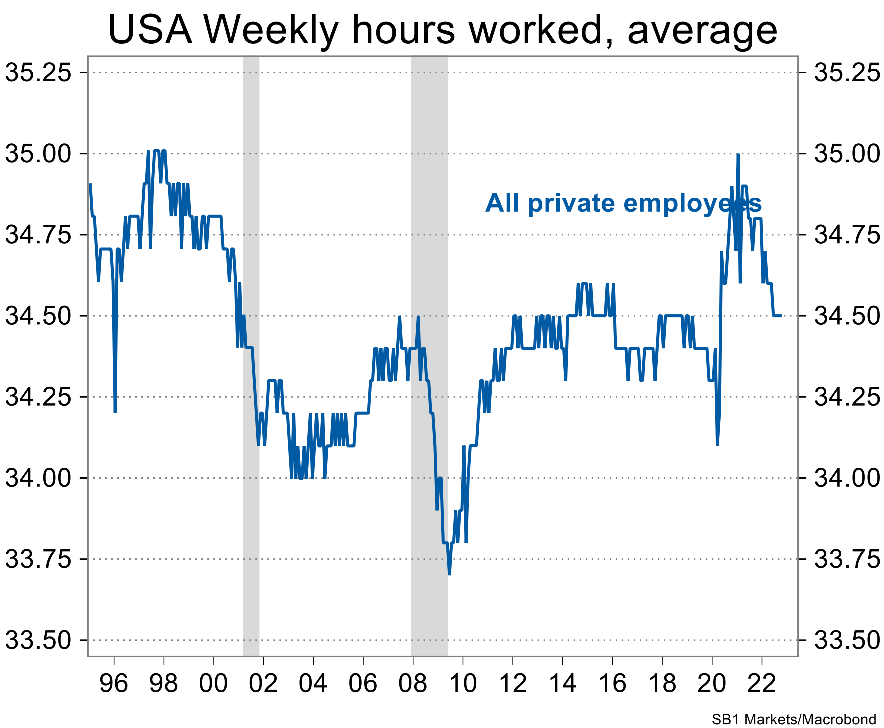


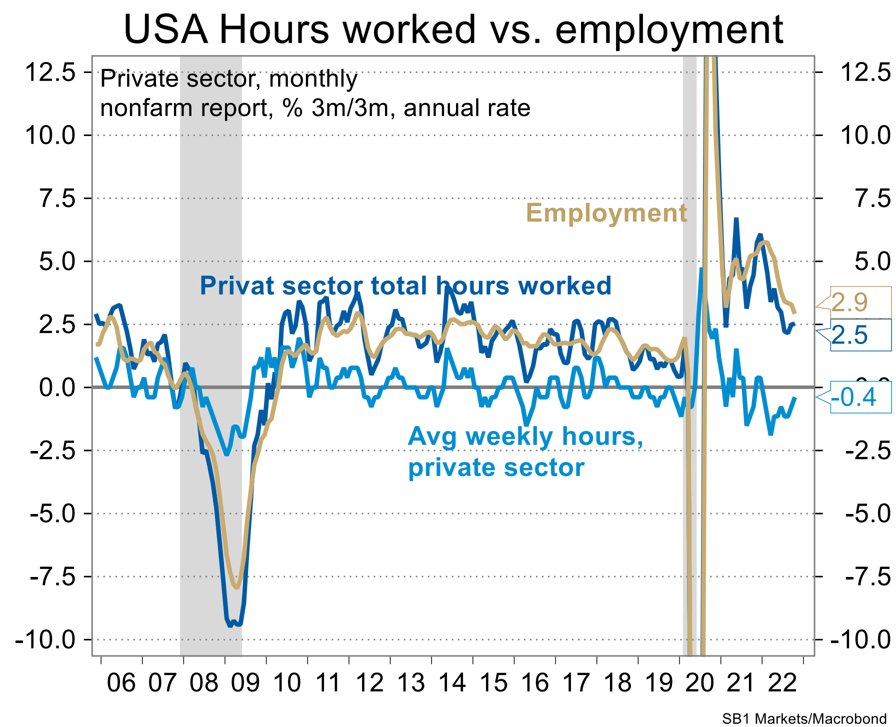
- Recent months, underlying growth (3m/3m) has slowed in manufacturing, construction, and in 'other services' – others are reporting faster growth



Average weekly hours is trending down, hours worked up as employment is up

The decline avgerage weekly hours from Nov-21 is strange, given lack of labour

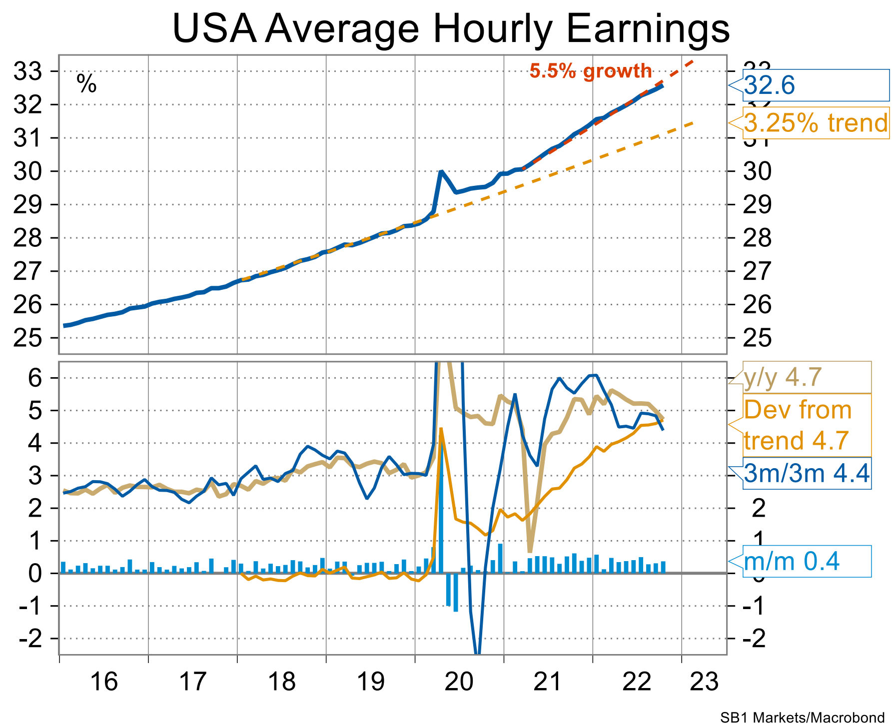


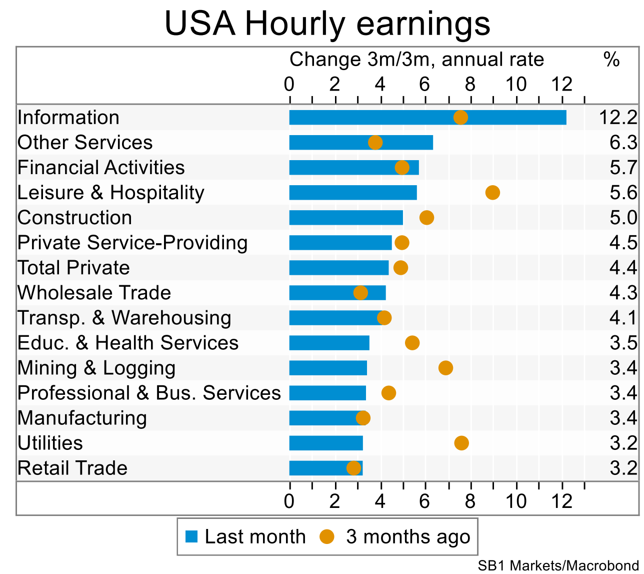


- Hours worked is up at 2.5% in the non-farm private sector last 3m/3m

Wage growth at a 5% – 5.5% pace – but is easing

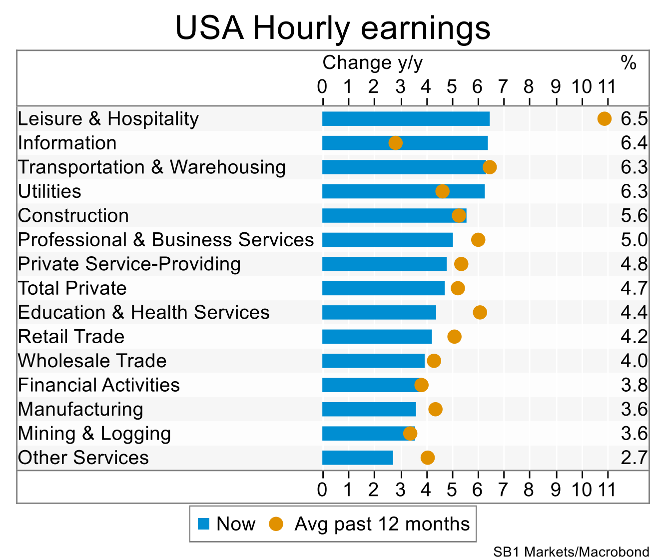
8 sectors report slower underlying (3m/3m) wage growth, 4 sectors faster growth (than 3 months ago)





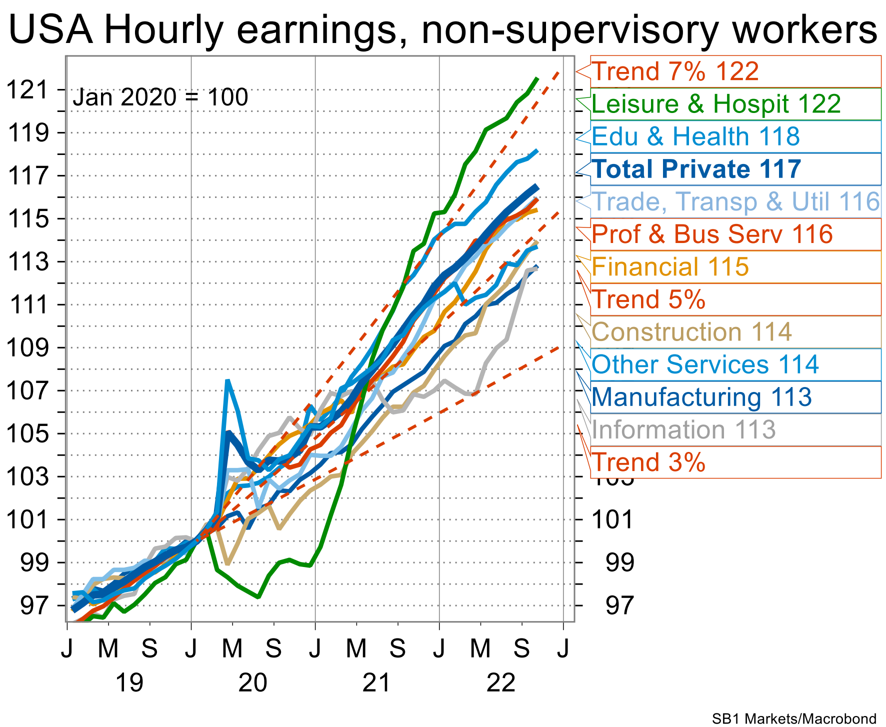
- The **average wage** rose by 0.4% in September, 0.1 pp above expectation. Annual wage inflation fell 0.3 pp to 4.7%, in line with expectations
  - » Underlying (3m/3m) growth came down 0.4 pp to 4.4%, the slowest pace since Q3-21
  - » Just before the pandemic, wage inflation was at approx. 3¼%, but it was below 3% until late 2018 – and that 3% inflation yielded 2% CPI inflation

These monthly wage data are not adjusted for the change in employment mix between sectors or within sectors. Check more wage indicators at the next pages



Wages are climbing at a 4% – 7% pace

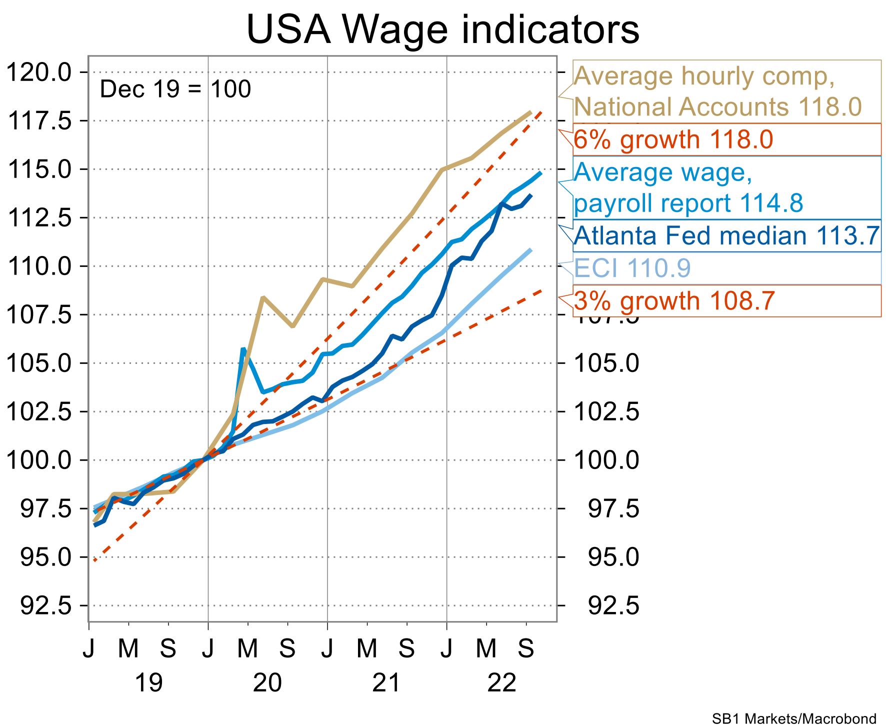
... And well above the pre-pandemic growth paths in all sectors

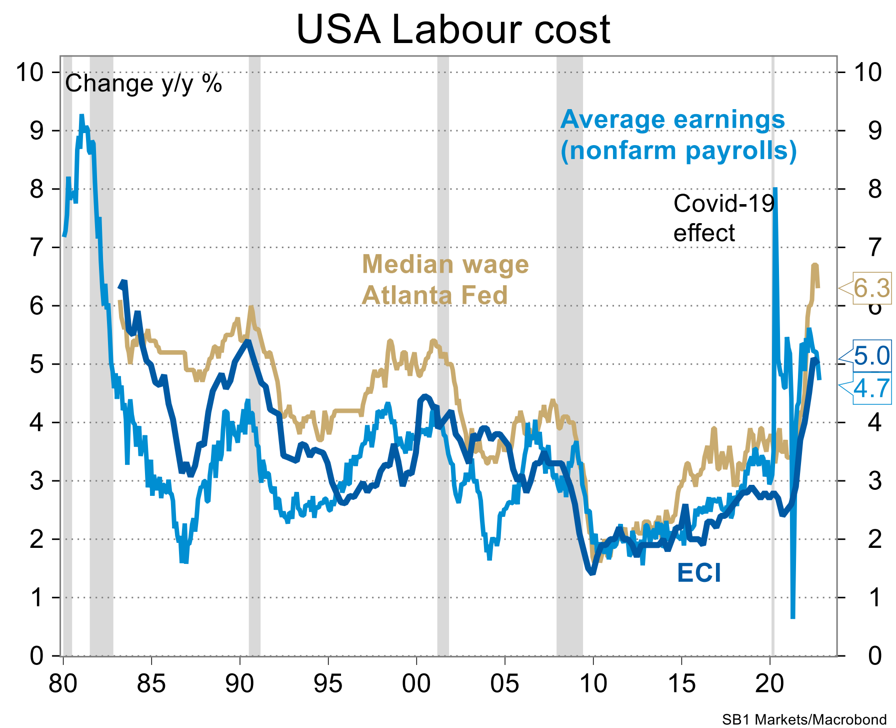


Memo: On the chart above, wages for non-supervisory workers are shown. When all employees are included, growth is slightly lower in most sectors

All indicators combined: some signs that wage inflation may have peaked

However, all are reporting much higher wage inflation than pre Covid: 2% price inflation 'impossible'

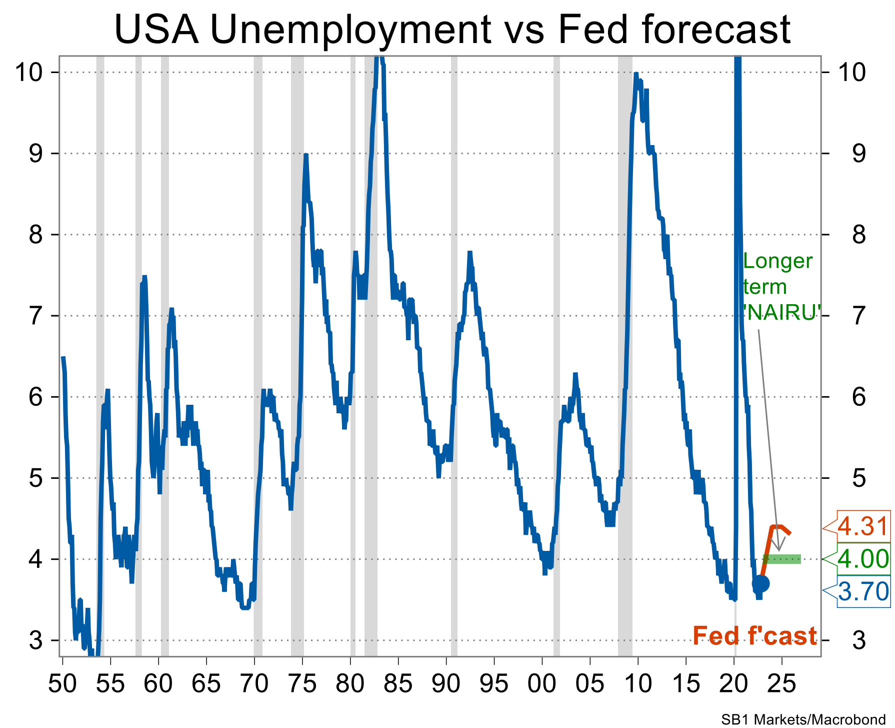


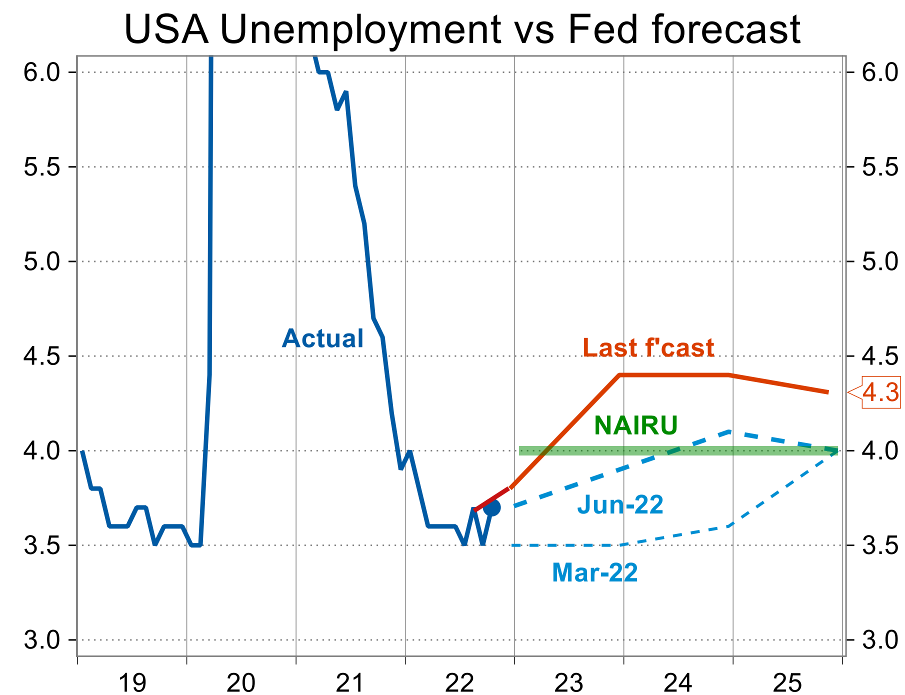


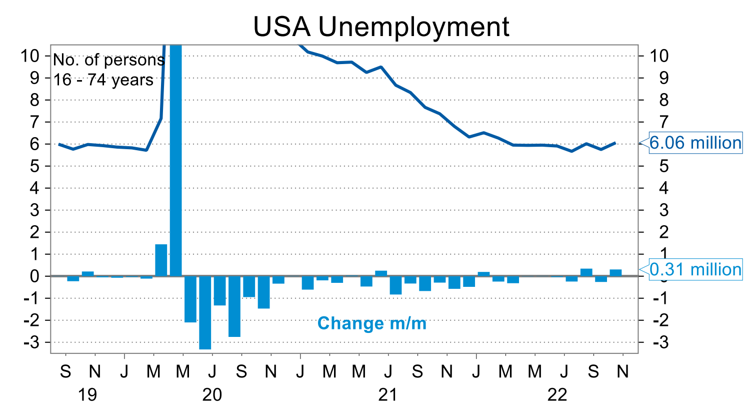
- **All wage indicators** are reporting faster wage growth, and all reporting wage growth well above the average recent years. More on hourly earnings in Q3 here
- Growth in wage/earnings/compensation indicators are up 2.5 – 4 pp vs the their respective 10 y averages before the pandemic
- Over the past 10 years, inflation has been close to 2% (before the pandemic, that is)
- It will be a impossible to keep inflation at 2% if wage inflation remains at the current levels. Productivity growth has not accelerated. Profit margins may take a beating – and they no doubt will – but not sufficient to bring inflation down to acceptable levels on their own. Wage inflation will probably not slow by much before demand for labour weakens – and unemployment increases

Fed's hope: just a marginal increase in unemployment the coming years

Even if excess demand for labour has to be cut dramatically. Not impossible. But not likely



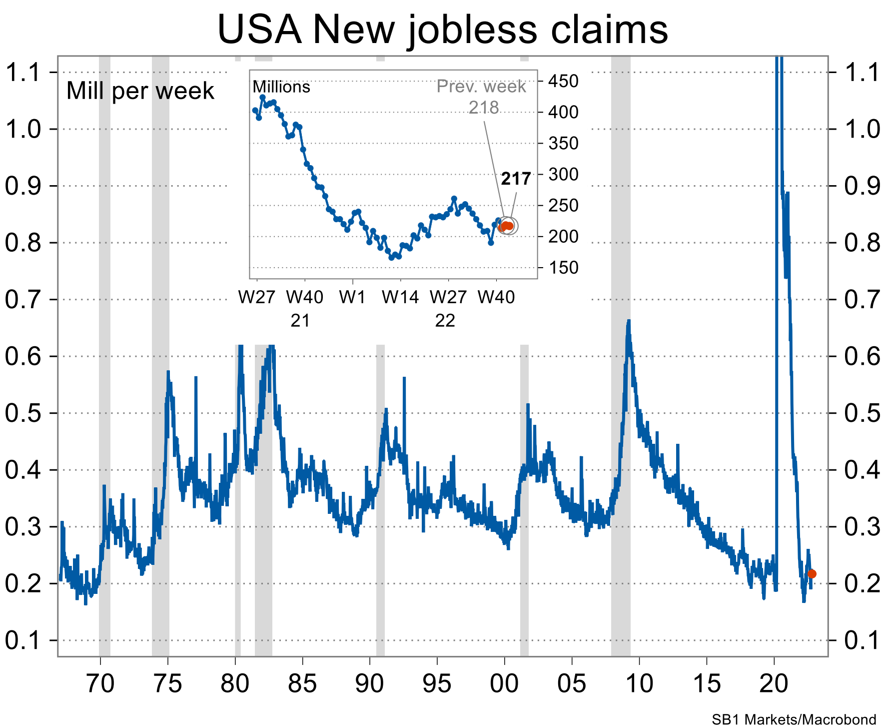


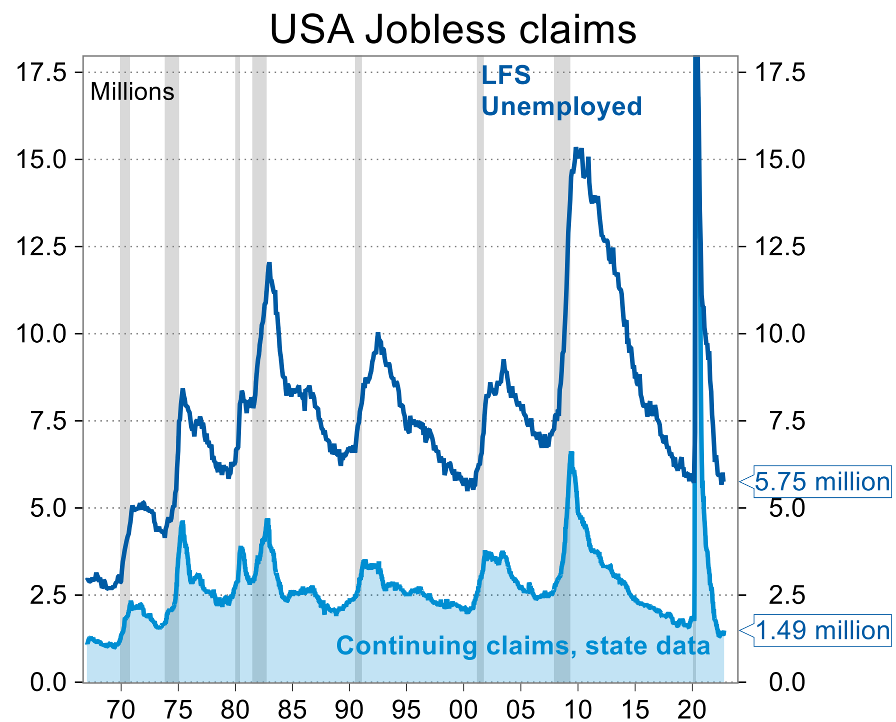


- Unemployment increased by 310' persons in October

The inflow of new jobless claims remains at very low level

New jobless claims just marginally down to 217’, expected 220’

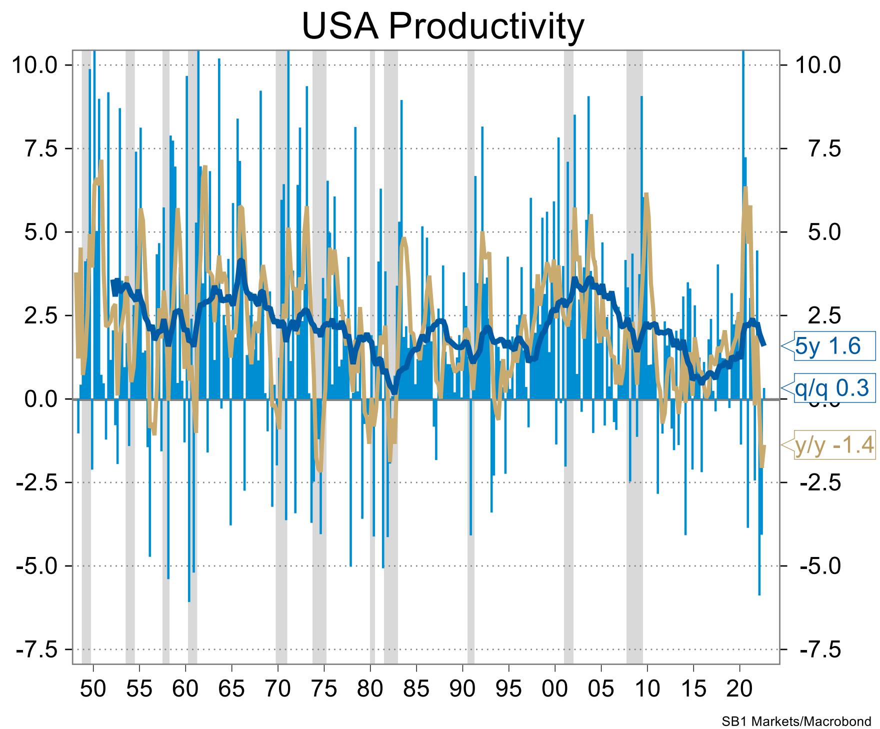


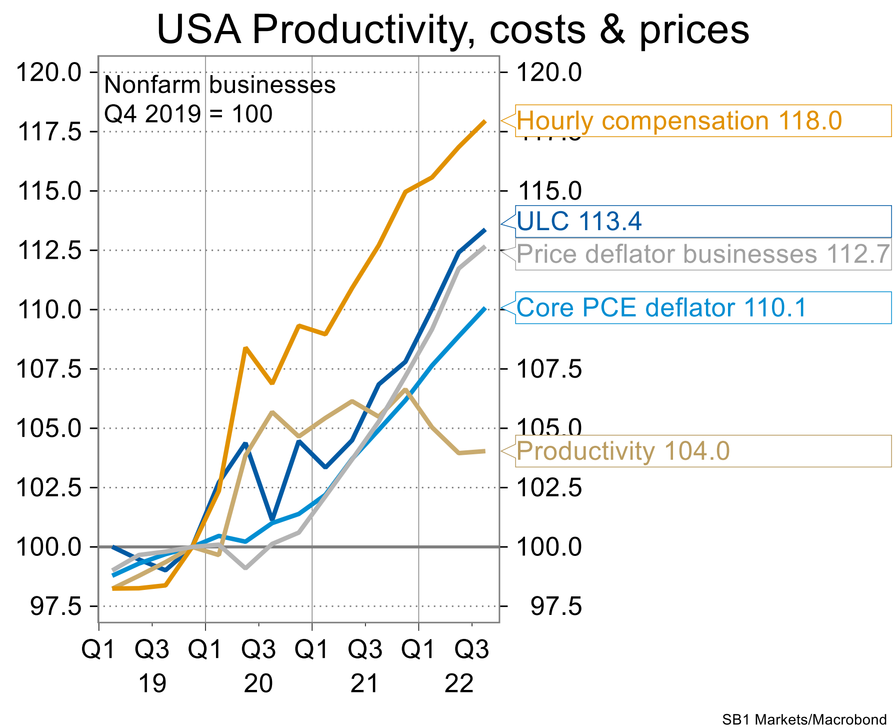


- **New jobless claims** fell by 1’ to 217’, from a 1’ upward revised number the previous week
- **Continuing claims** rose by 37’ to 1,485’ in week 42. The trend is slightly upwards but the level remains very low
- Both indicate a very tight labour market

No growth in productivity in Q3 but growth past 3 years revised up by 0.8 pp/y!

Unit labour cost is revised down by the same amount, still climbing far too fast



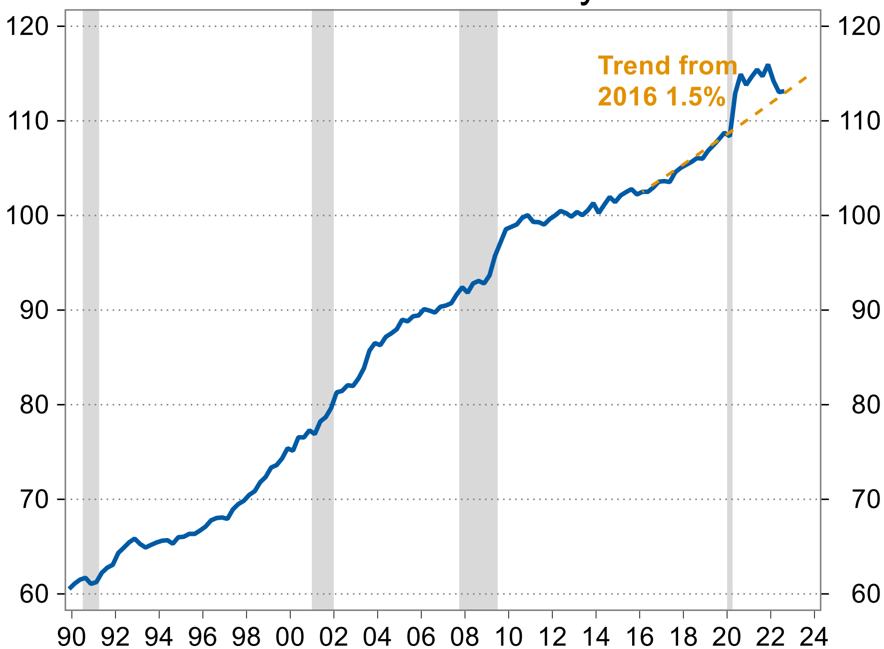


- **Productivity** rose by 0.3% in Q3 (annualised), expected up by 0.6%, after the unusual steep decline during H1. Over the past 4 quarters, productivity has fallen by 1.4%, as less productive (and less paid) service sector workers have returned to their jobs after the pandemic). However, following the upward revision of GDP growth since 2019 (in the annual revision, published some weeks ago), productivity growth was revised substantially upwards, from a 0.6% average pace to a 1.4% average pace! That's still not impressive, but in line with recent history (check the two following pages)
- **Hourly compensation (wages ++)** grew at a 3.8% pace in Q3, and the annual rate is 4.7%. Average growth since Q4-19 is 6.2%. Growth is slowing somewhat, but not convincing as lower paid service sector workers have returned to work, taking the average wage down
- **Unit labour costs** (hourly compensation – productivity) grew by 3.5% in Q2, up 6.1% y/y. Since Q4-19, ULC has grown at a 4.7% pace, revised down from 6.4% but still far above a normal level – which of course is incompatible vs the 2% inflation target

The current productivity data are not that bad!

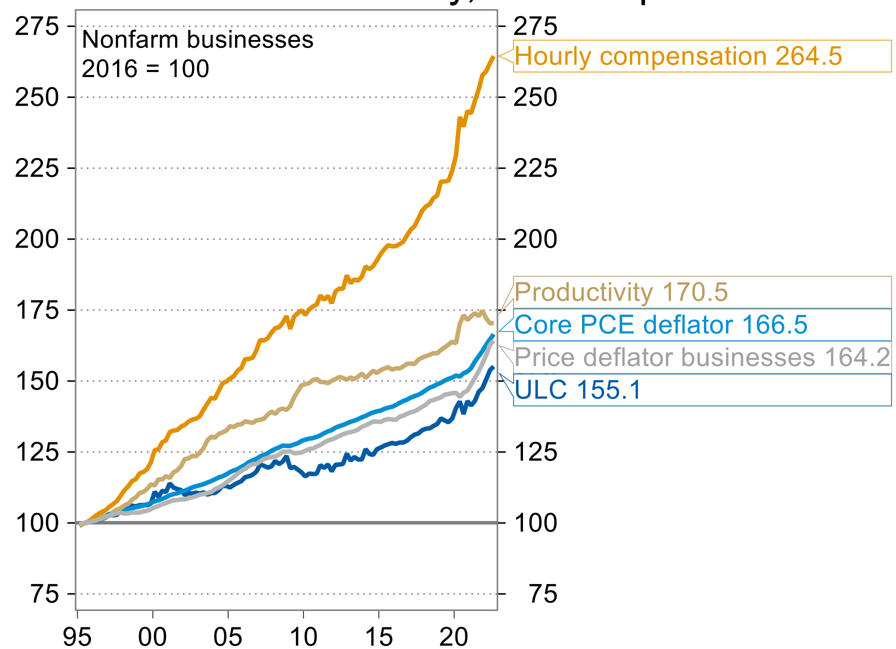
(but unit labour costs are still not reassuring)

USA Productivity



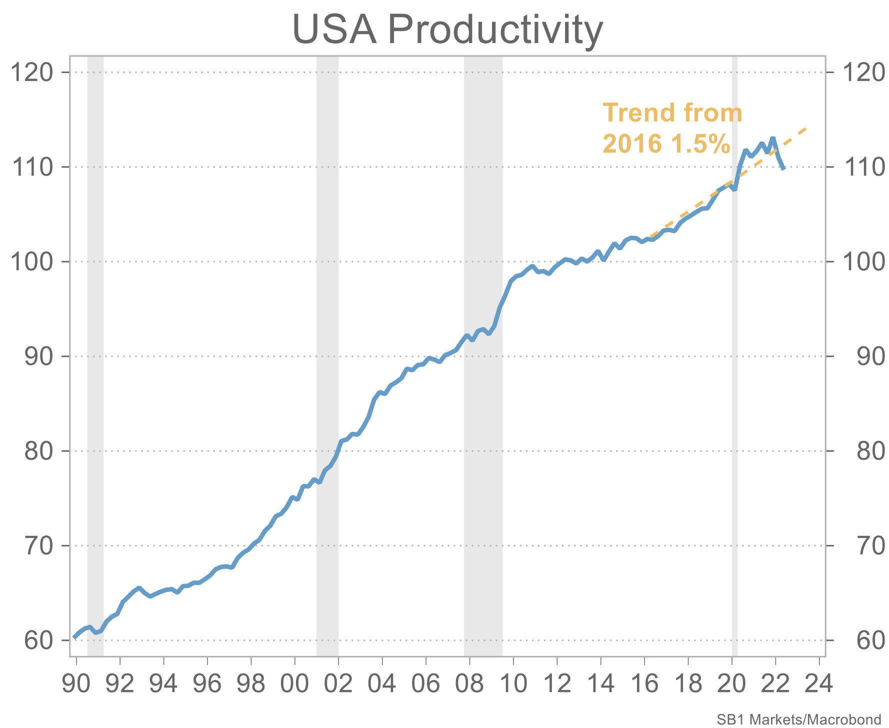
SB1 Markets/Macrobond

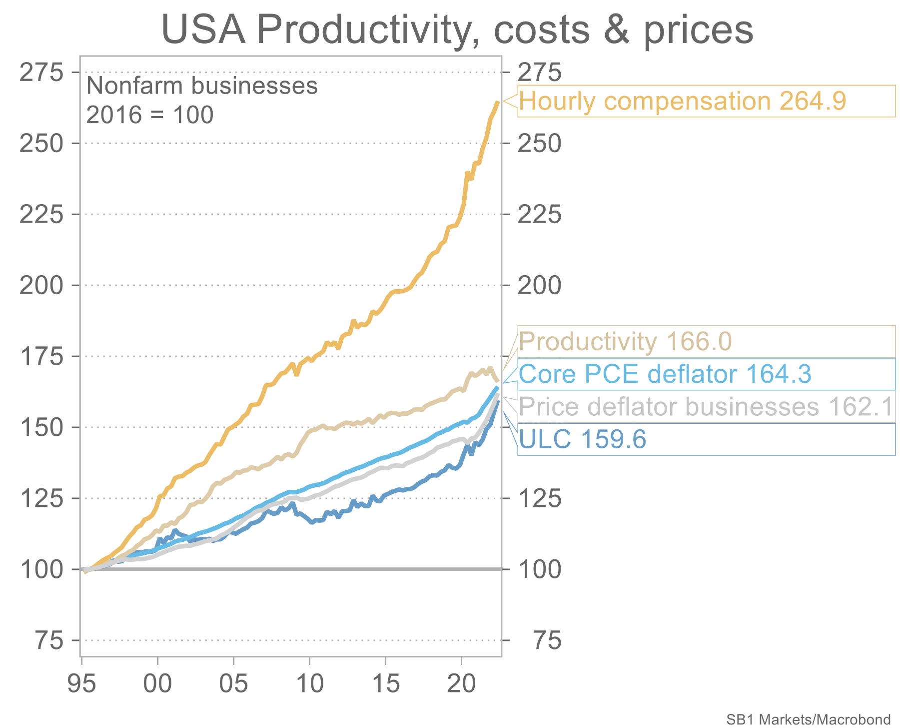
USA Productivity, costs & prices



SB1 Markets/Macrobond

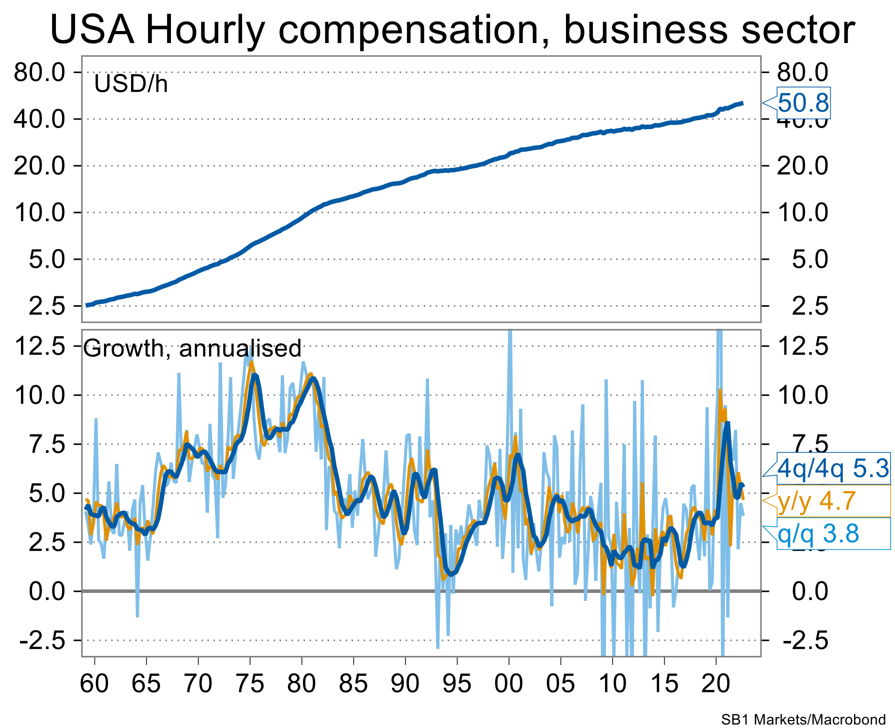
Before the GDP revision: Productivity was weak, cost were rising very fast

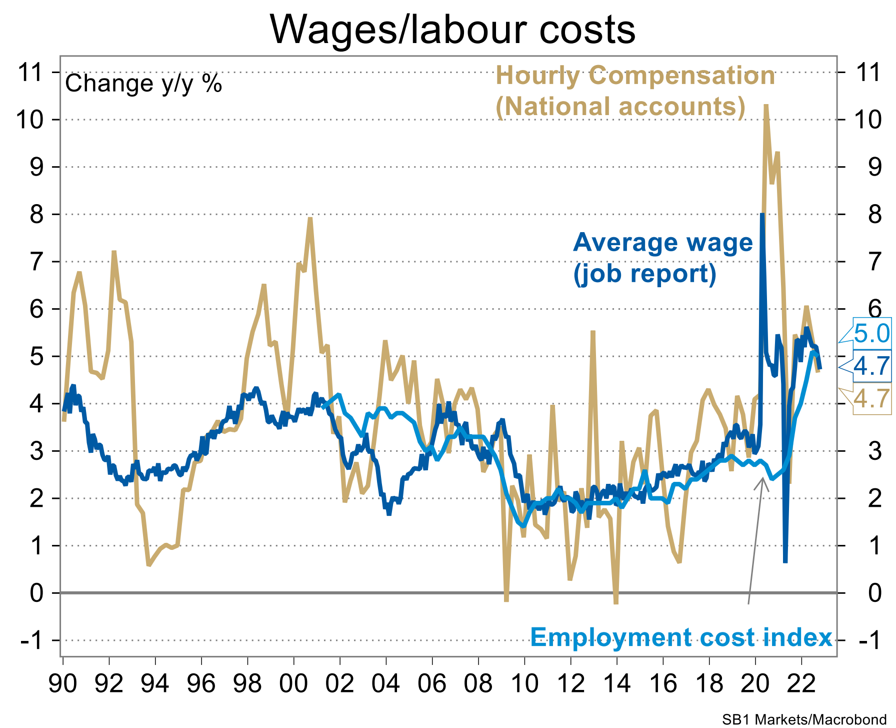




Hourly wage cost inflation has peaked, but remains above the pre-pandemic level

Wage inflation has slowed, as low productive (and less paid) service sector workers have returned

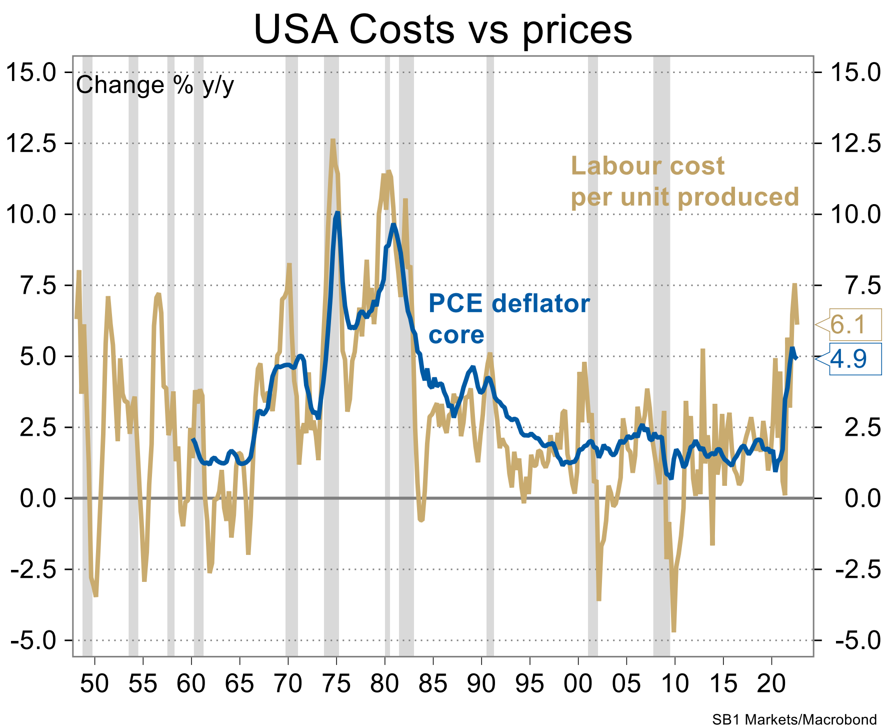


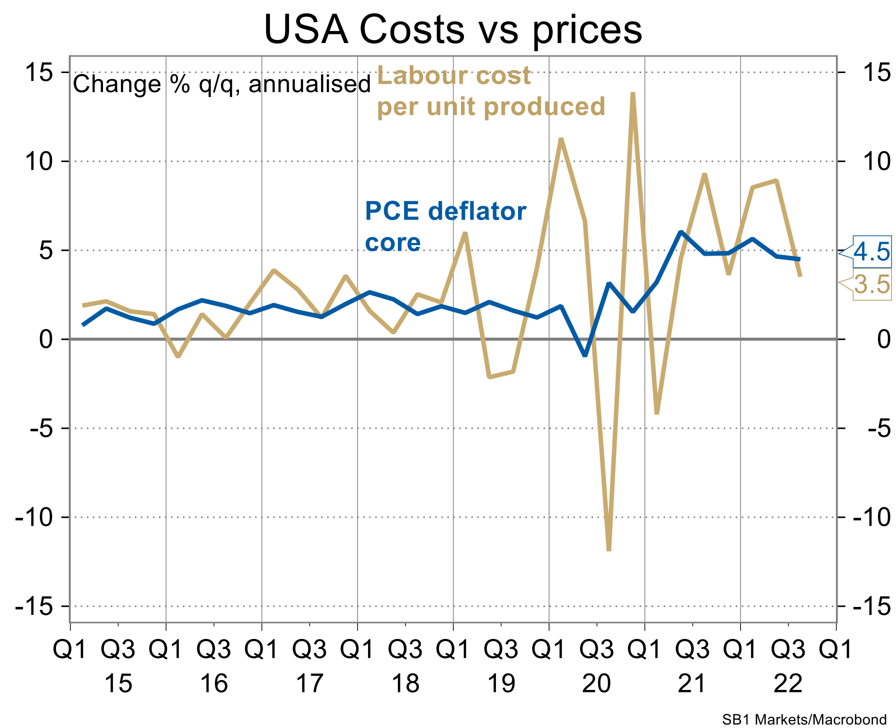


- Hourly labour cost is up 4.7% y/y, and smoothed 4q/q4 at 5.3%
- The average over the 10 years before the pandemic was 2.5% (and until 2018 even lower)
- National hourly labour costs are very volatile short term, but is over time close to other wage indicators

Labour costs per unit produced up 6.1% the past year – but slowed to 3.5% in Q3

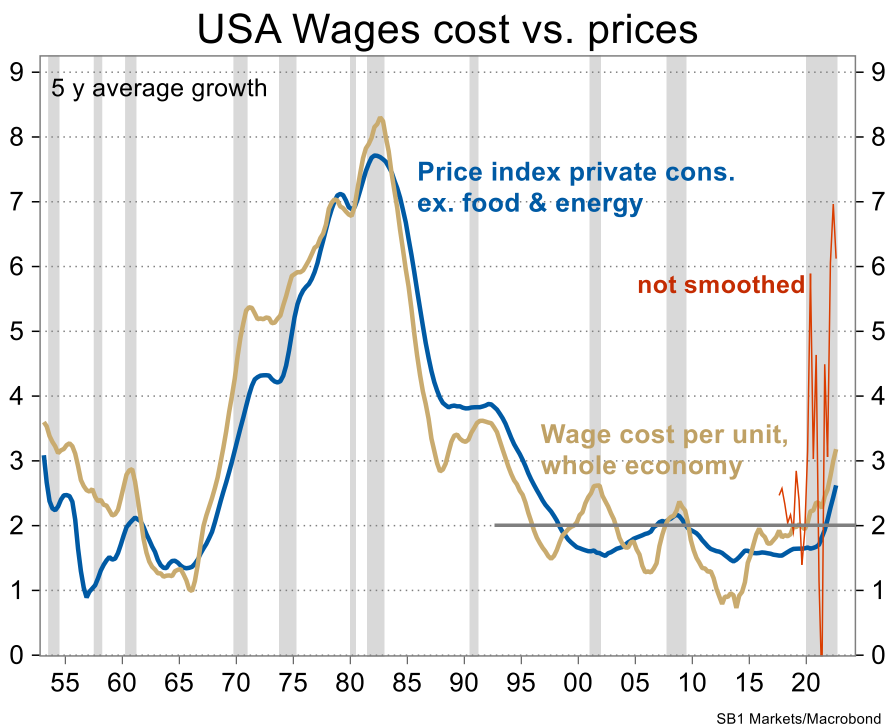
Growth in ULC the previous quarters have been the highest in 4 decades

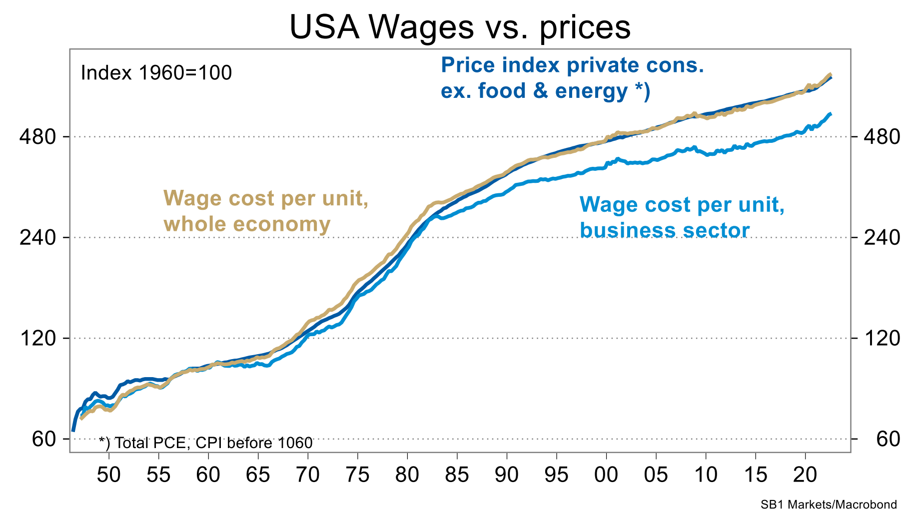


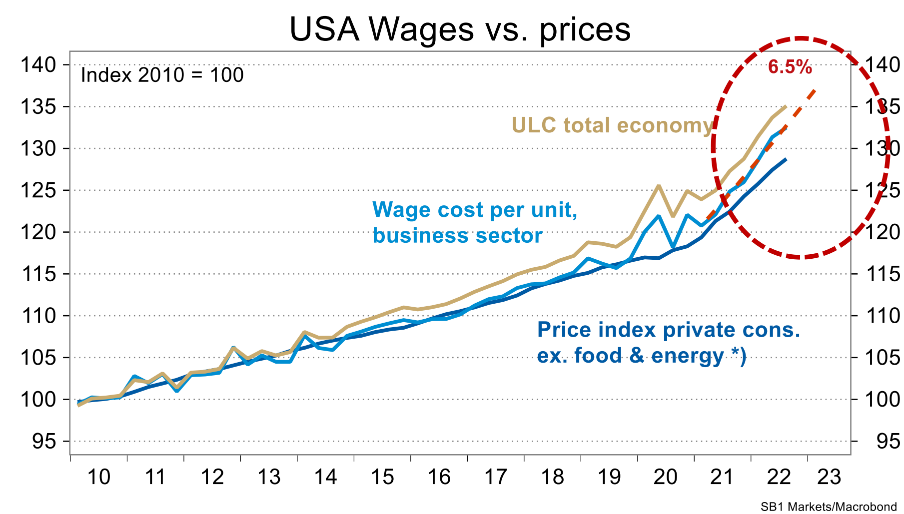


Wage inflation is still the main risk, not raw materials/energy/corp. margins

Core inflation will be hard do get down, given the cost surge recent quarters

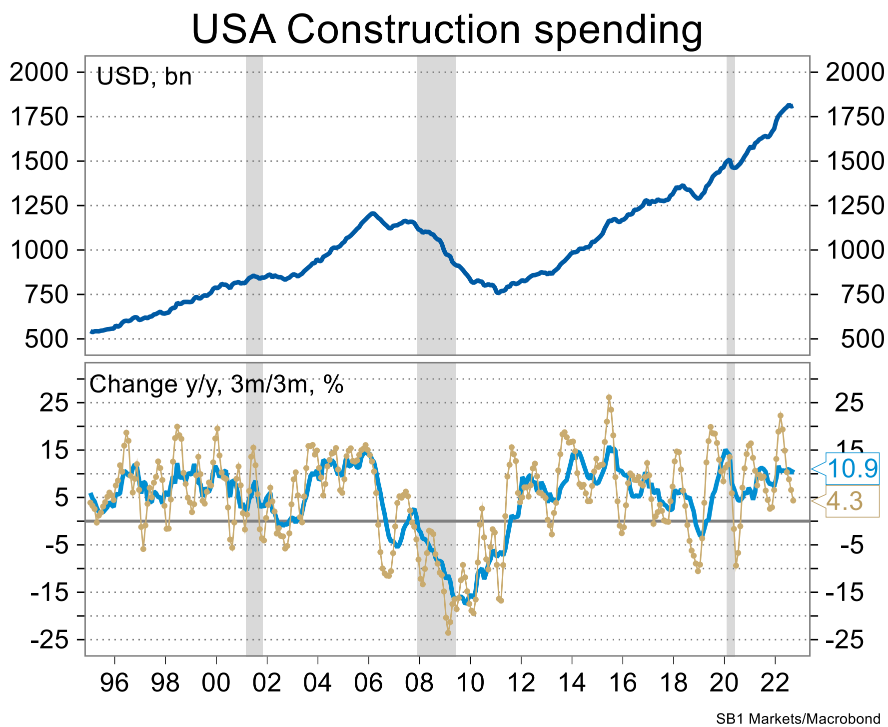


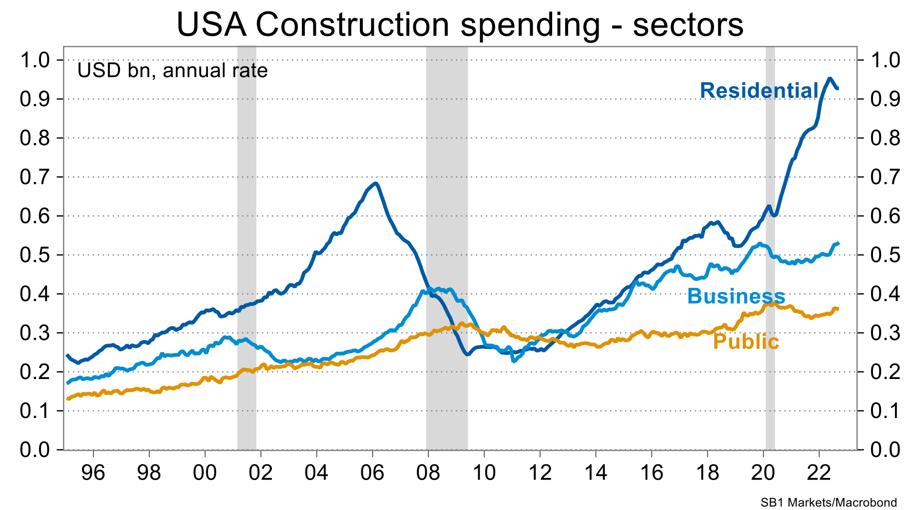


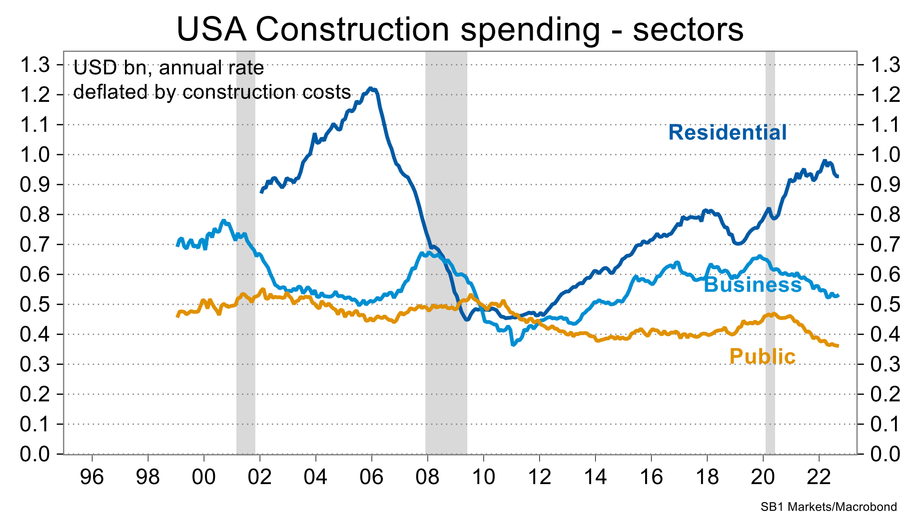


USA construction spending <u>increased</u> by 0.2% in September (expect. down 0.5%)

The increase was solely in the business segment. The trend, however, is down for all sectors



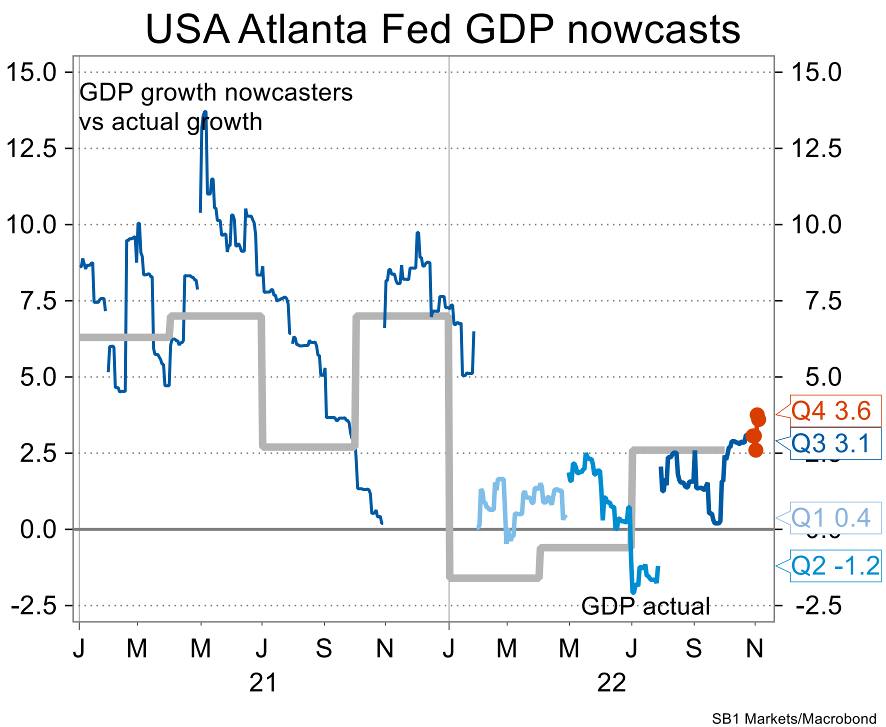


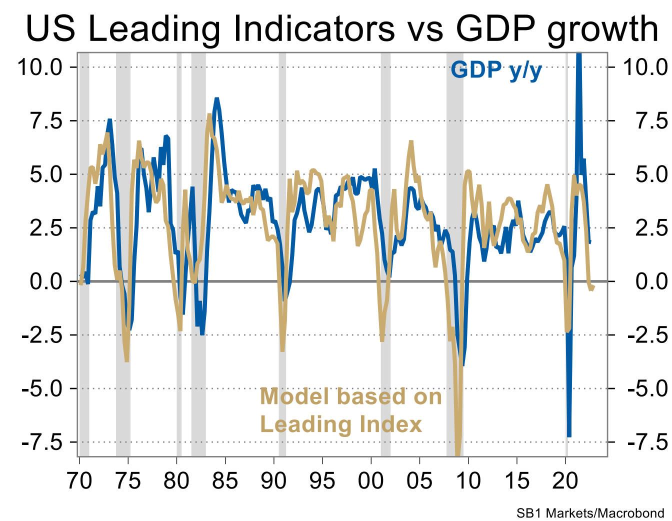


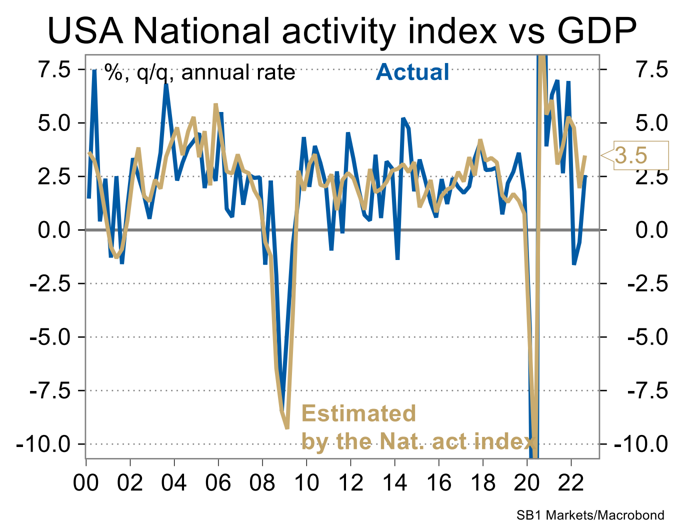
- **Spending data** are published in nominal terms – and constructions costs have surged (but will slow now)
- **Residential construction investment** volumes are now falling
- **Business construction investment** volumes have been falling since before the pandemic – which is good news: the downside is not that large
- **Public sector investment** volumes have fallen since early 2021 (Biden's infrastructure success?)

Atlanta Fed's Q4's forecast stable at 3.6%!

Private consumption, investments are turning up, less support from foreign trad in Q4 vs Q3





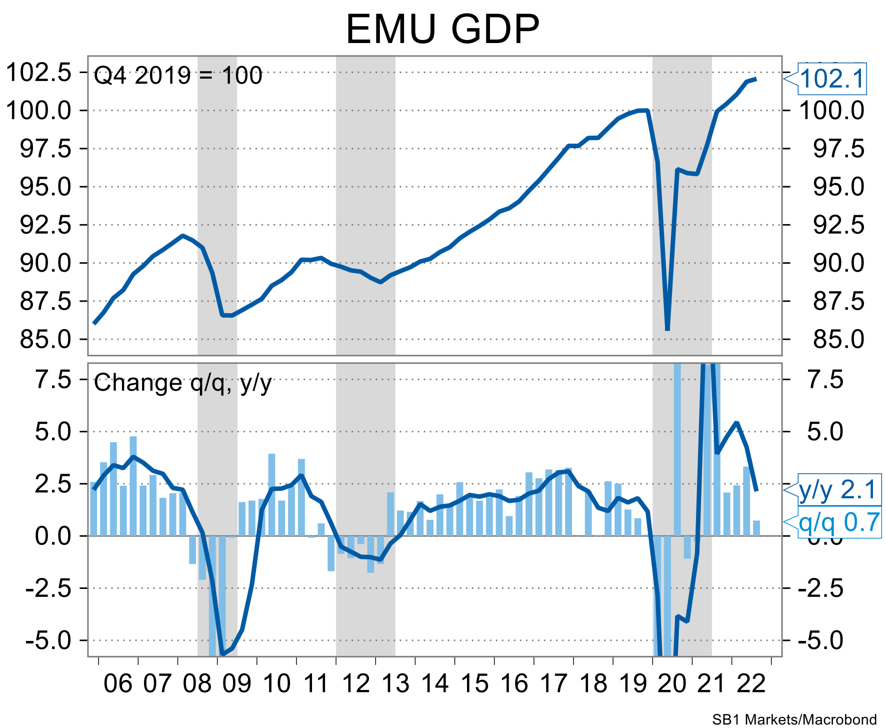


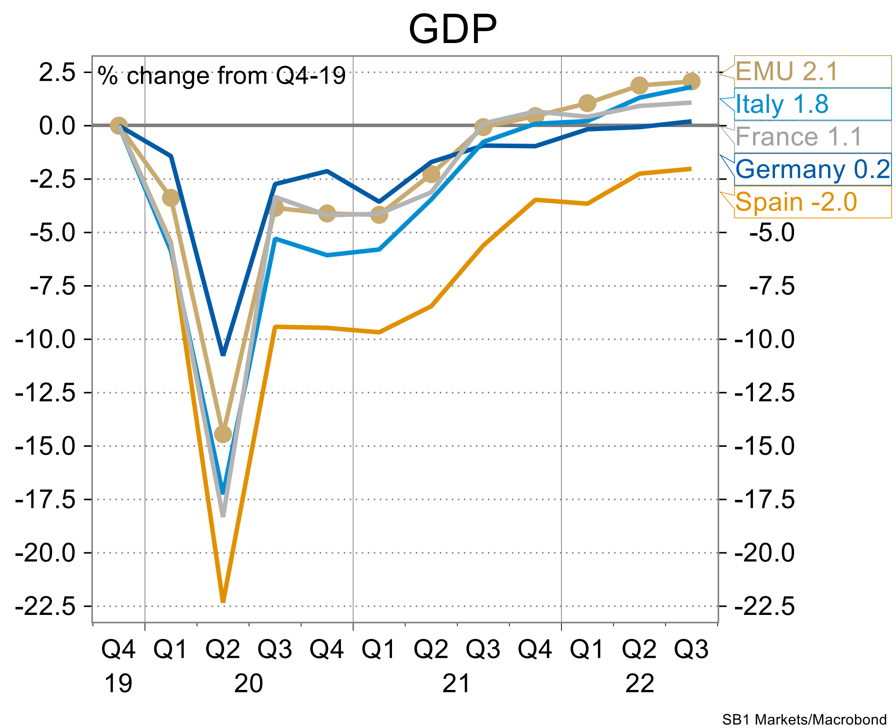
- National Activity index suggests 4% (the July pace). Leading indicators say zero!

SpareBank 1 MARKETS

No recession yet: Eurozone GDP expanded at 0.7% (annualised) pace in Q3

The market expected a 0.4% growth pace

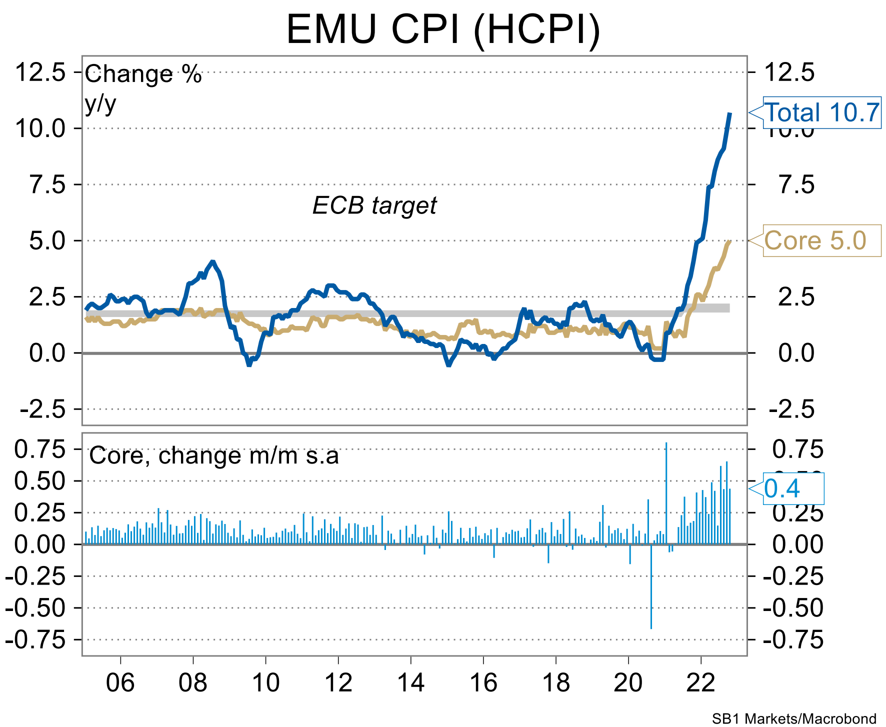


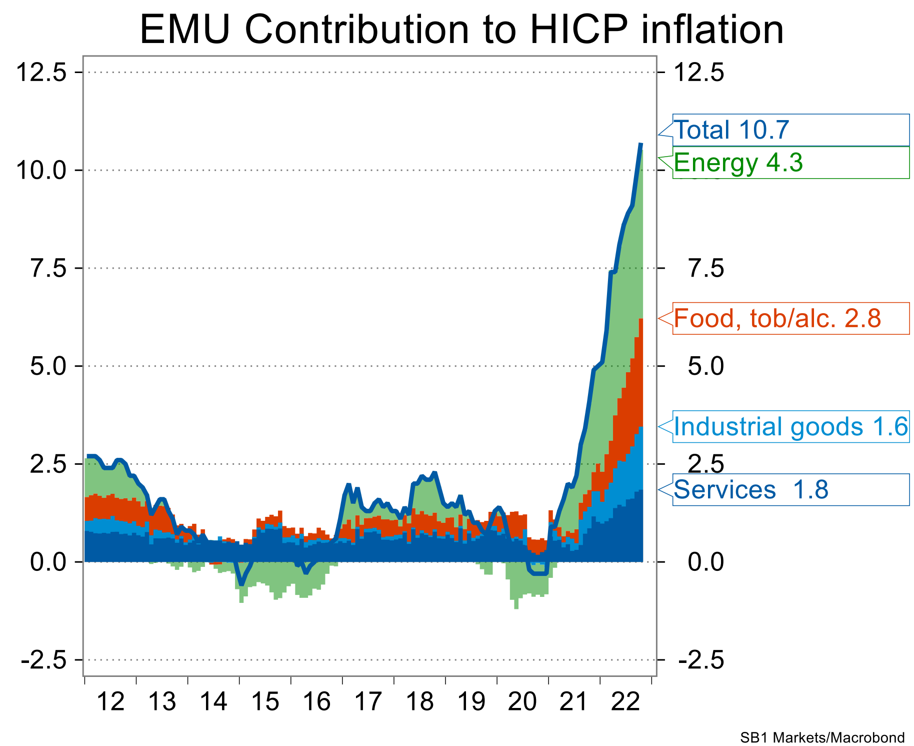


- GDP grew 0.2% in Q3 (not annualised), expected 0.1% - and is up 2.1% y/y and 2.1% above the Q4-19 level
- Italian GDP grew rapidly in Q3, up 0.5%, expected +0.3%
- German GDP was up 0.3% (not annualised), expected -0.3%; France + 0,2%, as expected; and Spain +0.2%, below the expected 0.3%
- *Details will follow in a fortnight*

Inflation higher than expected in October too, as headline inflation hits 10.7%

Core inflation up 0.2 pp to 5% y/y, expected unch.

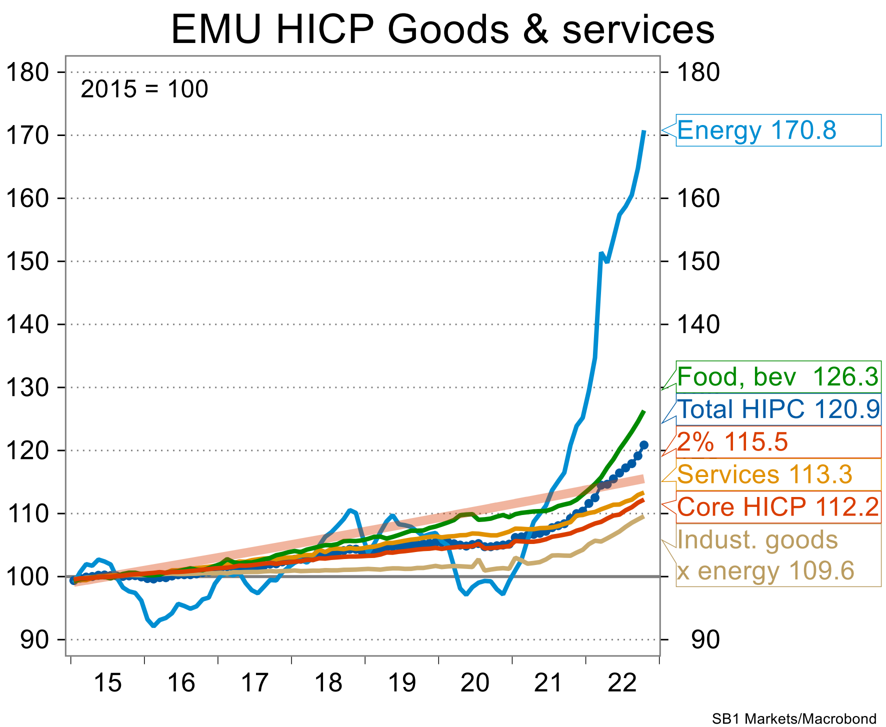


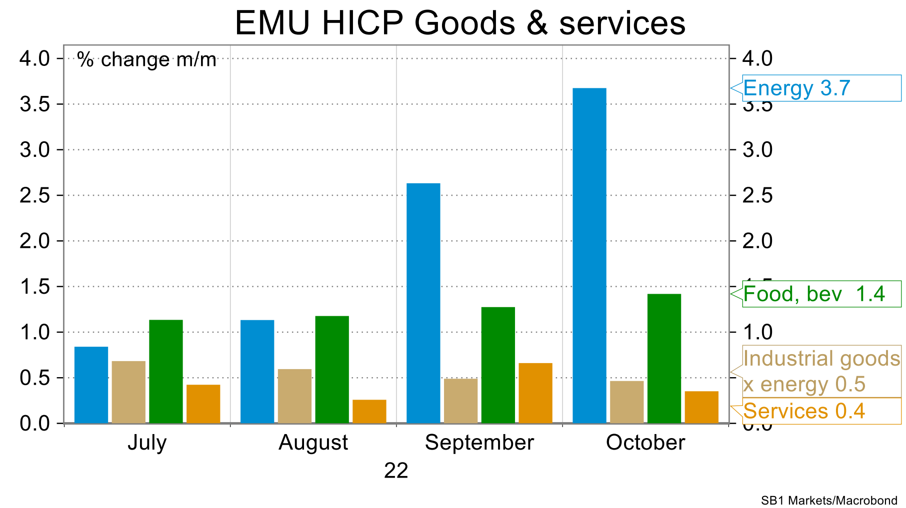


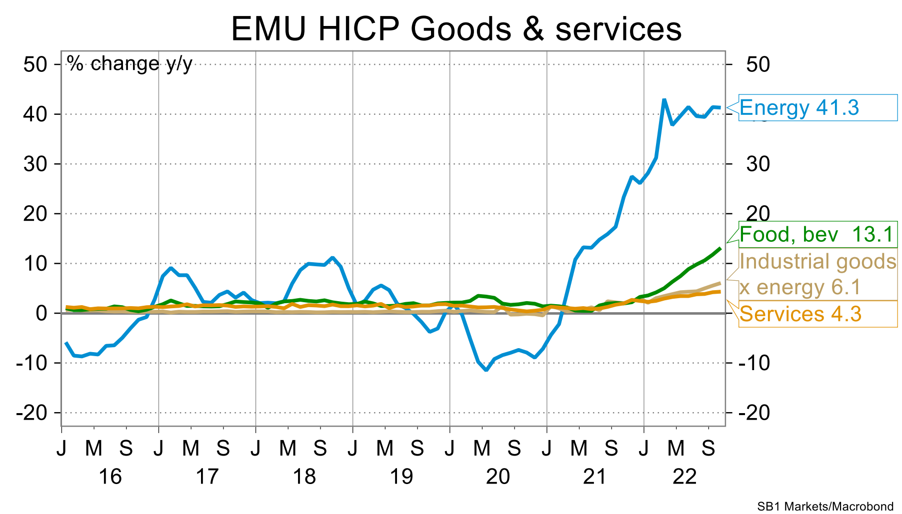
- The **total HICP** rose 1.4% m/m in Oct (seas adj), and 10.7% y/y, which was 0.5 pp above expectations (however, national data that came out Friday the previous week revealed that the forecast was far too low)
  - » Energy prices rose 3.7% m/m, they are up 41% y/y (unch.), and contribute by 4.3 pp to the headline rate. Food prices rose 1.4% m/m - and the latter is up 13% y/y, contributing 2.8 pp to overall CPI growth
- **The core** rose 0.4% m/m. Both goods and services contributed. The annual rate accelerated 0.2 pp to 5%, the highest ever, again…
- The **ECB** hiked rates by 75 bps last week and reiterated that their job is to control inflation. However, the bank’s statement with regards to further hikes was softer, and they can afford to be – 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. So far, they have not succeeded

Energy prices rose 3.7% in Sept, and food prices added another 1.4%!

Energy prices are now up 41% y/y – we thought we would see a slower pace already…



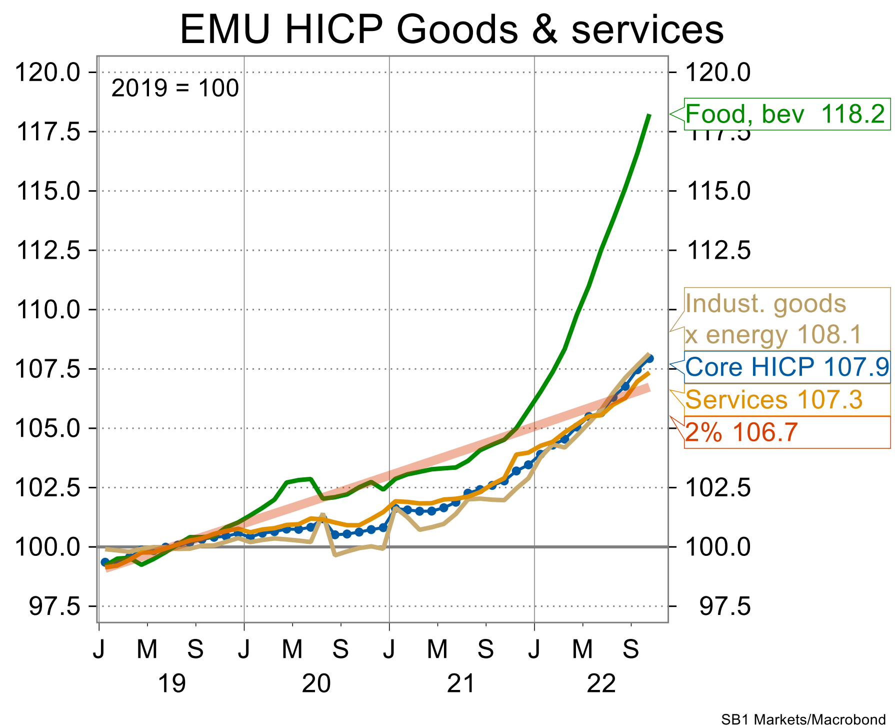


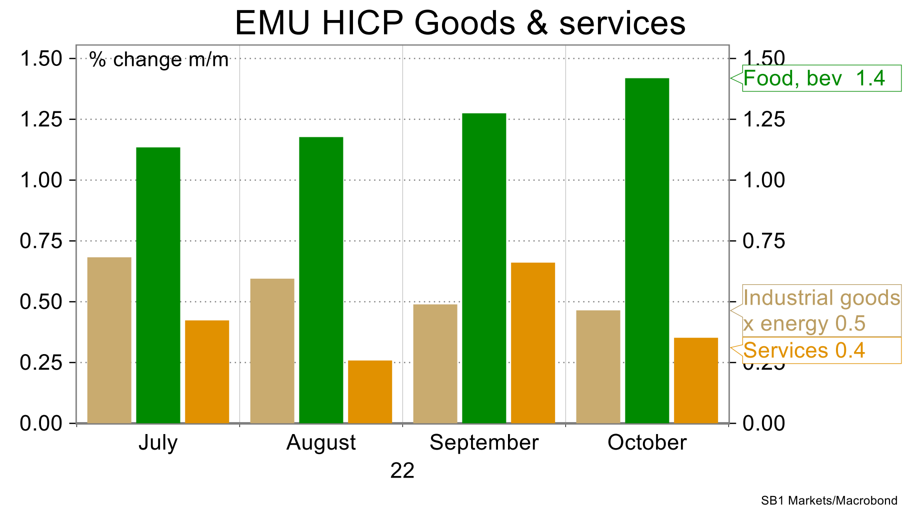


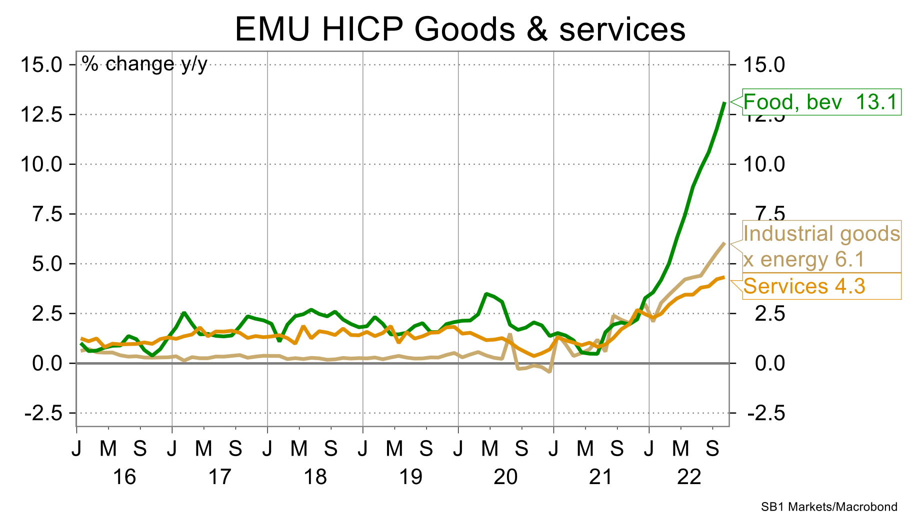
- Food prices rose 1.4% in Oct, more or less in line with price hikes recent months – and they are up 13.1% y/y
- Gas prices have fallen sharply recently and will bring energy prices down. We hope…

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

Food inflation at 13%, industrial goods x energy at 6.1%, and services 4.3%. The target? 2%...



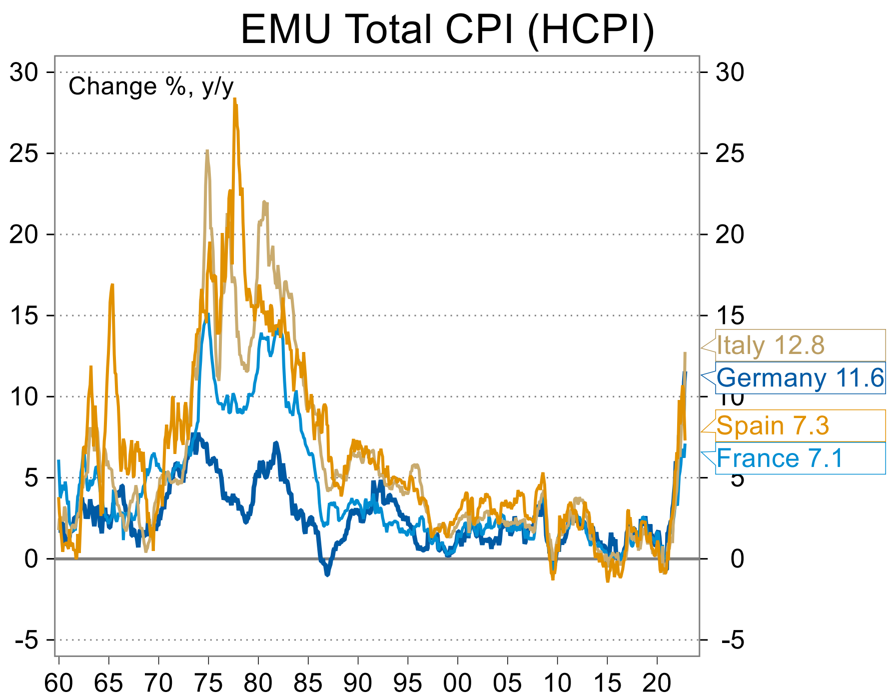


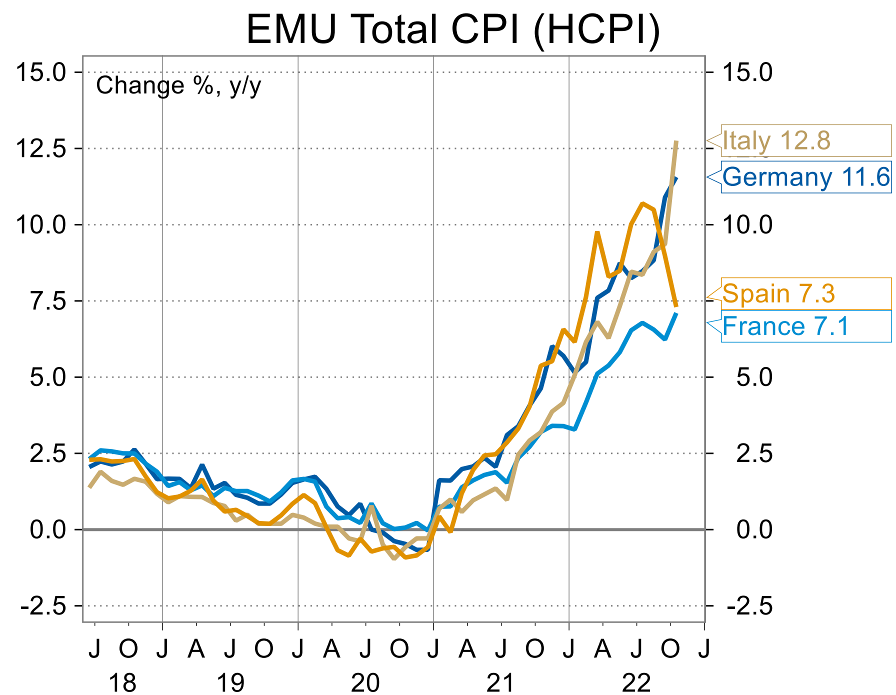


- **Industrial goods** prices increased 0.5% in Oct, and are up 6.1% y/y. And now, these prices are <u>well above a 2% path since 2019</u>
- **Services prices** gained 0.4% in Oct, and these prices are also above a 2% path vs the 2019 level – they are up 4.3% y/y. Transport and hotels/restaurants have contributed on the upside last year
- (No further details in the preliminary HICP report)

Inflation is high across the union

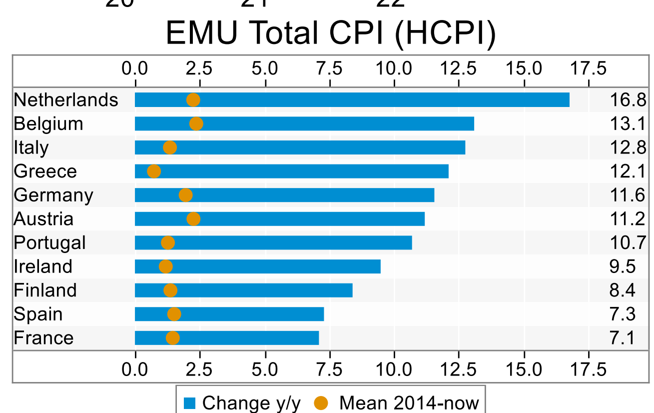
But the inflation in France and Spain are down from the peak





SB1 Markets/Macrobond

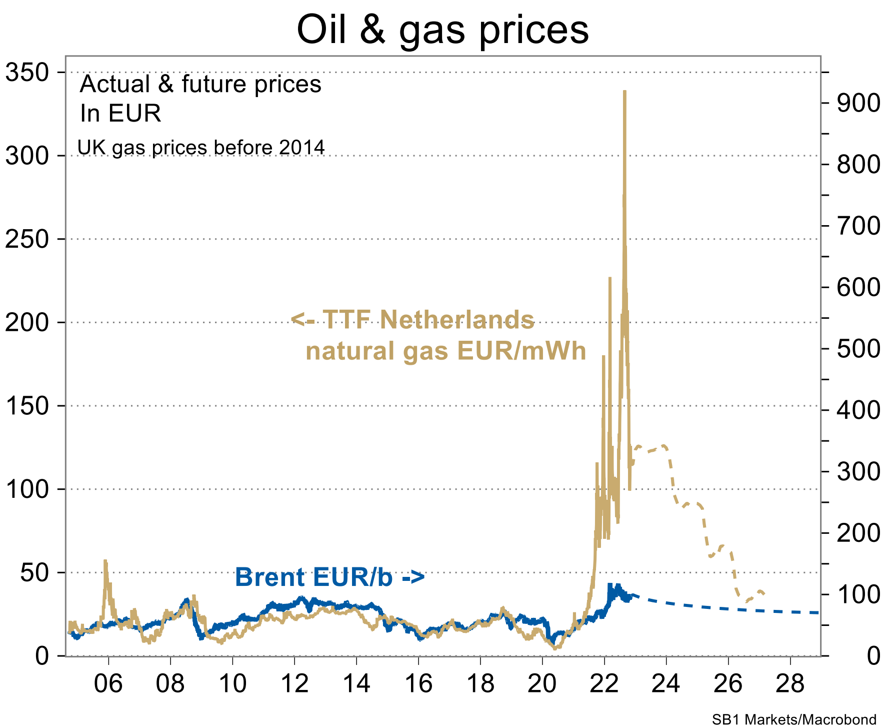
- In fact, the Spanish CPI (HICP) fell m/m and surprised on the downside in October, as in September, but in the remaining 3 of the big 4 inflation surprised on the upside
  - » In Spain and France lower energy prices have lower/stabilised CPI inflation
- In Germany, CPI rose 1.1% m/m, twice as much as expected for the 2nd month in a row, bringing the y/y rate to 11.6% - the highest since 1949 – and then back to the early 1920s, during the Weimar Republic

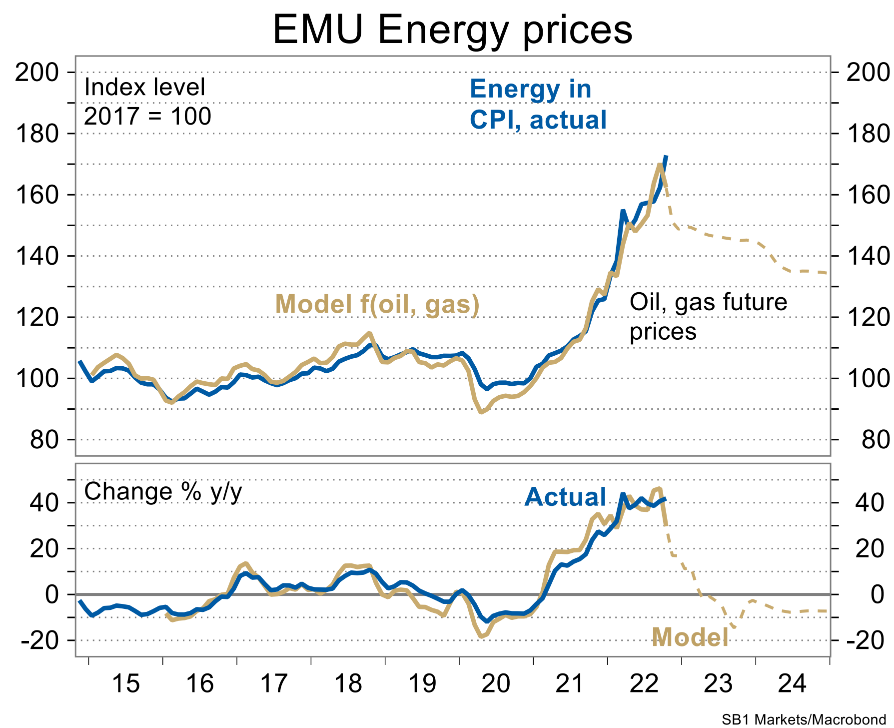


SpareBank 1 MARKETS

Gas, oil prices have lifted 'energy CPI inflation' up to 41% but….

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

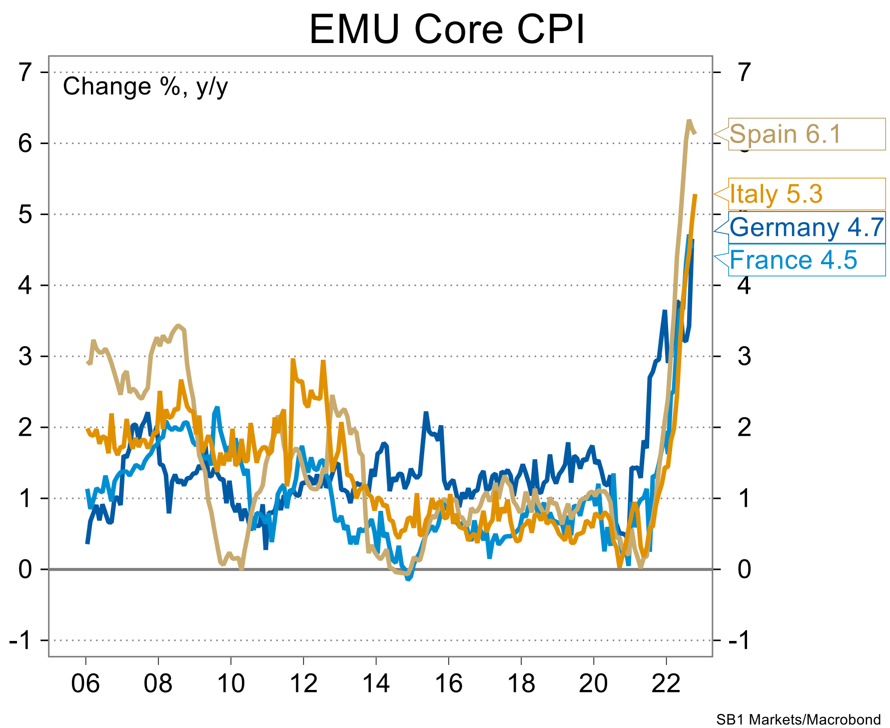


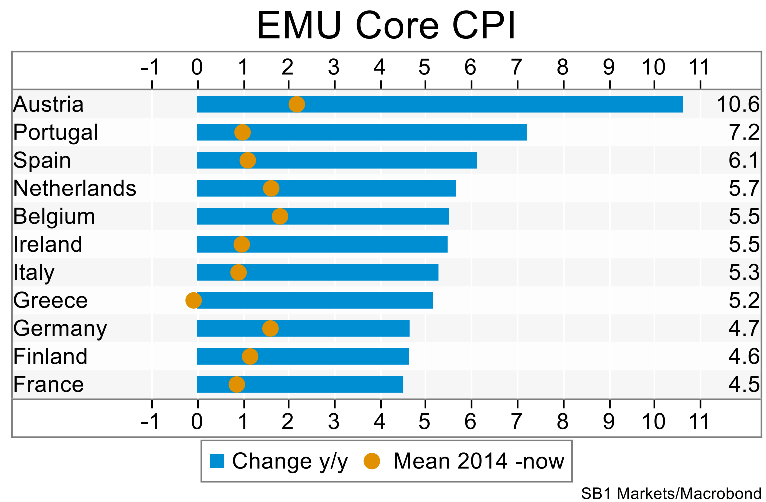


- Gas prices have fallen sharply past two months, both in the short and the long end of the price curve
- Early next year, energy prices will be down, measured y/y – even after the current surge.
  If the market got it right this time …

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

…putting further pressure on the ECB

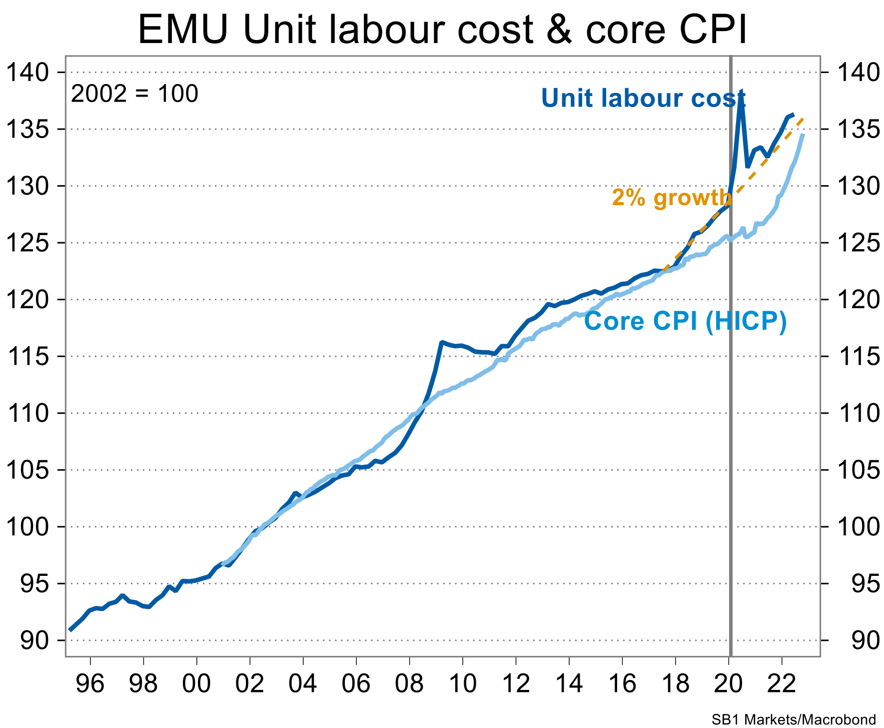




- On this page: The last obs. is partly Sept, partly Oct

Unit labour cost inflation suggests limited risk to inflation, over time

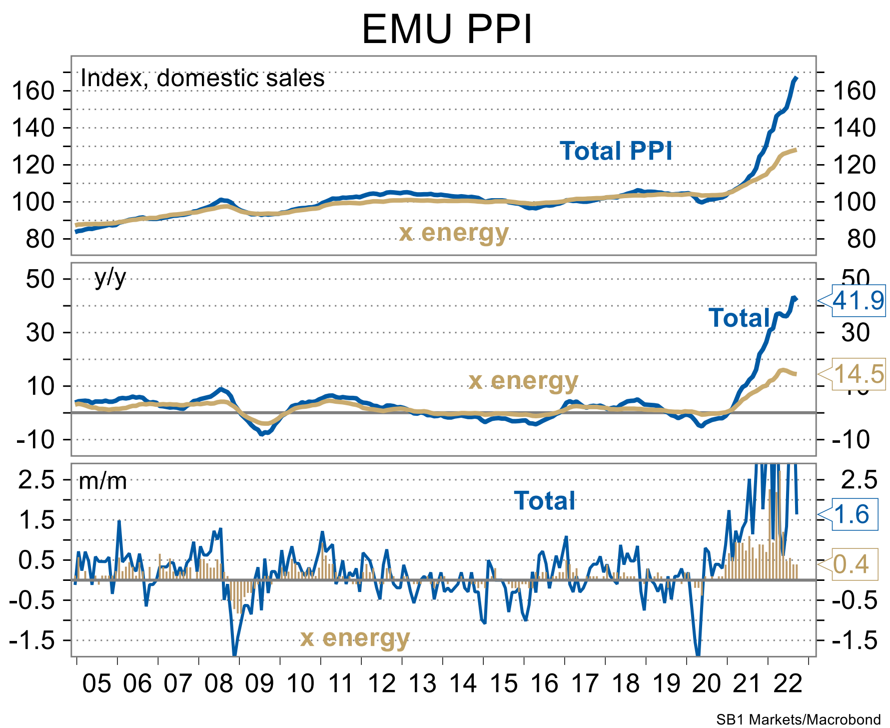
Wage inflations is moderate, and ULC is up at a pace just marginally above 2%

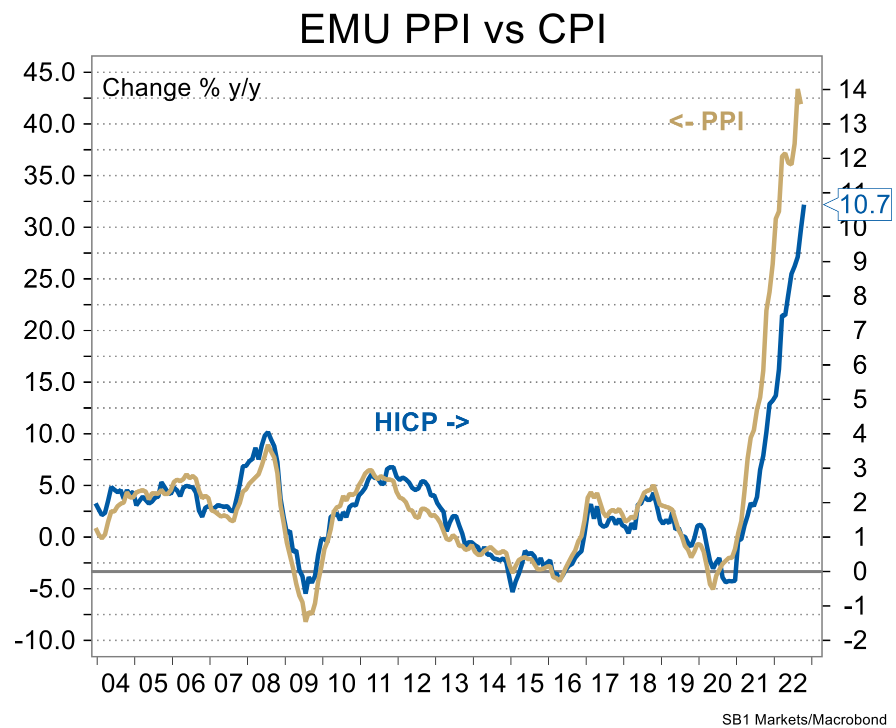


- **Unit labour cost** (labour cost per unit produced = wage cost/production volume, growth in UCL= wage growth – productivity growth) has jumped up during the pandemic as productivity fell because employment was not cut (as in the US)
- On the other hand, in the 3 years before the pandemic – and through the pandemic so far – ULC has accelerated to 2% from 1%. The 1% growth in unit cost corresponded to the long term growth in core rate of inflation at 1%, well below ECB's 2% target – and a 2% ULC inflation will over time yield a 2% CPI inflation

Producer prices keep rising, but PPI x energy has peaked

The total PPI rose 1.6% m/m in September, the core index added 0.4%

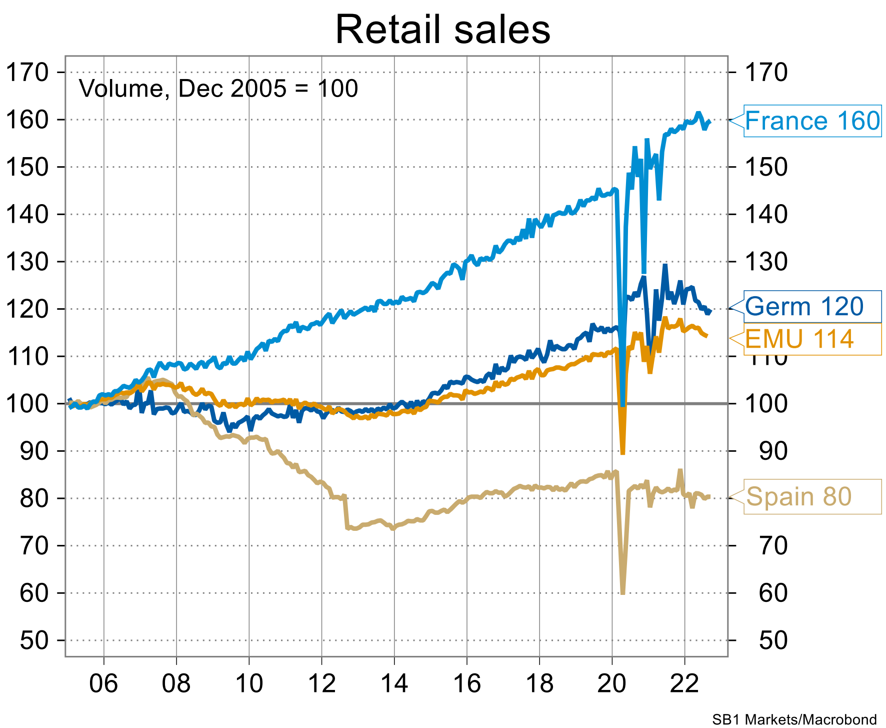


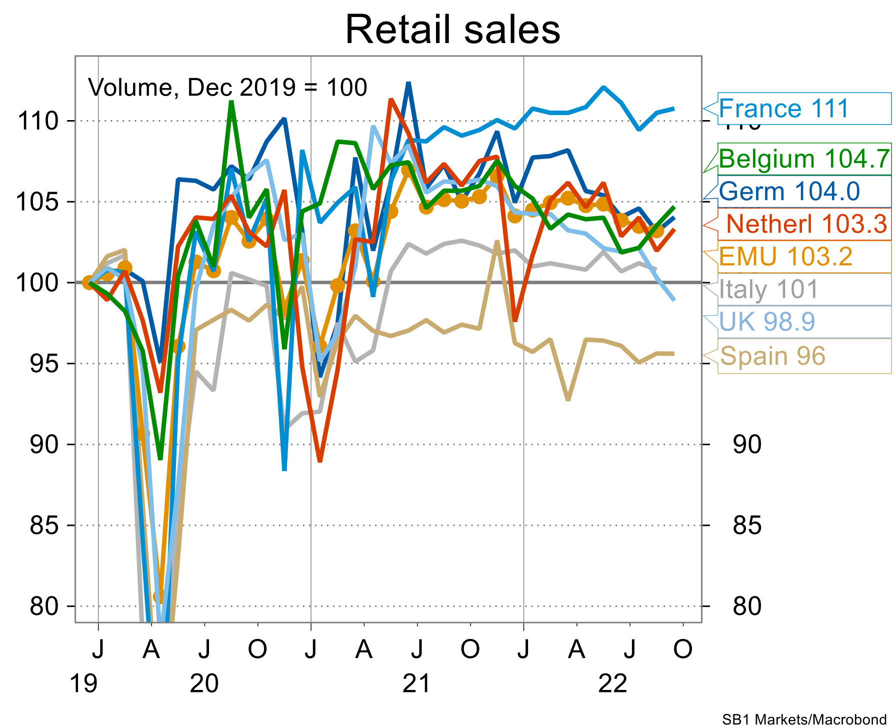


- PPI was up 42% y/y, all included, and 14.5% x energy
- No guarantee that energy prices cannot rise from here come winter-time, even if future prices have fallen sharply recent weeks but the core is very likely coming down

Retail sales surprised on the upside in September, Germany up 0.9% m/m

…expected -0.3%. France reported growth as well, Spain was flat – and Italy has not yet reported

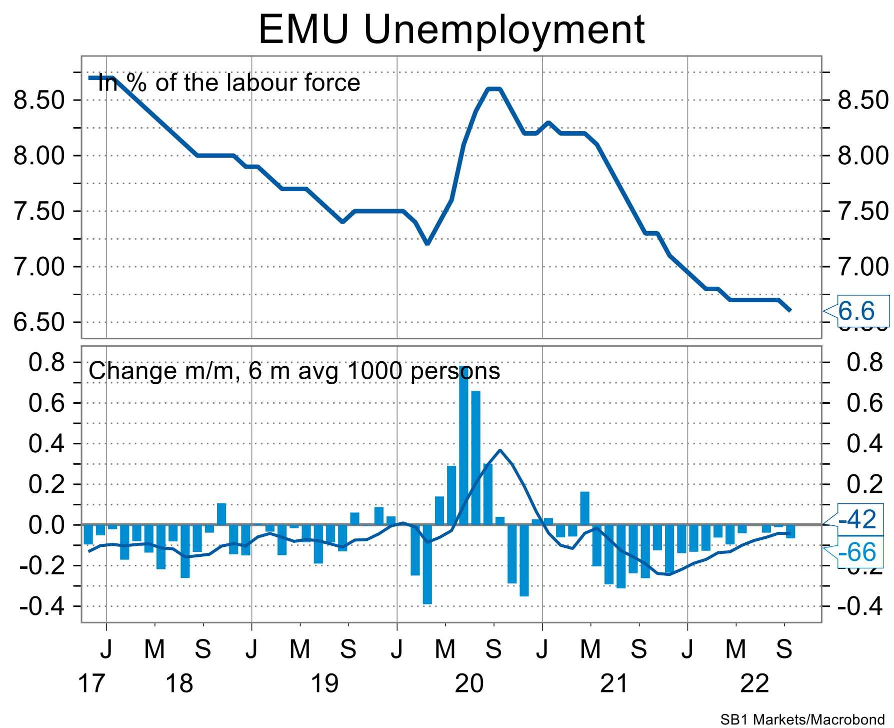


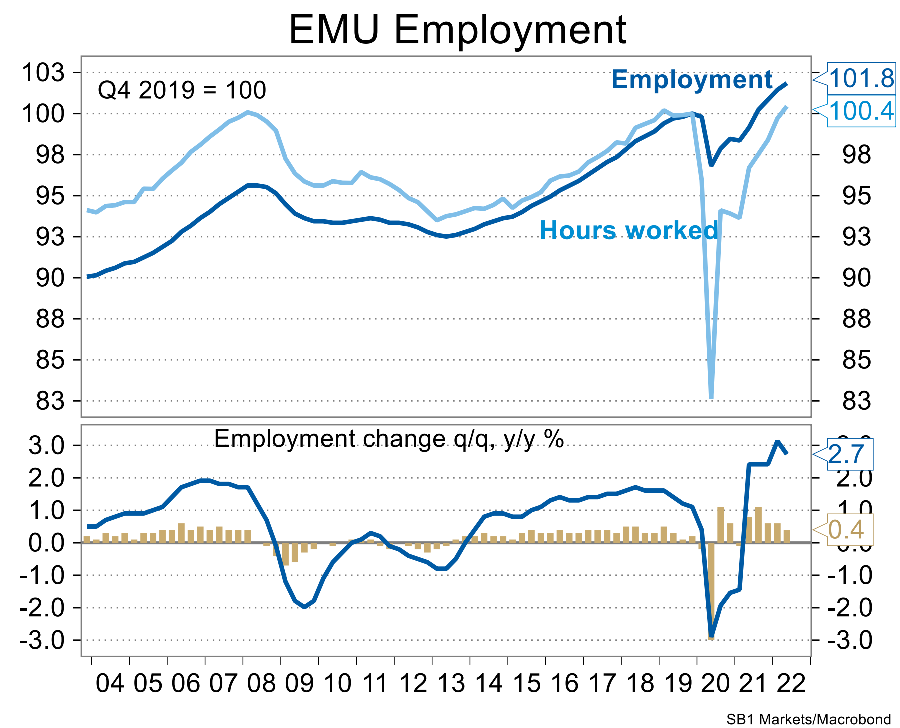


- Sales in the EMU is expected up 0.4% in September, data out today – a reasonable estimate
- Sales are above the pre-pandemic level in most of the EMU – with Spain as an exception (and Italy was not far above in August)

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

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



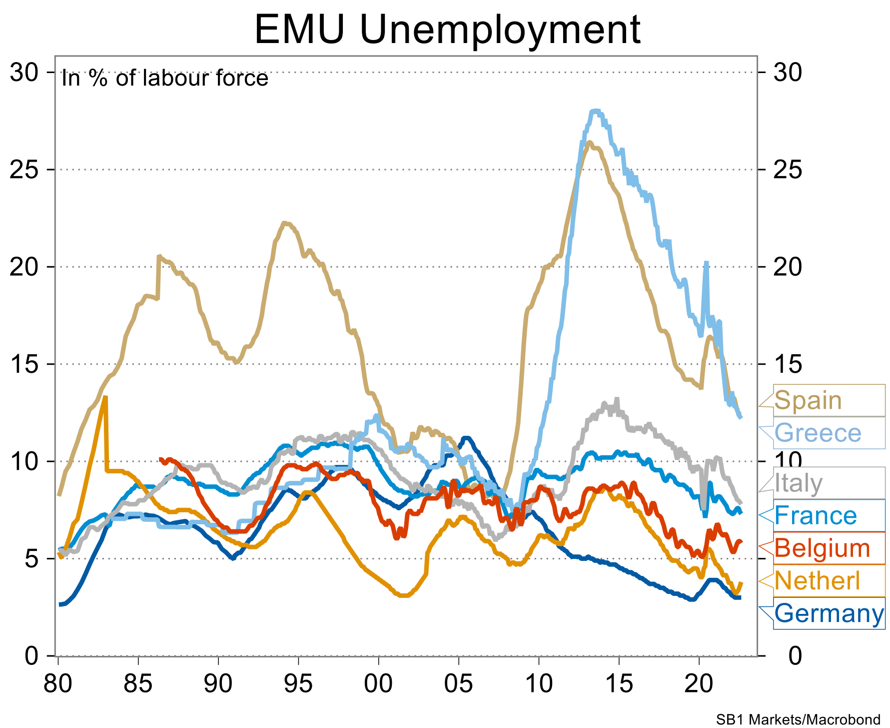


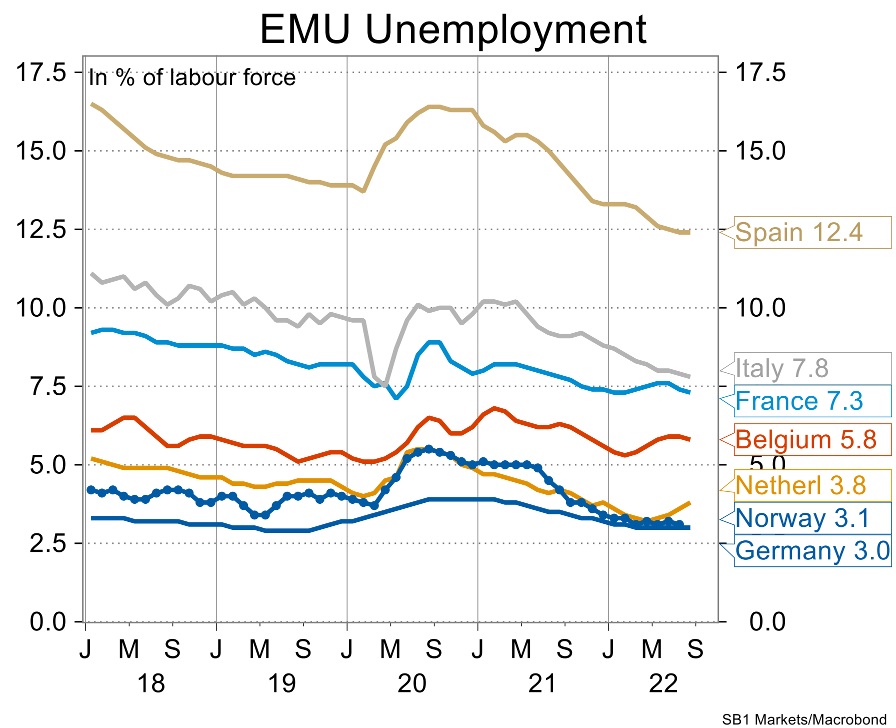
- **The number or unemployed** declined further in September
- **Employment** grew by 0.4% in Q2 (not annualised), and hours worked grew too
  - » The employment level & the employment rate is higher than before the pandemic
- The number of **unfilled vacancies** soared to the highest level ever in Q2, 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%

SpareBank 1 MARKETS

Unemployment is lower than average everywhere

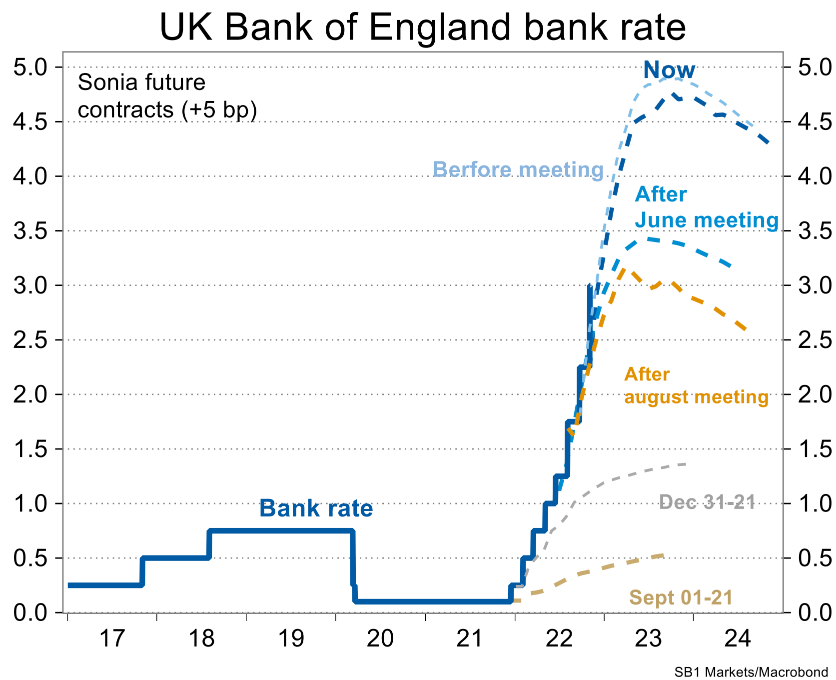
Belgium has been marginally on the way up – and now the Netherlands has followed suit





Bank of England raises rates by 75 bps - largest hike since 1989

…and forecasts a longer recession



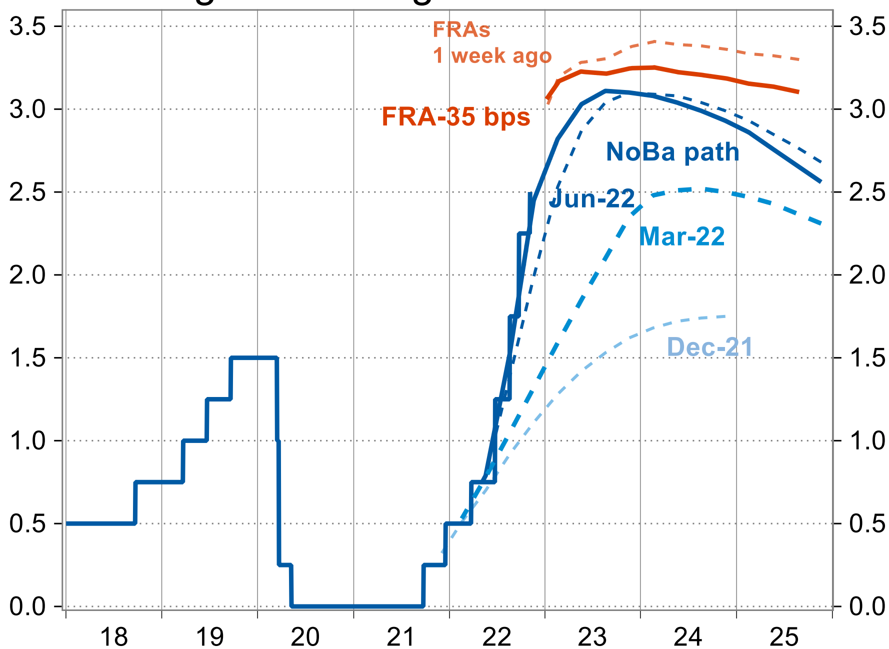
- **The policy rate** was lifted by 75 bps to 3%, as widely expected
  - » 7 of 9 members voted for a 75 bp hike, while 1 member preferred a 50 bp hike, and 1 member voted for 25 bps
  - » The Bank was clearly front loading rate hikes in order to prevent it from risking an extended tightening later
  - » In its statement, the bank projects a contraction in GDP for 5 - 8 quarters, depending on the terminal rate (3% vs. 5.25%), but signalled that the bulk of the rate hikes is behind us, but that some further increases are needed to bring inflation back to the target of 2%. However, the governor stated that the projected terminal rate is closer to today's rate than the peak markets predictions in Oct.
  - » Peak inflation is now expected at 11% in Q4 this year, which is down from 13% in the last MPR due to the Energy Price Guarantee. Unemployment is forecasted to reach just under 6.5% (from the current 3.5%) and that there will be a negative output gap of 3%

- The **short end of the UK curve** kept sliding at the bank stated that most of the rate hikes are in the past. Predictions of a prolonged recession, on the other hand, sent the GBP tumbling yet again, and the pound is down 2.6% for the week

Norges Bank raised by 25 bps to 2.50%

The bank is acknowledging that the economy is cooling, and we are yet to see full effect of hikes

Norges Bank signal rate vs market



SB1 Markets/Macrobond

The policy rate was raised by 25 bps to 2.50%, as expected by both us and some half of the economist. The market was also split, but the market response was smaller than we expected

The bank also signaled that **the rate will likely be hiked further** in December (by 25 bps, they said in Sept)

According to the statement and the governor, the underlying data suggests that the rate could have been hiked by more than 25 bps. GDP growth and inflation have surprised at the upside, and unemployment at the downside. However, the bank sees signs of a slowdown in the economy, and it acknowledges that monetary policy works with a lag – the rate is already in restrictive territory.

Given the households debt level, almost entirely floating, the impact could be substantial. In addition, Norway does not have a wage inflation problem and the risk of overreaching is clearly present – in other words: the bank can afford to wait and see

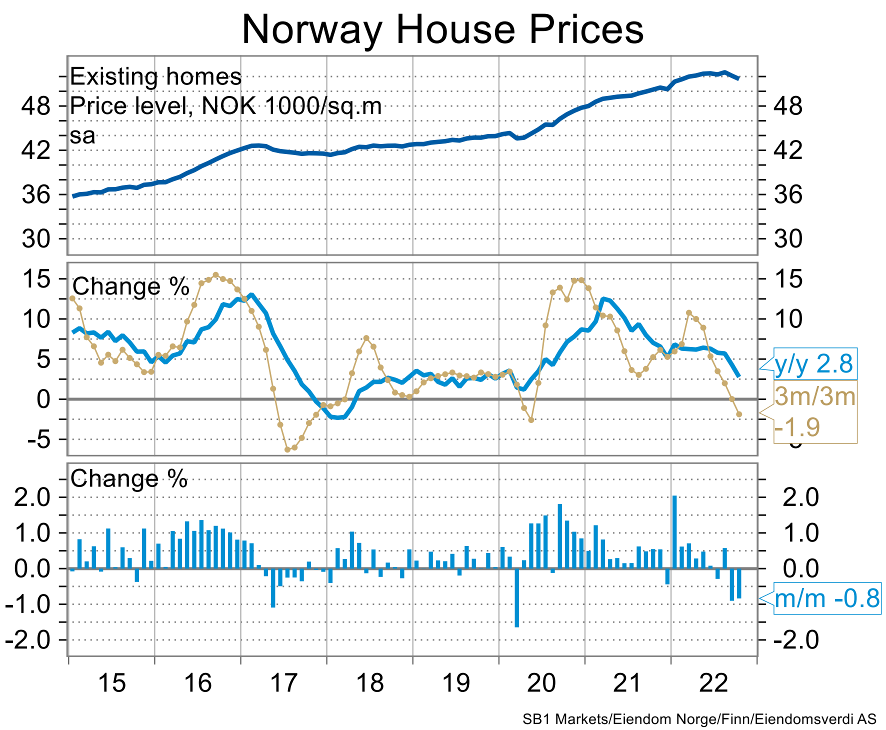
Market reaction

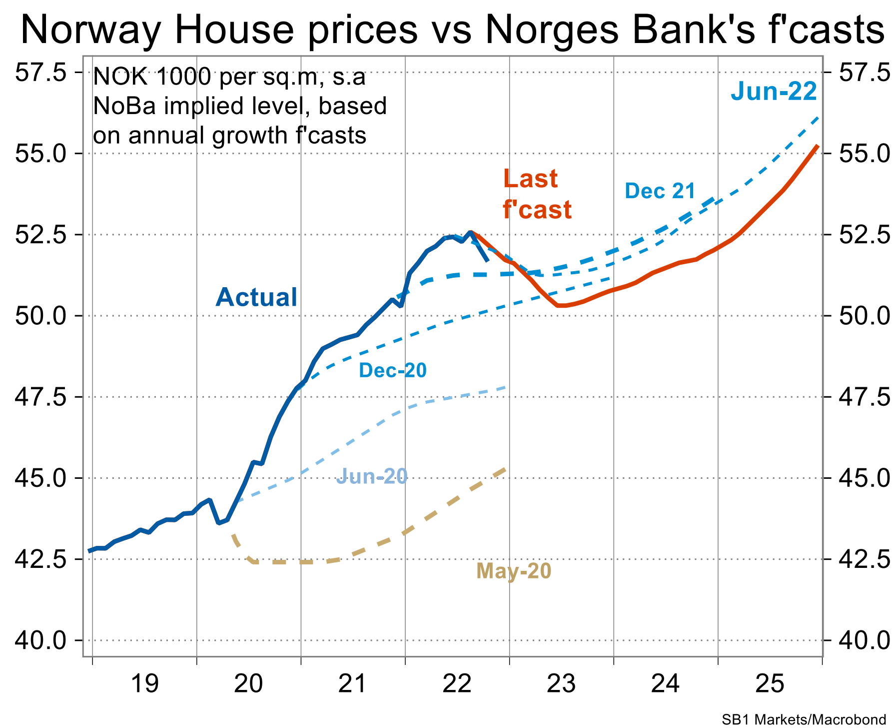
» The **Dec-3 FRA** fell 4 bps, but rest of the curve rose. The Dec-3 FRA at 3.53% is far to high if NoBa hikes by just 25 bps or even 50 bps in December.
  - However, the NIBOR spread has very likely widened substantially, the 3 m NIBOR is at 3.40%, implying NIBOR spreads at 76 bps if NoBa hikes by 25 bps in December, and 62 bps if NoBa hike by 50 bps in Dec! The 'normal spread is some 40 bps in (35 bps + the normal Q4 liquidity year end premium at 5 bps)

» The **NOK** depreciated 1% just after the announcement, but has strengthened thereafter, no doubt supported by a higher oil price

Winter is coming, house prices down 0.8% in Oct; Sept print revised down

Prices are falling faster than NoBa assumed, almost ½ of the assumed decline already executed

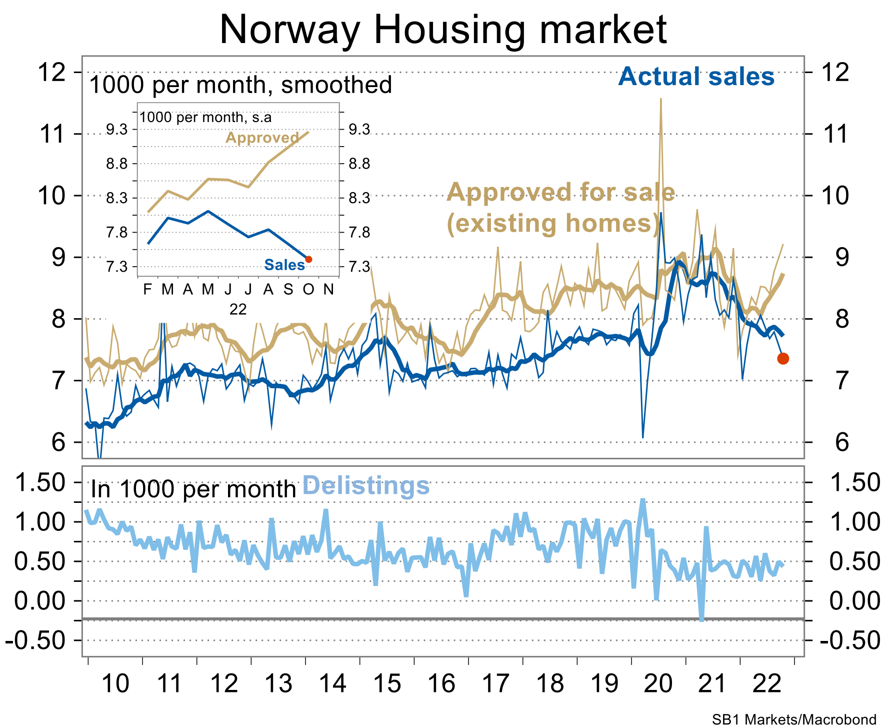


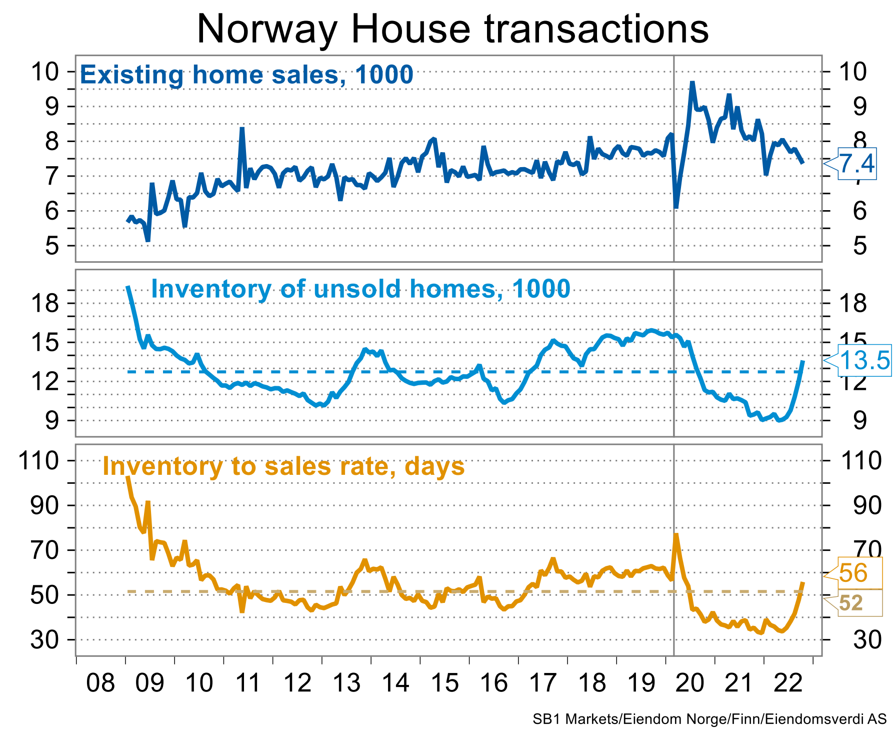


- **House prices** declined 0.8% in October, we thought even 2% was likely (which was close to the 1.9% drop in Oslo). September was revised down by 0.3 to -0.9%. Barring the price fall at the start of the pandemic, we have to go back to 2017 to find a greater fall in prices. Norges Bank expected a 0.4% decline. Prices are now down 1.9% measured 3m/3m – but are still up 2.8% y/y. Prices fell in 11 of 16 cities, and the most in Oslo. Underlying (3/3m) are up in 3 cities, down in 13
- **Existing home transactions** fell further, to 7.6' which is 15% below the peak during the pandemic but still just back to the average 2019 level. However, no. of **homes approved for sale** rose further, and is clearly above a normal level.
- **The inventory of unsold homes** rose by 1.6' units in September, the steepest increase ever (the two previous months were last ATHs!), to 13.5', which is above avg. Since June, the inventory has shot up twice as fast than anytime before! Still, the time on market for those homes actually sold remains low
- **Norges Bank** expects a 4% price decline from August till next summer. Now prices have declined by 1.7%. The risk is no doubt on the downside

A record rapid pace of inventory accumulation as sales slow rapidly as well

The inventory is increasing twice as fast as ever before, and the inventory is above average

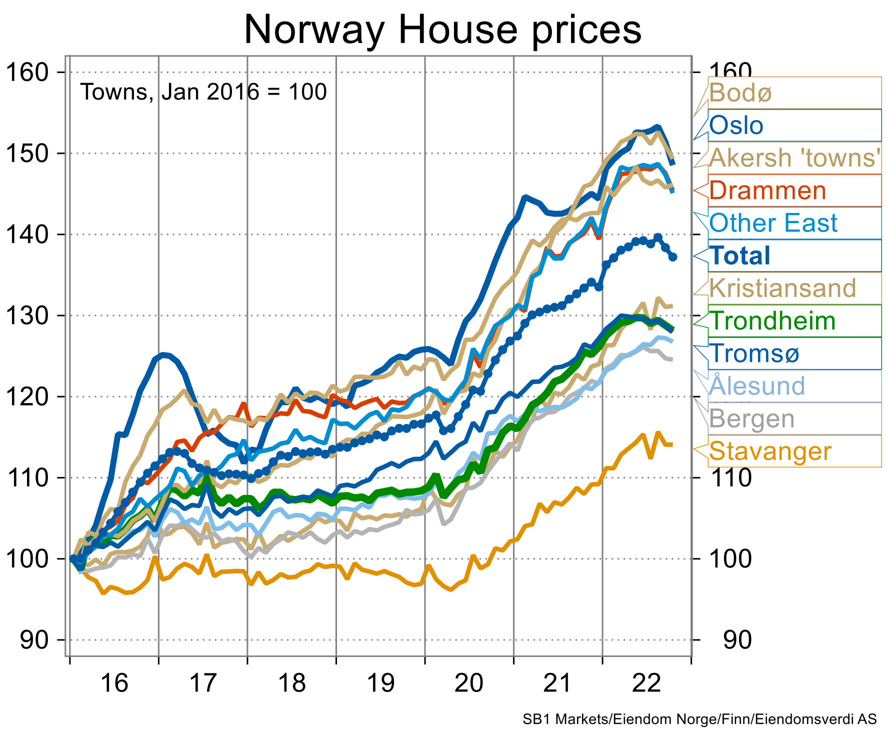


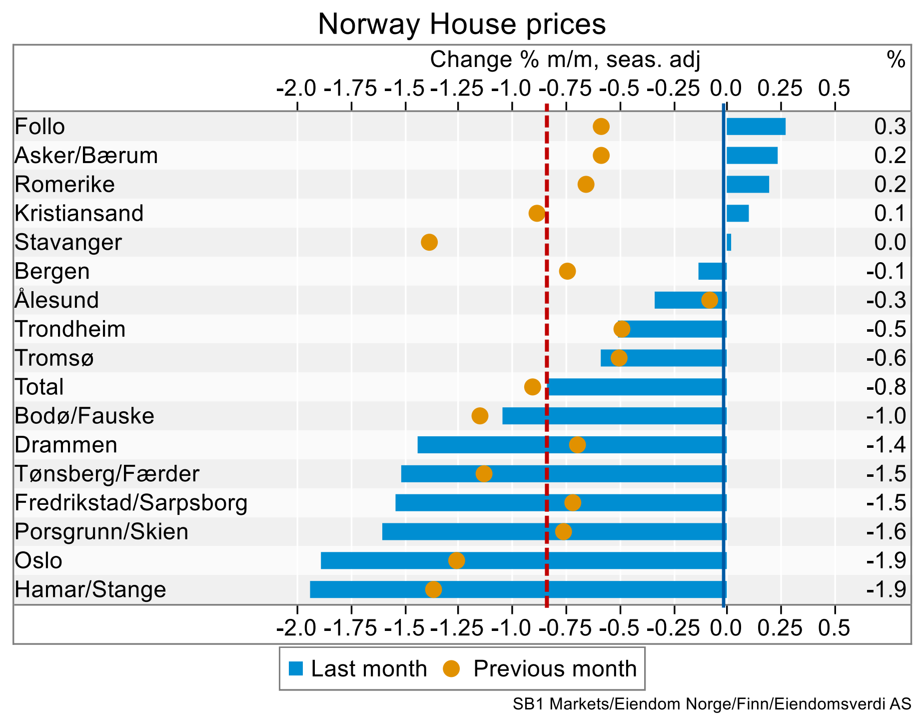


- The **number of transactions** fell in further in October and is now slightly below a normal (2019) level (7.3')
- The **supply of new existing homes for sale (approvals)** rose further and to way above a normal level in October (9.2')
- The **inventory of unsold homes** rose by 1.6', the fastest increase ever (August and September were also ATHs ☺). The lift over the past 4 months is twice as fast as ever seen before, up to 13.5 from 9.1' in June, or almost 50%)
- The **inventory/sales ratio** added 10 days to 56 days, vs an average at 52 days – and the ratio is still not high
- The **time on market** for those homes actually sold was unchanged at 32 days (average 42 days) – so there is not yet any buyer's strike for homes which are 'correctly' priced. However, if all those homes not sold should have been sold, substantial price cuts would very likely have been needed

Prices in Oslo and Hamar fell by 1.9% in October

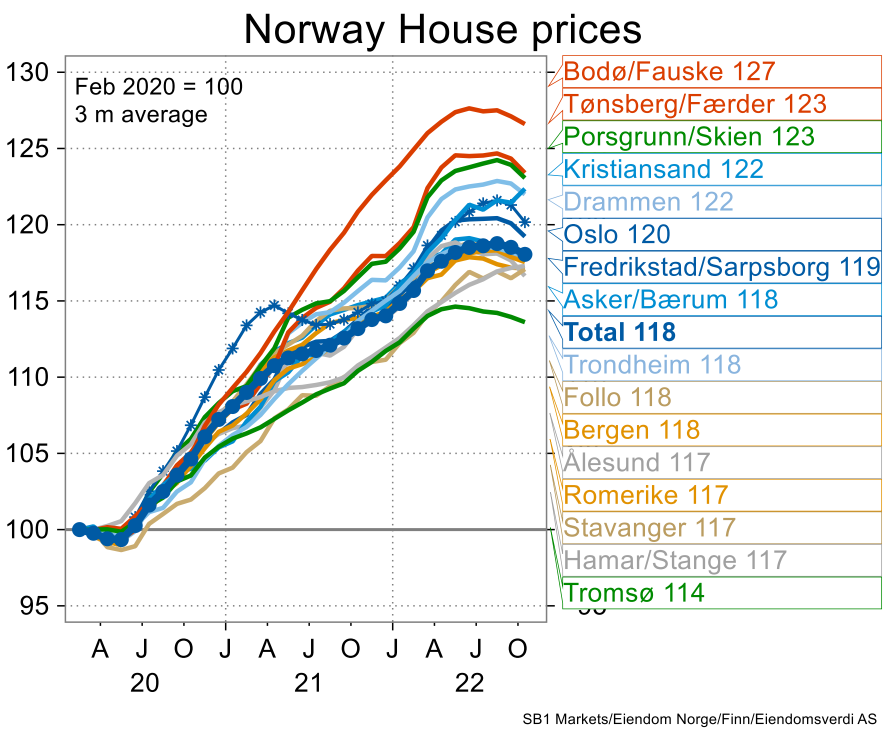
Prices fell in all but 4 cities; Just Follo, Asker/Bærum, Romerike and Kristiansand up

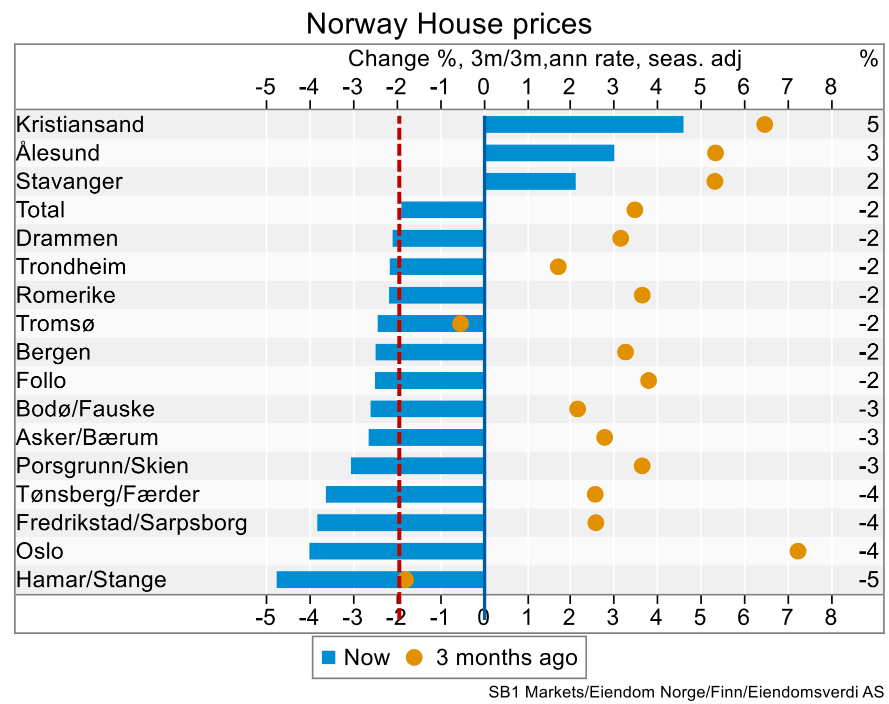




The big picture: Prices are now turning down most places

Prices measured 3m/3m are still up in Kr.sand, Ålesund and Stavanger, but down in 11 of 16 cities

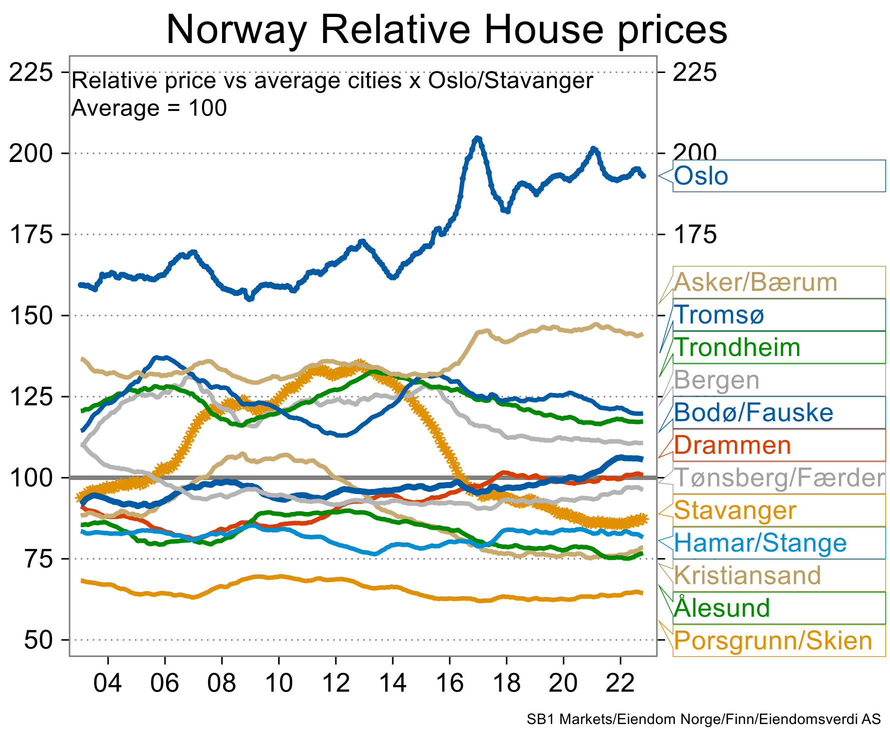


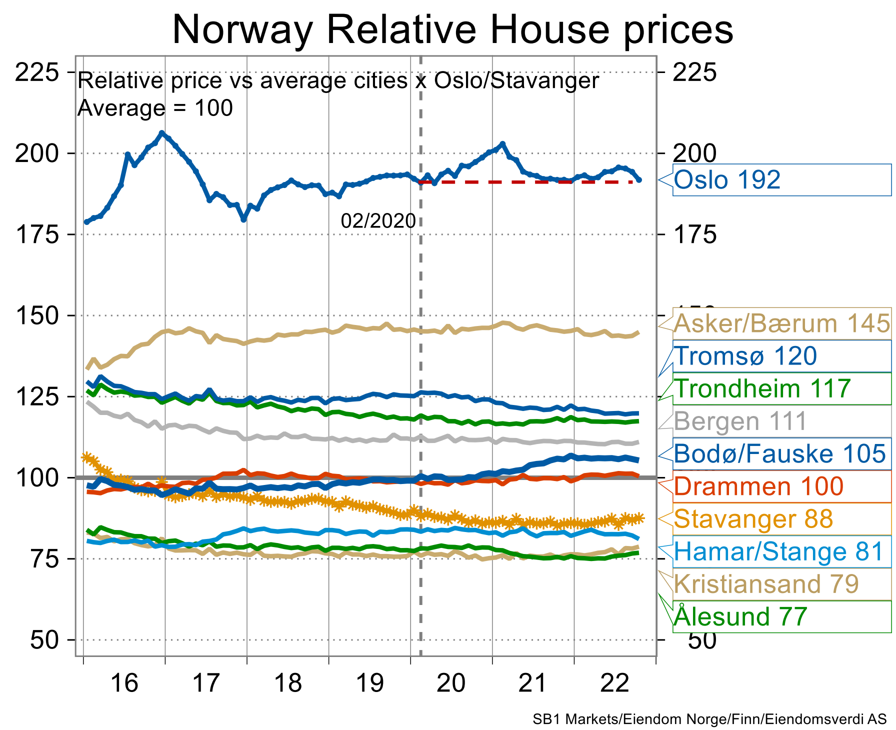


- Bodø the winner through the pandemic (and since 2016). Recent months, prices in Bodø have been falling but now Oslo is speeding up too
- After Bodø, south-eastern towns have been the winners since early 2020; Tønsberg, Porsgunn/Skien, Drammen, Oslo, and Fredrikstad/Sarpsborg. Prices are now seem to have turned most places
- Tromsø, Hamar, Stavanger, and Romerike are at the bottom of the list (vs. early 2020)
- Now: Prices are falling most places, even smoothed 3m/3m. 13 ‘cities’ are down, while just 3 still are up measured 3m/3m. 3 months ago, just 2 cites were reporting underlying decline in prices

Oslo relative prices back to the pre-pandemic level

Stavanger has been slowly recovering, as have Kristiansand and Ålesund, vs the rest of the pack

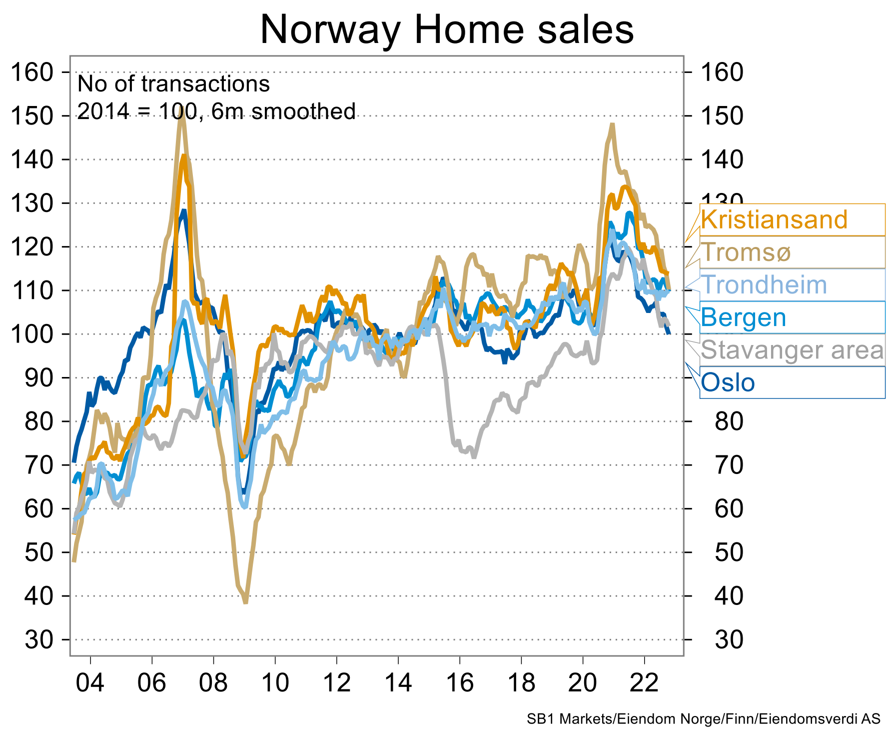


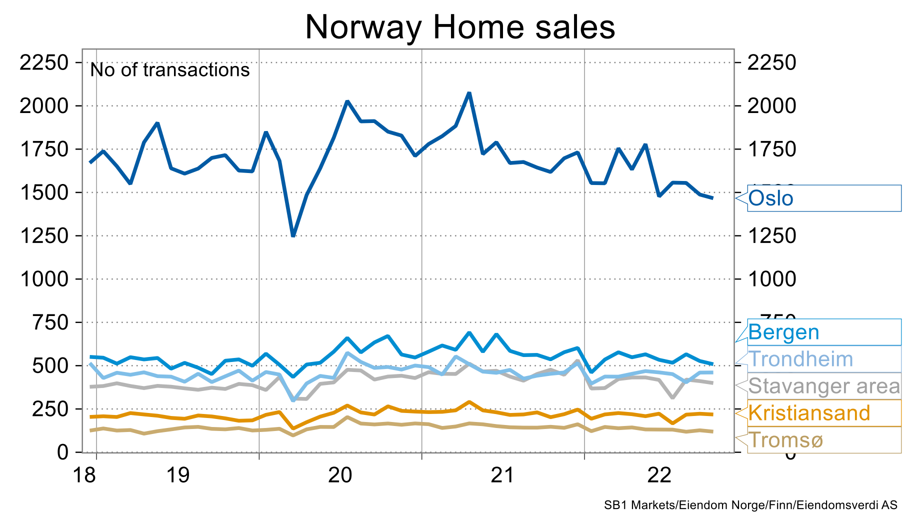


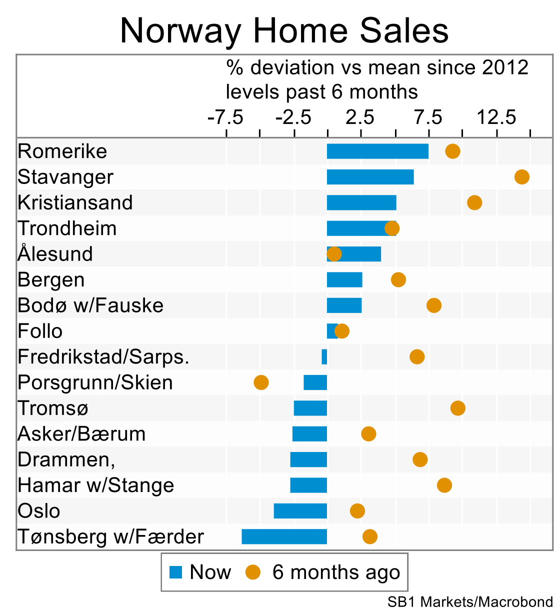
- **Housing starts** in Stavanger/Rogaland are still not lower than normal. It is still profitable to build, even at 'Hamar/Stange' prices! And why shouldn't it, land prices are far from zero!

Sales are declining everywhere, all are well down from the recent peak

… and sales in almost half of the cities have fallen below the 10 y average

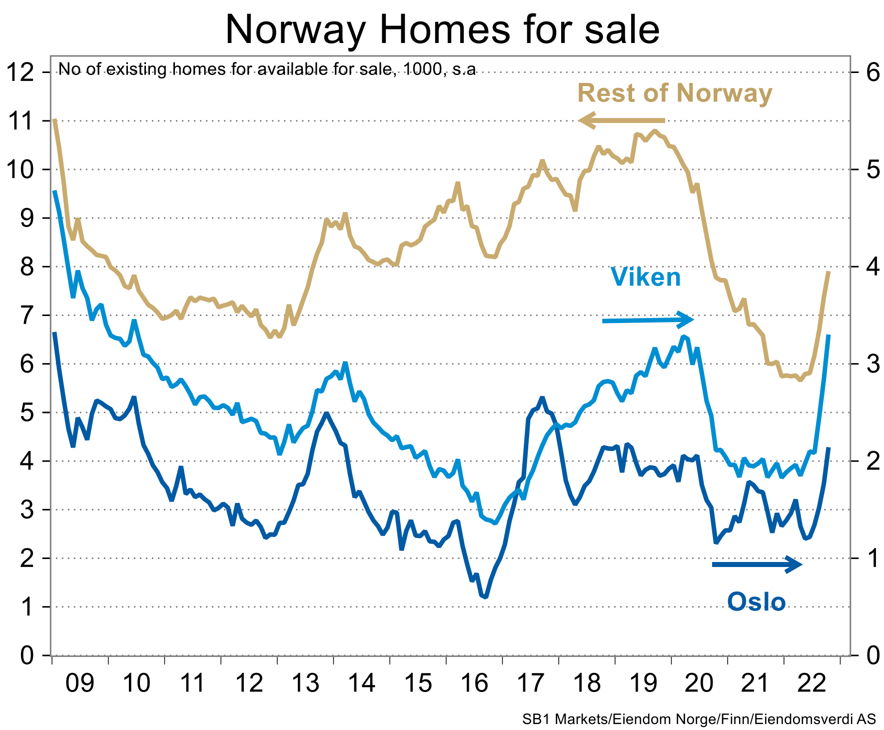


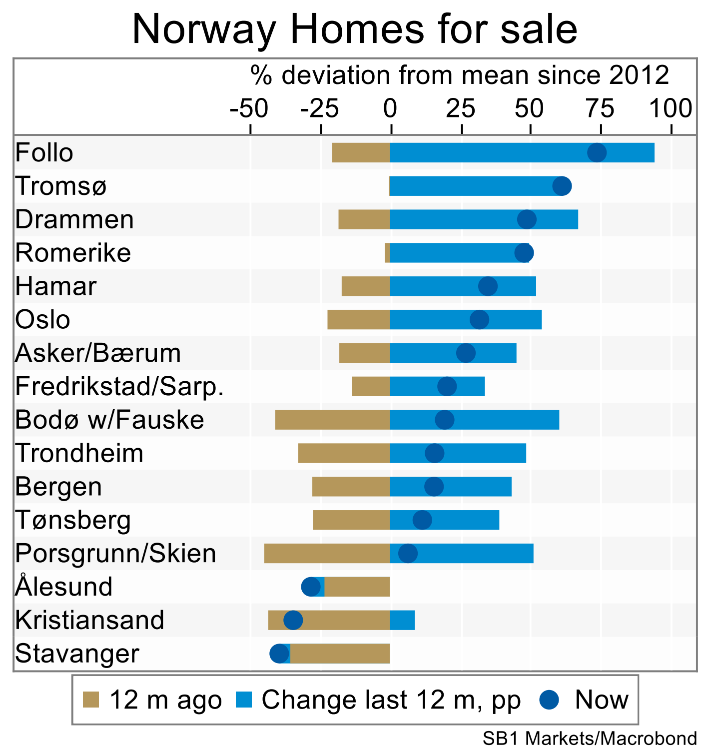




The inventory on the way up everywhere, and the fastest ever most places

14 of 16 cities reported higher inventories y/y, 14 cities above the 10 y average, 3 below

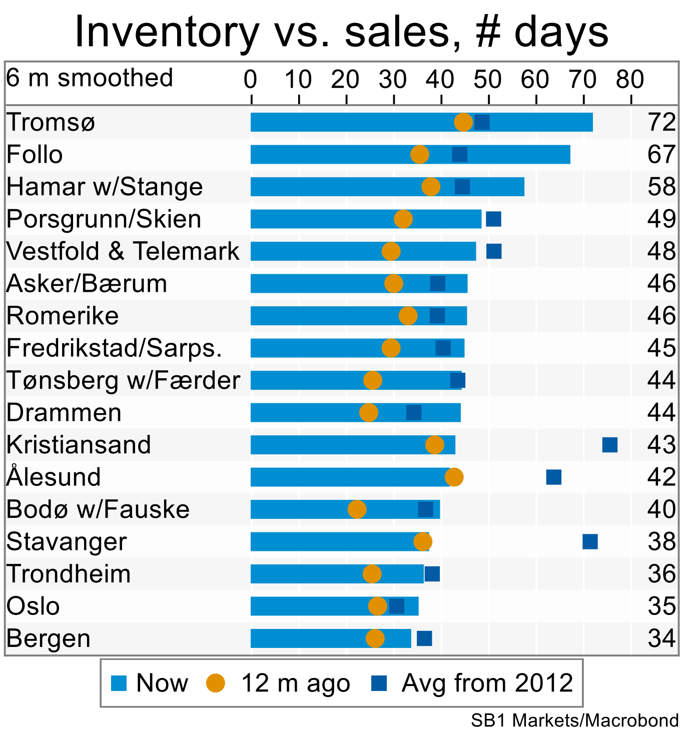




- Follo is reporting the largest increase over the past year, and the inventory is 75% above the average since 2012! Tromsø no 2 on the list. Viken in total is at the highest level since 2010!
- The inventory in Oslo is also well above a normal level – but far from record high
- The inventory has increased the fastest pace past 4 months in Bergen (+85%) Drammen (84%), Oslo (76%), and all are well above normal levels

The inventory is turned around slower than normal many places

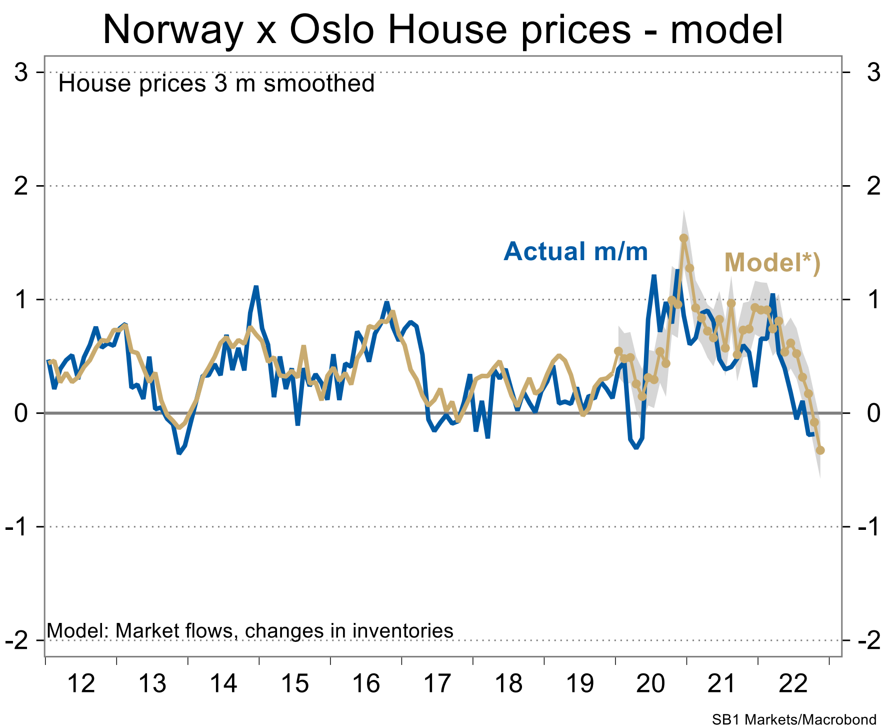
9 cities are reporting higher i/s-ratios than normal, 7 cities report lower i/s-ratios

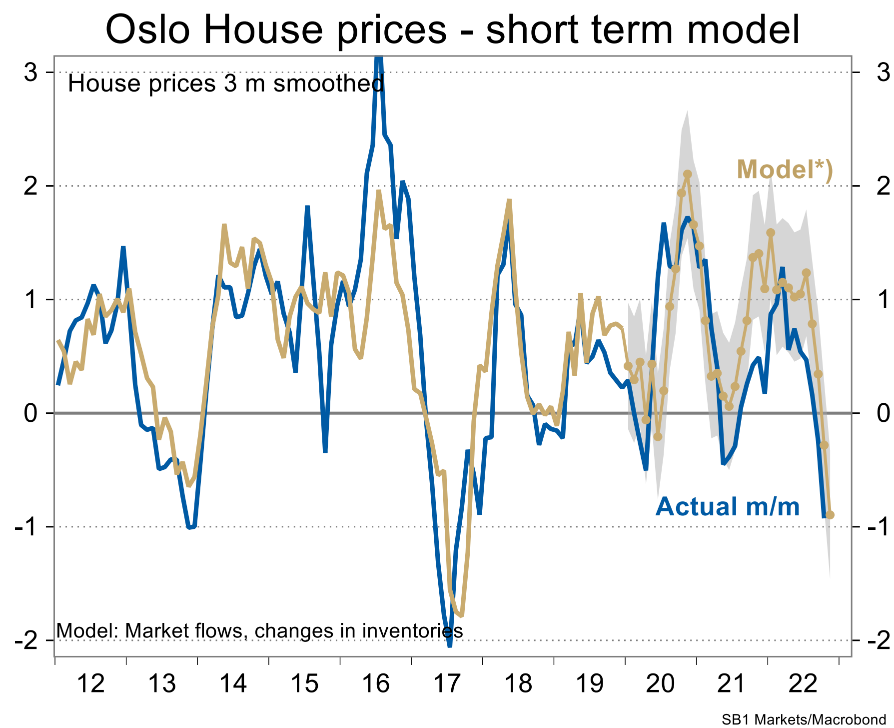


- The i/s ratio is higher than one year ago in 15 cites, flat in 1
- The i/s ratio is far above average levels in Tromsø, Follo and Hamar

Short term market flows suggest continued price fall, especially in Oslo

Higher mortgage rate will also contribute to a slowdown coming months

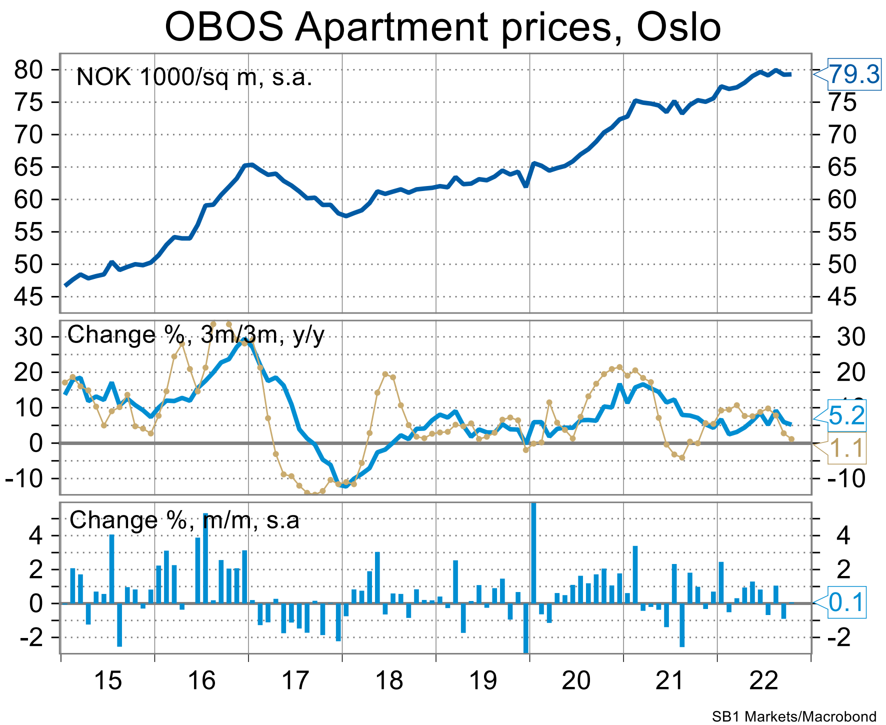


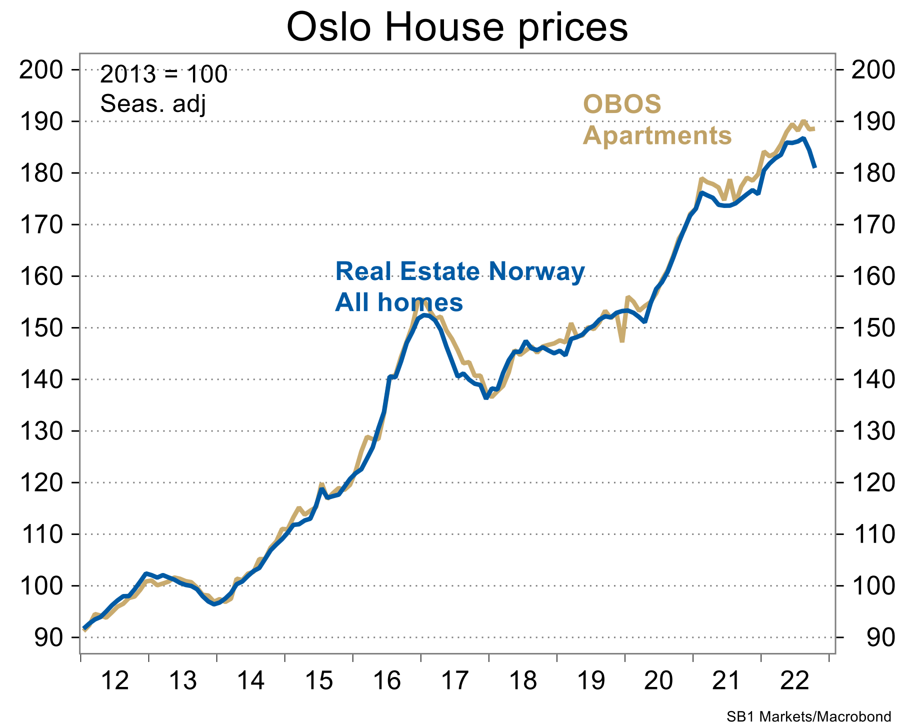


- Our **national x Oslo model** based on flows and the inventory signals a 0.3 fall in house prices (in comparison, prices in Norway x Oslo fell by 0.5% in October)
- Our **Oslo model** signals a further fall in prices and more than in the rest of the country
- **Mortgage rates** are not included in these short-term market models, because they have not consistently added to the models' performance. Still, over time, mortgage rates and credit growth are important driver for the flows at the housing market, and now rates are rapidly on the way up
- *These models are not long-term price models, just short-term models based on flows of (existing) houses approved for sale, actual sales and changes in inventories – which are normally correlated to prices*

OBOS co-op apartment prices down just 0.1% in October, the Oslo total -1.9%

The gap to the rest of the market is larger than normal

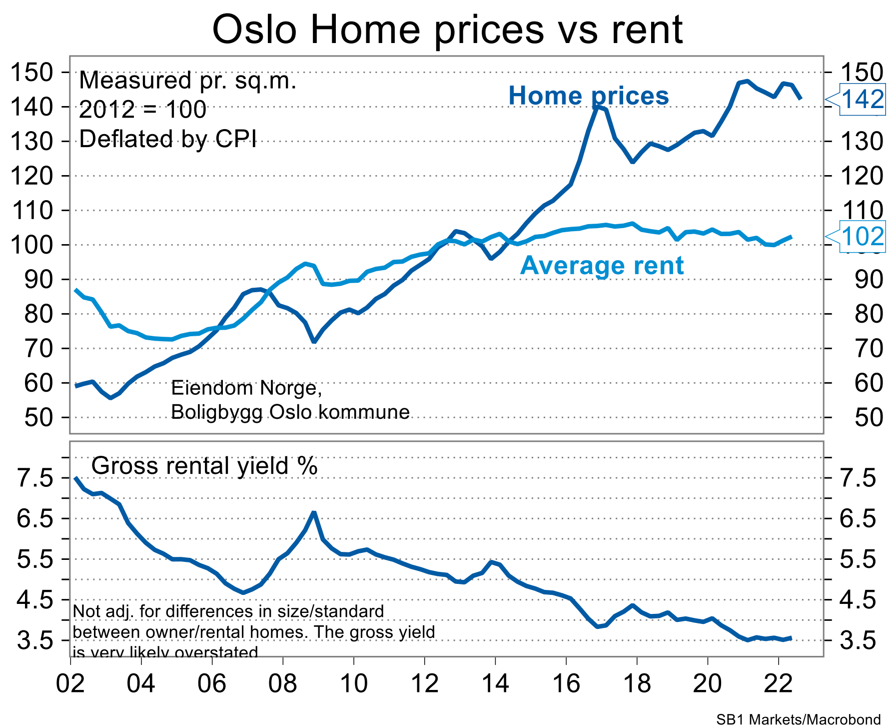


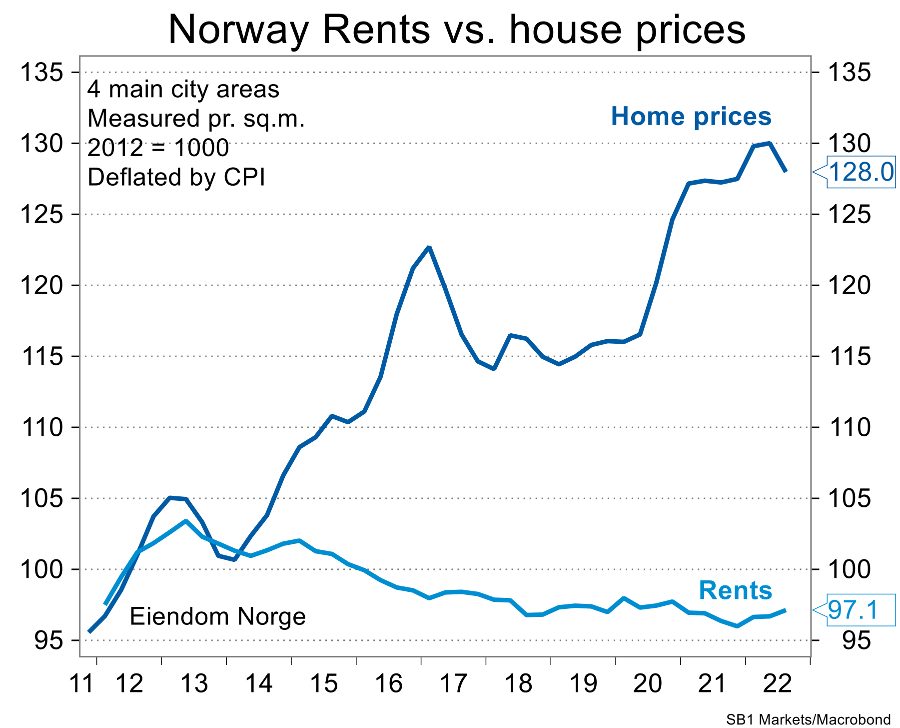


Co-op apartment prices follow the overall Oslo market quite closely, the average price level is somewhat lower than total Oslo market

Why have house prices been so strong recent years? Lack of housing?

If so, strange that rents have been so weak? May is just be 'search for yield' (as mortgage rates fell)

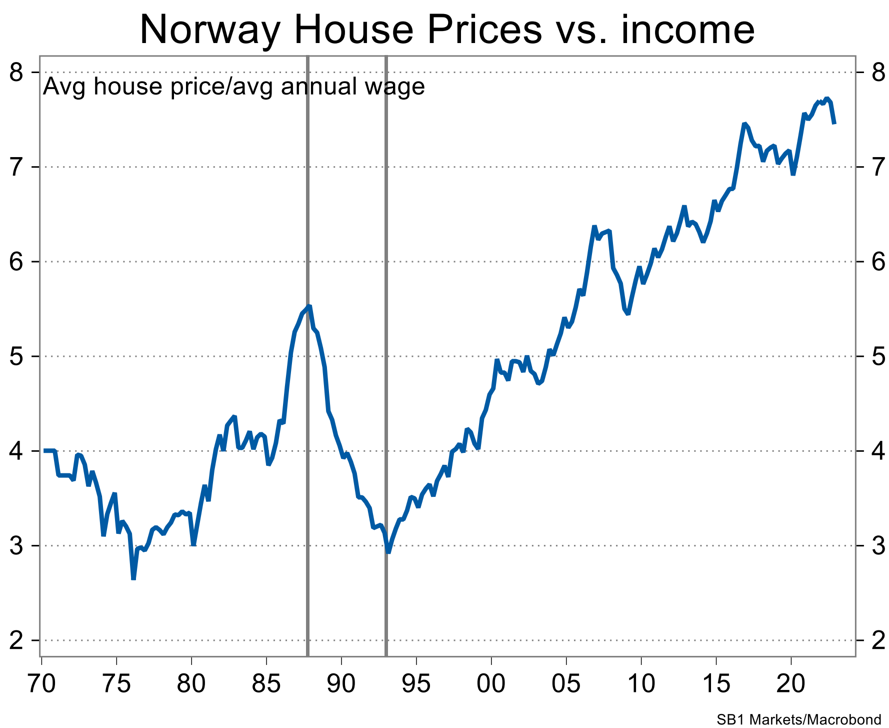


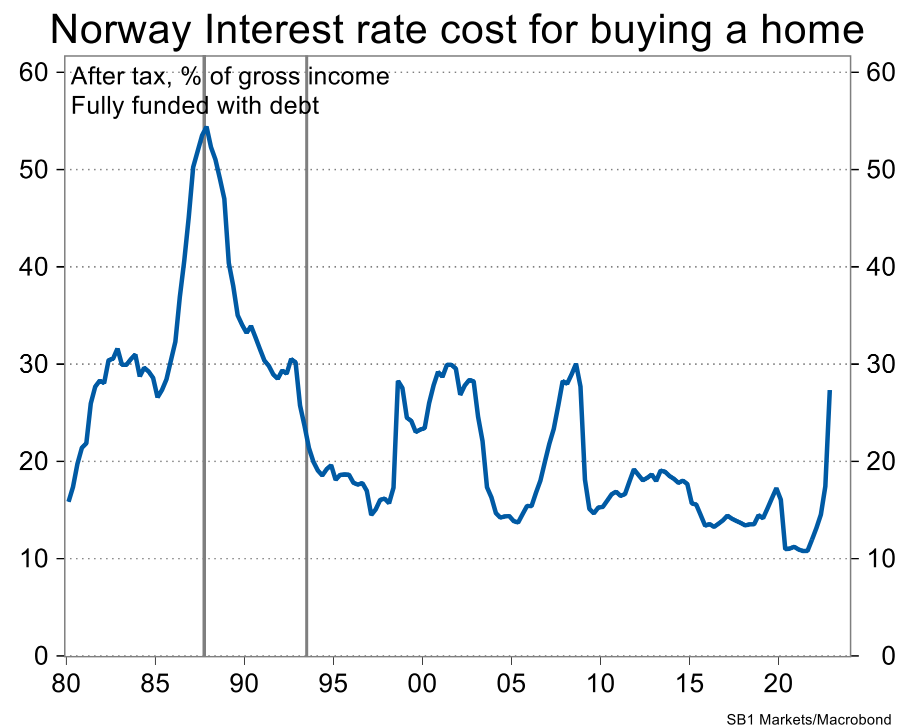


- Yield compression, as interest rates were low vs. income expectations
  - » Rents have been close to flat in real terms the past 10 years in Oslo, while prices are up 42% in real terms (almost 4% per year)
  - » Rents have fallen by 3% in real terms in the average of Oslo/Bergen/Trondheim and Stavanger areas, according to Eiendom Norge, while prices are up 28%
- BTW, mortgage rates are not falling anymore…

The cost of buying an averege home vs the average yearly wage income

The P/Income ratio is falling but still very high. The interest rate burden is now climbing rapidly

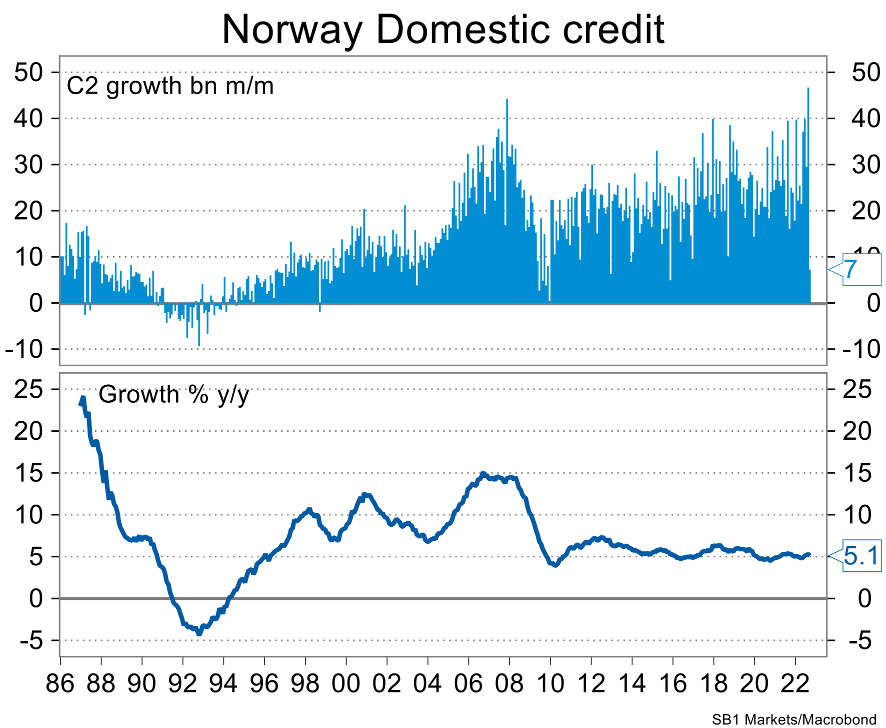


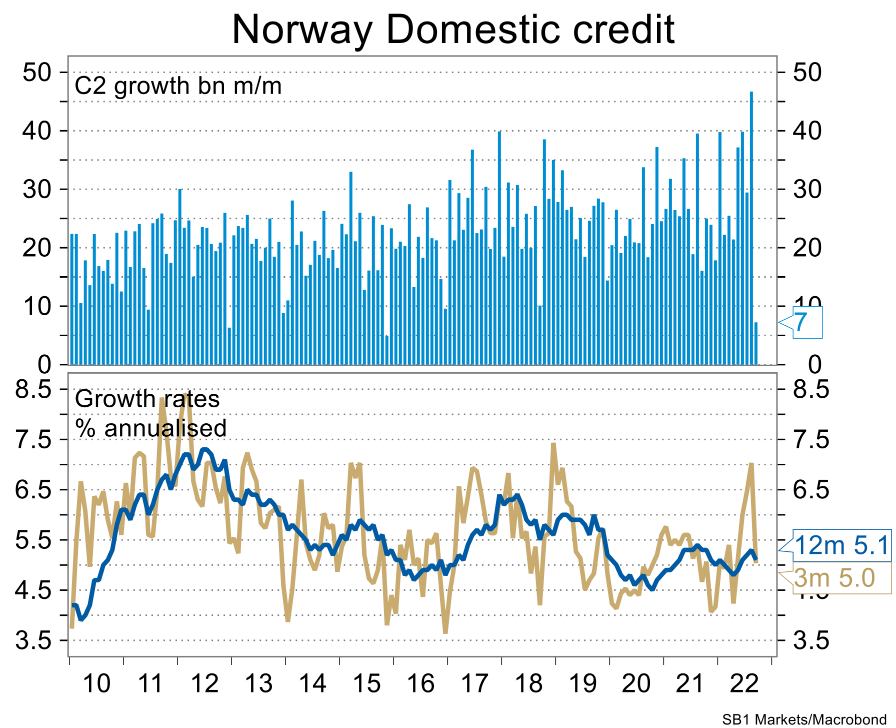


SpareBank 1 MARKETS

After the August borrowing spree, payback time in September

Growth in household debt is gradually slowing, and is now slightly under the NoBa estimate from September

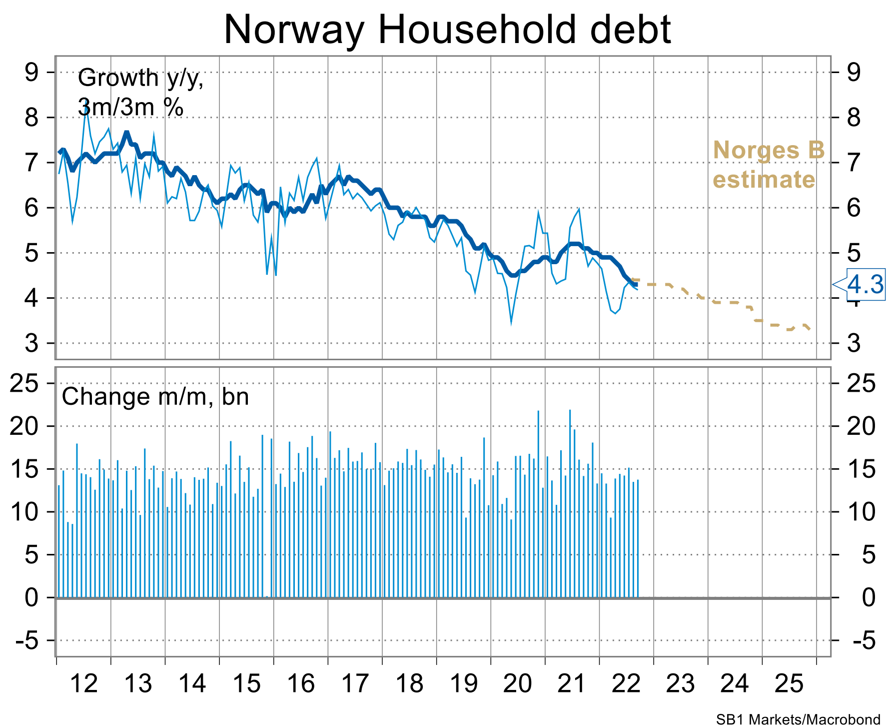


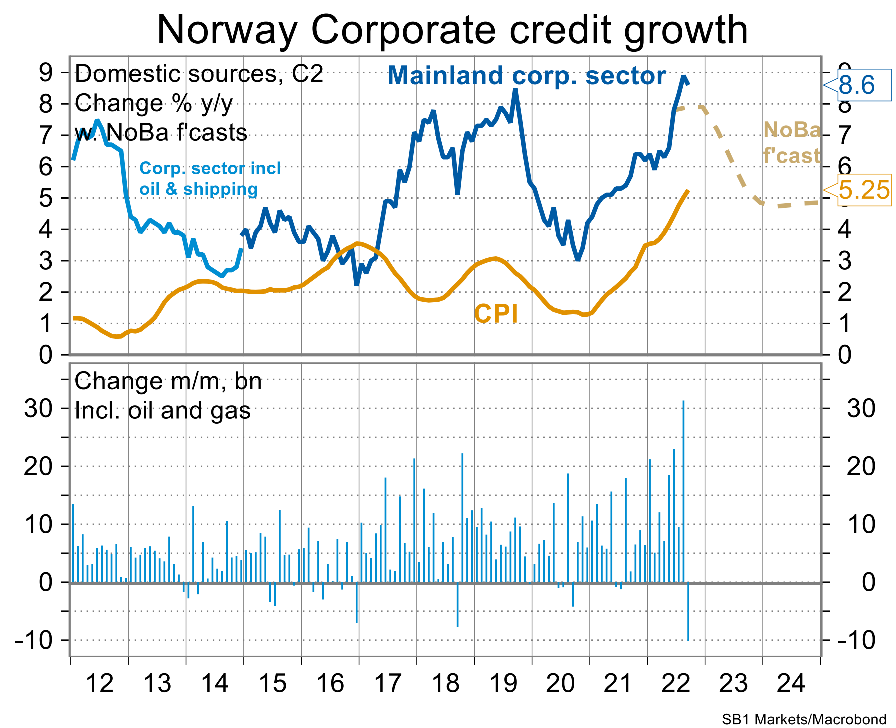


- **Total domestic debt** (C2) rose by NOK 7 bn in Sept, down from 45 bn in Aug, we expected 19 bn. The annual growth rate fell 0.2 pp to 5.3%, we expected an uptick from the prev. reported 5.2% to 5.3%! The 3m/3m growth rate fell to 5% from 7%. What happened?
- **Corporate C2 credit** contracted by NOK 10 bn, following the unprecedented 31 bn lift in Aug, and the annual rate fell by 0.7 pp to 7%. For Mainland companies, the annual rate fell 0.3 pp to 8.6%, way above NoBa's estimate. The unusual swing is probably due to transfers of debt from abroad
- **Household credit** rose by NOK 14 bn in Sept, 1 bn more than we expected (and up 1.5 bn form Aug). The annual rate was unch. at 4.3%, as we expected. NoBa estimated 4.4%. We expect a further slowdown as higher interest rates and falling house prices curb demand for debt
- **Local governments** added NOK 4 bn in Sept, 0.5 bn more than we expected. The annual growth rate gained 0.5 pp to 4.3%. Last summer the rate was 8%! Finally, local gov's are not increasing their debt/income ratio

Demand for household credit is slowly slowing

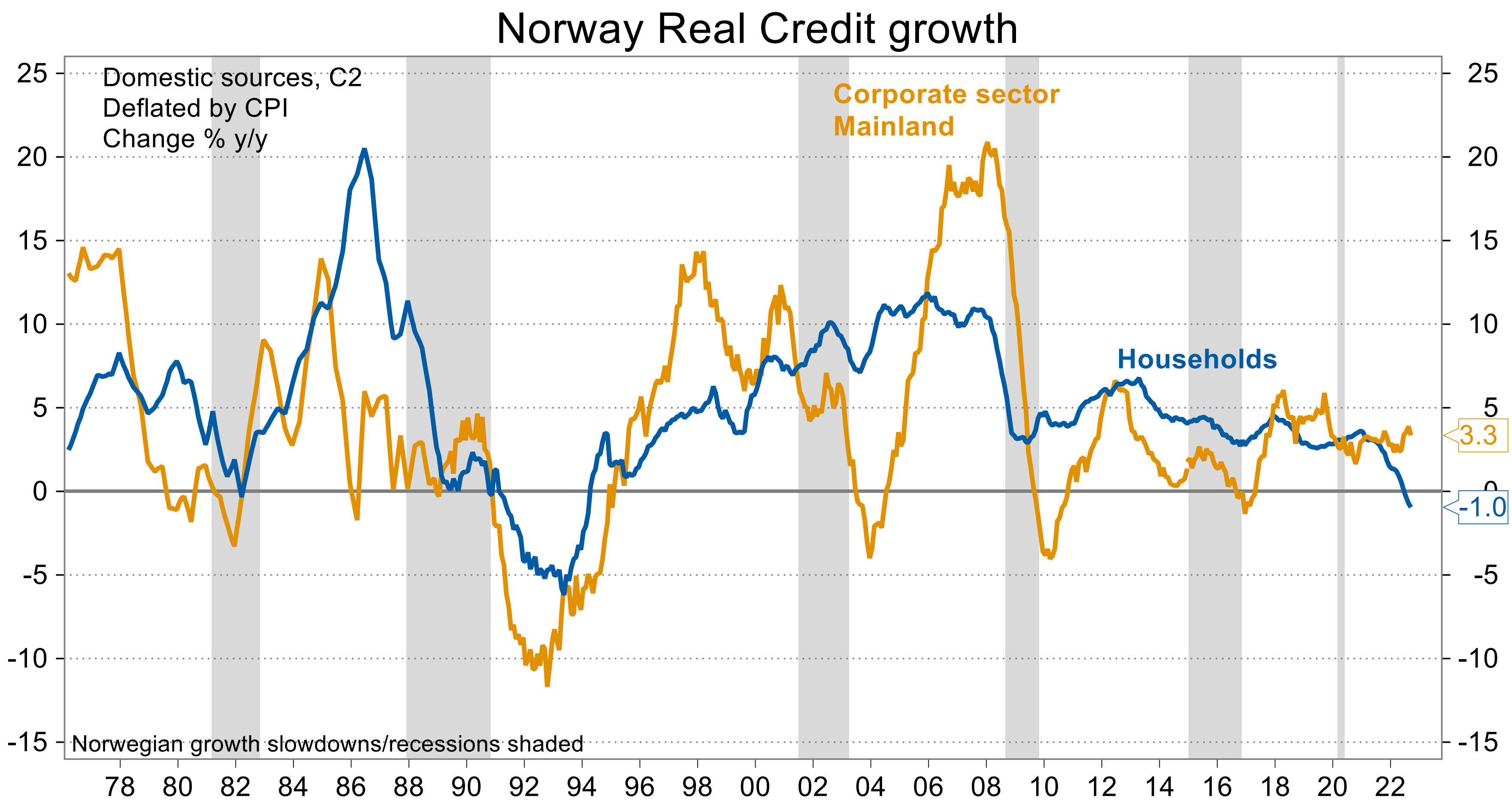
…while growth in credit to the corporate sector is higher than since before the Financial Crisis





- **Household credit** growth has been rather stable past 6 months, at a pace close to the actual annual growth rate, 4.3%. Still, we deem the trend to be slightly downwards. the y/y rate is now at 4.3%, 0.1 pp below NoBa's est. NoBa expects growth to slow to 4.0% by the end of 2023 as a result of higher rates and falling house prices. We expect household credit growth to slow faster the coming months/quarters
- Monthly growth in **corporate domestic credit** is volatile, most likely because loans are transferred to or from abroad. In Sept, debt fell by NOK 10 bn, the largest decline ever, following the larges increase ever, in August, NOK 31 bn. Growth in Mainland business debt has shot up recent months, and is at 8.6% in Sept, 0.7 pp above NoBa' f'cast. NoBa expect credit growth to slow the coming years, but nothing like during slow-growth periods

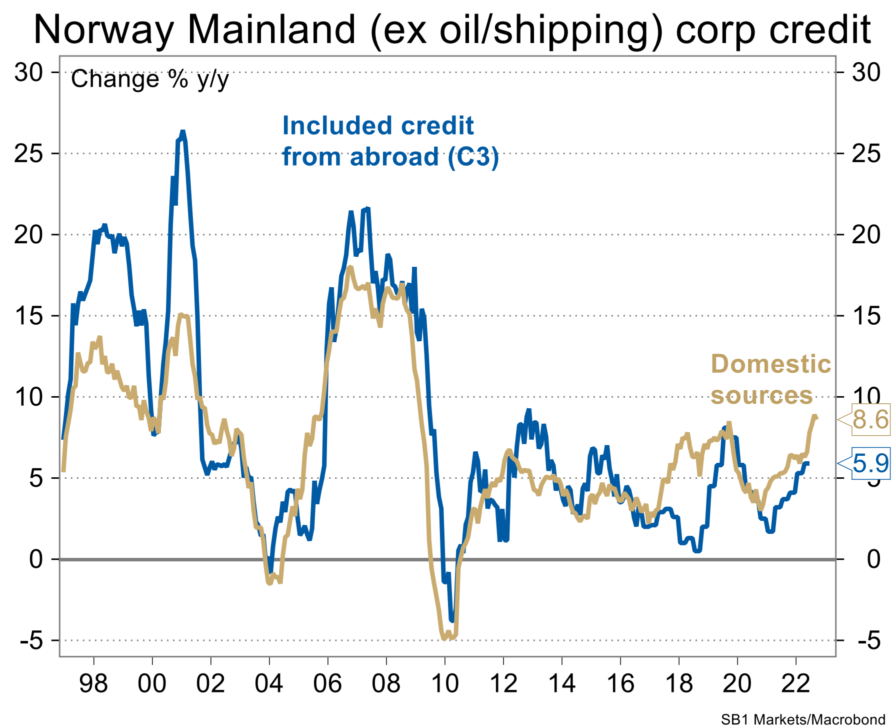
Real credit growth slows during economic slowdowns, recessions

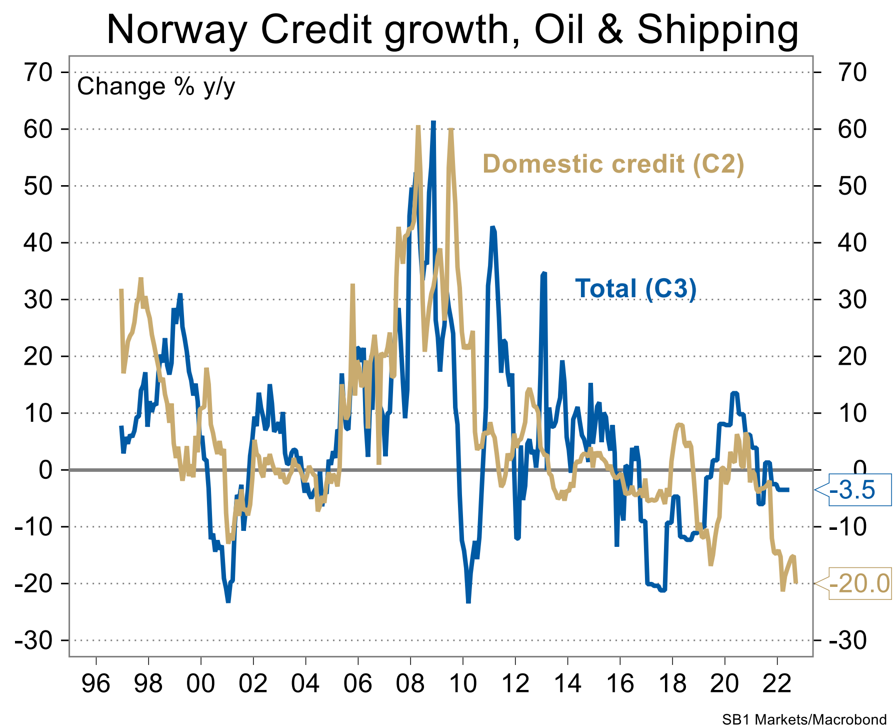


SB1 Markets/Macrobond

Mainland corporates increased their total debt (including foreign credit) by 5.9%

… in Q2. Debt from domestic sources (in C2) was up 8.3% in Sept. Some transfer of foreign loans?

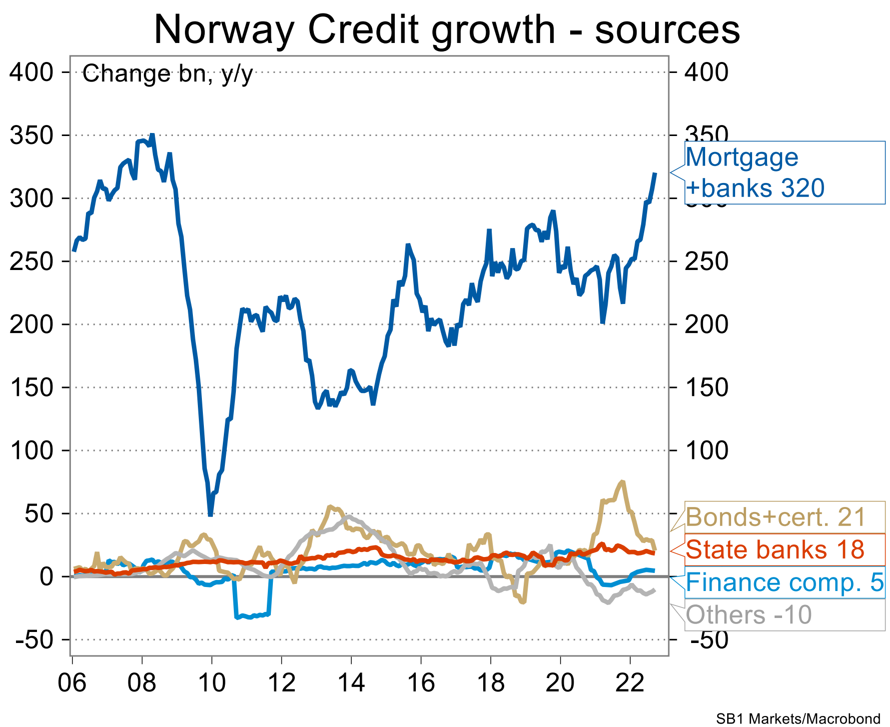


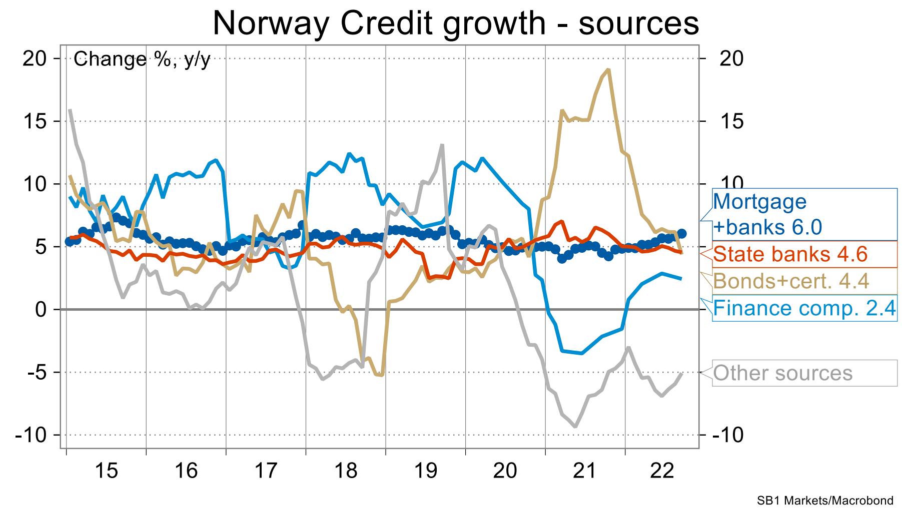


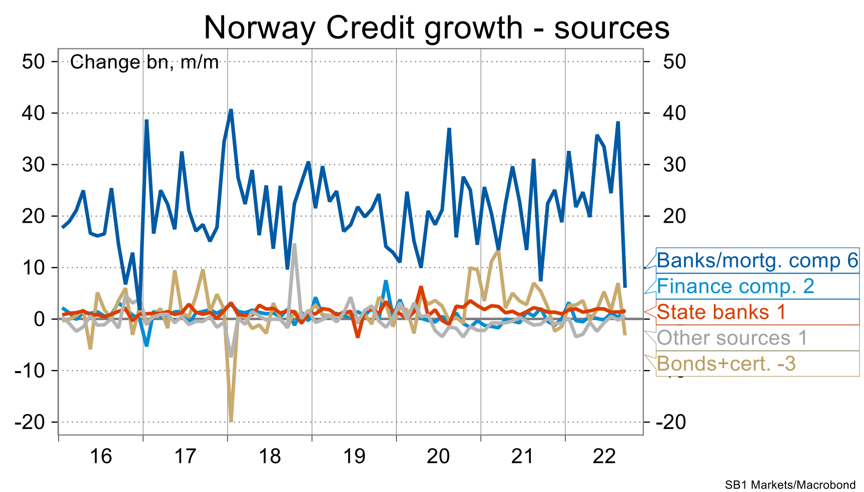
- **Oil and shipping** companies have been moving the opposite way, borrowing more abroad, paying down debt in Norway. The sum is down 3.5% (Q2), even if domestic debt is down 20% (via transactions)!

Banks are increasing their large market share further

Bond market borrowing has slowed substantially recently







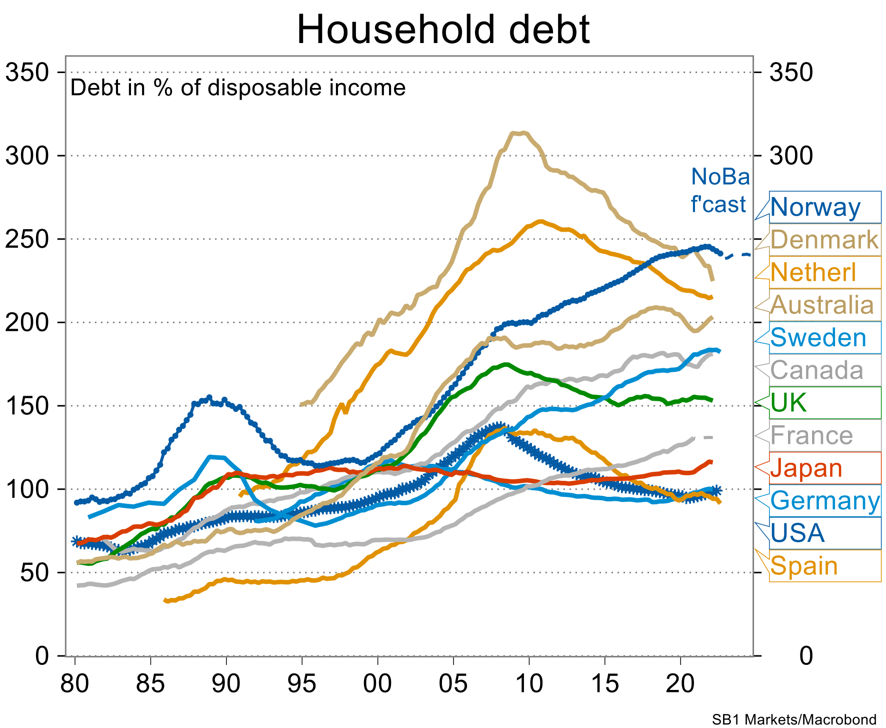
- Banks/mortgage companies are up NOK 320 bn (6.0%) y/y, and accelerating!
- Net issuance of bonds (to non-financial sector) is up NOK 21 bn (4.4%) y/y – a normal growth rate but well down from the peak late last year (75 bn, 19%). The credit cycle has turned
- Finance companies are up a mere 1.9% y/y, while all 'others' have reduced their lending
  - » Both insurance/pension funds as well as Statens Lånekasse, Eksfin are included in our residual 'others', but just the sum of SL & Eksfin is down

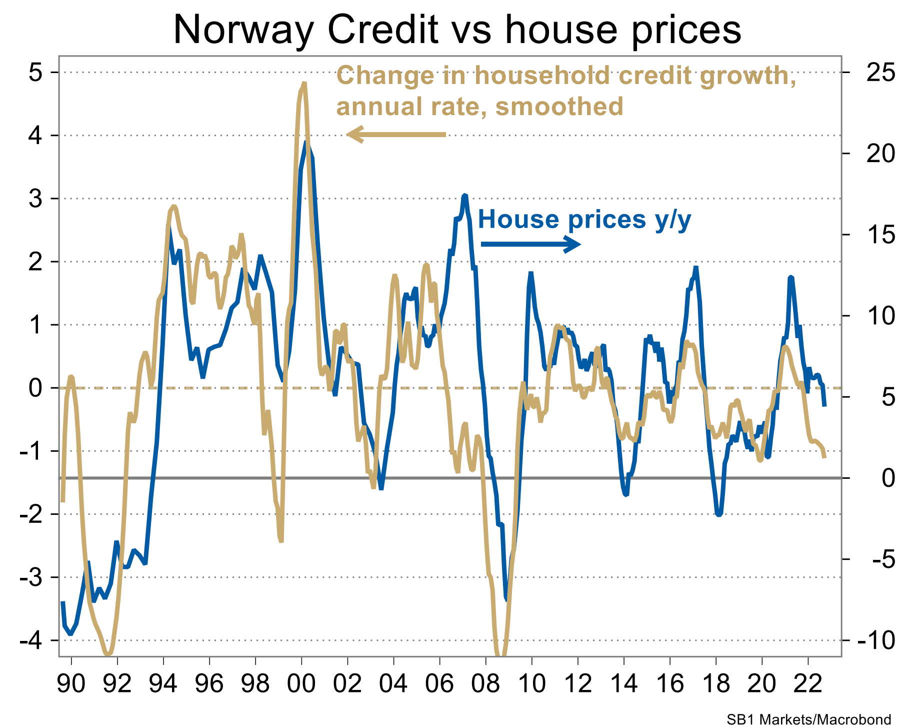
The seasonally adjusted 'sum of the parts' credit supply do not exactly equal changes in the total C2 seasonally adjusted. Consumer banks are included in 'banks and mortgage companies'

SpareBank 1 MARKETS

Household debt/income: We are no. 1! But the debt/income ratio turns down

... And the downside may be substantial

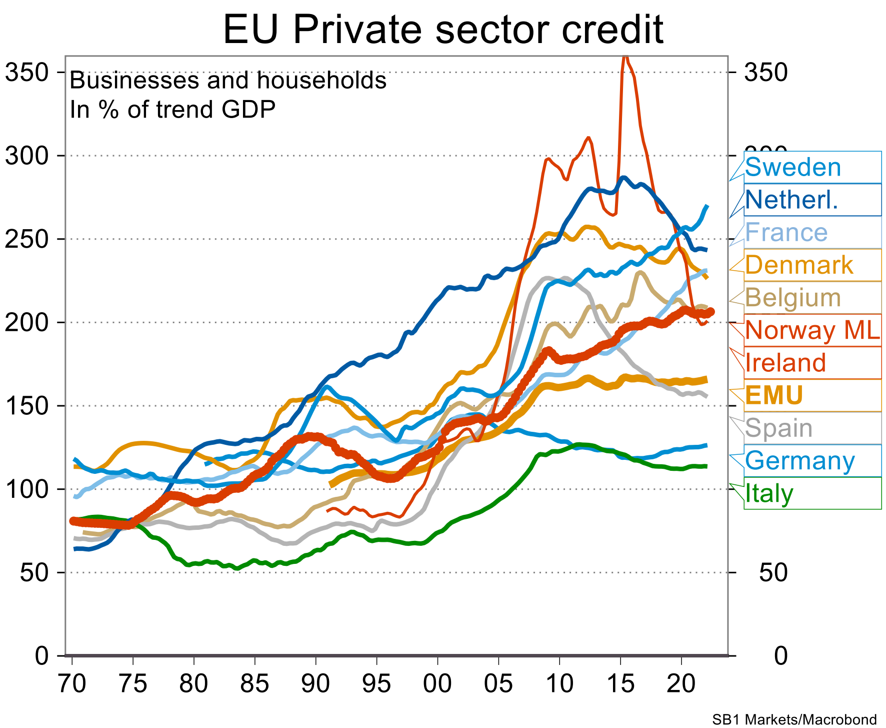


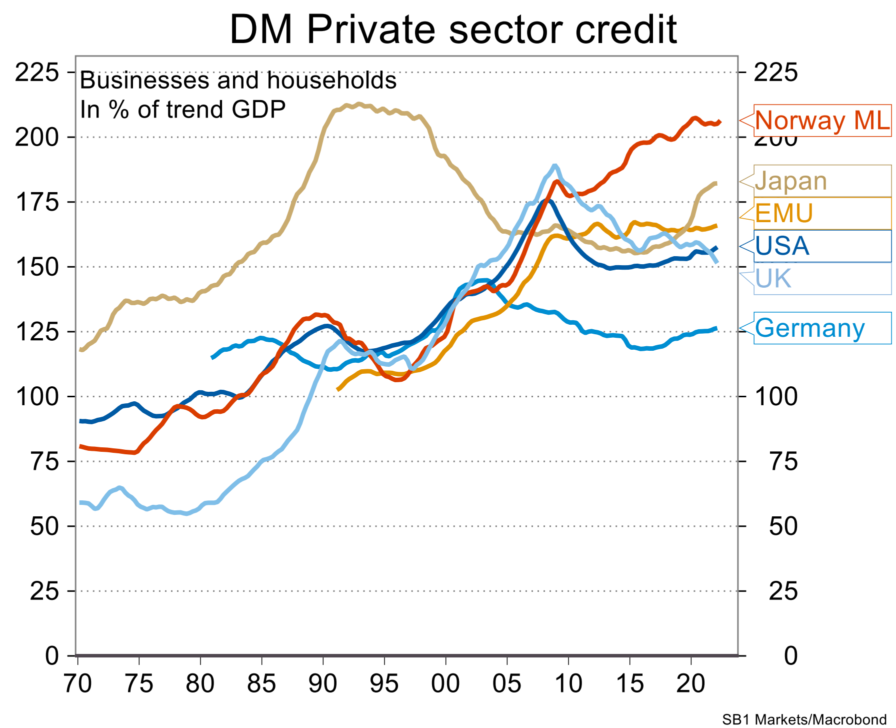


- **Norwegians households' debt has** steady been growing faster than income but not more since last year
- **Changes** in credit **growth** (the 2nd derivative) is usually correlated to economic growth, and asset markets – including growth (1st derivative) in house prices
  - » A slow retreat in the debt ratio will probably be healthy in the long run, and if it is gradual, it will not be too painful - even not for the housing market
  - » If credit growth slows less than 1 pp per year, that is – say from a 5% growth rate to 4% next year, and then down to 3% etc, house prices should just flatten

The private sector has mostly been deleveraging since the Financial crisis

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





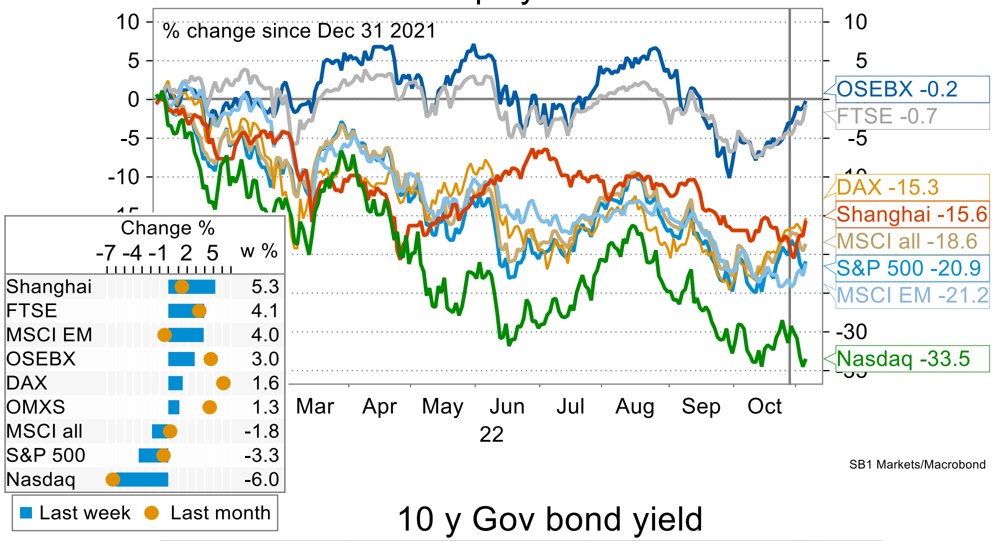
- But not everywhere: Not in Norway, Sweden (+Canada & Australia, of course). The French have been accumulating debt as well
- Rather interesting: Debt ratios in Germany and Japan have turned up recently – and the Americans are borrowing more again

SpareBank 1 MARKETS

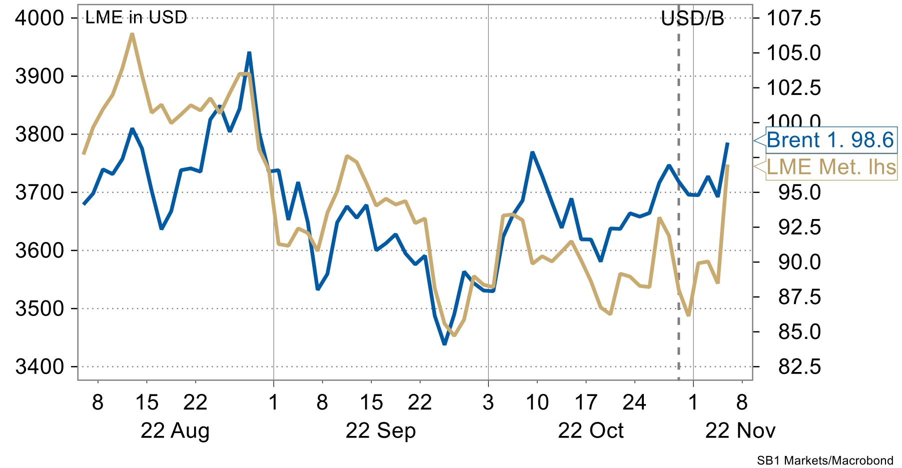
Risk off in equity markets, bond yields up – together with raw material prices

Some hope for an investment driven recovery in China? CNY up; NOK further up, the GBP lost ground again

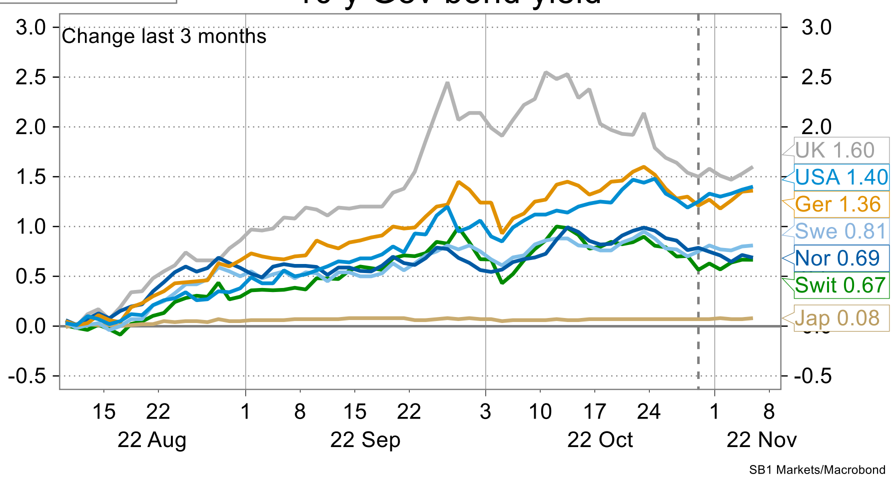
Equity Indices



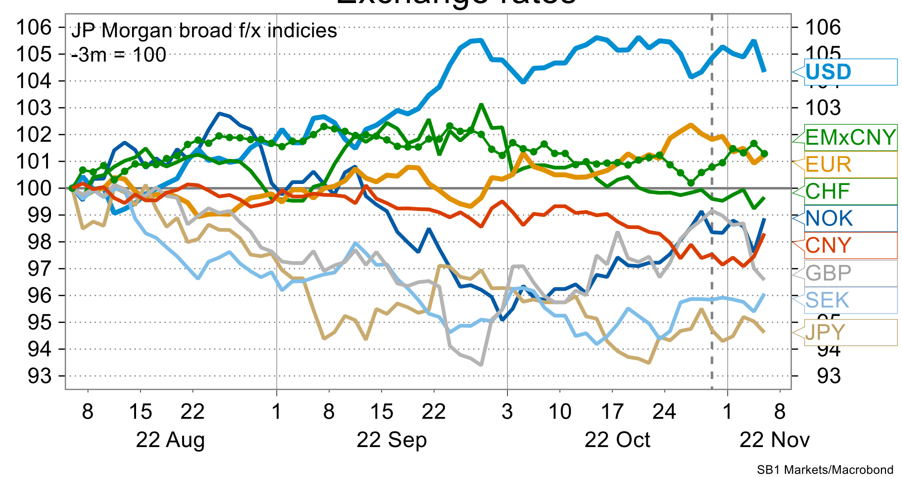
Oil vs. metals



10 y Gov bond yield



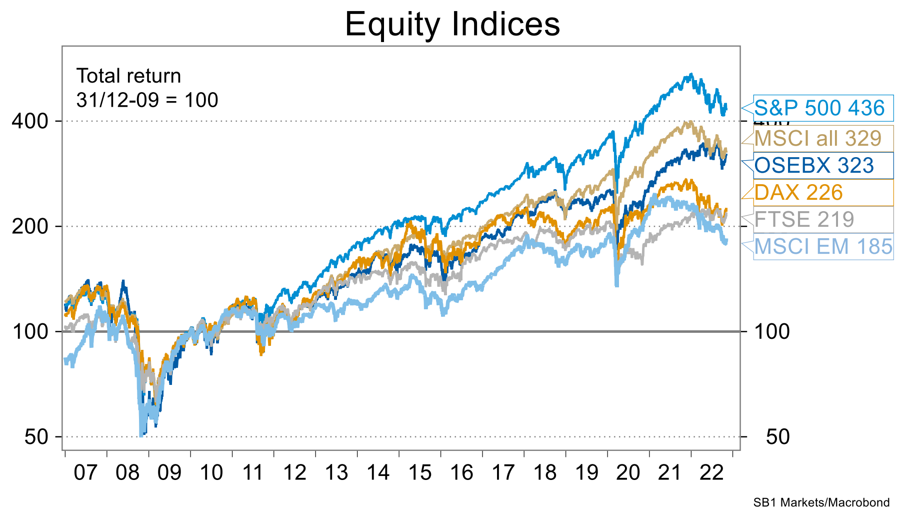
Exchange rates

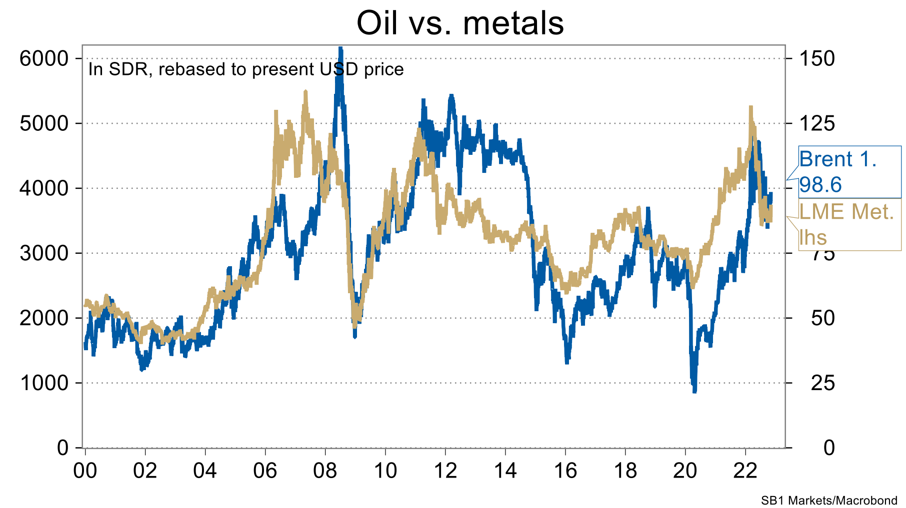


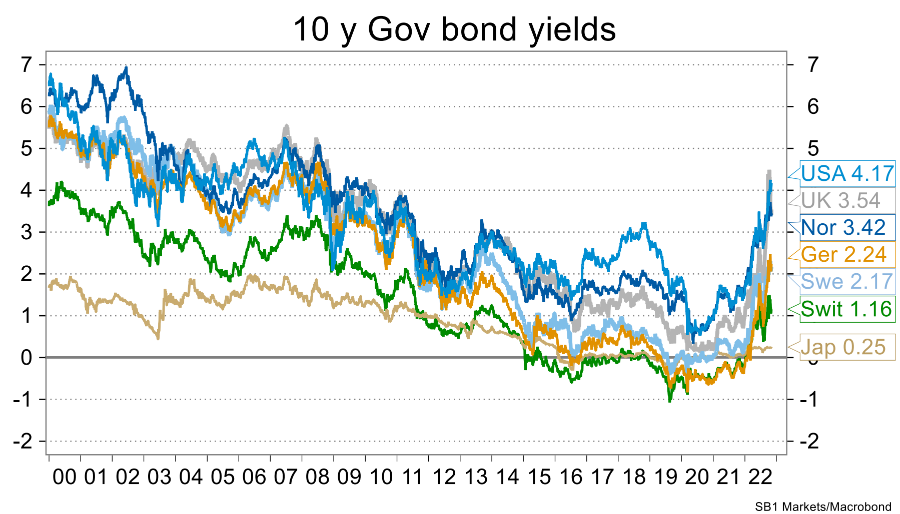
SpareBank 1 MARKETS

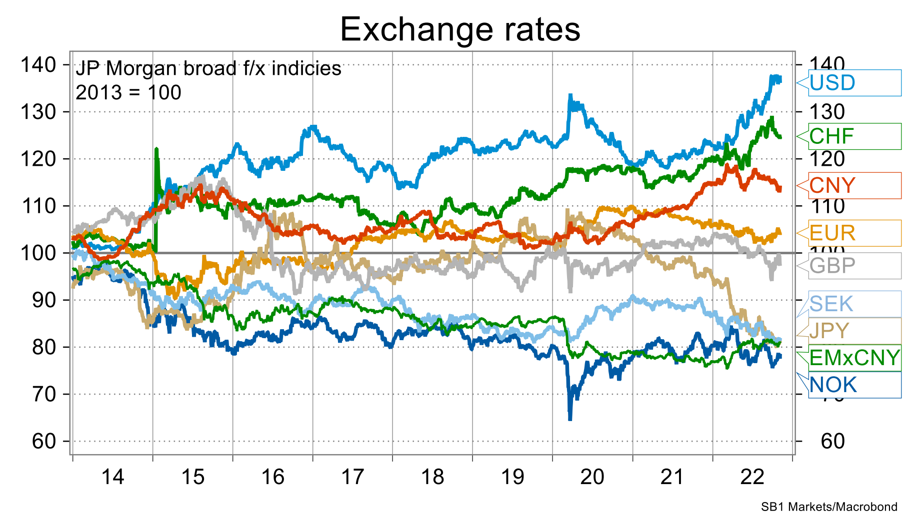
The long-term picture: Stock markets down, commodities down, bond yields up

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





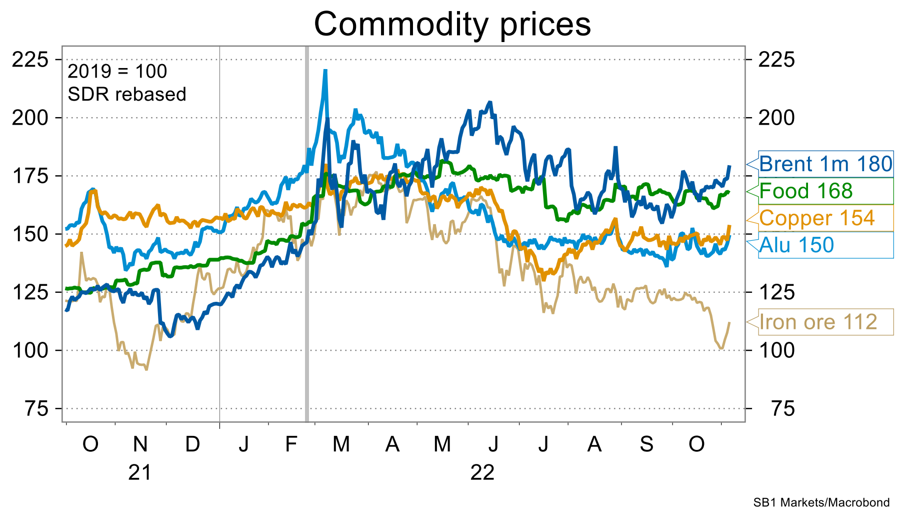


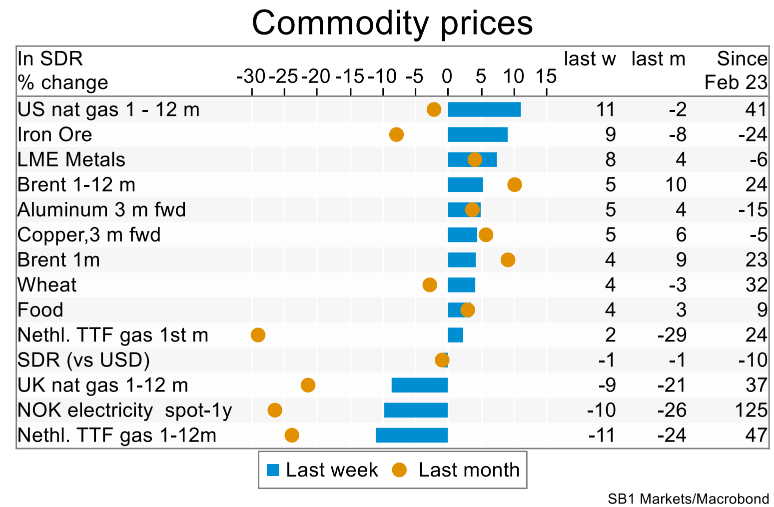


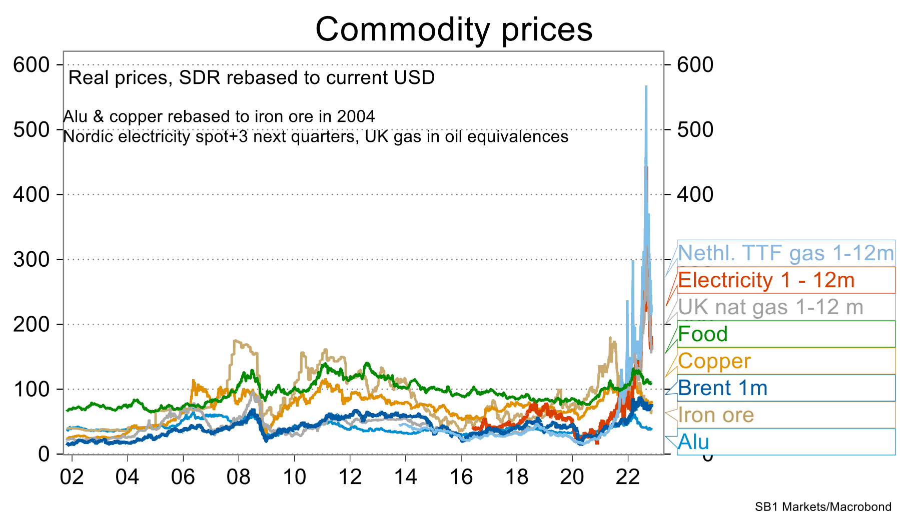
SpareBank 1 MARKETS

Commodity prices up hast week, but European gas/electricity further down

The iron ore price partly recovered, on hopes of a new Chinese covid policy, investments stimulus







Last week – prices in SDR

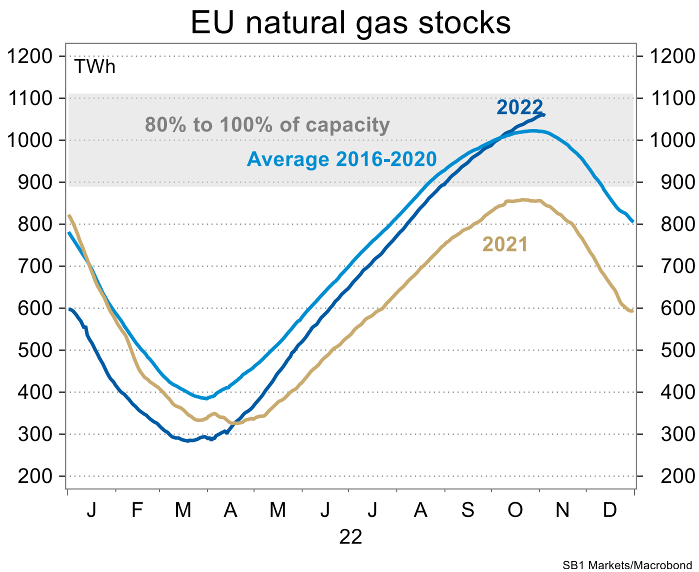
- **European natural gas** fell further last week, as did **Norwegian electricity prices**, down 9 - 10% (the next 12 months)
- **Oil prices** climbed further, up 4 - 5%
- The Economist's **food commodity index** suddenly turned up, and in SDRs they are higher than before the war, but still lower than the past 10 y average, at least in USD
- **Metal prices** rose sharply, the LME index +8%

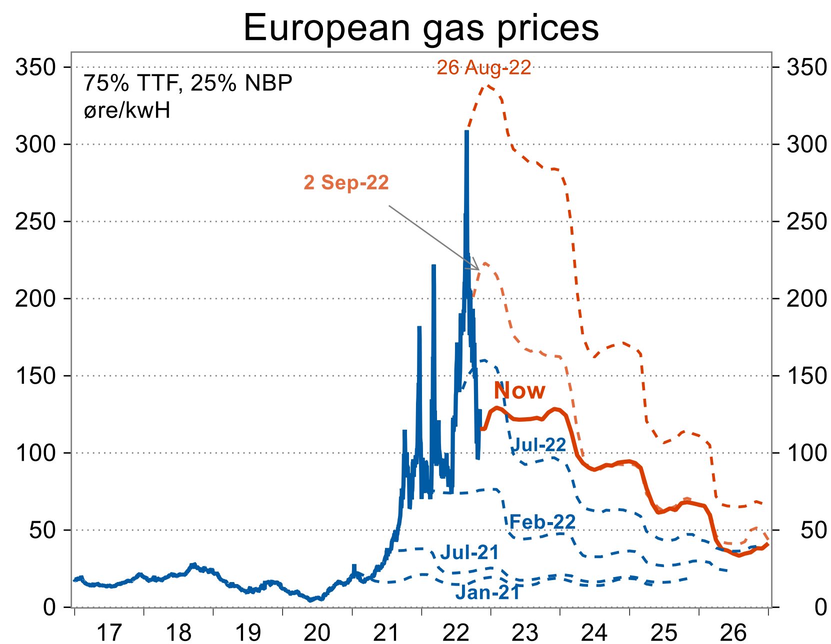
SDR: IMF's Special Drawing Rights – a 'global currency'

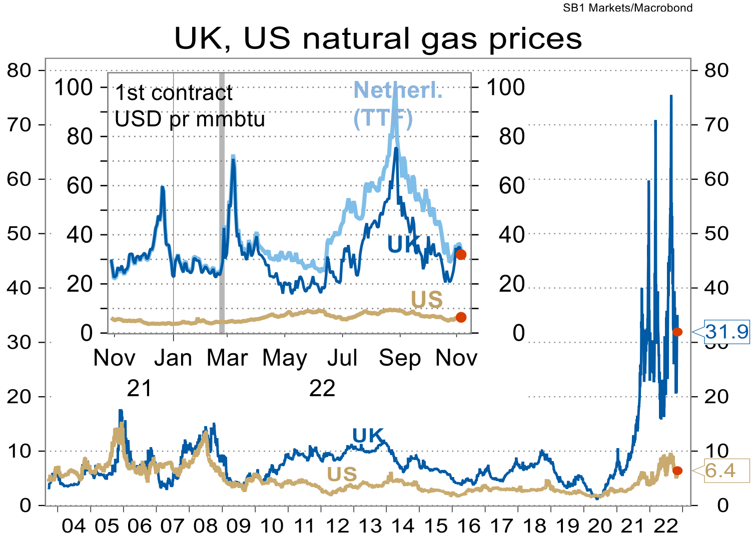
SpareBank 1 MARKETS

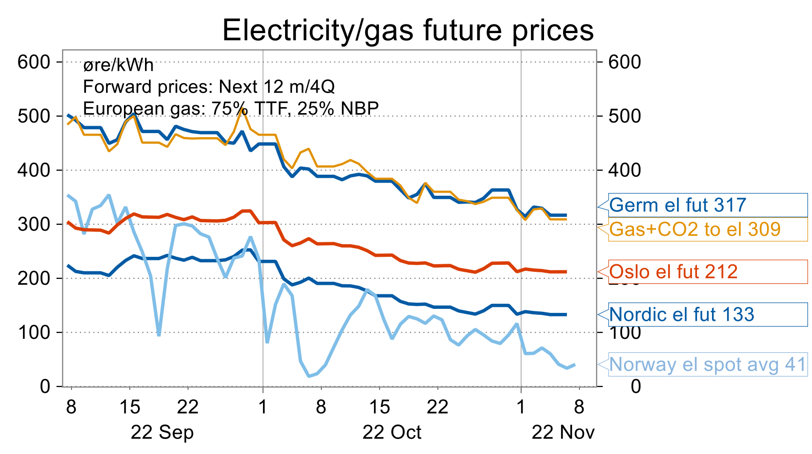
European gas prices further down, as inventories are filled up

Electricity prices are trending rapidly down as well





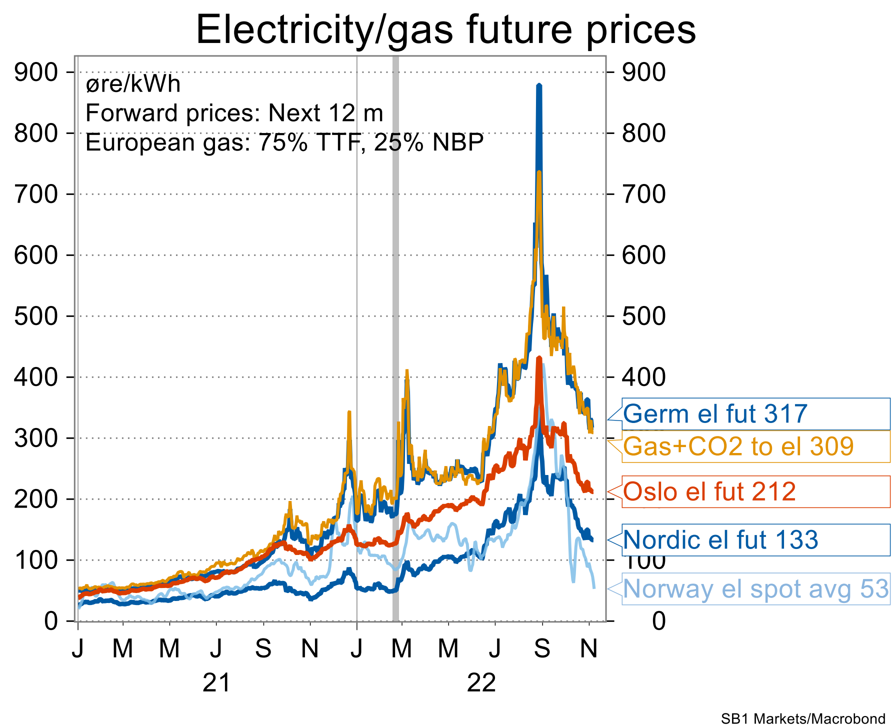


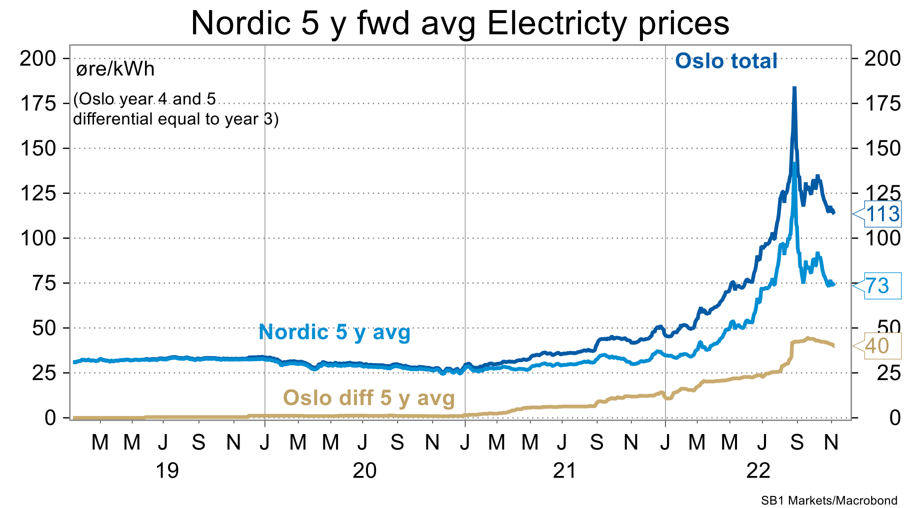


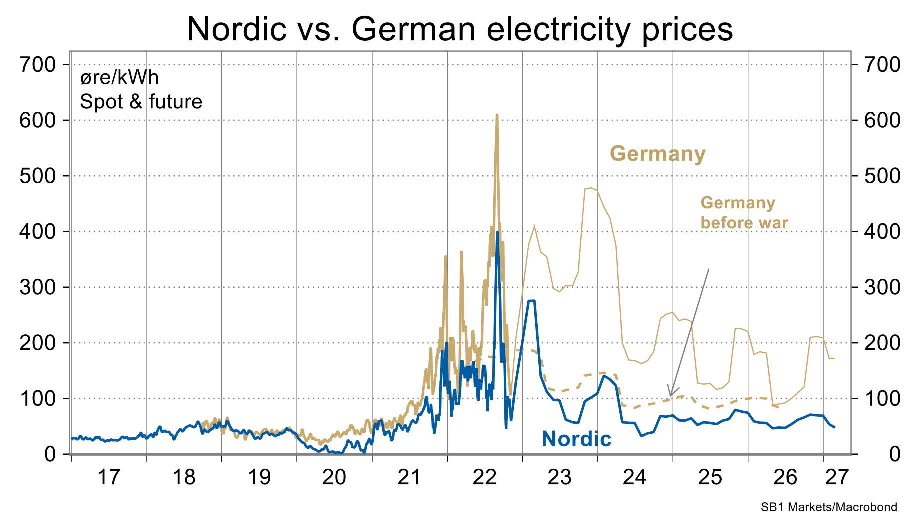
SpareBank 1 MARKETS

European gas & electricity sharply down last week

… but the price level is still high, at least the 12 m fwd prices



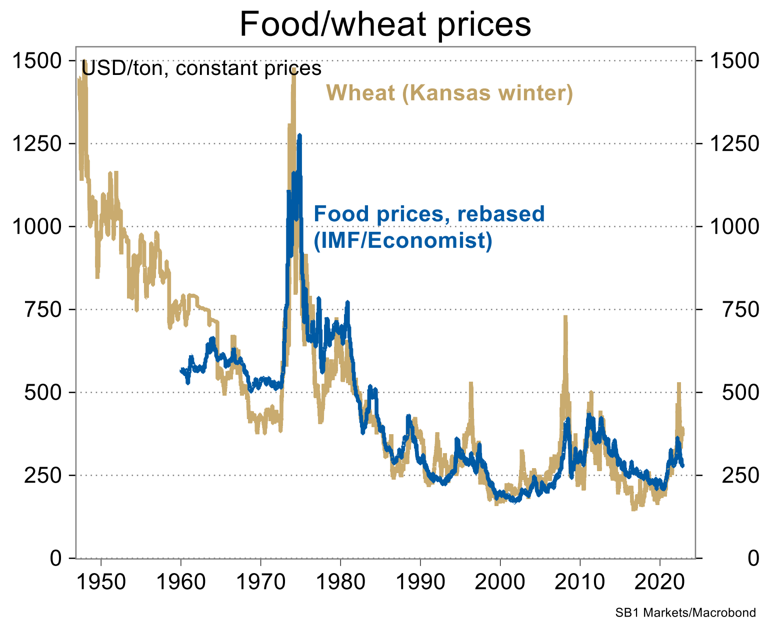


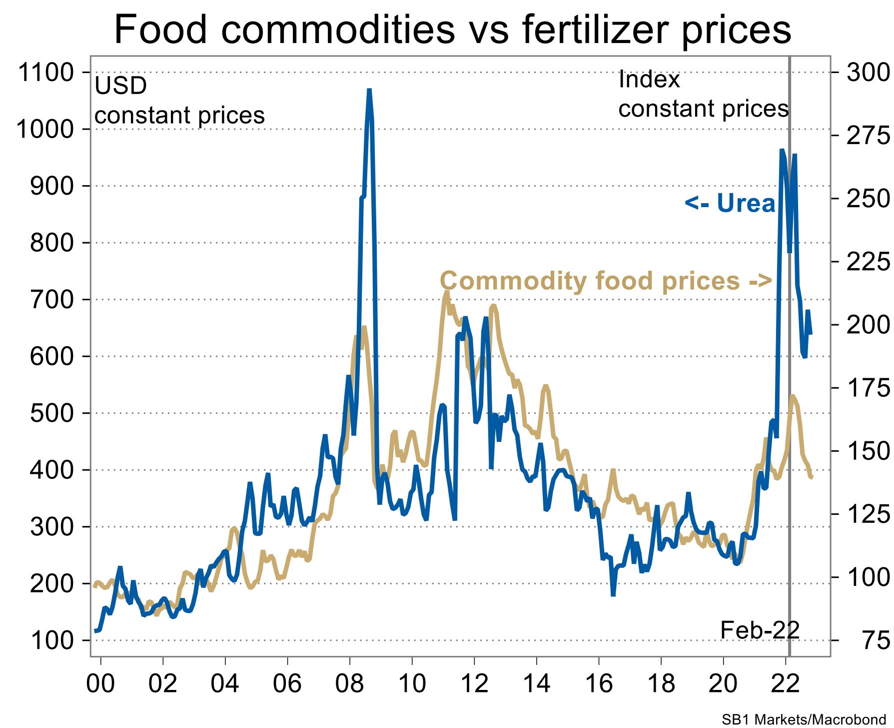


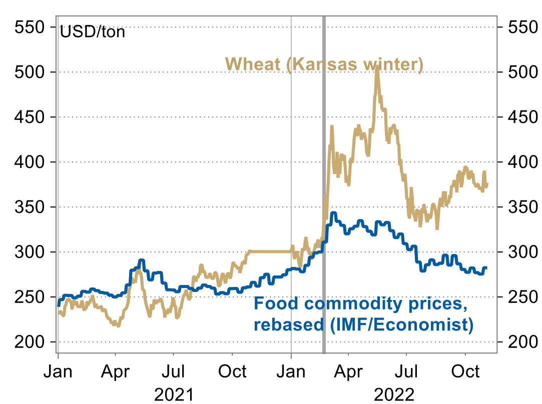
European gas: 75% Dutch TTF, 25% UK NBP, excl. CO2 cost

Food prices are trending down

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



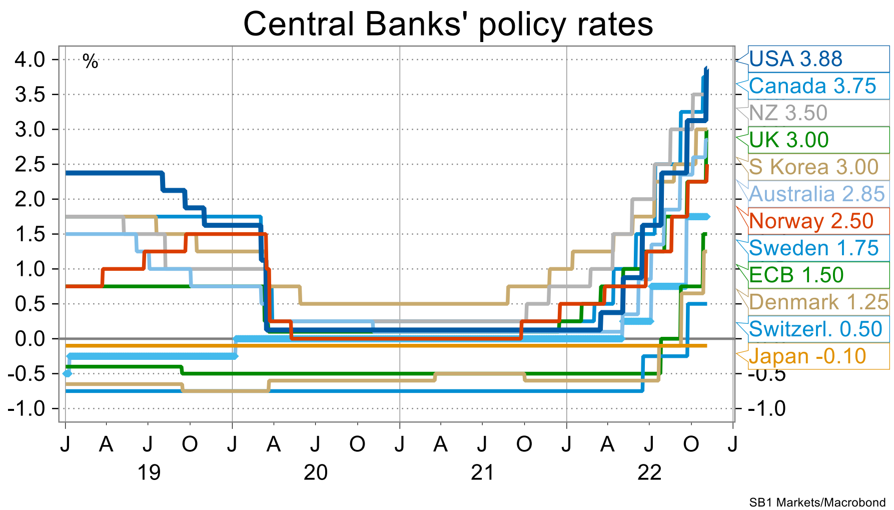


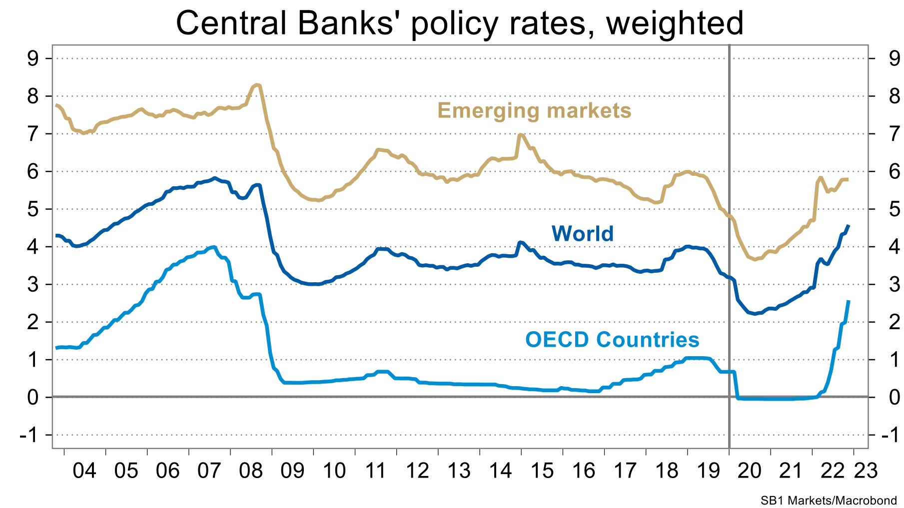


Urea prices have been falling too

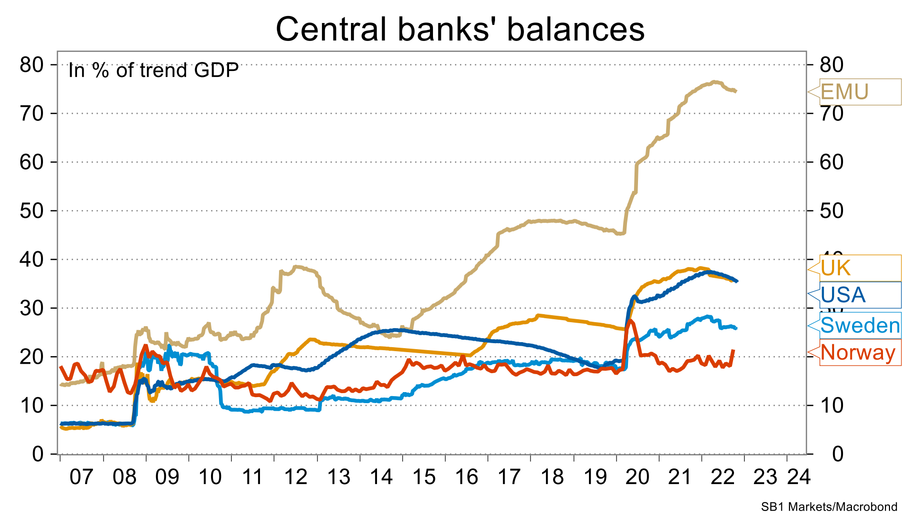
Last week: US & UK +75 bps; Australia and Norway just +25 bps

Norway has fallen down to the 7th place on the rich man's rate ranking list





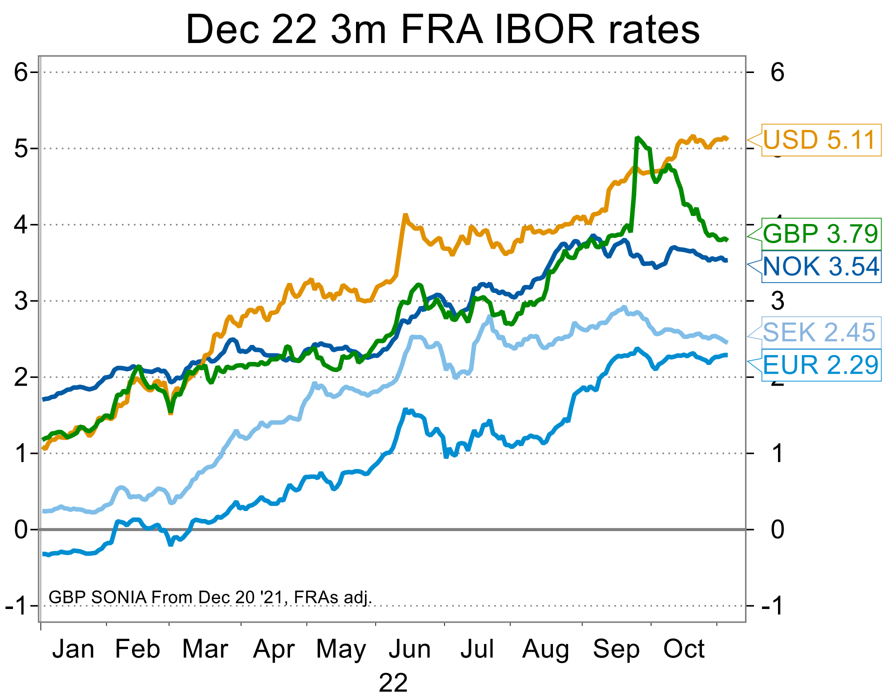
- **Central banks** are hiking rates even if they expect growth to slow (US, EMU) or the economy to contract (Sweden, UK, Norway) because inflation is way above target (including all measures of underlying inflation, partly also costs) and is expected to remain above target for several years
- The **EM average policy rate** fell 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 have started reducing their holdings, moving into the **QT zone**. US ramped up its QT program (doubled the pace) from the beginning of September

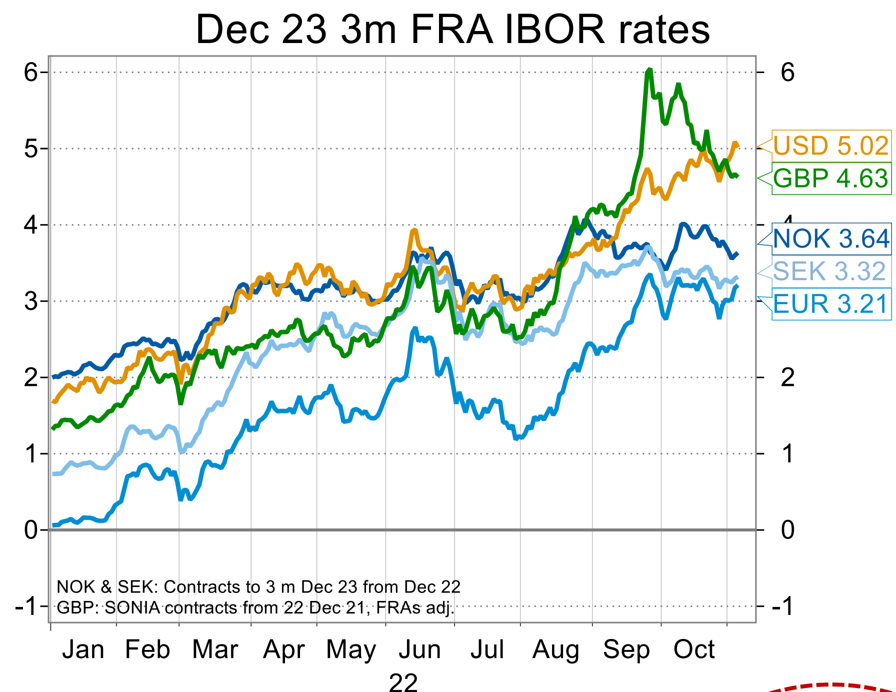


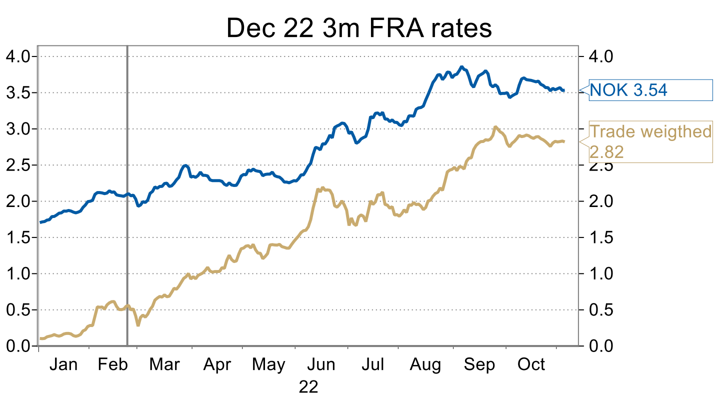
SpareBank 1 MARKETS

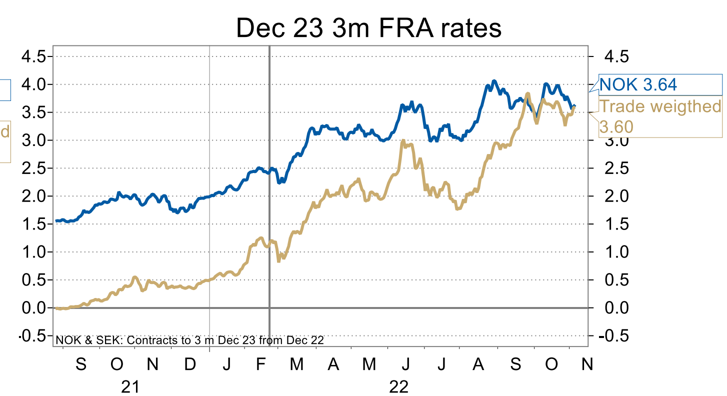
FRAs on the way down most places, except for the US

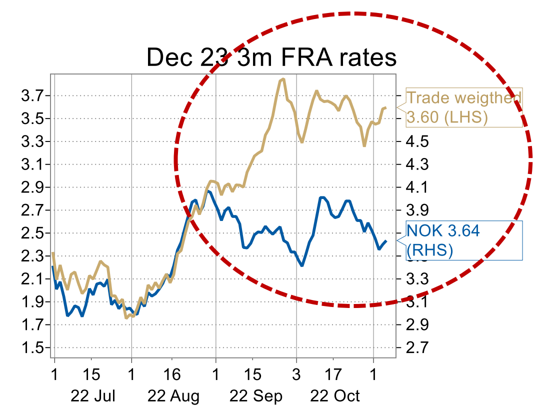
GBP rates have come down to more reasonable levels. And the ECB can not kill the European economy









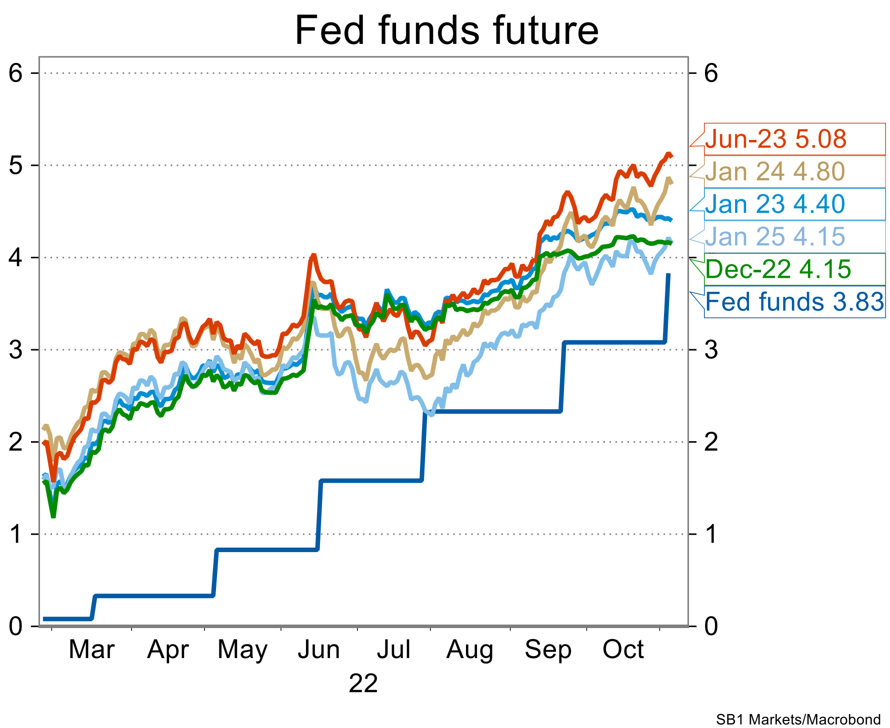


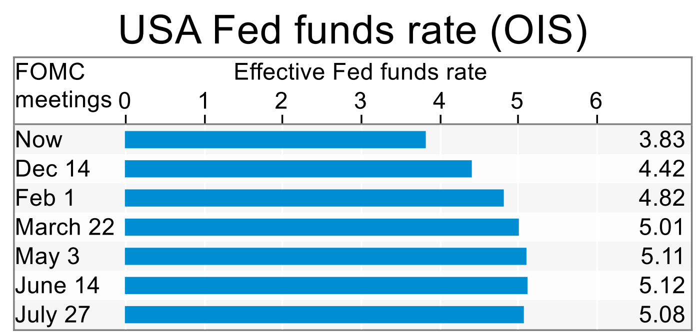
SB1 Markets/Macrobond

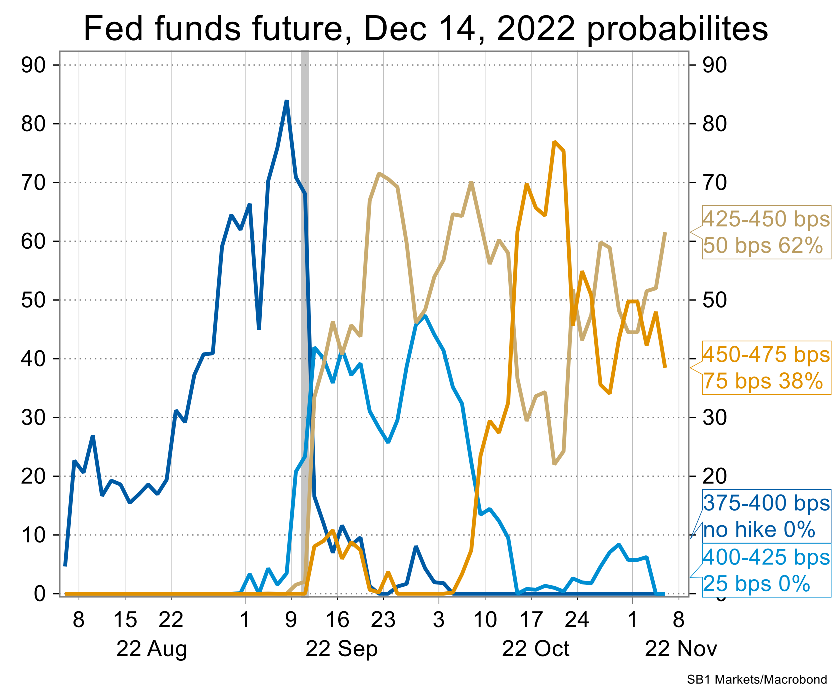
SpareBank 1 MARKETS

Another ‘triple’ hike last week, but +50 bps most likely in December, says the market

However, the probability is 38% for a fifth ‘triple’ hike in row

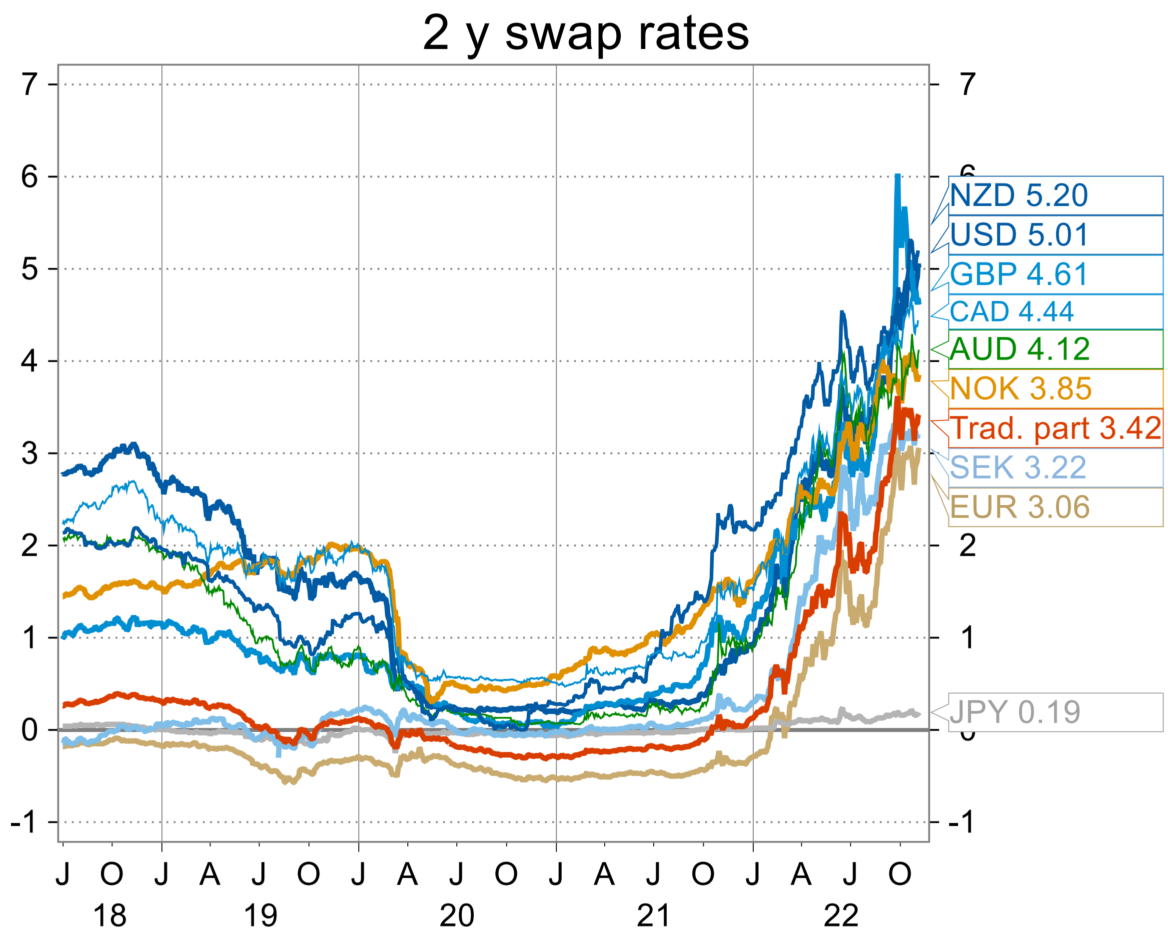




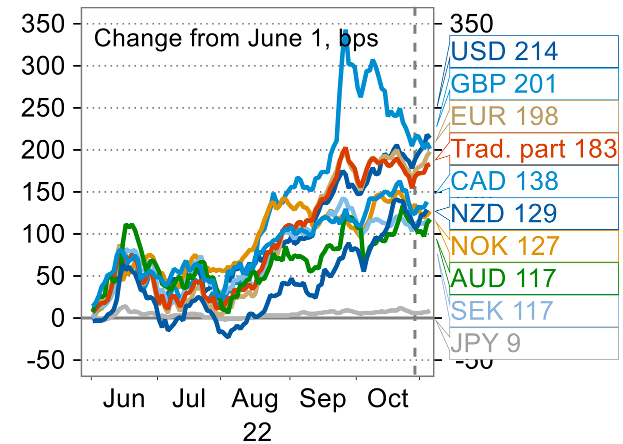


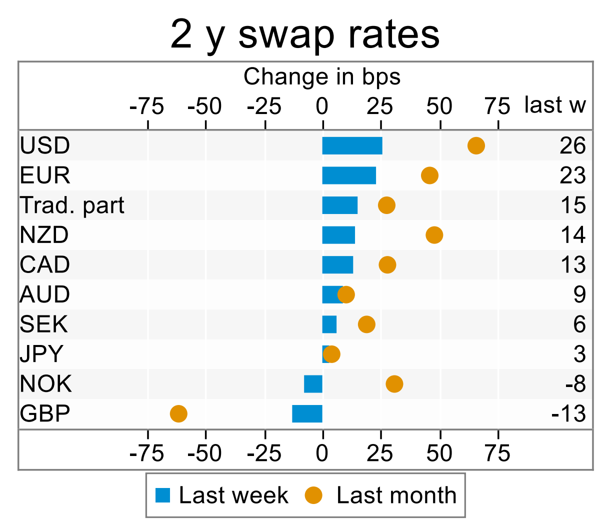
All 2 y swap rates mostly up last week

GBP rates fell even if BoE delivered the 75 bps hike



SB1 Markets/Macrobond

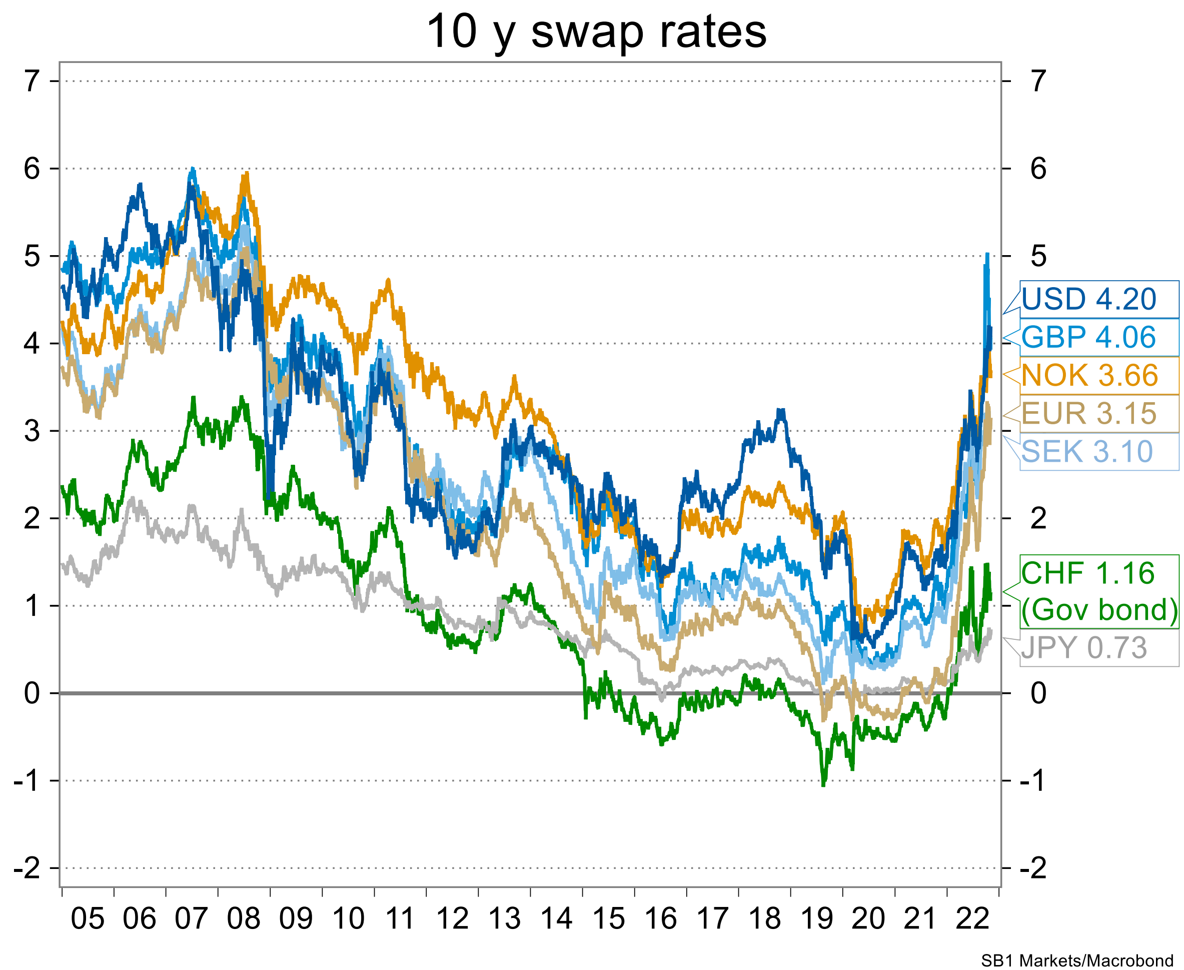


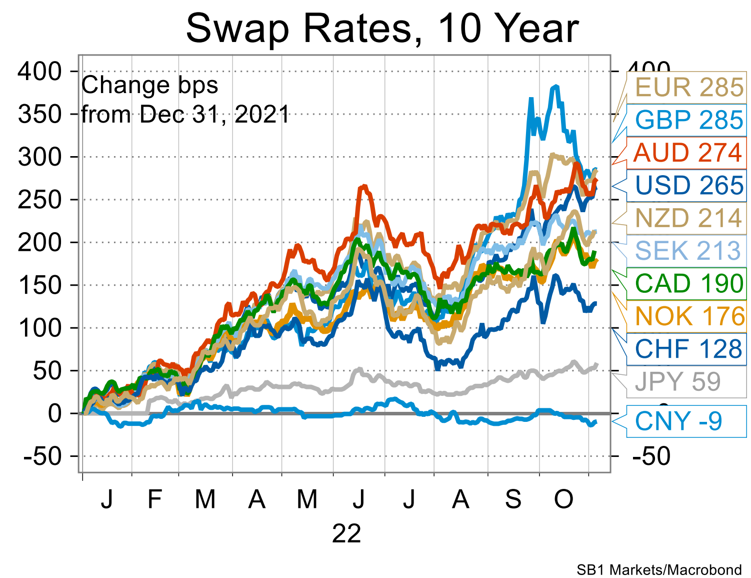


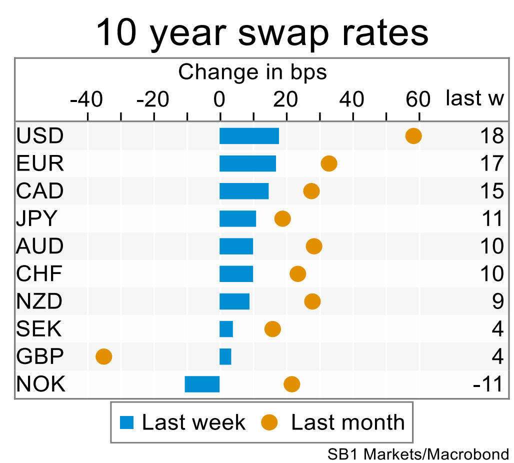
SB1 Markets/Macrobond

SpareBank 1 MARKETS

Up everywhere, except for Norway

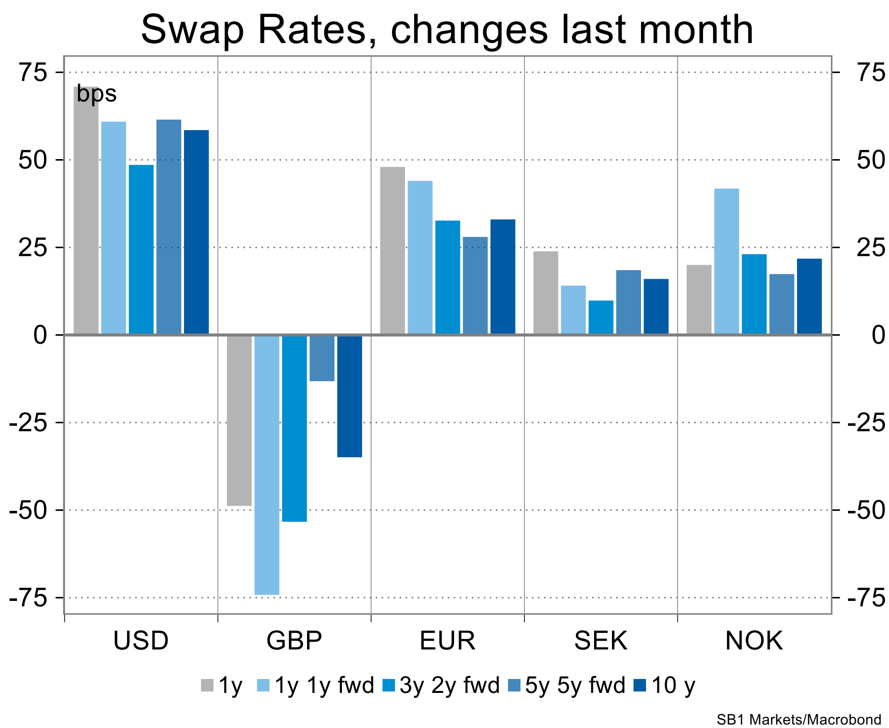


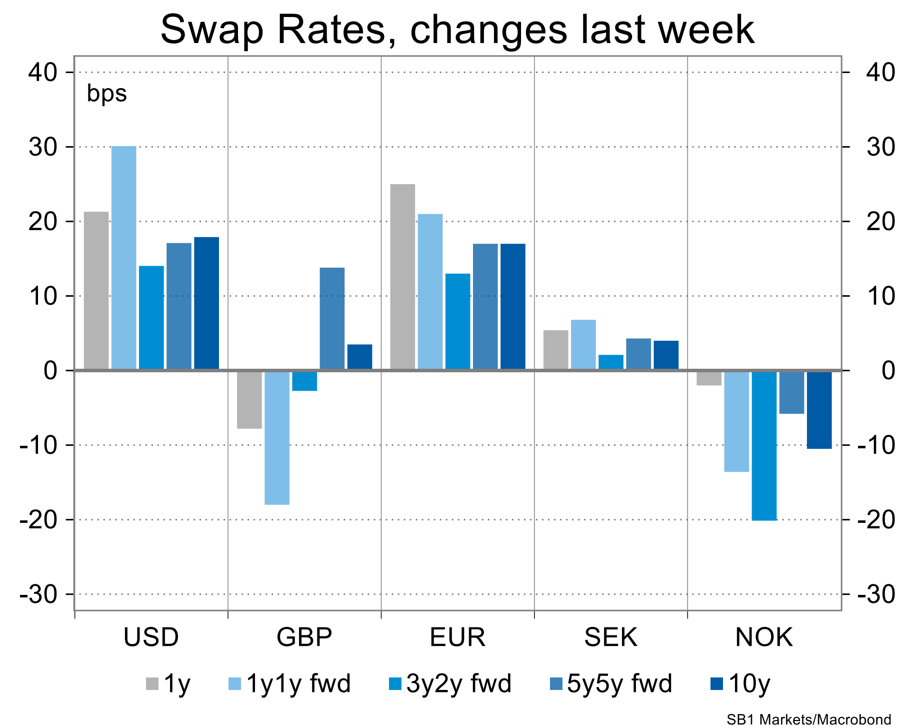




CHF: 10 y government bond yield

NOK rates down all over the curve, others mostly up

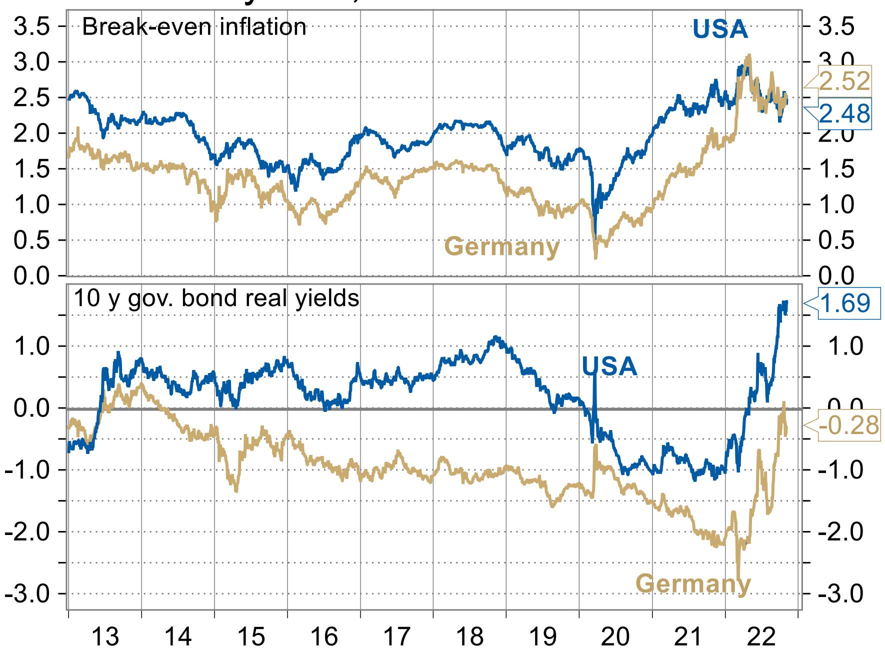




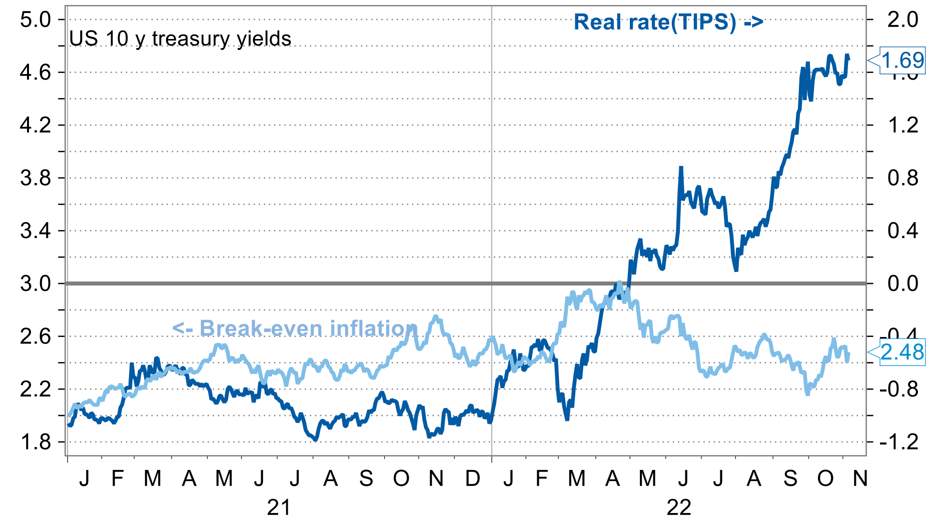
Real rates are flip-flopping, both in the US and in Germany – up last week

Inflation expectations marginally down

Real yields, break-even inflation



SB1 Markets/Macrobond



US & Germany 10 y Gov bond yield

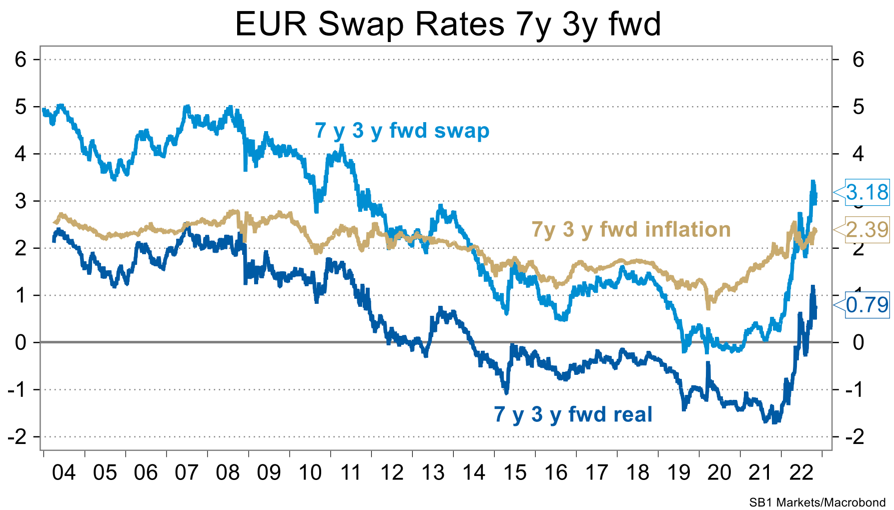
	Yield	Change 1w	Change 1m	YTD	Min since April-20
USA nominal treasury	4.17	0.15	0.55	2.65	0.52
.. break-even inflation	2.48	-0.03	0.24	-0.08	1.06
.. TIPS real rate	1.69	0.18	0.31	2.73	-1.19
Germany nominal bund	2.24	0.15	0.43	2.45	-0.65
.. break-even inflation	2.52	-0.03	0.27	0.63	0.40
.. real rate	-0.28	0.18	0.16	1.82	-2.80

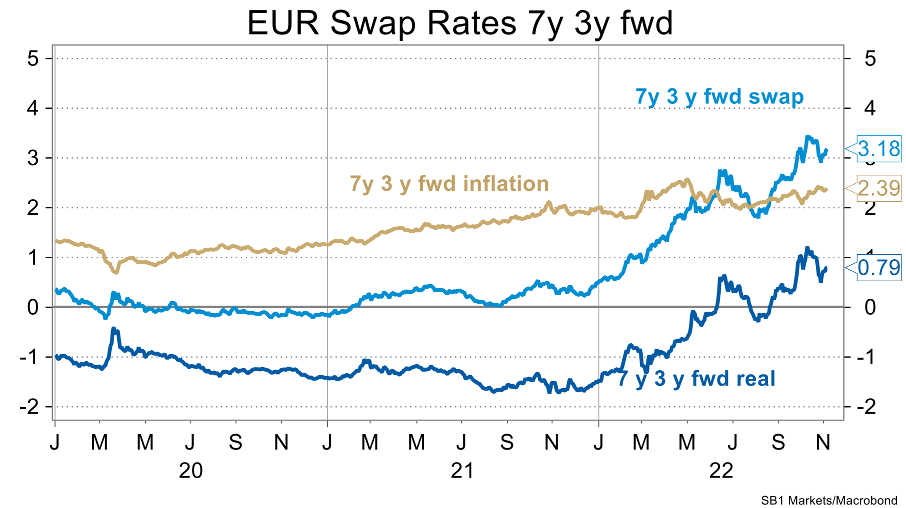
SB1 Markets/Macrobond

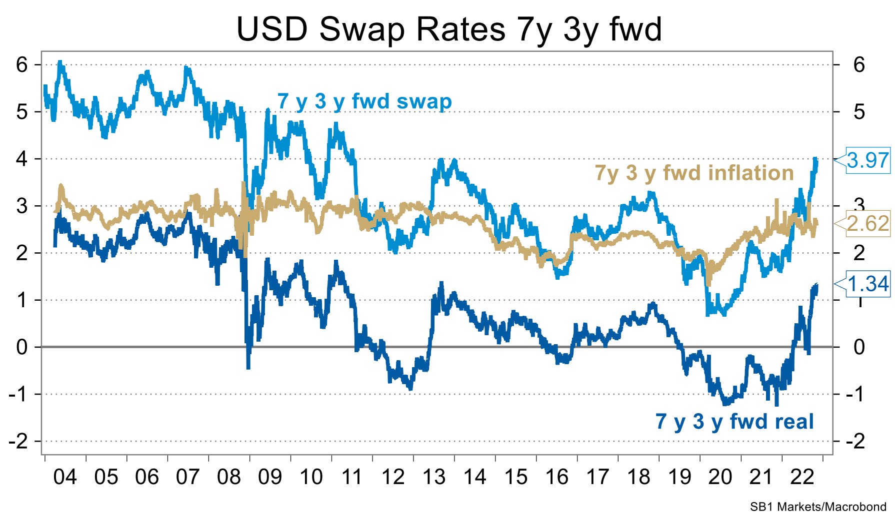
- The lift in real rates so far in 2022 is (still) one for the history books!
- No signs of war angst or flight to safety
- In the US, a 10 y CPI expectation at 2.48% is somewhat above Fed's 2% target for the PCE-deflator (which on average is some 0.3 pp below CPI inflation)

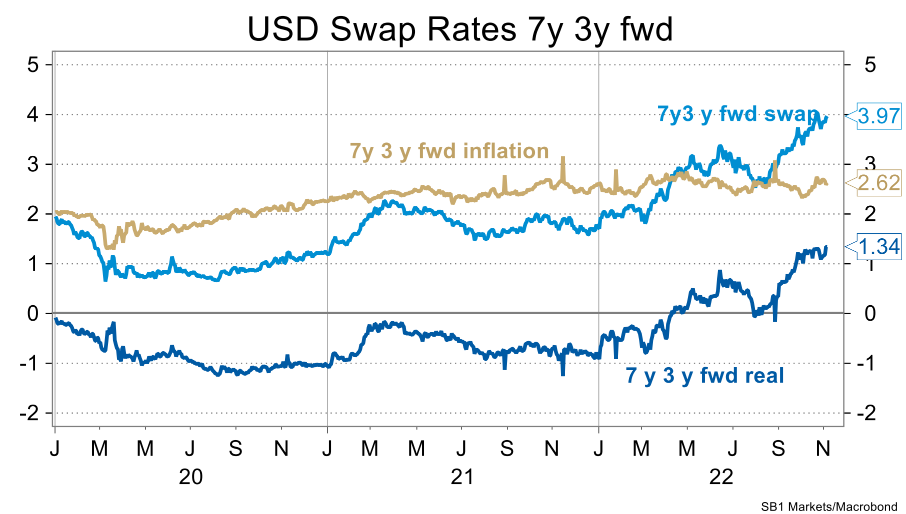
EUR real rates up, 'long term' +0.8% (measured via the swap marked)

Still below USD rates, but at least not that different!

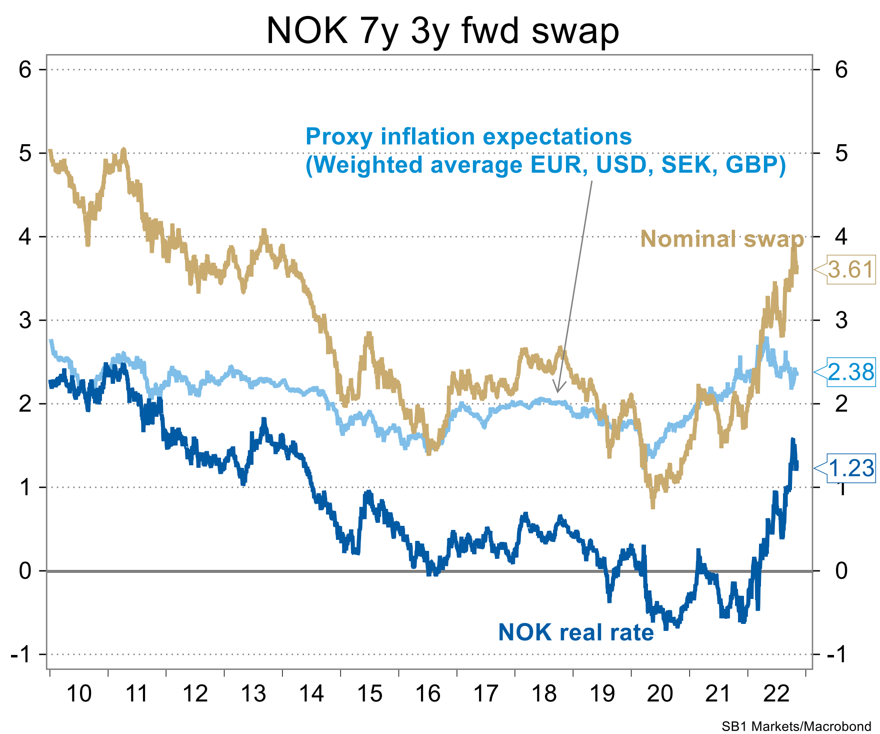


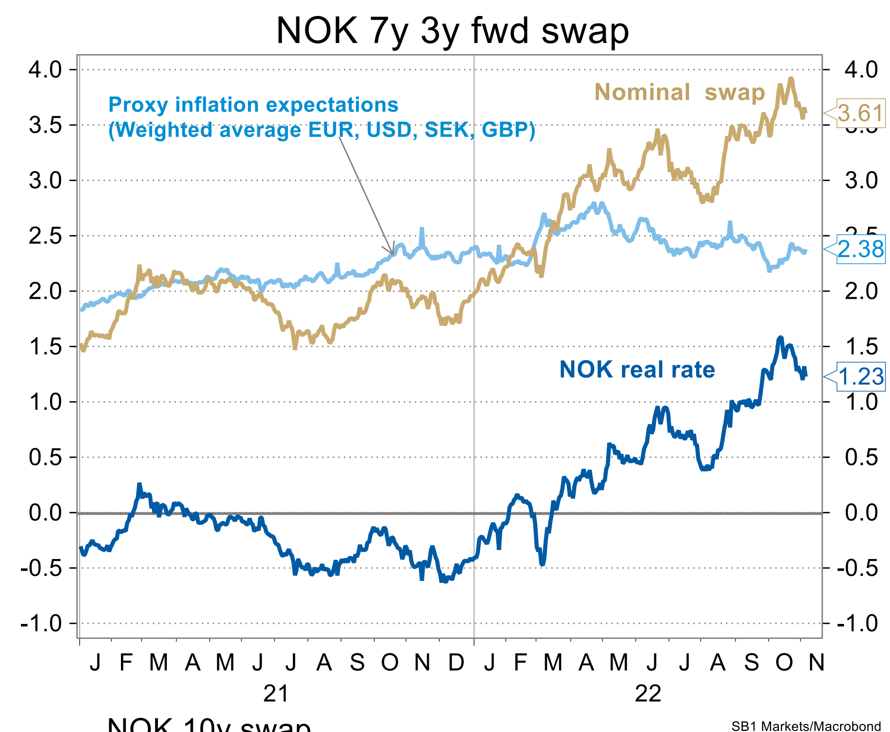


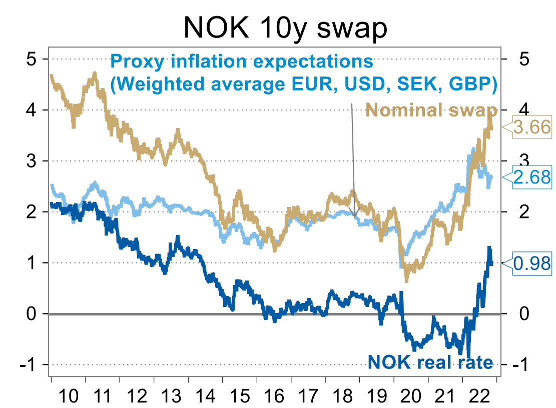




NOK real rates probably stable



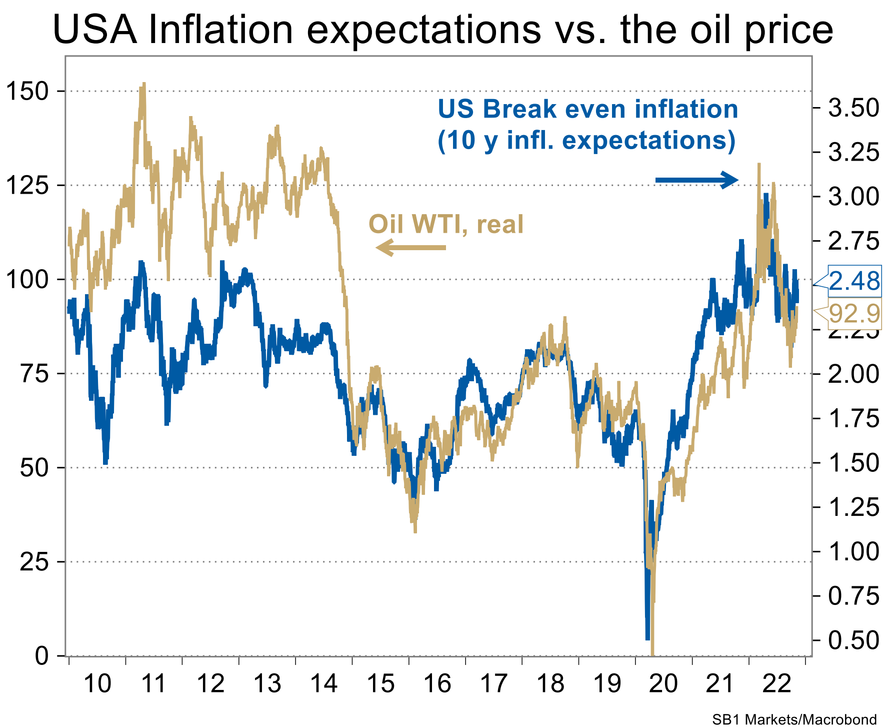


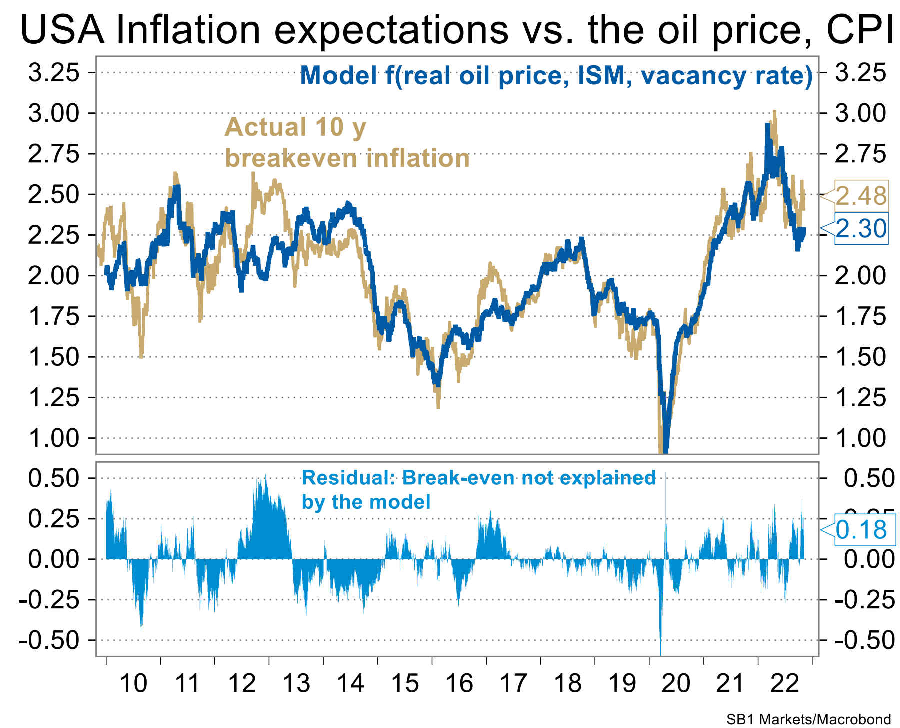


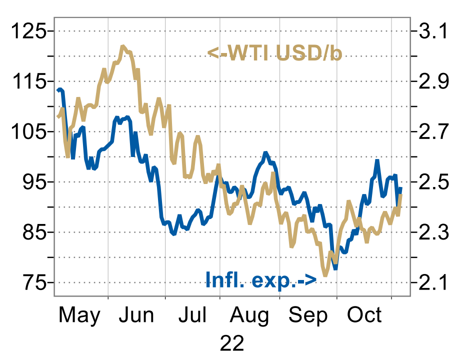
Memo: Our NOK inflation expectation proxy is a weighted average of EUR, SEK, GBP, and USD inflation swaps, cross-checked vs historical inflation differentials and inflation expectations from surveys

US inflation expectations down but still somewhat too high?

At least they are, vs our model estimate





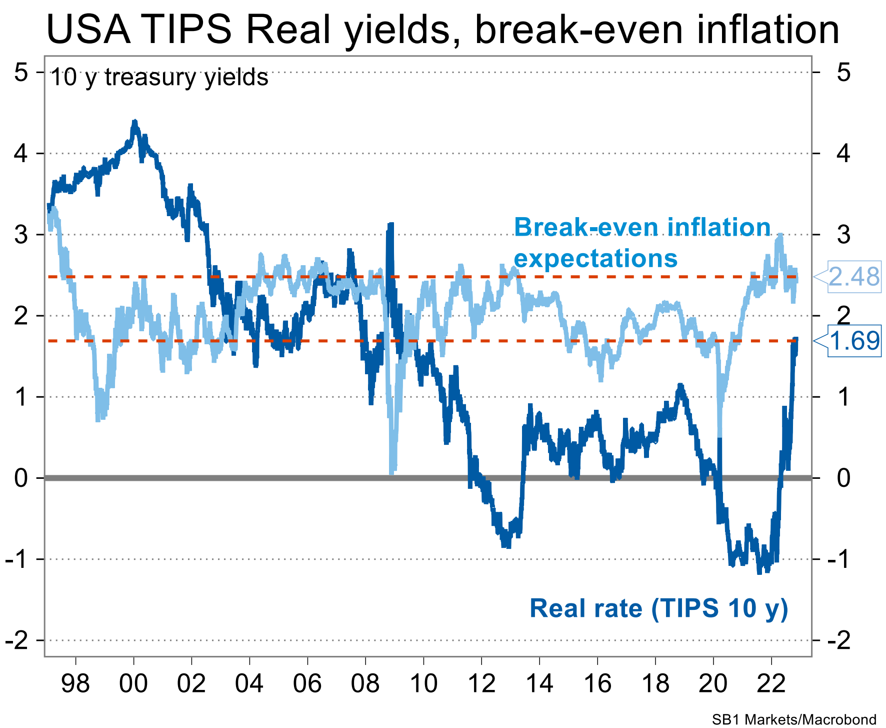


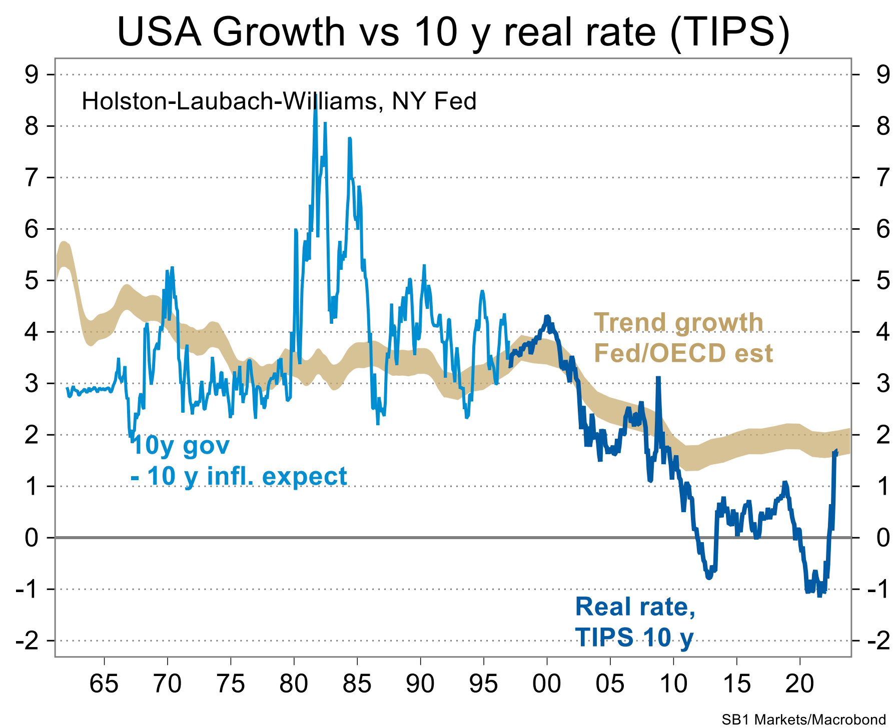
- A simple model including the <u>spot</u> oil price, the <u>current</u> ISM and the <u>current</u> vacancy rate pretty well explains the <u>long-term</u> breakeven inflation expectation in the bond yield curve
- What now? We are uncertain about the oil price, but rather confident that both the ISM, 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 3.2% from 6.2%): -36 bps
  - » - 10 USD/b: -10 bps

SpareBank 1 MARKETS

Growth vs real rates: The gap has closed!

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

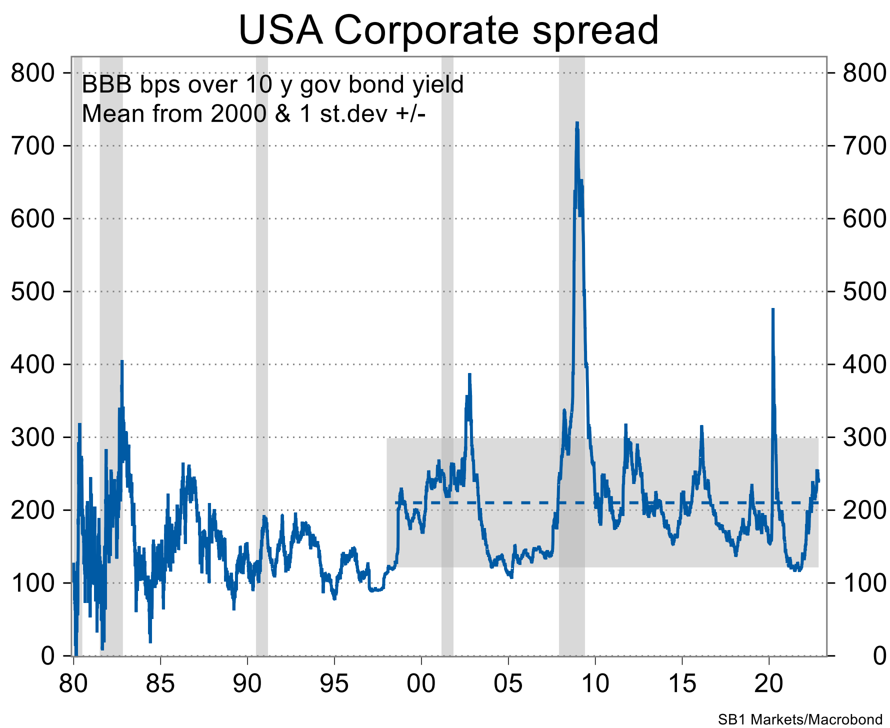


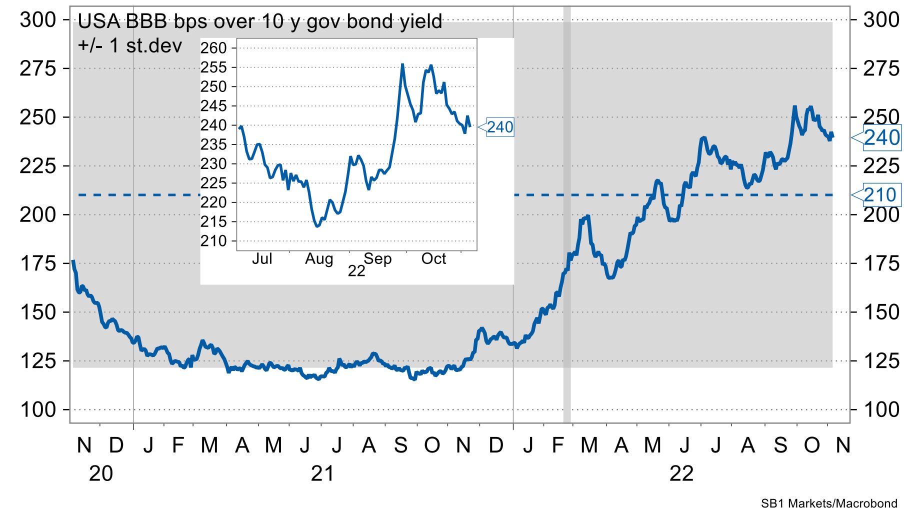


SpareBank 1 MARKETS

Risk on: Credit spreads unchanged last week, even if equity markets retreated

The trend is still up – and we expect more to come (because the economy will weaken)

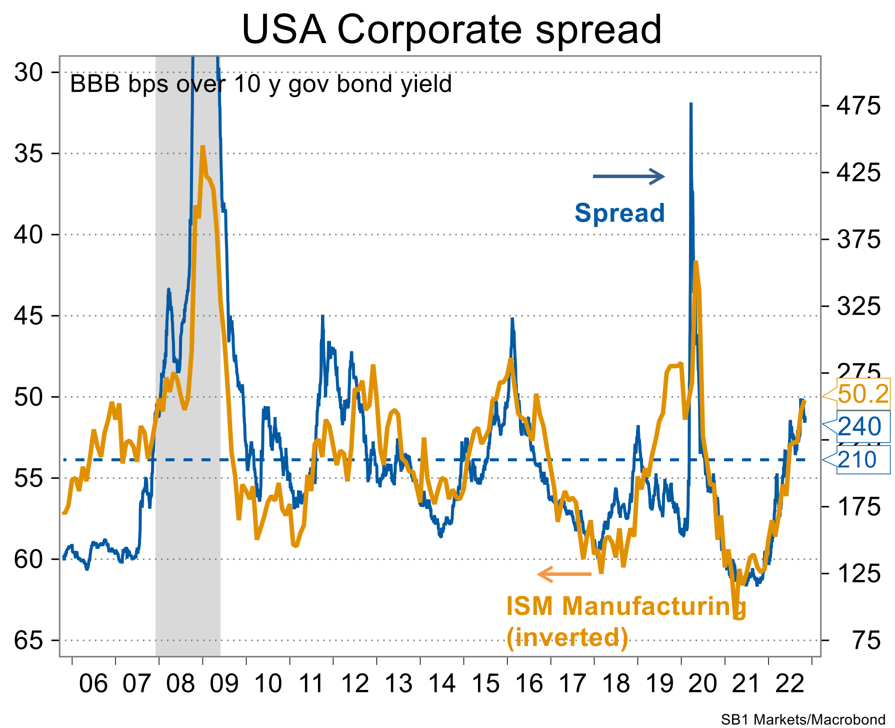


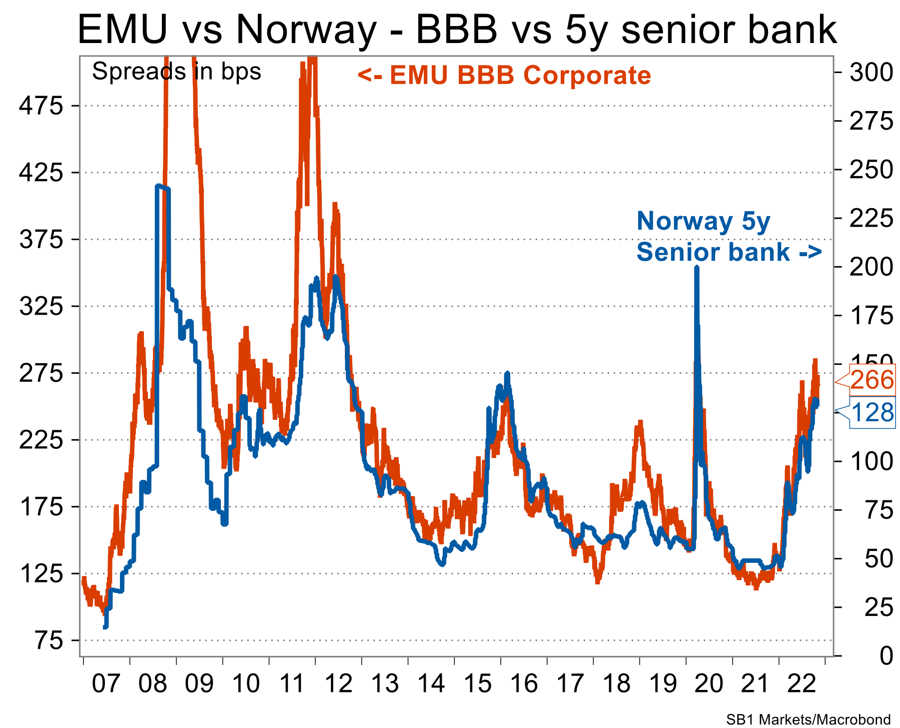


- The US BBB spread is up 120 bps from the bottom last autumn, more than a doubling
- In addition, real rates have increased by 270 bps from the bottom late last year
- Thus, the basis for all valuation metrics has changed dramatically, check the chart two pages forward!

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 55 in some few months time? We are quite sure…



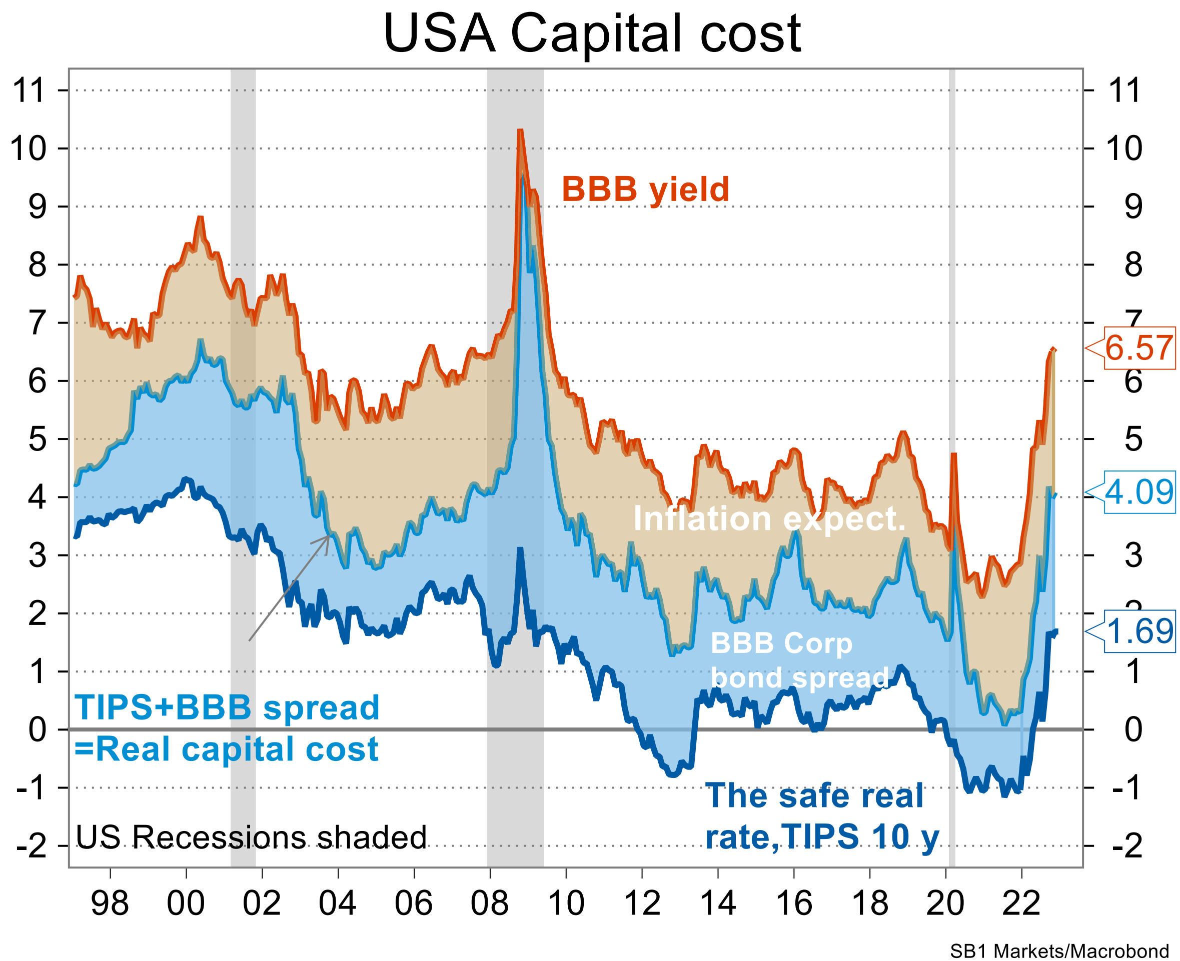


- The answer is not irrelevant for your view on the outlook for spreads, we think
- And do you think Norwegian spreads will be influenced by changes in the global credit market?
- Last week: Norwegian credit spreads rose in sympathy with higher spreads abroad the previous week
- The good news: The recent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

SpareBank 1 MARKETS

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

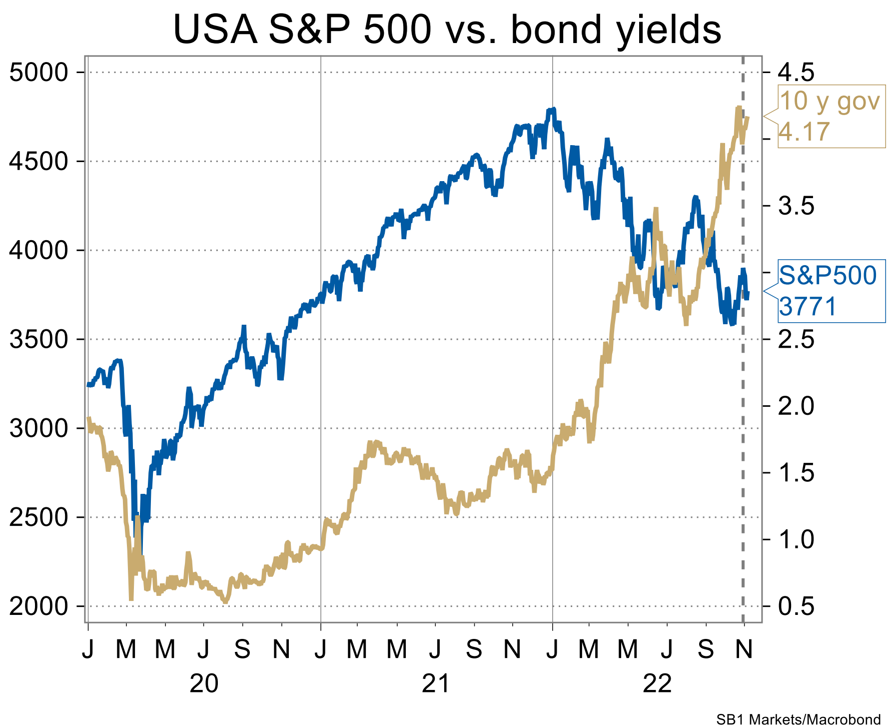
All valuation metrics have changed dramatically. *As have all calculations of return on capital*

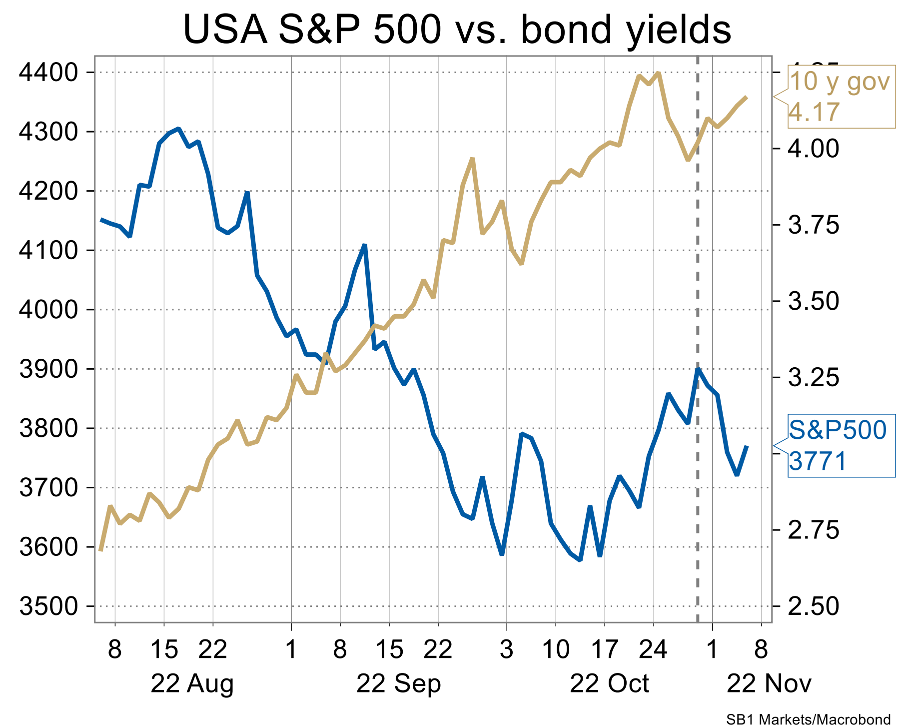


- Spreads and real rates fell last week but the story remains intact
- The total real borrowing cost for a BBB company has increased to 3.9% bps from zero by the end of last year:
  - » The TIPS real rate is up from -100 to + 170 bps
  - » The BBB corporate investment grade spread is up from 120 bps to 240!
- Add on modest inflation expectations, the nominal borrowing cost has increase from well below 3% to above 6.4% (though down from 6.7% at the local peak two weeks ago)

Equity markets surprised by the Federal Reserve. Not so much the bond market

The 10 y bond yield still up 15 bps, the S&P500 lost 3.3% (Nasdaq -6.6%)



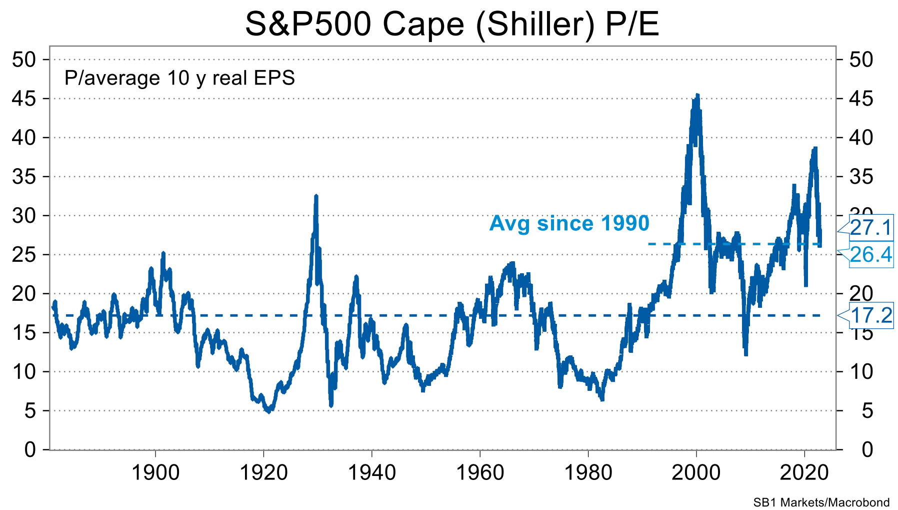


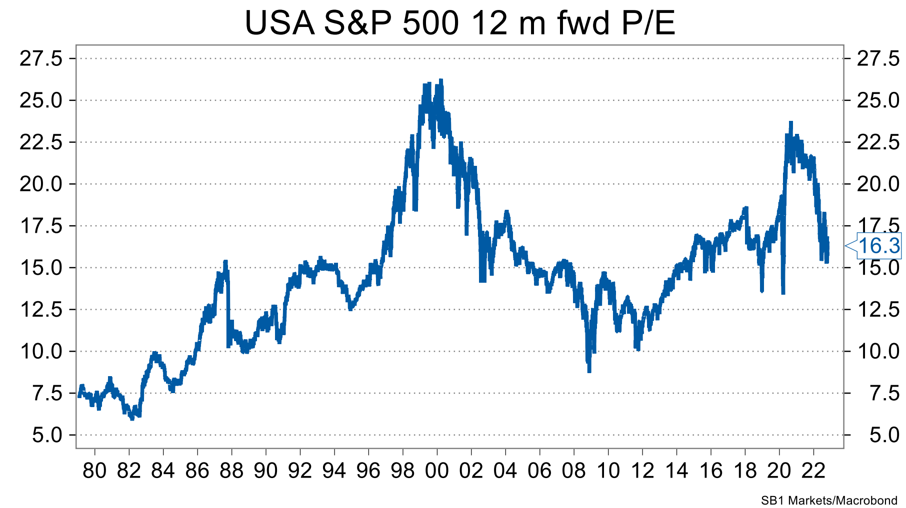
- Bond volatility has surged recent weeks/months, to levels not seen in 15 years. 'Something' is going on

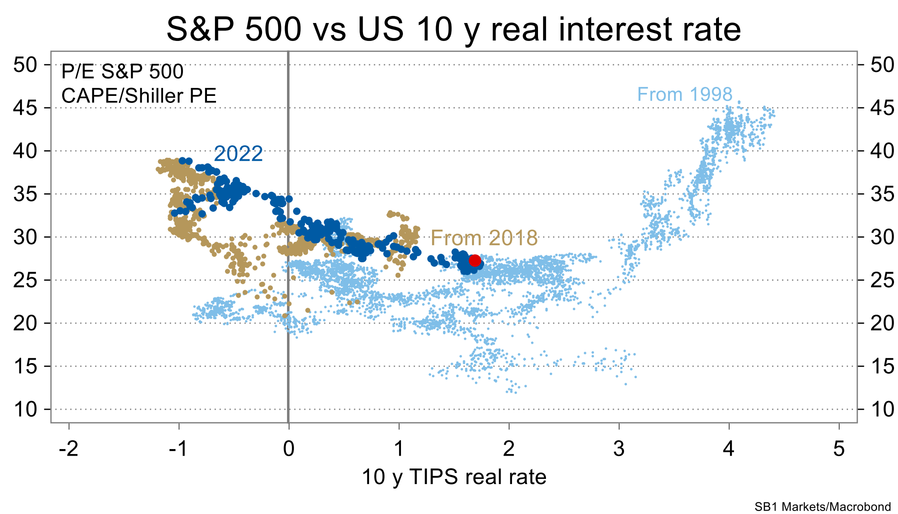
SpareBank 1 MARKETS

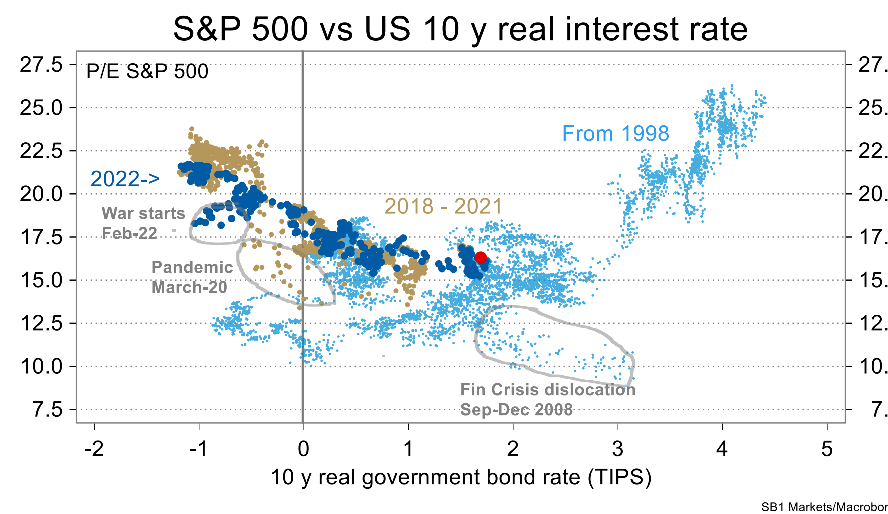
4 valuation charts: Check the extreme tight correlation between real rates, P/E

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







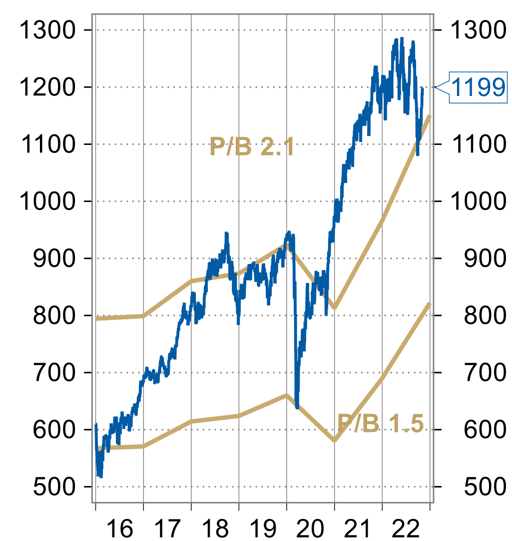


SpareBank 1 MARKETS

The OSEBX up to a Price/Book at 2.24

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

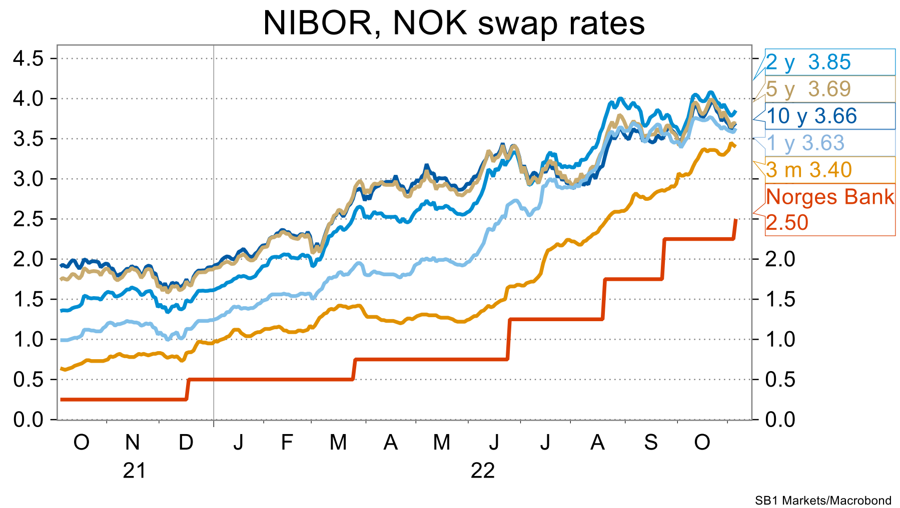
Source: Oslo Børs, Vital, Bloomberg, SB1 Markets, Macrobond.

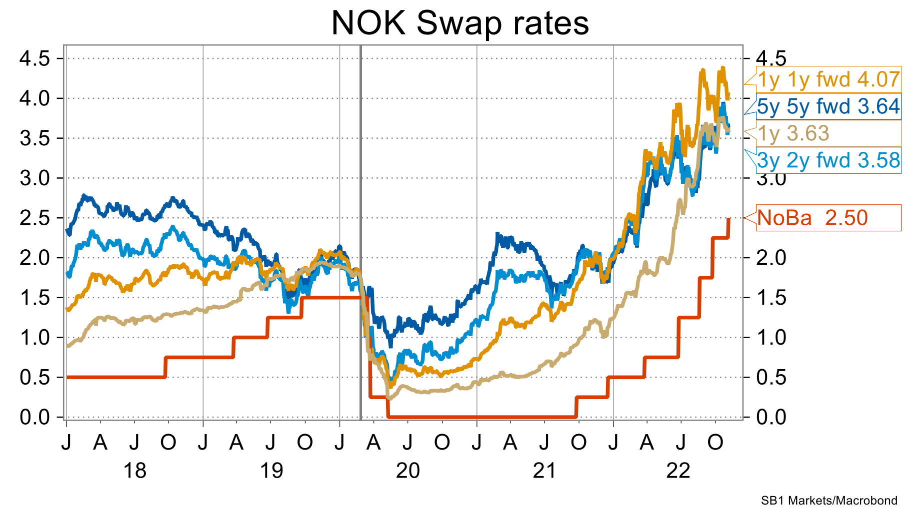


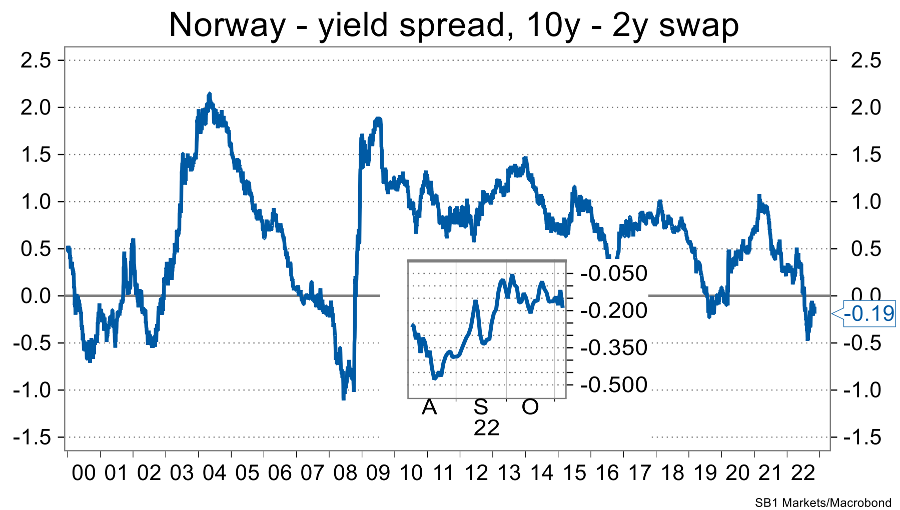
Source: Oslo Børs, Vital, Bloomberg, SB1 Markets, Macrobond.

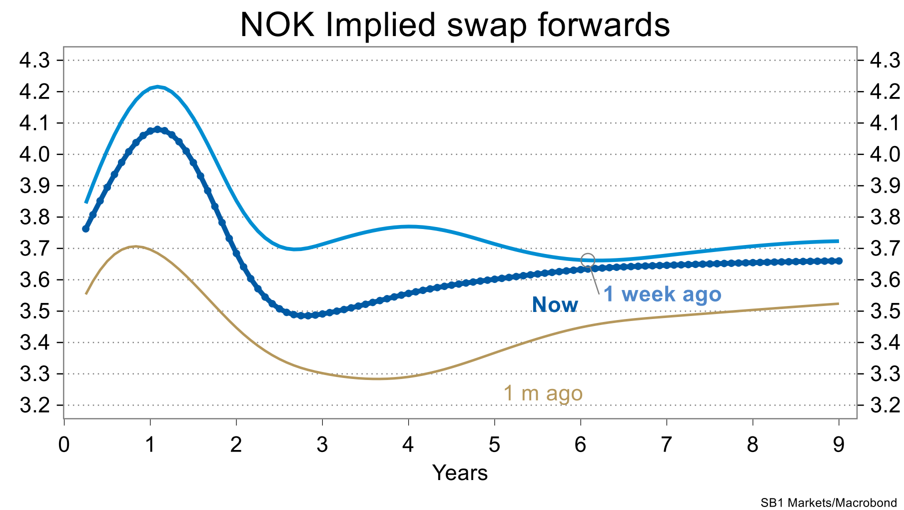
Norwegian swaps down all over the curve, most the 2 – 4 year segment

The 3m NIBOR up 10 bp to 3.40%, even if NoBa hiked just 25 bps. However, FRA rates declined



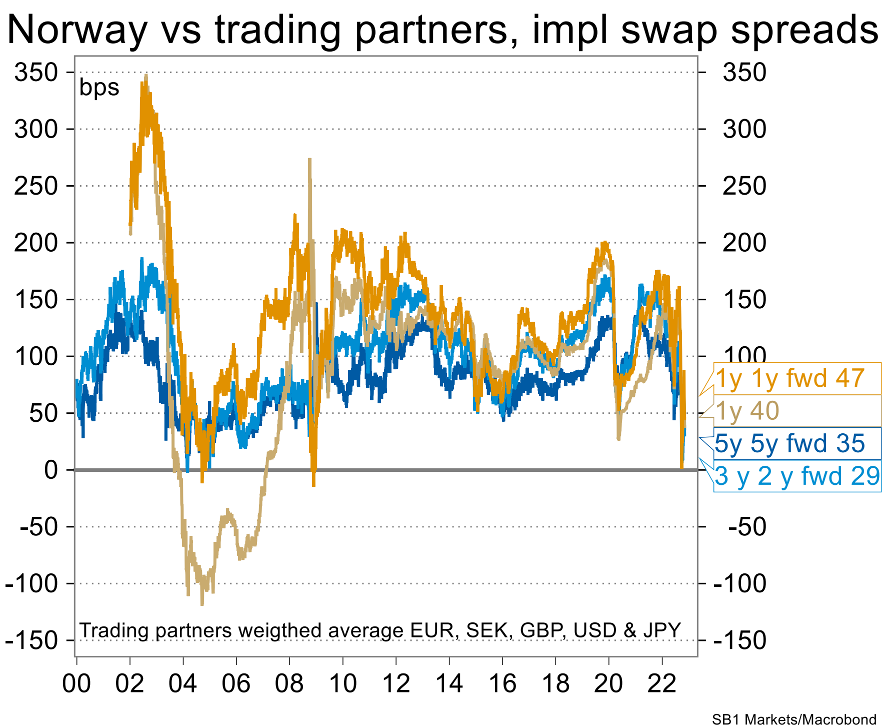


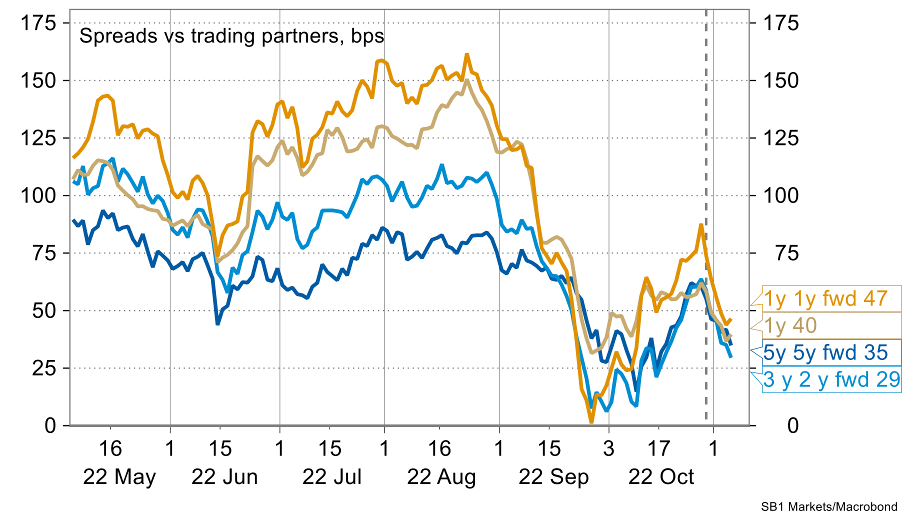


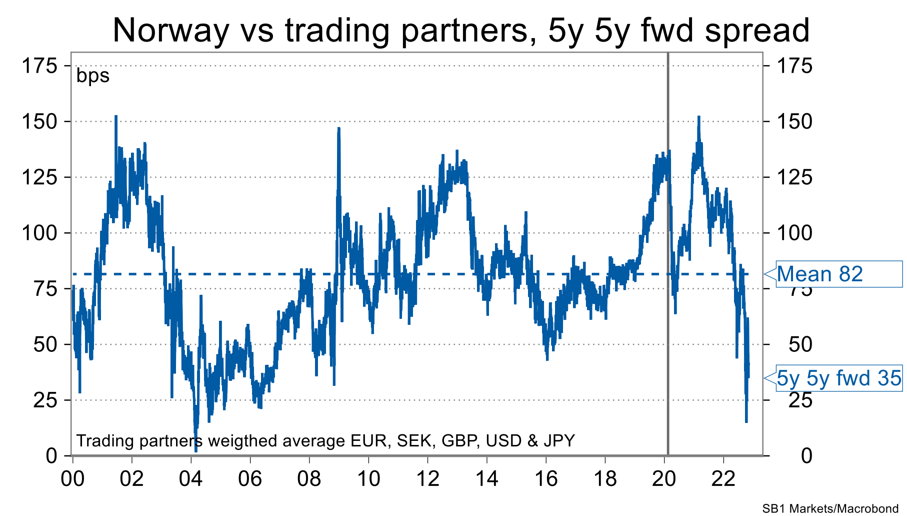


NOK rate spreads vs our trading partners, narrowed last week

Spreads are becoming too narrow? At least not much potential at the downside (barring a housing collapse)



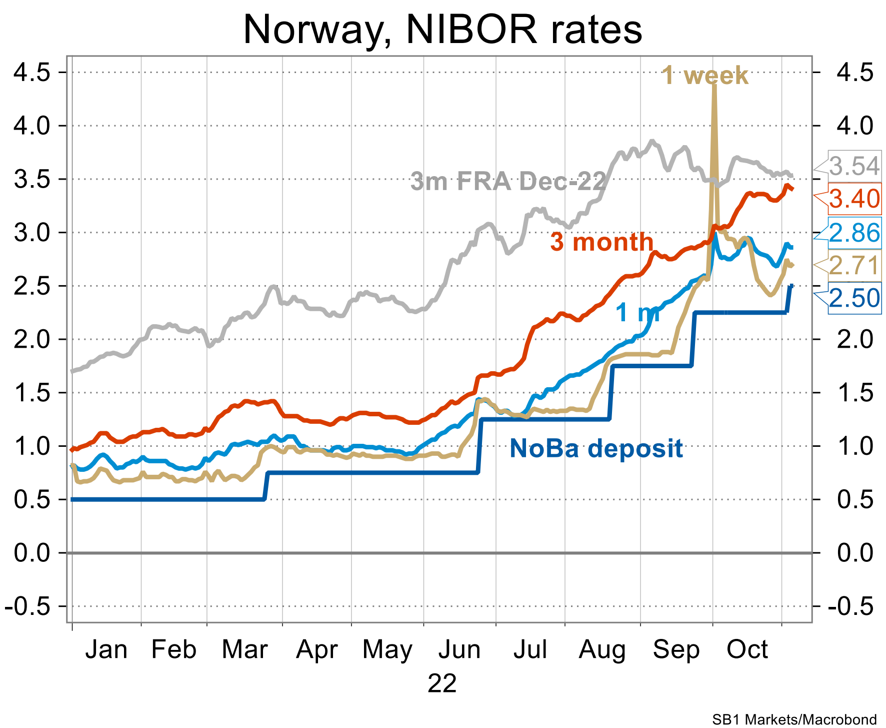


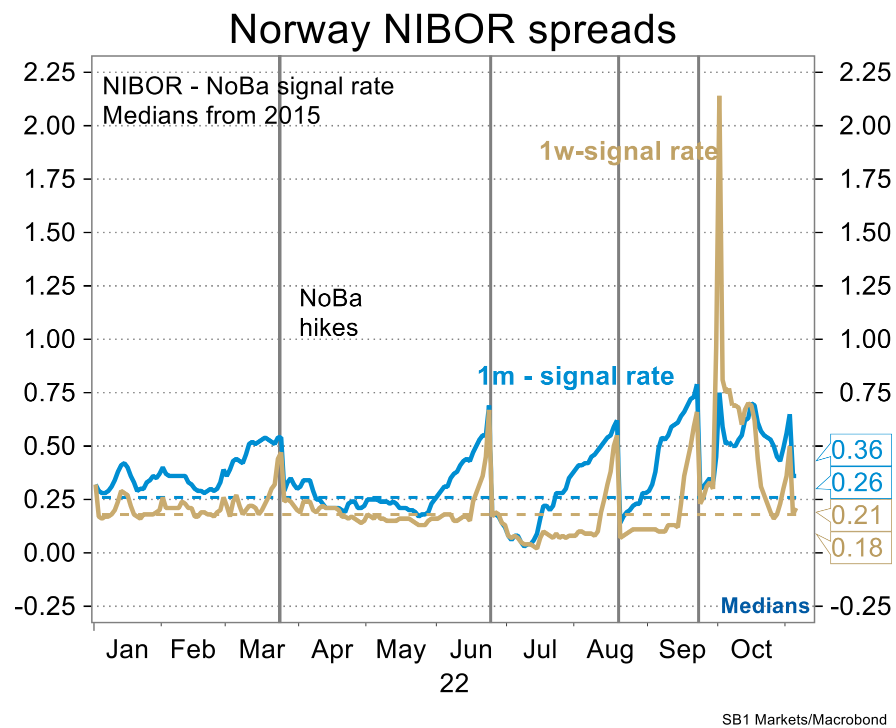


- NOK rates are still st the average level among our trading partners
- We assume spreads now should be far lower than the historical average. The main downside risk: A much weaker Norwegian housing market

NIBOR spreads a tad higher than normal again, even if the 1 m rate fell

Market rates fell less than we expected following the 25-bps hike

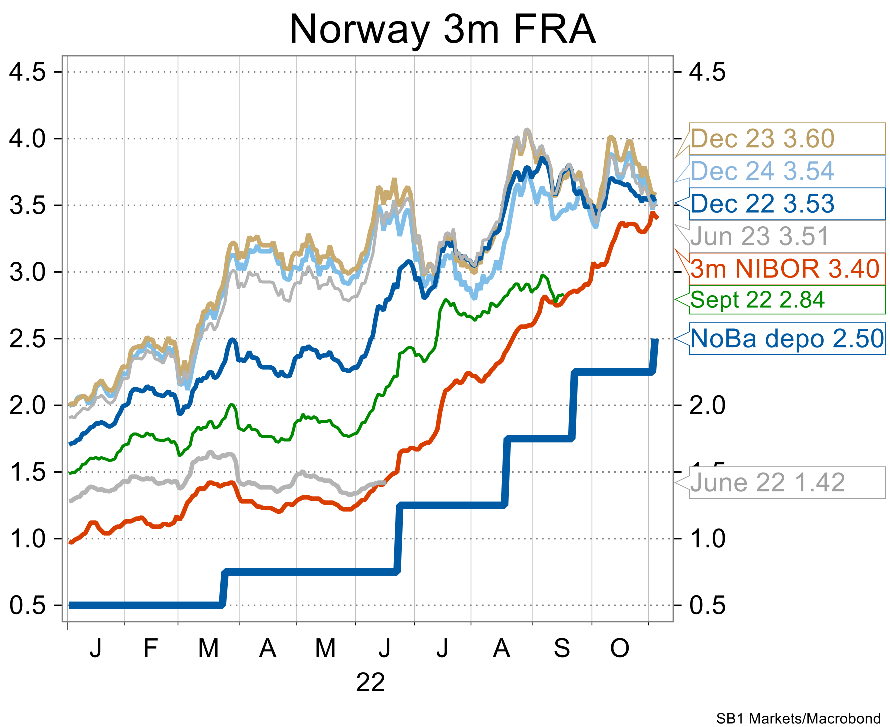


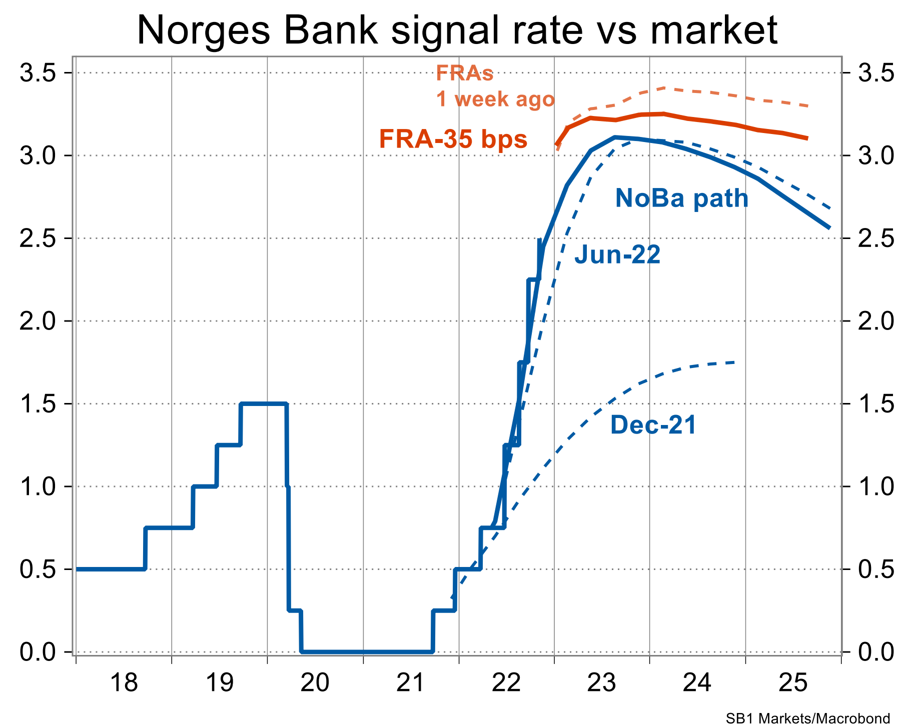


SpareBank 1 MARKETS

FRAs down 2 – 20 bps, most in the long end, we expected more in the short end

The current 3.40% NIBOR and Dec-23 at 3.53% imply high NIBOR spreads the coming months



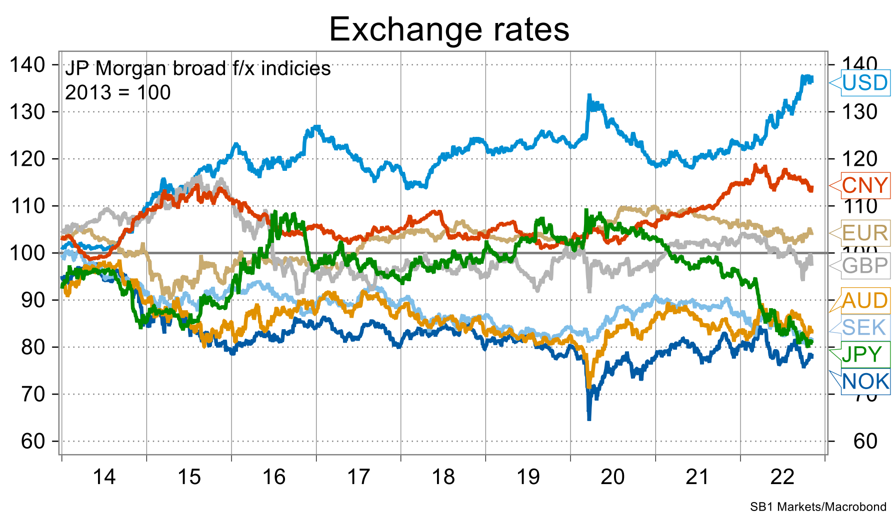


- The current 3 m NIBOR at 3.40% and the Dec-22 3 m FRA at 3.53% (up 10 bps, down 3 bps resp.) are 90 and 103 bps above the current signal rate. Even if NoBa hikes by 50 bps in December, which we think is not very likely, the NIBOR spread will be far above a 'normal' 35 bps

SpareBank 1 MARKETS

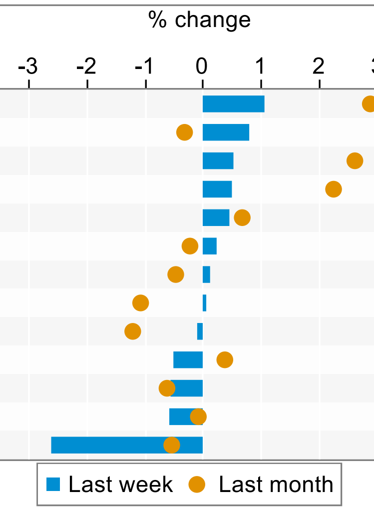
NOK close to the top of the list last week too, the CNY also recovered

The GBP fell sharply. Yields turned south, as BoE said rate expectations were too aggressive



F/x markets

JP Morgan f/x broad indices + 3 f/x crosses	Last week	Last month
NOKEUR	1.1	2.9
CNY	0.8	-0.3
NOK	0.5	2.6
NOKUSD	0.5	2.2
CAD	0.5	0.7
SEK	0.2	-0.2
AUD	0.1	-0.5
CHF	0.1	-1.1
JPY	-0.1	-1.2
USD	-0.5	0.4
EURUSD	-0.6	-0.6
EUR	-0.6	-0.1
GBP	-2.6	-0.5

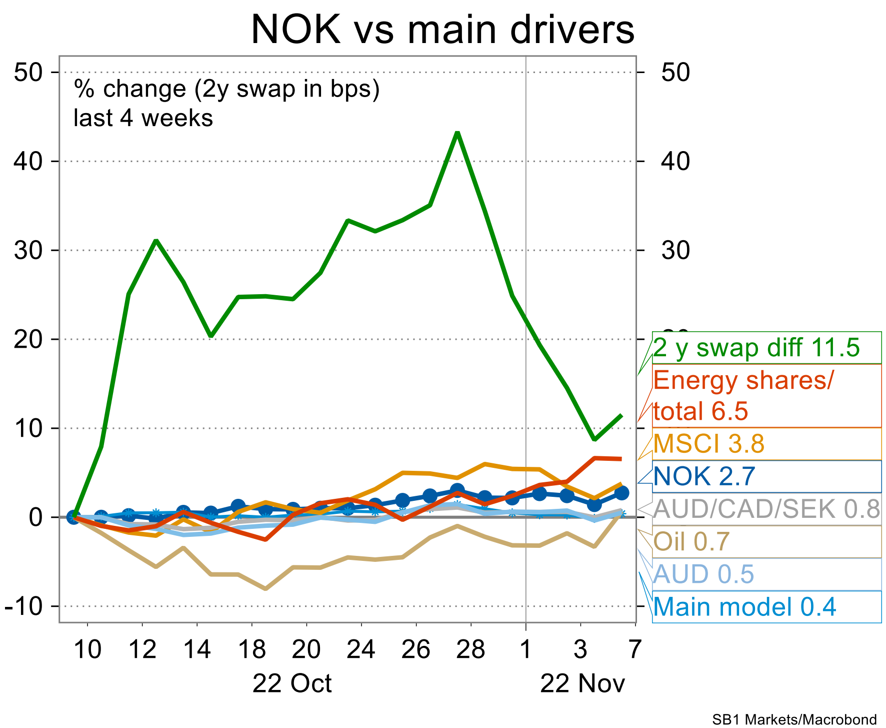


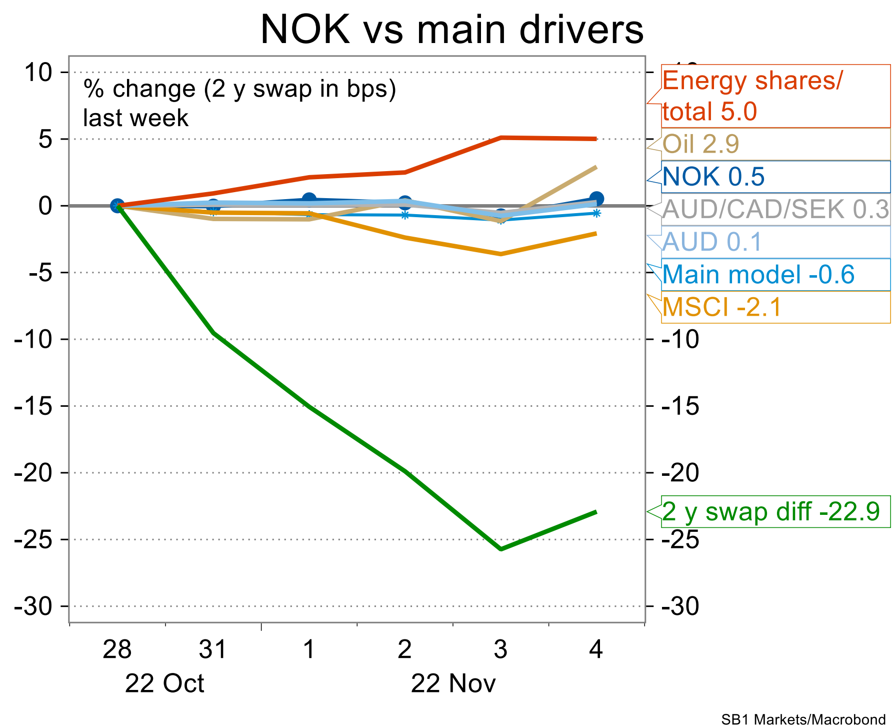
SB1 Markets/Macrobond

SpareBank 1 MARKETS

NOK up 0.5%, supported by… just the oil price? Our model signalled -0.6%

The NOK is in line with the model estimate



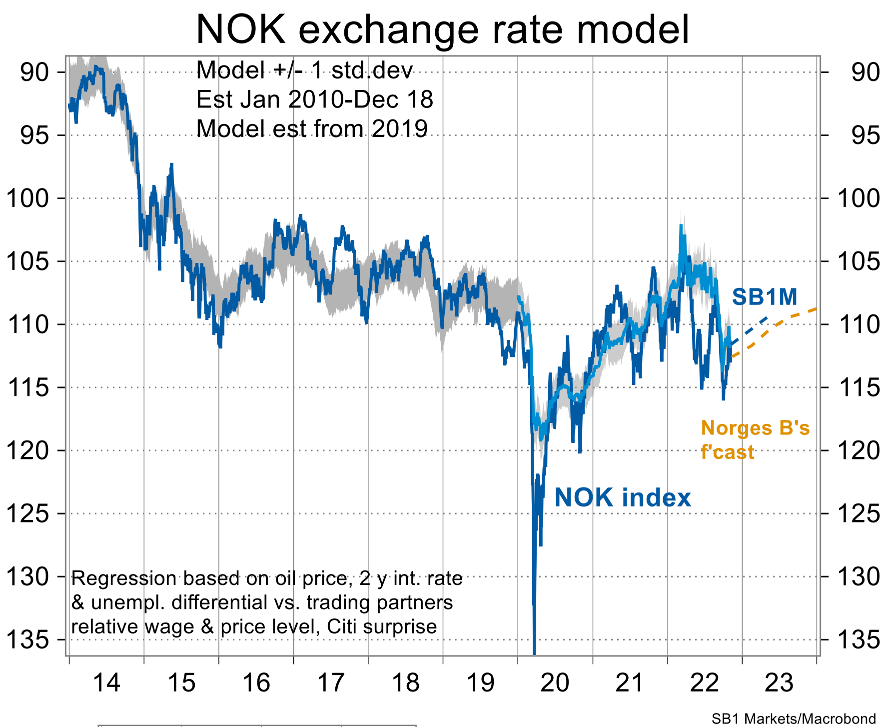


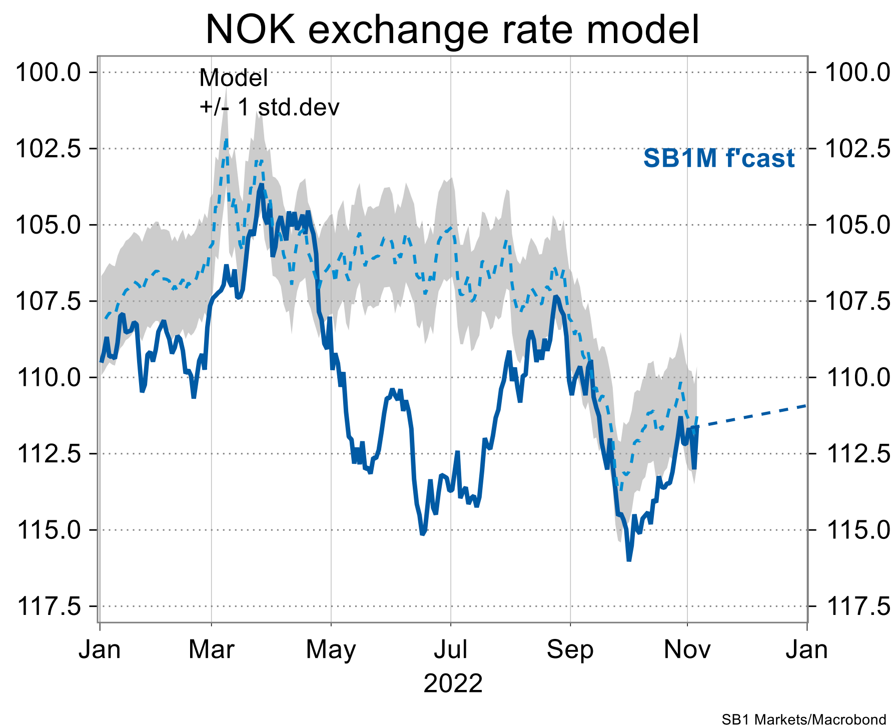
Gaps vs. our model estimates narrowed further last week

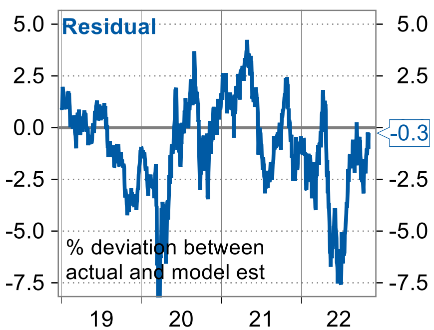
- ***NOK is 0.3% <u>below</u> our main model estimate (from -1.3%)***
- The NOK is 6% <u>weaker</u> than our AUD/CAD/SEK-model, our 'super-cycle peers', predicts, a substantial weakening (unch)
- NOK is 4% weaker than an estimate from a model that includes global energy companies equity prices (vs the global stock market) (unch)

At this and the following pages we have swapped Norges Bank's I44 index for JP Morgan's broad NOK index and rebased it to the current index value for the I44. The I44 has an earlier closing time than the 'official' closing time for f/x crosses. There are no substantial difference between these two indices over time

The NOK is just 0.3% below the model estimate

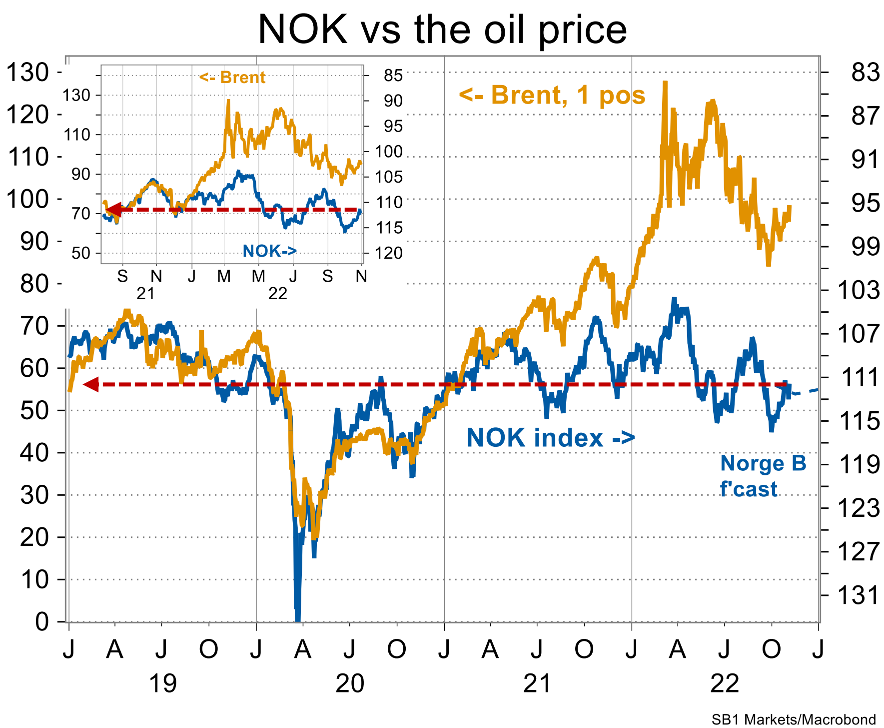


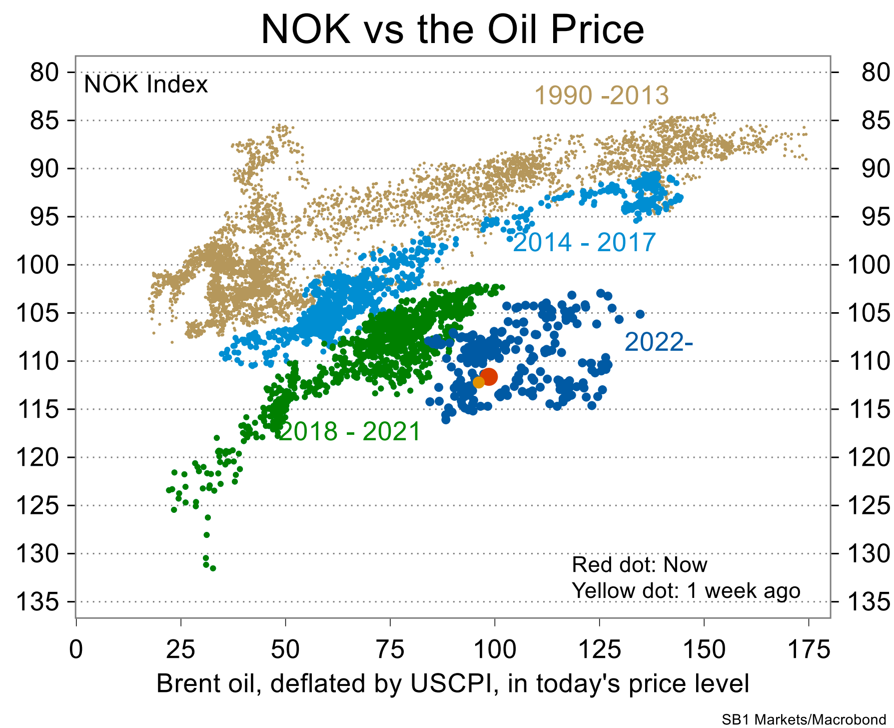




Oil up 2.9% last week, NOK up too

The ‘gap’ vs the oil price has narrowed somewhat recently

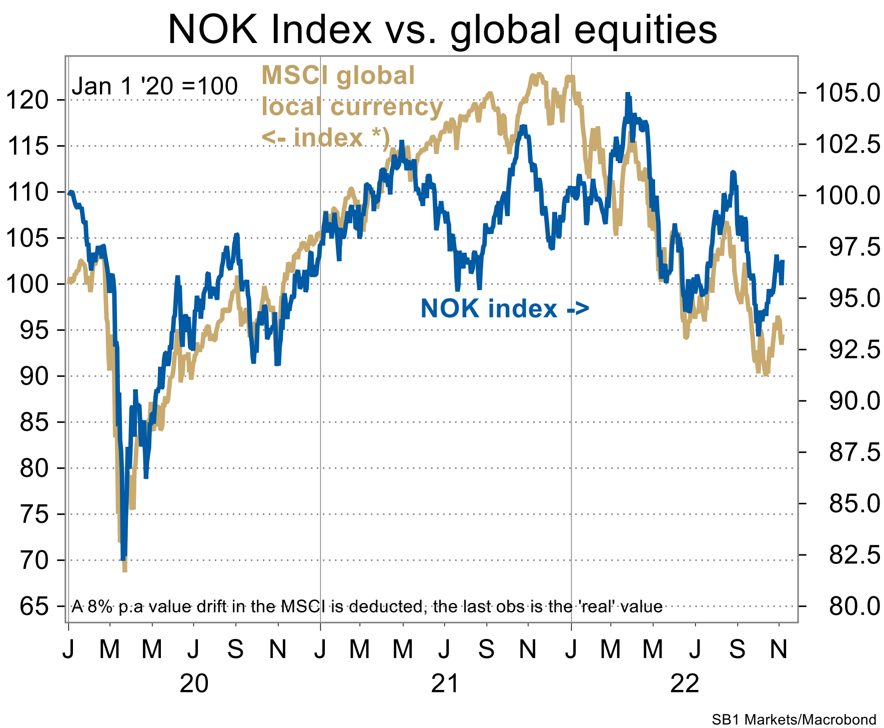


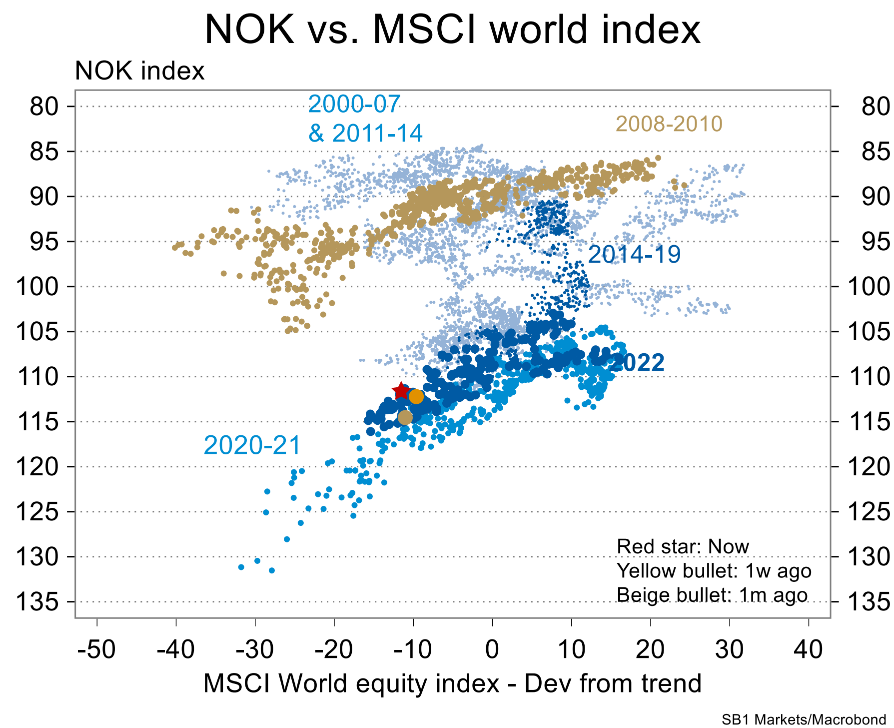


- The correlation between the NOK and the oil price has been close to non-existent since the start of 2022, rather unusual

The NOK up even if the global stock market declined

The NOK has been closely in sync with the global stock market since April

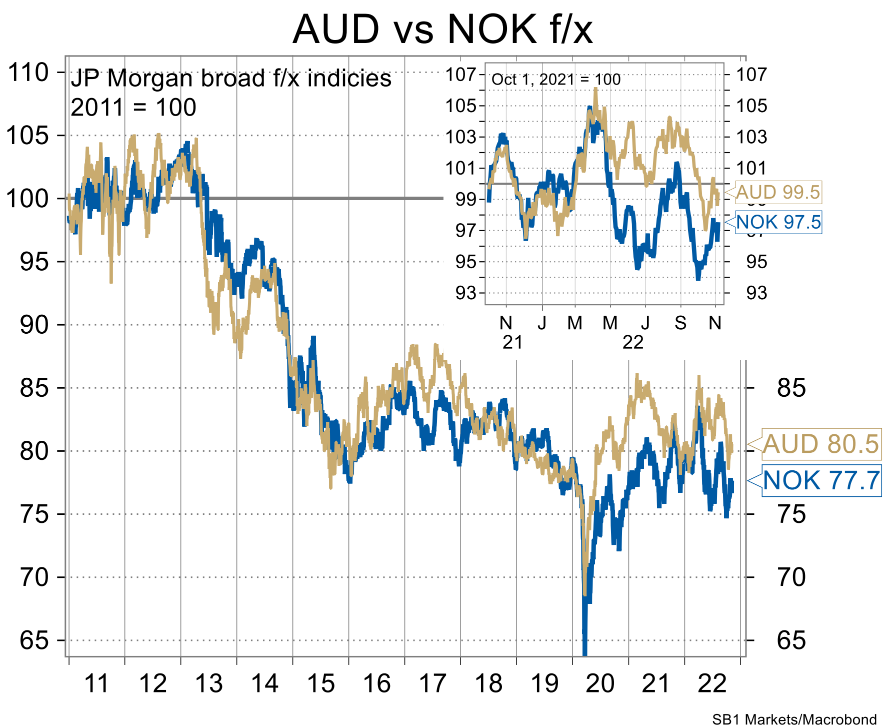


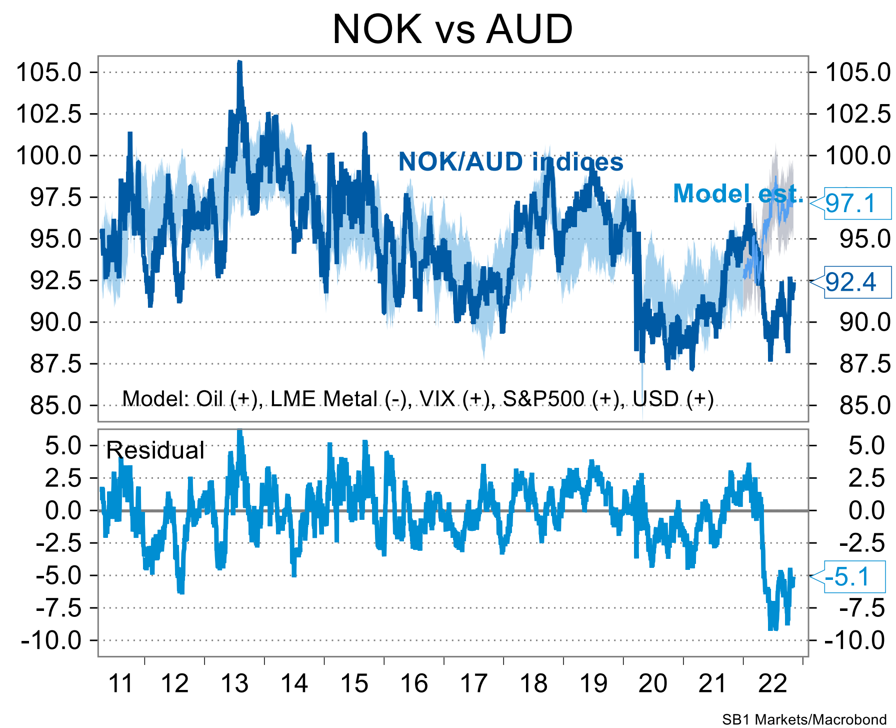


- However, has not been any stable correlation over time, and when it is, the oil price is normally the real driver. Not so much now

Both the AUD and NOK up last week – NOK is still lagging

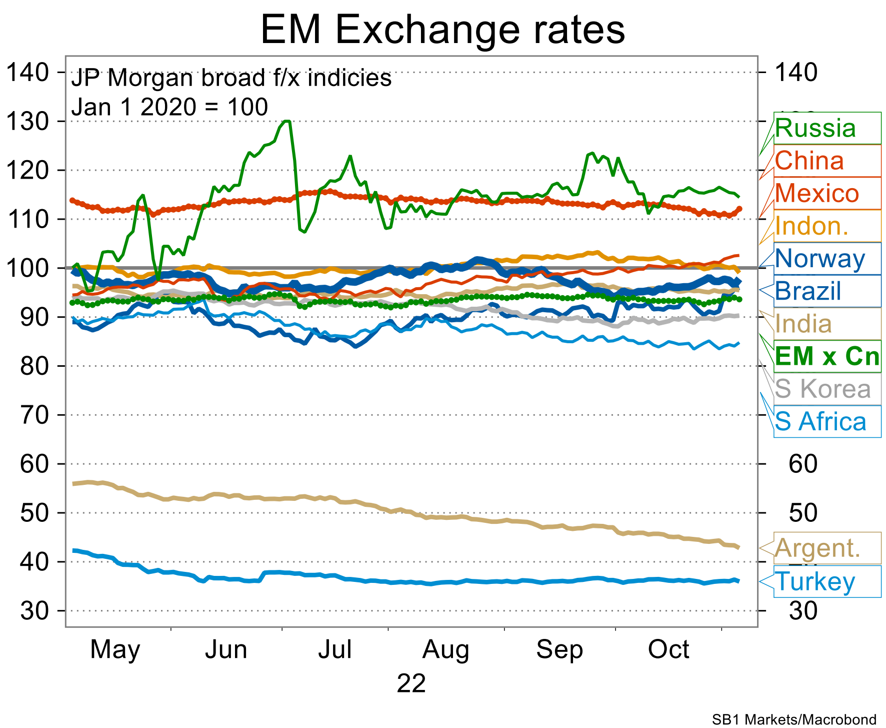
NOK is 5.1 % below our model f'cast vs AUD

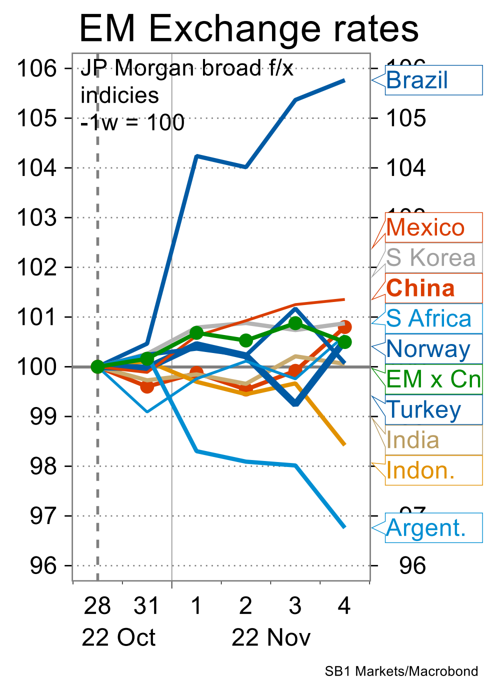


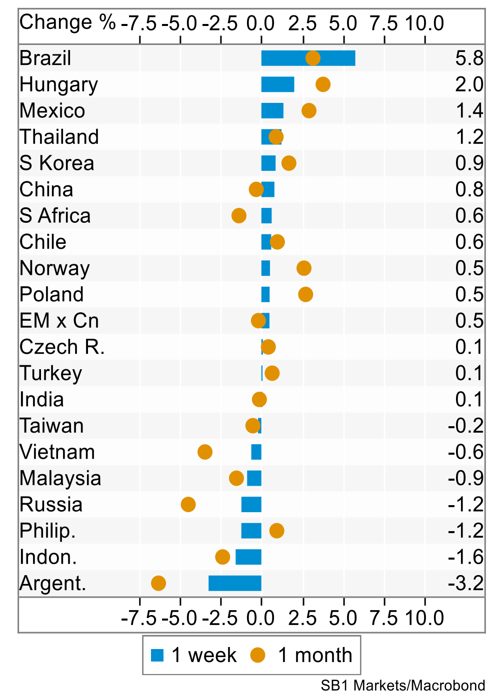


- The discrepancy between the NOK and AUD is unusual, given the normal factors that normally has explained the limited gap between the two
- Normally, NOK strengthens vs the AUD when the oil price rises vs. the LME metal index, when VIX, and the S&P500 index increases, and the USD index appreciates.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

EM f/x (x China) in sum up last week







- The CNY has been slightly on the weak side recent weeks, and fell by 0.7% last week

DISCLAIMER

SpareBank 1 Markets AS ("SB1 Markets")

This report originates from SB1 Markets' research department. SB1 Markets is a limited liability company subject to the supervision of The Financial Supervisory Authority of Norway (Finanstilsynet). SB1 Markets complies with the standards issued by the Norwegian Securities Dealers Association (VPFF) and the Norwegian Society of Financial Analysts.

No investment recommendation

Any views and opinions relating to securities mentioned in this report should be interpreted as general market commentary, and not as investment recommendations within the meaning of section 3-10 of the Norwegian Securities Trading Act.

No personal recommendation

The information contained in this publication is general and should not be construed as a personal recommendation within the meaning of the Norwegian Securities Trading Act, section 2-4. It does not provide individually tailored investment advice regarding a particular financial situation, investment experience, risk profile or preferences of the persons who may receive this report. For tailored investment advice regarding stocks mentioned in this publication, please consult our brokerage desk or your individual investment advisor.

Research for the purposes of unbundling

This report is deemed to constitute a minor non-monetary benefit for the purposes of the inducement rules under MiFID II. The report is publicly available on our website (no log-in required).

Conflicts of interest

SB1 Markets, affiliates and staff may perform services for, solicit business from, hold long or short positions in, or otherwise be interested in the investments (including derivatives) in any stock mentioned in this publication. To mitigate possible conflicts of interest and counter the abuse of confidential information and insider knowledge, SB1 Markets has set up effective information barriers between divisions in possession of material, non-public information and other divisions of the firm. Our research team is well versed in the handling of confidential information and unpublished research material, contact with other divisions, and restrictions on personal account dealing. The views expressed in this report accurately reflect the analyst's personal views about the companies and the securities that are subject of the report, and no part of the research analyst's compensation is related to the specific recommendations or views expressed in this report.

Accuracy of sources

All opinions and statements in this publication are, regardless of source, given in good faith, and may only be valid as of the stated date of this publication and may be subject to change without notice. SB1 Markets has taken all reasonable steps to ensure that the information contained in this report is true and not misleading. Notwithstanding such efforts, we make no guarantee as to its accuracy or completeness.

Risk information

Return on investments is inherently exposed to risks. The value of an investment position may both rise and fall during the investment period. If the return on investments is positive at one time, there is no guarantee that it will remain such in future. In certain cases, losses may exceed the sum of the original investment.

Limitation of liability

Any use of information contained in this report is at your own individual risk. SB1 Markets assumes no liability for any losses caused by relaying on the information contained in this report, including investment decision taken on the basis of this report.

Limitation on distribution

This publication is not intended for, and must not be distributed to, individuals or entities in jurisdictions where such distribution is unlawful.