October 31, 2022

Macro Weekly

Week 44

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Last week, I

- **The War/European Energy/Commodities**
  - » Russia has withdrawn form deal regarding **export of grain from Ukraine** – after the attack at the military Crimean harbour
  - » **Most commodity prices** fell last week, but **oil prices** rose further. **Irone ore** prices fell sharply due to less hope for a recovery in the Chinese construction sector
- **Preliminary October DM PMIs**
  - » Down, down, both in Europe and the US, and the main DMs x Japan report composite PMIs below 50. We estimate a 1 p drop in the global composite PMI to 48.7. Manufacturing orders are plunging everywhere, no doubt due to weaker domestic demand most places. The delivery times indices are falling rapidly, and price indices are declining but remain at well above normal levels
- **USA**
  - » **GDP** rebounded at tad better than expected in Q3, up 2.6% (annualised). Even so, GDP is up just 0.3% from Q4 last year, as activity fell at 1.1% pace in H1. The lift was entirely due to a 3.2% of GDP cut in the trade deficit, as exports rose while imports finally yielded, from a very high level. Growth in private domestic demand slowed further, to 0.6% in Q3, even if household consumption surprised on the upside. Housing investments nosedived, and deducted 1 pp from GDP growth, and business investment grew at moderate pace. The GDP price deflator slowed sharply, to 4.1%, due to the decline in energy prices. The core GDP deflator grew by 4.5%, just marginally down from the pace in Q2, and far above Fed's inflation target. Corporate profits were probably close to unch. in Q3 as wages probably rose more than value added (but several data are still missing)
  - » **Household spending** grew more than expected in September (and in Q3, also because Aug was revised upwards), and prices rose less than expected. The savings rate fell too, but the 'Wall of Money' (excess saving accumulated through the pandemic) is still mostly intact, though those savings are heavily concentrated among those who are well off
  - » The **employment cost index** rose 1.2% in Q3 (as expected down from 1.3% in Q2, and is up 5% y/y, 2 ¾ pp above the 10-year average before the pandemic. Public sector employment costs shot up, while cost inflation slowed in Q3, from a very high level in Q2. In National accounts, the wage cost per unit produced in the whole economy was up more than 6% y/y in Q3
  - » **New home sales** fell but less than expected in September. However, **pending (existing) home sales** nosedived 10%, much more than expected. **Price indices** surprised on the downside; The Case/Shiller index reported a 1.2% m/m decline in August. Following the 42% surge through the pandemic, home prices are very exposed as the mortgage rate has surged 7.5%, the highest in 20 years, and **demand for new mortgages** has 'collapsed'
  - » **Core PCE inflation** was up 0.5% in September, in line with expectations; August data revised down by 0.1 pp to 0.5% m/m. All but two sectors report of price increases below 2%. And even though there are signs that inflation has peaked, the pace of price increases is still too high and widespread – so no compelling arguments for the Fed not to go ahead as planned and raise rates by 75 bps

Last week, II

- **EMU**
  - **The ECB** lifted its signal rates by another 75 bps, to a 1.5% deposit rate. Fear of a prolonged period of high inflation and a wage-price spiral are cited as reasons for the recent hike, and more rate hikes are in the pipeline, the bank says, while at the same time acknowledging that the risk of a recession has increased. In addition, the ECB changed the wording on the outlook for further rate hikes: Last time, the bank said it would raise rates over the next several meetings. Now it just said it expected to raise rates further. In order to further tighten monetary conditions, the bank also lifted interest rates in the TLTRO III programme. The whole yield curve fell sharply, but the short end recovered on Friday
  - **The first Q3 GDP** reports were slightly better than expected, as Germany grew 0.3% (not annualised), expected down 0.2%! EMU will report today
  - The preliminary **October CPI** reports indicate a further increase in the annual growth rate – to above 10.0%
  - **Business sentiment** fell further in October but remains above an average level, according to EU's survey, and are in fact signalling 2% GDP growth! Manufacturing and construction are reporting growth above normal, services are below. Other surveys/nowcasters signal a decline in GDP, like the PMI, Ifo, and CEPR's EuroCoin
  - Household credit growth is slowing, business credit not. Banks say they are tightening credit conditions, and interest rates are rising rapidly
- **Sweden**
  - **Swedish GDP** unexpectedly reversed the 1.3% August dip and was up 1% m/m in September, and growth in Q3 also surprised on the upside with GDP being up 0.7% (2.8% annualised), while the market expected +0.1%
  - However, the outlook is bleaker, and the **KI survey** is signaling a 2% contraction in GDP. Manufacturing still report growth above average (but the index is rapidly on the way down, while services and trade is far below average
  - **Retail sales** fell by 0.4% in September, the 5th decline in row. Sales are down 5.6% y/y. In addition, sales are well below the pre-pandemic trend. The outlook is not the best: consumer confidence (the micro index) fell sharply, to 6.5 st.dev below average, a rather unusual data-point. Home prices are falling rapidly
- **Norway**
  - The NAV open **unemploymen**t was marginally down in October – the rate unchanged at 1.6%, which is the lowest since before the GFC and close to the level seen in 1980. The latest print was 0.1 pp below the NoBa f'cast from September and is another piece of data (along with recent GDP figures and inflation data) that adds fuel to the + 50 bps hike crowd. The LFS unemployment data showed a marginal increase, however the rate at 3.2% is still very low.
  - **New vacancies** rose marginally but are trending down. The level still remains high, but we are still not seeing an acceleration in wage growth. The current wage growth is trending up at less than 3.5% (volatile monthly figures show a 4% y/y growth) which is an argument for Norges Bank to stick to its plan of 2 x 25 bps
  - **Retail sales** rose 0.1% in September, we expected a substantial decline. Still, the trend is down – and sales are back to the modest pre-pandemic trend

The Calendar: Final PMIs, ISM. FOMC, BoE & NoBa. US labour market. Norwegian home prices

Time	Count.	Indicator	Period	Forecast	Prior
Monday October 31					
08:00	GE	Retail Sales MoM	Sep	-0.5%	-1.3%
08:00	SW	Wages Non-Manual Workers YoY	Aug		3.1%
08:00	NO	Credit Indicator Growth YoY	Sep	(5.3)	5.2%
11:00	EMU	CPI Estimate YoY	Oct	10.0%	10.0%
11:00	**EMU**	**CPI Core YoY**	**Oct P**	**4.9%**	**4.8%**
11:00	EMU	GDP SA QoQ	3Q A	0.10%	0.80%
14:45	US	MNI Chicago PMI	Oct	47.6	45.7
Tuesday November 1					
02:45	CH	Caixin China PMI Mfg	Oct	48.5	48.1
08:30	SW	Manufacturing PMI	Oct		49.2
10:00	NO	Manufacturing PMI	Oct	(48.5)	50
14:45	US	Manufacturing PMI	Oct F	49.9	49.9
15:00	**US**	**JOLTS Job Openings**	**Sep**	**9625k**	**10053k**
15:00	US	Construction Spending MoM	Sep	-0.5%	-0.7%
15:00	**US**	**ISM Manufacturing**	**Oct**	**50.0**	**50.9**
16:00	**WO**	**Manufacturing PMI**	**Oct**	**(48.7)**	**49.8**
	US	Wards Total Vehicle Sales	Oct	14.30m	13.49m
Wednesday November 2					
10:00	EMU	Manufacturing PMI	Oct F	46.6	46.6
13:15	US	ADP Employment Change	Oct	195k	208k
19:00	**US**	**FOMC (Upper Bound)**	**Nov-02**	**4.00%**	**3.25%**
Thursday November 3					
02:45	CH	Composite PMI, Caixin	Oct		48.5
02:45	CH	Services PMI, Caixin	Oct	49.2	49.3
08:30	SW	Services PMI	Oct		55.1
10:00	**NO**	**Deposit Rates**	**Nov-03**	**2.63%**	**2.25%**
11:00	**NO**	**Home prices MoM, s.a**	**Oct**	**(-2.0%)**	**-0.6%**
11:00	EMU	Unemployment Rate	Sep	6.6%	6.6%
13:00	**UK**	**Bank of England Bank Rate**	**Nov-03**	**3.00%**	**2.25%**
13:30	US	Trade Balance	Sep	-$71.9b	-$67.4b
13:30	US	Productivity	3Q P	0.7%	-4.1%
13:30	US	Unit Labor Costs	3Q P	3.9%	10.2%
14:45	US	Services PMI	Oct F	46.6	46.6
15:00	**US**	**ISM Services**	**Oct**	**55.5**	**56.7**
16:00	**WO**	**Services PMI**	**Oct**	**(48.9)**	**50.0**
Friday November 4					
10:00	EMU	Services PMI	Oct F	48.2	48.2
10:00	EMU	Composite PMI	Oct F	47.1	47.1
11:00	EMU	PPI YoY	Sep	42.1%	43.3%
13:30	**US**	**Change in Nonfarm Payrolls**	**Oct**	**200k**	**263k**
13:30	**US**	**Unemployment Rate**	**Oct**	**3.6%**	**3.5%**
13:30	**US**	**Average Hourly Earnings MoM**	**Oct**	**0.3%**	**0.3%**
13:30	US	Average Hourly Earnings YoY	Oct	4.7%	5.0%
13:30	US	Labor Force Participation Rate	Oct	62.4%	62.3%
16:00	**WO**	**Composite PMI**	**Oct**	**(48.7)**	**49.7**

- **PMI/ISM**
  - » **The preliminary PMIs** from the rich part of the world fell further, and all but Japan are below the 50-line, as both manufacturing and services reported a decline in activity. Europe (EMU, UK) is at the bottom but US is not far above. Manufacturing orders are weak, both in Europe and in the US. Delivery times are coming down, as are reported price increases – but price indices are well above normal levels. China's 'official' PMI (not the one included in the global index) fell by 1.9 p to 49.0. We expect a 1 p decline in the global composite PMI, the 4th print in row below the 50-line . In the US, the **manufacturing ISM** is expected down to the 50-line, more or less as signalled by regional Fed surveys and the PMI. ISM is expected to report strong growth in the service sector (where the PMI disagrees)
- **USA**
  - » **The FOMC** will very likely hike by 75 bps again, for the 4th time in row, the steepest increase in Fed' signal rate since the early 80s. The level is still 'low' after the expected hike, at 3.75% – 4.00%, vs the 20% level reached that time. Powell will give a presser, but not a dot-plot or new forecasts at this meeting. We expect Powell to signal that further hikes are very likely but as the bank has moved fast into a contractive territory, the speed will now most likely slow down. The market expect at 50 bps hike in December – and it seems unlikely to become more than that
  - » Will the **labour market report 'low' wage growth** in October on Friday – and higher **unemployment**, and a slower **employment** growth? Will number of **unfilled vacancies** decline sharply in September, as it surprisingly did in August (data out Tuesday). Will the **SME survey** report a less tight labour market? These are more important for the interest rate outlook than what Powell communicates on Wednesday
  - » Q3 **productivity, unit labour costs** are of great interest for us, and should be for the market. Current trends are not encouraging, to put it mildly – cost inflation is far too high
- **EMU**
  - » **October CPI** will 'surprise' on the upside, at least based on country data published on Friday
  - » **Q3 GDP** will also 'surprise' on the upside, based on country data published on Friday. We think a 0.2% growth rate (0.8% annualised) is more likely than 0.1%
  - » **Unemployment** is expected to remain unchanged at 6.6%, at the lowest level since the early 80s. The decline in number of unemployed has slowed recent months, and is approaching the zero line. We expect to see a positive number soon
- **UK**
  - » A 75 bps hike from the **Bank of England** too? We think nerves have calmed down somewhat. Price inflation as well as wage inflation is too high but growth is now slowing rapidly, partly because real incomes are falling rapidly. The risk is clearly at the downside vs. the expected 75 bps, not on the upside – even if a new budget is not presented
- **Norway**
  - » **25 bps or 50, that's the question:** on balance, 25 bps from Norges Bank is enough this time – but the outcome is open. Economists are evenly split, according to Bloomberg. Check our arguments next page
  - » **Home prices** no doubt fell further in October, and more than in September (-0.6%). Less than a 1% decline would be surprising, and our -2% f'cast is not unlikely. At least in Oslo, prices must have fallen sharply, at least if unsold homes were 'fairly' included (which of course is impossible but there you know our excuse if we turn out to be wrong). Home buyers have got their proof of financing sharply reduced recent weeks, and interest rate for new loans have crossed the 4% line in many banks. The buying power is sharply reduced

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

SpareBank 1 MARKETS

Norges Bank preview: 25 bps is enough now

The 25-bps list is far longer than the 50-bps list, but inflation, GDP, and unemployment are important

Arguments in favour of a 25 bps hike

- NoBa **said so** in September, and can afford to **wait and see** if the previous rate hikes slow the economy sufficiently
- **Business surveys** have weakened further abroad and in Norway (PMI, SSB manufacturing survey, NHO survey)
- **GDP growth forecasts** are being revised down most places, also for Norway
- **Home prices** fell more than expected in September, and reports from the housing markets are on the weak side
- **New home sales** are falling, and starts are heading down
- **Household credit** growth is slowing, and in NoBa's **lending survey**, banks signalled a significant slowdown in lending to both households and businesses in Q4
- **Consumer confidence** is falling further
- **LFS employment** is slowly declining, and the LFS unemployment rate rose a tick in August (but not significant)
- The inflow of **new vacancies** fell in Sep and is trending down (a small uptick in Oct did not change that)
- **Wage growth** was revised down, and remained moderate in September. Thus, wage inflation has not accelerated through 2022
- **NOK** has strengthened more than NoBa assumed
- **Gas prices** have fallen sharply. Other **raw material prices,** are heading down, and **freight** rates are rapidly falling
- **Short term rates** among our **trading partners** are slightly down
- **Equity markets** are down (vs mid Sept), and **credit spreads** have widened, also in Norway

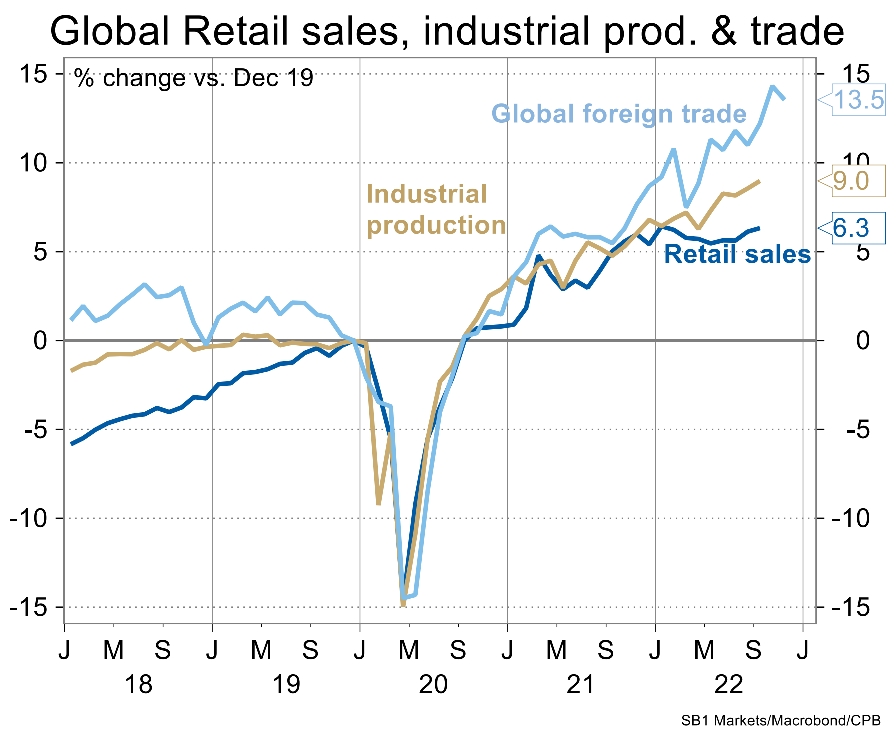
Arguments in favour of a 50 bps hike

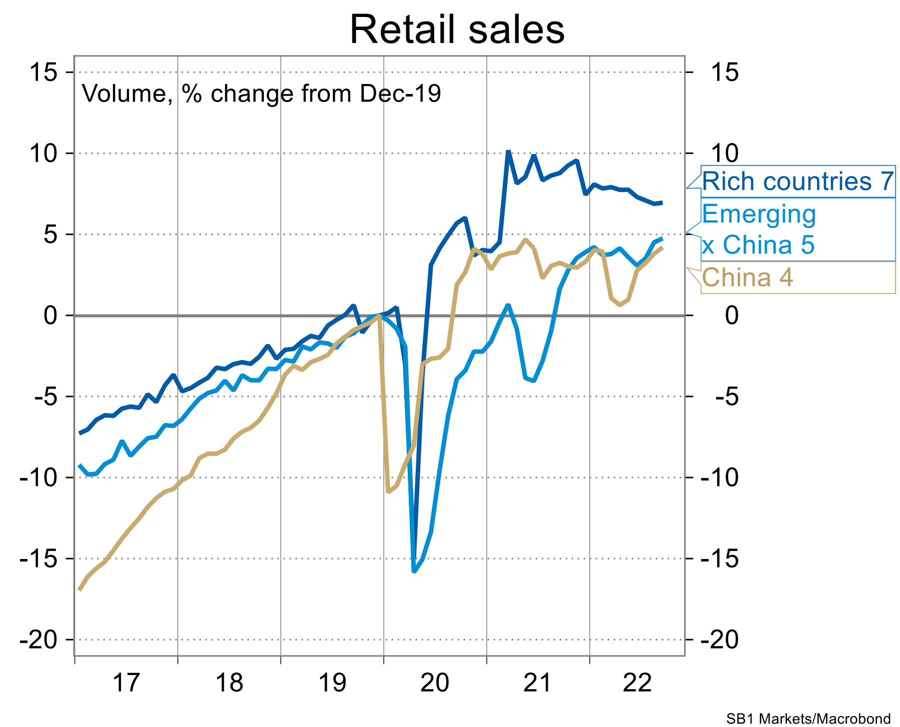
- **Inflation** was higher than expected in Sept, rather broad based
- **Mainland GDP** was revised upwards and grew more than expected in August
- **NAV unemployment** was 0.1 pp below NoBa's path both in Sept and Oct
- In SSB's manufacturing survey, companies are still reporting substantial **lack of labour**
- Formally, **the 2023 budget proposal** was not as tight as NoBa expected but we never thought NoBa's estimates were reasonable (and we think it is highly unlikely NoBa will use the budget as an argument for hiking more aggressively than assumed in Sept)
- **The oil price is** slightly up
- **Other central banks** have opted for 50 – 75 bps hikes recently (but Australia lifted just 25 bps)
- **The market** expects it

- **So what:** Even if 'the big 3' are stronger than NoBa assumed in Sept, the bank should lower the pace to 25 bps. The main argument is that it will take some time to assess the impact of the previous hikes, and that hiking may have a significant impact in the most indebted household sector in the world (vs income), and with the lowest duration or their debts (in practice, just floating rates). Even if several data are still OK, growth is now very likely slowing both abroad and at home. At the same time, NoBa should carry a big stick, and promise to fight inflation by hiking rates more than signalled in September, if needed – in order to dampen the impression of a 'dovish' central bank and to enhance the impact of hikes already implemented

Retail sales probably up in September, due to Emerging markets

Industrial production very likely rose too. Recent global trade data may be too upbeat?



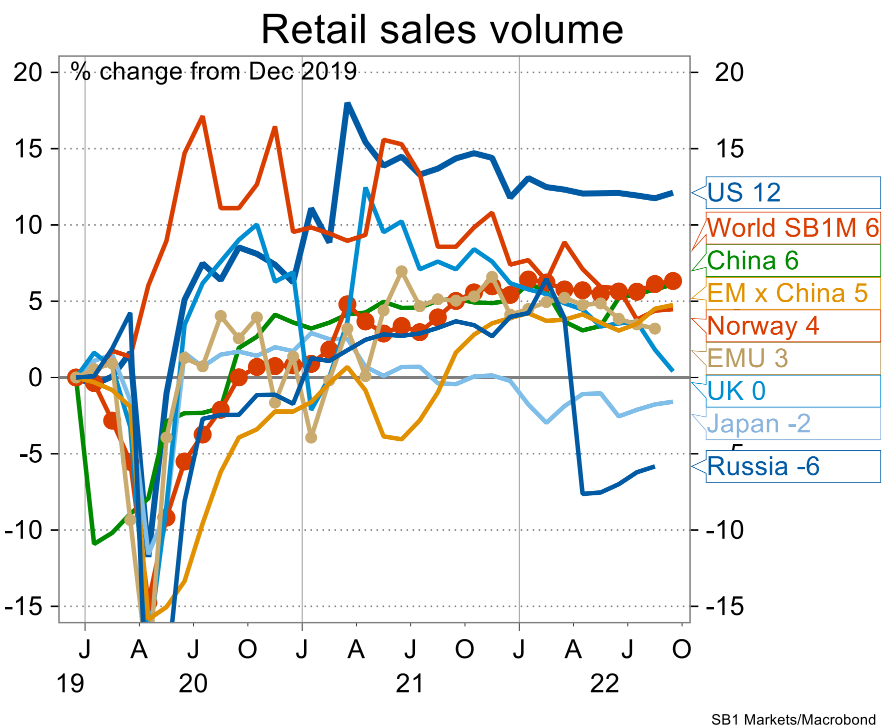


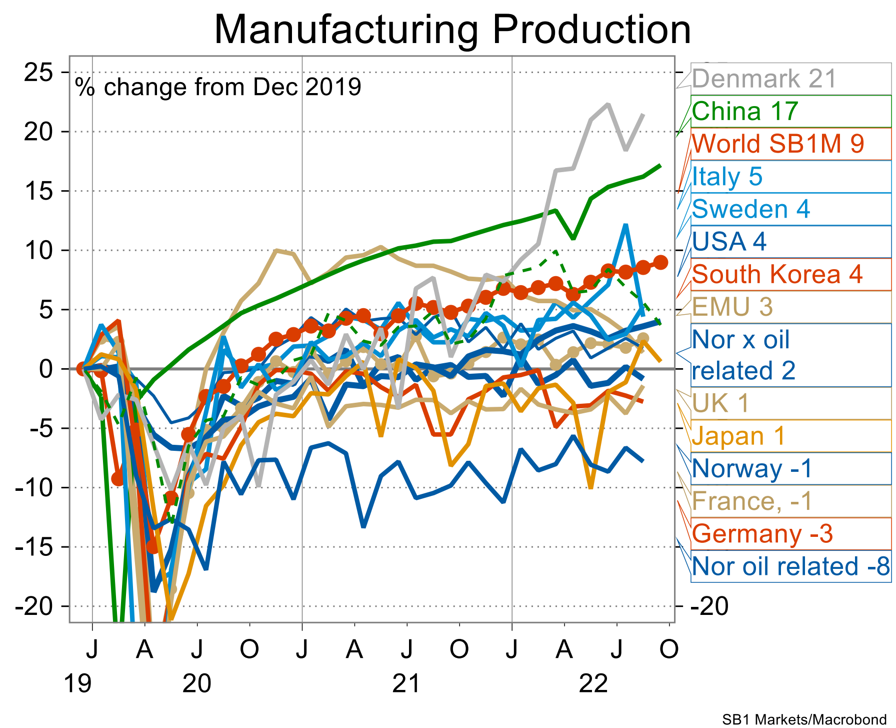
- So far, not that many countries have reported September data, so these are our preliminary estimates

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

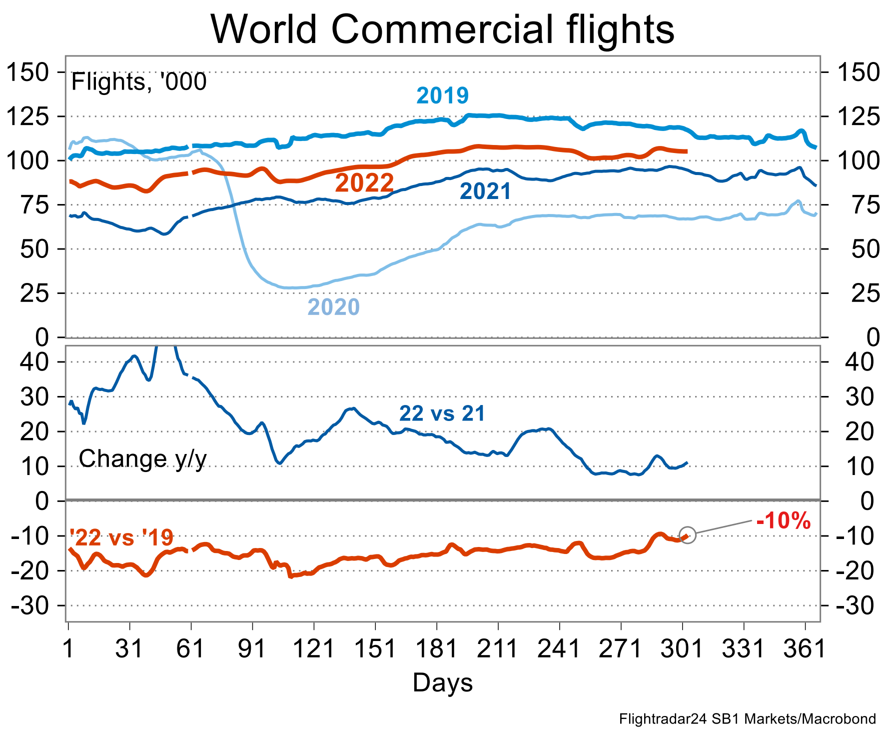
Is manufacturing exposed? Surveys, like the PMIs send a warning sign too

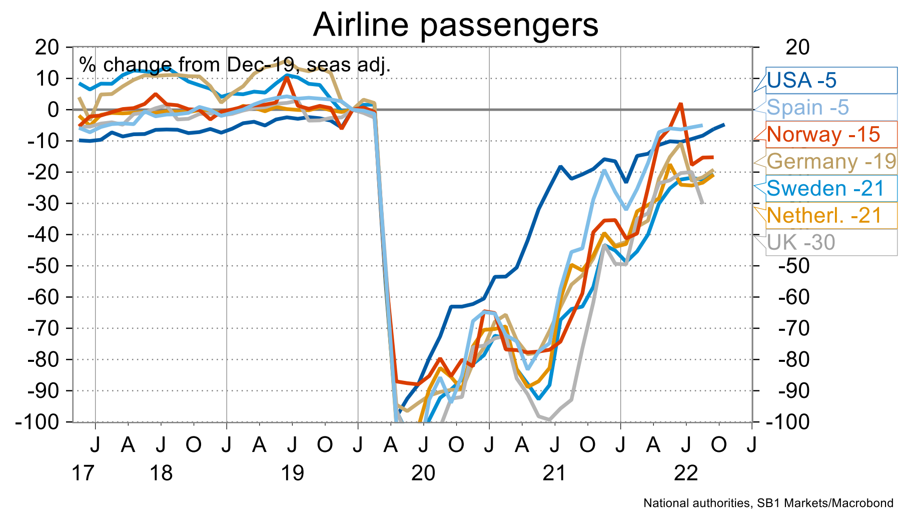


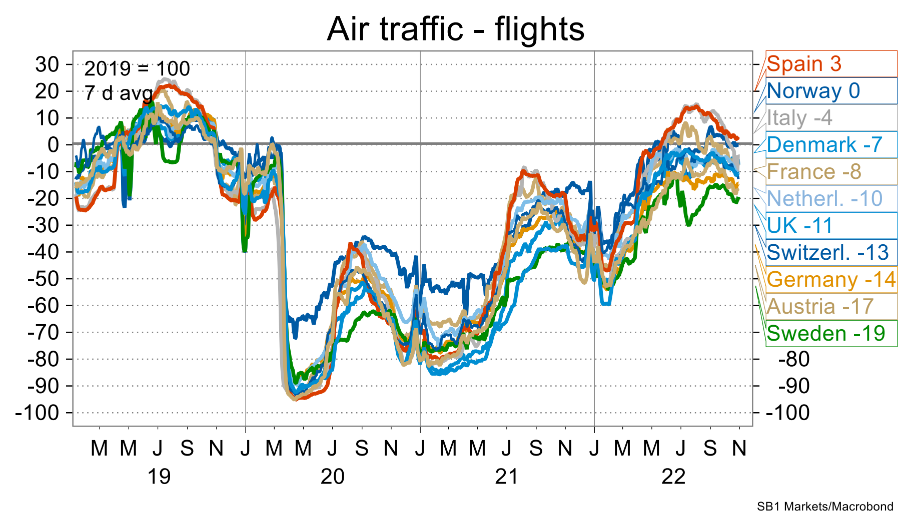


US retail sales: Personal consumption of goods, ex auto & energy

Global airline traffic slightly up, down ‘just’ 10% vs. 2019 level

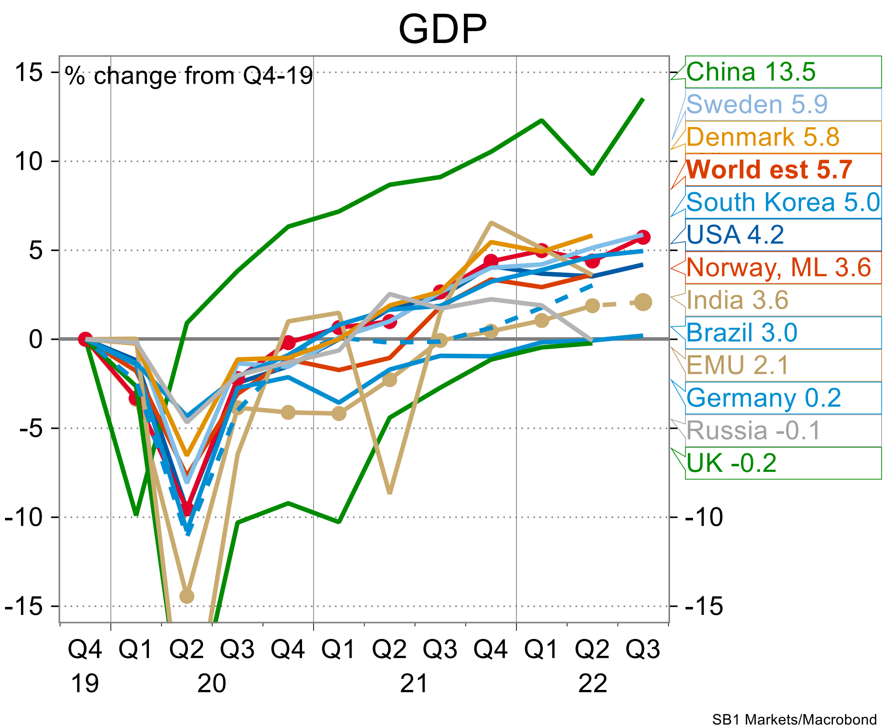


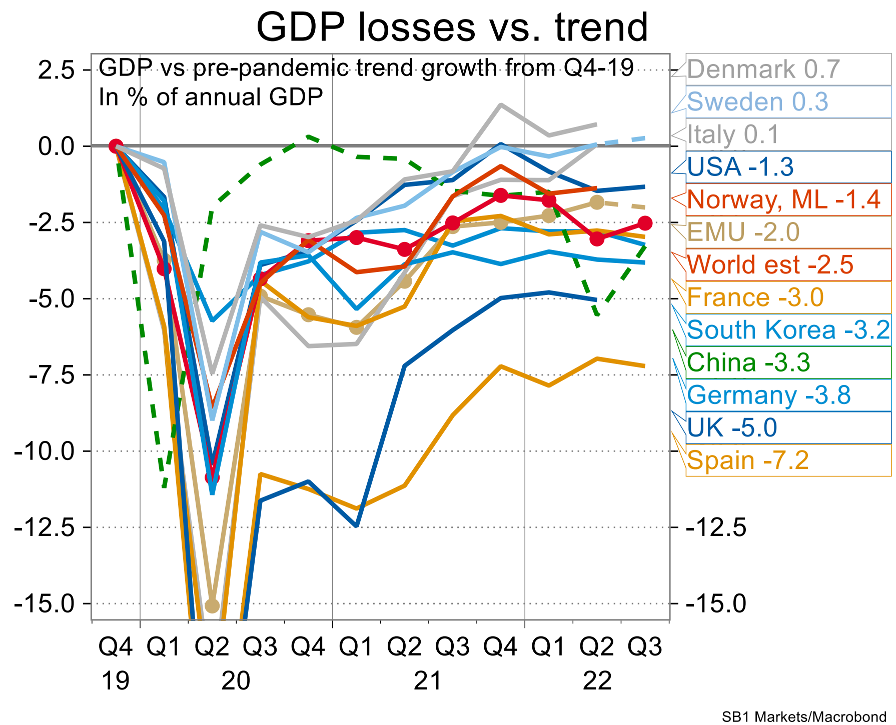




Global GDP recovered in Q3, mostly thanks to China, but with help from the US

… and probably the EMU! Still global GDP is 2.5% below the pre-pandemic trend path

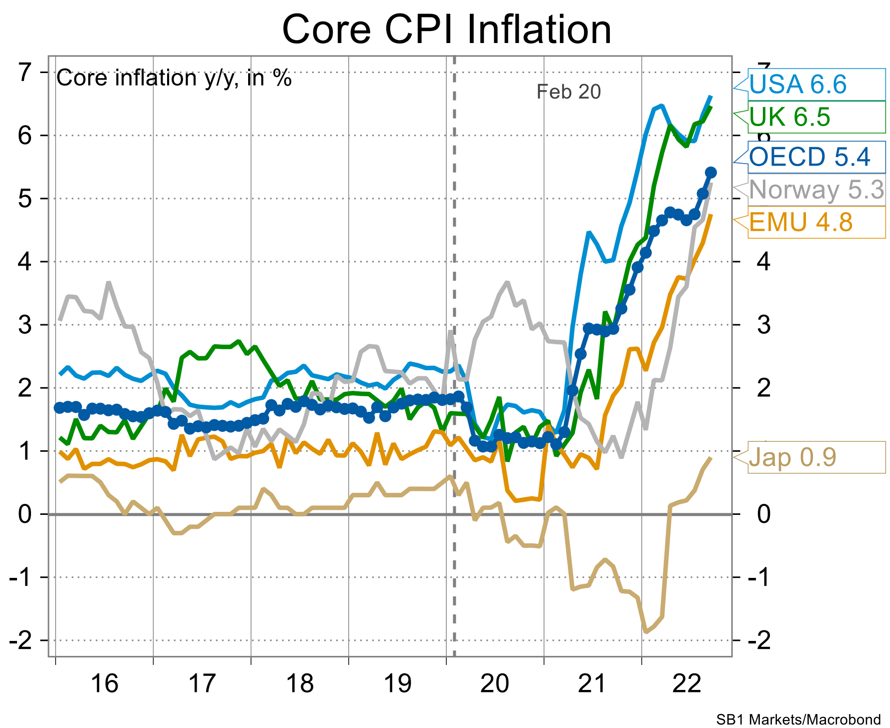


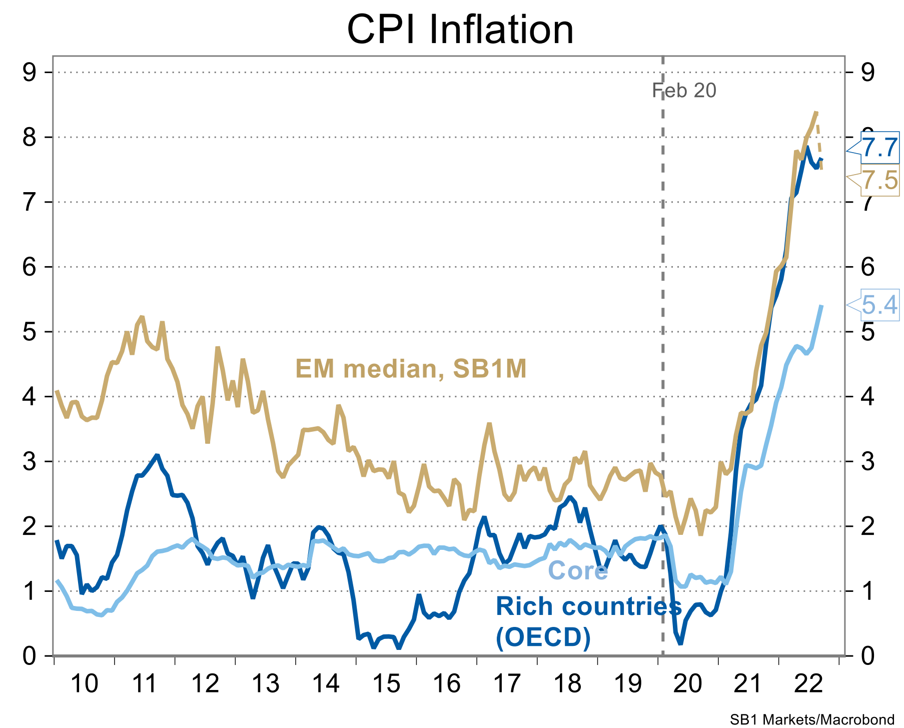


- … even if unemployment, at least in the rich part of the world is ‘zero’, and employment rates are record high almost everywhere
- Most countries have not yet reported Q3 data

Peak inflation? Data are not that obvious anymore

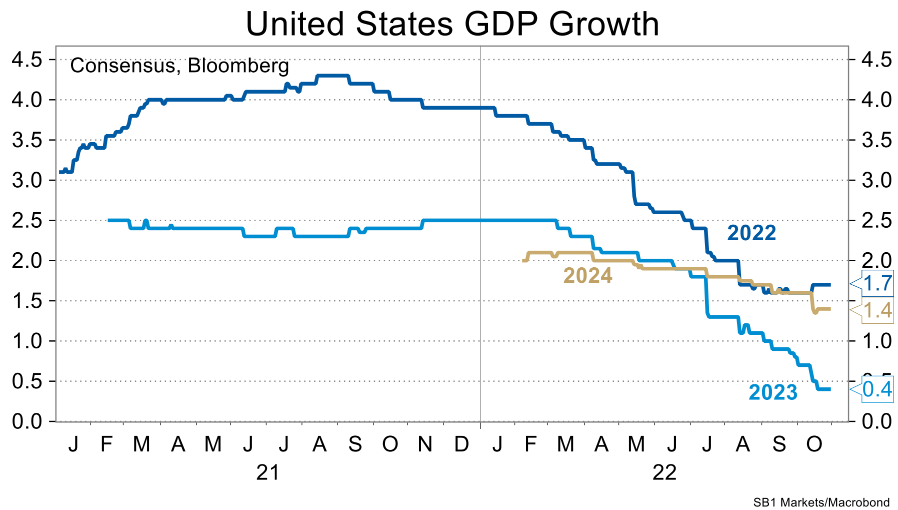
The going rate is 8% headline inflation, and 5% core inflation, and the latter is still on the way up

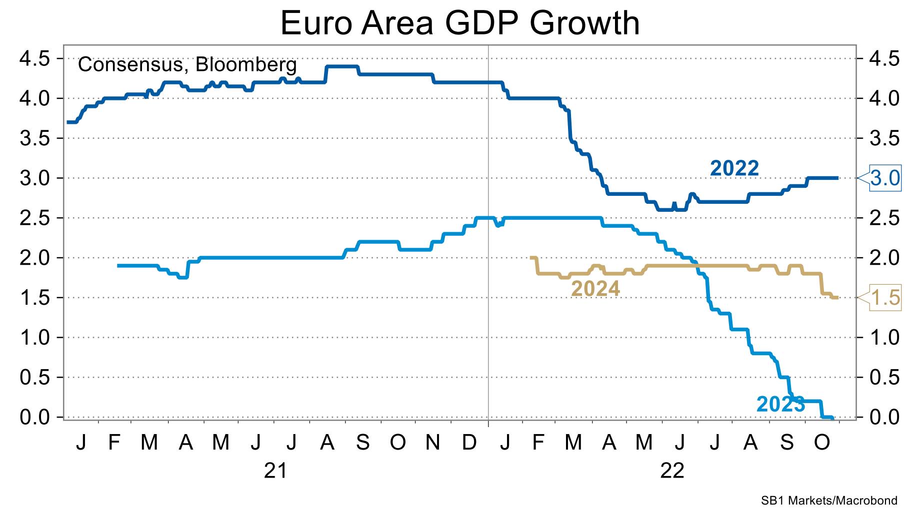


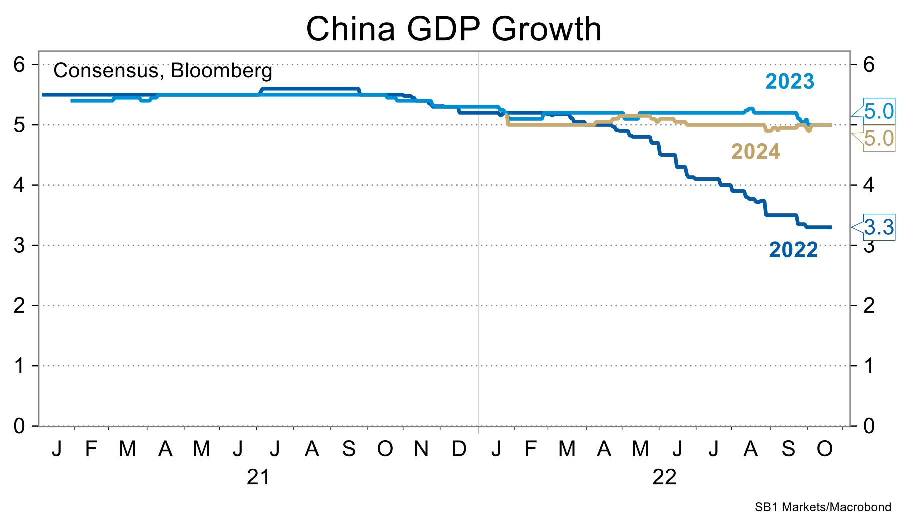


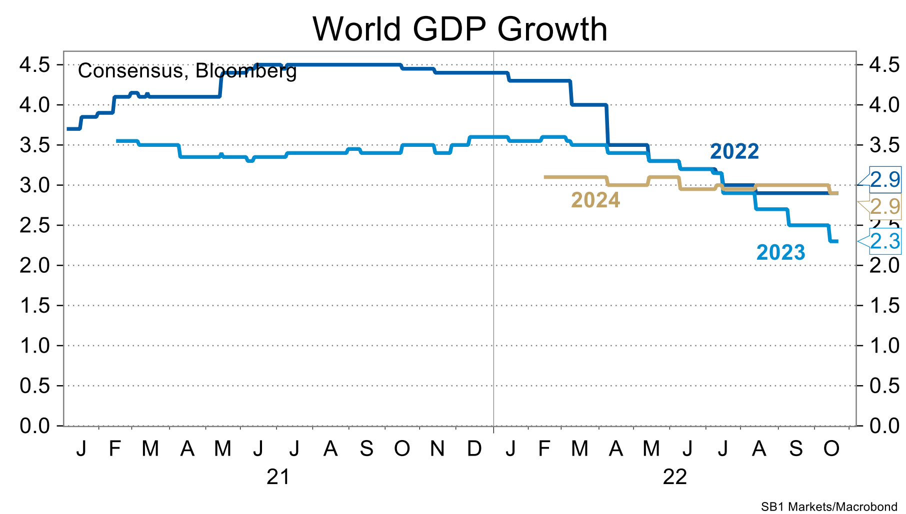
GDP growth expectations: 2023 forecasts are sliding down in US & EMU

In addition, 2022 will be a 'lost' year in China





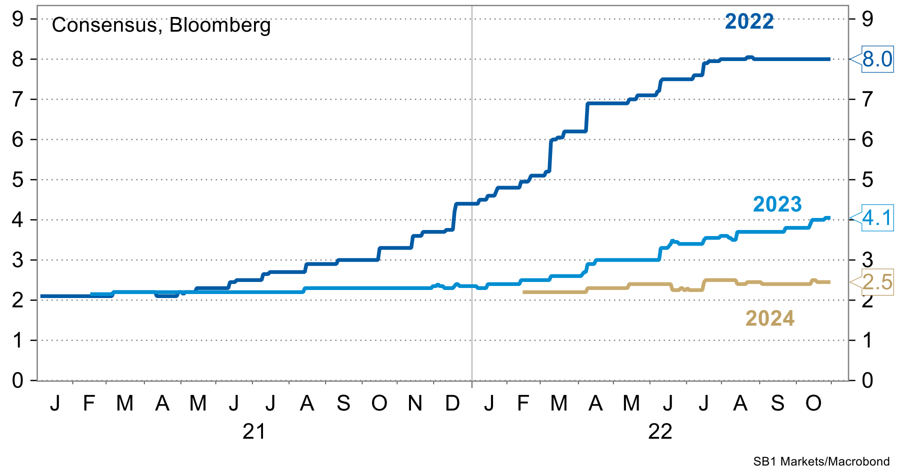




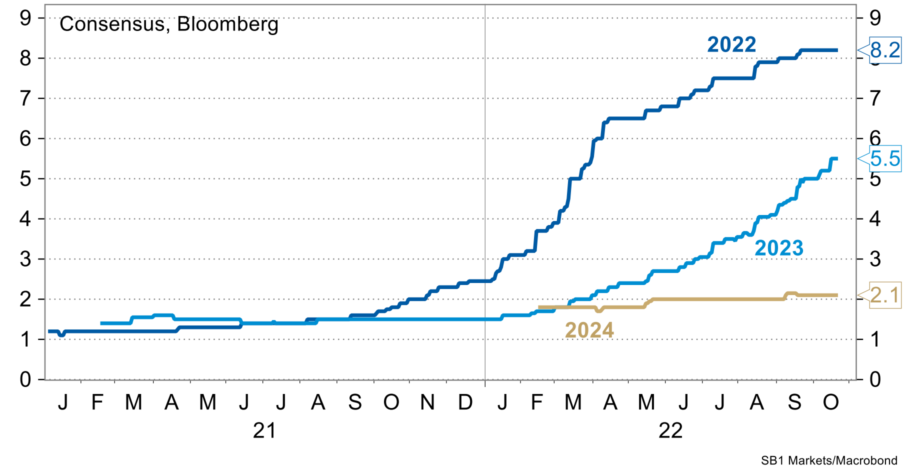
2023 inflation forecasts are still drifting upwards

Especially the 2023 EMU inflation expectations

United States CPI forecasts



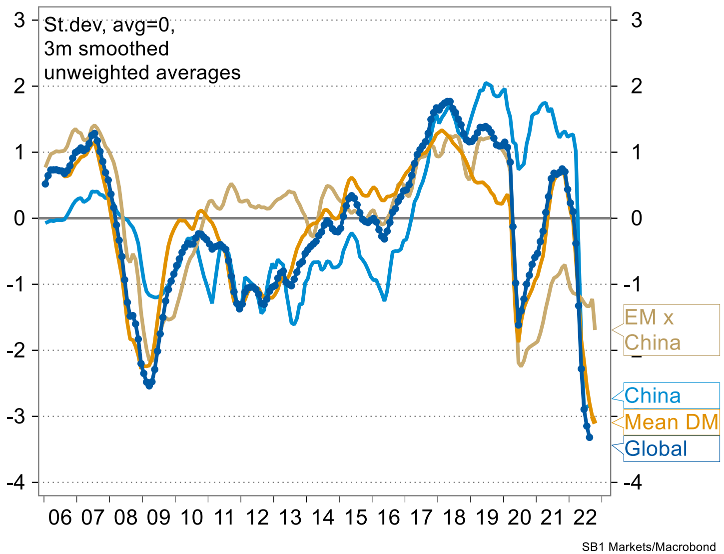
Euro Area CPI forecasts



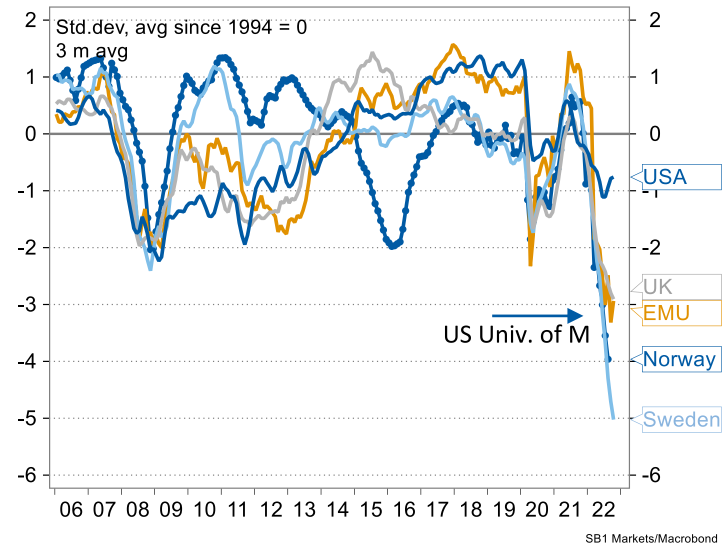
Consumer confidence further down almost everywhere

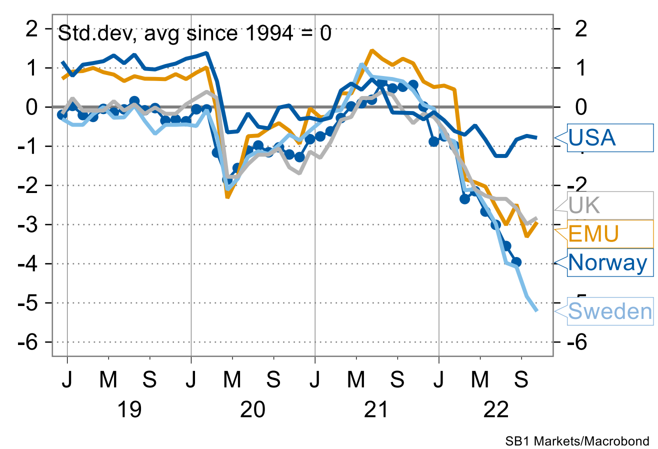
The Nordics at the bottom, rest of Europe close to. US a tad up past 3 m!

Global consumer confidence



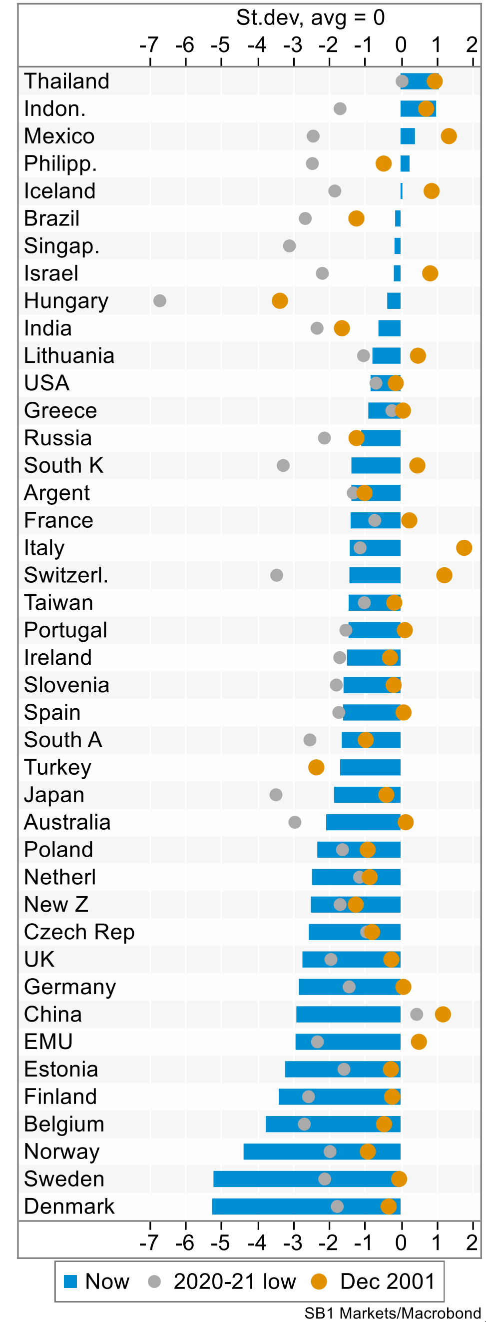
Consumer confidence





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

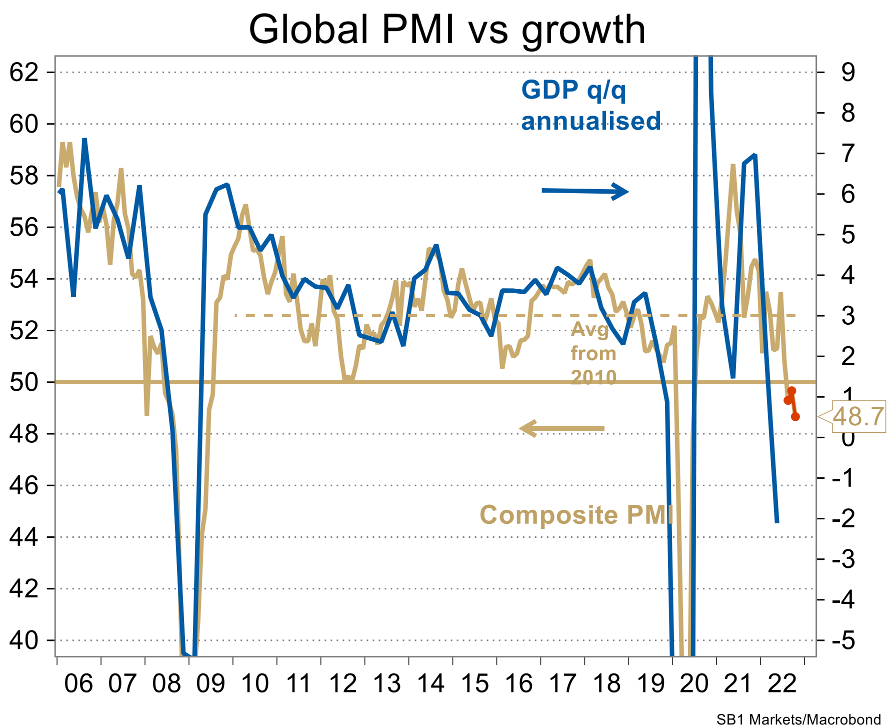
Consumer confidence

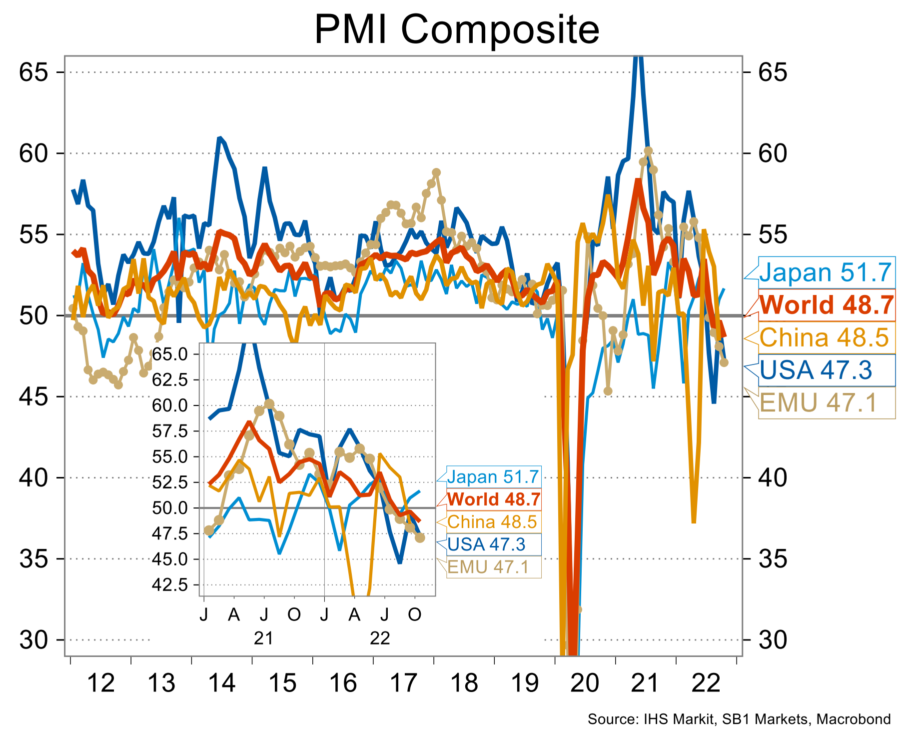


Norway is the average of Finans Norge & Opinion

The world composite PMI very likely down again in October, led by rich countries

Both US, EMU, and UK reported weaker PMIs than expected – and all are below the 50 line





- The composite PMI very likely fell in October, following the small uptick (which turned out to weaker than we assumed, due to another setback in China). We so far assume a 1 p drop, to 48.7, the lowest print the past 15 years, barring the Financial Crisis and the start of the Pandemic
- The US PMIs surprised the most on the downside
- In the EMU, Germany was the weakest, but the rest of the union is also below the 50 line
- Caxin has not reported its October data. This morning, the NBS/CPLF PMIs were reported down 1.9 p

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

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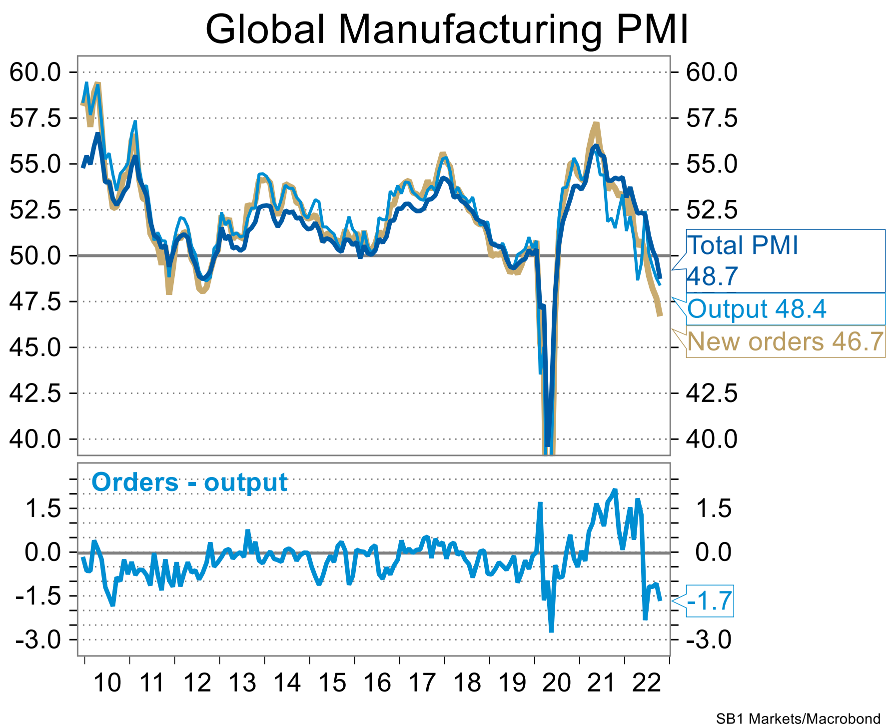
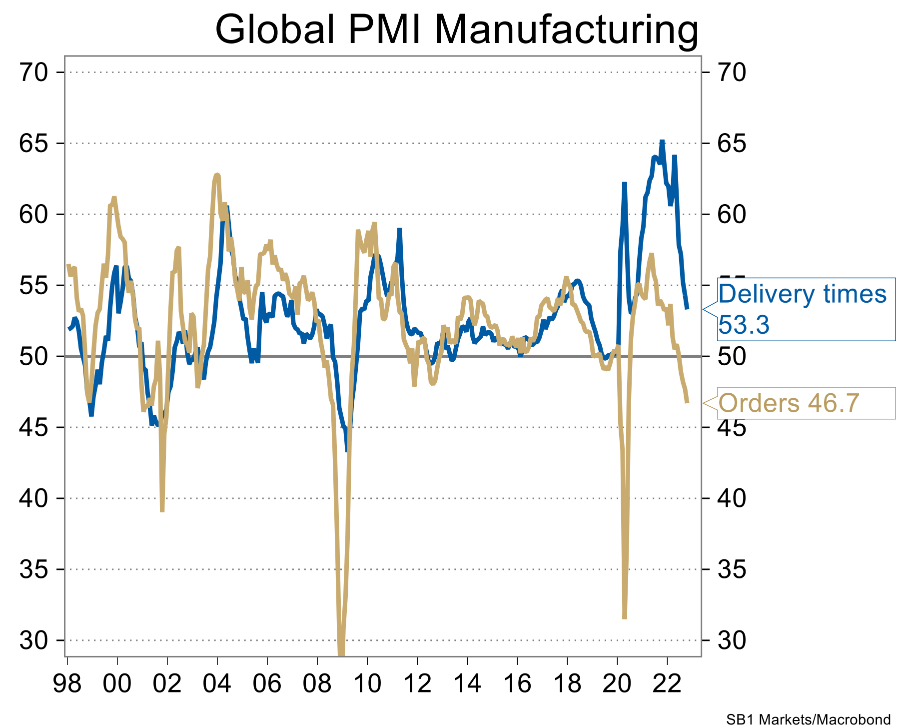
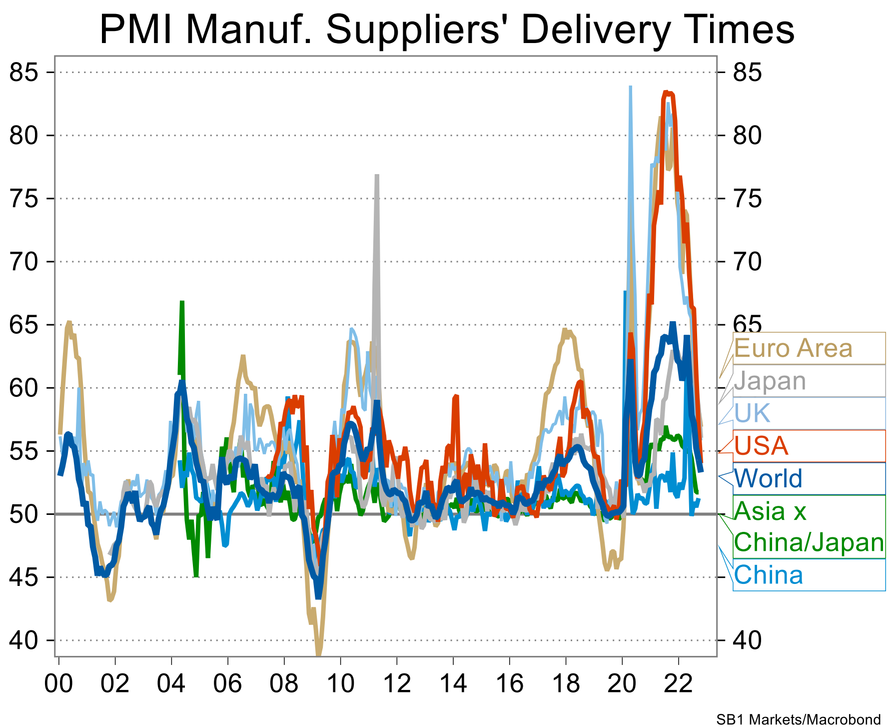
Manufacturing orders are contracting very fast, both in Europe & US

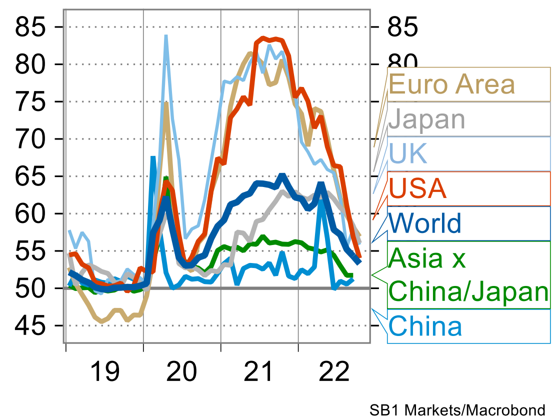
The delivery times index fell further in October – and is almost back to a normal level





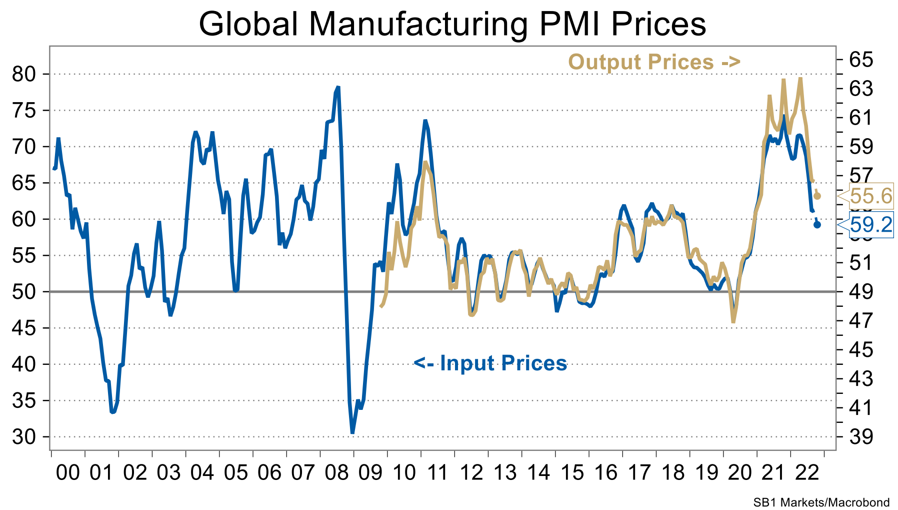
Delivery times are coming rapidly down everywhere

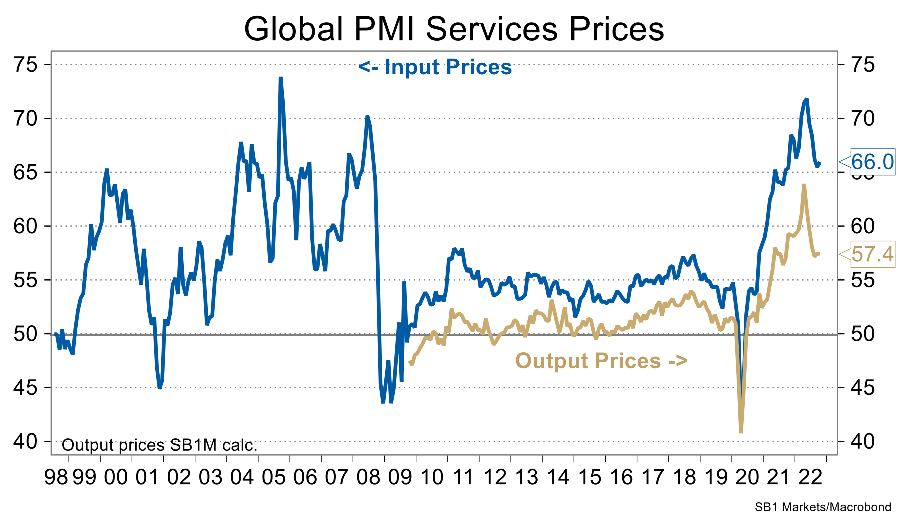


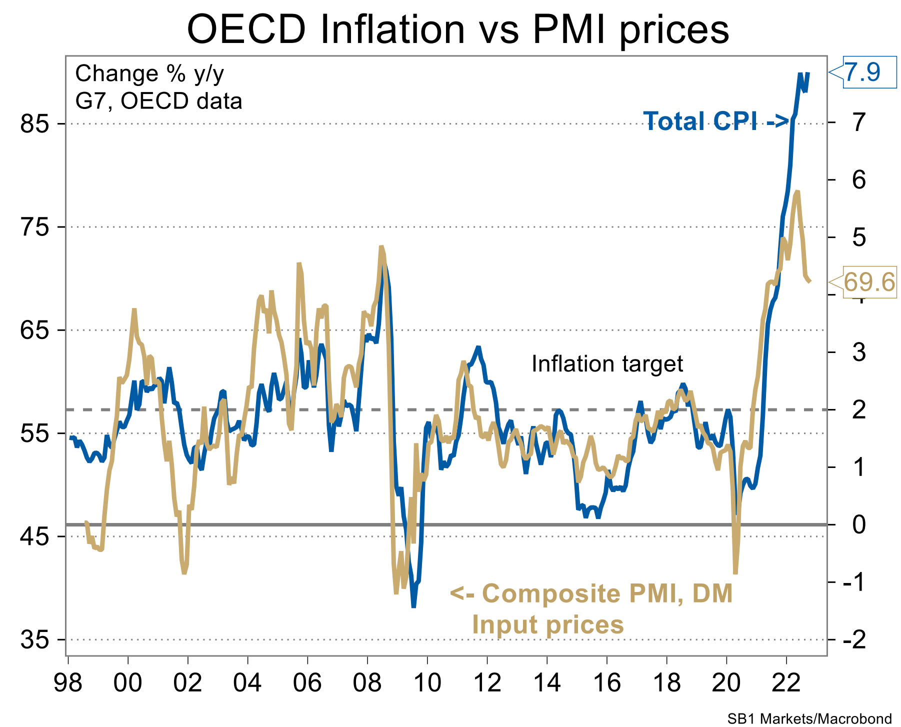


- **The global delivery times** PMI sub-index (changes in delivery times vs the previous month) has been inching down since the peak last October. The decline is broad among the Western rich countries
- **The interpretation of this index is uncertain** – are companies really reporting changes in delivery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

Price indices are heading down, but remain elevated







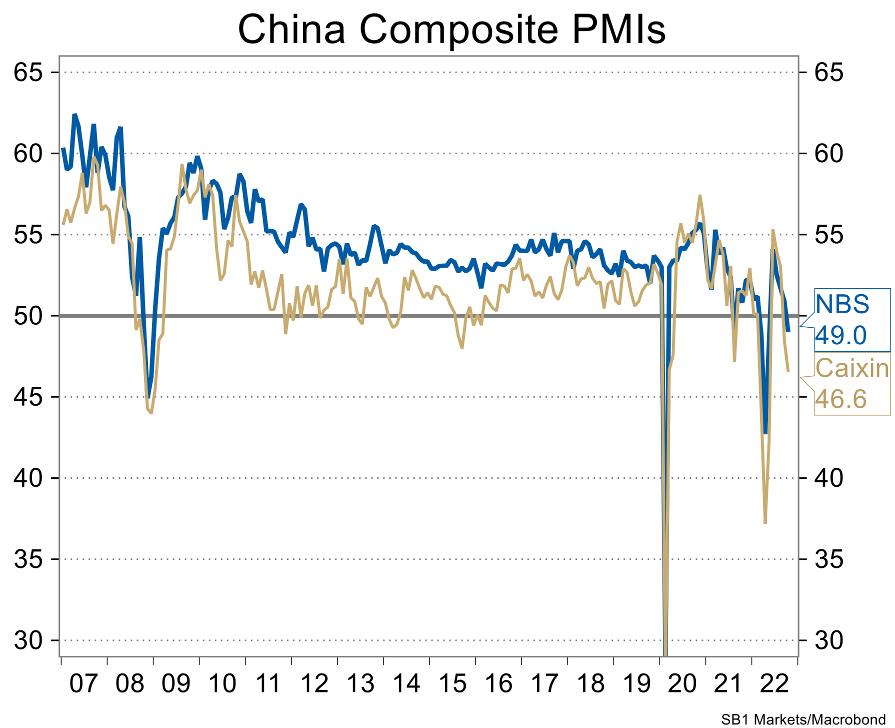
- These PMIs signal a substantial price pressure the coming months
- We are still much more concerned about wage inflation than the actual price inflation due to factors that are most likely transitory, like hikes in raw material prices, freight cost or short lived margins expansion when demand is surprisingly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

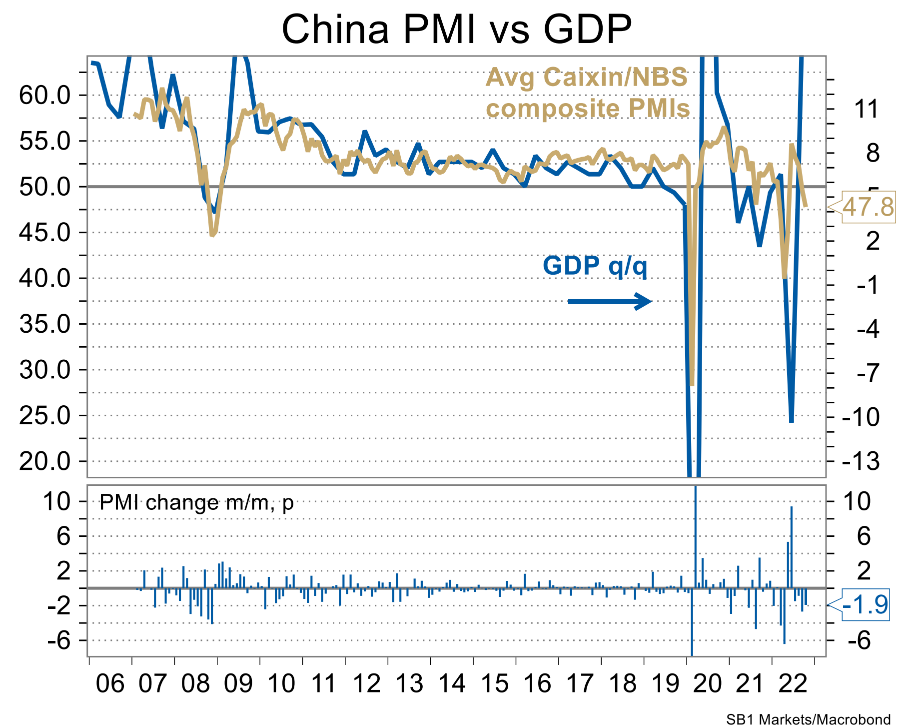
Last obs. based on preliminary PMIs from EMU, Japan, UK, and the US

SpareBank 1 MARKETS

The 'official' PMI down to below 50 again in October

Some 4% GDP growth is signalled

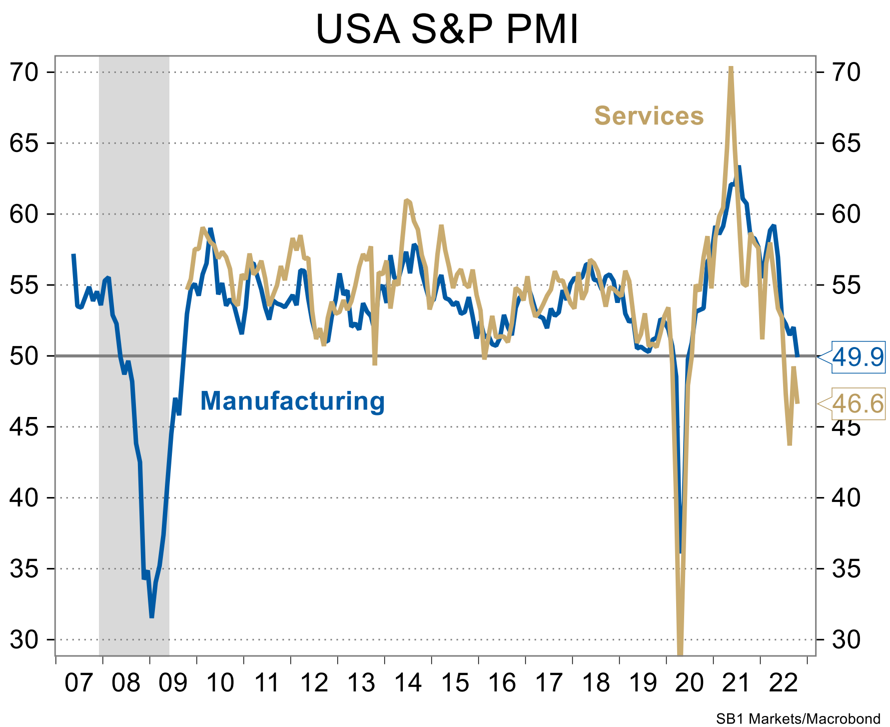


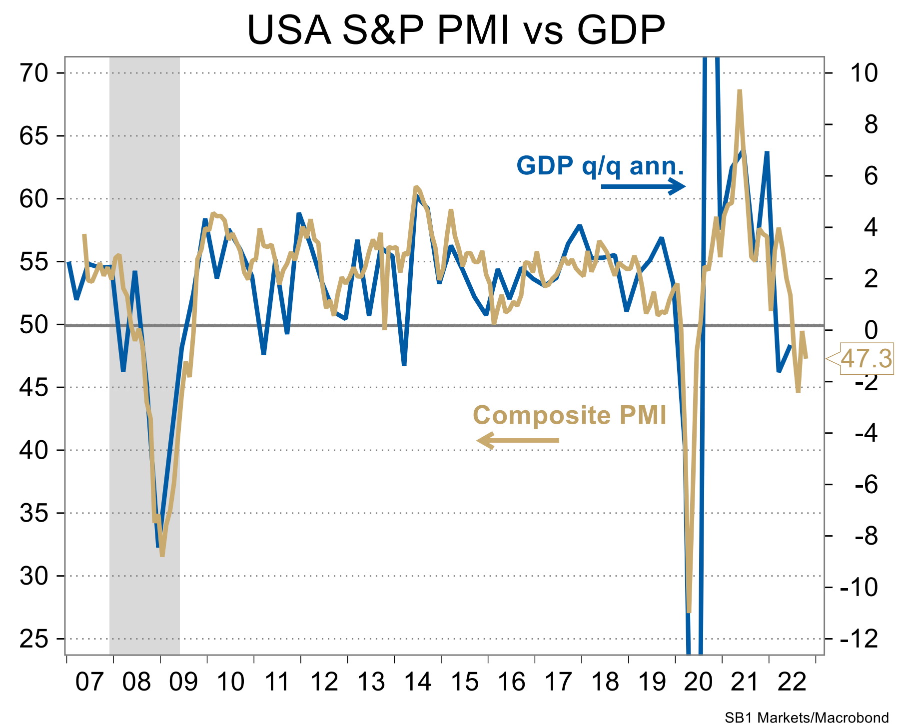


- The **NBS/CFLP composite PMI** fell by 1.9 p to 49.0, expected down 0.4 p – which is well below an average level. In fact the index has been below 50 just in 2008, early 2020 and in the lockdown months this spring
- The **Caixin PMIs** will be reported later this week
- *At the chart to the right we have assumed a decline in Caixin's composite PMI in line with the setback in the NBS/CFLP survey in October*

US PMIs down in October, the composite down 2.2 p to 47.3, a recession level

Both the services and the manufacturing PMIs surprised on the downside – new orders plummeted





- **The S&P composite PMI** fell 2.2 p to 47.3 in October, signalling some 1.2% (ann. rate) contraction in GDP. An 0.2 p decline to 49.3 was expected
  - » Services was again the weakest link, the index fell by 2.6 p to 46.6. The total manufacturing PMI fell to 49.9
- **The manufacturing new orders index** dropped 3.4 p to 46.7! This is the lowest print since the pandemic, and before that since Aug-09
- **The price indices** fell further but are still reporting faster price increases than normal

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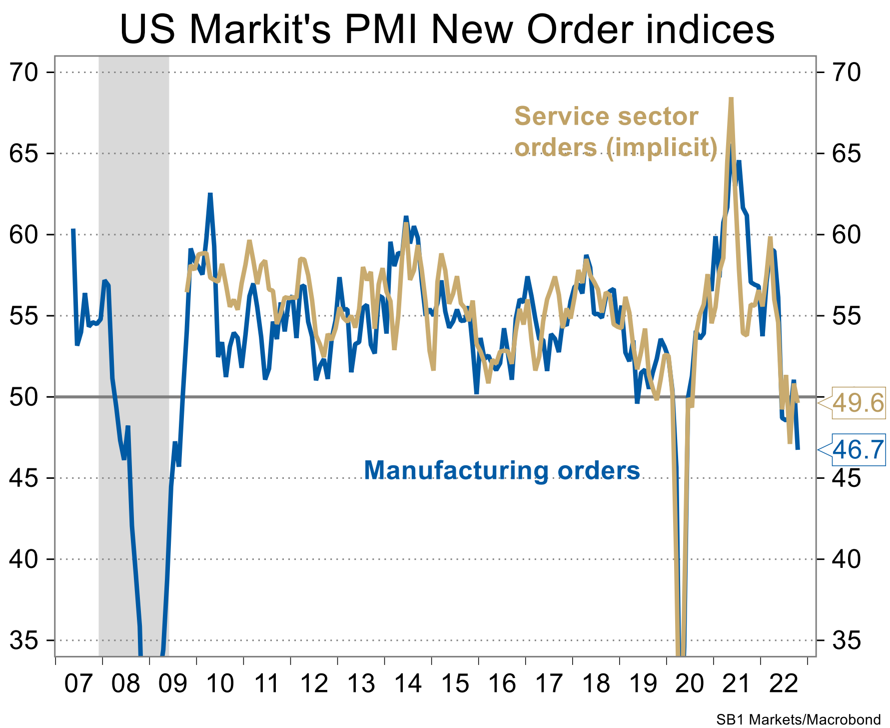
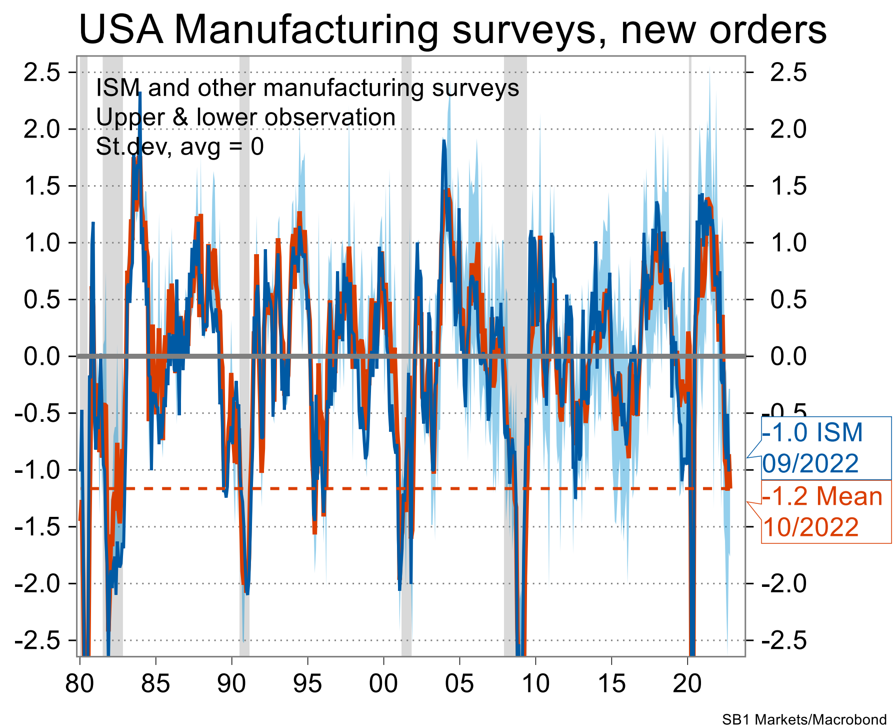
The PMIs – and all other manufacturing surveys insist a serious order shortfall

The manuf. PMI reports decline in new orders, just the Fin Crisis, start of the pandemic worse

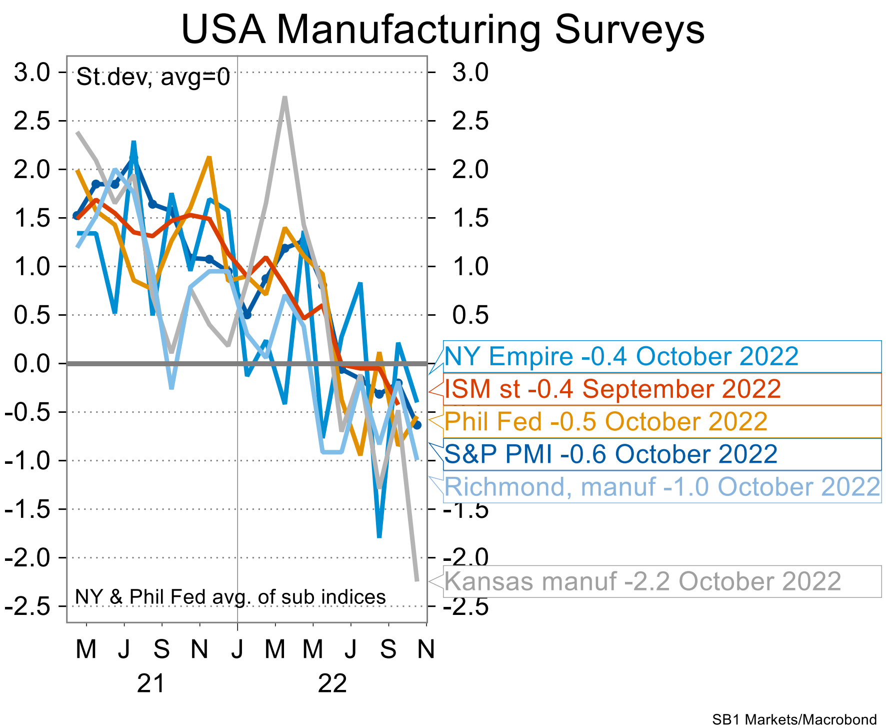


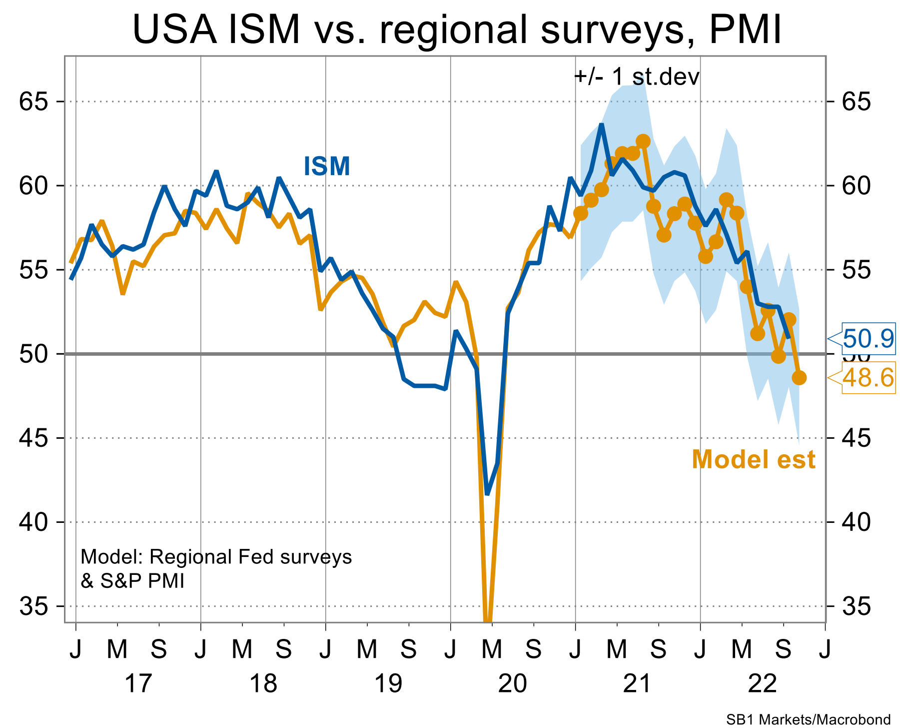


- Just once, in 1995, the order inflow was reported weaker than now, without the US entering or being in a recession

Another decline in the ISM, to or below the 50-line?

A model estimate based on the surveys published so far signals below 50. Consensus is at 50

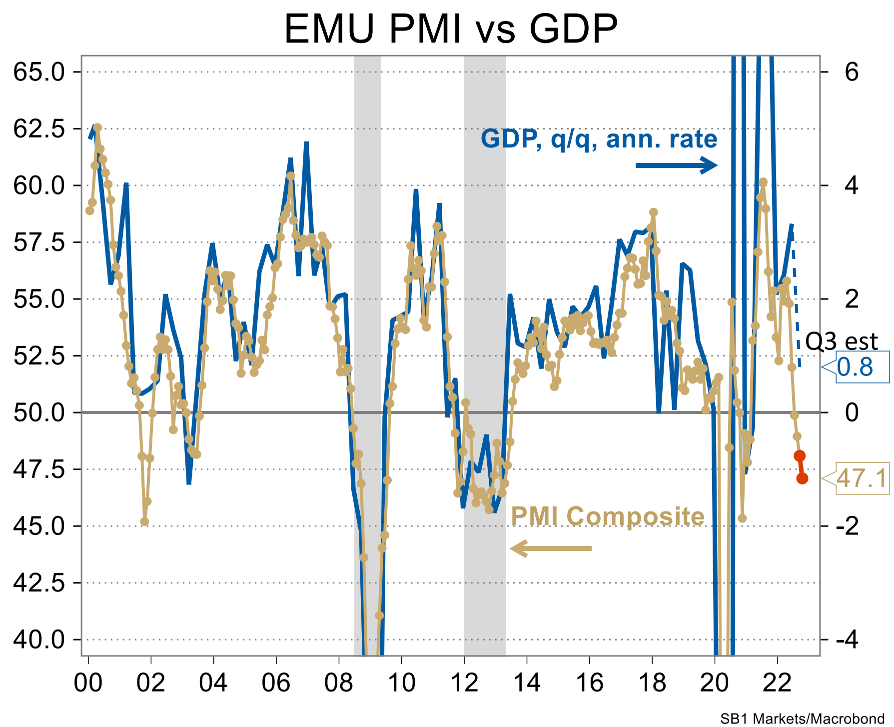


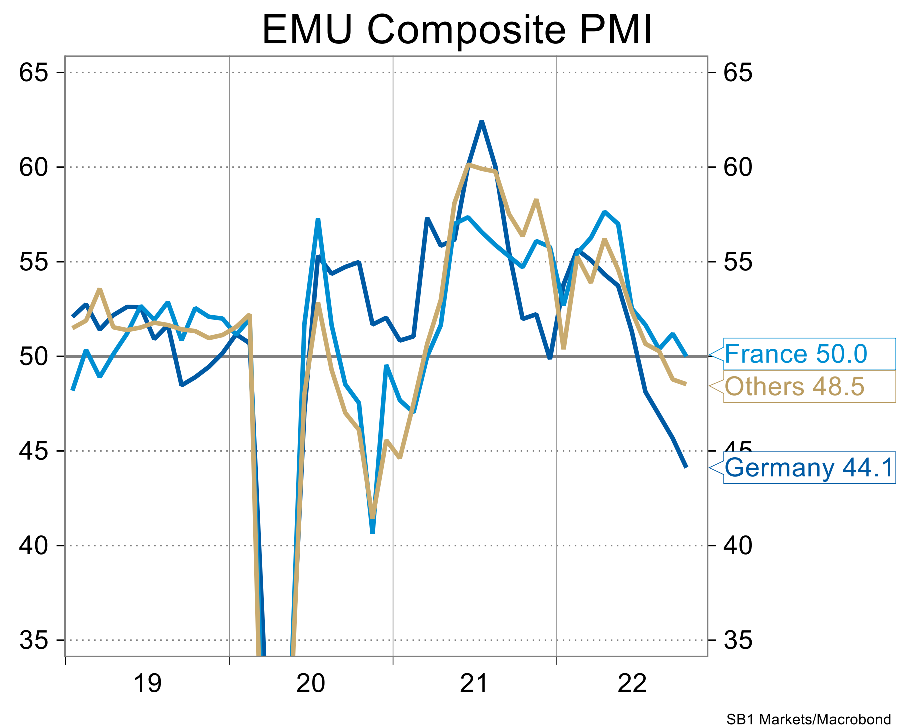


- Big picture: Growth is slowing sharply but manufacturing indices do not signal that the economy has entered a recession (even if order indices are really worrisome)

Eurozone PMI continues to slide, due to very weak German PMI data

The PMIs in EMU x France & Germany are also in contractionary territory

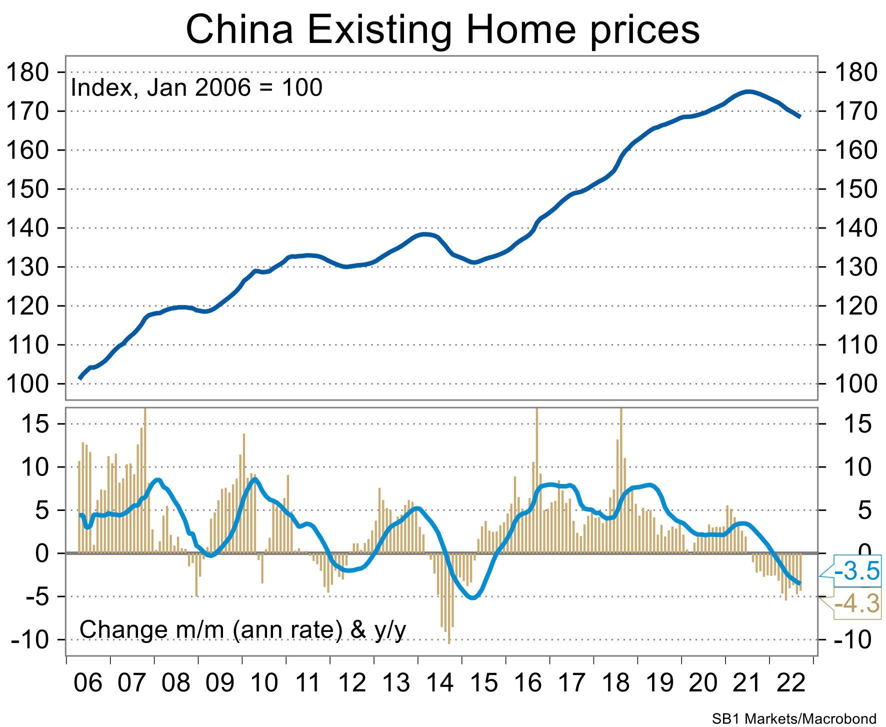


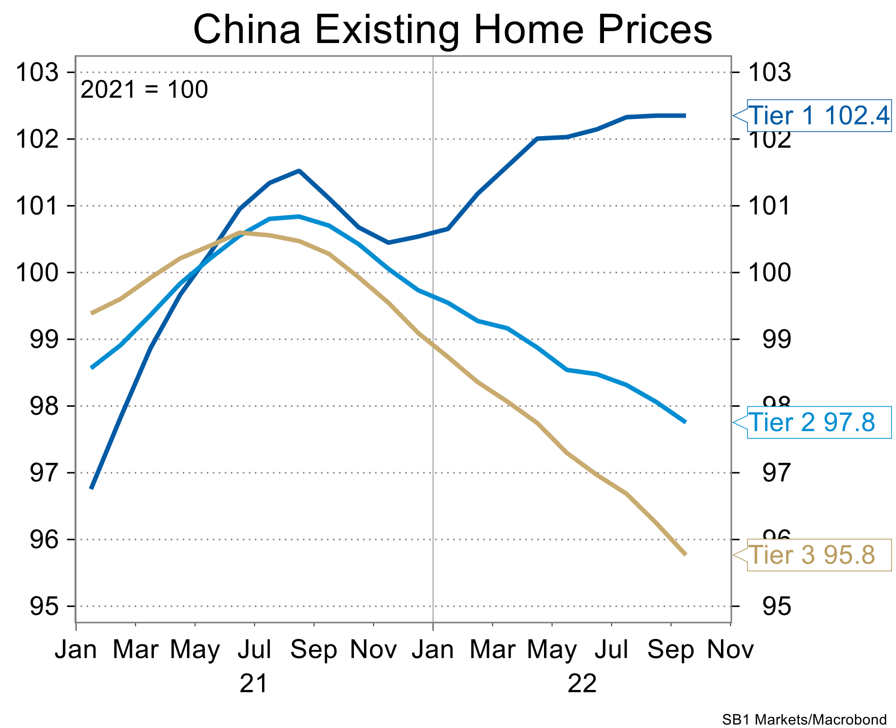


- **The composite PMI** declined 1 p in Oct, to 47.1, which is 0.4 p below expectations – signalling a 1% contraction in GDP in Q4. High inflation/energy prices and higher interest rates are dampening demand, according to S&P. The setback in the German economy is of course a drag on the overall EMU PMI. However, economic activity is falling across the region, and especially in the manufacturing sector
- **Services** fell 0.6 p to 48.2, suggesting that the sector is contracting
- **Manufacturing** also slowed further; the PMI fell 1.8 p to 46.6, 1.2 p below consensus. The output index decreased 2.1 p to 44.2, and the new order index declined by 3.5 p to 37.8, a level only reached twice before, during the pandemic and the financial crisis!
- **The delivery times** and price indices both fell but remain higher than normal. However, as new orders and production are both is declining, supply chains problems and pricing power will very likely be further reduced the coming months
- If the PMIs and other surveys continue down at the current pace, the pressure on (and within) the **ECB** to hike rates rapidly will no doubt fade, even if inflation is high and unemployment is low. Wage inflation has not yet exploded, and the underlying cost pressure is not like in the US

Existing home prices fell further in August – for the 13th month in row

- the longest stretch with falling prices ever. New home prices on the way down too

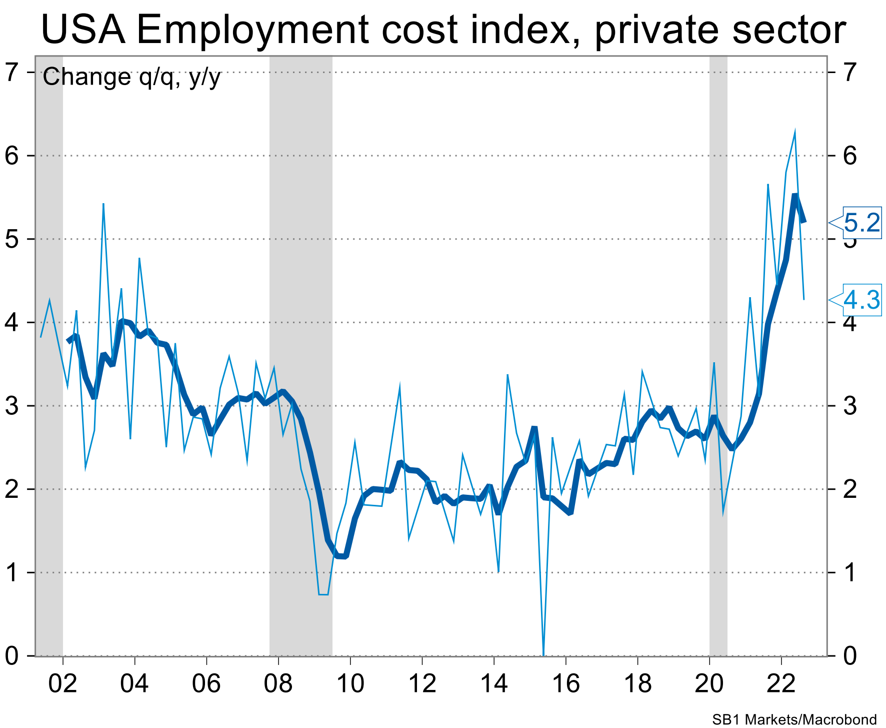


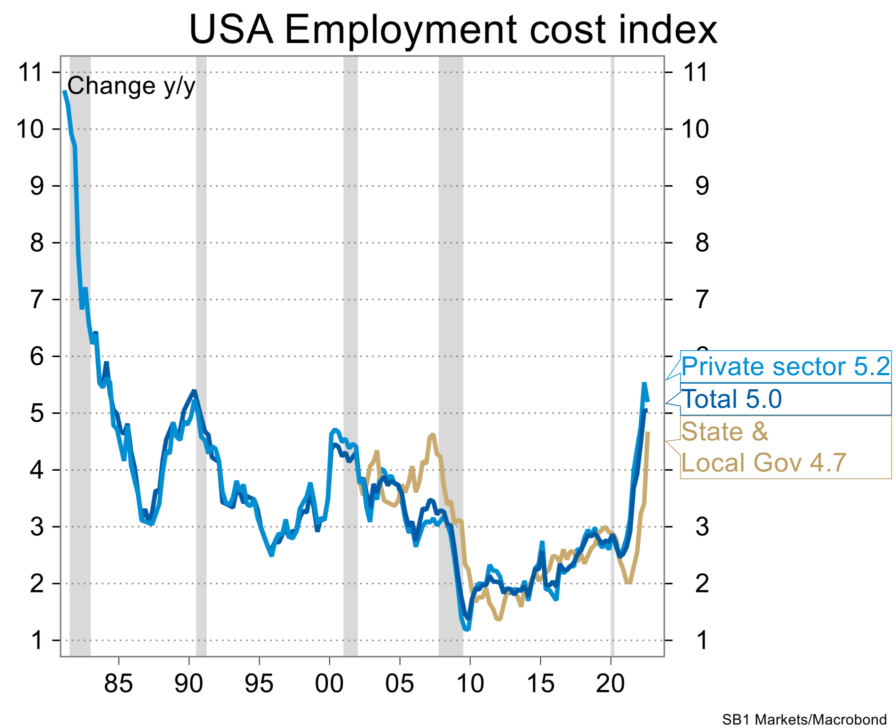


- **Existing home prices** peaked last July, and have been falling at a gradually faster pace, until May. In September, prices fell at 4.3% pace. Prices are down 3.5% y/y, less than the price setback in 2014/15. However, the current setback has now lasted longer than the previous
- **New home prices** also fell last autumn but at a slower pace than existing home prices. In September, prices fell 2.4%, and they are down 2.3% y/y. Some builders have reported deep price cuts to reduce the inventory and secure financing. The gradual decline in prices since last summer is probably due both some fire sales from construction companies that have run out of other sources of financing, and some hesitance from home buyers
- Prices are still climbing (albeit slowly) in the **four largest Tier 1 cities**, but are falling elsewhere – and at the fastest pace in the ‘smaller**’ Tier 3 cities**
- **Central authorities** have signalled willingness to expand credit supply again, both to finance infrastructure projects and the construction sector, mostly through local governments that would be allowed to borrow (even) more

Employment cost inflation fell in Q3, according to the ECI. Still far too high

ECI inflation is more than 2½ pp above the 10 y average – which yielded 2% CPI inflation

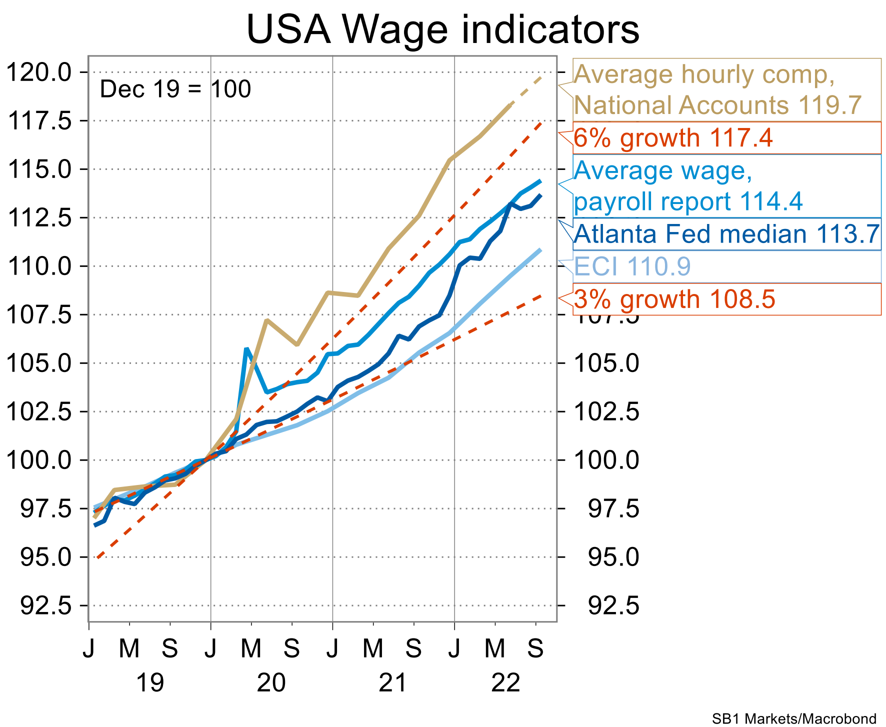


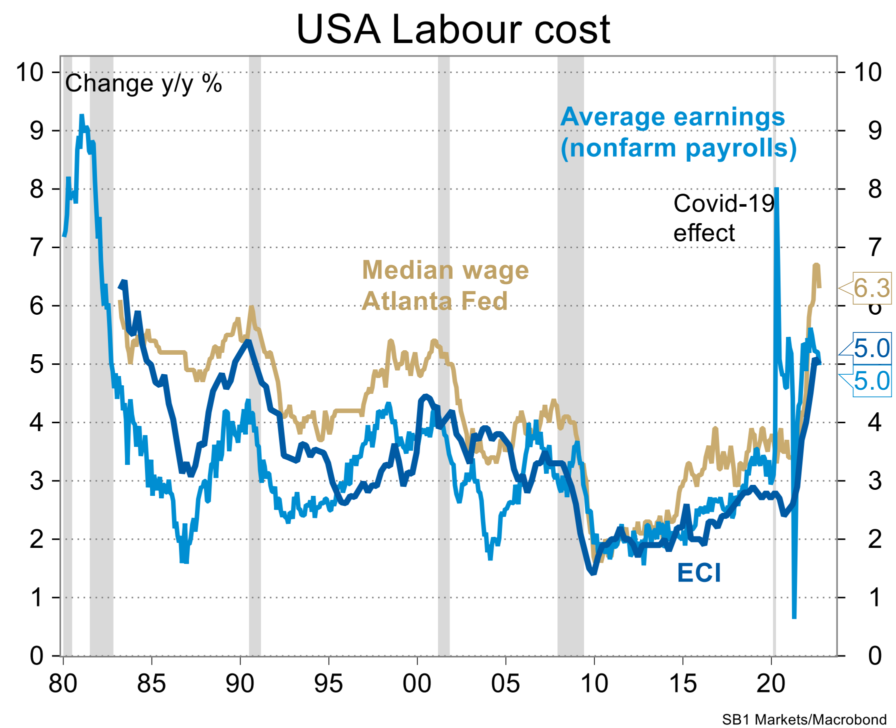


- The **Employment cost index for all civilian workers**, which measures wages and other wage costs for <u>the same types of jobs (and is not influenced by changes in employment between sectors/type jobs)</u>, rose by 1.2% q/q in Q3, as expected, and down from 1.3% in Q2. The annual rate was unchanged at 5.0%, the highest level since 1990, and ><u>2.5 pp above the 10 y average before the pandemic</u>
  - » In the private sector, the ECI rose by 1.1% q/q (4.3% annualised), down from the 'dramatic' 6.3% in Q2, when some bonus payments boosted the ECI. The average of Q2 and Q3 is at 5.3%. The annual growth is 5.2% y/y, down from 5.5% in Q2
  - » State and local gov employment costs shot up in Q3, to 4.7% from just 3.4% y/y, and the discrepancy to the private sector narrowed
- <u>**Wage inflation** is the real problem for the Fed, far more than the impact of high energy/food/raw material prices</u>. Those commodity prices are already on the way down, and the contribution to CPI inflation will come down

Wage inflation remains far too high, according to all wage indicators

Current wage inflation is 2.5 – 3.5 pp higher than the 10 y average before the pandemic

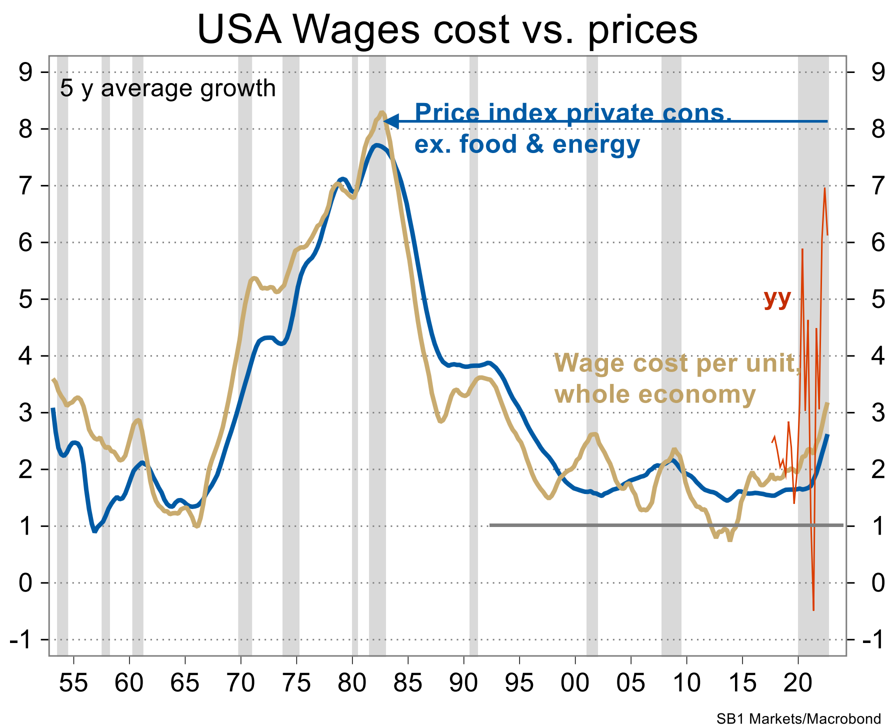


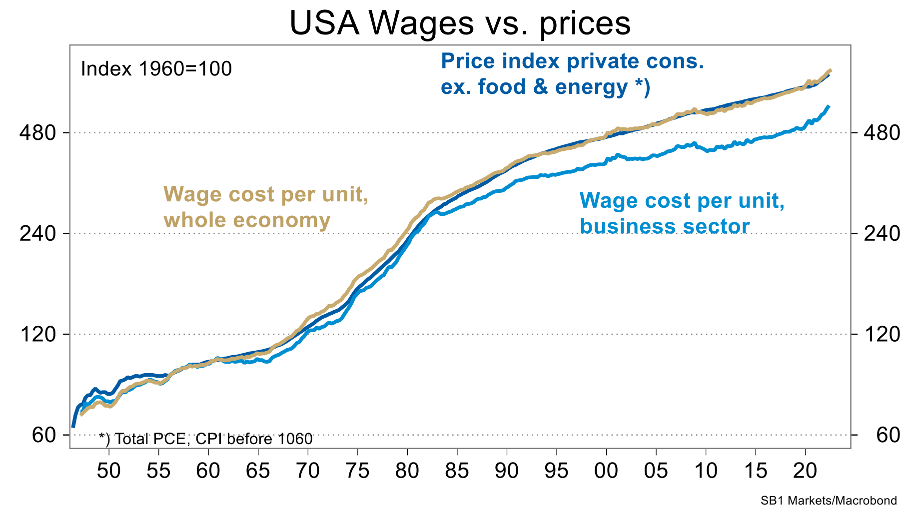


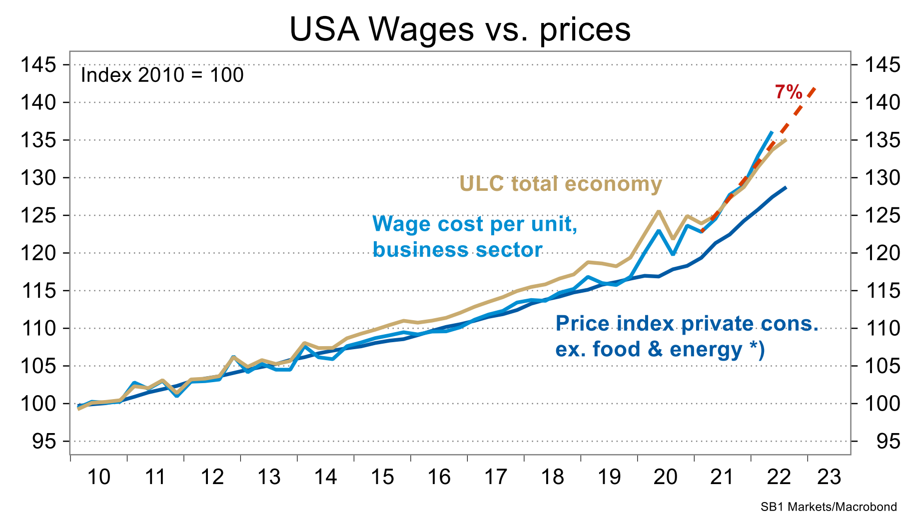
- **All wage indicators** are reporting faster wage growth, and all reporting wage growth well above the average over the recent years
- Over the past 10 years, inflation has been close to 2%, and well above 2% if calculated over a shorter period
- It will be a 'challenge' to keep CPI inflation at 2% if wage inflation remains 2.5 – 3.5 pp higher than rates that have produced 2% price inflation. 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 – aka a recession

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

Wage cost per unit produced in the whole economy is up 6% y/y



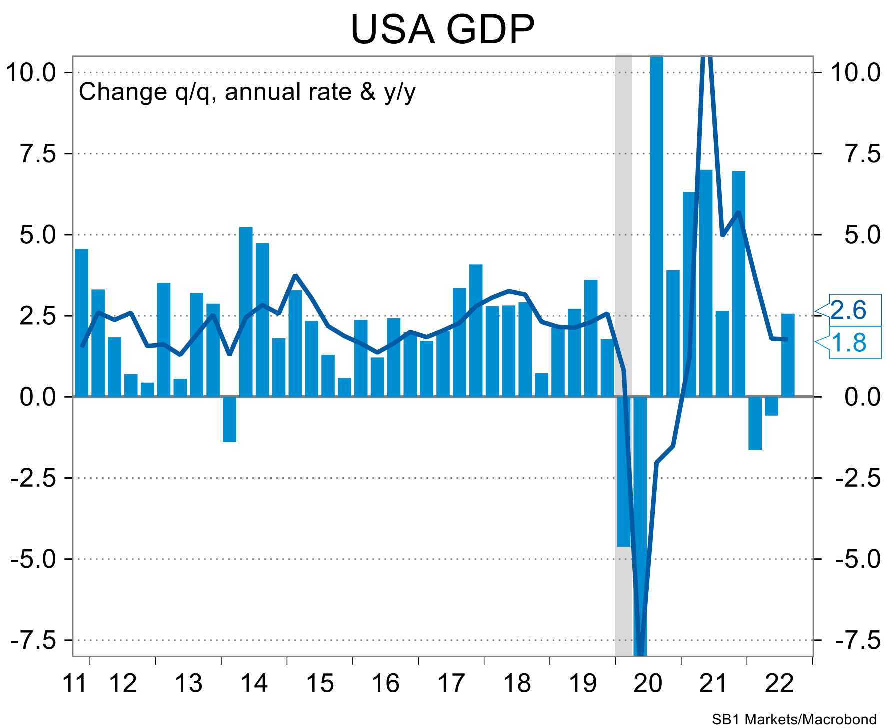


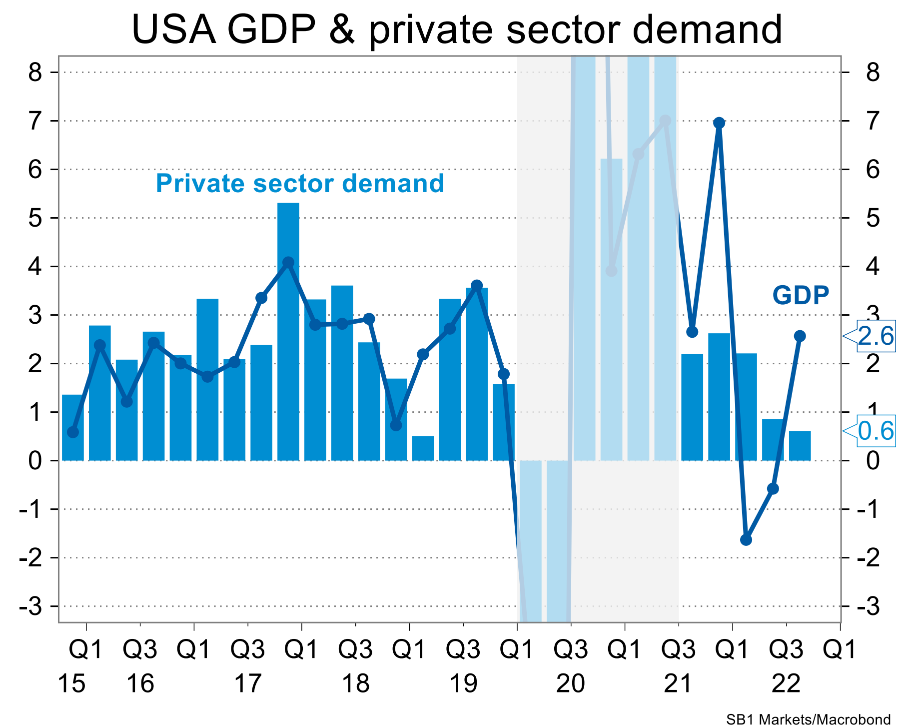


- **Labour cost per unit produced** (ULC) is the main, and in fact in practice the only, driver of inflation over time
- Now, the underlying growth in ULC is at 6% – 7%, yielding the same rate of inflation over time. That's Fed's challenge

GDP recovered in Q3, due to net exports. Domestic private demand up just 0.6%

GDP grew 2.6% in Q3, expected 2.3% - up from a -1.1% pace of decline in H1. So far in 2023: +0.3%

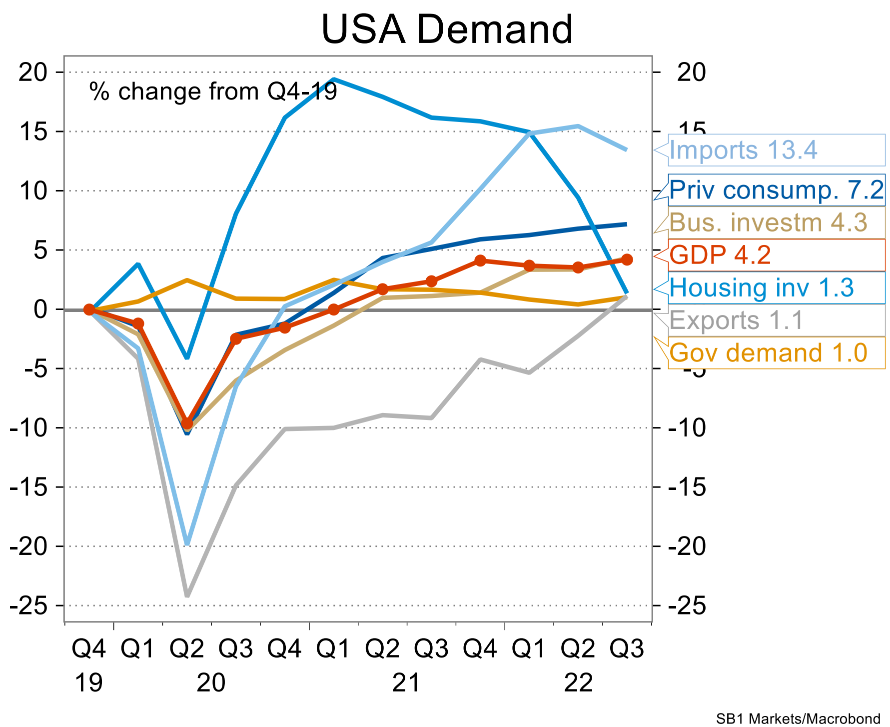


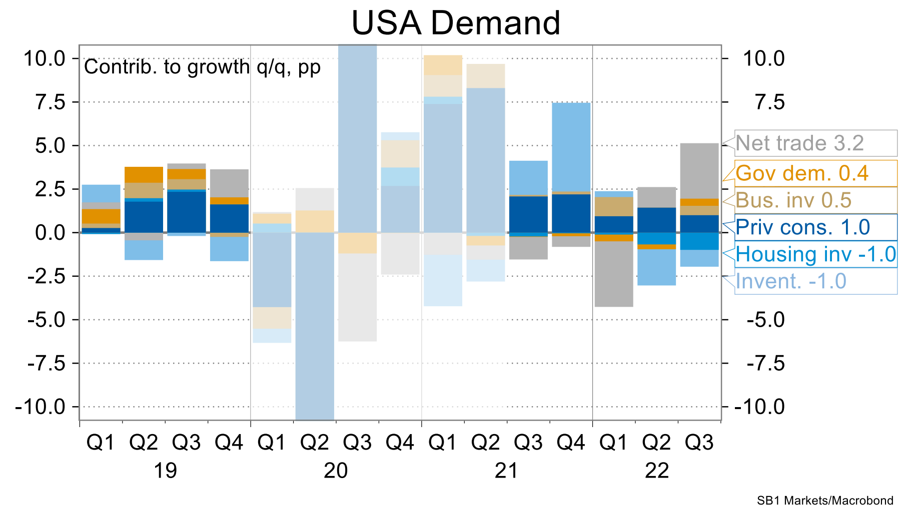


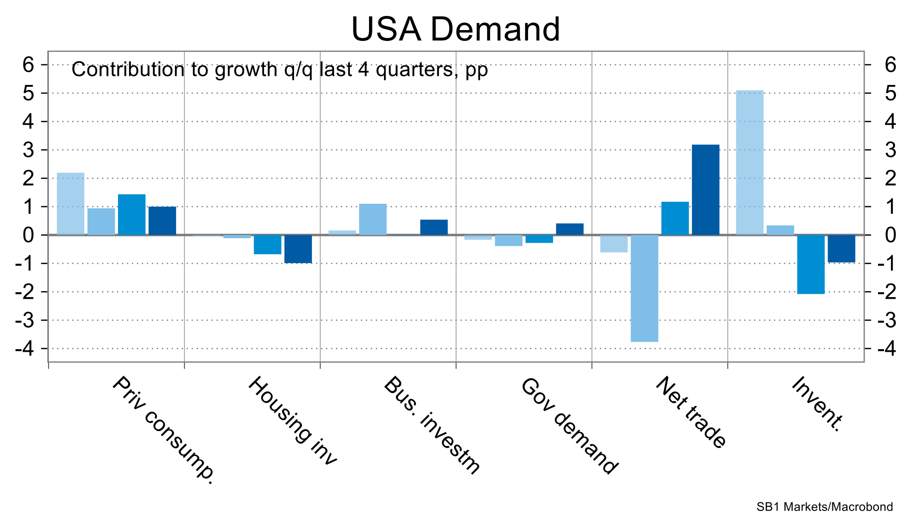
- Following a decline in both Q1 and Q2, GDP recovered in Q3, as imports fell and exports rose. Net trade lifted domestic production by 3.2%, that is more than the overall growth in GDP
- Growth in **private sector demand** has slowed the past three quarters, and fell to 0.6% in Q3. Private consumption rose 1.4%, more than expected, and contributed by 1 pp to GDP growth. Investments fell, due to business structures and housing. Housing fell 26%, deducting 1 pp from GDP growth!
- **Inventories** rose at a slower pace, which reduced GDP growth by 1 pp (and the net contribution from trade and inventories is 2.2 pp). Inventories may still be somewhat too high
- **Core PCE inflation** (Fed's price measure) slowed as expected to 4.5%, while the overall GDP deflator grew 'just' 4.1% in Q3, as energy prices fell
- We assume **corporate profits** flattened in Q3, as the total wage cost probably grew faster than value added

Higher exports, lower imports the story in Q3. And the 'collapse' in housing

Business investments rose slightly, while inventory build-up slowed



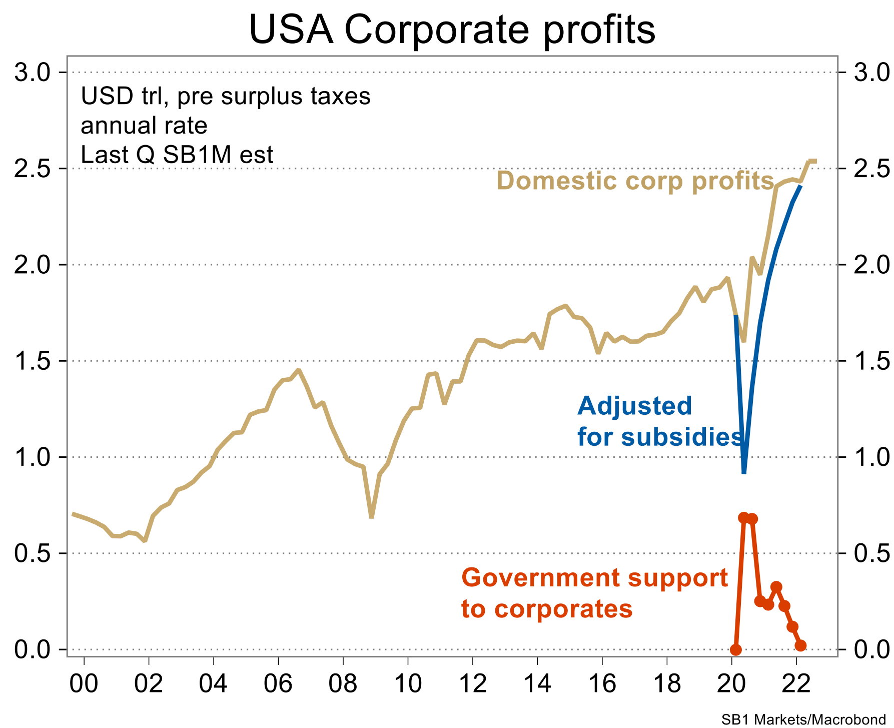


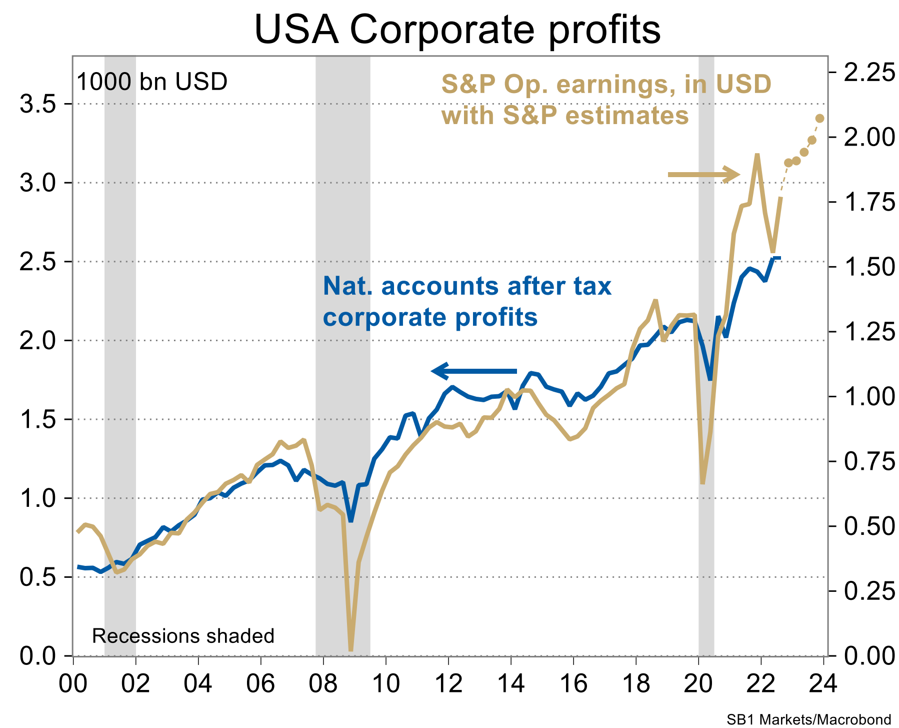


We have shaded the 'hard' pandemic quarters at the chart on the top

Corporates' profits flattened in Q3?

Some data are still missing but wage costs probably grew faster than value added

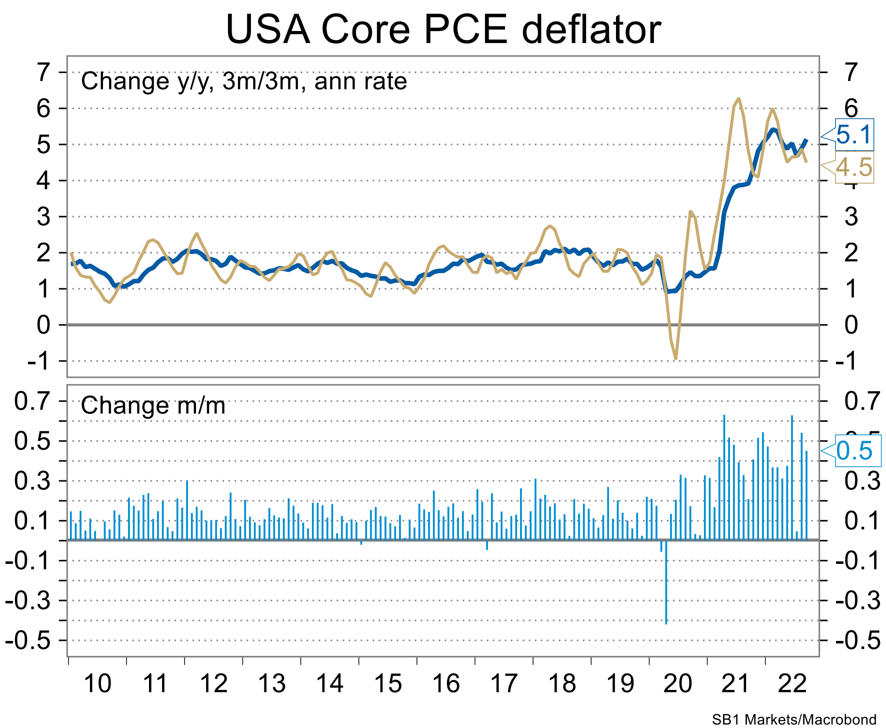


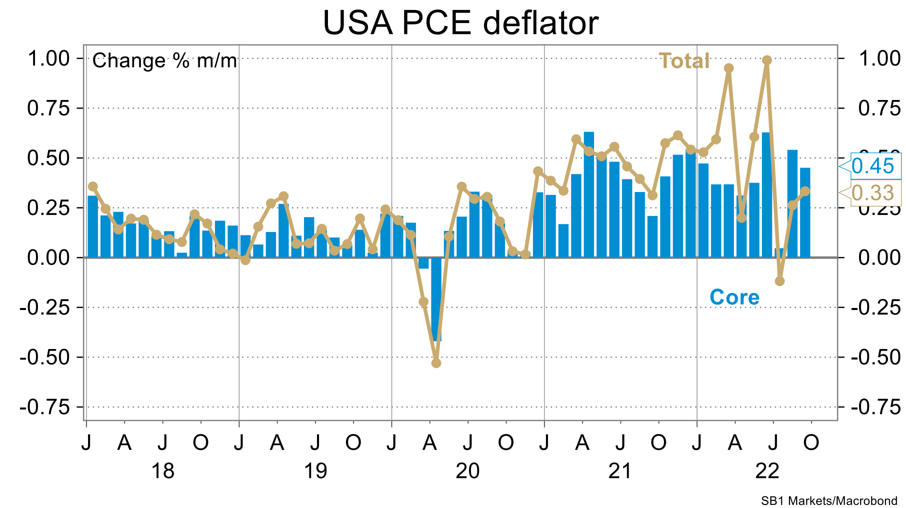


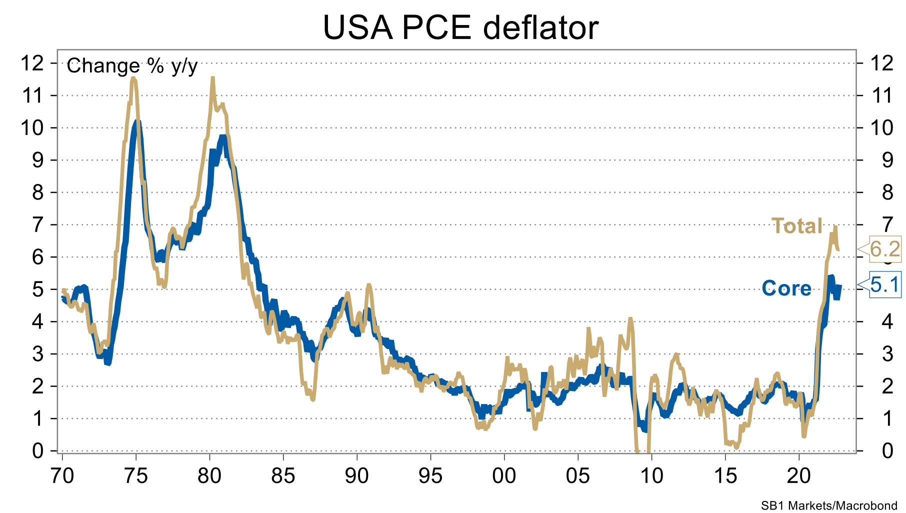
- **We assume domestic corporate profits** was unch. in Q3. Growth in nominal corporate GDP slowed (we assume to 1.5%, but the estimate is uncertain!), and that total compensation of employees rose by 1.8%, the highest since Q4 last year. Net tax payments/subsidies have normalised, no more 'covid support'
- The **S&P** estimates that S&P 500 profits rose by some 14% (q/q, and up just 3% y/y) in Q3 following the more than 10% decline in Q1 (seasonally adjusted). S&P profits (including profits from abroad, measured in a strong USD!) are still way above normal vs National Account profits for the total corporate sector (including all corporates operating in the US, domestically or foreign owned). Thus, a downside risk for S&P 500 earnings? (S&P's forecast is usually far to optimistic, at this time a quarter ago, they expected 2% growth in Q2 operating earnings. Now, it turns out they fell by 7%)
- We think the **profit outlook** is bleak. Wage inflation will not subside immediately given the super tight labour market – and a continued price inflation at the current pace does not seem to be tolerated anymore by the Federal Reserve. Exciting times ahead

Core inflation up in line with expectations in September; August data revised down

The core PCE deflator rose by 0.5%, in line with expectations. The annual rate is now at 5.1%



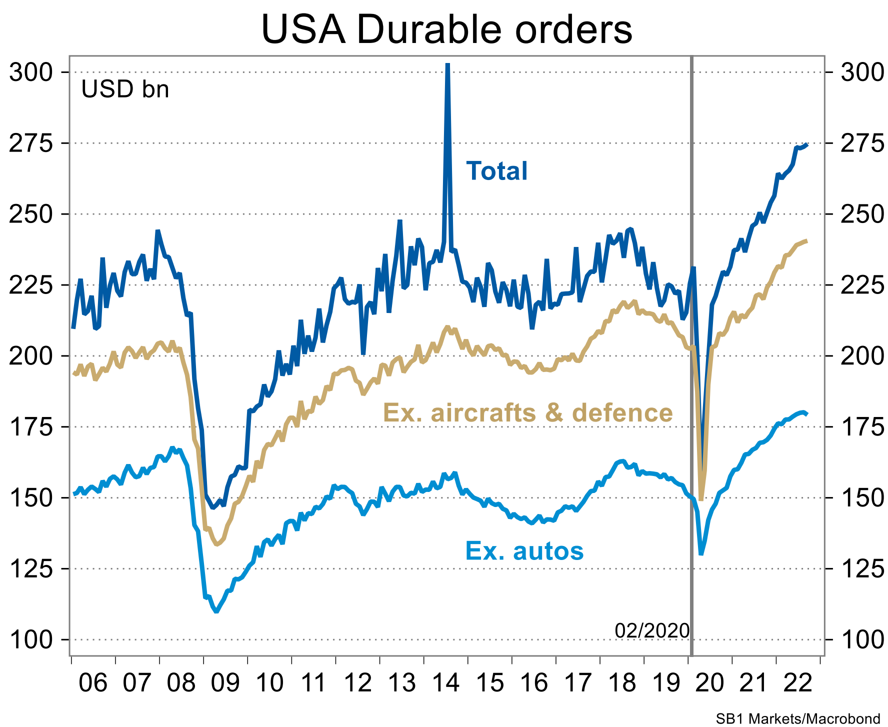


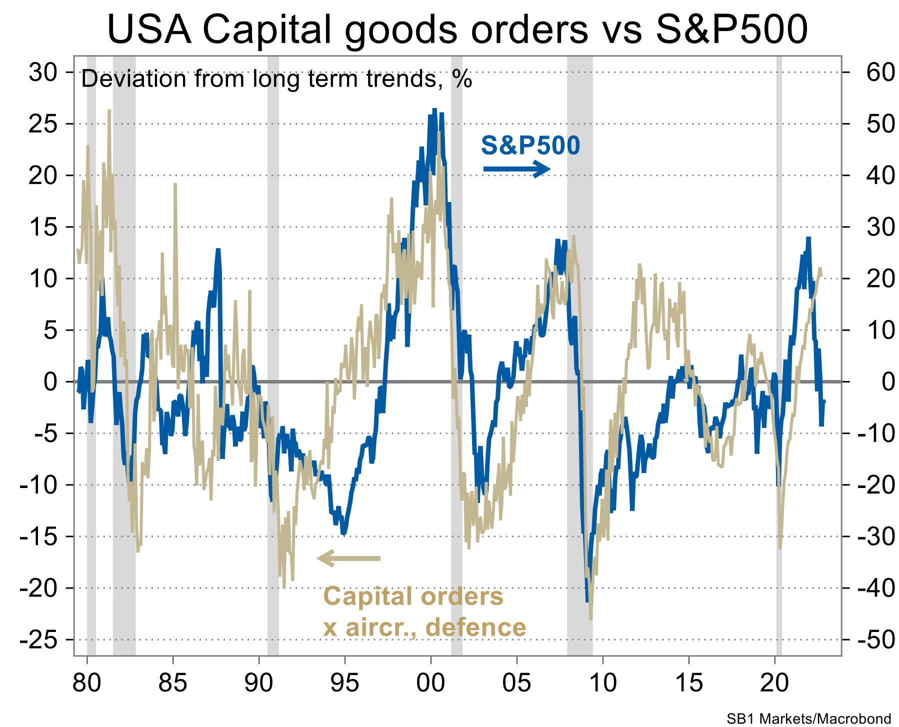


- **The core PCE** August print was revised down by 0.1 pp to 0.5%, and in September prices rose by 0.451%, thus close to 0.4%, down from 0.6% in August. The annual rate was at 5.1%, up from 4.9% in August, and 0.1 pp lower than expected. The annual rate peaked at 5.4% in February
- **The total PCE deflator** was up 0.3% in September, as expected. The annual rate at 6.2% was 0.1 pp lower than expected. The peak was at 7.0% in June

Growth in orders slows but still far better than 'all' business surveys signal

Strong defence, aircraft and auto imports support overall order growth

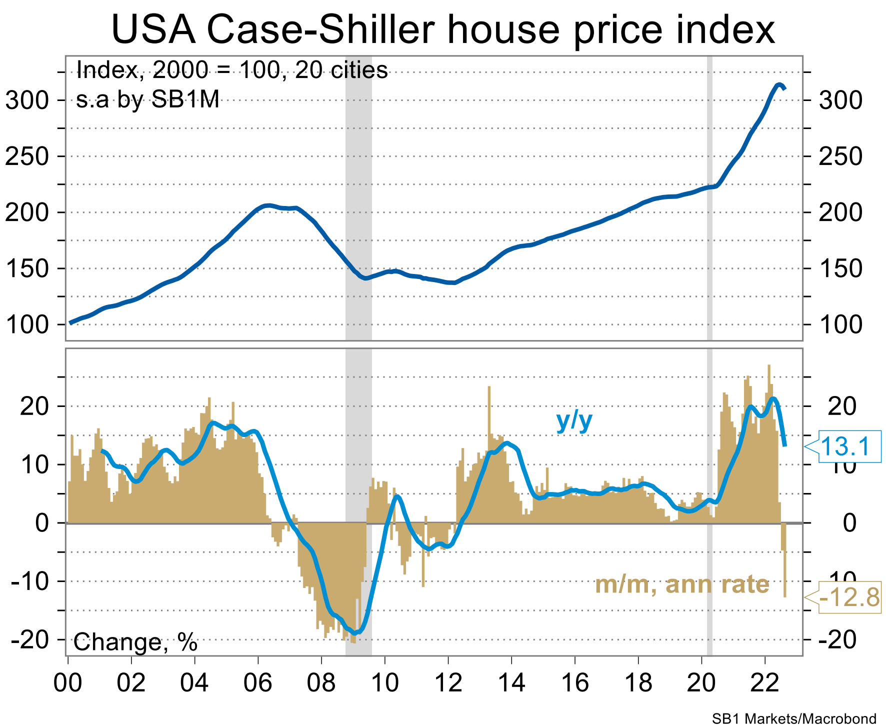


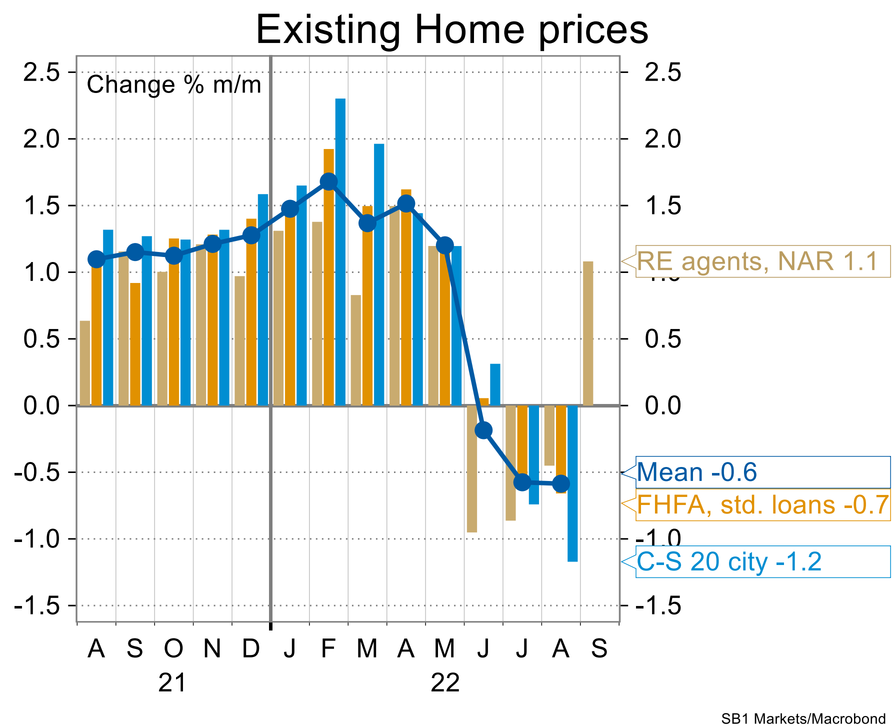


- **Total durable** orders gained 0.4% in September, expected up 0.6%
- The volatile aircraft & defence orders rose sharply, and **other orders** (our core concept) were up 'just' 0.2%. Growth has slowed, but orders are still up almost 5% 3m/3m, although in nominal terms
- **Core investment goods orders** fell 0.8%, expected up. Underlying growth has clearly slowed, an August may have been the peak
- **Order inflow** is far above pre-pandemic levels, especially for investment good orders, but surveys now signal a significant decline the coming months (which they have indicated since June, so far without any success)
- The stock market has taken a serious beating, this time well before the order cycle turned south. Higher real interest rate were probably enough

The decline in house prices is accelerating, Case/Shiller down 1.2% in August

Prices are still up 13.1% y/y, but the sign may soon change

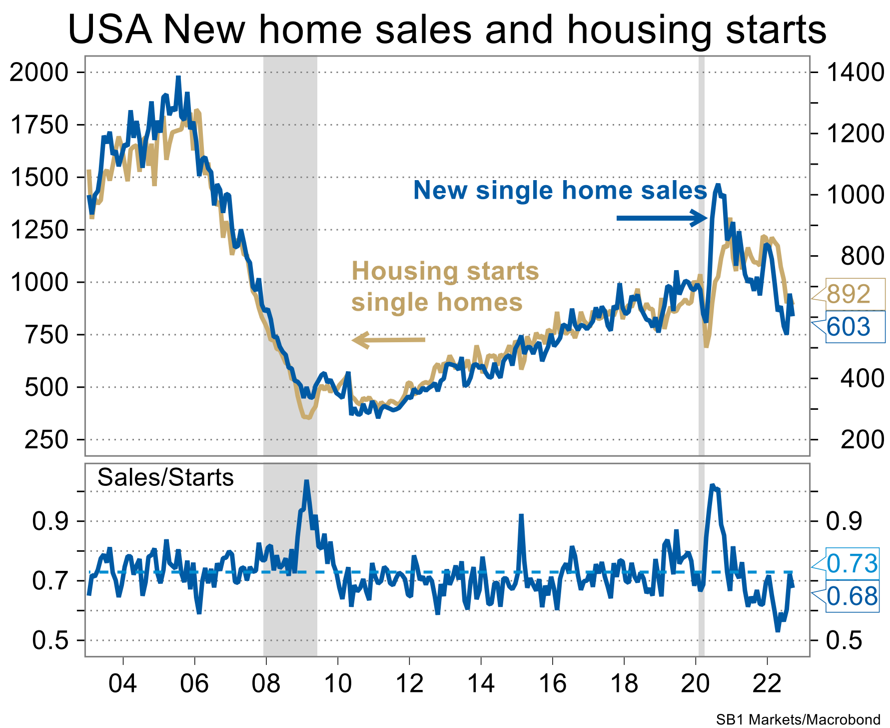


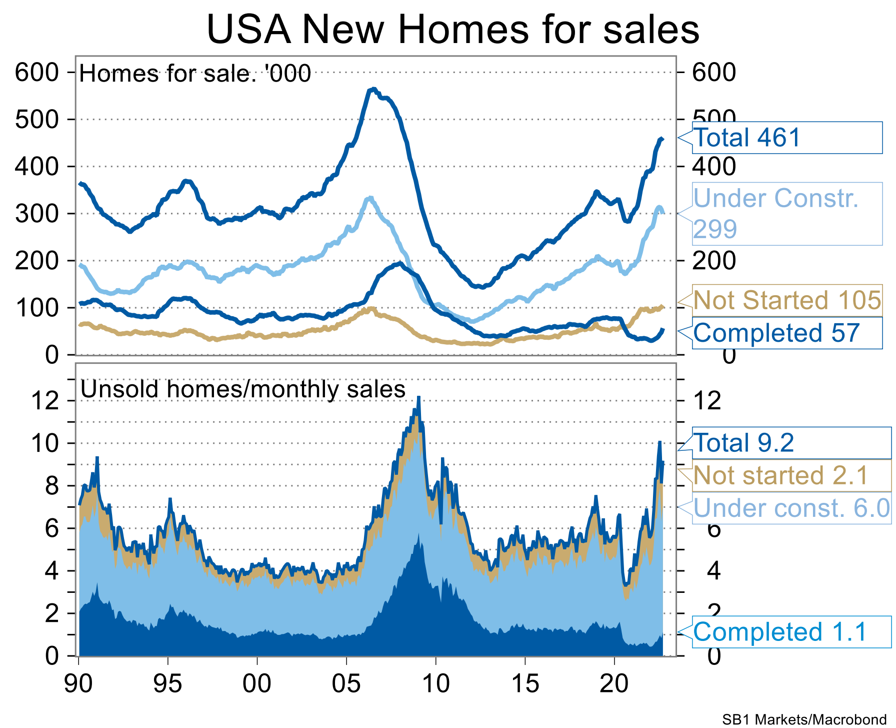


- **S&P's Case/Shiller's 20 cities** price index fell by 1.2% in August (July - Sept avg., our seas. adj, -1.3% the 'official' seasonal adjustment) expected down 0.5% – 0.8%), equalling a -12.8% annualised pace. The decline in July was revised up to 0.7% from 0.5%. The index is still up 13.1% - down from 16% in July
- **The FHFA** (Federal Housing Financing Agency) price index, which covers homes with loans guarantied by the government sponsored Fannie Mae or Freddie Mac ('Husbankene', has a countrywide coverage), was down 0.7% in August, and is up almost 12% y/y
- **Realtors** reported a 1.1% increase in home prices in September, which we doubt is the 'real' change in house prices last month. Prices are up 8.5% y/y
- <u>We still expect prices to yield substantially the coming months, following the unprecedented 42% lift since before the pandemic to the peak in June, and the surge in mortgage rates, up to 7.5% (30 y fixed), from 4% before the pandemic: affordability is totally crushed!</u>

New home sales down in September, very likely much more to go

The trend is set, and home builders are signalling a further, large decline

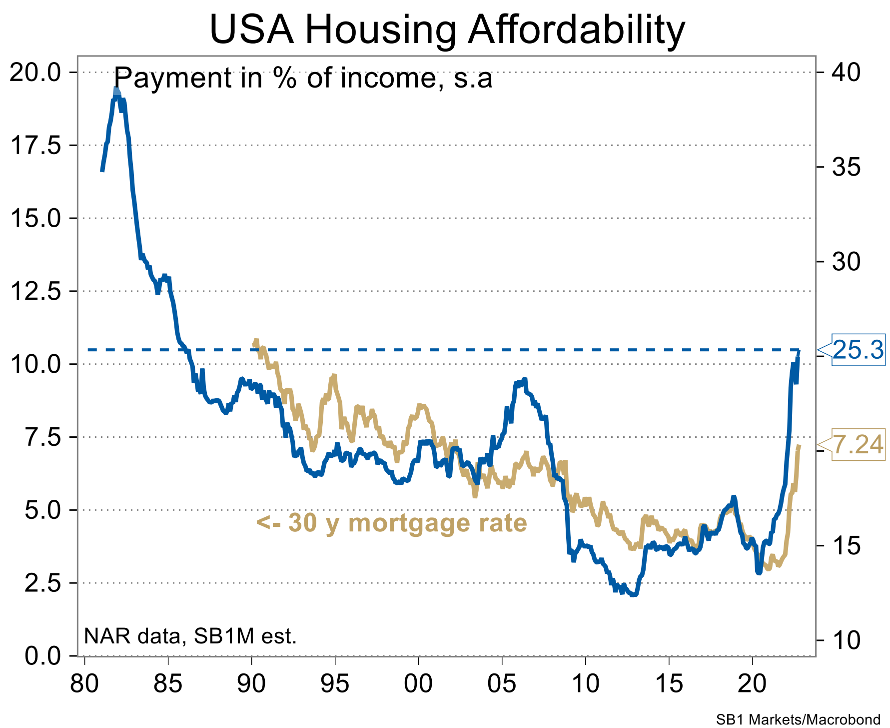


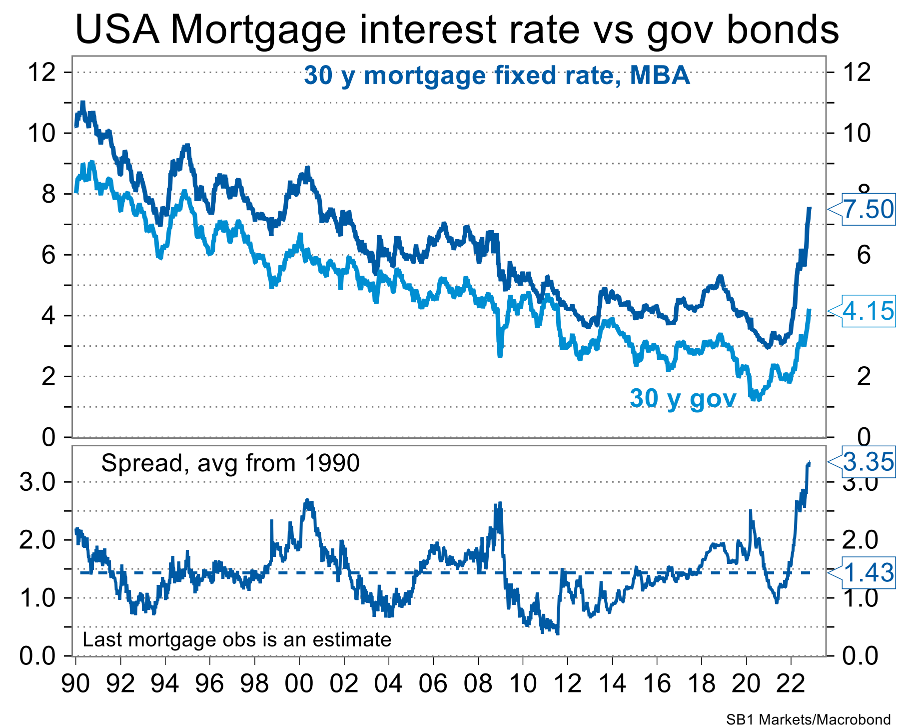


- **New single home sales** surprised sharply on the upside in August, and just a smaller part than expected of the lift was reversed in September. Sales fell to 603, expected 581, down from 677' in August. In July, sales were down at 543'! Anyway, the trend is down, home builders are extremely anxious, demand for new mortgages are falling rapidly.
- **The inventory of unsold homes** fell marginally in September, but the trend is straight up, and the level is high, both in absolute terms, and vs. sales – the latter not that far from ATH, at 9.2 months of sales. Most of the inventory is 'for real', either completed homes (but the level in this category is still very low) or under construction (and these homes will be completed) – as the supply side responded to the strong increase in demand & prices. A steep increase in number of homes for sales that are not yet started, also confirms the strength of the potential supply side (but most of these projects will very likely not be started as at least the housing market has entered a recession)
- Prices increased slightly in September but the short term trend is flat – and very likely, prices will soon turn south

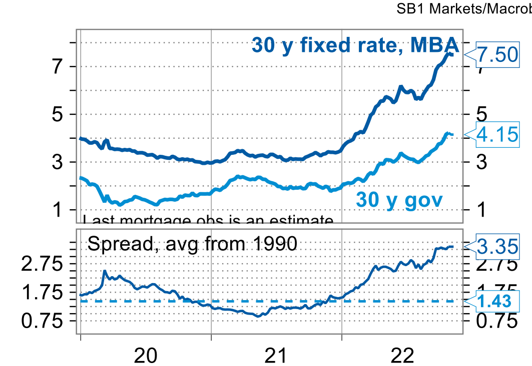
A mortgage market meltdown, the margin to 30 y gov bond unprecedented!

The effective mortgage 30 y rate at 7.50%, a 20 year peak. Will the Fed be forced to do a 'BoE'?



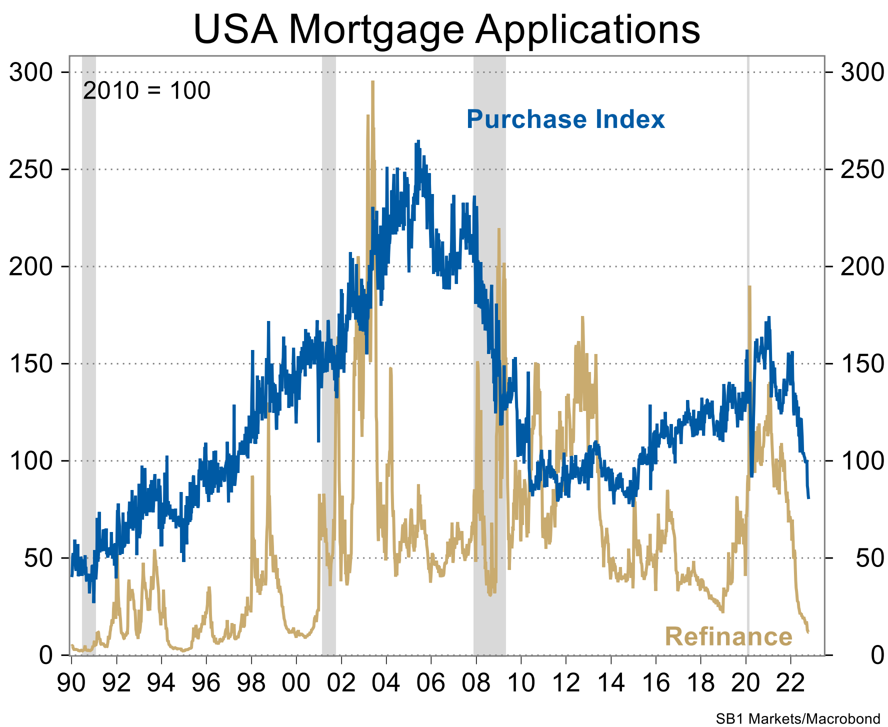


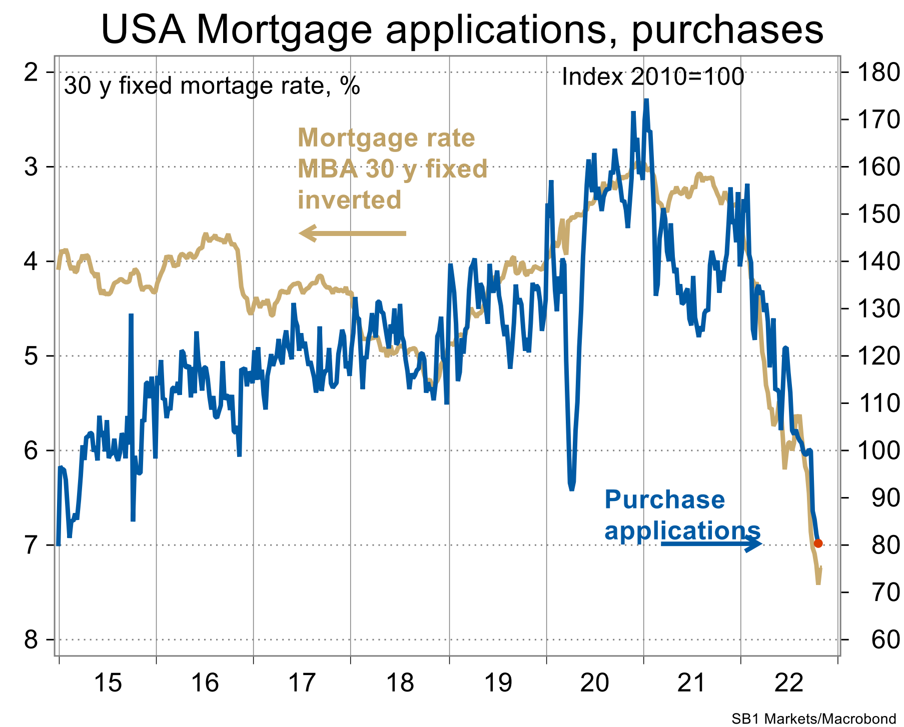
- The 30 y fixed mortgage rate has shot recent weeks (and months), both due to higher 30 y gov. bond rate and a dramatic widening of the spread up to the mortgage rate. The spread was 0.9 pp at the bottom when the Federal Reserve snapped up all net mortgage bond issuances even if prices rose 20% y/y. Now the Fed is selling mortgage backed bonds, and the spread is above 3.30%
- At which stage will the Fed decide that the market is not working, and that is has to start buying bonds again, just like the Bank of England had to do in order to prevent a completely meltdown in the UK gilt market last months? We think that we are not that far away, probably far less than 100 bps
- Housing affordability (house price x mortgage rate/income) is the deteriorating by the day – to the worst level since 1986!



Mortgage applications have plummeted, for good reasons

Applications for new loans are down by <u>49%</u> from the local peak in January, and are still falling

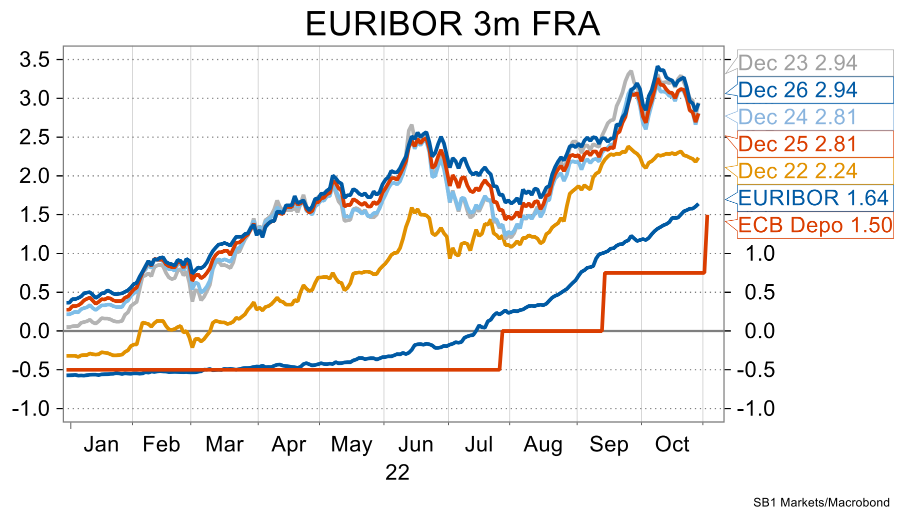


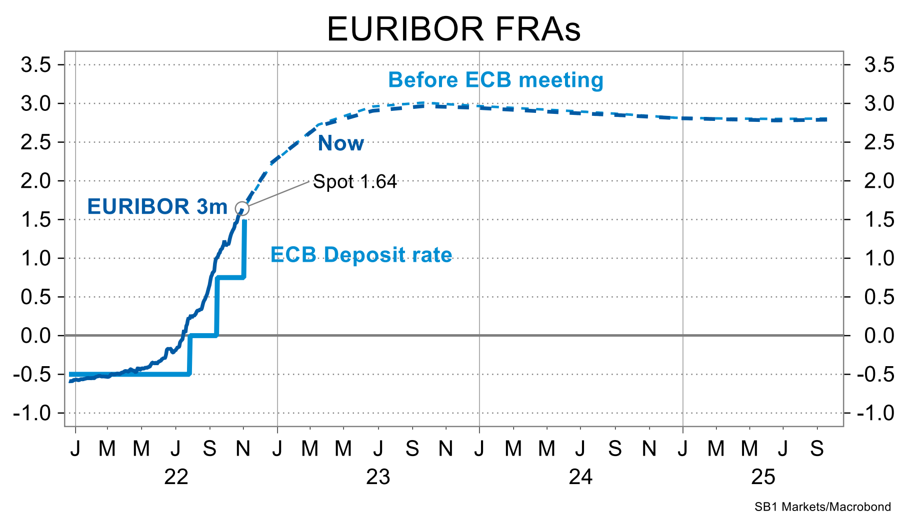


- Demand is now on the low end – 40% below the pre-pandemic level, not far above the bottom during the financial crisis
- Recently, mortgage rates have risen, alongside the increase in the 30-year treasury bond rate
- ‘Nobody’ is refinancing, for good reasons, given the current mortgage rate

ECB doubles rate in an already weakening economy but signals a slower pace?

The ECB hiked the signal rate by 75 bps - *«because inflation is far too high»*

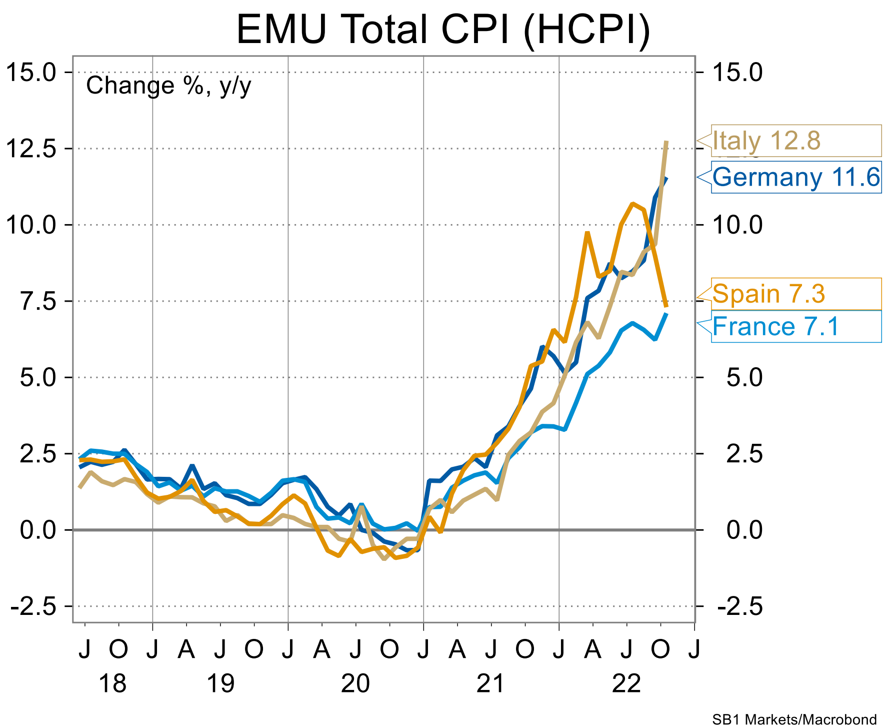


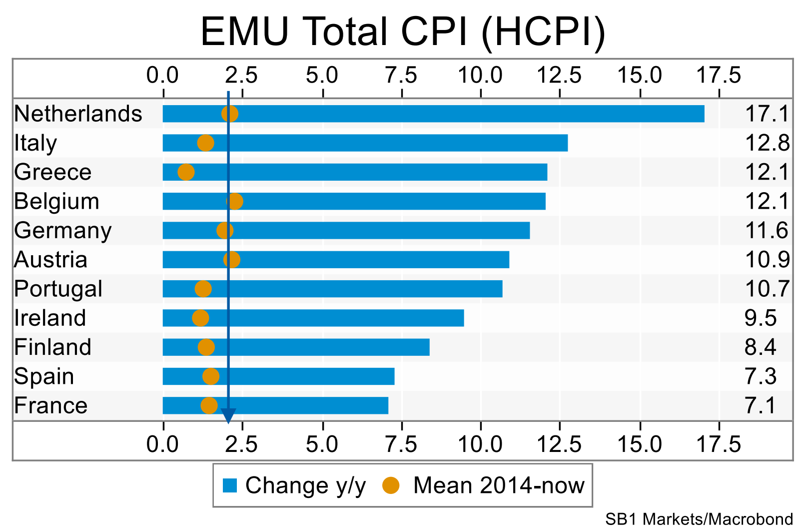


- **The 75 bps hike** was expected by the majority of economists as inflation data had continued to surprise on the upside, but the market had expected the bank to be slightly more hawkish and the FRAs fell after the decision as the wording of their statement was changed to hiking rates "for several meetings" to "the council… expects to raise interest rates further". All despite the bank recognising that demand is softening and that the risk of a recession has increased, but that they are data that indicate that are wages picking up (Is the bank seeing something we are not?)
- The bank repeated its statement **that inflation is far too high** and likely to stay above target for an extended period, and that the bank stands ready to adjust all of its instruments within their mandate to bring down inflation
- The bank also made changes to **the TLTRO III programme** (encouraging bank lending). Rates will now be indexed to average ECB interest rates (these rates used to be 50 bps below the ECB deposit rate, and for some it could be in the range of -1% to -0.5%) and three voluntary repayment dates are introduced for banks who want to reduce borrowing. In addition, **the minimum reserves** are now to be renumerated at the deposit facility rate (currently at 1.5%) as opposed to the main refinancing operations rate (2%)
- Largarde repeated several times that the ECB has **made significant progress to withdraw monetary accommodation and that it has more ground to cover and that there are more hikes in the pipeline.** The president also stated that while the risk of a recession has increased - the ECB's job is to bring down inflation
- At the same time, the bank continued **not to give a forward guidance**. Rather the bank said it will be data dependent and follow a meeting-by-meeting approach (central banks always do that anyway, even with a forward guidance), and focus on three factors: inflation outlook, measures taken so far, and the transmission lag of monetary policy
- **Short term market rates** fell after the announcement. Longer dated EURIBOR FRAs also fell, but less than in the short end. Long term yields fell almost 20 bps. The market is realising that the rate hikes are starting to work and that the economic outlook has already weakened. However, at Friday the short end of the curve turned up again

Inflation further up in October, to 11.6% in Germany, 12.8% in Italy

… at least according to preliminary data. Inflation in Spain down to 7.3%, due to energy subsidies

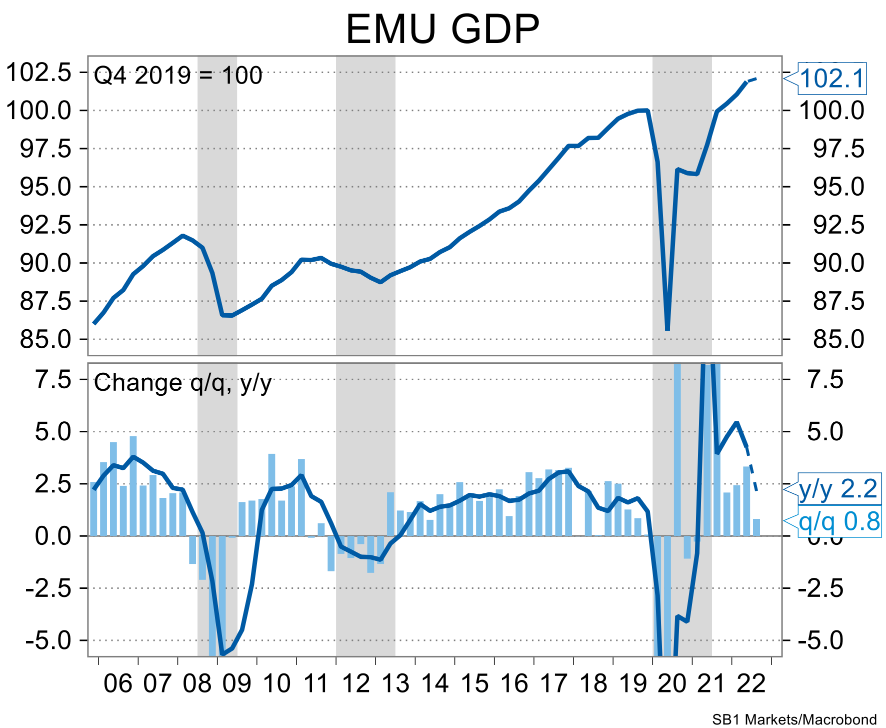


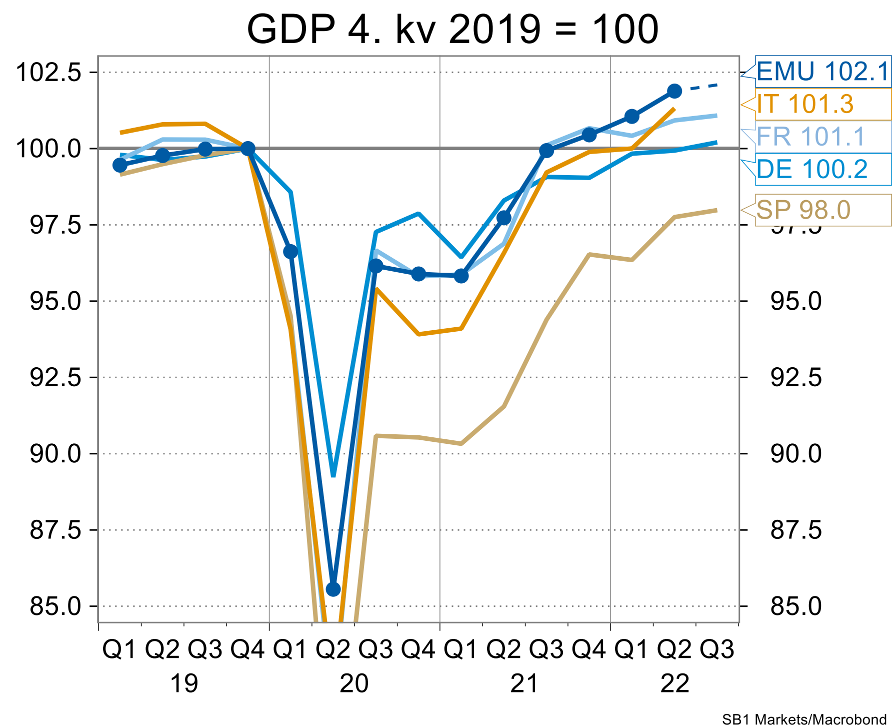


- More details in the final numbers

Q3 GDP better than expected but not impressive, of course, up 0.8% (annualised)

GDP marginally up in both Germany, France and Spain, EMU in sum up 0.2%, if Italy does not disap.

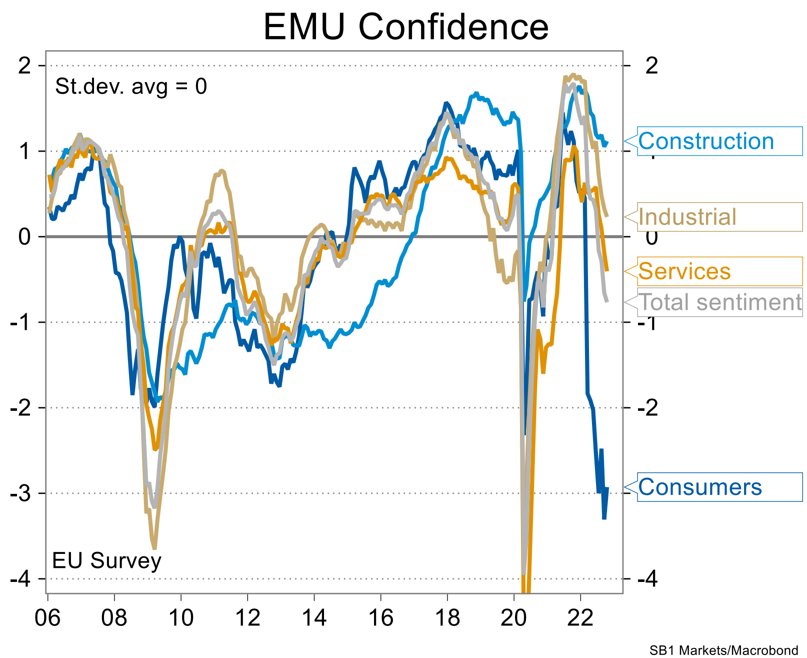


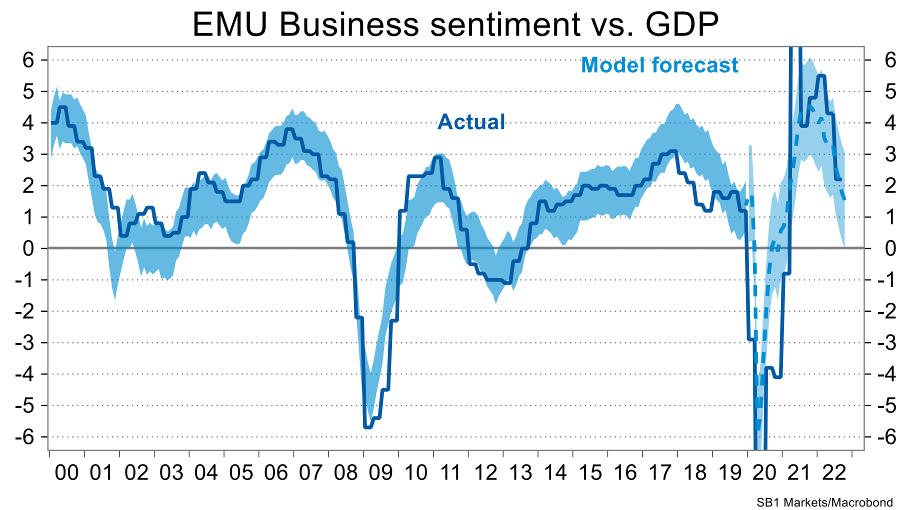


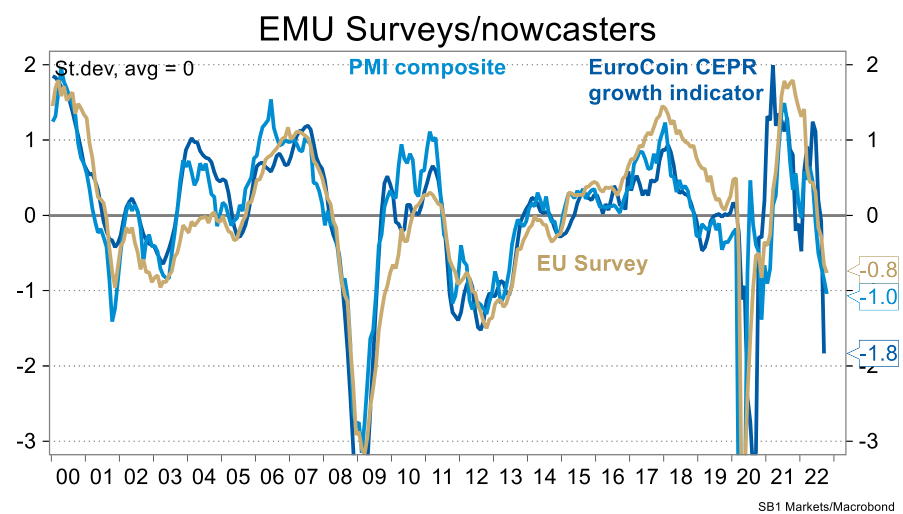
- German GDP up 0.3% (not annualised), expected -0.3%
- France + 0,2%, as expected
- Spain +0.2%

Economic sentiment further down but businesses are still reporting growth!

The overall index fell 1.1 p to 92.5 in October. Consumer confidence up but remains at -3 st.dev



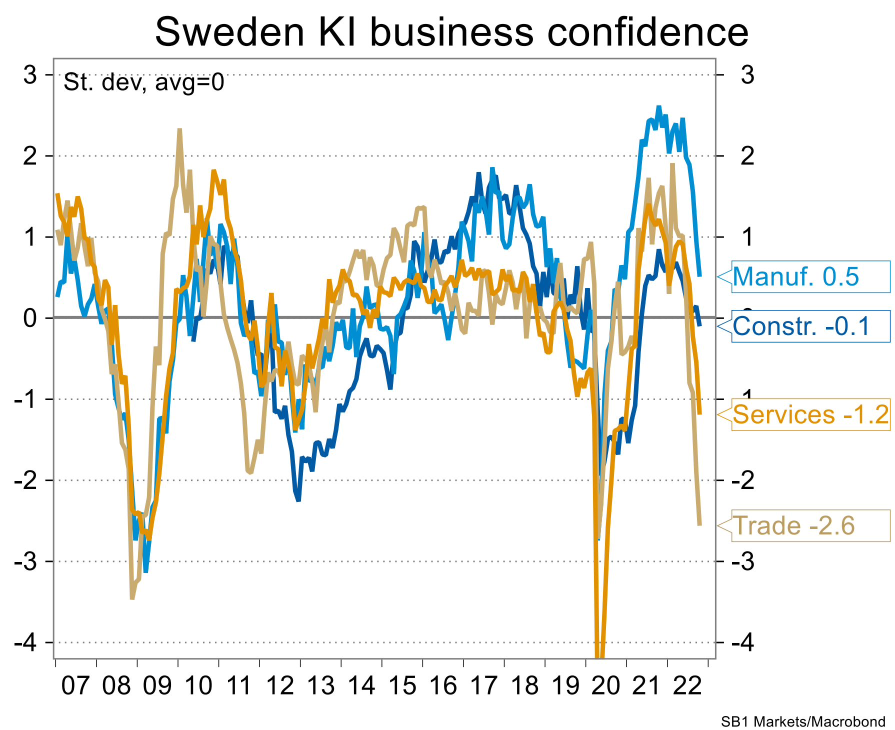


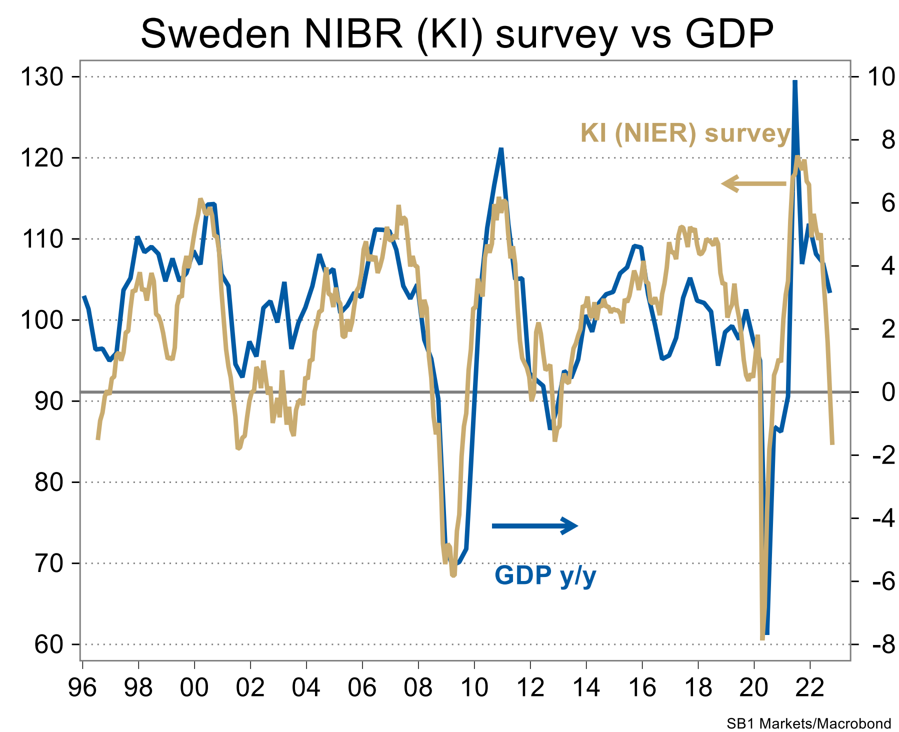


- **The Economic sentiment index** is 0.8 st.dev below average, with a large contribution from households. Businesses are on average above (+0.1 st.dev) – but surely rapidly on the way down, and the service index fell fell further to 0.4 st.dev below average
- Thus, even if there is war nearby and inflation is surging, businesses are still reporting growth marginally above trend. Consumers are pessimistic but historically their views on the economy has been irrelevant vs. GDP growth, just businesses tell us something relevant, at least vs GDP
- **All of the surveys we follow are now signalling growth at (or mostly) below trend,** or an outright recession (like the EMU PMIs, and CEPR's EuroCoin GDP indicator

Business confidence deteriorated further in Oct, a decline in GDP is signalled

Confidence in the manufacturing is still above average, other sectors are below. Trade at the bottom

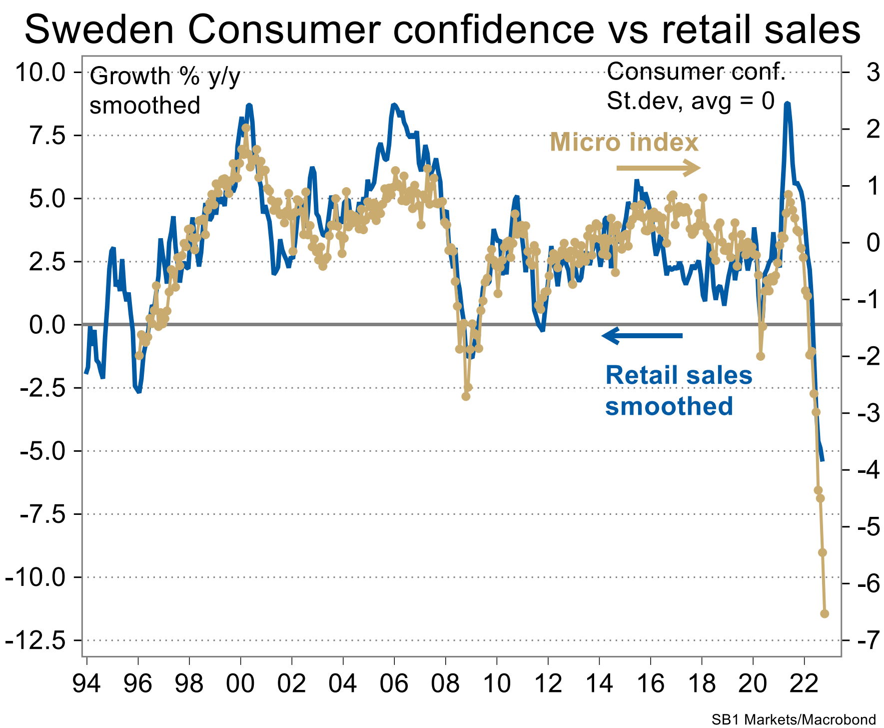


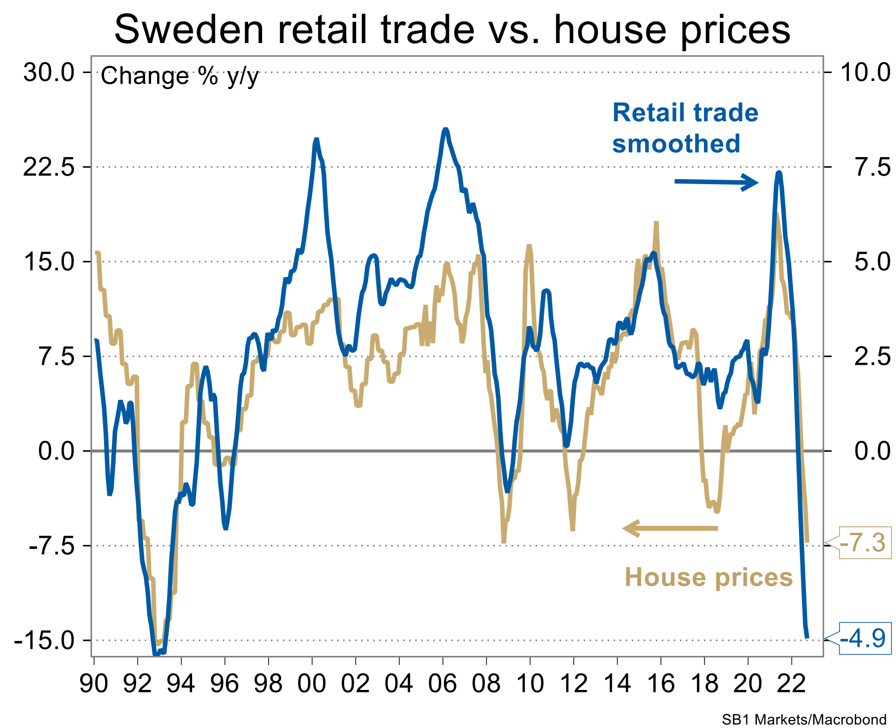


- **The composite index** fell to 84.6 in October from 90.8 in September, probably more than expected. The decline equals a 0.6 st.dev decline to 1.5 st.dev below average. The index signals a 2% GDP contraction, down from +2% in August. The Riksbank expects a small increase in GDP in Q3 (q/q) but then a 0.9% (total) decline in Q4 and Q1
- **4 out of 4 main sub-sectors** are reporting declining confidence, and just manufacturing still above average
  - » The **trade sector confidence plummeted** in Sept, and is now 2.5 st.dev under water
  - » The **manufacturing sector sentiment** has declined over the past three months, however, manufacturing sector sentiment remains above average, **construction** is jus below par – but is probably exposed due to the turnaround in the real estate market
  - » **Services** are at -1.2 below average

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

House prices and retail sales down in tandem with consumer confidence

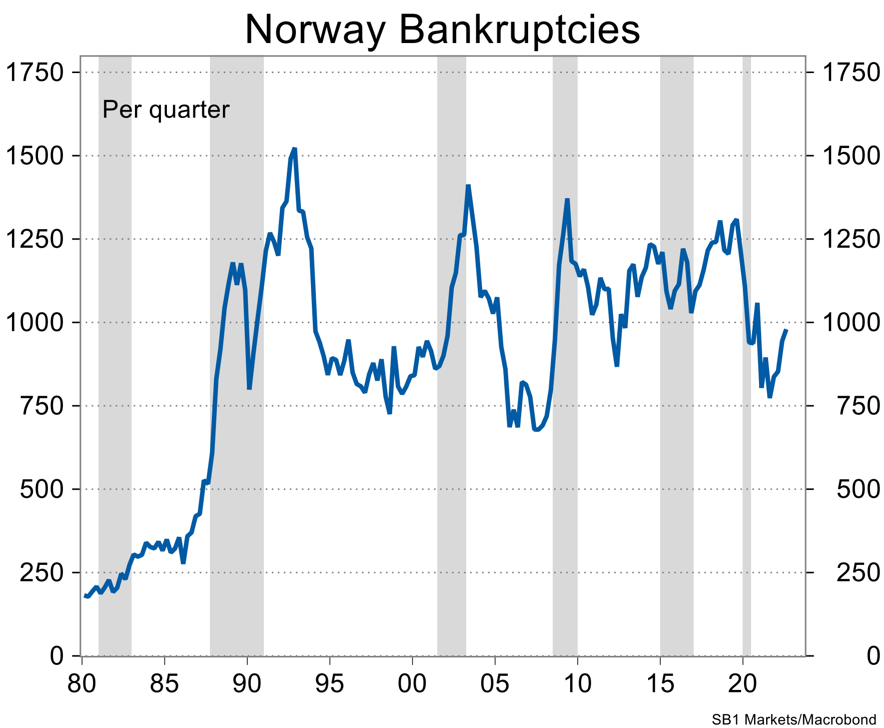


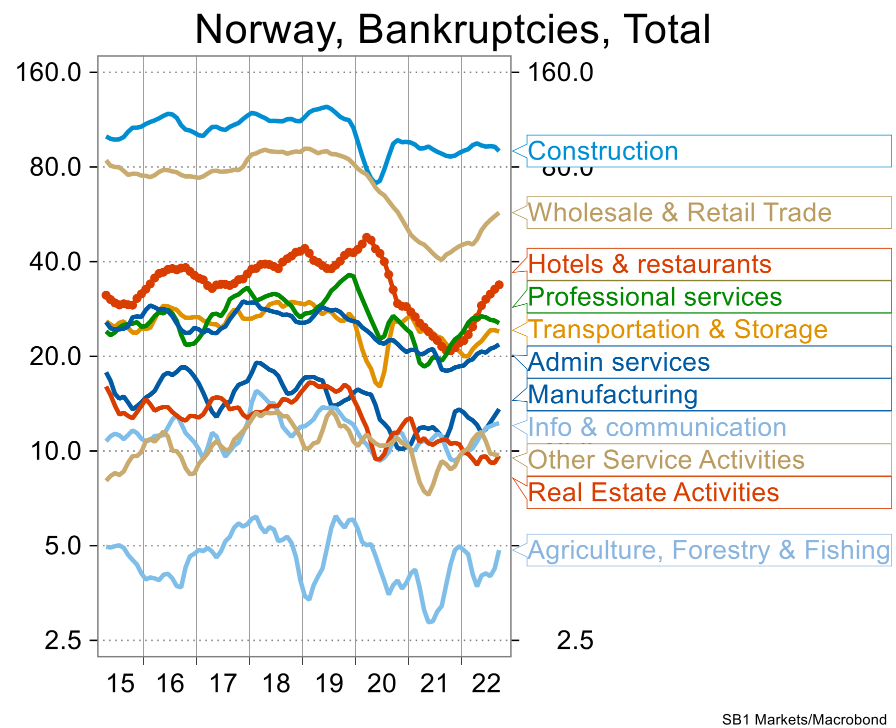


- **Consumer confidence** (the micro index)) fell to 35 in Oct from 44.8 in Sep, a 1 st. dev. drop, to -6.5 st.dev below average – which is a rather remarkable observation, we would say
  - The **macro index** was also down, to 2.4 st.dev below average, just marginally down. The total confidence index fell 0.4 st.dev., to -5.2, the lowest ever
  - Both **retail sales** and **house prices** have fallen alongside the decline in consumer confidence – higher rates and high inflation is softening both sentiment and ultimately demand - the outlook is rather bleak

Bankruptcies up in Q3, but still far below the pre-pandemic level

More bankruptcies in trade, and hotel & restaurants but both below the pre-pandemic level

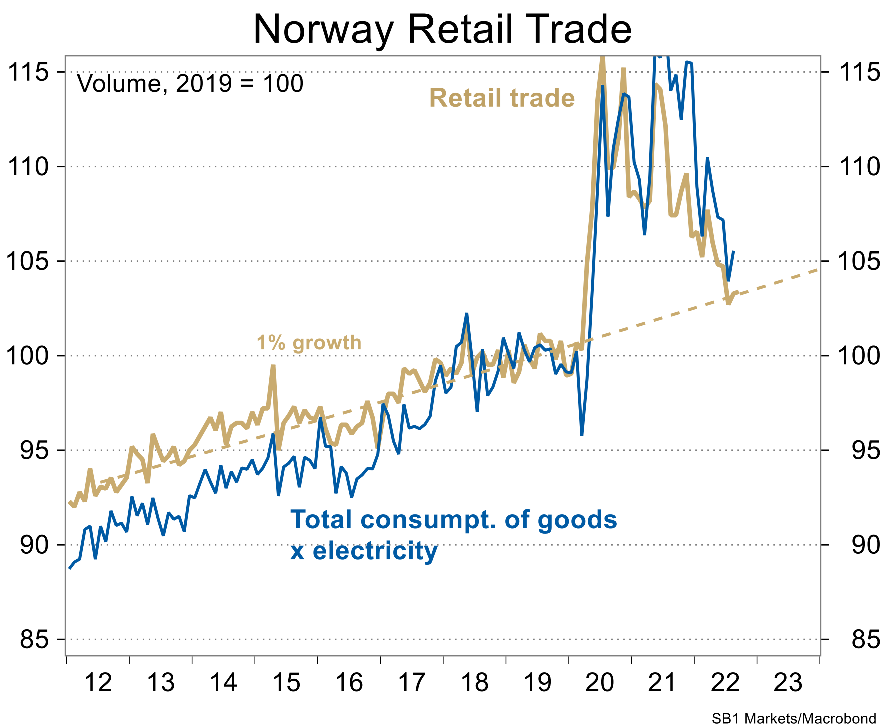


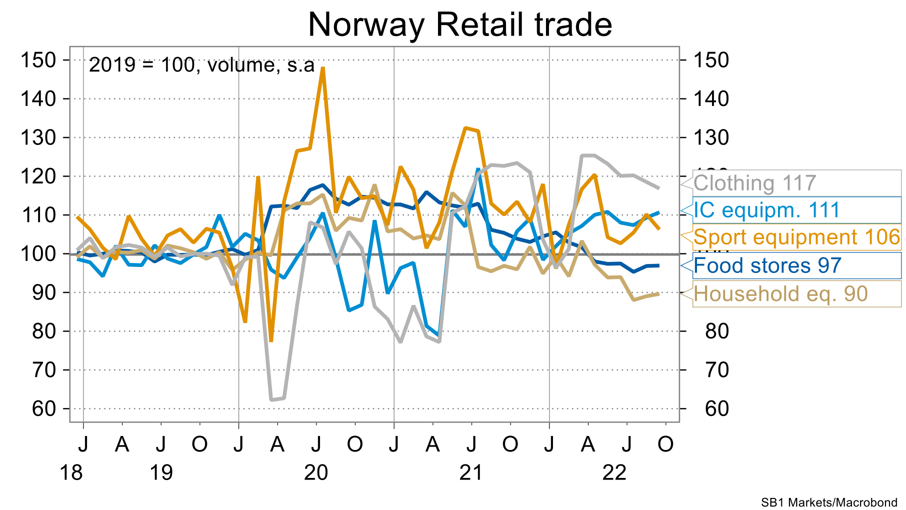


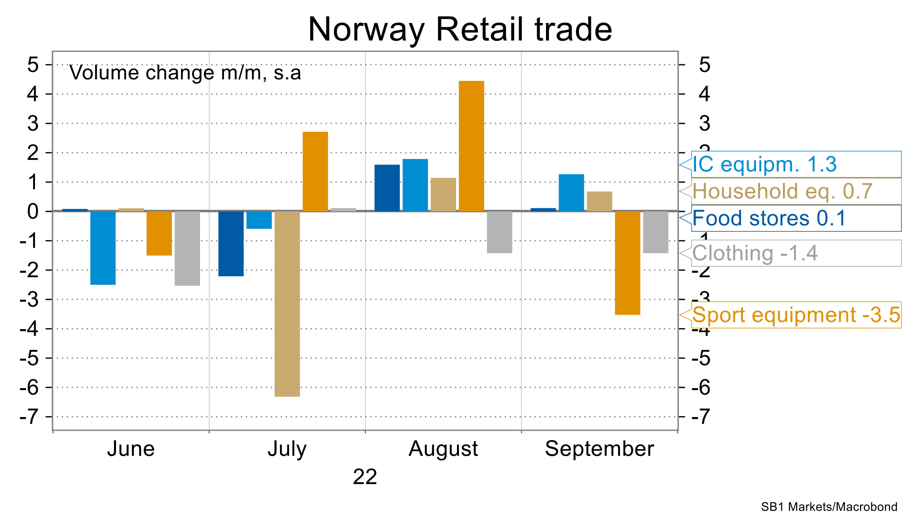
- The energy price ‘crisis’ has so far not pushed many companies into financial hardship, at least not into bankruptcy

Retail sales stronger than expected September (too) but the trend is down

Retail sales were up 0.1%, we expected a substantial decline. Sales fell at 2% pace in Q2



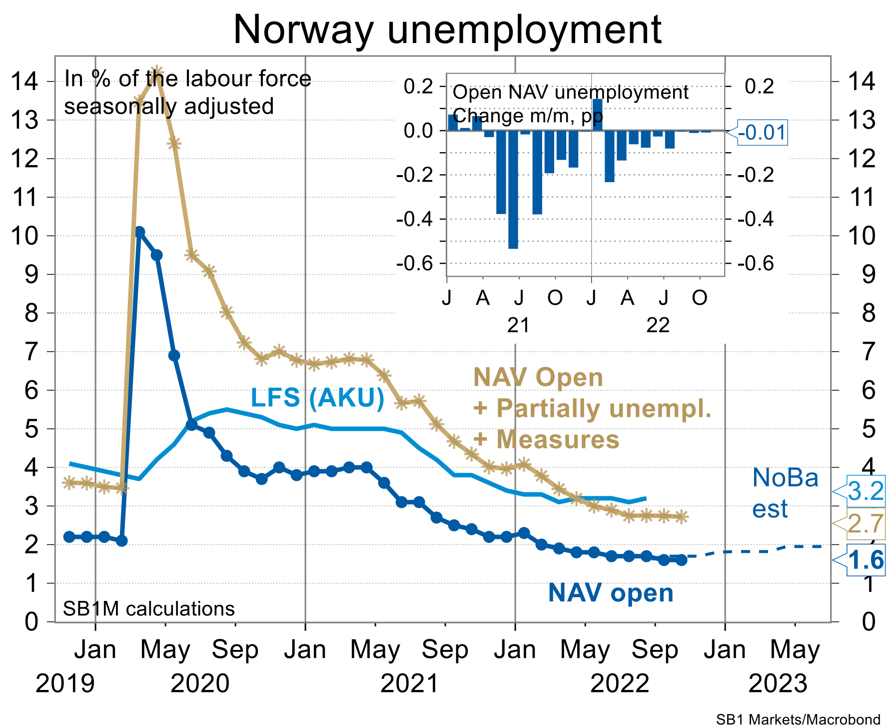


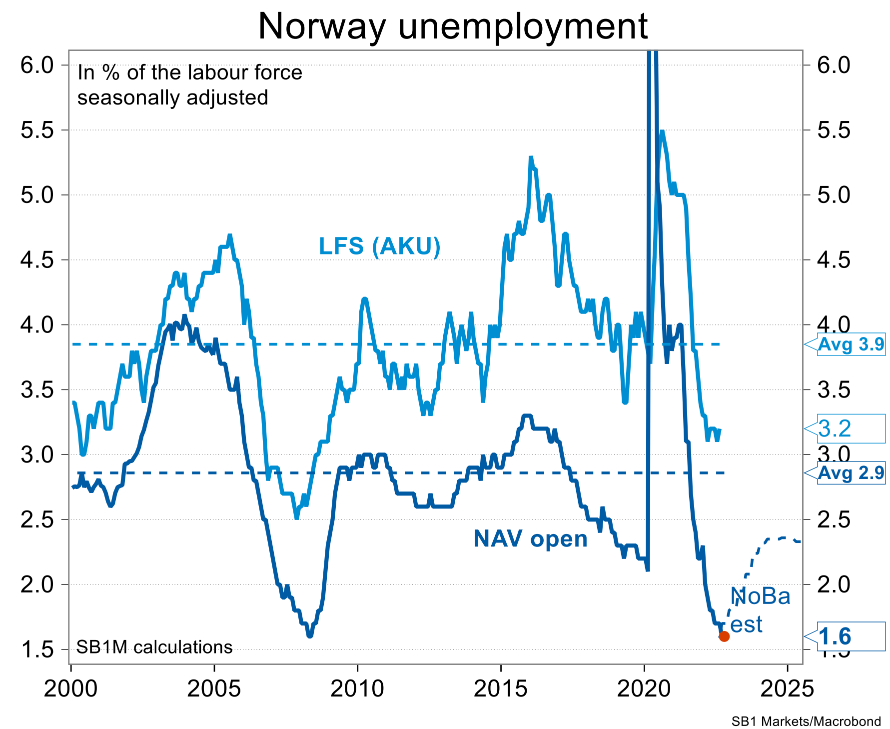


- **Retail sales** are down 4% y/y, and by almost 11% from the peak, early in the pandemic. Sales are close to the weak 1% pre-pandemic growth path
- Very likely, the lift in inflation and higher interest rates have aided sales back down to the pre-pandemic trend – and we expect sales to fall below the trend the coming months/quarters
- Sport equipment fell the most in September (following an even stronger April). All main sectors ex. ITC are heading down

NAV unemployment marginally down in October, and 0.1 pp below NoBa f'cast

Open unemployment unch. at 1.6% (sa), as expected. In isolation, an argument for a 50 bps hike?

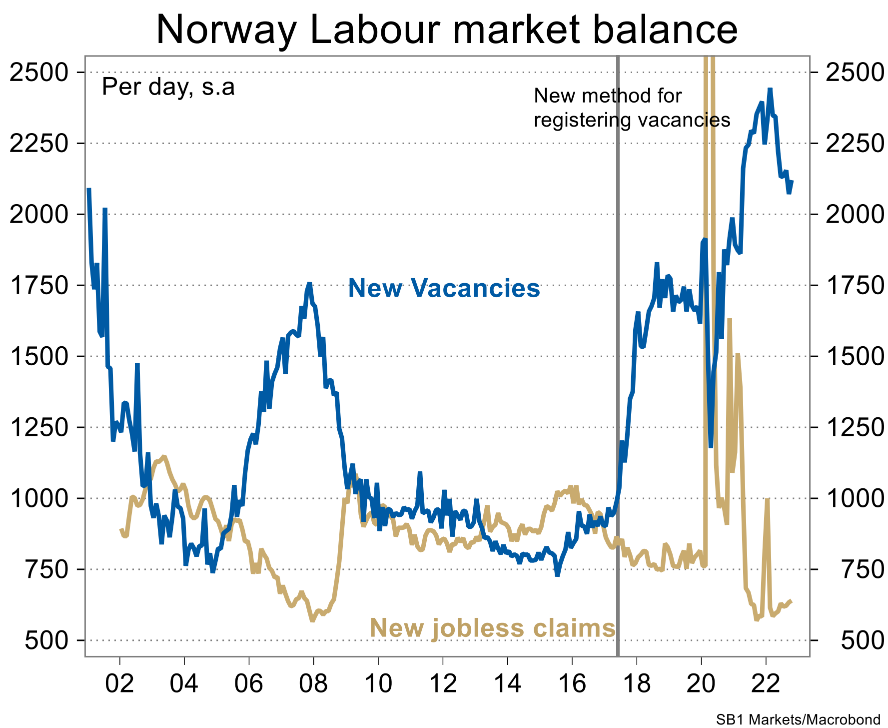


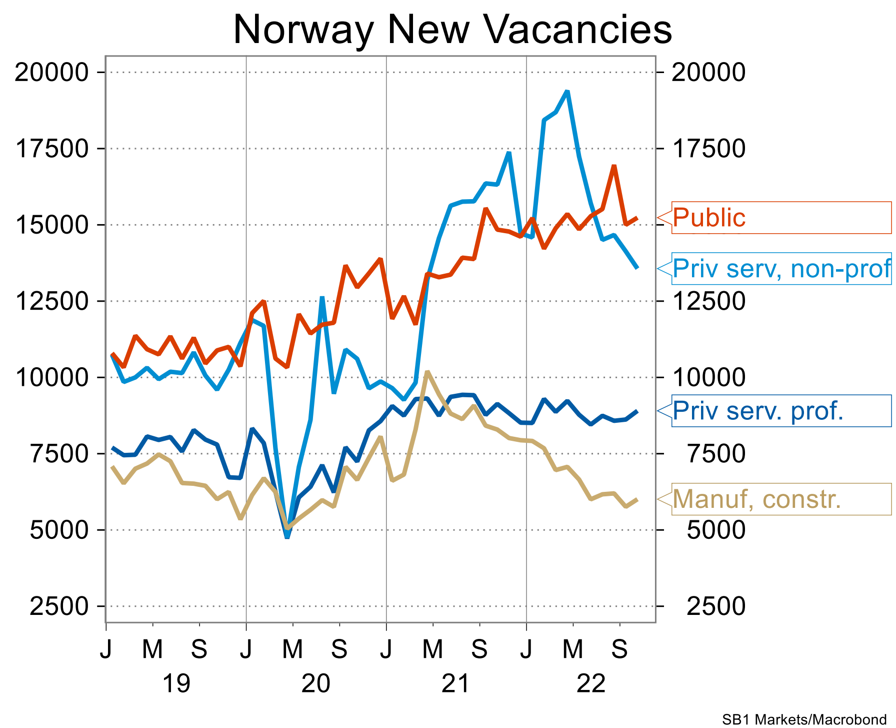


- **The 'full time' open NAV unemployment**, fell by 240 persons in Oct (seas. adj) to 47.6'. The change was as we assumed, but Sept was marginally revised upwards. The rate at 1.6% (s.a) is equal to the lowest level before the financial crisis in 2008, and almost the lowest level since 1980, and +0.1 pp below NoBa's estimate in the Sept MPR. Unadjusted the rate was unch. at 1.6% (1.55%), expected down to 1.5%
- Including labour market measures, unemployment fell by 800' persons, 500 more than we expected, and the rate is at 2.0%
- The inflow of **new job seekers** is trending slowly upwards, but the level remains very low. The **inflow of new vacancies** rose marginally in Oct, but the trend is down, from the peak before the summer. Even so, the level remains very high. The decline is broad, except for the public sector.
- **The LFS (AKU) unemployment rate** reversed the 0.1 July, decline, as the rate rose to 3.2%. This rate has been flat since the spring

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

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

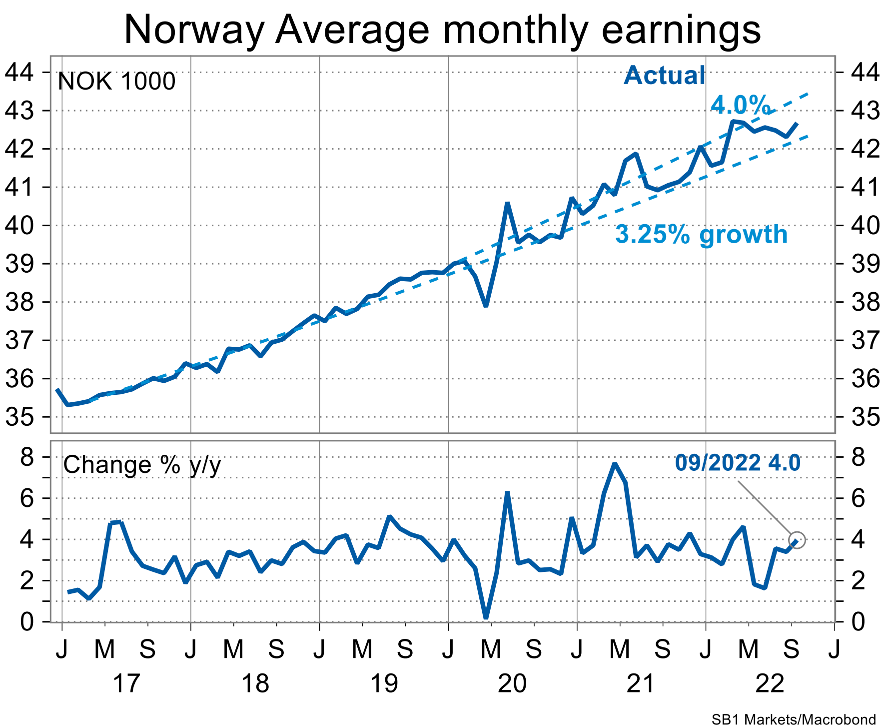


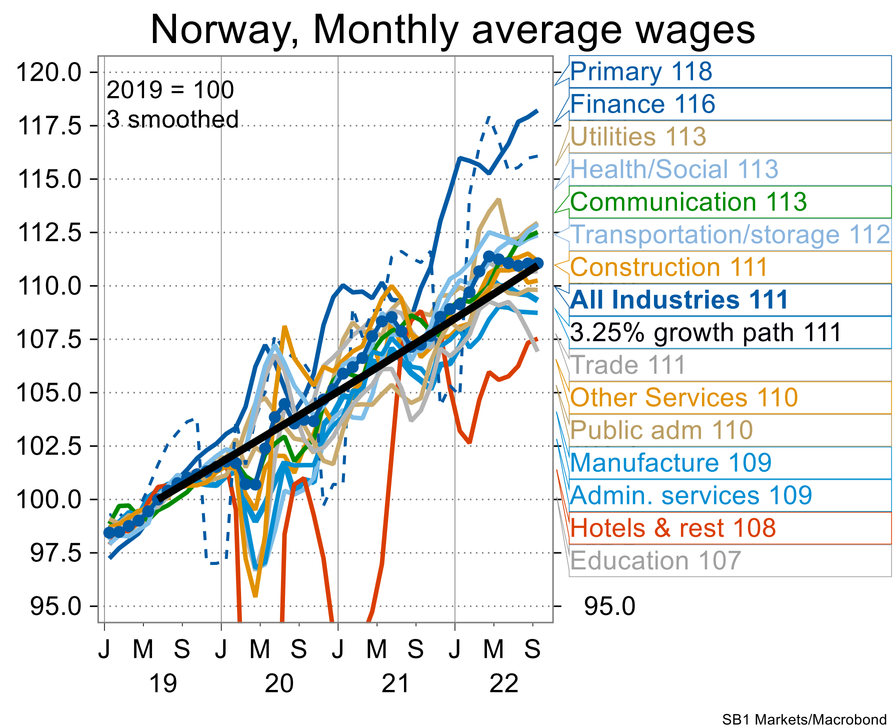


- The no. of new vacancies rose marginally in October, but the trend is clearly down
- Most sectors have announced somewhat fewer new vacancies recently, most pronounced in the construction sector
- The no. of new jobless claims have probably bottomed at a very low level, and is trending very slowly upwards

Wage inflation is (very likely) NOT accelerating, wage trends up less than 3.5%

Regrettably wage data are volatile – annual growth in August was revised down 2 pp to 3.4%

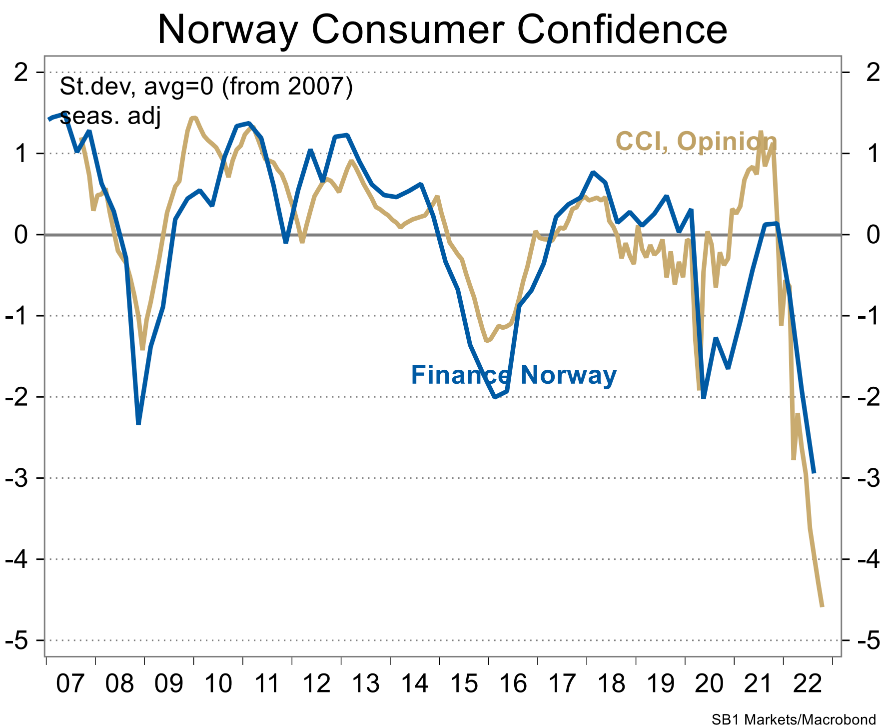




- **Monthly average cash earnings** are rather volatile – and more than normal since the beginning of the pandemic. The average monthly wage depends on hours worked, bonuses, sector mix etc. – and data are often substantially revised
  - » The previous month's annual wage inflation was revised down by close to 2 pp to 3.4%! So take the current 4.0% growth rate with 2 grains of salt
- However, given the present stats – which are the best at hand – we are not witnessing any acceleration in wage inflation. The quarterly labour cost index was up 3½% in Q2, and growth is not accelerating. National accounts up to Q2 have come to the same conclusion.
- Wage inflation is extremely important vs. the longer-term inflation outlook, and the need for monetary tightening. So far, wage inflation has been clearly below our expectations!

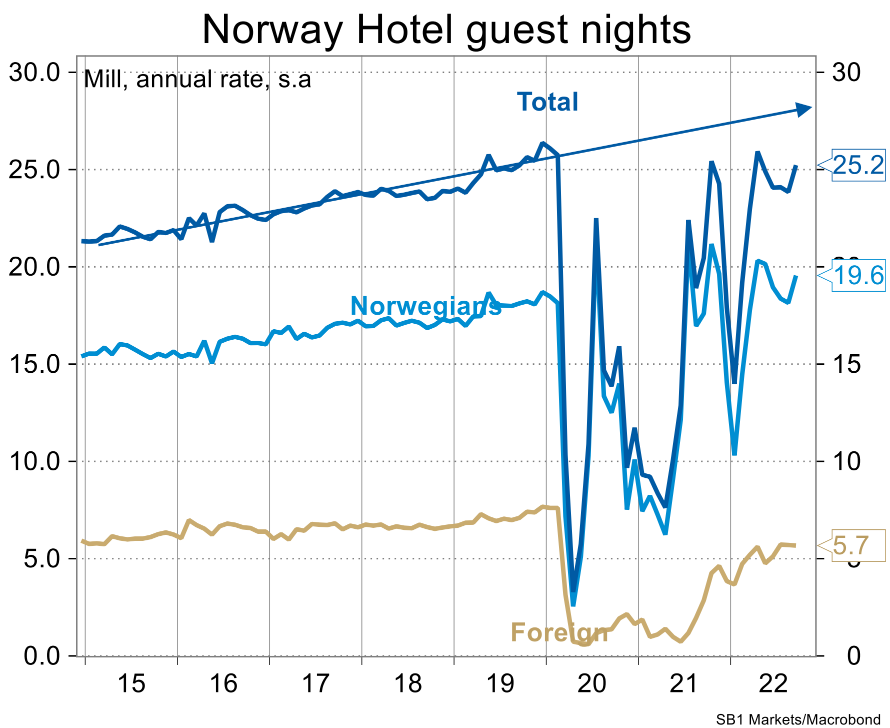
Consumer confidence down to ATL in ~~May~~ ~~July~~ ~~August~~ ~~September~~ October…

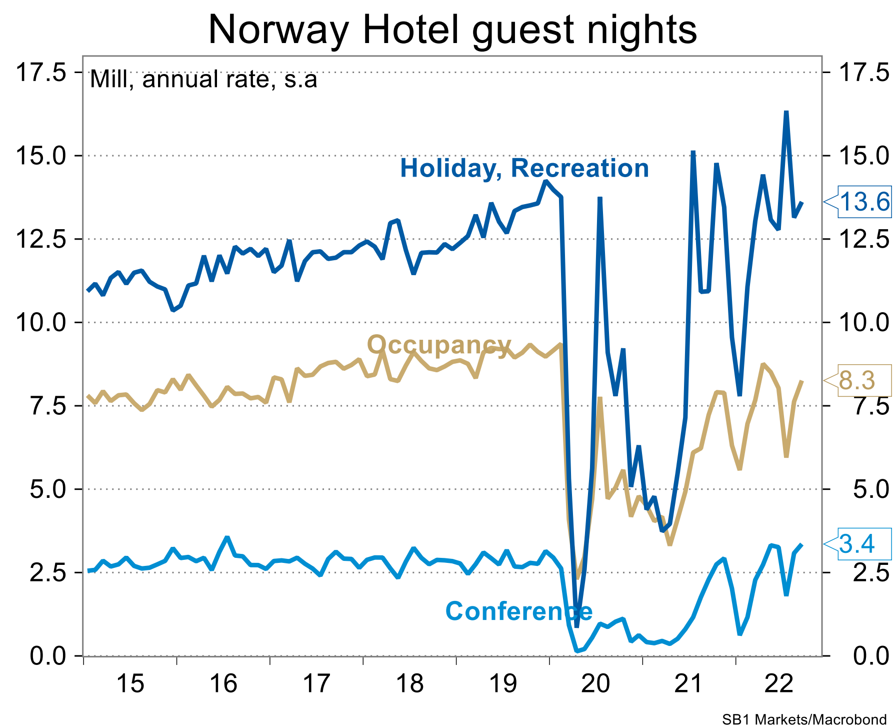
CCI from Opinion fell further in October, by -0.3 st.dev to -4.6



- **The CCI print** from Opinion in October was the lowest on record– high inflation and higher interest rates are no doubt biting
- The index 4.6 st.dev below average. The bottom during the pandemic was 2.0 st. dev. below average
- **Will households stop spending or retreating from the housing market?** The housing market has no doubt turned the corned, while sales are trending down
- The **net share of optimists** is -32%. Given inflation and the hikes in interest rates + some geopolitical uncertainty, this share could easily have been larger
- On the other hand, even if a large share of the population recognises that their own economy will be hurt, it does not imply that they all plan to cut spending sharply. Even so, the decline in confidence is of course worrisome

Business hotel guest nights almost back to normal, conferences ATH, recreation OK



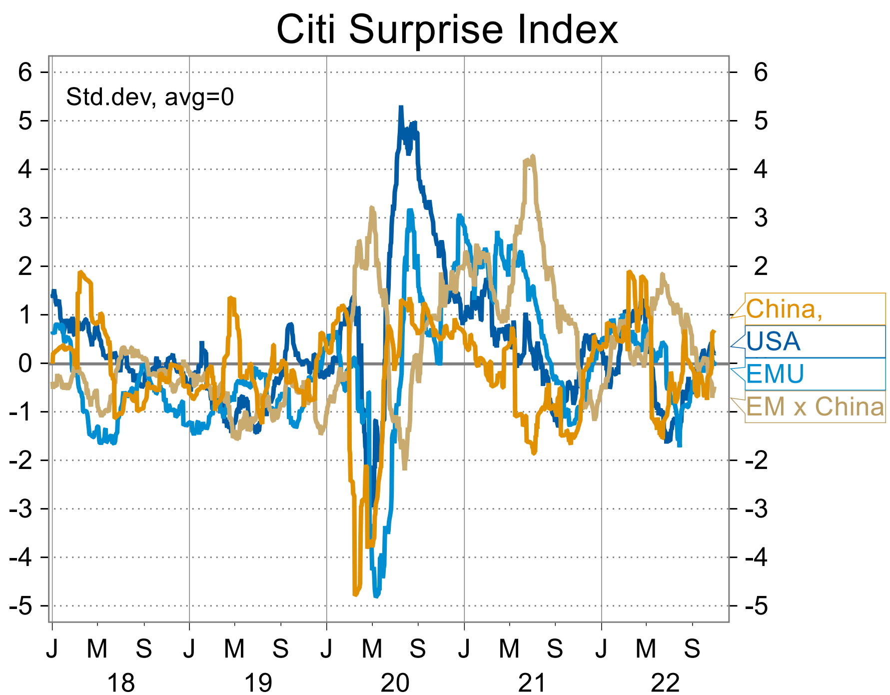


- Recreational demand is back to a normal level, even if the total number of foreigners are still down 25% vs the pre-pandemic level
- The conference market is back the pre-pandemic level – it took just some few weeks after restrictions were lifted
- Other business guest nights are some 10% % below the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

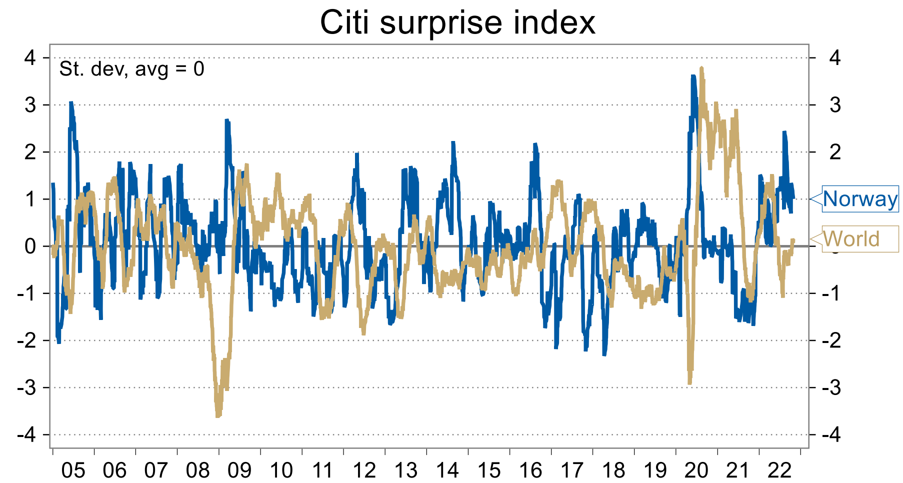
SpareBank 1 MARKETS

Data marginally above expectations, according to the Citi surprise index

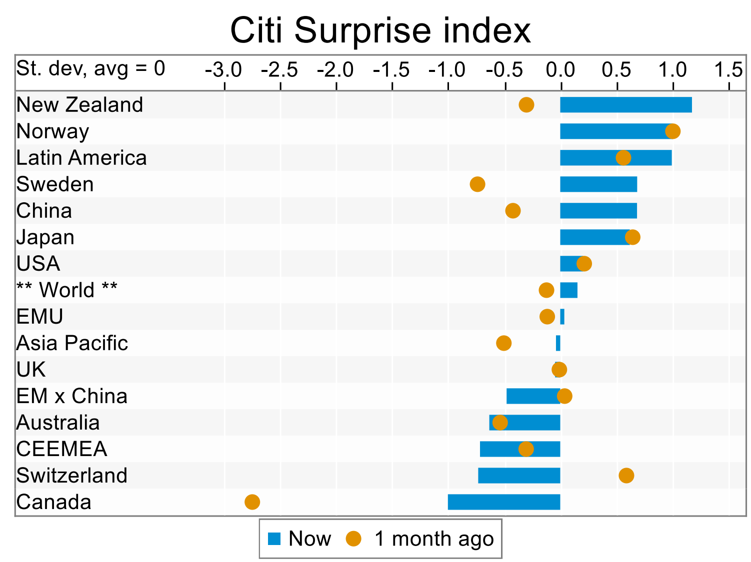
Norway almost at the top (but we do not really feel like that is the case…). US, EMU, CN > zero



SB1 Markets/Macrobond



SB1 Markets/Macrobond



SB1 Markets/Macrobond

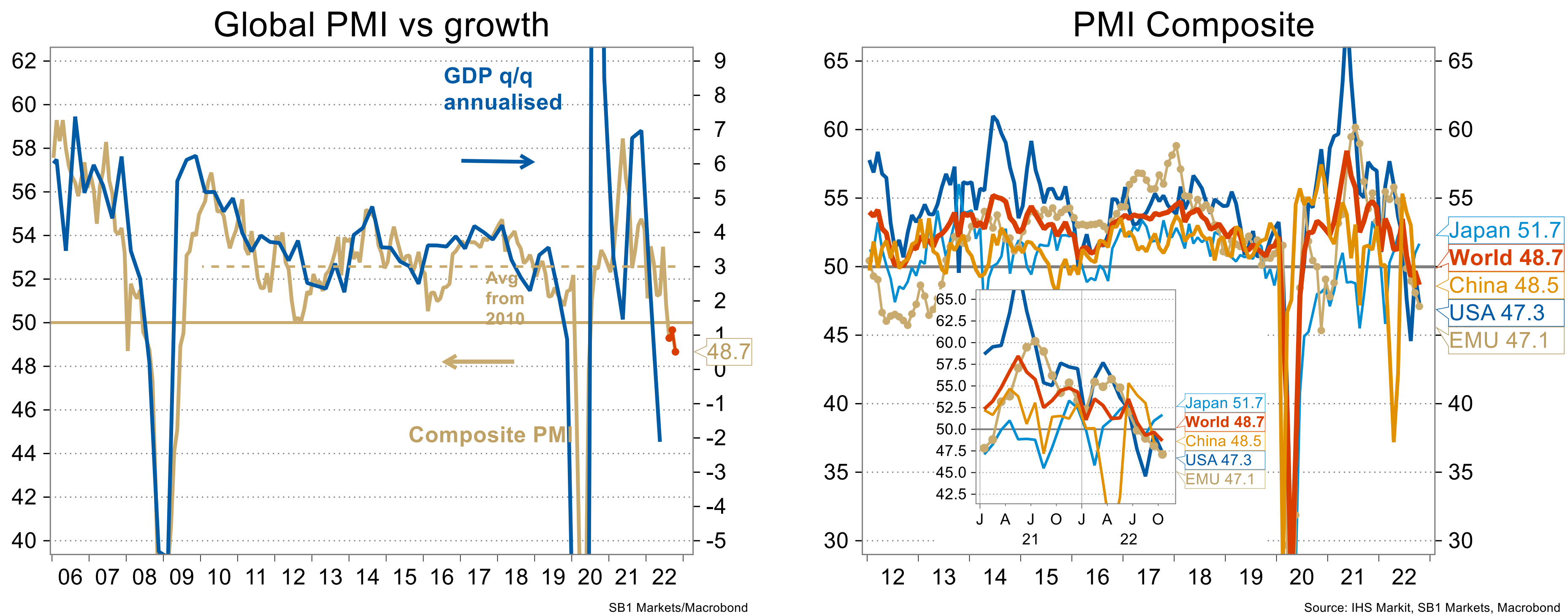
- **Norway** no. 2 on the list, according to Citi
- … even if our super-cycle friends **Australia, Canada** are at the bottom of the, while Sweden has recovered last two week (even if GDP surprised at the downside)

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 world composite PMI very likely down again in October, led by rich countries

Both US, EMU, and UK reported weaker PMIs than expected – and all are below the 50 line

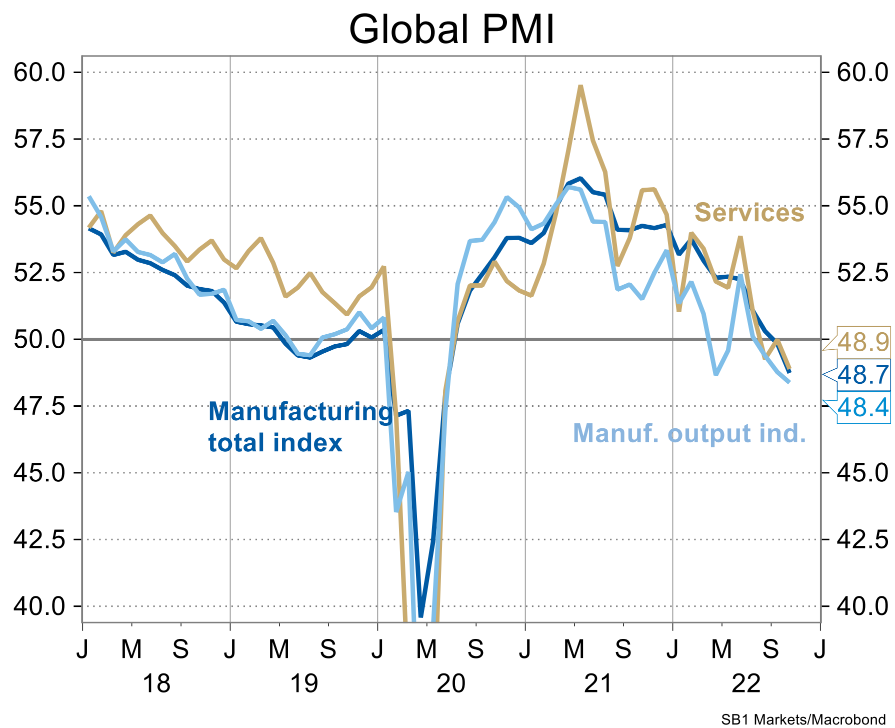


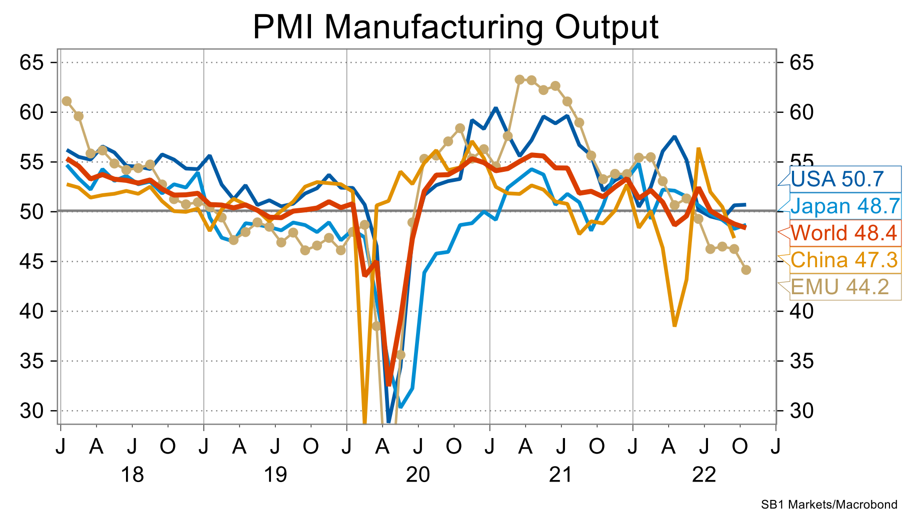
- The composite PMI very likely fell in October, following the small uptick (which turned out to weaker than we assumed, due to another setback in China). We so far assume a 1 p drop, to 48.7, the lowest print the past 15 years, barring the Financial Crisis and the start of the Pandemic
- The US PMIs surprised the most on the downside
- In the EMU, Germany was the weakest, but the rest of the union is also below the 50 line
- Caxin has not reported its October data. This morning, the NBS/CPLF PMIs were reported down 1.9 p

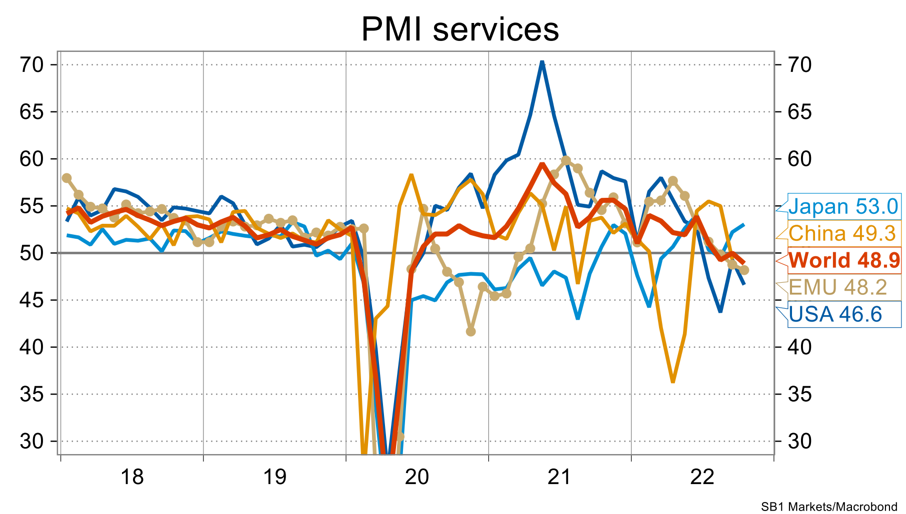
Our estimates are based on the preliminary PMIs from US, EMU, Japan UK, Australia. The estimates are uncertain, but usually by less than 0.5 p if the Chinse PMI does not change too much

Services in the US down again, but manufacturing output keeps up

In the EMU both manufacturing and services reported a faster contraction in October

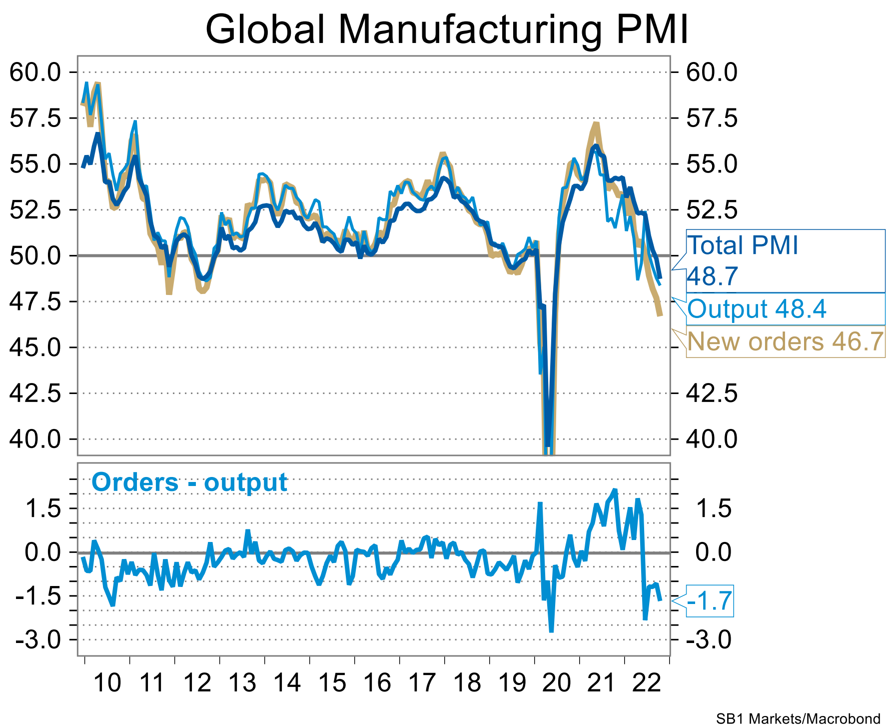


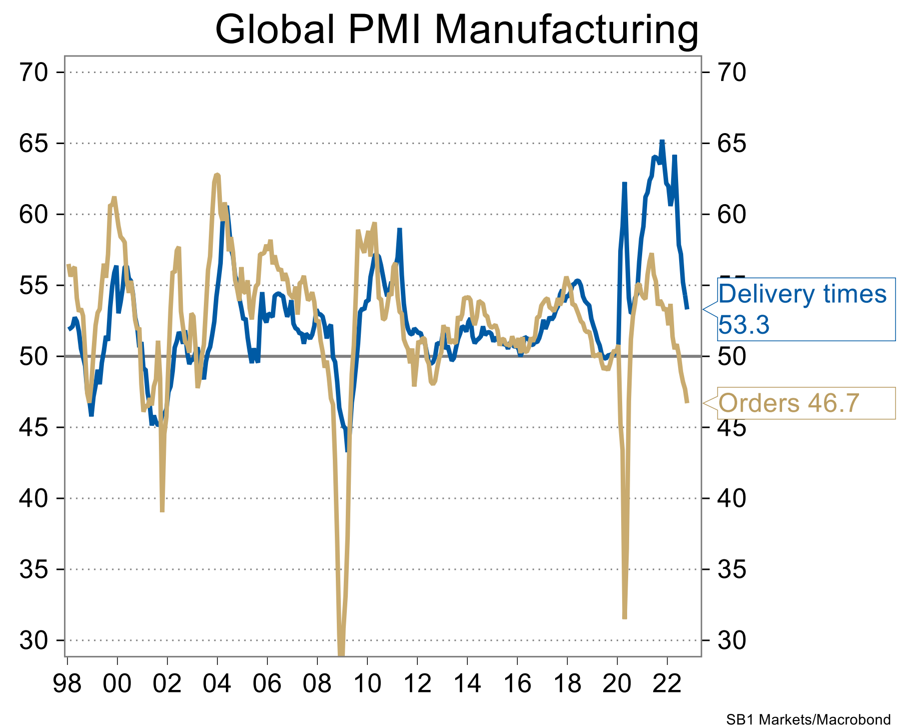




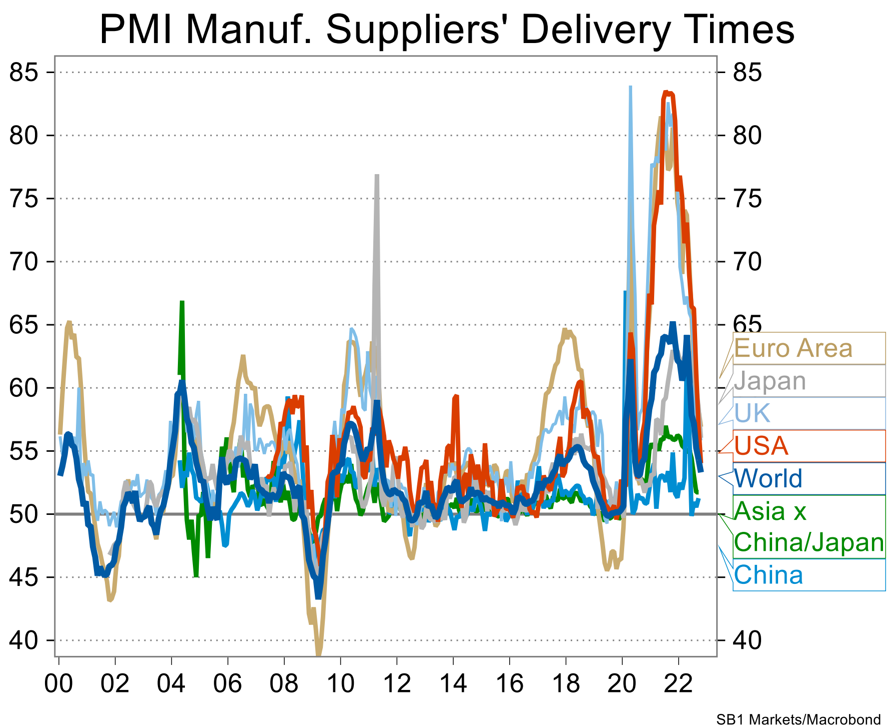
Manufacturing orders are contracting very fast, both in Europe & US

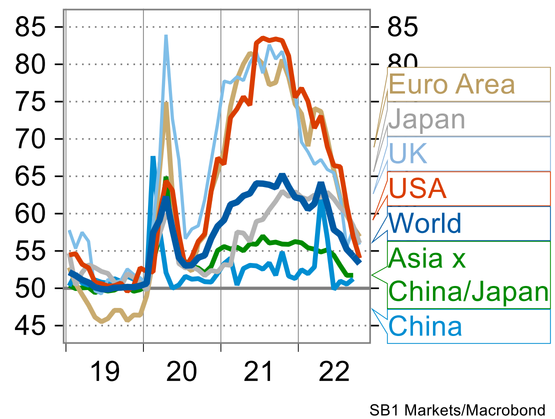
The delivery times index fell further in October – and is almost back to a normal level





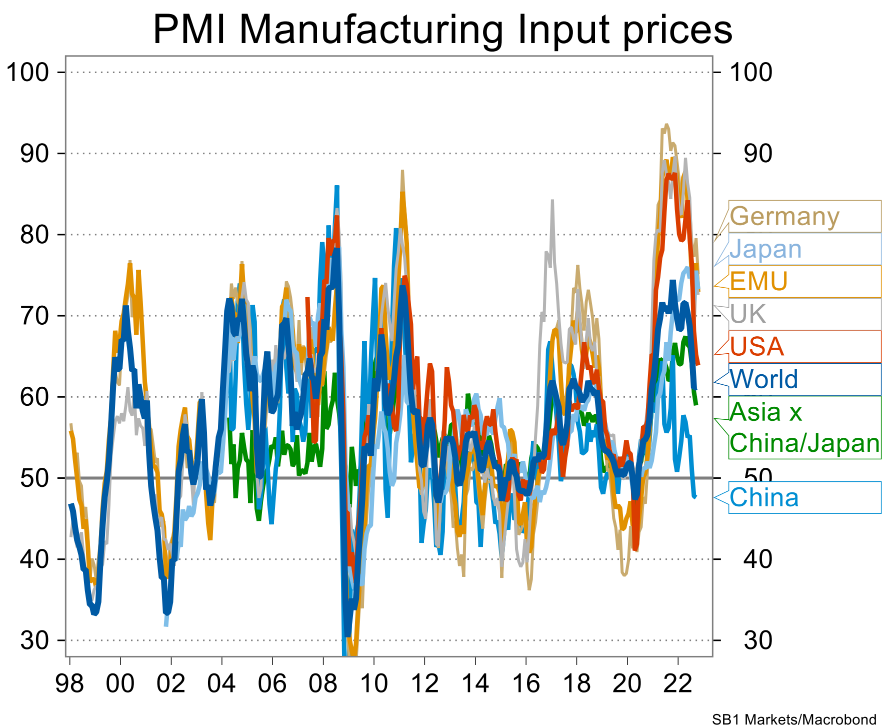
Delivery times are coming rapidly down everywhere

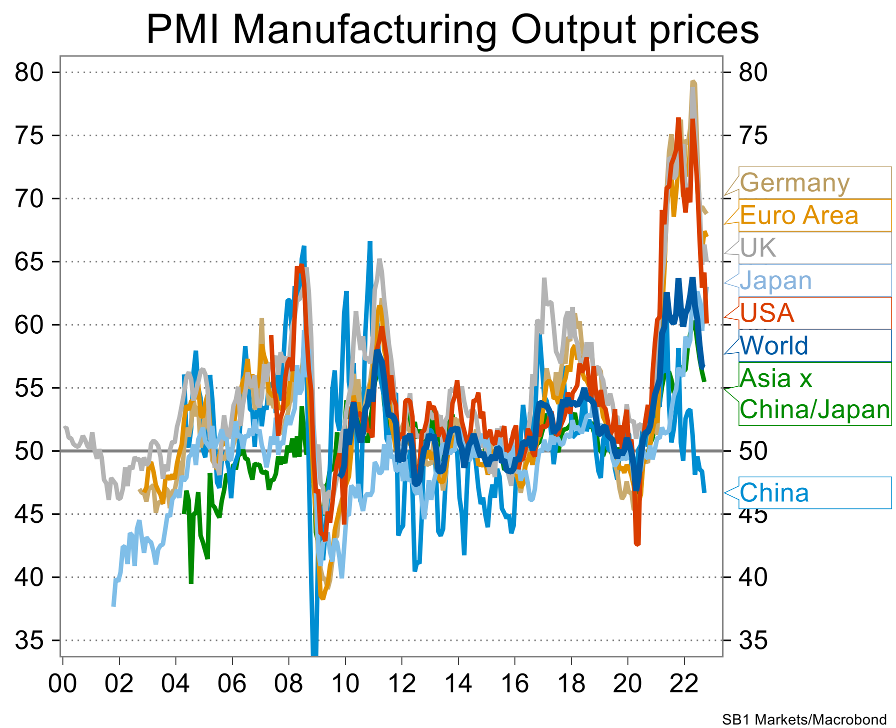




- **The global delivery times** PMI sub-index (changes in delivery times vs the previous month) has been inching down since the peak last October. The decline is broad among the Western rich countries
- **The interpretation of this index is uncertain** – are companies really reporting changes in delivery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

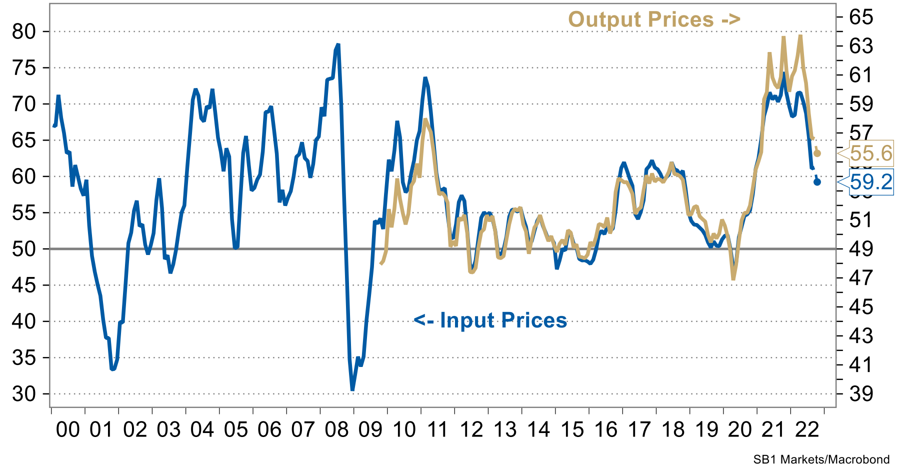
Manufacturing price inflation is heading downwards but remains elevated



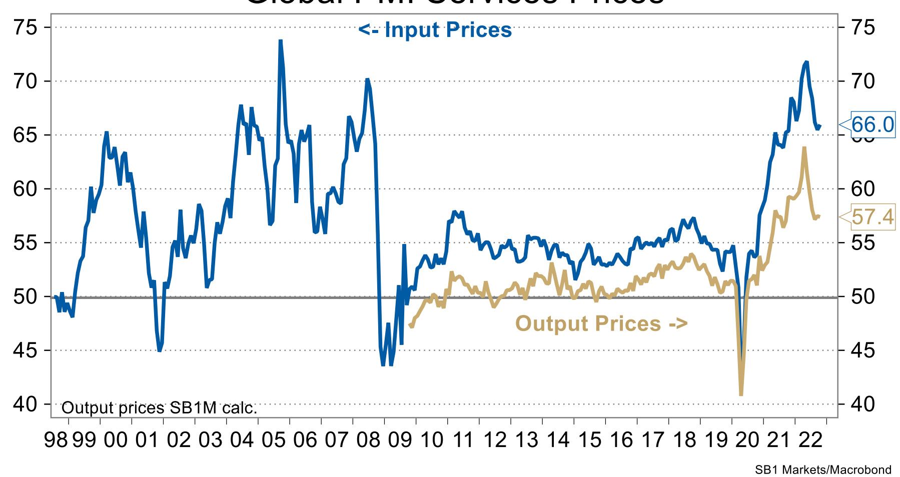


Price indices are heading down, but remain elevated

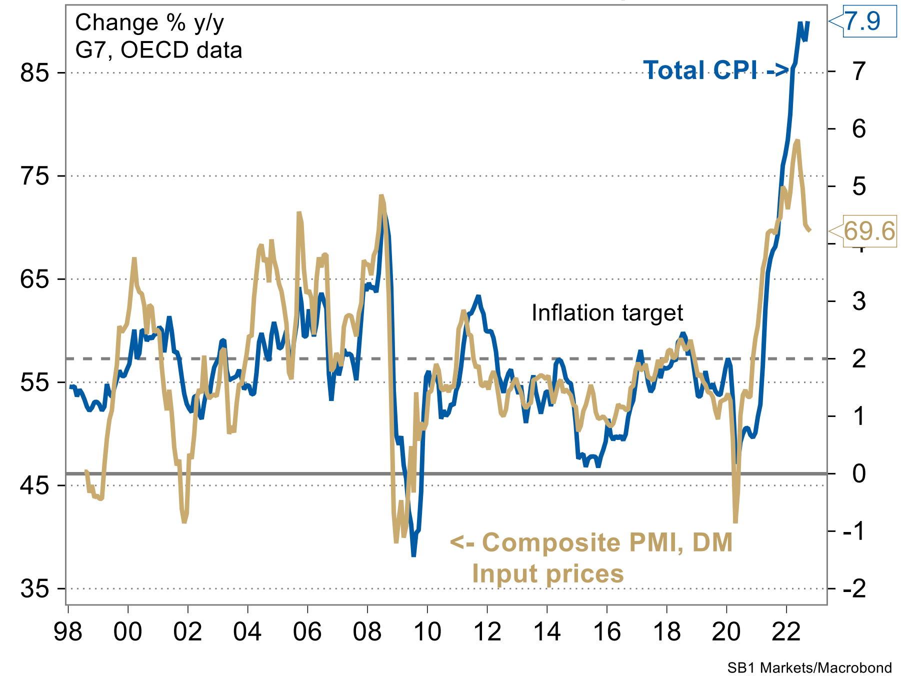
Global Manufacturing PMI Prices



Global PMI Services Prices



OECD Inflation vs PMI prices

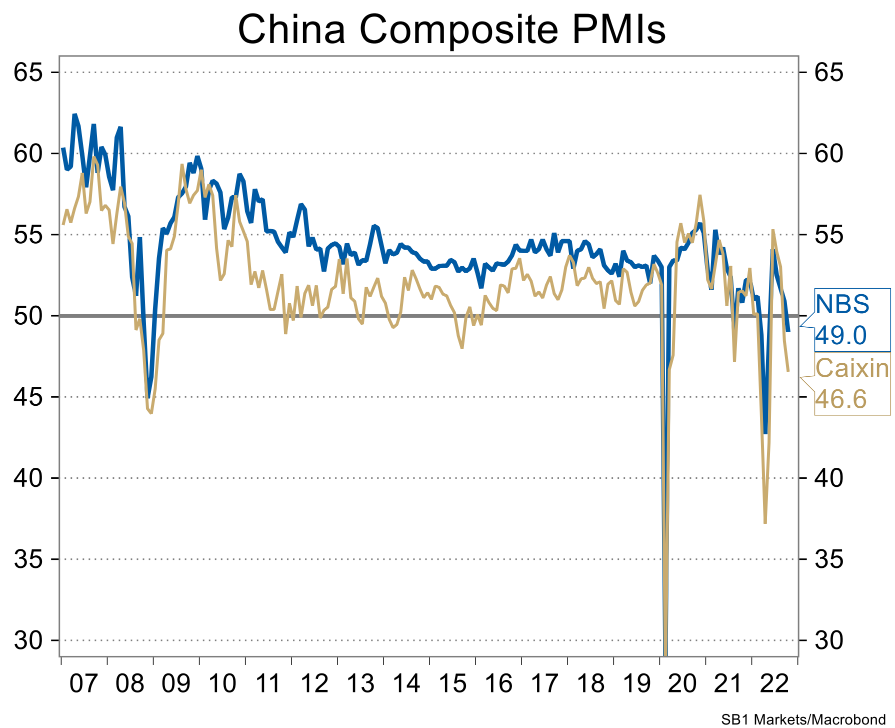


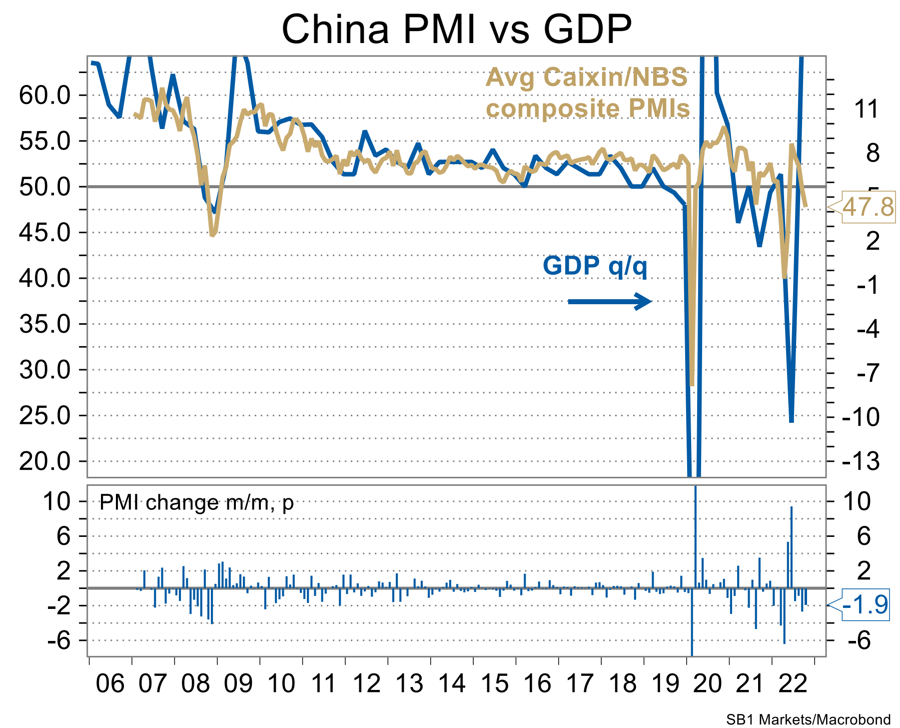
- These PMIs signal a substantial price pressure the coming months
- We are still much more concerned about wage inflation than the actual price inflation due to factors that are most likely transitory, like hikes in raw material prices, freight cost or short lived margins expansion when demand is surprisingly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

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

The ‘official’ PMI down to below 50 again in October

Some 4% GDP growth is signalled

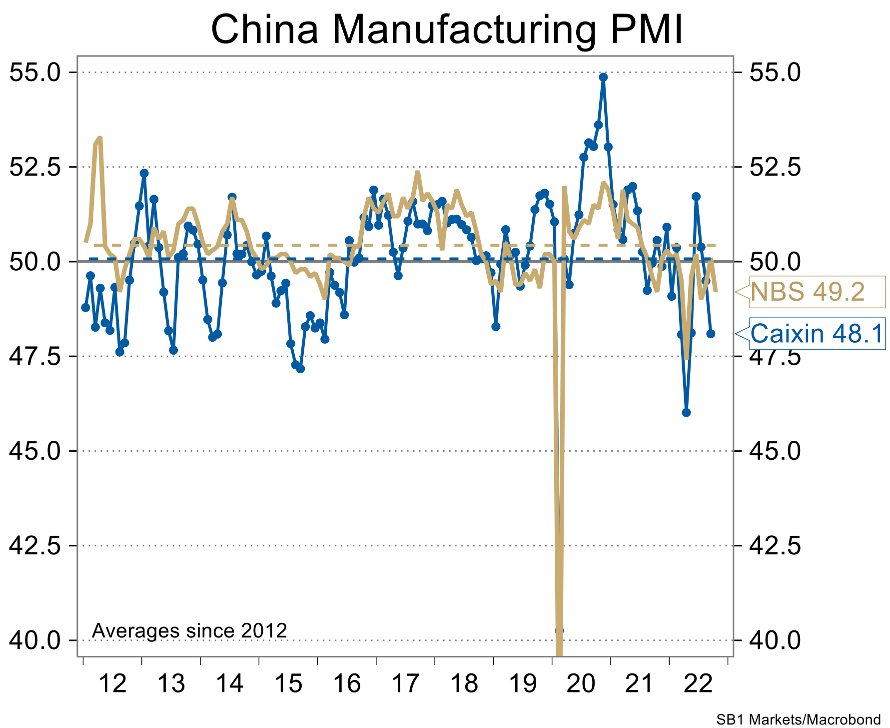


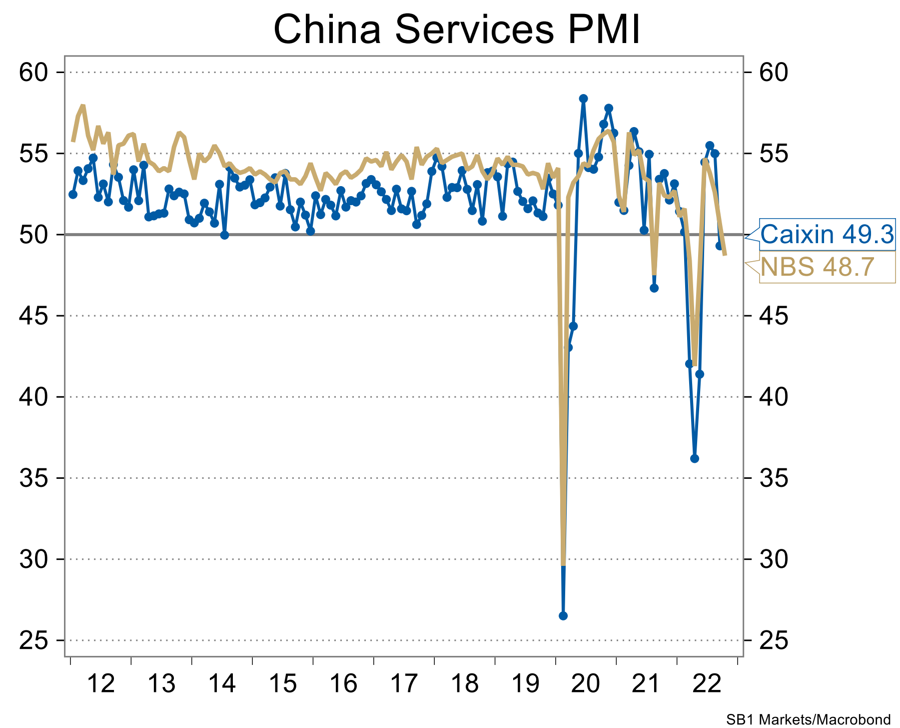


- The **NBS/CFLP composite PMI** fell by 1.9 p to 49.0, expected down 0.4 p – which is well below an average level. In fact the index has been below 50 just in 2008, early 2020 and in the lockdown months this spring
- The **Caixin PMIs** will be reported later this week
- *At the chart to the right we have assumed a decline in Caixin’s composite PMI in line with the setback in the NBS/CFLP survey in October*

Both manufacturing and services down to below the 50-line again

Both also weaker than expected

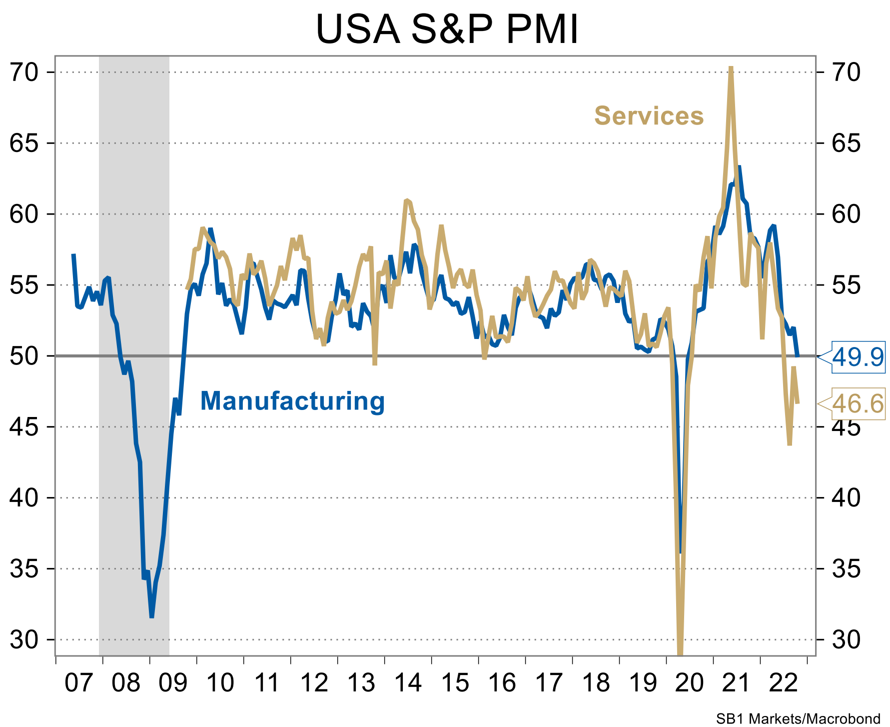


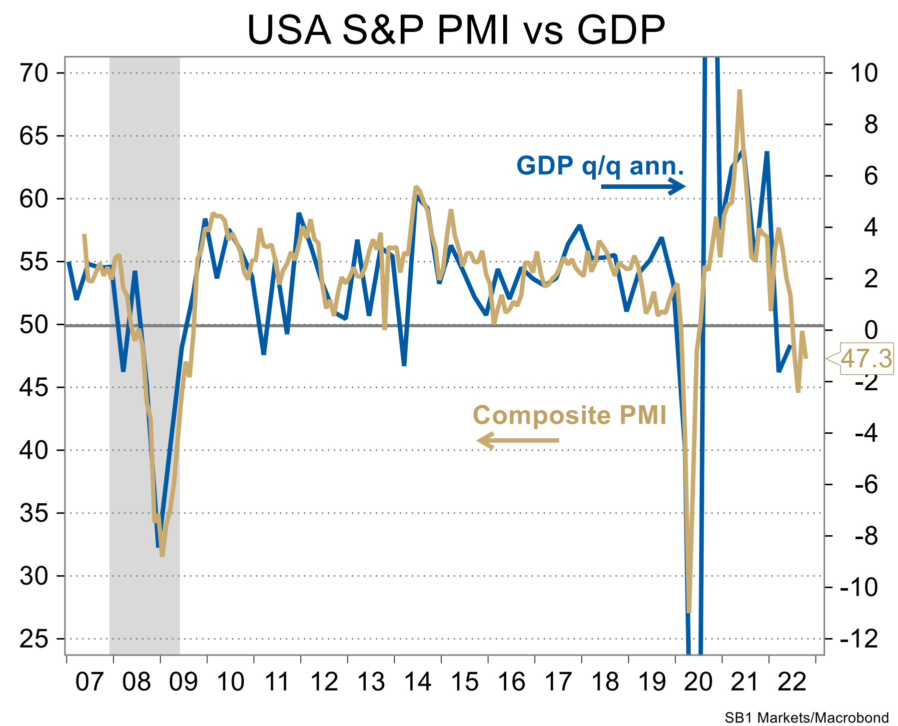


- The **NBS/CFLP** Manuf. PMI fell by 0.9 p to 49.2, expected -0.1 p to 50.0)
- **Services** down 1.9 p to 49.3, expected -0.4 p to 50.2
- **Caixin** will report its PMIs later this week

US PMIs down in October, the composite down 2.2 p to 47.3, a recession level

Both the services and the manufacturing PMIs surprised on the downside – new orders plummeted

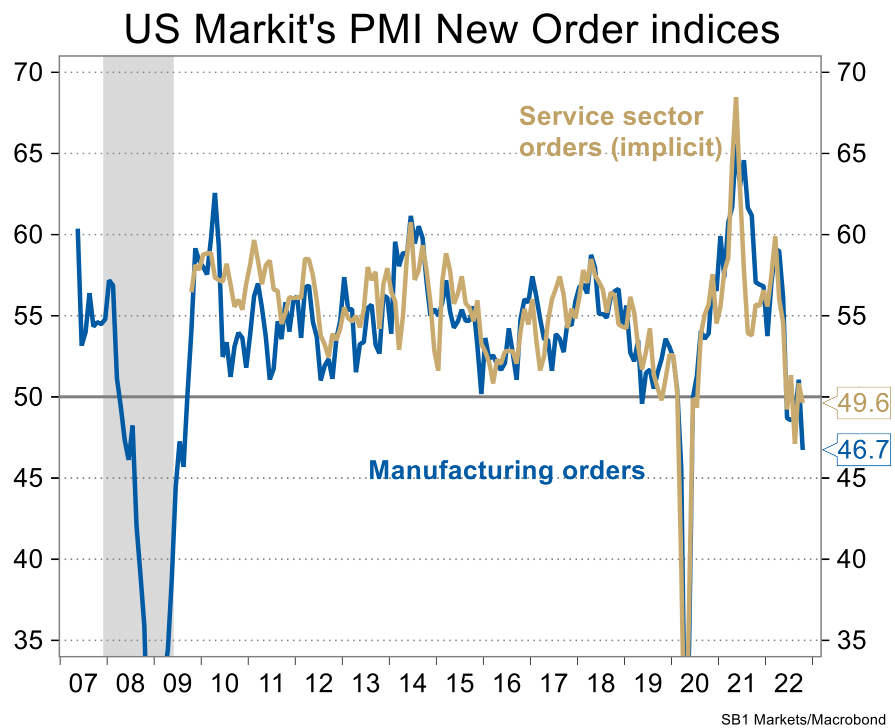


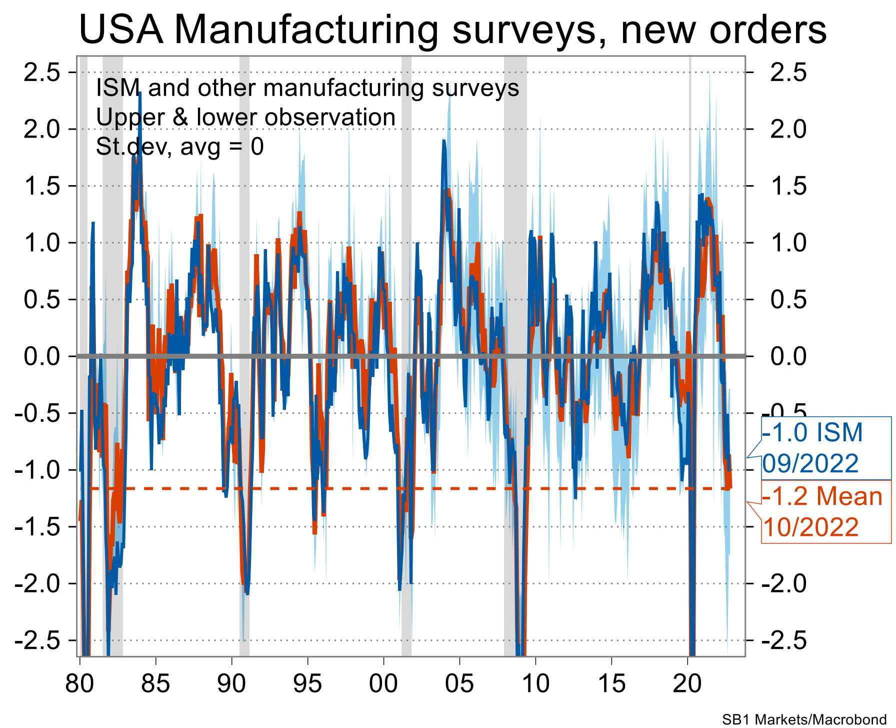


- **The S&P composite PMI** fell 2.2 p to 47.3 in October, signalling some 1.2% (ann. rate) contraction in GDP. An 0.2 p decline to 49.3 was expected
  - » Services was again the weakest link, the index fell by 2.6 p to 46.6. The total manufacturing PMI fell to 49.9
- **The manufacturing new orders index** dropped 3.4 p to 46.7! This is the lowest print since the pandemic, and before that since Aug-09
- **The price indices** fell further but are still reporting faster price increases than normal

The PMIs – and all other manufacturing surveys insist a serious order shortfall

The manuf. PMI reports decline in new orders, just the Fin Crisis, start of the pandemic worse

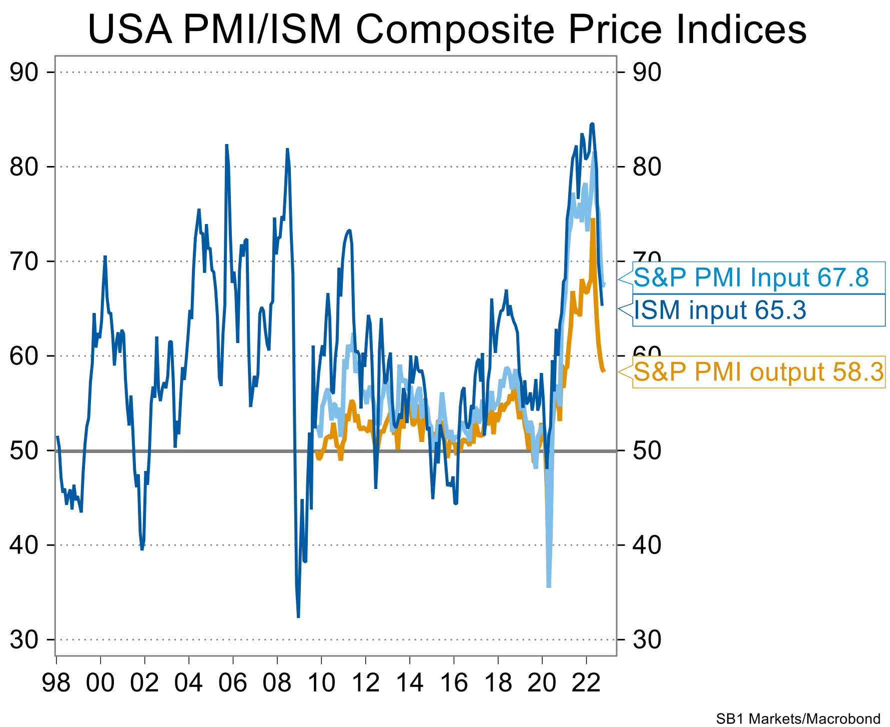


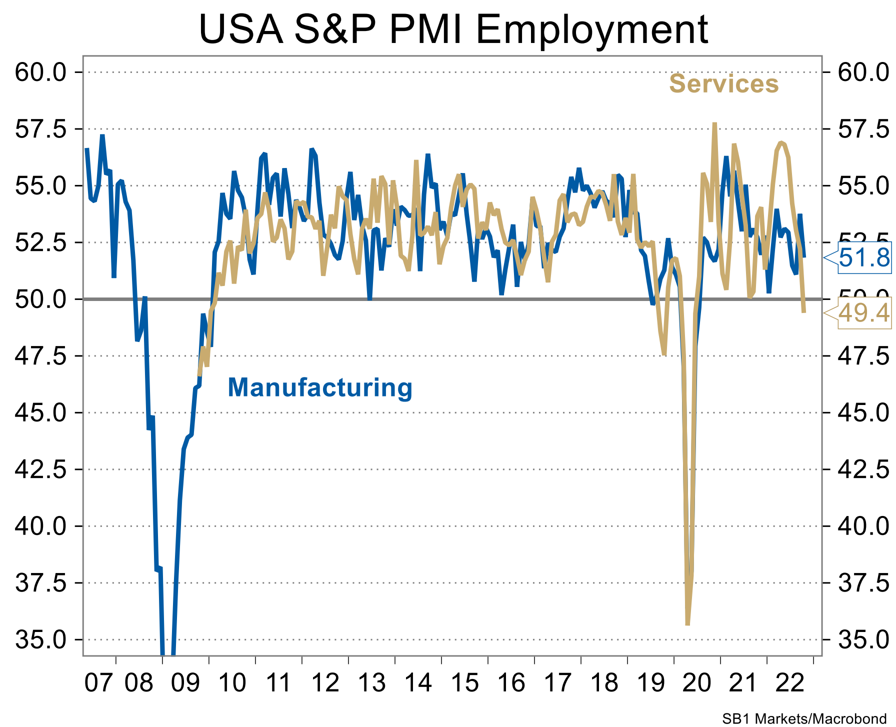


- Just once, in 1995, the order inflow was reported weaker than now, without the US entering or being in a recession

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

But still much faster than normal. Manufacturers are still increasing payrolls, but at a slower pace…

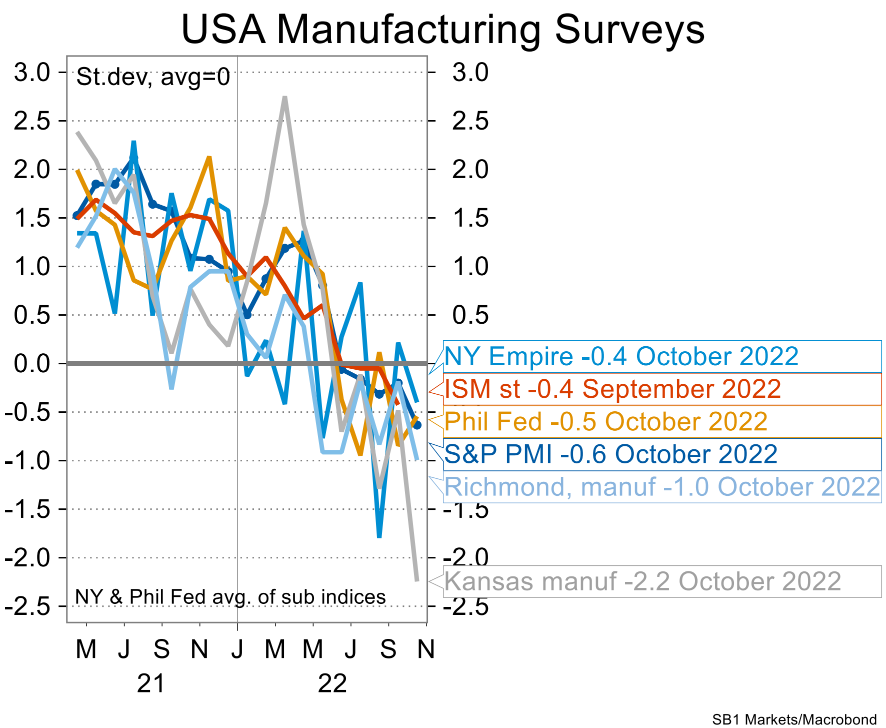


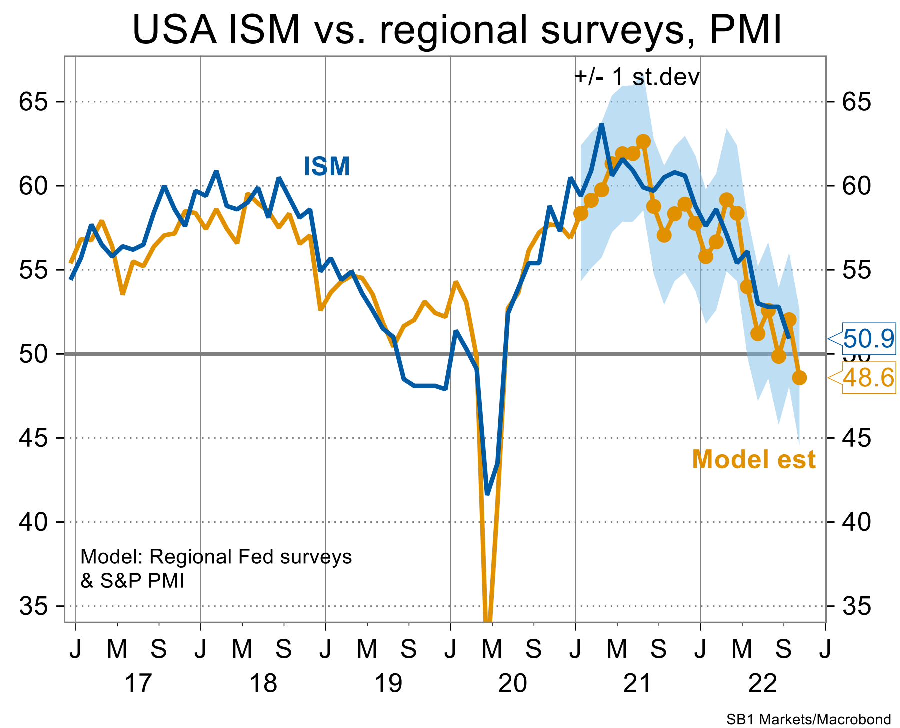


- … but the in service sector, <u>payrolls are on the way down</u>, according to the PMI

Another decline in the ISM, to or below the 50-line?

A model estimate based on the surveys published so far signals below 50. Consensus is at 50

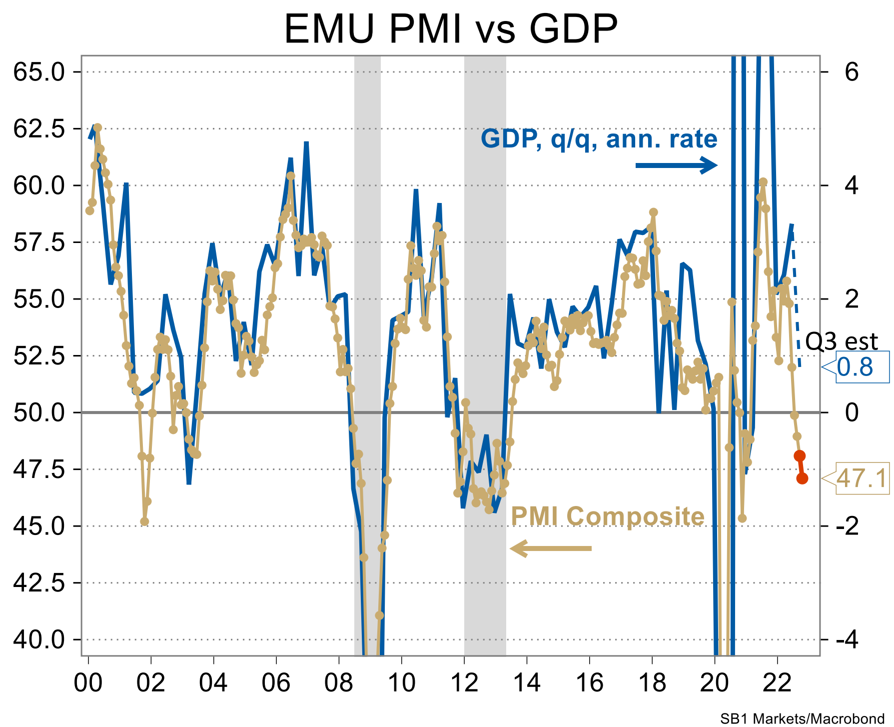


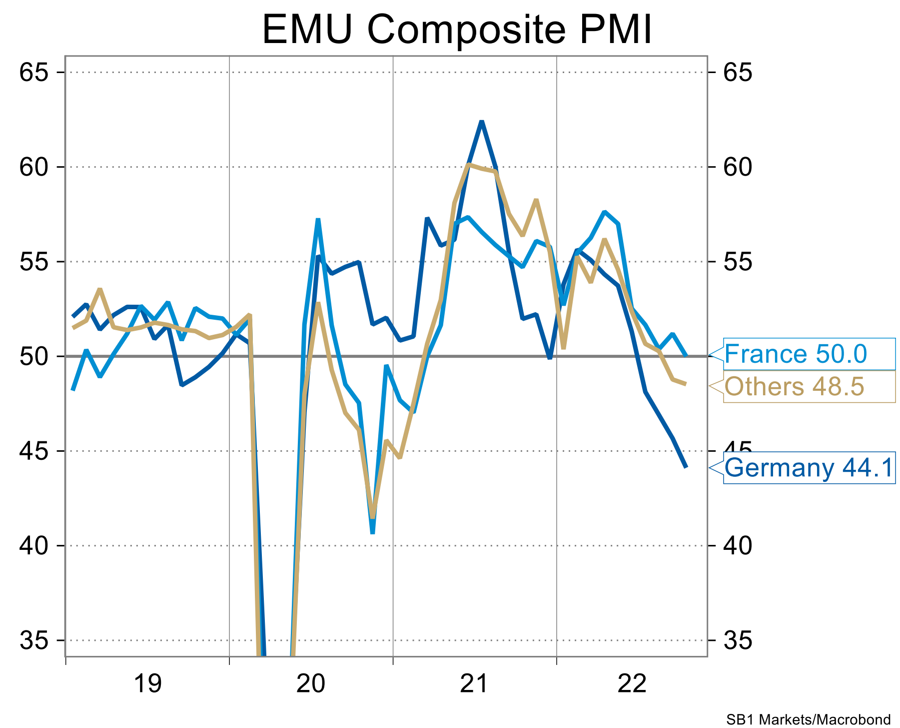


- Big picture: Growth is slowing sharply but manufacturing indices do not signal that the economy has entered a recession (even if order indices are really worrisome)

Eurozone PMI continues to slide, due to very weak German PMI data

The PMIs in EMU x France & Germany are also in contractionary territory

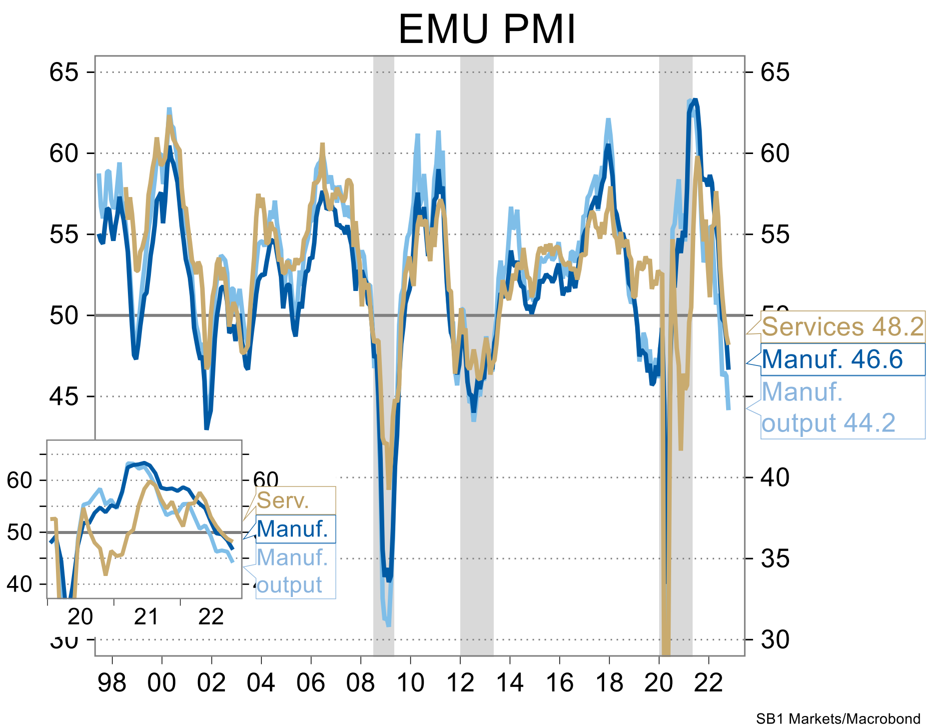


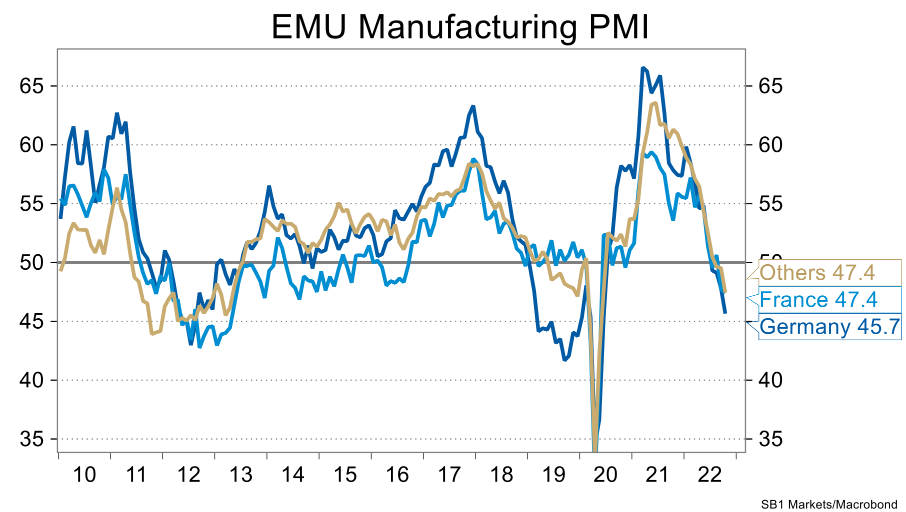


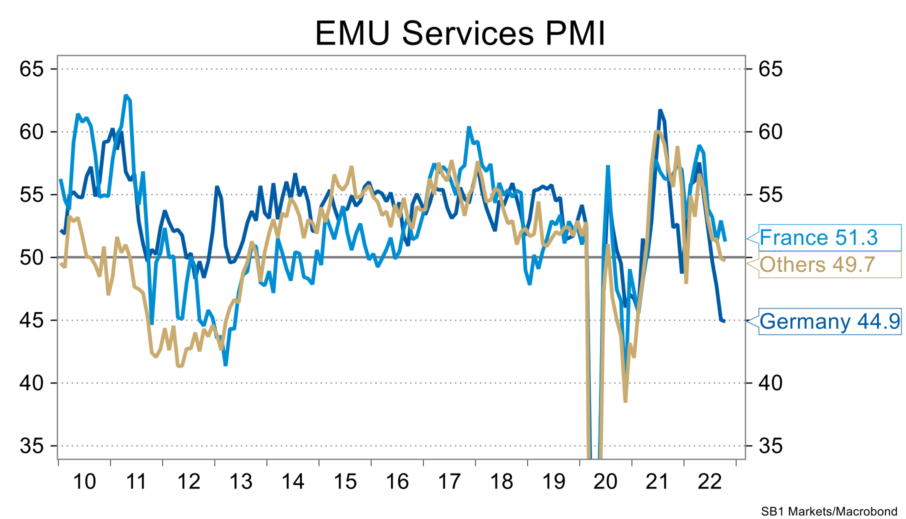
- **The composite PMI** declined 1 p in Oct, to 47.1, which is 0.4 p below expectations – signalling a 1% contraction in GDP in Q4. High inflation/energy prices and higher interest rates are dampening demand, according to S&P. The setback in the German economy is of course a drag on the overall EMU PMI. However, economic activity is falling across the region, and especially in the manufacturing sector
- **Services** fell 0.6 p to 48.2, suggesting that the sector is contracting
- **Manufacturing** also slowed further; the PMI fell 1.8 p to 46.6, 1.2 p below consensus. The output index decreased 2.1 p to 44.2, and the new order index declined by 3.5 p to 37.8, a level only reached twice before, during the pandemic and the financial crisis!
- **The delivery times** and price indices both fell but remain higher than normal. However, as new orders and production are both is declining, supply chains problems and pricing power will very likely be further reduced the coming months
- If the PMIs and other surveys continue down at the current pace, the pressure on (and within) the **ECB** to hike rates rapidly will no doubt fade, even if inflation is high and unemployment is low. Wage inflation has not yet exploded, and the underlying cost pressure is not like in the US

Manufacturing sector contacting for the fourth month; services further below par

The output index decreased 2.1 p to 44.2: a sharp decline in production is reported



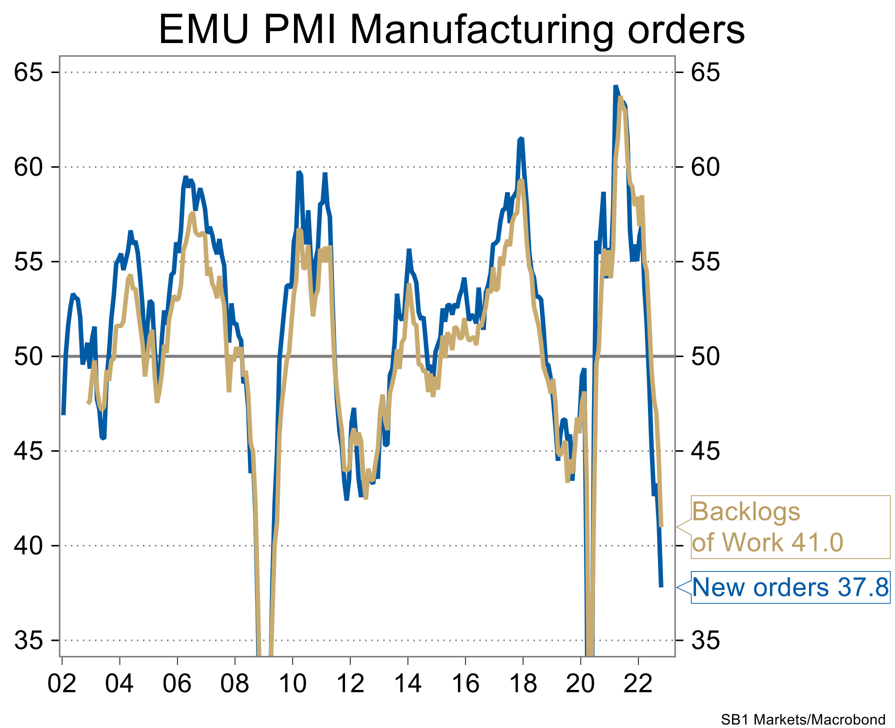


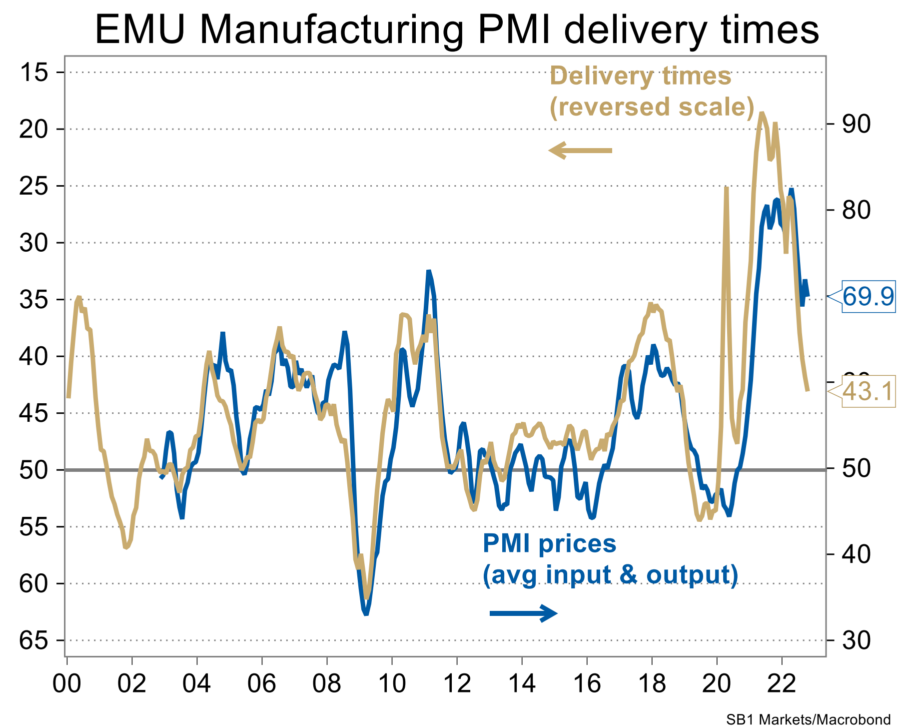


- German manuf. PMI decreased by 2.1 p to 45.7, and the French manuf. PMI fell by 0.3 p to 47.4. The total EMU manuf. PMI was down 1.8 p to 46.6
- The EMU service sector as a whole is likely contracting, as the PMI fell by 0.6 to 48.2

New orders index has only been lower twice; during the GFC and the pandemic

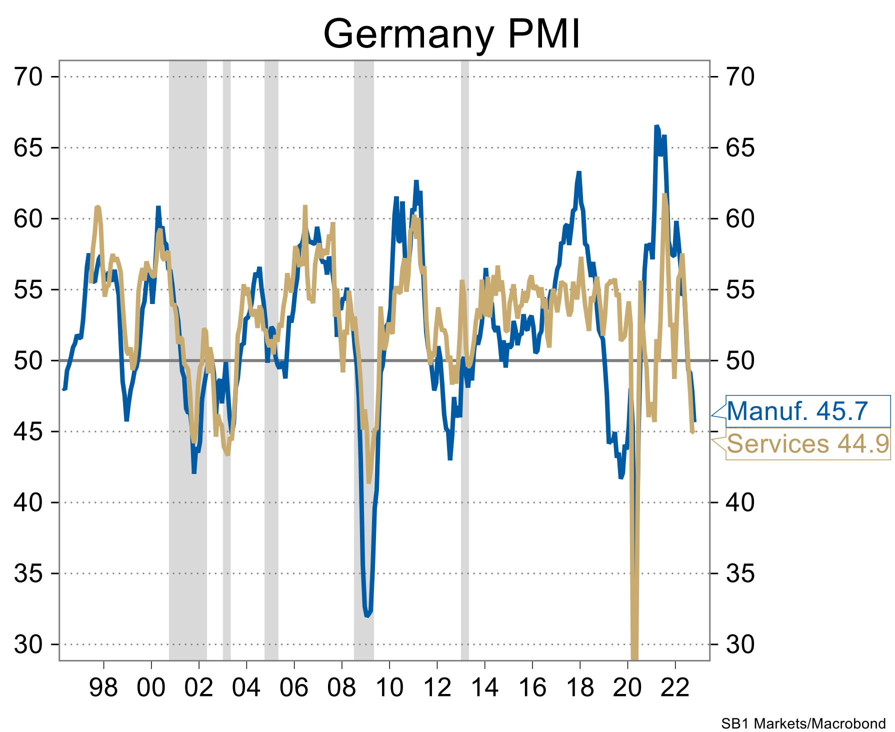
The order backlog fell further. Delivery times are declining, but prices are increasing at a slower pace

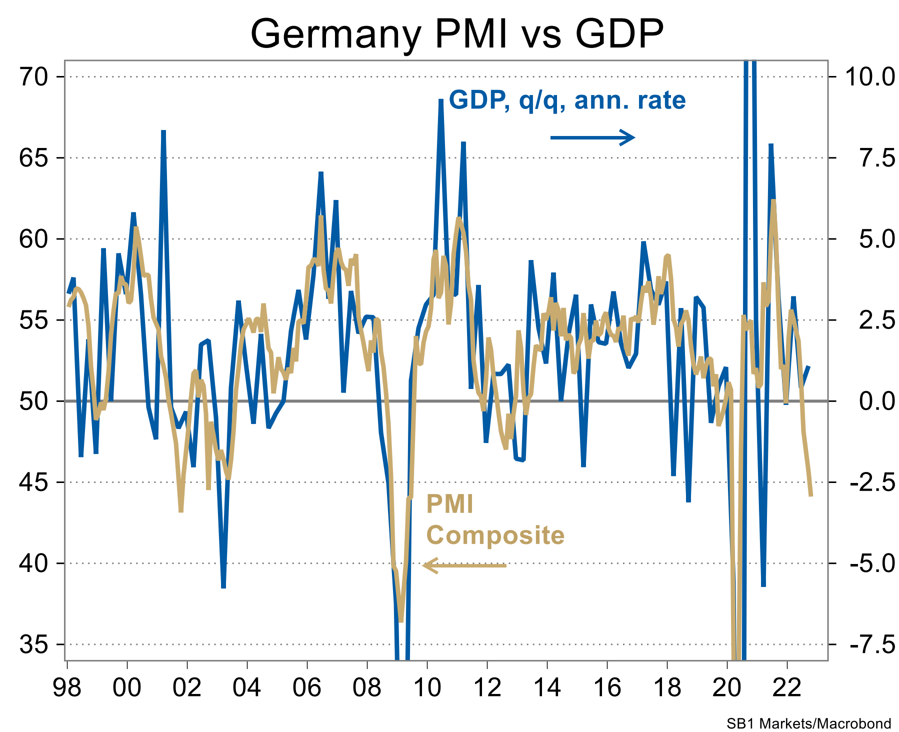




Germany: Weakest PMI since June-09, barring the pandemic

High energy costs is detrimental for both supply and demand

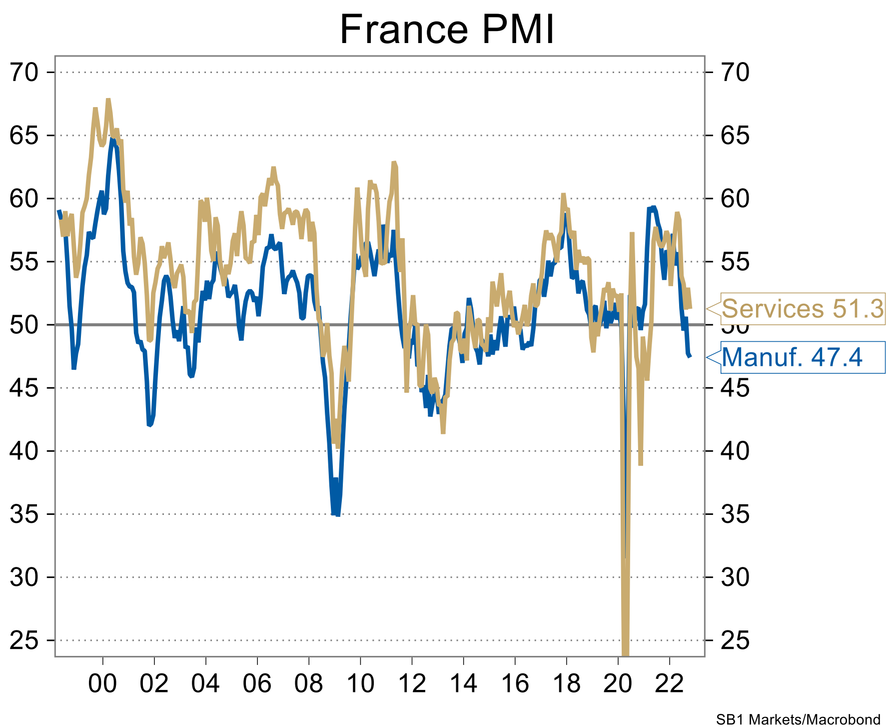


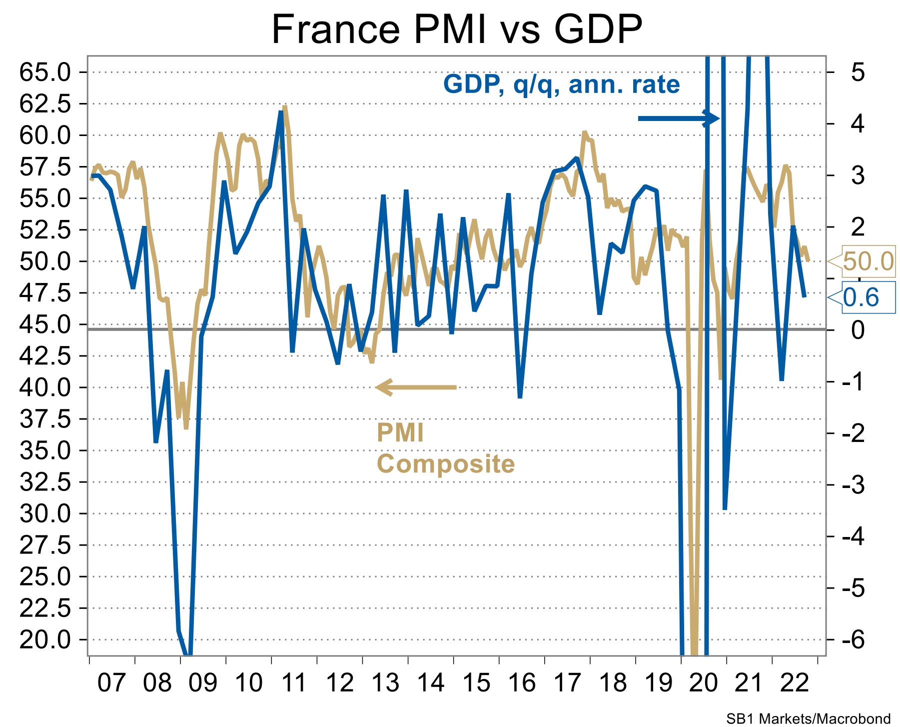


- Higher interest rates and a general high inflation rate are also not helping
- The composite PMI was down 1.6 p to 44.1 in October, expected 45.3. The current level indicates a 2.5+% contraction in GDP
- Both manufacturing and services were down; however the fall in the services PMI was marginal

France: Composite PMI down to 50 in Oct, indicating 1 – 1½ % growth

The services PMI fell 1.6 p to 51.3, while manufacturing was down 0.3 p to 47.4, beating expectations

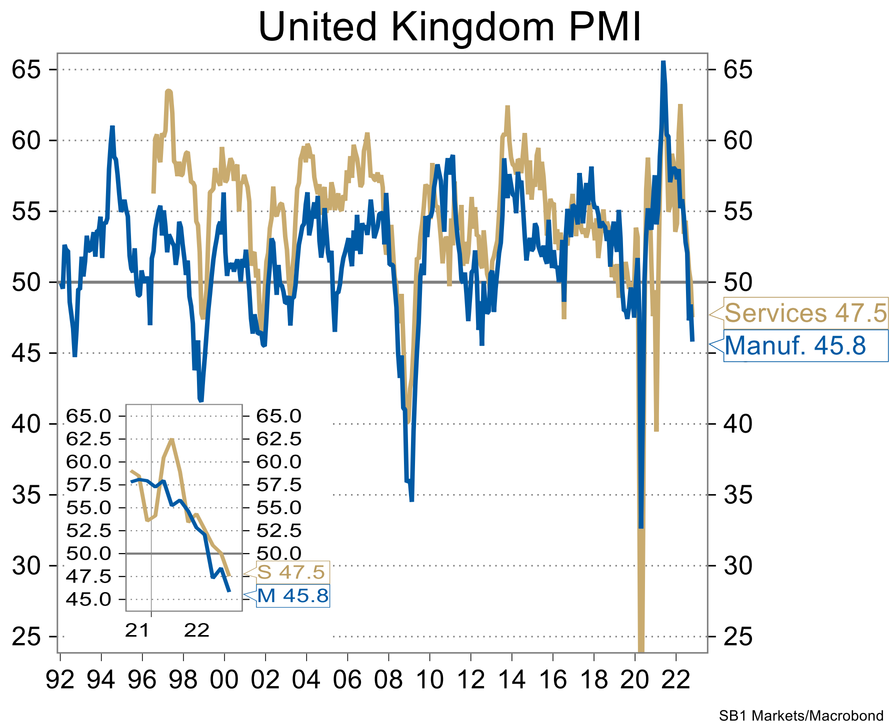


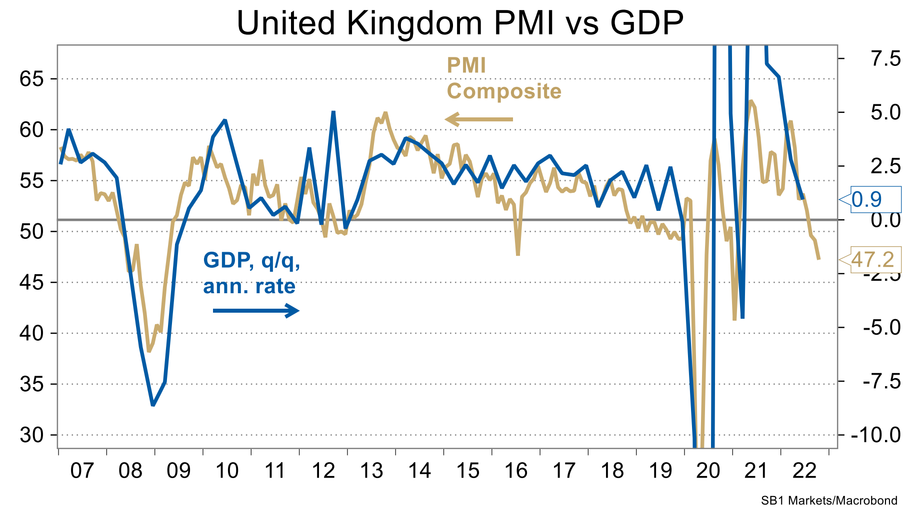


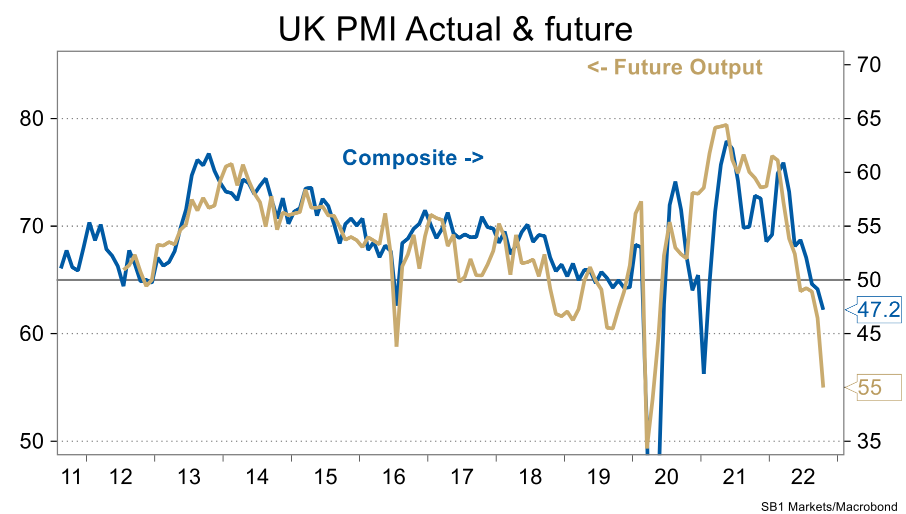
- The difference between France and Germany? Energy prices, at least in the CPI. The headline CPI is up 7.1% in France vs 11.6% in Germany

High inflation, rising interest rates & political chaos sends PMIs further down

The composite index further down in October – the UK economy is in stagnation



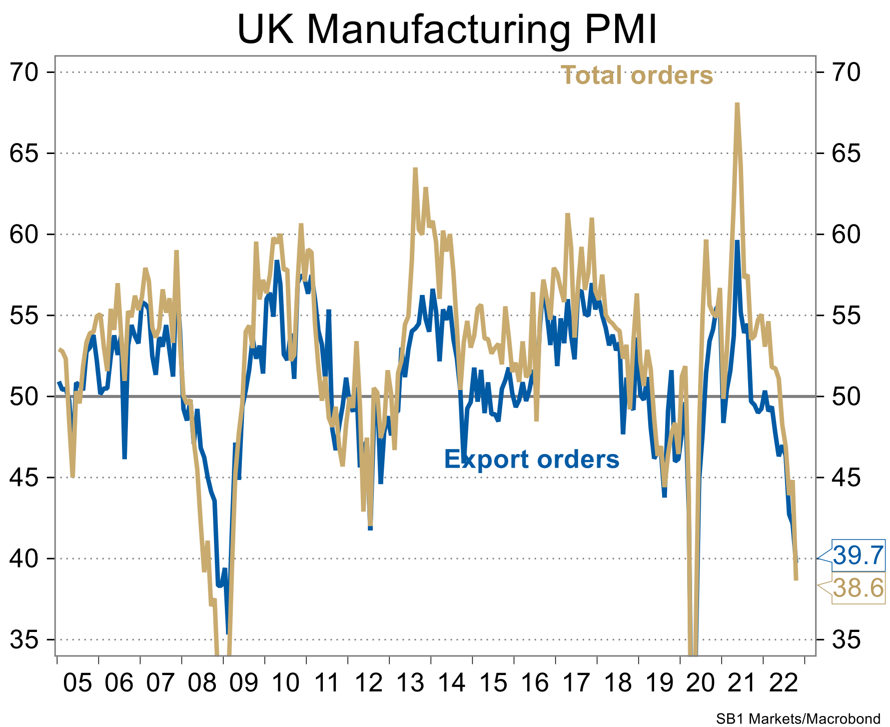


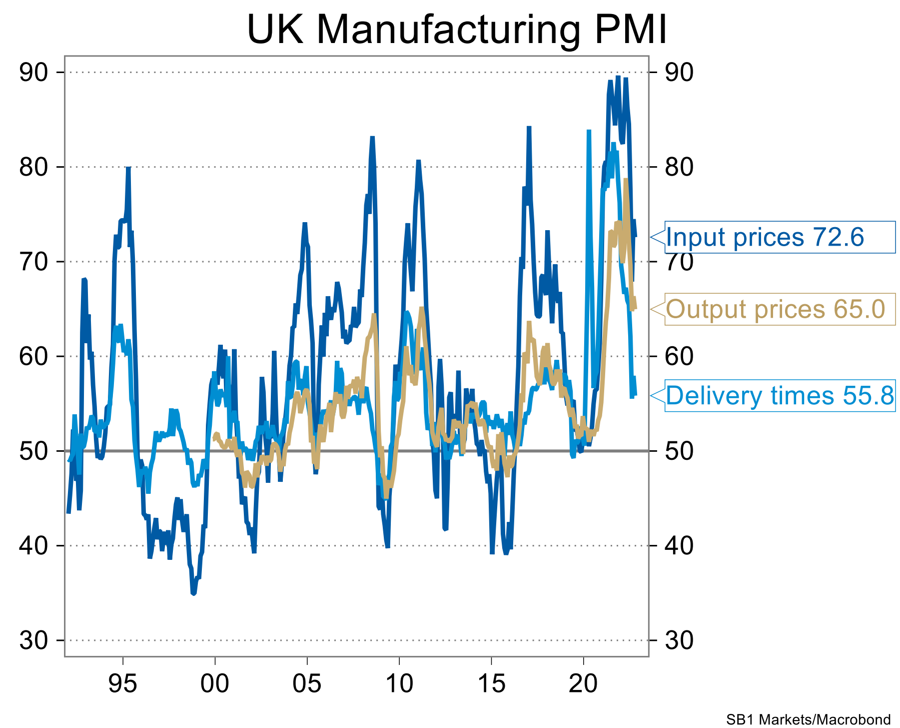


- The UK composite index fell 1.9 p to 47.2 in Oct, expected 48.1. The manufacturing PMI surprised massively on the downside, falling 2.6 p to 45.8; 2.2 p below expectations. The services PMI was also on the weak side, down 2.5 p to 47.5, expected 49.6
- Growth is clearly coming to a halt, while the latest inflation print was at 10.1% (core at 6.5%), putting the BoE in a bit of a squeeze. A recession is unavoidable? That what's the BoE thinks too, as it continues to hike its bank rate

Orders are collapsing, down to the 30s! Prices indices down, but remain very high

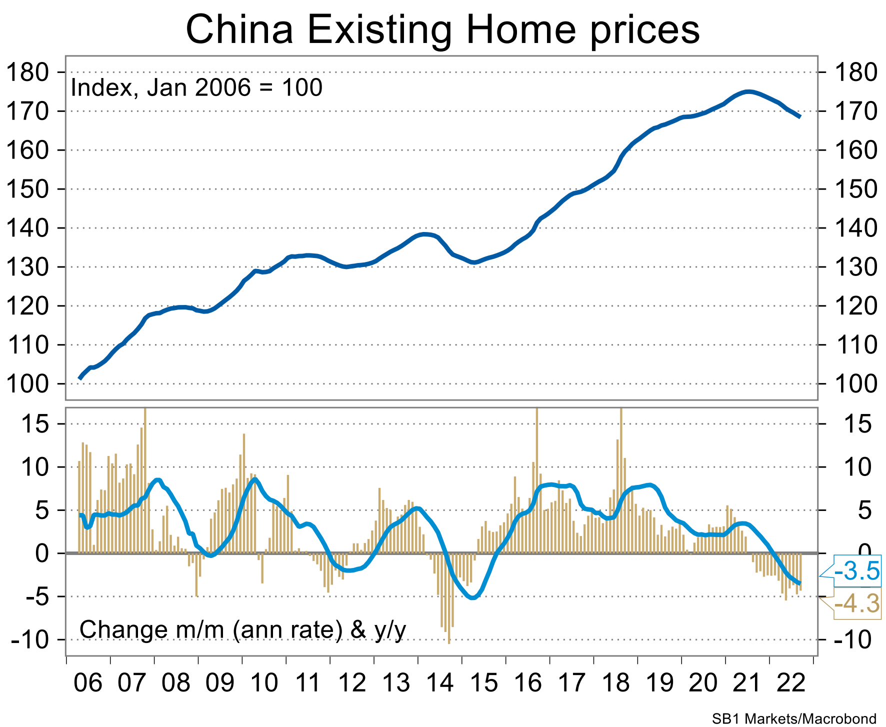
Delivery times seem to have normalised

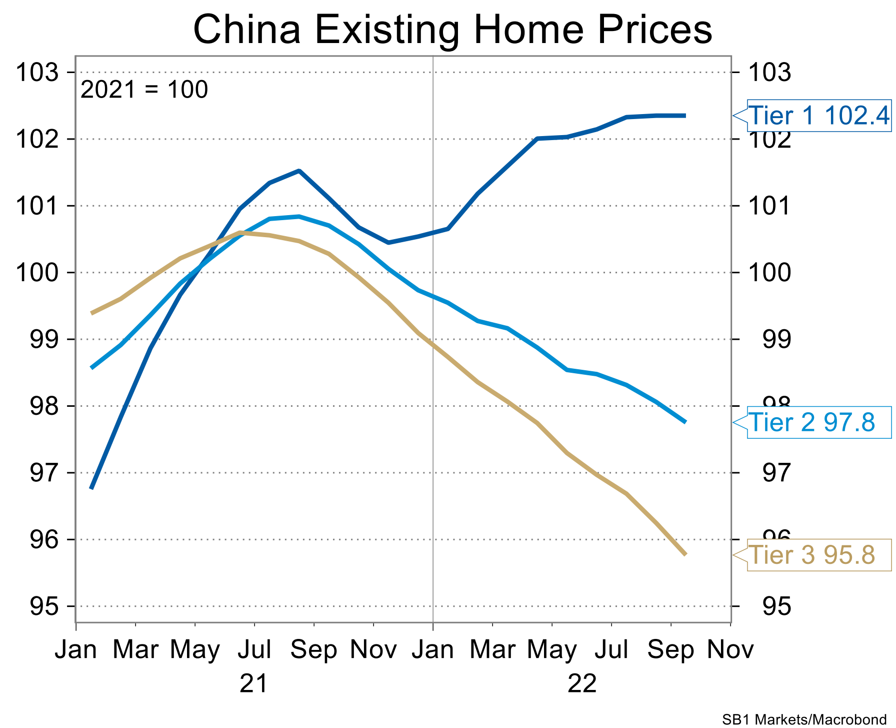




Existing home prices fell further in August – for the 13th month in row

- the longest stretch with falling prices ever. New home prices on the way down too

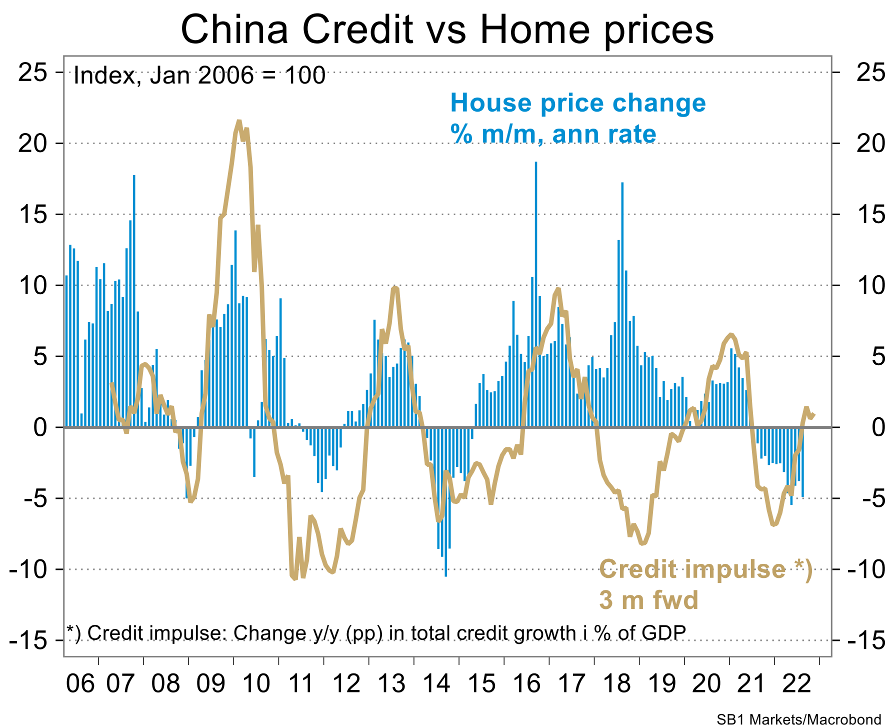




- **Existing home prices** peaked last July, and have been falling at a gradually faster pace, until May. In September, prices fell at 4.3% pace. Prices are down 3.5% y/y, less than the price setback in 2014/15. However, the current setback has now lasted longer than the previous
- **New home prices** also fell last autumn but at a slower pace than existing home prices. In September, prices fell 2.4%, and they are down 2.3% y/y. Some builders have reported deep price cuts to reduce the inventory and secure financing. The gradual decline in prices since last summer is probably due both some fire sales from construction companies that have run out of other sources of financing, and some hesitance from home buyers
- Prices are still climbing (albeit slowly) in the **four largest Tier 1 cities**, but are falling elsewhere – and at the fastest pace in the 'smaller**' Tier 3 cities**
- **Central authorities** have signalled willingness to expand credit supply again, both to finance infrastructure projects and the construction sector, mostly through local governments that would be allowed to borrow (even) more

Credit growth has accelerated marginally but mostly due to local gov. borrowing

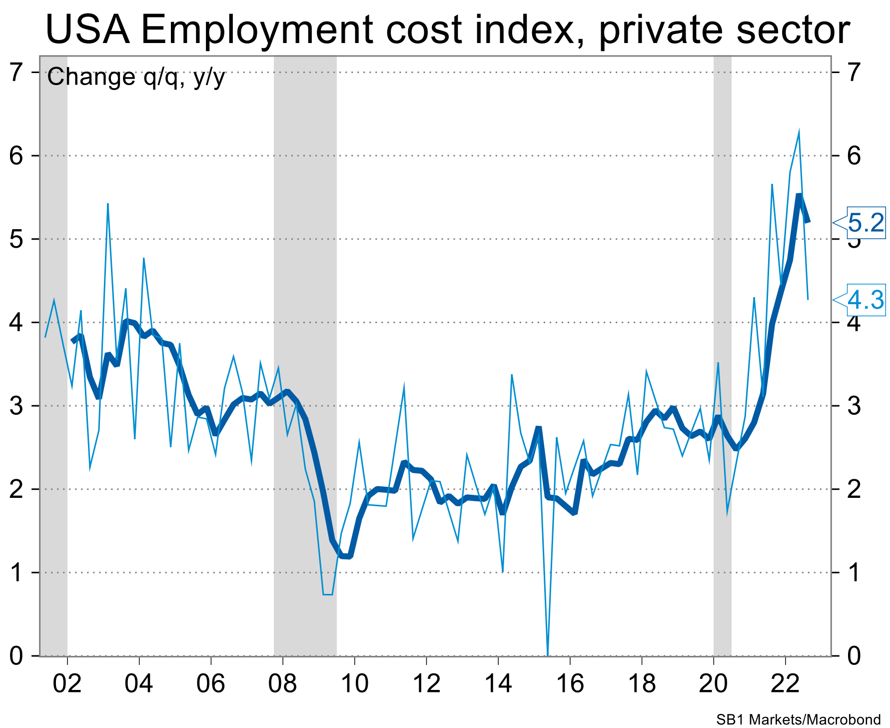
… to compensate for lower income from land sales (which constituted 40% of local gov. revenues)

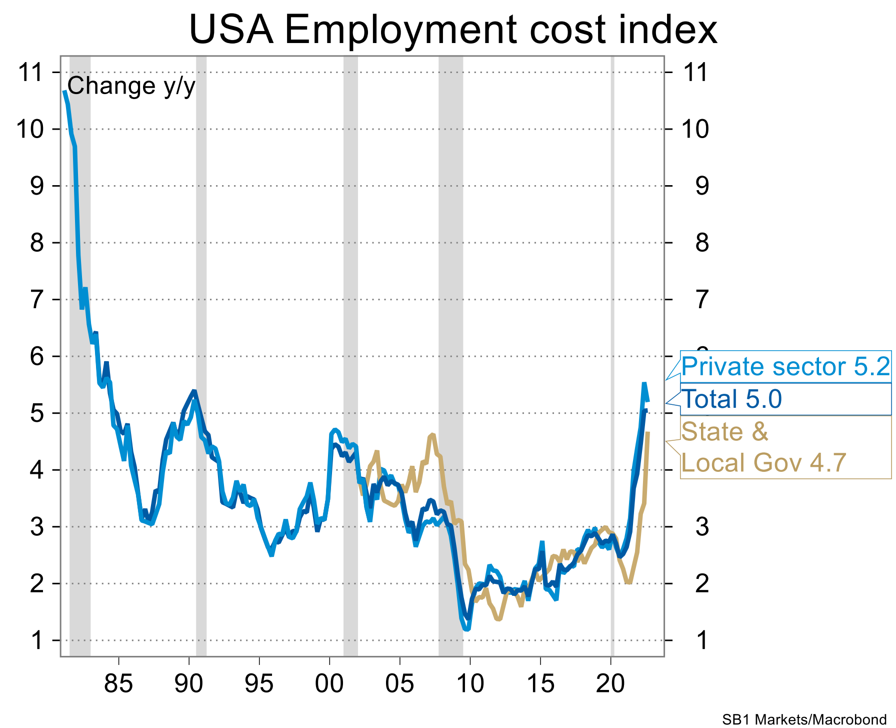


- These land sales equalled 6.5% of GDP last year
- Sales of land to developers have nosedived so far in 2022, down some 60% - and more than 50%, measured in size
- The central government last week forbid local government to sell land to their financial vehicles (LGFV) in order to boost local government revenues. These LGFV have funded this land ‘buying’ by taking on more debt - which the Ministry of Finance described as a ‘sham’, as it is hidden from the official accounts of the local governments – but still in the end is a liability for them

Employment cost inflation fell in Q3, according to the ECI. Still far too high

ECI inflation is more than 2½ pp above the 10 y average – which yielded 2% CPI inflation

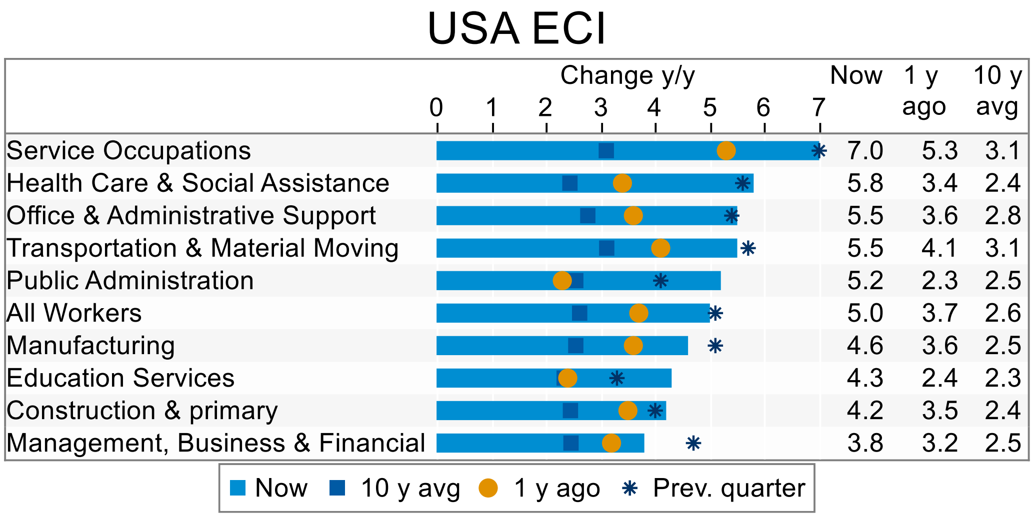




- The **Employment cost index for all civilian workers**, which measures wages and other wage costs for <u>the same types of jobs (and is not influenced by changes in employment between sectors/type jobs)</u>, rose by 1.2% q/q in Q3, as expected, and down from 1.3% in Q2. The annual rate was unchanged at 5.0%, the highest level since 1990, and ><u>2.5 pp above the 10 y average before the pandemic</u>
  - In the private sector, the ECI rose by 1.1% q/q (4.3% annualised), down from the 'dramatic' 6.3% in Q2, when some bonus payments boosted the ECI. The average of Q2 and Q3 is at 5.3%. The annual growth is 5.2% y/y, down from 5.5% in Q2
  - State and local gov employment costs shot up in Q3, to 4.7% from just 3.4% y/y, and the discrepancy to the private sector narrowed
- <u>**Wage inflation** is the real problem for the Fed, far more than the impact of high energy/food/raw material prices</u>. Those commodity prices are already on the way down, and the contribution to CPI inflation will come down

Employment costs are growing faster than normal in all sectors

... a substantial cost push risk vs inflation. Annual cost inflation slowed in 3 sectors, accelerated in 5

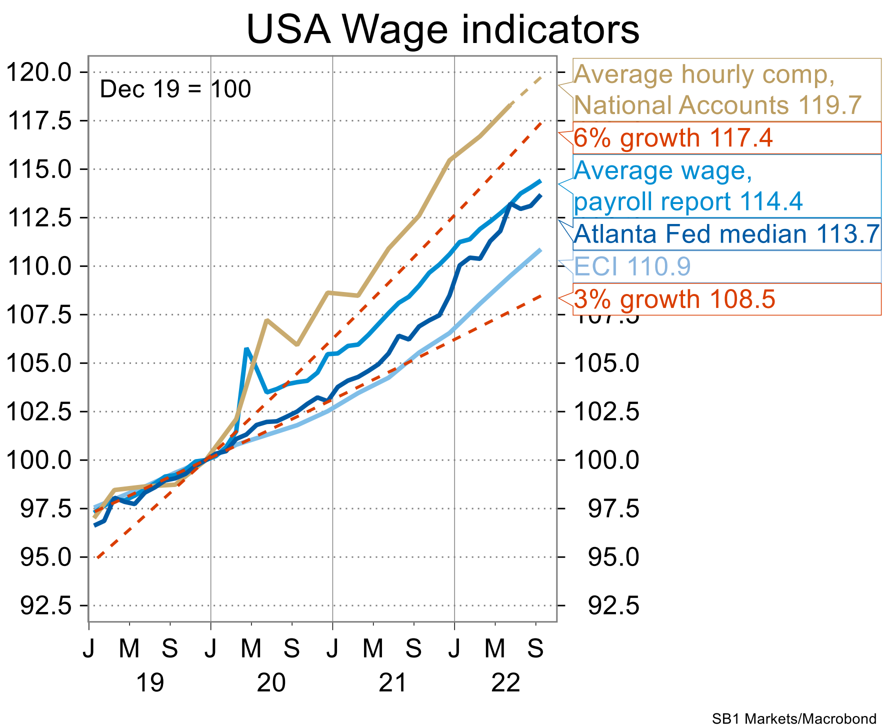


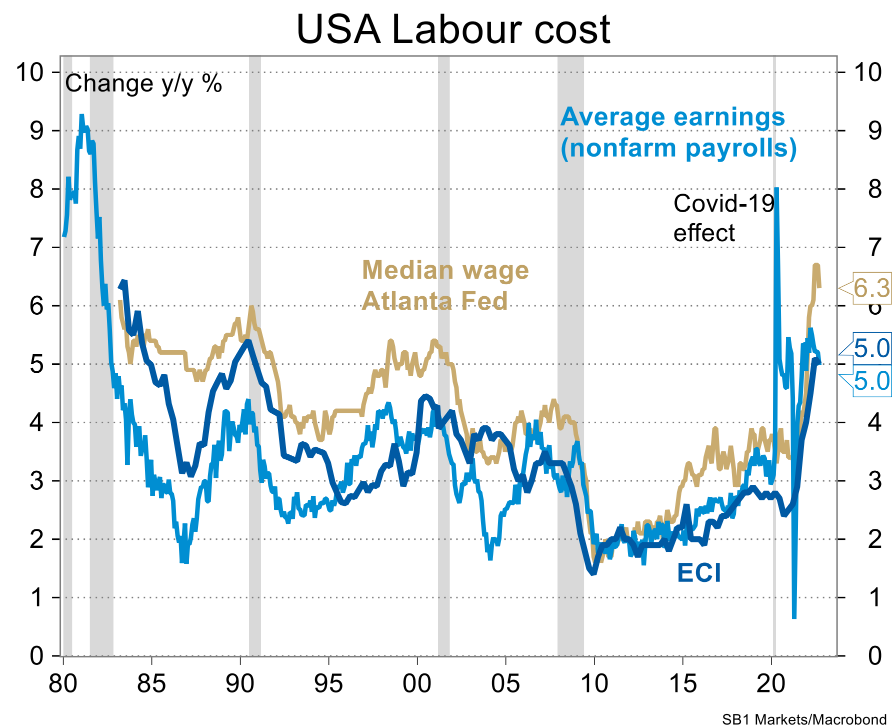
	Now	1 y ago	10 y avg
Service Occupations	7.0	5.3	3.1
Health Care & Social Assistance	5.8	3.4	2.4
Office & Administrative Support	5.5	3.6	2.8
Transportation & Material Moving	5.5	4.1	3.1
Public Administration	5.2	2.3	2.5
All Workers	5.0	3.7	2.6
Manufacturing	4.6	3.6	2.5
Education Services	4.3	2.4	2.3
Construction & primary	4.2	3.5	2.4
Management, Business & Financial	3.8	3.2	2.5

SB1 Markets/Macrobond

Wage inflation remains far too high, according to all wage indicators

Current wage inflation is 2.5 – 3.5 pp higher than the 10 y average before the pandemic



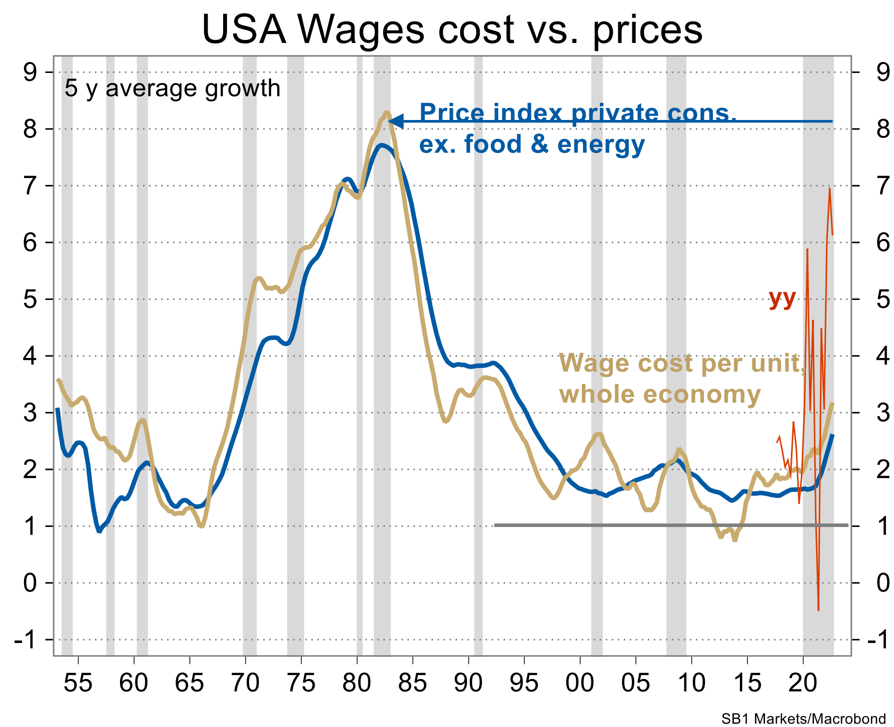


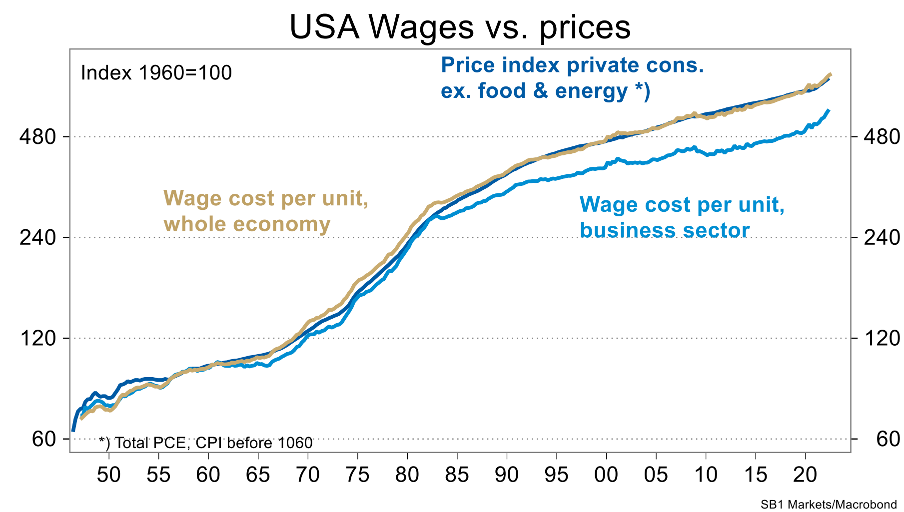
- **All wage indicators** are reporting faster wage growth, and all reporting wage growth well above the average over the recent years
- Over the past 10 years, inflation has been close to 2%, and well above 2% if calculated over a shorter period
- It will be a 'challenge' to keep CPI inflation at 2% if wage inflation remains 2.5 – 3.5 pp higher than rates that have produced 2% price inflation. Productivity growth has not accelerated. Profit margins may take a beating – and they no doubt will – <u>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 – aka a recession</u>

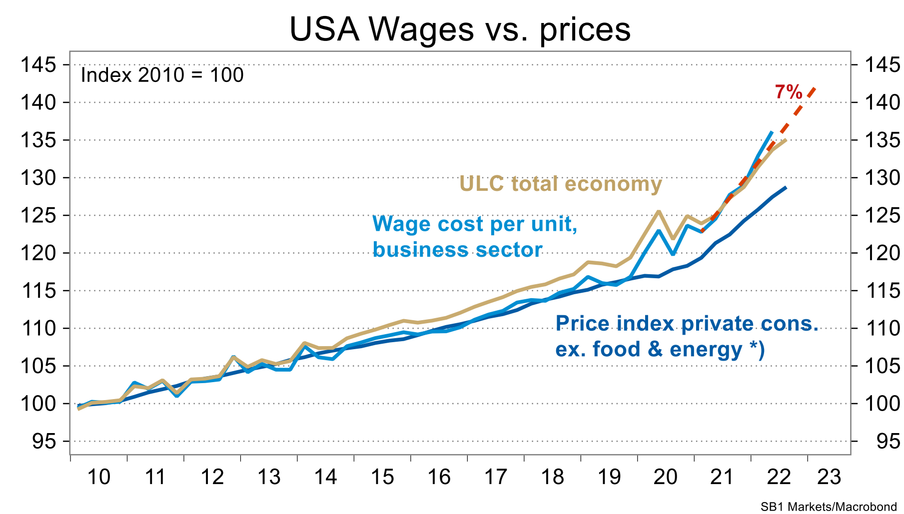
SpareBank 1 MARKETS

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

Wage cost per unit produced in the whole economy is up 6% y/y





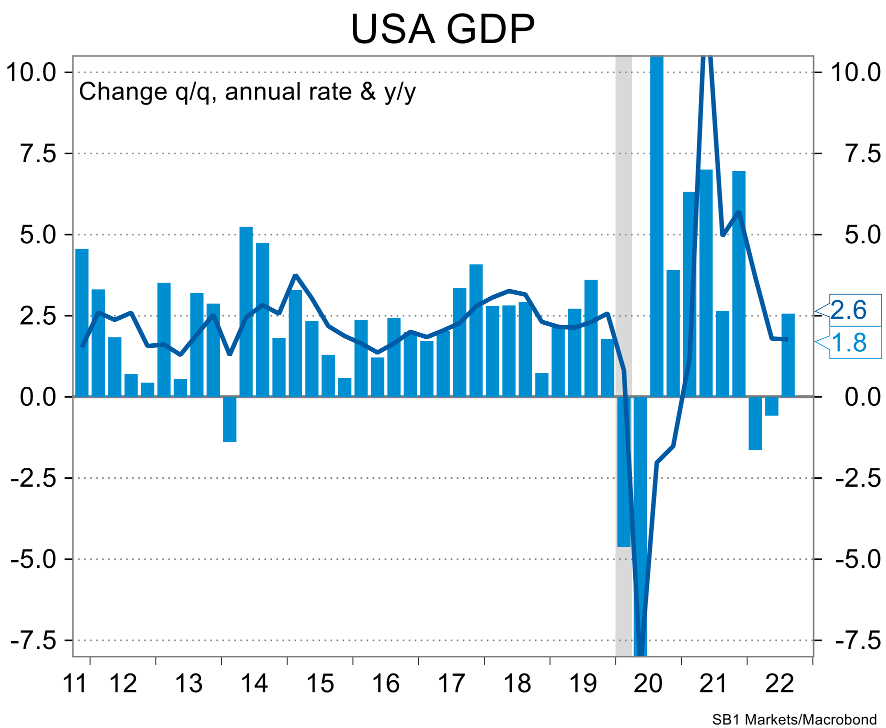


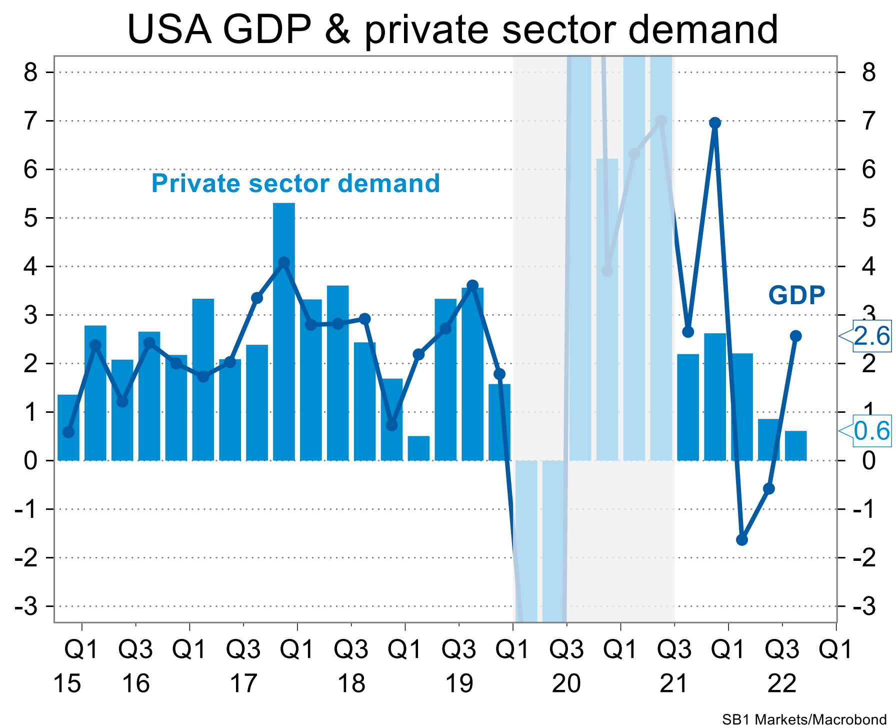
- **Labour cost per unit produced** (ULC) is the main, and in fact in practice the only, driver of inflation over time
- Now, the underlying growth in ULC is at 6% – 7%, yielding the same rate of inflation over time. That's Fed's challenge

SpareBank 1 MARKETS

GDP recovered in Q3, due to net exports. Domestic private demand up just 0.6%

GDP grew 2.6% in Q3, expected 2.3% - up from a -1.1% pace of decline in H1. So far in 2023: +0.3%

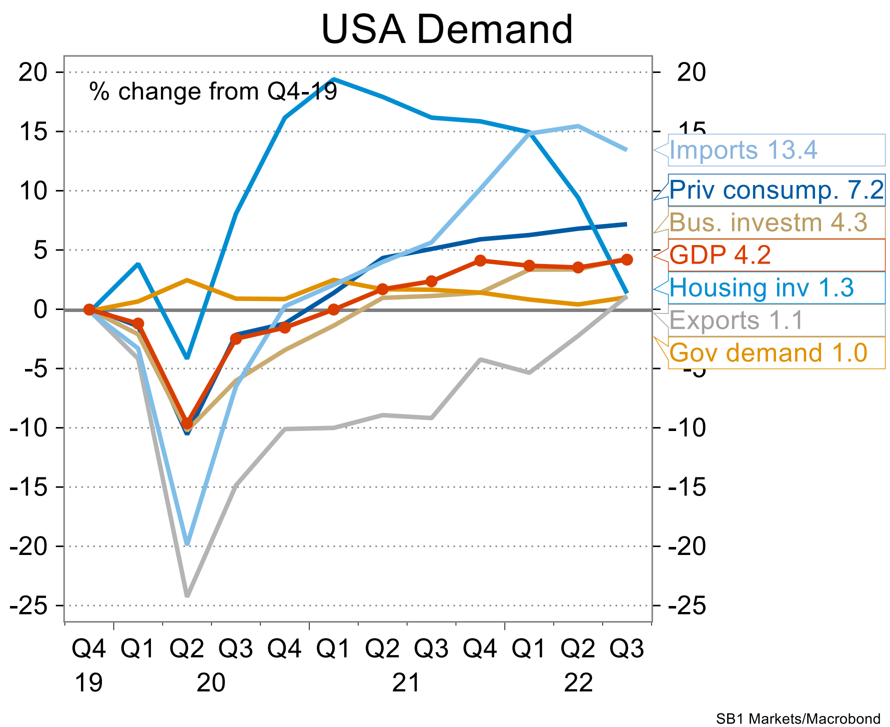


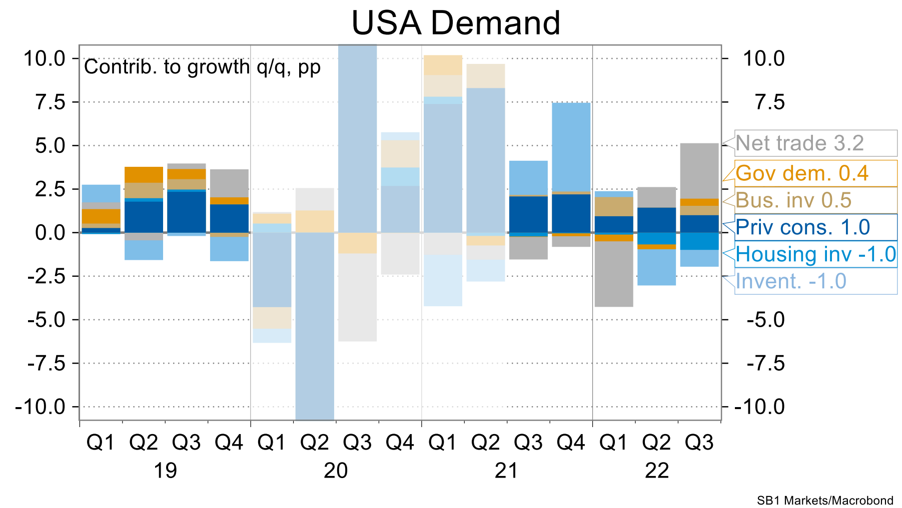


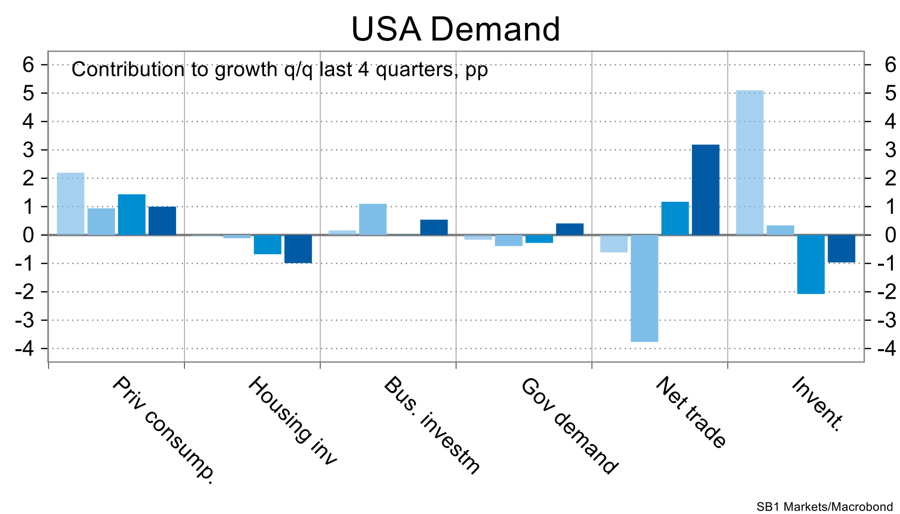
- Following a decline in both Q1 and Q2, GDP recovered in Q3, as imports fell and exports rose. Net trade lifted domestic production by 3.2%, that is more than the overall growth in GDP
- Growth in **private sector demand** has slowed the past three quarters, and fell to 0.6% in Q3. Private consumption rose 1.4%, more than expected, and contributed by 1 pp to GDP growth. Investments fell, due to business structures and housing. Housing fell 26%, deducting 1 pp from GDP growth!
- **Inventories** rose at a slower pace, which reduced GDP growth by 1 pp (and the net contribution from trade and inventories is 2.2 pp). Inventories may still be somewhat too high
- **Core PCE inflation** (Fed's price measure) slowed as expected to 4.5%, while the overall GDP deflator grew 'just' 4.1% in Q3, as energy prices fell
- We assume **corporate profits** flattened in Q3, as the total wage cost probably grew faster than value added

Higher exports, lower imports the story in Q3. And the 'collapse' in housing

Business investments rose slightly, while inventory build-up slowed



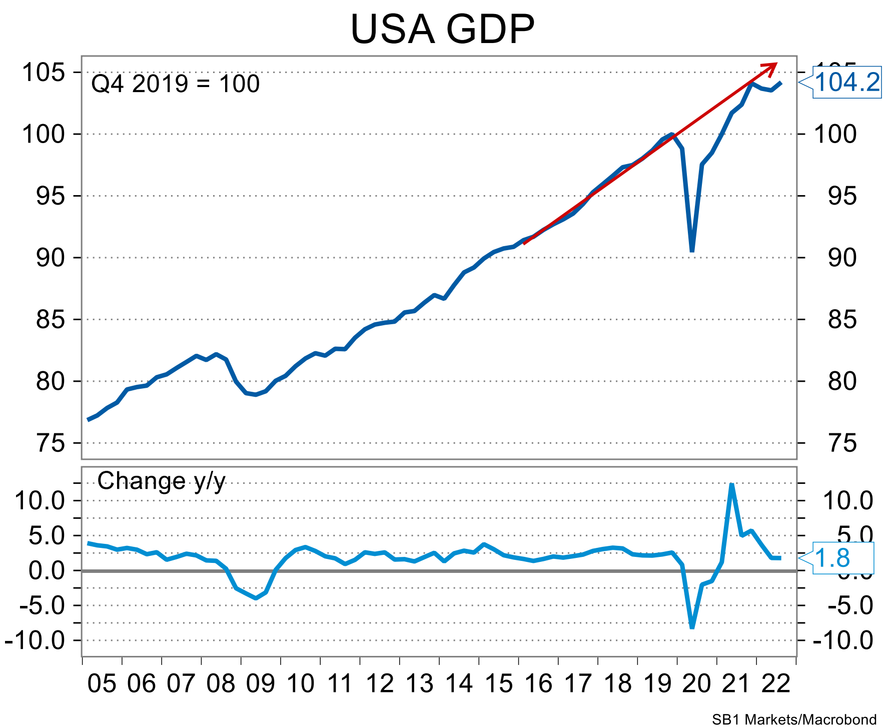


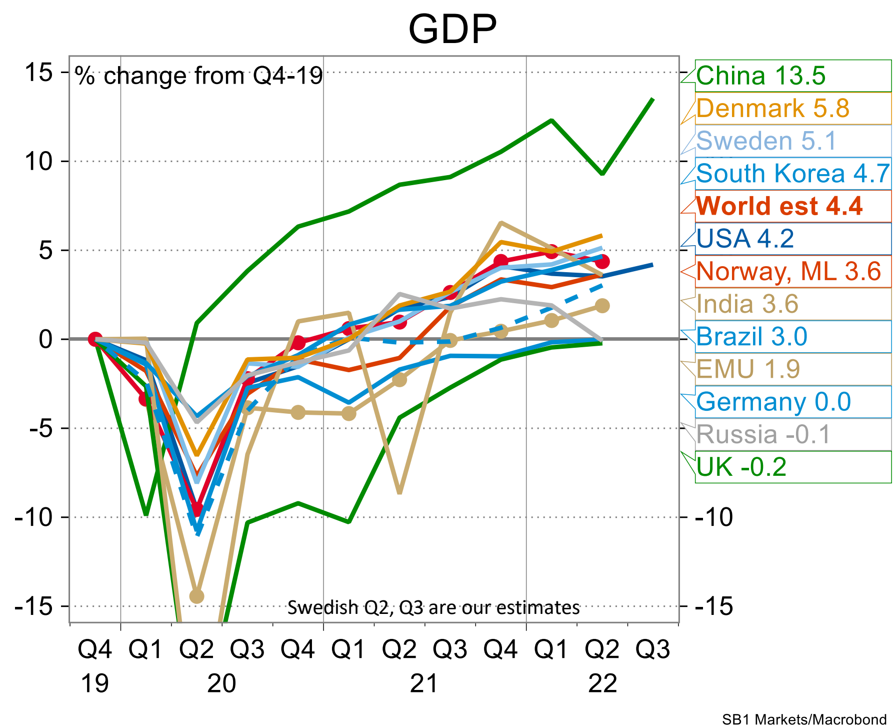


We have shaded the 'hard' pandemic quarters at the chart on the top

GDP up 1.8% y/y (unch.), and revised up (check next page)

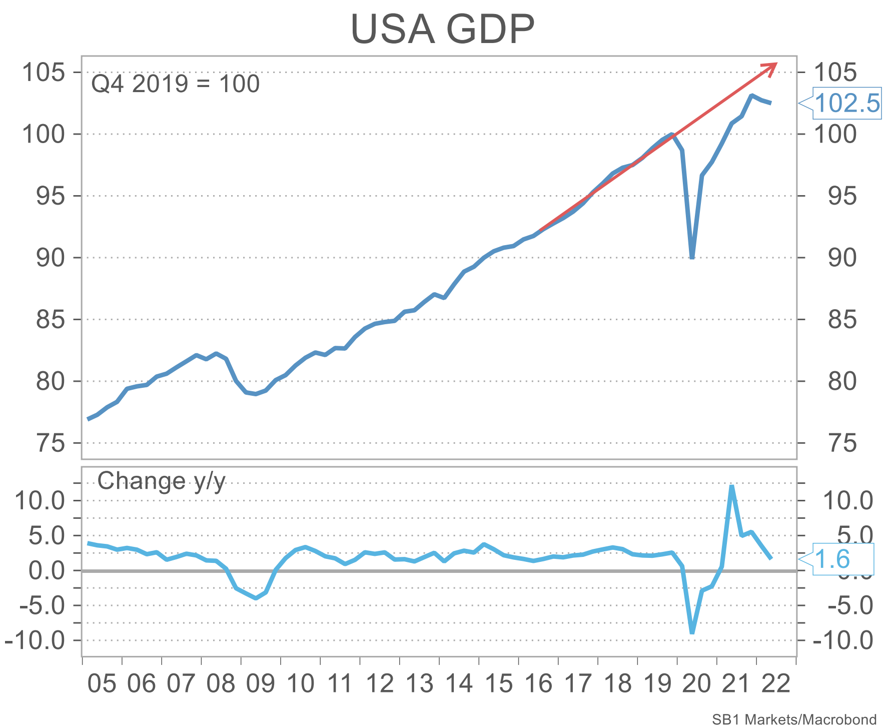
However, GDP is still almost 2% below the pre-pandemic growth path





Spot the difference: GDP before the annual revision (published some weeks ago)

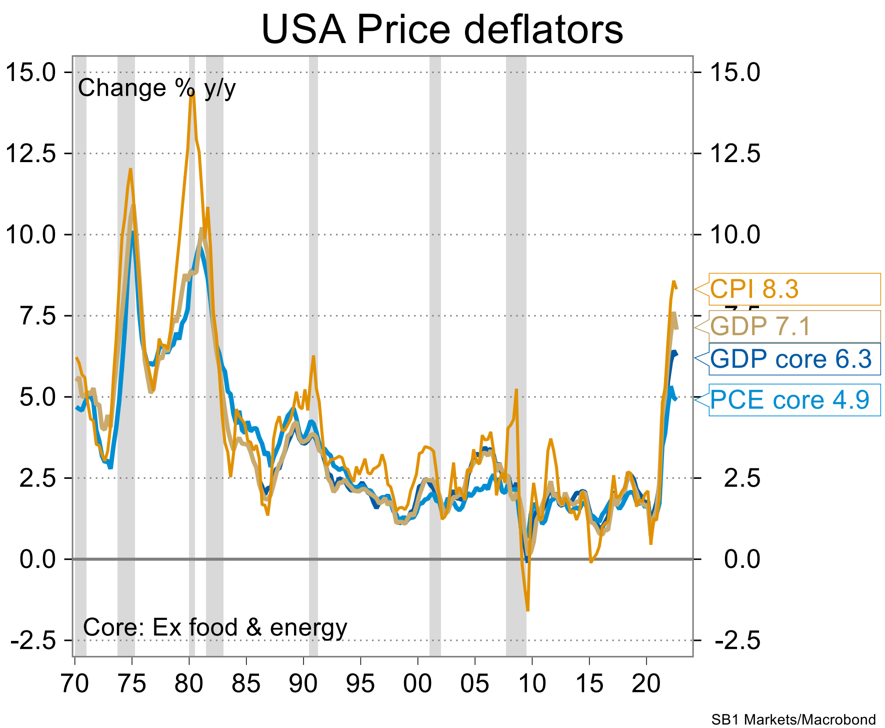
The GDP level in Q2-22 was revised up by 1%

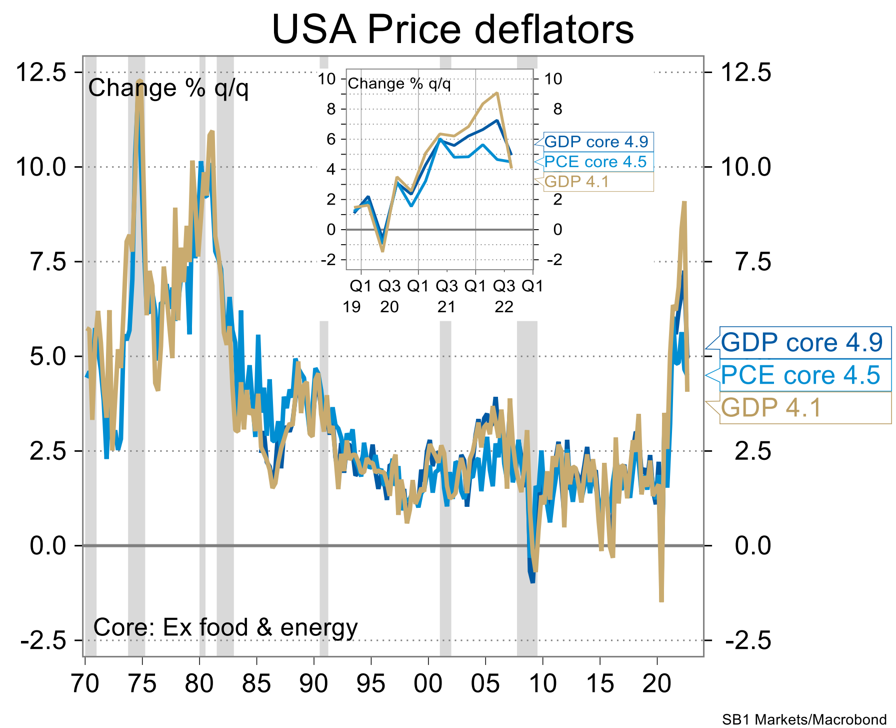


Swedish Q2, Q3 are our estimates

Peak inflation: The GDP price deflator sharply down in Q3, as oil/gas prices fell

Still, up 4.1% in Q3, down from 9.1% in Q2. The core GDP deflator still up 4.9% (and up 6.3% y/y)

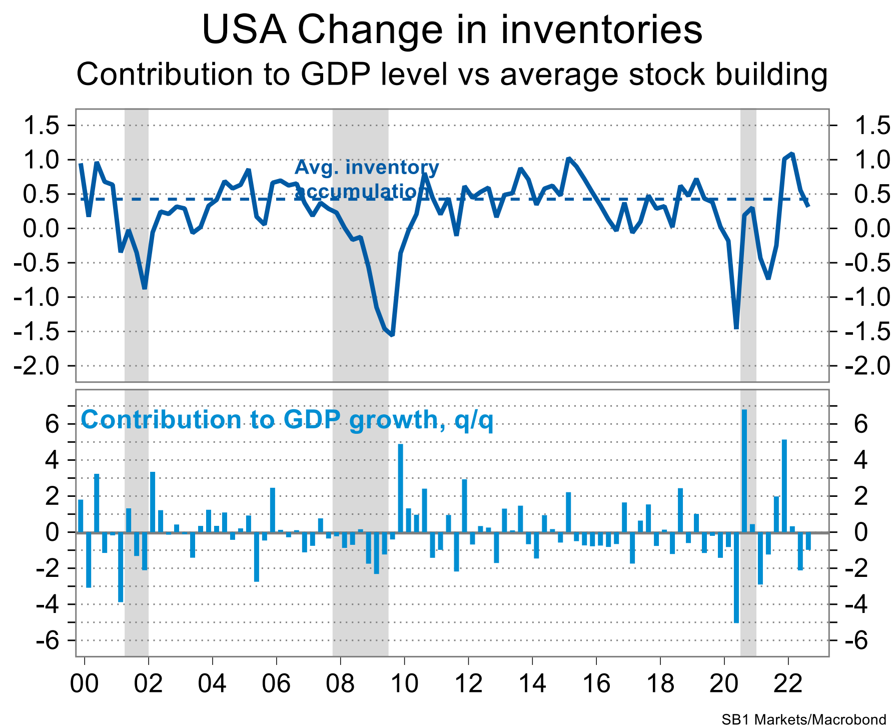


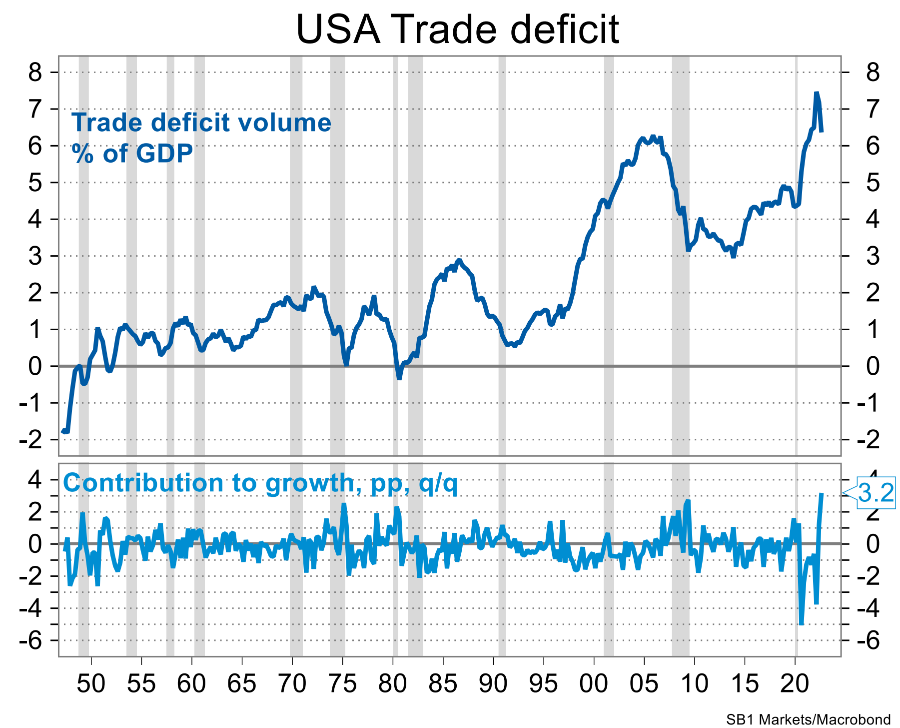


- The core (x energy, food) PCE (private consumption) deflator, Fed's preferred inflation measure rose 4.5% in Q3, down from 4.7% in Q2, as expected. The core PCE inflation peaked in Q2-21

Inventory growth slowed – but not a real reduction yet

Inventories may be somewhat too high, even if the buildup the previous quarters was not that large



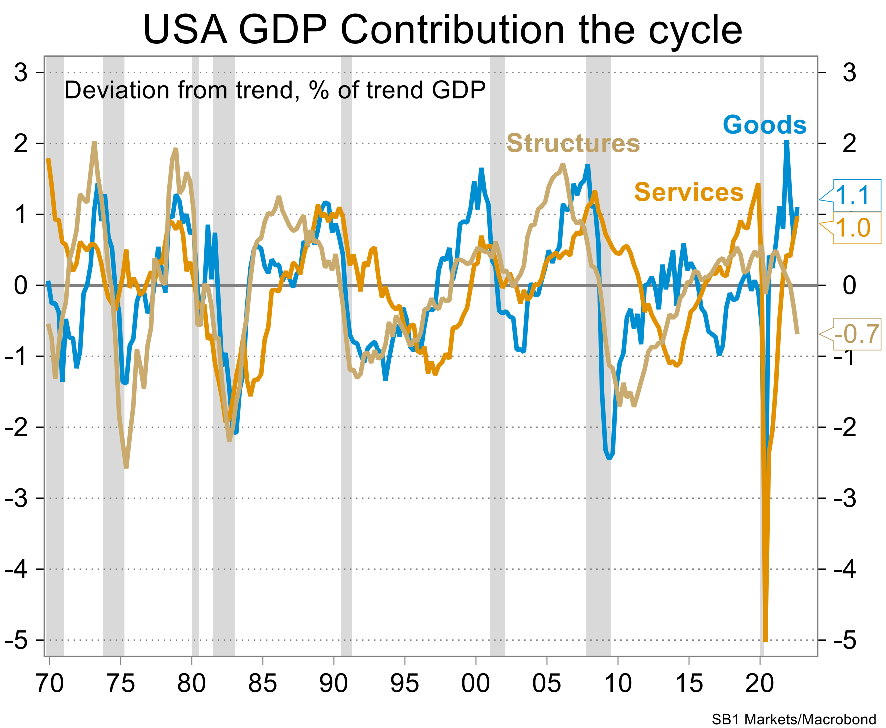


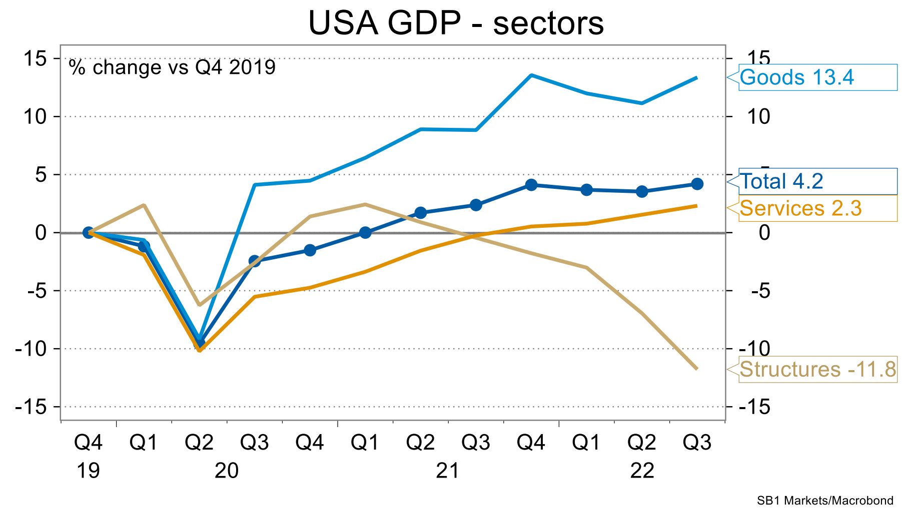
- **Inventories** rose at close to a normal pace in Q3, from above the previous 3 quarters
- **The trade deficit** narrowed sharply in Q3, but remain large, measured in volume terms

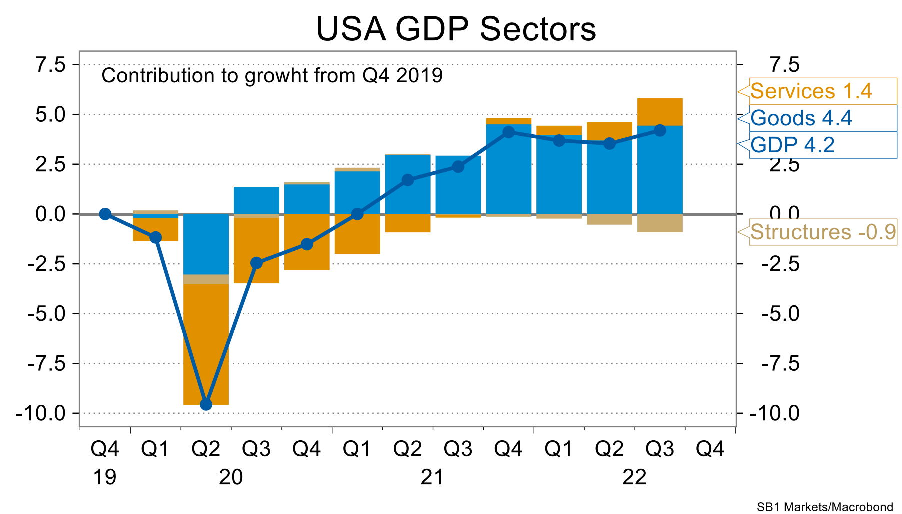
SpareBank 1 MARKETS

Structures (construction) sharply down, services still rapidly on the way up

Goods have more or less stabilised

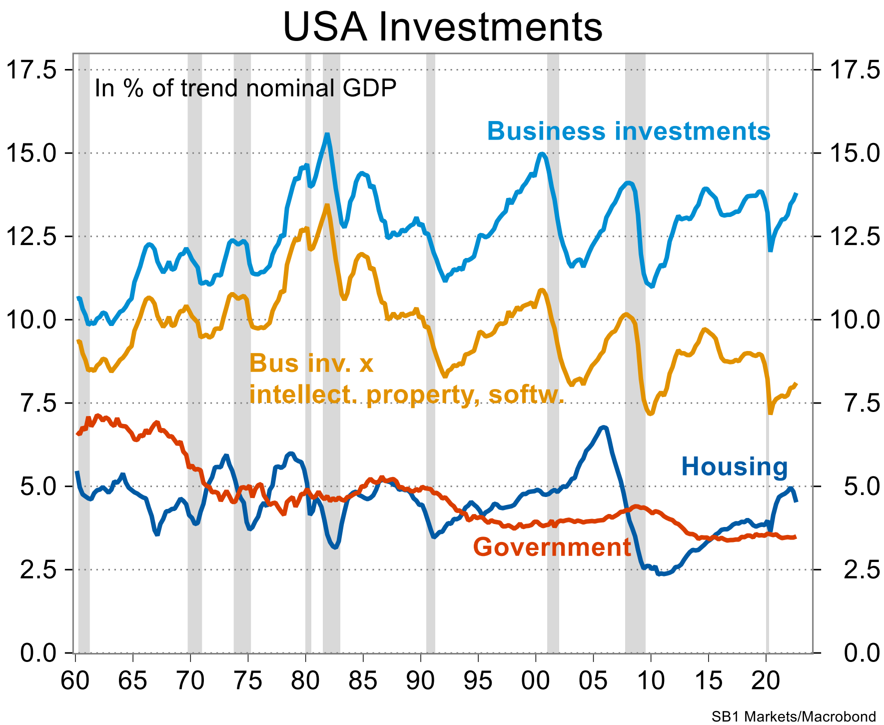


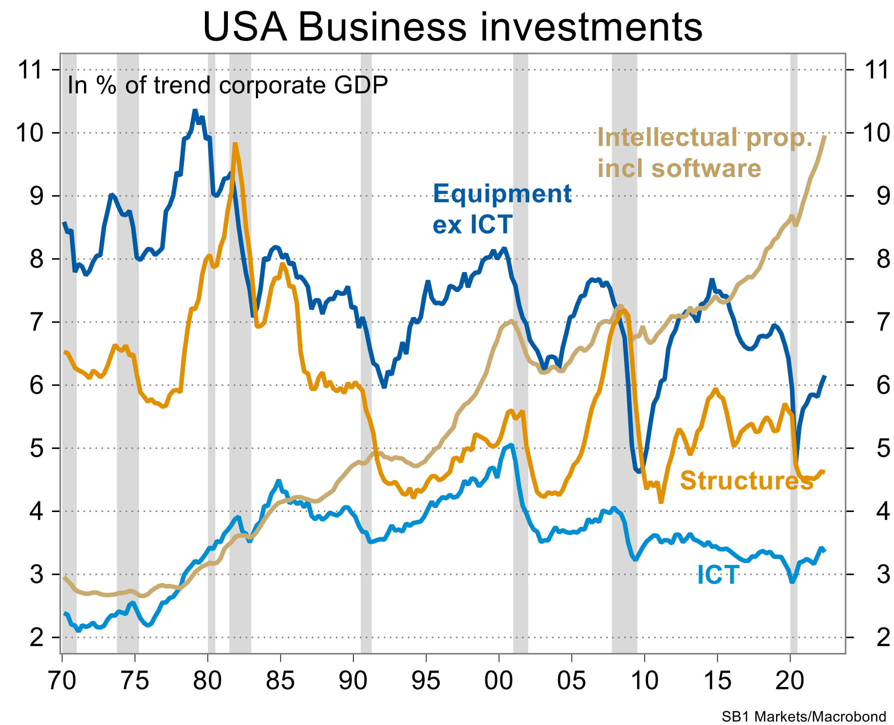




Investments: Housing has turned south, and business structures down in Q3

Business investments above trend just due to IP & software, ICT. Other equipment, structures still weak



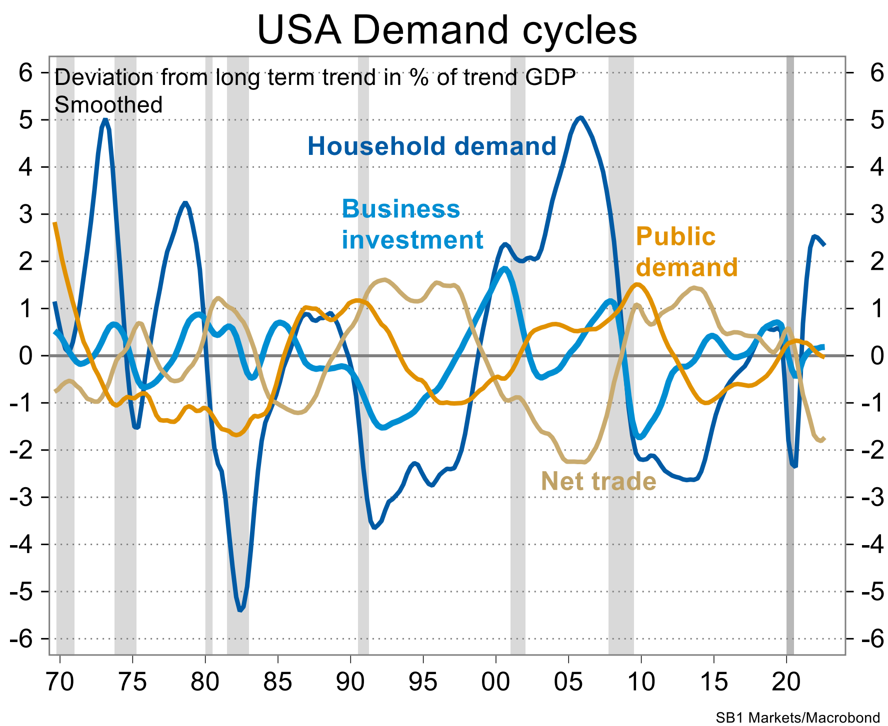


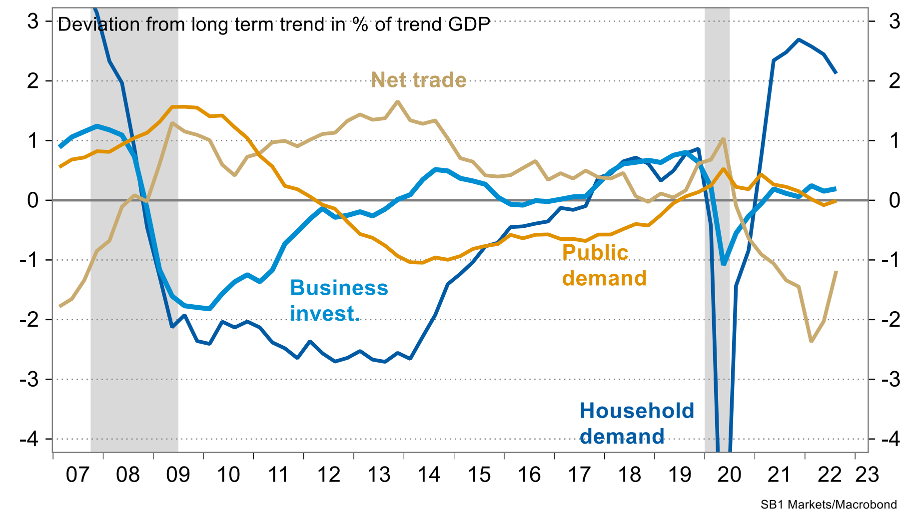
- **Business investments** are up 4.3% vs. the Q4-19 level (in volume terms), driven IP/software and ICT equipment. Investments in structures are still very low. Investments in equipment x ITC may is most likely below trend
  - » Thus the outlook for business investments is not clear: The boom in IP/software/ICT may well continue, even if the levels are high. Anyway, these investments have so far been less exposed during recessions than other types of investments. Investments equipment are above trend but not by much. Investments in structures are below a declining trend
  - » However, higher interest rates, and weaker growth in demand does not normally support business investment, and we are probably close to the peak in Q3
- **Housing investments** fell 26% in volume terms (annualised), and housing investments/GDP fell visibly. The investment level is still not low, and given the decline in construction starts, a substantial downside risk
- **Government investments** as share of GDP are rather trending down than up

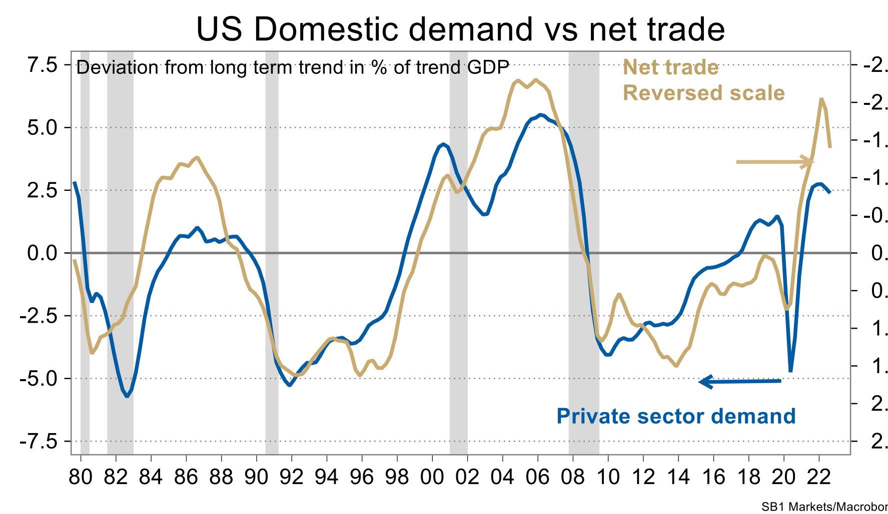
SpareBank 1 MARKETS

Both household demand and public demand is slowing

The downside risk is probably the largest for household demand



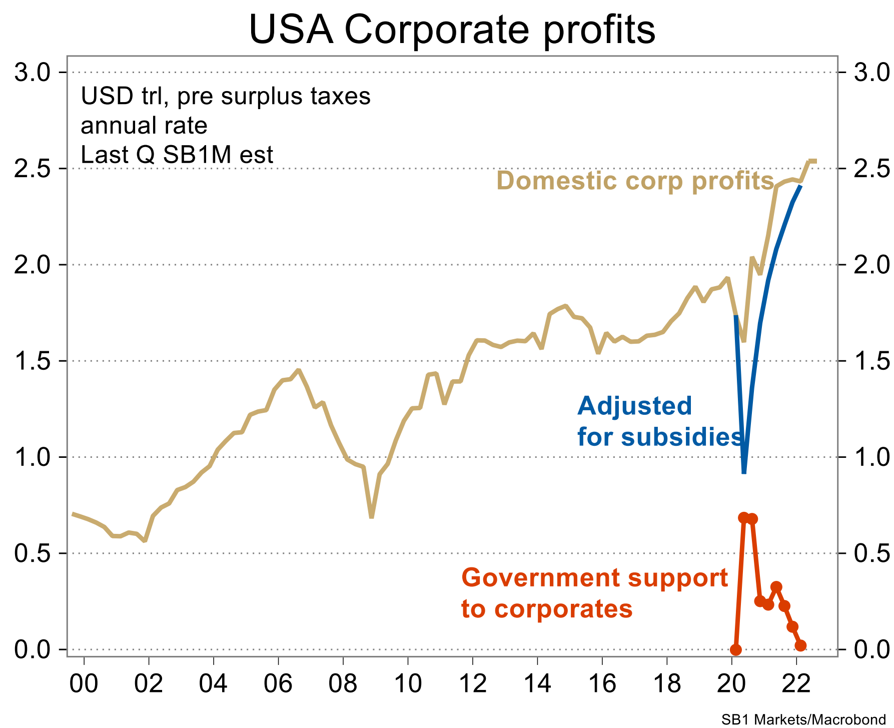


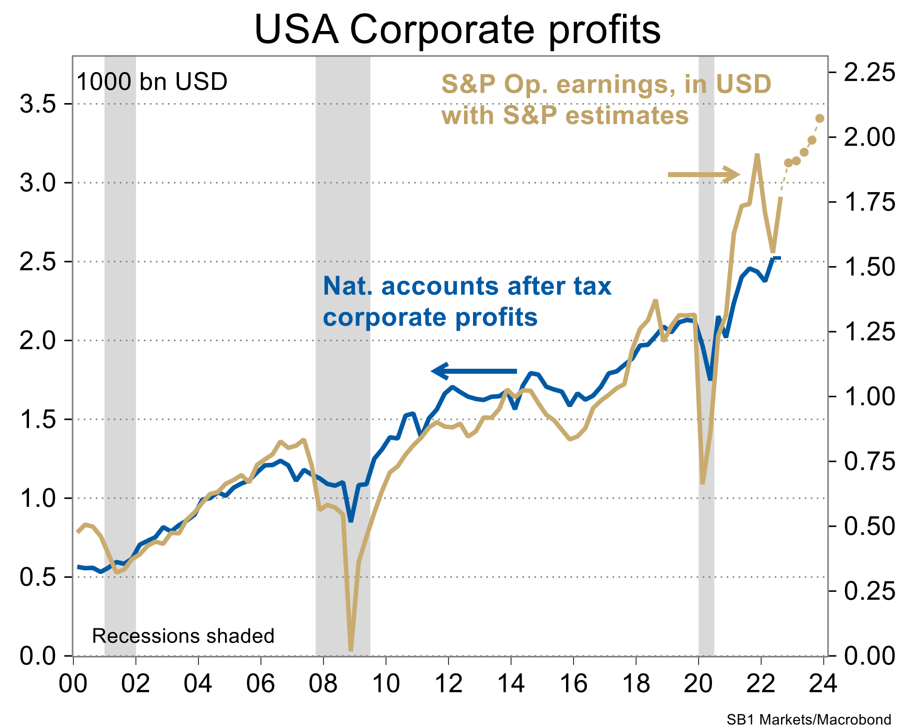


- Net trade has declined more than normal vs. the increase in domestic demand but has now turned up – and may have further to go
- *Check more on the household sector some few pages forward*

Corporates' profits flattened in Q3?

Some data are still missing but wage costs probably grew faster than value added

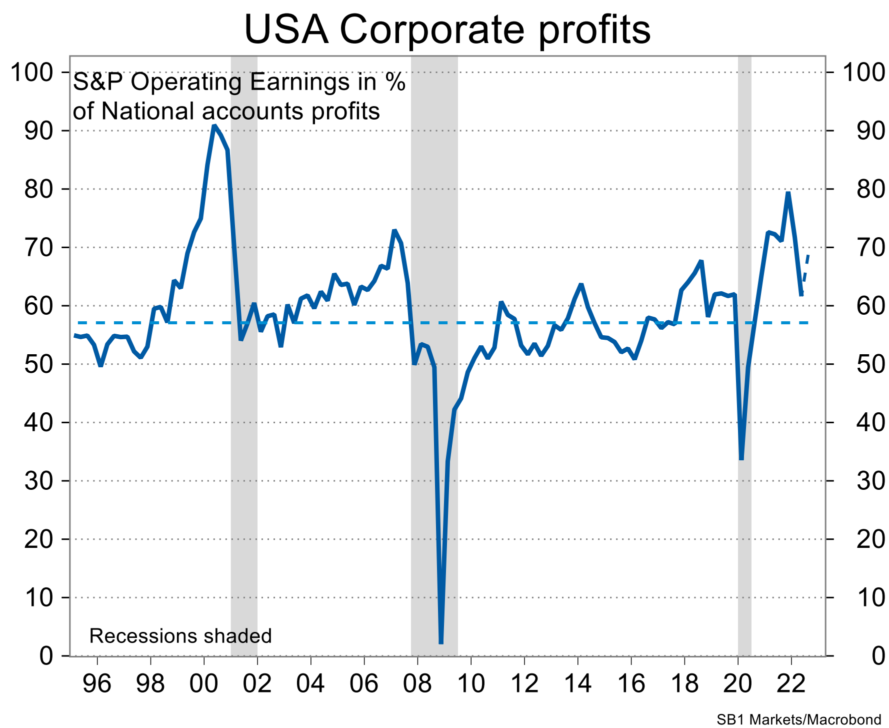


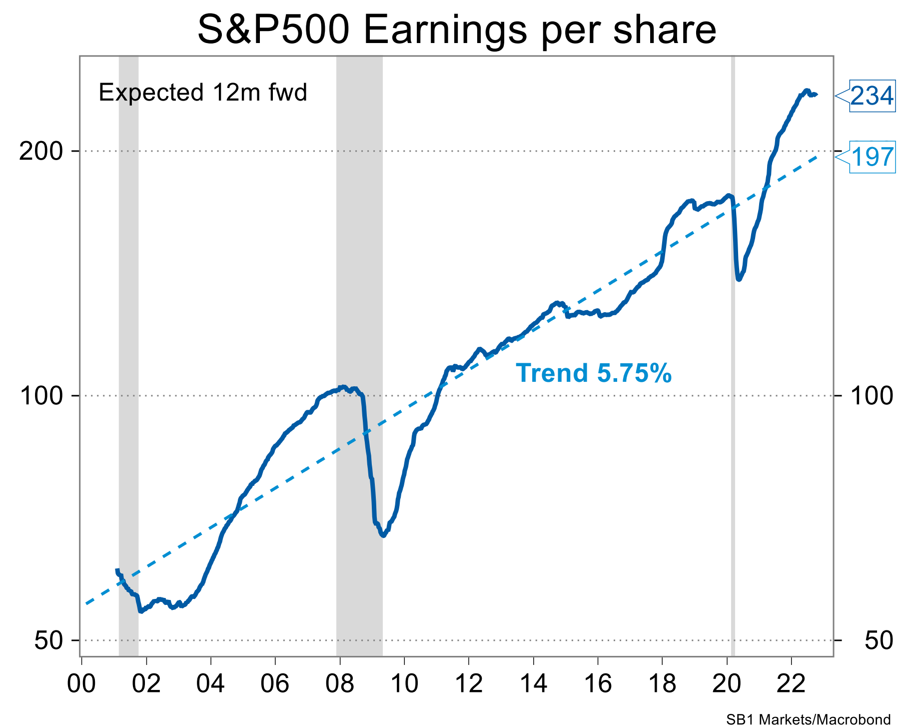


- **We assume domestic corporate profits** was unch. in Q3. Growth in nominal corporate GDP slowed (we assume to 1.5%, but the estimate is uncertain!), and that total compensation of employees rose by 1.8%, the highest since Q4 last year. Net tax payments/subsidies have normalised, no more 'covid support'
- The **S&P** estimates that S&P 500 profits rose by some 14% (q/q, and up just 3% y/y) in Q3 following the more than 10% decline in Q1 (seasonally adjusted). S&P profits (including profits from abroad, measured in a strong USD!) are still way above normal vs National Account profits for the total corporate sector (including all corporates operating in the US, domestically or foreign owned). Thus, a downside risk for S&P 500 earnings? (S&P's forecast is usually far to optimistic, at this time a quarter ago, they expected 2% growth in Q2 operating earnings. Now, it turns out they fell by 7%)
- We think the **profit outlook** is bleak. Wage inflation will not subside immediately given the super tight labour market – and a continued price inflation at the current pace does not seem to be tolerated anymore by the Federal Reserve. Exciting times ahead

Profits in the National accounts are still strong. S&P profits are even better

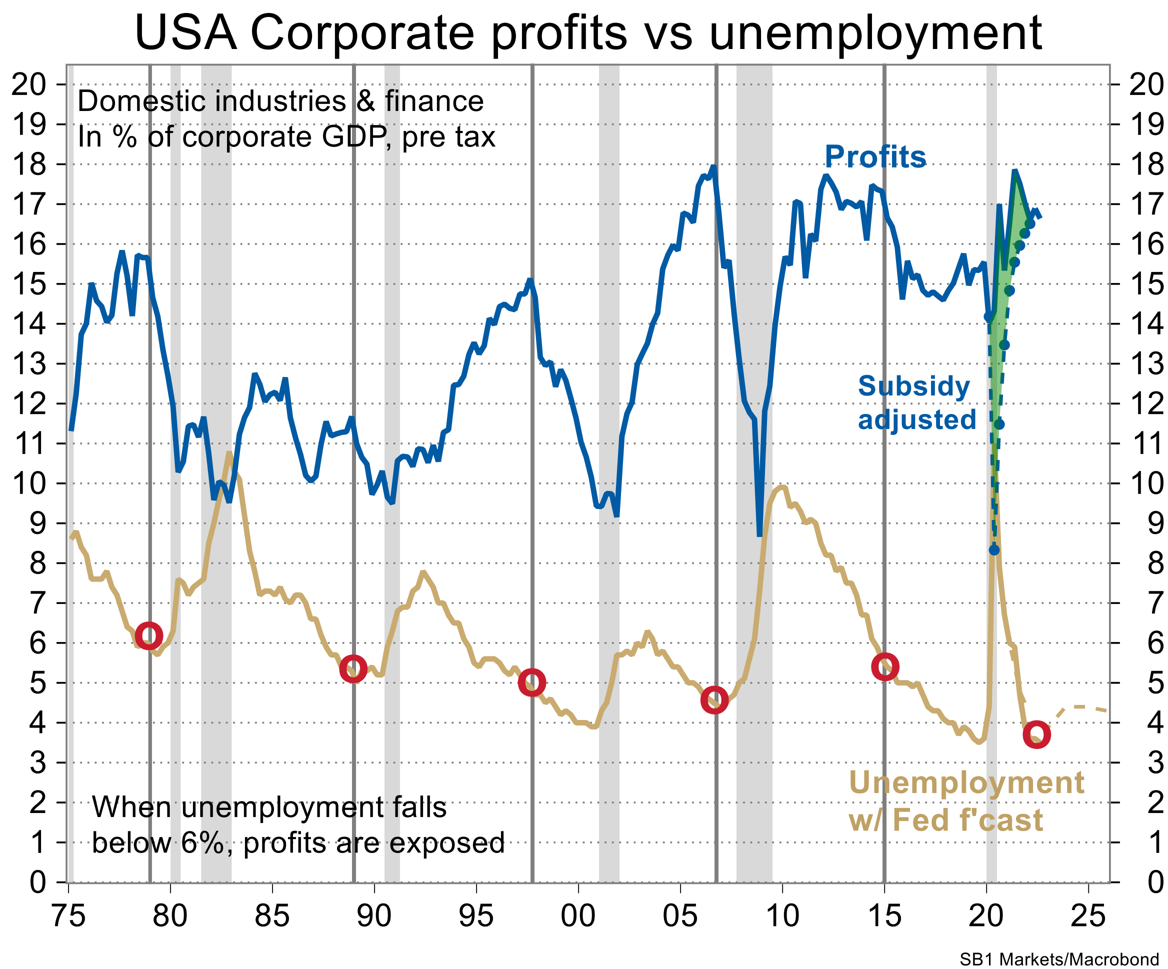
Until further notice (and expectations have now turned down)





The profit cycle has peaked. Now, make ready for the next leg

The bottom line has always been hurt when the labour market becomes too tight. Like it is now

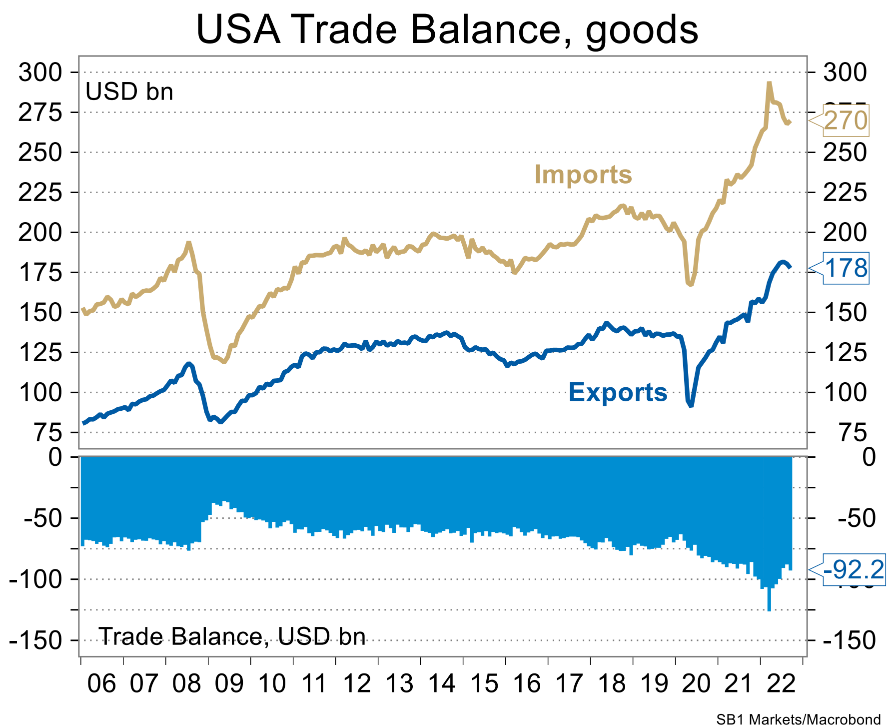


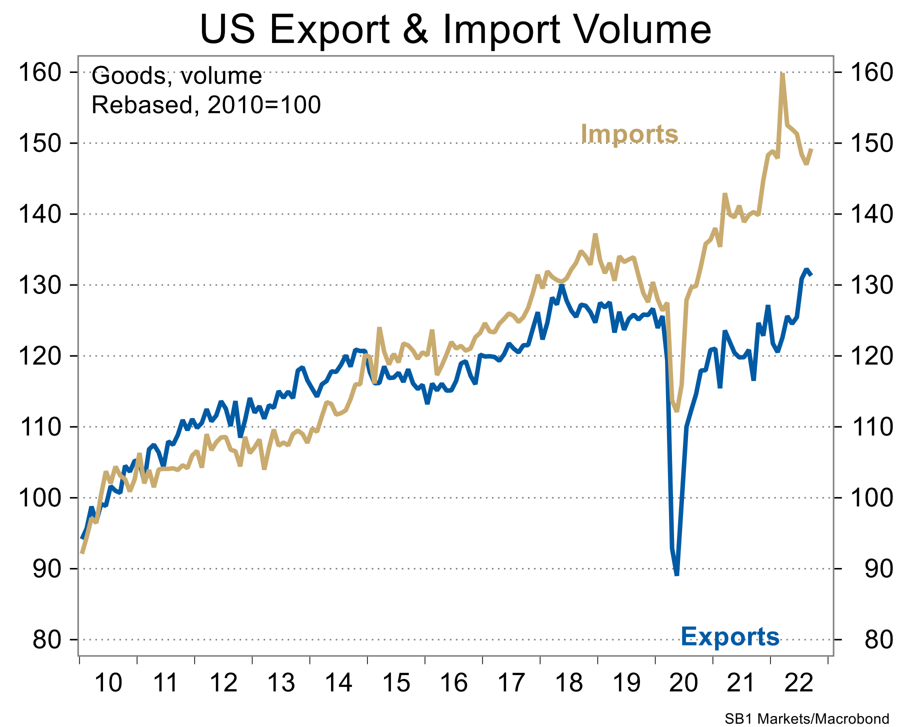
- Prices are increasing at an incredible pace but so are wage costs, and government support is on the way down
- When **unemployment** falls below 5% – 6% companies have normally been struggling to keep their share of value added – as their employees are getting the upper hand
  - » Unemployment is now at 3.6%, and it is falling rapidly as other indicators (especially vacancies) suggest that the labour market is even tighter than the 3.5% rate signals
- In addition, it is reasonable to expect the production taxes-subsidies to normalise the coming quarters.
  - » The impact is shown as the green area on the chart above
- <u>Thus, it is quite likely that the profit share is headed downwards from here</u>

All data are not yet published, and the Q1 numbers are just our estimate

The trade deficit a tad larger than expected in Sept, still a huge drop in Q3

The trade deficit in goods widened by USD 5 bn to 92 bn in Sept, expected unchanged

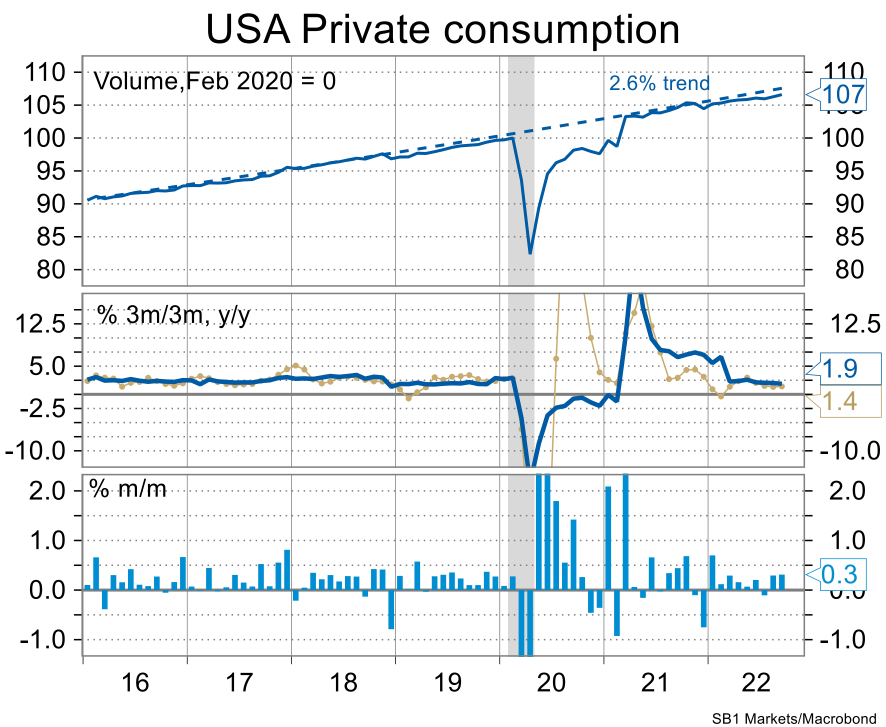


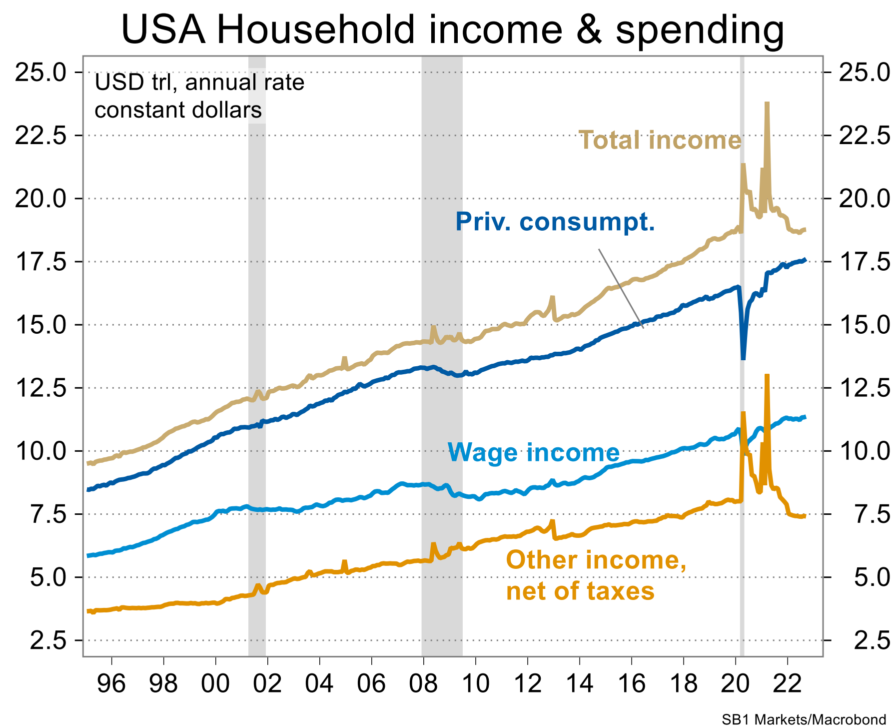


- In Sept, exports fell, and imports rose, both marginally. The trends are the opposite:
- Imports are declining rapidly, from a very high level
- Growth in exports has been rather impressive, even in volume terms. Export volumes are up some 5% from before the pandemic. Imports have fallen sharply from the March peak, by 8% - but imports are still up 15% from early 2020. The slowdown in import volumes is due to weaker domestic demand, and a decline in stock-building (in the GDP report)

Consumption is ~~flattening~~ trending upwards

Consumption grew 0.3% in Sept, 0.1 pp more than expected, and Aug revised up 0.2 pp to 0.3%

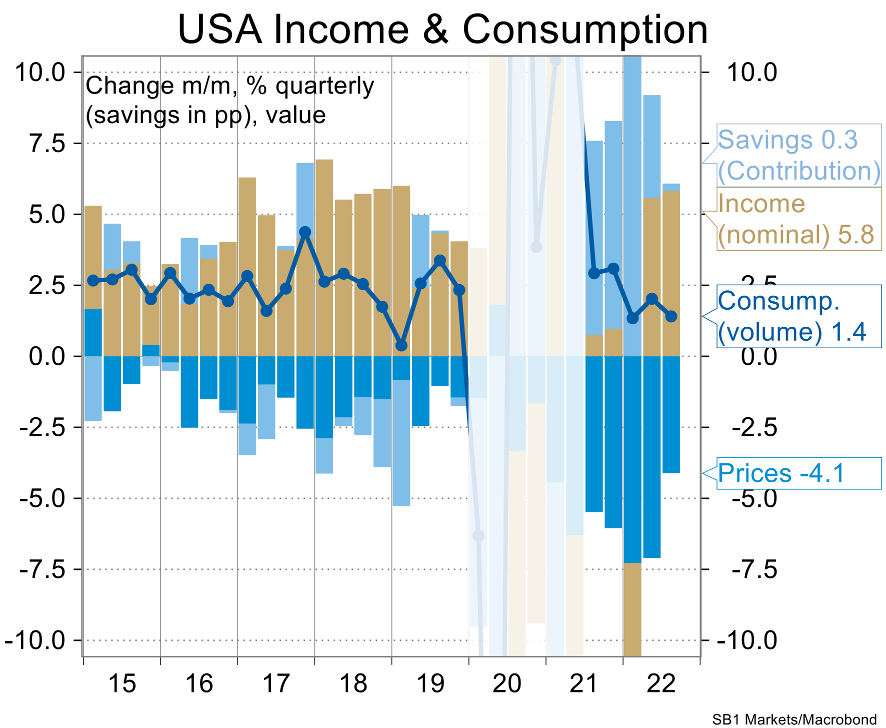


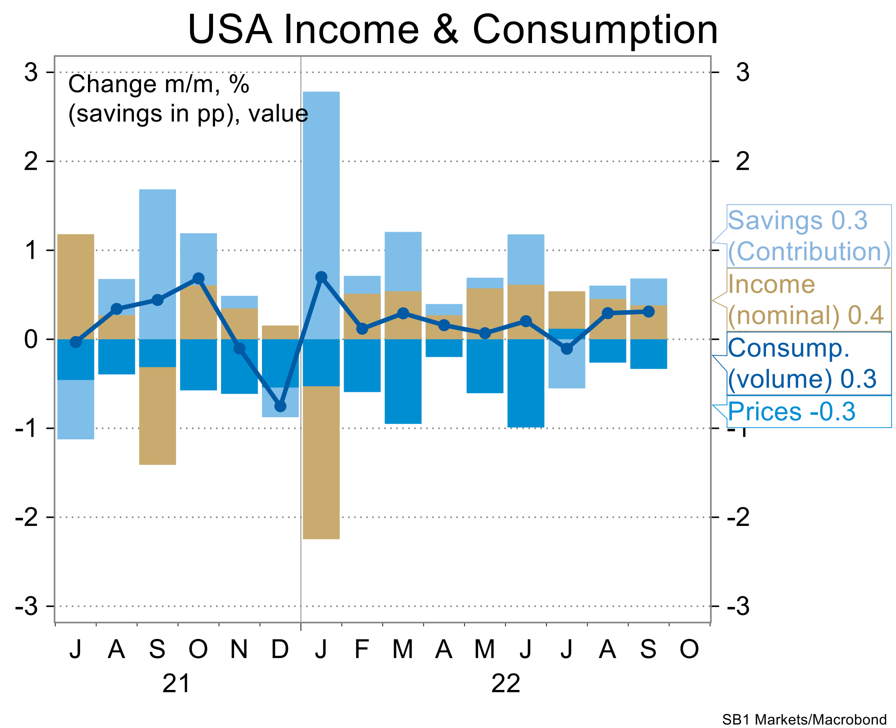


- **Private consumption** hade almost flattened, but August and September saved Q3, and demand is heading upwards into Q4. Personal spending rose 0.6% nominally, expected 0.4%
- **Personal nominal disposable income** gained 0.4% in Sept, and was up by 0.1% in real terms. Real disposable income has flattened but rose slightly in September.
- **The savings rate** was fell 0.3 pp to 3.1%, and is now more than 4% below the pre-pandemic level. However, even if the accumulated extraordinary savings through the pandemic is now run down, most of the Wall of Money is still intact which may make it possible for households to keep up the level of spending (at least for those who saved…)

Price inflation slowed in Q3 but was still high at 4.1%, income grew 5.8%

… and funded most of the 1.4% volume growth in consumption – the savings rate contributed 0.3 pp

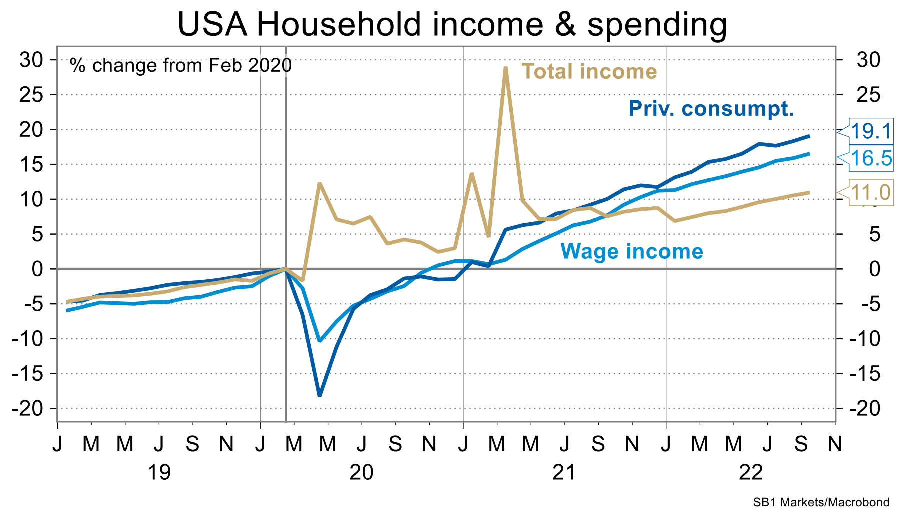


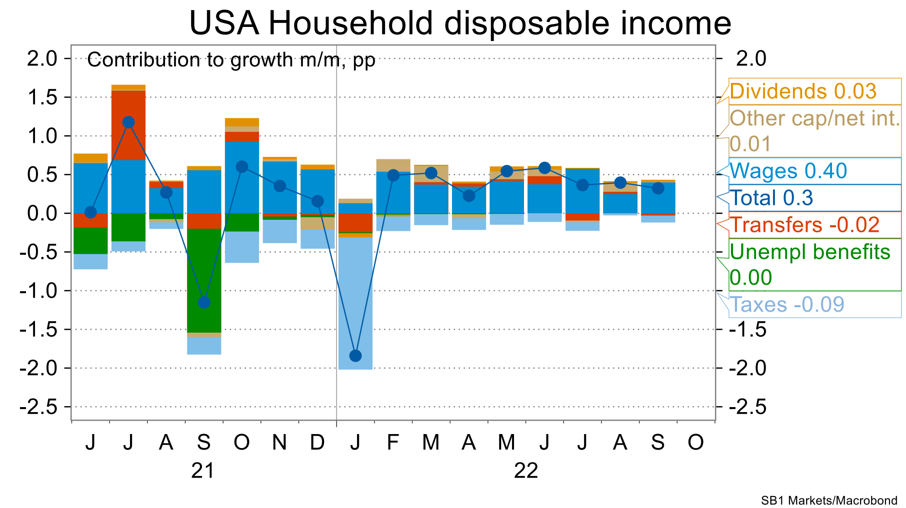


We have shaded the ‘hard’ pandemic quarters at the chart to the left

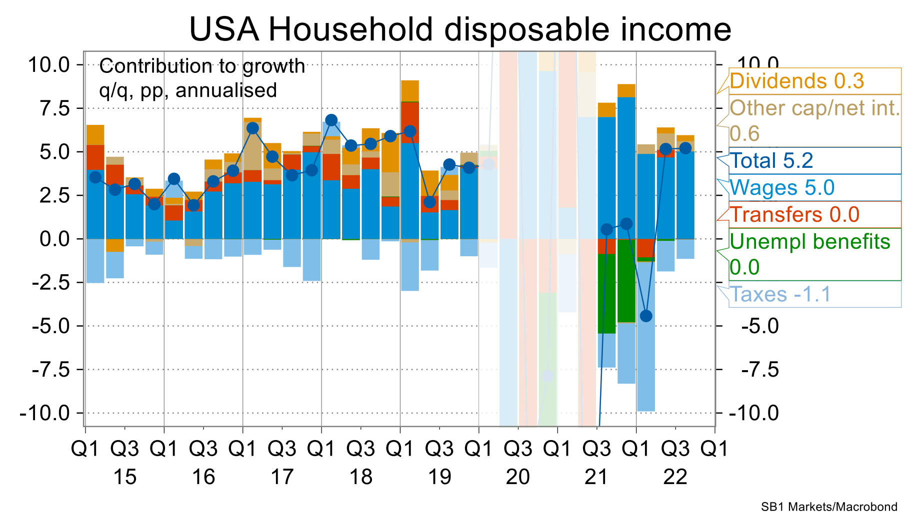
Income growth still higher than normal, nominally – by some 0.4% per month

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





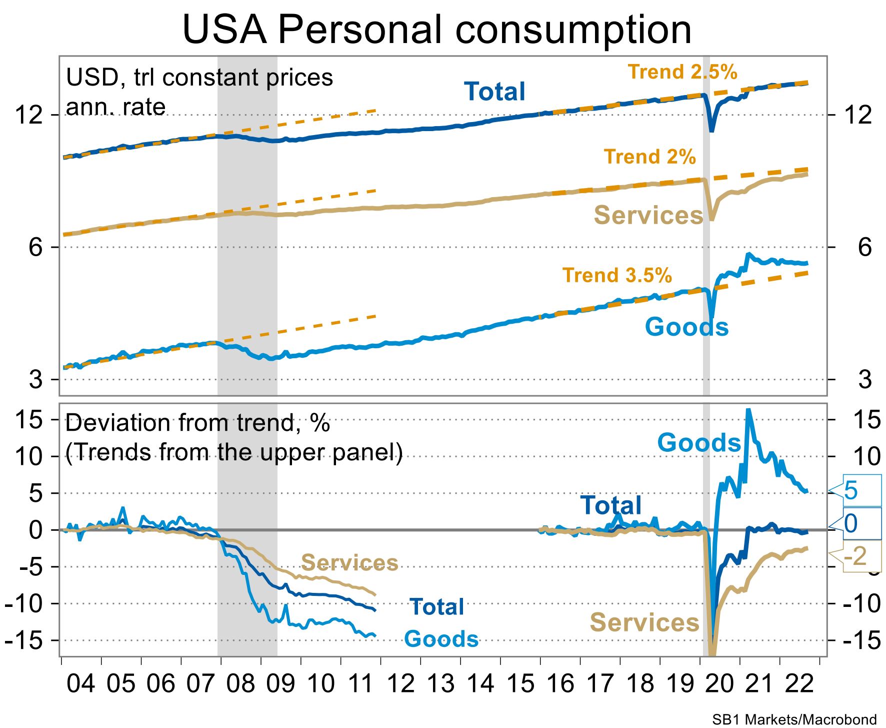
- **Total household disposable income** flattened from the spring in 2021 to early 2022 but has been trending steady upwards since January. Household income fell in Q1 due to higher tax payments but rose sharply again in Q2
- **Total wage income** is growing rapidly and the level is far above the pre-pandemic growth path at 4.25% (now at 7% – 8%). The reason is of course the sharp increase in wage inflation. Wage growth was revised somewhat down in the annual revision

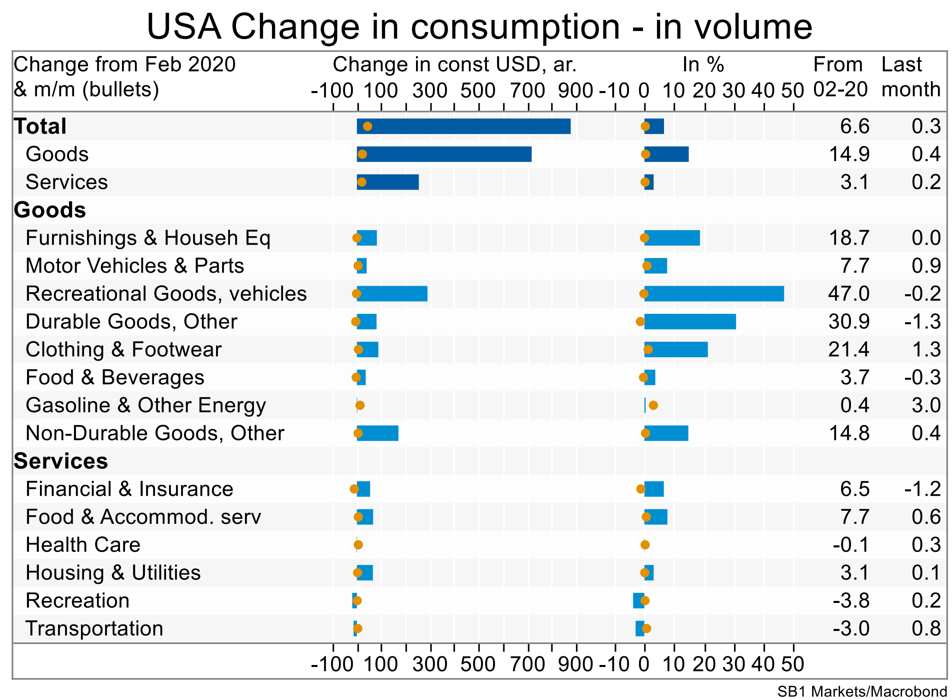


We have shaded the 'hard' pandemic quarters at the lower right chart, as these data make no sense now

Services are 3.1% above the pre-pandemic level; Goods are 14.9% above

Spending on services is still 2% below the pre-pandemic trend, spending on goods is 5% above!



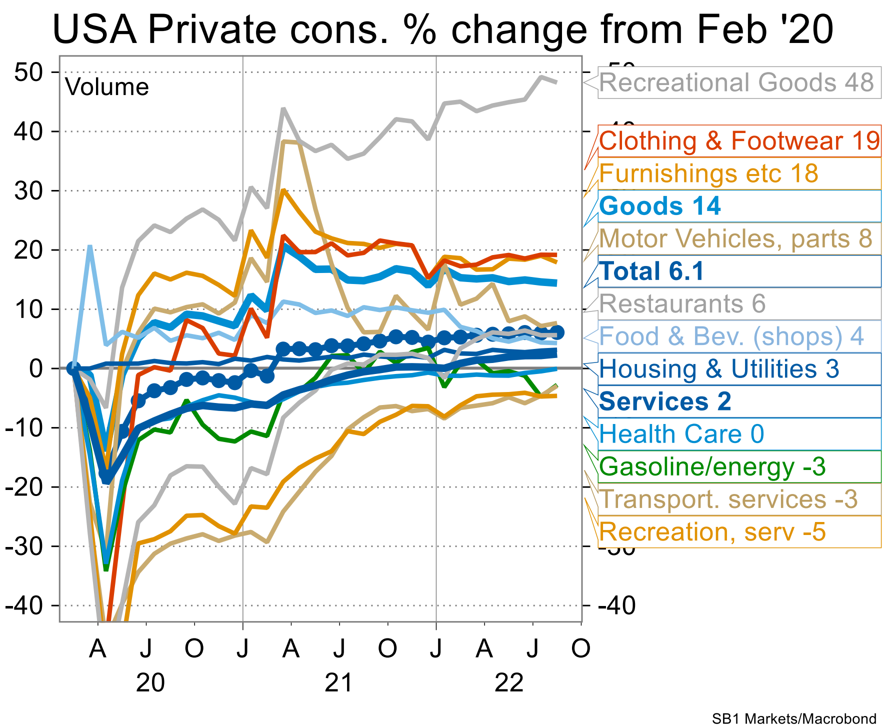


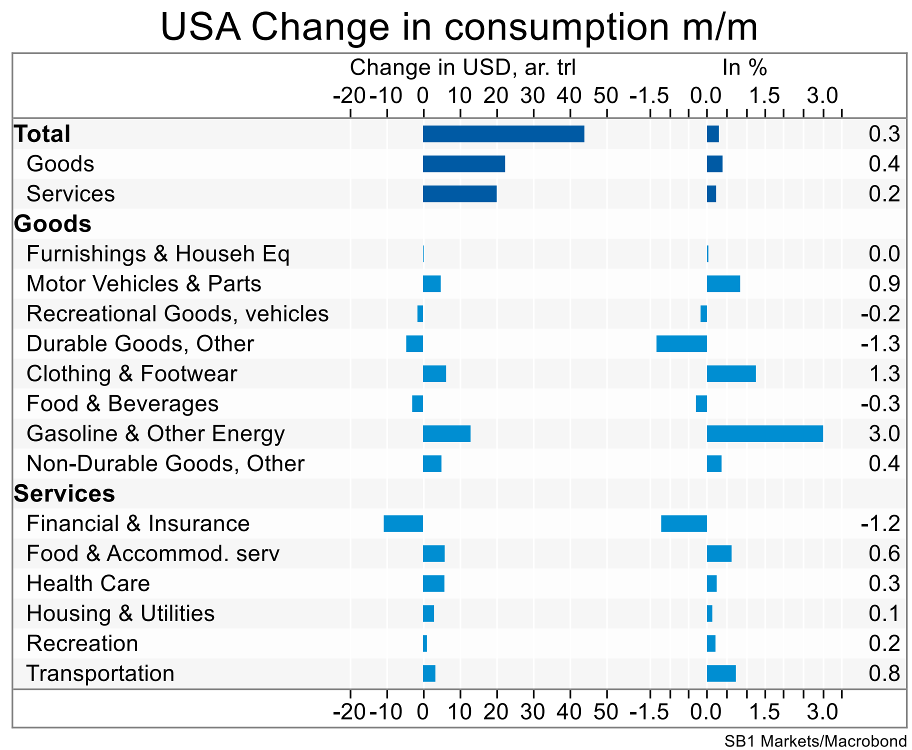
- Both consumption of goods and even more service consumption was revised up in the annual GDP revision

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

Mixed September consumption data, goods more up than services, in value terms

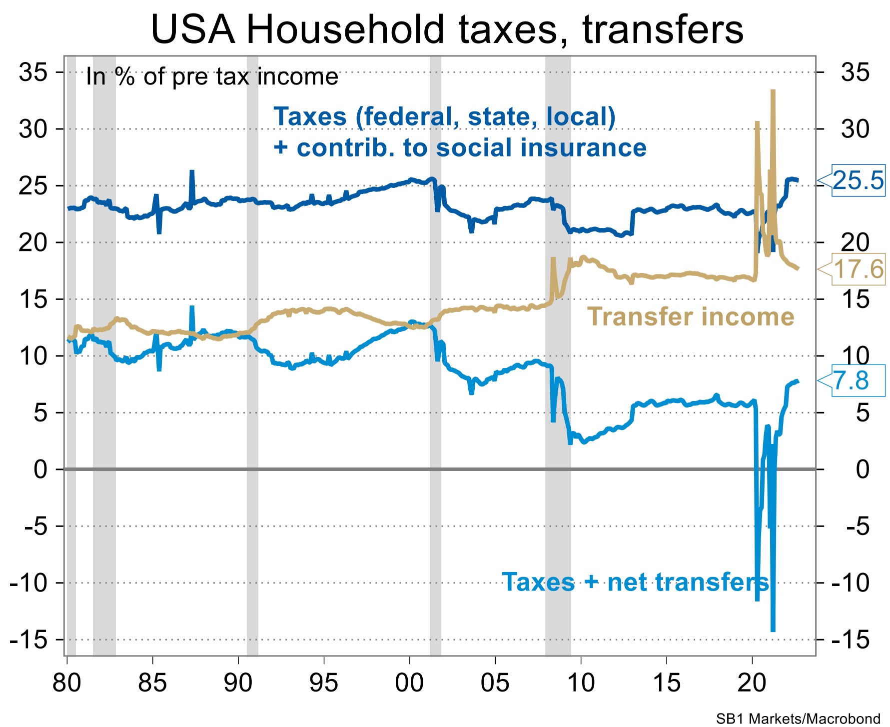
… mostly due to a lift in gasoline/energy prices

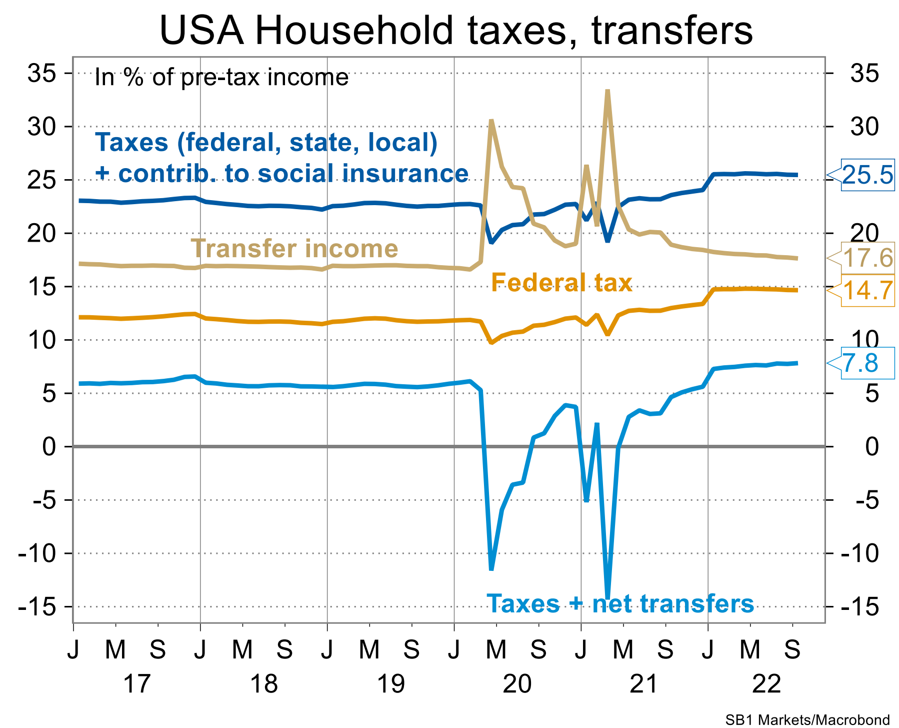




Households contribute more to the Federal coffers than before the pandemic!

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

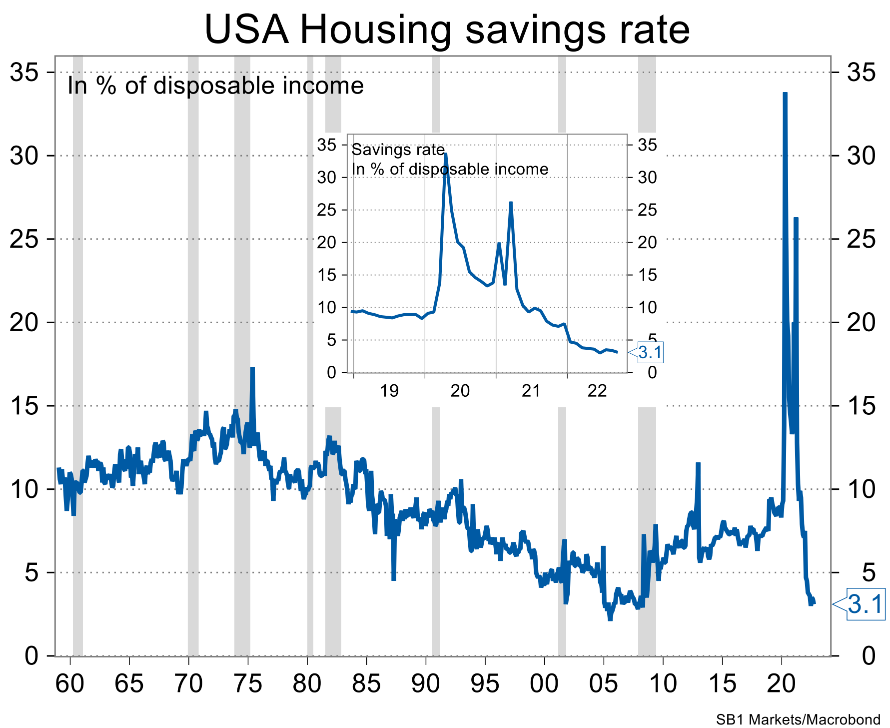


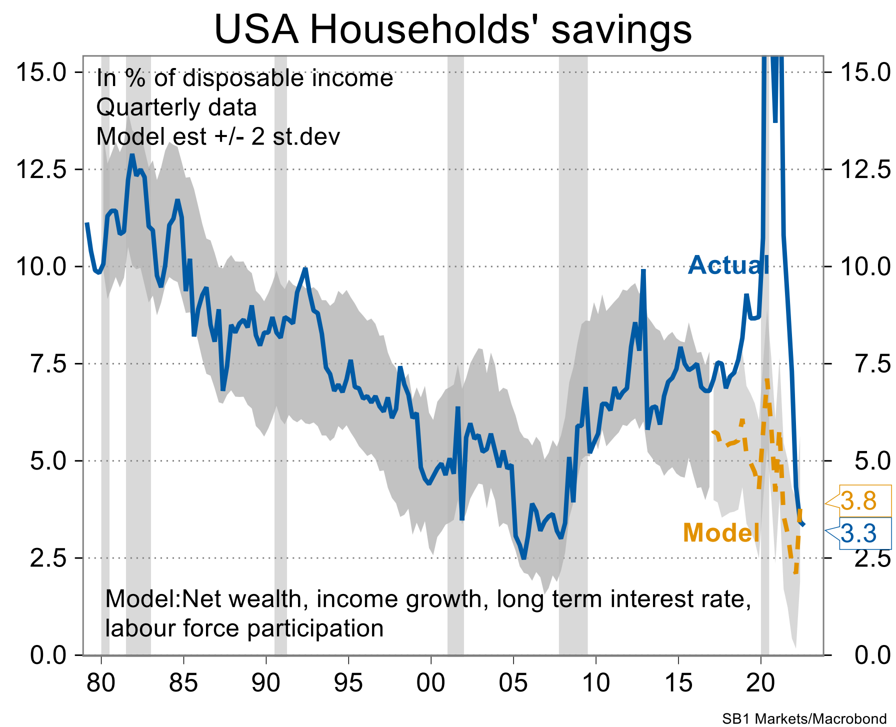


- Transfers are trending down but are still higher than before the pandemic (vs total pre-tax income). However, the total tax rate is climbing faster. The total gross federal income tax rate at 25.5% of pre-tax disposable income is equal to the ATH in 2001!
- Thus, the net tax rate is on the way up, and has recovered to 7.8%, above the 6% pre-pandemic level – but far below the 10% – 12% from before year 2000 – as the transfer rate is at 18%, up from below 15% from before the Financial Crisis

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

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

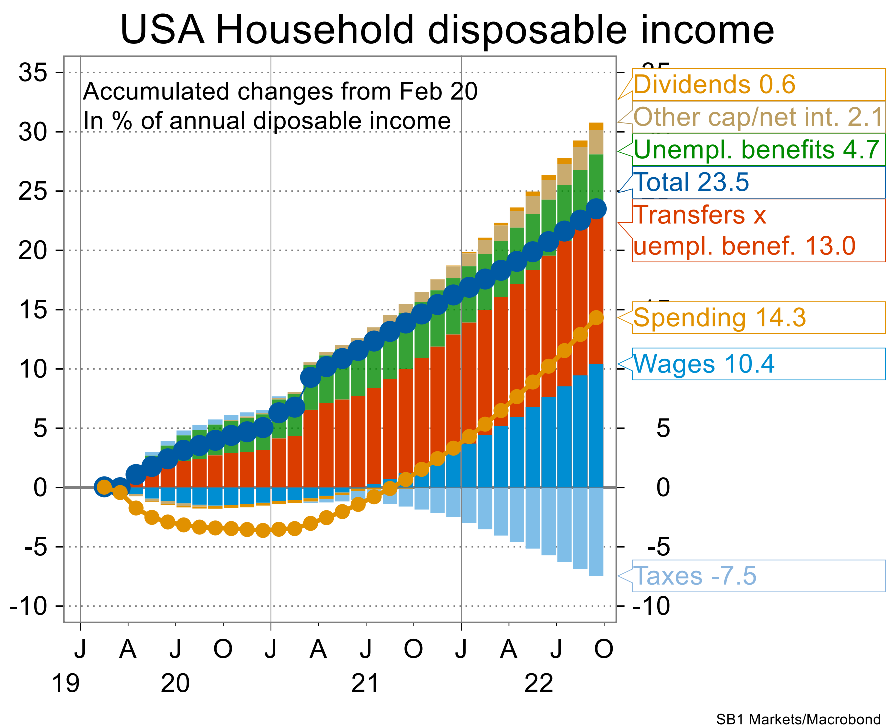


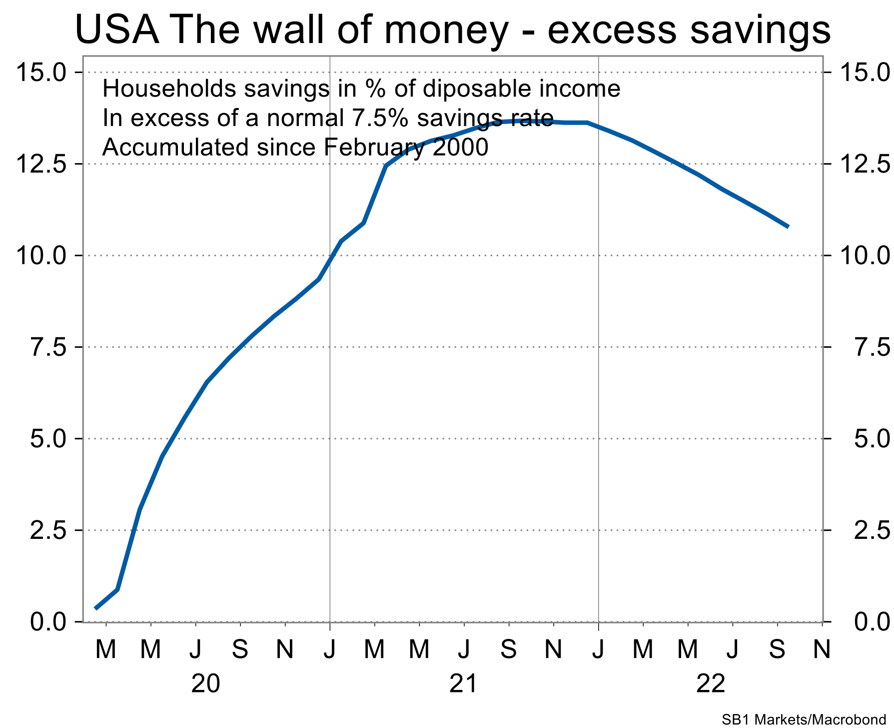


- The **savings rate** was 3.1% in Sept, down 0.3 pp from an 0.1 pp downward revised August 3.4% level
- Households are now dipping into 'normal' savings in order to keep up consumption, as their real incomes are not keeping up, due to the high rate of inflation. The savings rate is now more than 4 pp lower than before the pandemic
  - » However, household have saved much more than normal during the pandemic, equalling to some 13% of disposable income – on average for all households, that is. This 'Wall of Money' is now shrinking at a 4.4 pp pace per year, if the savings rate stabilises at 3.1%
- Our old savings model, yielded an estimated 3.8% savings rate in Q2. During the 2016 – 2019 period our model has underestimated the savings rate systematically by some 2 pp, but the gap was closed in Q2

The Wall of Money is coming down faster than previously assumed

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

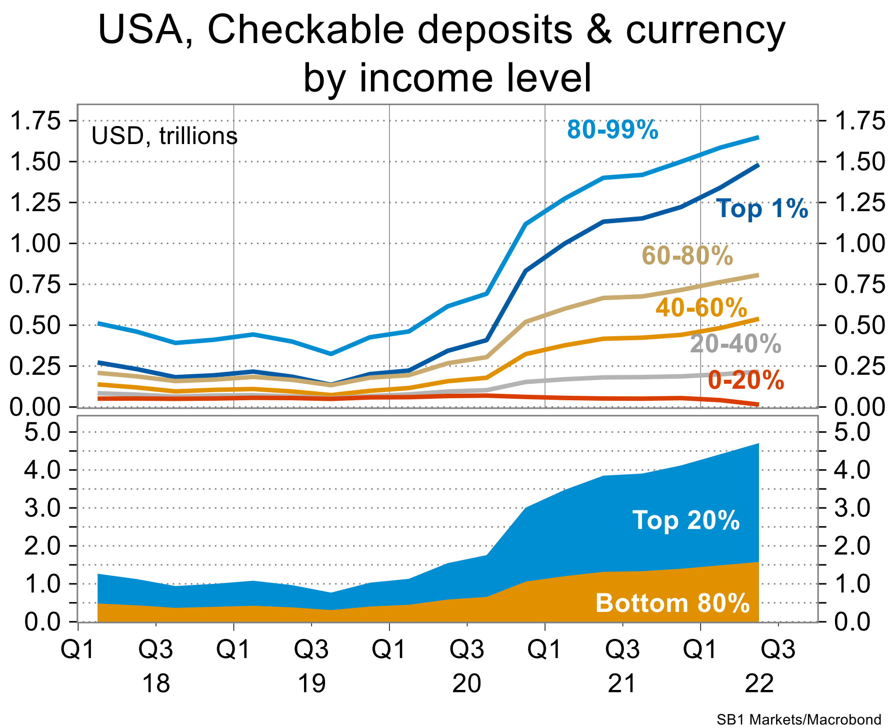




- Transfers from the government and low spending (on services) explained the lift in savings - but now spending is coming back, and the savings rate is now lower than before the pandemic

Most of the accumulated savings reside with the top 20%

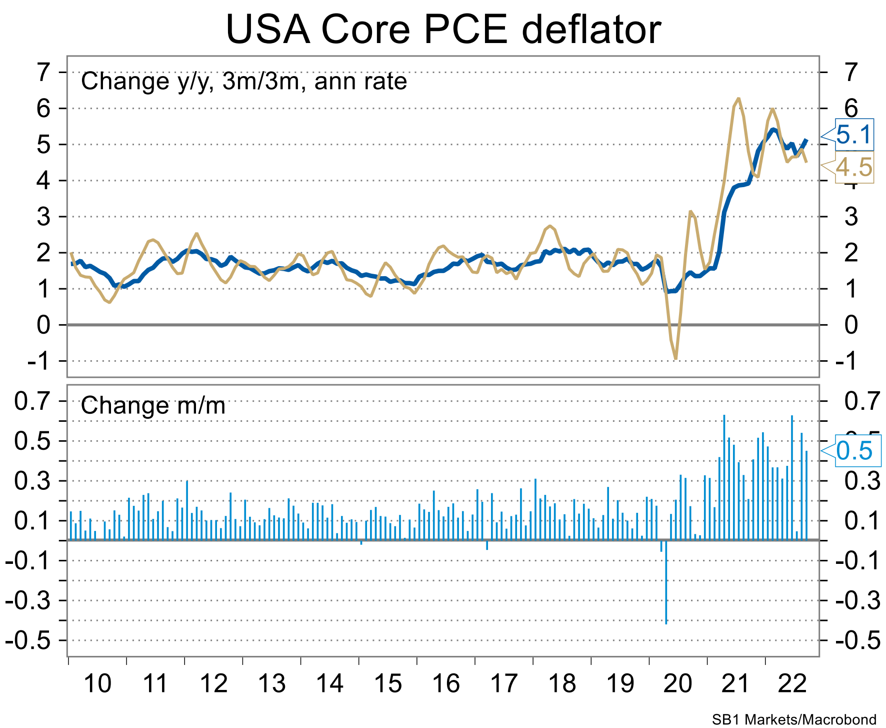
Those at the bottom of the income ladder did not save much more during the pandemic

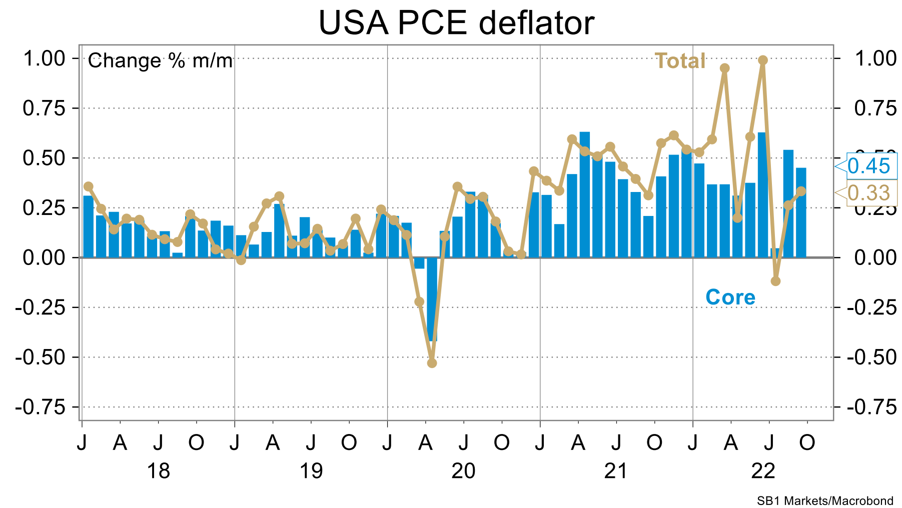


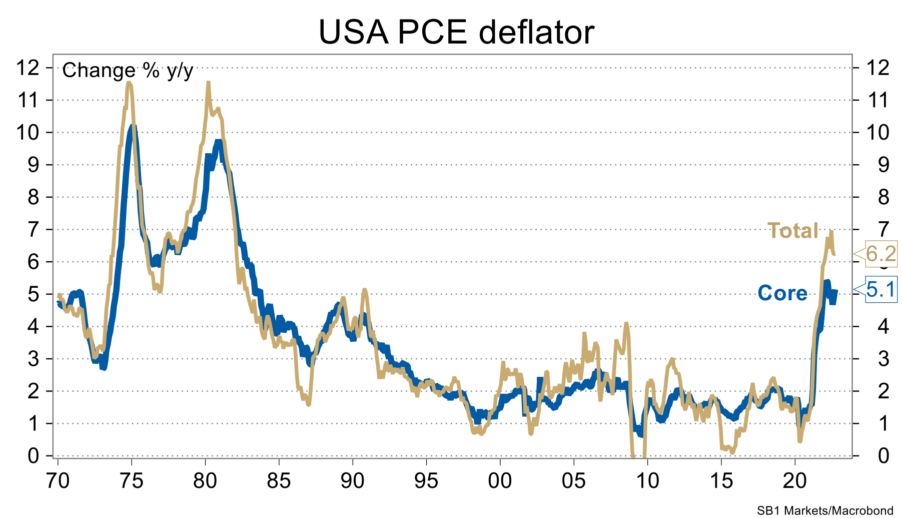
- This will of course determine where the money will be spent and if at all, due to the wealth effect and because these groups do necessarily have to spend these savings to keep up consumption

Core inflation up in line with expectations in September; August data revised down

The core PCE deflator rose by 0.5%, in line with expectations. The annual rate is now at 5.1%



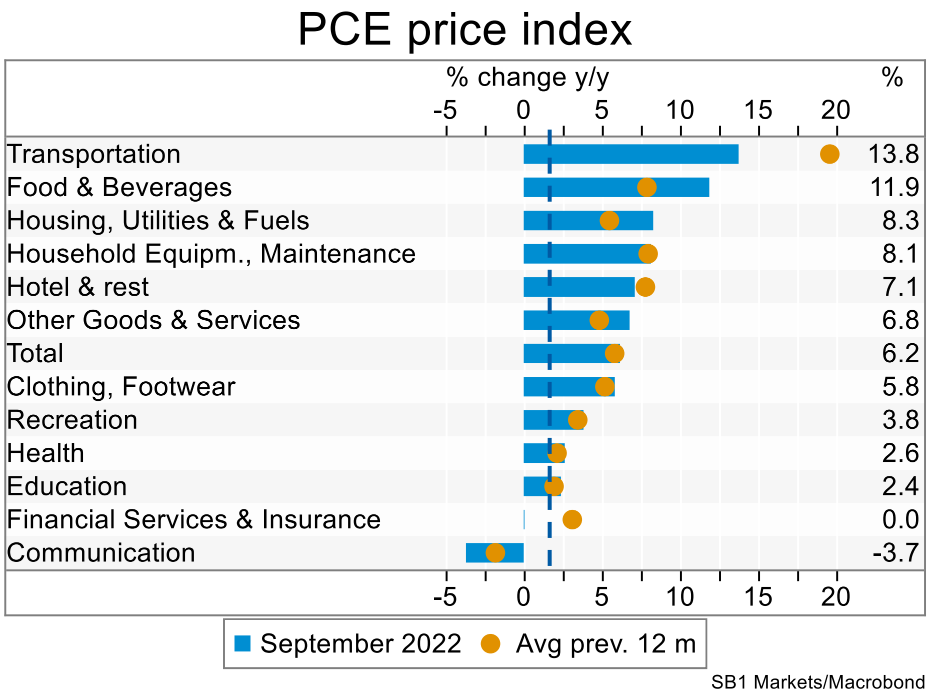


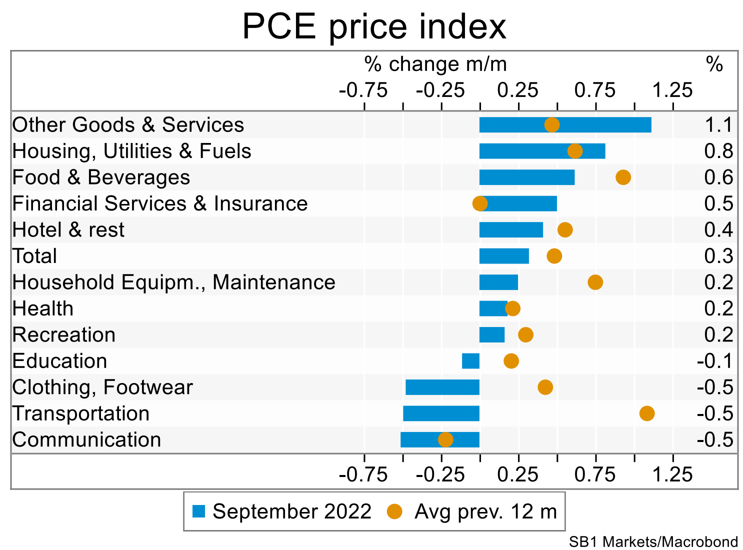


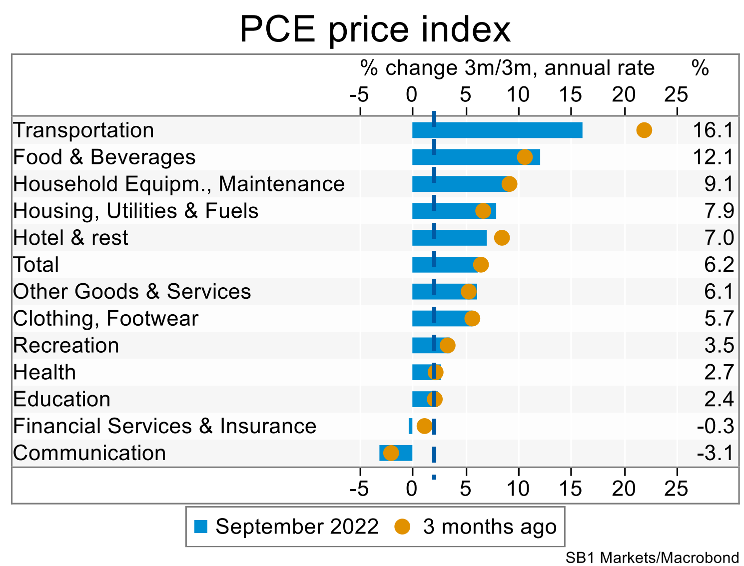
- **The core PCE** August print was revised down by 0.1 pp to 0.5%, and in September prices rose by 0.451%, thus close to 0.4%, down from 0.6% in August. The annual rate was at 5.1%, up from 4.9% in August, and 0.1 pp lower than expected. The annual rate peaked at 5.4% in February
- **The total PCE deflator** was up 0.3% in September, as expected. The annual rate at 6.2% was 0.1 pp lower than expected. The peak was at 7.0% in June

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

... and all but 2 are up more than 2% measured 3m/3m, the total is up 6.2%

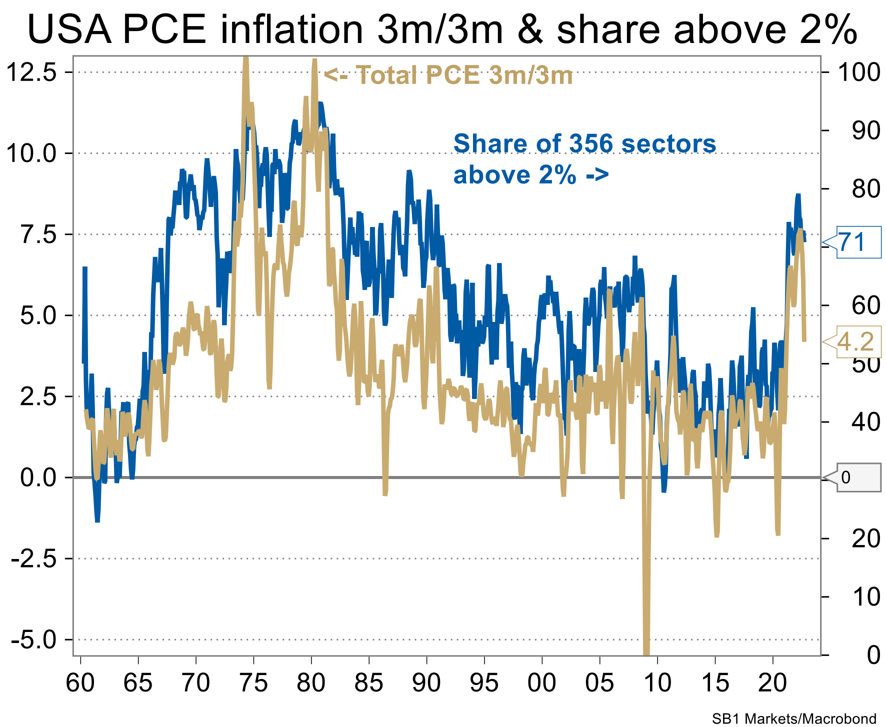


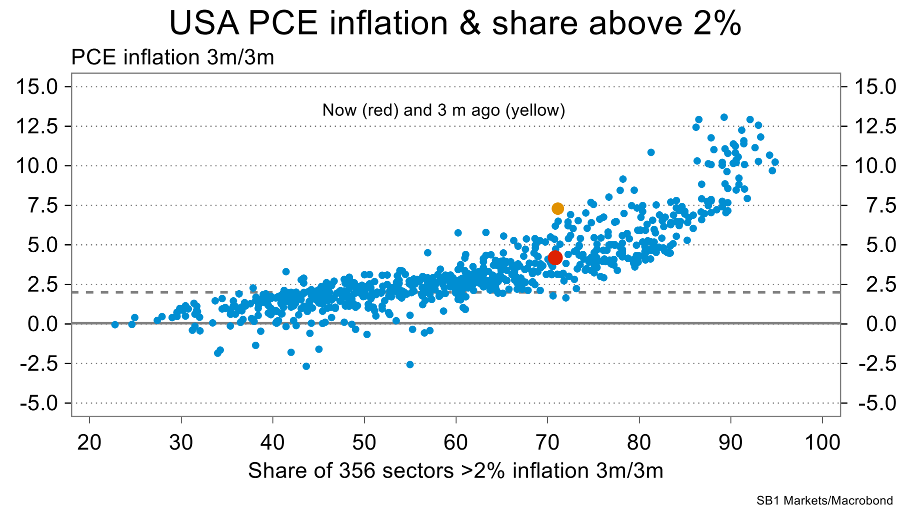


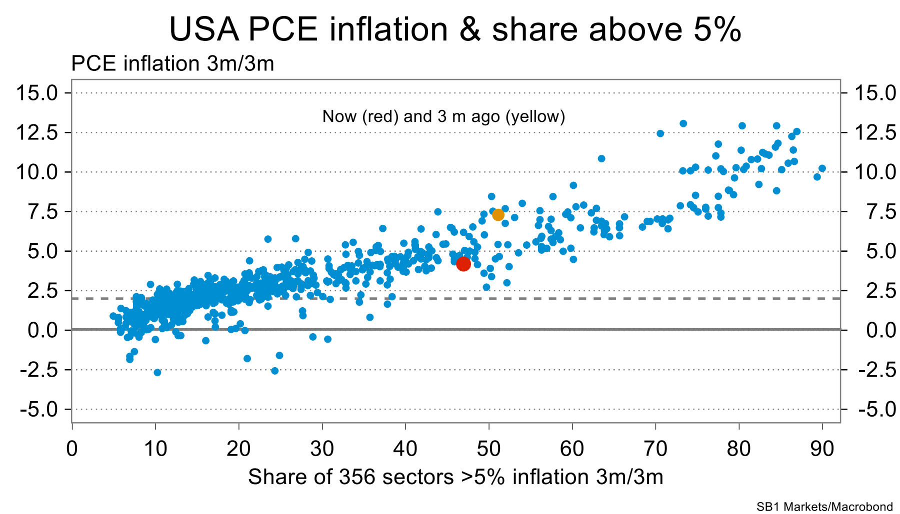


- Still, the momentum has slowed marginally, as some sectors report slower underlying (like 3m/3m) growth. However, just as many sectors report faster growth
- Transportation, clothing, and communication prices fell in September
- All in all, inflation is still far too high and it is broad

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

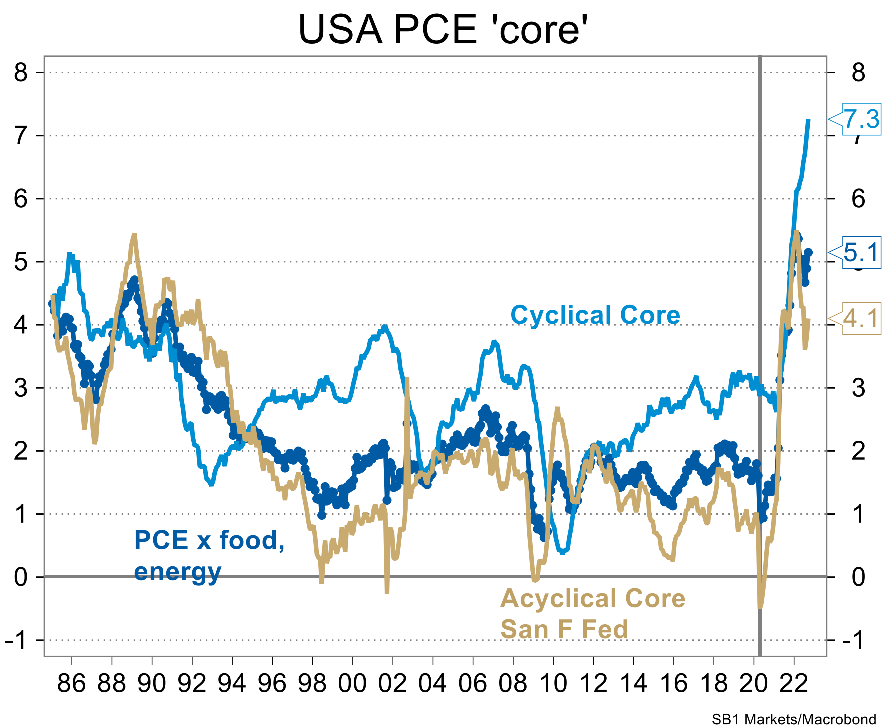


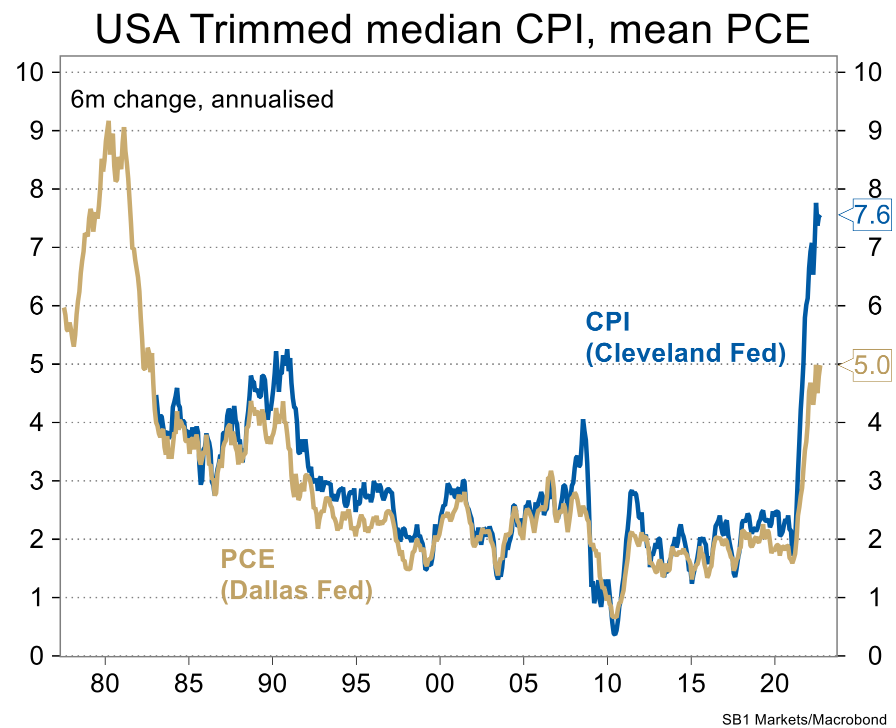




Inflation has peaked but all underlying/breadth measures remain very high

Wages are more important, anyway

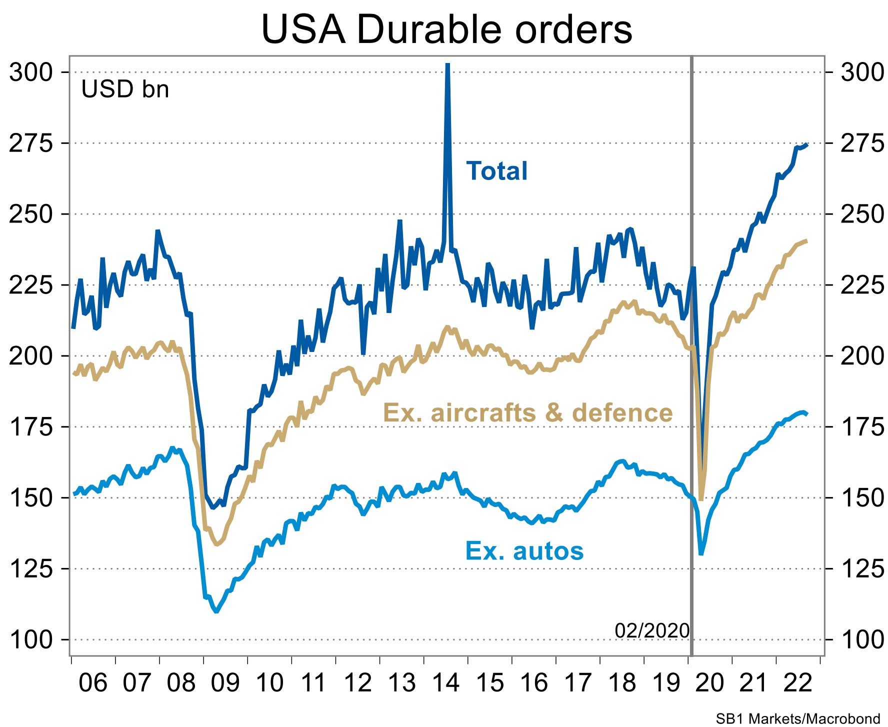


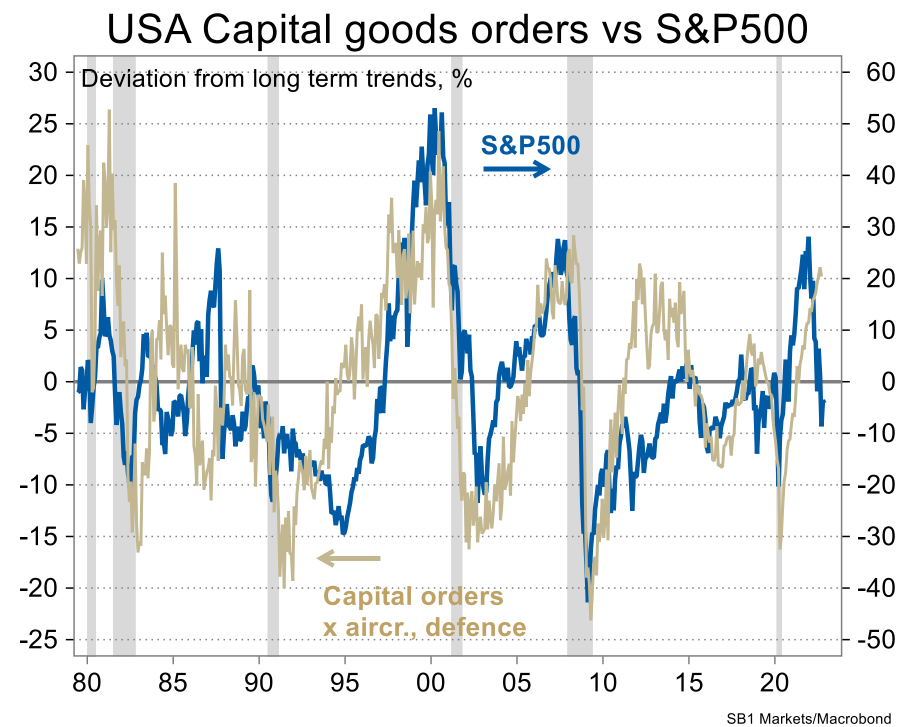


- The **trimmed PCE mean** (Dallas Fed) accelerated 0.2 pp to 5.0% (measured over the past 6 months), back up the to the peak level (since 1983) first reached June. This is very likely among the most important price indicators for the FOMC, if not the most important
- **The trimmed median CPI (Cleveland Fed)** is up 7.6% over 6 months
- **Core cyclical and acyclical PCE** prices are up 7.0% – 3.8% resp., and the cyclicals are still on the way up
- Other measures of underlying inflation are also still among the highest levels in 30 – 40 years

Growth in orders slows but still far better than 'all' business surveys signal

Strong defence, aircraft and auto imports support overall order growth

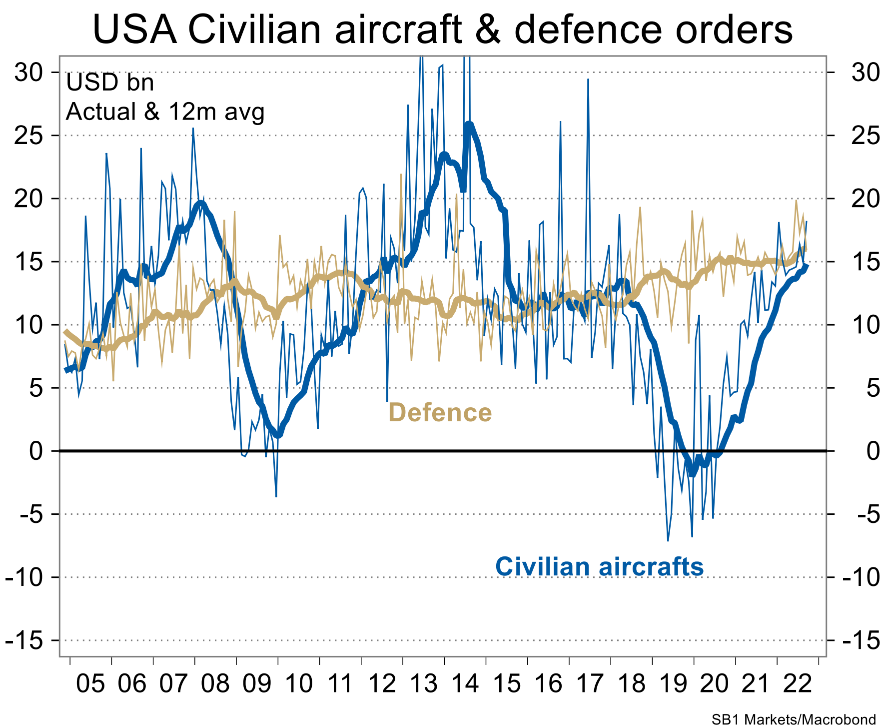


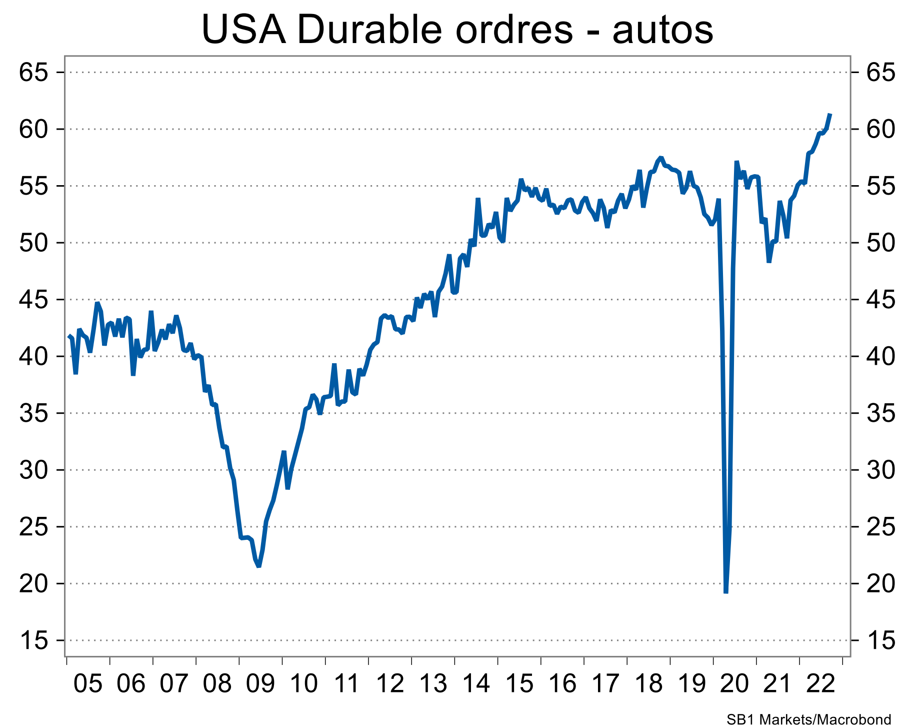


- **Total durable** orders gained 0.4% in September, expected up 0.6%
- The volatile aircraft & defence orders rose sharply, and **other orders** (our core concept) were up 'just' 0.2%. Growth has slowed, but orders are still up almost 5% 3m/3m, although in nominal terms
- **Core investment goods orders** fell 0.8%, expected up. Underlying growth has clearly slowed, an August may have been the peak
- **Order inflow** is far above pre-pandemic levels, especially for investment good orders, but surveys now signal a significant decline the coming months (which they have indicated since June, so far without any success)
- The stock market has taken a serious beating, this time well before the order cycle turned south. Higher real interest rate were probably enough

Aircraft & defence orders at ~~normal~~ higher levels than normal

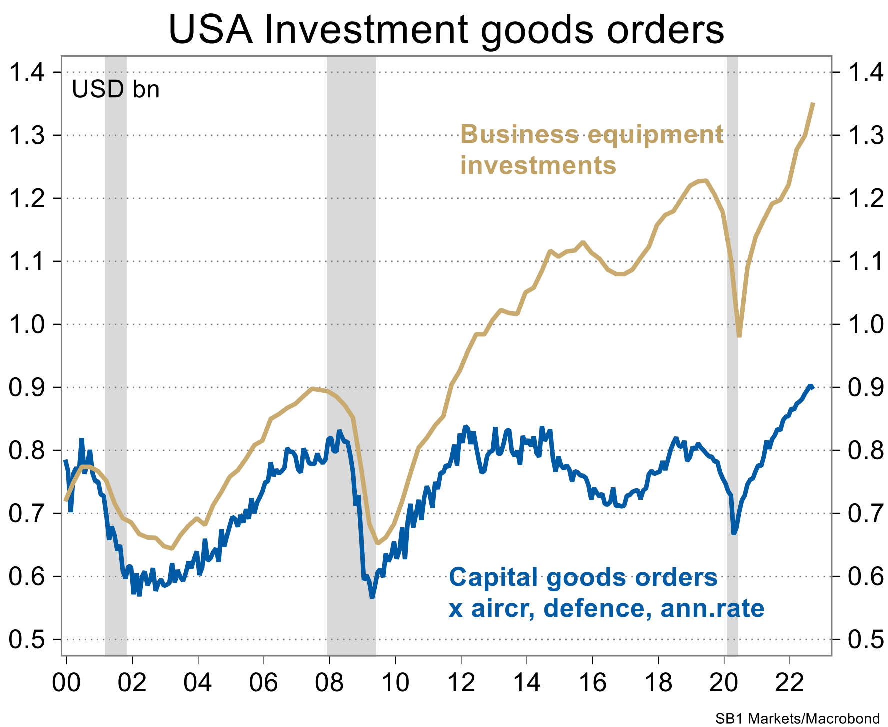
… while auto orders rose in further in September – to another ATH, at least in nominal terms

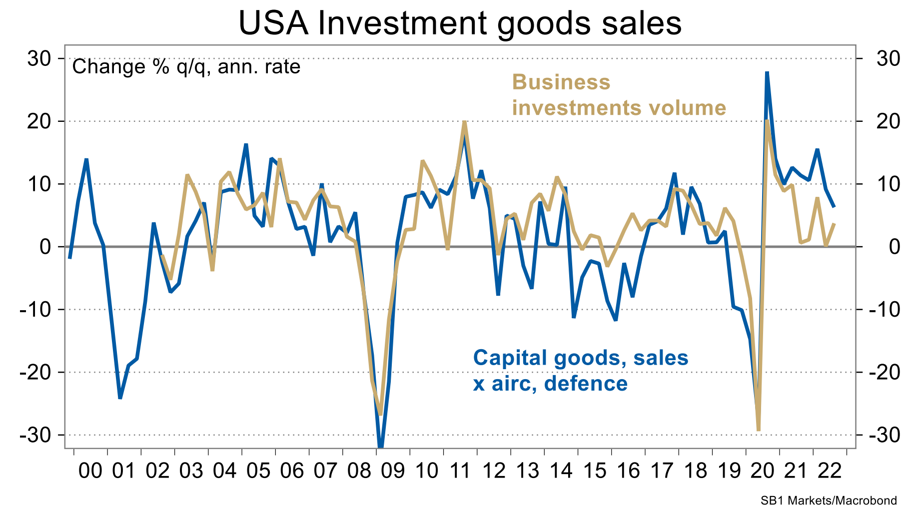


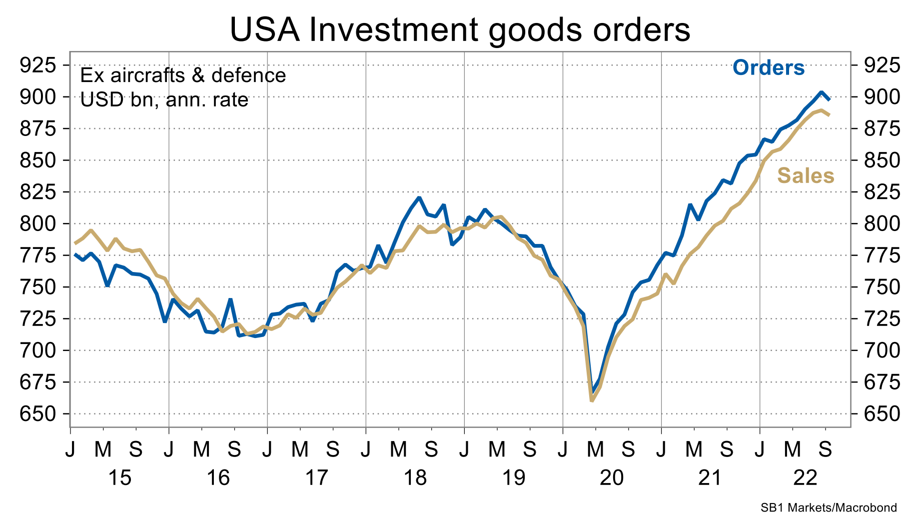


Core capital orders are peaking? One month is not a new trend but still…

There is still a decent underlying growth, at least in nominal terms. Investment growth has slowed



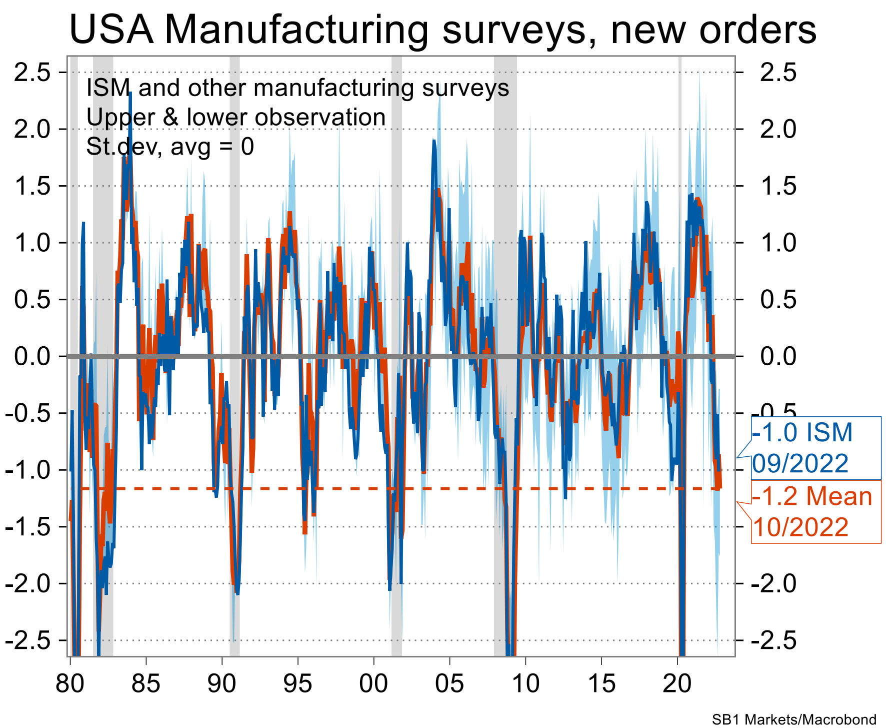


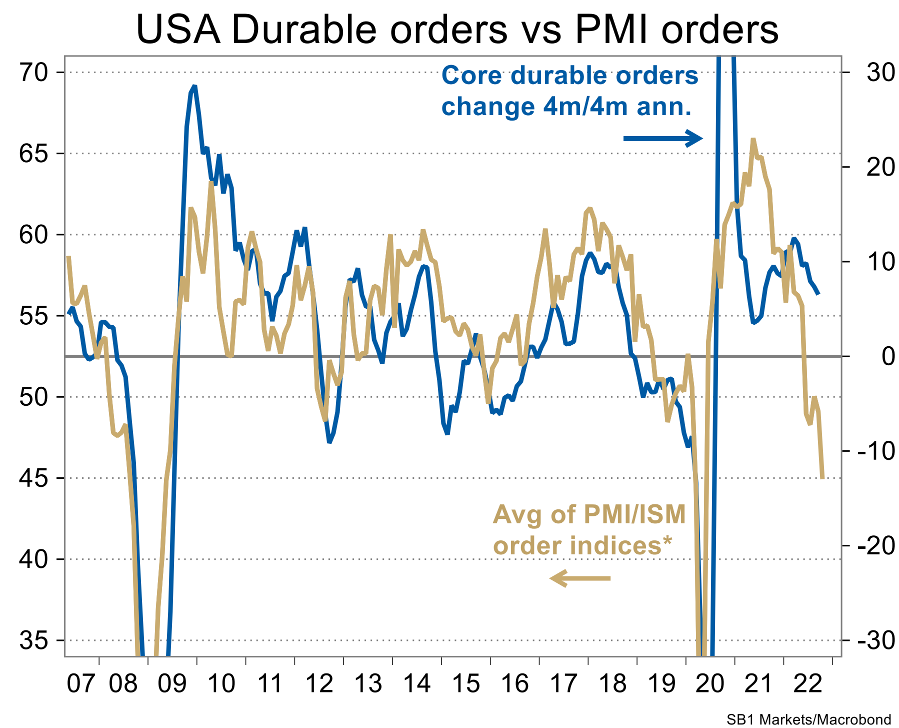


- **Core (x aircraft, defence) capital goods orders** fell by 0.7% in Sept, expected up 0.5%, partly compensated by an upward revision of August (revised up 0.4 pp) Shipments fell 0.5% m/m. All data are in nominal terms
- **The business investment** level is well above the pre-pandemic level – and not low vs. a reasonable long term trend (both in nominal and volume terms)

Surveys are signalling a steep decline in new orders

... which so far has <u>not</u> materialised...



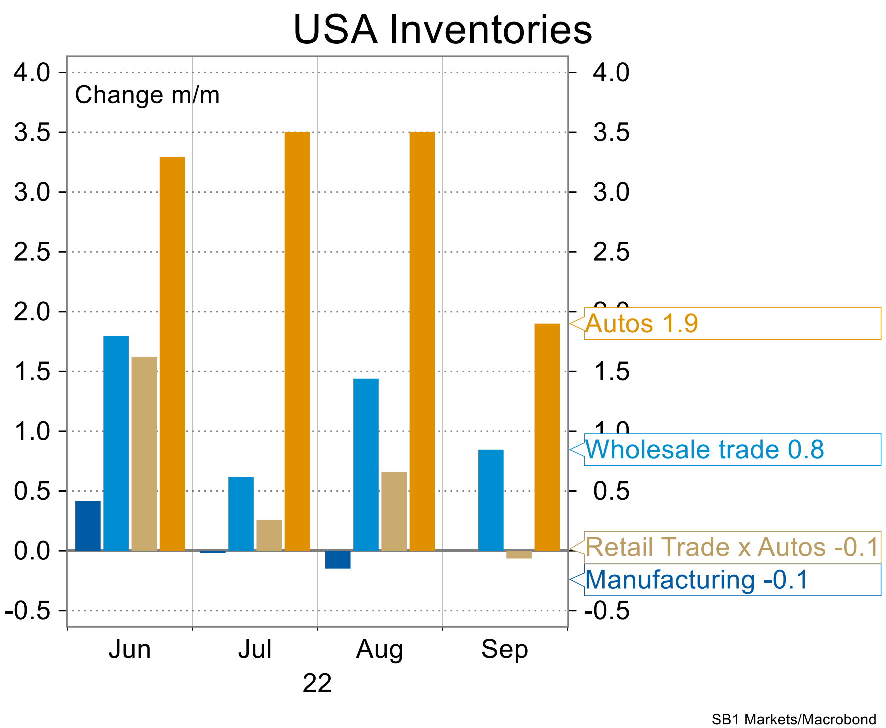


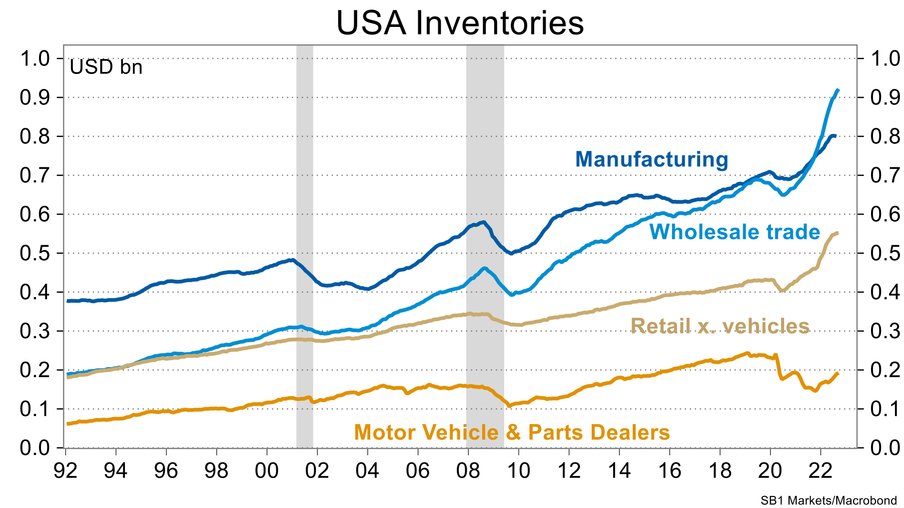
* The ISM order index is

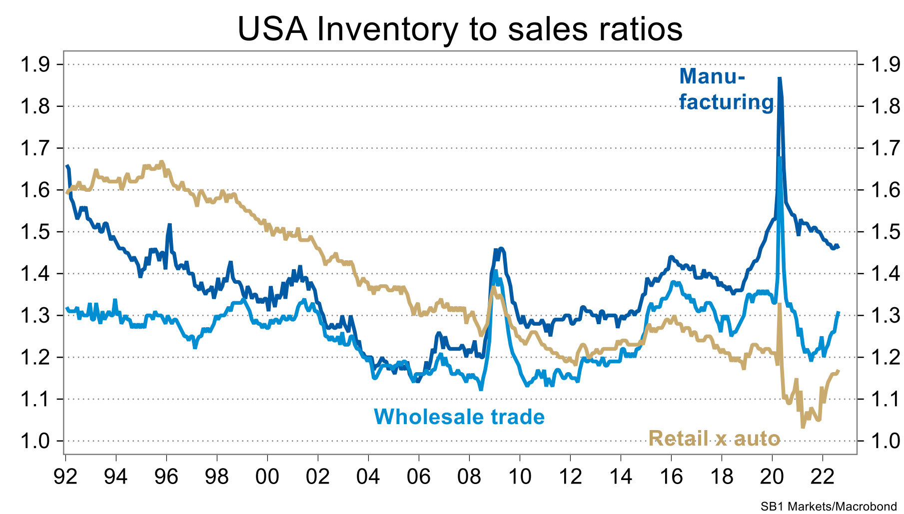
SpareBank 1 MARKETS

Inventories still up vs. sales, but at a slower pace in retail x autos

Inventories in trade are not very high vs sales but growth in inventories has slowed



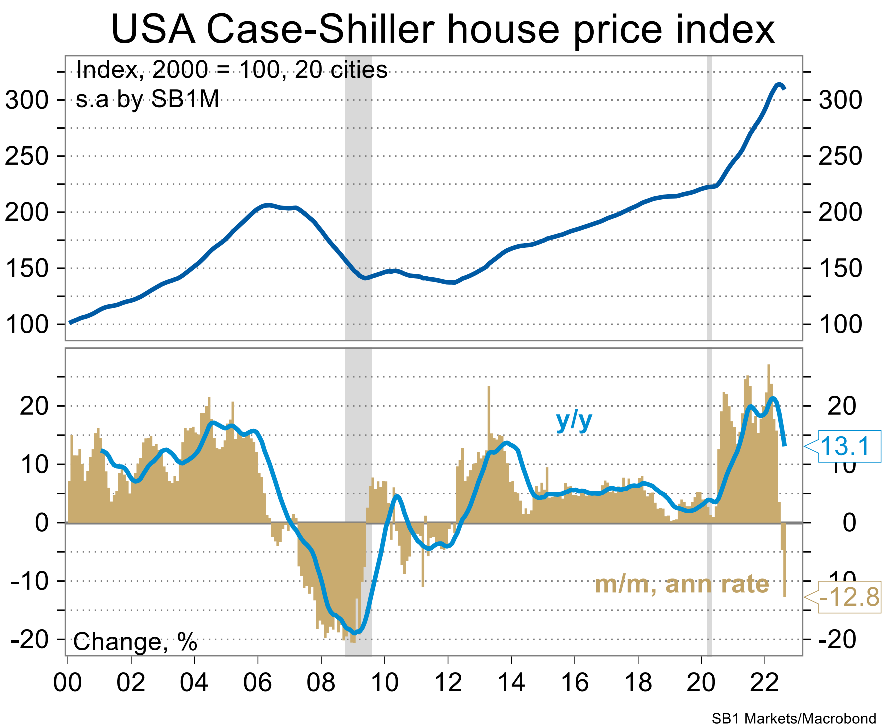


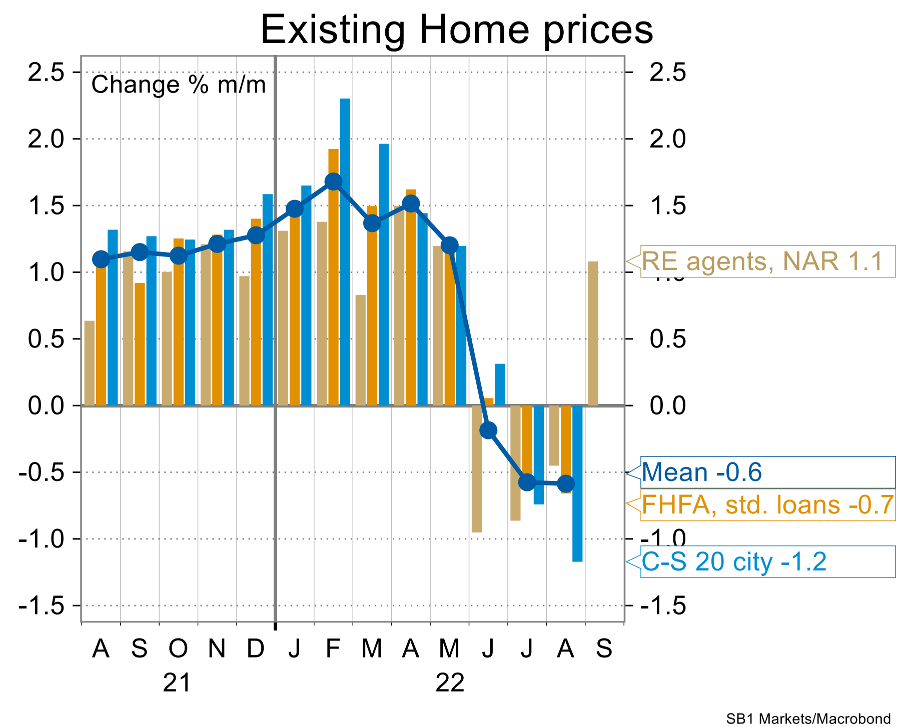


- Inventories in the **manufacturing sector** have stabilised at a level that seems to be to high vs sales

The decline in house prices is accelerating, Case/Shiller down 1.2% in August

Prices are still up 13.1% y/y, but the sign may soon change

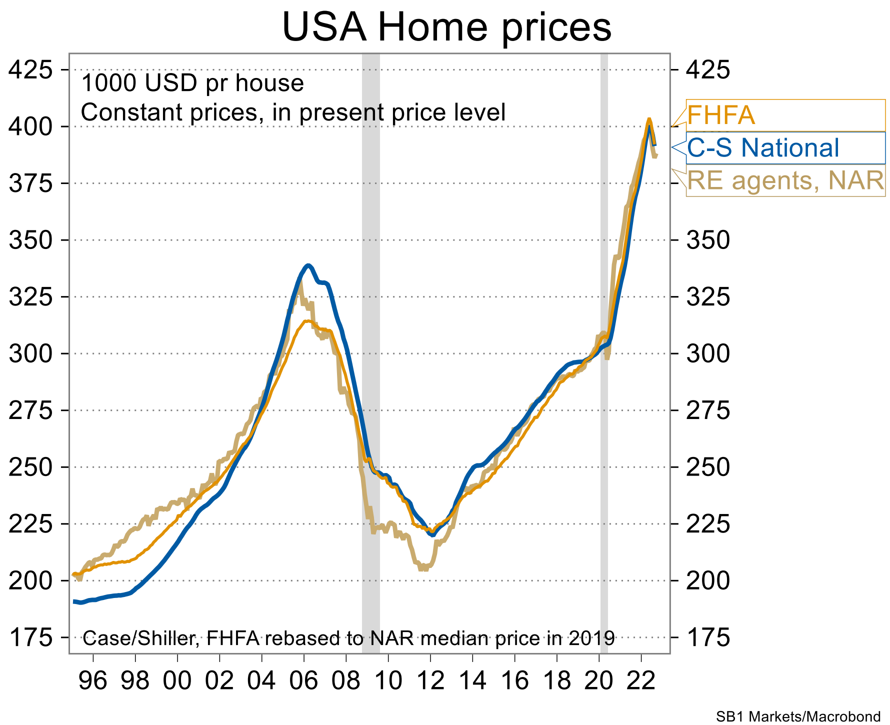


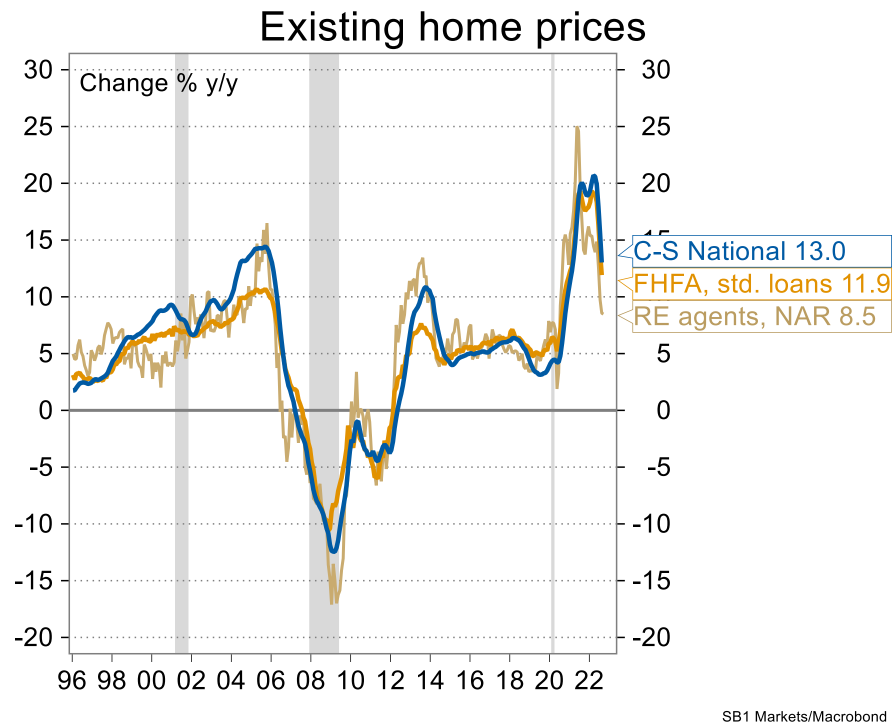


- **S&P's Case/Shiller's 20 cities** price index fell by 1.2% in August (July - Sept avg., our seas. adj, -1.3% the 'official' seasonal adjustment) expected down 0.5% – 0.8%), equalling a -12.8% annualised pace. The decline in July was revised up to 0.7% from 0.5%. The index is still up 13.1% - down from 16% in July
- **The FHFA** (Federal Housing Financing Agency) price index, which covers homes with loans guarantied by the government sponsored Fannie Mae or Freddie Mac ('Husbankene', has a countrywide coverage), was down 0.7% in August, and is up almost 12% y/y
- **Realtors** reported a 1.1% increase in home prices in September, which we doubt is the 'real' change in house prices last month. Prices are up 8.5% y/y
- <u>We still expect prices to yield substantially the coming months, following the unprecedented 42% lift since before the pandemic to the peak in June, and the surge in mortgage rates, up to 7.5% (30 y fixed), from 4% before the pandemic: affordability is totally crushed!</u>

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

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

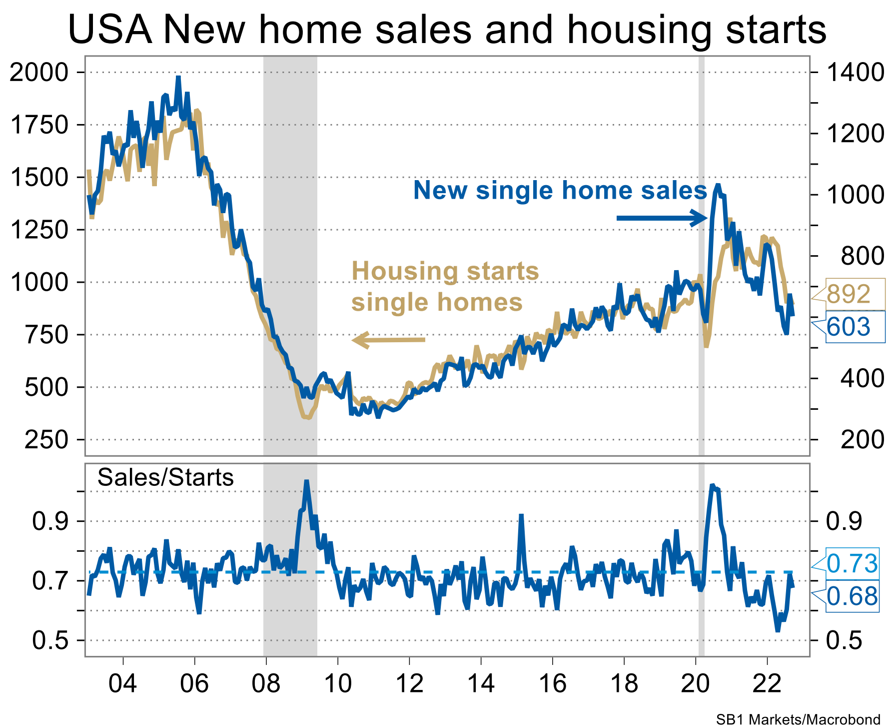


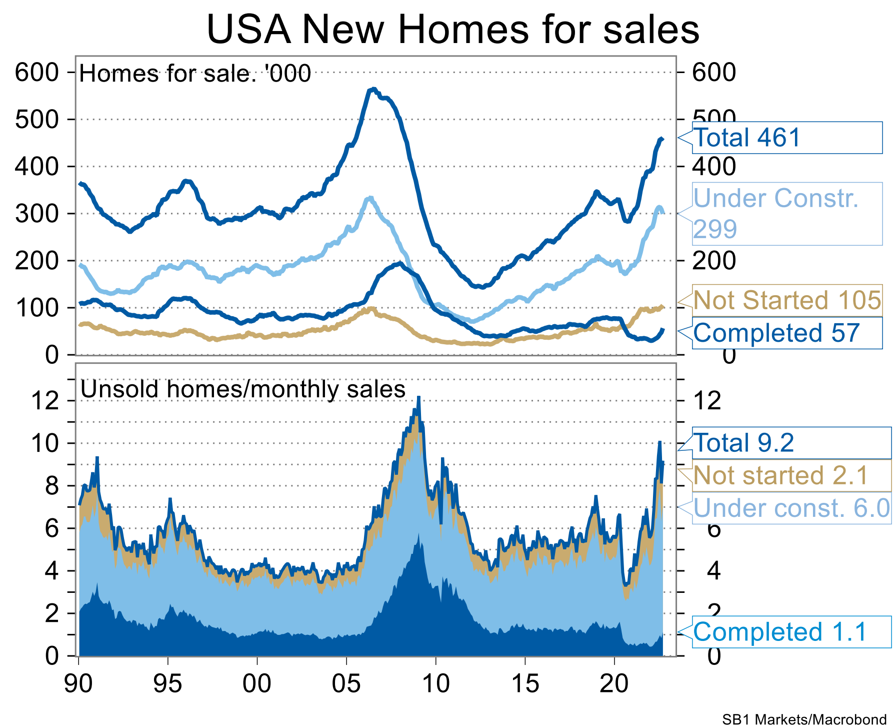


- Real prices are far above the pre-financial crisis level too
- There are still some big differences vs the mid 2000 housing bubble
  - » **Housing starts** are at a lower level. The **inventory** of second-hand homes for sale is still close to record low (vs high 15 – 16 years ago). However, the inventory of new homes for sale is climbing rapidly, and is now rather high
  - » Households average **debt/income ratio** has fallen sharply since the peak before the financial crisis, and their cash positions have soared (on average) to above debts. However, credit growth has accelerated rapidly during the pandemic, and housing affordability is far weaker than in early 2006, when the previous bubble burst
  - » The **savings rate/net financial investments rates** have now fallen to well below the pre-pandemic level – but the ratios are above their respective levels in 2005

New home sales down in September, very likely much more to go

The trend is set, and home builders are signalling a further, large decline

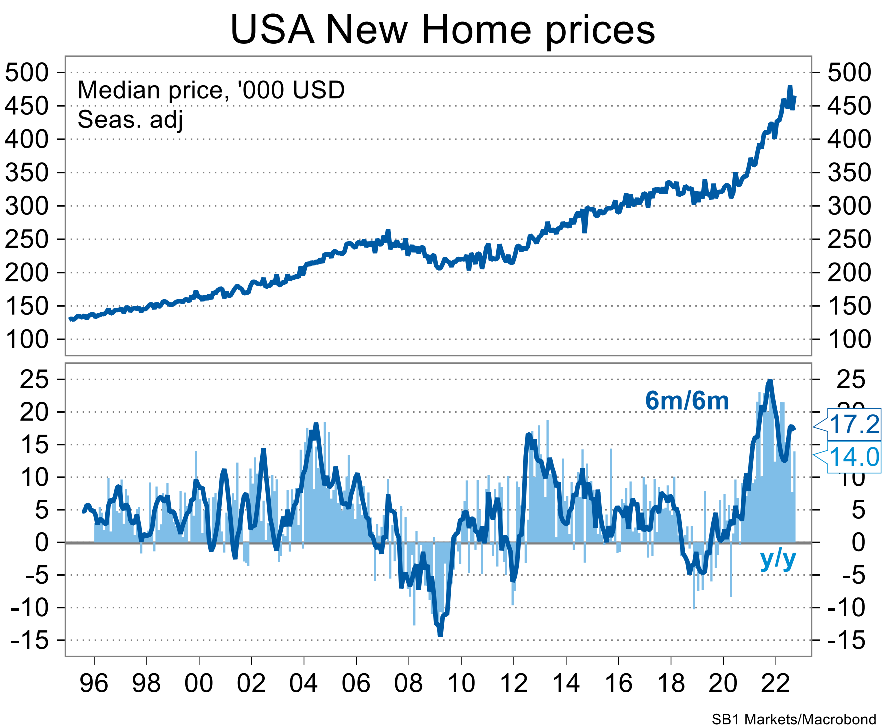


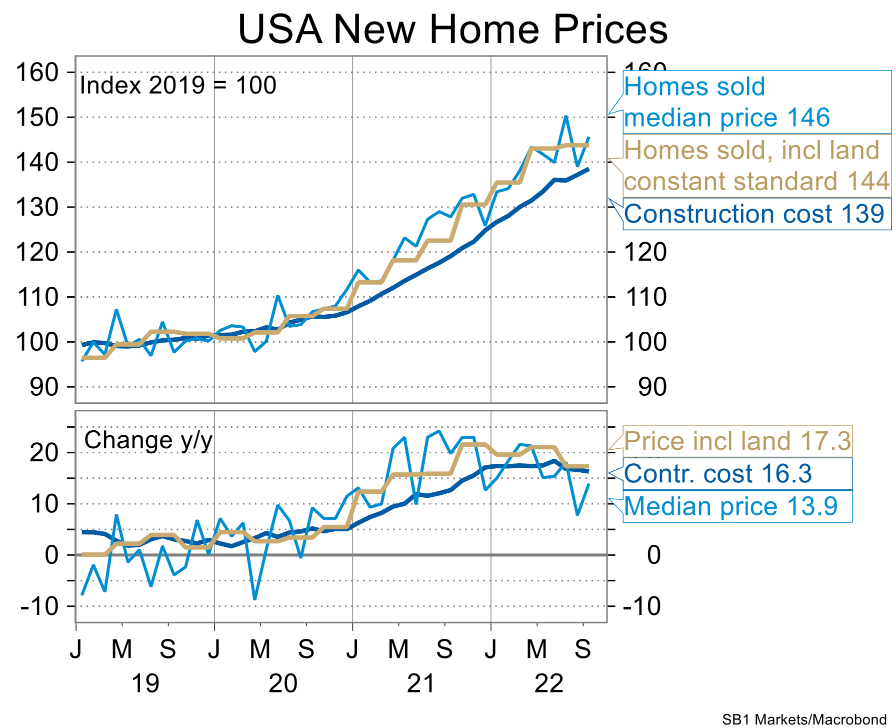


- **New single home sales** surprised sharply on the upside in August, and just a smaller part than expected of the lift was reversed in September. Sales fell to 603, expected 581, down from 677' in August. In July, sales were down at 543'! Anyway, the trend is down, home builders are extremely anxious, demand for new mortgages are falling rapidly.
- **The inventory of unsold homes** fell marginally in September, but the trend is straight up, and the level is high, both in absolute terms, and vs. sales – the latter not that far from ATH, at 9.2 months of sales. Most of the inventory is 'for real', either completed homes (but the level in this category is still very low) or under construction (and these homes will be completed) – as the supply side responded to the strong increase in demand & prices. A steep increase in number of homes for sales that are not yet started, also confirms the strength of the potential supply side (but most of these projects will very likely not be started as at least the housing market has entered a recession)
- Prices increased slightly in September but the short term trend is flat – and very likely, prices will soon turn south

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

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

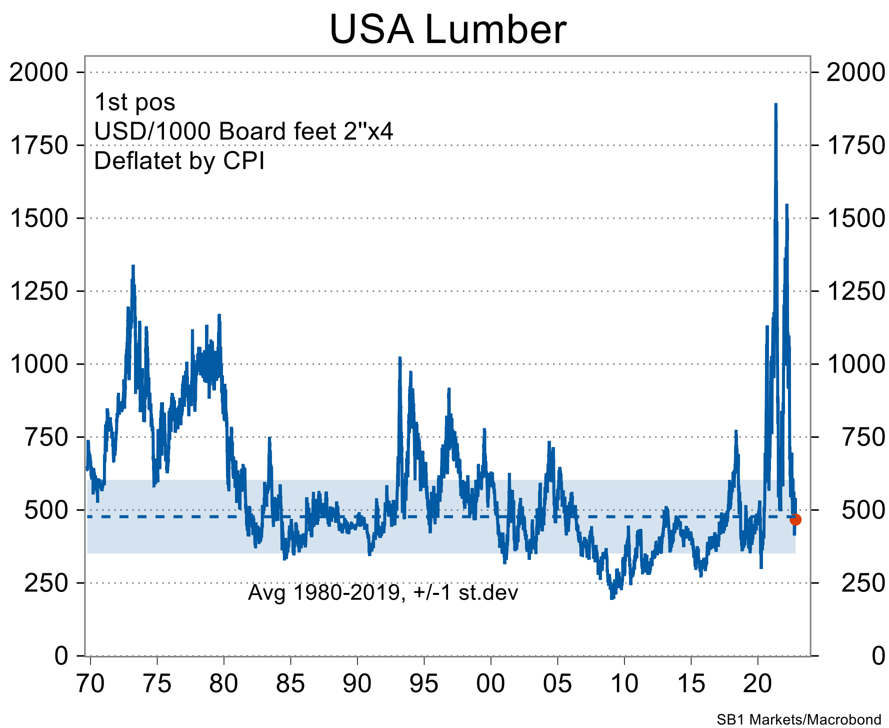


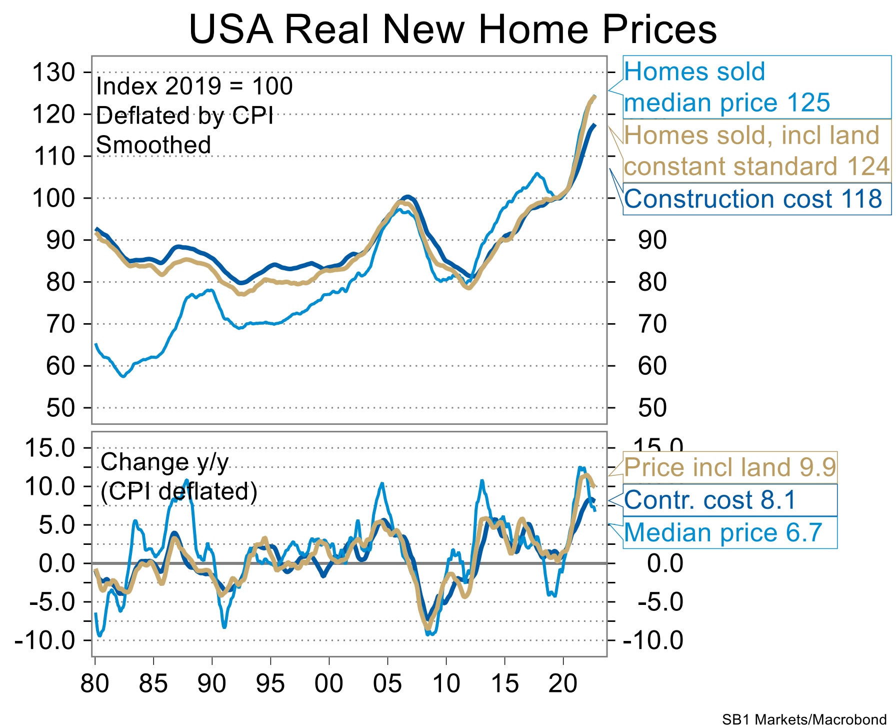


- The monthly **median new home sales prices** are <u>very</u> volatile, as they are not adjusted for changes in the mix of homes sold. In September, prices were up 14% y/y, up from 7.9% in August, still down from above 20% at the peak – and prices have flattened since the spring
- The **construction price index** is adjusted for changes in standard and size, as is the **new homes sold price index**, which also includes cost of land: they are up by 16% (in Sept) and 17% (Q3) resp. However, the home sold price index has also flattened since the spring. Construction costs have flattened, and will very likely now ease substantially as <u>material prices are nosediving</u>

A spectacular increase in real new home prices/construction cost past 2 years

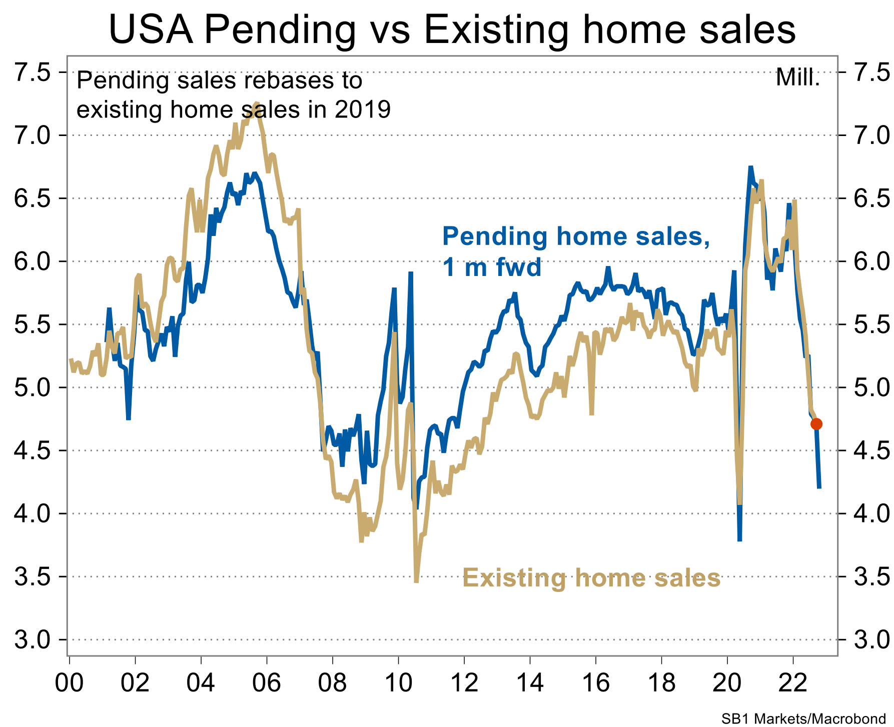
A reversal is likely. Some material prices have already normalised

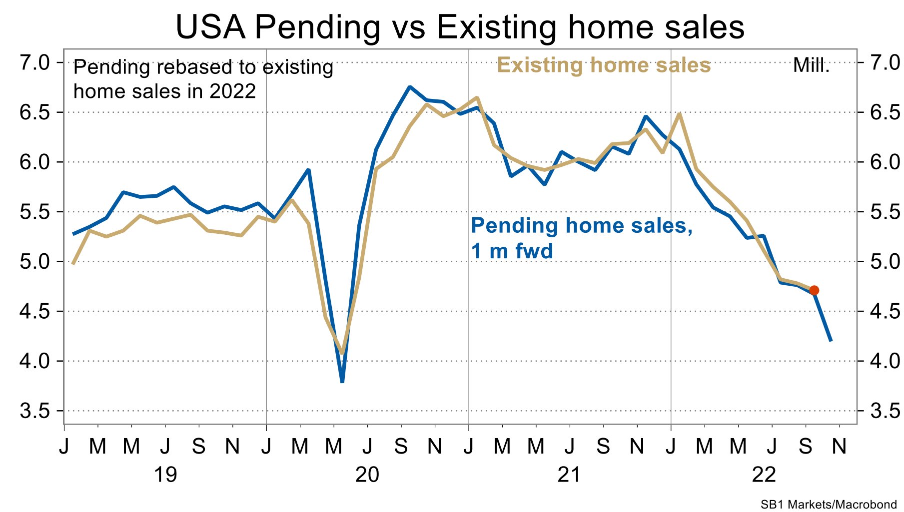


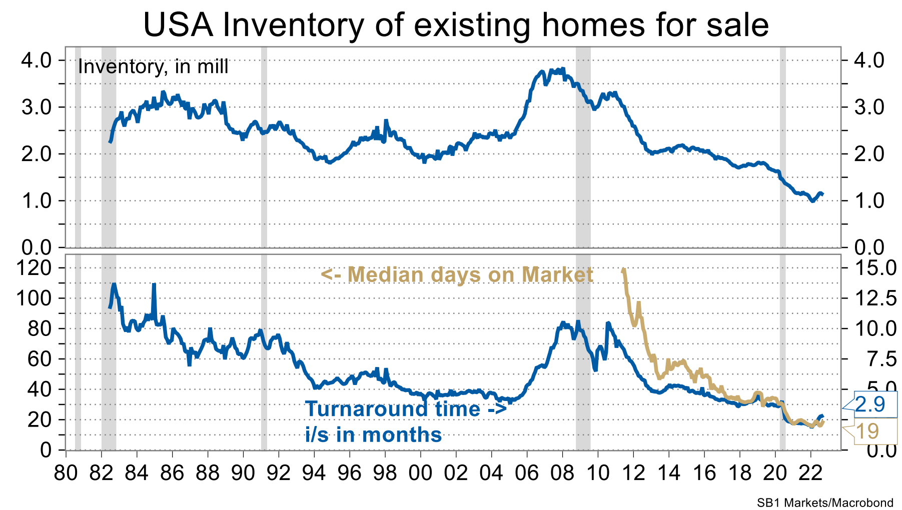


Pending home fell off the cliff in September, not far above ATL

No. of agreed transactions fell 20%, and is down 35% from last November





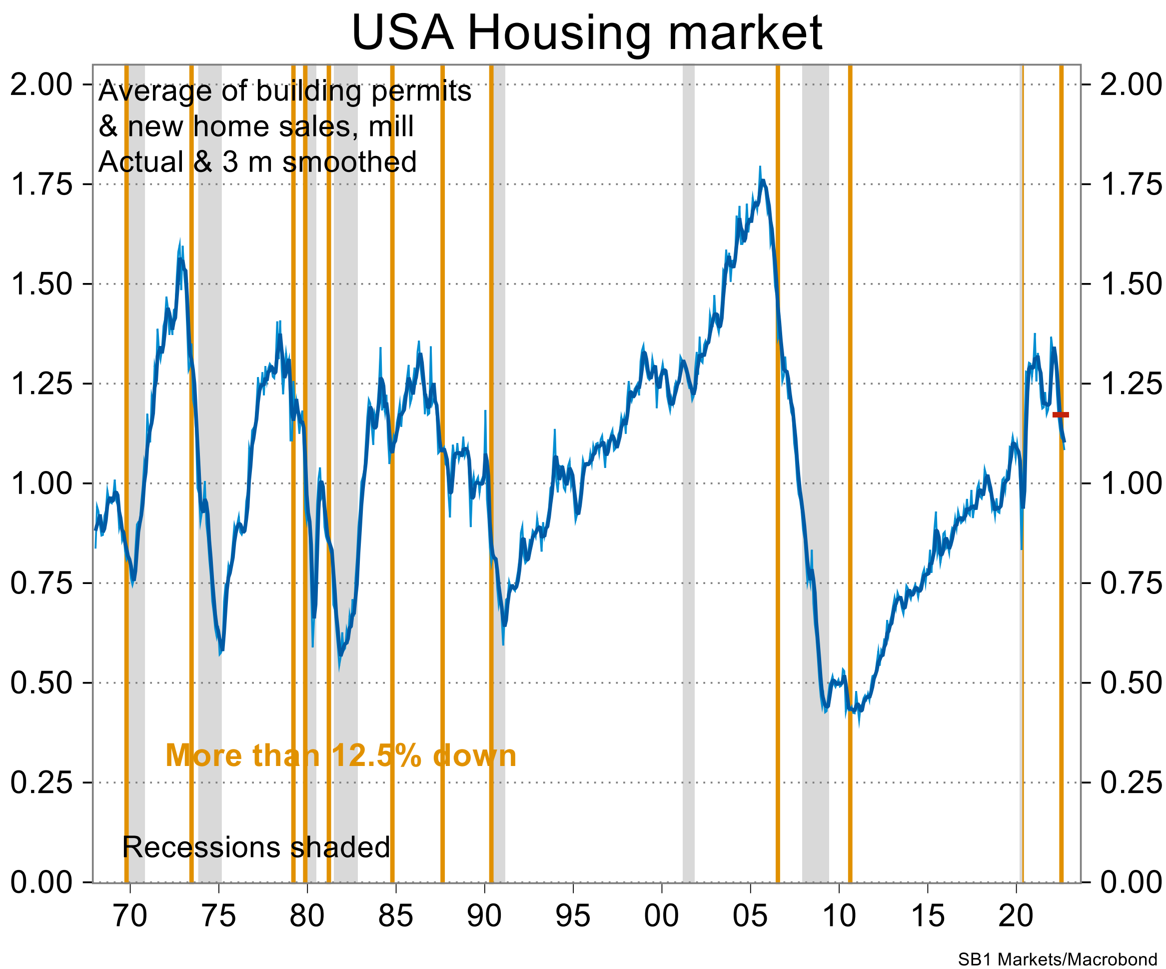


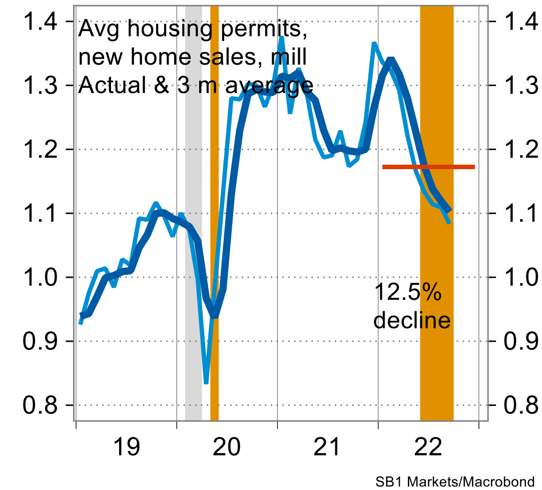
- The decline in September was far larger than expected (4%), and the level is approaching previous troughs, in 2010, and 2020. Existing home sales (actual transactions) will very likely follow suit in October
- The decline confirms that higher mortgage rates <u>are</u> slowing the housing market sharply

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

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

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

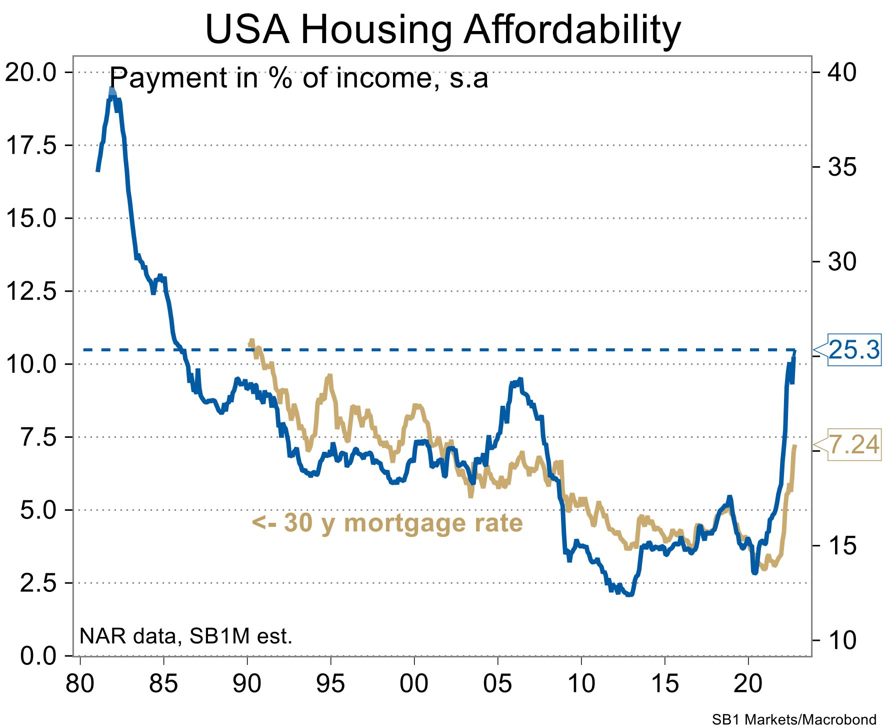


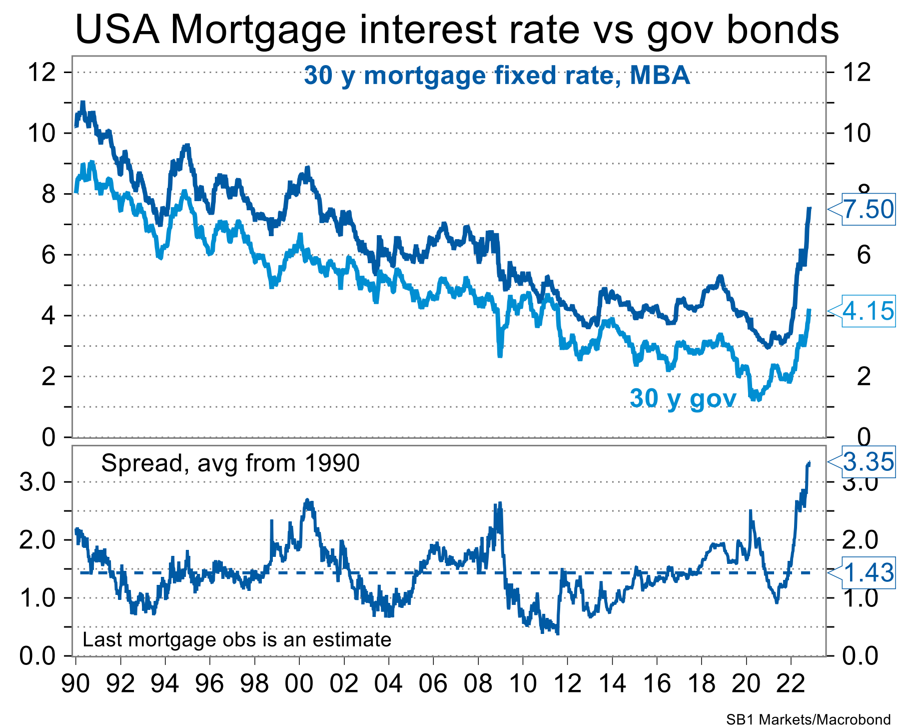


- Most recessions are 'housing recessions' as demand for housing and residential investments decline substantially ahead of and during recessions
  - » The only exception in recent decades was the 'Nasdaq' recession in 2001
  - » In addition, the pandemic recession was not caused by a setback in the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

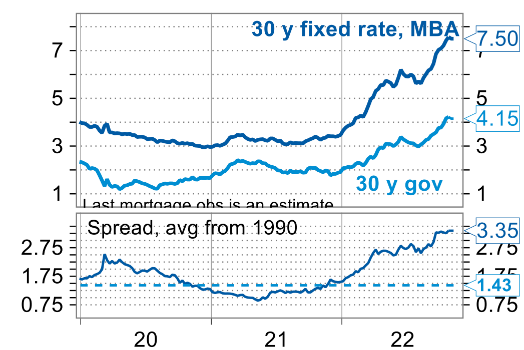
A mortgage market meltdown, the margin to 30 y gov bond unprecedented!

The effective mortgage 30 y rate at 7.50%, a 20 year peak. Will the Fed be forced to do a 'BoE'?



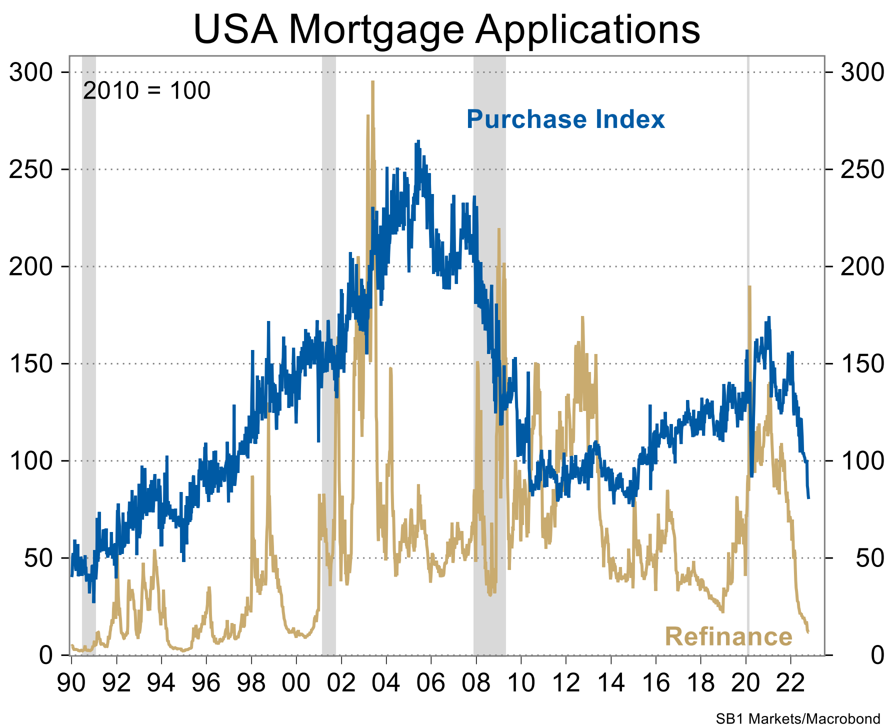


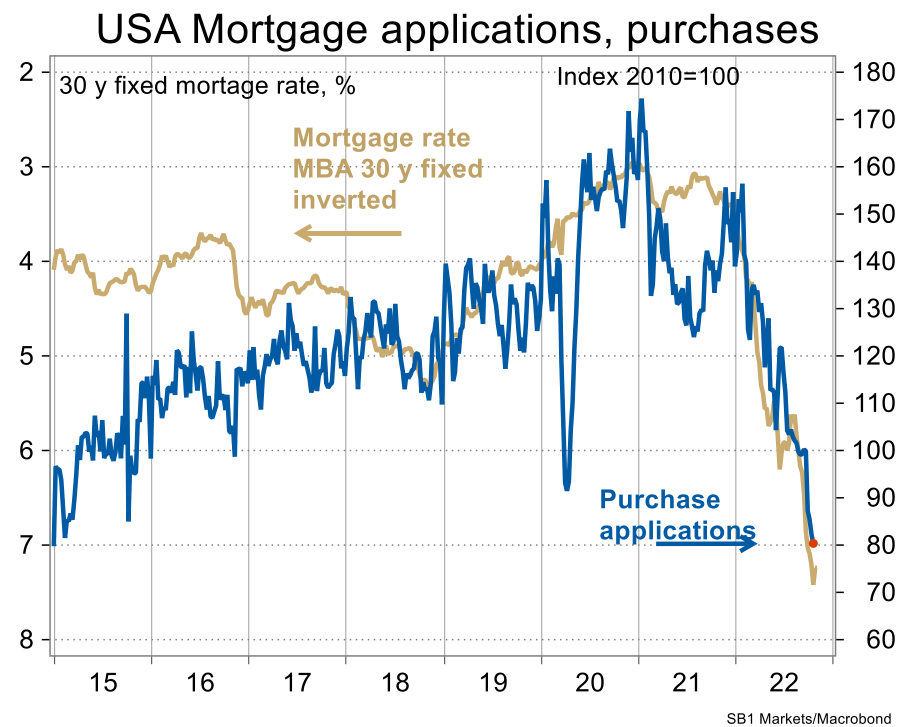
- The 30 y fixed mortgage rate has shot recent weeks (and months), both due to higher 30 y gov. bond rate and a dramatic widening of the spread up to the mortgage rate. The spread was 0.9 pp at the bottom when the Federal Reserve snapped up all net mortgage bond issuances even if prices rose 20% y/y. Now the Fed is selling mortgage backed bonds, and the spread is above 3.30%
- At which stage will the Fed decide that the market is not working, and that is has to start buying bonds again, just like the Bank of England had to do in order to prevent a completely meltdown in the UK gilt market last months? We think that we are not that far away, probably far less than 100 bps
- Housing affordability (house price x mortgage rate/income) is the deteriorating by the day – to the worst level since 1986!



Mortgage applications have plummeted, for good reasons

Applications for new loans are down by <u>49%</u> from the local peak in January, and are still falling

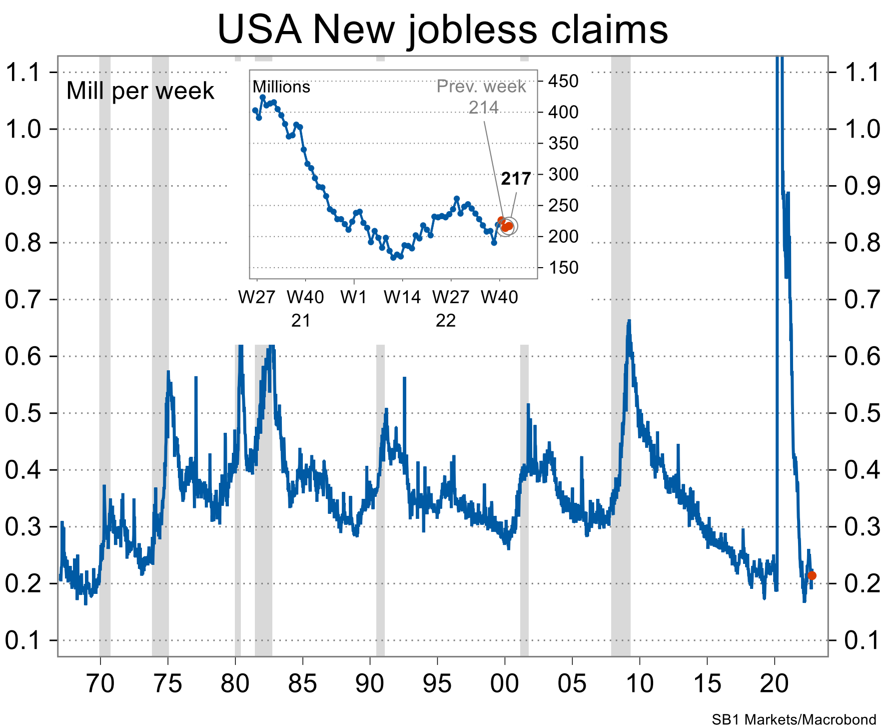


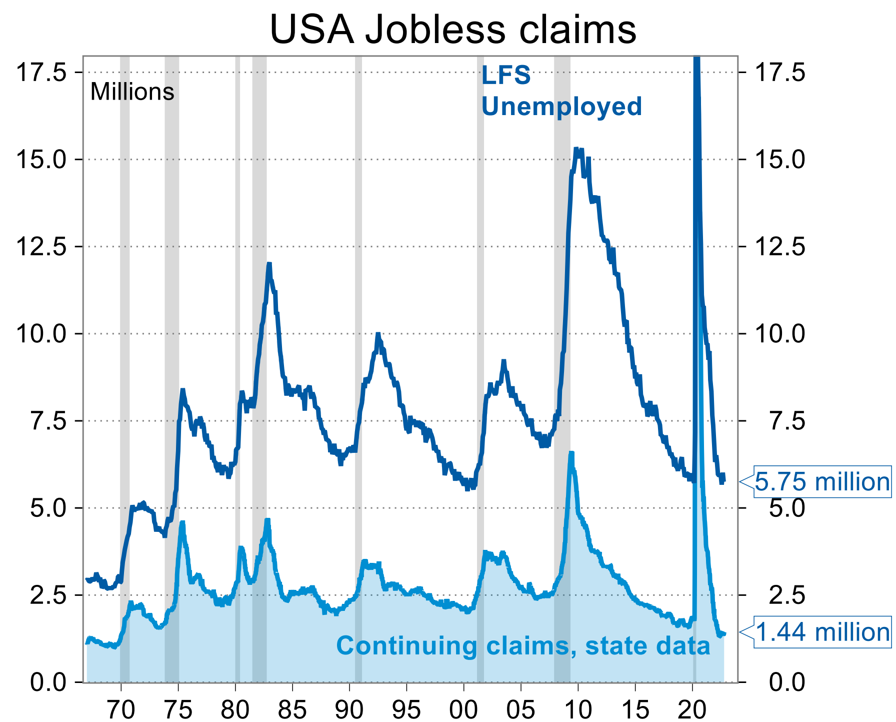


- Demand is now on the low end – 40% below the pre-pandemic level, not far above the bottom during the financial crisis
- Recently, mortgage rates have risen, alongside the increase in the 30-year treasury bond rate
- ‘Nobody’ is refinancing, for good reasons, given the current mortgage rate

The inflow of new jobless claims remains at very low level

New jobless claims just marginally up to 217’, expected 220’ – a incredibly low level

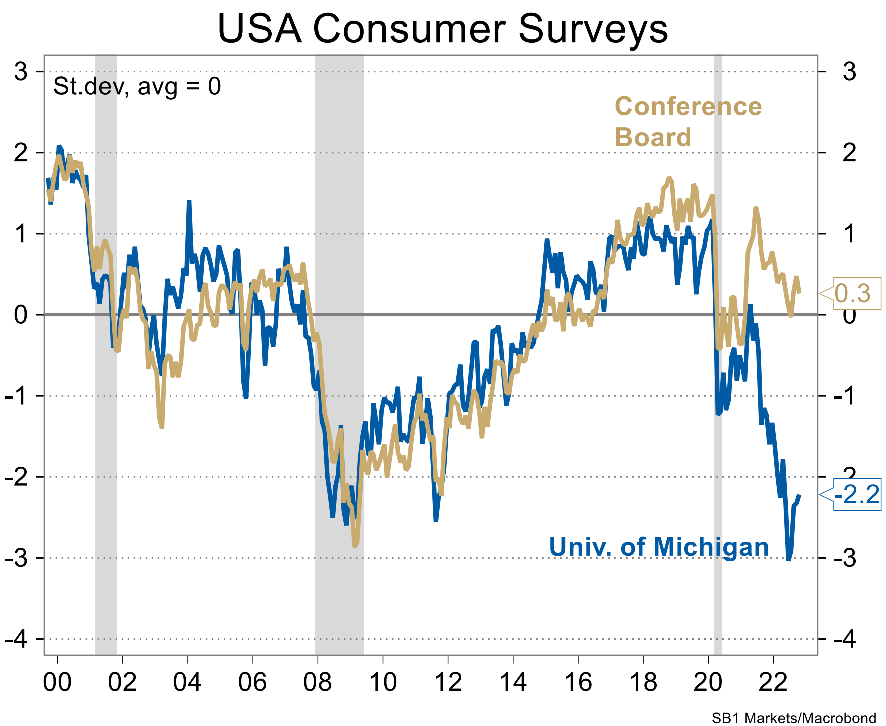




- **New jobless claims** rose by 3’ to 217’
- **Continuing claims** rose by 55’ to 1,440’ in week 41. The trend is slightly upwards but the level remains very low
- Both indicate a very tight labour market

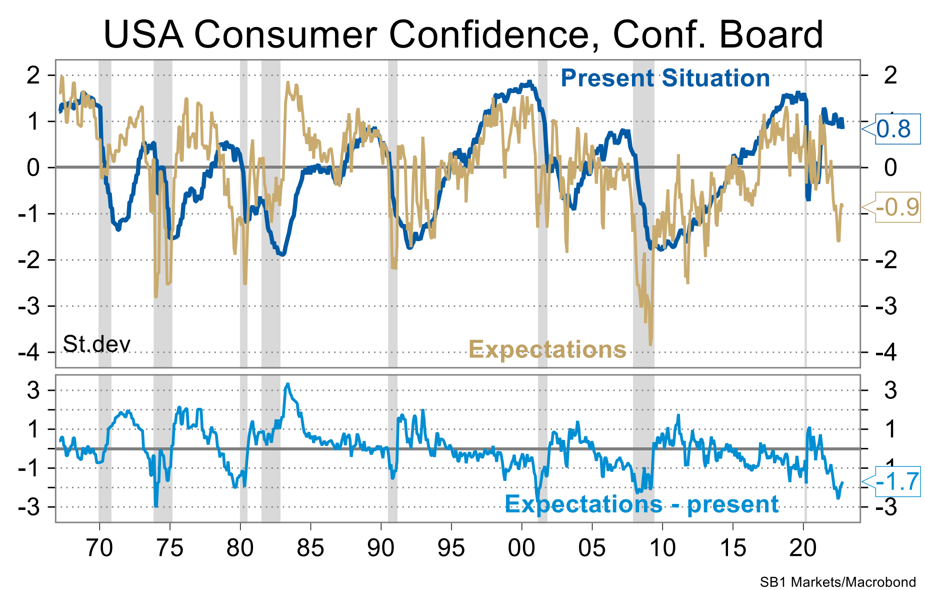
Conference Board's Consumer confidence slightly down in October, still > avg.

However, expectations are below average, normally a warning sign. Inflation expectations marg. up



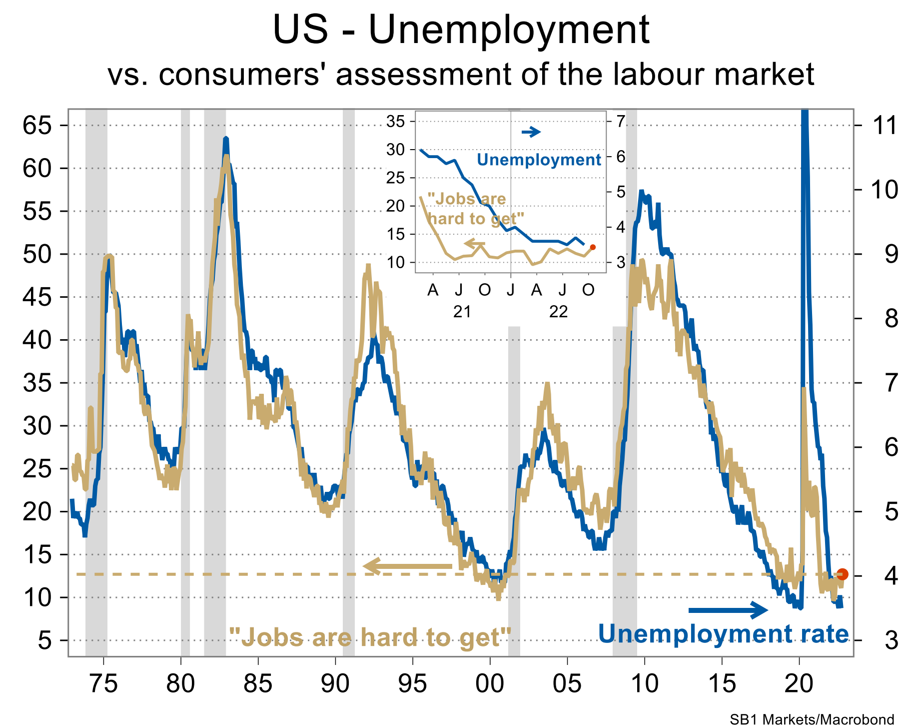
- **The other consumer** surveys we follow are on another planet, even if they have recovered somewhat since the summer. University of Michigan's sentiment in Oct was unch. from the first estimate at -2.2 st.dev below avg. – a very low level
  - » Two other confidence surveys, from IBD/TPP and Univ. Florida are not much better than the UM survey – and <u>Conf. Board's survey is an outlier</u>

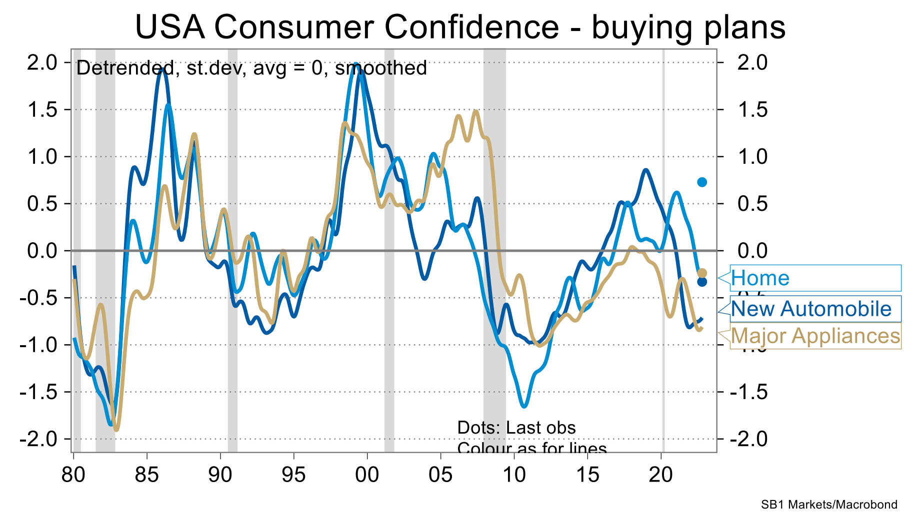
- **The main index** declined by **5.3 p to 102.5 in Oct, expected down to 105.7. The present situation index fell 11 p, while the expectation component fell just marginally**
  - » The decline in the main index equalled 0.2 st.dev, and the index remain 0.3 pp above average – due to a still strong present situation index, at +0.8 st.dev.
  - » **Expectations** are weak, 0.9 st.dev below average, which is normally seen in recessions (but not only)
  - » **The difference** between households assessment of the present situation and their expectations is at -1.7. <u>The gap is always the largest just before or when a recession hit, check the chart below</u>

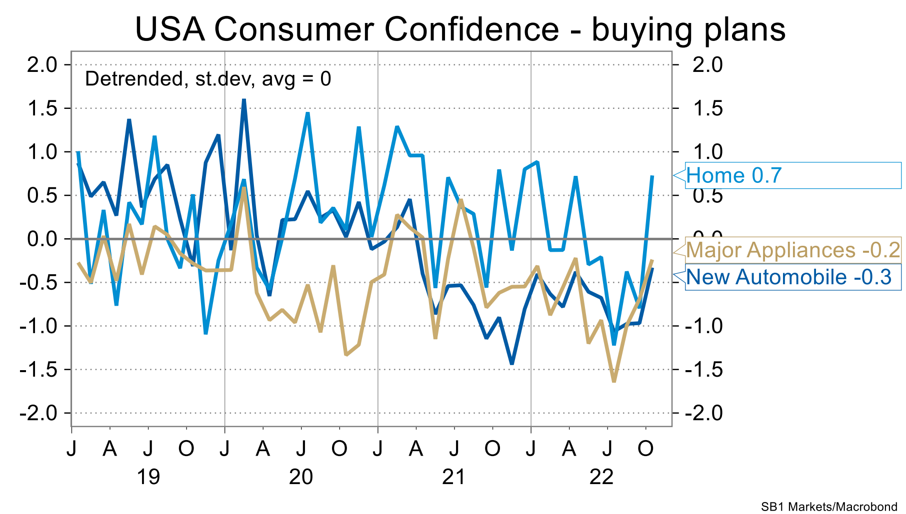


Home buying plans straight up in October; Autos, appliances also up. Really??

Rather surprising given the surge in mortgage rates recent months, in addition to high inflation

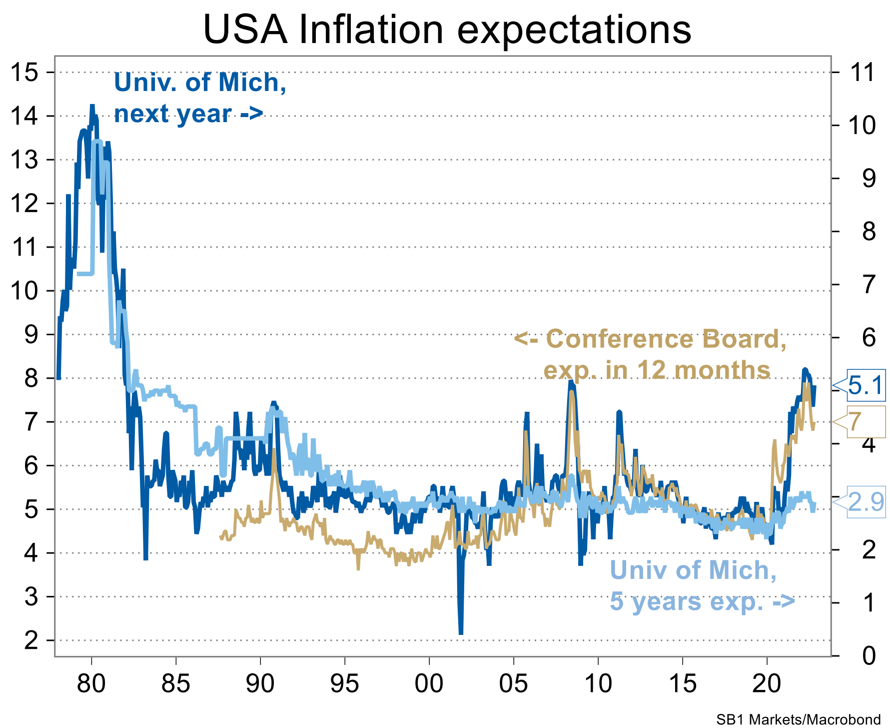


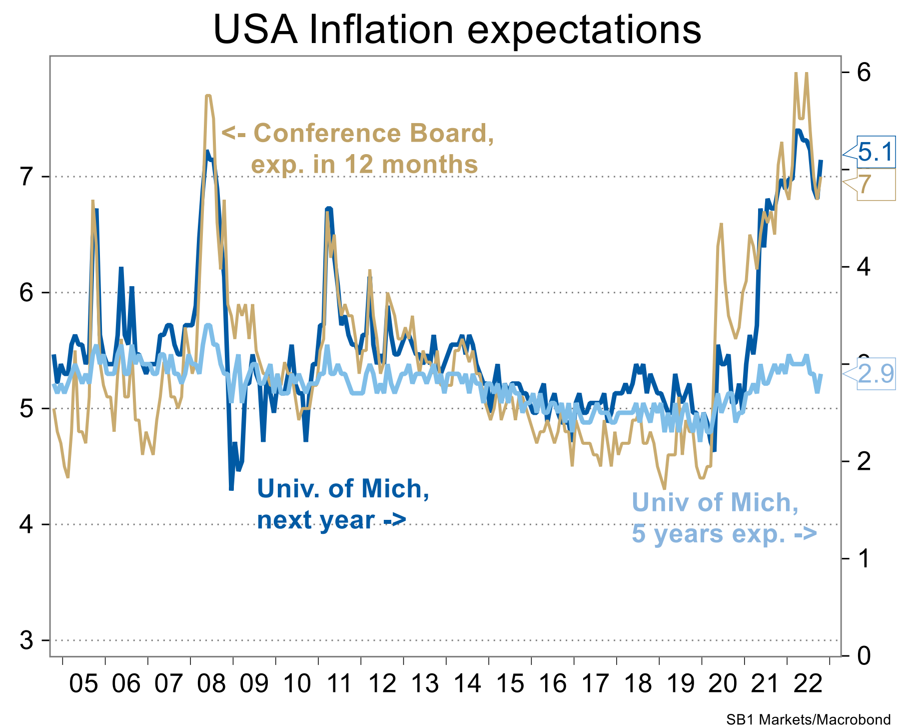




- Furthermore, households are getting a tad more cautious vs the **labour market.** Jobs are still not hard to get, but somewhat less easier than the level seen since last summer

Inflation expectations up in October, still well down from the peak

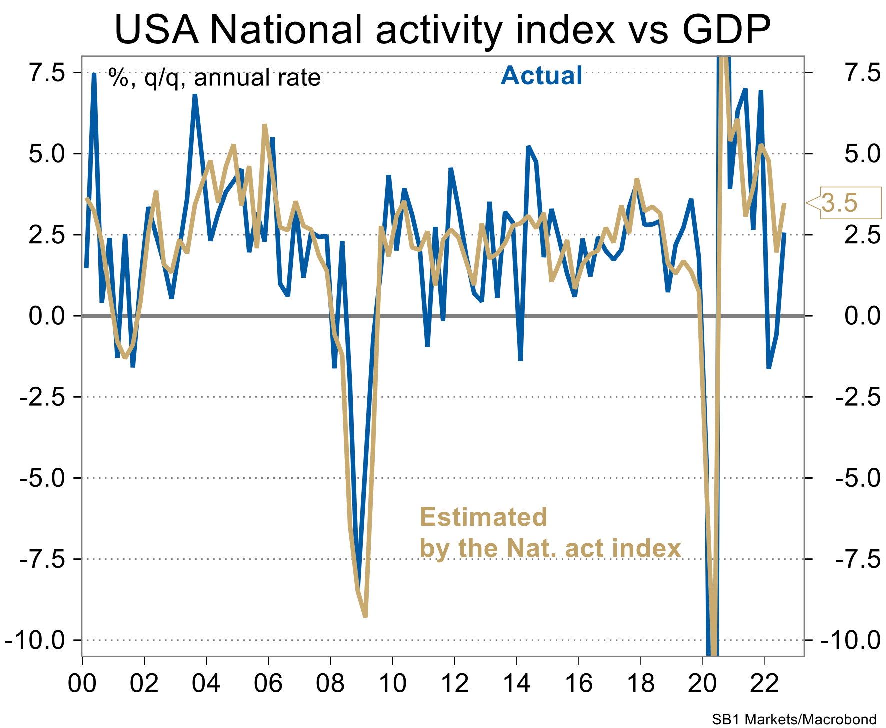


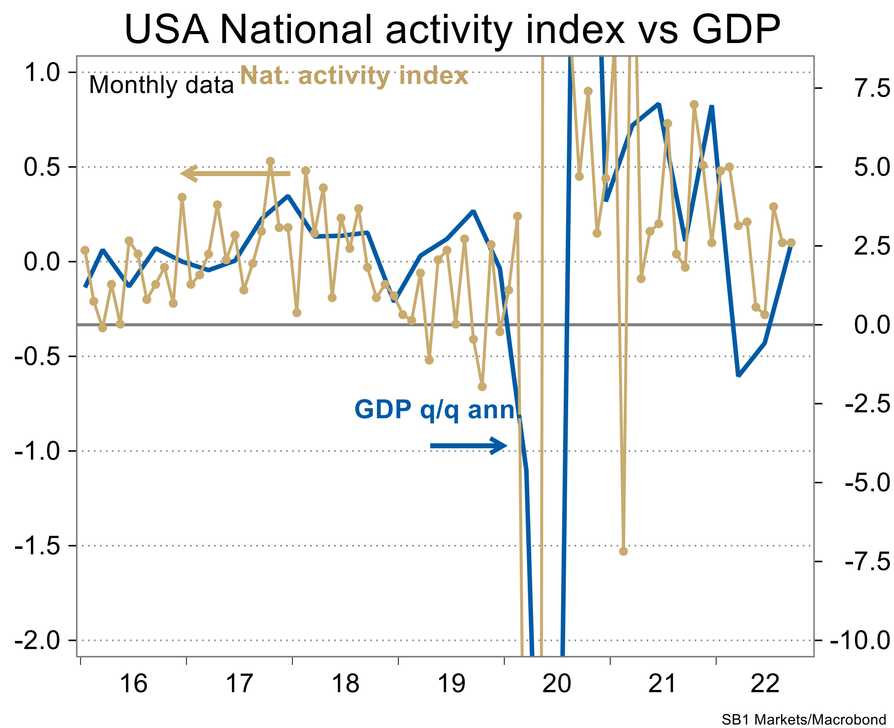


SpareBank 1 MARKETS

The National activity index signalled 3.5% GDP growth in Q3.

… and the index signals a 2.5% growth pace at the end Q3, which bodes well for Q4

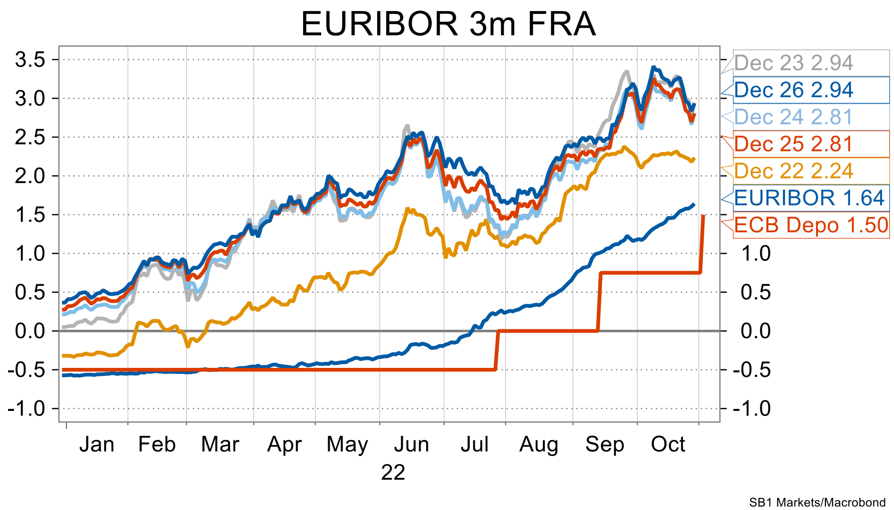


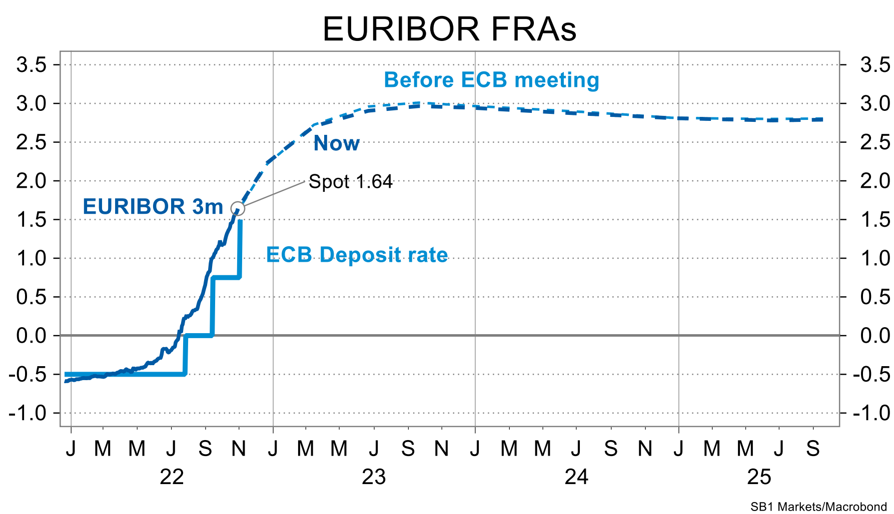


SpareBank 1 MARKETS

ECB doubles rate in an already weakening economy but signals a slower pace?

The ECB hiked the signal rate by 75 bps - «*because inflation is far too high*»





- **The 75 bps hike** was expected by the majority of economists as inflation data had continued to surprise on the upside, but the market had expected the bank to be slightly more hawkish and the FRAs fell after the decision as the wording of their statement was changed to hiking rates "for several meetings" to "the council… expects to raise interest rates further". All despite the bank recognising that demand is softening and that the risk of a recession has increased, but that they are data that indicate that are wages picking up (Is the bank seeing something we are not?)
- The bank repeated its statement **that inflation is far too high** and likely to stay above target for an extended period, and that the bank stands ready to adjust all of its instruments within their mandate to bring down inflation
- The bank also made changes to **the TLTRO III programme** (encouraging bank lending). Rates will now be indexed to average ECB interest rates (these rates used to be 50 bps below the ECB deposit rate, and for some it could be in the range of -1% to -0.5%) and three voluntary repayment dates are introduced for banks who want to reduce borrowing. In addition, **the minimum reserves** are now to be renumerated at the deposit facility rate (currently at 1.5%) as opposed to the main refinancing operations rate (2%)
- Largarde repeated several times that the ECB has **made significant progress to withdraw monetary accommodation and that it has more ground to cover and that there are more hikes in the pipeline.** The president also stated that while the risk of a recession has increased - the ECB's job is to bring down inflation
- At the same time, the bank continued **not to give a forward guidance**. Rather the bank said it will be data dependent and follow a meeting-by-meeting approach (central banks always do that anyway, even with a forward guidance), and focus on three factors: inflation outlook, measures taken so far, and the transmission lag of monetary policy
- **Short term market rates** fell after the announcement. Longer dated EURIBOR FRAs also fell, but less than in the short end. Long term yields fell almost 20 bps. The market is realising that the rate hikes are starting to work and that the economic outlook has already weakened. However, at Friday the short end of the curve turned up again

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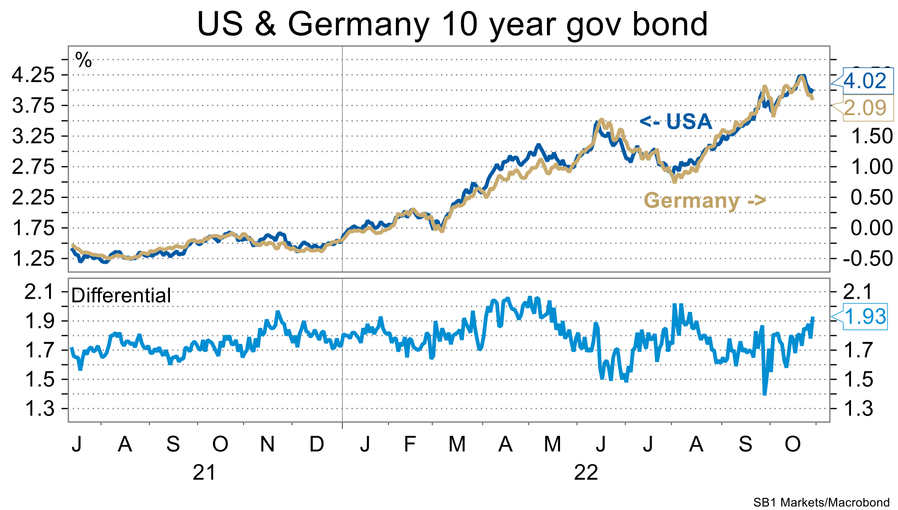
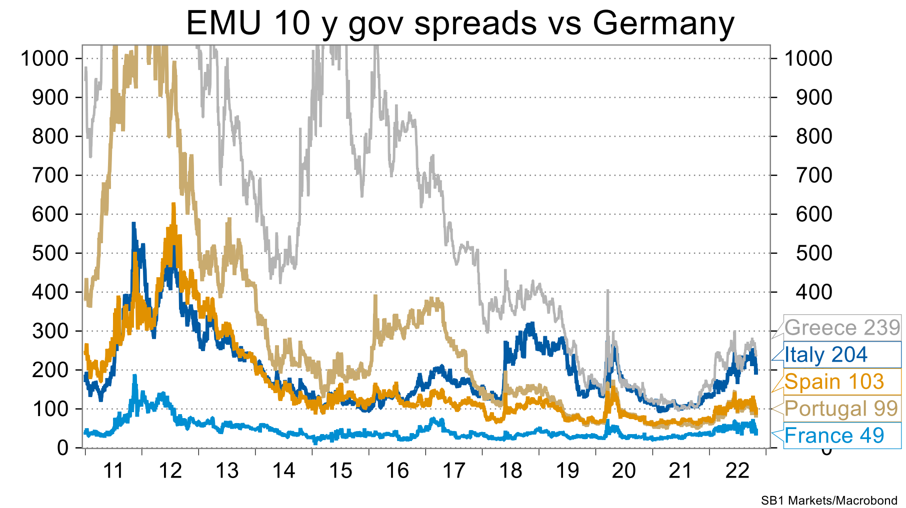
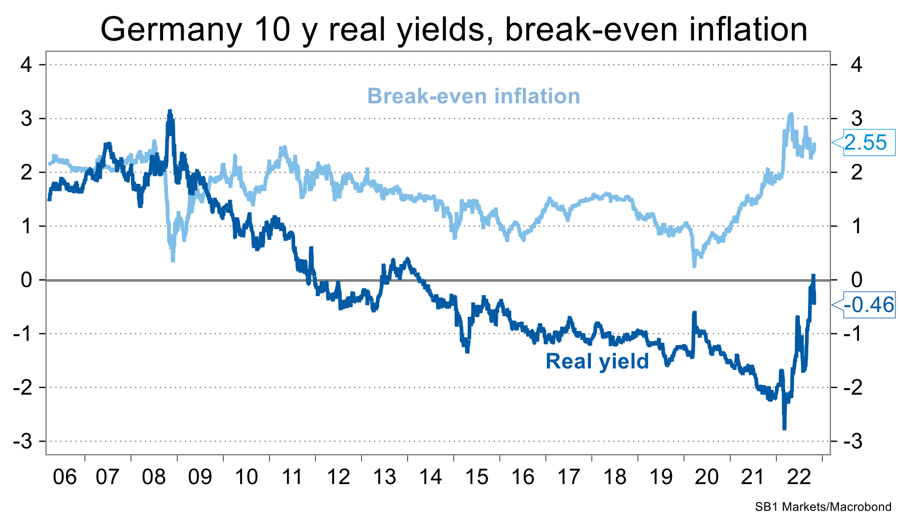
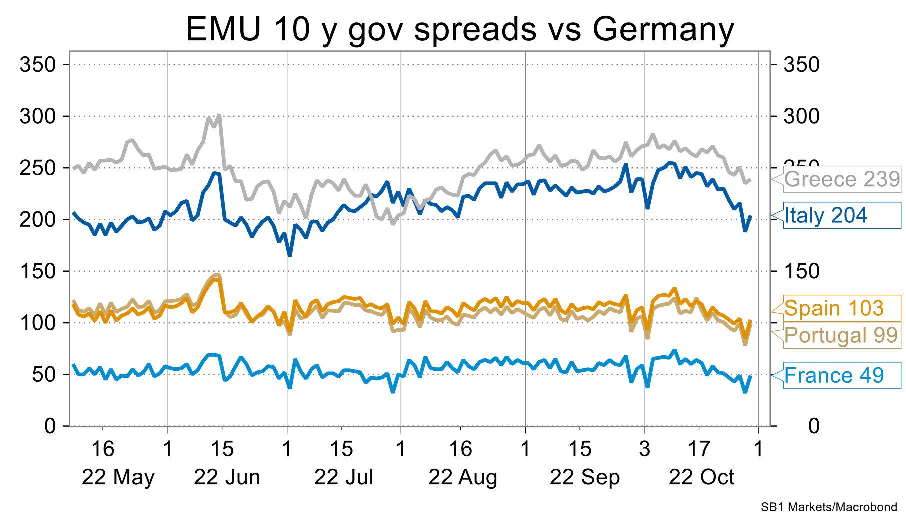
Bond yields down last week, also before ECB's meeting. Spreads are narrowing



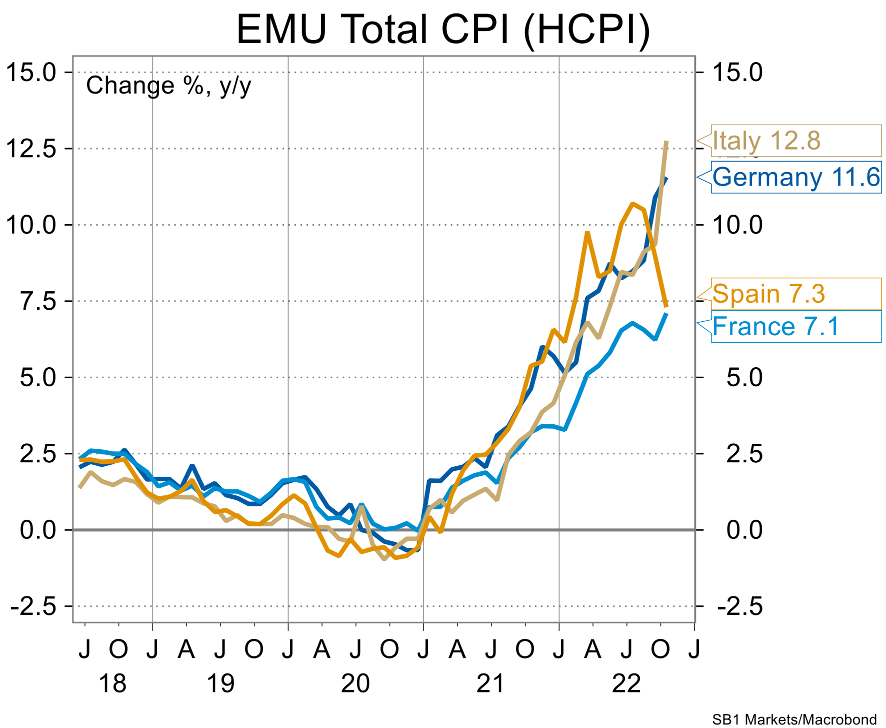


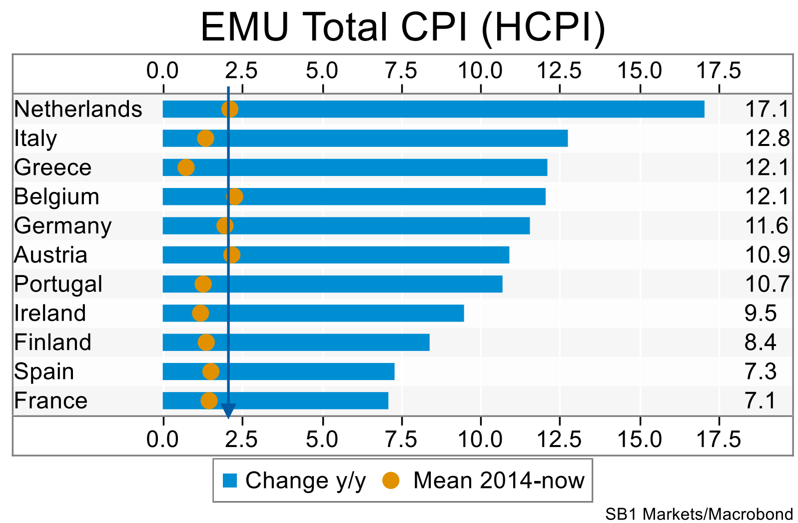




Inflation further up in October, to 11.6% in Germany, 12.8% in Italy

… at least according to preliminary data. Inflation in Spain down to 7.3%, due to energy subsidies

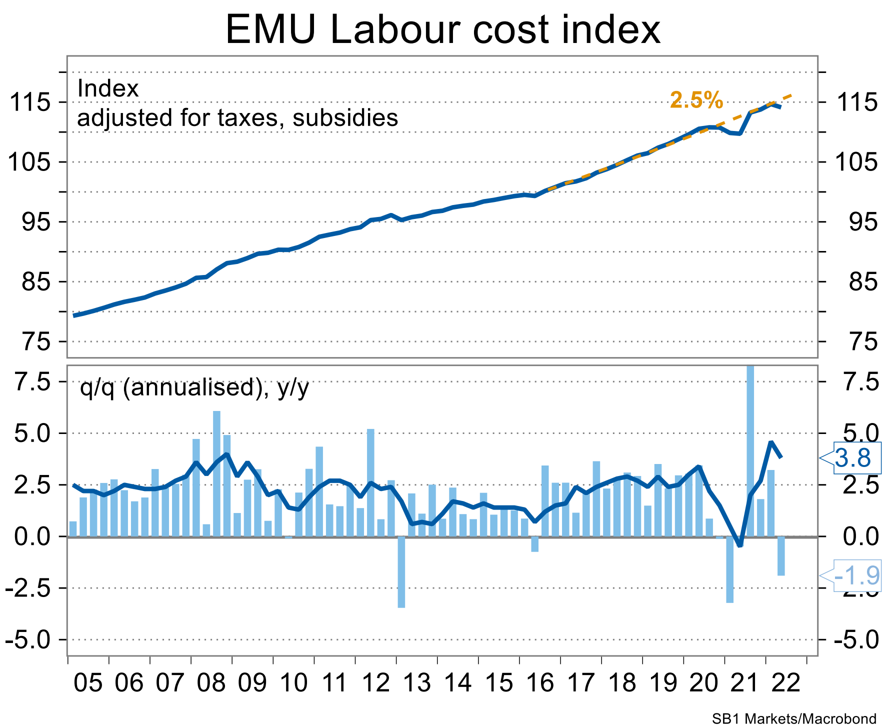


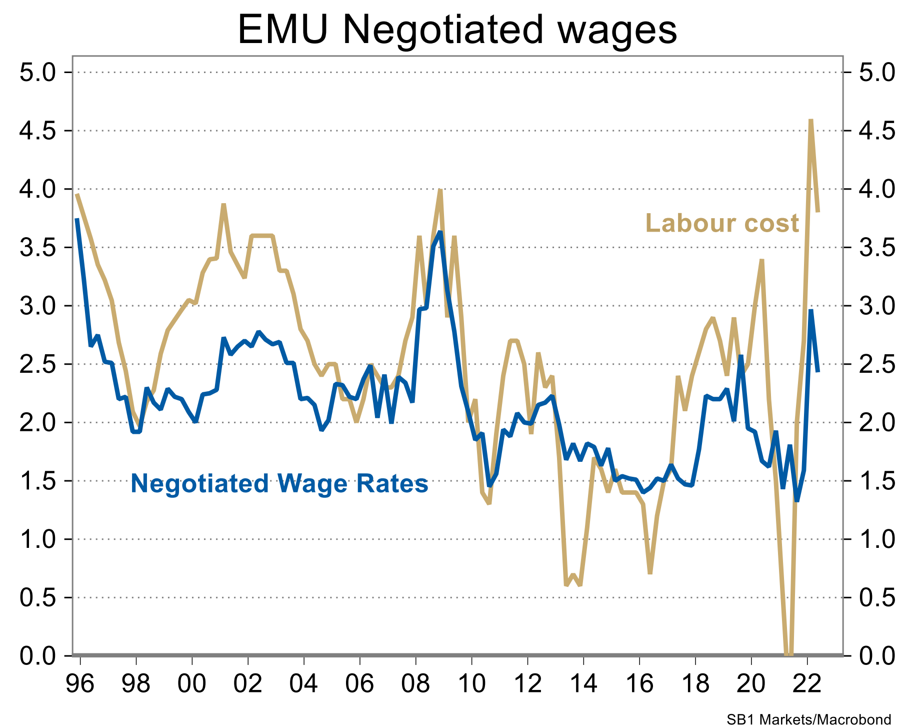


- More details in the final numbers

Europe does not have a wage problem, at least not so far

Wage inflation remains in check, even measured by negotiated wages

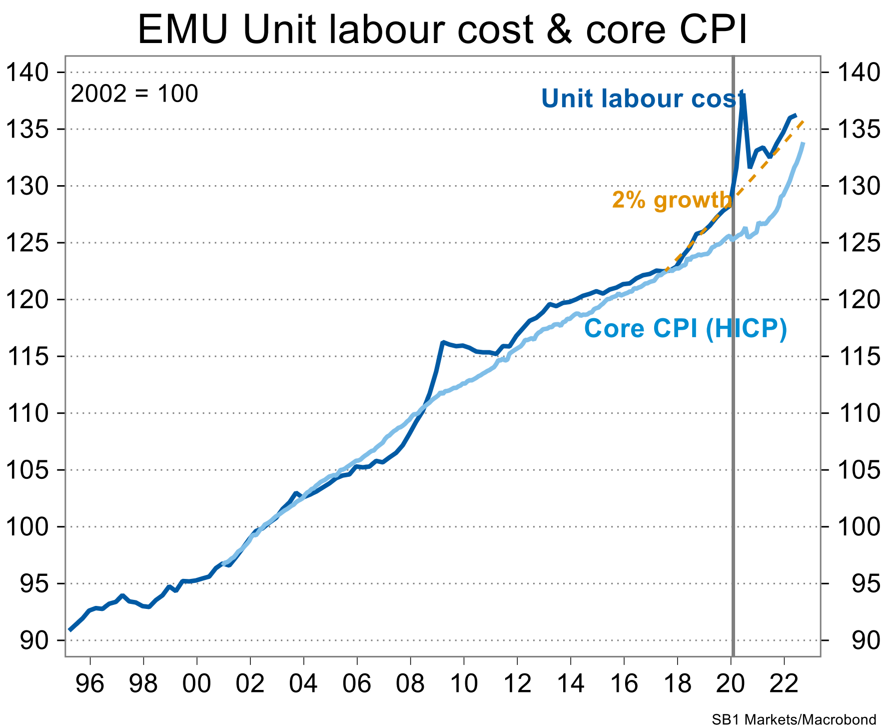




- The current 2.5% growth path used to fed into a CPI inflation of around 1.6%, before the pandemic. However, productivity growth has slowed, and Unit Labour cost inflation has accelerated, but remains muted, check next page
- Negotiated wages were up 2.4% y/y in Q2, confirming that there is no take off in wage inflation

Unit labour costs have accelerated but are but still close to a 2% trajectory

Wage inflation has not accelerated but productivity growth has slowed during/after the pandemic



- **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% – and a 2% ULC inflation will <u>over time</u> yield a 2% CPI inflation

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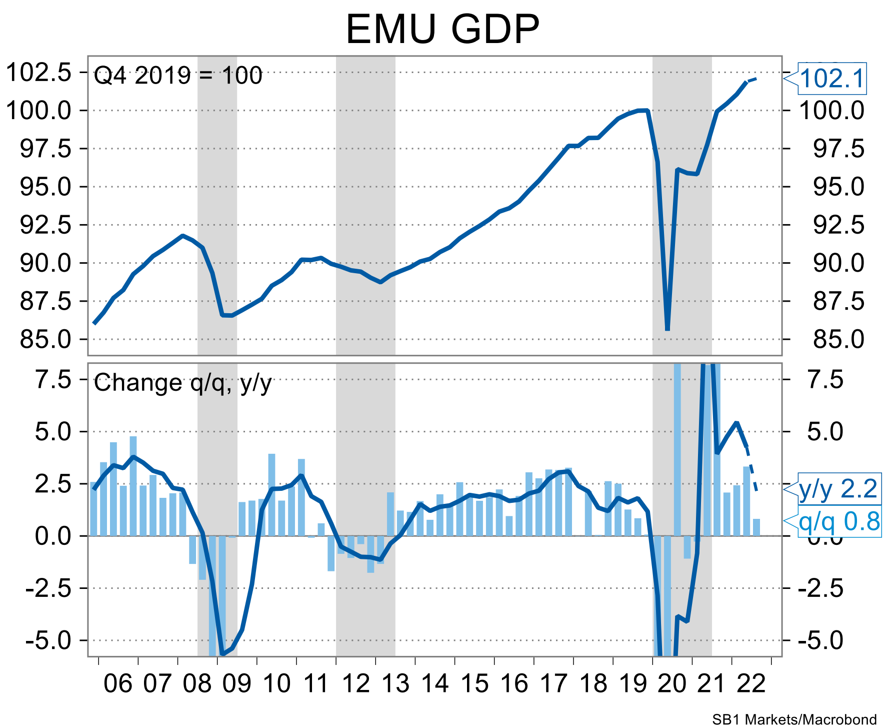
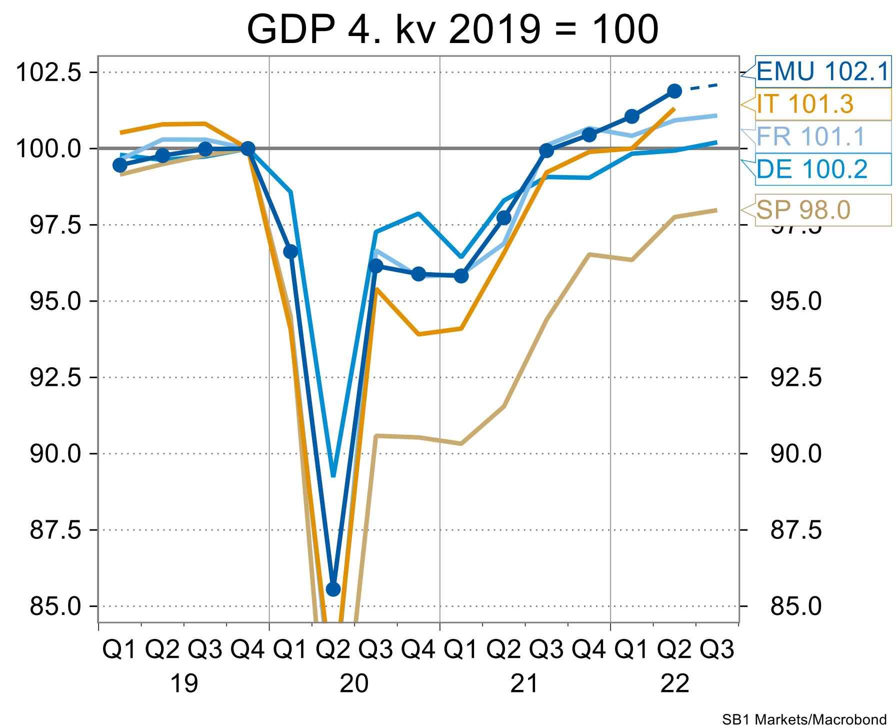
Q3 GDP better than expected but not impressive, of course, up 0.8% (annualised)

GDP marginally up in both Germany, France and Spain, EMU in sum up 0.2%, if Italy does not disap.

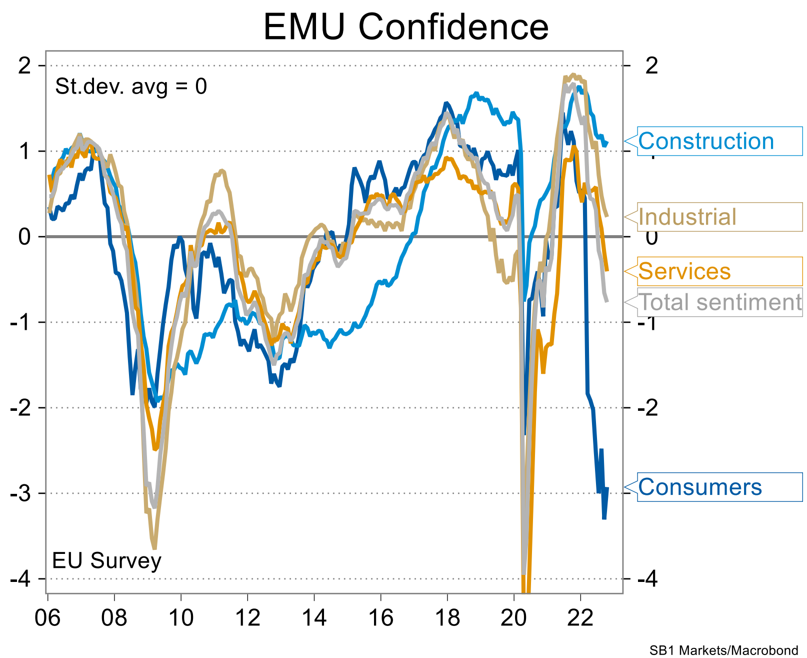


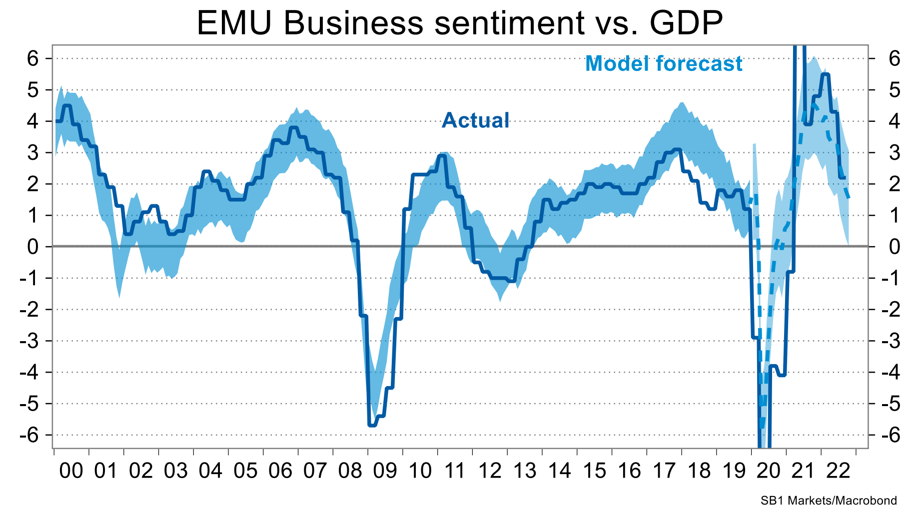


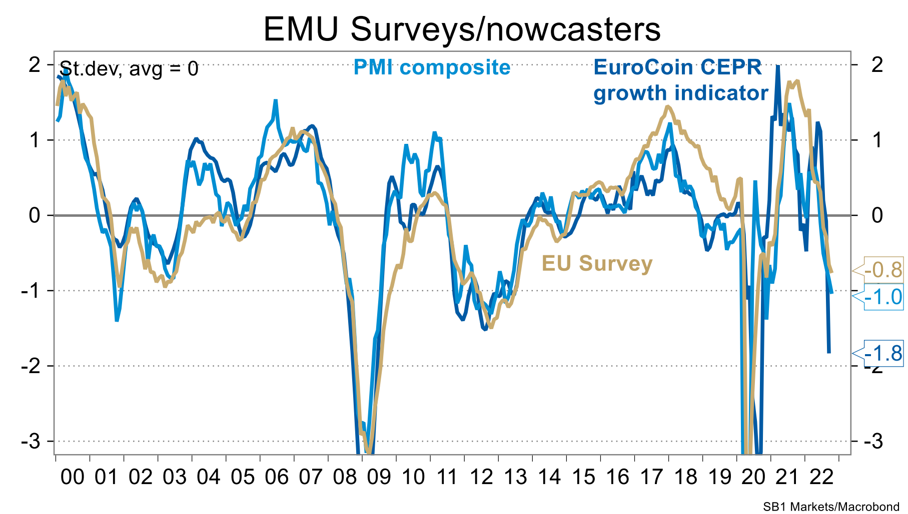
- German GDP up 0.3% (not annualised), expected -0.3%
- France + 0,2%, as expected
- Spain +0.2%

Economic sentiment further down but businesses are still reporting growth!

The overall index fell 1.1 p to 92.5 in October. Consumer confidence up but remains at -3 st.dev







- **The Economic sentiment index** is 0.8 st.dev below average, with a large contribution from households. Businesses are on average above (+0.1 st.dev) – but surely rapidly on the way down, and the service index fell fell further to 0.4 st.dev below average
- Thus, even if there is war nearby and inflation is surging, businesses are still reporting growth marginally above trend. Consumers are pessimistic but historically their views on the economy has been irrelevant vs. GDP growth, just businesses tell us something relevant, at least vs GDP
- **All of the surveys we follow are now signalling growth at (or mostly) below trend,** or an outright recession (like the EMU PMIs, and CEPR's EuroCoin GDP indicator

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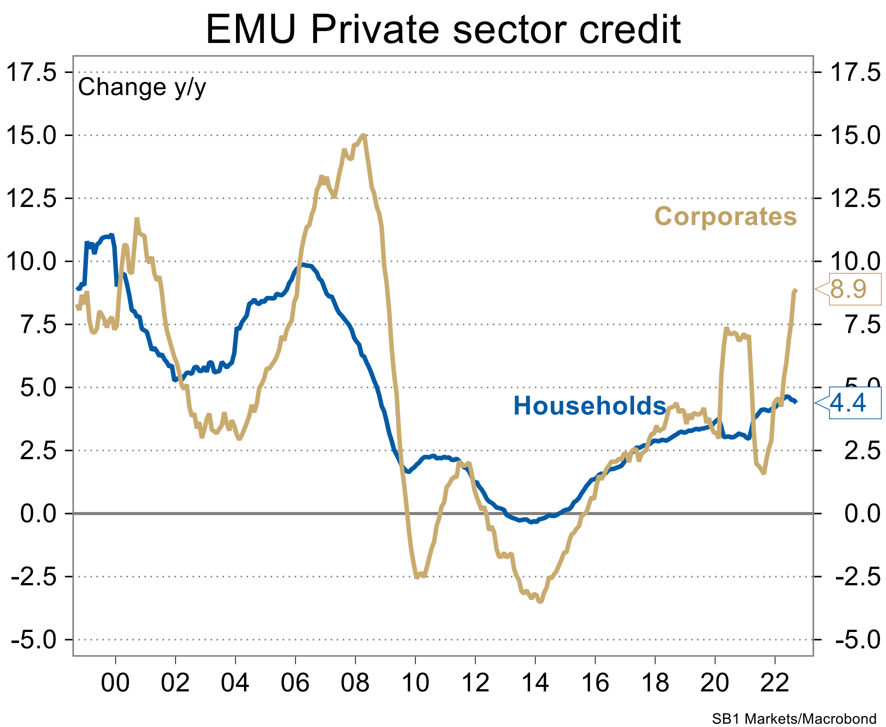
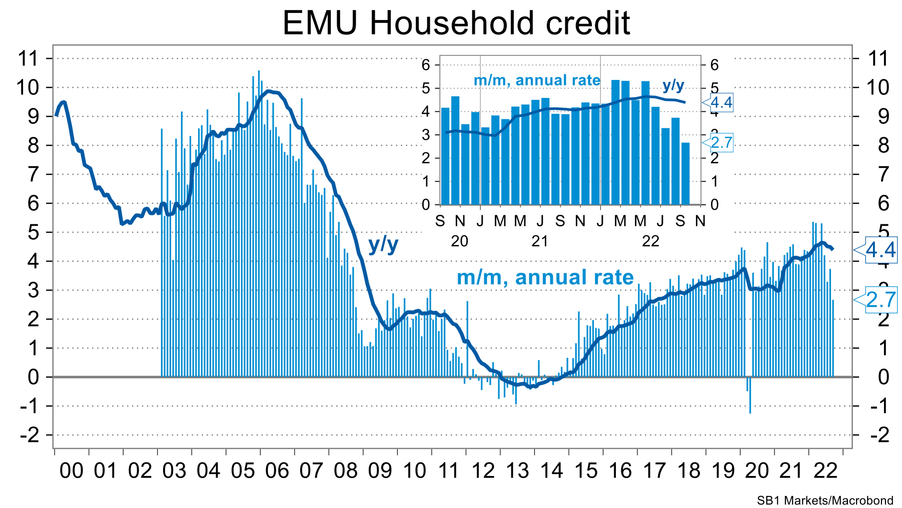
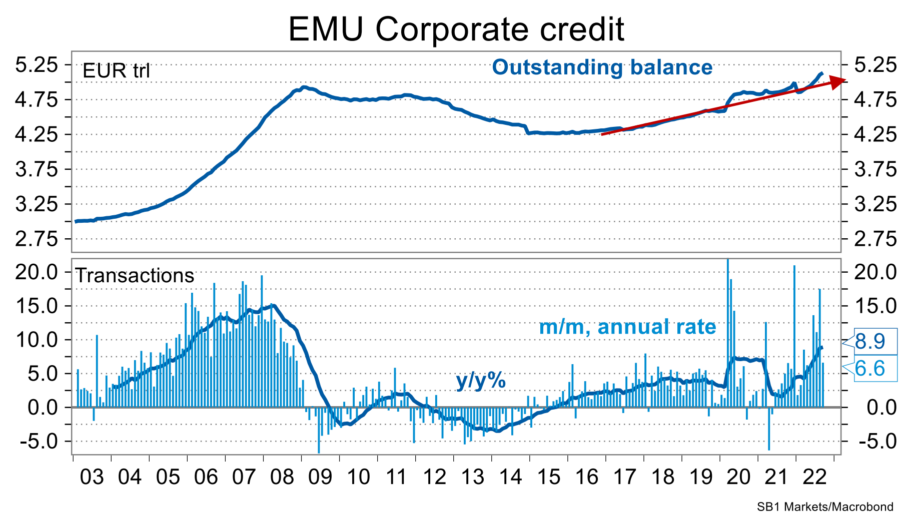
Corporate credit growth has accelerated sharply. A good sign, or not?

Household credit demand is clearly softening



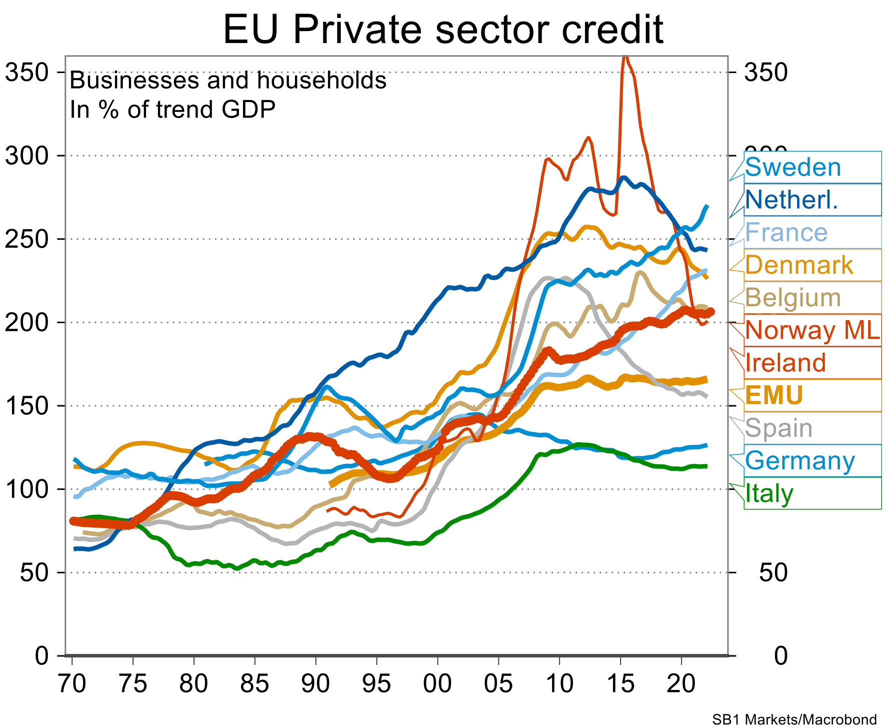


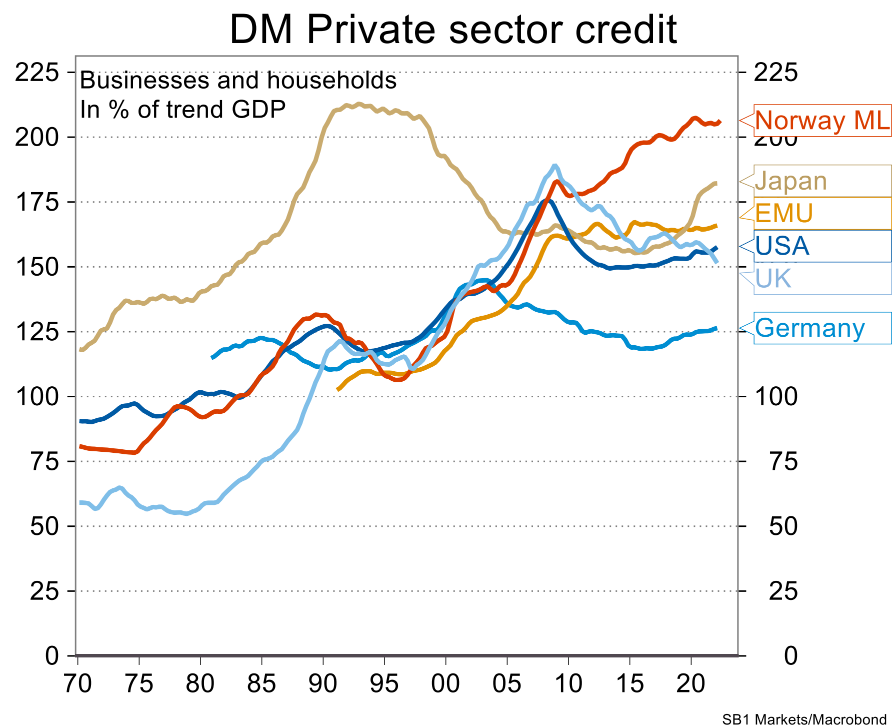


- **Annual growth rates** at 4.4% – 8.9% are well above <u>normal</u> nominal income growth. Now, incomes are growing much faster due to high inflation (=income for the corporate sector) and strong growth in employment, out of the pandemic
  - » The **corporate debt** level is above the pre-pandemic trend growth path, as is **household debt**
- Household credit growth has slowed significantly since June. A warning sign? Are corporates borrowing to fund investments or to finance deficits? So far, profits have been OK, in aggregate, that is
- The last **banking survey** shows that European banks are tightening their standards, especially vs. households. Check the next page

The private sector has mostly been deleveraging since the Financial Crisis

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





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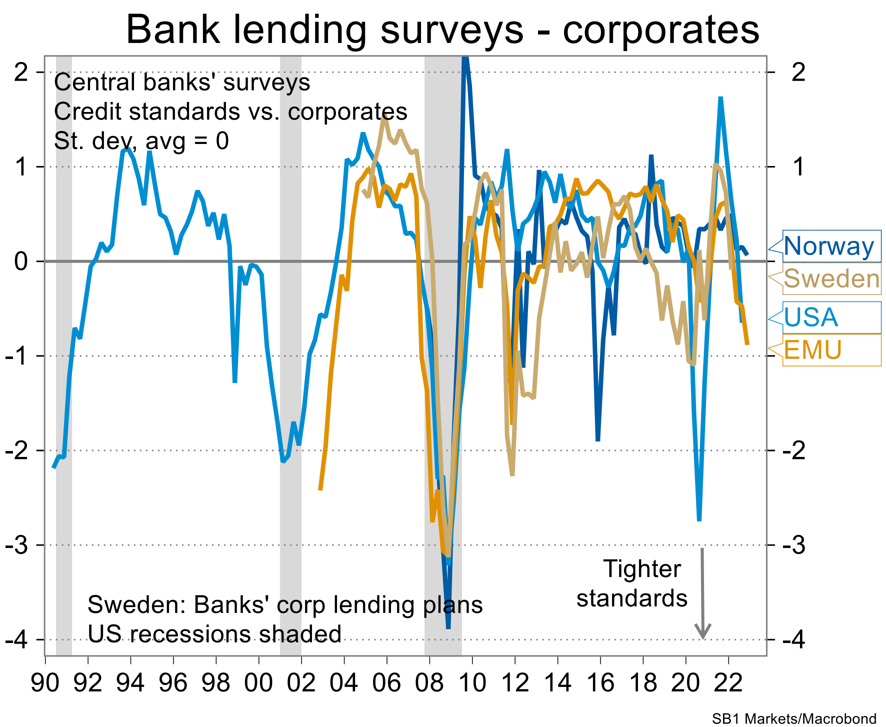
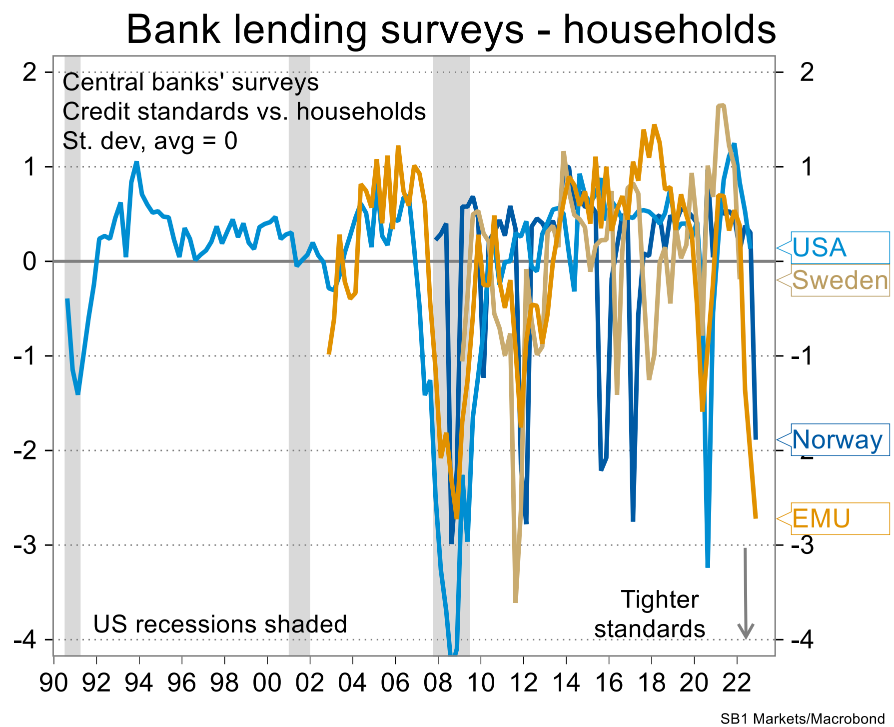
European banks report tighter standards both vs. households and businesses

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

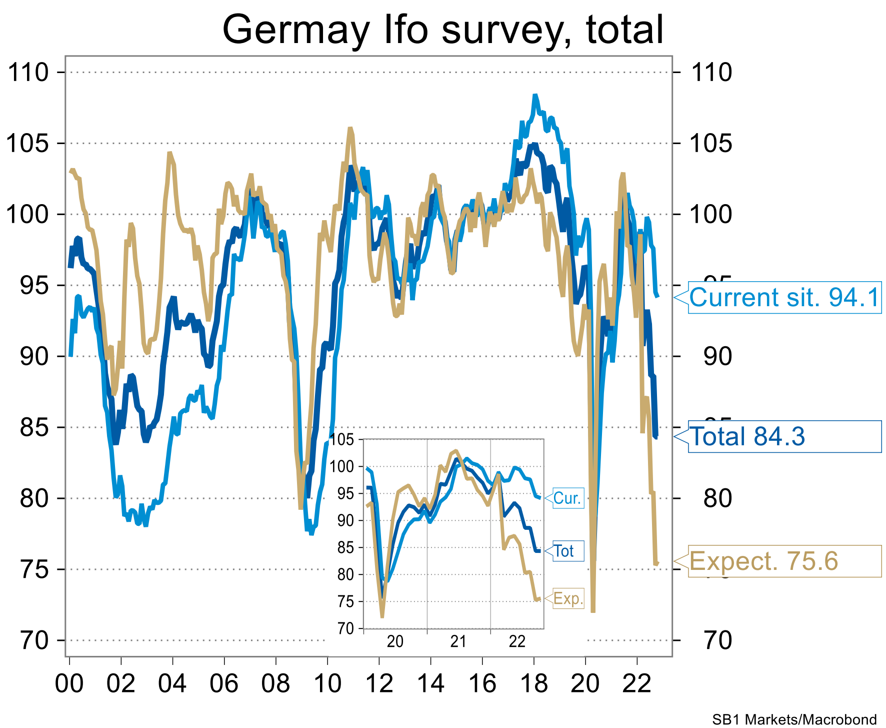


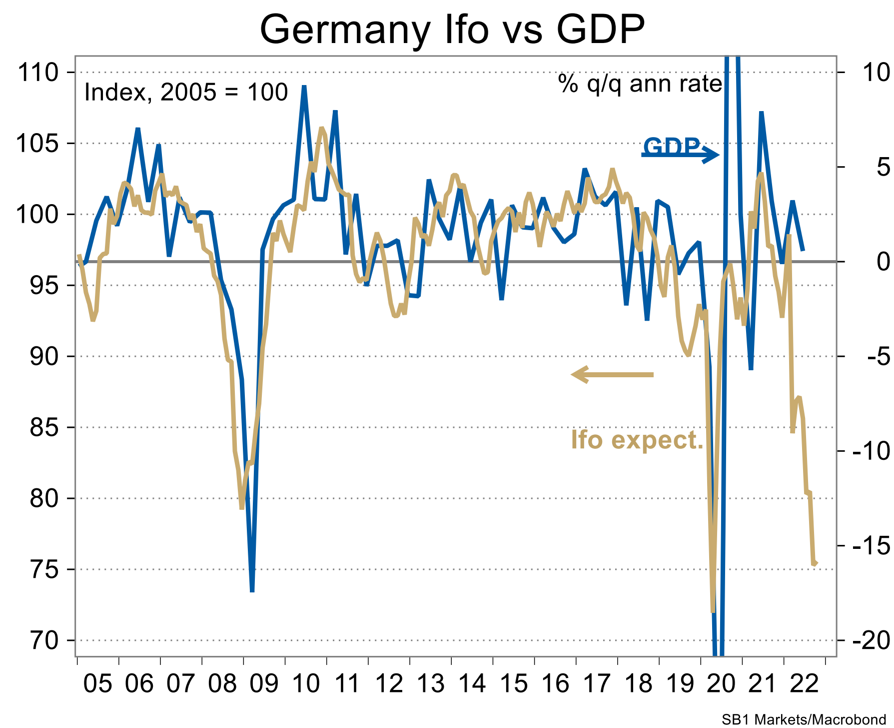


- EMU banks are now more reluctant to offer loans to the businesses
- **US banks** are signalling tighter lending standards vs corporate sector but not vs households, whereas the opposite is true for **Norwegian banks** according to the lending survey two weeks ago

Ifo expectations above expectations in October – sentiment is still dire

The index was up 0.3p to 75.6, but still signals a substantial fall in GDP. Consensus was 75.0



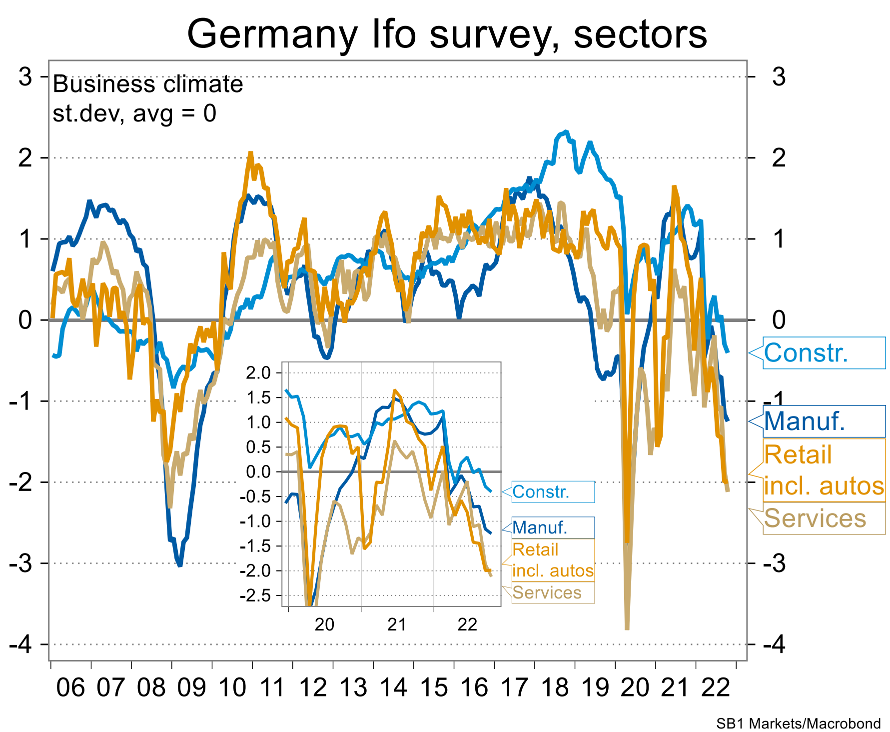


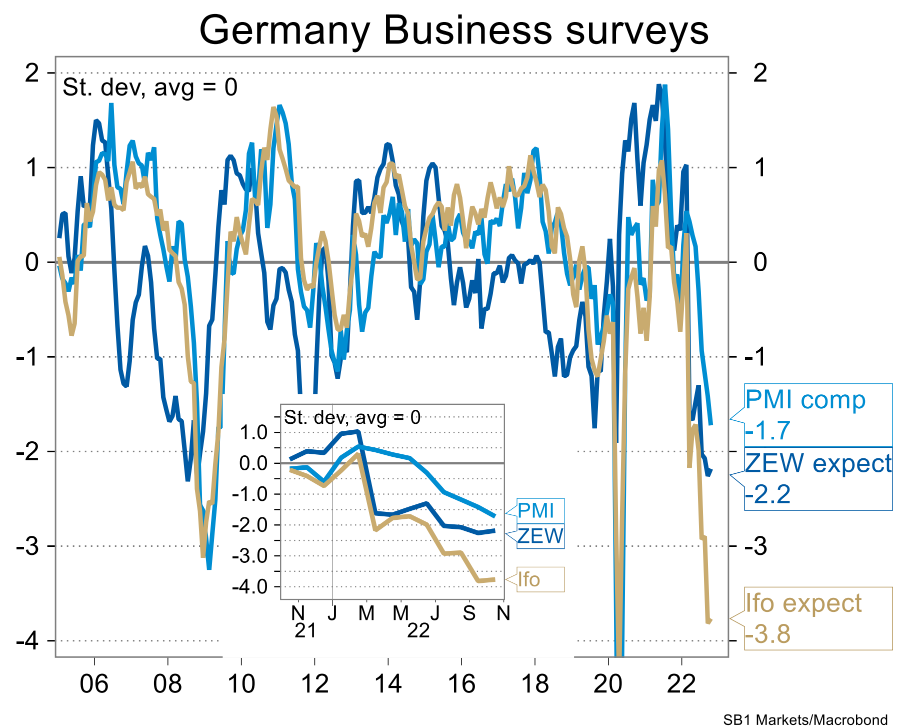
- **The expectation index** rose by 0.3 p to 75.6, 0.6 p better than expected. The level is very low, at 3.9 st.dev below average, lower than the lowest print during the financial crisis. The correlation to GDP is not perfect but a huge decline in GDP is signalled, at a 16% pace! The energy crisis is no doubt the main reason for the sharp deterioration of business sentiment
- The **assessment of the current situation** was down 0.4 p to 94.1, which was 1.7 p above expectations. The level is around average – signalling a normal growth rate. The problem is the expectations
- The **total Ifo business climate index** fell by 0.1 p to 84.3; expected 83.3

Business climate: the average of the current situation and expectations

3 out of 4 sectors report of weaker business climate in October, retail marg. up

And all sector indices are below average

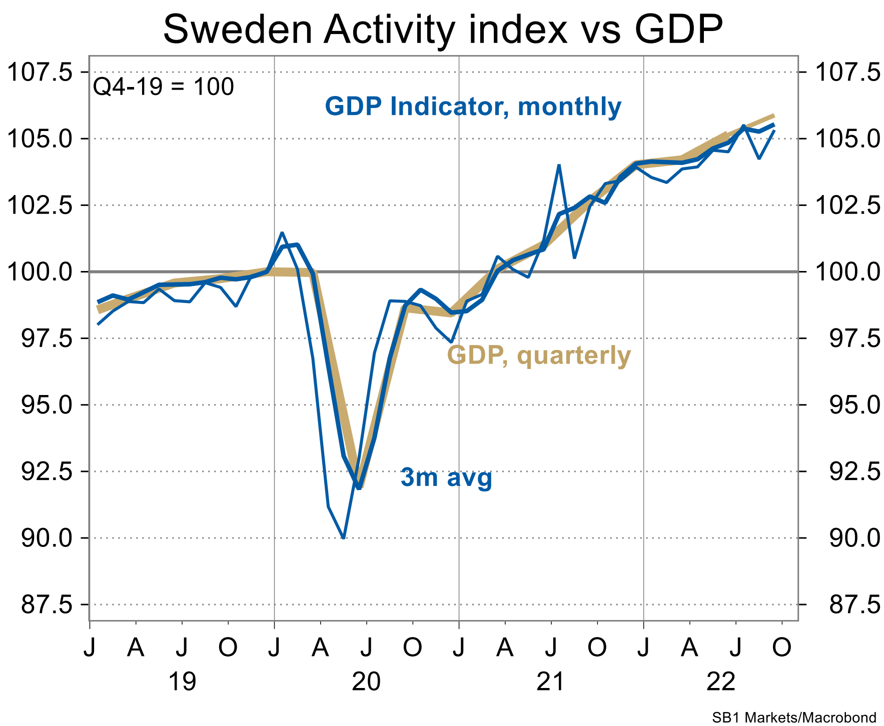


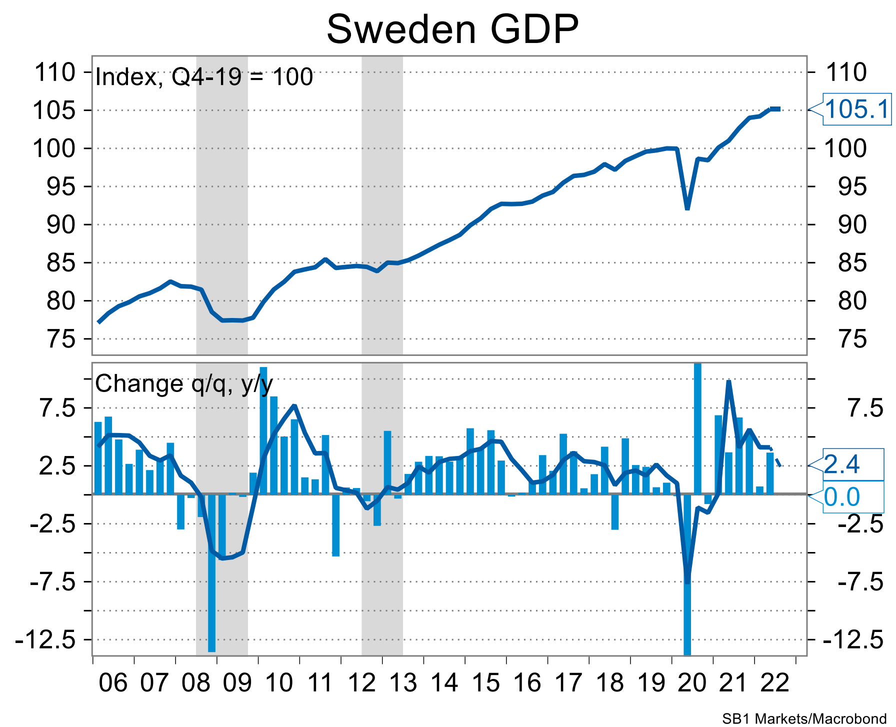


- Only the Retail sector reported that the business climate had improved marginally
- Other surveys are also well into negative territory, signaling slower growth/fall in output in the coming months

Swedish GDP unexpectedly reversed the 1.3% August dip in September, up 1%

Sept was expected down 0.2%! Q3 up 0.7% (2.8% annualised), expected up just 0.1%!

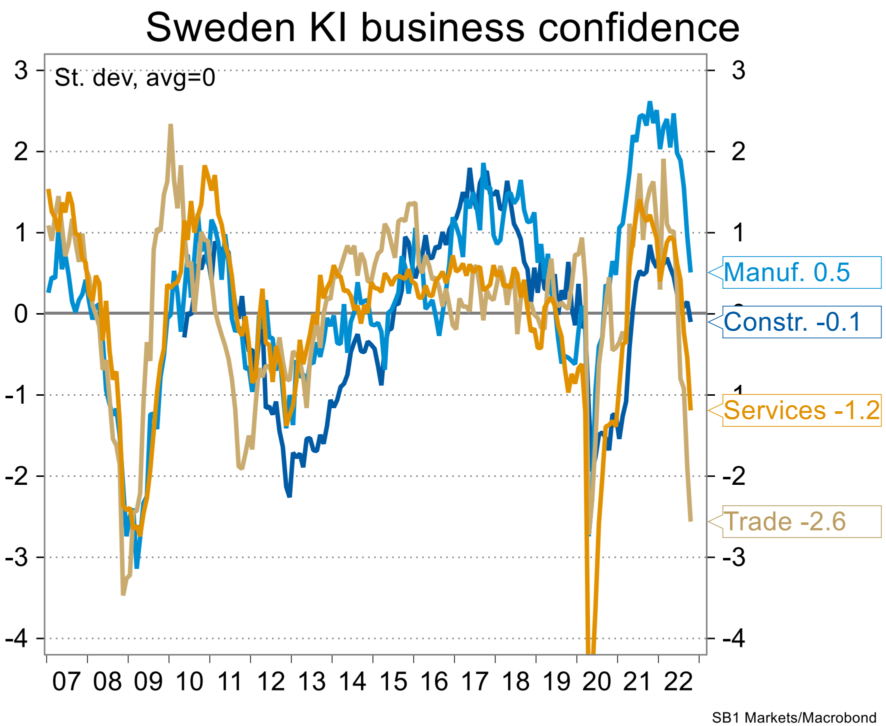


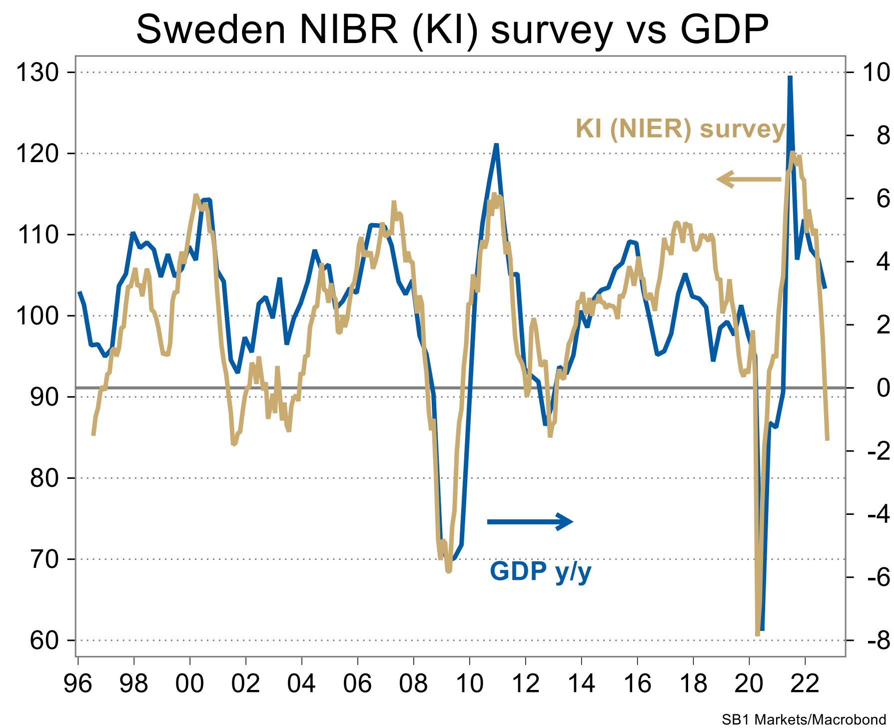


- **Still, growth is probably slowing**
- **The outlook** is weakening, according to Swedish companies. The KI (NIER) survey has fallen to 1.5 st.dev below average, signalling a 2% GDP contraction, check next page

Business confidence deteriorated further in Oct, a decline in GDP is signalled

Confidence in the manufacturing is still above average, other sectors are below. Trade at the bottom





- **The composite index** fell to 84.6 in October from 90.8 in September, probably more than expected. The decline equals a 0.6 st.dev decline to 1.5 st.dev below average. The index signals a 2% GDP contraction, down from +2% in August. The Riksbank expects a small increase in GDP in Q3 (q/q) but then a 0.9% (total) decline in Q4 and Q1
- **4 out of 4 main sub-sectors** are reporting declining confidence, and just manufacturing still above average
  - » The **trade sector confidence plummeted** in Sept, and is now 2.5 st.dev under water
  - » The **manufacturing sector sentiment** has declined over the past three months, however, manufacturing sector sentiment remains above average, **construction** is jus below par – but is probably exposed due to the turnaround in the real estate market
  - » **Services** are at -1.2 below average

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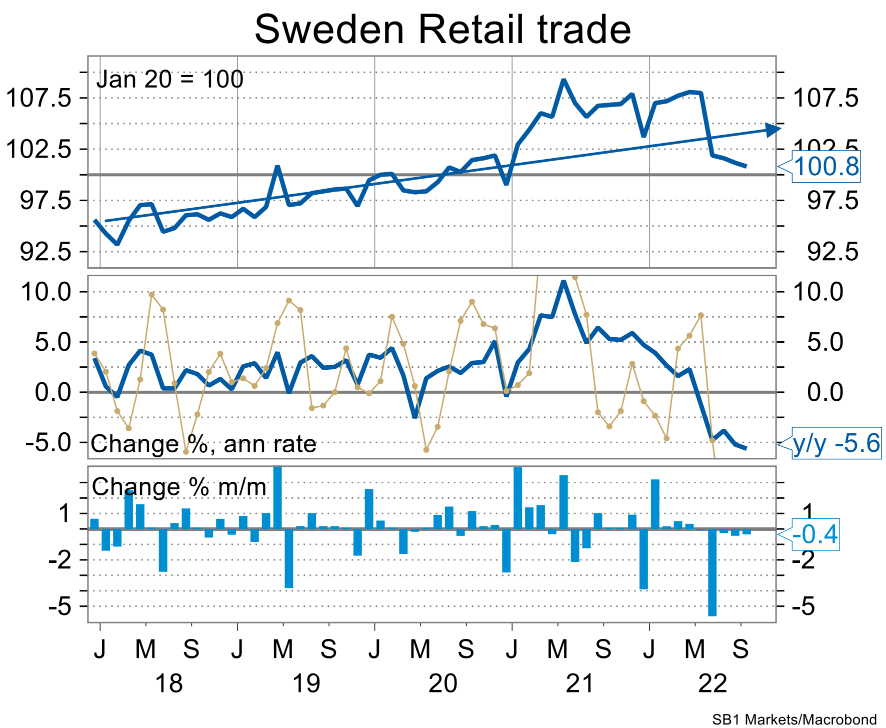
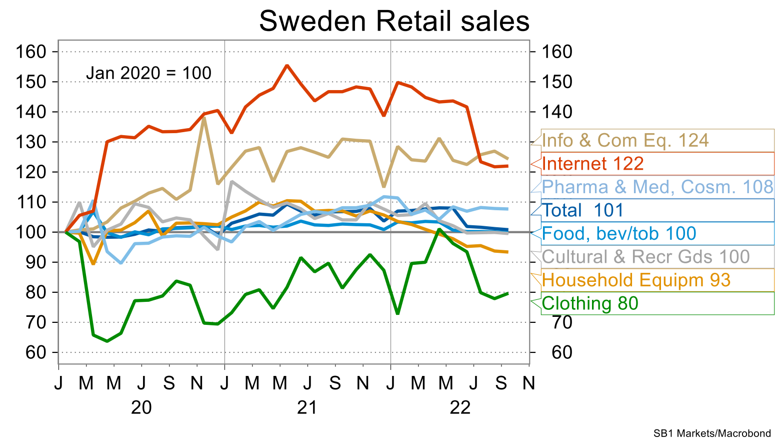
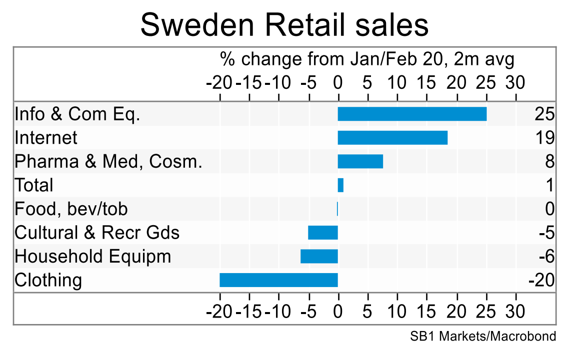
Retail sales down for the 5th month in September, down 5.6% y/y

Sales are now ‘just’ 0.8% higher than before the pandemic, and well below the pre-pandemic trend



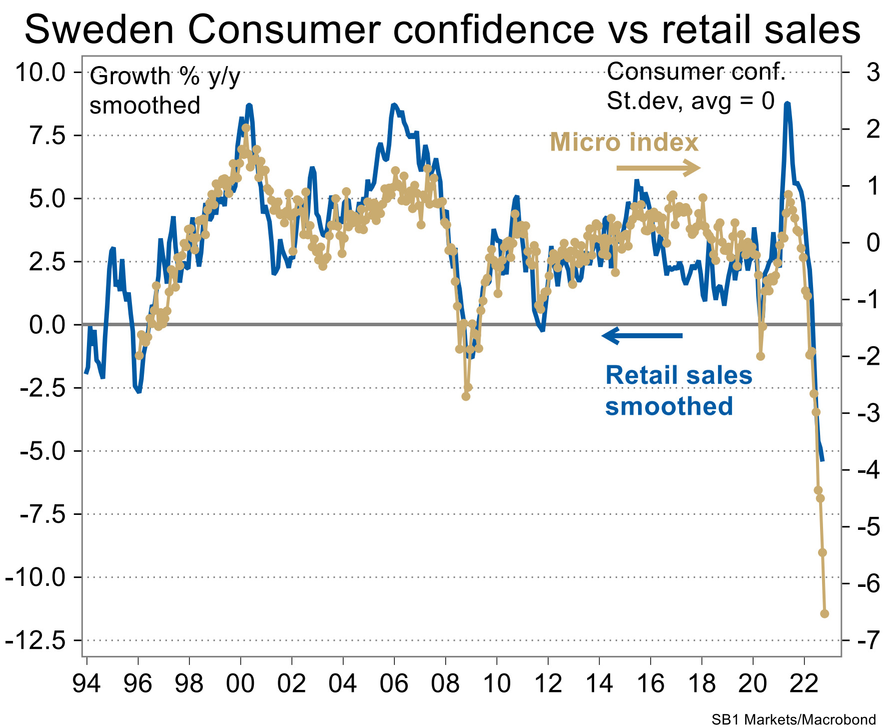


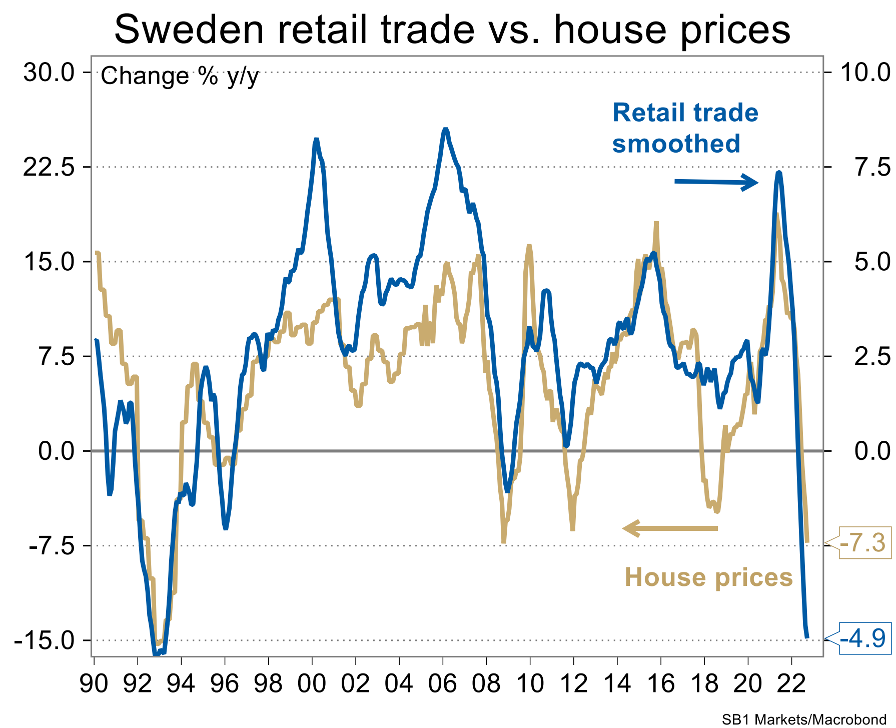


- **Sales fell 0.4% m/m in September**, following the 0.4% drop in August. Sales are down 6.7% from the peak last spring – and the underlying trend is down
- **The fall in retail sales is broad**: all sectors are down from the peak, even pharma. Clothing and internet sales have fallen the most

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

House prices and retail sales down in tandem with consumer confidence

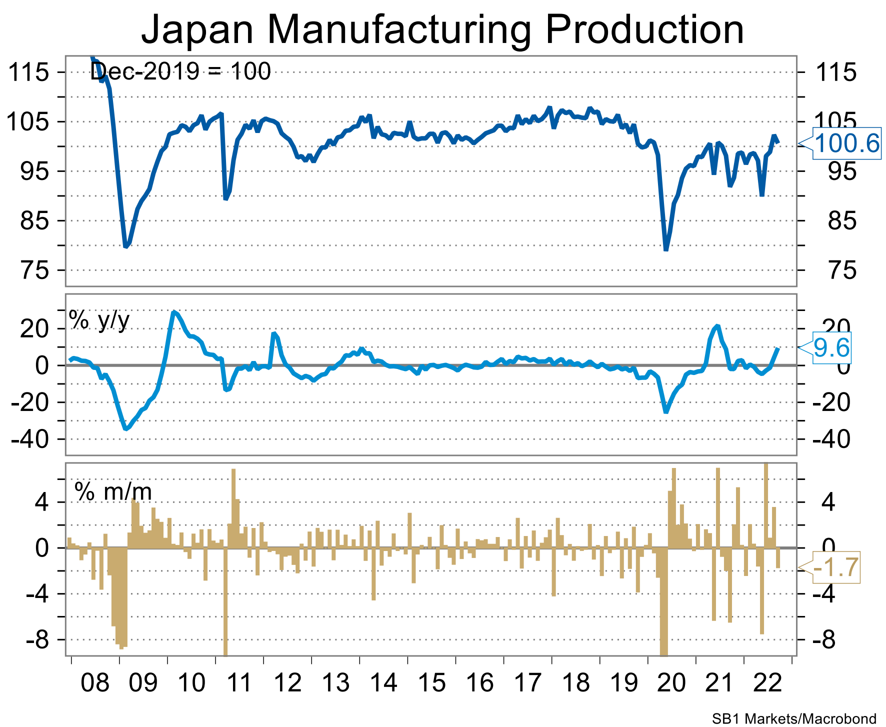


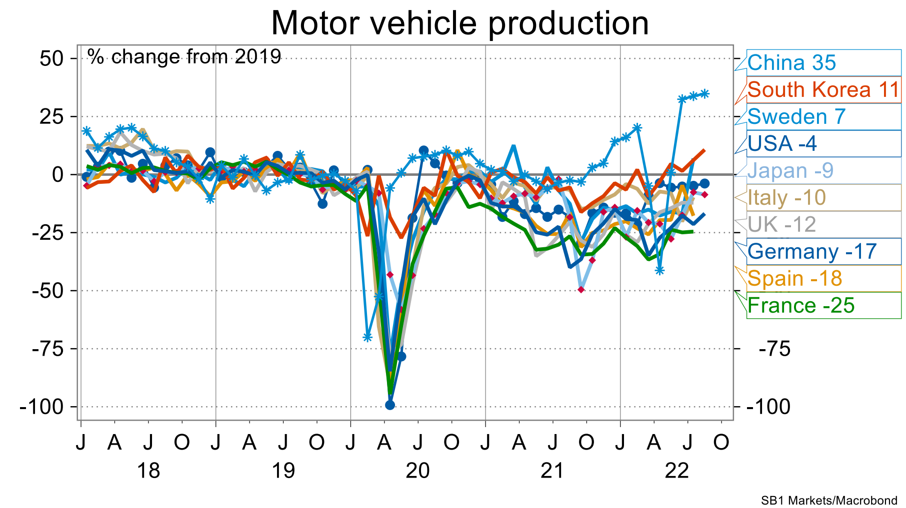


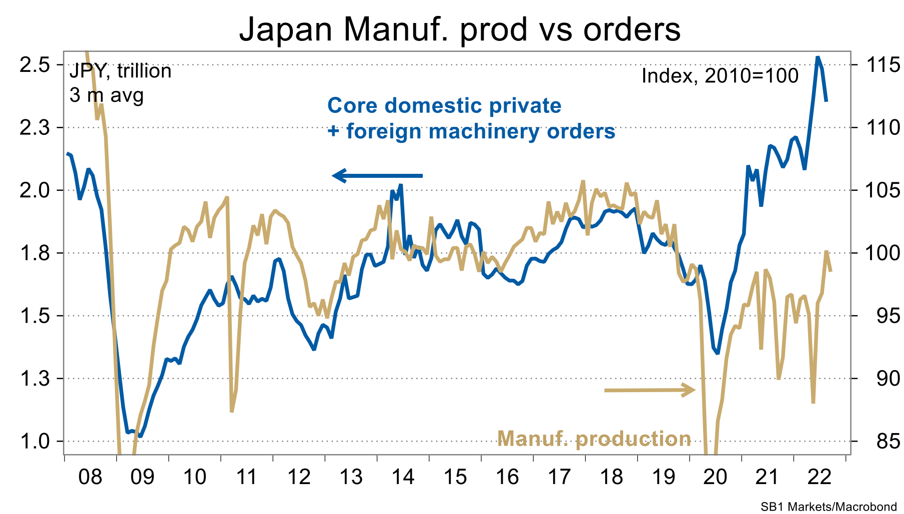
- **Consumer confidence** (the micro index)) fell to 35 in Oct from 44.8 in Sep, a 1 st. dev. drop, to -6.5 st.dev below average – which is a rather remarkable observation, we would say
  - » The **macro index** was also down, to 2.4 st.dev below average, just marginally down. The total confidence index fell 0.4 st.dev., to -5.2, the lowest ever
  - » Both **retail sales** and **house prices** have fallen alongside the decline in consumer confidence – higher rates and high inflation is softening both sentiment and ultimately demand - the outlook is rather bleak

Manufacturing production down 1.7% in September, expected -1%

… following the 3.5% lift in August, and the trend is up



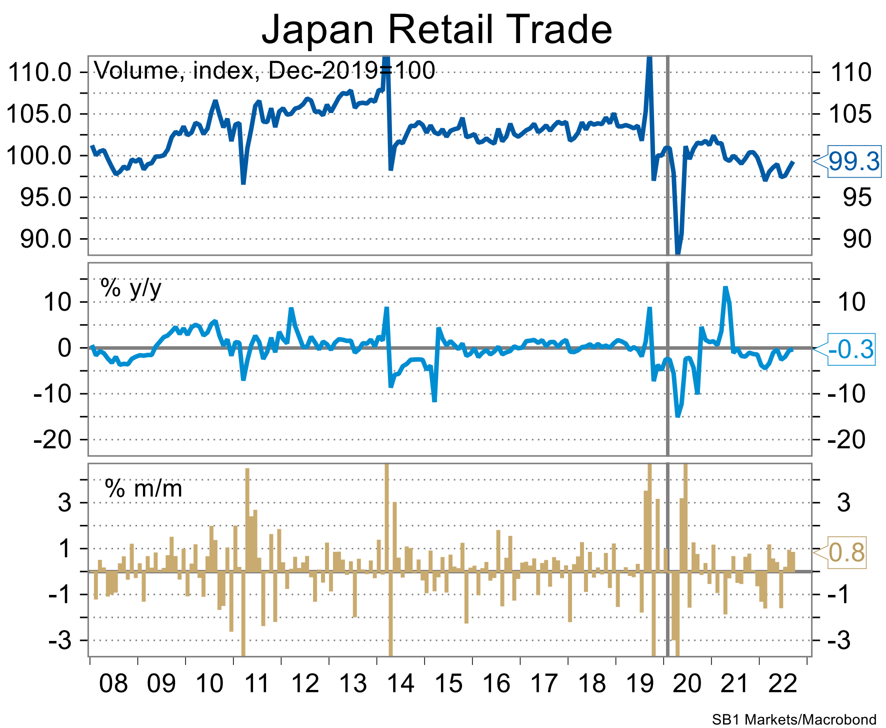


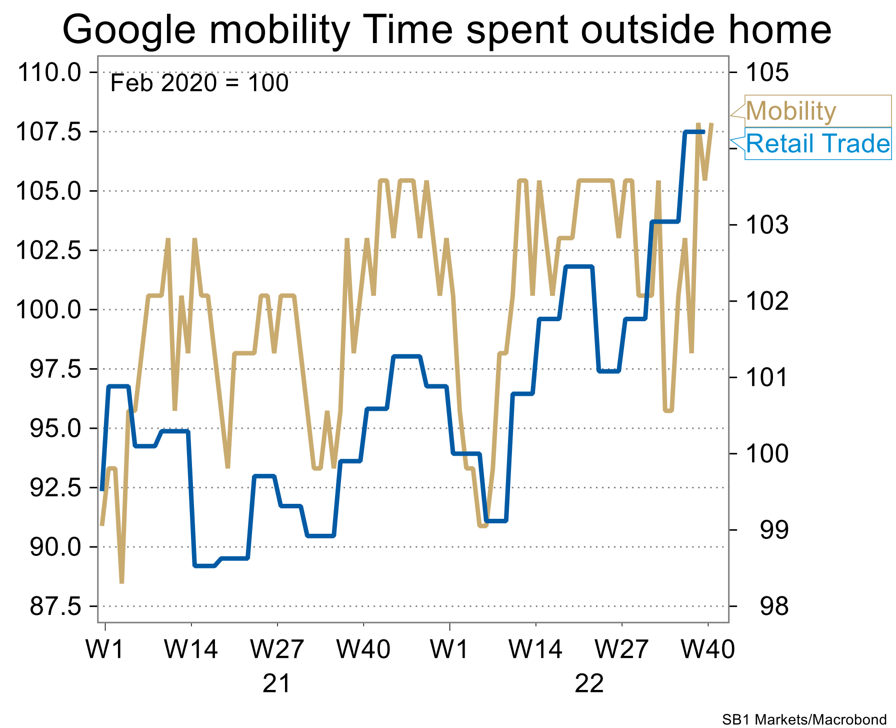


- **Production** fell due to a Covid wave and imposed restrictions in May but has since recovered, and it is even higher than before the pandemic
- **Overall order inflow** has strengthened substantially through 2021, and into 2022. The declining JPY explains at least part of the increase, probably also higher prices

Retail sales rose further in September – the trend since the spring is flat

… but the level is still very low. Sales up 0.8%, twice as much as expected, down from 1% in Aug





- Still, sales are down 0.3% y/y, and well below the level in 2019

Highlights

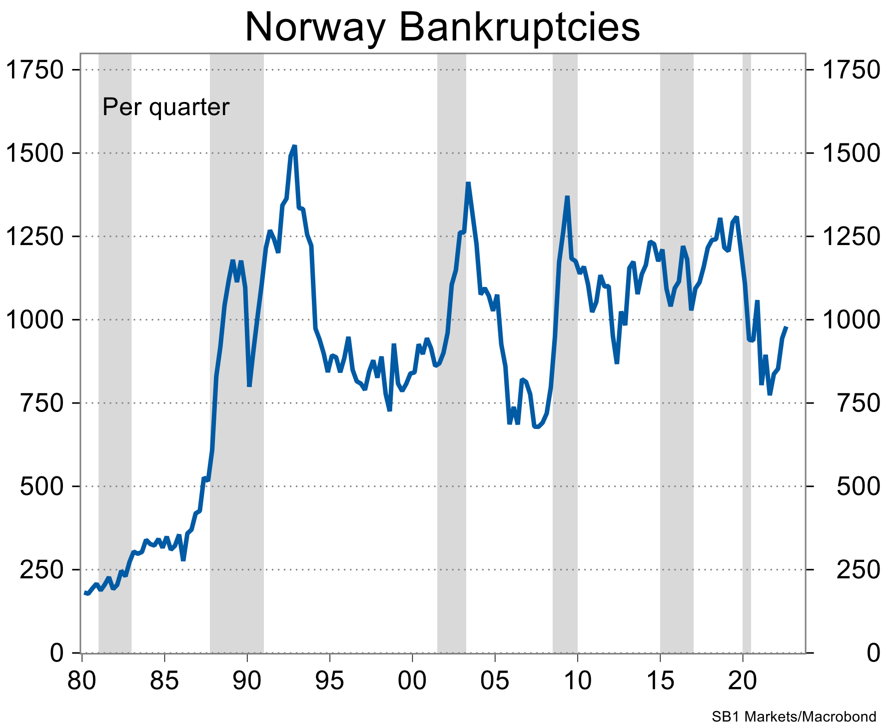
The world around us

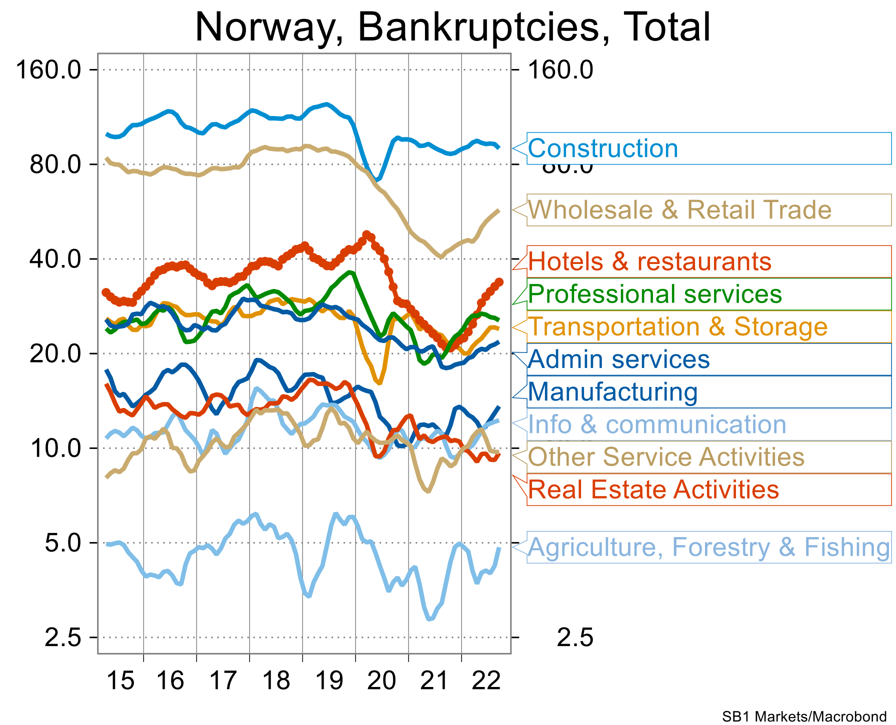
The Norwegian economy

Market charts & comments

Bankruptcies up in Q3, but still far below the pre-pandemic level

More bankruptcies in trade, and hotel & restaurants but both below the pre-pandemic level

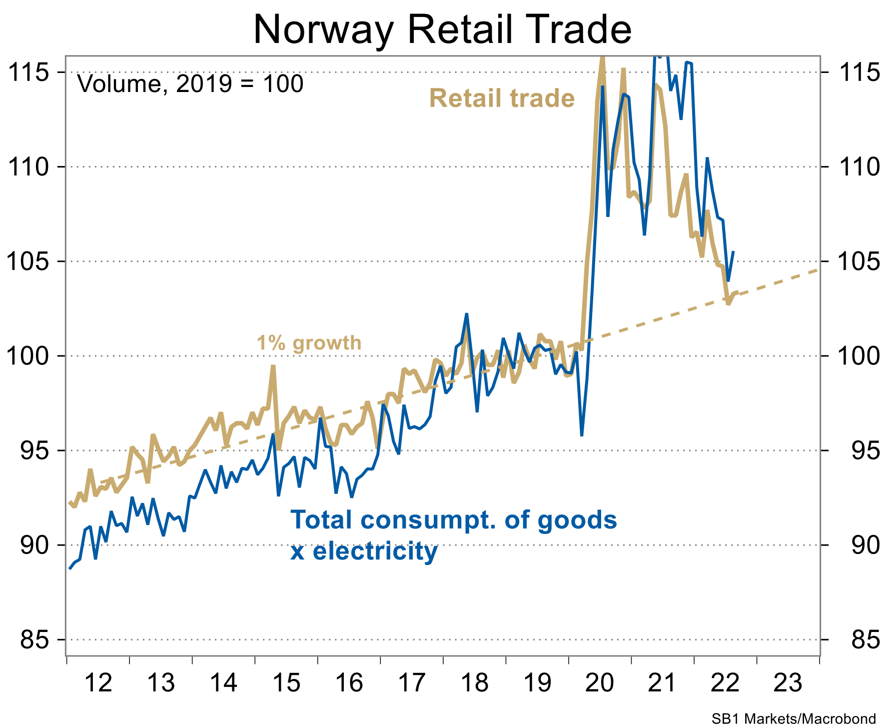


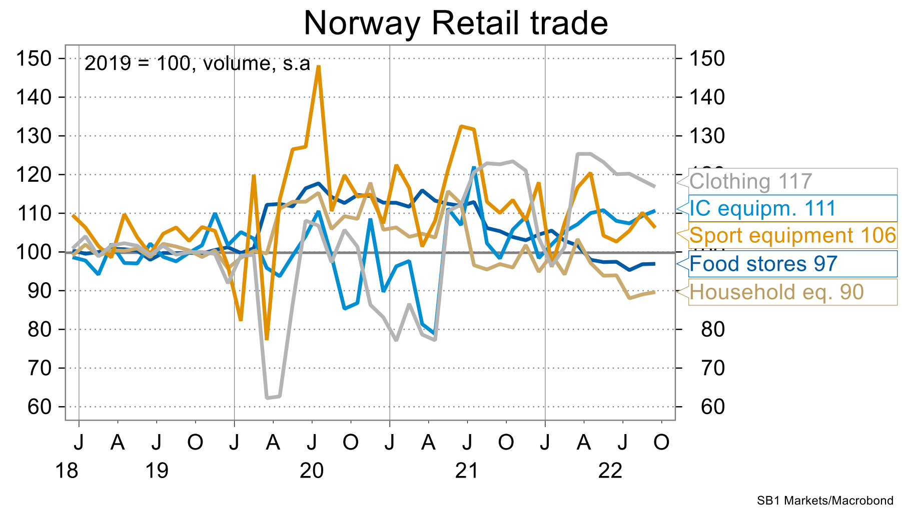


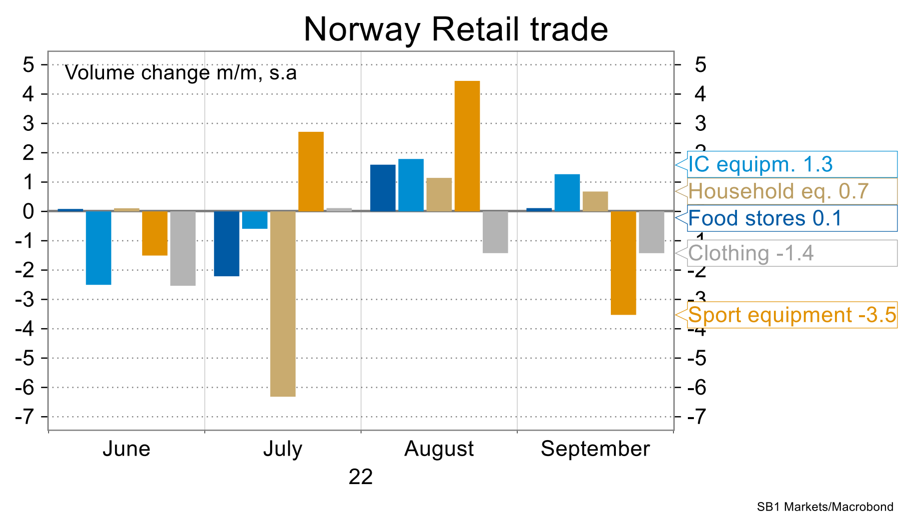
- The energy price ‘crisis’ has so far not pushed many companies into financial hardship, at least not into bankruptcy

Retail sales stronger than expected September (too) but the trend is down

Retail sales were up 0.1%, we expected a substantial decline. Sales fell at 2% pace in Q2



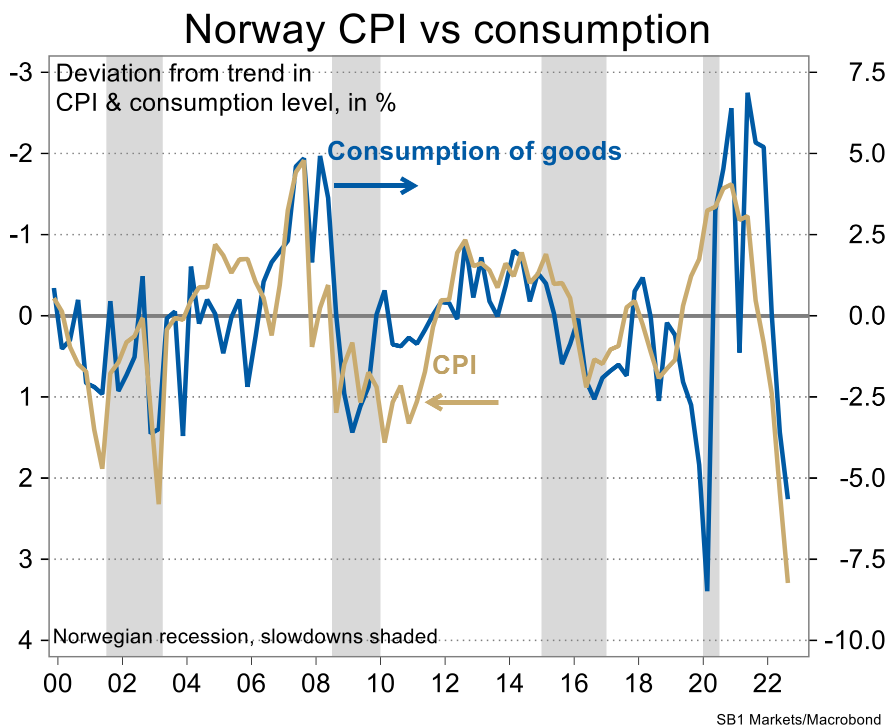




- **Retail sales** are down 4% y/y, and by almost 11% from the peak, early in the pandemic. Sales are close to the weak 1% pre-pandemic growth path
- Very likely, the lift in inflation and higher interest rates have aided sales back down to the pre-pandemic trend – and we expect sales to fall below the trend the coming months/quarters
- Sport equipment fell the most in September (following an even stronger April). All main sectors ex. ITC are heading down

Higher consumer prices contribute to lower consumption, as always

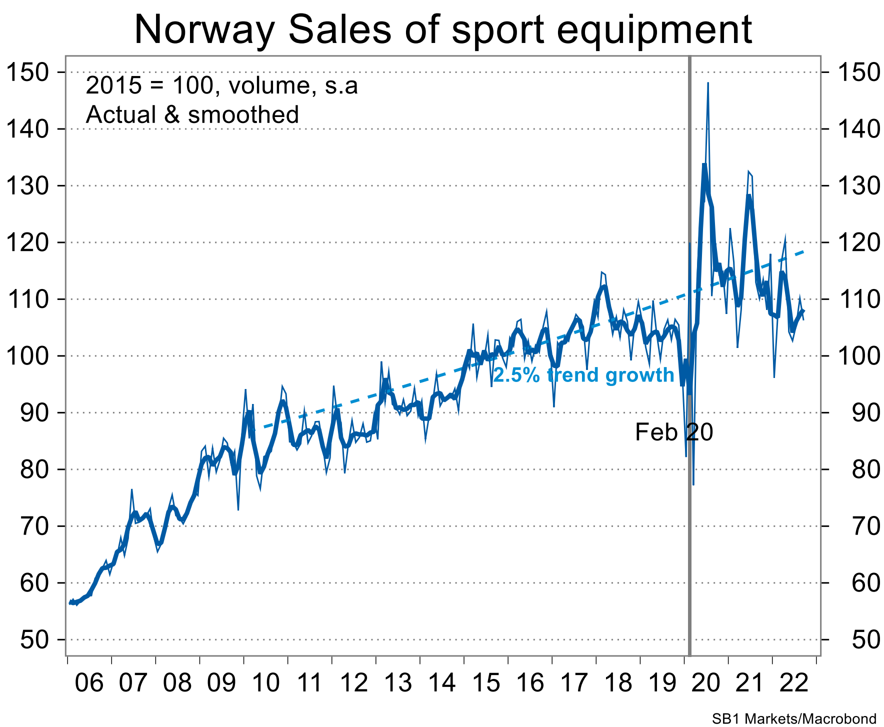
Consumption of goods (volume) are negatively correlated to changes in consumption prices



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

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

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



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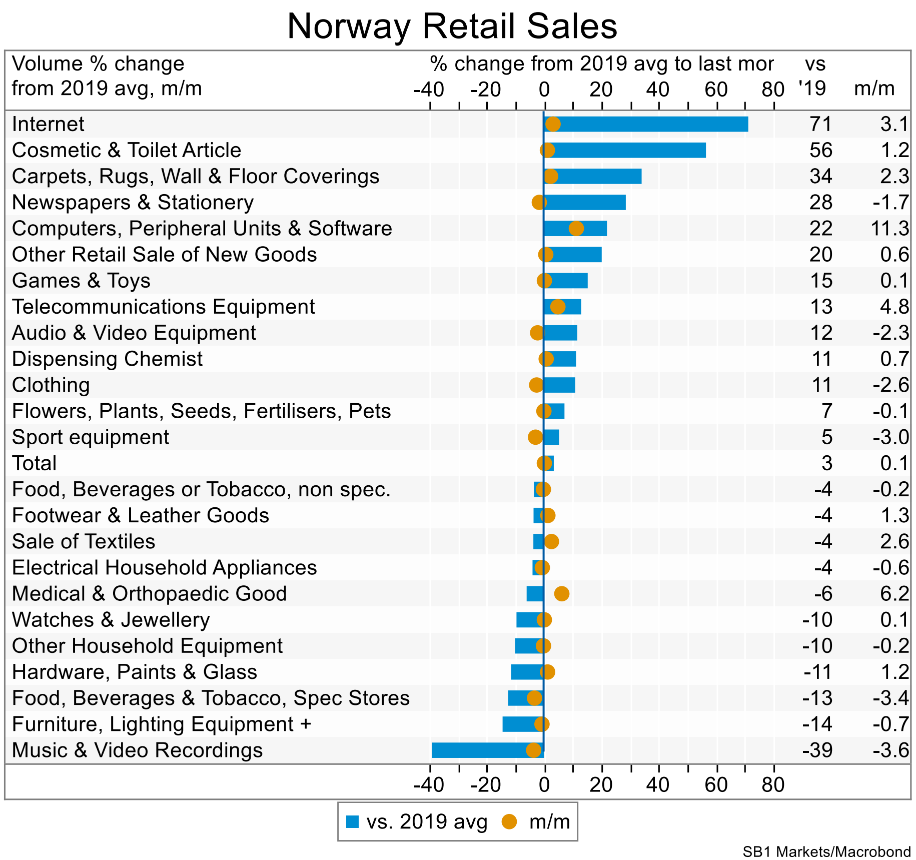
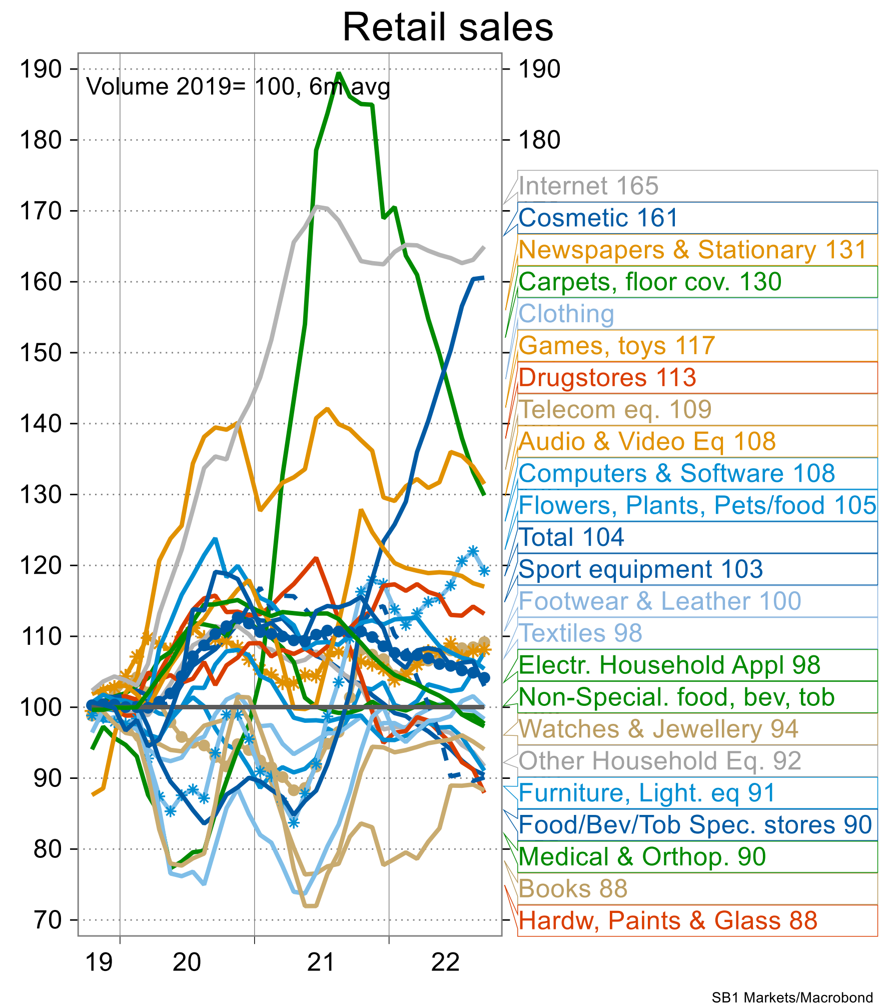
Since before the pandemic: Still huge sectoral differences in sales volumes

Cosmetics, Internet sales at the down. Home refurbishing still strong but down by 1/3 from the peak

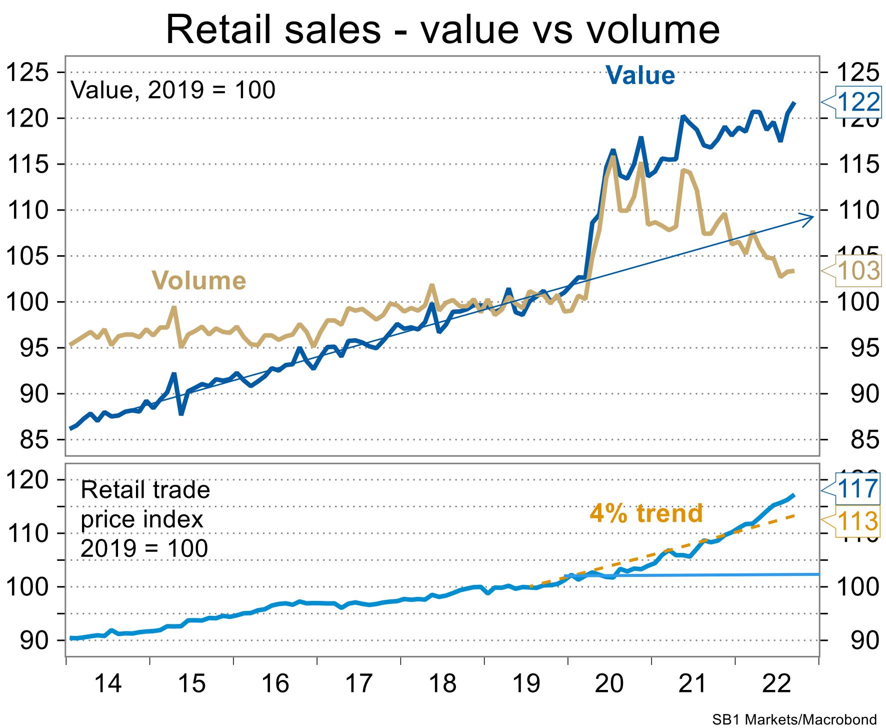


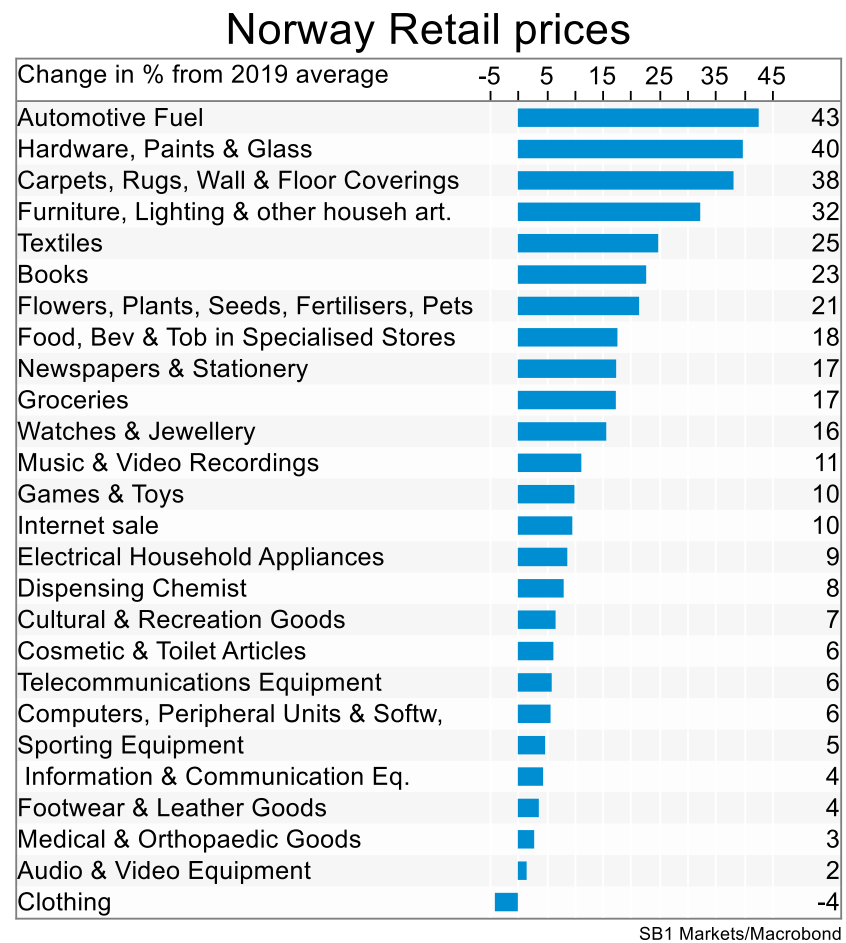


- The losers were mainly losers before the pandemic too
- Where is the risk now
  - » Guideline: Start at the top of the list.
  - » There are excuses, but probably not that many

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

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



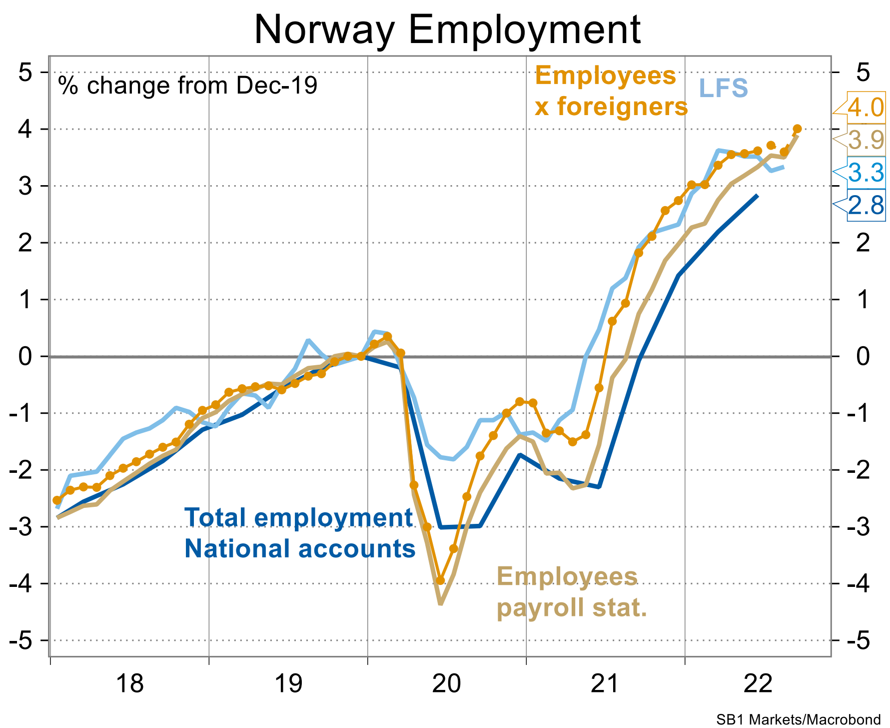


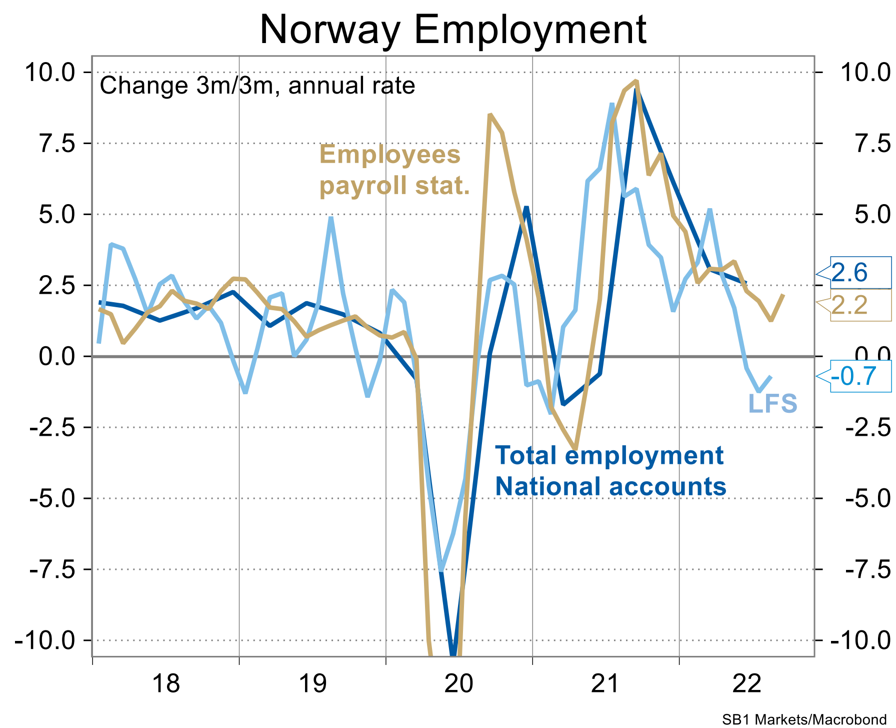
- Retail sales, measured in value terms, are 18% above the 2019 level and close to 10% above the pre-pandemic trend
- Huge differences is **price changes**:
  - Gasoline up 38%, floor coverings, hardware (building materials) are up 38% – 40%, furniture 31%
  - Close to the bottom of the list: Sport equipment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

SpareBank 1 MARKETS

Employment growth is calming down, and LFS employment is declining

Though, the no. of employees rose by 0.4% in Sept. Wage inflation revised down and is moderate

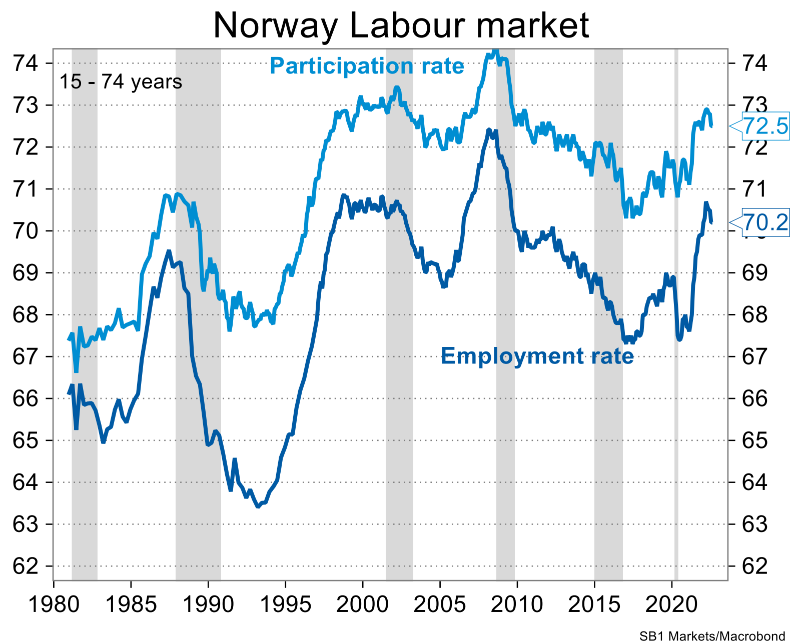


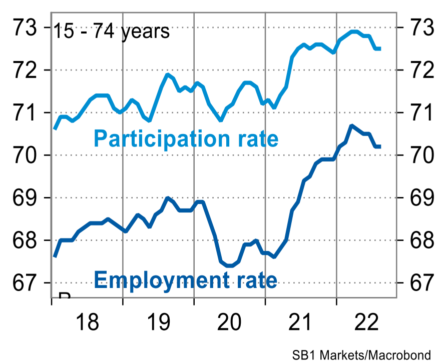


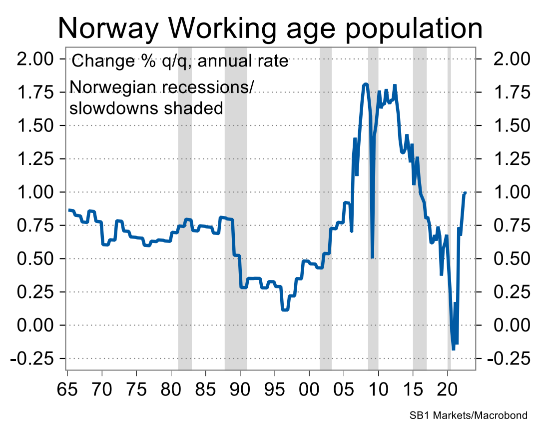
- **The LFS** ('AKU' survey) employment data (both employees and self-employed, with permanent residency in Norway) rose by 0.1% in August (avg. July – Sept vs the previous 3 months) but is down 0.2% over the past 3 months
  - » LFS employment is up 3.3% from before the pandemic
- The **register based employee stats ('A-ordningen)**, reports a 0.4% growth in the no. of employees in Sept, up from unch. in Aug (revised down from +0.1%), and better than we expected. The 3m/3m rate is 2.2%, still impressive – but underlying growth is slowing. The level is up 3.9% since Q4-19. Excluding foreigners on short term stay, the no. of employees is up 4.0% (our est.)
- **National accounts** reported a 2.8% lift in employment to Q2-22 from Q4-19 (and a 0.6% increase q/q in Q2)

Both participation & employment rates are down (but a tad too volatile)

The broad picture: Both rates have flattened – and may possibly be heading down



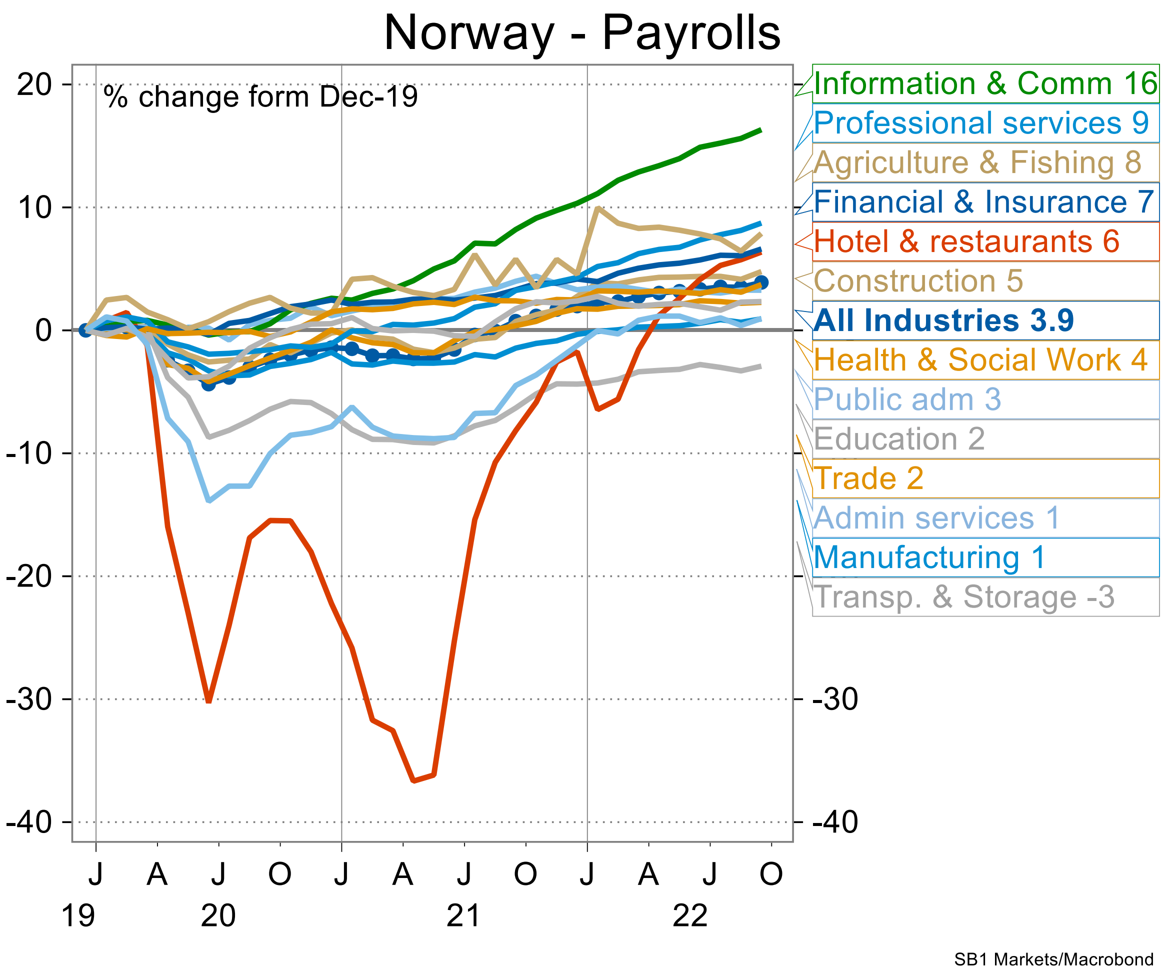


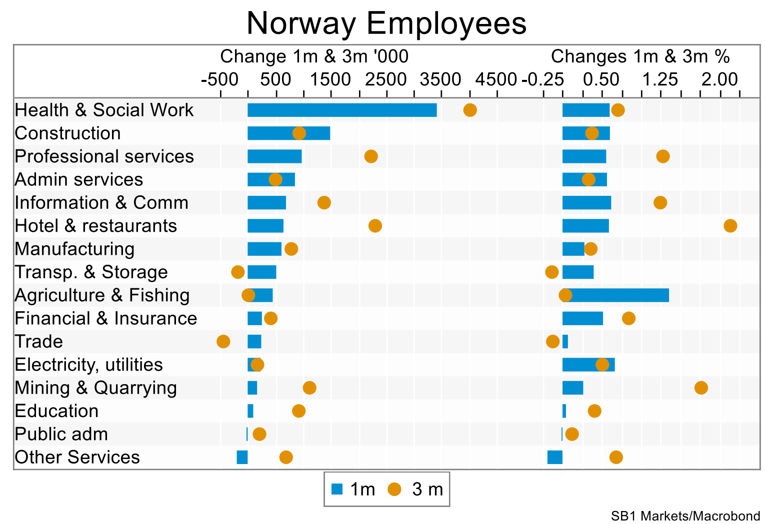


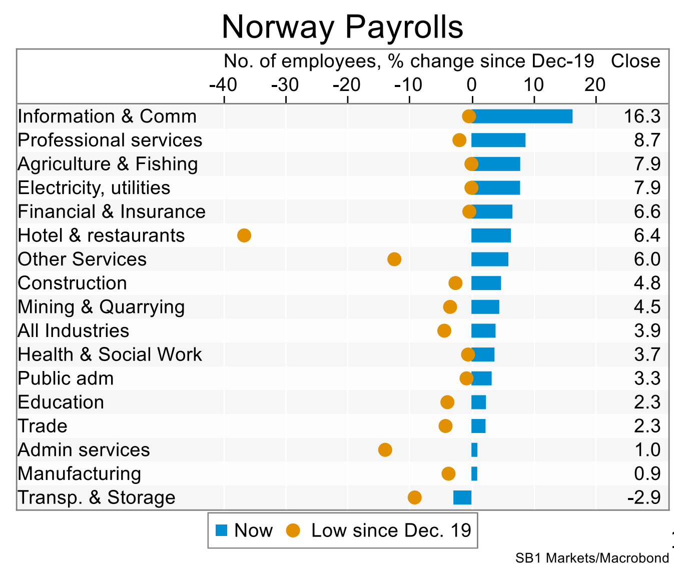
- **The employment rate** was unch. at 70.2% in August
  - » Ahead of the pandemic the rate was almost 69%, and it is up from the 67.4% trough in early 2021 (and from the same level in 2017, after the 'oil crisis'). The employment rate is measured in % of the working age 15 - 74 y population
  - » In March, the employment rate was at 70.7%, the highest since after the Financial Crisis
- **The participation rate** rose 0.1 pp to 72.5% in August, and it is marginally lower than during the spring
  - » Are there still reserves out there? <u>If so, why are they not turning up now, given the very high vacancy level, 'everywhere'?</u>
- **Both rates are** rather volatile from month to month, especially the participation rate after a revision of data
- **Working age population** is up 1% over the last year, in fact a higher growth rate than just before the pandemic
  - » Labour immigration has accelerated, possible as a ketchup effect after low immigration during the pandemic. Given the tight labour markets in the rest of Europe, we doubt labour immigration will solve the labour deficit in Norway. However, Ukrainian refugees immigrated in Q2, and has contributed to the increase in total working age population. So far, not many of them are employed, according to SSB

Now trade (& transport) cuts payrolls, as sales are declining

The surprising lift in September was partly due to a larger than normal lift in health/social work

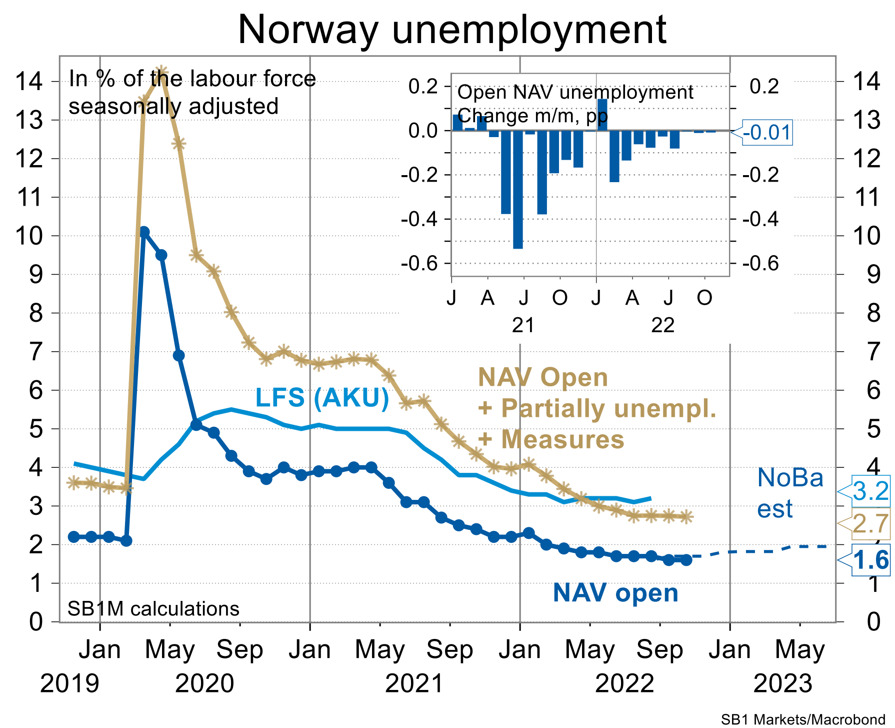


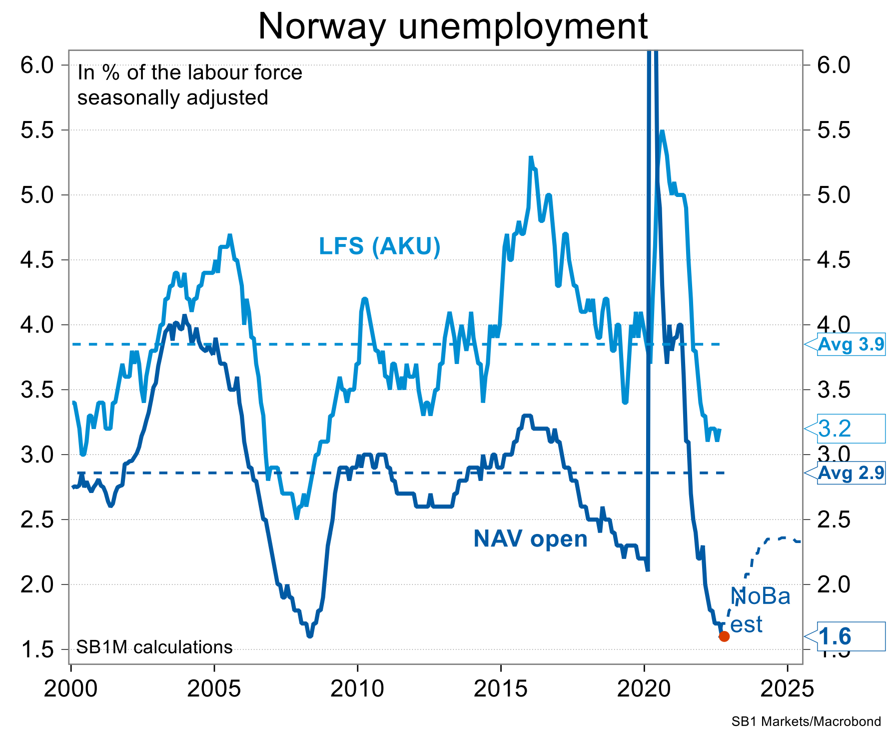




NAV unemployment marginally down in October, and 0.1 pp below NoBa f'cast

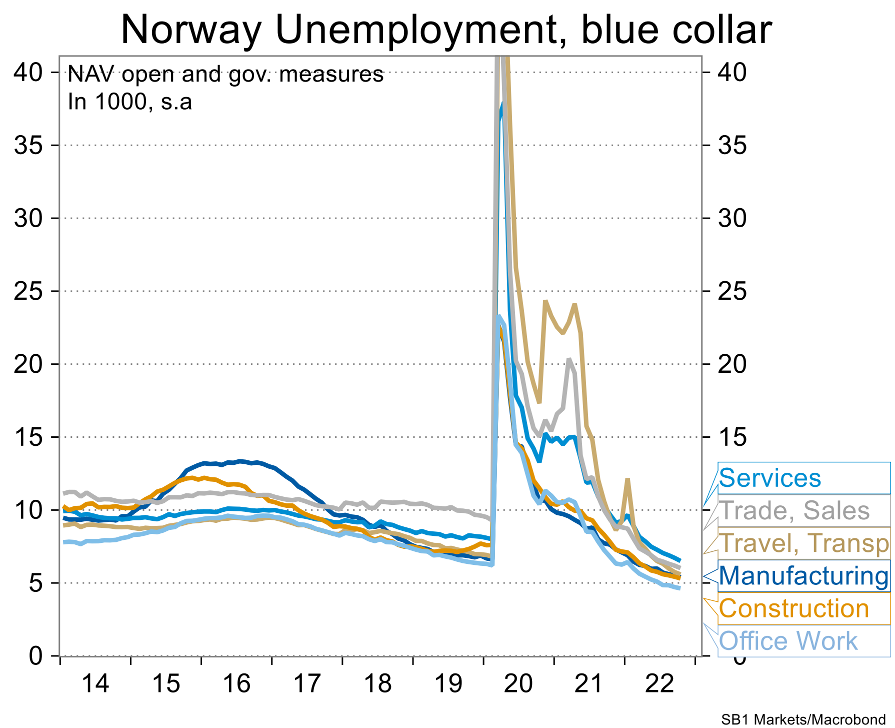
Open unemployment unch. at 1.6% (sa), as expected. In isolation, an argument for a 50 bps hike?

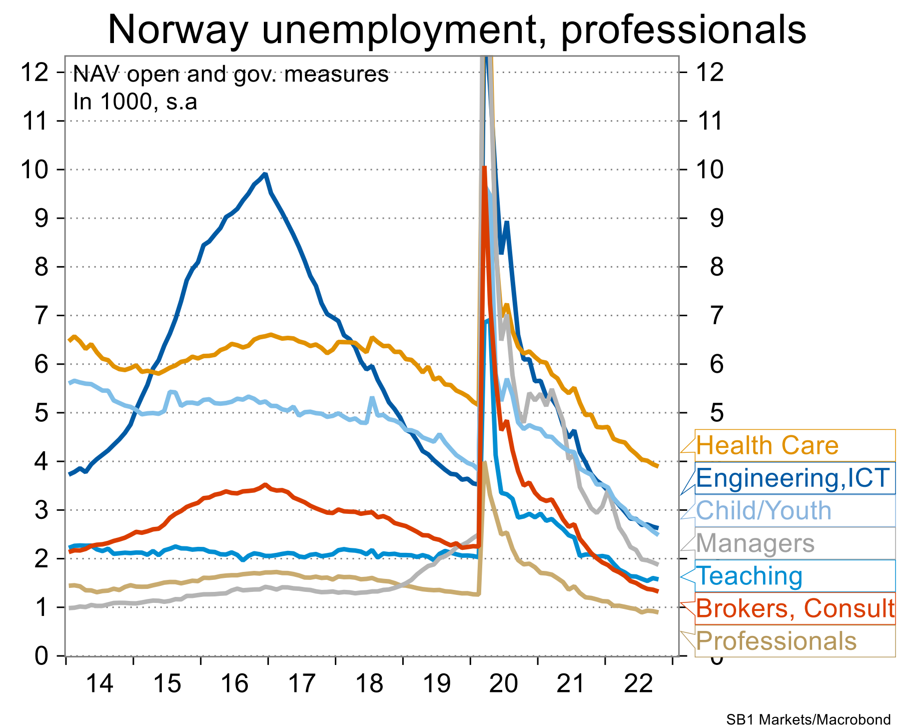




- **The 'full time' open NAV unemployment**, fell by 240 persons in Oct (seas. adj) to 47.6'. The change was as we assumed, but Sept was marginally revised upwards. The rate at 1.6% (s.a) is equal to the lowest level before the financial crisis in 2008, and almost the lowest level since 1980, and +0.1 pp below NoBa's estimate in the Sept MPR. Unadjusted the rate was unch. at 1.6% (1.55%), expected down to 1.5%
- Including labour market measures, unemployment fell by 800' persons, 500 more than we expected, and the rate is at 2.0%
- The inflow of **new job seekers** is trending slowly upwards, but the level remains very low. The **inflow of new vacancies** rose marginally in Oct, but the trend is down, from the peak before the summer. Even so, the level remains very high. The decline is broad, except for the public sector.
- **The LFS (AKU) unemployment rate** reversed the 0.1 July, decline, as the rate rose to 3.2%. This rate has been flat since the spring

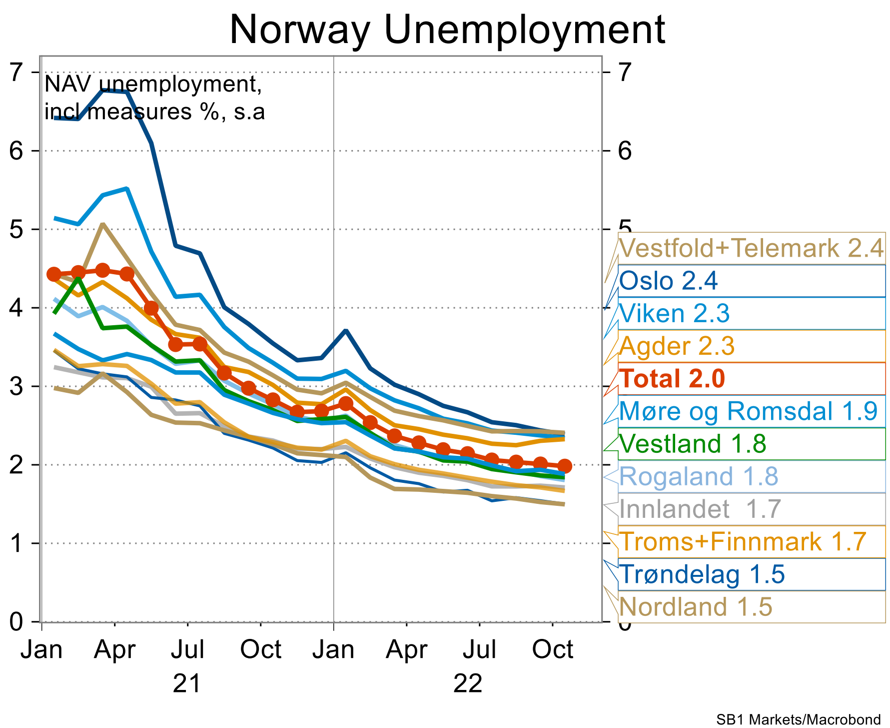
Unemployment is still trending down for all sorts of labour

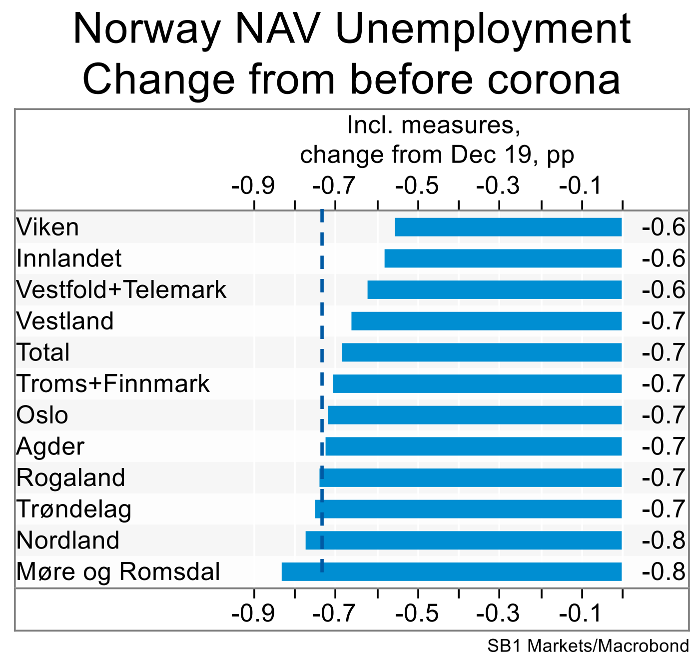




Unemployment is still falling almost everywhere – except for Agder

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

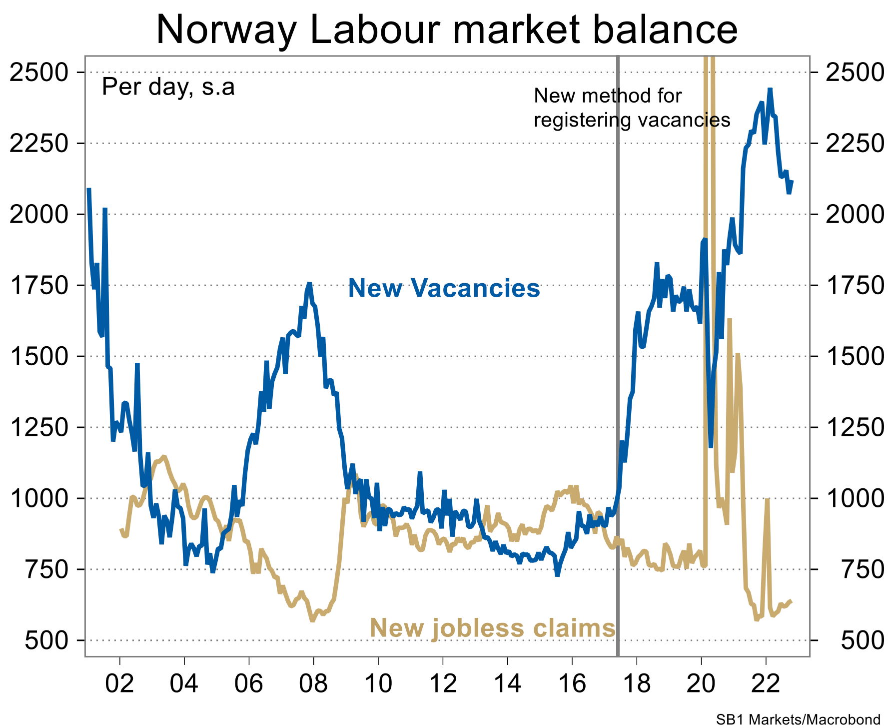


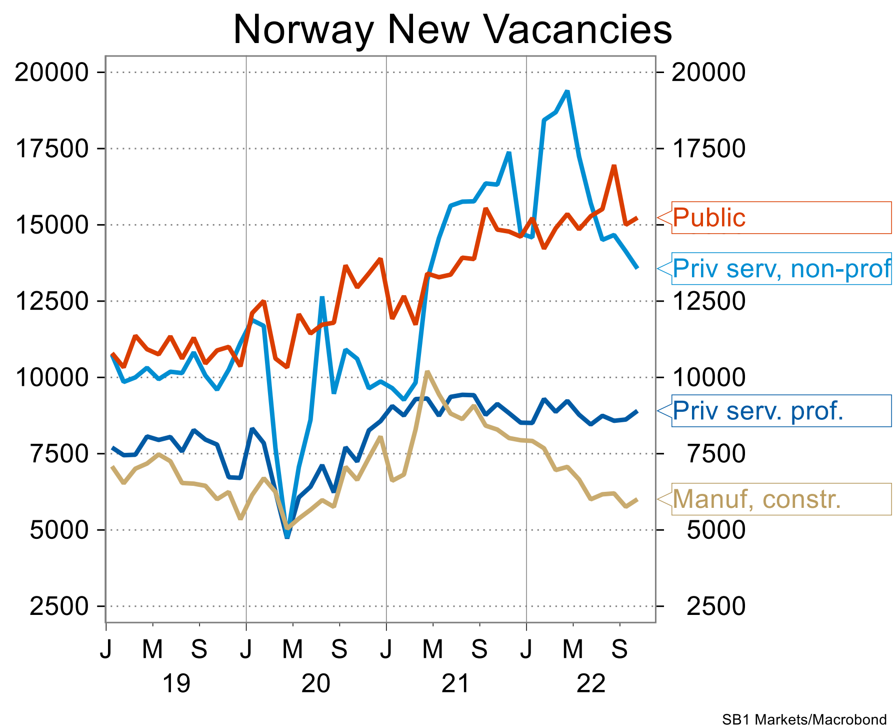


- The unemployment rate in Agder rose marginally in both September and October
- Nordland and Trøndelag at the bottom – Oslo at the top, as usual

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

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

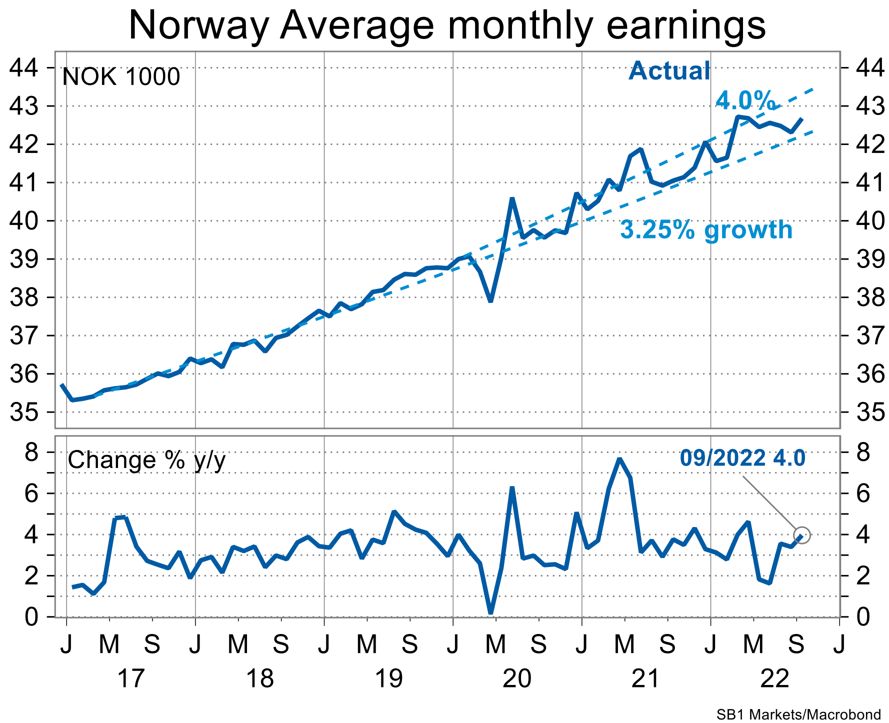


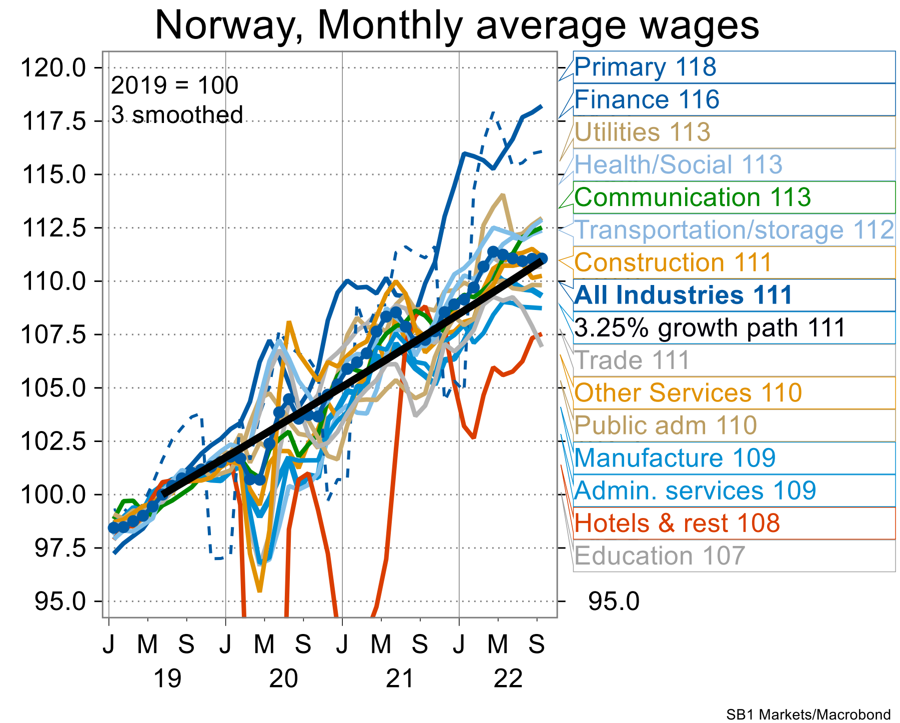


- The no. of new vacancies rose marginally in October, but the trend is clearly down
- Most sectors have announced somewhat fewer new vacancies recently, most pronounced in the construction sector
- The no. of new jobless claims have probably bottomed at a very low level, and is trending very slowly upwards

Wage inflation is (very likely) NOT accelerating, wage trends up less than 3.5%

Regrettably wage data are volatile – annual growth in August was revised down 2 pp to 3.4%

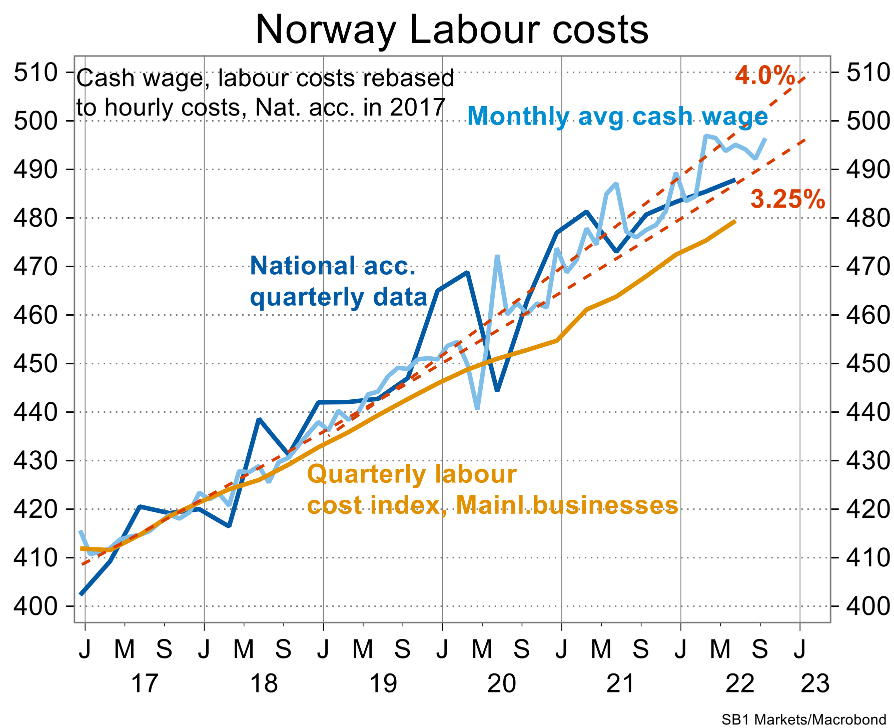


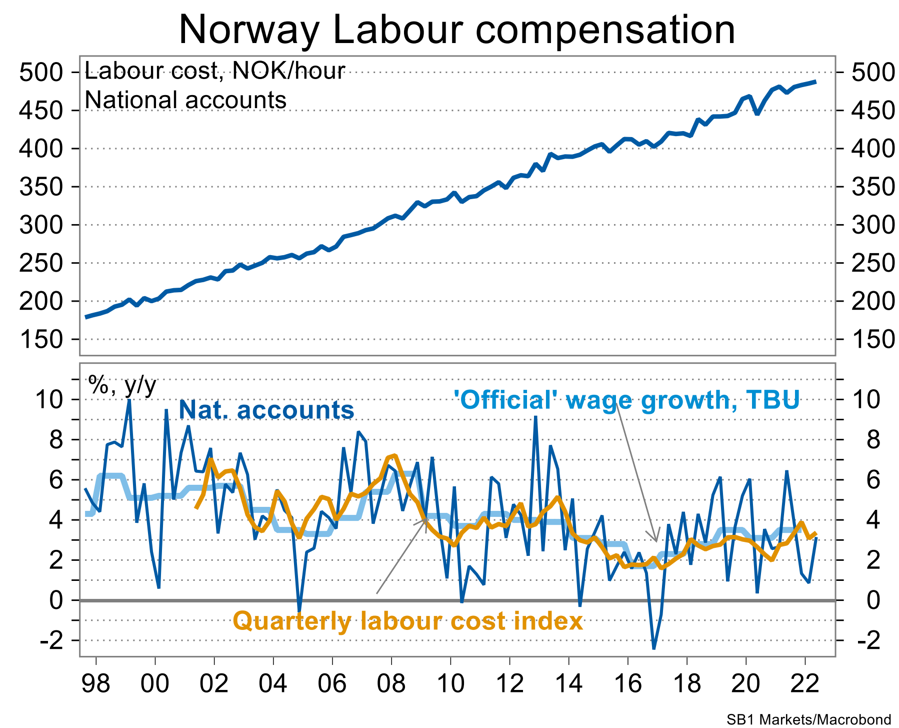


- **Monthly average cash earnings** are rather volatile – and more than normal since the beginning of the pandemic. The average monthly wage depends on hours worked, bonuses, sector mix etc. – and data are often substantially revised
  - » The previous month's annual wage inflation was revised down by close to 2 pp to 3.4%! So take the current 4.0% growth rate with 2 grains of salt
- However, given the present stats – which are the best at hand – we are not witnessing any acceleration in wage inflation. The quarterly labour cost index was up 3½% in Q2, and growth is not accelerating. National accounts up to Q2 have come to the same conclusion.
- Wage inflation is extremely important vs. the longer-term inflation outlook, and the need for monetary tightening. So far, wage inflation has been clearly below our expectations!

Wage data are volatile and not not always consistent

Taken together: No signs of a sharp acceleration in wage inflation

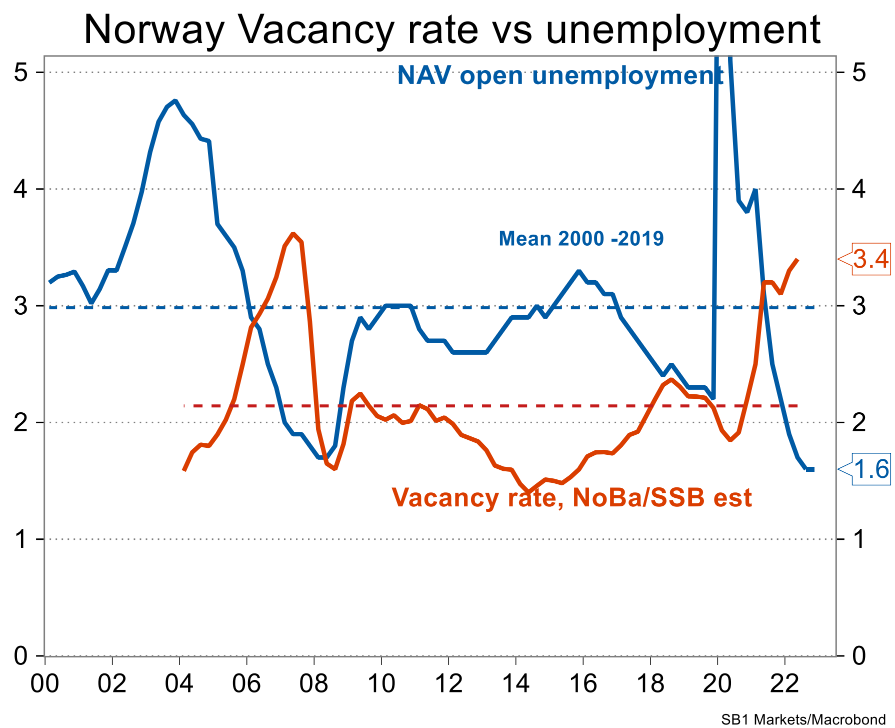


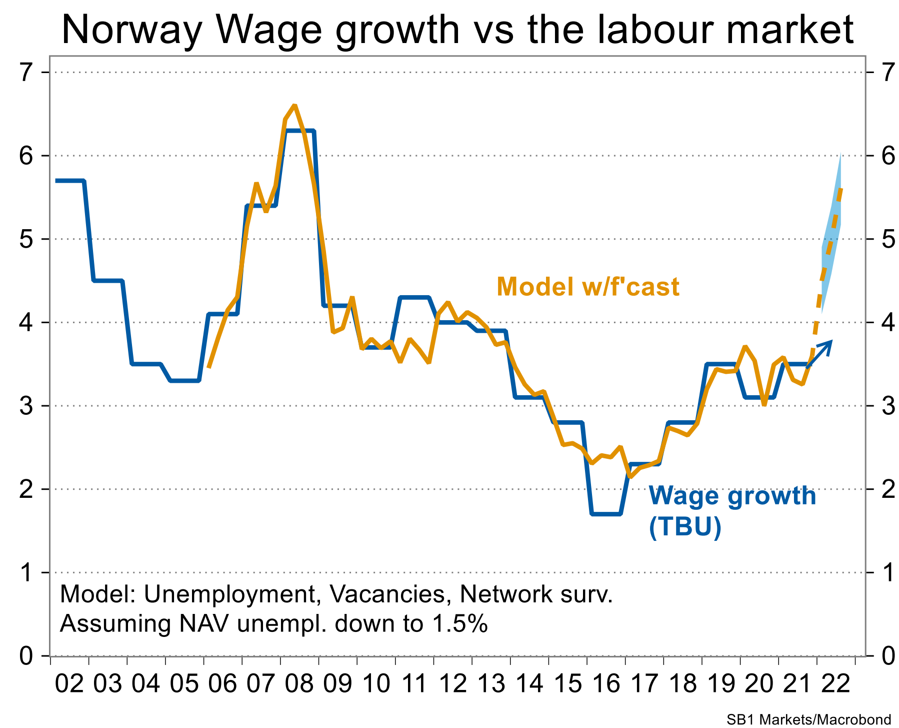


- The quarterly labour cost index correlates the best with the ‘official’ wage growth as calculated by the TBU

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

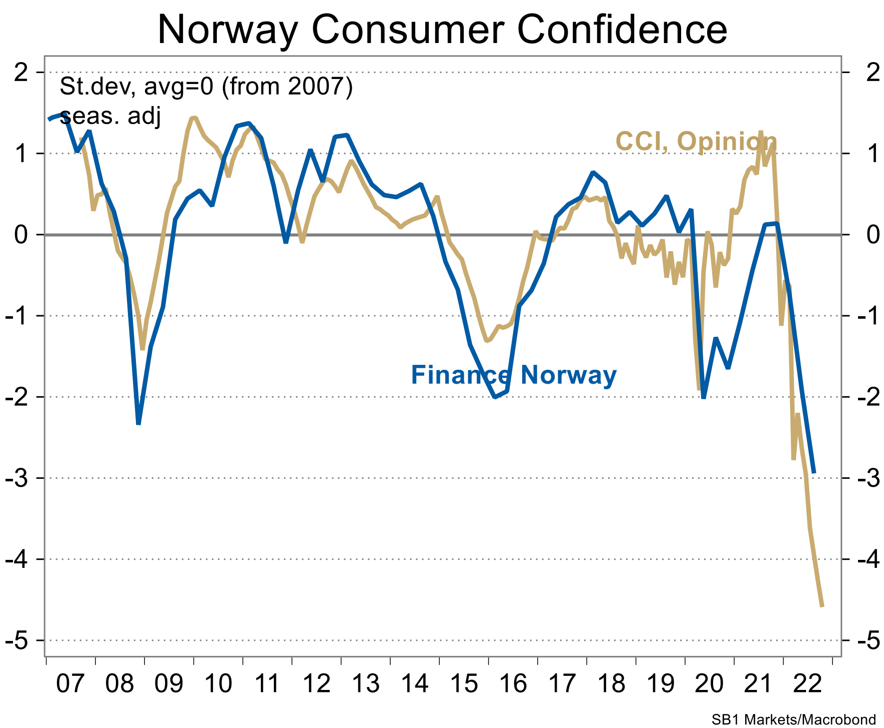
… if nothing is done in order to weaken the labour market. But somebody is doing something now





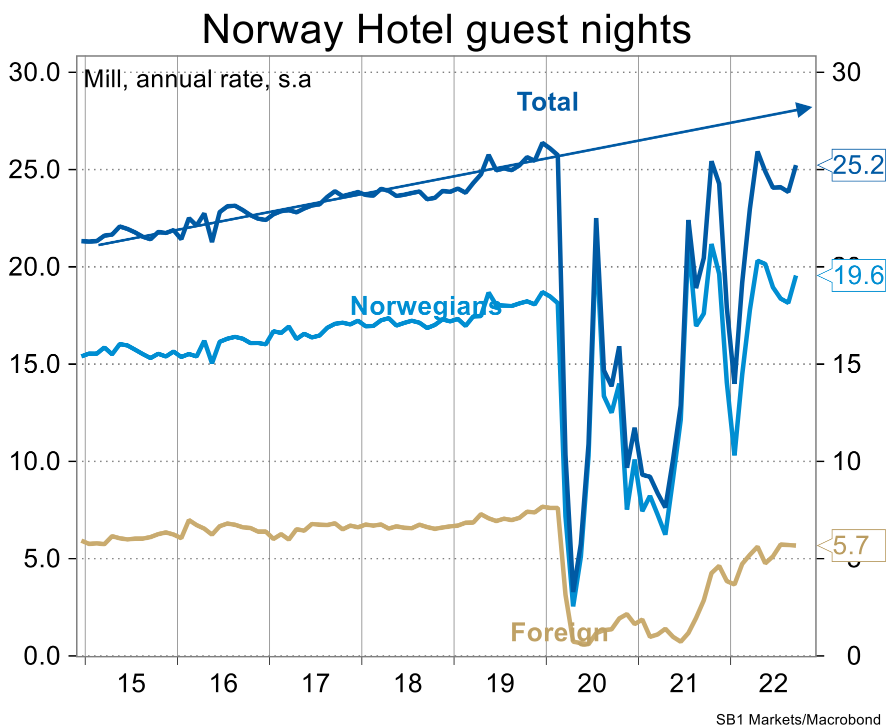
Consumer confidence down to ATL in ~~May~~ ~~July~~ ~~August~~ ~~September~~ October…

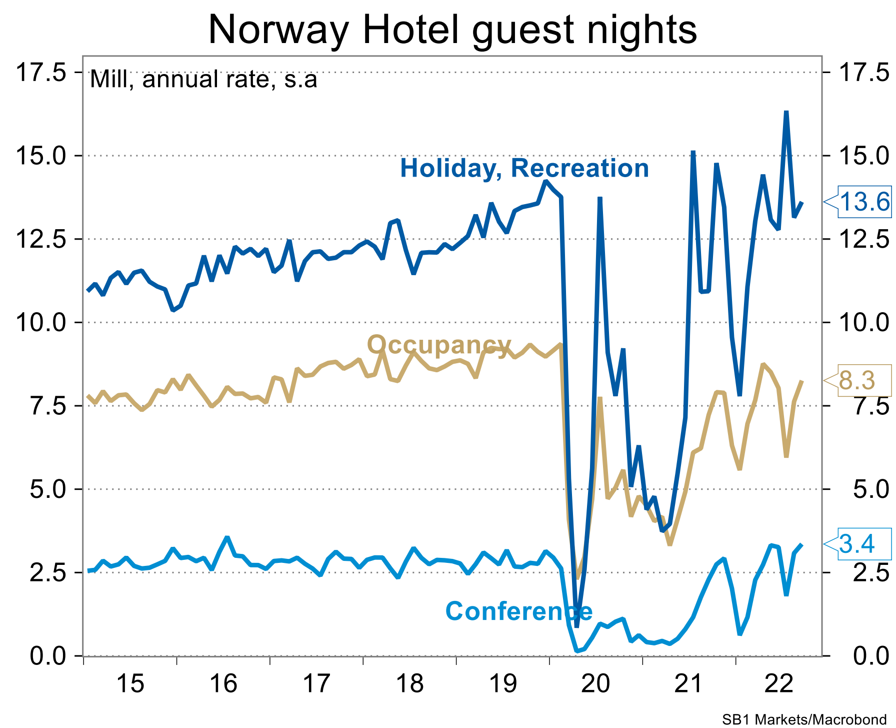
CCI from Opinion fell further in October, by -0.3 st.dev to -4.6



- **The CCI print** from Opinion in October was the lowest on record– high inflation and higher interest rates are no doubt biting
- The index 4.6 st.dev below average. The bottom during the pandemic was 2.0 st. dev. below average
- **Will households stop spending or retreating from the housing market?** The housing market has no doubt turned the corned, while sales are trending down
- The **net share of optimists** is -32%. Given inflation and the hikes in interest rates + some geopolitical uncertainty, this share could easily have been larger
- On the other hand, even if a large share of the population recognises that their own economy will be hurt, it does not imply that they all plan to cut spending sharply. Even so, the decline in confidence is of course worrisome

Business hotel guest nights almost back to normal, conferences ATH, recreation OK

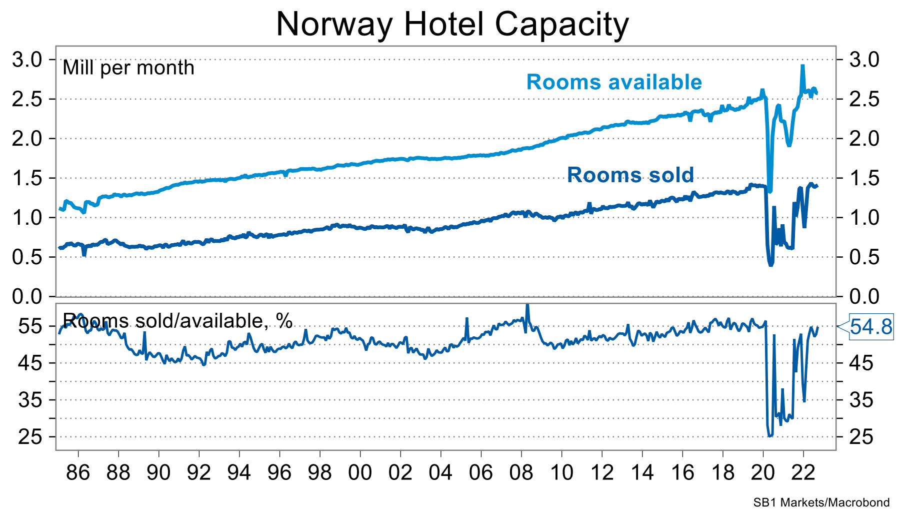


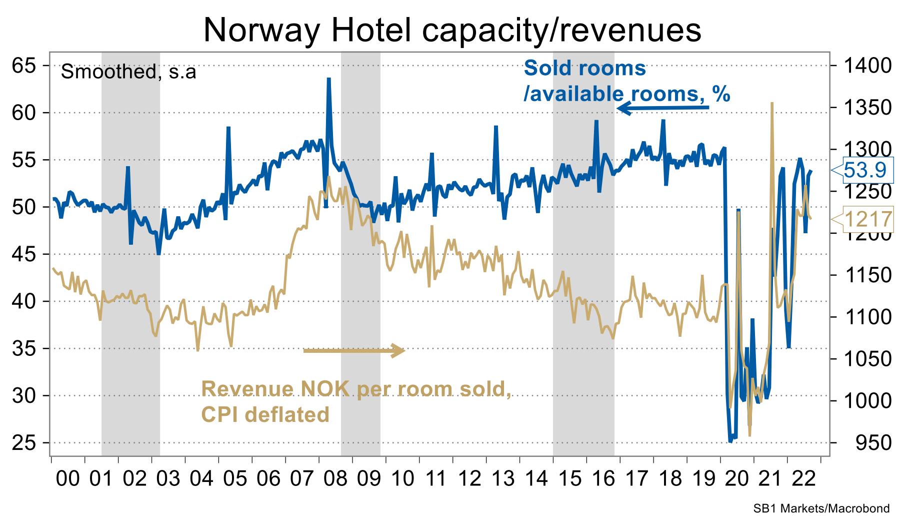


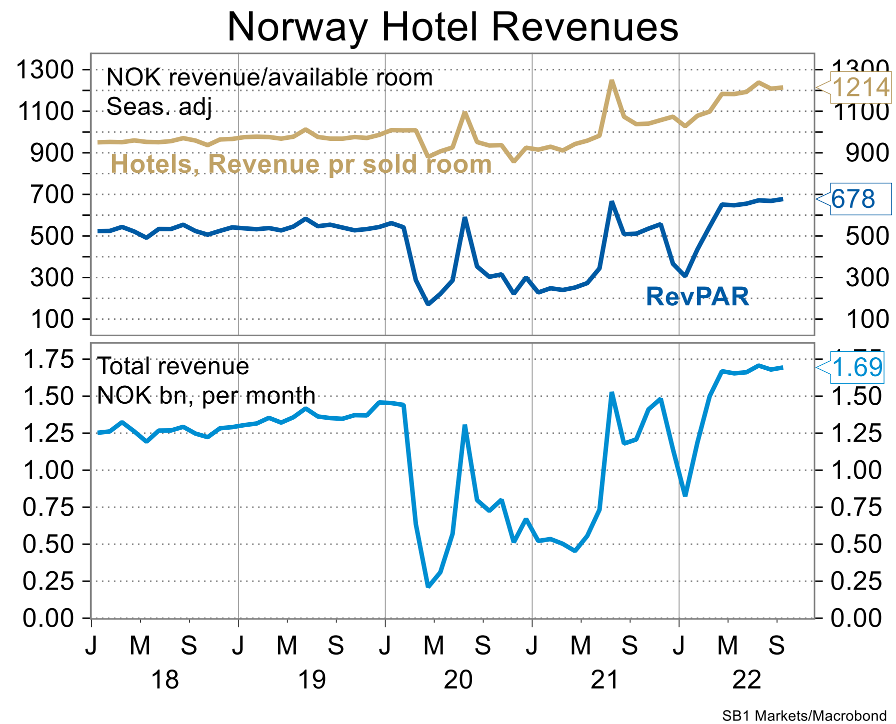
- Recreational demand is back to a normal level, even if the total number of foreigners are still down 25% vs the pre-pandemic level
- The conference market is back the pre-pandemic level – it took just some few weeks after restrictions were lifted
- Other business guest nights are some 10% % below the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

Capacity utilisation almost back to normal but prices are up 20%+ since Feb-20…

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







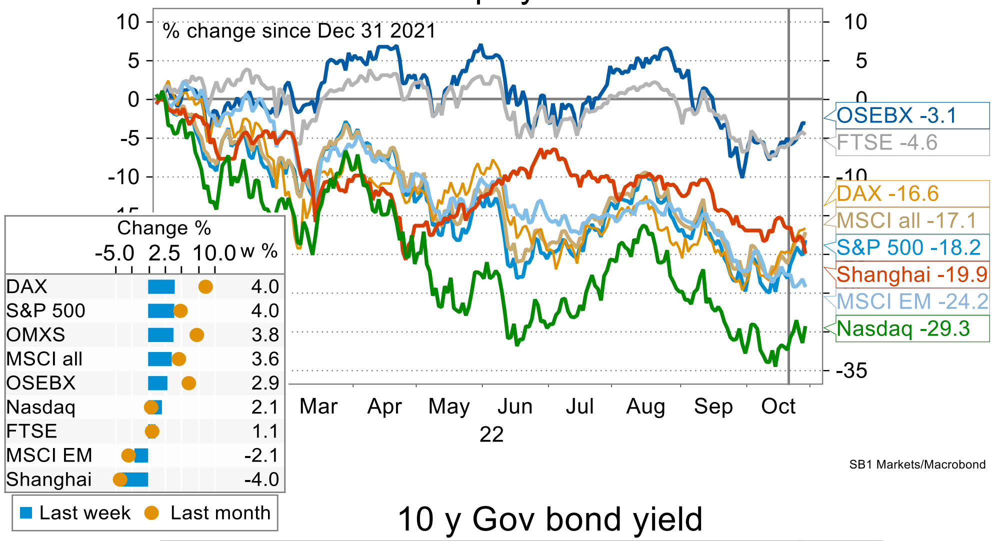
- **Capacity utilisation** (room sold vs. rooms available) was 54% in September, somewhat below the normal level ahead of the pandemic
- **Revenue per sold room** is up 21% from the Feb-20 level, a substantial increase (aka inflation)
- **RevPAR** (revenue per available room) is also far above the pre-pandemic level, 25%

SpareBank 1 MARKETS

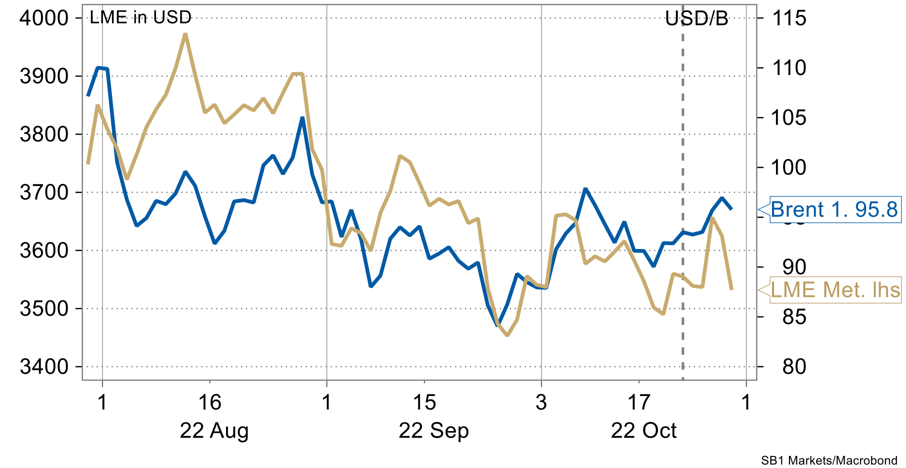
Risk on, as bond yields yielded. Oil up, most other commodities down

Chinese/H-K equities fells as President Xi took full control. USD, CNY down; Most others f/x up

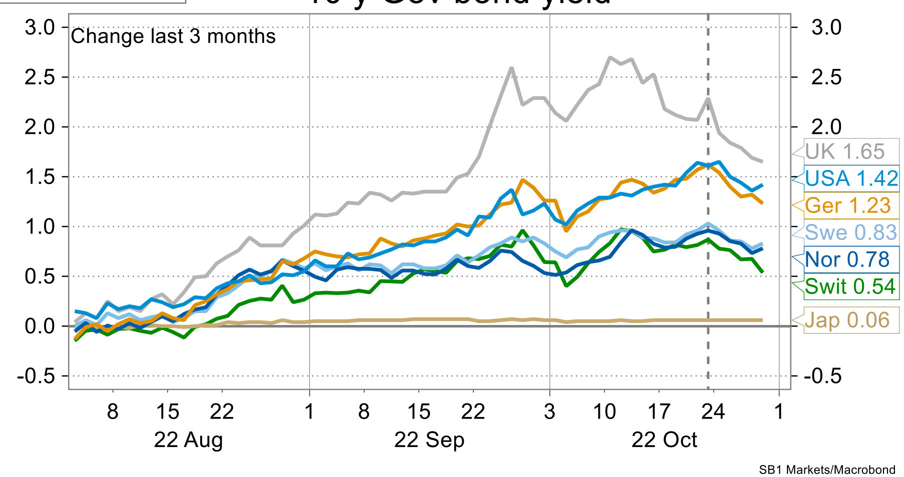
Equity Indices



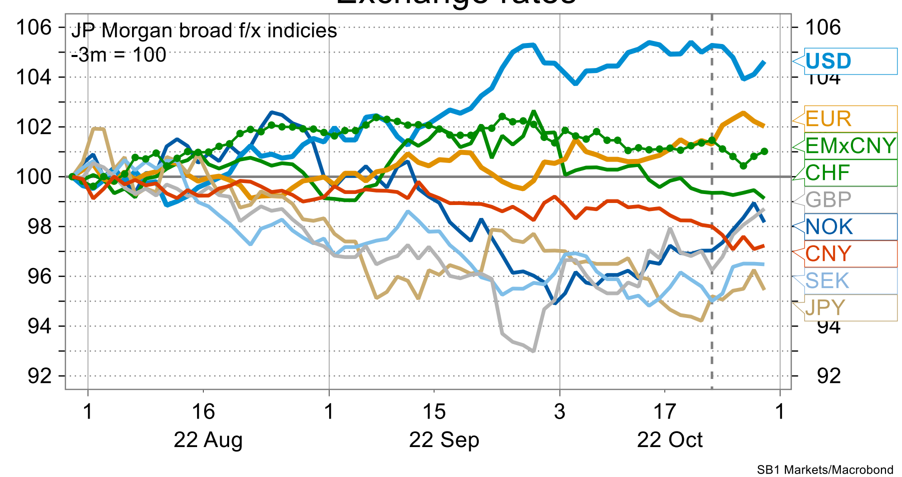
Oil vs. metals



10 y Gov bond yield

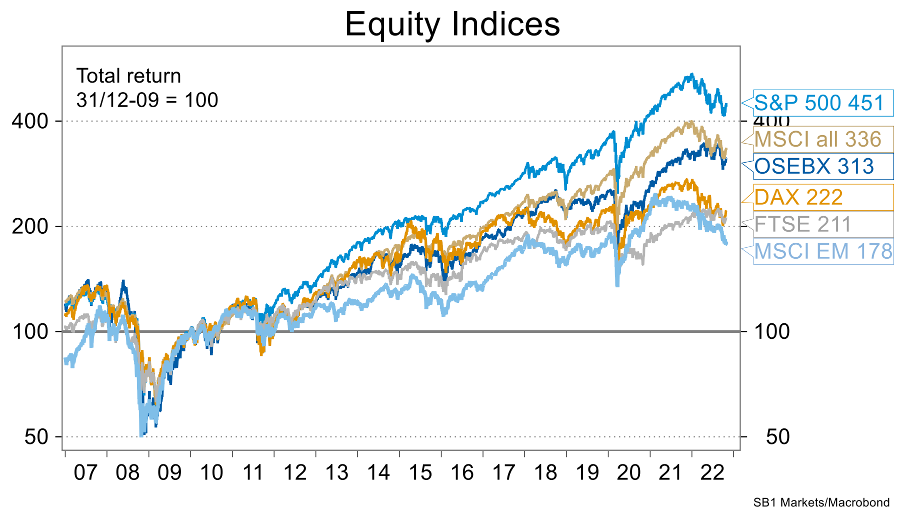


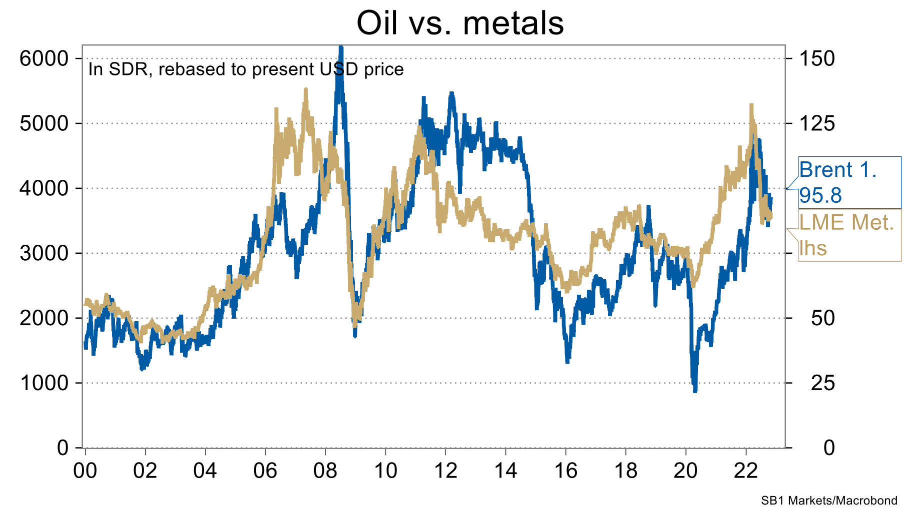
Exchange rates

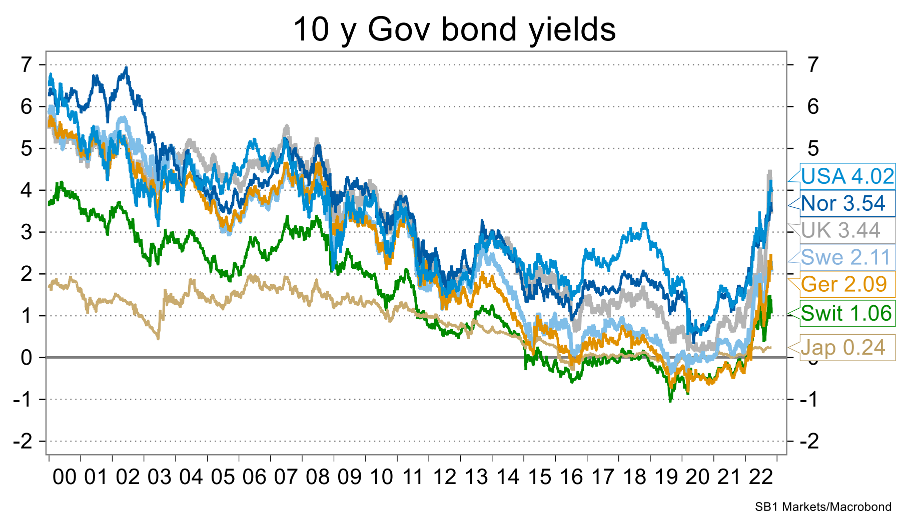


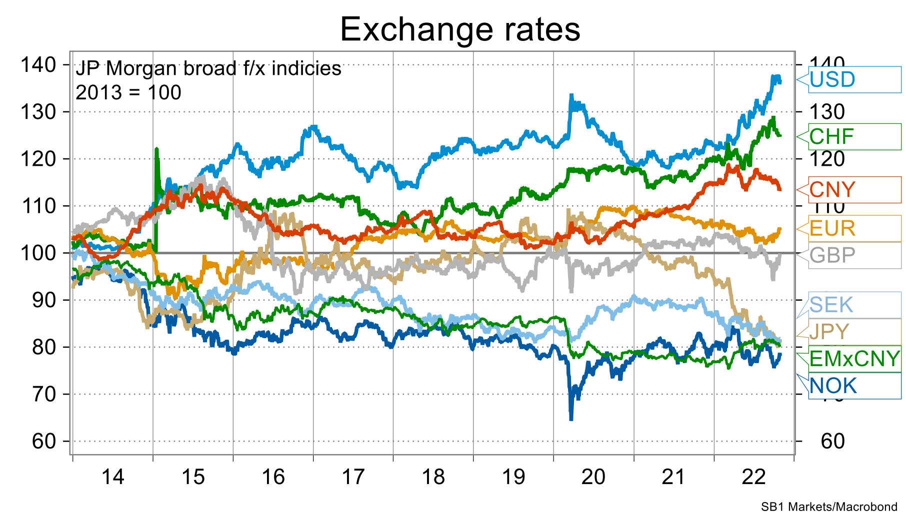
The long-term picture: Stock markets down, commodities down, bond yields up

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





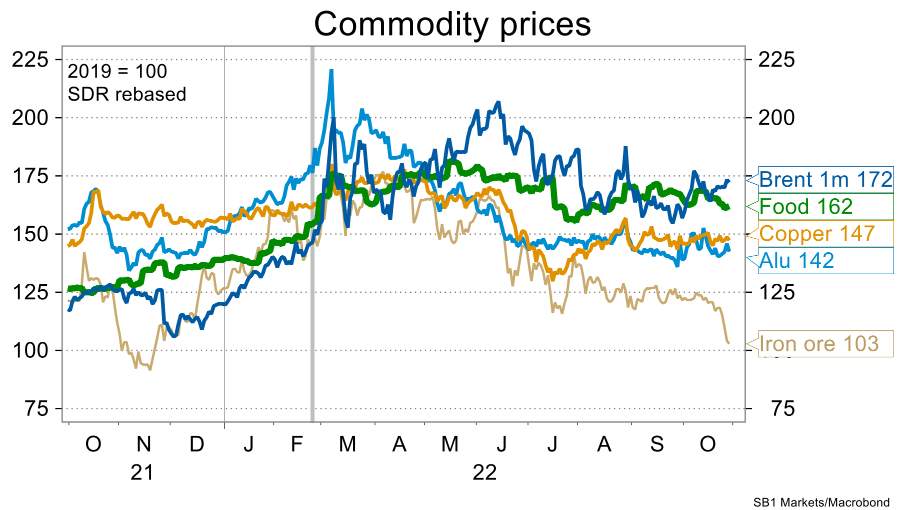


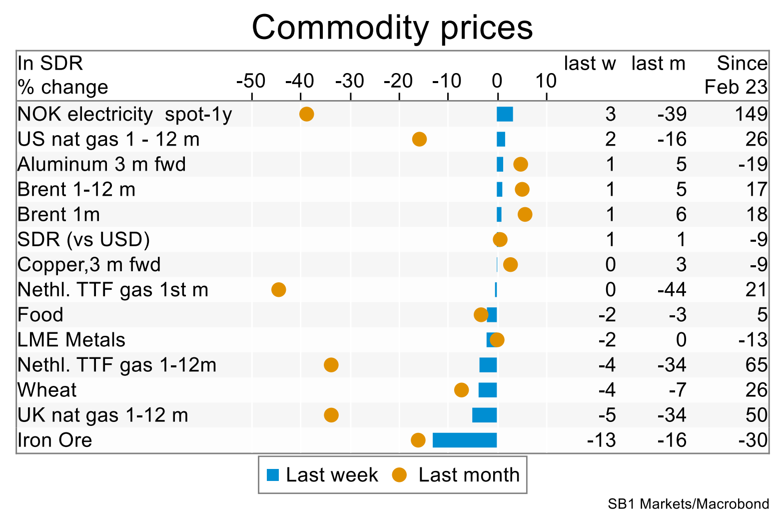


SpareBank 1 MARKETS

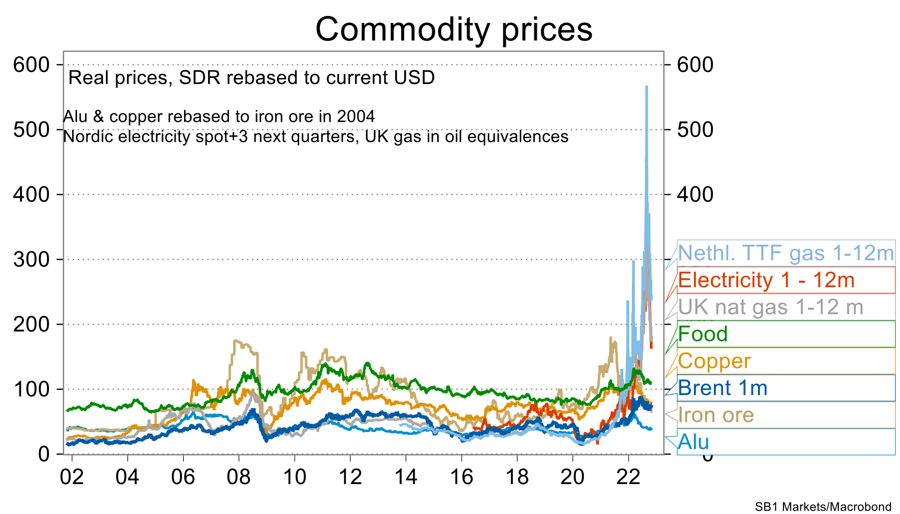
Commodity prices more down than up

Iron ore prices fell sharply, less hope for a recovery in Chinese construction sector





In SDR % change	last w	last m	Since Feb 23
NOK electricity spot-1y	3	-39	149
US nat gas 1 - 12 m	2	-16	26
Aluminum 3 m fwd	1	5	-19
Brent 1-12 m	1	5	17
Brent 1m	1	6	18
SDR (vs USD)	1	1	-9
Copper,3 m fwd	0	3	-9
Nethl. TTF gas 1st m	0	-44	21
Food	-2	-3	5
LME Metals	-2	0	-13
Nethl. TTF gas 1-12m	-4	-34	65
Wheat	-4	-7	26
UK nat gas 1-12 m	-5	-34	50
Iron Ore	-13	-16	-30



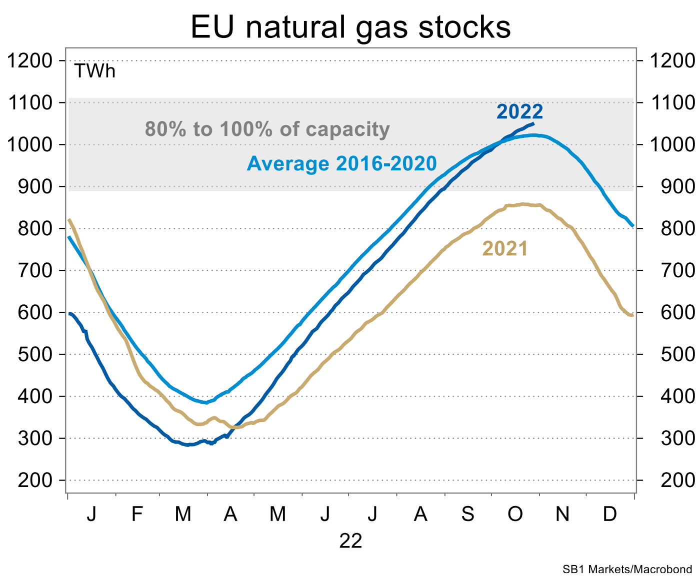
Last week – prices in SDR

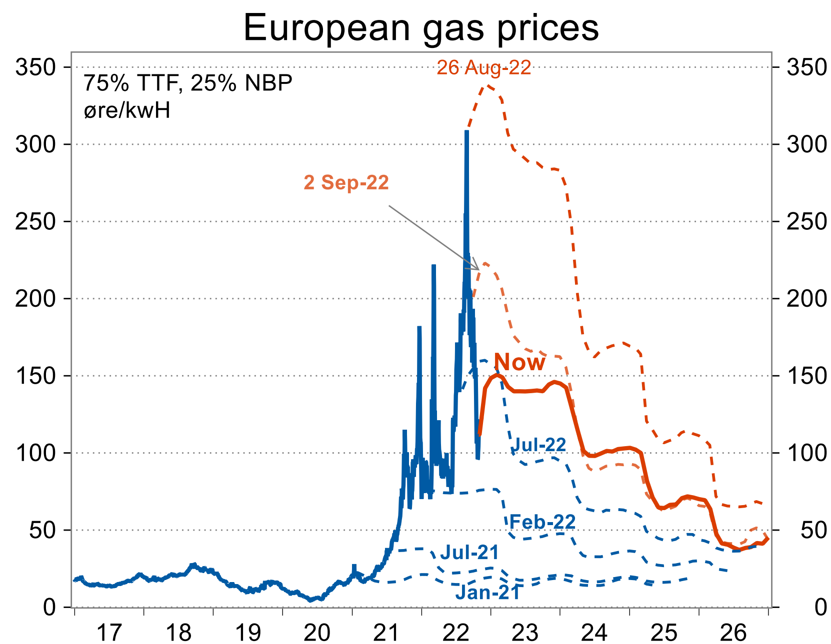
- **European natural gas** fell further last week, while Norwegian **electricity prices** flattened following the steep decline recent weeks
- **Oil prices** were close to unchanged
- The Economist's **food commodity index** continued downwards last week, and is once more trending down, even measured in SDRs (which are depreciating vs. the USD). Food commodity prices are lower than the 10 y average measured in constant USD
- **Metal prices** were mixed but in average down (LME). **Iron ore** prices 'collapsed' (-13%) as hopes for a revival in steel demand in China faded after the CCP conference, and steel inventories were reported up

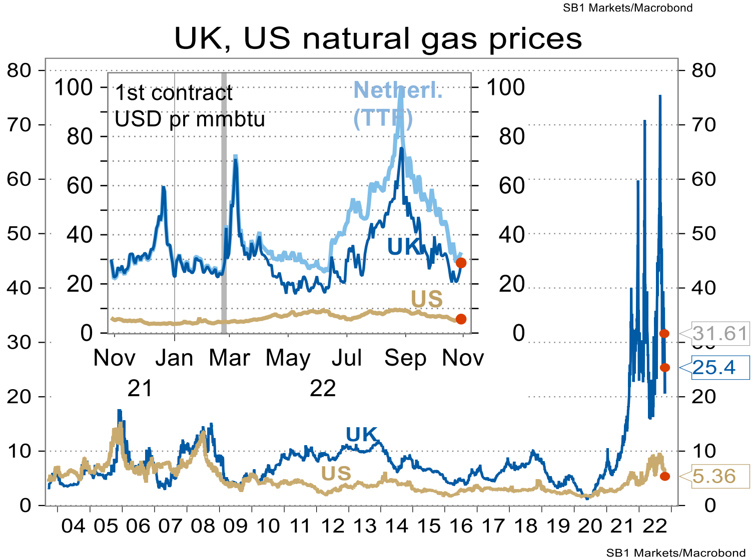
SDR: IMF's Special Drawing Rights – a 'global currency'

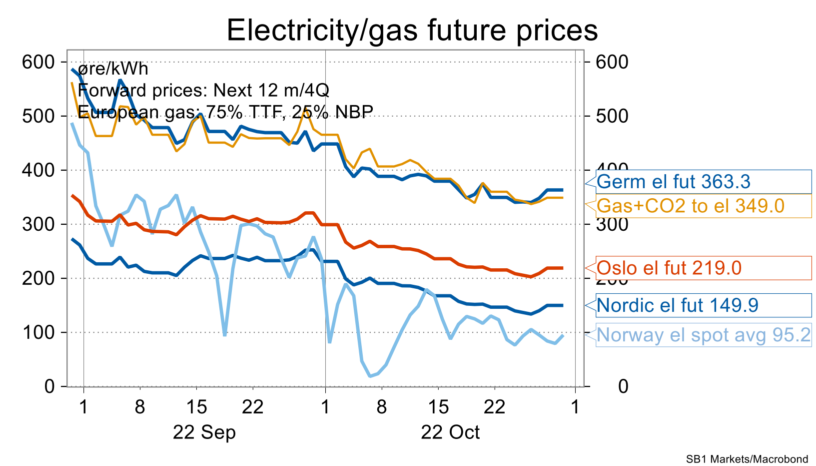
‘Spot’ European gas prices further down, as inventories are filled up

Electricity prices are trending down as well







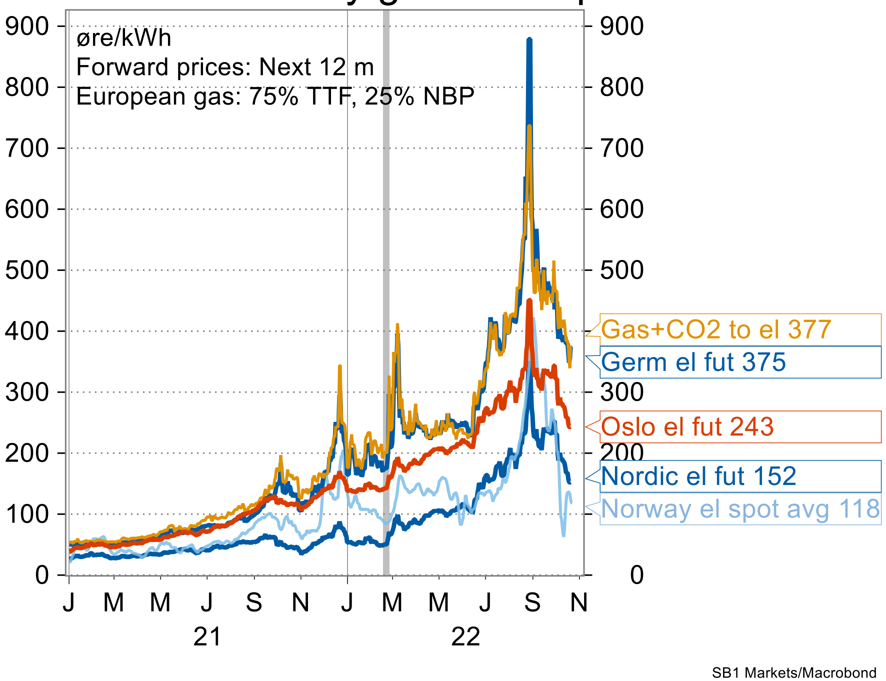


SpareBank 1 MARKETS

European gas & electricity sharply down last week

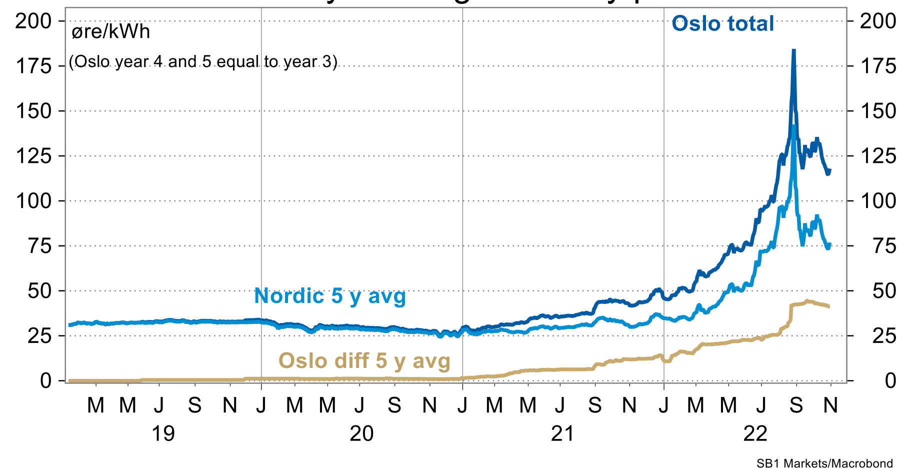
… but the price level is still high, at least the 12 m fwd prices

Electricity/gas future prices

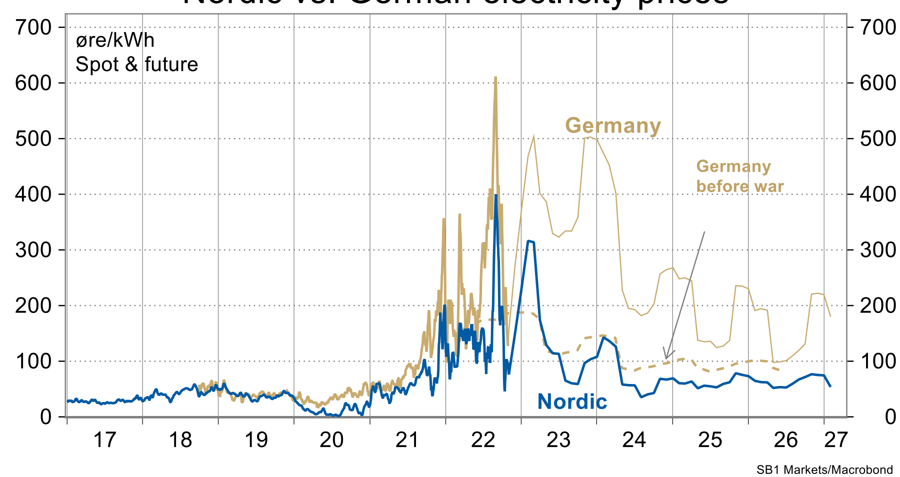


- More discussions of a price cap gas, at least for gas imported to EU through pipelines (with no alternative usages)

Nordic 5 y fwd avg Electricty prices



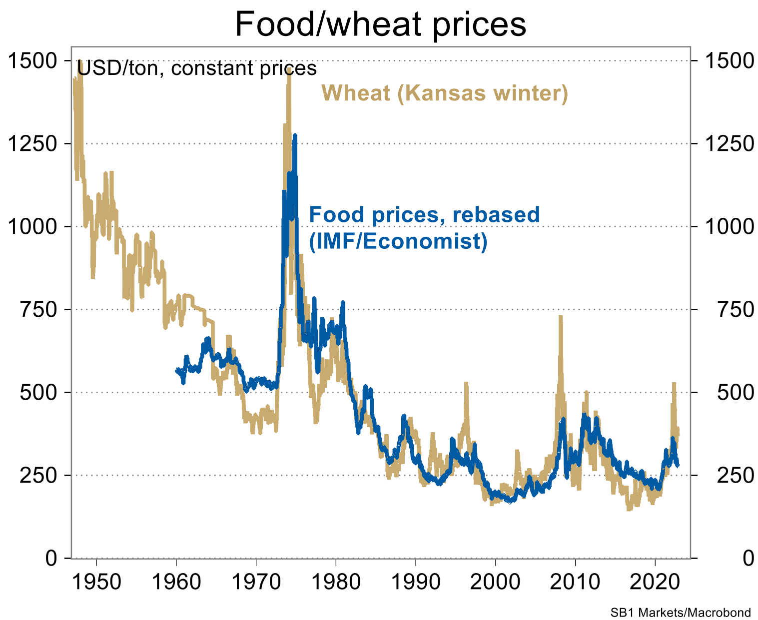
Nordic vs. German electricity prices

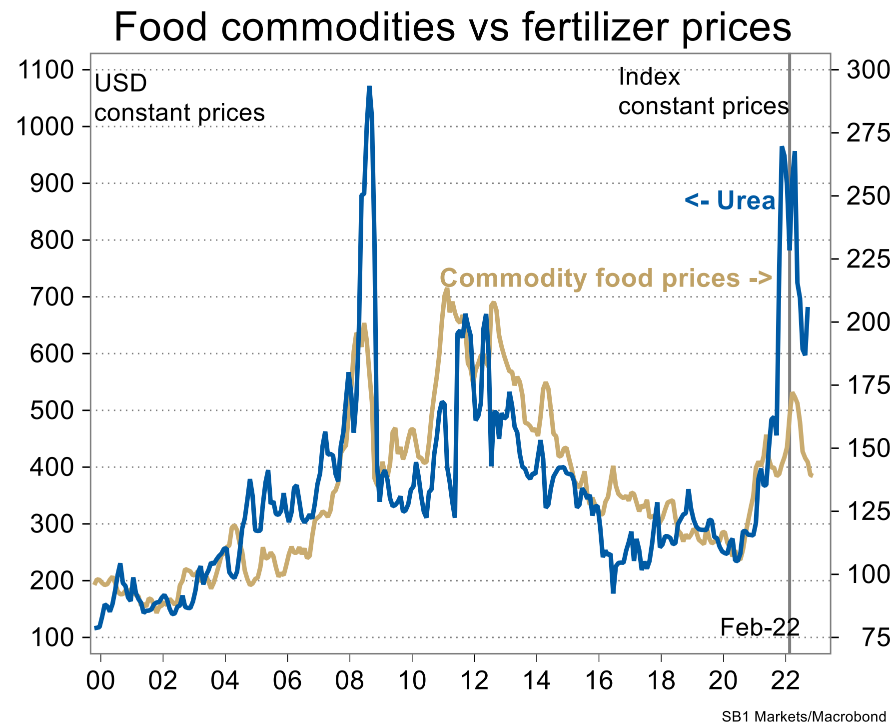


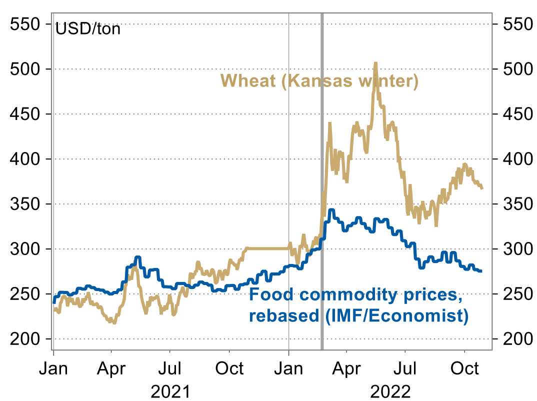
European gas: 75% Dutch TTF, 25% UK NBP, excl. CO2 cost

Food prices are trending down

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



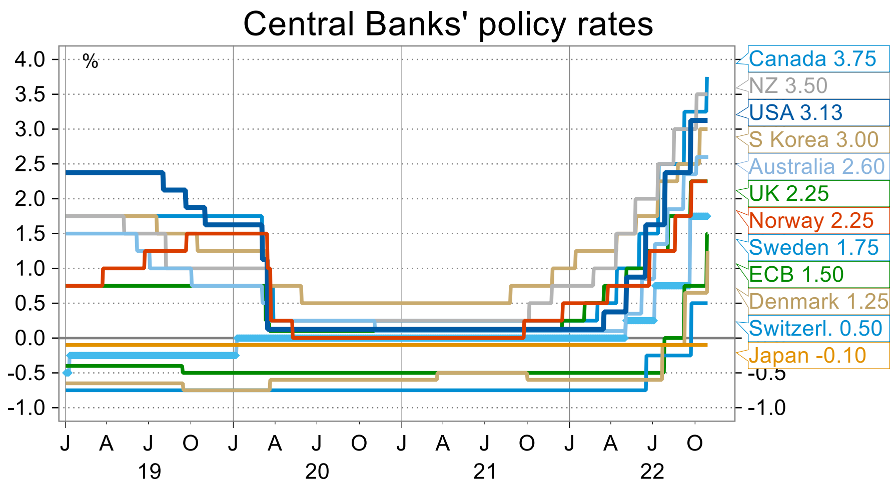


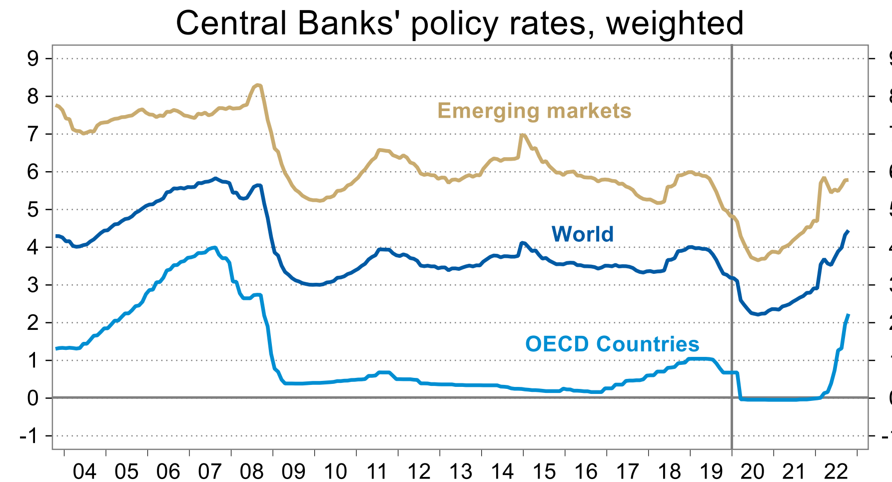


Urea prices have been falling too

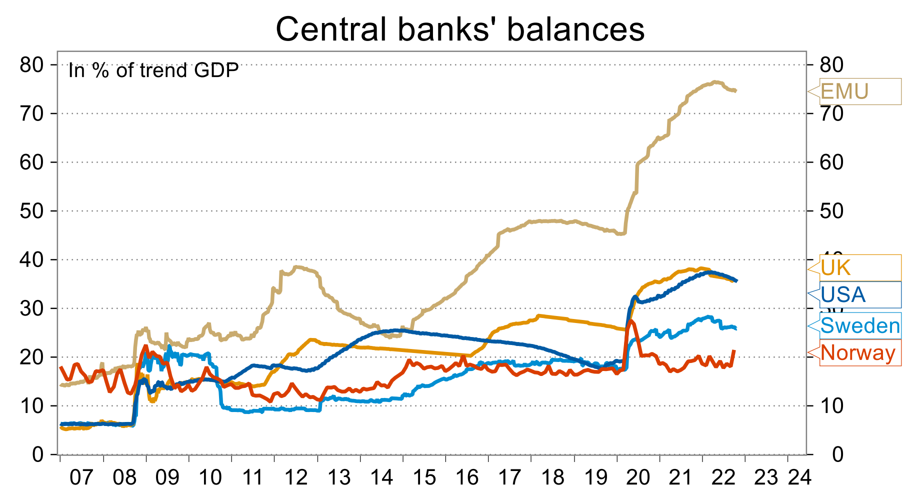
Canada 'slowed' to +50 bps, and Australia to +25 bps

While ECB lifted its signal rates by 75 bps, as widely expected. More to come this week



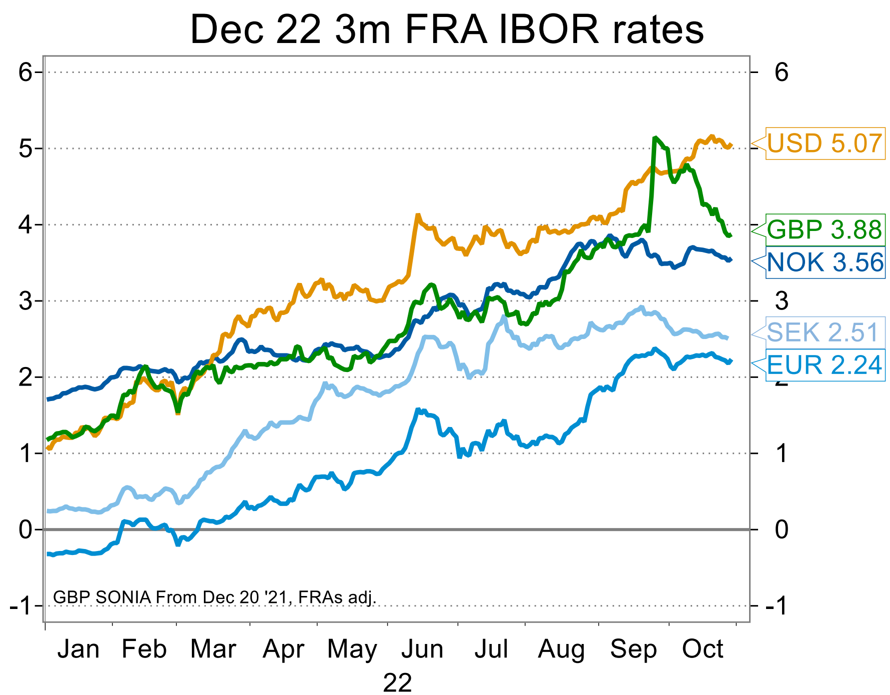


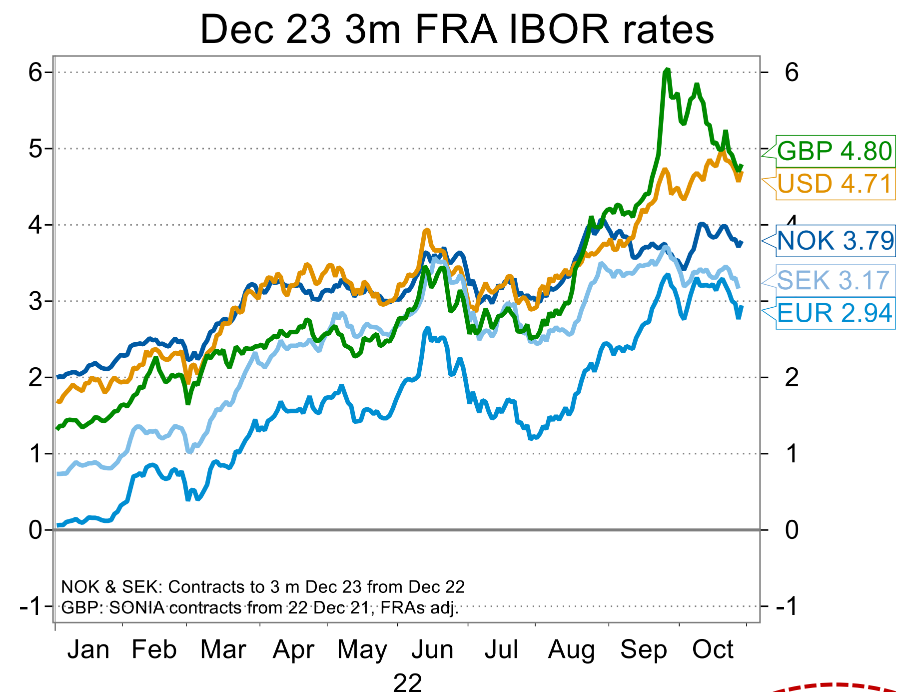
- **Central banks** are hiking rates even if they expect growth to slow (US, EMU) or the economy to contract (Sweden, UK, Norway) because inflation is way above target (including all measures of underlying inflation, partly also costs) and is expected to remain above target for several years
- The **EM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

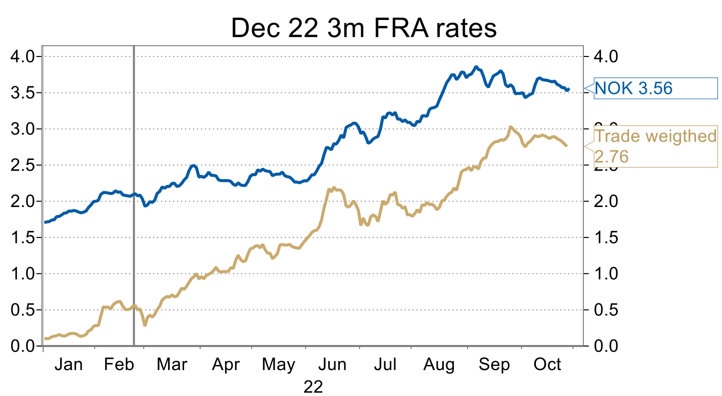


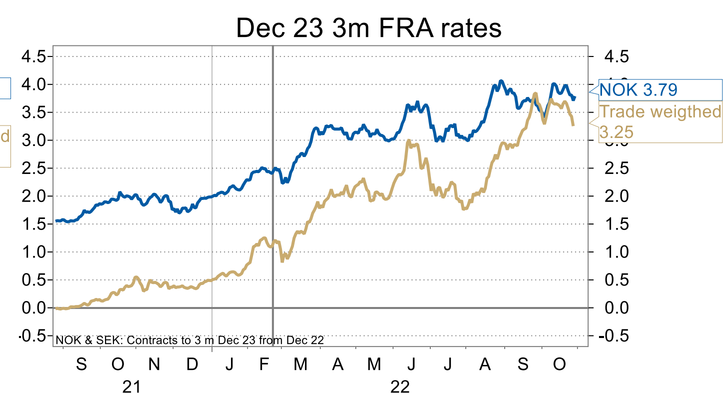
FRAs on the way down most places

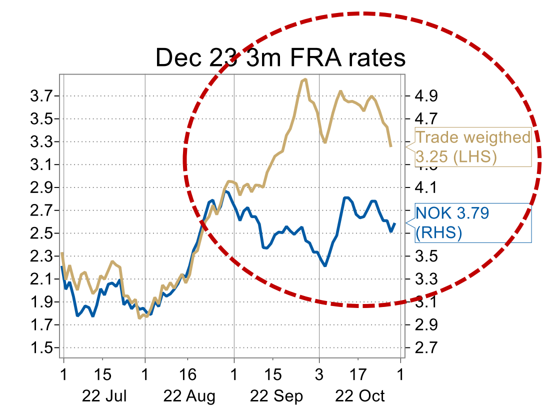
GBP rates have come down to a more reasonable level. And the ECB can not kill the European economy







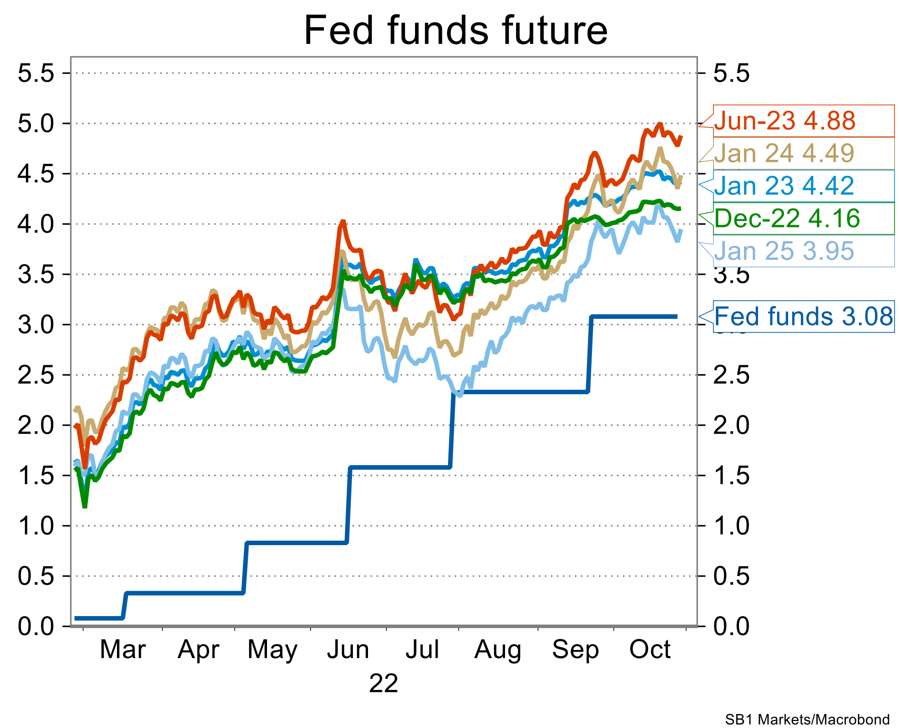


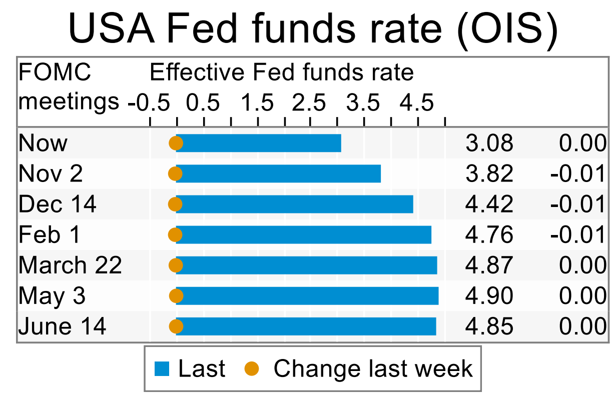


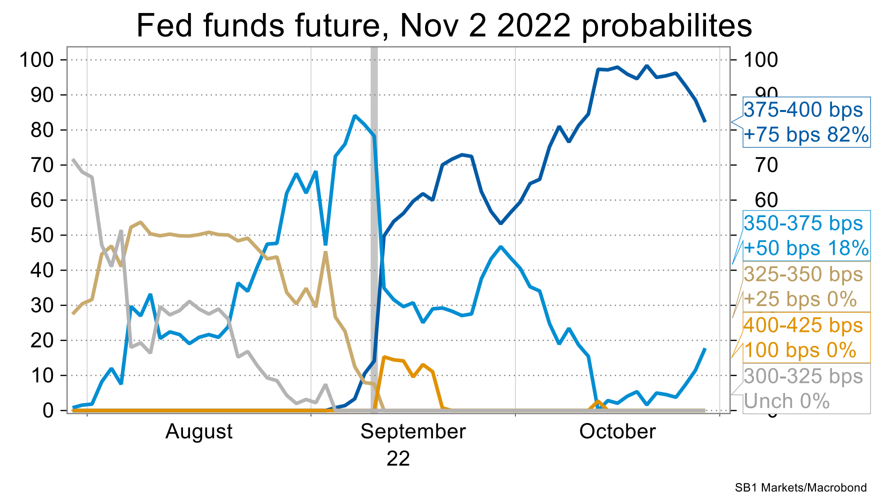
SB1 Markets/Macrobond

Another ‘triple’ hike on Wednesday still most likely but markets don’t exclude 50 bps

If 75 bps: Up to 3.75% – 4.00%. A peak at 4.90% is expected in May

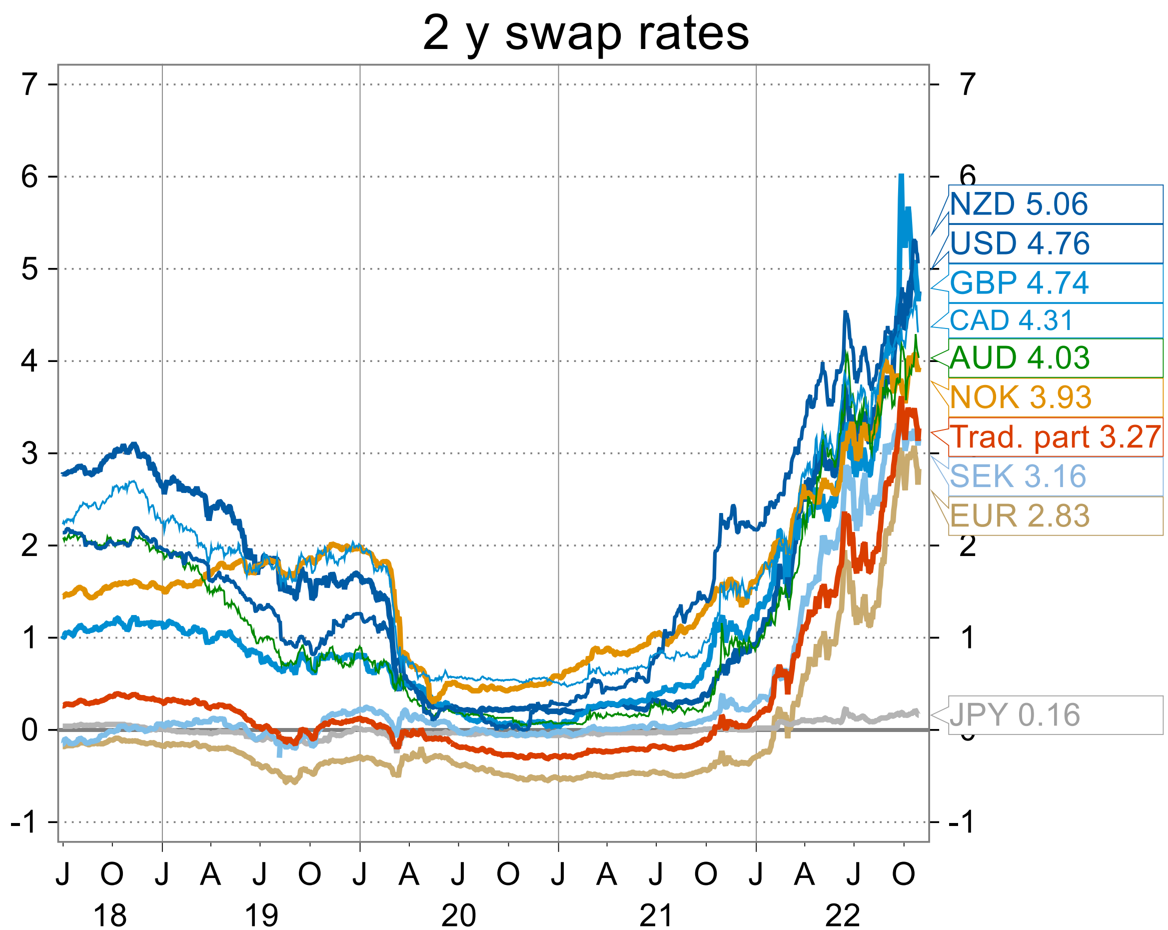




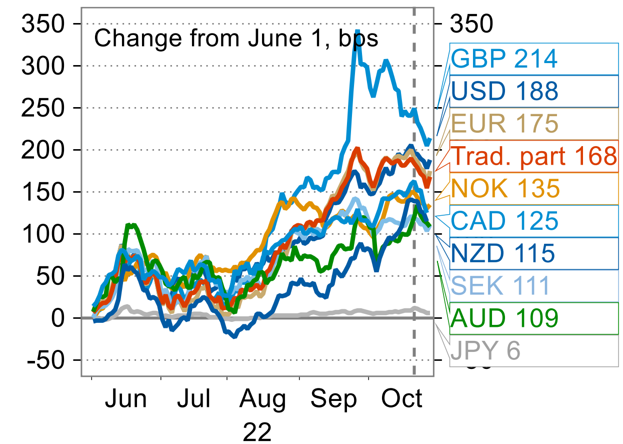


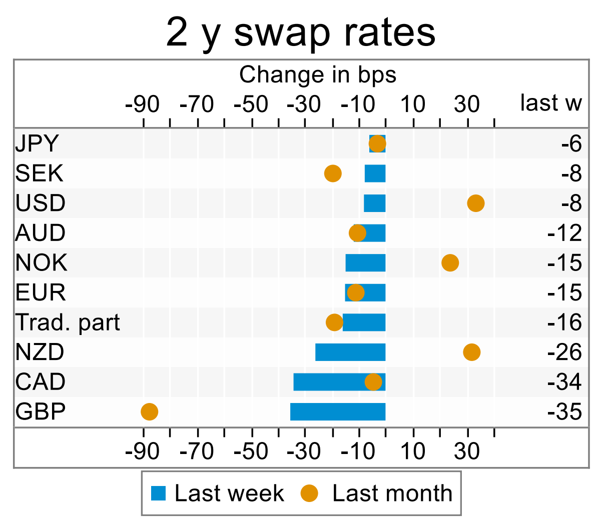
All 2 y swap rates down last week

GBP rates fell the most and there may be some more downside ahead



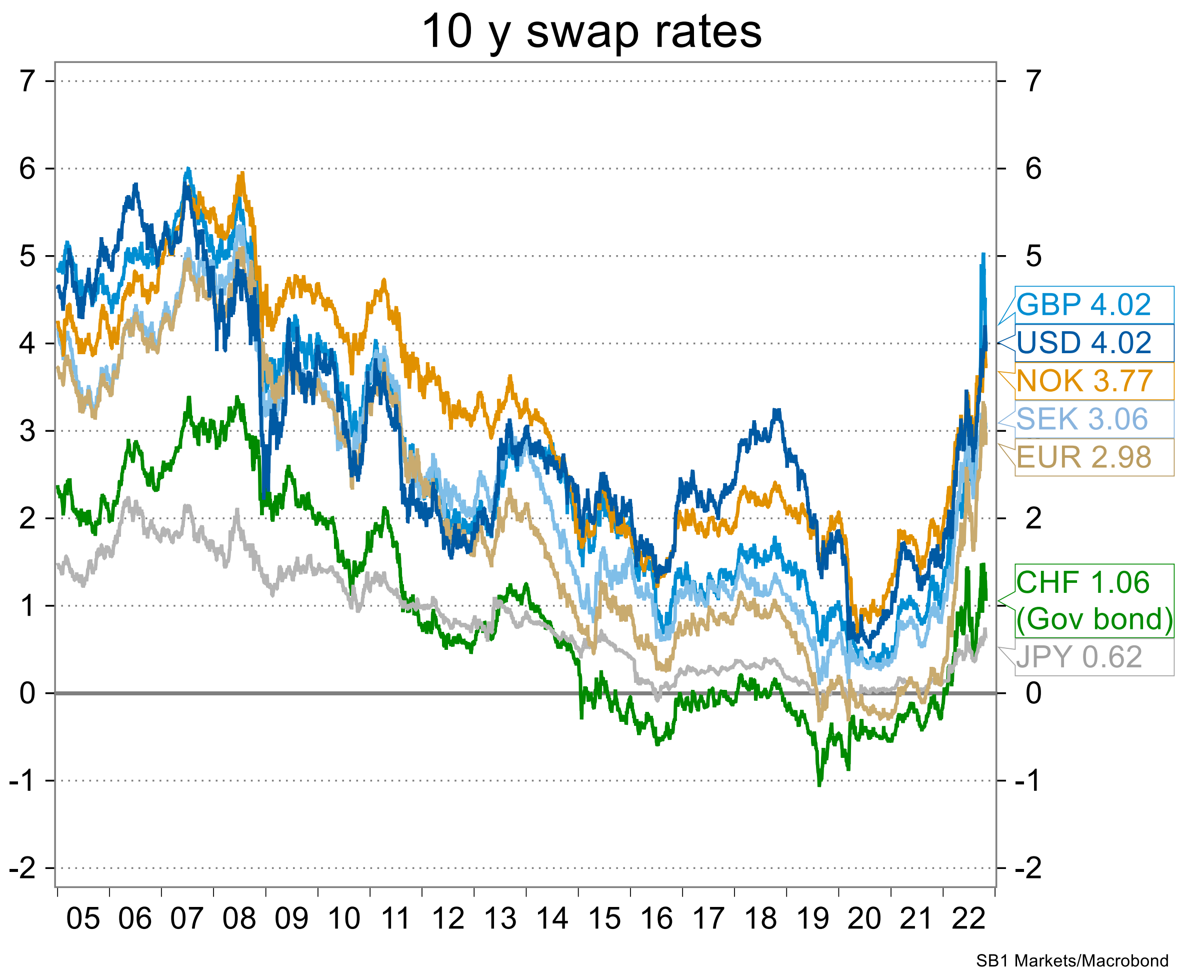
SB1 Markets/Macrobond

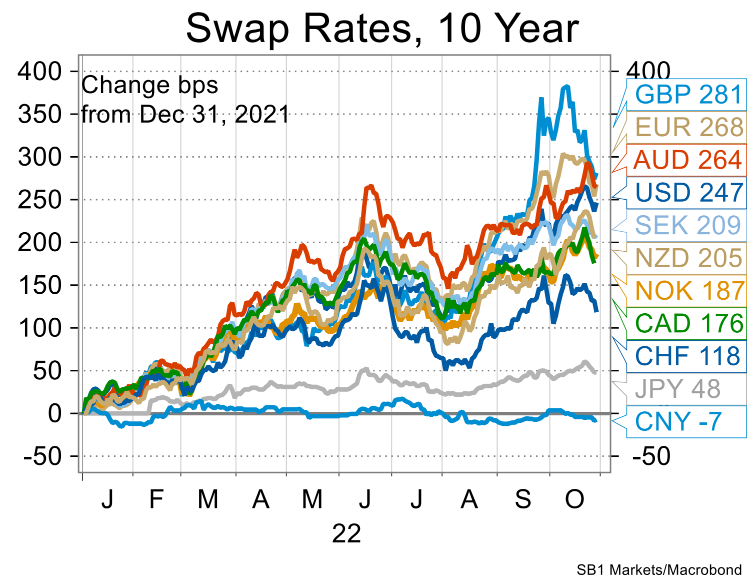


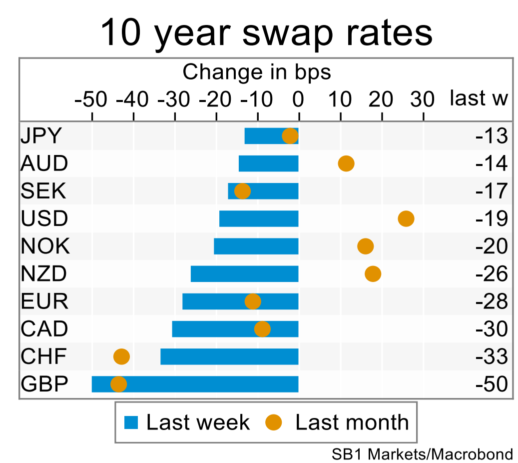


SB1 Markets/Macrobond

Down everywhere, the most in the UK, where rates are back to 'normal'



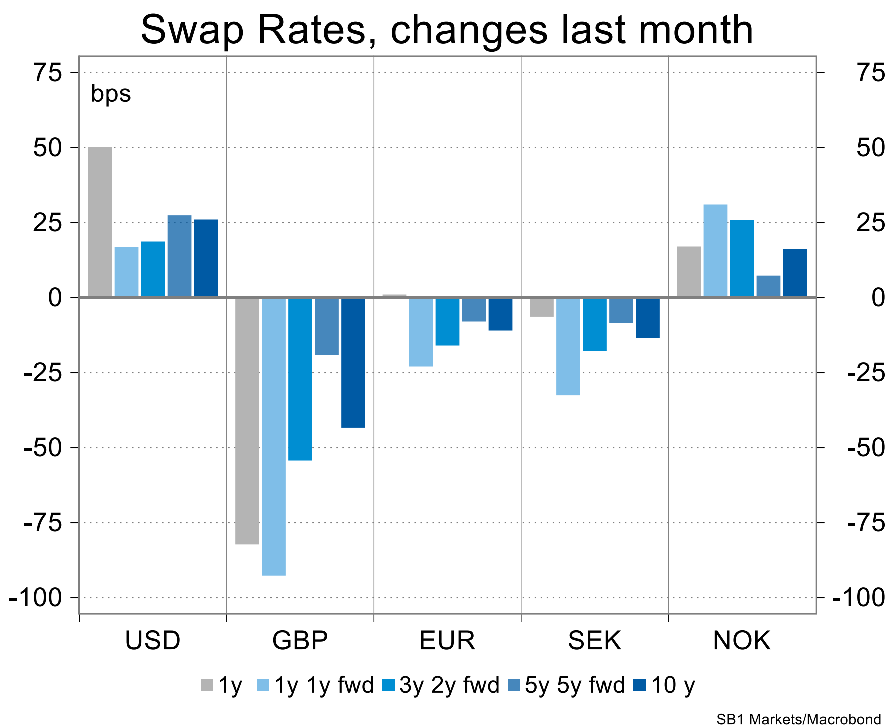


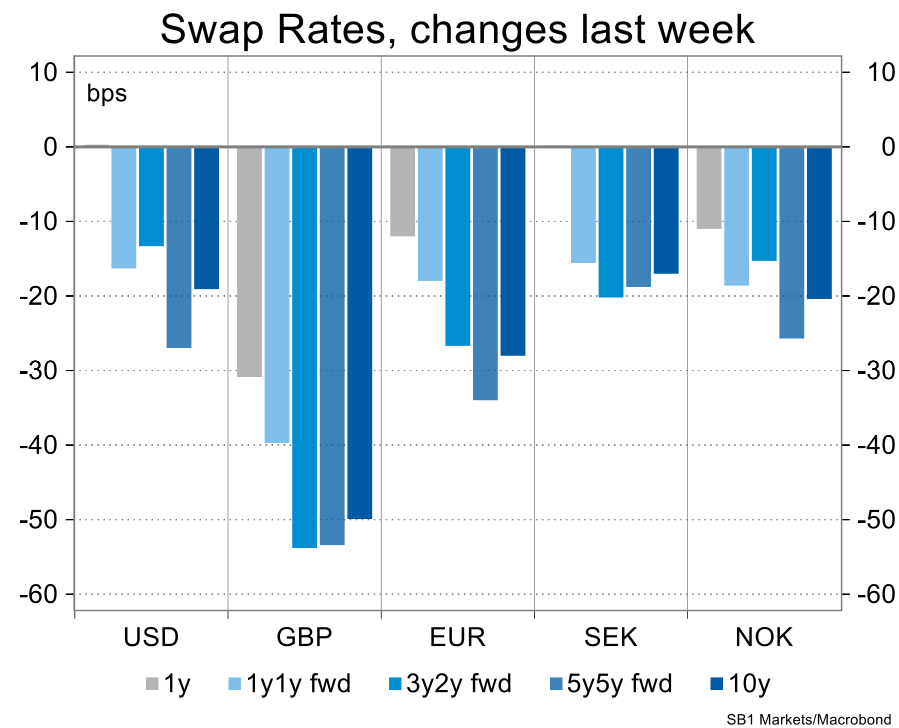


CHF: 10 y government bond yield

All rates down everywhere

In Norway somewhat less than among our trading partners



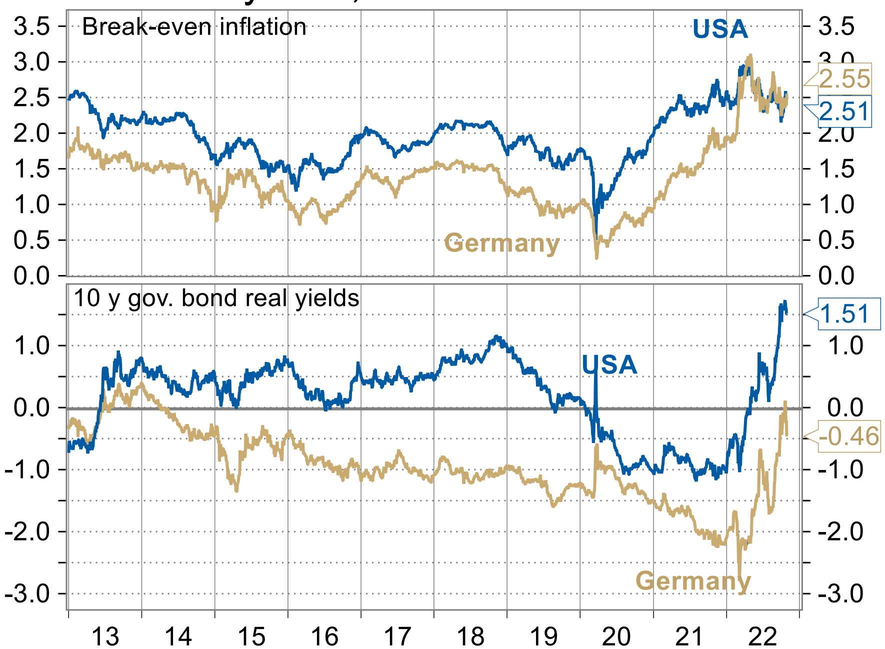


SpareBank 1 MARKETS

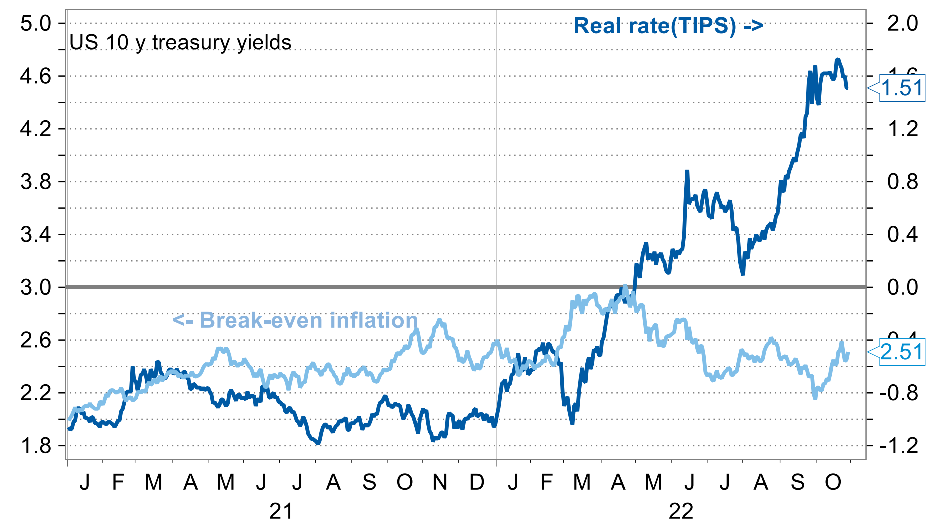
German 10 y real rate down 57 bps, US real rate -18 bps!

Inflation expectations rose 18 bps in Germany, unch. in the US

Real yields, break-even inflation



SB1 Markets/Macrobond



US & Germany 10 y Gov bond yield

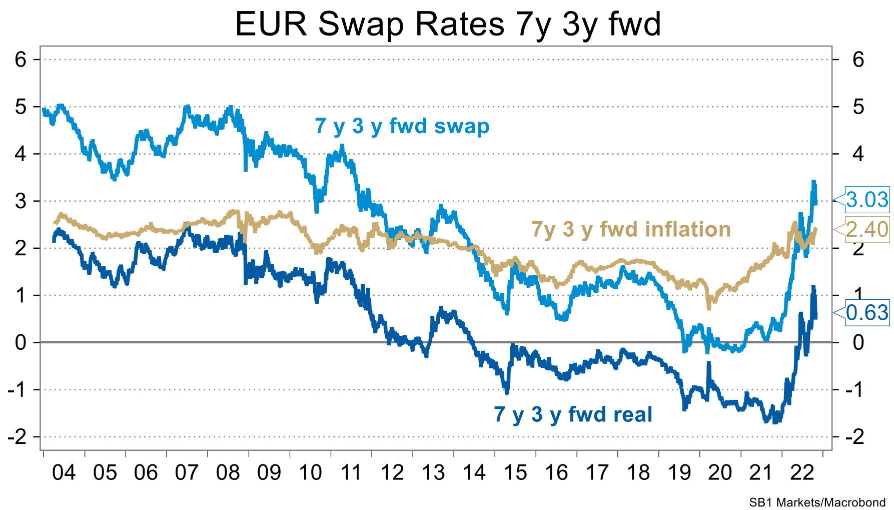
	Yield	Change 1w	Change 1m	YTD	Min since April-20
USA nominal treasury	4.02	-0.19	0.30	2.50	0.52
.. break-even inflation	2.51	-0.01	0.18	-0.05	1.06
.. TIPS real rate	1.51	-0.18	0.12	2.55	-1.19
Germany nominal bund	2.09	-0.39	-0.24	2.30	-0.65
.. break-even inflation	2.55	0.18	0.10	0.66	0.40
.. real rate	-0.46	-0.57	-0.34	1.64	-2.80

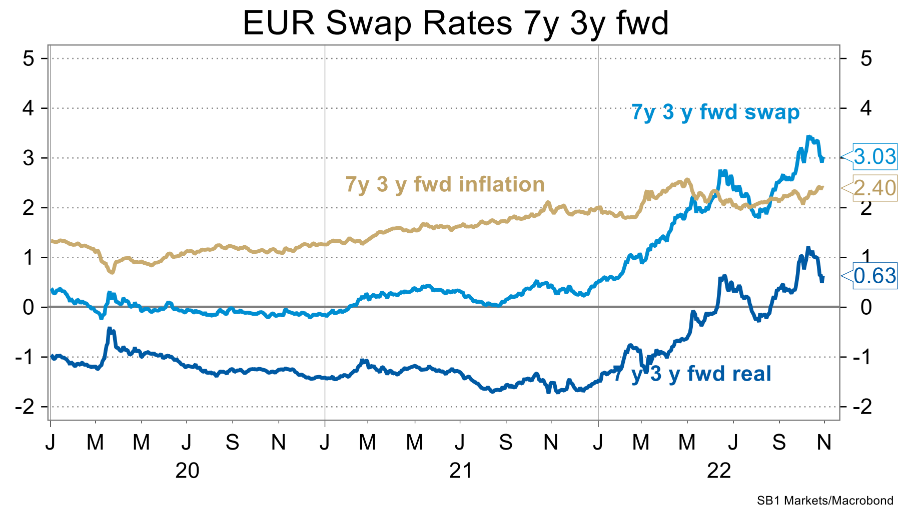
SB1 Markets/Macrobond

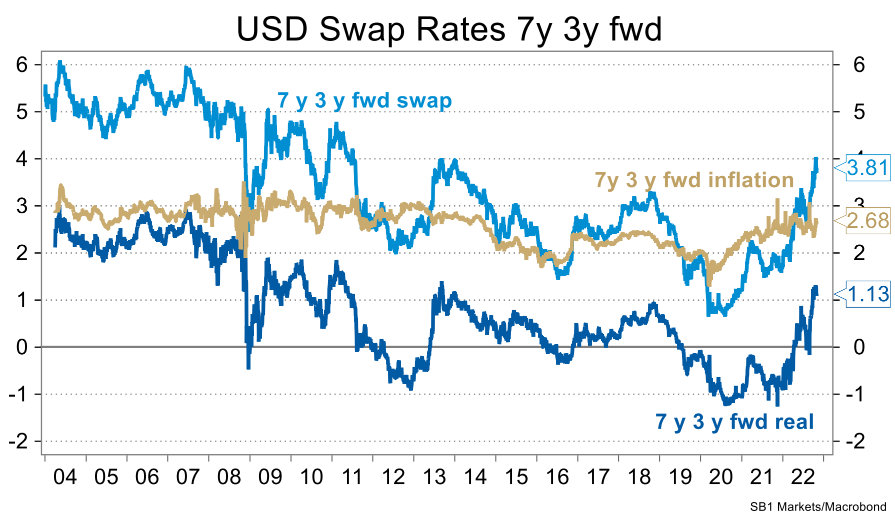
- The lift in real rates so far in 2022 is (still) one for the history books!
- No signs of war angst or flight to safety
- In the US, a 10 y CPI expectation at 2.51% is somewhat above Fed's 2% target for the PCE-deflator (which on average is some 0.3 pp below CPI inflation)

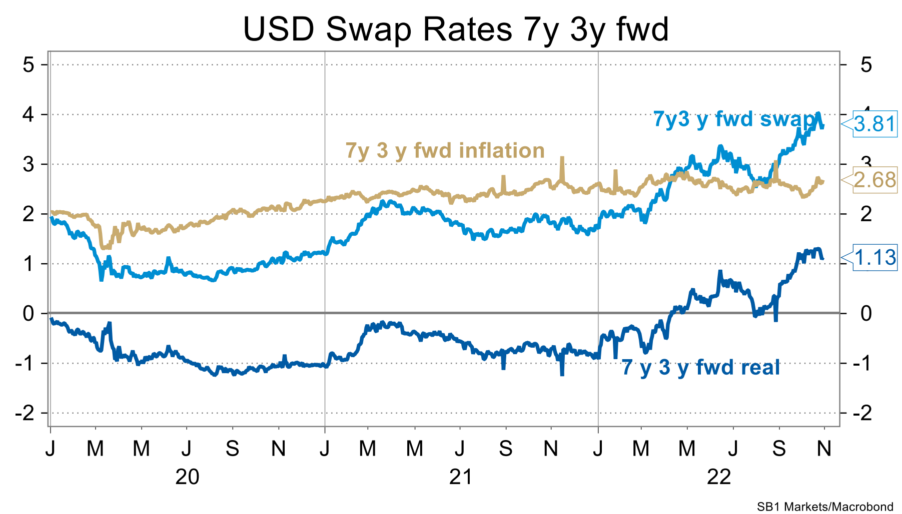
EUR real rates sharply down, 'long term' still at +0.6% (measured via the swap m)

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



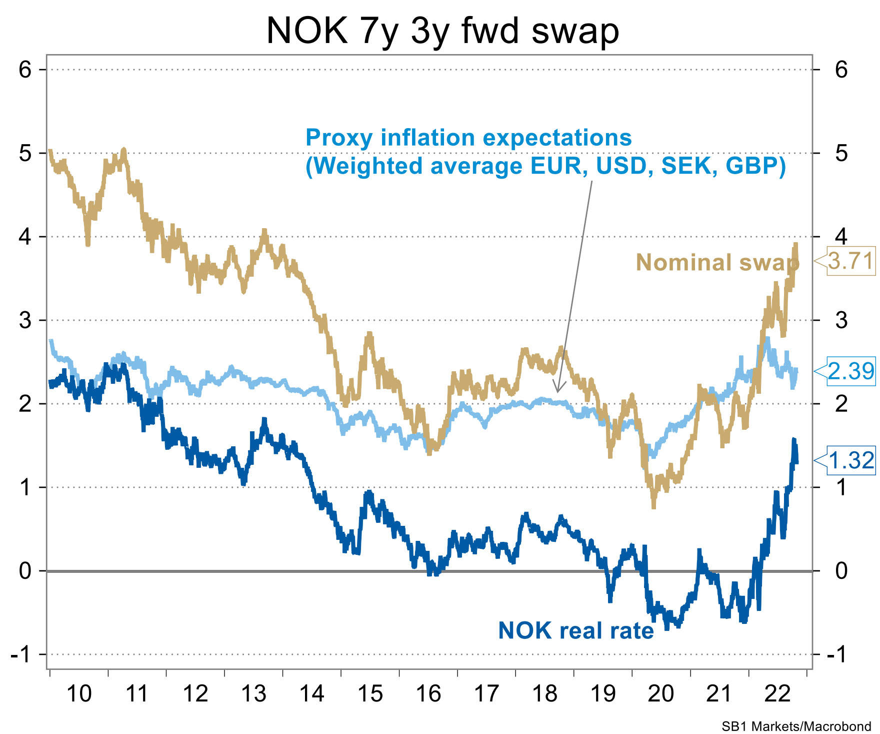


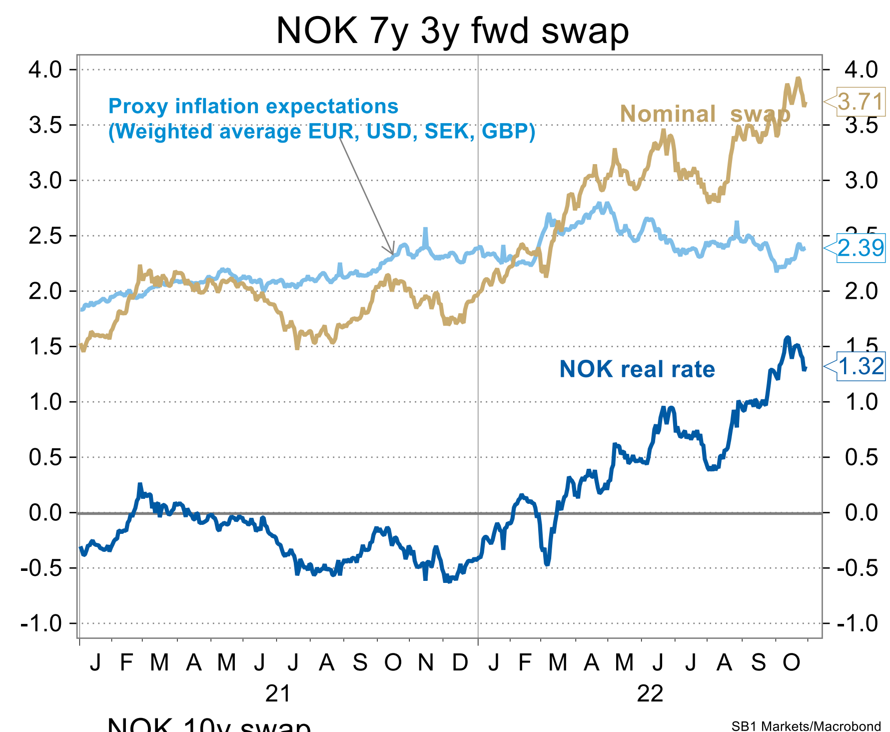


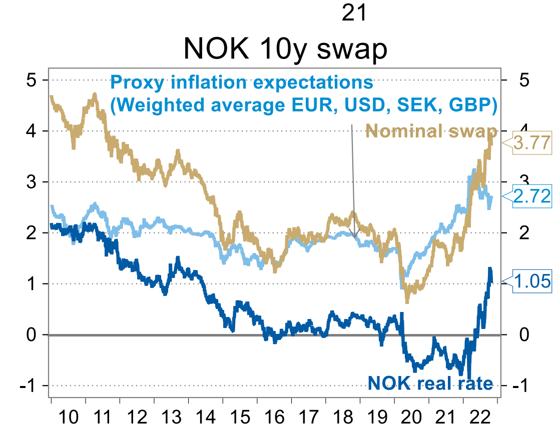


NOK real rates very likely down too

However, the trend is sharply up







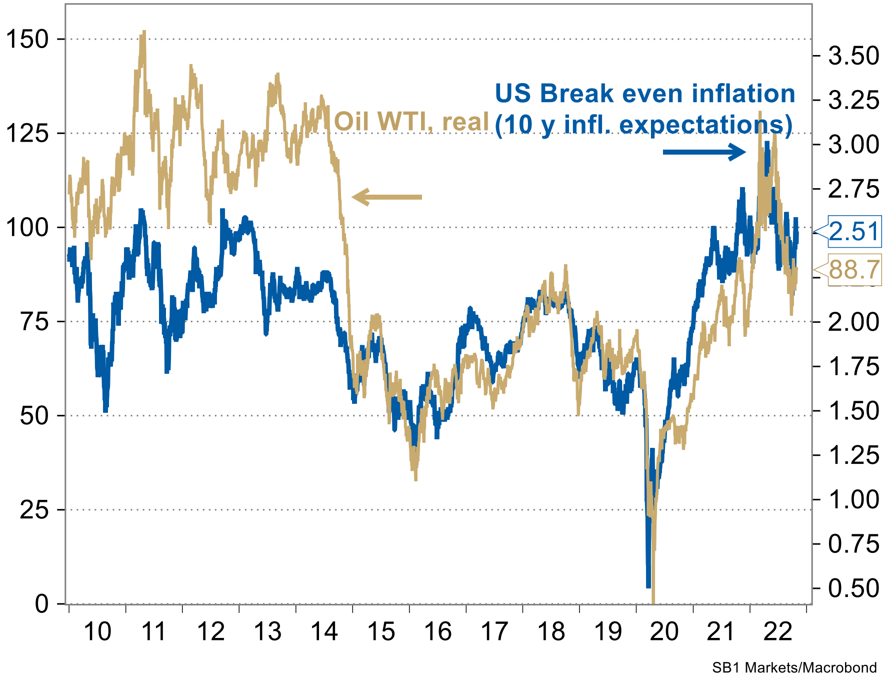
Memo: Our NOK inflation expectation proxy is a weighted average of EUR, SEK, GBP, and USD inflation swaps, cross-checked vs historical inflation differentials and inflation expectations from surveys

SpareBank 1 MARKETS

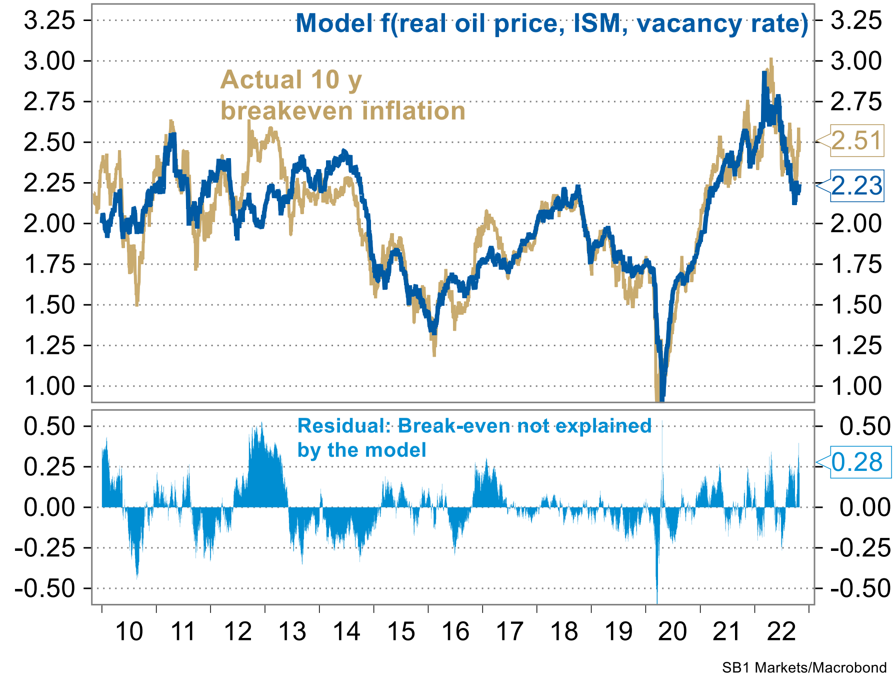
US inflation expectations are still too high?

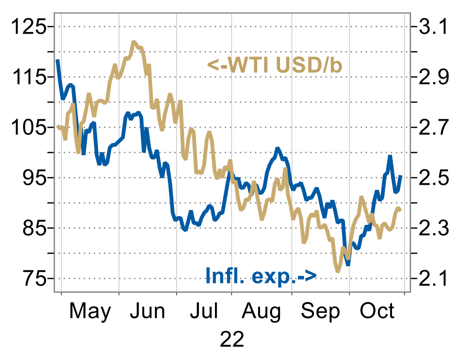
At least they are, vs our model estimate

USA Inflation expectations vs. the oil price



USA Inflation expectations vs. the oil price, CPI

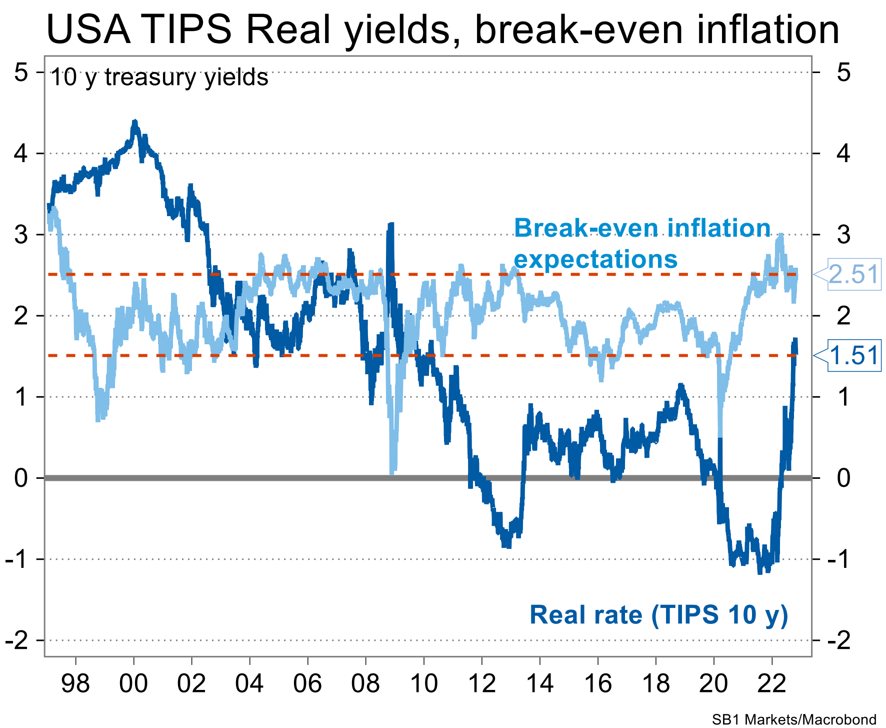


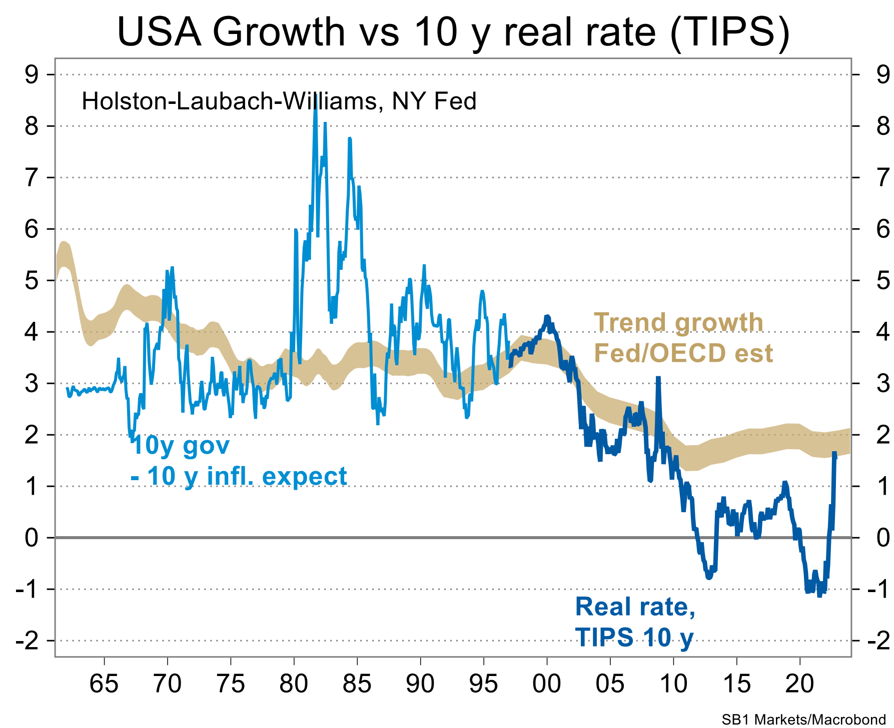


- A simple model including the <u>spot</u> oil price, the <u>current</u> ISM and the <u>current</u> vacancy rate pretty well explains the <u>long-term</u> breakeven inflation expectation in the bond yield curve
- What now? We are uncertain about the oil price, but rather confident that both the ISM, 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

Growth vs real rates: The gap has closed!

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

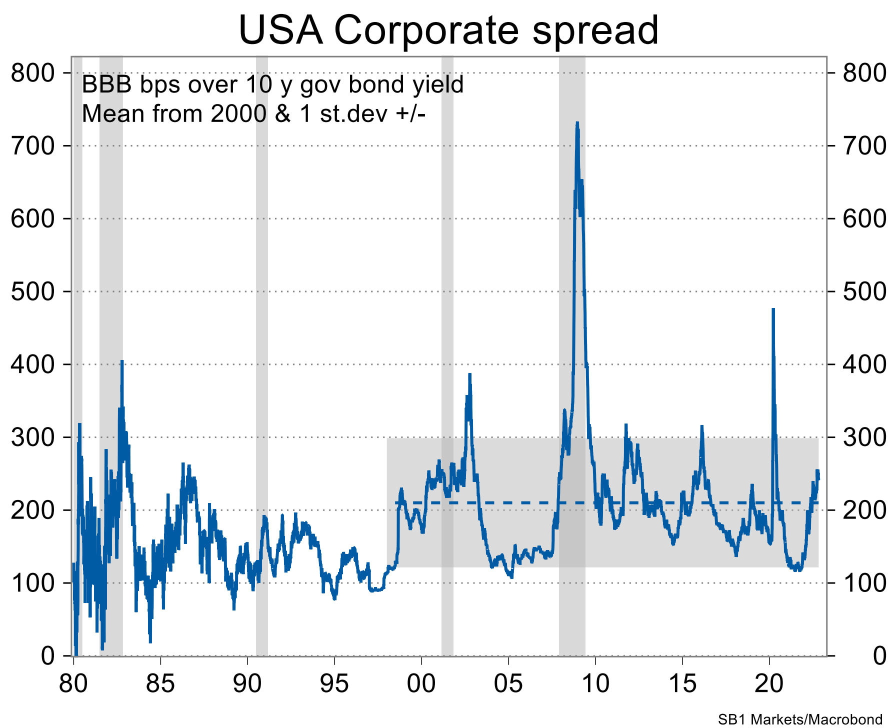


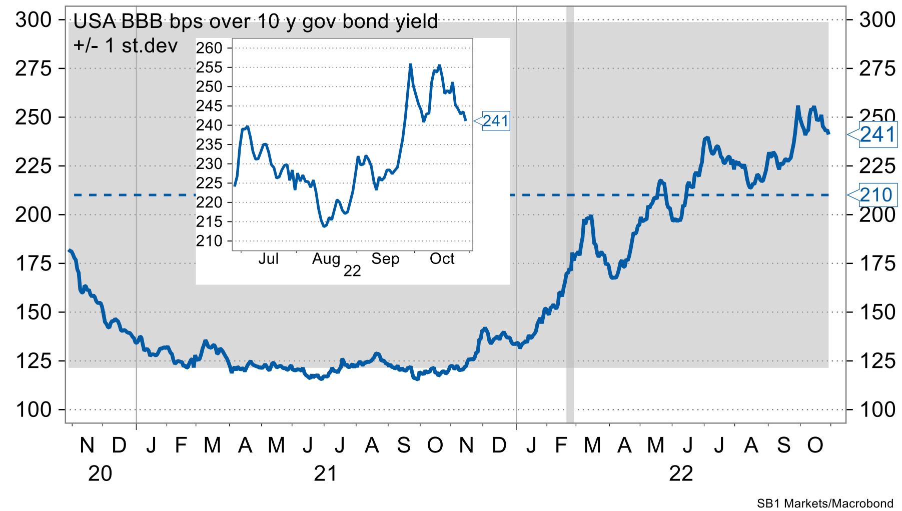


SpareBank 1 MARKETS

Risk on: Credit spreads further down!

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

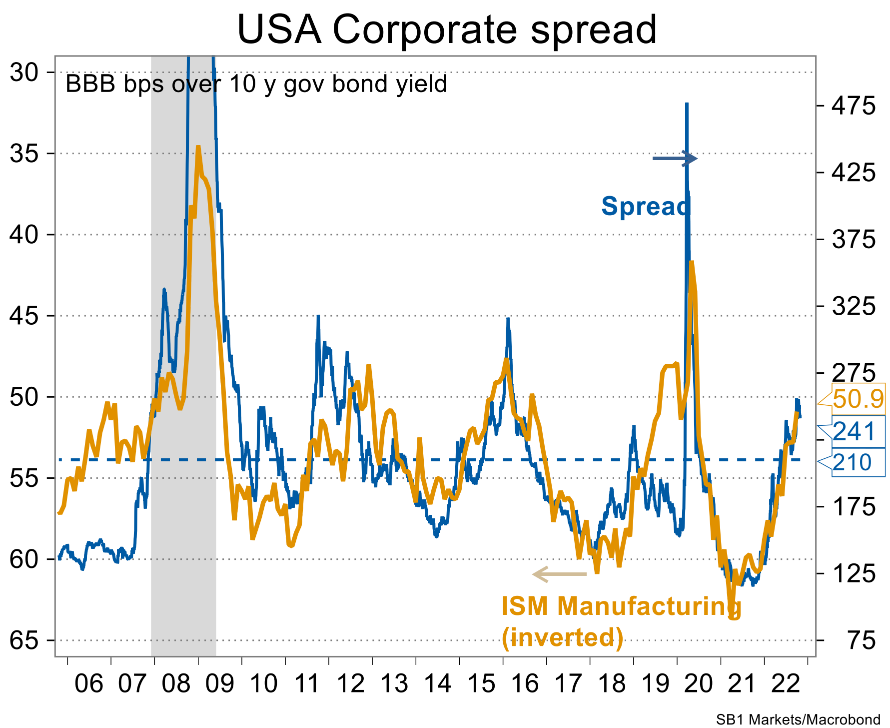


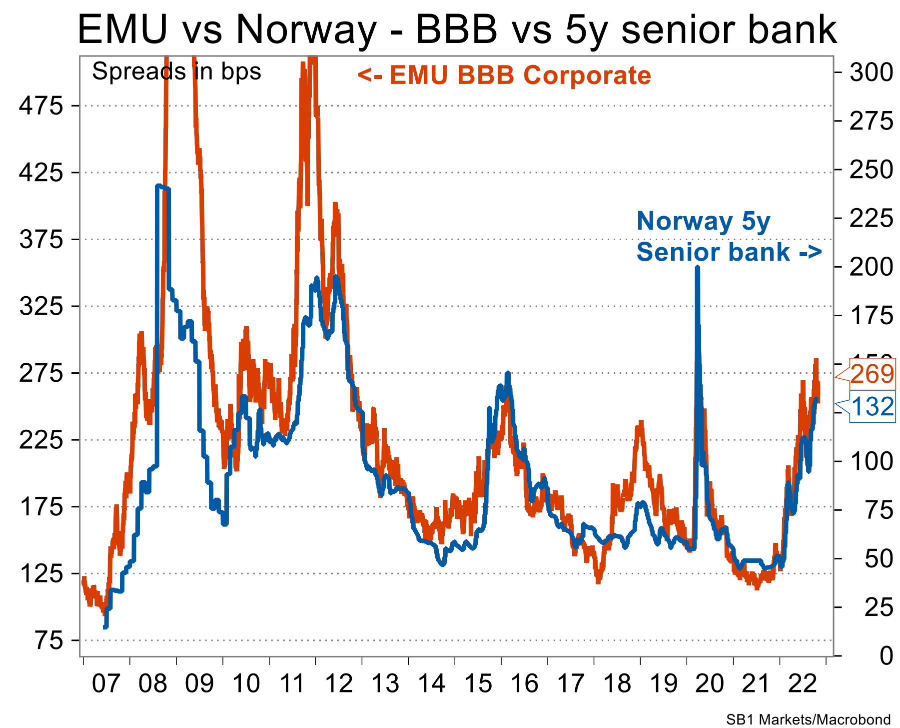


- The US BBB spread is up 120 bps from the bottom last autumn, more than a doubling
- In addition, real rates have increased by 270 bps from the bottom late last year
- Thus, the basis for all valuation metrics has changed dramatically, check the chart two pages forward!

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

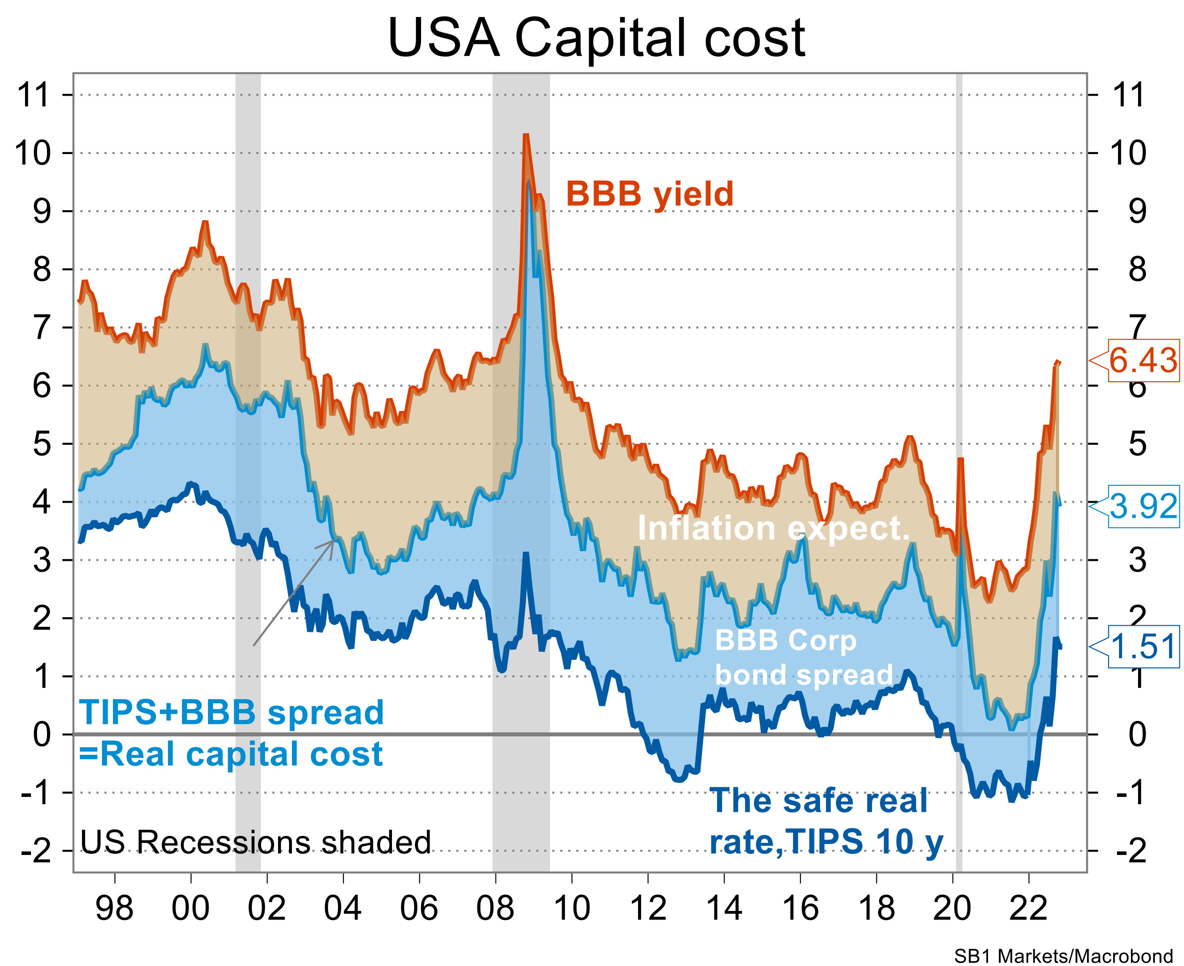




- The answer is not irrelevant for your view on the outlook for spreads, we think
- And do you think Norwegian spreads will be influenced by changes in the global credit market?
- Last week: Norwegian credit spreads rose in sympathy with higher spreads abroad the previous week
- The good news: The recent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

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

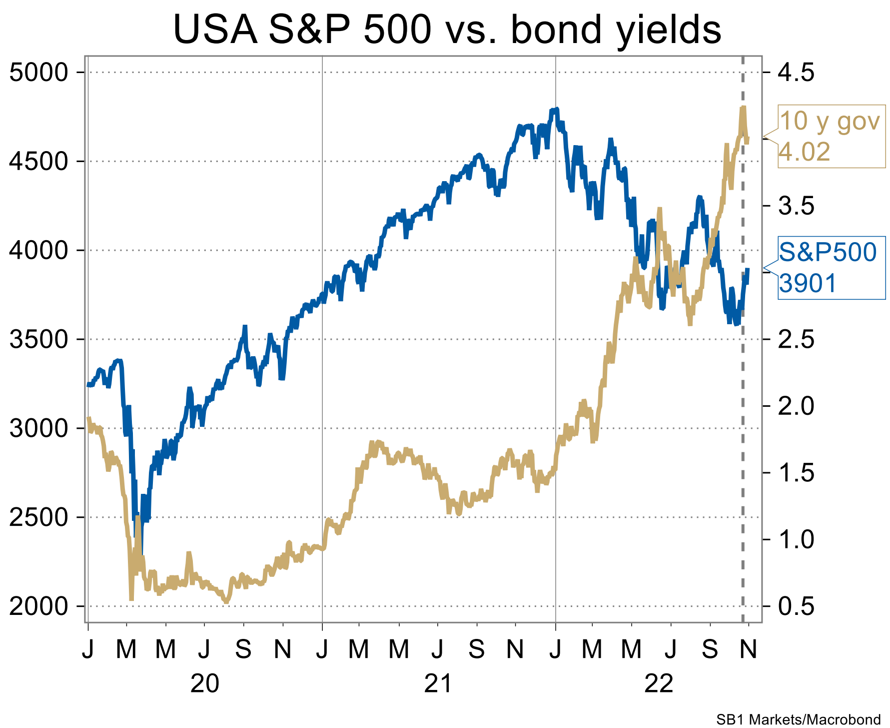
All valuation metrics have changed dramatically. *As have all calculations of return on capital*

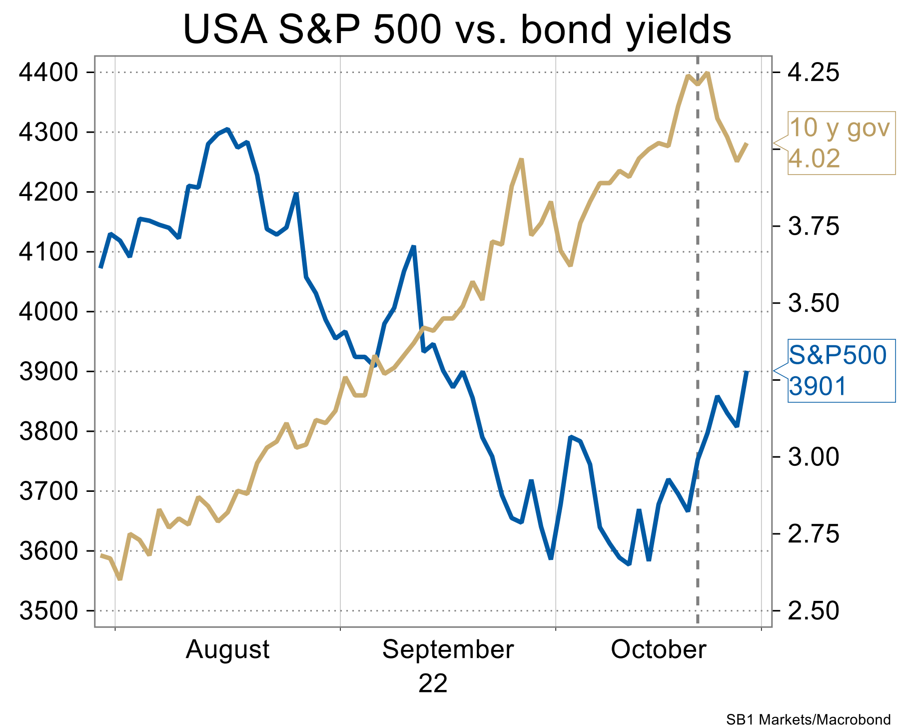


- Spreads and real rates fell last week but the story remains intact
- The total real borrowing cost for a BBB company has increased to 3.9% bps from zero by the end of last year:
  - » The TIPS real rate is up from -100 to + 151 bps
  - » The BBB corporate investment grade spread is up from 120 bps to 241!
- 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 further up, as bond yields fell

The 10 y bond yield -18 bps, the S&P500 gained 4.0%, and is up by 9.1 from the Oct 12 trough



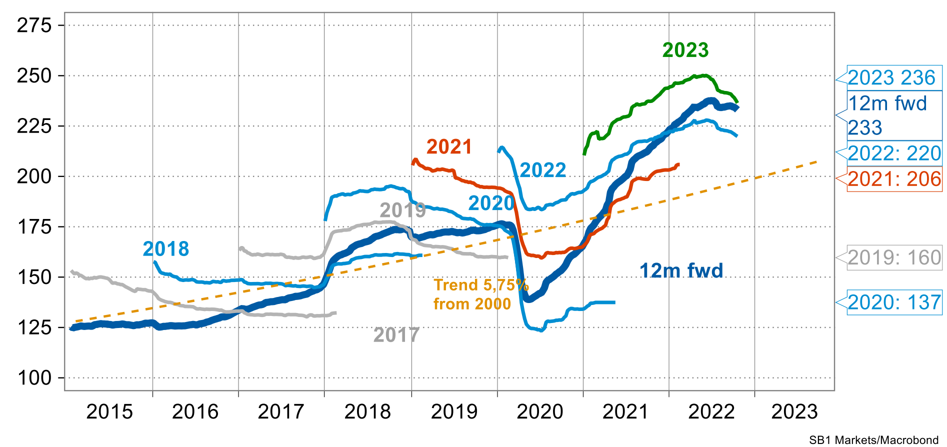


- Bond volatility has surged recent weeks/months, to levels not seen in 15 years. 'Something' is going on

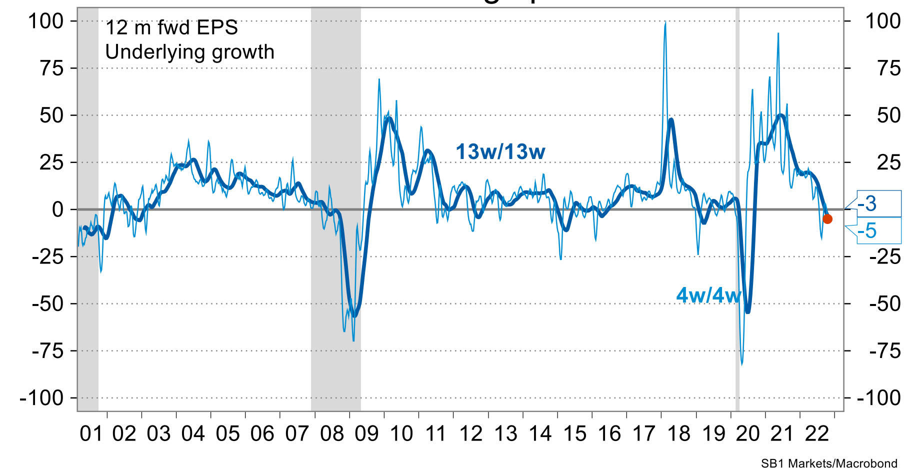
Earnings forecasts are heading down again, still much more to go

S&P 500 expected 12 m fwd EPS was some 15% above trend and has just fallen some 5%

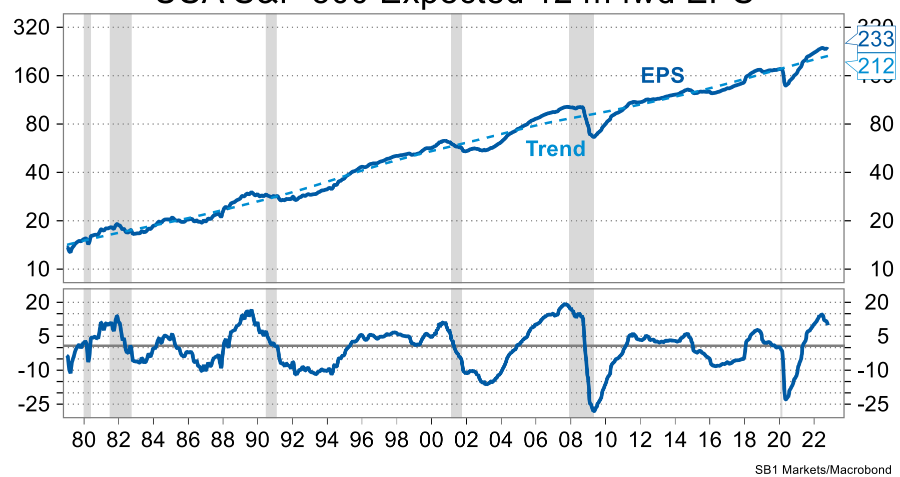
Annual S&P 500 EPS consensus (Factset)



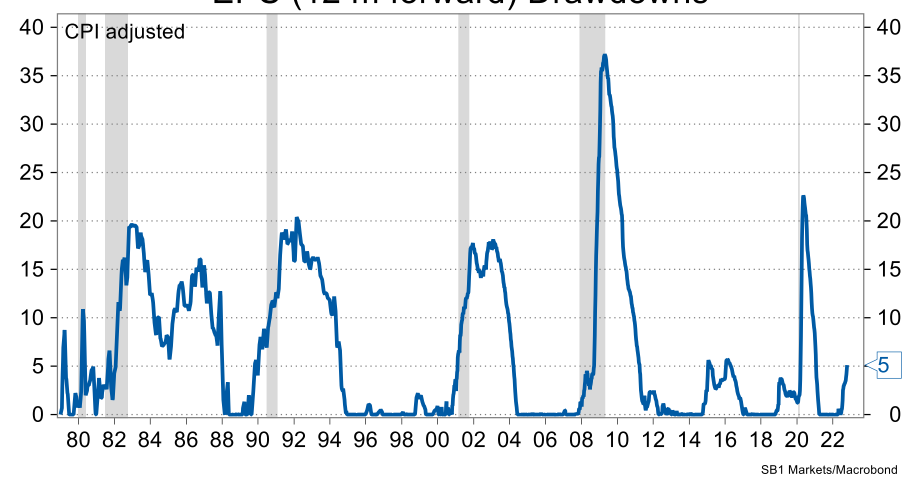
S&P500 Earnings per share



USA S&P 500 Expected 12 m fwd EPS

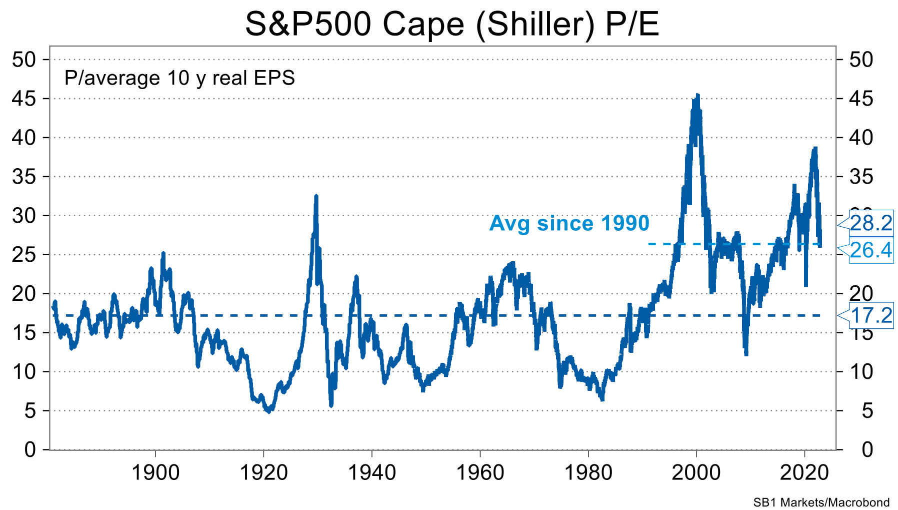


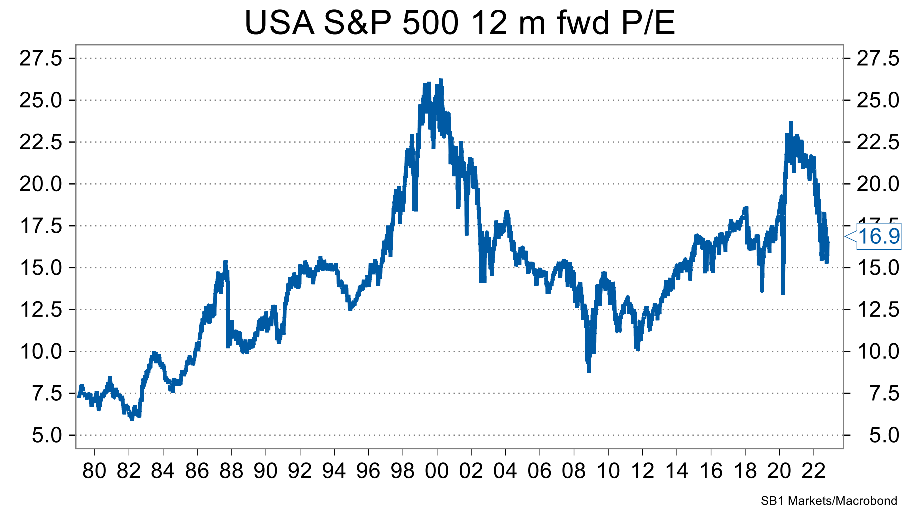
EPS (12 m forward) Drawdowns

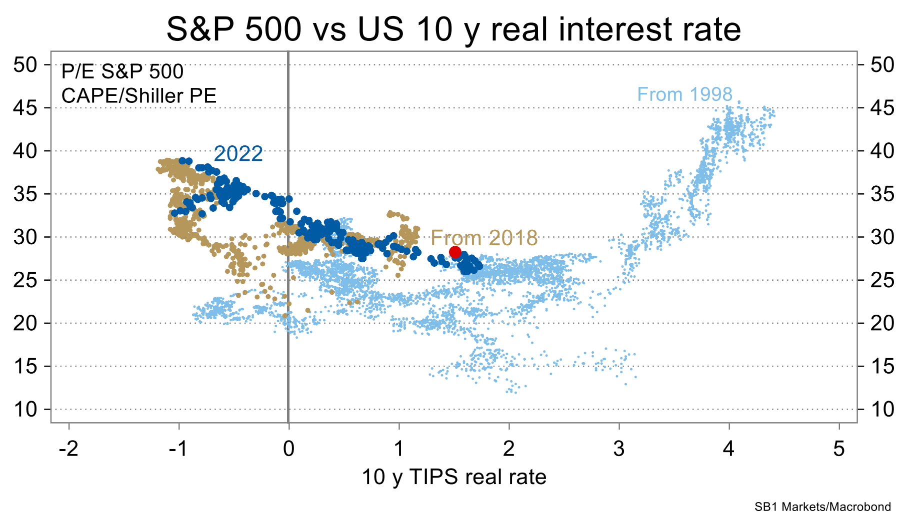


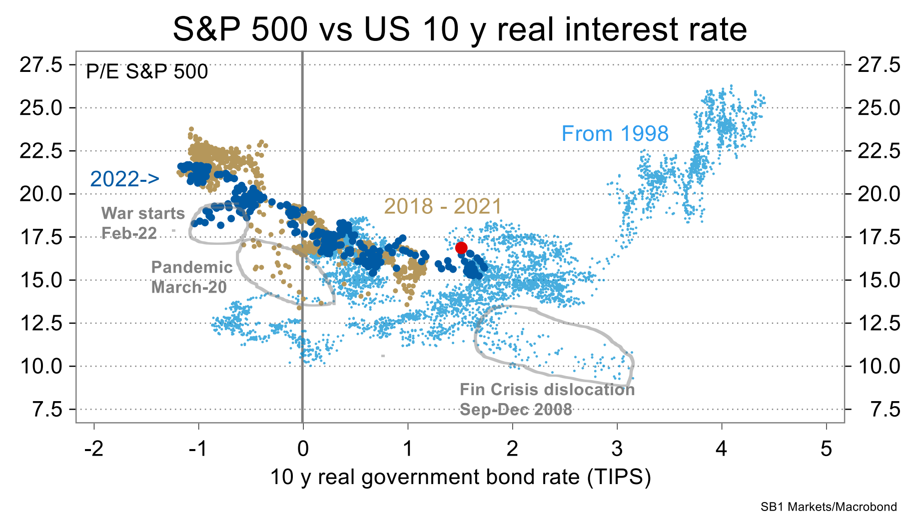
4 valuation charts: Check the extreme tight correlation between real rates, P/E

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



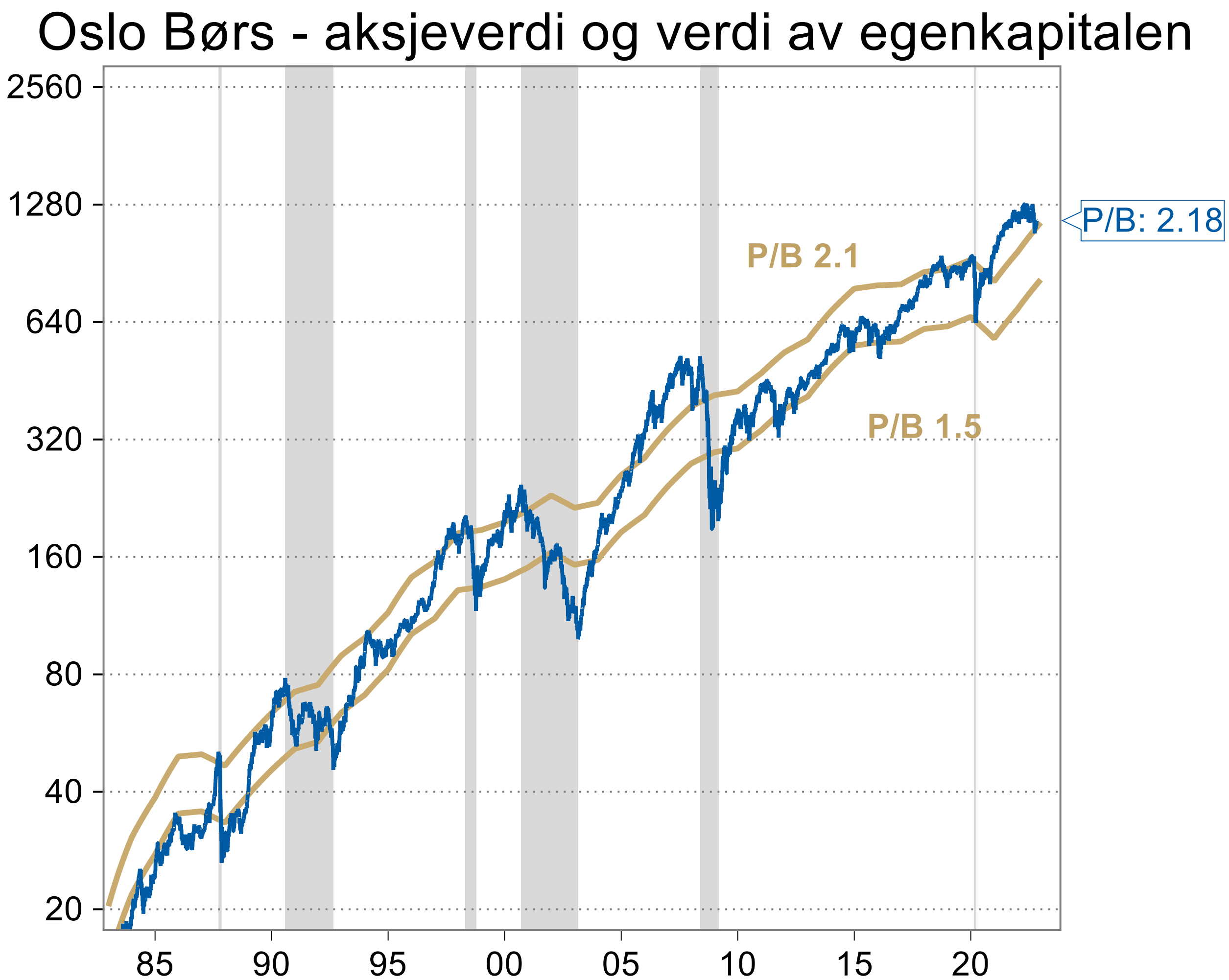




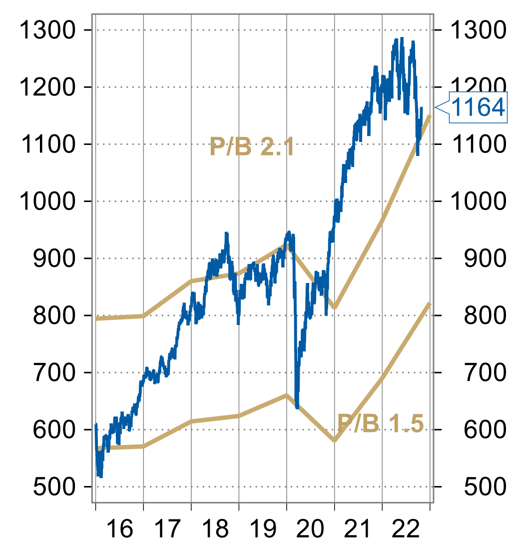


Finally, OSEBX almost hit the upper band of the 1.5/2.1 Price/Book corridor

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



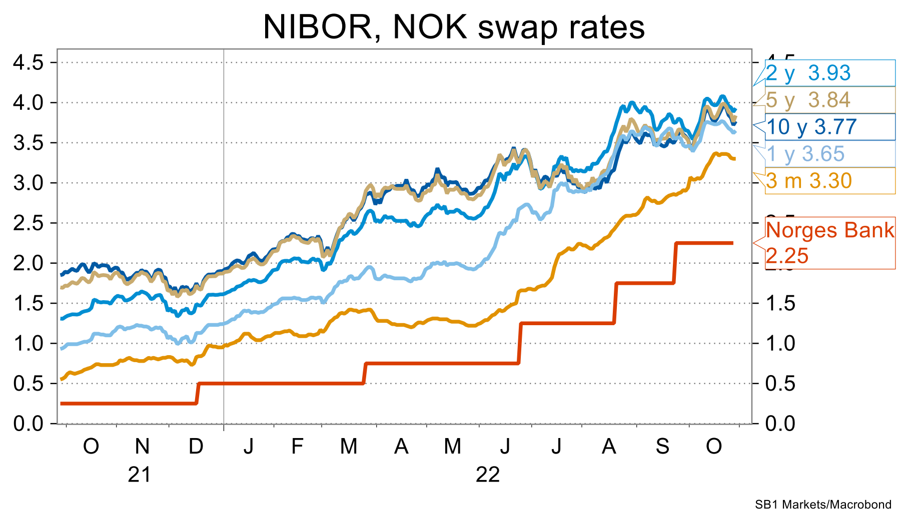
Source: Oslo Børs, Vital, Bloomberg, SB1 Markets, Macrobond.

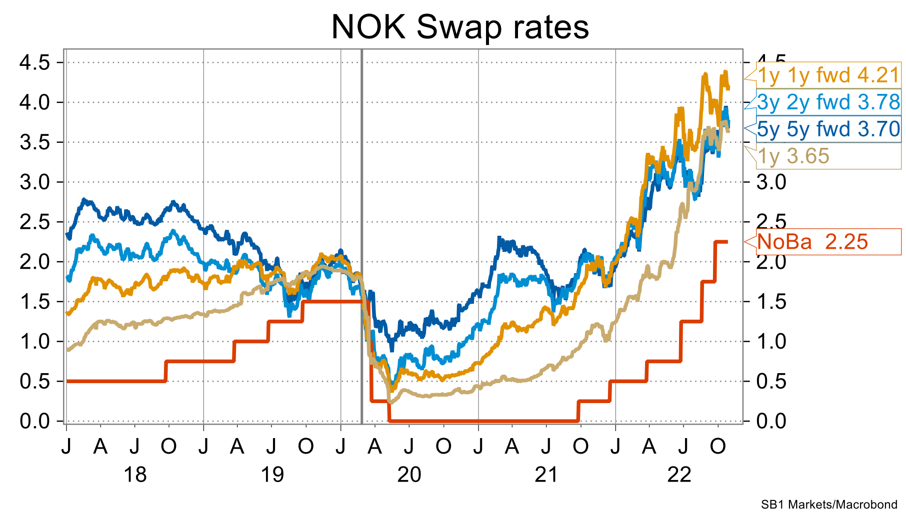


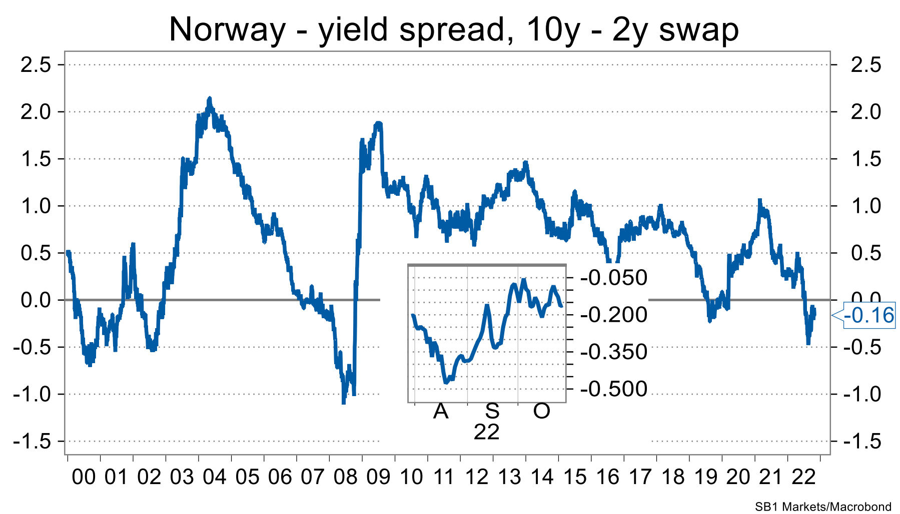
Source: Oslo Børs, Vital, Bloomberg, SB1 Markets, Macrobond.

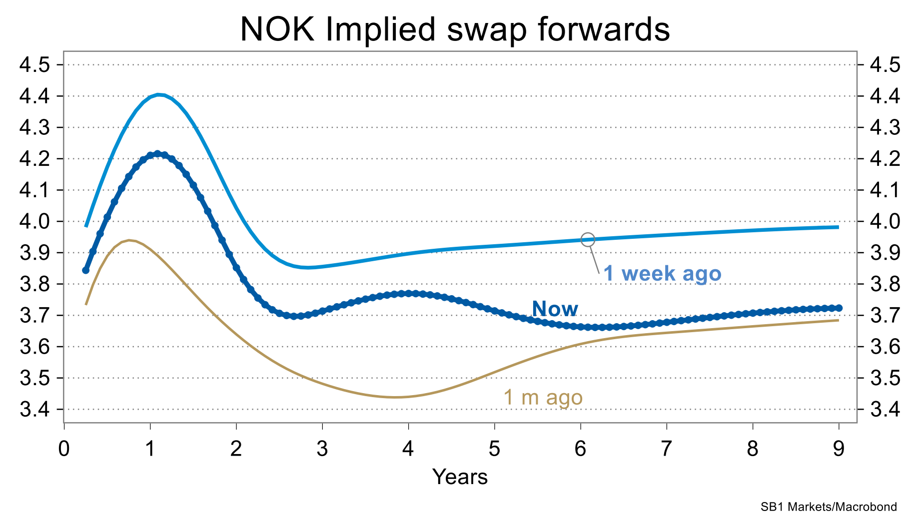
Norwegian swaps down all over the curve, by up to 25 bps

The 3m NIBOR down 6 bp to 3.30% but the larges decline 5 y 5y fwd





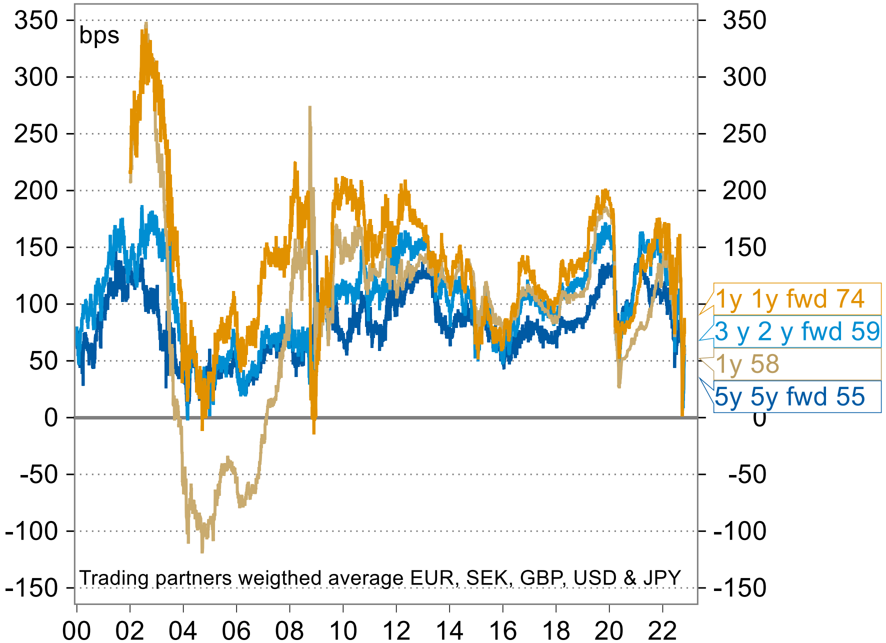


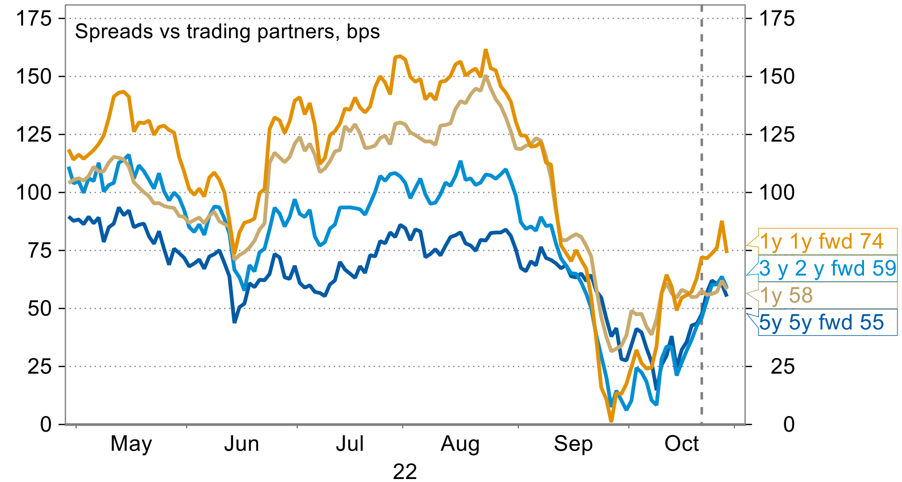


NOK rates fall a tad less than among our trading partners, spreads further up

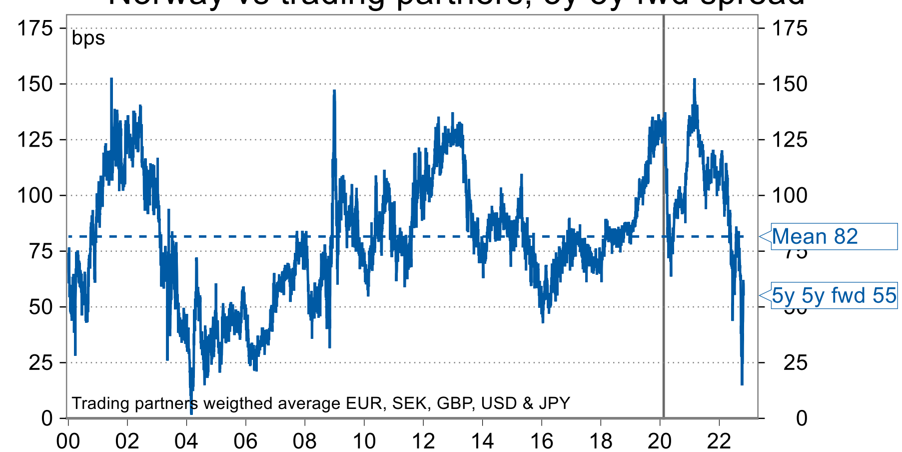
Spreads are still at reasonable levels, we do not have a case

Norway vs trading partners, impl swap spreads





Norway vs trading partners, 5y 5y fwd spread



- NOK rates are still above the average level among our trading partners – but the margins fell sharply in September. In October, spreads have widened somewhat but they remain well below an average level
- Still, spreads have in average been wider than we think they will be the coming years, at least as soon as the oil/gas boom deflates at some stage

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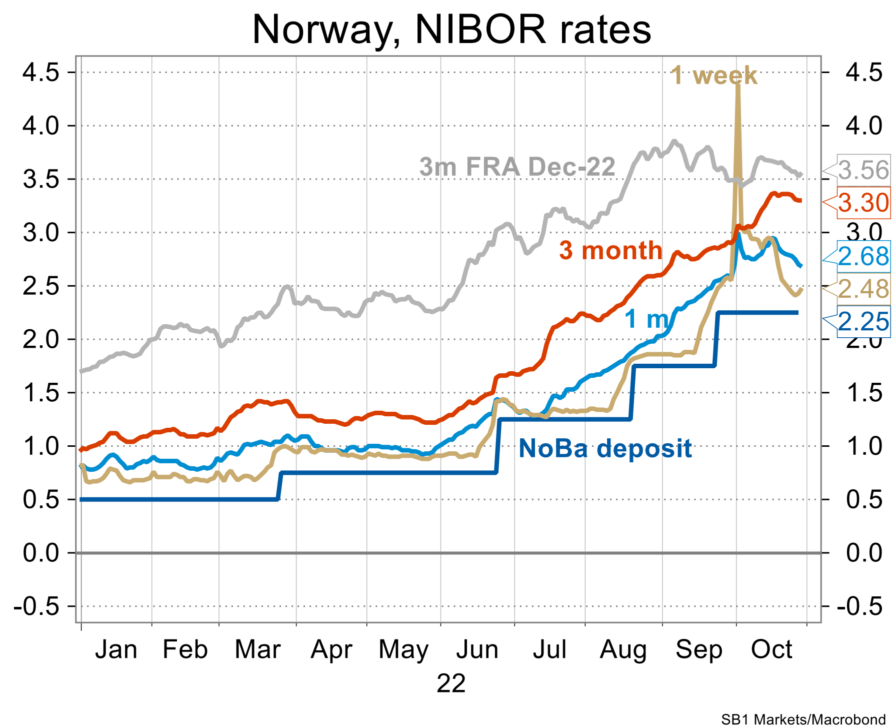
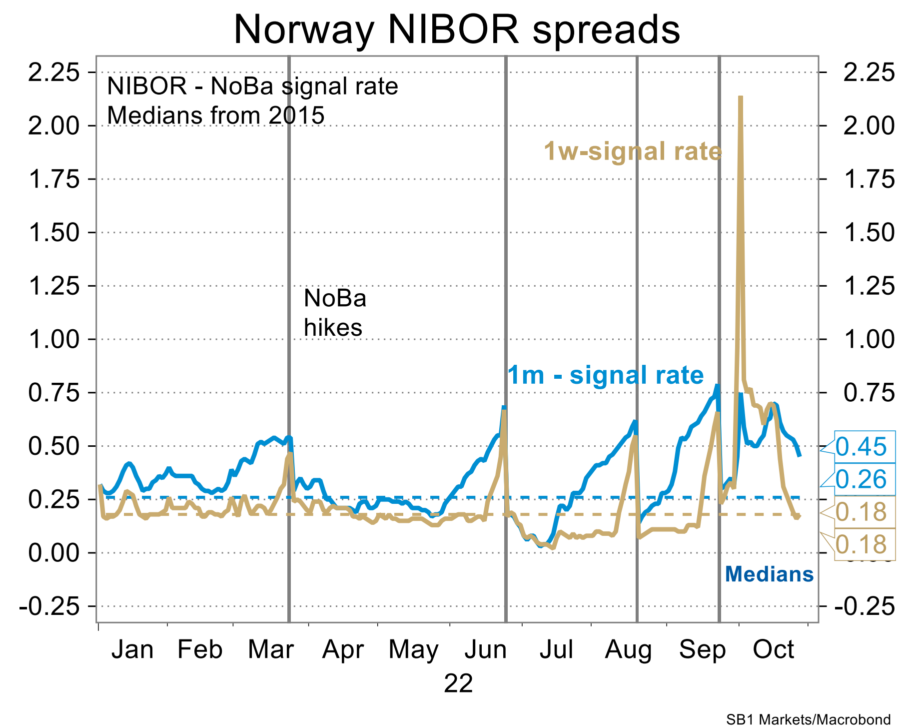
NIBOR spreads have normalized, the 1 w spread is back to an average level

Given that a 50 bps Nov 3 NoBa hike is discounted, the 1 m NIBOR spread is at a normal level

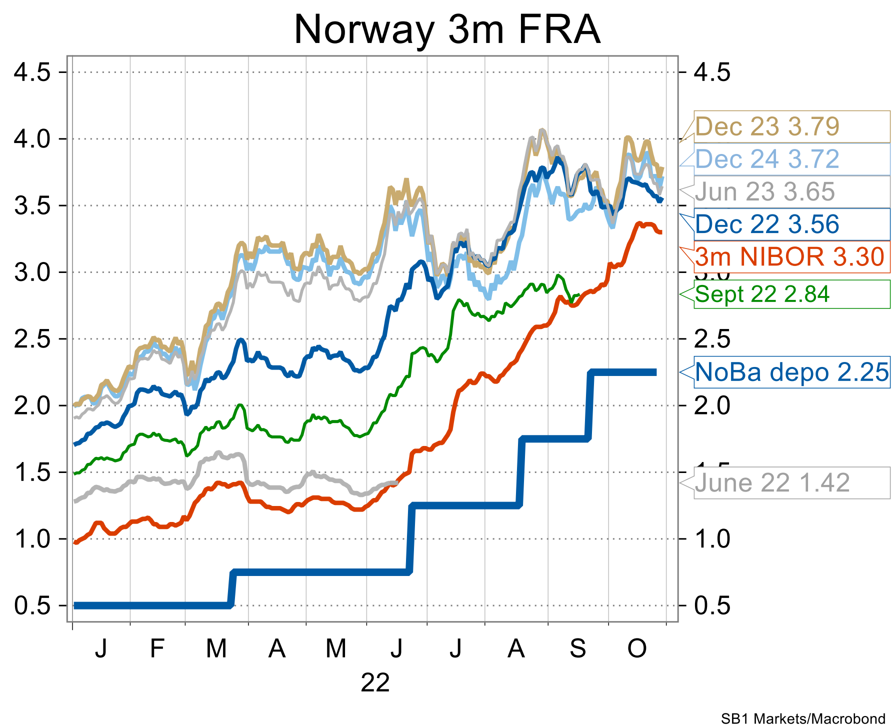


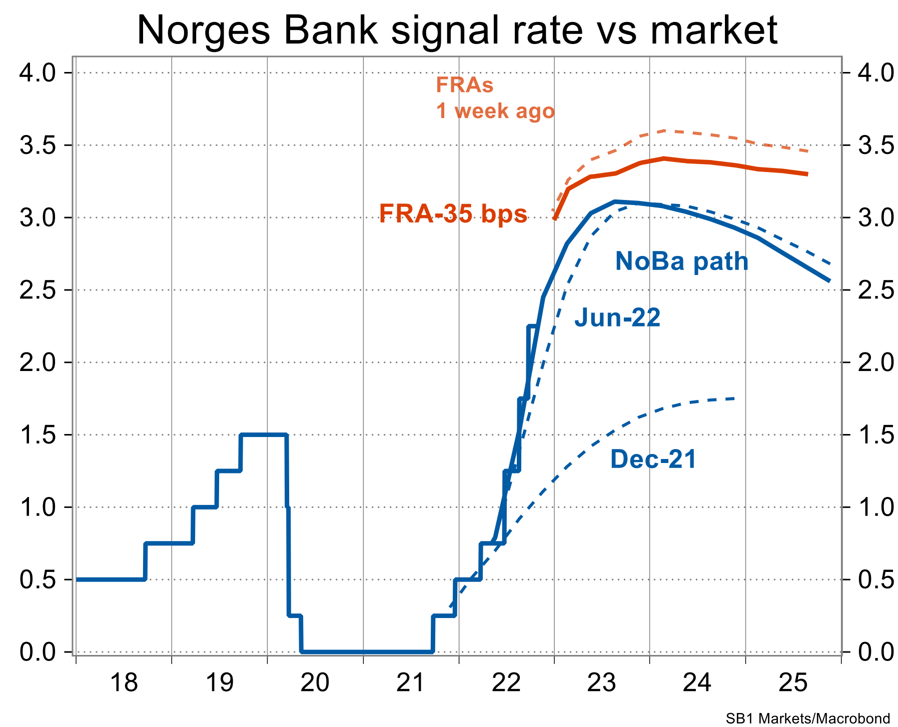


- Which signals that the longer term NIBOR spreads are at normal levels too
- If so, the FRA-rates adjusted for a ‘normal’ spread at some 35 bps, reveal the market’s expectations for Norges Bank’s signal rate

FRAs down 6 – 19 bps. Still a 50 bps hike is discounted now, and 60% for +50 in Dec

We think FRAs rates are still to aggressive, even after the recent decline

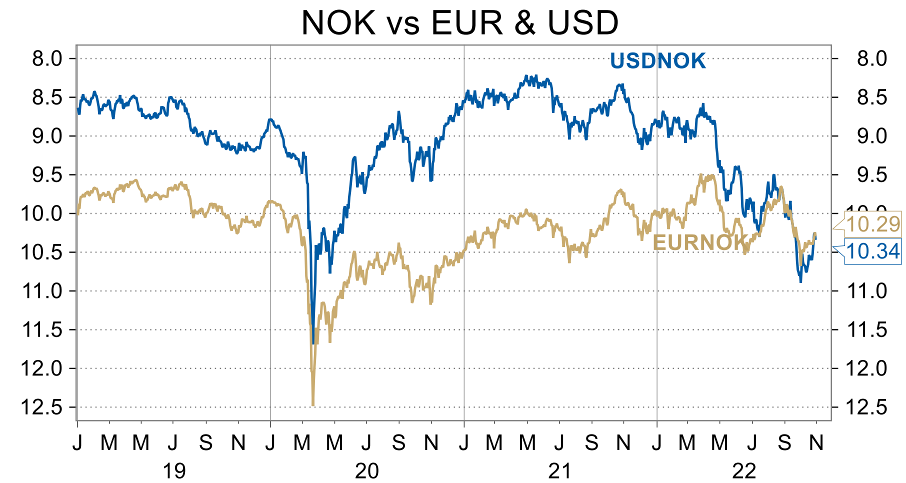


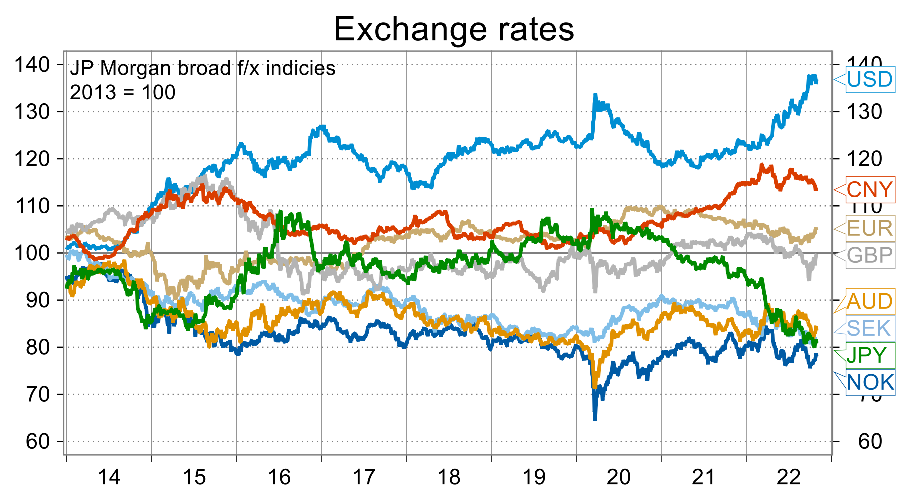


- Given the current 3 m NIBOR at 3.30% and the Dec-22 3 m FRA at 3.56% (both down 6 bps last week), the market still discounts a 50 bps hike at Thursday, and 60% for another 60 bps hike in December (given 25 bps as the alternative) – assuming a normal 35 bps 'underlying' NIBOR spread and the 'normal' 5 bps extra end of year spread
- A 50 bps NoBa hike would not surprise us much – even if we deem a 25 bps hike to be more appropriate – but the upside risk vs the FRA path is very limited. If NoBa hikes by 50 bps, it is very likely that the bank in the press release or at the press conference (extra service from the bank these busy rate days) will signal that another 50 bps in December is a done deal

The GBP strengthened further, no more Truss angst. USD, CNY down

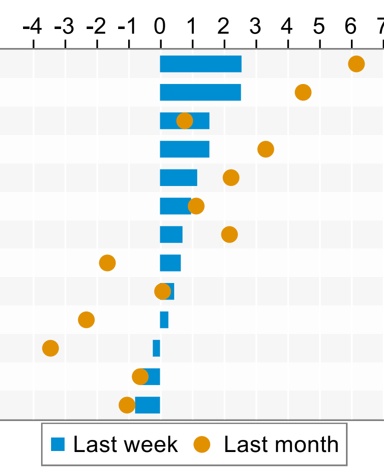
NOK further up, together with AUD, CAD & SEK





F/x markets

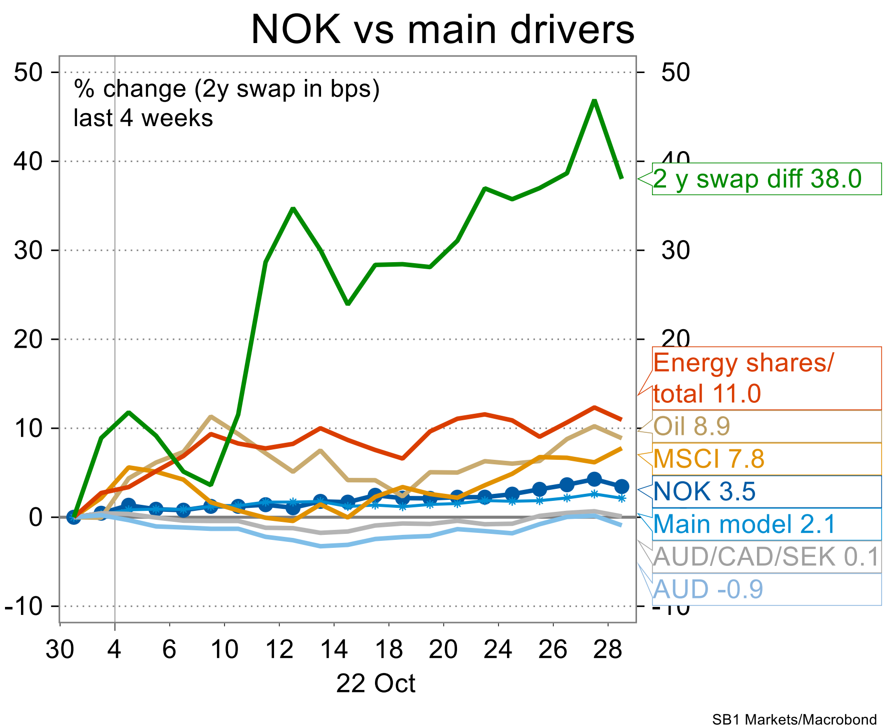
JP Morgan f/x broad indices + 3 f/x crosses	Last week	Last month
GBP	2.6	6.2
NOKUSD	2.5	4.5
SEK	1.6	0.8
EURUSD	1.6	3.3
NOK	1.2	2.2
NOKEUR	1.0	1.1
EUR	0.7	2.2
AUD	0.7	-1.7
CAD	0.4	0.1
JPY	0.3	-2.3
CHF	-0.2	-3.4
USD	-0.6	-0.6
CNY	-0.8	-1.0

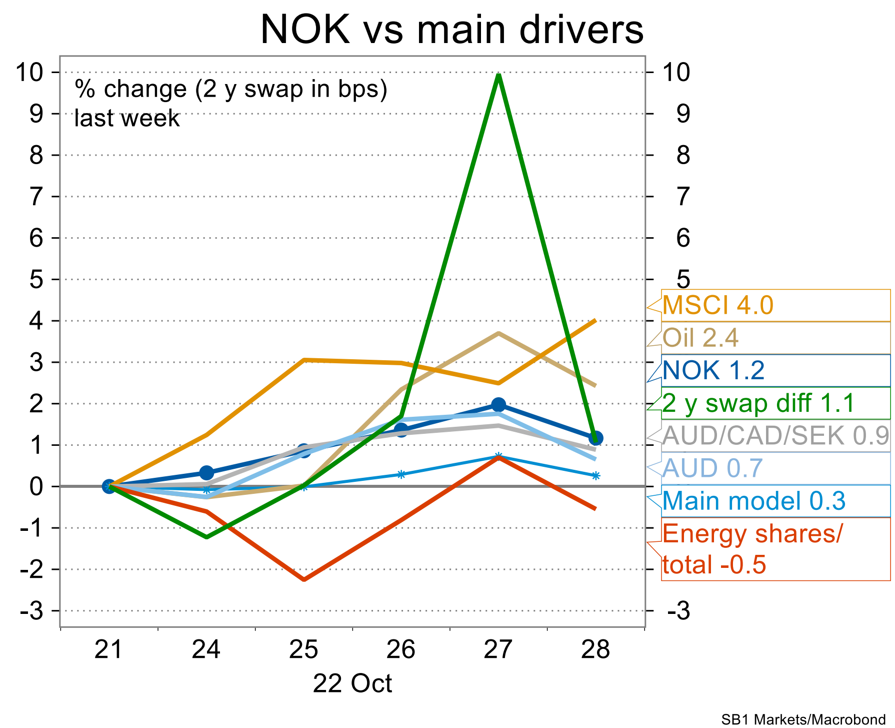


SB1 Markets/Macrobond

NOK up 1.2%, supported an higher oil price, and stronger stock markets

Not much on the downside last week



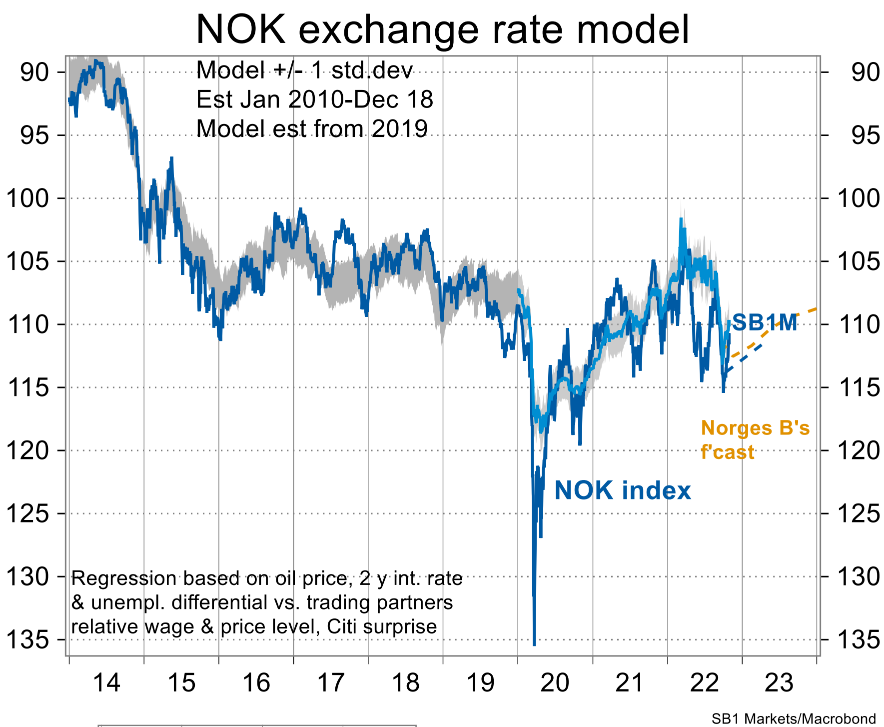


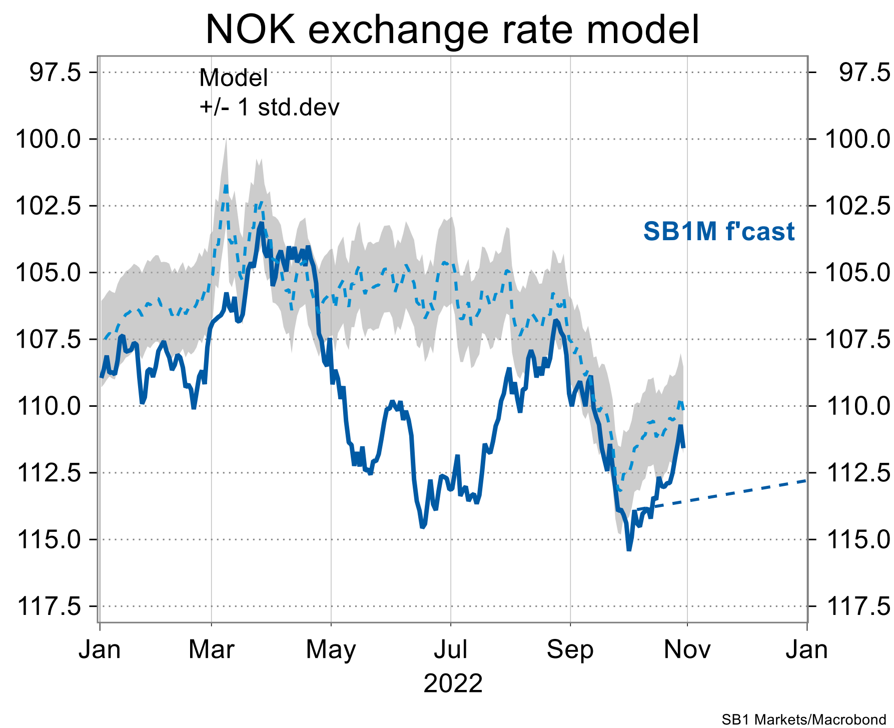
Gaps vs. our model estimates narrowed last week

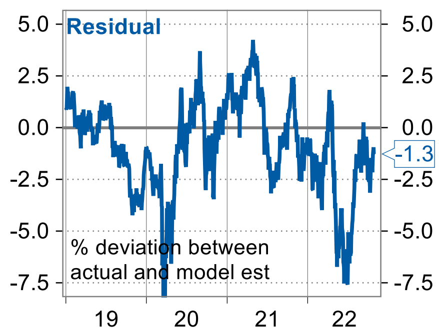
- ***NOK is 1.3% <u>below</u> our main model estimate (from -1.9%)***
- The NOK is 6% <u>weaker</u> than our AUD/CAD/SEK-model, our 'super-cycle peers', predicts, a substantial weakening (from -7%)
- NOK is 4% weaker than an estimate from a model that includes global energy companies equity prices (vs the global stock market) (from -6%)

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 1.3% below the model estimate

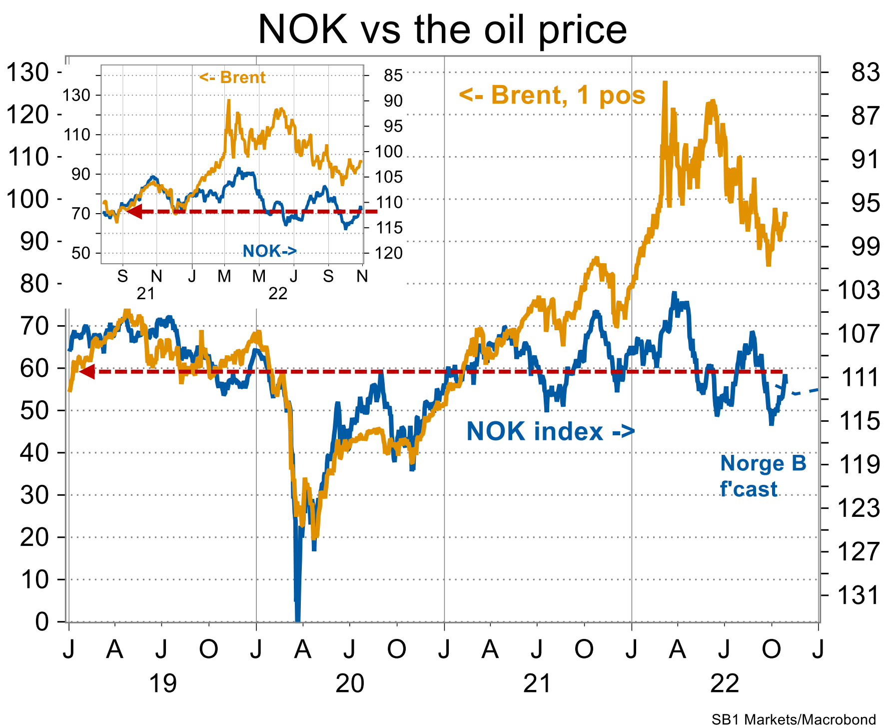


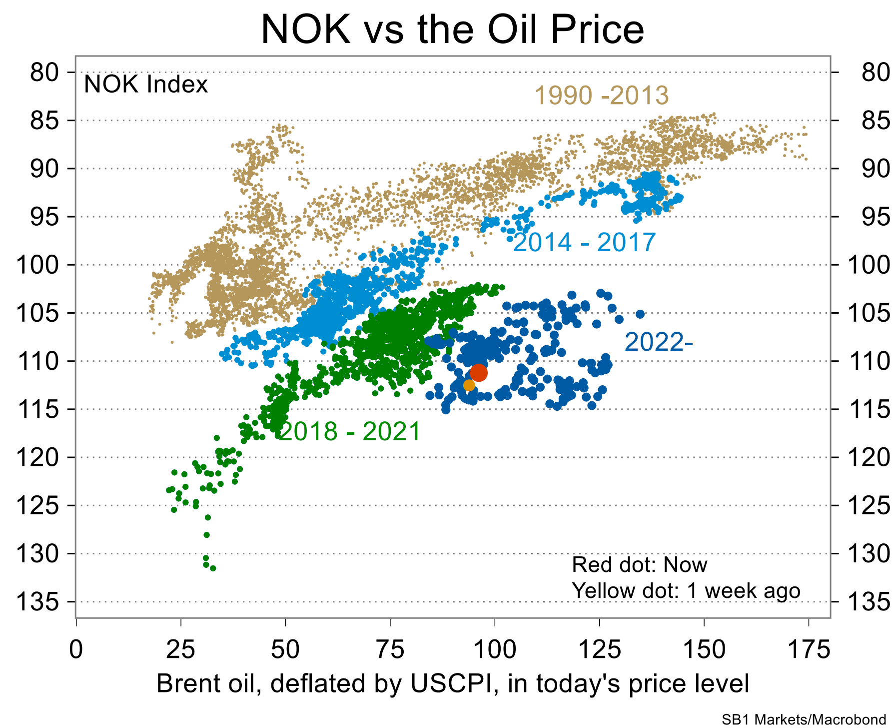




Oil up, NOK up

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

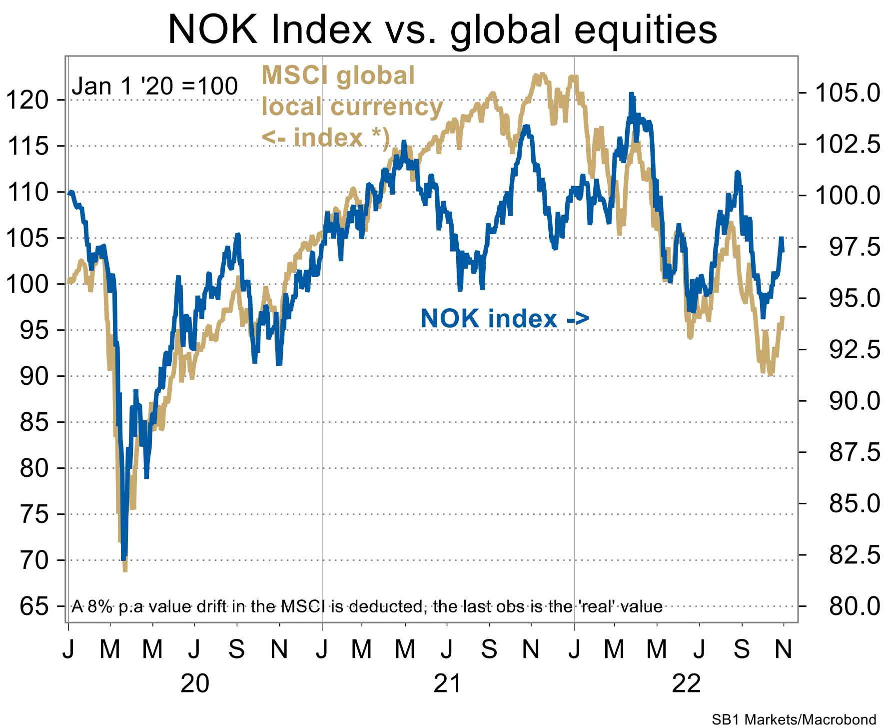


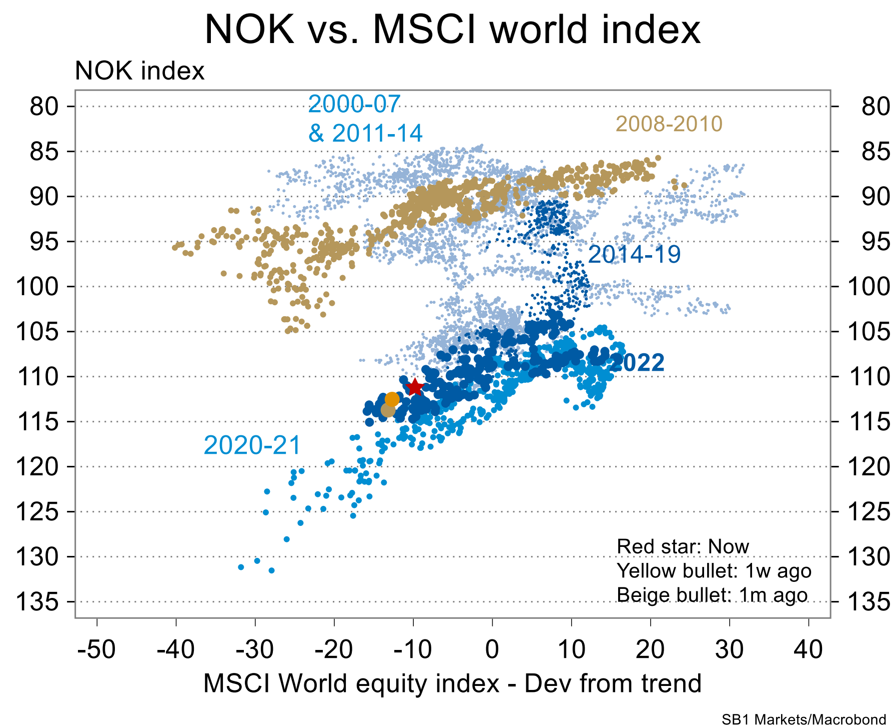


- The correlation between the NOK and the oil price has been close to non-existent since the start of 2022, rather unusual

The NOK up alongside a stronger global stock market

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

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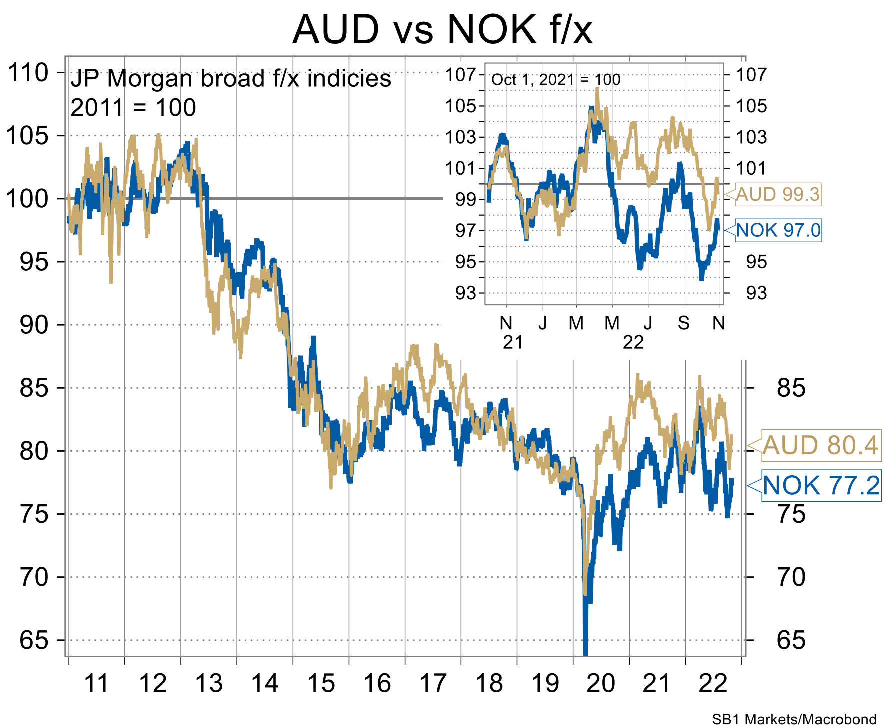
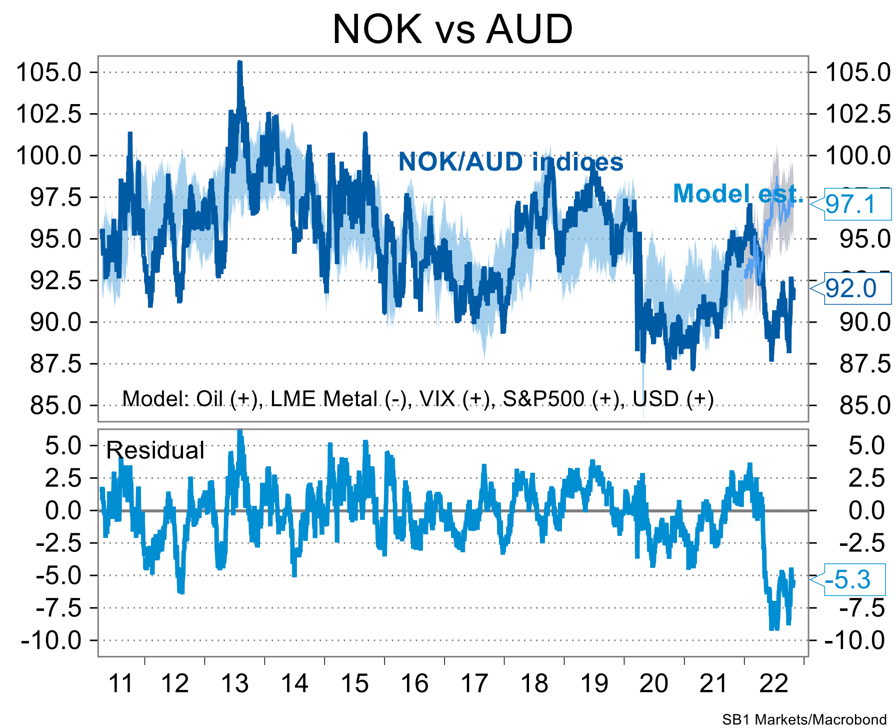
Both the AUD and NOK up last week – NOK the most but is still lagging

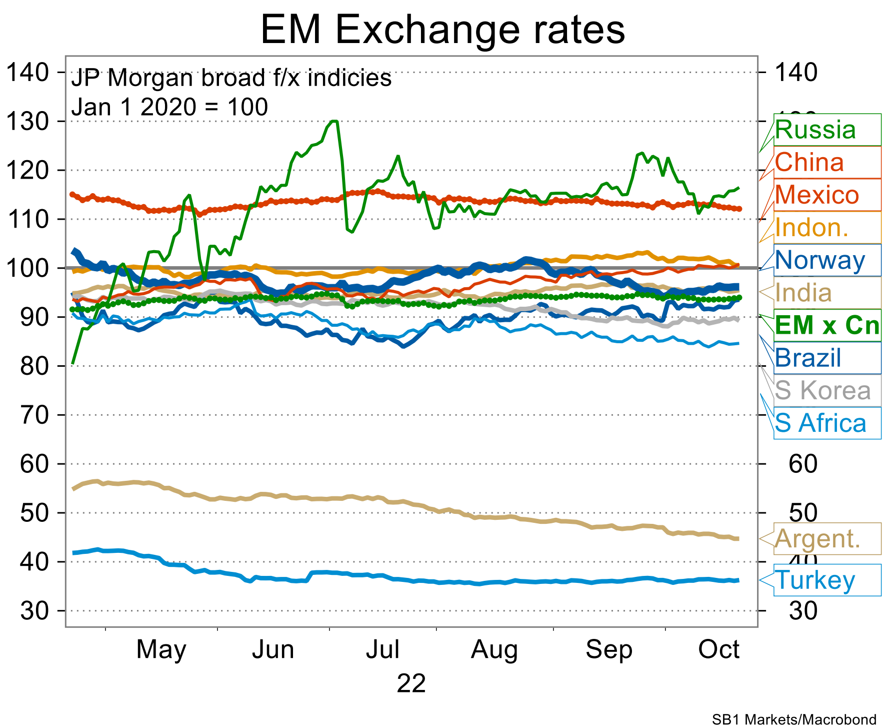
NOK is 5.3 % below our model f'cast vs AUD

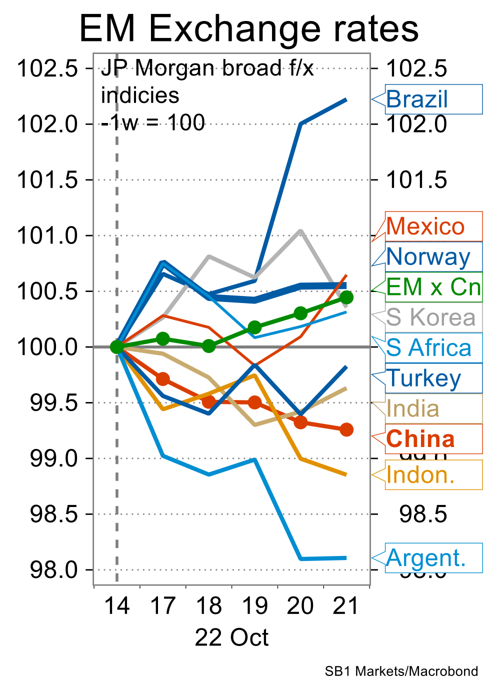


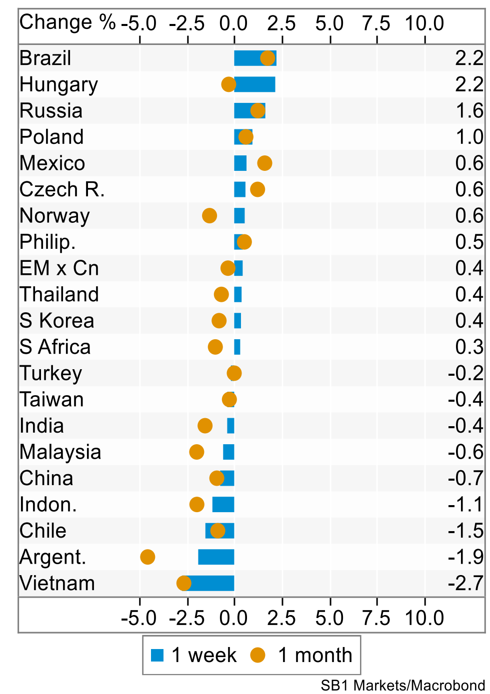


- The discrepancy between the NOK and AUD is unusual, given the normal factors that normally has explained the limited gap between the two
- Normally, NOK strengthens vs the AUD when the oil price rises vs. the LME metal index, when VIX, and the S&P500 index increases, and the USD index appreciates. 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

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