

Weekly Focus

A hot summer adds to Euro area stagflation challenge

US CPI offered the first positive surprise on inflation in a long time being flat on the month of July versus consensus expectations of 0.2% m/m. And it was not all due to lower gasoline prices as core inflation also undershot expectations rising 0.3% m/m versus consensus of 0.5% m/m. The good news is that there are clear signs that pressure on goods prices are easing: commodity prices have come down, freight costs are lower, supply chains are easing and pricing power is weaker as demand has softened and inventories are high. We also see tentative signs that inflation expectations have peaked.

However, it is too early to declare victory over US inflation as several Fed speakers also highlighted afterwards. The labour market is still very tight and employment growth has not yet cooled down suggesting that wage growth will continue to run high. It is currently close to 6%, which is much too high to bring inflation back to 2% on a sustained way. Hence, we still look for the Fed to hike 75bp on 21 September to get rates quickly back to neutral and into restrictive area. Admittedly the probability of only 50bp has increased and the decision will most likely be determined by the next round of payrolls and inflation in early September.

In the euro zone the inflation picture has been further complicated over the summer by a strong rise in gas and electricity prices. The warm weather has increased demand for air-conditioning and curtailed electricity production due to droughts that lower water levels in reservoirs and rivers and also led to a reduction in French nuclear power production. For environmental reasons French nuclear plants face restrictions on discharging water into waterways when river temperatures get too high. French electricity prices have doubled over the past three months and are now 10 times higher than in April 2021. The increase is set to push up inflation even further and add to recession risks, thus exacerbating the stagflationary environment.

On the geopolitical front China concluded military exercises around Taiwan in what has been the largest scale drills around Taiwan ever. It comes in response to the visit by US speaker of the House Nancy Pelosi, which in China's view is a breach of the 'One-China policy' and a further move towards supporting Taiwan independence. This week we sent out a paper looking into the background of the crisis and assessing the risk of war, see *Research China: The risk of a Taiwan war and what it implies – part 1*, 11 August.

Markets mainly responded to the lower-than-expected US inflation print this week by sending equities and EUR/USD higher. Bond yields initially dropped following the release but moved higher again Thursday as optimism about lower inflation and slower rate hikes faded again.

Looking into next week the main releases will be US data on retail sales, regional business surveys for August and housing data. In Europe we get the German ZEW and the final CPI print for August, which provides more details than the flash estimate. China will publish its monthly batch of industrial production, retail sales and home sales. Especially the latter will be interesting given the continued stress in the property market. Norges Bank is set to increase rates by 50bp on Thursday.

Key global views

- High risk of recession in Europe in H2. We expect the US to fall into recession in Q22023
- US inflation to peak in Q3, wage growth to stay high. Euro inflation to stay elevated in Q3 on higher electricity prices. Easing pressure from oil, metals, freight and food to pull global inflation lower in 2023.
- Fed to hike by another 125bp this year, then stop. ECB to hike a further 100bp this year, then stop.

Key market movers

- Mon: China Industrial production and retail sales, US Empire index
- Tue: German ZEW, US housing starts
- Wed: US retail sales, FOMC minutes
- Thur: Norges Bank meeting, Euro CPI (final), US Philly Fed survey, existing home sales

Selected reading from Danske Bank

Research China: The risk of a Taiwan war and what it implies – part 1, 11 Aug

US Labour Market Monitor – Labour market conditions remain strong despite mixed data, 10 Aug

FX Forecast Update – holiday edition: EUR/USD to move firmly below parity, 14 July

Editor

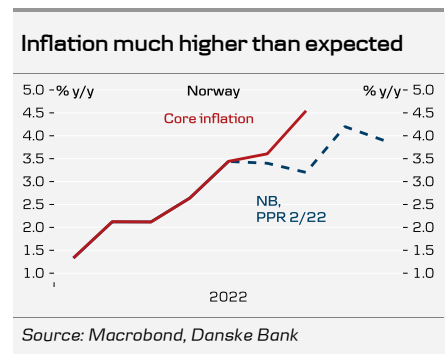
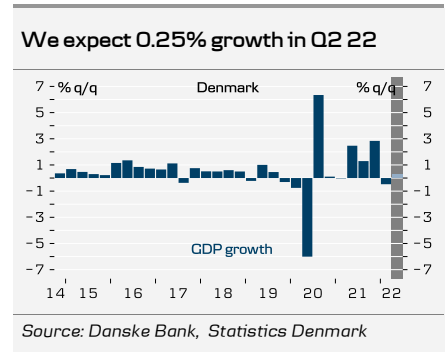
Allan von Mehren
+45 45 12 80 55
alvo@danskebank.dk

Scandi market movers

- In **Denmark**, the GDP indicator is due on Monday, showing the initial growth estimate for the Danish economy in Q2 22. We expect growth of 0.25% q/q. Danish industrial production was very strong during the quarter. On the other hand, the quarter saw declining retail sales. We see this as partly reflecting a shift among consumers towards greater consumption of services like travel and dining out instead of goods. Strong industrial production combined with a quarter free of lockdowns, unlike at the start of Q1, forms the foundation for our expectation of positive growth in Q2 22 despite the headwinds from lower goods consumption and high inflation.

Monday should also bring the Confederation of Danish Employers' (DA) wage growth figures for the private sector in Q2 22. The combination of high inflation and a large percentage of Danish companies reporting labour shortages in Q2 22 provides a basis for potentially large wage increases. However, DA published its so-called flash figure earlier in the summer, which provided an initial indication of how wages moved during the quarter. That indicated wages rising by 3.4% compared to the same quarter last year, and thus an easing of wage pressures in the wake of the 3.8% increase in Q1 22.

- No economic indicators will be published in **Sweden** next week.
- In **Norway**, the coming week brings a rate-setting meeting at Norges Bank. Announcing a 50bp hike to 1.25% in June, the bank said that the policy rate would "most likely be raised further to 1.5 percent in August". Both the double hike and the prospect of a further rate increase at an "interim" meeting show that the bank is worried about being behind the curve and rushing to get interest rates above the neutral rate so that monetary policy is contractionary and can start to rein in inflation. Since the June meeting, inflation has surprised to the upside again, jumping to 4.5% in July, well above the bank's forecast of 3.2%. Unemployment was also slightly lower than expected in July, which suggests that capacity utilisation is higher than anticipated. We therefore expect Norges Bank to deliver another 50bp hike in August. This is largely priced into the market, so interest will centre on what signals the bank puts out about the September meeting (there is no new policy rate forecast in August). The high inflation numbers for July suggest that the bank will at the very least have to leave the door open for a further 50bp rise in September. Based on our expectation of a clear downturn in both the global and the domestic economy during the autumn, we still expect Norges Bank's policy rate to peak this year, probably at 2.25%, although the accelerated hiking cycle to counter inflation means that the risk to our 2.25% forecast is to the upside.



Scandi update

Denmark – Another unexpected jump in inflation

Industrial production rose 1.1% in June, while the previous month’s figures were revised higher, taking the overall increase for Q2 22 to 6.9%. That is a very strong figure, not least considering the supply chain problems manufacturers around the world face right now. Pharmaceuticals, in particular, again delivered strong growth figures, though this industry is not so hard hit by supply issues.

Denmark’s current account surplus stood at DKK28.6bn in June – the largest surplus ever. The main driver is shipping, which is currently very lucrative. Many of Denmark’s neighbours are seeing their current accounts being eroded at the moment due to energy and commodities prices rising so dramatically. This is also the case in Denmark, but the country produces a considerable amount of energy itself, and then of course shipping is pulling strongly in the other direction.

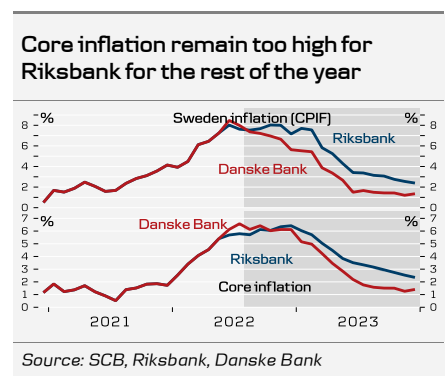
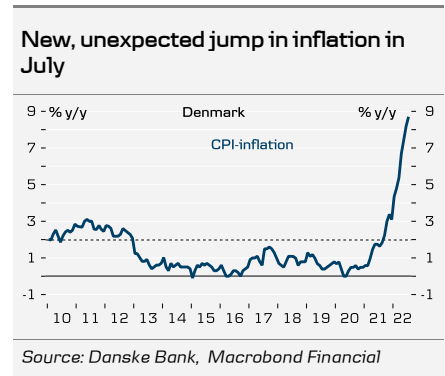
Inflation hit 8.7% in July compared to 8.2% in June despite a sizeable decline in petrol prices. Hence, inflation rose once more, and again unexpectedly, and food was once again the prime culprit. Food prices rose by 3.1% on average between June and July, which adds up to an increase of 14.6% compared to a year ago. That is a very pronounced increase for such a large category of goods. We continue to expect inflation will decline towards the end of the year, though further significant increases in European gas and electricity prices mean normal levels of inflation are still some considerable way off.

We have received a string of numbers for the Danish economy over the summer. The number of jobless rose by 1,900 in June, but this should be seen against the increase in the labour force due to newly arrived Ukrainian refugees. Employment rose by 8,000 in May, and has now risen for 16 months in a row. The labour market continues to look strong overall. Retail sales fell by 3.2%, the fifth decline during the first six months of the year, and a reflection of the substitution towards greater consumption of services. There were 211 bankruptcies among active companies in July, which does not indicate a major wave of bankruptcies, but rather that we have likely reached a more normal level. Consumer confidence fell slightly in July and so remains at a historical low, though this has not really been reflected in overall consumption yet.

Sweden – high inflation pushes Riksbank towards 75 bp hikes

July inflation turned out fairly close to our own and market expectations, printing 8.0 % yoy and 6.6 % yoy for headline CPIF and CPIF excl. Energy respectively. That is 0.4 and 0.8 p.p. above Riksbank’s corresponding forecasts. Looking at details, the main upside surprises were higher food and car prices and smaller clothing sales than usual. On the other hand, furniture, hotel/restaurant, transportations services and recreation prices showed lower price increases than expected. Looking forward, we expect core inflation to remain above 6 % y/y for the remainder of the year.

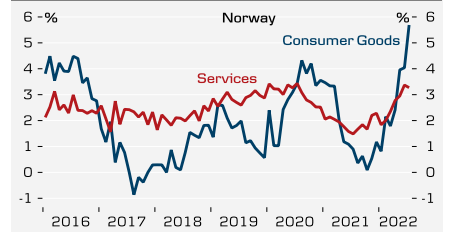
With inflation well above Riksbank’s forecast and 5y inflation expectations above the target, we believe Riksbank is pressured to accelerate tightening. Hence, we shift our call to 75 bp for both the September and November meetings. After that, with a repo rate at 2.25% by the end of the year, Riksbank would be finished tightening.



Norway – Inflation rises further

Core inflation in Norway continues to climb, thanks to a combination of higher imported prices for everything from food to furniture, and higher domestic prices driven by increased costs for labour, transport, energy and so on. In seasonally-adjusted terms, prices were rising by around 0.3-0.4% m/m in recent months, but accelerated to 0.7% in July. As expected, food prices jumped following the settlement with Norwegian farmers, but there were also big increases in prices for other goods, both imported and domestically produced. Core inflation therefore increased from 3.6% y/y in June to 4.5% y/y in July. Given the time it takes for global price drivers to feed through into Norwegian inflation, core inflation will probably remain high or even climb further in the coming months. Fortunately, though, there are signs of global price drivers such as commodities, freight and, to some extent, energy now being on the way down, so the outlook is still for lower inflation next year.

Goods driving inflation



Source: Macrobond, Danske Bank

Calendar – 15-19 August 2022

Monday, August 15, 2022				Period	Danske Bank	Consensus	Previous
1:50	JPY	GDP deflator, preliminary	y/y	2nd quarter		-0.8%	-0.5%
1:50	JPY	GDP, preliminary	q/q ann.	2nd quarter		0.7% 2.6%	-0.1% -0.5%
4:00	CNY	Industrial production	y/y	Jul		4.3%	3.9%
4:00	CNY	Retail sales	y/y	Jul		4.9%	3.1%
4:00	CNY	Fixed assets investments	y/y	Jul		6.2%	6.1%
6:30	JPY	Industrial production, final	m/m y/y	Jun			8.9% -3.1%
8:00	NOK	Trade balance	NOK bn	Jul			87.5
8:00	DKK	GDP indicator	q/q	2nd quarter	0.25%		-0.1%
8:30	DKK	Wages Growth (Private employment)	y/y	2nd quarter			3.4%
14:30	USD	Empire Manufacturing PMI	Index	Aug		5.0	11.1
16:00	USD	NAHB Housing Market Index	Index	Aug		55.0	55.0
22:00	USD	TICS international capital flow, Net inflow	USD bn	Jun			182.5
Tuesday, August 16, 2022				Period	Danske Bank	Consensus	Previous
8:00	GBP	Unemployment rate (3M)	%	Jun		3.8%	3.8%
8:00	GBP	Average weekly earnings ex bonuses (3M)	y/y	Jun			4.3%
11:00	DEM	ZEW current situation	Index	Aug		-52.0	-45.8
11:00	DEM	ZEW expectations	Index	Aug		-60.0	-53.8
11:00	EUR	Trade balance	EUR bn	Jun			-26.0
14:30	CAD	CPI	m/m y/y	Jul			-18.1%
14:30	USD	Building permits	1000 (m/m)	Jul		1650	1696.0 (0.1%)
14:30	USD	Housing starts	1000 (m/m)	Jul		1540	1559.0 (-2.0%)
15:15	USD	Capacity utilization	%	Jul		80.1%	80.0%
15:15	USD	Industrial production	m/m	Jul		0.3%	-0.2%
15:15	USD	Manufacturing production	m/m	Jul		0.3%	-0.5%
Wednesday, August 17, 2022				Period	Danske Bank	Consensus	Previous
1:00	USD	Fed's Williams speaks					
1:50	JPY	Exports	y/y (%)	Jul		0.2	0.2
1:50	JPY	Import	y/y (%)	Jul		0.5	0.5
1:50	JPY	Trade balance, s.a.	JPY bn	Jul		-1923.6	-1928.9
4:00	NZD	Reserve Bank of New Zealand (cash rate decision)	%			3.0%	2.5%
8:00	GBP	CPI	m/m y/y	Jul		0.4% 9.8%	0.8% 9.4%
8:00	GBP	CPI core	y/y	Jul		5.9%	5.8%
8:00	NOK	GDP (mainland)	m/m	Jun			-0.2%
8:30	NOK	Consumer confidence	Net. bal.	3rd quarter			-11.7
11:00	EUR	Employment, preliminary	q/q y/y	2nd quarter			0.6% 2.9%
11:00	EUR	GDP, preliminary	q/q y/y	2nd quarter	0.7% 4.0%	0.7% 4.0%	0.7% 4.0%
14:30	USD	Retail sales control group	m/m	Jul		0.3%	0.8%
16:30	USD	DOE U.S. crude oil inventories	K				5457
20:00	USD	FOMC minutes					
Thursday, August 18, 2022				Period	Danske Bank	Consensus	Previous
3:30	AUD	Employment change	1000	Jul		26.5	88.4
6:30	SEK	Capacity utilization, industry	%	2nd quarter			90.4%
8:00	NOK	GDP (mainland)	q/q	2nd quarter	0.7%	0.7%	-0.6%
8:00	NOK	GDP (total)	q/q	2nd quarter			-1.0%
10:00	NOK	Norges Banks monetary policy meeting	%		1.75%		1.3%
11:00	EUR	HICP inflation, final	m/m y/y	Jul	0.1% 8.6%	-18.9%	0.1% 8.6%
11:00	EUR	HICP - core inflation, final	y/y	Jul	4.0%	4.0%	4.0%
13:00	TRY	Central Bank of Turkey rate decision	%		14.0%	14.0%	14.0%
14:30	USD	Initial jobless claims	1000		265		262
14:30	USD	Philly Fed index	Index	Aug		-5.0	-12.3
16:00	USD	Existing home sales	m (m/m)	Jul		4.85	5.12 -0.054
19:20	USD	Fed's George speaks					
19:45	USD	Fed's Kashkari speaks					
Friday, August 19, 2022				Period	Danske Bank	Consensus	Previous
1:01	GBP	GfK consumer confidence	Index	Aug		-42.0	-41.0
1:30	JPY	CPI - national	y/y	Jul		2.6%	2.4%
1:30	JPY	CPI - national ex. fresh food	y/y	Jul		2.4%	2.2%
8:00	GBP	Retail sales ex fuels	m/m y/y	Jul		0.0% -	0.4% -5.9%
8:30	EUR	Current account	EUR bn	Jun			-4.5
14:30	CAD	Retail sales	m/m	Jun			2.2%

Source: Danske Bank

Macroeconomic forecast

Macro forecast. Scandinavia

	Year	GDP ¹	Private cons. ¹	Public cons. ¹	Fixed inv. ¹	Ex-ports ¹	Im-ports ¹	Infla-tion ¹	Wage growth ¹	Unem-ploym ³	Public budget ⁴	Public debt ⁴	Current acc. ⁴
Denmark	2021	4.9	4.3	4.2	6.2	8.0	8.0	1.9	3.0	3.7	2.6	36.7	8.3
	2022	3.5	2.1	-0.3	3.3	4.1	1.9	6.4	3.7	2.5	1.0	31.9	8.8
	2023	0.7	1.3	0.9	-0.4	2.2	2.5	2.6	4.0	2.7	0.7	29.9	8.1
Sweden	2021	4.8	6.1	2.6	5.9	7.6	9.3	2.2	2.7	8.8	-0.2	37.3	5.2
	2022	1.1	2.6	0.1	-0.3	5.4	6.3	6.4	2.0	7.4	-0.3	33.0	4.9
	2023	1.6	1.7	1.2	1.3	3.9	3.4	3.5	2.1	7.2	0.3	31.0	5.2
Norway	2021	4.1	4.9	3.8	-0.9	4.7	2.3	3.5	3.5	3.2	-	-	-
	2022	3.6	6.7	1.3	3.1	6.0	7.5	4.6	3.7	1.8	-	-	-
	2023	1.6	2.5	1.3	2.0	4.0	4.0	2.0	3.7	2.1	-	-	-

Macro forecast. Euroland

	Year	GDP ¹	Private cons. ¹	Public cons. ¹	Fixed inv. ¹	Ex-ports ¹	Im-ports ¹	Infla-tion ¹	Wage growth ¹	Unem-ploym ³	Public budget ⁴	Public debt ⁴	Current acc. ⁴
Euro area	2021	5.3	3.6	3.9	3.9	10.4	8.1	2.6	4.1	7.7	-5.1	97.4	3.2
	2022	2.9	2.5	1.4	3.1	5.6	7.0	7.6	3.2	6.8	-3.7	94.7	2.4
	2023	0.5	0.6	2.4	2.2	2.6	4.8	4.1	3.4	6.8	-2.5	92.7	2.9
Germany	2021	2.6	0.3	2.9	1.0	9.5	9.0	3.2	3.4	3.6	-3.7	69.3	7.4
	2022	1.0	2.4	0.7	2.6	1.8	6.8	7.9	3.3	3.0	-2.5	66.4	6.4
	2023	0.0	0.2	2.8	2.5	2.1	4.8	4.8	3.9	3.0	-1.0	64.5	6.8
Finland	2021	3.0	3.6	2.7	1.1	5.6	5.6	2.2	2.3	7.7	-2.6	72.3	0.9
	2022	1.5	1.6	1.5	4.0	1.0	2.5	6.0	2.8	6.4	-2.8	65.0	-0.6
	2023	1.6	2.5	1.0	2.5	2.0	3.5	2.5	2.6	6.3	-2.3	64.8	-0.2

Macro forecast. Global

	Year	GDP ¹	Private cons. ¹	Public cons. ¹	Fixed inv. ¹	Ex-ports ¹	Im-ports ¹	Infla-tion ¹	Wage growth ¹	Unem-ploym ³	Public budget ⁴	Public debt ⁴	Current acc. ⁴
USA	2021	5.7	7.9	0.5	7.8	4.5	14.0	4.7	4.2	5.4	-12.4	126.9	-3.5
	2022	2.4	2.9	-0.8	3.9	2.9	9.6	8.5	5.2	3.6	-4.2	124.0	-3.5
	2023	0.1	0.1	1.1	-1.2	-2.3	-1.7	4.7	4.2	3.9	-3.8	121.0	-3.2
China	2021	8.0	10.2	-	5.2	-	-	0.7	5.0	-	-5.6	68.9	3.0
	2022	3.7	4.8	-	3.0	-	-	2.5	5.0	-	-7.7	77.8	1.1
	2023	5.7	6.5	-	5.0	-	-	2.5	5.5	-	-7.1	81.8	1.0
UK	2021	7.4	6.2	14.3	5.9	-1.3	3.8	2.6	5.1	4.5	-5.4	95.6	-2.6
	2022	4.0	4.8	1.3	8.1	0.7	14.7	8.4	4.4	3.6	-3.9	95.5	-4.8
	2023	-0.2	-0.3	1.2	-1.9	-2.4	-2.4	5.6	3.3	4.1	-1.9	97.0	-3.7
Japan	2021	1.7	1.1	2.1	-1.3	11.9	5.1	-0.2	-	2.8	-	-	-
	2022	1.7	3.3	1.4	-1.8	3.6	4.1	1.6	-	2.5	-	-	-
	2023	1.8	1.6	0.7	1.7	2.9	1.1	1.1	-	2.5	-	-	-

Source: OECD and Danske Bank. 1) % y/y. 2) % contribution to GDP growth. 3) % of labour force. 4) % of GDP.

Financial forecast

Bond and money markets										
		Key interest rate	3m interest rate	2-yr swap yield	10-yr swap yield	Currency vs EUR	Currency vs USD	Currency vs DKK	Currency vs NOK	Currency vs SEK
USD	12-Aug	2.50	2.92	3.51	2.92	102.9	-	723.1	953.6	1015.2
	+3m	3.50	3.94	3.75	3.30	98.0	-	759.4	1081.6	1071.4
	+6m	3.75	4.00	3.75	3.30	96.0	-	775.5	1083.3	1125.0
	+12m	3.75	3.99	3.40	2.80	95.0	-	784.2	1052.6	1157.9
EUR	12-Aug	0.00	0.33	1.38	1.83	-	102.9	743.9	981.1	1044.5
	+3m	0.75	0.98	1.70	2.15	-	98.0	744.3	1060.0	1050.0
	+6m	1.00	1.12	1.80	2.20	-	96.0	744.5	1040.0	1080.0
	+12m	1.00	1.12	1.70	2.00	-	95.0	745.0	1000.0	1100.0
JPY	12-Aug	-0.10	-0.01	0.10	0.36	120.5	133.6	6.17	8.14	8.67
	+3m	-0.10	-	-	-	128.4	131.0	5.80	8.26	8.18
	+6m	-0.10	-	-	-	122.9	128.0	6.06	8.46	8.79
	+12m	-0.10	-	-	-	118.8	125.0	6.27	8.42	9.26
GBP*	12-Aug	1.75	-	2.89	2.28	84.8	121.3	877.0	1156.6	1231.3
	+3m	2.50	-	2.55	2.30	86.0	114.0	865.4	1232.6	1220.9
	+6m	2.50	-	2.55	2.35	85.0	112.9	875.9	1223.5	1270.6
	+12m	2.50	-	2.35	2.05	84.0	113.1	886.9	1190.5	1309.5
CHF*	12-Aug	-0.75	-	0.67	1.32	97.0	94.3	766.8	1011.3	1076.6
	+3m	0.25	-	-	-	97.0	99.0	767.3	1092.8	1082.5
	+6m	0.75	-	-	-	96.0	100.0	775.5	1083.3	1125.0
	+12m	0.75	-	-	-	95.0	100.0	784.2	1052.6	1157.9
DKK	12-Aug	-0.10	0.62	1.67	2.10	743.93	723.08	-	131.88	140.40
	+3m	0.65	1.17	2.00	2.45	744.25	759.44	-	142.43	141.08
	+6m	0.90	1.30	2.10	2.50	744.50	775.52	-	139.69	145.06
	+12m	0.90	1.30	2.00	2.30	745.00	784.21	-	134.23	147.65
SEK	12-Aug	0.75	1.52	2.50	2.31	1044.5	1015.2	71.2	93.9	100.0
	+3m	1.25	1.95	2.70	2.40	1050.0	1071.4	70.9	101.0	-
	+6m	2.00	2.25	2.65	2.50	1080.0	1125.0	68.9	96.3	-
	+12m	2.00	2.25	2.50	2.40	1100.0	1157.9	67.7	90.9	-
NOK	12-Aug	1.25	2.31	3.39	3.09	981.1	953.6	75.8	100.0	106.5
	+3m	1.75	2.53	3.05	3.35	1060.0	1081.6	70.2	-	99.1
	+6m	2.25	2.60	2.95	3.40	1040.0	1083.3	71.6	-	103.8
	+12m	2.25	2.60	2.85	3.20	1000.0	1052.6	74.5	-	110.0

*Notes: GBP swaps are SONIA and CHF swaps are SHARON.

We have updated our Norges Bank forecasts after yesterday's Norges Bank meeting but not yet our Norwegian yield outlook

Commodities

	12-Aug	2022				2023				Average	
		Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	2022	2023
ICE Brent	98	98	112	115	100	95	95	95	95	106	95

Source Danske Bank

Disclosures

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