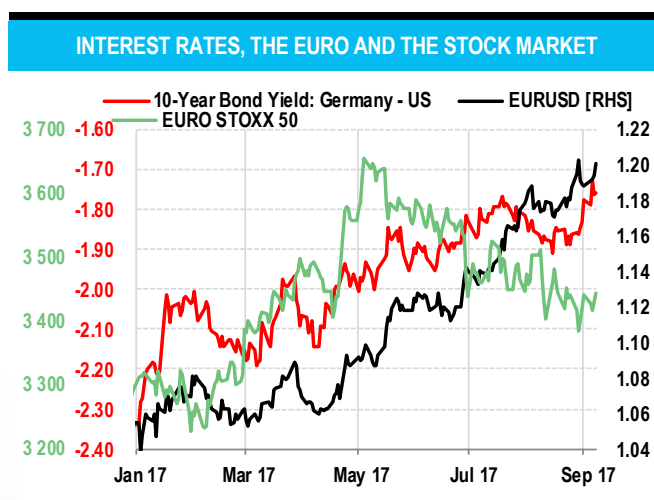


Financial markets as self-appointed subcontractors

■ Financial markets are very much influenced by expectations about monetary policy ■ The recent euro strength reflects anticipations of a scaling back of the ECB's asset purchase programme ■ Market anticipations complicate the ECB's task

Financial markets are the self-appointed subcontractors of central banks. Their monetary policy anticipations influence growth and inflation via exchange rates, wealth effects, confidence channels, the cost of funding, etc. When in easing mode, central banks very much welcome this: it reinforces a given monetary impulse like an interest rate cut or the launch of an asset purchase program. Things get complicated when they're in a tightening mode and market action can pre-empt policy change. International capital flows play a key role in this respect. Think of the taper tantrum in the US in 2013, how it impacted emerging markets, the concerns it raised about US exports and growth.

Today, the ECB is facing a similar challenge. Investors anticipate a scaling back or possibly even an end of the asset purchase programme. Ten-year bond yields have risen and the differential with the US has narrowed, also because investors relatively speaking have become more upbeat about the eurozone compared to the US. The ensuing euro strength has weighed on the equity market and has contributed to modestly tighter financial and monetary conditions. This does not warrant a less confident outlook for growth yet but it does create a challenge for the ECB in terms of communication. Mario Draghi yesterday didn't want to comment about levels of the euro, as the exchange rate is not an explicit objective for the bank. However, it leaves markets guessing at what point the ECB considers the strong euro becomes a genuine headwind for growth. The new ECB staff projections on the other hand show that an exogenous shock which would move the EURUSD to 1.31 in 2019 would, compared to the base scenario of an unchanged exchange rate, have a negative growth impact of 0.3% next year and the year after and lower inflation with respectively 0.4 and 0.5%. Market anticipation also creates a challenge for the ECB in terms of action all the more so because simply maintaining QE for longer would confront it with a shortage of bonds to buy in certain markets.



William De Vijlder

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Economic scenario

Eco
WEEK

ECONOMIC RESEARCH DEPARTMENT



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Markets overview

The essentials

Week 1-9 17 > 7-9-17

➤ CAC 40	5 123	➤ 5 115	-0.2 %
➤ S&P 500	2 477	➤ 2 465	-0.5 %
➤ Volatility (VIX)	10.1	➤ 11.6	+1.4 %
➤ Euribor 3M (%)	-0.33	➤ -0.33	-0.1 bp
➤ Libor \$ 3M (%)	1.32	➤ 1.32	+0.1 bp
➤ OAT 10y (%)	0.69	➤ 0.62	-6.8 bp
➤ Bund 10y (%)	0.38	➤ 0.30	-7.8 bp
➤ US Tr. 10y (%)	2.16	➤ 2.06	-9.6 bp
➤ Euro vs dollar	1.19	➤ 1.20	+1.1 %
➤ Gold (ounce, \$)	1 322	➤ 1 347	+1.9 %
➤ Oil (Brent, \$)	52.8	➤ 54.1	+2.4 %

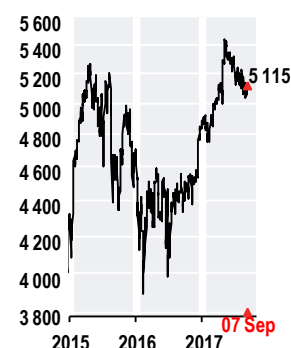
10 y bond yield, OAT vs Bund



Euro-dollar



CAC 40



Money & Bond Markets

Interest Rates	highest' 17	lowest' 17
€ ECB	0.00 at 02/01	0.00 at 02/01
Eonia	-0.36 at 02/06	-0.37 at 05/06
Euribor 3M	-0.33 at 02/01	-0.33 at 10/04
Euribor 12M	-0.16 at 02/01	-0.16 at 23/06
\$ FED	1.25 at 15/06	0.75 at 02/01
Libor 3M	1.32 at 25/08	1.00 at 02/01
Libor 12M	1.71 at 15/03	1.68 at 06/01
£ BoE	0.25 at 02/01	0.25 at 02/01
Libor 3M	0.28 at 05/01	0.28 at 01/09
Libor 12M	0.59 at 09/01	0.59 at 06/09

At 7-9-17

Yield (%)	highest' 17	lowest' 17
€ AVG 5-7y	0.35 at 17/03	0.18 at 21/06
Bund 2y	-0.80 at 27/06	-0.96 at 24/02
Bund 10y	0.30 at 06/07	0.09 at 02/01
OAT 10y	0.62 at 06/02	0.59 at 14/06
Corp. BBB	1.24 at 01/02	1.24 at 07/09
\$ Treas. 2y	1.28 at 03/07	1.14 at 24/02
Treas. 10y	2.06 at 13/03	2.06 at 07/09
Corp. BBB	3.38 at 14/03	3.38 at 05/09
£ Treas. 2y	0.08 at 29/06	0.01 at 28/02
Treas. 10y	1.03 at 26/01	0.87 at 14/06

At 7-9-17

10y bond yield & spreads

5.35%	Greece	505 pb
2.73%	Portugal	242 pb
1.92%	Italy	162 pb
1.48%	Spain	118 pb
0.62%	Belgium	32 pb
0.62%	France	32 pb
0.62%	Ireland	32 pb
0.51%	Austria	21 pb
0.44%	Netherlands	14 pb
0.30%	Germany	0 pb
0.30%	Finland	

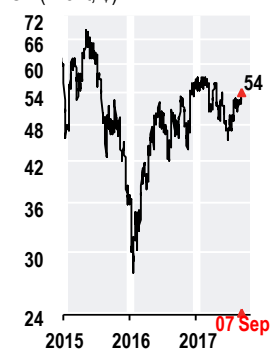
Commodities

Spot price in dollars	lowest' 17	2017(€)
Oil, Brent	54 at 26/06	-16.2%
Gold (ounce)	1 347 at 03/01	+2.3%
Metals, LMEX	3 239 at 03/01	+7.0%
Copper (ton)	6 874 at 08/05	+9.3%
CRB Foods	338 at 24/04	-12.2%
wheat (ton)	154 at 24/04	-7.3%
Corn (ton)	124 at 30/08	-17.6%

At 7-9-17

Variations

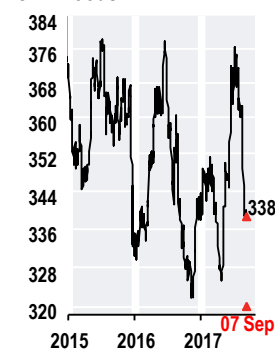
Oil (Brent, \$)



Gold (Ounce, \$)



CRB Foods



Exchange Rates

1€ =	highest' 17	lowest' 17	2017
USD	1.20 at 29/08	1.04 at 03/01	+13.8%
GBP	0.92 at 29/08	0.84 at 19/04	+7.3%
CHF	1.14 at 03/08	1.06 at 08/02	+6.7%
JPY	130.22 at 30/08	115.57 at 17/04	+5.8%
AUD	1.49 at 01/06	1.37 at 23/02	+2.6%
CNY	7.81 at 03/08	7.22 at 03/01	+6.5%
BRL	3.72 at 29/08	3.24 at 15/02	+8.4%
RUB	68.39 at 02/08	59.66 at 17/04	+6.2%
INR	76.90 at 29/08	68.18 at 07/04	+7.4%

At 7-9-17

Variations

Equity indices

Index	highest' 17	lowest' 17	2017	2017(€)
CAC 40	5 115 at 05/05	4 749 at 31/01	+5.2%	+5.2%
S&P500	2 481 at 07/08	2 239 at 02/01	+10.1%	-3.3%
DAX	12 889 at 19/06	11 510 at 06/02	+7.1%	+7.1%
Nikkei	20 230 at 20/06	18 336 at 14/04	+1.5%	-4.1%
China*	81 at 30/08	59 at 02/01	+39.4%	+21.7%
India*	571 at 04/08	445 at 03/01	+20.6%	+12.3%
Brazil*	2 099 at 07/09	1 639 at 21/06	+19.5%	+10.3%
Russia*	622 at 03/01	497 at 22/06	-10.4%	-16.8%

At 7-9-17

Variations

* MSCI index



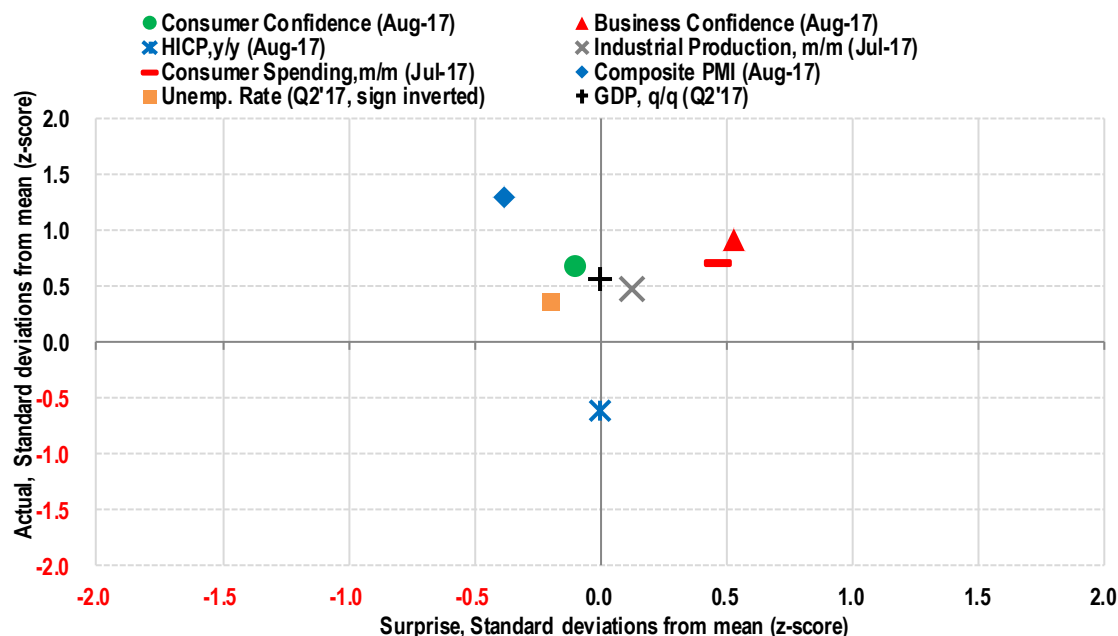
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Pulse

France: economic data remain well oriented

The French economic indicators released in the past few weeks continue to deliver a positive message. They have been broadly as expected (when there was a surprise, be it positive or negative, it was not a big one as illustrated by the Z-score centered around zero on the x-axis) while maintaining a positive momentum (Z-score positive on the y-axis). Inflation remains the sole indicator to run below its long-term average.



Note: z-score is a score which indicates how many standard deviations an observation is from the mean: $z=(x-\mu)/\sigma$ where x : observation, μ : mean, σ : standard deviation. On the X-axis, x corresponds at the last known surprise for each indicator represented on the graph, μ and σ corresponds respectively to the mean and the standard deviation of the last 24 value for monthly data and the last 8 quarters for quarterly data. On the Y-axis, x corresponds at the last known value of indicator, μ and σ corresponds respectively to the mean and the standard deviation for this indicator since 2000.

Sources: INSEE, Markit, BNP Paribas calculations

Indicators preview

Inflation and industrial production data are dominating next week's agenda.

Date	Country	Event	Period	Survey	Prior
12/09/2017	United Kingdom	CPI MoM	Aug	0.5%	-0.1%
	United States	NFIB Small Business Optimism	Aug	105.0	105.2
13/09/2017	Germany	CPI MoM	Aug F	0.1%	0.1%
	Eurozone	Industrial Production SA MoM	Jul	0.2%	-0.6%
	United States	PPI Ex Food and Energy MoM	Aug	0.2%	-0.1%
14/09/2017	Japan	Industrial Production MoM	Jul F	--	-0.8%
	France	CPI MoM	Aug F	0.5%	0.5%
	United States	CPI Ex Food and Energy MoM	Aug	0.2%	0.1%
15/09/2017	United States	Retail Sales Advance MoM	Aug	0.1%	0.6%
	United States	Industrial Production MoM	Aug	0.1%	0.2%
	United States	Capacity Utilization	Aug	76.8%	76.7%



Economic scenario

UNITED STATES

- GDP growth keeps on a decent 2% pace and picked-up a bit in Q2. However the fiscal outlook remains uncertain. A fiscal stimulus still is possible, but it would not be implemented before end-2017. Potential effects are thus uncertain.
- The labour market is as buoyant as ever. Still, the support to households' disposable income is not as strong as it looks as wage inflation remains limited.
- With inflation relatively muted at this stage of the cycle, the Fed is in no rush to increase rates. We forecast the Fed Funds target rates to come at 1.25/1.50% by year-end, 2/2.5% by mid-2018.

CHINA

- After a period of stabilisation and slight recovery since Q2 2016, economic growth is expected to slow down moderately in the coming quarters.
- Exports should continue to rebound and infrastructure projects will continue to drive investment. However, downside risks are high due to the reduction in excess production capacity in the industry and given risks of a downturn in the property market and financial instability.
- The authorities will maintain an expansionist fiscal policy while the central bank should continue to tighten monetary conditions cautiously, especially to foster a deleveraging of financial institutions.

EUROZONE

- The recovery is getting stronger and broader: the dispersion of economic performances among member states is receding.
- Despite the cyclical recovery, core inflation still shows no sign of a convincing upward trend. For the recovery to enter its inflationary phase the economy has to improve further, until the point at which wages will tend to increase.

The level of slack remains uncertain though. Broader measures of labor underutilization reach 18%, double the level of the current unemployment rate. The ECB is expected to remain cautious.

FRANCE

- A clear growth acceleration is underway. Higher rates of growth should resume. Households' consumption is supported by the jobs recovery but restrained by the upturn in inflation. Investment and exports dynamics are favourable. Risks lie slightly on the upside.
 - We expect the output gap to slowly narrow and the unemployment rate to progressively decline, containing the rise in inflation.
- Fiscal policy should continue to combine growth supportive measures and consolidation ones. The fiscal deficit should not be a lot more reduced but it should remain below the 3% threshold.

SUMMARY

%	GDP Growth			Inflation		
	2016	2017 e	2018 e	2016	2017 e	2018 e
Advanced	1,6	2,1	1,9	0,8	1,6	1,7
United-States	1,6	2,3	2,6	1,3	1,9	2,3
Japan	1,0	1,7	1,0	-0,1	0,4	0,6
United-Kingdom	1,8	1,5	1,0	0,6	2,8	2,8
Euro Area	1,7	2,1	1,6	0,2	1,5	1,1
Germany	1,8	1,8	2,0	0,4	1,9	1,7
France	1,1	1,6	1,6	0,3	1,4	1,0
Italy	1,0	1,3	0,9	-0,1	1,3	0,8
Emerging	4,1	4,6	4,9	4,4	3,1	3,4
China	6,7	6,6	6,4	2,0	1,8	2,3
India	7,5	7,3	7,8	4,9	4,9	5,2
Brazil	-3,5	1,0	3,0	8,8	3,6	3,8
Russia	-0,6	1,2	2,0	7,1	4,2	4,3

FX RATES

Exchange Rates		2018					
End of period	Q4e	Q1e	Q2e	Q3e	Q4e	2017e	2018e
USD EUR / USD	1,13	1,15	1,17	1,19	1,20	1,13	1,20
USD / JPY	118	120	118	116	114	118	114
GBP / USD	1,26	1,29	1,31	1,37	1,41	1,26	1,41
USD / CHF	0,99	0,97	0,96	0,94	0,96	0,99	0,96
EUR EUR / GBP	0,90	0,89	0,89	0,87	0,85	0,90	0,85
EUR / CHF	1,12	1,12	1,12	1,12	1,15	1,12	1,15
EUR / JPY	133	138	138	138	137	133	137

INTEREST RATES

Forecasts currently under revision.



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