

# ECOWEEK

No. 18-01, 5 January 2018

## Eurozone growth: flat out

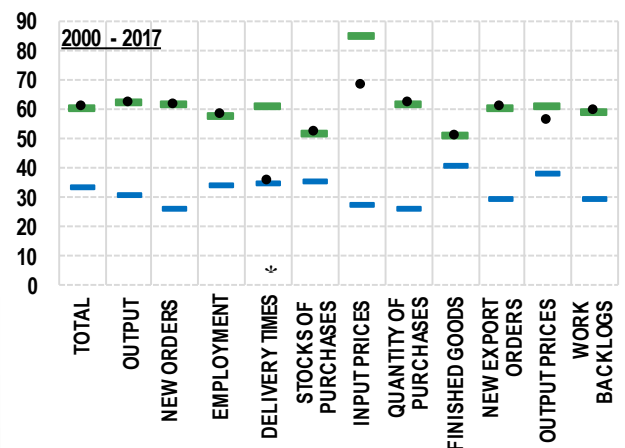
■ The Markit PMI for the manufacturing sector as well as the composite indicator saw another increase in December, with the former reaching a record high ■ Most of the sub-series are at or near historical highs and reflect the breadth of the recovery ■ This and the expected evolution of the drivers of final demand point to ongoing robust growth

The eurozone economy continues to power ahead. The Markit PMI for the manufacturing sector released at the start of the week showed the index for December reaching the highest level on record (the survey began in mid-1997). The Services Business Activity index also registered an increase and the Composite Output index, at 58.1, reached the highest level since February 2011. To illustrate the breadth of the movement in the manufacturing sector, the chart shows for 11 sub-series, as well as for the total, the highest and lowest reading since 2000 plus the most recent observation. Virtually all components are at or very close to their historical highs. For delivery times the number is low and this reflects long delivery times, another manifestation of strength. The reading for input prices is relatively speaking on the low side. Output prices on the other hand are close to the historical high which together with lengthening delivery times and work backlogs would point towards a pick-up in eurozone inflation.

The PMI numbers warrant confidence for the growth outlook in 2018. Using the historical relationship between the composite PMI and quarterly real GDP growth, one obtains a 'nowcast' for real GDP growth in the final quarter of last year of 0.8%, which is an acceleration from an already strong performance of 0.6% in the third quarter. Admittedly the statistical relationship is not perfect (regression  $R^2$  of 0.70) but the coefficient is highly significant and recent forecast errors have been small. Moreover, the PMI series display a high level of inertia: a high level in a given month tends to be followed by a high level in the following months, which supports the expectation of ongoing strong GDP growth. This purely statistical approach can be complemented by looking at the drivers of final demand. Consumer spending should be supported by job creation, a pick-up in wage growth, low interest rates, easy access to credit. To some degree, the wealth effect can also play a role. Corporate investments should continue to grow at a healthy pace on the back of profits growth, rising capacity utilisation and attractive financing conditions. The European Commission expects fiscal policy to be broadly neutral. Exports should benefit from the broad-based upswing in the world economy. To conclude, the eurozone economy has ended the year 2017 on a particularly strong footing. Different indicators warrant confidence for the next several months. However, this is likely to intensify the debate on the appropriateness of the current monetary stance of the ECB, in particular if core inflation would move in the direction shown today by supply side bottleneck indicators.

### EUROZONE MANUFACTURING PURCHASING MANAGERS INDEX

— Highest — Lowest • Last Value (31/12/2017)



\* inverted scale

Sources: Markit, BNP Paribas

William De Vijlder

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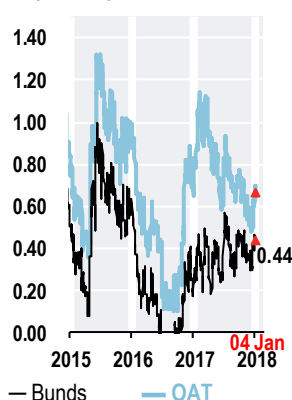
## Markets overview

## The essentials

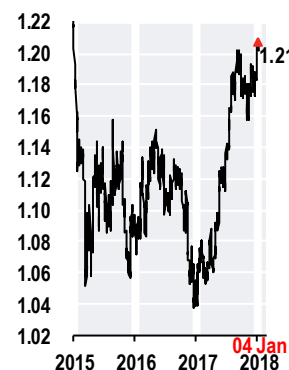
Week 29-12 17 &gt; 4-1-18

➤ CAC 40	5 313	➤ 5 414	+1.9 %
➤ S&P 500	2 674	➤ 2 724	+1.9 %
➤ Volatility (VIX)	11.0	➤ 9.2	-1.8 pb
➤ Euribor 3M (%)	-0.33	➤ -0.33	+0.0 bp
➤ Libor \$ 3M (%)	1.69	➤ 1.70	+0.2 bp
➤ OAT 10y (%)	0.66	➤ 0.66	+0.3 bp
➤ Bund 10y (%)	0.42	➤ 0.44	+1.2 bp
➤ US Tr. 10y (%)	2.41	➤ 2.45	+4.2 bp
➤ Euro vs dollar	1.20	➤ 1.21	+0.6 %
➤ Gold (ounce, \$)	1 303	➤ 1 318	+1.1 %
➤ Oil (Brent, \$)	66.6	➤ 68.1	+2.2 %

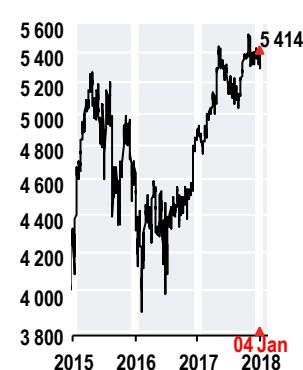
10 y bond yield, OAT vs Bund



Euro-dollar



CAC 40



## Money &amp; Bond Markets

Interest Rates		highest' 18	lowest' 18
€ ECB	0.00	0.00 at 01/01	0.00 at 01/01
Eonia	-0.36	-0.35 at 01/01	-0.37 at 02/01
Euribor 3M	-0.33	-0.33 at 01/01	-0.33 at 01/01
Euribor 12M	-0.19	-0.19 at 01/01	-0.19 at 03/01
\$ FED	1.50	1.50 at 01/01	1.50 at 01/01
Libor 3M	1.70	1.70 at 02/01	1.69 at 01/01
Libor 12M	2.12	2.12 at 03/01	2.11 at 01/01
£ BoE	0.50	0.50 at 01/01	0.50 at 01/01
Libor 3M	0.52	0.52 at 01/01	0.52 at 03/01
Libor 12M	0.76	0.77 at 02/01	0.76 at 03/01

At 4-1-18

Yield (%)		highest' 18	lowest' 18
€ AVG 5-7y	0.49	0.49 at 02/01	0.43 at 01/01
Bund 2y	-0.64	-0.64 at 04/01	-0.66 at 01/01
Bund 10y	0.44	0.46 at 02/01	0.42 at 01/01
OAT 10y	0.66	0.70 at 02/01	0.66 at 04/01
Corp. BBB	1.21	1.23 at 02/01	1.21 at 04/01
\$ Treas. 2y	1.96	1.96 at 04/01	1.89 at 01/01
Treas. 10y	2.45	2.47 at 02/01	2.41 at 01/01
Corp. BBB	3.63	3.64 at 02/01	3.59 at 01/01
£ Treas. 2y	0.45	0.47 at 02/01	0.40 at 01/01
Treas. 10y	1.27	1.32 at 02/01	1.23 at 01/01

At 4-1-18

10y bond yield &amp; spreads

4.70%	Greece	426 pb
1.98%	Italy	153 pb
1.91%	Portugal	147 pb
1.54%	Spain	110 pb
0.66%	France	22 pb
0.66%	Ireland	22 pb
0.65%	Belgium	21 pb
0.61%	Austria	17 pb
0.60%	Finland	15 pb
0.54%	Netherlands	10 pb
0.44%	Germany	

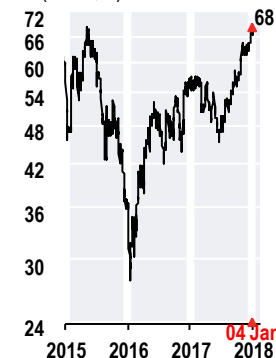
## Commodities

Spot price in dollars		lowest' 18	2018(€)
Oil, Brent	68.1	66.4 at 02/01	+1.6%
Gold (ounce)	1 318	1 303 at 01/01	+0.5%
Metals, LMEX	3 405	3 379 at 03/01	-1.0%
Copper (ton)	7 146	7 101 at 03/01	-1.4%
CRB Foods	341	336 at 01/01	+1.0%
wheat (ton)	162	159 at 01/01	+1.3%
Corn (ton)	128	127 at 01/01	+0.1%

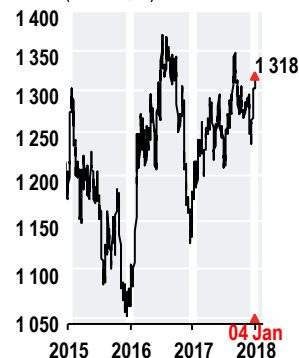
At 4-1-18

Variations

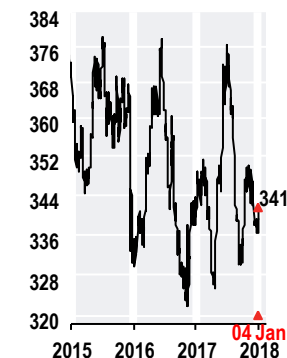
Oil (Brent, \$)



Gold (Ounce, \$)



CRB Foods



## Exchange Rates

€ =		highest' 18	lowest' 18	2018
USD	1.21	1.21 at 04/01	1.20 at 01/01	+0.6%
GBP	0.89	0.89 at 04/01	0.89 at 02/01	+0.4%
CHF	1.18	1.18 at 04/01	1.17 at 01/01	+0.6%
JPY	136.18	136.18 at 04/01	135.08 at 02/01	+0.7%
AUD	1.54	1.54 at 02/01	1.53 at 03/01	+0.0%
CNY	7.85	7.85 at 04/01	7.82 at 03/01	+0.3%
BRL	3.90	3.98 at 01/01	3.90 at 04/01	-2.2%
RUB	68.79	69.36 at 02/01	68.79 at 04/01	-0.5%
INR	76.55	76.64 at 01/01	76.40 at 03/01	-0.1%

At 4-1-18

Variations

## Equity indices

Index		highest' 18	lowest' 18	2018	2018(€)
CAC 40	5 414	5 414 at 04/01	5 289 at 02/01	+1.9%	+1.9%
S&P500	2 724	2 724 at 04/01	2 674 at 01/01	+1.9%	+1.3%
DAX	13 168	13 168 at 04/01	12 871 at 02/01	+1.9%	+1.9%
Nikkei	23 506	23 506 at 04/01	22 765 at 01/01	+3.3%	+2.6%
China*	93	93 at 04/01	88 at 01/01	+4.8%	+4.2%
India*	614	614 at 04/01	606 at 01/01	-0.2%	-0.1%
Brazil*	2 139	2 139 at 04/01	2 023 at 01/01	+2.9%	+5.2%
Russia*	639	639 at 04/01	604 at 01/01	+4.8%	+5.1%

At 4-1-18

Variations

\* MSCI index



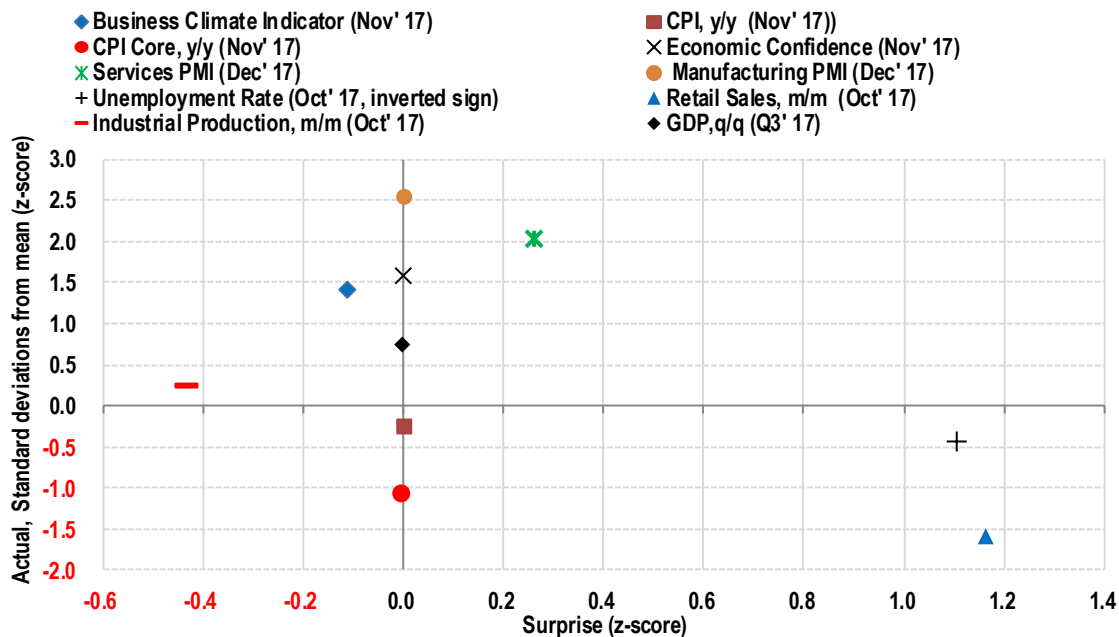
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## Pulse

## Eurozone: A positive picture

Looking at the vertical axis, most indicators are in positive territory, i.e. doing better than the long term average. Inflation is an exception (unsurprisingly), as well as retail sales. Unemployment is also below, which is of course a good sign. Looking at the horizontal axis, most recent data have been in line with expectations. All in all, our pulse indicator paints a positive picture for the eurozone though low inflation remains an issue.



Sources: Markit, Bloomberg, BNP Paribas calculations

## Indicators preview

Markets will follow closely the release next week of the producer price and consumer price inflation in the US so as to assess whether they change the outlook for Fed policy. For the eurozone, the economic confidence indicator should confirm the strength of the upswing. Analysts will scrutinise the meeting account of the ECB for indications of differences of opinion with respect to QE in 2018.

Date	Country	Event	Period	Survy	Prior
01/08/18	Eurozone	Economic Confidence	Dec	114.7	114.6
01/09/18	Eurozone	Unemployment Rate	Nov	8.8%	8.8%
01/09/18	United States	NFIB Small Business Optimism	Dec	108.0	107.5
01/10/18	France	Industrial Production MoM	Nov	--	1.9%
01/10/18	United Kingdom	Industrial Production MoM	Nov	0.4%	0.0%
01/11/18	France	Bank of France Ind. Sentiment	Dec	--	106
01/11/18	Eurozone	Industrial Production SA MoM	Nov	0.6%	0.2%
01/11/18	Eurozone	ECB account of the monetary policy meeting			
01/11/18	United States	PPI Ex Food, Energy, Trade MoM	Dec	0.2%	0.4%
01/12/18	France	CPI EU Harmonized MoM	Dec	--	0.4%
01/12/18	United States	CPI Ex Food and Energy MoM	Dec	0.2%	0.1%
01/12/18	United States	Retail Sales Advance MoM	Dec	0.4%	0.8%

Sources: Bloomberg, BNP Paribas



## Economic scenario

### UNITED STATES

- GDP growth is accelerating along with the recovery in the emerging countries and reinforcing world trade. However the fiscal outlook remains uncertain. A fiscal stimulus still is possible, but it would not be implemented very rapidly. 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 1.50% by year-end, 2.00% by mid-2018.

### CHINA

- Economic growth has started to moderate during the fall and this trend should continue in the coming quarters.
- Despite the slowdown, the central bank will have to continue to act to encourage the deleveraging of financial institutions and corporates and reduce financial instability risks. The authorities should maintain an expansionist fiscal policy in the short term.
- The tightening of domestic credit conditions, restructuring measures in the industry and the correction in the property market will weigh on economic activity. Meanwhile, exports and private consumption should be supporting factors.

### 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		
	2017 e	2018 e	2019 e	2017 e	2018 e	2019 e
<b>Advanced</b>	<b>2,1</b>	<b>2,4</b>	<b>1,7</b>	<b>1,7</b>	<b>1,7</b>	<b>1,9</b>
United-States	2,3	2,9	1,9	2,1	2,0	2,2
Japan	1,5	1,3	0,6	0,3	0,6	0,8
United-Kingdom	1,5	1,2	1,8	2,7	2,7	2,4
<b>Euro Area</b>	<b>2,3</b>	<b>2,4</b>	<b>1,8</b>	<b>1,5</b>	<b>1,6</b>	<b>1,7</b>
Germany	2,6	2,8	2,1	1,7	1,7	1,8
France	1,8	2,0	1,6	1,2	1,6	1,8
Italy	1,6	1,5	1,1	1,4	1,4	1,5
Spain	3,1	2,6	2,2	2,1	1,8	1,6
Belgium	1,6	1,6	1,5	2,1	1,9	1,9
<b>Emerging</b>	<b>4,5</b>	<b>4,8</b>	<b>4,9</b>	<b>4,0</b>	<b>4,2</b>	<b>4,2</b>
China	6,8	6,4	6,5	1,6	2,3	2,5
India	7,0	7,6	7,8	3,4	4,5	4,9
Brazil	1,0	3,0	2,5	3,5	3,5	3,9
Russia	1,8	1,6	1,5	4,0	4,3	4,5

Source : BNP Paribas Group Economic Research (e: Estimates & forecasts)

### INTEREST RATES & FX RATES

Interest rates, %		2018				2019
End of period		Q1e	Q2e	Q3e	Q4e	Q4e
<b>US</b>	Fed Funds	1.75	2.00	2.25	2.25	2.25
	Libor 3m \$	1.55	1.70	1.80	1.85	1.75
	T-Notes 10y	2.60	2.75	2.75	3.00	2.90
<b>Ezone</b>	ECB Refi	0.00	0.00	0.00	0.00	0.25
	Euribor 3m	-0.30	-0.30	-0.30	-0.30	0.10
	Bund 10y	0.65	0.75	1.10	1.50	1.80
	OAT 10y	0.95	1.00	1.30	1.70	2.00
<b>UK</b>	Base rate	0.50	0.50	0.50	0.75	1.25
	Gilt 10y	1.45	1.55	1.90	2.30	2.30
<b>Japan</b>	BoJ Rate	-0.10	-0.10	-0.10	-0.10	-0.10
	JGB 10y	0.08	0.08	0.08	0.08	0.00

Exchange Rates		2018				2019
End of period		Q1e	Q2e	Q3e	Q4e	Q4e
<b>USD</b>	EUR / USD	1.14	1.13	1.18	1.22	1.30
	USD / JPY	116	117	115	112	105
	GBP / USD	1.25	1.26	1.33	1.39	1.48
	USD / CHF	1.03	1.04	1.01	0.98	0.96
<b>EUR</b>	EUR / GBP	0.91	0.90	0.89	0.88	0.88
	EUR / CHF	1.17	1.18	1.19	1.20	1.25
	EUR / JPY	132	132	136	137	137

Source : GlobalMarkets (e: Estimates & forecasts)



# GROUP ECONOMIC RESEARCH

■ **William DE VIJDER**  
Chief Economist

+33.(0)1 55 77 47 31

[william.devijlder@bnpparibas.com](mailto:william.devijlder@bnpparibas.com)

## ADVANCED ECONOMIES AND STATISTICS

■ **Jean-Luc PROUTAT**  
Head

+33.(0)1.58.16.73.32

[jean-luc.proutat@bnpparibas.com](mailto:jean-luc.proutat@bnpparibas.com)

■ **Alexandra ESTIOT**  
Works coordination - United States - United Kingdom - Globalisation

+33.(0)1.58.16.81.69

[alexandra.estiot@bnpparibas.com](mailto:alexandra.estiot@bnpparibas.com)

■ **Hélène BAUDCHON**  
France (short-term outlook and forecasts) - Labour markets

+33.(0)1.58.16.03.63

[helene.baudchon@bnpparibas.com](mailto:helene.baudchon@bnpparibas.com)

■ **Frédérique CERISIER**  
Euro Area (European governance and public finances), Spain, Portugal

+33.(0)1.43.16.95.52

[frederique.cerisier@bnpparibas.com](mailto:frederique.cerisier@bnpparibas.com)

■ **Thibault MERCIER**  
Euro Area (short-term outlook and monetary policy), France (structural reforms)

+33.(0)1.57.43.02.91

[thibault.mercier@bnpparibas.com](mailto:thibault.mercier@bnpparibas.com)

■ **Catherine STEPHAN**  
Nordic countries - World trade - Education, health, social conditions

+33.(0)1.55.77.71.89

[catherine.stephan@bnpparibas.com](mailto:catherine.stephan@bnpparibas.com)

■ **Raymond VAN DER PUTTEN**  
Germany, Netherlands, Austria, Switzerland - Energy, climate - Long-term projections

+33.(0)1.42.98.53.99

[raymond.vanderputten@bnpparibas.com](mailto:raymond.vanderputten@bnpparibas.com)

■ **Tarik RHARRAB**  
Statistics and Modelling

+33.(0)1.43.16.95.56

[tarik.rharrab@bnpparibas.com](mailto:tarik.rharrab@bnpparibas.com)

## BANKING ECONOMICS

■ **Laurent QUIGNON**  
Head

+33.(0)1.42.98.56.54

[laurent.quignon@bnpparibas.com](mailto:laurent.quignon@bnpparibas.com)

■ **Céline CHOLET**

+33.(0)1.43.16.95.54

[celine.choulet@bnpparibas.com](mailto:celine.choulet@bnpparibas.com)

■ **Thomas HUMBLLOT**

+33.(0)1.40.14.30.77

[thomas.humblot@bnpparibas.com](mailto:thomas.humblot@bnpparibas.com)

## EMERGING ECONOMIES AND COUNTRY RISK

■ **François FAURE**  
Head - Argentina

+33.(0)1 42 98 79 82

[francois.faure@bnpparibas.com](mailto:francois.faure@bnpparibas.com)

■ **Christine PELTIER**  
Deputy Head - Greater China, Vietnam, other North Asian countries, South Africa

+33.(0)1.42.98.56.27

[christine.peltier@bnpparibas.com](mailto:christine.peltier@bnpparibas.com)

■ **Stéphane ALBY**  
Africa (French-speaking countries)

+33.(0)1.42.98.02.04

[stephane.alby@bnpparibas.com](mailto:stephane.alby@bnpparibas.com)

■ **Sylvain BELLEFONTAINE**  
Turkey, Latin America

+33.(0)1.42.98.26.77

[sylvain.bellefontaine@bnpparibas.com](mailto:sylvain.bellefontaine@bnpparibas.com)

■ **Sara CONFALONIERI**  
Africa (Portuguese & English-speaking countries)

+33.(0)1.42.98.43.86

[sara.confalonieri@bnpparibas.com](mailto:sara.confalonieri@bnpparibas.com)

■ **Pascal DEVAUX**  
Middle East, Balkan countries

+33.(0)1.43.16.95.51

[pascal.devau@bnpparibas.com](mailto:pascal.devau@bnpparibas.com)

■ **Anna DORBEC**  
CIS, Central European countries

+33.(0)1.42.98.48.45

[anna.dorbec@bnpparibas.com](mailto:anna.dorbec@bnpparibas.com)

■ **Hélène DROUOT**  
Korea, Thailand, Philippines, Andean countries

+33.(0)1.42.98.33.00

[helene.drouot@bnpparibas.com](mailto:helene.drouot@bnpparibas.com)

■ **Johanna MELKA**  
India, South Asia, Russia

+33.(0)1.58.16.05.84

[johanna.melka@bnpparibas.com](mailto:johanna.melka@bnpparibas.com)

■ **Michel BERNARDINI**  
Contact Média

+33.(0)1.42.98.05.71

[michel.bernardini@bnpparibas.com](mailto:michel.bernardini@bnpparibas.com)



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 Registered Office: 16 boulevard des Italiens – 75009 PARIS  
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