

# ECOWEEK

No. 18-21, 25 May 2018

## Eurozone: domestic support, global risks

- The ECB meeting account shows a central bank which is confident about the growth outlook despite the recent softness of data
- The concerns relate to global factors which have become more prominent: the threat of trade protectionism ■ This concern is also echoed by the Federal Reserve

The much expected manufacturing, services and composite PMIs for May produced by IHS Markit confirmed what is now looking as a trend: for the eurozone, Germany and France all series were down except for the French manufacturing PMI. However, the indices remain at high levels so we should speak of 'softening' or 'easing' rather than 'declining'. Semantic nuances don't stop analysts from feeling a certain unease. After all, the eurozone PMIs, following their decline, are now at a level not seen in the past twelve months.

The question of "what's going on" is covered at length in the account of the ECB meeting of 25-26 April published on 24 May. In summary three things are happening: 1) temporary factors like the harsh winter have weighed on growth; 2) after surprisingly strong sentiment, data are returning to normal, with underlying momentum remaining intact; 3) supply side bottlenecks in some countries (e.g. Germany) and sectors (e.g. construction) are weighing on growth. Enough reasons for not being carried away by the softening of many survey data in recent months. In this respect, the European Commission eurozone consumer confidence for May published on 23 May provided additional comfort. Looking ahead, the drivers of final demand (consumption, investment, government spending, exports) still look robust: a slightly expansionary fiscal policy, job creation, wage gains, low interest rates, earnings growth, rising capacity utilisation, global trade growth. With sentiment data weakening however, a prudent observer will pay particular attention to sources of downside risk, which are essentially of a global nature. If oil prices were to keep on rising, the drag on growth would of course increase. In addition there is the threat of increased protectionism. In its insistence on this factor the ECB is joined by the Federal Reserve: the FOMC meeting minutes refer to trade as a source of uncertainty. Monitoring comments of company executives will become particularly important: trade-related uncertainty over an extended period of time would end up weighing on investment intentions considering that investment projects, once launched, are hard to stop. This in turn could spill over to hiring intentions and end up impacting households.

PURCHASING MANAGER INDICES														
	Manufacturing							Services						
	EURO ZONE	AUSTRIA	FRANCE	GERMANY	IRELAND	ITALY	NETHERLANDS	EURO ZONE	FRANCE	GERMANY	IRELAND	ITALY	SPAIN	
Jun-17	57.4	60.7	54.8	59.6	56.0	55.2	58.6	54.7	55.4	56.9	54.0	57.6	53.6	58.3
Jul-17	56.6	60.0	54.9	58.1	54.6	55.1	58.9	54.0	55.4	56.0	53.1	58.3	56.3	57.6
Aug-17	57.4	61.1	55.8	59.3	56.1	56.3	59.7	52.4	54.7	54.9	53.5	58.4	55.1	56.0
Sep-17	58.1	59.4	56.1	60.6	55.4	56.3	60.0	54.3	55.8	57.0	55.6	58.7	53.2	56.7
Oct-17	58.5	59.4	56.1	60.6	54.4	57.8	60.4	55.8	55.0	57.3	54.7	57.5	52.1	54.6
Nov-17	60.1	61.9	57.7	62.5	58.1	58.3	62.4	56.1	56.2	60.4	54.3	56.0	54.7	54.4
Dec-17	60.6	64.3	58.8	63.3	59.1	57.4	62.2	55.8	56.6	59.1	55.8	60.4	55.4	54.6
Jan-18	59.6	61.3	58.4	61.1	57.6	59.0	62.5	55.2	58.0	59.2	57.3	59.8	57.7	56.9
Feb-18	58.6	59.2	55.9	60.6	56.2	56.8	63.4	56.0	56.2	57.4	55.3	57.2	55.0	57.3
Mar-18	56.6	58.0	53.7	58.2	54.1	55.1	61.5	54.8	54.9	56.9	53.9	56.5	52.6	56.2
Apr-18	56.2	58.0	53.8	58.1	55.3	53.5	60.7	54.4	54.7	57.4	53.0	58.4	52.6	55.6
May-18	55.5		55.1	56.8					53.9	54.3	52.1			

Source: Markit, BNP Paribas

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ECONOMIC RESEARCH DEPARTMENT



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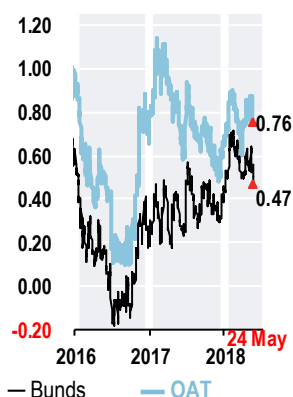
## Markets overview

### The essentials

Week 18-5 18 > 24-5-18

➤ CAC 40	5 615	▶ 5 548	-1.2 %
➤ S&P 500	2 713	▶ 2 728	+0.5 %
➤ Volatility (VIX)	13.4	▶ 12.5	-0.9 pb
➤ Euribor 3M (%)	-0.33	▶ -0.32	+0.2 bp
➤ Libor \$ 3M (%)	2.33	▶ 2.33	+0.1 bp
➤ OAT 10y (%)	0.84	▶ 0.76	-8.6 bp
➤ Bund 10y (%)	0.58	▶ 0.47	-10.6 bp
➤ US Tr. 10y (%)	3.07	▶ 2.98	-9.4 bp
➤ Euro vs dollar	1.18	▶ 1.17	-0.4 %
➤ Gold (ounce, \$)	1 292	▶ 1 305	+1.0 %
➤ Oil (Brent, \$)	79.2	▶ 79.1	-0.1 %

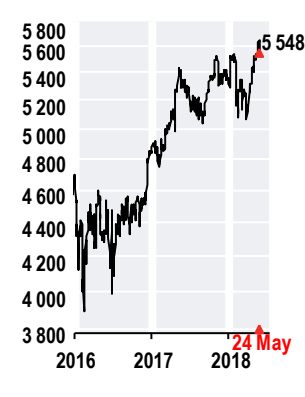
10 y bond yield, OAT vs Bund



Euro-dollar



CAC 40



### Money & Bond Markets

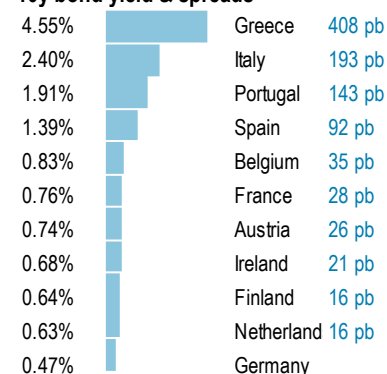
Interest Rates	highest' 18	lowest' 18
€ ECB	0.00	0.00 at 01/01
Eonia	-0.36	-0.35 at 01/01
Euribor 3M	-0.32	-0.32 at 23/05
Euribor 12M	-0.19	-0.19 at 01/01
\$ FED	1.75	1.50 at 22/03
Libor 3M	2.33	2.37 at 04/05
Libor 12M	2.75	2.78 at 27/04
£ BoE	0.50	0.50 at 01/01
Libor 3M	0.62	0.79 at 19/04
Libor 12M	0.92	1.06 at 17/04

At 24-5-18

Yield (%)	highest' 18	lowest' 18
€ AVG 5-7y	0.59	0.41 at 15/02
Bund 2y	-0.64	-0.55 at 07/03
Bund 10y	0.47	0.42 at 15/02
OAT 10y	0.76	0.60 at 08/02
Corp. BBB	1.55	1.17 at 23/05
\$ Treas. 2y	2.49	1.89 at 16/05
Treas. 10y	2.98	2.41 at 17/05
Corp. BBB	4.31	3.59 at 17/05
£ Treas. 2y	0.64	0.40 at 21/03
Treas. 10y	1.44	1.23 at 15/02

At 24-5-18

10y bond yield & spreads



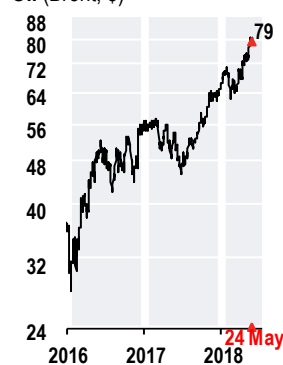
### Commodities

Spot price in dollars	lowest' 18	2018(€)
Oil, Brent	62.2 at 13/02	+21.6%
Gold (ounce)	1 288 at 17/05	+2.5%
Metals, LME	3 343 at 26/03	+0.2%
Copper (ton)	6 556 at 26/03	-2.5%
CRB Foods	335 at 04/04	+8.7%
wheat (ton)	155 at 16/01	+28.5%
Corn (ton)	126 at 08/01	+18.3%

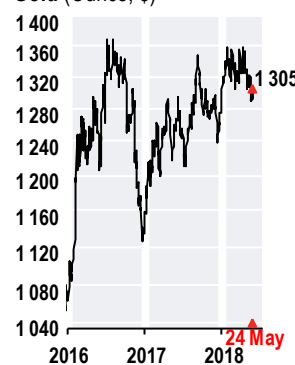
At 24-5-18

Variations

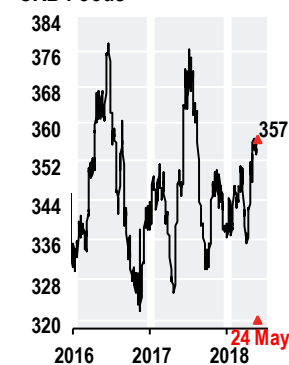
Oil (Brent, \$)



Gold (Ounce, \$)



CRB Foods



### Exchange Rates

€ =	highest' 18	lowest' 18	2018
USD	1.25 at 25/01	1.17 at 23/05	-2.4%
GBP	0.89 at 02/03	0.86 at 17/04	-1.2%
CHF	1.20 at 19/04	1.15 at 27/02	-0.7%
JPY	137.29 at 02/02	127.81 at 24/05	-5.5%
AUD	1.61 at 26/03	1.53 at 09/01	+1.0%
CNY	7.92 at 25/01	7.47 at 23/05	-4.3%
BRL	4.41 at 18/05	3.87 at 08/01	+7.5%
RUB	72.24 at 11/04	68.06 at 09/01	+4.5%
INR	80.10 at 25/04	75.92 at 08/01	+4.5%

At 24-5-18

Variations

### Equity indices

Index	highest' 18	lowest' 18	2018	2018(€)
CAC 40	5 640 at 22/05	5 066 at 26/03	+4.4%	+4.4%
S&P500	2 873 at 26/01	2 581 at 08/02	+2.0%	+4.5%
DAX	13 560 at 23/01	11 787 at 26/03	-0.5%	-0.5%
Nikkei	24 124 at 23/01	20 618 at 23/03	-1.4%	+4.3%
China*	92 at 26/01	88 at 09/02	+4.2%	+6.4%
India*	552 at 29/01	547 at 23/05	-3.3%	-7.5%
Brazil*	1 914 at 26/01	1 914 at 24/05	+4.2%	-3.1%
Russia*	620 at 26/02	571 at 16/04	+8.9%	+5.2%

At 24-5-18

Variations

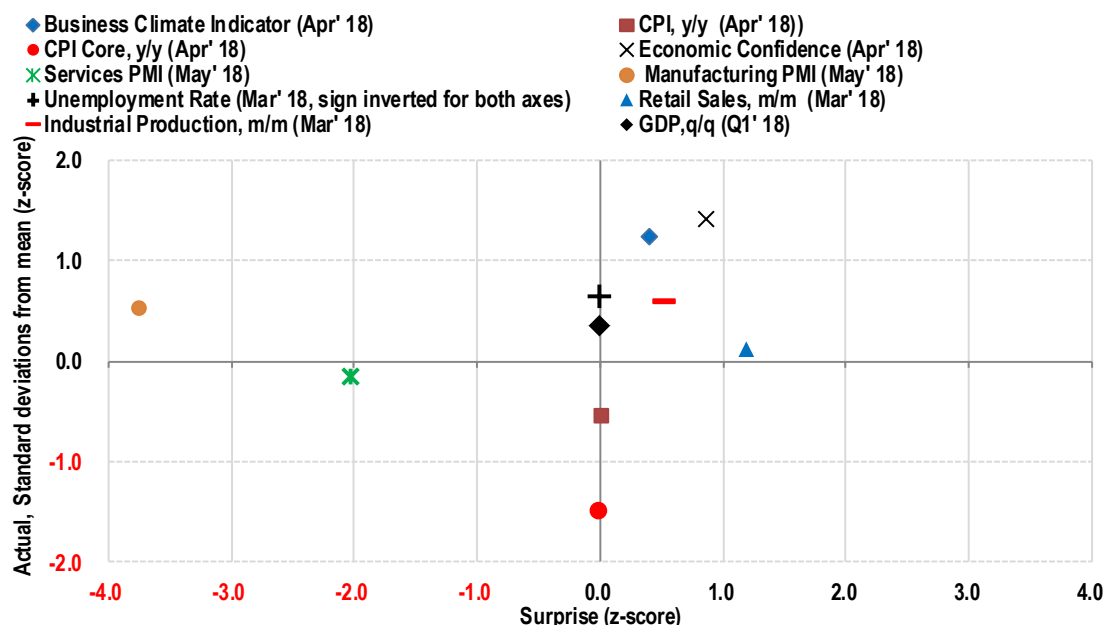
\* MSCI index



## Pulse

## Eurozone: subdued inflation, softer sentiment

The chart sums up pretty well the situation in the eurozone. Inflation, though in line with expectations, is below the long term average, hence the caution of the ECB in modifying its policy stance. Activity and demand-related data on the other hand are above the long term average, reflecting robust growth, although the PMIs for May came in below expectations, warranting close monitoring of data in coming weeks so as to gauge whether we're experiencing a mere normalisation or something more significant.



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,  $\mu$ : mean,  $\sigma$ : standard deviation. On the X-axis,  $x$  corresponds at the last known surprise for each indicator represented on the graph,  $\mu$  and  $\sigma$  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,  $\mu$  and  $\sigma$  corresponds respectively to the mean and the standard deviation for this indicator since 2000 (for China since 2011).

## Indicators preview

Next week will see many important data releases with consumer confidence in France, the US, Japan, the UK, the eurozone as well as the Markit PMIs in several countries. Inflation data in France and Germany will also be important in the run-up to the ECB meeting in June. The OECD will publish its new forecasts and the beige book will help assessing how the US economy is doing. Finally on Friday 1 June we will have both the ISM and the labour market data in the US.

Date Time	Country	Event	Period	Survey	Prior
05/29/18	France	Consumer Confidence	May	--	101
05/29/18	United States	Conf. Board Consumer Confidence	May	128.0	128.7
05/30/18	Japan	Consumer Confidence Index	May	--	43.6
05/30/18	France	GDP QoQ	1Q	--	0.3%
05/30/18	Germany	Unemployment Claims Rate SA	May	--	5.3%
05/30/18	Eurozone	Economic Confidence	May	--	112.7
05/30/18	Eurozone	OECD Economic Forecasts			
05/30/18	Eurozone	Consumer Confidence	May	--	--
05/30/18	Germany	CPI EU Harmonized MoM	May	--	-0.1%
05/30/18	United States	ADP Employment Change	May	195 000	204 000
05/30/18	United States	U.S. Federal Reserve Releases Beige Book			
05/31/18	United Kingdom	GfK Consumer Confidence	May	--	-9
05/31/18	France	CPI EU Harmonized MoM	May	--	0.2%
05/31/18	Eurozone	Unemployment Rate	April	--	8.5%
05/31/18	United States	PCE Core MoM	April	0.1%	0.2%
06/01/18	France	Markit France Manufacturing PMI	May	--	55.1
06/01/18	Eurozone	Markit Eurozone Manufacturing PMI	May	--	55.5
06/01/18	United States	Change in Nonfarm Payrolls	May	195 000	164 000
06/01/18	United States	ISM Manufacturing	May	58.0	57.3

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. Tax cuts would add +0.5 pp to the GDP growth this year, that would trend near 3%.
- The labour market is as buoyant as ever, showing its first signs of tension (participation rates and real wages are up).
- Fed Funds rates: 1.75% in Q1 2018, 2% by mid-2018.

### CHINA

- Economic growth will decelerate in 2018. 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. Fiscal policy should remain expansionist.
- The outlook for exports and household spending is rather favourable in the short term, but the tightening of domestic credit conditions, restructuring measures in the industry and less buoyant property market will weigh on economic activity.

### 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 ECB is expected to remain cautious. Possible extension of APP after Sept. no rates hike before mid-2019.

### FRANCE

- A clear growth acceleration is underway. Households' consumption is supported by the jobs recovery but restrained by the upturn in inflation. Investment and exports dynamics are favourable.
- A slight rise in inflation is appearing but remains to be confirmed.

### INTEREST RATES AND FX RATES

- In the US, ongoing strong growth and a very low unemployment rate pave the way for several rate hikes (we expect 4 this year and 1 next). This will put upward pressure on bond yields in 2018. The ECB is expected to stop its QE programme at the end of 2018 and to hike its rates by the middle of 2019. As a consequence, bond yields should follow a rising trend, including in 2019. No change expected in Japan
- The narrowing bond yield differential between the US and the eurozone should cause a strengthening of the euro, all the more so considering it is still below its long-term fair value (around 1.34).

### SUMMARY

%	GDP Growth			Inflation		
	2017	2018 e	2019 e	2017	2018 e	2019 e
<b>Advanced</b>	<b>2.2</b>	<b>2.6</b>	<b>1.9</b>	<b>1.8</b>	<b>1.9</b>	<b>1.8</b>
United-States	2.3	3.1	2.1	2.1	2.3	2.1
Japan	1.7	1.3	0.6	0.5	0.9	0.9
United-Kingdom	1.8	1.5	1.8	2.7	2.6	2.1
<b>Euro Area</b>	<b>2.5</b>	<b>2.6</b>	<b>2.1</b>	<b>1.5</b>	<b>1.7</b>	<b>1.7</b>
Germany	2.5	2.4	2.0	1.7	1.8	1.9
France	2.0	2.3	1.9	1.2	1.6	1.7
Italy	1.5	1.5	1.2	1.3	1.4	1.5
Spain	3.1	2.8	2.2	2.0	1.6	1.6
Netherlands	3.3	2.3	1.7	1.3	1.7	1.8
<b>Emerging</b>						
China	6.9	6.4	6.4	1.6	2.3	2.5
India	6.6	7.4	7.6	3.6	4.5	4.2
Brazil	1.0	3.0	3.5	3.4	3.3	3.8
Russia	1.5	1.8	1.7	3.7	3.0	4.0

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

### INTEREST RATES & FX RATES

Interest rates, %		2018				2017	2018e	2019e
End of period		Q1e	Q2e	Q3e	Q4e			
<b>US</b>	Fed Funds	1.75	2.00	2.25	2.50	1.50	2.50	2.75
	Libor 3m \$	2.01	2.15	2.35	2.55	1.69	2.55	2.55
	T-Notes 10y	3.00	3.10	3.20	3.25	2.41	3.25	3.00
<b>Ezone</b>	ECB Refi	0.00	0.00	0.00	0.00	0.00	0.00	0.25
	Euribor 3m	-0.33	-0.33	-0.33	-0.33	-0.33	-0.33	0.07
	Bund 10y	0.70	0.85	1.20	1.50	0.42	1.50	1.80
	OAT 10y	1.00	1.10	1.40	1.70	0.66	1.70	2.05
<b>UK</b>	Base rate	0.50	0.75	0.75	1.00	0.50	1.00	1.50
	Gilts 10y	1.55	1.65	1.75	1.90	1.23	1.90	2.25
<b>Japan</b>	BoJ Rate	-0.10	-0.10	-0.10	-0.10	-0.04	-0.10	-0.10
	JGB 10y	0.06	0.08	0.08	0.08	0.05	0.08	0.00

Exchange Rates		2018				2017	2018e	2019e
End of period		Q1e	Q2e	Q3e	Q4e			
<b>USD</b>	EUR / USD	1.26	1.27	1.28	1.28	1.20	1.28	1.34
	USD / JPY	106	105	104	102	113	102	98
	GBP / USD	1.38	1.41	1.44	1.45	1.35	1.45	1.52
	USD / CHF	0.93	0.93	0.93	0.94	0.97	0.94	0.93
<b>EUR</b>	EUR / GBP	0.91	0.90	0.89	0.88	0.89	0.88	0.88
	EUR / CHF	1.17	1.18	1.19	1.20	1.17	1.20	1.25
	EUR / JPY	134	133	133	131	135	131	131

Source: GlobalMarkets BNP Paribas (e: estimates & forecasts)



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Prepared by Economic Research – BNP PARIBAS  
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Tel: +33 (0) 1.42.98.12.34 – Internet :  
[www.group.bnpparibas.com](http://www.group.bnpparibas.com)  
Publisher: Jean Lemierre. Editor: William De Vijlder



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