



Summary

United States

Not this time either

We expect monetary status quo from the Fed. Financial markets regained their calm, but the rebound in oil prices came to a halt, postponing the date at which inflation will move back towards target. Prospects for growth, and the way the Fed sees them, are as dependent as ever on the labour market.

► Page 2

Eurozone

ECB: See you in September

The ECB left its policy unchanged. The central bank esteems that the Brexit victory increases the downside risks to European growth, but that it is still too early to assess the precise effect. Mario Draghi gives a rendezvous in September.

► Page 3

Market overview

► Page 4

Summary of forecasts

► Page 5

Also in :



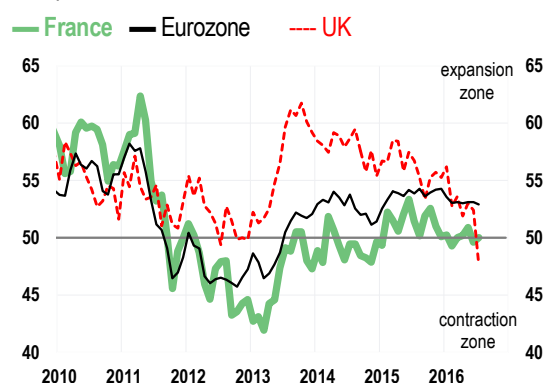
Brexit and business confidence: first effects

- A net, widespread improvement in business confidence in France
- Limited deterioration in the Eurozone ■ The UK plunges

July's improvement in the business climate in France stands as an exception. The Insee composite index regained the two points lost in June. After disruptions due to the blockades of refineries and other labour unrest, the catching-up effect won the upper hand over the negative effects expected from all the uncertainty engendered by the Brexit vote. The only trace that could be seen was in the business leaders' assessments of their own production prospects, which dropped 6 points. Otherwise the results were strong. For the first time since November 2014, there was a widespread improvement in business confidence, which touched all sectors (confidence rose 1 point in industry and construction, 2 points in wholesaling and 3 points in services and retailing). Markit PMI indexes (flash estimates) point in the same direction, albeit more moderately. The composite index gained 0.4 points to 50, lifted by the manufacturing sector as well as services. In contrast, the same figures for the Eurozone were in decline, with a sharp drop in manufacturing (down 0.9 points to 51.9) and virtually none in services (-0.1 point to 52.7), which limited the overall decline in the composite index (-0.2 points to 52.9). In the UK, the business climate index plunged, down nearly 5 points in services (to 47.4) and 3 points in manufacturing (to 49.1). The composite index shed 4.7 points to 47.7. Although the decline in the UK was surprisingly strong, it seems only natural that it would be the first to feel the negative effects of Brexit. Even so, we should continue to expect knock-on effects to strain activity on this side of the Channel.

BUSINESS CONFIDENCE

Composite PMI



Source: Markit

THE WEEK ON THE MARKETS

Week 15-7 16 > 21-7-16

↗ CAC 40	4 373	► 4 376	+0.1 %
↗ S&P 500	2 162	► 2 165	+0.2 %
↗ Volatility (VIX)	12.7	► 12.7	+0.1 %
↘ Euribor 3M (%)	-0.29	► -0.30	-0.4 bp
↗ Libor \$ 3M (%)	0.69	► 0.70	+1.4 bp
↘ OAT 10y (%)	0.23	► 0.23	-0.4 bp
↘ Bund 10y (%)	-0.06	► -0.07	-0.5 bp
↘ US Tr. 10y (%)	1.59	► 1.56	-2.9 bp
↘ Euro vs dollar	1.11	► 1.10	-0.7 %
↘ Gold (ounce, \$)	1 328	► 1 323	-0.4 %
↘ Oil (Brent, \$)	47.7	► 46.8	-2.0 %

Source: Thomson Reuters



United States

Not this time either

- The Fed is expected to leave its monetary policy unchanged again. After a few days of severe turmoil, the financial markets have levelled off, resulting in an easing of US monetary and financial conditions.
- After the rebound in oil prices came to a halt, inflation prospects have been pulled downward, albeit mildly.
- Once again, US cyclical trends – as well as the Fed's analysis – are closely linked to job market trends.

The June FOMC meeting maintained the monetary status quo, also because its members thought it best to be cautious while awaiting the results of the UK referendum. A month after the vote, it is still too early to fully measure the consequences of the UK's decision to leave the EU. The financial markets' initial reaction was very abrupt, but the situation quickly stabilised. The dollar appreciated, but then levelled off, and it has not gained very much in effective terms (the effective exchange rate has increased by roughly 1.5% since the Brexit vote, but is still about 2% below the level at the beginning of the year). The equity markets plunged in the aftermath of the referendum, but have since recovered, and the S&P500 index is now about 3% higher than the pre-Brexit level. Interest rates are lower than before the 23 June referendum (by about 20 basis points for 10-year Treasuries, mortgage rates and the spread on BAA-rated corporate bonds). All in all, monetary and financial conditions have eased, which should give US economic growth a boost, even if mildly. In contrast, the rebound in oil prices was cut short, and prices have levelled off at about USD 6.55 below the peak of early June (West Texas Intermediate was trading at USD 51.2 per barrel on 8 June, before dropping to USD 44.7 on 21 July). This trend further pushes back the horizon for US inflation to return to the Fed's target rate, as illustrated by the slight decline in 5-year inflation expectations.

Brexit seems to have left the US unscathed, at least for the moment. If the only reason for the June decision to maintain the monetary status quo had been the uncertainty that prevailed prior to the referendum, then we could be virtually guaranteed of a July rate increase. Yet this was not the case. Last month the Fed surely feared that a "leave" vote could potentially have severely disruptive effects on world financial markets, similar to the sell-off triggered by China's official announcements in summer 2015. This risk has certainly not been lifted yet, and the month of August must be approached with caution, especially since shallow liquidity could exacerbate the size of any adjustments. Even so, the risk seems mild. The UK's rapid and apparently serene transition of power, as well as the stabilisation of Sterling's external value, are very encouraging.

What seems to be worrying the Fed even more are job market trends. At the latest FOMC meeting, members only had access to the May

A rebound that came to a halt

- Inflation expectations (5-year TIPS vs T-Bond yield, %)
- West Texas Intermediate (USD per barrel)

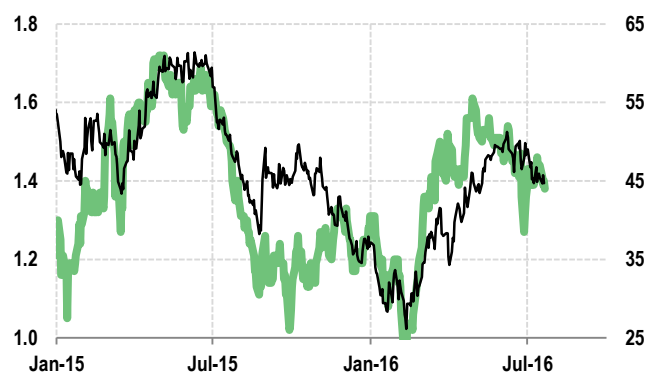


Chart 1

Source : Macrobond

jobs report: job creations were estimated at only 38k, a figure that was later revised downwards (to 11k). June's correction was just as impressive, but in the other direction, with 287k job creations. Yet smoothed over 3 months, these employment trends continue to indicate a slowdown (147k in June, down from more than 200k through March). In itself, there is nothing alarming about that: if this pace were sustained over time, it would be strong enough to stabilise the unemployment rate. Other job market indicators, in contrast, are less reassuring: 1) the labour participation ratio for the 25-54 age group shed 0.2 percentage points after rising constantly for six months, and 2) wage acceleration has stalled. Although it is too early to speak of a deteriorating situation, the overall improvement in job market conditions seems to have stalled.

This pause might be short lived if it is due solely to the consequences of the cyclical slowdown earlier this year. If this is the case, then the most recently available economic figures for June are rather encouraging, with manufacturing production up 0.5%, retail sales up 0.6% and housing starts up 4.8%. Our M&N composite economic indicator – the weighted sum of ISM survey data – rebounded very strongly recently to peak at 56 in June, the highest level since last fall.

The Fed probably wants to move away from the zero lower bound as quickly and as far as possible. Yet the persistent risks associated with a premature tightening of monetary policy also call for caution. If the good news is confirmed by September – and accompanied by another reduction in underemployment – then it could create a window of opportunity for a key rate increase.



Eurozone

ECB: See you in September

- The ECB is maintaining the monetary status quo. The central bank esteems that the Brexit victory increases the downside risks to European growth, but that it is still too early to assess the precise effect.
- Mario Draghi gives a rendezvous in September when the ECB will present its updated macroeconomic projections. M. Draghi reiterated the ECB's "readiness, willingness ability" to act if needed, emphasising the availability of all instruments within its mandate.
- The press conference was dominated by questions on the parameters of the Public Sector Purchase Programme (PSPP) and the situation of banks, notably in Italy.
- Without going into detail, M. Draghi said the central bank had shown flexibility so far in meeting its monthly purchasing targets.
- As to the Italian banks, M. Draghi said he was in favour of a public backstop under exceptional circumstances to avoid fire sale, while letting the decision up to the European Commission

After the Bank of England last week, the European Central Bank (ECB) maintained the monetary status quo at its July monetary policy meeting. While acknowledging that the Brexit victory in the UK referendum creates downside risk for the eurozone recovery, Mario Draghi said it was still too early to fully assess the effects and to draw the right conclusions for guiding monetary policy. He also noted that the financial markets have shown "encouraging resilience" to the shock while underscoring the key role of the announced readiness of central banks to provide liquidity.

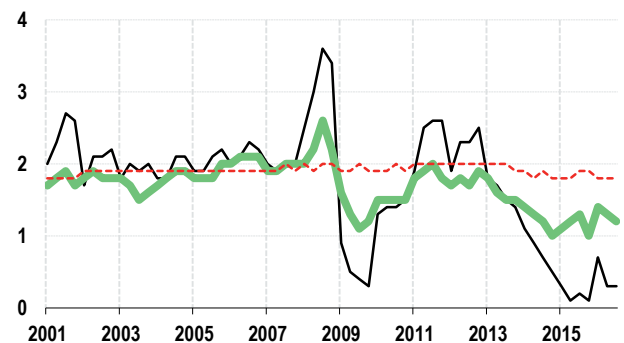
Announcements of monetary policy changes are likely to take place in September, when the ECB presents its updated macroeconomic projections until 2018. In the meantime, a series of economic data and survey covering the summer months will provide a more precise idea of the first repercussions the UK "leave" vote will have on the eurozone economy. Earlier this week, the European Commission published its preliminary estimate of the impact, which calls for growth to slow between 0.25 and 0.5 points by 2017. This estimate must be taken cautiously said M. Draghi, however, as it is hard to measure the impact of uncertainty arising from the more or less lengthy negotiations between the UK and the EU. In any case, those negotiations will not begin until the UK government officially notifies the European Council of its intention to leave the EU, which could take several months.

As to inflation, M. Draghi pointed out that, unlike market expectations, surveys of professional forecasts do not show any material signs of a downturn in inflation expectations due to Brexit so far. Nevertheless, the expected downward revisions of growth forecasts are bound to have an impact on prices dynamics. Although headline inflation

Survey of Professional Forecasters

Inflation expectations

— current year — next year — 5 years ahead



Graphique

Source : ECB

should automatically rise as of year-end 2016 due to the base effects of energy prices, core inflation (excluding energy and food items), the most pertinent measure from a medium-term perspective, could be revised downwards. Under this scenario, the central bank would probably announce stronger monetary support. M. Draghi reiterated the ECB's "readiness, willingness ability" to act if needed, emphasising the availability of all instruments within its mandate. Our forecast is an extension by six months of the asset purchases programme, which would run through September 2017 at the earliest.

The press conference was dominated by questions on the parameters of the Public Sector Purchase Programme (PSPP) and the situation of banks, notably in Italy. After repeatedly stating that the PSPP parameters had not been discussed by the Governing Council, M. Draghi did point out that the ECB had been able to exploit the existing flexibility of the programme so far in order to meet its monthly purchasing targets. As a radical modification of the current distribution key seems unlikely, we think the ECB will be capable of being flexible again in the future, resorting to more substitute purchases (of supranational bonds) in jurisdictions facing a shortage of eligible sovereign bonds, and to fewer such purchases in countries with no scarcity issue.

Lastly, concerning the banks, M. Draghi esteems that the worries concern profitability and not solvency, insisting on the fact that solvency had been strengthened since 2009. As to Italian banks, M. Draghi said he was in favour of a public backstop under exceptional circumstances to avoid fire sale, while letting the decision up to the European Commission.



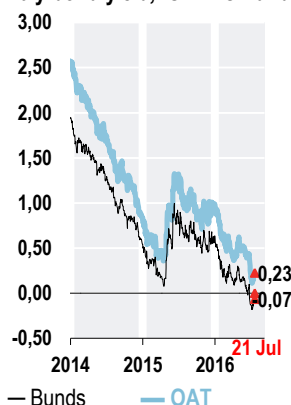
Markets overview

The essentials

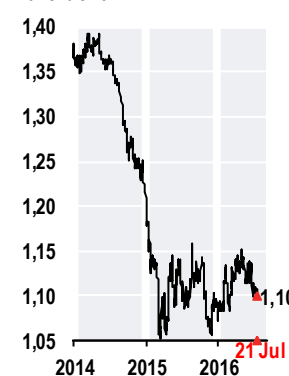
Week 15-7-16 > 21-7-16

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➤ Euribor 3M (%)	-0.29	➤ -0.30	-0.4 bp
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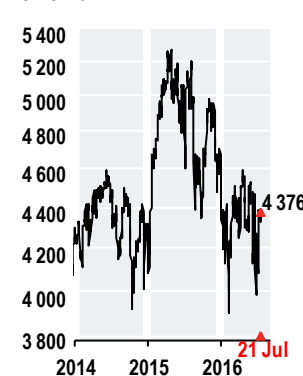
10 y bond yield, OAT vs Bund



Euro-dollar



CAC 40



Money & Bond Markets

Interest Rates		highest' 16		lowest' 16	
€ ECB	0.00	0.05 at 01/01	0.00 at 16/03		
Eonia	-0.34	-0.13 at 01/01	-0.36 at 26/05		
Euribor 3M	-0.30	-0.13 at 01/01	-0.30 at 20/07		
Euribor 12M	-0.05	0.06 at 01/01	-0.06 at 07/07		
\$ FED	0.50	0.50 at 01/01	0.50 at 01/01		
Libor 3M	0.70	0.70 at 20/07	0.61 at 04/01		
Libor 12M	1.34	1.34 at 20/07	1.12 at 12/02		
£ BoE	0.50	0.50 at 01/01	0.50 at 01/01		
Libor 3M	0.52	0.59 at 15/02	0.49 at 14/07		
Libor 12M	0.83	1.07 at 01/01	0.81 at 14/07		

At 21-7-16

Yield (%)		highest' 16		lowest' 16	
€ AVG 5-7y	0.01	0.49 at 12/01	-0.07 at 11/07		
Bund 2y	-0.64	-0.34 at 01/01	-0.70 at 11/07		
Bund 10y	-0.07	0.63 at 01/01	-0.18 at 08/07		
OAT 10y	0.23	0.98 at 01/01	0.11 at 08/07		
Corp. BBB	1.31	2.50 at 20/01	1.31 at 21/07		
\$ Treas. 2y	0.69	1.06 at 01/01	0.56 at 05/07		
Treas. 10y	1.56	2.27 at 01/01	1.36 at 08/07		
Corp. BBB	3.31	4.50 at 12/02	3.27 at 08/07		
£ Treas. 2y	0.17	0.65 at 01/01	0.12 at 13/07		
Treas. 10y	0.96	1.96 at 01/01	0.86 at 08/07		

At 21-7-16

10y bond yield & spreads

8.06%	Greece	812 pb
3.06%	Portugal	312 pb
1.24%	Italy	130 pb
1.12%	Spain	119 pb
0.51%	Ireland	57 pb
0.25%	Belgium	32 pb
0.23%	France	29 pb
0.21%	Austria	27 pb
0.13%	Finland	19 pb
0.11%	Netherlands	17 pb
-0.07%	Germany	

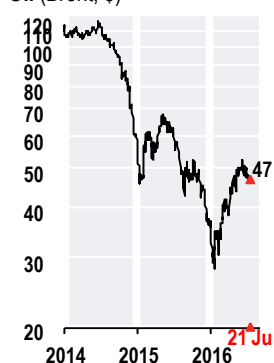
Commodities

Spot price in dollars		lowest' 16		2016(€)	
Oil, Brent	47	28 at 20/01	+29.4%		
Gold (ounce)	1 323	1 062 at 01/01	+23.0%		
Metals, LMEX	2 432	2 049 at 12/01	+9.0%		
Copper (ton)	4 967	4 328 at 15/01	+4.2%		
CRB Foods	350	329 at 11/01	+3.2%		
wheat (ton)	2	1 at 04/01	-1.5%		
Corn (ton)	1	1 at 06/07	-9.7%		

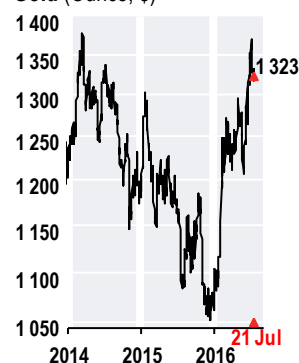
At 21-7-16

Variations

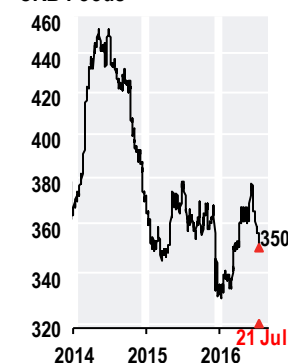
Oil (Brent, \$)



Gold (Ounce, \$)



CRB Foods



Exchange Rates

€ =		highest' 16		lowest' 16		2016	
USD	1.10	1.15 at 03/05	1.07 at 05/01	+1.2%			
GBP	0.83	0.86 at 06/07	0.73 at 05/01	+12.9%			
CHF	1.09	1.11 at 04/02	1.08 at 24/06	+0.0%			
JPY	116.95	131.84 at 01/02	110.95 at 08/07	-10.5%			
AUD	1.47	1.60 at 11/02	1.45 at 20/04	-1.8%			
CNY	7.34	7.49 at 08/06	6.99 at 05/01	+4.1%			
BRL	3.58	4.53 at 16/02	3.56 at 30/06	-16.7%			
RUB	70.36	91.22 at 11/02	69.76 at 19/07	-11.3%			
INR	73.91	77.50 at 11/02	71.42 at 05/01	+2.8%			

At 21-7-16

Variations

Equity indices

Index		highest' 16		lowest' 16		2016	2016(€)
CAC 40	4 376	4 637 at 01/01	3 897 at 11/02	-5.6%		-5.6%	
S&P500	2 165	2 173 at 20/07	1 829 at 11/02	+5.9%		+4.6%	
DAX	10 156	10 743 at 01/01	8 753 at 11/02	-5.5%		-5.5%	
Nikkei	16 810	19 034 at 01/01	14 952 at 24/06	-11.7%		-1.3%	
China*	58	59 at 01/01	48 at 12/02	-2.1%		-3.4%	
India*	475	481 at 14/07	393 at 11/02	+4.9%		+2.0%	
Brazil*	1 613	1 618 at 20/07	860 at 21/01	+28.0%		+53.8%	
Russia*	495	509 at 28/04	331 at 20/01	+10.1%		+20.9%	

At 21-7-16

Variations

* Indices MCSI



Economic forecasts

En %	GDP Growth			Inflation			Curr. account / GDP			Fiscal balances / GDP		
	2015	2016 e	2017 e	2015	2016 e	2017 e	2015	2016 e	2017 e	2015	2016 e	2017 e
Advanced	1.9	1.5	1.3	0.3	0.7	1.6						
United States	2.4	1.8	1.6	0.1	1.3	2.2	-2.6	-2.5	-2.9	-2.5	-3.1	-3.1
Japan	0.5	0.2	0.2	0.8	0.0	0.7	3.3	3.6	3.3	-4.6	-4.3	-4.2
United Kingdom	2.3	1.4	0.7	0.1	0.6	2.2	-5.2	-5.7	-4.5	-3.9	-3.2	-3.3
Euro Area	1.6	1.4	0.9	0.0	0.1	1.3	3.2	2.9	2.7	-2.1	-2.0	-1.8
Germany	1.4	1.4	1.1	0.1	0.2	1.6	8.6	8.4	7.8	0.7	0.2	0.2
France	1.2	1.4	1.0	0.1	0.2	1.1	-0.2	-0.1	-0.7	-3.5	-3.3	-3.0
Italy	0.6	0.9	0.3	0.1	-0.2	0.9	2.2	1.9	1.8	-2.6	-2.7	-2.5
Spain	3.2	2.7	1.5	-0.6	-0.7	1.3	1.4	1.2	1.1	-5.1	-4.0	-3.1
Emerging	4.1	4.3	4.9	6.1	6.4	5.5						
China	6.9	6.6	6.3	1.4	1.9	2.2	3.1	3.2	2.4	-2.4	-3.0	-3.2
India	7.3	7.8	8.4	4.9	5.6	5.0	-1.3	-0.9	-1.3	-4.1	-3.9	-3.5
Brazil	-3.8	-3.0	2.0	9.0	8.6	5.0	-3.3	-1.1	-1.6	-10.3	-8.7	-7.0
Russia	-3.7	-0.5	2.0	15.6	7.4	6.4	5.3	3.5	3.6	-3.7	-4.5	-3.8
World	3.1	3.1	3.3	3.6	4.0	3.8						

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

Financial forecasts

Interest rates		2015				2016						
End period		Q1	Q2	Q3	Q4	Q1	Q2	Q3e	Q4e	2015	2016e	2017e
US	Fed Funds	0.25	0.25	0.25	0.5	0.5	0.5	0.25-0.50	0.25-0.50	0.01	0.25-0.50	0.25-0.50
	3-month Libor \$	0.27	0.28	0.33	0.61	0.63	0.65	0.65	0.70	0.61	0.70	1.05
	10-year T-notes	1.93	2.35	2.03	2.27	1.79	1.49	1.55	1.60	2.27	1.60	1.75
EMU	Refinancing rate	0.05	0.05	0.05	0.05	0.00	0.00	0.00	0.00	0.05	0.00	0.00
	3-month Euribor	0.02	-0.01	-0.04	-0.13	-0.24	-0.29	-0.30	-0.30	-0.13	-0.30	-0.30
	10-year Bund	0.18	0.77	0.59	0.63	0.16	-0.13	0.00	-0.20	0.63	-0.20	-0.20
	10-year OAT	0.42	1.20	0.90	0.98	0.41	0.20	0.30	0.10	0.98	0.10	0.10
	10-year BTP	1.29	2.31	1.73	1.60	1.23	1.35	1.10	0.80	1.60	0.80	0.80
UK	Base rate	0.50	0.50	0.50	0.50	0.50	0.50	0.00	0.00	0.50	0.00	0.00
	3-month Libor £	0.57	0.58	0.58	0.59	0.59	0.56	0.75	0.75	0.59	0.75	1.25
	10-year Gilt	1.58	2.03	1.77	1.96	1.42	1.02	1.35	1.50	1.96	1.50	1.80
Japan	Overnight call rate	0.02	0.01	0.01	0.04	-0.00	-0.06	-0.30	-0.30	0.04	-0.30	-0.50
	3-month JPY Libor	0.17	0.17	0.17	0.17	0.10	0.06	-0.05	-0.10	0.17	-0.10	-0.25
	10-year JGB	0.40	0.44	0.35	0.25	-0.04	-0.23	-0.20	-0.20	0.25	-0.20	-0.30

Exchange rates		2015				2016						
End period		Q1	Q2	Q3	Q4	Q1	Q2	Q3e	Q4e	2015	2016e	2017e
USD	EUR / USD	1.07	1.11	1.12	1.09	1.14	1.11	1.10	1.10	1.09	1.10	1.05
	USD / JPY	120	122	120	120	112	103	108	110	120	110	124
EUR	EUR / GBP	0.72	0.71	0.74	0.74	0.79	0.83	0.82	0.80	0.74	0.80	0.68
	EUR / CHF	1.04	1.04	1.09	1.09	1.09	1.08	1.14	1.16	1.09	1.16	1.20
	EUR/JPY	129	136	134	131	128	114	119	121	131	121	130

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



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