



### ECONOMIC RESEARCH DEPARTMENT

## Summary

### Global

#### 2017: A critical year for the climate negotiations

In November 2016, the Paris agreement on climate change came into force and the countries even decided to accelerate the agenda for its implementation. However, the Trump presidency casts a shadow on further progress.

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### Eurozone

#### Characteristics of a healthier job market

The job market continues to recover, although it still has not offset the impact of the Great Recession.

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Also in :



## A weak euro for long

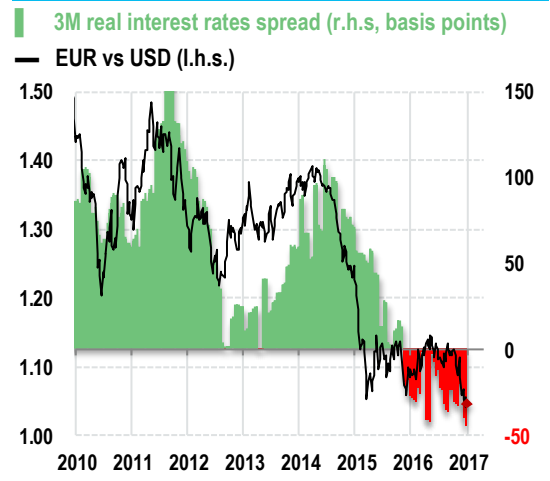
### ■ The euro is very low again vs. the dollar ■ A situation that is likely to persist

At around USD 1.05 on 5 January, the euro is trading at one of its lowest levels against the dollar in the past fifteen years. It is also very cheap regarding its purchasing power parity (USD 1.30), an advantage for European exporters that is bound to persist. This can almost entirely be attributed to the monetary policies of the US Federal Reserve (Fed) and the European Central Bank (ECB), which are completely out of phase.

Whereas the first has begun to raise key rates, the other is resolutely holding the cost of money below the zero lower bound. The Fed halted its quantitative easing programme – the modern version of printing money – in October 2014, while the ECB is pursuing QE at a monthly pace of EUR 80 billion (soon to be reduced to EUR 60 billion).

As a result, the already historical-wide yield gap, which largely governs the weakening of the single currency, continues to widen (see chart).

### EURO-DOLLAR EXCHANGE RATE VS YIELD GAP



Source: Thomson Datastream

### THE WEEK ON THE MARKETS

Week 30-12 16 > 5-1-17

↗ CAC 40	4 862	► 4 901	+0.8 %
↗ S&P 500	2 239	► 2 269	+1.3 %
↘ Volatility (VIX)	14.0	► 11.7	-2.4 %
↘ Euribor 3M (%)	-0.32	► -0.32	-0.2 bp
↗ Libor \$ 3M (%)	1.00	► 1.01	+0.7 bp
↗ OAT 10y (%)	0.69	► 0.82	+13.1 bp
↗ Bund 10y (%)	0.11	► 0.16	+5.4 bp
↘ US Tr. 10y (%)	2.45	► 2.37	-7.8 bp
↗ Euro vs dollar	1.05	► 1.06	+0.5 %
↗ Gold (ounce, \$)	1 157	► 1 184	+2.3 %
↘ Oil (Brent, \$)	56.7	► 56.2	-1.0 %

Source: Thomson Reuters

## Global

### 2017: A critical year for the climate negotiations

- CO<sub>2</sub> emission stagnated in 2015. However, more effort needs to get the world economy on a low carbon pace.
- The Paris agreement concluded at the COP21 in December 2015 came officially into force on 4 November
- The major advance at the COP22 in Marrakech was the acceleration of the agenda concerning the implementation of the Paris agreement.
- The Trump presidency might slow the transition towards a low-carbon economy, without derailing the process.

In the past decade, substantial progress has been made in reducing carbon emissions. In 2015, energy-related CO<sub>2</sub> emissions stalled at 32.1 billion tonnes for the second successive year, even though the world GDP grew by around 3% (chart 1). It provides further evidence of the weakening of the link between emissions and economic growth.

This development is due to three important trends. First, energy efficiency has increased as households and businesses have become more aware about the savings that can be made by isolation and other energy-saving innovations.

Second, the energy mix has become less carbon intensive, in particular in electricity production. Behind this development is the growing role of renewable energies. In 2015, investment in renewables excluding large hydro-electric projects increased by 5% to USD 285.9 billion exceeding the previous record of USD 278.5 billion achieved in 2011. Even more remarkable was the amount of generating capacity added, 134 GW, mainly in wind and solar PV. This amounted to 53.6% of the gigawatt capacity installed in 2015. For the first time, investment in renewables made up the majority of all newly installed electricity capacity. Nevertheless, the share of renewable capacity remains modest at only 16.2% of all installed capacity. Moreover, it only accounted for 10.3% of global electricity generation, preventing the emission of 1.5 Gt of CO<sub>2</sub> equivalent. In addition, specifically in the United States, the combination of hydraulic fracturing and horizontal drilling, is responsible for surging U.S. oil and natural gas production. The shale gas revolution is largely responsible for the decline in coal in the US power generation.

Third, the industrial structure has been changing, in particular in the advanced economies. Services have become more important to the detriment of the more energy-intensive manufacturing sector. Worldwide, total primary energy supply (TPES) per unit of GDP was 15% lower in 2014 than a decade earlier. In Europe, the decline was even 20%.

Despite the progress in recent years, there is still a long way to go. The International Energy Agency estimates that global energy demand will be 30% higher in 2040, as the declines in energy consumption in the advanced economies will be more than offset by consumption increases in the developing world. Even in this scenario,

#### CO<sub>2</sub> emissions from fossil fuel use and cement production (Gt CO<sub>2</sub>)

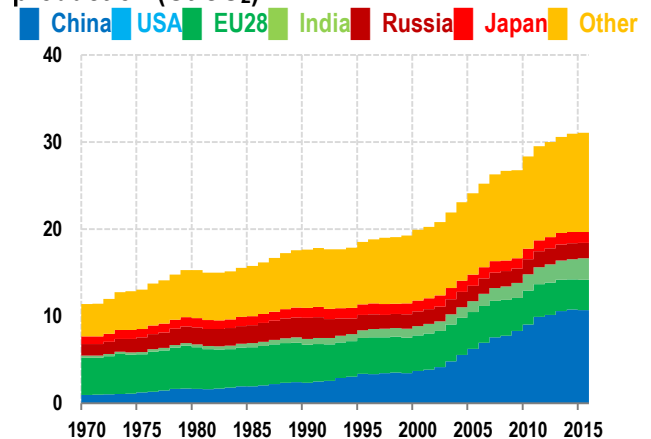


Chart 1

Source: PBL

hundreds of millions of people are still left without basic energy services. As carbon emissions are still closely linked to energy usage, global warming risks to exceed the 2°C from pre-industrial times, the ceiling target adopted at the 2015 Paris Agreement.

In the run-up to the Paris Climate Conference COP21, all participating countries filed their carbon reduction plans, the so-called Nationally Determined Contributions (NDCs). The sum of these pledges will not be sufficient to slow carbon emissions sufficiently in order to limit global warming to less than 2°C (Chart 2). A scenario consistent with a 50% chance of achieving this objective requires to limit the concentration of greenhouse gases in the atmosphere to 450 parts per million (ppm). It will require greenhouse gas emissions to be 40-70% below 2010 levels by 2050 and near or below zero by the end of the century. To achieve it, the NDCs will have to be tightened.

#### Limited progress at COP22

The Paris agreement concluded at the COP21 in December 2015 came officially into force on 4 November 2016, as more than 55 countries representing more than 55% of total global greenhouse gas emissions, had ratified it. It was a promising start for the climate conference COP22 held from 7 to 17 November in Marrakech. The agreement is now ratified by 120 countries.

The main objective of the COP22 was to put some force behind the pledges made in Paris. The Paris agreement only provided a framework for what has to be done to limit global warming to 1.5-2°C. The next step is to establish new procedures and mechanisms to achieve the objective, which is loosely called the Paris rulebook. These include rules on how countries will communicate their efforts with regards to adaptation, climate finance, transfer of technology, and human and institutional capacity building. For the moment, the

varying quality of information included in NDCs prevents a full assessment of the individual and collective efforts. In addition, as the NDC are not ambitious enough a mechanism is needed to upscale the national efforts. At the Marrakech summit, the agenda for getting this toolbox in place was advanced to 2018 instead of 2020 as was decided in Paris.

As the conference took place in Africa, the COP22 was expected to clarify the mechanisms to mobilise climate finance to help the developing countries in taking adaptation measures. The developed countries are confident to reach the USD 100 billion. According to an OECD analysis, pledges made in 2015 will boost public finance from an average USD 41 billion over 2013-14 to USD 67 billion by 2020. The Organisation estimates that the rest of the money can be found by mobilising private finance in an efficient way. These calculations are contested by the developing countries, which argue that only financial transfers for climate specific actions should be counted. On this basis, Oxfam estimates that net-climate specific assistance only amounted in 2013-14 on average to between USD 11 billion and USD 21 billion. Moreover, only 18% of these transfers go to the least developed countries. In the end, the developed countries only reaffirmed the USD 100 billion mobilisation goal without any further precision.

### 2017: A crucial year

The election of Donald Trump as the 45th US President cast a shadow over the deliberations at the COP22. During his election campaign, Mr. Trump had portrayed himself as a climate sceptic, promised to boost the fossil fuel industry and to roll back regulations. He even threatened to leave the Paris Agreement.

An immediate withdrawal of the Paris agreement is unlikely. The Treaty prescribes that a Party can leave only after four years. The only way to quite the Agreement immediately is to leave the UN Framework Convention on Climate Change (UNFCCC), which is a rather drastic step. The biggest threat for the Agreement is that the Trump administration will simply ignore the US pledges. The Paris deal might unravel if other major countries follow the US example.

Nevertheless, there is reason for optimism as the momentum for taking climate action remains strong at a global level. Even in the absence of regulations, companies have already been anticipating future legislations, for example by including carbon prices in their investment decisions.

This is partly due to the growing pressure from the financial sector on industries to reduce greenhouse gas emission. Investors are increasingly demanding climate related information to better assess their exposure to climate-related risks. To reduce the risk of stranded assets, they might engage with fossil fuel companies or even divest altogether from fossil fuels. Institutional investors are also under growing pressure from a wide range of stakeholders to pay attention to environmental issues. In addition to a good retirement income, pension fund members want their fund to pay attention to environmental, social and corporate governance issues. Moreover, media and campaign groups are trying to influence institutional investors. This also increases the reputational risks associated with the handling of climate issues.

### Global greenhouse gas emissions

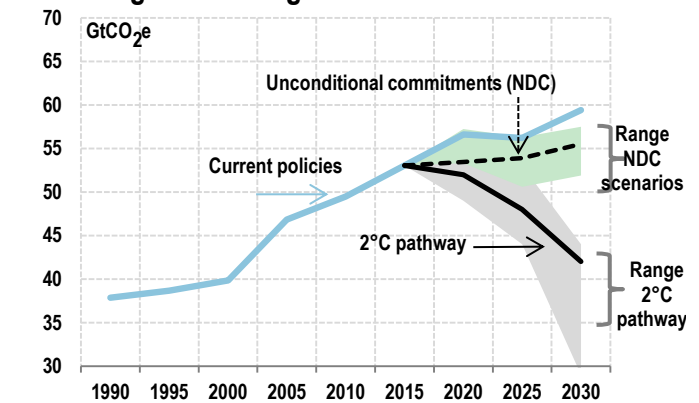


Chart 2

Sources: UNEP, PBL, BNP Paribas

Moreover renewables are becoming more competitive with regard to coal-and natural gas fired power generation, as installation prices are declining, in particular for solar PV. Renewables in the US continue to receive support at the state and federal level. Key federal tax credits for wind and solar were extended just 12 months ago, with substantial Republican support. These tax credits will remain in place until their phase out periods start in 2020. It is likely that investment projects might be brought forward ahead of the expiration of the tax credits. Finally, Mr Trump's promises to support the coal industry are likely to remain empty, as coal mining will continue to shrink for the simple reason that gas has become less expensive.

This year will be crucial for the international efforts to reduce carbon emissions. During this year, the countries that signed up to the Paris Agreement should start implementing their pledges. The COP23 organised by the Fiji Islands in Bonn in early November will be the last one before the crucial COP24 meeting. A lukewarm approach of the Trump administration on environmental issues might make it more difficult to agree internationally on further reductions in greenhouse gas emissions.

## Eurozone

### Characteristics of a healthier job market

- The job market continues to recover, although it still has not offset the impact of the Great Recession.
- The unemployment rate will continue to decline, albeit at a slightly slower pace in the months ahead. At the current pace, it would still take another three years to return to pre-crisis levels.
- About 4.5 million jobs were created in the eurozone over the past three years, which is close in volume to the job destructions reported during the crisis. Yet part-time employment has developed rapidly.

The eurozone job market continues to recover. Employment has picked up at a sufficiently rapid pace to lower unemployment, to varying degrees depending on the country. Even so, the impact of the Great Recession of 2008 has not been erased yet. Available data also highlights other striking trends since the crisis, notably the rapid rise of part-time employment.

#### The job market will continue to recover

In the eurozone, employment bottomed out again in mid-2013 and has been improving ever since (+0.7% in 2014, +1.1% in 2015). Granted, job creations have slowed recently, rising only 0.2% q/q in Q3 2016, the lowest quarterly rate since early 2015. On an annual basis, however, job growth is still rather vigorous (+1.2% y/y), in keeping with the pace of Q3 GDP growth (1.7% y/y). Moreover, data from the European Commission's survey on hiring intentions (as well as from the survey of purchasing managers) improved markedly in the second half of 2016 and are still looking upbeat in both industry and services.

Over the 3-year period, more than 4.5 million jobs were created in the eurozone according to ECB data. Although the volume of employment exceeds pre-crisis levels in France and of course in Germany as well, the same cannot be said for Italy. In Spain, the road ahead is still very long: employment is still more than 10% below the 2008 figure (see chart 1). In Q3 2016, eurozone employment was only 0.6% lower than at the beginning of the crisis in early 2008, and it will apparently break past this level in 2017. Yet the eurozone's labour force is also growing (at an average annual rate of 0.3% to 0.4% since 2010), which means that even if employment returns to the 2008 level, the unemployment rate would not fall to the pre-crisis figure. At 9.8% of the labour force in October, the unemployment rate in the eurozone is still 2.5 points above the early 2008 figure (7.3% in Q1). At the current pace of decline, the jobless rate is unlikely to return to pre-crisis levels for another three years, i.e. not before early 2020.

Yet this pace could slow somewhat in the future, under the double impact of a slowdown in job creations in 2017, assuming the expected economic slowdown is confirmed, and an upturn in the labour force, a trend that has accelerated somewhat since mid-2015

#### Employment

Q1 2008 =100, — EZ ; — GE, - - - FR, — IT, — SP, - - - others

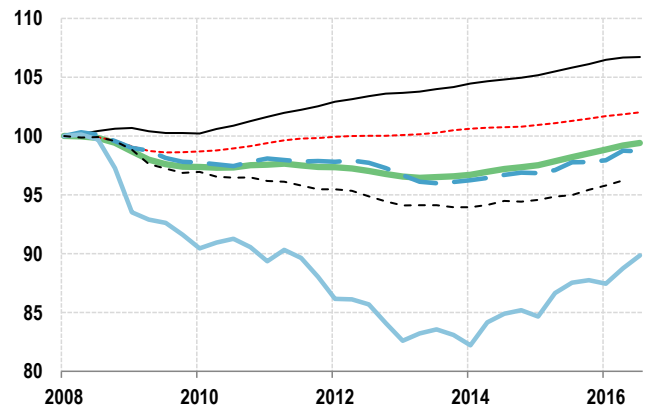


Chart 1

Sources: Eurostat, national sources, BNPP calculations

#### Unemployment

— Euro area harmonised unemployment rate; — Trend

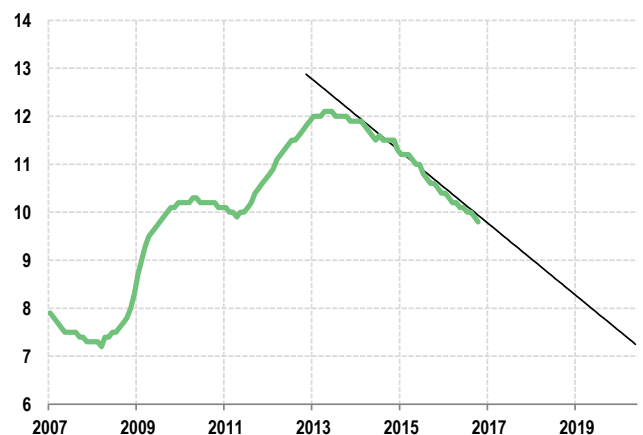


Chart 2

Sources: Eurostat, BNPP calculations

(to at least 0.7% in 2016). The increase in the labour force can be attributed to a combination of factors, albeit to varying degrees depending on the country: higher job market participation rates for women and especially for seniors; a structural trend that certain reforms may have intensified in some countries; the inflow of refugees, the overall impact of which is small, even though it could be significant in the most welcoming countries; and also the "natural" return to the work force of discouraged job seekers, in keeping with cyclical improvements.

#### Change in the structure of job creations

Although the upturn in employment might seem slow from the perspective of reducing unemployment, several studies show that the pace of job creations was relatively fast during the recovery, faster



than generally foreseen in forecasts, and faster than what could have been expected from GDP growth rates<sup>1</sup>. Thanks to several factors, job creations were more reactive to growth in recent years: wage moderation was stronger than in previous recovery phases; some countries conducted structural job market reforms that aimed to facilitate job creations, and others promoted public policies targeting job support measures.

More prosaically, the ECB<sup>1</sup> highlights the intensification of the deindustrialisation process in favour of services – which are traditionally more labour intensive than industrial activities – and the rapid development of part-time work in recent years.

Concerning part-time employment, chart 3 shows the trends in employment and the number of hours worked since 2008 (both per capita and total). During the recessions of 2008-2009, then 2011-2013, the total number of hours worked declined by about 7% from the Q1 2008 level, which is much sharper than the roughly 3.5% decline in employment. On a per capita basis, the number of hours worked also declined by about 3.5% over this period, a normal cyclical trend linked notably to the decline in overtime work and to partial unemployment measures introduced during the period. Since 2013, the average number of hours worked per capita has levelled off at a low level during the recovery phase: cyclical factors that could have boosted the number of hours worked were offset by the effects of a more structural decline in the number of hours worked per capita and the growing importance of part-time employment<sup>2</sup>. Among youth, this is a strong, long-standing and regular trend (chart 4). For middle aged and senior workers, in contrast, the crisis seems to have triggered an increase in part-time employment, whose share of total employment has now peaked at a new threshold. On the whole, the share of part-time work has increased by 3 percentage points since 2008, rising from 18.6% to 21.6% of employment in mid-2016.

■ Employment and number of hours worked

Q1 2008 = 100, — employment; — hours worked, - - - hours worked per worker

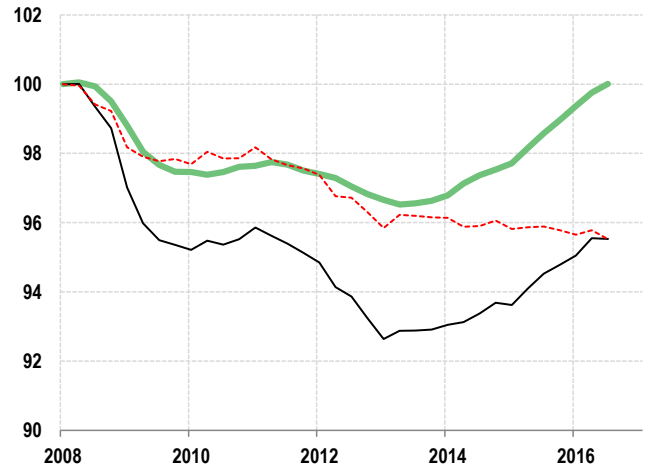


Chart 3

Source: ECB

■ Part-time work

% of total employment, by age:

- - - 15- 24 years, — 55-64 years; — 25-54 years

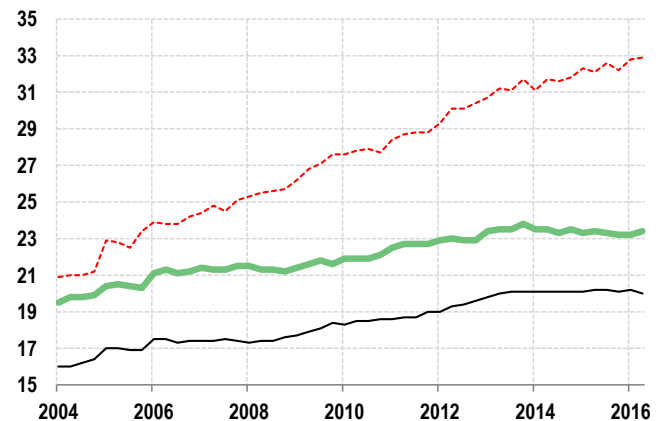


Chart 4

Source: Eurostat

<sup>1</sup> See “The employment-GDP relationship since the crisis”, ECB Economic Bulletin, June 2016 issue.

<sup>2</sup> As might be expected, the increase in part-time employment was strongest for service sector jobs.





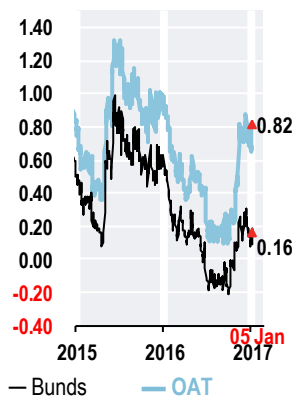
Markets overview

The essentials

Week 30-12 16 > 5-1-17

Table with 4 columns: Index, 30-12 16, 5-1-17, and % change. Includes CAC 40, S&P 500, Volatility (VIX), Euribor 3M, Libor \$ 3M, OAT 10y, Bund 10y, US Tr. 10y, Euro vs dollar, Gold, and Oil (Brent).

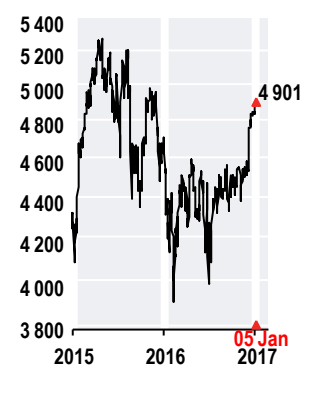
10 y bond yield, OAT vs Bund



Euro-dollar



CAC 40



Money & Bond Markets

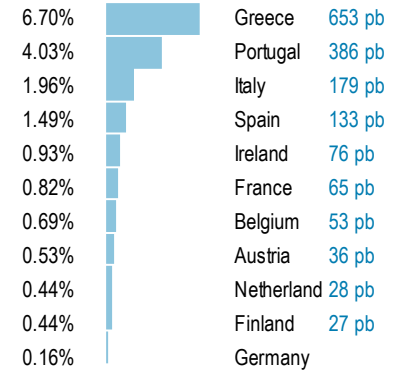
Table of Interest Rates with columns for currency, rate, highest '17, lowest '17, and date. Includes ECB, FED, and BoE rates.

At 5-1-17

Table of Yield (%) with columns for instrument, yield, highest '17, lowest '17, and date. Includes AVG 5-7y, Bund, OAT, and Treasury yields.

At 5-1-17

10y bond yield & spreads



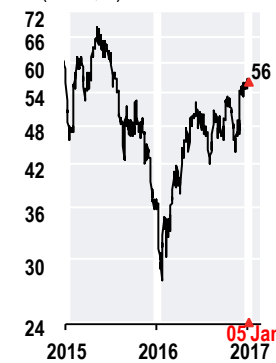
Commodities

Table of Spot price in dollars with columns for commodity, lowest '17, 2017(€), and % change. Includes Oil, Gold, Metals, Copper, CRB Foods, wheat, and Corn.

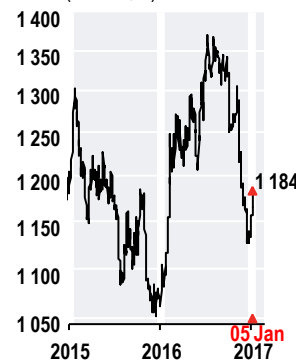
At 5-1-17

Variations

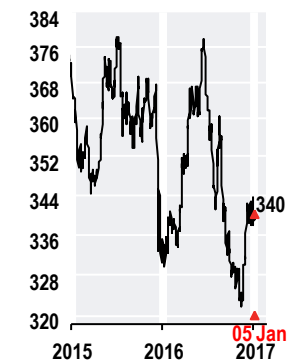
Oil (Brent, \$)



Gold (Ounce, \$)



CRB Foods



Exchange Rates

Table of Exchange Rates with columns for currency, highest '17, lowest '17, and 2017 % change. Includes USD, GBP, CHF, JPY, AUD, CNY, BRL, RUB, and INR.

At 5-1-17

Variations

Equity indices

Table of Equity Indices with columns for index, highest '17, lowest '17, and 2017 % change. Includes CAC 40, S&P500, DAX, Nikkei, and MSCI indices for China, India, Brazil, and Russia.

At 5-1-17

Variations

\* MSCI index





## Economic forecasts

En %	GDP Growth			Inflation			Curr. account / GDP			Fiscal balances / GDP		
	2016 e	2017 e	2018 e	2016 e	2017 e	2018 e	2016 e	2017 e	2018 e	2016 e	2017 e	2018 e
<b>Advanced</b>	1.6	1.7	2.1	0.8	1.7	1.9						
<b>United States</b>	1.5	2.2	2.8	1.2	2.2	2.6	-2.5	-2.4	-2.4	-3.4	-4.2	-5.0
Japan	0.8	0.9	0.7	-0.1	1.1	1.0	3.8	4.0	4.4	-4.6	-4.2	-4.1
United Kingdom	2.1	1.1	1.6	0.6	2.4	2.6	-5.5	-4.6	-3.5	-3.7	-4.0	-4.1
<b>Euro Area</b>	1.6	1.2	1.5	0.2	1.2	1.3	3.2	2.9	2.9	-1.8	-1.6	-1.4
Germany	1.8	1.5	1.8	0.4	1.6	1.5	8.9	8.1	8.4	0.6	0.6	0.5
France	1.3	1.1	1.5	0.3	1.0	1.1	-0.9	-0.6	-0.8	-3.4	-3.1	-2.8
Italy	0.8	0.4	0.7	-0.1	0.9	1.0	2.0	2.2	2.0	-2.5	-2.6	-2.6
Spain	3.2	2.1	1.9	-0.4	1.6	1.6	1.1	1.6	1.6	-4.6	-3.8	-3.2
Netherlands	2.2	1.5	1.4	0.1	0.8	1.2	8.5	8.2	7.9	-1.1	-0.5	-0.2
Belgium	1.4	1.2	1.4	1.8	1.6	1.6	0.8	0.6	0.6	-2.9	-1.6	-1.9
<b>Emerging</b>	4.3	4.6	5.1	4.8	4.4	4.2						
China	6.7	6.2	6.4	2.0	2.3	2.5	2.2	1.7	1.5	-3.0	-3.3	-3.5
India	7.5	8.1	8.3	5.0	5.7	4.9	-1.1	-0.5	-1.3	-3.9	-3.5	-3.5
Brazil	-3.7	1.0	3.0	8.8	4.9	4.4	-1.2	-1.7	-2.5	-9.6	-10.4	-8.4
Russia	-0.5	1.0	2.5	7.0	4.6	4.2	2.5	2.7	3.2	-3.9	-3.0	-1.9
<b>World</b>	3.1	3.3	3.8	3.1	3.3	3.3						

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

## Financial forecasts

Interest rates		2016				2017				2016e	2017e	2018e
		Q1	Q2	Q3	Q4e	Q1e	Q2e	Q3e	Q4e			
<b>US</b>	Fed Funds	0.25-0.5	0.25-0.5	0.25-0.5	0.50-0.75	0.50-0.75	0.50-0.75	0.75-1.00	1.00-1.25	0.50-0.75	1.00-1.25	2.00-2.25
	3-month Libor \$	0.63	0.65	0.85	0.91	0.90	0.90	0.95	1.10	0.91	1.10	2.45
	10-year T-notes	1.79	1.49	1.61	2.35	2.55	2.75	2.85	3.00	2.35	3.00	3.50
<b>EMU</b>	Refinancing rate	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00
	3-month Euribor	-0.24	-0.29	-0.30	-0.30	-0.30	-0.30	-0.30	-0.30	-0.30	-0.30	-0.15
	10-year Bund	0.16	-0.13	-0.19	0.30	0.40	0.50	0.60	0.70	0.30	0.70	1.20
	10-year OAT	0.41	0.20	0.12	0.75	0.90	0.90	1.00	1.10	0.75	1.10	1.70
	10-year BTP	1.23	1.35	1.19	2.05	1.90	2.10	2.30	2.50	2.05	2.50	3.00
<b>UK</b>	Base rate	0.50	0.50	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25
	3-month Libor £	0.59	0.56	0.38	0.40	0.40	0.40	0.40	0.40	0.40	0.40	0.40
	10-year Gilt	1.42	1.02	0.76	1.55	1.70	1.65	1.75	1.90	1.55	1.90	2.15
<b>Japan</b>	Overnight call rate	-0.00	-0.06	-0.06	-0.10	-0.10	-0.10	-0.10	-0.10	-0.10	-0.10	-0.10
	3-month JPY Libor	0.10	0.06	0.06	0.05	0.05	0.05	0.05	0.05	0.05	0.05	0.05
	10-year JGB	-0.04	-0.23	-0.08	0.00	0.05	0.05	0.10	0.15	0.00	0.15	0.15

Exchange rates		2016				2017				2016e	2017e	2018e
		Q1	Q2	Q3	Q4e	Q1e	Q2e	Q3e	Q4e			
<b>USD</b>	EUR / USD	1.14	1.11	1.12	1.07	1.04	1.02	1.02	1.00	1.07	1.00	1.09
	USD / JPY	112	103	101	110	115	120	125	128	110	128	135
<b>EUR</b>	EUR / GBP	0.79	0.83	0.87	0.86	0.84	0.82	0.82	0.80	0.86	0.80	0.76
	EUR / CHF	1.09	1.08	1.09	1.07	1.08	1.10	1.12	1.12	1.07	1.12	1.15
	EUR / JPY	128	114	114	118	120	122	128	128	118	128	147

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



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