

Economic Weekly: Views from Paris

ECONOMIC RESEARCH - Philippe WAECHTER – CHIEF ECONOMIST - +33 1 78 40 36 68 - philippe.waechter@am.natixis.com

Key element of the week starting February 9

The major point this week was on GDP growth in the Euro Area. GDP was up by 0.3% (1.4% at annual rate (AR)) for the last quarter of 2014. For the whole year, growth was 0.9% and carry-over for 2015 at the end of 2014 is 0.35%

There are four groups of countries plus Greece. The first one contains countries where the level of activity is above the pre-crisis level: Germany, Belgium, Austria and France. German growth was +0.7% in the 4th quarter (2.8% AR) and 1.6% in 2014. In France, GDP was up by 0.1% (0.3% AR) in the fourth quarter and 0.4% for 2014. In Belgium growth was +0.1% (0.4% AR) and +1% for 2014 and in Austria numbers were +0.1% (0.4% AR) and 0.3% for 2014.

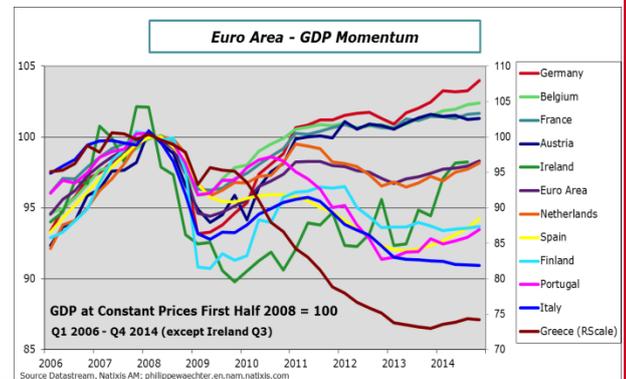
The Euro Area and Netherlands are in a catch-up zone, below the GDP pre-crisis level. In the Netherlands, GDP was up by 0.5% in the last quarter of 2014 (2% AR) and 0.8% for 2014.

In Spain and Portugal, the rebound is spectacular. GDP was up 0.7% (2.8%AR) and 0.5% (2% AR) respectively in the fourth quarter and 1.4% and 0.9% for 2014.

The Spanish GDP level is now above Finnish GDP regarding the pre-crisis level as a reference. Finland is in its third year of recession.

The fourth group is for Italy where GDP growth was 0% in the fourth quarter and -0.4% for 2014.

Greece is outside the classification as its GDP is down by more than 25% compared to the pre-crisis level. In the fourth quarter GDP was down by -0.2% (-0.8% AR) but for the whole year and for the first time since 2007 growth was positive at 1%



Other Important Issues

- The other important point is what has happened in Sweden where the Central Bank has pushed down its repo rate into negative territory at -0.1%. The Riksbank has explained its move by the long lasting deflation seen in Sweden. Beside this measure and to fight it the Bank has announced that it will purchase government bonds for SEK 10bn. In fact, Sweden as Denmark and Switzerland are constrained by the ECB strategy to keep its interest rates at the Zero Lower bound for an extended period. These countries must avoid an appreciation of their currency and must adopt a very accommodative monetary strategy
- Mark Carney the Bank of England Governor said that interest rates could converge to 0 as the inflation rate will turn negative in 2015. He is persuaded that the next move will be a liftoff but.... A negative inflation rate and weak core inflation can change landmarks.
- Retail sales were down by -0.8% in the USA in January. A lower gas price is an important explanation of this drop. Ex gasoline, retail sales change was 0%. Without auto sales and gas, core retail sales were up by 0.2%. It's low but not alarming.
- The Chinese inflation rate is trending downward to 0.8% in January from 1.5% in December. There is a role for lower energy prices but internal demand doesn't create pressures and that's worrisome
- The Japanese GDP was up by 0.6% (2.2% AR) in the fourth quarter. In 2014 GDP growth was null
- The industrial production index was stable in December for the Euro area and up by 1% (at AR) for the last quarter. In France, industrial production was up by 1.5% in December but down by -1.75% in Q4
- In Greece, the February 11 meeting was a failure as was the next meeting the 16, next Friday 20

What will happen this coming week?

- First surveys for February with the ZEW in Germany (Tuesday) and the flash estimate for the Markit survey in China, Japan, Euro Area, Germany, France and the USA (Friday)
- Inflation rate in France – It will drop in negative territory (Thursday)
- Inflation (Tuesday), employment (Wednesday), retail sales (Thursday) in the United Kingdom
- Industrial production and housing starts in the USA (Wednesday)

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Weekly Column

What did we learn last week?

Growth momentum was moderate in the last quarter of 2014 in the Euro Area – GDP was up by 0.3% (1.4% at annual rate).

With this growth number, the GDP level is back to its start of 2011 level. From the summer of 2011 to the first quarter of 2013 the Euro Area was in recession. Since then the GDP is creeping up, reducing the gap. In other words, the direct impact of austerity policies has been erased. It has been long and shows the lack of capacity to rebound for the Eurozone. That's why the new ECB policy based on demand is important.

In 2014 GDP growth was 0.9% after -0.45% in 2013. Carry-over for 2015 at the end of 2014 is 0.35%.

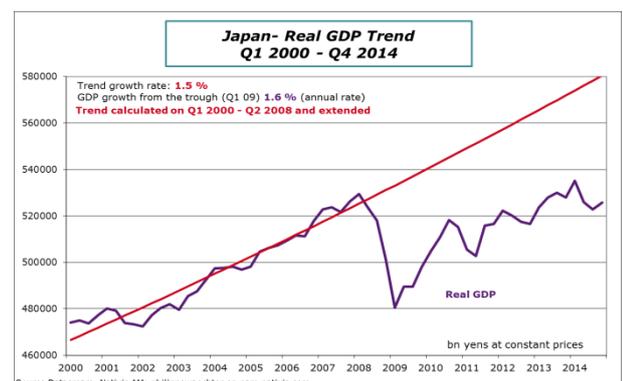
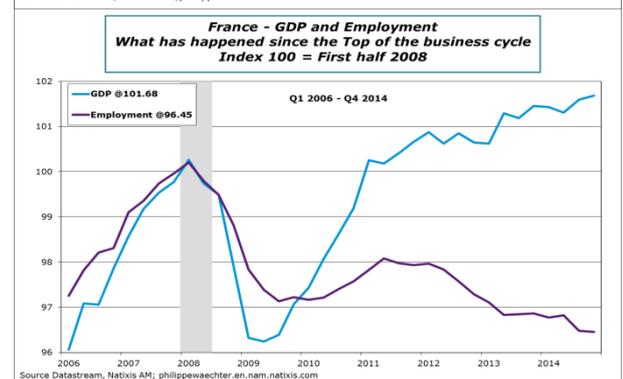
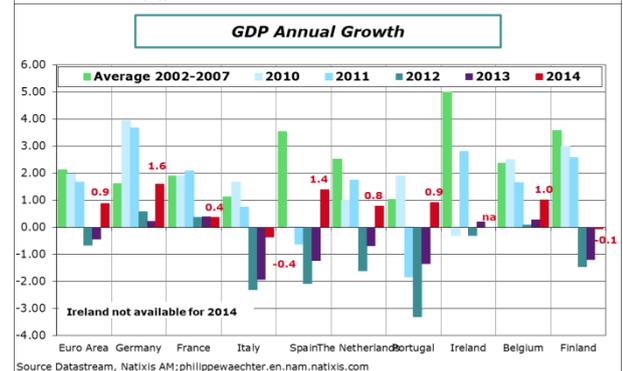
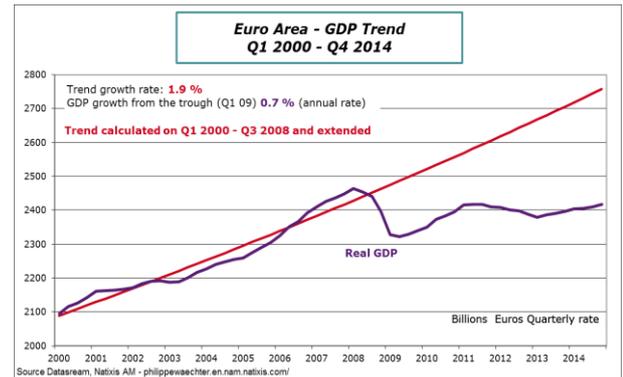
We do not have details on demand but we have the geographical detail. In the four main countries, the two most dynamic at the end of 2014 were Germany and Spain with a 0.7% growth (2.8% at AR). France GDP was up by just 0.1% and Italy was stable.

The economy of the Euro Area is still very heterogeneous but there are sources of change. That's how the **rebound in Spain and in Portugal** must be interpreted. There is a rapid improvement in these two countries even if they are still far from an equilibrium path. The unemployment rate is too high in these two countries to imagine being on a balanced growth path (the unemployment rate was in December 2014 at 23.7% in Spain and 13.4% in Portugal).

We notice that Finland which is very rigorous and serious about peripheral countries has ending its 3rd year of recession in 2014. Its GDP trajectory is now weaker than the Spanish one since the beginning of the crisis.

The most problematic issue is Italy. There were a lot of positive expectations since the arrival of Matteo Renzi as prime minister. Italy is in recession for the third consecutive year in 2014 and an improvement cannot be rapidly expected. That's one of most worrying country in Europe. Its **GDP level is back to 2000 level** and we do not see a U-Turn coming soon.

In France, GDP growth was +0.4% in 2014 as it was also in 2012 and in 2013. In fact since the first quarter of 2011 GDP growth is just at 0.4% at annual rate. This is not compatible with higher employment. That's one main weakness of the current government economic policy. Details for the 4th quarter (+0.1% and 0.3% at AR) show a rebound in exports but consumption was up but at a slower pace and investment was contracting again (companies investment was negative and residential investment was down rapidly). **Domestic demand and external demand have positive but modest contributions to growth. At the same time, inventories had a negative contribution.** I expect a recovery in 2015 but figures from the end of 2014

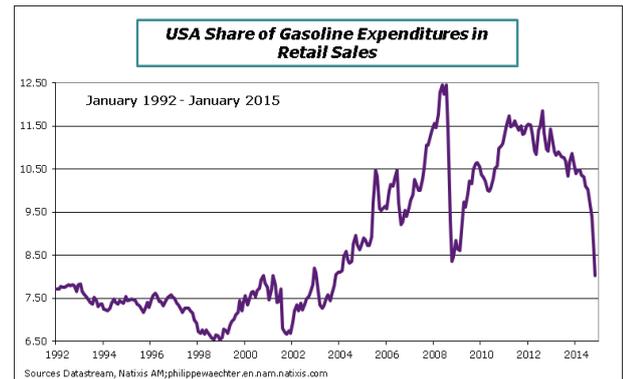


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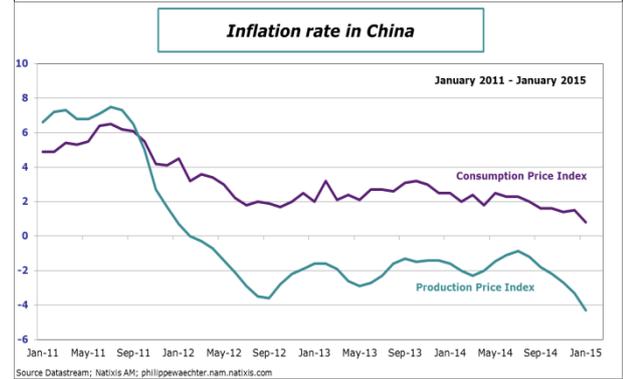
do not give information for a break in the current French economic dynamics. I expect that the demand based monetary policy and the low oil price will boost internal demand creating the conditions for a 1% GDP growth in 2015.

Growth in Japan was up by 0.6% (2.2% at AR). This improvement was mainly driven by net exports. Households' expenditures are up again but at a slow pace. For the whole year growth was at 0 and the carry-over for 2015 at the end of 2014 is negative by -0.35%.

In the USA, retail sales were down during the last two months (December and January). But ex gasoline the number was null in January. The impact of the lower oil price is important for households. The arbitrage between gas expenditures and the rest is about 3% of the total retail sales figure for the last twelve months. In other words, the lower oil price has reduced gas expenditures by more than USD 10bn from January 2014 to January 2015. It a rapid improvement in their purchasing power and it will be as in Europe a strong support for 2015.



In China inflation is still trending downward. The inflation rate was just 0.8% in January and the production price index was down to -4.3%. This is a real constraint for indebted companies as now real interest rate is above 9%. That's why the Central Bank of China will have to become more accommodative. It has already started at the end of last year on interest rates but also in January with lower rates of reserves. But it will have to continue. The internal demand is not strong enough to create a strong support for growth and to fight the risk of deflation. It's still risky ahead.



In Greece, the last two meetings have failed to find an agreement between Greece and the other 18 members of the Eurogroup. The discussion is between an extension of the current program proposed by the Eurogroup and a bridge loan expected by the Greek government ahead of a new deal.

The non-official press release from Monday's meeting shows that there was no convergence between the positions. The next meeting will be on Friday.

There are two questions:

1 - Who wants to take the risk of a Grexit? We cannot minimize the risk of this type of event as it would create a loss of confidence in the Euro construction. Can it be a Lehman point?

2 - The negotiation seems to continue until the point of non-return. The Greek government must show that it has gone to the maximum to continue to have support from Greek people and from the left of the party. For Eurogroup members, the difficulty will be to convince their own parliament to vote a new deal with Greece. It could be a concern in Germany, Finland but also in some peripheral countries (Portugal). They must show that they have gone as far as they could but didn't want to take the risk on the Euro construction.

The negotiation continues

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EQUITY MARKETS FEBRUARY 13, 2015

	Level		On a year (close)		Change in local currency			Change in Euro		
	12/31/14	02/13/15	Min	Max	1 Y	YTD	1w	1 y	YTD	1 w
CAC 40	4272.75	4759.36	3918.62	4759.36	10.35	11.39	1.46			
DAX	9805.55	10963.40	8571.95	10963.40	14.24	11.81	1.08			
EuroStoxx	3146.43	3447.59	2874.65	3447.59	11.29	9.57	1.46			
FTSE	6566.09	6873.52	6182.72	6878.49	3.22	4.68	0.29	14.47	9.68	0.62
SNP 500	2058.90	2096.99	1815.69	2096.99	14.60	1.85	2.02	37.35	8.09	1.51
Nasdaq	4736.05	4893.84	3999.73	4893.84	15.40	3.33	3.15	38.31	9.66	2.63
Nikkei 225	17450.77	17913.36	13910.16	17979.72	23.25	2.65	1.50	27.16	10.06	1.28
MSCI Emerging	956.31	986.65	909.98	1100.98	4.32	3.17	0.83	25.03	9.49	0.32
MSCI World USD	1709.67	1752.18	1592.60	1764.12	6.63	2.49	1.84	27.80	8.76	1.33

INTEREST RATES – FEBRUARY 13, 2015

	Interest Rates – February 13, 2015							Interest Rates December 31, 2014			
	Level				Weekly Change			Central Bank	3 month	2 Year	10 Year
	Central Bank	3 month*	2 Year	10 Year	3 month	2 Year	10 Year				
USA	0 - 0.25	0.258	0.66	2.02	0.00	0.01	0.07	0 - 0.25	0.26	0.67	2.17
Zone Euro	0.05	0.048	-0.21	0.295	-0.01	-0.02	-0.05	0.05	0.08	-0.07	0.54
UK	0.5	0.53	0.489	1.661	0.00	-0.10	0.02	0.5	0.53	0.51	1.76
Japan	0.1	0.173	0.048	0.418	0.00	0.01	0.08	0.1	0.18	-0.03	0.33
SPREADS		3 month* (02/13/15)	2 year (02/13/15)	10 year (02/13/15)	3 month (12/31/14)	2 year (12/31/14)	10 year (12/31/14)				
USA – Euro Area		0.20 (0.20) [§]	0.83 (0.64) [§]	1.62 (1.41) [§]	-0.04	0.19	1.1				
UK – Euro Area		0.48 (0.48) [§]	0.77 (0.58) [§]	1.21 (1.09) [§]	0.24	0.37	1.09				

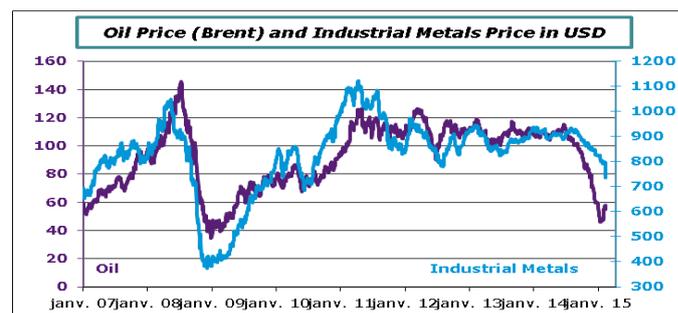
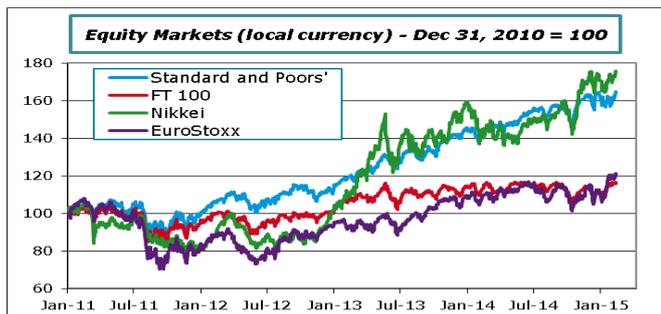
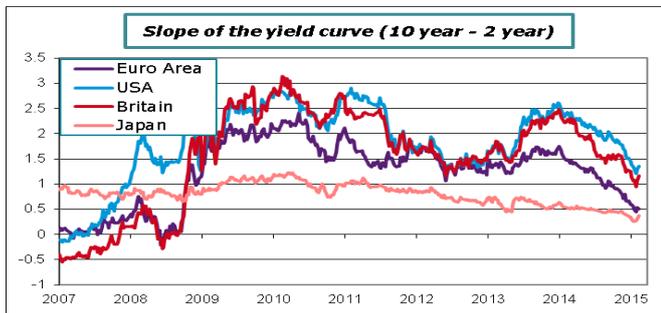
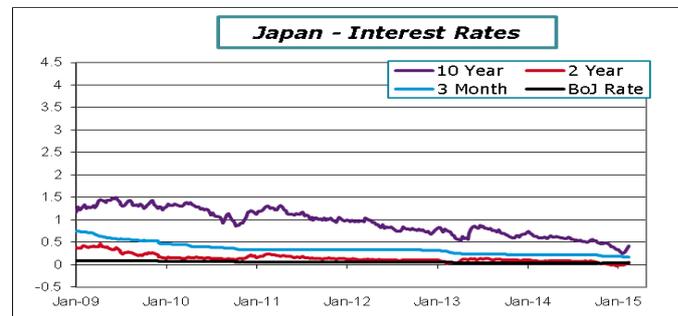
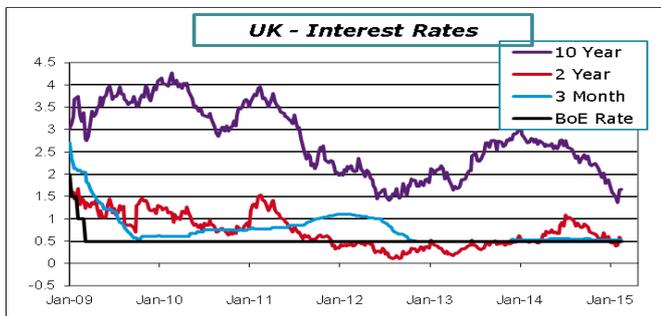
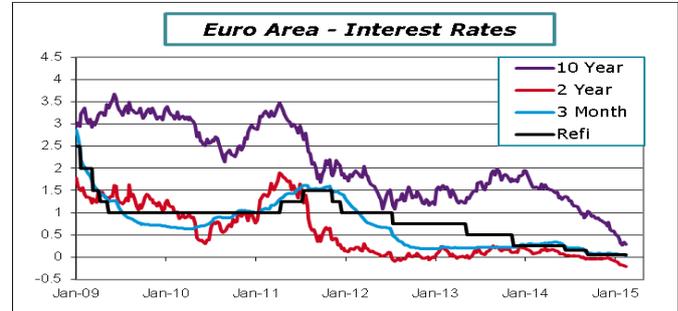
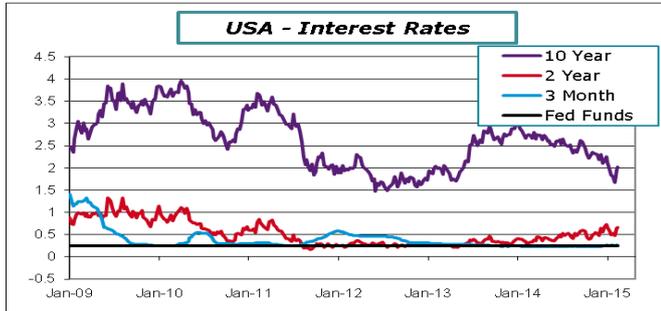
* 3 month interbank rate, [§] previous week

FOREX – GOLD – OIL MARKET – FEBRUARY 13, 2015

	Level		Change			
	12/31/2014	02/13/15	1 week	YTD	1 year	
Euro – Dollar (var. + higher euro)	1.210	1.140	0.51	-5.77	-16.56	
Euro – Yen (var. + higher euro)	145.079	135.319	0.22	-6.73	-3.08	
Euro – Sterling (var. + higher euro)	0.779	0.740	-0.96	-4.98	-9.91	
Dollar – Yen (var. + higher dollar)	120.550	119.030	1.30	-1.26	16.16	
Dollar – Sterling (var. + higher sterling)	1.559	1.539	0.83	-1.27	-7.47	
Dollar – Yuan (var. + higher dollar)	6.206	6.240	-0.06	0.55	2.91	
Oil Price (Brent)	Dollar	55.84	57.18	-0.35	2.40	-47.33
	Euro	46.15	50.15	-0.85	8.67	-36.87
Gold Price (Ounce)	Dollar	1186.33	1232.54	-0.09	3.90	-5.00
	Euro	980.39	1080.95	-0.59	10.26	13.86

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Financial Markets – February 13, 2015



Sources DataStream; Natixis AM; philippewaechter.nam.natixis.com

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Registered Office: 21 quai d'Austerlitz – 75634 Paris Cedex 13 - Tel. +33 1 78 40 80 00

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