Economic Weekly: Views from Paris

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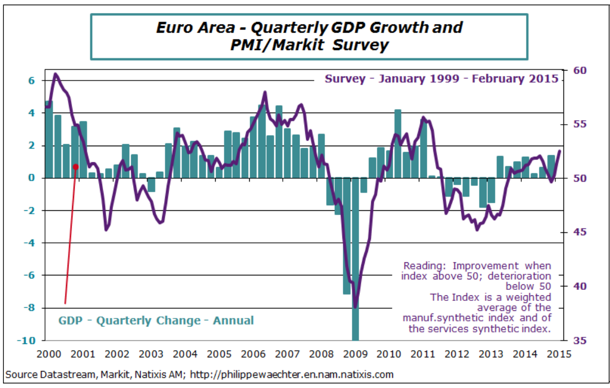
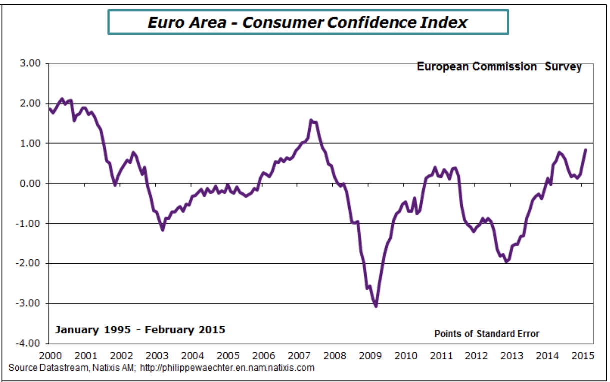
Key element of the week starting February 16

In February, in the Euro Area, companies and households have sent a positive message on their expectations. Confidence indices were up for both. The PMI/Markit index is at its highest level since June 2011 and the European Commission Consumer Confidence index has never been so high since September 2007. Two points to be noticed: constraints are not binding as strongly as they did. This is related to lower euro, lower rates and lower oil price in the Euro Area. Every economic agent has more capacity to adapt to its environment and to make arbitrage. The other issue is that uncertainty on Greece and anxiety linked to Ukraine haven't had impact on companies and households' behavior.
The PMI/Markit index has a profile which is consistent with GDP quarterly growth and the consumer confidence index is well correlated with consumption momentum. Both indicators will be supportive for stronger growth. In other words, these two types of signal suggest that the economic situation is changing on the upside in the Euro Area.
The ZEW survey for February in Germany gave the same signal. The combination of all these indicators may show the real start of the Eurozone economic expansion.





Other Important Issues

- The agreement last Friday on Greece is just a way to postpone the deadline that was fixed on February 28. Greece may have 4 months to find a new deal if the arguments presented to the Eurogroup on Tuesday 24 are convincing (phone agreement by the Eurogroup expected tomorrow). But the bailout conditions have not been removed. The situation is still tight.
- In the USA, the industrial production index has followed a slower trend during the last couple of months (+0.06% in December and +0.18% in January). The PMI/Markit index was slightly higher (54.3) but the new orders index is stable at 54.7 and the new exports orders index is showing a slower momentum. This can probably linked to the dollar strength.
- The Federal Reserve doesn't want to hurry to lift-off its interest rates (Fed's minutes)
- Since last week and referring to the meeting that was held on January 22, the ECB now publish minutes of its council. It will be interesting to follow the evolution of the balance of strength between meeting's members.
- The inflation rate in France was -0.4% in January – Close to deflation as the contribution of the index ex energy was just 0.2%. It's clearly not enough.
- Strong recovery in Japanese exports in December and January. Positive on economic growth
- Stronger CBI survey in the UK in February – Higher real wage rate due in large part by a drop to 0.3% of the inflation rate: good for purchasing power – Trend in retail sales remains good

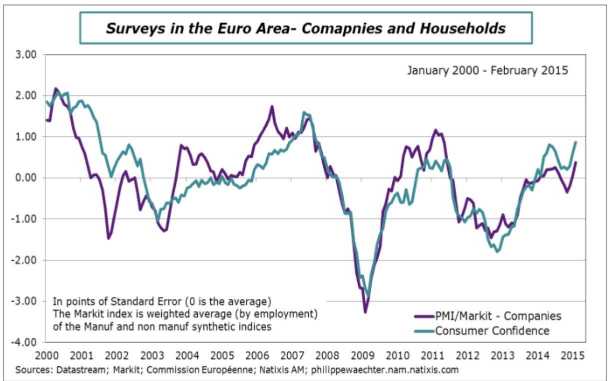
What will happen this coming week?

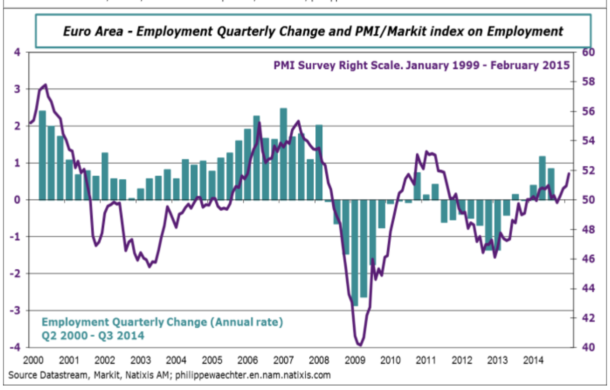
- The main point this week will be Janet Yellen testimony at the Congress. It will be on Tuesday 24 (and repeated on 25). We expect insights on the Fed's monetary policy during the Q&A session.
- Surveys in the Euro Area with IFO (Monday in Germany), INSEE (Tuesday in France) and Istat (Thursday in Italy) to have a clearer view on the short term outlook
- Inflation in the US (Thursday) and details in the Euro Area (Tuesday)
- In France, consumer confidence & unemployment (Wednesday), consumers' expenditures (Friday)

Weekly Column

What did we learn last week?

The first point to be mentioned is the surveys' improvement seen in February. Companies and households are now more optimistic.
The PMI/Markit index is at its highest since June 2011 and the Consumer Confidence index is back to September 2007 level for the first time.





Companies and households take advantage of the drop of the euro exchange rate, of the low interest rates and of the sharp reduction in oil price. These changes improve their purchasing power and their margin and give to each of them the capacity to adapt to a new environment.
The ECB strategy to favor a demand driven monetary policy makes sense and is supportive for economic growth. The change in expectations that will accompany the quantitative easing operation could improve again this momentum.
In the Markit survey, the main point to notice is the rapid improvement of the labor market index. As this index is consistent with quarterly employment change, this can lead to a stronger labor market dynamics. Households' uncertainty will then be reduced. **A convergence to a more virtuous cycle can be expected and let imagine stronger growth prospects in 2016 and 2017.**
These surveys do not take into account risks associated with Greece. The ZEW survey in Germany was up in February with a strong improvement in the current condition index. It looks like a situation where the menace of a Grexit was not credible?

The second point is the agreement on Greece between the Greek government and the Eurogroup. The deadline which was fixed on February 28 has been postponed for 4 months. But the situation is still complicated for Greece. Its bailout commitments are still binding and the Greek government must follow this line. Today (Tuesday) the Greek government will present measures that will be discussed, after an agreement by the Eurogroup, in the coming 4 months for a new deal.
The Greek government may have some degrees of freedom in the management of the primary budget surplus (budget balance less interest paid on public debt) but this will have to be negotiated.

The question was to know who has won with this agreement. My guess is that I expect that Europe has not lost too much
In other words, Greece has had a 4 month delay but has to follow the bailout convention and will have to negotiate a new deal. The postponement of the deadline was necessary to avoid a Grexit and its negative consequences on the Euro Area but all has to be done now to maintain the Hellenic Republic in the Eurozone.

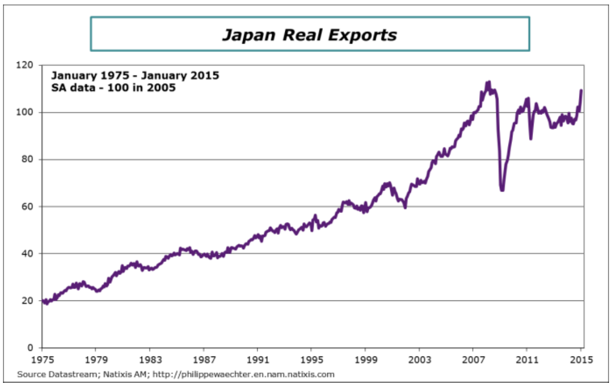
In the USA, there is probably a kind of soft spot; Data in December and January have less momentum, less strength than data published in October and November. This could be seen on industrial production, on retail sales last week and on Fed's survey this week for February (Empire state Survey, PhylliFed survey). There was also no acceleration in the NAHB survey on Homebuilder confidence. The global momentum is still robust but the question is to know if the peak cycle hasn't been touch already?

In this environment which is also characterized by low inflation expectations and still some important imbalances on the labor market the question is on the Fed's behavior. **Is it necessary for the US central bank to change its interest rates strategy rapidly? The Fed's minutes published last week do not**

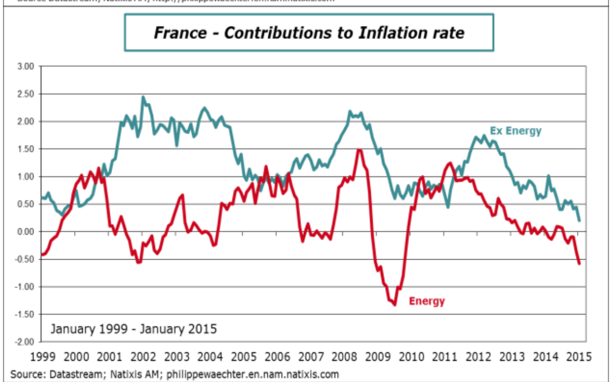
suggest a rapid lift-off. The US central bank is aware that acting too late is probably more efficient that acting too early. Janet Yellen's testimony at the Congress on Tuesday 24 will bring a lot of information.
Is it necessary to hike interest rates when a higher dollar can do the job? Since last July, the dollar effective exchange rate appreciates a lot and this is a constraint on the economic activity. Is it necessary to go beyond this point?

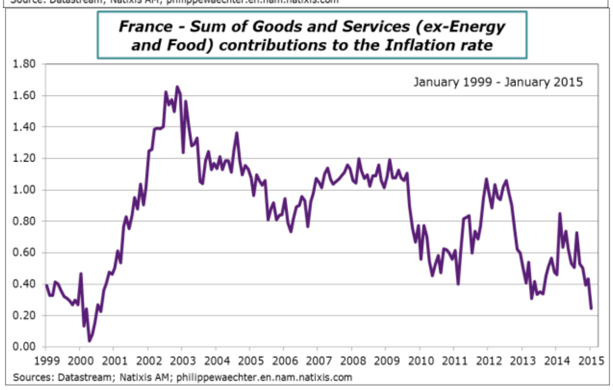
The ECB has published for the first time the minutes of its last monetary policy committee. This meeting was important because it decided on QE. But what will be interesting here will be the evolution of the balance of strength between committee members.

In Japan, exports have had a real stronger momentum during the last couple of months. December and January figures show a break in trend. That's good news for the Japanese economy as there are still fragilities on the internal market. It's like in the Euro Area, an impulse from outside is important to improve the short term dynamics. May be is it the first step of the currency depreciation?



In France, the inflation rate was down to -0.4% in January. On a month to month basis, the consumer price index dropped by 1%.
This monthly change is mainly due to January sales (there are sales in France in January and July). The inflation rate is negative and reflects a negative contribution from the energy sector for -0.6%. The ex-energy index had a contribution of only +0.2%. It's weak reflecting the absence of pressures within the French economy.
The situation is worrisome as core goods and core services do not have a strong contribution. When added the two contributions are at 0.25% which is the lowest contribution since August 2000. We see on the chart that this indicator is sliding rapidly. If we want to talk about deflation, that's the indicator to watch.
In February the inflation rate will be lower. In January 2014 there was a VAT rate increase but the impact was mainly seen in February. So the base effect will be important in February 2015. Moreover, there is still room for a downside adjustment on the energy contribution.





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EQUITY MARKETS FEBRUARY 20, 2015										
	Level		On a year (close)		Change in local currency			Change in Euro		
	12/31/14	02/20/15	Min	Max	1 Y	YTD	1w	1 y	YTD	1 w
CAC 40	4272.75	4830.90	3918.62	4833.28	10.92	13.06	1.50			
DAX	9805.55	11050.64	8571.95	11050.64	14.89	12.70	0.80			
EuroStoxx	3146.43	3490.53	2874.65	3490.53	11.82	10.94	1.25			
FTSE	6566.09	6915.20	6182.72	6915.20	1.50	5.32	0.61	12.96	10.51	0.76
SNP 500	2058.90	2110.30	1815.69	2110.30	14.70	2.50	0.63	38.35	9.10	0.94
Nasdaq	4736.05	4955.97	3999.73	4955.97	16.13	4.64	1.27	40.08	11.38	1.57
Nikkei 225	17450.77	18332.30	13910.16	18332.30	26.87	5.05	2.34	31.84	12.89	2.57
MSCI Emerging	956.31	984.42	909.98	1100.98	3.56	2.94	-0.23	24.91	9.57	0.07
MSCI World USD	1709.67	1768.09	1592.60	1768.09	6.77	3.42	0.91	28.78	10.08	1.21

INTEREST RATES – FEBRUARY 20, 2015											
	Interest Rates – February 20, 2015							Interest Rates December 31, 2014			
	Level				Weekly Change						
	Central Bank	3 month*	2 Year	10 Year	3 month	2 Year	10 Year	Central Bank	3 month	2 Year	10 Year
USA	0 - 0.25	0.262	0.67	2.11	0.00	0.01	0.09	0 - 0.25	0.26	0.67	2.17
Zone Euro	0.05	0.048	-0.202	0.347	0.00	0.00	0.04	0.05	0.08	-0.07	0.54
UK	0.5	0.53	0.525	1.828	0.00	0.04	0.15	0.5	0.53	0.51	1.76
Japan	0.1	0.173	0.033	0.389	0.00	-0.02	-0.03	0.1	0.18	-0.03	0.33

SPREADS	3 month* (02/20/15)	2 year (02/20/15)	10 year (02/20/15)	3 month (12/31/14)	2 year (12/31/14)	10 year (12/31/14)
USA – Euro Area	0.21 (0.21) §	0. 87 (0.87) §	1.76 (1.71) §	-0.04	0.19	1.1
UK – Euro Area	0.48 (0.48) §	0.73 (0.69) §	1.48 (1.37) §	0.24	0.37	1.09

* 3 month interbank rate, § previous week

FOREX – GOLD – OIL MARKET – FEBRUARY 20, 2015						
		Level		Change		
		12/31/2014	02/20/15	1 week	YTD	1 year
Euro – Dollar (var. + higher euro)		1.210	1.137	-0.30	-6.05	-17.09
Euro – Yen (var. + higher euro)		145.079	135.012	-0.23	-6.94	-3.77
Euro – Sterling (var. + higher euro)		0.779	0.735	-0.72	-5.66	-10.61
Dollar – Yen (var. + higher dollar)		120.550	119.100	0.06	-1.20	16.46
Dollar – Sterling (var. + higher sterling)		1.559	1.537	-0.15	-1.42	-7.73
Dollar – Yuan (var. + higher dollar)		6.206	6.255	0.24	0.79	2.82
Oil Price (Brent)	Dollar	55.84	58.62	-3.38	4.98	-46.90
	Euro	46.15	51.56	-3.09	11.74	-35.95
Gold Price (Ounce)	Dollar	1186.33	1206.68	-2.10	1.72	-8.26
	Euro	980.39	1061.43	-1.81	8.27	10.66

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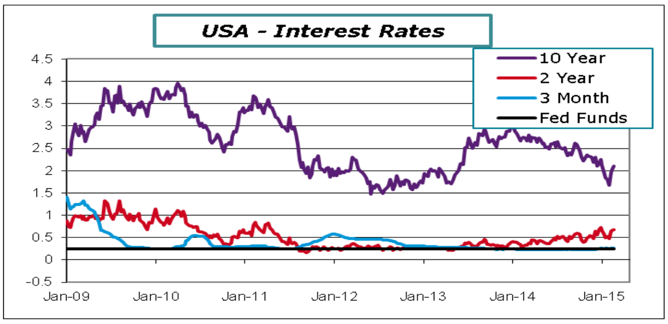
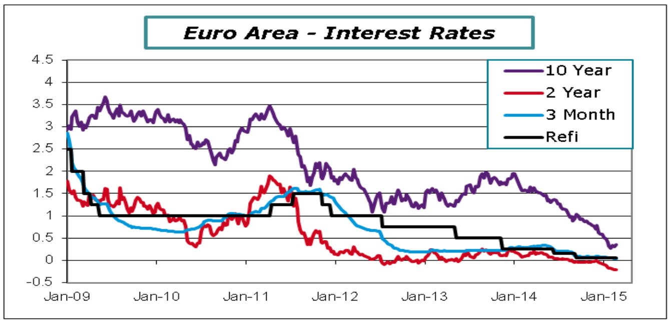
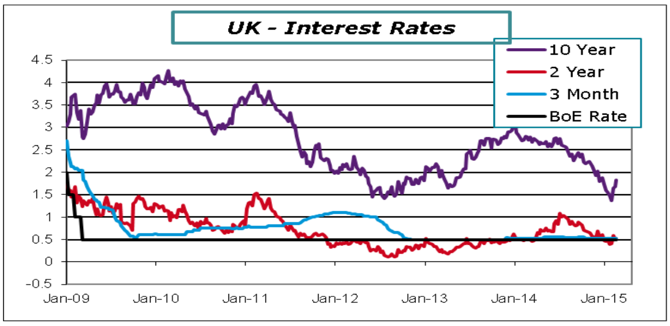
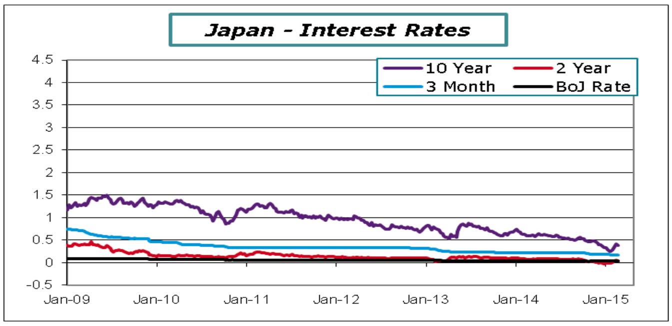
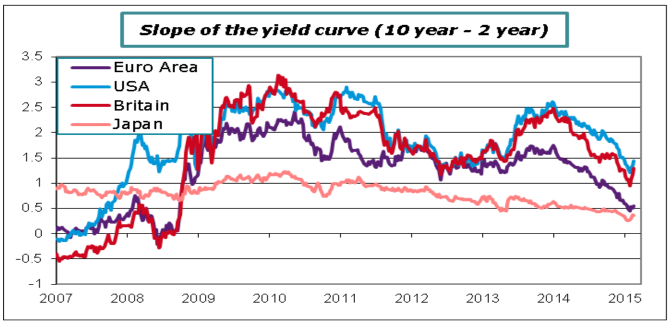
Financial Markets – February 20, 2015

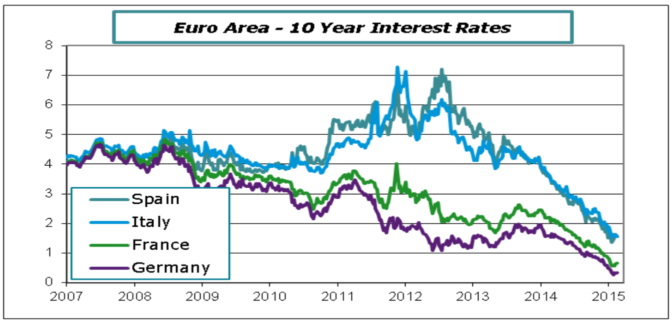


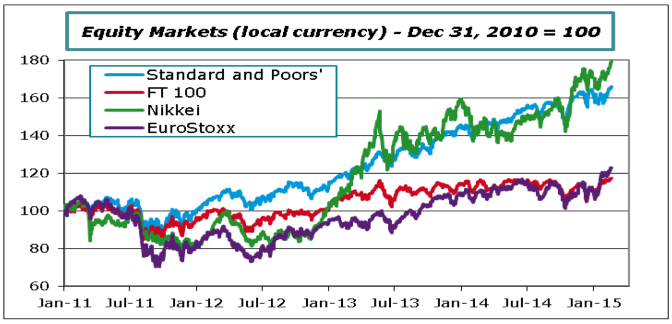


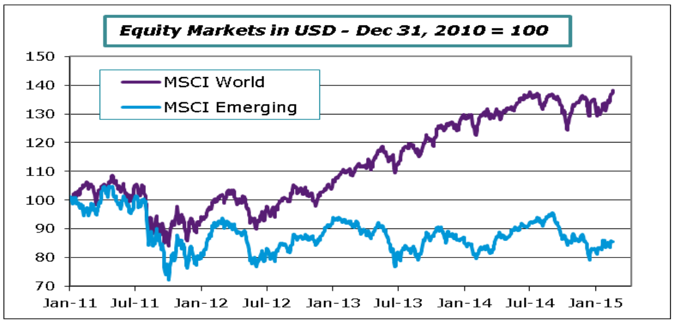


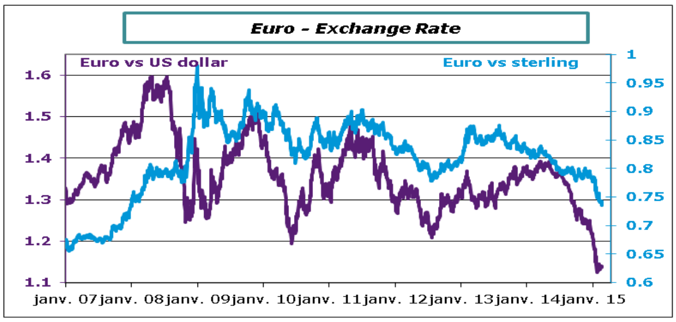


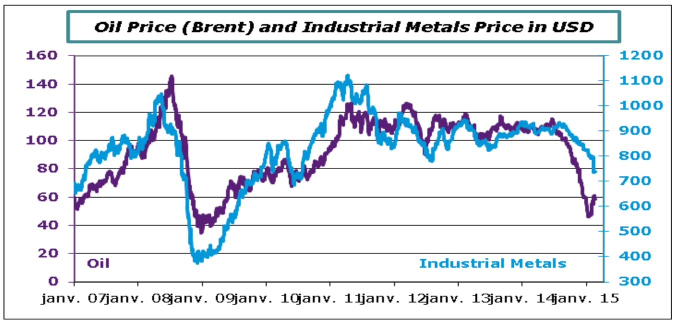












Sources DataStream; Natixis AM; philippewaechter.nam.natixis.com

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