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SCENARIOECO

Economic and Sectoral Research Department

NOW, INVESTMENT HOLDS THE KEY

- Global activity remains strong. Sentiment indicators point to continued expansion in 2018 and firm manufacturing activity supported by a pickup in investment. In the US, a large fiscal impulse will extend the business cycle.
- With key markets approaching full employment, GDP growth may be constrained by supply-side constraints, giving rise to some inflationary pressures.
- Global stock markets sold off sharply in February after a long bull market, on inflation fears but the correction proved short lived with no credit spread widening. Trade tensions catalysed a new volatility spike in March. Albeit very gradual, monetary policy normalisation and the absence of further acceleration in global growth is likely to entail somewhat higher volatility in 2018 than in 2017.
- Trade tensions morphing into a full-blown trade war ranks top of the list of downside risks. A sharp shock to bond yields and political risks also remain on our radar.

SOCIETE GENERALE

Table of contents

Document completed on 29 March 2018

Outlook Summary

GLOBAL ECONOMY

- Global activity remains strong albeit probably close to the peak level. Sentiment indicators point to continued expansion in 2018 and firm manufacturing activity ahead in the advanced economies, supported by a pickup in investment. Robust international trade flows are also behind a self-reinforcing growth momentum. Global GDP growth is expected to reach 3.8% in 2018 (vs 3.7% in 2017) and 3.6% in 2019.
- Inflation fears moderated in March following moderate average earnings in the US and ECB President Draghi statements on “still need to see further evidence” on inflation. Moreover, medium-term oil price futures remain below current spot levels. However, with key markets approaching full employment, growth may be constrained by the supply-side, placing some upward pressure on inflation. Tariffs also present an inflationary risk.
- The main risks to our economic and financial scenario are related to 1) rinsing protectionism/fragmentation across the world, 2) upside inflation surprises in the US forcing the Fed to quicken its tightening pace, 3) political risks in Europe (including a no-deal Brexit), 4) a “hard landing” in China triggering a fall in international trade, and 5) a repricing of global risk due to geopolitical tensions.

ADVANCED ECONOMIES

- Tax cuts and higher now also higher spending caps in the US are set to prolong the business cycle, lifting both consumer spending and investment. This has led us to revise up our growth forecast for both 2018 and 2019. Low and falling unemployment may boost wages which, in turn, would lift inflation risks.
- Growth in the euro area will benefit from the self-reinforcing momentum leaded by industry and trade. The growth cycle is expected to continue in 2018-2019, under the combined effect of an investment pick up and a host of accommodating policies. Core inflation is expected to post only a modest recovery. However, the risk of new inflationary pressures in Germany cannot be ruled out as the country is close to full employment.
- Several issues, including Northern Ireland, may yet prevent the conclusion of the Withdrawal Agreement in the Brexit negotiations. Given that there is still a risk of no-deal Brexit, businesses still face considerable uncertainty, which is likely to weigh on investment and hiring decisions. Despite strong export demand, UK growth remains subdued.

EMERGING MARKETS

- Growth is expected to moderate gradually in China, but strong external demand will keep growth high in Emerging Asia at around 6% over 2018-19.
- In Emerging Europe, growth rates should moderate after the 2017 rebound. Activity will remain supported by a favourable external environment and accommodative policies (Romania, Turkey).
- In Latin America, the recovery is expected to strengthen reflecting firmer growth in South America (Brazil, Argentina).
- Regional growth in Africa is expected to continue accelerating in 2018 and 2019 amid stronger commodity prices, and improved weather conditions enabling an increase in agricultural output.
- In the Middle East, higher oil prices will enable a recovery in domestic demand benefiting non-energy sectors, but necessary fiscal adjustments will continue to weigh on the medium-term growth outlook.

CENTRAL BANKS

- We expect the Fed to remain gradual in its approach to monetary policy normalization, but still expect more hikes than the market discounts in 2018-2019.
- In the euro area, core inflation is expected to post only a modest recovery. The ECB is expected to implement a very gradual exit strategy from its unconventional monetary and hike rates only in 2019.
- The reappointment of Kuroda as governor of the BOJ signals continued accommodative monetary policy (a yield target for 10y bonds, and negative policy interest rate).

FINANCIAL MARKETS

- Global stock markets suffered pronounced volatility in February after a long bull market, on inflationary fears (rising oil prices and US wages).
- Volatility reached its highest level since 2011 but the correction was short lived with no credit spread widening and no significant movements on exchange rates.
- If monetary conditions remain accommodative into the medium term, yield-seeking investors could increase exposure to lower-rated borrowers, which would increase financial vulnerabilities.

INVESTMENT IS THE NEXT GROWTH RELAY

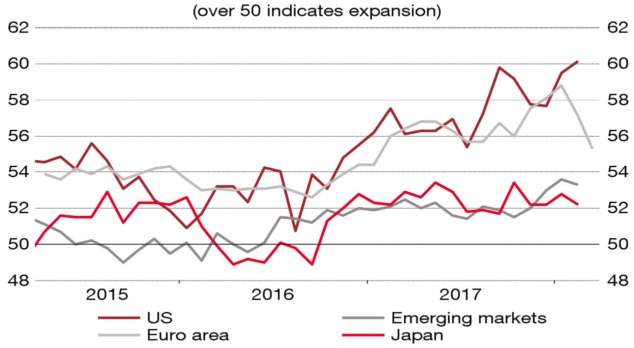
- **The global economy is experiencing an expansion that has not been equalled since 2012**
- **The current business cycle could face supply constraints**
- **The pick-up in investment observed in the main economies provides some reassurance**

SURPRISINGLY STRONG GROWTH OVER THE LAST YEAR

Global activity has been surprisingly strong over the last year. After several years of quasi-stagnation, industrial production in developed countries is showing very dynamic trends, growing even faster than in emerging countries. Global trade has also rebounded sharply, reflecting the global pick-up in demand. After fears of deflation in 2015-2016, concerns are now focused on inflation, following Donald Trump's election and his fiscal stimulus program. Since then, economic momentum has persisted but questions are arising as to the solidity of the dynamic at play.

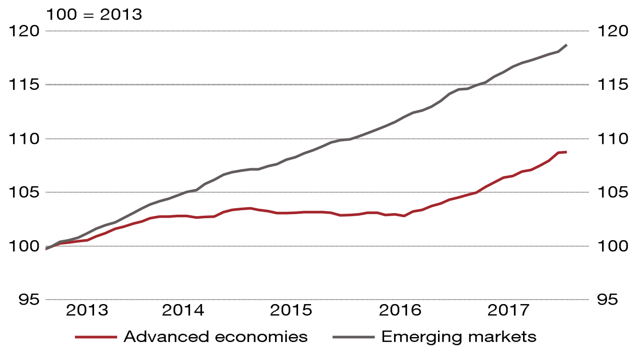
PMI indices

(over 50 indicates expansion)



Source: Thomson Reuters Datastream

Industrial production



Source: Thomson Reuters Datastream

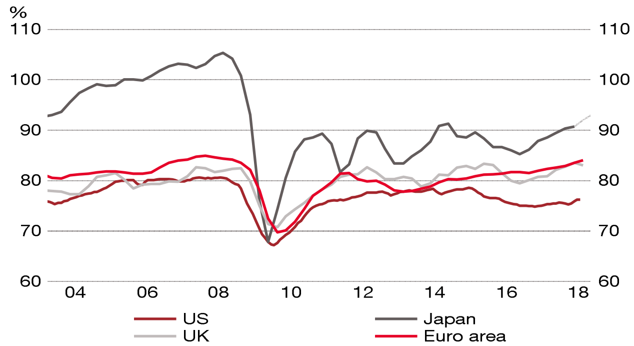
These questions revolve around the nature of the "cycle". Is it simply a catch-up after years of weak growth? Could the recovery in demand lead to inflation? Can we expect to see an acceleration of productivity? Is demand solid enough to deal with an environment of higher interest rates?

In the current debate on the medium- and long-term growth outlook, the theme of investment plays a central role, since it is the factor that will help to ensure a permanent process of capital accumulation and prolong the cycle.

AND A REVIVAL OF INVESTMENT

Although financial conditions are still very accommodative, the current growth spurt does not seem to be driven solely by a boom in consumption fuelled by debt. After several years of sluggishness, investment is showing strong trends again.

Capacity utilisation rate

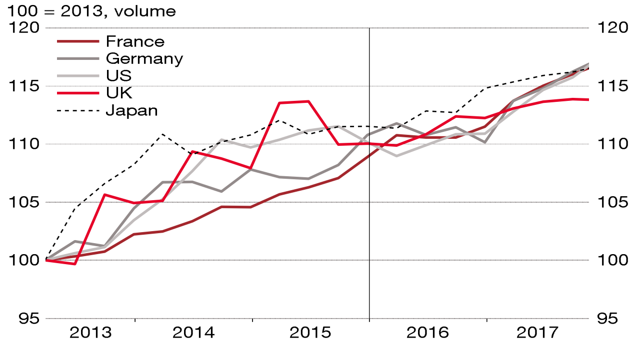


Source: Thomson Reuters Datastream

The share of investment in GDP is not yet back at the levels seen before 2008 in developed countries. But production capacity utilisation rates have been picking up for a little more than a year and are starting to reach record highs in Europe (France, Germany, UK) while in the US and Japan they are still below peak levels but are rising gradually. A similar scenario is evident in certain major emerging countries, notably Central and Eastern Europe and Turkey. In the latter, inflationary pressure is already being felt in an environment in which the labour market is showing signs of tension. In the developed countries, inflation remains low, which explains the very gradual rate of exit from unconventional monetary policies.

"Productive" investment therefore is reviving in most countries. A pick-up has been observed in companies' capital expenditure, both in terms of investment in machinery and equipment as well as in IT and non-residential construction. This indicates that the strength of growth in recent quarters may have a virtuous effect. It is worth noting that while private non-residential investment in volume terms is increasing in a synchronized manner in the main developed countries, this is not the case for the UK where the level remains close to that of 2015. Uncertainties around Brexit are weighing on the prospects of entrepreneurs.

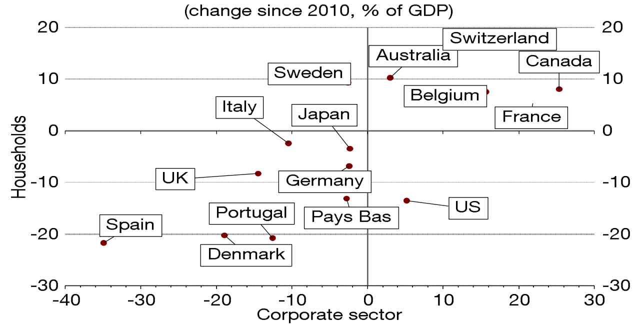
Non-residential investment



Source: Thomson Reuters Datastream

Private sector debt

(change since 2010, % of GDP)

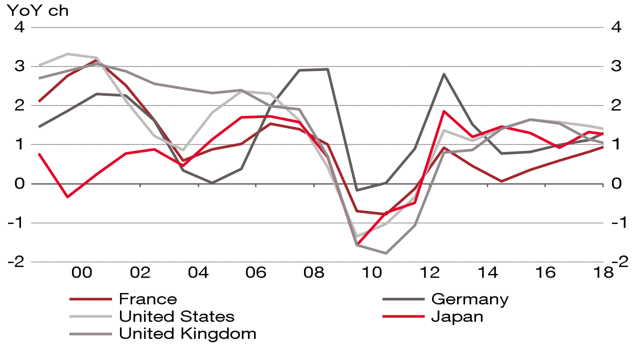


Source: Thomson Reuters Datastream

This raises a question as to whether the current growth, which is more capital intensive, could give rise to an increase in growth potential in the foreseeable future. If this is not the case, are we simply in a catch-up cycle after years of low capex, while remaining in a situation of secular stagnation?

It is, of course, difficult to predict the length of the current cycle. On an encouraging note, it seems there has been a slight pick-up in labour productivity gains.

Labour productivity - GDP per capita in volume



Source: Thomson Reuters Datastream

The recovery in investment and concomitant rise in labour productivity suggest that growth is being underpinned by a certain number of solid elements: higher investment, more jobs, with no inflationary spiral. Neither do we see a spiral in global debt.

THE ISSUE OF DEBT

Accommodative monetary policies have enabled economic agents to benefit from a historically favourable interest rate environment. As such, companies have been able to raise capital to finance their activity and investment.

Corporate debt in a certain number of developed and emerging countries has been on an upward trend in recent years. This in itself is not worrying, but it raises a question around the potential vulnerability of the production sector to an environment of higher interest rates. If growth remains high, the return on capital may be enough to cover its cost. However, a negative scenario could emerge if economic growth were to turn weak and inflation and the cost of debt were to increase.

For the time being, stagflation, triggered for example by a new oil shock, seems unlikely, but the rise in debt calls for close monitoring of the effectiveness of current investment. A dynamic of investment growth that is not accompanied by sustainable productivity gains could lead to constraints emerging on the supply side. This would give rise to inflationary pressure and a premature end to the current growth cycle.

Economic Forecasts

Real GDP growth (annual, %)	2015	2016	2017	2018 (f)	2019 (f)	Share of world GDP 2016 (%) Purchasing power parities[1]	Share of world GDP 2016 (%) Current exchange rates	GDP - 2016 USDbn Current exchange rates
Developed markets	**2.3**	**1.6**	**2.3**	**2.4**	**1.9**	**37.8**	**57.1**	**43 033**
United States	2.9	1.5	2.3	2.9	2.4	15.5	24.8	18 624
Japan	1.4	0.9	1.7	1.4	1.0	4.4	6.6	4 960
Euro area	2.0	1.8	2.5	2.2	1.7	11.6	15.7	11 922
Germany	1.5	1.9	2.5	2.1	1.9	3.3	4.6	3 473
France	1.0	1.1	2.0	2.0	1.7	2.3	3.3	2 464
Italy	0.8	1.0	1.5	1.4	1.1	1.9	2.5	1 861
Spain	3.4	3.3	3.1	2.6	2.1	1.4	1.6	1 238
United Kingdom	2.3	1.9	1.7	1.5	1.3	2.3	3.5	2 658
Emerging markets	**4.0**	**4.2**	**4.6**	**4.7**	**4.6**	**62.2**	**42.9**	**31 256**
Asia	6.2	6.0	6.2	5.9	5.7	35.0	24.8	18 724
China	6.9	6.7	6.9	6.4	6.0	17.8	14.9	11 181
India	8.0	7.1	6.8	6.9	6.8	7.3	3.0	2 210
Africa	3.2	0.8	2.4	3.4	3.7	3.9	2.3	1 152
Latin America	0.1	-0.7	1.5	2.1	2.8	7.9	6.6	4 790
Brazil	-3.8	-3.6	1.0	2.0	2.5	2.6	2.4	1 809
Eastern Europe (incl. Turkey, ex. Russia)	3.0	2.6	5.0	3.8	3.0	4.8	3.1	2 341
Russia	-2.8	-0.2	1.5	1.2	1.2	3.2	1.7	1 296
Middle East	2.7	5.3	1.9	3.2	3.6	7.4	4.3	2 953
World - Weighted by PPP rates	**3.4**	**3.2**	**3.7**	**3.8**	**3.6**	**100**		
World - At current exchange rates	**3.0**	**2.7**	**3.3**	**3.3**	**3.1**		**100**	**74 289**
Oil price (Brent USD/Barrel)	**52.5**	**43.5**	**54.0**	**62.0**	**65.0**			

Consumer prices index (annual growth rate, %)	2015	2016	2017	2018 (f)	2019 (f)
United States	0.1	1.3	2.1	2.2	2.5
Japan	0.8	-0.1	0.4	0.8	1.3
Euro area	0.0	0.2	1.5	1.3	1.8
Germany (HICP)	0.1	0.4	1.7	1.6	1.8
France (CPI)	0.1	0.2	1.0	1.4	1.6
Italy (HICP)	0.7	0.5	0.8	1.3	1.4
Spain (HICP)	-0.6	1.4	1.4	1.4	1.9
United Kingdom	0.0	0.7	2.6	2.5	2.3

[1] Purchasing Power Parity (PPP) rates are used to equalise the cost of a standardised basket of goods between different countries. The GDP weighting of different countries as a share of world GDP expressed in PPP is based on the latest estimates by the World Bank.

	13/03/2018	Jun 2018	Dec 2018	Dec 2019	2016	2017	2018 (f)	2019 (f)
Interest rates								
United States								
Fed Funds target rate	1.25-1.5	1.75-2	2-2.25	2.75-3	0.39	0.95	1.80	2.50
10 year Gvt Bonds	2.8	3.1	3.4	3.7	1.8	2.4	3.1	3.5
Japan								
Complementary Deposit Facility rate	-0.10	-0.10	-0.10	-0.10	-0.08	-0.10	-0.10	-0.10
10 year Gvt Bonds	0.0	0.1	0.2	0.4	0.0	0.1	0.1	0.3
United Kingdom								
Bank rate	0.50	0.75	0.75	0.75	0.40	0.30	0.65	0.75
10 year Gvt Bonds	1.5	1.6	1.6	1.6	1.3	1.2	1.5	1.6
Euro area								
Refinancing rate	0.00	0.00	0.00	0.50	0.01	0.00	0.00	0.30
10 year Gvt Bonds								
Germany	0.6	0.6	0.9	1.4	0.1	0.4	0.7	1.2
France	0.8	0.8	1.1	1.5	0.5	0.8	0.9	1.3
Italy	2.0	2.1	2.3	3.0	1.5	2.1	2.1	2.8
Spain	1.4	1.5	1.6	1.9	1.4	1.6	1.5	1.7
Exchange rates								
EUR / USD	1.24	1.23	1.20	1.25	1.11	1.13	1.22	1.23
EUR / GBP	0.89	0.89	0.91	0.94	0.82	0.88	0.90	0.93
EUR / JPY	132	132	132	128	120	127	132	130
GBP / USD	1.40	1.37	1.32	1.32	1.35	1.29	1.36	1.32
USD / JPY	107	107	110	102	109	112	108	106

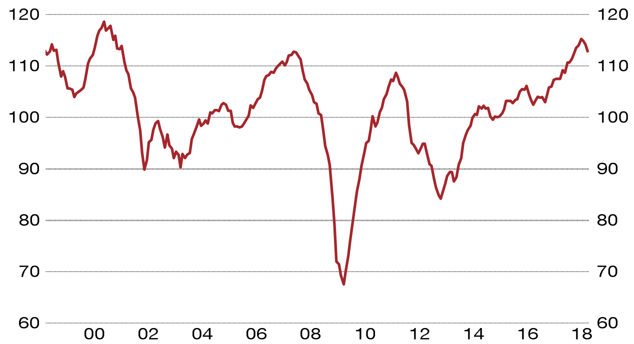
EURO AREA

- **Activity will continue to be underpinned by investment and an improving job market**
- **Moderate inflation will give the ECB time to normalize monetary policy**
- **Political risk could derail this scenario if there are financial pressures**

The euro area economy should continue to outperform the trend seen in recent years. The region stands to benefit from a dynamic of sustained investment insofar as the capacity utilization rate in the manufacturing sector is near historical highs. Supportive financial conditions and an improvement in confidence – in an environment in which corporate earnings are improving– will help to sustain corporate investment.

The surveys confirm a revival of optimism in most sectors, including manufacturing, services, retailing, consumption and construction. The European Commission Economic Sentiment Indicator has reached its highest level in nearly 18 years.

Economic sentiment indicator

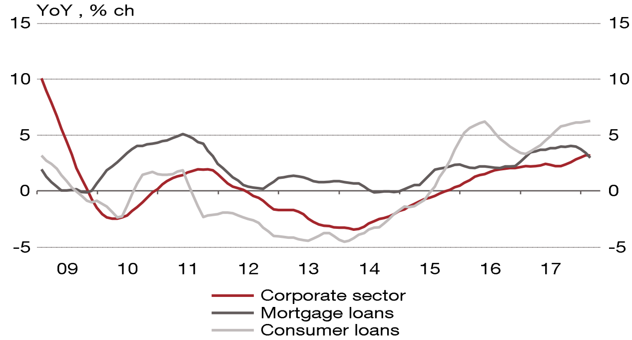


Source: Thomson Reuters Datastream

Consumption is likely to be another growth driver as household disposable income will benefit from the improvement in the labour market. Shortages on this market are being felt, which over the next two years could give rise to inflationary pressures.

The current environment is however a one of low inflation. Against this backdrop, we expect the ECB to maintain an accommodative monetary policy stance, with an initial interest rate hike not coming until 2019. The ECB will also maintain the size of its balance sheet unchanged as is once it terminates QE in 2018. A supportive monetary environment will favour access to credit. Growth in 2019 is likely to settle under the impact of less dynamic global growth and investment.

Private sector bank lending



Source: Thomson Reuters Datastream

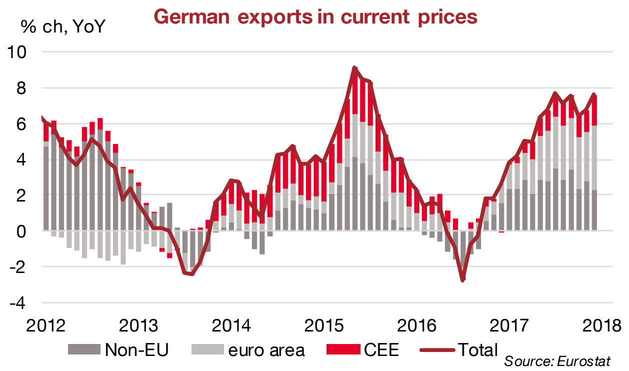
There remains a risk, nevertheless, of renewed financial pressure in the region if the political environment were to deteriorate. In this regard, questions around the impending formation of a coalition in Italy should not be neglected. Similarly, protectionist risks associated with a disordered Brexit could weigh on investment decisions.

	2015	2016	2017	2018 (f)	2019 (f)
Real GDP, % ch	**2.0**	**1.8**	**2.5**	**2.2**	**1.7**
Household consumption	1.8	1.9	1.7	1.7	1.7
Public consumption	1.3	1.8	1.2	1.3	1.0
Investment	3.0	4.5	3.1	2.8	2.4
Exports	6.1	3.4	5.3	4.7	4.0
Imports	6.5	4.8	4.3	4.2	4.1
Purchasing power of disposable income, % ch	**1.5**	**1.8**	**1.6**	**2.0**	**1.3**
Unemployment rate, %	**10.9**	**10.0**	**9.0**	**8.3**	**7.9**
Households saving rate, % of disposable income	**12.4**	**12.2**	**12.1**	**12.3**	**11.9**
Inflation rate, %	**0.0**	**0.2**	**1.5**	**1.3**	**1.8**
Fiscal balance, % of GDP	**-2.1**	**-1.5**	**-1.1**	**-1.0**	**-1.0**
Current account balance, % of GDP	**3.2**	**3.4**	**3.5**	**2.9**	**3.0**

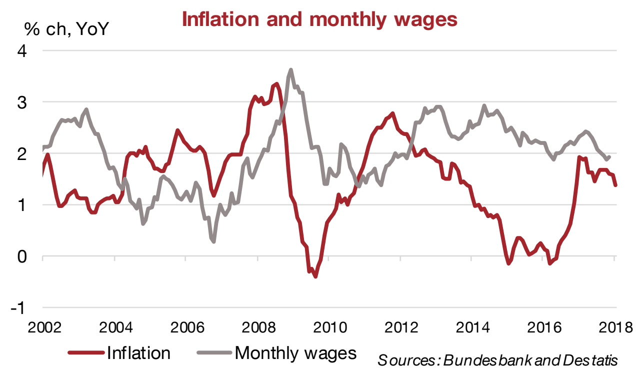
GERMANY

- **Growth should slightly slow from 2018 onwards after last year's strong performance**
- **The negotiated wage increases should not give rise to a marked acceleration of inflation**
- **Despite an anticipated increase in expenditure, the budget balance should remain in surplus**

Growth in Germany reached 2.5% in 2017, its strongest performance since 2011, in line with a cyclical recovery in the euro area. Germany will continue to benefit from strong global trade in an environment in which productive investment is increasing in developed countries. Private consumption is set to remain strong, underpinned by an increase in household purchasing power. Nevertheless, growth will moderate from 2018 with the economy approaching full employment (employment is at its highest level since reunification in 1990).



Despite strong employment, inflation should remain contained. Real wages in the manufacturing sector are increasing strongly, but are less dynamic in services and unskilled jobs. Moreover, many older workers and household second-income earners occupy less well-paid jobs ("mini-jobs").



The new governing coalition between the CDU and SPD is scheduling an increase in public investment in infrastructures and digital technologies, and in current expenditure (healthcare and education). This will be introduced between 2018-2022 and will be financed via resources from previous budget surpluses. As such, it will not compromise the budget balance.

Despite solid fundamentals, the German economy is facing risks. The population is ageing, which is aggravating the shortage of labour. Surprises on the inflation front could still materialize in a context of full employment and accommodative fiscal and monetary policies. Lastly, a ramp up in protectionist measures in the United States could hurt German industry, which largely hinges on external trade.

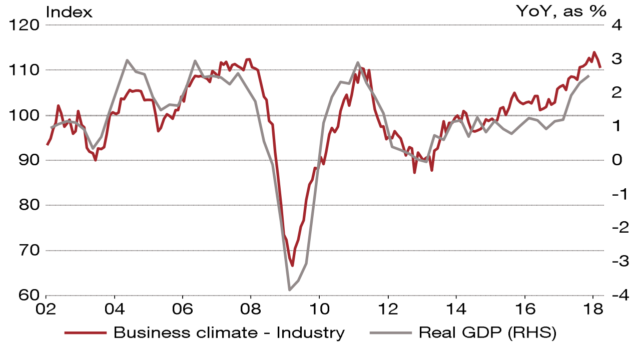
	2015	2016	2017	2018 (f)	2019 (f)
Real GDP, % ch	**1.5**	**1.9**	**2.5**	**2.1**	**1.9**
Household consumption	1.6	1.9	2.1	1.7	2.0
Public consumption	2.9	3.7	1.6	1.5	1.0
Investment	1.0	2.9	3.9	2.2	2.2
Exports	4.7	2.4	5.3	4.7	4.1
Imports	5.2	3.8	5.6	4.8	4.2
Purchasing power of disposable income, % ch	**1.9**	**2.2**	**2.1**	**2.0**	**1.9**
Unemployment rate, %	**6.4**	**6.1**	**5.7**	**5.3**	**5.0**
Households saving rate, % of disposable income	**9.6**	**9.7**	**9.9**	**10.2**	**10.1**
Inflation rate, %	**0.2**	**0.5**	**1.7**	**1.6**	**1.8**
Fiscal balance, % of GDP	**0.7**	**0.8**	**0.9**	**1.0**	**1.0**
Current account balance, % of GDP	**8.6**	**8.2**	**7.9**	**7.7**	**7.7**

FRANCE

- **The cyclical catch-up is set to continue and growth is expected to remain close to 2% in 2018**
- **Despite a rise in inflation, consumption is set to be the main driver of activity**
- **Growth in corporate debt continues, causing increased sensitivity to a rise in interest rates**

Economic momentum remains strong. GDP accelerated in Q4-17 (0.7% QoQ), driven by investment and exports. Moreover, at the start of 2018, business and household confidence surveys remained at high levels.

Real GDP and business climate



Source: Thomson Reuters Datastream

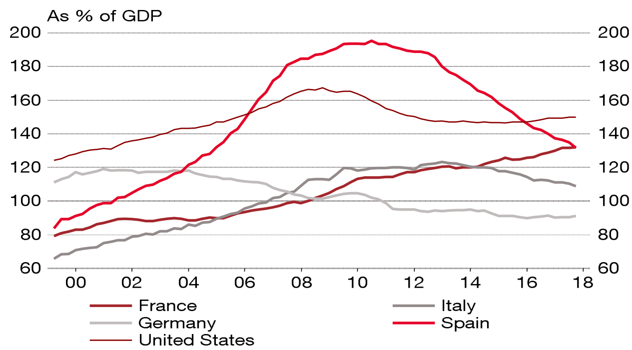
We expect growth to remain at 2% in 2018 for the second year in a row, a performance not seen since 2006-2007. Subsequently, GDP is set to start slowing modestly in 2019.

Private consumption will be the main GDP growth driver. Households will benefit from the continued increase in employment and the strength of capital incomes. Purchasing power is nevertheless likely to be hampered in 2018 by fiscal policy (notably an increase in the CSG tax) and a modest rise in inflation (driven by energy and tobacco prices), before rebounding in 2019.

Growth in investment should return to a more moderate pace in 2018 and in 2019. Household investment (primarily comprising the purchase of new homes and expenditure on maintenance and renovation) is likely to ease. The slight increase in interest rates and the rise in real estate prices will reduce home-buying capacity. In contrast, we expect corporate investment to remain very strong in 2018 given the current high level of production capacity utilization. Business investment should also benefit from growth in exports, although the euro exchange rate is a key factor that requires close monitoring, in case of significant appreciation.

Against this backdrop, corporate debt and, to a lesser degree, household debt should continue to increase. While several factors play a mitigating role on the potential impact of this trend (mainly a concomitant increase in corporate cash levels), the latter is being closely monitored by the macro-prudential authorities because it exposes France to the risk of a more rapid increase in interest rates than currently expected.

Private non-financial sector debt



Source: Thomson Reuters Datastream

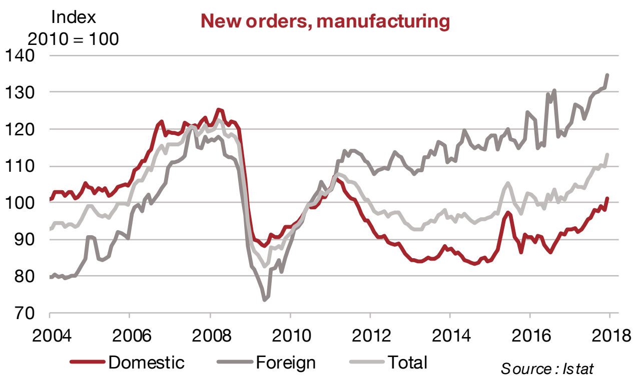
	2015	2016	2017	2018 (f)	2019 (f)
Real GDP, % ch	**1.0**	**1.1**	**2.0**	**2.0**	**1.7**
Household consumption	1.3	2.1	1.3	1.7	1.7
Public consumption	1.1	1.2	1.6	1.4	1.2
Investment	0.9	2.7	3.8	3.1	2.1
Exports	4.0	1.9	3.3	4.5	4.0
Imports	5.5	4.2	4.1	4.1	3.8
Inflation rate, %	**0.1**	**0.2**	**1.0**	**1.4**	**1.6**
Purchasing power of disposable income, % ch	**0.8**	**1.8**	**1.6**	**1.5**	**1.9**
Unemployment rate, %	**10.1**	**9.8**	**9.1**	**8.6**	**8.1**
Households saving rate, % of disposable income	**14.2**	**14.0**	**14.3**	**14.1**	**14.2**
Fiscal balance, % of GDP	**-3.6**	**-3.4**	**-2.6**	**-2.4**	**-2.9**
Current account balance, % of GDP	**-0.4**	**-0.9**	**-1.6**	**-1.5**	**-1.5**

ITALY

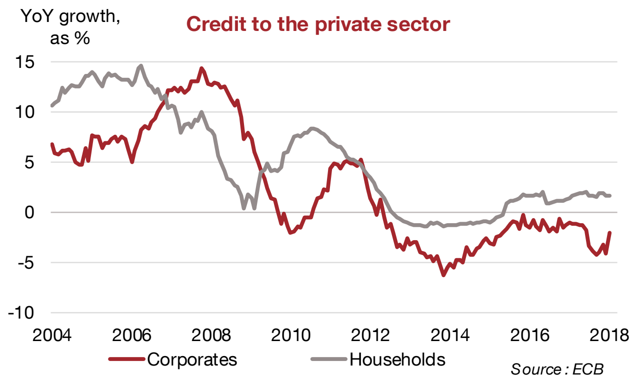
- **GDP growth should remain strong in 2018 and decelerate from 2019**
- **The defeat of the traditional parties in the general elections did not result in financial instability**
- **Uncertainty could increase if a populist movement leads the coalition and relaxes fiscal policy**

In the wake of the euro area, Italian growth accelerated in 2017 to 1.5%. the expansion was driven by investment, particularly in the transport sector, and by strong industrial output.

In 2018, growth will remain dynamic. Investment will benefit from the attractive borrowing terms offered by the ECB's accommodating policy and slightly improved corporate margin rates. The good momentum of exports will support industrial production. In contrast, household consumption will continue to be penalized by moderate job creation and sluggish wage growth.



Going forward, we expect a temporary acceleration in inflation due to rising energy prices but core inflation should remain lower than the European average because of a durable fragility in the labour market. The unemployment rate should continue to fall but will remain above 10% in 2019.



The political situation in the aftermath of the elections remains very uncertain. The defeat of the traditional parties (the Democratic Party of Matteo Renzi and Forza Italia, party of Berlusconi) for the benefit of the 5-star Movement (Luigi di Maio) and the League (Matteo Salvini) signs the distrust of the Italians in front of the political class in a context of high unemployment and poverty, while the perceived management of the migration crisis by the European Union has generated a significant rise in euro scepticism in the peninsula.

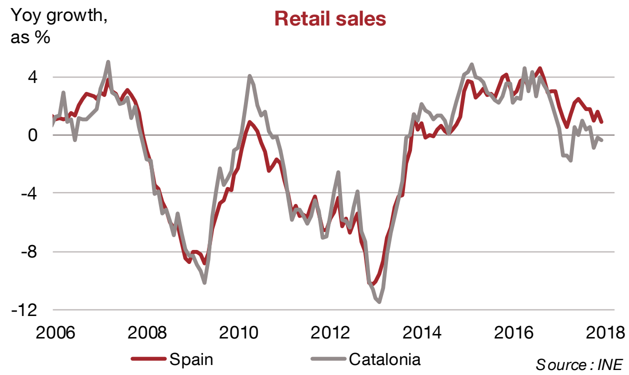
The electoral programs of the Eurosceptic parties give an important place to a large fiscal shock: tax cuts for households and businesses, repeal of the 2011 pension reform, increase in family allowances and large infrastructure plans. In such a case, the risk of a fiscal slippage would increase.

	2015	2016	2017	2018 (f)	2019 (f)
Real GDP, % ch	**0.8**	**1.0**	**1.5**	**1.4**	**1.1**
Household consumption	1.9	1.4	1.3	1.0	1.1
Public consumption	-0.6	0.6	0.1	0.4	0.6
Investment	1.9	3.3	3.9	4.5	1.8
Exports	4.2	2.6	6.0	5.4	3.7
Imports	6.6	3.8	5.7	5.3	4.1
Inflation rate, %	**0.1**	**-0.1**	**1.3**	**1.3**	**1.5**
Purchasing power of disposable income, % ch	**0.3**	**1.0**	**0.9**	**1.1**	**0.8**
Unemployment rate, %	**11.9**	**11.7**	**11.3**	**10.7**	**10.3**
Households saving rate, % of disposable income	**10.5**	**10.6**	**10.3**	**10.4**	**10.2**
Fiscal balance, % of GDP	**-2.6**	**-2.5**	**-2.2**	**-2.4**	**-2.4**
Current account balance, % of GDP	**1.5**	**2.7**	**2.9**	**3.0**	**2.9**

SPAIN

- **After three years of rapid growth, the economy is set to slow in 2018 and 2019**
- **With fiscal balance consolidating, Spain will exit the Excessive public deficit procedure in 2018**
- **Political paralysis continues in Catalonia, without overly worrying markets**

After three years of robust growth, the Spanish economy is starting to slow. The construction sector has lost momentum after double-digit growth in the first half of 2017. Household consumption has slowed. This trend is set to continue, with less job creation — unemployment is close to its estimated structural level of around 13% — and wage growth per capita scarcely above that of inflation, in an environment in which the savings rate is close to a historical low.



Source : INE

Investment should also progress more moderately after three years of strong growth and in the absence of pressure on production capacities. However, exports of goods and services will continue to benefit from the cyclical expansion of Spain's main trading partners in the eurozone. The competitiveness gains made over the last ten years will not be jeopardized by the still moderate growth in wages.

We anticipate GDP growth of 2.6% and 2.1% respectively in 2018 and 2019 and a gradual return to potential growth of 1.6% in 2022. Inflation will accelerate in 2019 due to the anticipated increase in oil prices.

Source : INE (Instituto Nacional de Estadistica)

The current account has been rebalanced after the crisis and Spain is running surpluses. Public finances have also improved. After ten years of heavy public deficits, Spain will finally exit the excessive deficit procedure in 2018.

Risks remain concerning the outcome of the political crisis after the referendum and Catalonia's unilateral declaration of independence in October 2017, and the takeover of the region by the Central administration. Political paralysis in Catalonia and the region's economic underperformance are set to continue but without worrying the financial markets or excessively penalizing business and investment throughout the country.

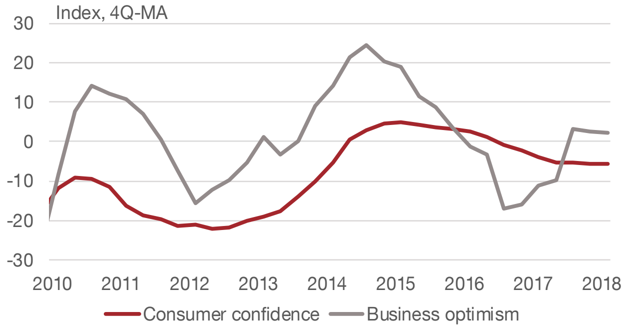
	2015	2016	2017	2018 (f)	2019 (f)
Real GDP, % ch	**3.4**	**3.3**	**3.1**	**2.6**	**2.1**
Household consumption	3.0	3.0	2.4	2.2	1.8
Public consumption	2.1	0.8	1.6	1.1	0.8
Investment	6.5	3.3	5.0	3.8	3.5
Exports	3.9	3.1	5.0	4.3	4.0
Imports	6.1	1.3	5.0	3.7	3.5
Purchasing power of disposable income, % ch	**2.3**	**2.0**	**1.2**	**1.7**	**1.4**
Unemployment rate, %	**22.1**	**19.7**	**17.2**	**15.7**	**14.5**
Households saving rate, % of disposable income	**8.6**	**7.7**	**6.9**	**6.4**	**6.1**
Inflation rate, %	**-0.6**	**1.4**	**1.4**	**1.4**	**1.9**
Fiscal balance, % of GDP	**-5.3**	**-4.5**	**-3.1**	**-2.4**	**-1.9**
Current account balance, % of GDP	**1.1**	**1.9**	**1.7**	**1.8**	**2.0**

UNITED KINGDOM

- **GDP growth is set to average 1.5% in 2018 as consumption and investment slow**
- **The BoE is set to proceed with one rate hike of 25bp in 2018 before a pause in 2019**
- **Brexit uncertainty is the main risk to the outlook as negotiations remain in deadlocks**

The uncertainty surrounding Brexit should further weigh on business investment. Real wage growth remains sluggish (despite a tight labour market), savings rate near record low levels, and indebtedness has been rising fast, all factors that will constrain consumer spending in coming quarters. On the contrary, exports will continue benefiting form a weak sterling pound and the momentum in the global economy, improving the outlook. Against this backdrop, we expect real GDP growth to average 1.5% and 1.3% in 2018 and 2019 respectively.

Consumer & business confidence



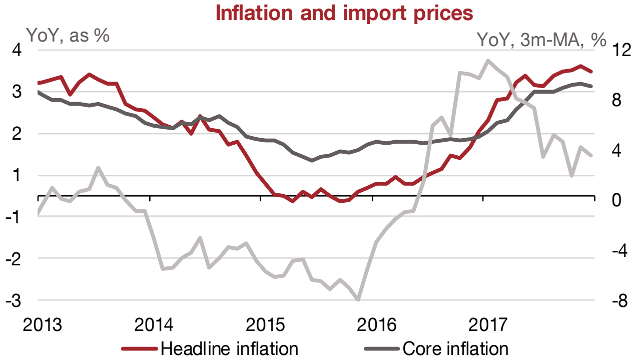
Sources : ONS, CBI

The unexpected strength in tax receipts throughout H2-17 is set to narrow the fiscal deficit to 2.2% of GDP in 2017. Given the government's pledge to reducing the sovereign debt ratio, we see no new additional spending in the short-term. The government's fiscal mandate of reducing the deficit below 2% of GDP by 2021 could be challenged by the prospective cost of Brexit financial settlement, estimated at £37.1bn by the Office for Budget Responsibility.

The Bank of England is likely to proceed with one rate hike of 25bp in Q2-18 as inflation remains well above the 2% target, setting the policy rate at 0.75% in 2018. As economic growth slows in H2-18 and H1-19, we expect monetary policy to remain accommodative with no further rate hike whilst inflation eases. Yet, we see an upside risk on inflation outlook as sterling volatility and supply constraints may fuel price pressures.

Brexit developments remain the main risk to our central scenario over the medium-term. The second phase of negotiations, which kicks-off late March, aims to an understanding on the framework for the future relationship and complete an orderly withdrawal of the U.K. from the EU. The agreed-transition-period, which maintains the status-quo until year-end 2020, relies on a final agreement on the withdrawal process. We expect it to be ratified by late-2018. During the transition, the UK will remain in the Single Market and the Customs Union. Regarding the complexity of the talks, we do not expect a full trade agreement before the official departure date on 29 March 2019.

Inflation and import prices



Sources : ONS, SG

	2015	2016	2017	2018 (f)	2019 (f)
Real GDP, % ch	**2.3**	**1.9**	**1.7**	**1.5**	**1.3**
Household consumption	2.6	2.9	1.7	1.2	1.2
Public consumption	0.6	0.8	0.3	1.7	1.6
Investment	2.8	1.8	3.9	2.0	0.6
Exports	5.0	2.3	5.0	1.5	4.9
Imports	5.1	4.8	3.5	3.1	4.0
Purchasing power of disposable income, % ch	**5.3**	**0.2**	**0.5**	**2.1**	**1.4**
Unemployment rate, %	**5.3**	**4.9**	**4.4**	**4.2**	**4.3**
Households saving rate, % of disposable income	**9.2**	**7.1**	**6.0**	**6.5**	**6.6**
Inflation rate, %	**0.0**	**0.7**	**2.6**	**2.5**	**2.3**
Fiscal balance, % of GDP	**-4.3**	**-2.9**	**-2.2**	**-2.3**	**-2.5**
Current account balance, % of GDP	**-5.2**	**-5.7**	**-4.7**	**-5.5**	**-5.9**

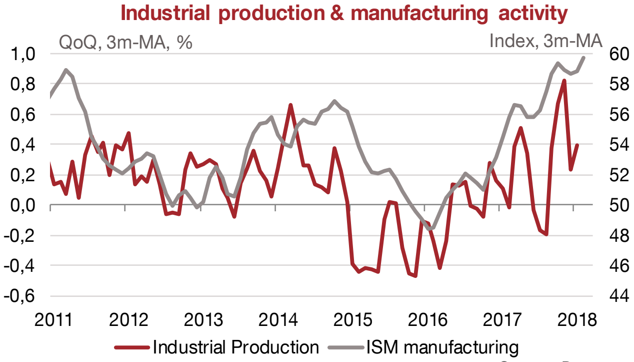
UNITED STATES

- **GDP growth is set to accelerate in 2018 on the back of a large fiscal stimulus**
- **We expect the Fed to deliver six rate hikes of 25bp each through 2019**
- **As mid-term elections near, protectionist measures may increase, risking global retaliation**

Tax reform and additional discretionary spending is likely to lift further GDP growth in the next two years, extending the current expansion cycle. Additional disposable income should lift households' expenditures. Investment will benefit from growing demand, increased profitability resulting from the corporate tax reform and higher public spending.

The stimulus –an estimated $2tn package over ten years– is unlikely to give a long-term boost to the economy as public debt raises. Under the assumption of continued public spending in 2020 prior a progressive scale-back in budget caps, we anticipate GDP growth to average 2.9% and 2.4% in 2018 and 2019 respectively, before a cyclical trough of 1% in 2020-2021. Over the longer-run, we expect the GDP growth trajectory to converge back to its long-term trend, around 1.8%.

Industrial production & manufacturing activity



Source : Datastream

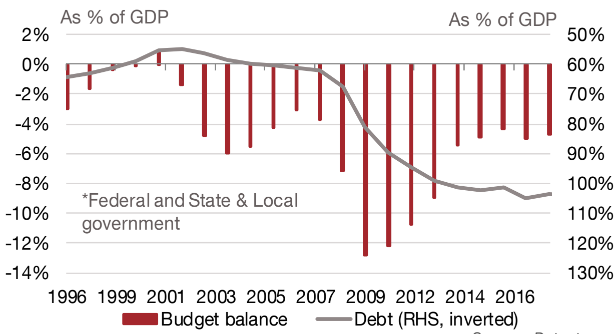
In addition, the stimulus plan comes at a time when the US is operating near-full capacity. As the unemployment rate drops further, wage growth is likely to accelerate. We see a slight tick-up in the labour force participation rate, highlighting reduced shadow slack and an improving labour market.

In this context, tighter monetary policy is set to act as a headwind. Inflationary pressures could surprise on the upside, potentially forcing the Fed to proceed with more than current market's expectation of three rate hikes of 25bp in 2018 and two the following year. We believe inflation will accelerate only gradually above the 2% target in 2018 (2.2%) and 2019 (2.5%), consistent with six rate hikes of 25bp each through year-end 2019.

The sustainability of US public finances will be a key concern in the longer-run. We expect the general government deficit to widen sharply to 6.0% of GDP in 2018 and 6.8% of GDP in 2019. This will increase the gross public debt to over 130% of GDP by 2027.

The US trade policy remains the main risk to our scenario. As mid-term elections near in November 2018, we expect more trade restrictions to come after a first set of tariffs announced on steel and aluminium.

General government deficit and gross debt



Source : Datastream

	2015	2016	2017	2018 (f)	2019 (f)
Real GDP, % ch	**2.9**	**1.5**	**2.3**	**2.9**	**2.4**
Household consumption	3.6	2.7	2.7	3.3	2.4
Public consumption	1.4	0.8	0.1	1.7	3.4
Investment	3.4	2.2	3.0	3.8	2.8
Exports	0.4	-0.3	3.4	4.6	3.9
Imports	5.0	1.3	3.9	7.0	6.3
Purchasing power of disposable income, % ch	**3.1**	**0.8**	**1.4**	**3.1**	**2.9**
Unemployment rate, %	**5.3**	**4.9**	**4.4**	**3.9**	**3.6**
Households saving rate, % of disposable income	**3.1**	**0.8**	**1.4**	**3.1**	**2.9**
Inflation rate, %	**0.1**	**1.3**	**2.1**	**2.2**	**2.5**
Fiscal balance, % of GDP	**-4.3**	**-5.0**	**-4.7**	**-6.0**	**-6.8**
Current account balance, % of GDP	**-2.4**	**-2.4**	**-2.3**	**-2.9**	**-3.9**

JAPAN

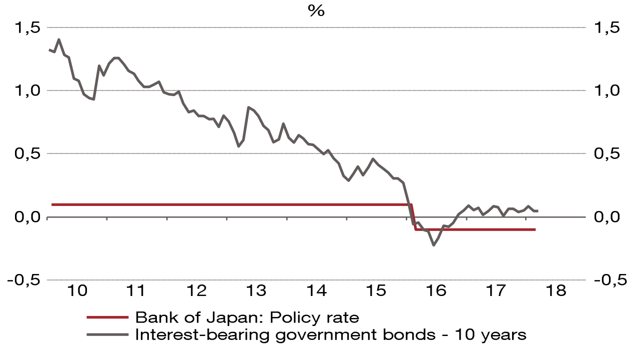
- **The overall policy stance is supportive to growth, which will remain above potential**
- **Labour shortages are evident, but wages and inflation are unlikely to gain much traction**
- **Threats coming from N. Korea, rising protectionism and yen strength are risk factors to watch**

After expanding at 1.7% in 2017, well above the potential growth rate of 0.5% projected by the Bank of Japan (BOJ), real GDP is expected to slow down progressively to an average of 0.8% in 2018-2022.

On the domestic front, the government will continue to pursue flexible fiscal policies and run a primary budget deficit in coming years. The reappointment of Kuroda as governor of the BOJ also signals the maintain of accommodative monetary policy, which combines a quantitative easing program, a yield target for ten-year Japanese government bonds and a policy interest rate of -0.1%. Currently at 0%, we expect a modest increase in the yield target in late 2018.

Interest rates

%



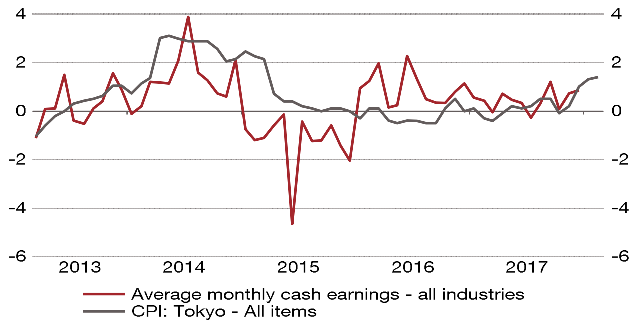
Source: Thomson Reuters Datastream

The consumption tax hike from 8% to 10% scheduled to October 2019 is however set to disrupt spending patterns and to moderate the expansion. On the external front, slower global trade momentum will weigh slow export momentum; albeit the services will be boosted by tourism in 2020, expected to benefit from 2020 Summer Olympic games to be held in Tokyo.

The authorities will continue to implement structural reforms intended to lift potential growth and aiming at reflating the economy. Among other initiatives, the government is pushing for a new “*Work Style Reform*”. The package includes caps on overtime hours and income policies to improve working conditions as well as to alleviate the manpower shortage as the nation’s working-age population declines.

Wages and prices

% ch YoY



Source: Thomson Reuters Datastream

Labour shortages are evident, yet wage growth remains weak. Employers are likely to use yen strength as an argument to not significantly increase wages in the spring talks. Setting aside the impact of the consumption tax hike in 2019, inflation will not gain much traction and is likely to remain below target in the next few years.

The stance of the US economy is likely the most important risk for Japan. Rising bond yields in international markets, protectionist temptations in key countries, persistent yen strength and geopolitical tensions around North Korea are other risks factors.

	2015	2016	2017	2018 (f)	2019 (f)
Real GDP, % ch	**1.4**	**0.9**	**1.7**	**1.4**	**1.0**
Household consumption	0.0	0.1	1.0	0.8	0.6
Investment	1.8	1.1	3.9	1.5	0.6
Exports	3.0	1.3	6.8	6.3	4.2
Imports	0.7	-1.9	3.6	3.9	1.7
Purch. power of net disposable income, % ch	**0.8**	**2.3**	**1.6**	**0.8**	**1.4**
Unemployment rate, %	**3.4**	**3.1**	**2.8**	**2.8**	**2.8**
Saving rate, % of net disposable income	**2.8**	**5.1**	**5.6**	**5.6**	**6.4**
Inflation rate, %	**0.8**	**-0.1**	**0.4**	**0.8**	**1.3**
Fiscal balance, % of GDP	**-3.5**	**-4.2**	**-4.1**	**-3.8**	**-3.0**
Current account balance, % of GDP	**3.0**	**3.7**	**4.0**	**4.0**	**4.0**

CHINA

- **The economy should slow in 2018-2019 with lower investment and consumption**
- **Economic policy will continue to focus on adjusting financial imbalances**
- **Risk could come from a bigger-than-anticipated financial adjustment**

The GDP growth rate should continue to moderate in the years ahead as the authorities continue to focus on progressively correcting past excesses (that led to overcapacities and high debt). With GDP growth projected slightly below 6.5% for 2018-2019, the authorities will have achieved the target indicated during the 2010 five-year plan to double annual GDP by 2020.

The efforts to rebalance the Chinese growth model should lead to a slowdown of investment in relation to consumption. The goal still being to reduce overcapacities in manufacturing and curb the surge in corporate debt seen in recent years. Consumption should continue to benefit from an increase in household incomes in an environment in which the labour market is showing signs of tension and household confidence surveys are rising to record high levels.

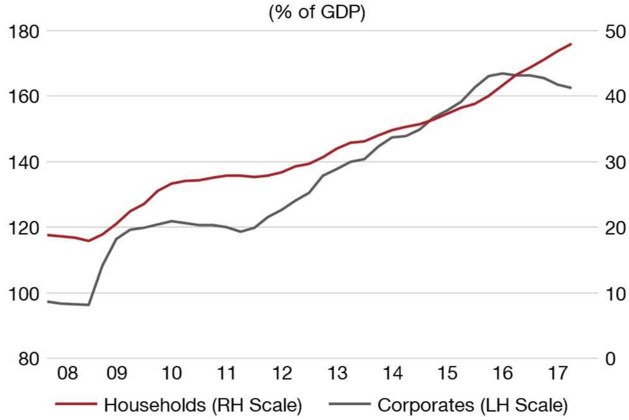
Household confidence index

Source: Thomson Reuters Datastream

Economic policy will focus on ensuring stable growth and on dealing with the issue of excessive corporate debt, notably that of public-owned enterprises in which a certain stabilization has already been observed. The authorities are also starting to centre on the rapid rise in household debt. This subject was notably broached in March during the annual National People's Congress. Monetary and macro-prudential policy, therefore, will maintain a restrictive bias over the next two years. The budget policy will focus on supporting growth, notably via the infrastructure investment plans.

Credit to the private sector

(% of GDP)



Source: Thomson Reuters Datastream

This scenario of a moderate slowdown could be upended in the event of excessive tightening of monetary conditions that could weigh on the country's financial stability due to its high levels of debt. Another risk is that the dynamic of global trade could be obstructed in the event of a trade war between China and the US.

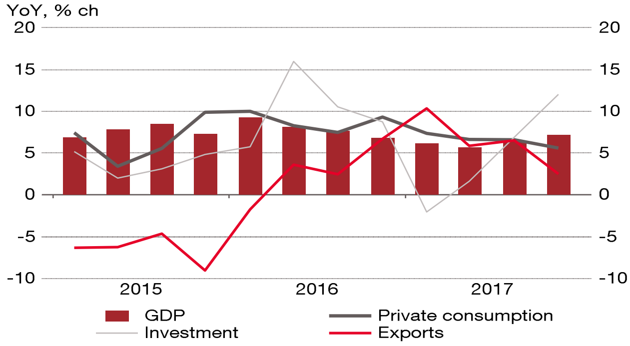
	2015	2016	2017	2018 (f)	2019 (f)
Real GDP, % ch	**6.9**	**6.7**	**6.9**	**6.4**	**6.0**
Consumption	8.1	8.6	7.6	7.5	7.3
Investment	6.2	6.4	5.0	4.7	4.5
Net exports (contrib. to growth, pp)	-0.1	-0.7	0.1	0.1	-0.1
Inflation rate, %	**1.4**	**2.0**	**1.8**	**2.4**	**2.5**
General government balance, % of GDP	**-2.8**	**-3.7**	**-3.7**	**-3.7**	**-3.9**
General government debt, % of GDP	**41.1**	**44.3**	**47.6**	**50.8**	**53.9**
External debt , % of GDP	**11.8**	**12.0**	**13.0**	**14.0**	**15.0**
Current account balance, % of GDP	**2.7**	**1.7**	**1.4**	**1.2**	**0.9**

INDIA

- **We expect growth to reach around 7% a year in 2018-2019**
- **The RBI will be watching inflation closely, but the budget deficit is expected to increase**
- **External financing needs will show an upward trend**

The economy has seen a sharp growth in recent years, underpinned by favourable trading conditions (relatively low energy prices) and a return to normal monsoon rains which has improved agricultural yields. We anticipate growth of around 7% a year in 2018-2019.

GDP and demand items



Source: Thomson Reuters Datastream

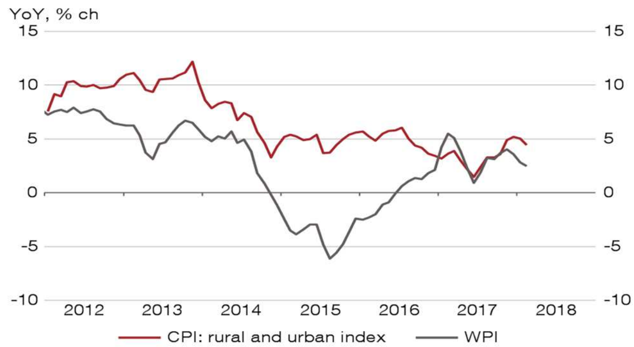
Private consumption, which was disrupted following demonetization in November 2016 (removal from circulation of all ₹500 and ₹1000 banknotes which caused a disruption in payments) is back on track again. Insofar as companies' capacity utilization is increasing, investment should also rebound, albeit moderately. Big companies are currently cleaning up their balance sheets following a period of high debt. The outlook is more favorable in the longer term: the ratification of a new law on bankruptcies and the bank recapitalization initiative announced at the end of 2017 should improve the quality of balance sheets and increase credit availability.

The RBI, which has made inflation the corner stone of its monetary policy framework, will increase interest rates if inflationary pressures arise. Long considered a factor of instability, inflation is currently at the low end of the RBI's target range of 2-6%. That said, food prices and the price of crude oil are already increasing.

The government plans to increase expenditure to upgrade infrastructure over the next five years and to increase subsidies and social security allowances to obtain support from electors, which will push up the public deficit. A general election is scheduled in April 2019.

India's external financing needs have decreased. Still, the country remains a net importer of energy resources. An increase in the oil price and momentum engendered by growth could cause an increase in the current account deficit.

Inflation rate



Source: Thomson Reuters Datastream

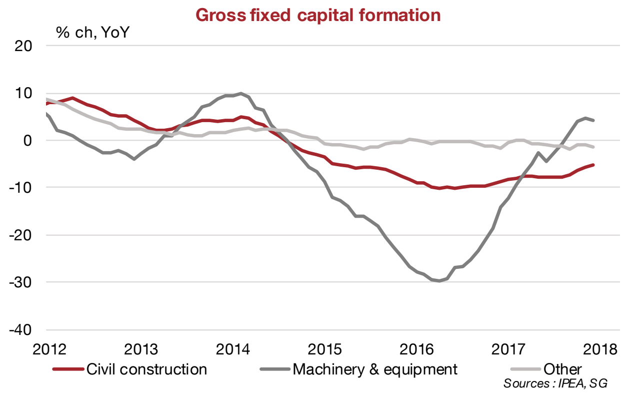
	2015	2016	2017	2018 (f)	2019 (f)
Real GDP, % ch (fiscal year)	**8.0**	**7.1**	**6.8**	**6.9**	**6.8**
Household consumption	6.1	8.1	7.2	7.0	6.9
Investment	6.5	7.9	7.5	7.5	7.3
Exports	-5.3	5.8	6.4	6.3	6.1
Imports	-5.9	5.3	10.2	8.5	6.5
Inflation rate, %	**6.0**	**4.5**	**4.6**	**4.7**	**4.8**
General government balance, % of GDP	**-7.1**	**-6.6**	**-6.4**	**-6.2**	**-5.9**
General government debt, % of GDP	**69.5**	**69.6**	**68.7**	**67.1**	**65.2**
External debt , % of GDP	**22.7**	**21.4**	**19.3**	**22.3**	**22.1**
Current account balance, % of GDP	**-1.1**	**-0.7**	**-1.4**	**-1.5**	**-1.6**

BRAZIL

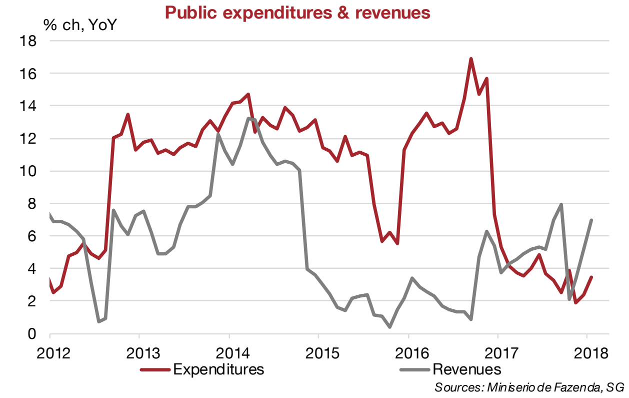
- **Activity is expected to continue its recovery trend, supported by consumption and exports**
- **Inflation is likely to remain moderate, enabling the BCB to keep monetary conditions loose**
- **The main risks are a strong deterioration of public finances increasing political noise**

The economic recovery remains modest. GDP expanded by just 0.1% QoQ in the Q4-17 (+2.1% YoY) reflecting mostly stagnating domestic consumption. Investment however gained momentum supported by growing expenditures on machinery & equipment.

All in all, the economy is expected to modestly accelerate in 2018. The progressive improvement of the labour market and looser monetary conditions will support consumption spending. Higher external demand and improving terms of trade will also strengthen the activity. Political uncertainties and corporate sector deleveraging will put a brake to the recovery of real investment .



The inflation outlook is still benign. Inflation stabilized at 2.8% YoY with food prices declining amid good crops. The price of other items with strong stickiness like services are also strongly decelerating. Inflation will slowly converge towards the 4.5% BCB target on the back of higher energy prices. In 2017, the BCB reduced its policy rate from 13% to 6.5%, its lowest level ever. Financial conditions are likely to remain supportive absent of strong pressures on the currency.



Albeit the slight improvement, the fiscal picture will remain a source of concern. The primary fiscal deficit diminished to 1.5% of GDP in January and debt has stabilized. However, this improvement looks only temporary. The ongoing recovery of public revenues reflects stronger activity, but it also reflects one-off revenues from public bank reimbursements to the Treasury and a tax renegotiating program from overseas non-reported assets. Without deeper structural reforms regarding mandatory expenditures. The cap on primary expenditure growth (based on past year inflation) is likely to be missed in 2019.

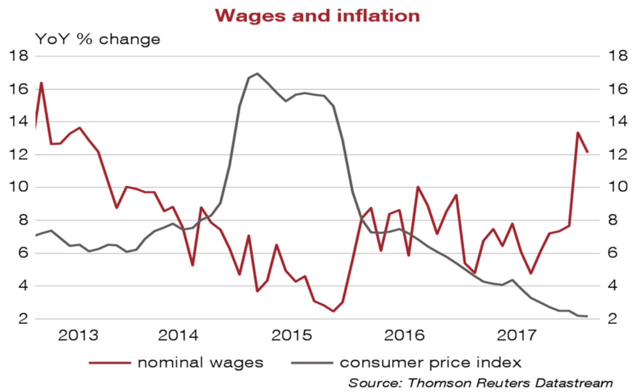
	2015	2016	2017	2018 (f)	2019 (f)
Real GDP, % ch	**-3.5**	**-3.5**	**1.0**	**2.0**	**2.5**
Household consumption	-3.2	-4.3	1.0	2.0	2.4
Public consumption	-1.4	-0.1	-0.6	-0.6	0.0
Investment	-13.9	-10.3	-1.8	4.7	6.0
Exports	6.8	1.9	5.2	4.0	3.8
Imports	-14.2	-10.2	5.0	3.5	4.0
Inflation rate, %	**9.5**	**8.0**	**3.7**	**4.0**	**4.5**
General government balance, % of GDP	**-10.3**	**-8.5**	**-7.5**	**-7.0**	**-6.0**
General government debt, % of GDP	**65.5**	**69.9**	**75.0**	**75.0**	**77.0**
External debt , % of GDP	**25.6**	**29.0**	**27.0**	**26.5**	**26.0**
Current account balance, % of GDP	**-3.3**	**-1.3**	**-0.5**	**-1.0**	**-1.5**

RUSSIA

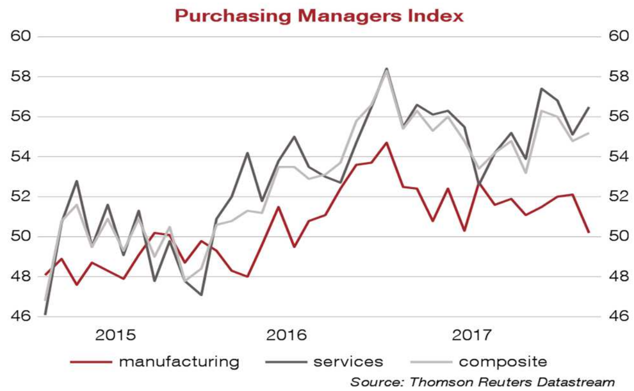
- **Growth will remain constrained by sluggish domestic demand in 2018-2019**
- **Despite some acceleration, inflation is set to remain moderate in the short term**
- **A decline in oil prices or new sanctions to the country could generate financial volatility**

Despite a favourable external environment and a rise in oil prices, growth in Russia is expected to remain below 2% in 2018-2019. Investment should continue to feature a modest expansion, amid a steady deterioration of corporate margins and slack lending to businesses.

Household consumption should nevertheless pick up due to an acceleration in real wage growth (+6% yoy in January 2018) in an environment of historically low unemployment (5.1% in December 2017) and declining active population. Exports, which grew sharply in 2017, are likely to benefit further from the strength of the European Union (which accounts for 40% of Russian exports) and Asia (30% of Russian exports, of which 11% relating to China).



On the supply side, industrial production remains weak, reflecting both the reduction in oil extraction following the agreement with OPEC and disappointing performances in the manufacturing and construction sectors. The import substitution campaign does not seem to be succeeding overall, although some specific sectors are holding up well (automotive, pharmaceutical, chemicals, plastic).



Public finances consolidated significantly in 2017 thanks to strong revenues (oil receipts, VAT). The fiscal policy is expected to remain restrictive in 2018-2019, the goal being to bring the budget deficit below 1% of GDP in 2019.

With inflation having fallen to levels not seen since the Soviet era, the Russian central bank reduced its key interest rate in December 2017 and again in February 2018. Now at 7.5%, the central bank is expected to further reduce its policy rate but will ensure that real interest rates remain positive to anchor inflationary expectations.

The economy is still exposed to financial volatility in the event of oil price downward fluctuations, a turnaround in emerging markets or additional sanctions.

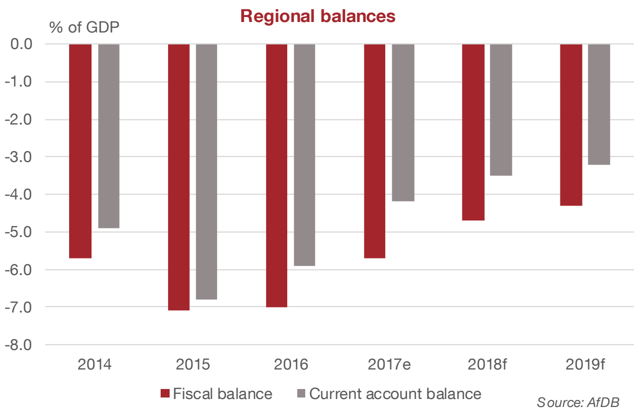
	2015	2016	2017	2018 (f)	2019 (f)
Real GDP, % ch	**-2,8**	**-0,2**	**1,5**	**1,2**	**1,2**
Household consumption	-9,8	-4,5	3,9	3,0	2,5
Investment	-9,9	-1,8	4,0	2,5	2,0
Exports	3,7	3,2	5,0	3,0	2,5
Imports	-25,9	-3,8	16,7	9,0	7,0
Inflation rate, %	**15,5**	**7,0**	**3,7**	**4,0**	**4,0**
General government balance, % of GDP	**-3,4**	**-3,7**	**-2,1**	**-1,5**	**-1,0**
General government debt, % of GDP	**15,9**	**15,6**	**17,4**	**17,7**	**18,2**
External debt , % of GDP	**38,0**	**40,0**	**35,9**	**35,0**	**34,6**
Current account balance, % of GDP	**5,0**	**2,0**	**2,8**	**3,2**	**3,6**

AFRICA

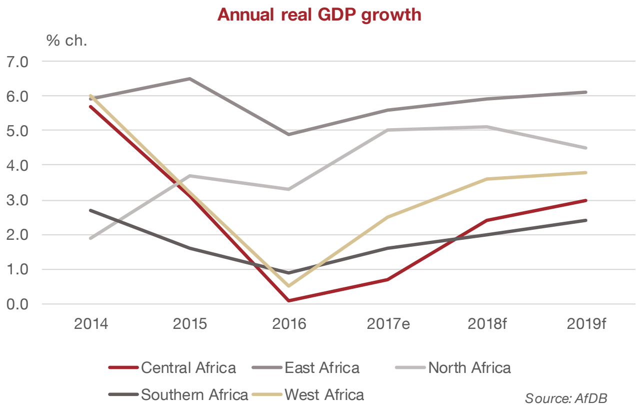
- **Regional growth is expected to continue accelerating in 2018 and 2019, above 4%**
- **Public and current account deficits are starting to be absorbed, but are still worrying factors**
- **Differences between countries (large/small, oil/non-oil producing, etc.) will persist**

The rebound in regional growth in Africa which began in 2017 is expected to continue, and growth is to rise above 4% in 2018 and 2019. This acceleration can be attributed to i) a more favourable international environment (rise in commodity prices, firmer growth in developed countries – the main export markets, continued interest by foreign investors), and ii) better weather conditions enabling an increase in agricultural output (which accounts for 20% of GDP and more than 50% of employment in Africa). Nevertheless, these growth levels are not enough to ensure a genuine pick-up in the region, not least because demographic growth remains high: average GDP per inhabitant in the region, which had fallen in 2016 and stagnated in 2017, is expected to grow only slightly in 2018 and 2019 (<1%/year).

Against this more favourable backdrop, financial imbalances (public and external) should continue to be gradually absorbed: the average budget deficit should decrease to 4/4.5% of GDP in 2018 and 2019, mainly because of significant fiscal adjustments in oil-producing countries and the rise in oil prices. The average current account deficit is expected to contract to around 3.5% of GDP in 2018 and 2019. Despite this slight (recent) improvement, debt levels (public and external) have increased rapidly and 30 African countries now have public debt above 50% (vs. only 15 countries in 2013).



Behind these broad trends, there continues to be significant differences between the different sub-regions, the different economic structures (oil producing and non-oil producing countries), the “small” and “large” countries, and so on.



In South Africa, growth is expected to remain at a slow pace (expected below 1.5%/year in 2018 and 2019), although J. Zuma's replacement by C. Ramaphosa as president has reassured investors (local and foreign) and could lead to a slight economic acceleration (due to more business-friendly and less erratic policies). The outlook for the rest of Sub-Saharan Africa continues to be split between oil-exporting and oil-importing countries. The growth rates for the former in 2018 and 2019, despite a slight rebound, are set to remain significantly below those in the period prior to 2014. These countries must continue to implement the adjustment policies already underway (Nigeria), combined in certain cases with the need/willingness to restructure part of their public debt (Angola, certain countries in the Central African CFA Franc region). By contrast, countries that benefit from a more diversified economic structure (Senegal, Ivory Coast, Ghana, Kenya) should continue to register growth rates above 5%.

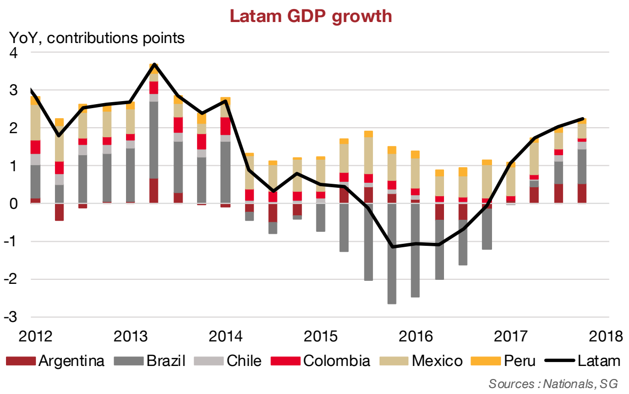
In North Africa, those countries that have begun (Egypt: reduction in energy subsidies) or are pursuing (Morocco: partial deregulation of its foreign exchange regime) macroeconomic reforms should continue to record an acceleration in growth. The outlook in Tunisia and Algeria is more uncertain: adjustments are still required to reduce their budget and external deficits and to speed up investment and growth; however, the capacity of both governments to achieve this is limited due to fragile social situations.

LATIN AMERICA

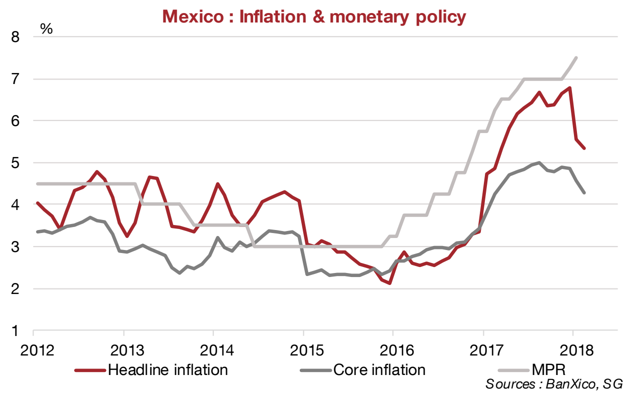
- **Favourable external tailwinds and looser monetary conditions will support regional growth**
- **In Mexico, the policy-mix is restrictive and political noise has increase (NAFTA, elections)**
- **The largest economies in the region are entering an electoral cycle**

After struggling with negative headwinds in 2015-2016, Latin American economies are on a recovery phase. The GDP growth rate of the region neared 2% at the end of 2017. Activity is set to accelerate in 2018 leaded by the economic recovery of Brazil, which is leaving behind a two-year long recession. A supportive domestic policy-mix and a favourable external environment —thanks to improving metal and oil prices along with stronger demand from Asia—are set to sustain capital expenditures in countries like Chile, Peru or Colombia.

Inflation has declined in most countries. In Brazil, Chile and Peru prices grow below the lower target band of Central banks. Monetary authorities will maintain ease financial conditions, favouring consumption and investment. In South America, inflation is likely to remain historically low, apart from Argentina, which suffers from still high-inflation inertia.

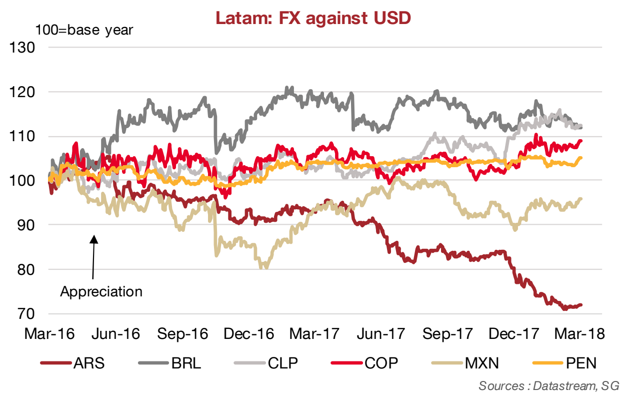


Unlike most South American countries, the economic outlook for Mexico is more challenging. Energy price deregulation pushed inflation up from 2% to 7%, and prompted a strong monetary tightening Increasing uncertainties regarding the NAFTA renegotiations along with July General Elections are also generating financial volatility. Such environment may push the Banco de Mexico to keep tight monetary conditions. The government is on fiscal consolidation trend while PEMEX has announced further expenditures cuts. The economy will benefit from export dynamism but the policy mix is likely to constrain both consumption and investment.



Risks to the outlook are related to the commodity cycle, as the region is dependent on primary exports and the terms of trade evolution. Should US monetary policy increase interest rates further than what markets expect, central banks could be forced to tightening their policies faster than expected.

The region is also on an electoral cycle that could potentially translate into market volatility. In Colombia, the main uncertainties ahead of May 2018 presidential elections are related to the future implementation of the peace treaty between the government and FARC. Mexico will also organize general elections (July 2018) amid increasing political tensions with the US and a rejection of traditional political parties. In Brazil, general elections are scheduled for October 2018. For the moment, markets are pricing that the new president will manage to form a stable coalition capable of implementing a fiscal consolidation plan. Yet, rejection of political class is high among the electorate and, for now, parties have not announced their final candidates.

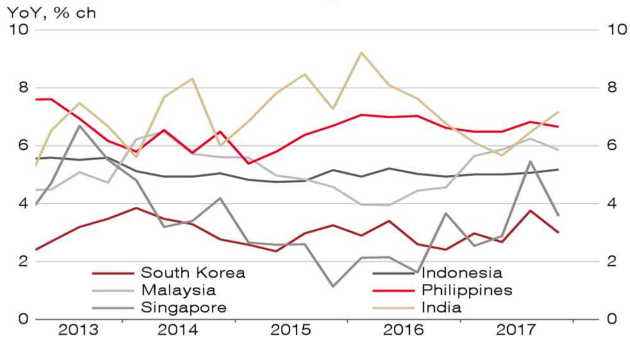


EMERGING ASIA

- **Trade expansion helped firm the outlook for Emerging Asia, growth expected at 6% in 2018-19**
- **The external positions of Emerging Asian economies will remain robust**
- **Given its strong integration to global value chains, Asia would be hardly hit by a “trade war”**

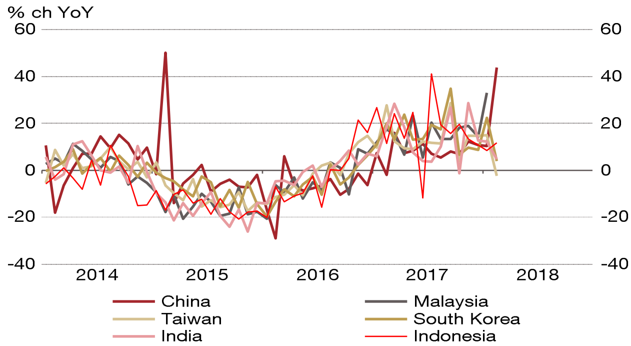
Emerging Asia will grow at around 6% over 2018–19 at broadly the same pace as in 2017. The region continues to account for over half of world growth and it keeps growing at a faster pace than other emerging markets. Strong growth in the United States, Euro zone, Japan will continue supporting exports across most of emerging Asia. Regional growth is also expanding with robust growth in China.

Quarterly GDP



Source: Thomson Reuters Datastream

Value of exports in USD



Source: Thomson Reuters Datastream

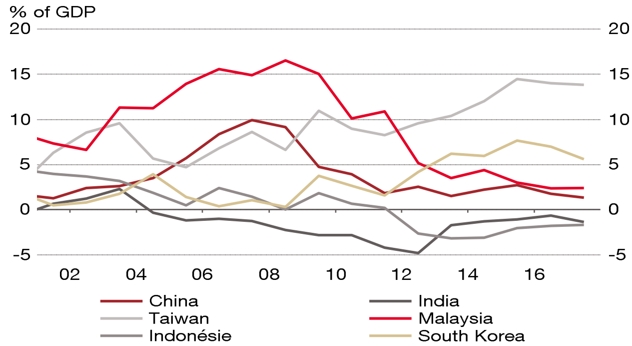
A commitment to growth targets and the recovery in the world economy is supporting momentum in China, but the economy should slow down as the country pursues a transition to a more sustainable growth path.

In India, a cyclical growth recovery has gone hand in hand with continued fiscal consolidation and an anti-inflationary monetary policy that have underpinned macroeconomic stability. In the medium term, large fiscal deficits, supply bottlenecks and structural impediments remain the main constraints to growth.

In South Korea, growth surged in 2017 boosted by a jump in exports and a strong expansion in investment. The current account surplus is narrowing but is expected to remain large above 5% in the medium term. However, unfavourable demographics are expected to lower GDP growth on the long run.

South East Asia benefits from strengthening global demand. Going forward, robust domestic private spending and the implementation of planned infrastructure initiatives will support growth around 5% on the medium term.

Current account balance



Source: Thomson Reuters Datastream

The external positions of Emerging Asian economies are generally robust and most countries will continue running current account surpluses. The exceptions are India and Indonesia, but in both countries the current account deficit is expected to remain contained.

Risks to the growth outlook in emerging Asia are related to the possibility of more rapid monetary policy normalization, which could trigger capital outflows from the region and potentially create liquidity constraints for overindebted corporates. The scale of Emerging Asia’s international reserves provides however considerable buffers. the expansion of trade restrictions.

A greater risk is related to a rise in protectionism. Of all the regions, Asia would be the most vulnerable to a trade war and rising tariffs. Even if they were applied to a single market (i.e. China), the adverse impact would spread out across the Asia region via regional trade linkages and the integration of global value chains.

GULF COUNTRIES

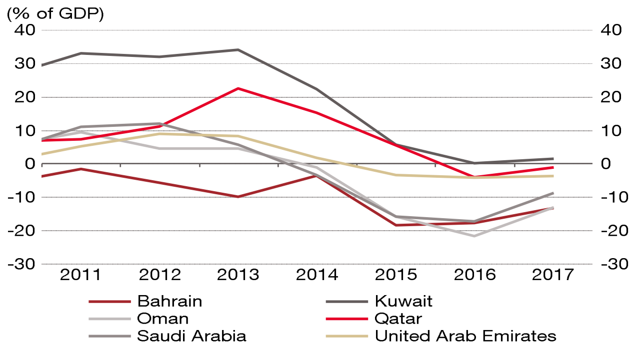
- **The rise in oil prices will enable a recovery in public finances and growth**
- **The gradual introduction of VAT and reduction in subsidies will push up inflation**
- **The fundamentals are improving but the budget deficits of Bahrain and Oman remain high**

The extension of the OPEC+ agreement to limit oil production has helped to support oil prices. The oil price was at USD 70/b in March 2018, 60% higher than the average in 2016. While higher oil prices enable a recovery in both export and public revenues, the need to pursue budgetary adjustments to return to a sustainable trajectory will continue to weigh on the growth outlook in the medium term. Domestic demand should strengthen in the short term but non-oil GDP growth will remain below the average expansion of 7.5% recorded in the period 2003-2014.

Inflation is set to increase due to the reduction of fuel subsidies on the local market and the introduction of a VAT rate of 5% in Saudi Arabia and the UAE at the start of 2018, and probably in the other Gulf countries in 2019.

The budget deficit of the Gulf countries is likely to decrease gradually from an average of 9% of GDP in 2017 to 5% of GDP by 2020. Sovereign bond issuance on the international markets (USD40bn in 2016 and USD60bn in 2017) should remain strong in 2018 and 2019.

Budget balance

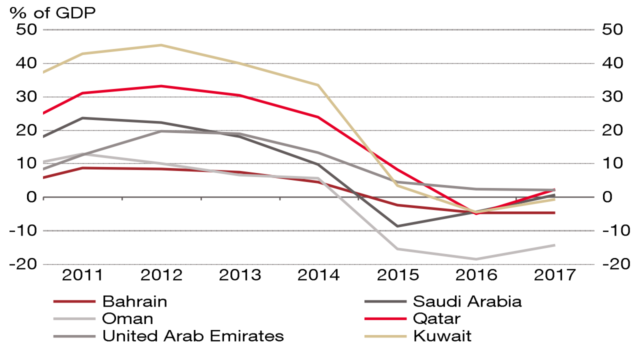


Source: Thomson Reuters Datastream

The broad improvement in current accounts should ensure that the currency pegs against the dollar will remain in place. Nevertheless, Bahrain continues to face significant vulnerabilities, with a large budget deficit and an increase in its public debt ratios in 2017. Its monetary stability will depend on continued financial support from its allies, Saudi Arabia and the United Arab Emirates.

In Oman, the state is implementing infrastructure projects and initiatives to support employment for nationals, which will keep its public deficits high. At present, the markets are easily absorbing the country's external debt issuance. The current account deficit will also remain very high. The minimum oil price to balance the budget and the current account in the sultanate is USD80/b. In the event of pressure on liquidity, Oman can always mobilize its sovereign funds.

Current account balance

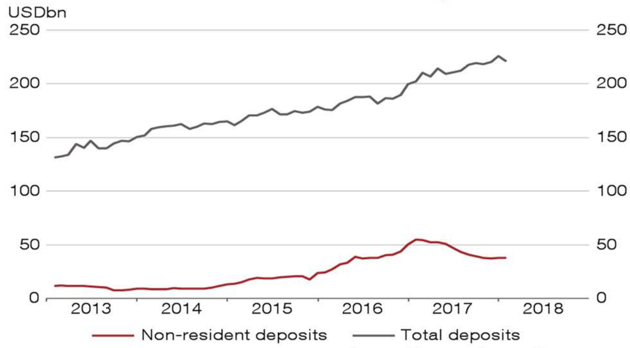


Source: Thomson Reuters Datastream

There is a growing perception among GCC on the need to diversify the economy away from oil resources. In Saudi Arabia, the authorities have launched a vast reform program (new law on bankruptcies and greater openness to foreign investors) with a view to improving the business environment and promoting growth that will create more jobs. The United Arab Emirates are also trying to foster export complexity.

Regarding political tensions among Gulf countries, Qatar could resist the blockade by other states in the region thanks to new commercial routes for imported goods. The authorities responded to the capital outflows of non-residents by using the sovereign fund to provide liquidity and guarantee financial stability. Nevertheless, the political crisis in the region is not over, and this remains a factor of uncertainty.

Qatari commercial banks - deposits



Source: Thomson Reuters Datastream

CENTRAL AND EASTERN EUROPE

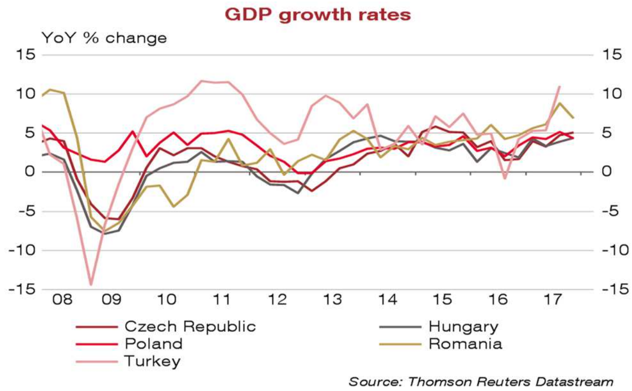
- **GDP growth should remain well-oriented in CEE driven by both domestic and external demand**
- **With inflation rising, a more restrictive monetary policy stance is to expect**
- **Romania posts twin deficits and show signs of overheating**

After the 2017 acceleration, GDP growth should remain well-oriented in CEE in 2018. The expansion could however moderate in 2019 against the backdrop of a less supportive external environment and more restrictive domestic monetary policies.

Private consumption could slightly decelerate as inflation erodes households' purchasing power in 2018-2019. It will however remain a key driver of growth, supported by improving labour markets. Unemployment rates have been decreasing sharply in the region and recent industry surveys suggest that labour shortages have increased.

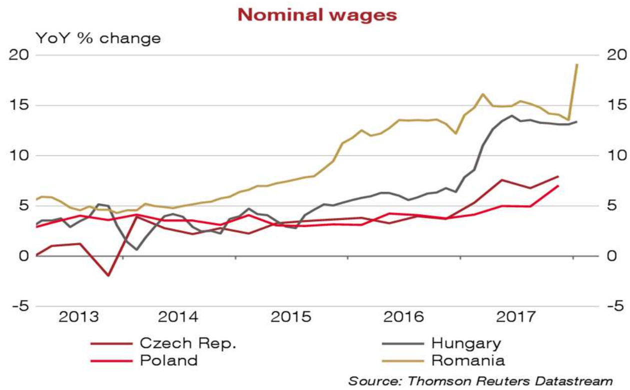
After the 2016 decline, investment has started to recover in 2017 and should accelerate in 2018 thanks to the utilization of EU structural funds, which could lead to a specific boost in the construction sector. Expansionary fiscal policies (especially in Romania and Hungary) will also sustain demand.

Exports should remain strong in 2018 supported by the dynamism of the Euro area and the strong integration of CEE in global value chains (particularly in the car industry and in electronics). They will however moderate in 2019 as the Euro area is expected to lose momentum.

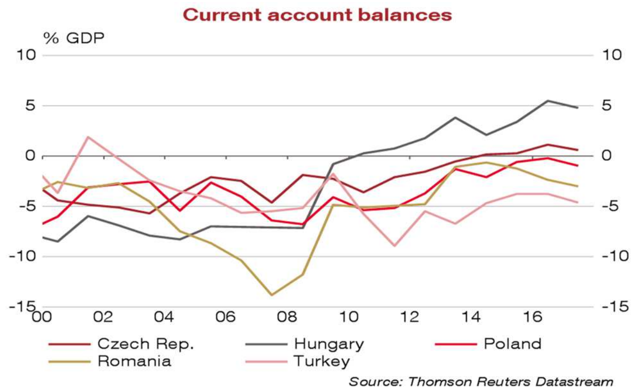


This strong growth momentum in CEE is well-balanced. Debt levels have been decreasing in the region and external financial situations have generally improved. However, inflationary pressures are looming in the region, mainly driven by demand pressures. Wages have surged since the beginning of the year, outstripping productivity growth in Romania, Hungary and Bulgaria.

Up to now, only the Czech National Bank and the Romanian National Bank have started to increase policy rates. But Further rate hikes are likely to be discussed in 2018, especially in Poland, Czech Republic and Romania.

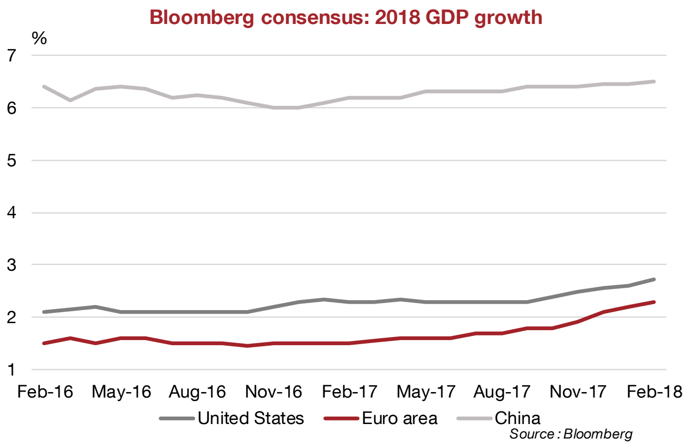


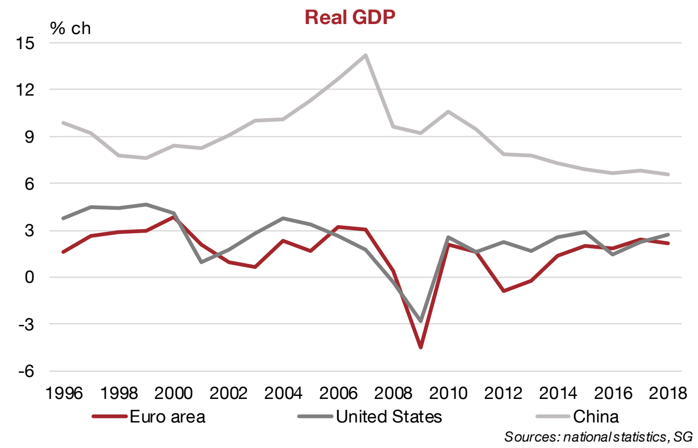
Looking forward, overheating risks could appear in some countries. Romania is the most concerned with a consumption boom and a deterioration in both the fiscal and current account balances.



Following the recovery and double-digit growth figures in Q3 2017, Turkey's economy also faces signs of overheating: a positive output gap, inflation well above target and a wider current account deficit. Favourable external conditions will continue supporting exports, but external financing needs will remain large, exposing Turkey to changes in global financial conditions.

Economic Data

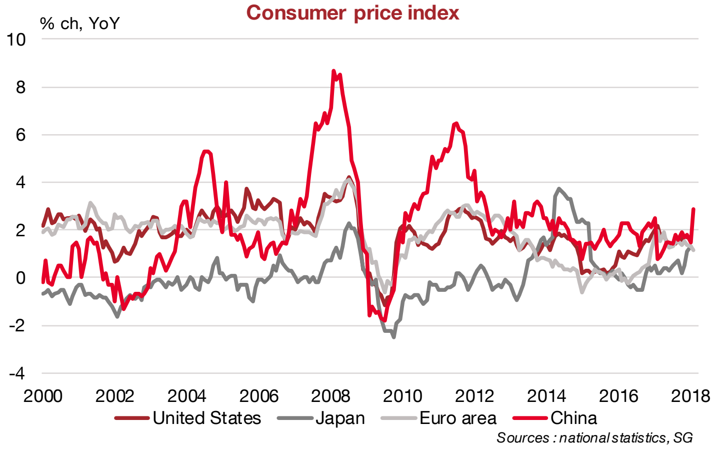




	2010	2011	2012	2013	2014	2015	2016	2017	2018(f)	2019(f)	2020 (f)	2021(f)	2022(f)
Real GDP, % ch													
World	**4.2**	**3.2**	**2.5**	**2.7**	**2.9**	**2.9**	**2.6**	**3.3**	**3.3**	**3.1**	**2.8**	**2.6**	**2.6**
United States	2.5	1.6	2.2	1.7	2.6	2.9	1.5	2.3	2.9	2.4	1.5	1.0	1.0
Japan	4.2	-0.1	1.5	2.0	0.3	1.4	0.9	1.7	1.4	1.0	0.7	0.4	0.8
United Kingdom	1.7	1.5	1.5	2.1	3.1	2.3	1.9	1.7	1.5	1.3	1.4	1.5	1.6
Euro area	2.0	1.7	-0.8	-0.2	1.4	2.0	1.8	2.5	2.2	1.7	1.5	1.4	1.4
Germany	3.9	3.7	0.7	0.6	1.9	1.5	1.9	2.5	2.1	1.9	1.6	1.5	1.5
France	1.9	2.1	0.2	0.6	1.0	1.0	1.1	2.0	2.0	1.7	1.5	1.5	1.5
Italy	1.6	0.7	-2.9	-1.7	0.2	0.8	1.0	1.5	1.4	1.1	1.0	0.9	0.9
Spain	0.0	-1.0	-2.9	-1.7	1.4	3.4	3.3	3.1	2.6	2.1	1.8	1.6	1.6
China	10.6	9.5	7.9	7.8	7.3	6.9	6.7	6.9	6.4	6.0	5.7	5.4	5.2
India	10.3	6.6	5.5	6.4	7.5	8.0	7.1	6.8	6.9	6.8	6.2	5.9	5.7
Brazil	7.5	4.0	1.9	3.0	0.5	-3.5	-3.5	1.0	2.0	2.5	2.5	2.5	2.5
Russia	4.5	5.1	3.7	1.8	0.7	-2.8	-0.2	1.5	1.2	1.2	1.5	1.5	1.5
Real investment, % ch													
World*	**3.9**	**4.7**	**2.8**	**2.6**	**3.3**	**2.7**	**3.3**	**3.4**	**3.4**	**2.9**	**1.6**	**1.6**	**1.3**
United States	2.0	3.0	2.6	1.8	3.5	3.4	2.2	3.0	3.8	2.8	1.7	1.1	1.0
Japan	-1.6	1.7	3.5	5.0	2.9	1.8	1.1	3.9	1.5	0.6	0.8	1.4	0.4
United Kingdom	4.5	2.2	2.1	3.4	7.1	2.8	1.8	3.9	2.0	0.6	2.1	2.9	1.7
Euro area	-0.5	1.6	-3.3	-2.4	1.9	3.0	4.5	3.1	2.8	2.4	2.1	2.1	2.1
Germany	5.0	7.4	-0.1	-1.2	3.7	1.0	2.9	3.9	2.2	2.2	2.2	2.2	2.2
France	1.8	2.2	0.3	-0.7	0.0	0.9	2.7	3.8	3.1	2.1	1.8	1.8	1.7
Italy	-0.6	-1.7	-9.4	-6.6	-2.2	1.9	3.3	3.9	4.5	1.8	1.6	1.6	1.6
Spain	-4.9	-6.9	-8.6	-3.4	4.7	6.5	3.3	5.0	3.8	3.5	2.6	2.2	2.2
China	7.1	9.1	7.2	6.2	6.4	6.2	6.4	5.0	4.7	4.5	1.1	1.1	0.7
India	15.2	11.5	2.4	2.5	1.9	6.5	7.9	7.5	7.5	7.3	7.0	6.8	6.5
Brazil	17.9	6.8	0.8	5.8	-4.2	-13.9	-10.3	-1.8	4.7	6.0	3.5	4.0	4.0
Russia	6.4	9.2	5.9	1.3	-2.7	-13.4	1.4	4.0	2.5	2.0	2.0	2.0	2.0

Sources: Datastream, IMF, OECD, SG computations and forecasts
* Weighted average of the 11 countries shown here

Economic Data

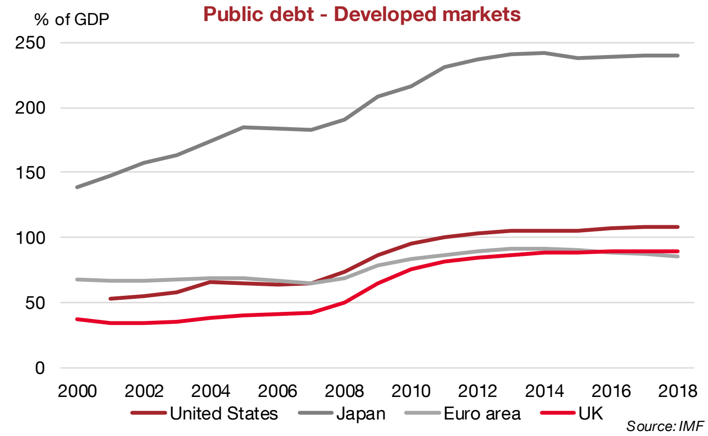


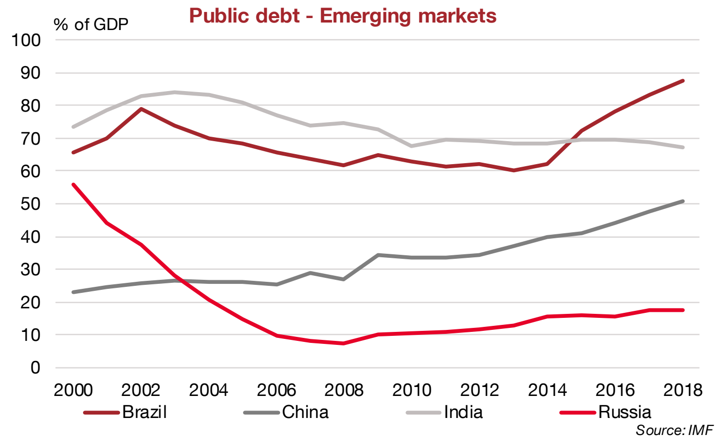
	2010	2011	2012	2013	2014	2015	2016	2017	2018(f)	2019(f)	2020 (f)	2021(f)	2022(f)
Fiscal balance, % GDP													
United States	-12.2	-10.7	-9.0	-5.5	-4.9	-4.3	-5.0	-4.7	-6.0	-6.8	-6.9	-6.6	-6.4
Japan	-9.1	-9.1	-8.3	-7.6	-5.4	-3.5	-4.2	-4.1	-3.8	-3.0	-2.8	-2.8	-2.8
United Kingdom	-9.4	-7.5	-8.2	-5.4	-5.5	-4.3	-2.9	-2.2	-2.3	-3.1	-3.0	-3.0	-2.9
Euro area	-6.2	-4.2	-3.6	-3.0	-2.6	-2.1	-1.5	-1.1	-1.0	-1.0	-0.7	-0.7	-0.6
Germany	-4.2	-1.0	0.0	-0.2	0.3	0.7	0.8	0.9	1.0	1.0	1.0	1.0	1.0
France	-6.8	-5.1	-4.8	-4.0	-3.9	-3.6	-3.4	-2.6	-2.4	-2.9	-2.0	-1.8	-1.6
Italy	-4.2	-3.7	-2.9	-2.9	-3.0	-2.6	-2.5	-2.2	-2.4	-2.4	-2.2	-2.2	-2.2
Spain	-9.4	-9.6	-10.5	-7.0	-6.0	-5.3	-4.5	-3.1	-2.4	-1.9	-1.6	-1.4	-1.2
China	-0.4	-0.1	-0.3	-0.8	-0.9	-2.8	-3.7	-3.7	-3.7	-3.9	-4.0	-4.1	-4.2
India	-8.6	-8.3	-7.6	-7.0	-7.2	-7.1	-6.6	-6.4	-6.2	-5.9	-5.8	-5.6	-5.4
Brazil	-2.7	-2.5	-2.5	-3.0	-5.4	-10.3	-8.5	-7.5	-7.0	-6.0	-5.5	-5.0	-4.8
Russia	-3.2	1.4	0.4	-1.2	-1.1	-3.4	-3.7	-2.1	-1.5	-1.0	-0.5	0.3	0.5
Public debt*, % GDP													
United States	89	94	99	101	102	101	105	104	104	106	109	115	119
Japan	184	200	206	210	215	215	218	221	223	224	222	221	220
United Kingdom	76	81	85	86	87	88	88	90	89	90	91	92	92
Euro area	84	86	90	92	92	90	89	87	85	83	81	80	78
Germany	81	79	80	77	75	71	68	65	61	58	55	53	50
France	82	85	90	92	95	96	97	97	97	97	96	95	93
Italy	115	117	123	129	132	132	132	131	130	129	128	127	127
Spain	60	70	86	96	100	99	99	98	97	95	94	92	91
China	34	34	34	37	40	41	44	48	51	54	57	60	62
India	67	70	69	69	69	70	70	69	67	65	63	61	60
Brazil	63	61	62	60	62	65	70	75	75	77	79	79	78
Russia	11	11	12	13	16	16	16	17	18	18	18	18	18

Sources: Datastream, IMF, SG computations and forecasts

* BRIC: source IMF; Developed countries: national sources (Maastricht methodology for EU countries)

Economic Data





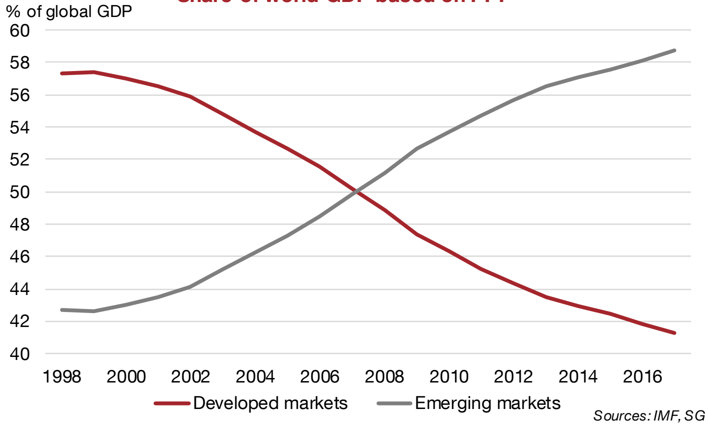
	2010	2011	2012	2013	2014	2015	2016	2017	2018(f)	2019(f)	2020 (f)	2021(f)	2022(f)
Inflation, %													
World*	**2.4**	**3.8**	**2.7**	**2.4**	**2.2**	**1.4**	**1.6**	**2.1**	**2.3**	**2.6**	**2.4**	**1.9**	**2.0**
United States	1.6	3.1	2.1	1.5	1.6	0.1	1.3	2.1	2.2	2.5	1.9	0.7	1.2
Japan	-0.7	-0.3	-0.1	0.3	2.8	0.8	-0.1	0.4	0.8	1.3	1.7	1.0	1.0
United Kingdom	3.3	4.5	2.8	2.6	1.5	0.0	0.7	2.6	2.5	2.3	2.1	2.0	1.9
Euro area	1.6	2.7	2.5	1.4	0.4	0.0	0.2	1.5	1.3	1.8	1.7	1.7	1.6
Germany	1.1	2.1	2.0	1.5	0.9	0.2	0.5	1.7	1.6	1.8	1.7	1.7	1.7
France	1.6	2.2	1.9	0.8	0.4	0.1	0.2	1.0	1.4	1.6	1.8	1.9	1.9
Italy	1.6	2.9	3.3	1.2	0.2	0.1	-0.1	1.3	1.3	1.5	1.4	1.2	1.3
Spain	2.9	2.4	2.5	0.4	-0.5	-0.6	1.4	1.4	1.4	1.9	1.8	1.7	1.7
China	3.3	5.4	2.6	2.6	2.0	1.4	2.0	1.8	2.4	2.5	2.6	2.6	2.6
India	9.5	9.5	10.0	9.4	5.8	4.9	4.5	3.5	4.7	4.8	4.9	5.0	5.0
Brazil	5.0	6.6	5.4	6.2	6.3	9.5	8.0	3.7	4.0	4.5	4.5	4.5	4.5
Russia	6.9	8.4	5.1	6.8	7.8	15.5	7.0	3.7	4.0	4.0	4.0	4.0	4.0
Current account balance, % of GDP													
United States	-2.9	-2.9	-2.6	-2.1	-2.1	-2.4	-2.4	-2.3	-2.9	-3.9	-4.7	-4.4	-4.0
Japan	3.9	2.1	1.0	0.9	0.8	3.0	3.7	4.0	4.0	4.0	3.9	3.9	3.8
United Kingdom	-3.8	-2.4	-4.3	-5.6	-5.4	-5.2	-5.7	-4.7	-5.5	-5.9	-5.6	-5.1	-4.8
Euro area	-0.1	-0.1	1.4	2.2	2.4	3.2	3.4	3.5	2.9	3.0	3.0	3.0	3.0
Germany	5.4	6.0	7.1	6.8	7.5	8.6	8.2	7.9	7.7	7.7	7.7	7.6	7.5
France	-0.8	-1.0	-1.2	-0.9	-1.3	-0.4	-0.9	-1.6	-1.5	-1.5	-1.6	-1.7	-1.7
Italy	-3.4	-3.0	-0.3	1.0	1.9	1.5	2.7	2.9	3.0	2.9	2.8	2.7	2.6
Spain	-3.9	-3.2	-0.2	1.5	1.1	1.1	1.9	1.7	1.8	2.0	2.2	2.2	2.3
China	3.9	1.8	2.5	1.5	2.2	2.7	1.7	1.4	1.2	0.9	0.7	0.4	0.2
India	-2.8	-4.2	-4.8	-1.7	-1.3	-1.1	-0.7	-1.4	-1.5	-1.6	-1.8	-2.0	-2.4
Brazil	-3.4	-2.9	-3.0	-3.0	-4.2	-3.3	-1.3	-0.5	-1.0	-1.5	-2.0	-2.0	-2.0
Russia	4.1	4.7	3.2	1.5	2.8	5.0	2.0	2.8	3.2	3.6	3.8	3.9	4.0

Sources: Datastream, IMF, SG computations and forecasts

* Weighted average of the 11 countries shown here

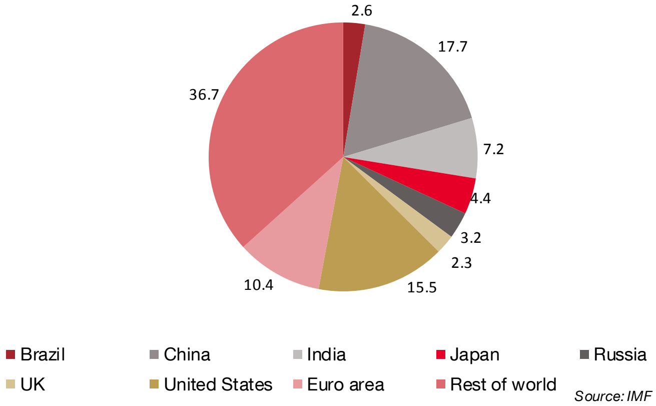
Structural Data

Share of world GDP based on PPP



Sources: IMF, SG

Share in world GDP based on PPP



Source: IMF

As of 2016	GDP in $ (USDbn)	GDP p. capita ($, at PPP)	Population (Millions)	Credit (% GDP)*	International investment position, net** (% GDP)	Openness ratio***
United States	18 624	57 608	323	151	-45	20
Euro area	11 923	37 071	341	163	-7	67
Germany	3 479	48 449	82	106	52	69
France	2 466	42 336	65	189	-15	44
Italy	1 851	36 823	61	115	-9	47
Spain	1 233	36 347	46	166	-80	49
Netherlands	778	51 249	17	231	64	139
China	11 232	15 395	1 383	211	16	33
Japan	4 937	41 220	127	158	61	25
United Kingdom	2 629	42 421	66	170	-4	40
India	2 264	6 694	1 300	57	-16	28
Brazil	1 799	15 238	206	66	-34	18
Canada	1 530	46 441	36	212	10	53
South Korea	1 411	37 730	51	193	18	64
Russia	1 283	26 926	143	67	17	37
Australia	1 262	48 712	24	203	-59	32
Mexico	1 047	18 935	122	43	-44	74
Indonesia	932	11 717	259	41	-36	30
Turkey	863	24 986	80	85	-53	40
Switzerland	669	60 374	8	238	115	86
Saudi Arabia	646	55 331	32	65	92	49

Sources: World Bank, BIS, IMF, Datastream

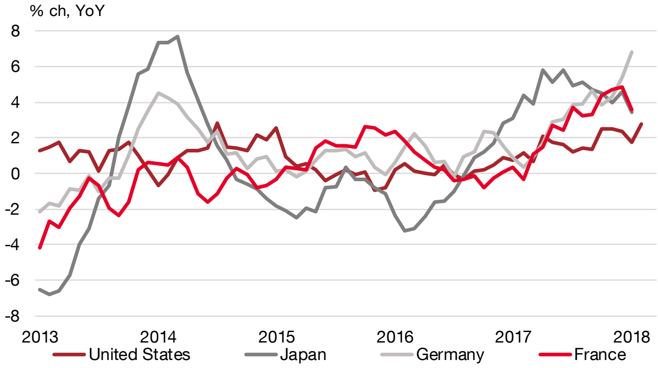
*Bank loans and debt securities of the non financial private sector

** Total external financial assets minus total external liabilities

*** Sum of imports and exports, divided by GDP

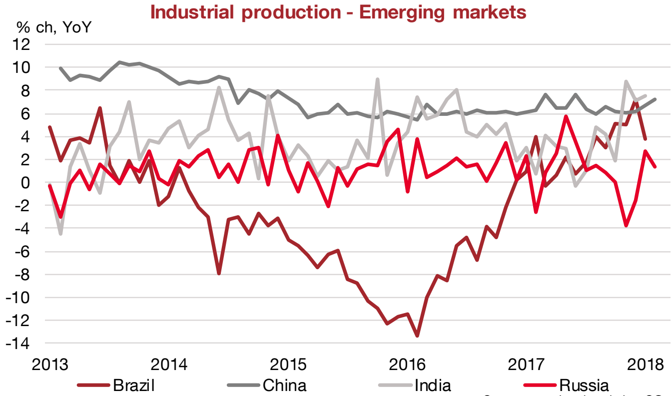
Cyclical Data

Industrial production - Developed markets



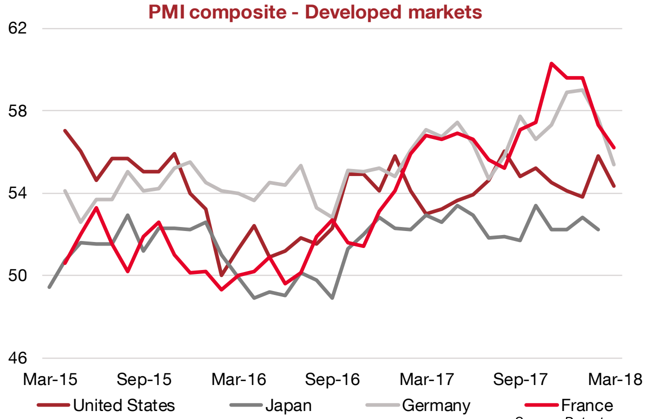
Sources: national statistics, SG

Industrial production - Emerging markets



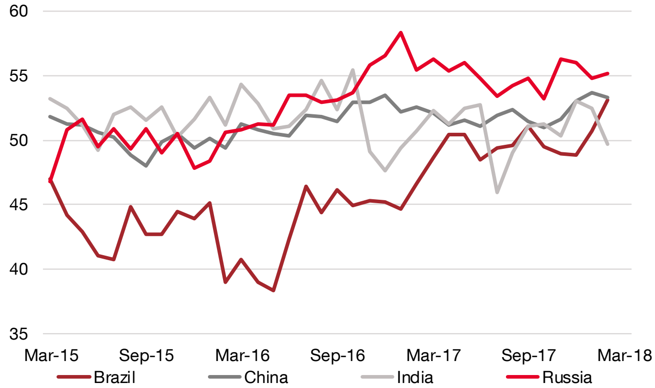
Sources: national statistics, SG

PMI composite - Developed markets



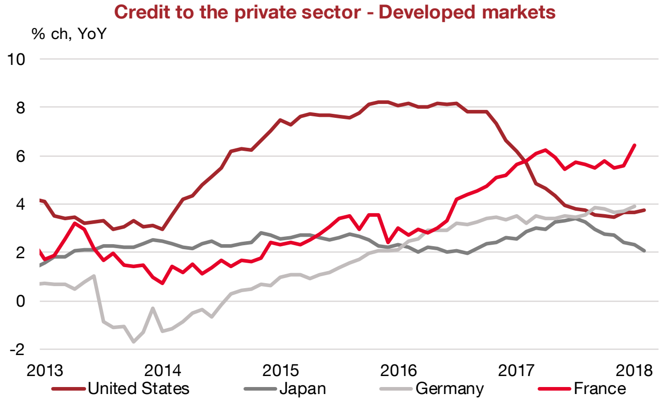
Source: Datastream

PMI composite - Emerging markets



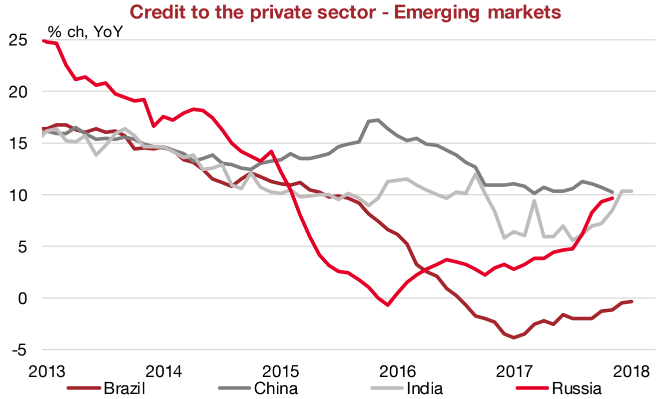
Source: Datastream

Credit to the private sector - Developed markets



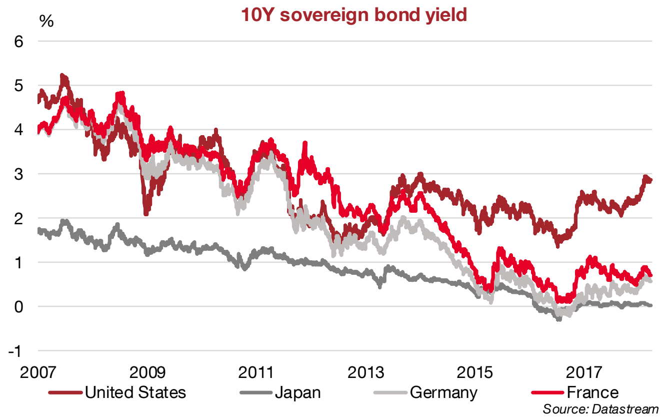
Sources: national statistics, SG

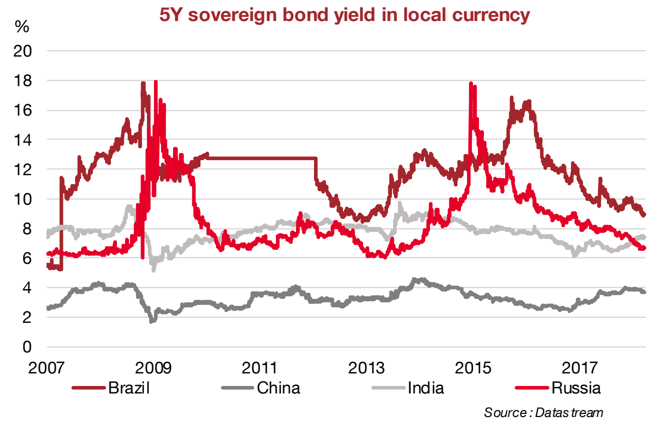
Credit to the private sector - Emerging markets

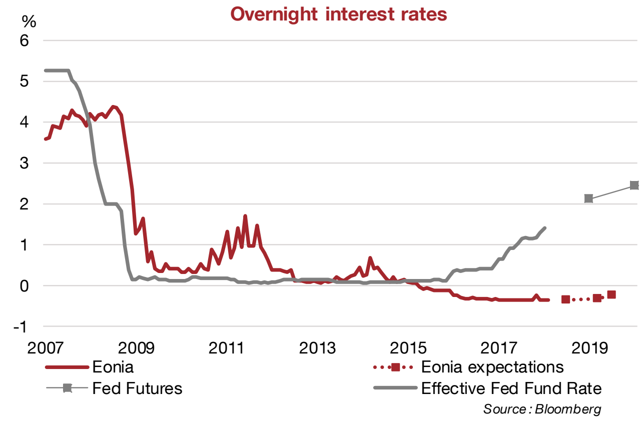


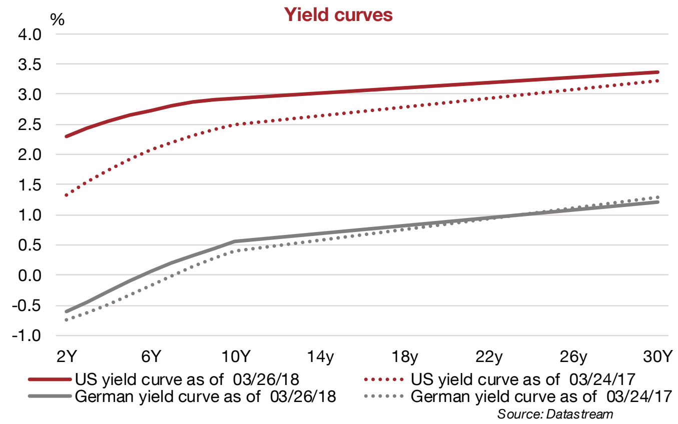
Sources: national statistics, SG

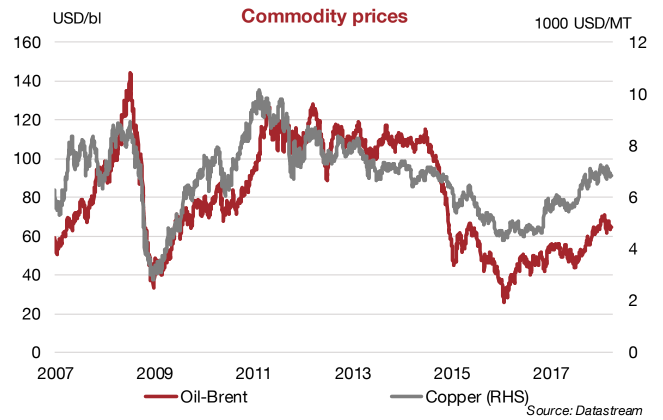
Financial Data

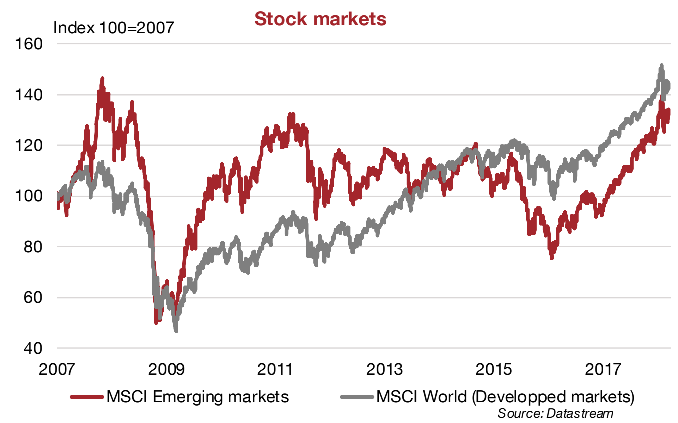






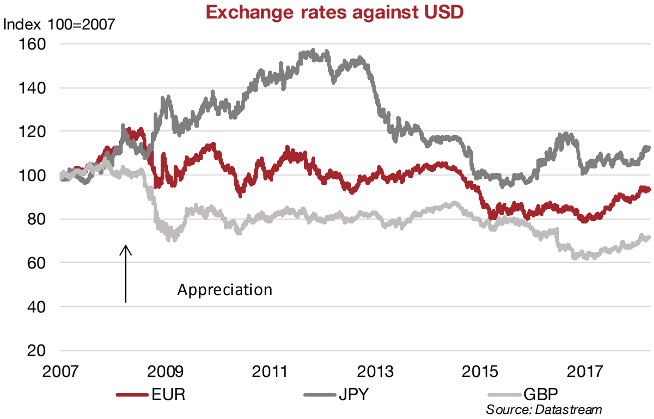




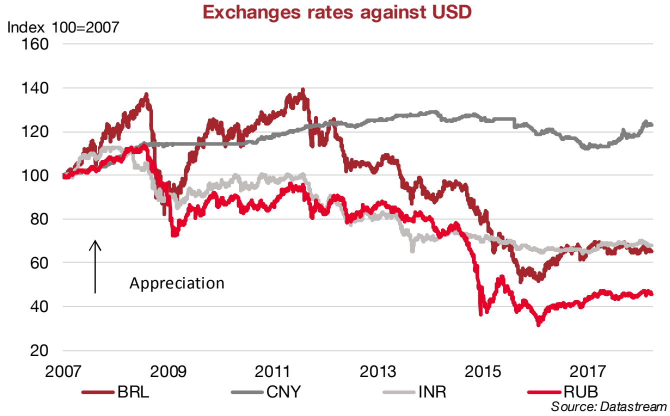


Financial Data

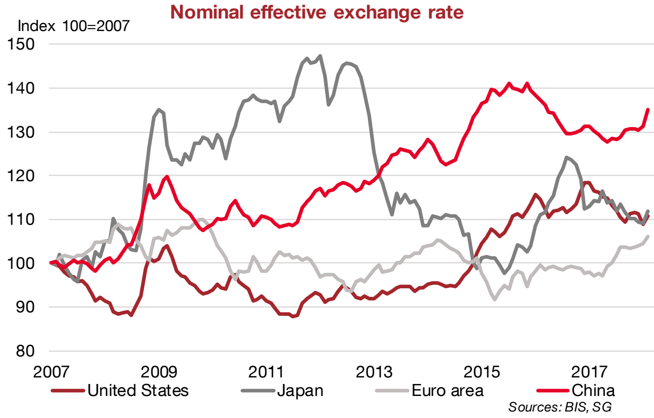
Exchange rates against USD



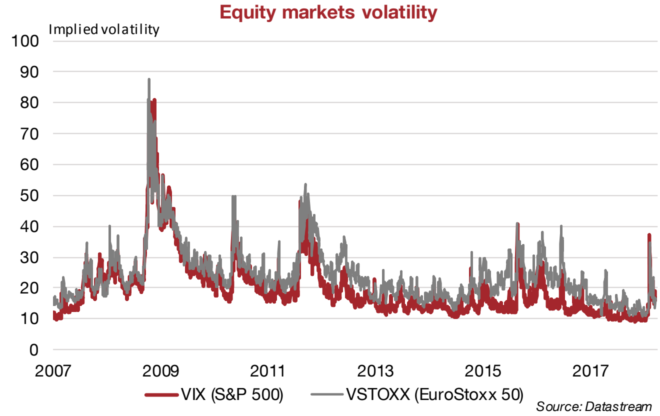
Exchanges rates against USD



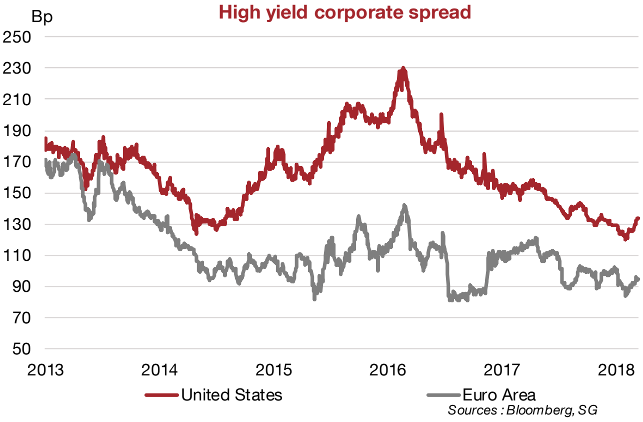
Nominal effective exchange rate



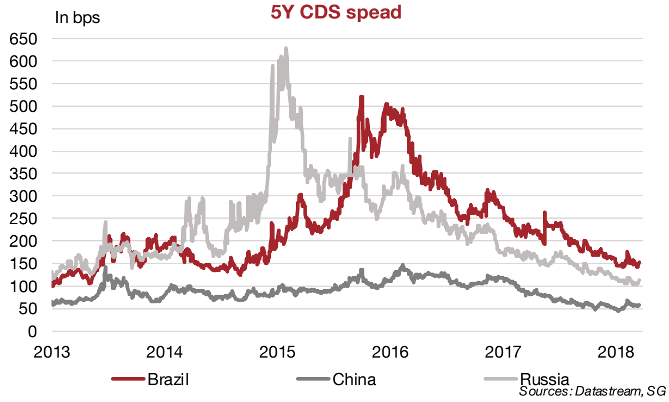
Equity markets volatility



High yield corporate spread



5Y CDS spead



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