Germany

German consumers remain confident and drive growth

In Germany, activity gathered pace in Q1 2017 (+0.6% after +0.4% in late 2016), buoyed by more dynamic construction investment in particular. Activity should slow very slightly in Q2 (+0.5%). In H2, household purchasing power should remain robust and activity should remain vigorous (+0.5% per quarter), driven once again by domestic demand. On average over the year, growth is expected to remain steady in 2017 (+1.9%, after +1.8% in 2016).

Construction investment boosted growth in Q1

Activity in Germany gathered pace in Q1 2017 (+0.6% after +0.4%). Aided by mild temperatures in February and March, construction investment gained momentum (+2.3% after +0.8%). In reaction, it is expected to slip back in Q2 (–0.5%) and activity is likely to slow a little (+0.5%). It should then increase steadily in H2 (+0.6% per quarter), in line with the sharp rise in building permits issued recently. On average over the year, this investment is expected to remain sustained (+2.6% after +2.5%). As the business climate is very positive in industry, investment in capital goods is likely to pick up in 2017 (+1.9% as an annual average, after +0.9%).

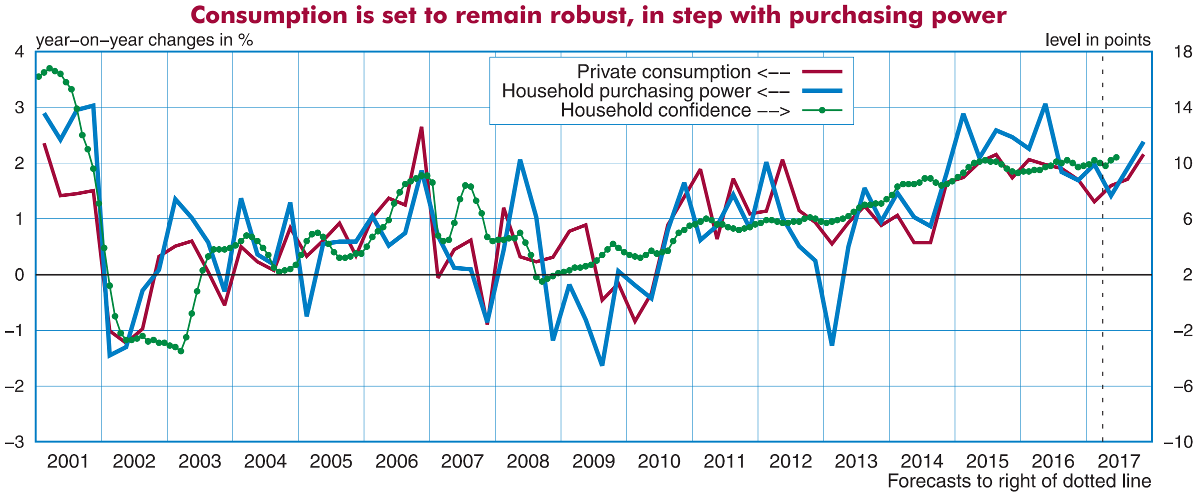
Private consumption should provide solid support for growth

In Q1 2017 German household expenditure rose only very slightly (+0.3% after +0.2%). Employment is set to remain dynamic in 2017 (+1.6% as an annual average, after +1.2%), which should allow the job market integration of refugees. Consequently, the unemployment rate should level out at a very low level in 2017 (around 3.7%). With the rise in the minimum wage on 1st January 2017 and a very low unemployment rate, wages are expected to increase a little faster in 2017 than in 2016 (+2.6% after +2.5%). As a result, German household purchasing power in 2017 should decline less (+1.9% after +2.2%) than elsewhere in Europe. Given the high level of household confidence, household consumption is likely to rise through to the end of the year (+0.6% per quarter, *Graph*), showing resilience on average over the year (+1.7% after +1.9%). Government consumption should continue to rise steadily through to the end of the year (+0.5% per quarter). All in all, thanks to robust domestic demand, GDP is expected to rise by 0.5% per quarter in H2. As an annual average, it is expected to grow by 1.9% in 2017, after +1.8% in 2016.

Foreign trade is set to make a neutral contribution to growth in 2017

In Q1, exports were buoyant once again (+1.3% after +1.7%) whereas imports slowed significantly, taking the contribution of foreign trade to growth up to +0.4 points (after –0.2 points). In Q2, exports are expected to return to a pace more in line with world demand for German products (+0.8%) and foreign trade should again hold back growth until the end of 2017. As an annual average, foreign trade should make a neutral contribution to growth in 2017 (after –0.3 points in 2016). ■

Consumption is set to remain robust, in step with purchasing power



Sources: Destatis, GfK, INSEE forecast

Italy

Reduced household savings act as a cushion

In Q1 2017 Italian activity picked up (+0.4% after +0.3%), driven by private consumption. It should subsequently settle at +0.3% per quarter through to the end of 2017, thanks to buoyant exports and corporate investment. In addition, despite the slowdown in their purchasing power, Italian households should continue to consume in 2017 by reducing their savings. As an annual average, activity is set to accelerate slightly: +1.3% after +1.0%.

Household consumption should hold firm despite the upturn in inflation

In Q1 2017 household consumption picked up (+0.5% after +0.1%) and should subsequently weaken slightly through to the end of the year (+0.2% per quarter on average). Consumer confidence remains high, despite waning considerably since the start of 2016. Due to the upturn in inflation (+1.5% over 12 months in May 2017 against –0.1% in October), household purchasing power should decline in 2017 (+0.5% after +1.5% in 2016). Nevertheless, payroll employment is expected to remain buoyant (+1.4% in 2017), which should be sufficient to trigger a new drop in unemployment, by 0.8 points to 10.9% in late 2017. Consequently, precautionary savings are likely to fall; although household consumption is expected to slow in 2017 (+1.1% as an annual average, after +1.3%) it should do so at a much slower pace than household purchasing power (*Graph*).

Investment should remain buoyant in 2017

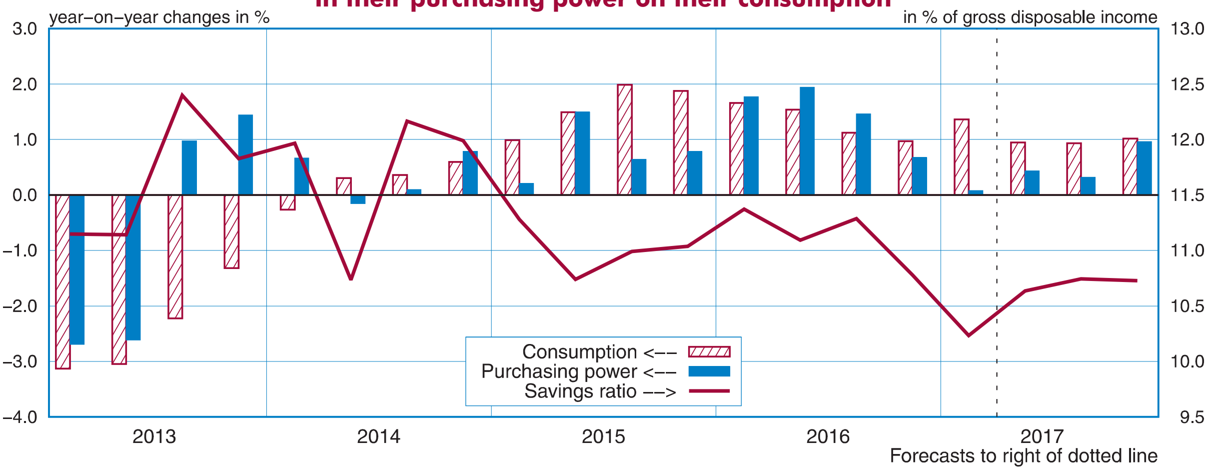
Over 2016 as a whole, construction investment returned to growth (+1.4%) for the first time since 2006. It gathered momentum at the start of 2017 (+0.6%, after +0.4%), and should grow steadily throughout the remainder of the year (+1.8% on average).

In reaction to a sharp rise in H2 2016 (+6.1%), driven by transport equipment purchases in particular, equipment investment fell during the winter (–3.0%). The self-financing ratio is at its highest level and the additional depreciation allowance scheme has been ramped up since January 2017 for investments relating to new technologies. The business climate is at a ten-year high. As a result, investment in capital goods is expected to regain momentum: +0.8% in Q2 2017, followed by +0.7% per quarter in H2. As an annual average, it should rise again but less strongly than in 2016 (+1.9% in 2017 after +7.5%).

Exports are expected to gather pace significantly in 2017

Exports are expected to accelerate significantly in 2017 (+4.4% after +2.6% in 2016), in response to world demand for Italian products. Imports are also set to rise more quickly (+5.6% after +3.1%) so that foreign trade should hold back growth slightly (0.2 points after –0.1 points in 2016). All in all, growth should almost maintain this pace through to the rest of the year, at +0.3% per quarter. On average over 2017, GDP is expected to rise more quickly than in 2016 (+1.3% after +1.0%), once again slightly below the growth rates of the other main Eurozone partners (see *Special Analysis* p. 37).■

In late 2016 and early 2017, households saved less, cushioning the impact of the drop in their purchasing power on their consumption



Sources: Istat, INSEE forecast

Spain

Slowdown postponed

In Spain, activity grew robustly again in Q1 2017 (+0.8% after +0.7%), driven mainly by a rebound in investment in capital goods. Growth should remain just as high in Q2. However, the upturn in inflation should hold back consumption in H2, and with it, activity. On average in 2017, gross domestic product (GDP) should slow, but only slightly (+3.0% after +3.2%).

The business climate remains positive

In Q1 2017, Spanish activity accelerated slightly (+0.8% after +0.7%). In Q2 the business climate remains favourable in both services and industry, and is picking up in construction; growth should therefore remain high (+0.8%). However, the sharp upturn in inflation since the end of 2016 is eating into purchasing power gains, and household consumption is likely to weaken slightly in the second half of the year. As a result, GDP should slow down slightly in H2: +0.7% in Q3 followed by +0.6% in Q4. As an annual average, it should slow only very slightly in 2017: +3.0% after +3.2% in 2016 and in 2015.

Consumption is expected to suffer slightly due to the rise in inflation

Household consumption slowed in Q1 2017 (+0.4% after +0.8%). It is expected to be more dynamic in Q2 (+0.6%) before slowing down slightly, although to a lesser extent than suggested by the slowdown in purchasing power, with gains being whittled away by inflation (Graph). Indeed, inflation rose to +2.0% over the year to May, against +0.5% in October 2016, and is not expected to drop below +1.5% by the end of 2017. In addition, employment should decelerate slightly: its previous momentum was partly generated by the tourism sector which is expected to create fewer jobs in 2017, with Spain's attractiveness having already increased significantly in 2016. On average over the year, private consumption is likely to slow (+2.3% after +3.2%).

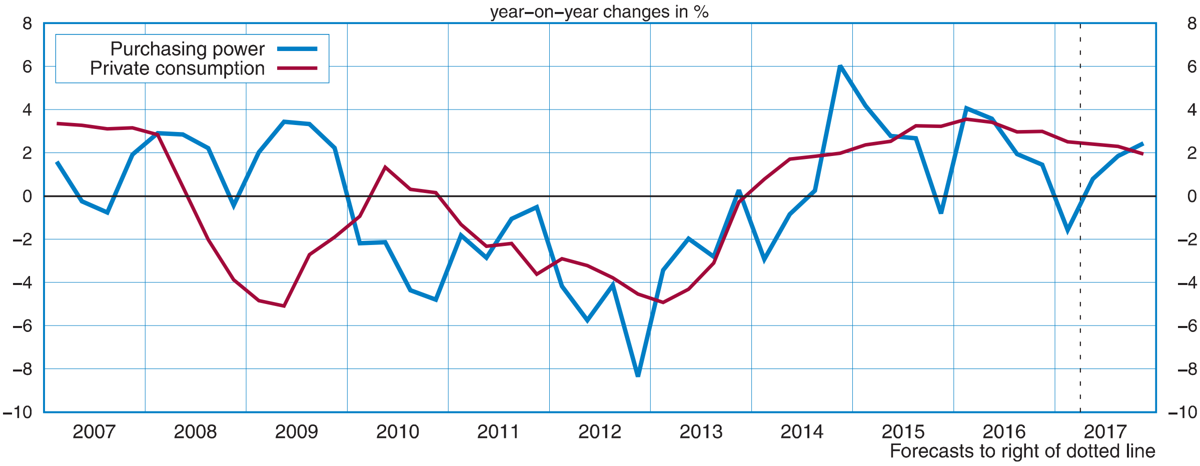
Investment in construction should pick up significantly

Investment in capital goods bounced back strongly in early 2017 (+3.1% after –0.1%) but should subsequently slow down slightly: with the investment rate nearing its 2008 level, the catch-up effect is likely to run out of steam. Moreover, the financial situation of enterprises is expected to deteriorate slightly due to the rises in wages, energy prices and taxation. Conversely, investment in construction should become more vigorous (+4.2% on average over the year after +1.9%), as suggested by the significant recovery in the number of residential building permits, the rise in purchasing intentions and households' intentions to carry out building work, as well as the recent improvement in the business climate in the construction sector.

Foreign trade should continue to foster growth

Thanks to the acceleration in global demand and gains in market shares, and despite buoyant domestic demand, foreign trade should continue to foster growth in 2017, contributing +0.5 points on average over the year, as last year. ■

Household consumption is expected to slow more moderately than household purchasing power



Sources: INE, Eurostat, INSEE forecast

United Kingdom

Consumption finally slows

In Q1 2017, UK activity slowed significantly (+0.2% after +0.7%), as households began to adjust their consumption to their past loss of purchasing power. Growth should remain slow through the rest of the year (+0.3% per quarter) as household consumption remains weak. Companies are also likely to restrict their investment in H2, as they adopt a wait-and-see attitude amid uncertainty as to the terms of the country's exit from the European Union. On an annual average basis, growth should decrease a little (+1.5%, after +1.8%). Year on year, the slowdown should be more pronounced: +1.1% year on year expected at the end of 2017, against +1.9% one year earlier.

Households end up adjusting their consumption to their past fall in purchasing power

In Q1 2017, UK activity slowed significantly (+0.2% after +0.7%) in the wake of consumption (+0.3% after +0.7%; *Graph*). British households had overconsumed in H2 2016, anticipating the upturn in inflation due to the fall in sterling and linked to the Brexit vote at the end of June 2016 (see Focus in *Conjoncture in France*, December 2016, p. 121-123). At the beginning of 2017, they began to adjust their consumption to their purchasing power. After falling to an all-time low at the end of 2016 (3.3%), their savings ratio would even appear to have started rising in early 2017.

Through to the end of 2017, purchasing power should rise again modestly: inflation should ease slightly and nominal wages are expected to benefit from the 4% increase in the minimum wage on 1st April 2017. However, consumption is likely to continue adjusting to the past fall in purchasing power, and it is also being affected temporarily by an increase in the tax on purchases of new cars on 1st April. It should therefore fall in Q2 (–0.2%) and then rise again a little in H2 2017 (+0.2% per quarter). On an annual average basis, it should slip significantly in 2017: +1.4% after +2.8%.

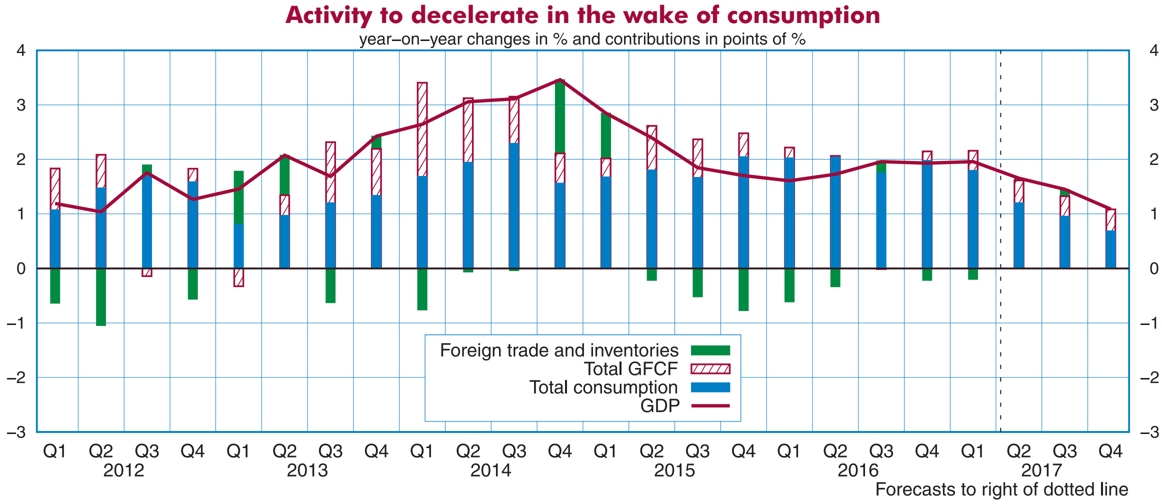
A temporary rebound is expected in investment in a wait-and-see climate

In H1, corporate investment is likely to pick up (+0.6% then +0.8%, after –0.9% at the end of 2016), as suggested by the recent improvement in order books and in investment intentions. It should slow down significantly in H2, however (+0.3% per quarter), as companies adopt a wait-and-see attitude as to the terms of the UK's exit from the European Union. All in all, corporate investment should grow by 1.1% in 2017, after falling back by 1.5% in 2016.

Exports are likely to profit from the recovery in world trade

At the beginning of 2017, exports fell (–1.6%) in reaction to the sharp rise at the end of 2016 (+4.6%), while imports rebounded (+2.7% after –1.0%). In Q2, exports should pick up again (+1.6%), in line with world demand, then slow down through to the end of the year as the favourable effect of the past fall in sterling fades out. Imports should increase slowly, following domestic demand. On average in 2017, the contribution of foreign trade to growth should be negative (–0.3 points, as in 2016). ■

Activity to decelerate in the wake of consumption



Sources: NSO, INSEE forecast

United States

Investment and imports on the rise

American activity stalled in Q1 (+0.3%), hampered by low private consumption and government spending, but is set to gather pace in the spring (+0.7%). It should then grow by 0.5% per quarter until the end of 2017. On average, growth is expected to rise in 2017 (+2.1% after +1.6%), buoyed by a rebound in corporate investment that began at the start of the year.

After stalling, consumption is set to rise again in the spring

Household consumption slowed significantly in Q1 2017 (+0.2% after +0.9%), particularly consumption of energy– because of the mild winter – and automobiles. Consequently, it held back activity as a whole (+0.3% after +0.5%). However, household confidence has reached its highest level since 2005. Household purchasing power should benefit from an easing of inflation (down from +2.6% year-on-year to the start of 2017 to +1.9% at the end of the year) and a promising job market, with the unemployment rate at its lowest level since 2005 (4.3% in May). In late 2017, households should also start to benefit from the tax cuts announced by the new government. Their consumption is thus expected to gather pace in the spring (+0.7%) and then grow steadily in H2 (+0.5% per quarter). It should remain dynamic on average over the year (+2.4% after +2.7%). Public spending is likely to bounce back after an unexpected drop at the start of the year, especially on defence.

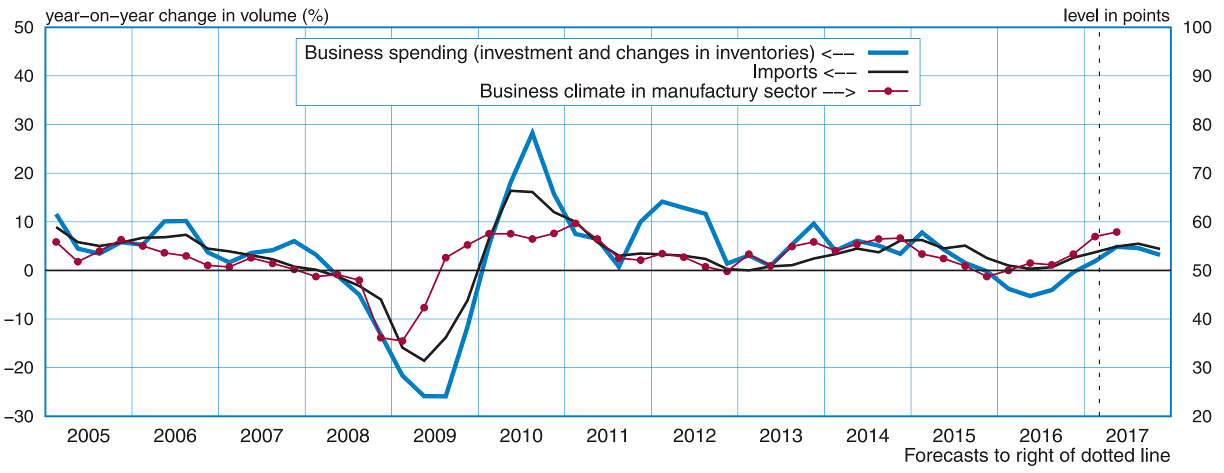
Investment is likely to bounce back significantly in 2017

The business leaders surveyed in the business tendency surveys remain optimistic, despite a decline in the short-term climate in April. Corporate investment picked up significantly in Q1 (+2.7% after +0.2% per quarter since the spring of 2016), driven by a recovery in spending in the oil sector in particular. It should subsequently slow down while continuing to increase steadily (+0.7% followed by +0.9% per quarter), and bounce back significantly on average over the year (+4.4% after –0.5%). It is likely to be one of the main factors driving the acceleration of gross domestic product (GDP): +2.1% after +1.6% in 2016.

Foreign trade is expected to hamper growth a little more in 2016.

Exports bounced back in Q1 (+1.4% after –1.1%), driven by buoyant foreign demand and the stabilisation of the dollar after several quarters of appreciation. They should slow down slightly through to the end of 2017 (+0.9% on average per quarter) but accelerate significantly on average over the year (+3.2% after +0.4%). Imports slowed in Q1 (+0.9% after +2.2%) in the wake of domestic demand, and are expected to increase at a similar rate through to the end of the year (*Graph*). Over the year as a whole, they should accelerate briskly (+4.6% after +1.1%), to such an extent that foreign trade is likely to weigh down more heavily on growth in 2017 (contribution of –0.3 points, after –0.1 points). ■

The rebound in domestic demand is driving American imports



Sources: BEA, ISM, INSEE forecast

Japan

Consumption and exports in much better shape

In Q1 2017 Japanese activity grew at the same rate as in the previous quarter (+0.3%), driven by a slight rebound in private consumption and a new sharp rise in exports. Through to the end of 2017, gross domestic product should continue to rise at a moderate pace, as suggested by the resilience of the business climate in the spring: +0.2% in Q2 followed by +0.3% in each of the last two quarters. Over the year as a whole, GDP should grow at virtually the same rate as in 2016 (+1.1% after +1.0%).

The business climate remains positive and exports are very dynamic

Since the start of 2017 the business climate has remained generally positive in Japan. The Markit indices, among others, have recovered and continue to rise after dipping in 2016 in both services and industry (*Graph*). Consequently, activity grew by 0.3% in Q1 2017, as in the previous quarter, driven by a combination of slightly higher household consumption (+0.3% after 0.0%) and exports which remained buoyant (+2.1% after +3.4%), particularly those to China.

Between now and the end of the year, exports should rise more moderately. On average in 2017, foreign trade is expected to contribute +0.4 points to total growth of +1.1%, after already contributing +0.6 points to the +1.0% rise in gross domestic product (GDP) in 2016.

Private consumption is in much better shape

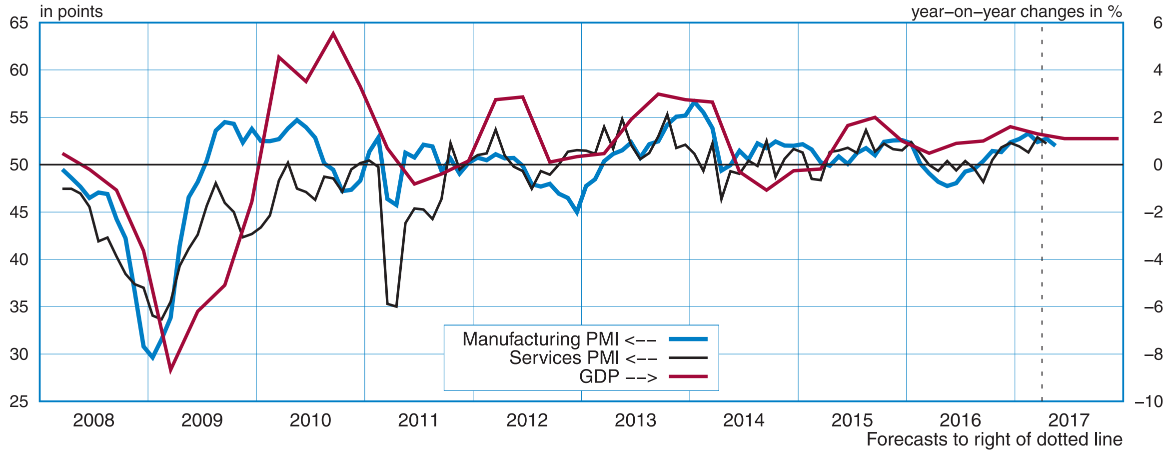
After gathering pace in Q1, household consumption expenditure should continue to grow moderately (+0.2% to +0.3% per quarter). It should be buoyed by purchasing power gains generated by slight wage rises. The unemployment rate is set to stabilise at 2.8%, its lowest level since June 1994. Through to the end of the year, inflation – fuelled by energy prices and the recent depreciation of the yen – is expected to stand at +0.3% year-on-year, which should have very little negative impact on household income. Over the year as a whole, private consumption should also pick up (+0.9% after +0.3%).

Public and private investment are set to pick up

After dropping in 2015 and 2016 in reaction to the massive stimulus plan in 2013, government investment is expected to accelerate further in 2017, after the announcement of new spending on infrastructure at the end of 2016. Boosted by the rise in demand and the high level of company profits, corporate investment should continue to rise steadily (+0.6% to +0.7% per quarter). On average over the year, it is expected to pick up significantly (+3.3% after +1.4%).

All in all, corporate investment and household consumption should be the main factors driving GDP growth in H2 (+0.3% per quarter). ■

The short-term outlook is promising



Sources: Japan Markit, Japanese Cabinet Office

Emerging economies

The recovery is confirmed

In early 2017 the business outlook for the emerging economies continued to improve, with the rebound in commodity prices and the upswing in world trade. In China, activity remains steady and imports are rising sharply, in the wake of the newly buoyant domestic demand. Activity should pick up slightly through to the end of the year due to the recovery of exports and the maintenance of powerful government support measures. As an annual average, growth in the Chinese economy is expected to stand at +6.8% in 2017, like the two previous years, but the investment slowdown should come to an end, with the result that imports should increase strongly (+13.5%) after two years of near stagnation. As a result, China is likely to be the leading contributor to the acceleration of world trade. Processing trade-related activities should also pick up.

In Brazil the business climate is improving, especially in industry, reflecting the upswing in exports. In Russia the business climate is improving rapidly with the rebound in commodity prices and the appreciation of the rouble: activity should return to growth in 2017. The Eastern European countries are expected to maintain their momentum, driven by promising demand from the Eurozone.

Chinese imports are set to pick up significantly, buoyed by domestic demand and processing trade

Activity in China slowed in Q1 2017 (+1.3% after +1.7%). It should pick up in Q2, rising to +1.8%, buoyed by domestic demand, and subsequently increase by 1.6% per quarter until the end of the year. As an annual average, it should grow by 6.8% in 2017, as in the two previous years.

Despite a downturn since March, the business climate remains positive. Domestic demand is strengthening further. In particular, corporate investment has been gathering pace since the autumn, in both construction and manufactured goods, after two years of slowdown. This should reduce the over-production seen in the cement and steel industries in previous quarters. In addition, fiscal policy remains highly accommodating.

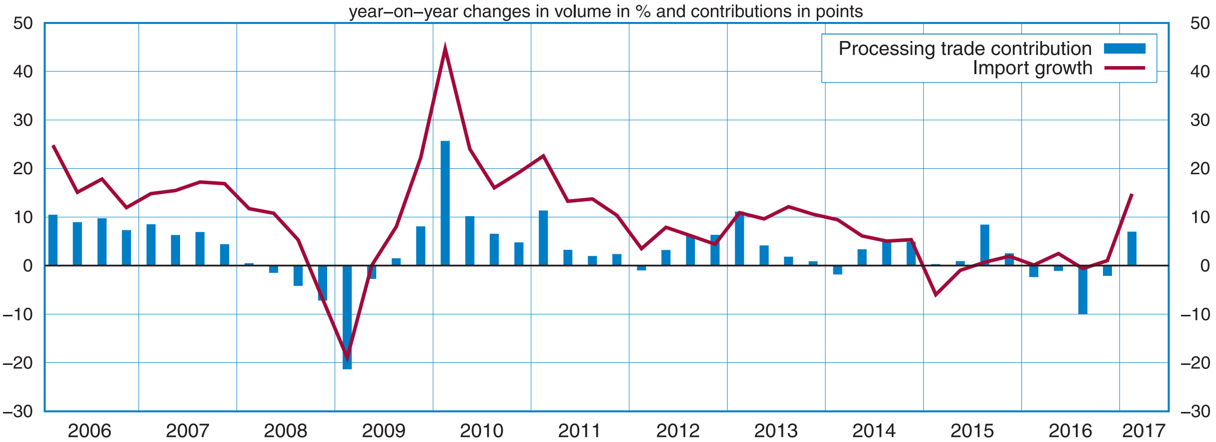
Consumption also remains dynamic. Household confidence has improved significantly since December. Retail sales have been gathering pace since mid-2016, all the more so since inflation has fallen. Vehicle registrations should pick up during the coming months after a sharp downturn in late 2016, hit by a restriction on purchase subsidies for the most polluting vehicles.

Exports fell significantly in Q1 2017 (–2.0%). They are expected to bounce back in Q2 (+2.6%), in the wake of sharply rising foreign demand, and then increase by 1.5% per quarter through to the end of the year. All in all in 2017, they should pick up tentatively (+0.9%), after declining in 2016 (–1.6%) for the first time since 2009.

Imports continued to gather pace markedly in Q1 2017 (+6.4%, and +13.9% over 12 months, *Graph 1*). They were again driven by processing trade, representing nearly 45% of Chinese imports, and by investment. Even though they are set slow down through to the end of the year (+1.5% in Q2 2017 followed by +1.7% per quarter), as an annual average, imports are set to soar in 2017

1 - Growth in imports and contribution of processing trade in China

year–on–year changes in volume in % and contributions in points



Source: Chinese customs administration, INSEE calculations

(+13.5%) after two years of near stagnation (including +0.8% in 2016). As a result, China is likely to be the main contributor to the acceleration of world trade.

Russian activity perks up

Russia has seen a return to growth with the rebound in commodity prices and the appreciation of the rouble. In Q1 2017, gross domestic product (GDP) grew by 0.4% after +0.3% at the end of 2016, thanks to the rise in exports. Domestic demand has improved: retail sales and new registrations have bounced back, thanks to the rise in purchasing power linked to the continuous drop in inflation since the start of 2016. With the short-term climate remaining positive (Graph 2), GDP should continue to pick up gradually: annual growth is set to reach +1.2% in 2017, after –0.2% in 2016 and –2.8% in 2015.

Activity remains buoyant in the CEEC

Aggregate GDP in the Central and Eastern European Countries (CEEC) continued to increase at a brisk pace in Q1 2017 (+1.2% after +1.1%), buoyed by solid industrial production. Benefiting from demand from the Eurozone, chiefly Germany, activity in the CEEC should regain its trend momentum for the remainder of the year (+0.8% on average per quarter). As an annual average, activity should grow by 3.8% in 2017 (after +2.9% in 2016).

In India, growth remains sustained

In late 2016, India continued to enjoy sustained growth in spite of the surprise demonetisation of 500- and 1000-rupee banknotes in November. After deteriorating briefly, the business climate started to improve significantly in January and industrial production rose again in Q1 2017. Despite rising commodity prices leading to an upturn in inflation, India should maintain its dynamic growth in 2017, driven mainly by domestic demand.

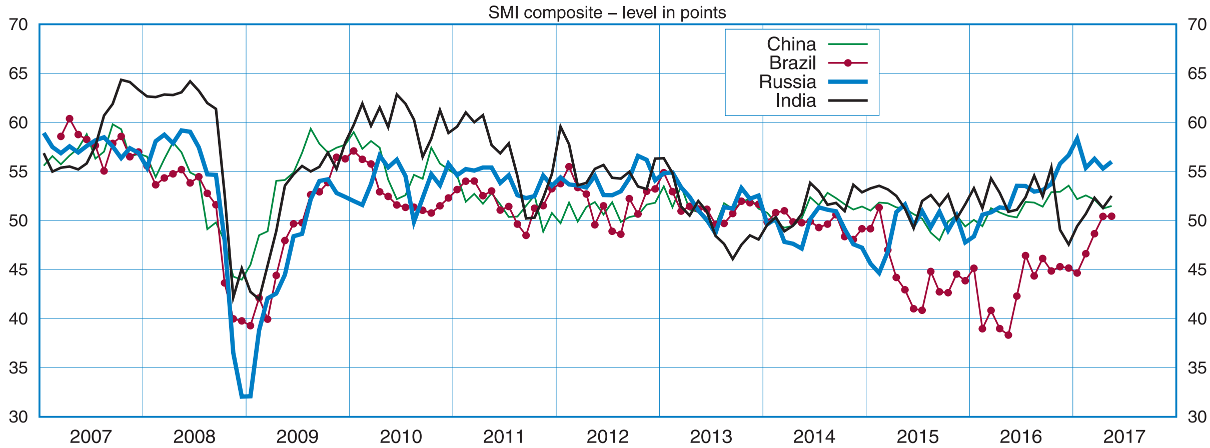
Brazil emerges from recession

Brazilian activity continued to shrink in 2016 (–3.6%) – a recession almost as harsh as that experienced in 2015 (–3.8%). However, the business climate improved significantly in industry and services at the start of 2017, and industrial production rose slightly in Q1. With the continuous drop in inflation, household purchasing power should decline more slowly. Thanks to the recovery of exports and the rise in commodity prices, GDP bounced back in Q1 2017 (+1.0% after –0.9%) and should continue to grow thereafter. As an annual average in 2017, Brazil could return to growth (+0.9%) despite the many political uncertainties.

The Turkish economy gathers pace

In Turkey, after a technical rebound in late 2016 following a summer affected by the attempted coup, activity returned to steady growth in Q1 2017 (+1.4%), thanks to powerful government stimulus measures and rising exports, boosted by the weak pound. In Q2, the business climate is improving significantly in manufacturing industry, and industrial production soared in April. As a result, Turkish growth is expected to accelerate: +4.1% on average in 2017, after +3.0% in 2016, but below the average recorded between 2000 and 2012 (+4.9%). ■

2 - The business climate remains positive in the emerging countries



Source: Markit