Germany

Growth is expected to remain solid

In Germany, growth in activity remained solid in Q4 (+0.6%) after a very dynamic Q3 (+0.7%). Once again foreign trade boosted growth and government consumption remained buoyant. In 2018, household expenditure is expected to be vigorous once again, encouraged by dynamic wages and a very low unemployment rate. But exports are expected to lose some momentum, which is likely to cause activity to slow slightly (+0.6% then +0.5%) in spite of dynamic investments. Gross domestic product grew 2.5% over the year 2017 after +1.9% in 2016. For 2018, the growth overhang at the end of H1 is expected to be +1.9%.

Household consumption is likely to pick up sharply

In Q4, household expenditure stagnated after falling (0.0% after –0.2%). Wages slowed considerably and purchasing power fell. Government consumption remained buoyant (+0.5% after +0.5%).

Wages are expected to pick up again at the beginning of 2018 (+0.9% then +0.8%), boosted by the increase in the minimum wage applied progressively since the beginning of 2017 and wage negotiations. Purchasing power should bounce back at the beginning of 2018 in spite of a rise in inflation to 2.0% mid-year. Job creation is set to remain vigorous (+0.4% then 0.3%) and the unemployment rate should stabilise at a very low level. A rebound is expected in private consumption (+0.6% per quarter), sustaining growth (*Graph*). The uncertainty surrounding the formation of a government has not affected household confidence. The savings ratio is expected to remain stable. Furthermore, government consumption is set to slow slightly (+0.4% per quarter).

Investment should bounce back

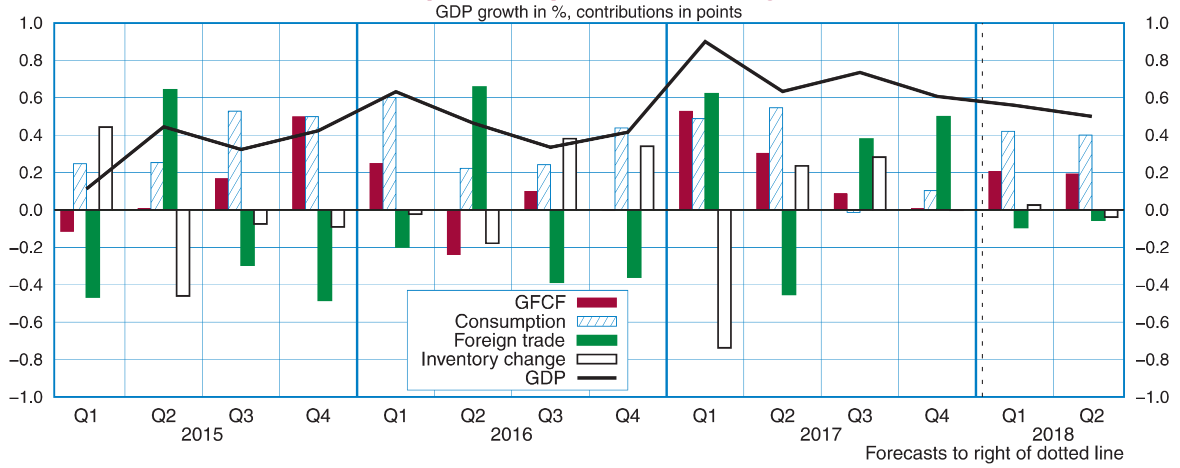
Activity slowed slightly in Germany in Q4 2017 (+0.6% after +0.7%). Indeed, investment slowed again at the end of 2017, due to a decline in construction (–0.4% after –0.3%) and a slowdown in investments in capital goods (+0.7% after +1.3%). Investment in construction is expected to bounce back in Q1 as suggested by the high levels in the surveys (+0.7%), but then is expected to fall back in Q2 in line with the lower number of building permits granted at the end of 2017 (+0.5%). Investment in capital goods is also expected to accelerate as an after-effect in Q1 and to maintain this pace in Q2 (+1.8% per quarter).

Foreign trade is likely to weigh down a little on growth at the start of 2018

Foreign trade sustained growth significantly in Q4 (+0.5 points), with exports growing faster than imports (+2.7% compared to +2.0%). However, foreign trade is expected to weigh down on growth at the beginning of 2018 (–0.1 point per quarter), with exports slowing more markedly (on average +1.0% per quarter) than imports (+1.4% per quarter). Hence German activity is likely to slow down slightly in Q1 and Q2 2018 (+0.6% then +0.5%). GDP growth improved considerably in 2017 to reach 2.5%, after 1.9% in 2016. The growth rate carried over for 2018 at the end of H1 is expected to be +1.9%. ■

Consumption is expected to sustain growth

GDP growth in %, contributions in points



Sources: Destatis, INSEE calculations

Italy

Growth is expected to stand up to political uncertainties

In 2017, Italian activity grew 1.5%, its most substantial increase since 2010. At the end of the year, it rose by 0.3%, after +0.4% in Q3. This improvement should continue at a fairly sustained pace in H1 2018 (+0.4% per quarter), in line with private consumption. Investment is unlikely to suffer from a wait-and-see attitude in the context of the legislative elections on 4 March. The growth overhang is expected to be +1.2% by mid-2018.

Household consumption should return to a lively pace

In Q4 household consumption slowed (+0.1% after +0.4%). Purchasing power is expected to slow down in Q1 2018, as nominal wages are increasing less quickly than inflation, but should bounce back in Q2 (+0.0% then +0.5%). Nevertheless, the rise in employment should absorb the growth in the labour force, so that unemployment rate is expected to decrease (to 10.8% in Q2 against 11.2% a year earlier). The labour force participation rate is very dynamic and appears to be driven by an increased participation among older workers in the labour market (Focus).

Household confidence remained high in January and precautionary savings should now come down a little, so that consumption can return to a steady pace (+0.4% per quarter).

Equipment investment is set to sustain growth

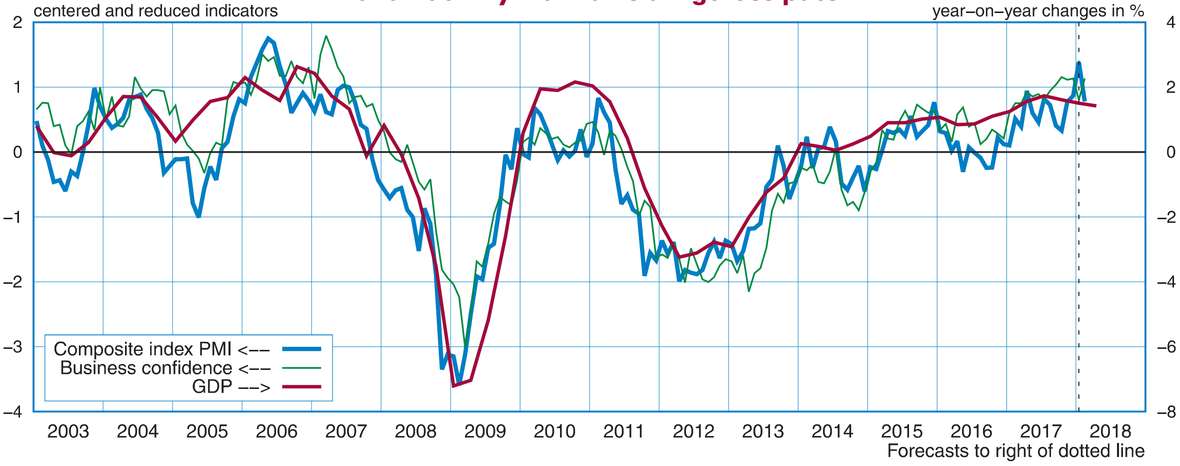
After strong expansion in Q3 2017 (+8.0%), equipment investment increased slightly slower in Q4 (+3.5%). However, it continues to take advantage of favourable conditions: industrialists' confidence is rising and self-financing capacities are high. Investment in equipment should therefore maintain a sustained pace (+1.2% per quarter) until mid-2018. The growth overhang is already expected to reach +9.8% in June 2018, as investment seems not to be suffering from a wait-and-see attitude with the legislative elections in March.

In Q4 2017 investment in construction pursued its rapid growth (+0.9%) after a more irregular start of the year. Leading indicators are down, suggesting moderate growth until spring (+0.3% per quarter).

In 2017, foreign trade made a positive contribution to activity

For the first time in four years, foreign trade made a positive contribution to activity in 2017 (+0.3 points). The pace of exports was close to that of world demand in Q4 (+2.0%) and should drop slightly below this level in H1 2018 (+0.9% per quarter), due to the appreciation of the euro. After +6.0% in 2017, the growth overhang of exports for 2018 is expected to be +4.2% by mid-year. Imports remained buoyant at the end of 2017 (+1.0%) and should remain solid until mid-2018, boosted by domestic demand. They are expected to increase at a rate of 0.9% per quarter. All in all, their annual growth overhang should be +3.8% by mid-2018 after +5.7% in 2017. ■

Italian activity maintains a vigorous pace



Sources: Istat, Markit, INSEE forecast

Spain

Activity has slowed but continues to show sustained growth

Activity in Spain activity remained buoyant in Q4 2017, as in the previous quarter (+0.7%). Private consumption was the main growth driver. Activity is expected to remain strong until June 2018, again driven by vigorous domestic demand. The contribution of foreign trade is likely to weaken a little due to a stronger Euro. All in all, the growth overhang in mid-2018 is expected to be +2.3%, after +3.1% in 2017.

Entrepreneurs' morale remains high

In February, the indicators from the business tendency surveys remained at high levels in all sectors, suggesting that growth should remain vigorous in Q1 2018 (+0.7%). In Q2, activity is expected to slacken very slightly (+0.6%) in a less favourable foreign trade context. The growth overhang is likely to reach +2.3% by mid-2018.

Consumption is unlikely to pick up in spite of buoyant wages

Household consumption slowed in Q4 2017 (+0.6% after +0.7%). The consumer confidence indices are still high and indicate that it should remain sustained in Q1 2018. Nominal wages are expected to rise, boosted partly by the progressive increase in the minimum wage. Inflation is expected to slip back slightly to 1.4%, against 1.9% in Q3 2017, and households should take advantage of these conditions to partly rebuild their savings ratio, which stands at its lowest level since 2008.

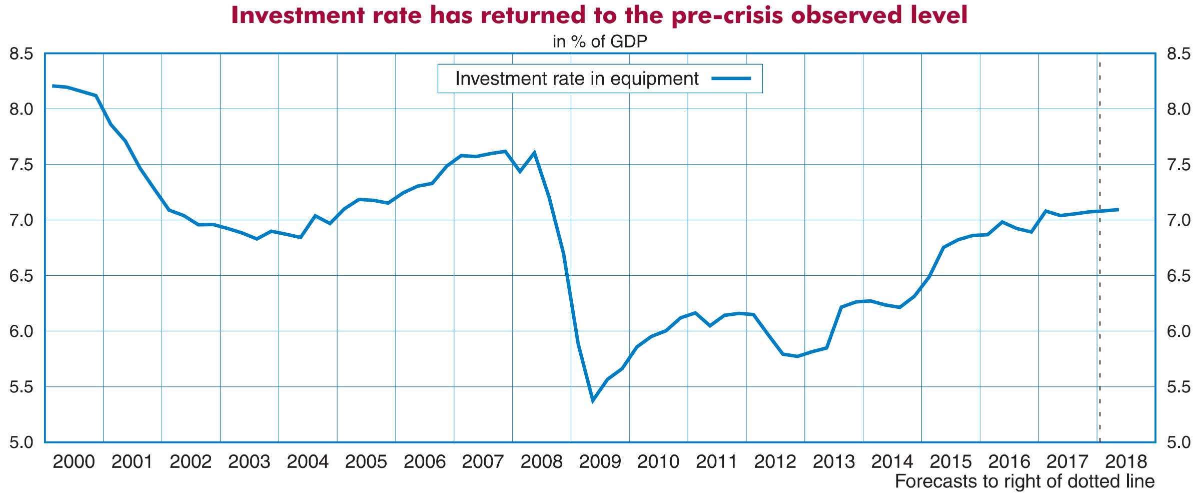
The investment rate has returned to its pre-crisis level

Investment in capital goods remained strong in Q4 2017 after a very vigorous Q3 (+0.9% after +2.9%). With investment as a share of GDP almost reaching its pre-crisis level (*Graph*) and against a backdrop of political uncertainty in Catalonia, growth in the investment rate is expected to run out of steam. The carry-over effect in investment to mid-2018 is expected to reach +4.0% after +6.2% in 2017. In the construction sector, non-residential investment should remain very strong, reflecting the earlier increase in building permits.

Foreign trade is expected to contribute less to growth

Lastly, in H1 2018, foreign trade is expected to stimulate Spanish growth less markedly than in 2017, due a slight slowdown in world demand and a strong Euro. Its contribution to the growth overhang of GDP in mid-2018 is expected to be +0.2 points, after +0.3 points over the whole year 2017 and +0.7 points in 2016. ■

Investment rate has returned to the pre-crisis observed level



Source: INE

United Kingdom

A consumption slowdown ahead

In Q4 2017, British activity slowed slightly to +0.4%, after +0.5%. It is expected to slow down to +0.3% per quarter in H1 2018: the past rise in inflation is likely to continue adversely affecting household consumption, as they reconstitute their savings. On average over the year, growth reached +1.7% in 2017 after +1.9% in 2016, but year-on-year the slowdown is sharper: at the end of 2017, GDP growth stood at 1.4% over one year compared to 2.0% a year earlier. The growth overhang in mid-2018 is expected to stand at +1.1%.

Households appear to be slowing their consumption in favour of saving

In Q4 2017, British activity slowed slightly (+0.4% after +0.5% in Q3). Indeed, household consumption slowed to +0.3%, after +0.4% in Q3. In H1 2018, purchasing power is expected to rise slightly (+0.3% then +0.4%) thanks to vigorous wages and a fall in inflation, as the past increase in the price of imports stops filtering through to headline inflation. However, growth in household consumption is likely to slow down again to +0.2% per quarter, as suggested by major purchase intentions (*Graph*), with households gradually rebuilding their saving capacity. Thus the savings ratio, which fell to 3.7% at the beginning of 2017, historically its lowest ever level, is expected to rise moderately to reach 5.4% by mid-2018.

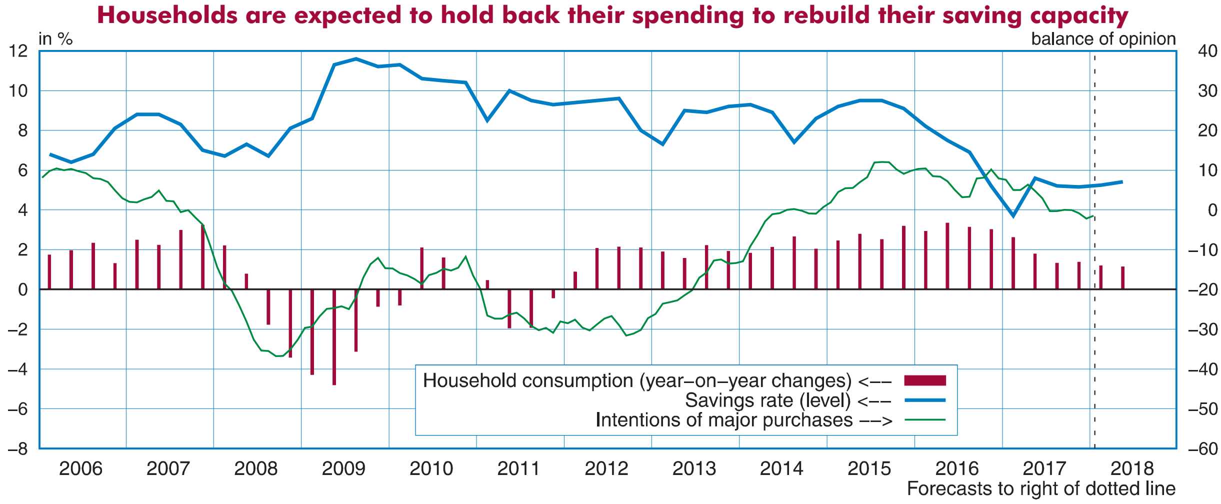
Investment is likely to be penalised by a wait-and-see attitude with regard to Brexit

Corporate investment came to a standstill in Q2 2017 (+0.0% after +0.9%). In H1 2018, it is expected to grow at a moderate pace (+0.4% per quarter). Indeed, in spite of full order books and a high production capacity utilisation rate, planned investments are stagnating, hindered by the uncertainty surrounding Brexit. In line with the bleak business climate in construction, household investment is expected to fall (–0.5% then 0.0%), also hampered by the same wait-and-see attitude.

Foreign trade is expected to benefit from the upswing in world trade

At the end of 2017, exports fell (–0.2% after +0.2%) but are expected to gather momentum again in H1 2018 (+0.9% then +0.7%), driven by world demand. Imports accelerated in Q4 2017 (+1.5% after +1.0%), but are expected to slow down after that (+0.5% per quarter) in line with the slowdown in domestic demand. Accordingly, the contribution of foreign trade to GDP growth is expected to be slightly positive (+0.1 points per quarter). ■

Households are expected to hold back their spending to rebuild their saving capacity



Sources: ONS, European Commission, INSEE forecast

United States

Activity is set to pick up pace, driven by the fiscal stimulus

In Q4 2017, activity slowed in the United States (+0.6% after +0.8%), driven by domestic demand but hampered by the rebound in imports.
In Q1 2018, it looks set to grow at the same pace, held back by a slowdown in exports and consumption. It should bounce back in the spring, with the first effects of the tax reform.
As an annual average, activity accelerated strongly in 2017 (+2.3% after +1.5%) and is likely to hold its momentum until mid-2018, with a growth overhang reaching +2.2%.

The fiscal stimulus should sustain domestic demand this spring

At the end of 2017, the business climate indicators in services slipped back slightly while industrial output bounced back, after having suffered during the hurricanes in September. GDP is therefore expected to grow by 0.6% in Q1 2018, as in the previous quarter, then pick up in spring, to +0.8%, as a result of the first effects of the tax reform voted by Congress in December (*Focus*). Activity accelerated sharply as an annual average in 2017 (+2.3% after +1.5%) and the growth overhang in 2018 should reach +2.2% in June.
This upturn is likely to benefit companies, whose investments gathered pace at the end of 2017 to reach +1.6%, after three vigorous quarters. The one-off additional depreciation allowance planned in the reform should encourage companies to invest from Q2 rather than Q1. By following an acceleration profile in this way (+1.0% then +2.0%) throughout the half-year, this should contribute significantly to a pick-up in US activity (*Graph*).

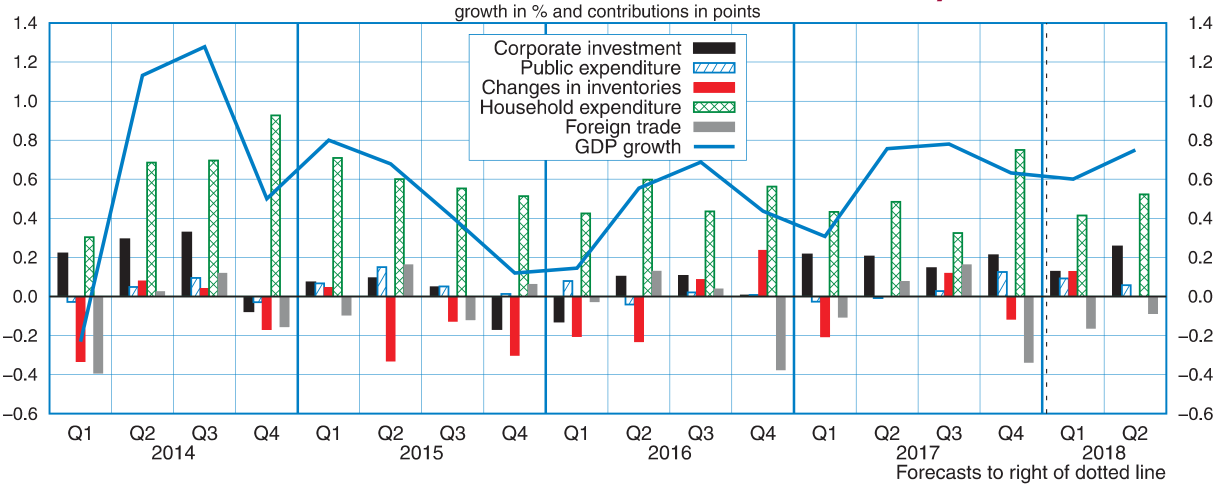
Vigorous wages and a drop in taxes should bolster purchasing power

Household purchasing power accelerated at the end of the year, to +0.3% after +0.2%, despite the rise in both energy inflation and core inflation. It should jump in H1 2018 (+0.9% per quarter), buoyed by wages that are much more dynamic than inflation and a sharp slowdown in taxes and social contributions as a result of the tax reform. Prices are expected to accelerate again, to an annual pace of +2.9% by mid-2018 against +1.9% one year earlier, driven by the rise in oil prices and the solid momentum of the labour market. The unemployment rate should stabilise at over 4.0%, its lowest level since the beginning of the 2000s. Consumption, which picked up sharply at the end of the year (+0.9% after +0.5%), is likely to remain buoyant in H1 2018 (+0.6% then +0.7%).

Imports are likely to remain buoyant

Imports rebounded at the end of 2017 (+3.3% after –0.2%), a knock-on effect of the previous three quarters when domestic demand accelerated. They look likely to slow to +1.4% in Q1 then should rebound to +1.7%. As an annual average, they accelerated in 2017 (+3.9% after +1.3%) and their growth overhang for 2018, which should reach +5.2% by mid-year, suggests that this momentum is likely to hold firm, making the United States one of the main contributors to the upturn in world trade.
Foreign trade again hampered US activity in 2017, removing 0.2 growth points, as in 2016, and it is already expected that the growth overhang for 2018 will contribute –0.4 points. ■

The acceleration in investment should bolster US activity
growth in % and contributions in points



Source: U.S. Bureau of Economic Analysis

Japan

Domestic demand should remain robust

In Q4 2017, activity in Japan remained buoyant (+0.4%) after two consecutive quarters of sustained growth (+0.6% per quarter). Foreign trade no longer sustained activity (having contributed +0.6 points in Q3). Government investment shrank again (–0.2% after –2.6%), but investment in the private sector remained robust (+0.5% after +0.6%). In H1 2018 activity is expected to accelerate slightly (+0.3% per quarter), sustained by domestic demand, but it should grow less rapidly than it did in 2017.

Household consumption should remain dynamic

In Q4 2017, Japanese activity remained buoyant after several quarters of solid growth (+0.4% after +0.6%). In annual average terms, the acceleration was sharp in 2017 (+1.7% after +0.9%). Activity should see a moderate upturn in H1 2018 (+0.3% per quarter), and the growth overhang for 2018 should stand at +1.3% by mid-2018.

Employment should continue to grow (+0.2% in Q1 then +0.1%), with supply-side tension on the labour market (Graph). The stabilisation of the unemployment rate at just under 3.0%, and Shinzo Abe's plans to encourage wage rises, should lead to an increase in wages in spring 2018. Inflation is set to increase (+1.1% year-on-year in Q1, then +1.3% in Q2), without compromising the increase in purchasing power. Consumption should remain dynamic (+0.5% at the end of the year then +0.4% per quarter), continuing to sustain activity. Over the year 2017 as a whole, consumption rose sharply (+1.0% after +0.1%) and the growth overhang should stand at +0.9% in mid-2018.

Investment should hold firm

Government investment shrank again in Q4 (–0.2%, after –2.6%). It should bounce back in early 2018 (+0.4%) then accelerate a little in Q2 (+0.6%), boosted in particular by military spending and infrastructure spending in preparation for the Olympic Games in 2020. Corporate investment should remain solid (+0.6% in Q1 then +0.5%), with the rate of profit remaining at a historically high level.

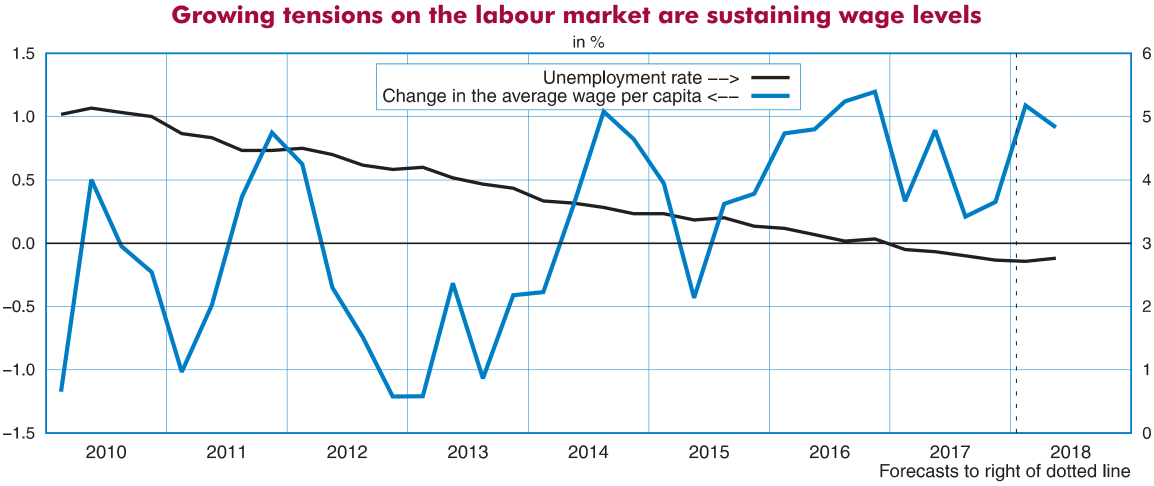
Foreign trade should remain neutral

Having remained buoyant in Q4 (+2.4% after +2.1%), exports should gradually slow (+1.5% then +0.8%) in the wake of Chinese imports. As an annual average, Japanese exports picked up sharply in 2017, to +6.8% after +1.3%. The growth overhang for 2018 should stand at +5.0% at the end of June.

Imports bounced back in Q4 (+2.9% after –1.2%) as consumer spending rallied. They should slow to +1.0% per quarter through to mid-2018. Imports performed strongly in 2017, recording +3.6% of annual growth after shrinking by –1.9% in 2016. The growth overhang for 2018 should stand at +3.8% by the mid-point of the year.

As in Q4 2017, the contribution of foreign trade to activity should be virtually nil through to mid-2018. ■

Growing tensions on the labour market are sustaining wage levels



Sources: Statistics Bureau, Ministry of Internal Affairs and Communications, Cabinet Office of Japan

Emerging economies

Slowdown in China, upturn in the other emerging countries

In China, activity barely slowed in Q4 2017 (+1.6% after +1.7%). Imports contracted (–1.0% after +1.6%) and exports bounced sharply back (+2.0% after –2.4%). Chinese activity is expected to slow down a little by mid-2018 (+1.5% per quarter), in the wake of domestic demand. On average over the year, in 2017 it maintained the pace of the last few years, and its growth overhang should already have reached +5.2% by mid-2018.

In Brazil and Russia, activity picked up again in 2017. Following this strong rebound as they emerge from the crisis, their growth is expected to return to a pace more in line with past performances. After slowing in 2017, Indian GDP is expected to pick up markedly. Likewise, after slowing down in 2016, activity in Turkey picked up in 2017 and should stay buoyant thanks to foreign demand. Finally, growth in Eastern Europe is expected to continue at a sustained pace, driven by demand from the Eurozone.

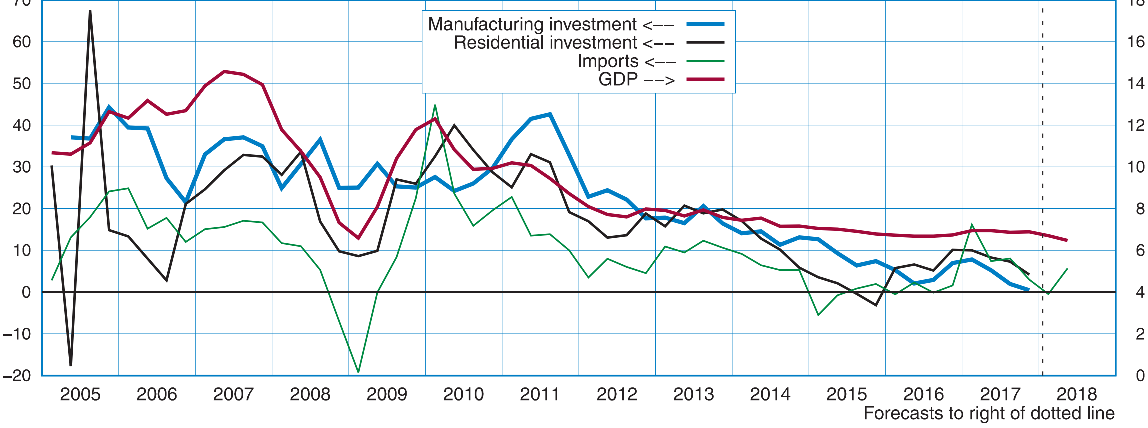
China: activity slows slightly along with domestic demand

In China, reported activity grew by 1.6% in Q4 2017, a pace very slightly weaker than at the beginning of the year. It is expected to slow down a little more through to mid-2018 (+1.5% per quarter), in the wake of domestic demand. On average over the year, it grew by 6.9% in 2017 after +6.7% in 2016, and its growth overhang should already have reached +5.2% by mid-year.

Domestic demand slackened again in the autumn, after three quarters of acceleration between mid-2016 and the start of 2017 (*Graph 1*). Industrial production has been slowing gradually since the summer and corporate profits, which bounced back at the end of 2016, have generally stalled since the spring, both in the private sector and for public-sector firms, in particular under the effect of the slump in producer prices. Investment has also continued to slow, in particular in the manufacturing sector, both in equipment and structures, as well as in construction. Finally, growth in retail sales has progressively declined, hampered by an upswing in consumer prices.

Chinese imports contracted at the end of the year after picking up over the summer (–1.0% after +1.6%), in connection with the slowdown in domestic demand. They are expected to rebound by mid-2018 (+3.0% then +2.0%), backed by a strong yuan and as they cease to be adversely affected by the drop in the share of the processing trade in China's foreign trade. On average over the year, imports bounced back in 2017 (+8.5% after +0.8%), making China one of the main drivers of the recovery in world trade. Their growth overhang for 2018, which is expected to reach +3.5% by mid-2018, is nevertheless expected to slow gradually, in the wake of the slowdown in activity.

1 - Growth in imports and activity in China



Source: NBSC

Exports saw a marked recovery in Q4 (+2.0% after –2.4%) under the effect of buoyant foreign demand, especially from the advanced economies. They are expected to slow gradually, in line with world trade, hampered by the past strength of the yuan: they should increase by 2.0% in Q1 2018, then 1.8% in Q2. On average over the year, they gathered pace in 2017 (+3.7% after –3.0%) and their growth overhang for 2018 should reach +4.7% by mid-year.

Russia: recovering

After two years of recession, activity grew at the beginning of 2017 and then started to gain momentum over the summer (+0.7%). It is expected to remain buoyant: the business climate (*Graph 2*) remains favourable and domestic demand is being driven by the drop in inflation, as can be seen by the continuous increase in retail sales over the year 2017. Economic activity appears to have grown by an annual average of 1.6% in 2017, and the growth overhang in mid-2018 is already expected to stand at +2.2%.

India: activity picks up again after slowing in 2017

In 2017, Indian growth was negatively affected by the surprise demonetisation of 500 and 1,000-rupee banknotes at the end of 2016, as well as the implementation of a harmonized VAT regime in July. Nevertheless, late in 2017 activity started to pick up again, which has been reflected by an improvement in the business climate in the manufacturing sector, now at its highest level since 2012, and a rebound in industrial production. At the start of 2018, India should keep a sustained rate of growth, mainly driven by vigorous domestic demand.

Brazil: activity is set to pick up in the wake of industry

At the end of 2017, falling inflation continued to boost purchasing power. The business climate is improving in industry and to a lesser extent in services. However, activity was at a standstill in Q4 (+0.1%), hit by a fall in exports, but it is expected to regain momentum during H1 2018 (+0.5% per quarter). In 2017, Brazil emerged from the recession (+1.0%), and the growth overhang by mid-2018 is likely be substantially higher (+1.2%) than growth over the last few years.

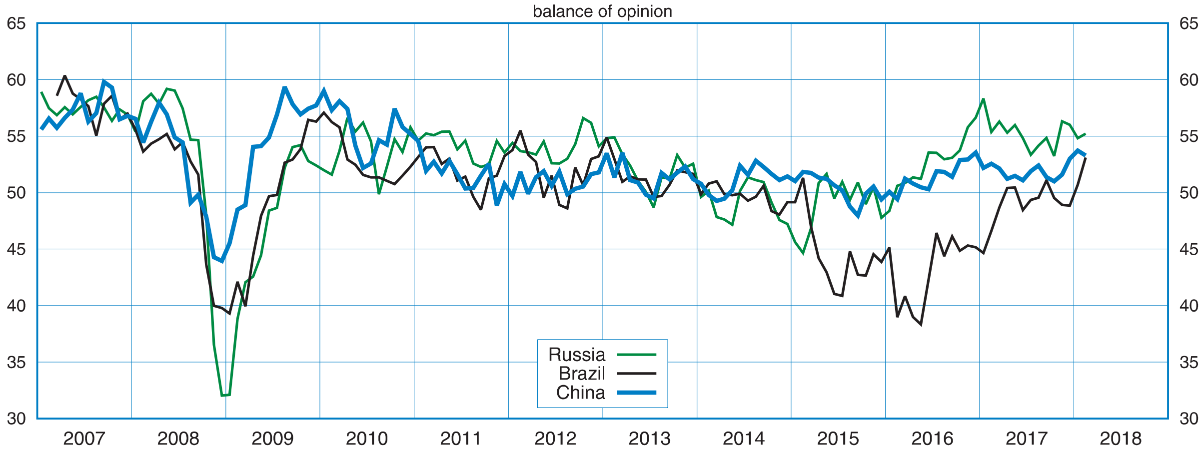
Turkey: activity driven by exports

After slowing in 2016, growth regained its momentum in 2017, with GDP gathering pace continually to reach +1.7% in Q3. At the end of 2017 the business climate remained favourable, at its highest level since 2014, and industrial production continued to rise. Exports picked up sharply, taking advantage of the recovery in world demand and the depreciation of the Turkish lira. In Q4 growth appears to have remained buoyant (+1.0%) and should continue at a sustained pace in early 2018.

CEEC: growth is benefiting from the acceleration in world demand

In the Central and Eastern European Countries (CEEC), the business climate remains very favourable. Activity remained very vigorous in Q4 (+0.9% after +1.2%). Indeed, industrial production gained momentum, boosted by demand from the Eurozone, in particular from Germany. Activity should continue to grow at a steady rate through to mid-2018. On average in 2017, GDP also accelerated to reach +4.6%, and the mid-year growth overhang in 2018 is expected to rise to +4.0%. ■

2 - The business climate in the manufacturing industry is picking up in the emerging countries



Source: Markit