ECONOMIC ENVIRONMENT

United States

CYCLICAL RECOVERY BUT SHORTAGE OF DEFLATIONARY CREDIT

Growth is still driven by the manufacturing sector, which continues to benefit from solid growth in world trade and vigorous restocking in the short term. It is this dynamic that is at the origin of the return of job creations in the private sector, even beginning to spread to the non-manufacturing sector. A solid rise of 3% in private consumption in the first quarter and the continuing improvement in profitability supplements this classic cyclical recovery picture.

However, the manufacturing sector should experience a marked slowdown in its activity in the coming months due to further destocking. Moreover, growth will remain hampered by the structural shortage in credit, a sign that borrowers are still defaulting due to solvency issues. This financial deflation has led to a long-term property deflation and sharp deflationary pressure in the rest of the economy. The fall in the price of property assets is a powerful force for debt reduction, particularly for households. The rise in their savings rate, which fell back down to 3%, should be appreciable: their consumption will experience lows. The cyclical recovery will be at best moderate.

Euro zone

THE RECOVERY HAS HARDLY BEGUN

After running out of steam in the last quarter 2009, GDP should increase slightly in the first quarter 2010. The industrial sector will continue to drive growth, thanks to the favourable cycle of stocks and the dynamism of exports, particularly in Germany, which remains the key element in the continuation of the recovery in the longer term.

On the other hand, the activity in local services has been affected by the weakness in domestic demand. More specifically, household consumption will drastically curtail growth in the first quarter, as shown by stagnation in household confidence over several months due to concern about the struggling employment market: the unemployment rate reached 10%, its highest level since August 1998.

Furthermore, the construction sector is suffering in the long term from the property crisis in several countries, and occasionally from very poor climate conditions in Germany where activity collapsed by 15% in the first quarter. Lastly, the persistent worries regarding sovereign debt, and that of Greece in particular, will continue to burden the entire Eurozone economy in the medium term. In this context of weakened domestic demand, inflation sporadically increased in March, due to the base effects on food and energy prices: it should fall again from next month.

China

ROBUST GROWTH AND RESTRUCTURING UNDERWAY

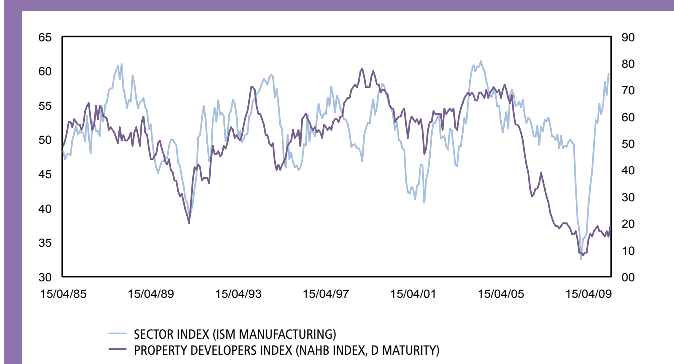
After a rise of 11.9% in the first quarter 2010, growth in China is consolidating, reorienting from investment towards consumption, shaped by economic policy. On one side, retail sales are increasing despite the rise in inflation from 1.9% to 2.7% due to food-processing prices. The budget policy increased benefits by 8% and expenses for social housing by 80%, with the aim of reducing household savings rates.

On the other hand, both residential and non-residential investment slowed considerably: the tightening of monetary policy, with a strict observation of credit quotas allotted to the different banks and provinces, resulted in a very marked slowdown in credit, which increased no more than 21% over one year in March, compared to nearly 35% at the end of 2009.

After the lull in Sino-American tension, a rise in the yuan against the dollar seems likely, which would contribute to the essential reorientation of growth in investment towards consumption.

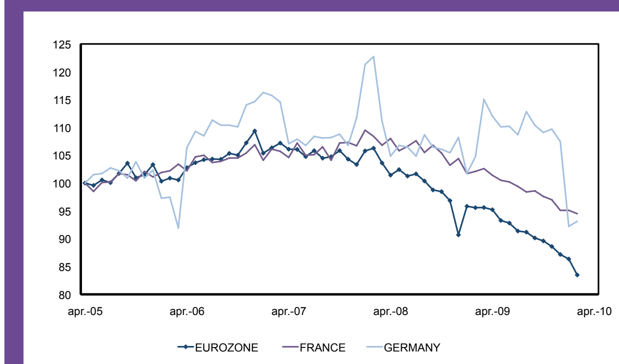
Laurent Berrebi,
Chief Economist

United-States: cyclical recovery but property deflation manufacturing



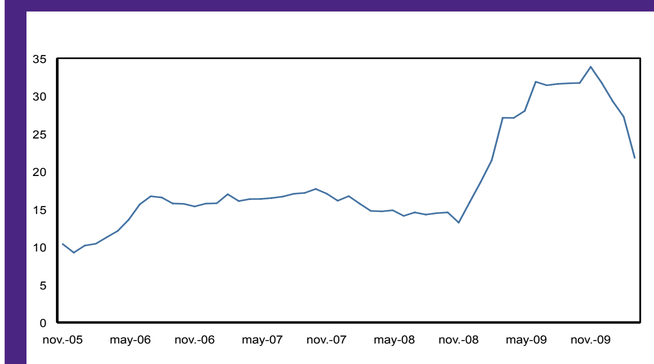
Sources: Datastream, Groupama AM

Eurozone: construction sector index (100 base at the start of the period)



Sources: Datastream, Groupama AM

China: very marked slowdown in credit from financial institutions (credit, year-on-year, %)



Sources: Datastream, Groupama AM

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