



United States

LOWER INTEREST RATES BOOST CONSUMER SPENDING

Growing at a rate of 4%, unseen in nearly four years, consumer spending boosted economic activity in the fourth quarter. Spending was buoyed by the wave of mortgage refinancing brought on by the decline in long-term interest rates of the preceding two quarters. However, such a marked decline in the savings rate is temporary, as it is unwarranted by fundamentals: the level of household wealth justifies a savings rate of around 7%, households continue to reduce debt at a high rate of 2.4% of annual revenue, even as they see the jobs market continue to worsen. Consumer spending should thus return to a growth rate of 2%.

The rise in long-term interest rates should also lead to further declines in housing sales and prices, as indicated by the reduced long-term outlook for property developers. Finally, the pace of restocking, which exceeded \$120 billion per year in the third quarter, is expected to return to its "normal" level of around \$50 billion. Impacted by the inventory cycle's reversal and the rise in the savings rate and in long-term interest rates, growth should weaken beyond Q1. The brighter side in terms of fundamentals is the gradual loosening of the credit market for SMEs, along with the return of non-residents to the U.S. corporate bond market: reduced funding constraints should eventually lead to improved job creation and investment by SMEs.

United States: consumer goods are driving the new acceleration in economic activity



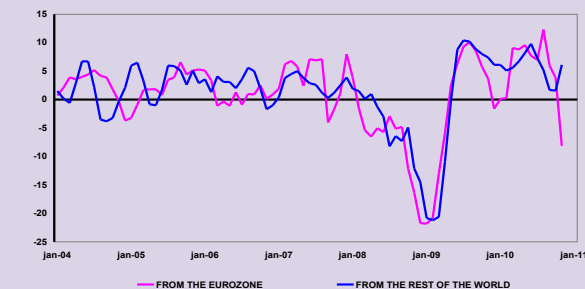
Euro zone

DESPITE GERMAN MOMENTUM, GROWTH REMAINS LACKLUSTRE

Growth was revised downward, from 0.3% to 0.2%, mainly due to consumer spending which in the end increased by a meagre 0.1% (instead of the 0.3% previously estimated), and in spite of rises of 0.4% and 0.5% in Germany and France, respectively. In the fourth quarter, domestic demand continued to be penalised by the peripheral countries, now in recession. German consumption shows no clear signs of recovery, suffering from low gains in purchasing power and continued debt reduction by consumers. France is one of the few countries where consumption has been strong, particularly due to the scheduled end of the car-scrapping bonus. Growth is expected to remain lacklustre, especially in the fourth quarter, as German foreign trade has slowed due the decline in demand from Europe's peripheral countries.

In the first quarter, European growth should benefit from the rebound in global growth, as evidenced by the strength of business indicators in the industrial sector. Beyond that, the outlook is clouded by austerity plans and higher long-term interest rates. The latter will have a significant impact on real estate, particularly in France, and Italy, where growth excluding inventory accumulation was already negative in the third quarter. Italian domestic demand is reversing, as shown by the sharp decline in business indices in services and construction, while the unemployment rate is rising.

Germany: new manufacturing orders suffer from the recession in the peripheral countries (new export orders, qtrly chg, %)



China

CALIBRATED MONETARY TIGHTENING TO TAME INFLATION AND CALM THE HOUSING BUBBLE

Activity remained strong in the short term due to restocking, but is expected to slow after the first quarter under the impact of tighter monetary policy with a twofold objective:

Firstly, even if an inflationary spiral is not in progress, the central bank will seek to curb inflation which is putting a brake on consumer spending, as households worry about soaring food prices. China could thus accept a higher appreciation of the yuan than the expected 5%. Secondly, the Bank of China wants to slow the flow of credit in order to calm the property market: a bursting housing bubble could have serious repercussions on the banking system. To dampen overheating in real estate, the government will also build 10 million public housing units. The continued rise in the required reserve ratio and prime interest rates, which were raised respectively by 350 and nearly 100 basis points in one year, will nevertheless be partly offset by the widening budget deficit: in 2010, the central government's fiscal deficit increased by one percentage point of GDP under the impact of higher social spending (education, health, transfers), which lowered rates of household saving as well as outlooks for consumption.

China: sharp increase in required reserve ratios (%)

