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# MACRO HIGHLIGHTS

WEEK OF 5 SEPTEMBER 2016

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## OUR HIGHLIGHTS:

- ▶ **Economists' insight: On track for December 2016**
    - The disappointing August employment and manufacturing ISM reports in the US point to a postponed Fed funds rate hike to December 2016.
    - Emerging-market GDP numbers confirm the economic rebound, driven by the sector's weakest economies.
  - ▶ **Focus on Europe: Non-performing loans undermine the effectiveness of monetary policy in peripheral countries**
    - Bank lending growth has again accelerated in the eurozone, in a sign that monetary policy is working.
    - But significant disparities among countries call for further ECB action – this time in its banking supervisory role.
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### ECONOMISTS' INSIGHT

## ON TRACK FOR DECEMBER 2016

**Disappointing job-creation numbers in the USA make a Fed funds rate hike this month unlikely, and we still expect the hike to come in December.** In August, 151,000 nonfarm jobs were created, which was below the consensus estimate of 180,000. Private-sector job growth slipped to 126,000 from 225,000 in July.

The August employment report was much weaker than the June and July reports, in line with the slowing job-creation trend so far this year. On average, 182,000 new nonfarm jobs have been created per month this year, compared to 229,000 in 2015. The same trend holds true in the private sector, where the average number of new jobs fell from 221,000 per month in 2015 to 160,000 so far this year. The unemployment rate is unchanged at 4.9%.

**The August figures are particularly important in the light of recent comments by Fed officials, who indicated that the timing of the next Fed funds rate hike would hinge in part on this employment report.** Upcoming statements by the Fed will provide more clarity, but the poor showing by the ISM manufacturing index – which dipped from 52.6 in July to 49.4 in August – supports our scenario, under which the Fed softens its tone and waits until December to raise rates.



**While the chances of a Fed funds rate hike in December rather than September have increased, expectations of additional hikes further out have not changed significantly.** 2-year and 10-year Treasury yields are nearly unchanged at 0.78% and 1.60%, respectively.

The emerging-market economic calendar was quite full this past week, with the publication of GDP figures for Brazil and India followed by leading economic indicators. Broadly speaking, and in line with our expectations, **economic activity in the emerging-market bloc has been relatively stable, with most growth coming from weaker economies such as Russia and Brazil** (see table below).

	Annual real GDP growth		Manufacturing PMI indexes	
	Q2	Q1	August	July
China	+6.7%	+6.7%	50.0	50.6
India	+7.1%	+7.9%	52.6	51.8
Brazil	-3.8%	-5.4%	45.7	46.0
Russia	-0.6% (advance)	-1.2%	50.8	49.5

Growth in India fell short of our expectations owing to more moderate consumer spending (+6.8% vs. +8.3%) yet should remain on a firm uptrend over the next few quarters as leading indicators there pick up speed. The monsoon season is expected to end well, and this should buoy consumer spending in rural regions. At the same time, rising public-sector wages and progress in reform efforts – including the application of a unified VAT system – represent real growth drivers.

In Brazil, the removal of Dilma Rousseff marks the end of the political soap opera that has gripped the country for the past few quarters. Investors can now turn their attention back to the many economic challenges faced by the administration of Michel Temer, the country's new leader. The critical issue will be to reduce the country's fiscal imbalances against a backdrop of slowing growth and high inflation. **The rebound in commodity prices and the political breakthrough provided a boost that will not last forever, while structural reforms aimed at raising the country's productivity have yet to be adopted.**



FOCUS ON EUROPE

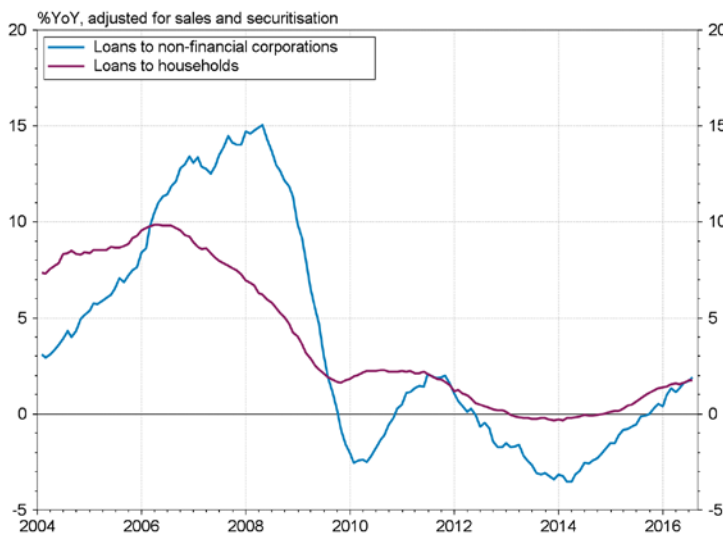
# NON-PERFORMING LOANS UNDERMINE THE EFFECTIVENESS OF MONETARY POLICY IN PERIPHERAL COUNTRIES

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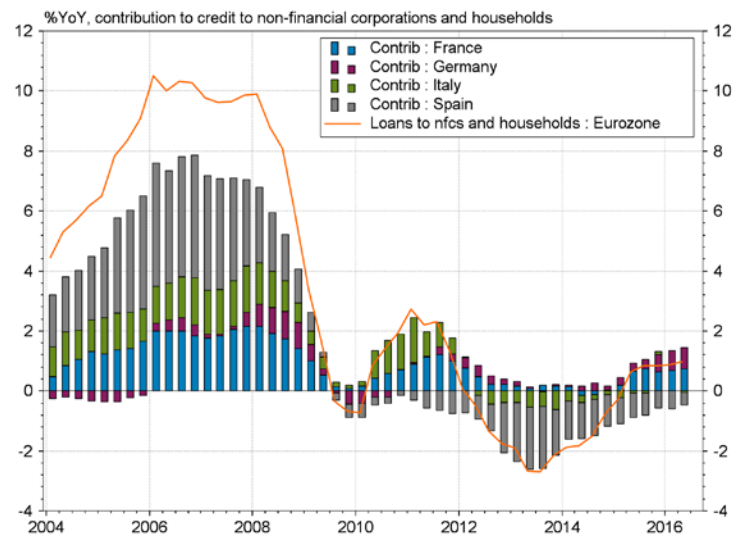
Monthly statistics published by the European Central Bank (ECB) show that bank lending to the private sector picked up in July. Credit to households and non-financial corporations grew by 1.7% versus 1.5% in June. **The growth rate of loans to households held steady at 1.8% in July; this figure continued to be supported, as we expected, by loans to households for house purchase, which showed an unadjusted annual growth rate of 2.3% in July versus 2.1% in June.** Of particular note, and **for the first time since November 2011, bank loans to non-financial corporations expanded faster than loans to households**, with the annual growth rate rising from 1.7% to 1.9%.

Bank lending to the private sector in the eurozone is picking up again...

...despite sharp disparities among countries



Source: Thomson Reuters Datastream / ECB, Edmond de Rothschild (Suisse)



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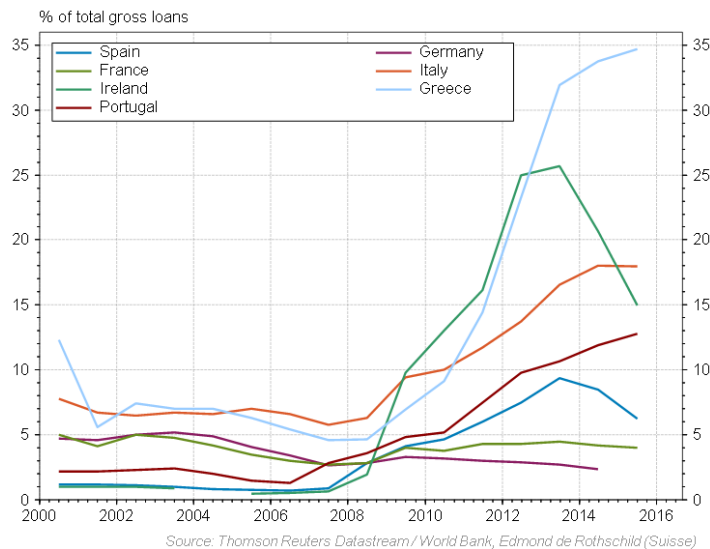
**However, strong disparities among individual countries paint a more mixed picture.** Bank lending is especially firm in core eurozone countries. For example, loans to non-financial corporations showed annual growth of 5.3% in France and 2.9% in Germany in July, but in peripheral countries this type of lending continued to contract. In July, the annual growth rate in loans to non-financial corporations was -0.2% in Italy, -0.8% in Spain and -1.4% in Portugal.

These divergent trends do not call into question the effectiveness of monetary policy, but they do show that its effects are not the same across the board. **The root of the problem lies in the non-performing loans carried by banks in peripheral countries, which hamper the banks' ability to create new loans.** At the



end of 2015, non-performing loans represented 18% of banks' total loan portfolio in Italy, 6.3% in Spain and 12.8% in Portugal.

The proportion of non-performing loans remains high in peripheral countries



**This situation will dilute the effectiveness of any further monetary easing.** Constrained by the size of their portfolio of non-performing loans, banks in these countries cannot create much in the way of new loans despite the highly attractive terms offered by the ECB. At the same time, the ECB's corporate bond purchases (under its CSPP programme) will not become a substitute for bank lending, because it is mainly large and medium-sized corporations that are currently in a position to issue debt that is eligible for the ECB's purchase programme.

**We expect the ECB to announce further measures on 8 September**, such as extending the bond purchase programme beyond March 2017 and revising the rules concerning the weighting of these purchases by country in order to expand purchases in peripheral countries. **But bank lending across the eurozone will only improve if the ECB acts more decisively in its banking supervisory role.** In order to cement long-term growth, European officials will have to develop tools – along the lines of the Paulson plan put in place in 2008 in the USA – that will speed up the process of cleaning up bank balance sheets. Adopting a uniform definition of non-performing loans in the eurozone, which would lead to a market for these securities – as Mario Draghi called for in July – would be a useful, albeit insufficient, first step.





## OUR GROWTH AND INFLATION FORECASTS

REAL GDP GROWTH (%)	2013	2014	2015	2016f	Consensus	2017f	Consensus
United States	1.5	2.4	2.4	1.9	1.5	2.2	2.2
Japan	1.4	-0.1	0.6	0.7	0.5	1.3	0.7
Eurozone	-0.2	0.9	1.5	1.7	1.5	1.1	1.2
Germany	0.4	1.6	1.4	1.6	1.6	1.2	1.3
France	0.6	0.6	1.3	1.4	1.3	0.9	1.1
Italy	-1.8	-0.3	0.6	1.1	0.8	1.1	0.9
Spain	-1.7	1.4	3.2	2.8	2.8	2.2	2.0
Portugal	-1.1	0.9	1.5	1.2	1.1	1.6	1.3
Luxembourg	4.4	4.1	4.9	3.7	3.4	4.1	2.7
Europe ex-Eurozone							
United Kingdom	1.9	3.1	2.2	1.0	1.5	-0.2	0.6
Switzerland	1.8	1.9	0.9	1.1	1.0	1.2	1.4
Sweden	1.2	2.4	3.8	3.6	3.2	2.9	2.4
Israel	3.2	2.7	2.5	2.8	2.6	3.0	3.1
Emerging Markets							
China	7.7	7.3	6.9	6.5	6.5	6.0	6.3
Brazil	3.0	0.1	-3.9	-4.3	-3.5	0.7	1.0
India	6.3	7.0	7.3	7.5	7.5	7.3	7.7

CONSUMER PRICE INDEX (%)	2013	2014	2015	2016f	Consensus	2017f	Consensus
United States	1.5	1.6	0.1	1.3	1.3	2.3	2.2
Japan	0.4	2.7	0.8	0.2	-0.1	0.6	0.7
Eurozone	1.4	0.4	0.0	0.2	0.3	1.1	1.3
Germany	1.6	0.8	0.1	0.5	0.4	1.3	1.5
France	1.0	0.6	0.1	0.3	0.3	0.8	1.2
Italy	1.2	0.2	0.1	0.1	0.0	0.8	1.0
Spain	1.5	-0.2	-0.6	-0.1	-0.4	0.9	1.2
Portugal	0.4	-0.2	0.5	0.6	0.6	1.3	1.2
Luxembourg	1.7	0.7	0.1	0.7	0.0	1.4	1.7
Europe ex-Eurozone							
United Kingdom	2.6	1.5	0.0	1.4	0.7	3.5	2.2
Switzerland	-0.2	0.0	-1.1	-0.5	-0.5	-0.1	0.3
Sweden	0.4	0.2	0.7	0.9	0.9	1.5	1.6
Israel	1.5	0.5	-0.6	-0.3	-0.3	1.2	1.2
Emerging Markets							
China	2.6	2.0	1.4	2.1	2.0	2.4	2.0
Brazil	6.2	6.3	9.0	8.9	8.6	7.3	5.6
India	9.9	6.7	4.9	5.1	4.9	4.8	5.3



## OUR MONETARY POLICY FORECASTS

KEY RATES (%)	2013	2014	2015	2016f	Consensus	2017f	Consensus
United States	0.25	0.25	0.50	0.75	0.70	1.25	1.00
Japan	0.10	0.10	0.10	-0.10	-0.10	-0.10	-0.20
Eurozone	0.25	0.05	0.05	0.00	0.00	0.00	0.00
Europe ex-Eurozone							
United Kingdom	0.50	0.50	0.50	0.25	0.10	0.25	0.10
Switzerland	0.00	-0.25	-0.75	-1.00	-0.80	-1.00	-0.85
Sweden	0.75	0.00	-0.35	-0.50	-0.55	0.00	-0.50
Israel	1.00	0.25	0.10	0.10	0.15	0.50	0.75
Emerging Markets							
China	6.00	5.60	4.35	3.85	4.15	3.35	4.10
Brazil	10.00	11.75	14.25	14.00	13.60	13.50	11.30
India	7.75	8.00	6.75	6.50	6.40	6.50	6.35

## OUR CURRENCY FORECASTS

FOREIGN EXCHANGE*	2013	2014	2015	2016f	Consensus	2017f	Consensus
Dollar							
EUR/USD	1.37	1.20	1.08	1.08	1.09	1.04	1.10
USD/JPY	105	120	120	116	105	121	110
GBP/USD	1.66	1.56	1.47	1.24	1.27	1.20	1.32
USD/CHF	0.89	0.99	1.00	1.00	0.99	1.00	1.00
USD/CNY	6.05	6.21	6.49	6.70	6.75	6.90	6.80
Euro							
EUR/JPY	144	144	130	125	114	126	121
EUR/GBP	0.83	0.77	0.73	0.87	0.86	0.87	0.83
EUR/CHF	1.23	1.20	1.09	1.08	1.08	1.04	1.10
EUR/SEK	8.85	9.44	9.17	9.53	9.29	9.60	8.90

\*end of period data



## RETURNS ON FINANCIAL ASSETS

### Major benchmarks and currencies

Markets Performances (local currencies)	Last Price	1-Week (%)	1-Month (%)	Year-to-Date (%)	Last Year (%)
<b>Equities</b>					
World (MSCI)	421	0.8%	1.6%	7.6%	-1.8%
United States (S&P 500)	2'180	0.6%	1.3%	8.3%	1.4%
Euro Area (DJ EuroStoxx)	332	2.3%	3.5%	-0.9%	11.2%
United Kingdom (FTSE 100)	6'855	0.6%	2.0%	13.8%	-1.4%
Switzerland (SMI)	8'324	1.5%	1.4%	-2.4%	1.1%
Japan (NIKKEI)	17'082	1.8%	4.5%	-9.5%	11.0%
Emerging (MSCI)	910	1.6%	3.0%	16.9%	-14.6%
<b>Bonds (Bloomberg/EFFAS)</b>					
United States (7-10 Yr)	1.59%	-0.3%	-0.8%	6.6%	2.1%
Euro Area (7-10 Yr)	-0.08%	-0.1%	-0.1%	6.6%	1.0%
Germany (7-10 Yr)	-0.08%	-0.3%	-0.1%	7.4%	0.9%
United Kingdom (7-10 Yr)	0.67%	-0.3%	0.2%	10.7%	0.7%
Switzerland (7-10 Yr)	-0.48%	-0.3%	-0.6%	3.3%	3.7%
Japan (7-10 Yr)	-0.02%	-0.3%	-0.6%	2.6%	1.4%
Emerging (5-10 Yr)	4.22%	-0.3%	1.0%	12.7%	1.6%
United States (IG Corp.)	2.79%	-0.3%	0.8%	9.3%	-0.8%
Euro Area (IG Corp.)	0.45%	-0.1%	0.2%	5.9%	-0.5%
Emerging (IG Corp.)	3.47%	-0.2%	1.1%	11.4%	-2.3%
United States (HY Corp.)	6.39%	0.1%	1.8%	14.9%	-3.5%
Euro Area (HY Corp.)	3.03%	0.4%	1.5%	7.5%	0.3%
Emerging (HY Corp.)	7.46%	0.2%	1.6%	17.1%	3.6%
United States (Convert. Barclays)	46	0.2%	2.6%	9.1%	-0.8%
Euro Area (Convert. Exane)	7'343	0.6%	0.8%	-2.1%	7.6%
<b>Real Estate</b>					
World (MSCI)	207	0.7%	-0.2%	11.7%	1.0%
United States (MSCI)	219	1.5%	-1.8%	11.4%	4.6%
Euro Area (MSCI)	240	0.8%	0.1%	18.4%	16.1%
United Kingdom (FTSE)	6'568	0.4%	1.1%	-0.4%	9.4%
Switzerland (DBRB)	3'817	0.1%	-1.2%	5.8%	4.6%
Japan (MSCI)	235	0.6%	1.4%	-11.8%	0.9%
Emerging (MSCI)	107	1.0%	1.3%	10.2%	-6.8%
<b>Hedge Funds (Dow Jones)</b>					
Hedge Funds Industry	547	n.a.	1.1%	-0.5%	-0.7%
Distressed	735	n.a.	1.1%	1.0%	-5.3%
Event Driven	587	n.a.	1.5%	-1.0%	-6.3%
Fixed Income	305	n.a.	1.1%	0.9%	0.6%
Global Macro	874	n.a.	0.3%	-1.3%	0.2%
Long/Short	652	n.a.	1.3%	-3.8%	3.6%
Managed Futures (CTA's)	328	n.a.	1.6%	3.7%	-0.9%
Market Neutral	262	n.a.	0.9%	-2.7%	1.7%
Multi-Strategy	530	n.a.	1.1%	1.7%	3.8%
Short Bias	26	n.a.	-8.1%	-14.7%	2.4%
<b>Commodities</b>					
Commodities (CRB)	415	-0.8%	-0.4%	9.3%	-15.2%
Gold (Troy Ounce)	1'335	1.5%	-0.1%	25.7%	-10.6%
Oil (Brent, Barrel)	46	-4.2%	7.9%	30.5%	-35.9%
<b>Currencies</b>					
USD	95.6	-0.4%	-0.6%	-3.0%	9.3%
EUR	1.12	0.1%	0.6%	2.7%	-10.2%
GBP	1.33	2.0%	2.3%	-9.4%	-5.4%
CHF	0.98	0.5%	0.3%	2.3%	-0.8%
JPY	103.4	-0.4%	-0.9%	16.3%	-0.4%

Source : Bloomberg

↑ ↓ Momentum (1-week / 1-month / 3-month)

Performance (Negative \ Positive)





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