

# ECONOMIC ENVIRONMENT

## United States

### STUCK DUE TO THE NECESSARY REDUCTION OF PRIVATE DEBT

The sharp decline of 3.5 points in the ISM manufacturing index in June alone, returning to its level of 6 months ago, is no surprise: off-season inventory growth remained weak at 0.9% in the first quarter, a rate towards which it would be expected to fall in the second half once the growth phase of the inventory cycle is complete. Although world trade is slowing, the US economy remains hampered by a decline in the leverage effect of the banking system and any form of lending: financing conditions remain difficult for all borrowers, with the exception of large companies, for which massive bond issuances benefit from structurally strong demand by US institutional investors, given the ALM problems. By contrast, households are being forced to reduce their debt at an annual rate of 3% of income. For that reason, the residential property market fell heavily after the tax incentives expired, and the savings rate, which was 4% in May, has not yet stopped climbing, a result of sales of household financial assets, which financed consumption earlier in the year. Nevertheless, the government may still count on a high level of investor confidence in US public debt if it has to boost the economy again.

## Euro zone

### EUROZONE SUPPORTIVE OF BUDGETARY RIGOUR, REGARDLESS OF THE VERY DIFFERENT PRIVATE DEBT PROBLEMS FROM COUNTRY TO COUNTRY

GDP is expected to accelerate in the second quarter due to exports, the inventory cycle and a rebound in the construction sector, after the harsh winter earlier in the year. However, growth will then end in the second quarter because of a weakening of domestic demand. Following the announcement of budget-consolidation measures, the economic climate grew worse: the reversal of household expectations presages a continuation of the drop in consumption after an already significant contraction in the first quarter, resulting from the high unemployment rate (10%) and a correction in the automobile market after sales incentives expired. Out of all the countries in the entire Eurozone, Spain is currently the most worrisome, not because of its public debt trend, which in our view is of little concern, but rather because of its inappropriate economic policy. Indeed, Spain is currently suffering from a considerable surplus of private debt, the indispensable absorption of which is already depressing domestic demand. However, the forced reduction of the budget deficit, specifically through salary reductions, is amplifying the debt reduction process, although it will be difficult for the population to accept these sacrifices, as it has already been affected by severe unemployment, which is at an historic high of 20% and will continue to worsen. Spain is entering a very turbulent period, during which the risks weighing on the system are high.

## China

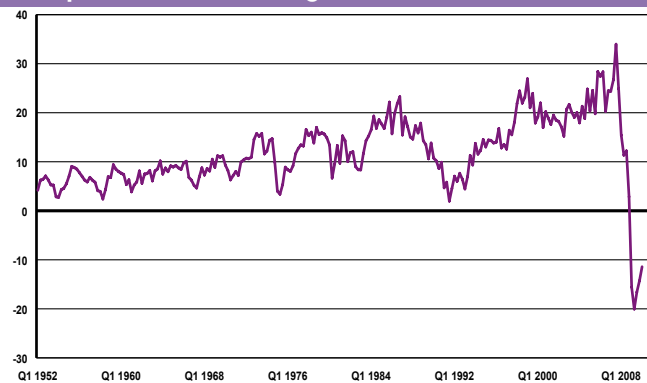
### SEEKING TO PREVENT A REAL ESTATE BUBBLE

Leading indicators show a more marked slowing than we anticipated. A return to more reasonable growth in household consumption, as measured by both retail sales and new car registrations, is not inspiring any concern. In fact, consumer prospects are good, especially given the continuing strong growth in the jobs market, which is evenly distributed among the various provinces. By contrast, the sharp decline in loan production, which was sought by the Chinese authorities and is quite inadequate in their eyes, is problematic. This is because although total loans outstanding are indeed slowing, with repercussions on growth and particularly on investment by companies and provinces, real estate loans outstanding are continuing to accelerate, inflating the real estate bubble, which will significantly reduce long-term growth in China, according to the authorities. Consequently, as long as real estate speculation persists and the real estate market remains turbulent, the monetary authorities will continue to apply a tight monetary policy and reduce bank liquidity, at the risk of excessively softening interest rates on the Chinese markets and causing a severe slowing of their economy.



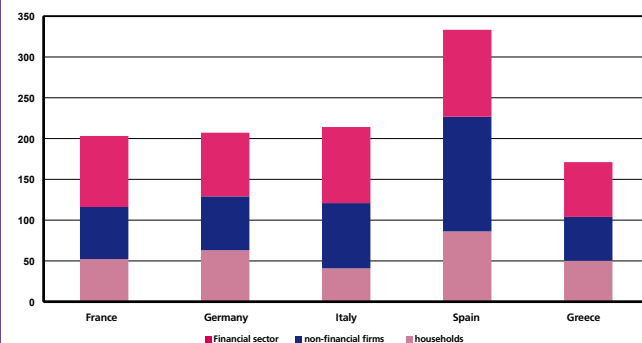
Laurent Berrebi,  
Chief Economist

### United States: Continuing sharp decline in private-sector debt (growth in debt, % GDP)



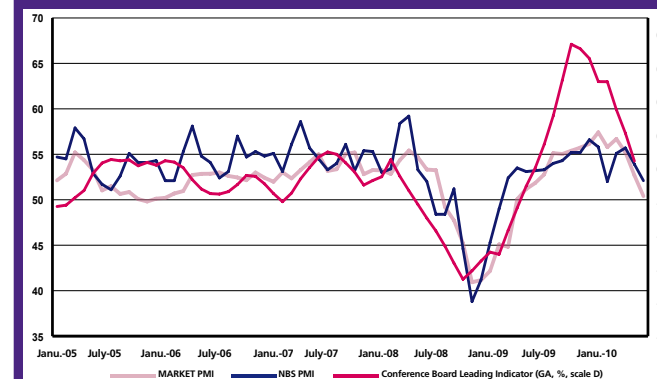
Sources: Datastream, Groupama AM

### Euro zone: private sector debt (% GDP)



Sources: Datastream, Groupama AM

### China: significant reversal in leading indicators



Sources: Datastream, Groupama AM