International developments

Oil and raw materials

The offer is intended to meet market needs

In Q4 2013 the price of a barrel of Brent crude remained high (an average of 109 US$). The decline in production in the OPEC nations and the dynamic demand from OECD countries led to a substantial reduction of oil stocks in developed economies with the exception of the USA, propping up crude oil prices.

In Q1 2014, the physical market should ease up. Demand should slow in OECD countries in the usual seasonal manner. Supply should increase thanks to a rise in OPEC production, particularly in Libya. Unconventional oil production in the USA should also be highly dynamic.

In Q2 2014, the upturn in consumption in emerging markets should drive an increase in global demand, despite the seasonal lull in OECD countries. Production should increase in line with demand, particularly the cyclical production of biofuels. Overall, the price of Brent crude is expected to fluctuate around its current level of $108 per barrel.

Faced with an increase in demand, any delay in the increase of output in the OPEC nations could lead to an increase in crude prices, as OECD stock levels are low. On the other hand, dynamic production by unconventional means or a faster than predicted improvement in the situation in Libya, Iraq or Iran could allow prices to ease slightly. Lastly, a potential decrease in Russian production, if diplomatic tensions should worsen, could contribute to a rise in prices.

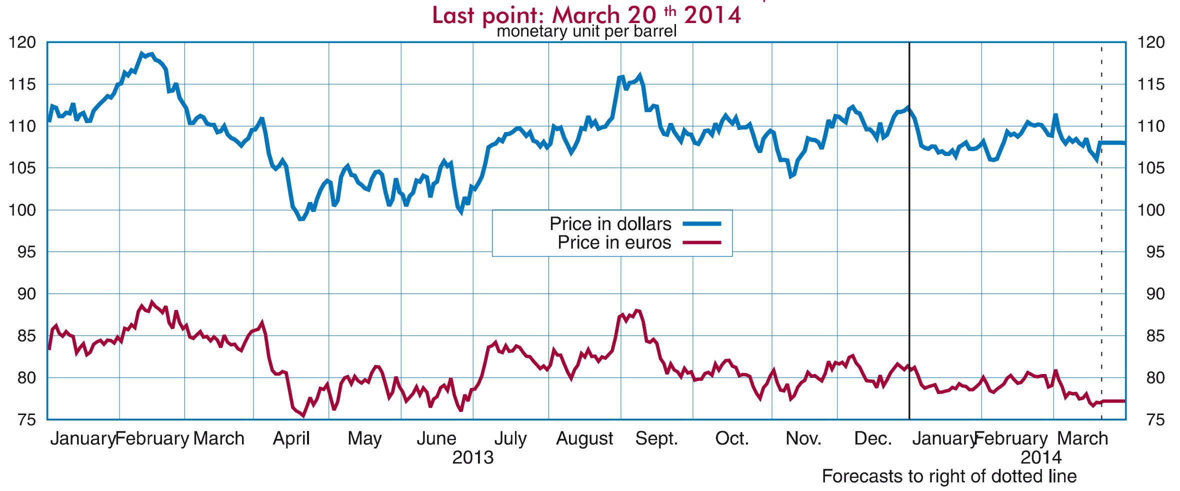
A significant reduction in oil stock levels in Q4 2013

The dynamism of international demand and uncertainties regarding production, linked to the geopolitical situation in the Middle East, helped maintain the price of North Sea oil (Brent) at a high level in Q4 2013 (an average of $109, see Graph 1). The decline in prices, resulting from the partial easing of tensions, was interrupted from November onwards by the renewed dynamism of global demand, particularly in the OECD countries.

Global demand increased (+200,000 bpd) thanks to the seasonal consumption boost in the OECD nations (+200,000 bpd). Demand was particularly robust in Japan (+400,000 bpd), bolstered by strong activity levels in the petrochemical industry. Rising demand for industrial fuels led to an increase in overall energy demand in the USA (+100,000 bpd), particularly from the petrochemical and agricultural sectors. In Europe, non-stock demand for crude oil declined (-400,000 bpd) as the economic recovery remained tentative. Furthermore, consumption in non-OECD countries declined (-100,000 bpd).

At the same time, world oil supply remained practically stable (-100,000 bpd). Production decreased in the OPEC nations (-800,000 bpd). Despite a slight, temporary rebound in October, Libyan production remains very low, and in November 2013 reached its lowest level since September 2011 (220,000 bpd). Production also remained low in Iraq and Iran, where sanctions remained in place despite the agreement reached

1 - Price of *Brent* in € and in $
Last point: March 20 th 2014



Source: Commodity Research Bureau

with Western powers in November. Moreover, production saw a seasonal decline in Saudi Arabia (see Graph 2). Conversely, production was dynamic in OECD nations (+400,000 bpd).

In Q1 2014, demand should stall while supply should remain dynamic

On the physical market, non-stock demand should fall by 1 million bpd. This decline should be a result of the seasonal drop-off in demand from the OECD nations, but also in the USA (-300,000 bpd). As a result of maintenance work, the output of refineries should remain low during this period. Furthermore, demand should subside after the peak caused by the dynamic consumption of Q4 2013, while stock levels should remain high. Demand should also fall in Europe (-400,000 bpd), with the seasonal reduction in energy use outweighing the limited growth seen in the Eurozone. Demand from non-OECD countries should also shrink (-400,000 bpd), particularly as a result of the slowdown in the Russian economy.

Meanwhile, crude oil supply should pick up by around 400,000 bpd, as production by the non-OPEC producers remains dynamic, particularly in the USA (+500,000 bpd), while also increasing slightly in the OPEC countries. The completion of maintenance work on Iraqi production facilities, which saw a production increase of 500,000 bpd in February 2014, should allow the oil cartel to increase total crude production (+200,000 bpd) and reach its declared target of 30,000,000 bpd.

Supply and demand should both be dynamic in 2014

In Q2 2014, oil supply should increase further (+500,000 bpd). Liquefied natural gas production should grow in the OPEC nations (+100,000 bpd) and OPEC's crude oil production target (30,000,000 bpd) should be met. Outside OPEC, production will be largely sustained by the dynamism of biofuel supply (+400,000 bpd).

Non-stock demand for oil should also increase (+700,000 bpd), as consumption grows in emerging economies (+1.5 Mbpd), while demand should actually contract in the OECD nations (-700,000 bpd): the drop-off in Japanese consumption after the winter (-900,000 bpd) is not expected to be offset by the increased dynamism of European demand (+300,000 bpd).

The price of oil should hover around $108 per barrel of Brent over the forecasting period

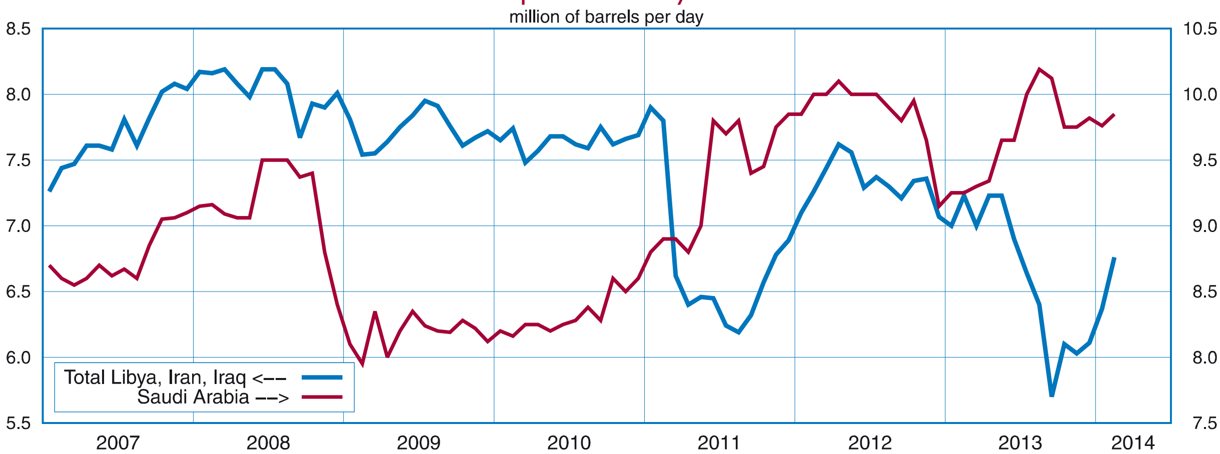
The price of a barrel of Brent crude is expected to fluctuate around the $108 mark between now and June 2014. This hypothesis corresponds closely to recent market prices (an average of $109/barrel in February). Production should be dynamic in the OPEC nations and the USA, meeting demand. Nonetheless a potential decrease in Russian production, if the diplomatic situation continues to deteriorate, could fuel a price increase.

Light fluctuations in industrial commodity prices

Industrial metal prices rose again in Q4 2013. Copper prices in particular saw a slight increase (see Graph 3), in response to strong consumption in emerging economies, particularly China, before falling back in Q1 2014. Aluminium prices, meanwhile, continue to fall as a result of the high levels of stock held by China.

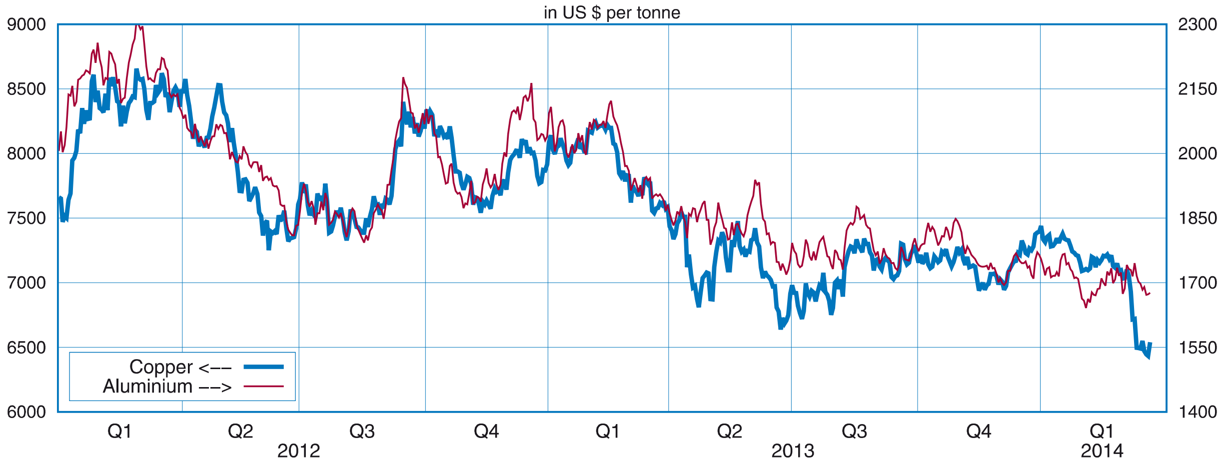
The sizeable variations in global supply of various commodities have led to significant price developments. Abundant harvests have thus prompted substantial reductions in cereal prices, particularly wheat and corn.■

2 - Oil production in Saudi Arabia, Libya, Iran and Iraq
Last point: February 2014



Source: AIE

3 - Prices of industrial metals
Last point: March, 21 st 2014



Source: London Metal Market

Financial markets

Monetary policy at a crossroads

With the global recovery gathering pace, the question of when monetary policy will be tightened is becoming ever more pressing. In the USA, the Fed began reducing the volume of its monthly securities purchasing in December 2013, a first step towards an eventual end to quantitative easing. This tightening in the US prompted a monetary and market crisis in emerging economies with current account deficits. Monetary policy remains highly accommodating in the United Kingdom, but faced with the substantial reduction in unemployment the Bank of England may well opt for a change of strategy in the near future. Meanwhile the European Central Bank (ECB), faced with a fragile recovery and weak inflation, has decided not to change the course of its monetary policy. The ECB is still ensuring easy access to liquidity. While sovereign debt financing conditions continue to become more favourable, particularly for the EU's peripheral nations, this improvement in credit conditions has barely filtered through to firms.

On the currency markets, the Euro remains strong against the dollar despite the reduction in the Fed's efforts to prop up the American economy. Over the forecasting period, the conventional assumptions for exchange rates against the Euro are: 1.38 dollars, 140 yen and 0.83 pounds.

The Fed starting to reduce its support for the American economy

As the recovery continues, the central banks of the major advanced economies continue to apply monetary policies which are largely expansionary. However, the short-term prospects remain mixed and the monetary institutions are thus faced with different priorities. In the USA, the Federal Reserve has made several successive reductions (January and February 2014, then again in April 2014) to the volume of its monthly securities purchases, thus beginning the strategic reduction of its support for the American economy, scheduled since spring 2013. In April 2014, the Fed will buy just 25 billion dollars' worth of mortgage-backed securities (MBS) and 30 billion dollars of Treasury bonds, a total reduction of 30 billion dollars on the levels seen in 2013. Despite the substantial reduction in unemployment, which stood at 6.7% in February, the base rate should remain unchanged at 0.25% over this forecasting period, as it has done since September 2009, in accordance with the declarations made by the Fed.

An expansionist monetary policy is still in place in the Eurozone, in order to ensure favourable refinancing conditions for the European banks. These conditions should indeed remain favourable, in spite of early repayment of some of the extra-long-term loans granted by the ECB to the banks in late 2011 and early 2012, and as such the most likely scenario is that the ECB will not need to take any more non-standard measures on the interbank market during this forecasting period. The ECB is nonetheless concerned by the weak inflation seen in the Eurozone, although the central bankers remain convinced that their anticipation of a rise in inflation in the medium term is well-founded. The ECB has made it clear that its base rate, fixed at 0.25% since November 2013, should remain stable over the forecasting period.

In the United Kingdom, the Bank of England (BoE) has not been practising quantitative easing since summer 2012, but its monetary policy remains highly accommodating (a base rate of 0.5%, a programme encouraging lending to businesses). Having fallen substantially, the rate of unemployment is now approaching the threshold at which the BoE had announced that it would begin raising interest rates, a turn of events which has prompted the Bank to minimise the significance of the unemployment rate and draw attention to a broader panoply of indicators suggesting underuse of production capacities. In Japan, the central bank continues to pursue the highly expansionist monetary policy inaugurated in early 2013 in an effort to put an end to deflation (the Bank of Japan has fixed a long-term inflation target of 2%). The Japanese central bank thus continues to expand the monetary base at an annual rate of 60 to 70 billion yen (approximately 15% of GDP per year). The base rate remains stable at 0.1%.

Imbalances persist on the European money market

The working of the Eurozone interbank market is largely defined by the important role of the ECB. Banks are still largely refinancing via loans granted by the ECB in late 2011 and early 2012, with the volume of day-to-day lending between banks remaining low, along with the interest rates. Uncertainty regarding the banks' capacity to lend to one another without support from the ECB, as the surplus liquidity begins to ebb away, has nonetheless sparked a slight upturn in interest rates and in the volatility of the interbank market.

Furthermore, the interbank market remains fragmented: refinancing conditions for banks are more favourable in those countries at the heart of the Eurozone (e.g. Germany and France), where the banks have been able to turn to the interbank market again, than they are in the peripheral nations (particularly Spain and Italy). The renationalisation of financing channels has knock-on effects on the financing conditions available to non-financial enterprises in the various European economies, and continues to limit the effects of the ECB's monetary policy. The disparity between the low rates available to French and German businesses and the higher rates charged to Italian and Spanish companies has thus not improved for small businesses.

Lending still sluggish in the Eurozone

In the Eurozone, the conditions of financing via bank lending remained difficult in Q1 2014. In February outstanding bank lending to non-financial corporations fell (a 3.1% year-on-year reduction, *see Graph 1*), as it has done every month for the past year and a half. According to the ECB's Eurozone lending survey, the banks who responded indicated that they had further tightened their conditions for lending to businesses in Q4 2013, but that this tightening had been more moderate over the past four quarters as business prospects continued to improve. In France, outstanding loans to non-financial enterprises increased slightly in Q1 2014 (1.0% in February in year-on-year percentage change). While business lending and consumer credit remain robust, the mortgage market continues to show the signs of weakness which appeared in Q3 2013: the rate of new property lending has been in continuous decline since August 2013.

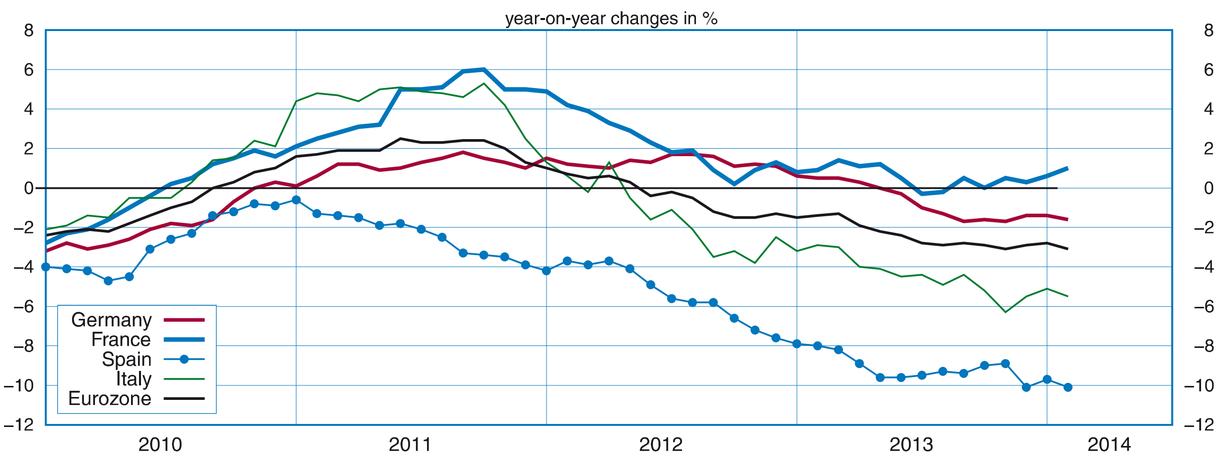
The European sovereign debt market continues to ease up

The return to normal conditions for the financing of European sovereign debt continued in Q4. France and Germany currently enjoy excellent financing conditions on the secondary market. Despite a slight tightening of financing conditions since the start of 2013, American sovereign debt is also trading at very low rates of interest, as is British sovereign debt. Financing conditions for Spanish and Italian sovereign debt have eased: both countries are now able to lend at rates below 5%. Financing conditions for Portuguese sovereign debt have also improved significantly, and the government is planning to exit the Troika's bailout programme in June 2014. The interest rates applied to Greek debt on the secondary market continue to subside, but the country is still not in a position to issue long-term sovereign bonds.

Stock markets remain restive

After a sustained increase throughout 2013, the stock market indices in the advanced economies stalled at the start of Q1 2014, and their volatility increased. This unease can be attributed to the

1 – Outstanding bank lending to non-financial enterprises in the Eurozone
(Last point: February 2014)



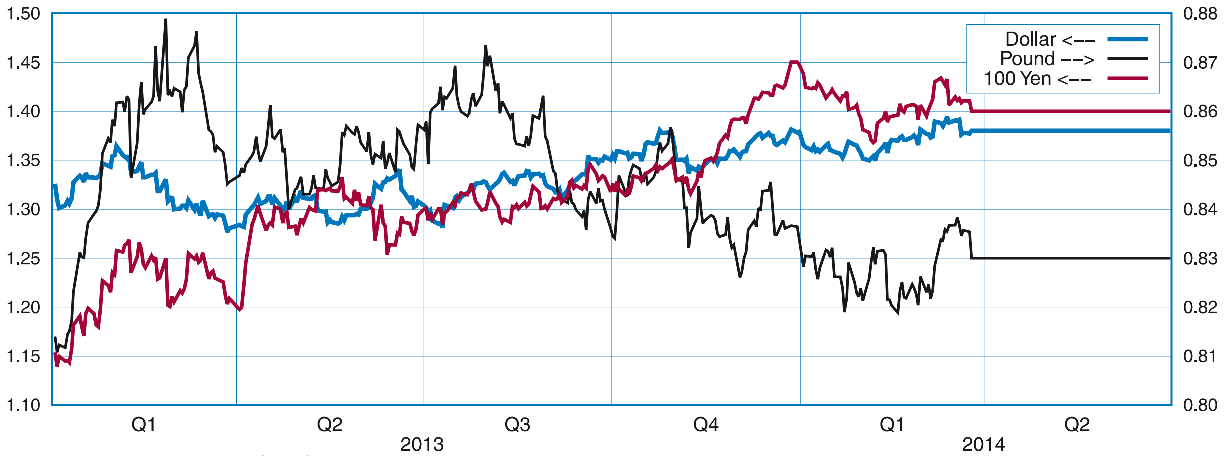
Source: European Central Bank

stock market crisis which hit emerging economies in Q1 2014. In the wake of the Fed's decision to adopt a more restrictive monetary policy, and with the economic outlook less favourable than expected, the stock market indices in emerging economies dropped off from their levels of Q4 2013, a correction on a comparable scale to that seen in summer 2013. As a result of the slowdown - which has now come into effect - in money creation in the USA, foreign capital invested in emerging markets has been repatriated, inducing considerable currency devaluation and a decline in the stock market indices in some emerging nations (Russia, Turkey, Argentina). In an attempt to shore up their currencies the central banks have intervened, most notably by raising their base interest rates.

The Euro remains strong against the dollar

Despite the slowdown in American quantitative easing, the Euro remains strong against the dollar in Q1 2014 (*see Graph 2*). The capital withdrawn from emerging economies seems to have been predominantly reinvested in the Eurozone, as the interest rate and growth perspectives remain more favourable than those seen in the USA. The value of sterling has risen noticeably since mid-2013, bolstered by the British recovery, while the yen remains weak against the Euro as a result of the massive quantitative easing programme put in place by the Japanese central bank. Faced with the drop-off in growth in China, the monetary authorities have allowed the yuan to depreciate against the dollar, to the extent that the Chinese currency reached its lowest value for more than a year in March 2014.■

2 – Euro exchange rates
Last point: March, 24th 2014



Source: European Central Bank

Eurozone

The recovery is gradually gaining a firmer footing

In Q4 2013 activity accelerated in the Eurozone (+0.3% after +0.1% in Q3) as the result of a rebound in investment and exports.

According to business tendency surveys, activity should generally continue to recover, but at a slower rate. Growth in the Eurozone should thus be slightly more dynamic in H1 2014 than it was in H2 2013 (+0.4% in Q1 2014 and +0.3% in Q2, compared to +0.4% across the whole of H2 2013).

Indeed consumption should be bolstered by the increase in purchasing power. Above all, with the improvement in activity and employment perspectives, households should reduce their precautionary savings. Consumption should thus increase slightly more rapidly than purchasing power.

Moreover, a return to growth and the need to renew production capacities after a phase of considerable adjustment should continue to boost investment in equipment. In the construction sector the decline in investment should be reduced, the result of a tentative rise in confidence levels.

Exports should progress at a steady rate, as should imports, sustained by internal demand, and the contribution of foreign trade to growth should be neutral.

All in all, the growth overhang for 2014 at the end of June should be clearly positive at +0.9%, following two years (2012 and 2013) of declining activity.

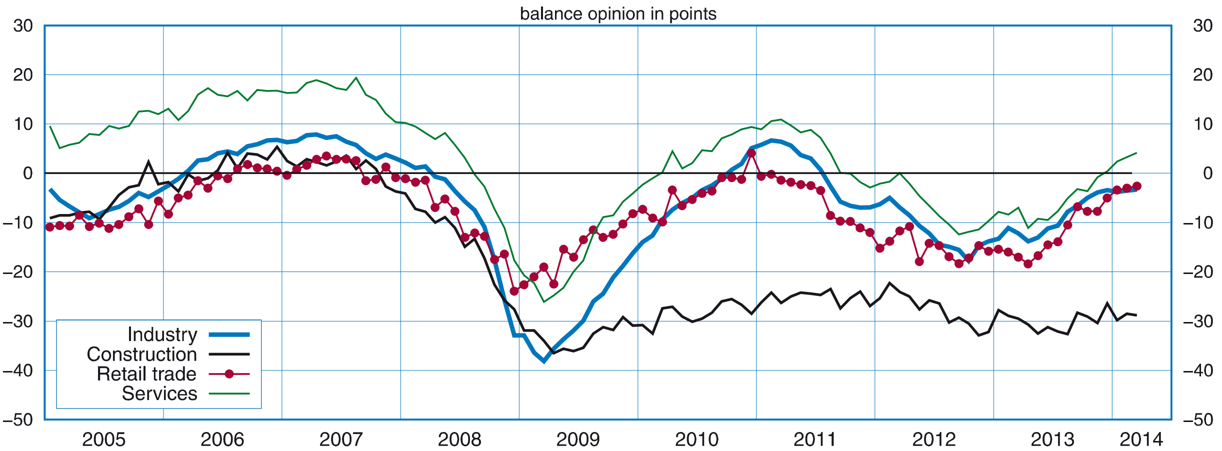
Moderate growth in Q4 2013

In Q4 2013 the GDP of the Eurozone increased by 0.3%, as predicted in our Conjoncture in France published in December 2013. After three consecutive quarters of growth, the Eurozone has now definitively moved out of recession, and activity has even accelerated from its Q3 level (+0.1%). While household consumption has grown only slightly (+0.1%), investment has shown a clear improvement (+1.1% after +0.6% in Q3). Exports have rebounded (+1.2% after 0.0%) while imports have slowed (+0.4% after +1.0%). All in all, the positive contribution of foreign trade has more than compensated for the negative contribution of stocks (+0.4 points and -0.3 points respectively), an exact inversion of the situation seen in Q3 (-0.4 points v. +0.3 points).

The rebound should continue in H1 2014

According to the business tendency surveys published by the European Commission, activity has been increasing since spring 2013 in the industrial, retail and service sectors (see Graph 1). The deterioration of the business climate in the construction sector has halted in early 2014, but the surveys remain at a very low level. Activity in the Eurozone should thus pick up again in H1 2014 (+0.4% in Q1 then +0.3% in Q2), supported by domestic demand as fiscal consolidation efforts are relaxed.

1 - Confidence index by sector



Source: European commission

Spain, France and Italy should experience similar rates of growth, but activity in Germany should remain more dynamic across the forecasting period.

Private sector consumption picks up

Taking productivity gains into account, the rate of growth in economic activity is unlikely to be sufficient to trigger a rebound in employment, which should remain stable in H1 2014. As the labour force should remain constant, the unemployment rate (12% in January 2014) should remain unchanged over this forecasting period.

Nominal wages should see a moderate increase in H1 2014, with a slight increase in France and Spain and a more substantial rise in Germany. Furthermore, fiscal consolidation efforts should be reduced significantly. Purchasing power, which seems to have dropped off slightly in late 2013, should therefore see limited growth over this forecasting period (a year-on-year increase of 0.5% in H2 2014, compared with a decline of 0.9% in H2 2013).

Above all, with the upturn in activity and employment perspectives, households should continue to reduce their precautionary savings (see Graph 2). Consumption should thus increase (+0.2% in Q1 2014 and +0.4% in Q2, with a sharp profile in France) and the savings ratio should decrease (from 12.4% in Q4 2013 to 12.1% in Q2 2014).

Rebound in investment held back by the construction sector

The gradual acceleration of economic activity, as predicted by entrepreneurs on the basis of their responses to business tendency surveys, and the need to renew production capacities after a phase of adjustment, should sustain the acceleration of investment in equipment.

Investment in construction, meanwhile, should remain virtually stable in Q1 2014, particularly as a result of the mild winter in Germany. Levels of confidence in the construction industry are no longer in decline, but they still remain very low. Investment in construction should see another slight decrease in Q2 as a result of the strong Q1.

Foreign trade no longer contributing to growth

Exports should rise more rapidly than the general growth in international trade in H1 2014, based on the assumption that the increase in market share seen over the past three years continues.

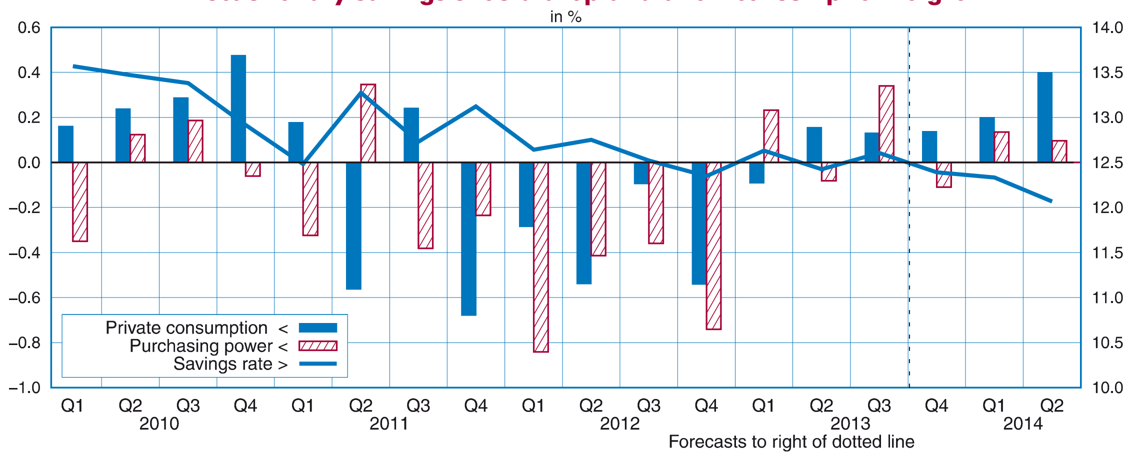
In line with the rebound in domestic demand and the dynamism of exports, imports should increase at the same rate. All in all, the contribution of foreign trade to economic growth should be neutral.

Inflation should not decline any further

In February 2014, headline inflation stood at +0.7% year-on-year. It should rise slightly to +0.8% in June 2014, bolstered by energy price rises. Based on the assumption that the price of a barrel of Brent crude should remain stable at $108 (€78.30), and as the decline observed in spring 2013 drops off the one-year window, the year-on-year variation in energy prices should see an increase standing at 0.6% by June 2014, after -2.3% in February.

Furthermore, with the lack of inflationary pressure resulting from the high rate of unemployment in most Eurozone countries, core inflation should remain low at +0.9%.■

2 – Precautionary savings should drop and allow consumption to grow



Sources: Eurostat, INSEE calculations and forecasts