ECONOMIC OUTLOOK · The US continues to perform well while doubts increase regarding the emerging economies

The US is still leading the global recovery. Developments in the economic situation of almost all advanced countries were as expected in July and August but this was not the case of most of the emerging countries whose latest activity figures have been weaker than forecast. In the case of China, uncertainty has grown regarding the rate at which its economy is slowing down although we still believe the government can engineer a soft landing. On the other hand serious recession in Russia and Brazil, within a complicated political context, has increased mistrust towards emerging economies as a whole.

UNITED STATES

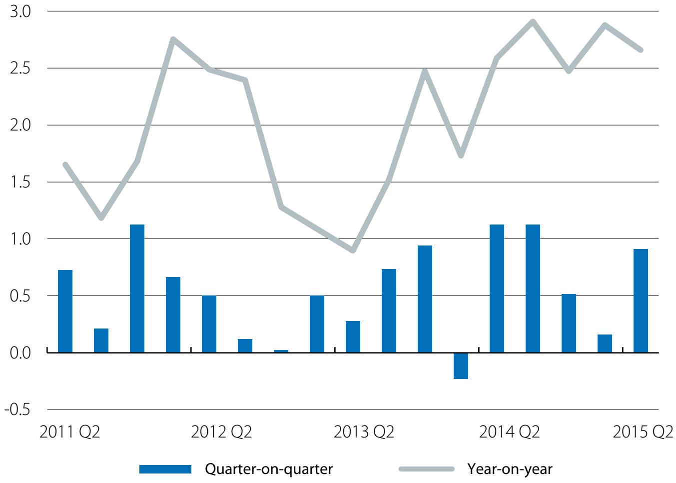
Growth in the US economy speeded up in 2015 Q2. In the US GDP rose significantly by 0.9% quarter-on-quarter in 2015 Q2, 2.7% in year-on-year terms, after a substantial upward revision. The revision for growth in Q1 was also considerable (from 0.0% quarter-on-quarter to +0.2%). By demand component, of note was the positive contribution made by private consumption whose rate of growth accelerated compared with Q1, and also exports which advanced strongly after the disruption caused by the west coast dock strike during the first few months of the year. The relative weakness of capital goods investment can be explained by the after-effect of high spending on equipment during the first nine months of 2014. Business confidence indicators also suggest this weakness will be short-lived.

The revised GDP figure for the last three years has resulted in slightly lower underlying growth. Together with the growth figures for 2015 Q2, the Bureau of Economic Analysis presented its usual revision of the GDP series for the last three years. The change caused by the downward revision of the annual average growth figure for GDP between 2012 and 2014, from 2.3% to 2.0%, is largely due to lower rates in private consumption. On the other hand, this revision did not entirely resolve the problems of seasonality attributed to the series produced by the government institution. Although the difference between average GDP growth in Q1 and the rest of the quarters has been reduced (from 1.2 points to 0.7 points currently), the gap is still significant.

Recent business indicators point to a continued recovery in Q3. The consumer confidence index produced by the Conference Board picked up in August and broke through the threshold of 100 points thanks to improved expectations and the perception of a stronger labour market. Although retail sales only saw moderate growth in July, the upward revision

US: GDP

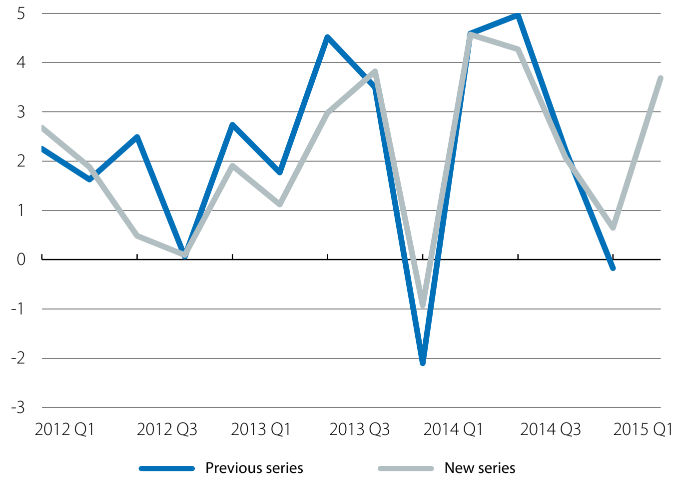
Year-on-year and quarter-on-quarter change (%)



Source: *"la Caixa" Research, based on data from the Bureau of Economic Analysis.*

US: revision of GDP

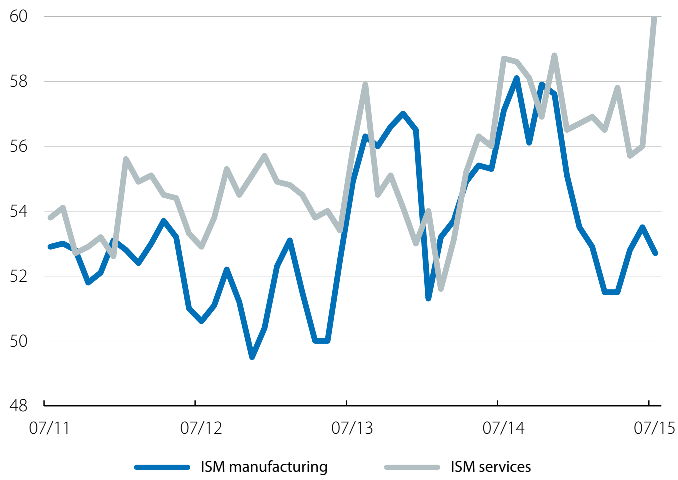
Annualised quarter-on-quarter growth (%)



Source: *"la Caixa" Research, based on data from the BEA.*

US: business sentiment indicators

(Level)



Source: *"la Caixa" Research, based on ISM data.*

of the previous month also means the indicator points to a favourable situation. Business sentiment indices (ISM) for manufacturing and services continue to be in the expansionary zone and suggest good prospects for investment. The ISM for manufacturing dipped slightly to 52.7 points, which corresponds with GDP growth close to 3% while the more robust ISM for services, which account for 85% of private employment, climbed to 60.3 points, a level that coincides with growth in the economy of more than 5%. Lastly the real estate sector continued its sustained recovery with positive figures for new homes started and property sales, while June's weakness in the Case-Shiller price index for second-hand residential properties should be interpreted as a temporary glitch.

Employment once again enjoys a good month although wage rises have yet to materialise in July. 215,000 net jobs were created, a figure indicative of a strong market. The unemployment rate also remained stable at a low 5.3% and the broad unemployment rate (the U6), which includes under-employment (those working part-time involuntarily for economic reasons), fell by 0.1 pps to 10.4%. Such solid job creation and consolidated economic recovery in the US would suggest it is a good time to start raising interest rates. However, financial instability, falling commodity prices, the dollar's appreciation and the absence of inflationary pressures (wage rises remain at a contained 2.1% year-on-year) advise patience. The first interest rate hike will therefore probably be postponed until the end of 2015.

Inflation remains moderate, similarly to wages. July's general CPI slowed down compared with May and June in month-on-month terms, pointing to a situation of very moderate price rises which is also likely to continue given the recent fall in oil prices. Along the same lines core inflation, which excludes food and energy, also slowed up its rate of growth and recorded a subdued rise month-on-month (0.1%). In year-on-year terms the advance stands at 0.1% for the general index and at 1.8% for the underlying figure.

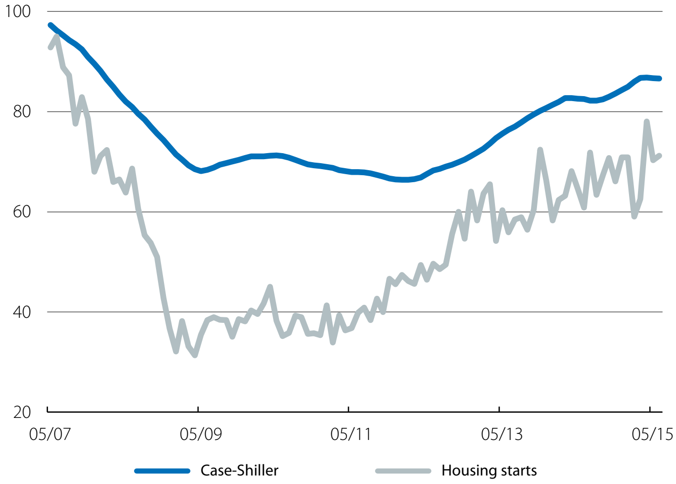
JAPAN

Economic activity declines in 2015 Q2. Japan's GDP fell by 0.4% quarter-on-quarter in 2015 Q2 (+0.7% year-on-year), a worse figure than predicted by our central scenario. Weaker private consumption than suggested by the last indicators and a decline in exports due to the downward slide in demand from China (which accounts for 18% of all exports) were the most negative factors. Nonetheless the slight upward revision for GDP in 2015 Q1 has improved the final balance. We also expect more robust growth in the second half of the year than in the first.

Improved business confidence and contained inflation will support the Japanese economy. The good figures for the Tankan business sentiment index for large firms, both in services and manufacturing, point to an improvement in

US: construction and house prices

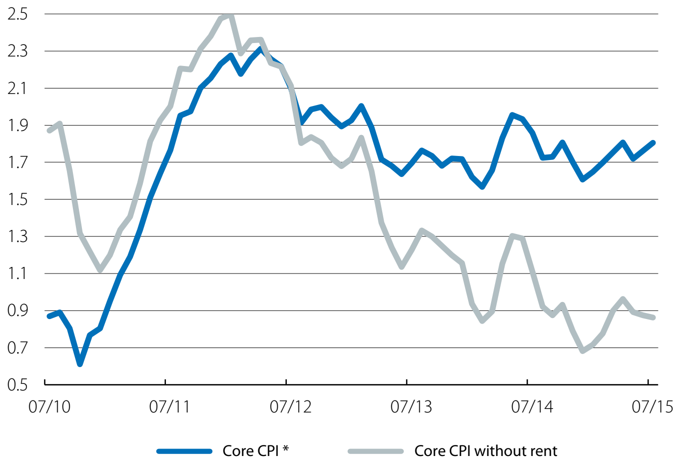
Index (100 = April 2006)



Source: *"la Caixa" Research, based on data from the US Census and Standard & Poor's.*

US: CPI

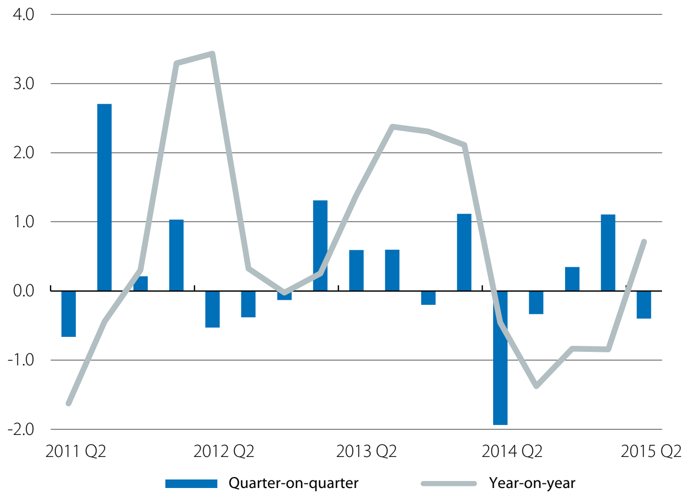
Year-on-year change (%)



Note: ** Core: general index without energy or food.*
Source: *"la Caixa" Research, based on data from the Bureau of Labor Statistics.*

Japan: GDP

Year-on-year and quarter-on-quarter change (%)



Source: *"la Caixa" Research, based on data from the Ministry of the Interior and of Communication.*

investment expenditure. The stagnation in prices, largely due to falling oil prices, should also boost private consumption as it will help households by offsetting the absence of wage rises.

EMERGING ECONOMIES

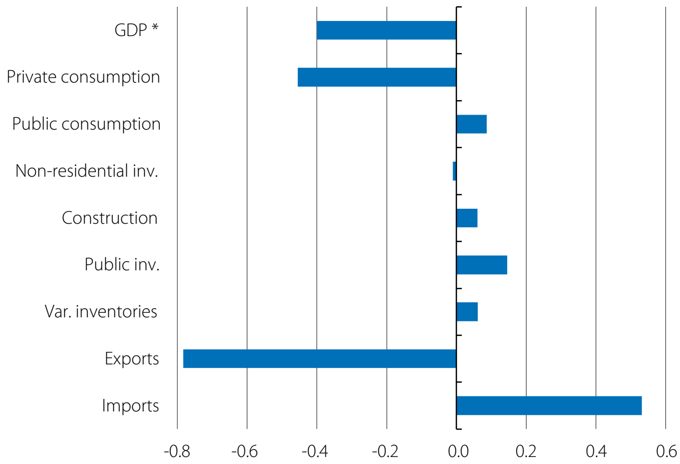
China is the centre of attention during the summer. Heavy stock market losses (close to 40%) and the weakness of the latest activity indicators (PMI and industrial production) forced the country's authorities to act. Of note is the devaluation of the renminbi (3% against the dollar), a further cut in the official interest rate (to 4.60%, the fifth since November) and the reduction in the cash reserve ratio. However, far from calming investors these measures seem to have increased doubts regarding the Asian economy's real state of health. In this respect our main scenario continues to predict a soft landing for the economy although the downside risks have grown significantly.

The situation in Brazil and Russia has worsened, dragged down by political instability. The growing uncertainty regarding emerging economies has also been fuelled by the deterioration of these two large countries. Brazil's GDP fell by 2.6% year-on-year in 2015 Q2, much further than expected. In addition to this drop were serious inflationary tensions (9.6% year-on-year in July) and a high current account deficit (4.5% of GDP in Q1). Given this context, there is no more room for expansionary policies and the already precarious situation faced by President Dilma Rousseff is now worse. For its part the Russian economy declined by 4.6% in 2015 Q2, also deteriorating more than expected. The rouble crisis, Ukraine conflict and low oil prices, which particularly hurt Russia, suggest that both 2015 and 2016 will be difficult.

India is the exception to doubts regarding the emerging economies. The country grew by 7.0% in 2015 Q2, a figure that, although somewhat lower than the growth achieved in Q1 and consensus forecasts, is in line with our main scenario. Prices are still under control in this context of significant growth: inflation stood at 3.8% in July, far below the 7.2% of 2014. Since the elections in May 2014, India has enjoyed political stability and a clear mandate for reform. Nevertheless it is vital to tackle the country's large bottlenecks within an environment of high corporate and public debt.

Japan: GDP components

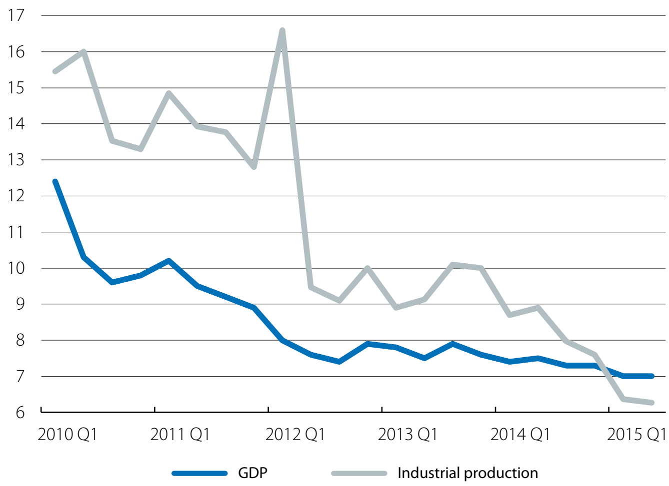
Contribution to growth in 2015 Q2 (pps)



Note: * Quarter-on-quarter change.
Source: "la Caixa" Research, based on data from the Ministry of the Interior and Communication.

China: GDP and industrial production

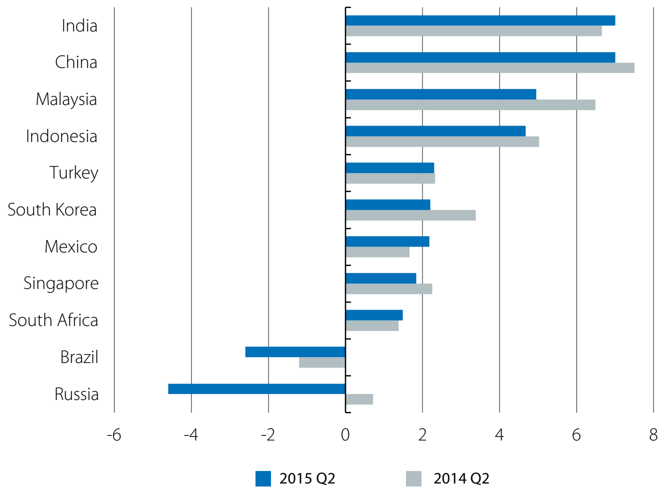
Year-on-year change (%)



Source: "la Caixa" Research, based on data from the National Statistics Office of China.

Emerging countries: GDP

Year-on-year change (%)



Source: "la Caixa" Research, based on data from Thomson Reuters Datastream.