TWO SIDES PARTNER WEBINAR

(London, 24 January 2025)

THE EUROPEAN ECONOMIC OUTLOOK

From one shock to the next !

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SUMMING UP - JANUARY 2024

We are not in a happy world

Recession and inflation are with us

The forecasts suggest that things will modestly improve

But they may well be optimistic

- **How long will the war last ?**
- **And now Middle-East turmoil !**
- **Inflation is coming down, but …**
- **... core inflation remains high**
- **Public debt is rising**

And medium-run prospects are dim

FIVE SHOCKS IN FIVE YEARS

2020 - Covid and worst recession since the war

2021 - High inflation (supply chain chaos)

2022 - War in Ukraine (more inflation and high interest rates)

2023 - War in the Middle East (and much greater uncertainties)

2024 - Trump ! (and more uncertainties)

PROSPECTS

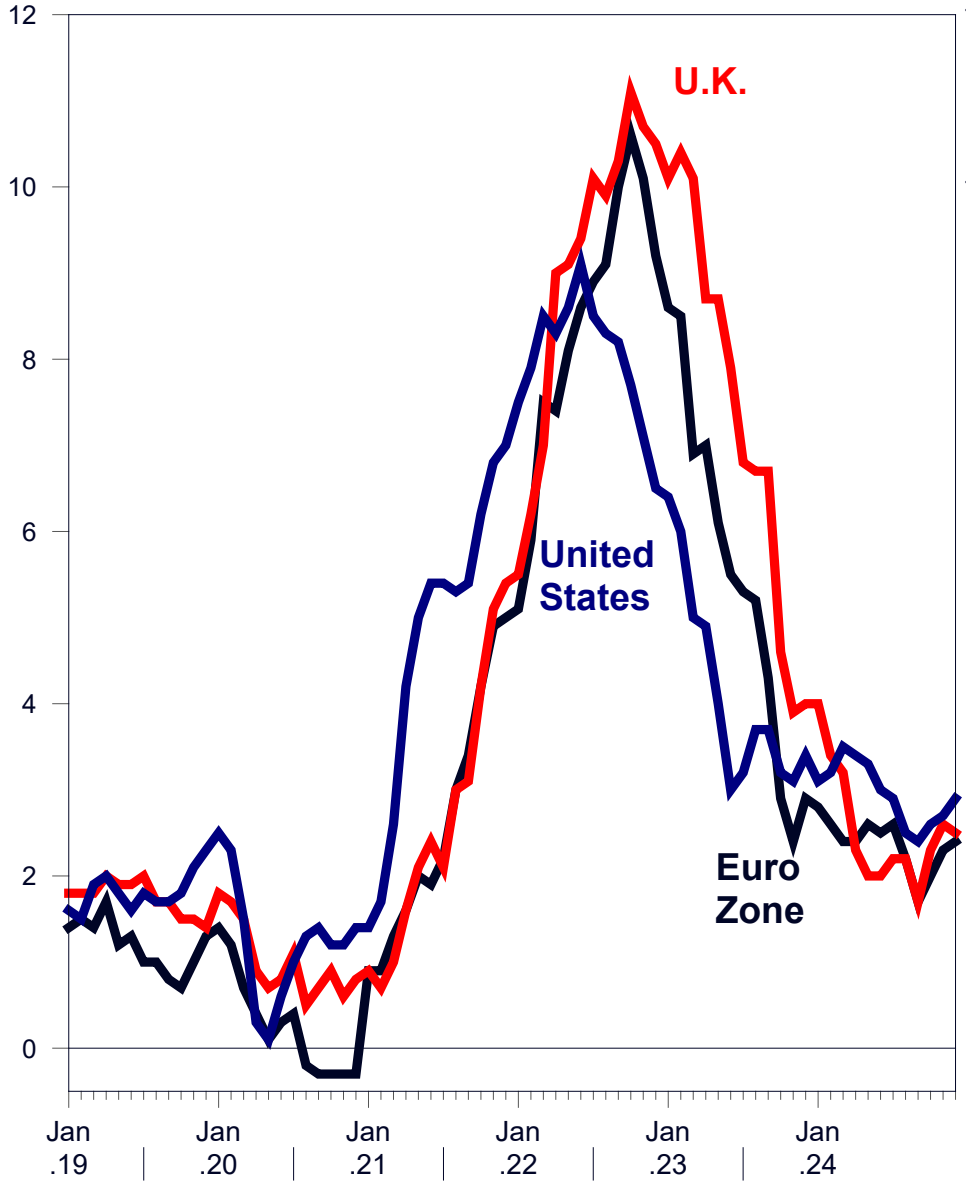
Inflation decelerating
- **... but slowly**
- **... (and not everywhere)**

Growth reviving
- **... but slowly**
- **... (and not everywhere)**

Uncertainties increasing
- **... everywhere**

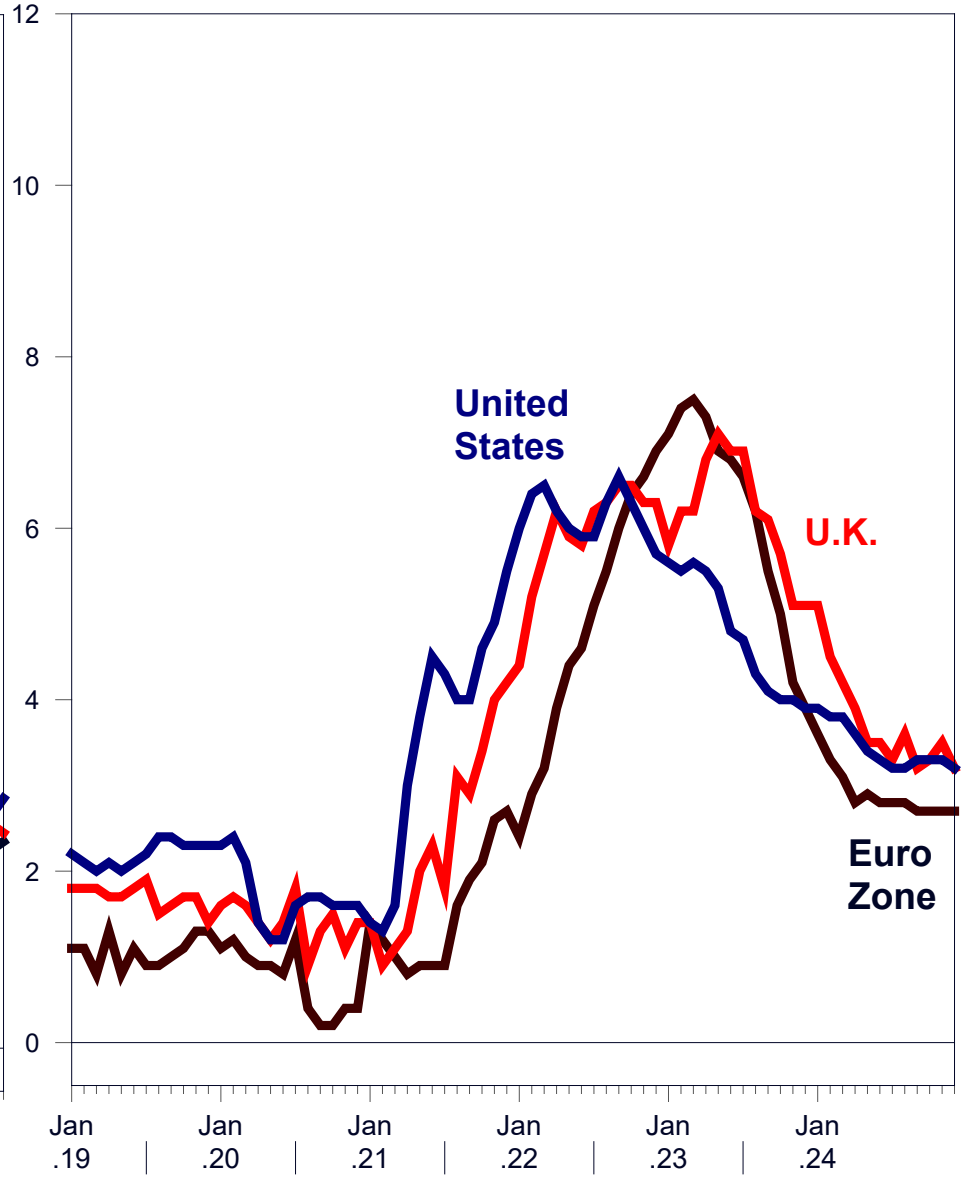
INFLATION

(consumer prices; per cent changes)



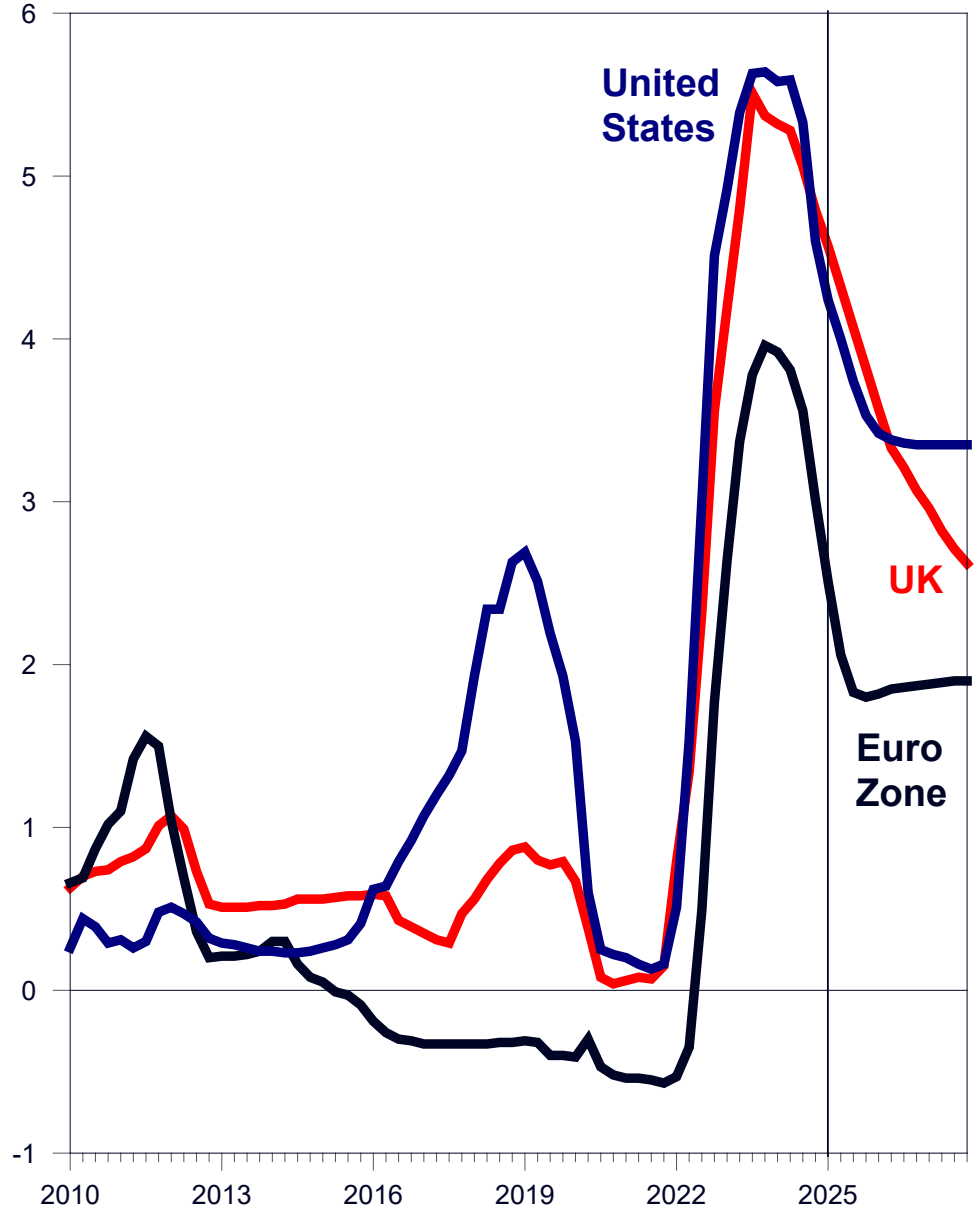
CORE* INFLATION

(per cent changes)



* Excluding energy and food.

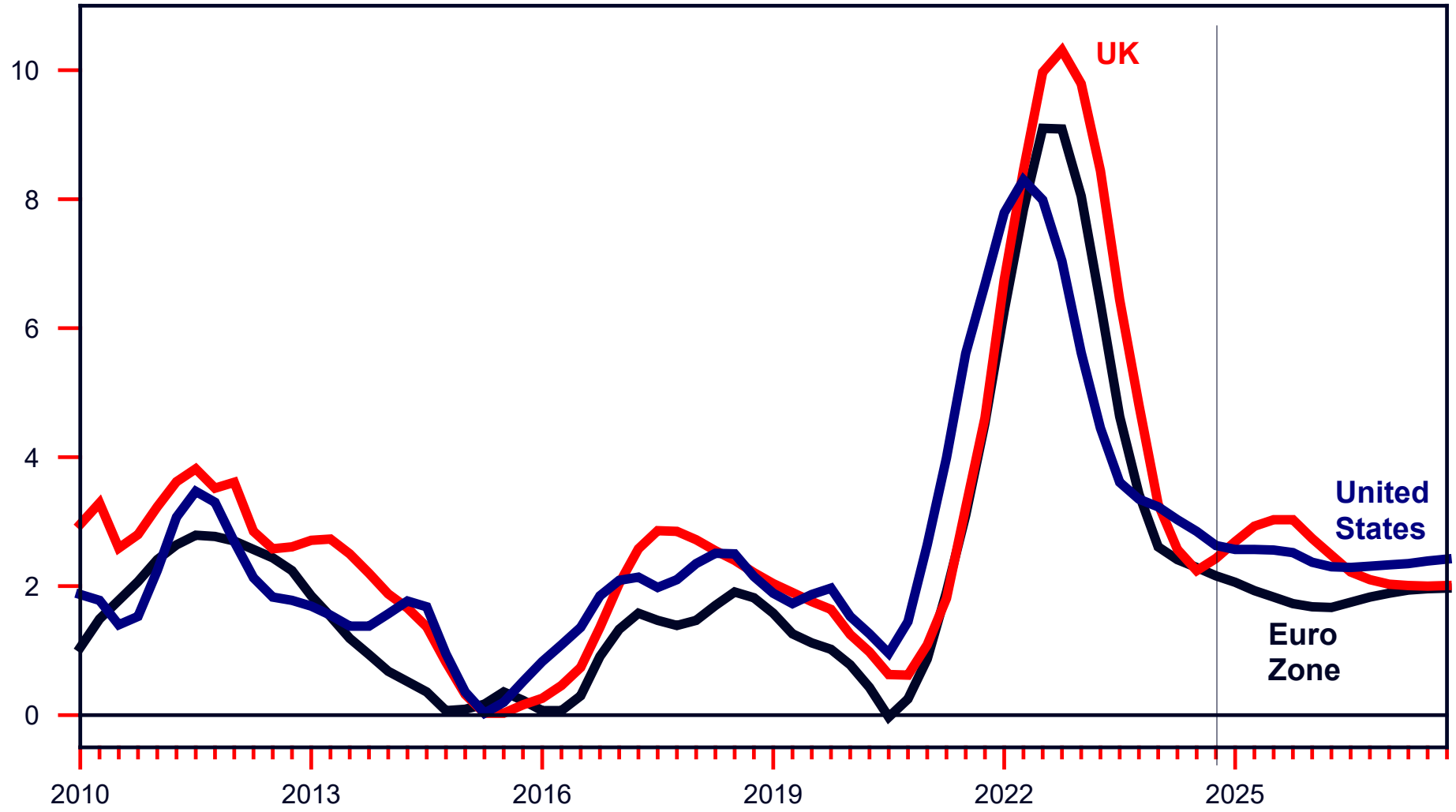
SHORT-TERM INTEREST RATES



Source: Oxford Economics.

CONSUMER PRICE INFLATION

(per cent changes from previous year; 3 quarter mov. aver.)



Source: Oxford Economics.

GROWTH RATES

(GDP; percentage changes)

	January 2024			Now		
	2024	2025	2026	2024	2025	2026
USA	2.0	1.4	1.9	2.8	2.6	2.7
EuroZ.	0.6	1.8	2.0	0.8	1.1	1.5
China	4.4	4.0	3.9	5.0	4.4	4.1
Germany	-0.1	1.5	2.0	-0.2	0.4	1.2
France	0.6	2.1	2.4	1.1	0.8	1.4
Italy	0.5	1.2	0.8	0.5	0.8	0.9
Spain	1.4	1.7	1.7	3.1	2.5	1.8
UK	0.6	1.6	1.9	0.8	1.1	1.7

GROWTH RATES

Cumulative difference in GDP growth between January 2024 forecast and January 2025 forecast

United States	2.8
Eurozone	-1.0
China	1.2
Germany	-2.0
France	-1.8
Italy	-0.3
Spain	2.6
UK	-0.5

Source: Oxford Economics.

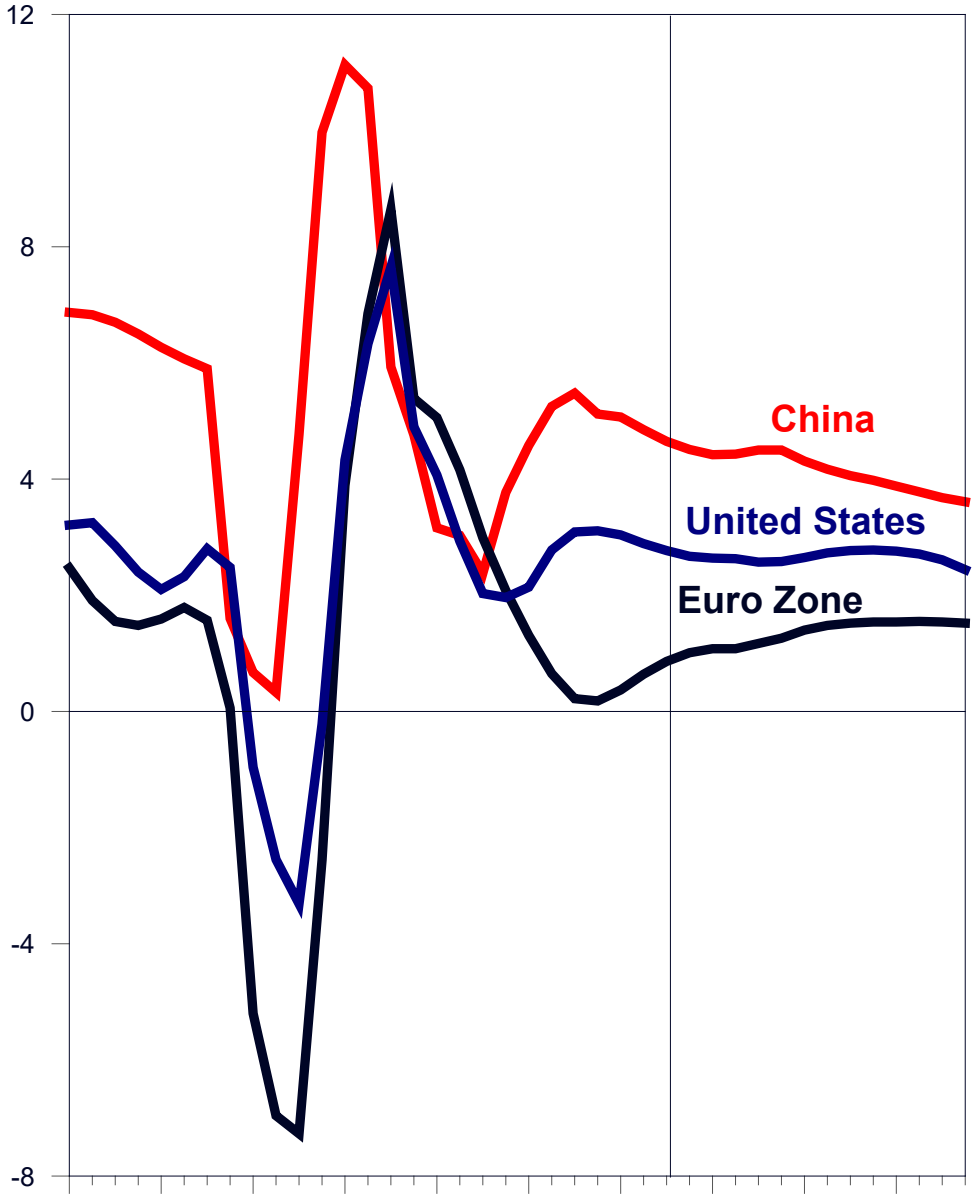
GROWTH RATES

(GDP; percentage changes)

	2022	2023	2024	2025	2026	2027
USA	2.5	2.9	2.8	2.6	2.7	2.7
EuroZ.	3.6	0.5	0.8	1.1	1.5	1.5
China	3.0	5.2	5.0	4.5	4.1	3.7
Germany	1.4	-0.1	-0.2	0.4	1.2	1.3
France	2.6	1.1	1.1	0.8	1.4	1.8
Italy	4.8	0.8	0.5	0.8	0.9	0.8
Spain	6.2	2.7	3.1	2.5	1.8	1.6
UK	4.8	0.4	0.8	1.1	1.7	1.8

GDP GROWTH

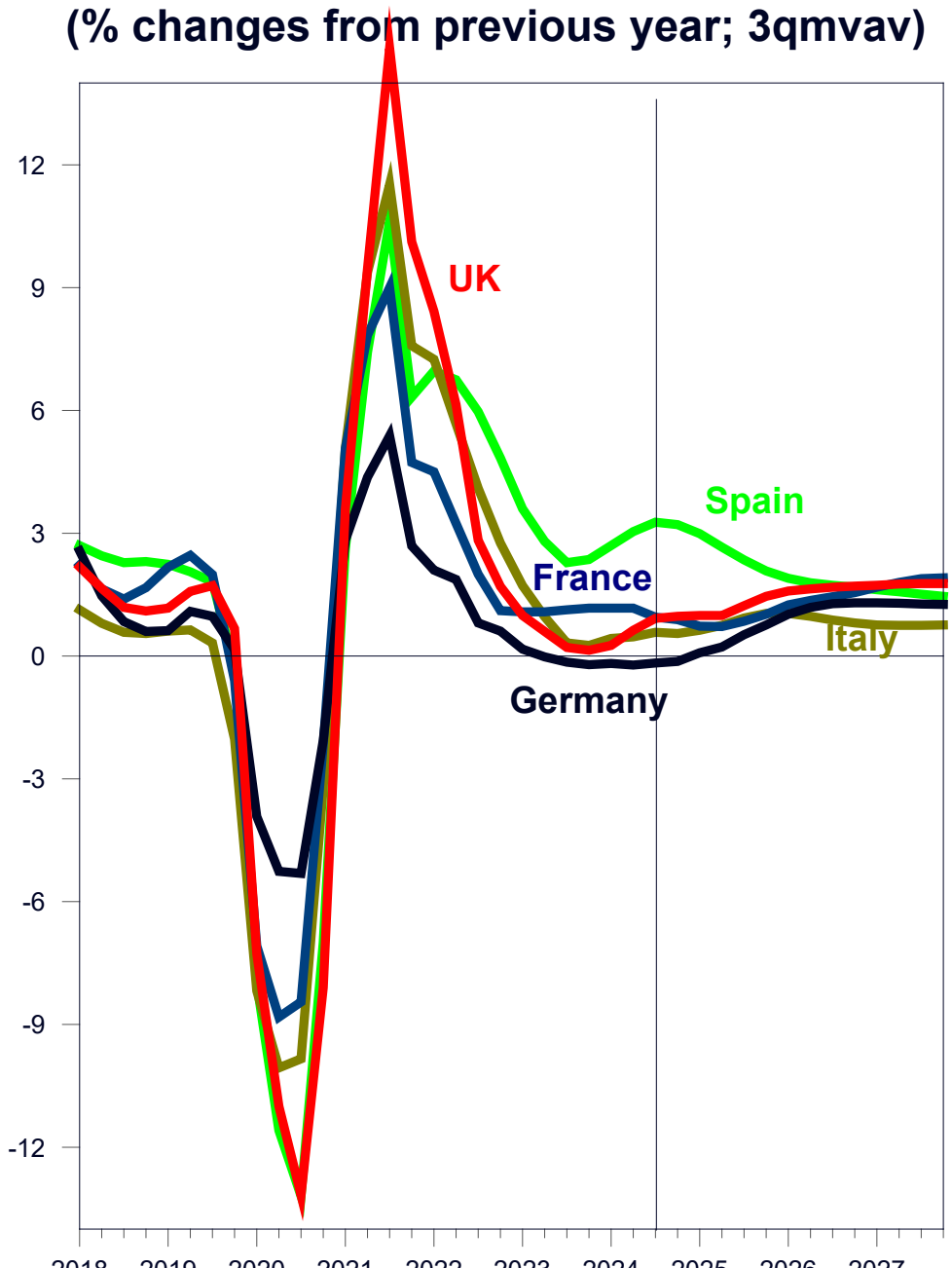
(% changes from previous year; 3qmvav)



Source: Oxford Economics.

GDP GROWTH

(% changes from previous year; 3qmvav)



Source: Oxford Economics.

UNCERTAINTIES

The economic picture
- **Oil and energy prices**
  - **could go up**
- **Defence expenditure**
  - **must go up**
- **Globalization**
  - **is going down**

The geo-political picture
- **The US versus China**
- **The EU versus Russia**
- **Populism on the rise**

And then Trump !
- **(totally unpredictable ?)**

WHAT MIGHT TRUMP DO ?

Cut taxes **(America is at full employment)**	**Higher demand inflation** **Higher interest rates**
Reduce immigration **(America is at full employment)**	**Lower potential growth** **Higher wage inflation** **Higher interest rates**
Raise tariffs **(America is at full employment)**	**Higher inflation** **Higher interest rates** **Retaliation and danger of a trade war**

Overall effects on economy very uncertain. Initially perhaps some faster growth but in the longer run the impact could be neutral or negative

A TRADE WAR ?

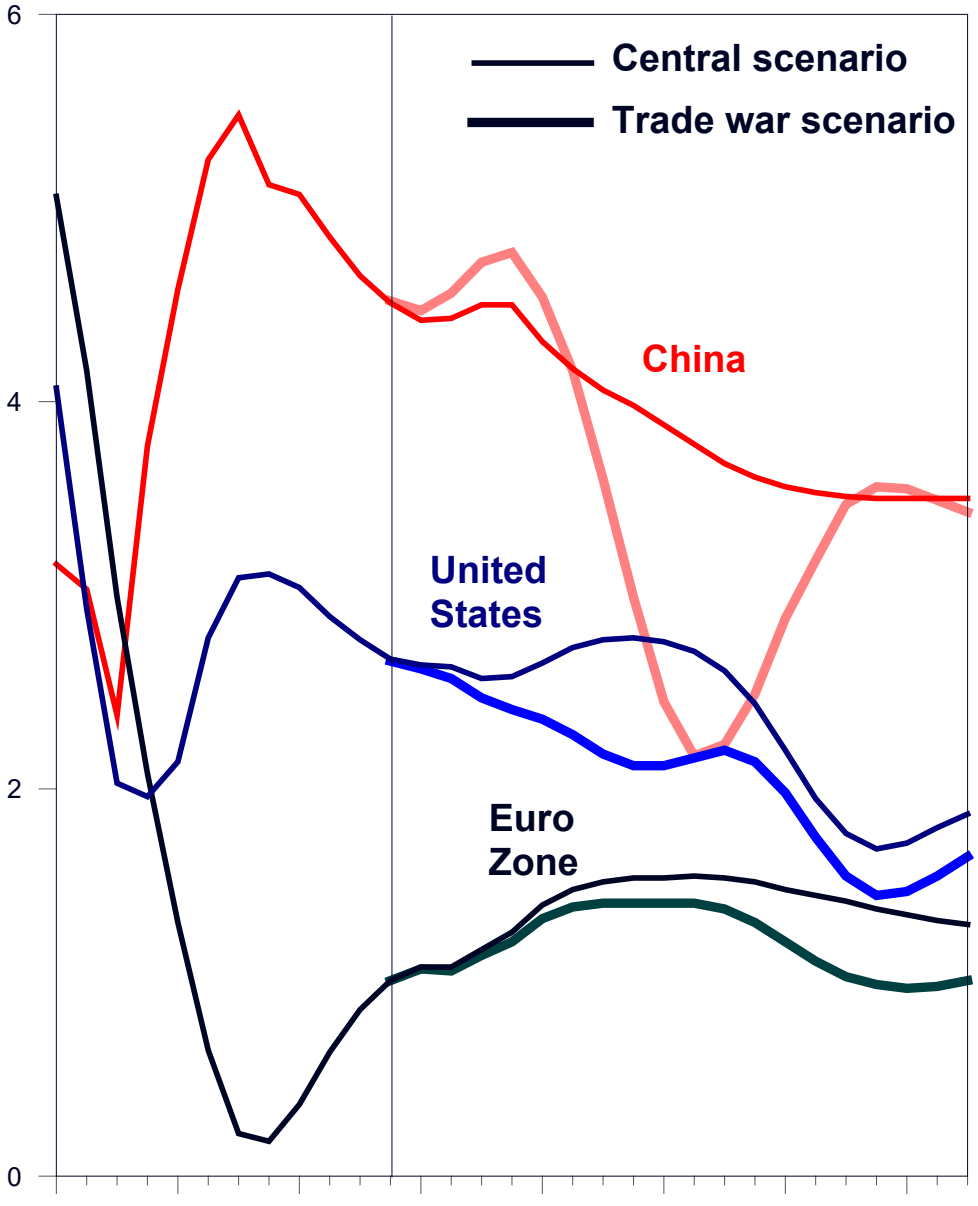
The central forecast assumes only moderate protectionism: 30 per cent tariffs on Chinese imports and some targeted tariffs (steel, aluminium, cars ...) on the EU, Canada, Mexico and a few Asian economies

But this may be optimistic. A more extreme scenario assumes that he will impose a 60 per cent tariff on Chinese imports and a 10 per cent tariff on all other trading partners

This leads to retaliation and a global trade war

TRADE WAR - GDP GROWTH

(% changes from previous year; 3qmvav)



Source: Oxford Economics.

TRADE WAR - GDP LOSS

Cumulative loss of output in trade war scenario - 2025 to 2029

USA	**-0.9**
China	**-1.0**
Eurozone	**-0.4**

Not a wonderful picture, but not a tragedy either

Source: Oxford Economics.

MEDIUM-TERM ISSUES

January 2024

- German sluggishness
- Rising demands on government
- Slower productivity growth

January 2025

- Not much change - if anything all a bit worse
- Europe's sluggishness
  - Germany
  - Italy
  - UK
- Faltering globalization

EUROPE'S SLUGGISHNESS

Germany

- **Over dependent on US (defence), China (exports), Russia (energy)**
- **Traditional industry in retreat**
- **High-tech industry weak**

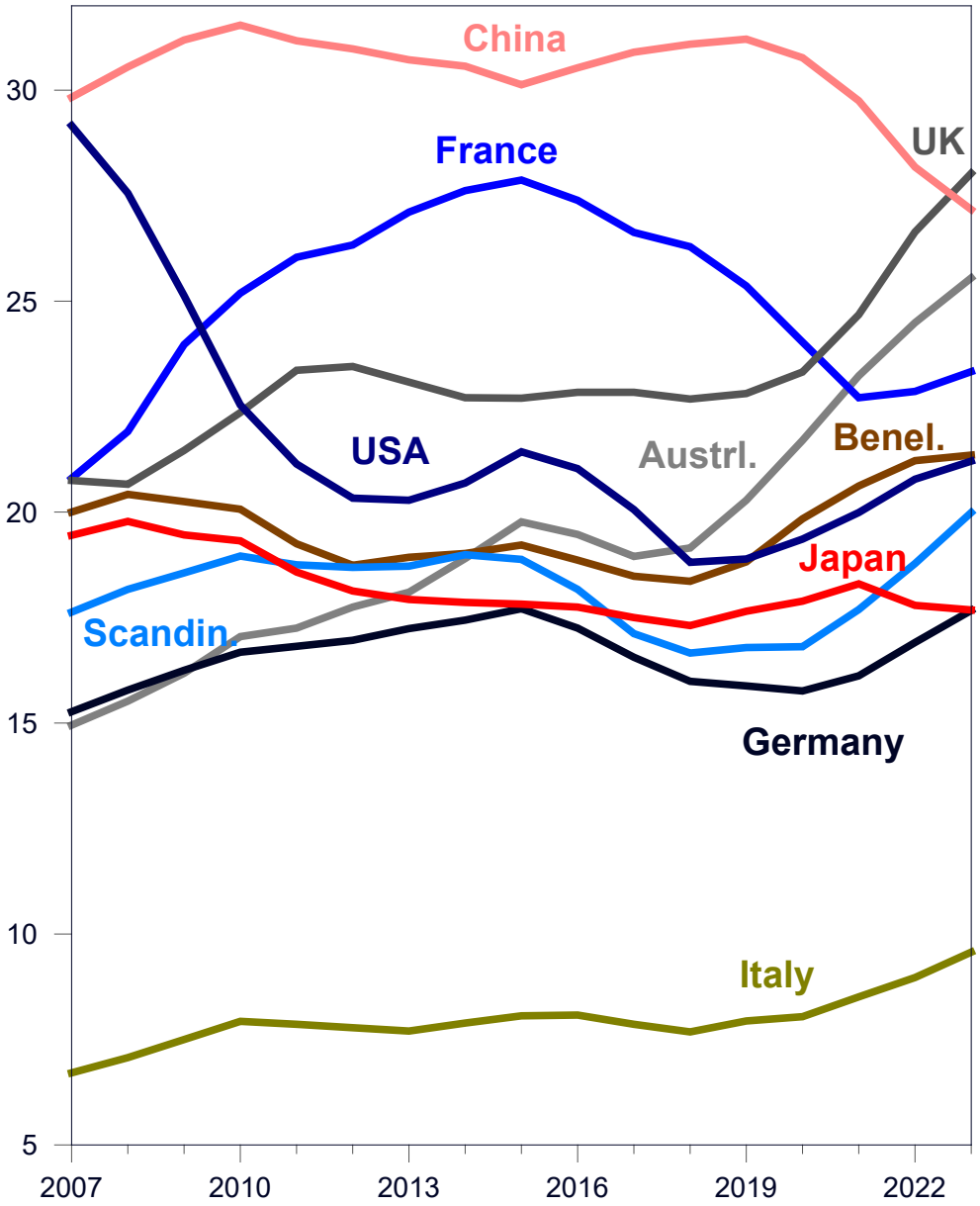
Italy

- **Like Germany has missed the digital transformation**
- **In addition vastly over-regulated**

UK

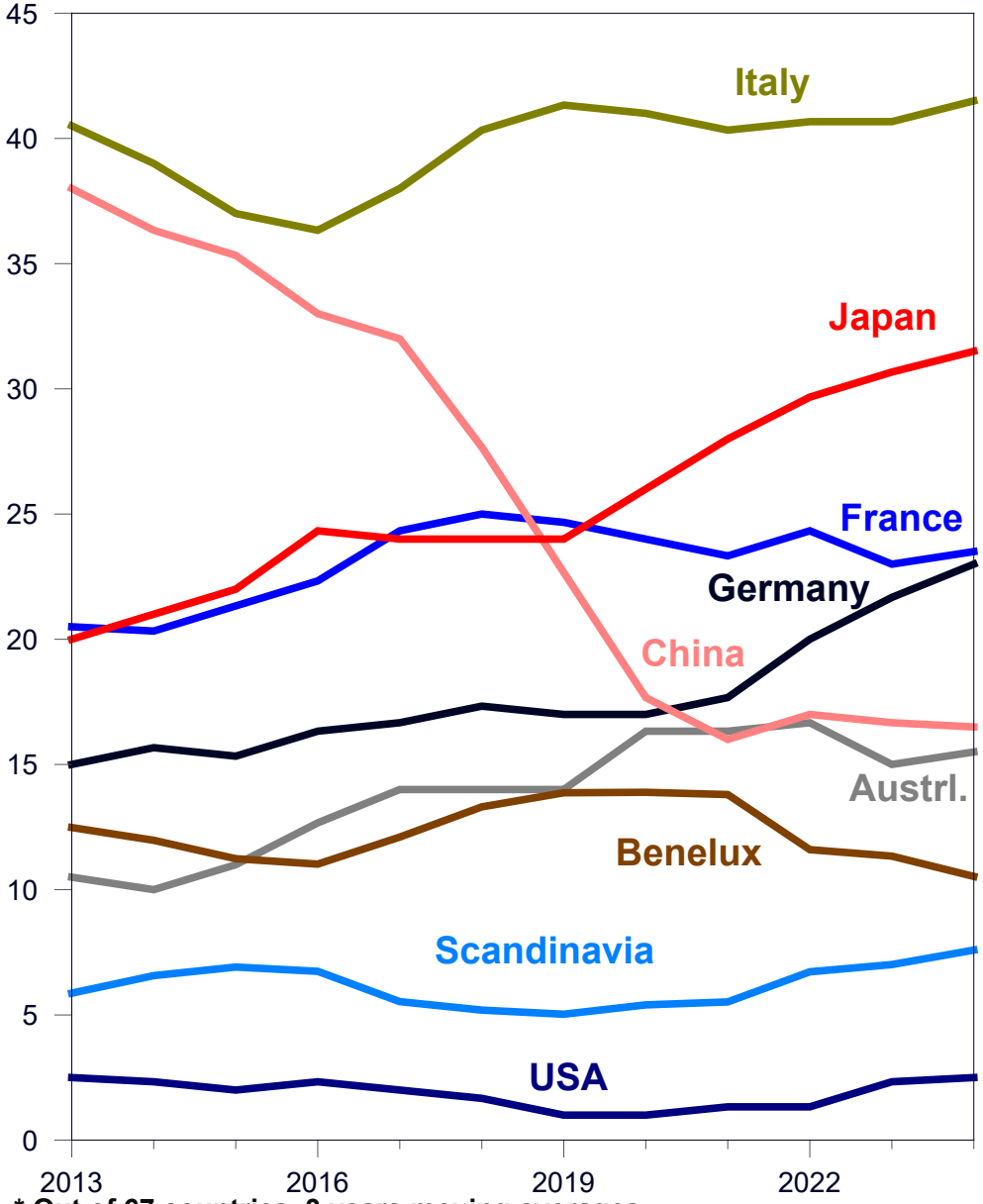
- **Neither over-regulated nor a laggard in high-tech**
- **But hurt by Brexit and low investment**

HIGH-TECH EXPORTS IN % OF MANUFACTURED EXPORTS*



* Three years moving averages.
Source: World Bank.

RANKINGS IN DIGITAL COMPETITIVENESS*



* Out of 67 countries. 3 years moving averages.

Source: IMD.

EASE OF DOING BUSINESS 2019

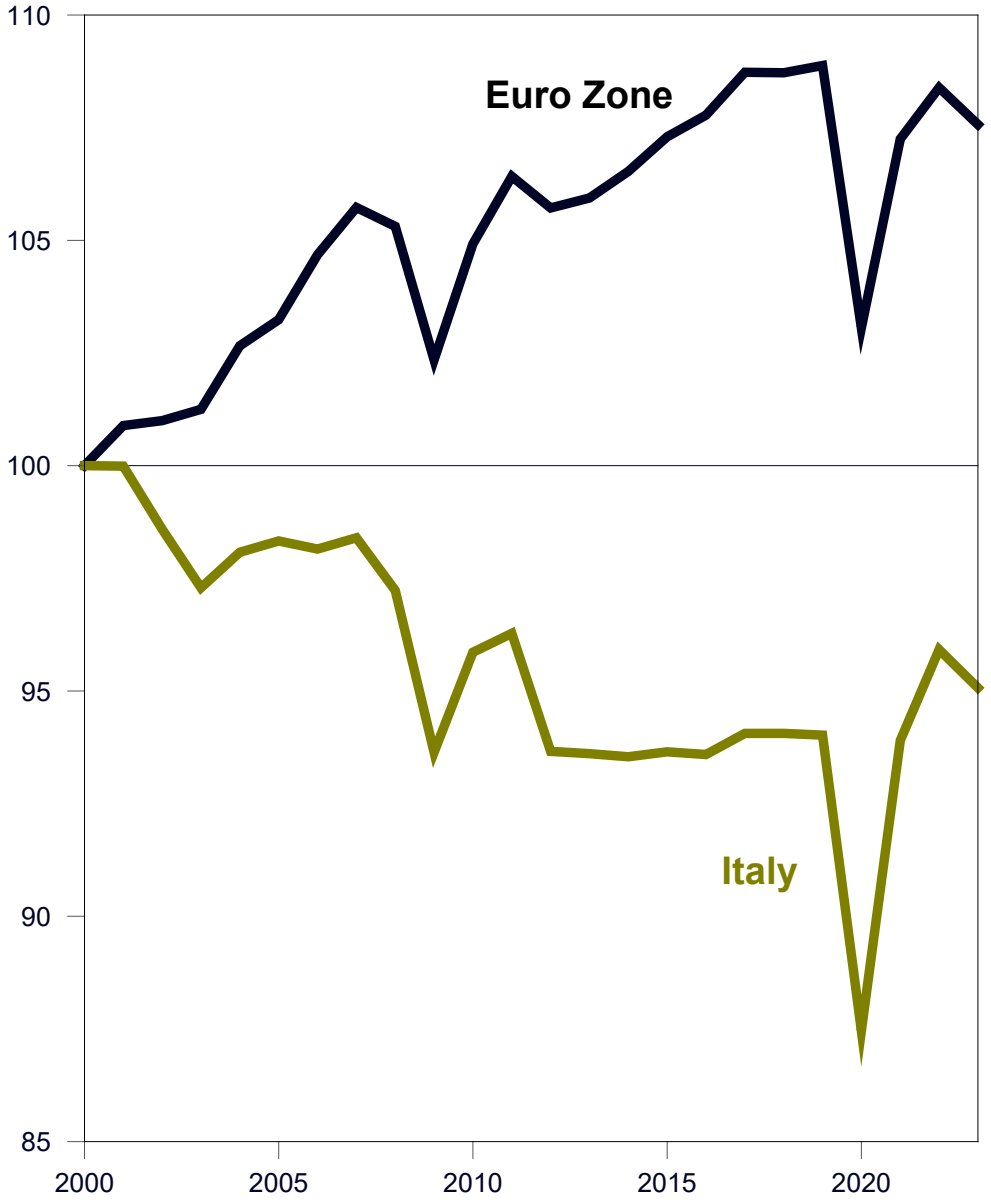
Rankings out of 188 countries

Scandinavia	5
United States	6
United Kingdom	8
Australia	13
Germany	22
Japan	29
China	31
France	32
Benelux	45
Italy	58
Venezuela	188

Source: World Bank.

PRODUCTIVITY* GROWTH

(2000 = 100)

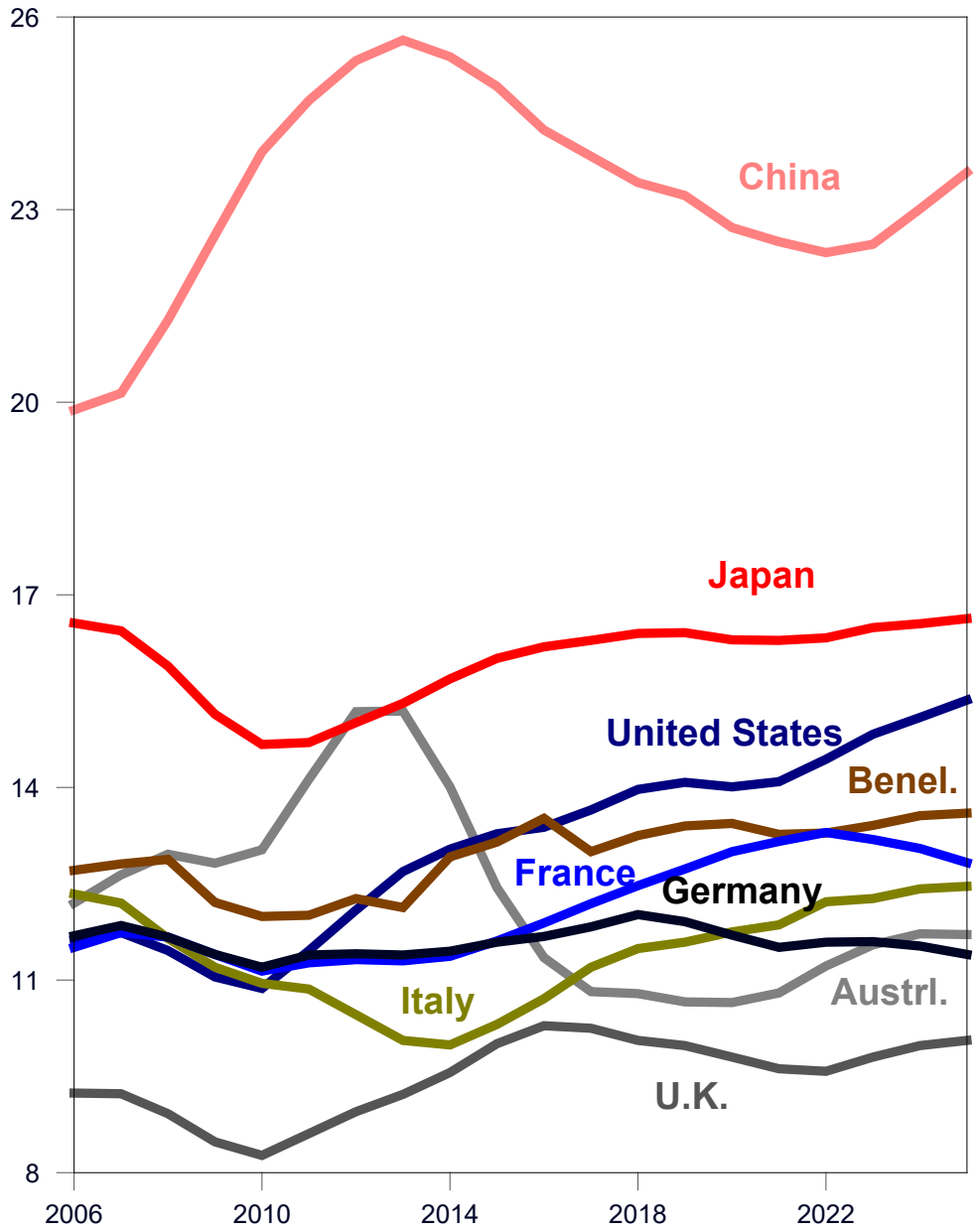


*** GDP per employee.**

Source: Oxford Economics.

BUSINESS INVESTMENT

(in per cent of GDP)



Source: Oxford Economics.

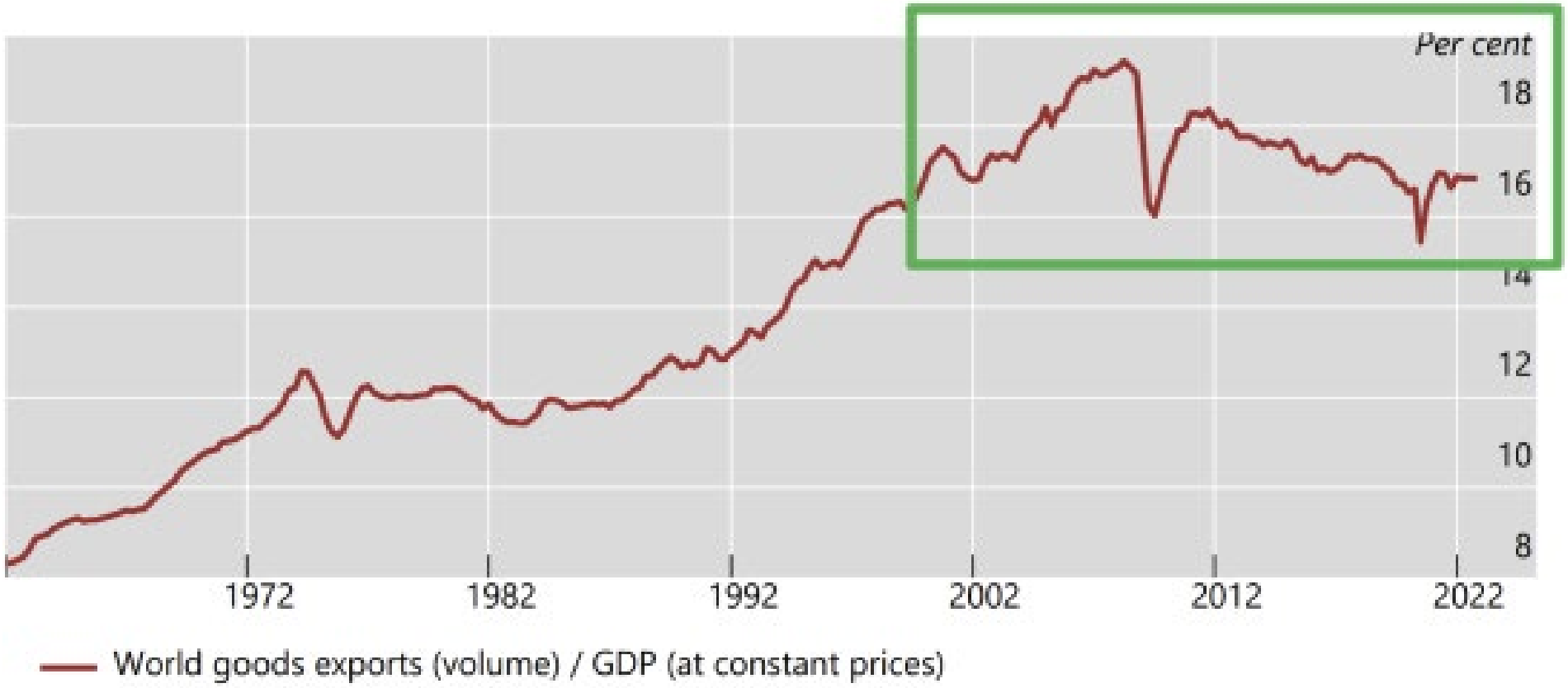
RATIO OF WORLD TRADE TO WORLD GDP GROWTH

	"Elasticity"	
	Total trade	Trade in manufacts.
1950-60	1.6	1.9
1960-73	1.5	1.8
1973-90	1.3	1.9
1990-2008	1.8	2.0
2008-23	0.7	0.7

Source: WTO.

GLOBALIZATION IN RETREAT

SHARE OF WORLD EXPORTS IN WORLD GDP



Source: BIS.

THE TRIUMPH OF GLOBALIZATION 1990-2008

The value-added chain is "sliced-up": components are produced everywhere and sold everywhere thanks to:

- **Falling trade barriers as country after country embraces freer trade**
- **Falling transport costs as air travel spreads and container ships grow in size**
- **Falling communication costs because of the new ICT technologies**
- **The opening of China, with its enormous reserves of unskilled and cheap labour**
- **The opening of Eastern Europe with its large reserves of skilled and relatively cheap labour**

Difficult to see how any of these forces can continue to stimulate trade ...

... though something new is always possible

IS GLOBALIZATION COMING TO AN END ?

Rising protectionism

Anecdotal evidence of some MNCs coming home

Supply chains that are too fragile/too complex
Some of these are being whittled down

The spread of 3D production, robots, artificial intelligence

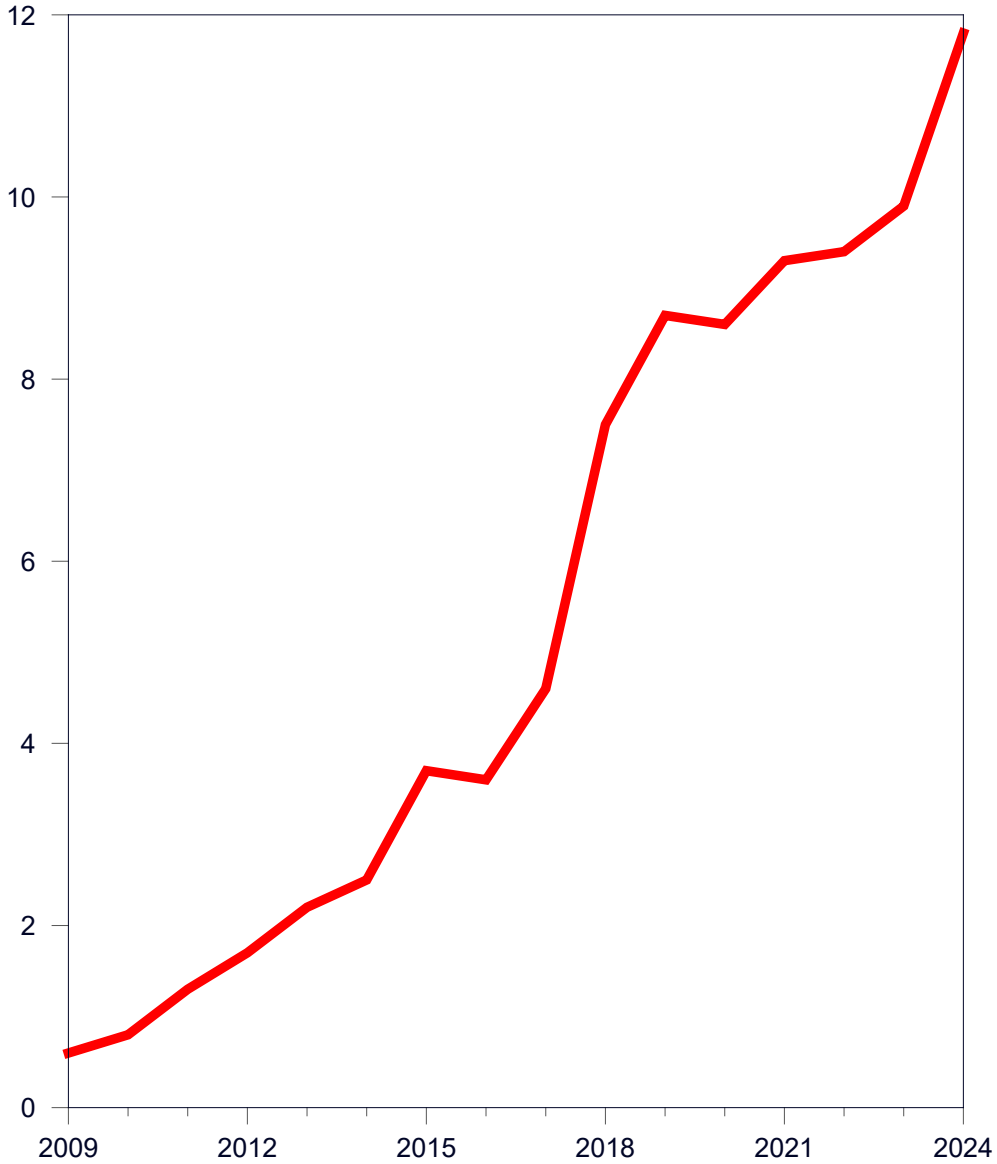
None of these forces are, as yet, very strong (but watch Trump)

Hence, announcing an end to globalization would seem premature, but trade growth is likely to be less rapid (relative to output) than it has been over the last 60 years

And this may well lead to a lower growth of productivity because of diminished competitive pressures

RISING PROTECTIONISM

Percent of world trade covered by import restrictive measures



Source: WTO.

SUPPLY CHAINS

Double vulnerability

i) Over-dependence on just-in-time supplies

ii) Over-optimism on the persistence of a benign global trading and geo-political environment

SUPPLY CHAINS

Possible hindrances

- **Protectionism**
- **Earthquakes**
- **Tsunamis**
- **Strikes**
- **Canal closures (e.g., Suez, Panama)**
- **Pandemics**
- **Wars (e.g., Red Sea bombing)**
- **etc.**

SUPPLY CHAINS REVISITED

Original aim: search for lower costs and greater efficiencies

Present aim: search for stability and sustainability (eg: lower transport costs)

Hence "re-shoring" or "near-shoring"

A VERY UNCERTAIN SHORT- AND MEDIUM-TERM OUTLOOK

Short-term risks

- Resilient inflation
- Semi-stagnation
- Rising debt and interest rates
- Trump's unpredictability

Medium-term risks

- Trump's unpredictability
- Slowing globalization
- Lower productivity growth
- Increasing geo-political tensions

Are there any upsides ?

- Can you think of any ? Technology perhaps

AND WHAT ABOUT PAPER ?

In both the Eurozone and in the UK, 2022-23 were terrible years, but 2024 saw some recoveries

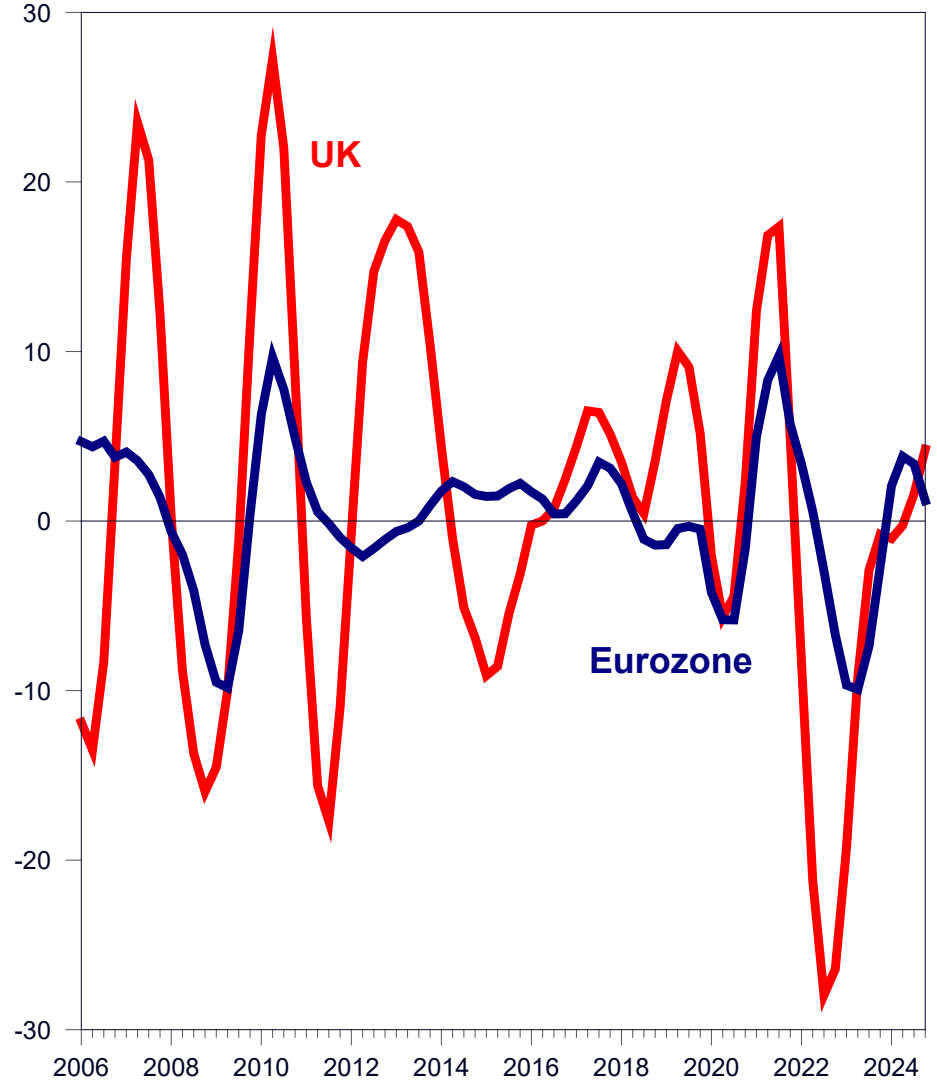
The Eurozone's paper cycle is much less volatile than the UK one, and is also much more closely correlated with GDP developments than is the case in the UK

Going forward, tentative forecasts by Oxford Economics suggest a better picture for Britain than for the Continent

Modest growth in the UK, renewed declines in the Eurozone

WEST EUROPEAN PAPER AND PULP PRODUCTION

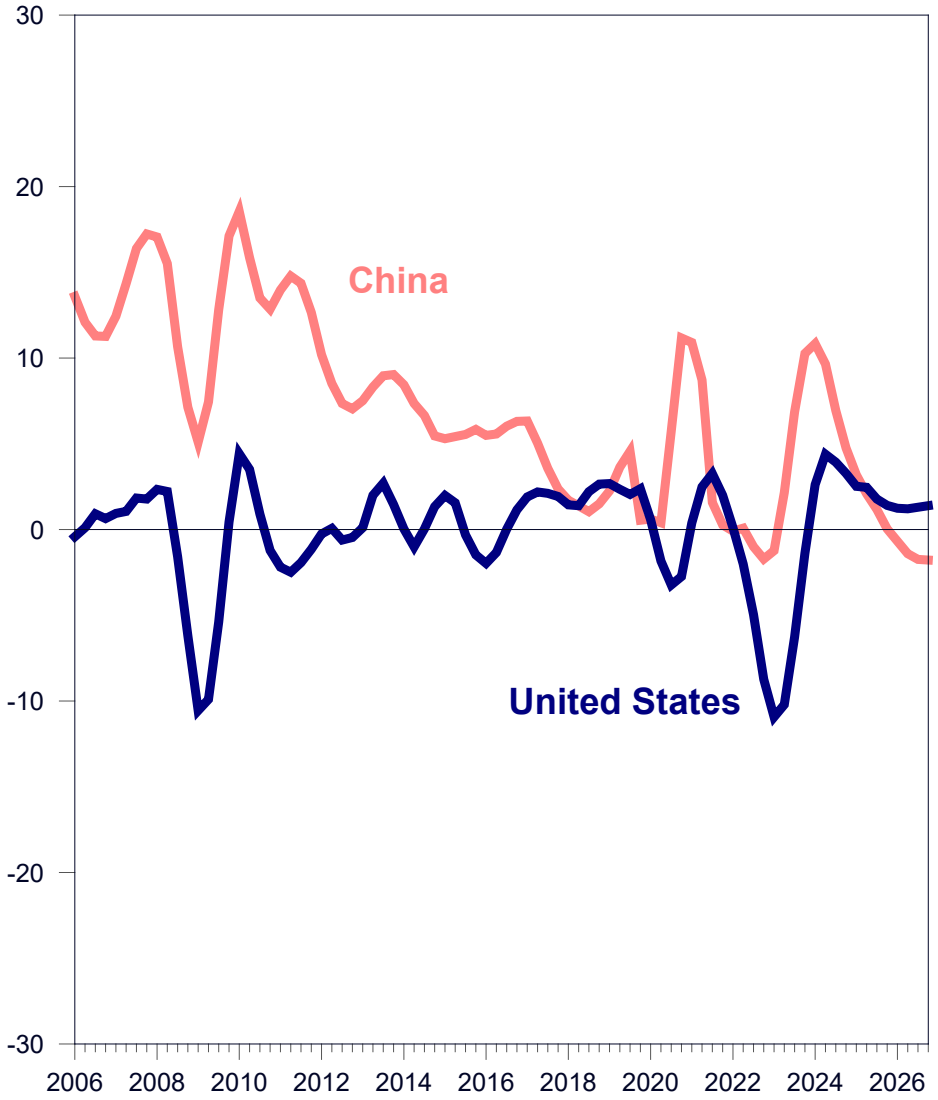
(% ch. from prev. year; 3 qtrs.mov.aver.)



Source: Oxford Economics.

US AND CHINA PAPER AND PULP PRODUCTION

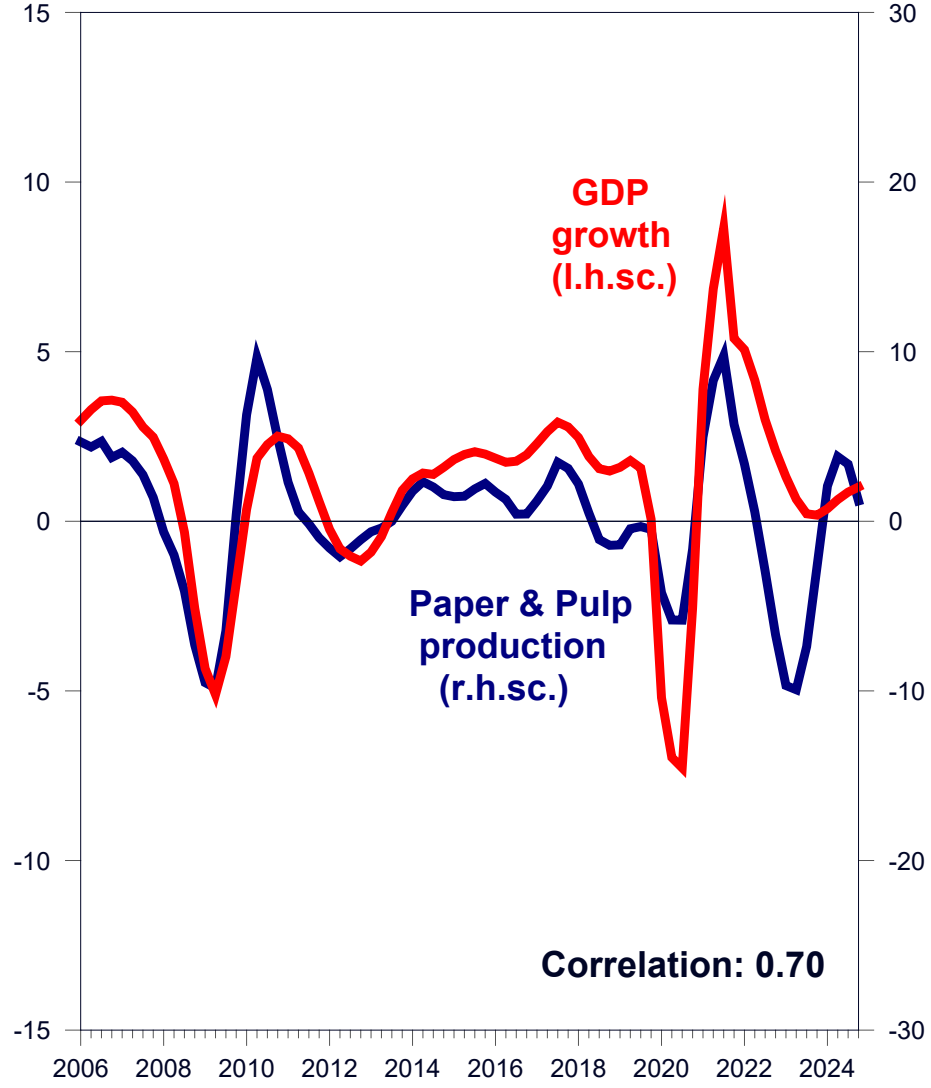
(% ch. from prev. year; 3 qtrs.mov.aver.)



Source: Oxford Economics.

EUROZONE GDP AND PAPER & PULP PRODUCTION

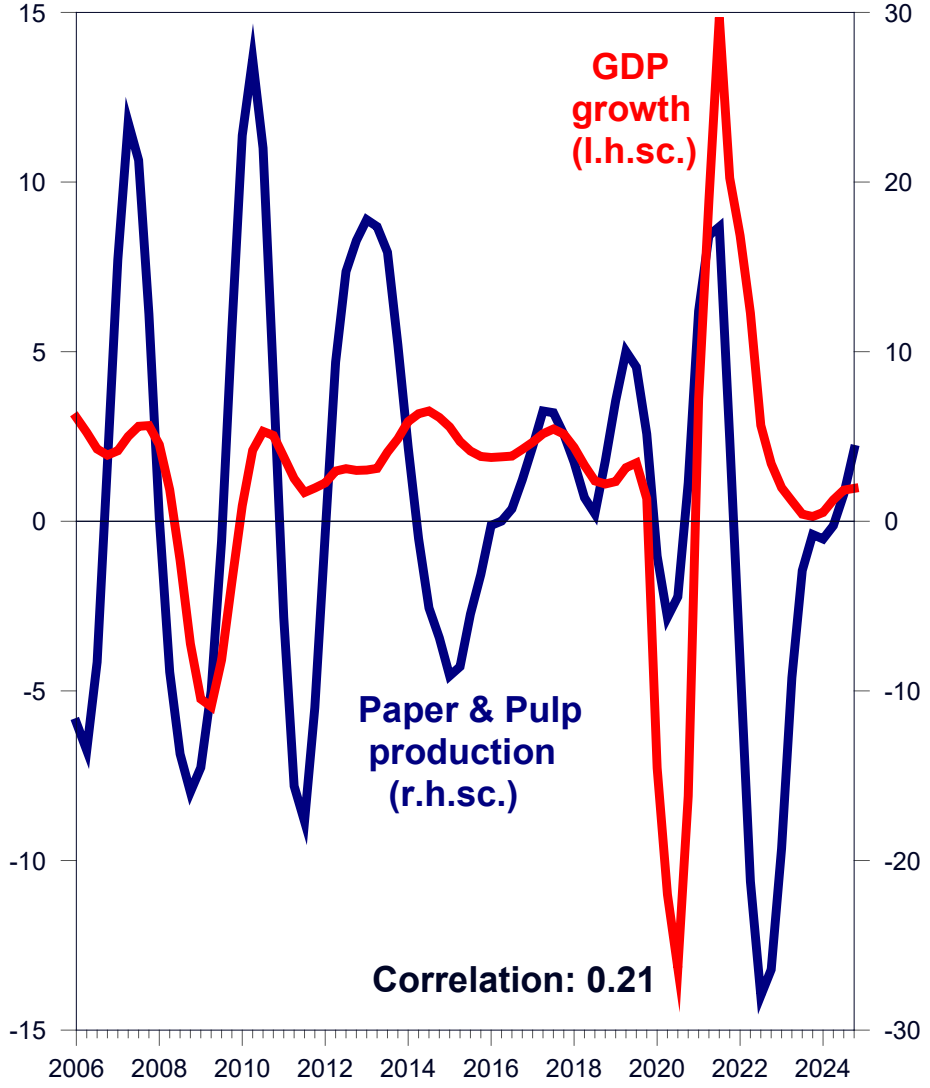
(% changes; 3 years mov. avrgs.)



Source: Oxford Economics.

UK GDP AND PAPER & PULP PRODUCTION

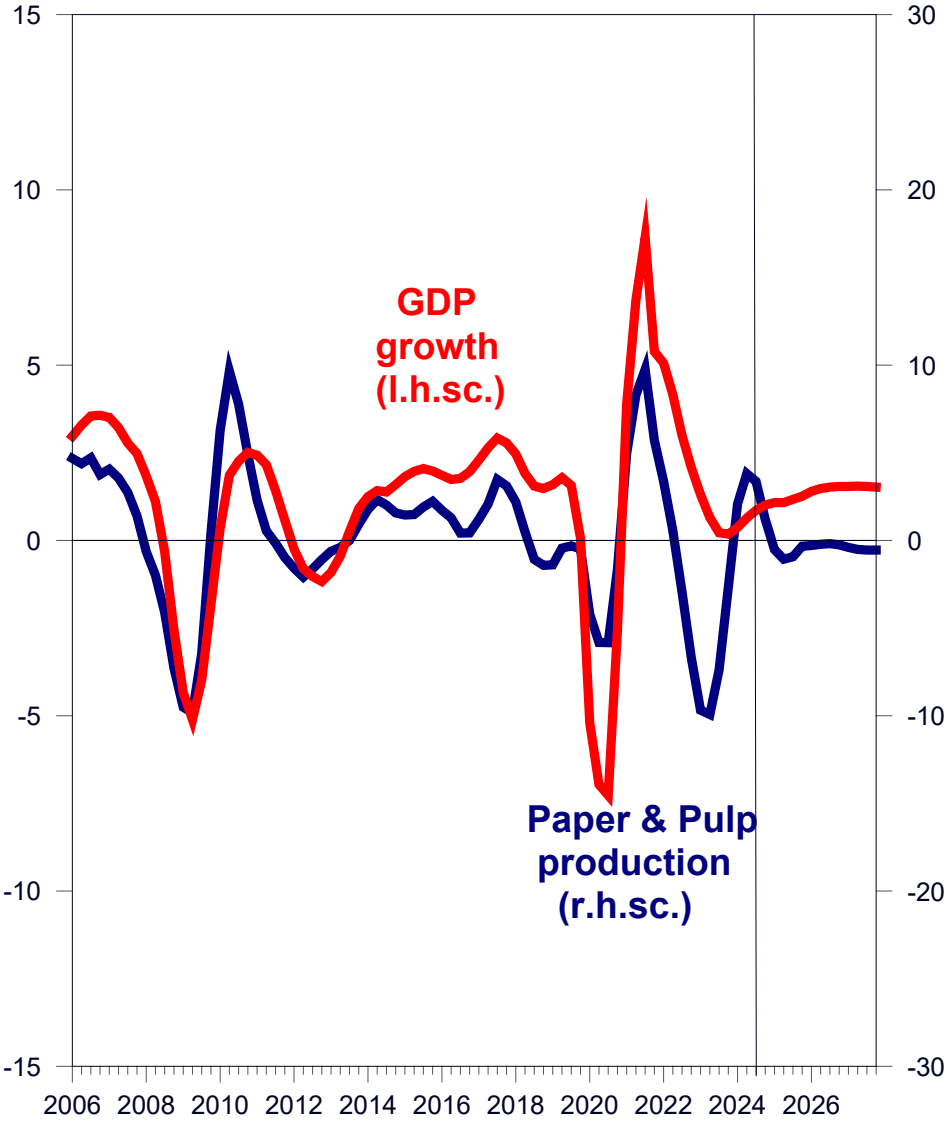
(% changes; 3 years mov. avrgs.)



Source: Oxford Economics.

EUROZONE GDP AND PAPER & PULP PRODUCTION

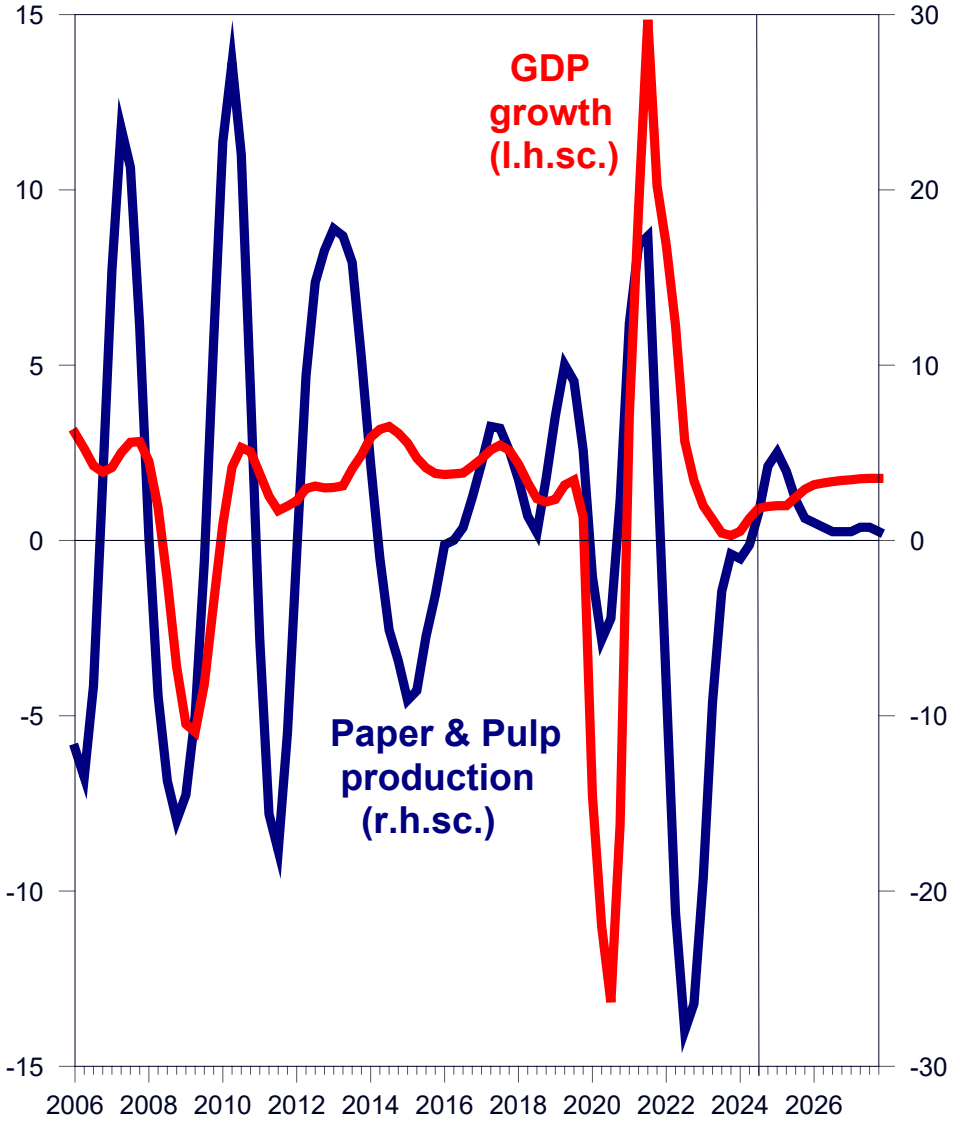
(% changes; 3 years mov. avrgs.)



Source: Oxford Economics.

UK GDP AND PAPER & PULP PRODUCTION

(% changes; 3 years mov. avrgs.)



Source: Oxford Economics.

SUMMING UP - JANUARY 2024

We are not in a happy world

SUMMING UP - JANUARY 2025

We are not in a happy world

... not to mention climate change !