

**BBVA**

RESEARCH

September  
**2016**



# **Eurozone**

## **Economic Watch**

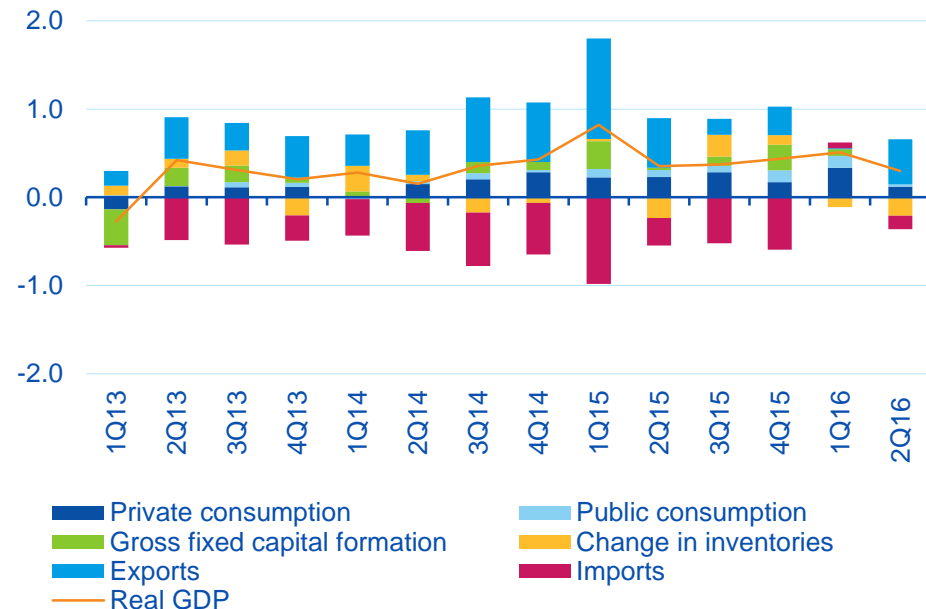
# Outlook of recent economic indicators

- **Economic growth slowed in 2Q16** by 0.2pp to +0.3% QoQ. Investment continued very weak and stagnated in Q2, partly offset by strong net exports and the moderate increase of consumption
- Our **MICA-BBVA indicator estimates quarterly GDP growth to decelerate slightly again to +0.2% QoQ in 3Q16**
- **Confidence data so far suggest some resilience of the eurozone after Brexit**, but still weak global demand and the moderate euro appreciation could put a brake on the industrial sector
- **Hard data in July point to a slightly gloomier outlook.** Both industrial production and exports disappointed, increasing concerns about the recovery of investment and the support from net exports, while the **strong increase in retail sales points to private consumption as the main driver of growth**
- **Subdued but stable core inflation combined with lower declines in energy prices led inflation to positive rates in recent months.** Easing energy base effects from a year ago might increase inflation in coming months to rates slightly below 1% in December
- The **ECB** barely changed its projections over the forecast horizon and **kept monetary policy stance unchanged in September.** Before the year end, an extension of QE (+6 months) is very likely combined with some technical adjustments to cope with scarcity of German bonds

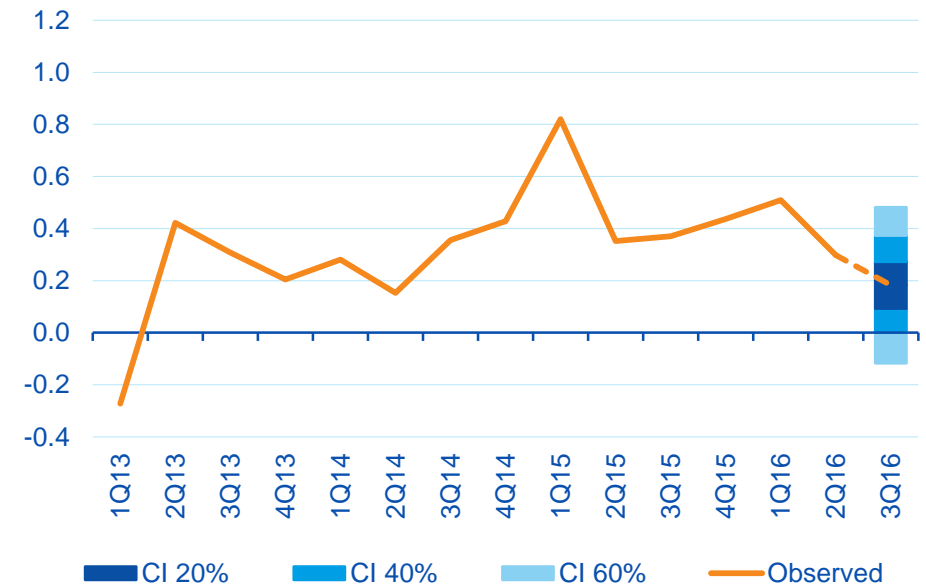
# Economic recovery should continue in 3Q16 but at slower pace

- **During 2Q16 GDP growth reflected the lack of fixed investment** and a poor contribution from both private and public consumption, that was only partially offset by a boost from external demand, particularly in Germany and Spain
- Incoming data suggest **a further moderation in GDP growth in 3Q16** (+0.2% QoQ after +0.5% in Q1 and +0.3% in Q2), once again signalling weakness in gross investment added to a slightly lower contribution from external demand that should balance a mild increase in private consumption

GDP (% QoQ), contribution by components (pp)



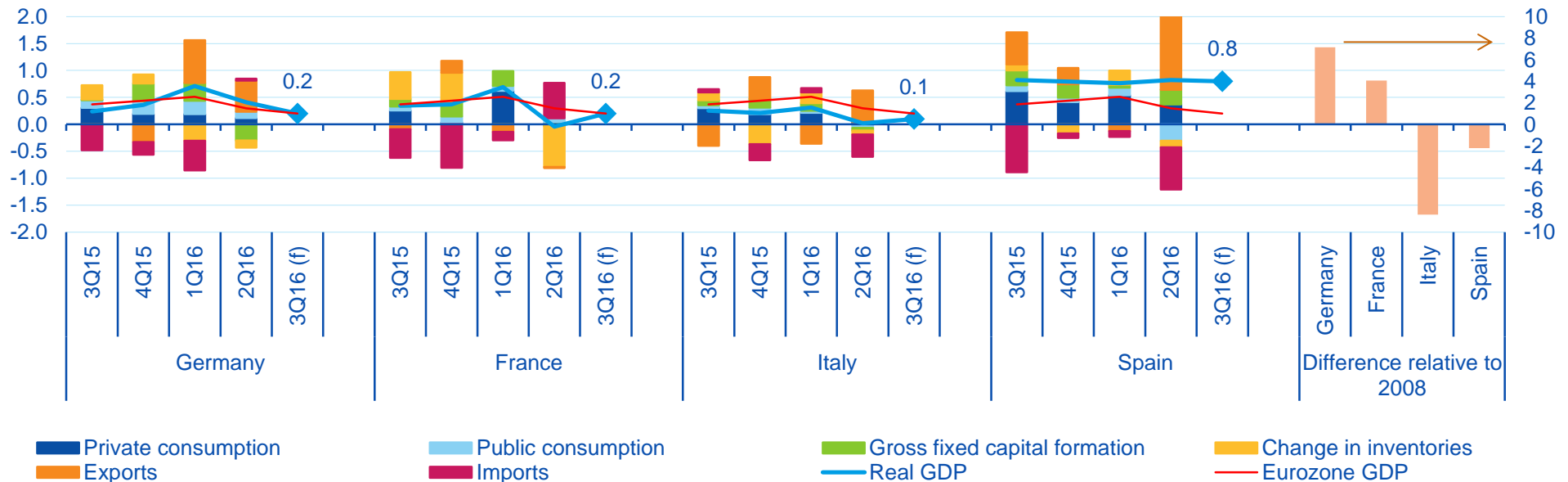
GDP and MICA forecasts (% QoQ)



# A slowdown in Germany is expected during 3Q16, while slight growth could return in France and Italy

- Data for 3Q16 anticipates **some growth slowdown in Germany** (BBVAe: +0.2% QoQ after +0.4% QoQ) in the back of declining investment, while **France and Italy would return to slight GDP growth rates** (BBVAe: +0.2% and +0.1% QoQ, respectively after flat figures in 2Q16)
- **Spain continues to outperform GDP growth in the region** (BBVAe: +0.8% QoQ) driven by both private consumption and external demand

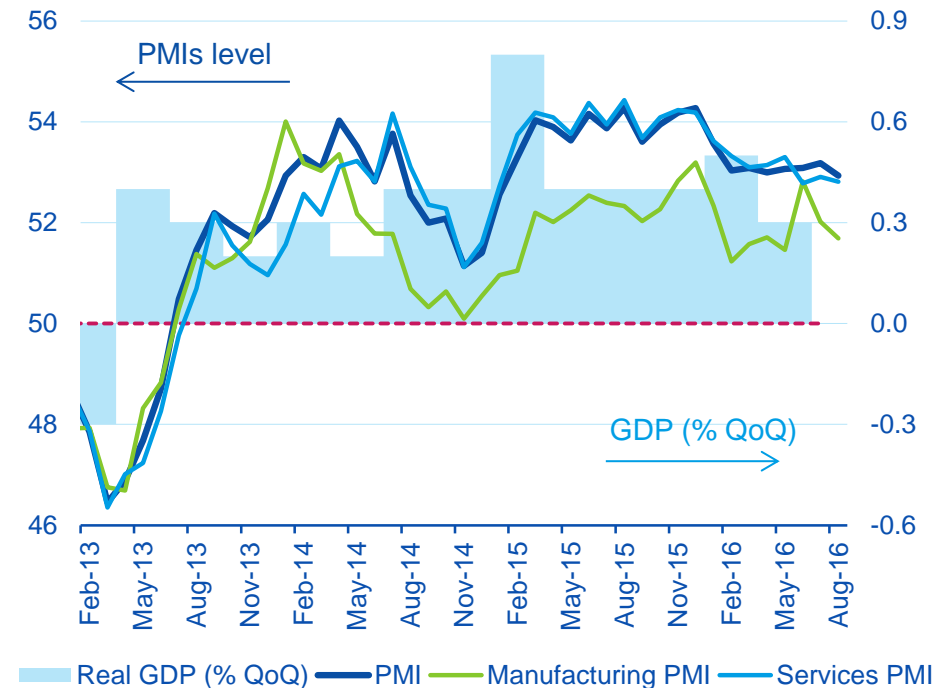
## GDP (% QoQ), contribution by component (pp) and forecasts



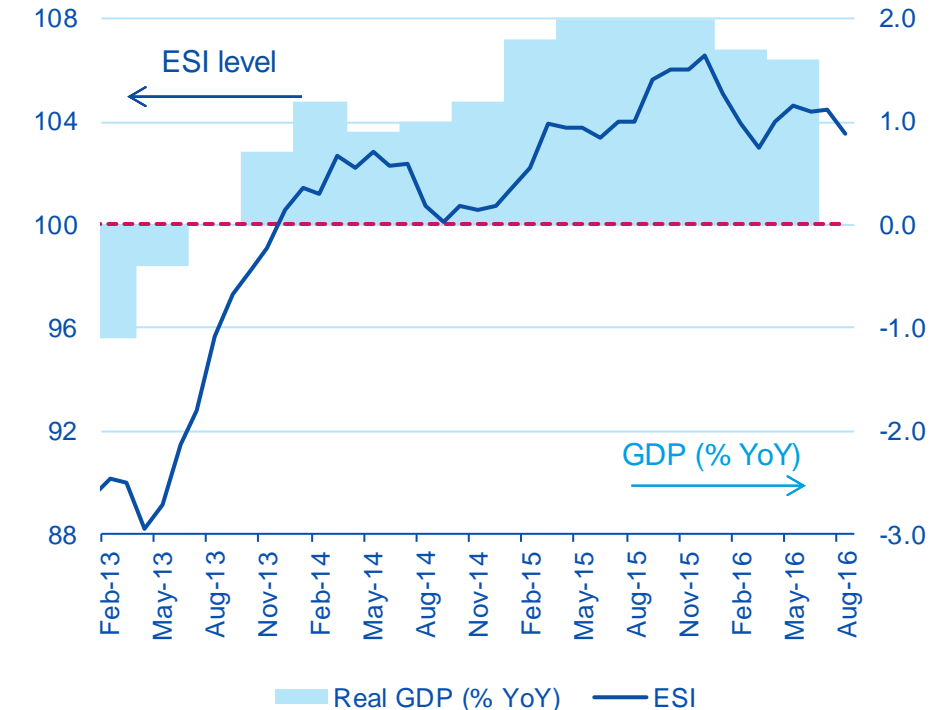
# PMIs and ESI confidence indicators remained in positive ground after Brexit, but declined in August

Confidence data showed some resilience after Brexit, but manufacturing confidence points to a gloomier outlook, while confidence in services remained stable over the last quarter

**PMI and GDP (% QoQ)**

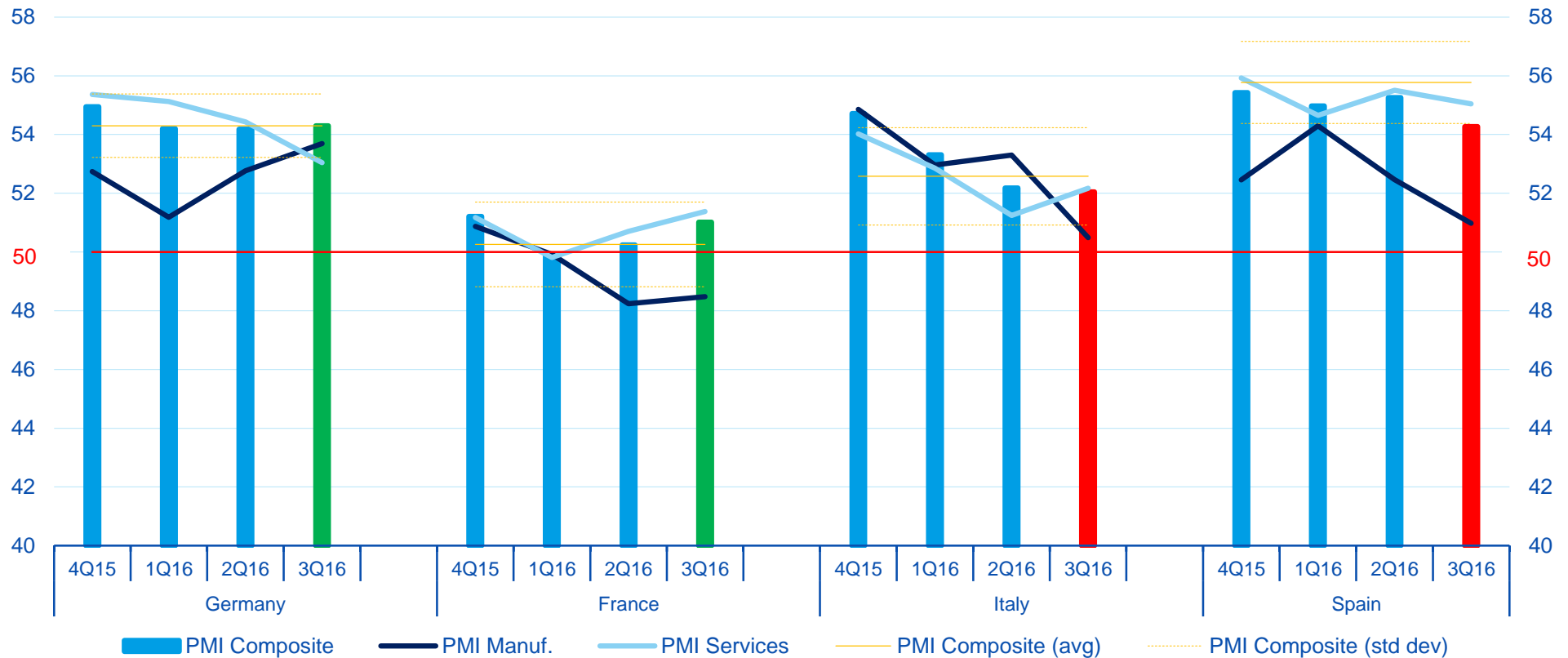


**ESI and GDP (% YoY)**



# Across countries, manufacturing PMIs fell in Italy and Spain, while services weakened in Germany

PMI (level)\*

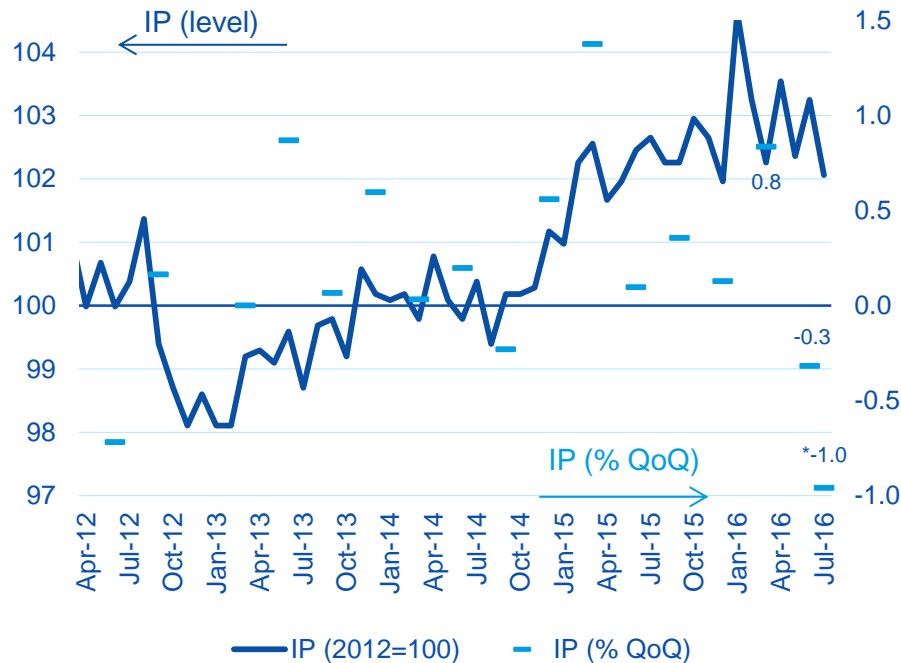


\* 3Q16 calculated using data for July and August  
 Source: Eurostat and BBVA Research

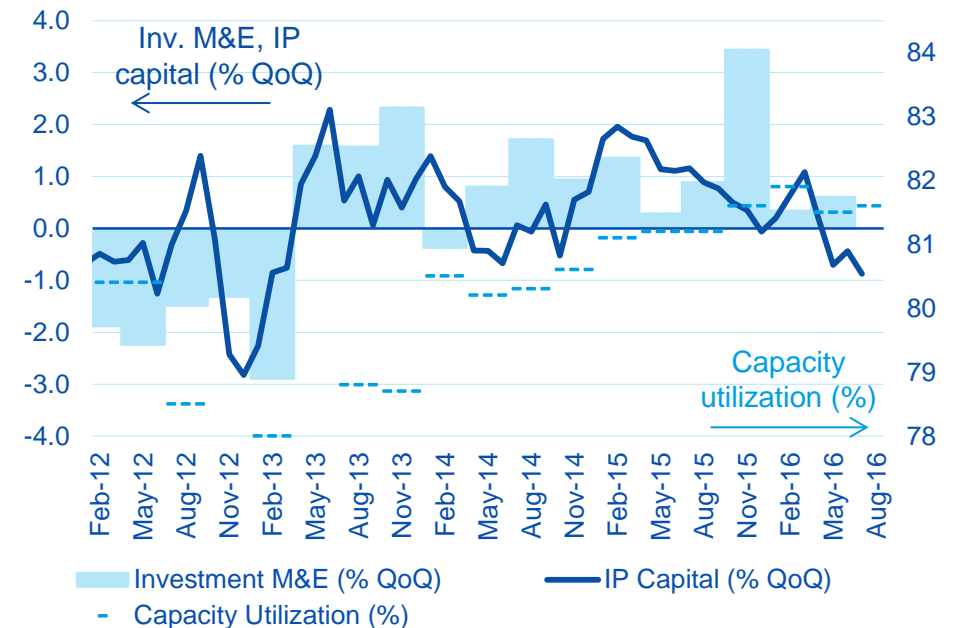
# Decline in industrial production at the beginning of 3Q16

- **Industrial production disappointed in July**, raising doubts about the sustainability of the sector recovery after failing to grow in 2Q16
- Despite positive but mild prospects for external demand and stable capacity utilization, **declining production of intermediate and capital goods** posit challenges for sustainable investment recovery

Industrial production (% QoQ)



IP Capital (% QoQ), investment in machinery and equipment (% QoQ) and utilization capacity (%)



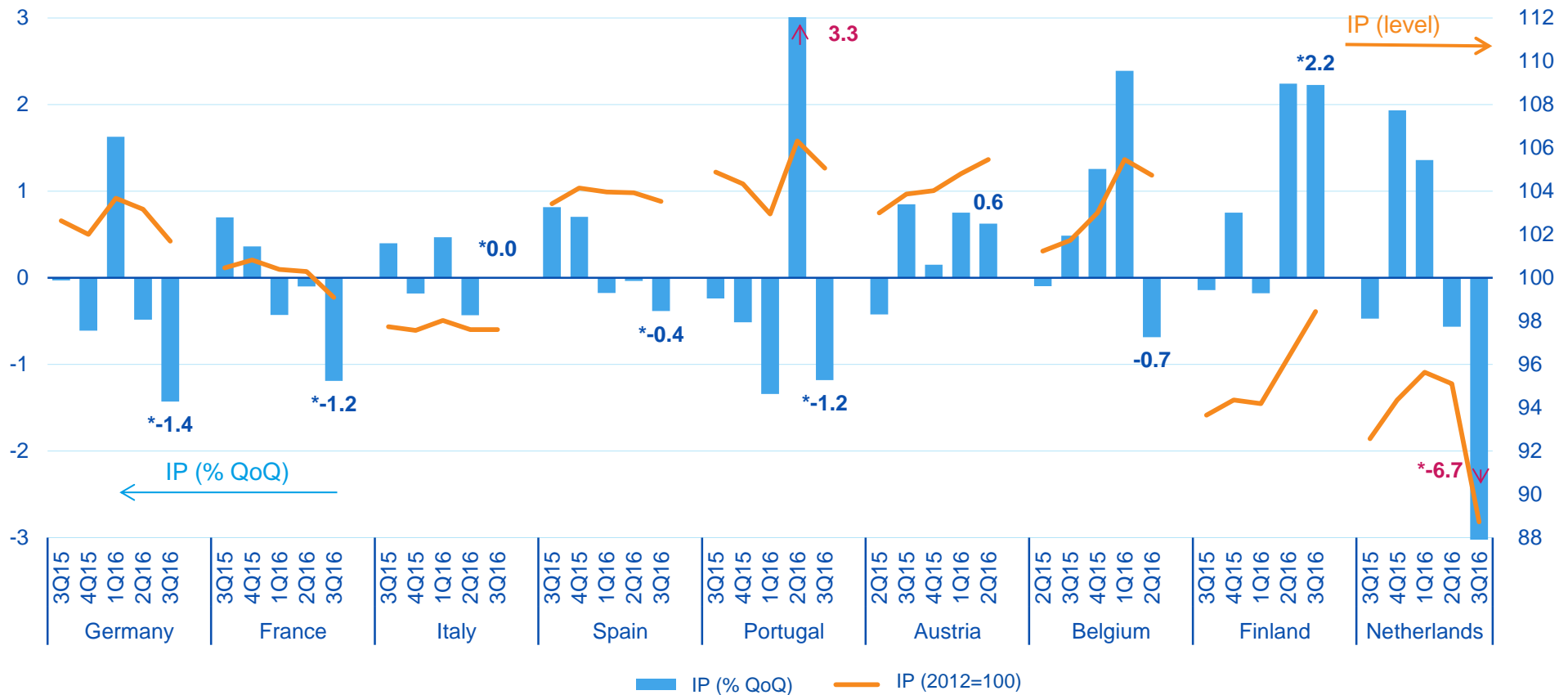
\* July with respect to three previous months

Source: Eurostat and BBVA Research

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# Across countries, the sluggishness of the industrial sector is widespread

Industrial production (% QoQ)



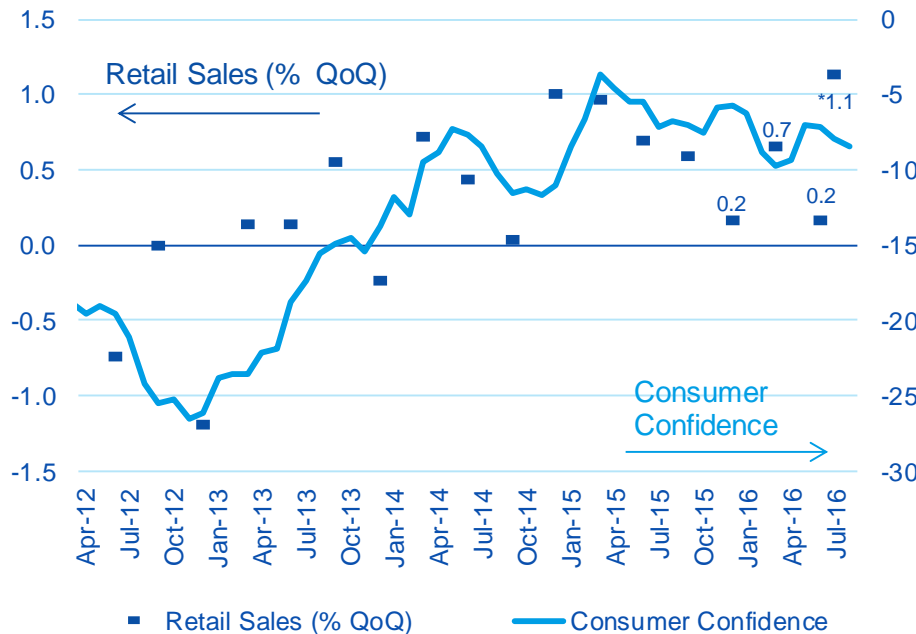
\* 3Q16 calculated using data for July  
 Source: Eurostat and BBVA Research



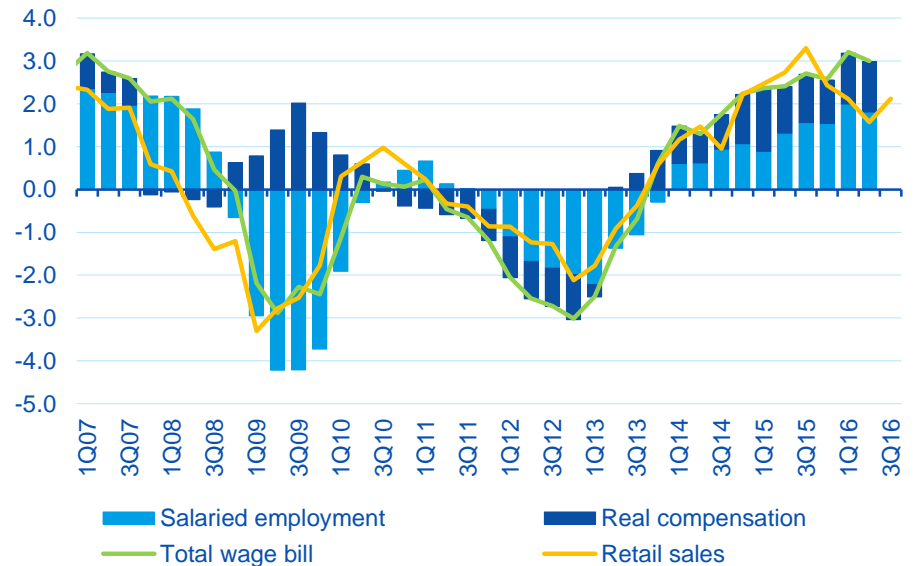
# Positive retail sales in July point to private consumption remaining as the main driver of growth

Beyond volatility over 1H16 -linked to terrorist attacks-, **retail sales increased strongly in July after the significant moderation in 2Q16** and suggest that private consumption could remain robust in 3Q16 (so far +1.1% QoQ)

Retail sales (% QoQ) and consumer confidence



Retail sales and total wage bill (% YoY)\*



\* July with respect to three previous months

Source: Eurostat and BBVA Research

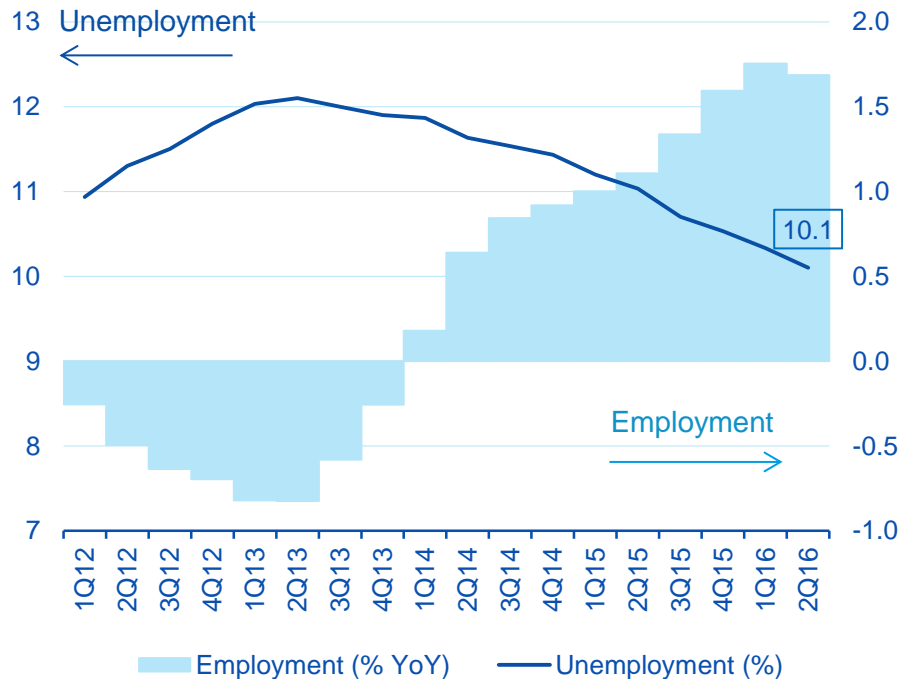
\* 3Q16 calculated using data for July

Source: Eurostat and BBVA Research

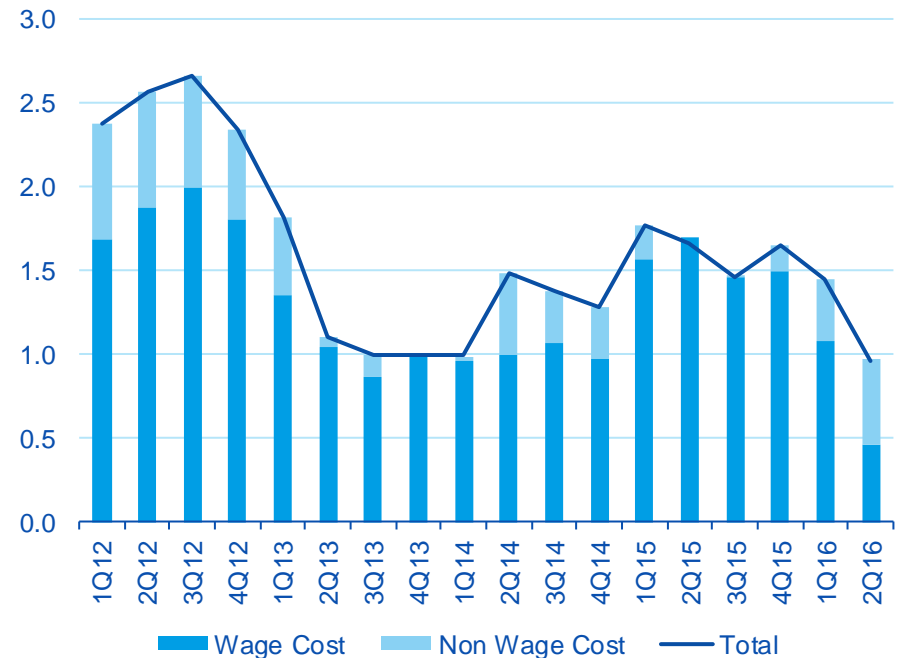
# Positive unemployment and employment dynamics, while wages moderate in 2Q16

**Unemployment continues to fall** while employment growth keeps rising beyond 1.5%. Labour costs have moderated significantly in Q2 to below 1% due to a lower wage component

**Employment (% YoY) and unemployment rate (%)**

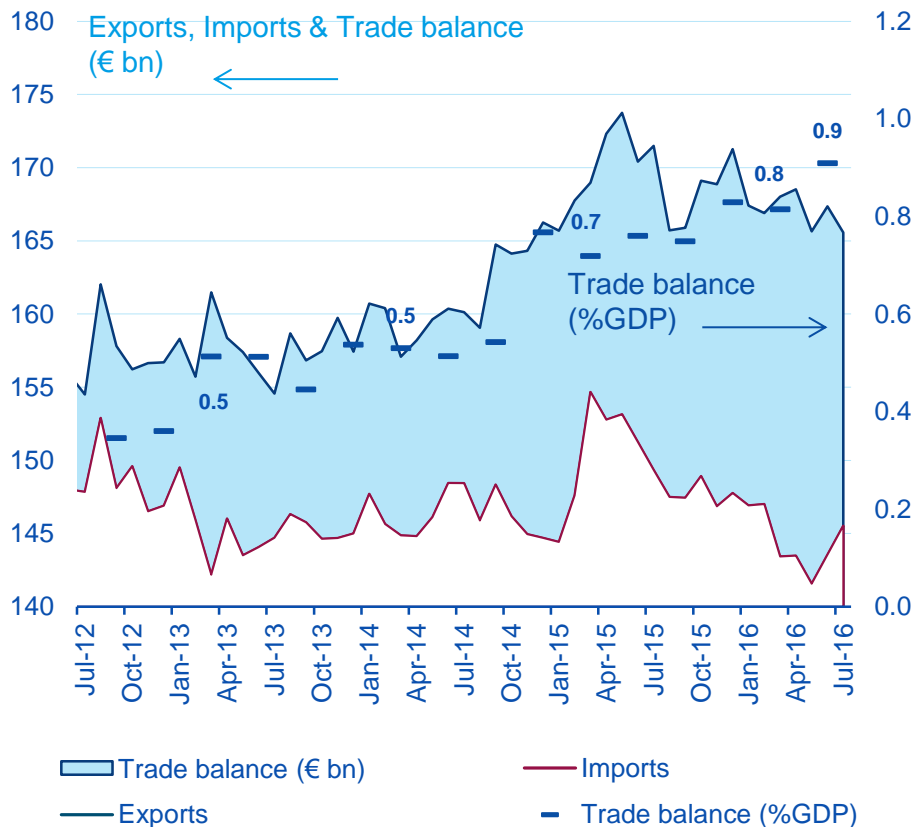


**Total labour costs (% YoY)**

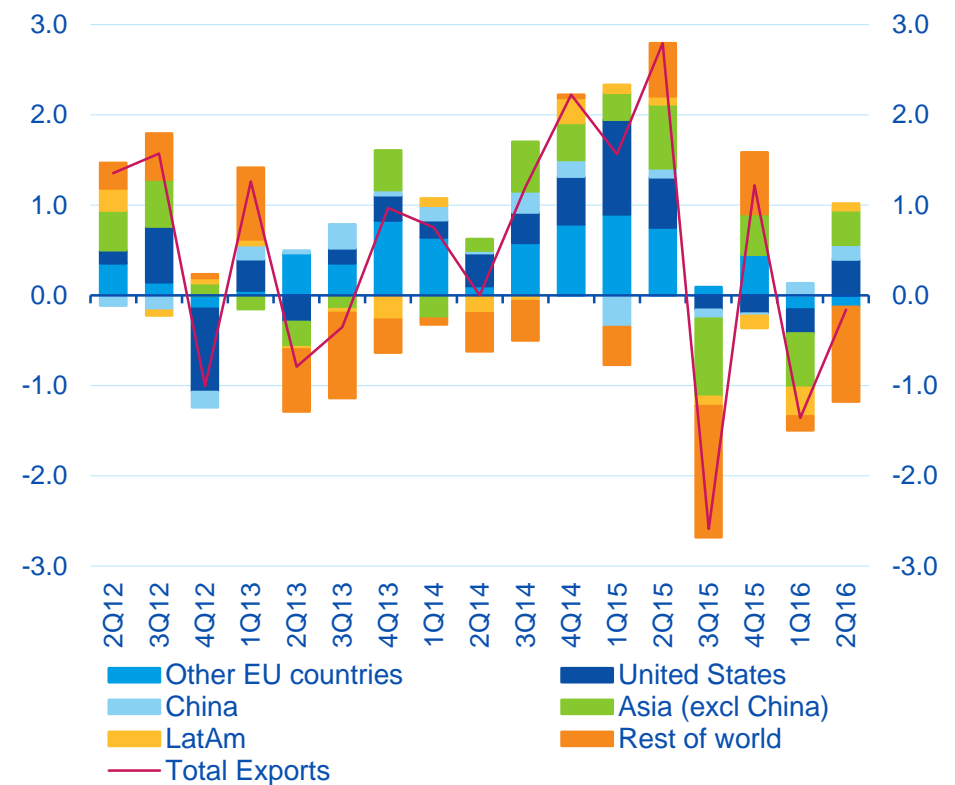


# July data point to a lower contribution of net exports in 3Q16

Trade balance (€ bn, % GDP)



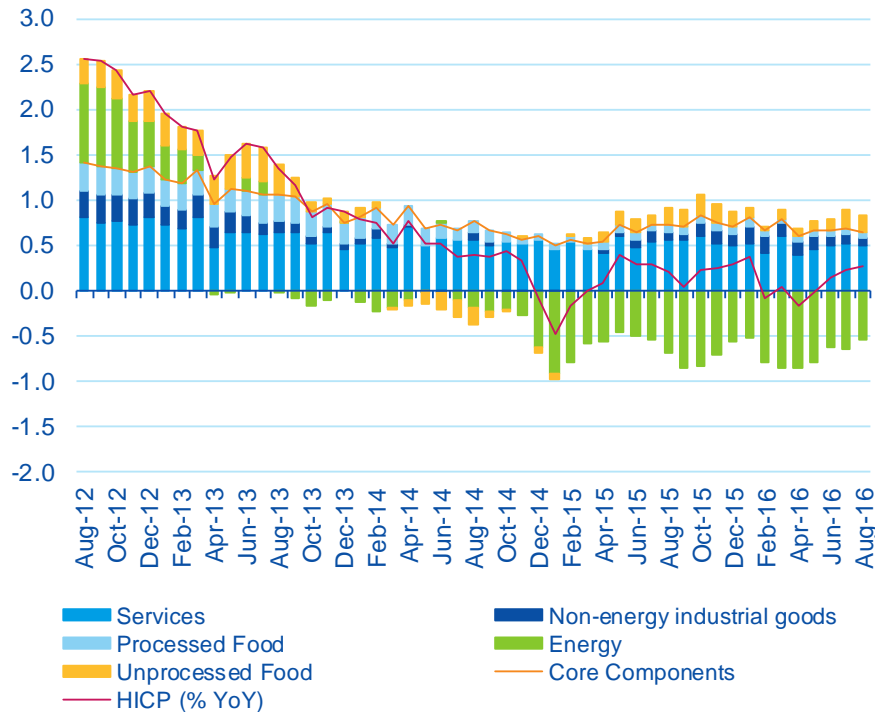
Exports (% QoQ) contribution by destination (pp)



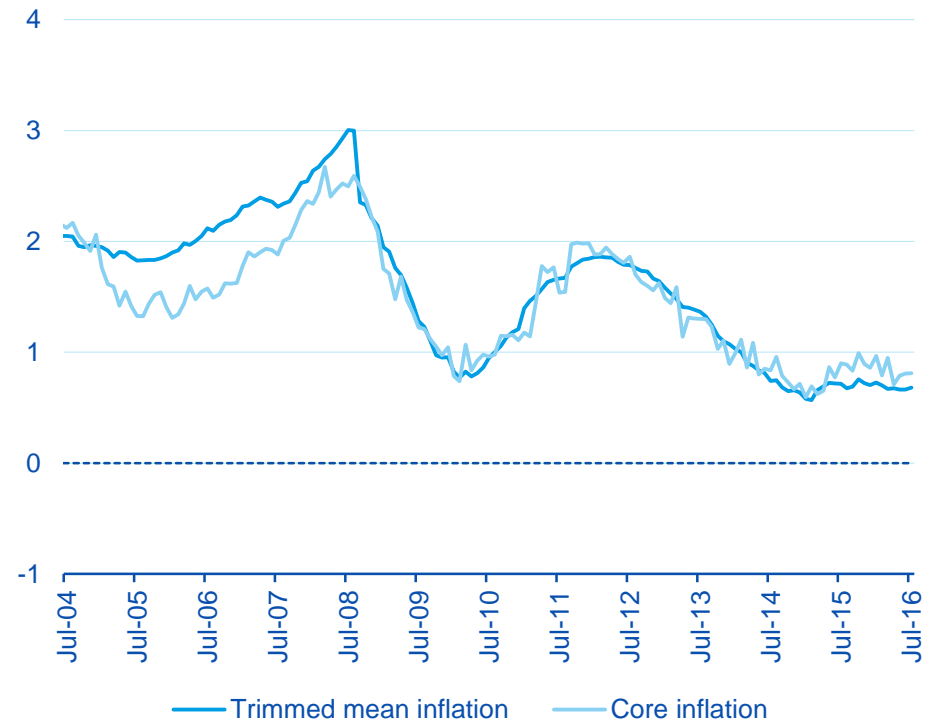
# Subdued but stable core inflation combined with lower drops in energy prices led inflation to positive rates

Easing energy base effects from a year ago might increase inflation in the coming months from the current +0.2% YoY to rates slightly below +1% in December

**Eurozone: Inflation (% YoY) and contribution of components (pp)**

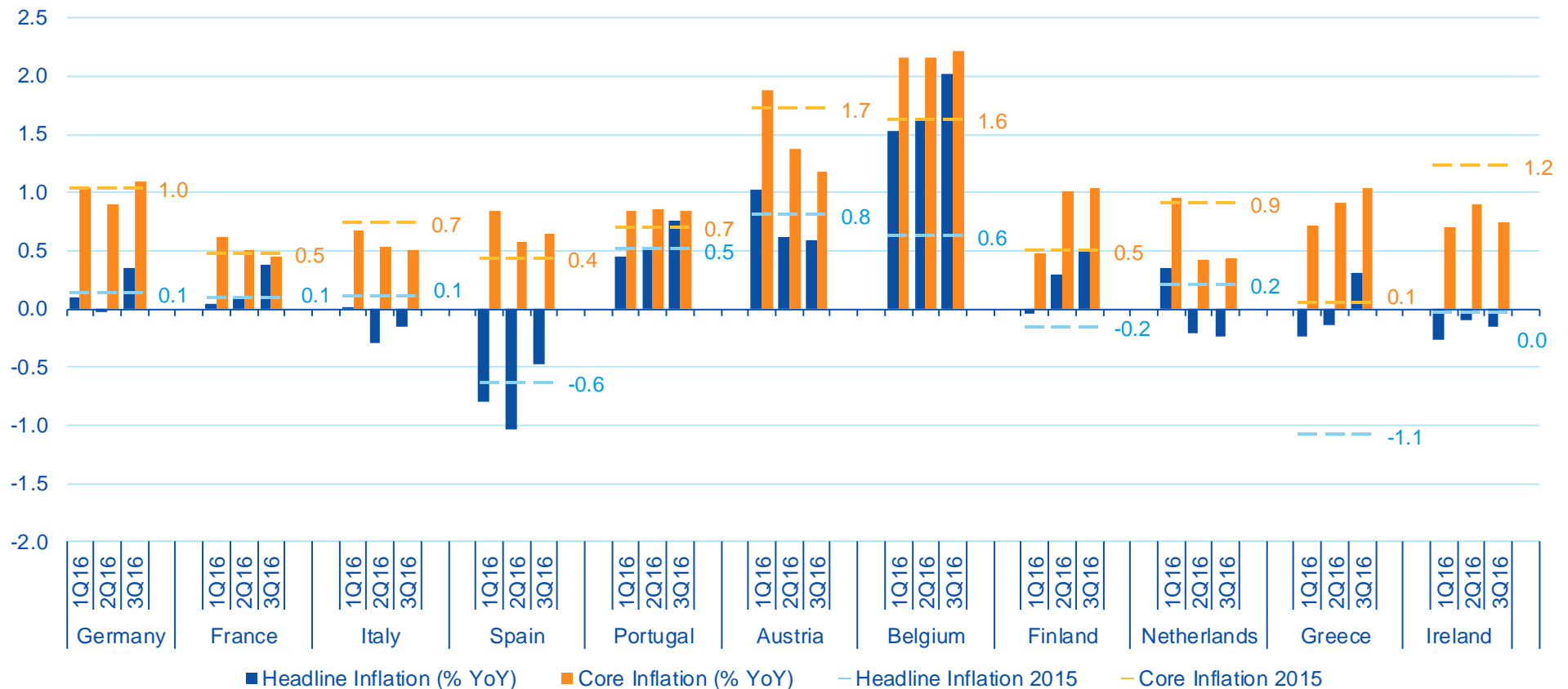


**Eurozone: inflation (% YoY)**



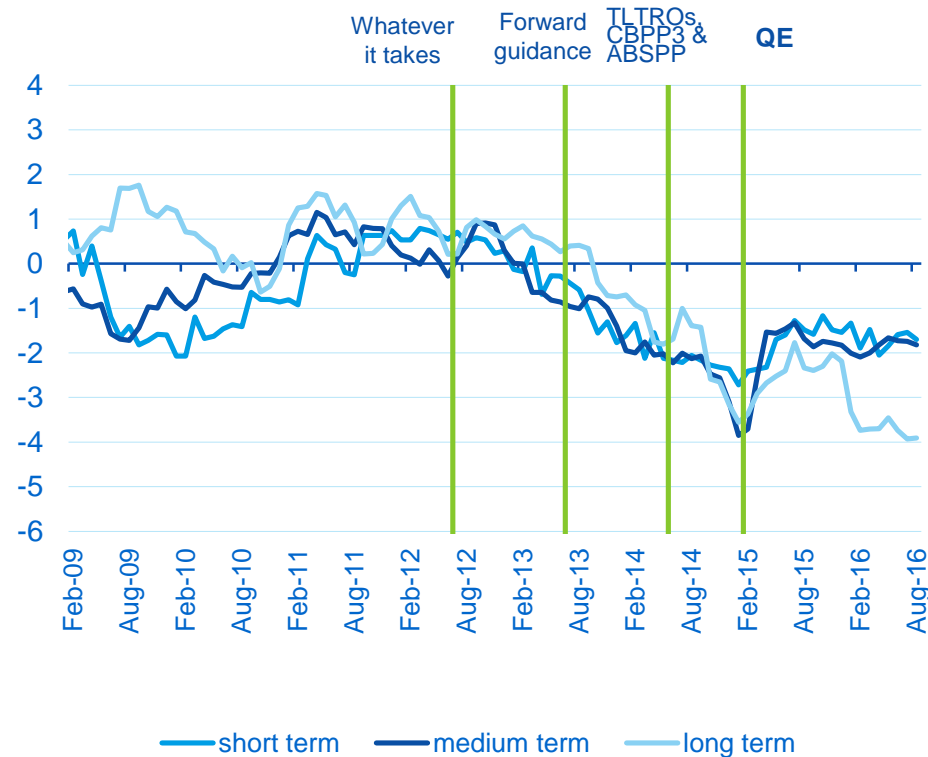
# Inflation is picking up slightly in most countries during course of 3Q16

Headline and core inflation (% YoY)



# ECB kept monetary policy stance unchanged in September, not extending QE beyond March '17

## BBVA EZ Inflation Monitor Index



Source: Reuters and BBVA Research

**September meeting:** ECB disappointed by not announcing new stimulus

- The Staff barely changed its projections over the forecast horizon
- The Governing Council tasked the relevant committees to evaluate the options available

**Before the year end:** an extension of QE (+6 months) is very likely, combined with some technical adjustments to cope with the scarcity of German bonds.

- More likely a fine-tuning in QE before any change in capital key (political decision)
- Cut in depo rate very unlikely
- Increase the amount of QE, unlikely for now

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