

EUROZONE

ECONOMIC WATCH

JANUARY 2017



Key messages: some changes for the better

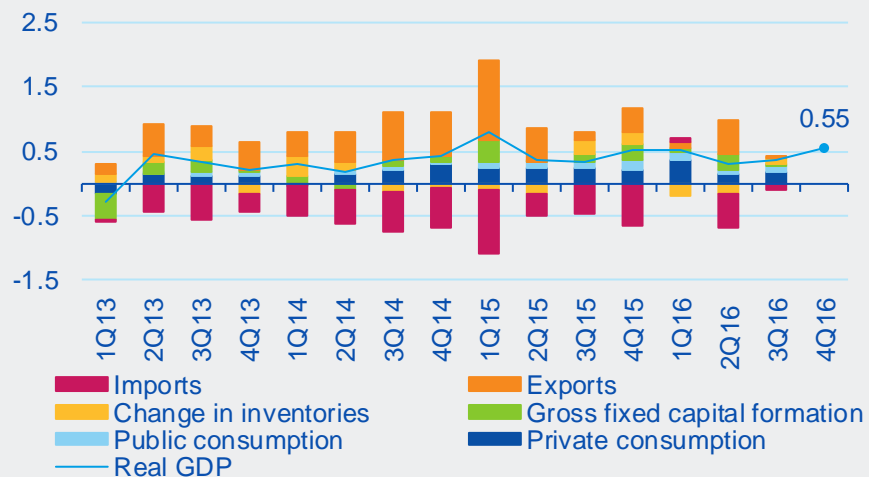
- **Improving confidence in 4Q16** across the board **shows the resilience of the eurozone** to the various potentially disturbing political events during the second half of 2016, while leading components suggest a **slightly more optimistic outlook for coming months**, supported by increasing export orders and the depreciation of the euro.
- **Hard data up to November** also point to the same direction. **The strength of consumption** remains in place **and exports seem to recover, but concerns about the weakness of investment have not been dispelled**. Beyond data volatility in 4Q16, positive underlying signs are taking root.
- Our **MICA-BBVA model estimates quarterly GDP growth in the eurozone to gain momentum to 0.5/0.6% QoQ in 4Q16**, after growth of 0.3% in the previous two quarters.
- **These figures point to growth of 1.7% in 2016 and to a slight upward bias for 2017** (our last projections stood at 1.5%), but we remain cautious on the outlook for coming quarters given the wide range of risks.
- **Risks remain tilted to the downside and are mostly political**, both at national and regional level, but derive also from financial sector fragilities and public debt sustainability in some countries.
- **Inflation is picking up** given the energy prices' base effects, **but core measures remain subdued**. We continue to expect headline inflation to increase in early 2017 (to around 1.8% YoY, and then to fall back a bit) mostly due to oil price increases and base effects.

ECONOMIC DEVELOPMENTS

GDP growth seems to have accelerated in 4Q16...

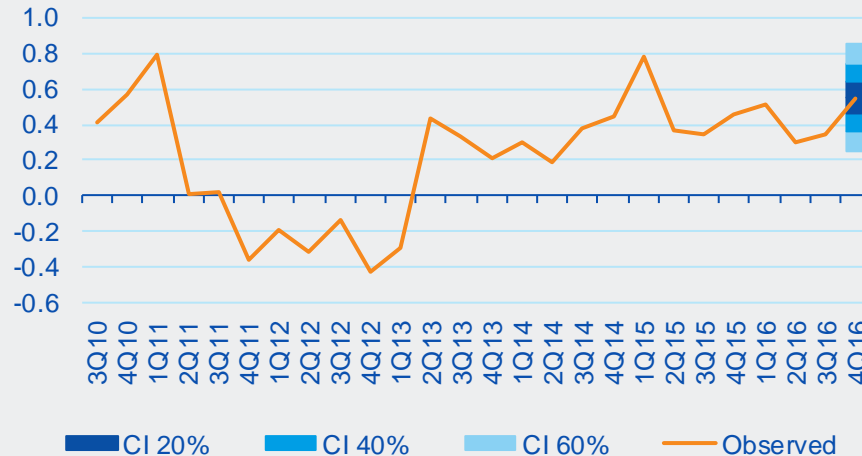
GDP, CONTRIBUTION BY COMPONENTS

(%QoQ, pp)



GDP AND MICA FORECASTS

(%QoQ)

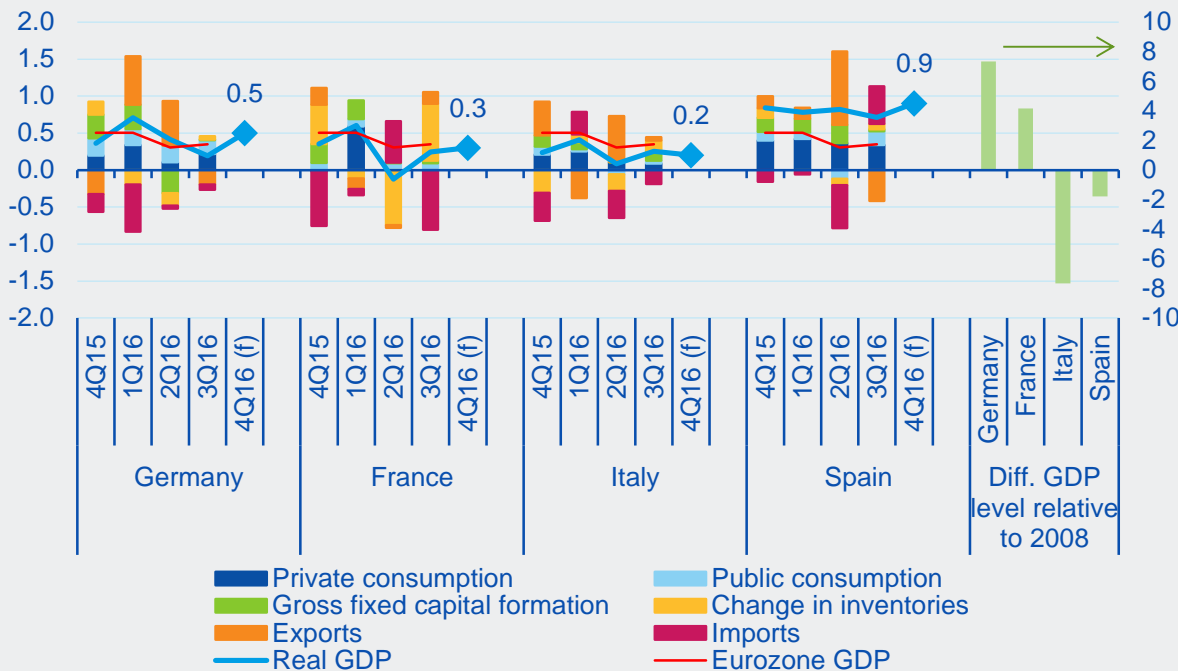


- **GDP growth stable in 3Q16** (0.3% QoQ), thanks to stronger consumption and despite low investment and a negative contribution from net exports
- Available indicators suggest that the **economy gained sizable traction in 4Q16**, as the eurozone has shown high resilience to increased political uncertainty
- **Domestic demand continues to support growth** thanks to a continued decline of labor market slack and favorable policies, **added to tailwinds** such as improving global demand and euro depreciation

ECONOMIC DEVELOPMENTS

... with improvements in Germany and Spain

GDP, CONTRIBUTION BY COMPONENTS (%QoQ, pp)

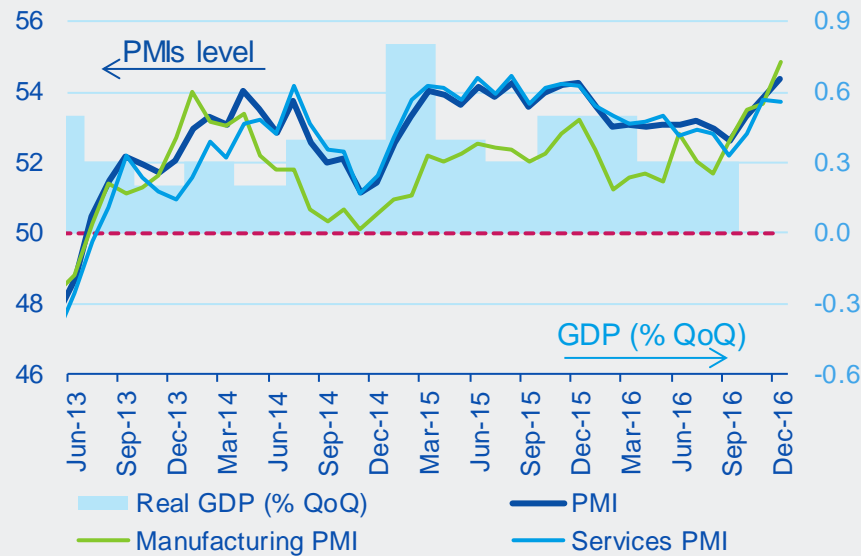


- Data for 4Q16 point to **further widespread acceleration of GDP growth...**
- ...in **Germany** (BBVAe: 0.5% QoQ after 0.2% QoQ), **Spain** (BBVAe: 0.9% QoQ after 0.7% QoQ), and **France** (BBVAe: 0.3% QoQ after 0.2% QoQ)
- In contrast, **Italy growth could slow in 4Q16** (BBVAe: 0.2% QoQ after 0.3% QoQ in 3Q16)

ECONOMIC DEVELOPMENTS

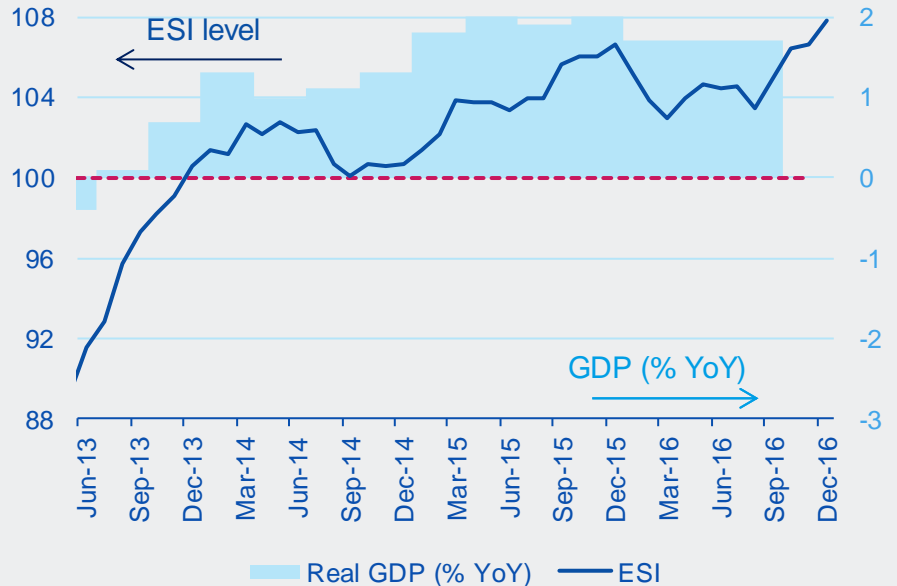
Confidence gains traction in 4Q across sectors, showing resilience to political uncertainty

PMI AND GDP
(level, %QoQ)



- Confidence data **so far continue to show the economy's resilience** to increasing uncertainty since the summer, with manufacturing increasing strongly driven by expectations on global demand and a weaker euro

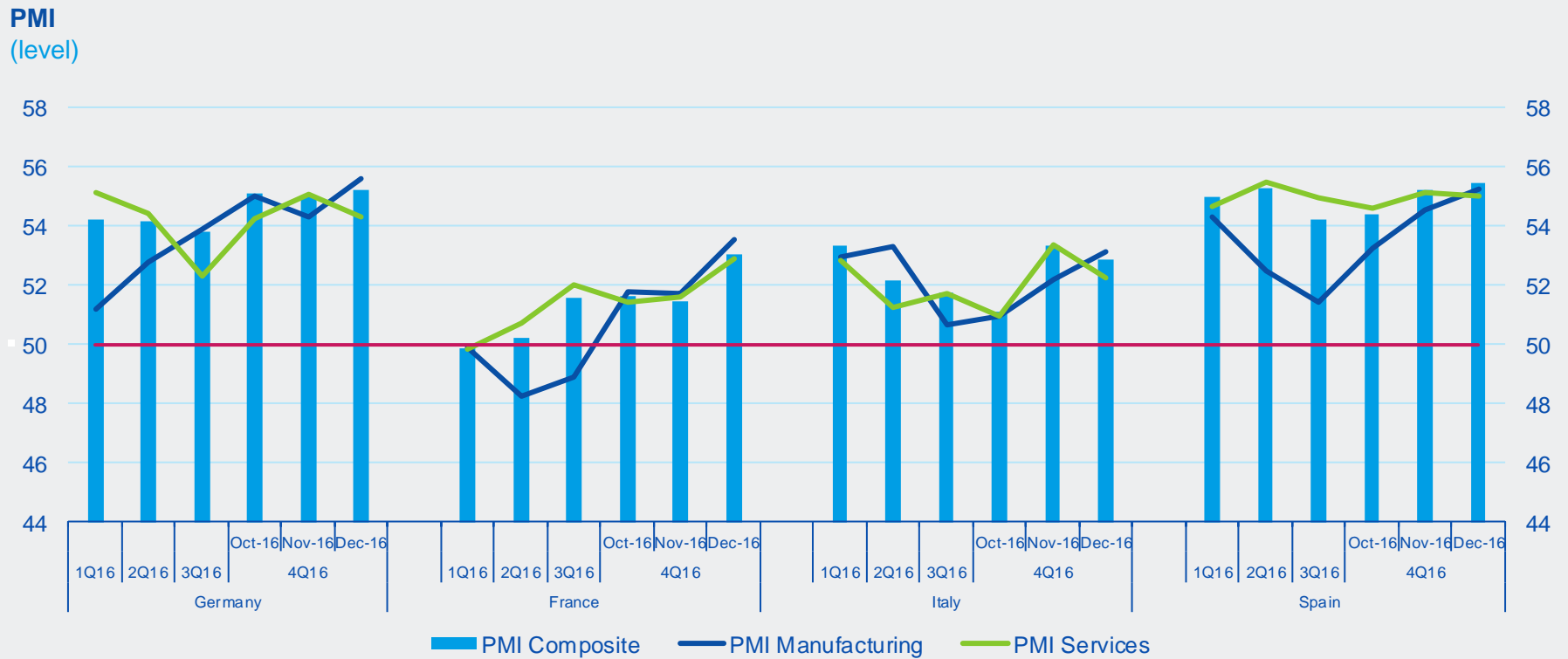
ESI AND GDP
(level, %QoQ)



- But **we remain cautious** as political events in coming months could end up weighing on confidence

ECONOMIC DEVELOPMENTS

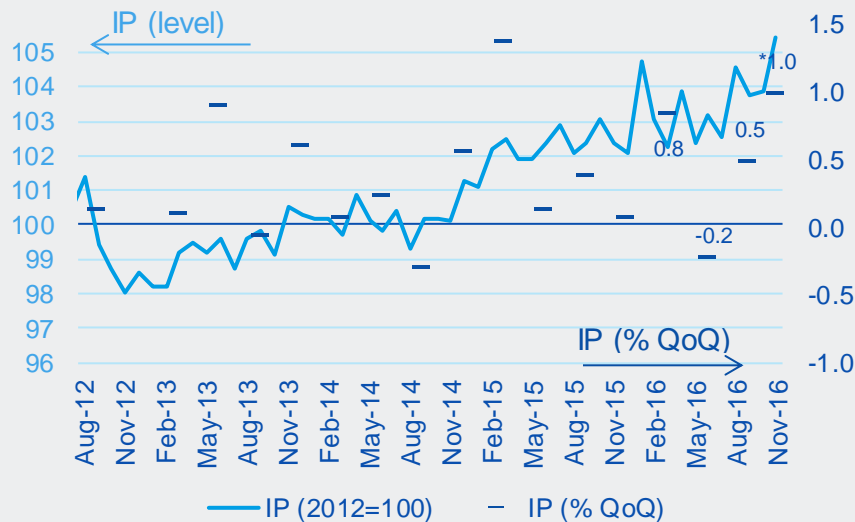
Manufacturing and services' PMIs improved in all core countries in 4Q, although German and Italian services slowed in December



ECONOMIC DEVELOPMENTS

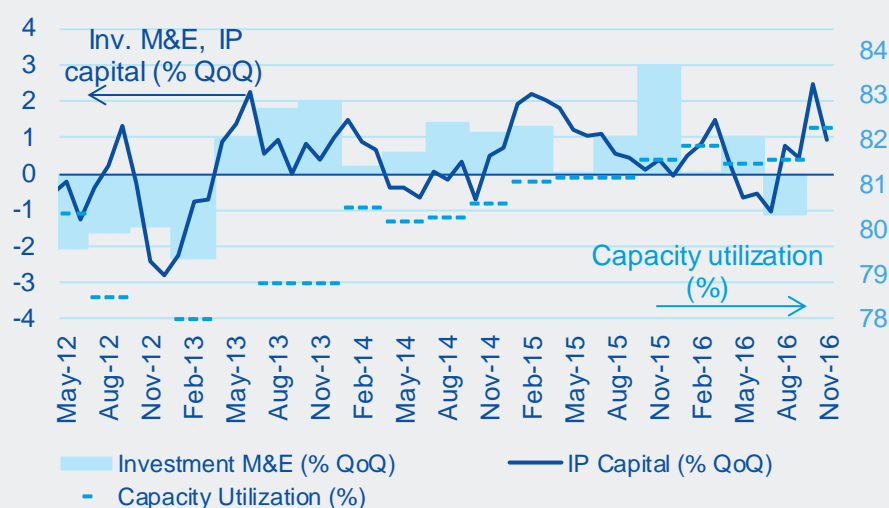
Sharp increase of industrial output in November. Positive signs stem from the good performance of capital and intermediate goods in 4Q

INDUSTRIAL PRODUCTION
(%QoQ, pp)



- Industrial production **increased 1.5% MoM in November** after 0.1% MoM in October, **accelerating with respect to 3Q16** (1.0% QoQ)

IP CAPITAL, INVESTMENT IN MACHINERY AND EQUIPMENT AND UTILIZATION CAPACITY
(%QoQ, %)



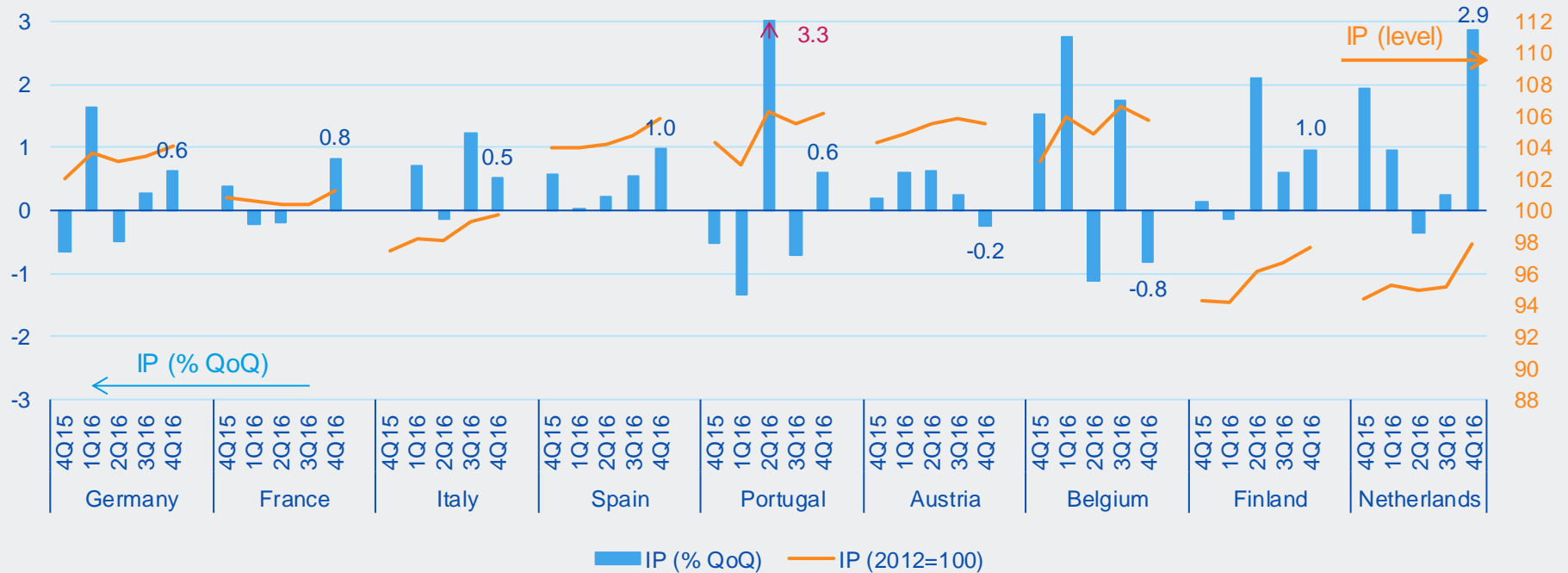
- Production of **capital and durable consumer goods** added to **high capacity utilization** suggest a recovery in equipment and machinery investment in 4Q16

*October and November with respect to three previous months
Source: Eurostat and BBVA Research

ECONOMIC DEVELOPMENTS

Mixed growth of industrial output across countries, with an acceleration in most core countries at the end of 2016

INDUSTRIAL PRODUCTION (%QoQ, pp)

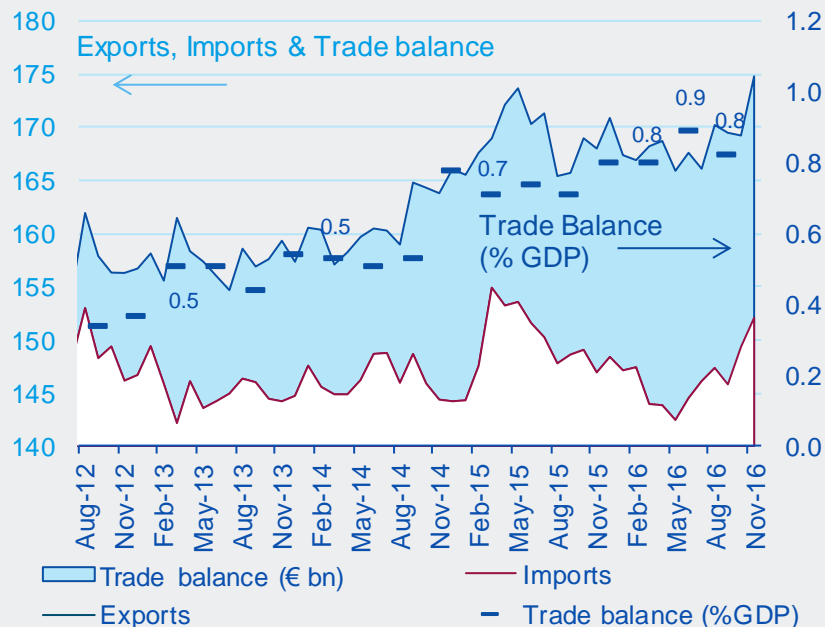


*4Q16 calculated using October and November data. Only October for Austria and Belgium
Source: Eurostat and BBVA Research

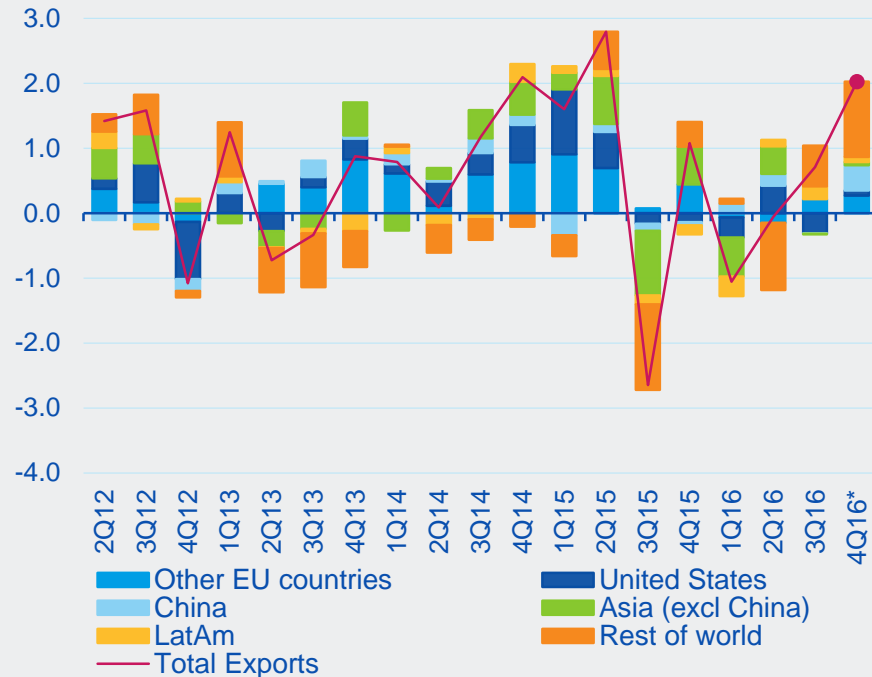
ECONOMIC DEVELOPMENTS

Exports picked up in November, sustaining the upward trend observed over the second half of the year

TRADE BALANCE
(€ bn, %GDP)



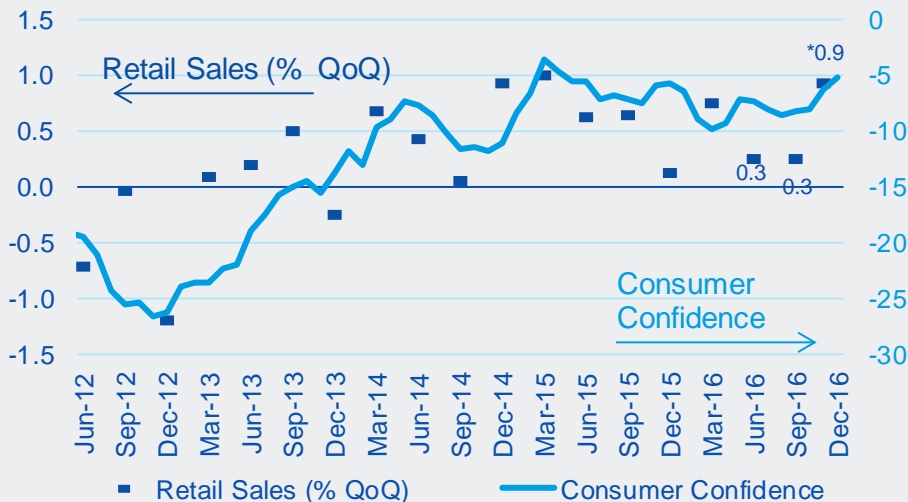
EXPORTS CONTRIBUTION BY DESTINATION
(%QoQ, pp)



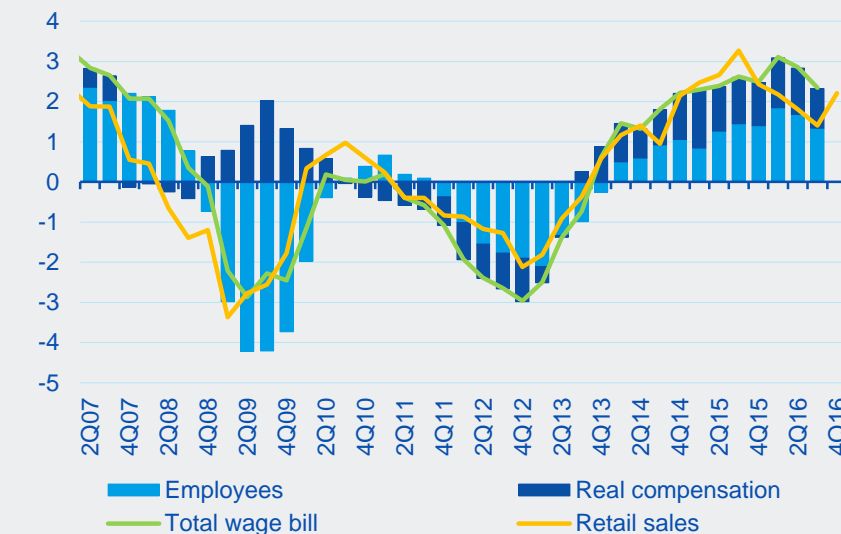
ECONOMIC DEVELOPMENTS

Improvement of retail sales suggests that private consumption continued to underpin growth in 4Q16

RETAIL SALES AND CONSUMER CONFIDENCE
(%QoQ, pts)



RETAIL SALES AND TOTAL WAGE BILL
(%YoY)



- **Retail sales declined in November** (-0.4% after +1.4 MoM in October). Nonetheless, overall figures of 4Q16 (0.9% QoQ) revert the moderation of the previous two quarters

- **Consumer confidence continued to gain momentum at the end of 2016.** Together with labour market gains should support household spending

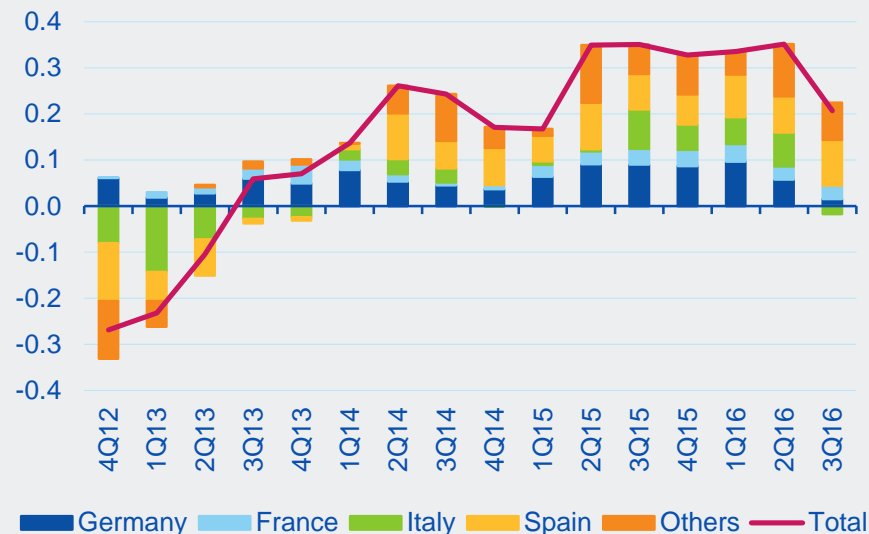
*October and November with respect to three previous months
Source: Eurostat and BBVA Research

ECONOMIC DEVELOPMENTS

Employment growth slowed in 3Q mainly driven by weaker public and private services ...

JOB GROWTH CONTRIBUTION BY COUNTRY

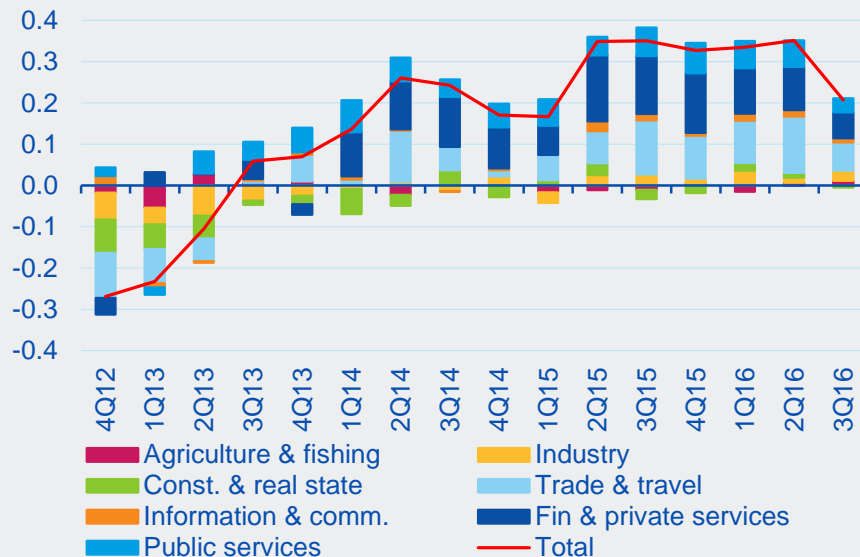
(pp, %QoQ)



- Lower employment growth contribution from Germany and Italy in 3Q16, but higher from Spain

JOB GROWTH CONTRIBUTION BY SECTOR

(pp, %QoQ)



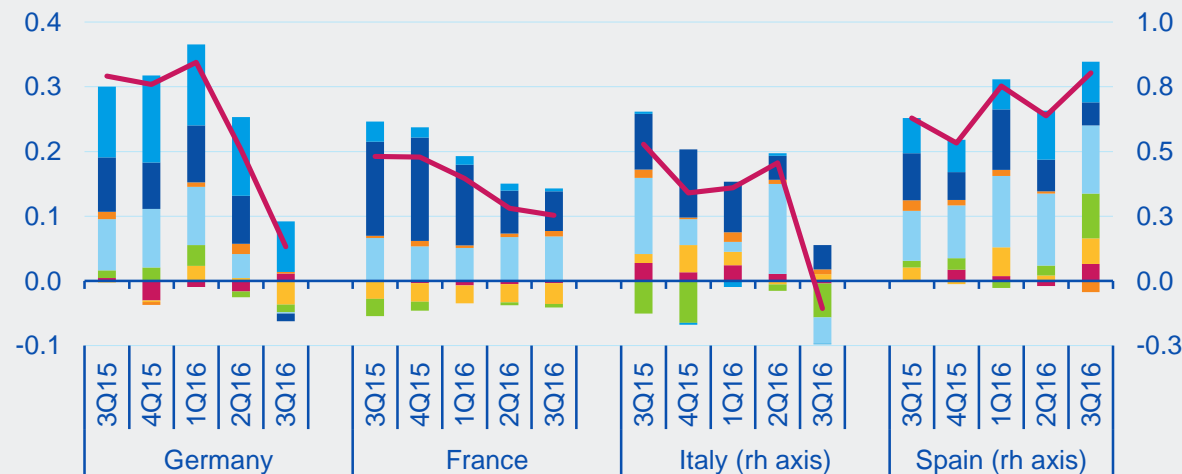
- By sector, lower contributions from public and private services, which add to trade and travel activities

ECONOMIC DEVELOPMENTS

...with weakness mostly in Germany and Italy, while job creation continued in France and Spain

JOB GROWTH CONTRIBUTION BY SECTOR

(pp, %QoQ)

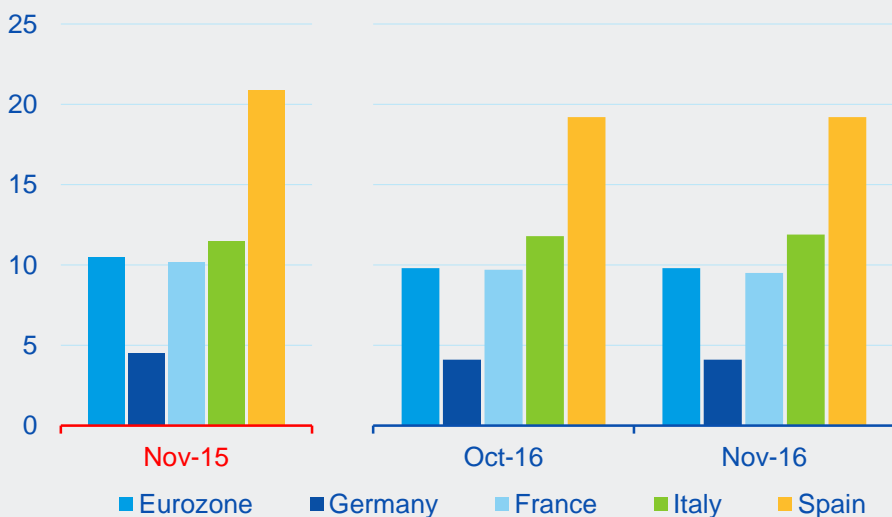


- **Public employment** explained all job growth in **Germany**, offsetting the decline of private employment growth
- **Job destruction in Italy** in 3Q driven by construction, trade and travel activities
- Employment growth in **France and Spain** still supported by services

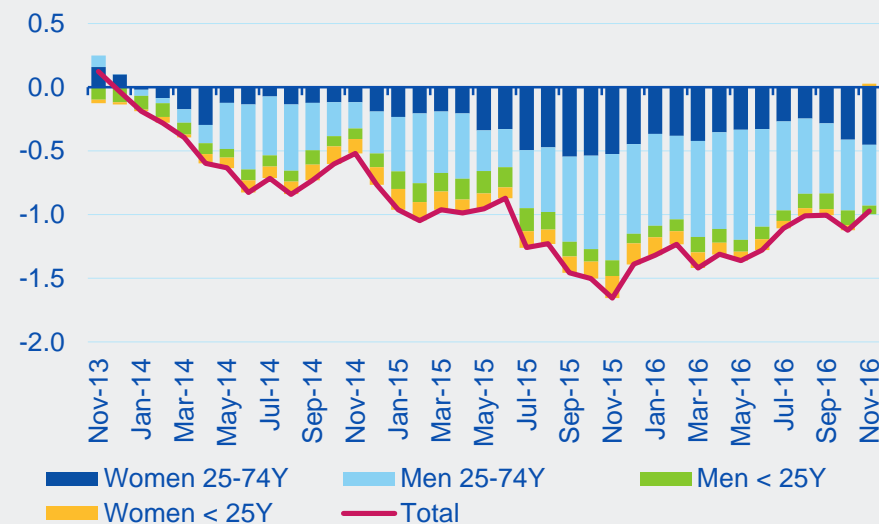
ECONOMIC DEVELOPMENTS

Unemployment continued to decline during 4Q16 to stand at 9.8% in the Eurozone as a whole

UNEMPLOYMENT RATE BY COUNTRY (%)



ANNUAL UNEMPLOYMENT CHANGE BY GENDER & AGE (millions)



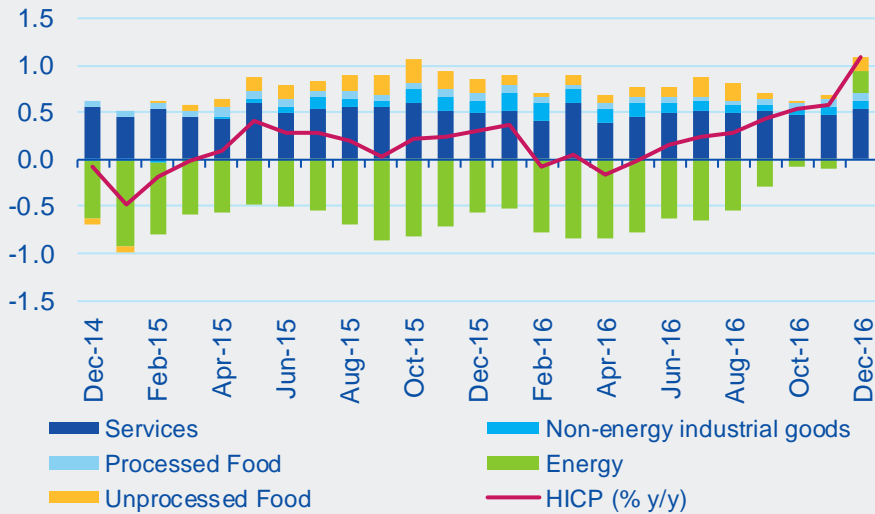
- **Jobless rate continues to fall at a low pace**, driven mostly by Spain

- **Unemployed decline** is observed mostly among the experienced population

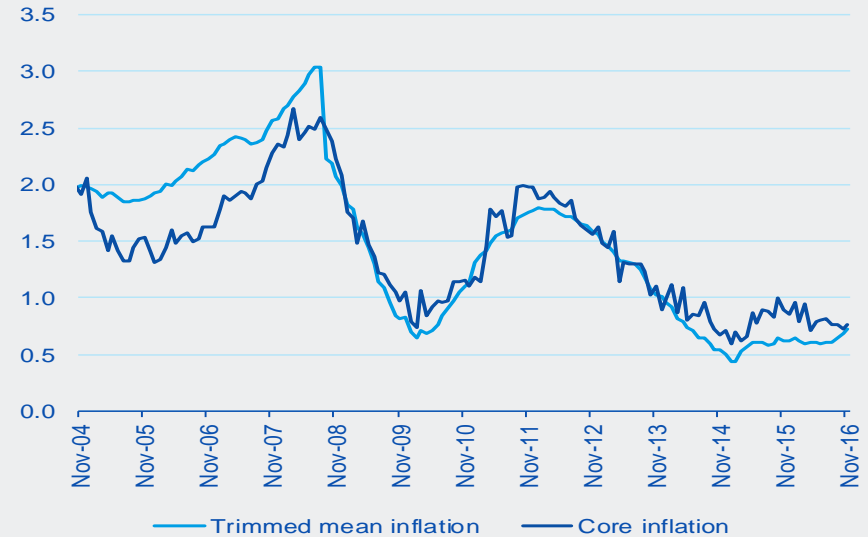
ECONOMIC DEVELOPMENTS

Annual headline inflation accelerated to 1.1% YoY in December last year driven by energy prices, but the core rate remained subdued

INFLATION AND CONTRIBUTION OF COMPONENTS (%YoY, pp)



INFLATION AND TRIMMED MEAN (%YoY)



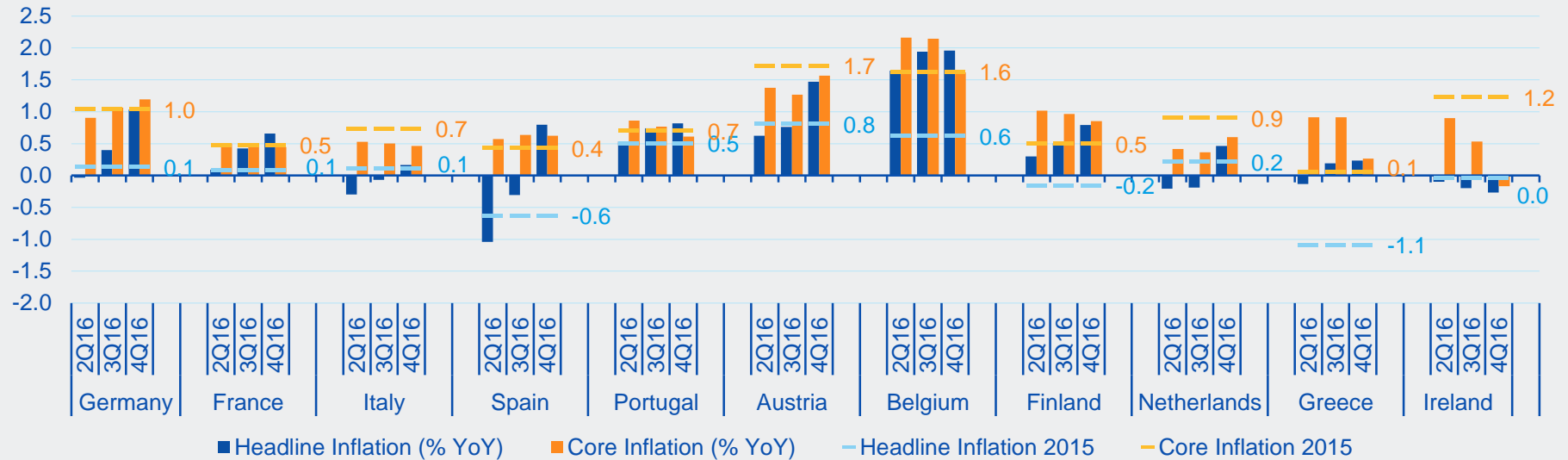
- Eurozone **HCPI** came out slightly higher than expected at **1.1% YoY in December**, accelerating from previous month (0.6% YoY in November) and marking the highest figure since September 2013

- The **core measure** increased slightly to 0.9% YoY
- **We expect increases in inflation in early 2017** to around 1.8% YoY

ECONOMIC DEVELOPMENTS

Inflation is picking up in most countries in 4Q16

HEADLINE AND CORE INFLATION (%YoY)



- By country, **HCPI inflation picked up in all core countries** in December 2016: **Germany** (1.7% after 0.7% YoY), **Spain** (1.4% after 0.5% YoY), **Italy** (0.5% after 0.1% YoY) and **France** (0.8% after 0.7% YoY)

EUROZONE

ECONOMIC WATCH

DECEMBER 2016



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