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Eurozone Economic Watch

Sept 2017

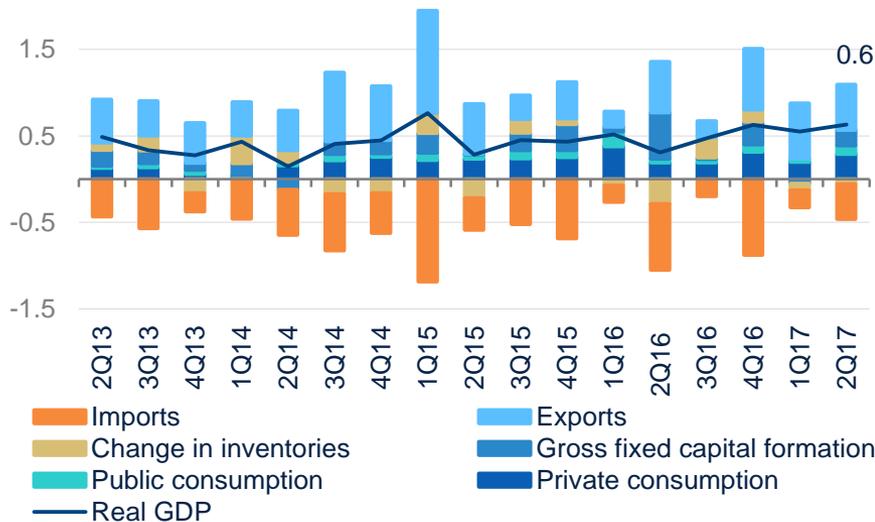


Eurozone: Growth expected to stabilize in 3Q on strong confidence

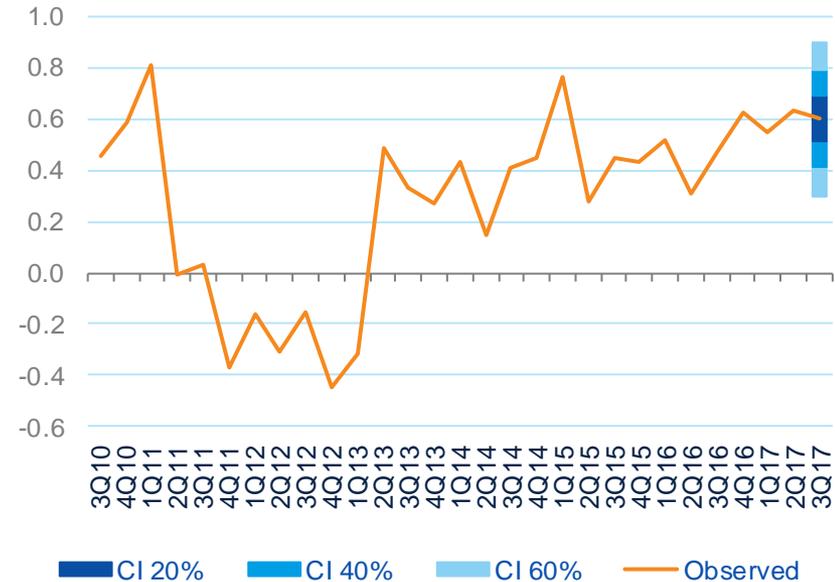
- ◆ **After the positive surprise in Q2 GDP growth (0.6%), the outlook seems to stabilize in 3Q17**, while underlying figures continued to suggest a solid recovery.
- ◆ Our **MICA-BBVA model** for short-term growth estimates a quarterly **GDP figure of 0.6% in 3Q17**, but **we cannot rule out a slight moderation given weaker hard data**. Overall, the performance in the central quarters of the year poses an **upward bias for this year's growth forecasts (2%)**.
- ◆ **Confidence data remained positive across major countries in 3Q17**, characterized by a lower optimism in services and improving manufacture sentiment.
- ◆ **Retail sales moderated in July**, but employment gains and high consumer confidence will continue to support growth of private consumption in the quarter.
- ◆ **Foreign trade is slowing down in 3Q17**, which adds to the milder growth of industrial output in July.
- ◆ **Inflation accelerated in August to 1.5% YoY driven by energy and food prices**, but core measures remained steady (at 1.3% YoY) and subdued. **Expect lower headline inflation in the months ahead** due to energy prices.

Incoming data of 3Q suggest a stabilization of GDP growth after a slight positive surprise in the previous quarter

GDP, Contribution by Components
(%QoQ, pp)



GDP and MICA forecasts
(%QoQ)

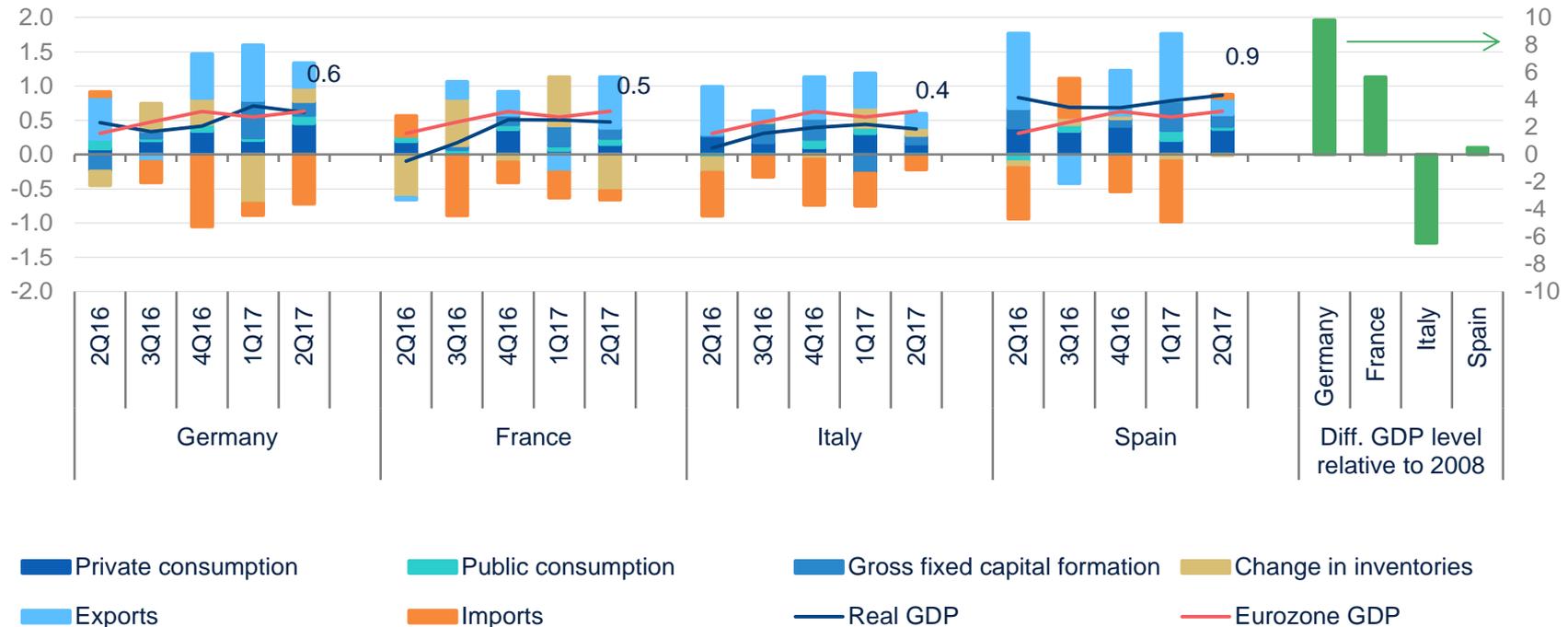


Source: Eurostat and BBVA Research

- ◆ GDP growth accelerated to **0.6% QoQ** in 2Q17. **Domestic demand** is still behind the recovery, strengthening on the back of **investment**
- ◆ As a consequence, imports accelerated more than exports, leading to a **lower contribution from external demand**
- ◆ Our **MICA-BBVA** model suggests a stabilization of **GDP growth at 0.6% in 3Q17**, but we cannot discard some moderation

France and Italy GDP growth remained stable at decent levels in 2Q17, while Germany registered a slight deceleration to 0.6%

GDP, Contribution by components
(%QoQ, pp)

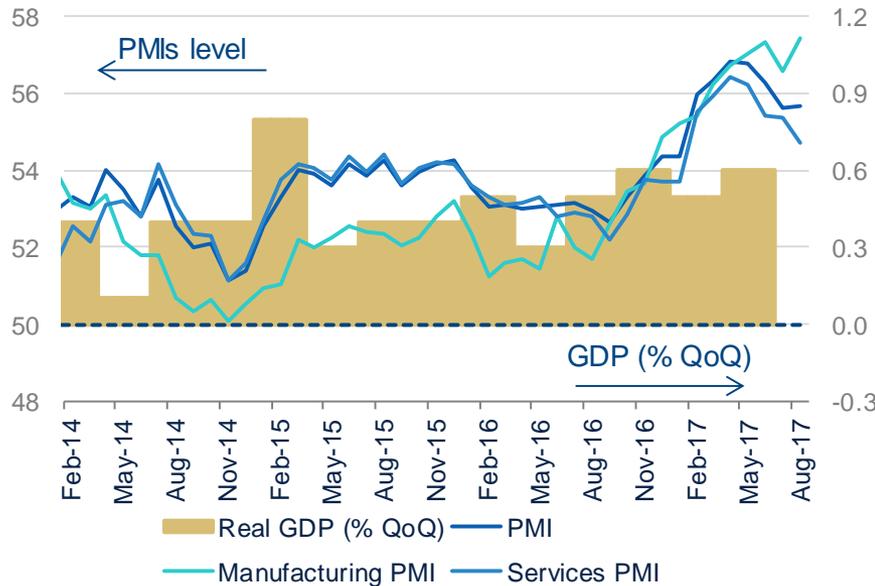


Source: Eurostat and BBVA Research

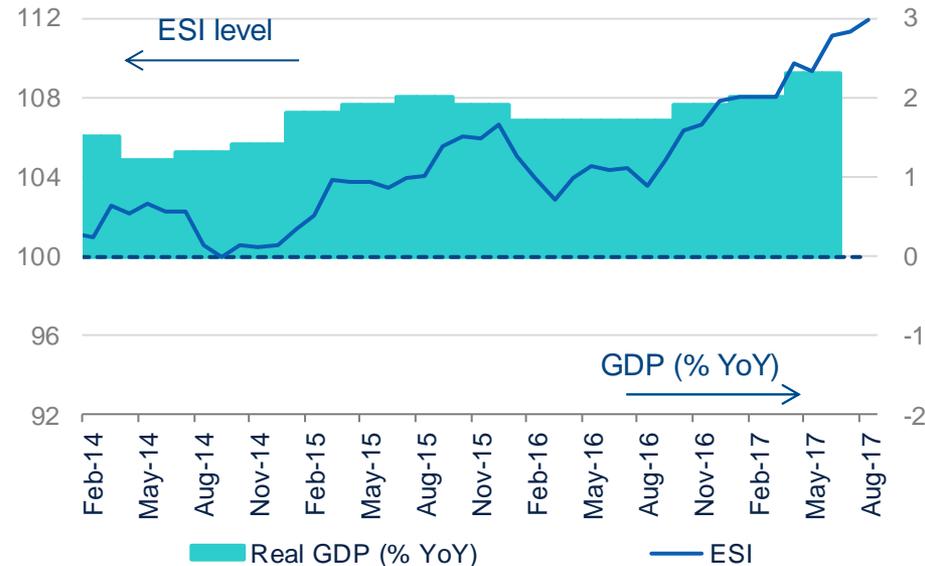
- ◆ In France, GDP grew 0.5% QoQ in 2Q17 driven by a strong net exports' contribution
- ◆ In contrast, domestic demand was the main contributor in Germany (+0.5pp driven by consumption) and Italy (+0.4pp contributed by investment)
- ◆ Spain's growth continues to outperform the region, at 0.9% QoQ, though it seems to be decelerating

Overall, PMI confidence figures remained steady in August supported by a buoyant manufacturing sector

PMI and GDP
(level, %QoQ)



ESI and GDP
(level, %YoY)



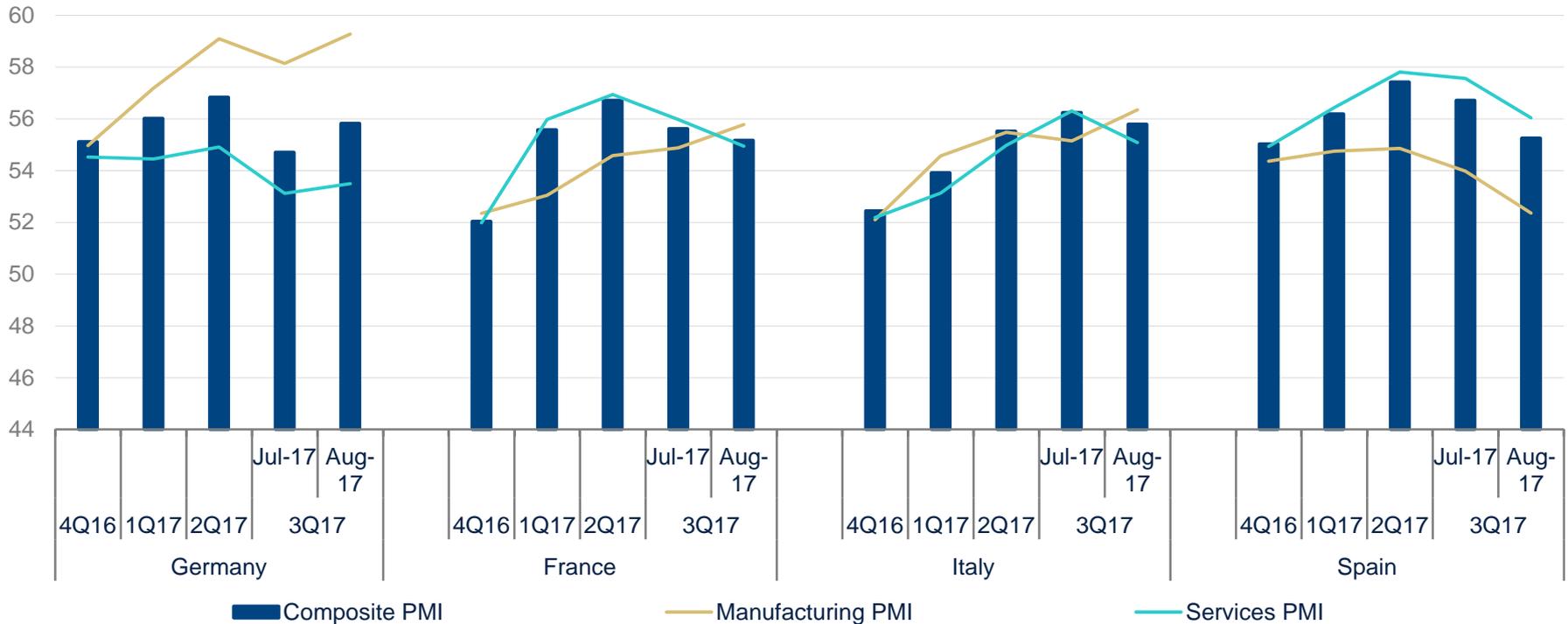
Source: Eurostat and BBVA Research

◆ **Confidence figures remained broadly stable at high levels** but hiding some decoupling between a stronger manufacturing sector and a milder optimism in services

◆ **Confidence among both businesses and consumers has risen to its highest level** since before crisis, according to the European Economic Sentiment

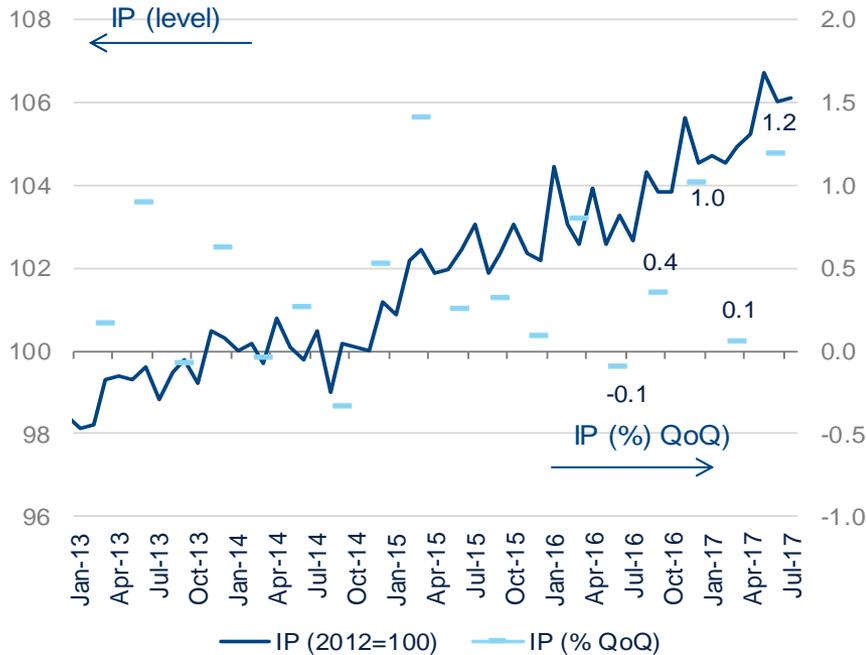
Manufacturers' confidence improved in most core countries but services' optimism seems to be cooling down

PMI
(level)



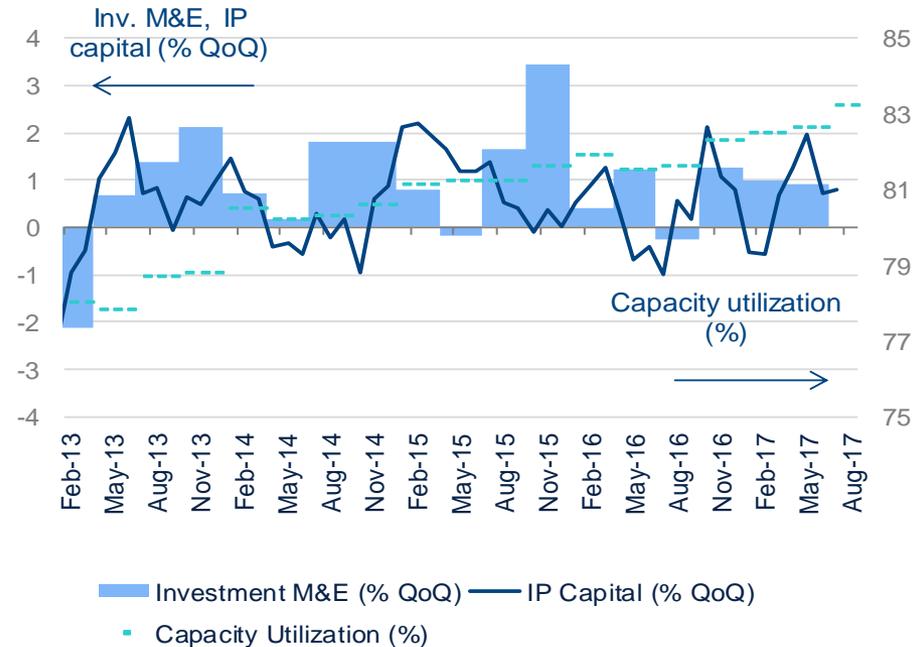
A mild growth of industrial production in July lags behind the buoyant manufacture surveys

Industrial production
(level, %QoQ)



Source: Eurostat and BBVA Research

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



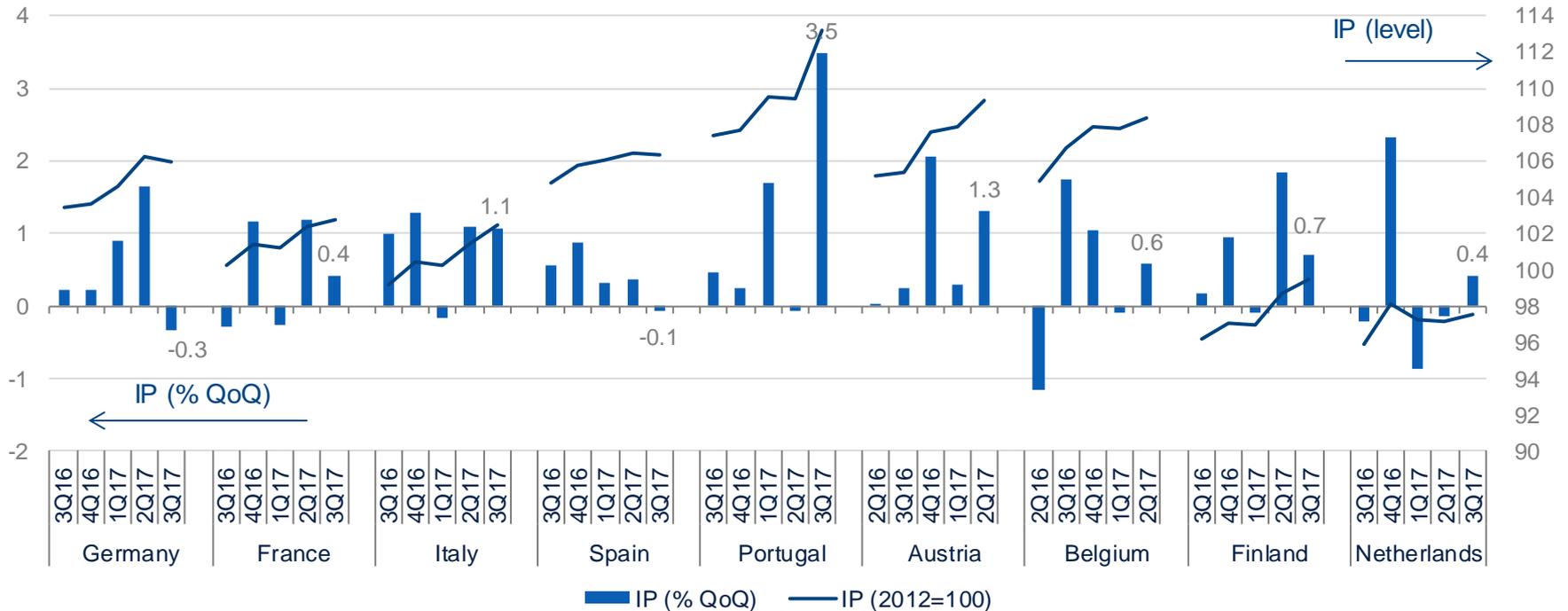
Source: Eurostat and BBVA Research

◆ Industrial production improved only marginally (+0.1% MoM) after dropping -0.6% MoM in June (+1.2% QoQ)...

◆ ...but the increase in production of durables and capital goods, together with high capacity utilization, point to a still favourable outlook in coming months

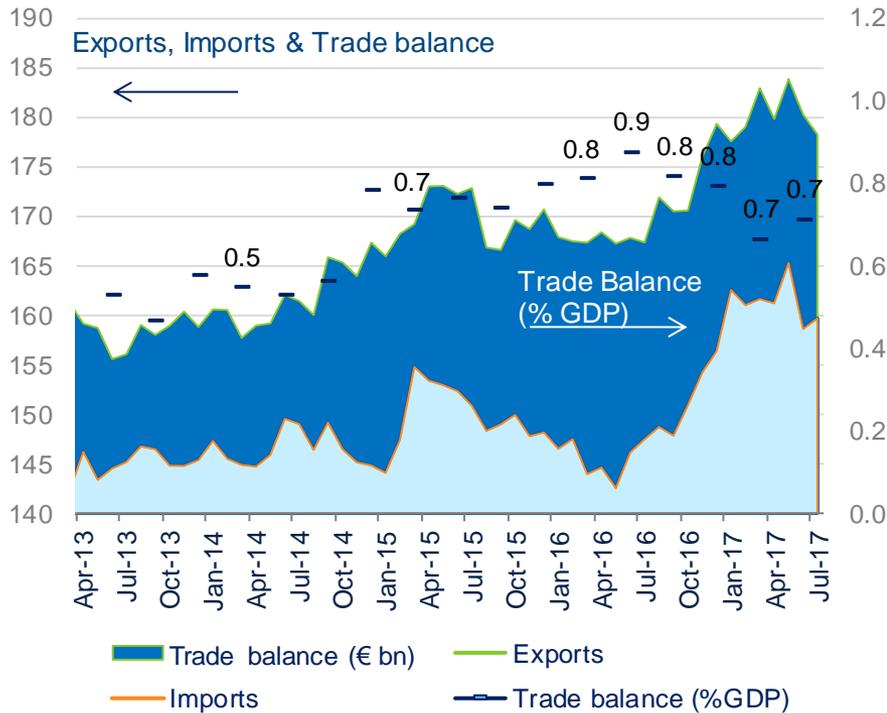
With strong gains in Portugal and Italy but losses in Germany and Spain, performance of industrial output was mixed at the start of 3Q

Industrial production
(%QoQ, level)

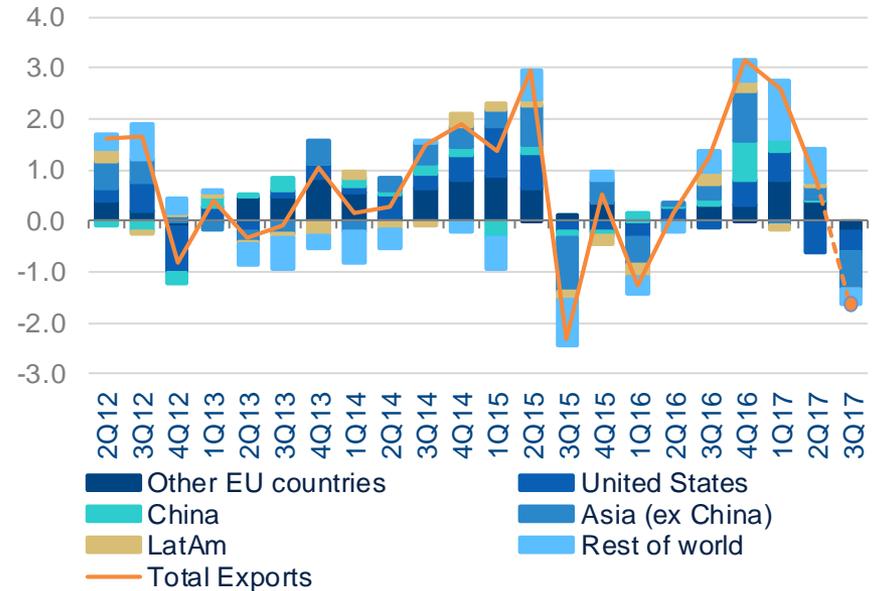


Foreign trade figures cooled down in 3Q but solid imports hides the strength in domestic demand

Trade balance
(€ bn, %GDP)

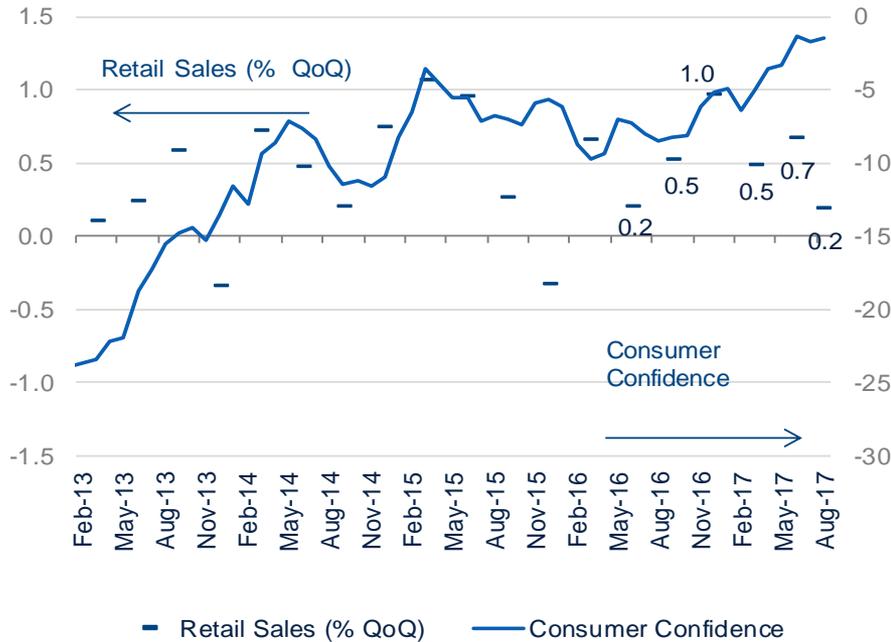


Exports contribution by destination
(%QoQ, pp)

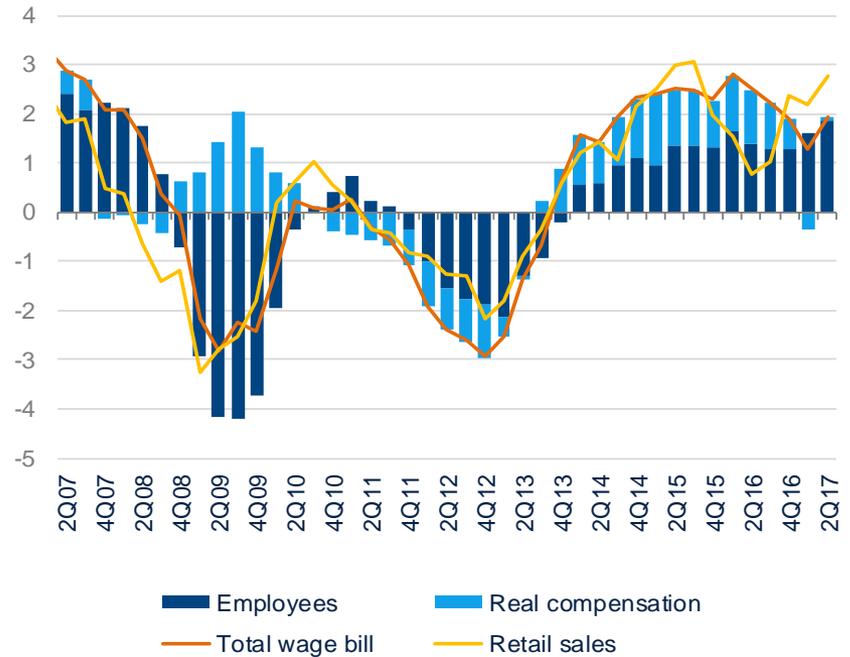


Retail sales moderated at the beginning of 3Q17 while consumer confidence remained broadly stable at high levels

Retail sales and consumer confidence
(%QoQ, pts)



Retail sales and total wage bill
(%YoY)



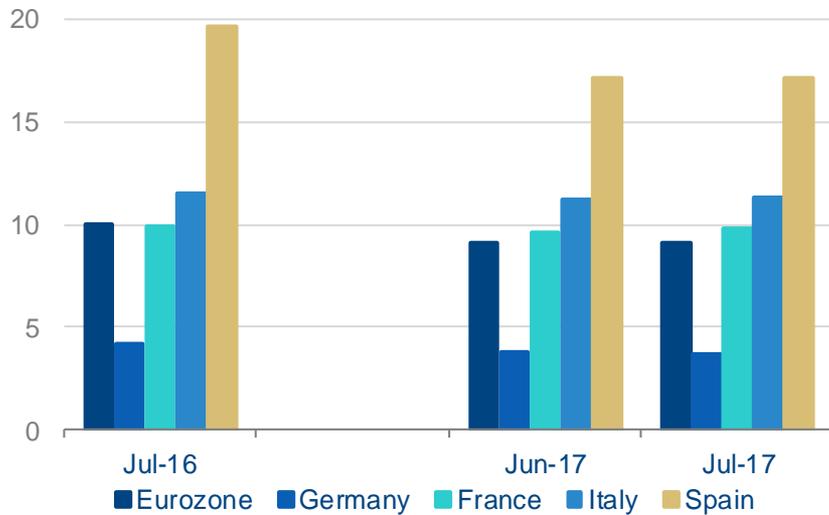
Source: Eurostat and BBVA Research

◆ Retail sales recorded their first monthly decline of the year in July (-0.3% MoM) after a strong gain in June (+0.6% MoM)

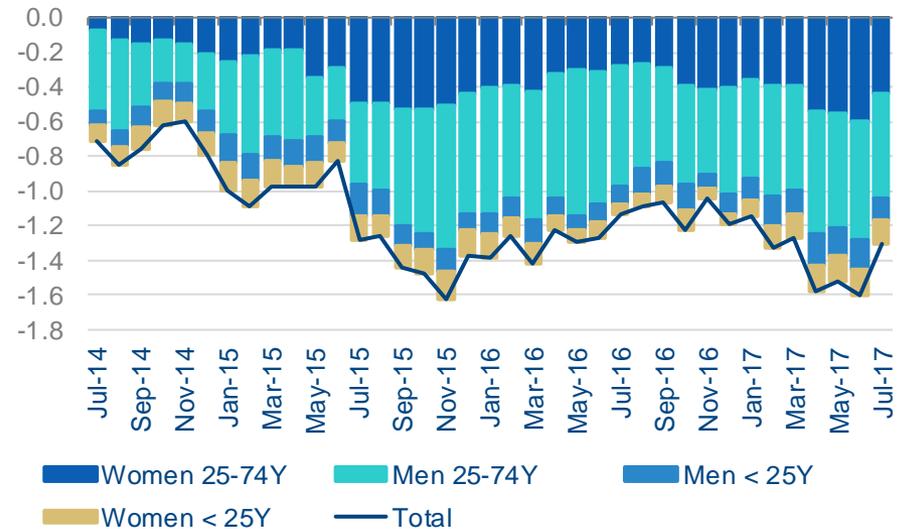
◆ Nonetheless, annual figures continue to point to consumption as a strong driver of economic recovery due to gains in employment

The unemployment rate kept steady in July at 9.1%

Unemployment rate by country (%)



Annual unemployment change by gender & age (millions)



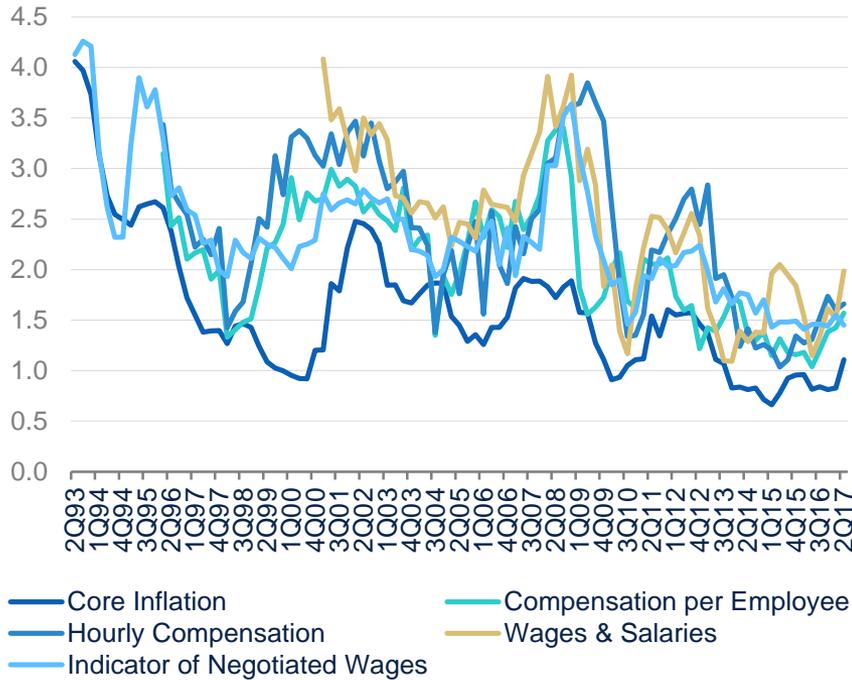
Source: Eurostat and BBVA Research

◆ **Jobless rate remained stable at 9,1% in July**, while the annual decline of 0.9pp is mostly driven by Spain and to a lesser extent by Germany

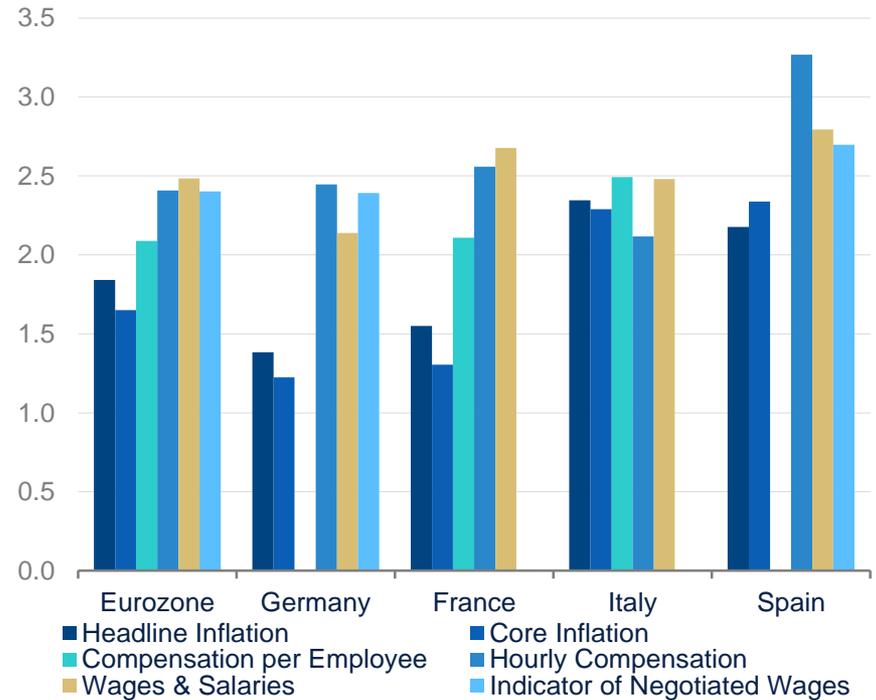
◆ **The unemployment fall is observed mostly among the experienced population**

Although increasing, annual wage growth remains subdued

Eurozone: CPI inflation and wage measures
(% YoY)



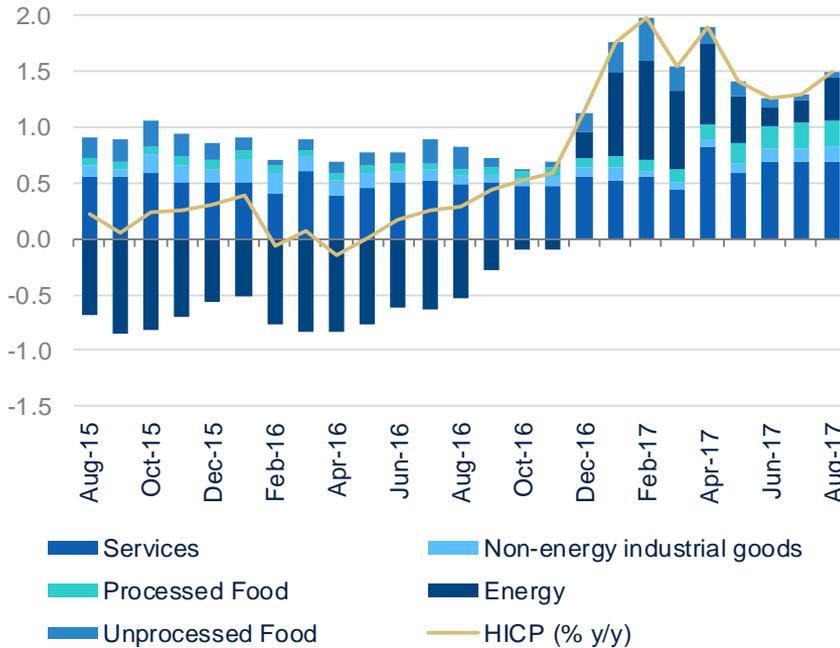
Average growth of CPI and wage measures*
(% YoY)



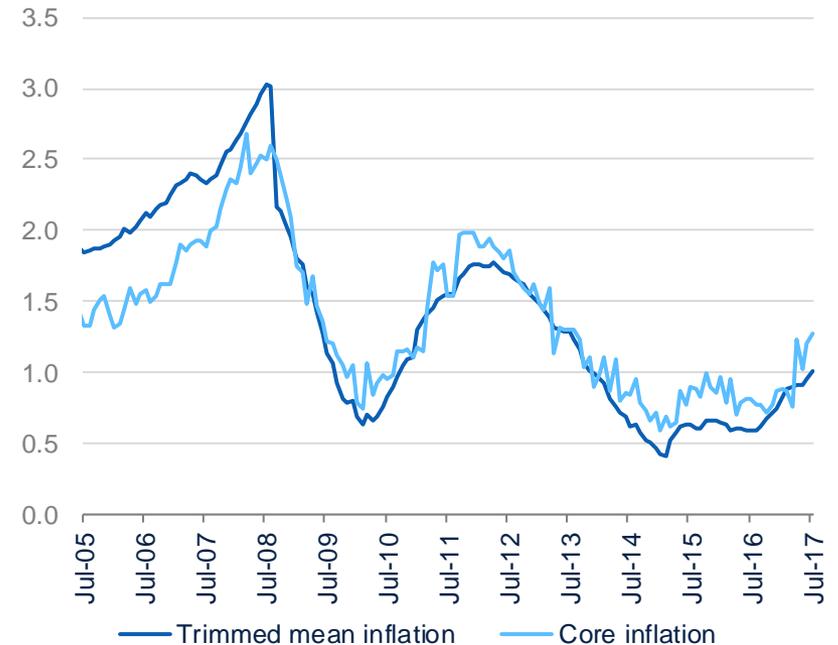
Source: Eurostat and BBVA Research
*Based on different individual samples of quarterly data

Headline inflation accelerated in August driven by energy and food

Inflation and contribution of components
(%YoY, pp)



Core and trimmed-mean inflation
(%YoY)



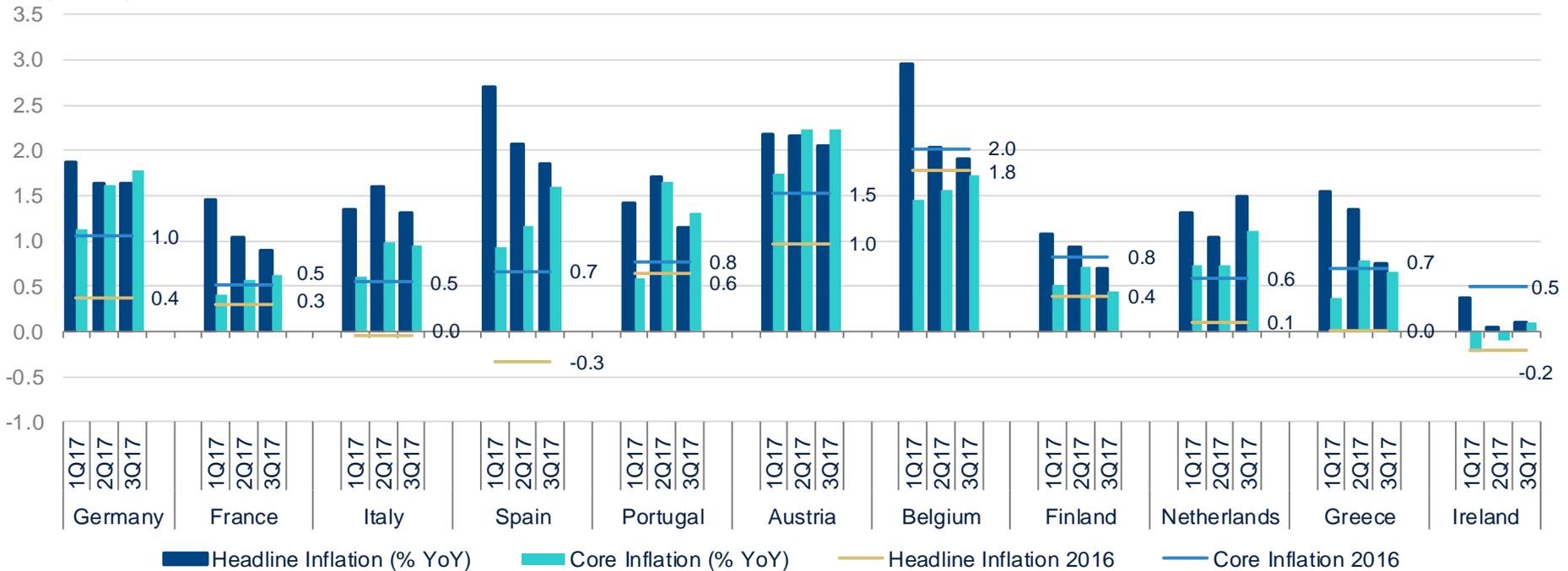
Source: Eurostat and BBVA Research

◆ Eurozone HCPI came slightly above expectations (+1.5% YoY) on higher energy inflation and stability unprocessed food prices. Core inflation remained stable at 1.3%

◆ Headline inflation is expected to moderate to around 1% in coming months due to energy prices, while core inflation should increase only very gradually

By country, inflation core measures remain subdued in 3Q despite August's pick-up in headline figures

Headline and core inflation (%YoY)



Source: Eurostat and BBVA Research

◆ August HCPI increased in all core countries: **Germany** (1.8% after 1.5% YoY), **France** (1.0% after 0.8% YoY), **Italy** (1.4% after 1.2% YoY) and **Spain** (2.0% after 1.8% YoY)

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