



BBVA Research

Eurozone Economic Watch

February 2019

Creando Oportunidades

Eurozone: Weak momentum persists in early 2019, as global headwinds weigh on export orders and industrial sector

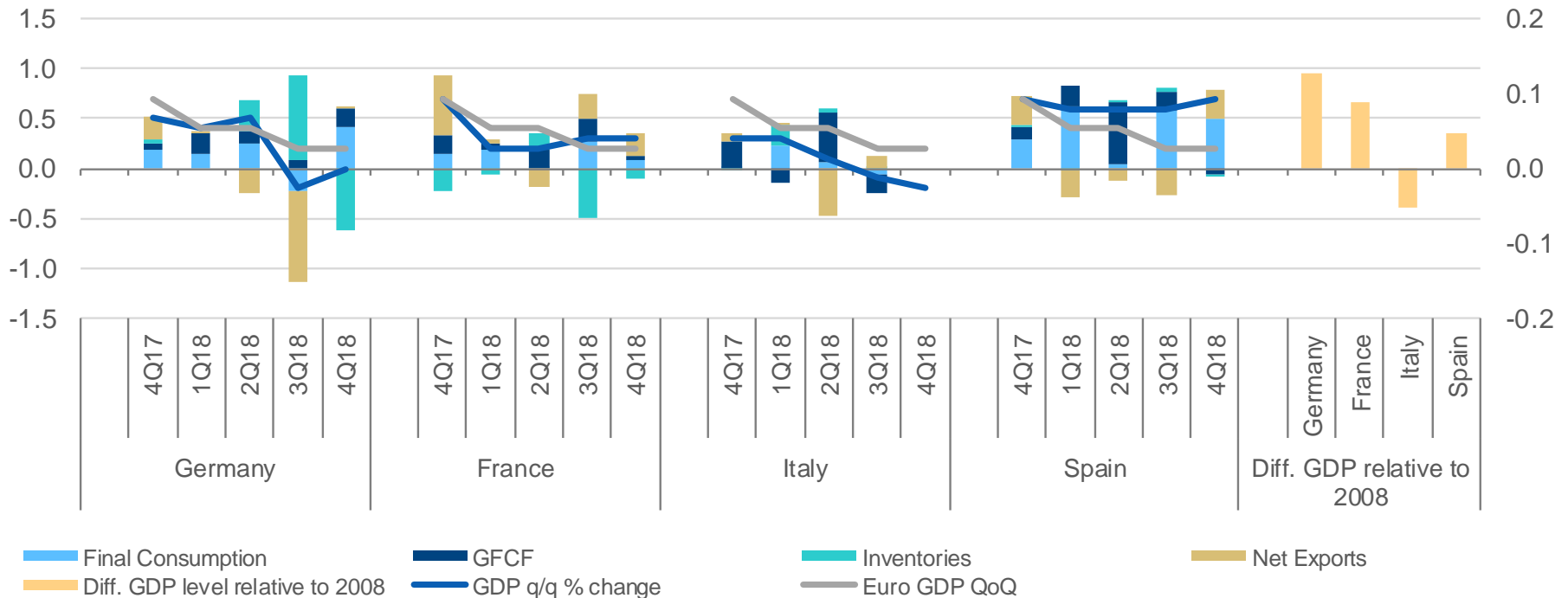
- Flash estimates reveal that Eurozone economic growth remained subdued in 4Q18. While the preliminary GDP data lacks detail, we expect slowing global demand, weakening domestic industrial activity besides problems in the automotive sector to be driving the Eurozone slowdown. Our MICA estimates that Eurozone growth for 1Q19 will maintain at around 0.2% q/q.
- Hard data up to December were mixed. Industrial production declined further, dragged by continued decline in capital goods orders, particularly related to investments. However, nominal exports consolidated their recovery while retail sales picked up.
- Composite PMIs recovered in February due to a rebound in services. However, manufacturing PMIs remained weak, slipping further into contraction levels in Germany. Slowing manufacturing activity presents an increasing risk of negative spillover effect on still resilient services sector.
- Easing oil Brent prices will shape inflation down in January, clearly below the ECB's target for 2019-20, while core inflation is likely to gradually trend upwards.
- Risks are tilted to the downside, mostly related to political events. The risk of a no-deal Brexit is higher given the close deadline. Other risks include political (government stability and euroscepticism) and policy uncertainty (deficit compliance, structural reforms), banking concerns as well as renewed threat of auto tariffs by the US. It is unlikely that the US increases tariffs suddenly but it may choose to keep the threat alive so as to obtain trade concessions from the Eurozone.

Italy slips into recession while Germany narrowly avoids it, France improves and Spain holds steady

Eurozone GDP growth in 4Q18 disappointed expectations of a rebound following a weak Q3 in wake of regulatory changes in the automotive sector

GDP and expenditure contribution by country

(%QoQ, pp)

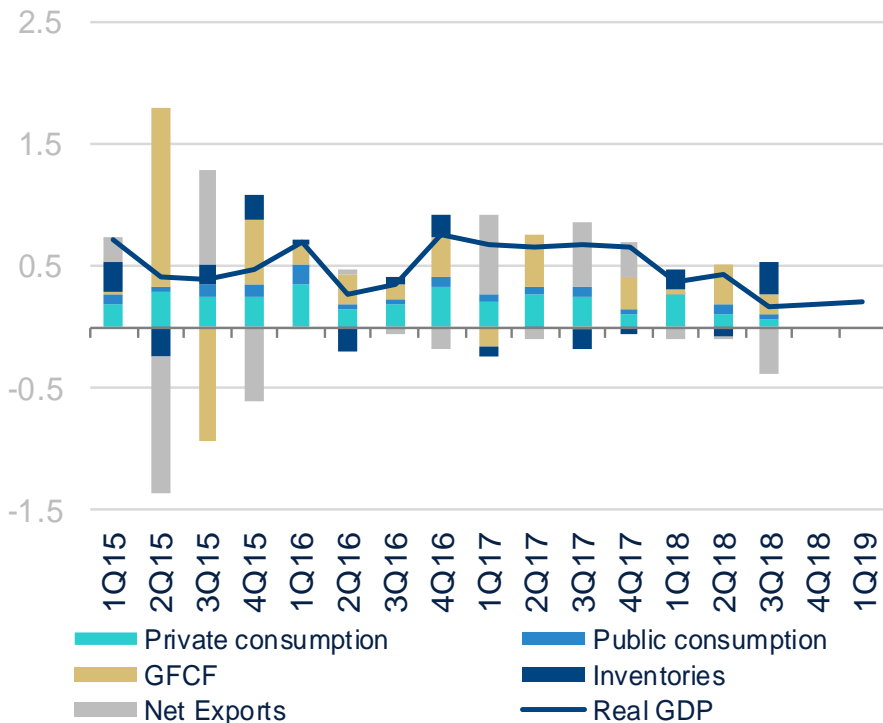


Weak momentum persists in early 2019, as global headwinds weigh on export orders and industrial sector

National figures show still strong domestic demand, but easing support from net exports. Increasing concerns on the effects of trade tensions and global slowdown. The deterioration of confidence seems to have halted, although only in services and consumers.

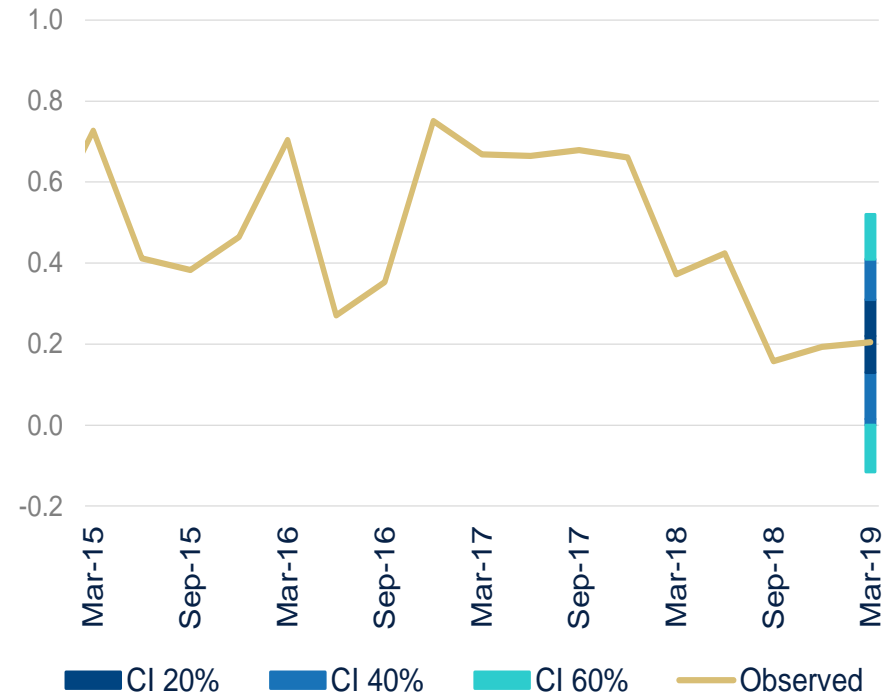
GDP, contribution by components

(%, QoQ)



GDP and MICA forecasts

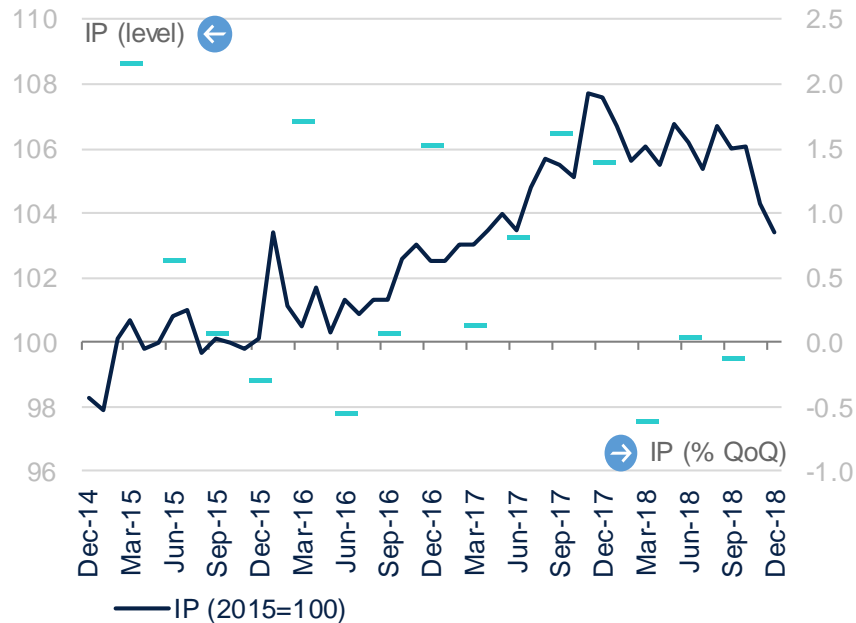
(%, QoQ)



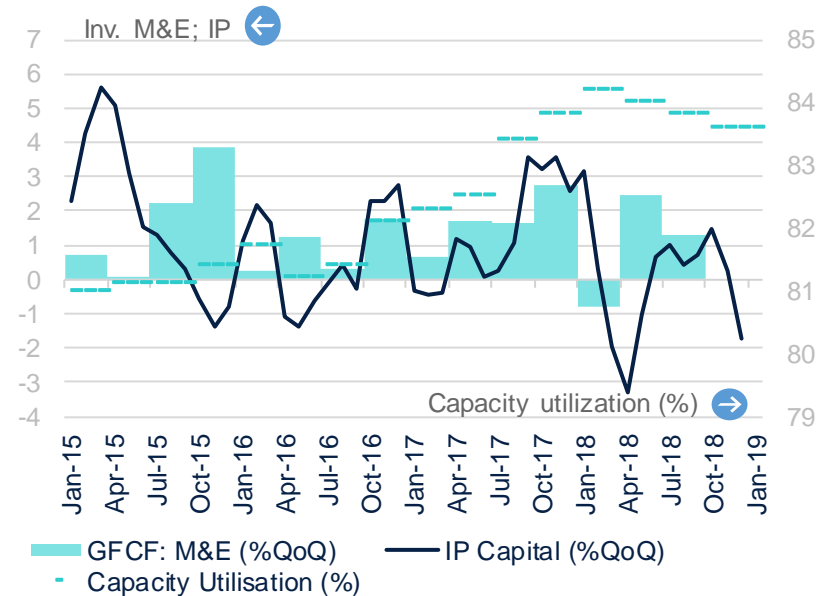
Industrial production fell in December, led by capital goods; it suggests that the investment recovery could lose steam in coming quarters

Industrial production continues its decline although it seems to have moderated. However, the continued fall in capital goods does not seem to augur well for new investments in the sector.

Industrial production (Level, % QoQ)



IP capital equipment, investment in M&E and capacity utilization (%QoQ; %)

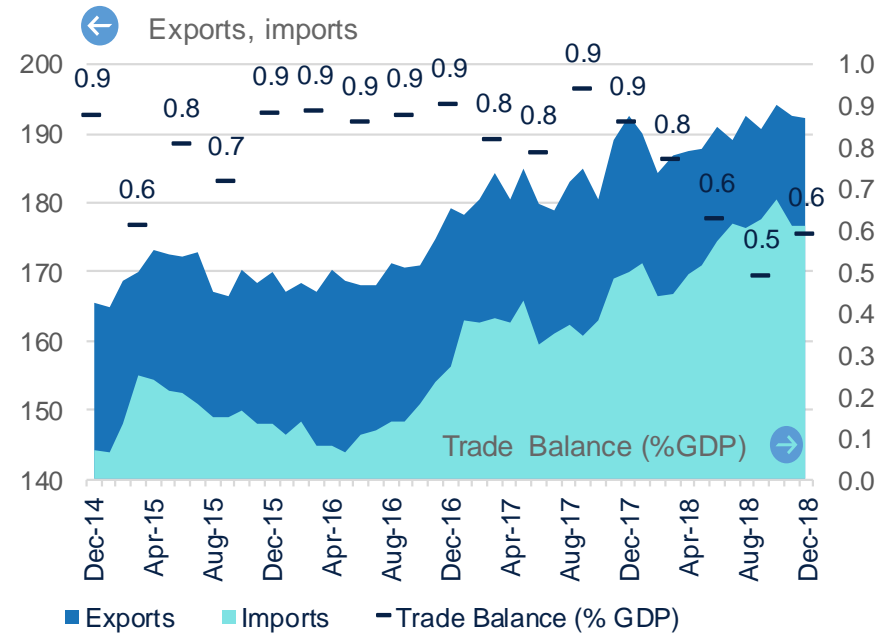


Export growth consolidated towards year end after a weak start

Export growth consolidated towards the end of 2018 after a weak start, supported by higher demand from within the EU as well as the US.

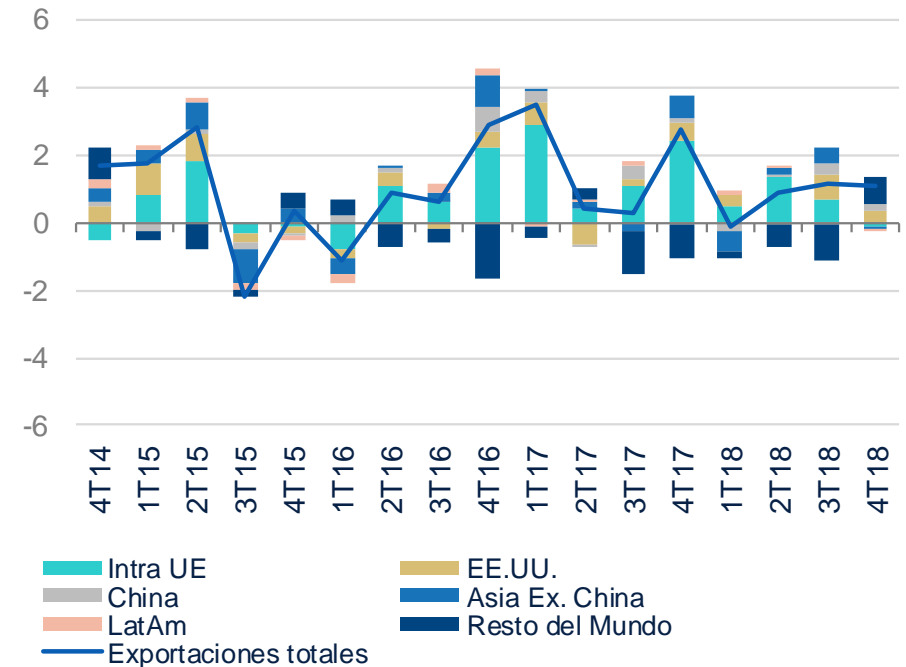
Trade balance

(€bn; %GDP)



Exports by destination

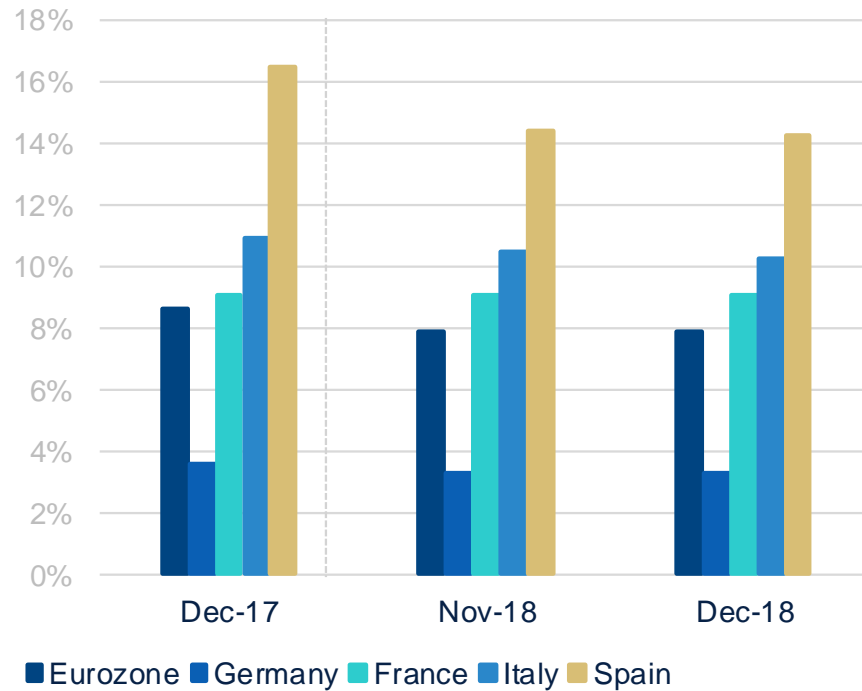
(%YoY; pp)



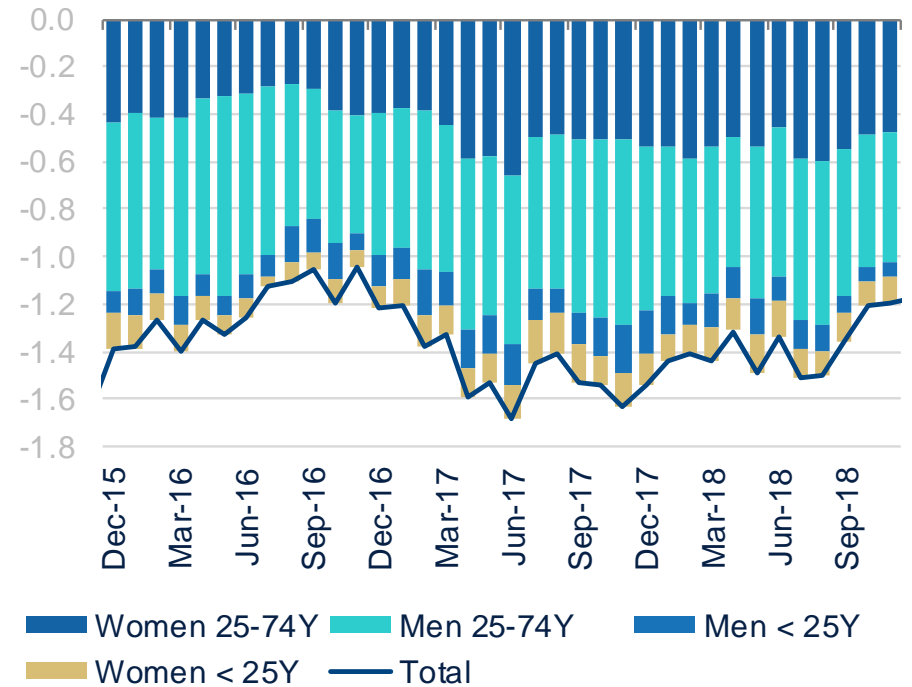
The unemployment rate remained broadly unchanged in December

Despite significant differences across countries, the tightening of the labour market could put some upward pressure on wages in coming quarters.

Unemployment rate by country (%)



Annual unemployment change by gender and age (Million)

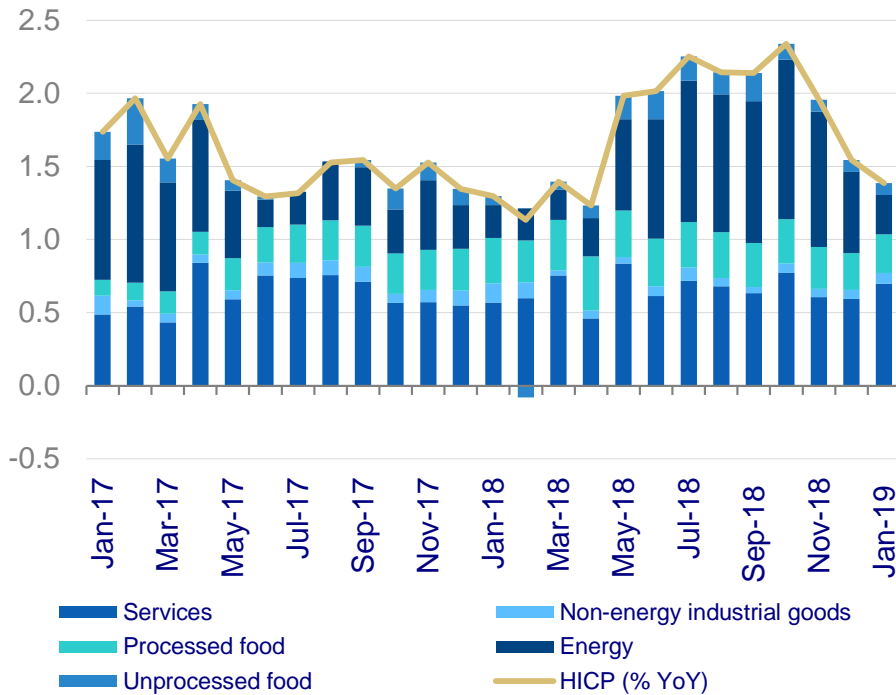


Slowing headline inflation driven by soft oil prices and steady core inflation at low levels

Brent oil prices will tilt inflation down in coming months, to levels clearly below the ECB’s target, while core inflation is likely to trend upwards very gradually.

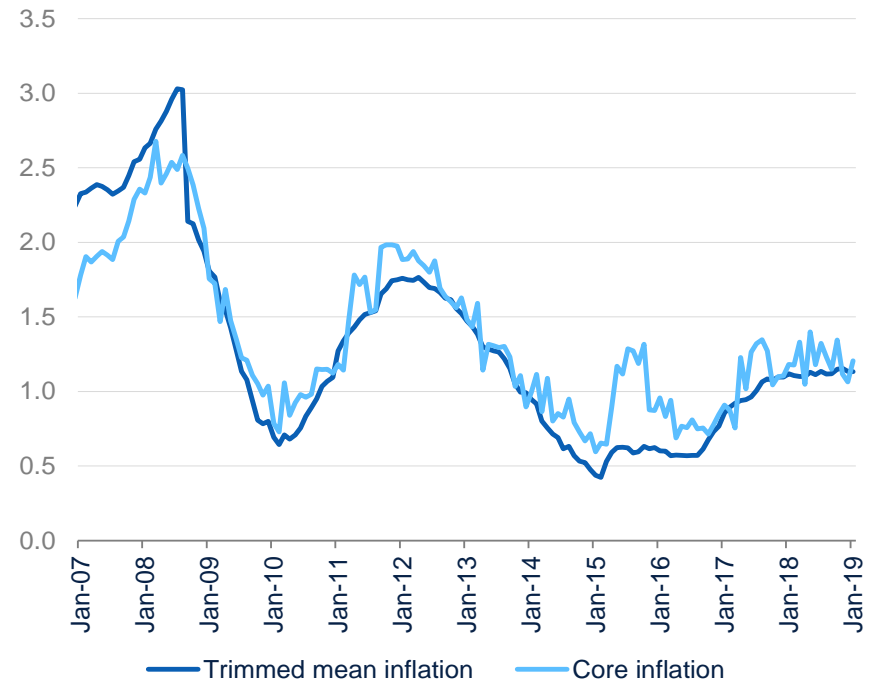
Inflation contribution of components

(%YoY, pp)



Core and trimmed-mean inflation

(%YoY; pp)

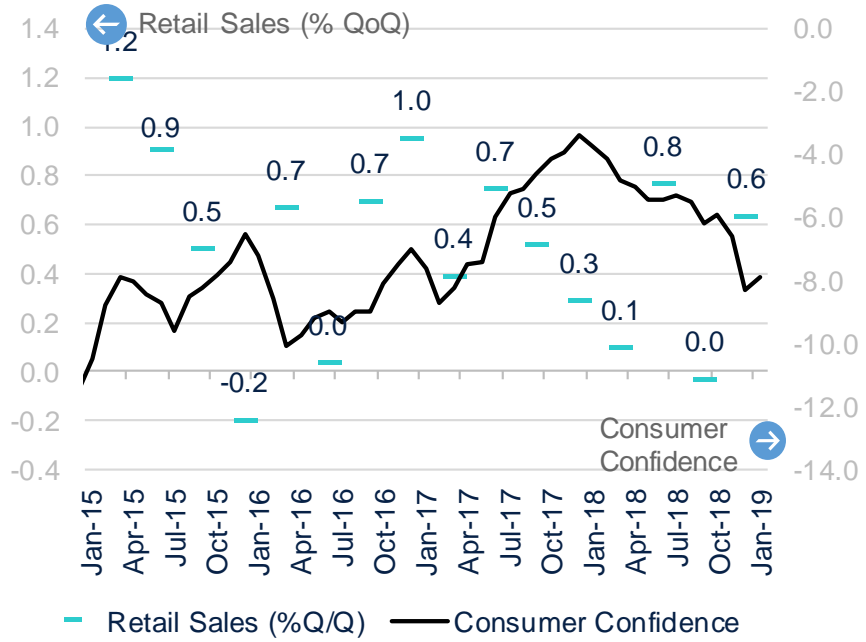


Retail sales slowed in December, led by waning Black Friday effect

Moderating retail sales growth in December partly reflected the waning Black Friday effect. However, a recovery in January consumer confidence bodes well for retail sales growth in early 2019.

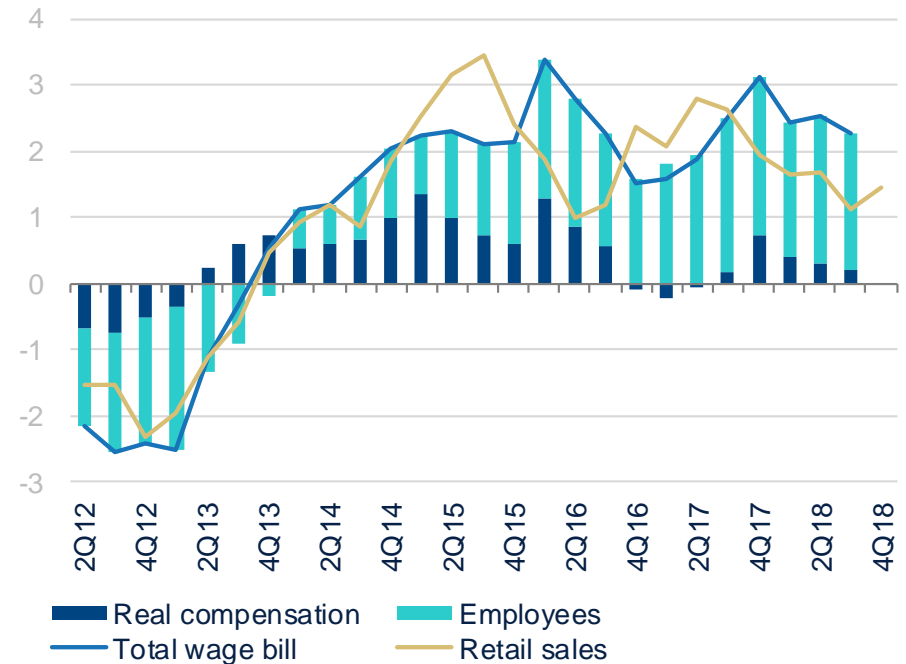
Retail sales and consumer confidence

(%QoQ, level)



Retail sales and total wage bill

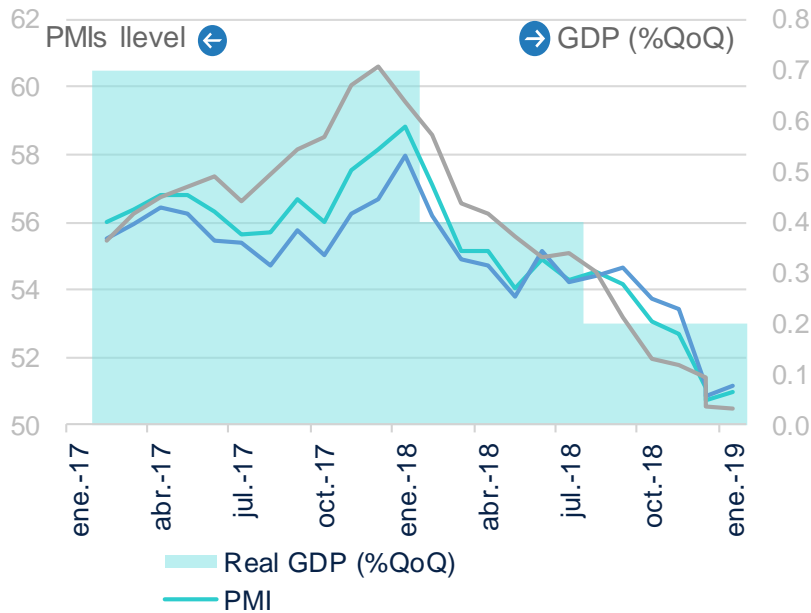
(%YoY; pp)



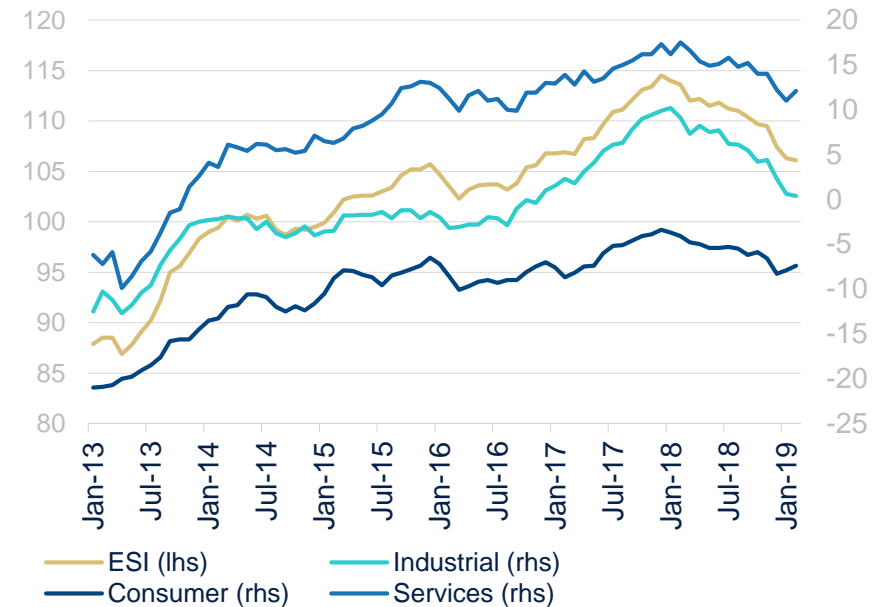
Resilient services sector is underpinning economic sentiment, in turn offsetting continued weakness in manufacturing activity

ESI and PMI tell a similar message: a divergence between weak manufacturing and resilient services. GDP during 1Q19 may improve, but is unlikely to return to previous rates.

PMI and GDP
(level, %QoQ)



EC confidence survey
(level)

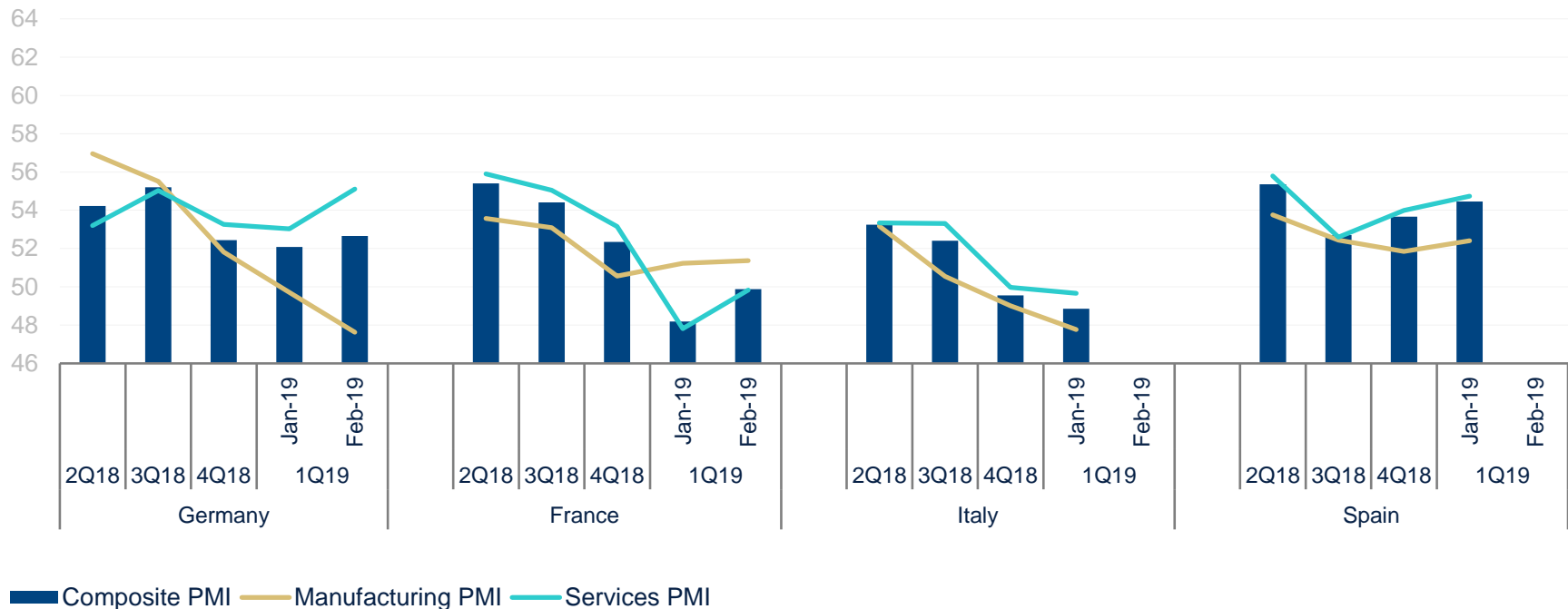


Uptick in February Eurozone composite PMIs was led by services sector, which offset extended weakness in manufacturing activity

Latest PMIs are consistent with a Q1 GDP growth rate about 0.1% QoQ in the Eurozone and 0.2% in Germany. For France, Q1 GDP growth seems to be set to stagnate or even contract slightly amid weak demand, as reflected by a decline in new orders for two straight months.

PMI Survey

(level)



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