

# Economic Watch

## Europe

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Economic Analysis

Europe Unit

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## Signs of recovery in the second quarter

### But the carry-over effect of 1Q13 poses a downward bias to our forecast for 2013

- **GDP fell by -0.2% q/q in 1Q13, below our expectations<sup>1</sup>**

The detailed National Accounts breakdown confirmed that the eurozone GDP fell by -0.2% q/q in 1Q13 after -0.6% q/q in 4Q12, pulled down by the drop in exports (-0.8% q/q) that resulted in a flat net exports contribution to quarterly GDP growth thanks to a larger fall in imports (-1.1% q/q). Positive news stemmed from the slight increase in private consumption (0.1% q/q after -0.6% in 4Q12), although it remained subdued, and together with falling external support resulted in a strong fall in investment (-1.6% q/q). Ongoing fiscal consolidation in most member states was reflected in a further fall in public consumption (-0.1% q/q). All this resulted in a lower negative contribution of domestic demand (-0.2pp after -0.7pp in 4Q12).

- **PMIs improve in May for the second month in a row, compensating the drop registered in February and March<sup>2</sup>**

Soft indicators in April and May were together somewhat better than expected, with PMIs partly offsetting the setback in March and April. All the countries covered by the survey by Markit registered in May weaker rates of contraction than in previous months, especially in Spain, Greece and France.

Additionally, Germany returned to the "growth" area, as the Composite PMI hits a 50.2 level after the brief dip observed in April. This improvement is mainly due to the better outturn of the manufacturing sector, as the manufacturing PMI rebounded after a two-months-fall owing to a slight increase in production and new orders.

In France, manufacturing PMI's suggest that the drop in industrial activity is moderating, thanks to the lower rate of contraction of production and new industrial orders. Also the downturn in services softens, though the sector remains subdued.

- **The most recent hard data point to a mild economic growth in 2Q13**

Hard indicators are only available for April, but they suggest that business activity is already recovering in 2Q13. Industrial production<sup>3</sup> increased in April for the third month in a row, to a level which is 1% above the average for 1Q13, while export orders suggest that external demand will continue to support the sectoral recovery. Less optimistic news stemmed from the domestic side, as retail sales dropped slightly again in April, and combined with low consumer confidence as well as increasing unemployment suggest that private consumption should remain very subdued in the second quarter.

1: See [http://www.bbva.com/research/KETD/fbin/mult/130605\\_Europe\\_Flash\\_GDP\\_1Q13\\_tcm348-390671.pdf?ts=1462013](http://www.bbva.com/research/KETD/fbin/mult/130605_Europe_Flash_GDP_1Q13_tcm348-390671.pdf?ts=1462013)

2: See [http://www.bbva.com/research/KETD/fbin/mult/130605\\_Europe\\_Flash\\_Europa-PMI\\_ENG\\_tcm348-390678.pdf?ts=1462013](http://www.bbva.com/research/KETD/fbin/mult/130605_Europe_Flash_Europa-PMI_ENG_tcm348-390678.pdf?ts=1462013)

3: See [http://www.bbva.com/research/KETD/fbin/mult/130613\\_Europe\\_Flash\\_tcm348-391452.pdf?ts=1462013](http://www.bbva.com/research/KETD/fbin/mult/130613_Europe_Flash_tcm348-391452.pdf?ts=1462013)

Germany's exports increased in April (8.4% y/y) after two consecutive months of negative figures (-4.2% y/y and -2.8% y/y in March and February, respectively). This increase is mainly due to exports to non-European countries, while those to European countries have also recovered in April for the first time in two months. We also see positive exports performance in France too, as they rebounded in April (9.3% y/y after -4.8% y/y and -4.6% y/y in the previous two months), though in this case the gain is mainly due to more exports to other European countries.

Summing up, the positive surprise in both soft data in May and hard data in April is reflected in a slightly higher forecast of our model (MICA-BBVA) for eurozone GDP growth in 2Q13, which is now +0.2% instead of the 0.1% q/q that we incorporated in our macroeconomic scenario.

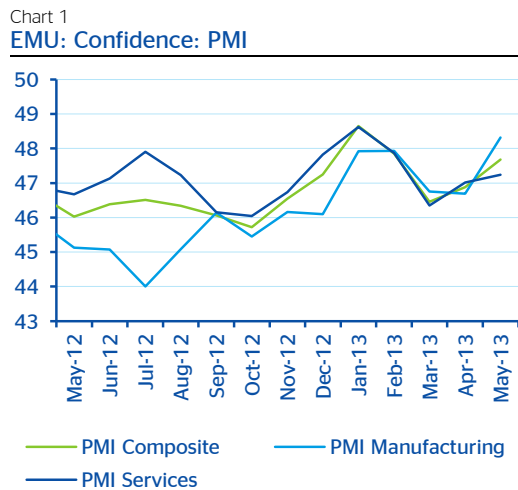
- **Downward bias in our GDP growth forecast for the whole 2013 due to the negative carry-over effect of Q1**

Despite these positive surprises, the carry-over effect of the stronger than expected GDP fall in 1Q13 suggests that the eurozone economy could contract by -0.3% or -0.4%, below our previous forecast for 2013 (-0.1%).

- **Inflation is likely to increase slightly in June, but slowing again as from August**

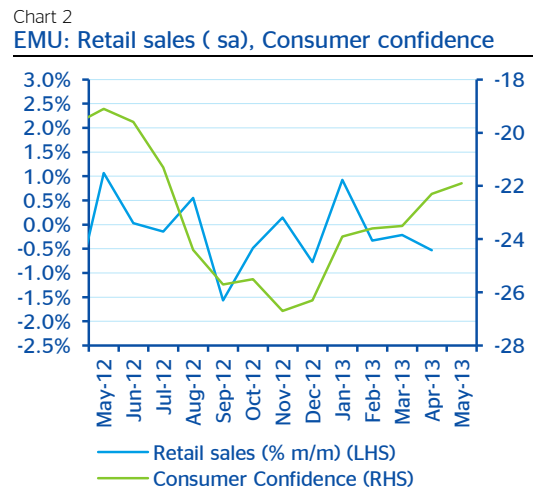
Regarding prices, headline inflation increased by 0.2pp to 1.4% y/y in May, as expected, mainly driven by higher inflation in services, while the fall in energy prices eased. Looking forward, after another increase in inflation in June due to higher energy prices, we expect inflation to slow again especially from August to hover around 1.3% in 2H13.

**Confidence rebounds in May**



Source: Markit Economics

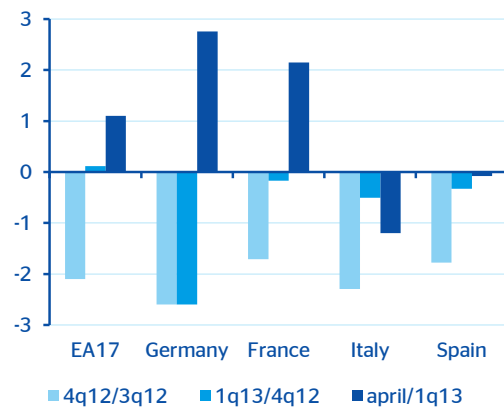
**Indicators for private consumption improve but are still subdued**



Source: European Commission and Eurostat

**Industrial Production rebounded in April more than expected, especially in Germany and France**

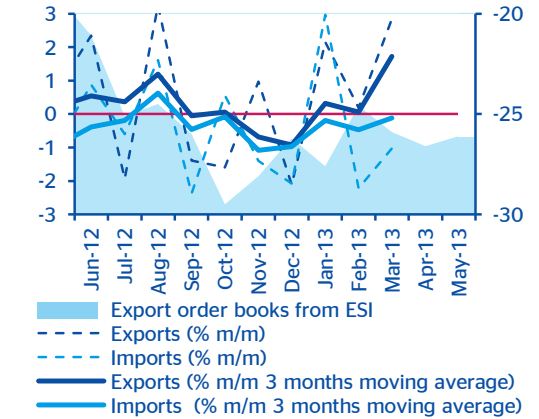
Chart 3  
EMU:IPI exc. Construction



Source: Eurostat

**Exports rebound in March and imports continue falling**

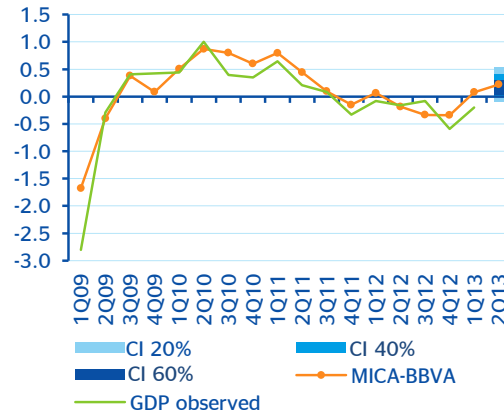
Chart 4  
EMU: External sector



Source: European Commission and Eurostat

**Our MICA model suggests growth already in Q2**

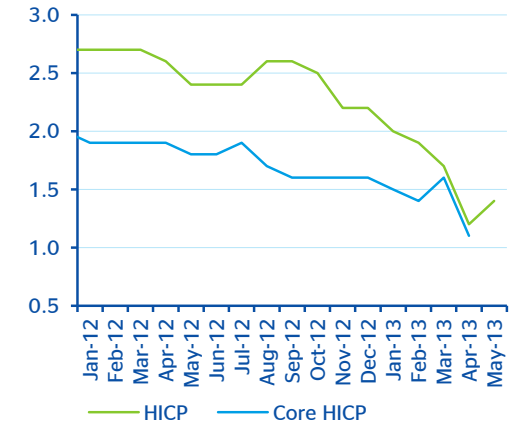
Chart 5  
EMU: MICA-BBVA



Source: BBVA Research

**Inflation increased in May driven by higher services prices**

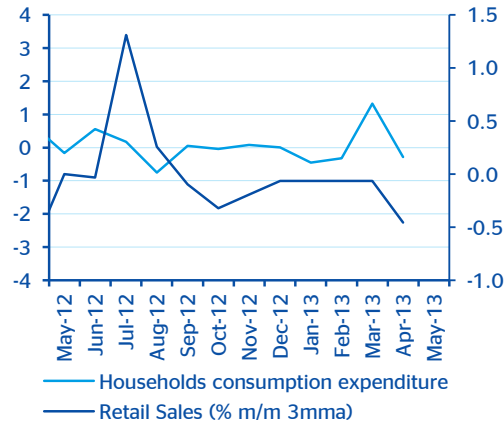
Chart 6  
EMU: HICP y/y %



Source: Eurostat

**French consumption indicators remain weak**

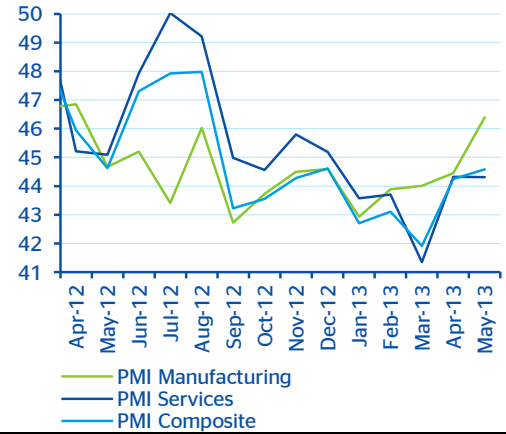
Chart 7  
France: Retail sales & HH Consumption Expenditure



Source: INSEE and Eurostat

**French confidence recovers over the last two month from very low levels**

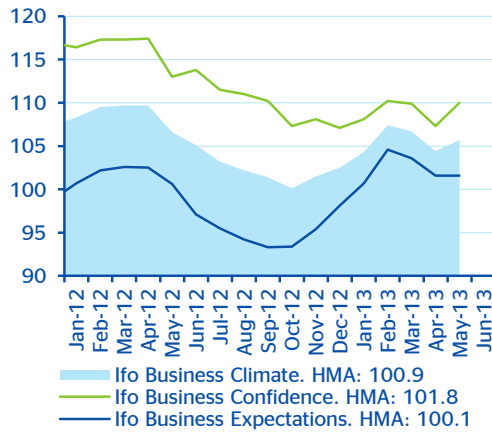
Chart 8  
France: PMIs



Source: Markit economics

**German IFO index remains relatively strong**

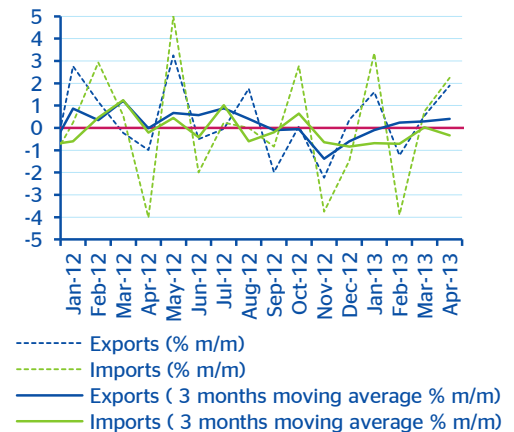
Chart 9  
Germany: Ifo Business Climate Index



Source: Ifo-Institut für Wirtschaftsforschung

**German exports improve in March and April, in a month over month basis**

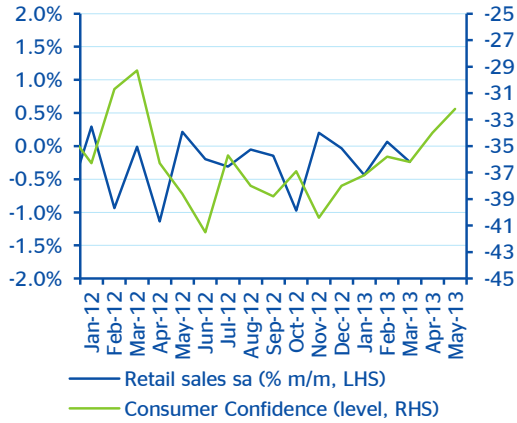
Chart 10  
Germany: External sector, sa



Source: Haver Analytics

**Italian private consumption remains subdued despite the slight improvement in consumer confidence**

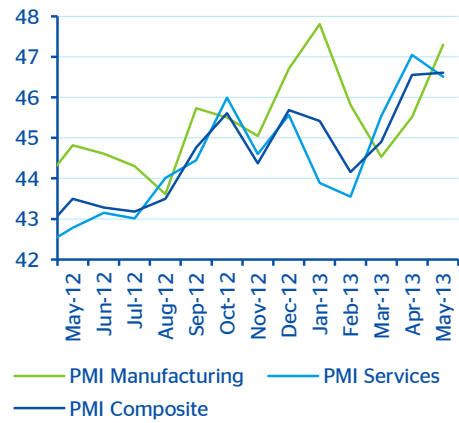
Chart 11  
Italy: Retail sales and Consumer confidence



Source: Eurostat and European Commission

**Italy soft data points to a moderation of the recession in 2Q13**

Chart 12  
Italy: PMIs



Source: Markit economics

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