

Euro Area Macro Monitor

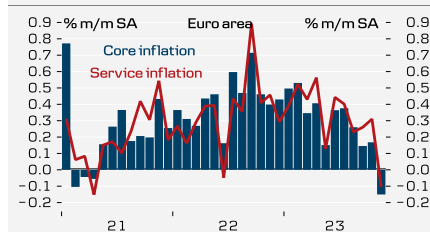
Did Christmas come early for the ECB?

- Closely approaching year-end, economic activity in the euro area is stagnating after a strong recovery in 2021 and 2022 after the pandemic.** Real GDP contracted in Q3, indicating that the yearly growth rate is close to 0%, reflecting how the ECB's restrictive monetary policy is working its way through the economy. Similarly, November PMIs remained in contractionary territory, although sparking some hopes as they increased in November. Manufacturing PMI ticked up to 44.2 from 43.1, while the service PMI followed track climbing up to 48.2 from 47.8. **The upbeat print supports our base case of activity bottoming out now, while we expect growth to gradually turn north following rising real income lower inflation.** Yet, the outlook is more uncertain than usual, and the downside risks include a more rapid transmission of monetary policy, larger than expected energy price increases and geopolitical tensions
- The November inflation print came in far below expectations, and on the surface, it seems like Christmas came early for the ECB with a broad-based decline in inflation.** Headline inflation fell to 2.4% y/y compared to consensus of 2.7% y/y while declining 0.5% m/m. Core inflation ticked down to 3.6% y/y from 4.2% y/y in October. Remarkably, the monthly change in core inflation was negative at -0.15% seasonally adjusted, driven by both negative goods and service price inflation. **Yet, we remain cautious and try not to be carried away by one good print.** We still need to see more months with low inflation momentum to rule out statistical errors and get a clearer picture. The labor market is historically strong, and companies are reporting labor shortages amid strong wage growth. Thus, we continue to expect a gradual decline in inflation, which we expect to stay above the 2% target next year.
- Negotiated wages have trended upward since 2022 and increased by 4.7% y/y in Q3 2023 up from 4.6% in the previous quarter. **With inflation falling this implies a continued recovery in household's purchasing power.** We expect wage pressure to peak in the coming months, albeit remaining well above thresholds considered consistent with the inflation target in the coming years. This reflects a catch-up in lost purchasing power and not a wage-price-spiral. The strong wage growth stems from a remarkably robust labor market. **The unemployment rate was historically low in October at 6.5%**, and employment gains have been strong despite restrictive monetary policy. Business surveys suggest that hiring has only recently stalled amid slowing activity as companies continue to report labor shortages both in the service sector and the industry. **Looking forward, we expect a mild increase in the unemployment rate due to lagged effects of monetary policy and weak growth.**
- The EU's fiscal rules, prohibiting public budget deficits above 3% of GDP and debt-to-GDP above 60% have been suspended since the pandemic's start in 2020.** Recently, politicians have been negotiating a new set of rules, but with no agreement in sight, the clock is ticking as the old rules will be reinstated from 1 January 2024. We expect no final rule set by year-end. **Instead, member states are likely to establish a "landing zone" for the new rules at the ECOFIN meeting on December 8, allowing the Commission to direct fiscal rules aligned with this new agreement.** This deal will likely contain the old numerical targets but allow for more leeway in terms of country specific fiscal adjustment paths. For more details, see *Euro Area Research: New fiscal rules in the EU - aligning theory and practice?*, 29 November.

Key points

- The month-on-month change in core inflation shows encouraging signs.
- GDP data supports our call for a minor contraction in the European economy for H2 2023.
- ECB is done hiking and we expect cuts only in the summer 2024.

Negative core inflation, also driven by negative service price inflation



Source: ECB, Macrobond Financial, Danske Bank

The wage pressure has been strong since 2022



Source: ECB, Macrobond Financial, Danske Bank

Assistant Analyst

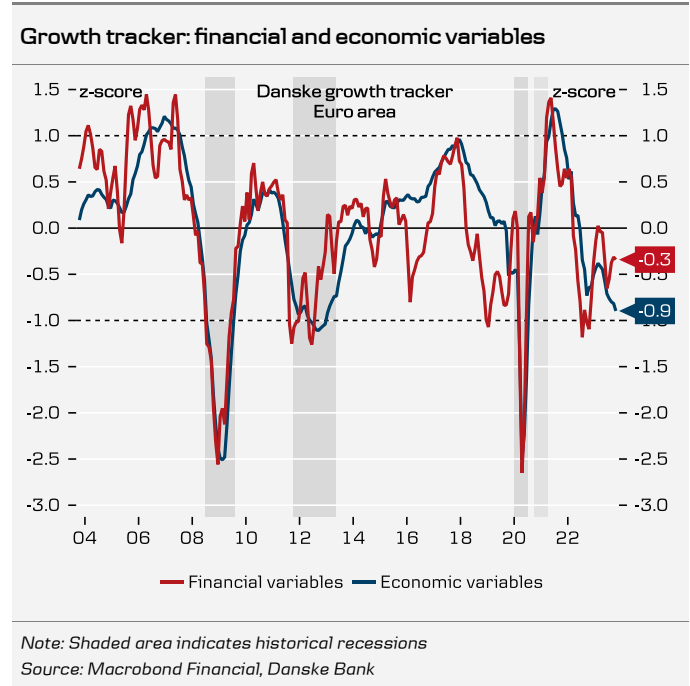
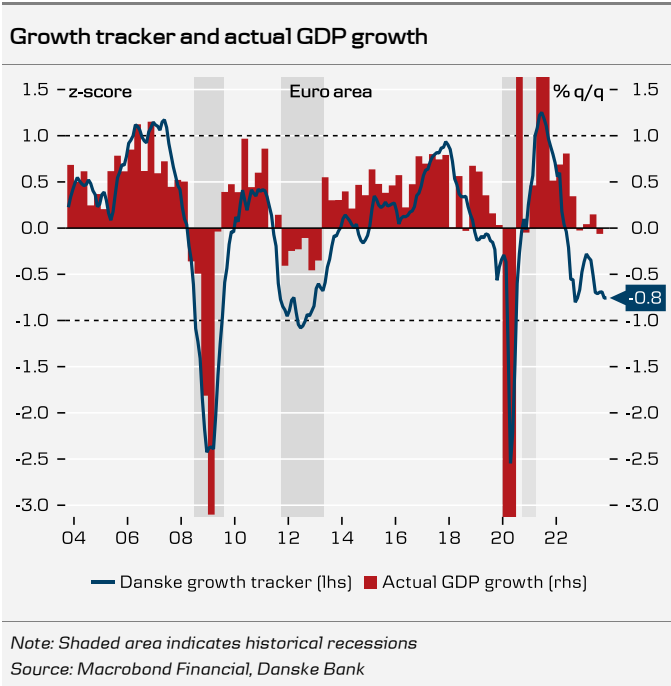
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The Danske euro area growth tracker

Our growth tracker remains in negative territory at -0.8 close to recessionary territory (-1.0 or below). Economic variables declined to -0.9 while the more volatile financial variables show more positive signals. Hence, economic variables almost signal a recession now in line with the negative GDP figures and weak PMIs. Financial variables have moved up due to the recent downside surprises in inflation recently and lower interest rate expectations. To predict the near-term growth we put more emphasis on the economic variables and still expect weak activity.



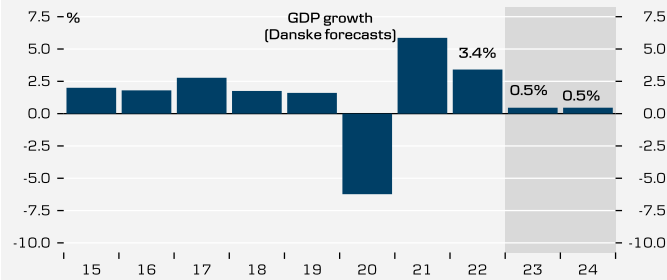
Danske growth tracker decomposition

	November 2023
Economic variables	-0,9
Unemployment	0,1
Profit growth	0,0
Capacity utilisation	-0,3
OECD CLI	-0,3
European sentiment indicator	-0,6
Consumer confidence	-0,8
ZEW	-0,9
Credit growth	-0,9
Composite PMI	-1,0
PMI order-inventory balance	-1,4
EuroCOIN	-1,8
Real M1 growth	-3,0
Financial variables	-0,3
Eurostoxx50	0,4
Corporate vs. gov. bond yield	-0,1
Euro surprise index	-0,5
Sentix	-1,1

Source: Macrobond Financial, Danske Bank

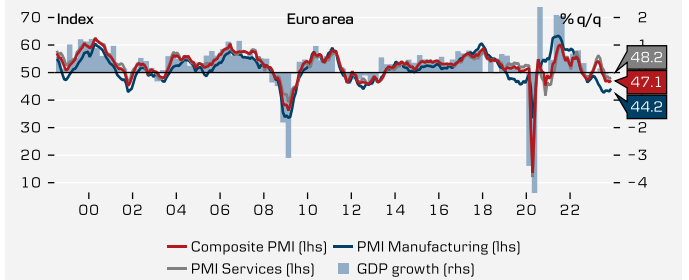
Euro area

GDP growth forecasts



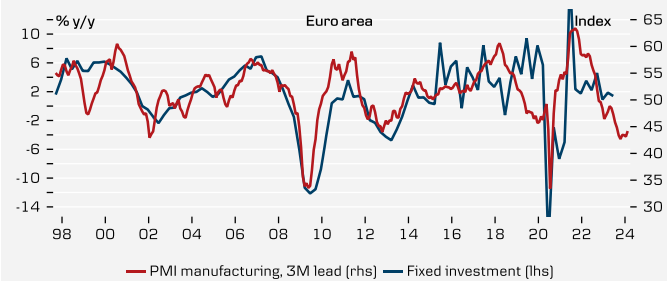
Source: Macrobond Financial, Danske Bank forecasts

PMI and GDP growth



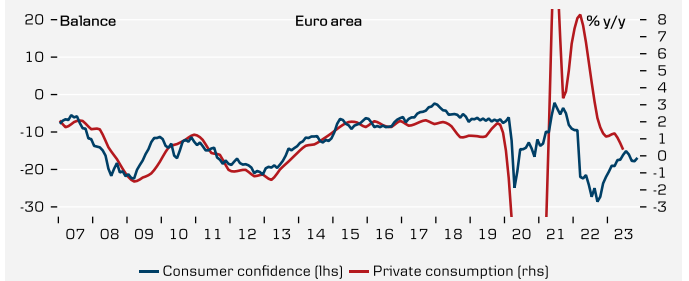
Source: Macrobond Financial, Danske Bank

Manufacturing sentiment and investments



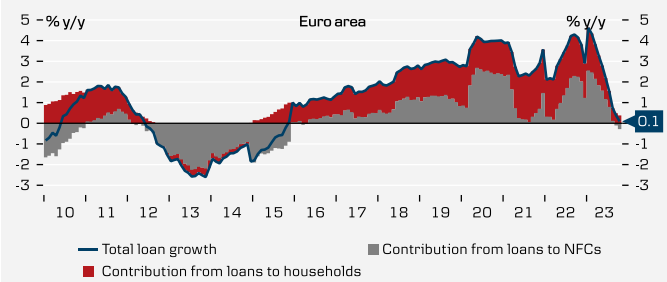
Source: Macrobond Financial, Danske Bank

Consumer confidence and private consumption



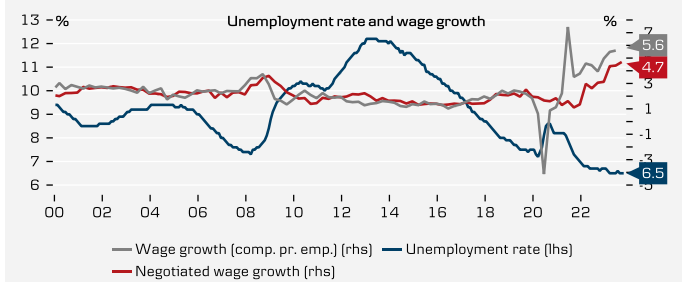
Source: Macrobond Financial, Danske Bank

Credit growth



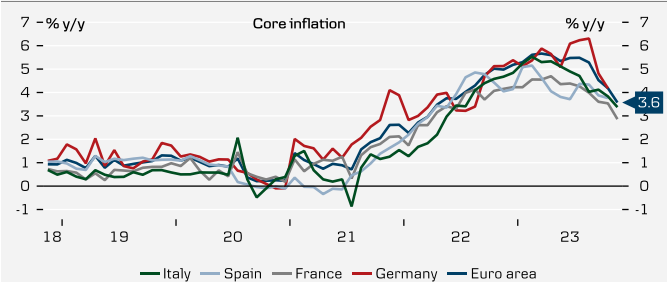
Source: Macrobond Financial, Danske Bank

Unemployment and wage growth



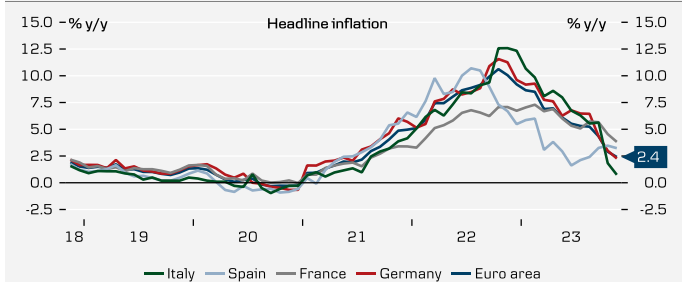
Source: Macrobond Financial, Danske Bank

Core inflation



Source: Macrobond Financial, Danske Bank

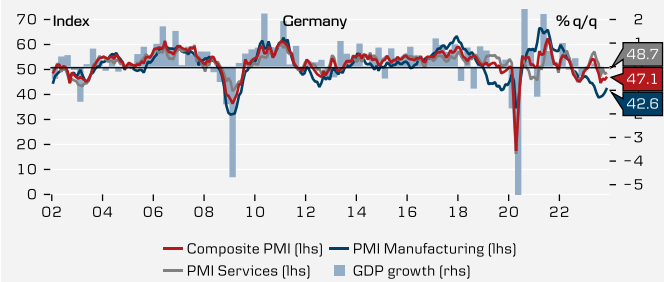
HICP inflation



Source: Macrobond Financial, Danske Bank

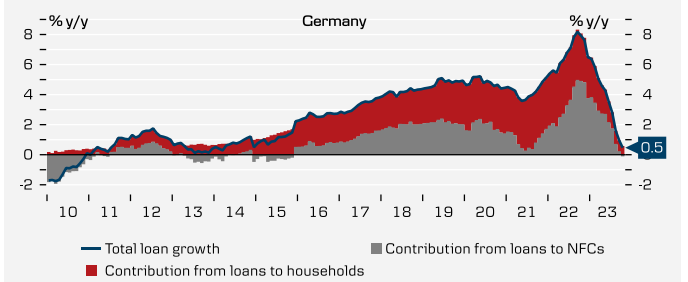
Germany

PMI and GDP growth



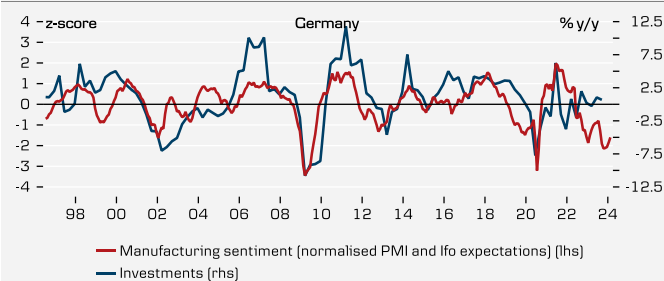
Source: Macrobond Financial, Danske Bank

Credit growth



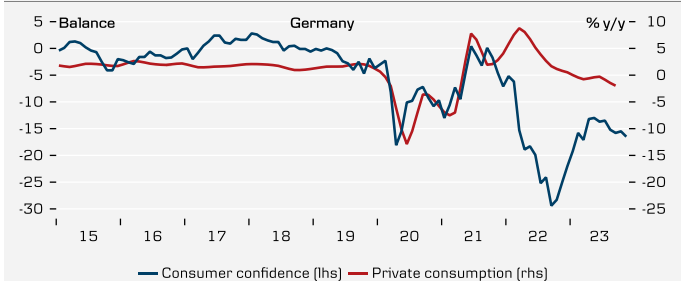
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Manufacturing sentiment and investments



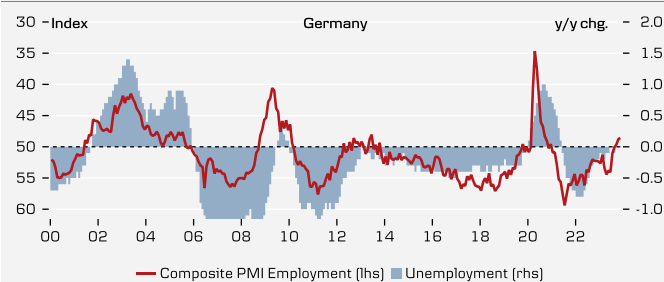
Source: Macrobond Financial, Danske Bank

Consumer confidence and private consumption



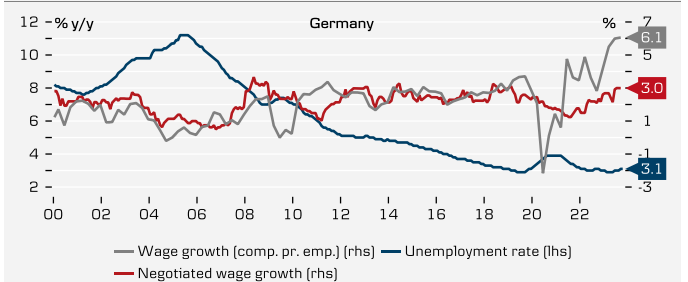
Source: Macrobond Financial, Danske Bank

Unemployment and PMI



Source: Macrobond Financial, Danske Bank

Unemployment and wage growth



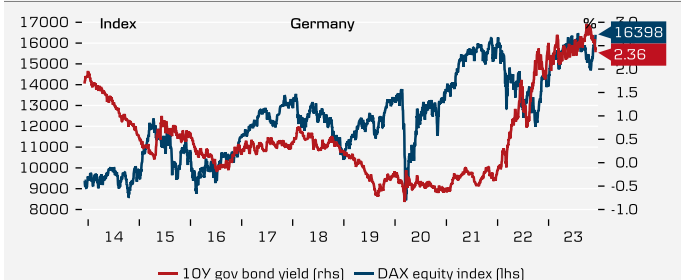
Source: Macrobond Financial, Danske Bank

Price expectations



Source: EU Commission, Macrobond Financial, Danske Bank

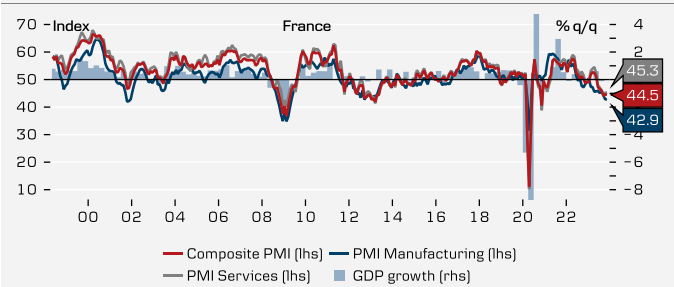
Financial markets



Source: Macrobond Financial, Danske Bank

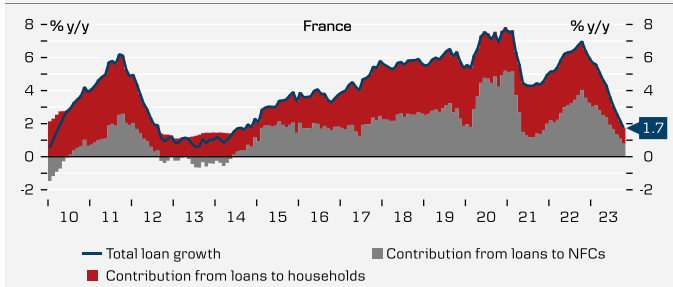
France

PMI and GDP growth



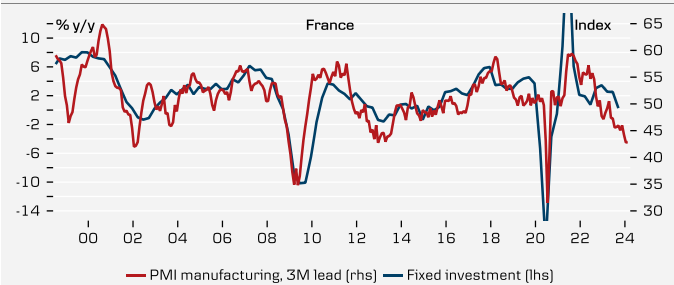
Source: Macrobond Financial, Danske Bank

Credit growth



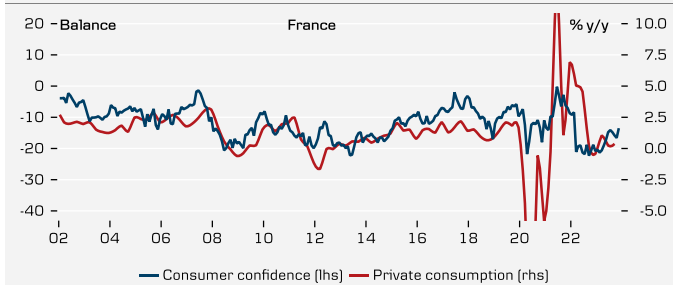
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Manufacturing sentiment and investments



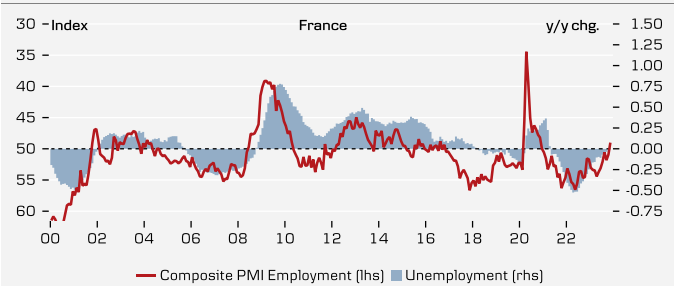
Source: Macrobond Financial, Danske Bank

Consumer confidence and private consumption



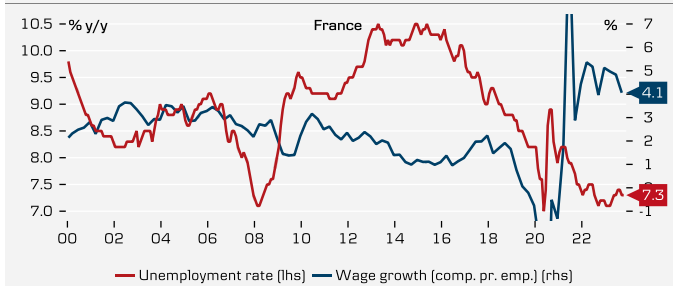
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Unemployment and PMI



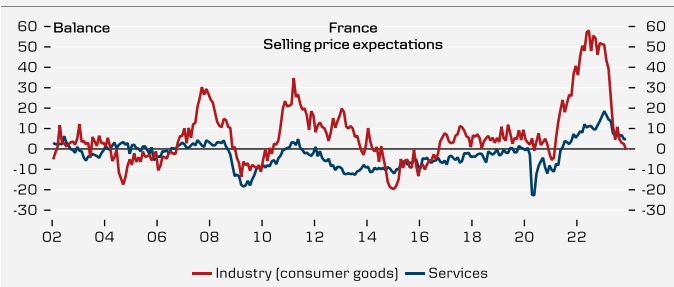
Source: Macrobond Financial, Danske Bank

Unemployment and wage growth



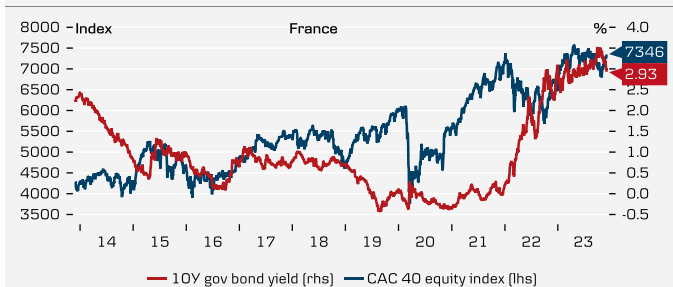
Source: Macrobond Financial, Danske Bank

Price expectations



Source: EU Commission, Macrobond Financial, Danske Bank

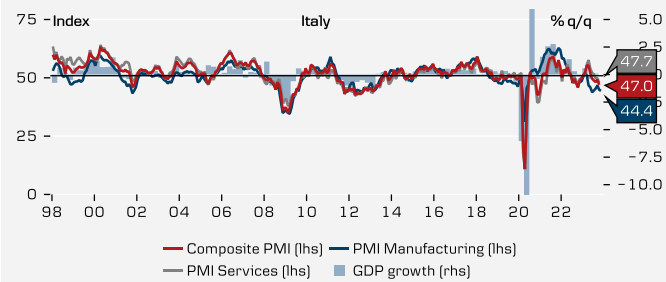
Financial markets



Source: Macrobond Financial, Danske Bank

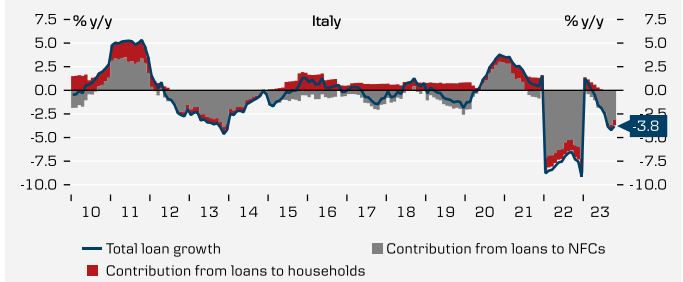
Italy

PMI and GDP growth



Source: Macrobond Financial, Danske Bank

Credit growth



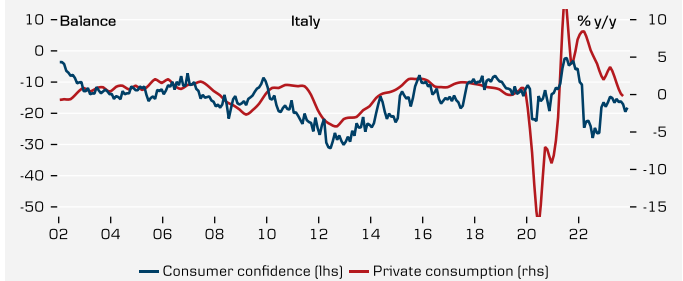
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Manufacturing sentiment and investments



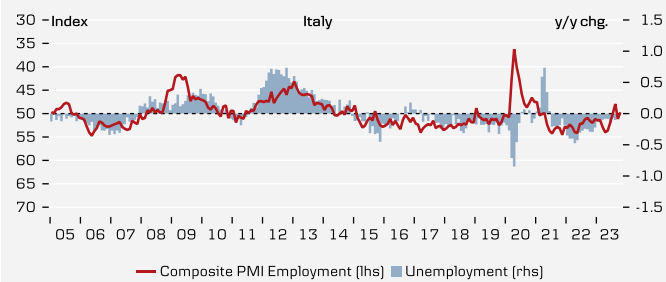
Source: Macrobond Financial, Danske Bank

Consumer confidence and private consumption



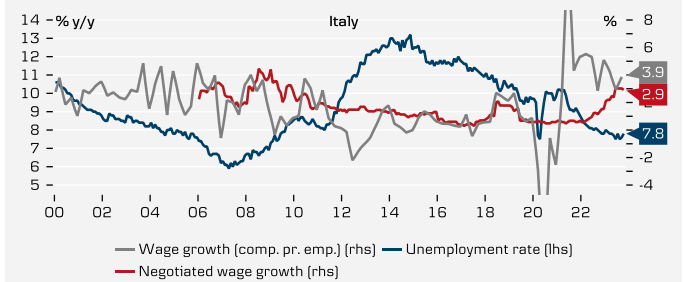
Source: Macrobond Financial, Danske Bank

Unemployment and PMI



Source: Macrobond Financial, Danske Bank

Unemployment and wage growth



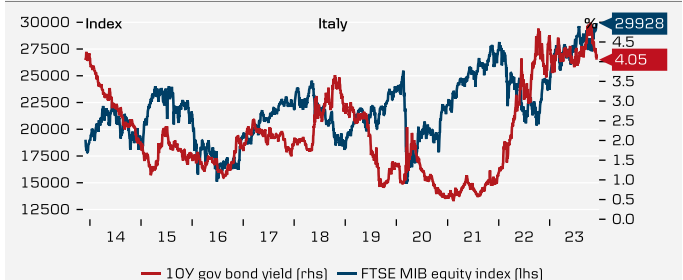
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Price expectations



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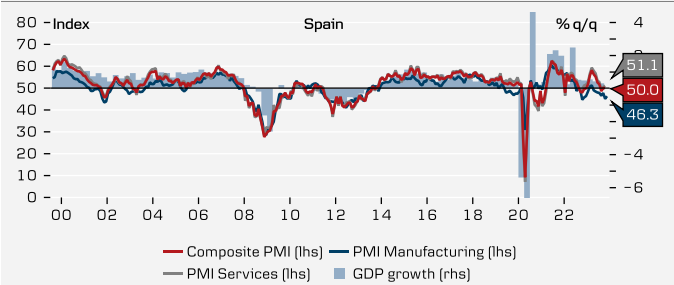
Financial markets



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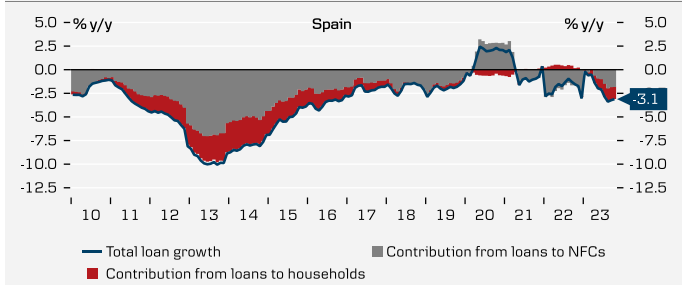
Spain

PMI and GDP growth



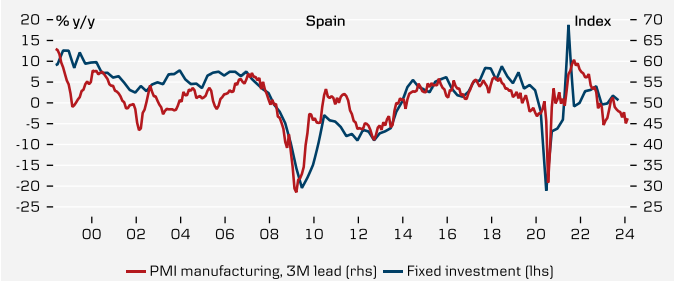
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Credit growth



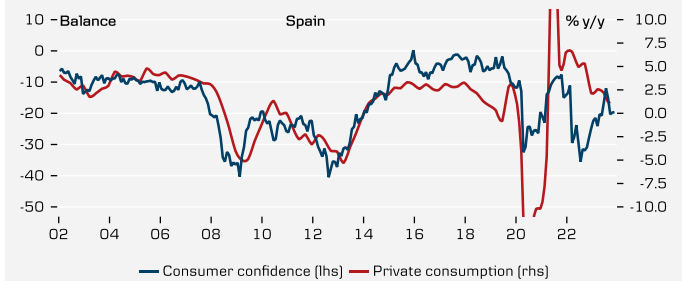
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Manufacturing sentiment and investments



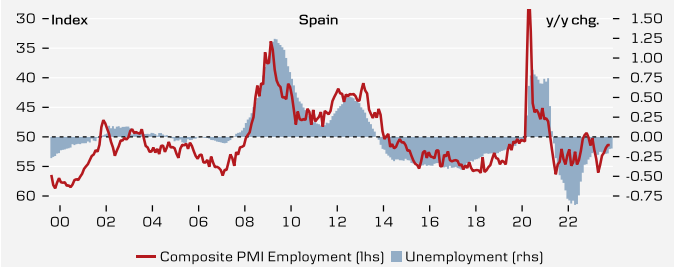
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Consumer confidence and private consumption



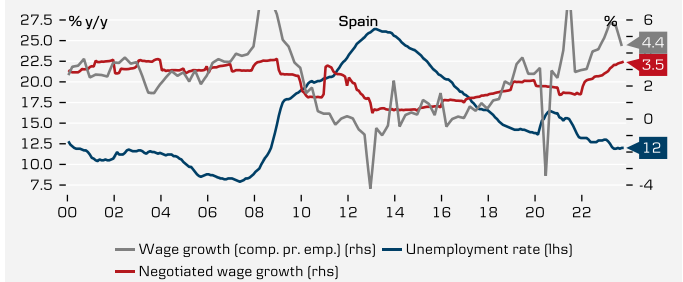
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Unemployment and PMI



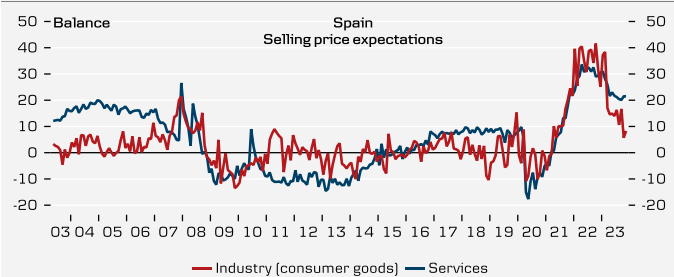
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Unemployment and wage growth



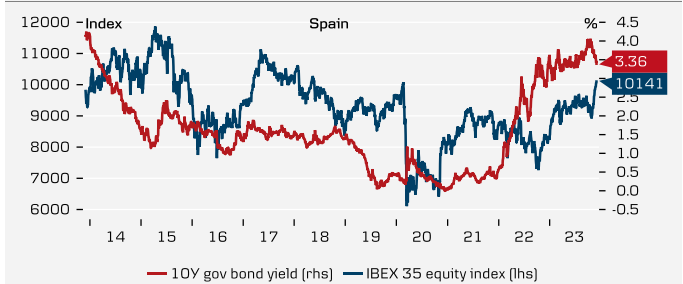
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Price expectations



Source: EU Commission, Macrobond Financial, Danske Bank

Financial markets



Source: Macrobond Financial, Danske Bank

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