

# Euro Area Macro Monitor

## Tug of war between fiscal easing and monetary tightening

- September brought few rays of light for the euro area economy.** Business surveys such as PMIs and consumer confidence fell further into recessionary territory amid waning jobs growth and slowing retail spending. While gas and electricity prices have come somewhat off their latest peaks, meteorologists have *warned* that Europe could suffer a colder winter with less wind and rain than usual, keeping risks of gas rationing and new price spikes alive. On top of earlier measures, EU countries agreed on a 5% mandatory reduction in peak electricity consumption, a windfall tax on fossil fuel companies and a EUR/Mwh 180 price cap for electricity generated by non-gas power producers. But despite intense negotiations no agreement on an EU-wide gas price cap has yet been reached, amid fears that it could divert gas to other regions that are willing to pay more for supplies.
- A ‘tug of war’ is increasingly visible between fiscal easing and monetary tightening.** While high inflation keeps pressure on ECB to front-load more rate hikes (we expect another 75bp in October), governments are coming up with ever more creative ways to shield consumers and firms from the adverse repercussions of the energy crisis. Germany announced an up to EUR 200bn (5.5% of GDP) aid package, financed through new borrowing and channelled through the Economic Stabilisation Fund (WSF), with the aim to cap gas and electricity prices. While this could limit inflation pressures in the near-term, we doubt that it will be enough to prevent the economy falling into recession in H2 22. Germany’s display of fiscal largesse has antagonised some EU countries lacking the same fiscal firepower and behind the scenes discussions are intensifying over another round of EU-wide borrowing to confront the current crisis, by for example reviving the Covid-era SURE lending scheme.
- In contrast to the US, an inflation peak remains out of sight in Europe,** where HICP inflation rose to 10% in September. Heterogeneous country developments (with rising inflation in Germany, Netherlands and Italy vs. falling inflation in Spain and France), reflecting idiosyncratic country measures to limit price increases, further complicate the job of finding the right policy calibration for ECB. Despite tentative signs of moderating inflation pressures in non-essential items such as package holidays, a renewed rise in firm selling price expectations suggests that the weakening demand environment has yet to slow price increases on a broad scale.
- Italy’s election brought a resounding win for the right-wing coalition of Brothers of Italy, League and Forza Italy** gaining ca. 44% of the vote, enough for a majority in both chambers of parliament. With lingering fiscal uncertainties, Italian bond spreads widened after the election outcome, although partly also due to the general risk-off mood in markets. A new government will probably not take office before the end of October, with the personality of the crucial finance ministry yet to be decided. However, a difficult balancing act awaits the government, just as Italy is heading into the crucial 2023 budget season, with a slowing economy and calls for additional support for households and firms growing louder. Any attempts for big revisions to Italy’s recovery and resilience plans and accompanying structural reforms will be seen as negative by the market and rating agencies, as it could endanger continued NGEU fund disbursements and any future activation of the ECB’s TPI programme.

### Key points

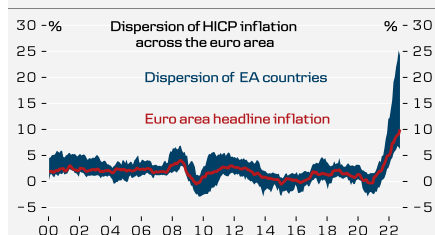
- Finding common solutions for Europe’s energy crisis is easier said than done.
- ‘Tug of war’ between fiscal easing and monetary tightening intensifies.
- Difficult balancing act awaits new Italian government.

### Ifo business expectations lower than during the Global Financial Crisis



Source: Ifo, Eurostat, Macrobond Financial, Danske Bank

### Growing inflation dispersion makes ECB’s job even harder



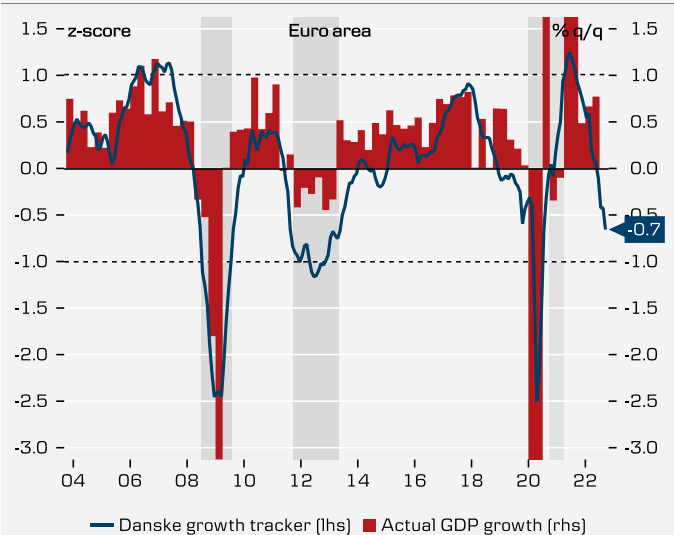
Source: Eurostat, Macrobond Financial, Danske Bank

Senior Euro Area Analyst  
Aïla Mihr  
+45 45 12 85 35  
amih@danskebank.dk

# The Danske euro area growth tracker

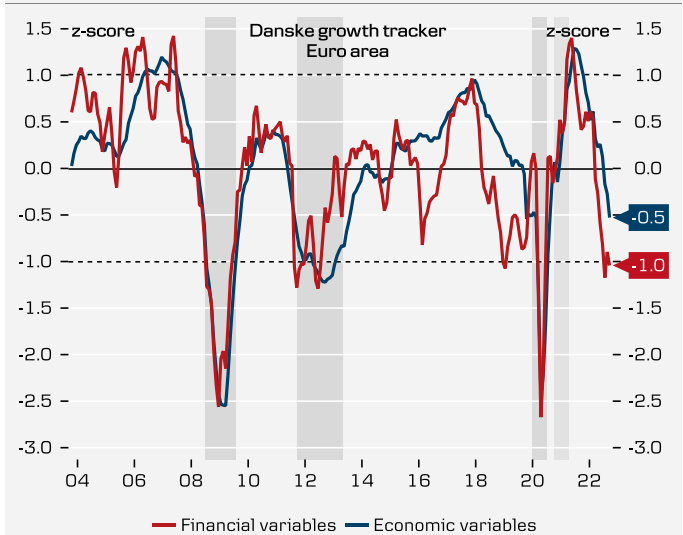
Our growth tracker fell further to a value of -0.7 in September. Both financial and economic variables continued their downtrend, with the sharp fall in consumer confidence standing out. While, our growth tracker does not yet signal that the euro area has entered recession territory (-1 or below), our traffic light suggests that the recession risk remains high.

Growth tracker and actual GDP growth



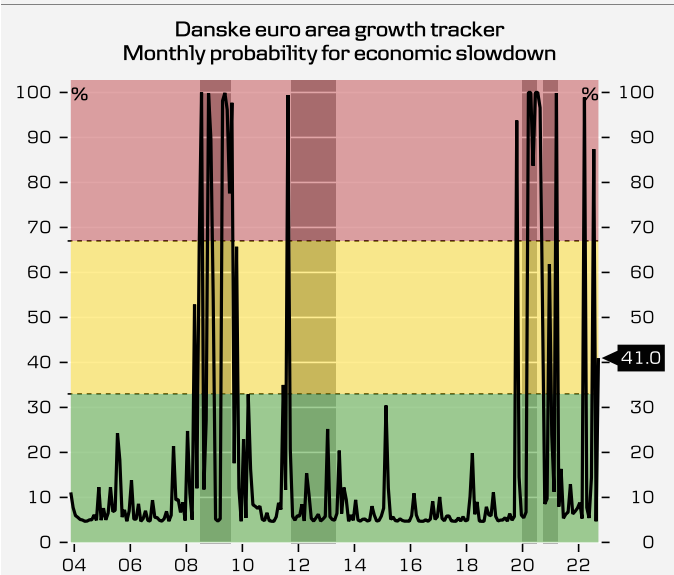
Note: Shaded area indicates historical recessions  
Source: Macrobond Financial, Danske Bank

Growth tracker: financial and economic variables



Note: Shaded area indicates historical recessions  
Source: Macrobond Financial, Danske Bank

Monthly probability of economic slowdown



Note: Shaded area indicates historical recessions  
Source: EViews, Macrobond Financial, Danske Bank

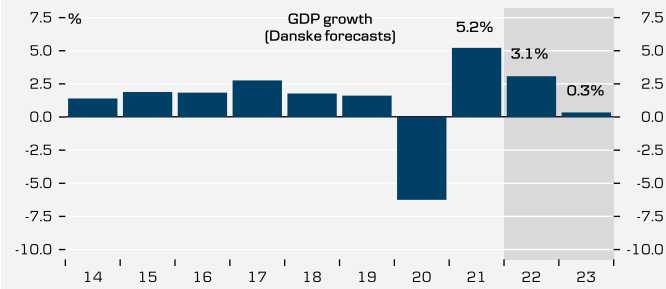
Danske growth tracker decomposition

	September 2022
<b>Economic variables</b>	-0,5
Profit growth	1,2
Unemployment	1,1
Credit growth	0,8
Capacity utilisation	0,6
Real M1 growth	-0,4
European sentiment indicator	-0,6
ZEW	-0,8
OECD CLI	-0,8
Composite PMI	-0,8
EuroCOIN	-1,7
PMI order-inventory balance	-1,8
Consumer confidence	-3,2
<b>Financial variables</b>	-1,0
Euro surprise index	-0,1
Corporate vs. gov. bond yield	-1,1
Eurostoxx50	-1,1
Sentix	-1,9

Source: Danske Bank

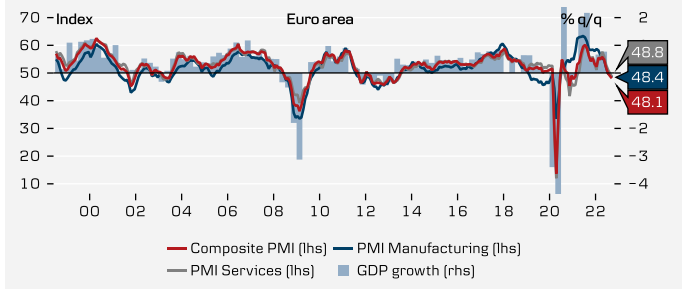
# Euro area

## GDP growth forecasts



Source: Macrobond Financial, Danske Bank forecasts

## PMI and GDP growth



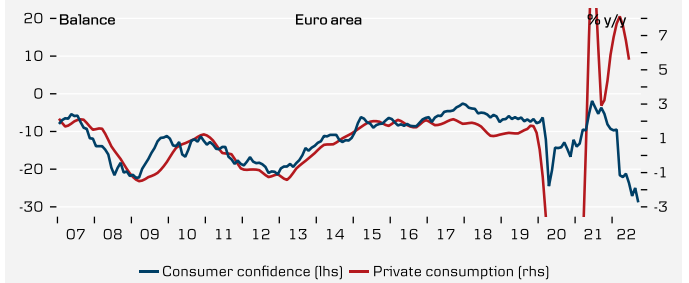
Source: Macrobond Financial, Danske Bank

## Manufacturing sentiment and investments



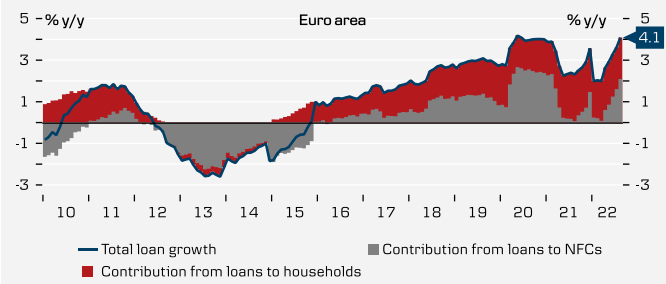
Source: Macrobond Financial, Danske Bank

## Consumer confidence and private consumption



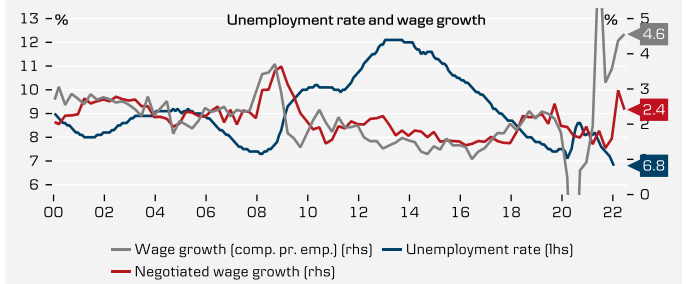
Source: Macrobond Financial, Danske Bank

## Credit growth



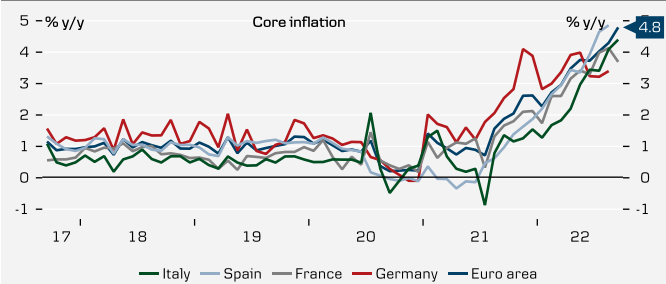
Source: Macrobond Financial, Danske Bank

## Unemployment and wage growth



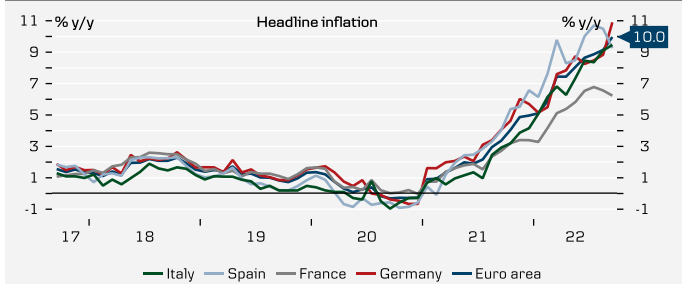
Source: Macrobond Financial, Danske Bank

## Core inflation



Source: Macrobond Financial, Danske Bank

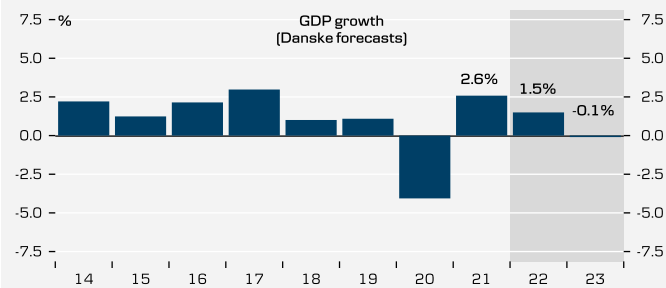
## HICP inflation



Source: Macrobond Financial, Danske Bank

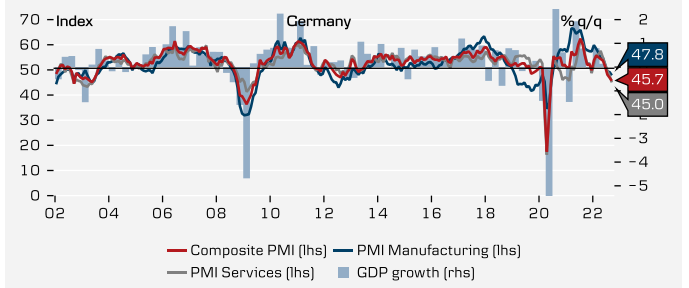
# Germany

## GDP growth forecasts



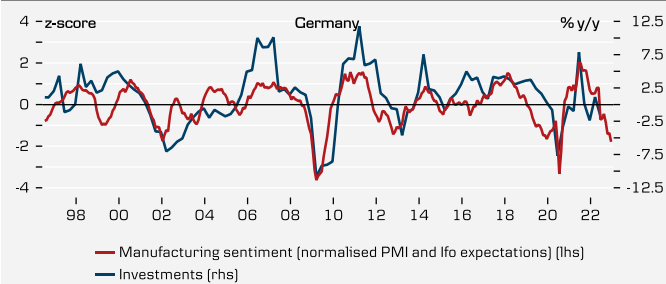
Source: Macrobond Financial, Danske Bank forecasts

## PMI and GDP growth



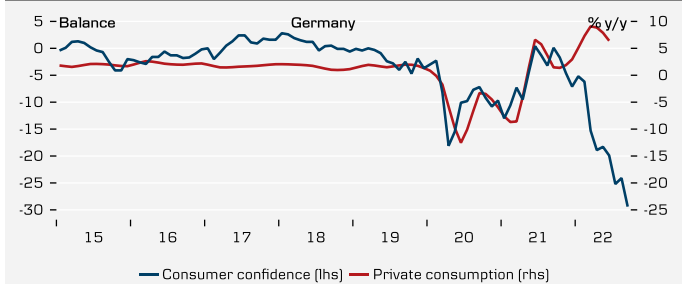
Source: Macrobond Financial, Danske Bank

## Manufacturing sentiment and investments



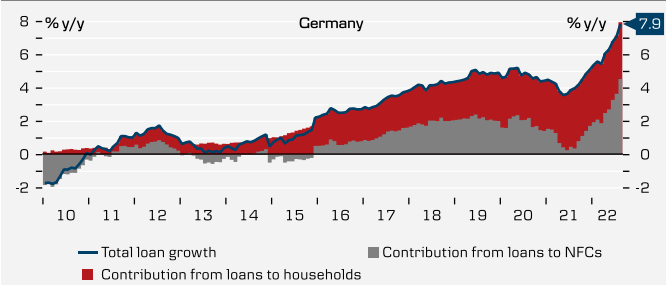
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## Consumer confidence and private consumption



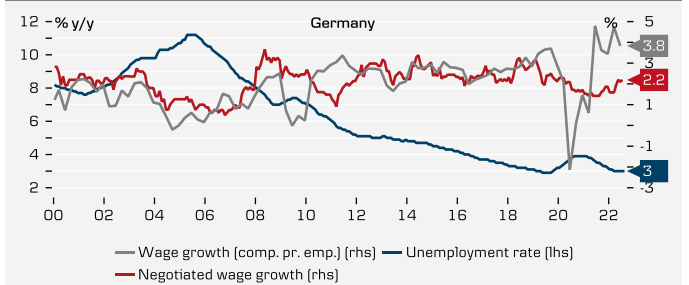
Source: Macrobond Financial, Danske Bank

## Credit growth



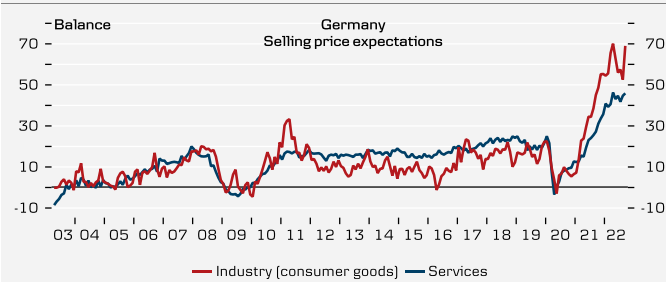
Source: Macrobond Financial, Danske Bank

## Unemployment and wage growth



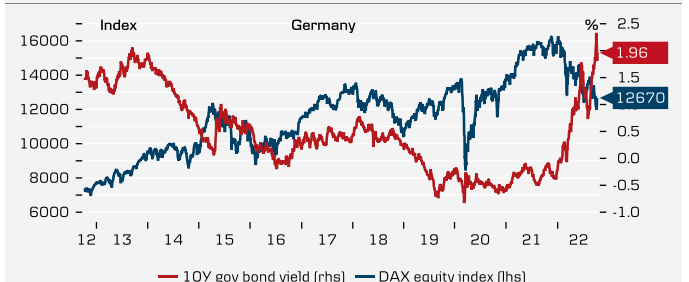
Source: Macrobond Financial, Danske Bank

## Price expectations



Source: EU Commission, Macrobond Financial, Danske Bank

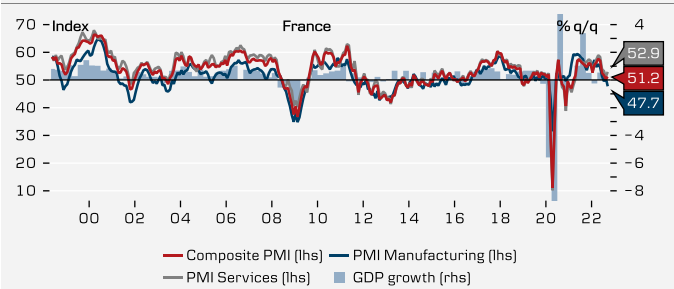
## Financial markets



Source: Macrobond Financial, Danske Bank

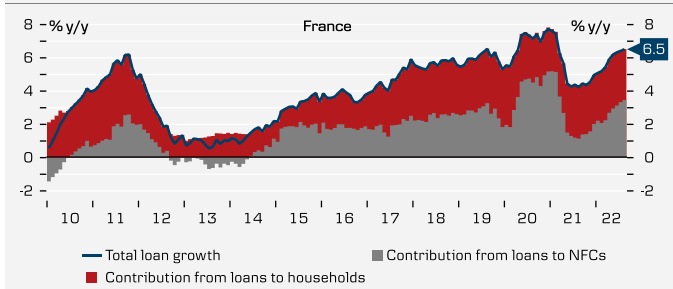
# France

## PMI and GDP growth



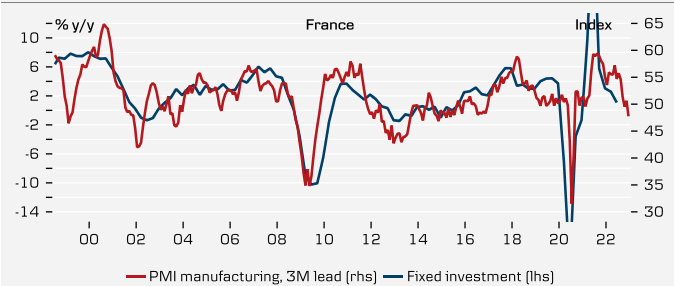
Source: Macrobond Financial, Danske Bank

## Credit growth



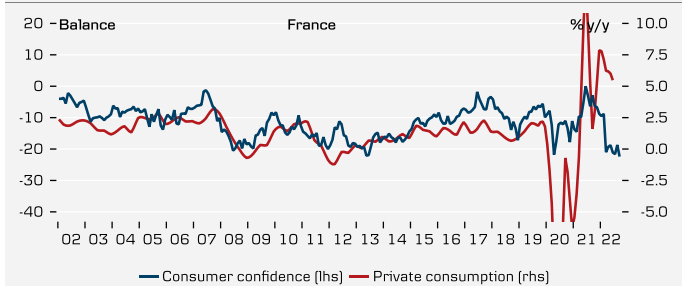
Source: Macrobond Financial, Danske Bank

## Manufacturing sentiment and investments



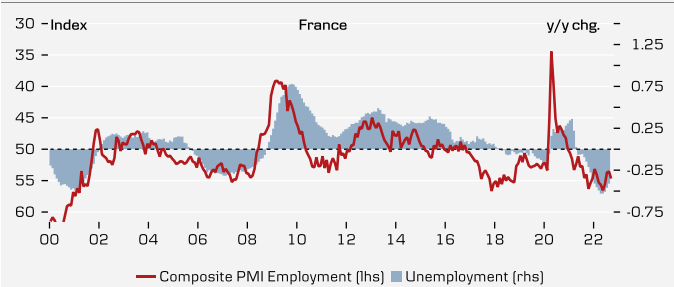
Source: Macrobond Financial, Danske Bank

## Consumer confidence and private consumption



Source: Macrobond Financial, Danske Bank

## Unemployment and PMI



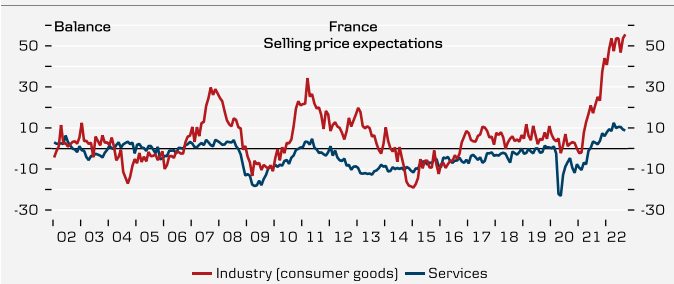
Source: Macrobond Financial, Danske Bank

## Unemployment and wage growth



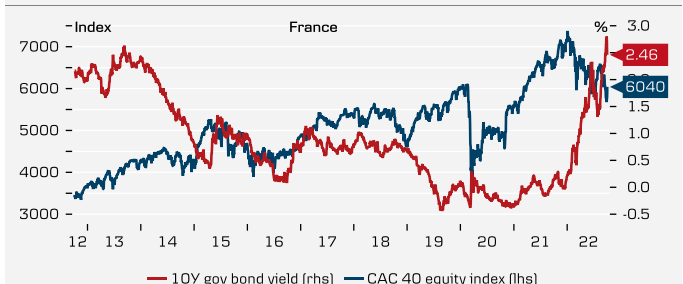
Source: Macrobond Financial, Danske Bank

## Price expectations



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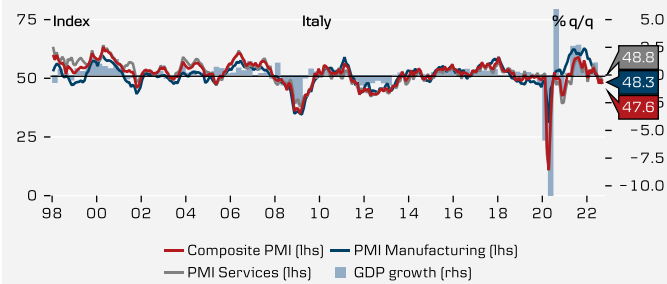
## Financial markets



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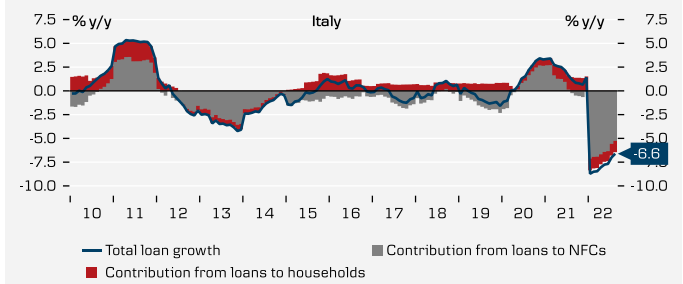
# Italy

## PMI and GDP growth



Source: Macrobond Financial, Danske Bank

## Credit growth



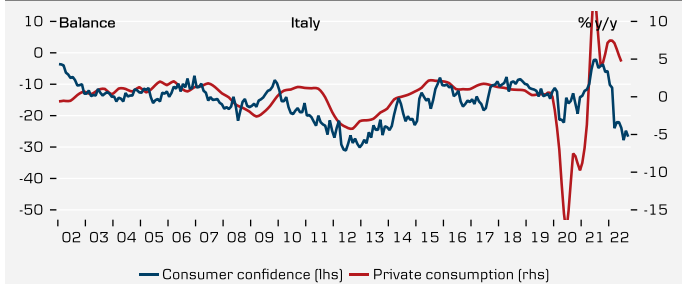
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## Manufacturing sentiment and investments



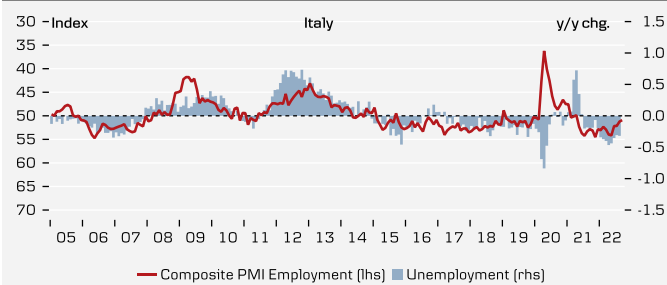
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## Consumer confidence and private consumption



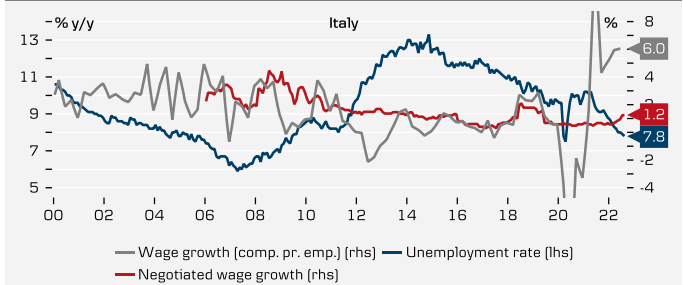
Source: Macrobond Financial, Danske Bank

## Unemployment and PMI



Source: Macrobond Financial, Danske Bank

## Unemployment and wage growth



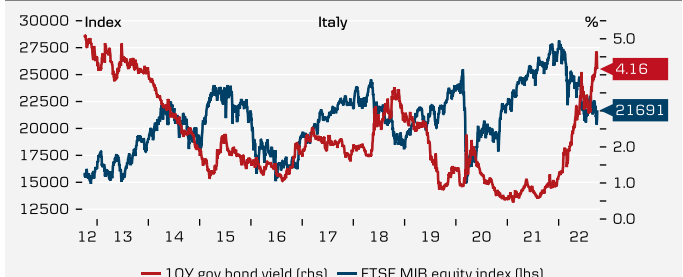
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## Price expectations



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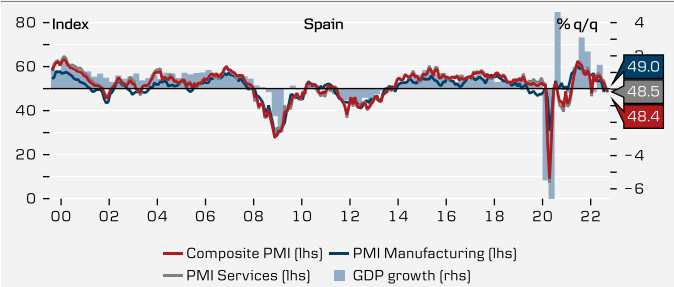
## Financial markets



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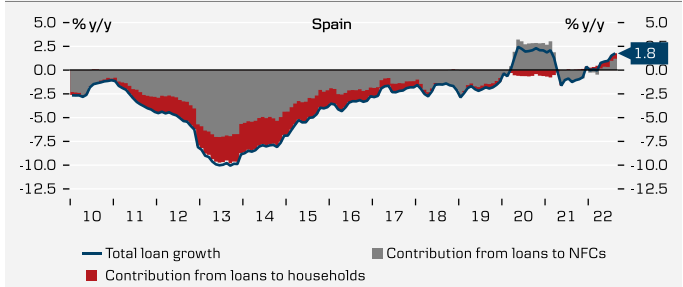
# Spain

## PMI and GDP growth



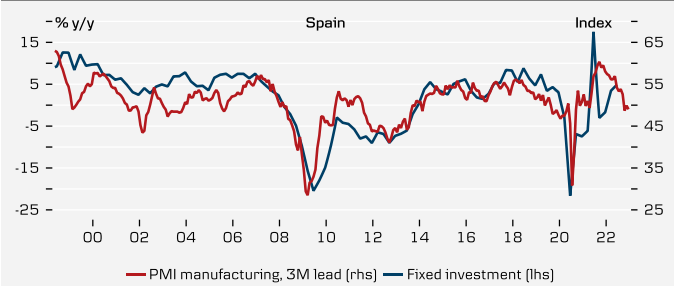
Source: Macrobond Financial, Danske Bank

## Credit growth



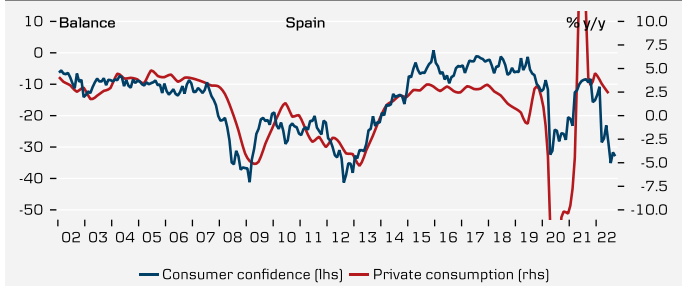
Source: Macrobond Financial, Danske Bank

## Manufacturing sentiment and investments



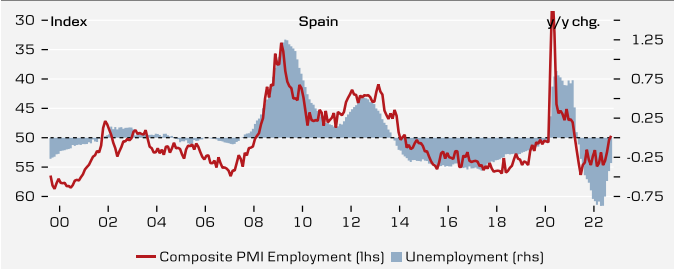
Source: Macrobond Financial, Danske Bank

## Consumer confidence and private consumption



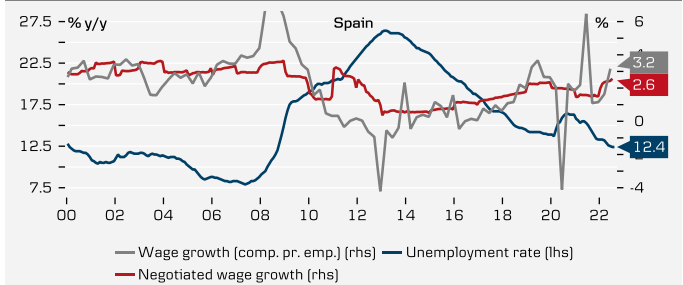
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## Unemployment and PMI



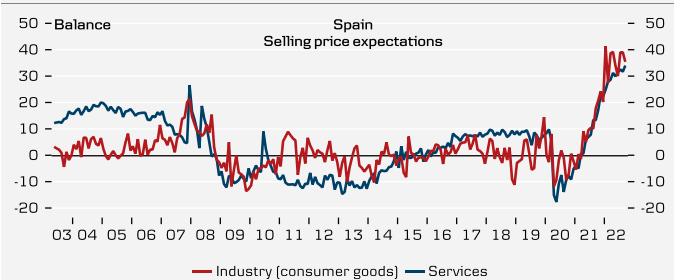
Source: Macrobond Financial, Danske Bank

## 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

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