

Euro Area Macro Monitor

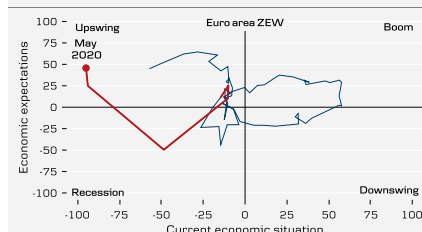
Spring is in the air

- **May brought the first evidence that a recovery is taking shape in the euro area** (see Danske growth tracker). Both the service and manufacturing PMIs rebounded – though remaining in contraction territory – as the economies partly started to emerge from lockdowns. Moreover, forward-looking expectations components in a range of leading indicators extended their rebound, signalling that the economy should soon move into the ‘upswing quadrant’. **Overall, leading indicators tell us that the downturn has bottomed out, but the level of the PMIs still indicate that economic activity continues falling, only at a slower pace than previously.** Hence, it is essential that we see PMIs rebounding above the 50 level in the coming months before we can talk about a real recovery taking shape. We still expect a gradual euro area recovery to unfold in H2 20, led by private consumption and supported by a sizeable fiscal boost, but the risk of an asymmetric recovery between the North and South remains. Germany unveiled another massive recovery stimulus package of EUR130bn (3.8% of GDP) to boost consumer demand and strategic investments, and the fiscal tailwind is one reason why we expect the German economy to weather the COVID-19 storm better than other European countries (see *The Big Picture - Reopening, recovery and risks*, 2 June 2020).
- In contrast to the economic damage, the negative impact on the euro area inflation outlook has been more muted so far. Thanks to a surge in food prices and an upward bias for core inflation, resulting from imputations of services prices, euro area HICP inflation just about avoided falling into sub-zero territory in May (0.06%). We think disinflationary pressures from falling oil prices and discounting campaigns will maintain the upper hand in the near term. However, **unprecedented monetary/fiscal easing and cost push inflation in some industries leave room for a reflation spiral eventually to emerge** (see also *Euro Area Research - The road to recovery*, 14 May).
- **May also marked the beginning of a possible new era for the EU.** The EU Commission unveiled the details of an ambitious recovery fund (under the headline ‘Next generation EU’) amounting to EUR500bn in grants + EUR250bn in loans (see chart for country allocation and *Flash Comment: Next Generation EU: A landmark for European history?*, 27 May). **We view the recovery fund as an important game changer both on the economic and political fronts.** Although it does not resolve the issue of high debt levels, it marks an important step towards solidarity and risk sharing at the European level. We expect the fiscal boost to alleviate the risk of an asymmetric recovery, although most of it will likely only materialise in H1 21.
- The arrival of a common European fiscal response is especially welcome, as the ECB’s crisis fighting power has lately come under pressure after the ruling of Germany’s constitutional court. However, ECB policymakers left no doubt about their commitment to support the euro area recovery and contain financial fragmentation and extended the Pandemic Emergency Purchase Programme (PEPP) at the June meeting by another EUR600bn until June 2021 (see *Flash ECB Research: ECB gave markets a PEPP talk*, 4 June). **Credit growth, especially to corporations, has accelerated in recent months in a sign that the ECB’s stimulus is supporting the real economy.**

Key points

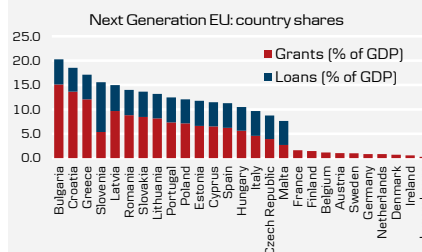
- The downturn has bottomed out, but a real recovery is yet to come
- The proposed EU recovery fund reduces the risk of an asymmetric recovery and marks a possible new era of the EU project
- ECB ‘PEPPs up’ its bond buying

Euro area seen moving further into upswing quadrant



Source: ZEW, Macrobond Financial, Danske Bank

Southern and Eastern European countries set to benefit most from recovery fund grants



Source: FAZ, Danske Bank

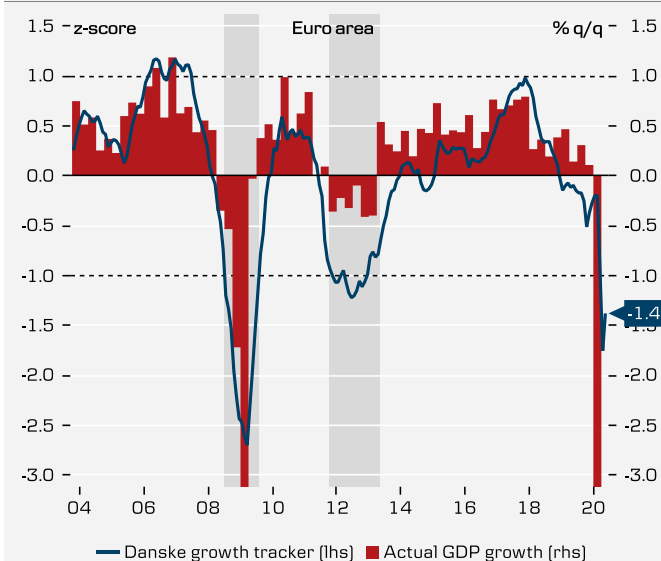
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The Danske euro area growth tracker

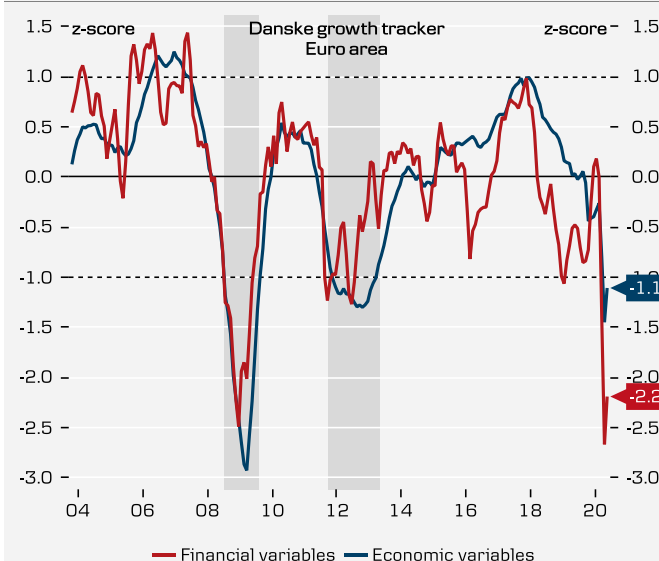
With a value of -1.4, our Danske growth tracker remains in recession territory (value of -1 or below), but still showed signs of a rebound in May, led both by financial and economic variables. The receding recession risk is also apparent from our growth tracker traffic light, which translates our growth tracker signal into a probability framework. After months of elevated recession risks, the implied monthly probability of a slowdown is back at the lowest level since February 2020, as the traffic light has returned to the 'green area'.

Growth tracker and actual GDP growth



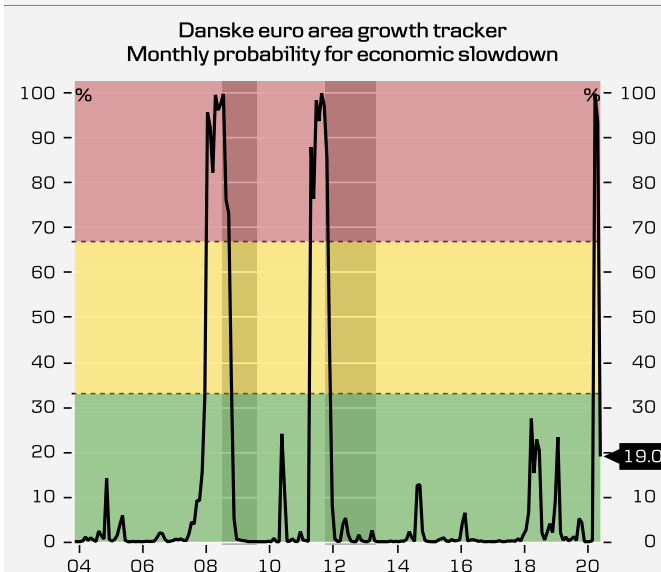
Note: Shaded area indicates historical recessions
Source: Macrobond Financial, Danske Bank

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

	May 2020
Economic variables	-1.1
Unemployment	0.4
Profit growth	0.4
Real M1 growth	0.4
Credit growth	0.2
OECD CLI	0.0
PMI order-inventory balance	0.0
Consumer confidence	-1.4
EuroCOIN	-1.5
ZEW	-1.7
European sentiment indicator	-3.1
Capacity utilisation	-3.2
Composite PMI	-4.0
Financial variables	-2.2
Eurostoxx50	-0.9
Corporate vs. gov. bond yield	-1.1
Sentix	-2.5
Euro surprise index	-4.2

Source: Danske Bank

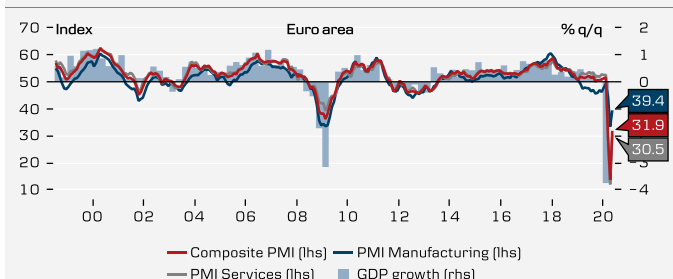
Euro area

GDP growth forecasts



Source: Macrobond Financial, Danske Bank forecasts

PMI and GDP growth



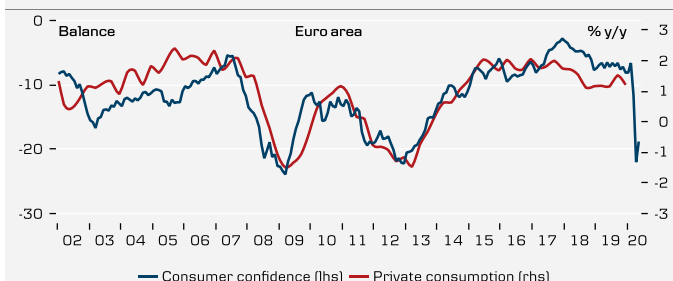
Source: Macrobond Financial, Danske Bank

Manufacturing sentiment and investments



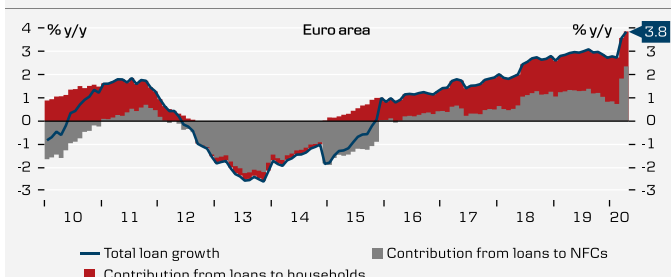
Source: Macrobond Financial, Danske Bank

Consumer confidence and private consumption



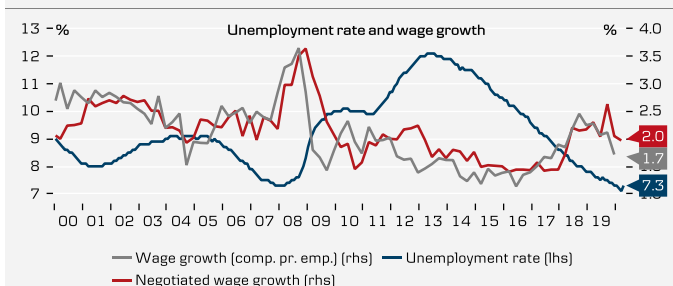
Source: Macrobond Financial, Danske Bank

Credit growth



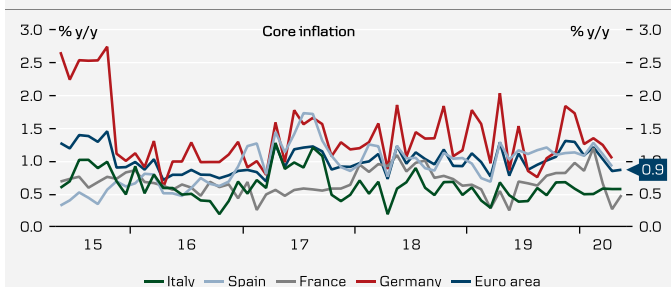
Source: Macrobond Financial, Danske Bank

Unemployment and wage growth



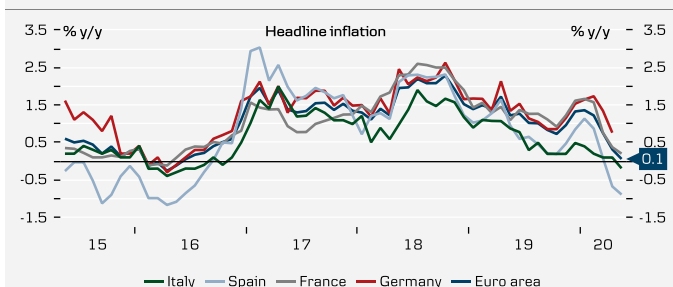
Source: Macrobond Financial, Danske Bank

Core inflation



Source: Macrobond Financial, Danske Bank

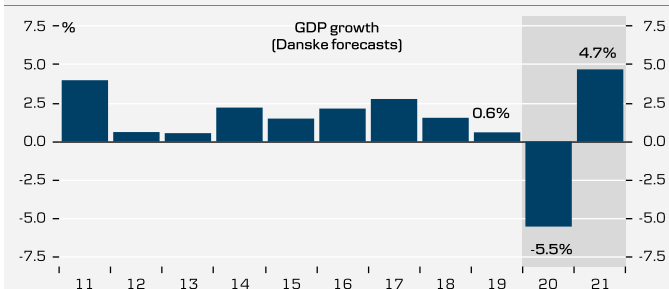
HICP inflation



Source: Macrobond Financial, Danske Bank

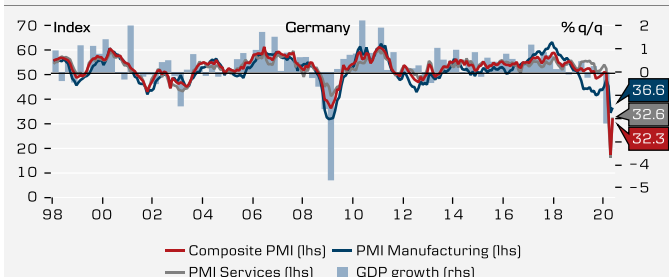
Germany

GDP growth forecasts



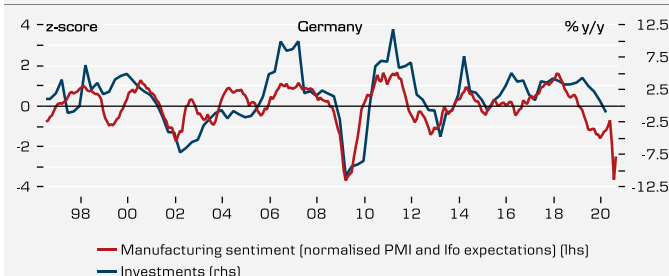
Source: Macrobond Financial, Danske Bank forecasts

PMI and GDP growth



Source: Macrobond Financial, Danske Bank

Manufacturing sentiment and investments



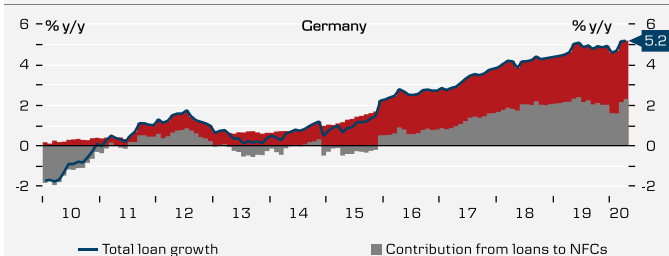
Source: Macrobond Financial, Danske Bank

Consumer confidence and private consumption



Source: Macrobond Financial, Danske Bank

Credit growth



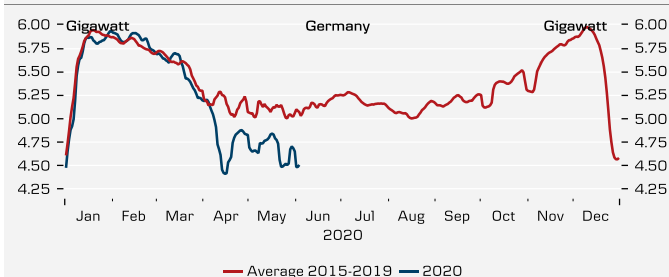
Source: Macrobond Financial, Danske Bank

Unemployment and wage growth



Source: Macrobond Financial, Danske Bank

Electricity consumption



Source: Macrobond Financial, Danske Bank

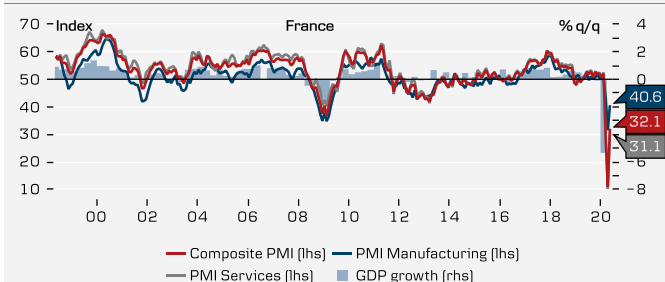
Financial markets



Source: Macrobond Financial, Danske Bank

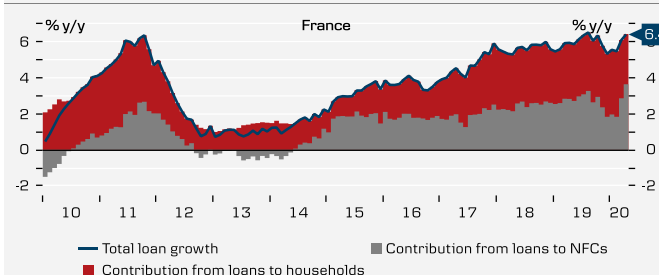
France

PMI and GDP growth



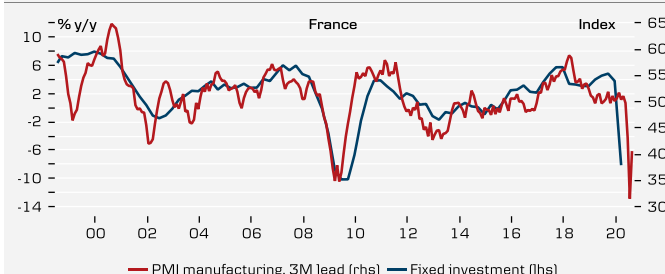
Source: Macrobond Financial, Danske Bank

Credit growth



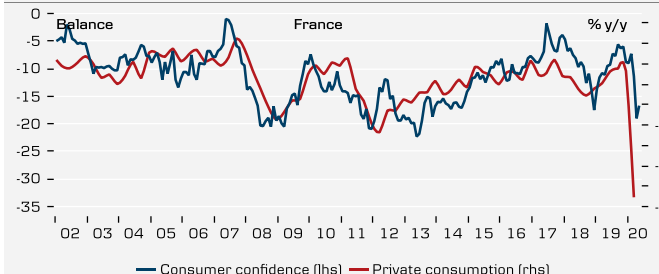
Source: Macrobond Financial, Danske Bank

Manufacturing sentiment and investments



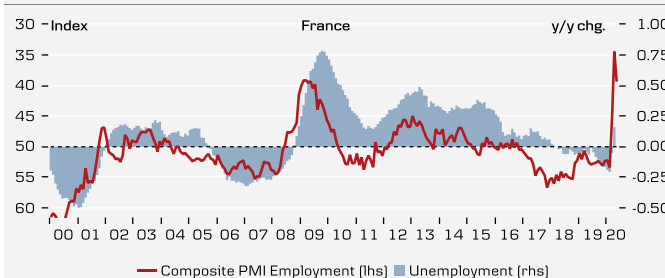
Source: Macrobond Financial, Danske Bank

Consumer confidence and private consumption



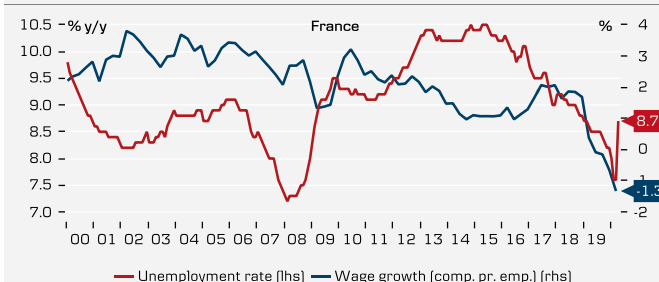
Source: Macrobond Financial, Danske Bank

Unemployment and PMI



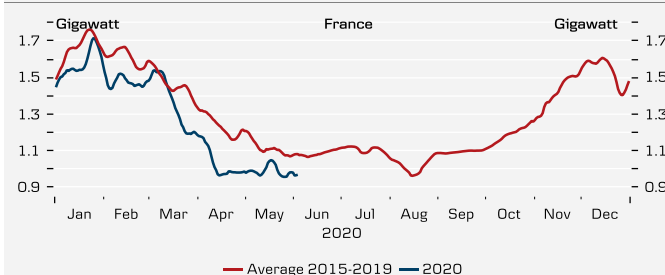
Source: Macrobond Financial, Danske Bank

Unemployment and wage growth



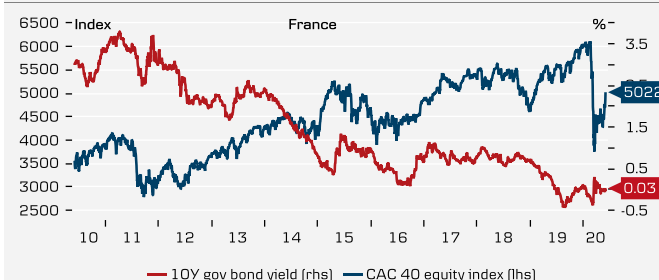
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Electricity consumption



Source: Macrobond Financial, Danske Bank

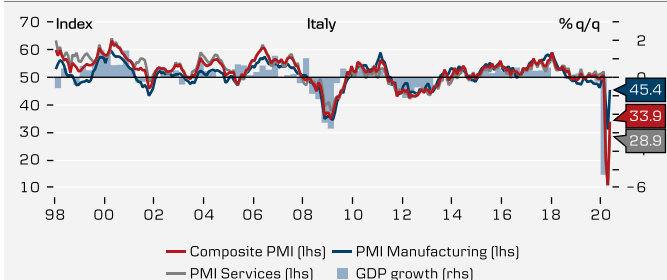
Financial markets



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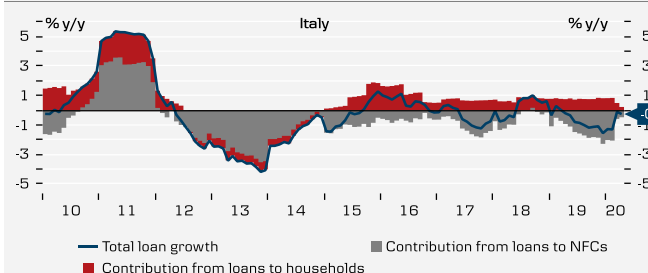
Italy

PMI and GDP growth



Source: Macrobond Financial, Danske Bank

Credit growth



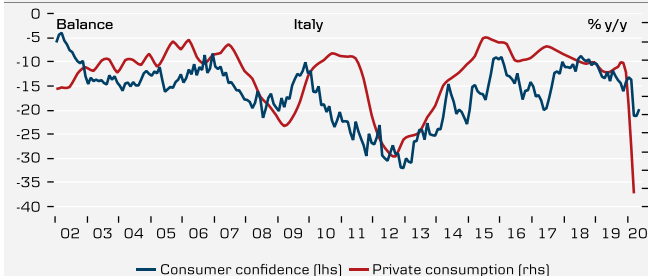
Source: Macrobond Financial, Danske Bank

Manufacturing sentiment and investments



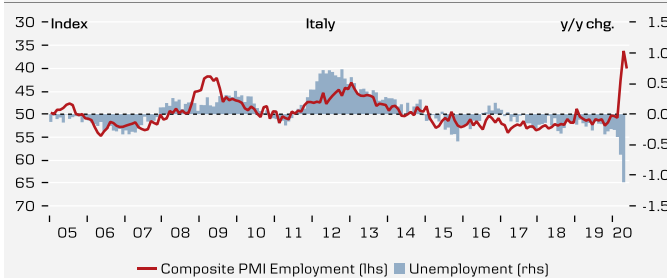
Source: Macrobond Financial, Danske Bank

Consumer confidence and private consumption



Source: Macrobond Financial, Danske Bank

Unemployment and PMI



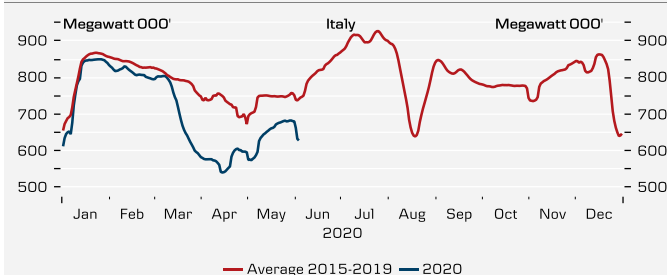
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Unemployment and wage growth



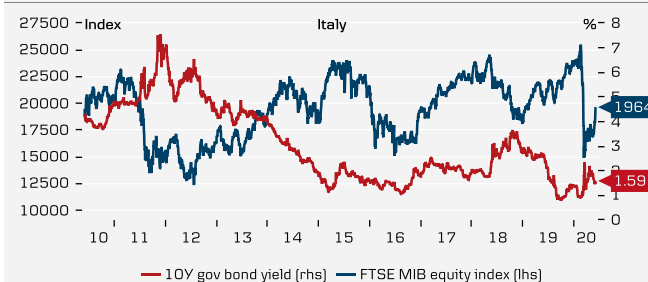
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Electricity consumption



Source: Macrobond Financial, Danske Bank

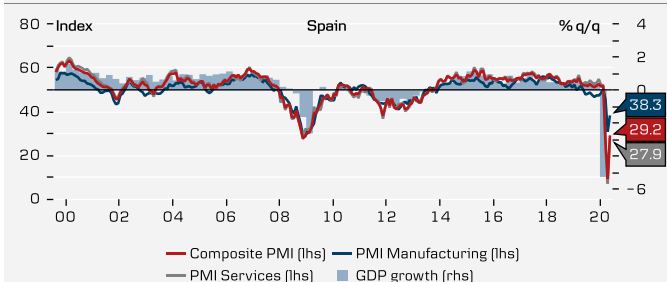
Financial markets



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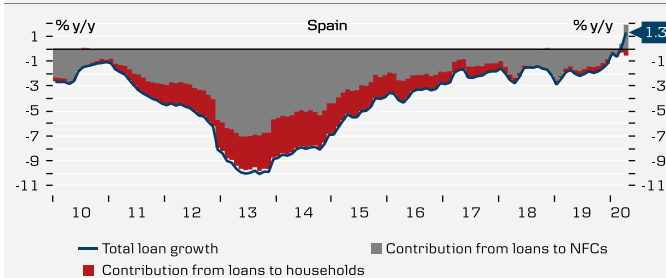
Spain

PMI and GDP growth



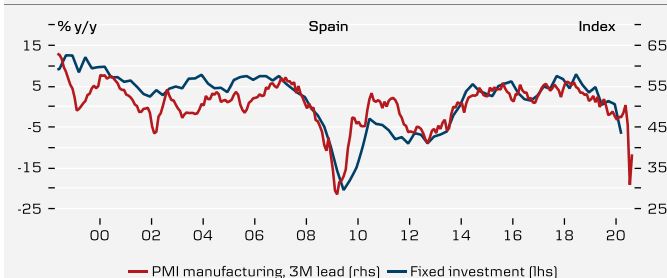
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Credit growth



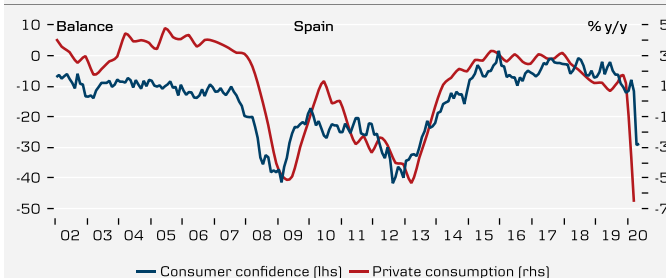
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Manufacturing sentiment and investments



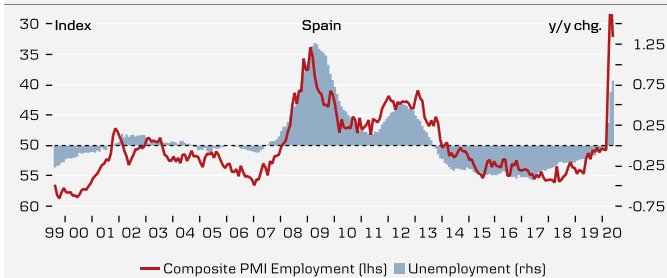
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Consumer confidence and private consumption



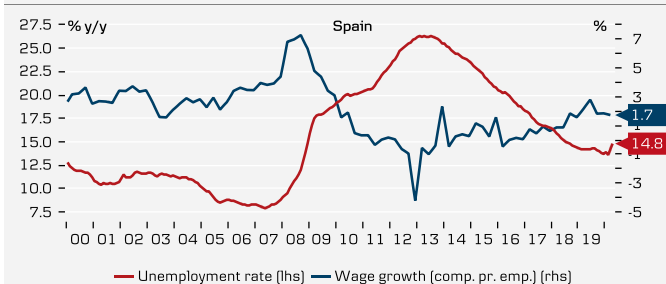
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Unemployment and PMI



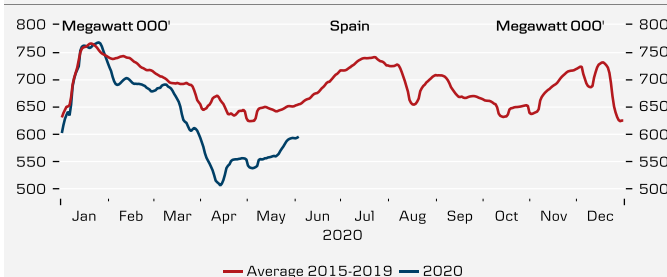
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Unemployment and wage growth



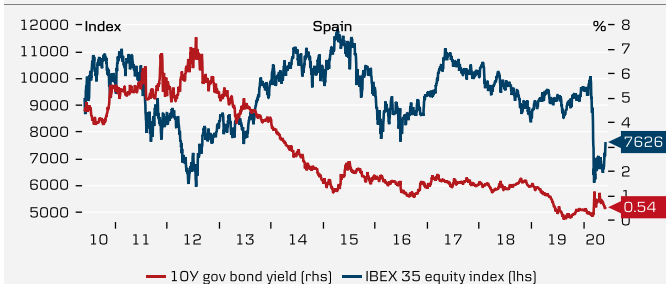
Source: Macrobond Financial, Danske Bank

Electricity consumption



Source: Macrobond Financial, Danske Bank

Financial markets



Source: Macrobond Financial, Danske Bank

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This research report has been prepared by Danske Bank A/S ('Danske Bank'). The authors of this research report are Rune Thyge Johansen, Assistant Analyst, and Aila Mihr, Senior Analyst.

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None.

Date of first publication

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