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## MACRO NEWS

16 / 08 / 17

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### EUROZONE GDP: THE FIRMER RECOVERY SPREADS

#### Berenberg Macro Flash

Eurozone GDP, Q2 (qoq, in %) – 2nd reading

<b>Actual:</b>	<b>0.6</b>
Previous:	0.5
Consensus:	0.6
Berenberg:	0.5

**Solid growth spreads across the Eurozone:** The Eurozone enjoyed its 17<sup>th</sup> consecutive quarter of growth in Q2. And most countries of the currency union were at the party. As the core's recovery becomes ever more entrenched, countries that have for a very long time (Greece) struggled to get a stable footing, are beginning to recover, too. This is good news. Since inflation has remained low and does not vary much across countries, it makes the job of the currency union's central bank, the ECB, a little less challenging. Given what the Eurozone has been through, this is a sweet spot. Whether this is still the case in years to come, remains to be seen. It is clear that the job is far from done. The Eurozone needs more time of economic recovery and political stability to fully forget about the years of the double whammy of the financial and euro crises and is adequately prepared to weather economic storms in the future. The second largest economy in the Eurozone is planning to overhaul its labour code. If Macron succeeds in France on his endeavour and pushes for some institutional changes in continental Europe, and we believe he does, France and the Eurozone should enjoy solid growth for years to come.

**Small upward revision of Q2 growth:** The second reading confirmed the first estimate of real GDP growing by 0.6% qoq in Q2. The second reading includes more country-level data, including the actual performance of the industrial and retail sector of the quarter's last month (June). Industrial production in June fell mom, with only a small impact on the quarterly average change versus Q1 which was 1.2%. Retail sales increased further in June, with the quarterly average at 0.9% qoq. The result was a small upward revision in GDP compared to the first estimate, with the qoq growth rate rising from 0.56% to 0.63%. We have to wait for the third estimate published on 5 September for a breakdown of the expenditure components of GDP.

**Outlook positive, chance that GDP growth holds up its solid pace in H2:** For the rest of the year, we expect some moderation in the pace of expansion, from 0.5-0.6% qoq in the first half, down to 0.4-0.5% which is closer to trend. Leading indicators such as the PMIs for two months in a row have signalled that the growth rate has reached somewhat of a peak. The less weaker euro is also biting into growth as it weighs on exports while raising demand for imports. An overall rise in foreign demand may, however, offset what the appreciated exchange rate costs the Eurozone in competitiveness. If the last four quarters (2016 Q2–2017 Q1) and the national Q2 data provided so far are any guidance, it is domestic demand that is boosting the economy, while net exports have not been a big driver (see chart). In case the PMI reverses its downward trend and other sentiment indicators continue skyrocketing, the Eurozone economy may continue to expand with robust momentum in the second quarter of 2017.



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**ECB looks only at core inflation at this point:** The ECB will welcome the firmer and probably lasting recovery of the Eurozone. But for the ECB it is only about inflation, in particular the core reading. Core inflation has shown some life rising from 0.9% yoy in January to 1.2% in July. Recently, ECB President Draghi sounded slightly more confident that underlying inflation will respond to the resilient recovery. At the next two meetings on September 7 and October 26 the Governing Council will have fresh staff projections and 1-2 more inflation numbers. The challenge going forward will be to start to discuss trimming the monthly asset purchases while remaining dovish in tone. A further euro appreciation could imply a fall in the ECB's inflation projections and, especially if the 2019 and beyond forecasts are affected, a slower pace or a later start of tapering. Since the exchange rate has stabilised recently it may, however, not be such an issue after all. In any case, the ECB can stress that even in a tapering world or one without QE, the stance will remain very accommodative for a long time. We do not expect the ECB to change its main policy rate, the refi rate, before September 2019. We expect the ECB to reduce its asset purchases from a monthly rate of €60 bn to €45bn as of January 2018 and scale back the asset purchases in further steps of €15bn every three months thereafter.

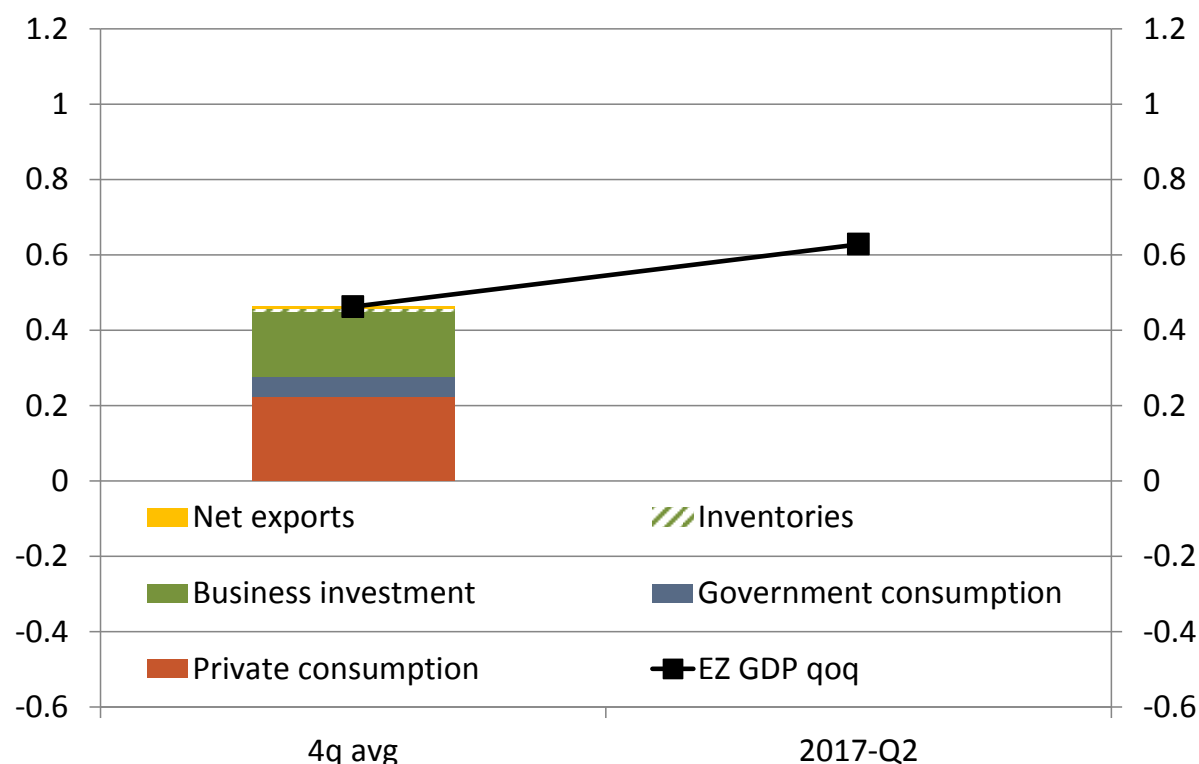


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Chart: Eurozone GDP (qoq, in %) – 4-quarter average including contributions to GDP growth versus Q2



The 4 quarter average is taken of the four quarters 2016 Q2-2017 Q1. Sources: Eurostat.

### Eurozone GDP (in %)

	Q2 17	Q1 17	Q4 16	Q3 16	Q2 16	Q1 16
qoq	0.6	0.5	0.6	0.4	0.3	0.5
yoy	2.1	1.9	1.9	1.7	1.7	1.7

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