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EUROZONE PMIS: BOTTOMING OUT?

Berenberg Macro Flash

Eurozone PMI, February

	Composite	Services	Manufacturing
Actual:	**51.4**	**52.3**	**49.2**
Previous:	51.0	51.2	50.5
Consensus:	51.1	51.3	50.3
Berenberg:	50.9	51.2	50.0

Spring may be in the air …: Driven by stronger activity among domestically-oriented services in Germany and France, the Eurozone PMI composite edged higher from 51.0 to 51.4 in February (see chart 1). Although still close to the stagnation level of 50, the first gain since last August adds to the evidence provided by this week's slightly better German ZEW expectations and Eurozone consumer confidence that the Eurozone economy may soon hit bottom. Although the grey winter is not over yet, the stability of the service sector supports our hope that spring could indeed be brighter. While new orders were in contraction territory for a second consecutive month, led by factory order books, they did not drop further, but instead rose slightly.

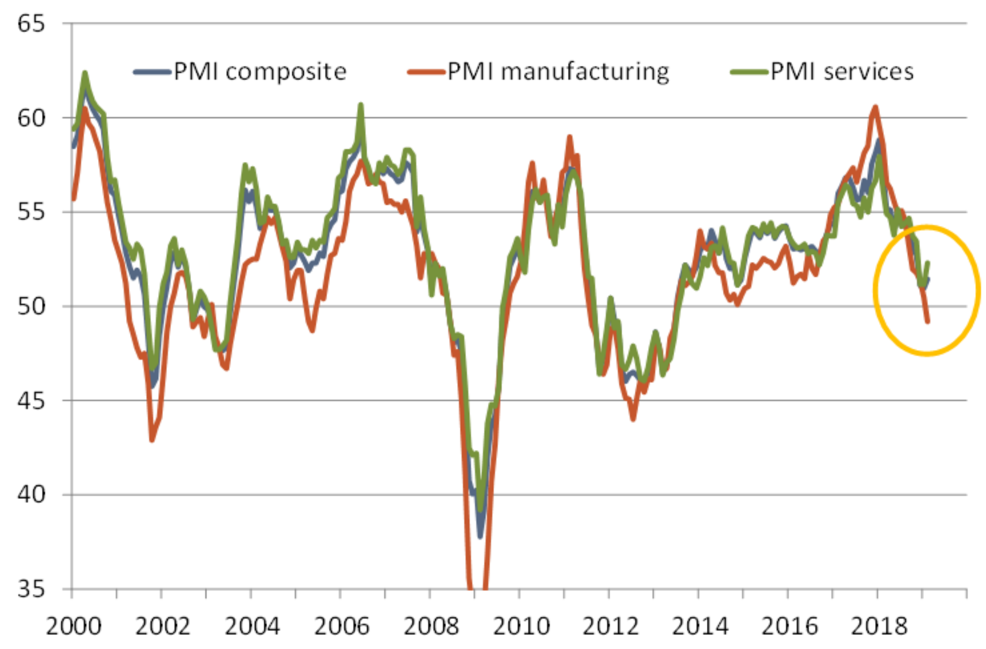
… but still a few weeks to go, at least: These are just the first positive signs. We probably need real circuit breakers to bring the economy back on track. It will take some easing of trade tensions – both between the US-Chinese and US-EU, less negative news out of China and the UK to avoid a hard Brexit. These three conditions could be met at some time this spring. Until and unless this is the case, Eurozone data, driven by weak manufacturing will continue to disappoint. We have to brave ourselves for a weak Q1. After 0.2% qoq in both quarters of H2, GDP growth will probably be a notch lower this quarter (0.1%). Despite today's rise in the PMI, the average for January and February of the PMI (51.2) is below the Q4 level (52.3). After a still subdued second quarter (0.3%), Eurozone growth could return to its potential rate of around 0.4% in the second half of 2019 (see chart 2). Stronger wage growth, continued employment gains and confidence should underpin private consumption and domestic demand (see charts 3, 4 and 5). Still, our Eurozone growth forecast of 1.1% for 2019 remains well below consensus (1.4%).

The two worlds of Germany: The cross-sector divide is getting more extreme in Germany. A very strong showing of service providers (up from 53.0 in January to 55.1 in February) covered up the worst slump among manufacturers in over six years (down from 49.7 to 47.6). The PMI composite edged higher for a second month (up from 52.1 to 52.7). Given their domestic orientation, services do very well amid a solid labour market, rising disposable incomes and stable household consumption. Meanwhile, manufacturers, particularly, those that sell big-ticket items overseas, are faring ever more badly in a very challenging external environment. The survey cited "uncertainty relating to US-China trade tensions and weakness in the autos industry" as a driver for the lowest reading of order books since August 2012. The renewed fear of car tariffs may have contributed even more. That German manufacturers continue to create jobs is a positive, but may also owe to employers' fears that once they lay off part of their work force, it will be tough to rehire if the outlook starts to improve again with the labour market at full employment.

Positive news from France: After dropping sharply in December and surprising in January with a further fall, the French PMIs recovered in February (49.9 after 48.2 in January) amid a strong boost from services (up from 47.8 to 49.8). The yellow vest movement is losing momentum in response to Macron's sweeteners, the fall in pump prices and some revulsion against the violent fringes of the protest movement. Stronger employment gains and only a marginal decline in new orders suggest that after the highly visible effect in late 2018, the economic impact from the social unrest will likely fade in Q1. While the domestic environment is turning less challenging, it will take a few months before the economy is back on track. Essentially, the yellow vest protests will have to stop and the external headwinds start to blow less forcefully.

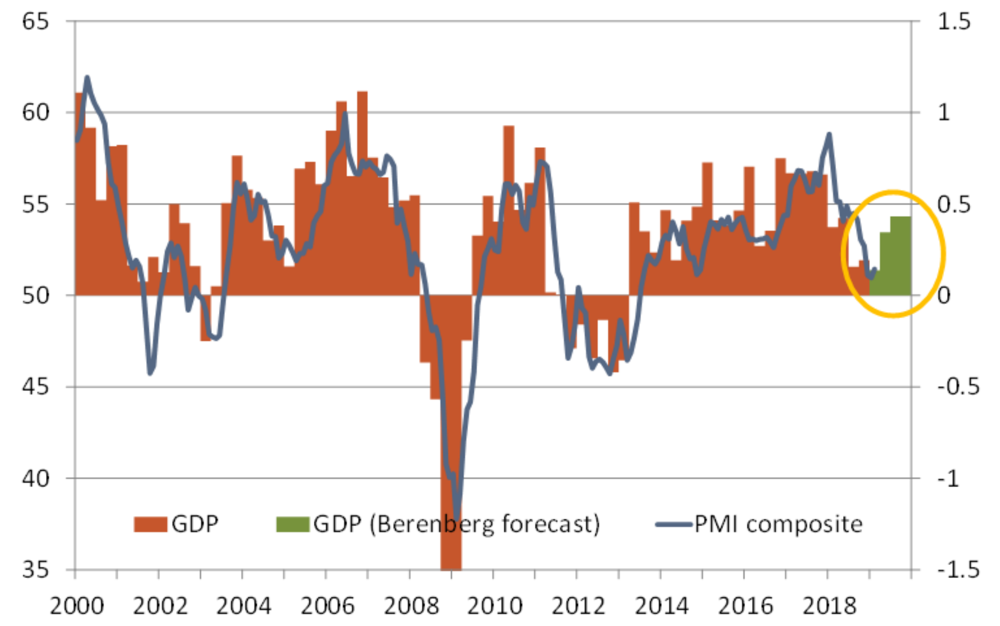
The rest of the Eurozone suffered the "worst spell since late 2013" according to the PMI press release. Italy was probably a big factor once again, with renewed political uncertainty weighing on Spain after gains in January.

Chart 1: Eurozone PMI manufacturing and services



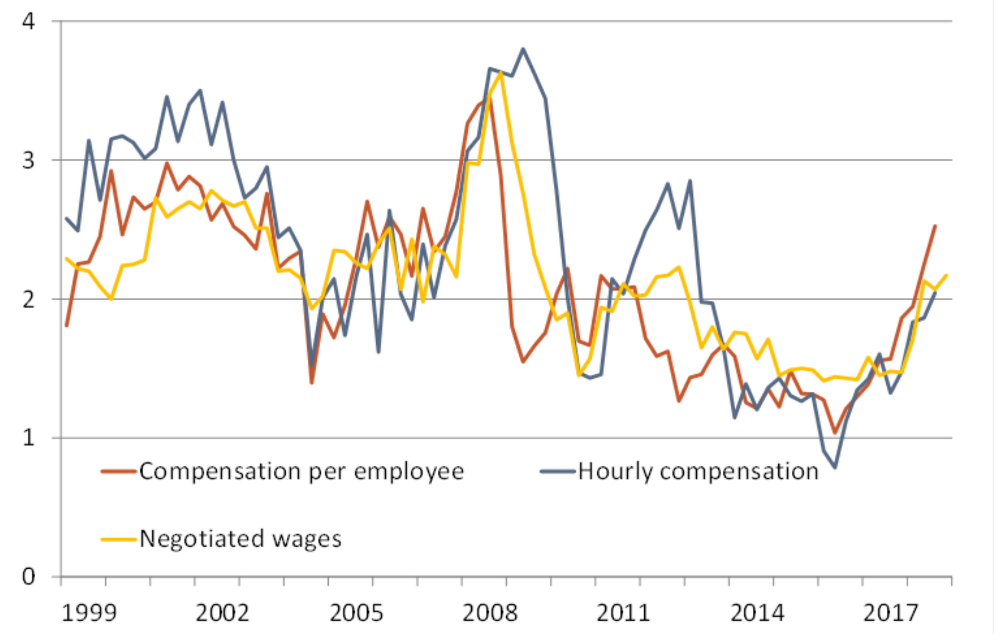
Source: Markit

Chart 2: Eurozone PMI composite versus GDP (qoq, in %)



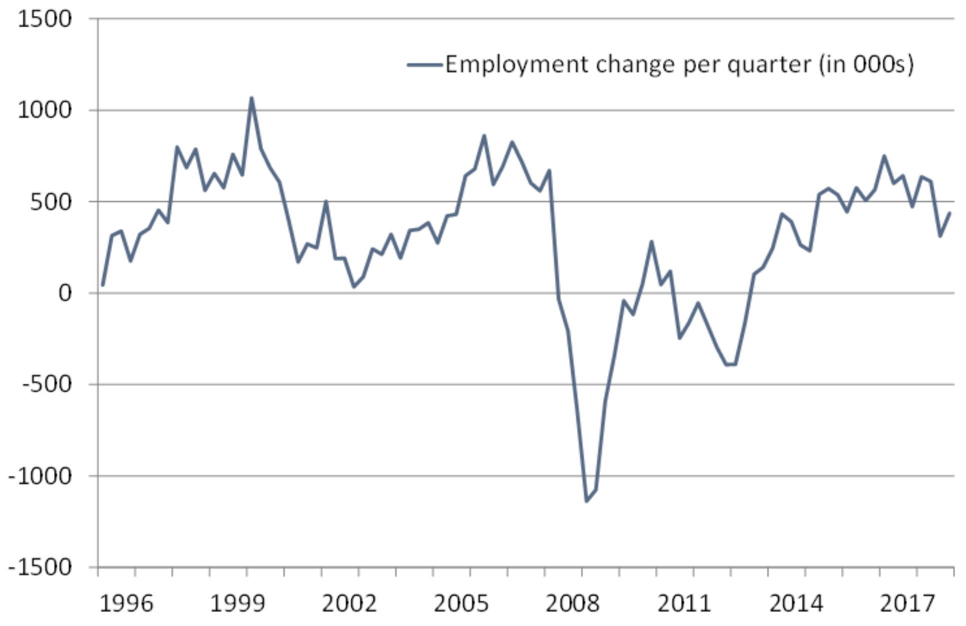
Source: Markit

Chart 3: Eurozone negotiated wages, compensation per employee and hourly compensation (yoy, in %)



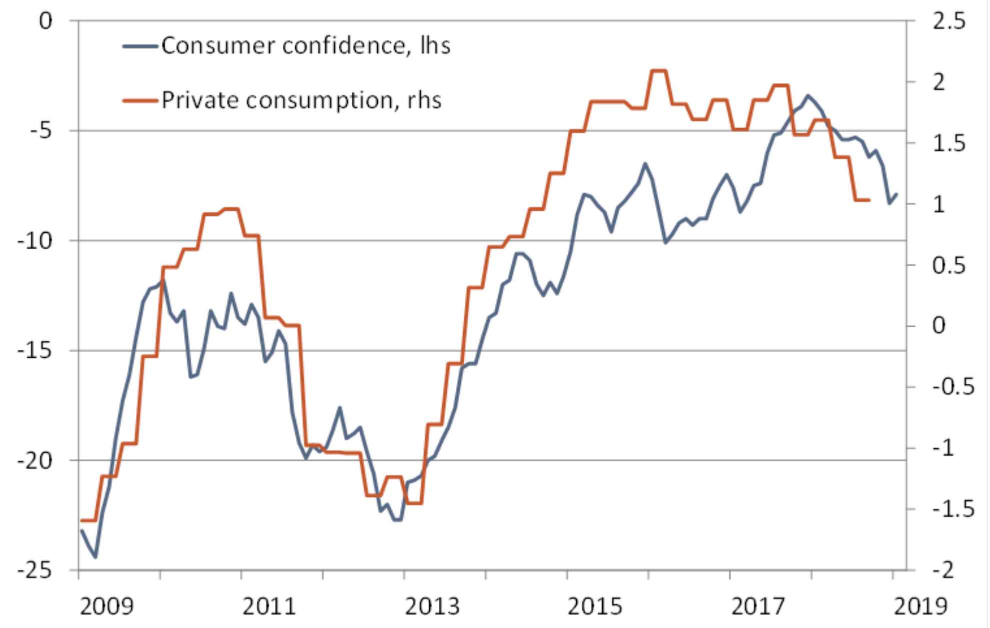
Source: ECB

Chart 4: Eurozone employment growth (analogue to US non-farms payrolls)



Qoq change in thousand people in employment. Source: Eurostat

Chart 5: Eurozone consumer confidence and private consumption (yoy, in %)



Index level for consumer confidence. Yoy change of (real) private consumption in %. Sources: European Commission. Eurostat