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EUROPEAN REBOUND PROBABLY UNDERWAY DESPITE STILL-WEAK PMIS

Berenberg Macro Flash

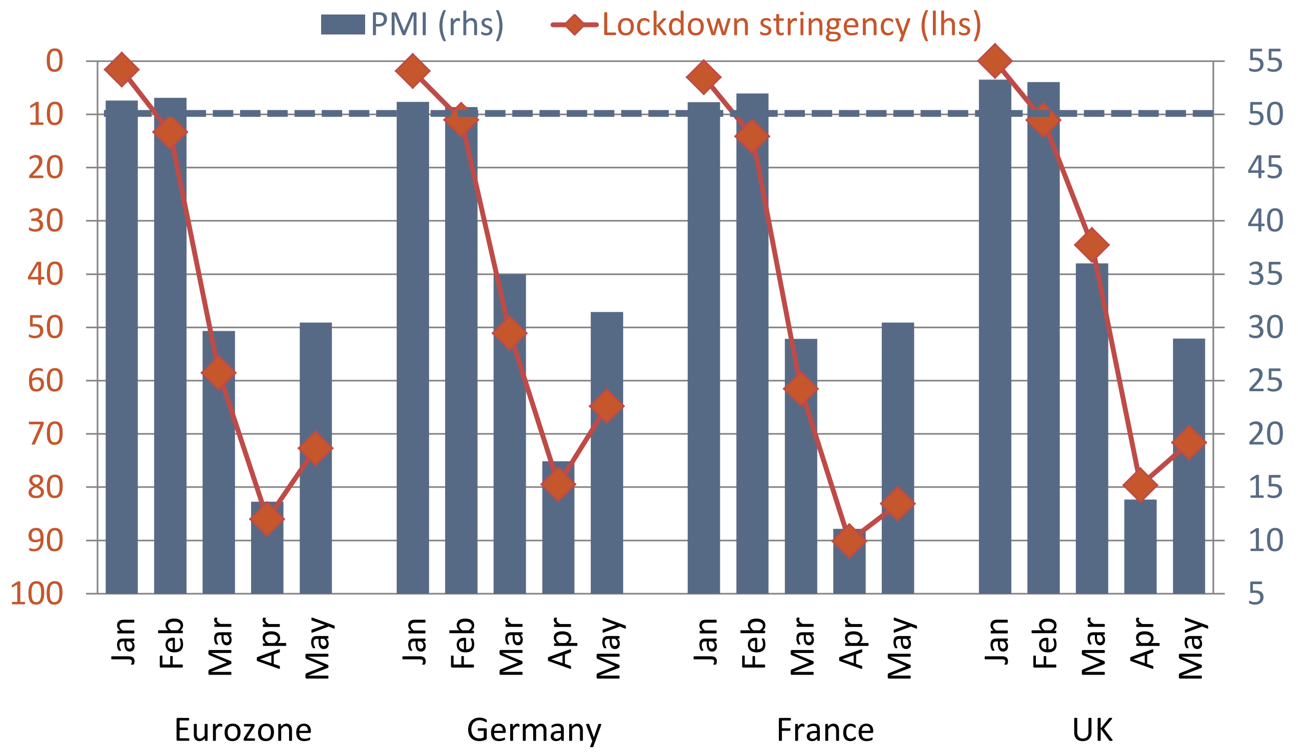
Not much improvement - what is going on? Today's May PMI data for Europe are difficult to interpret. While the headline indexes picked up a bit in May from the record lows in April across most countries and sectors, they remain well below the 50 mark which typically indicates no change in output versus the previous month. Taken at face value, the surveys suggest a mere slowdown in the torrid pace of economic decline in May rather than the start of an economic recovery. The data seems implausibly pessimistic, in our view. Weighed down by the weak sentiment in the real economy and still-subdued activity relative to normal times, the May PMI are probably hiding the modest rebound that is underway across major parts of the continent already. Many respondents to the survey may have indicated that output and the inflow of orders remain depressed rather than really answering the question whether May was better or worse than April. A host of survey and daily data suggest that economic activity has picked up a little in May from the April low as countries have started to ease their lockdowns.

Keeping in mind the caveats, we can still draw two key conclusions from the PMI data:

- **Output trends roughly in line with the pace at which countries are re-opening:** Germany's headline index rose to 31.4 from 17.4. France, which is roughly three weeks behind Germany with its easing of lockdowns, came in lower than Germany but from a much lower starting point (30.5 from 11.1). In the UK, which is around three weeks behind France and six weeks behind Germany – but introduced its lockdown later, the composite index increased to 28.9 from 13.8.
- **Manufacturing continues to do better than services:** While all sectors, apart from healthcare and some of its related industries, have fared badly in the coronavirus recession – producers have done less badly than retailers, restaurants and other consumer facing services industries. Looking across the major regions (April data in parentheses): Eurozone – 35.4 (18.1) for manufacturing output and 28.7 (12.0) for services; Germany – 31.5 (19.7) for manufacturing and 31.4 (16.2) for services; France – 35.3 (15.1) for manufacturing and 29.4 (10.2) for services; and the UK – 34.9 (16.3) for manufacturing and 27.8 (13.4) for services.

Still on track for a tick-shaped recovery: The progress in gradually lifting the lockdowns and restarting economic activity remains tentative and subject to potential reversals. But major European economies including Germany, France and Italy have made clear progress while keeping there virus trends under control. The UK lags the other major European economies. But ahead of the planned re-opening of non-essential in-store retail on 1 June, the UK is already returning to work in some key areas such as manufacturing and construction. Crucially, the current progress across the whole continent remains in line with our underlying assumptions for a tick-shaped rebound in Europe – that is, the sharp downturn in Q1 and Q2 will be followed by a somewhat flatter upturn that ultimately raises GDP back to the pre-corona level of GDP some two years after the Q2 2020 trough. Reflecting further gains in economic activity in the coming weeks, the PMIs for June could improve more noticeably.

Chart 1: Tightness of lockdowns and European PMI composite indices



Oxford University lockdown stringency indices, 0 to 100 (most stringent), left-hand scale, inverted; PMI of 50 = no change versus previous month, right hand scale. To estimate a likely average degree of restrictions for May, we assume that each country will gradually remove its current (18 May) restrictions over the rest of May at the same pace as they did so far during May. Sources: Markit, Oxford University Covid-19 tracker, Berenberg.

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