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29/06/20

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EUROZONE SENTIMENT: RECOVERY UNDERWAY

Berenberg Macro Flash

Further progress ...: The strong rebound in the European Commission's gauge for economic sentiment finishes off two weeks of major European survey releases for June. They show that the recovery from the Covid-19 mega-recession is firmly underway. After edging higher by only a tad in May, the index that combines business and consumer confidence jumped by 8.2 points to 75.7 in June from 67.5 in May and April's all-time low of 67.0 (see Chart 1). It was the biggest mom gain since the series started in 1985.

... but a little disappointing: Despite breaking a record, the June rebound was a little underwhelming relative to expectations and previous losses. Unlike the ZEW, PMI and Ifo surveys, the economic sentiment index surprised to the downside (Reuters consensus: 80 points). The increases in May and June recover only 28% of the combined plunge from March-May (down by 38.6 points). That the index for economic sentiment is still 27.7 points below the pre-crisis high of 103.4 in February highlights how long the journey back to normality is. The European Commission's sentiment index includes some backward-looking components. This partly explains why it first responded slower to the deteriorating environment, and now takes a little longer than the other surveys to recover.

On track for tick-shaped recovery: Like the survey data for activity (PMI) and business conditions (ZEW and Ifo), the European Commission's economic sentiment index is currently more difficult to interpret than usual. The comparison of the current levels with the pre-crisis or the trough levels in April may provide less value than in more settled times. For example, not all respondents may rate a change from extremely bad (April) to still bad (May, June) as an improvement.

Judging by high-frequency indicators, we think the rebound over the past two months from the extremely depressed levels of activity in April has been more pronounced than the 28% rebound of the sentiment index from its March/April plunge would suggest. Although current economic activity remains c15% below pre-crisis levels, in our view, it is well up from the c30% shortfall in April as supply and production facilities have been switched on again. In the absence of a huge virus-related setback in major economies that would trigger harsh and widespread rather than modest and regional new restrictions (as currently in the US), the advanced world remains on track for a [tick-shaped recovery](#). In our view, economic output in the Eurozone can return to the pre-crisis level some two years after the Q2 2020 trough.

Differences by country and sector: The change in economic sentiment over the past months largely mirrors the extent to which countries enacted lockdown measures in March and April and relaxed them over the past two months. As fewer shops and factories were closed during Germany's somewhat lighter lockdown, sentiment fell less in Germany than in France and Italy. As the German lockdown measures were lifted from mid-April onwards rather than throughout May, as



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in many other countries, German sentiment recovered more significantly already in May. In June, France and Italy started to catch up with Germany. Sentiment in Germany rose by 6.6 points, in France by 9.4 points and in Italy by 8.2 points in June. Sentiment in Spain, which soured less than in Germany from February to April and recovered as much during May and June, is now the least depressed relative to the long-term average of 100 among the four big Eurozone countries at 83.1 – versus 81.9 in Germany, 77.1 in France and 71.2 in Italy (see Chart 2). A resumption of European travel probably plays a role for Spain, which heavily depends on foreign tourists.

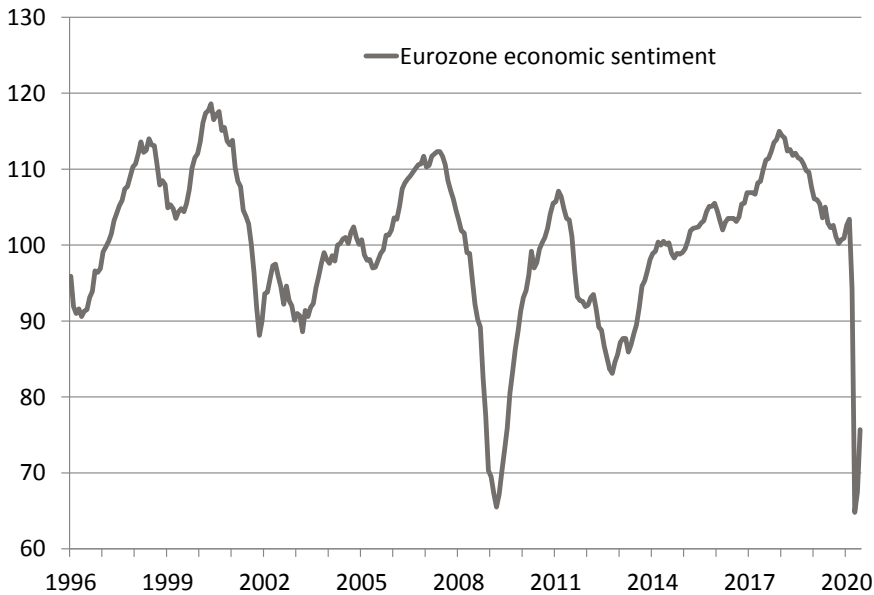
Both consumer and business confidence rose in June in the Eurozone (see Chart 3). Consumers grew more confident about the general economic conditions, their own future financial situation and major purchases (see Chart 4). This should support household consumption going forward. Reassuringly, the rise in business confidence was broad-based across sectors after softer sentiment in May among service providers and construction companies had offset gains in the manufacturing sector. Significantly less negative production expectations drove sentiment among manufacturers higher. Order books still weigh on sentiment in that sector (see Chart 5). Businesses seem to be holding back on investments. Export orders dropped slightly further in June to -49.7 after -47.7 in May, but remained well above the record low of -63.8 at the trough of the post-Lehman crisis in March 2009. Rising stocks of finished products also dampen the overall rebound in manufacturing.

Consumer facing service providers, who had been hit most harshly by the lockdowns in March and April, now benefit more than other sectors from the easing of social distancing measures. Driven by a rebound in demand expectations, the services confidence indicator rose by 8 points to -35.6 in June relative to a 5.8 points gain among manufacturers to -21.7 and a 4.9 points increase in the construction sector to -12.4. Despite the rebound, confidence in the services sector still has the longest journey to a full recovery: relative to February, sentiment in this sector is still 46.7 points lower than it was in February relative to gaps of 17.8 points in construction, 15.5 points in manufacturing and a shortfall of 8.1 points for consumer confidence.



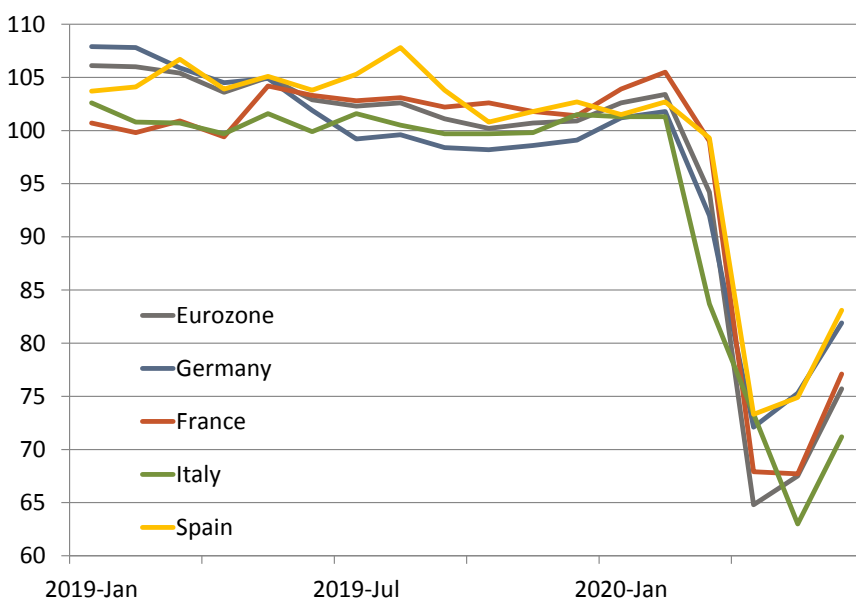
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Chart 1: Eurozone economic sentiment



In %. The percent balance equals percent of respondents reporting an increase minus the percent of respondents reporting a decrease. Source: European Commission, Berenberg

Chart 2: Eurozone economic sentiment by country

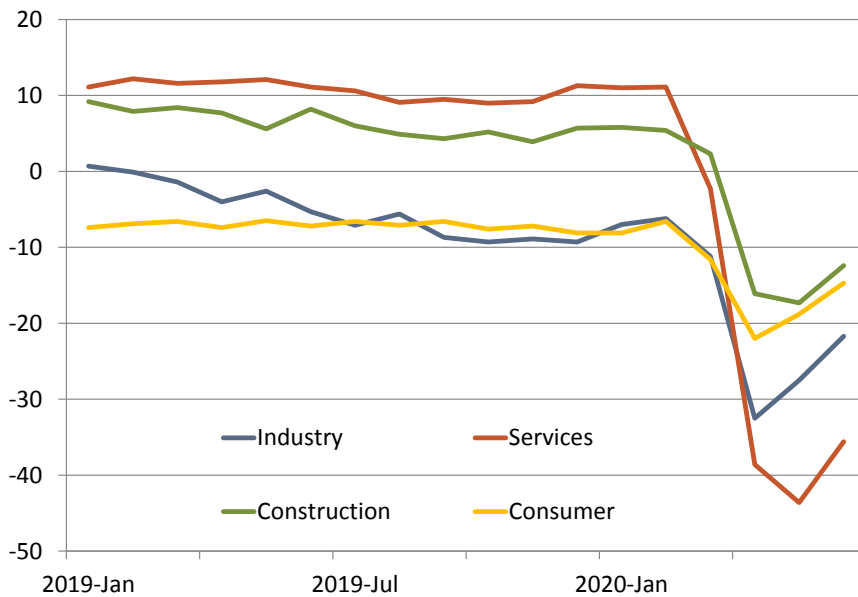


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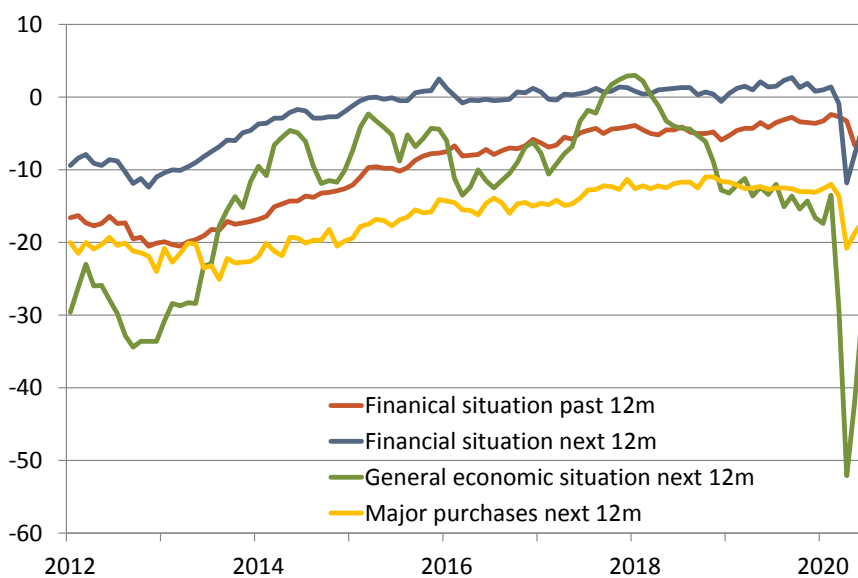
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Chart 3: Eurozone economic sentiment by sector



In %. The percent balance equals percent of respondents reporting an increase minus the percent of respondents reporting a decrease. Source: European Commission, Berenberg

Chart 4: Components of consumer sentiment

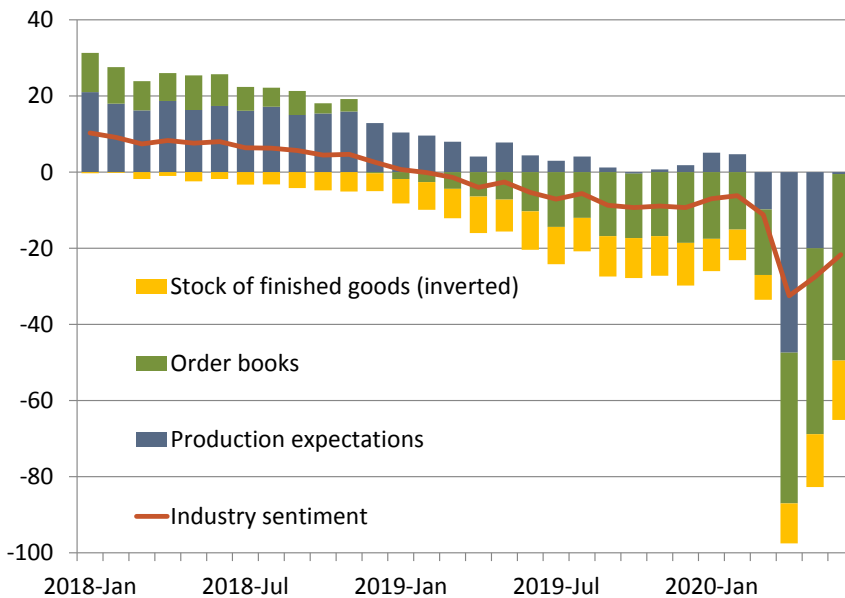


In %. The percent balance equals percent of respondents reporting an increase minus the percent of respondents reporting a decrease. Source: European Commission, Berenberg



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Chart 5: Industry sentiment by components



In %. The percent balance equals percent of respondents reporting an increase minus the percent of respondents reporting a decrease. Source: European Commission, Berenberg

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