Christopher Dembik, Senior European Economist | christopher.dembik@berenberg.com | +336 01 44 43 60

# EUROZONE PMI: BETTER THAN EXPECTED BUT RISKS ARE LOOMING

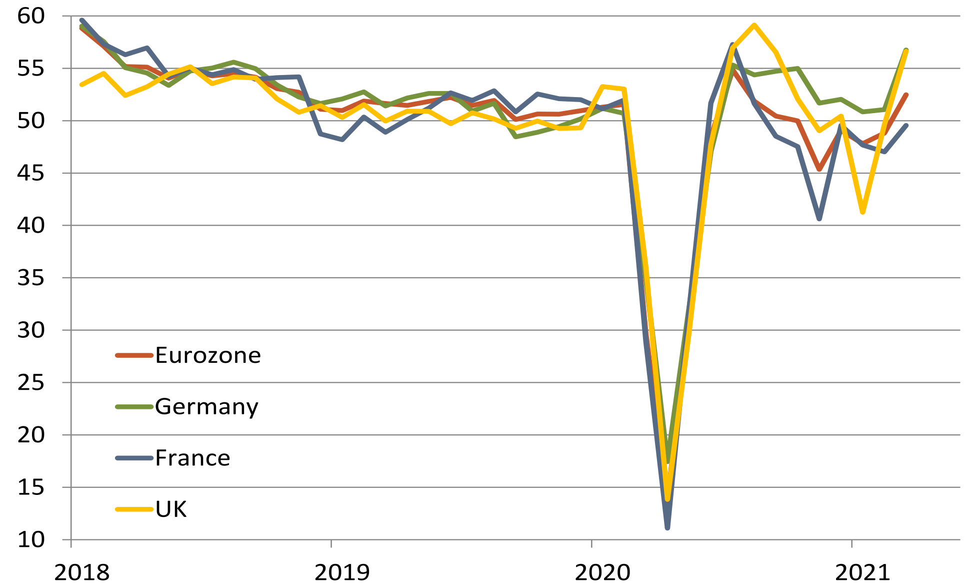
## Berenberg Macro View

**A nice surprise:** March's flash PMI data from IHS Markit showed a broad improvement in the manufacturing and the service sectors across the main European economies. Eurozone business activity returned to growth for the first time in six months. The composite PMI rose to 52.5 from 48.8 in the Eurozone, to 49.5 from 47 in France and to 56.8 from 51.1 in Germany. In the UK, the rapid vaccination progress contributed to a surge in the composite PMI to 56.6 from 49.6 led by the fastest increase in UK service activity since August 2020. A level above 50 signals an expansion and a level below 50 signals a contraction. The goods-producing, export-oriented manufacturing sector is still benefiting from the recovery in global demand mostly fuelled by the US and China. Manufacturing continues to limit the damage from the pandemic to the overall economy. The PMI manufacturing indices advanced strongly in March (Eurozone: 62.4 after 57.9 – a record high since June 1997; Germany: 66.6 after 60.7 – a record high since April 1996; France: 58.8 after 56.1 – a 39-month high, UK: 57.9 after 55.1 – a 40-monnth high). Unsurprisingly, services continue to lag the rebound in manufacturing in the Eurozone. While the recovery in the manufacturing sector accelerated, the service sector, which partly relies on face-to-face interactions, remains constrained by stay-at-home orders and forced closures implemented to curb the pandemic. However, the modest easing of virus containment in several countries in February and early March led to a slower rate of contraction in the service sector in the Eurozone, at 48.8 after 45.7. In Germany, the PMI services index moved into growth territory for the first time since September 2020, reaching 50.8 from 45.7 in February.

**Risks are still looming:** Markit conducted its flash survey between 12-23 March. Most responses were collected prior to the extension and tightening of further restrictions in many European countries to contain the third wave of the pandemic (think four-week lockdown in France and in Italy and extension of the semi lockdown in Germany and the Netherlands until at least the third week of April). Therefore, the pick-up in business optimism in the service sector is likely to be at least partly reversed in the coming weeks. In addition, inflationary pressure continues to intensify, led by a near-record rise in manufacturing input costs as raw material shortages deteriorated further. But it should have limited negative impact on consumer spending, in our view. As risks are titled to the upside in the short term, we reduced our 2021 GDP calls last week to 4.1% from 4.4% for the Eurozone with similar changes for Eurozone member countries (for details, see Forecast at a glance). The German economy may expand by 3.5% instead of 4.0% this year. We look for France's 2021 GDP growth to reach 5.3% against 6.4% in our previous projection.

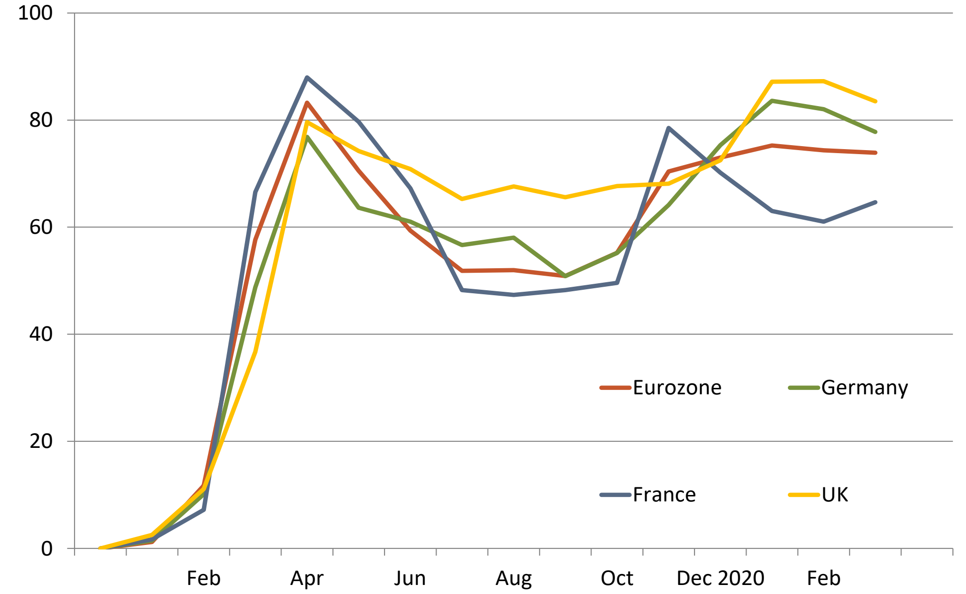
**A bright future once the pandemic fades:** Despite the hit to economic activity in Q1 and the delayed re-opening of Eurozone economies, businesses remain optimistic for the year ahead. The expected acceleration in vaccine rollout and its positive impact to hospitalisation rates in the UK and in Israel give every reason for optimism. We expect restrictions in most European economies to be gradually lifted from the second half of April onwards. Households who cannot spend as much as they want will be able to spend a little more. This should ultimately support an increase in demand from Q2 onwards. If the pace of vaccinations accelerates in line with current projections for vaccine supply, summer should be more normal again. The delayed re-opening of the Eurozone economies pushes more of the projected rebound into 2022. In addition, consumers are now building up more excess savings. They will thus have more money to spend later on. Upon reducing our growth forecast for 2021, we have thus raised our call for Eurozone GDP growth in 2022 to 4.7% from 4.3%.

**Chart 1: European composite purchasing managers' indices (PMIs)**




*50=no change. Source: Markit, Berenberg*

Chart 2: Lockdown 2.0 stringency across major European countries




*Oxford University lockdown stringency indices, 0 to 100 (most stringent). Oxford University collects information on policy responses (containment and closure, economic and health system policies), scores their stringency and aggregates scores into a stringency index. Source: Oxford University, Berenberg*