ECONOMIC PULSE

EUROZONE: GLOOMY SEPTEMBER, DOUBLE-DIGIT INFLATION, MARKED DETERIORATION IN CONFIDENCE SURVEYS

Dark clouds are continuing to gather over the Eurozone economy. The first set of data available for September is not positive and this can be seen in our Pulse. Looking at the survey data, the blue area (recent conditions) is shrinking when compared to the dotted line (conditions four months earlier) and even, on some indicators, when compared to the grey dodecagon (the long-term average). The opposite is true for the inflation data.

In fact, inflation reached a new level, at 10% y/y in September according to Eurostat's preliminary estimate. Not only did inflation reach double figures – which was predictable, but still bad news – but its 0.9-points rise compared to July was broad-based across all its main components. The increase in manufactured goods prices contributed 0.1 percentage points, services prices 0.2 and the energy and food components 0.3 each. Admittedly, the further rise in inflation was not broad-based across all the Member States in the Eurozone. Inflation actually fell in six of them, by an average of 0.8 points. This was not insignificant, but insufficient when compared to the average increase of 1.1 points in the thirteen other countries, whose weight is larger. France continues to stand out by having the lowest inflation rate in the Eurozone (6.2% y/y), down 0.4 points from July. Inflation also fell significantly in Spain (by 1.2 points to 9.3% y/y, bringing it back below the 10% level). But the further rise in inflation in Italy (+0.4 points, to 9.5% y/y) and particularly in Germany (+2.1 points, to 10.9% y/y) had a bigger impact.

Will September see inflation peak in the Eurozone? There is still a great deal of uncertainty. What is a lot less uncertain (or even is certain) is that inflation will take a long time to return to the 2% target. By the end of 2023 we expect inflation to still be above 3% year-on-year, and by the end of 2024 it should be around target, keeping in mind that these forecasts are accompanied by a clear upward risk. In view of this situation, we now think that the ECB will not stop raising its key rates once the estimated neutral level has been reached (2%) but that it will continue to raise them, bringing them into restrictive territory (3% for the deposit rate). The cumulative increase by the end of the year should reach 150 bps (two +75 bps increases, in October and December, rather than +75 bps and +50 bps) and is likely to extend into Q1 2023 (+50 bps in February, +25 bps in March).

This enforced monetary tightening will take place while the economy appears to be heading into recession. The European Commission's surveys for September point in this direction, along with the PMIs (slightly below the 50 threshold since July for the composite index). Like inflation, the further deterioration in the Commission's Economic Sentiment Indicator (ESI) in September was not only substantial (-4 points over a month) but also broad-based across all business sectors (as in July). Based on past experience, periods when such a widespread fall is observed tend to coincide with recessionary phases. At the present time we have only two such observations, but the drop is significant and we can expect it to recur over the next few months.

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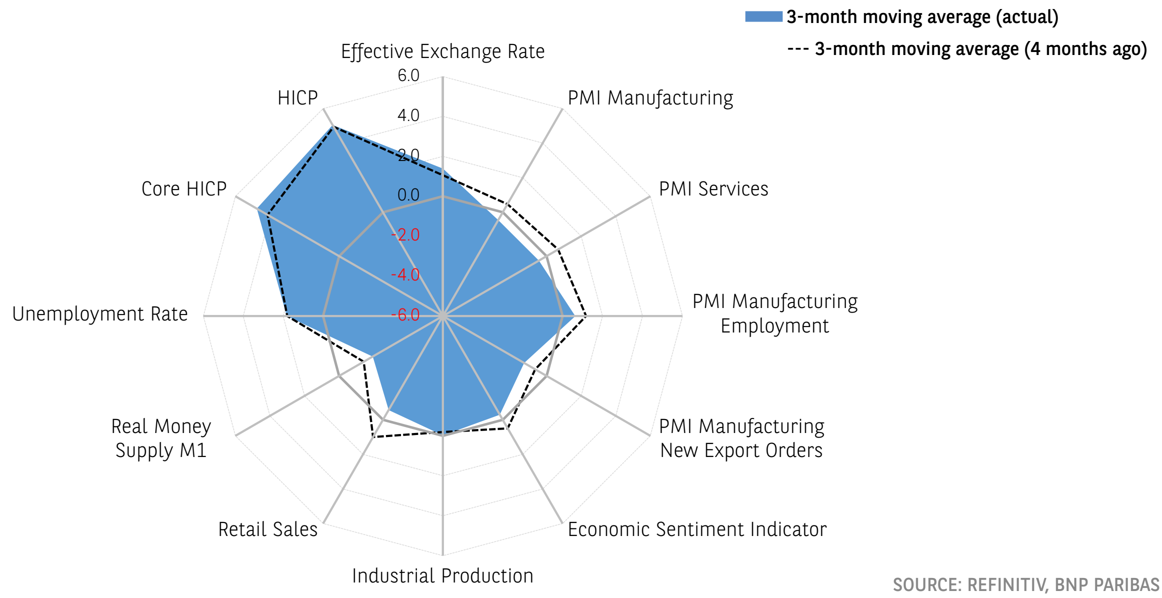
EUROZONE: QUARTERLY CHANGES



SOURCE: REFINITIV, BNP PARIBAS

The indicators in the radar are all transformed into 'z-scores' (deviations from the long-term average, as standard deviations). These z-scores have mean zero and their values are between -6 and +6. In the radar chart, the blue area shows the actual conditions of economic activity. It is compared with the situation four months earlier (dotted-line). An expansion of the blue area compared to the dotted area signals an increase in the variable.