

# Economic Watch

## Eurozone

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Economic Analysis

Europe

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## Slight downward bias for growth in the fourth quarter

### Eurozone: activity data worse than expected but inflation recovers somewhat

- **GDP growth confirmed at 0.1% q/q in 3Q13, with weak exports**

Net foreign demand weighed negatively on quarterly growth due to the strength of imports and the stagnation of exports. The negative contribution (-0.3pp) was offset by a positive contribution of domestic demand (+0.4pp), with both private consumption and investment growing mildly and an upward surprise stemming from public consumption and, especially, inventories (Chart 1).

- **Confidence indicators up to November are consistent with GDP growing at a moderate pace by year-end**

Data from the EC's confidence survey (ESI) and PMIs are showing mixed signs in the fourth quarter (Charts 3 and 4). ESI figures remain on an upward trend, though at a slower pace than before. In contrast, the composite PMI deteriorated again in November, due to the worsening in confidence in the service sector thus pointing to a weak domestic demand. Still, PMI indices remain in expansionary territory. Overall, these confidence figures confirm that the recovery in the eurozone is slow, led only by Germany and with disappointing figures for France (see below).

- **Activity indicators at the beginning of 4Q13 are somewhat disappointing**

The hard data published for 4Q and the inertia from the end of 3Q point to a weak environment. Industrial production and retail sales fell in October (Charts 5 and 6), suggesting that the recovery is still fragile. Nonetheless, the stabilization in the labour market (Charts 9 and 10) along with subdued inflation (Chart 12) should end up supporting households' spending.

- **The MICA-BBVA model suggests that the recovery could have gained some traction by year end (+0.2 % / +0.3 % q/q).**

Despite the worse-than-expected hard data, our model for short-term projections continues to point to a growth between +0.2% and +0.3% q/q in 4Q13 (Chart 2), similar to what we incorporated to our projections in our last Europe Economic Outlook (which imply average negative growth of -0.4% this year and a recovery of +1.1% in 2014). We think, however, that there are downward biases to this projection for the last quarter given the inertia of recent data.

- **Inflation is likely to remain subdued in the medium term**

The preliminary estimate of harmonized inflation stepped up by 0.2pp to 0.9% y/y in November (Chart 12), slightly more than expected (0.8%), due to a more moderate fall in energy prices, but also to a higher-than-expected inflation in services that could result in core inflation at 1.1% y/y. The upward surprise in November is moderate, but nonetheless is good news as it counters fears of deflation triggered last month after October inflation decreased by 0.4pp to 0.7% (we expected then 0.9% but many analysts were expecting 1.1%). Looking forward, we see inflation increasing further in December (to 1% or 1.1% y/y), but it is likely to slow again early next year, hovering slightly above 1% the rest of the year. Now we expect average inflation for 2014 close but slightly above 1%, though we continue to think that a strong disinflationary process is unlikely throughout next year.

## Germany: leading the recovery in the eurozone

- **Significant improvement in confidence so far in 4Q13**

Soft data improved markedly in November (Charts 15 and 16), especially PMIs, mostly driven by better expectations in the service sector, suggesting that domestic demand could have remained robust in 4Q13 (after contributing with 0.6pp to quarterly GDP growth in 3Q13). Note that the composite PMI remains at levels similar to those observed by mid-2011, when GDP grew at around 0.5% q/q. In addition, the improvements in the export orders subcomponent of PMIs, along with data from trade balance in October (Charts 19 and 20), suggest that net exports could be contributing positively to growth again by year-end.

- **Disappointing activity data in October**

Retail sales dropped more than expected, while industrial output declined again in monthly terms (Charts 17 and 18), after the significant drop registered in September, somewhat in contrast to soft indicators. But consumers and industrial expectations have also improved in recent months, suggesting that hard indicators should be improving by the end of the fourth quarter. Still, our forecast of 0.5% q/q for the quarter is too positive now, and we envisage growth closer to 0.2%/0.3%.

## France: recent data not very positive

- **GDP contracted slightly in 3Q13, below expectations**

GDP fell by -0.1% q/q in 3Q13, after the rebound observed in 2Q13 (+0.5%) (Chart 25). The slowdown in private consumption and the decline in investment resulted in a neutral contribution of domestic demand, after +0.4pp in 2Q13. However, the above was partly offset by a strong contribution from inventories (+0.5pp). The sharp decline in exports, along with the stabilization of imports, resulted in a negative contribution of external demand (-0.7pp after neutral contribution in 2Q13).

- **Recent confidence data have worsened but we still expect positive growth in 4Q13**

Soft indicators unexpectedly declined in October and November (Charts 27 and 28), with PMIs returning again below the 50 points threshold. The deterioration in confidence was widespread across sectors. Nonetheless, activity data for October did not reflect such a large decline (Charts 29 and 30), with retail sales and industrial output remaining virtually flat. Overall, we expect GDP to grow slightly in 4Q13 (around 0.2% q/q), but with a downward bias (Chart 26).

## Italy: slowly emerging from recession

- **GDP stagnated in 3Q13, but only thanks to inventories**

Despite the upward revision to quarterly GDP growth (0% from a first estimate of -0.1% q/q), the detailed breakdown showed that private consumption and investment weighed negatively on activity, while exports grew at a more moderate pace than imports (Chart 37).

- **Even though latest soft data lost ground, hard data suggest that activity is gaining some traction by year-end**

After the significant improvement of soft data in September, confidence lost ground again in October and November (Charts 39 and 40), driven by worsening expectations in the service sector, while the outlook for the industrial sector remains more upbeat. Retail sales fell in November, but industrial production in October was strong (Chart 41), and stands 0.7% above the average of 3Q13. We continue to expect slight growth in 4Q13 (around 0.1% q/q), but with a downward bias (Chart 38).

## Spain: robust exports and revival private demand

- **Exports slow, but private domestic demand starts to revive**

Regarding foreign demand (Charts 55 and 56), firms' expectations (exports orders) and spending data (foreign sales of large companies) suggest that exports are likely to slow again in 4Q13, but remaining robust. In addition, data on foreign tourism seem to remain in an upward trend, confirming the strong increase observed over the year.

Some indicators of private demand (car registrations and consumers' confidence) show further evidence of an improvement in households' consumption in 4Q13, though retail sales in October were disappointing (Chart 54). Overall, the more positive data was also felt on the labour market (Charts 57 and 58), as registered employment from social security increased while registered unemployment declined (-1.4% t/t s.a.).

- **Economic recovery remains on track in 4Q13 (+0.3% q/q)**

Data available for 4Q13 suggest that, after emerging from recession in the previous quarter, the economy could have gained some traction by year end. The MICA-BBVA model estimates a quarterly GDP growth of +0.3% q/q (Chart 50), in line with our scenario and thus consistent with an annual GDP fall of around 1.3% in 2013 as a whole.

## Eurozone

### National accounts: positive contribution of domestic demand offset export weakness

Quarterly GDP growth slowed by 0.2pp to 0.1% q/q in 3Q13. The MICA-BBVA model estimates a quarterly GDP growth between +0.3%/+0.2% q/q in 4Q13, in line with our scenario. Data for the last quarter are still limited, so we think that there are downward biases to this projection.

Chart 1  
GDP (%q/q) and contribution by components (pp)\*

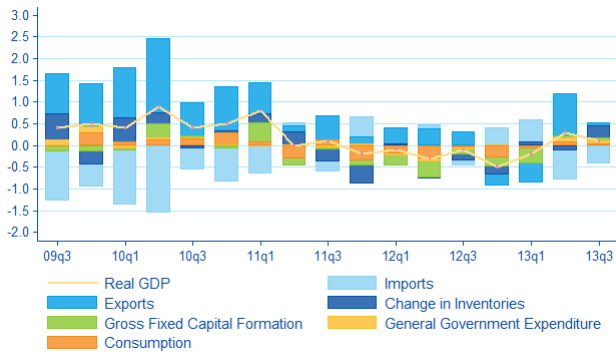
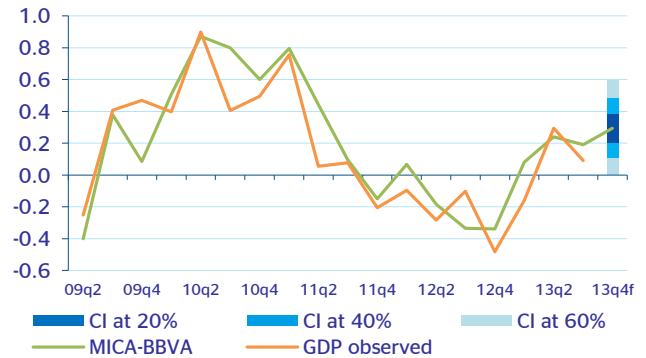


Chart 2  
GDP growth (%q/q) and MICA-BBVA forecast\*



### Confidence: data up to November consistent with GDP growing at a moderate pace in 4Q13

Figures from EC's survey remain on its upward trend, but at a slower pace than before. In contrast, PMI indices are still in expansionary territory. Overall, these confidence figures confirm that the recovery in the eurozone is slow, led only by Germany.

Chart 3  
PMI and GDP growth (%q/q)\*

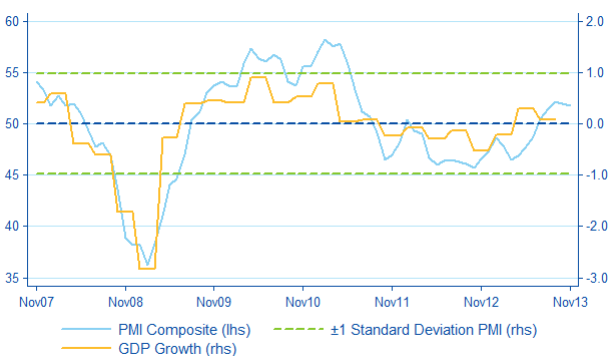
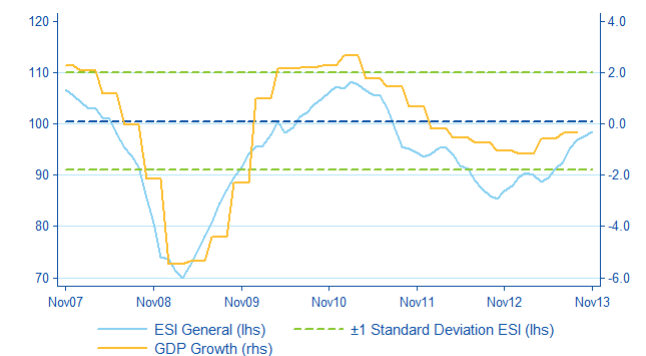


Chart 4  
Confidence (ESI) and GDP growth (%/y) \*\*



### Activity: data available up to October are somewhat disappointing

Industrial production unexpectedly fell in October by -1.1% m/m, leading the index to -0.9% below the Q3 average. Retail sales fell again in October, suggesting that the recovery of private consumption is not yet confirmed.

Chart 5  
Industrial prod.(%/y), manuf. new order and output PMI\*

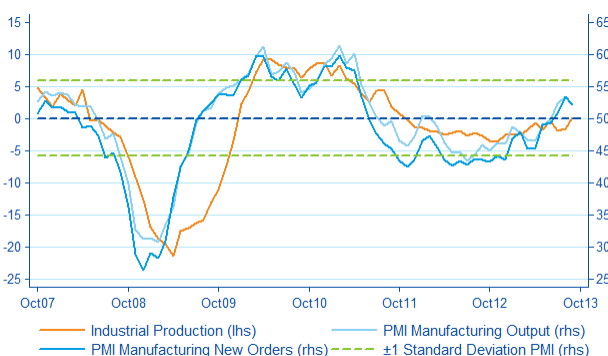


Chart 6  
Retail trade (% 3m/3m) and consumption growth (%q/q)\*



\*Source: HAVER and BBVA Research

## Foreign sector: exports slow, but remain a key driver of the recovery

Exports gained some traction by end-3Q13, while export orders suggest that they are likely to continue to grow at a solid pace in coming months. Nonetheless, imports also gained some momentum, reflecting a more dynamic domestic demand, so net exports support could ease.

Chart 7  
Current account (% of GDP)\*

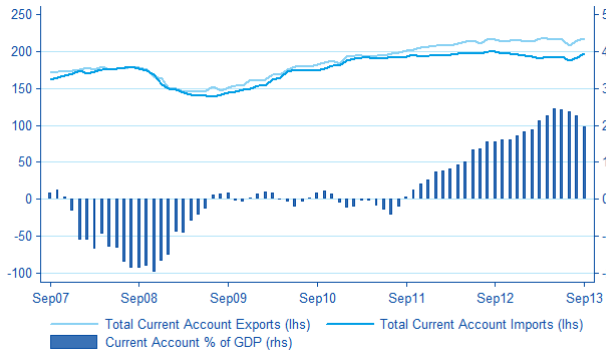
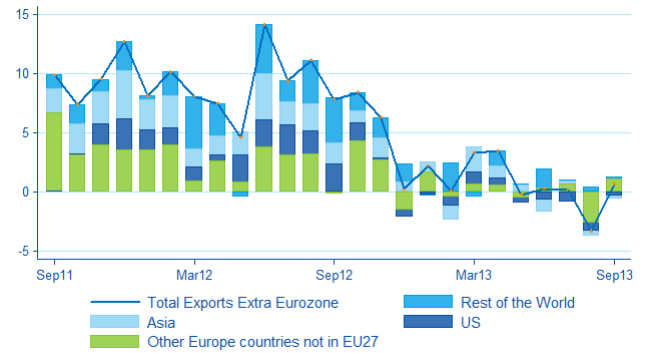


Chart 8  
Exports by destination (contribution to %/y)



## Labour market: broadly stable throughout the past half year

Though we think that a mild economic recovery is son track, the unemployment rate is unlikely to decline in the short run, given the lag between activity and employment as well as the economic slack, remaining at high levels. As a result, wage costs are moderating.

Chart 9  
Unemployment rate (%) and employment expectations\*

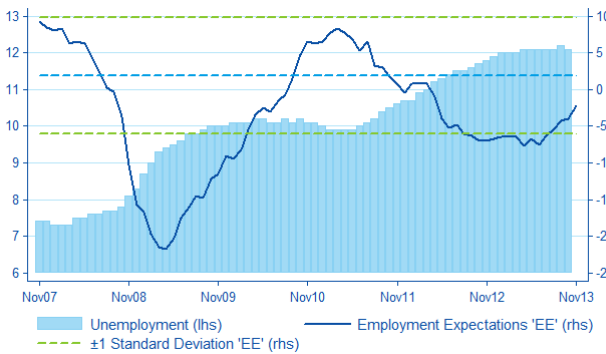
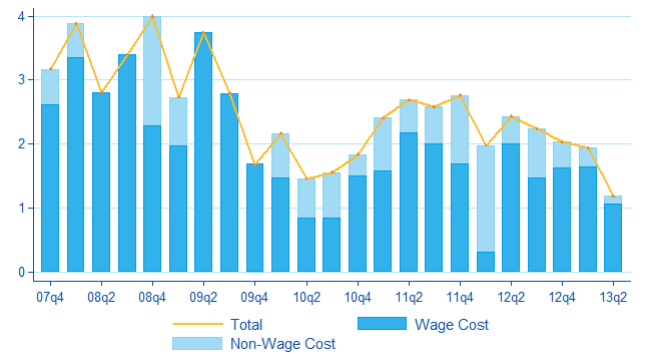


Chart 10  
Labour cost in business sector (%/y)\*



## Prices: inflation is likely to remain subdued in the medium term

Inflation stepped up by 0.2pp to 0.9% y/y in November, due to more moderate fall in energy prices, but also to higher-than-expected inflation in services that could result in core inflation at 1.1% y/y.

Chart 11  
Inflation rate, headline and core (%/y)\*

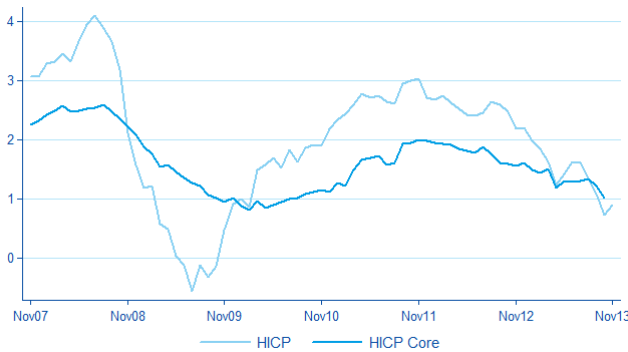
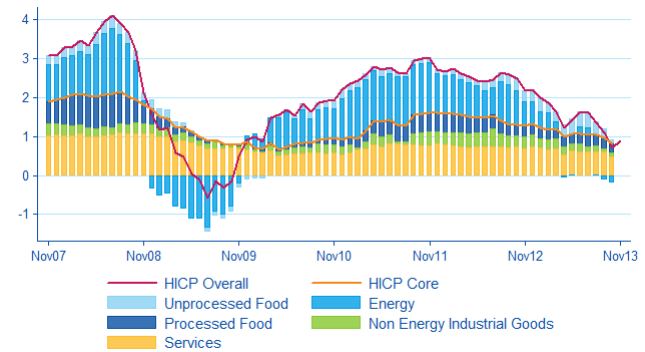


Chart 12  
Inflation by components (contribution in %)\*



\* Source: HAVER and BBVA Research

## Germany

### National accounts: robust domestic demand, especially investment

GDP growth slowed in 3Q13, as net exports weighed negatively on activity and were not offset by the stronger contribution of domestic demand. Our forecast of 0.5% q/q for 4Q13 is probably too positive, and we would be facing growth closer to 0.2%/0.3%.

Chart 13  
GDP (%q/q) and contribution by components (pp)\*

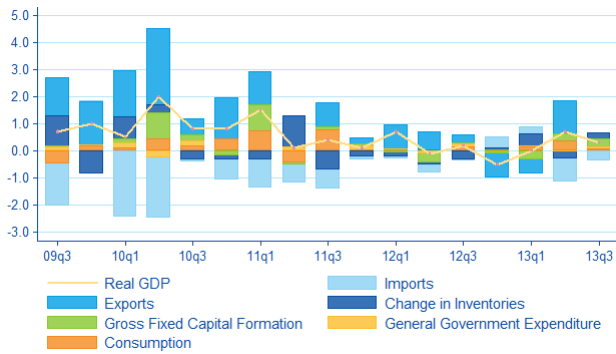
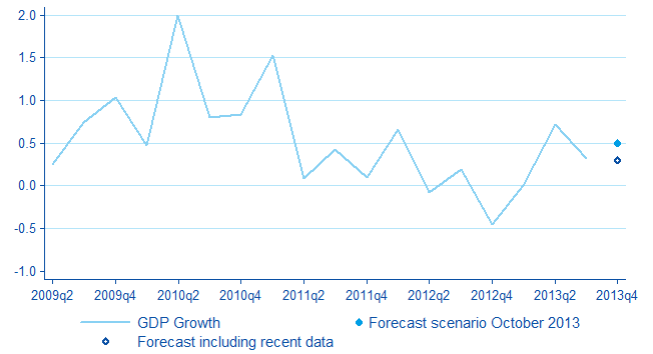


Chart 14  
GDP (%q/q) and forecasts\*



### Confidence: significant improvement so far in 4Q13, especially in November

Strong confidence was mostly driven by better expectations in the service sector. The composite PMI remains at levels similar to those observed by mid-2011, when GDP grew at around 0.5% q/q.

Chart 15  
PMI and GDP growth (%q/q)\*

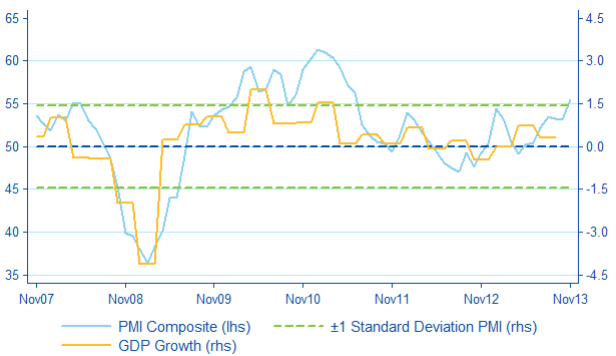
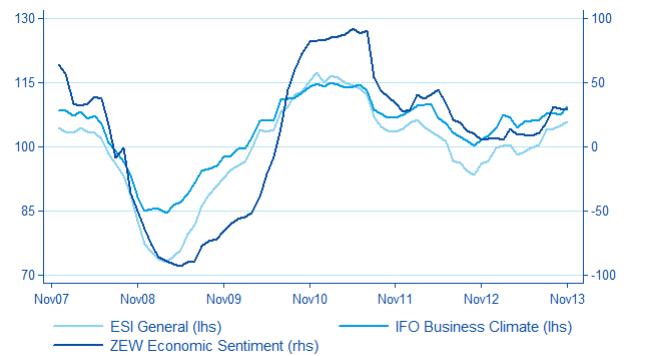


Chart 16  
Confidence indicator (ESI, Ifo and ZEW)\*



### Activity: disappointing data in October

Retail sales dropped more than expected, while industrial output declined again in monthly terms, after the significant drop registered in September, though it keeps growing in annual terms.

Chart 17  
Industrial prod. (%y/y) and manufacturing PMI\*

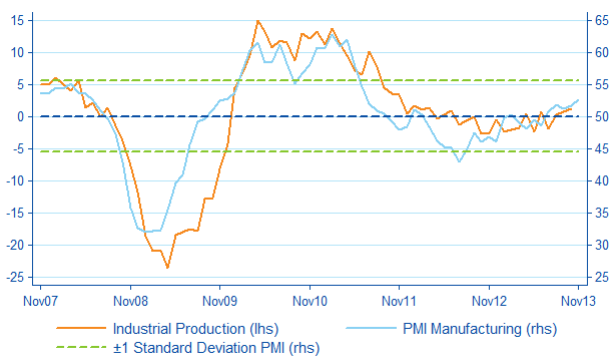


Chart 18  
Retail trade (% 3m/3m) and consumption growth (%q/q)\*



\*Source: HAVER and BBVA Research

## Foreign sector: exports increase again in recent months, but at a similar pace than imports

Exports increased slightly in October, after rebounding in the previous two months. As a result, exports level remains around 1.6% above 3Q13 (0.4% q/q).

Chart 19  
Current account (% of GDP)\*

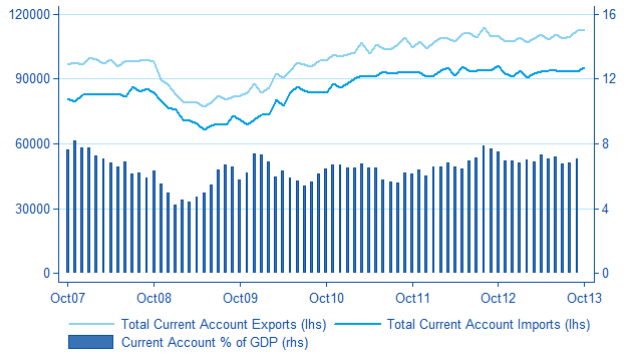
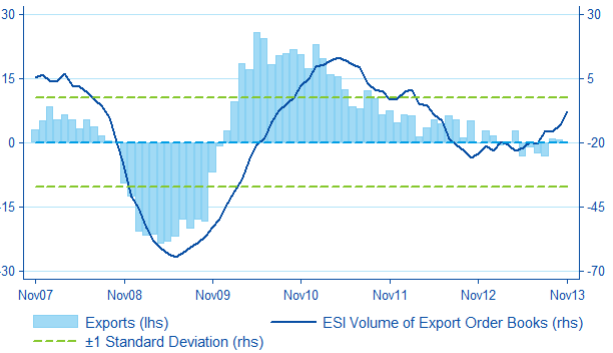


Chart 20  
Export growth (%/y) and volume of export order books\*



## Labour market: unemployment rate at historical low levels

Unemployment rate has remained broadly stable in the last two months at 5.2%. This could put some upward pressures on wages in coming months, though wage costs moderated sharply in Q2..

Chart 21  
Unemployment rate (%) and employment expectations\*

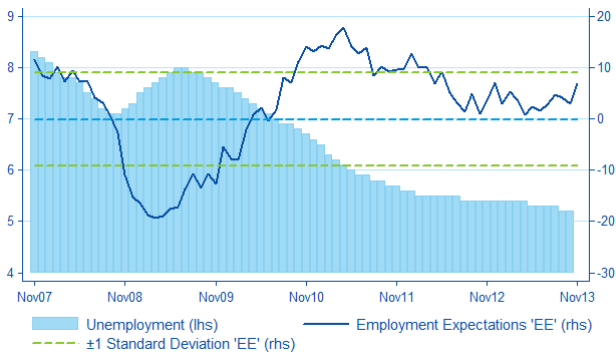
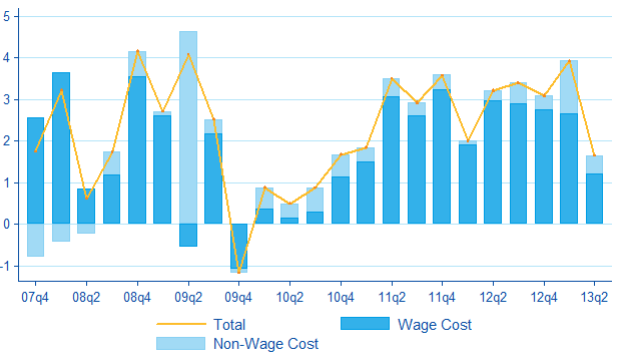


Chart 22  
Labour cost in business sector (%/y)\*



## Prices: no upward pressures in the pipeline

Harmonized inflation increased by 0.4pp to 1.6% y/y in November. Slowing inflation in recent months was mostly due to lower energy prices, with core inflation remaining at moderate levels during the past year.

Chart 23  
Inflation rate, headline and core (%/y)\*

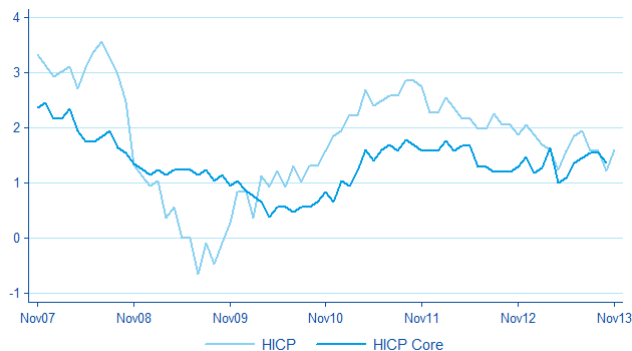
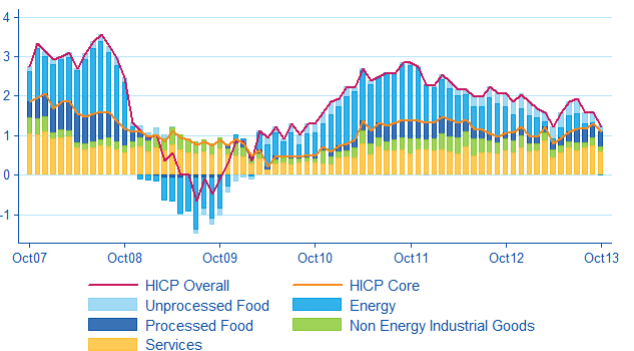


Chart 24  
Inflation by components (contribution in %)\*



\* Source: HAVER and BBVA Research

## France

### National accounts: domestic consumption was not enough to offset declining investment

GDP contracted -0.1% q/q in 3Q13, after the rebound observed in 2Q13, due to a sharp negative net export contribution. We expect GDP to grow slightly in 4Q13 (around 0.2% q/q), but with a downward bias.

Chart 25  
GDP (%q/q) and contribution by components (pp)\*

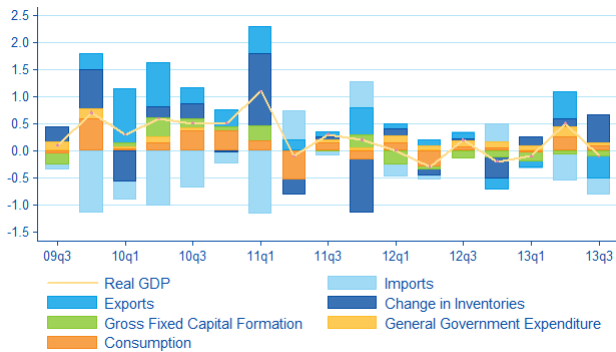
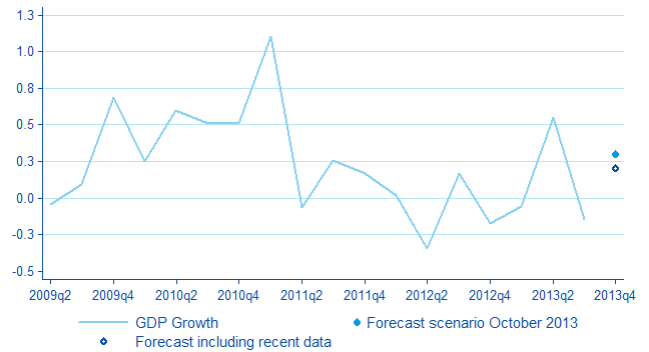


Chart 26  
GDP (%q/q) and forecasts\*



### Confidence: unexpectedly decline in October and November

PMIs returned again to below the 50 points threshold. The deterioration of PMIs was widespread across sectors. Other confidence indicators have been more stable during the past two months.

Chart 27  
PMI and GDP growth (%q/q)\*

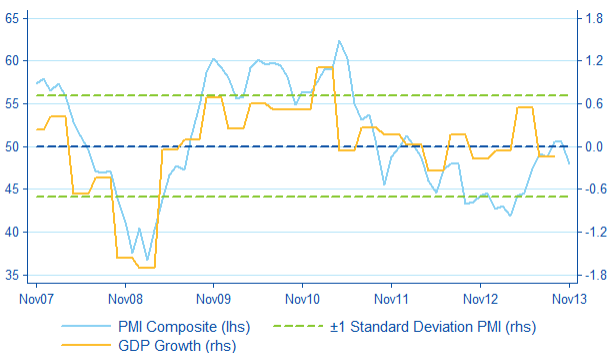
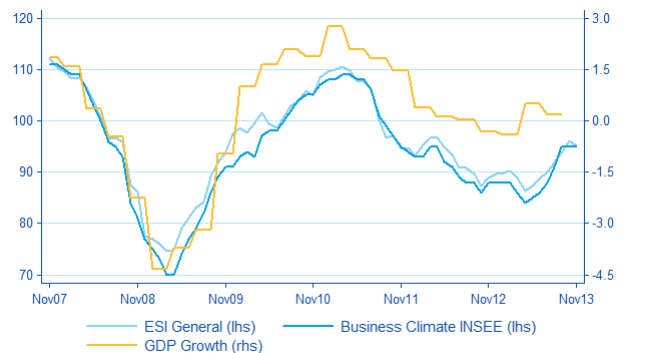


Chart 28  
Confidence indicator (ESI and INSEE)\*



### Activity: still very limited, but not reflecting the large decline observed in confidence

Retail sales and industrial production remained virtually flat in monthly terms in October, suggesting some economic stabilization in the current quarter.

Chart 29  
Industrial prod. (%/y) and manufacturing PMI\*

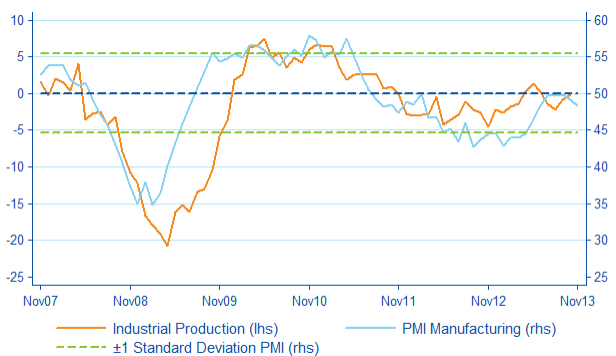
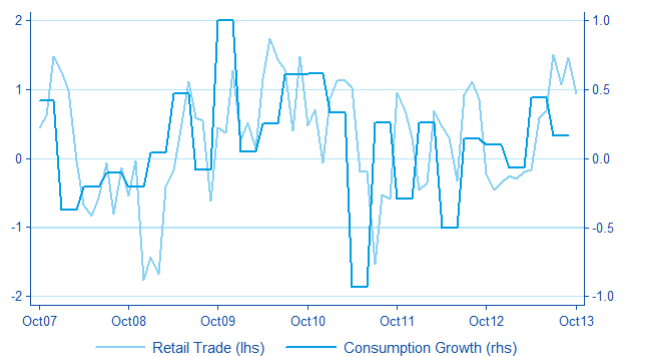


Chart 30  
Retail trade (% 3m/3m) and consumption growth (%q/q)\*



\*Source: HAVER and BBVA Research



### Foreign sector: unlike in other member state, exports are not the main driver of growth

Exports declined strongly in September, falling by -2.5% q/q, while imports remained resilient. In addition, this performance is likely to continue in coming months.

Chart 31  
Current account (% of GDP)\*

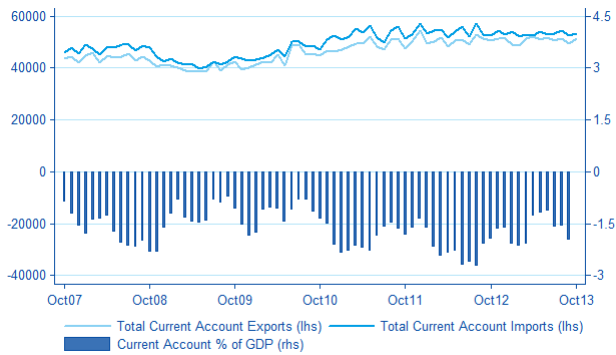
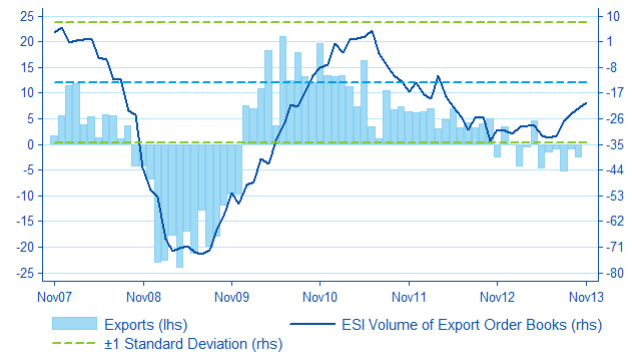


Chart 32  
Export growth (%/y) and volume of export order books\*



### Labour: some stabilization in recent months

The unemployment rate stabilized at around 11% in the past year after increasing by around 0.2pp per quarter over the previous year. Labour cost decelerated sharply during the first half of the year driven by falling non-wage costs.

Chart 33  
Unemployment rate (%) and employment expectations\*

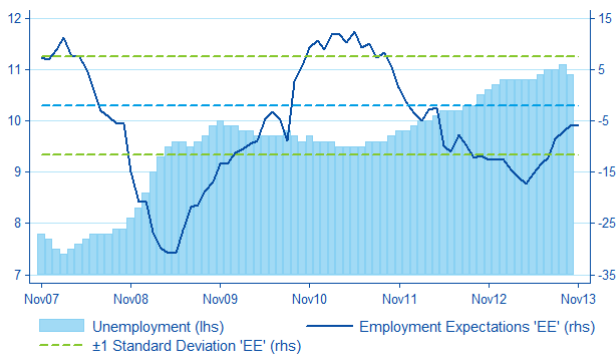
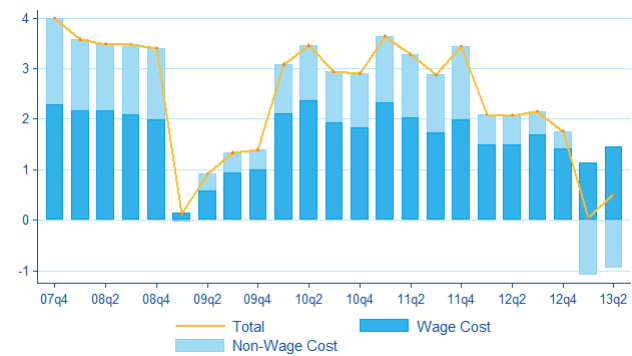


Chart 34  
Labour cost in business sector (%/y)\*



### Prices: inflation below 1% y/y

Harmonized inflation increased by 0.1pp to 0.8% y/y in November, while core inflation remained stable at 0.8% y/y. Unlike in other countries, slowing inflation through the year was due to lower prices of both energy and core components.

Chart 35  
Inflation rate, headline and core (%/y)\*

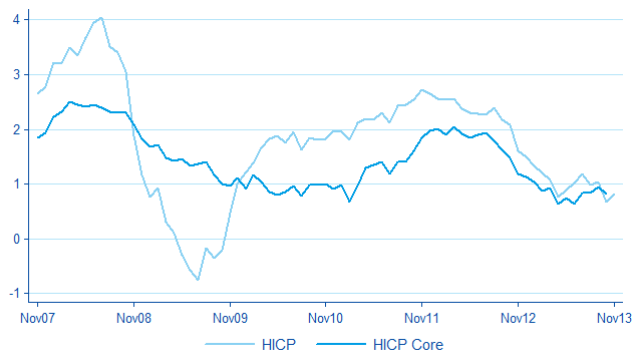
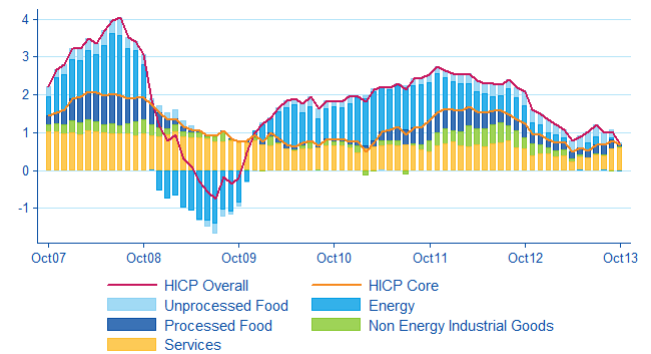


Chart 36  
Inflation by components (contribution in %)\*



\* Source: HAVER and BBVA Research

## Italy

### National accounts: slowly emerging from recession

GDP stagnated in 3Q13, with both private consumption and investment weighing negatively on growth. We continue to expect a slight growth in 4Q13 (around 0.1% q/q), but with a downward bias.

Chart 37  
GDP (%q/q) and contribution by components (pp)\*

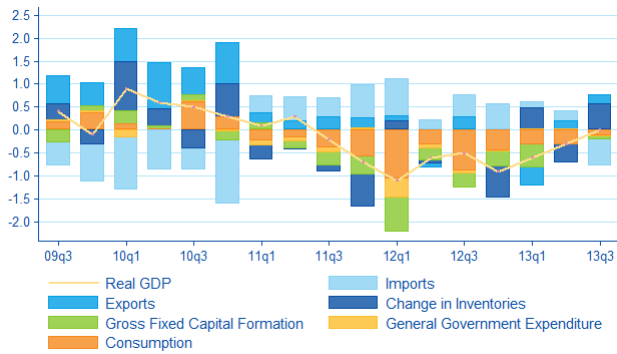
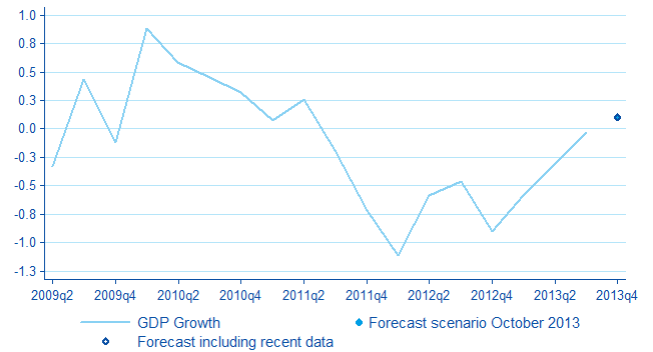


Chart 38  
GDP (%q/q) and forecasts\*



### Confidence: losing ground in recent months

After the significant improvement of soft data in September, PMIs lost ground in October and November, driven by worsening expectations in services sector, while the outlook for industrial sector remains more upbeat. Other confidence indicators have performed better.

Chart 39  
PMI and GDP growth (%q/q)\*

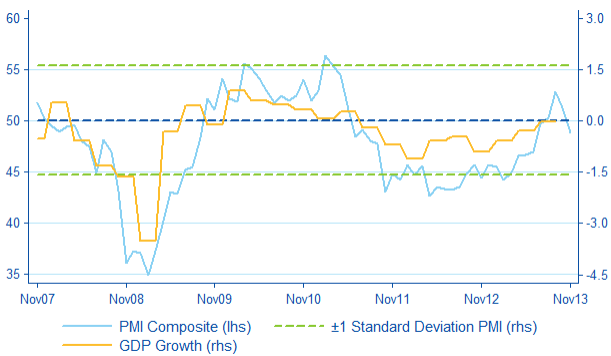
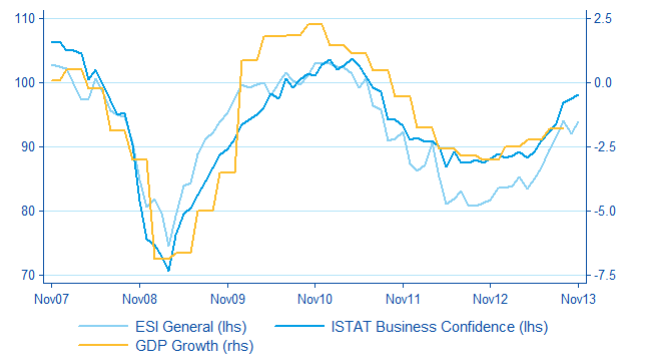


Chart 40  
Confidence indicator (ESI and ISTAT)\*



### Activity: limited data suggest that activity is gaining some traction by year end

Industrial production in October was strong (0.7% above the average of 3Q13) but retail trade has lost ground recently.

Chart 41  
Industrial prod. (%/y) and manufacturing PMI\*

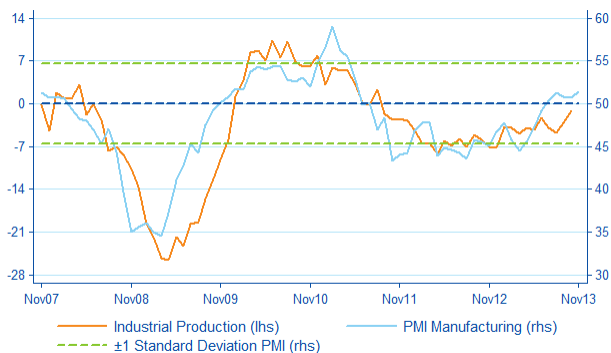


Chart 42  
Retail trade (% 3m/3m) and consumption growth (%q/q)\*



\*Source: HAVER and BBVA Research

## Foreign sector: net exports, the main growth factor in the short term

Last data of export order books (November) suggest that exports are likely to grow again in 4Q13 after the gains observed in 3Q13 (+0,7% q/q)

Chart 43  
Current account (% of GDP)\*

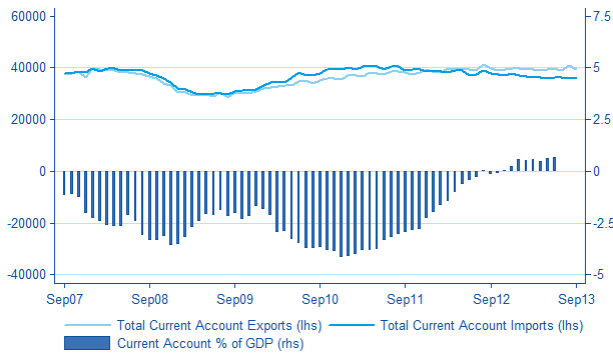
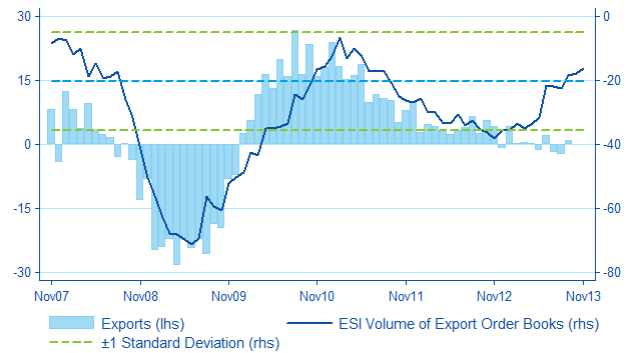


Chart 44  
Export growth (%/y) and volume of export order books\*



## Labour market: unemployment in stable levels with more moderate increases of labour cost

The unemployment rate has remained stable over the past two months with the last employment expectations bouncing back. The labour cost was still increasing at strong rates in Q2.

Chart 45  
Unemployment rate (%) and employment expectations\*

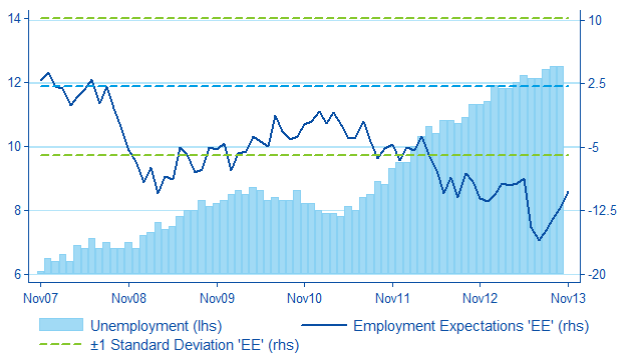
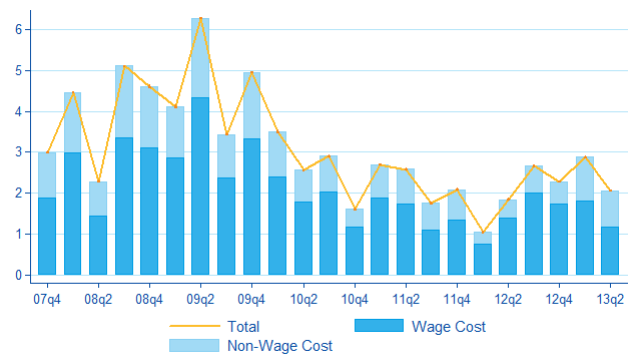


Chart 46  
Labour cost in business sector (%/y)\*



## Prices: inflation slows in November

Inflation has moderated rapidly over the past two months, although core inflation remains broadly stable at above 1%.

Chart 47  
Inflation rate, headline and core (%/y)\*

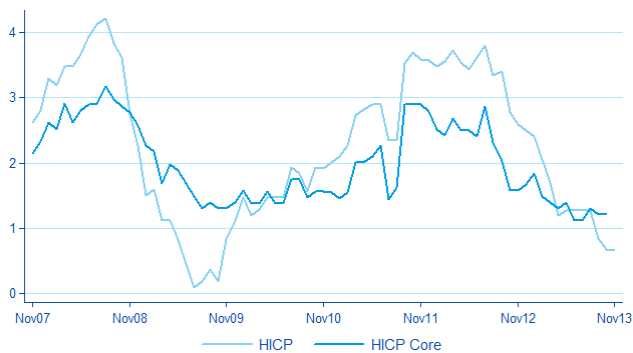
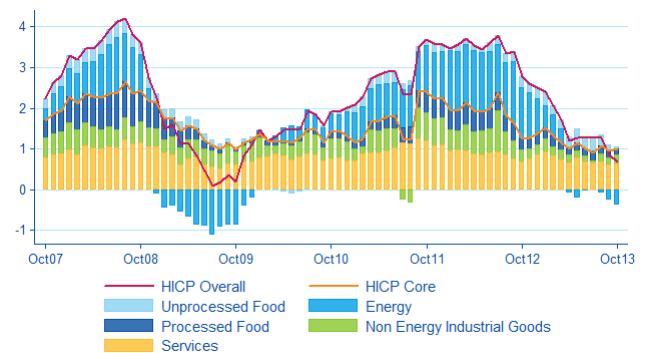


Chart 48  
Inflation by components (contribution in %)\*



\* Source: HAVER and BBVA Research

## Spain

### National accounts: exports slow, but private domestic demand starts to revive

The economy grew at +0.1% q/q in 3Q13, leaving behind a long recession mainly due to robust exports and revival of private demand. The MICA-BBVA model estimates for 4Q13 a quarterly GDP growth of +0.3% q/q

Chart 49  
GDP (%q/q) and contribution by components (pp)\*

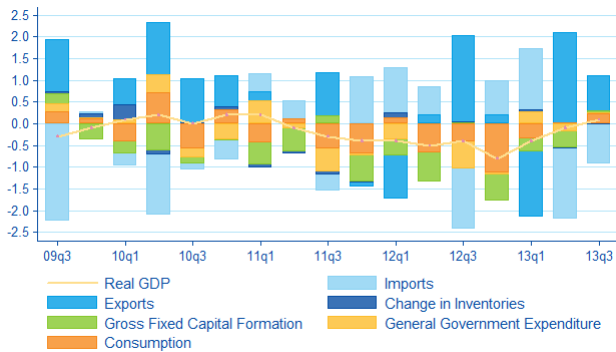
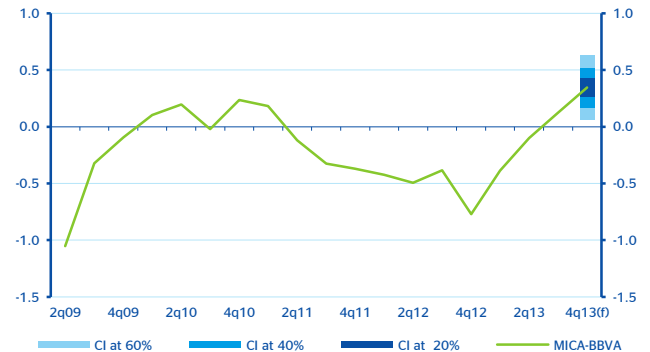


Chart 50  
GDP growth (%q/q) and MICA-BBVA forecast\*



### Confidence: latest data consistent with positive GDP growth again in 4Q13

ESI and PMI indexes show stabilizing confidence levels in 4Q13. With an improvement in the last figures (November) of both indices, while PMI is in expansionary territory (above 50) for the third time in the past four months

Chart 51  
PMI and GDP growth (%q/q)\*

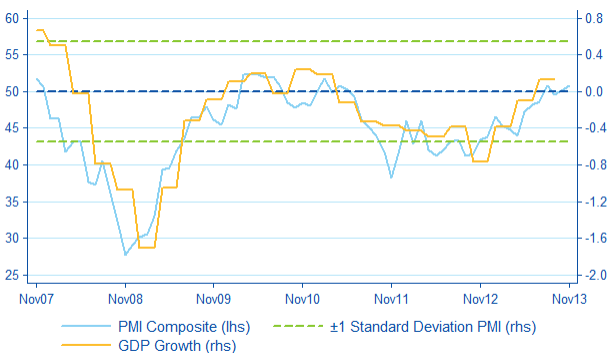
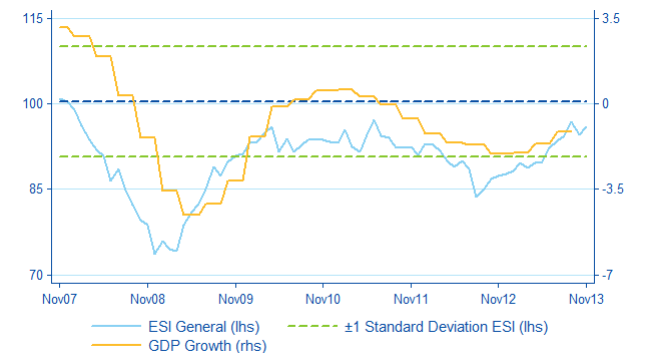


Chart 52  
Confidence (ESI) and GDP growth (%y/y) \*



### Activity: recession eases but the recovery is still fragile

Industrial production registered a slight decline in October (-0.8 y/y after +0.8 y/y in September), staying close to Q3 levels. Meanwhile, last data of retail sales were disappointing

Chart 53  
Industrial prod. (%y/y) and manufacturing PMI\*

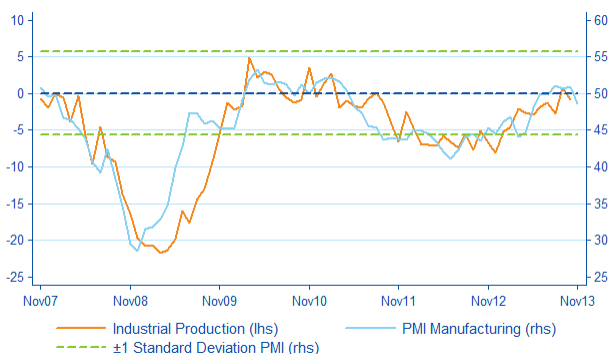


Chart 54  
Retail trade (% 3m/3m) and consumption growth (%q/q)\*



\*Source: HAVER and BBVA Research

## Foreign sector: exports are likely to slow again in 4Q13 but remain robust

Firms' expectations (exports orders) suggest that exports are likely to moderate at the end of 2013. Imports are increasing due to the reviving of domestic demand, compensating part of the export increase.

Chart 55  
Current account (% of GDP)\*

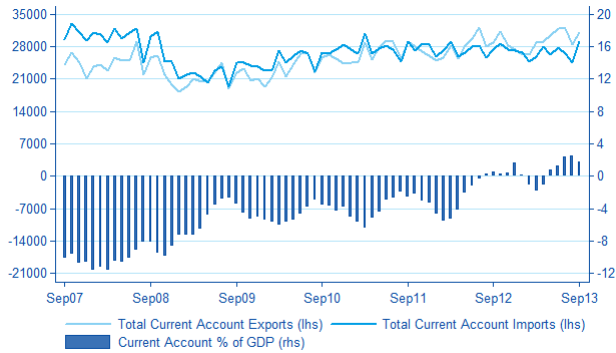
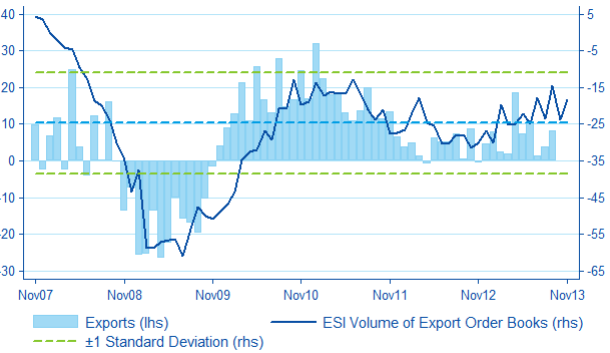


Chart 56  
Export growth (%/y) and volume of export order books\*



## Labour: social security affiliates increase and unemployment stabilizes

Affiliation to Social Security has increased in November for the second consecutive month, after more than five years of falls. Unemployment has stabilized, albeit at a high level of 26%, pointing to a change of cycle in labor market.

Chart 57  
Unemployment rate (%) and employment expectations\*

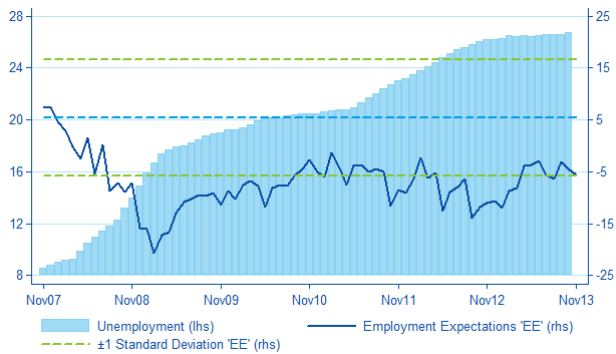
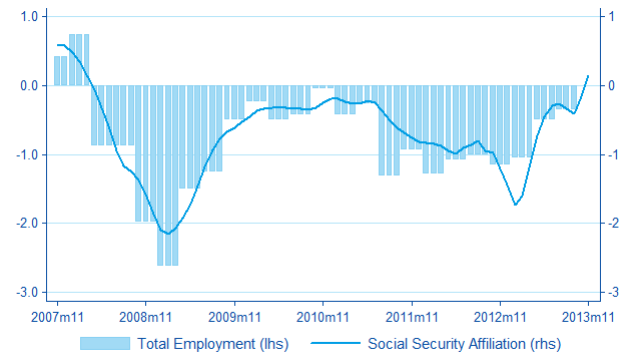


Chart 58  
Employment growth: N.A. and social security (% 3m/3m)\*



## Prices: inflation in line with expectations and pointing to an acceleration of core HICP

Headline inflation would have increased by 0.3 percentage points to stand again in positive territory. Our estimates suggest that core inflation would also have increased, somewhat less than one-tenth in November, up to 0.3% y/y.

Chart 59  
Inflation rate, headline and core (%/y)\*

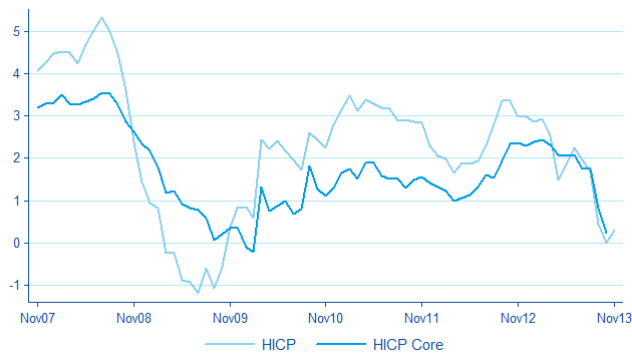
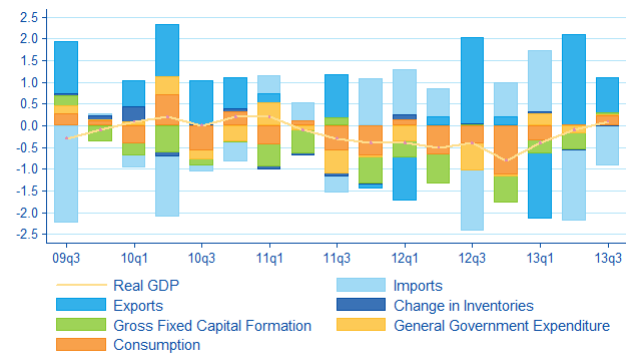


Chart 60  
Inflation by components (contribution in %)\*



\* Source: HAVER and BBVA Research

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