Eurozone: Vaccination vs Delta

The holiday season is likely to spread the Delta variant more widely across the eurozone, though a rapidly advancing vaccination campaign will limit the fallout. With consumers eager to open their wallets, companies can more easily pass on higher input prices. The European Central Bank remains dovish, but the PEPP programme is unlikely to be extended

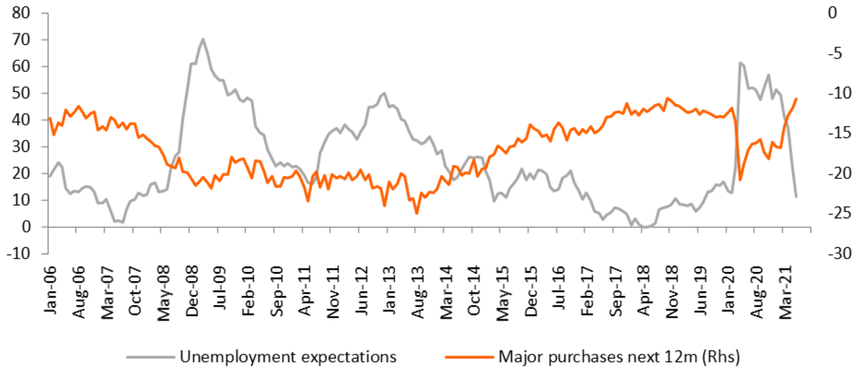
Source: Shutterstock

Consumers prepare for a spending spree

Eurozone sentiment indicators are surging as freedom from the pandemic looks to be within reach. But let's not forget that the Delta variant is now gaining ground in continental Europe, with increased travelling likely to accelerate the spread. In terms of the growth outlook, however, we don't expect this to make a big dent, as the majority of the population will probably be fully vaccinated by the end of summer, limiting the negative fallout from increased infections.

While the second quarter started on a weak footing, growth clearly picked up throughout the period. The European Commission's economic sentiment indicator hit a 21-year high in June, with confidence now way above the long-term average in all sectors. The fear of second-round increases in unemployment is now rapidly fading away and we are starting to see, albeit still anecdotally, a lack of skilled labour in certain sectors. No wonder that consumer intentions to make major purchases over the next 12 months are close to the highest level in 20 years. So we're still comfortable with our 4.5% growth forecast for this year and 4.0% for 2022.

Fading unemployment fear boosts spending plans

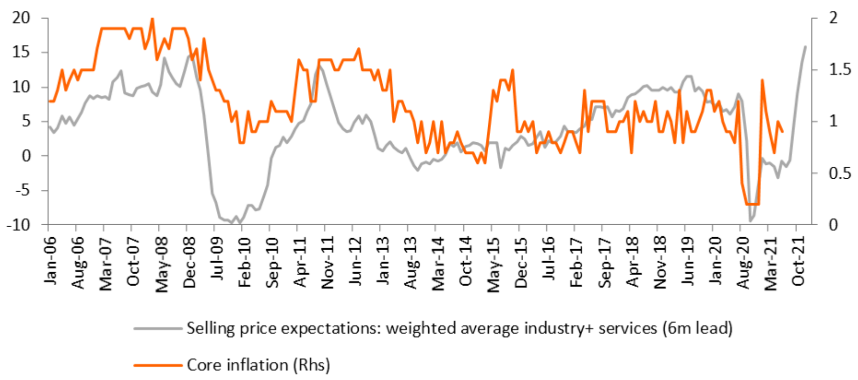


Source: Refinitiv Datastream

Companies are passing through higher costs

Inflation came in at 1.9% in June, though underlying inflation seems to be stuck at 0.9%. But goods inflation jumped from 0.4% in April to 1.2% in June, which reflects producers pricing through higher input costs to the consumer. And this is not going to end any time soon. The PMI survey reported in June that average input prices are rising at a rate exceeded only once over the 23-year survey history. While this was already seen in the manufacturing sector in the last few months, the survey also showed the steepest increase in service sector costs since July 2008. Meanwhile, the ECB remains pretty sanguine, with staff inflation forecasts of only 1.5% for 2021 and 1.4% for 2022. While we don't see inflation remaining above 2% either, we think the ECB is now definitely on the low side of potential outcomes.

Selling prices are expected to increase



Source: Refinitiv Datastream

Dovish ECB

The ECB surprised in its June meeting by actually maintaining its intention to buy bonds at a significantly higher pace. But the hawks didn't wait long to question this decision with Bundesbank

President Jens Weidman pleading for a tapering of asset purchases (which will have to happen anyway, if the envelope is not increased). It will be hard to find a convincing argument to extend the Pandemic Emergency Purchase Programme beyond March 2022, though we still expect a slight increase in the Asset Purchase Programme to make the exit from PEPP a little smoother.

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