

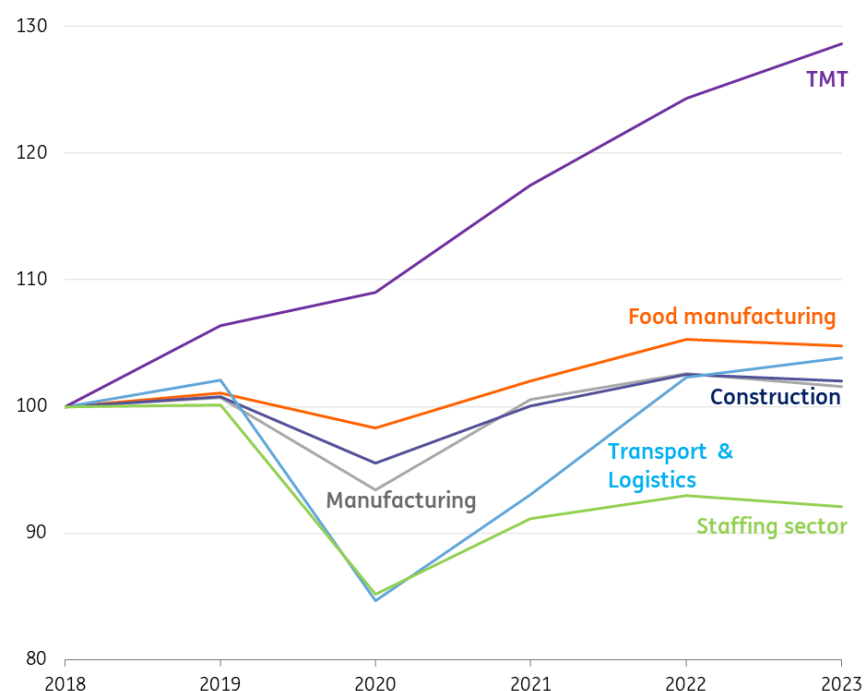
Many European sectors will suffer from a weak economy in 2023

In 2023, many EU sectors will see diminishing growth due to a weak economy. Manufacturing, staffing and construction are likely to face a small decline though not all sectors will shrink. While the Technology, Media & Telecom (TMT) and transport sectors should see lower growth than last year, the outlook remains positive



Sluggish developments in many industries

Development production (volume value added) EU sectors (Index 2018=100)

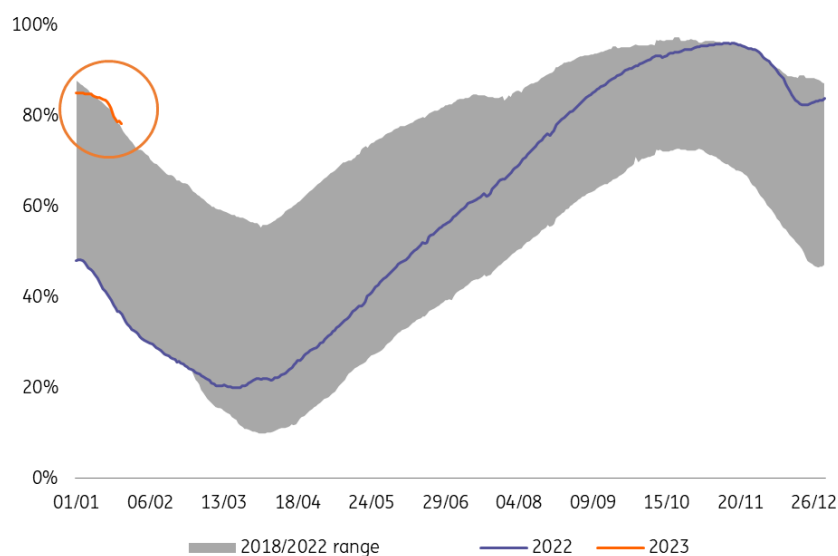


Energy prices still a drag but gas and power markets have eased

Given the circumstances, European companies could not have hoped for a better situation during the first half of the heating season. Demand destruction, milder-than-usual weather and continued LNG supply have ensured that storage levels are still at record-high levels. Day-ahead TTF gas prices have fallen as much as 83% from the peak in August 2022 and APX power prices by 75%. This leaves Europe in a [better-than-expected position](#) for the remainder of this winter and the same is true for the 2023 filling season of gas storages. However, it is still vital that the region is cautious through the remainder of this winter, as Europe needs to try to end the current heating season with storage as high as possible as [gas flows from Russia](#) could still be reduced further, both in terms of pipeline flows and LNG shipments. Futures markets currently expect TTF gas prices to trade between 55 and 65 euro/MWh throughout 2023 and carbon prices to remain within their trading band of 75 to 100 euro per ton CO₂. Hence, markets currently expect APX baseload power prices to trade between 140 and 175 euro/MWh throughout 2023. That is a lot lower compared to the future prices before the start of the winter, but still three to four times higher than pre-crisis levels. Hence, energy prices will continue to weigh on European sectors in 2023.

European gas storage levels are at record high levels

EU gas storage levels



Source: ING Research based on Refinitiv and Gas Infrastructure Europe

Manufacturing: Still cloudy, but gradually clearing up

In recent months, the outlook for European industry has improved somewhat thanks to a mild winter and governments bolstering producer confidence by dampening the extreme energy prices. Given the fact that the sector has encountered a growing number of persistent problems, production held up well in 2022. Average growth was around 2%, but sectoral differences were large, ranging from sharp contractions in energy-sensitive basic materials such as chemicals (-5.5%) and base metals (-3.5%), to strong growth in consumer goods such as pharmaceuticals (+14%) and clothing (+5%). Production interruptions have been greatly reduced, but like the high energy prices, are not yet a thing of the past. In addition, a post-Covid consumption shift from products to services and stagnation in the US will most likely continue to weigh on demand in the first half of 2023. The reopening of the economy in China provides some counterweight on the demand side.

Manufacturers' expectations for the near future have become less pessimistic. In addition, automakers clearly continue to benefit from the more reliable supply of semiconductors and other electronic components, which is enabling them to eliminate the large production backlogs. In that respect, it is also encouraging that [the Ifo index](#), Germany's most prominent indicator, rose for the fourth time in a row in January. Still, don't expect a full-blown industrial upswing in 2023. The more bearish factors dominate for now, and some renewed but subdued growth in the second half of 2023 seems the most realistic scenario.

Food manufacturing: Slight decline after two years of strong growth

Growth in production volumes in food manufacturing has been particularly strong over the last two years, partially because of a Covid rebound. Over the past 20 years, there are three periods in

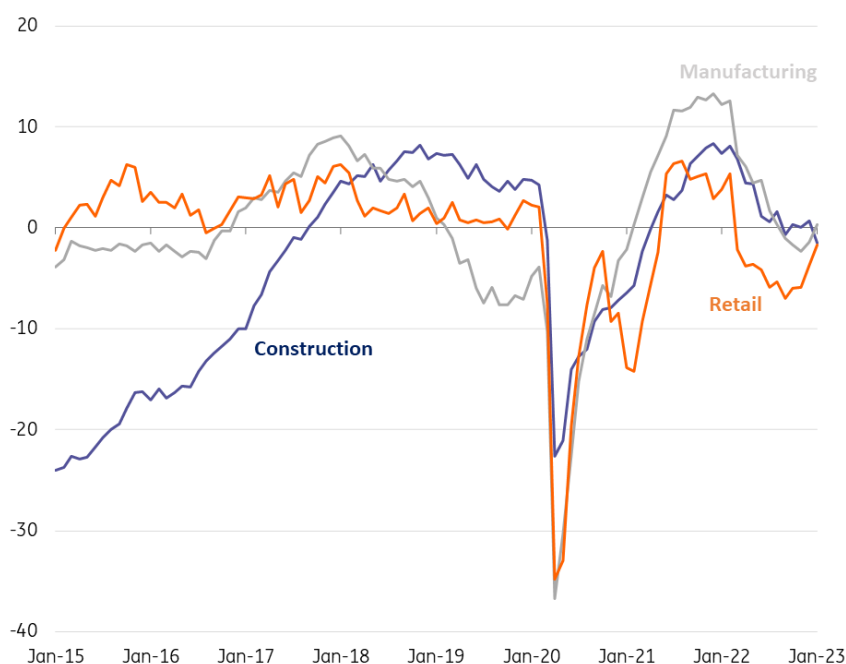
which production volumes decreased in line with a general economic downturn, namely 2008-'09, 2012-'13 and 2020. We believe 2023 could mark a decline in the range of 0.5% to 1% for food makers as the general economy balances between contraction and stagnation. While the inflation peak seems to have passed, there are still many food manufacturers that plan to raise sales prices in the months ahead. However, since December, this group is no longer in the majority. Food inflation came in at 12.2% in 2022 which has likely caused shifts in consumer demand as more households look to save money when shopping for groceries or eating out. For food producers, this could mean that companies that primarily focus on making private-label products and supplying discounters fare a bit better in terms of sales volumes compared to branded food makers. Still, the latter have more pricing power in general and are in a better position to defend margins.

Construction: Order books still well-filled

In November 2022, EU construction production decreased a bit (-0.4%) compared to October but was still above the volume of a year earlier. Higher interest rates and a weaker economy are making home buyers and firms more reluctant to invest in new residential and non-residential buildings. In addition, higher building material costs have made new investments more expensive although some [building materials prices](#) have decreased in the last few months. That said, EU construction firm order books are still well filled with 9.0 months of ensured works at the beginning of 2023. The EU construction confidence indicator declined in the first half of 2022, but since then, has hovered around neutral. So, the developments are certainly not bad in every subsector. High energy prices are creating additional demand for energy-saving construction works in the installation and maintenance market. All in all, we expect only a very slight decrease (-0.5%) in total EU construction volumes in 2023.

Increase in sentiment indicator retail and manufacturing sector in January 2023

European Union Sentiment indicators



Source: Eurostat, ING Research

Retail: Weak start to the year but some recovery expected

2023 is likely to be another interesting year for retail. Last year saw people spend more money than ever at the store and online, although volumes have been on a declining trend since late 2021. This is a clear sign that consumers are suffering from high prices. We also note that pre-pandemic preferences are now returning with consumers once again spending more on services and less on goods. Slowing volumes and easing supply chain problems have led to fast growth in inventories, which could prove problematic early in the year given that consumers are becoming more cautious about spending on goods. The big question mark is how purchasing power will recover over the course of the year as inflation is expected to drop. Wage growth is set to increase, but not to the extent that purchasing power will improve in the first half of the year. Still, with unemployment expected to remain low, there seems to be potential for recovery in sales volumes in the second half of the year.

TMT: Growth will slow but remain strong

We estimate that growth in the information and communication sector was 5.8% in 2022 and we forecast 3.5% growth for 2023. This is a composite figure that reflects growth above 3.5% in the sub-sector “Computer programming, consultancy, and information service activities”, while growth should be more subdued in the telecom sub-sector. Our expected growth for the information and communication sector is below the historic average, in line with the expected economic slowdown. The sector has been growing much faster than the overall economy over the years. According to European Commission survey data, managers of the largest subsectors of the information and communication sector have a neutral view about the near-term business prospects. They do not think that there are specific factors which will restrain growth, although some managers report it is a challenge to find personnel. Interestingly, the sector is experiencing a lot of price pressure, which is favourable for customers. Nominal growth will therefore be more subdued than volume growth in 2023.

Transport & Logistics: Rebound of passenger travel outweighs headwinds for freight

The European transport and logistics sector is entering a new phase of reality after the unprecedented impact from the pandemic and the Russian invasion of Ukraine. Unlike 2022, this year starts with (nearly) all travel restrictions removed. With European interest in (leisure) travel continuing to resume, the aviation sector is set to proceed on a low double-digit recovery track. Public transport networks are also expected to see higher occupancy rates. On the dominant freight side, the outlook is bleaker, with consumers spending more on services and demand for goods faltering amidst economic weakness and sanctions. German road transport traffic on motorways – a relevant indicator – ended last year in slight negative territory. But freight logistics could pick up over the course of the year as the European manufacturing sector shows signs of improvement, and China’s Covid policy U-turn could benefit airlines as well as trade (and the ports- and shipping sector). On balance, we expect the transport and logistics sector to grow by 1.5% in 2023.

Staffing: Hiring freezes seen due to EU recession fears

After two years of buoyant market growth, the outlook for the European staffing sector is darkening for 2023. With economic activity in most European economies expected to slow down,

market volumes in the European Union are likely to decline by 1% in 2023. A combination of lower economic growth forecasts and rising costs will likely soften demand for temporary agency workers, especially in certain energy-intensive and/or consumer-oriented industries. Although unemployment will rise slightly, the labour market remains tight in most European economies. Hence, clients are more likely to turn to temp agencies since they are better equipped to find candidates than the clients themselves. However, at the same time, the tight labour market will limit the growth potential of temporary employment agencies, as it becomes more difficult for them to recruit new employees.

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