Eurozone: A false start to the new year

With Covid-19 cases swelling again in the last few months of 2020, several European countries had to tighten containment measures and extend them into this year. The risk now is that GDP contracts again in the first quarter. The slow start to the vaccine campaign is not helping either, but GDP growth should pick up from the second quarter onwards

A virtually deserted Eiffel Tower in Paris

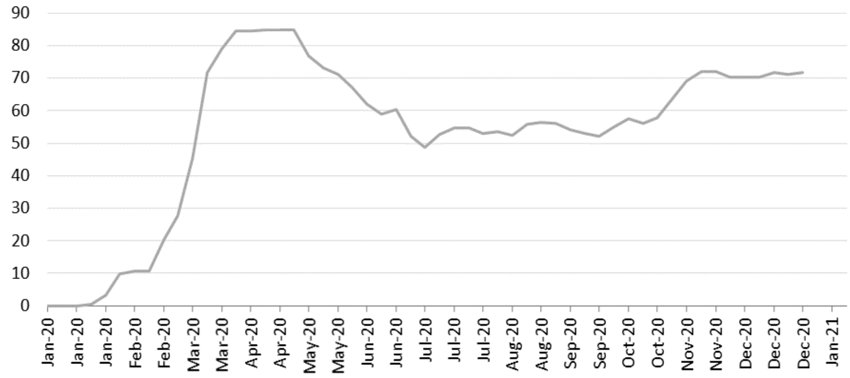
The short-term outlook

With rising numbers of Covid-19 cases in the last few months of 2020, several eurozone countries were forced to tighten lockdown measures and extend them into the first quarter of this year. Manufacturing remained relatively strong over the past few months (PMI at 55.2 in December), but judging by the mobility data, consumption was probably slightly weaker, resulting in a GDP contraction in the fourth quarter (though less dramatic than in the second).

Winter sports holidays will be partially cancelled and bars and restaurants might stay closed beyond January, which will also hurt consumption in the next few months. And while Brexit probably gave a boost to 4Q exports, with UK retailers building up inventories, the reverse will be seen in 1Q. Finally, with the more contagious strain of Covid-19 now reaching the continent, the risk of a third wave in the first quarter, unfortunately, cannot be excluded. We're looking at first-quarter growth to be at best 0%, which probably means two consecutive quarters of negative growth.

Stringency of containment measures

Average for the six biggest eurozone countries



Source: Refinitiv Datastream

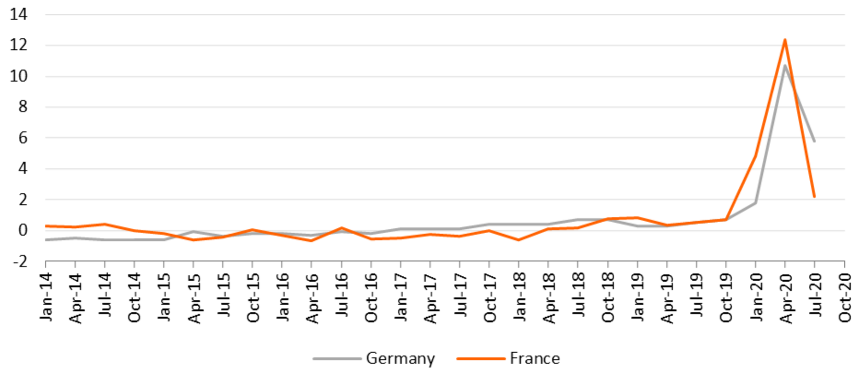
The vaccine effect

The purchase of the vaccine has been coordinated at a European level, with the EU ordering more than one billion doses from several producers, although some of them won't have them ready until the second half of the year. At the time of writing, only the Pfizer/BioNTech has been approved by the EU, but the Moderna vaccine is likely to follow in the first half of January.

The start of the vaccination campaign has been slow and sometimes chaotic, with some countries not even having started in the first week of January. As the approval for the AstraZeneca vaccine has been delayed and the Johnson & Johnson vaccine still in phase 3, there might also be some supply problems. Germany hopes to have vaccinated 60% of the population by the end of the summer and other countries are unlikely to be faster. So herd immunity is only expected to be reached in the course of 4Q 2021. That said, with the most vulnerable groups being inoculated first, the opening up of the economy is likely to begin in the second quarter, though some social distancing rules will remain in place for some time to come.

Household savings rate

Divergence from the 2014-2019 average



Source: Refinitiv Datastream

The strength of the recovery

2021 is starting on the wrong foot, with the eurozone economy still struggling. But even though the vaccination process will be drawn-out, we believe that from the second quarter and beyond, some of the excess savings households built up in 2020 will be unleashed, boosting consumption. And that especially goes if the tourism and entertainment sectors are gradually reopened in the European spring.

The second half of the year will also get a boost from the European Recovery Fund with public investment shifting into higher gear. It's unclear to what extent businesses will be able to join the investment boom, as many will still try to rebuild their financial health. Exports will benefit from a synchronised worldwide recovery, though the strong euro is likely to temper this tailwind. That's why we have now downgraded our GDP growth forecast to 3.0% this year, followed by 3.5% in 2022, given the weak start to the year. That means that it will take until the summer of 2023 for the eurozone to regain its pre-crisis activity level.

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