

Three calls for the eurozone: It's still brighter in the south

Portugal, Italy, Greece and Spain have outpaced the eurozone's average growth over the past few years, and we expect this trend to continue in 2025



Italian Prime Minister Giorgia Meloni at last month's Mediterranean Dialogues conference

1 Call 1: Southern member states will over-perform for the fifth consecutive year

Remember that horrible acronym PIGS, used to describe the southern Economic and Monetary Union (EMU) member states being targeted by financial markets during the euro crisis? How times have changed. Over the last four years, Portugal, Italy, Greece and Spain have outpaced the eurozone's average growth. And this trend is expected to continue next year.

These countries have received a significantly larger portion of the NextGen funds compared to their northern counterparts and still have plenty of money to spend. Additionally, the service sector's share of GDP in these southern nations is higher than the eurozone average, which is beneficial as European manufacturing faces challenges from high energy prices and upcoming US import tariffs. That said, Italy, with a bigger manufacturing base and a more challenging fiscal situation, might have trouble keeping up with the other three.

Call 2: Labour market turning, wage growth coming down

The eurozone labour market is tighter than the sluggish economic environment would suggest. With labour markets already under strain since the pandemic, businesses have hoarded labour while production remains weak, resulting in a decline in productivity.

During periods of high inflation, businesses could afford to retain excess staff because profits were bolstered by price-driven revenue growth. However, with inflation now reduced and wage growth remaining high, profit growth has rapidly diminished. As wage costs surpass revenue growth, the ability to keep underused employees on the payroll is no longer sustainable.

Businesses are indeed more downbeat on hiring. We expect unemployment to increase moderately throughout 2025 as hoarding labour is becoming a lot more expensive. It also adds to the recent trend of higher bankruptcies, but the positive is that it should also help with some cyclical recovery in productivity.

3 Our bold call: Fiscal convergence but no common financing tool in 2025

Fiscal tensions within the eurozone are quickly increasing. France and Germany have been following almost completely opposing fiscal policies in recent times.

With a government debt ratio of 115% of GDP and an average fiscal deficit of 6% of GDP over the past few years, France urgently needs austerity. With government debt slightly above 60% of GDP, a fiscal deficit of less than 2% of GDP and an investment gap of more than €600bn, Germany needs fiscal stimulus.

This fiscal policy approach of two extremes is not sustainable, and we expect to see a new type of fiscal convergence in 2025, with France becoming more German and Germany becoming more French. At the same time, talks about new common European financing instruments – as needed as they are – will be postponed as just paying the interest rates on newly issued European debt would require changes to an already tight EU budget.

Author

Carsten Brzeski

Global Head of Macro

carsten.brzeski@ing.de

Bert Colijn

Chief Economist, Netherlands

bert.colijn@ing.com

Peter Vanden Houte

Chief Economist, Belgium, Luxembourg, Eurozone

peter.vandenhoute@ing.com

Disclaimer

This publication has been prepared by the Economic and Financial Analysis Division of ING Bank N.V. ("ING") solely for information purposes without regard to any particular user's investment objectives, financial situation, or means. *ING forms part of ING Group (being for this purpose ING Group N.V. and its subsidiary and affiliated companies)*. The information in the publication is not an investment recommendation and it is not investment, legal or tax advice or an offer or solicitation to purchase or sell any financial instrument. Reasonable care has been taken to ensure that this publication is not untrue or misleading when published, but ING does not represent that it is accurate or complete. ING does not accept any liability for any direct, indirect or consequential loss arising from any use of this publication. Unless otherwise stated, any views, forecasts, or estimates are solely those of the author(s), as of the date of the publication and are subject to change without notice.

The distribution of this publication may be restricted by law or regulation in different jurisdictions and persons into whose possession this publication comes should inform themselves about, and observe, such restrictions.

Copyright and database rights protection exists in this report and it may not be reproduced, distributed or published by any person for any purpose without the prior express consent of ING. All rights are reserved. ING Bank N.V. is authorised by the Dutch Central Bank and supervised by the European Central Bank (ECB), the Dutch Central Bank (DNB) and the Dutch Authority for the Financial Markets (AFM). ING Bank N.V. is incorporated in the Netherlands (Trade Register no. 33031431 Amsterdam). In the United Kingdom this information is approved and/or communicated by ING Bank N.V., London Branch. ING Bank N.V., London Branch is authorised by the Prudential Regulation Authority and is subject to regulation by the Financial Conduct Authority and limited regulation by the Prudential Regulation Authority. ING Bank N.V., London branch is registered in England (Registration number BR000341) at 8-10 Moorgate, London EC2 6DA. For US Investors: Any person wishing to discuss this report or effect transactions in any security discussed herein should contact ING Financial Markets LLC, which is a member of the NYSE, FINRA and SIPC and part of ING, and which has accepted responsibility for the distribution of this report in the United States under applicable requirements.

Additional information is available on request. For more information about ING Group, please visit www.ing.com.