

Snap | 28 July 2023

## Eurozone economic sentiment indicator confirms weak start to third quarter

The eurozone economy performed weaker than expected at the start of the third quarter, thereby increasing the recession risk. Inflation expectations ticked up slightly in the service sector though, indicating that data so far leave room for interpretation for the ECB regarding a possible September hike



Sentiment deteriorated for both industry and services, with industry performing a lot worse

Economic sentiment dropped for the third month in a row in July (from 95.3 to 94.5), confirming the view provided by the IFO and PMI that the economy is going through a sluggish phase. With GDP growth already trending around the zero line, this means that the risk of recession is increasing somewhat. Still, a prolonged economic slump is not our base case at the moment.

Sentiment deteriorated for both industry and services, with industry performing a lot worse. Order books continue to weaken for industry and production expectations are therefore becoming more pessimistic. This is also resulting in slowing employment expectations. In services, there is some more optimism about business in the coming months, but here we also see dropping employment expectations. This indicates that the labour market is likely to cool further in the coming months.

In terms of inflation, selling price expectations show a mixed picture. For industry, selling price

expectations are down to pre-pandemic levels, indicating that goods inflation is set to trend down quickly in the second half of the year. But for services, selling price expectations ticked up slightly in July, which leaves the risk of a slower trend down to 2% than the ECB might like.

ECB President Christine Lagarde [was very clear yesterday](#) that the next few weeks will be all about interpreting incoming data to determine whether a September rate hike is necessary. While the ESI will of course not be high on that list, today's data do illustrate that there will likely not be any definitive answers provided by the numbers in the coming weeks. There will continue to be room for interpretation, making the September decision particularly challenging for the governing council.

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