

Eurozone PMI paints worrisome growth picture

Another weak PMI for the eurozone confirms a sluggish economy with recession as a downside risk. Inflation pressures for services remain stubborn as wage pressures continue to be a concern. The latter adds to our expectations that the ECB's hiking cycle is not over yet



There is very little to like about today's PMI. In recent months, the PMI has painted a worsening picture of eurozone activity, and August data are no different. The composite PMI dropped from 48.6 to 47 with the services PMI also dropping below 50. Inflationary concerns are not over though.

The manufacturing sector has been in contraction for some time, with new orders falling and backlogs of work easing. This is helping inflationary pressures subside quickly. Services activity held up for a while but is now also showing contraction, according to the survey. While goods inflation is easing on the back of lower costs and weak demand, services inflation remains elevated for now due to increased wage cost pressures – despite weakening demand.

The economic picture that we're seeing is quite worrisome. Growth in the bloc was decent at 0.3% quarter-on-quarter between April and June, but strong Irish growth masked a lot of underlying

weakness. While we expect tourism to have contributed positively to third-quarter growth, business surveys like the August PMI show a picture of deteriorating activity. This makes a recession a realistic downside risk to the outlook.

The main concern that the European Central Bank will have with this reading is the inflationary effect of wage pressures. The economy is cooling off significantly, but hawks on the ECB board will be tempted to push for one more hike as wage pressures are translating into elevated inflation pressures for services. The fact that the selling price inflation indicator from the PMI inched up this month clearly leaves the door open to another ECB rate hike.

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