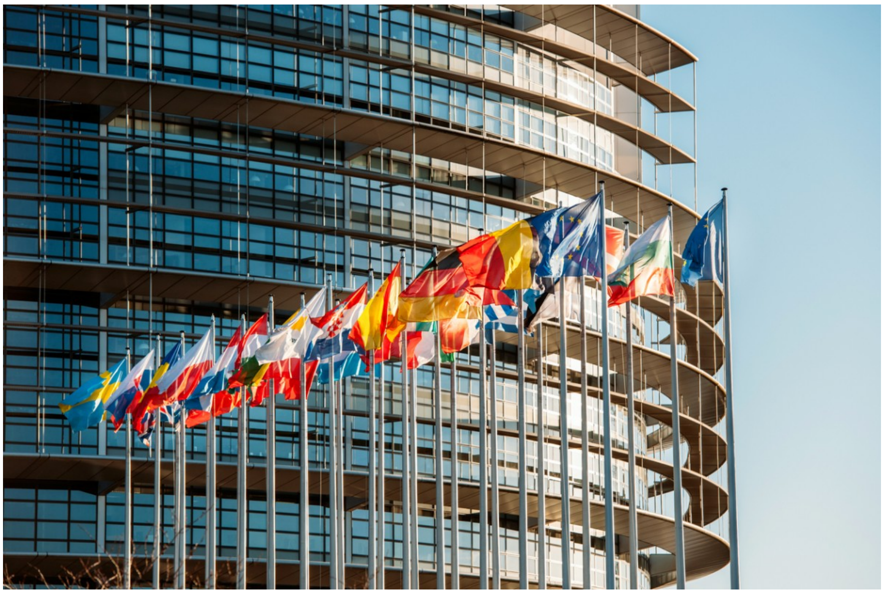
Eurozone PMI provides silver lining to 2Q performance

The increase in the PMI shows that calendar effects may have overstated the slowdown in May, but it doesn't provide much evidence that the soft patch has ended



Source: iStock

After dropping to a one-and-a-half year low in May, the eurozone PMI increased to 54.8 in June from 54.1. While not a fantastic result, the release does provide a silver lining to the current streak of disappointing data from the eurozone. Output growth picked up in the service sector, while the survey for manufacturing output continued to slide. New orders and hiring have been picking up from May, mainly due to a calendar effect as May had a large number of public holidays this year. The overall trend remains subdued compared to the fast-paced growth from late 2017.

As expected, optimism among businesses has been easing. In Germany, there was a split between improved optimism among service sector businesses and tanking confidence among manufacturers. This is where a possible trade war impact would be largest if indeed tariffs for the automobile sector were to go up, as has been alluded to by President Trump.

Even though the soft patch in eurozone data has been dragging on for a while now, pipeline inflation pressures continue to move in the right direction for the ECB. Input prices have been increasing significantly in June and will put more pressure on inflation in the coming months. Service sector businesses indicated a fast increase in price growth, which would bring core inflation on track to improve in the months ahead, confirming the ECB's path towards the exit of quantitative easing.

The eurozone is ending the first half of 2018 much less positively than initially expected. While output growth has maintained a steady pace, 1Q was much slower than 4Q 2017 mainly due to one-off factors. It does not look like 2Q has been much better and while a growth pace of 0.4% quarter on quarter is certainly not bad, it could be that weaker confidence among businesses and consumers will bring permanence to the slower growth pace of the first half year. With trade war worries, the running down of QE and political uncertainty back on the menu, strong fundamentals will probably be met with bouts of concern for the second half of the year as well.

Author

Bert Colijn
Chief Economist, Netherlands
bert.colijn@ing.com