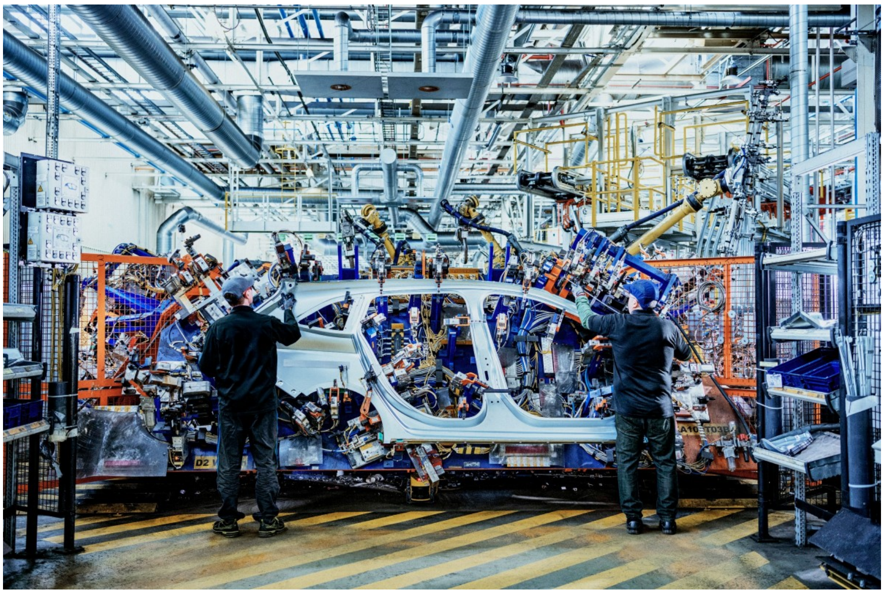
Eurozone PMI remains positive but reveals grim details

A record surge in energy prices is the most immediate impact of the Ukraine war on the eurozone economy, and is set to have a significant weakening effect on GDP in the months ahead



The manufacturing PMI suffered from increased supply chain problems

The most important aspect of today's PMI release was not the headline reading. The composite PMI fell from 55.5 to 54.5 in March, which was a modest drop but leaves it well into positive territory. That suggests that the first weeks of the Russia-Ukraine war have not yet caused output to drop in the eurozone. The manufacturing PMI suffered from increased supply chain problems and higher input prices, causing it to slide from 58.2 to 57. The services PMI also remained in positive territory, mainly thanks to the reopening of economies as pandemic restrictions have eased.

It is the underlying insights from the survey that show more concern about the health of the economy. Most importantly: businesses have clearly been impacted by the surge in energy prices seen since the war started. Both input and output prices surged at a record pace in March. This suggests a broadening of inflation as even higher energy prices are causing passthrough effects to happen more quickly than expected. We already expect inflation to soar above 7% in March and think that prices are set to increase further in April. The impact on consumer purchasing power will be sizable and dampen consumption expectations as already reflected in the plunging consumer confidence figures from yesterday.

Also important is that backlogs of work have been decreasing. Together with dropping business sentiment and weakening real wage growth, this results in a much weaker economic outlook for the months ahead. So while the PMI suggests that eurozone output continued to grow in March, the coming months could well see a much tougher economic environment, and declining GDP can therefore not be ruled out.

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