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Western European Economic Indicators and Insights

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EUROZONE: Contraction Continues?

Surveys May Exaggerate Actual Weakness, But Highlight Downside Risks Continue Ahead

Still very much reiterating the message of the previous data, the October flash PMIs suggest that economic activity in the Eurozone is still contracting and on a broad basis geographically, with fresh weakness seen for Germany, slightly better results for France but output falling at the fastest since May elsewhere.

Clear Volatility in Survey Results

The PMI data at the national levels have been volatile of late, implying perhaps not too much should be read into the drop back in manufacturing activity that was the main feature in this update, this result also being behind the pointer from the aggregated survey to a somewhat steeper contraction for the whole private sector.

Specifically, the manufacturing PMI undershot expectations, sliding afresh, with a 0.8 point drop to 45.3, unwinding most of the gain seen in the six-month high seen in September. Again, in contrast, the flash services PMI moved in the opposite direction to the manufacturing numbers, albeit edging up just 0.1 point after the clear fall seen in September. As for price pressures, these showed output prices falling for the seventh consecutive month, albeit with mixed signals regarding input costs.

Surveys Exaggerating Actual Weakness?

Looking at recent results, and on a Eurozone-wide basis, the aggregated PMI numbers suggest a contraction similar to that of the previous quarter is occurring into Q4, and possibly a little more steeply so. Notably, other alternatively-sourced survey results (such as the German Ifo numbers and the French INSEE business sentiment figures) are also showing soggier signs, now more clearly corroborating the PMI weakness messages. Regardless, official numbers (particularly those such as industrial production that feed directly into GDP) have yet to echo these very downbeat survey results, a development that has belatedly been recognized by the compilers of the PMI figures. Indeed, *it is likely that the Eurozone GDP data for Q3 (due mid-November) will be no worse than the 0.2% slide seen in the previous quarter*, ie less than half the weakness that the PMI numbers are suggesting has been occurring.

But Weakness Clearly Continuing

Given the continuing if not increasing volatility in these PMI numbers, especially in the likes of the French and German components, not too much should be read into the incremental information from this October update save to underline that the Eurozone economy probably remains in recession, albeit more likely than not still modestly so and with the geographical breath unclear.

DE View: Regardless, and perhaps more importantly, *the PMI data underscore that for all the hints of better signs evident in economic signals elsewhere there is no reason for complacency, instead very much highlighting that this on-going recession in the Eurozone has no clear end in sight*, with downside risks still to the fore. A possible added downside risk may be coming from rising input cost pressures, the latter possibly the factor behind the fresh weakness in manufacturing, the latter all the more puzzling given the hints of an improved global backdrop.

At the margin, the data make it more likely the ECB will cut official rates afresh next month, but with a stable decision still the more likely.