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EUROZONE: Strong surge in GDP.

Resilience even among the peripherals

GDP jumped by 0.8% Q/Q in Q1, clearly above expectations and very much up from the 0.3% unrevised pace of the previous quarter (Q3 2010 numbers were revised up a notch). The Q1 advance is the eighth in a row, also being above the average pace in that sequence. As a result, the Q1 Y/Y rate was up half a percentage point to a new cycle-high of 2.5%.

Save for the geographical details, this flash estimate (as usual) comes with no breakdown, neither on the output nor spending side. The latter will be forthcoming on June 8, ie only just in time for the next ECB Council meeting (due the following day) to examine the numbers and potentially include them in its updated economic projections. However, the data very much imply that the ECB will be able to upgrade its estimate for current year growth from the January projections which were based around a range centered on 1.7%.

In regard to the geographical breakdown, this showed very mixed messages, with growth in Germany and France picking up sharply and back above trend, with faster growth also seen in the likes of Belgium, Austria and the Netherlands. As for the fiscally errant countries, growth in Spain was also stronger, albeit modestly so, while there was a surprise fresh rise in GDP in Greece. However, Portugal saw a further contraction while Italy failed to pick up from an anaemic Q4 result (no data for Ireland is yet available).

The overall Eurozone GDP backdrop looks more than respectable and, seemingly, very much echoes the ECB line of positive underlying momentum continuing. Admittedly, the bounce in Q1 GDP is probably nothing more than a further display of the strong quarter-to-quarter volatility seen in the last few years, with part of the strong pick-up in the likes of Germany and Austria accentuated by a pick-up in construction from weather-depressed activity at the end of 2010. Notably, a positive swing in the inventory cycle seemingly accounted for much of the pick-up in GDP, very clearly so in France and the Netherlands where break-downs have been detailed.

In addition the signals regarding consumer spending are hardly inspiring, albeit with hints of greater resilience than recent retail sales data would suggest. However, while consumer spending apparently grew in Germany, it contracted afresh in the Netherlands and only picked up in France as a result of car buying incentives which have now lapsed. All of which points to a still soft consumer backdrop continuing into the current quarter, where high food and energy prices have very much eroded household spending power to a degree that is now taking a toll on consumer sentiment.

As a result, it would be a brave assertion to suggest that underlying Eurozone momentum is picking up. Nevertheless, perhaps the most notable aspect of these Q1 numbers is the resilience in peripheral Eurozone country data, albeit with their still fragile growth rates still showing an increased divergence with the Eurozone vanguard of France and particularly Germany.

As for the ECB, these GDP numbers will probably make it feel more able (and may be somewhat more compelled) to tighten again with a hike in July looking much more likely. It will be aware that, despite the faster GDP gain in Q1, the Eurozone economy still has ample spare capacity given that the level of GDP is still some 2 percentage points below its early-2008 peak, but will view the Q1 GDP as giving it scope to bear down on inflation risks even if the latter are emanating from abroad.