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WEEKLY ANALYSIS

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TEMPORARY LULL ON EUROPEAN RATES

The European economy will avoid recession in Q3. Inflation to stabilize at +8%. Temporary consolidation of yields. Moderate appreciation of the euro. European equity risk premium touches 35%.

Key points

- European economic growth contrasts with US recession
- European GDP growth of +0.7% in Q2 surprises despite German weakness
- Leading indicators increasingly uncertain
- Household confidence at historic low
- Inflation stabilizes near +8% in Q3
- The ECB is belatedly tightening its tone
- Is a rise in the euro possible?
- Temporary lull in European interest rates
- European equity risk premium reaches 35%.

European economic growth contrasts with US recession

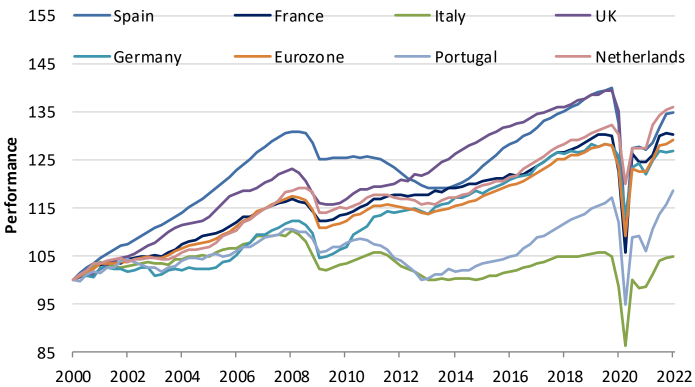
The European economy had already ended the first quarter with growth of +0.5%, significantly higher than expected, even though the geopolitical crisis was already having its first inflationary effects in the second half of the quarter. The resilience of the European economy at the beginning of the year allowed European GDP to grow almost as much as we had expected before the invasion of Ukraine (+0.6%). Europe, although logically more directly affected by the strong increase in uncertainty than the United States and also heavily penalized by inflation, had already clearly surprised observers by recording positive growth, which contrasted with the -1.4% drop in US GDP.

Without the uncertainties having really diminished and in a particularly tense context in terms of oil and gas supply and its effects on inflation, the European economy has still managed to once again outperformed the US economy in the second quarter. While the US saw its GDP fall for the second consecutive quarter by -0.9%, the European economy grew by +0.7% at the end of June. The European economy is surprisingly resilient in the first half of the year, even though it is facing domestic and international headwinds. Domestic demand is affected by the decline in household and business confidence, while external demand is weakening with the US recession and the anaemic growth in China. The European economic slowdown remains, however, widely perceived as inevitable in the second half of the year.

The +0.7% growth of European GDP in Q2 is surprising despite Germany's weakness

The growth was indeed a big surprise, exceeding economists' estimates (+0.2%) while Russian threats to cut off gas supplies were already causing record inflation (+8.9%) and rapidly rising uncertainty. Over a year, European GDP is thus up by +4% and therefore exceeds expectations of a +3.4% increase. Italy (+1%) and Spain (+1.1%) recorded higher increases in their respective gross domestic products thanks to the return of tourists after the previous downturns. In France, the dynamic was again positive (+0.5%), while Germany lost momentum (0%) after a particularly strong first quarter (+0.8%).

Quarterly GDP growth-Europe



Sources: Bloomberg, BBGI Group SA

The reopening of European economies and fiscal support seem to be offsetting the effects of the energy crisis for the time being, but the European economy has probably not yet faced the full impact of the reorganization of energy sources. The outlook for the second half of the year is still very uncertain. The current quarter should still allow the southern European countries to benefit from a very promising return of tourists. But the pressure on household purchasing power from