

ECONOMIC RESEARCH – JUNE 2025

INVESTMENT INSIGHT

EUROPE



- ✓ Leading indicators remain moderately optimistic
- ✓ Household confidence set to improve
- ✓ Inflation falls back below ECB target (+2%)
- ✓ ECB to cut rates below 2%

CONFIDENCE GROWS STRONGER

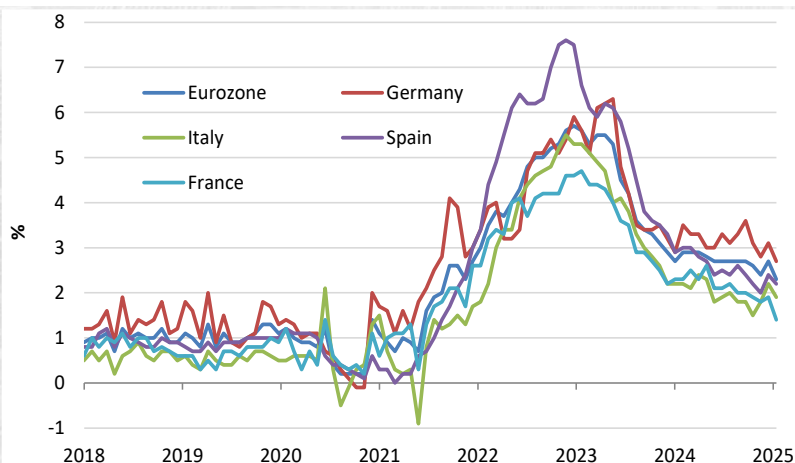
Leading indicators show cautious optimism

Leading economic indicators for the second quarter of 2025 suggest a continuation of growth in the Eurozone, albeit at a very slow pace. While the manufacturing sector is showing signs of stabilizing, the services sector, which has been the primary driver of recent activity, appears to be losing momentum. This divergence highlights a nuanced and somewhat indecisive economic landscape.

Household confidence remains stagnant

Despite a significant number of rate cuts by the ECB and a fall in inflation, household confidence in the Eurozone has failed to improve, remaining at historically low levels. This stagnation in consumer sentiment is a surprising and unprecedented situation. Consumers remain cautious and reluctant to make major purchases, which could dampen household consumption and confirm that the economic recovery is still fragile. This lack of confidence is a major obstacle to a more robust and sustainable recovery, as domestic demand is a key component of economic health.

Eurostat CPI - Underlying inflation (Eurozone YoY)



Sources : Bloomberg, BBGI Group

Sectoral divergence and regional contrasts

A closer look at the data reveals a notable divergence between economic sectors. While the manufacturing sector has shown signs of recovery, with the PMI improving from 45.2 to 48.7, it remains below the key growth threshold of 50. In contrast, the services sector, which has been a primary driver of activity, appears to be losing momentum. This is compounded by striking regional differences, with a clear deterioration in French PMI indicators contrasting with a more fragile but improving signal from Germany. This uneven recovery highlights the lack of a cohesive economic dynamism across the bloc.

Inflation stabilizes around the ECB's target

After a period of gradual decline, headline inflation in the Eurozone has stabilized near the ECB's target, with a year-on-year rate of 1.9% in May. While underlying inflation, which excludes volatile components, remains slightly higher at 2.3%, the overall trend is favorable. The continuing disinflation in producer prices, which fell by -2.2% month-on-month in April, further supports the outlook for future price moderation. This positive development provides the ECB with the necessary data to justify its continued policy of gradual monetary easing.

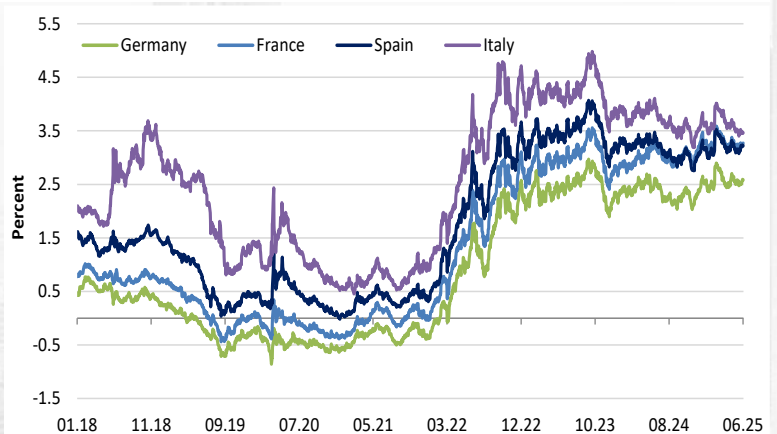
The ECB navigates a complex policy landscape

The favorable inflation trend has been a key factor in the ECB's ability to maintain its policy of gradually lowering interest rates. Its latest 0.25% rate cut in March was made possible by the continued decline in price growth. However, with inflation now approaching the 2% target, the central bank faces a dilemma: whether to pause its actions to avoid overshooting or to continue providing support to a fragile economy. This decision will be influenced by the ongoing moderation of wage growth, which is a key component of services inflation.

Future policy hinges on external risks

The path of future ECB policy is highly uncertain due to external risks, most notably the threat of US tariffs. The current slow and fragile growth trajectory justifies continued support from the institution. However, the potential for a trade war could not only slow international trade but also trigger a resurgence of inflation, complicating the ECB's policy decisions. These factors, combined with the extreme difficulty in estimating the full impact of a trade war, will likely prompt the ECB to resume its rate cuts in September. We anticipate the ECB will continue its gradual easing, with key rates likely to fall below 2% in the coming months, reflecting its commitment to supporting growth while managing inflation expectations.

10-year interest rates European countries



Sources : Bloomberg, BBGI Group

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