

EUROPEAN CONSUMERS STILL FIRMLY IN THE WOODS

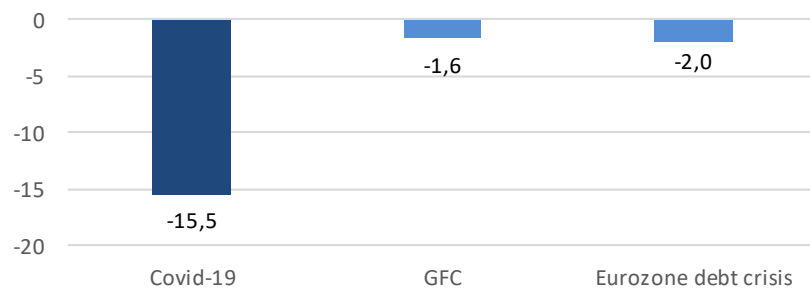
3 September 2020

KATHARINA UTERMÖHL, CFA
Senior Economist Europe
Katharina.uterhoehl@allianz.com

AURÉLIEN DUTHOIT
Sector Analyst
Aurelien.duthoit@eulerhermes.com

All eyes on the European consumer: Private consumption is key in determining the shape and speed of the Covid-19 recovery. Given the sharp setback in consumer spending in H1 2020, which far exceeded anything seen during the Great Financial Crisis as well as the Eurozone debt crisis, without a meaningful rebound in private consumption, economic recovery prospects will remain rather dim.

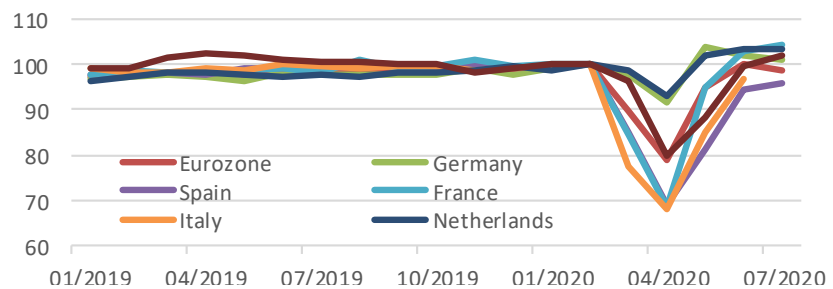
Figure 1: Maximum drop in Eurozone private consumption relative to pre-crisis level



Sources: Refinitiv, Allianz Research.
*Forecast for H1 2020

This explains the widespread excitement about the apparent V-shaped recovery in European retail sales that has materialized since governments across the region lifted lockdown restrictions from late April onwards. Several major European economies including heavyweights such as Germany, France, the Netherlands and the UK have returned to or even exceeded February - i.e. pre-crisis - retail sales levels.

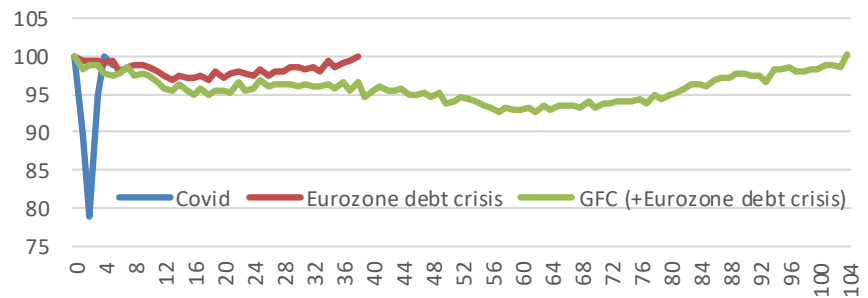
Figure 2: Retail sales, except motor vehicles, Index: Feb 2020=100



Sources: Refinitiv, Allianz Research.

Strikingly, the pace of the current retail recovery far exceeds what we saw in the wake of the Great Financial Crisis and the Eurozone debt crisis.

Figure 3: Eurozone retail recoveries in comparison (Index: 100= pre-crisis level, in months)

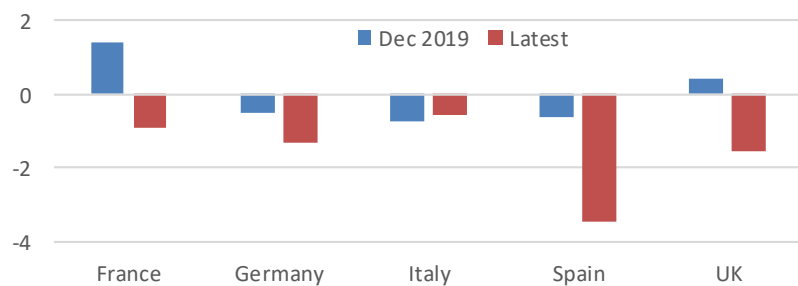


Sources: Refinitiv, Allianz Research.

But a V-shaped retail recovery in the immediate crisis aftermath does not make a V-shaped private consumption recovery. In particular, we see three reasons why the consumer recovery in Europe will look quite detached from the trend in retail trade:

1. **Retail sales \neq private consumption:** In fact, retail sales are not a very good proxy for the pulse of the consumer. After all, they make up only around 45% of private consumption, with the remainder consisting above all of housing-related expenses as well as services. It is the latter (around 25% of the total) that will be disproportionately more affected in the current crisis as “social expenditure” is cut back out of lingering contagion fears.

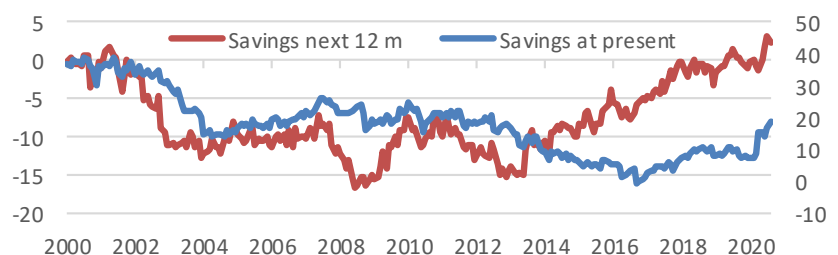
Figure 4: Consumer confidence: Dec 2019 vs. latest available



Sources: Refinitiv, Allianz Research.

A better gauge for private consumption prospects is therefore consumer confidence, which still remains quite depressed, registering below the long-term average across European economies, alongside [sky-high saving intentions](#).

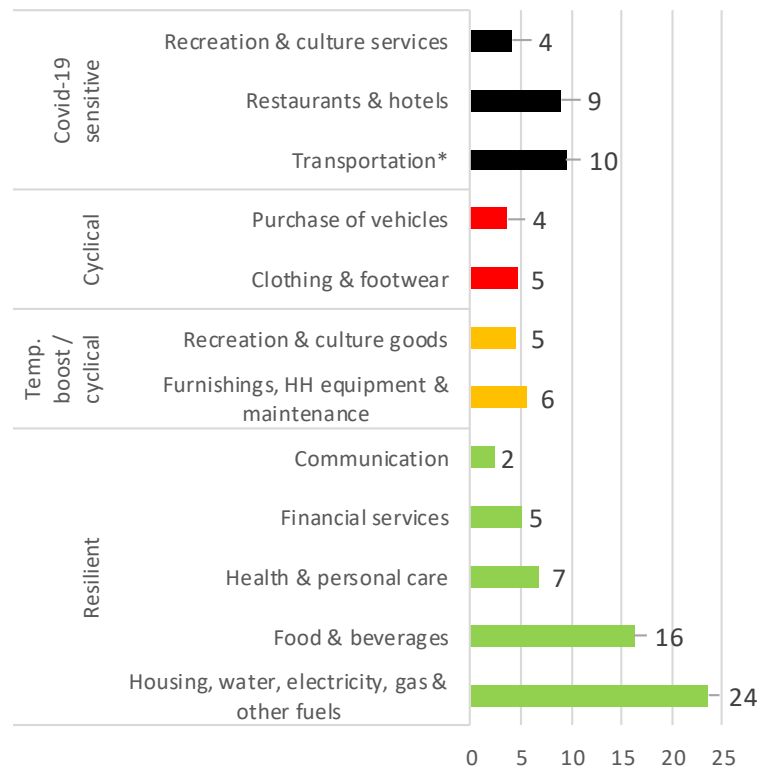
Figure 5: Eurozone consumer confidence - Savings at present (rhs) vs. savings next 12m (lhs)



Sources: Refinitiv, Allianz Research.

- Doomed durables – prepare for a W-formation in retail trade:** The sharp rebound in retail trade has been propped up by a temporary boost in durable goods, which is unlikely to continue. For instance, furnishings and recreation & culture goods proved quite resilient in Q2 as consumers spent more of their disposable incomes on beautifying homes and gardens and setting up virtual offices during the lockdowns. Moreover, the temporary VAT reduction in Germany added additional tailwind. However, we don't think that spending on these durables (around 11% of total private consumption), which tends to be closely related to the cycle, can remain immune to the Covid-19 downturn for much longer.

Figure 6: Eurozone private consumption by component (% of total)



Sources: Refinitiv, Allianz Research.

Note: Transportation here excludes purchase of vehicles

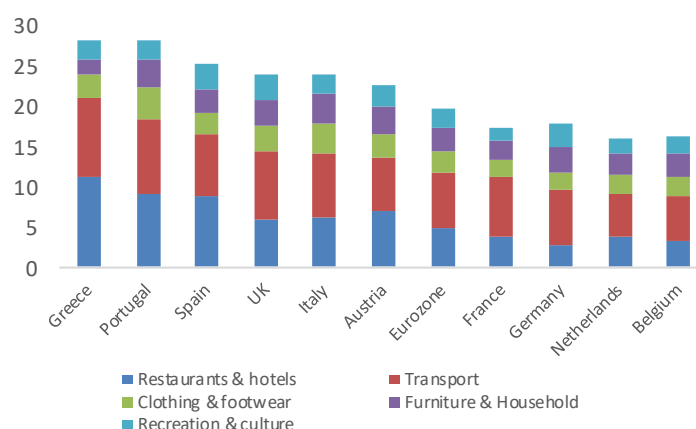
This is particularly true with [unemployment set to rise further](#) over the coming months as income-support schemes are phased out and insolvencies are expected to pick up. In fact, it is time to acknowledge that even without a meaningful second infection wave the V-shaped rebound in retail trade will turn out to be solely the first leg of a W-shaped recovery formation.

- Mind the Covid-19 specific consumption headwinds:** In addition to the usual recession victims such as cyclical durables but also clothing & footwear, the peculiarities of the Covid-19 downturn, i.e. ongoing contagion concerns, will continue to put additional consumption components under immense pressure. Covid-19 sensitive spending centers on "social expenditure" and therefore

includes transportation, restaurants & hotels and recreation & culture services. These vulnerable components represent almost one fourth (23%) of total private consumption in the Eurozone. A return to pre-crisis spending patterns will therefore hinge on the availability and wide distribution of a vaccine.

Taking together these findings, what does that mean for the recovery outlook across European economies? Adding up recession and Covid-19 sensitive sectors as a share of national GDP underlines the highly divergent recovery prospects across Europe. After all, the sum of consumption components at risk during the current downturn range from 13% of GDP in Belgium to twice that with 26% in Greece. Interestingly our calculations see a greater risk for the private consumption recovery in Greece, Portugal, Spain and the UK than in Italy.

Figure 7: Recession and Covid-19 sensitive consumption components (% GDP)



Sources: Refinitiv, Allianz Research.

What will be the impact on corporates? The recovery in activity seen across many consumption-driven sectors is likely to be short-lived. Retailers, in particular, should not expect a full-fledged and sustainable recovery in retail sales. The post-lockdown retail surge, which saw consumers to some degree make up for lost time, will progressively fade away and consumers will start to feel the bite of rising unemployment. Meanwhile, profit margins will continue to suffer from rising price pressures and the extra costs associated with running stores amid a major sanitary crisis.

These assessments are, as always, subject to the disclaimer provided below.

FORWARD-LOOKING STATEMENTS

The statements contained herein may include prospects, statements of future expectations and other forward-looking statements that are based on management's current views and assumptions and involve known and unknown risks and uncertainties. Actual results, performance or events may differ materially from those expressed or implied in such forward-looking statements.

Such deviations may arise due to, without limitation, (i) changes of the general economic conditions and competitive situation, particularly in the Allianz Group's core business and core markets, (ii) performance of financial markets (particularly market volatility, liquidity and credit events), (iii) frequency and severity of insured loss events, including from natural catastrophes, and the development of loss expenses, (iv) mortality and morbidity levels and trends, (v) persistency levels, (vi) particularly in the banking business, the extent of credit defaults, (vii) interest rate levels, (viii) currency exchange rates including the EUR/USD exchange rate, (ix) changes in laws and regulations, including tax regulations, (x) the impact of acquisitions, including related integration issues, and reorganization measures, and (xi) general competitive factors, in each case on a local, regional, national and/or global basis. Many of these factors may be more likely to occur, or more pronounced, as a result of terrorist activities and their consequences.

NO DUTY TO UPDATE

The company assumes no obligation to update any information or forward-looking statement contained herein, save for any information required to be disclosed by law.