Will household spending save Europe in 2025?

20 january 2025

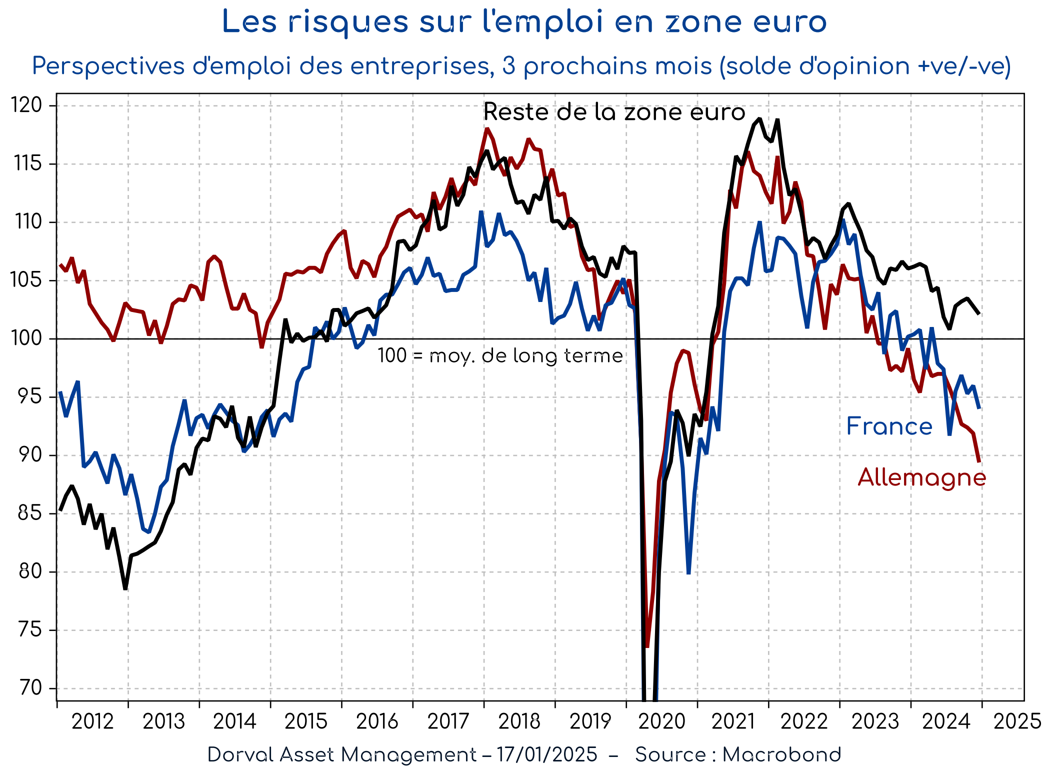
Dear clients, dear partners,

The prospect of a trade war is raising questions about growth forecasts in Europe. Under certain conditions, household spending could play a positive role in 2025.

While the economic world awaits the announcement of Donald Trump's first measures on trade, Europe faces major challenges. The IMF's latest projections call for Eurozone GDP growth of 1% in 2025, after 0.8% in 2024, down 0.2% on the forecasts made in October 2024. The downside risks for European growth relate both to the impact of trade uncertainties on business investment, and to an overly pronounced weakening of the labor market. In France, and even more so in Germany, companies are increasingly pessimistic about employment. This pessimism is partly offset by greater resilience in other countries, particularly in Southern Europe, but it remains a cause for concern (graph 1).

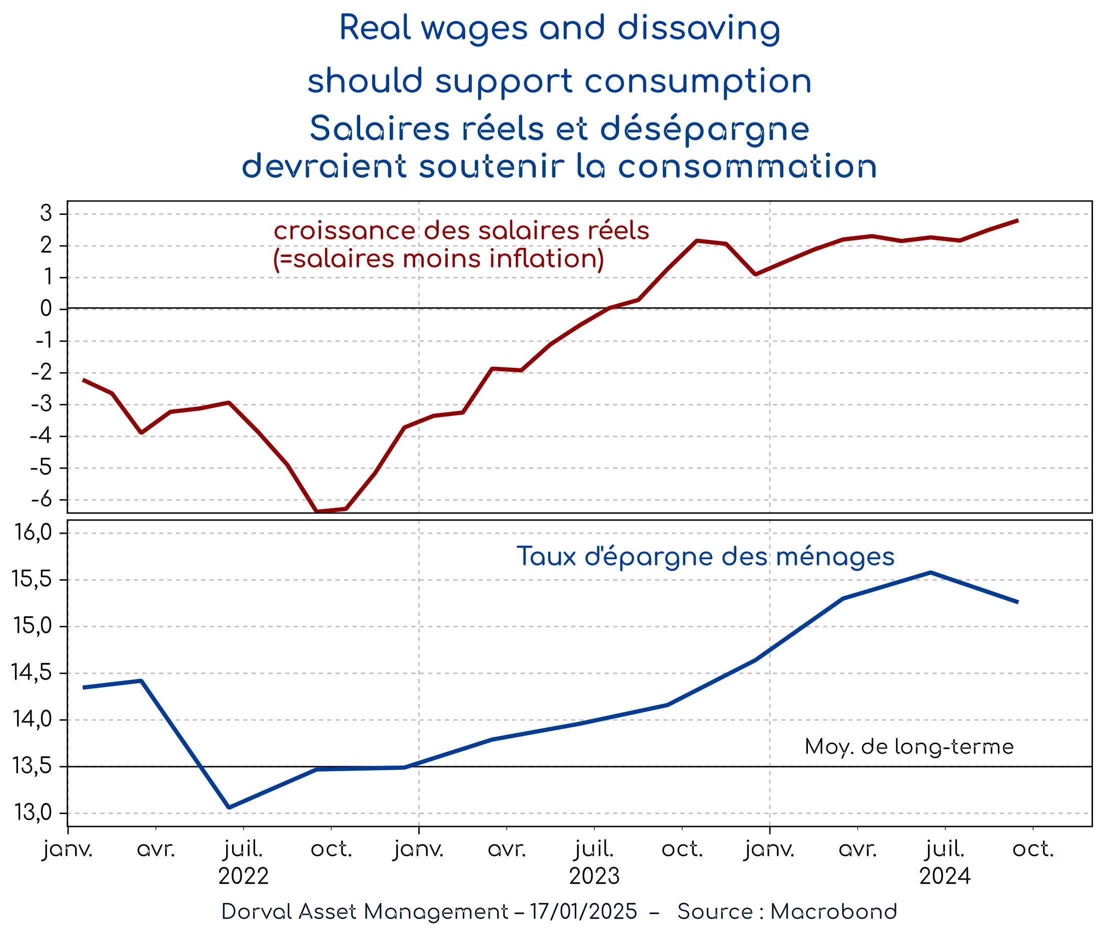
Employment risks in the euro zone

Business employment outlook, next 3 months (balance of opinion +ve/- ve)



Rest of euro zone / 100= long-term average / France / Germany

The labor market issue is central, as it is the main threat to the outlook for household spending. The other fundamentals are much more positive (graph 2), with gains in purchasing power enabled by disinflation, a high savings rate that should gradually normalize, and falling money market interest rates. The ECB's latest survey of eurozone households, which covers the month of November, suggests that households expect their consumption to grow by +3.5% over the next twelve months, or around +1.5% excluding inflation (compared with +0.9% in 2024).



Real wage growth (=wages minus inflation) / Household savings rate / Long-term average

These positive expectations could be consolidated by the end of the fall in property prices, which have even started to rise again in most European countries (graph 3). Figures are not yet available, but it is now very likely that average property prices in the eurozone reached a new all-time high in Q4 2024. The recent rise in long-term interest rates, which remains very moderate, may well limit the rise in property prices, but all the signs are that the ECB's policy has already both reactivated the bank lending channel and stimulated demand. In the light of these developments, the eurozone does not appear to be threatened by a Chinese-style deflationary spiral. On the contrary, the recovery in the real estate market may help to boost consumption, both through the wealth effect and via purchases associated with house moves.

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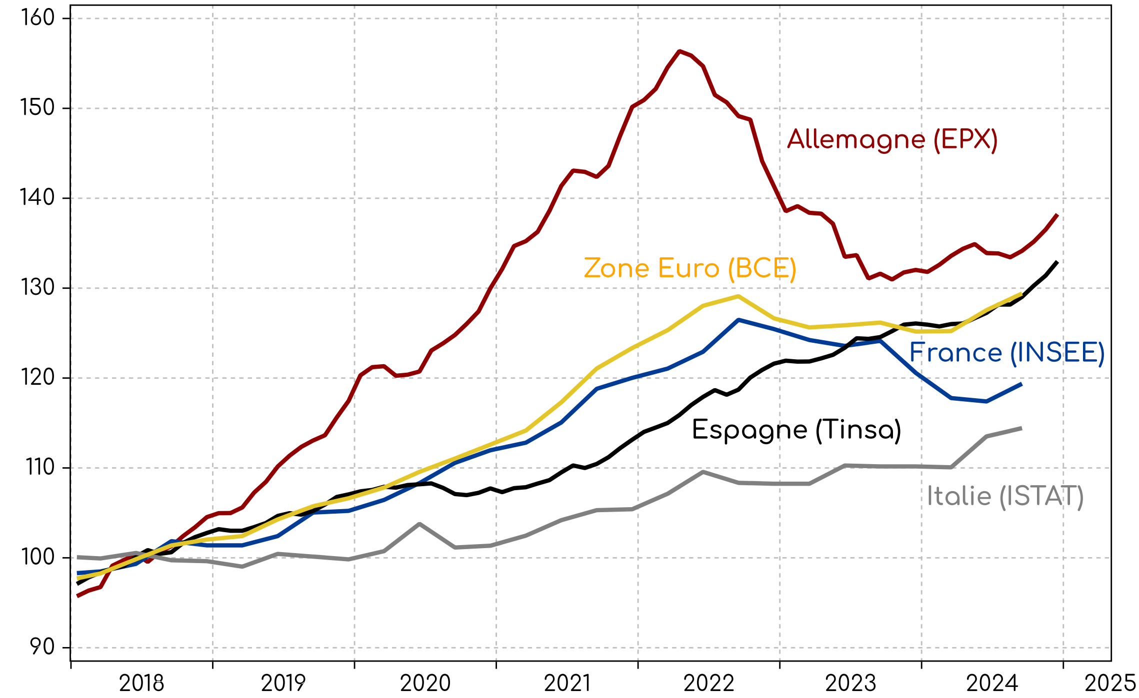
Eurozone property prices back on track

Prices base 100 in 2018

Remontée des prix de l'immobilier en zone euro

Prix base 100 en 2018



Dorval Asset Management – 17/01/2025 – Source : Macrobond

Germany (EPX) / Euro zone (ECB) / France (INSEE) / Spain (Tinsa) / Italy (ISTAT)

Between these positive fundamentals and the risks associated with the looming trade war and the weakening employment situation, the outlook for household spending hangs in the balance. The European policy mix will have to absorb these risks by continuing to ease financial conditions and limiting budgetary restrictions. At this stage, and despite the high level of uncertainty, we believe that European domestic demand should prove resilient. In our portfolios, this scenario is expressed by an above-neutral exposure to equities in our European flexible funds, by an overweighting of financial stocks, and by investment in a basket of small stocks whose sales are predominantly in Europe.

Our exposure rates are as follows:

- **Dorval Convictions: 65% net exposure to equities, comprising 60% Euro STOXX 50 SRI core basket, 6.5% financials basket, 6% small-caps basket. Hedged using Euro STOXX 50 futures.**

Dorval Asset Management

Public limited company with share capital of €493,876

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