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Eurozone contraction smaller than feared

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By Ralph Atkins in Frankfurt

The eurozone economy contracted significantly late last year, although less than feared after an unexpectedly robust performance by France partly offset chronic weakness across crisis-hit southern Europe.

Eurozone gross domestic product fell 0.3 per cent in the fourth quarter compared with the previous three months, highlighting the impact of the region's growing debt crisis.

Italian GDP fell 0.7 per cent, plunging the country into recession – defined as two consecutive quarters of contraction. Greece and Portugal were in deep recession throughout 2011, official data confirmed this week. Spain's economy contracted 0.3 per cent in the fourth quarter.

Northern Europe was also hit. The Netherlands reported a surprise fourth quarter contraction of the same size as Italy's, reflecting fiscal austerity measures.

Eurozone policymakers were relieved, however, by the surprise expansion of 0.2 per cent in French GDP over the same period, boosted by exports. Germany, meanwhile, reported a smaller than expected 0.2 per cent fourth quarter contraction.

The “core” eurozone economies at least were likely to avoid a deep recession, said Gilles Moec, European economist at Deutsche Bank, with “the balance of risks, for France and the euro area in aggregate, oscillating between shallow recession and subdued growth”. That reflected a substantial improvement compared with a few months ago “when the data were replicating the slopes seen in 2008-2009.”

Survey data have led the European Central Bank to spot signs of “stabilisation” across the eurozone and Germany's economy may already be rebounding, with local economic sentiment indicators rising. Its optimism has discouraged speculation about more cuts in the ECB's main interest rate from the current 1 per cent, a record low.

Financial market sentiment has been helped by the ECB's injection in December of €489bn in three year loans into the eurozone banking system. Erik Nielsen, chief economist at UniCredit, argued that the ECB's success in ensuring credit flowed into the real economy would be crucial “otherwise you will continue to get a double whammy – a big fiscal tightening and a big monetary policy tightening”.

Any rebound in the first weeks of this year would have been hit, however, by the exceptionally bitter weather, which caused widespread economic disruption.

Moreover, southern European economies remain fragile, with Italy's plunge into recession highlighting the the challenge facing Mario Monti, the country's prime minister.

The eurozone's 0.3 per cent fall in fourth quarter GDP compared with a 0.2 per cent contraction over the same period in the UK – and a 0.7 per cent expansion in the US economy.

After a brisk start to 2011, eurozone growth quickly decelerated, with stark north-south divergences emerging. In the third quarter, overall eurozone GDP rose just 0.1 per cent. France's economy, however, grew 0.3 per cent in the third quarter.

Germany's third-quarter figures were revised on Wednesday revised to show a 0.6 per cent expansion over the previous quarter – up from the 0.5 per cent reported previously. Germany's statistical office said a positive contribution to growth in the fourth quarter had come from investment – especially in the building sector, which suggested that the unusually mild start to the winter had been an important factor.

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