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Crawl before fall

BY EDWARD HADAS

Europe: The eurozone economy is stabilising. While the first estimate of the region's GDP in the second quarter showed a tiny 0.1% decline, there were increases of 0.3% in both Germany and France. But cheers should be muted.

Sure, positive surprises are welcome after many months of deterioration. The consensus expectation of eurozone GDP change for 2009 moved from 0.5% growth last October to a 4.2% decline in June, before improving to a 4% decline in July, according to research boutique Consensus Forecasts. Expectations are likely to become less negative once again.

If this recession were to follow the recent historical pattern, the forecasts would soon be moving up dramatically. In the four downturns since 1974, eurozone GDP declined an average of 1.1%, followed by an average 4.7% cumulative growth in the two years following the trough, according to BNP Paribas. The shrinkage this time has been 5%, suggesting near double-digit percentage growth rates during the recovery.

Some economists are already talking about such a v-shaped recovery in the eurozone and around the world. But this time could well be different – and more difficult.

To start, the recession has hit so much of the world that few countries can rely on sustained export growth to pull them out of trouble. That is especially true of eurozone members, since their currency is expensive and demand for capital goods - the region's strong point - won't return in strength until a global recovery is well established.

The main challenge to growth, though, is financial. A still crippled global credit system will keep consumers and businesses cautious. The end of preternaturally low policy interest rates and frighteningly high government deficits isn't yet in sight, but the transition to normality could easily go wrong.

The relevant precedents are both discouraging. Japan, which resembles the eurozone in its savings culture and ageing population, has never fully recovered from the excesses of the 1980s. And the US central bank's attempt to keep a non-inflationary recovery on track with a tightening in 1936 caused a recessionary relapse.

Enjoy the good news while it lasts. There are reasons to suppose it may not last that long.

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Context News

On 13 August, France and Germany both surprised markets by reporting provisional second quarter GDP growth of 0.3%. Consensus forecasts had pointed to a 0.2% contraction in each. In the eurozone as a whole, GDP declined by a less-than-forecast 0.1%.