BEA 東亞銀行

Economic Research **March 2024**

Market Monitor – Europe

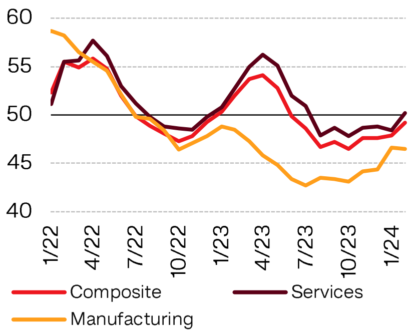
Somewhat Less Gloomy in Early 2024

- The eurozone's PMI further recovered from the doldrums, with uneven performance across the member states. Similarly, the UK's economy also showed signs of stabilisation after entering into a recession in 2H 2023.
- The overall disinflation trend continues, but the last mile might prove bumpy.
- The ECB and the BoE confirmed signs of disinflation, but will need more confidence to declare victory.

Recovering from last year's autumn doldrums

The Eurozone's PMI edged towards a boom-bust dividing level, with uneven performance geographically. The eurozone composite purchasing managers' index (PMI) picked up from 47.9 to 49.2 in February 2024, signalling further recovery from the relatively depressed level in autumn last year. Specifically, the services PMI recorded the first expansion since August 2023 at 50.2, driven by stabilising job creation and business outlook, offsetting the weak momentum in the manufacturing sector (manufacturing PMI: 46.5, edged down from 46.6). Geographically, France recorded a notable rebound with its composite PMI rising from 44.6 to 48.1, but Germany was still a major drag with its composite PMI declining to a relatively low level of 46.3 from 47.0. The southern European economies such as Italy and Spain continued to stay resilient, driven by their robust services sectors (Composite PMI for Italy: 51.1, up from 50.7; Spain: 53.9, up from 51.5).

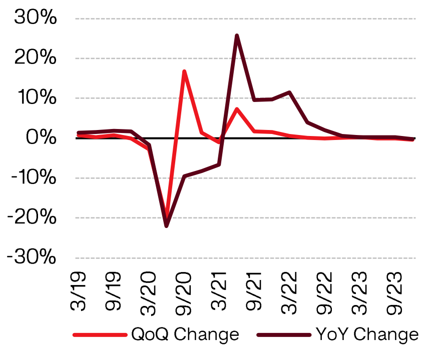
Eurozone Purchasing Managers' Index



Source: Bloomberg

The UK's economy entered into a technical recession in 2H 2023, but the latest PMI showed signs of stabilisation. The UK's gross domestic product (GDP) contracted for the second consecutive quarter in Q4 2023 with a quarter-on-quarter (QoQ) decline of 0.3%, following a QoQ fall of 0.1% in Q3. Among the major expenditure components, net trade was the main drag on QoQ GDP growth, subtracting by 0.63 percentage points (ppts); while household and government consumption were also weak (-0.08 and -0.06 ppts to headline growth, respectively). Together, they offset the positive contribution of gross fixed capital formation (+0.44 ppts). For 2023 as a whole, the UK GDP grew slightly by 0.1%. Nevertheless, the UK composite PMI edged up from 52.9 to a solid 53.0 level in February 2024, pointing to a steady expansion in the first two months of 2024. The prospect of interest rate cuts was cited as a factor driving business and consumer spending, particularly in the services sector.

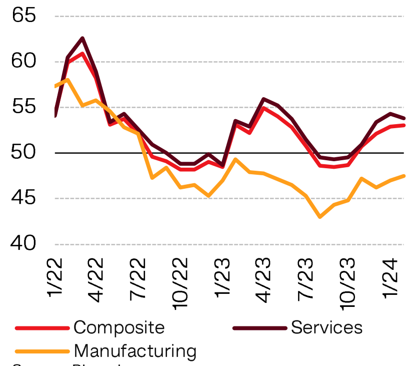
UK Gross Domestic Product



Source: CEIC

The UK Spring Budget 2024 (Budget) offered a modest near-term boost to households, with limited impact on overall economic growth and inflation. The Budget proposed another 2-ppts cut in employee National Insurance Contribution, and a freeze on fuel and alcohol duty in a bid to provide further support to households. However, these measures are only partly funded by the fiscal headroom based on the latest revenue and economic forecasts, while the remaining will be funded by small revenue-raising measures, such as an extension of the Energy Profit Levy, and the end of the non-domiciled regime. As such, the net impact on overall economic growth and inflation is expected to be limited and not likely to affect the Bank of England's (BoE) monetary policy stance ahead.

UK Purchasing Managers' Index



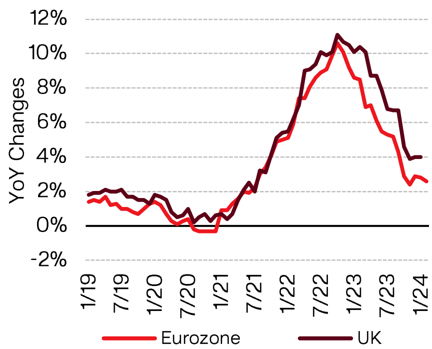
Source: Bloomberg

Central banks need more evidence for sustained disinflation

The eurozone's inflation continued to slow moderately. Both headline and core consumer price inflation decelerated by 0.2 percentage points to 2.6% and 3.1% year-on-year (YoY) in February 2024, while their respective month-on-month (MoM) growth still increased by 0.6% and 0.7%, indicating the last mile of the disinflation process could be lengthy. The decline in energy prices (-3.7% YoY) and further slowdown in non-energy industrial goods' prices (from +2.0% to +1.6% YoY) continued to lead the disinflation process. However, food, alcohol & tobacco prices stayed relatively high at 4.0% YoY, and services prices only edged down one-tenth to 3.9%.

The UK's inflation held steady in January 2024. The headline and core inflation in the UK stayed at 4.0% and 5.1% YoY, remaining unchanged compared to December 2023, both below expectations for a slight uptick due to a utility price rise and positive base effects kicked in. Goods inflation edged lower by one-tenth to 1.8% YoY in January, of which furniture and household goods slowed notably from 2.5% to 0.4% YoY. However, services inflation slightly accelerated by one-tenth to a still elevated 6.5% YoY level, indicating the stickiness of services inflation. Specifically, communication services, restaurants & hotels and recreation & culture prices continued to have little change and stayed high at 8.2%, 7.0% and 5.7% YoY, respectively.

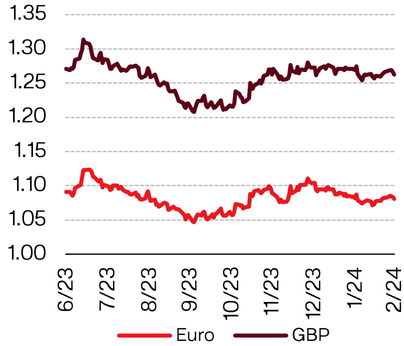
Inflation Rate



Source: CEIC

The ECB and the BoE confirmed signs of disinflation, but will need more confidence to declare victory. For the European Central Bank (ECB), the negotiated wage grew by 4.5% YoY in Q4 2023, the first slowdown since Q2 2022, indicating initial signs of moderating wage pressures and possibly services inflation. However, the wage data remains higher than the level (around 3%), consistent with the ECB's 2% inflation target. In the latest ECB's monetary policy meeting, they kept policy rates on hold as expected, while the ECB's President Lagarde said that "a little more" information will be available in April and "a lot more" in June. This opens the door for policy change in June, but whether ECB will move or not remains entirely data-dependent. For the UK, the BoE Governor Andrew Bailey confirmed encouraging signs of disinflation, but also highlighted robust employment and a recent economic uptick after a technical recession in 2H 2023. Similarly, the BoE also wants to see more evidence of disinflation towards its target amid still elevated services inflation.

Euro & British Pound against USD



Source: Bloomberg, data as of 29/2/2024

Financial markets were fuelled by positive market sentiment

Positive sentiment drove equity markets mostly higher in February. With inflation having peaked, the market expects the central banks, including the ECB and BoE, to cut rates later this year, leading to generally positive market sentiment. In addition, the technology sector, particularly artificial intelligence (AI) related companies in the US, staged a very strong performance, driving buoyant equity market performance across the globe. At the end of February 2024, the German DAX index and the French CAC index increased solidly by 4.6% and 3.5%, respectively, while the UK FTSE 100 index stayed flat. The euro and British pound closed at US$ 1.0805 and US$ 1.2625 in February 2024, respectively, representing a slight depreciation of 0.1% and 0.5% over the previous month.

Disclaimer

This material is prepared by The Bank of East Asia, Limited ("BEA") for customers' reference only. The content is based on information available to the public and reasonably believed to be reliable, but has not been independently verified. Any projections and opinions contained herein are expressed solely as general market commentary, and do not constitute an offer of securities or investment, nor a solicitation, suggestion, investment advice, or guaranteed return in respect of such an offer. The information, forecasts, and opinions contained herein are as of the date hereof and are subject to change without prior notification, and should not be regarded as any investment product or market recommendations. This material has not been reviewed by the Securities and Futures Commission of Hong Kong, Hong Kong Monetary Authority, or any regulatory authority in Hong Kong.

BEA will update the published research as needed. In addition to certain reports published on a periodic basis, other reports may be published at irregular intervals as appropriate without prior notice.

No representation or warranty, express or implied, is given by or on behalf of BEA, as to the accuracy or completeness of the information and stated returns contained in this material, and no liability is accepted for any loss arising, directly or indirectly, from any use of such information (whether due to infringements or contracts or other aspects). Investment involves risks. The price of investment products may go up or down, and may become valueless. Past performance is not indicative of future performance. The investments mentioned in this material may not be suitable for all investors, and the specific investment objectives or experience, financial situation, or other needs of each recipient are not considered. Therefore, you should not make any investment decisions based solely on this material. You should make investment decisions based on your own investment objectives, investment experience, financial situation, and specific needs; if necessary, you should seek independent professional advice before making any investment.

For more information, please visit our webpage at https://www.hkbea.com/html/en/bea-about-bea-economic-research.html. For any enquiries, please contact the Economic Research Department of BEA (email: lerd@hkbea.com/telephone number: (852) 3609-1504/postal address: GPO Box 31, Hong Kong).