Economic Research

May 2024

Market Monitor – Europe

European economy returned to moderate growth

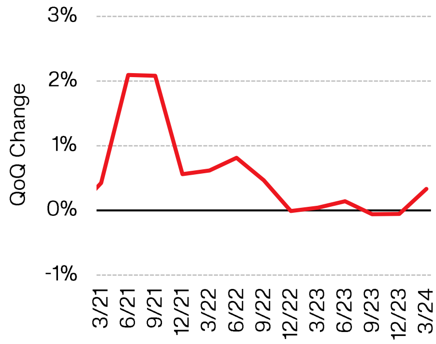
- The eurozone economy returned to growth in Q1 2024, with a broad-based improvement among member states. The UK economy also recovered further.
- Inflation in Europe has largely moderated.
- Forward guidance from the ECB and the BoE has turned dovish, with the ECB likely to cut rates earlier, possibly in mid-2024.

The European economy broadly recovered in early 2024

Eurozone economic growth momentum beats expectations. Amidst improving external demand and softening inflation, the eurozone's economy resumed growth, with real GDP growth rising by 0.3% quarter-on-quarter (QoQ) in Q1 2024, following the 0.1% declines in Q3 and Q4 2023. The 0.3% QoQ growth in Q1 2024 was the fastest pace since Q3 2022. On a year-on-year (YoY) basis, the eurozone economy expanded by 0.4% in Q1 2024.

A broad-based improvement was noted among eurozone member states. France and Germany reported stronger output, both rising by 0.2% QoQ in Q1 2024, up from +0.1% and -0.5% in Q4 2023, respectively. During the quarter, construction and exports helped lift modest growth in Germany, while France's growth was underpinned by household consumption and investment. Italy's economy also grew faster by 0.3% QoQ in Q1 2024, up from 0.1% in Q4 2023. Spain's economic momentum held up, as GDP growth remained unchanged at 0.7% QoQ in Q1 2024. Besides, Ireland's economy bounced back visibly from a 3.4% QoQ decline in Q4 2023 to growth of 1.1% in Q1 2024.

Eurozone Economic Growth



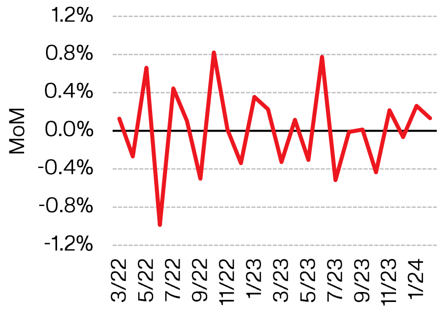
Source: CEIC

Economic Research

May 2024

The UK economy recovered further in early 2024. The UK's GDP expanded by 0.1% month-on-month (MoM) in February, following an upward-revised growth of 0.3% in January. Among the major sectors, production output played a key role in driving growth in February, rebounding by 1.1% MoM after a 0.3% drop in January. Besides, services output edged up by 0.1% MoM in February, making a positive contribution to growth for two consecutive months. However, construction output contracted by 1.9% MoM in February. On a three-month basis, the UK's GDP grew by 0.2% from December 2023 to February 2024, compared to the three months to November 2023. Meanwhile, business surveys pointed to continued expansion ahead. The UK's composite PMI stood at 54.1 in April, having stayed in expansionary territory since November 2023. Growth was led by the services sector, with its PMI at 55.0 in April, while manufacturing PMI fell into contractionary territory at 49.1 in April, down from 50.3 in March.

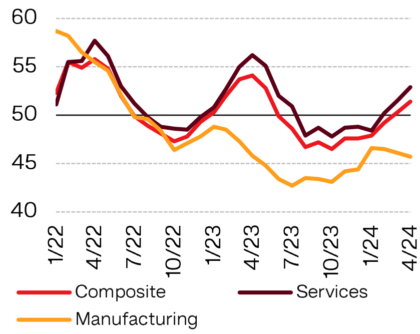
Monthly UK Gross Domestic Product



Source: CEIC

The eurozone's business sentiment showed further improvement in April. The eurozone's PMI rose from 50.3 in March to 51.7 in April, remaining in expansionary territory for the second month and representing the highest reading since June 2023. The services sector continued to drive growth, with its PMI surging from 51.5 in March to 53.3 in April, the third consecutive month of expansion. On the other hand, manufacturing PMI weakened, falling from 46.1 in March to 45.7 in April. Overall, economic divergence was still visible among the member states. Germany and France reported mild output expansion, with their final composite PMIs at 50.6 and 50.5 in April, respectively. Meanwhile, Italy and Spain performed strongly, with their PMIs largely steady at 52.6 and 55.7 in April, respectively. Taken together, the eurozone's economic momentum showed further signs of improvement, albeit at varying paces across different sectors and countries.

Eurozone Purchasing Managers' Index

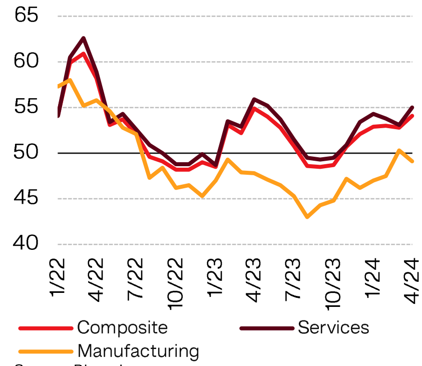


Source: Bloomberg

Central banks signalled rate cuts are on the way

Inflation in the eurozone remained stable. In April, the eurozone's headline and core CPI grew by 2.4% and 2.7% YoY, respectively, compared to 2.4% and 2.9% in March. On a MoM basis, the eurozone's headline and core CPI inflation eased slightly to 0.6% and 0.7% in April, down from 0.8% and 1.1% in March, respectively. Most notably, services inflation slowed to 3.7% YoY in April after hovering at 4.0% in the five months ending in March. While inflationary pressures have not yet fully subsided, recent months of progress in slowing inflation in the Eurozone would offer room for the ECB to adjust its monetary policy in the future.

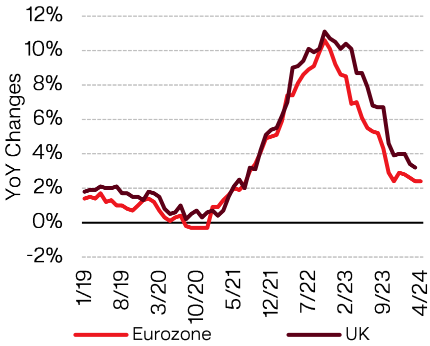
UK Purchasing Managers' Index



Source: Bloomberg

UK inflation eased slightly, and wage growth mildly slowed further. The UK's CPI and core inflation slowed from 3.4% YoY and 4.5% in February to 3.2% and 4.2% in March, respectively. Among the major categories, goods inflation slowed down further from 1.1% YoY in February to 0.8% in March, marking the lowest reading since April 2021, but services inflation remained sticky at 6.0% YoY in March. Furthermore, wage pressures showed more encouraging signs, although they remained at an elevated level. Weekly labour earnings, excluding bonuses, grew by 6.0% YoY in the three-month period ending February, mildly lower than the 6.1% growth in the three-month period ending January. A further slowdown in wage growth will be the key to bringing down underlying inflationary pressures.

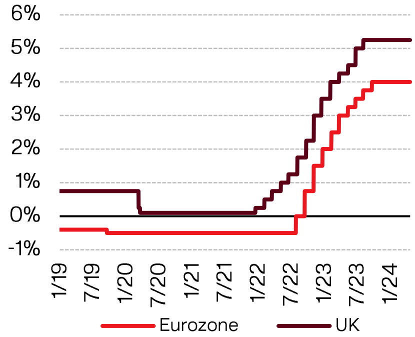
Inflation Rate



Source: CEIC

The European Central Bank (ECB) signalled that a rate cut may be on the way. In the April monetary policy meeting, the ECB left its key interest rates unchanged, as expected. In the post-meeting statement, the ECB stated that *"it would be appropriate to reduce the current level of monetary policy restriction"* if they become more confident that inflation is heading towards their target in a sustained manner. In addition, ECB President Christine Lagarde mentioned in an interview in mid-April that the ECB will cut rates soon, in the absence of any major surprises. The ECB's Vice President, Luis de Guindos, also made similar remarks in late April. This guidance clearly suggests that the ECB could start cutting rates as soon as the upcoming June meeting.

Policy Rate



Source: CEIC

The prospects of the Bank of England's (BoE) rate cuts have risen. The BoE's Governor Andrew Bailey said in mid-April that there was more "demand-led inflation pressure" in the US than in the UK, and there was *"strong evidence"* of softening inflation pressures in the UK. This hinted that the BOE would cut rates earlier than the Fed. Having said that, inflation is still sticky in the UK, so more data will be needed to confirm sustained disinflation progress. It is likely that the BOE will hold on in the near term and consider lowering interest rates in 2H 2024.

Stock markets diverged alongside a depreciation in currencies

A pullback in the Fed's rate cut hopes triggered significant market volatility. In April, financial markets further pushed back the Fed's rate cut expectations following stronger-than-expected US inflation readings. A marked increase in US treasury yields, along with rising tensions in the Middle East, weakened investor risk appetite, resulting in a mixed performance among major stock markets in Europe. The UK FTSE 100 index, the German DAX index, and the French CAC index closed by +2.4% MoM, -3.0%, and -2.7%, respectively, in April. Given the expected monetary policy divergence between the Fed and major central banks in Europe, the Euro and British pound saw a MoM depreciation of 1.1% and 1.0%, closing at US$ 1.067 and US$ 1.249, respectively, by the end of April.

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.

This material is the property of BEA and is protected by relevant intellectual property laws. Without the prior written consent of BEA, the information herein is not allowed to be copied, transferred, sold, distributed, published, broadcast, circulated, modified, or developed commercially, in either electronic or printed forms, nor through any media platforms that exist now or are developed later.

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).