

Market Monitor – Europe

Modest growth trajectory amid ongoing uncertainty



- European economies face persistent uncertainty, encompassing issues ranging from EU-US trade negotiations to political instability in France.
- The eurozone sustained modest growth, while the UK's momentum moderated across sectors.
- The ECB and BoE stayed put in September and turned cautious on further easing.

European economies face persistent uncertainty

EU-US trade relations saw renewed tensions. After a recent EU-US trade deal took effect in August, both sides are preparing for the next phase of negotiations addressing a range of non-tariff issues such as digital and technology rules, corporate compliance and climate-related regulations. These developments underscored the broad scope of issues that must be addressed in upcoming trade discussions, which could strain the bilateral ties.

The EU proposed new steel tariffs. The EU steel sector has long been under pressure, with its steelmaking capacity utilisation at only 67% in 2024. This is significantly below the healthy threshold of around 80%, reflecting stiff global competition. To prevent further deterioration of the EU steel sector, the European Commission presented a proposal limiting tariff-free import volumes to 18.3 million tonnes annually (a reduction of 47% compared to 2024 quotas), while doubling duties on above-quota imports from the current 25% to 50%. The measures are pending approval from the European Parliament and the European Council.

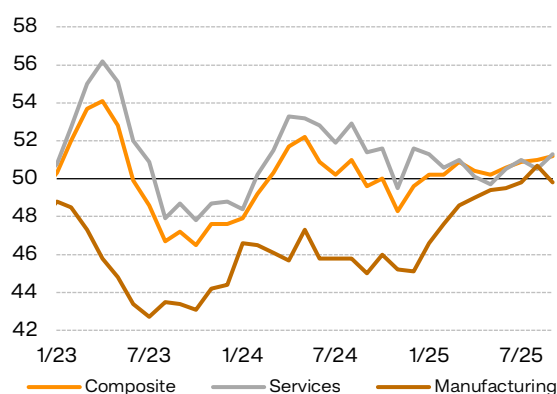
French political instability has intensified. On 6th October 2025, French Prime Minister Sébastien Lecornu resigned after serving less than one month in office, making him the third Prime Minister to resign since December 2024. Financial markets reacted sharply, with immediate equity selloffs and rising government bond yields. Lecornu's departure has increased uncertainty surrounding the passage of the 2026 budget, potentially limiting new spending initiatives and delaying critical fiscal reforms. Earlier, prolonged political instability and fiscal challenges had already led Fitch Ratings to downgrade France's sovereign credit rating from "AA-" to "A+" in September. Recent developments are likely to further strain the French economy.

The eurozone grew steadily while UK momentum moderated

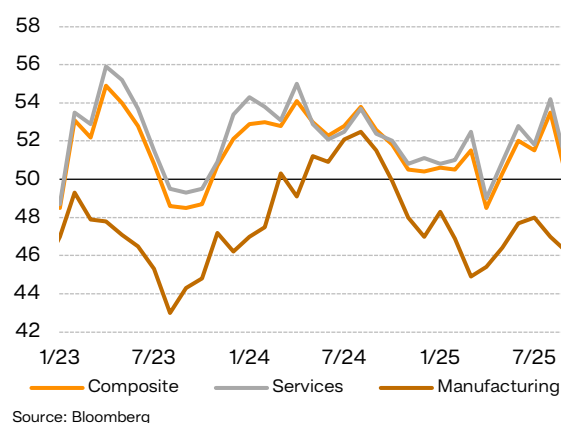
The eurozone sustained modest growth. The eurozone composite purchasing managers' index (PMI) has continued its upward trend since June, reaching 51.2 in September. This growth was driven by the services PMI, which hit an 8-month high of 51.3, reflecting a notable pick-up in domestic services demand. However, the manufacturing sector weakened following an improvement in August, with its PMI slipping into contractionary territory at 49.8 in September, down from 50.7 in August. Among major member states, Germany and Spain saw accelerated growth momentum, Italy maintained stable expansion, while the French economy remained subdued.

UK momentum moderated toward the end of Q3. UK gross domestic product (GDP) registered zero growth in July, after growing by 0.4% month-on-month (MoM) in June. The primary drag came from production output, which contracted by 0.9% MoM in July, while services and construction output posted modest gains of 0.1% and 0.2% MoM, respectively. Leading indicators suggested broad-based moderation across sectors by the end of Q3. The composite PMI dropped sharply from 53.5 in August to 50.1 in September. The manufacturing sector's contraction deepened, with its PMI falling from 47.0 in August to 46.2 in September. Meanwhile, the services PMI indicated slower expansion, dropping from 54.2 to 50.8.

Eurozone PMI



UK PMI



The ECB and BoE held rates unchanged

Inflation pressures remained contained in the eurozone. Eurozone headline inflation edged higher to 2.2% year-on-year (YoY) in September from 2.0% in August, while core inflation remained stable at 2.3%. The increase was largely attributed to a narrower YoY decline in energy prices (from -2.0% to -0.4%) and slightly faster services price growth (from 3.1% to 3.2%).

The European Central Bank (ECB) stressed a balanced inflation outlook to signal a pause in the near term. The ECB held its deposit facility interest rate unchanged at 2.0% during September's meeting. While revising up the GDP growth forecast for 2025 by 0.3 percentage points to 1.2%, the ECB's updated projections revealed a balanced inflation outlook around the 2% policy target, with inflation forecasts at 2.1%, 1.7% and 1.9% for 2025 through 2027, respectively. Moreover, President Christine Lagarde referred to inflation risks as "quite contained" in both directions, indicating no serious threats to the inflation outlook. With policy rates approaching neutral levels, the ECB is expected to maintain its current stance, though further monetary easing remains possible should downside risks to the economy increase.

UK inflation remained far above target. UK headline inflation remained elevated at 3.8% YoY in August, unchanged from July, while core inflation eased slightly from 3.8% to 3.6%. Food and non-alcoholic beverage prices accelerated for the fifth straight month to 5.1% YoY in August, the fastest since January 2024. Services price growth also remained robust at 4.7% YoY in August, though it slowed from 5.0% in July, likely due to seasonal effects in airfares. Compared to other advanced economies, UK households continued to face significant cost-of-living pressures.

The Bank of England (BoE) maintained a cautious stance. The BoE's monetary policy committee maintained its Bank Rate at 4.0% in September, with 7 members voting to hold rates versus 2 supporting a 25-basis-point reduction. Meanwhile, the BoE decided to slow the pace of quantitative tightening, announcing a reduction of GBP 70 billion in the holding of UK government bonds between October 2025 and September 2026, down from the GBP 100 billion reduction over the preceding 12 months. Given persistently above-target inflation, the BoE is expected to proceed cautiously and await further progress in disinflation before enacting additional monetary policy easing.

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).