

# Euro wrap-up

## Overview

- While final euro area HICP figures maintained a downwards trend in headline and core inflation, Bunds made modest losses as services inflation was revised marginally higher from the flash estimate.
- Gilts made modest gains on a quiet day for UK economic news.
- The March ZEW survey results are due on Tuesday, while the following day brings February inflation figures from the UK and the flash March Commission consumer confidence index.

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### Daily bond market movements

Bond	Yield	Change
BKO 2½ 03/26	2.942	+0.003
OBL 2.1 04/29	2.475	+0.009
DBR 2.2 02/34	2.455	+0.016
UKT 0% 01/26	4.280	-0.024
UKT 0½ 01/29	3.991	-0.017
UKT 4% 01/34	4.085	-0.011

\*Change from close as at 4:30pm GMT.

Source: Bloomberg

## Euro area

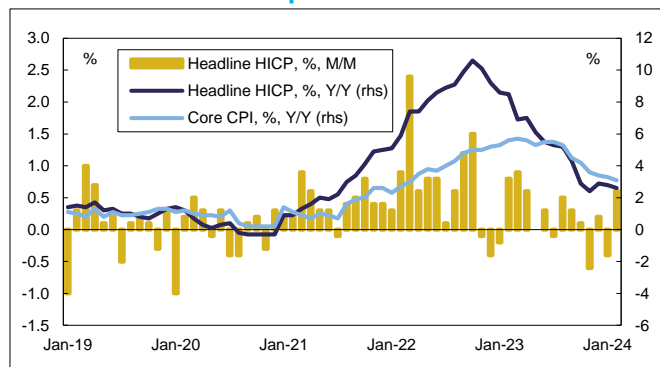
### Downtrend in euro area inflation maintained despite higher energy and sticky services prices

Today's final euro area inflation figures for February aligned with the flash estimates that saw the headline HICP rate drop for a second successive month, by 0.2ppt to 2.6%Y/Y. Admittedly, this remained 0.2ppt above November's low, but a hefty 8.1ppts below the peak in October 2022. Moreover, the downtrend would have been greater in the absence of a notable rise in energy costs – up 2.4ppts to a six-month high of -3.7%Y/Y – due to a policy-related jump in household energy charges and higher motor fuel prices. More encouragingly, food inflation fell slightly more than previously estimated, by 1.7ppts – the most in eleven months – to 3.9%Y/Y, the lowest for more than two years, with fresh food inflation down 16.7ppts to -3.5%Y/Y, the weakest for almost six years. And consistent with the global weakening in costs in the factory sector, core goods inflation was also down for a twelfth consecutive month, by 0.4ppt to 1.6%Y/Y, the lowest since July 2021, representing a more rapid disinflationary path from the peak than previous such adjustments to high inflation in the sector. Indeed, a discounted-related rebound in clothing inflation in February was more than offset by multi-year lows in furnishings, household appliances and toys, games and hobbies. But more disappointingly, today's release brought a modest upwards revision to services inflation, by 0.1ppt from the flash estimate, to leave it moving sideways at 4.0%Y/Y for a fourth month – underpinned by sticky hospitality prices and higher insurance premiums – resonating with the Governing Council's persisting concerns about the persistence of high inflation in the sector. This notwithstanding, the drop in overall core HICP inflation was unrevised from the flash release, down 0.2ppt to a two-year low of 3.1%Y/Y.

### Mixed messages about underlying inflationary pressures

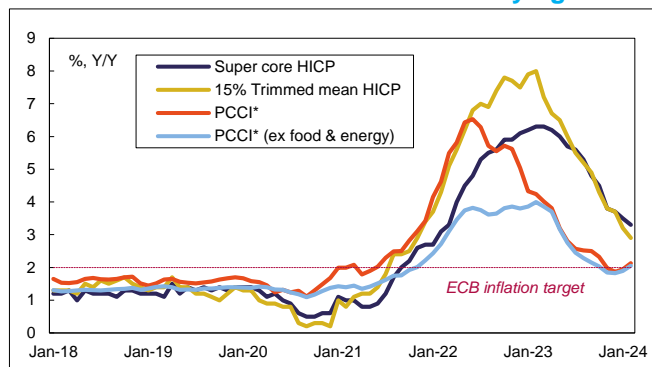
With recent inflation prints affected by significant base effects, the ECB might also be conscious that the increases in prices of services and core goods in February were above their respective long-run averages for the month. The ECB's seasonally-adjusted figures also suggested that momentum in services prices accelerated last month, with the monthly rise (0.5%M/M) the strongest in ten months, to be up 3.2%3M/3M annualised. So, while momentum in non-energy industrial goods remained extremely low at just 1.1%3M/3M ann., core prices overall were up 2.4%3M/3M ann., the most in four months and a rate that, if sustained, would be incompatible with a lasting return of inflation to target. The ECB might also be disheartened by the uptick in the persistent and common component of inflation (PCCI) – which the Governing Council believes can provide one of the more reliable guides to future inflation – which rose 0.2ppt to a four-month high of 2.1%3M/Y. But when excluding food and energy, the core PCCI was merely in line with the 2% target. Furthermore, with the share of items in the HICP basket with inflation above 2% having fallen sharply further in February, to a two-year low of 62%, other measures of underlying inflation also suggested that the disinflation path remains intact. In particular, the 15% trimmed mean HICP rate fell 0.3ppt to a 28-month low of 2.9%Y/Y, while the super core HICP rate fell 0.2ppt to a two-year low of 3.3%Y/Y.

### Euro area: Consumer price inflation



Source: Macrobond and Daiwa Capital Markets Europe Ltd.

### Euro area: Selected measures of underlying inflation



\*Persistent and Common Component of inflation. Source: Macrobond and Daiwa Capital Markets Europe Ltd.

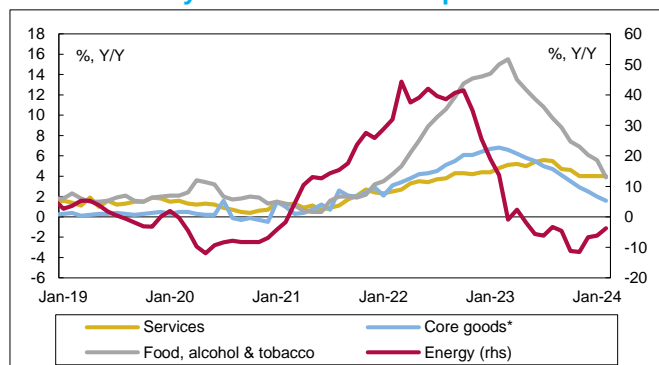
## Inflation likely to undershoot ECB projections over coming quarters amid subdued growth

While the near-term inflation outlook remains uncertain, not least due to the earlier timing of Easter this year, we maintain our view that headline and core inflation will continue on a gradual downtrend over coming months. In part reflecting possible upward seasonal impulses from hospitality, transport and food this month, we expect core inflation this quarter to be a touch higher than the ECB's most recent projection (3.1%Y/Y). Nevertheless, restrained by lacklustre economic growth and softening wage pressures, we continue to expect headline and core inflation to ease to below the 2% target in Q324. Indeed, while the ECB earlier this month revised down its inflation forecasts in each quarter through to Q126, our current expectation for headline inflation in Q2 of 2.3%Y/Y is a touch below that assumed by the ECB, with our expectation for Q3 0.3ppt lower at 1.9%Y/Y. And our quarterly profile for core inflation from Q2 on undershoots that of the ECB through to the end of the forecast horizon at the end of 2026. With wage growth starting to slow and a decline in job vacancies suggesting that the labour market is becoming somewhat less tight, services inflation should also resume a downwards profile from April too. Earlier this month, ECB President Lagarde downplayed the chances of a first rate cut next month given the lack of substantive new information on wage developments likely to be available by then. And the more hawkish members of the Governing Council will point to ongoing persistence in services momentum as further justification to refrain from action at the next monetary policy meeting. However, we continue to expect a first rate cut to come in June to coincide when the ECB updates its macroeconomic projections.

## Trade surplus jumps to a series high amid a rise in exports and slump in imports at start of year

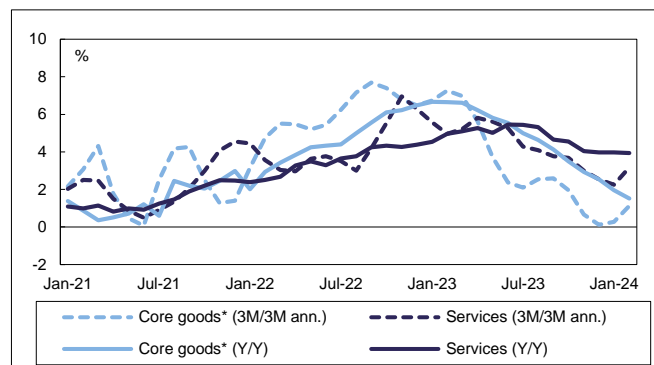
While euro area [manufacturing](#) output maintained a downtrend at the start of the year, today's goods trade report was more encouraging. In particular, the trade surplus almost doubled in January to a series-high €28.0bn, some €30bn higher than a year earlier and a whopping €76bn above the record deficit in August 2022. Among other things, there was a notable narrowing in the trade deficit with China to the smallest in two years. The improvement in the overall trade balance in part reflected a rebound in the value of exports, by 2.1%M/M – the most for 17 months – with an increase in shipments to China, Japan and the UK offsetting a second successive decline to the US. But this still left the total value of exports up just 1.3%Y/Y. The trade surplus was also boosted by a further sharp drop in the value of imports that month, with the 4%M/M decline the steepest in eleven months to leave them down 16.1%Y/Y. Of course, to some extent the ongoing adjustment in import values reflects price developments. But with import prices having dropped just 0.6%M/M in January, today's figures suggest that a large chunk of the weakness at the start of the year was due to a drop in volumes, reflecting persisting lacklustre demand. So, while we will need to await the lagged publication of trade volumes figures next month, today's data suggest that, having subtracted from growth in two of the previous three quarters, net trade provided a welcome positive contribution to GDP growth at the start of 2024.

### Euro area: Key HICP inflation components



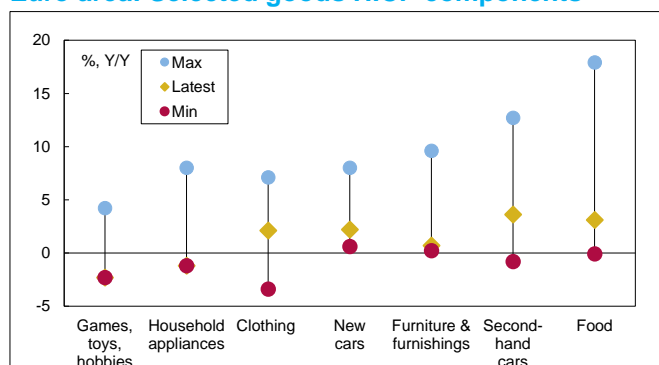
\*Non-energy industrial goods. Source: Macrobond and Daiwa Capital Markets Europe Ltd.

### Euro area: Core inflation momentum



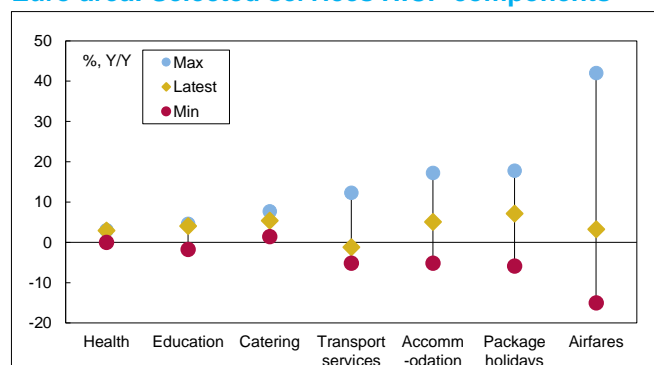
\*Non-energy industrial goods. Source: Macrobond and Daiwa Capital Markets Europe Ltd.

### Euro area: Selected goods HICP components\*



\*Since 2020. Source: Macrobond and Daiwa Capital Markets Europe Ltd.

### Euro area: Selected services HICP components\*



\*Since 2020. Source: Macrobond and Daiwa Capital Markets Europe Ltd.

## The coming two days in the euro area

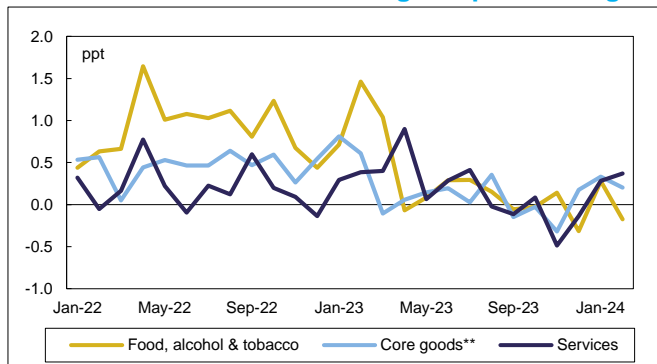
The coming two days will bring the first of this week's March sentiment surveys, including the Commission's preliminary consumer confidence indicator on Wednesday. While the index is expected to rise for a second successive month in March, by ½pt, this would leave it merely back to its level in December and therefore consistent with subdued consumer spending. Meanwhile, ahead of the flash PMIs on Thursday, the German ZEW sentiment survey (due tomorrow) is likely to flag ongoing investor concerns about conditions in the euro area's largest member state. Indeed, while sentiment with respect to the outlook for the coming six months will benefit from expectations of lower interest rates, investors will likely remain downbeat about the current situation, with the balance firmly in negative territory and consistent with contraction in German GDP. In terms of hard economic data, tallying with the pickup already reported in Germany, euro area construction activity in January is likely to have benefitted from unseasonably mild weather at the start of the year. Aside from the data, ECB President Lagarde will give a keynote address at the start of the ECB Watchers conference on Wednesday, while Chief Economist Lane and influential Executive Board member Schnabel will participate on panel discussions.

## UK

### The coming two days in the UK

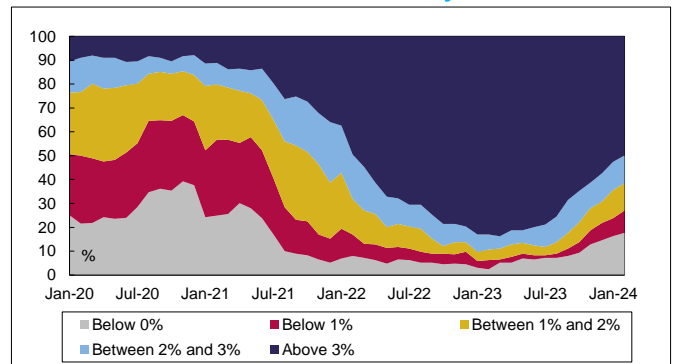
After a quiet start to the week for top-tier releases, focus in the UK will turn to the release of February's inflation data on Wednesday. We expect the headline CPI rate to drop 0.6ppt to 3.4%Y/Y – a touch below the Bloomberg survey consensus and the BoE's expectation in the February MPR – which would be the lowest since September 2021. While the energy component will again add to inflation, we expect the other major components to more than offset that impact, with food inflation likely falling more than 1ppt to its lowest level since April 2022 and core goods inflation likely falling about ½ppt to the lowest since April 2021. Moreover, in part reflecting a significant base effect from a year earlier when prices in the category rose the most in any February on the series, services inflation is also likely to drop about ½ppt to 6.0%Y/Y or less for the first time since January 2023. As a result, we expect core inflation to fall a chunky 0.6ppt to 4.5%Y/Y, which would be the lowest since December 2021. Wednesday will also bring PPI inflation data for February and the ONS house price index for January.

### Euro area: Deviations from long-run price change\*



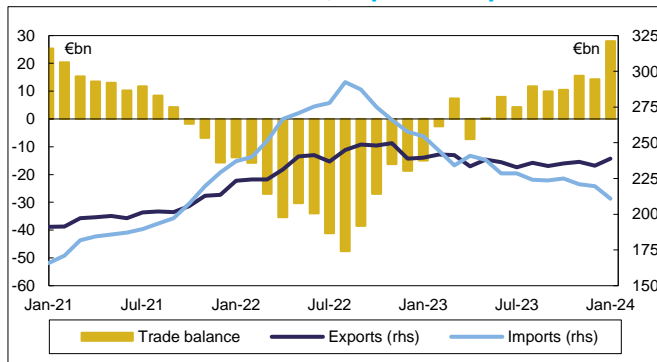
\*Monthly change in prices compared to average for the month in the decade before the pandemic. \*\*Non-energy industrial goods. Source: Macrobond and Daiwa Capital Markets Europe Ltd.

### Euro area: Share of HICP basket by inflation rate



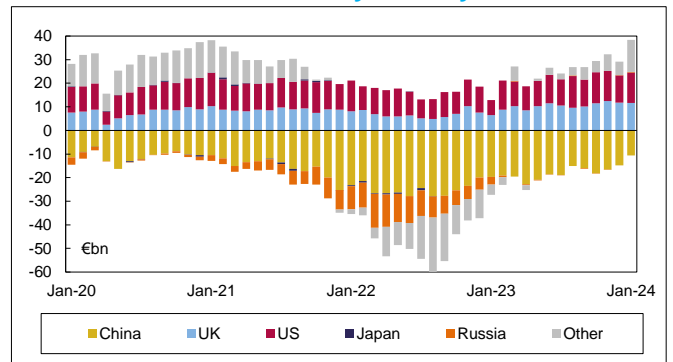
Source: ECB and Daiwa Capital Markets Europe Ltd.

### Euro area: Trade balance, export & import values



Source: Macrobond and Daiwa Capital Markets Europe Ltd.

### Euro area: Trade balance by country






Source: Macrobond and Daiwa Capital Markets Europe Ltd.

# European calendar

## Today's results

### Economic data

Country	Release	Period	Actual	Market consensus/ <i>Daiwa forecast</i>	Previous	Revised
Euro area	 Final HICP (core HICP) Y/Y%	Feb	<b>2.6 (3.1)</b>	<u>2.6 (3.1)</u>	2.8 (3.3)	-
	 Trade balance €bn	Jan	<b>28.1</b>	-	13.0	14.3
UK	 Rightmove house prices M/M% (Y/Y%)	Mar	<b>1.5 (0.8)</b>	-	0.9 (0.1)	-










### Auctions

Country	Auction
- Nothing to report -	






Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

## Upcoming releases

### Economic data

Country	GMT	Release	Period	Market consensus/ <i>Daiwa forecast</i>	Previous
<b>Tuesday 19 March 2024</b>					
Euro area	 10.00	Labour costs Y/Y%	Q4	-	5.3
Germany	 10.00	ZEW current assessment (expectations) balance	Mar	-82.0 (20.5)	-81.7 (19.9)
<b>Wednesday 20 March 2024</b>					
Euro area	 10.00	Construction output M/M% (Y/Y%)	Jan	-	0.8 (1.9)
	 15.00	European Commission's preliminary consumer confidence	Mar	-15.0	-15.5
Germany	 07.00	PPI Y/Y%	Feb	-3.8	-4.4
Italy	 09.00	Industrial production M/M% (Y/Y%)	Jan	-	1.1 (-2.1)
UK	 07.00	CPI (core CPI) Y/Y%	Feb	<u>3.4 (4.5)</u>	4.0 (5.1)
	 07.00	PPI output (input) Y/Y%	Feb	-0.5 (-2.7)	-0.5 (-3.3)
	 09.30	House price index Y/Y%	Jan	-	-1.4

### Auctions and events

<b>Tuesday 19 March 2024</b>					
Euro area	 08.30	ECB's Guindos scheduled to speak			
UK	 10.00	Auction: £2bn of 4.75% 2043 bonds			
<b>Wednesday 20 March 2024</b>					
Euro area	 -	The ECB and its Watchers conference – ECB's Lagarde, Lane, De Cos and Schnabel all scheduled to speak			
Germany	 10.30	Auction: 2.5% 2044 bonds			
	 10.30	Auction: 0.0% 2052 bonds			

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

The next edition of the Euro wrap-up will be published on 20 March 2023

Access our research blog at:

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