

# Euro wrap-up

## Overview

- While French inflation undershot expectations, Bund followed USTs lower.
- Gilts were little changed on a quiet day for UK economic news.
- Wednesday will bring the flash euro area inflation reading for January, alongside the final services PMIs for the same month.

**Emily Nicol**  
+44 20 7597 8331

**Edward Maling**  
+44 20 7597 8030

### Daily bond market movements

Bond	Yield	Change
BKO 2.1 03/28	2.112	+0.003
OBL 2½ 04/31	2.458	+0.012
DBR 2.9 02/36	2.886	+0.020
UKT 3¾ 03/27	3.683	-0.006
UKT 4¾ 03/30	3.942	+0.008
UKT 4½ 03/35	4.509	+0.004

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

## Euro area

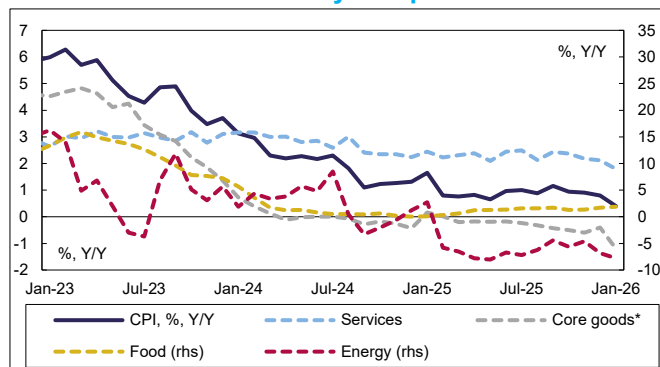
### French inflation undershoots as extended discounting pushes core goods CPI to a near-9-year low

While Friday's [German inflation](#) data for January slightly exceeded expectations, today's flash French estimates surprised firmly to the downside. In particular, the headline HICP rate fell 0.3ppt to 0.4%Y/Y, while headline inflation on the national measure was down a chunkier 0.5ppt, to 0.3%Y/Y. Both measures were the softest for more than five years. Like in Germany, the national detail suggested that higher fresh food prices provided an upwards impulse to inflation this month, pushing inflation of that component up 1.8ppts to 1.4%Y/Y, a nine-month high. Overall food inflation (1.9%Y/Y) was the strongest for almost two years. But energy inflation fell 1ppt to -7.8%Y/Y, an eight-month low, supported in part by a softer rise in petrol prices than a year earlier. Base effects played a significant role in the core components too. Indeed, contrasting markedly with the jump in Germany, French core goods inflation was the most negative since February 2017 (-1.2%Y/Y). This was principally due to a longer discounting period in clothing and footwear prices this January than last, suggesting that the impact on inflation will be temporary. But having remained between 2-2½%Y/Y over the past 16 months, services inflation also moderated 0.3ppt to 1.8%Y/Y, the softest rate for four years, as increases in doctors' fees were smaller than last year. Overall, core CPI inflation in France looks to have declined to just 0.8%Y/Y, the lowest rate since mid-2021. While January is likely to mark the trough in French inflation not least as energy base effects will push the headline rate higher this month, today's data reinforce our view that tomorrow's estimates of euro area inflation in January will confirm another step down further below the 2.0% target.

### Tighter credit conditions suggest a further ECB rate cut this year can't be ruled out

The resilience of euro area economic activity has all but ensured an uneventful ECB monetary policy announcement on Thursday. Nevertheless, a soft flash euro area inflation print tomorrow should provide a reminder that the downside risks to the ECB's inflation projections are non-negligible. Among those downside risks, the strength of the euro exchange rate is prominent. But recent ECB analysis has also flagged the underwhelming recovery in euro area credit growth, which has arguably disappointed given the extent of monetary policy loosening over the past cycle. Tallying with those concerns, today's quarterly Bank Lending Survey (BLS) suggested that credit conditions unexpectedly tightened for businesses in Q4 – as reported by a net +7% of banks – and were expected to continue tightening to a broadly similar extent in the current quarter (+6%). That tightening principally reflected elevated risk aversion from lenders and concerns about the economic outlook. And the changes were most pronounced in Germany (+16%) and France (+10%). While the sampling period for this survey closed shortly before the US threatened to levy fresh tariffs against those member states, elevated geopolitical tensions surrounding Greenland might have played a role. But its broader findings were also consistent with the conclusions of the ECB's survey on access to finance for enterprises (SAFE), conducted a month earlier, which flagged tighter lending

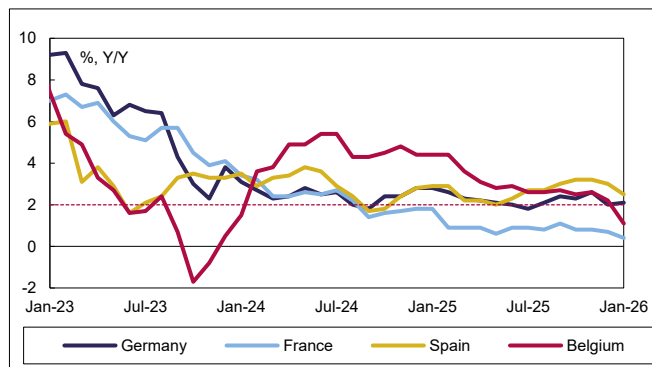
### France: CPI inflation & key components



\*Non-energy industrial goods.

Source: Macrobond and Daiwa Capital Markets Europe Ltd.

### Euro area member states: Headline HICP inflation

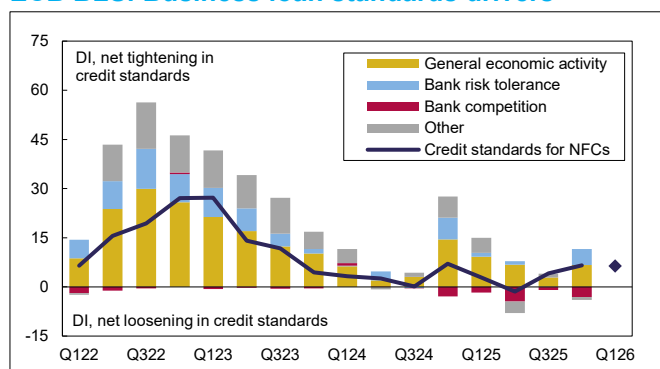


Source: Macrobond and Daiwa Capital Markets Europe Ltd.

conditions for businesses, particularly SMEs. With regards to the housing market, however, the BLS suggested that credit conditions for mortgages were unexpectedly loosened slightly in Q4 (-2%) despite heightened perceptions of risks.

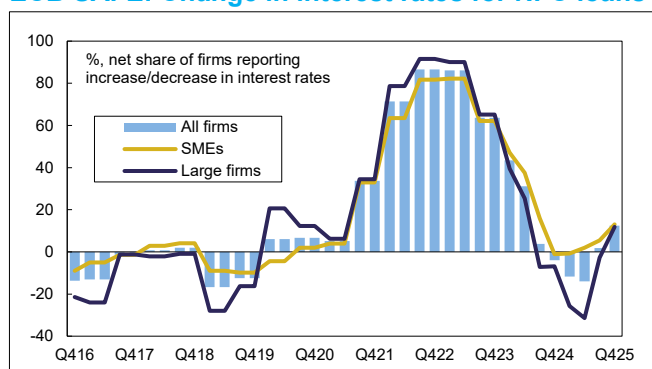
Separately, the BLS reported that business loan demand picked up only marginally in Q4 (+3%), with the growth solely reflecting investment by larger firms. And growth in demand for such lending is expected to remain somewhat tepid (+6%) in the current quarter too. Demand for household mortgages rose in Q4 on the back of the ongoing recovery in house prices in the core member states. But as interest rates offered barely minimal support, the net demand increase (+9%) was the smallest since Q124 (+2%, from +21% in Q325) and banks expect mortgage demand to slow further in Q1 (+2%). Such lacklustre demand for both business and mortgage loans corresponds with our view that current monetary policy is broadly neutral rather than accommodative. At the same time, geopolitics and trade policy volatility will likely continue to contribute to tighter lending conditions through their influence on risk tolerance - as the BLS suggests - with consequences not least for export-oriented, supply-chain-sensitive, and energy-intensive subsectors.

#### ECB BLS: Business loan standards drivers\*



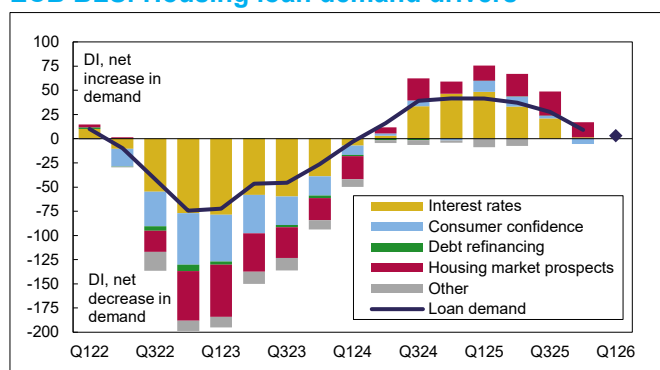
\*Diamond shows bank expectations for the current quarter.  
 Source: ECB, Macrobond and Daiwa Capital Markets Europe Ltd.

#### ECB SAFE: Change in interest rates for NFC loans\*



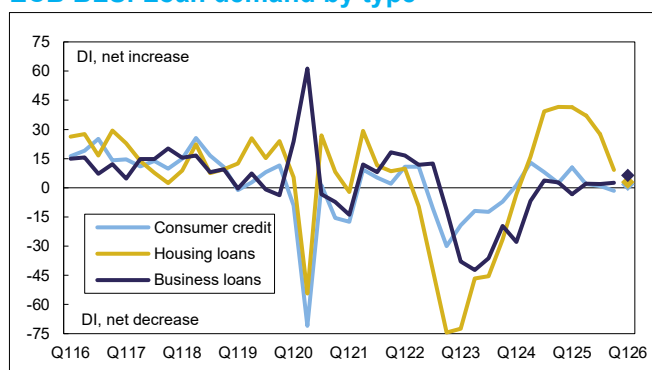
\*Until Q124, the ECB SAFE survey was conducted on a biannual basis.  
 Source: ECB, Macrobond and Daiwa Capital Markets Europe Ltd.

#### ECB BLS: Housing loan demand drivers\*



\*Diamond shows bank expectations for the current quarter.  
 Source: ECB, Macrobond and Daiwa Capital Markets Europe Ltd.

#### ECB BLS: Loan demand by type\*



\*Diamonds shows bank expectations for the current quarter.  
 Source: ECB, Macrobond and Daiwa Capital Markets Europe Ltd.

## The day ahead in the euro area

The main data focus in the euro area on Wednesday will be the aforementioned flash estimates of inflation for January. Notwithstanding the uptick in Germany, inflation data from other major member states – including France, Spain, Belgium and Portugal – have come in on the soft side. Taken together with expectations of a further moderation in Italy (data also due tomorrow), we now expect euro area inflation to ease 0.2ppt to 1.7%Y/Y, which would mark the softest reading since April 2021. Admittedly, the risks to this forecast are skewed slightly to the upside due to rounding. But we also expect core inflation to move sideways at 2.3%Y/Y with risks skewed to the downside. In addition, PPI data will likely suggest that goods producer price pressures remained absent at the end of last year. Wednesday will also bring the final services PMIs for January, which will include a first reading from Italy and Spain. While the flash release saw the euro area headline activity index fall ½pt to 51.9, a four-month low, this principally reflected a questionable deterioration in France, which contrasted stable conditions presented by the larger INSEE survey. Overall, tomorrow's release should remain consistent with broadly firming growth momentum at the start of the new year.



## The day ahead in the UK

Ahead of the BoE's monetary policy announcement on Thursday, tomorrow will bring just the final UK services PMIs for January. The flash survey reported a marked improvement in the activity index at the start of the year, rising 2.9pts to 54.3, the highest level since April 2024 and broadly in line with the long-run average. The price PMIs also suggested stickiness in services inflation. So, despite signalling ongoing weakness in the labour market, tomorrow's survey results will reinforce our view that the majority on the MPC will vote to keep interest rates unchanged this week.



## European calendar

### Today's results

#### Economic data

Country	Release	Period	Actual	Market consensus/ <i>Daiwa forecast</i>	Previous	Revised
France	 Preliminary HICP (CPI) Y/Y%	Jan	<b>0.4 (0.3)</b>	0.6 (0.6)	0.7 (0.8)	-
Spain	 Unemployment (net employment) change 000s	Jan	<b>30.4 (17.3)</b>	-	-16.3 (33.1)	- (35.5)










#### Auctions

Country	Auction
Germany	 sold €1.354bn of 2.5% 2035 green bonds at an average yield of 2.79%
UK	 sold £4.25bn of 4.75% 2035 bonds at an average yield of 4.585%


Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

### Tomorrow's releases

#### Economic data

Country		GMT	Release	Period	Market consensus/ <i>Daiwa forecast</i>	Previous
Euro area		09.00	Final composite (services) PMI	Jan	<u>51.5 (51.9)</u>	51.5 (52.4)
		10.00	Preliminary headline (core) HICP Y/Y%	Jan	<u>1.7 (2.3)</u>	1.9 (2.3)
		10.00	PPI Y/Y%	Dec	-2.2	-1.7
Germany		08.55	Final composite (services) PMI	Jan	<u>52.5 (53.3)</u>	51.3 (52.7)
France		08.50	Final composite (services) PMI	Jan	<u>48.6 (47.9)</u>	50.0 (50.1)
Italy		08.45	Composite (services) PMI	Jan	50.1 (51.3)	50.3 (51.5)
		10.00	Preliminary HICP (CPI) Y/Y%	Jan	0.8 (0.9)	1.2 (1.2)
Spain		08.15	Composite (services) PMI	Jan	55.4 (56.8)	55.6 (57.1)
UK		09.30	Final composite (services) PMI	Jan	<u>53.9 (54.3)</u>	51.4 (51.4)

#### Auctions and events

Germany		10.30	Auction: to sell up to €4bn of 2.5% 2032 bonds
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Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

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