

# Euro wrap-up

## Overview

- While data showed that euro area exports ended 2024 on a soft note, Bunds made losses as European leaders met to discuss the region's security, raising the likelihood of increased borrowing to fund defence spending.
- Gilts also made losses on a quiet day for UK economic news.
- Tuesday will bring the latest UK labour market data along with the German ZEW investor survey for February and updated estimates of French inflation in January.

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### Daily bond market movements

Bond	Yield	Change
BKO 2.2 03/27	2.131	+0.023
OBL 2.4 04/30	2.263	+0.041
DBR 2½ 02/35	2.487	+0.057
UKT 4% 01/27	4.194	+0.006
UKT 4% 07/29	4.216	+0.011
UKT 4% 07/34	4.525	+0.027

\*Change from close as at 5.00pm GMT.

Source: Bloomberg

## Euro area

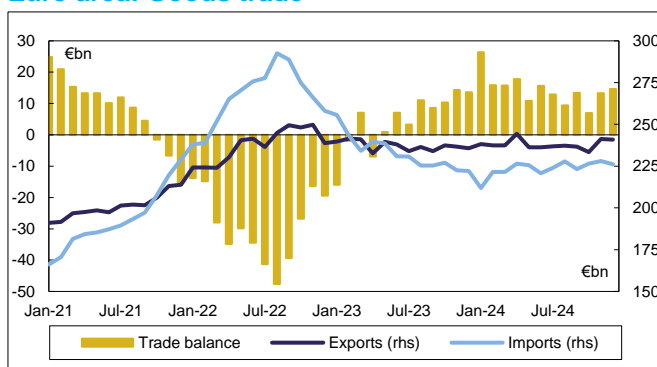
### Goods exports soft in December but up over Q4 as a whole

Industrial production in December reached its lowest level in more than four years, confirming a seventh successive quarterly decline. A key cause of that downtrend in output has been weak external demand, with goods exports outside of the euro area even weaker than manufacturing output alone would have suggested. Indeed, goods export volumes in October hit their lowest level since June 2020 and December 2010 when excluding the pandemic period. And while exports in both value and volume terms rebounded somewhat in November, today's trade values data suggested that they ended the year on a soft note. Indeed, goods export values dropped in December for the third month in four, with shipments down in key categories of traditional strength, such as machinery, transport, chemicals and related items. However, with food and commodity exports up, the decline in overall shipments abroad was modest (-0.2%M/M). So, despite continued weakness over the quarter in machinery and transport items, total exports rose 0.7%3M/3M, with the quarterly average in Q4 only a touch below the level in Q2. Import values were also subdued in December falling 0.8%M/M. As a result, the euro area goods trade surplus rose more than €1bn on the month and also more than €1bn from a year earlier to a six-month high of €14.6bn. However, import values were still up in Q4 for a third successive quarter, rising 0.8%3M/3M. And while import prices ticked up in December, import volumes likely outpaced exports in Q4, so that goods trade subtracted from GDP growth again for a second successive quarter.

### Trade deficit with China up 100% & surplus with the US up 50% from pre-pandemic levels

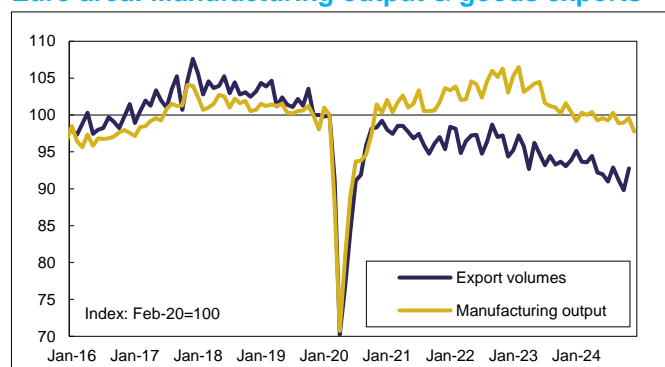
Among the euro area's most important trading partners, goods export values to China were broadly flat on the month in December. But that left them down 9.4%Y/Y and about 22% below the peak at the start of 2023, highlighting the extent to which weaker demand from China has been a key drag on European manufacturers since the pandemic. And so, the euro area's bilateral trade deficit with China remained very large in December at just over €20bn, double the average in 2019 before the pandemic. Goods exports to the US – by far the euro area's most important export market, accounting for twice the share as China – fell almost 2%M/M from November's series high to suggest that importers saw no need to front-load shipments to try to dodge tariffs in the wake of the US election. But they were still up more than 4%Y/Y. And with imports from that country also softer, the euro area bilateral trade surplus with the US was broadly steady in December at €16.3bn, about 50% higher than the average in the year before the pandemic. Of course, the large bilateral trade surplus with the US – which among the euro area member states is explained predominantly by surpluses from Germany and Ireland, and to a lesser extent Italy and France – is in the firing line of President Trump's plan for bumper 'reciprocal' tariffs on top of the new targeted 25% tariffs on iron, steel and aluminium (which account for only about 2.5% of the region's shipments to the US).

### Euro area: Goods trade\*



\*Seasonally adjusted values. Source: Macrobond and Daiwa Capital Markets Europe Ltd.

### Euro area: Manufacturing output & goods exports



Source: Macrobond and Daiwa Capital Markets Europe Ltd.

## Europe a key target of Trump’s reciprocal tariff plans

Tariffs faced by European exporters to the US are on average currently just a few percentage points lower than those faced by US exporters to the EU. And US exporters typically face much higher tariffs on their shipments to other important markets. But the new White House (rather spuriously) complains that Europe’s VAT more significantly distorts competition with the US. It also has a bugbear with the Digital Service Tax imposed by a handful of member states, including France, Italy and Spain. And so, increased tariffs on a range of items, not least on motor vehicles, machinery and chemicals – which in their broadest sense account for more than half of euro area exports to the US and the bilateral trade surplus – might well be lined up in the absence of a new deal. The case for specifically including pharmaceuticals – which currently face an average tariff paid of 0.001%, represent more than one fifth of all exports to the US and account for the largest source of the trade surplus – might appear strong. And certainly, beyond the euro area, Denmark’s pharma shipments of Novo Nordisk’s drugs might be in scope given Trump’s Greenland ambitions. But increasing the cost of pharmaceuticals in the US could seem politically disadvantageous. And differences in US and certain European corporation tax arrangements seem the best explanation for the current trade imbalance.

## The day ahead in the euro area

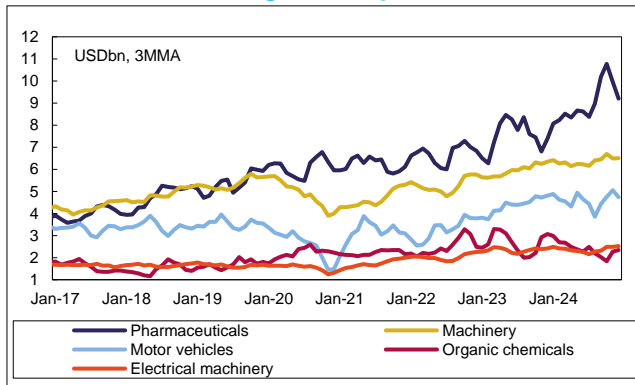
With the region’s equities having made strong gains over the past month, and this coming weekend’s Federal Elections providing an opportunity to bring about greater political stability in Germany, February’s ZEW investors’ survey might be expected to strike a relatively more upbeat tone. Indeed, Bloomberg’s consensus forecast is for an outsized improvement in the expectations index (from 10.3 currently to 20.0). However, in the context of numerous headwinds – including increasingly hostile rhetoric from the US relating to trade and security, ongoing economic stagnation, as well as some residual pre-election uncertainty – we look for a somewhat more moderate pickup to about 15. Meanwhile, final French inflation detail for January will provide more granular detail on price developments last month after flash estimates surprisingly reported no change in the headline HICP rate from December’s print (1.8%Y/Y) rather than the expected increase.

## UK

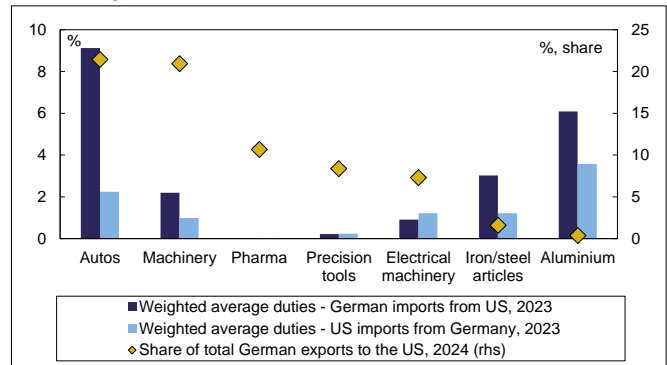
### The day ahead in the UK

After a relatively quiet start to the week in the UK, tomorrow’s labour market report will mark the start of this week’s top-tier dataflow. But after November’s figures surprised significantly to the upside as private sector regular wage growth accelerated

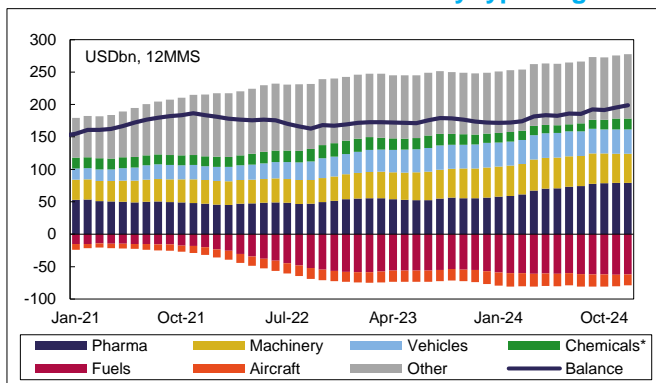
### Euro area: Selected goods exports to the US



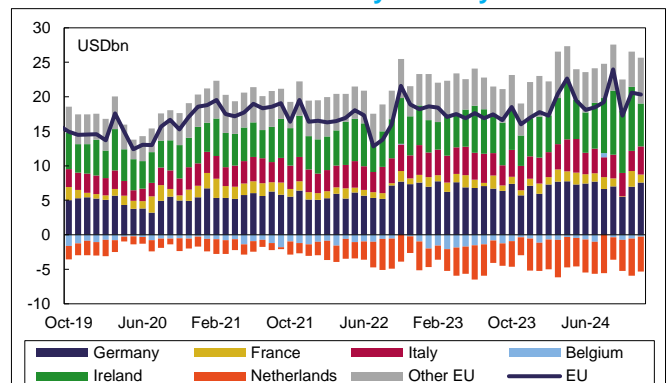
### Germany: Selected tariffs on trade with the US



### Euro area: Trade balance with US by type of good



### EU: Trade balance with US by country





to 6.0%3M/Y, we and the BoE expect a further pickup to 6.3%3M/Y in December, more than 1ppt above the BoE's November projection. But despite the strength of underlying wage growth, policymakers should also be concerned by continued signs of a softening of conditions in the labour market. Indeed, we expect another uptick in the unemployment rate in the three months to December to 4.5%, with a further drop in the number of payrolled employees and vacancies also set to underscore falling demand for workers.

## European calendar

### Today's results

#### Economic data

Country	Release	Period	Actual	Market consensus/ <i>Daiwa forecast</i>	Previous	Revised
Euro area 	Trade balance €bn	Dec	<b>14.6</b>	14.5	12.9	13.3
UK 	Rightmove house prices M/M% (Y/Y%)	Feb	<b>0.5 (1.4)</b>	-	1.7 (1.8)	-




#### Auctions

Country	Auction
- Nothing to report -	




Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

### Tomorrow's releases

#### Economic data

Country	GMT	Release	Period	Market consensus/ <i>Daiwa forecast</i>	Previous
Germany 	10.00	ZEW current situation (expectations) balance	Feb	<b>-89.5 (15.0)</b>	-90.4 (10.3)
France 	07.45	Final HICP (CPI) Y/Y%	Jan	<b>1.8 (1.4)</b>	1.8 (1.3)
UK 	07.00	Average wages (excluding bonuses) 3M/Y%	Dec	<b>5.9 (5.9)</b>	5.6 (5.6)
	07.00	Unemployment rate 3M%	Dec	<b>4.5</b>	4.4
	07.00	Employment 3M/3M change 000s	Dec	50	36
	07.00	Payrolled employees M/M change 000s	Jan	-30	-47
	07.00	Claimant count rate % (change 000s)	Jan	-	4.6 (0.7)
	09.30	Preliminary output per hour Y/Y%*	Q4	-	-1.8

#### Auctions and events

Euro area 	14.00	ECB Executive Board Member Cipollone to speak on the ECB's balance sheet in MNI webcast			
Germany 	10.30	Auction: to sell up to €4.5bn of 2.2% 2027 bonds			
UK 	09.30	BoE Governor Bailey to speak on 'preserving and enhancing open financial markets' in fireside chat with Bruegel			
	10.00	Auction: to sell £1.75bn of 4% 2063 bonds			

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

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