

Euro wrap-up

Overview

- Bunds made losses despite downside surprises in the latest German and French inflation data.
- Gilts followed USTs lower despite further weak UK car registration data and a downwards revision to the UK services PMIs.
- Thursday will bring the flash estimate of euro area inflation in December along with the latest Commission sentiment survey, construction PMIs, and euro area retail sales and German factory orders figures.

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Daily bond market movements

Bond	Yield	Change
BKO 0 12/22	-0.712	+0.014
OBL 0 10/25	-0.729	+0.023
DBR 0 02/31	-0.519	-
UKT 1½ 09/22	-0.146	+0.012
UKT 0% 06/25	-0.080	+0.017
UKT 4% 12/30	0.246	+0.039

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

Source: Bloomberg

Euro area

Inflation still subdued at end-year in Germany and France

Ahead of tomorrow's flash estimates of euro area inflation in December, today's data from Germany and France made clear that price pressures remained subdued at the end of 2020. Contrasting with expectations of a rise, German inflation on the EU-harmonised measure was unchanged at the series low of -0.7%Y/Y. The detail published on the national measure showed that a slower pace of decline in energy prices added to inflation while food prices provided some offset. But while services inflation was steady, inflation of non-energy industrial goods slowed, suggesting a slight softening of core inflation perhaps related to the stronger euro. The flash estimate of French inflation in December also surprised on the downside, with the headline rate on the EU measure down 0.2ppt to 0.0%Y/Y, matching September's four-year low. The detail was much like that of its German counterpart, with the latest weakness coming from prices of food and manufactured items, while services inflation was steady and the pace of decline in energy prices somewhat less marked. Looking ahead, inflation in both countries will rise from the start of this year, not least due to oil prices. But in Germany the rise will be accentuated by the reversal of the temporary VAT cut (the main rate was cut by 3ppts to 16% from 1 July to end-2020) as well as the introduction of the new carbon tax which will increase domestic heating bills. Meanwhile, despite a slight upside surprise last week from Spain, where the EU-harmonised measure rose 0.2ppt to -0.6%Y/Y, tomorrow's euro area figures seem highly likely to show little change from November's readings of -0.3%Y/Y for headline CPI and 0.2%Y/Y for core inflation.

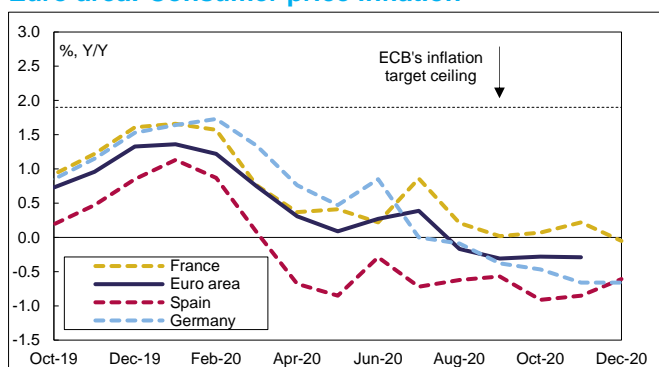
French consumer confidence rebounds back to top of Covid-era range...

The latest French consumer confidence survey surprised on the upside, with a larger-than-expected jump in the headline sentiment index in December of 6pts – the most in any single month this year – to 95, matching the highest level during the pandemic. The improvement within the survey detail – which coincides with last month's easing of containment measures – was broad-based. Most notably perhaps, the share of households considering it to be a suitable time to make major purchases jumped above the long-run average for the first time since February. Households' assessment of their future financial situation also rose above the long-run average. And while fears of unemployment remained high by historical standards, they also eased somewhat. Overall, therefore, notwithstanding the risks that a further damaging wave of coronavirus would pose, French consumer spending should remain relatively resilient in the first quarter.

...but final services PMIs hint at deterioration in conditions in the second half of December

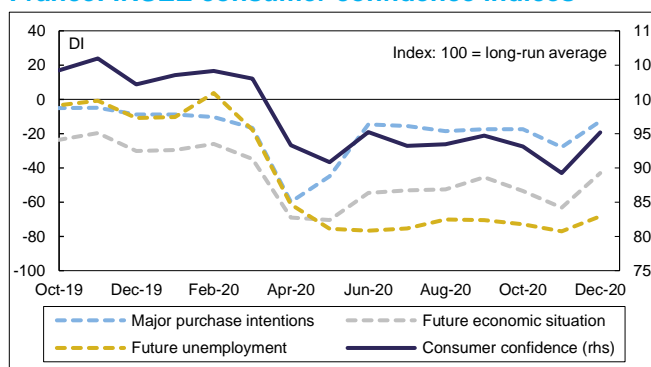
The final services PMIs for December, however, flagged the risks of a renewed deterioration in the New Year in response to the intensified spread of Covid-19. While they were improved from November, the headline PMIs for the euro area and

Euro area: Consumer price inflation*



*Flash estimates for Germany, France and Spain for December 2020.
Source: Refinitiv and Daiwa Capital Markets Europe Ltd.

France: INSEE consumer confidence indices



Source: INSEE, Refinitiv and Daiwa Capital Markets Europe Ltd.

Germany were revised down significantly from their preliminary estimates – respectively by 0.9pt to 46.4 and 0.7pt to 47.0 – to suggest a weakening of momentum as the month went on. Indeed, the headline services PMIs for each of the member states bar Ireland were still consistent with contraction, with Italy's (just 39.7) strikingly weak. At the aggregate euro area level, incoming new work fell for a fifth successive month, with ongoing pandemic containment measures, including travel restrictions, weighing on demand from abroad as well as at home. The survey reported another drop in employment in the services sector, albeit at a slower pace than in prior months. And despite rising input costs, output prices continued to be cut.

The day ahead in the euro area

On a busy day for new economic data from the euro area, tomorrow will bring the European Commission's sentiment survey results and construction PMIs for December, the flash estimates of euro area and Italian inflation for the same month, and euro area retail sales and German factory orders figures for November. The euro area retail sales figures are likely to be subdued, despite the strong growth recorded in [Germany](#) where the economy was resilient to the second wave of pandemic. With French sales hit by the closure of non-essential stores, the median forecast on the Bloomberg survey is for a drop in euro area sales of 3.4%M/M, which would be the largest monthly fall since April albeit nowhere near as severe as the 11.8%M/M decline posted that month. Thanks to the strength in Germany, we anticipate a far smaller decline. Meanwhile, following today's German and French figures, we now expect the headline euro area inflation rate to be unchanged at -0.3%Y/Y in December, with the core CPI rate also unchanged at the series low of 0.2%Y/Y for a fourth successive month. However, we caution that price data for a large share items in the basket will need to be imputed by the statisticians, rendering the figures less reliable than usual.

UK

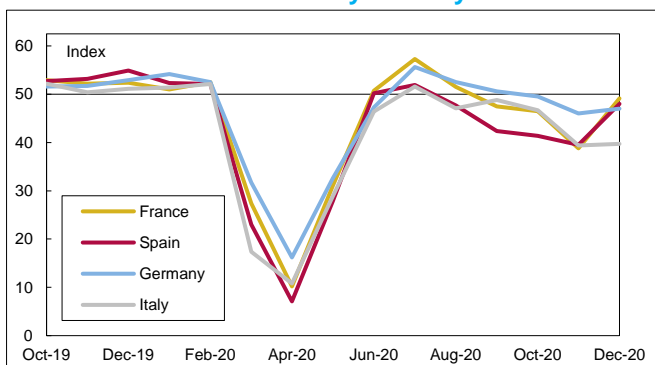
New car registrations cap worst year since 1992

Like in the euro area, UK new car registrations ended 2020 on a suitably disappointing note, falling 10.9%Y/Y following the steeper drop of 27.3%Y/Y the prior month. Following the extreme declines during the first wave of pandemic in the spring and a subsequent V-shaped rebound in Q3, the weakness at the end of the year meant that only 1.631mn new cars were registered in 2020, down 29.4%Y/Y to the mark the lowest full-year level since 1992. Admittedly, the decline in sales in the fourth quarter was not as marked as during the initial period of lockdown thanks not least to click-and-collect sales, which were able to continue even as showrooms were shut due to the pandemic restrictions. Nevertheless, sales to all main categories of customers – private, business and fleet – fell sharply in November and December. And with Covid-19 containment measures likely to last throughout the first quarter, another year of total new car registrations below 2mn seems likely in 2021. One bright spot, however, was the marked rise in sales of battery electric vehicles, whose share of total new registrations increased by 5ppts in 2020 to 6.6%, while the combined share of plug-in and hybrid electric vehicles near-doubled to 10.9%. Further solid growth in those categories seems inevitable this year.

Final services PMIs point to renewed weakening as year-end approached

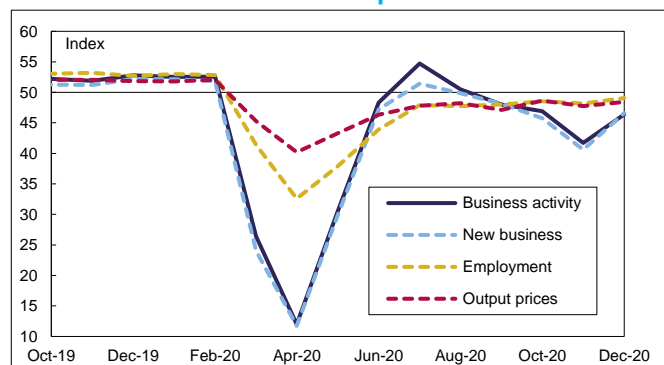
Like in the euro area, the final services PMIs for December pointed to a renewed weakening in the sector as the month went on, almost certainly in response to the worsening in the pandemic, particularly in London and the South East. In particular, the headline services activity PMI was revised down 0.5pt from the flash estimate to 49.4, still up almost 2pts from November when lockdown restrictions in England were tighter but consistent with contraction in the sector nevertheless. Also as in the euro area, all key survey indicators of current momentum – including new business, new export orders and employment – pointed to ongoing weakness. And despite increased cost pressures, output prices in the sector fell for a fourth successive month. Buoyed by the vaccine roll-out, however, the survey measure of business expectations twelve months ahead rose to the highest in almost six years. So, while this week's tighter new restrictions will likely last to the end of March, all but guaranteeing a steeper pace of contraction in GDP in Q121 than in Q420, there is some light at the tunnel for as long as the vaccines are judged effective.

Euro area: Services PMIs by country



Source: Markit, Refinitiv and Daiwa Capital Markets Europe Ltd.

Euro area: Services PMI components

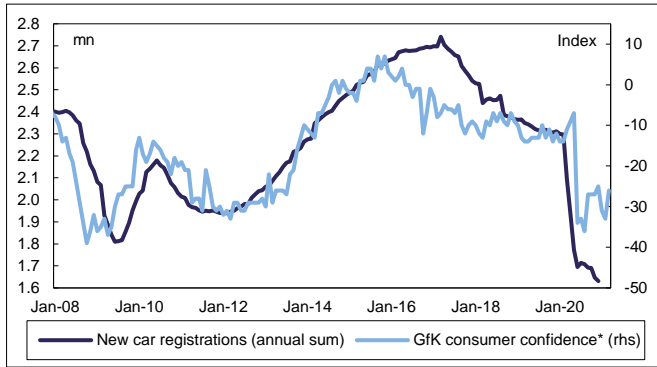


Source: Markit, Refinitiv and Daiwa Capital Markets Europe Ltd.

The day ahead in the UK

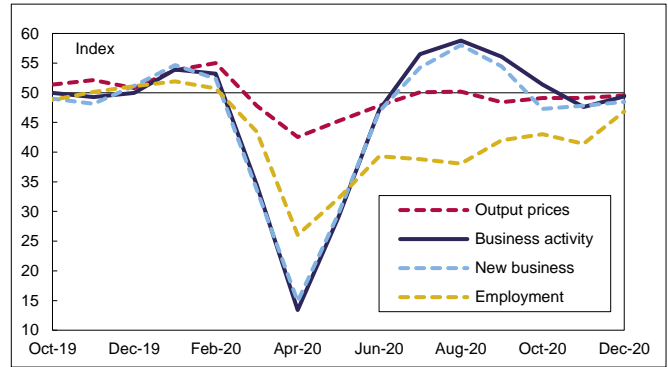
Like in the euro area, Thursday will bring the UK's construction PMIs for December. The headline index is likely to fall from 54.7 in November, albeit remaining above the key 50 expansion/contraction level as the sector avoided the more stringent restrictions affecting the services sector.

UK: New car registrations & consumer confidence



*Confidence has three-month lead.
Source: GfK, Refinitiv and Daiwa Capital Markets Europe Ltd.

UK: Services PMI components















Source: Markit, Refinitiv 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
EMU	 Final services (composite) PMI	Dec	46.4 (49.1)	47.3 (49.8)	41.7 (45.3)	-
	 PPI Y/Y%	Nov	0.4 (-1.9)	-2.1	-2.2	-
Germany	 Final services (composite) PMI	Dec	47.0 (52.0)	47.7 (52.5)	46.0 (51.7)	-
	 Preliminary CPI (EU-harmonised CPI) Y/Y%	Dec	-0.3 (-0.7)	-0.2 (-0.6)	-0.3 (-0.7)	-
France	 Final services (composite) PMI	Dec	49.1 (49.5)	49.2 (49.6)	38.8 (40.6)	-
	 INSEE consumer confidence	Dec	95	92	90	-
	 Preliminary CPI (EU-harmonised CPI) Y/Y%	Dec	0.0 (0.0)	0.2 (0.2)	0.2 (0.2)	-
Italy	 Services (composite) PMI	Dec	39.7 (43.0)	45.0 (47.3)	39.4 (42.7)	-
Spain	 Services (composite) PMI	Dec	48.0 (48.7)	44.0 (45.6)	39.5 (41.7)	-
UK	 BRC shop price index Y/Y%	Dec	-1.8	-	-1.8	-
	 Final services (composite) PMI	Dec	49.4 (50.4)	49.9 (50.7)	47.6 (49.0)	-
	 New car registrations Y/Y%	Dec	-10.9	-	-27.4	-













Auctions

Country	Auction
Germany	 Auction: €4.12bn of 0% 2031 bonds at an average yield of -0.52%
UK	 Auction: £3bn of 0.25% 2031 bonds at an average yield of 0.332%









Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

Tomorrow's releases

Economic data

Country	GMT	Release	Period	Market consensus/ <i>Daiwa forecast</i>	Previous
EMU	08.30	 Construction PMI	Dec	-	45.6
	10.00	 European Commission economic confidence	Dec	89.4	87.6
	10.00	 European Commission final consumer confidence	Dec	-13.9	-17.6
	10.00	 European Commission industrial (services) confidence	Dec	-8.7 (-15.0)	-10.1 (-17.3)
	10.00	 Retail sales M/M% (Y/Y%)	Nov	-3.2 (1.0)	1.5 (4.3)
	10.00	 CPI estimate (core CPI) Y/Y%	Dec	-0.3 (0.2)	-0.3 (0.2)
Germany	07.00	 Factory orders M/M% (Y/Y%)	Nov	-1.2 (2.5)	2.9 (1.8)
	08.30	 Construction PMI	Dec	-	45.6
France	08.30	 Construction PMI	Dec	-	42.8
Italy	08.30	 Construction PMI	Dec	-	49.8
	10.00	 Preliminary CPI (EU-harmonised CPI) Y/Y%	Dec	-0.2 (-0.3)	-0.3 (-0.3)
UK	08.30	 Construction PMI	Dec	-	54.7

Auctions and events

France	 09.50	Auction: 0.5% 2040 bonds
	 09.50	Auction: 0% 2030 bonds
	 09.50	Auction: 0.75% 2052 bonds
Spain	 09.45	Auction: 0% 2026 bonds
	 09.45	Auction: 0.7% 2033 index-linked bonds
	 09.45	Auction: 1% 2050 bonds
	 09.45	Auction: 2024 bond
UK	 09.30	BoE publishes Decision Maker Panel data

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

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