Europe | Economic Research | 04 January 2022

Euro wrap-up

Overview

- Bunds made modest gains despite data suggesting ongoing resilience in the labour market in Germany and Spain at the end of last year and a pickup in German retail sales.
- Gilts played catch up with large losses as the market opened after yesterday's public holiday, while the UK manufacturing PMI survey implied ongoing moderate expansion in the sector.
- Tomorrow brings the final euro area services PMIs and flash Italian inflation numbers for December.

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Daily bond market movements

Bond	Yield	Change
BKO 0 12/23	-0.631	-0.010
OBL 0 10/26	-0.437	-0.016
DBR 0 08/31	-0.142	-0.017
UKT 0¹/₈ 01/24	0.724	+0.082
UKT 0³/₈ 10/26	0.886	+0.089
UKT 0¼ 07/31	1.068	+0.103

*Change from close as at 4:00pm GMT.
Source: Bloomberg

Euro area

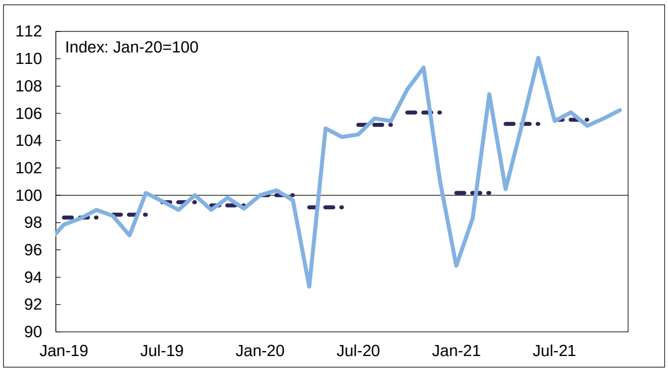
Economic activity probably slowing but not shrinking

The wave of Covid-19 that got underway in November and December continues to spread across Europe, with a notable surge in France, Italy and Spain into the New Year. While the number of new cases, and ICU occupancy, has fallen back in Germany, the spread of Omicron risks a rebound in early 2022. So, selective restrictions remain in force across the region. Indeed, some measures were tightened over recent days, e.g. German nightclubs closed from 28 December, and working from home became the default in France with masks mandatory out of doors from yesterday. However, certain other measures have been slightly relaxed. Germany eased restrictions on travel from several countries, including the UK, while the length of quarantine for fully vaccinated people in France and Spain has been reduced. On the whole, at least for the vaccinated, restrictions remain less stringent than during previous lockdowns. While mobility data suggest a drop in travel for retail and recreation, as well as work, from the early autumn, they also suggest a relatively manageable impact. Evidence continues to suggest that the Omicron variant poses less of a threat to health systems than earlier variants. And given the increased economic resilience to the pandemic over previous successive waves, euro area GDP is likely to have slowed in Q421 and Q122 close to the rates of 0.2%Q/Q and 0.4%Q/Q respectively forecast by the ECB last month, rather than suffer an outright contraction.

German labour market resilient amid steady retail sales and signs of pickup in industrial sector

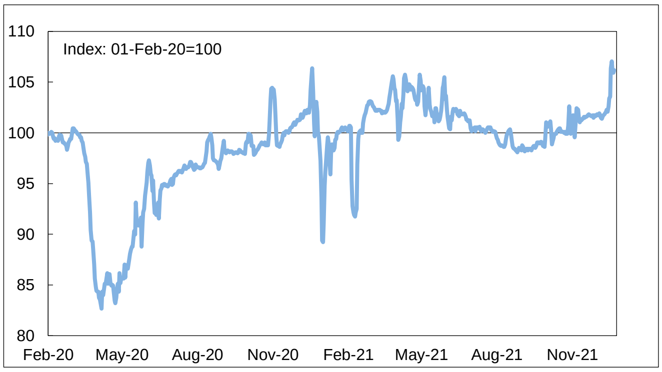
Germany's labour market certainly continued to display resilience towards the end of the year. The claimant count dropped for an eighth successive month in December and by a larger-than-expected 23k (albeit the least since May) to 2.405mn, some 523k below the pandemic peak in June 2020. As a result, the claimant count rate declined by 0.1ppt for a third successive month in December to 5.2%, just 0.2ppt above the pre-pandemic level and 1.2ppts below the pandemic peak. And while the number of workers benefiting from the government's kurzarbeit short-term working scheme probably increased towards year-end, the further 21k rise in vacancies in December to a series high of 817k suggests that German firms are not overly alarmed about the impact of the latest coronavirus wave. Admittedly, unexpected growth in German retail sales in November – which rose 0.6%M/M to take the average in the first two months of Q4 0.4% above the Q3 average – came before most restrictions were tightened at the national level. However, the rise in the truck toll mileage index in December points to a stronger end to the year for Germany's industrial sector, which should help to offset some of the weakness likely to have been experienced in consumer-facing services. Beyond Germany, Spain's labour market also appears to have remained firm at the end of 2021, with registered unemployment down for an eighth successive month in adjusted terms in December and by more than 40k to 3.09mn, 60k below the level at the end of 2019 and more than 925k below the pandemic

Germany: Retail sales*



**Dashed lines represent quarterly average. Source: Refinitiv and Daiwa Capital Markets Europe Ltd.*

Germany: Truck toll mileage index



Source: Refinitiv and Daiwa Capital Markets Europe Ltd.

peak in June 2020. And Spanish registered employment rose a further 70.8k on an adjusted basis to a new series high of 19.842mn, more than 360k above the pre-pandemic peak.

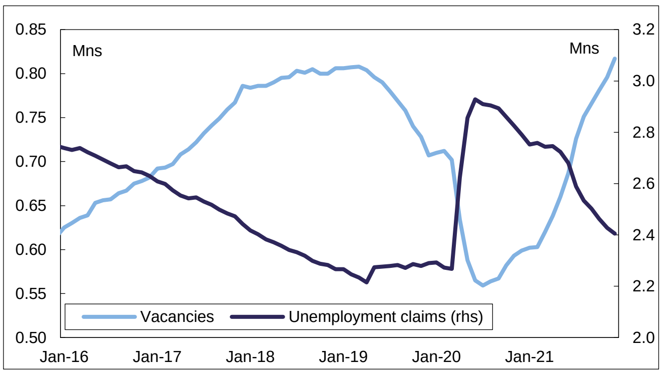
Final PMIs hint at easing supply chain pressures amid moderate production growth

Yesterday's final euro area manufacturing PMIs offered no major revisions from the flash release and thus also remained consistent with modest growth in the sector in the fourth quarter with the output PMI moving sideways in December at 53.8, admittedly matching the lowest since July 2020. Of most note were the hints of an easing of supply-side constraints, with supplier delivery times the shortest since February (albeit still significantly longer than the pre-pandemic norm) allowing firms to replenish their inventories at the fastest rate in the survey's history. However, demand was slightly softer than initially estimated, with the new orders PMI down 0.9pt on the month to the lowest reading since November 2020. Despite easing slightly, price pressures in the sector remained extremely elevated. At the country level, in spite of a sizeable downwards revision from the flash estimate, Germany's output PMI was still up 0.7pt in December at 52.1, a three-month high although still well below the average level (64.1) seen through the first half of last year. The French output PMI also reached a three-month high in December (50.4), while the equivalent Spanish index increased for the first month in four (up 1.2pts to 53.7). So, at face value, the biggest disappointment in yesterday's release was the 2.5pts drop in the Italian output PMI, although at 59.7 it still implied the strongest production growth among member states and at a broadly similar pace to the average for the year as a whole.

New car registrations remain very weak

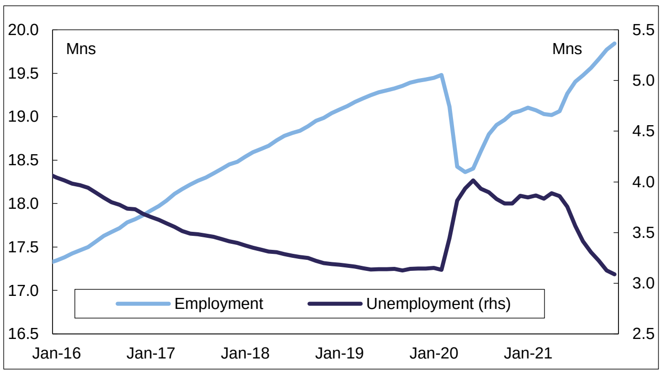
Supply-chain disruption has been most acutely felt in the autos sector, with the impact again apparent in the first December new car registrations numbers from the member states. Despite a further modest improvement, French registrations remained well down on a year earlier (-15.1%Y/Y) to reach the lowest level for any December since 2008. Over the year as a whole, with the exception of 2020, French new car registrations dropped to the lowest since 1975, roughly one quarter below their level in 2019. Italian car registrations weakened further in December, to be down 27.5%Y/Y and 38% lower than in December 2019 to be the weakest for the month since 1993. While this left full-year Italian sales up more than 5% compared with 2020, they were still down by almost 25% compared with 2019. Spain's new car registrations were the strongest since August. Nevertheless, they were still down 18.7%Y/Y. So, while they were marginally higher than in 2020, Spanish full-year sales were still almost one third lower than in 2019.

Germany: Unemployment and job vacancies



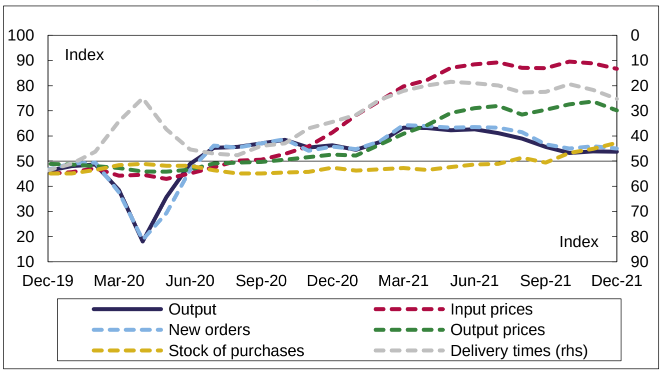
Source: Refinitiv and Daiwa Capital Markets Europe Ltd.

Spain: Unemployment and employment



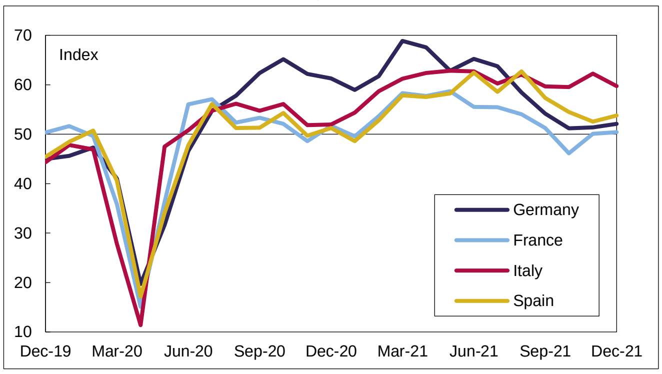
Source: Refinitiv and Daiwa Capital Markets Europe Ltd.

Euro area: Manufacturing PMIs



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

Euro area: Manufacturing PMIs by member state*



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

The day ahead in the euro area

Ahead of Friday's release of the euro area's December flash inflation estimate, tomorrow will bring further insight with the release of the preliminary Italian CPI numbers. These will follow today's equivalent French figures, which showed headline inflation (on the EU-harmonised basis) moving sideways in December at 3.4%Y/Y. Within the detail on the national measure, a jump in manufactured goods inflation was offset by a modest easing in the services and energy components. In contrast, the Spanish data, published at the end of last year, showed headline inflation surging 1.2ppts to 6.7%Y/Y, the highest since March 1992. But this reflected higher electricity and food prices – indeed, core inflation (on the national measure) rose 0.4ppt to just 2.1%Y/Y. Wednesday will also bring revised December services and composite PMIs from the euro area and member states, which might well bring about a further downwards revision to the output indices as new coronavirus cases in France, Italy and Spain surged over the festive period. The latest French consumer confidence survey also seems bound to report a more downbeat assessment in the final month of last year.

UK

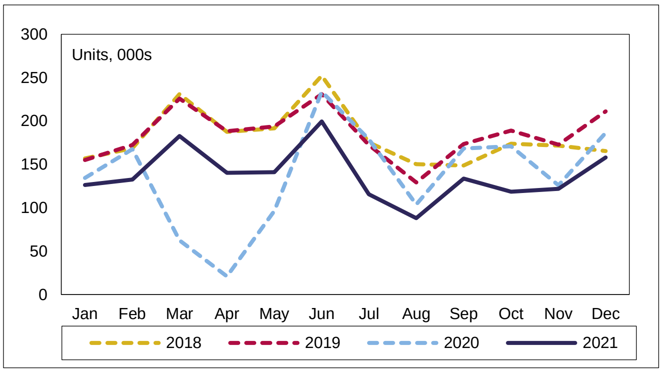
Hit to activity from Omicron likely to be less severe than in previous waves

Like several euro area member states, the number of new coronavirus cases in the UK surged during the festive period, with the total of new positive tests over the past seven days reaching almost 1.2mn. But with hospital admissions still well down from past peaks, and now declining in the Omicron hotspot of London, and only limited restrictions in place across England, the effect on overall economic output looks set to be relatively limited. Admittedly, high frequency data suggest a non-negligible negative impact on activity in hospitality and recreation from mid-December, which will likely weigh on GDP around the turn of the year. But while travel for employment will likely remain weak for the next fortnight as the government encourages continued working from home, it remains well above the troughs seen previously. And assuming no tightening of restrictions when PM Johnson gives an update tomorrow evening, we continue to think that UK GDP will have slowed in Q421 and Q122, to leave growth moderately softer than the rates of 1.0%Q/Q and 1.2%Q/Q in each quarter projected in November by the BoE, rather than contracted outright.

Final manufacturing PMI implies ongoing moderate expansion

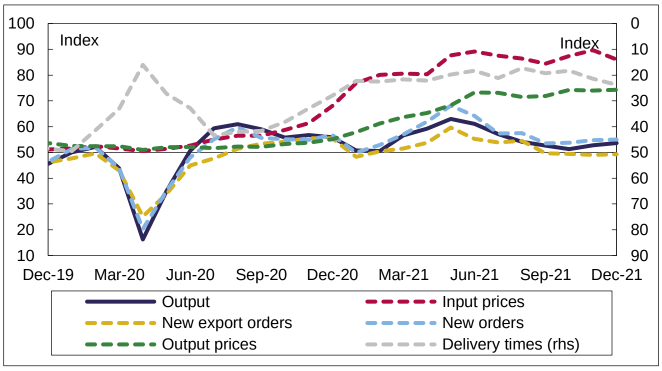
Certainly, the UK's final manufacturing PMI survey today suggested limited additional impact from the emergence of Omicron. For now, at least, firms indicate that the supply-chain crisis has started to stabilise somewhat, with supplier delivery

France: New car registrations



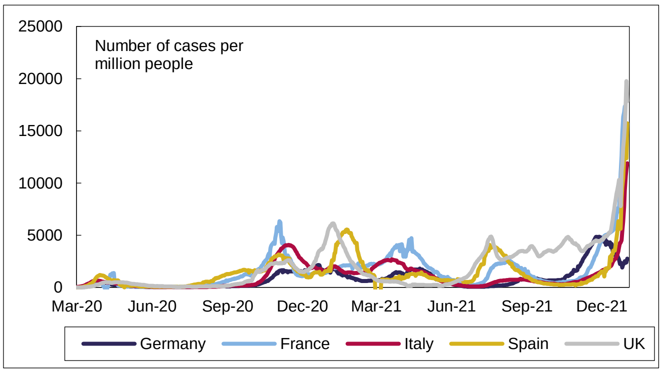
Source: Refinitiv and Daiwa Capital Markets Europe Ltd.

UK: Manufacturing PMIs



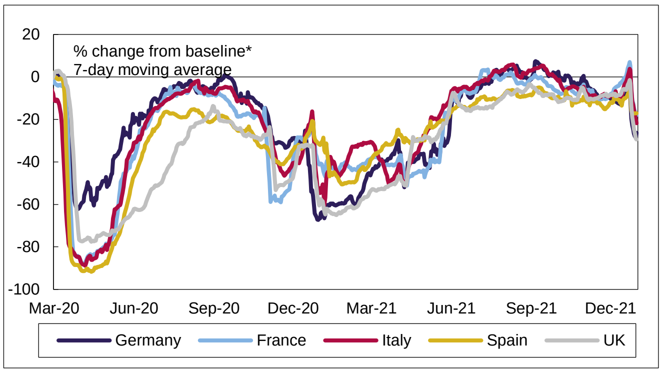
Source: Refinitiv, Markit and Daiwa Capital Markets Europe Ltd.

New coronavirus cases



Source: *OurWorldinData and Daiwa Capital Markets Europe Ltd.*

Mobility: Travel for retail and recreation



**Compared to the median value, for the corresponding day of the week, during the five week period 3-Jan – 6-Feb 2020. Source: Google Mobility Data and Daiwa Capital Markets Europe Ltd.*

times the shortest last year and allowing a further increase in output. Indeed, the respective survey component was up by 0.9pt to 53.6, a four-month high, supported by a 6.3pt rebound in the investment goods output PMI (54.1). But while the consumer and intermediate goods output PMIs (54.7 and 52.1 respectively) implied ongoing growth they were softer than in November. Although domestic new orders remained positive, the relevant index was still well down on levels seen earlier in the year. And overseas orders continued to fall as the implementation of new Brexit-related customs controls from the start of this year, logistical difficulties, and the possibility of further pandemic-related restrictions weighed on external demand. While manufacturers remained broadly upbeat about the production outlook for the year ahead, with factories across Asia expected to remain disrupted by Omicron, supply-chain challenges may yet worsen once again over the near term, which in turn could inject additional price pressures.

The day ahead in the UK

Tomorrow should be a quiet day for UK economic news, with no top-tier data due for release.

European calendar

Today's results

Economic data

Country	Release	Period	**Actual**	Market consensus/ *Daiwa forecast*	Previous	Revised
Germany	Retail sales M/M% (Y/Y%)	Nov	**0.6 (-0.2)**	-0.3 (-3.1)	-0.3 (-4.1)	0.5 (-3.3)
	Unemployment rate % (change 000s)	Dec	**5.2 (-23)**	5.3 (-15)	5.3 (-34)	-
France	Preliminary CPI (EU-harmonised CPI) Y/Y%	Dec	**2.8 (3.4)**	2.9 (3.5)	2.8 (3.4)	-
Spain	Unemployment change 000s	Dec	**-76.8**	-	-74.4	-
UK	BRC shop price index Y/Y%	Dec	**0.8**	-	0.3	-
	Final manufacturing PMI	Dec	**57.9**	57.6	58.1	-
	Net consumer credit £bn (Y/Y%)	Nov	**1.2 (0.4)**	0.8 (-)	0.7 (-1.0)	0.8 (-)
	Net mortgage lending £bn (mortgage approvals 000s)	Nov	**3.7 (67.0)**	3.1 (66.0)	1.6 (67.2)	1.1 (67.1)

Auctions

Country	Auction
Germany	sold €3.96bn of 0% 2023 bonds at an average yield of -0.62%

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

Yesterday's results

Economic data

Country	Release	Period	**Actual**	Market consensus/ *Daiwa forecast*	Previous	Revised
Euro area	Final manufacturing PMI	Dec	**58.0**	58.0	58.4	-
Germany	Final manufacturing PMI	Dec	**57.4**	57.9	57.4	-
France	Final manufacturing PMI	Dec	**55.6**	54.9	55.9	-
	New car registrations Y/Y%	Dec	**-15.1**	-	-3.2	-
Italy	Manufacturing PMI	Dec	**62.0**	61.5	62.8	-
	New car registrations Y/Y%	Dec	**-27.5**	-	-24.6	-
Spain	Manufacturing PMI	Dec	**56.2**	56.4	57.1	-
	New car registrations Y/Y%	Dec	**-18.7**	-	-12.3	-

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/ *Daiwa forecast***	**Previous**
Euro area	09.00	Final services (composite) PMIs	Dec	53.3 (53.4)	55.9 (55.4)
Germany	08.55	Final services (composite) PMIs	Dec	48.4 (50.0)	52.7 (52.2)
	-	New car registrations (production)* Y/Y%	Dec	-	-31.7 (-31.7)
France	08.50	Final services (composite) PMIs	Dec	57.1 (55.6)	57.4 (56.1)
	07.45	INSEE consumer confidence	Dec	97	99
Italy	08.45	Services (composite) PMIs	Dec	54.0 (56.1)	55.9 (57.6)
	10.00	Preliminary CPI (EU-harmonised CPI) Y/Y%	Dec	3.8 (4.2)	3.7 (3.9)
Spain	08.15	Services (composite) PMIs	Dec	57.4 (56.0)	59.8 (58.3)
Auctions and events					
Germany	10.30	Auction: €4bn of 0% 2032 bonds			
Spain	09.30	Auction: to sell 0% 2024 bonds			
	09.30	Auction: to sell 0% 2028 bonds			
	09.30	Auction: to sell 0.85% 2037 bonds			
	09.30	Auction: to sell 0.65% 2027 index-linked bonds			

**Approximate date of release. Source: Bloomberg and Daiwa Capital Markets Europe Ltd.*