

# Euro wrap-up

## Overview

- Bunds made modest losses as the flash euro area inflation estimate came in a touch firmer than expected, but the Commission's survey flagged a hit to services activity in December and German IP data disappointed.
- Gilts also made small losses as the UK construction PMI was consistent with ongoing moderate growth in the sector in December.
- The coming week brings euro area unemployment, IP and trade data, as well as the UK's monthly GDP report, all for the month of November.

**Chris Scicluna**  
+44 20 7597 8326

**Emily Nicol**  
+44 20 7597 8331

### Daily bond market movements

Bond	Yield	Change
BKO 0 12/23	-0.600	+0.017
OBL 0 10/26	-0.381	+0.027
DBR 0 02/32	-0.045	+0.021
UKT 0 <sup>1</sup> / <sub>8</sub> 01/24	0.827	+0.012
UKT 0 <sup>3</sup> / <sub>8</sub> 10/26	0.982	+0.019
UKT 0 <sup>1</sup> / <sub>4</sub> 07/31	1.176	+0.020

\*Change from close as at 4:15pm GMT.  
Source: Bloomberg

## Euro area

### Inflation edges up in December on higher prices of food and other goods

According to today's flash estimates, euro area consumer price inflation edged up in December, confounding expectations of a marginal drop. However, the rise of 0.1ppt to 5.0%Y/Y in the headline HICP rate is highly likely to represent the peak. Within the detail, additional pressure at the end of the year came from non-energy industrial goods inflation, which jumped 0.5ppt to a euro-era high of 2.9%Y/Y as some pipeline pressures appeared to be passed on to consumers. But that impact was offset by a drop in services inflation of 0.3ppt to 2.4%Y/Y, perhaps in part weighed by the revival in the pandemic. So, core inflation (excluding energy, food and tobacco) was unchanged at 2.6%Y/Y. Among the non-core components, energy inflation still accounted for roughly half of all inflation despite falling for the first time in eleven months, down 1.5ppts to 26.0%Y/Y. In part, the decline reflected lower petroleum prices, which helped to offset the impact of sharply higher household energy bills in Spain related to wholesale gas price pressures. In contrast, food inflation jumped 1.0ppt to a nineteen-month high of 3.2%Y/Y.

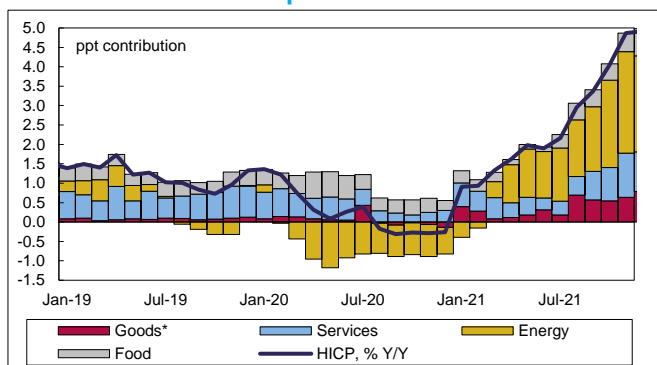
### Inflation will drop in New Year and should move steadily lower through H22

Looking ahead, the inflation outlook is highly uncertain, and will continue to be impacted by the pandemic, both in Europe and globally. However, headline inflation will take a step down in January as the effect of German tax changes fall out of the calculation. In the absence of new pressures in wholesale gas markets – which will in part reflect relations with Russia as well as the vagaries of the weather – energy inflation will move lower as the year goes on not least due to base effects. Assuming that supply-chain strains ease steadily, as surveys suggest they should do, non-energy industrial goods inflation will also likely fall back. And with wage pressures still muted, services inflation should remain contained. So, we expect headline inflation to be back close to 4.0%Y/Y in January, and to decline further in the second half of 2022 to below 2.0%Y/Y by year-end. Today's Commission survey suggested that inflation expectations are starting to moderate too. The survey index of consumer price expectations fell for a second successive month in December, with the selling price expectations indices for retail, services, manufacturing and construction all easing slightly too.

### Economic sentiment in December hit by the Omicron variant

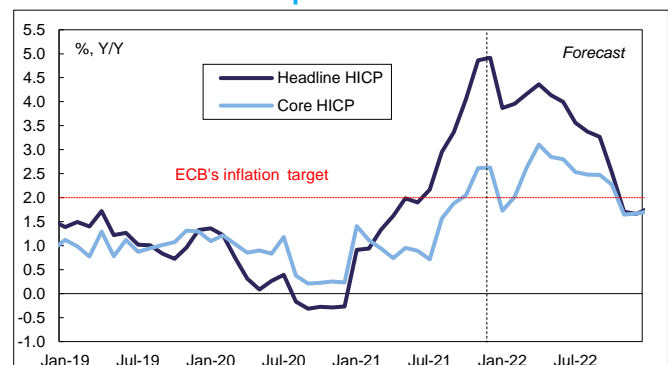
In terms of economic activity, today's Commission survey results flagged the adverse impact of the current wave of pandemic and associated restrictions across the member states. The headline euro area economic sentiment indicator (ESI) fell for the second successive month and by the most (-2.3pts) since November 2020 to 115.3, its lowest since May and almost 4pts below the survey high reached in July. While the deterioration was widespread, the most severe declines were

### Euro area: Consumer price inflation – contributions



Source: Refinitiv and Daiwa Capital Markets Europe Ltd.

### Euro area: Consumer price inflation – forecast



Source: Refinitiv and Daiwa Capital Markets Europe Ltd.

seen in those countries with the tightest restrictions – Germany (-2.8pts), Netherlands (-4.1pts) and Austria (-5.4pts). Admittedly, the survey was conducted before the surge in cases in France, Italy and Spain over the festive period. Nevertheless, the euro area ESI still remained at a historically high level and well above the long-run average (100). Moreover, the quarterly average (117.2) was the third-highest on record and just 0.9pt lower than in Q3, consistent with the view that GDP growth slowed, rather than went into reverse, in the final quarter of 2021.

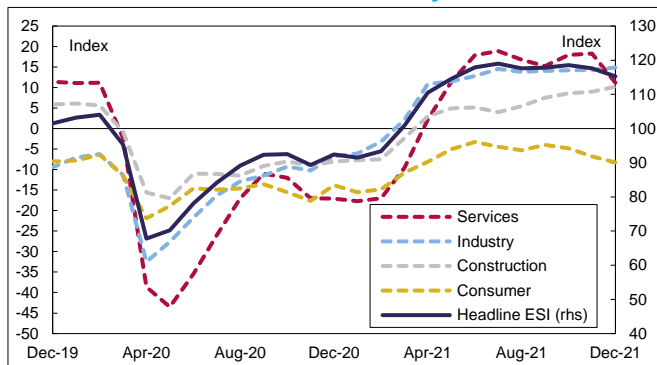
### Consumer-facing sectors most severely impacted, manufacturers more upbeat

Within the detail, the hit to sentiment was unsurprisingly most striking in the consumer-facing sectors, with the services index down 7.1pts (the most since the onset of the pandemic) to 11.2, the lowest since May but broadly in line with the long-run average. Retailers were less upbeat too – the respective index was down 2.6pts to a seven-month low. And consumers were the most downbeat since April as expectations for the economic outlook and future purchases fell and unemployment fears rose. In contrast, sentiment in industry rose to a fresh series high (up 0.6pt to 14.9) supported by strong order books in the sector, while manufacturers noted a marked improvement in past production. Construction firms were also more optimistic on the back of elevated order books, with the sector's headline index matching the record high previously reached in late 2018. As such, there was a further increase in employment expectations across most sub-sectors, with the respective index in manufacturing rising to a survey record. But given heightened uncertainties about the near-term outlook, services firms scaled back their employment intentions for the first month in five.

### Euro area retail sales strengthen ahead of the new pandemic wave

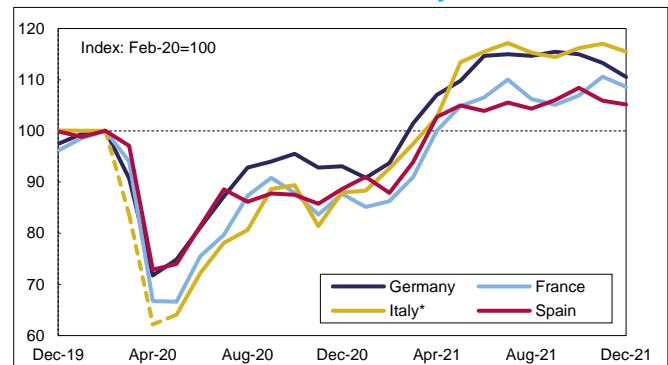
Despite the resurgence in the Delta variant and tighter restrictions on unvaccinated people in certain member states in November, euro area retailers saw a solid rise in sales for the second successive month, by 1.0%M/M, the largest monthly increase since June. This was underpinned by a near-4%M/M rise in Spain, back to the pre-pandemic level for the first time, with moderate growth in Germany (0.6%M/M) and France (1.1%M/M) too. And this was in spite of the largest monthly drop in fuel sales (-1.5%M/M) in a year as mobility was reduced. Indeed, spending on food rose for the third consecutive month (0.6%M/M), while core sales (excluding food and fuel) jumped 1.6%M/M. And perhaps in light of the rise in coronavirus cases, there was a further increase in online purchases, to leave them trending in October and November almost 3% above the Q3 average. Overall, retail sales in the first two months of Q4 averaged 1% higher than in Q3. But while retail sales may well have remained firm in the run up to Christmas, spending on consumer-facing services likely took a sharp step down.

#### Euro area: Economic sentiment by sector



Source: Refinitiv, European Commission and Daiwa Capital Markets Europe Ltd.

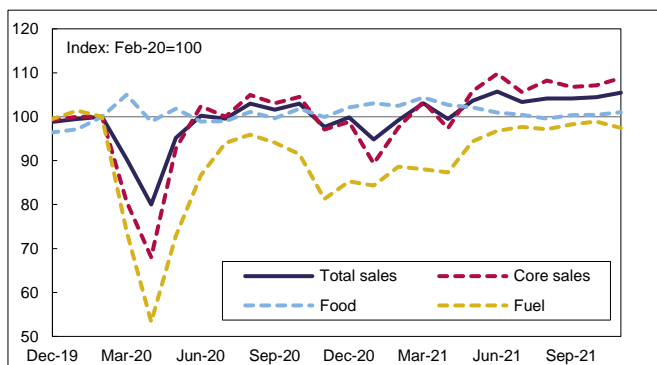
#### Euro area: Economic sentiment by member state



\*No survey results in April 2020.

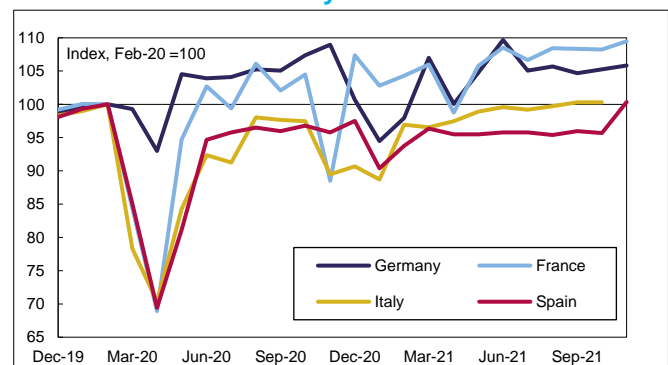
Source: Refinitiv, European Commission and Daiwa Capital Markets Europe Ltd.

#### Euro area: Retail sales



Source: Refinitiv and Daiwa Capital Markets Europe Ltd.

#### Euro area: Retail sales by member state



Source: Refinitiv and Daiwa Capital Markets Europe Ltd.

## German IP disappoints despite accelerating autos production

After yesterday's German data revealed another solid month of [manufacturing turnover](#) in November, today's IP report was underwhelming, with total output declining 0.2%M/M following downwardly revised growth (2.4%M/M) in October. Part of this weakness reflected a near-4½%M/M drop in energy output, while construction activity also fell 0.8%M/M. But contrasting with the surge in manufacturing sales (4.1%M/M), manufacturing output rose just 0.1%M/M in November, the largest discrepancy in growth since reunification. Within the detail, production of capital goods fell 0.8%M/M, as a decline in machinery and equipment (-3.6%M/M to its lowest level since 2020) offset a further recovery in autos production (4.1%M/M). More encouragingly, production of intermediate goods rose for the second-successive month (0.8%M/M), while output of consumer goods increased (0.8%M/M) to its third-highest level since the pandemic. Overall, manufacturing output in the first two months of Q4 was trending 0.8% above the Q3 average. With other manufacturing indicators – e.g. truck toll mileage, turnover and sentiment surveys including the ESI and PMIs – raising the possibility of an upwards revision to November's IP data in due course, as well as pointing to a solid outturn in December, we maintain our view that manufacturing will provide a welcome boost to GDP growth in Q4. Today's goods trade numbers were also suggestive of a modest positive contribution from net trade to GDP growth in Q4. For example, export volumes rose for a second month in November (0.9%M/M) to leave them trending almost 1½% higher than the Q3 average. Meanwhile, import volumes were up a more modest 0.4%M/M in November (with higher prices pushing import values up 3.3%M/M) to be averaging roughly 1% above the Q3 level.

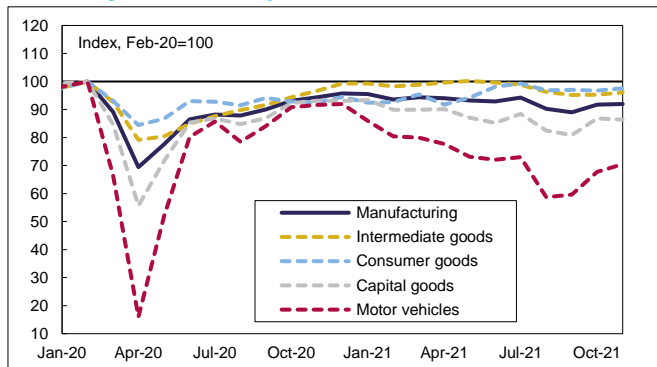
## French IP weakens in November too

French industrial production also fell short of expectations in November, with output down (-0.4%M/M) for the second month out of the past three. This in part reflected a near-1½%M/M decline in construction activity, but manufacturing output also fell (-0.6%M/M) to its second-lowest level since June. There were production declines in a range of sub-sectors from machinery and equipment (-1.4%M/M), textiles (-0.6%M/M) and pharmaceuticals (-0.5%M/M) and most substantially transport equipment (-4.6%M/M). But the latter reflected a reversal of the near-13%M/M increase in other transport – notably aircraft – seen in October, while autos output jumped (10.5%M/M) in November, albeit merely to its highest level since August. Overall, industrial output was trending so far in Q4 broadly sideways from Q3, with a modest drop in manufacturing offsetting higher output from the construction and energy sectors.

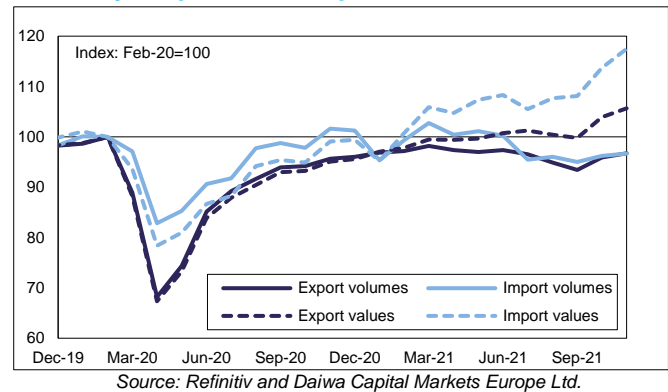
## The week ahead in the euro area

The coming week will get underway on Monday with the latest euro area unemployment figures for November, which are expected to report a further decline in the unemployment rate by 0.1pt to 7.2%, a fresh series low (when excluding the initial drop at the onset of the pandemic when many jobless workers found it difficult to search for work). The euro area Sentix

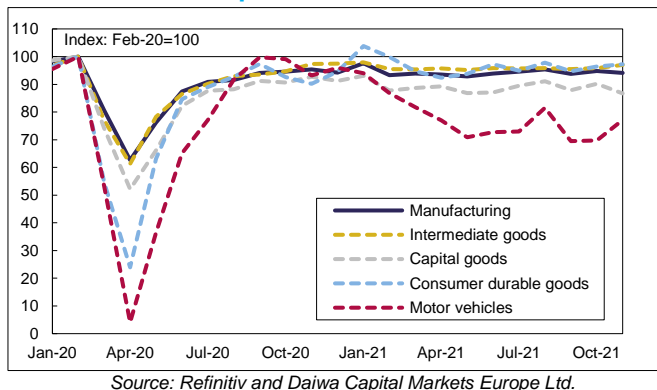
### Germany: Industrial production



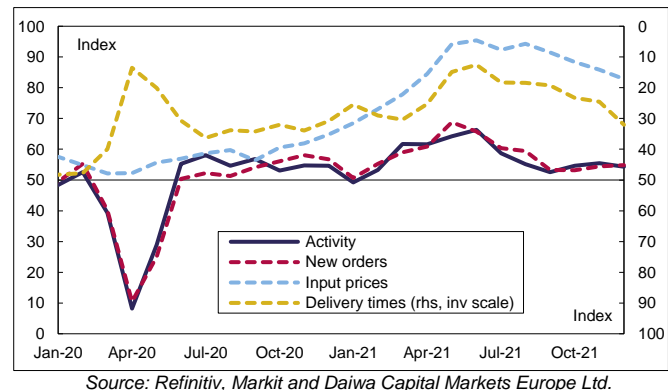
### Germany: Exports and imports



### France: Industrial production



### UK: Construction PMIs



survey for financial investors will also provide an update on sentiment at the start of January. Monday will also bring the latest industrial production numbers from Ireland, ahead of the equivalent Spanish and euro area numbers published on Tuesday and Wednesday respectively. Following today's weaker than expected figures from Germany and France, aggregate euro area industrial production growth is expected to be softer than the rise of 1.1%/M/M in October, with risks to the consensus increase of ½%/M/M skewed clearly to the downside. Euro area trade figures for November, due to be published on Friday, are expected to reveal that the trade surplus moved sideways, after falling to an eighteen-month low of €2.4bn in October due not least to higher energy prices. Friday will also bring updated French and Spanish inflation data for December, as well as Germany's full-year GDP figures for 2021. Tuesday will also bring the Bank of France's December sentiment survey, which will provide an update on its estimate for Q4 GDP.

## UK












### PMIs signal ongoing construction growth as supply strains ease somewhat

A quiet end to the week for UK economic data brought the December construction PMIs, which suggested that the sector provided some support to growth at the end of the year. In particular, while it dropped more than 1pt to a three-month low, the headline activity index remained in moderate growth territory at 54.3. In addition, a pickup in the new orders index to the highest since August (54.8), as well as ongoing job creation, indicates the prospect of ongoing growth in the sector in the current quarter. Although some firms, especially in commercial real estate, reported that tighter pandemic restrictions had impacted growth last month, overall the news on supply strains was much more encouraging. For example, the share of construction firms reporting supplier delays fell last month by a sizeable 13ppts to 34%. Overall supplier performance was judged to have deteriorated the least in thirteen months. And, while still high, input price inflation slowed to the lowest in nine months. Within the detail, growth in house-building saw the strongest growth, with an acceleration in December (the respective index rose to 55.3). In contrast, civil engineering activity (49.1) reportedly fell back for the first time since February.

### The week ahead in the UK

The UK data highlight of the coming week will be Friday's GDP report for November. High frequency data suggest that private sector services activity picked up, while retail sales recorded another month of strong growth. Additionally, a surge in the provision of booster vaccinations seems likely to have supported the health sector again. And with a modest pickup in manufacturing output also anticipated, we would expect to see a notable acceleration in GDP growth from the disappointing 0.1%/M/M rate recorded in October, with the likelihood that output returned back to its pre-pandemic level for the first time. Friday will also bring November's trade data. Ahead of this, the dataflow brings the BRC retail sales monitor (Tuesday), the REC/KPMG report on jobs and RICS residential survey (Thursday), all for the month of December.














## Daiwa economic forecasts

	2021		2022				2021	2022	2023
	Q3	Q4	Q1	Q2	Q3	Q4			
<b>GDP forecasts %, Q/Q</b>									
Euro area 	2.2	0.3	0.2	1.5	1.0	0.5	5.1	3.9	2.7
UK 	1.3	0.6	0.4	1.2	0.6	0.6	6.8	4.2	1.9
<b>Inflation forecasts %, Y/Y</b>									
Euro area									
Headline CPI 	2.8	4.6	4.0	4.2	3.4	2.0	2.6	3.4	1.8
Core CPI 	1.4	2.4	2.1	2.9	2.5	1.9	1.5	2.4	1.7
UK									
Headline CPI 	2.8	4.9	5.4	5.3	4.6	2.8	2.6	4.5	1.9
Core CPI 	2.6	3.8	4.2	3.7	3.1	2.1	2.4	3.3	2.0
<b>Monetary policy</b>									
ECB									
Refi Rate % 	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00
Deposit Rate % 	-0.50	-0.50	-0.50	-0.50	-0.50	-0.50	-0.50	-0.50	-0.25
PEPP envelope* (€bn) 	1850	1850	1850	1850	1850	1850	1850	1850	1850
BoE									
Bank Rate % 	0.10	0.25	0.25	0.50	0.50	0.75	0.25	0.75	1.00
Gilt purchases* (£bn) 	875	875	875	875	866	866	875	866	833

\*Target end of period. Source: Bloomberg, ECB, BoE and Daiwa Capital Markets Europe Ltd.









## The coming week's data calendar

### The coming week's key data releases

Country	GMT	Release	Period	Market consensus/ <i>Daiwa</i> <i>forecast/actual</i>	Previous
<b>Monday 10 January 2022</b>					
Euro area 	09.30	Sentix investor confidence	Jan	12.3	13.5
	10.00	Unemployment rate %	Nov	7.2	7.3
<b>Tuesday 11 January 2022</b>					
France 	-	Bank of France industrial sentiment	Dec	104	104
Italy 	09.00	Retail sales M/M% (Y/Y%)	Nov	- (11.1)	0.1 (3.7)
Spain 	08.00	Industrial production M/M% (Y/Y%)	Nov	0.4 (0.5)	-0.4 (-0.9)
UK 	00.01	BRC retail sales monitor, like-for-like sales Y/Y%	Dec	-	1.8
	09.30	Final output per hour Y/Y%	Q3	-4.8	4.3
	09.30	Unit labour costs Y/Y%	Q3	-	-3.8
<b>Wednesday 12 January 2022</b>					
Euro area 	10.00	Industrial production M/M% (Y/Y%)	Nov	0.5 (0.8)	1.1 (3.3)
<b>Thursday 13 January 2022</b>					
Italy 	09.00	Industrial production M/M% (Y/Y%)	Nov	0.5 (3.7)	-0.6 (2.0)
UK 	00.01	RICS house price balance %	Dec	70	71
<b>Friday 14 January 2022</b>					
Euro area 	10.00	Trade balance €bn	Nov	1.5	2.4
Germany 	09.00	GDP Y/Y%	2021	2.7	-5.0
France 	07.45	Final CPI (EU-harmonised CPI) Y/Y%	Dec	2.8 (3.4)	2.8 (3.4)
Spain 	08.00	Final CPI (EU-harmonised CPI) Y/Y%	Dec	6.7 (6.7)	5.5 (5.5)
UK 	07.00	GDP M/M% (3M/3M%)	Nov	0.4 (0.8)	0.1 (0.9)
	07.00	Industrial production M/M% (Y/Y%)	Nov	0.2 (0.6)	-0.6 (0.4)
	07.00	Manufacturing production M/M% (Y/Y%)	Nov	0.2 (-0.3)	0.0 (1.3)
	07.00	Index of services M/M% (3M/3M)	Nov	0.5 (1.1)	0.4 (1.1)
	07.00	Construction output M/M% (Y/Y%)	Nov	0.3 (2.7)	-1.8 (3.3)
	07.00	Goods trade balance £bn	Nov	-14.2	-13.9

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

### The coming week's key events & auctions













Country	GMT	Event / Auction
<b>Monday 10 January 2022</b>		
- Nothing scheduled -		
<b>Tuesday 11 January 2022</b>		
Euro area 	11.20	ECB President Lagarde gives remarks at Bundesbank President handover ceremony
Germany 	10.30	Auction: €750mn of 2033 inflation-linked bonds
UK 	10.00	Auction: £3bn of 0.375% 2026 bonds
<b>Wednesday 12 January 2022</b>		
Germany 	10.30	Auction: €1.5bn of 0% 2052 bonds
<b>Thursday 13 January 2022</b>		
Euro area 	11.30	ECB Vice President de Guindos takes part in a virtual Q&A event
	-	Eurostat to publish euro area labour force survey for Q3
Italy 	10.00	Auction: 3Y and 7Y bonds
UK 	00.01	KPMG/REC report on jobs
	09.30	Bank of England publishes Bank Liabilities and Credit Conditions surveys
<b>Friday 14 January 2022</b>		
Euro area 	13.30	ECB President Lagarde scheduled to speak

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.



## Today's results

### Economic data

Country	Release	Period	Actual	Market consensus/ <i>Daiwa forecast</i>	Previous	Revised
Euro area	 Preliminary CPI (core CPI) Y/Y%	Dec	<b>5.0 (2.6)</b>	<u>4.8 (2.7)</u>	4.9 (2.6)	-
	 Retail sales M/M% (Y/Y%)	Nov	<b>1.0 (7.8)</b>	-0.5 (5.6)	0.2 (1.4)	<b>0.3 (1.7)</b>
	 European Commission's economic sentiment indicator	Dec	<b>115.3</b>	116.0	117.5	<b>117.6</b>
	 European Commission's final consumer confidence	Dec	<b>-8.3</b>	-8.3	-6.8	-
	 European Commission's industrial (services) confidence	Dec	<b>14.9 (11.2)</b>	14.1 (16.1)	14.1 (18.4)	<b>14.3 (18.3)</b>
Germany	 Industrial production M/M% (Y/Y%)	Nov	<b>-0.2 (-2.4)</b>	1.0 (-0.8)	2.8 (-0.6)	<b>2.4 (-0.9)</b>
	 Trade balance €bn	Nov	<b>12.0</b>	12.8	12.8	<b>12.7</b>
France	 Consumer spending M/M% (Y/Y%)	Nov	<b>0.8 (14.8)</b>	0.5 (13.9)	-0.4 (-5.3)	<b>-0.6 (-5.6)</b>
	 Industrial production M/M% (Y/Y%)	Nov	<b>-0.4 (-0.5)</b>	0.5 (0.6)	0.9 (-0.5)	<b>- (-0.6)</b>
	 Manufacturing production M/M% (Y/Y%)	Nov	<b>-0.6 (-1.2)</b>	-	0.9 (0.1)	<b>1.1 (0.2)</b>
	 Trade balance €bn	Nov	<b>-9.2</b>	-7.2	-7.5	<b>-7.7</b>
UK	 Construction PMI	Dec	<b>54.3</b>	54.0	55.5	-

### Auctions

Country	Auction
- Nothing to report -	

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

Access our research blog at:

<https://www.uk.daiwacm.com/ficc-research/recent-blogs>

This research report is produced by Daiwa Securities Co. Ltd., and/or its affiliates and is distributed by Daiwa Capital Markets Europe Limited. Daiwa Capital Markets Europe Limited is authorised and regulated by The Financial Conduct Authority and is a member of the London Stock Exchange and Eurex Exchange. Daiwa Capital Markets Europe Limited and its affiliates may, from time to time, to the extent permitted by law, participate or invest in other financing transactions with the issuers of the securities referred to herein (the "Securities"), perform services for or solicit business from such issuers, and/or have a position or effect transactions in the Securities or options thereof and/or may have acted as an underwriter during the past twelve months for the issuer of such securities. In addition, employees of Daiwa Capital Markets Europe Limited and its affiliates may have positions and effect transactions in such securities or options and may serve as Directors of such issuers. Daiwa Capital Markets Europe Limited may, to the extent permitted by applicable UK law and other applicable law or regulation, effect transactions in the Securities before this material is published to recipients.

This publication is intended for investors who are MiFID 2 Professional (or equivalent) Clients and should not therefore be distributed to such Retail Clients. Should you enter into investment business with Daiwa Capital Markets Europe's affiliates outside the United Kingdom, we are obliged to advise that the protection afforded by the United Kingdom regulatory system may not apply; in particular, the benefits of the Financial Services Compensation Scheme may not be available.

Daiwa Capital Markets Europe Limited has in place organisational arrangements for the prevention and avoidance of conflicts of interest. Our conflict management policy is available at <http://www.uk.daiwacm.com/about-us/corporate-governance-regulatory>. Regulatory disclosures of investment banking relationships are available at <https://daiwa3.bluematrix.com/sellside/Disclosures.action>.

#### Explanatory Document of Unregistered Credit Ratings

This report may use credit ratings assigned by rating agencies that are not registered with Japan's Financial Services Agency pursuant to Article 66, Paragraph 27 of the Financial Instruments and Exchange Act. Please review the relevant disclaimer regarding credit ratings issued by such agencies at: <https://lzone.daiwa.co.jp/l-zone/disclaimer/creditratings.pdf>