

# Euro wrap-up

## Overview

- Bunds made large gains while Bank of France Governor Villeroy noted that while further tightening was likely, jumbo rate hikes will not become the norm.
- Gilts also rallied, even as UK inflation beat expectations jumping to its highest rate since 1982.
- Thursday brings euro area CPI and construction output figures, while attention in the UK will be on the long-awaited fiscal update.

Emily Nicol  
+44 20 7597 8331

### Daily bond market movements

Bond	Yield	Change
BKO 2.2 12/24	2.076	-0.070
OBL 1.3 10/27	1.954	-0.102
DBR 1.7 08/32	1.998	-0.103
UKT 1 04/24	2.938	-0.099
UKT 1½ 07/27	3.152	-0.125
UKT 4½ 06/32	3.131	-0.153

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

## UK

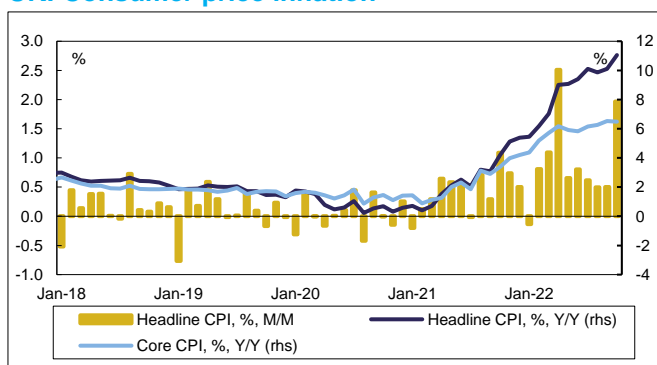
### UK inflation beats expectations as it jumps to the highest since 1982

UK inflation beat already high expectations in October, with prices jumping 2.0% M/M, the third strongest increase on the series dating back to 1988, to leave the annual rate up 1.0ppt to 11.1% Y/Y, a level last reached in 1982 and 0.2ppt higher than projected by the BoE at the start of the month. The principal cause of the rise was energy, which surged 14.6% M/M, due to the 27% increase in a “typical” household energy bill, which saw electricity prices rise almost 17% M/M and gas prices increase 37% M/M. So, despite a further moderation in petrol prices, for which the annual rate (22.2% Y/Y) eased to its lowest for a year and almost half the peak in July, annual energy inflation jumped 9.5ppts to a series-high 59.0% Y/Y, to account for a little more than two-thirds of the increase in the headline CPI rate. Food inflation also maintained a steady upwards trend, rising 1.7ppts to 16.5% Y/Y, the highest since September 1977, with notable increases in prices of margarine (42.1% Y/Y), and other dairy products (27.3% Y/Y). Admittedly, price pressures in core goods moderated last month, with non-energy industrial goods inflation down 0.3ppt to 6.7% Y/Y. In part, that reflected the first annual decline in second-hand car prices since March 2020 as well as an easing in furniture inflation – both components that had previously been pushed significantly higher by supply-chain strains. But this was offset by a further pickup in services inflation, by 0.1ppt to 6.3% Y/Y, with price increases in hotel stays at a series high (16.1% Y/Y). As such, core inflation moved sideways at an above-consensus 6.5% Y/Y. And the NIESR 10% trimmed mean measure rose 0.5ppt to a new series high of 8.8% Y/Y, suggesting a possible further broadening of price pressures.

### Core inflation likely to trend higher over the near term

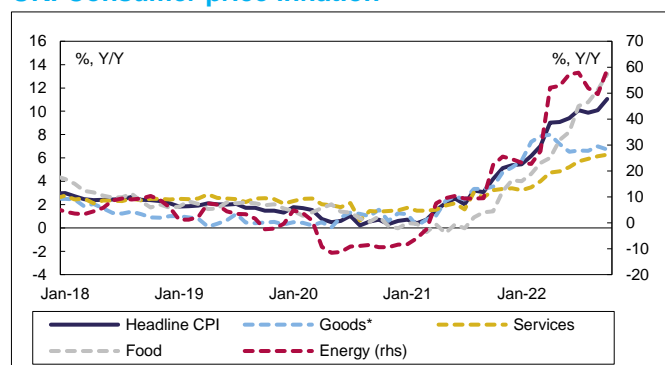
The near-term outlook for UK inflation remains highly uncertain, not least given the unknown profile for fiscal policy including the energy price guarantee from April next year, for which we should get somewhat greater clarity in tomorrow’s Autumn Statement. Even assuming a further uptick in household energy bills in April, however, energy inflation has likely peaked. And with producer goods inflation having seemingly also peaked – the input PPI measure fell for the fourth consecutive month in October to 19.2% Y/Y, with the output price measure down 1½ppt to 14.8% Y/Y – and global demand likely to weaken, consumer non-energy industrial goods inflation should maintain a modest downwards trend. Nevertheless, still significant cost pressures including strong pay growth, as well as the annual indexation to prices of certain sub-components, including mobile phone tariffs, at the start of the year, will continue to add upside pressures to services inflation over coming months. So, while the headline CPI rate might well have now reached its peak, core inflation is likely to rise marginally further over the remainder of the year, before gradually easing from the New Year. Indeed, we currently forecast headline inflation to still be above 5% at the end of 2023 and above the BoE’s 2% target through to the end of 2024. Taken together with [yesterday’s data](#), which confirmed the still-tight jobs market and the strongest regular wage growth outside of the height of

### UK: Consumer price inflation



Source: Refinitiv and Daiwa Capital Markets Europe Ltd.

### UK: Consumer price inflation



Source: Refinitiv and Daiwa Capital Markets Europe Ltd.

the pandemic since the series began in 2001, today's release reaffirms our expectation that the MPC will raise Bank Rate by a further 50bps to 3.50% in December, with additional tightening likely to come in Q1 too.

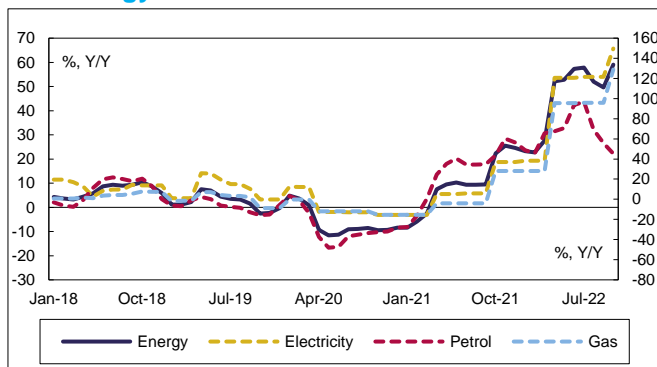
## House price growth slows sharply, but expect more to come

Contrasting with CPI inflation, today's ONS house price index confirmed a marked slowdown in growth in September, as higher mortgage rates took their toll. In particular, the average house price inflation slowed 3.6ppts to 9.5%Y/Y, to be more than 5½ppts below July's peak. Admittedly, this in part reflected base effects from the strength a year ago ahead of the conclusion of the government's temporary Stamp Duty discount. But compared with August, prices rose just 0.1%M/M, the softest pace for almost a year and down from average monthly growth of more than 1.0%M/M in the previous ten months. And while the government again reduced the Stamp Duty thresholds at the end of September, the blowout in interest rates in October – with the average 2Y fixed rate on a 75% LTV mortgage in October up 184bps on the month (and some 480bps higher than the trough in September 2021) to 6.01% – is bound to have stifled house price growth significantly further. Indeed, the RICS residential survey saw its headline house price balance fall into negative territory for the first time since June 2002. And while the decline in the Rightmove index of asking prices (-1.1%M/M) was in line with the pre-pandemic five-year average for November, the RICS survey suggested that price expectations for twelve months ahead was the weakest since 2010 while the Nationwide house price index fell in October by 0.9%M/M, the most since the first wave of Covid-19 in June 2020.

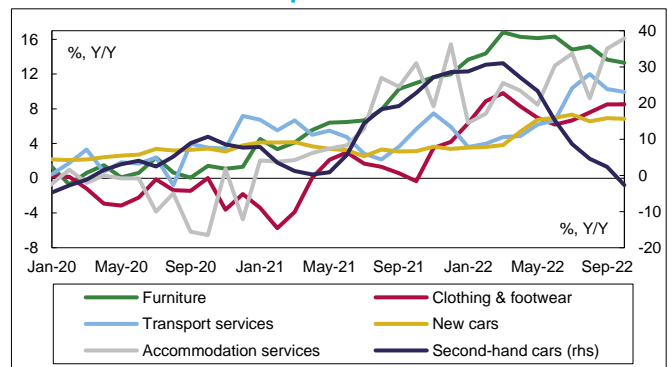
## The day ahead in the UK

Attention in the UK tomorrow will be on Chancellor Hunt's Autumn Statement and accompanying economic and fiscal forecasts from the OBR. This follows Hunt's decision last month to reverse the majority of the measures announced in Kwarteng's disastrous 'mini-budget' on 23 September. But while the Treasury estimated that the U-turn on many of Kwarteng's measures saved roughly £32bn in tax revenue that would otherwise have been foregone, and the forecast of debt interest payments will be lower than it would have been had the Statement been presented on 31 October as previously planned, reports suggest that the OBR will estimate that borrowing in 2025-27 will be around £70bn higher than previously estimated in March. As a result, expect a return to fiscal austerity with plans for sizeable spending cuts, while tax hikes will also be notable (including perhaps the lowering of the threshold for the 45p top rate of income tax from £150k to £125k) that might also be difficult for Conservative party backbench MPs to stomach. Given the implications for the inflation outlook and impact on monetary policy, the government's decision on the energy price cap from April will be of particular interest. Also important for the outlook for rates will be the extent to which cuts in public spending and tax increases will be back-loaded beyond the monetary policy horizon and indeed beyond the likely date of the next general election. Separately, BoE's Chief Economist Pill and external MPC member Tenreyro are also due to speak tomorrow.

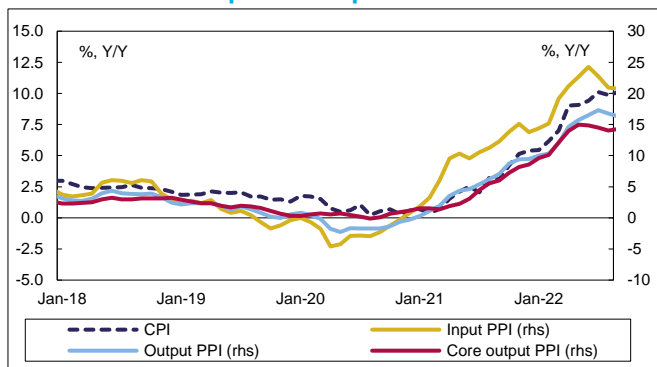
### UK: Energy inflation



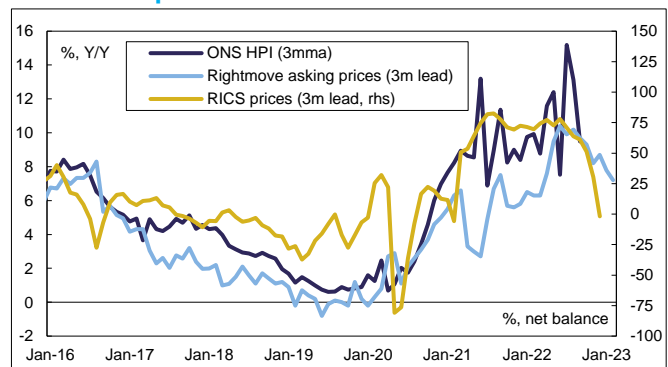
### UK: Selected CPI components



### UK: Consumer & producer price inflation



### UK: House price indicators



## Euro area

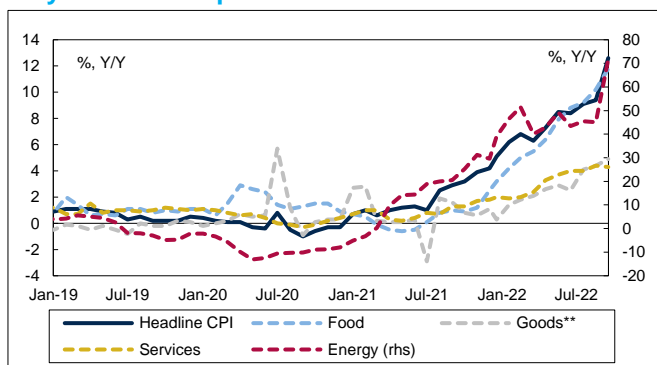
### Surge in Italian inflation confirmed despite slight downwards revision from flash estimate

Today's updated Italian CPI figures surprised on the downside, with the headline HICP rate revised down from the flash by 0.2ppt to 12.6%Y/Y. However, this was still 3.2ppts higher than in September, representing a marked surge due principally to higher energy and food prices. Admittedly, the downwards revision principally reflected a slight tweak in the energy component, although those prices were still up 26.9%M/M and 71.7%Y/Y, as household energy bills jumped 46.4%M/M to be up an exceptional 136.7%Y/Y. Food inflation was still up 1.6ppt to 11.8%Y/Y despite a similar marginal easing from the flash estimate. But non-energy industrial goods inflation was pushed slightly higher to 4.9%Y/Y from 4.4%Y/Y in September. So, while services inflation edged lower in October, by 0.1ppt to 4.3%Y/Y, core HICP inflation rose 0.2ppt to 4.6%Y/Y, 0.1ppt stronger than initially estimated. While the equivalent figures were unchanged from the preliminary figures in Germany (up 0.7ppt to 11.6%Y/Y), France (up 0.9ppt to 7.1%Y/Y) and Spain (down 1.7ppts to 7.3%Y/Y), today's release raises the likelihood that euro area headline HICP inflation in October will be nudged lower when the final data are published tomorrow. Indeed, to two decimal places, the flash aggregate HICP estimate stood at 10.66%Y/Y in October. However, core inflation is likely to be unrevised at the record high of 5.0%Y/Y.

### The day ahead in the euro area

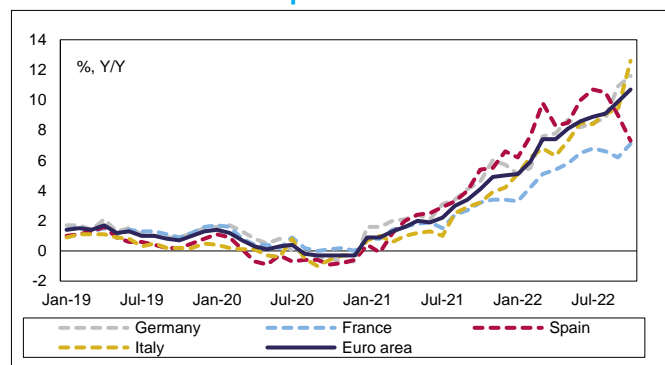
Tomorrow will bring the aforementioned updated estimate of euro area HICP inflation in October, including a detailed component breakdown, as well as additional measures of underlying price pressures comprising the ECB's trimmed mean figures. The flash release saw headline inflation jump 0.8ppt to a record high of 10.7%Y/Y, although risks to this are to the downside, with the core rate up 0.2ppt to 4.8%Y/Y. Meanwhile, euro area construction output numbers are set to confirm contraction last quarter, while euro area new car registration figures for October are also due.

#### Italy: Consumer price inflation\*



\*HICP measure. \*\*Non-energy industrial goods. Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

#### Euro area: Consumer price inflation\*










\*HICP measure. Source: Bloomberg 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
Italy	 Final CPI M/M% (Y/Y%)	Oct	<b>3.4 (11.8)</b>	<u>3.5 (11.9)</u>	0.3 (8.9)	-
	 Final HICP M/M% (Y/Y%)	Oct	<b>3.8 (12.6)</b>	<u>4.0 (12.8)</u>	1.6 (9.4)	-
UK	 CPI M/M% (Y/Y%)	Oct	<b>2.0 (11.1)</b>	<u>1.8 (10.8)</u>	0.5 (10.1)	-
	 Core CPI Y/Y%	Oct	<b>6.5</b>	<u>6.5</u>	6.5	-
	 PPI output prices M/M% (Y/Y%)	Oct	<b>0.3 (14.8)</b>	0.5 (14.6)	0.2 (15.9)	<b>0.3 (16.3)</b>
	 PPI input prices M/M% (Y/Y%)	Oct	<b>0.6 (19.2)</b>	0.3 (18.1)	0.4 (20.0)	<b>0.9 (20.8)</b>
	 House price index Y/Y%	Sep	<b>9.5</b>	-	13.6	<b>13.1</b>



#### Auctions

Country	Auction
Germany 	sold €1.28bn of 1% 2038 bonds at an average yield of 2.26%





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 	07.00	EU27 new car registrations Y/Y%	Oct	-	9.6
	10.00	Final HICP M/M% (Y/Y%)	Oct	<u>1.5 (10.6)</u>	1.2 (9.9)
	10.00	Final core HICP Y/Y%	Oct	<u>5.0</u>	4.8
	10.00	Construction output M/M% (Y/Y%)	Sep	-	-0.6 (2.3)
Italy 	09.00	Trade balance €bn	Sep	-	-9.6

#### Auctions and events

Euro area 	15.00	ECB's Villeroy scheduled to speak
France 	09.50	Auction: 0.75% Feb-2028 bonds
	09.50	Auction: 0.75% Nov-2028 bonds
	09.50	Auction: 0.50% 2029 bonds
	10.50	Auction: 0.10% 2031 index-linked bonds
	10.50	Auction: 3.15% 2032 index-linked bonds
Spain 	10.50	Auction: 0.10% 2047 index-linked bonds
	09.30	Auction: 0.00% 2025 bonds
	09.30	Auction: 0.70% 2032 bonds
UK 	09.30	Auction: 5.15% 2044 bonds
	11.30	Chancellor Hunt to deliver Autumn Statement with OBR forecast
	12.30	BoE Chief Economist Pill scheduled to speak
	14.30	BoE MPC member Tenreyro scheduled to speak

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/Dislosures.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>

#### **IMPORTANT**

This report is provided as a reference for making investment decisions and is not intended to be a solicitation for investment. Investment decisions should be made at your own discretion and risk. Content herein is based on information available at the time the report was prepared and may be amended or otherwise changed in the future without notice. We make no representations as to the accuracy or completeness. Opinions [and/or estimates] reflect a judgment as at the date of publication and are subject to change without notice. Daiwa Capital Markets Europe Limited retains all rights related to the content of this report, which may not be redistributed or otherwise transmitted without prior consent.