

# Euro wrap-up

## Overview

- As several ECB Governing Council members echoed yesterday's hawkish signal from Christine Lagarde, euro area government bonds made further losses even as the flash PMIs suggested a moderation of cost pressures.
- While UK retail sales fell in November, Gilts more than reversed yesterday's gains as the flash PMIs pointed to an easing in the economic downturn in December.
- The coming week will bring more economic sentiment survey results from the euro area, Germany, France and the UK, as well as new data on euro area labour costs, German PPI inflation and the UK current account deficit.

**Chris Scicluna**  
+44 20 7597 8326

**Emily Nicol**  
+44 20 7597 8331

### Daily bond market movements

Bond	Yield	Change
BKO 2.2 12/24	2.419	+0.084
OBL 1.3 10/27	2.226	+0.082
DBR 1.7 08/32	2.162	+0.090
UKT 1 04/24	3.505	+0.108
UKT 1½ 07/27	3.332	+0.112
UKT 4¼ 06/32	3.357	+0.114

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

## Euro area

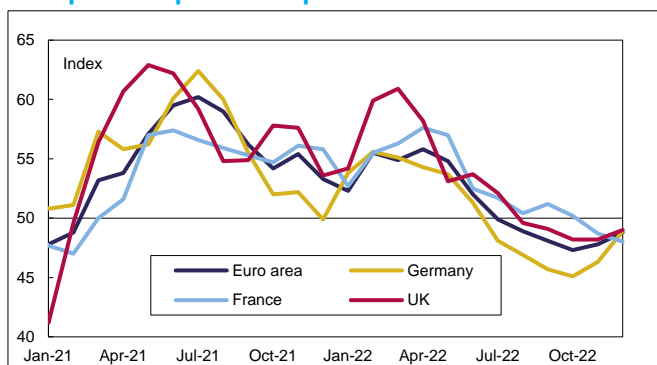
### Flash PMIs suggest moderation in economic downturn and easing of price pressures

The flash December PMIs for the euro area were relatively encouraging, suggesting that the current downturn in economic activity need not be marked and also that price pressures appear to be moderating on improved supply conditions. In particular, while it continued to point to recession, the euro area composite output PMI rose 1pt to a four-month high of 48.8. The surveys for both manufacturing and services were less downbeat than of late, with the output index for the former up almost 2pts to a six-month high, and the activity index for the latter up a little more than ½pt to a four-month high. New orders fell at a slightly softer pace in both major sectors too. Overall input cost growth moderated to the softest pace since May 2021 (the respective composite PMI dropped more than 3pts to 68.4), while output price growth slowed to a 12-month low (down 1.4pts to 61.3). The moderation in inflationary pressures appears at least in part to reflect improved supply conditions. Most notably, delivery times in manufacturing improved for the first time since January 2020 ahead of the pandemic. So, overall expectations with respect to the outlook for activity over the coming twelve months picked up, albeit remaining well below the long-run average.

### Improvement in German survey contrasts deterioration in French PMIs

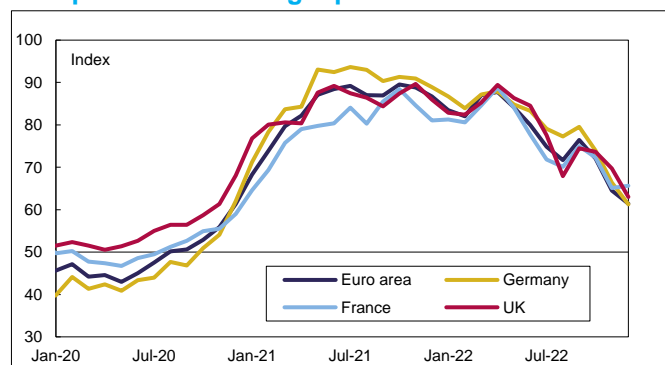
At the country level, the improvement in the flash PMIs was led by the German survey, which suggested a welcome stabilisation in economic conditions towards year-end. In particular, Germany's composite output PMI rose 2.6pts to a six-month high of 48.9, with the services activity index up to the best in five months (49.0) and the manufacturing output index up to the best in six months (48.7). Overall, the survey suggests that a relatively shallow recession is underway in Germany. In contrast to the improved German indices, however, the French survey fell short of expectations. Most notably, the French services activity PMI fell for a third consecutive month in December, to 48.1, the lowest since February 2021. So, while the manufacturing output index (47.7) signalled a slightly softer pace of decline, the French composite output PMI fell 0.7pt to 48.0, similarly the weakest since early 2021 and consistent with contraction. We note, however, that the PMIs typically provide a less accurate guide to French economic activity than other survey indicators such as yesterday's [INSEE](#) indices, which were reassuringly stable. Beyond the two largest member states, S&P Global suggested that the PMIs pointed to a fourth successive drop in economic output in the rest of the euro area, albeit with the pace of decline the slowest of the run. At the sectoral level, perhaps unsurprisingly, S&P Global reported that the steepest downturns continue to be registered in energy-intensive sectors such as chemicals and plastics. Perhaps related to that, it also noted a marked fall in transportation. But there was reportedly also a welcome improvement in consumer-facing firms, including in tourism and recreation and, to a lesser extent, producers of household goods.

### Europe: Composite output PMIs



Source: S&P Global, Refinitiv and Daiwa Capital Markets Europe Ltd.

### Europe: Manufacturing input cost PMIs



Source: S&P Global, Refinitiv and Daiwa Capital Markets Europe Ltd.

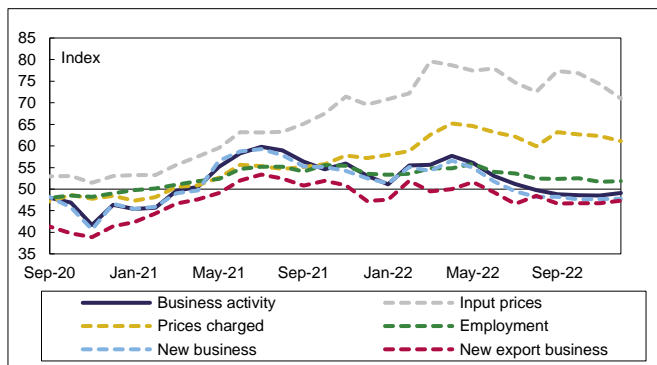
## Despite a modest revision, headline CPI fell in November with underlying pressures easing too

After [ECB President Lagarde](#) yesterday struck a particularly hawkish tone in response to the significant upwards revisions to the Eurosystem's near-term inflation projections, today's final euro area consumer price inflation figures confirmed that the headline HICP rate fell back in November. Admittedly, there was a modest upwards revision from the flash estimate, by 0.1ppt to 10.1%Y/Y. Nevertheless, that left it still 0.5ppt below October's record high. As in the preliminary release, the moderation in part reflected lower energy prices, with the annual inflation rate down 6.6ppts to 34.9%Y/Y, reflecting a sizeable decline in prices of household liquid fuels (-6.9%M/M) and more modest falls in prices of electricity, gas and petrol. Prices of unprocessed food also fell back from recent highs, to leave the respective annual rate down 1.7ppts to 13.8%Y/Y. However, given pressures in the processed food component, total food inflation rose a further 0.5ppt to a new series high of 16.4%Y/Y. Among the core items, a moderation in clothing inflation was offset by higher prices of household furnishing and appliances, to leave non-energy industrial goods inflation unchanged at a series high 6.1%Y/Y. And while restaurant inflation maintained a steady upwards trend, marked falls in the package holidays and accommodation components saw services inflation edge 0.1ppt lower to 4.2%Y/Y. While this left euro area core inflation steady at the series high of 5.0%Y/Y, there were signs that underlying price pressures might well have reached a turning point. Certainly, both the 10% and 15% trimmed mean CPI estimates fell in November, by 0.3ppt to 8.5%Y/Y and 0.1ppt to 7.7%Y/Y respectively. And with producers' input cost burdens continuing to ease – as suggested by today's flash PMIs – and demand slowing, we expect consumer goods inflation to gradually retreat over coming quarters too.

## The week ahead and festive period in the euro area

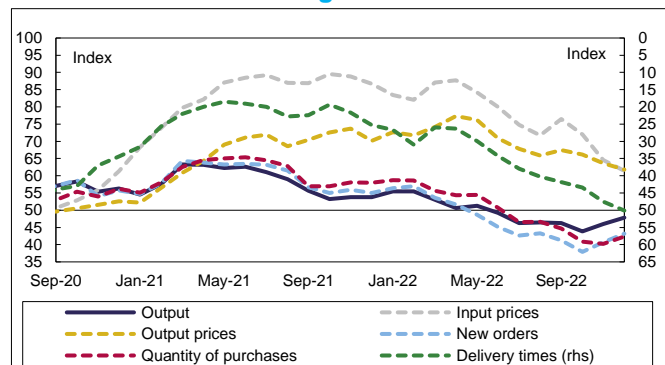
Ahead of the festive period, the coming week brings further updates on euro area economic conditions in December, with the German ifo business climate survey on Monday and the European Commission's flash consumer confidence index on Tuesday. In terms of the inflation outlook, of note will be euro area labour costs figures for Q3 (Monday), as well as German PPI data for November (Tuesday). After a quiet festive period for top-tier euro area data, the first week of the New Year will bring several releases of note, concluding with euro area flash December CPI inflation (6 January). With energy inflation likely to have fallen further, we expect the headline CPI rate to ease slightly by 0.1ppt to 10.0%Y/Y. However, core inflation might well temporarily rise to a new high due to firmer non-energy industrial goods and services inflation. Euro area PPI figures for November will be published on Thursday 5 January, followed by the European Commission's economic surveys, which will provide an update on business and consumer price expectations in December. Meanwhile, retail sales figures for November will likely reveal that the ongoing squeeze on households' finances weighed further on spending in the middle of Q4. Other releases of note due early in the New Year include German trade data and factory orders for November on 5 and 6 January respectively.

### Euro area: Services PMIs



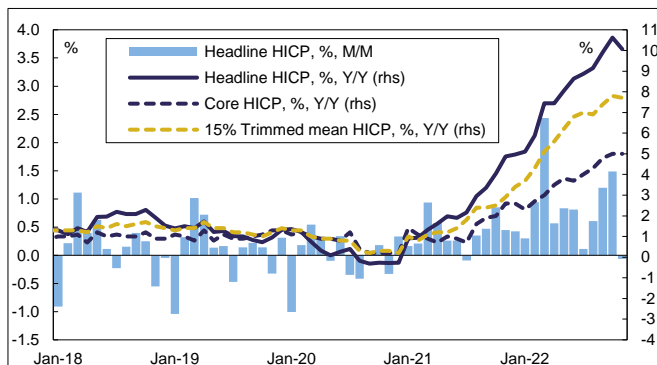
Source: S&P Global, Refinitiv and Daiwa Capital Markets Europe Ltd.

### Euro area: Manufacturing PMIs



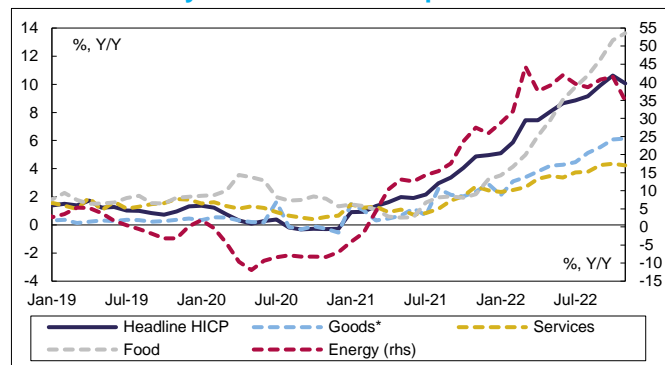
Source: S&P Global, Refinitiv and Daiwa Capital Markets Europe Ltd.

### Euro area: CPI inflation



Source: Refinitiv and Daiwa Capital Markets Europe Ltd.

### Euro area: Key CPI inflation components



\*Non-energy industrial goods.

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

## UK

### Retail sales volumes firmly on track for big drop in Q4

Contrary to the expected rise, UK retail sales volumes fell 0.4%M/M in November with no obvious support from Black Friday promotions. Growth in October was revised up by 0.3ppt to 0.9%M/M, suggesting that the rebound following the holiday for the Queen's funeral was a touch stronger than previously thought. But sales volumes were still down 2.2%3M/3M, the most on that basis in more than a year. And the average level in the first two months of Q4 was 0.9% below the Q3 average, strongly suggesting that retail sales will fall in Q4 for the sixth successive quarter. Indeed, sales volumes in November were down a steep 5.9%Y/Y to a level almost 9½% below the pandemic peak in April last year and 0.7% below the pre-pandemic level in February 2020. And December's sales volumes seem highly likely to have fallen by much more than in November due to the past week's disruption from snow and rail strikes. So, we now expect retail sales to drop 1½%Q/Q or more this quarter.

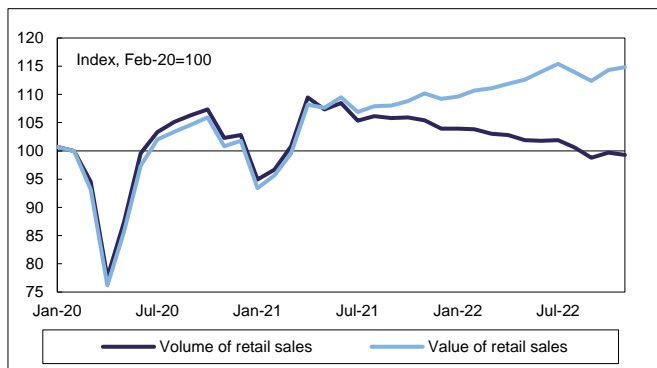
### Value of retail sales up again due to higher prices

Within the detail of the November figures, the volume of sales of auto fuel fell 1.8%M/M, but excluding them sales volumes were still down 0.3%M/M. Sales from clothes and textile stores were up for a third successive month to be trending almost 3% above the Q3 level, with consumers seemingly spending more as those retailers eschewed their usual November price hikes. In contrast, while food sales volumes were up 0.9%M/M, they were trending firmly below the Q3 average, as were sales at household goods stores, a strong reflection of high rates of inflation in those sub-sectors. Indeed, given price increases, the total value of retail sales was up 0.7%M/M in November to be up 3.6%Y/Y and 14.1% above the pre-pandemic level in February 2020.

### Consumer confidence up to five-month high but still below lockdown and GFC lows

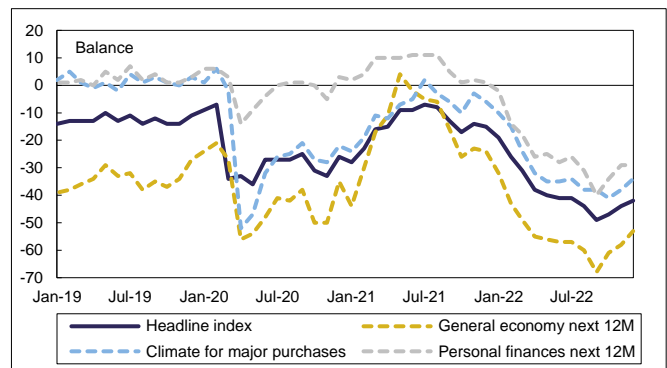
The weakness in retail sales is hardly a surprise given the severe drop in per capita real household disposable income, estimated by the OBR to decline 4.3% in the current fiscal year, the largest fall since records began more than six decades ago. So, consumer confidence has been at a historically low level too. Nevertheless, according to today's GfK survey, consumer confidence managed to rise for the third successive month in December to a five-month high. That, however, still left confidence below the worst levels recorded during the pandemic lockdowns and the global financial crisis. But the climate for making major purchases was judged to be the least bad since March, as were expectations for the economic outlook over the coming twelve months, perhaps benefiting from the decline mortgage rates from the highs reached in the

#### UK: Retail sales



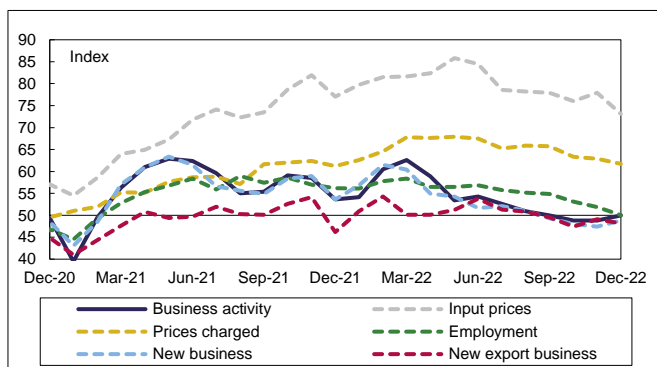
Source: Refinitiv and Daiwa Capital Markets Europe Ltd.

#### UK: Consumer confidence



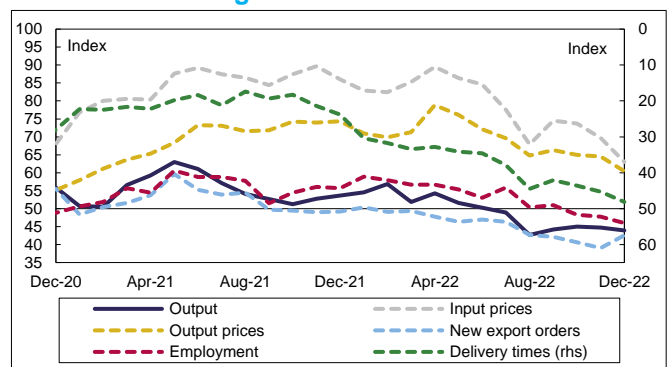
Source: GfK, Refinitiv and Daiwa Capital Markets Europe Ltd.

#### UK: Services PMIs



Source: S&P Global, Refinitiv and Daiwa Capital Markets Europe Ltd.

#### UK: Manufacturing PMIs



Source: S&P Global, Refinitiv and Daiwa Capital Markets Europe Ltd.

aftermath of the autumn Truss gilt-market crisis. We note, however, that real disposable incomes are set to decline sharply again in FY23/4, probably more than 2½%Y/Y, and so we expect retail sales and overall consumer spending to continue to decline next year too.

### Flash PMIs consistent with contraction despite some stabilisation in December

At face value, like the equivalent euro area indices, today's flash UK PMIs for December also suggested some stabilisation heading towards year end, with the composite PMI rising 0.8pt to 49.0. But this left the Q4 average almost 2pts below the Q3 level and consistent with ongoing contraction. And while there was a more marked improvement in the services sector, the activity index (up 1.2pts to 50.0) was merely implying stagnation, while the new business component recorded the fourth consecutive sub-50 reading. Moreover, having been conducted between 6-14 December, this survey will certainly not fully reflect the disruption from the past week's snow and rail strikes, with hospitality set to have been particularly severely impacted at what is typically one of its busiest periods. Meanwhile, manufacturing conditions remained tough with the output PMI down 0.8pt to a four-month low of 43.9, with demand matching the weakest level since the start of the pandemic. So, firms in the sector cut their purchases of inputs by the most in more than 2½ years, and continued to cut staff for a third consecutive month. Services firms were also reluctant to add to their headcount, with suggestions that companies were choosing not to replace voluntary leavers due to economic uncertainties. Today's report was not all doom and gloom, however, with a further marked easing in cost burdens reported this month, with the manufacturing input price PMI falling to its lowest in more than two years and the respective services index at a sixteen-month low. And so, while the composite output price PMI remained at an elevated level, it too fell to its lowest since August 2021, further supporting the [BoE's](#) decision yesterday to slow the pace of tightening and its assessment that inflation has probably peaked this quarter.










### The week ahead and festive period in the UK

It should be a relatively quiet festive period for UK economic top-tier data, with December sentiment indicators likely of most note. The start of the coming week will bring the latest CBI industrial trends and distributive trades surveys (Monday and Wednesday respectively), which are likely to flag ongoing weakness in manufacturing and retail as demand wanes due to the cost of living crisis. Likewise, the final December PMIs – for manufacturing and services, due 3 and 5 January respectively – seem likely to report a more downbeat assessment than suggested by today's flash estimates due to the disruption caused by ongoing rail strikes and snow, while the construction PMIs (due 6 January) might also slip below the key 50 expansion/contraction level for the first time in four months. But, with supply bottlenecks having eased, we might well see improvements in the autos sector, with November car production numbers (23 December) and December car registrations (7 January) expected to trend higher. The coming week will also bring updated estimates of Q3 GDP, alongside balance of payments data (22 December).

*The next edition of the Euro wrap-up will be published on 3 January 2023*



## Daiwa economic forecasts


















	2022			2023			2022	2023	2024
	Q2	Q3	Q4	Q1	Q2	Q3			
<b>GDP</b>	<b>%, Q/Q</b>						<b>%, Y/Y</b>		
Euro area 	0.8	0.3	-0.3	-0.3	-0.1	0.1	3.3	-0.1	0.8
UK 	0.2	-0.2	-0.3	-0.3	-0.5	-0.3	4.4	-1.1	0.1
<b>Inflation, %, Y/Y</b>									
Euro area									
Headline HICP 	8.0	9.3	10.2	8.9	7.0	5.3	8.4	6.0	1.9
Core HICP 	3.7	4.4	5.1	4.9	4.1	3.2	3.9	3.6	1.9
UK									
Headline CPI 	9.2	10.0	10.8	9.9	8.0	6.8	9.1	7.4	3.2
Core CPI 	6.0	6.3	6.3	5.8	4.6	3.9	5.9	4.5	3.0
<b>Monetary policy, %</b>									
ECB									
Refi Rate 	0.00	1.25	2.50	3.50	3.50	3.50	2.50	3.50	3.00
Deposit Rate 	-0.50	0.75	2.00	3.00	3.00	3.00	2.00	3.00	2.50
BoE									
Bank Rate 	1.25	2.25	3.50	4.25	4.25	4.25	3.50	4.25	3.25

Source: Bloomberg, ECB, BoE and Daiwa Capital Markets Europe Ltd.


## European calendar

### Today's results

#### Economic data










































Country	Release	Period	Actual	Market consensus/ Daiwa forecast	Previous	Revised
Euro area 	Preliminary manufacturing (services) PMI	Dec	<b>47.8 (49.1)</b>	47.1 (48.5)	47.1 (48.5)	-
	Preliminary composite PMI	Dec	<b>48.8</b>	47.9	47.8	-
	Final HICP M/M% (Y/Y%)	Nov	<b>-0.1 (10.1)</b>	-0.1 (10.0)	1.5 (10.6)	-
	Final core CPI Y/Y%	Nov	<b>5.0</b>	5.0	5.0	-
	Trade balance €bn	Oct	<b>-28.3</b>	-	-37.7	<b>-36.4</b>
Germany 	Preliminary manufacturing (services) PMI	Dec	<b>47.4 (49.0)</b>	46.3 (46.3)	46.2 (46.1)	-
	Preliminary composite PMI	Dec	<b>48.9</b>	46.5	46.3	-
France 	Preliminary manufacturing (services) PMI	Dec	<b>48.9 (48.1)</b>	48.0 (49.0)	48.3 (49.3)	-
	Preliminary composite PMI	Dec	<b>48.0</b>	48.7	48.7	-
Italy 	Final CPI M/M% (Y/Y%)	Nov	<b>0.5 (11.8)</b>	0.5 (11.8)	3.4 (11.8)	-
	Final HICP M/M% (Y/Y%)	Nov	<b>0.7 (12.6)</b>	0.6 (12.5)	3.8 (12.6)	-
Spain 	Labour costs Y/Y%	Q3	<b>4.0</b>	-	3.8	-
UK 	GfK consumer confidence	Dec	<b>-42</b>	-43	-44	-
	Retail sales including auto fuel M/M% (Y/Y%)	Nov	<b>-0.4 (-5.9)</b>	0.3 (-5.6)	0.6 (-6.1)	<b>0.9 (-5.9)</b>
	Retail sales excluding auto fuel M/M% (Y/Y%)	Nov	<b>-0.3 (-5.9)</b>	0.3 (-5.8)	0.3 (-6.7)	<b>0.7 (-6.4)</b>
	Preliminary manufacturing (services) PMI	Dec	<b>44.7 (50.0)</b>	46.5 (48.5)	46.5 (48.8)	-
	Preliminary composite PMI	Dec	<b>49.0</b>	48.0	48.2	-


#### Auctions

Country	Auction
UK 	BoE sold £3.10bn gilts in sale of financial stability portfolio holdings

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

## Key data releases – December/January 2023

19	20	21	22	23
<b>EURO AREA</b>  LABOUR COSTS (Q3) CONSTRUCTION OUTPUT (OCT)  <b>GERMANY</b>  IFO BUSINESS CLIMATE SURVEY (DEC)  <b>UK</b>  CBI INDUSTRIAL TRENDS SURVEY (DEC)	<b>EURO AREA</b>  EC CONSUMER CONFIDENCE (DEC P)  <b>GERMANY</b>  PPI (NOV)	<b>GERMANY</b>  GFK CONSUMER CONFIDENCE (JAN)  <b>UK</b>  LLOYDS BUSINESS BAROMETER (DEC) CBI DISTRIBUTIVE TRADES SURVEY (DEC) PUBLIC FINANCES (NOV)	<b>FRANCE</b>  RETAIL SALES (NOV)  <b>ITALY</b>  PPI (NOV)  <b>UK</b>  GDP (Q3 F) CURRENT ACCOUNT (Q3)	<b>FRANCE</b>  PPI (NOV)  <b>ITALY</b>  ECONOMIC, CONSUMER & BUSINESS CONFIDENCE (DEC)  <b>SPAIN</b>  GDP (Q3 F)  <b>UK</b>  NEW CAR MANUFACTURING (DEC)
	<b>GERMANY</b>  RETAIL SALES* (NOV)	<b>UK</b>  NATIONWIDE HOUSE PRICES* (DEC)	<b>EURO AREA</b>  M3 MONEY SUPPLY (NOV)  <b>SPAIN</b>  RETAIL SALES (NOV)  ECB PUBLISHES ECONOMIC BULLETIN	<b>SPAIN</b>  CPI (DEC P)
<b>EURO AREA</b>  MANUFACTURING PMI (DEC F)  <b>GERMANY</b>  MANUFACTURING PMI (DEC F)  <b>FRANCE</b>  MANUFACTURING PMI (DEC F) NEW CAR REGISTRATIONS* (DEC)  <b>ITALY</b>  MANUFACTURING PMI (DEC) NEW CAR REGISTRATIONS (DEC)  <b>SPAIN</b>  MANUFACTURING PMI (DEC) UNEMPLOYMENT (DEC) NEW CAR REGISTRATIONS* (DEC)	<b>GERMANY</b>  CPI (DEC P) UNEMPLOYMENT (DEC)  <b>UK</b>  MANUFACTURING PMI (DEC F)	<b>EURO AREA</b>  SERVICES & COMPOSITE PMIS (DEC F)  <b>GERMANY</b>  SERVICES & COMPOSITE PMIS (DEC F) NEW CAR REGISTRATIONS & PRODUCTION* (DEC)  <b>FRANCE</b>  CPI (DEC P) CONSUMER CONFIDENCE (DEC) SERVICES & COMPOSITE PMIS (DEC F)  <b>ITALY</b>  SERVICES & COMPOSITE PMIS (DEC)  <b>SPAIN</b>  SERVICES & COMPOSITE PMIS (DEC)  <b>UK</b>  BRC SHOP PRICE INDEX (DEC) BANK LENDING (NOV)	<b>EURO AREA</b>  PPI (NOV) CONSTRUCTION PMI (DEC)  <b>GERMANY</b>  TRADE BALANCE (NOV) CONSTRUCTION PMI (DEC)  <b>FRANCE</b>  CONSTRUCTION PMI (DEC)  <b>ITALY</b>  CPI (DEC P) CONSTRUCTION PMI (DEC)  <b>UK</b>  NEW CAR REGISTRATIONS (DEC) SERVICES & COMPOSITE PMIS (DEC F)	<b>EURO AREA</b>  CPI (DEC P) RETAIL SALES (NOV)  EC ECONOMIC CONFIDENCE SURVEYS (DEC)  <b>GERMANY</b>  FACTORY ORDERS (NOV)  <b>FRANCE</b>  CONSUMER SPENDING (NOV)  <b>UK</b>  CONSTRUCTION PMI (DEC)

 UK public holiday. \*Approximate date of release. 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.