

# Euro wrap-up

## Overview

- Euro area government bonds rallied as French inflation surprised on the downside and German import prices fell by a record amount.
- Gilts also made sizeable gains as UK mortgage approvals slumped and a survey suggested that shop price inflation edged lower.
- Thursday will bring flash Italian inflation for December, as well as euro area construction and final UK services PMIs.

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### Daily bond market movements

Bond	Yield	Change
BKO 2.2 12/24	2.567	-0.084
OBL 1.3 10/27	2.292	-0.114
DBR 1.7 08/32	2.272	-0.108
UKT 1 04/24	3.468	-0.138
UKT 1¼ 07/27	3.495	-0.127
UKT 4¼ 06/32	3.500	-0.152

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

## Euro area

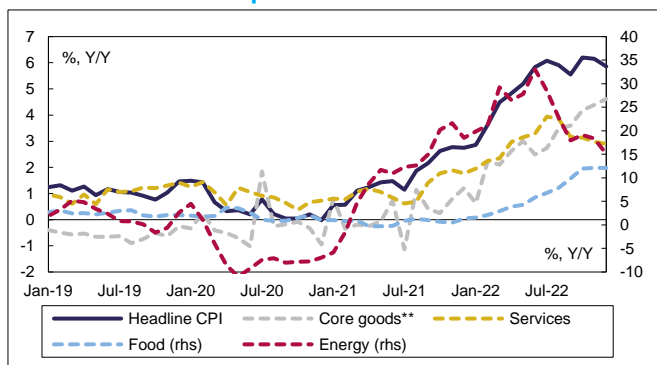
### Flash French inflation surprises to the downside as energy inflation drops to a 15-month low

Coming on the back of downward surprises in the flash estimates of German and Spanish CPI inflation in December, today's French figures were similarly better than expected. In particular, consumer prices fell 0.1%M/M, to leave the EU-harmonised HICP rate of inflation down 0.4ppt to 6.7%Y/Y, a three-month low, having been expected to rise by 0.2ppt. The national CPI measure of inflation also eased 0.3ppt to 5.9%Y/Y. Like in Germany and Spain, the downwards shift in France reflected a drop in energy prices (-3.6%M/M) to push the respective annual rate down 3.3ppts to 15.1%Y/Y, the lowest since September 2021. Services inflation also edged slightly lower in December, by 0.1ppt to 2.9%Y/Y, offsetting a further modest uptick in manufactured goods inflation, by 0.2ppt to 4.6%Y/Y, a new series high. Overall, today's release confirms that the euro area inflation estimate for December (due Friday) will fall sharply. Indeed, taken together with the declines recorded in other euro area member states (including Portugal where the HICP rate fell 0.4ppt to 9.8%Y/Y, and Belgium where the CPI rate eased 0.3ppt to 10.3%Y/Y), and even assuming no improvement in Italy (in line with the current Bloomberg survey median forecast), we would expect to see headline euro area inflation moderate by at least 0.8ppt to 9.3%Y/Y. Risks to that forecast are skewed to the downside. Core inflation, however, seems likely to have remained sticky in December, with risks of a possible uptick above 5.0%Y/Y.

### German import prices fall by record amount in November

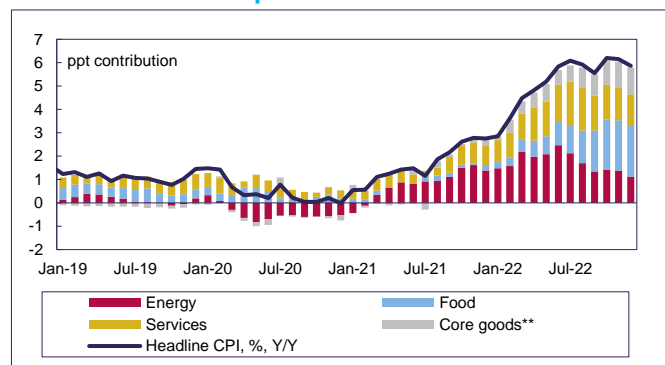
Following yesterday's downside surprise in German consumer price inflation, today's German import price data also fell significantly short of expectations. Indeed, German import prices fell for a third successive month in November and by a record 4.5%M/M, almost three times the expected drop. Given base effects, the annual rate of import price inflation declined 9ppts to 14.5%Y/Y, still very high but more than 18ppts below the peak in August. Perhaps unsurprisingly, lower prices of imported energy (down more than 16%M/M) accounted for much of the drop in prices in November. However, even excluding such items, import prices fell for the first time since June, dropping 0.7%M/M after being unchanged in October. Prices of consumer, capital and basic goods alike fell in November to add to evidence of an easing of cost pressures in the manufacturing sector. Indeed, excluding energy, import price inflation slowed almost 2ppts to 9.7%Y/Y, having been up more than 15%Y/Y in June. Of course, the ECB will worry that inflation of services might remain under upwards pressure due to higher labour costs and/or a desire among firms to rebuild margins even as goods inflation shifts into reverse.

### France: Consumer price inflation\*



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

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## Services PMIs also point to softer inflationary pressures despite a less severe downturn in activity

The final services PMI surveys were, however, broadly encouraging with respect to the near-term inflation outlook in the sector. Indeed, they also suggested a further easing in services input cost burdens at the end of last year to the lowest in eleven months. And the increase in prices charged also eased to a four-month low, amid an ongoing decline in demand in the sector. Nevertheless, today's final PMIs also provided an upwards surprise to the activity component, which is now estimated to have risen 1.3pts in December to 49.8, a four-month high and broadly consistent with stagnation in the sector. And while still firmly in contractionary territory, the new business component (48.4) rose to its highest since June. The increase in the euro area's aggregate output PMI was driven by Germany, with the respective index jumping more than 3pts in December to 49.2, albeit still the weakest of the member states. Indeed, the PMIs implied a marginal pace of contraction in the services sector in France (49.5), stagnation in Italy (49.9) and modest growth in Spain (51.6). Of course, given the weakness in the manufacturing sector, the composite PMIs for the larger member states remained below 50. But with the aggregate euro area index having been revised higher from the flash release to 49.3, to be up 1½pts on the month and its highest reading since July, today's survey further suggests that the current downturn in economic activity in the region might not be as severe as initially feared.

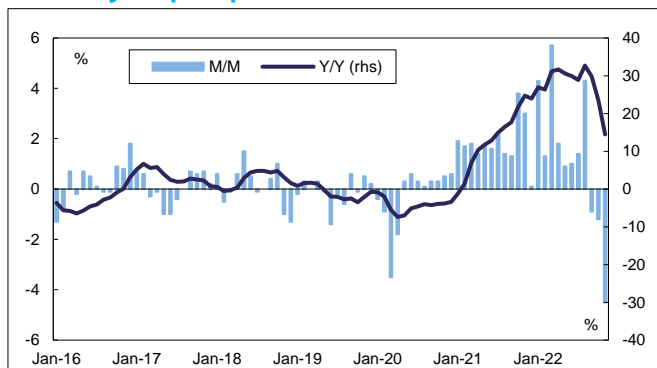
## French consumer confidence bucks the trend at the of last year

Contrasting with the improvement in other sentiment surveys, as well as the Commission's flash euro area consumer confidence indicator, the French INSEE consumer confidence survey reported a modest drop in headline sentiment in December. Indeed, the indicator fell 1pt to 82, above the lows seen during the summer (79) but nevertheless still well below levels recorded at the start of the year (99). With households more downbeat about their financial situation, the share of households considering it a good time to make major purchases fell again in December, to the lowest since the start of the pandemic, suggesting that household consumption will remain subdued for the time being.

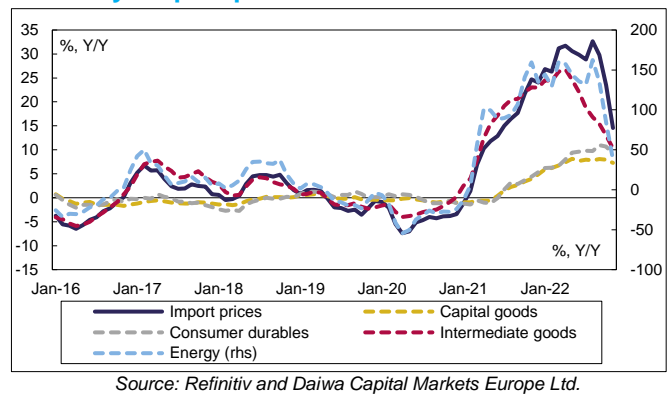
## The day ahead in the euro area

Ahead of Friday's euro area inflation estimate, the main focus tomorrow will be the flash Italian consumer price figures for December. While the Bloomberg survey consensus is for HICP inflation to move sideways at 12.6%Y/Y, the figures from other member states suggest that the risks to this forecast are skewed to the downside. In addition, tomorrow brings the release of the euro area construction PMIs for December, which are expected to suggest that activity in the sector continued to contract at the end of the year. The latest German goods trade numbers for November are also due for release.

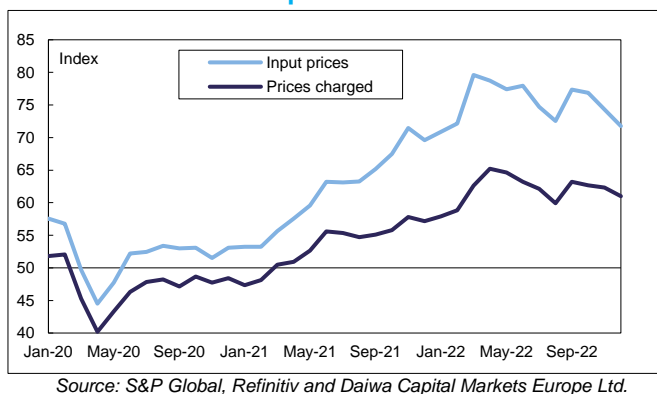
### Germany: Import price inflation



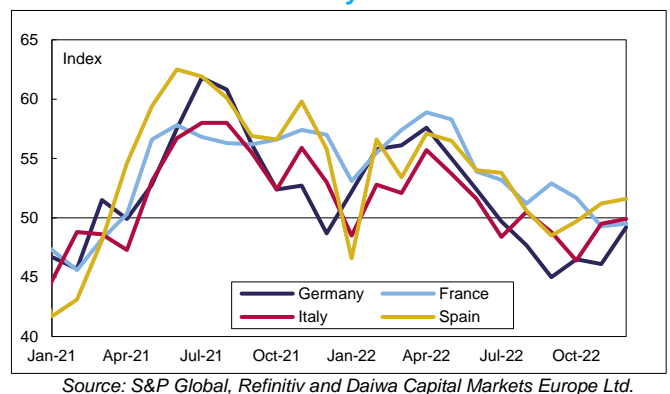
### Germany: Import price inflation



### Euro area: Services input cost PMIs



### Euro area: Services activity PMIs



## UK

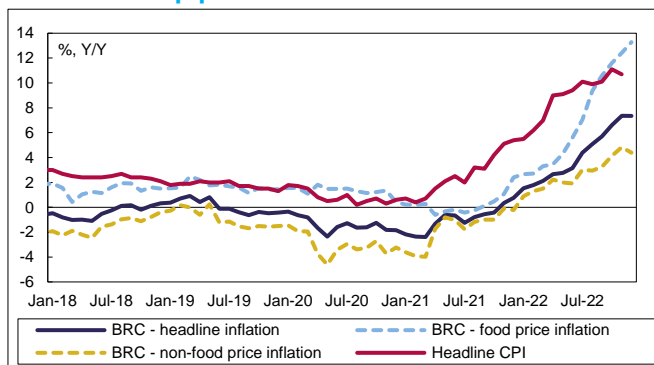
### UK shop price inflation slows slightly in December as non-food prices fail to rise

According to the BRC survey, UK shop price inflation slowed slightly in December, dropping 0.1ppt from November's high to 7.3%Y/Y. That was despite further pressure in food prices, which rose 1.1%M/M to be up 13.3%Y/Y. In contrast, non-food prices failed to rise for the first time since January, being unchanged in December so that the respective annual rate slowed 0.4ppt to 4.8%Y/Y. While the BRC index remains well below the headline CPI rate due to the exclusion of energy and services prices, the survey provides further evidence that UK CPI inflation peaked at 11.1%Y/Y in October. Certainly, given the sharp fall in UK petrol prices of around 5%M/M in December, we expect headline CPI inflation to have fallen for a second successive month, by around ½ppt from 10.7%Y/Y in November. Among other better news on the inflation front, the ongoing drop in wholesale gas prices amid unseasonably mild winter weather across Europe suggests that household energy bills need not rise quite as far as previously feared once the government scales back support from April on. And today also brought further encouraging signs with respect to household inflation expectations, with a Citi/YouGov survey reporting that the average expectation for inflation in 5-10 years' time declined a further 0.3ppt in December to 3.6%Y/Y, more than 1ppt below August's peak (4.8%Y/Y) in August and only marginally higher than the pre-pandemic average of 3.2%Y/Y.

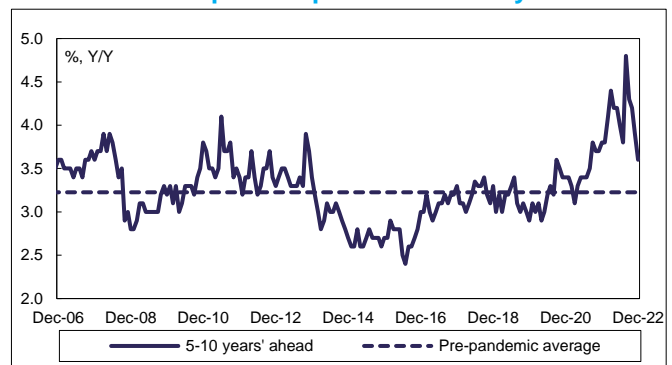
### Credit card borrowing rises but mortgage approvals slump

Amid the higher cost of living, today's BoE monthly lending figures for November reported a sizeable increase in households' credit card borrowing in spite of the recent jump in interest rates. Indeed, credit card borrowing increased by a net £1.2bn in November, up from just £0.4bn in October and the second largest one-month increase since the series began in 1993. This saw the annual growth in the outstanding stock of such lending rise above 12%Y/Y. Taken with other unsecured lending, total consumer credit rose a net £1.5bn in November, up from £0.7bn in the previous two months, to leave the annual growth rate unchanged at 7%Y/Y. There was another solid increase in new mortgage lending too, by £4.4bn, up from £3.6bn in October but nevertheless below the previous six-month average (£5.2bn). But this reflects completions on mortgage approvals made ahead of the Truss-related blow-out in interest rates. The average effective interest rate on this lending stood a still relatively low 3.35% in November up 26bps on the month but nevertheless more than double the low just twelve months before. Indeed, with the average interest rate offered on a 2Y fixed-rate mortgage with a LTV ratio of 75% at a whopping 5.97% in November, the number of approvals on new mortgages once again fell sharply that month, down to 46.1k, from 57.9k in October and the lowest since June 2020, suggesting a marked slowdown in secured lending in early 2023 and a likely ongoing adjustment in the housing market over coming quarters.

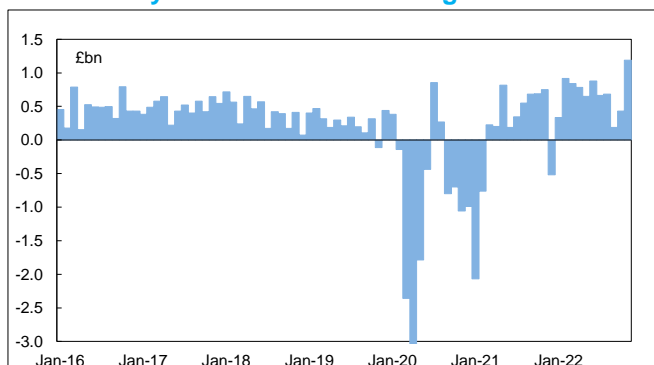
#### UK: BRC shop price inflation



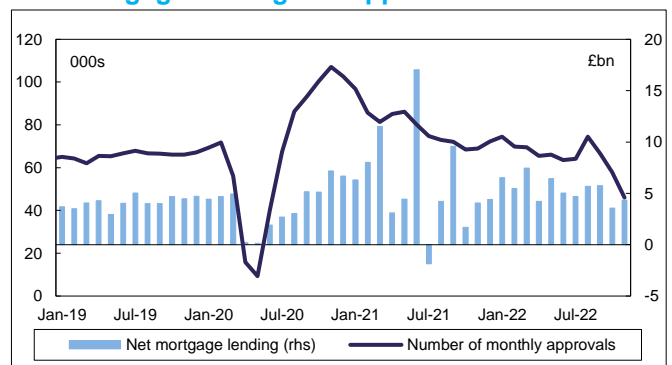
#### UK: Household price expectations 5-10 years ahead



#### UK: Monthly credit card net lending















#### UK: Mortgage lending and approvals














## The day ahead in the UK

In the UK, tomorrow will bring the final service sector and composite PMIs for December. The flash release revealed that the composite PMI rose 0.8pt to 49.0, thanks to a marked improvement in the services sector, where the activity index rose 1.2pts to 50.0, albeit merely implying stagnation. Of course, having been conducted between 6-14 December, the preliminary survey will not fully reflect the disruption from the impact of the snow and rail strikes, with hospitality set to have been particularly severely impacted at what is typically one of its busiest periods. Meanwhile, new car registration numbers for December and the BoE's latest Decision Maker Panel survey results will also be published.

## European calendar

Today's results						
Economic data						
Country	Release	Period	Actual	Market consensus/ <i>Daiwa forecast</i>	Previous	Revised
Euro area	 Final services (composite) PMI	Dec	<b>49.8 (49.3)</b>	49.1 (48.8)	48.5 (47.8)	-
Germany	 Final services (composite) PMI	Dec	<b>49.2 (49.0)</b>	49.0 (48.9)	46.1 (46.3)	-
France	 Preliminary CPI M/M% (Y/Y%)	Dec	<b>-0.1 (5.9)</b>	0.5 (6.4)	0.3 (6.2)	-
	 Preliminary HICP M/M% (Y/Y%)	Dec	<b>-0.1 (6.7)</b>	0.4 (7.3)	0.4 (7.1)	-
	 Final services (composite) PMI	Dec	<b>49.5 (49.1)</b>	48.1 (48.0)	49.3 (48.7)	-
	 INSEE consumer confidence	Dec	<b>82</b>	84	83	-
Italy	 Services (composite) PMI	Dec	<b>49.9 (49.6)</b>	49.5 (-)	51.2 (49.6)	-
Spain	 Services (composite) PMI	Dec	<b>51.6 (49.9)</b>	50.7 (-)	51.2 (49.6)	-
UK	 BRC shop price index Y/Y%	Dec	<b>7.3</b>	-	7.4	-
	 Net consumer credit £bn (Y/Y%)	Nov	<b>1.5 (7.0)</b>	1.0 (-)	0.8 (7.0)	<b>0.7 (6.9)</b>
	 Net mortgage lending £bn (approvals '000s)	Nov	<b>4.4 (46.1)</b>	- (53.0)	4.0 (59.0)	<b>3.6 (57.9)</b>
Auctions						
Country	Auction					
Germany	 sold €4.48bn of 2.2% 2024 bonds at an average yield of 2.58%					

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	 09.00	Construction PMI	Dec	-	43.6	
Germany	 07.00	Trade balance €bn	Nov	7.5	6.8	
	 08.30	Construction PMI	Dec	-	41.5	
France	 08.50	Construction PMI	Dec	-	40.7	
Italy	 08.45	Construction PMI	Dec	-	52.0	
	 10.00	Preliminary CPI M/M% (Y/Y%)	Dec	0.2 (11.6)	0.5 (11.8)	
	 10.00	Preliminary HICP M/M% (Y/Y%)	Dec	0.2 (12.6)	0.7 (12.6)	
	 09.30	Final services (composite) PMI	Dec	50.0 (49.0)	48.8 (48.2)	
	 09.00	New car registrations Y/Y%	Dec	-	23.5	
Auctions and events						
UK	 09.30	BoE Decision Maker panel survey				
	 11.30	Auction: £3.5bn of 4.125% 2027 bonds				

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

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