

# Euro wrap-up

## Overview

- Gilts made significant losses as UK GDP failed to contract in Q4 despite a non-negligible drop in December.
- While a hawkish Governing Council member suggested that the ECB could end Asset Purchase Programme reinvestments in Q3, Bunds also made losses on a quiet day for euro area economic data.
- The coming week will bring new data for the UK labour market, inflation, and retail sales as well as euro area jobs, IP and trade.

**Chris Scicluna**

+44 20 7597 8326

### Daily bond market movements

Bond	Yield	Change
BKO 2½ 03/25	2.744	+0.072
OBL 2.2 04/28	2.394	+0.073
DBR 2.3 02/33	2.360	+0.067
UKT 1 04/24	3.549	+0.104
UKT 1¼ 07/27	3.325	+0.120
UKT 4¼ 06/32	3.393	+0.107

\*Change from close as at 5.00pm GMT.

Source: Bloomberg

## UK

### GDP moves sideways in Q4 to remain below pre-pandemic level

Broadly in line with expectations and just 0.1ppt softer than the BoE's latest forecast, GDP in Q4 was unchanged on the quarter after contracting 0.2%Q/Q in Q3. As a result, it was still 0.8% below the pre-pandemic level in Q419, leaving the UK as the sole member of the G7 to have failed to surpass that benchmark. While spending on a range of services and goods, including food, declined, household consumption edged up in Q4 by 0.1%Q/Q. That was not enough to reverse the decline of 0.4%Q/Q in Q3 – which was in part related to the national holiday for the Queen's funeral – and so left household consumption more than 2% below the pre-pandemic level. Fixed investment was stronger in Q4, up 1.5%Q/Q, with firmer growth in both the public and private sectors. Most welcome was a rise of 4.8%Q/Q in business investment, which returned it to the pre-pandemic level. That, however, was led by a rebound in transport equipment, likely at least in part due to an easing of supply-chain strains. And it left the level of business investment merely 0.2% above the level in Q316 immediately following the Brexit referendum. Government consumption also supported economic activity in Q4, rising 0.8%Q/Q thanks in part to spending on Covid-19 booster vaccines. And inventory adjustments added arithmetically to GDP growth too, although the ONS suggested that this reflected technical factors and that destocking likely occurred.

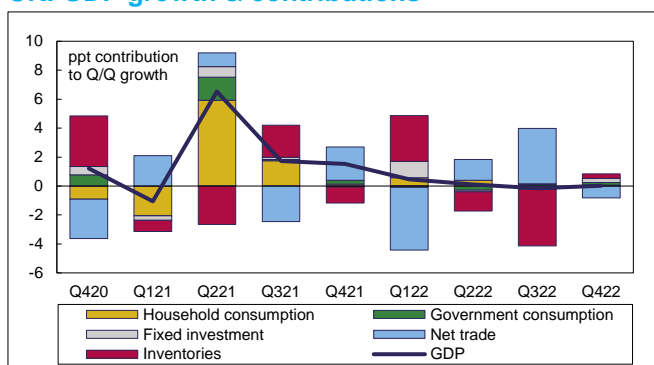
### Underlying trade deficit widens again

While domestic demand picked up in Q4, net trade subtracted from economic growth. Import volumes rose 1.5%Q/Q, due principally to higher deliveries of machinery, transport equipment and chemicals, likely in part due to easing supply constraints. In contrast, export volumes declined 1.0%Q/Q, falling back below the pre-pandemic level. That was due principally to a fall of 3.1%Q/Q in services exports, related in part to financial services. In contrast, goods exports were firmer. However, that in part reflected increased shipments of non-monetary gold, which distort the picture of the underlying trade performance. And, excluding such items, the trade deficit widened in Q4 by 0.3ppt to 4.2% of GDP, back close to the high on the series dating back to 1997.

### Drop in economic activity in December points to renewed contraction in Q1

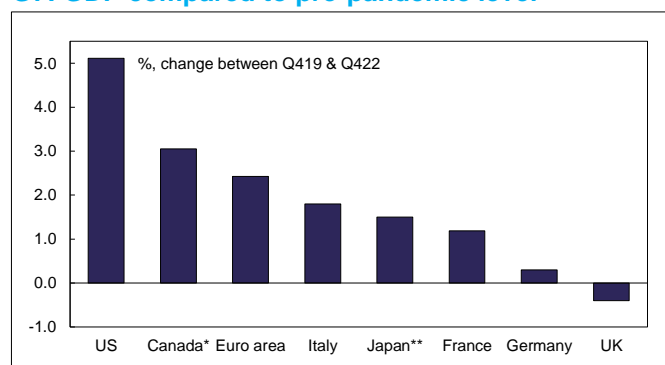
The absence of any economic growth in Q4 reflected the contraction in December, when GDP fell 0.5%M/M following growth of just 0.1%M/M the prior month. Services activity dropped 0.5%M/M, in part due to the effect of strikes, administration of fewer Covid vaccinations, weak retail sales, and disruption to English Premier League fixtures due to the FIFA World Cup. Like GDP, that left services output unchanged on the quarter in Q4. Manufacturing output was effectively flat in December and over Q4 as a whole, as growth in pharmaceuticals and transport equipment – the latter reflecting improved supply

### UK: GDP growth & contributions



Source: Refinitiv and Daiwa Capital Markets Europe Ltd.

### G7: GDP compared to pre-pandemic level



\*compared to Q322 \*\*using our Q422 forecast. Source: Refinitiv and Daiwa Capital Markets Europe Ltd.

chains – offset weakness in most other major categories. Overall industrial production declined in Q4, however, as utilities and mining activity subtracted. In contrast, while it was the coldest December in a decade, construction output was also flat that month. But that meant it rose for a fifth successive quarter in Q4, up 0.3%Q/Q. Of course, we would not be surprised to see significant revisions to the Q4 GDP figures, not least a downwards revision to the estimate of business investment, which currently looks eye-catchingly firm. But the weak end to the quarter already implies significant negative carry-over into Q1. And with household demand likely to remain under pressure, the housing market now firmly in retreat, strikes persisting, and private investment likely to be weaker, we forecast a contraction in GDP in Q1 and, indeed, in the following two quarters too.

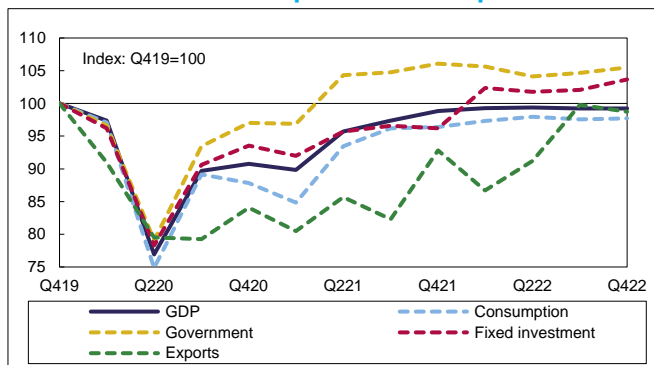
## The week ahead in the UK

The coming week brings a number of key UK economic data releases, including the latest labour market report (Tuesday), inflation figures (Wednesday) and retail sales data (Friday). Despite the weakness in GDP, the labour market has remained remarkably resilient. Admittedly, surveys suggest softer employment growth over recent months – indeed, the REC report on jobs implied a fourth consecutive drop in permanent placements in January. But given subdued labour force participation, the unemployment rate is likely to come in at 3.7% in the three months to December, just 0.1ppt higher than in the three months to September and 0.2ppt above the 48-year low recorded in August. As such, wage growth is expected to slow only modestly from the 6.4%3M/Y rate recorded in November – with private sector regular pay growth likely still above 7.0%Y/Y – and therefore remain uncomfortably high for the BoE. In terms of inflation, we expect the headline CPI rate to have eased for third consecutive month in January, by 0.4ppt to 10.1%Y/Y, a full percentage point below the October peak. The drop will principally reflect a further moderation in energy inflation amid a sharp decline in petrol prices. But while services inflation is expected to have remained at a series high, a drop in core goods inflation should see the core CPI rate edge slightly lower too. But with household purchasing power continuing to be eroded by high prices and consumer confidence historically weak, retail sales are likely to have maintained a downwards trend at the start of the year. Retail sales are expected to fall 0.3%M/M in January, and a little further than that excluding petrol, leaving both measures down 5.8%Y/Y. Meanwhile, BoE Chief Economist Pill will speak publicly on the UK economy on Thursday.

## The week ahead in the euro area

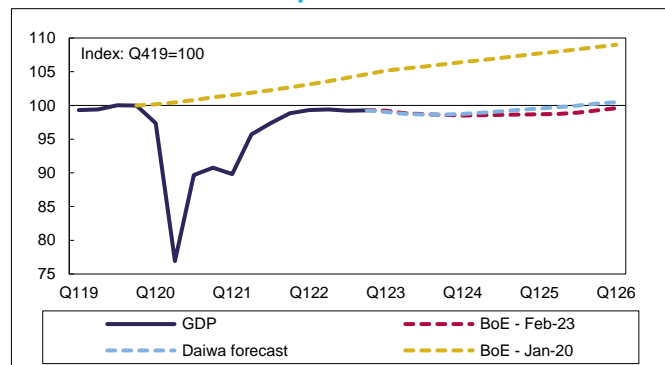
The coming week will be relatively thin on the ground for new top-tier euro area data, although the releases due will likely report a sharp weakening in economic activity at the end of 2022. For example, the updated euro area Q4 GDP figures on Tuesday might well see the modestly positive growth initially estimated (0.1%Q/Q) revised away, as the inclusion of December activity figures take a toll. Indeed, the soft end to the year will be illustrated by the euro area industrial production

### UK: GDP – selected expenditure components



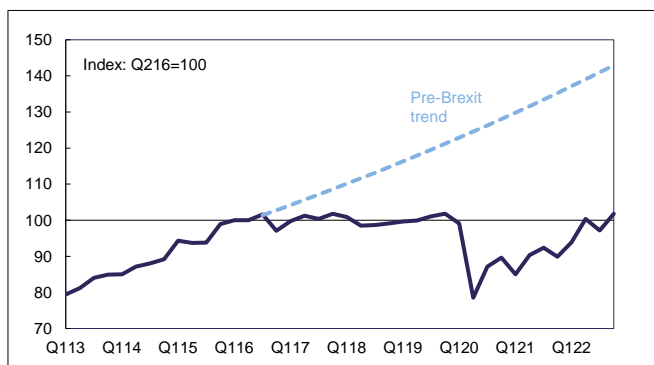
Source: Refinitiv and Daiwa Capital Markets Europe Ltd.

### UK: GDP forecast comparison



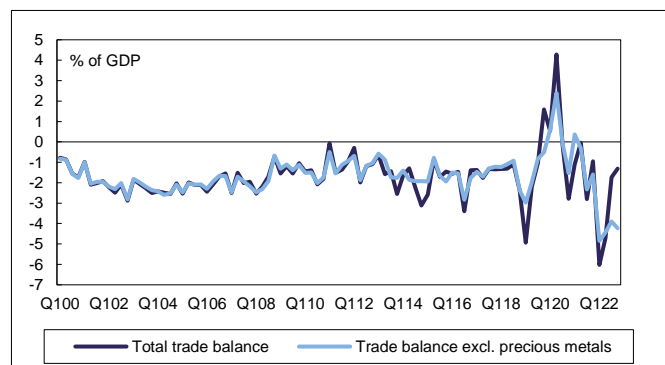
Source: Refinitiv, BoE and Daiwa Capital Markets Europe Ltd.

### UK: Business investment



Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

### UK: Trade balance as % of GDP

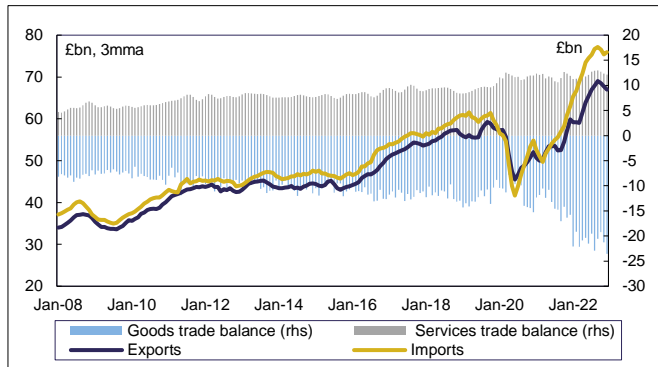


Source: ONS and Daiwa Capital Markets Europe Ltd.

and goods trade figures for December due on Wednesday. While figures published today from Italy were firmer than expected, with industrial output up 1.6%M/M, they were still consistent with a notable decline in Q4 (-1.0%Q/Q), a similar quarterly rate as in France and Spain. Moreover, with output (excluding construction) having declined sharply in [Germany](#) (-2.1%M/M) and especially Ireland (-8.5%M/M), we expect aggregate euro area IP to have fallen by a little less than 1%M/M, fully reversing the increase in November, and leaving it down around ½%Q/Q in Q4. Despite the slowdown in GDP growth in Q4, the accompanying labour market data (Tuesday) will likely report another solid increase in employment last quarter, reflecting not least increases in Germany (107k) and Spain (89k). Also of note in the week ahead will be revised January inflation estimates from Spain (Tuesday) and France (Friday), with the Spanish Statistical Office having cautioned that the flash release – which reported a surprise increase in inflation in January – was based on a smaller response rate than usual. We will also again hear from some ECB Governing Council members in the coming week, including ECB Chief Economist Lane who on Thursday will take stock of the euro area’s hiking cycle.

**The next edition of the Euro wrap-up will be published on 14<sup>th</sup> February 2023**

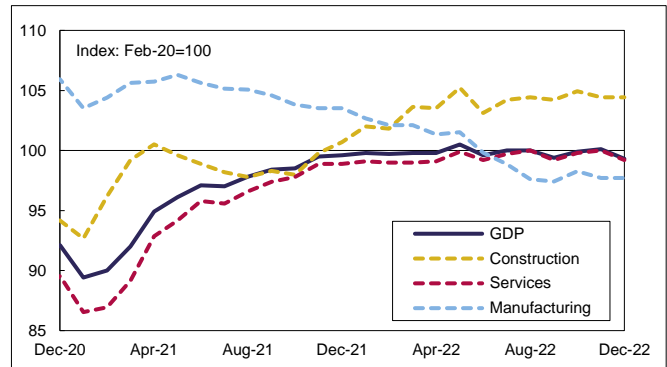
**UK: Trade balance (£bn)\***



\*Excluding precious metals.

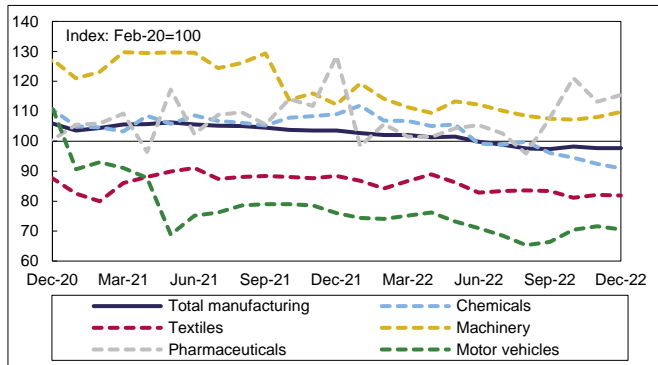
Source: Refinitiv and Daiwa Capital Markets Europe Ltd.

**UK: Monthly GDP & sectorial output**



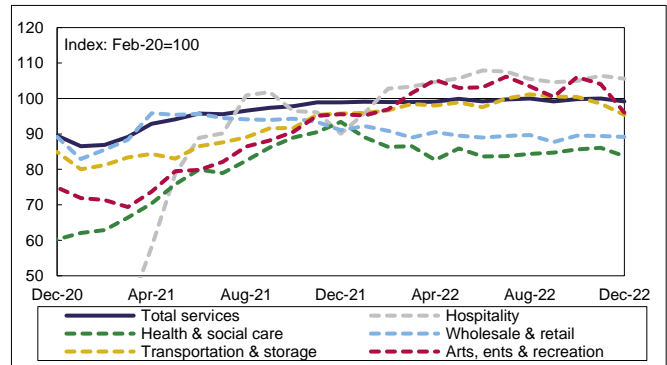
Source: Refinitiv and Daiwa Capital Markets Europe Ltd.

**UK: Manufacturing output by selected subsector**












Source: Refinitiv and Daiwa Capital Markets Europe Ltd.

**UK: Services activity by selected subsector**





Source: Refinitiv and Daiwa Capital Markets Europe Ltd.

## 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 	0.9	0.3	0.1	0.0	0.1	0.1	3.5	0.6	1.0
UK 	0.1	-0.2	0.0	-0.2	-0.3	-0.1	4.0	-0.5	0.3
<b>Inflation, %, Y/Y</b>									
Euro area									
Headline HICP 	8.0	9.3	10.0	7.4	5.4	3.7	8.4	4.6	2.2
Core HICP 	3.7	4.4	5.1	5.1	4.1	3.2	3.9	3.7	2.1
UK									
Headline CPI 	9.2	10.0	10.7	9.5	7.6	6.3	9.1	6.8	2.5
Core CPI 	6.0	6.3	6.4	5.9	4.8	3.9	5.9	4.4	2.5
<b>Monetary policy, %</b>									
ECB									
Refi Rate 	0.00	1.25	2.50	3.50	3.75	3.75	2.50	3.75	3.00
Deposit Rate 	-0.50	0.75	2.00	3.00	3.25	3.25	2.00	3.25	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	
Italy 	Industrial production M/M% (Y/Y%)	Dec	<b>1.6 (0.1)</b>	0.2 (-)	-0.3 (-3.7)	<b>-0.1 (-3.4)</b>	
UK 	GDP Q/Q% (Y/Y%)	Q4	<b>0.0 (0.4)</b>	<u>0.0 (0.4)</u>	-0.3 (1.9)	<b>-0.2 (-)</b>	
	GDP M/M%	Dec	<b>-0.5</b>	<u>-0.5</u>	0.1	-	
	Industrial production M/M% (Y/Y%)	Dec	<b>0.3 (-4.0)</b>	-0.2 (-5.2)	-0.2 (-5.1)	<b>0.1 (-4.3)</b>	
	Manufacturing production M/M% (Y/Y%)	Dec	<b>0.0 (-5.7)</b>	-0.2 (-6.1)	-0.5 (-5.9)	<b>-0.6 (-5.6)</b>	
	Index of services M/M% (Q/Q%)	Dec	<b>-0.8 (0.0)</b>	-0.3 (0.1)	0.2 (-0.1)	<b>- (0.0)</b>	
	Construction output M/M% (Y/Y%)	Dec	<b>0.0 (3.7)</b>	-0.2 (2.8)	0.0 (4.0)	<b>-0.5 (4.6)</b>	
	Goods trade balance (ex precious metals) £bn	Dec	<b>-19.3 (-23.6)</b>	-17.3 (-)	-15.6 (-21.0)	<b>-14.7 (-21.2)</b>	
Auctions							
Country	Auction						
- Nothing to report -							

Source: Bloomberg 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 13 February 2023</b>					
- Nothing scheduled -					
<b>Tuesday 14 February 2023</b>					
Euro area		10.00	GDP – second estimate Q/Q% (Y/Y%)	Q4	<u>0.1 (1.9)</u> / 0.3 (2.3)
		10.00	Preliminary employment Q/Q% (Y/Y%)	Q4	- / 0.3 (1.8)
France		06.30	ILO unemployment rate %	Q4	7.1 / 7.1
UK		07.00	Unemployment claimant count rate % (change '000s)	Jan	- / 4.0 (19.7)
		07.00	Payrolled employees monthly change, '000s	Jan	0 / 28
		07.00	ILO unemployment rate %, 3M	Dec	3.7 / 3.7
		07.00	Average earnings including (excluding) bonuses 3M/Y%	Dec	6.2 (6.5) / 6.4 (6.4)
		07.00	Employment change '000s, 3M/3M	Dec	40 / 27
<b>Wednesday 15 February 2023</b>					
Euro area		10.00	Industrial production M/M% (Y/Y%)	Dec	<u>-1.0 (-)</u> / 1.0 (2.0)
		10.00	Trade balance €bn	Dec	-16.0 / -15.2
Spain		08.00	Final HICP (CPI) Y/Y%	Jan	<u>5.8 (5.8)</u> / 5.5 (5.7)
		08.00	Final core CPI Y/Y%	Jan	<u>7.5</u> / 7.0
UK		07.00	CPI M/M% (Y/Y%)	Jan	<u>-0.5 (10.1)</u> / 0.4 (10.5)
		07.00	Core CPI Y/Y%	Jan	<u>(6.2)</u> / 6.3
		07.00	PPI output prices M/M% (Y/Y%)	Jan	0.1 (13.3) / -0.9 (14.7)
		07.00	PPI input prices M/M% (Y/Y%)	Jan	0.2 (14.7) / -1.2 (16.5)
		09.30	House price index Y/Y%	Dec	- / 10.3
<b>Thursday 16 February 2023</b>					
Italy		09.00	Total trade balance €bn	Dec	- / 1.4
Spain		09.00	Total trade balance €bn	Dec	- / -3.3
<b>Friday 17 February 2023</b>					
Euro area		09.00	ECB current account balance €bn	Dec	- / 13.6
France		07.45	Final HICP (CPI) Y/Y%	Jan	<u>7.0 (6.0)</u> / 6.7 (5.9)
UK		07.00	Retail sales including auto fuels M/M% (Y/Y%)	Jan	-0.3 (-5.8) / -1.0 (-5.8)
		07.00	Retail sales excluding auto fuels M/M% (Y/Y%)	Jan	-0.4 (-5.8) / -1.1 (-6.1)

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

## The coming week's key events & auctions

Country	GMT	Event / Auction
<b>Monday 13 February 2023</b>		
- Nothing scheduled -		
<b>Tuesday 14 February 2023</b>		
Italy	 10.00	Auction: €3.5bn of 3.50% 2026 bonds
	 10.00	Auction: €3.5bn of 3.85% 2029 bonds
	 10.00	Auction: €1.5bn of 3.25% 2038 bonds
UK	 10.00	Auction: £3bn 3.25% 2033 bonds
<b>Wednesday 15 February 2023</b>		
Euro area	 14.00	ECB President Lagarde participates in a debate on the ECB Annual Report 2021
Germany	 10.30	Auction: €1.0bn of 1.25% 2048 bonds
	 11.30	Auction: €1.5bn of 0.00% 2052 bonds
<b>Thursday 16 February 2023</b>		
Euro area	 09.40	ECB's Panetta scheduled to speak – 'Monetary policy after the energy shock'
	 09.00	ECB publishes its Economic Bulletin
	 15.00	ECB's Chief Economist Lane scheduled to speak – 'The euro area hiking cycle: An interim assessment'
France	 09.50	Auction: 2.50% 2026 bonds
	 09.50	Auction: 0.75% 2028 bonds
	 09.50	Auction: 2.50% 2030 bonds
	 10.50	Auction: 0.10% 2029 index-linked bonds
	 10.50	Auction: 0.10% 2032 index-linked bonds
	 10.50	Auction: 0.10% 2038 index-linked bonds
Spain	 09.30	Auction: 0.80% 2027 bonds
	 09.30	Auction: 0.80% 2029 bonds
	 09.30	Auction: 2.55% 2032 bonds
UK	 17.00	BoE Chief Economist Pill participates in a fireside chat on the UK economy
<b>Friday 17 February 2023</b>		
Euro area	 11.30	ECB's Villeroy scheduled to speak on monetary policy and inflation

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

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