Euro wrap-up

Overview

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- Bunds followed USTs higher despite signs of ongoing resilience in the euro area's labour amid weakening economic momentum and signals from a German investor survey of some stabilisation in the outlook.
- Gilts also made gains as UK labour market data signalled a loss of momentum in wage growth and a further decline in job vacancies.
- Wednesday will bring September results for euro area industrial production and goods trade, as well as UK inflation data for October.

Daily bond market movements

Bond	Yield	Change
BKO 3.1 12/25	2.980	-0.088
OBL 2.4 10/28	2.549	-0.110
DBR 2.6 08/33	2.598	-0.112
UKT 3½ 10/25	4.550	-0.077
UKT 4½ 06/28	4.169	-0.138
UKT 3¼ 01/33	4.147	-0.161

*Change from close as at 5.00pm GMT.
Source: Bloomberg

Euro area

Euro area GDP contracted in Q3 with at least half of member states with declining or zero growth

Today's second estimate of euro area GDP confirmed a modest contraction of 0.1%Q/Q in Q3, which left economic output up just 0.1%Y/Y. And while the level of GDP was some 3.0% above the pre-pandemic benchmark in Q419, this continued to lag significantly behind the US, where output in Q3 was more than 7% higher. There was significant variation of the economic performance among member states. We already knew that, influenced by the activities of multinationals, Ireland (-1.8%Q/Q) reported the largest drop in GDP growth in the euro area last quarter. But today's data also unveiled a third consecutive contraction in the Netherlands (-0.2%Q/Q). Indeed, of the fifteen member states to have published data so far, ten reported a decline or no growth in GDP in Q3, including Germany (-0.1%Q/Q), Italy (0.0%Q/Q), Austria (-0.6%Q/Q) and Finland (-0.9%Q/Q). The weakness was offset in part by firm expansions in Belgium (0.5%Q/Q) and Spain (0.3%Q/Q) and modest growth in France (0.1%Q/Q). But momentum appears to have faded throughout the quarter across the member states, suggesting a negative carry over into Q4.

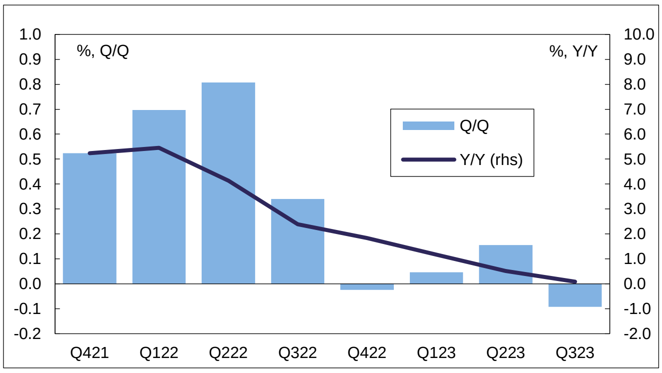
Employment growth accelerated, highlighting ongoing resilience to weaker GDP growth (for now)

Despite slowing economic momentum, today's figures confirmed ongoing resilience of the labour market over the summer. Indeed, despite the contraction in GDP, there was a tenth successive quarterly increase in employment, with the pace accelerating slightly from Q2 by 0.2ppt to 0.3%Q/Q (467k). That left it up 1.3%Y/Y and 3.4% (5.58mn) above the pre-pandemic level in Q419. While employment appears to have continued to have grown widely across the euro area in Q3, more than half of the increase was accounted for by Spain, no doubt buoyed by an increase in tourism over the summer period. But various surveys in October suggested no marked improvement in economic momentum in the euro area at the start of Q4, signalling that GDP likely moved sideways at best. And with vacancies having started to fall as firms in manufacturing look to cut headcount amid weak demand for goods and employment in certain services is set to fall back as the tourism season draws to a close, surveys suggest that jobs growth might be grinding to a halt.

German investor survey points to stabilisation in the outlook but downbeat about Q4

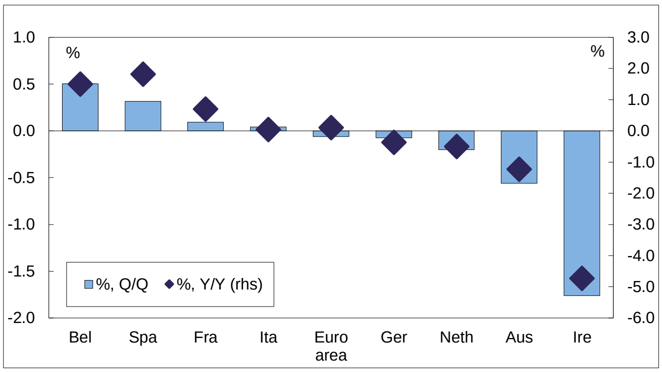
Like last week's euro area Sentix survey findings, today's German ZEW investor survey pointed to ongoing challenges in the middle of the fourth quarter. In particular, the current conditions index edged up just 0.1pt to -79.8 in November, the second lowest reading since the initial pandemic slump in 2020 and the global financial crisis before that. Indeed, the index was trending so far in Q4 some 10pts below the Q3 average and remained some 70pts below the long-run average, supporting our view that Germany's economy slipped into recession in the second half of 2023. But the survey also raised cautious

Euro area: Euro area GDP growth



Source: Refinitiv Datastream and Daiwa Capital Markets Europe Ltd.

Euro area: GDP growth in selected member states



Source: Eurostat, Macrobond and Daiwa Capital Markets Europe Ltd.

optimism that the trough has now passed. Indeed, financial market participants were once again more upbeat about the outlook over the coming six months, with the respective expectations balance rising for a fourth consecutive month, by 10.9pts to 9.8, the first positive reading since April. Against this backdrop, firms from various sectors, including autos, steel, machinery, chemicals and retail, were less pessimistic about their expectations for profit growth over the coming six months.

The day ahead in the euro area

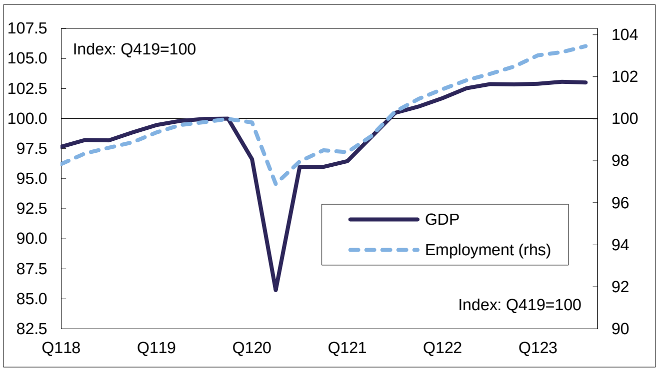
Tomorrow's euro area's data flow will bring further insights into economic momentum at the end of third quarter, with the publication of industrial production data for the region as a whole. Figures published so far by the larger member states have been mixed, with declines in Germany (-1.4%M/M) and France (-0.5%M/M) and no growth in Italy contrasting with a rise in Spain (1.1%M/M). But Friday's releases also revealed a contraction in September in the Netherlands, Ireland and Austria, so we expect aggregate euro area output to have declined by more than 1.0%M/M in September, which would leave it down 1.2%Q/Q in Q3. Meanwhile, euro area goods trade figures for September will offer further insight into the contribution of net trade to GDP in Q3. According to the German numbers, the decline in export values outpaced the drop in imports during September, suggesting a broadly neutral contribution from net trade last quarter. Final French and Italian HICP data for October are also due to be published tomorrow.

UK

Labour market data continue to present mixed messages

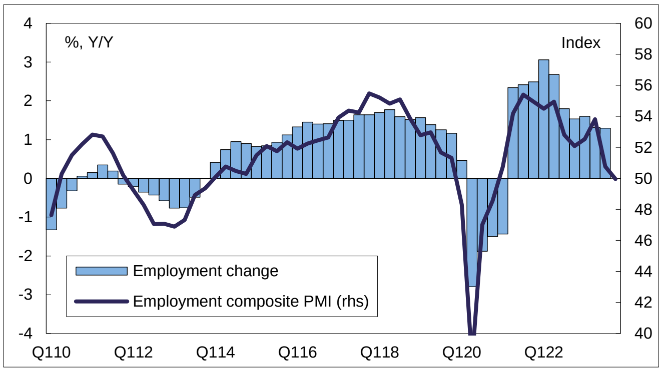
Despite the slowdown in economic activity over the summer, and downbeat signals from various survey measures, the UK's labour market has continued to hold up relatively well. Admittedly, key indicators have provided mixed messages about the extent of the tightness in the labour market, complicating the judgement of the risks of inflation persistence stemming from wage growth. And the suspension of the ONS' official Labour Force Survey due to the decline in the response rate has added further to the challenges of assessing current conditions. But while today's figures beat expectations, suggesting still elevated wage growth and again presented mixed messages about the amount of slack (or lack of) in the labour market, they were on the whole consistent with a slowdown in momentum and further supported our view that the MPC has come to the end of its interest rate tightening cycle.

Euro area: GDP and employment levels



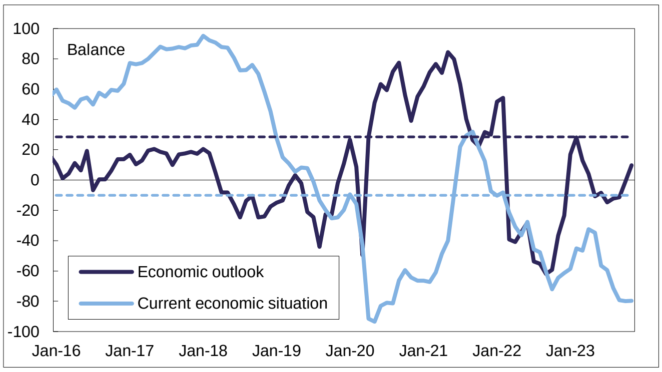
Source: Refinitiv Datastream and Daiwa Capital Markets Europe Ltd.

Euro area: Employment growth & PMI*



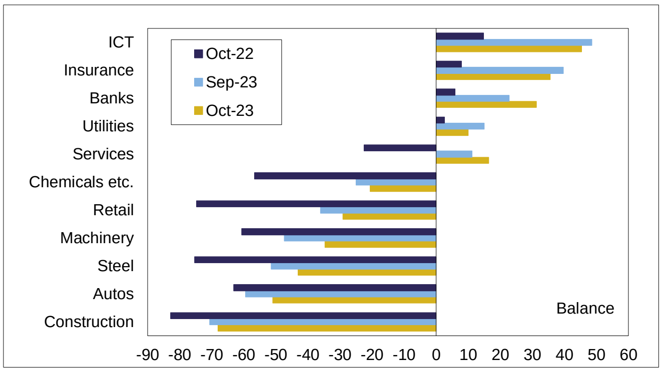
**Q423 figure for employment PMI is October survey. Source: Refinitiv Datastream, S&P Global and Daiwa Capital Markets Europe Ltd.*

Germany: ZEW investor sentiment indices*



**Dashed lines represent long-run average. Source: Refinitiv Datastream and Daiwa Capital Markets Europe Ltd.*

Germany: ZEW expected profit growth indices



Source: Refinitiv Datastream and Daiwa Capital Markets Europe Ltd.

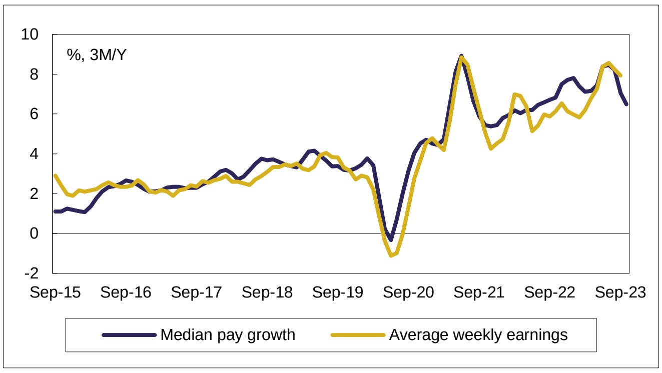
Pay growth still historically high, but signs that pressures are moderating more rapidly

The labour earnings figures came in a bit firmer than expected in the three months to September, with the headline rate moderating just 0.5ppt on the quarter to a still historically high 7.9%3M/Y, influenced in part by the Civil Service one-off payments made in July and August 2023 as well as only a marginal easing in private sector pay growth by 0.1ppt to 7.7%3M/Y. This in part reflected a pickup in wage growth in the hospitality and retail sector amid an increase in summer bonuses and still very strong growth in finance and insurance, which largely offset a dip in manufacturing and construction pay growth. When excluding bonuses payments, private regular pay was down 0.4ppt over the quarter at 7.8%3M/Y, although this was counterbalanced by a jump in public sector regular pay, up 1ppt to a series-high 7.3%3M/Y. And with wage growth having moderated to a smaller degree than inflation, today's figures confirmed that real regular pay adjusted for CPI (1.1%3M/Y) rose for a third consecutive month and by the most for almost two years. But looking at the most recent trend on an annualised three-month basis, private sector regular pay slowed a substantial 4.9ppts on the quarter in September to 5.6%3M/3M ann., the lowest since April 2022. And when including bonuses, total pay growth was down 7.3ppts to fourteen-month low of 5.2%3M/3M ann.. Moreover, real-time data from HMRC reinforce the impression that labour earnings growth is weakening. In particular, growth in median pay slowed 2.0ppts in October to 6.5%3M/Y, with annualised growth on a three-month basis falling into negative territory for the first time since the initial Covid-19 lockdown.

Employment unexpectedly ticks higher, but signs that labour demand is weakening

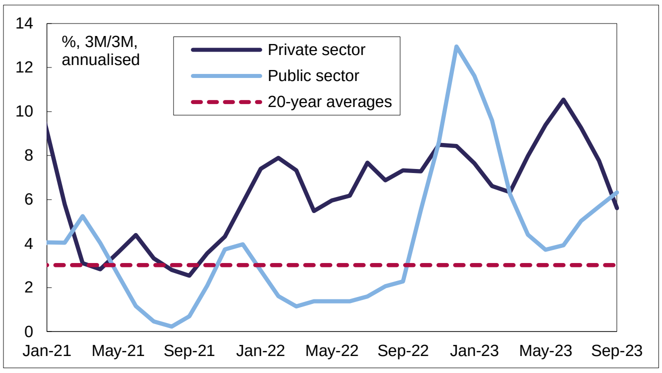
In terms of today's signals on employment, there was a notable upwards revision to the number of payrolled employees derived from HMRC data in September. Indeed, contrasting with the initial estimate of a decline of 11k, payrolled employees were now assessed to have risen by 32k that month. And the flash reading for October suggested a further rise of 33k, to leave employees on this measure up 398k compared with a year ago and roughly 1.75mn above the pre-pandemic level. Meanwhile, having declined in the previous three months, the ONS's experimental measure of employment – based on HRMC data – suggested an increase in the three months to September, by 54k. But this was still down by more than 100k compared with the summer peak and still roughly 90k below the pre-pandemic benchmark. As such, there remains a significant difference in the estimated number of people in work between the series. Despite the modest pickup in employment in September, today's release also reported a further sizable decline in the number of job openings in the three months to October, by 58k to 957k, the sixteenth successive quarterly decline with sixteen out of the eighteen subsectors reporting a drop, to leave the level of vacancies at their lowest since May 2021. This tallies closely with recent survey indicators, such as last week's REC report on jobs, which suggested that permanent placements fell for a thirteenth consecutive month in October, as firms reduced demand in the face of rising economic uncertainties and also reported increasing redundancies. Against this backdrop, today's figures saw the claimant count rise for a fourth month out of the past

UK: Measures of wage growth



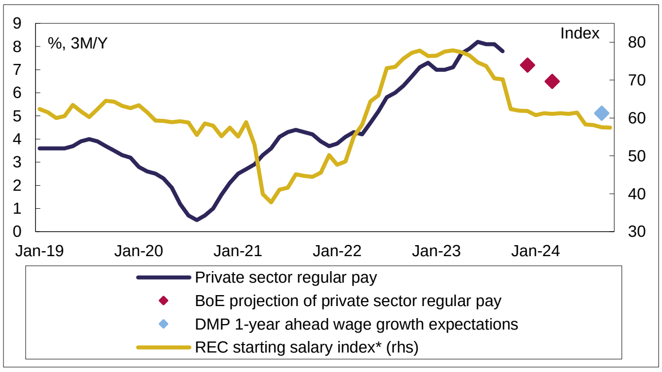
Source: ONS, HMRC, Refinitiv Datastream and Daiwa Capital Markets Europe Ltd.

UK: Average weekly earnings



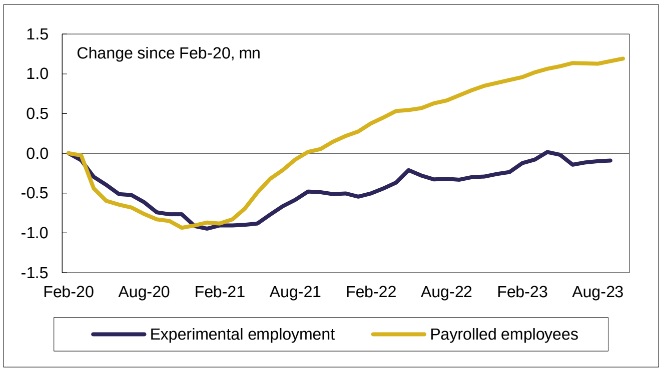
Source: Refinitiv Datastream and Daiwa Capital Markets Europe Ltd.

UK: Indicators of wage growth



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

UK: Employment & payrolled employees



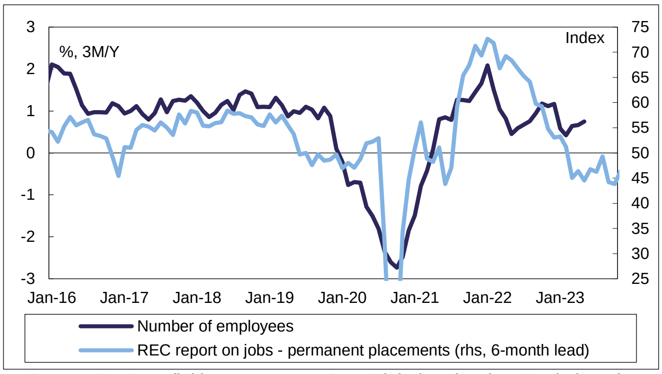
Source: ONS, Refinitiv Datastream and Daiwa Capital Markets Europe Ltd.

five in October, by 17.8k, to its highest level since May 2022. And while the claimant count rate remained unchanged at 4.0% and the ONS's experimental unemployment rate moved sideways over the third quarter at 4.2%, we expect it to shift higher over coming quarters.

The day ahead in the UK

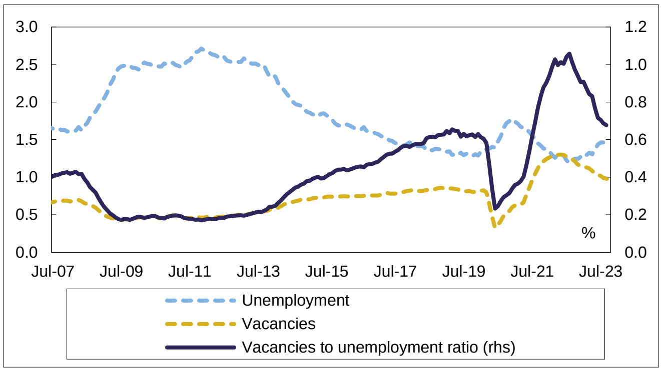
The UK data highlight tomorrow will be the October CPI release, which will report a notable drop in the headline rate due principally to the decline in Ofgem's household energy bill cap. Indeed, with consumer prices expected to have increased in October at just a fraction of the 2%M/M jump this time last year, we forecast headline inflation to decline around 2ppts to 4.7%Y/Y, which would mark the lowest for two years. While energy will provide the principal drag and food inflation is expected to fall for a sixth successive month, we also expect an ongoing disinflationary trend in non-energy industrial goods inflation to a two-year low as well as a modest easing in services inflation (albeit still at an elevated level of 6.7%Y/Y). As such, we forecast core inflation to decline a further 0.4ppt to a 19-month low of 5.7%Y/Y. The latest producer price inflation figures will provide a guide to consumer goods inflation over coming months, while the ONS house price index for September is expected to report the first annual decline since the start of 2012.

UK: Employment growth



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

UK: Job vacancies & unemployment rate*



**Unemployment rate based on ONS's experimental series. Source: ONS, Refinitiv Datastream and Daiwa Capital Markets Europe Ltd.*

European calendar

Today's results

Economic data

Country		Release	Period	**Actual**	Market consensus/ <u>*Daiwa forecast*</u>	Previous	Revised
Euro area		GDP – second estimate Q/Q% (Y/Y%)	Q3	**-0.1 (0.1)**	<u>*-0.1 (0.1)*</u>	0.1 (0.5)	-
		Preliminary employment Q/Q% (Y/Y%)	Q3	**0.3 (1.4)**	-	0.2 (1.3)	0.1 (-)
Germany		ZEW current assessment (expectations) balance	Nov	**-78.8 (9.8)**	-76.9 (5.0)	-79.9 (-1.1)	
Spain		Final HICP (CPI) Y/Y%	Oct	**3.5 (3.5)**	<u>*3.5 (3.5)*</u>	3.3 (3.5)	
UK		Payrolled employees, monthly change '000s	Oct	**33**	-18	-11	32
		Unemployment claimant count rate % (change '000s)	Oct	**4.0 (17.8)**	-	4.0 (20.4)	- (9.0)
		Average weekly earnings (excluding bonuses) 3M/Y%	Sep	**7.9 (7.7)**	7.4 (7.7)	8.1 (7.8)	8.2 (7.9)

Auctions

Country		Auction
Germany		sold €4.1bn of 3.1% 2025 bonds at an average yield of 3.06%

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

Yesterday's results

Economic data

Country		Release	Period	**Actual**	Market consensus/ <u>*Daiwa forecast*</u>	Previous	Revised
UK		Rightmove house price index M/M% (Y/Y%)	Nov	**-1.7 (-1.3)**		0.5 (-0.8)	-

Auctions

Country	Auction
	- Nothing to report -

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

Tomorrow's releases

Economic data

Country		GMT	Release	Period	Market consensus/ <u>*Daiwa forecast*</u>	Previous
Euro area		10.00	Industrial production M/M% (Y/Y%)	Sep	<u>*-1.1 (-6.2)*</u>	0.6 (-5.1)
		10.00	Trade balance €bn	Sep	6.7	11.9
France		06.30	Unemployment rate %	Q3	-	6.9
		07.45	Final HICP (CPI) Y/Y%	Oct	<u>*4.5 (4.0)*</u>	5.7 (4.9)
Italy		09.00	Final HICP (CPI) Y/Y%	Oct	<u>*1.9 (1.8)*</u>	5.6 (5.3)
UK		07.00	CPI (core CPI) Y/Y%	Oct	<u>*4.7 (5.7)*</u>	6.7 (6.1)
		07.00	Output (input) PPI Y/Y%	Oct	-1.0 (-3.3)	-0.1 (-2.6)
		09.30	House price index Y/Y%	Sep	-0.7	0.2

Auctions and events

Country		GMT	Event
Euro area		10.00	EU Commission publishes economic forecasts
Germany		10.30	Auction: 0.0% 2052 bonds
		10.30	Auction: 1.8% 2053 bonds

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

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