Daiwa Capital Markets

Euro wrap-up

Overview

Chris Scicluna +44 20 7597 8326

Emily Nicol +44 20 7597 8331

- Bunds made sizeable gains as German inflation fell further than expected, dropping to its lowest level since June 2021, even as the Commission survey suggested that services price expectations remain sticky.
- While UK mortgage approvals ticked higher, Gilts also made gains as households made a net repayment of their mortgage debt for a second successive month.
- Thursday will bring the flash estimates of euro area inflation, euro area unemployment figures, and the results of the BoE's latest Decision Maker Panel survey.

Daily bond market movements

Bond	Yield	Change
BKO 3.1 12/25	2.806	-0.104
OBL 2.4 10/28	2.351	-0.092
DBR 2.6 08/33	2.421	-0.072
UKT 3½ 10/25	4.528	-0.054
UKT 4½ 06/28	4.091	-0.106
UKT 3¼ 01/33	4.086	-0.081

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

Euro area

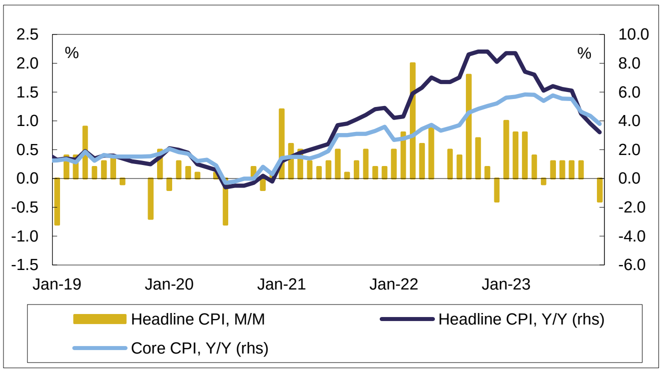
Flash estimate of German inflation drops further than expected to 29-month low in November

According to the flash estimate, German consumer price inflation extended its downtrend in November and by more than expected. In particular, the EU-harmonised HICP rate fell 0.7ppt to 2.3%Y/Y, the lowest since June 2021 and 0.2ppt below the median forecast on the Bloomberg survey. And the national CPI measure fell 0.6ppt to 3.2%Y/Y, also a 29-month low and 0.3ppt below the Bloomberg consensus. The fall in headline inflation was in part driven by further significant declines in the non-core components related in part to favourable base effects. In particular, on the national CPI measure, thanks also to a significant drop in auto fuel prices, energy inflation fell 1.3ppts to -4.5%Y/Y, marking the steepest year-on-year fall since end-2020. And while food prices rose on the month, the respective inflation rate still moderated 0.6ppt to a 21-month low of 5.5%Y/Y. But among the core components, services inflation – which remains the biggest concern of ECB policymakers – fell 0.5ppt to a 15-month low of 3.4%Y/Y, with the data from the Länder suggesting a relatively broad-based moderation in this component. And with non-energy industrial goods inflation also lower in part due to subdued demand and the widespread easing in global factory price pressures, German core CPI inflation (excluding all food and energy) fell 0.5ppt to 3.8%Y/Y, the lowest since August 2022.

Data from other member states also indicate notable decline in euro area headline & core inflation

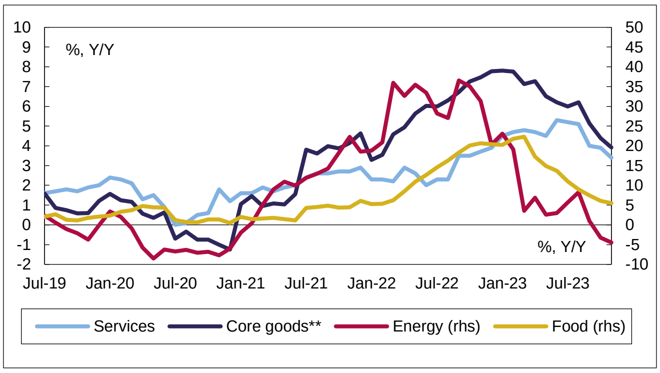
The flash November inflation figures from the other member states reporting today were mixed but also reassuringly consistent with a further moderation in underlying price pressures. Contrary to expectations of a small increase, Spanish inflation declined by 0.3ppt on both the HICP and CPI headline measures to three-month lows of 3.2%Y/Y. While no detailed data were published, INE reported that a rise in electricity inflation was more than offset by notable falls in the components for auto fuel, food and package tours. However, the Spanish core CPI measure, which excludes energy and unprocessed food, fell a steeper 0.7ppt to 4.5%Y/Y, the lowest since April 2022, suggesting that the moderation was relatively broad-based. Elsewhere, Irish HICP inflation fell a marked 1.3ppts to 2.3%Y/Y, which was the lowest since July 2021. While the major non-core components were significantly softer this month, core Irish inflation (excluding fresh food and energy) fell 0.4ppt to a ten-month low of 3.9%Y/Y. In Belgium, the headline HICP rate bucked the trend elsewhere by rising almost 0.7ppt in November. But it remained very low at -1.0%Y/Y. And the pickup in November was due principally to a less negative contribution from energy. Indeed, thanks to a weakening in services pressures, core CPI inflation (excluding fresh food and energy) fell 0.6ppt to 5.95%Y/Y, the lowest since August 2022. So, based on today's figures, the headline and core measures of euro area inflation have clearly fallen further in November, with the all-important services component also probably softer. Headline euro area inflation is likely to have fallen by at least 0.3ppt to a 28-month low of 2.6%Y/Y. And euro

Germany: Consumer price inflation*



*National measure. Source: Macrobond and Daiwa Capital Markets Europe Ltd.

Germany: Key CPI components*



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

area core inflation (excluding all food and energy) also looks likely to decline by at least 0.3ppt, to 3.9%Y/Y, which would be the lowest since June 2022.

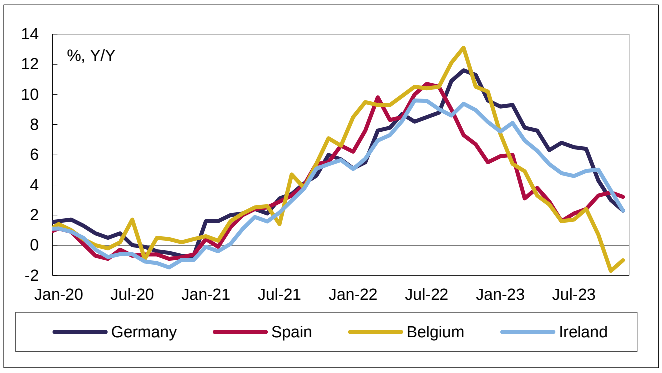
Consumer price expectations fall back, but survey flags stickiness in services selling prices

With euro area inflation having seemingly fallen further this month, household price expectations for the year ahead also eased again, with the European Commission's survey gauge down 2pts in November to a three-month low of 9.3. While this remains above the summer low (4.9) before the brief spike in petrol prices, it is well below the peak in March 2022 (63.8) and roughly 14pts below the long-run average, implying that consumers expect the disinflationary trend to be maintained over coming quarters. While still higher than the euro area aggregate, the index for Germany (18.3) eased to its lowest in five months and was almost 20pts below the long-run average, with the equivalent French and Spanish indices taking a notable step down this month and the Italian index recording the twelfth consecutive negative reading. The improvement in consumer expectations tallied with a further drop in retailers' selling price expectations for the coming three months, with the respective index falling to its lowest level since April 2021. And reflecting a moderation in input cost burdens and weak demand (see below), the respective manufacturing selling price index dropped to a three-year low. In contrast, however, today's survey suggested renewed impetus in selling price expectations in the construction and services sectors, with the equivalent indices up to six- (9.4) and eight-month (17.6) highs respectively. And while it was still well down on last year's peak (30.1), the services index remains well above the long-run average (6.1) and will no doubt reinforce concerns among the more hawkish Governing Council members about the stickiness of underlying inflation in the sector.

Economic sentiment suggests further stabilisation but remains consistent with contraction in Q4

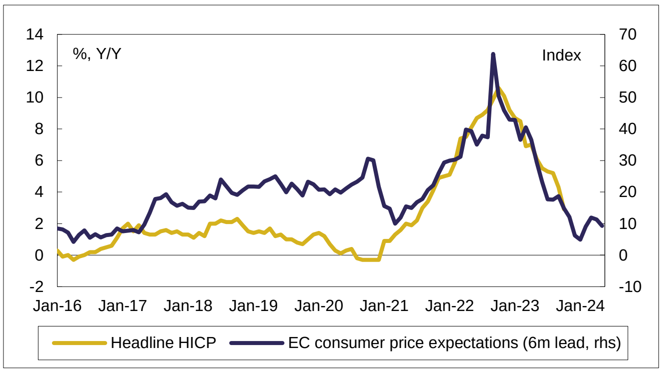
Like last week's flash PMIs, the Commission survey's sentiment indices signalled some further stabilisation in business conditions in the middle of Q4, similarly suggesting that the trough in the euro area's economic downturn may have been reached. Indeed, the headline euro area economic sentiment index (ESI) rose for the second successive month in November, by 0.3pt to 93.8, a four-month high. Admittedly, this still left the index more than 6% below the long-run average and trending so far in Q4 a touch below the average in Q3 when euro area GDP contracted 0.1%Q/Q, and more than 4pts below the average in the first half of the year. Perhaps most striking among the larger member states was a notable jump in the Netherlands, where the ESI rose 2.9pts to a seven-month high of 96.1. Elsewhere, the improvement in sentiment in France and deterioration in Germany largely reversed adjustments at the start of Q4, to leave the respective ESIs still some 4% and 11% below the long-run averages. And the Italian and Spanish ESIs fell to their lowest in just over a year, to be some 3½% and 1% below their long-run averages.

Euro area: Consumer price inflation*



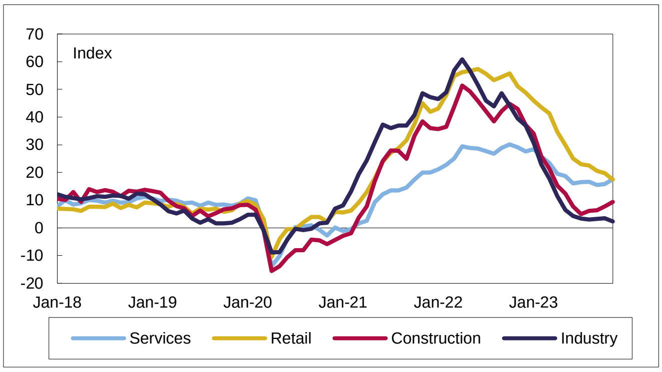
*EU harmonised measure. Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

Euro area: Consumer inflation & price expectations*



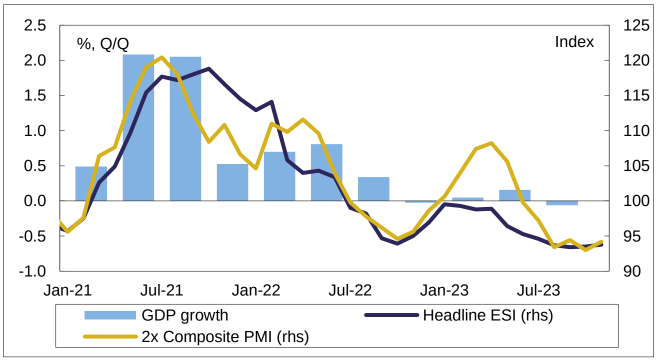
*Twelve months ahead. Source: Macrobond and Daiwa Capital Markets Europe Ltd.

Euro area: Firm selling price expectations*



*Three months ahead. Source: Macrobond and Daiwa Capital Markets Europe Ltd.

Euro area: GDP growth & sentiment indices



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

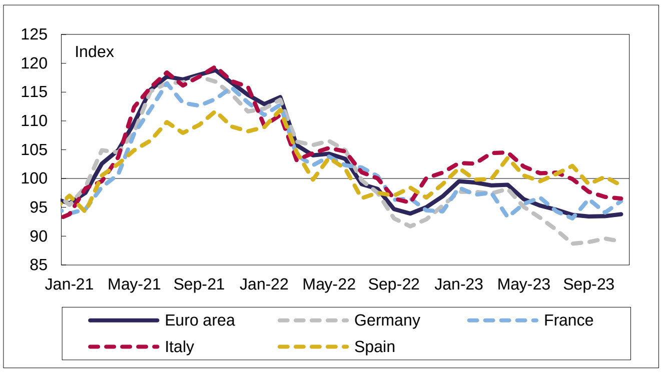
Services and retailer sentiment given a modest boost, but manufacturers increasingly gloomy

Within the sectoral detail for the euro area, there was a further modest improvement in services sentiment in November to the highest since July as firms reported a first pickup in demand in seven months. Retailers were also somewhat less downbeat amid some stabilisation in recent sales and an anticipated pickup in demand in the run up to Christmas. And while retailers' inventories were still considered to be historically elevated, they were judged to have fallen very slightly for the first month in seven. The pickup in retail sentiment tallied with the improvement in consumer confidence to a three-month high, with recent spending on big-ticket items reportedly the strongest since May 2022. Nevertheless, with households seemingly preferring to save rather than spend additional income, purchase intentions for the year ahead remained historically weak. Perhaps most surprising in today's survey was the modest upturn in construction sentiment, with the respective index suggesting that firms were the least pessimistic since July. But while they reported a rise in building activity in November, the respective index was still well below the average in the five years before the pandemic. Moreover, giving the substantial increase in borrowing costs over the past couple of years, thin order books and declining house prices, the challenges in the sector will remain substantive for a while to come. Finally, industrial sector sentiment worsened to the second-lowest level since August 2020, with a notable downturn reported among auto and clothing manufacturers. And with firms even gloomier gloomy about the outlook for production and exports as orders continued to decline, they signalled their intentions to cut headcount further into the New Year. Services firms also planned to scale back the pace of hiring over the near term and retailers intended to cut back on staffing levels too. As such, in aggregate, firms' employment expectations were the lowest since April 2021.

The day ahead in the euro area

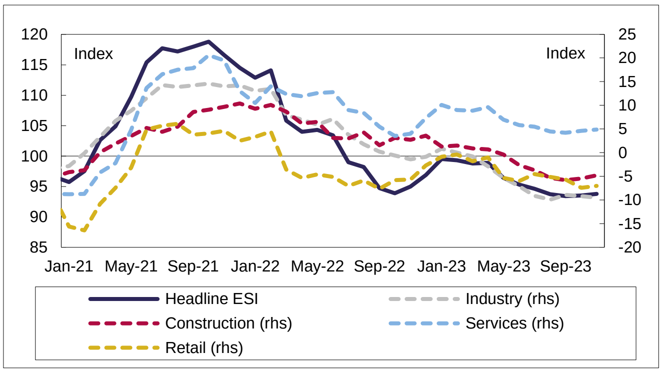
The data focus on Thursday will remain on inflation in November, with the flash euro area figures due along with those from France and Italy. Given today's results from Germany, Spain and certain other member states, we maintain our forecast of a drop of 0.3ppt in the headline euro area inflation rate to a 28-month low of 2.6%Y/Y. Core inflation (excluding all food and energy) also looks likely to decline by at least 0.3ppt, to 3.9%Y/Y, which would be the lowest since June 2022. Euro area unemployment figures for October are also due, with the headline rate expected to remain unchanged at 6.5%, just 0.1ppt above the series low reached in the summer. German figures for jobless claims in November and retail sales in October are among the other data due from the member states. Following four successive declines, German retail sales volumes are likely to have risen last month, although the expected modest increase would fail to reverse the drop of 0.6%M/M in September let alone the cumulative fall of more than 2.0% since June. But while German jobless claims are expected to rise for a tenth successive month in November, the claimant count rate is expected to remain steady at 5.8%, 0.3ppt above the level a year earlier.

Euro area: Economic sentiment indices, by country



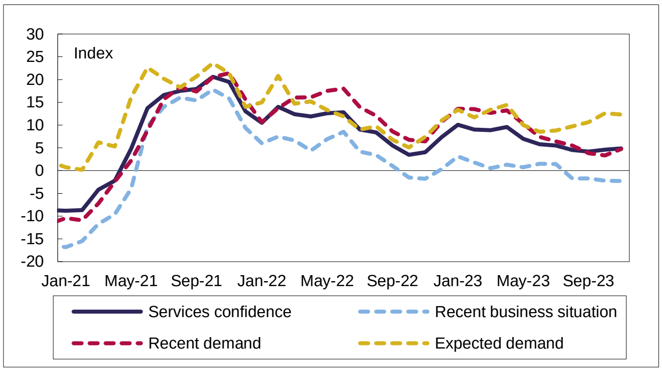
Source: EC, Macrobond and Daiwa Capital Markets Europe Ltd.

Euro area: Economic sentiment indices, by sector



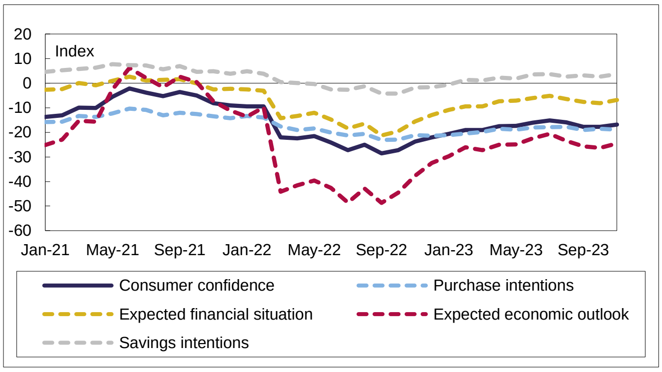
Source: EC, Macrobond and Daiwa Capital Markets Europe Ltd.

Euro area: Services sentiment indices



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

Euro area: Consumer confidence indices



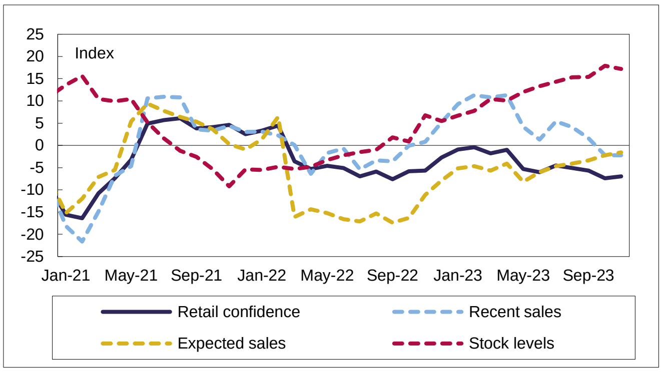
Source: EC,Macrobond and Daiwa Capital Markets Europe Ltd.

UK

The day ahead in the UK

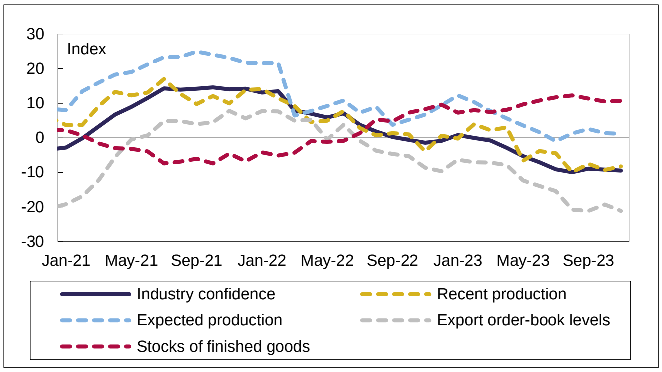
In the UK, the November results of the BoE's Decision-Maker Panel business survey are due. In last month's release, the trend in business inflation expectations remained broadly favourable despite some volatility in the single-month figures. On a three-month basis, firms' expectation for the rate of increase in their own prices over the coming twelve months fell 0.3ppt to 4.5%, the lowest on the (admittedly short) survey. One-year ahead CPI inflation expectations in the three months to October fell 0.3ppt to 4.6%, the lowest since November 2021. And the equivalent three-years ahead measure fell 0.1ppt to a series low of 3.1%Y/Y. However, wage growth expectations remained sticky and elevated.

Euro area: Retail sentiment indices



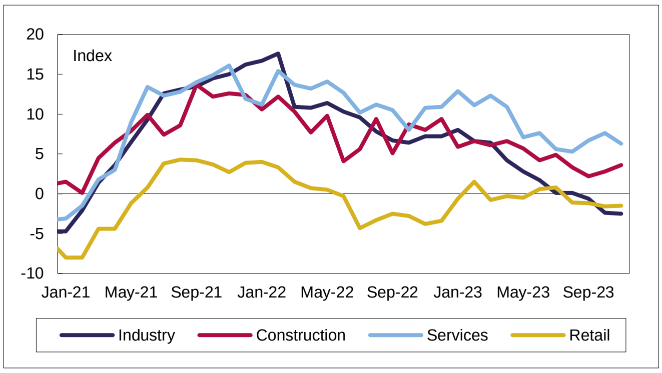
Source: EC, Macrobond and Daiwa Capital Markets Europe Ltd.

Euro area: Industry sentiment indices



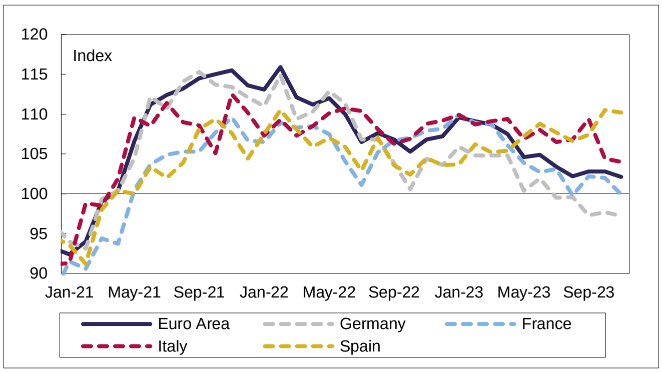
Source: EC, Macrobond and Daiwa Capital Markets Europe Ltd.

Euro area: Employment intentions indices



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

Euro area: Employment intentions indices



Source: EC, Macrobond 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		European Commission economic sentiment index	Nov	**93.8**	93.5	93.3	93.5
		European Commission industrial (services) confidence index	Nov	**-9.5 (4.9)**	-9.0 (4.2)	-9.3 (4.5)	-9.2 (4.6)
		European Commission final consumer confidence index	Nov	**-16.9**	*-16.9*	-17.8	-
Germany		Preliminary HICP (CPI) Y/Y%	Nov	**2.3 (3.2)**	2.7 (3.5)	3.0 (3.8)	-
Italy		ISTAT business (manufacturing) confidence index	Nov	**103.4 (96.6)**	- (96.0)	103.0 (96.0)	- (96.4)
		ISTAT consumer confidence index	Nov	**103.6**	102.0	101.6	-
Spain		Preliminary HICP (CPI) Y/Y%	Nov	**3.2 (3.2)**	3.7 (3.7)	3.5 (3.5)	-
		Retail sales Y/Y%	Oct	**5.0**	-	6.5	6.3
UK		Net consumer credit £bn (Y/Y%)	Oct	**1.3 (8.1)**	1.5 (-)	1.4 (8.0)	-
		Net mortgage lending £bn (mortgage approvals '000s)	Oct	**-0.1 47.4)**	0.4 (45.8)	-0.9 (43.3)	-1.0 (43.7)

Auctions

Country		Auction
Germany		sold €2.82bn of 2.6% 2033 bonds at an average yield of 2.45%
Italy		sold €3.0bn of 4.1% 2029 bonds at an average yield of 3.61%
		sold €3.5bn of 4.2% 2034 bonds at an average yield of 4.17%
		sold €1.0bn of floating-rate 2026 bonds at an average yield of 4.43%
UK		sold £4.25bn of 3.5% 2025 bonds at an average yield of 4.554%

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

Tomorrow's releases

Economic data

Country		GMT	Release	Period	Market consensus/ *Daiwa forecast*	Previous
Euro area		10.00	Preliminary HICP (core HICP) Y/Y%	Nov	*2.6 (3.9)*	2.9 (4.2)
		10.00	Unemployment rate %	Oct	6.5	6.5
Germany		07.00	Retail sales M/M% (Y/Y%)	Oct	0.4 (-2.5)	-0.6 (-4.4)
		08.55	Unemployment change '000s (rate %)	Nov	22.5 (5.8)	30.0 (5.8)
France		07.45	Preliminary HICP (CPI) Y/Y%	Nov	4.1 (3.7)	4.5 (4.0)
		07.45	Consumer spending M/M% (Y/Y%)	Oct	-0.2 (-0.2)	0.2 (-3.0)
		07.45	PPI Y/Y%	Oct	-	-1.7
		07.45	Final GDP Q/Q% (Y/Y%)	Q3	*0.1 (0.7)*	0.6 (1.1)
Italy		10.00	Preliminary HICP (CPI) Y/Y%	Nov	1.1 (1.0)	1.8 (1.7)
UK		00.01	Lloyds business barometer	Nov	35	39
		09.30	DMP 3M output price (1Y CPI) expectations 3M/Y%	Nov	-	4.5 (4.6)

Auctions and events

Country		GMT	Event
Euro area		15:30	ECB President Lagarde speaks at ECB Forum on banking supervision

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

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