

Euro wrap-up

Overview

- Despite a bigger-than-expected pickup in euro area consumer confidence, Bunds made gains while construction output maintained its downtrend.
- Gilts outperformed as UK consumer price inflation fell further than expected in November.
- Thursday will bring the latest INSEE French business survey results and UK public finances data while the ISTAT Italian sentiment indices and UK retail sales figures are due Friday.

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Daily bond market movements

Bond	Yield	Change
BKO 3.1 12/25	2.462	-0.043
OBL 2.4 10/28	1.951	-0.044
DBR 2.6 08/33	1.975	-0.038
UKT 3½ 10/25	4.079	-0.157
UKT 4½ 06/28	3.510	-0.142
UKT 3¼ 01/33	3.539	-0.105

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

Source: Bloomberg

Euro area

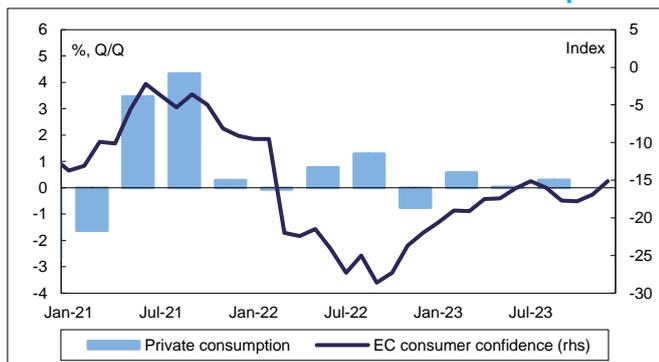
Consumer confidence up more than expected to highest since Russia's invasion of Ukraine

According to today's flash estimate, the European Commission's euro area consumer confidence index improved in December for a second successive month, rising a larger-than-expected 1.8pts in December to -15.1, to match July's reading and be the joint-highest since the Russian invasion of Ukraine in February 2022. There was no detail published by the Commission with today's flash estimate. But the few national survey results available so far, also published today, provided cause for cautious optimism about the near-term outlook for personal spending. In Germany, the GfK headline index – presented as a forecast for January – rose for a second successive month to a seven-month high. The detail suggested that expectations for the broader economy as well as households' own incomes were the most upbeat since July. And most encouragingly, and probably reflecting the boost from slowing inflation, consumers' willingness to make major purchases rose to the best since March 2022. Meanwhile, in the Netherlands, consumer confidence rose to the highest since January 2022, with willingness to spend the best since the Russian invasion of Ukraine. And tallying with the euro area figure, Belgian confidence was the highest since February 2022, with the survey detail similarly reporting improved perceptions of the outlook for the economy and personal finances. So, today's survey results suggest that, as in Q3 when it rose 0.3%Q/Q, private consumption should provide the main impetus to GDP growth over coming quarters as increased real disposable incomes provide greater scope to spend.

Construction output on track for another drop in Q4 amid gloomy house-builder sentiment

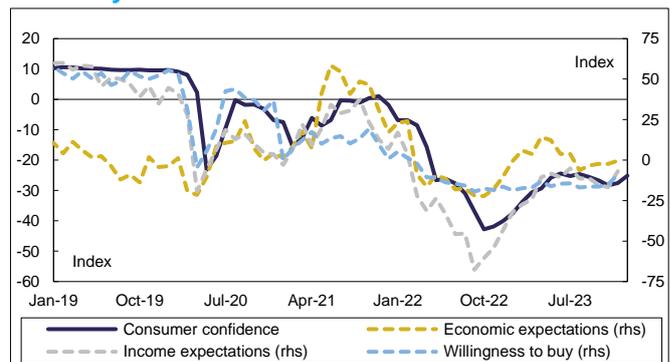
In marked contrast to private consumption, construction investment, which dropped for the fourth successive quarter and by 0.9%Q/Q in Q3, looks set to continue to contract over the near term as high interest rates continue to bite. Today's figures reported that euro area construction sector output dropped 1.0%M/M in October to a ten-month low, some 0.7% below the Q3 average to be on track for another quarterly decline. The declines in Germany (-2.1%M/M) and France (-3.3%M/M) were particularly marked. While building work and civil engineering activity in the euro area fell at a similar pace in October, there remain significant differences in conditions between the two subsectors. While civil engineering output remains well above the pre-pandemic level supported in part by NGEU projects, the opposite is true for building work, which has weakened significantly as both residential and commercial real estate prices trend lower. With building permits and new orders falling as an increasing share of borrowers look to reset mortgages at higher interest rates over coming quarters, surveys unsurprisingly suggest that sentiment among house-builders remains very weak. Building firms are also therefore signalling a desire to cut headcount. Indeed, according to the French Builders Federation (FFB), constructors in the euro area's second largest economy expect output to fall 5.5%Y/Y in 2024 at the expense of 90k jobs. With some other member states likely to be harder hit than France, the overall drop to euro area employment from the building sector is likely to be substantive.

Euro area: Consumer confidence & consumption



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

Germany: Consumer confidence



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

The coming two days in the euro area

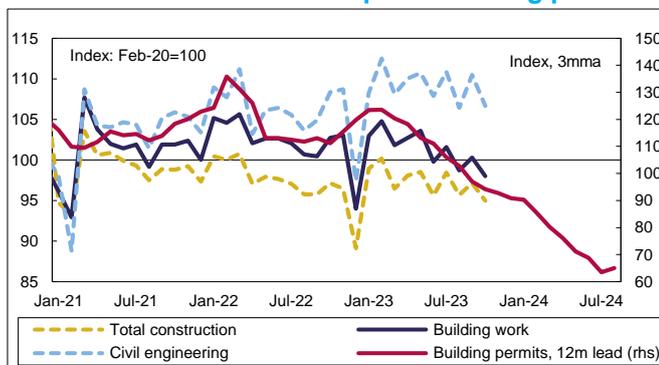
The run-up to Christmas will be relatively quiet for top-tier economic data from the euro area. Thursday will bring the French INSEE business climate survey results for December with the equivalent Italian ISTAT sentiment indices due on Friday. Both surveys will provide a cross-check to the [downbeat flash PMIs](#) for December, which suggested a renewed weakening of momentum heading towards year-end. We note that the INSEE survey often provides a more reliable guide to conditions in the French economy than the PMIs. But the headline business confidence index fell below the long-run average in October, deteriorated further in November to a 33-month low consistent with stagnation, and is not expected to improve in December. While the ISTAT headline Economic Sentiment Index also dropped in November to the lowest level since the first half of 2021, it was nevertheless above the long-run average and consistent with positive Italian GDP growth in Q4.

UK

Inflation drops well below BoE projection with broad-based moderation in core items

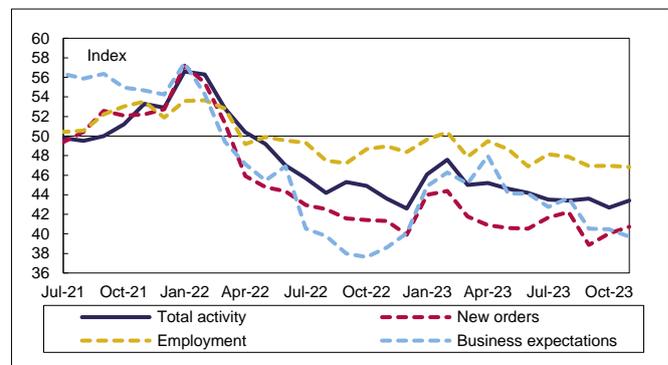
Consumer price inflation fell much further than expected in November, with the headline CPI rate declining 0.7ppt to 3.9%Y/Y, the lowest since September 2021. That was 0.4ppt below the median forecast on the Bloomberg survey, and a whopping 0.7ppt below the BoE's projection published only last month. Encouragingly too, the decline in inflation was highly broad-based, with significant moderation in the core components. Most importantly for the MPC, with prices falling more than the norm for the month in the two decades ahead of the pandemic, services inflation slowed 0.3ppt to 6.3%Y/Y, the softest since January and 0.6ppt below the BoE's forecast. Some of that decline reflected typically volatile items such as airfares and cultural services, such as theatre and live music ticket prices. But restaurant inflation slowed to the lowest in more than a year, while the insurance component eased to a six-month low. Meanwhile, prices of non-energy industrial goods fell 0.5%M/M, the most in any November for more than two decades, pushing the annual rate down 1.0ppt to 3.3%Y/Y, the lowest since September 2021. Once again, the downwards pressure was broad-based, with significant declines in a wide range of items from clothing and footwear to furniture and household goods and second-hand cars. Reassuringly perhaps, discounting was not limited to Black Friday specials, with the ONS collecting its data ten days before that event. And as a result, core CPI inflation fell 0.6ppt to a 22-month low of 5.1%Y/Y, 0.5ppt below the median forecast on the Bloomberg survey.

Euro area: Construction output & building permits



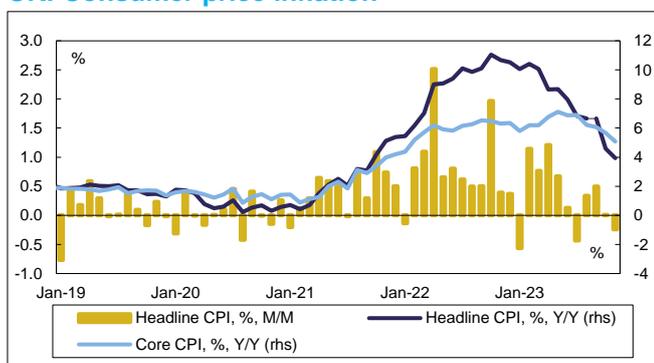
Source: Refinitiv Datastream and Daiwa Capital Markets Europe Ltd.

Euro area: Selected construction PMIs



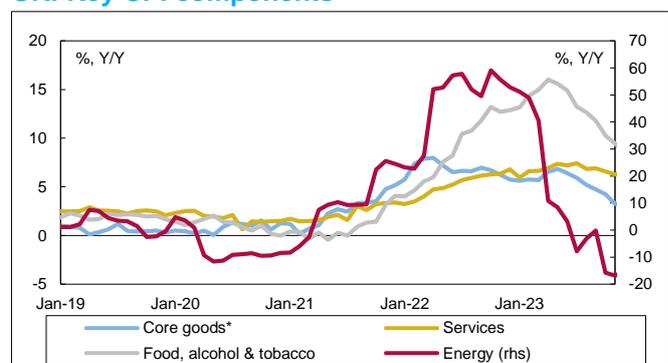
Source: S&P Global, Macrobond and Daiwa Capital Markets Europe Ltd.

UK: Consumer price inflation



Source: Refinitiv Datastream and Daiwa Capital Markets Europe Ltd.

UK: Key CPI components



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

Producer price data point to ongoing consumer goods disinflation over coming months

Beyond the core items, disinflation of food and related items continued, with the annual rate slowing 0.9ppt to a 17-month low of 9.4%Y/Y thanks not least to falling prices of bread and cakes and a moderation in inflation of other staples. In addition, with petrol prices down 2.6%M/M, energy inflation dropped by 1.2ppt to a new series low of -16.9%Y/Y. Looking ahead, prices of auto fuel might well pose upside risks due to events in the Red Sea. And a 5% increase in the regulated household energy price cap will add to inflation in January. However, given recent developments in wholesale markets, household electricity and gas bills might well be cut 10% in April, which could sustain energy inflation in negative territory throughout the year. Meanwhile, today's PPI data reported a further drop in food product inflation to just 2.1%Y/Y, the lowest since March 2021. And core output producer goods inflation slowed to just 0.2%Y/Y, the lowest since 2020. So, even if retailers pause discounting in the run-up to Christmas, non-energy goods inflation should fall steadily further into the New Year.

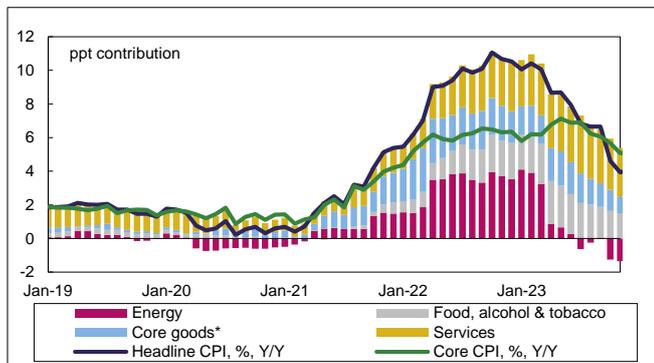
Services inflation to tick higher in New Year before resuming downtrend despite firm wage growth

Of course, services inflation will be most important for the path of monetary policy. Despite today's much lower-than-expected figures, certain items within this component will likely receive a further positive impulse from indexation in the New Year. And still-elevated growth in average [weekly labour earnings](#) (7.3%3M/Y excluding bonuses in October), even stronger increases in the National Living Wage set to be implemented in April, and significant uncertainty about the tightness of the labour market will maintain BoE concerns about services inflation persistence over coming months. However, recent pay momentum and survey indicators all point to a moderation in wage growth into the New Year. And the extent of pass-through of unit labour cost growth to services inflation will likely be restrained by subdued demand. So, while we project a rebound in services inflation back above 7.0%Y/Y in January, we also expect a firm downtrend to resume thereafter, to remain firmly below the path projected by the BoE last month. Indeed, services inflation should fall below 5.0%Y/Y on Q224 and further in the second half of 2024 and into 2025.

Downside surprise supports case for first rate cut in mid-24 despite persistence concerns

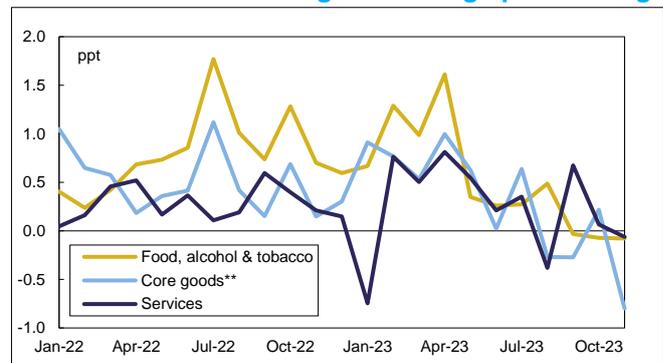
Of course, both headline and core inflation in the UK remains firmly above rates in the other G7 economies. And given the hit to product market competition and labour market flexibility from Brexit, as well as the impact of record National Health Service waiting lists on labour market inactivity, there are reasons to believe that the risks of inflation persistence will be greater in the UK than its peers too. But with core goods and services inflation likely to moderate beyond the New Year, we project core CPI inflation to fall below 3.0%Y/Y in Q224 and 2½%Y/Y in Q324. And while a decline in headline inflation to below 2.0%Y/Y in Q224 would be a temporary response to base effects and a sharp cut in the household energy price cap in April, we project it to remain below 2½%Y/Y in Q324, roughly 1ppt below the BoE's current baseline projection for that

UK: Contributions to CPI inflation



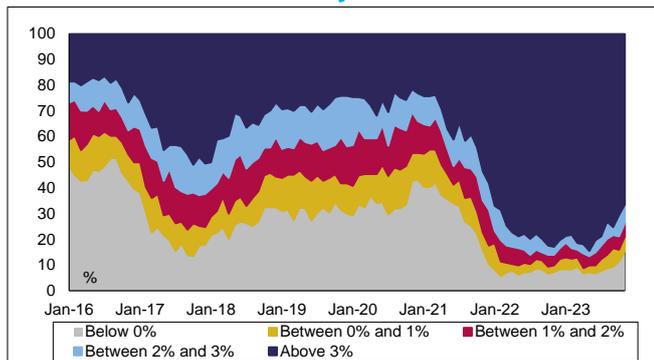
*Non-energy industrial goods. Source: Refinitiv Datastream and Daiwa Capital Markets Europe Ltd.

UK: Deviations from long-run average price change*



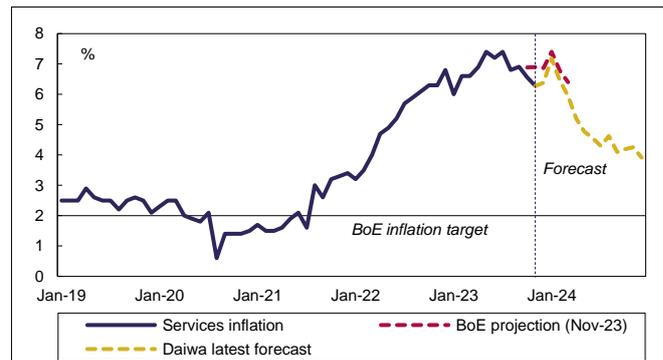
*Pre-Covid long-run average for the respective month. **Non-energy industrial goods. Source: Refinitiv Datastream & Daiwa Capital Markets Europe Ltd.

UK: Share of CPI basket by inflation rate



Source: Refinitiv Datastream and Daiwa Capital Markets Europe Ltd.

UK: Services inflation forecasts



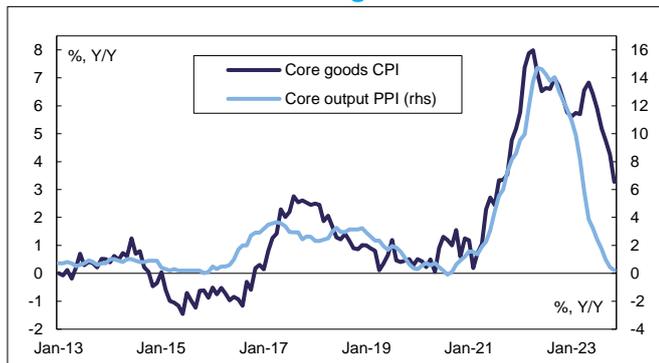
Source: BoE, Refinitiv Datastream and Daiwa Capital Markets Europe Ltd.

quarter. So, we would expect the BoE to project that both headline and core inflation will be back to 2.0%Y/Y or below in 2025. And notwithstanding the likelihood of a further politically-motivated easing of fiscal policy in the spring, we maintain our expectation of a first rate cut in August and steady further easing thereafter. Indeed, not least as Bank Rate is currently well above any reasonable estimate of neutral, and real interest rates will otherwise steadily rise as and when inflation continues to decline, we see the risks skewed to an earlier first rate cut, in May.

The coming two days in the UK

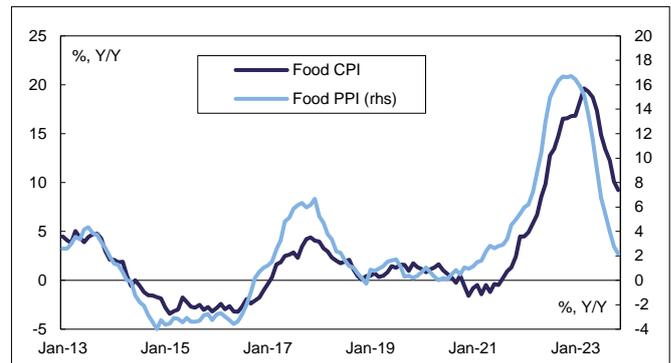
The most notable UK data to be published before Christmas will be the November retail sales report on Friday. Having declined for a third month in the past four and by 0.3%M/M in October, retail sales are expected to rebound by less than ½%M/M in November to be down more than 1.0%Y/Y and be trending more than ½% below the Q3 average. Final national accounts for Q3 are also due on Friday and should confirm that GDP moved sideways from Q2 last quarter. Ahead of those data, Thursday will bring the November public finances data and the CBI's distributive trades survey results for December.

UK: Producer & consumer goods inflation*



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

UK: Producer & consumer food inflation



Source: Refinitiv Datastream and Daiwa Capital Markets Europe Ltd.



The next edition of the Euro wrap-up will be published on 2 January 2024



Daiwa economic forecasts

	2023		2024				2023	2024	2025
	Q3	Q4	Q1	Q2	Q3	Q4			
GDP	%, Y/Y								
Euro area	0.1	-0.1	0.1	0.2	0.2	0.2	0.7	0.3	1.0
UK	0.0	0.1	0.1	0.1	0.1	0.2	0.5	0.3	0.7
Inflation, %, Y/Y									
Euro area									
Headline HICP	5.0	2.7	2.5	2.1	1.7	2.3	5.4	2.2	1.8
Core HICP	5.1	3.7	2.7	1.8	1.5	1.9	4.9	1.9	1.6
UK									
Headline CPI	6.7	4.2	3.7	1.9	2.1	2.5	7.3	2.5	2.1
Core CPI	6.4	5.3	4.5	2.8	2.4	2.6	6.2	3.0	2.1
Monetary policy, %									
ECB									
Refi Rate	4.50	4.50	4.25	4.00	3.75	3.50	4.50	3.50	2.75
Deposit Rate	4.00	4.00	3.75	3.50	3.25	3.00	4.00	3.00	2.25
BoE									
Bank Rate	5.25	5.25	5.25	5.25	5.00	4.50	5.25	4.50	2.75

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

European calendar

Today's results

Economic data

Country	Release	Period	Actual	Market consensus/ <i>Daiwa forecast</i>	Previous	Revised
Euro area	 EU27 new car registrations Y/Y%	Nov	6.7	-	14.6	-
	 Preliminary consumer confidence index	Dec	-15.1	-16.3	-16.9	-
	 Construction output M/M% (Y/Y%)	Oct	-1.0 (-0.7)	-	0.4 (-0.3)	0.7 (-)
Germany	 PPI Y/Y%	Nov	-7.9	-7.5	-11.0	-
	 GfK consumer confidence index	Jan	-25.1	-27.0	-27.8	-27.6
UK	 Headline CPI (core CPI) Y/Y%	Nov	3.9 (5.1)	<u>4.4 (5.6)</u>	4.6 (5.7)	-
	 PPI output (input) Y/Y%	Nov	-0.2 (-2.6)	-0.5 (-3.0)	-0.6 (-2.6)	-0.3 (-)
	 House price index Y/Y%	Oct	-1.2	-	-0.1	-0.6

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

The coming days' releases

Country	GMT	Release	Period	Market consensus/ <i>Daiwa forecast/actual</i>	Previous
Thursday 21 December 2023					
France	 07.45	INSEE business sentiment indicator	Dec	97	97
	 07.45	INSEE manufacturing confidence (production outlook)	Dec	98 (-)	99 (-11)
	 -	Bank of France retail sales* Y/Y%	Nov	-	-2.8
Italy	 10.00	PPI Y/Y%	Nov	-	-12.4
UK	 00.01	Lloyds business barometer	Dec	-	42
	 07.00	Public sector next borrowing (excl banks) £bn	Nov	13.0 (13.0)	14.0 (14.9)
	 11.00	CBI reported retail sales balance	Dec	-14	-11
Friday 22 December 2023					
France	 07.45	PPI Y/Y%	Nov	-	-1.2
Italy	 09.00	ISTAT business (manufacturing) sentiment indicator	Dec	- (96.9)	103.4 (96.6)
	 09.00	ISTAT consumer confidence index	Dec	104.0	103.6
Spain	 08.00	Final GDP Q/Q% (Y/Y%)	Q3	<u>0.3 (1.8)</u>	0.5 (2.0)
UK	 07.00	Final GDP Q/Q% (Y/Y%)	Q3	0.0 (0.6)	0.2 (0.6)
	 07.00	Retail sales including auto fuels M/M% (Y/Y%)	Nov	0.4 (-1.3)	-0.3 (-2.7)
	 07.00	Retail sales excluding auto fuels M/M% (Y/Y%)	Nov	0.3 (-1.4)	-0.1 (-2.4)

*Approximate date of release. Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

The coming two weeks' data calendar

The coming few week's key data releases

Country	GMT	Release	Period	Market consensus/ <i>Daiwa</i> <i>forecast/actual</i>	Previous	
Monday 25-Tuesday 26 December 2023						
- Nothing scheduled -						
Wednesday 27 December 2023						
Germany		-	Retail sales* M/M% (Y/Y%)	Nov	-	1.2 (0.1)
Thursday 28 December 2023						
- Nothing scheduled -						
Friday 29 December 2023						
Spain		08.00	Preliminary HICP (CPI) Y/Y%	Dec	-	3.3 (3.2)
UK		07.00	Nationwide house price index M/M% (Y/Y%)	Dec	-	0.2 (-2.0)
Monday 01 January 2024						
- Nothing scheduled -						
Tuesday 02 January 2024						
Euro area		09.00	M3 money supply Y/Y%	Nov	-	-1.0
		09.00	Final manufacturing PMI	Dec	<u>44.2</u>	44.2
Germany		08.55	Final manufacturing PMI	Dec	<u>43.1</u>	42.6
France		08.50	Final manufacturing PMI	Dec	<u>42.0</u>	42.9
		-	New car registrations* Y/Y%	Dec	-	14.0
Italy		08.45	Manufacturing PMI	Dec	-	44.4
		17.00	New car registrations Y/Y%	Dec	-	16.2
Spain		08.15	Manufacturing PMI	Dec	-	46.3
		-	New car registrations* Y/Y%	Dec	-	7.0
UK		00.01	BRC shop price index Y/Y%	Dec	-	4.3
		09.30	Final manufacturing PMI	Dec	<u>46.4</u>	47.2
Wednesday 03 January 2024						
Germany		08.55	Unemployment change '000s (rate %)	Dec	-	22.0 (5.9)
Spain		08.00	Unemployment change '000s	Dec	-	-24.6
Thursday 04 January 2024						
Euro area		09.00	Final services (composite) PMI	Dec	<u>48.1 (47.0)</u>	48.7 (47.6)
Germany		08.55	Final services (composite) PMI	Dec	<u>48.4 (46.7)</u>	49.6 (47.8)
		13.00	Preliminary HICP (CPI) Y/Y%	Dec	-	2.3 (3.2)
France		08.50	Final services (composite) PMI	Dec	<u>44.3 (43.7)</u>	45.4 (44.6)
		07.45	Preliminary HICP (CPI) Y/Y%	Dec	-	3.9 (3.5)
Italy		08.45	Services (composite) PMI	Dec	-	49.5 (48.1)
Spain		08.15	Services (composite) PMI	Dec	-	51.0 (49.8)
UK		09.30	Final services (composite) PMI	Dec	<u>52.7 (51.7)</u>	50.9 (50.7)
		09.30	Net consumer credit £bn (Y/Y%)	Nov	-	1.3 (8.1)
		09.30	Net mortgage lending £bn (approvals '000s)	Nov	-	-0.1 (47.4)
		09.30	BoE's DMP 1Y CPI expectations Y/Y%	Dec	-	4.4
Friday 05 January 2024						
Euro area		08.30	Construction PMI	Dec	-	43.4
		10.00	Headline HICP (core HICP) Y/Y%	Dec	<u>2.9 (3.5)</u>	2.4 (3.6)
		10.00	PPI Y/Y%	Nov	-	-9.4
Germany		08.30	Construction PMI	Dec	-	36.2
France		08.30	Construction PMI	Dec	-	44.6
Italy		10.00	Preliminary HICP (CPI) Y/Y%	Dec	-	-0.6 (0.7)
		08.30	Construction PMI	Dec	-	52.9
UK		09.00	New car registrations Y/Y%	Dec	-	9.5
		09.30	Construction PMI	Dec	-	45.5

*Approximate date of release. Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

The coming two weeks' key events & auctions

Country	GMT	Event / Auction
Thursday 21 December – Tuesday 02 January 2024		
- Nothing scheduled -		
Wednesday 03 January 2024		
Germany 	10.30	Auction: 2Y bonds
Thursday 04 January 2024		
France 	09.50	Auction: Bonds with various maturities
Spain 	09.30	Auction: Bonds with various maturities
UK 	09.30	BoE publishes its Decision Maker Panel data – December 2023
	10.00	Auction: 3.75% 2038 bonds
Friday 05 January 2024		
- Nothing scheduled -		

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

Access our research blog at:

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