

# Euro wrap-up

## Overview

- Bunds made losses as euro area GDP narrowly avoided a second successive quarterly contraction in Q4 and the Commission survey suggested a pickup in inflation expectations in January.
- Gilts also made losses despite a sharp drop in a UK survey measure of inflation in January.
- Wednesday will bring the flash estimates of January inflation in Germany and France

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### Daily bond market movements

Bond	Yield	Change
BKO 3.1 12/25	2.510	-
OBL 2.1 04/29	2.165	+0.044
DBR 2.2 02/34	2.271	+0.039
UKT 3½ 10/25	4.318	+0.079
UKT 4½ 06/28	3.854	+0.056
UKT 3¼ 01/33	3.901	+0.030

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

## Euro area

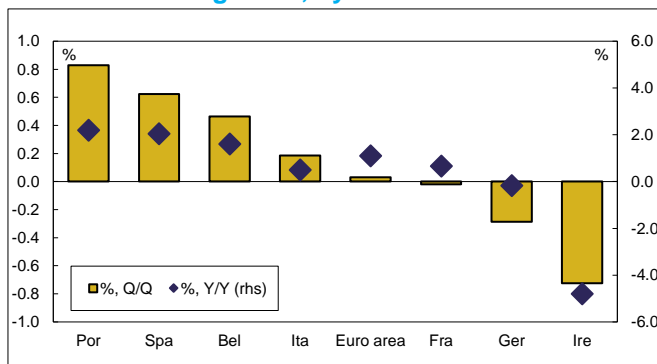
### Euro area avoids a technical recession, but economy merely stagnating

The first estimate of euro area GDP in Q4 marginally beat expectations, suggesting that a technical recession had been avoided. However, the figures merely confirmed zero growth in the fourth quarter, implying that the economy broadly stagnated over the past five quarters, as demand was hit first by the region's energy-price shock and then subsequently by the ECB's aggressive monetary tightening. So, while euro area economic output in Q423 remained some 3% above the pre-pandemic level, it continued to lag significantly behind the recovery in the US, where the level of GDP last quarter stood more than 8% above the Q419 benchmark. Today's release also highlighted the contrast between the weakness of the two largest core member states and the expansions at the southern periphery. Indeed, Destatis confirmed that German GDP contracted 0.3%Q/Q in Q4, leaving it down 0.2%Y/Y and strikingly just 0.1% above the pre-pandemic level. And the French economy also failed to grow last quarter. While the modest contraction in France in Q3 was revised away, Q4 marked the fourth quarter out of the past five to record zero growth, to leave the level of output just 1.8% higher than four years ago. Meanwhile, Italian GDP grew a stronger-than-expected 0.2%Q/Q in Q4. And while this left output little changed compared with a year earlier, it was still some 3½% above the Q419 level. But the expansion in Q4 was strongest in the Iberian economies, where Spanish GDP rose for the fourteenth consecutive quarter, by 0.6%Q/Q, to leave it 2.9% above the Q419 level, while Portuguese GDP rose a stronger 0.8%Q/Q, to leave it some 5½% above the level four years ago.

### Positive contribution from net trade likely masks weakness in domestic demand

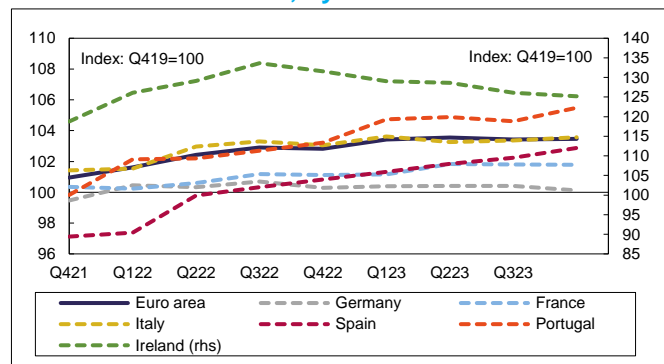
Eurostat will not publish an expenditure breakdown of euro area Q4 GDP until March. But the limited information published so far by the national authorities suggests that momentum in final domestic demand remained weak heading into year-end, with consumer spending constrained by the lasting impact of above-target inflation and fixed investment more acutely impacted by higher borrowing costs. And although net trade looks to have provided support to growth in many member states, this impact appears to have been partly offset by a drag from inventories as firms continued to run down stocks as work backlogs were used up and new orders fell. Certainly, Destatis reported that there was a marked decline in capex on machinery and equipment and construction. And French and Spanish fixed investment subtracted 0.2ppt and 0.4ppt from GDP growth in the respective member states. Household consumption provided no support to French GDP but rose 0.3%Q/Q in Spain, while government spending offered a modest boost in both countries. Inventories knocked a sizeable 1.1ppt off French GDP growth, but added a non-negligible 0.4ppt in Spain. However, both countries saw net trade contribute positively as imports fell sharply in France amid subdued domestic demand, while exports jumped in Spain. In Italy, finally, ISTAT reported that net trade made a positive contribution to GDP growth in Q4 but also that domestic demand fell.

### Euro area: GDP growth, by selected member state



Source: Macrobond and Daiwa Capital Markets Europe Ltd.

### Euro area: GDP levels, by selected member state



Source: Macrobond and Daiwa Capital Markets Europe Ltd.

## Commission ESIs signal ongoing stagnation with consumers less willing to make major purchases

Broadly consistent with the [flash PMIs](#), the Commission's business and consumer surveys suggest that there was no significant improvement in overall momentum at the start of the year. The euro area economic sentiment indicator (ESI) fell 0.1pt from December's seven-month high to 96.2, 1.5pt above the Q4 level and bang in line with the 2023 average, but 3.8% below the long-run norm and a level consistent with continued stagnation at best. While optimism in the services sector rose slightly to the best in a year, that reflected an improved assessment of recent business conditions and firms revised down their expectations for demand over the coming three months. Likewise, while manufacturers were also less downbeat in part due to a slightly less negative assessment of orders, production expectations were the weakest in six months. Meanwhile, confidence in retail and construction deteriorated again to well below the averages for both 2023 and the long run. And, on average, labour shortages were less of a restraint on activity in every sector and firms were the least inclined to increase headcount since April 2021. Moreover, in part as households were a little more downbeat about the outlook for their personal finances and the economy as a whole, the deterioration in consumer confidence flagged in the flash estimate was confirmed. And of additional concern, consumers' willingness to make major purchases over the coming twelve months dropped to the lowest since last February.

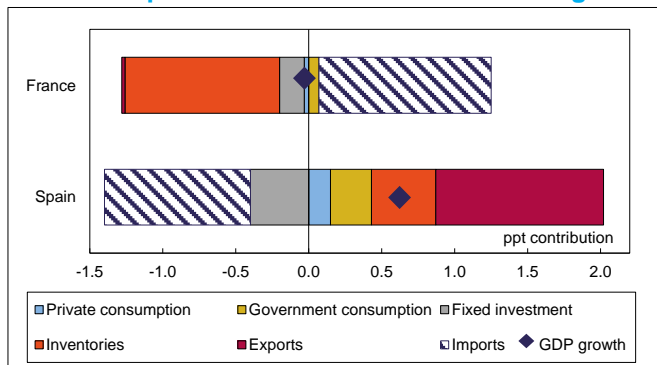
## Deterioration in sentiment concentrated in Germany, with confidence in Spain and Italy still firm

Like the GDP data, however, the headline euro area ESIs masked significant variation between the member states. The German sentiment index deteriorated almost 2½% on the month to a historically weak 89.8, a little more than 10% below the long-run average and below the averages of both Q3 and Q4, with each of the major sectors and households all more downbeat. In contrast, the ESIs for each of the other four largest member states picked up in January to the highest since the first half of last year. Also tallying with firmer economic output, and despite a deterioration in confidence among construction firms and consumers, Spain led the way, with its ESI a little more than 2½% above the long-run average. In terms of employment intentions too, Germany was similarly the only large country in which firms signalled a desire to cut headcount.

## Firms' and consumers' inflation expectations indices rise to multi-month highs

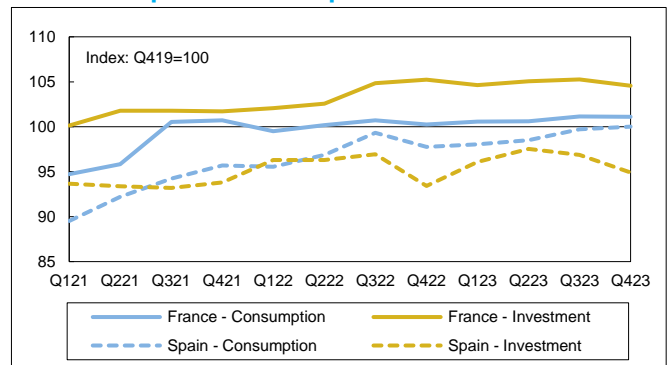
While the ESIs suggested that economic activity remains broadly stagnant, the Commission survey also indicated that price expectations picked up at the start of the year. Perhaps reflecting recognition that inflation likely ticked higher in January in response to the withdrawal of special government subsidies and tax cuts, the survey index of consumer price expectations for the coming twelve months rose for a second successive month to the highest since September and a level in line with the 2023 average. Moreover, price expectations for the coming three months in industry and construction rose to eight-month

### France & Spain: Contributions to Q423 GDP growth



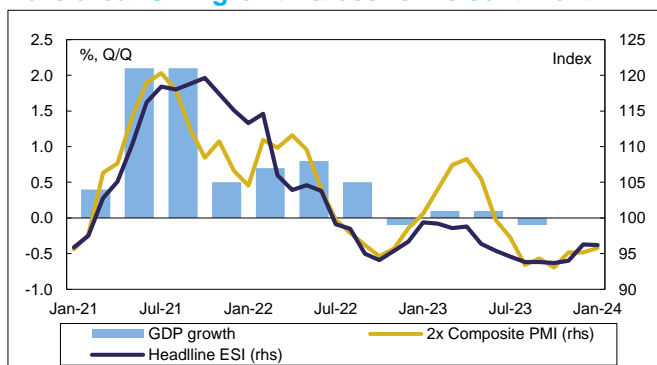
Source: Macrobond and Daiwa Capital Markets Europe Ltd.

### France & Spain: Consumption & fixed investment



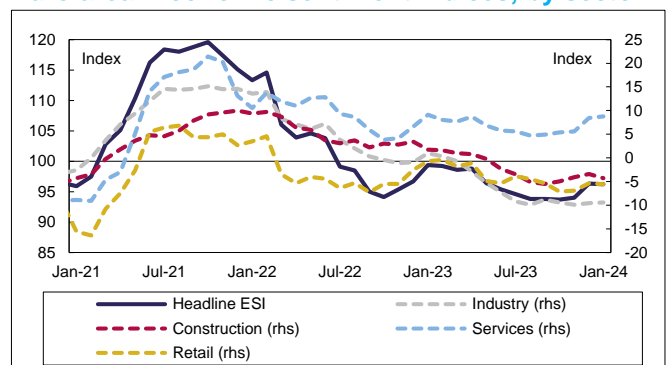
Source: Macrobond and Daiwa Capital Markets Europe Ltd.

### Euro area: GDP growth & economic sentiment



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

### Euro area: Economic sentiment indices, by sector



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

highs with the equivalent index for services the loftiest since March. However, likely in part reflecting the impact of soft demand, retail price expectations ticked up merely to a three-month high, well below the range in the two years to October. Only in industry were price-setting expectations below the long-run average. We note, however, that the ECB's household survey earlier this month reported a notable moderation in inflation expectations for the coming year and medium term.

## The day ahead in the euro area

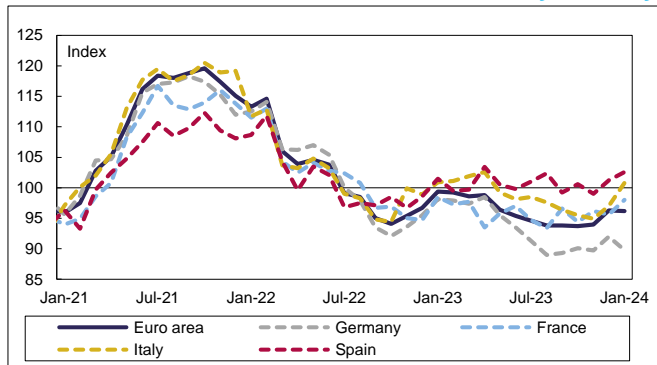
Ahead of the flash euro area January inflation estimates, tomorrow will bring the equivalent preliminary data from the two largest member states. Germany's headline harmonised HICP rate is expected to have partly reversed the jump in December (+1.5ppts) that was associated with base effects from the government's one-off energy support payment in December 2022, to be down ½ppt at 3.2%Y/Y. The French headline HICP rate is also expected to ease ½ ppt to 3.6%Y/Y, which would be the lowest since January 2022. Admittedly, these data are highly uncertain, not least as governments have continued to withdraw policy support to consumers and businesses, while the reweighting of the inflation basket to reflect the shift in consumption patterns last year is a further unknown. Today's Spanish figures saw the respective HICP rate unexpectedly rise 0.2ppt to 3.5%Y/Y, with Spain's statistical office noting that the increase in the national measure (up 0.3ppt to 3.4%Y/Y) reflected higher electricity prices amid the gradual reversal of energy tax cuts from the start of the year. In contrast, the national core measure (excluding fresh foods and energy) fell 0.2ppt to 3.9%Y/Y. Wednesday will also bring German retail sales figures for December and labour market numbers for January from the same member state.

## UK

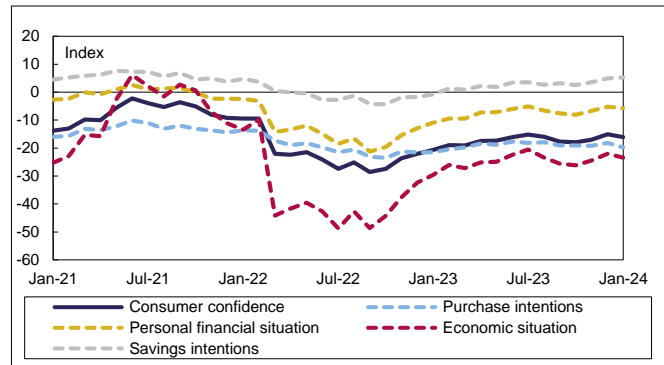
### BRC survey reports steepest drop in shop price inflation since 2008

According to the BRC, inflation on the UK high street has cooled significantly further at the start of 2024. After [sales fell in December](#) at the most since January 2021, and at the sharpest pace since the global financial crisis bar the pandemic, retailers appear to have heavily discounted goods during the New Year sales period in an attempt to attract custom. Overall, the BRC's shop price measure of inflation slowed in January by 1.4ppts – the most since December 2008 – to 2.9%Y/Y, the lowest since May 2022. Within the detail, the BRC's food inflation rate moderated 0.6ppt to 6.1%Y/Y, the softest since June 2022. And non-food inflation slowed 1.8ppts to just 1.3%Y/Y, the lowest since February 2022. According to the survey detail, discounting in clothing (down 4.7ppts -3.8%Y/Y) was particularly aggressive, while the inflation rate of electrical items returned to negative territory (-0.5%Y/Y) after a temporary jump the prior month and the furniture component dropped sharply (down 2.3ppts) to the lowest since 2021 (2.6%Y/Y). The BRC survey adds to evidence that, thanks to shift in the global balance of supply and demand, non-energy goods inflation will continue to ease in the January consumer price inflation data due on 14 February. However, due to increases in the services and energy components, the headline CPI

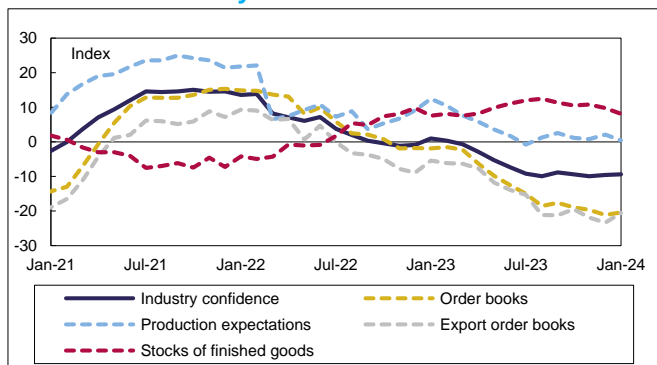
### Euro area: Economic sentiment indices, by country



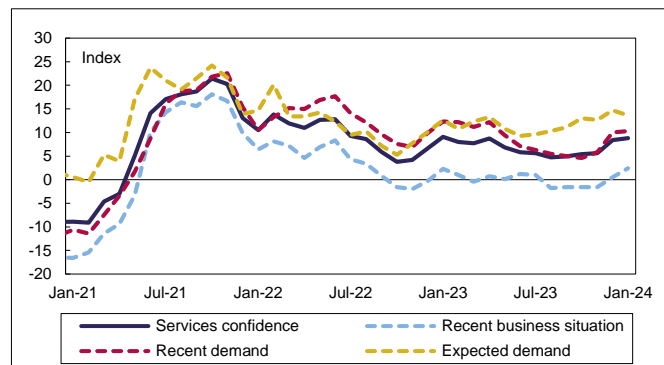
### Euro area: Consumer confidence



### Euro area: Industry sentiment indices



### Euro area: Services sentiment indices

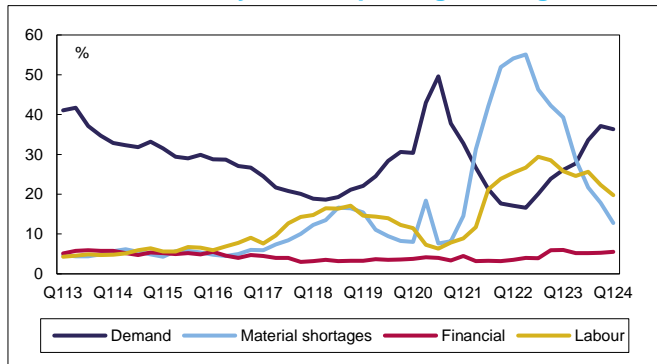


inflation rate probably rose temporarily in January. And the imposition of new Brexit-related border controls on imports of certain items from the EU and Northern Ireland into Great Britain from tomorrow will likely add to food inflation over coming months. But thanks not least to the prospect of a steep drop in household energy bills from April, as well as ongoing disinflation in non-energy goods and a more gradual dissipation of pressures in services, we expect CPI inflation to drop below 2.0%Y/Y in Q2.

### The day ahead in the UK

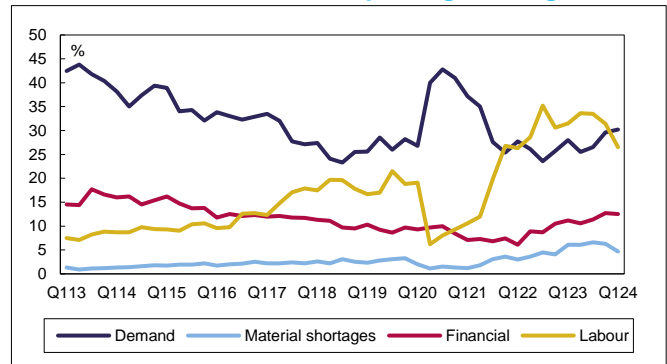
Tomorrow will bring the latest Nationwide house price report for January. The Bloomberg survey consensus is for a further modest pickup in house prices at the start of the year (0.1%M/M), reinforcing the view the bottom in the recent residential property market downturn has now been passed. Nevertheless, this would still leave prices down almost 1%Y/Y, with the recovery being restrained by high borrowing costs. Reflecting higher mortgage interest rates, today's BoE lending figures reported that households made the sixth net repayment (-£0.8bn) in the past ten months in December, to leave year-on-year growth in the stock of mortgage lending at zero for the first time since the series began in 1994. But, while still extremely elevated, the effective interest rate on new secured lending edged slightly lower for the first time November 2021. And the number of new mortgage approvals edged up to 50.5k in December, the most since June, albeit still some 16k below the pre-pandemic five-year average.

#### Euro area: Industry firms reporting limiting factors



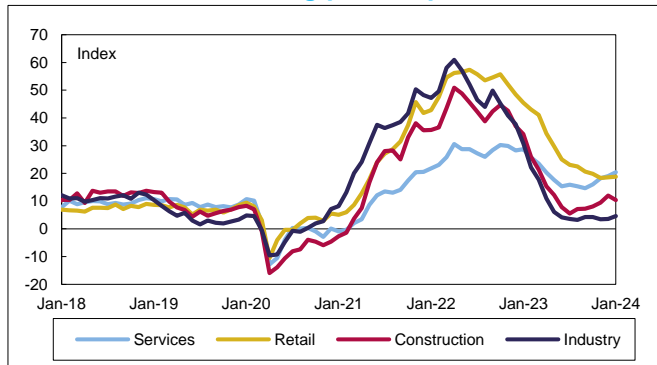
Source: EC, Macrobond and Daiwa Capital Markets Europe Ltd.

#### Euro area: Services firms reporting limiting factors



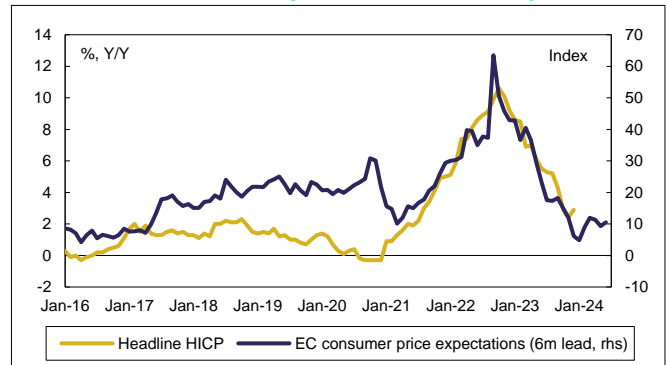
Source: EC, Macrobond and Daiwa Capital Markets Europe Ltd.

#### Euro area: Firms' selling price expectations\*



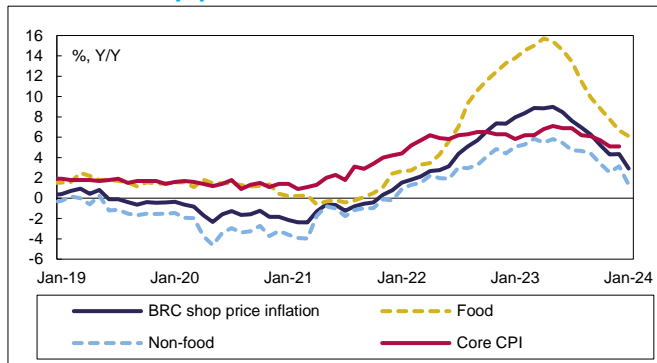
\*Three months ahead. Source: EC, Macrobond and Daiwa Capital Markets Europe Ltd.

#### Euro area: Consumer price inflation & expectations\*



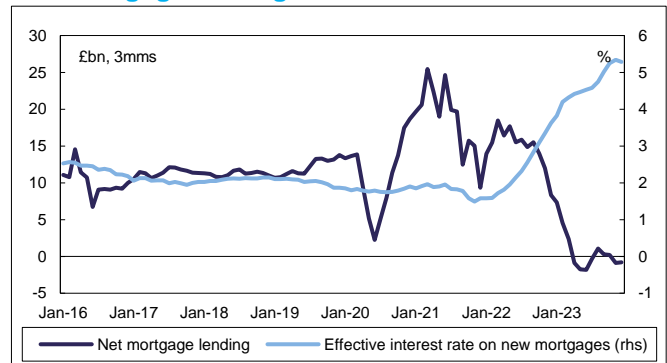
\*Twelve months ahead. Source: EC, Macrobond and Daiwa Capital Markets Europe Ltd.

#### UK: BRC shop price & CPI inflation



Source: Macrobond and Daiwa Capital Markets Europe Ltd.

#### UK: Mortgage lending & interest rate

















Source: Macrobond 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	 GDP – first estimate Q/Q% (Y/Y%)	Q4	<b>0.0 (0.1)</b>	<u>-0.1 (0.0)</u>	-0.1 (0.0)	-
	 European Commission's Economic Sentiment Indicator	Jan	<b>96.2</b>	96.4	96.4	96.3
	 European Commission's final consumer confidence indicator	Jan	<b>-16.1</b>	<u>-16.1</u>	-15.0	-
	 European Commission's industrial (services) confidence indicator	Jan	<b>-9.4 (8.8)</b>	-9.0 (8.1)	-9.2 (8.4)	-9.6 (-)
Germany	 GDP – first estimate Q/Q% (Y/Y%)	Q4	<b>-0.3 (-0.2)</b>	<u>-0.3 (-0.3)</u>	0.0 (-0.3)	-
France	 GDP – first estimate Q/Q% (Y/Y%)	Q4	<b>0.0 (0.7)</b>	<u>0.1 (0.7)</u>	-0.1 (0.6)	0.0 (-)
	 Consumer spending M/M% (Y/Y%)	Dec	<b>0.3 (1.3)</b>	0.0 (1.1)	0.7 (-1.1)	0.6 (-1.0)
Italy	 GDP – first estimate Q/Q% (Y/Y%)	Q4	<b>0.2 (0.5)</b>	<u>-0.1 (0.2)</u>	0.1 (0.1)	-
Spain	 GDP – first estimate Q/Q% (Y/Y%)	Q4	<b>0.6 (2.0)</b>	<u>0.2 (1.5)</u>	0.3 (1.8)	0.4 (1.9)
	 Preliminary HICP (CPI) Y/Y%	Jan	<b>3.5 (3.4)</b>	3.1 (2.7)	3.3 (3.1)	-
UK	 BRC shop price index Y/Y%	Jan	<b>2.9</b>	-	4.3	-
	 Net consumer credit £bn (Y/Y%)	Dec	<b>1.2 (8.5)</b>	-	2.0 (8.6)	2.1 (-)
	 Net mortgage lending £bn (approvals '000s)	Dec	<b>-0.8 (50.5)</b>	-	0.0 (50.1)	- (49.3)
	 M4 money supply M/M% (Y/Y%)	Dec	<b>0.5 (-0.9)</b>	-	-0.1 (-2.3)	-








#### Auctions

Country	Auction
Germany	 sold €4.13bn of zero-coupon 2026 bonds at an average yield of 2.49%
Italy	 sold €3.5bn of 4.1% 2029 bonds at an average yield of 3.14%
	 sold €1.5bn of 4.35% 2033 bonds at an average yield of 3.69%
	 sold €2.0bn of 3.35% 2035 bonds at an average yield of 3.85%
	 sold €2.0bn of 2031 floating-rate bonds at an average yield of 5.23%
UK	 sold £900mn of 0.125% 2051 index-linked bonds at an average yield of 1.333%


Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

### Tomorrow's releases

#### Economic data

Country	GMT	Release	Period	Market consensus/ <i>Daiwa forecast</i>	Previous
Germany	 07.00	Retail sales M/M% (Y/Y%)	Dec	0.5 (-1.2)	-2.2 (-1.5)
	 08.55	Unemployment change '000s (rate %)	Jan	12.5 (5.9)	5.0 (5.9)
	 13.00	Preliminary HICP (CPI) Y/Y%	Jan	3.2 (3.0)	3.8 (3.7)
France	 07.45	Preliminary HICP (CPI) Y/Y%	Jan	3.6 (3.2)	4.1 (3.7)
Spain	 08.00	Retail sales Y/Y%	Dec	-	5.2
UK	 00.01	Lloyds business barometer	Jan	-	35
	 07.00	Nationwide house price index M/M% (Y/Y%)	Jan	0.1 (-0.9)	0.0 (-1.8)

#### Auctions and events

Germany	 10.30	Auction: €4.5bn of 2.2% 2034 bonds
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Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

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