

Euro wrap-up

Overview

- As French President Macron consulted party leaders to try to identify a new compromise Prime Minister, Bunds made gains at the shorter end as final German inflation data for November confirmed a softening of services price pressures while Italian industrial production maintained a downtrend.
- Gilts followed USTs lower on a quiet day for UK economic news.
- There are no top-tier economic data due from the euro area and UK on Wednesday while the ECB's rate announcement and updated projections will be the focus on Thursday.

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Daily bond market movements

Bond	Yield	Change
BKO 2 12/26	1.959	-0.032
OBL 2½ 10/29	1.960	-0.013
DBR 2.6 08/34	2.126	+0.007
UKT 4% 01/27	4.273	+0.032
UKT 4% 07/29	4.157	+0.041
UKT 4% 07/34	4.324	+0.056

*Change from close as at 4:00pm GMT.

Source: Bloomberg

Euro area

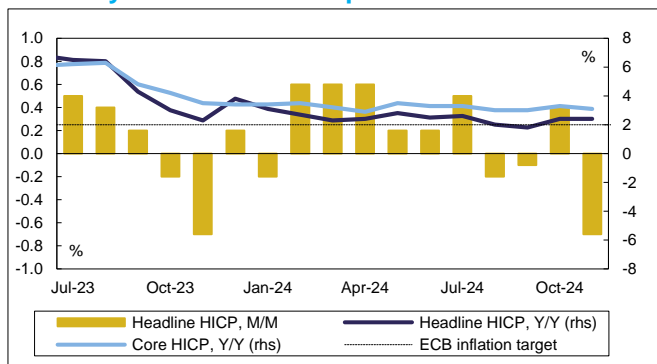
Final German inflation data confirm softening of services price pressures in November

Today's final estimates of German inflation in November represented the last notable data on price pressures to be released ahead of the ECB's policy announcement on Thursday. And they provided no major surprises, aligning with the flash estimates which had originally undershot expectations. So, contrary to the earlier consensus of an increase on the month, with prices down 0.7%M/M, the German EU-harmonised HICP measure was unchanged at 2.4%Y/Y in November. And the national CPI rate rose 0.2ppt – similarly less than initially expected – to 2.2%Y/Y. The HICP detail, published for the first time, confirmed that energy provided upwards pressure (up 1.8ppts to -3.6%Y/Y) as the month-on-month rates of decline in prices of household electricity, gas and auto fuel were much smaller than a year earlier. In contrast, HICP inflation of food, alcohol and tobacco moderated 0.4ppt to 2.9%Y/Y. More importantly, having risen to a 14-month high the prior month, services inflation fell 0.3ppt to 4.5%Y/Y. Today's figures confirmed that a moderation in a range of consumer-facing services, including recreation and culture (3.5%Y/Y), catering (6.7%Y/Y) and accommodation (2.7%Y/Y), contributed to that decline, suggesting a waning impact of rising labour costs. However, a drop in the typically-volatile package holiday component (4.5%Y/Y) also played a role to more than offset by a further rise of more than 1ppt in insurance to a series high of 15.8%Y/Y. So, while non-energy industrial goods inflation on the HICP measure rose 0.2ppt to a four-month high of 1.0%Y/Y, German core inflation on the EU-harmonised measure fell 0.2ppt to 3.1%Y/Y, a touch below the average of the prior six months.

While Germany was an outlier last month, euro area inflation should be back on target by mid-2025

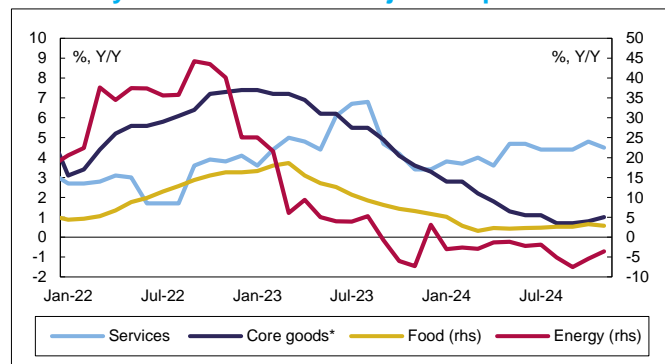
While German headline inflation was stable in November, it rose 0.3ppt in the euro area to a four-month high of 2.3%Y/Y. Although that increase also in large part reflected a significantly higher energy component, core inflation in the euro area was merely steady, at 2.7%Y/Y for a third successive month, in contrast to the decline in Germany. Indeed, headline and core inflation picked up in most other member states in November, thus deviating from the pattern in Germany. While differences between inflation in the various member states have narrowed back to levels that were normal before the global financial crisis, policy decisions, including with respect to the phasing out of energy price support, will continue to contribute to contrasting profiles over coming quarters. Overall in the euro area, we expect a higher energy component to push headline inflation up to about 2½%Y/Y in December. But with core goods and services price-setting behaviour seemingly back close to pre-pandemic norms, core inflation should take a step down in the New Year and headline inflation could well be at 2.0%Y/Y or below from Q2 onwards. Certainly, with recent data suggesting that its most recent forecast for the current quarter will be undershot, this week we expect the ECB to revise down its projection for inflation across the horizon to bring forward the date at which its target is met, from Q425 to mid-year. And its inflation projection for 2027 – to be published for the first time – should flag the non-negligible risk that inflation will undershoot the target over the medium term.

Germany: HICP consumer price inflation



Source: Macrobond and Daiwa Capital Markets Europe Ltd.

Germany: HICP inflation – major components



Source: Macrobond and Daiwa Capital Markets Europe Ltd.

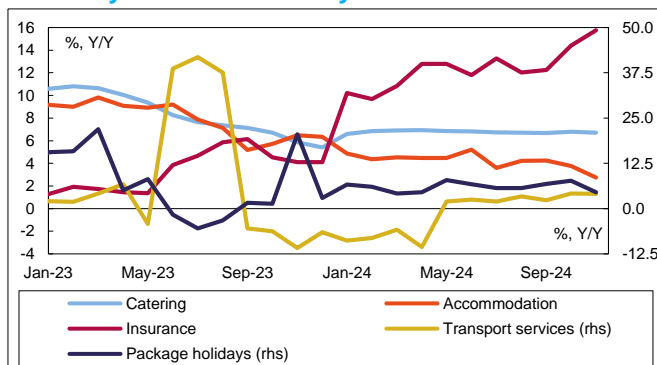
Italian industrial production maintained downtrend at start of Q4

In terms of economic activity, like in Germany and France, today's Italian industrial production release suggested a subdued start to the fourth quarter. Despite a pickup in energy production in marked contrast to Germany, Italian industrial output merely moved sideways in October as manufacturing slipped back slightly (-0.1%M/M). Within the manufacturing detail, positive trends in pharmaceuticals (3.5%3M/3M) and ICT equipment (1.5%3M/3M) were offset by a further decline in a range of subsectors including basic metals (-3.3%3M/3M), machinery (-1.4%3M/3M) and transport equipment (-3.5%3M/3M), with the latter down to the lowest level since June 2022. The overall level of industrial production was at its joint-lowest since July 2020, down 0.7%3M/3M and almost 5% below the pre-pandemic benchmark. This was on a par with France, but still significantly better than the retrenchment in Germany, where manufacturing output in October was some 13% below the February 2020 level. However, as in the other largest euro area member states, surveys suggest that the downturn in Italian manufacturing might well continue over coming months. Certainly, according to sentiment indicators – including the Commission ESIs and PMIs – pessimism among Italian manufacturers with respect to the production outlook has fallen close to its worst levels since the euro crisis outside the Covid-19 lockdown periods. And with the PMIs flagging a significant decline in new orders in November, the Commission survey suggested last month that a lack of demand was the most important factor limiting output for a decade.

Strong Irish data continue to flatter euro area manufacturing data

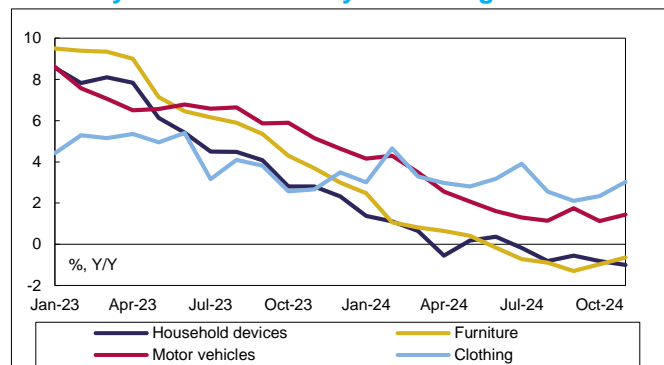
Overall, data from the five largest member states suggest that euro area industrial production (excluding construction) declined very modestly in October after dropping by an initially estimated 2.0%M/M in September. But, as is often the case, Ireland will again have a non-negligible impact on the aggregate euro area figure. Indeed, contrasting markedly the subdued performance elsewhere, Irish IP jumped 5.2%M/M in October, the most in seven months. There were also significant back revisions to the series, including a revised drop in September (from -10.7%M/M to -5.5%M/M). So, according to Ireland's statistical office, the level of industrial production in October was an extreme 80% above that in February 2020. Overall, this suggests that, when the aggregate figures are published on Friday, euro area industrial output potentially rose as much as 0.4%M/M in October, while the decline in September might also be softer than initially estimated. Of course, the underlying performance of the manufacturing sector will still have been lacklustre. Certainly, ECB policymakers will look past the distorting impact of the Irish data and focus instead on increasing signs of a loss of economic momentum in both the manufacturing and services sectors.

Germany: HICP inflation by selected services



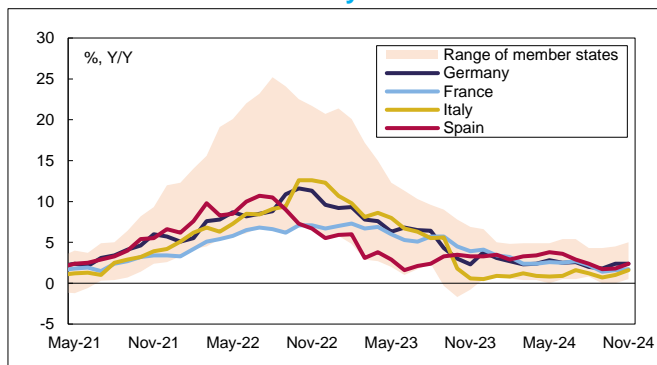
Source: Macrobond and Daiwa Capital Markets Europe Ltd.

Germany: HICP inflation by selected goods



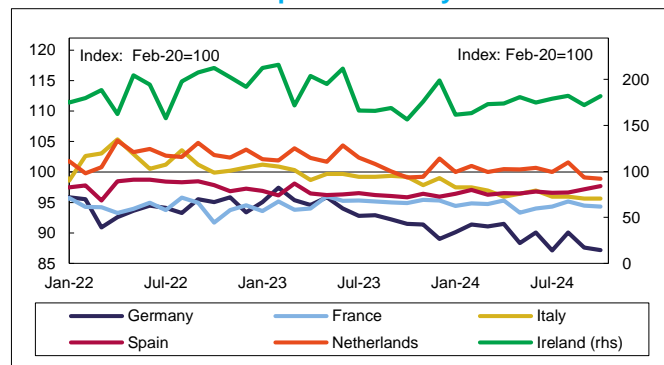
Source: Macrobond and Daiwa Capital Markets Europe Ltd.

Euro area: HICP inflation by member state



Source: Macrobond and Daiwa Capital Markets Europe Ltd.

Euro area: Industrial production by member state



Source: Macrobond and Daiwa Capital Markets Europe Ltd.

The coming two days in the euro area

With no top-tier data releases scheduled for the euro area on Wednesday, eyes now turn to Thursday's monetary policy announcement, which will confirm a further easing of the ECB's restrictive policy stance. We expect this week's Governing Council meeting to result in a cut of 25bps for a third consecutive meeting, and fourth time this cycle, to take the deposit rate to 3.00%. Certainly, recent data have failed to generate sufficient noise amongst Governing Council members to suggest that there will be serious consideration of a jumbo 50bps cut. Nonetheless, while the size of rate cut this time around will likely be conservative, we also expect the Governing Council to amend its forward guidance to acknowledge the increasingly two-sided nature of risks to the inflation outlook and provide a clearer sense of the likely future path of policy. While it is likely to reiterate that it will continue to follow a data-dependent and meeting-by-meeting approach, more dovish guidance should be forthcoming and will be justified by the ECB's updated macroeconomic projections. After a series of softer-than-expected inflation prints, these will likely bring forward the expected timing for headline inflation to return to target to mid-2025. By contrast, and despite several downbeat sentiment surveys, the ECB's baseline projection for GDP growth is likely to be only little changed, with private consumption still expected to lead to a gradual pickup in recovery momentum over coming quarters.

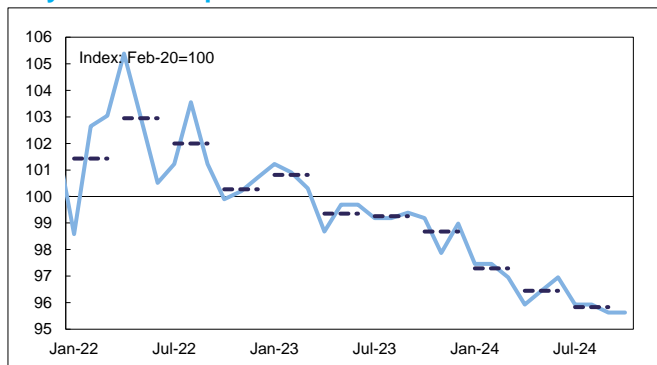
UK

The coming two days in the UK

Like the euro area, the UK is also set for a quiet couple of days on the data front. No top-tier releases are scheduled for Wednesday. And Thursday's RICS survey of surveyors is expected to report a further pickup in housing market activity following October's budget.

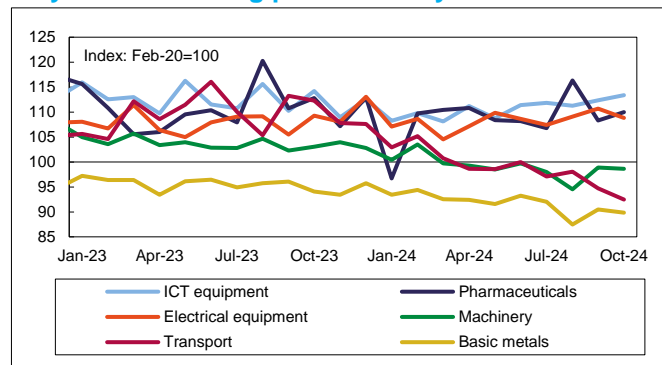
The next edition of the Euro wrap-up will be published on Thursday 12 December 2024

Italy: Industrial production*



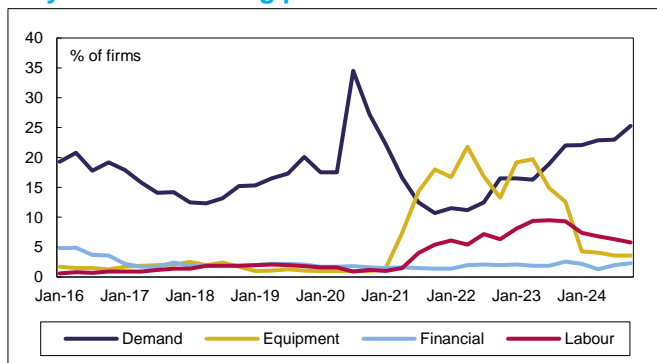
*Dashed dark blue lines represent quarterly average. Source: Macrobond and Daiwa Capital Markets Europe Ltd.

Italy: Manufacturing production by selected sector



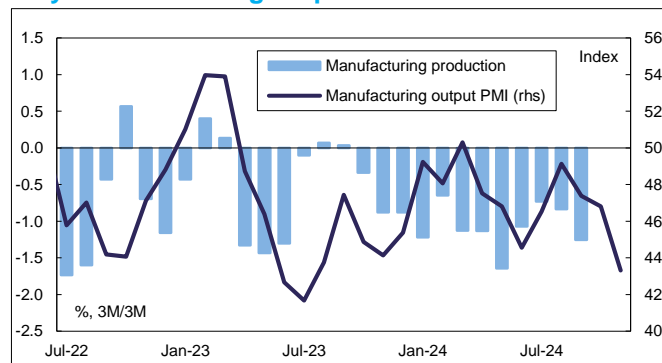
Source: Macrobond and Daiwa Capital Markets Europe Ltd.

Italy: Factors limiting production



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

Italy: Manufacturing output and PMI





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


European calendar

Today's results

Economic data

Country	Release	Period	Actual	Market consensus/ Daiwa forecast	Previous	Revised
Germany	 Final HICP (CPI) Y/Y%	Nov	2.4 (2.2)	<u>2.4 (2.2)</u>	2.4 (2.0)	-
Italy	 Industrial production M/M% (Y/Y%)	Oct	0.0 (-3.6)	-0.0 (-3.6)	-0.4 (-4.0)	-0.3 (-3.9)


Auctions

Country	Auction
UK	 sold £1.5bn of 0.75% 2033 inflation-linked bonds at an average yield of 0.745%

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

Monday's results

Economic data

Country	Release	Period	Actual	Market consensus/ Daiwa forecast	Previous	Revised
Euro area	 Sentix investor confidence index	Dec	-17.5	-12.3	-12.8	-

Auctions

Country	Auction
- Nothing to report -	


Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

Wednesday's releases

Economic data

Country	GMT	Release	Period	Market consensus/ Daiwa forecast	Previous
- Nothing scheduled -					



Auctions and events

UK		10.00	Auction: to sell £4bn of 4.25% 2034 bonds		
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Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

Thursday's releases

Economic data

Country	GMT	Release	Period	Market consensus/ Daiwa forecast	Previous
Euro area		13.15	Dec	<u>3.00 (3.15)</u>	3.25 (3.40)
UK		00.01	Nov	19	16

Auctions and events

Euro area		13.15	ECB monetary policy announcement		
		13.45	ECB President Lagarde holds post Governing Council meeting press conference		
		14.45	ECB to publish macroeconomic projections		
Italy		10.00	Auction: to sell up to €3bn of 2.7% 2027 bonds		
		10.00	Auction: to sell up to €3bn of 3.15% 2031 bonds		
		10.00	Auction: to sell up to €1.5bn of 3.35% 2035 bonds		
		10.00	Auction: to sell up to €1bn of 4.3% 2054 bonds		

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

Access our research blog at:

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