

# Euro wrap-up

## Overview

- Bunds made gains as President Lagarde repeated that ECB interest rates will be lowered further, while the flash euro area December PMIs remained consistent with broad stagnation despite surprising to the upside.
- Gilts made surprising losses as the flash UK PMIs were consistent with a marked loss of momentum since the summer and the biggest cut in employment in four years.
- Tuesday will bring euro area goods trade data, German sentiment surveys and the UK labour market report.

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### Daily bond market movements

Bond	Yield	Change
BKO 2 12/26	2.041	-0.022
OBL 2½ 10/29	2.065	-0.018
DBR 2.6 08/34	2.243	-0.011
UKT 4½ 01/27	4.348	+0.049
UKT 4½ 07/29	4.276	+0.045
UKT 4½ 07/34	4.440	+0.029

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

## Euro area

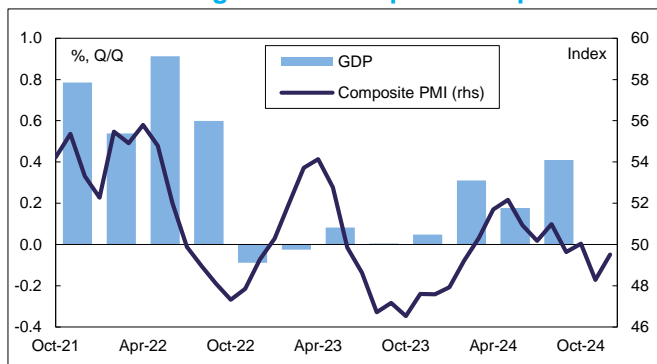
### Flash December PMIs surprise to the upside, but remain consistent with broad stagnation

After the [ECB](#) last week cut its key deposit rate by 25bps to 3.00% and revised its forward guidance to signal an intention to shift policy into a neutral stance over coming months, the flash December PMIs remained consistent with broad stagnation in the euro area in Q4 and an absence of economic growth momentum heading into the New Year. Admittedly, the euro area services output PMI surprised to the upside, rising 1.9pts to 51.4, to suggest a return to modest growth. The improvement in services sentiment was broad based, albeit led by the periphery, as the respective index for the euro area excluding Germany and France jumped 2.6pts to a six-month high (54.2). But today's survey continued to flag persisting weakness in manufacturing, with the factory output PMI down to a 12-month low (44.5) amid ongoing significant challenges in Germany (41.7) and France (39.6). As such, the euro area composite output PMI – up 1.2pts to 49.5 – failed to fully reverse the drop in November, leaving the average in Q4 1pt lower than in Q3 at 49.3, reinforcing the expectation that GDP growth has slowed sharply this quarter from 0.4%Q/Q in Q3 and might also be likely to undershoot the ECB's projection of 0.2%Q/Q. Despite rising on the month in December, the quarterly composite PMIs in Germany (down 0.4pt to 47.9) and France (down 3.4pts to 46.9) support our view that economic activity in the two largest member states moved sideways at best this quarter. But while certain factors adversely impacted growth elsewhere in the region – notably the fatal floods in Spain – the composite PMI for the euro area excluding Germany and France rose to a six-month high (52.6), leaving the quarterly index (51.9) unchanged from Q3 and consistent with ongoing steady expansion.

### Weak demand points to subdued economic recovery as firms cut headcount again

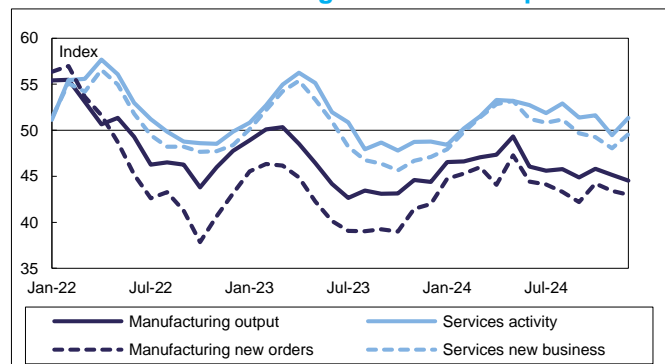
While ECB staff expect rising real incomes and the resilient labour market to support stronger household consumption over coming quarters, the flash PMIs continued to flag lacklustre demand in the services sector, with the new business component recording the fourth consecutive sub-50 reading in December despite an increase of 1.5pts this month. And with the new factory orders index (43.0) the second-lowest of the past 12 months and work backlogs falling sharply, the factory sector looks set to remain a non-negligible drag on growth heading into 2025. Against this backdrop, manufacturers reportedly continued to cut headcount. And with services firms also reporting no job growth, the composite employment PMI (49.1) fell to the lowest level in four years and the worst since the euro crisis in 2013 outside of the first phase of the pandemic. Having been hit in November by heightened political uncertainties related to the US election, collapse of the German coalition and political paralysis in France, the index for business expectations for the coming twelve months recovered somewhat this month. But it was still the second-lowest reading of the past year and remained well below the long-run average, underscoring that economic activity over coming quarters will likely remain lacklustre.

### Euro area: GDP growth & composite output PMI



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

### Euro area: Manufacturing & services output PMIs

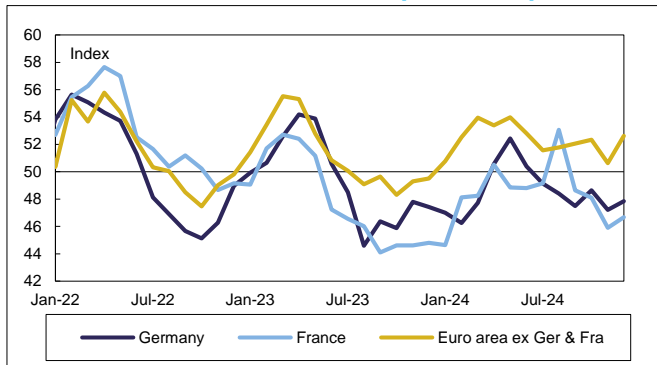


Source: S&P Global, Macrobond and Daiwa Capital Markets Europe Ltd.

### Services price PMIs tick higher, but labour costs growth continues to moderate

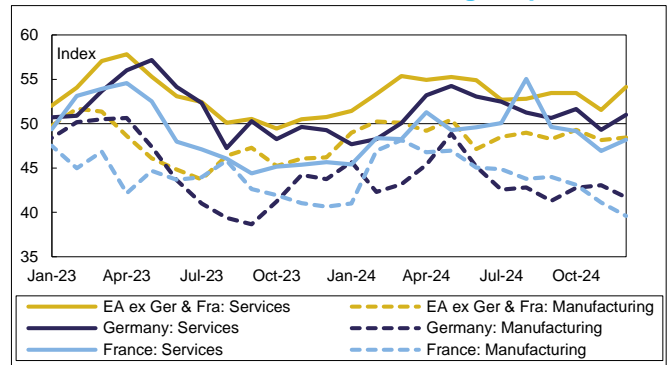
In terms of the indicators most closely related to inflation, today's survey suggested a slight pickup in cost growth at the end of the year. In particular, the euro area input price index rose to a four-month high (56.5), broadly in line with the long-run average. Consistent with recent stickiness in services inflation, the uptick was led by the services sector, with the respective index up to a five-month high still above the long-run trend. While firms attributed the pickup to higher pay pressures, today's updated figures confirmed a step down in overall labour cost growth of 0.6ppt to 4.6%Y/Y in Q3. Labour cost growth in the services sector moderated 0.3ppt to 4.5%Y/Y, the second-softest rate in the past two years. While the recent spike in German negotiated wages will keep labour cost growth in certain subsectors elevated over the near term, other indicators including the Indeed wage tracker point to softer pay growth at the start of Q4. And while today's PMIs suggested that prices charged in the services sector rose the most since August, we suspect that, as in the manufacturing sector, an absence of meaningful demand will help to limit pass-through to consumers over coming quarters.

#### Euro area member states: Composite output PMIs



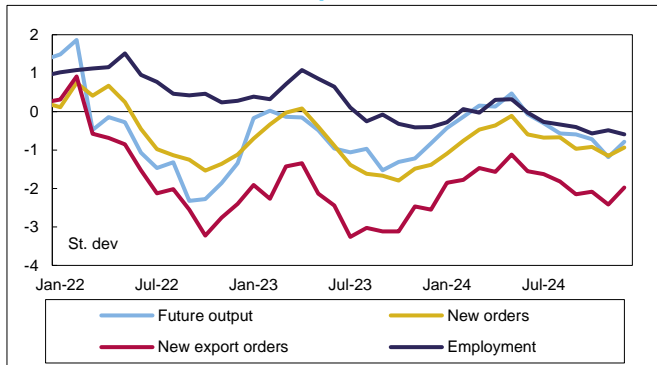
Source: S&P Global, Macrobond and Daiwa Capital Markets Europe Ltd.

#### Euro area: Services & manufacturing output PMIs



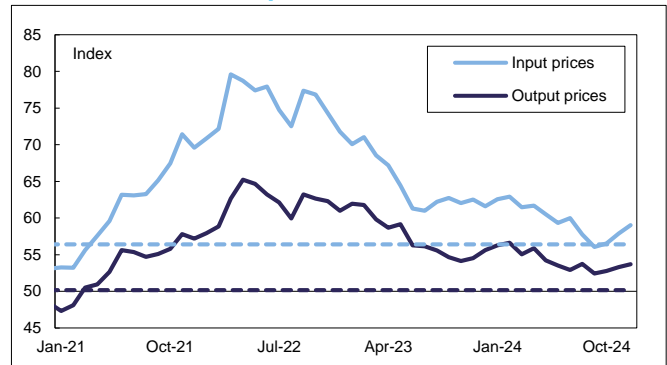
Source: S&P Global, Macrobond and Daiwa Capital Markets Europe Ltd.

#### Euro area: Selected composite PMIs



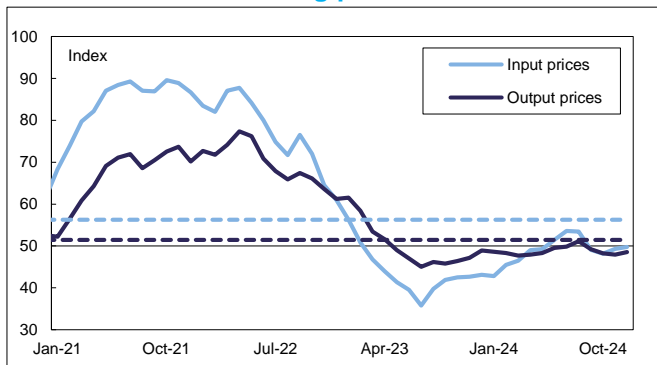
Source: S&P Global, Macrobond and Daiwa Capital Markets Europe Ltd.

#### Euro area: Services price PMIs\*



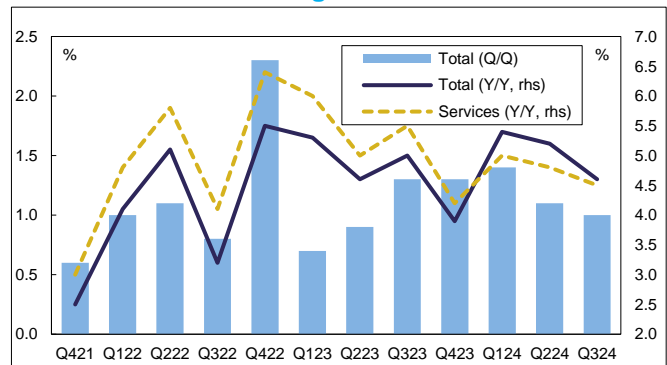
\*Dashed lines represent pre-pandemic average. Source: S&P Global, Macrobond and Daiwa Capital Markets Europe Ltd.

#### Euro area: Manufacturing price PMIs\*



\*Dashed lines represent pre-pandemic average. Source: S&P Global, Macrobond and Daiwa Capital Markets Europe Ltd.

#### Euro area: Labour cost growth



Source: Macrobond and Daiwa Capital Markets Europe Ltd.

## The day ahead in the euro area

The flow of sentiment surveys continues tomorrow, with the German ifo business indices and ZEW investor survey to provide a cross-check on today's PMIs. The ifo survey will also offer an update on conditions in the retail and construction sectors, which policymakers might hope well have been supported by recent cuts in interest rates. But contrasting the modest improvement in today's PMIs, investors are likely to be more downbeat heading into year-end, with the ZEW indices likely to tally with the pessimism in last week's Sentix survey, which reported that investors were the most downbeat about current conditions in Germany since June 2020. Meanwhile, the struggles of the factory sector will likely be reflected in some soft euro area goods trade data in October.

## UK

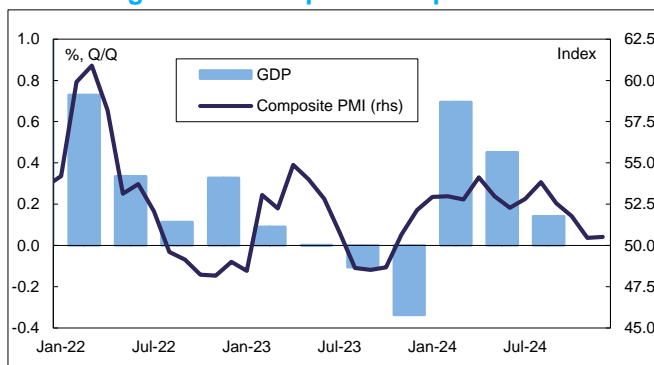
### Flash PMIs consistent with marked loss of momentum since the summer

After last week's [GDP data](#) for October suggested that UK economic activity is now broadly flat-lining, today's December flash PMIs underscored the marked loss of momentum since the summer, keeping the door open to the (admittedly relatively small) possibility of a rate cut at this week's MPC meeting. The headline composite activity PMI was unchanged in December at 50.5, matching the prior month's 13-month low. And that left the Q4 average at 50.9, a level that before the pandemic would have been consistent with a slight contraction in economic output. Indeed, it was similarly the lowest quarterly reading since Q4'23 (50.5) when GDP contracted 0.3%Q/Q, and a chunky 2.2pts below the average in Q3'24 when GDP grew just 0.1%Q/Q. The services activity index rose 0.6pt from November's 13-month low to 51.4, still well below the long-run average to suggest minimal momentum in the sector. And the manufacturing output PMI fell more than 2pts for the third successive month to an eleven-month low of 45.7 consistent with substantive retrenchment.

### New orders & employment drop sharply pointing to weakness ahead, but costs & prices pick up

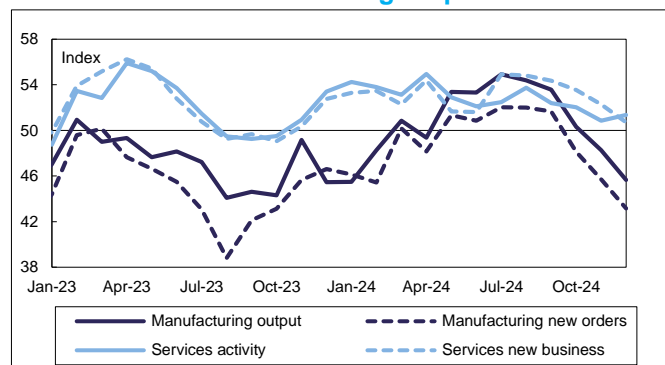
Disconcertingly, the new factory orders index also fell sharply to a 15-month low of just 43.2, while the equivalent PMI for the services sector dropped to a 13-month low consistent with stagnant demand (50.7). And seemingly in response to the end-October Budget announcement of increased employer National Insurance Contributions (NICs), the composite employment index (45.8) signalled the sharpest cuts to business headcount since January 2021 and the global financial crisis in 2009 when the first phase of pandemic is excluded. That ought to ring alarm bells at the BoE, adding to evidence that the current monetary stance is excessively tight. However, perhaps for similar reasons, the PMIs for input costs and output prices rose to the highest levels in eight and nine months respectively. And as we expect tomorrow's labour market data to report a

#### UK: GDP growth & composite output PMI



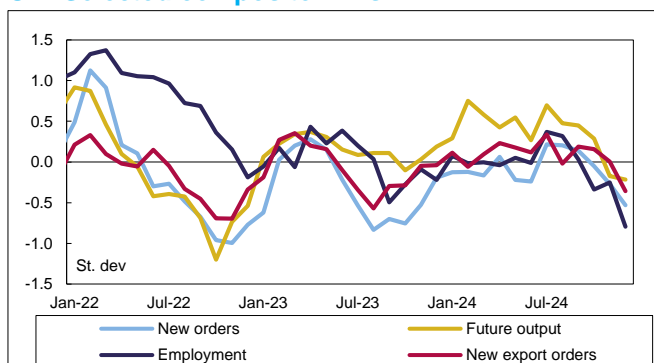
Source: S&P Global, Macrobond and Daiwa Capital Markets Europe Ltd.

#### UK: Services & manufacturing output PMIs



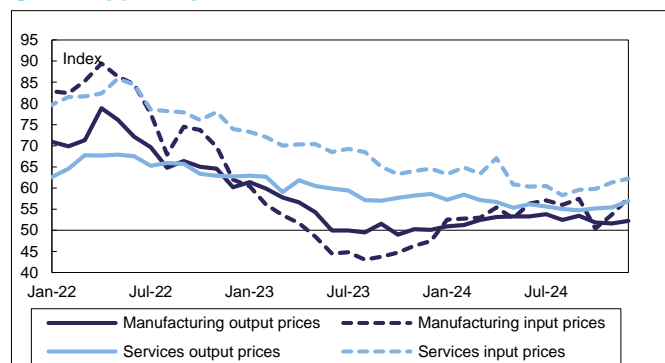
Source: S&P Global, Macrobond and Daiwa Capital Markets Europe Ltd.

#### UK: Selected composite PMIs



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

#### UK: Price PMIs















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

pickup in wage growth in October and Wednesday's CPI figures to show an increase in inflation to around 2½%Y/Y, for the time being we maintain our expectation that a majority of MPC members will vote to keep Bank Rate unchanged at 4.75% this week.

## The day ahead in the UK

The focus in the UK tomorrow will be the latest labour market report, with most attention on developments in wage growth. After private sector regular pay growth moved sideways (4.8%3M/Y) in September, the strength of October's PAYE data (6.3%3M/Y) flags the possibility of a moderate increase in October's ONS wage data, broadly in line with the BoE's projection. Tomorrow's report will also include updated estimates from the reweighting of the Labour Force Survey (LFS) that were published at the start of this month. These showed that, in the three months to June 2024, the changes in estimated population growth led to an increase in the level of employment (by a significant 402k), unemployment level (30k) and those economically inactive (60k). As such, the reweighted LFS measure of the level of employment in June was significantly closer to the HMRC payroll estimates. And consistent with the recent decline in the number of payrolled employees, we expect the LFS measure of employment to have slowed further in the three months to October. Overall, the reweighting had limited effects on the unemployment rate. And tomorrow's release is expected to see it move sideways at 4.3%.

## European calendar

Today's results						
Economic data						
Country	Release	Period	Actual	Market consensus/ <i>Daiwa forecast</i>	Previous	Revised
Euro area	 Preliminary manufacturing (services) PMI	Dec	<b>45.2 (51.4)</b>	45.3 (49.5)	45.2 (49.5)	-
	 Preliminary composite PMI	Dec	<b>49.5</b>	48.2	48.3	-
	 Labour costs Y/Y%	Q3	<b>4.6</b>	<u>4.6</u>	5.2	-
	 Job vacancy rate %	Q3	<b>2.5</b>	<u>2.5</u>	2.6	-
Germany	 Preliminary manufacturing (services) PMI	Dec	<b>42.5 (51.0)</b>	43.1 (49.4)	43.0 (49.3)	-
	 Preliminary composite PMI	Dec	<b>47.8</b>	47.5	47.2	-
France	 Preliminary manufacturing (services) PMI	Dec	<b>41.9 (48.2)</b>	43.1 (47.0)	43.1 (46.9)	-
	 Preliminary composite PMI	Dec	<b>46.7</b>	46.0	45.9	-
Italy	 Final HICP (CPI) Y/Y%	Nov	<b>1.5 (1.3)</b>	<u>1.6 (1.4)</u>	1.0 (0.9)	-
UK	 Rightmove house prices M/M% (Y/Y%)	Dec	<b>-1.7 (1.4)</b>	-	-1.4 (1.2)	-
	 Preliminary manufacturing (services) PMI	Dec	<b>47.3 (51.4)</b>	48.5 (51.0)	48.0 (50.8)	-
	 Preliminary composite PMI	Dec	<b>50.5</b>	50.6	50.5	-
Auctions						
Country	Auction	- Nothing to report -				

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

## Tomorrow's data releases

### Economic data

Country	GMT	Release	Period	Market consensus/ <i>Daiwa forecast</i>	Previous
Euro area	10.00	Trade balance €bn	Oct	11.6	13.6
Germany	09.00	ifo business climate indicator	Dec	85.5	85.7
	09.00	ifo current assessment (expectations) indicator	Dec	84.0 (87.5)	84.3 (87.2)
	10.00	ZEW investor survey – current situation (expectations) balance %	Dec	-93.0 (6.5)	-91.4 (7.4)
UK	07.00	Average wages (excluding bonuses) 3M/Y%	Oct	4.7 (5.0)	4.3 (4.8)
	07.00	Unemployment rate 3M%	Oct	4.3	4.3
	07.00	Employment 3M/3M change 000s	Oct	25	220
	07.00	Payrolled employees M/M change 000s	Nov	-10	-5
	07.00	Claimant count rate % (change 000s)	Nov	-	4.7 (26.7)

### Auctions and events

Country	GMT	Auction / Event
UK	10.00	Auction: to sell £3.75bn of 4.125% 2029 bonds

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

Access our research blog at:

<https://www.uk.daiwacm.com/ficc-research/recent-blogs>

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