

# Euro wrap-up

## Overview

- Bunds made modest gains as the ZEW survey inevitably reported that investors remain very downbeat about German economic conditions at the start of the year.
- Despite a pickup in private sector pay growth, Gilts made larger gains as data showed that the UK labour market continues to loosen with a rising unemployment rate and falling payroll employment and vacancies.
- Wednesday will bring UK public finances data while Thursday will bring updates on consumer confidence in the euro area and business sentiment in France and the UK.

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### Daily bond market movements

Bond	Yield	Change
BKO 2 12/26	2.203	-0.013
OBL 2½ 10/29	2.307	-0.018
DBR 2½ 02/35	2.502	-0.023
UKT 4½ 01/27	4.321	-0.042
UKT 4½ 07/29	4.331	-0.052
UKT 4½ 07/34	4.589	-0.068

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

## Euro area

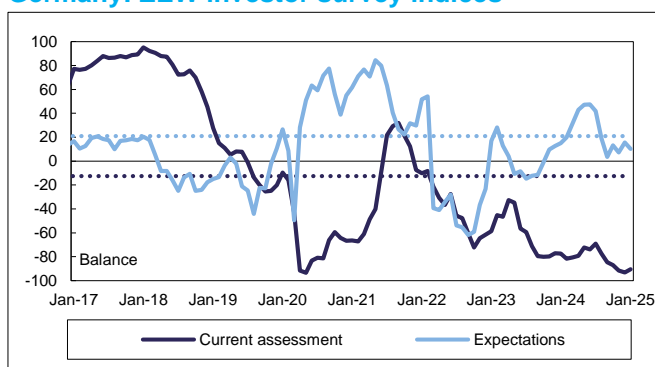
### Investors inevitably remain extremely gloomy about German economic outlook

With the German economy having likely contracted in Q4, headline inflation having ticked higher at the back end of 2024, and the economic outlook subject to significant uncertainties – both domestically and overseas – investor perceptions of conditions in the euro area's largest member state remained predictably gloomy at the start of 2025. Certainly, the modest increase in the ZEW survey's current conditions net balance for the first month in six in January was not indicative of any meaningful improvement in the economic backdrop at the start of the New Year. Indeed, at -90.4, the balance was still close to the lows reached at the start of the pandemic and height of the global financial crisis and well below the long-run average (-12.6). Moreover, no survey respondents considered conditions to be 'good' for a third successive month, the longest such run since early 2003. Given concerns about potential US trade tariffs, the likelihood of a vacuum in policy-making for a while after the Federal election next month, and persisting weak demand and competitiveness challenges, today's survey reported a deterioration in investor expectations for the coming six months. Indeed, despite widespread expectations of further ECB easing to come, the respective index (10.3) slipped to the third lowest level of the past 14 months. Among the various business sectors, investors were more upbeat about the outlook for IT services and insurance industries. But they revised down their expectations for profits in retail and construction. And despite a modest improvement compared with recent months, the profit outlook for the autos sector was judged to remain extremely unfavourable as intensified competition from China and concerns about higher tariffs weighed.

### The coming two days in the euro area

Following a relatively quiet Wednesday on the data front, the focus in the euro area on Thursday will turn to the Commission's flash consumer confidence index for January. With growth momentum in the euro area having slowed markedly at the end of the year, persistently downbeat sentiment is a key obstacle to the consumer-led recovery expected by most forecasters on the back of rising real incomes. In recent months, the Commission survey has signalled an ongoing downtrend in confidence – with the headline index down 0.7pt in December to an 8-month low of -14.5 – as savings intentions rose to a series high and fears of unemployment rose to the highest in more than two years. And with political and economic uncertainty still heightened, consumer confidence is expected to remain subdued at the start of the year. Likewise, political events are expected to continue to weigh on INSEE's business confidence indices (also due Thursday), despite the improving prospects for ending the French budget deadlock under new-Prime Minister Bayrou.

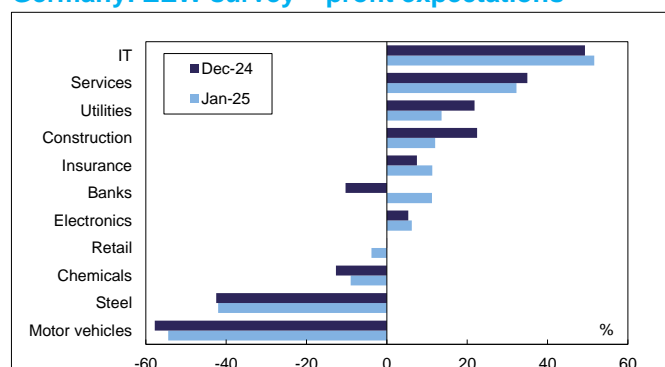
### Germany: ZEW investor survey indices\*



\*Dotted lines represent long-run average.

Source: Macrobond and Daiwa Capital Markets Europe Ltd.

### Germany: ZEW survey – profit expectations



Source: Macrobond and Daiwa Capital Markets Europe Ltd.

**UK**

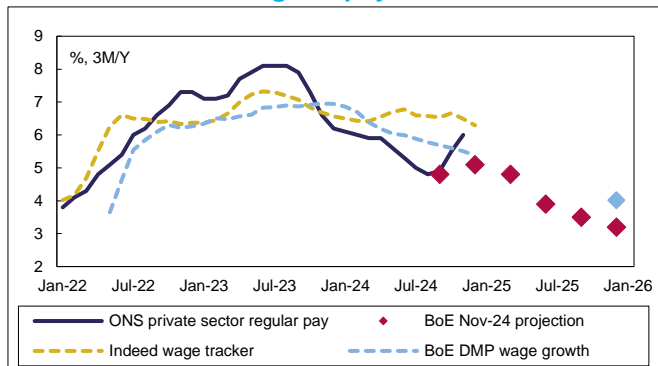
**No surprises as pay growth remains strong despite softening labour market**

Today's labour market report provided no surprises, underscoring that demand for workers softened over the second half of last year as economic activity flatlined. At the same time, private sector pay growth strengthened above the path projected by the BoE in November to a seven-month high, which if sustained would not be consistent with a return of inflation to target over the medium term. Such solid pay growth might also provide welcome support to consumer spending and overall GDP growth over coming quarters. But firms are already absorbing the elevated pay rises in their margins amid the soft demand environment, diminishing their impact on inflation. And surveys suggest that wage growth is highly likely to moderate steadily from the current quarter on in response to the looser labour market. Indeed, the current loss of momentum in economic activity and labour demand could intensify to increase significantly the risks that inflation will undershoot the target over the medium term. So, we still expect the BoE to continue to cut rates gradually, by 25bps a quarter in 2025 and H126.

**Real wages rise the most in three years but consumers prefer to save rather than spend**

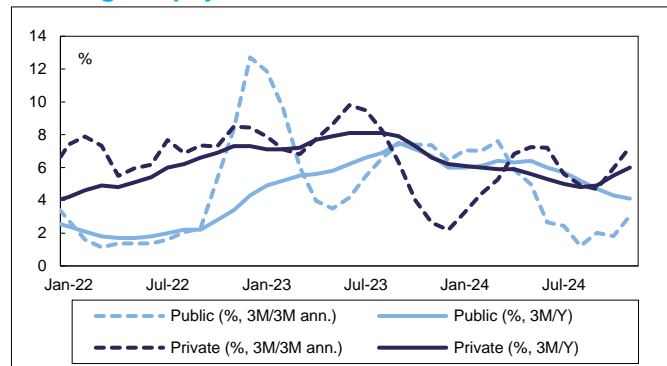
In terms of the detail, private sector regular pay growth rose 0.5ppts in November to 6.0%3M/Y. So, a moderation in December in line with the BoE's projection of 5.1%3M/Y – which would require a slowdown of 2.5ppts in the single-month rate to just 2.6%Y/Y – seems almost inconceivable. Indeed, private sector strength in the latest period was broad-based, with regular pay growth up in services to a six-month high of 5.6%3M/Y, and steady at 6.0%3M/Y in manufacturing. In contrast, public sector regular pay growth slowed to a two-year low of 4.1%3M/Y, and softened to the same pace when including bonuses. But given the strength in the private sector, whole economy total pay accelerated to a 6-month high of 5.6%3M/Y. That equated to a real-terms increase of 2.4%3M/Y, the strongest in more than three years and more than double the average in the five years before the pandemic. While real pay in the public sector was still below the level in Q419 before the pandemic, in the private sector it was 5.8% higher against the same benchmark. Such strong real pay growth would normally be expected to feed through to vigorous private consumption growth. But it has merely reversed the erosion of real pay in 2022 and early 2023 caused by high inflation. And the recent preference of households to save rather than spend, particularly as the risks of unemployment rise, suggests that any pickup in consumer spending over the near term is likely to remain modest at best.

**UK: Private sector regular pay**



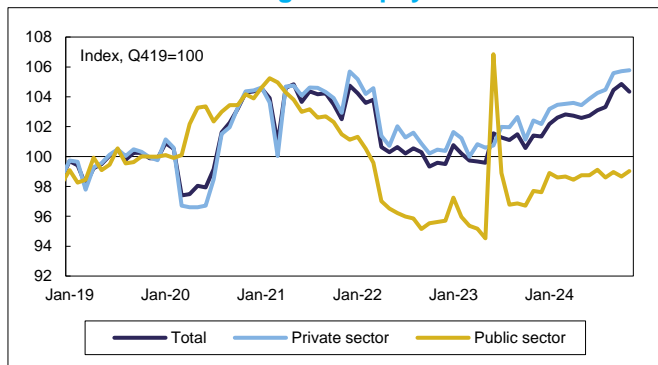
Source: BoE, Macrobond and Daiwa Capital Markets Europe Ltd.

**UK: Regular pay momentum**



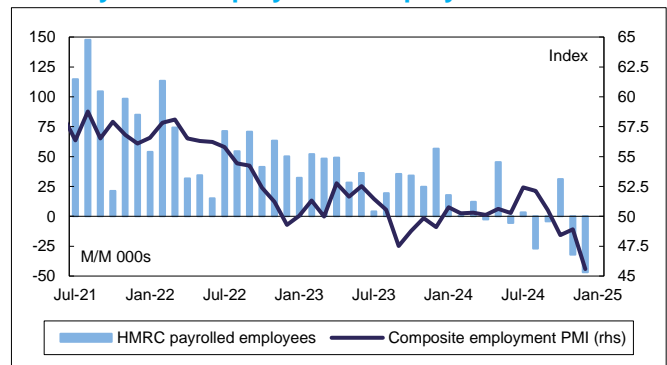
Source: Macrobond and Daiwa Capital Markets Europe Ltd.

**UK: Real-terms average total pay levels**



Source: Macrobond and Daiwa Capital Markets Europe Ltd.

**UK: Payrolled employees & employment PMI**

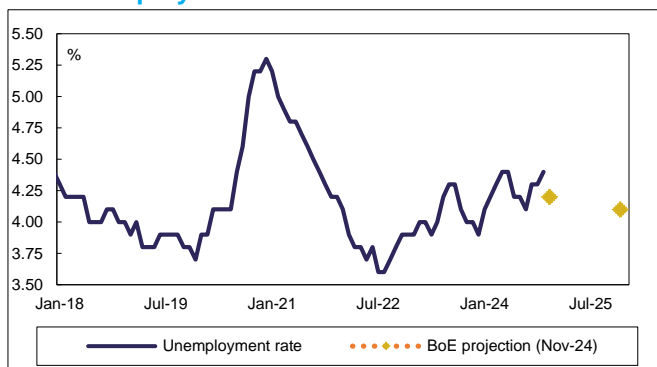


Source: S&P Global, Macrobond and Daiwa Capital Markets Europe Ltd.

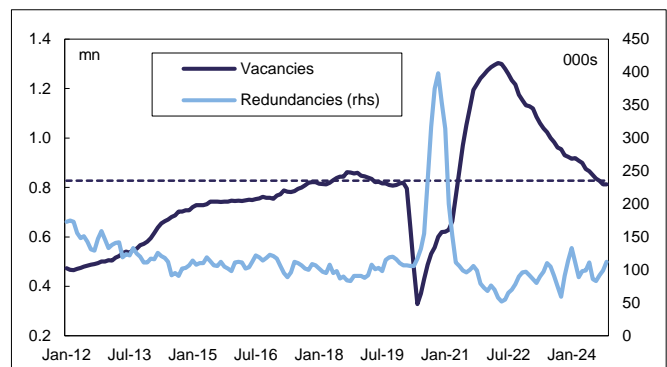
## Labour market now looser than before the pandemic, supporting pay moderation in 2025

Despite its strength in the three months to November, pay growth is likely to moderate from Q1 on. Timely indicators, such as the Indeed wage tracker, which slowed to a near-three-year low in December, point to a slight easing last month. And despite the big rise in National Living Wage from April, the DMP survey suggested that firms expect pay growth to slow more significantly, to just below 4%Y/Y by end-2025, as they try to offset the impact of the forthcoming rise in employer NICS. The steady loosening of the labour market over recent quarters strongly suggests that is realistic. Consistent with the marked deterioration in the employment PMI at the end of last year, the preliminary estimate of payrolled employees fell for the fourth month out of five in December and by 47k, the most since the first phase of the pandemic in 2020. While that figure is subject to revision, the LFS estimate of employment growth (admittedly also of debatable accuracy) slowed to just 36k in the three months to a seven-month low of November, to be up just 0.1%Y/Y. Despite a further drop in the inactivity rate to a 16-month low, the unemployment rate ticked up 0.1ppt to 4.4%, also a seven-month high and 0.2ppt above the BoE's projection for year-end. And the number of job vacancies edged down to the lowest since April 2021, notably below the average in the year ahead of the pandemic. With the ratio of vacancies to unemployment suggesting that the labour market is now looser than before the arrival of Covid-19, the majority of MPC members is highly likely to look through the latest uptick in pay growth and cut rates next month and gradually further over the remainder of the year and into 2026.

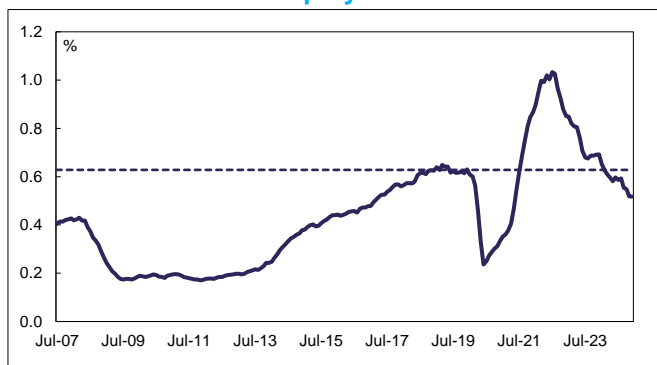
### UK: Unemployment rate



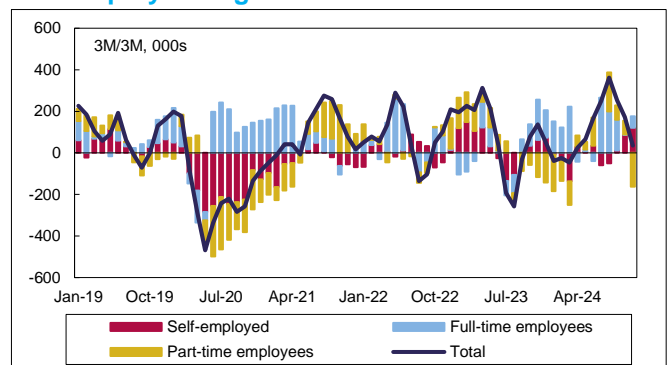
### UK: Job vacancies & redundancies



### UK: Vacancies to unemployment ratio\*



### UK: Employment growth



## The coming two days in the UK









December's public finance statistics (due tomorrow) will bring an update on UK government borrowing at the end of the calendar year. Public sector net borrowing in the first eight months of FY24-25 reached £113.2 bn, £0.4bn below the amount in the same period of the prior fiscal year but £2.0bn above the level consistent with the OBR's October forecast. An overshoot in borrowing by local authorities and public corporations more than offset the impact of a central government undershoot, which was in part related to lower-than-expected debt interest payments on inflation-linked bonds. Meanwhile, the CBI's industrial trends survey for January (Thursday) will provide an account of manufacturing conditions before the flash PMIs arrive (Friday). Consistent with the PMIs, the CBI has flagged a dim outlook for industrial firms, with order books (-40) reportedly falling to their lowest level since November 2020. And though some correction may be expected after last month's particular weakness, orders nonetheless seem bound to remain subdued.

The next edition of the Euro wrap-up will be published on Thursday 23 January



## European calendar

### Today's results

#### Economic data

Country	Release	Period	Actual	Market consensus/ <i>Daiwa forecast</i>	Previous	Revised
Euro area	 New car registrations Y/Y%	Dec	<b>3.6</b>	-	-3.4	-
Germany	 ZEW investor survey – current situation (expectations) balance %	Jan	<b>-90.4 (10.3)</b>	-93.1 (15.1)	-93.1 (15.7)	-
France	 Retail sales Y/Y%	Dec	<b>-0.8</b>	-	-0.1	-
UK	 Average wages (excluding bonuses) 3M/Y%	Nov	<b>5.6 (5.6)</b>	5.7 (5.5)	5.2 (5.2)	-
	 Unemployment rate 3M%	Nov	<b>4.4</b>	4.4	4.3	-
	 Employment 3M/3M change 000s	Nov	<b>36</b>	33	173	-
	 Payrolled employees M/M change 000s	Dec	<b>-47</b>	-8	-35	-32
	 Claimant count rate % (change 000s)	Dec	<b>4.6 (0.7)</b>	-	4.6 (0.3)	- (-25.1)


#### Auctions

Country	Auction
Germany	 sold €945mn of 2.1% 2029 green bonds at an average yield of 2.26%
	 sold €908mn of 2.3% 2033 green bonds at an average yield of 2.4%


Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

### Wednesday's releases

#### Economic data

Country	GMT	Release	Period	Market consensus/ <i>Daiwa forecast</i>	Previous
UK	 07.00	Public sector net borrowing £bn	Dec	-	11.2




#### Auctions and events

Germany	 10.30	Auction: to sell €1.5bn of 2.6% 2041 bonds
	 10.30	Auction: to sell €500mn of 2.5% 2044 bonds




Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

### Thursday's releases

#### Economic data

Country	GMT	Release	Period	Market consensus/ <i>Daiwa forecast</i>	Previous
Euro area	 15.00	Preliminary consumer confidence indicator	Jan	-14.1	-14.5
France	 07.45	INSEE business (manufacturing) confidence indicator	Jan	94 (96)	94 (97)
UK	 11.00	CBI industrial trends survey – total orders (selling prices) balance %	Jan	-35 (20)	-40 (23)

#### Auctions and events

France	 09.50	Auction: to sell up to €13bn of 2.5% 2027, 5.5% 2029 and 2.75% 2030 bonds
	 10.50	Auction: to sell up to €2.25bn of 0.6% 2034, 0.55% 2039, 1.8% 2040 and 0.1% 2053 inflation-linked bonds
UK	 10.00	Auction: to sell £4.25bn of 4.375% 2028 bonds

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

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