

Euro wrap-up

Overview

- While the broad-based decline in euro area inflation in October was confirmed, shorter-dated Bunds followed UST slightly lower.
- Gilts made gains as UK retail sales fell well short of expectations and started Q4 on the backfoot.
- The coming week will bring the flash European PMIs for November, the ECB account from October's Governing Council meeting, and an update on UK fiscal policy in the Chancellor's Autumn Statement.

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Daily bond market movements

Bond	Yield	Change
BKO 3.1 12/25	2.956	+0.020
OBL 2.4 10/28	2.532	+0.018
DBR 2.6 08/33	2.593	+0.005
UKT 3½ 10/25	4.533	+0.018
UKT 4½ 06/28	4.116	-0.020
UKT 3¼ 01/33	4.112	-0.031

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

Euro area

Final euro area HICP figures confirm softest inflation rate since July 2021

While the euro area's flash inflation estimates for October had delivered a more marked moderation than had been expected, there were no surprises from today's final figures. Indeed, these confirmed that the headline inflation rate fell 1.4ppts on the month – the second-largest monthly drop on the series – to 2.9%Y/Y, the softest inflation rate since July 2021. Sixteen out of the twenty member states saw a moderation and two countries – the Netherlands and Belgium – reporting deflation. It also took euro area inflation well below the ECB's forecast for Q4 as a whole (3.3%Y/Y). The main driver for the decline in inflation in October was energy, prices of which fell 1.1%M/M in October, amid a first monthly decline in petrol prices in five and a modest drop in electricity prices, having surged 6.2%M/M this month last year. So, the annual energy inflation rate plunged 6.6ppts to -11.2%Y/Y, the lowest since May 2020 and knocking more than one percentage point off headline inflation. Favourable base effects following the spike in prices last year also saw food inflation ease significantly, down 1.4ppt to 7.4%Y/Y, an eighteen-month low.

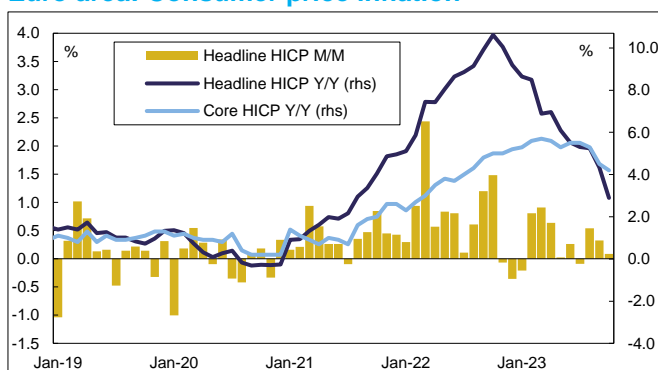
Underlying price pressures dissipating amid weakening demand

The moderation in inflation in October also represented better behaved price movements in the core components. Indeed, reflecting the ongoing improvement in the supply-demand imbalance and lower input cost burdens at the factory gate, the monthly increase in core goods prices (0.6%M/M) was just half that seen a year ago and bang in line with the pre-pandemic long-run average for the month. As such, the respective annual rate eased for an eighth consecutive month, by 0.6ppt to 3.5%Y/Y, the lowest since Russia's invasion of Ukraine. A deflationary trend was seen among a wide range of goods including furniture, household appliances and motor vehicles, for which the respective inflation rates were the lowest for at least two years, while clothing inflation slipped to a fourteen-month low. Admittedly, services inflation still contributed a chunky 2ppts to the headline HICP rate, albeit easing in October (-0.1ppt to 4.6%Y/Y) its softest rate since January. Despite an uptick in airfares, accommodation and education costs in October, inflation of catering services moderated. And overall, core inflation fell for a third successive month, by 0.3ppt to 4.2%Y/Y – the lowest since July 2022 – and 1.5ppts below March's series high.

More than 80% of items in HICP basket have easing inflation

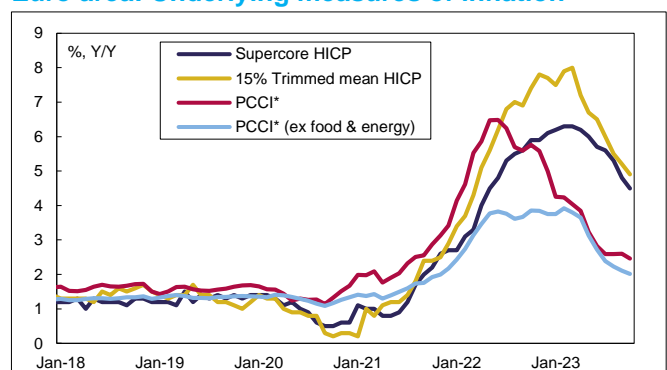
While base effects continued to play a significant role in the downtrend in October, recent momentum in the core components has improved markedly too, with the 3M/3M annualised rate of core goods prices down 0.6ppt to a 22-month low of 2.3%. And while still almost double the ECB's inflation target, momentum in services inflation also eased to a fourteen-

Euro area: Consumer price inflation



Source: Refinitiv Datastream and Daiwa Capital Markets Europe Ltd.

Euro area: Underlying measures of inflation



*Persistent and common components of inflation. Source: ECB, Refinitiv Datastream and Daiwa Capital Markets Europe Ltd.

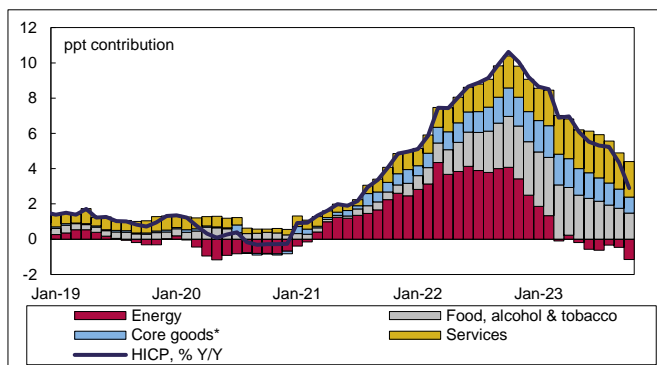
month low of 3.8%3M/3M annualised, more than 3ppts below last November's peak. Other measures of underlying price pressures published as part of today's release showed further improvement too. For example, the 15% trimmed mean HICP rate fell 0.6ppt to a twenty-month low of 4.3%Y/Y, while the share of items in the HICP basket with inflation above 2% also fell to the lowest since April 2022 (77%). And the share of items with easing inflation rose to above 80%. Moreover, the ECB's model-based measure of persistent and common component of inflation (PCCI), which the Governing Council believes can provide one of the more reliable guides to future inflation fell to its lowest rate (2.3%Y/Y) since September 2021, with the core PCCI (excluding energy and food) rate back at 2.0%Y/Y for the first time in almost two years. And so, we expect core inflation to fall to 4.0%Y/Y by year-end and in line with the ECB's forecast in Q4 (4.1%Y/Y), before taking a more substantial step-down in the New Year and falling back to 2% in Q24. So, while we expect headline inflation to remain just above the 2% target on average in H24, this should nonetheless allow the ECB to start cutting interest rates in Q2 next year.

The week ahead in the euro area

A key focus in the euro area in the coming week will be the latest set of economic sentiment surveys, which are likely to illustrate challenging economic conditions in the middle of the current quarter and further flag uncertainties about the outlook for growth at the turn of the year. Despite the recent moderation in inflation, the European Commission's preliminary consumer confidence index (Wednesday) is likely to suggest little improvement in November as household purchase intentions remain dampened by higher borrowing costs and rising concerns of unemployment. Meanwhile, the flash PMIs from the euro area, Germany and France (Thursday) will likely point to ongoing contraction in the middle of Q4 and signal that firms are scaling back workforces amid declining orders. Indeed, the headline euro area composite output PMI fell in October to 46.5, its lowest level for almost three years, with the respective German (45.9) and French indices (44.6) similarly signaling a significant contraction. But the French PMI has frequently overemphasised the deterioration in economic conditions in the euro area's second-largest member state. And so, the INSEE business survey (Thursday) will be watched more closely, while the German ifo institute's indices (Friday) will additionally provide an update on sentiment in the retail and construction sectors in November.

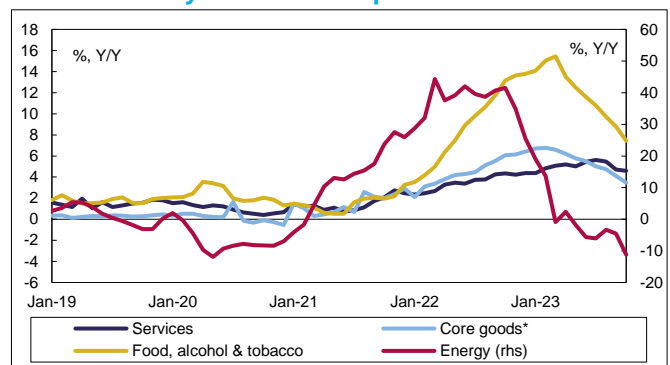
In terms of hard economic data, releases in the coming week include euro area construction output numbers for September (Monday) and new car registration numbers for October (Tuesday). While construction activity moved sideways in Germany at the end of Q3, an increase was recorded in France (1.8%M/M). The end of the week will also bring updated German Q3 GDP figures, which will include, for the first time, an official expenditure breakdown. Given the weakness in September activity figures, there is a risk that the contraction in GDP will be slightly larger than initially estimated (-0.1%Q/Q).

Euro area: Contributions to inflation



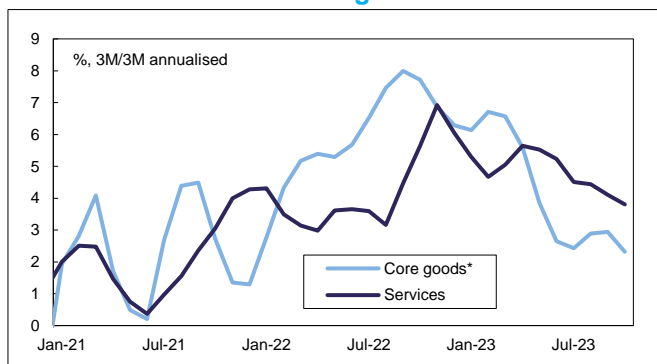
*Non-energy industrial goods. Source: Refinitiv Datastream and Daiwa Capital Markets Europe Ltd.

Euro area: Key inflation components



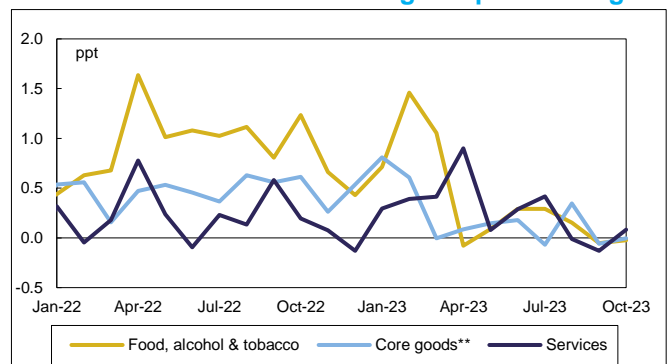
*Non-energy industrial goods. Source: Refinitiv Datastream and Daiwa Capital Markets Europe Ltd.

Euro area: Services & core goods* momentum



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

Euro area: Deviations from long-run price change*



*Monthly change in prices compared to average for the month in the decade before the pandemic. **Non-energy industrial goods. Source: Refinitiv Datastream and Daiwa Capital Markets Europe Ltd.

Separately, the ECB's account from the policy-setting meeting on 26 October will also be published on Thursday. While this meeting saw the Governing Council maintain a 'higher-for-longer' rate stance, President Lagarde's tone in the post-meeting press conference was more dovish. And so, we would expect the minutes to flag increasing evidence of the impact of the transmission of past rate hikes on the economy, and suggest that downside risks to the near-term growth outlook were intensifying.

UK

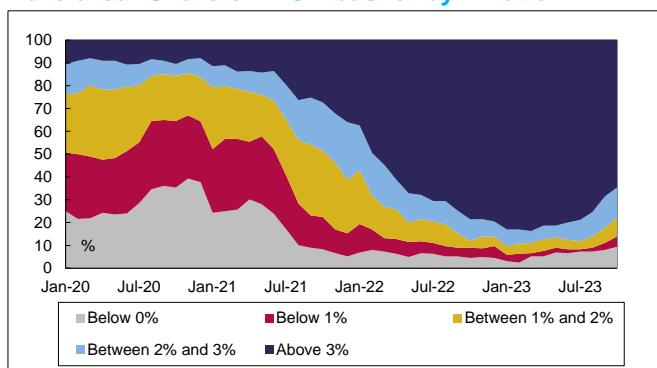
Retail sales fall well short of expectations at the start of Q4

Consistent with the downbeat signals from various retail surveys, today's UK retail sales figures suggested that the sector started the fourth quarter on the back foot as still elevated prices continued to dampen demand. Indeed, contrasting with some expectations of a bounce back from the substantial decline in September, total sales fell for a third month out of the past four in October, by 0.3% M/M. This left sales down 1.1% 3M/3M (the most since January), -2.7% Y/Y and 3.1% below the pre-pandemic benchmark in February 2020. Once again, inclement weather conditions at the start of Q4 appear to have taken a toll on demand, with unseasonably warm temperatures at the start of October deterring sales of autumnal apparel and heavy rainfall in the second half of the month reducing footfall. Given also the impact of higher petrol prices, fuel sales were the principal driver of the drop in October, down 2.0% M/M, the most since June 2022 and taking the level to its lowest since March 2021. But even when excluding fuel, sales were down in October for a second successive month (-0.1% M/M) taking them to a ten-month low, and leaving them trending some 0.8% below the Q3 average and almost 2% below the Q2 average. Indeed, food store sales fell for the first month in three (-0.3% M/M), led by a decline in sales at specialist food stores – such as bakeries and butchers – which were hit as households seemingly prioritised spending on essential food items amid an ongoing squeeze on budgets. Non-food store sales were also down for a second successive month (-0.2% M/M), reflecting further declines in clothing and furniture store sales. This was, however, partly offset by a modest pickup in non-store retailing (0.8% M/M), seemingly boosted by online promotions, such as Amazon's Big Deal Days' event. Looking ahead, despite the improvement in households' real disposable incomes, we expect consumers to remain relatively frugal in their spending as weak economic momentum and a slowing jobs market keep a lid on demand.

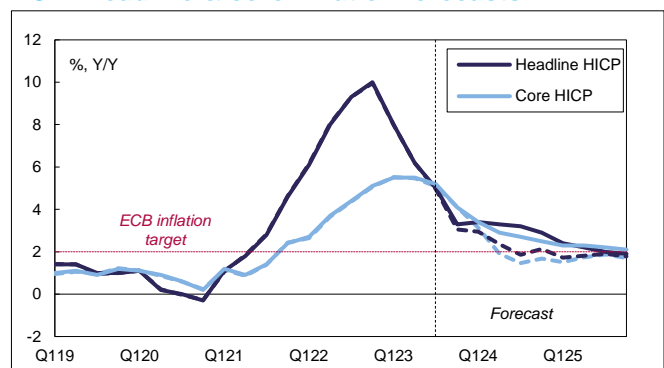
The week ahead in the UK

One key event in the coming week in the UK will come on Wednesday in the form of Chancellor Hunt's Autumn Statement and accompanying economic and fiscal forecasts from the Office for Budget Responsibility (OBR). But while the level of GDP has been revised higher than previously assumed in the publication of its forecasts last published in March, the current

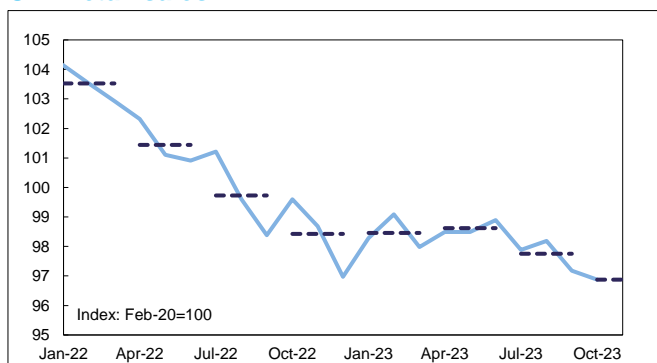
Euro area: Share of HICP basket by inflation



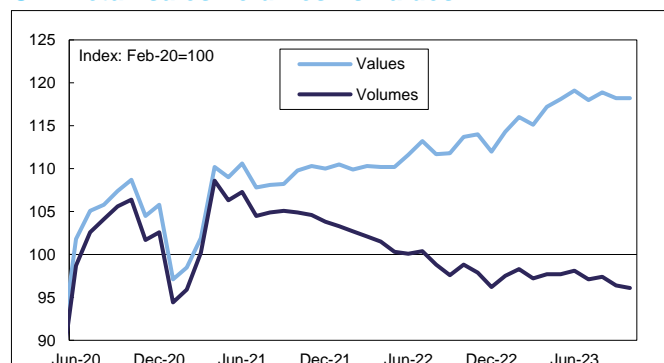
ECB: Headline & core inflation forecasts*



UK: Retail sales*



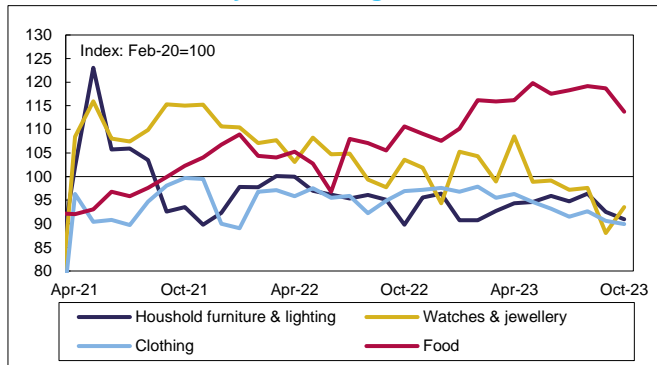
UK: Retail sales volumes vs values



economic backdrop will likely make for a relatively gloomy update. Certainly, GDP growth in H223 will be revised notably lower, with the OBR's March forecasts for full-year growth in 2024 (1.8%) and 2025 (2.5%) also set to be significantly weaker. Headline inflation is much higher than projected in March and is set to remain much firmer than the OBR previously expected over coming quarters. So, while the public finance figures in September (data due for October to be published on Tuesday) suggested that public sector net borrowing in the year-to-date was almost £20bn below the OBR's 2023 forecast profile, debt interest payments were trending slightly below expectations and public sector net debt as a percentage of GDP was lower than previously expected, the OBR's updated economic forecasts are likely to suggest little room for any significant fiscal giveaways ahead of the next general election due to be held by January 2025.

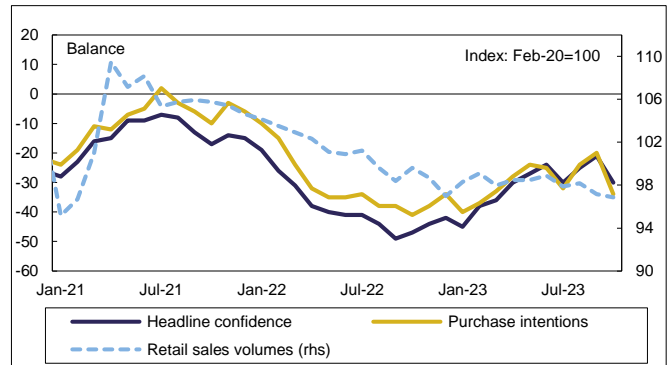
Like in the euro area, the coming week also brings the release of a number of November sentiment surveys including most notably the preliminary PMIs (Thursday). These are likely to remain consistent with an ongoing modest downturn in economic activity in the middle of Q4 and subdued domestic and external demand, with the composite PMI expected to be little improved on October's level of 48.7, to mark the fourth successive sub-50 'contractionary' reading. The CBI industrial trends survey (Wednesday) will provide additional insight into manufacturing conditions. Meanwhile, the GfK consumer survey (Friday) will offer an update on household sentiment in November. But despite an improvement in households' disposable incomes, heightened economic uncertainties and fears of job losses will keep confidence still historically low and purchasing intentions subdued.

UK: Retail sales by selected good



Source: Macrobond and Daiwa Capital Markets Europe Ltd.

UK: Retail sales & consumer confidence



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

Daiwa economic forecasts






	2023		2024				2023	2024	2025
	Q3	Q4	Q1	Q2	Q3	Q4			
GDP	%, Q/Q						%, Y/Y		
Euro area	-0.1	-0.1	0.1	0.2	0.3	0.3	0.4	0.3	1.4
UK	0.0	0.0	0.0	0.0	0.1	0.2	0.5	0.1	0.6
Inflation, %, Y/Y									
Euro area									
Headline HICP	5.0	3.1	3.0	2.4	1.9	2.1	5.5	2.3	1.8
Core HICP	5.1	4.1	3.1	1.9	1.5	1.7	5.0	2.0	1.7
UK									
Headline CPI	6.7	4.5	4.1	2.6	2.8	2.8	7.4	3.1	2.1
Core CPI	6.4	5.6	5.1	3.3	2.8	2.7	6.2	3.4	2.0
Monetary policy, %									
ECB									
Refi Rate	4.50	4.50	4.50	4.25	4.00	3.75	4.50	3.75	3.25
Deposit Rate	4.00	4.00	4.00	3.75	3.50	3.25	4.00	3.25	2.75
BoE									
Bank Rate	5.25	5.25	5.25	5.25	5.00	4.75	5.25	4.75	3.00

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	 ECB current account balance €bn	Sep	31.2	-	27.7	30.8
	 Final HICP (core HICP) Y/Y%	Oct	2.9 (4.2)	2.9 (4.2)	4.3 (4.5)	-
Spain	 Trade balance €bn	Sep	-3.8	-	-4.4	-
UK	 Retail sales incl. auto fuels M/M% (Y/Y%)	Oct	-0.3 (-2.7)	0.4 (-1.6)	-0.9 (-1.0)	-1.1 (-1.3)
	 Retail sales excl. auto fuels M/M% (Y/Y%)	Oct	-0.1 (-2.4)	0.4 (-1.6)	-1.0 (-1.0)	-1.3 (-1.5)


Auctions

Country	Auction
- Nothing to report -	










Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

Yesterday's results

Economic data

Country	Release	Period	Actual	Market consensus/ <i>Daiwa forecast</i>	Previous	Revised
Italy	 Trade balance €bn	Sep	2.3	-	2.1	2.0





















Auctions

Country	Auction
France	 sold €3.15bn of 2.50% 2026 bonds at an average yield of 2.98%  sold €2.43bn of 0.75% 2028 bonds at an average yield of 2.89%  sold €3.50bn of 2.75% 2029 bonds at an average yield of 2.92%  sold €635mn of 0.1% 2029 index-linked bonds at an average yield of 0.7%  sold €850mn of 0.1% 2036 index-linked bonds at an average yield of 0.99%  sold €263mn 0.1% 2053 index-linked bonds at an average yield of 1.01%
Spain	 sold €847 mn of 2.80% 2026 bonds at an average yield of 3.245%  sold €1.587bn of 3.55% 2033 bonds at an average yield of 3.61%  sold €1.92bn of 3.45% 2043 bonds at an average yield of 4.132%

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

The coming week's data calendar

The coming week's key data releases

Country	GMT	Release	Period	Market consensus/ <i>Daiwa</i> <i>forecast/actual</i>	Previous
Monday 20 November 2023					
Euro area 	10.00	Construction output M/M% (Y/Y%)	Sep	-	-1.1 (-0.1)
Germany 	07.00	PPI Y/Y%	Oct	-11.0	-14.7
Tuesday 21 November 2023					
Euro area 	07.00	EU27 new car registrations Y/Y%	Oct	-	9.2
France 	-	Bank of France retail sales Y/Y%	Oct	-	-4.3
UK 	07.00	Public sector net borrowing (ex banks) £bn	Oct	-	13.5 (14.3)
Wednesday 22 November 2023					
Euro area 	15.00	European Commission's preliminary consumer confidence index	Nov	-17.6	-17.9
UK 	11.00	CBI industrial trends, total orders (selling prices) balance %	Nov	-	-26 (7)
Thursday 23 November 2023					
Euro area 	09.00	Preliminary manufacturing (services) PMI	Nov	43.3 (48.0)	43.1 (47.8)
Euro area 	09.00	Preliminary composite PMI	Nov	46.9	46.5
Germany 	08.30	Preliminary manufacturing (services) PMI	Nov	41.1 (48.3)	40.8 (48.2)
Germany 	08.30	Preliminary composite PMI	Nov	46.5	45.9
France 	07.45	INSEE business (manufacturing) confidence index	Nov	98 (98)	98 (98)
France 	08.15	Preliminary manufacturing (services) PMI	Nov	43.3 (45.6)	42.8 (45.2)
France 	08.15	Preliminary composite PMI	Nov	44.6	44.6
UK 	09.30	Preliminary manufacturing (services) PMI	Nov	45.0 (49.5)	44.8 (49.5)
UK 	09.30	Preliminary composite PMI	Nov	48.4	48.7
Friday November 2023					
Germany 	07.00	GDP – second estimate Q/Q% (Y/Y%)	Q3	<u>-0.1 (-0.3)</u>	0.1 (0.0)
Germany 	09.00	Ifo business climate index	Nov	87.4	86.9
Germany 	09.00	Ifo current assessment (expectations) index	Nov	89.4 (85.5)	89.2 (84.7)
Spain 	08.00	PPI Y/Y%	Oct	-	-8.6
UK 	00.01	GfK consumer confidence index	Nov	-31	-30

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

The coming week's key events & auctions

Country	GMT	Event / Auction
Monday 20 November 2023		
Euro area	 07.00	ECB Chief Economist Lane scheduled to speak
Tuesday 21 November 2023		
Euro area	 16.00	ECB President Lagarde scheduled to speak
	 17.00	ECB's Schnabel scheduled to speak
Germany	 10.30	Auction: €3.5bn of 2.4% 2028 bonds
Wednesday 22 November 2023		
Euro area	 09.00	ECB to publish Financial Stability Report
Germany	 10.30	Auction: €1bn of 1% 2038 bonds
	 10.30	Auction: €500mn of 0% 2035 bonds
UK	 12.30	Chancellor of the Exchequer presents the Autumn Statement
Thursday 23 November 2023		
Euro area	 12.30	ECB to publish account of October Governing Council monetary policy meeting
	 21.30	ECB's Schnabel scheduled to speak
Friday 24 November 2023		
Euro area	 10.00	ECB's Lagarde scheduled to speak
	 13.00	ECB's de Guindos scheduled to speak
Italy	 10.00	Auction: Fixed rate and index-linked bonds

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

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