

Euro wrap-up

Overview

- Bunds made modest losses while the flash euro area activity and employment PMIs were softer than expected, but the survey's price indices rose sharply.
- Gilts underperformed as the UK PMIs, consumer confidence and retail sales data beat expectations.
- The coming week will bring the first estimates of Q4 GDP from the euro area and member states and January inflation from Germany, as well as various sentiment surveys and bank lending data.

Economic Research Team

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Daily bond market movements

Bond	Yield	Change
BKO 2 12/27	2.122	+0.014
OBL 2 1/2 04/31	2.492	+0.015
DBR 2.9 02/36	2.891	+0.006
UKT 3 3/4 03/27	3.694	+0.028
UKT 4% 03/30	3.949	+0.027
UKT 4 1/2 03/35	4.489	+0.016

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

Source: Bloomberg

Euro area

Flash euro area January PMIs miss expectations despite improvement in Germany

The flash euro area PMIs were a touch softer than expected, suggesting a possible loss of growth momentum around the turn of the year. Contrary to expectations of a rise, the headline euro area composite PMI was unchanged at 51.5, more than 1pt below November's 2½-year high and 0.8pt below the Q4 average. By sector, the reason for the forecast miss was the reported weakening in services, for which the activity PMI dropped ½pt to a four-month low of 51.9. In contrast, the manufacturing output PMI rose 1.3pt to 50.2 to suggest stabilisation in the factory sector after a deterioration at end-2025. Given the country breakdown, we were not overly concerned by the flat euro area composite PMI. In particular, the equivalent German index rose 1.2pts to 52.5, the second-best reading in more than 2½ years to match the Q4 average. That signalled the likelihood of a second-successive quarter of expansion in the euro area's largest member state in Q1 thanks to improvement in services and manufacturing alike. And the headline index for the euro area excluding Germany and France edged down just 0.2pt to 52.6, still above the long-run average, suggesting that Southern Europe still leads the way despite some inclement winter weather.

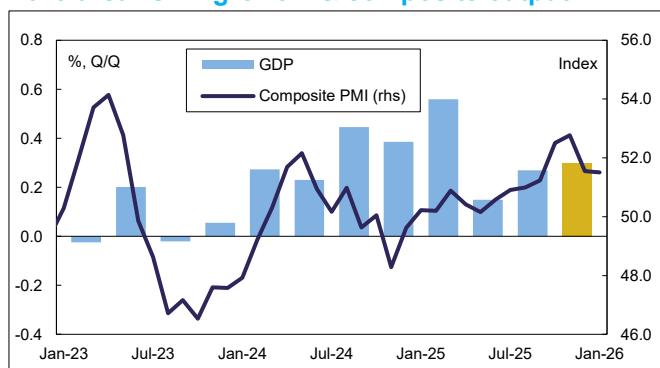
Disappointment in PMIs due to France where INSEE paints a brighter picture

So, among the member states, the downbeat tone was associated with France for which the composite output PMI fell 1.4pts to a three-month low of 48.6 due to a reported marked deterioration in services. While that might appear to point to contraction in French economic activity, as ever we are placing more weight on the INSEE business survey, which has a much larger sample and has provided a more reliable guide to growth over past quarters. Encouragingly, the INSEE indices pointed to steady French expansion in January in line with the growth of ¼%Q/Q we expect to see confirmed for Q4. The headline INSEE business climate index was unchanged at 99, just 1ppt below the long-run average. The detail suggested that French services continue to grow moderately, albeit a little below the long-run average pace and with variation across subsectors. ICT, real estate and logistical and distribution services were firmer but hospitality was weaker. French retailers were also more downbeat, albeit conditions were judged to be only marginally less favourable than normal. Most striking, however, the INSEE survey suggested the strongest expansion in French manufacturing in 3½ years led by significant vigour in non-autos transport goods where the business climate was judged to match the best in the 36-year series. Conditions in several other manufacturing subsectors, from motor vehicles to chemicals and textiles, were also judged to have improved.

Job growth absent at start of the year as input costs reportedly rise the most in 11 months

One area where the messages of the INSEE survey and PMIs aligned was the labour market as firms appeared reluctant to hire at the start of the year. Indeed, the euro area composite employment PMI slipped to an 11-month low (49.5) consistent

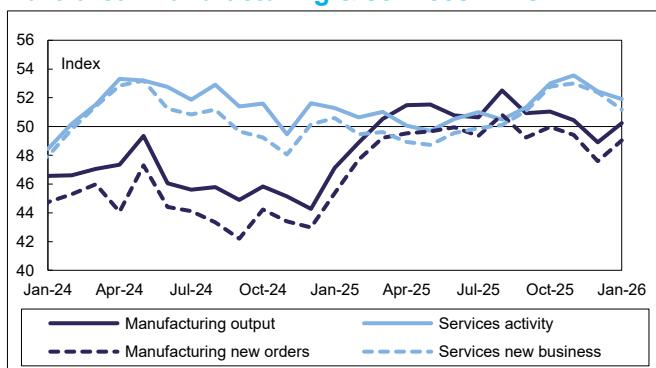
Euro area: GDP growth* & composite output PMI



*Gold bar represents Daiwa's GDP forecast for Q425.

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

Euro area: Manufacturing & services PMIs



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

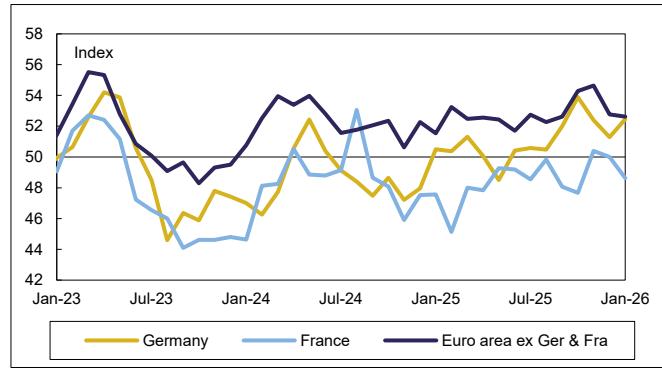
with headcount cuts, particularly in German manufacturing. The PMIs implied no job growth in services too, again reflecting a notable deterioration in Germany where the respective index was the lowest since the first Covid-19 wave. And the INSEE employment climate index fell to lowest level since April 2021, and well below the long-run average, similarly due to weakness in labour demand in French services. One reason might be new cost pressures, whether from pay (including higher minimum wages) or energy, transport and metals. Indeed, the euro area composite input price PMI rose in January back above the long-run average to an 11-month high (57.8), led by a pickup in the factory sector. The survey suggested that manufacturers struggled to pass on these costs due to soft demand. But prices charged by services also reportedly rose the most in 11 months and at an above-average pace with the respective German index jumping more than 5pts to the highest level since mid-2021. We doubt that this impact on services prices will be long-lasting. But it will provide a reminder to the Governing Council that a substantive and persistent undershooting of the ECB's inflation target is unlikely to materialise over the horizon in the absence of a major new negative shock to demand.

The week ahead in the euro area

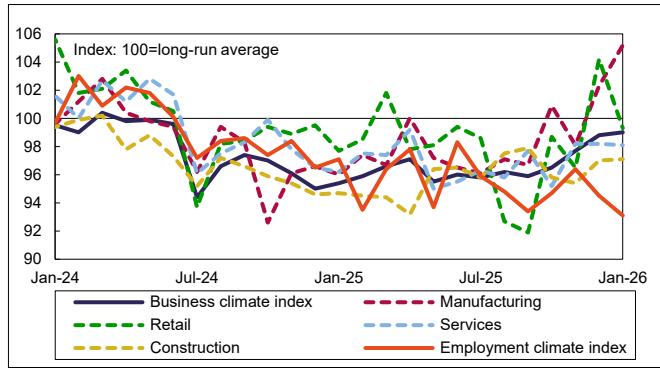
First estimates of Q4 GDP growth in the euro area and several member states (Friday) will provide the highlight of the coming week's European dataflow. In keeping with prior quarters, GDP growth showed encouraging resilience in Q325, accelerating a little more than $\frac{1}{4}\%$ Q/Q as higher government spending and a rebound in fixed investment offset the drag from net trade. Forward-looking surveys have suggested that growth momentum remained firm into Q4, while the industrial and construction sectors look set to contribute positively for the first quarter since Q1. So, we see euro area GDP picking up by a similar pace, around $\frac{1}{4}\%$ Q/Q, in Q4. We expect output to have risen across each of the largest member states. Having narrowly avoided a technical recession by virtue of flatlining in Q3, Germany likely returned to growth in Q4 for the first quarter in three. We expect output to have risen 0.2% Q/Q, consistent with the preliminary whole-year estimate released recently. First GDP estimates from France – which alongside that of Spain will include an expenditure breakdown – are likely to report a similar outturn, albeit in that instance representing a slowdown from growth of 0.5% Q/Q in Q3. Surveys also suggest that Italian growth might have quickened last quarter, potentially rounding up to 0.2% Q/Q, while continued Spanish outperformance in excess of $\frac{1}{2}\%$ Q/Q looks more assured. Irish estimates, which are due (Thursday) just ahead of the euro area release, will also be closely watched given their recent tendency to have an outsized effect on the aggregate data.

The end of the coming week will also bring the first of January's flash inflation estimates, most notably from Germany and Spain. Inflation in the former eased significantly last month, down 0.6ppt to a target-consistent 2%Y/Y. Offsetting policy measures are expected to keep inflation hovering close to that rate this month, although we see the risks as skewed to the downside. Despite an increase in the national carbon prices affecting heating oil and auto fuels, the effects from lower grid fees on electricity prices should weigh on energy inflation. That will be countered by the effects of a higher "Deutschland

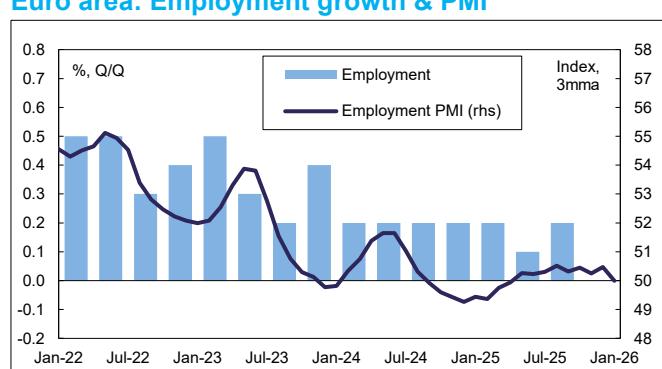
Euro area member states: Composite output PMIs



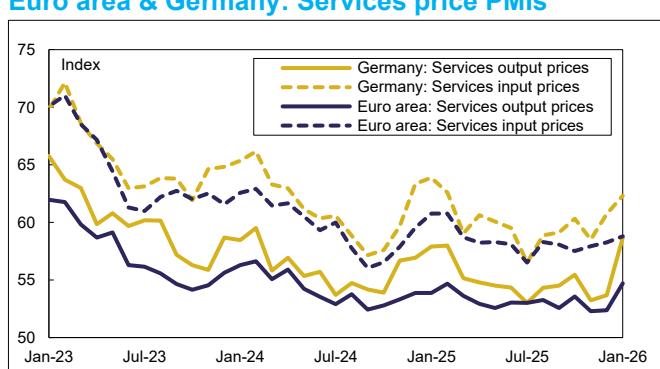
France: INSEE business sentiment indices



Euro area: Employment growth & PMI



Euro area & Germany: Services price PMIs



"ticket" price for transport services, while the combined impact of January's minimum wage increase and a cut to VAT for certain hospitality businesses create more uncertainty than usual. Spanish inflation is expected to fall more sharply at the start of the year, with the energy component likely to fall away entirely owing to favourable base effects. Friday also brings insights about underlying price trends at the end of last year, including German import price indices and PPI data from France and Italy. Updated labour market data are also due. Barring revisions, the euro unemployment rate will be expected to have trended sideways at 6.3% last month, close to its series low, while January data from Germany will provide a timelier insight as to conditions in the largest member state.

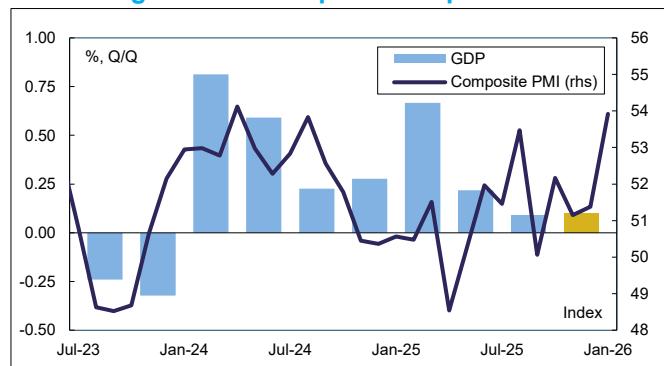
Otherwise, the start of the week will continue the steady flow of January's business surveys. The Commission's economic sentiment surveys (Thursday) and German ifo (Monday) will cross-check today's flash PMIs, while Istat's surveys (Wednesday) will provide the first insights for business and consumer confidence in Italy this year. The uptick in consumer confidence flagged by the Commission's flash reading and improved investor sentiment might also imply some payback for recent weakness for the German GfK survey (Wednesday). But as we [noted](#) on its release, recent geopolitical events and the (since withdrawn) threats of new tariffs from the US introduces downside risks for sentiment in Germany and France (Tuesday) in particular. December's euro area bank lending figures (Thursday) are also due.

UK

UK flash PMIs surprise to the upside, signalling fastest private-sector expansion since April 2024

To the extent that sluggish GDP growth in Q4 could be attributed to the hangover from September's JLR shutdown and extensive pre-Budget uncertainty, we expect a bounce back in Q1, which might also be interpreted in a continued moderate uptrend in the PMIs. As it happens, January's flash composite output PMI surprised significantly to the upside. An increase of 2½pts was the sharpest in almost three years, and at 53.9 the index was consistent with its fastest private-sector expansion since April 2024. As is often the case, the boost to activity was driven by the dominant services sector, for which the activity PMI jumped almost 3pts to 54.3. Financial services and tech businesses supposedly led that boost, while the survey also noted a rebound in projects that had previously been put on ice until Budget uncertainty lifted. New business continued to rise only modestly, but firms were at least not running down backlogs, perhaps hinting to a healthier stabilisation of future work pipelines. Moreover, the manufacturing sector offered ongoing support to growth momentum, with its respective output PMI up ½pt to 51.5. And with new factory orders also the firmest since February 2022 and export orders expanding for the first time in four years, the headline manufacturing PMI also rose a full 1pt, to 51.6, a 16-month high. Overall, the index for future output expectations rallied 2pts to 71.0, the best since before the preceding Budget in October 2024.

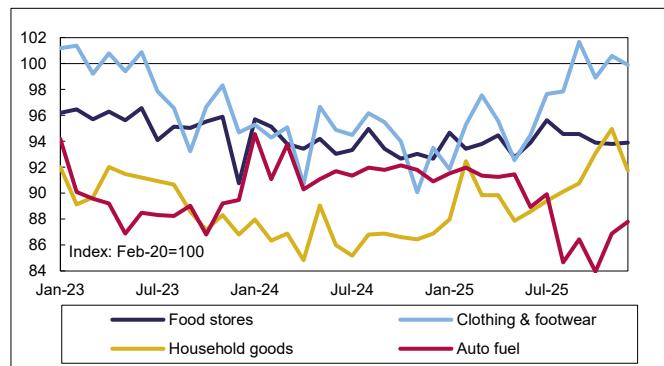
UK: GDP growth* & composite output PMI



*Gold bar represents Daiwa's GDP forecast for Q425.

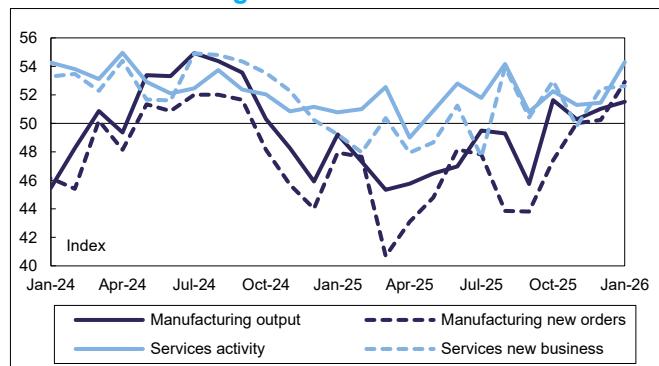
Source: S&P Global, Macrobond and Daiwa Capital Markets Europe Ltd.

UK: Retail sales volumes



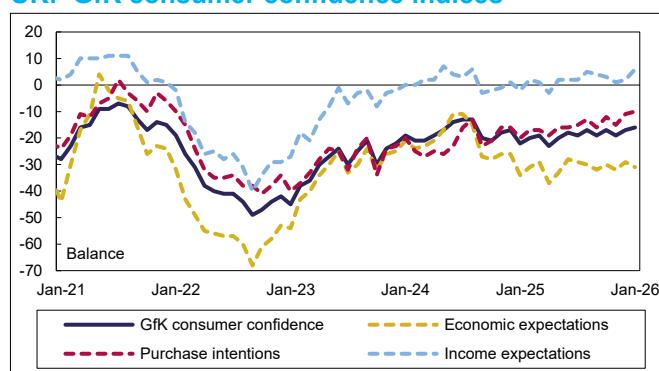
Source: Macrobond and Daiwa Capital Markets Europe Ltd.

UK: Manufacturing & services PMIs



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

UK: GfK consumer confidence indices



Source: Macrobond and Daiwa Capital Markets Europe Ltd.

Retail sales drop in Q4, but rise in December & improved confidence points to recovery ahead

Today's retail sales data and consumer confidence survey results also beat (admittedly weak) expectations to raise cautious optimism that domestic demand has started to turn for the better. Total retail sales volumes rose for the first month in three in December, by 0.4%M/M, led by a modest increase in food store sales, further growth in sales of auto fuel and a rebound in non-store retailing. This left them up 2.5%Y/Y, the strongest annual pace for eight months. But weakness in prior months caused sales volumes to fall 0.3%Q/Q in Q4, contrasting markedly with growth of 1%Q/Q or more in the first three quarters of the year. The weakness last quarter largely reflected a drop in food and online sales, while solid growth in non-food stores, particularly of household goods, suggested ongoing recovery in discretionary spending amid reports of widespread discounting. According to the GfK survey, consumer confidence rose to a 17-month high in January, albeit with the headline index (-16) remaining some way below the long-run average. Admittedly, households were somewhat more downbeat about the economic outlook for the coming 12 months. And there was an uptick in savings intentions again at the start of the year. Nevertheless, with income expectations the highest since mid-2024, household purchase intentions were the strongest for three years, pointing to a return to retail sales growth this quarter and a likely pickup in overall consumer spending too.

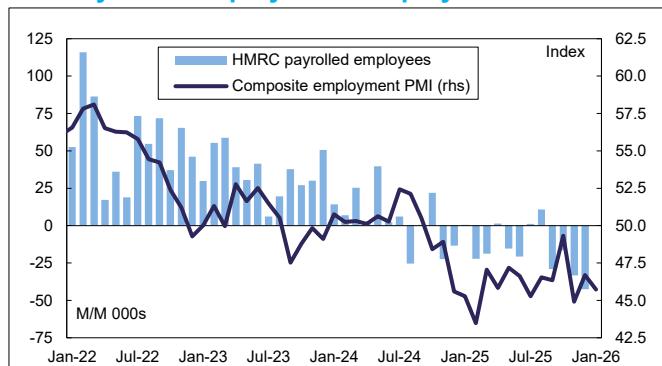
PMIs to reinforce MPC caution and raise questions about the timing of further rate cuts

At the very least, today's data will have cemented a cautious tone from the MPC when it next meets in the first week of February. Signs of firmer activity, at least temporarily, should allay some of the concerns about risks of persistent demand weakness. And some MPC members will likely be discouraged by the flash price PMIs, which could be seen as reinforcing concerns about the sustainability of underlying disinflation. For the services sector, increases in input costs reportedly remained elevated, while the respective output price PMI edged up to a nine-month high. Crucially, those underlying pressures allegedly owed to wages, which might have contributed to the persistent weakness of the employment PMI which was consistent with falling labour demand for a 16th consecutive month. In net, those signals reinforce our expectation that the BoE won't cut rates in Q1 for the first quarter in six. And to the extent that the data infer a greater risk of inflation persistence, they present a risk to our assumption about the timing of further cuts this year. In defence of our view, to the extent that the PMIs' strength might merely reflect payback for weakness in Q4 and perhaps a similar seasonal pattern to recent years, we think that it is unlikely that the momentum in January flash PMIs will be fully sustained. Still-weak hiring dynamics should continue to exert further downwards pressure on wage growth. And with inflation due to take a mechanical step down in Q2, we continue to forecast headline CPI converging gradually back to the inflation target over the coming quarters. We continue to expect the BoE to cut two additional times this year, which we currently have pencilled in for Q2 and Q3.

The week ahead in the UK

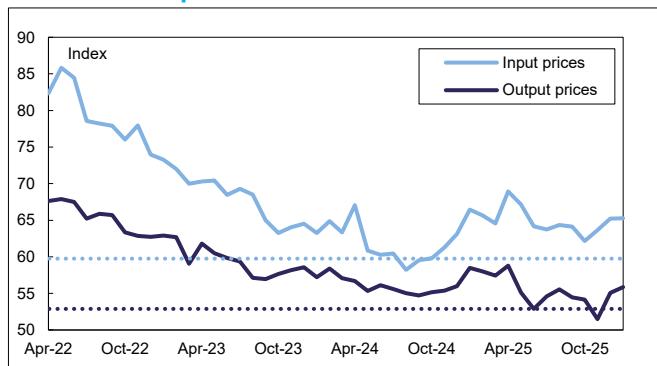
It will be a quieter week ahead for top-tier UK economic data. The first half of the week will bring just the BRC's shop price monitor for January which will provide a first insight into price pressures on the high street at the start of 2026. While food price inflation is likely to have remained elevated, we expect the BRC's measure of non-food inflation to remain firmly in negative territory as retailers extend discounts to entice consumers. Overall, the BRC's shop price inflation estimate will likely remain below 1%Y/Y, suggesting that core goods CPI inflation remained subdued into the New Year too. Meanwhile, the back end of the week will bring the BoE's monetary data for December. While mortgage lending remained solid in November (£4.5bn), the number of new mortgage approvals edged down to a five-month low, suggesting a possible slowing in secured lending growth around the turn of the year. In contrast, growth in consumer credit and business lending might well remain firm as Budget-related uncertainty continued to fade.

UK: Payrolled employees & employment PMI



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

UK: Services price PMIs*



*Dotted lines show long-run averages.
Source: S&P Global, Macrobond and Daiwa Capital Markets Europe Ltd.

Daiwa economic forecast

	2025		2026				2025	2026	2027	
	Q3	Q4	Q1	Q2	Q3	Q4				
GDP	%, Q/Q							%, Y/Y		
Euro area		0.3	0.3	0.3	0.3	0.3	0.3	1.4	1.1	1.3
UK		0.1	0.1	0.2	0.3	0.3	0.3	1.4	0.9	1.3
Inflation, %, Y/Y										
Euro area										
Headline HICP		2.1	2.1	1.7	1.7	1.6	1.8	2.1	1.7	1.8
Core HICP		2.3	2.4	2.3	1.8	1.6	1.7	2.4	1.8	1.6
UK										
Headline CPI		3.8	3.4	3.0	2.3	2.4	2.4	3.4	2.5	2.1
Core CPI		3.6	3.3	3.1	2.5	2.6	2.6	3.5	2.7	1.9
Monetary policy, %										
ECB										
Deposit Rate		2.00	2.00	2.00	2.00	2.00	2.00	2.00	2.00	2.00
Refi Rate		2.15	2.15	2.15	2.15	2.15	2.15	2.15	2.15	2.15
BoE										
Bank Rate		4.00	3.75	3.75	3.50	3.25	3.25	3.75	3.25	3.25

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	 Preliminary services (manufacturing) PMI	Jan	51.9 (49.4)	52.6 (49.2)	52.4 (48.8)	-
	 Preliminary composite PMI	Jan	51.5	51.9	51.5	-
Germany	 Preliminary services (manufacturing) PMI	Jan	53.3 (48.7)	52.5 (47.8)	52.7 (47.0)	-
	 Preliminary composite PMI	Jan	52.5	51.7	51.3	-
France	 Preliminary services (manufacturing) PMI	Jan	47.9 (51.0)	50.3 (50.5)	50.1 (50.7)	-
	 Preliminary composite PMI	Jan	48.6	50.0	50.0	-
UK	 INSEE business (manufacturing) confidence indicator	Jan	99 (105)	99 (101)	99 (102)	-
	 INSEE production outlook (own company) indicator	Jan	-4 (17)	-7 (9)	-7 (11)	-6 (10)
	 Retail sales – incl. auto fuels M/M% (Y/Y%)	Dec	0.4 (2.5)	0.0 (1.1)	-0.1 (0.6)	- (1.8)
	 Retail sales – excl. auto fuels M/M% (Y/Y%)	Dec	0.3 (3.1)	-0.1 (-1.7)	-0.2 (1.2)	-0.4 (2.6)
	 Preliminary services (manufacturing) PMI	Jan	54.3 (51.6)	51.7 (50.5)	51.4 (50.6)	-
	 Preliminary composite PMI	Jan	53.9	51.5	51.4	-
	 GfK consumer confidence indicator	Jan	-16	-16	-17	-

Auctions

Country	Auction
- Nothing to report -	

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/ <u>Daiwa forecast</u>	Previous
Monday 26 January 2026					
Germany	09.00	ifo business climate indicator	Jan	88.2	87.6
	09.00	ifo current assessment (expectations) indicator	Jan	86.0 (90.3)	85.6 (89.7)
Tuesday 27 January 2026					
Euro area	05.00	New car registrations Y/Y%	Dec	-	2.3
France	07.45	INSEE consumer confidence indicator	Jan	90	90
Spain	08.00	Unemployment rate %	Q4	-	10.45
UK	00.01	BRC shop price index Y/Y%	Jan	0.7	0.7
Wednesday 28 January 2026					
Germany	07.00	GfK consumer confidence indicator	Feb	-25.8	-26.9
Italy	09.00	Istat economic (manufacturing) confidence indicator	Jan	-	96.5 (88.4)
	09.00	Istat consumer confidence indicator	Jan	-	96.6
Thursday 29 January 2026					
Euro area	09.00	M3 money supply Y/Y%	Dec	3.0	3.0
	10.00	Commission economic sentiment indicator	Jan	97.0	96.7
	10.00	Commission services (industrial) confidence indicator	Jan	6.0 (-8.4)	5.6 (-9.0)
France	10.00	Final Commission consumer confidence indicator	Jan	<u>-12.4</u>	-13.2
Italy	11.00	Total jobseekers mns	Q4	-	3.05
Spain	11.00	Hourly wages M/M% (Y/Y%)	Q4	-	0.0 (2.6)
	08.00	Retail sales Y/Y%	Dec	-	6.0
Friday 30 January 2026					
Euro area	09.00	ECB consumer expectations survey – 1Y (3Y) ahead CPI Y/Y%	Dec	2.7 (2.4)	2.8 (2.5)
	10.00	GDP – first estimate Q/Q% (Y/Y%)	Q4	<u>0.3 (1.2)</u>	0.3 (1.4)
	10.00	Unemployment rate %	Dec	6.3	6.3
Germany	07.00	Import prices M/M% (Y/Y%)	Dec	-	0.5 (-1.9)
	08.55	Unemployment claims rate % (change 000s)	Jan	6.3 (3)	6.3 (3)
	09.00	GDP – first estimate Q/Q% (Y/Y%)	Q4	<u>0.2 (0.2)</u>	0.0 (0.3)
France	13.00	Preliminary HICP (CPI) Y/Y%	Jan	2.0 (2.0)	2.0 (1.8)
	06.30	GDP – first estimate Q/Q% (Y/Y%)	Q4	<u>0.2 (1.2)</u>	0.5 (0.9)
	06.30	Consumer spending M/M% (Y/Y%)	Dec	-0.4 (-0.6)	-0.3 (0.0)
Italy	07.45	PPI Y/Y%	Dec	-	-3.3
	09.00	GDP – first estimate Q/Q% (Y/Y%)	Q4	<u>0.2 (0.6)</u>	0.1 (0.6)
	11.00	PPI Y/Y%	Dec	-	-0.3
Spain	08.00	GDP – first estimate Q/Q% (Y/Y%)	Q4	<u>0.6 (2.9)</u>	0.6 (2.8)
	08.00	Preliminary HICP (CPI) Y/Y%	Jan	2.4 (2.3)	3.0 (2.9)
UK	09.30	Net consumer credit £bn (Y/Y%)	Dec	-	2.1 (8.1)
	09.30	Net mortgage lending £bn (approvals 000s)	Dec	-	4.5 (64.5)

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

The coming week's key events & auctions

Country	GMT	Event / Auction
Monday 26 January 2026		
Germany	11.00	Bundesbank President Nagel to give speech on the outlook for 2026, Berlin
	13.30	Bundesbank President Nagel to discuss monetary policy before the Bundestag, Berlin
Tuesday 27 January 2026		
Germany	10.30	Auction: to sell up to €6bn of 2028 bonds
Italy	10.00	Auction: to sell up to €3bn of 2.2% 2028 bonds
	10.00	Auction: to sell up to €1bn of 1.1% 2031 inflation-linked bonds
	10.00	Auction: to sell up to €1bn of 2.55% 2056 inflation-linked bonds
UK	10.00	Auction: to sell £3.25bn of 4.125% 2033 bonds
Wednesday 28 January 2026		
Euro area	10.00	Eurostat to publish household sector accounts for Q325
	18.00	ECB Executive Board member Schnabel to give a presentation in Frankfurt
Germany	10.30	Auction: to sell up to €6bn of 2.9% 2036 bonds
Thursday 29 January 2026		
Italy	10.00	Auction: to sell bonds*
UK	10.00	Auction: to sell £1.25bn of 0.125% 2028 bonds
Friday 30 January 2026		
- Nothing scheduled -		

*Details to be announced. Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

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