

Euro wrap-up

Overview

- While euro area unemployment fell to a series low and core producer prices rose the most in three years, shorter-dated Bunds followed USTs higher as energy prices stabilised after their recent marked jump.
- Gilts also made modest gains despite the final UK PMIs suggesting firmer growth in GDP and external demand in Q1.
- Thursday will bring euro area retail sales and French industrial production data for January, the latest construction PMIs and the ECB's account of its February policy-setting meeting.

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Daily bond market movements

Bond	Yield	Change
BKO 2.1 03/28	2.123	-0.021
OBL 2½ 04/31	2.365	-0.010
DBR 2.9 02/36	2.745	-0.004
UKT 4¾ 03/28	3.701	-0.027
UKT 4¾ 03/31	3.927	-0.029
UKT 4¾ 10/35	4.440	-0.028

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

Euro area

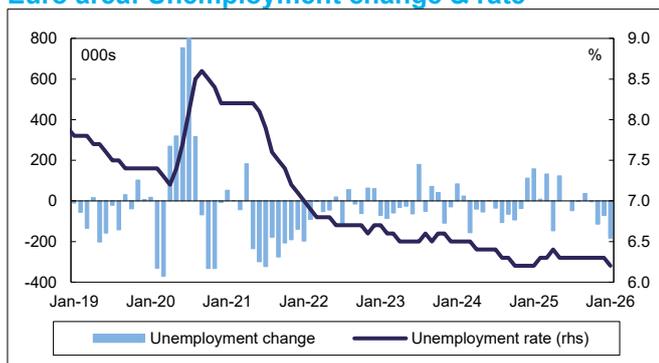
Unemployment falls to series low thanks to sharp decline in Italy

While the energy price shock triggered by events in the Middle East will add to business costs and weigh on sentiment and economic growth, the ECB will take comfort from the positive momentum ahead of the outbreak of war. One source of that resilience was the labour market as employment continued to rise and unemployment remained low and stable over the past year despite multiple shocks. Today's data reported a 10bp drop in the euro area unemployment rate in January to a new series low of 6.1%, 20bps lower than a year earlier. The decline in the number of jobless workers (-184k) was the steepest in four years. As in six of the prior seven months, the improvement was led by Italy where the number of people out of work fell 100k and the unemployment rate fell 0.4ppt to 5.1%, the lowest on the four-decade series. Elsewhere, the equivalent rate in Spain, where job growth has been strongest, fell below 10% for the first time in almost 18 years. French unemployment declined for a second successive month to 7.7%, still nevertheless 40bps above the level a year earlier. And the German unemployment rate on the ILO measure remained unchanged at 4.0%, up 50bps on a year earlier. The rise of more than 1.1mn in employment in the euro area in 2025 benefited in part from higher labour force participation reflecting additional supply of immigrant workers. And according to the ECB, increased labour demand was also partly a function of greater use of AI. According to its SAFE survey, firms making significant use of AI or investing in AI were more likely to take on additional workers than those that rarely use it or were not investing in the technology. And, while the employment PMIs pointed to softer growth in labour demand in the middle of Q1, firms planning to invest in AI over the coming year also had more positive expectations for future headcount growth.

PMIs remain consistent with positive services growth, but risks to outlook skewed to downside

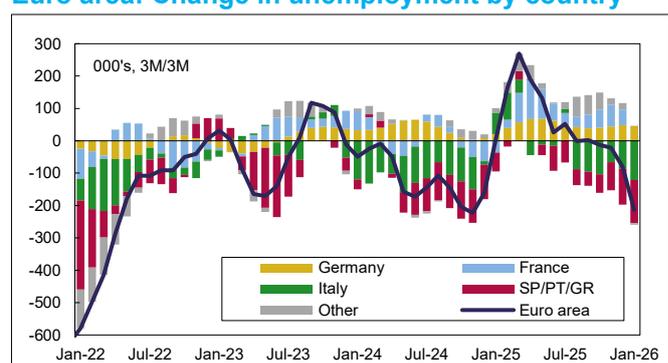
Today's final composite output PMIs for February suggested a modest pickup in economic growth ahead of the war after a moderation at the start of the year. The euro area output index rose 0.6pt to a three-month high of 51.9. That, however, left the average for the first two months of Q1 some 0.7pt below the Q4 average. And given the energy price shock, we might expect to see a deterioration this month. Today's survey results suggested that growth in services was relatively subdued in February, with the respective index (51.9) tracking some 1.2pts below the Q4 average. That was weighed in part by a weakening in Spain to an eight-month low (51.9), trending 3.8pts below the Q4 level, which contrasted markedly with the Commission's Spanish [Economic Sentiment Index](#) that implied the strongest expansion since Q324. Elsewhere, despite a boost from the Winter Olympics, Italy's services PMI (52.3) also fell slightly in February below the Q4 average. And while the respective German index (53.5) was the firmest in four months and above the long-run average, higher energy prices will likely weigh on spending in the sector over coming months.

Euro area: Unemployment change & rate



Source: Macrobond and Daiwa Capital Markets Europe Ltd.

Euro area: Change in unemployment by country

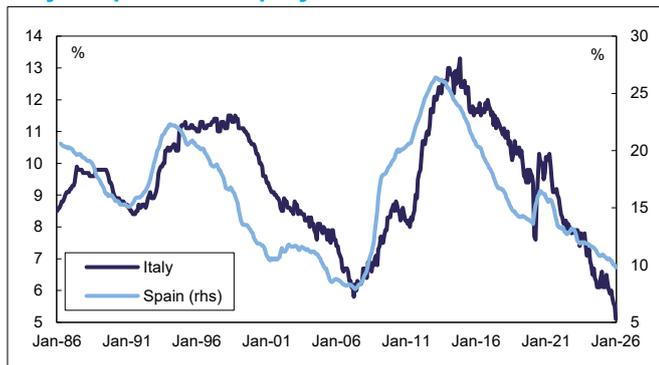


Source: Macrobond and Daiwa Capital Markets Europe Ltd.

Core producer prices rose the most in 3 years even before the latest spike in energy prices

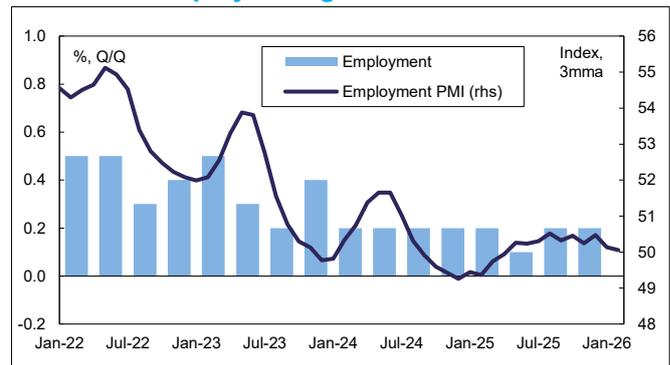
The improvement in the PMIs in February reflected evidence of further recovery in [manufacturing](#). And given the recent rise in order backlogs, factory production should be relatively well maintained over the near term. But, as in 2022, production in energy-intensive subsectors – such as chemicals, metal, paper and glassware – is likely to be hit hard by the spike in wholesale gas prices. And while the new factory orders PMI rose in February to the highest level since mid-2022, this might be expected to fall back sharply if the conflict persists. Even before the outbreak of war, producer prices had risen since the start of the year, with today's euro area PPI data showing prices of core goods (excluding energy) accelerating 0.5%M/M in January, the most in two years. And while headline PPI inflation (-2.2%Y/Y) was the most negative since October 2024, that reflected a significant drag from energy (-9.1%Y/Y), which seems bound to reverse imminently. In services, meanwhile, the PMIs suggested that costs remained relatively contained in February. But wage pressures reportedly remained a concern. And if demand in the sector holds up, the new energy price shock will no doubt keep services inflation higher for longer.

Italy & Spain: Unemployment rates



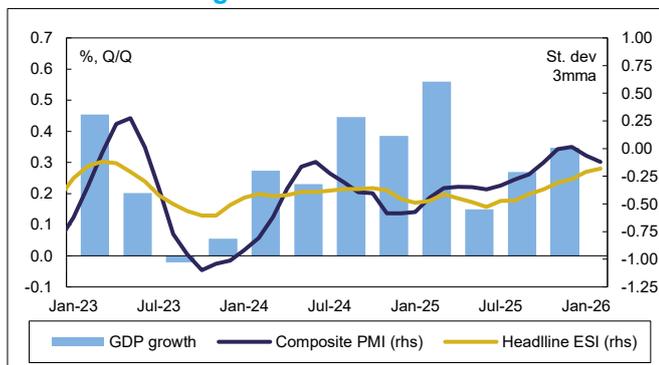
Source: Macrobond and Daiwa Capital Markets Europe Ltd.

Euro area: Employment growth & PMI



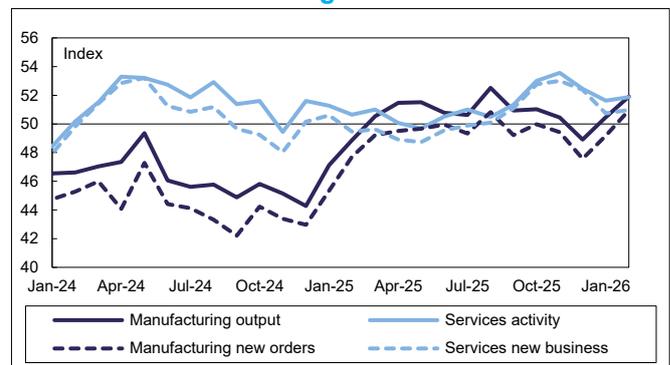
Source: S&P Global, Macrobond and Daiwa Capital Markets Europe Ltd.

Euro area: GDP growth & sentiment indices



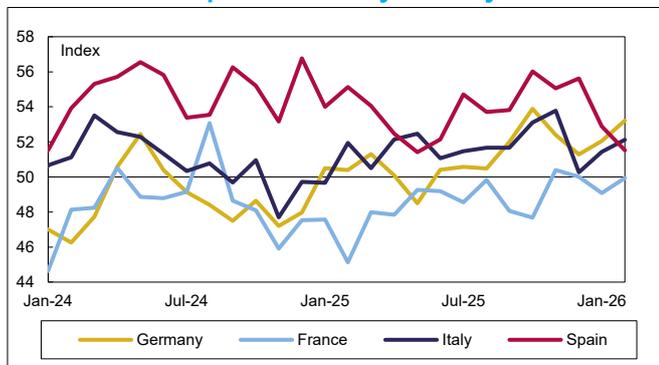
Source: S&P Global, EC, Macrobond and Daiwa Capital Markets Europe Ltd.

Euro area: Manufacturing & services PMIs



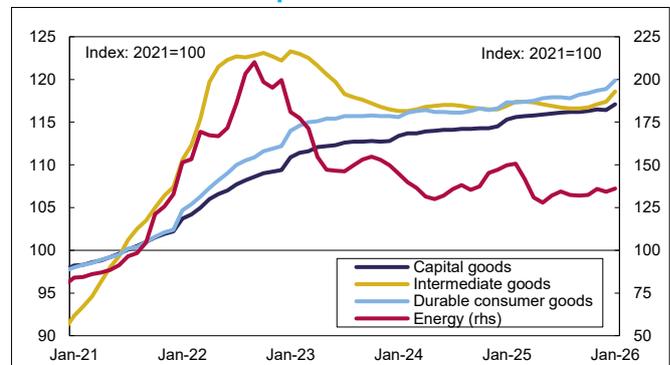
Source: S&P Global, Macrobond and Daiwa Capital Markets Europe Ltd.

Euro area: Composite PMIs by country



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

Euro area: Producer price indices



Source: Macrobond and Daiwa Capital Markets Europe Ltd.

The day ahead in the euro area

Activity figures will be the main draw of Thursday's euro area dataflow. Considering the evidence from the member states, euro area retail sales volumes were likely virtually flat at the start of the year. The near-1%M/M decline in Germany skews the risks slightly to the downside, but modest increases elsewhere should provide some offset. Revisions to the series

should also nullify the initially estimated drop in December. And that more favourable carry-over should leave retail sales trending broadly sideways with the level in Q4, improving prospects of a tenth consecutive quarterly increase. In the industrial sector, releases from France and Spain will provide a first view as to the likelihood for a rebound to IP following the broad-based declines in December. Based on the upturn in survey indices regarding French production, we expect payback there to be pronounced. Further ahead, the euro area construction PMIs will provide a view as to activity in the sector in February, albeit with poor weather likely serving as a headwind.

Ahead of Friday's euro area Q4 GDP update, today's final Italian estimates were unrevised from the flash figures, confirming a pick-up in growth to 0.3%Q/Q (0.8%Y/Y). The expenditure breakdown confirmed that consumption was more subdued and net trade subtracted alongside a drawdown in inventories. So, a hefty rise in fixed investment – by 3.9%Q/Q, the most in five years – was responsible for overall growth. Those data will have little impact on the figures from the euro area, where there remains the possibility of an upwards revision by 0.1ppt to 0.4%Q/Q. Final estimates from Ireland, due tomorrow, could be consequential in that regard.

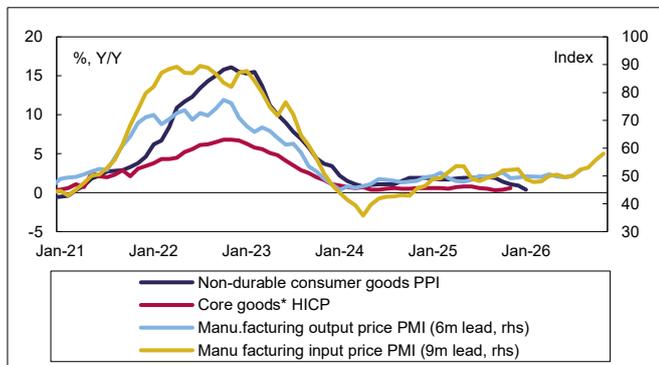
Data aside, the ECB's monetary policy account will provide insights into policymakers' perceptions of the balance of risks at the time of February's Governing Council meeting. Sadly, however, recent events might make those comments obsolete already, significantly reducing their value in terms of future policy direction. Nonetheless, it is bound to convey that the Governing Council was content with the broadly neutral stance of monetary policy last month amid two-sided risks to the inflation outlook.

UK

Final PMIs consistent with firmer growth in GDP & external demand ahead of war

Perhaps more than in the euro area, surveys pointed to a pickup in economic growth momentum in the UK ahead of the outbreak of war in the Middle East. While revised down slightly from the flash figures, today's final services and composite PMIs for February were consistent with a pickup in GDP growth in Q1 from 0.1%Q/Q in Q3 and Q4. The final composite activity PMI was unchanged from January at 53.7, to match the best in 18 months. And the headline services index fell just 0.1pt to 53.9, remaining close to the top of the range of the past two years. That left the services PMI trending this quarter more than 2pts above the Q4 average, the manufacturing output PMI trending more than 1pt higher, and the composite PMI consistent with GDP growth this quarter of ¼%Q/Q. Some of the other details of today's survey were not quite so upbeat. For example, firms continued to signal cuts to headcount. And while consistent with growth, new orders in services were not

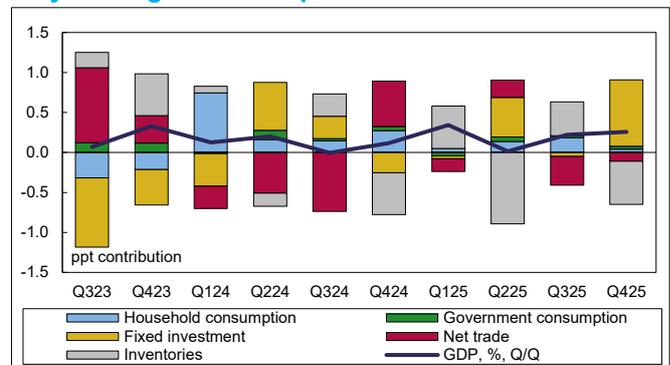
Euro area: Goods inflation indicators



*Non-energy industrial goods.

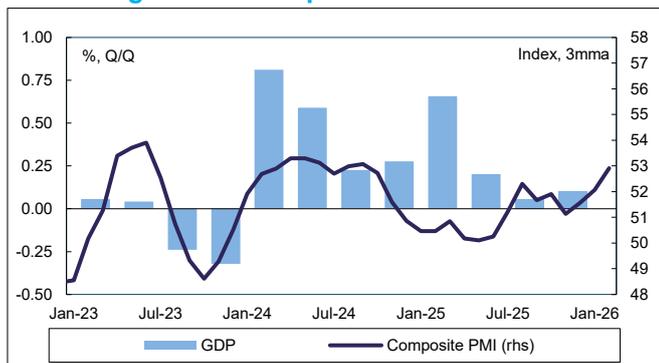
Source: S&P Global, Macrobond and Daiwa Capital Markets Europe Ltd.

Italy: GDP growth & expenditure contributions



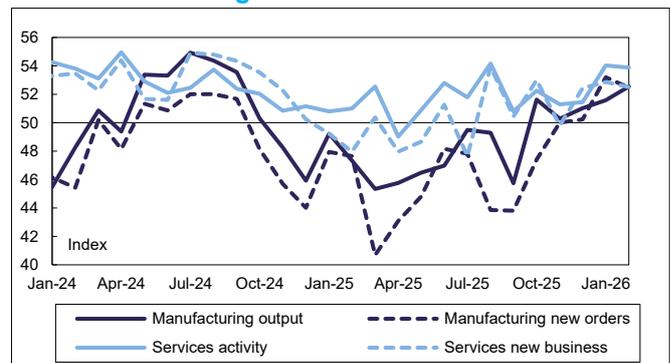
Source: Macrobond and Daiwa Capital Markets Europe Ltd.

UK: GDP growth & composite PMI



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

UK: Manufacturing & services PMIs



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

quite as buoyant as initially thought. But the PMIs were still suggestive of the strongest growth in new demand in Q1 since Q424 and the best quarter for export orders since Q321. But whether such firmness in external demand can weather the storm from the Middle East is now highly doubtful.

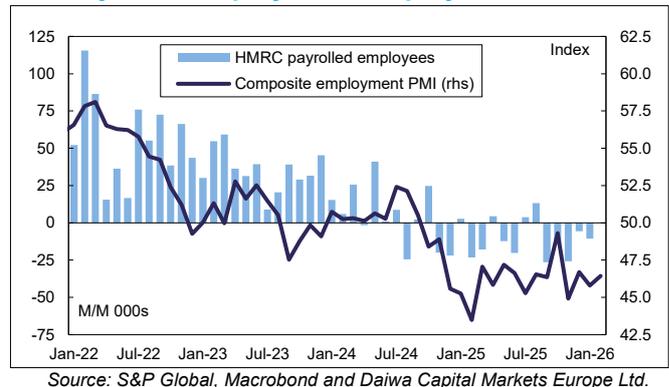
The day ahead in the UK

Considering its significance to several MPC members, the highlight of Thursday's UK dataflow should be February's Decision Maker Panel (DMP) survey. Certainly, external MPC member Mann – who, alongside Governor Bailey, signalled last month that she was close to pivoting in favour of a rate cut – said that she would be looking for further evidence of a moderation in forward-looking price- and wage-setting expectations and firms' CPI expectations. Of course, given the shock to energy prices, regardless of the data, it's unlikely now that either Bailey or Mann will back a cut at March's MPC meeting. Notwithstanding a likely moderation in inflation expectations in February, we expect most MPC members to be mindful of risks that expectations drift in the wrong direction again. Beyond the DMP survey, the construction PMIs will provide an indication of the strength of building activity in February. As in the euro area, we would be surprised to see a notable upturn given the unfavourable weather last month.

UK: Selected composite PMIs



UK: Payrolled employees & employment PMI



European calendar

Today's results

Economic data

Country	Release	Period	Actual	Market consensus/ <i>Daiwa forecast</i>	Previous	Revised
Euro area	Final composite (services) PMI	Feb	51.9 (51.9)	<u>51.9 (51.8)</u>	51.3 (51.6)	-
	Unemployment rate %	Jan	6.1	<u>6.2</u>	6.2	6.3
	PPI Y/Y%	Jan	-2.1	-2.6	-2.1	-
Germany	Final composite (services) PMI	Feb	53.2 (53.5)	<u>53.1 (53.4)</u>	52.1 (52.4)	-
France	Final composite (services) PMI	Feb	49.9 (49.6)	<u>49.9 (49.6)</u>	49.1 (48.4)	-
Italy	Composite (services) PMI	Feb	52.1 (52.3)	51.8 (52.6)	51.4 (52.9)	-
	GDP – final estimate Q/Q% (Y/Y%)	Q4	0.3 (0.8)	<u>0.3 (0.8)</u>	0.2 (0.6)	-
Spain	Composite (services) PMI	Feb	51.5 (51.9)	52.9 (52.9)	52.9 (53.5)	-
UK	Final composite (services) PMI	Feb	53.7 (53.9)	<u>53.9 (53.9)</u>	53.7 (54.0)	-

Auctions

Country	Auction
Germany	sold €960m of 2.3% 2033 green bonds at an average yield of 2.53%

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

Tomorrow's releases
Economic data

Country	GMT	Release	Period	Market consensus/ <i>Daiwa forecast</i>	Previous
Euro area	 08.30	Construction PMI	Feb	-	45.3
	 10.00	Retail sales M/M% (Y/Y%)	Jan	<u>-0.1 (2.0)</u>	-0.5 (1.3)
Germany	 08.30	Construction PMI	Feb	-	44.7
France	 07.45	Industrial production M/M% (Y/Y%)	Jan	0.4 (2.3)	-0.7 (1.7)
	 08.30	Construction PMI	Feb	-	43.5
Italy	 08.30	Construction PMI	Feb	-	47.7
	 09.00	Retail sales M/M% (Y/Y%)	Jan	-	-0.8 (0.9)
Spain	 08.00	Industrial production M/M% (Y/Y%)	Jan	0.5 (1.1)	-2.5 (-0.3)
UK	 09.00	New car registrations Y/Y%	Feb	-	3.4
	 09.30	DMP 3M output price (1Y CPI) expectations Y/Y%	Feb	3.4 (2.8)	3.5 (2.9)
	 09.30	Construction PMI	Feb	47.0	46.4

Auctions and events

Euro area	 12.30	ECB to publish monetary policy account of 4-5 February Governing Council meeting			
	 17.00	ECB President Lagarde to deliver 2026 Annual Global Risk Lecture at John Hopkins University in Bologna			
Germany	 10.00	Governing Council member Nagel to present the Bundesbank 2025 annual report			
France	 09.50	Auction: to sell up €13.5bn of 3.5% 2035, 1.25% 2036, 2.5% 2043 and 4.1% 2046 bonds			
Spain	 09.30	Auction: to sell 2.35% 2029, 3% 2033, 3.5% 2041 bonds and 1.15% 2036 inflation-linked bonds			
UK	 10.00	Auction: to sell £3.5bn of 4% 2029 bonds			

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

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