Euro wrap-up

Overview

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- Bunds made modest gains while the SPD maintained a lead in the latest German election poll and euro area producer price inflation rose to a multi-decade high.
- Gilts also made modest gains on a quiet day for UK economic news.
- Friday will bring new data for euro area retail sales and German car registrations as well as the final August services PMIs.

Daily bond market movements

Bond	Yield	Change
BKO 0 09/23	-0.732	-
OBL 0 10/26	-0.695	-0.009
DBR 0 08/31	-0.387	-0.010
UKT $0^{1}/_{8}$ 01/23	0.190	-0.004
UKT $0^{3}/_{8}$ 10/26	0.354	-0.008
UKT 0¼ 07/31	0.681	-0.010

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

Euro area

SPD maintains lead in latest German election poll

Ahead of Germany's federal election on 26 September, today brought the results of a fifth successive poll to show the centre-left SPD on track to win the largest share of the vote – a seemingly unthinkable prospect just a month ago. Today's survey, which was published by Kantar on behalf of Focus, was conducted between 25-31 August, i.e. either side of Sunday's televised leaders' debate at which SPD leader and Finance Minister Olaf Scholz was widely judged to have fared best. Today's poll gave the SDP 25% of the vote, an increase of 2ppts on the week and 10ppts from mid-July. And that represented a lead of 4ppts ahead of the centre-right CDU/CSU, who lost 2ppts on the week to be down 8ppts from mid-July and at a new series low. The Greens' share edged up to 19%, with the liberal FDP and nationalist AfD level on 11%, and far-left Linke on 7%.

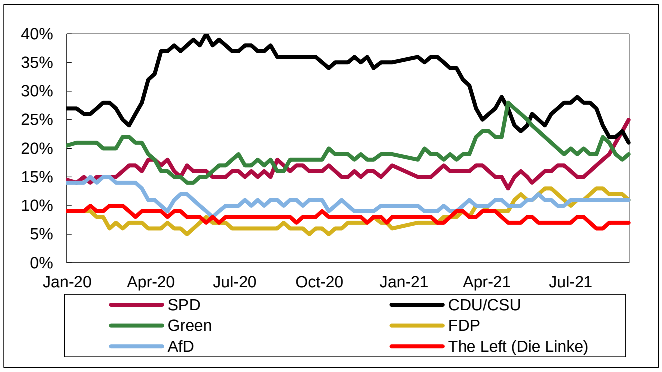
Recipe for lengthy coalition negotiations and incremental policy change

As they stand, the past week's polls suggest that a three-party coalition will be required to deliver a Bundestag majority after the election. And with several combinations of parties likely to be able to form a government, the initial outcome is set to be a lengthy period of negotiations that would be unresolved before 2022. Of course, there is more than enough time for the polls to change significantly, not least as Scholz's current high ratings reflect more the mistakes of the other party leaders than his and his party's policy platform. Nevertheless, Scholz is now best placed to be the next Chancellor. And, with Armin Laschet having failed to capitalize on the desire for change from the Merkel-led CDU/CSU, as well as the challenges of incorporating the far-left Linke into government, on balance a traffic light coalition – of SPD, Greens and FDP – might be the more likely coalition to emerge next year. While it might be tempting to see such a coalition as offering a radical step change for Germany, incremental policy change might be far more likely if the support of the FDP – which looks set to play the role of kingmaker after the election – is to be secured. Indeed, from a fiscal policy perspective, while there might be scope for greater financing of public investment off balance sheet through the government agencies, a traffic-light coalition government might still seem most likely to result in a broadly prudent fiscal policy with no major reform of the constitution's debt brake, or expansion and/or push for permanency of the EU's recovery funds either.

Euro area producer inflation jumps to highest since early 1980s

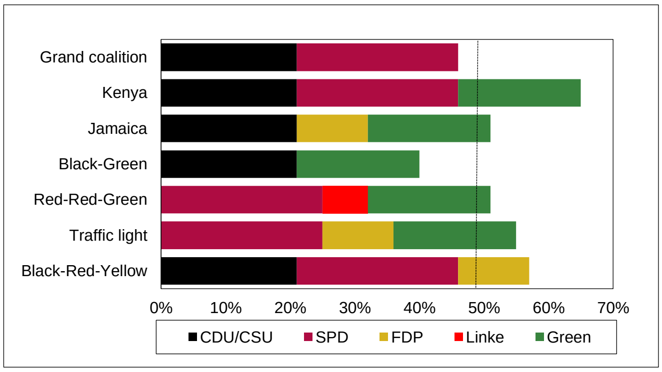
After the [euro area's flash CPI] estimates this week showed headline consumer price inflation jumping to its highest since November 2011, today's producer price inflation numbers signalled a further acceleration in prices at the factory gate too. In particular, producer prices rose a hefty 2.3%M/M, the second-highest monthly increase in 36 years and the fifth increase of

Germany: Federal election voting intentions



Source: Kantar opinion poll and Daiwa Capital Markets Europe Ltd.

Germany: Possible coalition voting intentions*



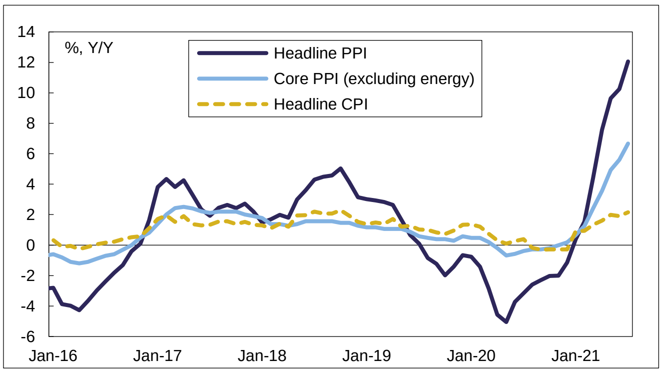
**Poll conducted 25-31 August 2021. Source: Kantar opinion poll for Focus and Daiwa Capital Markets Europe Ltd.*

more than 1%M/M in the past seven months. And that saw the headline PPI inflation rate jump a further 1.9ppt to 12.6%Y/Y – the highest level since the early 1980s. Pressures, however, remained first and foremost driven by prices of energy. For example, producer energy prices surged 5.7%M/M in July, the most since the series began in 2000, to leave the annual rate up 3.3pts to 28.9%Y/Y. But, even excluding that component, producer prices were up a chunky 1.0%M/M to be up 6.7%Y/Y, similarly a series high. As in recent months, this reflected upwards pressures on intermediate goods prices caused by global supply bottlenecks, with prices of such items up a steep 1.9%M/M and 12.6%Y/Y. Pass-through to producer prices further along the supply chain appears to remain more limited – prices of capital goods were up a moderate 0.5%M/M and 2.5%Y/Y, with consumer durables up 0.7%M/M and 2.7%Y/Y, and consumer non-durables up just 0.1%M/M and 2.6%Y/Y. So, consistent with recent surveys – including yesterday's final manufacturing PMIs for August that showed the input price index still notably higher than the output price measure – today's data suggest that manufacturers continue largely to absorb higher input costs within their margins, rather than pass them on in terms of higher prices of finished goods. And with both price PMIs having moderated to four-month lows, this further supports our view that the current spike in consumer price inflation will prove temporary and take a step down early next year as pandemic-related base effects wane.

Spanish unemployment records largest decline in the month of August

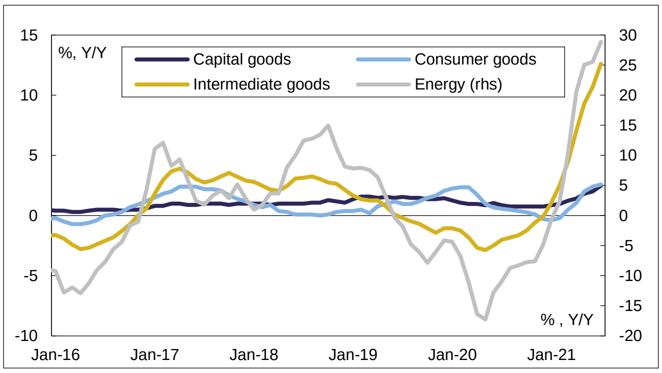
After yesterday's euro area unemployment figures confirmed another decline in July, Spanish data for August published today suggested further improvements in the labour market last month despite tapering of the government's ERTE job retention scheme. In particular, the number of people in registered employment rose a further 76.5k to 19.48mn, taking the cumulative increase since April to more than 450k and the increase from the pandemic trough above 1mn, to leave it just a smidgen below the level in February 2020. While August is typically a month that sees a rise in joblessness, today's report revealed a sizeable drop of 149k in the number unemployed – a record for the month of August, which compares with an average increase of 39k in the decade before the pandemic. In unadjusted terms, the decline of 82.6k was driven by workers from the services sector (-46.2k). But while the number of jobless (on an unadjusted basis) in the manufacturing sector was back close to the pre-pandemic level, unemployment in services still has much further to fall. And overall, while the number of people not in work is down by an adjusted 600k from the post-pandemic peak, today's figures confirmed still-significant amounts of spare capacity in the labour market, with 280k more people unemployed than before Covid. And with Spain's job support scheme due to conclude at the end of this month, we have doubts that the recent downward trend in unemployment will be as marked over coming months.

Euro area: Consumer and producer price inflation



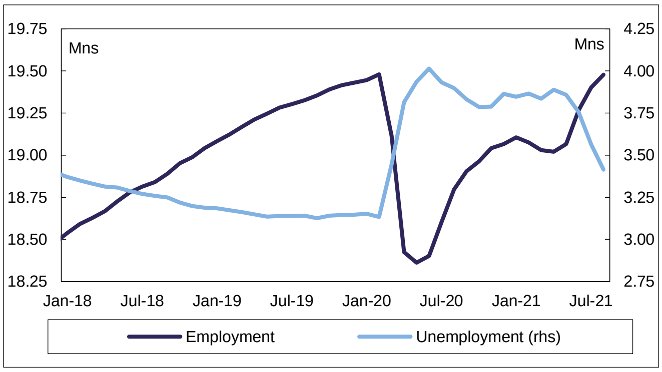
Source: Refinitiv and Daiwa Capital Markets Europe Ltd.

Euro area: Producer price inflation by good



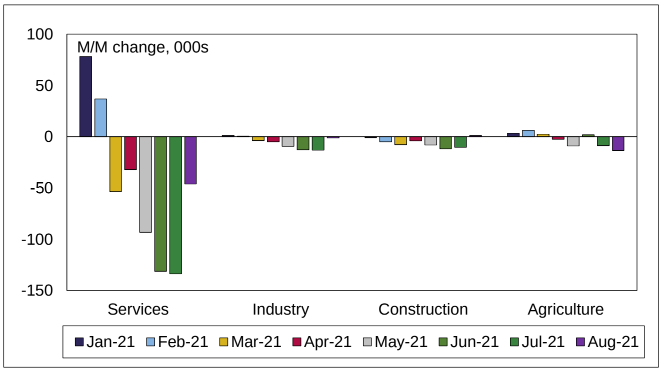
Source: Refinitiv and Daiwa Capital Markets Europe Ltd.

Spain: Employment and unemployment*



**Seasonally adjusted data.*
Source: Refinitiv and Daiwa Capital Markets Europe Ltd.

Spain: Change in unemployment by sector*



**Non-seasonally adjusted data.*
Source: Refinitiv and Daiwa Capital Markets Europe Ltd.

The day ahead in the euro area

Tomorrow sees the release of euro area retail sales figures for July. Consistent with the significantly weaker outturn from Germany that month, we expect sales to have fallen back after two consecutive months of strong growth, as households spent more on services. Meanwhile, the final services and composite PMIs are expected to align with the flash releases which continued to point to a solid recovery, albeit at a slightly moderated pace. The preliminary services activity PMI edged a little lower to 59.7 in August, from 59.8 previously, while the composite PMI fell 0.7pt to 59.5, still the joint-second-strongest reading since 2006. Friday should also bring German new car registrations data for August.

UK

The day ahead in the UK

After a quiet day for UK economic news, the week will end with the final release of the services and composite PMIs for August. In contrast to the euro area, the UK's flash PMIs signalled a more pronounced slowdown in the pace of recovery last month. In particular, despite being the first full month of looser Covid restrictions, the services sector reported the greatest loss of momentum – the activity PMI was down 4.1pts on the month to 55.5 – with businesses reporting that reduced output due to shortages of staff or materials was fourteen times higher than usual and the largest since the survey began in 1998. The preliminary composite PMI fell to a six-month low of 55.3.

European calendar

Today's results

Economic data							
Country		Release	Period	**Actual**	Market consensus/ *Daiwa forecast*	Previous	Revised
Euro area		PPI Y/Y%	Jul	**12.1**	11.1	10.2	-
Spain		Unemployment change '000s	Aug	**-82.6**	-	-197.8	-

Auctions		
Country		Auction
France		sold €6.32bn of 0% 2031 bonds at an average yield of -0.05%
		sold €2.12bn of 0.5% 2044 bonds at an average yield of 0.55%
		sold €1.92bn of 1.5% 2050 bonds at an average yield of 0.7%
Spain		sold €809mn of 1.5% 2027 bonds at an average yield of -0.288%
		sold €1.32bn of 0% 2028 bonds at an average yield of -0.133%
		sold €1.60bn of 0.5% 2031 bonds at an average yield of 0.309%
		sold €415mn of 0.7% 2033 index-linked bonds at an average yield of -1.029%

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

Tomorrow's releases

Economic data						
Country		BST	Release	Period	Market consensus/ *Daiwa forecast*	Previous
Euro area		09.00	Final services (composite) PMI	Aug	59.7 (59.5)	59.8 (60.2)
		10.00	Retail sales M/M% (Y/Y%)	Jul	0.0 (4.5)	1.5 (5.0)
Germany		08.55	Final services (composite) PMI	Aug	61.5 (60.6)	61.8 (62.4)
		-	New car registrations* Y/Y%	Aug	-	-24.9
France		08.50	Final services (composite) PMI	Aug	56.4 (55.9)	56.8 (56.6)
Italy		08.45	Services (composite) PMI	Aug	58.3 (-)	58.0 (58.6)
Spain		08.15	Services (composite) PMI	Aug	61.6 (-)	61.9 (61.2)
UK		09.30	Final services (composite) PMI	Aug	55.5 (55.3)	59.6 (59.2)

Auctions and events
- Nothing scheduled -

**Approximate date of release. Source: Bloomberg and Daiwa Capital Markets Europe Ltd.*

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