

Euro wrap-up

Overview

- Bunds made losses as German inflation surged to its highest since 1951, contrasting a downside surprise to the flash Spanish inflation rate.
- Most Gilts made losses, while long-dated bonds were supported by BoE purchases.
- Friday will bring the flash estimates of euro area inflation in September and the region's unemployment figures for August, as well as the latest UK current account numbers.

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Daily bond market movements

Bond	Yield	Change
BKO 0.4 09/24	1.796	+0.001
OBL 1.3 10/27	2.047	+0.035
DBR 1.7 08/32	2.200	+0.089
UKT 1 04/24	4.398	+0.110
UKT 1½ 07/27	4.427	+0.119
UKT 4¼ 06/32	4.135	+0.122

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

Euro area

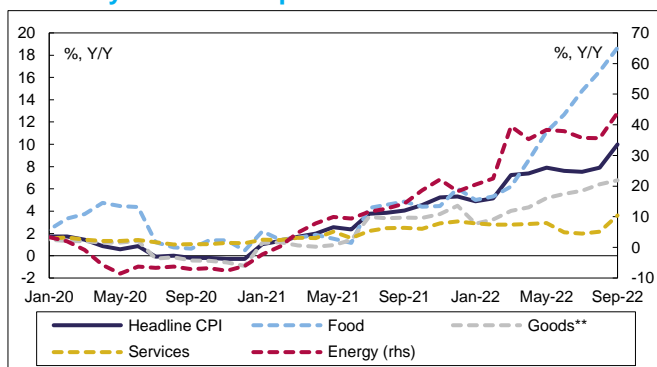
German inflation surges to a new high as summer discounting measures expire

Ahead of the euro area's flash inflation estimates tomorrow, today's German figures came in well above expectations, with prices up more than 2%M/M to leave the annual EU-harmonised HICP rate soaring 2.1pts to a new series high of 10.9%Y/Y. The national CPI measure of inflation also jumped to double-digit territory for the first time since 1951. Admittedly, the surge this month in part reflected expiration of the government's temporary energy-related support initiatives at the end of August. Indeed, energy prices were up a sizeable 6.8%M/M to leave the annual rate of inflation up more than 8ppts to 43.9%, a new series high, reflecting not least a near-12%M/M increase in petrol prices as the duty cut reversed. There was another strong increase in foods (1.8%M/M), which were up a record 18.7%Y/Y. Prices of other goods continued to trend higher too, with our estimate of non-energy industrial goods inflation up a further 0.4ppt to 6.8%Y/Y, as regional releases suggested a marked increase in clothing prices. And services inflation leapt 1.4ppts to 3.6%Y/Y, boosted principally by higher transport costs as the discounted €9 travel pass elapsed. Overall, today's numbers suggest that German core CPI inflation rose more than 1ppt to 4.0%Y/Y, a post-reunification high.

Spanish inflation declines more than expected on lower electricity, fuel and transport costs

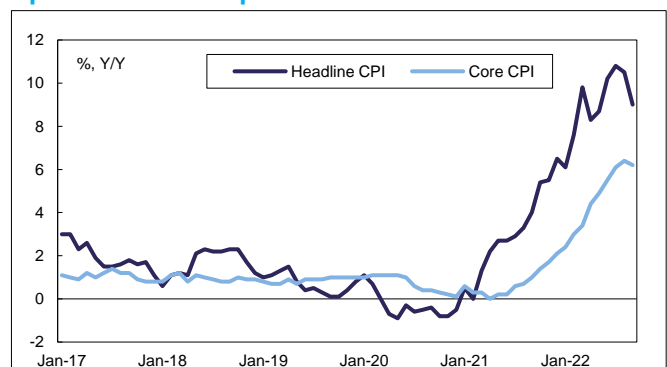
Contrasting with Germany, however, Spanish inflation fell well short of expectations in September. On the national CPI measure, prices declined 0.6%M/M to leave the headline inflation rate down a larger-than-expected 1.5ppts to 9.0%Y/Y, a four-month low. And the EU-harmonised HICP measure fell 1.2ppts to 9.3%Y/Y. Spain's statistical office (INE) attributed the easing largely to the decrease in electricity prices, perhaps reflecting the faster pass-through of developments in wholesale gas prices to consumers in Spain, as well as lower fuel prices and a decline in public transportation prices likely linked to government support initiatives. As such, the national core CPI estimate eased 0.2ppt to 6.2%Y/Y. Notwithstanding the marked decline in Spain, we expect most member states to report a strengthening in price pressures this month. Certainly, figures published by Belgium today showed headline inflation on the national measure increasing 1.4ppts to 11.3%Y/Y, the highest since August 1975. While this largely reflects higher energy prices, which were up around 60%Y/Y, core inflation in Belgium also rose 0.5ppt to 6.2%Y/Y, in part reflecting higher services inflation due to hospitality and package holidays. Overall, therefore, we maintain our view that euro area HICP inflation rose sharply this month, by 0.7ppt to 9.8%Y/Y. And the core HICP rate could rise to as much as 5.0%Y/Y from 4.3%Y/Y previously.

Germany: Consumer price inflation*



*National measure. Source: Refinitiv and Daiwa Capital Markets Europe Ltd.

Spain: Consumer price inflation*



*National measure. Source: Refinitiv and Daiwa Capital Markets Europe Ltd.

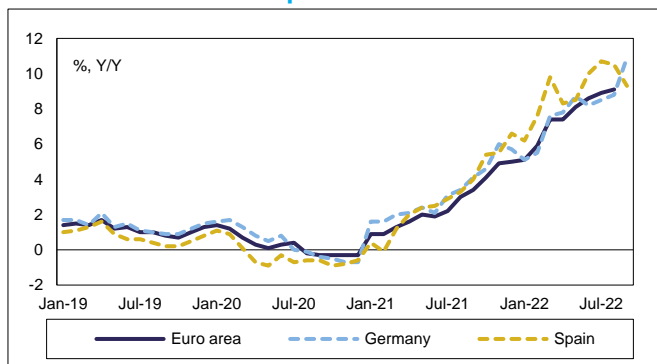
Consumer and business price expectations higher in September

With inflation highly likely to have risen to a new high in September, the concerns of the ECB’s hawks about potential second-round effects will not have diminished. Indeed, having fallen back over the summer, inflation expectations look to have picked up again over the past month. Today’s Commission survey results reported a rise in its index of consumer price expectations for the coming twelve months. At 41.3, that was still down from levels registered between March and July, and broadly equidistant between March’s peak and the long-run average. Selling-price expectations in the retail sector also ticked up to a two-month high in September. In addition, in industry and construction they rose to the highest since June, while selling-price expectations in services rose to the highest since April. That likely reflects increased concerns about cost pressures and supply challenges despite expectations of softer demand and question marks about firms’ capacity to keep passing on increased burdens to consumers.

Broad-based deterioration in economic sentiment points to recession ahead

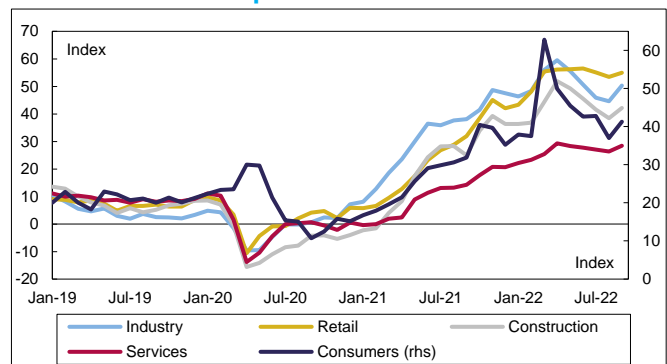
The uptick in inflation expectations coincided with a further deterioration in confidence, with the Commission’s euro area Economic Sentiment Index (ESI) dropping for the sixth month in the past seven to the lowest level since November 2020 and more than 6% below the long-run average. Confidence worsened in each of the five largest member states, with Germany faring worst of all, with its ESI falling 4.8pts to the lowest level since the first wave of Covid-19. Consistent with Friday’s [flash PMIs](#), the deterioration was broad-based. Optimism in industry fell to the lowest since the lockdowns of early 2021 as new orders and production expectations fell sharply. Confidence in services dropped to a 17-month low as the pent-up demand that supported growth earlier in the summer faded further. Retailers were also the most downbeat since winter 2021 as expectations of future demand were revised down. And confidence in construction fell to an 18-month low, as order books worsened and builders reported more widespread shortages of materials and equipment for the first month in five. With staff shortages seemingly less acute, firms’ employment expectations fell to the lowest level since April 2021, albeit remaining above the long-run average. Moreover, the steeper-than-expected deterioration in consumer confidence to a series low, reported in the preliminary estimate, was confirmed. All major sub-components of the consumer survey deteriorated. Notably, the climate for making major purchases was judged only to have been worse in April 2020 at the onset of the first wave of Covid-19. And the outlook for making major purchases over the coming twelve months was judged to have been worse only during the euro crisis.

Euro area: Consumer price inflation*



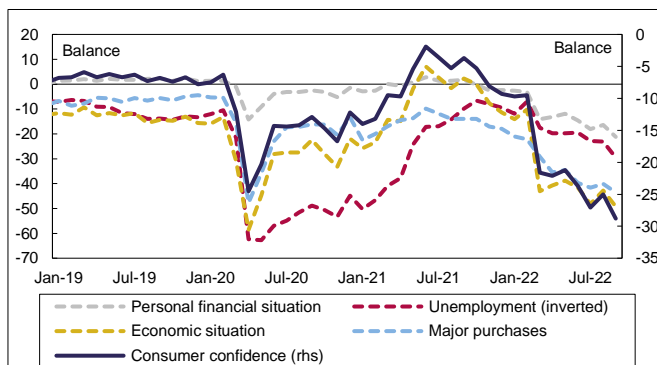
*HICP measure. Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

Euro area: Price expectations*



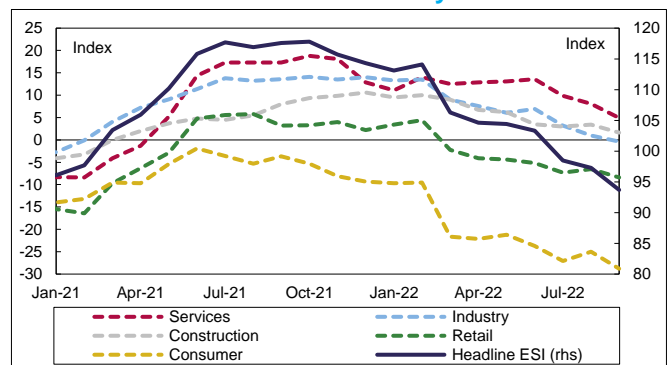
*Consumer expectations of price trends & business price-setting expectations for coming 12 months. Source: EC, Refinitiv and Daiwa Capital Markets Europe Ltd.

Euro area: Consumer confidence



Source: EC, Refinitiv and Daiwa Capital Markets Europe Ltd.

Euro area: Economic sentiment by sector



Source: EC, Refinitiv and Daiwa Capital Markets Europe Ltd.

The day ahead in the euro area

Looking ahead, the main focus tomorrow will be the aforementioned euro area CPI estimate for September. Assuming that the French HICP rate moves broadly sideways at 6.6%Y/Y and the Italian rate edges higher by 0.4ppt to 9.5%Y/Y – data also due for release tomorrow morning – we maintain our forecast that headline euro area inflation jumped 0.7ppt to 9.8%Y/Y in September, a new series high. Not least reflecting the likely jump in German core inflation, we expect euro area core CPI to have risen sharply to as high as 5.0%Y/Y in September. Attention will also turn to the latest labour data, with the euro area unemployment rate expected to have moved sideways at a record-low 6.6% in August, Germany's national jobless claims numbers will offer some insights into developments in September. Separately, EU energy ministers are due to meet again to discuss a package to curb energy prices, while ECB Executive Board member Schnabel is due to speak.

UK

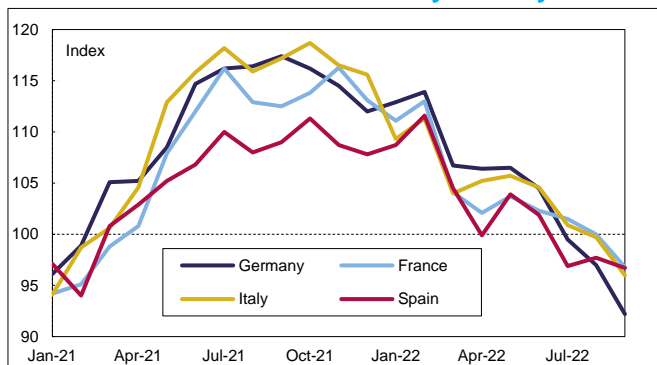
Car production continues to gather momentum, but still well behind pre-pandemic levels

On a relatively quiet day for UK economic data, today brought the latest car production figures for August. According to SMMT, UK car output rose compared with a year earlier for the fourth consecutive month, rising 34%Y/Y to 49.9k units, suggesting that the autos sector again provided a positive contribution to IP growth last month. But SMMT noted that the level of output remains extremely weak by historical standards and remains constrained by global supply shortages – indeed, output in August was still roughly 46% below the equivalent pre-pandemic level in August 2019. In the year to date, output (511k) was still almost half a million units below the equivalent average volume in the three years before the pandemic, and more than 600k lower than the year-to-date average in 2016.

The day ahead in the UK

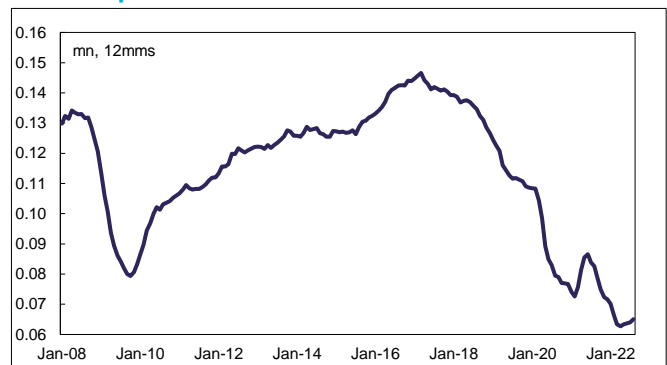
It will be a busier end to the week for UK releases, with the latest balance of payments figures likely to be of most interest after the current account deficit deteriorated to a record 8.3% of GDP in Q1. The worsening of the deficit was largely caused by the soaring price of energy imports following Russia's invasion of Ukraine, and there was only a marginal improvement in the trade deficit in the three months to June (down £3.7bn to £29.8bn). So, continued balance of payments weakness will sustain concerns about the cost to be faced by the government as it seeks to finance its tax cuts and energy bill support, leaving sterling and Gilts vulnerable to further correction. Alongside these data, final Q2 GDP figures are expected to confirm a contraction of 0.1%Q/Q, likely marking the beginning of a recession in the UK. The latest BoE bank lending figures will also be watched for further insights into demand for consumer credit and mortgage lending amid rising interest rates.

Euro area: Economic sentiment by country



Source: EC, Refinitiv and Daiwa Capital Markets Europe Ltd.

UK: Car production











Source: SMMT, Refinitiv 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	 EC economic sentiment indicator	Sep	93.7	95.0	97.6	97.3
	 EC industrial (services) confidence	Sep	-0.3 (4.9)	-0.7 (7.0)	1.2 (8.7)	1.0 (8.1)
	 EC final consumer confidence	Sep	-28.8	-28.8	-24.9	-
Germany	 Preliminary CPI M/M% (Y/Y%)	Sep	1.9 (10.0)	1.5 (9.5)	0.3 (7.9)	-
	 Preliminary HICP M/M% (Y/Y%)	Sep	2.2 (10.9)	1.5 (10.2)	0.4 (8.8)	-
Italy	 PPI M/M% (Y/Y%)	Aug	3.5 (50.5)	-	6.5 (45.9)	-
Spain	 Preliminary CPI M/M% (Y/Y%)	Sep	-0.6 (9.0)	-	0.3 (10.5)	-
	 Preliminary HICP M/M% (Y/Y%)	Sep	0.0 (9.3)	0.6 (10.0)	0.3 (10.5)	-


















Auctions

Country	Auction
Italy	 sold €2.75bn of 2.65% 2027 bonds at an average yield of 4.12%
	 sold €2.5bn of 2.5% 2032 bonds at an average yield of 4.7%
	 sold €1bn of 2029 floating-rate bonds at an average yield of 0.85%
UK	 BoE bought £1.42bn in its special long-term gilt tender


Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

Tomorrow's releases

Economic data

Country	BST	Release	Period	Market consensus/ <i>Daiwa forecast</i>	Previous
Euro area	 10.00	Preliminary HICP M/M% (Y/Y%)	Sep	<u>1.0 (9.8)</u>	0.6 (9.1)
	 10.00	Preliminary core HICP Y/Y%	Sep	<u>5.0</u>	4.3
	 10.00	Unemployment rate %	Aug	6.6	6.6
Germany	 08.55	Unemployment change '000s (rate %)	Sep	20.0 (5.5)	28.0 (5.5)
France	 07.45	Preliminary CPI M/M% (Y/Y%)	Sep	-0.2 (6.0)	0.5 (5.9)
	 07.45	Preliminary HICP M/M% (Y/Y%)	Sep	-0.1 (6.6)	0.5 (6.6)
	 07.45	PPI M/M% (Y/Y%)	Aug	-	1.6 (27.2)
Italy	 07.45	Consumer spending M/M% (Y/Y%)	Aug	-0.1 (-3.7)	-0.8 (-4.3)
	 10.00	Preliminary CPI M/M% (Y/Y%)	Sep	0.0 (8.6)	0.8 (8.4)
	 10.00	Preliminary HICP M/M% (Y/Y%)	Sep	1.7 (9.5)	0.9 (9.1)
Spain	 08.00	Retail sales Y/Y%	Aug	-	-0.5
UK	 00.01	Lloyds business barometer	Sep	-	16
	 07.00	Final GDP Q/Q% (Y/Y%)	Q2	-0.1 (2.9)	0.8 (8.7)
	 07.00	Current account balance £bn	Q2	-43.6	-51.7
	 07.00	Nationwide house price index M/M% (Y/Y%)	Sep	0.3 (9.9)	0.8 (10.0)
	 09.30	Net consumer credit £bn (Y/Y%)	Aug	1.4 (7.4)	1.4 (6.9)
	 09.30	Mortgage lending £bn (approvals 000s)	Aug	4.9 (62.0)	5.1 (63.8)

Auctions and events

Euro area	 16.30	ECB's Schnabel scheduled to speak
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Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

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