

Euro wrap-up

Overview

- Bunds followed US10s lower as euro area unemployment fell to a series low in August.
- Gilts also made significant losses as the Nationwide's UK house price index stopped falling in September.
- Tuesday will bring a retail price survey from the UK while Wednesday will bring retail sales and producer price figures from the euro area.

Chris Scicluna
+44 20 7597 8326

Emily Nicol
+44 20 7597 8331

Daily bond market movements

Bond	Yield	Change
BKO 3.1 09/25	3.216	+0.023
OBL 2.4 10/28	2.821	+0.049
DBR 2.6 08/33	2.909	+0.072
UKT 3½ 10/25	4.941	+0.071
UKT 4½ 06/28	4.583	+0.090
UKT 3¼ 01/33	4.548	+0.113

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

Euro area

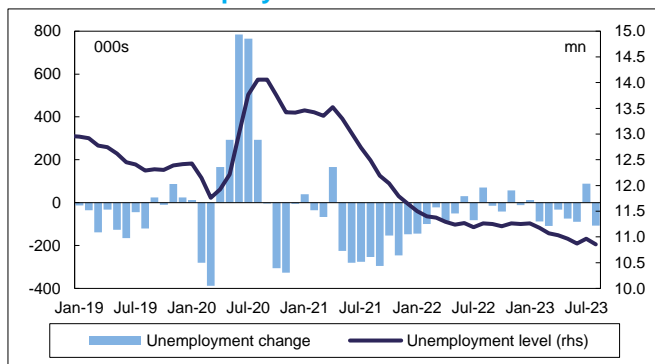
Euro area unemployment level falls to a new series low

While GDP growth through the first half of the year was modest at just 0.1%Q/Q in both Q1 and Q2, and evidence points to significant risks of a contraction in economic output in Q3, today's euro area jobless figures suggested ongoing resilience in the labour market over the summer. In particular, the number of people in unemployment unexpectedly fell in August, by 107k, the most in five months. Roughly two thirds of the drop in the latest month was accounted for by Italy, where a significant rise in July was more than fully reversed. The fall in the number of jobless in the euro area marked the sixth monthly drop out of the past seven, taking the cumulative decline since the start of the year to almost 400k – three quarters of which was accounted for by Spain – and the number of unemployed people down to a new series low of 10.86mn. So, having been revised slightly higher in July (by 0.1ppt to 6.5%), the euro area jobless rate fell back to 6.4%, matching June's series low. Among the member states, Germany's unemployment rate on the ILO measure moved sideways in August for the fourth consecutive month at 3.0%. But the equivalent rate fell in France (down 0.1ppt to 7.3%, still however some 0.2ppt above the low at the start of the year), Italy (down 0.2ppt to 7.3%) and Spain (down 0.1ppt to 11.5%), with the latter two the lowest since the global financial crisis.

Labour slack continues to trend lower, but signs that wage growth has peaked

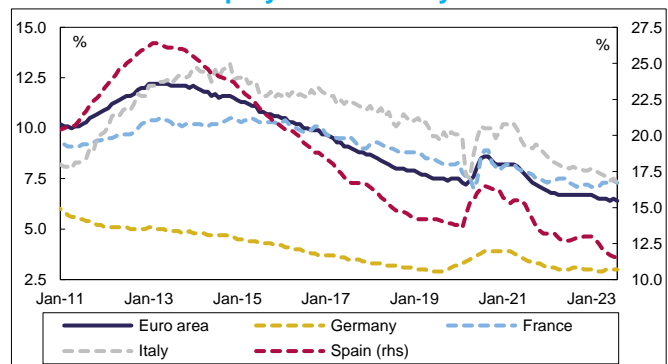
According to the most recent data, labour market slack similarly fell to a series low in Q2, falling 0.2ppt to 12.4%, 4.4ppts below the post-pandemic peak and more than 8.0ppts below the series peak after the euro crisis. While still higher than the other larger member states, Spain reported the largest decline in slack in Q2 (down 0.9ppt to 19.4%), with series lows in France (13.6%) and Italy (17.7%) too. Likewise, euro area employment rose in Q2 to a new high. But there were also some signs that the labour market was starting to loosen in the first half of the year. For example, the number of job vacancies fell in Q2 to its lowest level in five quarters with the drop most striking in services, where short-term and part-time work is common place. And while growth in employee compensation across the euro area remains boosted by increases in minimum wages and catch-up for past inflation – rising in Q2 to 5.6%Y/Y, a series high when excluding the pandemic distortions – there are signs that wage pressures might be peaking too. Certainly, according to the latest Indeed tracker, wage growth in the euro area slowed in August to 4.2%Y/Y, 1.0ppt below last October's peak and the weakest since May 2022. And while there appear to be some oddities in the Italian data – for which the respective Indeed growth rate fell to 0%Y/Y in August – we expect pay growth to moderate steadily over coming quarters as labour demand responds more forcefully to the loss of economic momentum.

Euro area: Unemployment



Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

Euro area: Unemployment rates by member state



Source: Refinitiv Datastream and Daiwa Capital Markets Europe Ltd.

Final manufacturing PMIs point to falling labour demand amid contraction in output & new orders

Judging from recent surveys too, labour demand has softened more significantly in the third quarter. Today's final manufacturing PMIs registered a fourth successive sub-50 reading in the euro area employment index, which fell 0.7pt to 48.8 to suggest the biggest drop in employment demand in the sector since late 2020. The national indicators for Germany, France and Spain similarly suggested weakening demand for manufacturing labour, coinciding with signals of a further marked decline in factory production. Indeed, the euro area manufacturing output PMI fell below the key 50 level for a sixth successive month to 43.1, 0.3pt below the flash estimate. That September figure matched the Q3 average, which was down more than 3pts from Q2 to be the lowest quarterly reading since the first wave of pandemic in Q220 and before that Q209 during the global financial crisis. The manufacturing output PMIs for each of the four largest member states were also firmly below 50 throughout Q3 with the German and French indices down in September to their lowest levels for the current downturn. Moreover, the euro area new orders PMI came in below 40 for a third successive month to similarly leave the quarterly average (39.1) at a level that has only been worse during the first wave of Covid-19 and global financial crisis.

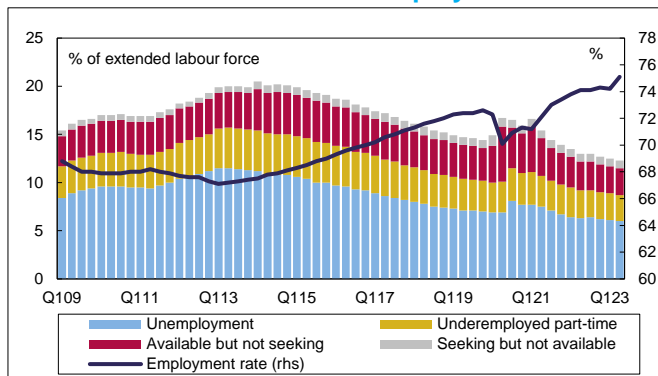
Manufacturers continue to run down backlogs of work as factory output prices continue to fall

So, while the euro area manufacturing output PMI was still up slightly from July's three-year low to suggest that the trough might be near, the chances of a sudden pickup in momentum seem limited. Indeed, the survey reported that work backlogs and purchasing activity declined for the sixteenth and fifteenth successive months respectively. And while inventories of finished items reportedly fell, stocks still appeared high relative to new orders to point to the likelihood of ongoing production weakness towards year-end even as the pandemic supply chains appear now to be very much in the past. Moreover, with demand failing to meet supply, and input costs on average still falling despite the pickup in oil prices, the final manufacturing PMIs suggested that factory output prices fell for a fifth successive month in September and at an accelerated pace. So, core goods disinflation looks set to continue for a while yet.

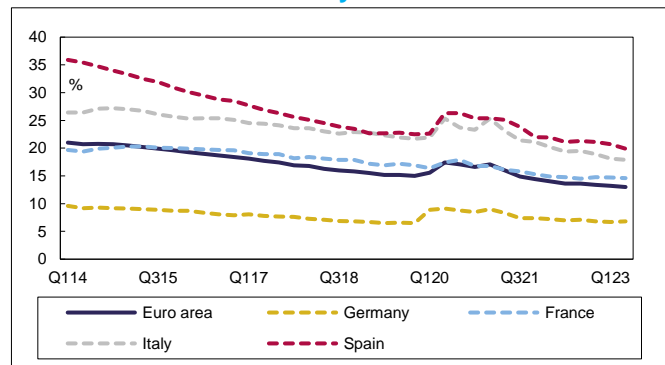
The coming two days in the euro area

Following a day bereft of euro area top-tier releases tomorrow, Wednesday brings euro area retail sales figures for August, which are likely to suggest lacklustre demand over the summer amid ongoing concerns about the economic outlook. Consistent with the weakness in data already published from Germany and France, aggregate euro area sales are forecast to have fallen 0.5% M/M in August, after declining 0.2% M/M in July, to leave them down 1.0% compared to a year earlier. Wednesday also brings the final release of services and composite PMIs for September. Like today's manufacturing indices, the services PMIs are expected to be indicative of a contraction in activity, albeit at a slightly moderated pace. So, while the

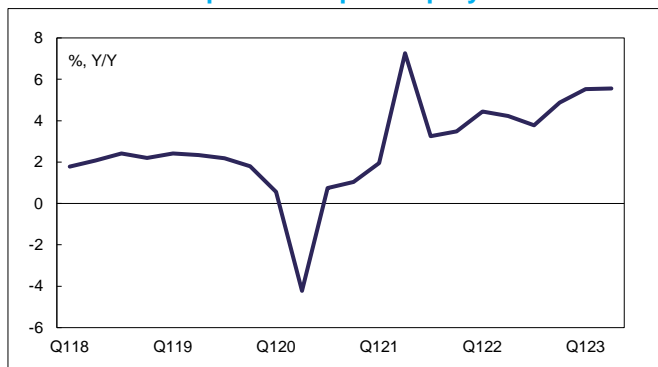
Euro area: Labour slack and employment rate



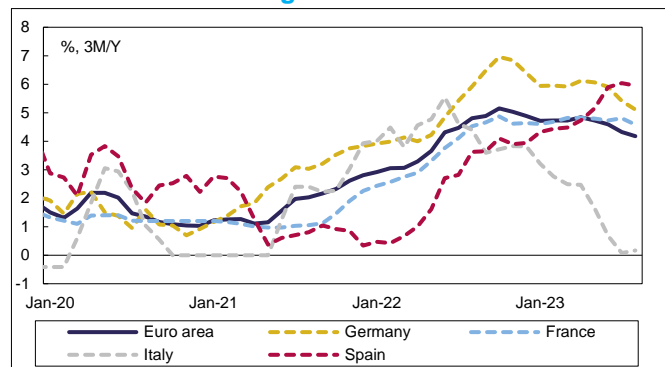
Euro area: Labour slack by member state



Euro area: Compensation per employee



Euro area: Indeed wage tracker



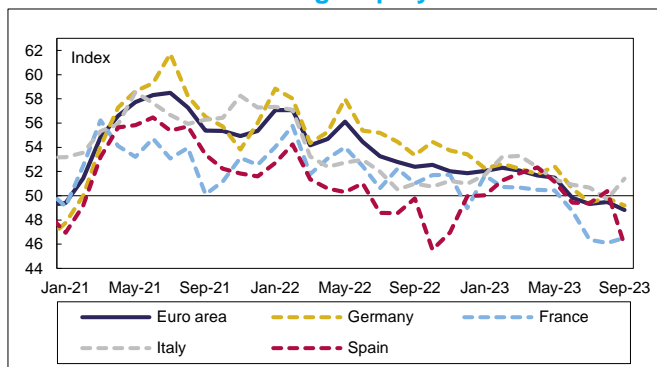
flash euro area composite output index rose 0.4pt in September to 47.1, the average in Q3 (47.5) was some 4.8pts below the Q2 average representing the weakest quarterly figure since the first wave of pandemic in 2020. Meanwhile, with today's PMIs continuing to flag a disinflationary trend in the manufacturing sector, the euro area's producer price inflation data are expected to report an accelerated pace of decline in August from the drop of -7.6%Y/Y in July. Separately, ECB Chief Economist Lane is scheduled tomorrow to give a keynote speech on the 'key factors of inflation and ECB's response'.

UK

The coming two days in the UK

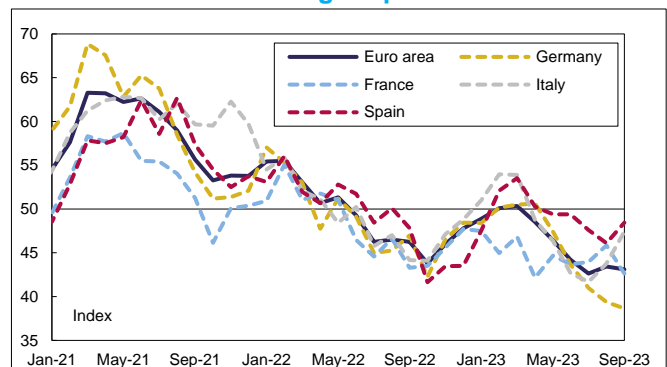
In the UK, tomorrow will bring an update on price developments on the high street with the publication of the BRC shop price report for September. Against the backdrop of subdued demand, the headline index is expected to add to growing evidence of cooling consumer goods inflation. Wednesday, meanwhile, sees the release of the final services and composite PMIs. The flash PMIs reported a notable drop in the services input costs index, to the lowest since March 2022, with a notable step down in activity in the services sector at the end of Q3 too. Indeed, the composite output index fell by 1.8pts to 46.8 in September, the lowest since the start of 2021 and the global financial crisis when excluding lockdown periods. This left the quarterly index down more than 5pts at 48.7 in Q3.

Euro area: Manufacturing employment PMIs



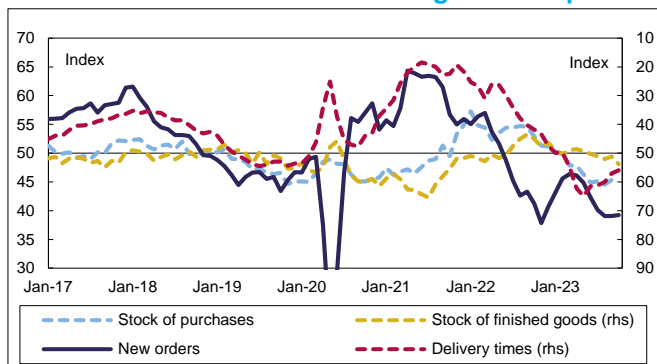
Source: Refinitiv Datastream, S&P Global and Daiwa Capital Markets Europe Ltd.

Euro area: Manufacturing output PMIs



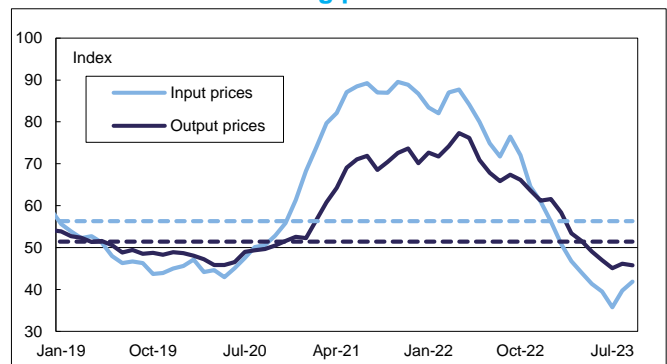
Source: Refinitiv Datastream, S&P Global and Daiwa Capital Markets Europe Ltd.

Euro area: Selected manufacturing PMI components



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

Euro area: Manufacturing price PMIs*












*Dashed lines represent pre-pandemic averages. Source: Refinitiv Datastream, S&P Global and Daiwa Capital Markets Europe Ltd.

The next edition of the Euro wrap-up will be published on 04 October 2023

European calendar

Today's results

Economic data

Country	Release	Period	Actual	Market consensus/ <i>Daiwa forecast</i>	Previous	Revised
Euro area	 Final manufacturing PMI	Sep	43.4	43.4	43.5	-
	 Unemployment rate %	Aug	6.4	6.4	6.4	6.5
Germany	 Final manufacturing PMI	Sep	39.6	39.8	39.1	-
France	 Final manufacturing PMI	Sep	44.2	43.6	46.0	-
Italy	 Manufacturing PMI	Sep	46.8	45.8	45.4	-
	 Unemployment rate %	Aug	7.3	7.7	7.6	7.5
Spain	 Manufacturing PMI	Sep	47.7	46.5	46.5	-
UK	 Nationwide house price index M/M% (Y/Y%)	Sep	0.0 (-5.3)	-0.4 (-5.6)	-0.8 (-5.3)	-
	 Final manufacturing PMI	Sep	44.3	44.2	43.0	-


Auctions

Country	Auction
- Nothing to report -	



Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

Tomorrow's releases

Economic data

Country	BST	Release	Period	Market consensus/ <i>Daiwa forecast</i>	Previous
UK		00.01 BRC shop price index Y/Y%	Sep	-	6.9









Auctions and events

Euro area		07.10 ECB Chief Economist Lane to give keynote speech on 'key factors of inflation and the ECB's response'
UK		10.00 Auction: £2.25bn of 1.5% 2053 green bonds






Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

Wednesday's releases

Economic data

Country	BST	Release	Period	Market consensus/ <i>Daiwa forecast</i>	Previous
Euro area		09.00 Final services (composite) PMI	Sep	<u>48.4 (47.1)</u>	47.9 (46.7)
		10.00 Retail sales M/M% (Y/Y%)	Aug	-0.5 (-1.0)	-0.2 (-1.0)
		10.00 PPI Y/Y%	Aug	-11.6	-7.6
Germany		08.55 Final services (composite) PMI	Sep	<u>49.8 (46.2)</u>	47.3 (44.6)
France		08.50 Final services (composite) PMI	Sep	<u>43.9 (43.5)</u>	46.0 (46.0)
Italy		08.45 Services (composite) PMI	Sep	50.2 (48.7)	49.8 (48.2)
Spain		08.00 Services (composite) PMI	Sep	49.8 (49.2)	49.3 (48.6)
UK		09.30 Final services (composite) PMI	Sep	<u>47.2 (46.8)</u>	49.5 (48.6)

Auctions and events

Euro area		09.00 ECB President Lagarde scheduled to speak at the ECB's academic conference on monetary policy
		12.40 ECB's de Guindos participates in annual conference at the Central Bank of Cyprus
		15.00 ECB's Panetta chairs a panel at the ECB's academic conference on monetary policy
Germany		10.30 Auction: €3bn of 2.4% 2030 bonds
UK		10.00 Auction: £4.25bn of 3.5% 2025 bonds

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

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