

Euro wrap-up

Overview

- Bunds ended the day little changed, while a French survey reported a broad-based deterioration business sentiment at the start of Q4.
- Despite a quiet day for UK economic news, longer-dated Gilts made modest losses.
- Friday will bring figures for euro area car registrations, German producer prices and UK and French retail sales.

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Daily bond market movements

Bond	Yield	Change
BKO 3.1 09/25	3.191	+0.005
OBL 2.4 10/28	2.840	+0.005
DBR 2.6 08/33	2.927	+0.005
UKT 3½ 10/25	4.954	-0.020
UKT 4½ 06/28	4.696	+0.001
UKT 3¼ 01/33	4.670	+0.016

*Change from close as at 5.00pm BST.

Source: Bloomberg

Euro area

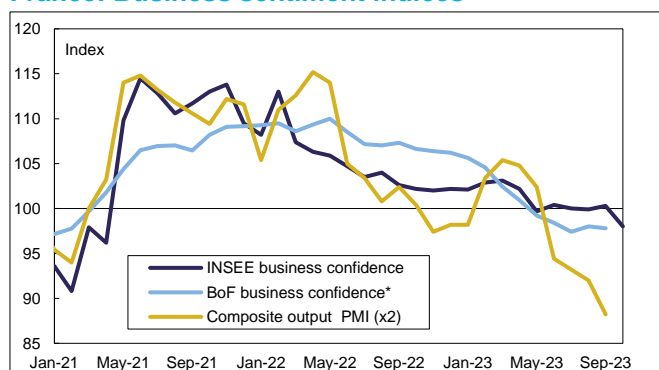
French business sentiment deteriorates at start of Q4

French sentiment surveys provided mixed messages about the economic performance in the euro area's second largest member state over the summer. While the more reliable national measures, including the INSEE and Bank of France business indicators, pointed to broadly stable conditions, the PMIs implied a marked contraction in economic activity in Q3. We continue to expect GDP to have expanded slightly in Q3. But today's INSEE business survey for October signalled a more notable deterioration in economic momentum at the start of Q4. In particular, the headline business index fell 2pts in October to 98, the weakest level since April 2021 and some 15pts below the level ahead of Russia's invasion of Ukraine in February last year. Admittedly, it was just 2pts below the long-run average, more than double the trough at the start of the first Covid lockdown and some 13pts above the average during the first year of the pandemic. Consistent with slowing economic momentum, the survey also signalled a slight deterioration in labour market conditions due to a decline in demand for temporary workers. This notwithstanding, the employment index (down 1pt to 104) remains above the long-run average. As such, while we think that French economic growth is probably pausing this quarter, today's survey still isn't necessarily consistent with a contraction in GDP.

Weakening demand weighs on retail and services sentiment

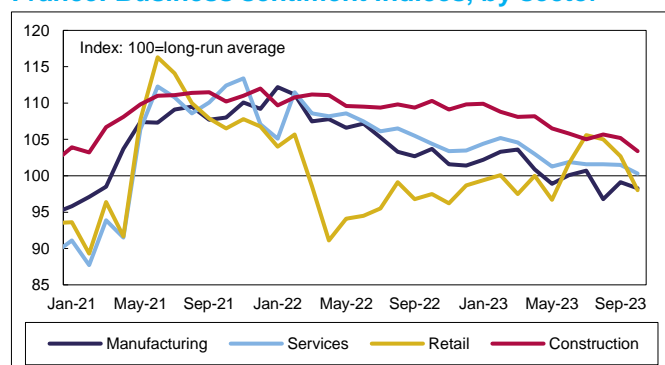
The INSEE survey results suggested that the deterioration in conditions at the start of Q4 was broad-based across sectors. Having rebounded earlier in the summer, the most striking decline in October related to retailing, with the respective business climate index down 5pts on the month to a below-average 98, the lowest in five months. Retailers reported a notable weakening in sales over the past three months, with the balance excluding autos the most negative since July 2022. Retailers also expected sales to weaken further over the coming three months. And with the level of stocks having reportedly only been higher at the start of 2012 and end of 2008, ordering intentions fell at the start of Q4, while fewer firms expect to raise selling prices over the coming three months. Today's survey also suggested that weakening demand had become an increasing drag on services activity over the past three months. Admittedly, the trend in services activity improved slightly in the three months to October due to a pickup in the information and communications subsector. However, despite a pickup in overseas visitors over the summer and a likely further boost from the Rugby World Cup, a drop in domestic tourism saw activity in hospitality, hotel and tourism services fall back, with firms expecting it to decline further over the coming three months too. And so, with the general business outlook the weakest since April 2021, albeit broadly in line with the long-run average, the survey also suggested that investment expectations for the next three months had moderated for a fourth consecutive quarter.

France: Business sentiment indices



*Weighted average. Source: BoF, INSEE, Refinitiv Datastream, Bloomberg and Daiwa Capital Markets Europe Ltd.

France: Business sentiment indices, by sector



Source: INSEE, Macrobond and Daiwa Capital Markets Europe Ltd.

Manufacturers most downbeat about recent production since spring 2021

Today's survey also suggested a slight deterioration in manufacturing sentiment in October, with the respective business climate index down 1pt to 98, to be just below the long-run average (100) for a third consecutive month. But this figure masked a more notable downturn in the recent trend in production, for which the respective survey component fell to its weakest since July 2020. This in part reflected a notable decline in the machinery and equipment sub-sector, for which the respective balance was the most negative since the first Covid lockdown in 2020 and the euro crisis before that. Sentiment in the food industry also weakened to its lowest since June 2009. But while auto makers reported a decline in output, sentiment was supported by a further notable improvement in other transport equipment, for which the composite index was the highest since the series began in 1990. Nevertheless, notwithstanding a slight improvement in domestic and foreign demand this month, French factory orders remain pretty low in a range of sectors including chemical, plastics and food. And the share of firms reporting inadequate demand (24%) rose to the highest since spring 2021, albeit remaining well below the long-run average (40%). So, with inventories of finished goods still above average, manufacturers on the whole were less upbeat about production expectations over the coming three months, with firms in the machinery, autos, pharmaceuticals and food subsectors expecting to cut output.

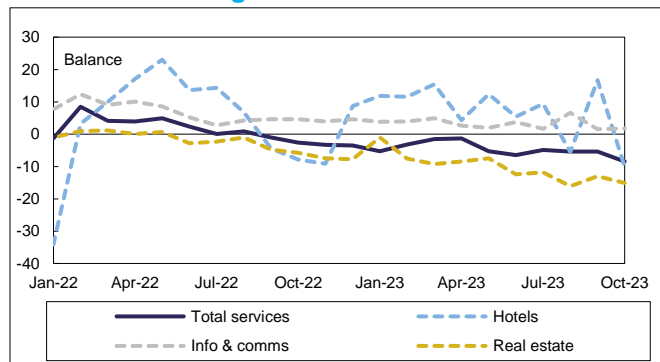
Construction firms more pessimistic about the outlook

While the INSEE construction composite business index remained above the long-run average in October, at 103, it was down 2pts on the month at the lowest reading since February 2021 and some 9pts below the post-pandemic peak at the end of 2021. But the detail suggested a notable deterioration in past activity, with the respective balance down 5pts to a below-average -4, the weakest since the end of 2020. And given higher borrowing costs, falling house prices and a marked drop in building permits, business managers were the most pessimistic about general prospects for the sector since April 2020. Admittedly, the Bank of France's economic update at the start of October suggested that business leaders expect a slight increase in building work this month, having risen in September too. However, not least given the weakness in activity in August, the Bank of France forecast the sector to have provided a slight drag on GDP growth in Q3. And there must be a significant risk of ongoing contraction in construction in Q4 too.

French GDP growth likely slowed sharply in Q3 but remained in positive territory

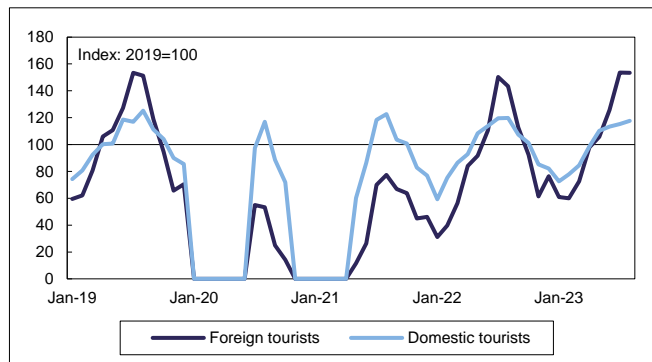
Notwithstanding the drag from construction, like the BoF and INSEE, we maintain our view that French economic output increased slightly in Q3. Despite a decline in August, industrial production remains on track for a modest increase compared with Q2, with a positive contribution from the coke and petroleum sector following strike-related contraction as well as

France: Services general business outlook indices



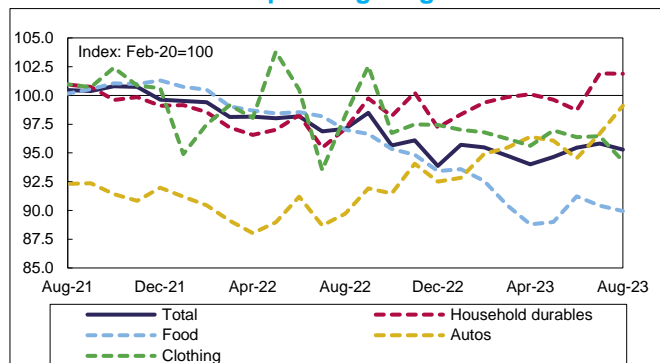
Source: INSEE, Macrobond and Daiwa Capital Markets Europe Ltd.

France: Number of tourists



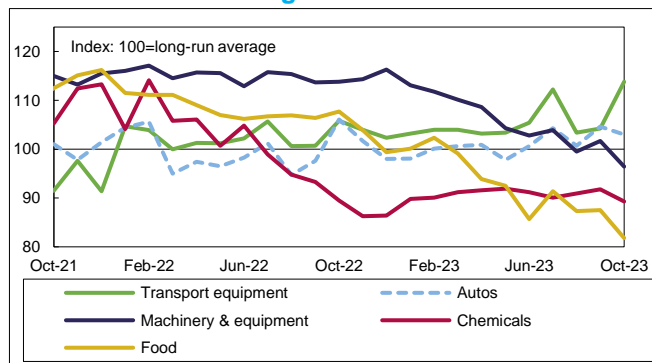
Source: INSEE, Macrobond and Daiwa Capital Markets Europe Ltd.

France: Consumer spending on goods



Source: INSEE, Refinitiv Datastream and Daiwa Capital Markets Europe Ltd.

France: Manufacturing sentiment indices



Source: Refinitiv Datastream and Daiwa Capital Markets Europe Ltd.

stronger car production. Admittedly, growth in services activity looks to have slowed from Q2 (0.6%Q/Q), not least due to softer domestic tourism figures. And while household spending on goods in August was trending almost 1% above the Q2 average, so that consumption should provide modest support to GDP growth in Q3, overall domestic demand was undoubtedly relatively subdued. And after exports were boosted temporarily in Q2 by the delivery of a luxury cruise liner, recent data suggest that net trade provided negligible support to GDP in Q3. So, overall, we maintain our view that GDP growth slowed sharply last quarter, by 0.4ppt to 0.1%Q/Q

The day ahead in the euro area

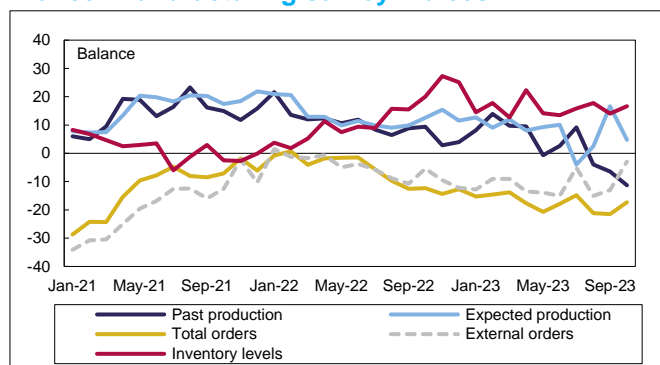
Tomorrow will bring the release of euro area new car registrations data for September, as well as German producer price figures and a Bank of France retail sales survey. The car sales figures published by the member states have been mixed, with a decline in Germany (-0.1%Y/Y) related to the ending of tax incentives for electric cars, while growth slowed in France (10.4%Y/Y) and Spain (2.3%Y/Y), but accelerated in Italy (22.8%Y/Y). Meanwhile, base effects from the energy shock last year will continue to provide a dampening effect on producer price inflation. And with underlying goods price pressures continuing to diminish, headline German PPI inflation is expected to have fallen further into negative territory in September, following a decline of 12.6%Y/Y in August. Separately, French retail spending in September might well see a bounce following the weakness over the summer, with notable declines in sales of furniture, clothing and consumer electronics having been registered in August.

UK

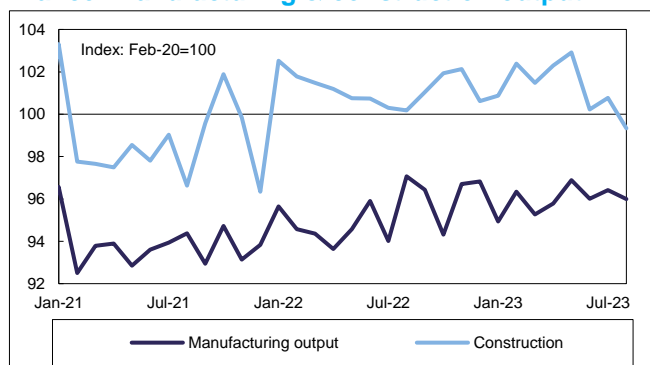
The day ahead in the UK

The most notable release due from the UK tomorrow is September's retail report, which is expected to report a modest decline in sales volumes of less than ½%M/M. Following the drop of 1.1%M/M in July and only a modest rebound in August, that would leave sales down on a quarterly basis in Q3 for the first time since Q422. The weakness would in part reflect the impact of higher prices of auto fuel on spending at petrol stations. But it will also be due to disappointing sales of autumn apparel due not least to the unseasonably high temperatures which matched the UK's record for the month. The latest GfK consumer confidence survey is also expected to suggest that household willingness to spend remained historically subdued at the start of Q4. Indeed, although the headline sentiment index is expected to have edged up to a its highest since January 2022, it will still remain well below the long-run average.

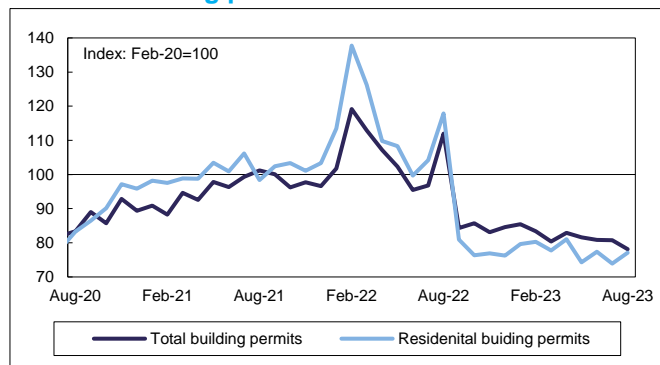
France: Manufacturing survey indices



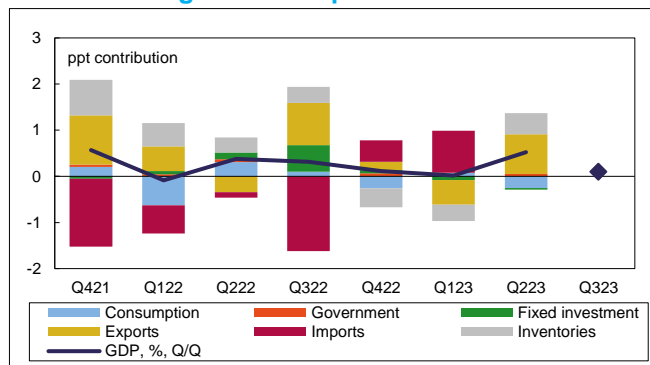
France: Manufacturing & construction output



France: Building permits





France: GDP growth & expenditure contributions













European calendar

Today's results

Economic data

Country	Release	Period	Actual	Market consensus/ <i>Daiwa forecast</i>	Previous	Revised
France	 INSEE business (manufacturing) confidence index	Oct	98 (98)	99 (98)	100 (99)	-
-Spain	 Trade balance €bn	Aug	-4.4	-	-4.9	-








Auctions

Country	Auction
France	 sold €4.30bn of 2.50% 2026 bonds at an average yield of 3.32%  sold €2.31bn of 2.75% 2027 bonds at an average yield of 3.25%  sold €2.98bn of 2.75% 2029 bonds at an average yield of 3.30%  sold €1.66bn of 2.50% 2030 bonds at an average yield of 3.30%  sold €675mn of 0.1% 2026 index-linked bonds at an average yield of 0.66%  sold €515mn of 0.1% 2029 index-linked bonds at an average yield of 0.74%  sold €558mn of 0.1% 2036 index-linked bonds at an average yield of 1.19%
Spain	 sold €1.03bn of 2.15% 2025 bonds at an average yield of 3.508%  sold €2.22bn of 0.8% 2029 bonds at an average yield of 3.679%  sold €1.67bn of 3.55% 2033 bonds at an average yield of 40.67%

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	 07.00	EU new car registrations Y/Y%	Sep	-	21.0
Germany	 07.00	PPI Y/Y%	Sep	-14.2	-12.6
France	 -	Bank of France retail sales index* Y/Y%	Sep	-	-4.0
UK	 00.01	GfK consumer confidence index	Oct	-20	-21
	 07.00	Retail sales incl. auto fuels M/M% (Y/Y%)	Sep	-0.2 (-0.1)	0.4 (-1.4)
	 07.00	Retail sales excl. auto fuels M/M% (Y/Y%)	Sep	0.2 (0.0)	0.6 (-1.4)
	 07.00	Public sector net borrowing excl. banks £bn	Sep	18.3	11.6

Auctions and events

- Nothing scheduled -

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

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