

Euro wrap-up

Overview

- Bunds made gains as the flash euro area composite PMI fell more than expected in September, signalling for the first time in seven months that the economy is contracting.
- Gilts followed USTs lower, while the flash UK PMIs implied ongoing moderate expansion in Q3 despite edging lower in September.
- Tuesday will bring the German ifo business survey for September.

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Daily bond market movements

Bond	Yield	Change
BKO 2.7 09/26	2.158	-0.065
OBL 2½ 10/29	2.014	-0.047
DBR 2.6 08/34	2.172	-0.031
UKT 4½ 01/27	3.922	+0.007
UKT 4½ 07/29	3.761	+0.025
UKT 4½ 07/34	3.934	+0.034

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

Source: Bloomberg

Euro area

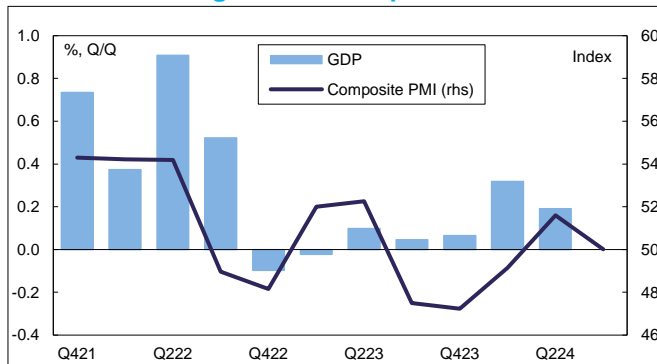
Flash PMIs offer gloomy economic assessment in September

While they had unexpectedly improved in August, today's flash PMIs for September offered a far gloomier assessment of economic momentum, arguably supporting the case for a further rate cut at the ECB's Governing Council meeting next month. In particular, the headline composite PMI fell a steeper-than-expected 2.1pts in September – the most in 15 months – to 48.9, the lowest since January and a level consistent with renewed contraction. The deterioration was broad-based. The services activity index declined 2.4pts to a seven-month low of 50.5, while the manufacturing output index fell 1.3pts to an eight-month low of 44.5. The deterioration in September left the quarterly composite index down 1.6pts to 50.0, consistent with stagnation in the euro area in Q3 and suggesting that risks to the ECB's and our own GDP growth projection of 0.2%Q/Q this quarter are skewed to the downside. Within the country breakdown, the composite PMIs remained consistent with contraction in Germany (47.2) and suggested that the French economy had also weakened markedly in September (47.4). And while today's survey suggested that the remainder of the euro area maintained a modest expansion at end-Q3 – likely still led by Spain – the respective index (51.1) similarly implied the softest growth since the start of the year.

Weakness partly due to Olympics-related distortion, but also downtrend in German manufacturing

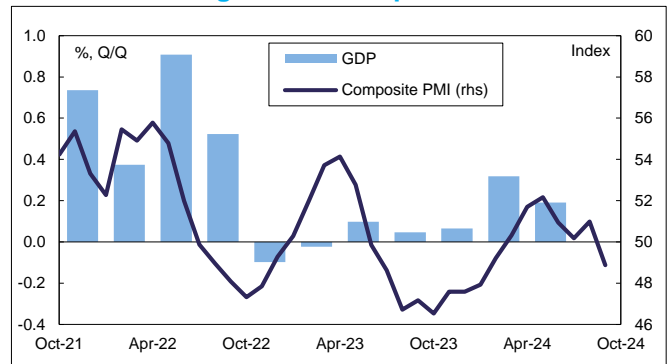
Admittedly, some recent volatility reflects distortions related to the Paris Olympics. In August, the French services PMI leapt to a two-year high. But this month it fell 6.7pts – the most since November 2020 – to a six-month low of 48.3. Like the pickup last month, we think the deterioration in that indicator this month exaggerates the swing in performance in the sector. Certainly, as noted in [Friday's euro wrap-up](#), the larger INSEE survey signalled a modest improvement in conditions in both August and September, suggesting another quarter of steady French GDP growth in Q3. Beyond France, however, today's flash PMIs also signalled slowing services momentum in Germany and elsewhere in the euro area. The weakness in manufacturing was also widespread across member states. However, once again, it was most striking in Germany, where the output component fell a further 2.3pts to 40.5, the lowest in a year, one of the weakest readings on the survey and a level consistent with significant contraction in IP. Today's survey also hinted at a likely further loss of economic momentum heading into Q4. Manufacturing backlogs and orders declined the most in nine months. And services backlogs were the lowest for more than 2½ years while new business fell for the first time in seven months. So, with expectations for output over the coming twelve months revised down too, firms also suggested that they cut headcount by the most since December 2020.

Euro area: GDP growth & composite PMI



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

Euro area: GDP growth & composite PMI



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

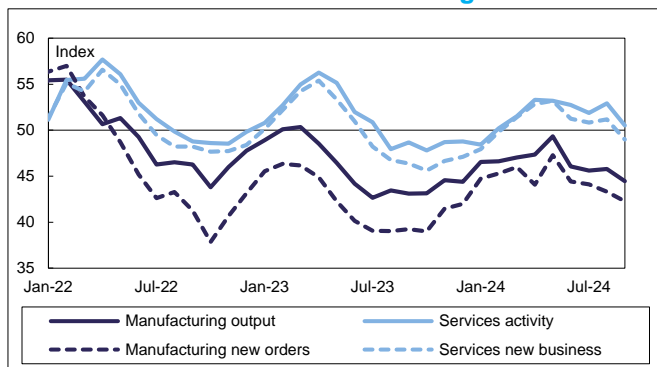
PMIs suggest that price pressures continue to diminish

In terms of inflation, the flash PMIs indicated a further easing in price pressures at the end of Q3 as the recent decline in the oil prices and shipping freight charges reduced input costs. In particular, according to today's survey results, manufacturing input costs fell for the first month in four, with output price growth marginally negative again as a lack of demand continued to diminish pricing power in Germany in particular. ECB policymakers will be most encouraged by the further moderation in services cost growth, with the respective index (55.7) the softest since February 2021 and back below the long-run average. While the index for services prices charged remained above the historical trend, it too was the lowest for almost 3½ years, suggesting that services inflation – which has recently remained stubbornly sticky at around double the ECB's 2% target – should resume a disinflationary trend over coming months, further supporting the case for the Governing Council to cut rates again sooner rather than later.

The day ahead in the euro area

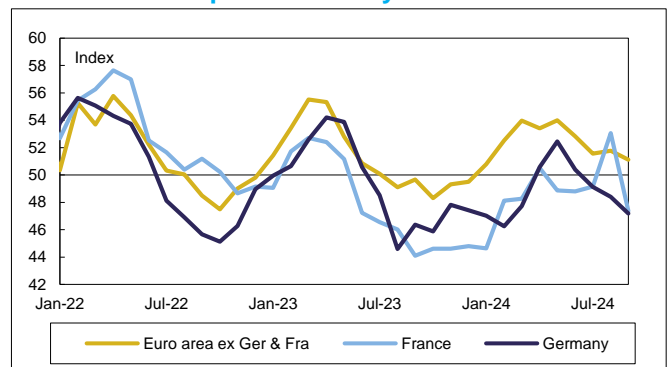
Tuesday will bring the German ifo institute business survey results for September, which will provide an alternative guide to economic conditions in the euro area's largest member state. But following the ZEW investor survey and today's flash PMIs,

Euro area: Services & manufacturing PMIs



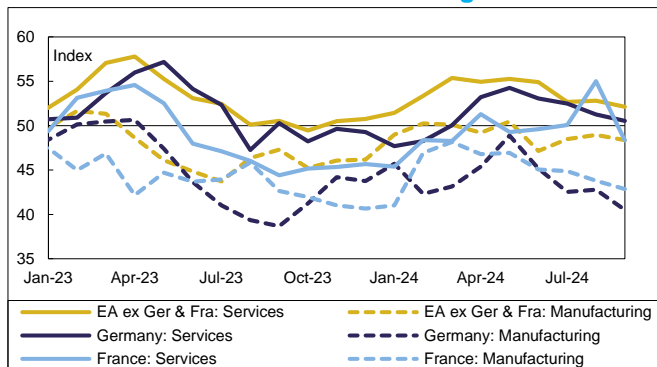
Source: Macrobond, S&P Global and Daiwa Capital Markets Europe Ltd.

Euro area: Composite PMIs by member state



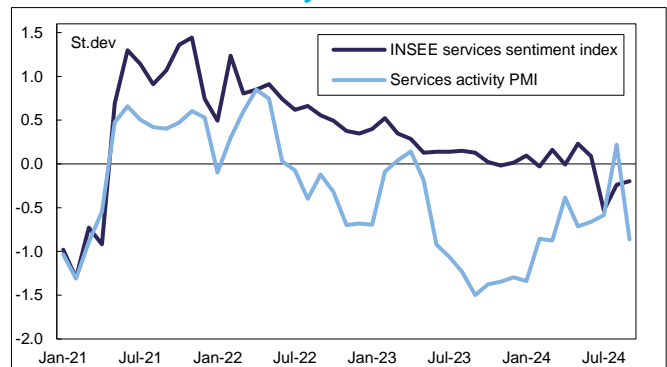
Source: Macrobond, S&P Global and Daiwa Capital Markets Europe Ltd.

Euro area: Services & manufacturing PMIs



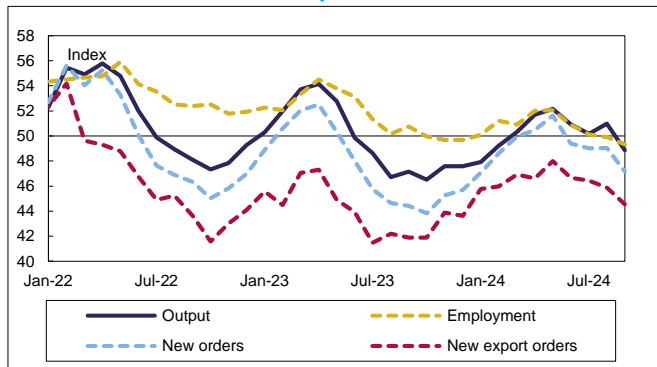
Source: Macrobond, S&P Global and Daiwa Capital Markets Europe Ltd.

France: Services survey indices



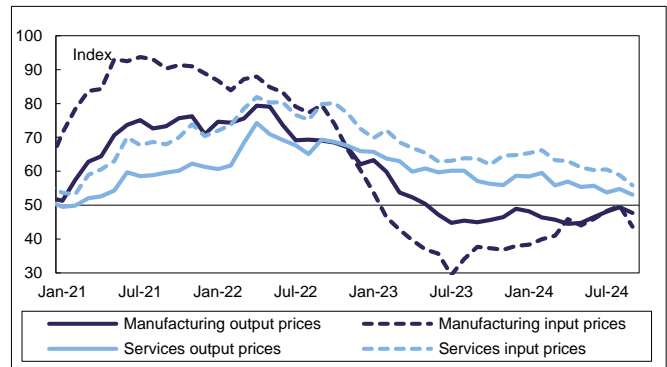
Source: Macrobond, S&P Global and Daiwa Capital Markets Europe Ltd.

Euro area: Selected composite PMIs



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

Euro area: Price PMIs



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

we expect the ifo to paint a similarly gloomy picture of German economic conditions, with firms signaling a further deterioration in both the current business situation and expectations for the coming six months. In addition to an update on manufacturing and services conditions, tomorrow's survey will also offer a guide to recent developments in the retail and construction sub-sectors.

UK

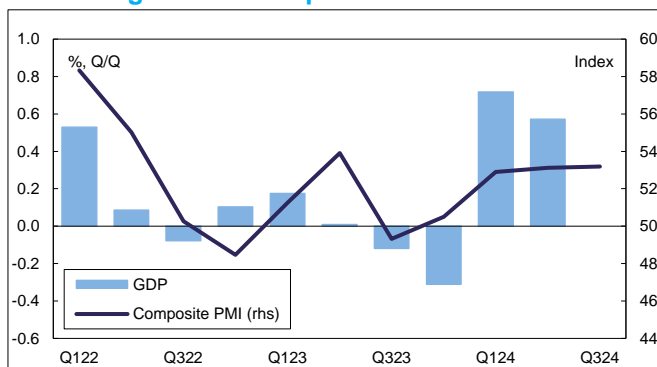
Flash UK PMI eases slightly in September but remains consistent with ongoing expansion

Missing expectations, but tallying with the downbeat message from Friday's GfK [consumer sentiment](#) survey, the flash UK PMIs deteriorated in September, with the composite output index falling 0.9pt to a two-month low of 52.9. The services activity and manufacturing output PMIs similarly declined 0.9pt to 52.8 and 53.5, the lowest for two and three months respectively. This however left the quarterly composite PMI at 53.2, little changed from Q2 and consistent with GDP growth of 0.3%Q/Q, in line with the BoE's and our own projection. Looking ahead, amid reports of lacklustre overseas demand, particularly from the EU, growth in new factory orders was the softest in three months as certain survey respondents reported that decision-making had been put on ice ahead of the Autumn Budget next month. In contrast, services firms were more upbeat about the near-term outlook, buoyed in particular by demand for new technology. And while there remained uncertainties about fiscal policy ahead of the 30 October Budget announcements, firms were on the whole more upbeat about the outlook over the coming twelve months. This notwithstanding, today's survey signalled a softer pace of jobs growth in the services sector and renewed job-shedding in manufacturing.

PMIs point to accelerated factory cost burdens, but easing services inflation

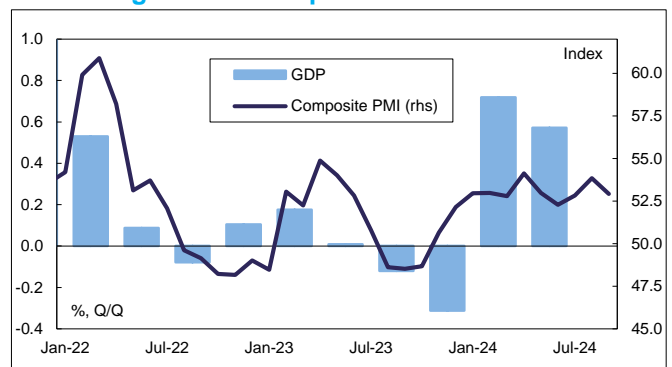
The survey's inflation components provided mixed messages about price pressures at the end of Q3. Despite the recent decline in freight shipping costs and oil prices, manufacturers cited increased costs associated with delivery delays, especially for items sourced from China. Indeed, today's survey implied the strongest input price growth in 20 months. The PMIs also reported a notable pickup in factory output prices this month, with the respective index the highest since May 2023. But this remained below the historical average. That suggests that core consumer goods inflation, which was just 0.3%Y/Y in August, will remain relatively subdued over coming months. Of course, of greater relevance to the near-term monetary policy outlook is developments in services inflation. And in this respect today's survey was somewhat more encouraging. While the services input price PMI edged slightly higher, at 58.6 it was still the second-lowest reading in 2½ years and below the long-run average. And while prices charged in the sector were still above average, the implied increase

UK: GDP growth & composite PMI



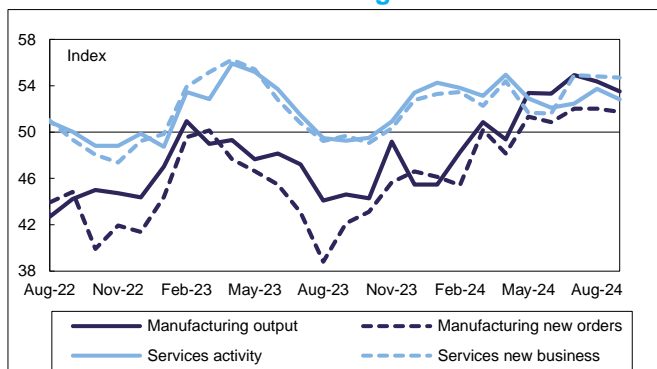
Source: Macrobond, S&P Global and Daiwa Capital Markets Europe Ltd.

UK: GDP growth & composite PMI



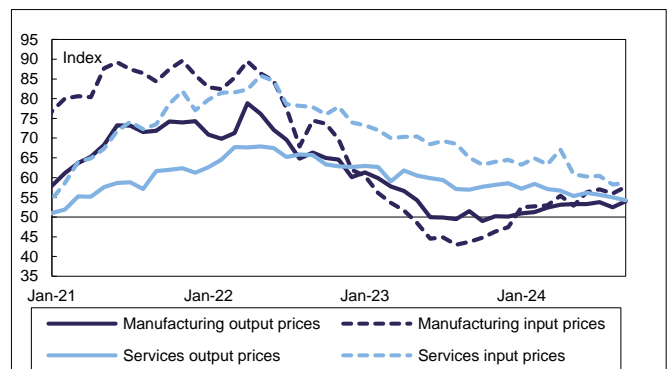
Source: Macrobond, S&P Global and Daiwa Capital Markets Europe Ltd.

UK: Services & manufacturing PMIs



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

UK: Price PMIs












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

was nevertheless the softest since February 2021, suggesting that the disinflationary trend in services CPI inflation should be maintained into Q4, supporting our view that the BoE will cut rates again in November and step up the frequency of future easing to every meeting thereafter.





The day ahead in the UK

It should be a quiet day for UK economic news tomorrow, with no top-tier releases scheduled.

European calendar

Today's results						
Economic data						
Country	Release	Period	Actual	Market consensus/ <i>Daiwa forecast</i>	Previous	Revised
Euro area	 Preliminary manufacturing (services) PMI	Sep	44.8 (50.5)	45.7 (52.3)	45.8 (52.9)	-
	 Preliminary composite PMI	Sep	48.9	50.5	51.0	-
Germany	 Preliminary manufacturing (services) PMI	Sep	40.3 (50.6)	42.3 (51.0)	42.4 (51.2)	-
	 Preliminary composite PMI	Sep	47.2	48.2	48.4	-
France	 Preliminary manufacturing (services) PMI	Sep	44.0 (48.3)	44.2 (53.1)	43.9 (55.0)	-
	 Preliminary composite PMI	Sep	47.4	51.5	53.1	-
UK	 Preliminary manufacturing (services) PMI	Sep	51.5 (52.8)	52.2 (53.5)	52.5 (53.7)	-
	 Preliminary composite PMI	Sep	52.9	53.5	53.8	-
	 CBI industrial trends survey – total orders (selling price) balance	Sep	-35 (8)	-23 (-)	-22 (15)	-
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	
Germany	 09.00	Ifo business climate indicator	Sep	86.0	86.6	
	 09.00	Ifo current assessment (expectations) indicator	Sep	86.1 (86.5)	86.5 (86.8)	
Auctions and events						
Germany	 10.30	Auction: to sell €4.5bn of 2.7% 2026 bonds				
UK	 10.00	Auction: to sell £1.5bn of 0.75% 2033 inflation-linked bonds				

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

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

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