Euro wrap-up

Overview

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- While German IP beat expectations, Bunds made gains as typically-hawkish Bundesbank President Nagel suggested that he would consider supporting a rate cut next week.
- Gilts also made gains even as a UK retail survey suggested that sales growth picked up at the end of Q3.
- The coming two days will bring the ECB's account of Septembers monetary policy meeting, German goods trade and retail sales figures for August, and a UK housing market survey.

Daily bond market movements

Bond	Yield	Change
BKO 2.7 09/26	2.223	-0.016
OBL 2½ 10/29	2.102	-0.017
DBR 2.6 08/34	2.245	-0.008
UKT 4⅛ 01/27	4.191	-0.027
UKT 4⅛ 07/29	4.073	-0.025
UKT 4¼ 07/34	4.187	-0.020

*Change from close as at 4:45pm BST.
Source: Bloomberg

Euro area

German IP maintains downtrend despite a jump in August

Consistent with yesterday's turnover data but much stronger than initial expectations, today's IP figures showed that German manufacturing output jumped sharply in August, with the 3.4%M/M increase the largest since November 2021. Construction activity recorded a more modest increase (0.3%M/M), while energy output posted a fourth monthly rise in five (2.3%M/M). As a result, overall industrial production rose 2.9%M/M. But this merely reversed the decline in July. Indeed, IP was still down 2.7%Y/Y, more than 10% below the pre-pandemic level and trending in the first two months of Q3 some 1.4% below the Q2 average. Smoothing for the recent monthly volatility, the level of manufacturing output in the three months to August was the second-weakest since the global financial crisis outside of the initial pandemic slump. And construction output was averaging in July and August a little more than 1% below the level in Q2 when the sector contracted around 2½%Q/Q. As such, today's data strongly suggest that industry will provide a non-negligible drag on GDP growth for the fifth quarter out of the past six.

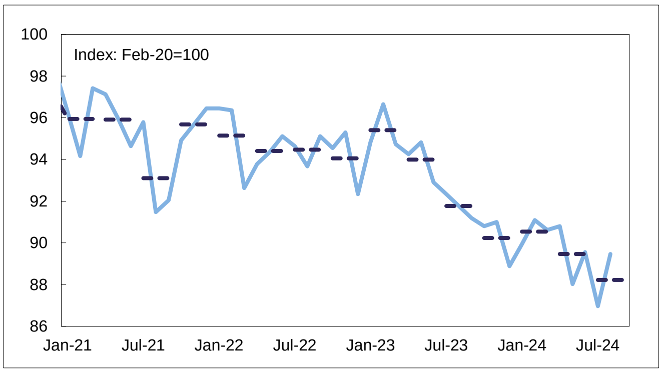
Autos drive production rebound, offsetting ongoing decline in machinery & equipment

Within the manufacturing detail, the increase in August was driven by a marked acceleration in autos production, which rose a whopping 19.3%M/M – the most since the resumption of business following the first Covid-19 lockdown – to the highest level in 18 months. Having fallen sharply at the start of the third quarter (-7.9%M/M), we suspect that the pickup in August in part reflects the timing of summer maintenance periods this year. Nevertheless, autos as well as the rail and aerospace subsectors appear on track to contribute positively to GDP growth for a second successive quarter. In marked contrast, output of machinery and equipment fell to the lowest level since May 2020 and the global financial crisis before that to be trending some 2% below the Q2 average. And despite rising in August, electrical machinery was averaging more than 5% lower than in Q2. With wholesale gas prices having ticked higher over the summer, production from certain energy-intensive subsectors – such as chemicals, coke & petroleum and paper – was also trending lower.

Surveys & inventories point to downbeat outlook for German manufacturing output

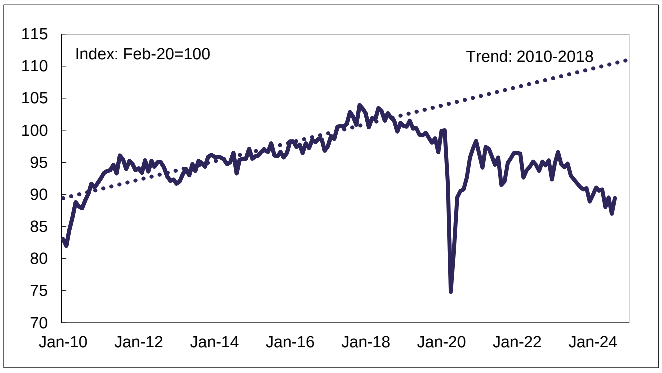
The steady uptrend in new auto orders should help to support production in that sector over the near term. Certainly, Germany's auto association (VDA) signalled another month of solid production growth in September, rising 15.6%Y/Y. This notwithstanding, the latest ifo survey suggested that auto manufacturers last month were much more downbeat about production expectations for the coming three months due not least to a further weakening in export prospects. The ifo survey and PMIs similarly pointed to a broad-based deterioration in conditions across the sector. So, with yesterday's orders data flagging a lack of underlying demand for German manufactured goods and orders looking low relative to inventories, the

Germany: Industrial production*



Dashed dark blue lines represents quarterly average. Source: Macrobond and Daiwa Capital Markets Europe Ltd.

Germany: Industrial production



Source: Macrobond and Daiwa Capital Markets Europe Ltd.

trend in manufacturing is highly likely to remain lacklustre for the time being, with a strong probability that it will be a drag on GDP through to the New Year.

The coming two days in the euro area

With only a handful of headline euro area data releases scheduled, one highlight over the next two days will be the ECB's account of September's monetary policy meeting, during which the Governing Council cut the deposit rate by a further 25bps. The account will provide further insight into policymakers' discussion about the economic outlook and the balance of risks with respect to the inflation outlook. However, since the meeting, not least given the downside surprise to inflation in September, subsequent comments from several members – including the typically hawkish Bundesbank's Nagel today – have raised the likelihood of a further rate cut this month.

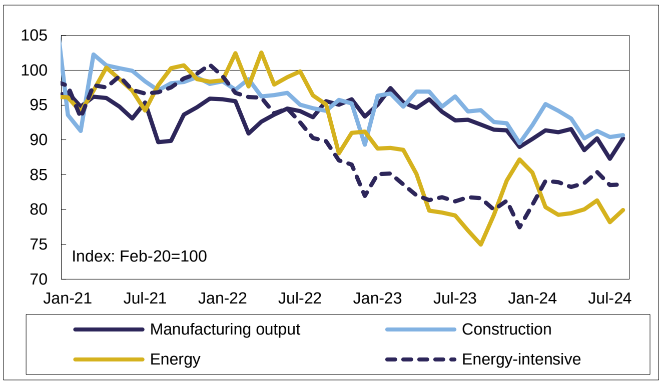
On the data front, the coming two days will bring further country-level updates on industrial production in August. Tomorrow's Irish IP figures – which due to the activities of multinational corporations based there for tax reasons have a tendency to skew the area-wide measure significantly – will be followed by the Italian release on Thursday. While surveys point to a further deterioration in production in August, Italian IP is expected to post a modest rise, albeit failing to fully reverse sharp contraction in July (-0.9%M/M). Meanwhile, signs of sluggish external demand will likely be reflected in tomorrow's German goods trade data for August. Flash estimates of exports to non-EU countries recorded a further decline in August of -1.1%M/M. Germany's statistical office Destatis is also scheduled to publish updated retail sales figures on Thursday.

UK

BRC survey signals solid end to Q3 for retail sales

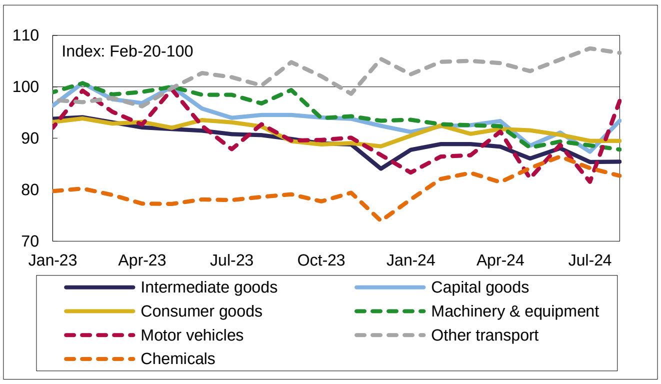
Having declined slightly in Q2, retail sales appear to have rebounded strongly in Q3. According to the ONS's official data, retail sales volumes rose in each of the first two months of the quarter to be trending some 1.6% higher than the Q2 average. And today's BRC survey suggested that spending on the high street remained firm in September, with the annual rate of sales values up 2.0%Y/Y, the strongest in six months, and like-for-like sales growth of 2.3%Y/Y the best since January 2022. With the BRC's measure of shop prices signalling deflation on the high street in September, like-for-like sales volume growth of 2.3%Y/Y was similarly the strongest since the start of 2022. Food sales volume growth over the quarter ticked up to 0.9%3M/Y, an improvement from the annual decline in Q2 but still down on Q1. But sales volumes of non-food items accelerated markedly, to 1.2%3M/Y, also the best since Q122.

Germany: Industrial output, by sector



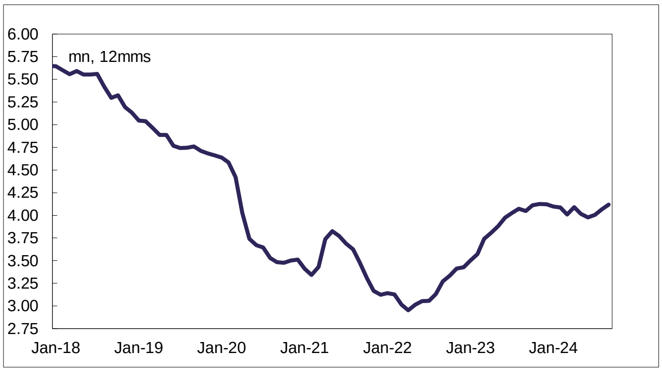
Source: Macrobond and Daiwa Capital Markets Europe Ltd.

Germany: Manufacturing output, by sector



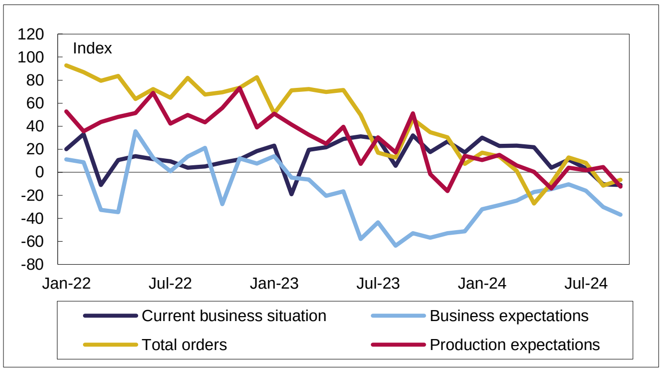
Source: Macrobond and Daiwa Capital Markets Europe Ltd.

Germany: Car production



Source: VDA, Bloomberg and Daiwa Capital Markets Europe Ltd.

Germany: ifo auto survey indices



Source: Macrobond and Daiwa Capital Markets Europe Ltd.

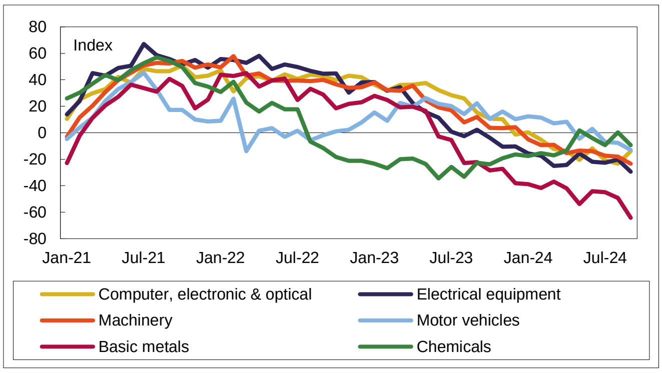
Autumnal weather prompted sales of apparel, but spending on many big-ticket items still muted

In part the pickup in sales of non-food items in Q3 appears to have reflected aggressive discounting amid highly competitive markets. However, sales last quarter also appear to have benefited from the vagaries of the weather. Whereas sales of non-food items in July and August were boosted by the belated arrival of summer sunshine, consumers reportedly significantly increased purchases of autumn apparel in September, which was the wettest on record in ten English counties. Sales of back-to-school goods, including laptops, were also seemingly strong. But sales of many other big-ticket items, including furniture and white goods, reportedly remained lacklustre amid sub-par consumer confidence. The fit between the BRC survey indices and official ONS retail sales figures is not perfect, being complicated among other things by seasonal adjustment. But today's survey raises the possibility of a third successive monthly increase in retail sales volumes on the ONS measure for the first time since early 2021. If so, however, October might well prove to be a damp squib. And sales growth over Q4 as a whole is highly likely to be significantly softer than Q3.

The coming two days in the UK

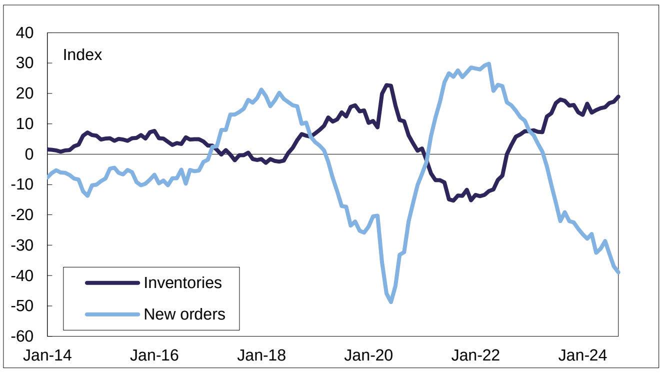
With no major UK releases scheduled for Wednesday, the data flow continues on Thursday with the results of the Bank of England's quarterly Credit Conditions Survey for Q3 and the RICS residential survey for September. Supported by dissipating risks to the economic outlook and expectations for lower interest rates, UK lenders reported a notable increase in household loan demand in the first half of the year. But credit availability was little changed in Q2 and was expected to remain limited in Q3 too. Corporate loan demand and credit supply was also expected to remain little changed over the past quarter despite an expected easing in financial conditions. The impact of declining mortgage rates is also likely to be reflected in the RICS survey, with an expected further pickup in buyer enquiries and instructions on the market. Against this backdrop, the survey is also likely to reveal a second-successive increase in the house price balance, in keeping with the positive momentum reflected by the equivalent Halifax (4.7%Y/Y) and Nationwide (3.2%Y/Y) measures.

Germany: ifo manufacturing business conditions



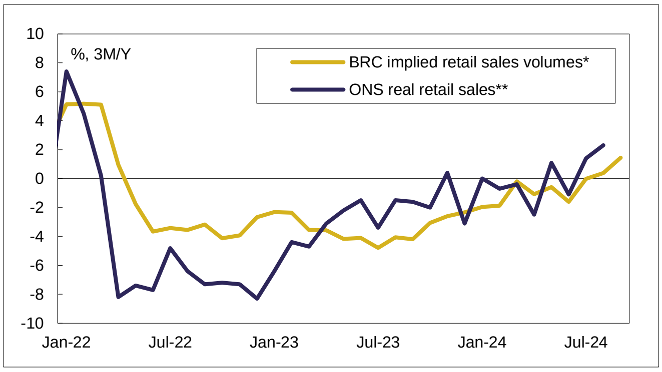
Source: Macrobond and Daiwa Capital Markets Europe Ltd.

Germany: ifo new orders & inventories indices



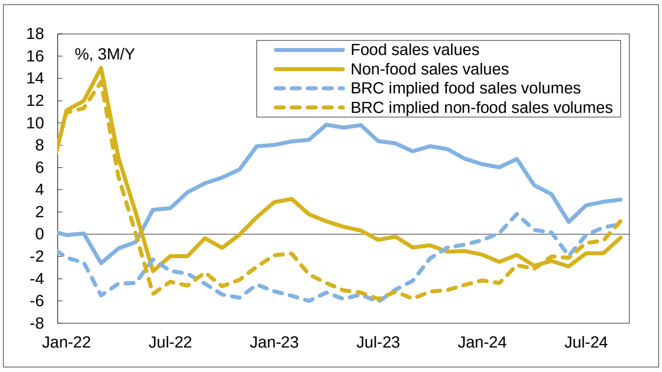
Source: Macrobond and Daiwa Capital Markets Europe Ltd.

UK: Retail sales



**BRC retail sales values deflated by BRC shop price index. **ONS real retail sales excluding auto fuel. Source: Macrobond and Daiwa Capital Markets Europe Ltd.*

UK: BRC retail sales indices



Source: Macrobond and Daiwa Capital Markets Europe Ltd.

The next edition of the Euro wrap-up will be published on Thursday 10 September

Daiwa Capital Markets

European calendar

Today's results

Economic data

Country		Release	Period	**Actual**	Market consensus/ *Daiwa forecast*	Previous	Revised
Germany		Industrial production M/M% (Y/Y%)	Aug	**2.9 (-2.7)**	0.8 (-3.8)	-2.4 (-5.3)	-2.9 (-5.6)
France		Trade balance €bn	Aug	**-7.4**	-	-5.9	-6.0
UK		BRC retail monitor – like-for-like sales Y/Y%	Sep	**1.7**	0.8	0.8	-

Auctions

Country		Auction
Germany		sold €954mn of 2.3% 2033 green bonds at an average yield of 2.16%
UK		sold £1bn of 0.125% 2039 inflation-linked bonds at an average yield of 1.044%

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

Wednesday's releases

Economic data

Country		BST	Release	Period	Market consensus/ *Daiwa forecast*	Previous
Germany		07.00	Trade balance €bn	Aug	18.5	17.0

Auctions and events

Germany		10.30	Auction: to sell €500mn of 0% 2036 bonds
		10.30	Auction: to sell €1bn of 2.6% 2041 bonds
UK		10.00	Auction: to sell £3.75bn of 4.25% 2034 bonds

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

Thursday's releases

Economic data

Country		BST	Release	Period	Market consensus/ *Daiwa forecast*	Previous
Germany		07.00	Retail sales M/M% (Y/Y%)	Aug	-	-
Italy		09.00	Industrial production M/M% (Y/Y%)	Aug	0.2 (-3.1)	-0.9 (-3.3)
UK		00.01	RICS house price balance %	Sep	10	1

Auctions and events

Euro area		12.30	ECB publishes monetary policy account of September Governing Council meeting
UK		09.30	BoE to publish quarterly credit conditions survey for Q3 2024

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

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