Euro wrap-up

Overview

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- Despite a marked decline in German industrial production, Bunds made losses as the market digested yesterday's news that Germany's ruling coalition had collapsed amid the dismissal of the finance minister.
- Gilts followed USTs higher after the BoE cut rates and signalled the likelihood of further gradual easing despite an upwards revision to its GDP and inflation projections.
- The coming week will bring updates on Q3 GDP in the euro area and UK, and labour market data from the UK, while the ECB will publish account from October's Governing Council meeting.

Daily bond market movements

Bond	Yield	Change
BKO 2 12/26	2.204	+0.036
OBL 2½ 10/29	2.255	+0.050
DBR 2.6 08/34	2.443	+0.040
UKT 4⅛ 01/27	4.437	-0.063
UKT 4⅛ 07/29	4.356	-0.081
UKT 4¼ 07/34	4.495	-0.064

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

Euro area

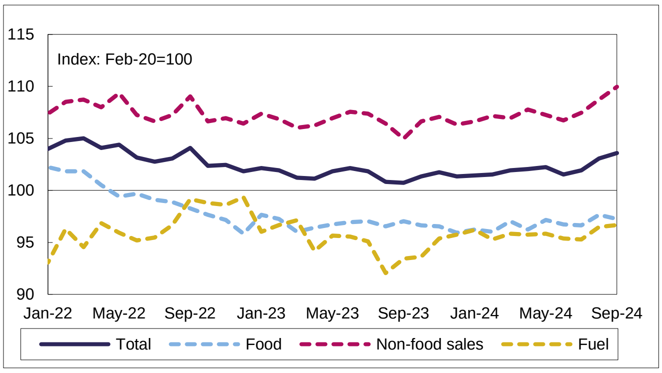
September retail sales data suggest GDP was led by household consumption in Q3

The first estimate of euro area GDP for Q3 surprised to the upside, with growth accelerating to a two-year high of 0.4%Q/Q. A more comprehensive expenditure breakdown will be published on 6 December, but data published by various member states – including Germany, France and Spain – suggest that growth was led by household consumption. Certainly, today's euro area retail sales figures were more encouraging, with sales volumes up for a third consecutive month and by 0.5%M/M. And reflecting notable back revisions to due to the inclusion of German data for the first time since April, September marked the eighth increase of the past nine months, with the level in August more than 1% higher than previously estimated. This left sales up 0.9%Q/Q in Q3, the strongest quarterly rise since Q421. Tallying the recent improvement in household purchase intentions, sales of core items – i.e. non-food and non-fuel – rose for a third consecutive months and by a firmer 1.0%M/M, to leave core sales up 1.4%Q/Q, the most in three years. While spending on auto fuel rose for a second successive month (0.2%M/M), sales at food stores slipped back (-0.5%M/M). This left them up a more modest 0.5%Q/Q a piece in Q3.

German IP declined in September, to register a fifth contraction in six quarters

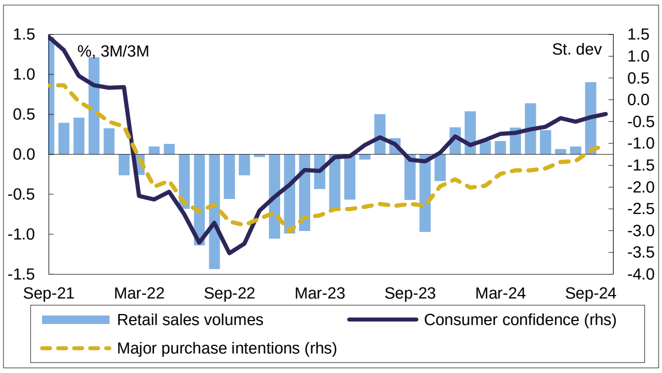
Amid heightened global political uncertainties, Chancellor Scholz yesterday evening unsurprisingly dismissed his uncooperative Finance Minister Lindner – leader of the Free Democrat Party (FDP) – leading to the collapse of the government and raising the likelihood of an early election, possibly in March next year. Scholz's Social Democrat Party (SDP) continue to lag behind opposition Christian Democratic Union (CDU), not least due to the woeful economic performance over recent years. And while last week's preliminary GDP release revealed a surprise tick up in German economic output in Q3 (0.2%Q/Q), today's industrial production release continued to illustrate ongoing significant challenges. As flagged by yesterday's turnover figures, industrial production fell sharply in September, by 2.5%M/M. This confirms a decline of 1.9%3M/3M in Q3 – marking a fifth negative contribution to GDP growth in six quarters. This left industrial output some 13% below its pre-pandemic level and more than 16% below the peak in 2017. Today's figures confirmed that production in autos fell back by -7.8%M/M in September in response to the increase of 15.4%M/M in August, leaving autos production only slightly improved on Q2 (0.3%3M/3M). With the exception of machinery & food, there was a broad-based decline in manufacturing industries, with output from energy-intensive industries dropping 3.3%M/M. Overall manufacturing production fell 2.8%M/M, to be down 1.9%3M/3M. And with construction down 1.4%3M/3M, we think there is a non-negligible risk of a modest downwards to Q3 GDP in due course.

Euro area: Retail sales



Source: Macrobond and Daiwa Capital Markets Europe Ltd.

Euro area: Retail sales & consumer confidence



Source: Macrobond and Daiwa Capital Markets Europe Ltd.

The week ahead in the euro area

The coming week will bring the euro area's industrial production figures for September, which will provide an update on manufacturing activity at the end of Q3. Figures published by member states over recent days – notably Germany and France – have disappointed, signalling a notable contraction that month following the autos-driven acceleration in August. Admittedly, the euro area figure will depend in part on tomorrow's Italian and (more notably) Irish data, for which the latter is highly volatile and often has a non-negligible impact on the aggregate figure. But having risen a cumulative 12.4% in July and August, we might expect to see some payback in Ireland at the end of Q3. Overall, we expect euro area industrial production to decline in September, possibly fully reversing the 1.8%M/M increase in August. This would leave output unchanged over the third quarter as a whole. A significantly negative print could bring a modest downwards revision to Q3 GDP, although we currently expect the updated estimate (due on Thursday) to confirm the 0.4%Q/Q expansion recorded in the preliminary release. This report will be accompanied by employment data for Q3, which, despite the deterioration in firms' hiring intentions recorded in the PMIs and Commission surveys, are expected to record the 14th consecutive quarter of growth.

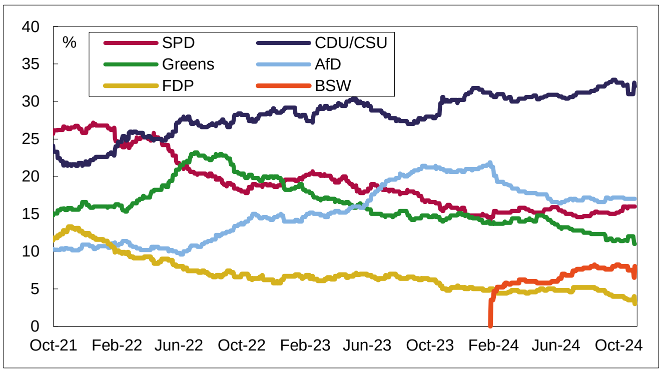
Ahead of this, the ZEW sentiment survey (due Tuesday) will provide an update on investor perceptions in the first half of November. Tallying with the message from the past week's Sentix investor survey, this might well suggest a modest improvement in current conditions and expectations for the coming six months in the largest member state, further suggesting that the bottom in the downturn has been reached. Separately, final October inflation figures will be published from Germany (Tuesday), France and Italy (both due Friday). Headline inflation in all three member states ticked higher in October, due principally to energy prices. But the granular detail will be watched for signs of persistence in underlying services inflation. The ECB's account from the Governing Council's 17 October policy meeting when it cut rates for a second-successive meeting and the third time this year will be published on Thursday.

UK

Bank Rate cut by 25bps to 4.75%, but Bailey cautions about cutting too quickly and by too much

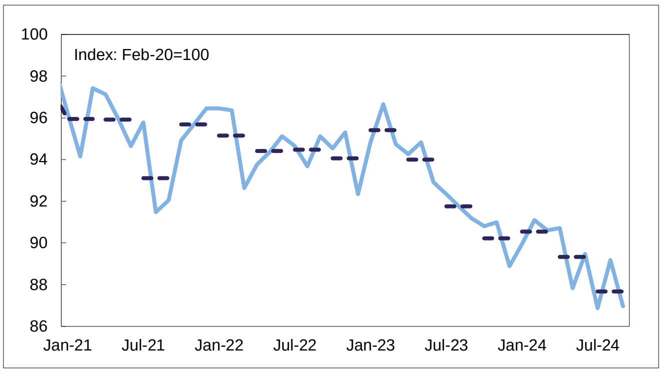
As expected, the BoE today announced a 25bps cut in interest rates, taking Bank Rate down to 4.75%, its lowest since June 2023. A strong majority on the MPC (8-1) saw enough progress on disinflation to cut rates for a second time this cycle. The notoriously hawkish external MPC member Mann was the sole member voting to maintain Bank Rate at 5.00%. For this member structural factors in wage and price-setting dynamics were delaying the underlying disinflation process, while the uncertainties of the impact of recent Budget announcements – related not least to the increase in the employers NICS

Germany: Political polling averages*



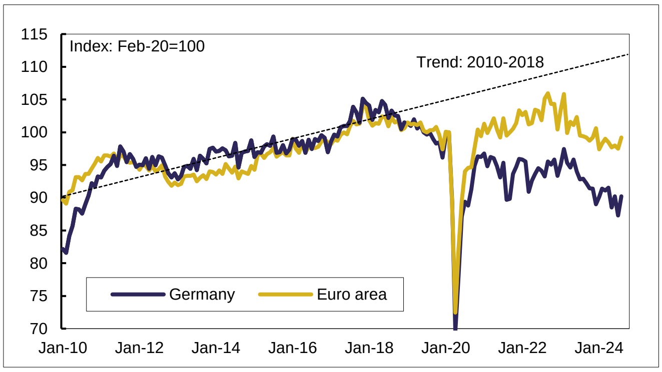
*Rolling average of latest polls by Kantar, YouGov, Allensbach, Infratest & Forschungsgruppe. Source: Macrobond and Daiwa Capital Markets Europe Ltd.

Germany: Industrial production*



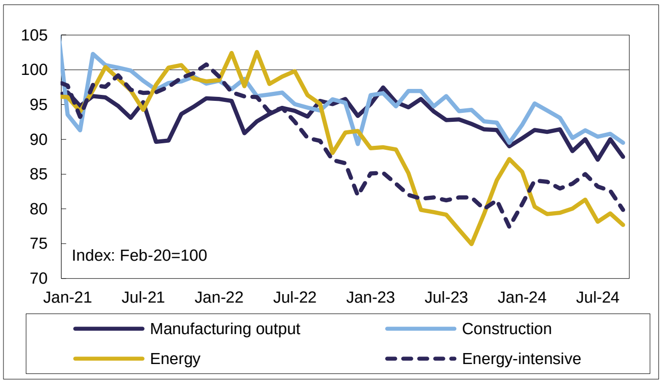
*Dashed lines denote quarterly average
Source: Macrobond and Daiwa Capital Markets Europe Ltd.

Germany: Industrial production trend



Source: Macrobond and Daiwa Capital Markets Europe Ltd.

Germany: Industrial production



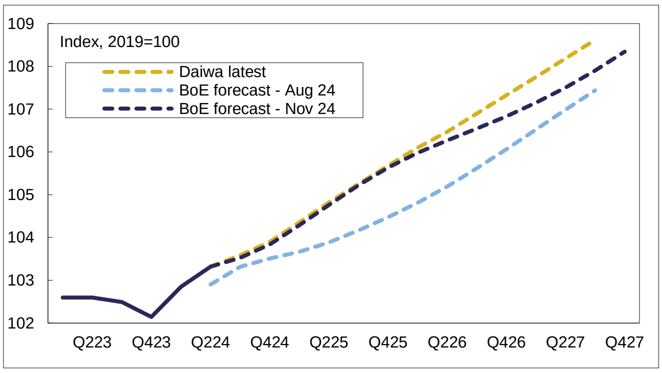
Source: Macrobond and Daiwa Capital Markets Europe Ltd.

contributions – requiring greater time to assess. Admittedly, the BoE nudged up both its CPI inflation and GDP projections compared with August as a result (see below). And the statement again maintained that policy would “remain restrictive for sufficiently long until the risks to inflation returning sustainably to the 2% target in the medium term had dissipated further”. Indeed, in his post-meeting commentary, Governor Bailey repeated that to “ensure inflation stays close to target, interest rates should not be cut too quickly or by too much”. This notwithstanding, he also acknowledged that if the economy evolves as expected, it is likely that interest rates will continue to fall gradually from here. As such, we think the MPC will proceed relatively cautiously with one 25bps cut a quarter – coinciding with the Bank’s updated macroeconomic projections – taking Bank Rate to 3.75% in Q425, which we think will mark the terminal rate this cycle.

Budget pushes BoE’s GDP and inflation profiles up, but 2% target still to be met in forecast horizon

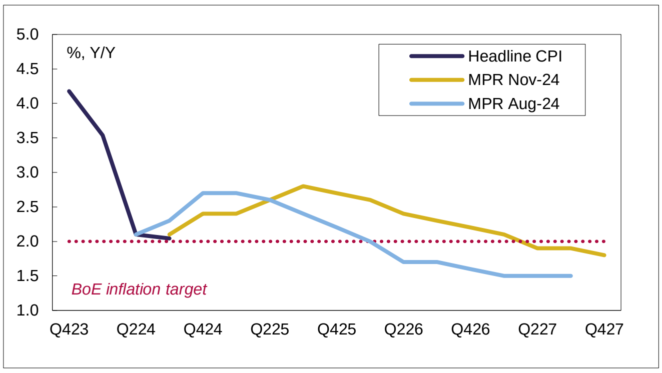
The Bank’s updated macroeconomic projections assumed that a period of economic slack may be required to normalise pay and price-setting dynamics to support the ongoing dissipation of inflation persistence, hence the need to keep policy restrictive over the near term. Indeed, while the BoE still expected growth momentum to have slowed sharply in the second half of this year to ¼%Q/Q in each quarter, it also judged that the impact of the Budget announcements would boost the level of GDP by around ¾% at the peak in a year’s time, relative to the August projections. And so, the BoE now expected annual GDP growth to accelerate to 1.5%Y/Y in 2025 – ½ppt higher than in August – before slowing in 2026 (1.4%Y/Y) and 2027 (1.2%Y/Y). In terms of the inflation outlook, like in August, the BoE projected the headline CPI rate to tick higher in Q4 due to the near-10% hike in the household regulated energy price cap in October. Admittedly, given the faster pace of disinflation over the summer than previously expected, the Bank revised down its projection for headline inflation in Q424 and Q125, by 0.3ppt a piece to 2.4%Y/Y. But the Budget announcements were judged to boost CPI inflation by just under ½ppt at its peak next year, reflecting both the indirect effects of the smaller margin of excess supply and direct impacts from the measures. As such, the profile for the Bank’s modal inflation projection from the middle of 2025 was revised higher, now expected to peak at 2.8%Y/Y in Q325, before subsequently resuming a gradual downward trend. Importantly, the Bank still expected a return to below the 2%Y/Y target within the forecast horizon in Q227, albeit a year later than it had previously assumed. And it is worth noting the tightening in financial market conditions over the past week, with 2Y Gilt yields a little more than 30bps higher than that assumed in the Bank’s projections. The inflationary impact of the increase in employers NICS contributions is also highly uncertain. So, overall, Bailey suggested that the path of interest rates will unlikely be significantly different in light of the Budget.

UK: Real GDP projections*



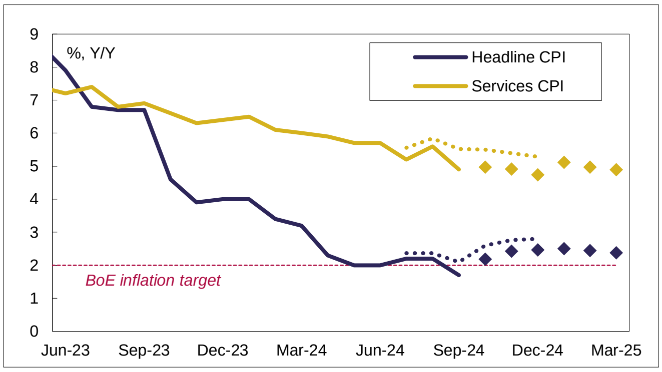
*At market-implied interest rates (4.8% 2024; 3.7% 2025 & 2026; 3.6% 2027)
Source: BoE Macrobond and Daiwa Capital Markets Europe Ltd.

UK: BoE CPI inflation projections*



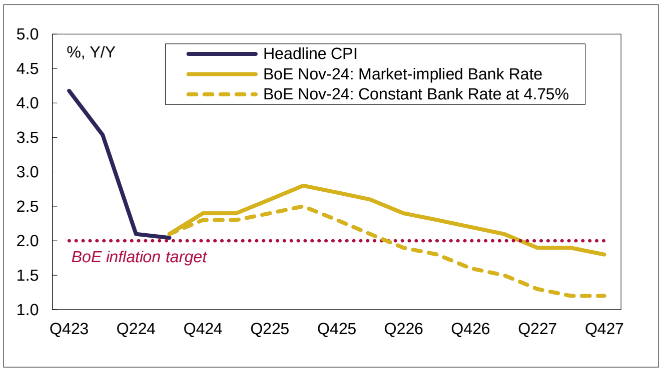
*Modal projections
Source: BoE, Macrobond and Daiwa Capital Markets Europe Ltd.

UK: BoE headline & services CPI projections*



*Diamonds (dashed lines) show projections from Nov-24 MPR (Aug-24 MPR)
Source: BoE, Macrobond and Daiwa Capital Markets Europe Ltd.

UK: BoE CPI inflation projections



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

The week ahead in the UK

The coming week will bring several top-tier UK releases – including the latest labour market report (Tuesday) and the first estimates of GDP in Q3 and September (Friday) – that will feed into the BoE's reaction function. Starting with Tuesday's labour marker report, owing to its importance as a key driver of services inflationary pressures, policymakers will be focused primarily on signs of further moderation in private sector regular pay growth for a fifth consecutive month. Leading indicators for total wages have so far hinted towards a gradual moderation in September – including the HMRC PAYE series (which fell by 1.4ppts to 3.4%3M/3M on an annualized basis in September), as well as more subtle progress from the BoE's own DMP survey data (down 0.1ppts to 5.7%3M/Y). With regards to Friday's GDP release, like the BoE, we expect this to confirm a notable moderation in growth momentum in Q3. Admittedly, survey indicators such as the PMIs signalled a particularly strong performance in construction and manufacturing sectors in September. And September's retail sales data also suggests that GDP returned to growth that month, at of 0.4%M/M in September. This notwithstanding, this would leave GDP over the third quarter as a whole at 0.3%Q/Q – down from 0.5%Q/Q in Q2 and 0.6%Q/Q in Q1. Given rising real incomes, household consumption looks to have provided a positive contribution.

The next edition of the Euro wrap-up will be published on 12 November 2024

Daiwa economic forecasts

	2024			2025					
	Q2	Q3	Q4	Q1	Q2	Q3	2023	2024	2025
GDP	**%, Q/Q**						**%, Y/Y**		
Euro area	0.2	0.4	0.1	0.3	0.3	0.3	0.5	0.7	1.0
UK	0.5	0.3	0.3	0.4	0.4	0.4	0.3	0.9	1.6
Inflation, %, Y/Y									
Euro area									
Headline HICP	2.5	2.2	2.3	2.1	1.8	1.8	5.4	2.4	2.0
Core HICP	2.8	2.8	2.8	2.5	1.9	1.8	4.9	2.9	2.1
UK									
Headline CPI	2.1	2.0	2.3	2.3	2.1	2.3	7.3	2.5	2.2
Core CPI	3.6	3.3	3.3	3.3	2.3	2.0	6.2	3.7	2.3
Monetary policy, %									
ECB									
Deposit Rate	3.75	3.50	3.00	2.50	2.25	2.25	4.00	3.00	2.25
Refi Rate	4.25	3.65	3.15	2.65	2.40	2.40	4.50	3.15	2.40
BoE									
Bank Rate	5.25	5.00	4.75	4.50	4.25	4.00	5.25	4.75	3.75

Source: Bloomberg, ECB, BoE and Daiwa Capital Markets Europe Ltd.

Daiwa Capital Markets

European calendar

Today's results

Economic data

Country	Release	Period	**Actual**	Market consensus/ *Daiwa forecast*	Previous	Revised
Euro area	Construction PMI	Oct	**43.0**	-	42.1	-
	Retail sales M/M% (Y/Y%)	Sep	**0.5 (2.9)**	0.4 (1.3)	0.2 (0.8)	1.1 (2.4)
Germany	Industrial production M/M% (Y/Y%)	Sep	**-2.5 (-4.6)**	-1.0 (-3.0)	2.9 (-2.7)	2.6 (-3.0)
	Trade balance €bn	Sep	**17.0**	20.9	22.5	21.4
	Construction PMI	Oct	**40.2**	-	41.7	-
France	Preliminary private sector wages Q/Q%	Q3	**-0.1**	0.0	-0.1	-
	Construction PMI	Oct	**42.2**	-	37.9	-
Italy	Construction PMI	Oct	**48.2**	-	47.8	-
Spain	Industrial production M/M% (Y/Y%)	Sep	**0.5 (0.6)**	0.4 (0.2)	-0.1 (-0.1)	-
UK	BoE Bank Rate %	Nov	**4.75**	***4.75***	5.00	-
	DMP 3M output price (1Y CPI) expectations %	Oct	**3.5 (2.5)**	-	3.6 (2.7)	3.5 (-)

Auctions

Country	Auction
France	sold €6.94bn of 3% 2034 bonds at an average yield of 3.24%
	sold €2.35bn of 4.75% 2035 bonds at an average yield of 3.24%
	sold €1.2bn of 0.5% 2044 bonds at an average yield of 3.55%
	sold €2.01bn of 3.25% 2055 bonds at an average yield of 3.78%
Spain	sold €2.39bn of 2.7% 2030 bonds at an average yield of 2.749%
	sold €495mn of 0.7% 2033 inflation-linked bonds at an average yield of 1.104%
	sold €1.61bn of 4% 2054 bonds at an average yield of 3.877%

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

Friday's releases

Economic data

Country	GMT	Release	Period	Market consensus/ *Daiwa forecast*	Previous
France	07.45	Trade balance €bn	Sep	-	-7.4
	07.45	Preliminary wages Q/Q%	Q3	0.5	0.6
Italy	09.00	Industrial production M/M% (Y/Y%)	Sep	-0.5 (-3.5)	0.1 (-3.2)

Auctions and events

Country	GMT	Event
Italy	10.00	ISTAT to publish monthly report on Italian economy
UK	00.01	KPMG, REC and S&P Global release UK report on jobs for October
	12.15	BoE Chief Economist Pill to brief Bank's Agents on updated macroeconomic projections

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

The coming week's data calendar

The coming week's key data releases

Country	GMT	Release	Period	Market consensus/ *Daiwa forecast/*	Previous
		Monday 11 November 2024			
		- Nothing scheduled -			
		Tuesday 12 November 2024			
Germany	07.00	Final HICP (CPI) Y/Y%	Oct	2.4 (2.0)	1.8 (1.6)
	10.00	ZEW investor survey – current situation (expectations) balance %	Nov	-	-86.9 (13.1)
UK	07.00	Average wages (excluding bonuses) 3M/Y%	Sep	-	3.8 (4.9)
	07.00	Unemployment rate 3M%	Sep	-	4.0
	07.00	Employment 3M/3M change 000s	Sep	-	373
	07.00	Payrolled employees M/M change 000s	Oct	-	-15
	07.00	Claimant count rate % (change 000s)	Oct	-	4.7 (27.9)
		Wednesday 13 November 2024			
Euro area	10.00	Industrial production M/M% (Y/Y%)	Sep	-	1.8 (0.1)
		Thursday 14 November 2024			
Euro area	10.00	GDP – second estimate Q/Q% (Y/Y%)	Oct	0.4 (0.9)	0.2 (0.6)
	10.00	Preliminary employment Q/Q% (Y/Y%)	Q3	-	0.2 (0.8)
Spain	08.00	Final HICP (CPI) Y/Y%	Oct	1.8 (1.8)	1.7 (1.5)
UK	00.01	RICS house price balance %	Oct	-	11
		Friday 15 November 2024			
France	07.45	Final HICP (CPI) Y/Y%	Oct	1.5 (1.2)	1.4 (1.1)
Italy	09.00	Final HICP (CPI) Y/Y%	Oct	1.0 (0.9)	0.7 (0.7)
UK	07.00	GDP – first estimate Q/Q% (Y/Y%)	Q3	*0.3 (1.1)*	0.5 (0.7)
	07.00	Monthly GDP M/M% (3M/3M%)	Sep	*0.4 (0.3)*	0.2 (0.2)
	07.00	Services output M/M% (3M/3M%)	Sep	-	0.1 (0.1)
	07.00	Industrial output M/M% (Y/Y%)	Sep	-	0.5 (-1.6)
	07.00	Construction output M/M% (Y/Y%)	Sep	-	0.4 (0.3)
	07.00	Trade (goods trade) balance £bn	Sep	-	-1.0 (-15.0)

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

The coming week's key events & auctions

Country	GMT	Event / Auction
		Monday 11 November 2024
		- Nothing to report -
		Tuesday 12 November 2024
Germany	10.30	Auction: to sell €5bn of 2% 2026 bonds
UK	10.00	Auction: to sell £2.25bn of 4.75% 2043 bonds
		Wednesday 13 November 2024
Germany	10.30	Auction: to sell €4bn of 2.6% 2034 bonds
Italy	10.00	Auction: to sell bonds*
UK	10.00	Auction: to sell £4bn of 4.375% 2028 bonds
		Thursday 14 November 2024
Euro area	12.30	ECB publishes monetary policy account of October Governing Council meeting
UK	21.00	BoE Governor Bailey delivers speech to Mansion House annual financial and professional services dinner
		Friday 15 November 2024
		- Nothing to report -

**Details to be announced. Source: Bloomberg and Daiwa Capital Markets Europe Ltd.*

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