

Euro wrap-up

Overview

- Bunds made modest losses as political uncertainty continued to dominate the news flow in France and data suggested that the industrial sector supported French GDP growth in Q3.
- Gilts made gains after a big downwards revision to the final UK PMIs implied that economic growth might have ground to a halt.
- The coming week will bring August data for euro area retail sales, German industrial production, factory orders and goods trade, while the account of the ECB's September policy-setting meeting is also due.

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Daily bond market movements

Bond	Yield	Change
BKO 1.9 09/27	2.011	+0.007
OBL 2.2 10/30	2.301	+0.008
DBR 2.6 08/35	2.699	+0.001
UKT 3¾ 03/27	3.959	-0.018
UKT 4¾ 03/30	4.115	-0.019
UKT 4½ 03/35	4.689	-0.020

*Change from close as at 4:20pm BST.
Source: Bloomberg

Euro area

In bid for survival, Lecornu promises not to use constitutional powers to force through Budget

Politics inevitably continues to dominate in France, where Prime Minister Lecornu today was meeting party leaders to try to reach agreement on a Budget plan ahead of a possible vote of no confidence as early as next week. Unlike his predecessors and to demonstrate a willingness to compromise and thus avoid immediate rejection of his government, he insisted that he would not use constitutional powers under Article 49.3 to force a Budget through parliament without a vote if his draft legislation fails to get majority backing. In a bid to gain support from the centre-left, he offered a new financial wealth tax, albeit one not as potent as the Zucman tax sought by the Socialist Party leadership. He also promised action on immigration to appeal to the right. On paper, that policy mix could offer a workable pathway to government survival and eventual delivery of a Budget. But his proposal to cut the fiscal deficit next year by 0.7ppt to 4.7% of GDP, as well as a reluctance to make major concessions on pensions and cuts to public expenditure, might well still prove too aggressive for most representatives in the National Assembly.

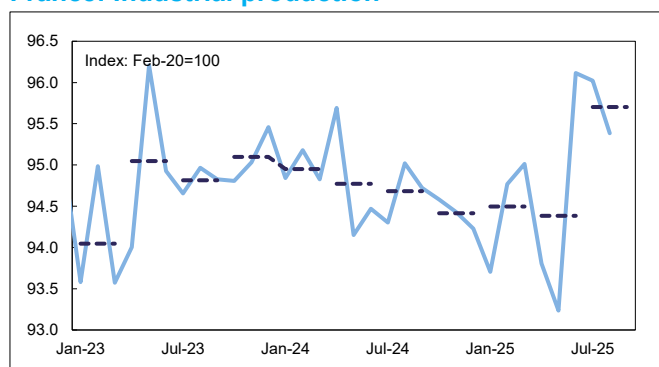
French industrial sector on track to boost Q3 GDP despite decline in August

Thankfully, the French economy remains relatively resilient to the political shenanigans. Indeed, today's industrial output data supported our view that French GDP growth in Q3 was close to the 0.3%Q/Q expansion in Q2. At face value, the August outturn disappointed expectations, with production down for a second successive month, by 0.7%M/M, the steepest drop since April. But the decline in July (-0.1%M/M) was significantly smaller than initially estimated. And given the positive carry over from June, IP was trending almost 1½% above the Q2 average. The weakness in August was principally driven by non-autos transport equipment (-6.0%M/M) as further payback for a surge in June. But this subsector still appears on track for solid growth over Q3 as a whole. A jump in ICT equipment output to the highest level since mid-2006 left it trending some 5½% higher than in Q2. And despite a fall in August, production of basic metals, coke and petroleum products also likely provided support in Q3. In contrast, autos output declined for a third month out of four to a seven-month low, while general and electrical machinery was also likely a modest drag on production in Q3. But outside of manufacturing, encouragingly, construction activity rose 1.2%M/M to the highest level this year, while energy was also on track to add to GDP growth.

Services PMIs flag downside risks to French outlook while Spain continues to outperform

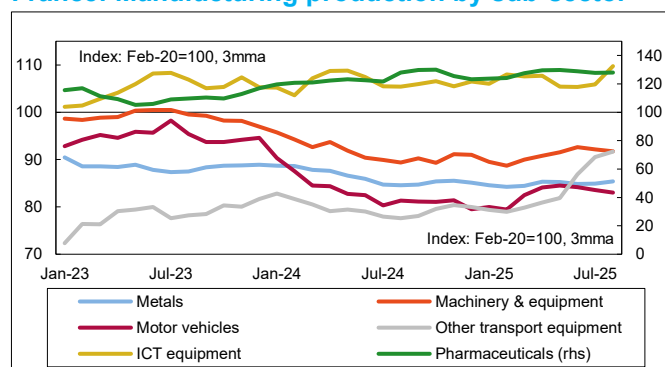
Despite the positive momentum in the middle of Q3, recent strike action against fiscal tightening measures might well have hit activity in September. Indeed, we suspect that this in part drove the deterioration in the latest French services PMI (48.5), which almost fully reversed the improvement in August and pushed the composite output index down to a five-month low

France: Industrial production*



*Dark blue dashed lines represent quarterly average.
Source: Macrobond and Daiwa Capital Markets Europe Ltd.

France: Manufacturing production by sub-sector



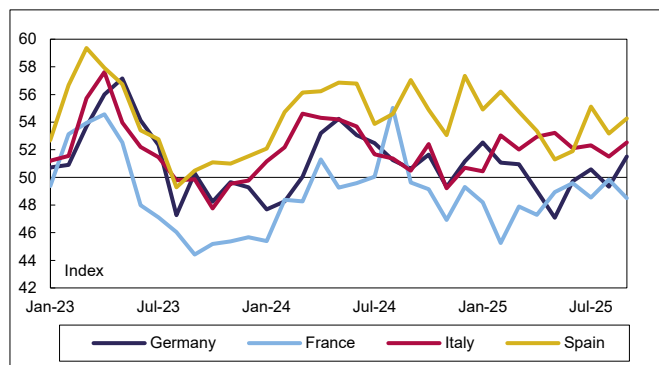
Source: Macrobond and Daiwa Capital Markets Europe Ltd.

(48.1), firmly in contractionary territory. We note, however, that the INSEE survey – which has a sample more than ten times larger than the PMIs – signalled the strongest services activity in seven months in September. Admittedly, the German services PMI in September was also revised lower from the flash by a full percentage point to 51.5. But as the manufacturing output component was pushed higher, the German composite index (52.0) was nevertheless the strongest in 16 months, with its quarterly index up more than 1pt consistent with modest expansion. The Italian (52.5) and Irish services PMIs (53.5) were also the firmest since May, while the equivalent Spanish index (54.3) implied ongoing outperformance in the region. Indeed, the quarterly Spanish composite PMI (54.1) in Q3 was more than 2pts higher than in Q2. Overall, the final euro area composite output index (51.2) pointed to a further moderate recovery in growth momentum at the end of Q3. But while that meant the quarterly average was the best since Q224, its level (51.0) might normally suggest GDP growth no stronger than 0.1%Q/Q. On balance, we maintain our view that euro area growth was a little stronger than that, picking up to 0.2%Q/Q. And the new business component rose to the highest since May 2024, suggesting ongoing recovery into year-end. As such, we continue to think that the ECB's rate-cutting cycle has concluded.

The week ahead in the euro area

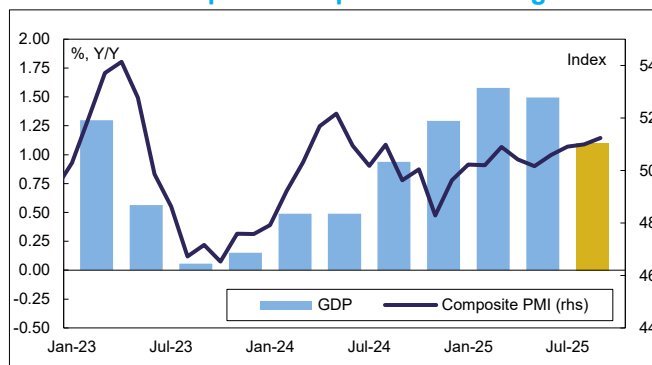
The focus over the coming week in the euro area will be the August activity data, with figures for euro area retail sales (Monday) and industrial production in Germany (Wednesday), Spain (Tuesday), Ireland (Thursday) and Italy (Friday) providing signals on growth in Q3. We expect euro area retail sales volumes to have barely risen in August. But taken alongside a modest upwards revision to July's number (-0.5%M/M), that should leave sales trending just a touch below the Q2 level, maintaining scope for a potential eighth-consecutive quarterly rise in retail sales volumes and helping prospects for a positive contribution from private consumption to GDP. Meanwhile, German IP probably softened into August, owing to the surprisingly strong outturn in July (1.3%M/M), summer maintenance and potential turbulence surrounding the EU-US trade talks. We note, however, that the German Ifo and PMI production indices pointed to another firm month for IP, suggesting that a decline may be relatively modest. In similar vein, factory orders are also expected to receive some payback. But those too seem unlikely to fully reverse July's sharp drop (-2.9%M/M), not least given the effects of bulk orders, weaker US demand and the stronger euro. Indeed, [German exports](#) continued their downtrend at the start of Q3, principally owing to the pullback in shipments to the US. The August trade data (Thursday) should continue to reflect that trend. Hard data aside, the coming week will also bring the ECB account of September's Governing Council meeting (Thursday), at which the ECB elected to hold policy rates, whilst President Lagarde reiterated that policy was in a 'good place'. The account is likely to convey a similar tone, setting out that while uncertainty remains more elevated than usual, the risks to the outlook have become more balanced, consistent with our view that the ECB has cut for the last time this cycle. A speech from Chief Economist Lane (Monday) may provide more insights into the ECB's reaction function going forward.

Euro area member states: Services PMIs



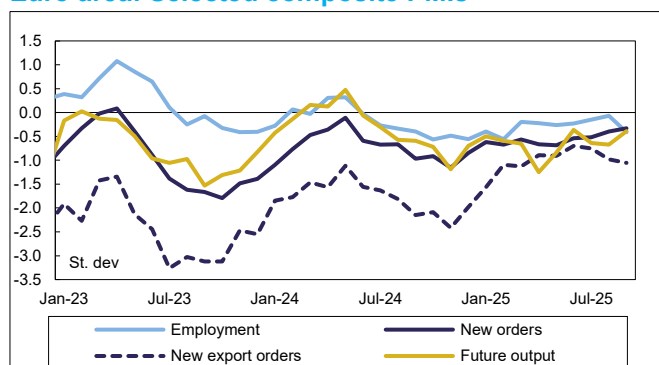
Source: S&P Global, Macrobond and Daiwa Capital Markets Europe Ltd.

Euro area: Composite output PMI & GDP growth*



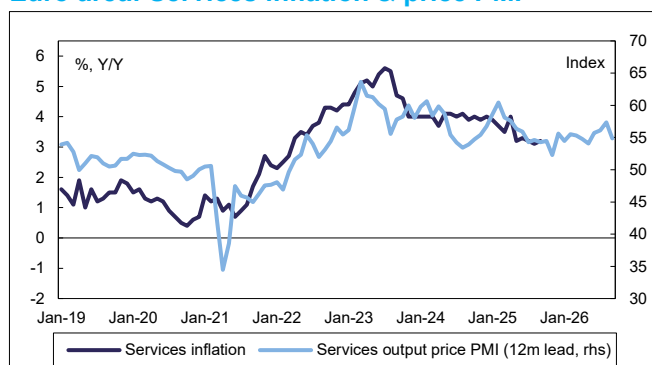
*Gold bar represents Daiwa's Q325 forecast. Source: S&P Global, Macrobond and Daiwa Capital Markets Europe Ltd.

Euro area: Selected composite PMIs



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

Euro area: Services inflation & price PMI



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

UK

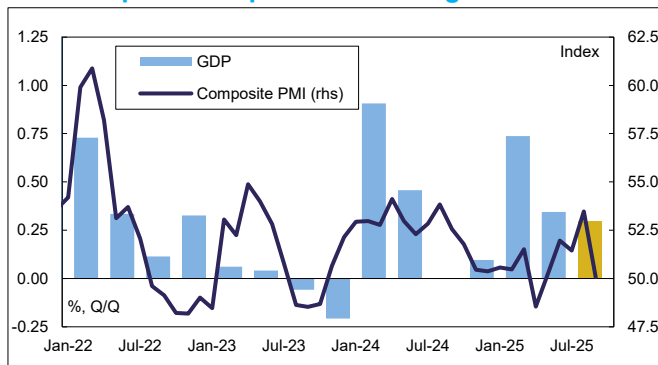
Sharp downwards revision to services PMI flags marked loss of growth momentum at end-Q3

Today's final services PMIs suggested that a further rate cut this year still can't be ruled out. More importantly, it left the services activity and headline composite output indices at five-month lows and at levels suggesting that economic growth momentum ground to a halt at the end of Q3. The deterioration in services in September was surprisingly marked, with the activity index falling 3.4pts from August's 16-month high to just 50.8, consistent with minimal expansion in the all-important sector. Growth in services new orders also slowed sharply, reportedly due in part to concerns about possible future tax hikes to come in the November Budget. And external demand in the sector fell on persistent global uncertainty. With backlogs of work down too, services firms' confidence in the outlook also inevitably softened. While the final manufacturing PMIs, published earlier this week, were revised only minimally from the flash estimates, the output index (45.7) had signalled the sharpest drop in factory output in six months amid extremely weak demand from home and abroad. So, the composite output PMI was revised down by almost 1pt from the flash estimate to be down almost 3½pts from August at a stagnant 50.1. The Q3 average (51.7) was still up on Q2 (50.3), when GDP grew 0.3%Q/Q. But the signs of a significant loss of growth momentum at the end of the quarter, also reflected in the further drop in the employment PMI well below 50, flags the risk of further deterioration into Q4 as tax-related uncertainty persists. Given sticky services inflation, the MPC's hawks might be unperturbed by the weakening of activity suggested by this survey. But the majority who voted for a cut in August will be mindful of the suggestion of a renewed pickup in downside risks to the outlook. So, a further fall in the composite PMI well into contraction territory in October would leave the outcome of the MPC's November rate vote very finely balanced.

The week ahead in the UK

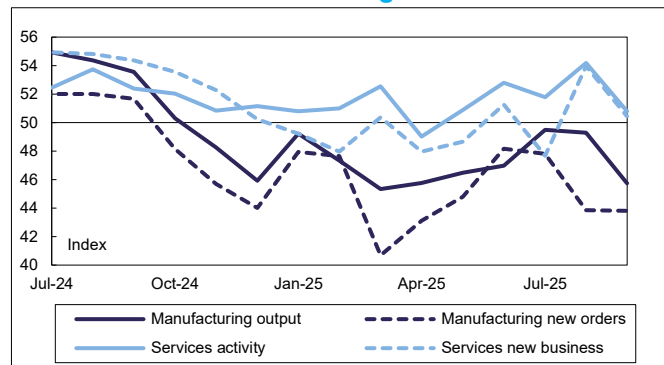
It should be a relatively quiet week ahead for UK economic news, with just a handful of second-tier surveys scheduled for release and speeches from BoE Governor Bailey (Monday) and Chief Economist Pill (Wednesday) otherwise. It is unclear as to whether Bailey will comment specifically on monetary policy in his speech. But it is highly likely that Pill will reiterate his preference to hold rates, given his stated concerns about inflation persistence and previous calls for a more 'cautious' approach to policy easing. The week's economic dataflow will kick off with September's construction PMIs (Monday). While that indicator has proved an unreliable guide to the official construction output series in recent months, its trend so far this quarter has deteriorated some 2.9pts relative to Q2 to be suggestive of an entrenched contraction. The RICS residential market survey (Thursday) will also give an indication as to whether angst about fiscal policy continues to weigh on broader housing market conditions, while we expect the REC jobs survey (Friday) to remain consistent with a weakening labour market.

UK: Composite output PMI & GDP growth*



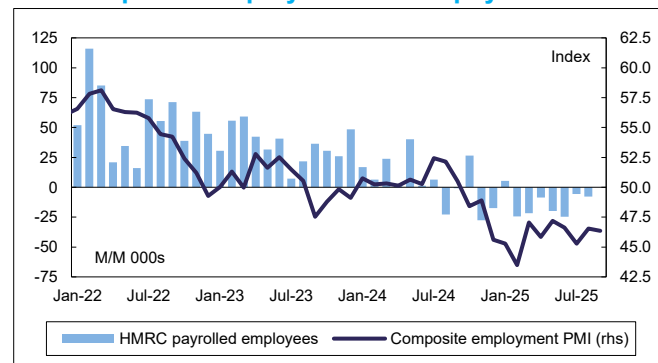
*Gold bar represents Daiwa's Q325 forecast. Source: S&P Global, Macrobond and Daiwa Capital Markets Europe Ltd.

UK: Services & manufacturing PMIs



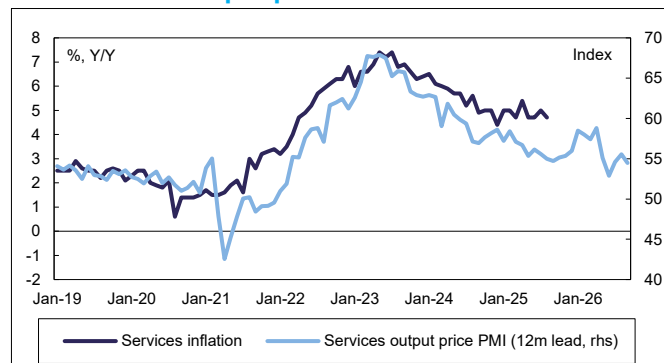
Source: S&P Global, Macrobond and Daiwa Capital Markets Europe Ltd.

UK: Composite employment PMI & payrolls












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

UK: Services output price PMI & inflation












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

Daiwa economic forecast

		2025				2026		2025	2026	2027
		Q1	Q2	Q3	Q4	Q1	Q2			
GDP		%, Q/Q						%, Y/Y		
Euro area		0.6	0.1	0.2	0.2	0.3	0.3	1.3	1.0	1.4
UK		0.7	0.3	0.3	0.3	0.3	0.4	1.5	1.3	1.5
Inflation, %, Y/Y										
Euro area										
Headline HICP		2.3	2.0	2.1	2.2	1.7	1.8	2.2	1.7	1.9
Core HICP		2.6	2.4	2.3	2.4	2.2	1.7	2.4	1.8	1.8
UK										
Headline CPI		2.8	3.5	3.8	3.5	3.1	2.5	3.4	2.6	1.9
Core CPI		3.6	3.7	3.7	3.5	3.3	2.6	3.6	2.6	1.7
Monetary policy, %										
ECB										
Deposit Rate		2.50	2.00	2.00	2.00	2.00	2.00	2.00	2.00	2.00
Refi Rate		2.65	2.15	2.15	2.15	2.15	2.15	2.15	2.15	2.15
BoE										
Bank Rate		4.50	4.25	4.00	4.00	3.75	3.50	4.00	3.50	3.50















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

European calendar

Today's results							
Economic data							
Country	Release		Period	Actual	Market consensus/ <i>Daiwa forecast</i>	Previous	Revised
Euro area		Final composite (services) PMI	Sep	51.2 (51.3)	51.2 (51.4)	51.0 (50.5)	-
		PPI Y/Y%	Aug	-0.6	-0.4	0.2	-
Germany		Final composite (services) PMI	Sep	52.0 (51.5)	52.4 (52.5)	50.5 (49.3)	-
France		Industrial production M/M% (Y/Y%)	Aug	-0.7 (0.4)	0.3 (0.6)	-1.1 (1.3)	-0.1 (1.8)
		Final composite (services) PMI	Sep	48.1 (48.5)	48.4 (48.9)	49.8 (49.8)	-
Italy		Composite (services) PMI	Sep	51.7 (52.5)	51.5 (51.5)	51.7 (51.5)	-
		Retail sales M/M% (Y/Y%)	Aug	-0.1 (0.5)	-	0.0 (1.8)	-
Spain		Composite (services) PMI	Sep	53.8 (54.3)	53.3 (53.3)	53.7 (53.2)	-
UK		Final composite (services) PMI	Sep	50.1 (50.8)	51.0 (51.9)	53.5 (54.2)	-
Auctions							
Country	Auction						
- Nothing to report -							

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

The coming week's key data releases

Country	BST	Release	Period	Market consensus/ <i>Daiwa forecast</i>	Previous
Monday 6 October 2025					
Euro area		08.30 Construction PMI	Sep	-	46.7
		09.30 Sentix investor confidence indicator	Oct	-7.9	-9.2
		10.00 Retail sales M/M% (Y/Y%)	Aug	0.1 (1.3)	-0.5 (2.2)
Germany		08.30 Construction PMI	Sep	-	46.0
France		08.30 Construction PMI	Sep	-	46.7
Italy		08.30 Construction PMI	Sep	-	47.7
Spain		08.00 Industrial production M/M% (Y/Y%)	Aug	0.4 (3.5)	-0.5 (2.5)
UK		09.30 Construction PMI	Sep	46.5	45.5
Tuesday 7 October 2025					
Germany		07.00 Factory orders M/M% (Y/Y%)	Aug	1.4 (3.0)	-2.9 (-3.4)
France		07.45 Trade balance €bn	Aug	-	-5.6
Wednesday 8 October 2025					
Germany		07.00 Industrial production M/M% (Y/Y%)	Aug	-1.0 (-0.4)	1.3 (1.5)
Thursday 9 October 2025					
Germany		07.00 Trade balance €bn	Aug	15.5	14.8
UK		00.01 RICS house price balance %	Sep	-17	-19
Friday 10 October 2025					
Italy		09.00 Industrial production M/M% (Y/Y%)	Aug	-0.3 (0.8)	0.4 (0.9)

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

The coming week's key events & auctions

Country	BST	Event / Auction
Monday 6 October 2025		
Euro area		09.00 ECB Chief Economist Lane to give keynote speech at the ECB Conference on Monetary policy, Frankfurt.
		18.00 ECB President Lagarde to appear before EU Parliament Committee on Economic and Monetary Affairs (ECON), Strasbourg.
UK		18.30 BoE Governor Bailey to give keynote speech at Scotland's Global Investment Summit, Edinburgh.
Tuesday 7 October 2025		
Germany		10.30 Auction: to sell up to €4.5bn of 2.2% 2030 bonds
UK		10.00 Auction: to sell £1.25bn of 0.125% 2028 bonds
Wednesday 8 October 2025		
Germany		10.30 Auction: to sell up to €1bn of 2.6% 2041 bonds
		10.30 Auction: to sell up to €1bn of 3.25% 2042 bonds
UK		10.00 Auction: to sell £5bn of 4% 2029 bonds
		16.00 BoE Chief Economist Pill to give speech at the University of Birmingham
Thursday 9 October 2025		
Euro area		12.30 ECB to publish monetary policy account of 10-11 September Governing Council meeting
UK		09.30 MPC external member Mann to give speech at Resolution Foundation event on 'Explaining the consumption gap', London.
Friday 10 October 2025		
UK		00.01 REC, KPMG & S&P Global UK Report on Jobs for September

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

Access our research blog at:

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

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