Euro wrap-up

Overview

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- Bunds made losses as the flash euro area PMIs pointed to the firmest economic growth momentum in more than four-years.
- While the flash UK PMIs were consistent with softer growth, Gilts also followed the global trend lower as price pressures in the services sector intensified.
- On Thursday, the German ifo and French INSEE business surveys will provide a crosscheck on the flash PMIs.

Daily bond market movements

Bond	Yield	Change
BKO 2.7 09/28	3.322	+0.103
OBL 2.9 10/31	3.412	+0.119
DBR 3 08/36	3.551	+0.092
UKT 4 05/29	4.901	+0.125
UKT 4⅛ 03/31	4.958	+0.121
UKT 4⅞ 07/36	5.346	+0.109

*Change from close as at 5:00pm BST.
Source: Bloomberg

Euro area

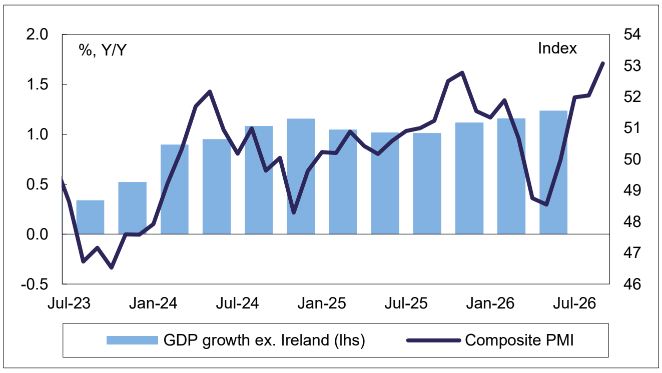
Flash PMIs suggest strongest economic growth momentum in more than four years

The flash euro area PMIs for September reinforced the case for a further ECB rate hike by year-end, signalling a firming of economic growth coupled with intensified cost and price pressures. Most notably, the composite activity PMI significantly beat expectations, rising just over 1pt to 53.1, the highest level since April 2023. And that pushed up the Q3 average to 52.4, the best quarterly result in more than four years suggestive of underlying economic growth of 0.4-0.5%Q/Q. We think that euro area GDP has grown at roughly half that pace this quarter, in part due to the likelihood of payback for the vigour in Ireland in Q2. However, the survey undeniably points to a broad-based pickup in momentum, which if sustained should be reflected in a renewed acceleration in economic activity in Q4. Indeed, the composite new orders index (52.8) suggested the strongest demand growth in more than four years, with new export orders the best since Russia's invasion of Ukraine. And while in recent months the survey suggested that the impetus for growth had become increasingly reliant on the factory sector, the flash September PMIs reported a welcome reacceleration in services, for which the activity index jumped to a 10-month high (53.0). Still buoyed by fiscal spending on defence and AI-related demand, the manufacturing output PMI edged up to its best level since early 2022 (53.4). Geographically too, growth in September appears to have been more widely spread. The German (53.8) and French (51.2) composite PMIs rose to their highest levels in 11 months and more than two years respectively. And while the equivalent index for the rest of the euro area moderated this month, the quarterly average (54.4) was the highest since Q421.

Cost & price pressures rise while labour market remains stable

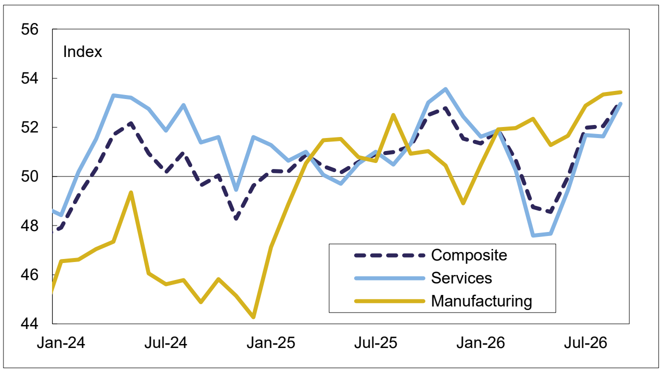
With energy prices sharply higher over the past month, unsurprisingly the flash PMIs reported a pickup in cost pressures in September. The euro area composite input price index rose the most since March to a four-month high (66.5) well above the long-run average. The increase was widely felt across the major sectors and member states. And firms appear increasingly inclined to try to pass on those costs to clients. Despite signs of persisting supply disruption, solid demand in the factory sector and rising backlogs, the rise in the manufacturing output price index (57.1) was relatively moderate and left it still below its level in July. But the equivalent index for services (56.1) rose more sharply to its highest level in more than 2½ years. And, of course, those selling-price indices for both major sectors moved well above their long-run averages. Meanwhile, the composite employment index continued to suggest modestly positive job growth in services and stability in the manufacturing sector. The labour market should still not be considered tight, and policymakers need not panic about possible second-round effects on inflation. But in the round, the flash PMIs will confirm suspicions that the near-term inflation outlook has worsened and that economic activity will be sufficiently resilient to cope with a shift to a 'restrictive monetary stance. Unless energy prices fall significantly over coming weeks, a rate hike in October certainly can't be ruled out.

Euro area: Composite PMI & GDP growth ex-Ireland



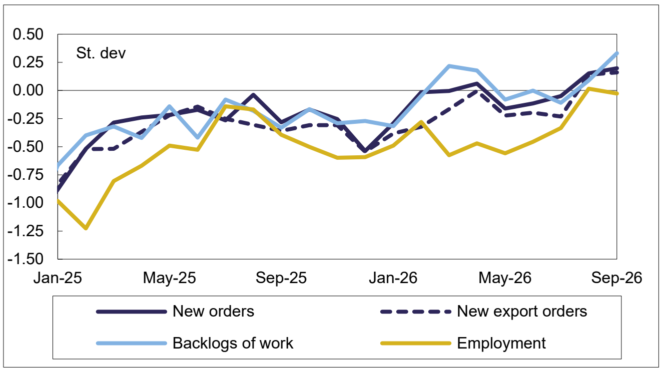
Source: S&P Global, Macrobond and Daiwa Capital Markets Europe Ltd.

Euro area: Output PMIs



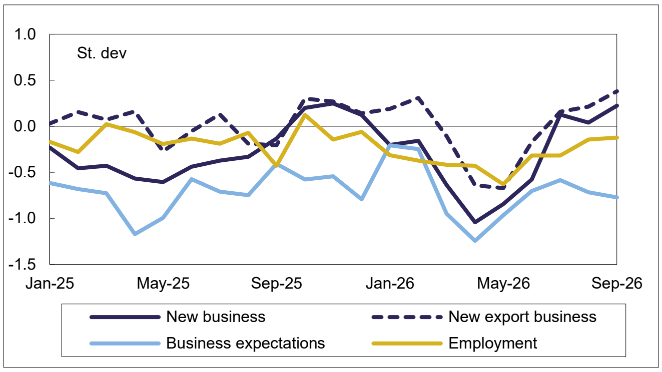
Source: S&P Global, Macrobond and Daiwa Capital Markets Europe Ltd.

Euro area: Selected manufacturing PMIs



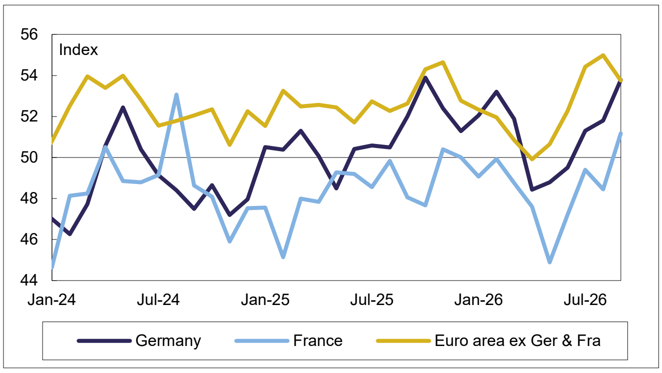
Source: S&P Global, Macrobond and Daiwa Capital Markets Europe Ltd.

Euro area: Selected composite PMIs



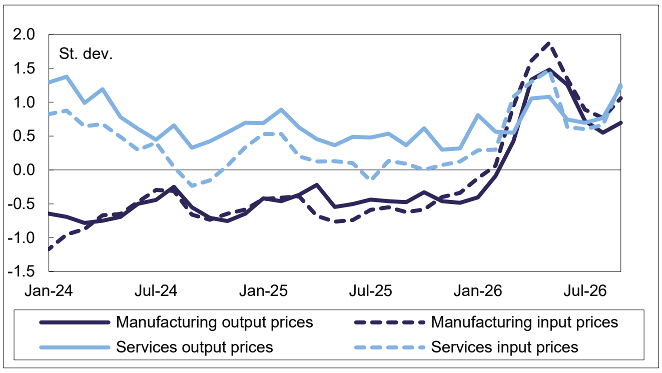
Source: S&P Global, Macrobond and Daiwa Capital Markets Europe Ltd.

Euro area member states: Composite output PMIs



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

Euro area: Manufacturing & services price PMIs



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

The day ahead in the euro area

September's business surveys will remain the focus of the euro area dataflow on Thursday. Specifically, the German ifo and French INSEE surveys – whose wider scope, larger samples and more granular sectoral detail provide more comprehensive assessments of economic activity in the respective member states – will provide a crosscheck on the signals of firmer growth momentum and more intense price pressures in the flash PMIs. Of course, today's results infer a strong likelihood that the national surveys will also point to firmer growth. But to the extent that the ifo and INSEE surveys were less downcast than the equivalent PMIs over recent months, we might expect smaller increases in the headline business climate indices. INSEE's business survey will also be accompanied by an update on French consumer sentiment which is likely to have slipped back in the face of higher energy prices. Finally, Spanish producer price data are likely to report an acceleration in inflation in August.

UK

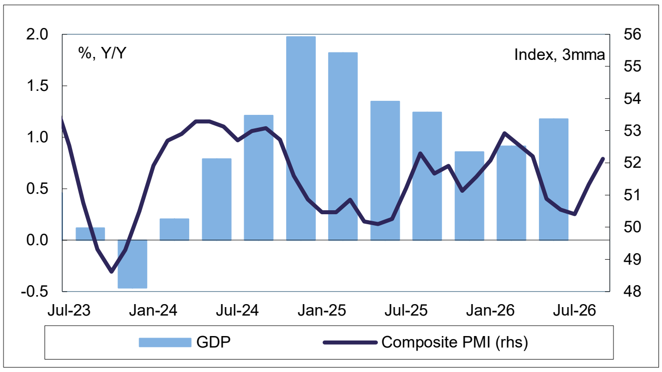
Flash PMIs suggest Burnham bounce proved short-lived for businesses

Like the euro area, the UK economy has appeared resilient to the sustained energy price shock, with GDP growth consistently surprising to the upside since the start of the year. Nevertheless, MPC policymakers have placed greater weight on survey indicators, including the PMIs, that point to softer underlying growth than suggested by the national accounts. And while the official activity figures remain consistent with another solid quarter of expansion in Q3 circa 0.5%Q/Q, supported in part by a positive carryover from Q2 and summer sunshine, today's flash UK PMIs suggested that growth momentum softened at the end of Q3 as inflationary pressures intensified. In particular, the composite output PMI fell 0.8pt in September to a three-month low of 51.7, around half a standard deviation below its long-run average. While the strength in July and August left the quarterly average (52.1) more than 1½pts above the Q2 level, historical relationships suggest that it remained consistent with GDP growth of just 0.1%Q/Q. The moderation in September was broad based, with the services activity (51.7) and manufacturing output indices (51.4) falling to their lowest levels in three and six months respectively. However, the near-term manufacturing outlook remained relatively encouraging. A pickup in new factory orders alongside a further rundown in stocks of finished goods pushed the orders-to-inventory ratio to its highest level in more than two years. Moreover, with the biggest backlogs of work since early 2022, manufacturers continued to expand headcount. In contrast, firms in the more dominant services sector continued to reduce staffing amid concerns of a weaker demand outlook.

Services inflationary pressures intensify, but manufacturing pressures contained

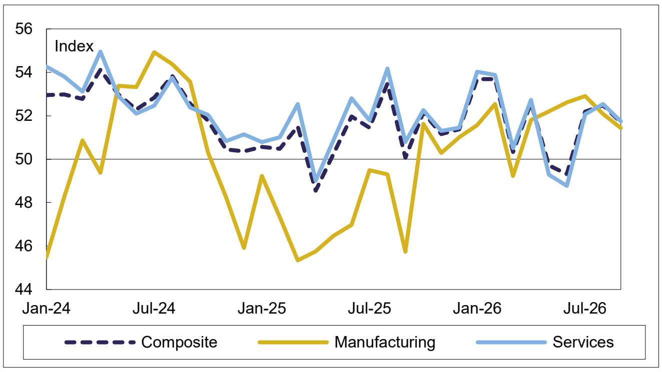
While some policymakers will continue to argue that subdued demand conditions and persisting labour market slack will keep domestic inflation pressures contained, today's PMI price indicators might strengthen the case of the MPC's hawks, who have voted for rate hikes at recent meetings. Reflecting the renewed rise in energy prices, services sector input and output price indices jumped to their highest levels since June and May respectively. And although firms reported that price pressures remained less intense than at the start of the US-Iran conflict, they nevertheless remained well above the average of the past two years. By contrast, cost pressures were reportedly no worse than in August in the manufacturing sector. Whether that will be sufficient to prevent a majority on the MPC from voting to tighten policy again in November remains to be seen. Much will depend on the trajectory of energy prices, and hence geopolitical developments. But there are plenty of other pertinent variables, including the August labour market report, September CPI data, the government's Budget announcement at the end of October and next month's PMIs too.

UK: GDP growth & composite output PMI



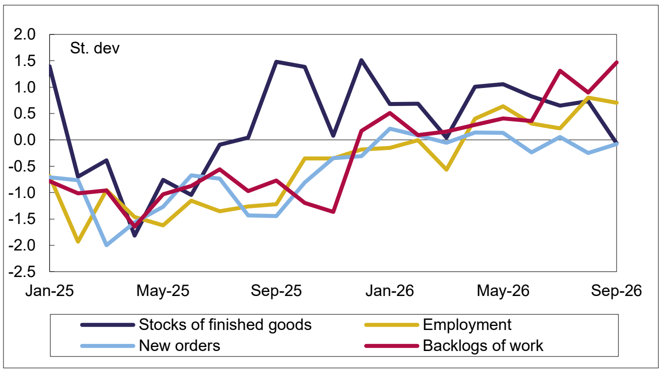
Source: S&P Global, Macrobond and Daiwa Capital Markets Europe Ltd.

UK: Output PMIs



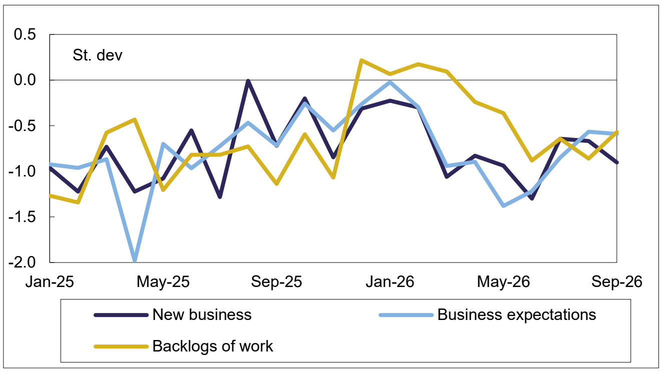
Source: S&P Global, Macrobond and Daiwa Capital Markets Europe Ltd.

UK: Selected manufacturing PMIs



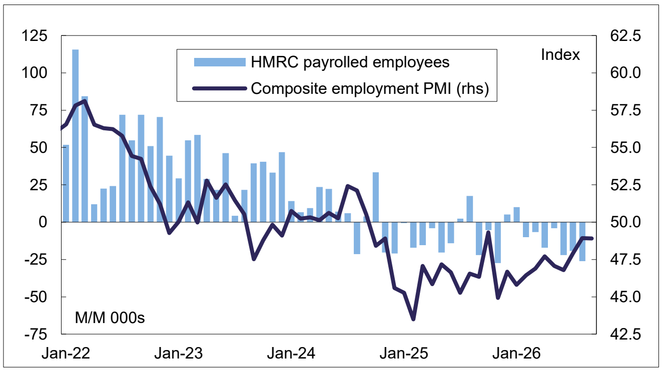
Source: S&P Global, Macrobond and Daiwa Capital Markets Europe Ltd.

UK: Selected services PMIs



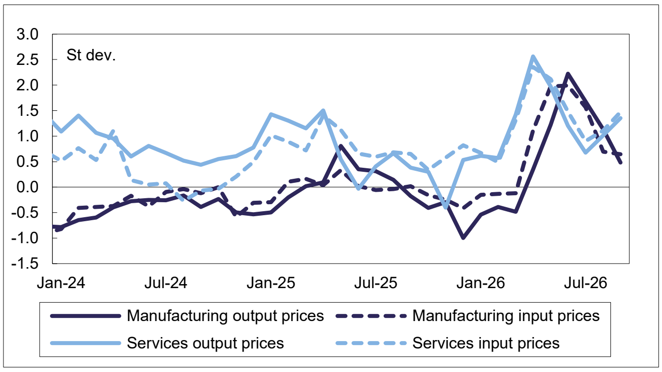
Source: S&P Global, Macrobond and Daiwa Capital Markets Europe Ltd.

UK: Payrolled employees & employment PMI



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

UK: Manufacturing & services price PMIs



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

The day ahead in the UK

Datawise, a retail sector survey from the CBI will provide the sole release of note in the UK on Thursday. But considering that survey's excessive pessimism and poor predictive power for the strength of the official sales series over recent months, it is unlikely to be given too much weight. As a result, the emphasis is likely to be placed on the incoming BoE-speak. Deputy Governor Sarah Breeden and external rate-setter Swati Dhingra are both due to speak at a conference in London, while Deputy Governor Clare Lombardelli might also comment on her outlook for monetary policy while attending a research conference in Poland. Since little time has passed since September's monetary policy meeting and the context provided by each MPC members' individual paragraph last meeting, their comments might be unlikely to affect market expectations for November's monetary policy decision. However, to the extent that Dhingra's stance is more dovish than the median MPC member, those from either Deputy Governor should be more closely watched.

European calendar

Today's results

Economic data

Country	Release	Period	**Actual**	Market consensus/ *Daiwa forecast*	Previous	Revised
Euro area	Preliminary services (manufacturing) PMI	Sep	**53.0 (52.7)**	51.4 (52.6)	51.6 (52.7)	-
	Preliminary composite PMI	Sep	**53.1**	51.7	52.0	-
Germany	Preliminary services (manufacturing) PMI	Sep	**52.9 (53.8)**	49.9 (54.0)	49.7 (54.3)	-
	Preliminary composite PMI	Sep	**53.8**	51.8	51.8	-
France	Preliminary services (manufacturing) PMI	Sep	**51.4 (50.3)**	48.3 (51.0)	48.0 (51.1)	-
	Preliminary composite PMI	Sep	**51.2**	48.7	48.5	-
UK	Preliminary services (manufacturing) PMI	Sep	**51.7 (52.0)**	52.0 (51.5)	52.5 (51.7)	-
	Preliminary composite PMI	Sep	**51.7**	52.0	52.5	-

Auctions

Country	Auction
Germany	sold €870mn of 3.4% 2047 bonds at an average yield of 3.78%
	sold €784mn of 2.9% 2056 bonds at an average yield of 3.80%

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

Tomorrow's releases

Economic data

Country	BST	Release	Period	Market consensus/ *Daiwa forecast*	Previous
Euro area	05.00	New car registrations Y/Y%	Aug	-	12.7
Germany	09.00	ifo business climate indicator	Sep	89.0	88.8
	09.00	ifo current assessment (expectations) indicator	Sep	89.0 (89.3)	88.5 (89.1)
France	07.45	INSEE consumer confidence indicator	Sep	85	86
	07.45	INSEE business (manufacturing) confidence indicator	Sep	98 (102)	98 (103)
	07.45	INSEE production (own-company production) outlook indicator	Sep	-11 (10)	-11 (9)
Spain	08.00	PPI Y/Y%	Aug	-	9.2
UK	11.00	CBI distributive trades survey - reported retail sales % net balance	Sep	-	-48

Auctions and events

Country	BST	Event
Euro area	09.00	ECB to publish Economic Bulletin 6/2026
Italy	10.00	Auction: to sell up to €2.5bn of 3% 2028 bonds
	10.00	Auction: to sell up to €1bn of 1.1% 2031 inflation-linked bonds
	10.00	Auction: to sell up to €1bn of 2% 2037 inflation-linked bonds
UK	10.30	External MPC member Dhingra to speak on a monetary policy outlook panel at the London Macro Policy Forum
	14.30	BoE Deputy Governor Breeden to speak in fireside chat at the London Macro Policy Forum
	15.00	BoE Deputy Governor Lombardelli to deliver a keynote speech at a research conference in Poland

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

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