

# Euro wrap-up

## Overview

- Bunds ended the day little changed despite a moderation in German inflation and a weakening in euro area economic sentiment in August.
- Gilts made modest gains as UK lending figures for July came in below expectations.
- Tomorrow brings the flash estimate of euro area CPI for August, along with unemployment figures for July. In the UK, August business and consumer sentiment indicators are due.

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### Daily bond market movements

Bond	Yield	Change*
BKO 0 09/18	-0.616	+0.008
OBL 0 10/21	-0.517	-0.004
DBR 0 08/26	-0.092	-0.008
UKT 1¼ 07/18	0.153	-0.017
UKT 3¼ 09/21	0.222	-0.018
UKT 1½ 07/26	0.642	-0.026

\*Change from close as at 4.30pm BST.

Source: Bloomberg

## Euro area

### Economic sentiment weakens slightly in August

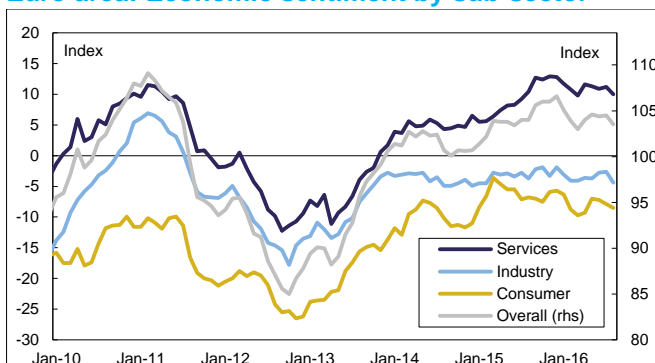
The European Commission's economic sentiment indicators typically provide the most reliable guide to GDP growth in the euro area. And while the latest edition of this survey suggested that economic conditions had become somewhat less favourable in the middle of Q3, they remained consistent with ongoing steady expansion. In particular, the overall euro area economic sentiment indicator (ESI) posted a larger-than-expected fall to 103.5, its lowest level since March, albeit still bang in line with the average of the past two years during which GDP growth has averaged 0.4%Q/Q. The slight deterioration in consumer confidence suggested by the flash estimate was confirmed, taking the index (down 0.6pt to -8.5) to its weakest since April and at the lower end of the range of the past eighteen months. There was a notable weakening in business confidence too, with the respective index falling to its lowest level since October 2013. Manufacturing sector confidence fell on the back of the sharpest reported drop in order books since February 2009, with firms' assessments of export orders the weakest since late 2012. Services sector confidence also slipped back to its long-run average due to lower expectations of future demand, while retailers were notably more downbeat about the present and expected future business situation, with the 2.7pts drop in the headline indicator taking it to its lowest level for a year. In contrast, construction firms continued to assess conditions to be more favourable, with the relevant index rising to its highest for almost eight years. And financial services firms were a touch more upbeat too.

Looking at the country breakdown, the ESI declined in three out of the four largest member states. But the modest increase in the French indicator (+0.9pt) came on the back of two successive monthly declines to leave it only just above its long-run average. Indeed, in the first two months of Q3, the average French ESI was down more than 1pt from the average in Q2, when the French economy flat-lined. Meanwhile, there was a sharp decline in the Italian ESI (-2.1pts) to its lowest level since February 2015 leaving it on average so far in Q3 3pts lower than in Q2, a quarter which was similarly flat for that country's GDP. In addition, there was a further weakening in the equivalent Spanish indicator (-1.5pts) to a 2½-year low suggesting a softening of GDP growth in what has recently been the euro area's fastest growing member state. Meanwhile, the German ESI also slipped back in August (-1.1pts). However, the German indicator was still on average in the first two months of the third quarter almost 1pt higher than in Q2, reinforcing our view that German GDP growth remains on track to be maintained at a rate close to the 0.4%Q/Q of Q2, which should help to support the overall expansion in the euro area at a similar pace to the 0.3%Q/Q recorded last quarter.

### German inflation edges lower

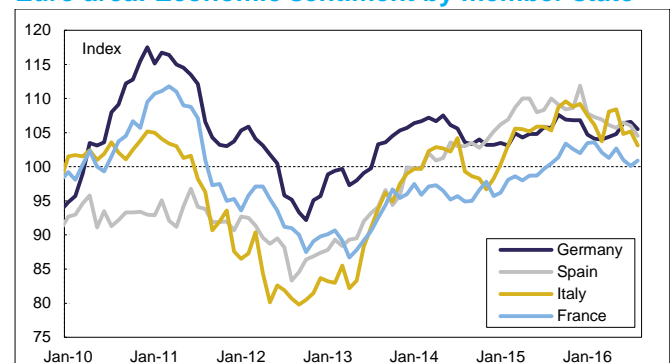
The Commission's survey also suggested that selling price intentions of firms – with the exception of retailers – were lower across the board, while consumer price expectations slipped back slightly for the second successive month, albeit still

### Euro area: Economic sentiment by sub-sector



Source: Thomson Reuters, European Commission and Daiwa Capital Markets Europe Ltd.

### Euro area: Economic sentiment by member state



Source: Thomson Reuters, European Commission and Daiwa Capital Markets Europe Ltd.



remaining above the average over the past year. Today's other data also showed that the flash estimate of German CPI for August came in on the soft side, with the rate on the national measure unchanged at 0.4%Y/Y. The limited detail available with this measure showed that the annual pace of decline in energy prices continued to ease (up 1.1ppt to -5.9%Y/Y), while food and services inflation moderated slightly. And on the EU-harmonised measure, CPI fell 0.1ppt to 0.3%Y/Y. So, while the equivalent flash Spanish inflation figure aligned with expectations, increasing 0.4ppt to -0.3%Y/Y the firmest rate this year, we expect the flash euro area CPI figure, due tomorrow, to be unchanged at 0.2%YY. And we also expect the flash core CPI rate to be unchanged for the third consecutive month at 0.9%Y/Y.

## The day ahead in the euro area and US

As well as the euro area inflation figures, tomorrow brings the equivalent flash CPI estimates from France and Italy, while the latest euro area unemployment figures for July are also due and are expected to show a further modest drop in the unemployment rate to 10.0%, a rate last seen in mid-2011. Wednesday also brings German labour market data for August, along with German retail sales and French consumer spending figures for July. Supply-wise, Germany will sell 2Y bonds, while Portugal will auction 5Y and 10Y bonds.

In the US, ahead of Friday's payrolls report, focus tomorrow will be on the ADP employment report, which is expected to show that payrolls in the private sector increased 175k in August. Wednesday also brings pending home sales figures for July, while current FOMC voting member Rosengren and members Kashkari and Evans (due to become voting members in 2017) are scheduled to speak.

## UK

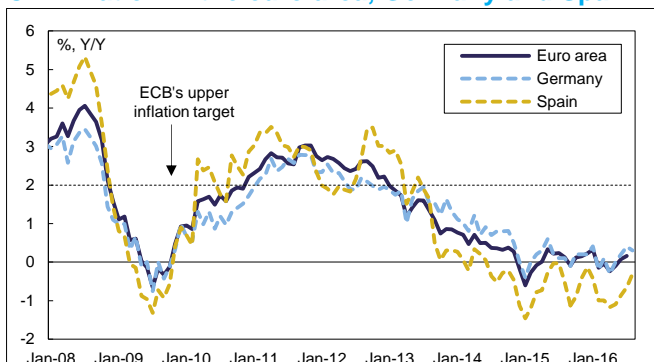
### Lending to household slowed slightly after Brexit

While the initial UK economic surveys published following the Brexit referendum were particularly downbeat, some more recent data releases have been consistent with a rather more optimistic outlook for the UK economy. And although today's BoE lending figures for July came in below expectations, they were not as bad as first impressions might have suggested. For example, excluding April for which the data were distorted due to the Stamp Duty tax change, net new mortgage lending fell to a thirteen-month low. However, the weakness was driven mainly by increased repayments as new gross mortgage lending rose to the highest level since March. And while the number of mortgage approvals for house purchase decreased sharply, this was still at a level similar to those registered in early 2015. Looking at the unsecured lending figures, the story is very similar. Net new unsecured lending fell to a seven-month low but the stock of consumer credit continued to grow at a double-digit percentage annual pace. So, while the figures suggested that, on average, borrowers became a touch more risk averse in managing their balance sheets following the referendum, the overall effect was not out of line with other occasions in the not too distant past. And looking ahead, lower borrowing costs resulting from the BoE's decision to ease monetary policy in early August should provide some support to credit demand in coming months.

### The day ahead in the UK

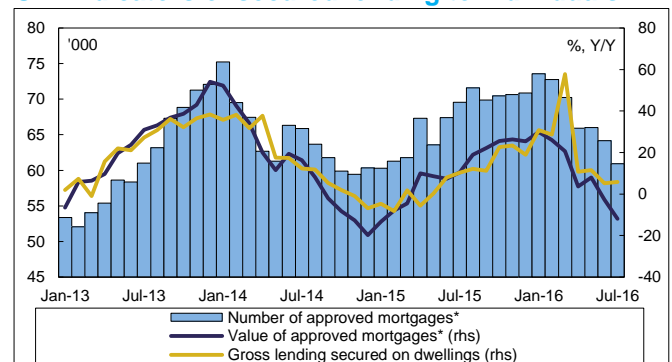
The data focus over the remainder of the week in the UK will be on the latest economic sentiment surveys, with the GfK consumer confidence and Lloyds Business Barometer indicators due tomorrow. The former is expected to have recovered slightly in August, but remain low by the standards of recent years at around -8, following the sharpest month-on-month drop on the series (from -1 to -12) in July. Meanwhile, the Nationwide index is expected to show that in August house price growth eased to back below 5%Y/Y.

### CPI inflation in the euro area, Germany and Spain



Source: Thomson Reuters, ECB and Daiwa Capital Markets Europe Ltd.

### UK: Indicators of secured lending to individuals











\*For house purchase.  
 Source: Thomson Reuters 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
EMU	 Economic sentiment indicator	Aug	<b>103.5</b>	104.1	104.6	<b>104.5</b>
	 Services (industrial) sentiment	Aug	<b>10.0 (-4.4)</b>	11.1 (-2.7)	11.1 (-2.4)	<b>11.2 (-2.6)</b>
	 Final consumer confidence	Aug	<b>-8.5</b>	-8.5	-7.9	-
Germany	 Preliminary EU-harmonised CPI Y/Y%	Aug	<b>0.3</b>	0.5	0.4	-
Italy	 Retail sales M/M% (Y/Y%)	Jun	<b>0.2 (0.8)</b>	-0.2 (0.1)	0.3 (-1.3)	<b>- (-1.5)</b>
Spain	 Preliminary EU-harmonised CPI Y/Y%	Aug	<b>-0.3</b>	-0.3	-0.7	-
UK	 Mortgage approvals `000s	Jul	<b>60.9</b>	61.9	64.8	<b>64.2</b>
	 Net consumer credit (net lending secured on dwellings) £bn	Jul	<b>1.2 (2.7)</b>	1.7 (3.1)	1.8 (3.3)	<b>1.9 (3.2)</b>




#### Auctions

Country	Auction
Italy sold	 €3bn of 0.45% 2021 bonds (01-Jun-2021) at an average yield of 0.19%
	 €1.75bn of 2023 floating-rate bonds (15-Jul-2023) at an average yield of 0.32%
	 €2.9bn of 1.25% 2026 bonds (01-Dec-2026) at an average yield of 1.14%
UK	 BoE APF operation: £1.17bn of 15Y+ Gilts purchased (2.08 cover ratio)

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

### Yesterday's results

#### Economic data

Country	Release	Period	Actual	Market consensus/ <i>Daiwa forecast</i>	Previous	Revised
EMU	 ECB QE net purchases €bn	Weekly	<b>10.3</b>	<u>12.6</u>	11.9	-
Italy	 Consumer confidence indicator	Aug	<b>109.2</b>	110.3	111.3	<b>111.2</b>
	 Manufacturing (economic) confidence	Aug	<b>101.1 (99.4)</b>	102.5 (-)	103.1 (103.3)	<b>102.9 (103.0)</b>














#### Auctions

Country	Auction
	- Nothing to report -



Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

## Tomorrow's data releases

### Economic data

Country	BST	Release	Period	Market consensus/ <i>Daiwa forecast</i>	Previous	
EMU		10.00	Unemployment rate %	Jul	10.0	10.1
		10.00	Flash CPI estimate Y/Y%	Aug	<u>0.2</u>	0.2
		10.00	Flash core CPI estimate Y/Y%	Aug	<u>0.9</u>	0.9
Germany		07.00	Retail sales M/M% (Y/Y%)	Jul	0.5 (0.3)	-0.1 (2.7)
		08:55	Unemployment change `000s (rate %)	Jul	-4 (6.1)	- (6.1)
France		07:45	Preliminary EU-harmonised CPI Y/Y%	Aug	0.4	0.4
		07:45	Consumer spending M/M% (Y/Y%)	Jul	0.3 (1.1)	-0.8 (0.6)
Italy		09:00	Unemployment rate %	Jul	11.6	11.6
		10:00	Preliminary EU-harmonised CPI Y/Y%	Aug	-0.1	-0.2
Spain		09:00	Current account balance €bn	Jun	-	2.8
UK		00:01	Lloyds business barometer	Aug	-	29
		00:01	GfK consumer confidence survey	Aug	-8	-12
		07.00	Nationwide house price index M/M% (Y/Y%)	Aug	-0.2 (4.8)	0.5 (5.2)

### Auctions and events

Country	BST	Auction / Event
Germany		11:30 Auction: To sell €4bn of 2018 zero-coupon bonds (14-Sept-2018)
UK		14.50 BoE APF operation: To purchase £1.17bn of 7-15Y Gilts

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

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