

Euro wrap-up

Overview

- Bunds made modest losses on a quiet day for euro area economic news.
- Gilts were little changed as public finance figures showed that UK public borrowing is not falling as quickly as previously expected.
- Tomorrow brings the latest consumer confidence survey in the euro area and the CBI Industrial Trends survey in the UK.

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Daily bond market movements

Bond	Yield	Change*
BKO 0 09/18	-0.609	-0.003
OBL 0 10/21	-0.501	+0.010
DBR 0 08/26	0.006	+0.024
UKT 1¼ 07/18	0.110	+0.001
UKT 3¼ 09/21	0.249	-0.002
UKT 1½ 07/26	0.810	+0.002

*Change from close as at 4.30pm BST.

Source: Bloomberg

UK

Against weaker economic backdrop more public borrowing is expected

The UK's public finances are not evolving as the OBR expected at a time of the FY16/17 budget in March. While the latest data released today showed that public sector net borrowing in August was £10.5bn, about £1bn lower compared to the same month last year, this still left cumulative net borrowing over the first five months of this financial year only 12.7% (£4.9bn) lower compared to the equivalent period in FY15/16. This is well short of the OBR's expectation for a 27.5% fall for FY16/17 as a whole.

There are reasons to believe that the pace of recovery in receipts will accelerate towards the end of the fiscal year as the government collects self-assessment income tax. But the OBR's forecast was made before the EU referendum and therefore does not incorporate the slowdown in the economy in the wake of the Brexit vote. While the immediate effect on economic growth may prove to have been smaller than previously feared, in part thanks to the BoE's swift easing in policy, what data are available so far suggest that growth has slowed appreciably. So the impact of slower growth on the public purse should still accumulate over the remainder of this year, nudging the trajectory for public sector borrowing up meaningfully. As a rule of thumb the OBR's calculations suggest that a one percentage point reduction in GDP growth raises public sector net borrowing by about ½% of GDP.

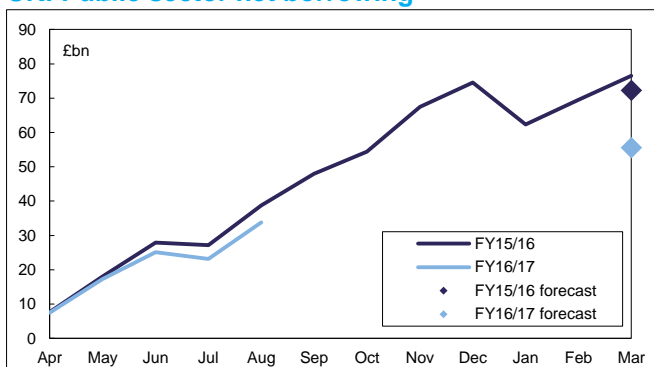
The current government is well aware of this, of course, and Theresa May was quick to abandon the previous government's target to balance the books by the end of this Parliament. However, balancing the budget, albeit at a later (unspecified) date, remains the government's objective. So the Autumn Statement on 23 November, the first one for the new Chancellor Philip Hammond, is not set to provide a complete turnaround in policy, still prioritising long-term fiscal prudence over a short-term economic boost.

Overall, we would expect the new OBR forecasts in November to show an increase in borrowing as a percentage of GDP in FY19/20 of about 2ppts compared with the previous forecast to about 1½% of GDP. Most of this additional borrowing will be accounted for by worse economic fundamentals, while it would still represent a tightening in fiscal policy between now and then, albeit by less than anticipated before the referendum.

The day ahead in the UK

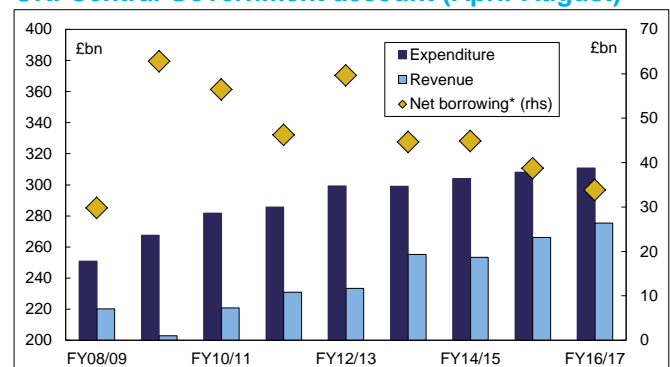
The CBI Industrial Trends Survey, which was relatively upbeat about the performance of the manufacturing sector after the Brexit vote, is the only release of note in the UK tomorrow. Its total orders indicator is expected to have moved sideways in September, while the price index will probably continue to signal that inflationary pressures continue to rise. On the policy front, the BoE Governor Mark Carney and external MPC member Kristin Forbes are scheduled to speak.

UK: Public sector net borrowing



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

UK: Central Government account (April-August)



*Total public sector.

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






Euro area

The day ahead in the euro area and US









After a quiet few days for euro area economic news, tomorrow brings the first of the week's top-tier releases with most notable the Commission's flash consumer confidence indicator for September. This is expected to report a modest improvement in the headline index at the end of Q3 having declined to a four-month low of -8.5 in August to leave the quarterly average almost ½pt lower than the -7.8 rate recorded in Q2. Thursday also brings the French INSEE business sentiment survey for September, as well as the ECB's latest Economic Bulletin.

In the US, the flow of housing market indicators continues tomorrow with August existing home sales figures and July's FHFA home price index. The usual weekly jobless claims numbers and the Chicago and Kansas Fed national activity indices are also due for release. Supply-wise, the Treasury will sell 10Y TIPS.

European calendar

Today's results							
Economic data							
Country	Release	Period	Actual	Market consensus/ <i>Daiwa forecast</i>	Previous	Revised	
UK 	Public sector net borrowing excluding interventions £bn	Aug	10.5	10.2	-1.0	-1.9	
Auctions							
Country	Auction						
Germany sold 	€4bn of 2021 zero-coupon bonds (08-Oct-2021) at an average yield of -0.51%						
UK 	BoE APF operation: £1.17bn 7-15Y Gilts purchased (2.96 cover ratio)						

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 	15:00	Preliminary consumer confidence	Sep	-8.2	-8.5		
France 	07:45	Business confidence indicator (production outlook)	Sep	101 (0)	101 (0)		
Spain 	09:00	Trade balance €bn	Jul	-	-1.4		
UK 	11:00	CBI Industrial Trends survey, total orders	Sep	-5	-5		
Auctions and events							
Country	BST	Auction / Event					
EMU 	09:00	ECB publishes Economic Bulletin					
EMU 	14:00	ECB's Draghi scheduled to speak at ERSB conference in Frankfurt					
UK 	13:00	BoE's Forbes scheduled to speak in London					
UK 	18:00	BoE's Carney scheduled to speak in Berlin					



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
- Nothing to report -						

Auctions

Country	Auction
UK sold	 £2.5bn of 1.5% 2047 bonds (22-Jul-2047) at an average yield of 1.529%  BoE APF operation: £1.17bn of 7-15Y Gilts purchased (2.72 cover ratio)

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

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