

# Euro wrap-up

## Overview

- Bunds made losses today as German exports and Italian IP data significantly exceeded expectations and the oil price continued its upward trend to reach its highest level in a year.
- Gilts similarly lost ground despite a UK sentiment survey highlighting the downside risks to near-term economic activity resulting from Brexit.
- Tomorrow brings surveys of German investors and UK retailers.

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### Daily bond market movements

Bond	Yield	Change*
BKO 0 09/18	-0.661	+0.004
OBL 0 10/21	-0.477	+0.017
DBR 0 08/26	0.060	+0.041
UKT 1¼ 07/18	0.214	+0.037
UKT 3¾ 09/21	0.411	+0.054
UKT 1½ 07/26	1.025	+0.054

\*Change from close as at 4.30pm BST.  
 Source: Bloomberg

## Euro area

### ECB likely to maintain asset purchases at current rate beyond March

Following the recent Bloomberg report mooted a possible consensus at the ECB about the need to taper its asset purchases once the time comes to bring the programme to an end, the account of September's Governing Council meeting published last week saw policymakers acknowledge for the first time the scarcity of bonds available to purchase. But while they conceded that market developments have raised implementation challenges for conducting their asset purchases, over the weekend ECB President Draghi and Vice President Constâncio offered little clarity about the future direction of policy, including as regards to the QE programme. Nevertheless, they continued to acknowledge that the envisaged return of inflation closer to target over the next few years – the ECB currently expects headline CPI to rise to average 1.6%Y/Y in 2018 – is very much dependent on maintaining significant policy accommodation over that period. And with Constâncio reiterating the ECB's commitment to maintain the present set of policies, particularly the QE component, until it attains "a sustained path towards the inflation objective", we still expect the ECB eventually to extend its asset purchases beyond March 2017 at the current monthly pace of €80bn.

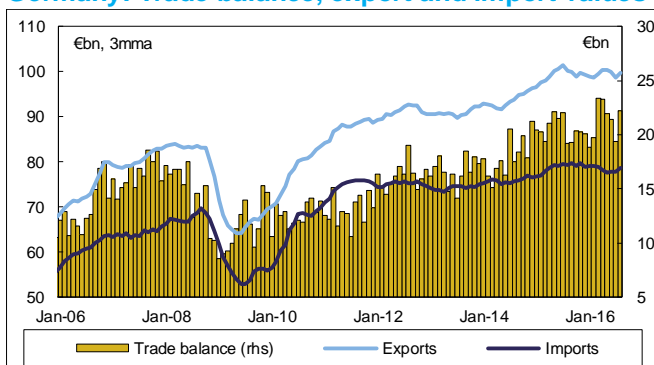
### German exports surge in August

While there will probably be little data-wise this week that will have a material impact on the debate of the ECB Governing Council at its monetary policy meeting next week, today's Germany trade report for August tallied with the strong industrial production figures released last week to show a very vigorous rebound in exports. In particular, the value of exports jumped almost 5½%M/M in August, the strongest monthly increase since 2010, to leave it 5% higher compared with a year earlier. Imports were strong too, up 3%M/M and more than 2%Y/Y, the first year-on-year rise since February. Meanwhile, on an adjusted basis, the trade surplus remained huge, rising to a four-month high of €22.2bn. However, the jump in exports in the latest month followed a drop in excess of 2½%M/M in July, and so the average for the first two months of Q3 was still down 0.3% compared with Q2, while the value of imports was up almost 1½% on the same basis. So, the risk remains that net trade was a drag on growth in Q3 for the first quarter in three.

### Italian IP stronger than expected in middle of Q3

Consistent with data out of Germany, France and Spain last week, Italian industrial production figures for August, released today, significantly beat expectations, rising 1.7%M/M, the strongest monthly increase since January's nineteen-month high, to leave output more than 4% higher compared with a year earlier. The improvement principally reflected a rise of more than 2%M/M in manufacturing production, the most in 5½ years, to leave output in the sector up more than 6%Y/Y. Encouragingly,

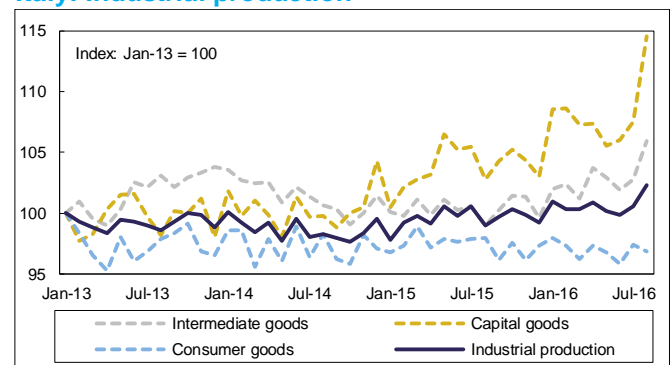
### Germany: Trade balance, export and import values\*



\*Goods trade report.

Source: Thomson Reuters and Daiwa Capital Markets Europe Ltd.

### Italy: Industrial production



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



production of capital goods increased 6½%M/M to its highest level for five years, while production of intermediate goods rose to its highest since early 2012. While we might well see some payback over coming months, on average in the first two months of Q3 manufacturing output was 1.8% higher than in Q2 while total IP was a little more than 1% higher on the same basis. And as a result, when aggregate euro area production figures are published on Wednesday, we now expect overall IP to have risen almost 2%M/M, the most since January. Elsewhere, the September Bank of France business survey pointed to a stronger showing from the services sector at the end of Q3, with the respective activity index up to the highest in five months, while the manufacturing sector saw continued 'slight expansion' in output. Both sectors anticipate improvement in October. And based on the survey results, the Bank forecasts French GDP growth in Q3 of 0.3%Q/Q, following a contraction of 0.1%Q/Q in Q2. We think growth might have fallen just a touch short of that rate, forecasting GDP growth of 0.2%Q/Q.

## The day ahead in the euro area and US

Tomorrow brings the first of October's sentiment indicators with the German ZEW survey of financial market participants. The current conditions balance is expected to remain little changed at the start of Q4, while investors' assessment of the outlook is forecast to have improved somewhat. However, survey participants' confidence might well have been impacted over the past week or so by the increased likelihood of a 'hard' Brexit and the subsequent further drop in sterling. Supply-wise, Germany will sell 30Y index-linked bonds, the Netherlands will auction 10Y bonds and Austria will sell 10Y and 30Y bonds. In the US, it should be another relatively quiet day for top-tier economic data with just the Fed's labour market conditions index due for release. Meanwhile, non-voting FOMC members Evans and Kashkari are due to speak.

## UK

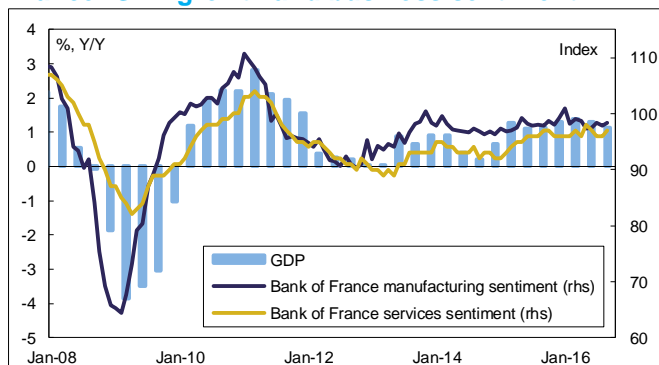
### BCC survey points to weaker growth ahead

The BCC's quarterly economic survey, released today, suggested that GDP growth slowed significantly in Q3 and continued to highlight the uncertainties ahead for the UK economy. In particular, it suggested that while conditions in the manufacturing sector had held up relatively well after June's referendum, with some firms in the sector benefiting from a weaker currency, firms in the services sector were on the whole more downbeat and reported a fall in the pace of domestic and foreign sales growth. And similar to the recent results of the BoE Agents' scores, the survey also emphasised that increased uncertainty had led businesses to lower their expectations for hiring, turnover, and investment, underscoring the downside risks to the longer-term economic outlook. This survey, therefore, was in line with other survey data covering the Q3 period and, when the first estimate of Q3 GDP is released on 27 October, we expect it to show that growth slowed to 0.3%Q/Q from 0.7% in Q2.

### The day ahead in the UK

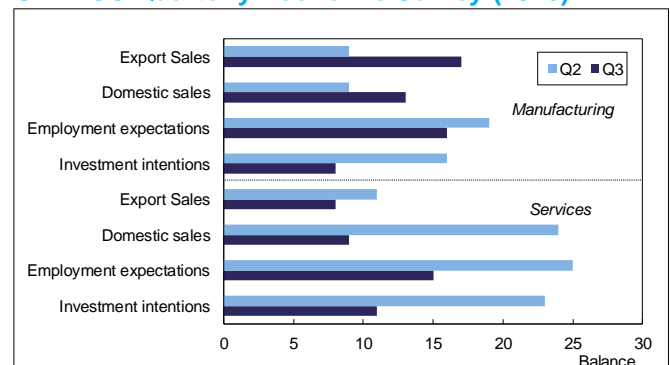
The flow of new economic data tomorrow brings the BRC/KPMG Retail Sales Monitor for September. On the policy front, Michael Saunders, the most recently appointed MPC member, is scheduled to testify before the Treasury Select Committee. In his first speech as an MPC member Saunders recently said that compared to the latest BoE projections he is less pessimistic about the UK economic outlook over the coming years. However, he also assessed that there is more slack in the labour market, suggesting that he is unconcerned about the potential for increased underlying inflation pressure from faster wages growth.

### France: GDP growth and business sentiment\*








\*Q3 GDP growth represents Bank of France surveys.  
 Source: Bank of France, Thomson Reuters and Daiwa Capital Markets Europe Ltd.

### UK: BCC Quarterly Economic Survey (2016)








Source: BCC

## European calendar

Today's results							
Economic data							
Country		Release	Period	Actual	Market consensus/ <i>Daiwa forecast</i>	Previous	Revised
EMU		ECB public sector asset purchases €bn	Weekly	18.1	14.0	11.5	-
Germany		Trade balance €bn	Aug	20.0	19.5	19.5	-
		Current account balance €bn	Aug	17.9	15.0	18.6	20.2
		Imports (exports) M/M%	Aug	3.0 (5.4)	0.7 (2.2)	-0.7 (-2.6)	-
France		Bank of France manufacturing sentiment indicator	Sep	98	99	98	-
Italy		Industrial production M/M% (Y/Y%)	Aug	1.7 (4.1)	-0.1 (-0.3)	0.4 (-0.3)	0.7 (-)
Auctions							
Country		Auction					
UK		BoE APF operation purchased £1.17bn of 3-7Y Gilts (4.11 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		10:00 ZEW expectations balance	Oct	-	5.4		
Germany		10:00 ZEW current assessment balance (expectations)	Oct	55.5 (4.0)	55.1 (0.5)		
UK		00:01 BRC Retail Sales Monitor, like-for-like sales Y/Y%	Sep	-0.3	-0.9		
Auctions and events							
Country	BST	Auction / Event					
Germany		10:30 Auction: To sell €500mn of 0.1% 2046 index-linked bonds (15-Apr-2046)					
UK		10:00 BoE's Saunders scheduled to speak at a hearing of Parliament's Treasury Select Committee					
		14:50 BoE APF operation: To purchase 15Y+ Gilts					

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

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