

Euro wrap-up

Overview

- Ahead of the outcome of the US Presidential election, Bunds made modest losses today despite some weaker German IP and trade data.
- Gilts ended the day slightly lower too as UK manufacturing output was slightly stronger than expected at the end of Q3.
- The European data focus tomorrow will be the UK's trade report for September, while the Bank of France sentiment survey is also due.

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Daily bond market movements

Bond	Yield	Change*
BKO 0 09/18	-0.630	+0.004
OBL 0 10/21	-0.404	+0.015
DBR 0 08/26	0.181	+0.027
UKT 1¼ 07/18	0.223	+0.022
UKT 3¼ 09/21	0.578	+0.029
UKT 1½ 07/26	1.238	+0.035

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

Euro area

Weaker German IP reflects payback for previous strength

After exceptionally strong output growth in August but a weak showing for German factory orders in September, a soft German IP report that month had looked likely. However, a near-2% monthly drop in output was much steeper than expected at the end of Q3 and left it up just 1.2% compared with a year earlier. And today's report showed that the weakness was broad based, with, for example, manufacturing output down 1.7%M/M, due to a near-2½%M/M drop in production of capital goods and more than 7%M/M decline in production of consumer durable goods, the latter being the steepest for more than five years. Meanwhile, energy output was down more than 3%M/M and construction output fell 1½%M/M. So, when excluding construction, the measure that corresponds with euro area IP, German industrial output fell 1.9%M/M, the steepest drop since August 2014. Admittedly, this came on the back of an upwardly revised increase of 3.4%M/M in August, which itself was the strongest for almost seven years. As such, over the third quarter as a whole, output just about posted a modest increase (0.2%Q/Q) following a decline of ½%Q/Q in Q216. And looking ahead, recent business sentiment surveys suggest that conditions in the sector have improved more significantly at the start of the fourth quarter.

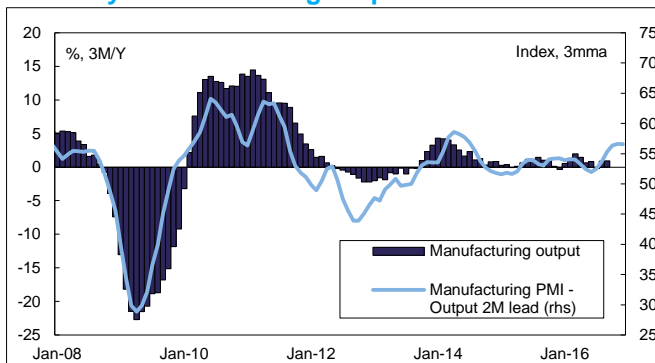
German and French exports decline at the end of Q3

Consistent with weaker production that month, German trade figures for September also reported a drop in the value of exports, by 0.7%M/M, to leave them up less than 1% compared with a year earlier. But given the decline in the value of imports that month, by 0.5%M/M, the adjusted trade surplus was little changed at €21.3bn, albeit leaving the surplus over the third quarter a touch lower than in Q216. While exports were broadly flat in Q3, they were outpaced by import growth of 1.4%Q/Q, the strongest quarterly rate since Q215. So, while German GDP growth in Q3 is set to have remained relatively firm at a similar pace to the 0.4%Q/Q rate seen in Q2, the contribution from net trade seems set to have been negative. Today's French trade figures for September, which showed the deficit widening €0.5bn to €4.8bn, a five-month high, also suggested that manufacturing output from that country (data due Thursday) looks likely to be weaker at the end of Q3. Indeed, the value of exports fell more than 2%M/M in September, with notable weakness in shipments to the UK and Italy. But, having risen a cumulative 2½% in July and August, exports were up more than ½%Q/Q over the third quarter as a whole. Despite declining in September, the value of imports was up 2½%Q/Q. So, as suggested by the first estimate of French GDP, net trade provided a notable drag on GDP growth in Q3 for the fourth quarter out of the past five.

The day ahead in the euro area and US

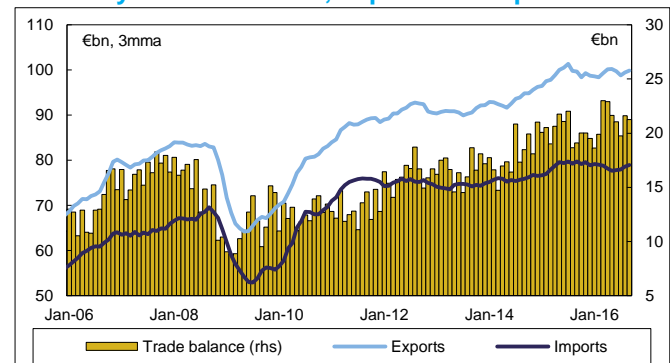
It should be a relatively quiet day for euro area economic news tomorrow, with just the Bank of France's latest business sentiment survey for October due for release. Meanwhile, ECB Executive Board members Praet and Cœuré are due to speak, and Germany will sell 2Y Bunds.

Germany: Manufacturing output and PMI



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

Germany: Trade balance, export and import values



Source: Thomson Reuters and Daiwa Capital Markets Europe Ltd.



In the US, with just wholesale trade figures due for release markets seem bound to take their direction from the outcome of today's Presidential election. Elsewhere, the Fed's Kashkari is due to speak, while the Treasury will sell 10Y Notes.

UK

Manufacturing growth started to recover

While UK economic surveys suggested that manufacturing sentiment recovered sharply following the marked decline in July following the referendum in June, thanks to strong demand from abroad associated not least with weaker sterling, hard economic indicators from that sector remained subdued, with output growing just 0.2%M/M in August. However, today's release for September showed that momentum continued to build towards the end of Q3, with manufacturing output up 0.6%M/M, the second highest pace since the end of 2014. Among the major subsectors, food products, pharmaceuticals and rubber and plastic products provided the largest positive contributions to the monthly increase, while transport equipment was a drag on growth. Notwithstanding the increase in September, production over the third quarter as a whole was weak, with today's figures suggesting that manufacturing output was down 0.9%Q/Q, compared with a drop of 1%Q/Q assumed in the first estimate of Q3 GDP. But given the notable decline in mining output in September (3.8%M/M), overall industrial production was weaker than expected, falling by 0.4%M/M for the second consecutive month. And this implies a fall of 0.5%Q/Q over the third quarter as a whole, compared with a decline of 0.4%Q/Q estimated in the preliminary Q3 GDP release.

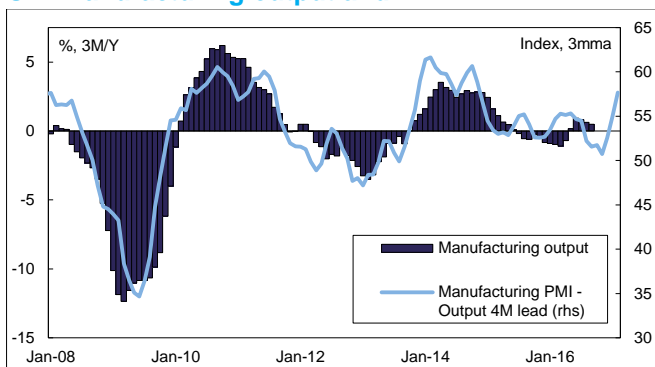
Consumer spending set to remain firm at the start of Q4

Of course, any downward revisions to GDP growth (0.5%Q/Q) in Q3 seem likely to depend on services activity. In this respect, while the monthly retail sales figures were softer than expected in September, they continued to post a significant increase over the quarter as a whole (growth of 1.8%Q/Q was bang in line with the first reading of Q3 GDP). And looking ahead, today's BRC survey suggested that the retail sector maintained its positive momentum at the start of Q4, with total sales and same store sales up by 2.4%Y/Y and 1.7%Y/Y respectively in October, the fastest pace since the start of the year. Looking through the monthly volatility, supported by a pick-up in non-food sales, three-month growth was up by 0.1ppt to 1.1%3M/Y, a pace last seen in July. So while retailers are reporting that they are increasing prices on the back of the weaker currency, the survey suggested that consumer spending is likely to remain firm and should continue to support GDP growth in Q4.

The day ahead in the UK

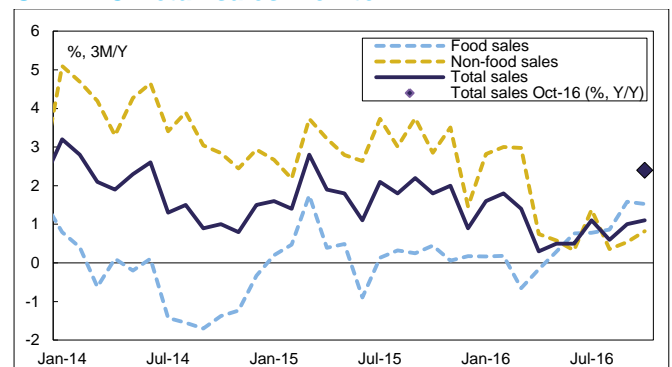
The latest UK trade figures, due tomorrow, are expected to show that the trade deficit fell in September as stronger manufacturing output growth and weaker sterling provided a boost to exports.

UK: Manufacturing output and PMI
















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

UK: BRC Retail sales monitor












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
Germany	 Industrial production M/M% (Y/Y%)	Sep	-1.8 (1.2)	-0.5 (2.0)	2.5 (1.9)	3.0 (2.4)
	 Trade balance €bn	Sep	24.4	22.4	20.0	19.9
	 Current account balance €bn	Sep	24.2	24.5	17.9	17.4
	 Imports (exports) M/M%	Sep	-0.5 (-0.7)	-0.2 (-0.8)	1.9 (3.4)	-
France	 Trade balance €bn	Sep	-4.8	-4.2	-4.3	-4.2
	 Current account balance €bn	Sep	-3.4	-	-2.1	-2.5
UK	 BRC Sales like-for-like Y/Y%	Oct	1.7	0.6	0.4	-
	 Industrial production M/M% (Y/Y%)	Sep	-0.4 (0.3)	0.0 (0.8)	-0.4 (0.7)	-
	 Manufacturing production M/M% (Y/Y%)	Sep	0.6 (0.2)	0.4 (-0.1)	0.2 (0.5)	-
	 NIESR GDP 3M/3M%	Oct	0.4	-	0.4	0.5
Country	Auction					
Germany sold	 €407mn of 0.1% 2026 index-linked bonds (15-Apr-2026) at an average yield of -0.94%					
UK sold	 £2.5bn of 1.75% 2037 bonds (07-Sep-2037) at an average yield of 1.811%					
	 BoE APF operation purchased £1.05bn of 15Y+ Gilts (2.74 cover ratio)					

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

Tomorrow's data releases						
Economic data						
Country	GMT	Release	Period	Market consensus/ <i>Daiwa forecast</i>	Previous	
France	 07:30	Bank of France manufacturing sentiment indicator	Oct	99	98	
UK	 09:30	Visible trade balance £bn	Sep	-11.4	-12.1	
	 09:30	Total trade balance £bn	Sep	-4.0	-4.7	
Auctions and events						
Country	GMT	Auction / Event				
EMU	 -	ECB's Praet and Nouy scheduled to speak in Brussels				
	 16:45	ECB's Cœuré scheduled to speak in Lyon				
Germany	 10:30	Auction: To sell €5bn of 2018 bonds (14-Dec-2018)				
UK	 09:30	BoE publishes Agents' Summary of Business Conditions				
	 14:50	BoE APF operation: To purchase 7-15Y Gilts				
	 18:00	BoE's Haldane scheduled to speak in London				

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

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