

# Euro wrap-up

## Overview

- Bunds followed USTs very slightly higher today as German Q3 GDP fell short of expectations, while euro area GDP growth was unchanged at 0.3%Q/Q.
- Gilts also made gains as UK consumer price inflation unexpectedly slipped back at the start of Q4.
- The data focus in Europe tomorrow will be UK labour market figures for September.

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### Daily bond market movements

Bond	Yield	Change*
BKO 0 12/18	-0.622	-0.008
OBL 0 10/21	-0.331	-0.002
DBR 0 08/26	0.311	-0.008
UKT 1¼ 07/18	0.210	-0.002
UKT 3¾ 09/21	0.654	-0.012
UKT 1½ 07/26	1.388	-0.018

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

## Euro area

### Euro area GDP confirmed at 0.3%Q/Q in Q3

Today's second release of euro area GDP data for Q3 saw growth confirmed at 0.3%Q/Q, broadly in line with the average of the recovery so far to leave output up 1.6% compared with a year earlier. But to two decimal places today's release suggests that growth was within a whisker of being upwardly revised with growth of 0.349%, and compared with 0.295% in Q2. While there is still no detailed breakdown, the national data suggest that household and government consumption supported growth, while net trade provided a negative contribution for the first quarter in three. And this would be broadly consistent with the latest monthly trade data, which today showed that despite an improvement in the surplus in September to €24.9bn, it was still down more than €1bn over the third quarter as a whole at €23bn. Indeed, while the value of exports were up in the third quarter by 0.7%Q/Q, the value of imports, despite a marked decline in September, were up by 1.6%Q/Q, the firmest quarterly increase since Q215.

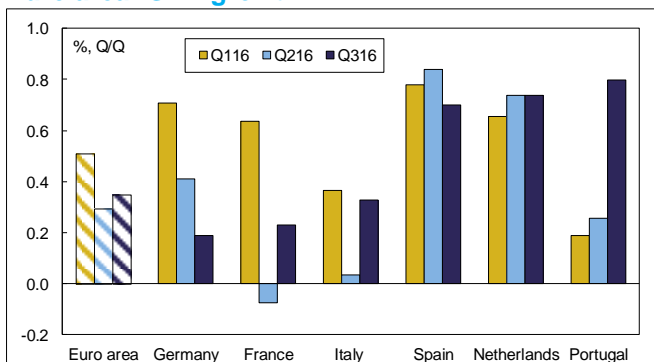
### Mixed performance among member states

Among member states, there was a downward surprise to the preliminary release of German GDP, with growth moderating more than expected in Q3 to a four-quarter low of 0.2%Q/Q, half the rate in Q2 and down from 0.7%Q/Q in Q1. The weakness was principally due to net trade, while private and government consumption continued to provide support. The first estimate of Italian GDP, meanwhile, came in a touch stronger than expected, with growth returning to positive territory at 0.3%Q/Q from a flat second quarter, admittedly principally reflecting a large positive contribution from stock accumulation, while net trade was a drag on growth. And this was broadly consistent with the initial GDP figures from France, released a few weeks ago, which suggested that the 0.2%Q/Q growth was more than fully accounted for by private inventories. So Spain's growth of 0.7%Q/Q means that it remained the fastest growing of the larger member states, although the Netherlands' economy performed much better than expected, also recording growth of 0.7%Q/Q for the third consecutive quarter. And there was an acceleration too in growth in Portugal and Greece in the third quarter, up 0.5ppt to 0.8%Q/Q and 0.2ppt to 0.5%Q/Q respectively, with the former the firmest since Q413.

### German ZEW survey provides mixed messages

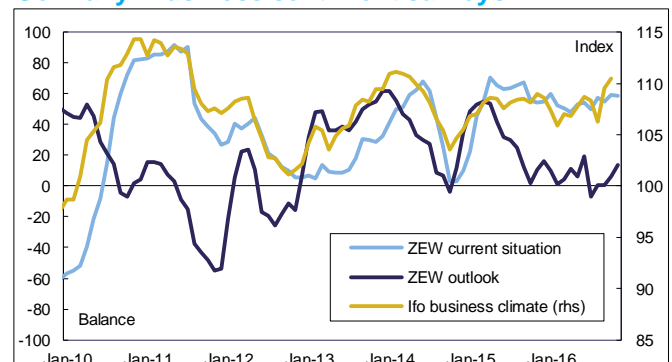
Recent sentiment surveys from the euro area have, on balance, signalled a modest improvement in economic conditions at the start of Q4, with indicators from Germany in particular suggesting that conditions were much more favourable. For example, the Ifo's business climate indicator rose to a two-and-a-half-year high in October, the composite PMI jumped to a ten-month high that month, while the ZEW's current situation index was at its highest since the start of the year. However, today's ZEW survey of investors signalled a modest loss of confidence in November, with the survey's current conditions

### Euro area: GDP growth



Source: Thomson Reuters and Daiwa Capital Markets Europe Ltd.

### Germany: Business sentiment surveys



Source: Thomson Reuters and Daiwa Capital Markets Europe Ltd.



index down 0.7pt on the month to 58.8. But this still left the index on average so far in Q4 5pts higher than the average in Q3, while the expectations balance increased by a stronger-than-expected 7.6pts on the month to 13.8 – while still notably lower than the pre-UK referendum peak, that was well above the average of the past twelve months. And so we continue to expect the economic expansion in the euro area's largest member state to have accelerated in the final quarter of the year, helping to maintain overall euro area GDP growth close to or above recent rates.

## The day ahead in the euro area and US

It should be a relatively quiet day for euro area economic news tomorrow with no data due for release, while the Commission is due to publish its overall assessment of the euro area government's draft budgetary plans for 2017. In the US, meanwhile, tomorrow brings October's industrial production data – expected to report a further modest rise in output at the start of Q4 – PPI figures for the same month, capital flows figures for September and the NAHB housing market index for November. In addition, Fed Governors Bullard, Kashkari and Harker are due to speak.

## UK

### Inflation surprises on the downside

The September CPI figures last month showed that the headline rate jumped by 0.4ppt to 1.0%Y/Y, fuelling expectations that, against the backdrop of the sharp depreciation in sterling, UK inflation was set to rise particularly rapidly over coming months. But instead of continuing along the upward trend as many expected, inflation eased by 0.1ppt in October, to 0.9%Y/Y. With oil prices having risen notably that month to leave the energy CPI rate positive for the first time in two years, the weakness reflected core inflation. Indeed, having risen to 1.5%Y/Y in September, a level unseen for six months, it slipped back to 1.2%Y/Y in October as a result of lower inflation in both major categories - services and goods. The former dropped from 2.6%Y/Y to 2.4%Y/Y, the lowest level since the start of the year, while the latter saw the pace of decline steepen by 0.3ppt to -0.6%Y/Y. But while the fall in sterling has not fed through to higher goods inflation yet, a taste of what is potentially to come was provided by the producer price indicators, where input PPI accelerated further to 12.2%Y/Y, the highest rate in five years and up almost 13ppts since the referendum. Of course, service-sector firms, as today's drop in services CPI demonstrated, can try and put a lid on price increases. But to do so firms are going to have to find efficiencies. These are likely to come primarily through cutting both staffing and labour compensation costs, which would erode real income growth further.

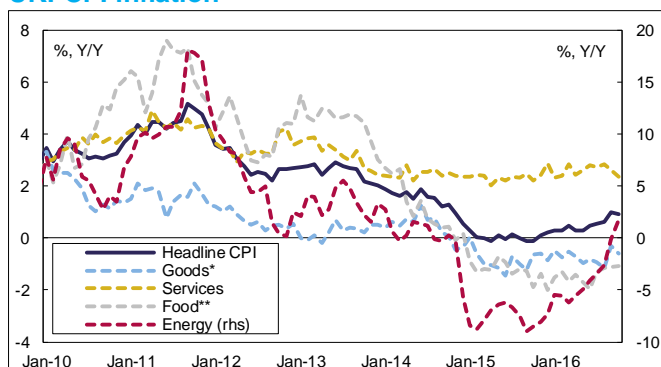
### House prices continued to rise in September

Meanwhile, the ONS House Price Index, released alongside the inflation data today, showed that house price growth remained firm in September, with the headline rate moving sideways at a downwardly revised 7.7%Y/Y. However, the level of prices continued rising, albeit the increase of 0.2%M/M was the lowest since February and significantly lower than the average over the first half of 2016. Within the detail, all major regions of the country saw house price growth remaining positive, with the east of England and London both seeing double-digit increases. Looking ahead, stretched affordability ratios and heightened uncertainty is likely to bring house price growth down in some areas, but with mortgage rates continuing to fall and the jobs market showing no significant signs of weakness, the tone of the UK housing market is set to remain positive in the months ahead.

### The day ahead in the UK

Consistent with recent economic surveys, which suggested that the labour market should continue tightening over the coming months, we expect the latest figures from the labour market, due tomorrow, to show a slight increase in employment in September, with headline three-month growth looking set to have remained close to the August level of 106k. And there is likely to be little change in the other major indicators too – the three-month unemployment rate should have remained at 4.9% for the fifth consecutive month, while wage growth will most likely have been stable at or very close to the 2.3%3M/Y rate reported in August.

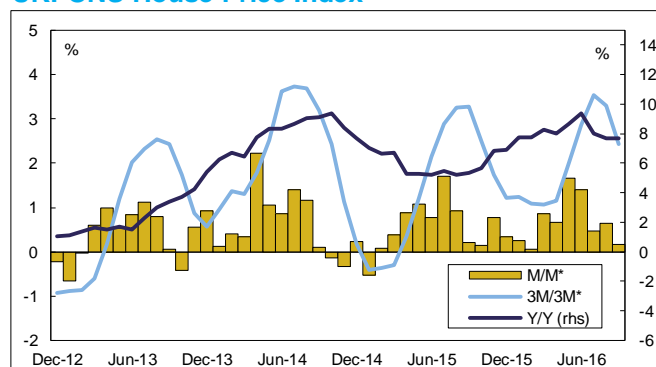
#### UK: CPI inflation



\*Excluding food and energy. \*\*Including alcohol and tobacco.

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













#### UK: ONS House Price Index









\*Seasonally adjusted data.

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	 GDP – second release Q/Q% (Y/Y%)	Q3	<b>0.3 (1.6)</b>	<u>0.3 (1.6)</u>	0.3 (1.6)	-
	 Trade balance €bn	Sep	<b>24.9</b>	22.1	23.3	<b>23.4</b>
	 ZEW expectations balance	Nov	<b>15.8</b>	-	12.3	-
Germany	 GDP – first release Q/Q% (Y/Y%)	Q3	<b>0.2 (1.7)</b>	<u>0.3 (1.8)</u>	0.4 (1.8)	-
	 ZEW current assessment balance (expectations)	Nov	<b>58.8 (13.8)</b>	61.6 (8.1)	59.5 (6.2)	-
France	 Final EU-harmonised CPI Y/Y%	Oct	<b>0.5</b>	<u>0.5</u>	0.5	-
Italy	 GDP – first release Q/Q% (Y/Y%)	Q3	<b>0.3 (0.9)</b>	<u>0.2 (0.8)</u>	0.0 (0.8)	- (0.7)
Spain	 Final EU-harmonised CPI Y/Y%	Oct	<b>0.5</b>	<u>0.5</u>	0.0	-
UK	 CPI (core CPI) Y/Y%	Oct	<b>0.9 (1.2)</b>	<u>1.2 (1.5)</u>	1.0 (1.5)	-
	 PPI input (output) price inflation Y/Y%	Oct	<b>12.2 (2.1)</b>	9.3 (1.8)	7.2 (1.2)	<b>7.3 (1.3)</b>
	 House price index Y/Y%	Sep	<b>7.7</b>	8.1	8.4	<b>7.7</b>
Country	Auction					
UK	 BoE APF operation purchased £1bn of 15Y+ Gilts (2.43 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	
UK	 09:30	Average earnings incl. bonuses (excl. bonuses) 3M/Y%	Sep	<u>2.4 (2.4)</u>	2.3 (2.3)	
	 09:30	ILO unemployment rate 3M%	Sep	<u>4.9</u>	4.9	
	 09:30	Employment change 3M/3M '000s	Sep	<u>120</u>	106	
	 09:30	Claimant count rate % (change 000s)	Oct	2.3 (2.0)	2.3 (0.7)	
Auctions and events						
Country	GMT	Auction / Event				
UK	 14:00	BoE's Cunliffe is scheduled to speak in Manchester				
	 14:50	BoE APF operation: To purchase 7-15Y Gilts				

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

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