

# Euro wrap-up

## Overview

- Bunds gained as ECB Vice President de Guindos made mildly dovish comments and BTPs rallied as Italy's Five Star Movement and Democratic Party made progress to reaching a new coalition government agreement.
- Gilts made gains as the main opposition parties agreed to work together through legislative means when the parliamentary recess ends next week to try to block a no-deal Brexit.
- Wednesday should bring more news on the Italian coalition negotiations while euro area bank lending data and further German and Italian economic sentiment survey results are due.

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### Daily bond market movements

Bond	Yield	Change
BKO 0 06/21	-0.907	-
OBL 0 10/24	-0.895	-0.012
DBR 0 08/29	-0.698	-0.027
UKT 1½ 01/21	0.377	-0.027
UKT 1 04/24	0.327	-0.039
UKT 1 % 10/28	0.505	-0.053

\*Change from close as at 4:30pm BST.  
Source: Bloomberg

## Euro area

### French economic sentiment stable

In marked contrast to yesterday's disappointing German ifo survey (see details below), but broadly consistent with the flash PMIs, today's French INSEE business confidence survey suggested that conditions are still holding up relatively well in the euro area's second-largest member state. In particular, the headline INSEE indicator was unchanged in August at 105, well above the long-run average. There was a modest improvement in the headline manufacturing indicator this month (up 1pt to a satisfactory 102), as firms – particularly in the food industry – were less downbeat about their order books and therefore more optimistic about their near-term production prospects. Meanwhile, conditions remained stable in the services and construction sectors, with the respective indices (105 and 111) well above the long-run average. There was a notable weakening in the retail sector, however, with the relevant index declining 4pts to 101, its lowest since January. Nevertheless, that still suggested that conditions in the sector were better than the long-run average. And while the employment climate was also assessed to be less favourable, overall the survey's turning point indicator continued to signal a positive short-term economic outlook.

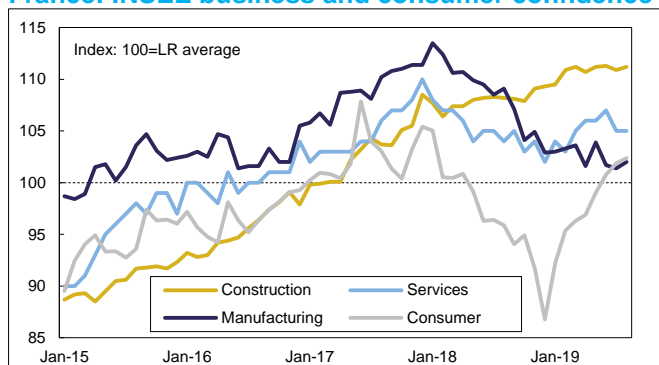
Similarly, the INSEE's consumer confidence survey suggested that households are currently broadly satisfied, with the headline index unchanged at 102 in August, matching the highest reading since January 2018, a whopping 15pts above the 'Gilets Jaunes'-related trough at the end of last year. Indeed, on average in the first two months of Q3, the consumer confidence indicator was more than 3pts higher than in Q2. And, overall, today's French economic survey results support our forecast for a slight pickup in French GDP growth this quarter to 0.3%/Q/Q.

### Germany heading for a recession?

While last week's flash PMIs offered some hope that the downturn in the euro area's largest member state might no longer be intensifying, yesterday's German ifo survey suggested the opposite was more likely the case. In particular, the headline business climate index declined for the fifth consecutive month to 94.3, the lowest since November 2012, leaving the average index in the first two months of Q3 more than 3pts below the average in Q2. This reflected a deterioration in assessments of current conditions and future expectations, with the latter at its lowest level for more than a decade. Yet again, manufacturers were more pessimistic about the current environment and the near-term outlook, with the respective indices at the weakest since the Global Financial Crisis in 2009. Moreover, there were further signs that the trials among manufacturers are spilling over to services – indeed, firms in the sector considered current conditions to be the worst for more than nine years in August, with the relevant index down on average so far in Q3 down more than 7pts from Q2.

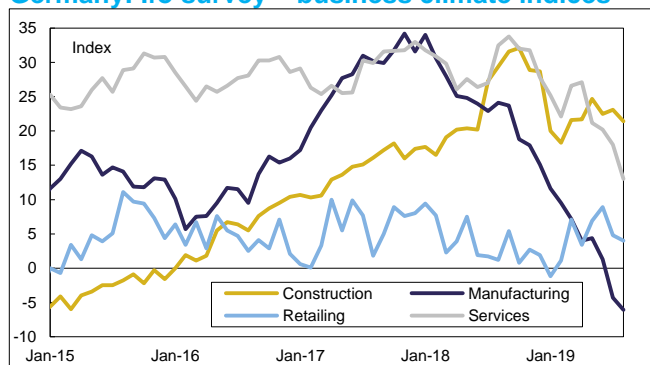
Germany's updated national accounts today confirmed the preliminary estimate of GDP, which had reported a contraction for the second quarter out of the past four in Q2, by 0.1%/Q/Q. Notably within the detail, a (probably unintentional) positive contribution of 0.3ppt from private inventories meant that the contraction in GDP wasn't significantly larger in Q2. Given the marked deterioration in

### France: INSEE business and consumer confidence



Source: Thomson Reuters and Daiwa Capital Markets Europe Ltd.

### Germany: Ifo survey – business climate indices



Source: Thomson Reuters and Daiwa Capital Markets Europe Ltd.



sentiment over recent months, that positive contribution from stock-building might seem unlikely to be repeated in the current quarter. In contrast, with order books having shrunk significantly over recent months, the weakness in overseas demand seen in Q2 – with exports declining at the steepest pace since Q412, to leave net trade subtracting 0.5ppt from GDP growth – might well be repeated in Q3. And while we expect fixed investment to avoid contraction this quarter, household consumption seems unlikely to be much stronger than the 0.1%Q/Q increase seen in Q2. As such, we now expect German GDP to contract by 0.1%Q/Q in Q3, followed by a modest increase in Q4, which would leave full-year GDP growth moderating by a full percentage point to just 0.5%Y/Y in 2019.

## The day ahead in the euro area and US

Italian politics will remain in focus on Wednesday. All signs today were that the Five Star Movement (M5S) and Democratic Party (PD) were making further strides to reaching a coalition agreement, news which provided a significant boost to BTPs. In particular, statements this afternoon suggested that agreement had been reached on personnel issues, most notably with PD conceding that Giuseppe Conte should be retained as Prime Minister. Important but difficult policy agreements, including on the 2020 Budget, however, remained to be settled. So, discussions on policy substance were set to continue this evening, and seem likely to continue tomorrow. An agreement between M5S and PD should result in a more prudent fiscal policy and as a result less conflict with the European Commission than would have emerged with the nationalist League in government.

Data-wise, tomorrow will bring the euro area's latest bank lending figures for July, which, despite softer GDP growth and weaker economic sentiment, are expected to report still solid consumer and business credit growth at the start of Q3. Wednesday will also bring more national-level sentiment indicators. Given the increased pessimism among businesses, Germany's GfK consumer survey is expected to signal a further moderation in household confidence in Q3. Similarly, against the backdrop of heightened political uncertainty Italy's households and businesses might well indicate a further deterioration in conditions in the latest ISTAT survey. In the markets, Germany will sell 10Y Bunds.

Wednesday should be a quiet day for economic data from the US with just weekly mortgage application figures due. Supply-wise, the Treasury will sell 2Y floating-rate notes and 5Y fixed-rate notes.

## UK

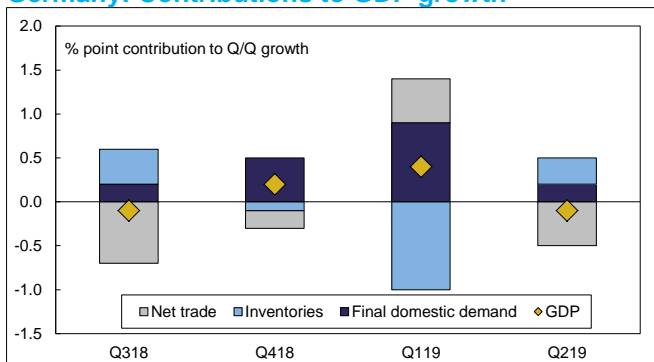
### Lending to households surprisingly picks up

Ahead of the Bank of England's lending figures on Friday, today's UK Finance numbers of the six major high-street lenders suggested that, despite heightened uncertainty about the outlook for Brexit, British households increased their borrowing at the start of Q3. While the total amount of outstanding credit card lending moderated slightly last month, there was a pickup in personal loans and overdrafts, to leave total consumer credit up 4.3%Y/Y in July, the strongest annual increase since February 2018. Perhaps reflecting the drop over recent months in mortgage interest rates, there was also a notable rise in net mortgage lending last month, by £2.9bn, the largest monthly increase since March 2016 and compared with an average increase of £1.7bn in the previous three months. The number of mortgage approvals for new house purchases also accelerated in July, up 43.3k, the highest since early 2017 to leave them more than 10% higher compared with a year earlier. It remains to be seen to what extent these trends will be replicated when all lenders are included in the BoE's numbers. And we would expect to see demand for lending to ease somewhat as the Brexit deadline looms.

### The day ahead in the UK

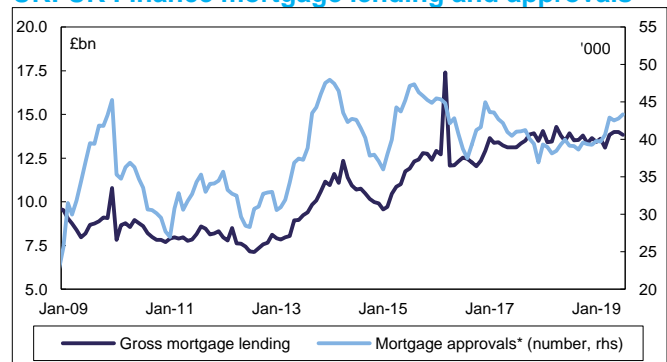
In the UK, a quiet day for top-tier releases tomorrow will see just the BRC's shop price index for August.

#### Germany: Contributions to GDP growth



Source: Destatis and Daiwa Capital Markets Europe Ltd.

#### UK: UK Finance mortgage lending and approvals







\*Figures include loans 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
Germany	 GDP – second release Q/Q% (Y/Y%)	Q2	<b>-0.1 (0.4)</b>	-0.1 (0.4)	0.4 (0.9)	-
France	 Business confidence (manufacturing confidence)	Aug	<b>105 (102)</b>	-	105 (101)	-
	 Consumer confidence	Aug	<b>102</b>	-	102	-
UK	 UK Finance loans for house purchase '000s	Jul	<b>43.3</b>	-	42.7	42.8



### Auctions

Country	Auction
Germany sold	 €3.95bn of 0% 2021 bonds at an average yield of -0.89%
Italy sold	 €2.0bn of 0% 2021 bonds at an average yield of 0.008%

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
Germany	 Ifo business climate	Aug	<b>94.3</b>	96.0	95.7	95.8
	 Ifo current assessment (expectations)	Aug	<b>97.3 (91.3)</b>	-	99.4 (92.2)	99.6 (92.1)

### Auctions


Country	Auction
- Nothing to report -	

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

## Tomorrow's releases

Country	BST	Release	Period	Market consensus/ <i>Daiwa forecast</i>	Previous
EMU	 09.00	M3 money supply Y/Y%	Jul	4.7	4.5
Germany	 07.00	GfK consumer confidence	Sep	9.6	9.7
Italy	 09.00	Consumer confidence	Aug	112.7	113.4
	 09.00	Business confidence (manufacturing confidence)	Aug	-	101.2 (100.1)
UK	 00.01	BRC shop price index Y/Y%	Aug	-	-0.1
	 -	Nationwide house price index* M/M% (Y/Y%)	Aug	-	0.3 (0.3)

### Auctions

Country	BST	Auction/Event
Germany	 10.30	Auction: to sell €3bn of 0% 2029 bonds

\*Approximate date of release. Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

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