

# Euro wrap-up

## Overview

- Despite some weak UK labour market data, Gilts sold off on speculation that a Brexit deal between the EU and UK was imminent.
- Bunds followed Gilts lower despite another downbeat ZEW investor survey.
- Ahead of the EU summit, Brexit will remain in focus tomorrow, while new data due include UK and final euro area inflation figures for September and updates on euro area trade and EU new car registrations.

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### Daily bond market movements

Bond	Yield	Change
BKO 0 09/21	-0.706	+0.012
OBL 0 10/24	-0.668	+0.020
DBR 0 08/29	-0.428	+0.031
UKT 3% 09/21	0.535	+0.033
UKT 1 04/24	0.486	+0.048
UKT 0% 10/29	0.696	+0.056

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

## Euro area

### ZEW reports weaker perceptions of German economy at the start of Q4

On a relatively quiet day for new economic data from the euro area, the flow of October economic surveys got underway on a weak note with the ZEW indices of investor analyst sentiment. In particular, the survey's index of German current conditions fell more than 5pts – a bigger decline than expected – to -25.3, the lowest level since April 2010 when the Greek debt crisis was escalating. However, the deterioration in the survey's outlook index, which gauges expectations for the coming six months, was minimal, dropping just 0.3pt to -22.8. While that still represented the second-lowest reading since 2011, it was nevertheless more than 20pts above the reading in August, suggesting that analyst assessments of the outlook have stabilised. We note, however, that the ZEW index of current conditions is often a good guide to the ifo business climate index, and so today's release reinforces our expectation of a deterioration in the ifo indices for the current month when they are released on 25 October.

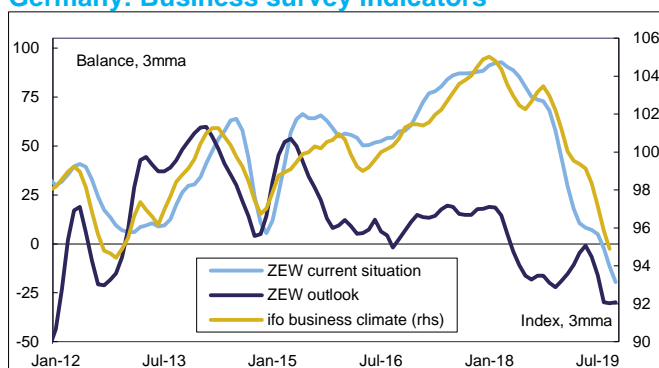
### No surprises from final French inflation data

Ahead of the release tomorrow of the equivalent euro area figures, the final estimates of French inflation in September provided no surprises whatsoever, predictably aligning with the flash data, which had seen the EU-harmonised measure of inflation drop 0.2ppt to 1.1%Y/Y, matching May's two-year low. The detail on the national measure confirmed that the decline was led by lower inflation of food (down 1.0ppt to 2.1%Y/Y) and energy (down 0.6ppt to 0.2%Y/Y). In contrast, services inflation edged higher (up 0.1ppt to 1.2%Y/Y), as prices of communication services rose on a year-on-year basis for the first time in more than a year, more than offsetting weaker inflation of airfares and healthcare. The pace of decline in manufactured items slowed (up 0.2ppt to -0.7%Y/Y) due to a slower pace of decline in clothes prices and an increase in car prices. As a result, core inflation on the EU-harmonised measure rose 0.2ppt to an eleven-month high of 0.8%Y/Y.

### The day ahead in the euro area and US

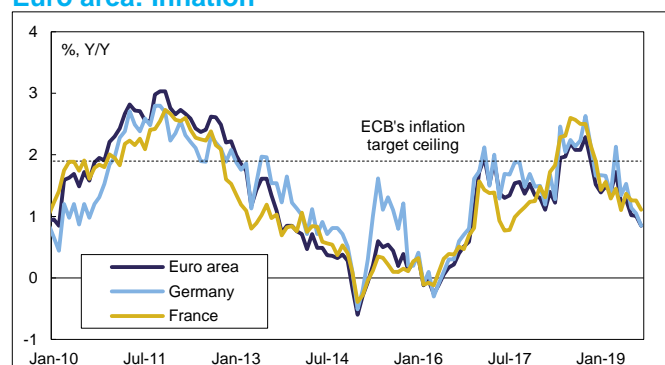
Wednesday will bring the aforementioned final euro area CPI figures for September. Like today's figures from France, and the equivalent data from [Germany and Spain](#) released last week, euro area headline inflation is likely to align with the flash reading to show a drop of 0.1ppt to 0.9%Y/Y, the lowest since November 2016. But while core inflation was nudged higher in the flash estimate by 0.1ppt to 1.0%Y/Y, rounding issues raise the risk of a downwards revision. Tomorrow will also bring September new car registrations figures from the euro area, which – like the national figures for the largest member states – are likely to report a double-digit annual rate of growth at the end of Q3, flattered to some extent by the low base the previous year as new emissions testing came into effect. And the euro area's trade report for August is likely to show a

### Germany: Business survey indicators



Source: Thomson Reuters and Daiwa Capital Markets Europe Ltd.

### Euro area: Inflation\*



\*Flash estimate for September 2019 for the euro area. Source: Thomson Reuters and Daiwa Capital Markets Europe Ltd.



narrowing in the surplus on the back of still-subdued external demand. Beyond the data, ECB Chief Economist Lane, Bundesbank President Weidmann, Bank of France National Bank President Villeroy de Galhau and Dutch National Bank President Knot will all speak publicly in the US. Finally, in the bond markets, Germany will sell 30Y Bunds.

In the US, Wednesday's principal focus will be the September retail sales figures, which are due together with business inventories numbers for August, the Fed's latest beige book and the NAHB housing market index for October. FOMC speakers include Chicago Fed President Charles Evans and Dallas Fed President Robert Kaplan. In the markets, the Treasury will sell 5Y TIPS.

## UK

### Is a Brexit deal imminent?

UK and EU negotiators were given to the end of today to reach a draft agreement on a deal that might be signed off by leaders at the EU summit on Thursday and Friday. And the mood music surrounding the talks became increasingly upbeat as the day wore on to push Gilts lower and sterling to its highest level against the euro since May. But the obstacles to such an agreement being reached tonight might yet be insurmountable. Key problems to resolve related to both practicalities and the detailed legal text, with material political differences seemingly remaining on all sides. Admittedly, the EU's chief negotiator Michel Barnier this morning stated that a deal this week was "still possible" even if it had become "more and more difficult". And late this afternoon reports suggested that a deal could be near, with Boris Johnson supposedly consulting the Northern Irish DUP to see if it would sign up to a possible new compromise.

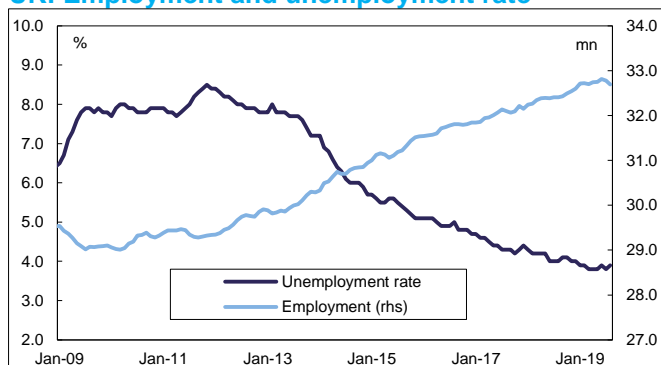
### Article 50 deadline to be extended whatever happens at the Summit

Of course, the EU does not want the positive mood to dissipate this week. So, while it still might not be possible to finalise an agreement tonight, at a minimum we would expect the Summit to come up with very warm words, commit to continue negotiations, and be prepared to pencil in a further Summit near the end of the month to try to reach a deal. Leaders will also likely discuss the length of any Article 50 extension that it will need to offer the UK if and when Boris Johnson writes to request one, as UK law will compel him to do if a deal is not endorsed by MPs by Saturday. Given the specifics of the UK legislation, a three-month extension to end-January would be most straight forward to agree although Johnson would surely prefer a shorter deadline. Meanwhile, if and when a deal is eventually reached, how that might fare in the House of Commons would still remain to be seen. Whether or not a majority in favour of the deal exists would depend very much upon the detail of the Withdrawal Agreement. And whether or not the DUP gives its support, the majority in Parliament might yet only give its consent if it was subject to a confirmatory referendum.

### Labour market cools on weaker economy

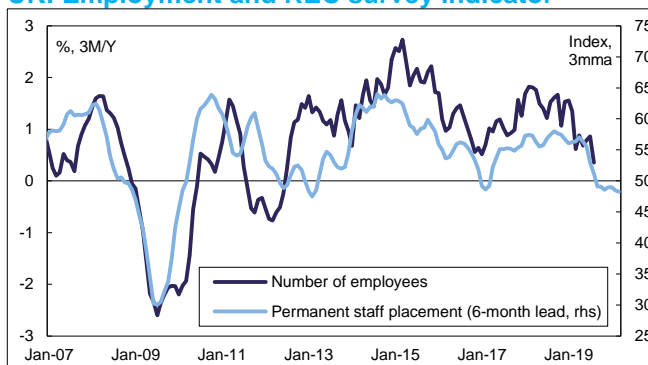
The steady loss of momentum in UK economic activity seen over recent months is being increasingly felt in the labour market, for which today's data were weaker than expected across the board. Most striking perhaps, having slowed steadily over recent months, employment fell 56k in the three months to August, representing the first decline in the number of people in work for almost two years. As a result, the unemployment rate reversed the decline the previous month, rising 0.1ppt back to 3.9%, still however 0.1ppt lower than a year earlier. Meanwhile, job vacancies maintained their negative trend, edging down in the three months to August to a near-two-year low. Evidence from the October REC jobs survey, which last week suggested the weakest increase in vacancies in more than seven years, and the September PMIs, which saw the composite employment index drop to a near-decade low of just 47.8, implies that employment is likely to decline in coming months too. Finally, having previously reached the strongest rates since 2008, the latest wage data missed expectations too, with regular pay and total labour earnings (including bonuses) both slowing 0.1ppt in the three months to August to 3.8%3M/Y. Like for jobs, we expect the weaker economic environment to contribute to a further softening of wage growth over coming quarters, albeit not so marked as to prevent ongoing positive growth in household consumption. And the loss of

#### UK: Employment and unemployment rate\*



\*Three-month moving averages. Source: Thomson Reuters and Daiwa Capital Markets Europe Ltd.

#### UK: Employment and REC survey indicator



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

momentum in the labour market, and in economic activity as a whole, is why we maintain our forecast for a cut in Bank Rate in January.

### **The day ahead in the UK**







Brexit will obviously remain the principle focus on Wednesday as officials make final preparations for the Summit on Thursday and Friday. EU leaders will not engage in technical negotiations at the Summit. So, agreement will need to be reached at official level tonight if the leaders are to be able to sign off a deal. And while reports suggest that additional progress is likely to have been made today, further work after the Summit to bridge remaining differences in position might be required if an agreement is eventually to be reached.

The economic data focus on Wednesday will turn to inflation. Having fallen a hefty 0.4ppt in August to 1.7%Y/Y, the lowest level since December 2016, the headline rate of CPI is expected to tick up to 1.8%Y/Y in September. A similar 0.1ppt rise in the core CPI rate to 1.6%Y/Y is also expected. The latest ONS house price data are expected to report a further slowing in the pace of national inflation in the sector from the near-seven-year low of 0.7%Y/Y registered in July. In addition, BoE Governor Carney will speak publicly at the Harvard Kennedy School and at an IMF event at the Washington DC annual meetings.



## European calendar

### Today's results

#### Economic data









Country	Release	Period	Actual	Market consensus/ <i>Daiwa forecast</i>	Previous	Revised
Germany	 ZEW current situation balance (expectations)	Oct	<b>-25.3 (-22.8)</b>	-25.0 (-27.0)	-19.9 (-22.5)	-
France	 Final CPI (EU-harmonised CPI) Y/Y%	Sep	<b>0.9 (1.1)</b>	0.9 (1.1)	1.0 (1.3)	-
UK	 ILO unemployment rate %	Aug	<b>3.9</b>	3.8	3.8	-
	 Employment 3M/3M, '000s	Aug	<b>-56</b>	20	31	-
	 Claimant count rate % (change '000s)	Sep	<b>3.3 (21.1)</b>	-	3.3 (28.2)	- (16.3)
	 Average earnings (excluding bonuses) 3M/Y%	Aug	<b>3.8 (3.8)</b>	4.0 (3.7)	4.0 (3.8)	3.9 (3.9)

#### Auctions

Country	Auction
Germany	 sold €3.166bn of 0% 2021 bonds at average yield of -0.70%
UK	 sold £2.75bn of 0.875% 2029 bonds at average yield of 0.633%

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

### Tomorrow's releases

Country	BST	Release	Period	Market consensus/ <i>Daiwa forecast</i>	Previous
EMU	 07.00	EU27 new car registrations Y/Y%	Sep	-	8.4
	 10.00	Trade balance €bn	Aug	18.0	19.0
	 10.00	Final CPI (core CPI) Y/Y%	Sep	1.0 (1.0)	1.0 (0.9)
Italy	 09.00	Industrial sales (orders) Y/Y%	Aug	-	-0.6 (-1.0)
	 10.00	Final CPI (EU-harmonised CPI) Y/Y%	Sep	0.3	0.5
UK	 09.30	CPI (core CPI) Y/Y%	Sep	1.8 (1.7)	1.7 (1.5)
	 09.30	PPI input prices (output prices) Y/Y%	Sep	-1.8 (1.2)	-0.8 (1.6)
	 09.30	House price index Y/Y%	Aug	-	0.7

#### Events & Auctions

Country	BST	Auction/Event
EMU	 13.30	ECB's Knot speaks in New York
	 16.00	ECB's Lane speaks in Washington
	 18.00	ECB's Weidmann and Villeroy De Galhau speak in New York
Germany	 10.30	Auction: €1bn of 1.25% 2048 bonds
UK	 14.00	BoE Governor Carney takes part in a panel session at IMF event

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

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