

Euro wrap-up

Overview

- Gilts made losses ahead of Saturday's House of Commons votes on the Brexit agreement, the outcome of which appeared too close to call.
- Bunds followed Gilts lower at the longer end of the curve on a quiet end to the week for economic data from the euro area.
- The coming week will bring Draghi's last ECB policy meeting, flash euro area PMIs and the fallout from the Brexit parliamentary votes.

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Daily bond market movements

Bond	Yield	Change
BKO 0 09/21	-0.686	-0.003
OBL 0 10/24	-0.635	+0.009
DBR 0 08/29	-0.392	+0.019
UKT 3¼ 09/21	0.533	+0.025
UKT 1 04/24	0.507	+0.033
UKT 0% 10/29	0.705	+0.027

*Change from close as at 4:35pm BST.

Source: Bloomberg

Euro area

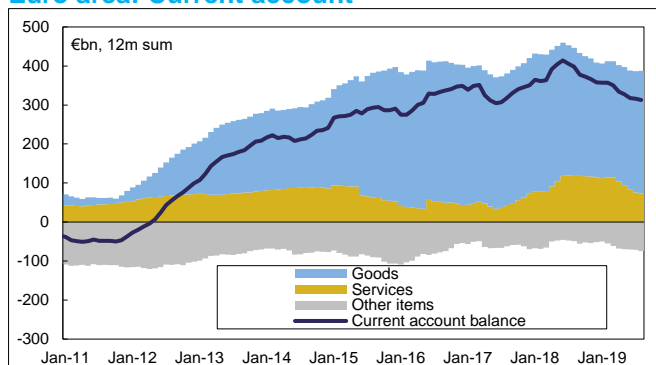
Current account surplus up in August

It was a quiet end to the week for economic data from the euro area, with the ECB's latest balance of payments report of most interest. With Wednesday's trade data having reported a big increase in the goods surplus in August to the highest since 2017 today's balance of payments report for the same month reported a hefty €5bn rise in the euro area's current account surplus, the most since January. That, however, merely took the current account surplus to €26.6bn, a high level albeit only slightly above the average for the year to date. On the methodology used by the ECB to calculate its balance of payments, however, the goods trade balance was actually very slightly smaller in August, at €27.7bn. And the increase in the current account surplus emanated from a jump in the services surplus, to a five-month high of €5.5bn, and an improvement in the income balance too. In the twelve months to August, the cumulative current account surplus fell €3.5bn to €312.4bn (2.7% of euro area GDP), down from the surplus of €397.9bn (3.5% of euro area GDP) in the twelve months to August 2018. At the country level in August, the current account surplus was again attributed largely to three large countries where domestic savings remain high: Germany (€16.9bn), Italy (€6.0bn), and the Netherlands (€4.7bn). France (a deficit of €4.7bn, the most in six months) provided only a modest offset. Looking ahead, we expect surpluses to remain exceptionally high in Germany (about 7% of GDP this year and next), Italy (between 2½-3% of GDP) and the Netherlands (about 9% of GDP).

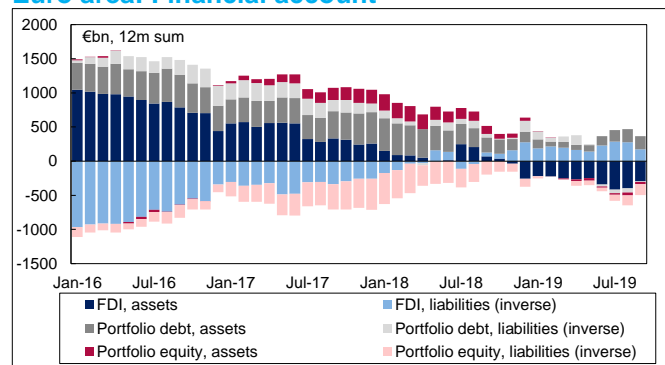
Direct disinvestments on the financial account

In the financial account, euro area residents made net acquisitions of foreign portfolio investment securities totalling €153bn in the twelve months to August 2019 (down from €411bn in the twelve months to August 2018). Over the same period, non-residents made net acquisitions of euro area portfolio investment securities amounting to €208bn (up from €153bn). In terms of direct investment, however, the picture was one of disinvestment. In particular, euro area residents made net disinvestments of €398bn in foreign assets in that period (compared to net investments of €207bn in the previous period). Likewise, non-residents made net disinvestments in euro area assets of €279bn in the most recent twelve-month period, reversing the net investments of €43bn in the twelve months to August 2018.

Euro area: Current account



Euro area: Financial account*



The week ahead in the euro area and US

The main event in the euro area in the coming week will be the conclusion of the ECB's Governing Council meeting on Thursday. The meeting will be most notable for being the final one to be chaired by Mario Draghi before Christine Lagarde takes over as ECB President at the start of next month. Policy-wise, however, the meeting will be a non-event. After the Governing Council last month agreed a package of new measures – including a 10bps cut in the deposit rate, an open-ended programme of net asset purchases to start on 1 November, a tiered rate framework to start on 30 October, and more generous conditions on the TLTRO-III operations – the outlook for policy seems unlikely to be discussed at the meeting. However, the much-publicised differences of opinion on the Governing Council will no doubt be a focus of the press conference. Moreover, Draghi might also be questioned on the desirability of the upwards shift in market rates across the curve seen since the meeting, which is in part likely related to the planned tiering framework. In terms of the economic outlook, meanwhile, there seems to be no good reason for the ECB to view its current forecasts as either too pessimistic or too optimistic.

Data-wise, the most notable new releases will be October survey results, including the flash PMIs on Thursday. The September PMIs suggested a further loss of momentum in the euro area at the end of the third quarter with declines in all key indicators and weakness most acute in manufacturing, for which the headline euro area PMI fell to 45.7, the lowest in more than seven years and the output and new orders indices down again likewise to the lowest since 2012. Other business climate indicators due include the German ifo and French INSEE indices on Friday and Wednesday respectively. And the Commission's preliminary consumer confidence index for October will also be released on Wednesday with the German GfK consumer survey results due Friday. The week will start with second-tier data, however, with German PPI data for September and Spanish trade figures for August arguably the most interesting releases on Monday and Tuesday respectively. In the markets, Germany will sell 10Y Bunds on Wednesday and Italy will sell a range of bonds on Friday.

In the US, the coming week will get off to a quiet start with no top-tier data due Monday and existing home sales figures for September the most notable release on Tuesday. Other housing market data due include the FHFA house price figures for August on Wednesday and new home sales figures for September on Thursday. That day will also bring preliminary durable goods figures for September, the flash Markit PMIs for October and usual weekly claims numbers. And Friday will bring the final University of Michigan consumer survey for the current month. In the markets, the Treasury will sell 2Y Notes on Tuesday, 5Y Notes and 2Y FRNs on Wednesday and 7Y Notes on Thursday. There will be no Fed-speak due to the purdah period ahead of the FOMC meeting the following week.

UK

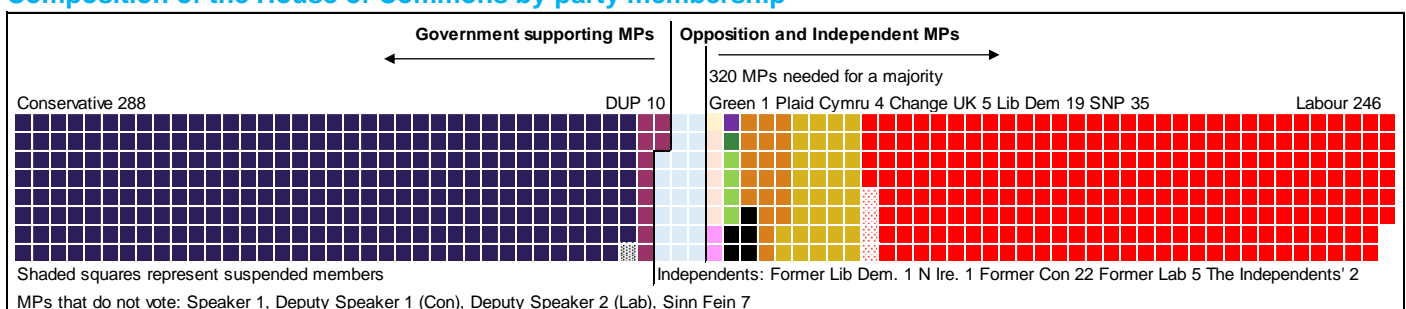
Vote on Brexit deal too close to call

There were no economic data of note released from the UK today, allowing all eyes to remain on MPs ahead of tomorrow's key votes on the Brexit Withdrawal Agreement in the House of Commons. In our view, the outcome of the vote is too close to call, with still no more than a 50% probability of the Agreement being endorsed unconditionally. Including one member currently suspended after being for a criminal offence, Johnson's Conservative Party has just 288 MPs, while 320 votes could be required to win a majority. So, PM Johnson's chances of success took a hit yesterday when the Northern Irish DUP insisted that its 10 MPs would vote against the deal, judging that it was unacceptable for them to place the Province in completely different trading arrangements to the rest of the UK. To win the day, therefore, Johnson will need the support of most of the 22 former Conservative independent MPs (most of whom he recently expelled from the parliamentary party) and the 28 hardline members of the Conservative ERG who failed to back Theresa May's deal, as well as at least ten Labour MPs.

Parliamentary amendments might be key to the way forward

At the time of writing, most ERG members and many former Conservative independents seemed highly likely to vote for deal. The number of Labour MPs who looked set to support it was in high single digits. However, fifteen of them intend to step down as MPs at the next general election, so might care little of the consequences to their careers in the Labour party.

Composition of the House of Commons by party membership



Source: *Institute for Government*
















Others might be emboldened to vote for it given the ambiguity of the messages from the party leadership with respect to the consequences for supporting the deal tomorrow. Most importantly perhaps, much might depend on parliamentary procedure, including whether MPs approve any amendments to tomorrow's main motion.

One key amendment (by Conservative independent Oliver Letwin) would allow MPs to indicate their possible future support for the forthcoming Withdrawal Amendment Bill while at the same time legally rejecting the deal tomorrow. That would keep alive the possibility that the deal would eventually be implemented, while also forcing Boris Johnson to write to the EU to request an Article 50 extension under the Benn Act. That extension would give more time for proper parliamentary scrutiny of the Agreement, including its economic impact, and more time for the Withdrawal Agreement Bill and equivalent EU legislation to be adopted. It could also, however, possibly lead to the Agreement eventually being adopted only conditional on a confirmatory referendum. All up, we now think it most likely that Johnson's deal will receive endorsement from MPs tomorrow, albeit in inconclusive form in accordance with this Letwin amendment. But the prospect of the UK leaving the EU as soon as 31 October might also thus be near-extinguished.

The week ahead in the UK



Brexit will no doubt continue to dominate the coming week, as policymakers respond to the outcome of the parliamentary votes. Beyond the politics, however, it should be a relatively low-key week for UK economic data. Public finances figures due on Tuesday will show that net borrowing in September continued to trend higher than its level a year earlier on a trajectory incompatible with the Government's fiscal rules. And the CBI industrial trends survey due the same day will suggest that manufacturing activity remained weak this month with orders in retreat following renewed Brexit-related inventory accumulation. UK Finance bank loan data for September, due Thursday, represent the only other UK release of note in the coming week. In the bond market, meanwhile, the DMO will sell 2025 Gilts on Tuesday.

Economic forecasts

	2019				2020				2018	2019	2020
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4			
GDP forecasts %, Q/Q											
Euro area 	0.4	0.2	0.1	0.2	0.2	0.2	0.2	0.1	1.9	1.1	0.8
Germany 	0.4	-0.1	-0.1	0.1	0.1	0.2	0.1	0.1	1.5	0.5	0.4
France 	0.3	0.3	0.3	0.3	0.3	0.3	0.2	0.2	1.7	1.3	1.2
Italy 	0.1	0.0	0.0	0.0	0.0	0.1	-0.1	-0.1	0.7	0.0	0.1
Spain 	0.5	0.4	0.4	0.4	0.4	0.4	0.4	0.3	2.4	2.2	1.6
UK 	0.5	-0.2	0.2	-0.1	0.2	0.2	0.2	0.1	1.4	1.0	0.5
Inflation forecasts %, Y/Y											
Euro area											
Headline CPI 	1.4	1.4	1.0	1.0	1.2	1.2	1.4	1.2	1.8	1.2	1.2
Core CPI 	1.0	1.1	0.9	1.0	1.1	1.2	1.4	1.3	1.0	1.0	1.0
UK											
Headline CPI 	1.9	2.0	1.9	1.7	2.0	1.7	1.5	1.5	2.5	1.9	1.7
Core CPI 	1.9	1.7	1.7	1.6	1.7	1.8	1.7	1.7	2.1	1.7	1.7
Monetary policy											
ECB											
Refi Rate % 	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00
Deposit Rate % 	-0.40	-0.40	-0.50	-0.50	-0.50	-0.50	-0.50	-0.50	-0.40	-0.50	-0.50
Net asset purchases* 	0	0	0	20	20	20	20	20	15	20	20
BoE											
Bank Rate % 	0.75	0.75	0.75	0.75	0.50	0.50	0.50	0.50	0.75	0.75	0.50
Net asset purchases** 	0	0	0	0	0	0	0	0	0	0	0

























*Monthly target €bn, end of period. **Monthly target £bn, end of period. Source: Bloomberg, ECB, BoE and Daiwa Capital Markets Europe Ltd.

European calendar

Today's results							
Economic data							
Country	Release	Period	Actual	Market consensus/ Daiwa forecast	Previous	Revised	
EMU 	Current account balance €bn	Aug	26.6	-	20.5	21.6	
Italy 	Current account balance €bn	Aug	6.0	-	8.4	-	
Auctions							
Country	Auction						
- Nothing scheduled -							












Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

The coming week's key data releases

Country	BST	Release	Period	Market consensus/ <i>Daiwa forecast</i>	Previous
Monday 21 October 2019					
Germany		07.00 PPI Y/Y%	Sep	-0.2	0.3
UK		00.01 Rightmove house price index M/M% (Y/Y%)	Oct	-	-0.2 (0.2)
Tuesday 22 October 2019					
Spain		09.00 Trade balance €bn	Aug	-	-2.5
UK		09.30 Public sector net borrowing	Sep	8.7	5.8
		11.00 CBI industrial trends survey, total orders (selling prices)	Oct	-24 (-)	-28 (12)
Wednesday 23 October 2019					
EMU		15.00 Consumer confidence indicator	Oct	-6.8	-6.5
France		07.45 Business confidence indicator	Oct	105	106
		07.45 Manufacturing confidence indicator (production outlook)	Oct	102 (-)	102 (4)
Thursday 24 October 2019					
EMU		09.00 Preliminary manufacturing PMI (services)	Oct	46.0 (52.0)	45.7 (51.6)
		09.00 Preliminary composite PMI	Oct	50.4	50.1
		12.45 ECB main refinancing rate %	Oct	0.00	0.00
		12.45 ECB marginal lending facility %	Oct	0.25	0.25
		12.45 ECB deposit facility rate %	Oct	-0.50	-0.50
Germany		08.30 Preliminary manufacturing PMI (services)	Oct	42.0 (51.8)	41.7 (51.4)
		08.30 Preliminary composite PMI	Oct	48.8	48.5
France		08.15 Preliminary manufacturing PMI (services)	Oct	50.0 (51.6)	50.1 (51.1)
		08.15 Preliminary composite PMI	Oct	50.9	50.8
Spain		08.00 Unemployment rate %	Q3	13.8	14.0
UK		09.30 Finance loans for house purchase '000s	Sep	42.2	42.6
Friday 25 October 2019					
Germany		07.00 GfK consumer confidence indicator	Nov	9.8	9.9
		09.00 Ifo business climate index	Oct	94.5	94.6
		09.00 Ifo current assessment balance (expectations)	Oct	98.0 (91.0)	98.5 (90.8)
France		07.45 PPI Y/Y%	Sep	-	-0.7
Spain		08.00 PPI Y/Y%	Sep	-	-2.5

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

The coming week's key events & auctions

Country	BST	Event / Auction
Monday 21 October 2019		
UK		16.00 BoE's Haldane speaks in Frankfurt
Tuesday 22 October August		
UK		10.30 Auction: to sell €3bn of 0.625% 2025 bonds
Wednesday 23 October 2019		
Germany		10.30 Auction: to sell €3bn of 0% 2029 bonds
Thursday 24 October 2019		
EMU		12:45 ECB monetary policy announcement
		13.30 ECB's Draghi speaks at a press conference following the Governing Council meeting
Friday 25 October 2019		
EMU		09.00 The ECB publishes its Survey of Professional Forecasters
		- ECB's Villeroy speaks in Paris
France		- French sovereign debt to be rated by Moody's
Italy		- Italian sovereign debt to be rated by S&P
		10.00 Auction: to sell bonds and index-linked bonds
UK		- UK sovereign debt to be rated by S&P

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

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