Euro wrap-up

Overview

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- Longer-dated Bunds made gains, despite a modest upside surprise to German factory orders data.
- Gilts also followed the global trend higher on a quiet day for UK economic news.
- Tomorrow will bring the BoE's latest monetary policy announcement and the publication of its quarterly Monetary Policy Report. Data-wise, German IP figures for September will be the most noteworthy release.

Daily bond market movements

Bond	Yield	Change
BKO 0 09/21	-0.647	+0.003
OBL 0 10/24	-0.582	-0.002
DBR 0 08/29	-0.327	-0.015
UKT 3¾ 09/21	0.553	-0.033
UKT 1 04/24	0.517	-0.036
UKT 0⅞ 10/29	0.731	-0.043

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

Euro area

Germany orders weak in Q3 despite stronger September

Most attention at the country level today was on the manufacturing sector, with German factory orders and Spanish IP figures for September. And there was a rare upwards surprise in the German factory orders data at the end of Q3, with headline manufacturing orders up 1.3%M/M in September. There was a welcome pickup in domestic orders (1.6%M/M), which reflected increased demand across the key sectors – i.e. new orders for consumer goods were up 3.1%M/M, capital goods up 2.3%M/M and intermediate goods up 0.3%M/M. And there was also a notable jump in overseas orders for capital goods too (+3.5%M/M). When adjusting for major items, the news was also more encouraging in September, with total orders 1.5% higher on the month with a 2% increase in domestic orders and a more than 1% increase in overseas orders (admittedly, this masked a more than 3%M/M drop in orders from elsewhere in the euro area). Of course, the more positive outturn in September follows marked weakness over recent months. And when smoothing out monthly volatility, total orders (on an adjusted basis) were still down 0.4%Q/Q over the third quarter as a whole, the seventh consecutive quarterly contraction. Moreover, when also including large one-off orders, total orders were down a steeper 0.8%Q/Q in Q3 and almost 5½ lower than a year earlier.

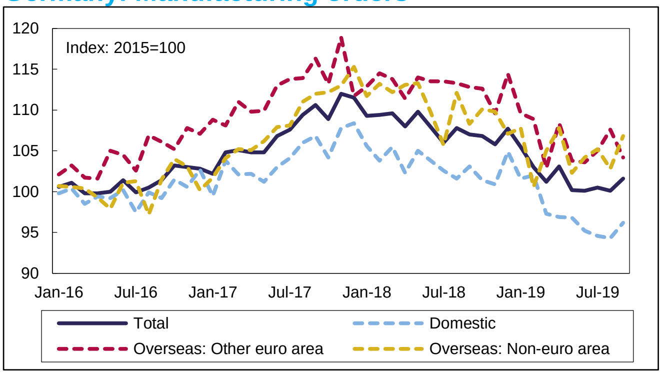
A weak end to Q3 for IP

Despite the better orders data, today's figures also showed that German manufacturing turnover – which typically closely aligns with production – fell for the fourth month out of the past six in September, with the 1.1%M/M decline leaving it down 1.0%3M/3M. This suggests that tomorrow's industrial production release will be soft. Certainly, today's output figures from Spain were softer, with the 0.8%M/M decline in September the third monthly fall out of the past four and the steepest since March, to leave annual growth moderating 0.6ppt to 0.8%Y/Y. And the weakness was broad based, with the decline in production of capital goods (-2.6%M/M), consumer goods (-0.9%M/M) and intermediate goods (-0.4%M/M) largely reversing the increases seen in August. So, this left Spanish manufacturing output 0.4% lower over the third quarter as a whole. And while energy production provided a modest boost in Q3, total industrial output declined 0.1%Q/Q, the first quarterly decline this year.

Retail sales softer in September

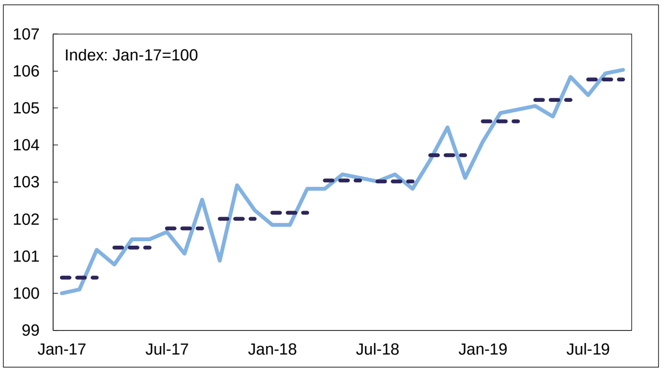
As we had expected, today's euro area retail sales data posted only modest growth at the end of the third quarter, reporting a rise of 0.1%M/M in September. This reflected similarly subdued growth in Germany (+0.1%M/M), no growth in Spain and declines in France (-0.5%M/M) and Portugal (-2.4%M/M). At the other end of the spectrum, sales in Ireland rose (2.4%M/M) at the fastest monthly pace since April 2018. Within the euro area detail, a decline in spending on food (-0.4%M/M) was offset by stronger fuel sales (+0.4%M/M). So, core sales were similarly restrained in September, with the 0.1%M/M increase only held up by spending on medical goods. But September's subdued outturn followed decent growth in August – total sales growth was upwardly revised to 0.6%M/M, while core sales were up 0.7%M/M. So, over the third quarter as a whole, retail sales were up ½%Q/Q, only a touch

Germany: Manufacturing orders*



*Adjusted for one-off large orders.
Source: Thomson Reuters and Daiwa Capital Markets Europe Ltd.

Euro area: Retail sales*



*Dashed dark blue line represents quarterly averages.
Source: Thomson Reuters and Daiwa Capital Markets Europe Ltd.

below growth in Q2 and consistent with our view that household consumption continued to provide support to GDP growth in Q3.

Euro area composite PMI points to softer growth

Like the manufacturing survey earlier in the week, today's final services PMI brought a modest upwards revision from the flash release. In particular, the headline business activity index was revised 0.4pt higher to 52.2, leaving it 0.6pt above its level in September. But this still signalled only moderate expansion in the sector at the start of Q4. So, given ongoing contraction implied by the manufacturing survey, the headline composite PMI – upwardly revised to 50.6 in October – still suggested one of the weakest growth rates of the past 6½ years. And with the new orders index posting the second successive sub-50 reading and employment rising at the softest pace since the start of 2015, the near-term outlook looks less favourable too.

At the country level, despite a modest upwards revision, Germany's services PMI (51.6) was still the second-lowest since mid-2013, with a similar pace of decline in new orders as that seen at the end of Q3. And overall, given the significant manufacturing weakness, the German composite PMI (48.9) remained consistent with negative GDP growth at the start of Q4. In contrast, the French services PMI aligned with the more positive assessment offered in the flash release (up 1.8pts to 52.9), with a similar increase in the composite PMI to 52.6. While the Italian services PMI was also more encouraging in October, with the headline index up 0.8pt to 52.2, a seven-month high, the composite PMI (up 0.2pt to 50.8) was still broadly consistent with stagnation. And a fall in the Spanish services PMI (down 0.6pt to 52.7), left the respective composite PMI (51.2) at its lowest level for almost six years.

The day ahead in the euro area and US

Tomorrow will bring the aforementioned German IP data for September. Expectations are for a drop in output of around ½%M/M, which would more than fully offset the increase in August and leave production almost 1% lower over the third quarter as a whole. Germany's construction PMI for October is also expected to imply weak conditions in that sector at the start of the fourth quarter. And Italy's retail sales figures are likely to report a modest pickup in September following notable weakness in the previous two months. Elsewhere, the European Commission will also publish updated economic forecasts, while in the markets, France and Spain will sell bonds with various maturities.

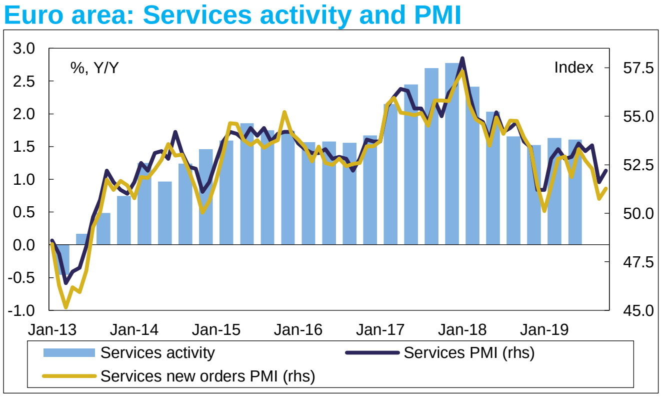
In the US, tomorrow's data calendar will include monthly consumer credit figures for September, as well as the weekly jobless claims numbers. In the markets, the US Treasury will sell 30Y bonds, while the Fed's Kaplan will speak in Dallas.

UK

The day ahead in the UK

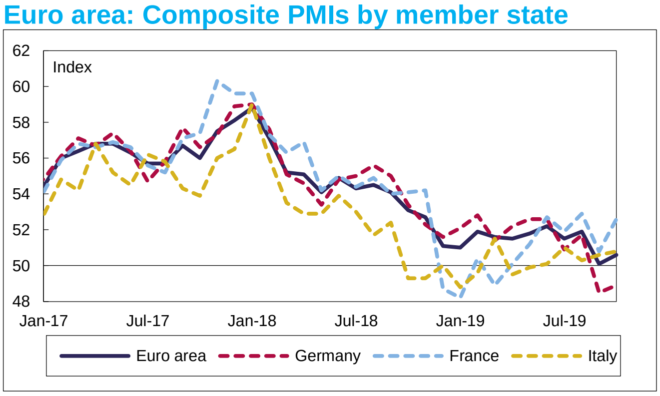
After a quiet day for economic news today, the main event in the UK tomorrow will be the BoE's latest monetary policy announcement, which will be accompanied by updated economic forecasts in its newly rebranded quarterly Monetary Policy Report. We expect no changes to policy, with Bank Rate set to be left at 0.75%. September's policy statement implied a further loss of confidence on the MPC about the Brexit process, and also acknowledged the more challenging external environment. Since then of course PM Johnson signed up to a draft Brexit Withdrawal Agreement with the EU. But with that having not been ratified by Parliament and a new general election next month, there remains significant uncertainty about the outlook for Brexit. Therefore, we would expect the MPC to remain relatively downbeat about the near-term outlook, with possible further downward revisions to both its GDP growth and inflation forecasts. Of course, in August, the MPC downplayed the value of its economic projections, emphasising the inconsistencies between the Bank's assumption of a smooth Brexit and the conditions underpinning moves in market asset prices, which at the time had reflected the increasing probability of a no-deal. And so, Carney seems likely to reiterate that downside risks not least associated with political uncertainty remain to the fore and therefore restate that the MPC will "take all appropriate measures to support jobs and activity, consistent with achieving the 2% inflation target commitment".

Euro area: Services activity and PMI



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

Euro area: Composite PMIs by member state



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

European calendar

Today's results

Economic data

Country	Release	Period	Actual	Market consensus/ *Daiwa forecast*	Previous	Revised
EMU	Final services PMI (composite PMI)	Oct	**52.2 (50.6)**	51.8 (50.2)	51.6 (50.1)	-
	Retail sales M/M% (Y/Y%)	Sep	**0.1 (3.1)**	0.1 (2.5)	0.3 (2.1)	**0.6 (2.7)**
Germany	Factory orders M/M% (Y/Y%)	Sep	**1.3 (-5.4)**	0.0 (-6.7)	-0.6 (-6.7)	**-0.4 (-6.5)**
	Final services PMI (composite PMI)	Oct	**51.6 (48.9)**	51.2 (48.6)	51.4 (48.5)	-
France	Final services PMI (composite PMI)	Oct	**52.9 (52.6)**	52.9 (52.6)	51.1 (50.8)	-
Italy	Services PMI (composite PMI)	Oct	**52.2 (50.8)**	51.0 (50.0)	51.4 (50.6)	-
Spain	Industrial production M/M% (Y/Y%)	Sep	**-0.8 (0.8)**	-0.8 (1.6)	0.9 (1.7)	**0.6 (1.4)**
	Services PMI (composite PMI)	Oct	**52.7 (51.2)**	52.9 (51.1)	53.3 (51.7)	-

Auctions

Country	Auction
	- Nothing to report -

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

Tomorrow's data releases

Economic data

Country	BST	Release	Period	Market consensus/ *Daiwa forecast*	Previous
Germany	07.00	Industrial production M/M% (Y/Y%)	Sep	-0.3 (-4.4)	0.3 (-4.0)
	09.30	Construction PMI	Oct	-	50.1
Italy	09.30	Retail sales M/M% (Y/Y%)	Sep	-	-0.6 (0.7)
UK	12.00	BoE Bank Rate %	Nov	0.75	0.75

Auctions and events

Country	BST	Auction / Event
EMU	09.00	ECB publishes its Economic Bulletin
	10.00	EU Commission publishes its Economic Forecasts
Spain	09.40	Auction: to sell 0.25% 2024 bonds
	09.40	Auction: to sell 0.15% 2023 index-linked bonds
	09.40	Auction: to sell 0.6% 2029 bonds
	09.40	Auction: to sell 1.85% 2035 bonds
France	09.50	Auction: to sell 0% 2029 bonds
	09.50	Auction: to sell 1.25% 2034 bonds
	09.50	Auction: to sell 1.5% 2050 bonds
	09.50	Auction: to sell 1.75% 2066 bonds
UK	09.30	The Office for Budget Responsibility publishes its fiscal forecasts
	12.00	BoE publishes its Monetary Policy Report
	12.30	BoE Governor Carney speaks at the post-policy announcement press conference

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

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