Euro wrap-up

Overview

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- Bunds made significant gains even as German Q3 GDP surprised modestly to the upside while euro area job growth slowed.
- Gilts also made big gains as UK retail sales dropped at the start of Q4.
- Friday will bring euro area trade figures for September and final inflation numbers for October.

Daily bond market movements

Bond	Yield	Change
BKO 0 09/21	-0.654	-0.014
OBL 0 10/24	-0.595	-0.032
DBR 0 08/29	-0.351	-0.047
UKT 3¾ 09/21	0.531	-0.019
UKT 1 04/24	0.494	-0.037
UKT 0⅞ 10/29	0.710	-0.049

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

Euro area

German GDP growth subdued but positive

German Q3 GDP beat expectations with growth of 0.1%Q/Q. So, technical recession was avoided in the euro area's largest member state. But growth there merely matched the Italian rate to be the weakest of all member states. And the second-quarter figure was revised down by 0.1ppt to show a contraction of 0.2%Q/Q, the weakest since Q113. So, GDP in Q3 remained below the Q1 level, while the annual growth rate ticked up just 0.2ppt to a still underwhelming 0.5%Y/Y, the second weakest in six years. Although the detailed expenditure breakdown is still unavailable, the German statistical agency reported that growth came mainly from private and public consumption. Having fallen the most in almost six years in Q2, exports also rose, while imports were little changed. But while construction investment was firmer, capex in machinery and equipment disappointingly fell. With economic survey indicators for October having been weak but stable, factory orders figures tilting slightly upwards, and fiscal policy set to be only moderately stimulative (with the structural surplus set to decline by about ½ppt of GDP), we currently expect German growth to remain modestly positive in Q4 and into the first half of 2020.

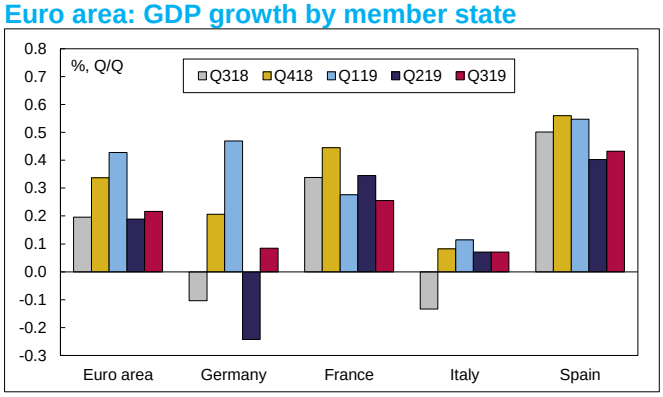
Job creation at near-six-year low

Despite the upside surprise to German GDP, euro area growth in Q3 was today confirmed at the flash estimate of 0.2%Q/Q, unchanged from Q2, with the annual rate similarly unchanged at 1.2%Y/Y. However, job creation slowed 0.1ppt last quarter to 0.1%Q/Q, the weakest since Q413, leaving the annual rate at 1.0%Y/Y. Among the member states, the slowdown in employment appears to have been concentrated in Italy and Spain, the latter of which recorded a rebound in October. Nevertheless, we expect aggregate job growth to remain subdued in Q4 and early in the New Year, and slow to an effective halt in the course of 2020. And so, the unemployment rate, which fell to 7.5% in August and September, is also likely to decline at a slower pace before leveling out by the middle of next year.

The day ahead in the euro area and US

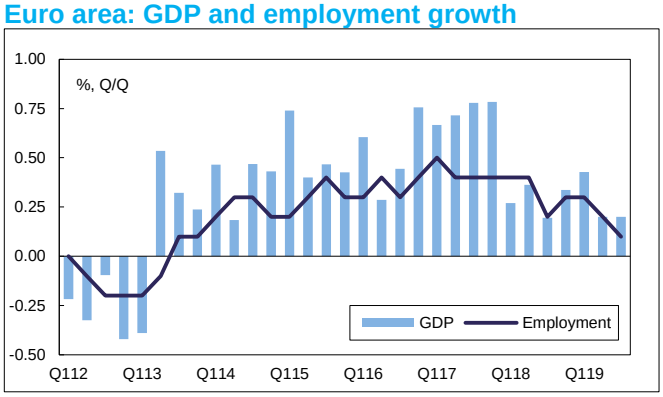
Tomorrow will bring final euro area inflation figures for October. With updated numbers from Germany, France and Spain having aligned with the respective flash estimates, we expect headline euro area CPI to confirm the 0.1ppt decline to 0.7%Y/Y reported in the preliminary release. However, given rounding effects and the unpredictability of Italian figures (also due tomorrow), there is a non-negligible risk that it will be revised higher. The euro area's core CPI rate is expected to be confirmed at 1.1%Y/Y, 0.1ppt higher than in September. Friday will also see the release of euro area trade figures for September, which should provide some insight into the extent to which net exports weighed on GDP growth in Q3.

Euro area: GDP growth by member state



Source: Thomson Reuters and Daiwa Capital Markets Europe Ltd.

Euro area: GDP and employment growth



Source: Thomson Reuters and Daiwa Capital Markets Europe Ltd.

It will be a busy end to the week for US top-tier releases, with retail sales and IP data for October most notable. But while retail sales are expected to have reversed some of the weakness seen in September, IP is forecast to have had a soft start to the fourth quarter, with a third monthly contraction out of the past four due partly to the negative impact of the strike at General Motors that month. Friday will also bring the latest business inventories figures for September, export and import prices data for October and the Empire Manufacturing index for November.

UK

Retail sales weaken at start of Q4

While UK GDP figures earlier this week suggested that household consumption maintained a moderate growth trend in the third quarter, today's retail sales numbers offered a more downbeat assessment of spending at the start of Q4. Indeed, contrasting with an expected increase, total retail sales declined 0.1%M/M in October, representing the third month in a row when sales have failed to grow. So, while this left sales up a seemingly healthy 3.1%Y/Y, on a three-month basis sales slowed in October to 0.2%3M/3M, the softest such pace since spring 2018, when activity was disrupted by heavy snow. The detail of today's figures suggested a weakening of the underlying consumption trend too. For example, when excluding spending on fuel (1.5%M/M), retail sales fell a steeper 0.3%M/M in October. And with the exception of department stores – where discounting last month provided a boost and followed a particularly subdued performance over the past year – sales were weaker across the board. While monthly sales figures are often volatile, on a three-month basis, spending at non-food stores declined for a second successive month (-0.2%3M/3M), while online sales fell for the first time in nineteen months (-0.2%3M/3M). While further discounting might support spending in the run up to Christmas, with consumer confidence remaining close to recent lows, employment and wage growth moderating, and the general election adding a further source of uncertainty regarding Brexit, we see little prospect of a sudden pickup in spending over coming months.

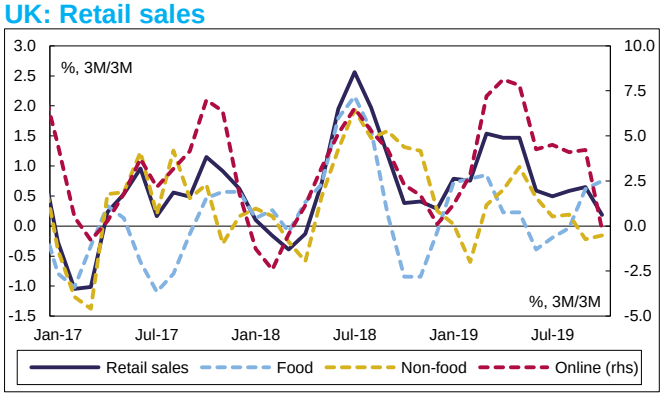
Housing market remains subdued

Concerns about the economic outlook continue to weigh on the housing market too. Yesterday's official ONS House Price Index suggested that inflation in the sector moved sideways at a subdued 1.3%Y/Y in September, broadly in line with the average of the past year but just half the pace seen in 2018 and significantly weaker than the near-8%Y/Y price growth seen ahead of the 2016 EU referendum. And today's RICS residential market survey suggested little improvement in conditions at the start of Q4. For example, the headline price balance fell 2pts in October to -5, a three-month low. This principally reflected a significant decline in the house price indices for the East and Northern England, down a whopping 63pts and 42pts respectively, with the former at its weakest level since 2011. In contrast, house price balances for London and the South East improved in October, signalling the softest pace of declines since late-2016 and mid-2017 respectively. But while surveyors in London also reported a significant improvement in new buyer enquiries last month, new supply to the market was reportedly the weakest since 2003 and agreed sales continued to fall. And overall, at the national level, demand and supply of housing remained subdued and well below the long-run average. So, while surveyors were somewhat more upbeat about the outlook further ahead, we continue to expect only subdued price growth over coming quarters, at least for as long as political and economic uncertainty persists.

The day ahead in the UK

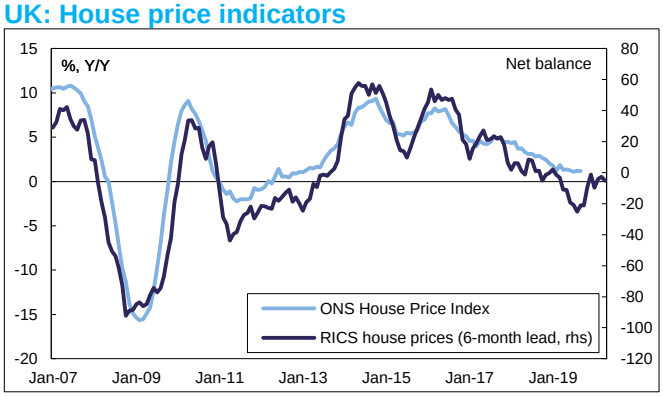
With no UK economic data of note due tomorrow, focus will remain firmly on politics.

UK: Retail sales



Source: Thomson Reuters and Daiwa Capital Markets Europe Ltd.

UK: House price indicators



Source: 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	GDP – second estimate Q/Q% (Y/Y%)	Q3	**0.2 (1.2)**	0.2 (1.1)	0.2 (1.2)	**-**
	Employment Q/Q% (Y/Y%)	Q3	**0.1 (1.0)**	-	0.2 (1.2)	**-**
Germany	GDP – first estimate Q/Q% (Y/Y%)	Q3	**0.1 (0.5)**	-0.1 (0.5)	-0.1 (0.4)	**-0.2 (0.3)**
France	Final CPI (EU-harmonised CPI) Y/Y%	Oct	**0.8 (0.9)**	0.7 (0.9)	0.9 (1.1)	**-**
Spain	Final CPI (EU-harmonised CPI) Y/Y%	Oct	**0.1 (0.2)**	0.1 (0.2)	0.1 (0.2)	**-**
UK	RICS house price balance	Oct	**-5**	-3	-2	**-3**
	Retail sales including fuel M/M% (Y/Y%)	Oct	**-0.1 (3.1)**	0.2 (3.7)	0.0 (3.1)	**-**
	Retail sales excluding fuel M/M% (Y/Y%)	Oct	**-0.3 (2.7)**	0.2 (3.4)	0.2 (3.0)	**- (2.9)**

Auctions

Country	Auction
UK	sold £2.25bn of 1.75% 2049 bonds at an average yield of 1.254%

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

Tomorrow's data releases

Economic data

Country	BST	Release	Period	Market consensus/ *Daiwa forecast*	Previous
EMU	10.00	Trade balance €bn	Sep	18.7	20.3
	10.00	Final CPI (core CPI) Y/Y%	Oct	0.7 (1.1)	0.8 (1.0)
Italy	09.00	Total trade balance €bn	Sep	-	2.6
	10.00	Final CPI (EU-harmonised CPI) Y/Y%	Oct	0.4 (0.2)	0.4 (0.2)

Auctions and events

Country	BST	Auction / Event
EMU	08.00	ECB's Mersch is scheduled to speak

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

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