

Euro wrap-up

Overview

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- On a day of positive risk appetite, Bunds made losses as the ifo business survey suggested only a relatively modest drop in German GDP in Q4.
- Gilts also made losses as a survey also suggested that UK retail sales remain relatively resilient in Q4.
- Wednesday will bring a fiscal update from the UK and the ECB's Financial Stability Review, while Thursday will bring the ECB's account of its October monetary policy meeting and data on euro area bank lending and German consumer confidence.

Daily bond market movements

Bond	Yield	Change
BKO 0 09/22	-0.759	+0.009
OBL 0 10/25	-0.754	+0.012
DBR 0 08/30	-0.567	+0.016
UKT 1½ 09/22	-0.034	+0.006
UKT 0% 06/25	0.015	+0.010
UKT 4% 12/30	0.323	+0.007

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

Source: Bloomberg

Euro area

ifo survey points to modest drop in German GDP in Q4

Like yesterday's [flash PMIs](#), the ifo business survey for November suggested that the hit to Germany's economy in Q4 from the coronavirus second wave should be far more modest than the hit in the first half of the year from the initial wave. The headline business climate index dropped for the second month in a row, falling by 1.8pts to 90.7, the lowest since July. But the deterioration was caused predominantly by a weakening in expectations of conditions six months ahead, for which the relevant index fell 3.2pts to a five-month low of 91.5. In contrast, the index of current conditions dropped just 0.4pt to 90.0, still the second-highest level since March.

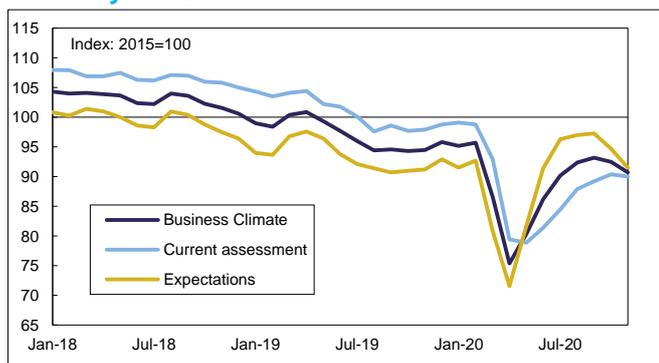
Manufacturing resilience compensating for services weakness

Like the flash PMIs, the ifo survey pointed to a positive mood in manufacturing, with firms in the sector reporting a further improvement in current conditions to the most favourable since February despite a weakening of future expectations for a second successive month. So, the deterioration principally reflected services, for which the respective business climate index fell back into negative territory for the first time since June, on weaker assessments of both current conditions and expectations. Unsurprisingly given current restrictions, the ifo institute noted particular weakness in hotels and hospitality. Retailers also reported a weakening in both current conditions and expectations, while construction firms were similarly more downbeat about the future.

German GDP growth in Q3 revised up

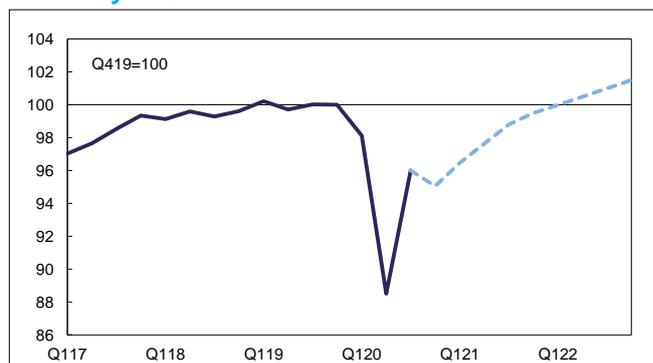
Updated German GDP figures for Q3 released this morning revised up the rate of growth, by 0.3ppt to a new record 8.5%Q/Q, which left the level 4.0% below the peak in Q419, the smallest such shortfall of all large European economies. Growth was driven by household consumption (up 10.8%Q/Q) and investment in machinery and equipment (up 16.0%Q/Q), while government consumption also rose (0.9%Q/Q). Having grown at the start of the year, however, construction investment dropped 2.0%Q/Q. Net trade also made a substantive contribution to growth, with exports of goods and services up 18.1%Q/Q, almost double the pace of imports (9.1%Q/Q). On the production side, the rebound in value-added was particularly vigorous in manufacturing (14.0%Q/Q), trade, transport, accommodation and food services (13.8%Q/Q) and public services, education and health (9.5%Q/Q). Looking ahead, we currently anticipate a contraction in German GDP in Q4 of about 1.0%Q/Q, weighed by a significant drop in consumption, with the decline in services activity more than outweighing continued expansion in manufacturing. This week's surveys, however, point to a smaller contraction in GDP. And we maintain our forecast of a resumption in German growth in Q121 to take the level of output above the Q3 level.

Germany: ifo Business Climate indices



Source: Refinitiv and Daiwa Capital Markets Europe Ltd.

Germany: GDP forecast*



*Dashed line represents forecast.

Source: Refinitiv and Daiwa Capital Markets Europe Ltd.

INSEE survey signals a steeper drop in GDP in France

Given the more intense spread of the pandemic, as well as the greater stringency of the containment measures, French GDP will suffer a steeper contraction in Q4 than its German equivalent. So, unsurprisingly, the November French INSEE business climate survey tallied with the flash PMIs to suggest a significant drop in economic activity this month but one that is in no way comparable in size with the record slump during the first wave of coronavirus. In particular, the headline business climate indicator fell by 11pts in November to 79, the same level as in June, still nevertheless a sizeable 25pts above the April low. Within the detail of the survey, there were steep drops in the respective indices for services (down 12pts to 77, led by accommodation and food, but with marked declines in professional and support services among others) and retail trade (down 23pts to 72). But the declines in manufacturing (down 2pts to 92) and wholesale trade (down 3pts to 87) were much more moderate. Meanwhile, due largely to lower demand in services, the employment index fell 6pts to a three-month low of 83. All indices, however, remain well above their springtime lows. Some of the government's containment measures will be lifted from next week, including the reopening of certain kinds of shops. However, many restrictions will persist beyond the festive season. And the INSEE survey flagged a marked deterioration in expectations in most services as well as retail, suggesting ongoing weakness into the New Year.

The coming two days in the euro area

The economic data calendar over the coming days is somewhat quieter. Spanish producer price figures are due tomorrow, followed on Thursday by the German GfK consumer confidence survey for November and euro area M3 money supply data, including bank lending, for October. There will also be a steady flow of news out of the ECB, with the six-monthly Financial Stability Review due tomorrow followed on Thursday with the account of the [October policy meeting](#), when Lagarde announced that policy would be recalibrated in December. We will also hear from ECB Board members Lane and Schnabel.

UK

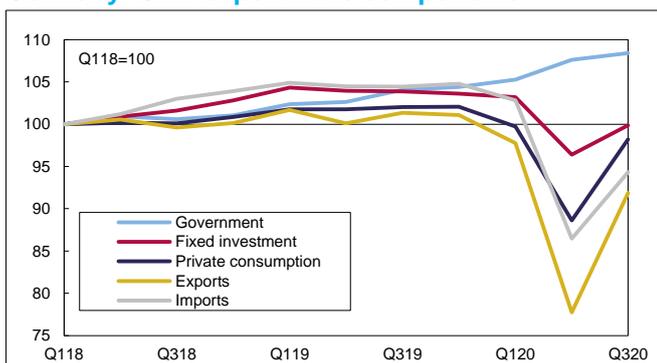
CBI survey suggests moderate hit to retail from latest store closures

Following last week's confirmation of another strong month for [retail sales in October](#), today's CBI distributive trades survey for November added to evidence that the drop in spending in Q4 will be nowhere near as deep as that during the first half of the year. While the survey measure of retail sales volumes dropped at the sharpest rate since June, the pace of decline was smaller than expected and only 2pts lower than in October (balance of -25%) even though non-essential stores in England were shut for much of the survey period (and will remain shut until next week). Indeed, internet sales grew at the fastest pace since October 2018 (up 8pts to +55%) and are expected to grow at a similarly robust pace next month (+53%). Meanwhile, the pace of decline in orders from a year ago reportedly continued to moderate to the slowest pace since December 2019 (balance of -10% from -39%), with only a slightly steeper pace of fall expected next month (-13%). Despite concerns of disruption to supply from the end of the Brexit transition, however, retail stock levels remained below the long-run average and were expected to remain so next month. Meanwhile, with English showrooms shut, motor trade volumes fell for a second consecutive month (-28%) and are expected to continue to fall in December (-32%). Finally, average retail selling prices in the current quarter reportedly increased at the fastest pace since before the coronavirus hit, although inflation was expected to ease in Q121. And retail employment continued to fall, albeit at a slower pace than last quarter.

The coming two days in the UK

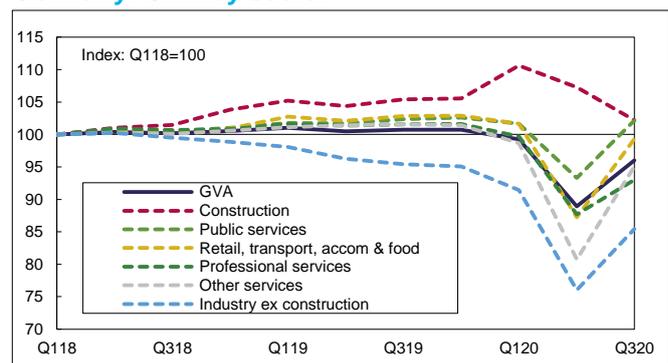
With no UK economic data due, the focus in the coming days will be on tomorrow's spending review announcement by the Government, which will include an update on the amount of funding to be provided to public services during this financial year and next. Reports last week suggested a public sector wage freeze is on the near-term agenda, while some tax rises and new spending restraint could be signalled from FY22-23. With the UK economy soon to be subject to a big adverse shock from the end of the Brexit transition period, the possibility of premature fiscal tightening is only one reason to expect the UK economic recovery to continue to lag that of its peers over the coming couple of years. In addition, tomorrow the OBR will publish updated economic and fiscal forecasts and the DMO will receive an updated Gilt remit.

Germany: GDP expenditure components



Source: Refinitiv and Daiwa Capital Markets Europe Ltd.

Germany: GVA by sector



Source: Refinitiv 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 	Final GDP Q/Q% (Y/Y%)	Q3	8.5 (-4.0)	8.2 (-4.3)	-9.7 (-11.3)	-
	Ifo business climate	Nov	90.7	90.2	92.7	92.5
	Ifo current assessment (expectations)	Nov	90.0 (91.5)	87.6 (93.5)	90.3 (95.0)	90.4 (94.7)
France 	Insee business confidence	Nov	79	84	90	-
	Insee manufacturing confidence (production outlook)	Nov	92 (-39)	91 (-14)	93 (-12)	94 (-)
UK 	CBI distributive trades, reported sales	Nov	-25	-	-23	-

Auctions

Country	Auction
UK 	sold £1.25bn of 1.75% 2057 bonds at an average yield of 0.86%

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

Tomorrow's releases

Economic data

Country	GMT	Release	Period	Market consensus/ <i>Daiwa forecast</i>	Previous
Spain 	08.00	PPI Y/Y%	Oct	-	-3.3

Auctions and events

EMU 	07.00	ECB's Research Bulletin published			
	09.30	ECB's November Financial Stability Review published			
Italy 	10.00	Auction: fixed rate and index-linked bonds			
UK 	13.00	Government to announce spending review outcome, OBR to publish updated forecasts and DMO to receive new Gilt remit			

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

Thursday's releases

Economic data

Country	GMT	Release	Period	Market consensus/ <i>Daiwa forecast</i>	Previous
EMU 	09.00	M3 money supply Y/Y%	Oct	10.4	10.4
Germany 	07.00	GfK consumer confidence	Dec	-4.9	-3.1

Auctions and events

EMU 	09.00	ECB's Monetary developments in the euro area published			
	12.00	ECB Chief Economist Lane scheduled to speak			
	12.30	ECB's account of the monetary policy meeting on 28-29 October published			
	13.30	ECB's Schnabel scheduled to speak			
UK 	09.30	BoE's October Capital Issuance data published			

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

The next edition of the Euro wrap-up will be published on 26 November 2020

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