

Euro wrap-up

Overview

- Bunds were little changed as the SPD won the largest share of the vote in Germany's federal election with a three-party coalition to be required to govern once Merkel departs.
- Gilts made losses as a speech by BoE Governor stated that current price pressures are likely to be transient, but also that the outlook remains uncertain and that Bank Rate might have to be raised.
- Tuesday will bring consumer confidence surveys from Germany and France while Wednesday will bring the Commission's broader sentiment survey.

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Daily bond market movements

Bond	Yield	Change
BKO 0 09/23	-0.696	+0.008
OBL 0 10/26	-0.565	+0.008
DBR 0 08/31	-0.225	+0.004
UKT 0 ⁷ / ₈ 01/24	0.371	-0.001
UKT 0 ³ / ₈ 10/26	0.587	+0.006
UKT 0 ¹ / ₄ 07/31	0.945	+0.022

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

Source: Bloomberg

Euro area

Scholz's SPD most likely to lead three-party coalition after German election

Following yesterday's federal election, the precise nature of Germany's next government remains unclear and is unlikely to be determined for a number of months. A repeat of the current grand coalition of the centre-right CDU/CSU and centre-left SPD – albeit inverted with the SPD being the senior partner – is arithmetically possible. However, given the marked change in electoral fortunes of those two establishment parties and the shifts in support for the other parties, it would seem unlikely. Instead, a three-party coalition government will almost certainly be required. And while both SPD and CDU/CSU now have to court the Greens and liberal Free Democrats (FDP) to get the right to lead the next coalition government, the SPD has the upper hand.

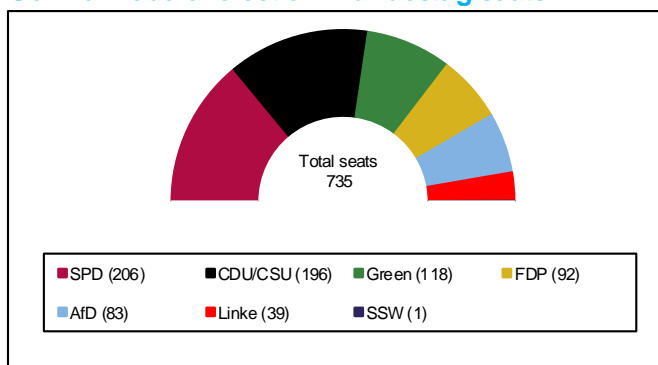
CDU/CSU beats expectations but would lack credibility in next government

Certainly, recent opinion polls proved to be accurate as far as the SPD was concerned. According to the preliminary official result, it took 25.7% of the vote, the largest share and up more than 5ppts from the previous election in 2017. The centre-right CDU/CSU outperformed their recent poll ratings, taking 24.1%. Nevertheless, that was still a record low and down almost 9ppts from 2017. In contrast, the Greens secured their best ever result. But while their share of 14.8% was almost 6ppts above their result in 2017, it was well down on the share suggested by polls early in the campaign. The FDP won 11.5%, little better than last time around. And the parties at the extremes both saw their support decline, leaving them both effectively consigned to the former East Germany. The far-right Alternative for Germany (AfD) share fell almost 2½ppts to 10.3%. And the far-left Die Linke won just 4.9%, down more than 4ppts and only securing representation in the next Bundestag by virtue of securing three direct mandates. Indeed, it performed so badly as to render a "Red-Red-Green" coalition of SPD, Die Linke and Greens unviable.

Traffic-light coalition of incremental reform still most likely outcome

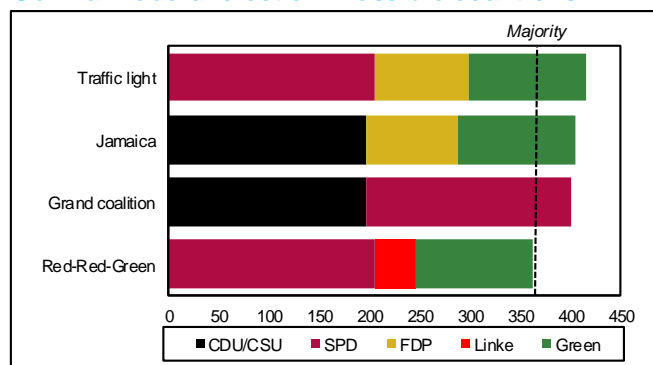
While both of the two establishment parties have said that they want to form the next government, only the SPD would appear to have a credible case. As well as having the largest share of the vote, it also has by some margin the most popular candidate for Chancellor in the shape of the centrist Olaf Scholz, a marked contrast to the hapless Armin Laschet of the CDU/CSU. Nevertheless, not least given the unviability of the Red-Red-Green combination, the Greens and FDP will have a strong position in the imminent coalition negotiations, able to play the two main parties against each other. Given the startling decline in the vote share of the CDU/CSU, however, it would seem extraordinary if it managed to scrape back into office this time around via a "Jamaica" alliance. Indeed, senior members of both parts of the centre-right Union have questioned their

German federal election: Bundestag seats*



*Preliminary result. Source: German Federal Returning Officer and Daiwa Capital Markets Europe Ltd.

German federal election: Possible coalitions*



*Preliminary result. Source: German Federal Returning Officer and Daiwa Capital Markets Europe Ltd.

legitimacy to govern following this result. So, we still see a Traffic-Light coalition of SPD, Greens and FDP as most likely to emerge as the next government, albeit perhaps not before next year. And while that might appear to represent a significant shift after 16 years of Merkel, given the influence of the FDP – whose leader Christian Lindner will want to demand a prominent economic portfolio in any new coalition – we still expect any reforms to emerge from the next government to be incremental rather radical. That might rule out significant tax rises. However, it need not preclude a significant increase in public investment to fund green projects, although such activity would seem more likely to end up off balance sheet.

Loans to NFCs still rising, but at a softer pace

While recent surveys point to a loss of vigour in the economic recovery, today's ECB monetary data were also a touch softer than of late, albeit remaining broadly consistent with ongoing economic growth. Encouragingly, the net flow of longer-dated loans was positive for an eighth successive month, albeit weaker than in recent months. Indeed, net new lending with a maturity of more than five years slowed to €4.6bn in August from an average of €22bn in the first seven months of the year. And so the annual growth in the stock of such loans eased 0.4ppt to a still-elevated 6.8%Y/Y. There was also a modest resumption in the net flow of loans with a maturity of up to 1 year, of €1.8bn in August. Nevertheless, having fallen by a cumulative €62bn in the previous three months when the surge in loans a year earlier rolled off balance sheets, the stock of such loans was still down 10.9%Y/Y. So overall, the net flow of new loans to NFCs reached €13bn in August, the most since March and a touch firmer than the average in the five years before the pandemic. This notwithstanding, the annual growth in the stock of loans to NFCs slowed a further 0.2ppt to 1.5%Y/Y, the softest pace since April 2016. Among the member states, the increase in lending last month was solely driven by Germany, with net flows in lending to NFCs in France, Italy and Spain negative.

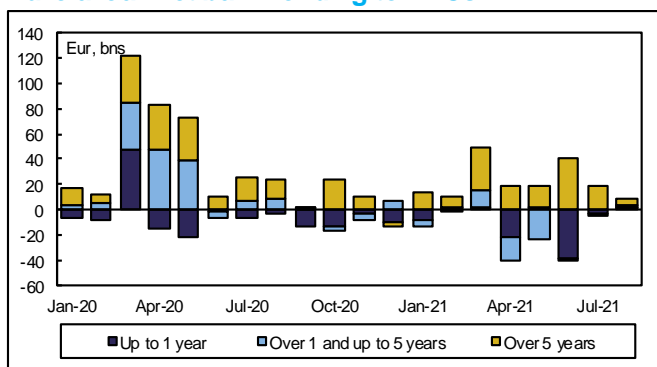
Consumer credit flat-lining as households increase their deposits

Bank lending to households remained solid in August, with the net flow moderating €8bn to €20bn, still above the pre-pandemic trend, to leave the annual growth rate steady at 4.2%Y/Y. But this was again underpinned by lending for house purchases, which was up a further €20bn in August, to leave the annual rate in the stock of such loans up 0.1ppt to 5.8%Y/Y, the highest since April 2008. In contrast, despite increased opportunities to spend, households took no additional consumer credit last month, to leave the annual growth of such loans at zero. Instead, households continued to accumulate bank deposits in August (€51bn), at almost double the average pace seen in the previous four months and more than twice the pre-pandemic norm. So, while the monthly increase was lower than that seen in the early stages of the pandemic, this left household deposits at almost €8.0trn in August. That is roughly €450bn more than would have been accumulated under the pre-pandemic trend, equating to excess saving worth more than 7% of annual household consumption. Deposits placed by NFCs also continued to rise at an above-average rate (€23bn) to €3.134trn.

The coming two days in the euro area

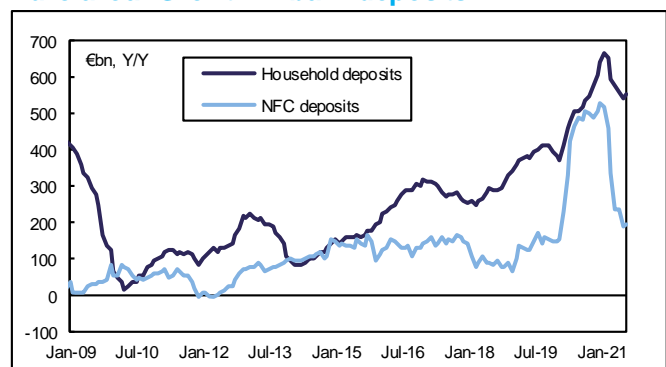
Following a relatively quiet day data-wise tomorrow, with just German and French consumer confidence surveys due to be published, Wednesday will bring the European Commission's comprehensive sentiment survey results. In line with last week's [flash PMIs](#), these will likely show that supply constraints are weighing further on business sentiment, with the headline Economic Sentiment Indicator expected to have edged lower in September for the second successive month, albeit remaining close to July's series high of 119.0. In contrast, the consumer confidence index is expected to confirm the surprise increase to a three-month high reported in the preliminary estimate. Meanwhile, the survey's indices of price expectations of consumers, retailers and industrial firms, are likely to remain elevated as the surge in energy prices and persistent supply shortages push costs higher. We will also get the first estimate of national CPI data for September with Spanish CPI numbers to be published on Wednesday. Market consensus sees the EU-harmonised CPI measure rising 0.3ppt to 3.6%Y/Y in September, the highest level in thirteen years. Aside from the data, focus will also be on the ECB's two-day Sintra monetary policy forum, which gets underway tomorrow. Most notable will be the concluding policy panel on Wednesday, which features the heads of the Fed, BoE and BoJ as well as the ECB.

Euro area: Net bank lending to NFCs



Source: ECB and Daiwa Capital Markets Europe Ltd.

Euro area: Growth in bank deposits



Source: Refinitiv, ECB and Daiwa Capital Markets Europe Ltd.



UK

The coming two days in the UK







After a quiet start to the week for UK economic data, Wednesday will bring the release of the BoE's lending data for August. Coinciding with the tapering of the government's stamp duty holiday, July brought only the second net mortgage repayment in the past decade, while the number of mortgage approvals – an indicator of future borrowing – similarly fell back to the lowest since July 2020. Wednesday's release of the BRC shop price index for September will be watched for any signs of upwards price pressures on the High Street.

The next edition of the Euro wrap-up will be published on 29th September 2021

European calendar

Today's results						
Economic data						
Country	Release	Period	Actual	Market consensus/ <u>Daiwa forecast</u>	Previous	Revised
Euro area 	M3 money supply Y/Y%	Aug	7.9	7.8	7.6	-
Spain 	PPI Y/Y%	Aug	18.0	-	15.3	15.6
Auctions						
Country	Auction					
- Nothing to report -						










Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

Tomorrow's releases						
Economic data						
Country	BST	Release	Period	Market consensus/ <u>Daiwa forecast</u>	Previous	
Germany 	07.00	GfK consumer confidence	Oct	-1.5	-1.2	
France 	07.45	Consumer confidence	Sep	100	99	
UK 	-	Nationwide house price index* M/M% (Y/Y%)	Sep	0.6 (10.7)	2.1 (11.0)	
Auctions and events						
Euro area 	13.00	ECB President Lagarde gives introductory speech at ECB Forum on Central Banking				
	13.30	ECB Vice Present de Guindos and board members Panetta and Schnabel each chair a session at the Forum				
UK 	10.00	Auction: £2bn of 1¼% 2051 bonds				






**Approximate date of release. Source: Bloomberg and Daiwa Capital Markets Europe Ltd.*

Wednesday's releases

Economic data

Country	BST	Release	Period	Market consensus/ <i>Daiwa forecast</i>	Previous
Euro area		10.00 European Commission's economic confidence	Sep	117.0	117.5
		10.00 European Commission's final consumer confidence	Sep	-4.0	-5.3
		10.00 European Commission's industrial (services) confidence	Sep	12.5 (16.4)	13.7 (16.8)
Italy		09.00 PPI Y/Y%	Aug	-	12.3
Spain		08.00 Preliminary CPI (EU-harmonised CPI) Y/Y%	Sep	3.5 (3.6)	3.3 (3.3)
UK		00.01 BRC shop price index Y/Y%	Sep	-	-0.8
		09.30 Net consumer credit £bn (Y/Y%)	Aug	0.3 (-)	0.0 (-2.7)
		09.30 Net mortgage lending £bn (mortgage approvals '000s)	Aug	3.5 (73.0)	-1.4 (75.2)
		09.30 M4 money supply Y/Y%	Aug	-	6.0

Auctions and events

Euro area		13.00 ECB Vice President de Guindos and board members Elderson and Lane each chair a session at the Forum
		16.45 US, UK, Japan and Euro area Central Bank Governors on policy panel discussion at ECB Forum on Central Banking
Germany		10.30 Auction: €4bn of 0% 2031 bonds
Italy		10.00 Auction: €2.5bn of 0.95% 2031 bonds
		10.00 Auction: €1.75bn of 2026 floating bonds

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

Access our research blog at:

<https://www.uk.daiwacm.com/ficc-research/recent-blogs>

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