

Euro wrap-up

Overview

- Bunds made modest losses despite another German survey flagging a deterioration in economic conditions due to supply chain disruption.
- Despite another upbeat UK labour market report, Gilts reversed some of their recent losses as spending surveys flagged warning confidence due to supply and price concerns.
- Tomorrow will bring euro area IP and UK GDP figures for August.

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Daily bond market movements

Bond	Yield	Change
BKO 0 09/23	-0.677	+0.012
OBL 0 10/26	-0.479	+0.029
DBR 0 08/31	-0.098	+0.025
UKT 0 ¹ / ₈ 01/24	0.553	-0.032
UKT 0 ³ / ₈ 10/26	0.773	-0.031
UKT 0 ¹ / ₄ 07/31	1.147	-0.040

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

Source: Bloomberg

Euro area

German ZEW signals further loss of confidence in economic outlook

Coming on the back of last week's disappointing [German output](#) release, today's ZEW survey signalled a further easing of investor confidence in the economic outlook due to the persistence of supply bottlenecks. In particular, the current situation balance fell for the first time since January and by a larger-than-expected 10.3pts in October, to 21.6. This, however, was merely the lowest level since July and remained considerably above the long-run average (-7.7). The index of expectations for the coming six months declined further too, down for a fifth successive month to 22.3 in October, the lowest since the initial wave of pandemic in March 2020, but nevertheless broadly in line with the long-run average. This in part reflected a weaker outlook for profit growth in sectors particularly impacted by supply shortages – i.e. autos, electronics, chemicals and pharmaceuticals. While associated supply constraints have seen costs rise substantially over recent months, investors' expectations for the inflation outlook remained well contained, with the relevant index slipping to a fifteen-month low. Nevertheless, against the backdrop of rising global bond yields and with the ECB set to slow the pace of asset purchases further in due course, the ZEW reported a further rise in the index for long-term interest rates, to its highest for three years.

The day ahead in the euro area

Tomorrow will bring euro area industrial production numbers for August. While IP in France grew solidly (1.0%M/M) and dropped only marginally in Italy and Spain, a sharp slump in German output (-4.1%M/M) combined with weakness in the Netherlands and Ireland, will lead to a notable decline in overall euro area IP. Based on national figures, we will likely see output fall 1.7%M/M, to leave it more than 2½% lower than the pre-pandemic level. Wednesday will also bring final German inflation for September, which is expected to confirm that headline CPI (on the harmonised measure) rose to series high above 4%Y/Y.

UK

UK labour market continues to strengthen, continuing to wave flags at the BoE

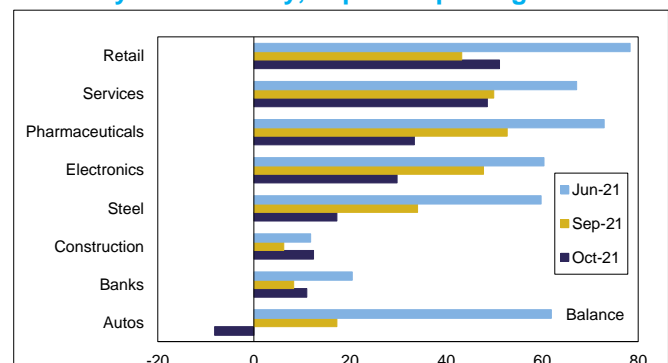
After some hawkish comments from several MPC members, including BoE Governor Bailey, over the past week flagging concerns about upside risks to the inflation outlook, today's UK labour market data and survey measures of household spending were inevitably closely watched. And the labour market report was once again a positive one, with further improvements in payrolls, vacancies and unemployment, while wage growth remained robust albeit moderating due to base

Germany: ZEW economic indicators*



*Dashed lines represent long-run average. Source: Refinitiv and Daiwa Capital Markets Europe Ltd.

Germany: ZEW survey, expected profit growth



Source: Refinitiv and Daiwa Capital Markets Europe Ltd.

effects. In particular, following a cumulative increase of 690k between April and August, the number of payrolled employees rose an additional 207k in September, the most during the current cycle, to 29.2mn, marking a rise of 3.6% compared with a year earlier and 0.4% (122k) compared with the pre-pandemic level. Once again, the biggest increases in payrolls were seen in those sectors that had previously been most acutely impacted by the pandemic – e.g. accommodation and food services, arts and entertainment, and wholesale and retail.

Job vacancy-to-worker ratio at highest on record

Consistent with labour and skill shortages, the number of vacancies in the UK in September maintained a firm upwards trend too, above 1mn for a third successive month, with 12 out of 18 sectors reporting record vacancies in the past quarter. Unsurprisingly, given clear evidence of ongoing staff shortages in the haulage sector, the strongest growth in vacancies in Q3 was reported in transport and storage (56%Q/Q or 18.5k), while the retail and hospitality sectors also reported an extremely strong increase in the number of vacancies, by a cumulative 60k. Indeed, the highest ratio of vacancies per 100 employee jobs was in the accommodation and food services industry at 5.9%, compared with an overall ratio of 3.7% which itself was a record high. Among other indicators, the number of hours worked surged in the three months to August (albeit remaining almost 3% below the pre-pandemic level), while the unemployment rate dropped 0.3ppt over the previous three months to 4.5%, down 0.7ppt from the pandemic peak at end-2020, albeit still 0.5ppt (146k) above the pre-pandemic trough. And the inactivity rate (for workers aged 16-64 years) dropped 0.2ppt from the previous quarter to 21.1%, still some 0.9ppt (346k) above the level before the outbreak of Covid.

Headline wage growth moderated, but underlying growth range revised higher

Notwithstanding the strong uptrend in jobs, wage growth moderated somewhat, with average weekly earnings slowing by a further 1.1ppt to 7.2%Y/Y in the three months to August. Excluding bonuses, growth in earnings also moderated 0.8ppt to 6.0%3M/Y. That, however, appears principally to reflect base effects from the declines a year earlier. Given the fading impact of the pandemic and related compositional effects, including the drop in the number of workers on furlough and increased working hours, underlying wage growth – which is so important for the BoE as it tries to gauge the extent of domestically generated price pressures – has been especially difficult to interpret over recent quarters. Looking through the various distortions, the ONS estimates that underlying earnings growth might be somewhere between 4.1-5.6%Y/Y, with the range revised 0.5ppt higher than a month ago. By reference, the peak in pay growth 2019 ahead of the pandemic was 3.9%Y/Y. While it will come to its own view, the BoE also seems highly likely to judge that core wage growth has picked up over recent months and is now above pre-pandemic levels.

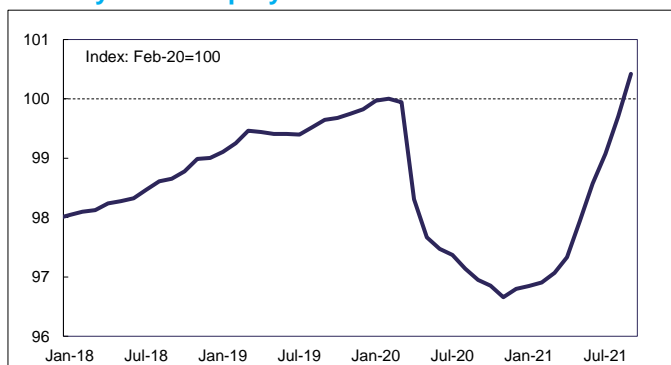
BRC survey suggests that UK retail sales growth moderated further in September

Despite ongoing improvements in the labour market, today's BRC retail sales monitor again reported slowing recovery momentum in the retail sector, with signs that waning consumer confidence, due not least to supply concerns and rising prices, was starting to weigh on demand for larger purchases. Overall, the BRC measure of headline sales growth on the High Street eased in September by 2.4ppts to 0.6%Y/Y, the softest pace since January's lockdown. And on a like-for-like basis, sales were down compared with a year earlier (-0.6%Y/Y), the first negative reading since March 2020. With the exception of clothing – boosted by the return to school and workplaces for many for the first time in eighteen months – the BRC reported that sales fell back across every major category.

Credit card spending boosted as consumers panic-bought and increased spending on socialising

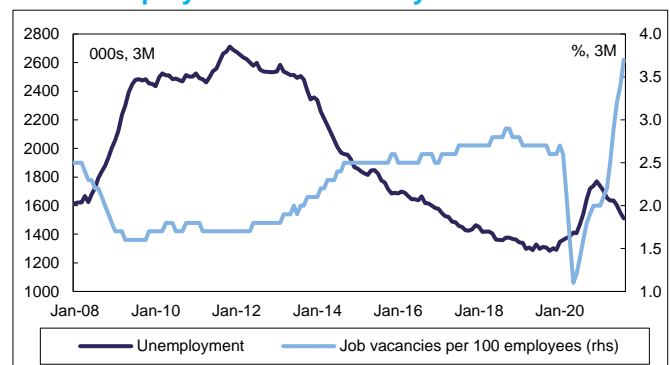
In contrast, today's Barclaycard spending report suggested strong total spending growth last month due not least to panic buying as the UK's supply crisis triggered extra expenditure on fuel. Indeed, spending on essentials on the Barclaycard measure was up 14.4% compared with September 2019. At the same time, tallying with the BRC survey, the Barclaycard

UK: Payrolled employees



Source: ONS and Daiwa Capital Markets Europe Ltd.

UK: Unemployment and vacancy ratio



Source: Refinitiv and Daiwa Capital Markets Europe Ltd.

data suggested softer spending growth on non-essentials. But it also implied increased social spending, with a surge in spending at eating and drinking establishments attributed in part to a more significant return to the office. Against the backdrop of ongoing supply chain shortages and rising food and energy prices, we expect to see a further moderation in discretionary spending over coming months. Certainly, Barclaycard and the BRC today cited a worsening in consumer confidence at the end of the third quarter, with Barclaycard noting that 90% of surveyed customers were concerned about their household finances on the back of higher prices, while the share of Brits who felt confident in their ability to buy non-essential items fell 4ppts in September to 59%, the smallest since February.

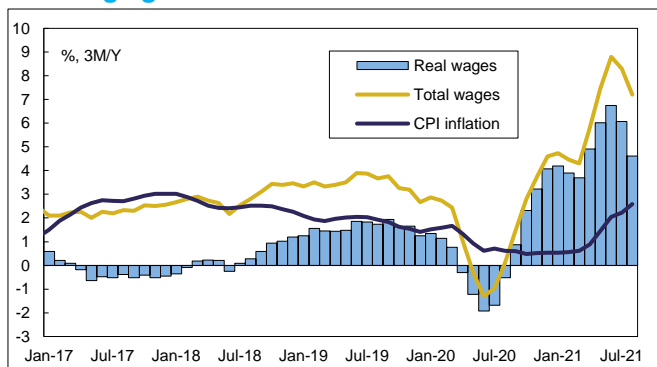
Hawkish MPC comments trigger a sharp rise in BoE rate hike expectations

Despite clear downside risks to growth over the near term, and having acknowledged that the economic recovery from the pandemic still had some distance to being fully realized, BoE Governor Bailey at the weekend appeared to start laying the groundwork for imminent tightening, warning of the need to act to prevent above-target inflation becoming permanently embedded. While the MPC had recently flagged greater uncertainties about the outlook for the labour market – not least given the conclusion of the government job support schemes last month, of which the CJRS was still supporting 1.3mn employees at the start of the month – Bailey thought that a pickup in unemployment over the near term was now unlikely, a view that was seemingly supported by the record high vacancy-to-employee ratio in today's figures. Meanwhile, external MPC member Saunders – who was one of two members voting last month to bring the BoE's net asset purchases to an early conclusion – judged that investors were right to have brought forward their expectations on rate hikes. Speeches by other MPC members this week, from Deputy Governor Cunliffe (tomorrow) and the up-to-now dovish externals Tenreyro and Mann on Thursday will of course be closely watched. But there is certainly a non-negligible chance of a 15bps hike in Bank Rate (to 0.25%) at next month's MPC meeting, when the BoE will update its economic forecasts. And if that hike is not forthcoming, a clear signal of the likelihood of a hike before year-end might now seem more likely than not.

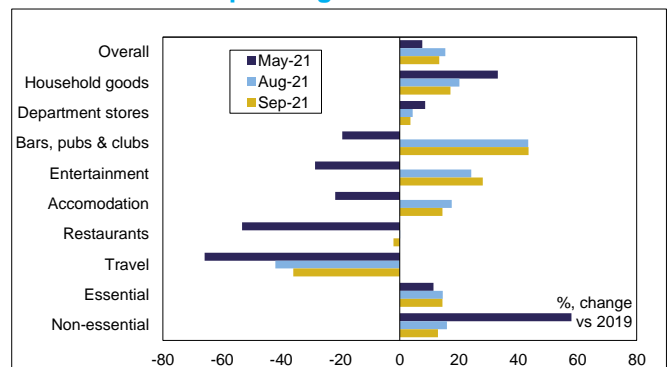
The day ahead in the UK

Wednesday's UK GDP data for August will also provide key insights for MPC members. Having moved broadly sideways at the start of the third quarter, GDP is expected to have been boosted by a pickup in services activity as hospitality was supported by "staycations". Manufacturing and construction output, however, seem likely to have been constrained by persistent supply bottlenecks. Overall, GDP is likely to have risen by around ½%M/M, which would leave the level of output 0.4% below the pre-pandemic level. The latest goods trade figures for August will also be published on Wednesday, while BoE Deputy Governor Cunliffe is due to give a pre-recorded speech at a global finance conference.

UK: Wage growth









UK: Credit card spending*





European calendar

Today's results

Economic data

Country	Release	Period	Actual	Market consensus/ <i>Daiwa forecast</i>	Previous	Revised
Germany	 ZEW current situation (expectations) balance	Oct	21.6 (22.3)	-	31.9 (26.5)	-
UK	 BRC sales, like-for-like Y/Y%	Sep	-0.6	-	1.5	-
	 Unemployment claimant count rate % (change '000s)	Sep	5.2 (-51.1)	-	5.4 (-58.6)	- (-88.0)
	 Average earnings including bonuses (excluding bonuses) 3M/Y%	Aug	7.2 (6.0)	7.0 (6.0)	8.3 (6.8)	-
	 ILO unemployment rate 3M%	Aug	4.5	4.5	4.6	-
	 Employment change 3M/3M, '000s	Aug	235	-	183	-



Auctions

Country	Auction
Germany	 sold €3.92bn of 0% 2023 bonds at an average yield of -0.69%
UK	 sold £1.25bn of 0.5% 2061 bonds at an average yield of 1.414%

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

Yesterday's results

Economic data

Country	Release	Period	Actual	Market consensus/ <i>Daiwa forecast</i>	Previous	Revised
France	 Bank of France industrial sentiment survey	Sep	100	103	104	103
Italy	 Industrial production M/M% (Y/Y%)	Aug	0.2 (0.0)	-0.2 (-0.3)	0.8 (7.0)	1.0 (7.2)


Auctions

Country	Auction
- Nothing to report -	

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

Friday's results

Economic data

Country	Release	Period	Actual	Market consensus/ <i>Daiwa forecast</i>	Previous	Revised
Germany	 Trade balance €bn	Aug	10.7	15.5	18.1	17.9









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/ <i>Daiwa forecast</i>	Previous
Euro area		10.00 Industrial production M/M% (Y/Y%)	Aug	-2.0 (3.0)	1.5 (7.7)
Germany		07.00 Final CPI (EU-harmonised) Y/Y%	Sep	4.1 (4.1)	3.9 (3.4)
UK		07.00 Monthly GDP M/M% (3M/3M%)	Aug	<u>0.5 (3.0)</u>	0.1 (3.6)
		07.00 Industrial production M/M% (Y/Y%)	Aug	0.2 (3.3)	1.2 (3.8)
		07.00 Manufacturing production M/M% (Y/Y%)	Aug	0.0 (4.1)	0.0 (6.0)
		07.00 Index of services M/M% (3M/3M%)	Aug	0.6 (3.8)	0.0 (4.5)
		07.00 Construction output M/M% (Y/Y%)	Aug	0.4 (5.7)	-1.6 (8.6)
		07.00 Goods trade balance £bn	Aug	-12.0	-12.7

Auctions and events

Germany		10.30 Auction: €1bn of 0% 2052 bonds
Italy		10.00 Auction: up to €3bn of 0% 2024 bonds
		10.00 Auction: up to €2bn of 0.5% 2028 bonds
		10.00 Auction: up to €1.5bn of 1.7% 2051 bonds
UK		10.00 Auction: £500mn of 0.125% 2051 index-linked bonds
		15.30 BoE Deputy Governor Cunliffe gives a pre-recorded speech at SWIFT's global financial services networking event

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

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