

Euro wrap-up

Overview

- Despite a slight deterioration in euro area consumer confidence, Bunds made further losses while French business confidence remained upbeat.
- Gilts made further significant losses as a UK manufacturing survey signalled intensified price pressures.
- Friday will bring the October flash PMIs and updates on UK retail sales and consumer confidence.

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Daily bond market movements

Bond	Yield	Change
BKO 0 09/23	-0.651	+0.020
OBL 0 10/26	-0.430	+0.048
DBR 0 08/31	-0.092	+0.037
UKT 0 ¹ / ₈ 01/24	0.710	+0.045
UKT 0 ³ / ₈ 10/26	0.871	+0.060
UKT 0 ¹ / ₂ 07/31	1.214	+0.071

*Change from close as at 4:00pm BST.
Source: Bloomberg

Euro area

Consumer sentiment softens at start of Q4

Ahead of tomorrow's flash PMIs, today brought some initial insights into consumer and business sentiment at the start of Q4. Having registered a surprising improvement in September, the Commission's flash euro area consumer confidence indicator dropped in October. But the decline (of 0.8pt to -4.8) was moderate and close to expectations, and left the index still above August's level and close to the average of the past six months. So, it does not signal a notable slowing of consumer spending. While there was no survey detail published with today's flash estimate, the deterioration in consumer sentiment seems likely to reflect increasing concerns about inflation, not least related to household essentials such as energy and food bills.

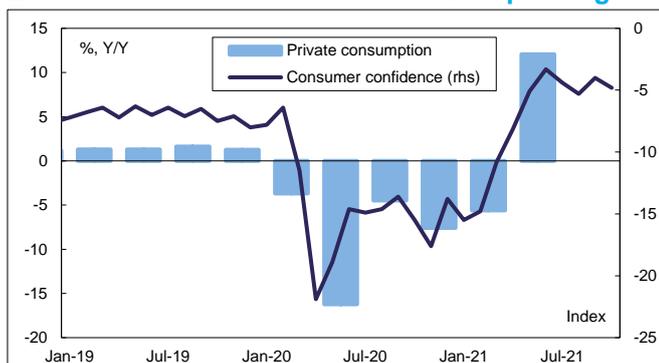
French service sector firms upbeat, manufacturing sentiment stable

In contrast to the euro area consumer survey, today's French INSEE business survey surprised on the upside, suggesting a more favourable outlook at the start of Q4, which might also be reflected in tomorrow's flash PMIs. In particular, the headline confidence index rose 2pts to 113 in October, matching the multi-year high reached in June, well above the pre-crisis reading and significantly higher than the long-run average. While the assessment of the business climate remains well above the long-run averages across the main subsectors, the improvement in October was principally driven by the services sector, for which increased optimism regarding the outlook pushed the headline confidence index to the highest since 2000. Conditions reportedly remained stable in manufacturing, although firms continued to report disruption to past and expected future production due to supply constraints. Indeed, roughly half of respondent manufacturers flagged that production has been limited by difficulties sourcing inputs, the most since the series began in the early 1990s. Unsurprisingly, problems remained most acute in the transport equipment sector, where three-quarters of firms were reportedly affected. Material shortages remained a constraint in the construction sector too, and firms across all sectors reported growing difficulties recruiting. In addition, with input costs remaining elevated, firms expect to raise selling prices further over coming months too.

The day ahead in the euro area

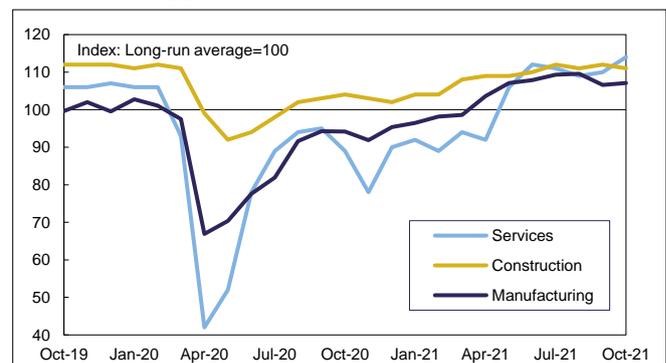
The focus tomorrow will be on the release of the flash euro area PMIs for October, which are expected to reveal that ongoing and widespread supply bottlenecks weighed further on business sentiment, with the headline output PMIs likely to have fallen further. Nevertheless, not least given the ongoing recovery in services, the composite output indices for the member states are expected to remain comfortably above the key 50-mark, therefore signaling only a moderate loss of recovery momentum rather than contraction. Indeed, the headline euro area composite PMI is forecast to have fallen 1pt to 55.2 in October, the lowest level in six months.

Euro area: Consumer confidence and spending



Source: Refinitiv and Daiwa Capital Markets Europe Ltd.

France: INSEE business confidence indices



Source: Refinitiv and Daiwa Capital Markets Europe Ltd.

UK

UK public borrowing still trending well below OBR forecast leaving fiscal room for manoeuvre

Every month of this fiscal year UK public borrowing has significantly undershot the OBR's forecast. And that remained the case with the September figures. In particular, net public sector borrowing (PSNB) excluding banks came in at £21.8bn last month, £7.0bn less than the same month a year ago and more than £4bn below the OBR's March forecast. The improvement from a year earlier came predominantly on the revenue side, as personal income tax receipts rebounded particularly vigorously in response to higher wage and jobs growth amid stronger-than-expected GDP growth. Indeed, the level of GDP in August was about 4% above that predicted by the OBR. In addition, public spending also failed to rise quite as much as had been expected. Given the September figure, as well as some favourable revisions to prior months, cumulative public sector net borrowing in the first six months of the fiscal year reached £108.1bn, barely more than half the level in the first half of the last financial year and about 30% less than the OBR's forecast for the period. And currently, full-year borrowing looks on track to come in close to £200bn, some £34bn below the OBR's forecast. So, at next week's Budget and Spending Review announcements, the OBR will certainly revise down its projection for public borrowing. However, the Government asked the OBR to base its economic forecasts on GDP data that were published before the most recent significant upwards revisions. And the OBR is unlikely to revise its pessimistic view of the likely level of scarring from the pandemic. So, its projections are still unlikely to reveal the full scope for relaxation of the Government's fiscal plans until next year's Budget. At that point, the Chancellor is likely to offer the prospect of a moderation in the planned tightening of the fiscal stance from FY23 on, including some politically motivated giveaways ahead of the next election.

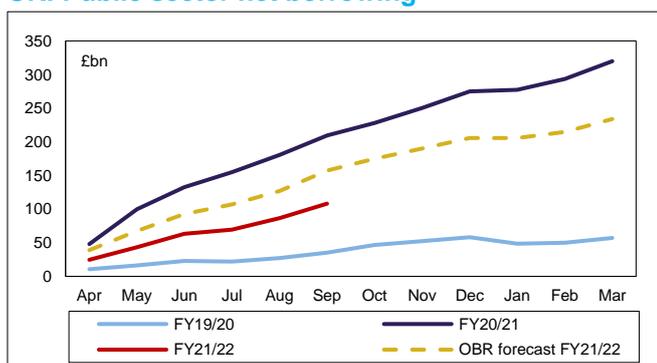
Manufacturers bemoan supply constraints, signal record selling price expectations

Ahead of tomorrow's flash PMIs, today's CBI industrial trends survey suggested that conditions remained challenging in the UK's manufacturing sector at the start of Q4. Admittedly, the headline indices suggested that positive output growth was maintained in the three months to October, with 11 out of 17 subsectors reporting an increase compared with a year ago. But there was a notable drop in the survey's orders indicator, which like the relevant production index was at its lowest since April, with persistent weakness reported in overseas orders in particular. And while manufacturers looked forward to growth in production over the coming three months, this was somewhat at odds with the marked decline in business optimism over the quarter. Indeed, almost two-thirds of firms cited the availability of materials as a factor likely to constrain output over the coming quarter, while there were also heightened concerns about labour shortages, related to a lack of skilled workers and available candidates. Against this backdrop, manufacturers continued to report significant price pressures, and expected domestic price inflation to accelerate further over the coming three months. Indeed, the selling price expectations index rose in October to the highest on the series dating back more than 30 years.

The day ahead in the UK

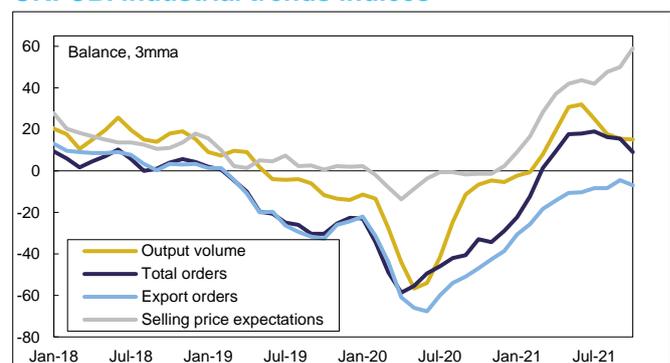
A busy end to the week for top-tier UK economic data includes September retail sales figures, the latest consumer confidence report and preliminary PMI surveys. The retail sales figures will also be closely watched for further signs of a slowdown in recovery momentum. However, sales at petrol stations will have been boosted significantly by the fuel crisis towards the end of the month, which saw widespread panic-buying of petrol amid reports of disruption to supplies. As such, total sales are expected to have risen 0.6% on the month, after falling 0.9% M/M in August, albeit leaving them 0.4% lower compared to a year earlier. Meanwhile, the latest GfK consumer confidence survey seems likely to highlight increasing concerns not least about rising prices, while the preliminary October PMIs are also expected to flag persistently high price pressures against the backdrop of supply bottlenecks. And with firms also expected to report labour shortages, as well as softer demand, the output PMIs, for both manufacturing and services, are likely to have fallen somewhat at the start of the fourth quarter, albeit remaining above the key-50 expansion level. Indeed, the UK's composite PMI is expected to edge down to 54.0 in October, from 54.9 previously, marking the lowest level in eight months.

UK: Public sector net borrowing



Source: ONS and Daiwa Capital Markets Europe Ltd.

UK: CBI industrial trends indices



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
Euro area	European Commission's preliminary consumer confidence	Oct	-4.8	-5.0	-4.0	-
France	INSEE business confidence	Oct	113	110	111	-
	INSEE manufacturing confidence (production outlook)	Oct	107 (21)	105 (17)	106 (23)	107 (22)
UK	Public sector net borrowing, excl. banks £bn	Sep	21.8	22.6	20.0	16.8
	CBI industrial trends, total orders (selling prices)	Oct	9 (59)	17 (40)	22 (41)	-

Auctions

Country	Auction
France	sold €3.20bn of 0% 2025 bonds at an average yield of -0.5%
	sold €2.61bn of 1% 2025 bonds at an average yield of -0.44%
	sold €1.69bn of 0.5% 2026 bonds at an average yield of -0.38%
	sold €299mn of 0.1% 2032 index-linked bonds at an average yield of -1.392%
	sold €625mn of 0.1% 2047 index-linked bonds at an average yield of -1.192%
	sold €824mn of 0.1% 2026 index-linked bonds at an average yield of -2.29%
Spain	sold €3.37bn of 0% 2027 bonds at an average yield of -0.089%
	sold €1.68bn of 0.85% 2037 bonds at an average yield of 0.942%

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	09.00	Preliminary manufacturing (services) PMI	Oct	57.1 (55.4)	58.6 (56.4)
	09.00	Preliminary composite PMI	Oct	55.2	56.2
Germany	08.30	Preliminary manufacturing (services) PMI	Oct	56.6 (55.2)	58.4 (56.2)
	08.30	Preliminary composite PMI	Oct	54.3	55.5
France	08.15	Preliminary manufacturing (services) PMI	Oct	54.0 (55.5)	55.0 (56.2)
	08.15	Preliminary composite PMI	Oct	54.7	55.3
UK	00.01	GfK consumer confidence	Oct	-16	-13
	07.00	Retail sales including auto fuels M/M% (Y/Y%)	Sep	0.6 (-0.4)	-0.9 (0.0)
	07.00	Retail sales excluding auto fuels M/M% (Y/Y%)	Sep	0.3 (-1.6)	-1.2 (-0.9)
	09.30	Preliminary manufacturing (services) PMI	Oct	56.0 (54.5)	57.1 (55.4)
	09.30	Preliminary composite PMI	Oct	54.0	54.9

Auctions and events

Euro area	09.00	ECB's survey of professional forecasters
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Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

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