

Euro wrap-up

Overview

- Bunds rallied as risk appetite fell following the attacks by Hamas on Israel, and German industrial production fell for a fourth successive month.
- Gilts also made significant gains on a quiet day for UK economic news.
- Tuesday will bring Italian IP data and the results of a UK retail survey, while Wednesday will bring updates on German inflation, euro area consumer expectations, and the UK labour market.

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Daily bond market movements

Bond	Yield	Change
BKO 3.1 09/25	3.019	-0.104
OBL 2.4 10/28	2.628	-0.124
DBR 2.6 08/33	2.763	-0.118
UKT 3½ 10/25	4.834	-0.047
UKT 4½ 06/28	4.474	-0.097
UKT 3¼ 01/33	4.478	-0.096

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

Euro area

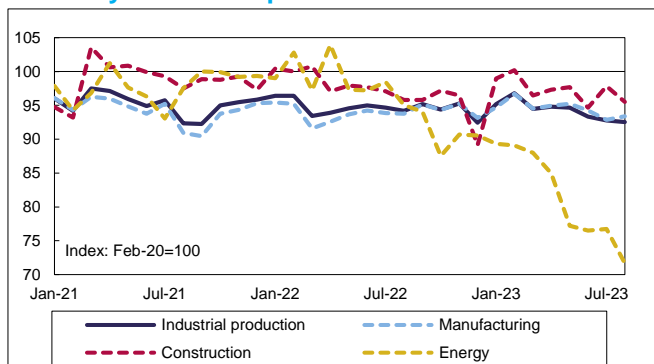
German IP falls for the fourth successive month, with construction and energy output weaker

Today's German industrial production data for August broadly aligned with expectations, maintaining a downtrend and thus illustrating the malaise in the euro area's largest member state. In particular, overall output fell for a fourth consecutive month, by 0.2%M/M, to leave it down 1.9%3M/3M and 1.7%Y/Y to be still some 7½% below the pre-pandemic benchmark. Admittedly, the weakness was led by a steep drop in energy production (-6.6%M/M), which marked the eighth fall in the sub-sector out of the past nine months – a period which saw the final shuttering of German's nuclear reactors – to be down almost 25%Y/Y and at the lowest level since reunification. Moreover, construction activity also fell back (-2.4%M/M), partially reversing the rise in July to be trending broadly sideways so far in Q3 compared with Q2. It was therefore a source of some relief that manufacturing production increased for the first month in three, by 0.5%M/M to leave it down just 0.4%Y/Y. That, however, still left it down more than 6½% compared with the February 2020 level and trending some 1.7% below the Q2 average to suggest that the factory sector will provide a non-negligible drag on GDP growth in Q3.

Auto production jumps while energy-intensive output edges higher from low level

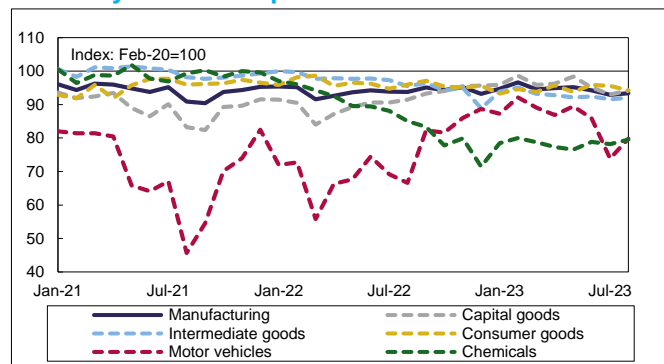
Within the manufacturing detail, growth was supported by an acceleration in car production of 8.0%M/M. However, this followed a cumulative decline of more than 17% over the previous two months, which reflected summer maintenance shutdowns, to leave it some 12% below the Q2 average and roughly 20% below the pre-pandemic level. Meanwhile, production in the energy-intensive sector rose for a second month out of the past three, by 0.9%M/M, albeit leaving it trending sideways over Q3 so far. The improvement in this category in August reflected a pickup in production of coke and petroleum, basic metals and chemicals, with the latter to a six-month high. But the downtrend in glassware was maintained, with output in the subsector falling to a new re-unification low and almost 24% below the level ahead of Russia's invasion of Ukraine. With business gas usage in August still almost 20% below the average for the month between 2018 and 2021, energy-intensive production was similarly still almost 20% below the pre-pandemic level. Finally, while overall output of capital and intermediate goods was higher in August, production of consumer items fell for a second successive month and by 1.4%M/M. And each of these major categories was still trending lower in the first two months of Q3. Nevertheless, looking ahead, survey indicators – including the PMIs and ifo institute business climate indices – suggest that the trough in Germany's manufacturing downturn might have been reached. Last week's factory orders data also suggested some stabilisation. And truck toll mileage figures rose for the second month in three in September (0.4%M/M) suggesting a pickup in production over the near term too.

Germany: Industrial production



Source: Refinitiv Datastream and Daiwa Capital Markets Europe Ltd.

Germany: Industrial production



Source: Refinitiv Datastream and Daiwa Capital Markets Europe Ltd.

Services activity rose at the start of Q3 to help offset manufacturing weakness

While Germany's industrial sector continues to struggle, services sales started the third quarter on the front foot. In particular, activity rose 0.8%M/M to be up 5.7%Y/Y and 1% higher than the Q2 average. The pickup was relatively broad-based, supported not least by strong growth in sales in professional, scientific and technical services, as well as transport and warehousing, real estate and catering. And while accommodation services sales fell back in July, this appears to have represented payback for exceptionally strong growth in the previous two months. Admittedly, today's ifo retail survey results suggested that sentiment deteriorated in the sector in September, as retailers of personal and household goods, as well as DIY stores and furniture outlets, flagged subdued demand. But retailers of computers and software, as well as car dealerships, assessed their current situations as relatively good. Moreover, firms on the whole were a touch less pessimistic about the near-term outlook amid the recent improvement in households' disposable incomes and high level of employment. And so, while German GDP almost certainly contracted in Q3 and might well do so again in Q4, services activity should at least have limited the decline last quarter.

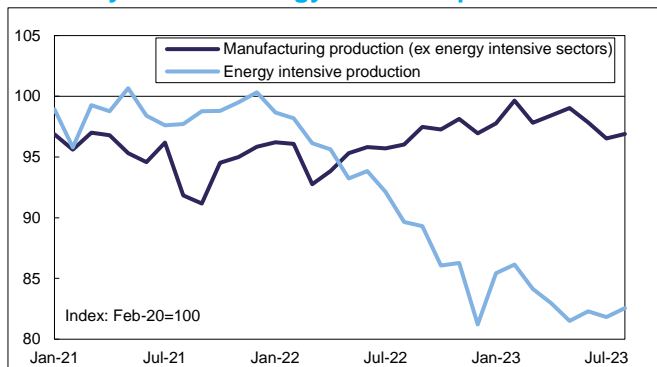
While on track for Q3 decline, Irish production rises in August

Among the other large manufacturing member states, production in August dropped 0.3%M/M in France and 1.1%M/M in Spain. However, in Ireland, where swings in output can be often very large and thus make a significant impact on the aggregate euro area figure, industrial production rebounded 6.1%M/M that month following a drop of 9.0%M/M in July. But the rise in manufacturing output was a more modest 1.3%M/M in August and followed a steep fall of 28.6%M/M the prior month. While that left it down a modest 0.5%3M/3M, the average level of Irish manufacturing output in the first two months of Q3 was more than 20% below the Q2 average. So, a marked drop seems likely over the third quarter as a whole despite the likelihood of further positive growth in September. Nevertheless, given the increases on the month in Ireland and Germany, euro area industrial production (excluding construction), data for which are due on Friday, appears to have grown modestly (by less than ½%M/M) in August.

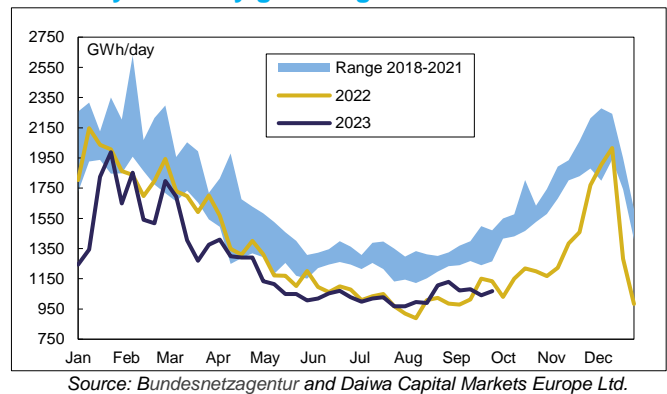
The coming two days in the euro area

Tomorrow brings the release of Italian IP data for August, which are expected to reveal that output fell a modest 0.3%M/M after declining 0.7%M/M in July, leaving output 2.0% lower compared to a year earlier. The focus on Wednesday will be the release of the ECB's monthly consumer survey, which will provide an update on households' price, income, spending and economic growth expectations in August. In July, the median forecast for inflation expectations 12 months ahead moved sideways at 3.4%Y/Y, with expectations three years ahead nudged slightly higher to 2.4%Y/Y. Also to be published that day

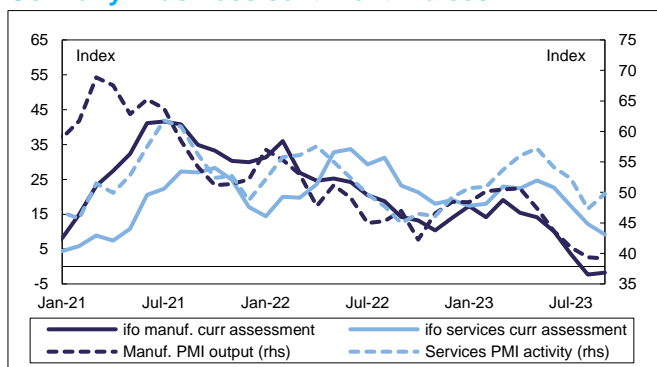
Germany: Total & energy-intensive production



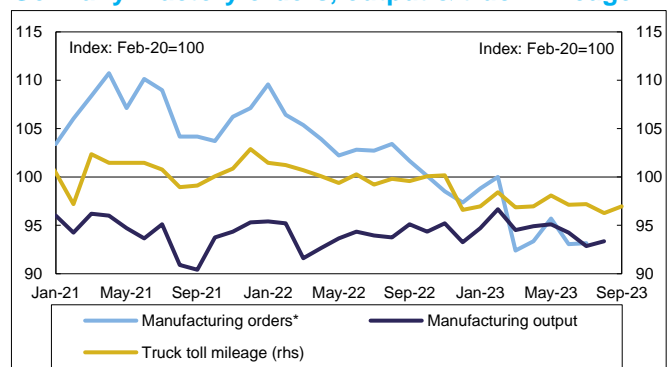
Germany: Industry gas usage



Germany: Business sentiment indices



Germany: Factory orders, output & truck mileage



*Orders excluding major items. Source: Refinitiv Datastream and Daiwa Capital Markets Europe Ltd.

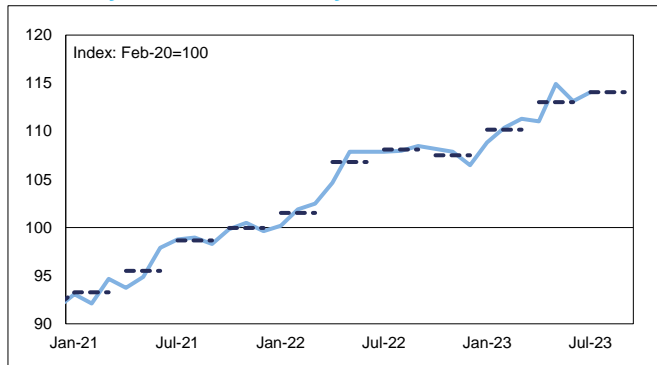
are updated German inflation figures for September, which will provide greater granularity on the flash estimates, which saw the EU-harmonised HICP rate drop 2.1ppts to a two-year-low of 4.3%Y/Y.

UK

The coming two days in the UK

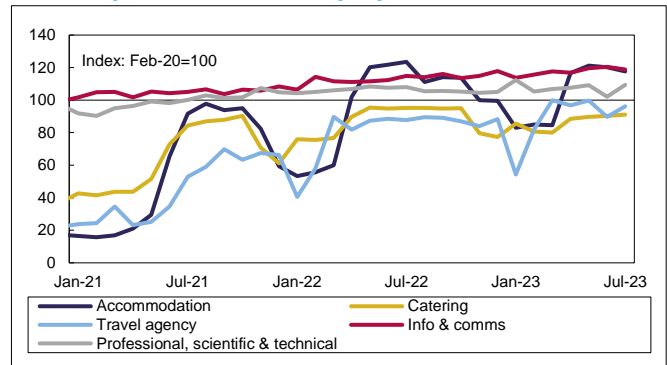
The coming two days are relatively quiet on the UK economic data front, with no headline releases scheduled. We will, however, get the release of the BRC retail sales monitor tomorrow, which will provide an update on demand on the high street at the end of the third quarter. On Wednesday, the latest REC report on jobs will likely point to a further loosening in the labour market in September, reflecting lacklustre economic momentum. In August, the survey suggested that, amid falling job vacancies, permanent placements fell by the most since the early stages of the pandemic. As such, while still historically elevated, the survey's measure of permanent starting salaries moderated to its lowest since April 2021 signaling the likelihood of a slowdown in average labour earnings over coming months.

Germany: Services activity*



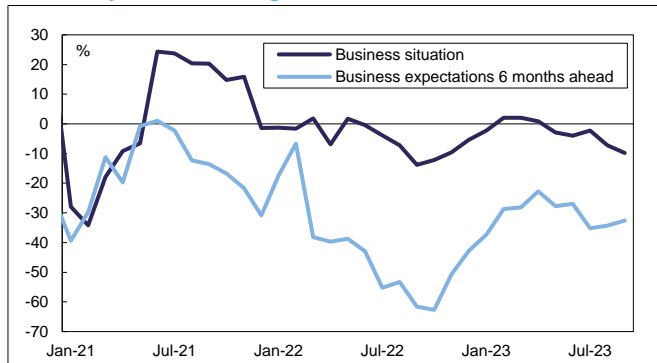
*Dashed line represents quarterly average. Source: Destatis and Daiwa Capital Markets Europe Ltd.

Germany: Services activity by selected sector



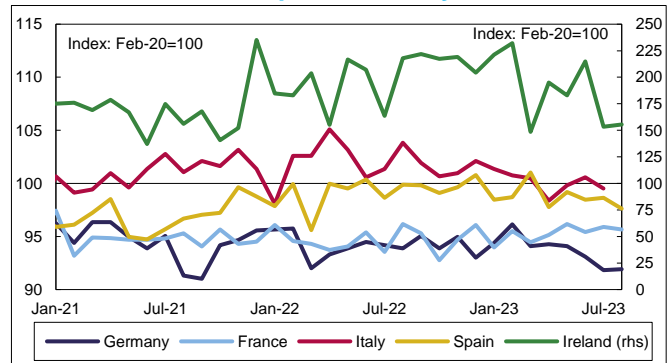
Source: Macrobond and Daiwa Capital Markets Europe Ltd.

Germany: Ifo retailing sentiment indices



Source: Macrobond and Daiwa Capital Markets Europe Ltd.

Euro area: Industrial production by member state





Source: Refinitiv Datastream and Daiwa Capital Markets Europe Ltd.

The next edition of the Euro wrap-up will be published 11 October 2023

European calendar

Today's results

Economic data

Country	Release	Period	Actual	Market consensus/ <i>Daiwa forecast</i>	Previous	Revised
Euro area	 Sentix investor confidence index	Oct	-21.9	-24.0	-21.5	-
Germany	 Industrial production M/M% (Y/Y%)	Aug	-0.2 (-2.0)	<u>-0.2 (-2.0)</u>	-0.8 (-2.1)	-0.6 (-1.7)



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
Italy		09.00 Industrial production M/M% (Y/Y%)	Aug	-0.3 (-5.0)	-0.7 (-2.1)
UK		00.01 BRC retail sales monitor, like-for-like sales Y/Y%	Sep	-	4.3



Auctions and events

Euro area		- 10-13 th - Various ECB board members speaking at IMF/World Bank conference, including President Lagarde
Germany		10.30 Auction: 0.10% 2033 index-linked bonds
		10.30 Auction: 0.10% 2046 index-linked bonds
UK		10.00 Auction: £900mn 0.125% 2039 index-linked bonds





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		09.00 ECB 1Y (3Y) CPI expectations Y/Y%	Aug	-(2.5)	3.4 (2.4)
Germany		07.00 Final HICP (CPI) Y/Y%	Sep	<u>4.3 (4.5)</u>	6.4 (6.1)

Auctions and events

Germany		10.30 Auction: €1.0bn of 2048 bonds
		10.30 Auction: €1.5bn of 2052 bonds
UK		00.01 REC report on jobs
		10.30 Auction: £3.75bn of 4.625% 2034 bonds

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

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