

Euro wrap-up

Overview

- Bunds made losses, while OATs outperformed, after far-right leader Le Pen suggested that the French budget could be passed soon, conditional on a more gradual pace of fiscal consolidation.
- Gilts made moderate losses as a BoE survey signalled that firms would look to pass on some new budget-related costs to higher prices, while also squeezing profit margins and wage growth.
- Friday will bring October's German IP figures and the expenditure breakdown for Q3 euro area GDP.

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Daily bond market movements

Bond	Yield	Change
BKO 2 12/26	1.998	+0.055
OBL 2½ 10/29	1.974	+0.060
DBR 2.6 08/34	2.103	+0.046
UKT 4½ 01/27	4.256	+0.030
UKT 4½ 07/29	4.132	+0.028
UKT 4½ 07/34	4.269	+0.023

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

Euro area

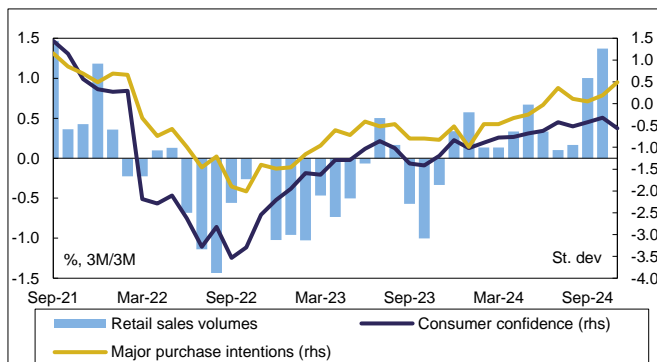
Retail sales soften in October after surprisingly firm Q3

Euro area retail sales volumes were surprisingly strong in Q3, rising for the fourth successive quarter and by 1.0%Q/Q, the most in more than three years. Having grown in each of the prior three months, it was not a significant surprise that sales volumes slipped back in October. And the fall of 0.5%M/M left them still 0.2% above the Q3 average. With prices slightly higher on the month, retail sales values dropped 0.3%M/M, similarly representing the first decline in four months. While food sales volumes ticked higher at the start of Q4, the other major categories declined. Core (i.e. ex-fuel and ex-food) sales volumes were down 0.9%M/M but were also still 0.3% above the Q3 average. And while auto fuel sales were down for a second successive month and by 0.3%M/M, that left them trending little changed from Q3. Among the member states, German retail sales volumes also fell back in October (-1.4%M/M) following three successive months of decent growth. And sales in France and Spain were flat on the month, but also still consistent with an ongoing uptrend. Perhaps in large part due to increased political uncertainty, the Commission's euro area consumer confidence index deteriorated to a five-month low in November, with household expectations for the economic outlook down to a 13-month low. However, the survey's index of major purchase intentions over the coming 12 months rose to the highest since the Russian invasion of Ukraine. So, with real disposable income growth also expected to remain firmly positive, we expect retail sales and overall household consumption to continue to expand over Q4 and into the New Year.

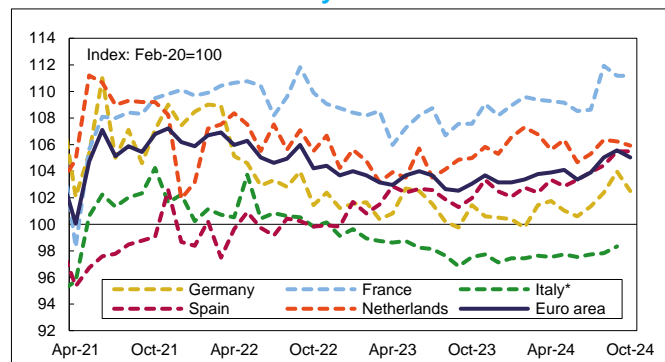
German orders boosted by major items, but core orders remain very subdued

While German manufacturing output fell in Q3 to its lowest level since the global financial crisis outside of the first Covid-19 lockdown, a large increase in factory orders in September raised some tentative hopes that the bottom in the manufacturing downturn might have been reached. And despite some inevitable payback at the start of Q4, today's data showed new orders falling a smaller-than-expected 1.5%M/M in October, to be 1.2% above the Q3 average and arguably suggestive of a somewhat improved demand trend. Indeed, total orders were up more than 5½%Y/Y – the most since December – and more than 8½% above the trough in May. Admittedly, the recent uptrend principally reflects a likely temporary boost to orders of major items, including of aircraft and ships, with the latter reporting in October the second-largest order since re-unification. And the decline in October in part reflected a normalisation in the aerospace subsector following a spike in September. But new auto orders fell to a five-month low, while a further significant drop in orders of machinery and equipment (-7.6%M/M) took them to the lowest since July 2020 and the global financial crisis before that. The weakness reflected drops in domestic (-5.3%M/M) and euro area orders (-7.6%M/M), offsetting a fifth consecutive increase in orders from non-euro area countries, which rose to the highest level since February 2022. When excluding bulk items, core orders were little changed in October

Euro area: Retail sales & consumer confidence



Euro area: Retail sales by member state



(0.1%M/M), maintaining a broadly sideways trend since March, some 8½% below the pre-pandemic benchmark and 18½% below the peak in April 2022. So, while production in certain subsectors will be supported over the near term, today's release strongly suggests that underlying demand for German manufactured goods remains subdued.

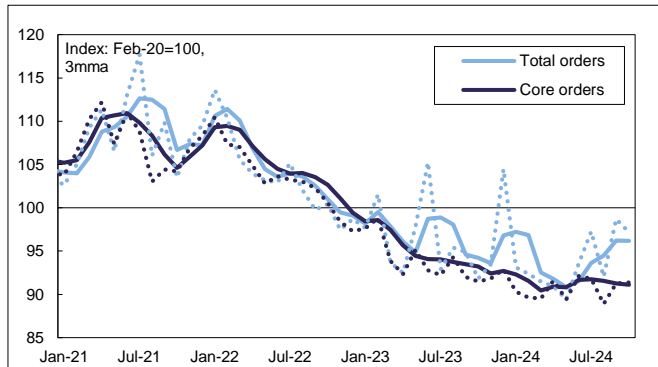
Decline in manufacturing turnover and construction PMI flag downside risks to IP

Despite the pickup in orders at the end of Q3 and subsequent increase in truck toll mileage – often a coincident guide to industrial production – manufacturing turnover fell in October for a second successive month and the seventh month out of the past eight. The drop of 1.3%M/M took turnover to its second-lowest level since June 2020. Admittedly, the pace of decline in manufacturing production in September was twice as severe as that implied by the turnover data that month. So, while today's data suggest that risks to tomorrow's IP release are skewed to the downside, we do expect some positive payback. Indeed, having fallen by 1.4%M/M in September, construction activity should also provide some temporary modest support at the start of Q4. This notwithstanding, the deterioration in the German construction PMI to a seven-month low (38.0) in November suggests that any bounce back in the building sector will likely prove short-lived.

French IP stagnant at start of Q4 with broad sideways trend likely to continue over the near term

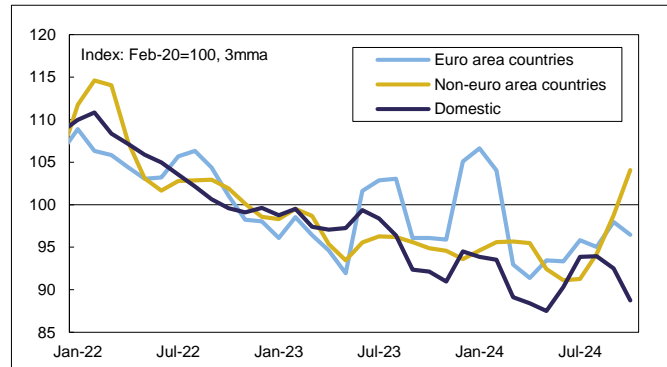
French manufacturing output continues to trend broadly sideways. Having dropped 0.7%M/M in September, it was unchanged on the month in October and was also unchanged from the Q3 average. The French autos sector had a weak start to Q4, with output down 2.9%M/M and other transport down too. But machinery and equipment goods rebounded 1.8%M/M in October, while production of coke and refined petroleum products accelerated 4.8%M/M. Beyond manufacturing, energy output fell for a third month, albeit by just 0.3%M/M. And having fallen for a fifth successive quarter and by 1.2%Q/Q in Q3, construction output edged up just 0.1%M/M in October. Survey indicators for French industry in November were mixed, with the manufacturing output PMI having dropped 2ppts to a 10-month low consistent with marked contraction (41.1) but the (often more reliable) INSEE survey suggesting a significantly better month for the sector. Today's French construction PMIs also posted modest improvement, with the headline index up to a 12-month high – albeit similarly still in contraction territory – thanks to a slower pace of decline in housing, commercial work and civil engineering. But like French manufacturing respondents to the PMI survey, French constructors also reported a further deterioration in order books and were also reportedly more downbeat about prospects for the year ahead. While ongoing ECB rate cuts should provide some support for French industry, we see little cause for optimism about the outlook, not least as political uncertainty at home and abroad will act as a significant disincentive to investment.

Germany: Factory orders*



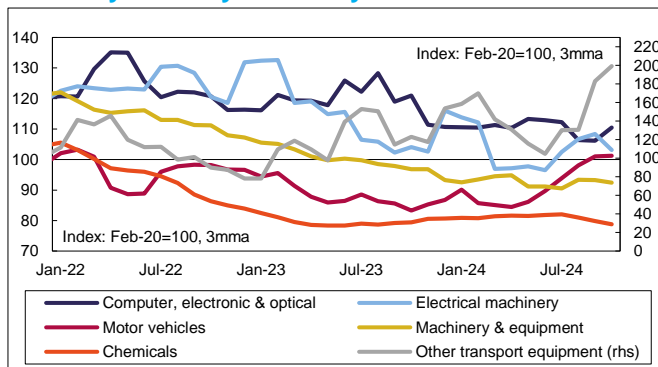
*Dotted lines represent unsmoothed data.
Source: Macrobond and Daiwa Capital Markets Europe Ltd.

Germany: Factory orders*



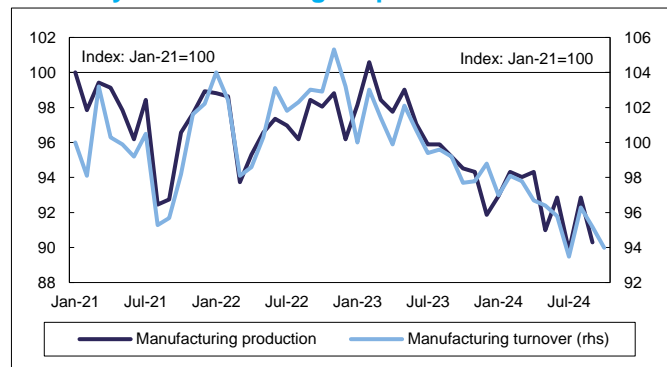
*Including large-scale orders.
Source: Macrobond and Daiwa Capital Markets Europe Ltd.

Germany: Factory orders by selected sector*



*Including large-scale orders.
Source: Macrobond and Daiwa Capital Markets Europe Ltd.

Germany: Manufacturing output & turnover



Source: Macrobond and Daiwa Capital Markets Europe Ltd.

The day ahead in the euro area

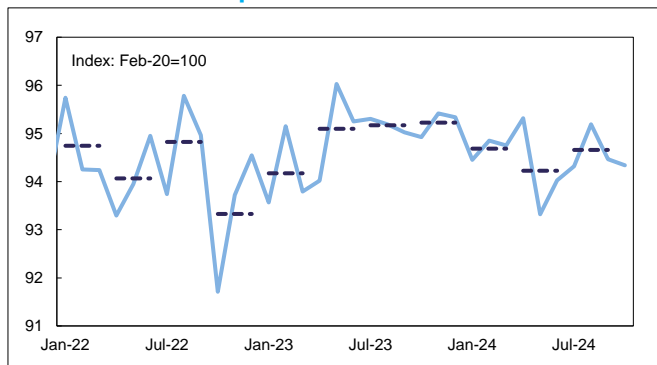
The end of the week will bring the third and final estimates for euro area GDP in Q3. In line with previous estimates, these are expected to reaffirm surprisingly strong growth of 0.4%Q/Q for the quarter, as today's sizable upwards revision to Irish growth (by 1.5ppts to 3.5%Q/Q) more than offset a slightly weaker result in Germany (-0.1ppt to 0.1%Q/Q). Importantly, tomorrow's release will also feature a first breakdown of contributions by expenditure components, which we expect will reveal positive contributions from private and government consumption. Meanwhile, weaker than expected turnover in October's German factory orders could flag a downside risk to Friday's aforementioned industrial production release. But owing to the extent of September's weak performance (-2.5%M/M), an uptick in production at the start of Q4 remains the most likely scenario. A boost in German IP may also reflect favorably on tomorrow's trade data, for which German and French October releases are both due.

UK

Firms expect higher prices but lower profit margins and pay due to budget announcements

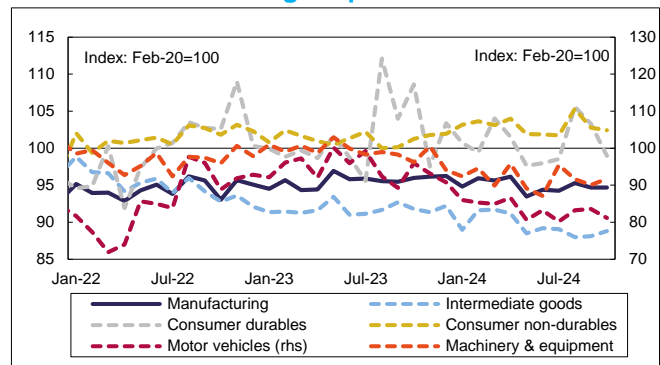
Consistent with the implied pickup in cost burdens flagged in the November PMIs, the results of the BoE's latest Decision Maker Panel survey suggested that UK firms expect reduced profit margins, higher prices, lower employment and pay growth as a consequence of the rise in employer National Insurance contributions announced in the government's budget. In particular, despite more than 50% of survey recipients signalling intentions to pass on some additional costs through higher prices, a higher share of firms (59%) expects lower profit margins than otherwise would have been the case. Certainly, the anticipated increase in output prices in twelve months' time rose to a six-month high in November, albeit the monthly uptick was modest, by 0.2ppt to 3.8%Y/Y, still well below the average in Q124 (4.1%Y/Y) and almost 3ppts below the peak in July 2022. And while firms' CPI expectations one year ahead also rose to a five-month high (2.9%Y/Y), medium-term inflation expectations for three years ahead remained relatively well anchored, up just 0.2ppt to 2.7%Y/Y, bang in line with the average in the first 10 months of the year. Meanwhile, with almost 40% of firms signalling intentions to cut pay, expectations for wage growth over the coming 12 months eased 0.3ppt to 3.8%Y/Y, the lowest since April 2022 and more than 1½ppts below current realised growth, which might in part offset any direct upwards inflationary pressures from the budget.

France: Industrial production exc. construction*



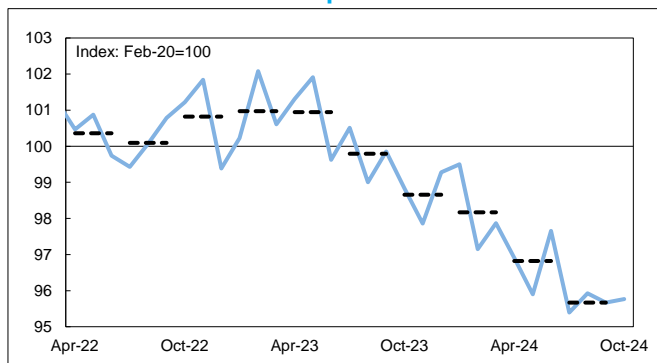
*Dashed dark blue lines represent quarterly average.
 Source: Macrobond and Daiwa Capital Markets Europe Ltd.

France: Manufacturing output - selected sub-sectors



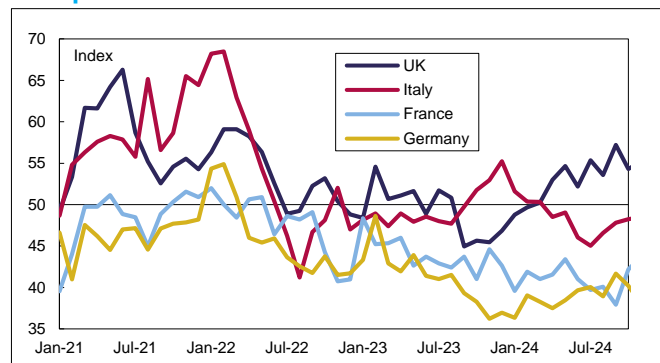
Source: Macrobond and Daiwa Capital Markets Europe Ltd.

France: Construction output*



*Dashed dark blue lines represent quarterly average.
 Source: Macrobond and Daiwa Capital Markets Europe Ltd.

Europe: Construction PMIs

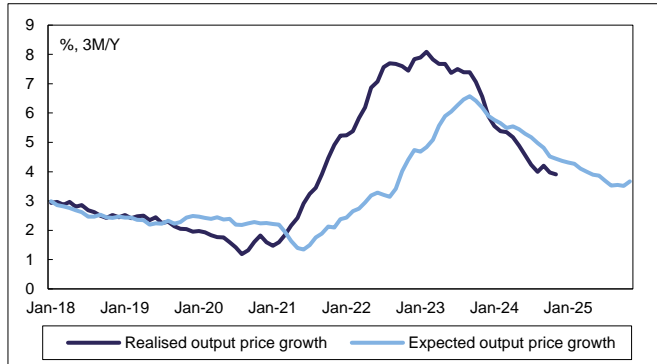


Source: S&P Global, Macrobond and Daiwa Capital Markets Europe Ltd.

The day ahead in the UK

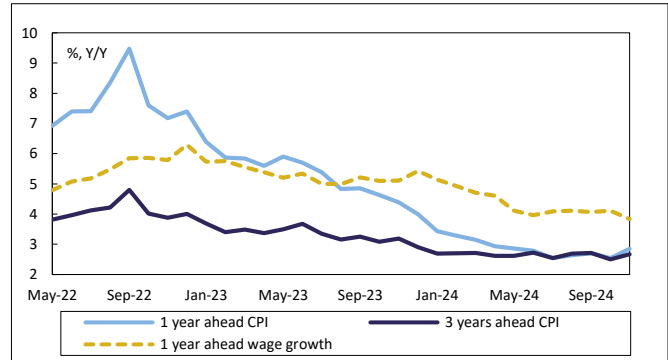
With no headline data releases scheduled for Friday, it should be a relatively quiet end to the week for UK economic news.

UK: Firms' output price expectations



Source: Macrobond and Daiwa Capital Markets Europe Ltd.

UK: Firms' CPI & wage growth expectations



Source: Macrobond 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	Retail sales M/M% (Y/Y%)	Oct	-0.5 (1.9)	-0.3 (1.7)	0.5 (2.9)	- (3.0)
	Construction PMI	Nov	42.7	-	43.0	-
Germany	Factory orders M/M% (Y/Y%)	Oct	-1.5 (5.7)	-2.0 (1.8)	4.2 (1.0)	7.2 (4.2)
	Construction PMI	Nov	38.0	-	40.2	-
France	Industrial production M/M% (Y/Y%)	Oct	-0.1 (-0.6)	0.3 (-0.2)	-0.9 (-0.6)	-0.8 (-)
	Construction PMI	Nov	43.7	-	42.2	-
Italy	Construction PMI	Nov	48.5	-	48.2	-
Spain	Industrial production M/M% (Y/Y%)	Oct	0.5 (1.9)	-0.1 (0.6)	0.5 (0.6)	0.6 (1.1)
	House price index Q/Q% (Y/Y%)	Q3	2.8 (8.1)	-	3.6 (7.8)	-
UK	DMP 3M output price (1Y CPI) expectations %	Nov	3.7 (2.8)	3.5 (2.6)	3.5 (2.5)	-
	Construction PMI	Nov	55.2	53.5	54.3	-




Auctions

Country	Auction
France	sold €1.056bn of 4% 2038 bonds at an average yield of 3.1%
	sold €1.573bn of 0.5% 2040 bonds at an average yield of 3.17%
	sold €882mn of 1.5% 2050 bonds at an average yield of 3.3%
	sold €1.086bn of 0.5% 2072 bonds at an average yield of 2.93%
Spain	sold €1.311bn of 2.7% 2030 bonds at an average yield of 2.365%
	sold €1.136bn of 3.45% 2034 bonds at an average yield of 2.743%
UK	sold £350mn of 0.125% 2073 inflation-linked bonds at an average yield of 1.179%

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

Friday's releases

Economic data

Country	GMT	Release	Period	Market consensus/ <i>Daiwa forecast</i>	Previous
Euro area 	10.00	GDP – final estimate Q/Q% (Y/Y%)	Q3	<u>0.4 (0.9)</u>	0.2 (0.6)
	10.00	GDP – household consumption Q/Q%	Q3	-	0.1
	10.00	GDP – government expenditure Q/Q%	Q3	-	0.9
	10.00	GDP – fixed investment Q/Q%	Q3	-	-2.5
	10.00	Final employment Q/Q% (Y/Y%)	Q3	<u>0.2 (1.0)</u>	0.1 (0.9)
Germany 	07.00	Industrial production M/M% (Y/Y%)	Oct	1.0 (-3.3)	-2.5 (-4.6)
	07.00	Trade balance €bn	Oct	15.7	16.9
France 	07.45	Trade balance €bn	Oct	-	-8.3

Auctions and events

- Nothing scheduled -

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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