Euro wrap-up

Overview

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- Bunds made gains as euro area industrial output declined to a seven-month low in August.
- Gilts opened higher after BoE Governor Bailey yesterday evening reiterated his concerns about the softening labour market.
- Thursday will bring the UK's monthly GDP report and euro area goods trade data for August.

Daily bond market movements

Bond	Yield	Change
BKO 1.9 09/27	1.908	-0.021
OBL 2.2 10/30	2.157	-0.041
DBR 2.6 08/35	2.563	-0.046
UKT 3¾ 03/27	3.868	-0.020
UKT 4⅜ 03/30	3.988	-0.045
UKT 4½ 03/35	4.535	-0.054

*Change from close as at 4:05pm BST.
Source: Bloomberg

Euro area

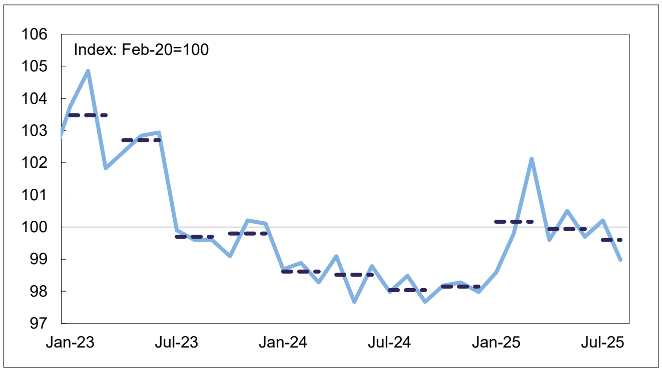
Industrial production falls to 7-month low driven by retrenchment in German autos

While surveys had signalled a meaningful pickup in euro area manufacturing output over the summer, today's industrial production figures for August disappointed. Total output declined 1.2%M/M to the lowest level in seven months. And in the absence of a near-10%M/M rise in Ireland, production would have dropped a little more than 2%M/M. But the decline principally reflected a (hopefully) temporary retrenchment in German car production, which was due in part to summer maintenance factory closures and transitions to new car models. As a result, aggregate euro area autos output declined 11½%M/M, to the lowest level this year, to be trending some 3% below the Q2 average. Various energy-intensive subsectors including chemicals, paper and coke and petroleum also saw production decline in August. But while machinery (-3.2%M/M) also partially reversed the jump in July, output in this subsector was still trending some 2½% above the Q2 average. And production of ICT equipment rose to a 20-month high in August to be tracking more than 3% higher on the quarter. As such, overall industrial production was trending just 0.3% below the Q2 average, suggesting that a pickup in autos in September could yet result in a positive outturn for IP growth over Q3 as a whole.

Car production to rebound in September, while services & construction to support growth in Q3

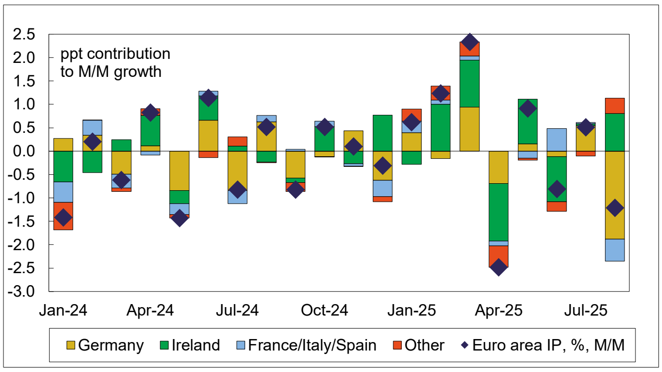
Of course, the near-term production outlook remains uncertain. But we do think that German auto production rebounded last month. For example, truck toll mileage in Germany – a proxy for manufacturing output – rose in September (½%M/M). And despite ongoing weakness in new orders, the euro area manufacturing output PMI and Commission production trend indices for the third quarter were still broadly in line with the Q2 average, suggesting that industry provided neither a significant drag nor a significant boost to GDP growth last quarter. While services activity slipped back slightly at the start of Q3, we think it regained lost ground over the rest of the summer supported by strong growth in tourism-related subsectors, information and communications. Construction data from various member states – including Germany, France, Spain and Portugal – reported a further pickup in activity in August too. As such, despite lacklustre manufacturing, we continue to forecast a modest increase in euro area GDP in Q3 (0.2%Q/Q). And if the Commission survey is to be believed, manufacturing output might now be accelerating at the start of Q4, with producers of investment goods the most upbeat about the output trend since spring 2023.

Euro area: Industrial production*



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

Euro area: Industrial production growth, by country



Source: Macrobond and Daiwa Capital Markets Europe Ltd.

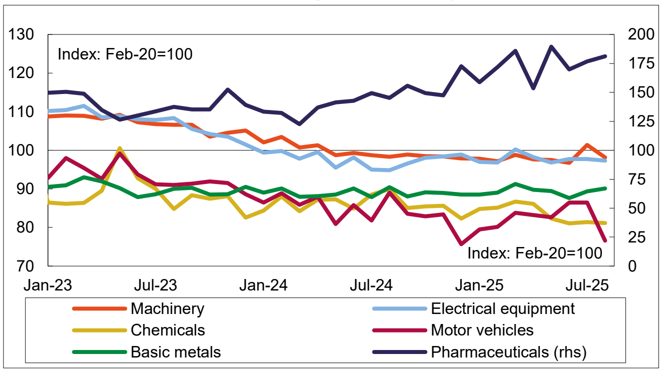
The day ahead in the euro area

Having risen only marginally from June's near-two-year low, we expect tomorrow's goods trade data to report that the euro area surplus widened slightly further in August. However, amid the ongoing slump in orders from the US, national releases suggest that improvement in the trade balance likely came courtesy of lower imports, sufficient to offset a likely fifth consecutive monthly decline in export values. Meanwhile, final Italian inflation data for September will round out the detail from the euro area's four largest members. For the record, today's French and Spanish estimates broadly aligned with expectations, despite national CPI in the latter being nudged slightly higher from its flash release (3.0%Y/Y), while the core rate was unchanged from August (2.4%Y/Y). Predictably, higher energy prices relative to their decline in the same month last year was responsible for most pressure in headline inflation in France, and virtually all that 0.3ppt increase in Spain. The remainder of the equivalent increase in France was attributed to higher services inflation across transport, health and communication components, themselves influenced in part by unfavourable base effects. The preliminary release of Italian inflation suggested that the HICP rate ticked up 0.2ppt to a three-month high of 1.8%Y/Y, driven in equal part by higher fuel and core goods components, most likely relating to stronger seasonal markups in clothing. Meanwhile, speaking arrangements from ECB President Lagarde and Chief Economist Lane in Washington D.C. will also be watched, not least as they closely follow Tuesday's assertion by the influential French Governor (and known-dove) Villeroy that the balance of risks for the ECB are still tilted to the downside and that the probability that the next move in rates will be down is greater than the probability of a hike.

The day ahead in the UK

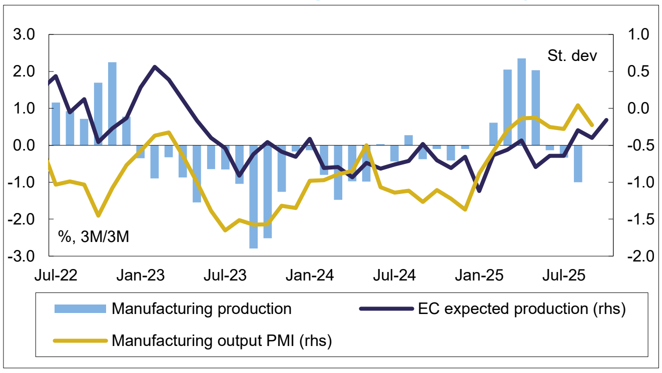
The August monthly GDP report will provide Thursday's focus for the UK. The most recent round of UK business surveys suggested that growth momentum slowed sharply at the end of Q3, likely amplified by September's production shutdown at JLR. But the August data were distinctively more upbeat. Indeed, the PMIs signalled the fastest expansion in activity for the past year. That was led by a pickup in the services sector, for which the respective activity PMI picked up to a 16-month high (54.2). Retail sales growth in that month also suggests another positive month for consumer-facing services. And having declined in July by a chunkier 1.3%M/M, we might expect some moderately positive payback for manufacturers. As such, GDP growth in the three months to August is likely to edge back up to 0.3%3M/3M, in line with the pace in Q2. Otherwise, the BoE's credit conditions survey will provide an update on banks' assessment of lending dynamics heading into Q4. Finally, with respect to the ongoing flow of BoE-speak this week, comments from external MPC member Catherine Mann on an IIF panel in Washington D.C. may also be of interest. While last week she flagged concerns about persistence weakness in private consumption and downside risks to the growth outlook, she also attributed much of that subdued performance to high inflation and so insisted that the BoE should maintain a restrictive policy stance.

Euro area: Manufacturing output, by sector



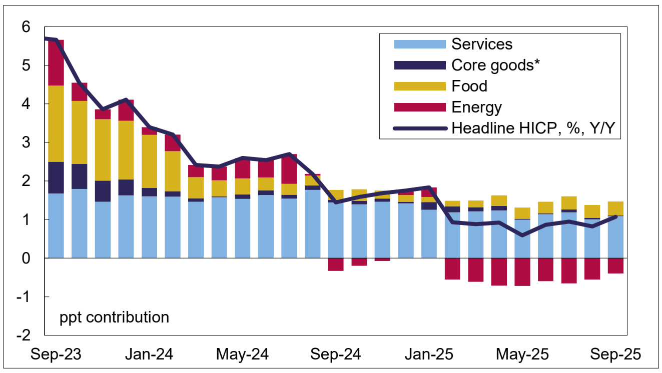
Source: Macrobond and Daiwa Capital Markets Europe Ltd.

Euro area: Manufacturing output & survey indices



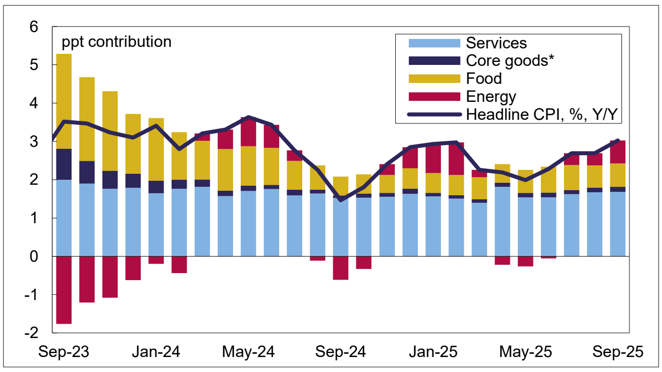
Source: S&P Global, Macrobond and Daiwa Capital Markets Europe Ltd.

France: Contributions to HICP inflation



**Non-energy industrial goods.*
Source: Macrobond and Daiwa Capital Markets Europe Ltd.

Spain: Contributions to CPI inflation



**Non-energy industrial goods.*
Source: Macrobond and Daiwa Capital Markets Europe Ltd.

European calendar

Today's results

Economic data

Country		Release	Period	**Actual**	Market consensus/ *Daiwa forecast*	Previous	Revised
Euro area		Industrial production M/M% (Y/Y%)	Aug	**-1.2 (1.1)**	*-1.2 (0.4)*	0.3 (1.8)	0.5 (2.0)
France		Final HICP (CPI) Y/Y%	Sep	**1.1 (1.2)**	*1.1 (1.2)*	0.8 (0.9)	-
Spain		Final HICP (CPI) Y/Y%	Sep	**3.0 (3.0)**	*3.0 (2.9)*	2.7 (2.7)	-

Auctions

Country		Auction
Germany		sold €757mn of 0% 2050 bonds at an average yield of 3.14%
		sold €1.182bn of 2.9% 2056 bonds at an average yield of 3.17%
UK		sold £1.5bn of 0.125% 2031 inflation-linked bonds at an average yield of 0.889%

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

Tomorrow's releases

Economic data

Country		BST	Release	Period	Market consensus/ *Daiwa forecast*	Previous
Euro area		10.00	Trade balance €bn	Aug	7.0	5.3
Italy		09.00	Final HICP (CPI) Y/Y%	Sep	*1.8 (1.6)*	1.6 (1.6)
UK		07.00	Monthly GDP M/M% (3M/3M%)	Aug	*0.2 (0.3)*	0.0 (0.2)
		07.00	Services output M/M% (3M/3M%)	Aug	0.1 (0.4)	0.1 (0.4)
		07.00	Industrial output M/M% (Y/Y%)	Aug	0.2 (-0.8)	-0.9 (0.1)
		07.00	Construction output M/M% (Y/Y%)	Aug	-0.2 (1.5)	0.2 (2.4)
		07.00	Trade (goods trade) balance £bn	Aug	-4.8 (-22.0)	-5.3 (-22.2)

Auctions and events

Country		BST	Event
Euro area		16.45	ECB Chief Economist Lane speaks in IIF panel discussing the rethinking of frameworks amid trade & policy fragmentation
		17.00	ECB President Lagarde to participate in IMF panel discussing global economy
France		09.50	Auction: to sell up to €11.5bn of 2.4% 2028, 2.5% 2030, 0% 2031 & 2.7% 2031 bonds
		10.50	Auction: to sell up to €1.25bn of 0.6% 2034, 1.8% 2040 & 0.1% 2053 inflation-linked bonds
Spain		09.30	Auction: to sell 1.25% 2030, 2.55% 2032 & 3.2% 2035 bonds
UK		09.30	BoE to publish quarterly Bank Liabilities and Credit Conditions surveys for Q325
		14.00	External MPC member Mann on monetary policy & trade panel at the IIF annual membership meeting, Washington D.C.

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

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