

Euro wrap-up

Overview

- Bunds were little changed as the German ifo survey flagged persisting manufacturing challenges in October but the greatest optimism in the outlook for 2½ years, while euro area bank lending remained firm.
- Gilts made modest gains as a CBI survey signalled weak UK retail sales growth at the start of Q4.
- Tuesday will bring the publication of the ECB's quarterly bank lending survey, Irish GDP data for Q3 and a UK shop price survey.

Chris Scicluna
+44 20 7597 8326

Emily Nicol
+44 20 7597 8331

Daily bond market movements

Bond	Yield	Change
BKO 1.9 09/27	1.968	+0.003
OBL 2.2 10/30	2.227	-0.001
DBR 2.6 08/35	2.616	-0.009
UKT 3½ 03/27	3.776	-0.010
UKT 4% 03/30	3.883	-0.015
UKT 4½ 03/35	4.403	-0.027

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

Euro area

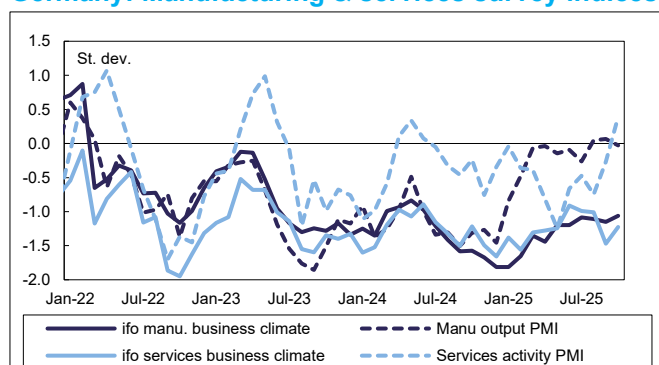
German ifo survey flags persisting manufacturing challenges in October, but recovery on the way

Like Friday's [flash PMIs](#), today's German ifo survey beat expectations, signalling a slight improvement in overall business conditions in the euro area's largest member state at the start of Q4. But while it rose in October, the survey's headline business climate index (up 0.7pt to 88.4) failed to reverse fully the decline in September and was no firmer than the Q3 average when the economy was possibly in a mild technical recession. And it was also still more than 1 standard deviation below the long-run average. Moreover, today's survey disappointingly reported a third successive decline in the current situation balance, with firms judging conditions to be the least favourable in seven months. This left the respective index (85.3) almost 1pt below the Q3 average, suggesting continued contraction in economic activity at the start of Q4. Weakness was most marked in the manufacturing sector, for which current conditions were judged to be the worst since March. This follows a challenging summer when a (hopefully temporary) drop in car production left manufacturing output in August at its lowest level in over 15 years outside of the initial Covid-lockdown. We think that factory production bounced back in September thanks to a pickup in autos. But preliminary turnover figures for that month point to a drop of almost 2%Q/Q in Q3, which would imply a non-negligible drag on GDP growth from the manufacturing sector last quarter. Nevertheless, according to the ifo institute, firms encouragingly suggested that the steady downtrend in new factory orders had come to an end at the start of Q4. Furthermore, manufacturers were reportedly the most upbeat about the six-month outlook since Russia's invasion of Ukraine in spring 2022. That might reflect optimism that the pullback in US demand after tariff front-running at the start of the year might be coming to an end. And it also likely reflects hopes that the government's plans to boost public spending on infrastructure and defence might finally start to come to fruition.

Broad-based but modest growth likely in Q4 to be followed by stronger recovery in H126?

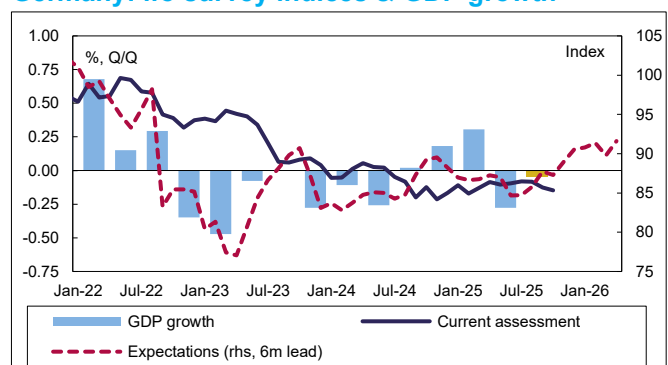
Like the flash PMIs, today's survey signalled a recovery in services sentiment, reportedly due to increased positivity among tourism firms and IT service providers. But while the services activity PMI (54.5) implied the strongest growth in the sector for more than two years in October, the ifo indices suggested a more moderate revival in the sector. In particular, the current conditions index remained close to the bottom of the range of the past 11 months, and the expectations balance was only marginally firmer than the Q3 average. But likely supported by a recent improvement in consumer confidence, retailers judged the current situation to be the best since July. And consistent with signals in previous surveys of a return to growth in civil engineering over the summer, the ifo indices suggested that constructors considered the business climate at the start of Q4 to be the best since mid-2023. As such, we still forecast a return to modestly positive GDP growth in the final quarter of the year. And with the overall ifo expectations index (91.6) up to the highest level for more than 2½ years, we continue to expect a more pronounced recovery in German economic growth momentum in 2026.

Germany: Manufacturing & services survey indices



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

Germany: ifo survey indices & GDP growth*



*Gold bar represents Daiwa Q3 GDP forecast.
Source: Macrobond and Daiwa Capital Markets Europe Ltd.

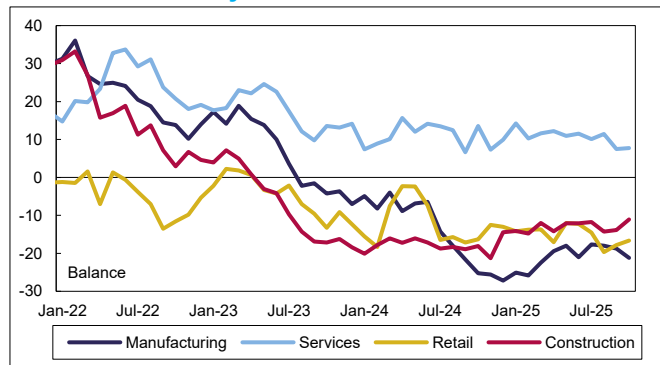
Growth in longer-term loans to businesses remains broadly firm in September

With the ECB having cut its key deposit rate by a cumulative 200bps through to June this year, interest rates on new bank loans have fallen from their peaks. Rates on new businesses loans, which are more closely linked to short rates, have fallen by more than those on households loans, which tend to have longer fixes and so are priced off the longer end of the curve. Over the past year, growth in business loans has been a touch firmer than that of mortgages. And while the annual rate of such lending moderated a touch in September, by 10bps to 2.9%Y/Y, the monthly flow remained positive and broadly steady at €13bn. Encouragingly, for a third successive month, the largest share of that new lending remained in longer-term maturities, which relates most closely to business capex. Growth in the stock of loans of maturities of more than five years rose to 2.9%Y/Y, the strongest since June 2023 while growth in lending of maturities of over one year and up to five years, remained strong at 4.1%Y/Y. According to the ECB's Survey on the Access to Finance of Enterprises, firms think that the economic outlook remains the principal constraint on the availability of external financing. And SMEs reported a slight increase in interest rates last quarter. But the opposite was true for large firms, which might be considered better equipped to cope with the changing global tariff landscape, elevated economic uncertainty and a more downbeat near-term outlook for profits.

Mortgage lending & consumer credit growth maintains uptrend, albeit with member state variation

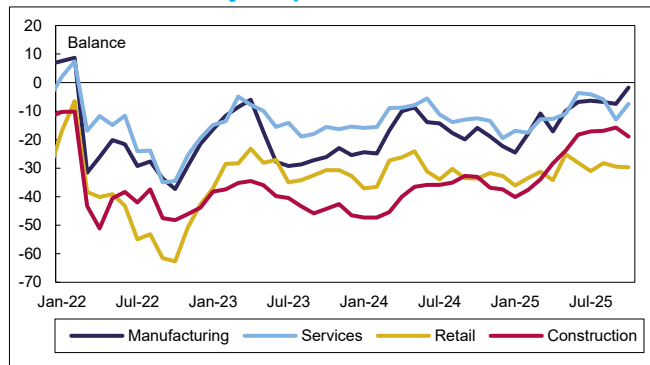
Despite recent stickiness in mortgage interest rates due to the upwards shift in yields on Bunds and core euro area govies this year, growth in the stock of loans for house purchase continued to edge up in September to reach a 2½-year high of 2.6%Y/Y. Indeed, the monthly flow of new mortgages was the strongest in more than three years. But this continues to mask significant differences across the member states. Buoyed by strong growth in incomes and house prices, mortgage lending to Spanish households, the cost of which has now declined to the lowest of the larger member states, accelerated 5.2%Y/Y, the strongest since 2007. In contrast, German mortgage lending, the cost of which has risen steadily this year to the highest in the euro area, remained sluggish, up just 1.3%Y/Y in September. Finally, while interest rates on such new loans remain particularly high and sticky – on average at 7.5% in August, in line with the mean so far this year, just 50bps off the peak and almost 200bps above the average on the existing stock – euro area consumer credit growth maintained its uptrend in September, rising 4.8%Y/Y, the most since February 2020. Tomorrow's ECB Q3 Bank Lending Survey will provide more colour from the lenders' perspective.

German ifo survey: Current conditions indices



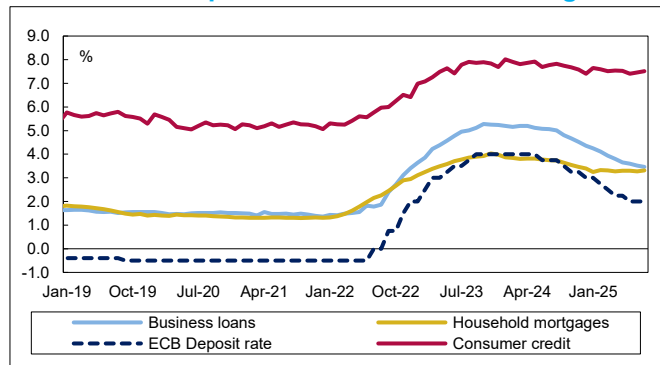
Source: Macrobond and Daiwa Capital Markets Europe Ltd.

German ifo survey: Expectations indices



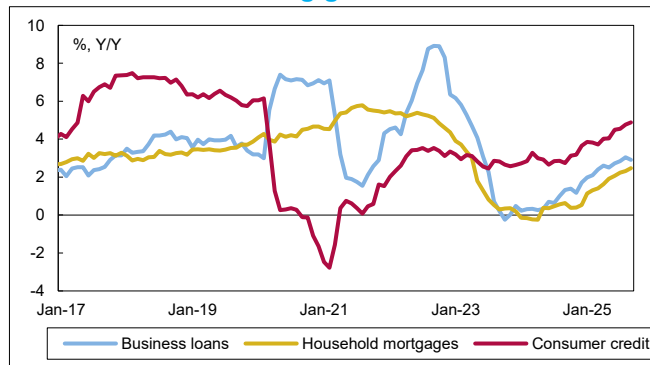
Source: Macrobond and Daiwa Capital Markets Europe Ltd.

Euro area: Composite cost of new borrowing



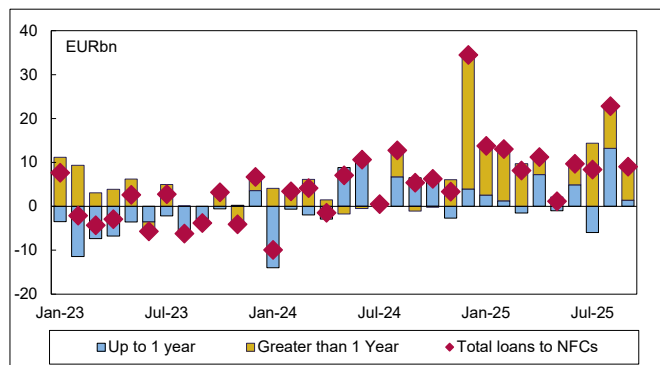
Source: Macrobond and Daiwa Capital Markets Europe Ltd.

Euro area: Bank lending growth



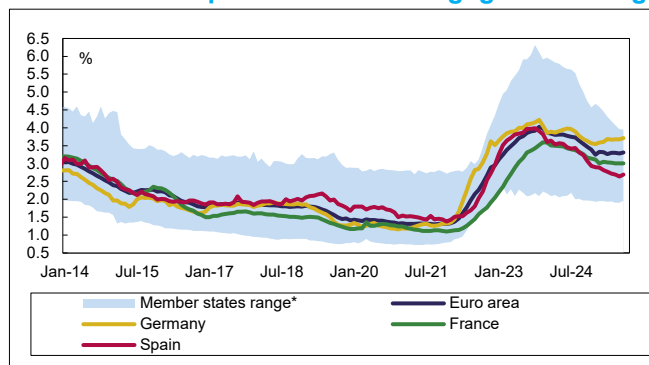
Source: Macrobond and Daiwa Capital Markets Europe Ltd.

Euro area: Net flow of loans to NFCs



Source: Macrobond and Daiwa Capital Markets Europe Ltd.

Euro area: Composite cost of mortgage borrowing



*Excluding Croatia. Source: Macrobond and Daiwa Capital Markets Europe Ltd.

The day ahead in the euro area

Following on from today's monetary figures, the ECB's quarterly Bank Lending Survey will provide a more forward-looking assessment of financial conditions in the euro area. Indeed, that release should be the most closely watched for policymakers on the eve of this week's Governing Council meeting, with recent upwards pressure on yields and uncertainty about the economic outlook posing potential headwinds to lending activity in Q4. Policymakers too may take a glance at the ECB's monthly consumer expectations survey, although we expect its findings to remain consistent with well-anchored inflation expectations. Meanwhile, consumer confidence indicators for Germany (GfK's headline reading being presented as a forecast for November) and Italy will show whether either of those countries might have contributed to October's more upbeat flash Commission indicator. Istat's business sentiment surveys will also provide a view on the mood in the Italian corporate sector at the start of Q4 prior to Thursday's Commission ESIs and next week's PMIs.

The day ahead in the UK

While it should be another relatively quiet day for UK economic news, we note that Tuesday's update to the BRC's shop price index will be of some interest. Certainly, after September's CPI print surprised to the downside, in part owing to a slower rate of increase in food prices, the BRC will provide an early indication as to the likelihood of further moderation into October.

European calendar

Today's results

Economic data

Country	Release	Period	Actual	Market consensus/ <i>Daiwa forecast</i>	Previous	Revised
Euro area	 M3 money supply Y/Y%	Sep	2.8	2.7	2.9	-
Germany	 ifo business climate indicator	Oct	88.4	88.0	87.7	-
	 ifo current assessment (expectations) indicator	Oct	85.3 (91.6)	86.0 (90.0)	85.7 (89.7)	- (89.8)
UK	 CBI distributive trades survey – reported retail sales % balance	Oct	-27	-	-29	-

Auctions

Country	Auction
- Nothing to report -	

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

Tomorrow's releases

Economic data

Country	GMT	Release	Period	Market consensus/ <i>Daiwa forecast</i>	Previous
Euro area	 05.00	New car registrations Y/Y%	Sep	-	3.9
	 09.00	ECB consumer expectations survey – 1Y (3Y) ahead CPI Y/Y%	Sep	-	2.8 (2.5)
Germany	 07.00	GfK consumer confidence indicator	Nov	-22.0	-22.3
Italy	 09.00	ISTAT consumer confidence indicator	Oct	97.0	96.8
	 09.00	ISTAT business (manufacturing) confidence indicator	Oct	-	93.7 (87.3)
UK	 00.01	BRC shop price index Y/Y%	Oct	1.6	1.4

Auctions and events

Euro area	 09.00	ECB to publish quarterly Bank Lending Survey for Q3/Q425
Germany	 10.30	Auction: to sell up to €4bn of 2.2% 2030 bonds
Italy	 10.00	Auction: to sell up to €2bn of 2.1% 2027 bonds
	 10.00	Auction: to sell up to €1.5bn of 1.8% 2036 inflation-linked bonds
UK	 10.00	Auction: to sell £1.5bn of 1.125% 2035 inflation-linked bonds

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

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