

Euro wrap-up

Overview

- Bunds made losses as the ECB left its monetary policy and guidance unchanged, but euro area Q3 GDP beat its expectations and Lagarde stated that some downside risks to the euro area growth outlook have alleviated.
- Gilts followed USTs lower on a quiet day for UK economic news.
- Friday will bring the flash estimate of euro area inflation in October.

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Daily bond market movements

Bond	Yield	Change
BKO 1.9 09/27	1.981	+0.012
OBL 2.2 10/30	2.250	+0.021
DBR 2.6 08/35	2.642	+0.022
UKT 3¾ 03/27	3.783	+0.026
UKT 4¾ 03/30	3.905	+0.035
UKT 4½ 03/35	4.422	+0.031

*Change from close as at 5:00pm GMT.

Source: Bloomberg

Euro area

ECB leaves policy unchanged but less concerned about downside risks

The ECB provided no major surprises when its latest Governing Council meeting concluded today. Inevitably, it left its monetary policy stance unchanged, keeping the deposit rate at 2.00%. Predictably too, it left unchanged its forward guidance that future decisions will remain data dependent not least given two-sided risks to the inflation outlook. But in her press conference, President Lagarde sounded a slightly more upbeat tone than previously, noting an alleviation of certain downside risks to growth thanks to geopolitical developments including the Middle East peace deal and Trump-Xi agreement. The Governing Council was also able to take comfort from today's first estimate of euro area GDP in Q3, which reported growth of 0.2%Q/Q, up 0.1ppt from Q2 and beating the ECB's projection of flat output. The Commission's economic sentiment survey lent credence to the findings of the flash PMIs that activity firmed slightly further at the start of Q4. And with the euro area unemployment rate steady at 6.3% in September just 0.1ppt above the series low, and the first signals on inflation in October also consistent with its outlook for prices, the Governing Council's confidence in its baseline projection will have been reaffirmed today. And as that scenario foresees inflation levelling off close to target over the horizon, in the absence of new shocks there would seem to be no need for the ECB to adjust policy one way or the other anytime soon.

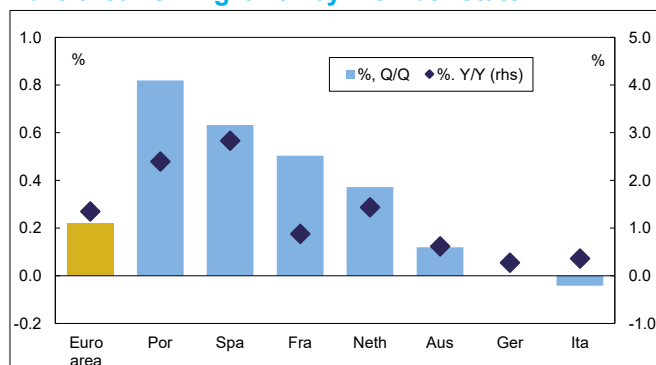
Euro area GDP growth picked up in Q3 despite stagnation in Germany & Italy

As usual, the headline euro area GDP growth figure in Q3 masked a wide range of outcomes for the member states. But the limited detail suggested that domestic final demand, likely related in part to IT services and tourism, again made a positive contribution to growth in the region while net trade and inventories subtracted. In Germany, economic output was flat in Q3 following a revised drop of 0.2%Q/Q in Q2. Given the weakness of industrial production, orders and exports in August, that was arguably as good as might have been hoped. Indeed, encouragingly, Destatis reported that fixed investment in machinery and equipment picked up, hinting that fiscal stimulus might at last be feeding through into real activity. After a slight decline in Q2, Italian GDP was also unchanged in Q3 as net exports offset a negative stock adjustment. In both countries, GDP was up less than ½%Y/Y, acting as a drag on the euro area annual rate (1.3%Y/Y). But given that manufacturing remains relatively high as a share of overall economic activity in both countries, those rates are still suggestive of a degree of resilience in the face of higher US tariffs and broader geopolitical uncertainty.

French growth the best in more than two years but Iberia still leads the way

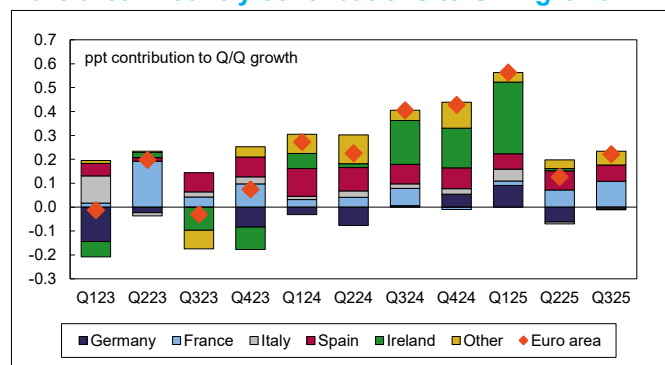
Elsewhere in the euro area, the expansion in Q3 was reassuringly firm. In France, GDP growth of 0.5%Q/Q was much stronger than expected, up 0.2ppt from Q2 and the best in more than two years, pushing the annual rate up to 0.9%Y/Y. As

Euro area: GDP growth by member state



Source: Macrobond and Daiwa Capital Markets Europe Ltd.

Euro area: Country contributions to GDP growth



Source: Macrobond and Daiwa Capital Markets Europe Ltd.

in Germany, capex made a positive contribution while private consumption grew minimally. But the acceleration in French growth was due principally to a marked pickup in exports, buoyed by the aeronautical sector, which also more than offset a negative contribution from stock adjustments. Data released yesterday had already revealed that Spanish GDP was again relatively strong in Q3, albeit moderating 0.2ppt from Q2 to 0.6%Q/Q to be up 2.8%Y/Y. As in France, household consumption and private capex made positive contributions. But Spanish exports fell and net trade made a significantly negative contribution. Portuguese growth also remained strong in Q3, at 0.8%Q/Q and 2.4%Y/Y, reinforcing Iberia's position at the forefront of euro area growth. And the Low Countries continued to avoid German inertia, with moderate expansions reported in the Netherlands (0.4%Q/Q) and Belgium (0.3%Q/Q).

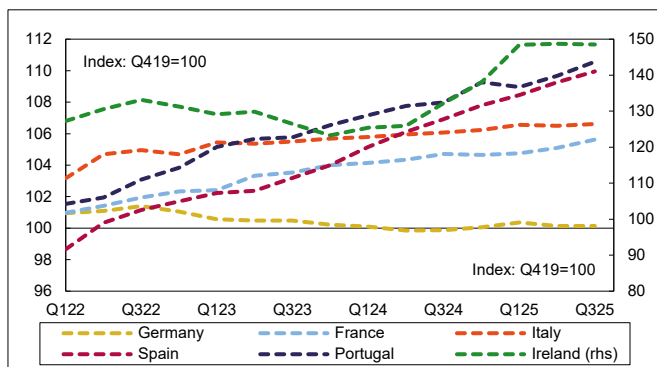
Commission survey points to a slight pickup in growth momentum at the start of Q4

Like last week's [flash euro area PMIs](#), the Commission's Economic Sentiment Indices (ESIs) pointed to a slight pickup in economic growth momentum at the start of Q4. The headline euro area ESI rose 1.2pts this month to 96.8, a 2½-year high. Admittedly, this was still a little more than 3% below the long-run average and consistent with only a modest acceleration in growth this quarter, perhaps to no stronger than ¼%Q/Q. But after activity flatlined in Q3, there was welcome improvement in Germany (up 1pt to 91.5, a three-month high) and Italy (up 1.4pts to 100.5, a 17-month high). And while it failed to provide an accurate gauge of GDP growth in the first three quarters of the year, it was still encouraging that the French ESI jumped 2.5pts to 95.4, a six-month high. While sentiment deteriorated slightly in Spain (103.9) and Portugal (104.4), today's survey pointed to ongoing Iberian outperformance at the start of Q4, with just the Greek ESI (107.5) higher.

Broad-based improvement in economic sentiment led by a rebound in the autos sector

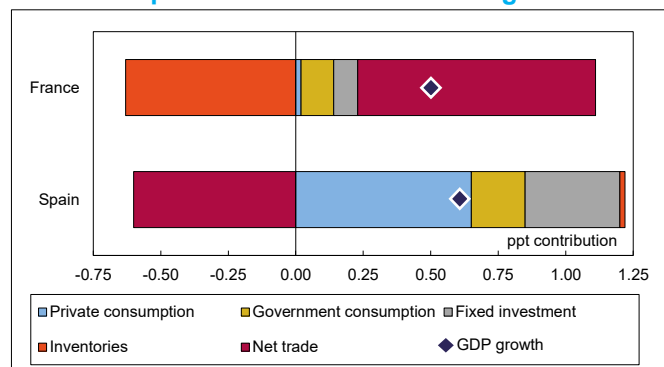
Business confidence improved across the main sectors in October but was principally driven by industry thanks in part to a rebound in German car production after summer shutdowns. Manufacturers' production expectations for the coming three months were the best since April 2023 reflecting widespread reports of a pickup in orders. Discouragingly, however, firms in the sector assessed their external competitiveness to have deteriorated to a new low. While the demand outlook for services weakened, sentiment in the sector was judged as the most favourable for three months. Construction activity reportedly had also been the firmest in 2½ years, supported by building and civil engineering work. And with consumer confidence up to an eight-month high, the outlook for retail sales looked the best since February 2022. But while household fears of unemployment receded in October, firms still aimed to reduce headcount, particularly in manufacturing and retail. And the outlook for consumption remained subject to downside risks as household savings intentions rose to a new record high. Inflation-wise, meanwhile, the Commission survey index of consumer price expectations for the coming year fell back close to the long-run average. And retail and service selling-price expectations eased, the latter to a near-4½-year low.

Euro area member states: GDP levels



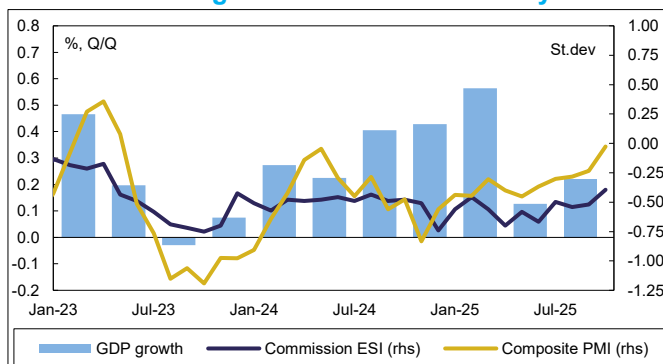
Source: Macrobond and Daiwa Capital Markets Europe Ltd.

France & Spain: Contributions to GDP growth



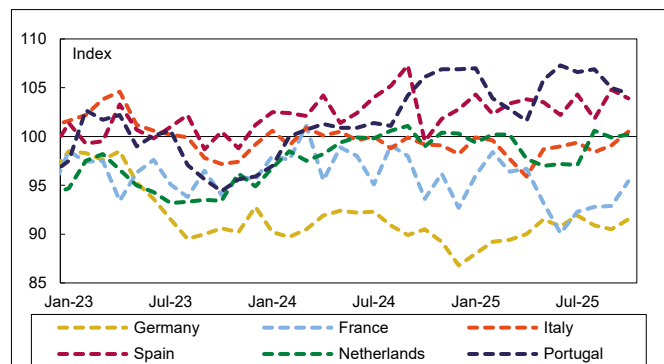
Source: Macrobond and Daiwa Capital Markets Europe Ltd.

Euro area: GDP growth & economic survey indices



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

Euro area: Economic sentiment indices



Source: Macrobond and Daiwa Capital Markets Europe Ltd.

Underwhelming German and Spanish inflation flags risks to Friday's flash euro area estimates

After euro area-wide inflation rates took a predictable, energy-led step-up last month, today's flash German estimates showed a slight cooling in October, with both the euro-harmonised and national measures moderating to 2.3%Y/Y. But being down just 0.1ppt from September's eight-month high, the HICP rate was still to the upside of most forecasts. And the detail on the national measure attributed virtually all of that decrease to lower food inflation, which plummeted 0.8ppt to 1.3%Y/Y, a nine-month low less than half of March's 3.0%Y/Y peak. While food prices were slightly lower on the month, that softness was flattered by a base effect related in part to the sharp increase in olive oil prices one year ago. And core components failed to offer any relief. Indeed, the core rate moved sideways at 2.8%Y/Y, close to the centre of its year-to-date range, with services inflation creeping up to a six-month high (3.5%Y/Y). The lack of detail published at the national level leaves the cause of that pressure open to speculation. But figures published by the lander suggested that some of that pressure came in part from typically volatile items such as package holidays and transport services. Similarly, the pickup in today's flash Spanish HICP estimate – which rose 0.2ppt to 3.2%Y/Y, a 16-month high, in contrast to the expected flat month – was related to an increase in rail and airfares, which are often volatile, as well as electricity prices.

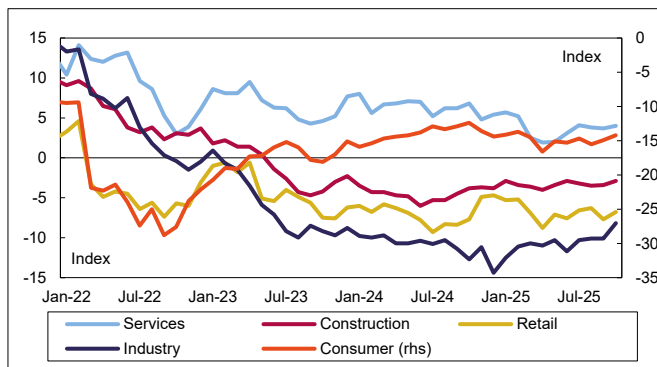
The day ahead in the euro area

Upside in Spain aside, the flash German (and Belgian) data remained broadly supportive of a softer flash euro area inflation reading tomorrow. We expect headline HICP inflation to temporarily fall back to 2.1%Y/Y, down 0.1ppt, principally thanks to a moderation in the non-core energy and food components. But signs of pressure in the more volatile services components could pose an upside risk to our forecast for an equivalent drop in core inflation. A decline of only 0.006ppt on the annual rate is required to round down the headline figure, so the likelihood of a return to 2.3%Y/Y is still relatively strong. Flash inflation releases from France and Italy, due just ahead of the euro area release, will give another signal as to that likelihood. And Friday will also bring a couple of notable releases from Germany, including last month's retail sales figures. Following two negative months, we might expect to see some modest upside in September, albeit to be accompanied by the headline that retail sales volumes fell back last quarter for the first time in six. German import price data for September will also offer more insights as to the potentially disinflationary effects of goods trade diversion away from the US to Europe.

The day ahead in the UK

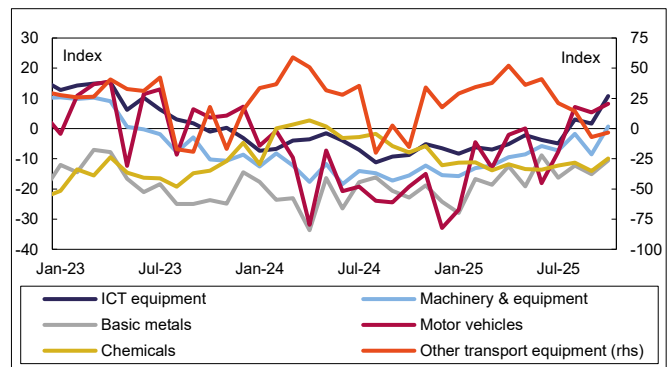
Friday will bring just a couple of second-tier UK survey releases, including a Lloyds business survey and October's update to Nationwide's house price indicator. The latter will be of most interest, particularly when considering that yesterday's bank lending figures – which, against the backdrop of the ongoing recovery in net lending, saw fresh mortgage approvals pickup to a ten-month high – could imply that speculation about tax changes in the autumn budget are failing to dampen activity in the housing market by as much as some feared.

Euro area: Economic sentiment indices



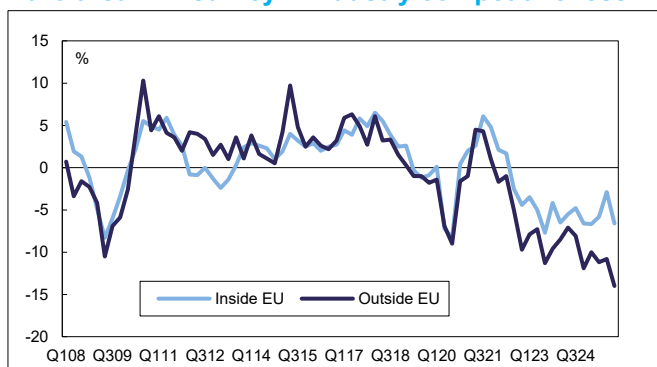
Source: EC, Macrobond and Daiwa Capital Markets Europe Ltd.

Euro area: Production trends in selected sectors



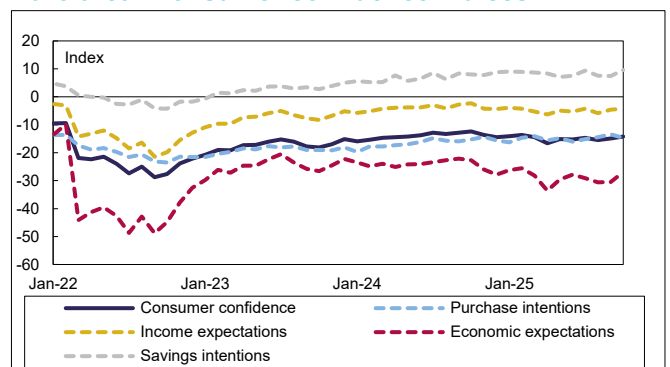
Source: EC, Macrobond and Daiwa Capital Markets Europe Ltd.

Euro area: EC survey – industry competitiveness



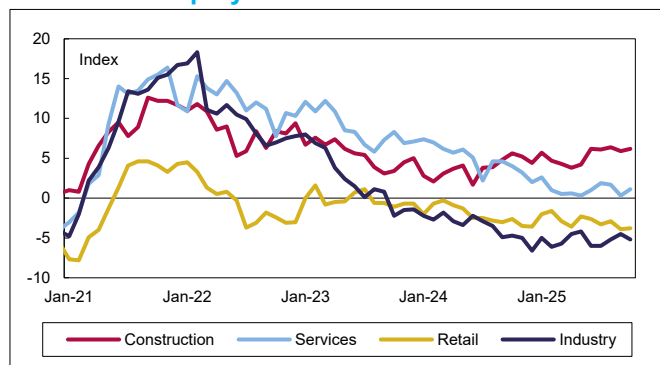
Source: EC, Macrobond and Daiwa Capital Markets Europe Ltd.

Euro area: Consumer confidence indices



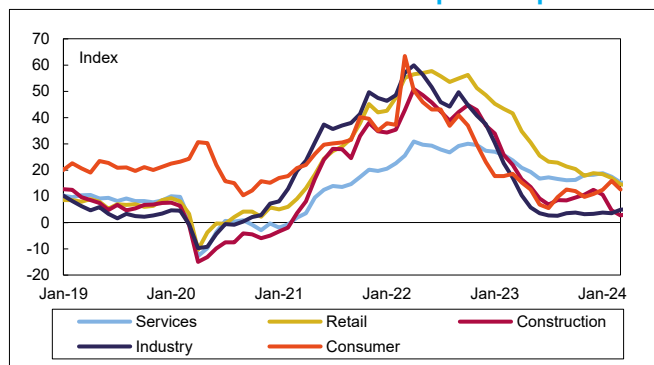
Source: EC, Macrobond and Daiwa Capital Markets Europe Ltd.

Euro area: Employment intentions indices



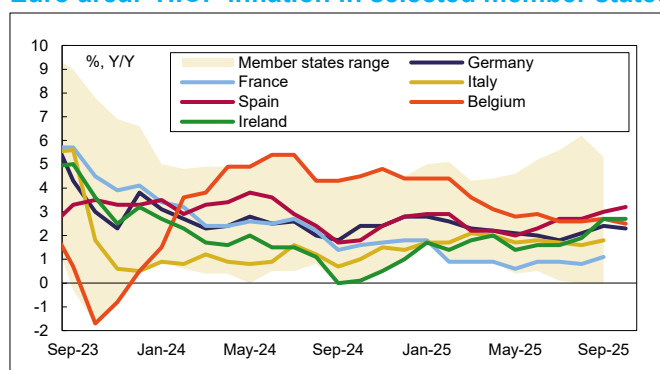
Source: EC, Macrobond and Daiwa Capital Markets Europe Ltd.

Euro area: Business & consumer price expectations



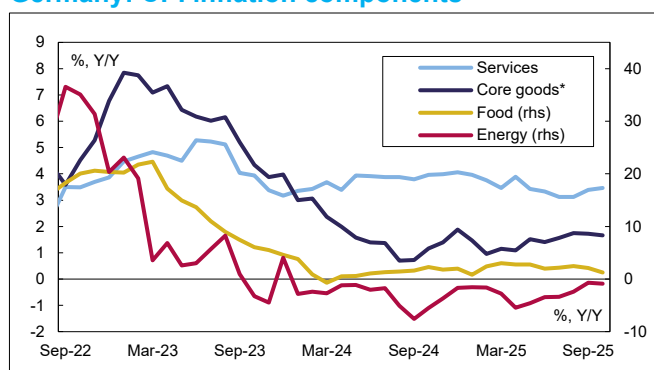
Source: EC, Macrobond and Daiwa Capital Markets Europe Ltd.

Euro area: HICP inflation in selected member states



Source: Macrobond and Daiwa Capital Markets Europe Ltd.

Germany: CPI inflation components



*Daiwa proxy, excluding food and energy 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	GDP – first estimate Q/Q% (Y/Y%)	Q3	0.2 (1.3)	0.1 (1.3)	0.1 (1.5)	-
	Commission economic sentiment indicator	Oct	96.8	96.0	95.5	95.6
	Commission services (industrial) confidence indicator	Oct	4.0 (-8.2)	3.8 (-10.0)	3.6 (-10.3)	3.7 (-10.1)
	Final Commission consumer confidence indicator	Oct	-14.2	-14.2	-14.9	-
	Unemployment rate %	Sep	6.3	6.3	6.3	-
Germany	ECB Deposit (Refinancing) Rate %	Oct	2.00 (2.15)	2.00 (2.15)	2.00 (2.15)	-
	Unemployment claims rate % (change 000s)	Oct	6.3 (-1)	6.3 (8)	6.3 (14)	- (13)
	GDP – first estimate Q/Q% (Y/Y%)	Q3	0.0 (0.3)	-0.1 (0.2)	-0.3 (-0.2)	-0.2 (-0.1)
France	Preliminary HICP (CPI) Y/Y%	Oct	2.3 (2.3)	2.2 (2.2)	2.4 (2.4)	-
	GDP – first estimate Q/Q% (Y/Y%)	Q3	0.5 (0.9)	0.2 (0.6)	0.3 (0.8)	- (0.7)
	Consumer spending M/M% (Y/Y%)	Sep	0.3 (-0.3)	-	0.1 (-0.8)	0.2 (-)
Italy	GDP – first estimate Q/Q% (Y/Y%)	Q3	0.0 (0.4)	0.1 (0.6)	-0.1 (0.4)	- (0.5)
Spain	Preliminary HICP (CPI) Y/Y%	Oct	3.2 (3.1)	3.0 (2.9)	3.0 (3.0)	-

Auctions

Country	Auction
Italy	sold €3bn of 2.85% 2031 bonds at an average yield of 2.75%
	sold €4.5bn of 3.45% 2036 bonds at an average yield of 3.46%
	sold €1bn of 2031 floating bonds at an average yield of 2.64%
	sold €1bn of 2032 floating bonds at an average yield of 2.69%
UK	sold £1.5bn of 0.375% 2030 bonds at an average yield of 3.796%

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

Wednesday's results

Economic data

Country	Release	Period	Actual	Market consensus/ <i>Daiwa forecast</i>	Previous	Revised
Italy	 Hourly wages M/M% (Y/Y%)	Q3	0.0 (2.6)	-	0.1 (2.8)	-
	 PPI Y/Y%	Sep	1.5	-	0.5	-
Spain	 GDP – first estimate Q/Q% (Y/Y%)	Q3	0.6 (2.8)	<u>0.6 (2.8)</u>	0.8 (3.1)	-
	 Retail sales Y/Y%	Sep	4.2	-	4.5	4.7
UK	 Net consumer credit £bn (Y/Y%)	Sep	1.5 (7.3)	1.5 (-)	1.7 (7.1)	- (7.2)
	 Net mortgage lending £bn (mortgage approvals 000s)	Sep	5.5 (65.9)	4.1 (64.0)	4.3 (64.7)	- (65.0)

Auctions

Country	Auction
Germany	 sold €3.378bn of 2.6% 2035 bonds at an average yield of 2.62%
UK	 sold £3.75bn of 4.125% 2033 bonds at an average yield of 4.191%

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	 10.00	Preliminary headline (core) HICP Y/Y%	Oct	<u>2.1 (2.3)</u>	2.2 (2.4)
Germany	 07.00	Retail sales M/M% (Y/Y%)	Sep	0.2 (2.7)	-0.2 (-1.1)
	 07.00	Import prices M/M% (Y/Y%)	Sep	-0.2 (-1.3)	-0.5 (-1.5)
France	 07.45	Preliminary HICP (CPI) Y/Y%	Oct	0.9 (1.0)	1.1 (1.2)
	 07.45	PPI Y/Y%	Sep	-	0.1
Italy	 10.00	Preliminary HICP (CPI) Y/Y%	Oct	1.6 (1.5)	1.8 (1.6)
UK	 00.01	Lloyds business barometer (own price expectations) % balance	Oct	-	42 (63)
	 07.00	Nationwide house prices M/M% (Y/Y%)	Oct	0.0 (2.3)	0.5 (2.2)

Auctions and events

Euro area	 09.00	ECB to publish quarterly Survey of Professional Forecasters for Q425
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Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

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