

Euro wrap-up

Overview

- Shorter-dated Bunds followed USTs slightly higher, while euro area inflation slipped back in October as energy and food price pressures faded.
- Gilts also made modest gains on a quiet day for UK economic news.
- On Thursday the BoE is expected to leave Bank Rate unchanged, but signal that the December MPC meeting remains 'live' for a further rate cut. Euro area retail sales, German IP, factory orders and goods trade data for September are also due.

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Daily bond market movements

Bond	Yield	Change
BKO 1.9 09/27	1.963	-0.018
OBL 2.2 10/30	2.229	-0.021
DBR 2.6 08/35	2.631	-0.011
UKT 3¾ 03/27	3.756	-0.026
UKT 4¾ 03/30	3.878	-0.027
UKT 4½ 03/35	4.406	-0.016

*Change from close as at 4:45pm GMT.
Source: Bloomberg

Euro area

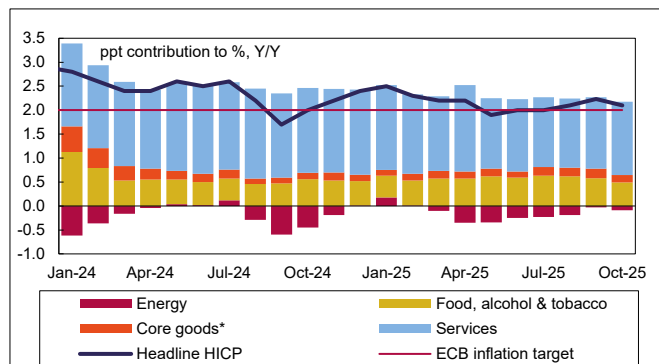
Euro area inflation slips back as energy and food price pressures fade

After euro area inflation took an energy-led step up in September to a five-month high (2.2%Y/Y), today's flash estimates for October saw the headline HICP rate ease 0.1ppt to 2.1%Y/Y. The improvement was similarly driven by the non-core components. Indeed, having risen to a seven-month high in September, energy more than fully reversed that increase (-1.0%Y/Y) benefitting from a further decline in petrol prices as well as lower Italian regulated prices. While still elevated by historical trends, a further normalisation in pricing and a favourable base effect pushed inflation of food, alcohol and tobacco down for a third consecutive month and by a chunky 0.5ppt to 2.5%Y/Y, a nine-month low. Notably, inflation of fresh foods (3.2%Y/Y) was more than 3ppts below the August peak. While seasonal discounting appears to have weighed in particular on clothing inflation in Italy, today's release suggested a continued widespread absence of factory price pressures in the region, with non-energy industrial goods inflation slipping to a four-month low (0.6%Y/Y). In contrast, services inflation rose more than expected, by 0.2ppt to 3.4%Y/Y, a six-month high. As such, contrasting expectations for a slight moderation, euro area core inflation moved sideways at 2.4%Y/Y, with the equivalent German rate up 0.2ppt to 2.8%Y/Y, the highest since April. Admittedly, the euro area core rate was still on the low side (2.365%Y/Y). And we suspect that upward impulse related to often-volatile transport services, with higher airfares playing a role in Germany and Spain, and unfavourable base effects from underground and tram pricing normalisation after last year's Paris Olympics pushing annual rates higher in France.

Higher inflation into year-end should prove temporary

Overall, today's inflation data will reinforce the ECB's stance that policy is in a "good place". While Lagarde yesterday reiterated that two-sided risks to the inflation outlook remain, the hawks on the Governing Council might view the renewed pickup in services momentum and stickiness in core inflation as further reason to resist an extra 'insurance' rate cut this cycle. Due to base effects, we expect services inflation to rise back above 3½%Y/Y at the turn of the year. But we continue to forecast a substantial step down in the spring before tracking between 2-2½%Y/Y through to the end of 2027 in part due to normalising pay growth, which should be illustrated by the ECB's wage tracker to be updated on Wednesday. Core goods pressures should also remain absent, weighed by soft demand, euro strength and a possible influx of imported goods redirected from the US. Energy inflation will also become a larger drag at the start of next year thanks to German cuts to electricity prices. And a more gradual phase-in to the introduction of the ETS2 carbon market from 2027 might require a downwards revision to the ECB's forecast of energy inflation that year in due course. Based on current policy, we expect headline inflation to fall back below 2.0%Y/Y from the start of 2026. But, as we also expect a gradual pickup in economic growth, it should still end the policy horizon near target.

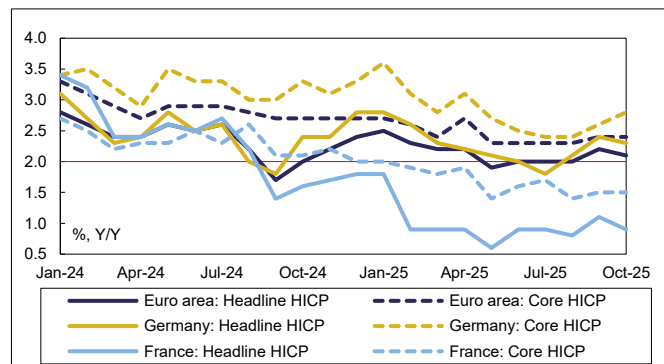
Euro area: Contributions to HICP inflation



*Non-energy industrial goods.

Source: Macrobond and Daiwa Capital Markets Europe Ltd.

Euro area: Headline & core HICP inflation



Source: Macrobond and Daiwa Capital Markets Europe Ltd.

The week ahead in the euro area

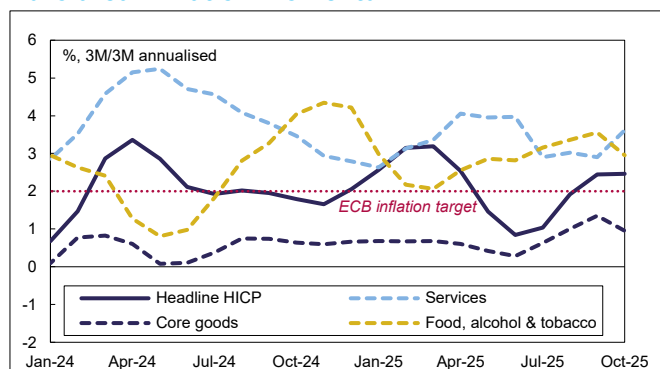
After the first estimate of euro area [GDP in Q3](#) reported a slight acceleration in growth, the coming week's September data releases will provide greater insight into economic momentum at the end of the quarter. Euro area retail sales (Thursday) are likely to suggest that household consumption remained relatively subdued last month. Indeed, today's German sales numbers reported growth of just 0.2%M/M in September, with spending on non-food items down for a second successive month (-0.7%M/M). This left German sales flat in Q3, consistent with the absence of consumption growth implied by Destatis commentary yesterday. Overall, aggregate euro area sales are forecast to rise modestly for a second successive month (<0.5%M/M) albeit leaving them broadly flat in Q3. With German economic output having moved sideways in Q3, we expect the September results from the largest member state for industrial production (Thursday), factory orders (Wednesday) and goods trade (Friday) to report some improvement at the end of the quarter after weakness over the summer. Certainly, the slump in car production in August was likely exacerbated by annual maintenance shutdowns and should be reversed in September. And recent surveys hint at a pickup in domestic and overseas demand. September IP data will also be published from France (Wednesday) and Spain (Thursday). Meanwhile, the final October PMI surveys – including manufacturing (Monday), services (Wednesday) and construction (Thursday) – are expected to signal ongoing modest recovery at the start of Q4. Aside from the data, there will be various ECB policymakers in action, including a keynote speech from President Lagarde (Tuesday), participation in a policy panel discussion with Chief Economist Lane (Thursday) and opening remarks by Executive Board hawk Schnabel at an ECB money markets conference (Thursday).

UK

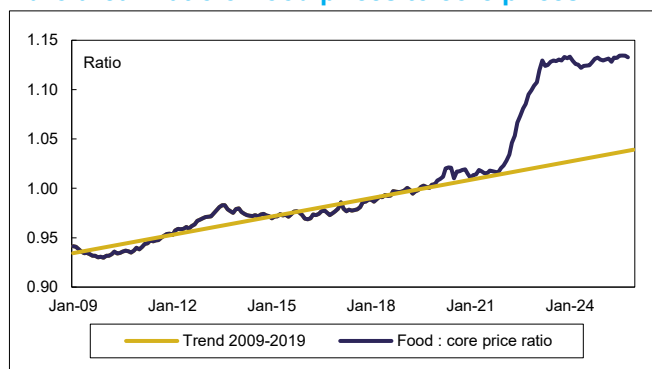
Uncertainty about Thursday's BoE announcement higher than usual given MPC split

Thursday's monetary policy announcement – which will be accompanied by the BoE's Monetary Policy Report, featuring its updated macroeconomic projections – is the main event in the coming weeks' UK economic calendar. But unlike this week's ECB affair, the outcome of the BoE's meeting is subject to uncertainty. The flurry of Bank-speak since September's meeting suggests that the fears of the MPC's more hawkish policymakers (Pill, Lombardelli, Greene and, for now, Mann) about persistent inflation risks haven't softened much. Likewise, those who have placed more weight on the recent labour market loosening in their assessments (Ramsden, Dhingra and Taylor) have appeared just as stubborn. So, that would appear to leave Governor Bailey and Deputy Governor Breeden with the decisive votes. Crucially, since both were sympathetic to concerns about the sluggishness of economic activity and softening of the labour market in their recent communications, the possibility of another 4-5 vote in favour of a 25bps cut, as in August, cannot be completely ruled out.

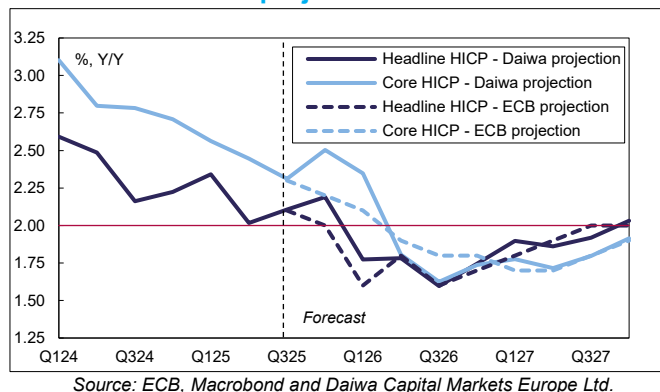
Euro area: Inflation momentum



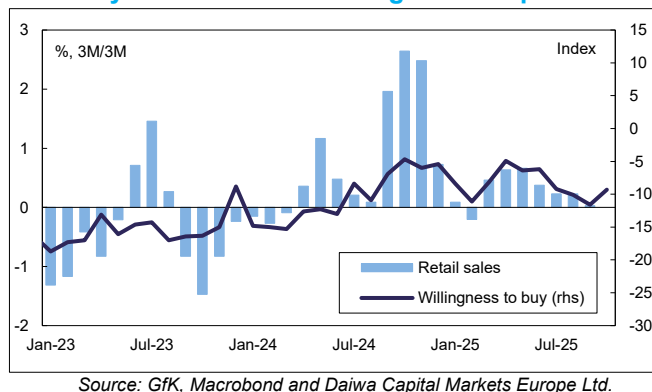
Euro area: Ratio of food prices to core prices



Euro area: Inflation projections



Germany: Retail sales & willingness to spend



We expect the MPC to hold Bank Rate at 4.00%, if only temporarily

Nevertheless, we still expect at least one, or more likely both, of them to err on the side of caution, which would result once more in a majority in favour of holding Bank Rate steady at 4.00%. Of course, there are several good reasons why the MPC would be in less of a rush to ease again. Not least among them, in our view, is the uncertainty about the fiscal stance and detailed measures to come in the government's Autumn budget (just three weeks out), and their implications for the inflation outlook. Of course, despite Q3 marking the peak of the UK's recent inflation bout and coming in slightly below the BoE's expectation, headline inflation in September remained almost 2ppts above target (3.8%Y/Y) with the services component at an elevated 4.7%Y/Y. That should maintain the MPC's concerns about potential second-round effects. Moreover, while the growth outlook remains subdued, forward-looking indicators have been somewhat resilient, and we note that GDP growth in Q2 of 0.3%Q/Q proved firmer than the BoE expected (0.1%Q/Q). Retail sales volumes have also been (suspiciously) strong, while revisions to the jobs data might also imply that the labour market is now weakening more slowly than earlier in the year.

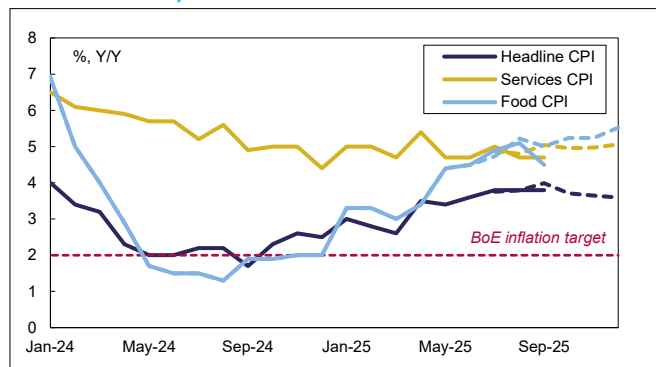
Bank guidance to be broadly unchanged; focus on signals for resumed cuts in December

Nevertheless, with inflation expected to take a first step down from this month and slowing wage growth suggestive of gradual disinflation across the horizon, the MPC should still maintain that a "gradual and careful approach to the further withdrawal of monetary policy remains appropriate". And while, on balance, we expect it to reiterate that the risks to the inflation outlook remain skewed to the upside, the statement might have a softer tone than we saw at September's meeting (when policymakers added that those risks remained "prominent" in the Committee's outlook). For the first time, each MPC member will be given a paragraph in the MPR to justify their vote, which might also give greater clarity about how the balance of the views is evolving. Perhaps still most important, however, will be the tone of Governor Bailey's press conference. Indeed, with the Autumn budget likely to confirm a non-negligible fiscal tightening, we would not be surprised if he were to signal that monetary policy would aim to offset its effects and, effectually, signal that December's MPC meeting remains 'live' for a rate cut. In addition to waiting for clarity on the budget measures, postponing until December would also benefit the BoE with more data, including two months' worth of inflation and labour market reports, plus the preliminary Q3 GDP estimates.

No decisive shift to the BoE's projections, but inflation outlook to be nudged lower in the near term

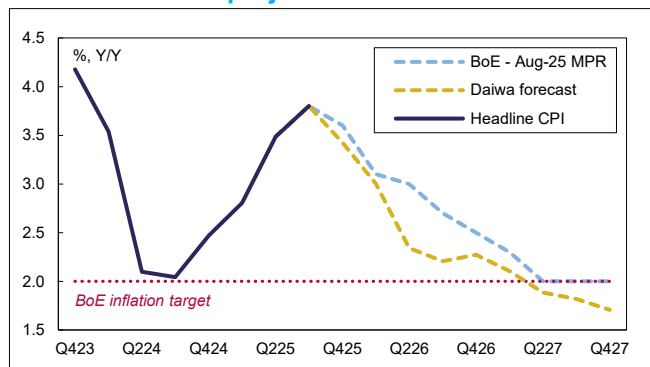
The BoE's updated medium-term projections should also not stand in the way of the MPC foregoing a more prolonged pause, albeit with a material shift in the BoE's inflation outlook seemingly out of the question. With the profile for core inflation expected to be little changed relative to August, the updated forecasts should continue to see inflation returning to

UK: Headline, services & food inflation vs BoE*



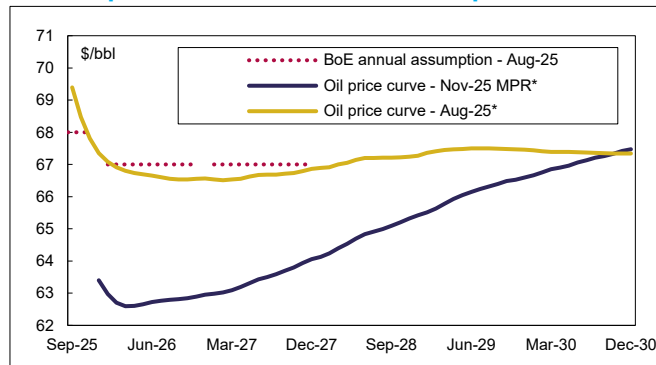
*Dashed lines represent BoE projections from August 2025 MPR.
 Source: Macrobond, BoE and Daiwa Capital Markets Europe Ltd.

UK: CPI inflation projections



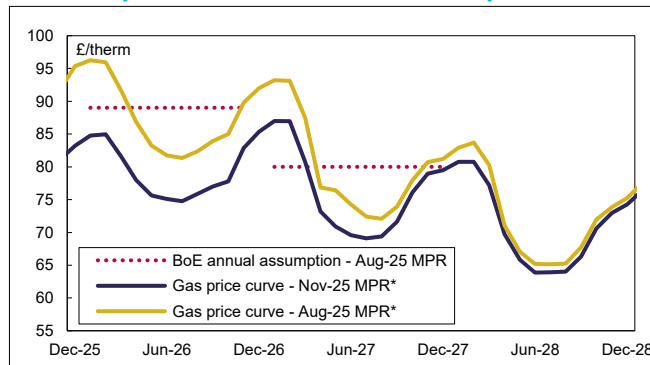
Source: Macrobond, BoE and Daiwa Capital Markets Europe Ltd.

UK: Oil price curves and BoE assumption



*Based on Daiwa's estimate of the BoE's forecast calculation period.
 Source: Bloomberg, BoE and Daiwa Capital Markets Europe Ltd.

UK: Gas price curves and BoE assumption



*Based on Daiwa's estimate of the BoE's forecast calculation period.
 Source: Bloomberg, BoE and Daiwa Capital Markets Europe Ltd.

target only by the end of 2026. But the outlook for headline inflation should still be nudged down over the near term, to just below 3½%Y/Y in Q4, and sub-3%Y/Y by Q226. That will partly stem from [September's CPI](#) undershoot, for which softer food inflation was a contributor. With that having fallen sharply to 4.5%Y/Y, 0.5ppt below the BoE's forecast, and with additional [hints of relief](#) ahead, the BoE will surely revise down its assumption for the peak in food inflation (from 5.5%Y/Y in December previously). Lower oil and gas prices – down ~5% and ~10% based on previous assumptions for 2026 alone – are also bound to lend support to a downwards revision. Adjustments to the BoE's outlook for GDP growth are also likely to be mostly reactive. Besides accounting for the ONS's latest revisions to the series, we would expect to see the BoE nudge down its forecast for GDP growth in the second half of this year, in part as payback for the lesser slowdown in Q2.

The next Euro wrap-up will be published on Wednesday 5 November 2025

Daiwa economic forecast

		2025				2026		2025	2026	2027
		Q1	Q2	Q3	Q4	Q1	Q2			
GDP		%, Q/Q						%, Y/Y		
Euro area		0.6	0.1	0.2	0.3	0.3	0.3	1.4	1.1	1.4
UK		0.7	0.3	0.2	0.3	0.3	0.4	1.5	1.3	1.5
Inflation, %, Y/Y										
Euro area										
Headline HICP		2.3	2.0	2.1	2.2	1.8	1.8	2.2	1.7	1.9
Core HICP		2.6	2.4	2.3	2.5	2.3	1.8	2.5	1.9	1.8
UK										
Headline CPI		2.8	3.5	3.8	3.4	3.0	2.3	3.4	2.5	1.9
Core CPI		3.6	3.7	3.6	3.4	3.2	2.5	3.6	2.6	1.7
Monetary policy, %										
ECB										
Deposit Rate		2.50	2.00	2.00	2.00	2.00	2.00	2.00	2.00	2.00
Refi Rate		2.65	2.15	2.15	2.15	2.15	2.15	2.15	2.15	2.15
BoE										
Bank Rate		4.50	4.25	4.00	3.75	3.50	3.25	3.75	3.25	3.00

Source: Bloomberg, ECB, BoE 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	 Preliminary headline (core) HICP Y/Y%	Oct	2.1 (2.4)	2.1 (2.3)	2.2 (2.4)	-
Germany	 Retail sales M/M% (Y/Y%)	Sep	0.2 (2.8)	0.2 (2.7)	-0.2 (-1.1)	-0.5 (-1.6)
	 Import prices M/M% (Y/Y%)	Sep	0.2 (-1.0)	-0.2 (-1.3)	-0.5 (-1.5)	-
France	 Preliminary HICP (CPI) Y/Y%	Oct	0.9 (1.0)	0.9 (1.0)	1.1 (1.2)	-
	 PPI Y/Y%	Sep	0.1	-	0.1	-
Italy	 Preliminary HICP (CPI) Y/Y%	Oct	1.3 (1.2)	1.6 (1.5)	1.8 (1.6)	-
UK	 Lloyds business barometer (own price expectations) % balance	Oct	50 (63)	-	42 (63)	-
	 Nationwide house prices M/M% (Y/Y%)	Oct	0.3 (2.4)	0.0 (2.3)	0.5 (2.2)	-
Auctions						
Country	Auction					
- Nothing to report -						

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

The coming week's data calendar

The coming week's key data releases

Country		GMT	Release	Period	Market consensus/ <i>Daiwa forecast</i>	Previous
Monday 3 November 2025						
Euro area		09.00	Final manufacturing PMI	Oct	<u>50.0</u>	49.8
Germany		08.55	Final manufacturing PMI	Oct	<u>49.6</u>	49.5
France		08.50	Final manufacturing PMI	Oct	<u>48.3</u>	48.2
Italy		08.45	Manufacturing PMI	Oct	49.3	49.0
Spain		08.15	Manufacturing PMI	Oct	51.8	51.5
UK		09.30	Final manufacturing PMI	Oct	<u>49.6</u>	46.2
Tuesday 4 November 2025						
Spain		08.00	Unemployment (net employment) change 000s	Oct	-	-4.8 (56.7)
Wednesday 5 November 2025						
Euro area		09.00	Final composite (services) PMI	Oct	<u>52.2 (52.6)</u>	51.2 (51.3)
		10.00	PPI Y/Y%	Sep	-0.2	-0.6
Germany		07.00	Factory orders M/M% (Y/Y%)	Sep	1.0 (-3.9)	-0.8 (1.5)
		08.55	Final composite (services) PMI	Oct	<u>53.8 (54.5)</u>	52.0 (51.5)
France		07.45	Industrial production M/M% (Y/Y%)	Sep	0.1 (0.7)	-0.7 (0.4)
		08.50	Final composite (services) PMI	Oct	<u>46.8 (47.1)</u>	48.1 (48.5)
Italy		08.45	Composite (services) PMI	Oct	52.1 (52.9)	51.7 (52.5)
		09.00	Retail sales M/M% (Y/Y%)	Sep	-	-0.1 (0.5)
Spain		08.15	Composite (services) PMI	Oct	54.0 (54.5)	53.8 (54.3)
UK		09.00	New car registrations Y/Y%	Oct	-	13.7
		09.30	Final composite (services) PMI	Oct	<u>51.1 (51.1)</u>	50.1 (50.8)
Thursday 6 November 2025						
Euro area		08.30	Construction PMI	Oct	-	46.0
		10.00	Retail sales M/M% (Y/Y%)	Sep	0.2 (1.0)	0.1 (1.0)
Germany		07.00	Industrial production M/M% (Y/Y%)	Sep	3.0 (0.1)	-4.3 (-3.9)
		08.30	Construction PMI	Oct	-	46.2
France		07.45	Preliminary private sector payrolls Q/Q%	Q3	-	0.2
		08.30	Construction PMI	Oct	-	42.9
Italy		08.30	Construction PMI	Oct	-	49.8
Spain		08.00	Industrial production M/M% (Y/Y%)	Sep	0.3 (1.7)	-0.1 (3.4)
UK		09.30	Construction PMI	Oct	46.7	46.2
		12.00	BoE Bank Rate %	Nov	<u>4.00</u>	4.00
		14.00	DMP 3M output price (1Y CPI) expectations Y/Y%	Oct	-	3.7 (3.4)
Friday 7 November 2025						
Germany		07.00	Trade balance €bn	Sep	16.9	16.9
France		07.45	Trade balance €bn	Sep	-	-5.5
		07.45	Preliminary wages Q/Q%	Q3	-	0.5

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

The coming week's key events & auctions

Country	GMT	Event / Auction
Monday 3 November 2025		
- Nothing scheduled -		
Tuesday 4 November 2025		
Euro area	 07.40	ECB President Lagarde to give keynote speech in Sofia, Bulgaria, followed by press conference (10.00)
Germany	 10.30	Auction: to sell up to €5bn of 2% 2027 bonds
UK	 10.00	Auction: to sell £5bn of 4% 2029 bonds
Wednesday 5 November 2025		
Euro area	 09.00	ECB to publish updated wage tracker tool
	 10.00	ECB Governing Council's Nagel & Villeroy to speak at Banque de France-Bundesbank monetary policy conference, Paris
Germany	 10.30	Auction: to sell up to €1bn of 2.6% 2041 bonds
	 10.30	Auction: to sell up to €1bn of 2.5% 2044 bonds
Thursday 6 November 2025		
Euro area	 18.30	ECB Chief Economist Lane speaks on panel discussing global trade at an IMF research conference, Washington D.C.
France	 09.50	Auction: to sell up to €11bn of 3.5% 2035, 3.6% 2042 & 3% 2049 bonds
Spain	 09.30	Auction: to sell 3% 2033, 1.85% 2035, & 3.5% 2041 bonds & 1.15% 2036 inflation-linked bonds
UK	 12.00	BoE monetary policy announcement, minutes and Monetary Policy Report to be published
	 12.30	BoE Governor Bailey to present updated macroeconomic projections in post-MPC press conference
Friday 7 November 2025		
Germany	 12.00	Bundesbank President & ECB Governing Council's Nagel in conversation with Fed Vice Chair Jefferson, Frankfurt
UK	 12.15	BoE Chief Economist Pill to brief Bank Agents on updated macroeconomic projections

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

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