Euro wrap-up

Overview

Emily Nicol
+44 20 7597 8331

Edward Maling
+44 20 7597 8030

- While comments from ECB policymakers underscored the strong probability of further policy tightening, shorter-dated Bunds made gains as oil prices fell back.
- Despite an upside surprise to UK GDP in July, shorter-dated Gilts also made gains while a BoE household survey reported a moderation in inflation expectations.
- On Thursday, the BoE will likely leave Bank Rate unchanged but adopt a more hawkish tone. Euro area & UK inflation & labour market data are also due for release.

Daily bond market movements

Bond	Yield	Change
BKO 2.7 09/28	3.188	-0.042
OBL 2.9 10/31	3.290	-0.019
DBR 3 08/36	3.502	+0.005
UKT 4 05/29	4.810	-0.057
UKT 4⅛ 03/31	4.896	-0.050
UKT 4⅞ 07/36	5.342	-0.031

*Change from close as at 5:00pm BST.
Source: Bloomberg

UK

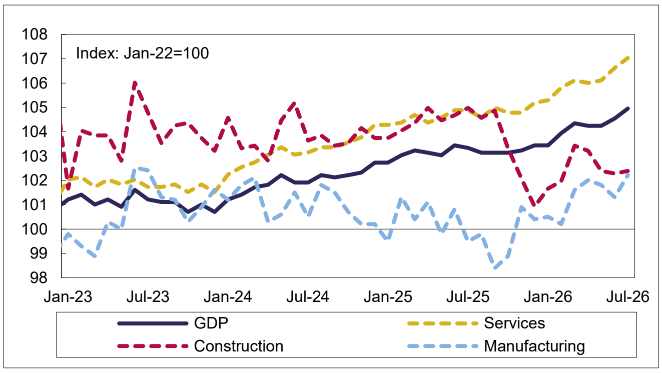
GDP significantly beat expectations in July to suggest unexpectedly solid growth in Q3

After GDP growth in Q2 of 0.4%Q/Q exceeded expectations so that the UK matched the strongest pace in the G7 over the first half of the year, today's monthly data suggested that the positive momentum extended into Q3. Economic output rose for a second successive month in July and by a stronger-than-expected 0.4%M/M, the fastest pace since February. This also maintained the quarterly pace at 0.4%3M/3M, while the annual growth rate accelerated to a 17-month high of 1.6%Y/Y. Contrasting with the underwhelming signals from business surveys, the hard data point to notable resilience to higher energy prices and heightened geopolitical uncertainty. While the monthly data are often subject to revision and the recent profile – with GDP contracting in only one of the past nine months – suggests some payback is likely over coming months, today's data increase the likelihood of another solid quarter of growth in Q3. As a result, we have revised higher our expectation for GDP growth in the current quarter to 0.5%Q/Q, 0.4ppt above the BoE's projection published in July, with risks to our forecast skewed to the upside. MPC policymakers continue to judge that underlying growth momentum is softer than implied by the headline figures. But it may become increasingly difficult to justify that view if activity continues to outperform expectations, not least as the principal sources of growth suggested by the detailed GDP breakdown appear plausible and sustainable.

AI-related demand providing a meaningful boost to activity

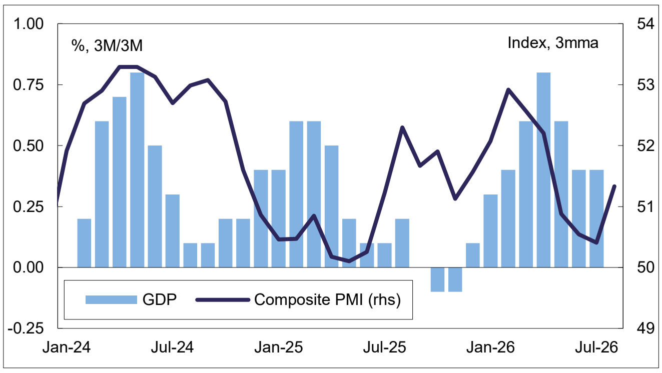
The increase in GDP in July was again driven by the services sector, where output rose 0.4%M/M, marking a fifth monthly gain in six months to be up 0.6%3M/3M. The detail provided further evidence that AI-related demand is providing non-negligible growth momentum, with computer programming, consultancy and related activities expanding for a seventh consecutive month to stand some 13% above the level at the start of the year. Indeed, this category alone contributed 0.12ppt to monthly GDP growth. Scientific R&D activity likewise matched its highest level in 18 months, up 7.0%3M/3M. The AI boost also appeared evident in manufacturing, where production of ICT equipment surged 5.2%M/M to a record high, while output of electrical machinery rose to the highest level in four months. Pharmaceutical production also rose, likely reflecting in part a recovery in demand from the US. And while output of general machinery slipped back in July, momentum on a three-month basis in both subsectors remained positive. Overall, manufacturing production rose 0.9%M/M to its highest level in three years. Admittedly, this strength was largely countered by payback in the volatile mining sector (-4.4%M/M). Meanwhile, likely reflecting ongoing uncertainty in the housing market amid rising mortgage rates as well as higher building costs, construction activity posted minimal growth in July to be down 0.5%3M/3M, with new private and public residential output both contracting sharply over the quarter.

UK: GDP & output by sector



Source: Macrobond and Daiwa Capital Markets Europe Ltd.

UK: GDP growth & composite output PMI

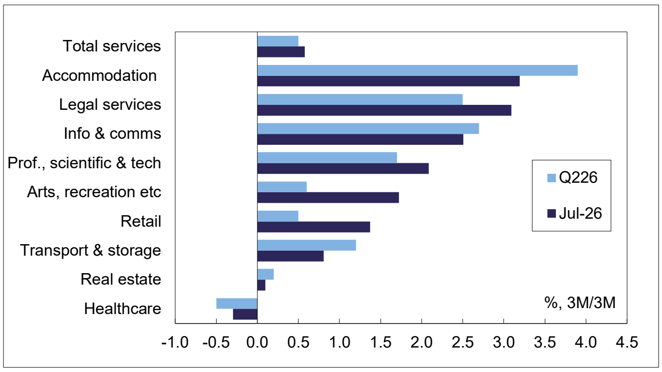


Source: S&P Global, Macrobond and Daiwa Capital Markets Europe Ltd.

Growth in underlying exports outpaced imports in July as EU demand rebounded

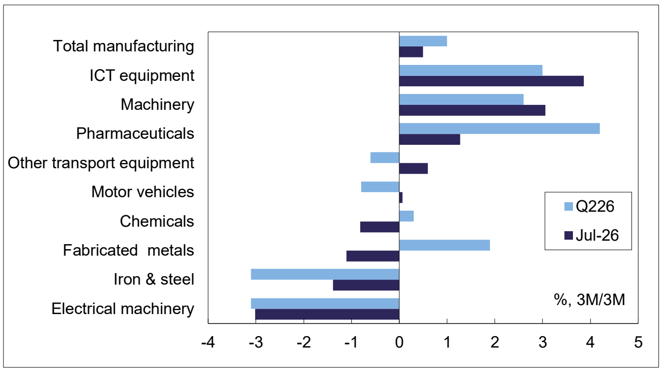
Firm manufacturing growth at the start of Q3 appears to have been accompanied by a further recovery in trade. Excluding precious metals, underlying goods export values rose £0.9bn (2.8%M/M) in July, while volumes increased by £1.3bn (3.5%M/M). Growth was relatively broad-based across the sub-sectors, but strongest for machinery and transport equipment, non-ferrous metals and chemicals. And while the increase in July largely reflected a rebound in shipments to the EU (6.5%M/M), exports to non-EU countries similarly continued to trend higher amid an ongoing recovery in US demand. Underlying goods imports also increased in July, supported by strong imports of cars from China, but at a more modest pace (2.1%M/M) than exports. While export volumes of services edged higher in July, they were marginally outpaced by imports, leaving the real services surplus little changed at an elevated £15.8bn. Trade in precious metals also provided support, with exports rising sharply while imports fell. As a result, total export volumes stood a little more than 1½% above the Q2 average, while import volumes were up just 0.5% on the same basis. As such, the adjusted trade deficit narrowed by £1.2bn to £6.3bn, taking it on a three-month basis (£18.9bn) to the lowest level since February. While monthly trade data are notoriously volatile, the July figures suggest that net trade is adding to growth in Q3 after making a negligible contribution last quarter.

UK: Services output in selected subsectors



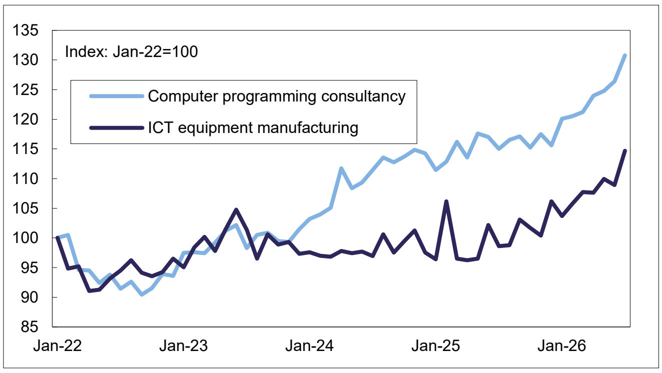
Source: Macrobond and Daiwa Capital Markets Europe Ltd.

UK: Manufacturing output in selected subsectors



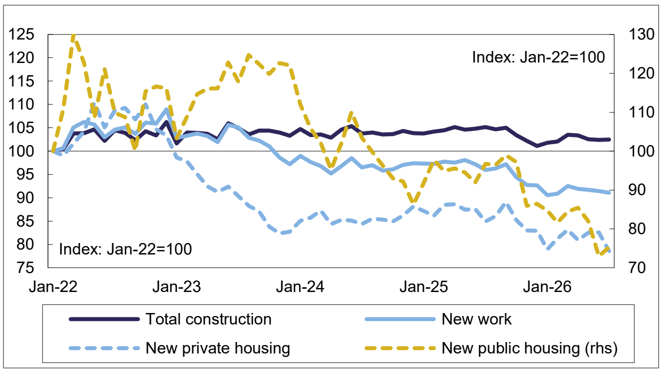
Source: Macrobond and Daiwa Capital Markets Europe Ltd.

UK: AI-related output



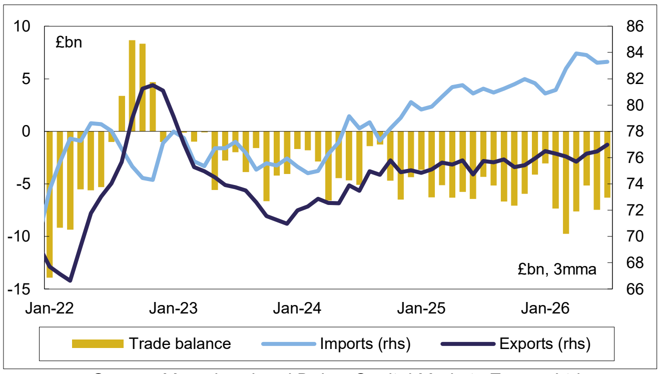
Source: Macrobond and Daiwa Capital Markets Europe Ltd.

UK: Construction output



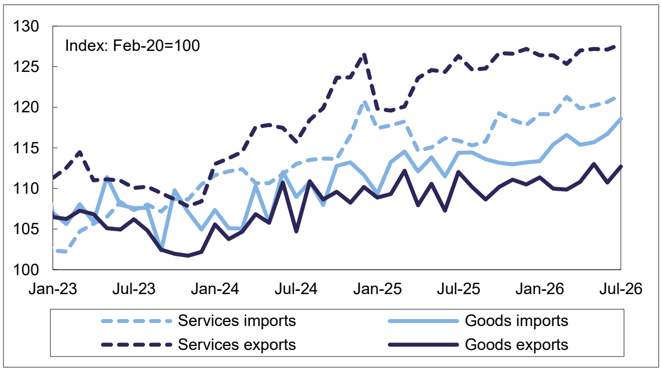
Source: Macrobond and Daiwa Capital Markets Europe Ltd.

UK: Real trade balance, export & import volumes



Source: Macrobond and Daiwa Capital Markets Europe Ltd.

UK: Export & import volumes*



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

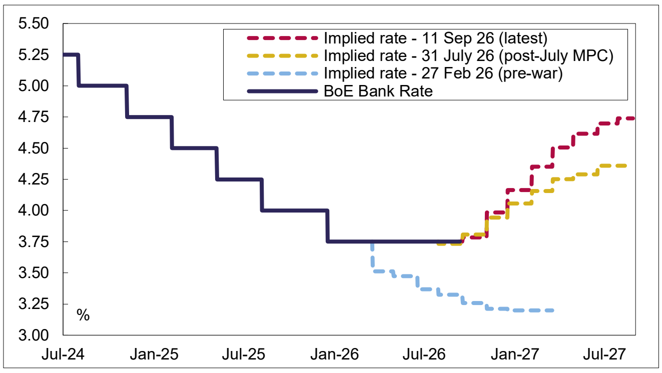
BoE likely to hold Bank Rate, but decision no longer clearcut & a more hawkish tone is inevitable

The firmer than expected GDP growth backdrop, coupled with the recent jump in global energy prices, suggests that Thursday's monetary policy decision from the BoE is now less predictable than it had appeared only a few weeks ago. Indeed, it is no longer far-fetched to imagine that the MPC might follow yesterday's ECB rate hike with one of its own. For now, we still expect the BoE's Monetary Policy Committee to hold rates steady at 3.75% for a sixth consecutive meeting. But the decision could be a tight one. And the MPC's communications are likely to convey a much more hawkish tone than they did in July and flag a willingness to raise Bank Rate as soon as November if the upside risks to the inflation outlook do not subside. While the dissenting camp grew at the last meeting as Mann joined Chief Economist Pill and Green in calling for a 25bps hike, the remaining six members of the MPC showed no urgency to follow. Indeed, Governor Bailey emphasised to journalists at the post-MPC press conference that they should not leave "thinking that the BoE is edging towards a hike". And the majority on the Committee judged that the backdrop of a soft labour market and tighter financial conditions continued to afford the MPC time to monitor the extent of potential second-round effects without moving to a more restrictive stance. Despite stronger-than-expected economic output and an improved labour market survey, the data released since July's meeting should have done little to change that picture. Evidence of second-round effects remains minimal and pay growth has continued to ease. Crucially, key forward-looking indicators like the BoE's DMP and the Bank Agents' assessments have remained relatively stable. And while conducted at the start of August and exaggerated by a change in data provider, the BoE's quarterly inflation attitudes survey today reported a slight softening in consumers' inflation expectations this quarter.

Upside inflation risks bring a November move into focus

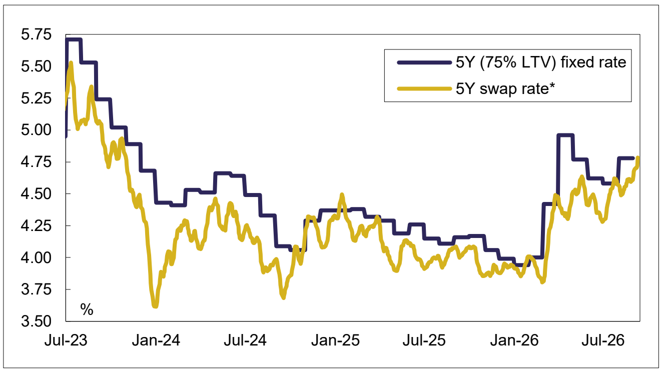
Bailey's comments to MPs earlier this week gave no indication of an imminent shift in his policy view. However, he and his fellow policymakers clearly accepted that the upside risks to the outlook have increased. Escalating tensions in the Middle East have sent wholesale oil and gas prices well above the outdated assumptions embedded in the BoE's July baseline projections. The MPC members also expressed concerns about higher refinery margins on retail fuel prices, AI-related price pressures and the effects of extreme weather events on food inflation next year. The improvement in economic activity data might also now be sufficient for some policymakers to reconsider their assumptions regarding the strength of underlying growth and the risks of greater inflation persistence. And assuming that energy prices follow the paths implied by the latest futures curves, we could see headline inflation rising to 4%Y/Y at the start of 2027, comfortably above the BoE's baseline projection. As a result, we cannot entirely rule out the possibility that one or more rate-setters – perhaps even enough to trigger a surprise hike – could switch their votes as soon as this meeting. In our view, however, the further marked tightening in financial conditions this week should help justify further caution. And with uncertainty remaining high, waiting until November would allow policymakers scope to incorporate developments in energy markets, autumn's wage settlements, swap markets and the fiscal policies included in the 28 October Budget into their updated projections.

UK: Bank Rate & OIS market-implied path



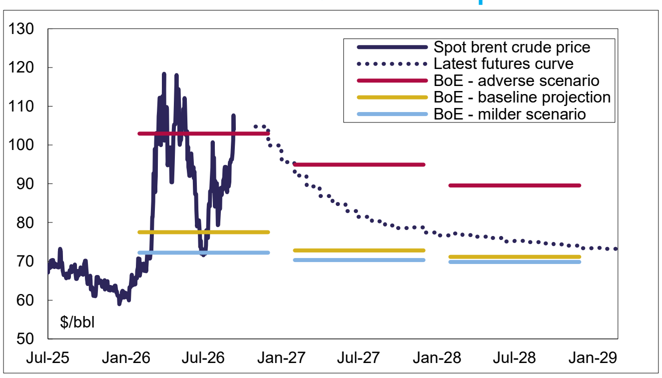
Source: Macrobond, Bloomberg and Daiwa Capital Markets Europe Ltd.

UK: 5Y mortgage & swap rates*



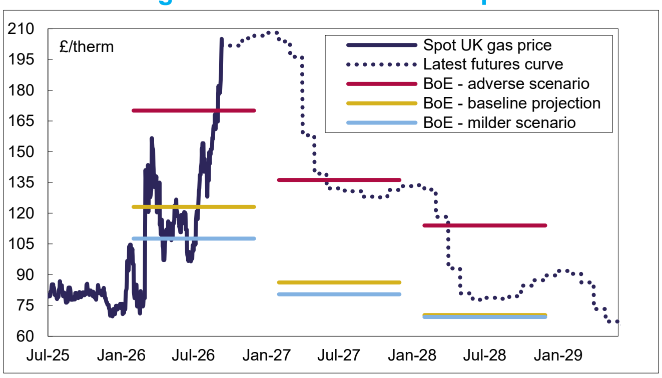
**5-day moving average.*
Source: Macrobond and Daiwa Capital Markets Europe Ltd.

UK: Brent crude futures & BoE assumptions



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

UK: Natural gas futures & BoE assumptions



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

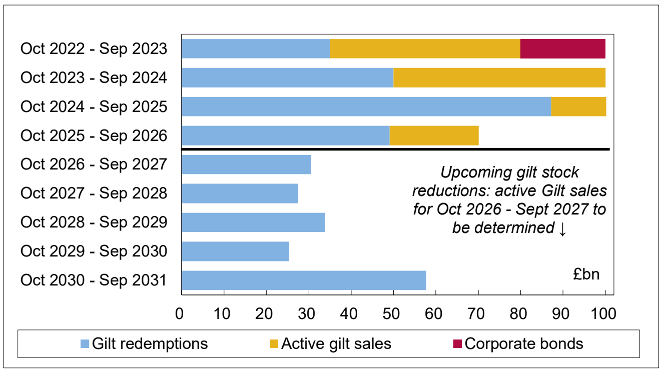
UK inflation and labour market updates to frame the BoE's decision

While updated figures on the UK labour market (Tuesday) and inflation (Wednesday) are unlikely to be decisive to the MPC's decision, they will help to frame the discussions. Indeed, having risen in July owing to a step-up in regulated household energy bills, August's inflation reading is likely to report a similar jump, driven this time by rising auto fuel prices. Overall, we see the headline CPI rate rising to a five-month high of 3.2%Y/Y, up 0.3ppt from July. While predominantly driven by energy components, a BRC survey did hint towards a firm pick up in food inflation. And we also see upside risks to core inflation owing to ongoing pressures in AI-related goods and more pronounced indirect effects, particularly in transport services. However, evidence of broader inflationary pressures is unlikely. And the latest labour market update should provide reassurance that wage growth continues to moderate, with the BoE's preferred series of private sector regular pay remaining particularly subdued at 2.8%Y/Y, a near-6-year low. Hiring sentiment also remains underwhelming, so despite tentative signs of stabilisation in labour market conditions more recently, the risks to the unemployment rate are also likely to be skewed to the upside. Meanwhile, signals from retail surveys also point to a further decline in retail sales volumes in August (Friday). Certainly, the latest rise in fuel prices will pose a headwind to household spending, not least on fuel. And with household incomes set to be squeezed further over the horizon and uncertainty regarding the outlook on the rise, we would be surprised if consumers did not judge that economic conditions had become less favourable since the start of August when consumer confidence (also due Friday) rose to a two-year high.

BoE expected to announce a slower reduction in its Gilt holdings owing to fewer redemptions

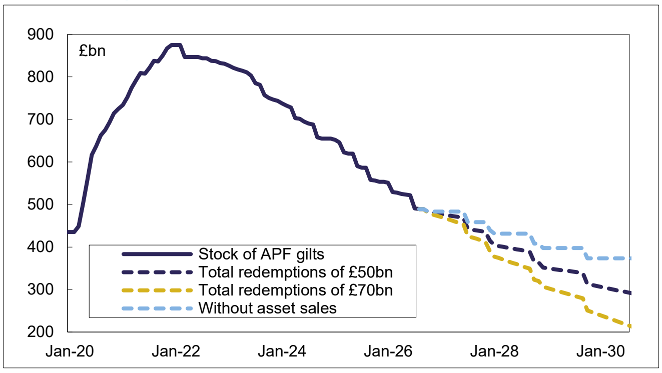
Concurrent with its announcement on interest rates, the MPC is also due to provide an update on its plans for Quantitative Tightening (QT) for the 12 months from October. Last September, the MPC elected to slow its pace of reduction in its stock of Gilt holdings within its Asset Purchase Facility, from £100bn to £70bn. And we, like most market participants, expect that pace to slow again to £50bn. As it was last year, however, that slowdown will predominantly reflect a slower pace of roll-off from maturing Gilts, as opposed to concerns about the market's capacity to absorb additional supply. Indeed, we expect a similar number of active sales (~£20bn) to what was conducted over the past 12 months. Given that the BoE in July revised up its estimate of the impact of QT sales on the 10Y Gilt yield since 2022 to 20-30bps, we would not be surprised if the BoE were to further reduce the share of sales accounted for by longer-dated bonds within that envelope. But it will still be eager to avoid accusations of fiscal dominance, particularly while the BoE's reserves remain sizable. A reduction of £50bn would bring the remaining stock of Gilt holdings in the APF down to around £438bn, 50% below its peak (£875bn) in 2022. All else equal, however, that should still leave the BoE's balance sheet some way above the Bank's range of estimates consistent with an 'ample' reserves regime, as uptake of the new repo facilities has recently seen reserves level off closer £640bn.

UK: APF maturities & sales profile



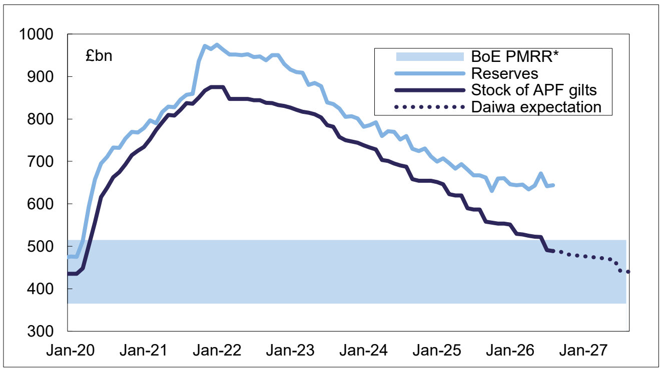
Source: BoE MPR Jul-26 and Daiwa Capital Markets Europe Ltd.

UK: APF gilt stocks & redemption scenarios



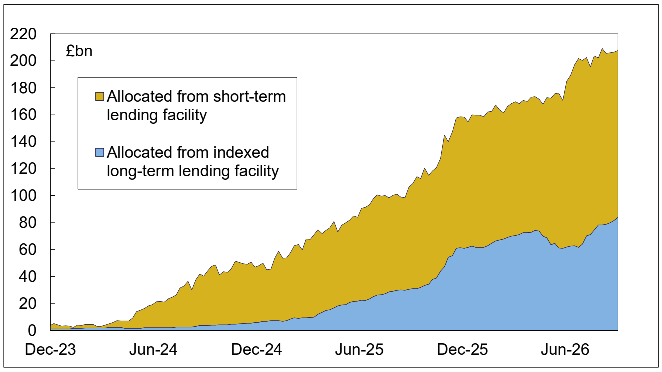
Source: BoE, Macrobond and Daiwa Capital Markets Europe Ltd.

UK: BoE reserves & APF gilt stocks



**Preferred Minimum Range of Reserves estimate as of March 2026.*
Source: BoE, Macrobond and Daiwa Capital Markets Europe Ltd.

UK: Outstanding drawings from BoE repo facilities



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

The week ahead in the euro area

After euro area GDP growth accelerated in Q2 to its fastest pace in four years and surveys point to continued expansion across the region over the summer, the coming week's activity indicators are nevertheless likely to suggest a mixed start to Q3. Despite another notable increase in Irish industrial production (2.7%M/M), declines in Germany and France imply that aggregate euro area industrial output (Wednesday) edged lower in July, by as much as ¼%M/M. Admittedly, this weakness partly reflects a temporary drop in German auto manufacturing amid a single plant shutdown that month for equipment upgrades. While Germany's trade report also highlighted softer intra-euro area shipments during the month, the euro area goods trade figures (Tuesday) should show exports maintaining their upward trend at the start of Q3, supported in part by strong demand from the US. With imports likely to have fallen sharply, the trade surplus is expected to widen markedly, reaching its highest level since February. Meanwhile, euro area construction output (Friday) is also expected to rise in July, although not enough to fully reverse June's steep decline (-1.8%M/M). In addition, the ZEW survey (Tuesday) is likely to reinforce the upbeat message from the past week's Sentix release, which showed investors assessing Germany's economic conditions in September as the most favourable in three years.

In terms of the inflation outlook, final euro area HICP estimates for August (Thursday) are expected to align with the flash release, which showed headline inflation jumping 0.4ppt to a three-year high of 3.3%Y/Y. However, the detail should highlight that the acceleration was energy driven, with the latest prices of fuel up 4%M/M and heating oil up 7½%M/M. Core goods inflation also rose to a 2½-year high of 1.2%Y/Y, likely reflecting some upward pressure on clothing prices due to differences in the timing of seasonal discounting relative to last year, alongside continued strength in AI-related components. The services breakdown will also be scrutinised for confirmation as to whether last month's moderation largely reflected volatile tourism-related categories or a broader easing in underlying price pressures. Elsewhere, the ECB's wage tracker and Q2 labour cost data (both Wednesday) are likely to provide little evidence of significant second-round inflation effects from wages. Job vacancies data (Tuesday) should illustrate the reduced scope for workers to secure stronger pay settlements. And although the ECB's August consumer survey may show a pickup in near-term inflation expectations in response to higher wholesale energy prices, we expect medium-term expectations to remain relatively well contained.

The next Euro wrap-up will be published on Tuesday 15 September 2026

Daiwa economic forecast

	2026				2027		2026	2027	2028
	Q1	Q2	Q3	Q4	Q1	Q2			
GDP	%, Q/Q						%, Y/Y		
Euro area	0.0	0.6	0.2	0.2	0.3	0.4	0.9	1.1	1.4
UK	0.6	0.4	0.5	0.2	0.5	0.3	1.4	1.4	1.4
Inflation, %, Y/Y									
Euro area									
Headline HICP	2.0	3.0	3.2	3.7	3.8	3.1	3.0	3.0	2.0
Core HICP	2.3	2.4	2.5	2.6	2.8	2.8	2.4	2.7	2.2
UK									
Headline CPI	3.1	2.8	3.2	3.6	3.8	3.3	3.1	3.1	1.7
Core CPI	3.2	2.5	2.7	3.0	3.1	3.2	2.9	3.0	2.4
Monetary policy, %									
ECB									
Deposit Rate	2.00	2.25	2.50	2.75	3.00	3.00	2.75	3.00	2.50
Refi Rate	2.15	2.40	2.65	2.90	3.15	3.15	2.90	3.15	2.65
BoE									
Bank Rate	3.75	3.75	3.75	4.00	4.00	4.00	4.00	4.00	3.50

Source: Bloomberg, ECB, BoE and Daiwa Capital Markets Europe Ltd.

Daiwa Capital Markets

The coming week's data calendar

The coming week's key data releases

Country		BST	Release	Period	Market consensus/ *Daiwa forecast*	Previous
Monday 14 September 2026						
- Nothing scheduled -						
Tuesday 15 September 2026						
Euro area		10.00	Trade balance €bn	Jul	-	1.8
		10.00	Final job vacancy rate %	Q2	*2.1*	2.3
Germany		07.00	Wholesale prices M/M% (Y/Y%)	Aug	-	0.2 (5.3)
		10.00	ZEW current situation (expectations) balance	Sep	-52.1 (40.0)	-61.1 (34.2)
France		07.45	Final HICP (CPI) Y/Y%	Aug	*2.7 (2.4)*	2.4 (2.1)
Spain		08.00	Final HICP (CPI) Y/Y%	Aug	*4.5 (4.3)*	3.9 (3.6)
UK		07.00	Average wages (excluding bonuses) 3M/Y%	Jul	3.9 (3.5)	4.1 (3.5)
		07.00	Private sector wages 3M/Y%	Jul	2.8	2.8
		07.00	Unemployment rate 3M%	Jul	5.0	4.9
		07.00	Employment 3M/3M change 000s	Jul	69	84
		07.00	Payrolled employment M/M change 000s	Aug	-10	-13
		07.00	Claimant count rate % (change 000s)	Aug	-	4.3 (-11)
Wednesday 16 September 2026						
Euro area		10.00	Industrial production M/M% (Y/Y%)	Jul	*-0.2 (-0.1)*	0.0 (0.1)
		10.00	Final labour costs Y/Y%	Q2	*3.1*	3.2
Italy		09.00	Final HICP (CPI) Y/Y%	Aug	*3.2 (3.3)*	2.9 (2.9)
UK		07.00	Headline (core) CPI Y/Y%	Aug	*3.2 (2.8)*	2.9 (2.6)
		07.00	PPI – output (input) prices Y/Y%	Aug	3.5 (5.4)	3.1 (4.9)
		09.30	House price index Y/Y%	Jul	-	2.0
Thursday 17 September 2026						
Euro area		10.00	Final headline (core) HICP Y/Y%	Aug	*3.3 (2.4)*	2.9 (2.5)
UK		12.00	BoE Bank Rate %	Sep	*3.75*	3.75
Friday 18 September 2026						
Euro area		09.00	ECB consumer expectations survey - 1Y (3Y) ahead CPI Y/Y%	Aug	3.0 (2.8)	2.9 (2.7)
		09.00	ECB current account €bn	Jul	-	35.1
		10.00	Construction output M/M% (Y/Y%)	Jul	-	-1.3 (-0.7)
Germany		07.00	PPI Y/Y%	Aug	3.9	3.0
UK		00.01	GfK consumer confidence indicator	Sep	-16	-14
		07.00	Retail sales - incl. auto fuels M/M% (Y/Y%)	Aug	-0.2 (1.9)	-0.5 (1.6)
		07.00	Retail sales - excl. auto fuels M/M% (Y/Y%)	Aug	-0.2 (1.9)	-0.9 (2.3)

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

The coming week's key events & auctions		
Country	**BST**	**Event / Auction**
		Monday 14 September 2026
Euro area	10.15	ECB's Schnabel gives keynote speech to a symposium on European competitiveness in Berlin
	16.15	ECB President Lagarde gives keynote speech on the European economy and resilience in Vienna
		Tuesday 15 September 2026
Germany	10.30	Auction: to sell up to €5bn of 2.7% 2028 bonds
UK	10.00	Auction: to sell £1.25bn of 0.5% 2029 bonds
	10.00	Auction: to sell £750mn of 4.25% 2040 bonds
		Wednesday 16 September 2026
Euro area	09.00	ECB to publish wage tracker update
Germany	10.30	Auction: to sell up to €1bn of 3.4% 2047 bonds
	10.30	Auction: to sell up to €1.5bn of 2.9% 2056 bonds
		Thursday 17 September 2026
Euro area	11.00	ECB Governing Council member and Bank of Finland Governor Rehn to participate in a roundtable discussion in London
France	10.50	Auction: to sell2.4% 2029, 2.7% 2031, 3.25% 2032, 2% 2032 bonds, & 2.1% 2037 inflation-linked bonds
Spain	09.30	Auction: to sell 0.7% 2032, 3.45% 2034 & 3.4% 2036 bonds
UK	12.00	BoE monetary policy announcement, statement & minutes to be published
	12.00	BoE to publish market notice regarding APF gilt sales for the 12 months from October
		Friday 18 September 2026
Euro area	10.15	ECB President Lagarde to join press conference following informal ECOFIN meetings in Dublin

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

Today's European calendar

Today's results

Economic data

Country	Release	Period	**Actual**	Market consensus/ *Daiwa forecast*	Previous	Revised
Italy	Unemployment rate %	Q2	**5.6**	-	5.3	5.5
UK	Monthly GDP M/M% (3M/3M%)	Jul	**0.4 (0.4)**	*0.1 (0.3)*	0.3 (0.7)	-
	Services output M/M% (3M/3M%)	Jul	**0.4 (0.6)**	0.0 (0.5)	0.4 (0.5)	-
	Industrial output M/M% (Y/Y%)	Jul	**0.2 (0.6)**	-0.2 (0.2)	-0.2 (-0.2)	-
	Construction output M/M% (Y/Y%)	Jul	**0.1 (-2.5)**	0.1 (-2.3)	-0.1 (-2.3)	-
	Trade (goods trade) balance £bn	Jul	**-3.5 (-21.0)**	-5.0 (-22.4)	-5.5 (-23.0)	-
	BoE/Ipsos inflation attitudes survey - 1Y ahead CPI Y/Y%	Q3	**3.2**	-	4.0	-

Auctions

Country	Auction
	- Nothing to report -

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

Access our research reports at:
https://www.uk.daiwacm.com/ficc-research/research-reports