Euro wrap-up

Overview

- Bunds followed the global trend lower as German PPI inflation jumped to the highest level in more than three years and household inflation expectations ticked higher.
- Gilts underperformed as UK retail sales beat expectations to maintain this year’s steady uptrend.
- The coming week’s European data focus will be on September consumer and business surveys, including the flash PMIs.

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Daily bond market movements

Bond	Yield	Change
BKO 2.7 09/28	3.273	+0.054
OBL 2.9 10/31	3.354	+0.055
DBR 3 08/36	3.515	+0.041
UKT 4 05/29	4.835	+0.102
UKT 4⅛ 03/31	4.904	+0.097
UKT 4⅞ 07/36	5.294	+0.072

*Change from close as at 5.00pm BST.
Source: Bloomberg

Euro area

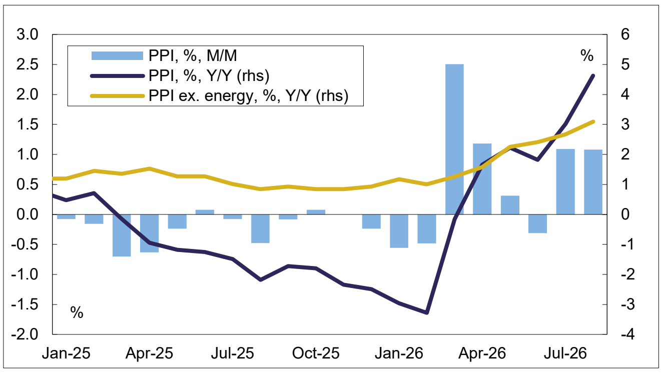
German producer prices jump on renewed energy cost pressures

The inflationary impact of higher wholesale energy prices over the summer was evident in today’s German producer price data. Factory prices rose a steeper-than-expected 1.1%M/M in August, matching July’s increase, to be up 4.6%Y/Y, the most since April 2023, and 6% since the start of the conflict at end-February. Producer energy prices rose a further 3.2%M/M to be 15% higher than at the start of the conflict. And refined petroleum product prices were up more than 40% over the same period. But today’s release provided only limited evidence that these cost pressures are being passed through the supply chain. Indeed, the monthly rise in non-energy producer prices was more modest (0.24%M/M). This nevertheless marked the ninth successive increase and pushed core PPI inflation (excluding energy) up to 3.1%Y/Y, similarly the highest in more than three years. Prices of intermediate goods continue to provide the clearest reflection of the energy shock, being up 6.1%Y/Y, the most since February 2023, with more pressure in the energy-intensive basic metals subsector (1.7%M/M) to leave such prices up almost 6% since the start of the conflict. And while producer prices of chemicals fell for a second month in August, they were still 8.6% above their level in February, with prices of chemical derivatives of hydrocarbons up by one third on the same basis.

Cost pressures yet to be fully reflected in prices of capital goods, food & other consumer items

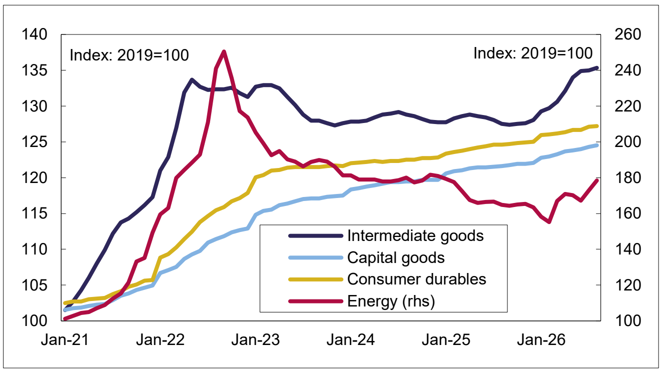
Among the other major categories, capital goods prices remained relatively well-behaved, rising 0.2%M/M in August and 1.3% cumulatively since February. Nevertheless, this pushed the annual rate up to 2.7%Y/Y, the highest in more than two years. There was also further evidence of AI-related price pressures, with producer prices of electronic components and boards and computers rising 15%Y/Y and 17%Y/Y respectively. However, the monthly rise in producer prices of consumer durables slowed to 0.1%M/M in August, to be up cumulatively less than 1% since February and 2.1%Y/Y. And encouragingly for households, producer prices of consumer non-durables were still down 2%Y/Y, thanks to a substantive ongoing drag from food (-3.8%Y/Y). Nevertheless, food prices rose in August for the first month in four (0.3%M/M) due not least to higher prices of meat. We expect the summer drought and increased energy costs to feed through steadily to higher food inflation by the new year. And while wage growth remains moderate, we expect German consumer core goods inflation to move gradually higher from its near-2 ½-year high in August as increased costs of energy and intermediate goods are passed on further to customers.

Germany: Producer price inflation



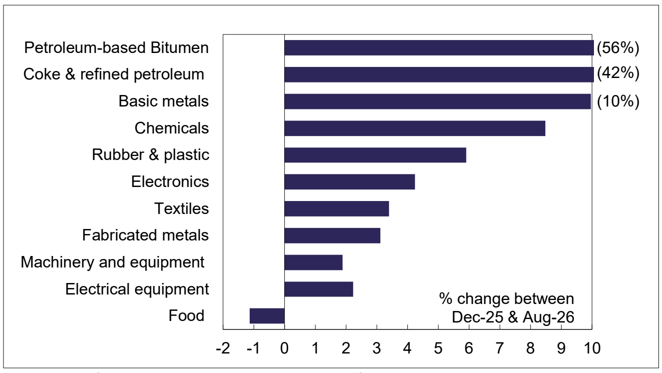
Source: Macrobond and Daiwa Capital Markets Europe Ltd.

Germany: Producer price levels



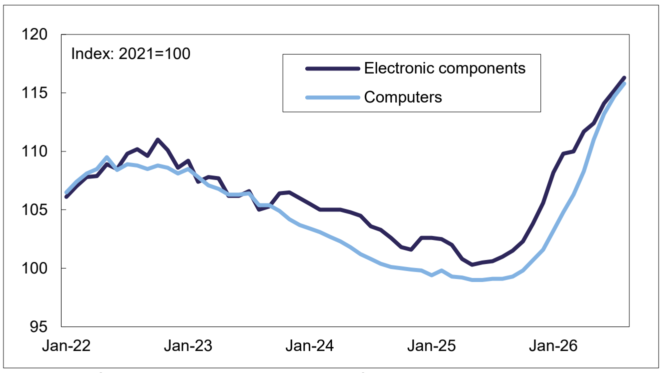
Source: Macrobond and Daiwa Capital Markets Europe Ltd.

Germany: YTD change in producer prices



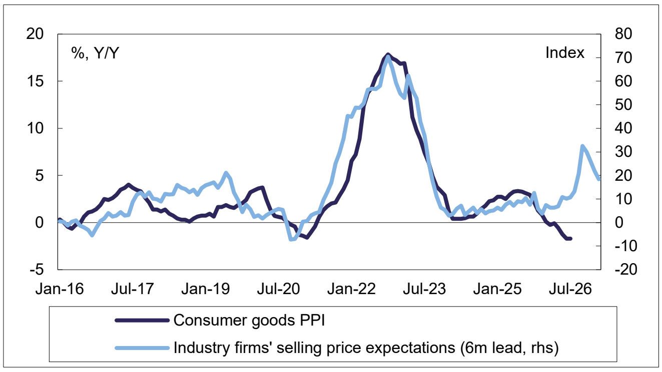
Source: Macrobond and Daiwa Capital Markets Europe Ltd.

Germany: AI-related producer prices



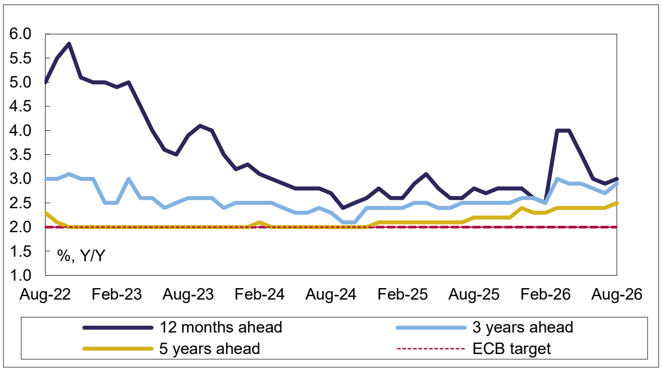
Source: Macrobond and Daiwa Capital Markets Europe Ltd.

Germany: PPI inflation & price expectations



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

Euro area: Consumer inflation expectations



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

Consumer inflation expectations remain contained despite rise in medium-term measures

For now, at least, households appear relatively sanguine about the inflationary implications of the energy price shock. According to the ECB's Consumer Expectations Survey, the median euro area inflation expectation for the next 12 months increased only modestly in August, up 0.1ppt to 3.0%Y/Y, a full percentage point below the peak reached in March and April. Expectations three years ahead also remained below March's high, despite rising 0.2ppt to 2.9%Y/Y. Nevertheless, ECB policymakers are likely to take note of the continued firming in medium-term inflation expectations, for which the median forecast for CPI five years ahead edged up a further 0.1ppt to new series high of 2.5%Y/Y. Taken together, today's releases suggest no need for Governing Council members to panic. But they will remain mindful that the longer energy prices remain high, the greater the risks of broader and more persistent inflationary pressures to come. And comments from certain ECB policymakers today, including the Governors from Latvia, Croatia and Slovakia, suggest that if economic activity and employment remain resilient, they will happily tighten policy into restrictive territory at the end of the year and again in 2027 to ward off those risks.

Despite support from Germany, euro area construction output flatlined in July

As for industrial production, July's euro area data for construction output underwhelmed. Production in the sector was unchanged on the month. So, given the steep decline in June (-1½%M/M), that left it tracking 1% below the Q2 average. The absence of any rebound could perhaps be attributed to the extreme heatwaves which afflicted several member states over the summer and led to destructive wildfire outbreaks in France and Spain. Over June and July, construction output was down cumulatively by 3% in France, 3.5% in Italy and 1.1% in Spain. Germany, on the other hand, fared slightly better. Output in that member state was down just 0.3% over the same period following a partial rebound in July (0.9%M/M). German construction growth in July was broad-based but again led by civil engineering activity (1.4%M/M), reflective of the support provided by higher infrastructure investment. By Eurostat's measure, that placed German civil engineering output at a record high in July, up 6.4%Y/Y. August's construction PMIs also hint at further support from Germany midway through Q3. Indeed, the headline activity index jumped by 6.6pts to 48.7, an eight-month high, in that instance led by improvements in subsectors beyond civil engineering. However, sharp declines in the construction PMIs in France and Italy, to 5½- and 4-year lows respectively, imply that further weakness elsewhere could dampen any impact on regional output. And while cooler temperatures towards the end of August might have facilitated a rebound in Southern Europe, rising materials costs and tightening financial conditions are set to provide greater headwinds. As such, the prospects of achieving a second successive quarter of euro area construction output growth appears relatively slim in Q3.

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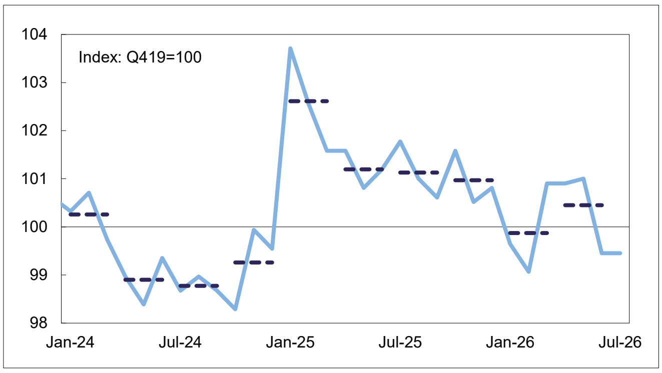
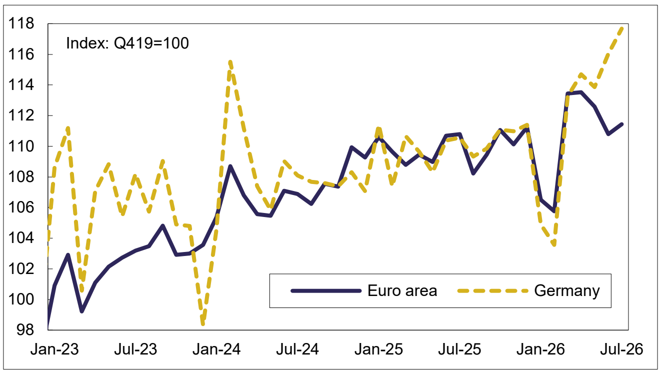
Euro area: Construction output*



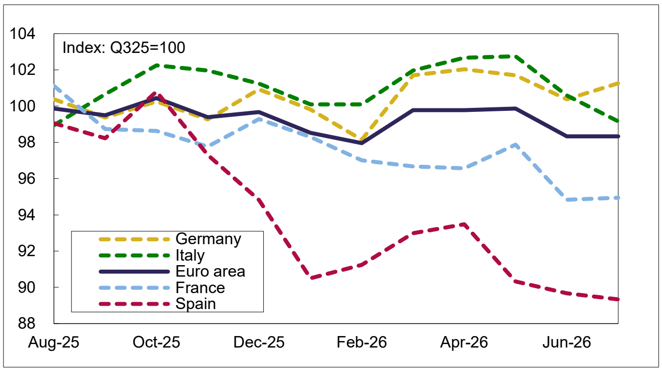
**Dashed lines represent quarterly averages.*
Source: Macrobond and Daiwa Capital Markets Europe Ltd.

Euro area & Germany: Civil engineering output



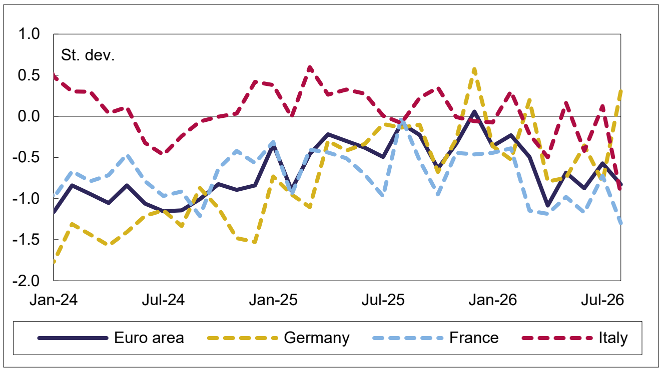
Source: Macrobond and Daiwa Capital Markets Europe Ltd.

Euro area member states: Construction output



Source: Macrobond and Daiwa Capital Markets Europe Ltd.

Euro area & member states: Construction PMI



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

The week ahead in the euro area

The euro area dataflow over the coming week will be predominantly focused on September's business and consumer sentiment surveys with the flash PMIs (Wednesday) likely to attract most headlines. The headline composite output PMI moved sideways in August (52.0) but nevertheless matched the highest level since last November, almost 3pts better than the Q2 average. The employment index suggested the firmest job growth in 10 months (50.8) consistent with firmer demand, with new export orders reportedly up for the first month in 4½ years. That improvement principally reflected assessments from German manufacturers whose own expansion led the euro area manufacturing output PMI to its highest level since the 2022 energy shock (53.3). And though services activity in the core member states reportedly slipped further into contraction, the effect on the respective euro area index (51.6) was largely offset by strength in the periphery, likely in part owing by tourism. Those factors, however, could weaken in September. And the latest rise in global energy prices seems bound to reassert pressure on firms' input prices and potentially selling prices too. So, overall, we see the risks to the flash activity PMIs as skewed slightly to the downside. But it's notable that the more comprehensive German ifo and French INSEE surveys (both Thursday) have pointed to greater resilience in services activity than the PMIs, and their September results should again be afforded weight in assessing economic conditions at the end of Q3.

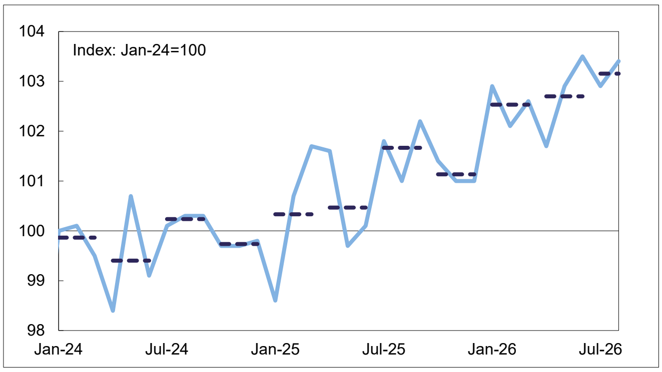
Consumer survey updates from Germany (Friday) and France (Thursday) will also add colour to the Commission's flash euro area confidence estimate (Tuesday). Despite remaining subdued compared to its pre-war mark, the headline indicator edged up to a six-month high in August (-15.5), helped by less pessimism in Germany. But rising uncertainty, higher energy prices and tighter financial conditions also suggest that the risks this month are skewed to the downside. In Germany, political uncertainty could be an additional headwind, given the far-right AfD's strong performance in Saxony-Anhalt. As it was on that occasion, elections this weekend in Berlin and Mecklenburg-Vorpommern are unlikely to be critical for Chancellor Merz. However, with the CDU/CSU polling in the high single digits in the latter, there has been speculation as to whether his party will even manage to surpass the 5% threshold needed to attain representation. Failing to do so would be an embarrassment for Merz, perhaps increasing the (still outside) probability that he might resign as Chancellor before more consequential state elections in 2027. Meanwhile, in terms of activity data, euro area bank lending statistics (Friday) are unlikely to contradict the ECB's view that policy over the summer was hardly restrictive. Final Q2 GDP estimates from Spain (Friday) will also be expected to affirm that member state's continued outperformance, with preliminary estimates suggesting that growth accelerated to 0.7%Q/Q

UK

Retail sales continue to defy expectations with uptrend still firm in August

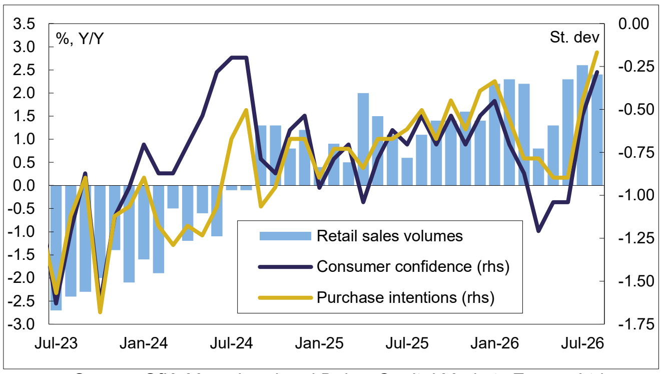
UK retail sales, like GDP growth, has repeatedly surprised on the upside this year. And contrary to expectations of a second successive monthly decline for the first time in 2026, retail sales volumes rebounded in August, rising 0.5%M/M to reverse the prior month's dip. As a result, sales were up 0.9%3M/3M and 2.4%3M/Y, underscoring the positive trend. Unchanged sales in September would leave them up 0.5%Q/Q in Q3, in line with the average pace in the first half of the year and matching our forecast for GDP this quarter. Given the surge in petrol and diesel prices in August, auto fuel sales again fell back that month to be down 2½%3M/3M. But all other major categories grew. On a three-month basis, growth remained particularly strong in non-store (i.e. largely online) sales (more than 5%3M/3M), buoyed not least by the effects of hot weather (e.g. on sales of air conditioners) and the FIFA World Cup (e.g. on sportswear). But growth in sales at general clothes stores and food stores was also solid, above ½%3M/3M, supported by very subdued inflation in both categories. Looking ahead, with nominal pay growth moderating, job growth absent and household energy bills set to rise in October and again more sharply in January, real household income growth will slow over the near term. And while consumer confidence rose last month to a two-year high in part reflecting optimism related to Keir Starmer's replacement as Prime Minister by Andy Burnham, we suspect that recovery in sentiment will not last the new administration's first Budget announcement at the end of next month. So, we expect growth in retail sales and broader consumer spending to moderate in Q4 and Q1, albeit still probably avoiding a shift into reverse gear as long as unemployment does not suddenly jump sharply higher.

UK: Retail sales*



**Volume terms. Dashed lines represent quarterly averages.*
Source: Macrobond and Daiwa Capital Markets Europe Ltd.

UK: Retail sales growth & consumer confidence



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

The week ahead in the UK

September's flash PMIs (Wednesday) will also provide the highlight of the coming week's UK dataflow. As in the euro area, the survey has brightened in recent months. Future production expectations have improved while a further pickup in activity in the dominant services sector pushed up the composite output PMI to a four-month high in August (52.5). That left the index trending more than 2pts above its Q2 average thus far in Q3, consistent with an acceleration in underlying GDP growth. The minutes from this week's MPC meeting showed that monetary policymakers are mindful of these signals of resilient activity. And while labour slack persists, the 10-month high in the employment PMI (48.9) was also potentially a signal of stabilizing job market conditions. However, the MPC should be cautious not to overinterpret the signals from the PMIs in isolation, as they have provided a poor guide to recent official GDP growth data. Nevertheless, the price PMIs should be watched, having already remained elevated even before the latest rise in global energy prices.

Meanwhile, the CBI's industrial trends survey (Tuesday) will provide a timelier signal on any shifts in manufacturers' price-setting and demand ahead of the PMIs. And a separate CBI survey will provide a first signal regarding September's retail sales (Thursday), although this survey has recently been excessively downbeat compared to the official data. The GfK consumer survey (Friday) may provide a more reliable signal, having reported confidence at a two-year high in August (-14) and the best major purchase intentions since December 2021. The risks to that release are likely skewed to the downside, however, given the higher inflation sparked by reescalation in the Middle East. Surveys aside, the week ahead will also bring an update on public borrowing (Friday). Higher-than-forecast debt interest payments have contributed to a modest overshoot which is unlikely to have improved through August. That release will provide an excuse to speculate about how Chancellor Healey might restore his headroom within the fiscal rules at next month's Budget (28 October). Lastly, Thursday will be a key date for BoE-speak with swing voters and Deputy Governors Breeden and Lombardelli as well as the uber-dove Swati Dhingra due to speak publicly.

The next Euro wrap-up will be published on Tuesday 22 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	3.3	3.8	3.9	3.3	3.0	3.1	2.0
Core HICP	2.3	2.4	2.4	2.6	2.8	2.7	2.4	2.7	2.2
UK									
Headline CPI	3.1	2.8	3.1	3.5	3.7	3.2	3.1	3.0	1.7
Core CPI	3.2	2.5	2.6	2.8	3.0	3.0	2.8	2.9	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.

The coming week's data calendar

The coming week's key events & auctions		
Country	BST	Event / Auction
		Monday 21 September 2026
		- Nothing scheduled -
		Tuesday 22 September 2026
Germany	10.30	Auction: to sell up to €5bn of 2.9% 2031 bonds
UK	10.00	Auction: to sell £4.75bn of 4.625% 2032 bonds
		Wednesday 23 September 2026
Euro area	17.30	ECB Chief Economist Lane to deliver lecture on 'Monetary Policy in the Euro Area' at the ICMB, Geneva
Germany	10.30	Auction: to sell up to €1bn of 3.4% 2047 bonds
	10.30	Auction: to sell up to €1bn of 2.9% 2056 bonds
		Thursday 24 September 2026
Euro area	09.00	ECB to publish Economic Bulletin 6/2026
Italy	10.00	Auction: to sell inflation-linked bonds
UK	10.30	External MPC member Dhingra to speak on a monetary policy outlook panel at the London Macro Policy Forum
	14.30	BoE Deputy Governor Breeden to speak in fireside chat at the London Macro Policy Forum
	15.00	BoE Deputy Governor Lombardelli to deliver a keynote speech at a research conference in Poland
		Friday 25 September 2026
Euro area	19.00	ECB Vice President Vujicic to speak on a policy panel at an inflation conference hosted by the Cleveland Fed & ECB in Ohio

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

The coming week's key data releases						
Country		BST	Release	Period	Market consensus/ *Daiwa forecast*	Previous
			Monday 21 September 2026			
UK		00.01	Rightmove house prices M/M% (Y/Y%)	Sep	-	-2.0 (-1.0)
			Tuesday 22 September 2026			
Euro area		15.00	Preliminary Commission consumer confidence indicator	Sep	-16.0	-15.5
UK		07.00	Public sector net borrowing £bn	Aug	15.6	1.8
		11.00	CBI industrial trends - total orders (selling prices) net % balance	Sep	-	-25 (22)
			Wednesday 23 September 2026			
Euro area		09.00	Preliminary services (manufacturing) PMI	Sep	51.4 (52.6)	51.6 (52.7)
		09.00	Preliminary composite PMI	Sep	51.6	52.0
Germany		08.30	Preliminary services (manufacturing) PMI	Sep	49.9 (54.0)	49.7 (54.3)
		08.30	Preliminary composite PMI	Sep	51.8	51.8
France		08.15	Preliminary services (manufacturing) PMI	Sep	48.3 (50.9)	48.0 (51.1)
		08.15	Preliminary composite PMI	Sep	48.7	48.5
UK		09.30	Preliminary services (manufacturing) PMI	Sep	52.0 (51.4)	52.5 (51.7)
		09.30	Preliminary composite PMI	Sep	52.0	52.5
			Thursday 24 September 2026			
Euro area		05.00	New car registrations Y/Y%	Aug	-	12.7
Germany		09.00	ifo business climate indicator	Sep	89.0	88.8
		09.00	ifo current assessment (expectations) indicator	Sep	89.0 (89.3)	88.5 (89.1)
France		07.45	INSEE consumer confidence indicator	Sep	85	86
		07.45	INSEE business (manufacturing) confidence indicator	Sep	98 (103)	98 (103)
		07.45	INSEE production (own-company production) outlook indicator	Sep	-	-11 (9)
Spain		08.00	PPI Y/Y%	Aug	-	9.2
UK		11.00	CBI distributive trades survey - reported retail sales % net balance	Sep	-	-48
			Friday 25 September 2026			
Euro area		09.00	M3 money supply Y/Y%	Aug	3.5	3.4
Germany		07.00	GfK consumer confidence indicator	Oct	-27.4	-26.6
France		07.45	Final wages Q/Q%	Q2	*0.7*	0.7
Spain		08.00	GDP - final estimate Q/Q% (Y/Y%)	Q2	*0.7 (2.7)*	0.6 (2.7)
UK		00.01	GfK consumer confidence indicator	Sep	-16	-14

Source: Bloomberg 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		ECB consumer expectations survey - 1Y (3Y) ahead CPI Y/Y%	Aug	**3.0 (2.9)**	3.1 (2.8)	2.9 (2.7)	-
		ECB current account €bn	Jul	**27.6**	-	35.1	-
		Construction output M/M% (Y/Y%)	Jul	**0.0 (-2.0)**	-	-1.3 (-0.7)	-1.5 (-1.4)
Germany		PPI Y/Y%	Aug	**4.6**	3.9	3.0	-
UK		Retail sales - incl. auto fuels M/M% (Y/Y%)	Aug	**0.5 (2.4)**	-0.2 (1.9)	-0.5 (1.6)	- (1.2)
		Retail sales - excl. auto fuels M/M% (Y/Y%)	Aug	**0.6 (2.7)**	-0.2 (1.9)	-0.9 (2.3)	- (1.8)

Auctions

Country	Auction
- Nothing to report -	

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

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