Euro wrap-up

Overview

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- While the ifo survey echoed the flash PMIs in signalling a further strengthening in German economic growth momentum, longer-dated Bunds made losses.
- Gilts also made losses as certain BoE MPC members flagged that a longer-lasting energy price shock would likely strengthen the case for monetary tightening.
- Friday will bring euro area bank lending data as well as consumer confidence survey results from Germany and UK.

Daily bond market movements

Bond	Yield	Change
BKO 2.7 09/28	3.315	-0.007
OBL 2.9 10/31	3.435	+0.024
DBR 3 08/36	3.597	+0.045
UKT 4 05/29	4.906	+0.004
UKT 4⅛ 03/31	4.974	+0.016
UKT 4⅞ 07/36	5.380	+0.035

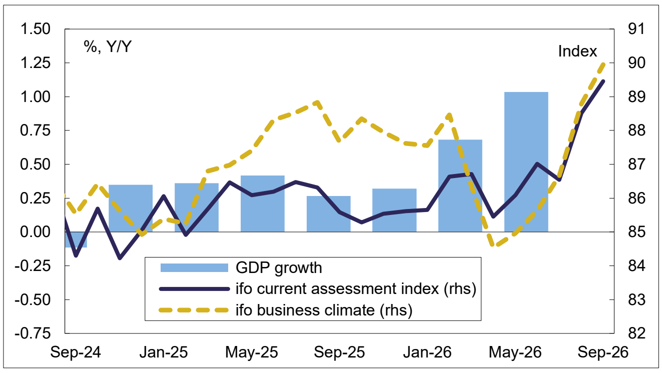
*Change from close as at 5:00pm BST.
Source: Bloomberg

Euro area

Ifo survey tallies with flash PMIs to signal strengthening German growth momentum

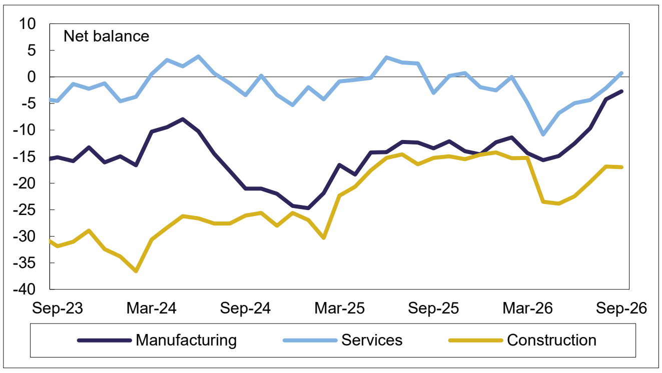
The signal of stronger underlying growth momentum in yesterday's flash PMIs was broadly echoed in today's German ifo survey results. Indeed, just as the euro area composite PMI rose more than anticipated this month to the highest level in more than three years, the ifo business climate index rose a greater than expected 1.1pt in September to 89.9, the best since May 2023. Encouragingly too, according to the ifo survey, current conditions were considered the most favourable since late 2023. And the outlook for the coming six months was judged the best since last November, well before the war in Iran darkened prospects. Unlike the German composite PMI, which also rose to the highest level since last autumn, each of the headline ifo indices remained well below their long-run averages. But their upwards trend suggests that the German economic recovery should be sustained into 2027. And like the PMIs, the detail implies that the expansion should be relatively broad-based. Buoyed by expectations in the electrical engineering subsector, which more than offset continued pessimism in autos, the business climate in manufacturing was considered the best in more than three years. Services were the most upbeat since last autumn while the business climate in retail was considered the best since before the start of the war in Iran. And while construction firms failed to signal substantive improvement in the sector, the ifo institute reported continued optimism in civil engineering surrounding increased public investment. Given a softer start to the quarter and supply strains caused by the continually low Rhine water level as well as the conflict in the Middle East, we currently expect a moderation in German GDP growth in Q3 to 0.2%Q/Q, which would be the softest rate in four quarters. But assuming no new adverse shocks, this week's surveys also point to a reacceleration in Q4 to around 0.4%Q/Q to take full-year growth above 1%Y/Y, which would comfortably mark the best year for German growth since 2022.

Germany: GDP growth & ifo survey indices



Source: Macrobond and Daiwa Capital Markets Europe Ltd.

Germany: ifo business climate indices by sector

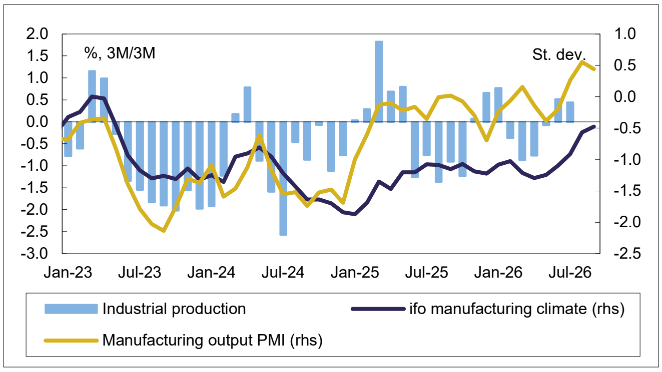


Source: Macrobond and Daiwa Capital Markets Europe Ltd.

INSEE survey flags softer French sentiment but remains consistent with modest growth in Q3

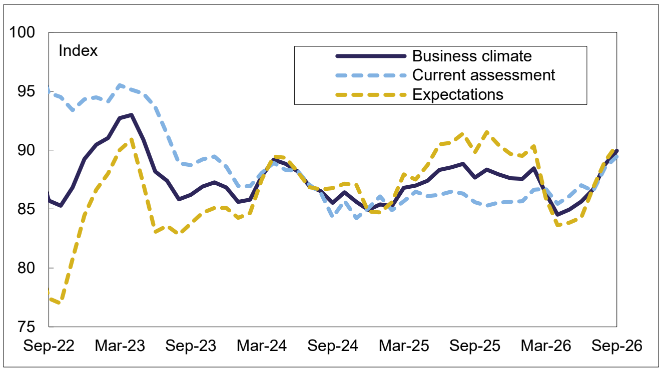
In contrast to the broadly upbeat German survey and the improvement in yesterday's French flash PMIs, today's INSEE sentiment indicators painted a somewhat less favourable picture of economic conditions at the end of Q3. The headline composite business climate index fell for the first month in three in September, by 2pts to 96.4, its lowest level since June and around 3½% below the long-run average. Nevertheless, the average quarterly index for Q3 remained almost 3pts above its Q2 level, consistent with modestly positive GDP growth this quarter of 0.1%Q/Q. Part of the divergence between the INSEE survey and PMIs likely reflects the inclusion of the retail and construction sectors in the former. Indeed, in September, the weakness was driven largely by a marked deterioration in retail sentiment, as firms reported softer recent and expected sales volumes. That tallied with persistently weak consumer confidence, which remained well below historical norms as household willingness to make major purchases hovered near recent lows. By and large, services firms were also less upbeat reflecting concerns about demand. However, the outlook for hospitality-related subsectors improved sharply, with firms signalling a rebound after being adversely affected by the summer heatwave. Meanwhile, despite higher borrowing costs, conditions in the construction sector remained broadly stable, with activity over the past month judged to be the best since May. And the manufacturing index held steady in September for a third successive month at an above-average 101. Despite strong recent growth in sales of EVs, manufacturers of autos revised down their assessment of the outlook for production. But consistent with survey indicators in other countries, French producers of ICT equipment judged the outlook to be the most favourable in more than 2½ decades, benefitting from the global AI-driven investment boom

Germany: Industrial production & survey indices



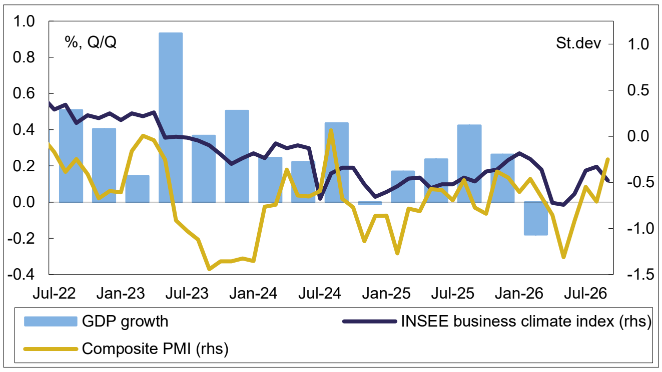
Source: S&P Global, Macrobond and Daiwa Capital Markets Europe Ltd.

Germany: ifo business survey indices



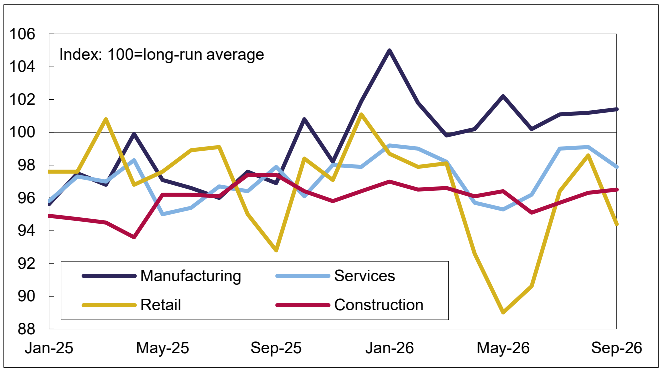
Source: Macrobond and Daiwa Capital Markets Europe Ltd.

France: GDP growth & sentiment indices



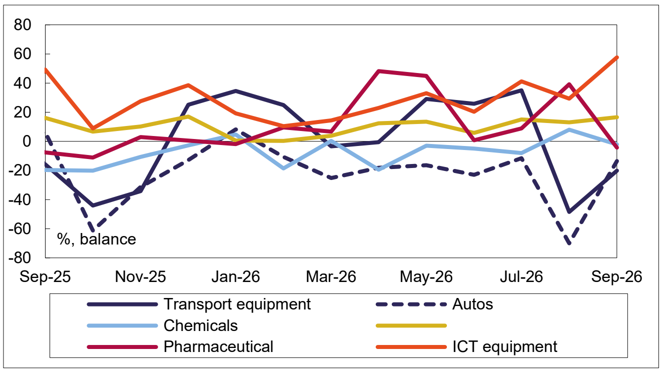
Source: INSEE, S&P Global, Macrobond and Daiwa Capital Markets Europe Ltd.

France: Business sentiment indices



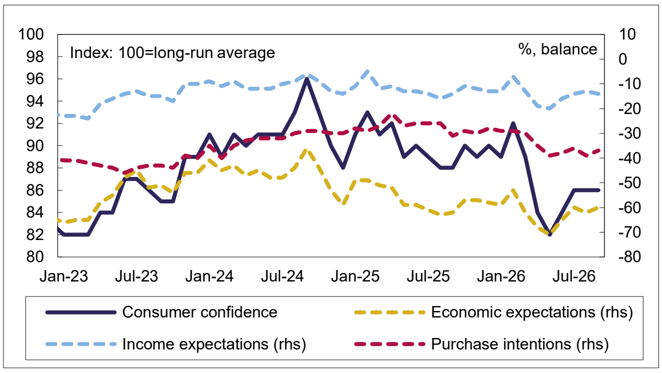
Source: INSEE, Macrobond and Daiwa Capital Markets Europe Ltd.

France: Selected manufacturing sentiment indices*



**Recent output. Source: INSEE, Macrobond and Daiwa Capital Markets Europe Ltd.*

France: Consumer confidence indices



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

The day ahead in the euro area

There are a handful of noteworthy data releases scheduled at the end of the week, including euro area monetary statistics and a consumer survey from Germany. The former will provide an update on bank lending activity in August, which is likely to have displayed further resilience ahead of the ECB's latest policy decision. Indeed, lending flows in July appeared little affected by the ECB's decision to raise interest rates for the first time in nearly three years. Net mortgage lending edged up. And while flows to businesses cooled, the stock of their loans reached a three-year high, which broadly supports the ECB's assertion that the prevailing monetary policy stance was not particularly restrictive. On the other hand, German consumer confidence – which will be presented by the GfK as a forecast for October – is unlikely to have sustained its recovery. Fuel price relief in the form of a temporary tax cut is only due to kick-in from 1 October, while domestic political turbulence is contributing to a more uncertain outlook, all of which is likely to weigh on sentiment. Still, business surveys imply that economic expectations could have improved, reducing the likelihood of a more pronounced retrenchment in confidence. Separately, final GDP estimates from Spain will also be expected to affirm that member state's continued outperformance, with preliminary estimates suggesting that growth accelerated to 0.7%Q/Q.

The day ahead in the UK

While today's CBI survey gave a characteristically downbeat assessment of retail sector activity this month – with the net balance of firms reporting a decline in retail sales volumes at a five-month high and orders placed at their lowest on the series since 1983 – Friday's GfK consumer survey release could provide a more insightful steer for household spending. Admittedly, the risks are skewed to the downside for the consumer survey too. Consumer sentiment rose sharply over the summer, reaching a two-year high in August (-14) having been supported by the hot weather and growing optimism both at home and abroad. However, September's flash PMIs suggest that the benefits of the sunshine and a 'Burnham bounce' might have been short lived. And given the precipitous rise in petrol prices this month, tighter financial conditions and simmering concerns about the government's forthcoming budget announcement, it seems unlikely that economic expectations will have scope for further improvement.

European calendar

Today's results

Economic data

Country	Release	Period	**Actual**	Market consensus/ *Daiwa forecast*	Previous	Revised
Euro area	New car registrations Y/Y%	Aug	**4.7**	-	2.4	-
Germany	ifo business climate indicator	Sep	**89.9**	89.0	88.8	-
	ifo current assessment (expectations) indicator	Sep	**89.5 (90.4)**	89.0 (89.3)	88.5 (89.1)	- (89.0)
France	INSEE consumer confidence indicator	Sep	**86**	85	86	-
	INSEE business (manufacturing) confidence indicator	Sep	**96 (101)**	98 (102)	98 (103)	- (101)
	INSEE production (own-company production) outlook indicator	Sep	**-9 (15)**	-11 (10)	-11 (9)	-10 (12)
Spain	PPI Y/Y%	Aug	**13.2**	-	9.2	9.4
UK	CBI distributive trades survey - reported retail sales % net balance	Sep	**-55**	-	-48	-

Auctions

Country	Auction
Italy	sold €2.5bn of 3% 2028 bonds at an average yield of 3.64%
	sold €1bn of 1.1% 2031 inflation-linked bonds at an average yield of 1.57%
	sold €1bn of 2% 2037 inflation-linked bonds at an average yield of 2.42%

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

Tomorrow's releases

Economic data

Country	BST	Release	Period	Market consensus/ *Daiwa forecast*	Previous
Euro area	09.00	M3 money supply Y/Y%	Aug	3.5	3.4
Germany	07.00	GfK consumer confidence indicator	Oct	-27.2	-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

Auctions and events

Country	BST	Event
Euro area	19.00	ECB Vice President Vujčić 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.

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