

Euro wrap-up

Overview

- Bunds made gains as a German business survey pointed to firmer economic momentum, while OAT spreads narrowed after Friday evening's decision by Moody's not to downgrade France's sovereign credit rating.
- Gilts were mixed, while a UK retail survey signalled a questionable improvement in retail sales growth at the start of Q4.
- Tuesday will bring survey results of euro area bank lending, French consumer confidence and UK shop price inflation.

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Daily bond market movements

Bond	Yield	Change
BKO 3.0 12/28	3.096	+0.044
OBL 2.9 10/31	3.188	+0.029
DBR 3 08/36	3.354	+0.012
UKT 4 05/29	4.930	+0.020
UKT 4½ 03/31	4.995	+0.013
UKT 4½ 07/36	5.345	-0.011

*Change from close as at 4:00pm GMT.

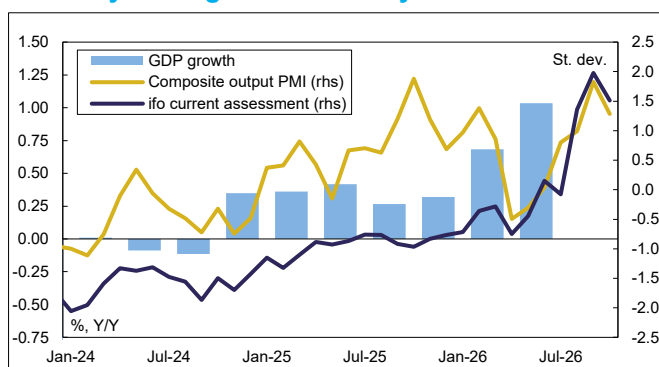
Source: Bloomberg

Euro area

German ifo survey points to firmer economic momentum in Q4 and into New Year

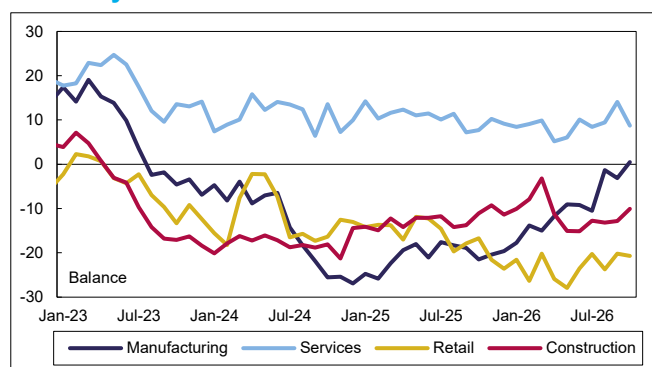
While German economic growth likely slowed sharply in Q3 as the impact of higher energy prices was compounded by the expiry of a fuel duty cut and record-low Rhine water levels, business surveys suggest that this loss of momentum will be short-lived. Certainly, today's ifo survey results reported a rise in the business climate index in October for a sixth successive month, to 91.2, the highest level since May 2023 and 1.7pts above the Q3 average. Admittedly, like Friday's flash [composite PMI](#), the current situation index edged lower this month, by 0.7pt to 88.8. But this remained close to the top of the range of the past couple of years. And, like the PMIs, the deterioration reflected a weakening in sentiment in the services sector, for which the respective index fell to a five-month low. Nevertheless, IT services providers were reportedly more upbeat, supported by the ongoing AI-investment drive. And overall, services firms considered the outlook for the coming six months to be the best since before the onset of the Iran war. Meanwhile, signs of improving momentum in manufacturing suggest that the weakness in Q3 will prove temporary. Indeed, with new orders continuing to trend higher, manufacturers judged current conditions to be the most favourable in more than three years. And despite the persistent competitiveness challenges facing sectors such as autos, manufacturers were more upbeat about the outlook than at any time since Russia's invasion of Ukraine in Spring 2022. The improvement was also increasingly broad-based across the sectors, with retailers also the most optimistic since February, perhaps reflecting hopes that the renewed cut in fuel duties this month will provide some relief to household budgets. And, perhaps surprisingly given elevated costs of materials and borrowing, construction firms were the least downbeat since Q1, with the government's infrastructure initiatives seemingly providing support. So, while geopolitical developments remain a key risk to the outlook, the increasingly broad-based improvement in business sentiment reinforces our expectation that German GDP will return to more robust growth in Q4 and maintain positive momentum into 2027.

Germany: GDP growth & survey indices



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

Germany: ifo current conditions indices



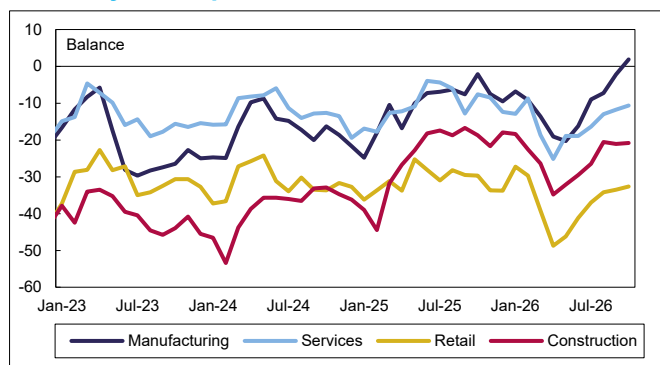
Source: Macrobond and Daiwa Capital Markets Europe Ltd.

French spreads narrow on ratings reprieve, but Moody's downgrade might be hard to resist in 2027

Spreads of OATs over Bunds outperformed today after Friday evening's announcement by Moody's that it decided not to downgrade its French sovereign ratings from Aa3 and instead simply maintained a negative outlook. The agency stated that it "assumes that a deficit-reducing budget for 2027 will be adopted, while financing costs and social tensions will abate somewhat in the next few months". Like Moody's, we also expect a form of the Lecornu government's draft budget eventually to be adopted. But we do not expect financing costs and social tensions to abate. And we don't expect the deficit next year to fall significantly from 5.4% of GDP this year. Admittedly, Moody's accepts that government debt will keep rising over the remainder of the decade. But it also "expects that the next president and government will seek to continue to narrow

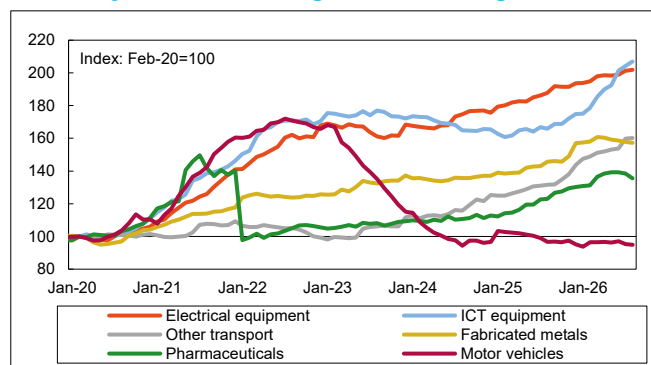
France's deficit" over coming years. However, the next president is likely to be Marine Le Pen, whose recently proposed fiscal tightening measures appeared spurious and in the past week denied the key role that pension reform needs to play to deliver fiscal sustainability. Moreover, unless and until a crisis occurs, the next government will likely struggle next year and beyond to pass any meaningful fiscal consolidation measures. Looking ahead, Moody's noted that a "downgrade of France's ratings would likely result from further evidence that the ability of the legislative institutions to take measures that would prevent a rapid and prolonged deterioration of debt affordability has weakened. A lasting pause or reversal of key provisions of previous structural reforms, most notably on pensions, would also add to downward pressure on the rating." So, based on those criteria, the case next year for Moody's to downgrade its French ratings – which would merely bring them in line with the assessments of S&P and Fitch – is likely to be impossible to resist.

Germany: ifo expectations indices



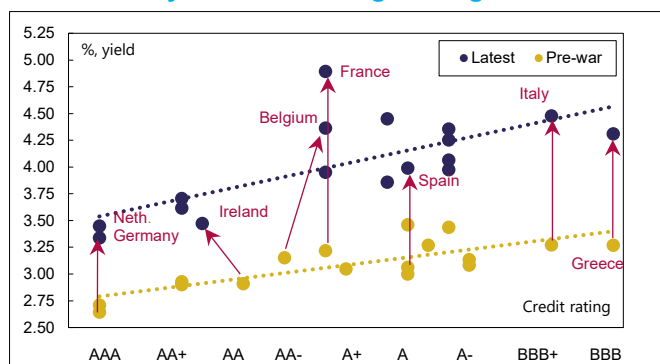
Source: Macrobond and Daiwa Capital Markets Europe Ltd.

Germany: Manufacturing order backlogs



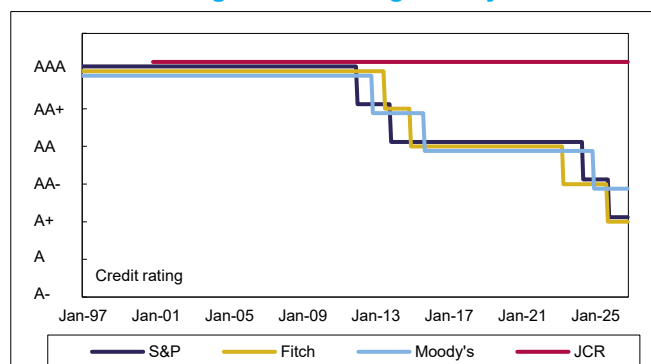
Source: Macrobond and Daiwa Capital Markets Europe Ltd.

France: 10Y yields & sovereign ratings*



*Pre-war yield level from 27 February 2026. Source: Bloomberg, major credit rating agencies and Daiwa Capital Markets Europe Ltd.

France: Sovereign credit rating history



Source: Major credit rating agencies and Daiwa Capital Markets Europe Ltd.

The day ahead in the euro area

Ahead of Thursday's ECB policy decision, attention on Tuesday will turn to its quarterly Bank Lending Survey and September monetary data for further signs that the recent rise in bond yields is feeding through to tighter bank credit conditions and weaker lending flows. Today's SAFE survey already provided some evidence of such transmission, with firms reporting a further net tightening in bank lending standards in Q3, and more than half of large enterprises reporting an increase in interest rates. And loan availability reportedly deteriorated by more than financing needs, largely reflecting the worsening economic outlook. Elsewhere, French consumer confidence seems likely to have weakened further in October, as higher prices and tighter financing conditions compounded the impact of political uncertainty and recent social disruption, although the latter is likely to have affected only a small share of responses collected late in the survey period.

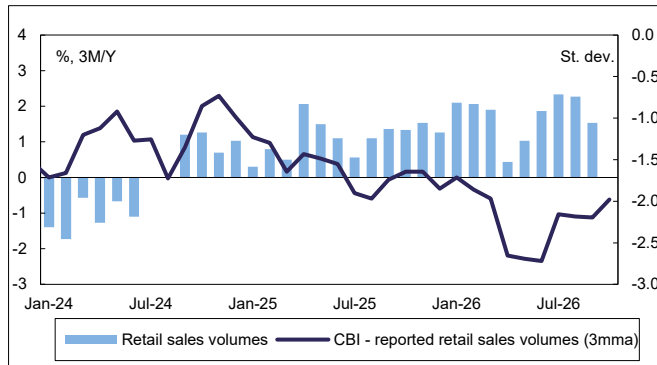
UK

Retail survey points to questionable pickup in sales in October, but outlook remains clouded

Echoing the broader improvement signalled by the flash October PMIs, today's CBI distributive trades survey also surprised to the upside, pointing to a striking turnaround in retail conditions at the start of Q4. In particular, the survey's net balance of sales volumes jumped a whopping 45pts to -10%, the highest level in 18 months. Encouragingly, sales were also judged to be broadly in line with norm for the time of the year for the first time in over two years. But this apparent improvement should be treated with caution. The CBI survey has been a poor guide to official retail sales recently, persistently signalling

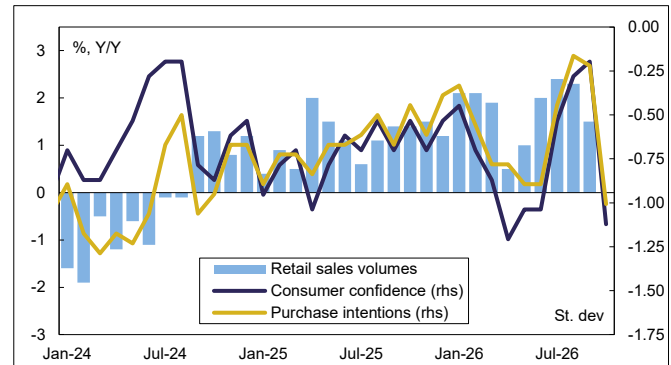
contraction even as official sales volume recorded positive annual growth in 15 out of the past 16 months. And for what it's worth, the CBI also reported that retailers expect sales to fall well short of seasonal norms in November despite the usual boost from Black Friday. That caution seems more consistent with October's sharp deterioration in consumer confidence, as squeezed household budgets drove reported purchase intentions to their weakest level in more than two years.

UK: Retail sales volumes & CBI survey



Source: Macrobond and Daiwa Capital Markets Europe Ltd.

UK: Retail sales volumes & consumer confidence



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

The day ahead in the UK

Another relatively quiet day for UK data will bring the BRC shop price survey for October, which looks set to provide further evidence that cost pressures are increasingly feeding through to consumers. Indeed, with manufacturers increasingly passing energy-related cost pressures down the supply chain, and food prices starting to reflect the impact of the summer drought, shop price inflation is expected to rise from 1.4%Y/Y in September to its highest rate since early 2024.

European calendar

Today's results

Economic data

Country	Release	Period	Actual	Market consensus/ <i>Daiwa forecast</i>	Previous	Revised
Germany	 ifo business climate indicator	Oct	90.2	89.9	89.9	-
	 ifo current assessment (expectations) indicator	Oct	88.8 (91.6)	89.9 (90.0)	89.5 (90.4)	-
Spain	 PPI Y/Y%	Sep	18.3	-	13.2	-
UK	 CBI distributive trades survey – reported retail sales % net balance	Oct	-10	-48	-55	-

Auctions

Country	Auction
- Nothing to report -	

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	 09.00	M3 money supply Y/Y%	Sep	3.4	3.5
France	 07.45	INSEE consumer confidence indicator	Oct	85	86
Spain	 08.00	Unemployment rate %	Q3	9.8	9.9
UK	 00.01	BRC shop price index Y/Y%	Oct	1.6	1.4

Auctions and events

Euro area	 09.00	ECB to publish quarterly Bank Lending Survey (BLS) for Q3/Q426
Germany	 10.30	Auction: to sell up to €5bn of 3% 2028 bonds
Italy	 10.00	Auction: to sell up to €2bn of 3% 2028 bonds
	 10.00	Auction: to sell up to €750mn of 1.25% 2032 inflation-linked bonds
	 10.00	Auction: to sell up to €750mn of 2.35% 2035 inflation-linked bonds
UK	 10.00	Auction: to sell £4.5bn of 4.625% 2032 bonds

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

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