Euro wrap-up

Overview

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- Bunds followed Treasuries lower as a German survey signalled a further marked improvement in investor expectations about the economic outlook.
- Gilts were little changed even as UK labour market data reported a further increase in the claimant count to the highest since the 1990s.
- Wednesday will bring final May inflation figures for the euro area and UK, as well as euro area new car registrations and construction output data.

Daily bond market movements

Bond	Yield	Change
BKO 0 06/22	-0.667	+0.012
OBL 0 04/25	-0.641	+0.021
DBR 0 02/30	-0.427	+0.023
UKT 0½ 07/22	-0.004	-0.006
UKT 0⅝ 06/25	0.002	-0.003
UKT 4¾ 12/30	0.206	+0.001

*Change from close as at 4:30pm BST.
Source: Bloomberg

Euro area

ZEW survey points to heady expectations for German outlook

Perhaps inevitably, the German ZEW survey for June strongly suggested that investor expectations with respect to the economic outlook continue to improve. Indeed, the survey measure of expectations of German economic conditions six months ahead rose for the third successive month and by more than expected to 63.4, the highest since 2006, marking an improvement in the net balance of optimists relative to pessimists to more than 112pts. The survey measure of current conditions picked up too, but not quite as much as had been expected. And it was still deeply in negative territory at -83.1, leaving the biggest mismatch between perceptions of current conditions and expectations on the survey since 2003-4 when the German economy was struggling to recover from recession but the Hartz reforms were set to provide a sizeable boost to competitiveness.

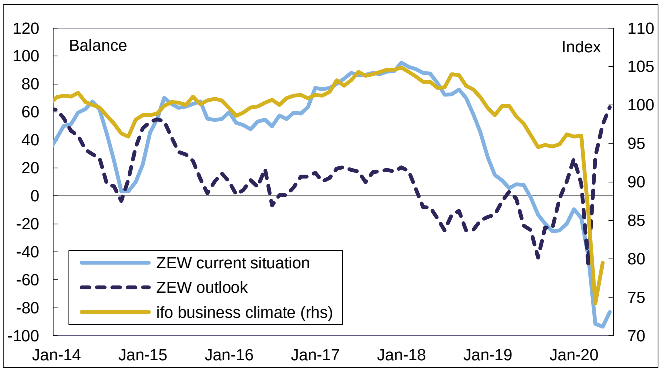
Big differences in expectations across the sectors

Nevertheless, according to the investors surveyed by ZEW, while GDP is now thought to be bottoming out, expectations of growth in Q3 and Q4 remain subdued. German fiscal stimulus is expected to support consumer-oriented sectors, and earnings forecasts are upbeat for IT and telecommunications firms. In contrast, expectations are negative for export-oriented industries such as autos and mechanical engineering, as well as for banks and insurers. Moreover, in the event of a second wave of pandemic in Europe, expectations across all sectors would become sharply negative once again in an instant.

The day ahead in the euro area and US

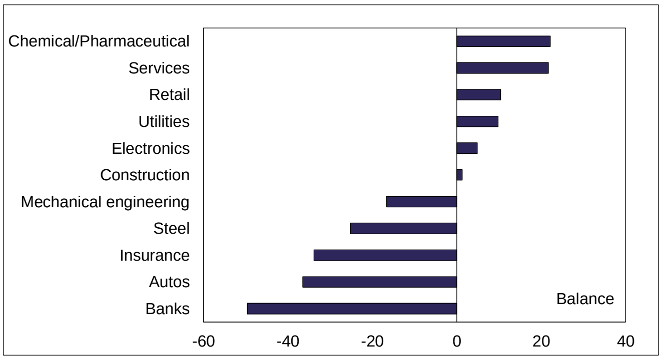
Looking ahead, tomorrow sees the release of euro area new car registrations for May. While these data will be improved from April's record decline, they will remain extremely weak – according to the VDA German new car registrations were down 50%Y/Y in May following a drop of 61%Y/Y the prior month, while registrations were still down in France (-50%Y/Y), Italy (-50%Y/Y) and Spain (-73%Y/Y). Wednesday also brings the release of final euro area CPI data for May. Today's German data aligned with the flash estimate that showed headline inflation (on the EU harmonised measure) declining 0.3ppt to 0.5%Y/Y. But there is a risk that headline euro area inflation will be revised slightly higher from the preliminary estimate, which showed that inflation fell from 0.3%Y/Y to 0.1%Y/Y, the lowest rate since 2016. Core inflation might also be nudged higher from the flash figure of 0.9%Y/Y. Euro area construction output data will also be published, as well as Italian industrial orders figures for April, which are likely to confirm that lockdown restrictions weighed heavily on activity. In terms of fiscal policy, Germany's cabinet should approve the further supplementary budget, to facilitate an additional €62.5bn of Bund issuance this year of on top of the €156bn approved in March. In the markets, meanwhile, Germany will auction €5bn of 10Y Bunds. In the US, as Fed Chair Powell repeats his semi-annual testimony before Congress, housing starts figures for May will be published and the Treasury will sell 20Y bonds.

Germany: ZEW and ifo sentiment survey indicators



Source: Thomson Reuters and Daiwa Capital Markets Europe Ltd.

Germany: ZEW survey - profit expectations



Source: Thomson Reuters and Daiwa Capital Markets Europe Ltd.

UK

Grimmest labour market conditions since the early 1990s

The latest UK labour market data were predictably grim. While about 8.7mn workers were receiving support via the government's Job Retention Scheme furlough programme at the end of last month, and that figure had increased to 9.1mn by the start of this week, the number of paid employees still fell a further 162.5k in May after plunging 449.3k in April. That left the number of payroll jobs down 2.1% since the start of lockdown in March and at the lowest level since September 2017. Median employee pay in May was down 4.3% from the peak in February, representing a drop of 1.8%Y/Y. The detail (for the period to April) showed that pay declined in industries where furloughing was most widespread, not least in the (already low-paying) hospitality sector. Moreover, the total number of weekly hours worked in the three months to April 2020 fell a record 8.9%3M/Y. Given increased joblessness, falling average wages and hours worked, and policies to increase take-up, the Claimant Count, which includes those employed with low income as well as those who are unemployed, rose almost 530k in May following an increase of just over 1.0mn in April. That took it to about 2.8mn, the highest level since the mass unemployment of the early 1990s.

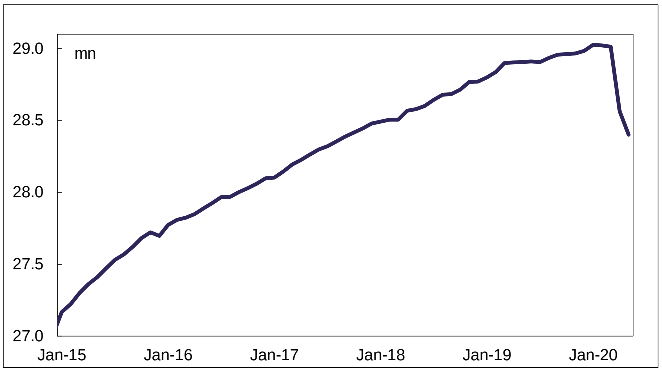
Beware a second wave of unemployment in the autumn

Looking ahead, the number of job vacancies fell in May to a record low, down about 60% from March, to suggest no imminent relief despite the initial easing of lockdown measures last month. But the further relaxation of restrictions on economic activity, including yesterday's reopening of many non-essential stores in England, should at least provide support to labour demand from the current month on. And ongoing support from the government's Job Retention Scheme should also encourage many firms to postpone decisions on redundancies. Nevertheless, the subsidies available under the scheme will be gradually reduced from August onwards before the programme concludes in October. So, we still expect a non-negligible share of workers currently furloughed to be made formally unemployed as and when the government support is withdrawn, representing a second wave of joblessness even if a second wave of pandemic is avoided. And that increase in unemployment will represent a meaningful risk of a double-dip in economic activity around the turn of the year.

The day ahead in the UK

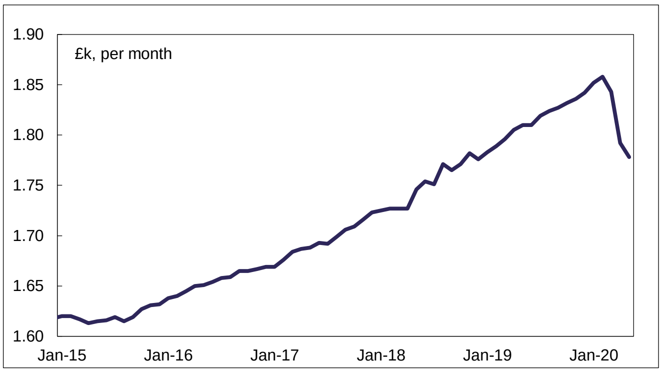
Like the euro area, tomorrow will bring an update on UK inflation, with the figures for May expected to show a further 0.2ppt drop in the headline CPI rate to 0.6%Y/Y, due principally to lower petrol and household energy prices. But amid very subdued demand, core inflation is also likely to have fallen from 1.4%%Y/Y in April. Just as elsewhere in Europe, the difficulties faced collecting data will raise issues about the reliability of the data published. In other news, the DMO will sell £3.75bn of 2023 bonds and £2.25bn of 2041 bonds.

UK: Paid employees



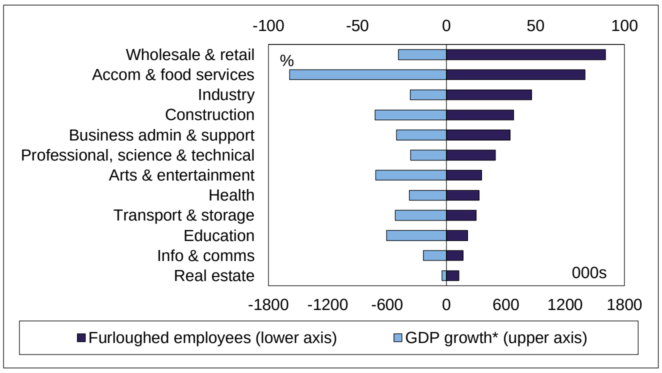
Source: ONS and Daiwa Capital Markets Europe Ltd.

UK: Median pay level per month



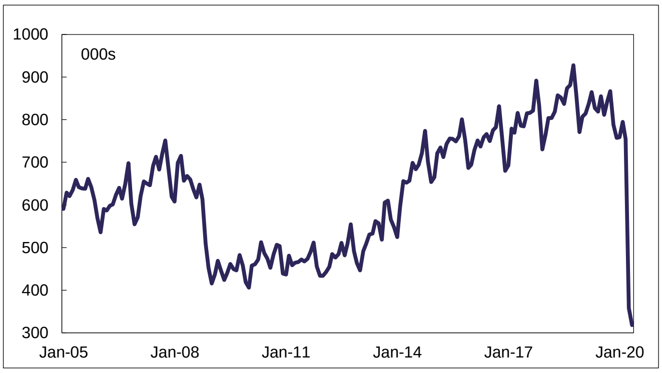
Source: ONS and Daiwa Capital Markets Europe Ltd.

UK: GDP & furloughed employees, selected sectors



**GDP growth rate between February 2020 and April 2020. Number of employees furloughed at end-May. Source: ONS, HM Treasury and Daiwa Capital Markets*

UK: Job vacancies



Source: ONS and Daiwa Capital Markets Europe Ltd.

European calendar

Today's results

Economic data

Country		Release	Period	**Actual**	Market consensus/ *Daiwa forecast*	Previous	Revised
EMU		Labour costs Y/Y%	Q1	**3.4**	-	2.4	**2.3**
Germany		Final CPI (EU-harmonised CPI) Y/Y%	May	**0.6 (0.5)**	0.6 (0.5)	0.9 (0.8)	**-**
		ZEW current assessment balance (expectations)	Jun	**-83.1 (63.4)**	-80.0 (60.0)	-93.5 (51.0)	**-**
UK		Claimant count rate % (change '000s)	May	**7.8 (528.9)**	-	5.8 (856.5)	**6.3 (1032.7)**
		Average earnings including bonuses (excluding bonuses) 3M/Y	Apr	**1.0 (1.7)**	1.5 (1.9)	2.4 (2.7)	**2.3 (-)**
		ILO unemployment rate 3M%	Apr	**3.9**	4.6	3.9	**-**
		Employment change 3M/3M '000s	Apr	**6**	-110	210	**-**

Auctions

Country		Auction
UK		sold £3bn of 1.5% 2026 bonds at an average yield of 0.016%
		sold £2bn of 4.75% 2030 bonds at an average yield of 0.224%

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

Yesterday's results

Economic data

Country		Release	Period	**Actual**	Market consensus/ *Daiwa forecast*	Previous	Revised
EMU		Trade balance €bn	Apr	**1.2**	-	23.5	**25.5**
Italy		Final CPI (EU-harmonised CPI) Y/Y%	May	**-0.2 (-0.3)**	-0.1 (-0.2)	0.0 (0.1)	**-**

Auctions

Country	Auction
	- Nothing to report -

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

Tomorrow's data releases

Economic data

Country		BST	Release	Period	Market consensus/ *Daiwa forecast*	Previous
EMU		07.00	EU-27 new car registrations Y/Y%	May	-	-76.3
		10.00	Final CPI (core CPI) Y/Y%	May	0.2 (0.9)	0.3 (0.9)
		10.00	Construction output M/M% (Y/Y%)	Apr	-	-14.1 (-15.4)
Italy		09.00	Industrial orders (sales) Y/Y%	Apr	-	-26.6 (-25.2)
UK		07.00	CPI (core CPI) Y/Y%	May	0.6 (1.3)	0.8 (1.4)
		07.00	PPI input prices (output prices) Y/Y%	May	-8.6 (-1.2)	-9.8 (-0.7)

Auctions and events

Country		BST	Auction / Event
Germany		10.30	Auction: €5bn of 2030 bonds
UK		10.00	Auction: £3.75bn of 0.125% 2023 bonds
		11.30	Auction: £2.25bn of 1.25% 2041 bonds

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

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