Euro wrap-up

Overview

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- Bunds and other core euro area government bonds made big losses as German retail sales rose above the pre-pandemic peak and French car registrations rose above their level a year earlier.
- Gilts also made losses despite a further fall in UK house prices.
- Thursday's will bring labour market and producer price figures from the euro area.

Daily bond market movements

Bond	Yield	Change
BKO 0 06/22	-0.073	+0.014
OBL 0 04/25	-0.026	+0.029
DBR 0 08/30	0.207	+0.036
UKT 0½ 07/22	-0.083	+0.014
UKT 0⅝ 06/25	-0.030	+0.029
UKT 4¾ 12/30	0.205	+0.036

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

Euro area

German retail sales rebound to a new high

Germany's significant success at controlling the pandemic and limiting the number of deaths from Covid-19 allowed the reopening of non-essential stores from the first week of May, sooner than in most other euro area member states. As a result, retail sales rebounded particularly vigorously that month, as pent-up demand was more than satisfied. Indeed, German retail sales volumes leapt in May by 13.9%M/M, the strongest growth rate on the 26-year series. Strikingly, that took the level of sales 3.6% above February's pre-pandemic peak and 3.8% above the level a year earlier. Within the detail, sales of food, beverages and tobacco were up 4.9%Y/Y while sales from non-food stores rose 3.5%Y/Y. Sales of furniture, household appliances and building supplies rebounded rapidly, by 8.6%Y/Y. But sales of clothes and textiles were still a long way below normal levels, being down 22.6%Y/Y. And pharmaceutical and cosmetic items fell 6.3%Y/Y. As ever, we caution that the retail sales data are highly volatile and regularly subject to significant revision. And we would not be surprised to see payback in June. Moreover, while shoppers were able to return to the stores, online sales remained very strong, up 28.7%Y/Y, suggesting that consumer behavior might well have changed for the long term, highlighting downside risks to the outlook for bricks-and-mortar jobs and related real estate.

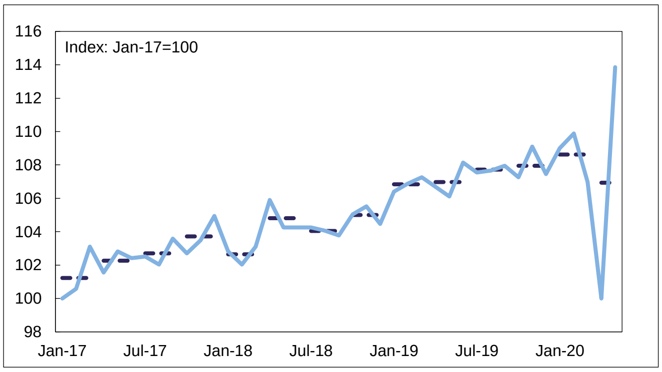
But unemployment rises too

Indeed, despite the jump in retail sales in May, on a seasonally adjusted basis, German unemployment rose by a further 69k in June, taking the level to 2.943mn, the highest since December 2013. On the same basis, the jobless claims rate edged up a further 0.1ppt to 6.4%, the highest since August 2015. Of course, without the government short-time wage subsidy (kurzarbeit) scheme, the jobless rate would be in double digits. While timely figures are unavailable, the Federal Labour Agency today revealed that it had subsidised the jobs of 6.83mn workers in April. Many of those workers will have left the scheme by now – e.g. VW workers returned to work on a full-time basis, without government support, from today. However, many other workers in sub-sectors likely to see a long-lasting hit to demand, particularly in services, will eventually be made redundant. And with today's data showing a fifteenth successive monthly decline in the number of job vacancies to the lowest level in five years, they could struggle to be reabsorbed into employment elsewhere. So, we expect the unemployment rate to continue to rise for a while yet, posing a downside risk to the outlook.

Car registrations leap in France, but underwhelm in Italy and Spain

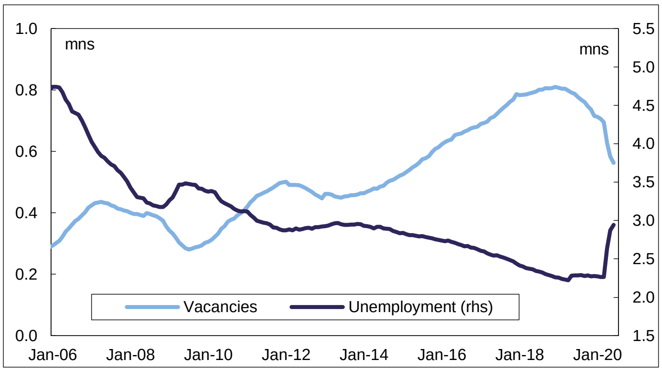
Having been down almost 80%Y/Y in April and still more than 50%Y/Y in May, euro area new car registrations inevitably fared much better in June, as car showrooms were able to reopen fully across the region. Today's data showed a striking

Germany: Retail sales*



*Dark blue lines represent quarterly averages. Q220 figure shows average for April and May. Source: Thomson Reuters and Daiwa Capital Markets Europe

Germany: Unemployment and job vacancies



Source: Thomson Reuters and Daiwa Capital Markets Europe Ltd.

improvement in France as sales rose 1.2%Y/Y, the first annual increase since 2019. Given the marked weakness seen over recent months, however, this left sales down 38.6%YTD/Y in the first half of the year, by far the worst performance since the series began in the early 1990s. Elsewhere the improvement in June was much less impressive, with Spanish registrations down 36.7%Y/Y to be down 50.9%YTD/Y, and Italian registrations down 23.1%Y/Y to be down 46.1%YTD/Y.

Manufacturing PMIs signal little more than stabilisation

With Covid-related restrictions on activity relaxed, the final June manufacturing PMIs inevitably suggested that the pace of deterioration in the euro area industrial sector eased significantly in June. The headline euro area manufacturing PMI was revised up by 0.5pt to a four-month high of 47.4, representing an increase of 8pts from May and 24pts above April's trough. That suggests progress towards a stabilisation of conditions after extreme contraction rather than any meaningful expansion. Indeed, Markit judged that the June readings implied a decline in output at an annual rate of about 2% compared to the near-30% year-on-year rate of decline in April. It also noted that, while consumer goods producers reported a return to growth, producers of intermediate and capital goods saw ongoing contraction. The survey detail also suggested that new orders from at home and abroad, work backlogs and employment continued to decline, albeit not as steeply as over the past few months.

Contrast between German and French PMIs probably misleading

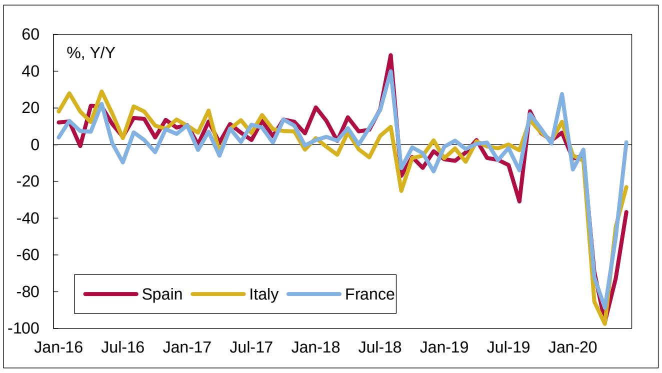
At the country level, the headline PMIs suggested that manufacturing activity in France (up almost 12pts on the month and upwardly revised to 52.3, a 21-month high) and Ireland (51.0) saw positive growth last month, while Spain's broadly stabilised (49.0). In contrast, it suggested that the sectors in Italy (47.5), the Netherlands and Germany (both the lowest of all member states at 45.2) continued to contract. While the discrepancy between Germany and France is striking, it probably reflects the limitations of the survey and the way by which the indices are calculated, as well as the often marked differences of impact of the pandemic between the various sub-sectors. It also likely reflects the fact that the drop in production over recent months in Germany (with the exception of certain sectors, such as autos) was not as marked as in France. And given the later easing of restrictions in France, the strength of the immediate rebound there was probably stronger than in Germany, even if it was not necessarily as sustainable.

The day ahead in the euro area and US

Tomorrow's economic data calendar focuses on the labour market, with euro area unemployment figures for May due, along with Spanish national labour numbers for June. The aggregate euro area unemployment rate is forecast to have risen from 7.3% to 7.9% in May, the highest since November 2018. Unemployment in Spain, meanwhile, is forecast to have fallen in June, as the relaxation of strict lockdown measures allowed businesses to return to work. Also out tomorrow are euro area producer price inflation data for May. In other news, ECB Executive Board members Mersch and Schnabel are due to participate in separate video conferences. In the markets, France and Spain will hold a number of bond auctions of mid- to long-dated maturities.

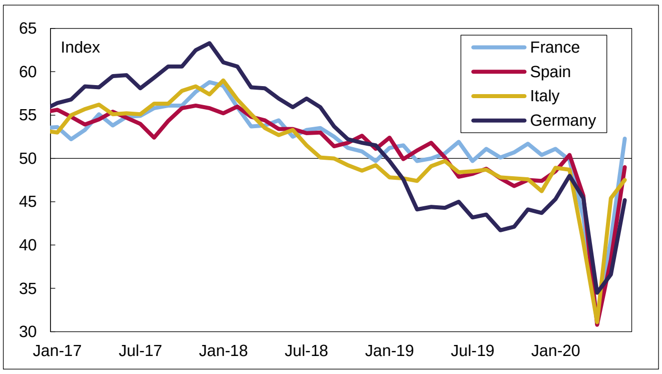
In the US, with markets closed on Friday, the week's data calendar concludes tomorrow with some key releases, including some notable labour market data. The BLS employment report is expected to show a further marked increase in nonfarm payrolls in June of about 2.5mn. However, the drop in the unemployment rate, from 13.3% in May, is expected to be relatively modest while wage growth is expected to fall back. Thursday will also bring the usual weekly jobless claims data and final trade and factory orders figures for May.

Euro area: New car registrations by member state



Source: Thomson Reuters, Bloomberg and Daiwa Capital Markets Europe Ltd.

Euro area: Manufacturing PMIs by member state



Source: Thomson Reuters, Markit and Daiwa Capital Markets Europe Ltd.

UK

House prices fall for first time since 2012

While estate agents were able to reopen in mid-May, and surveys indicated a subsequent surge in searches and enquiries, today's release of the Nationwide house price indices suggested that residential property prices remain under significant downwards pressure. In particular, following a drop of 1.7%M/M in May – which was the steepest since 2009 – prices fell a further 1.4%M/M in June to be down 0.1%Y/Y, the first negative annual rate since 2012. Of course, the decline in prices coincides with a sharp drop in transactions, which were still down 50%Y/Y. And the marked fall in mortgage approvals (down almost 90%Y/Y) in May points to a low level of activity ahead. While interest rates on floating-rate mortgages are down by around 70bps from February, several lenders have scaled back their higher loan-to-value mortgage offers. And applicants currently furloughed or receiving government support will also encounter tighter lending conditions going forward. Overall, with the economic outlook set to remain highly uncertain and unemployment likely to rise further as the government's support schemes are phased out, we expect supply to continue to exceed demand in the housing market, further weighing on house prices over the near term.

Downward pressure on shop prices moderated slightly

The BRC shop price index suggested that some of the downwards pressure on prices from the pandemic eased last month. The headline measure of prices rose 0.4%M/M to be down 1.6%Y/Y, representing a moderation of the pace of decline from -2.4%Y/Y in May. Food prices on this survey fell back for the second successive month, albeit by just 0.1%M/M to be up 1.5%Y/Y, the same annual rate as in May. But non-food prices rose for the first month since February, up 0.7%M/M to be down 3.4%Y/Y, following a drop of 4.6%Y/Y in May. The BRC's inflation rate focuses only on goods price pressures on the high street. And we expect retailers to continue to offer significant discounting going forward as they chase business.

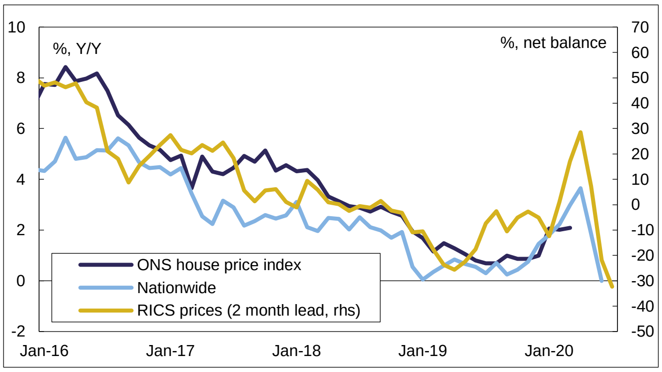
Manufacturing PMI implies stabilisation

There were no surprises from the final manufacturing PMI survey, with the headline index unchanged from the flash estimate in June at 50.1, marking a record monthly rise of 9.4pts from May, but still consistent with stabilisation in the sector rather than rapid growth. In addition, the output component was nudged slightly lower from the initial release to 50.7. With firms having been operational for the whole month (albeit under social distancing rules) for the first time since February, production seems bound to have risen considerably in June compared with previous months. While overseas orders remained exceptionally weak, domestic orders improved as lockdown measures were further eased and clients returned to work. And almost two-thirds of manufacturers indicated that they expected output to rise over the coming twelve months. This notwithstanding, despite ongoing support from the government's Job Retention Scheme, the survey suggested that firms continued to cut back their workforces.

The day ahead in the UK

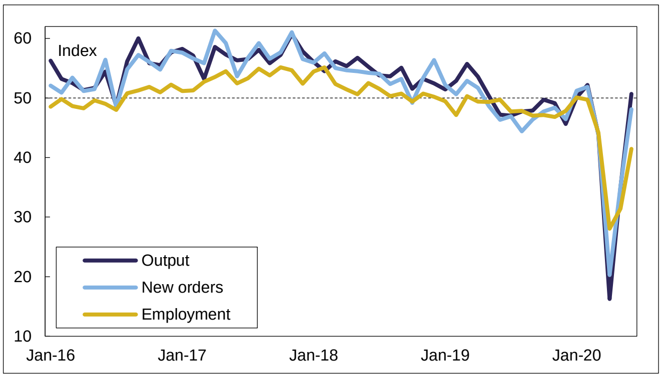
A quieter day on the UK economic data front tomorrow will bring just BoE data from its Decision Maker Panel survey for June. On the supply side, the DMO will sell 2025 and 2034 bonds.

UK: House price indicators



Source: Thomson Reuters and Daiwa Capital Markets Europe Ltd.

UK: Manufacturing PMIs



Source: Thomson Reuters, Markit and Daiwa Capital Markets Europe Ltd.

European calendar

Today's results

Economic data

Country		Release	Period	Actual	Market consensus/ *Daiwa forecast*	Previous	Revised
EMU		Final manufacturing PMI	Jun	**47.4**	46.9	39.4	-
Germany		Retail sales M/M (Y/Y%)	May	**13.9 (3.8)**	3.5 (-3.4)	-5.3 (-6.5)	**-6.5 (-6.4)**
		Final manufacturing PMI	Jun	**45.2**	44.6	36.6	-
		Unemployment change '000s (rate %)	Jun	**69.0 (6.4)**	120 (6.5)	238 (6.3)	**237 (-)**
France		Final manufacturing PMI	Jun	**52.3**	52.1	40.6	-
		New car registrations Y/Y%	Jun	**1.2**	-	-46.1	-
Italy		Manufacturing PMI	Jun	**47.5**	47.6	45.4	-
		New car registrations Y/Y%	Jun	**-23.1**	-	-49.6	**-44.6**
Spain		Manufacturing PMI	Jun	**49.0**	45.4	38.3	-
		New car registrations Y/Y%	Jun	**-36.7**	-	-70.6	-
UK		BRC shop price index Y/Y	Jun	**-1.6**	-	-2.4	-
		Nationwide house price index M/M% (Y/Y%)	Jun	**-1.4 (-0.4)**	-0.6 (0.9)	-1.7 (1.8)	-
		Final manufacturing PMI	Jun	**50.1**	50.1	40.7	-

Auctions

Country		Auction
UK		sold £3bn of 0.125% 2028 bonds at an average yield of 0.104%
		sold £2.25bn of 0.625% 2050 bonds at an average yield of 0.625%

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

Tomorrow's data releases

Economic data

Country		BST	Release	Period	Market consensus/ Daiwa forecast	Previous
EMU		10.00	Unemployment rate %	May	7.9	7.3
		10.00	PPI Y/Y%	May	-4.5	-4.5
Italy		09.00	Unemployment rate %	May	7.9	6.3
Spain		08.00	Unemployment change '000s	Jun	-113.0	26.6

Auctions and events

Country		BST	Auction / Event
EMU		14.00	ECB's Mersch scheduled to speak
		18:00	ECB's Schnabel scheduled to speak
France		09.50	Auction: 0% 2030 bonds
		09.50	Auction: 1.25% 2034 bonds
		09.50	Auction: 1.75% 2039 bonds
		09.50	Auction: 0.75% 2052 bonds
Spain		09.45	Auction: 0% 2025 bonds
		09.45	Auction: 0.8% 2027 bonds
		09.45	Auction: 1.25% 2030 bonds
		09.45	Auction: 1% 2030 index-linked bonds
UK		09.00	June Decision Maker Panel (DMP) data published
		10.00	Auction: £3.5bn of 0.625% 2025 bonds
		10.00	Auction: £2bn of 4.5% 2034 bonds

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

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