Euro wrap-up

Overview

Chris Scicluna
+44 20 7597 8326

Emily Nicol
+44 20 7597 8331

- Bunds were little changed despite a strong German ZEW investor sentiment survey while French retail sales fell back.
- Gilts made losses despite a further drop in UK payrolls, weak pay growth and evidence of a surge in redundancies to come.
- Wednesday will bring data for UK inflation and euro area goods trade.

Daily bond market movements

Bond	Yield	Change
BKO 0 09/22	-0.703	+0.006
OBL 0 10/25	-0.690	+0.003
DBR 0 08/30	-0.483	-
UKT 1¾ 09/22	-0.073	+0.034
UKT 0⅝ 06/25	-0.070	+0.033
UKT 4¾ 12/30	0.218	+0.025

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

Euro area

German ZEW survey points to ongoing firm recovery

Despite concerns about a possible breakdown in EU-UK trade discussions and the rise in coronavirus cases in Europe, Germany's ZEW investor confidence survey for September pointed to ongoing improvements in both current economic conditions and expectations for the near-term outlook. In particular, the current situations balance rose 15.1pts, the largest monthly increase since April 2015, to -66.2, admittedly still considerably weaker than the pre-pandemic level but nevertheless 27pts higher than May's trough. Moreover, the outlook balance also rose to its firmest reading for more than two decades. Admittedly, this survey does not always provide an accurate assessment of economic activity. However, it typically offers a guide to the findings of the more broad-based ifo business survey (due 24 September). So, having recovered 85% of the initial post-lockdown drop by August, the September readings might well see the headline ifo business climate index return close to the pre-Covid level.

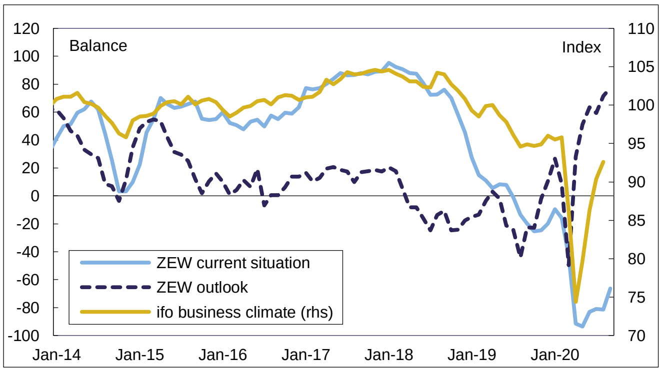
French retail sales slip slightly

While yesterday's Bank of France (BoF) survey pointed to ongoing recovery in overall economic activity in August, today's BoF French retail sales figures suggested a further modest decline last month, by 0.4%M/M, to leave sales still 2.5% below the pre-pandemic peak and the annual rate of growth moderating 1ppt to 1.4%Y/Y. While the weakness in part reflected lower spending on food, sales of industrial goods also slipped back for the second successive month, with particular weakness at DIY and furniture stores as well as of bicycles and motorcycles after extremely vigorous growth in May and June. In contrast, sales of clothing, footwear and sports equipment rose further. Overall, sales of industrial goods were still a little more than 2½% higher than February's peak. And on average so far in Q3, total sales were almost a fifth higher than the average in Q2, adding to evidence of a record rebound in GDP this quarter.

Euro area wage growth acceleration won't last

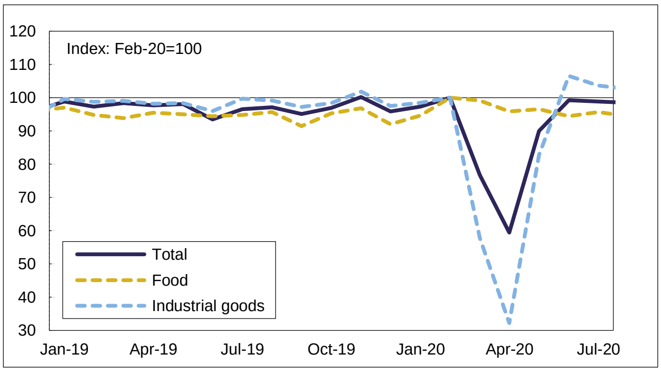
Euro area labour costs data for Q2 were also published today. And these showed that growth jumped last quarter, by 0.5ppt to 4.2%Y/Y, the strongest rate since Q108. The improvement in the industry and services sectors was striking, up 0.9ppt to 3.8%Y/Y and 4.4%Y/Y respectively. Once again this reflected firmer wage growth, which rose 1.4ppts to 5.2%Y/Y, as a sharp drop in the number of working hours was offset by government wage-support programmes, while tax relief and subsidies also helped support the non-wage component (0.8%Y/Y). Among the larger member states, with the exception of Italy, labour costs accelerated in Q2, with particularly strong wage growth in France (up 1.8ppts to 3.3%Y/Y) and Spain (up 2.8ppts to 6.6%Y/Y), while wage growth in Germany moved sideways at 4.9%Y/Y.

Germany: Sentiment indicators



Source: Refinitiv and Daiwa Capital Markets Europe Ltd.

France: Retail sales



Source: BoF, Refinitiv and Daiwa Capital Markets Europe Ltd.

German manufacturing employment well down in July

Of course, weak demand has prevented a pass-through to inflation, and wages will slow over coming quarters in response to rising labour market slack. Certainly, today's manufacturing employment figures illustrated the underlying softness in the German labour market, with the number of people employed in firms in the sector (of 50 or more workers) down 164k (2.9%) at the end of July compared with a year earlier, with broad-based weakness across subsectors – e.g. the number of people working in metal production was down a little more than 5½%Y/Y (14k), while the number employed in the autos sector was down 4.1%Y/Y (35k). But the drop so far has been clearly limited by the government's "Kurzarbeit" short-time work scheme. Indeed, the number of hours worked were down a sharper 8.5%Y/Y, with double-digit annual declines in metal production (-18.6%Y/Y), mechanical engineering (-12.0%Y/Y) and production of rubber and plastic goods (-10.9%Y/Y).

German hospitality sales higher, but still well below pre-Covid level

Destatis also published turnover data from the hospitality sector in July, which continued to indicate ongoing recovery since the relaxation of Covid-19-related restrictions. Indeed, sales were up 21.9%M/M in July, after growth of 65%M/M in June and 41%M/M in May. Of course, this followed a significant slump at the height of the outbreak, with sales in the sector still down 28.7% compared with the pre-crisis level in February, to leave them down 26.8%Y/Y and more than 37%Y/YTD in the first seven months of the year. Within the detail, the improvement in July was largely driven by accommodation, for which sales were up a further 38%M/M with turnover at hotels up by more than 40%M/M. But despite significant growth in May and June, accommodation sales were still down 29% compared with the pre-pandemic level, with just those at camping sites having trended higher since February. Meanwhile, restaurant sales rose more 15.6%M/M in July, to recover roughly 80% of the initial slump at the height of the crisis, albeit leaving them still down by almost 17% from February's level.

The day ahead in the euro area

A quieter day for economic releases tomorrow will bring just euro area trade figures for July. In line with national data from Germany and France, these are expected to show a further notable rise in the value of exports that month, which once again outpaced growth in imports.

UK

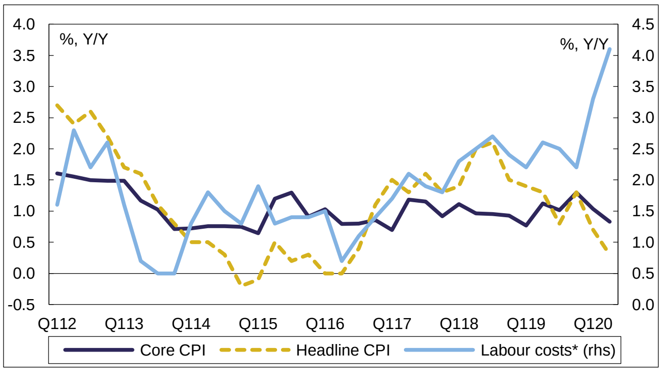
A mixed bag of labour market data

Today's UK labour market data showed a drop in the number of workers on furlough and a rise in working hours in July as conditions in many sub-sectors started to normalise after the lockdown. Moreover, the number of job vacancies rose again in August. But the improvements were relatively modest. At the same time, the number of payrolls fell again last month. And with the unemployment rate and the number of redundancies rising even before the government's Job Retention Scheme was being phased out, today's data seem to be merely the prelude to a significant jump in joblessness in the autumn.

UK payroll losses pick up slightly in August

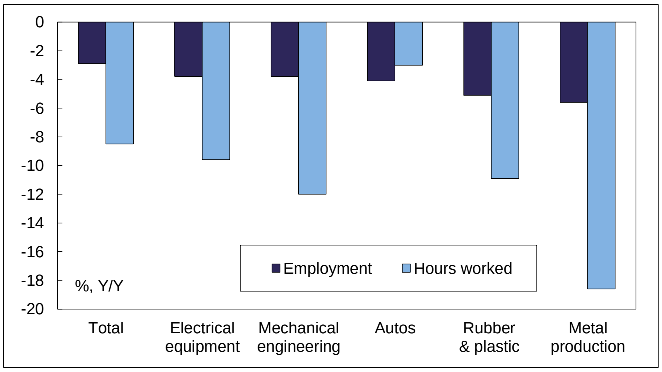
In terms of some of the detailed numbers, the number of employees on payrolls was down only around 36k on the month in August. But that was the biggest drop since May. And it left the number of payrolls 711k (2.5%) below the peak at the start of the year and at the lowest level in more than three years. The Claimant Count – which includes people in work on very low incomes and working hours as well as those out of work – rose 0.2ppt last month to 7.6%, up from 3.4% at the start of the year, to represent 2.7mn people. Meanwhile, the number of people estimated to be temporarily away from work, including furloughed workers, fell about 1mn in July, but remained close to 5.5mn at the end of the month, compared to the peak above 9mn in late April. Within that total at end-July, over 2.2mn of workers temporarily away from work had been absent for three months or more. There were also around 250k people away from work because of the pandemic and receiving no pay that month.

Euro area: Labour costs and inflation



**Excluding public sector. Source: Refinitiv and Daiwa Capital Markets Europe Ltd.*

Germany: Manufacturing employment, July 2020



Source: Destatis and Daiwa Capital Markets Europe Ltd.

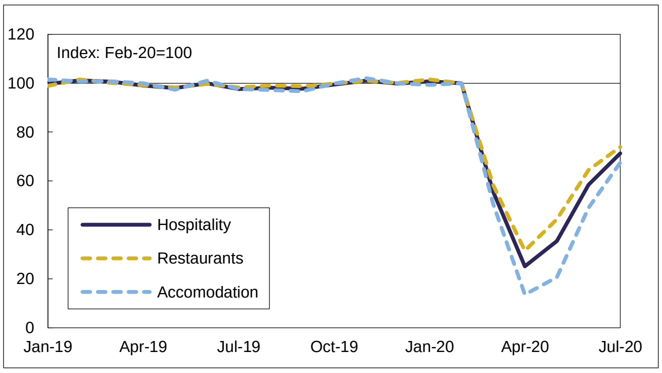
Redundancies set to accelerate into the autumn

Given the return to work of some employees, average nominal regular pay growth (i.e. ex bonuses) returned to positive territory in the three months to July. But with the average number of hours worked still relatively low, it was up just 0.2%3M/Y from -0.2%3M/Y previously. (By contrast, median monthly pay was up 2.3%Y/Y in July.) And including bonuses, total pay was still down 1.0%3M/Y, representing a drop of 1.8%3M/Y in real terms. More happily, the number of vacancies in the three months to August rose to 434k, up about 30% from the record low in the three months to June, but still down sharply from 818k in the three months to February and suggestive of relatively modest improvement. Of course, the Job Retention Scheme has – for the time being – helped to keep the headline ILO unemployment rate low. However, this rate still rose 0.2ppt in the three months to July to 4.1%. And the three-month average masked a rise of 0.6ppt in the single-month estimate in July to 4.4%, with the deterioration led by those under the age of 25. The number of redundancies was up 48k over the three months to July, the most since the global financial crisis in 2009, to 155k, the highest level since 2012. Unfortunately, firms over that period had already given the government insolvency service notifications of risks of 380k redundancies to come, and the total number over coming months could be twice as much as that, likely pushing the ILO unemployment rate several percentage points higher by the end of the year.

The day ahead in the UK

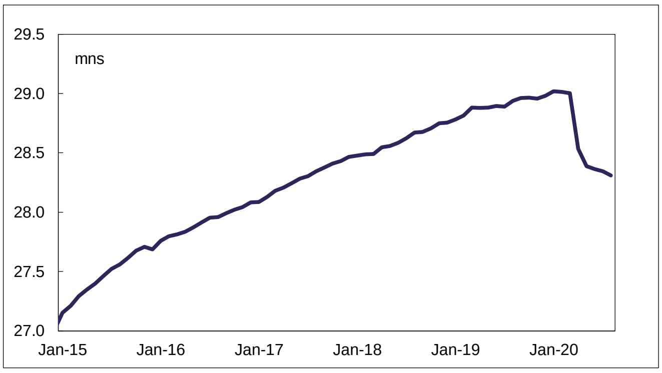
Ahead of the BoE's monetary policy announcement on Thursday, tomorrow will bring August inflation data. These are expected to show that headline CPI fell back sharply, close to zero from 1.0%Y/Y in July as one-off effects related to the pandemic likely subsided. Indeed, while the drag from energy inflation likely eased slightly, underlying price pressures are expected to have weakened considerably, with core inflation set to fall to just 0.5%Y/Y from 1.8%Y/Y previously. Wednesday will also bring the ONS house price index for June.

Germany: Hospitality turnover



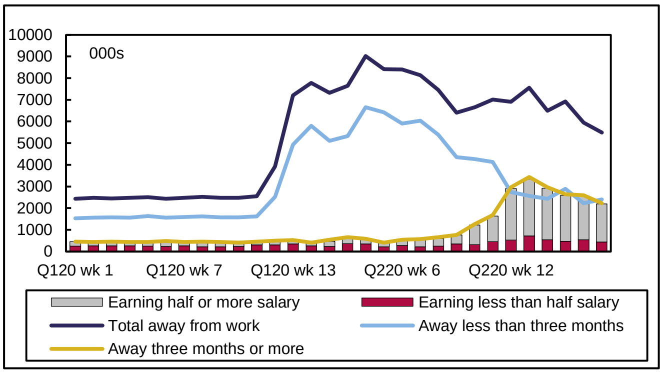
Source: Destatis and Daiwa Capital Markets Europe Ltd.

UK: Payrolls



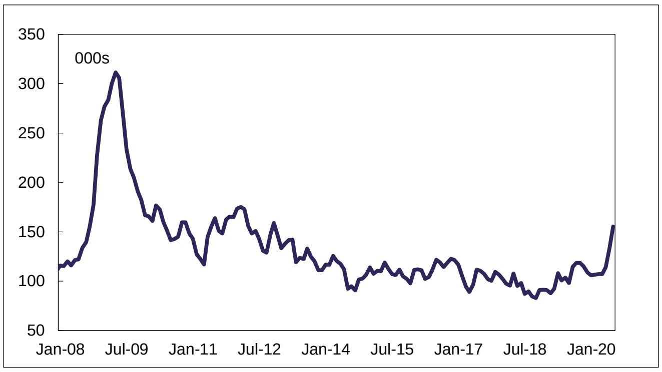
Source: ONS and Daiwa Capital Markets Europe Ltd.

UK: People temporarily away from paid work*



**Wage received figures refer to those temporarily away from work for three months or more. Source: ONS and Daiwa Capital Markets Europe Ltd.*

UK: Redundancies



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%	Q2	**4.2**	-	3.4	**3.7**
Germany		ZEW current situation (expectations)	Sep	**-66.2 (77.4)**	-70.3 (69.0)	-81.3 (71.5)	-
France		Final CPI (EU-harmonised CPI) Y/Y%	Aug	**0.2 (0.2)**	0.2 (0.2)	0.8 (0.9)	-
		BoF retail sales M/M% (Y/Y%)	Aug	**-0.4 (1.4)**	-	-0.3 (2.4)	-
Italy		Final CPI (EU-harmonised CPI) Y/Y%	Aug	**-0.5 (-0.5)**	-0.5 (-0.5)	-0.4 (0.8)	-
UK		Unemployment claimant count rate % (change '000s)	Aug	**7.6 (73.7)**	-	7.5 (94.4)	**7.4 (69.9)**
		Average earnings including bonuses (excluding bonuses) 3M/Y%	Jul	**-1.0 (0.2)**	-1.3 (-0.3)	-1.2 (-0.2)	-
		ILO unemployment rate 3M%	Jul	**4.1**	4.1	3.9	-
		Employment change Q/Q, '000s	Jul	**-12**	-118	-220	-

Auctions

Country		Auction
Germany		sold €3.3bn of 0% 2027 bonds at an average yield of -0.62%
UK		sold £2.75bn of 1.25% 2027 bonds at an average yield of 0.032%
		sold £1.75bn of 1.75% 2037 bonds at an average yield of 0.623%

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	Trade balance €bn	Jul	-	17.1
UK		07.00	CPI (core CPI) Y/Y%	Aug	0.1 (0.7)	1.0 (1.8)
		07.00	PPI input prices (output prices) Y/Y%	Aug	-5.3 (-0.7)	-5.7 (-0.9)
		07.00	Land Registry house price index Y/Y%	Jul	-	2.9

Auctions and events

Country		BST	Auction / Event
Germany		10.30	Auction: €1.5bn of 1.25% 2048 bonds
UK		10.00	Auction: £2.5bn of 0.375% 2030 bonds

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

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