

Euro wrap-up

Overview

- While the flash estimate of German inflation in June fell back, Bunds made losses as the Commission's euro area economic sentiment indicator rose to its highest level since 2000.
- Gilts also made losses as UK house price inflation rose to its highest level since 2004.
- Wednesday will bring the flash estimates of euro area inflation in June along with figures for French consumer spending in May and updated UK national accounts for Q1.

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Daily bond market movements

Bond	Yield	Change
BKO 0 06/23	-0.661	+0.002
OBL 0 04/26	-0.564	+0.011
DBR 0 08/31	-0.170	+0.022
UKT 0 ⁷ / ₈ 01/23	0.056	+0.007
UKT 0 ¹ / ₈ 01/26	0.348	+0.011
UKT 4 ³ / ₄ 12/30	0.741	+0.020

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

Source: Bloomberg

Euro area

Commission sentiment indicator rises to 21-year high

As foreshadowed by various national indicators released over the past week, today's Commission business and survey results for June suggested a marked improvement in confidence at the end of Q2. Indeed, the headline euro area economic sentiment indicator (ESI) rose a substantive 3.4pts to 117.9, the second-highest reading on the series dating back 36 years, and a level only previously surpassed in May 2000 at the peak of the boom following the launch of the single currency. Sentiment improved in each of the three largest member states, most notably rising to a post-reunification high in Germany and to a 21-year high in Italy. Across the various sectors, the survey reported broad-based improvement, albeit one that was led by services, for which sentiment jumped back above the long-run average to the best since December 2019 as firms looked forward to sustained recovery in sales. Industrial sector confidence also advanced further, rising to a new series high boosted by improved assessments of order books, which matched the series high. Retail confidence rose for a fourth successive month further above the respective long-run average to the highest since December 2017. And also supported by new orders, sentiment in construction, which was also above the long-run norm for the sector, rose to a post-pandemic high.

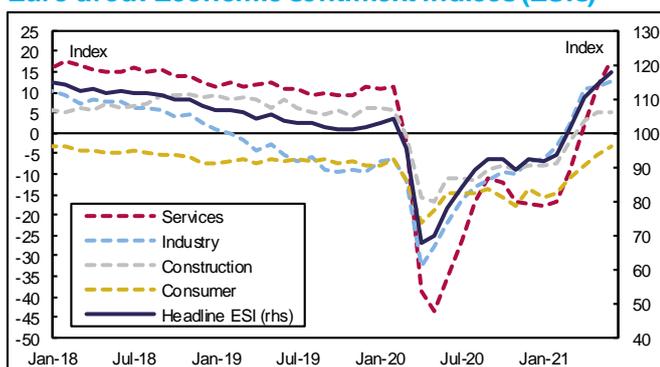
Consumer price expectations rise but continue to lag those of businesses

Among other details, the Commission survey reported a further improvement in business employment expectations to the best since November 2018, with gains in services and industry more than offsetting a slight weakening in construction. And that coincided with a sharp decline, well below the long-run average, in consumer fears of unemployment, as well as a renewed rise in household willingness to make major purchases. Less happily, the survey also implied that supply bottlenecks continue to bite, with the adequacy of retail sector inventories and stocks of finished products in manufacturing falling further to series lows. In addition, selling price expectations rose significantly for a fourth successive month, reaching series highs in industry and retail trade and the highest since the start of 1992 in construction. In services, selling price expectations also rose, returning to their January 2019 level. Consumer price expectations also increased for a sixth successive month, albeit not as significantly as those of businesses. Indeed, the respective survey measure merely reached the highest since May 2020, suggesting that firms continue to have difficulty passing on increased costs.

German inflation eases back in June due to energy, food and services

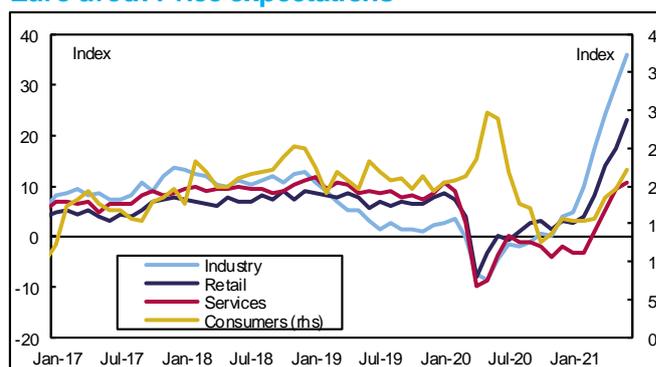
Consistent with a still-modest pass-through from producer cost pressures to consumer prices, according to the flash estimates German inflation moderated in June, with the national measure easing 0.2ppt from May's near-decade high to 2.3%YY and the EU HICP measure falling back 0.3ppt from a three-year high to 2.1%YY. The decline was in part due to

Euro area: Economic sentiment indices (ESIs)



Source: European Commission, Refinitiv and Daiwa Capital Markets Europe Ltd.

Euro area: Price expectations*



*European Commission survey indices for price-setting expectations, except for consumers. Source: Refinitiv and Daiwa Capital Markets Europe Ltd.

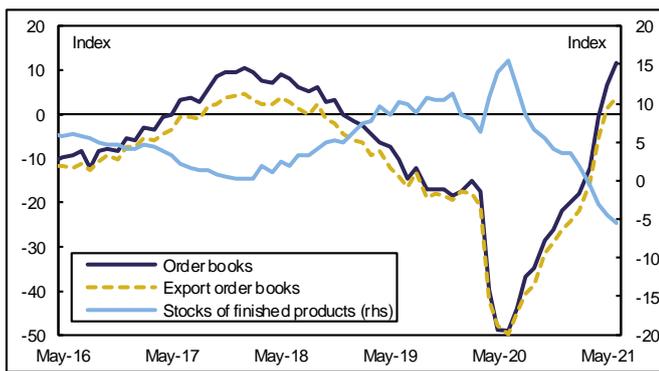
lower energy inflation, which eased back 0.6ppt from May's ten-year high to 9.4% Y/Y. And food inflation, which fell 0.3ppt to 1.6% Y/Y, also weighed. Moreover, services inflation was also weaker, dropping 0.6ppt to 1.6% Y/Y, seemingly due to lower inflation of package holidays and as fewer items were imputed by the statisticians as the economy reopened. So, while inflation of goods (including energy and food) was steady at 3.1% Y/Y, likely due to higher clothing prices, core inflation likely fell back 0.1ppt to 1.8% Y/Y. Of course, with prices having dropped in each month of Q3 last year not least due to the temporary cut VAT, base effects will push German inflation higher over coming months, before declining sharply back below 2.0% Y/Y in January. Meanwhile, in Spain, the flash estimate of the national measure of inflation also fell in June, albeit by just 0.1ppt to 2.6% Y/Y. While no detail was published, the Spanish statistical institute stated that fuel prices had been the cause of the decline and the national measure of core inflation was unchanged at just 0.2% Y/Y. Spanish HICP inflation was also unchanged at 2.4% Y/Y. Following today's data, we maintain our expectation that tomorrow's flash estimates for the euro area will see headline inflation fall back 0.2ppt to 1.8% Y/Y with the core measure also easing 0.1ppt to 0.8% Y/Y.

Regional elections suggest open race for French Presidency in 2022

As in the first round a week earlier, Marine Le Pen's far-right National Rally (RN) and President Macron's République En Marche (LREM) fared poorly in the Sunday's second round of France's regional elections, with the results giving a confidence boost to the centre-right Les Républicains (LR) ahead of the presidential elections next April. Indeed, the presidencies of each of the twelve metropolitan regions in mainland France were retained by the respective incumbent from the centre-right or centre-left. Notably, with less than 43% of the vote, the RN candidate fell well short of winning the party's key target of Provence-Alpes-Cote d'Azur in South-East France, where other centre-left or centre-right parties withdrew their candidates to allow the incumbent from LR a clear path to victory. In addition, Xavier Bertrand (LR) comfortably retained the presidency of the Northern Hauts de France region, winning more than 52% of the vote, double the share of his RN challenger, to amplify his chances of representing the centre-right in next year's national presidential election. Indeed, a national opinion poll conducted by Ipsos/Sopra Steria in the days just ahead of Sunday's regional elections suggests that Bertrand's share of support is now up to about 18%, within striking distance of the shares just shy of one quarter currently enjoyed by both Macron and Le Pen. However, the presidents of Auvergne-Rhône-Alpes (LR's Laurent Wauquiez) and the greater Paris region (Valérie Pécresse from the small conservative Soyons Libre party) also did their potential runs for the national presidency no harm, and it remains unclear around which candidate centre-right support will coalesce next spring.

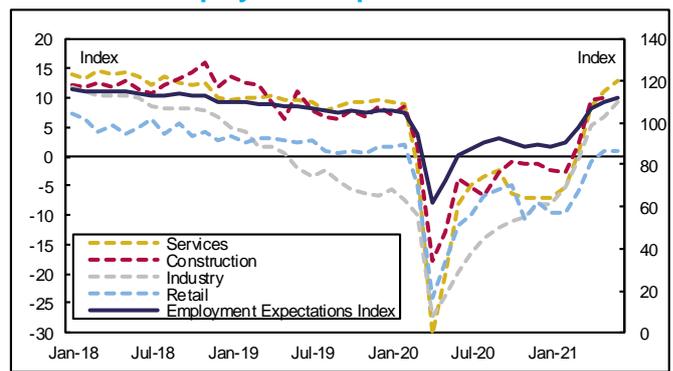
With turnout in the regional elections extremely low at less than 35%, we would caution against drawing strong conclusions from Sunday's results. Indeed, on balance, we maintain our expectation that Macron and Le Pen will face off against each other for the Presidency in the second round on 24 April. However, if anything, the regional polls suggest that we should

Euro area: Selected industrial sector indices*



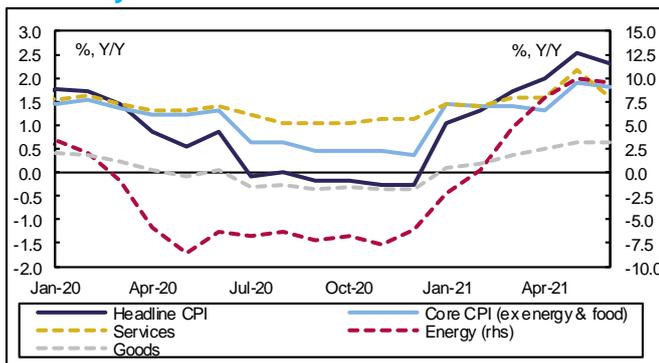
*Commission survey indices. Source: European Commission, Refinitiv and Daiwa Capital Markets Europe Ltd.

Euro area: Employment expectations



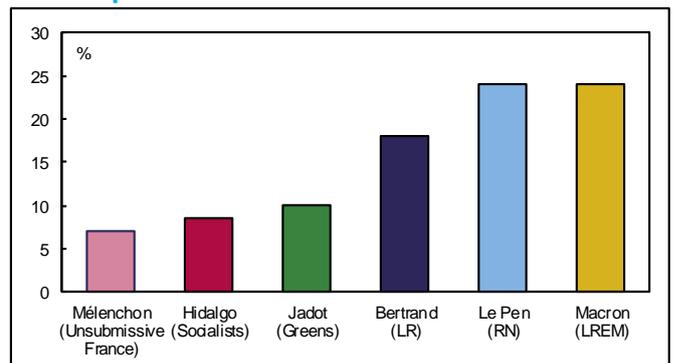
Source: European Commission, Refinitiv and Daiwa Capital Markets Europe Ltd.

Germany: Inflation*



*Flash estimates for June 2021. National measure of inflation. Source: Refinitiv and Daiwa Capital Markets Europe Ltd.

French presidential election: Round 1 vote intention



Source: Ipsos/Sopra Steria poll for France TV, Radio France and LCP-National Assembly and Daiwa Capital Markets Europe Ltd.

not rule out the possibility that a centre-right candidate will qualify for that run-off at the expense of one or the other. And if and when Le Pen again makes it through to the second round, we would strongly expect her opponent – Macron, Bertrand or an alternative from the centre-right – to defeat her, leaving the broad direction of French policy little changed.

The day ahead in the euro area

Following today's flash inflation figures from Germany and Spain, tomorrow brings the release of the equivalent data from the euro area, France, Italy and several smaller member states. With the annual rate of energy inflation now likely to have peaked, we expect the headline euro area HICP rate to fall back 0.2ppt to 1.8%YY with the core measure also easing 0.1ppt to 0.8%YY. Other new data due on Wednesday include figures for German jobless claims in June and French consumer spending on goods in May.

UK

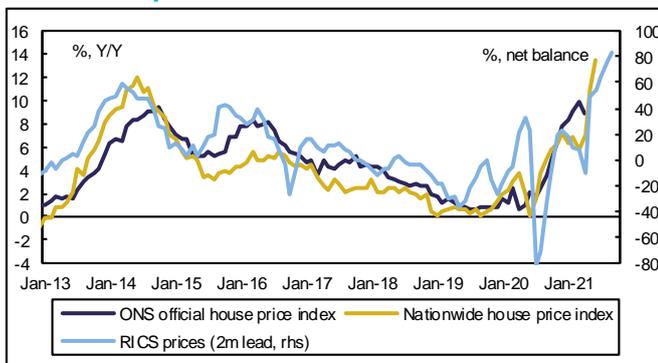
House price inflation up to highest since 2004

According to the Nationwide index, UK house prices rose 0.7%MM in June taking the annual inflation rate to 13.4%YY, the highest since 2004. Strength was seen across all regions of the UK, led by Northern Ireland and Wales (up 14%YY and 13.4%YY respectively in Q2), with Scotland (7.1%YY) and London (7.3%YY) lagging somewhat. Given base effects – prices fell in both May and June last year before rebounding from July on – the annual rate will slow next month. And the tapering and eventual conclusion of the government's stamp duty holiday in September is also likely to weigh on home prices heading towards year-end. However, today's BoE lending data reported an increase in mortgage approvals in May to a three-month high of 87.5k, well above the range from the global financial crisis to last summer, suggesting that momentum remains strong for now. Indeed, net mortgage borrowing rose in May to £6.6bn, more than 50% above the average in the year ahead of the pandemic. And average mortgage interest rates remained exceptionally low, with the effective rate on new mortgages up just 2bps in May to 1.90%, close to the pre-pandemic level and only 18bps above the series low, helping to maintain affordability manageable despite the recent price gains. So, assuming that unemployment does not leap sharply as and when the government's Job Retention Scheme is brought to an end in the autumn, housing market demand should remain firm for a while yet. And with the supply of new homes onto the market still low, house prices should remain firm too.

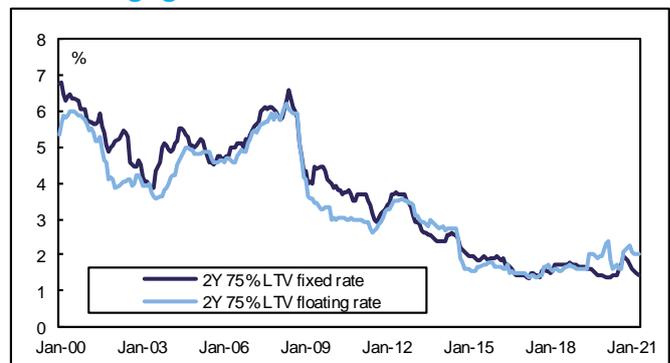
The day ahead in the UK

Tomorrow's final Q1 national accounts data are expected to confirm that UK GDP contracted by 1.5%Q/Q, more than reversing the growth of 1.3%Q/Q in Q4 to leave output down 6.1%YY and 8.7% below the pre-pandemic level in Q4 19. However, the trough came in January and monthly growth in February (0.7%MM) and March (2.1%MM) left economic output at the end of Q1 down a more moderate 5.9% from the pre-pandemic level. The updated expenditure figures will confirm that private consumption more than fully accounted for the decline in GDP, albeit with fixed investment and inventories also subtracting from growth but government spending and net trade providing some offset. The first release of balance of payments data for Q1 will also be released tomorrow. The BRC shop price index and Lloyds Business Barometer for June are also due tomorrow.

UK: House price indicators



UK: Mortgage interest rates*



European calendar

Today's results

Economic data

Country	Release	Period	Actual	Market consensus/ <i>Daiwa forecast</i>	Previous	Revised
EMU	 European Commission final consumer confidence	Jun	-3.3	-3.3	1.7	-
	 European Commission industrial (services) confidence	Jun	12.7 (17.9)	12.0 (14.5)	11.5 (11.3)	-
	 European Commission economic confidence	Jun	117.9	116.4	114.5	-
Germany	 Preliminary CPI (EU-harmonised CPI) Y/Y%	Jun	2.3 (2.1)	2.3 (2.1)	2.5 (2.4)	-
France	 INSEE consumer confidence	Jun	102	100	97	-
Spain	 Retail sales Y/Y%	May	19.6	-	41.0	40.5
	 CPI (EU-harmonised CPI) Y/Y%	Jun	2.6 (2.4)	2.7 (2.4)	2.7 (2.4)	-
UK	 Net consumer credit £bn (Y/Y%)	May	0.3 (-3.2)	0.3 (-)	-0.4 (-5.7)	-0.2 (-)
	 Net mortgage lending £bn (approvals '000s)	May	6.6 (87.5)	4.2 (85.3)	3.3 (86.9)	3.0 (-)
	 M4 money supply Y/Y%	May	7.3	-	9.1	-
	 Nationwide house price index M/M% (Y/Y%)	Jun	0.7 13.4)	0.8 (13.7)	1.8 (10.9)	-

Auctions

Country	Auction
- Nothing to report -	

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

Tomorrow's releases

Economic data

Country	BST	Release	Period	Market consensus/ <i>Daiwa forecast</i>	Previous
EMU	 10.00	Preliminary CPI (core CPI) Y/Y%	Jun	1.8 (0.8)	2.0 (1.0)
Germany	 08.55	Unemployment change '000s (rate %)	Jun	-19.0 (5.9)	-15.0 (6.0)
France	 07.45	Preliminary CPI (EU-harmonised CPI) Y/Y%	Jun	1.6 (1.9)	1.4 (1.8)
	 07.45	PPI Y/Y%	May	-	7.3
	 07.45	Consumer spending on goods M/M% (Y/Y%)	May	7.8 (-)	-8.3 (32.0)
Italy	 10.00	Preliminary CPI (EU-harmonised CPI) Y/Y%	Jun	1.4 (1.4)	1.3 (1.2)
	 09.00	PPI Y/Y%	May	-	7.9
UK	 00.01	Lloyds business barometer	Jun	-	33
	 00.01	BRC shop price index Y/Y%	Jun	-	-0.6
	 07.00	Final GDP Q/Q% (Y/Y%)	Q1	-1.5 (-6.1)	1.3 (-7.3)
	 07.00	Current account balance £bn	Q1	-15.2	-26.3

Auctions and events

Italy	 10.00	Auction: 5Y & 10Y bonds
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Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

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