

# Euro wrap-up

## Overview

- Bunds were little changed while euro area unemployment fell further than expected, German retail sales rebounded somewhat, and the flash PMIs were largely revised up to suggest stronger output and higher prices.
- Gilts made very modest losses while Governor Bailey insisted that the BoE wouldn't overreact to current price pressures.
- A quiet end to the week for economic data will bring news on euro area producer prices and the Spanish labour market.

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### Daily bond market movements

Bond	Yield	Change
BKO 0 06/23	-0.677	-0.006
OBL 0 04/26	-0.590	-
DBR 0 08/31	-0.201	+0.008
UKT 0 7/8 01/23	0.057	+0.006
UKT 0 7/8 01/26	0.331	+0.004
UKT 4 3/4 12/30	0.726	+0.012

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

Source: Bloomberg

## Euro area

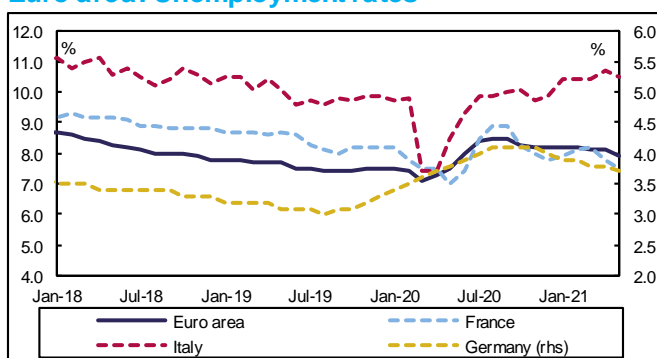
### Unemployment down again in May with widespread improvement

Benefiting from gradual economic reopening as well as ongoing support from government job retention schemes, the euro area's labour market continues to outperform expectations. The region's unemployment rate fell 0.2ppt in May to 7.9%, 0.6ppt below the pandemic peak in August and September and the lowest in one year, albeit still 0.8ppt above the trough in March 2020. The improvement was widespread too, with the equivalent ILO unemployment rates for each of the five largest member states declining, and France leading the way with a fall of 0.3ppt to 7.5%. The number of unemployed workers dropped 306k, the most since November, to 12.8mn, the lowest since June and about 1.1mn below the peak in September. However, that was still some 1.3mn above the March 2020 trough. Moreover, the unemployment rate was still likely flattered by the large number of workers who have left the labour force – the most up-to-date figures showed that euro area employment in Q121 was still down almost 3.6mn (2.2%) from the pre-pandemic peak in Q419. And a significant share of the labour force (probably still some 6% in March, albeit down from the peak of 20%) remained covered by job retention schemes. With business surveys flagging increased intentions to hire, and household fears of unemployment having dropped below the long-run average, we look for a further drop in joblessness over the near term. And while the resumption of job-seeking by many workers who had left the labour force will in due course add some upwards pressure to the unemployment rate, the ECB's latest full-year projection of 8.2% appears too downbeat to us. At the same time, however, with broader underemployment, including those working fewer hours than desired, likely still to be close to 15% (full Labour Force Survey data for Q121 will only be released on 15 July), we expect wage settlements to remain underwhelming and below levels consistent with the ECB's inflation objective heading into 2022.

### German retail sales rebound in May, consistent with firm growth in Q2

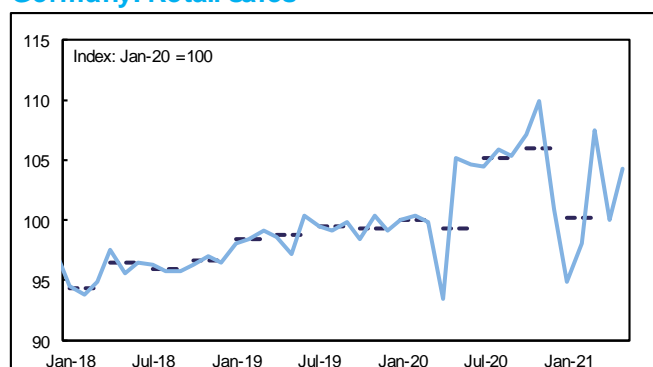
German retail sales rebounded in May as pandemic restrictions were lifted, but still fell a touch short of expectations. Indeed, the rise of 4.2%MM in real terms was not sufficiently strong to reverse April's drop of 6.8%MM, the second-steepest of the pandemic. Nevertheless, that still took sales almost 4.0% above the pre-pandemic level of February 2020. And with the average for the first two months of Q2 2.0% above the Q1 average, the data underscore the likelihood of a firm return to positive growth in consumption and GDP this quarter. Sales of all major items increased, led by clothing and footwear, sales of which rose 75%MM in nominal terms to the highest level since November, albeit remaining below their pre-pandemic level. Sales of home furnishings, IT goods and food, were also significantly stronger in May but failed to reverse fully the drop in April. Mobility data point to further firm growth in retail sales in June, although overall growth will be restrained by a pullback in shopping online.

### Euro area: Unemployment rates



Source: Refinitiv and Daiwa Capital Markets Europe Ltd.

### Germany: Retail sales\*



\*Dashed lines represent full-quarter averages.  
Source: Refinitiv and Daiwa Capital Markets Europe Ltd.

### New car registrations remain well below pre-pandemic norms in June

Having been flattered by base effects over recent months, French new car registrations in June disappointed, falling 14.7% Y/Y. While that left the total over the first six months of the year up 28.9% Y/Y, the June level was down 14% from the same month in 2019, and indeed 10% below the average for the month throughout the decade ahead of the pandemic. In Italy, meanwhile, new car registrations were up 12.6% Y/Y to be up 51% Y/Y over the first six months of the year. However, Italy's June level was still down 5% from the same month in 2019, and 13% below the average June level throughout the decade ahead of the pandemic.

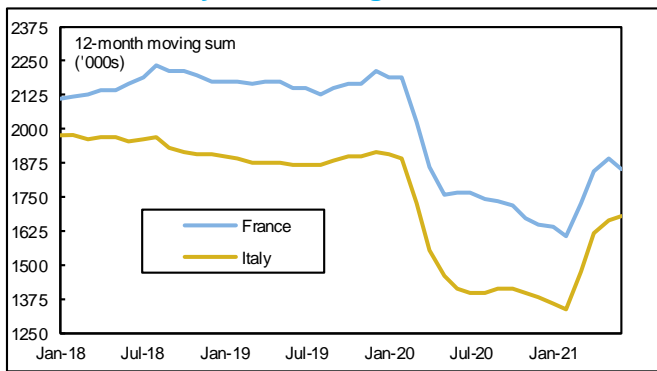
### Final manufacturing PMIs underscore impression of strength at end-Q2

Notwithstanding continued struggles in the auto sub-sector – which likely reflect a mix of supply- and demand-side issues – the final manufacturing PMIs for June were in almost every way stronger than the flash estimates, underscoring the impression of strong momentum at the end of Q2. So, for example, the region's output index was revised up a further few bps to 62.7, up 0.5pt from May and just 0.6pt below the series high reached in March. Markit reported strongest growth in the capital goods sector, although the intermediate goods sub-sector also reportedly registered a record high. New orders were also stronger than previously thought and close to series highs, while the survey measure of employment in the sector was revised up to a level never previously exceeded. At the same time, however, evidence of supply bottlenecks was stronger still, with the survey measures of backlogs and delivery times revised up to the second-highest on the series, and the input price PMI similarly nudged up to a series high (88.5). While unchanged from the flash estimate, the output price PMI was also the highest on record (71.1). At the country level, the output indices for both Germany and France were also revised up, with the former stronger on the month. And vigorous growth was widespread across the euro area, with the Netherlands still leading the way, output rising at a record high in Spain, and a historically high pace of expansion again recorded in Italy.

### The day ahead in the euro area

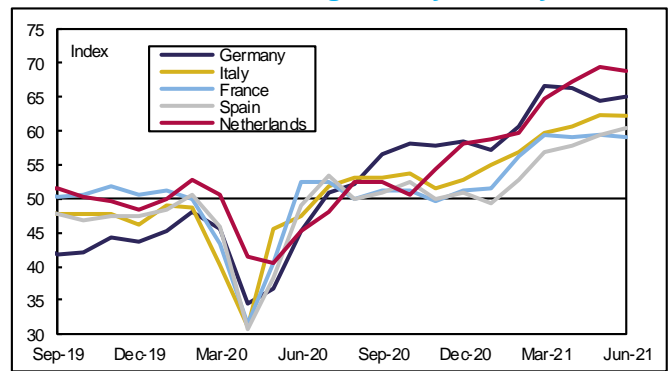
The week will end on a relatively quiet note for economic data from the euro area with May's producer price figures for the region most notable. With prices likely to rise by 1.0% M/M or more for the fourth month out of the past five, the annual PPI rate is likely to rise about 2ppts to about 9.5% Y/Y, which would be the highest since 1982. Given base effects, however, that is likely to represent the peak. Spanish unemployment claims data for June are also due tomorrow.

#### France and Italy: New car registrations



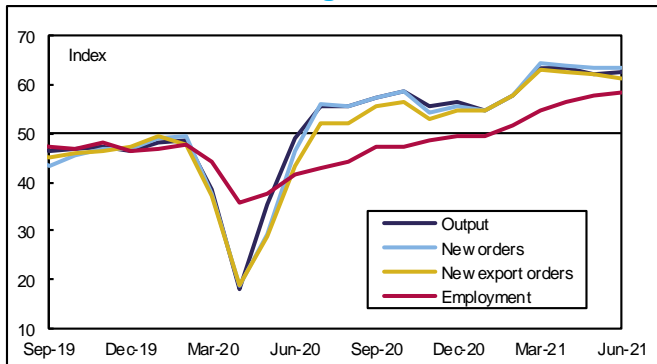
Source: Refinitiv and Daiwa Capital Markets Europe Ltd.

#### Euro area: Manufacturing PMIs by country



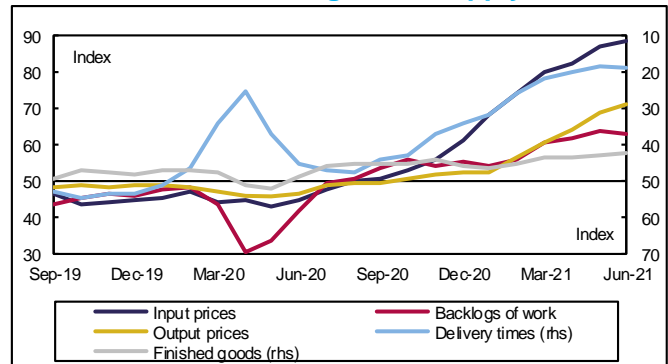
Source: Markit, Refinitiv and Daiwa Capital Markets Europe Ltd.

#### Euro area: Manufacturing PMIs – demand-side



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

#### Euro area: Manufacturing PMIs – supply-side



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

## UK

### Manufacturing output and orders PMIs revised down, stronger evidence of supply bottlenecks

While still consistent with vigorous growth in the sector, the UK's final manufacturing PMIs were somewhat disappointing, with the output and new orders indices revised down, and the symptoms of supply bottlenecks seemingly even more acute than previously thought. So, the output PMI of 61.1 was down almost 2pts from May while the new orders PMI of 64.2 was almost 4pts below the level the previous month. And a downwardly revised index for new export orders to more than 4pts below the May level again suggested that the UK is failing to benefit as much as its peers from the rebound in global demand. Meanwhile, the PMIs for delivery times and backlogs were at levels beaten only once on the series, while those for input (89.2) and output prices (73.2) were revised up to new record highs.

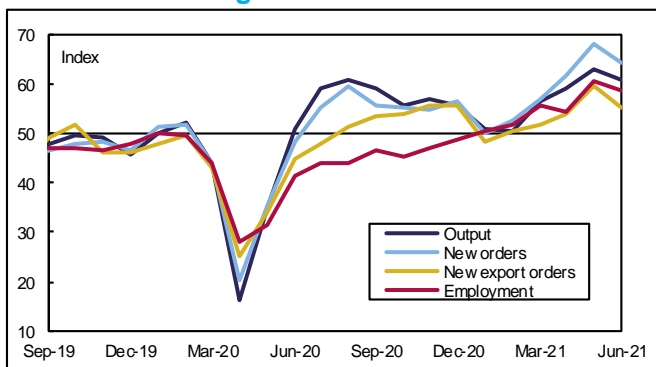
### Bailey insists BoE shouldn't overreact to current price pressures

Despite the evidence of significant near-term price pressures in many survey indicators and hard data, in his Mansion House speech today BoE Governor Bailey underscored his expectation that they would prove temporary. Indeed, following further hyperbolic comments this week from departing Chief Economist Haldane, flagging upside risks to inflation and calling the current juncture a "dangerous moment" for the economy, Bailey countered that it was "important not to overreact". In a characteristically balanced speech, he outlined "well-founded" reasons why pressures will be short-lived, including the scope for supply to eventually meet increased demand in the most affected sectors, the high probability of a switch back from spending on goods to services as the pandemic continues to fade, well anchored inflation expectations, and the still significant amount of labour market slack. With respect to the latter, HMRC today confirmed that there were 2.4mn workers still supported by the job retention scheme at end-May, with about half of that number working part-time, while from today firms will have to pay 10% of their wages. Meanwhile, although Bailey acknowledged that the economy was enjoying a "very rapid bounce-back" in response to the easing of restrictions and growing public confidence, he expected underlying growth eventually to revert to the underwhelming rates seen after the global financial crisis, with equilibrium interest rates also likely to remain low in the UK and elsewhere around the world. Bailey's views expressed today are highly likely to be shared by the other remaining MPC members. So, we maintain our view that Bank Rate will remain unchanged at least until 2023.

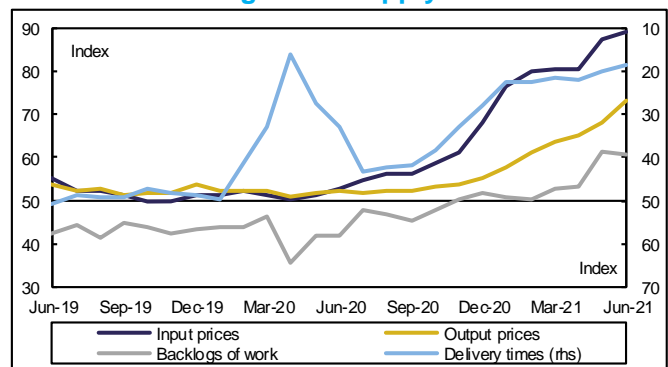
### The day ahead in the UK

Friday should be uneventful in the UK with no top-tier economic data due for release.

#### UK: Manufacturing PMIs – demand side













#### UK: Manufacturing PMIs – supply side












## European calendar

### Today's results

#### Economic data

Country	Release	Period	Actual	Market consensus/ <u>Daiwa forecast</u>	Previous	Revised
EMU	 Final manufacturing PMI	Jun	<b>63.4</b>	63.1	63.1	-
	 Unemployment rate %	May	<b>7.9</b>	8.0	8.0	-8.1
Germany	 Final manufacturing PMI	Jun	<b>65.1</b>	64.9	64.4	-
	 Retail sales M/M% ((Y/Y%))	May	<b>4.2 (-2.4)</b>	4.6 (-1.0)	-5.5 (4.4)	-6.8 (5.1)
France	 Final manufacturing PMI	Jun	<b>59.0</b>	58.6	59.4	-
	 New car registrations* Y/Y%	Jun	<b>-14.7</b>	-	46.4	-
Italy	 Manufacturing PMI	Jun	<b>62.2</b>	62.5	62.3	-
	 New car registrations Y/Y%	Jun	<b>12.6</b>	-	43.0	-
Spain	 Manufacturing PMI	Jun	<b>60.4</b>	59.5	59.4	-
UK	 Final manufacturing PMI	Jun	<b>63.9</b>	64.2	65.6	-



#### Auctions

Country	Auction
France	 sold €2.794bn of 2030 bonds at an average yield of 0.03%
	 sold €4.176bn of 2031 bonds at an average yield of 0.13%
	 sold €2.023bn of 2036 bonds at an average yield of 0.42%
	 sold €1.999bn of 2040 bonds at an average yield of 0.62%
Spain	 sold €1.878bn of 2026 bonds at an average yield of -0.245%
	 sold €1.652bn of 2028 bonds at an average yield of 0.036%
	 sold €1.209bn of 2050 bonds at an average yield of 1.404%
	 sold €0.547bn of 2033 index-linked bonds at an average yield of -0.739%
UK	 sold €3.5bn of 2025 bonds at an average yield of 0.281%



Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

### Tomorrow's releases

#### Economic data

Country	BST	Release	Period	Market consensus/ <u>Daiwa forecast</u>	Previous
EMU	 10.00	PPI Y/Y%	May	9.5	7.6
Spain	 08.00	Unemployment change '000s	Jun	-110.0	-129.4

#### Auctions and events

EMU	 13.30	ECB President Lagarde speaks publicly
	 08.00	ECB Governing Council member Hernandez de Cos speaks publicly

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

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