

Euro wrap-up

Overview

- Bunds followed US10s higher even as the Bundesbank predicted a return of German GDP to the pre-pandemic level this quarter, while euro area construction and French retail sales data posted growth.
- Gilts rallied as external MPC members Haskel and Mann argued against a pre-emptive tightening of BoE monetary policy.
- Tuesday will bring the ECB's bank lending survey and German producer price data for June.

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Daily bond market movements

Bond	Yield	Change
BKO 0 06/23	-0.701	-0.010
OBL 0 04/26	-0.661	-0.019
DBR 0 08/31	-0.390	-0.033
UKT 0 ¹ / ₈ 01/23	0.061	-0.045
UKT 0 ¹ / ₈ 01/26	0.264	-0.058
UKT 4 ³ / ₄ 12/30	0.550	-0.075

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

Source: Bloomberg

Euro area

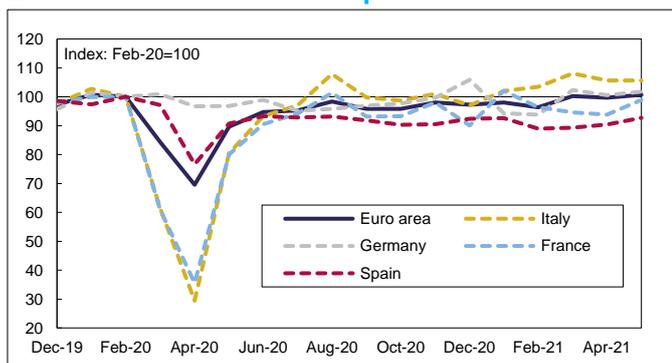
Construction output on track for solid growth in Q2, and probably beyond

While the back end of this week will be eventful in the euro area, bringing the ECB's latest policy announcement and the July flash PMIs, the first few days are set to be relatively quiet for economic news. Nevertheless, today brought a few data releases of second-tier importance which provided further insight into the strength of economic activity in the second quarter. Among these, the latest figures for euro area construction output reported growth of 0.9%M/M in May. That followed a drop of 0.4%M/M in April, which was significantly smaller than previously thought. So, it took euro area construction output to a new pandemic-era high and 0.6% above the level in February 2020. And it also left the average level in the first two months of Q2 2% above the average in Q1. So, euro area construction output looks set to register a fourth consecutive quarter of positive growth in Q2, and significantly stronger than the rates of 0.8%Q/Q and 0.6%Q/Q in the prior two quarters. For the second successive month, growth in building work (up 0.9%M/M), stimulated not least by the buoyant housing market, offset a drop in civil engineering output (-0.1%M/M). Growth was broad-based among the large member states, and led by France (5.4%M/M) and Spain (2.5%M/M). Looking ahead, surveys point to ongoing steady expansion in the sector, with confidence and new orders elevated by historical standards, particularly in Italy. Strong fundamentals in the residential property market and signals of a firm rebound in business investment also suggest that construction output should remain on an uptrend over coming quarters, with the EU recovery funds set to support civil engineering activity heading into 2022. Sadly, reconstruction from the past week's devastating floods in Germany, Austria and the Low Countries will also boost the sector.

French retail sales up in June but down in Q2 as a whole

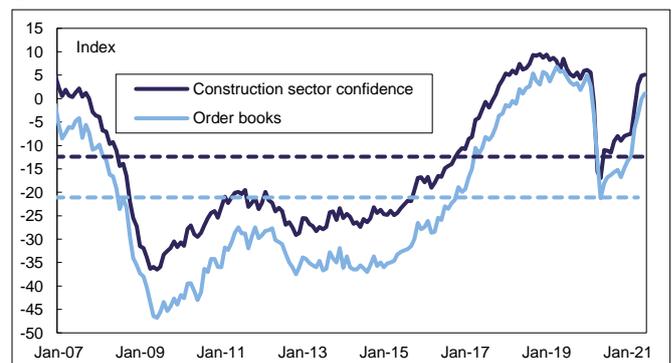
According to the Bank of France's latest retail survey, French retail sales grew for a second successive month in June, up 1.5%M/M following a rebound of 5.3%M/M in May. That, however, left sales down 2.3% from the pre-pandemic level in February 2020. And given the sharp drop of 6.6%M/M in April when restrictions were temporarily imposed, the Bank of France's measure of retail sales in Q2 fell 1.9%Q/Q from Q1. Within the detail, sales of food were little changed in June, rising just 0.2%M/M, to be down 0.9%Q/Q in Q2 and 6.6% below the pre-pandemic level. And while sales of manufactured products rose 10.2%M/M in June, supported by purchases of new cars (10.2%M/M) and clothing and textiles (25.6%M/M), they were down 6.2%Q/Q in Q2 but still some 4.4% above the pre-pandemic level. Of course, retail sales do not reflect total household consumption, and spending on a range of services was much more vigorous at the end of Q2 following the relaxation of restrictions on 9 June. Indeed, based on its business conditions survey, the Bank of France estimated that the level of hospitality activity last month jumped roughly 180%M/M, albeit to a level 30% below normal. Overall, with economic activity judged to have increased steadily throughout the quarter, the Bank of France earlier this month estimated that, having contracted 0.1%Q/Q in Q1, French GDP grew by about 1.0%Q/Q in Q2.

Euro area: Construction output



Source: Refinitiv and Daiwa Capital Markets Europe Ltd.

Euro area: Construction confidence and orders



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

German hospitality subdued in May, but GDP on track for growth in Q2 and Q3

Activity in the German hospitality sector remained subdued in May. On a seasonally adjusted basis, turnover in accommodation and food services fell 8.5%M/M from April to be almost 69% below the pre-pandemic level in February 2020. That left the average in the first two months of Q2 down some 22% from the Q1 average. In contrast to France, however, German retail sales were on track to contribute positively to GDP in Q2, trending 2.4% above the Q1 level in the first two months of last quarter. And mobility data point to firm growth in Germany in both hospitality and retail in June. Indeed, citing the likelihood of strong growth in services, the Bundesbank today assessed that German GDP growth was strong in Q2, reversing the contraction of 1.8%Q/Q in Q1. And with accelerated expansion expected in Q3, the Bundesbank flagged the possibility that German GDP might return to the pre-pandemic level in the current quarter. While the past week's severe floods, which killed more than 150 German citizens, affected some of the country's most populous and developed states (North Rhine-Westphalia and Rhineland-Palatinate) they are unlikely to have a sizeable macroeconomic impact not least as the major industrial centres were unaffected.

The day ahead in the euro area

Looking ahead, tomorrow sees the release of German producer price data for June, which will provide further insight into inflation pressures at the factory gate. In May, the German PPI rose 7.2%Y/Y, the fastest rate of growth since October 2008 and with significant pressures in prices of intermediate goods. A further rise in June to 8.6%Y/Y is expected tomorrow. In addition, the ECB's latest quarterly bank lending survey will provide insights into financial conditions in the region and euro area external current account data for May are also due.

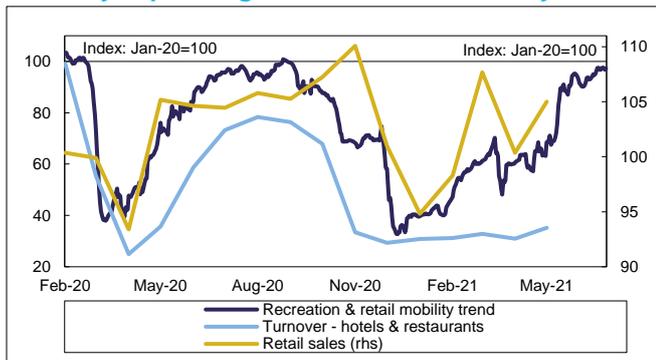
UK

Haskel and Mann argue against premature monetary tightening

After last week's more hawkish comments from two BoE MPC members ([Ramsden and Saunders](#)) flagging the possibility of an early end to QE next month and also perhaps rate hikes next year, external member Jonathan Haskel and new nominee Catherine Mann both spoke publicly today. Unlike last week's speakers, both were dovish. Among other things, Haskel judged that the long-term scarring of the UK economy from the pandemic was likely to be less severe than he had previously feared. And he noted that greater optimism about the outlook might well boost demand further over the near term relative to supply, thus adding to inflationary pressure. But Haskel also expected much of the high inflation to be a temporary phenomenon. Moreover, despite his broadly upbeat assessment, he also judged that the UK economy had not yet fully recovered from the shock of the pandemic, and faced additional headwinds ahead, not least from the delta variant – which continues to spread rapidly – and future fiscal tightening as the special support measures are phased out. As such, Haskel stated that "risk-management considerations lean against a pre-emptive tightening of monetary policy until we can be more sure the economy is recovering in a manner consistent with the sustained achievement of the inflation target." In an answer to questions, Haskel suggested that an early end to the BoE's net purchases next month would represent a tightening of policy. Therefore, based on today's speech, Haskel would seem likely on 5 August to vote in favour of maintaining the BoE's asset purchase target at £895bn, with those purchases to be conducted until near year-end.

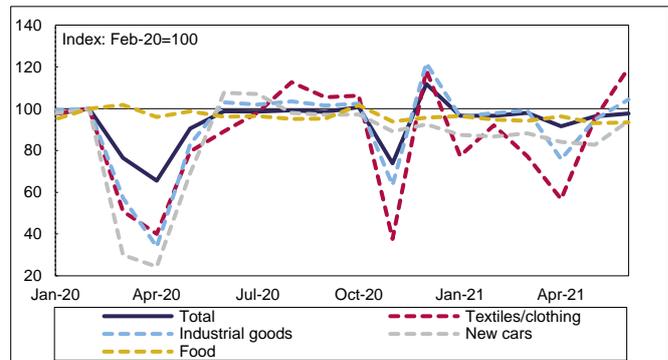
Meanwhile, Catherine Mann acknowledged that a "major surge" in inflation was underway. But she did not expect it to persist. And referring to the lessons of the global financial crisis, she also argued that the BoE should avoid premature tightening to ensure that the economic recovery will be sustained. Mann is not scheduled to take her place on the MPC until September, and so will not attend next month's policy meeting. However, her views and those of Haskel are a reminder that the hawks have not yet won the argument. Deputy Governor Ben Broadbent's scheduled speech this Thursday will now be closely watched.

Germany: Spending indicators and mobility trends*



*The baseline for mobility is the median value, for the corresponding day of the week, during the five-week period 3 Jan–6 Feb 2020. 7-day moving average.
 Source: Google Mobility Report, Destatis, Refinitiv and Daiwa Capital Markets Europe Ltd.

France: Retail sales



Source: Bank of France, Refinitiv and Daiwa Capital Markets Europe Ltd.

The day ahead in the UK

The UK data calendar will again be very quiet tomorrow, with no releases scheduled. Attention, therefore, will remain on pandemic developments, with the uptrend in new covid-19 cases on track to rival January's peak after most remaining restrictions in England were lifted today.

European calendar

Today's results						
Economic data						
Country	Release	Period	Actual	Market consensus/ <i>Daiwa forecast</i>	Previous	Revised
Euro area	Construction output M/M% (Y/Y%)	May	0.9 (13.6)	-	-2.2 (42.3)	-0.4 (45.2)
UK	Rightmove house prices M/M% (Y/Y%)	Jul	0.7 (5.7)	0.7 (5.7)	0.8 (5.1)	-
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	
Euro area	10.00	Current account balance €bn	May	-	22.8	
Germany	07.00	PPI Y/Y%	Jun	8.5	7.2	
Auctions and events						
Euro area	09.30	ECB bank lending survey				
Germany	10.30	Auction: €4bn of 0% 2028 bonds				
UK	10.00	Auction: £1.25bn of 1% 2071 bonds				

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

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