

Euro wrap-up

Overview

- While ECB President Lagarde repeated her key messages from yesterday's hawkish speech, Bunds made gains as Italian inflation posted a broad-based decline in June and euro area net lending to households contracted.
- Gilts made significant gains even as BoE Governor Bailey emphasised that UK core inflation was proving to be far stickier than expected.
- Thursday's focus will be flash inflation estimates from Germany and Spain, the Commission's economic survey results and UK bank lending data.

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Daily bond market movements

Bond	Yield	Change
BKO 2.8 06/25	3.089	-0.039
OBL 2.4 10/28	2.457	-0.049
DBR 2.3 02/33	2.312	-0.039
UKT 0% 06/25	5.115	-0.121
UKT 1% 10/28	4.547	-0.106
UKT 3¼ 01/33	4.308	-0.058

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

Euro area

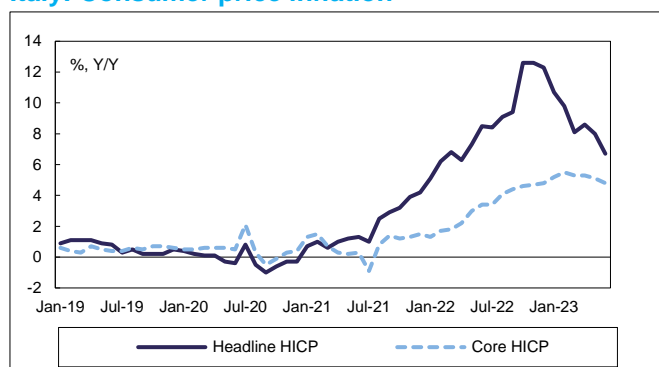
Italian inflation falls to 14-month low on broad-based moderation

While President Lagarde today repeated her hawkish view about the outlook for ECB rates, today's first estimates of inflation in June, which came from Italy, surprised slightly on the downside. On the EU-harmonised HICP measure, inflation stepped down 1.3ppts to a 14-month low of 6.7%Y/Y, almost 6ppts below the peak last autumn. And, encouragingly, the decline was broad-based. Energy prices were again predictably the principal driver, falling for the seventh successive month to push the respective inflation component down a hefty 9.5ppts to 2.0%Y/Y, the lowest in more than two years. Food inflation moderated slightly for a third successive month, down 0.4ppt to a nine-month low of 10.4%Y/Y. In addition, the pace of increase of core goods prices slowed for a fourth successive month, down 0.2ppt to an eight-month low of 5.0%Y/Y. Most notably perhaps, services inflation slowed 0.3ppt from May's series high to 4.8%Y/Y. The driver was lower inflation of transport services, but components for hospitality, leisure and culture also fell. With inflation of both services and non-energy industrialised goods softer, the core HICP rate eased for a second successive month, declining 0.3ppt to a six-month low of 4.8%Y/Y. While welcome, we caution that the core rate in Germany, due tomorrow, is likely to rise from May, perhaps more than offsetting the decline in Italy.

Mortgage lending declines sharply as ECB policy tightening takes its toll

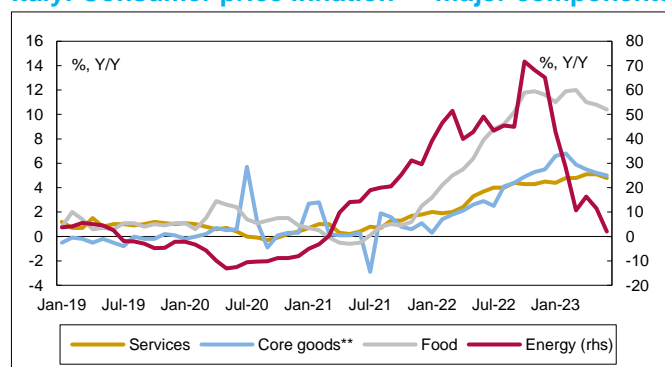
While ECB President Lagarde yesterday flagged significant uncertainties about the current nature of the monetary policy transmission mechanism, the impact of the past year's aggressive rate hikes on both lending and deposits was clearly evident in today's monetary data. Consistent with the rise in mortgage rates to the highest for eleven years, as well as ongoing weakness in the residential property market, lending to households (adjusted for sales and securitization) fell in May for the first time since 2014, by €2.8bn. This left the cumulative flow on a three-month basis at just €5bn, down around €75bn from the peak last April. On an unadjusted basis, loans for house purchase were down a whopping €33.8bn, due overwhelmingly to a substantial drop in France, the most since 2014. Admittedly, the extreme nature of that drop reflected technical factors, adjusted for which the decline would have been much more modest. In addition, likely reflecting demand related to the high cost of living, the net flow of consumer credit remained broadly stable in May, at around €2.0bn, to leave the cumulative flow on a three-month basis at a ten-month high (€6.7bn). And, more encouragingly, the net flow of business lending increased for the first month in four (€8.3bn), amid a stronger rise in the net flow of new loans of maturities greater than five years. That, however, might reflect the shift in the curve and expectations of higher rates to come, rather than firmer business fixed investment. And when adjusting for sales and securitisations, the net flow of loans to business was more modest (€3.2bn), to leave annual growth in the stock of such loans at 4.0%Y/Y, the softest since November 2021.

Italy: Consumer price inflation



Source: Refinitiv and Daiwa Capital Markets Europe Ltd.

Italy: Consumer price inflation* – major components



*HICP measure. **Non-energy industrial goods. Source: Refinitiv and Daiwa Capital Markets Europe Ltd.

Bank deposits continue to decline in response to rising interest rates

As for loans, the ECB's rate hikes also continue to impact bank deposits. Overnight deposits of households and NFCs, which have barely benefited at all from higher interest rates, dropped in May for the eighth and ninth successive months respectively. Admittedly, time deposits with maturities of between three months to two years continued to rise. So, the overall stock of household deposits rose for the first time in four months, although the increase of just €1bn left the cumulative outflow over the past three months at a notable €41bn. And with the net increase in NFC time deposits the lowest in a year, the cumulative outflow in NFC deposits in the three months to May (€65bn) was the largest since the series began in 2003. So, the M1 measure of money supply, which includes currency in circulation and overnight deposits, fell a record 6.4%Y/Y in May. Growth in the broader monetary aggregate M3, which includes time deposits and money market funds among others, slowed to a near-nine-year low of just 1.4%Y/Y.

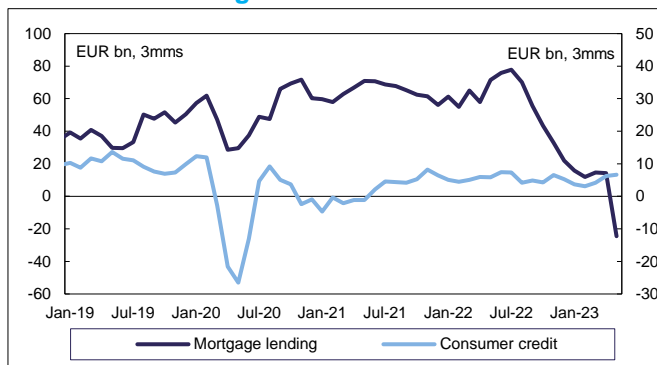
German consumer sentiment softens for first time in 9 months amid greater desire to save

After the [flash PMIs](#) and [ifo survey](#) suggested a deterioration in German business confidence at the end of Q2, today's GfK survey results similarly reported a softening in consumer sentiment. The drop in the survey's headline index – presented as a forecast for July – fell for the first time in nine months, declining by 1pt to -25.4. That is roughly equidistant between the level just before the Russian invasion of Ukraine early last year and the series low reached last autumn after wholesale gas prices hit extreme highs. Importantly, it also remains well below the series average (3.1). Within the survey detail, German consumers appeared somewhat more downbeat about prospects for their personal finances, and also tempered their optimism for the economic outlook. Perhaps unsurprisingly given higher interest rates, they also reported a significant increase in their willingness to save. Nevertheless, their stated willingness to spend also increased back close to the top of the range of the past year, albeit remaining low by historical standards. Overall, therefore, and probably unsurprisingly, the GfK survey suggests that German private consumption is likely to remain at best subdued in the coming quarter.

French consumer confidence rises to a 13-month high but purchase intentions maintain downtrend

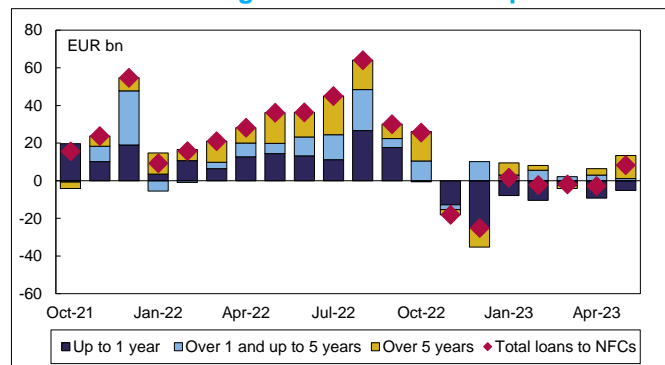
In contrast to Germany but consistent with the improvement reported in yesterday's [Italian ISTAT survey](#), today's INSEE survey suggested that French consumer sentiment recovered in June. In particular, the headline indicator increased 2pts to 85, a thirteen-month high, but nevertheless remained well below the long-run average (100) and still too close for comfort to the series low (80) recorded last September. Within the survey detail, households were reportedly the most upbeat about the prospects for the economic outlook since Russia's invasion of Ukraine, with income expectations also the highest since February 2022 as unemployment fears continued to recede and price expectations fell to the lowest level in fourteen years.

Euro area: Lending to households*



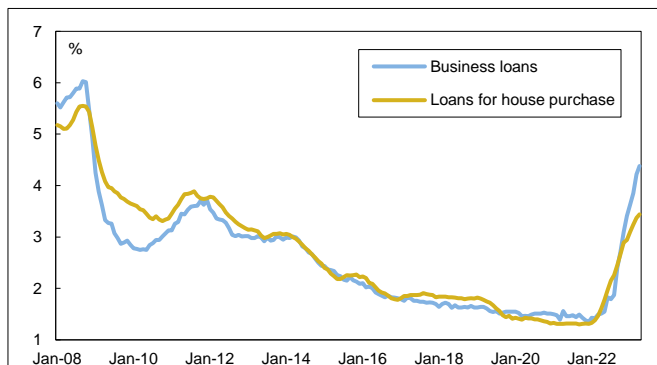
*Unadjusted for sales and securitisations. Source: Refinitiv and Daiwa Capital Markets Europe Ltd.

Euro area: Lending to non-financial corporations*



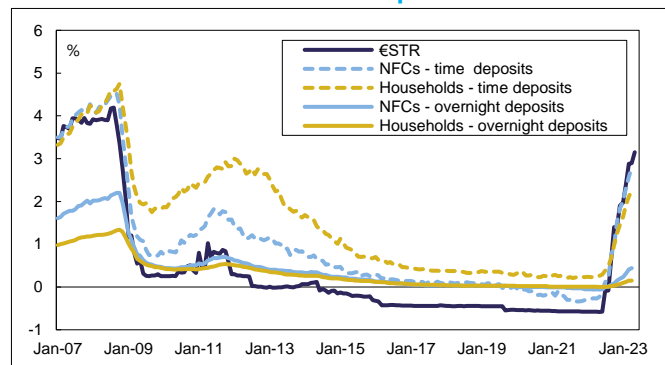
*Unadjusted for sales and securitisations. Source: ECB and Daiwa Capital Markets Europe Ltd.

Euro area: Interest rates on loans



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

Euro area: Interest rates on deposits



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

Like in Germany, today's survey suggested an increase in the share of households considering it a suitable time to save. But the share of households considering it a suitable time to make major purchases maintained a downwards trend, with the respective survey index the second-lowest since the survey began in 1981, suggesting that French private consumption is likely to remain subdued over the near term.

The day ahead in the euro area

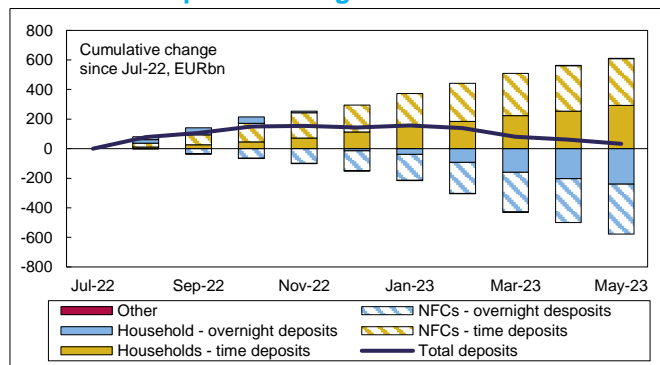
Focus on Thursday will remain firmly on inflation, with the flash estimates for June due from Germany, Spain, Belgium and Ireland. Reflecting base effects associated with last summer's discounted €9 monthly travel pass, German headline inflation is expected to have ticked higher (by about ½ppt) this month from May's fifteen-month low of 6.3%Y/Y. In contrast, headline HICP inflation in Spain is forecast to have fallen sharply, by almost 1½ ppts, to an eye-catching 1.5%Y/Y, which would be the lowest rate since March 2021 reflecting not least the faster pass-through of wholesale gas price developments in this country. The latest Commission economic surveys will also offer further insights into households' and firms' price expectations, and provide a further stock-take on economic growth momentum at the end of the second quarter. While last week's flash PMIs signalled a marked slowing in economic momentum, the Commission's flash consumer confidence index surprised on the upside, suggesting that the headline economic sentiment index might be broadly stable in June.

UK

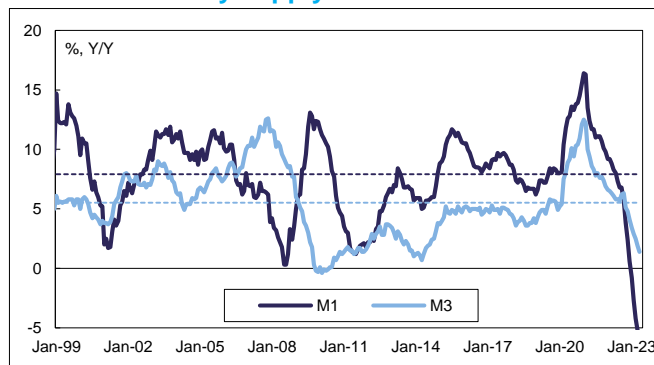
The day ahead in the UK

After a day bereft of top-tier UK economic data today, tomorrow will bring the BoE's bank lending figures for May. These might well show a (likely temporary) modest pickup in mortgage approvals last month. But households are expected to have made a third successive net repayment of mortgage debt for the first time since the series began in 1990. And like today's ECB numbers, these are likely to report the ongoing redistribution of households' deposits from overnight to higher-yielding time accounts.

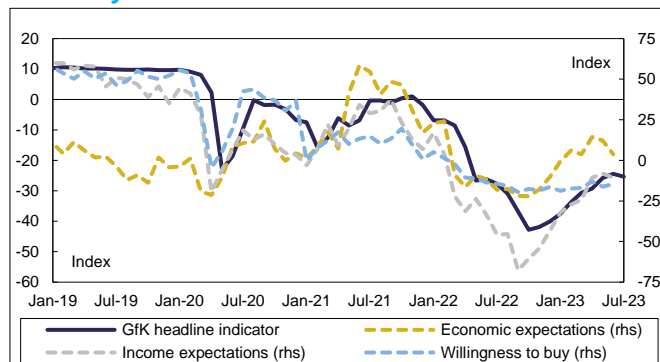
Euro area: Deposit holding of households & NFCs



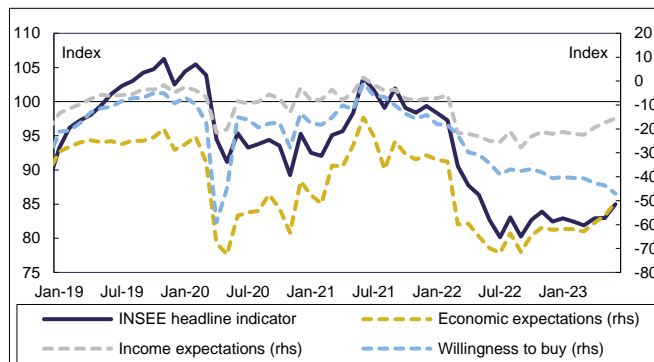
Euro area: Money supply*



Germany: GfK consumer confidence indices








France: INSEE consumer confidence indices




European calendar

Today's results

Economic data

Country	Release	Period	Actual	Market consensus/ <i>Daiwa forecast</i>	Previous	Revised
Euro area	 M3 money supply Y/Y%	May	1.4	1.5	1.9	-
Germany	 GfK consumer confidence	Jul	-25.4	-23.0	-24.2	-24.4
France	 INSEE consumer confidence	Jun	85	84	83	-
Italy	 Preliminary HICP (CPI) Y/Y%	Jun	6.7 (6.4)	6.8 (6.7)	8.0 (7.6)	-
Spain	 Retail sales Y/Y%	May	6.0	5.0	5.5	5.7








Auctions

Country	Auction
UK	 sold £2.75bn of 3.75% 2038 bonds at an average yield of 4.463%


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 EC Economic Sentiment Index	Jun	95.7	96.5
		10.00 EC industry (services) confidence	Jun	-5.6 (5.1)	-5.2 (7.0)
		10.00 EC final consumer confidence	Jun	-16.1	-17.4
Germany		13.00 Preliminary HICP (CPI) Y/Y%	Jun	6.8 (6.2)	6.3 (6.1)
Spain		08.00 Preliminary HICP (CPI) Y/Y%	Jun	1.5 (1.7)	2.9 (3.2)
UK		09.30 Consumer credit £bn (Y/Y%)	May	1.5 (-)	1.6 (7.7)
		09.30 Mortgage lending £bn (approvals, 000s)	May	-0.7 (49.5)	-1.4 (48.7)

Auctions and events

Euro area		09.00 ECB publishes Economic Bulletin
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Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

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<https://www.uk.daiwacm.com/ficc-research/recent-blogs>

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