

Euro wrap-up

Overview

- Shorter-dated Bunds made gains as German industrial production data fell short of expectations, with energy and construction output weaker and a lack of momentum in manufacturing.
- Gilts followed USTs higher on a day bereft of top-tier UK economic data.
- The coming week will bring the ECB account from June's monetary policy meeting, along with results for euro area IP and UK labour market and GDP.

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Daily bond market movements

Bond	Yield	Change
BKO 2.8 06/25	3.230	-0.040
OBL 2.4 10/28	2.725	-0.018
DBR 2.3 02/33	2.629	+0.007
UKT 0% 06/25	5.398	-0.105
UKT 1% 10/28	4.853	-0.057
UKT 3¼ 01/33	4.653	-0.007

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

Euro area

German industrial output eases in May with weakness in energy and construction

Given the sharp increase in German [manufacturing turnover](#) reported yesterday, today's industrial production figures disappointed, with output falling (an admittedly modest) 0.2%M/M in May to largely reverse the modest growth reported at the start of the second quarter. And so, having risen by a robust 2.1%3M/3M in March, output was up just 0.3%3M/3M in May and trending on average so far in Q2 a little more than ½% below that in Q1. Admittedly, much of the weakness in May came from a further marked decline in energy production, which fell a whopping 7.0%M/M, the second-steepest drop since the series began in 1991, to be down almost 19%Y/Y and trending more than 7½% below the Q1 average. Construction activity also fell back in May (-0.4%M/M), to be trending some 1.0% below the Q1 average. In contrast, manufacturing eked out a second-successive increase (0.2%M/M), although this left output trending broadly sideways so far in Q2 and more than 4% below the pre-pandemic benchmark, suggesting a clear lack of momentum in Germany's manufacturing sector.

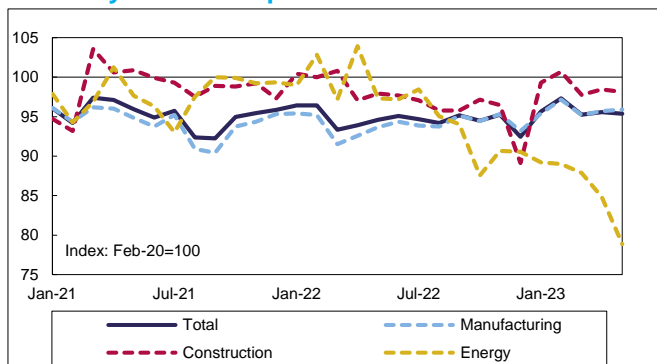
Autos production rises, but energy-intensive subsector continues to trend lower

The modest recovery in manufacturing was principally driven by the auto subsector, for which output rose 4.9%M/M to the joint-highest level since end-2020 and trending some 0.7% above the Q1 average, as supply bottlenecks continued to ease and manufacturers worked through pandemic-related backlogs. In contrast, production from the pharmaceutical sector fell sharply (-13.1%M/M) to its lowest level for more than two years, while production of machinery (-0.5%M/M) and computer, electronic & optical products (-0.1%M/M) edged lower, likely in part reflecting payback for strength at the start of the year. The structural adjustment in the energy-intensive sector, however, appears to be a lasting phenomenon. Indeed, firms continued efforts to cut reliance on energy despite the easing in wholesale gas prices, with industrial gas usage down about 10%Y/Y in May and around 20% lower than the average for that month in the four years before Russia's invasion of Ukraine. And so, production in energy-intensive subsectors fell a further 1.5%M/M in May to the second-lowest level since the global financial crisis, to be down around 12½%Y/Y and 3½% below the Q1 average. Within this category, production of glassware fell to its lowest level since March 2010, while chemicals production maintained a downwards trend to its second-lowest level since the start of 2009. And with manufacturers' gas usage still well below normal levels in June, output in these subsectors appears to have remained very subdued last month.

Manufacturing outlook remains clouded by subdued external demand

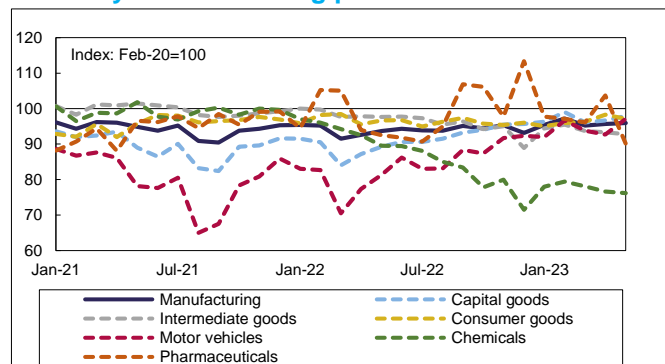
The latest autos production figures suggested ongoing recovery in June and a recent ifo institute survey suggest that firms in the sector enjoyed a marked improvement in business conditions that month. But truck-toll mileage edged lower again in

Germany: Industrial production



Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

Germany: Manufacturing production



Source: Refinitiv and Daiwa Capital Markets Europe Ltd.

June to maintain a broadly sideways trend in Q2, while [factory orders](#) continue to trend lower despite the pickup in May and inventories appear elevated. Moreover, surveys on the whole suggest that firms are increasingly gloomy about the outlook through the second half of the year amid concerns about [external demand](#). Indeed, according to a recent ifo institute survey, manufacturing firms' production expectations for the coming three months were the weakest since the onset of the pandemic. So, while services activity continues to trend higher – despite a modest drop in April, the level of sales in the sector was ¾% above the Q1 average – there is a non-negligible risk of a further contraction in German GDP in Q2.

The week ahead in the euro area

The coming week will bring a few euro area releases of note, including the publication on Thursday of the ECB account from the June monetary policy setting meeting. This meeting saw the Governing Council raise the deposit rate by 25bps to 3.50% to take the cumulative tightening since last July to 400bps. The statement signalled the likelihood of more tightening to come, while in her press conference, President Lagarde stated that the Governing Council still had “further ground to cover” and that a “material change” to the ECB’s baseline outlook would be required to prevent it hiking again in July. The minutes will be closely analysed for any insights into the path for policy beyond the July meeting.

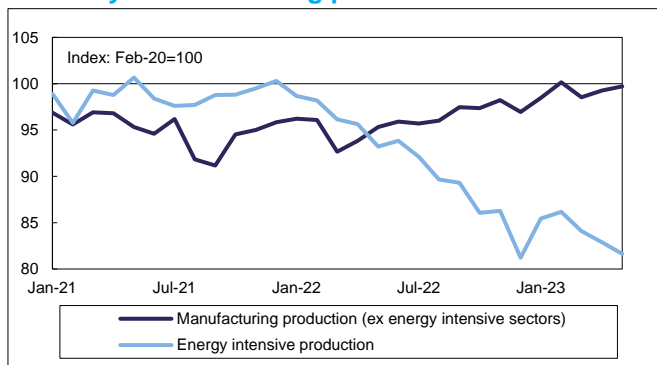
In terms of economic data, euro area industrial production figures for May will be published on Thursday. Based on figures published in Germany and [France](#), euro area output is expected to have recorded only modest growth in May despite an acceleration in autos production. But the often volatile Irish and Dutch production numbers will offer more insight on Monday. Like in [Germany](#), euro area goods trade figures for May (Friday) might well report a widening in the trade deficit amid subdued exports and firmer import values. The start of the week will also bring the euro area’s sentix investor survey findings for July, which will be followed by the German ZEW investor survey on Tuesday. In addition, final June inflation figures from Germany (Tuesday), Spain (Wednesday) and France (Thursday) are also due. The flash estimates saw HICP headline inflation rise in Germany (up 0.5ppt to 6.8%Y/Y) due to base effects associated with last year’s discounted travel pass, but fall sharply in Spain (down 1.3ppts to 1.6%Y/Y) and France (down 0.7ppt to 5.3%Y/Y).

UK

The week ahead in the UK

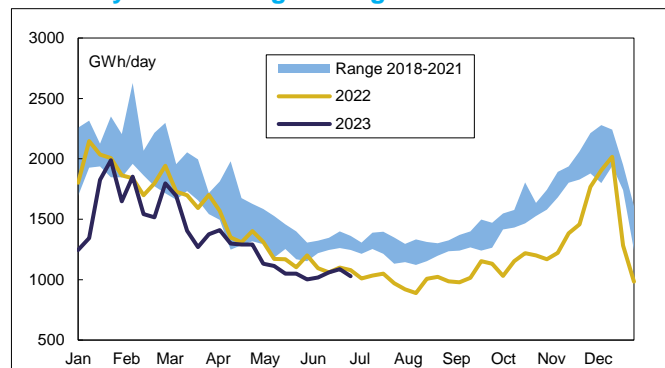
It will be a busy week ahead for top-tier UK releases, with the latest labour market figures on Tuesday of most interest for the BoE’s near-term monetary policy outlook. These are likely to report a marked slowdown in the pace of employment growth in

Germany: Manufacturing production



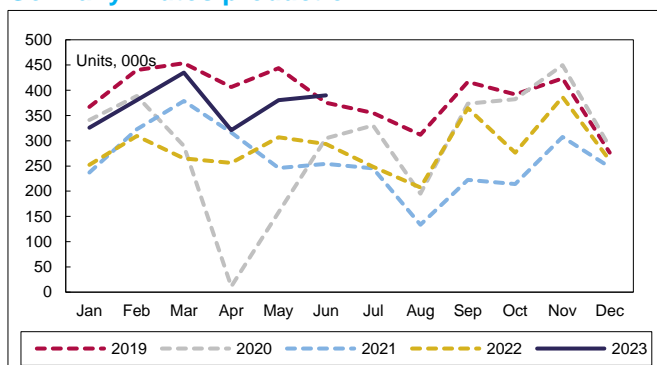
Source: Destatis, Refinitiv and Daiwa Capital Markets Europe Ltd.

Germany: Industrial gas usage



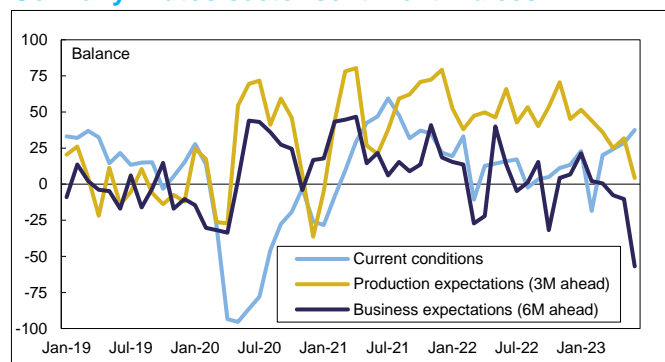
Source: Bundesnetzagentur and Daiwa Capital Markets Europe Ltd.

Germany: Autos production



Source: VDA, Bloomberg and Daiwa Capital Markets Europe Ltd.

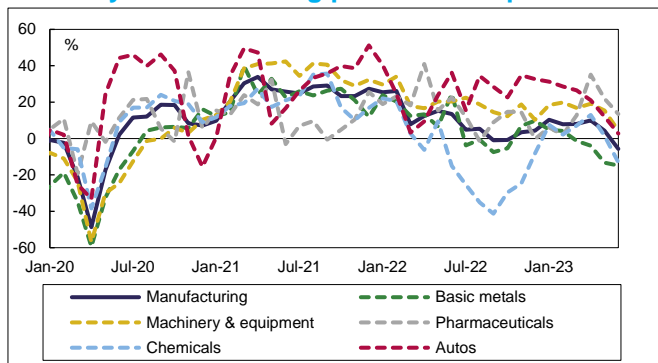
Germany: Autos sector sentiment indices



Source: ifo institute, Refinitiv and Daiwa Capital Markets Europe Ltd.

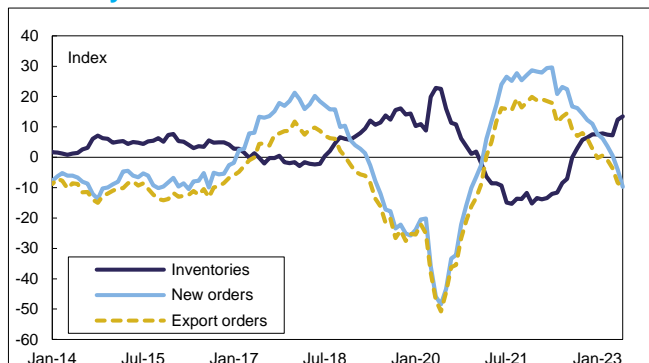
the three months to May, following the surge in April by 250k, which was the largest increase for twelve months. Nevertheless, the unemployment rate is expected to have moved sideways at 3.8%, suggesting a still very tight labour market. So, with single-month wages having jumped to a thirteen-month high in April (7.4%Y/Y), we continue to expect headline wage growth in the three months to May to remain little changed from April's outturn of 6.5%3M/Y. And, given the importance for the BoE, developments in private sector regular wage growth – which accelerated to 7.6%3M/Y in April – will be closely watched too. Meanwhile, May output results for GDP, services, manufacturing, construction and trade will follow on Thursday. Given the extra bank holiday for the King's coronation, we think that GDP contracted modestly that month, just as it fell in September due in part to the Queen's funeral, with industrial action also likely to have weighed slightly on activity. Thursday will also bring the BoE's latest consumer credit conditions survey, which seems bound to report a further significant decline in demand for loans and availability of credit in the three months to May amid tighter financial conditions and a more uncertain economic outlook. The impact of the BoE's aggressive monetary policy tightening and upwards shift in mortgage interest rates will likely be evident in the latest RICS residential survey that day too.

Germany: Manufacturing production expectations*



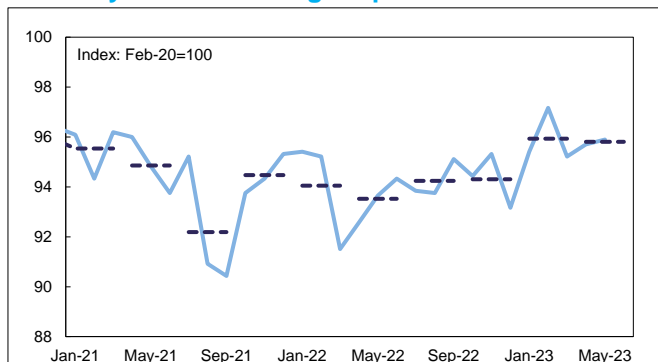
*Three months ahead. Source: ifo institute, Refinitiv and Daiwa Capital Markets Europe Ltd.

Germany: New orders and inventories



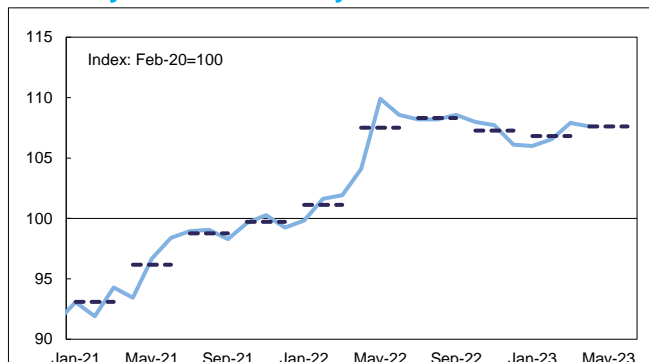
Source: EC, Refinitiv and Daiwa Capital Markets Europe Ltd.

Germany: Manufacturing output*



*Dashed dark blue lines represent quarterly averages. Source: Refinitiv and Daiwa Capital Markets Europe Ltd.










Germany: Services activity*



*Dashed dark blue lines represent quarterly averages. Source: Destatis and Daiwa Capital Markets Europe Ltd.




The next edition of the Euro wrap-up will be published on 11th July 2023

Daiwa economic forecasts

	2022 Q4	2023				2024 Q1	2023	2024	2025	
		Q1	Q2	Q3	Q4					
GDP		%, Q/Q					%, Y/Y			
Euro area 	-0.1	-0.1	0.1	0.2	0.1	0.1	0.4	0.7	1.1	
UK 	0.1	0.1	0.0	0.1	0.0	-0.2	0.3	-0.3	0.3	
Inflation, %, Y/Y										
Euro area										
Headline HICP 	10.0	8.0	6.2	4.3	2.6	2.6	5.2	2.3	1.7	
Core HICP 	5.1	5.5	5.5	5.0	4.2	3.5	5.0	2.6	1.8	
UK										
Headline CPI 	10.7	10.2	8.4	6.6	4.5	4.1	7.4	2.9	1.6	
Core CPI 	6.4	6.1	6.9	6.3	5.6	5.1	6.2	3.3	1.8	
Monetary policy, %										
ECB										
Refi Rate 	2.50	3.50	4.00	4.50	4.50	4.50	4.50	4.25	3.50	
Deposit Rate 	2.00	3.00	3.50	4.00	4.00	4.00	4.00	3.75	3.00	
BoE										
Bank Rate 	3.50	4.25	5.00	5.50	6.00	6.00	6.00	5.75	4.75	

Source: Bloomberg, ECB, BoE and Daiwa Capital Markets Europe Ltd.























European calendar

Today's results						
Economic data						
Country	Release	Period	Actual	Market consensus/ <i>Daiwa forecast</i>	Previous	Revised
Germany 	Industrial production M/M% (Y/Y%)	May	-0.2 (0.7)	0.0 (0.5)	0.3 (1.6)	-(1.7)
France 	Trade balance €bn	May	-8.4	-	-9.7	-10.6
Italy 	Retail sales M/M% (Y/Y%)	May	0.7 (3.0)	-	0.2 (3.2)	-
Auctions						
Country	Auction					
- Nothing to report -						

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

The coming week's data calendar

The coming week's key data releases

Country	BST	Release	Period	Market consensus/ <i>Daiwa</i> <i>forecast/actual</i>	Previous
Monday 10 July 2023					
Euro area 	09.30	Sentix investor confidence	Jul	-19.0	-17.0
Tuesday 11 July 2023					
Germany 	07.00	Final HICP (CPI) Y/Y%	Jun	<u>6.8 (6.4)</u>	6.3 (6.1)
	10.00	ZEW current assessment (expectations) balance	Jul	-63.8 (-10.0)	-56.5 (-8.5)
Italy 	09.00	Industrial production M/M% (Y/Y%)	May	0.5 (-4.5)	-1.9 (-7.2)
UK 	00.01	BRC retail sales monitor, like-for-like sales Y/Y%	Jun	-	3.7
	07.00	Payrolled employees, monthly change '000s	Jun	-	23
	07.00	Unemployment claimant count rate % (change '000s)	Jun	-	3.9 (-13.6)
	07.00	Average weekly earnings (excl. bonuses) 3M/Y%	May	6.8 (7.1)	6.5 (7.2)
	07.00	ILO unemployment rate 3M%	May	3.8	3.8
	07.00	Employment change 3M/3M '000s	May	89	250
Wednesday 12 July 2023					
Spain 	08.00	Final HICP (CPI) Y/Y%	Jun	<u>1.6 (1.9)</u>	2.9 (3.2)
Thursday 13 July 2023					
Euro area 	10.00	Industrial production M/M% (Y/Y%)	May	0.3 (-1.0)	1.0 (0.2)
France 	07.45	Final HICP (CPI)	Jun	<u>5.3 (4.5)</u>	6.0 (5.1)
UK 	00.01	RICS house price balance %	Jun	-34	-30
	07.00	GDP M/M% (3M/3M%)	May	-0.4 (-0.1)	0.2 (0.1)
	07.00	Industrial production M/M% (Y/Y%)	May	-0.4 (-2.3)	-0.3 (-1.9)
	07.00	Manufacturing production M/M% (Y/Y%)	May	-0.5 (-1.7)	-0.3 (-0.9)
	07.00	Index of services M/M% (3M/3M%)	May	-0.4 (-0.2)	0.3 (-0.1)
	07.00	Construction output M/M% (Y/Y%)	May	-0.3 (0.9)	-0.6 (3.6)
	07.00	Total trade balance (goods trade balance ex precious metals) £bn	May	-0.8 (-15.0)	-1.5 (-16.2)
Friday 14 July 2023					
Euro area 	10.00	Trade balance €bn	May	-	-7.1
Italy 	09.00	Trade balance €bn	May	-	0.3

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

The coming week's key events & auctions

Country	BST	Event / Auction
Monday 10 July 2023		
UK 	20.00	BoE Governor Bailey scheduled to speak
Tuesday 11 July 2023		
Germany 	10.30	Auction: €5.0bn of 2.4% 2028 bonds
Wednesday 12 July 2023		
Germany 	10.30	Auction: €5.0bn of 0% 2033 bonds
Euro area 	14.45	ECB Chief Economist Lane scheduled to participate in a panel discussion
UK 	07.00	BoE publishes its Financial Stability Report
	09.00	BoE Governor Bailey speaks at press conference on Financial Stability Report
	10.00	Auction: £3.5bn of 3.25% 2033 bonds
Thursday 13 July 2023		
Euro area 	12.30	ECB to publish account from 15 June Governing Council meeting
UK 	09.30	BoE publishes its Credit Conditions Survey
Friday 14 July 2023		
- Nothing scheduled -		

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

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