

# Euro wrap-up

## Overview

- Bunds followed the global trend slightly lower, even as a German investor survey pointed to a further deterioration in conditions at the start of Q3.
- Despite an unexpected pickup in the UK's unemployment rate, Gilts also made losses as wage growth accelerated to support the case for further significant BoE monetary policy tightening.
- After the BoE will publish its latest financial stability report tomorrow, Thursday will bring the latest UK GDP figures and BoE credit conditions survey. Euro area industrial production results are also due.

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### Daily bond market movements

Bond	Yield	Change
BKO 2.8 06/25	3.282	+0.010
OBL 2.4 10/28	2.750	+0.002
DBR 2.3 02/33	2.639	+0.006
UKT 0% 06/25	5.418	+0.055
UKT 1% 10/28	4.879	+0.039
UKT 3¼ 01/33	4.657	+0.019

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

Source: Bloomberg

## Euro area

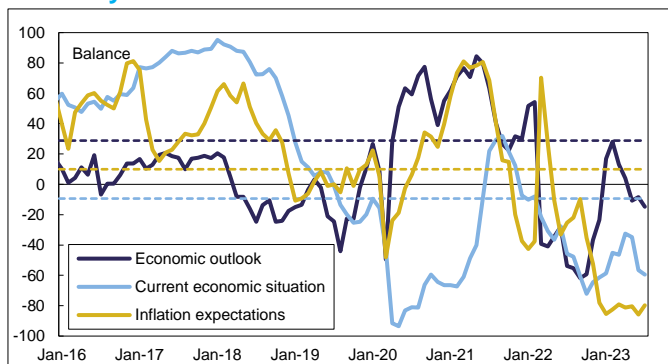
### German investor survey points to deteriorating conditions at the start of Q3

Today's German ZEW survey implied a further deterioration in investors' assessment of economic conditions at the start of the third quarter, suggesting that rising interest rates and weakening external demand continues to dampen Germany's recovery and raises risks of a prolonged (albeit relatively mild) recession in the largest member state. Indeed, the current conditions indicator fell for a third successive month in July, by 3pts to a seven-month low of -59.5, some 27pts below this year's peak in April and 50pts below the long-run average. There was also a decline in the survey's expectations balance this month, by 6.2pts to -14.7, similarly a seven-month low. While significantly higher than last year's trough (-61.9), this level is some 10pts below the Q2 average and 35pts below the long-run average, pointing to expectations of lacklustre recovery momentum through the second half of the year. And while earnings expectations for banks and insurance firms again improved in July and remained in positive territory, assessments of profitability in a range of other sub-sectors, including autos, steel, mechanical engineering and chemicals, were increasingly negative amid the weakening external outlook.

### German inflation ticked higher due to base effects associated with discounted travel pass

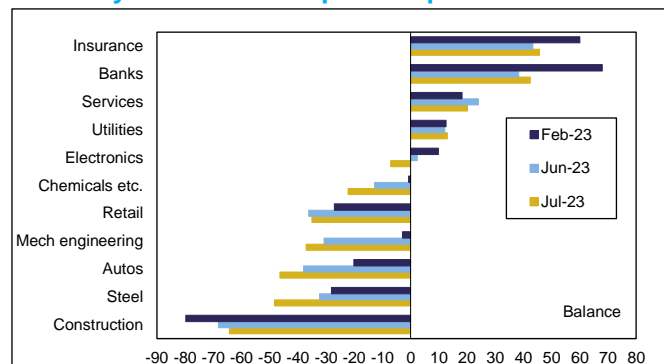
The ZEW survey also suggested a very modest pickup in inflation expectations in July to a four-month, albeit the respective index remained firmly in negative territory and well below the long-run average. This perhaps reflected the recent uptick in Germany's actual inflation, for which final figures published today confirmed an increase in the headline HICP rate in June, by 0.5ppt to 6.8%Y/Y. The national CPI rate was similarly up 0.4ppt to 6.4%Y/Y. The main cause was the base effect associated with last summer's highly-discounted rail fares, for which prices were up 65.2%Y/Y. Prices for combined travel tickets more than doubled compared with June 2022 to leave transport services costs up 25%Y/Y. So, while inflation in hospitality eased to a ten-month low and package holidays to a four-month low, services inflation rose 0.8ppt to a new high of 5.3%Y/Y. And while non-energy industrial goods inflation overall was softer despite a pickup in clothing, core inflation excluding food and energy rose 0.4ppt to 5.8%Y/Y. Among non-core items, energy inflation edged slightly higher than May (3.0%Y/Y), but was nevertheless 33.5ppts below September's peak and contributed just 0.2ppt to headline inflation. Within the detail, annual increases in electricity and natural gas maintained a steady downwards path in June reflecting base effects from the spike in wholesale gas prices after Russia's invasion of Ukraine last year and the German government's household energy bill support measures, while prices of heating oil and motor fuels fell sharply. Although food inflation remained a significant source of inflationary pressure, it also fell a further 1.2ppts to 13.7%Y/Y, the lowest in twelve months and some 8½ppts below March's peak.

### Germany: ZEW investor sentiment indices\*



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

### Germany: ZEW investor profit expectations



Source: Refinitiv and Daiwa Capital Markets Europe Ltd.

**The day ahead in the euro area**

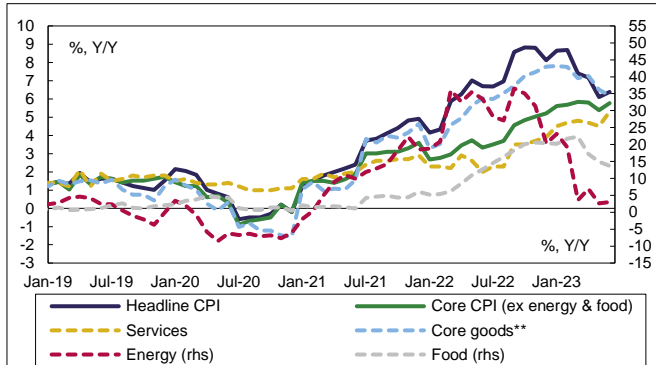
After a quiet day for euro area releases tomorrow, Thursday will bring the publication of the ECB account from the 15 June Governing Council policy-setting meeting. This meeting saw the Governing Council raise the deposit rate by 25bps to 3.50% and also signal the likelihood of more tightening to come, with President Lagarde stating that a “material change” to the ECB’s baseline outlook would be required to prevent it hiking again in July. So with a rate hike this month seems a done deal, the minutes will be closely analysed for any insights into the path for monetary policy beyond the July meeting. In terms of economic data, Thursday will bring the release of euro area industrial production results for May. Production figures published by member states so far have been mixed, with a sizeable decline in Ireland (-4.9%M/M) and modest drop in Germany (-0.2%M/M), contrasting with positive growth in France (+1.2%M/M), Italy (+1.6%M/M), Spain (+0.7%M/M) and the Netherlands (+1.2%M/M). Overall, we expect aggregate euro area production to have moved broadly sideways in May despite support from the autos sector. Thursday will also bring final estimates of French inflation for June.

**UK**

**Employment growth slows and inactivity falls to suggest easing demand-supply imbalance**

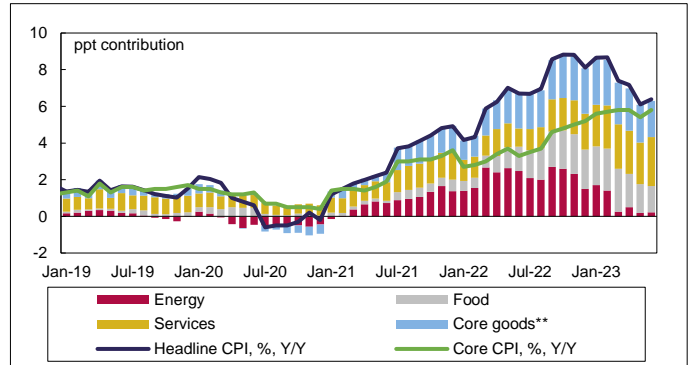
When it raised Bank Rate by a larger 50bps to 5.00% at its June policy meeting, the BoE’s MPC made clear that future decisions would continue to depend on indications of inflation persistence, including the tightness of the labour market and the behaviour of wage growth. But while today’s data suggested some signs of easing in the imbalance between labour demand and supply, wage growth accelerated again to support the case for more significant monetary policy tightening ahead. As was expected, jobs growth in the three months to May moderated from the twelve-month high of 250k in April, although the increase of 102k was broadly in line with the average during the post-lockdown recovery. Growth in the three months to May was largely underpinned by part-time employees (109k), which rose to the highest level since March 2020, while full-time employees fell for the fifth month out of the past six (-15k), albeit to be still some 759k above the pre-pandemic level. So, the employment rate rose 0.2ppt from the prior quarter to 76.0%. Encouragingly, the inactivity rate fell 0.4ppt over the quarter to 20.8%, the lowest since May 2020, with a very modest decline in the number of people inactive due to long-term sickness. So, the unemployment rate unexpectedly edged up 0.2ppt over the quarter to a 16-month high of 4.0%, admittedly exactly in line with the pre-pandemic rate and still historically low. The (more volatile) single-month unemployment figure jumped 0.7ppt to 4.3%, a 21-month high. The initial estimate of payrolls also reported the first monthly decline in June since February 2021, while the number of vacancies fell again in the three months to June for the twelfth consecutive month to the lowest level since July 2021 signalling a possible easing in labour market tightness ahead.

**Germany: Consumer price inflation\***



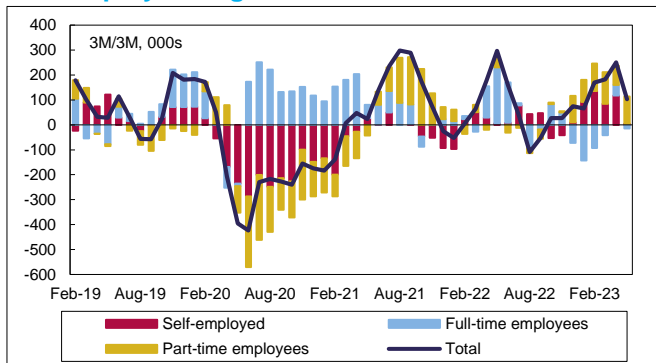
\*National measure. \*\*Non-energy industrial goods. Source: Refinitiv and Daiwa Capital Markets Europe Ltd.

**Germany: Contributions to consumer price inflation\***



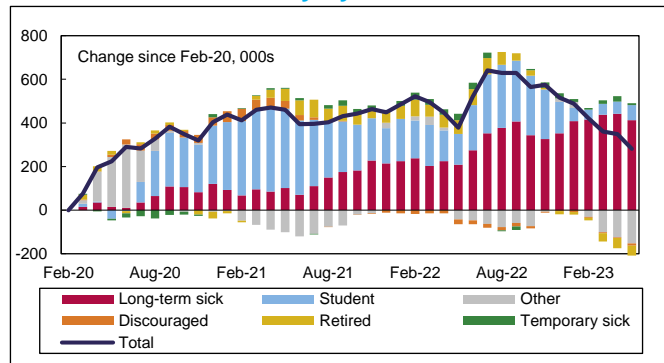
\*National measure. \*\*Non-energy industrial goods. Source: Refinitiv and Daiwa Capital Markets Europe Ltd.

**UK: Employment growth**



Source: Refinitiv and Daiwa Capital Markets Europe Ltd.

**UK: Economic inactivity by reason**



Source: Refinitiv and Daiwa Capital Markets Europe Ltd.

## Wage growth continues to accelerate

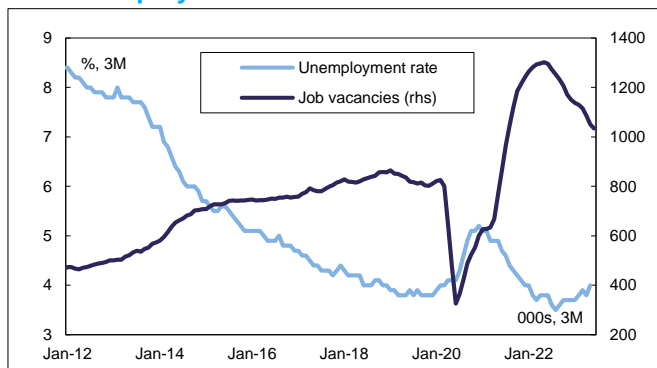
Nevertheless, more importantly for the BoE, today's data suggested a further acceleration in wages, with growth in total pay in the three months to May up 1.1ppt on the quarter to 6.9%3M/Y, a rate only exceeded in the midst of the pandemic. When excluding bonuses, regular pay rose 0.7ppt over the quarter to 7.3%3M/Y, the joint-highest with April 2022 and June 2021. The MPC will also be concerned to see that momentum in private sector regular pay rose, with growth of 7.7%3M/Y. This also represents a series high when excluding pandemic-related distortions, with the three-month annualised rate up 0.9ppt on the month to 9.4%, the highest since December 2020. While this continues in part to reflect the increase in the National Living Wage from 1 April, manufacturing saw the strongest growth in regular earnings (7.8%3M/Y) since the series began in 2001, with services regular pay growth (7.3%3M/Y) only marginally below April's record high too. So while there were some signs that recent earnings momentum in the public sector was starting to wane, today's data show that wage growth remains well above levels (3-3½%) considered to be consistent with achievement of the 2% inflation target over the medium term. As such, today's figures arguably leave the door open to another 50bps hike at the MPC's August meeting, particularly if next week's CPI release reveals another upwards shift in core inflation.

## The day ahead in the UK

Tomorrow will see the BoE publish its semi-annual Financial Stability Report, for which commentary on recent lending volumes, both secured and unsecured, as well as saving rates and deposits will be watched in light of the significant tightening in financial conditions. This will be followed on Thursday by the release of monthly GDP figures for May, including the breakdown of services, industry and construction activity as well as trade numbers. 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. As such, we expect GDP on a three-month basis to turn slightly negative (-0.1%3M/3M) for the first time since November. 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 increased economic uncertainties. The impact of the BoE's aggressive monetary policy tightening and upwards shift in mortgage interest rates will also likely be evident in the latest RICS residential survey.

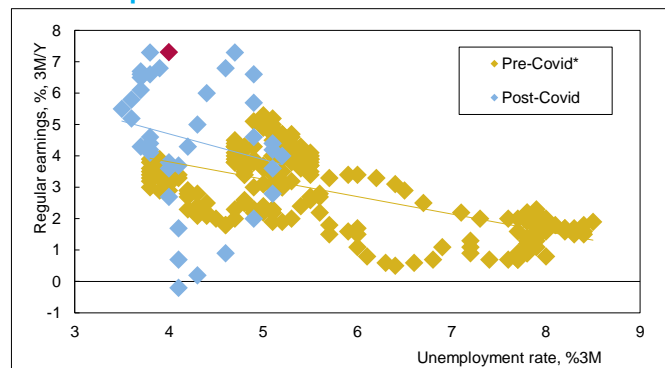
*The next edition of the Euro wrap-up will be published on 13 July 2023*

### UK: Unemployment rate and vacancies



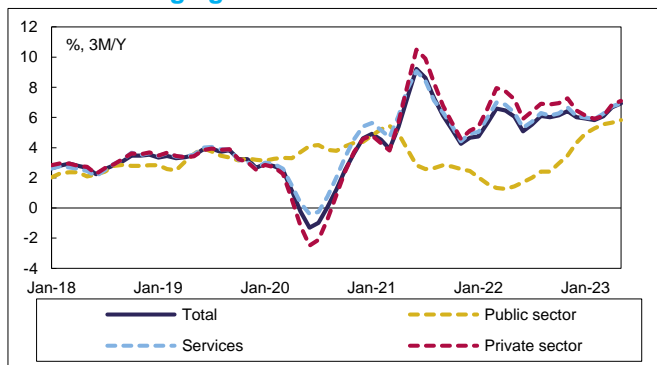
Source: Refinitiv and Daiwa Capital Markets Europe Ltd.

### UK: Phillips curve



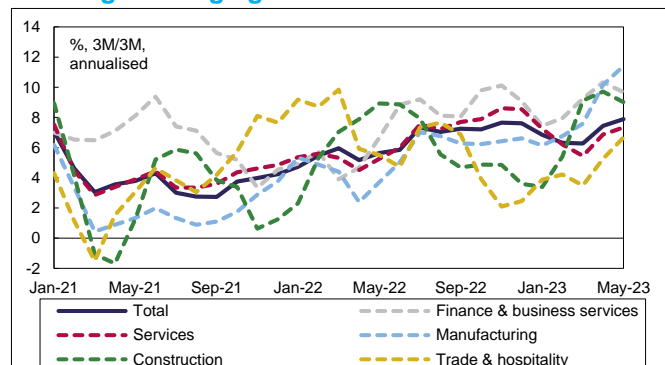
\*Jan-2001 to Feb-2022. Red diamond represents latest observation.  
Source: Refinitiv and Daiwa Capital Markets Europe Ltd.

### UK: Total wage growth



Source: Refinitiv and Daiwa Capital Markets Europe Ltd.

### UK: Regular wage growth












Source: Refinitiv 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	 Final HICP (CPI) Y/Y%	Jun	<b>6.8 (6.4)</b>	<u>6.8 (6.4)</u>	6.3 (6.1)	-
	 ZEW current assessment (expectations) balance	Jul	<b>-59.5 (-14.7)</b>	-63.8 (-10.0)	-56.5 (-8.5)	-
Italy	 Industrial production M/M% (Y/Y%)	May	<b>1.6 (-3.7)</b>	0.5 (-4.5)	-1.9 (-7.2)	<b>-2.0 (-7.4)</b>
UK	 BRC retail sales monitor, like-for-like sales Y/Y%	Jun	<b>4.2</b>	-	3.7	
	 Payrolled employees, monthly change '000s	Jun	<b>-9</b>	-	23	<b>20</b>
	 Unemployment claimant count rate % (change '000s)	Jun	<b>4.0 (25.7)</b>	-	3.9 (-13.6)	<b>- (-22.5)</b>
	 Average weekly earnings (excl. bonuses) 3M/Y%	May	<b>6.9 (7.3)</b>	6.8 (7.1)	6.5 (7.2)	<b>6.7 (7.3)</b>
	 ILO unemployment rate 3M%	May	<b>4.0</b>	3.8	3.8	-
	 Employment change 3M/3M '000s	May	<b>102</b>	89	250	-

#### Auctions


Country Auction

Germany  sold €3.8bn of 2.4% 2028 bonds at an average yield of 2.71%

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

### Yesterday's results

#### Economic data

Country	Release	Period	Actual	Market consensus/ <i>Daiwa forecast</i>	Previous	Revised
Euro area	 Sentix investor confidence	Jul	<b>-22.5</b>	-19.0	-17.0	-

#### Auctions


Country Auction

- Nothing to report -






Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

### Wednesday's releases

#### Economic data

Country	BST	Release	Period	Market consensus/ <i>Daiwa forecast</i>	Previous
Spain	 08.00	Final HICP (CPI) Y/Y%	Jun	<u>1.6 (1.9)</u>	2.9 (3.2)










#### Auctions and events

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

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

## Thursday's releases

## Economic data

Country	BST	Release	Period	Market consensus/ <i>Daiwa forecast</i>	Previous
Euro area 	10.00	Industrial production M/M% (Y/Y%)	May	<u>0.1 (-1.1)</u>	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	-35	-30
	07.00	GDP M/M% (3M/3M%)	May	-0.3 (-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)

## Auctions and events

Euro area 	12.30	ECB to publish account from 15 June Governing Council meeting			
Italy 	10.00	Auction: €4.5bn of 3.85% 2026 bonds			
	10.00	Auction: €3.0bn of 3.7% 2030 bonds			
	10.00	Auction: €1.25bn of 3.25% 2026 bonds			
	10.00	Auction: €1.25bn of 3.85% 2049 bonds			
UK 	09.30	BoE publishes its Credit Conditions Survey			

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