

# Euro wrap-up

## Overview

- After the Bundesbank late on Friday cut its remuneration of domestic government deposits back to 0%, and as German industrial production fell more abruptly than expected in June, Bunds made gains at the short end of the curve but followed USTs lower at the longer end.
- Gilts followed USTs lower across the curve on a quiet day for UK macroeconomic data.
- Tuesday will bring the ECB's latest Consumer Expectations Survey results, final German inflation data for July and a UK retail sales survey for the same month.

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### Daily bond market movements

Bond	Yield	Change
BKO 3.1 09/25	2.949	-0.053
OBL 2.4 10/28	2.572	-0.004
DBR 2.6 08/33	2.583	+0.027
UKT 0% 06/25	4.890	+0.042
UKT 1% 10/28	4.427	+0.045
UKT 3% 01/33	4.441	+0.069

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

Source: Bloomberg

## Euro area

### German IP drops more than expected in June to seven-month low

German industrial production in June was weaker than expected, dropping 1.5%M/M, materially worse than the median forecast on the Bloomberg survey (-0.5%M/M) albeit consistent with the fall in manufacturing [turnover](#) (1.6%M/M) reported on Friday. That left industrial production at a seven-month low in June, down 1.8%Y/Y, 6.8% below the pre-pandemic level and more than 10% below the pre-pandemic peak. And over the second quarter as a whole, IP dropped 1.3%Q/Q to raise the risks of a downward revision to GDP, which is currently estimated to have been unchanged from Q1. Within the detail, manufacturing output fell 1.3%M/M in June to be down a more moderate 0.6%Q/Q in Q2. Production in June was weighed not least by autos, which dropped 3.5%M/M. But that followed growth in the subsector of 5.8%M/M the prior month, and so autos output still grew for a fifth successive quarter and by 1.0%Q/Q in Q2. But with production of machinery and equipment down, capital goods output fell 3.9%M/M in June to be down 0.4%Q/Q, suggestive of a weakening in investment intentions in the face of rising interest rates. In contrast, with output of pharmaceuticals (up 7.9%M/M in June) providing some offset, consumer goods production rose 1.8%M/M in June and 1.2%Q/Q in Q2 to mark the first growth in that subsector in five quarters.

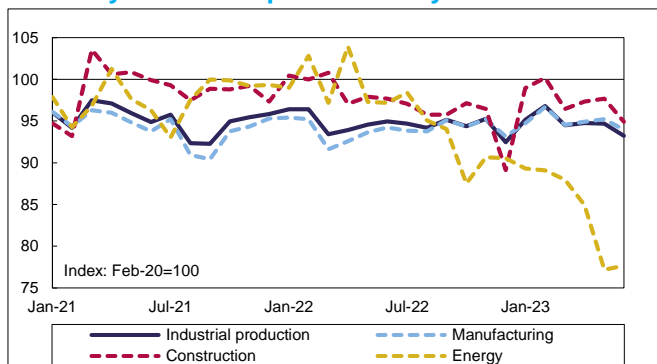
### Adjustments to gas price shock ongoing despite uptick in chemicals production

Over the past year, the intermediate goods subsector has been the weakest major category of manufacturing output, as firms cut back production of energy-intensive items in the face of the extreme shock to natural gas prices and concerns about the reliability of energy supply. With natural gas prices down significantly from their peak, albeit still above pre-pandemic levels, there was a hint that the adjustment in that subsector might be relatively well advanced. Indeed, production of chemicals and related products rose in June for the first month in three and by 3.5%M/M. But that still left it more than 20% below its pre-pandemic level and also down 1.7%Q/Q in Q2. Moreover, industry gas usage has continued largely to trend below its level at the same time last year, and firmly below the range before Russia's invasion of Ukraine. And with output of basic metals, glassware, coke and petroleum, among others, still falling in June, overall production of energy-intensive items was still more than 17% below the pre-pandemic level and down 3.5%Q/Q in Q2.

### Nuclear power plant closures & hit to rate-sensitive construction also weighed on IP in Q2

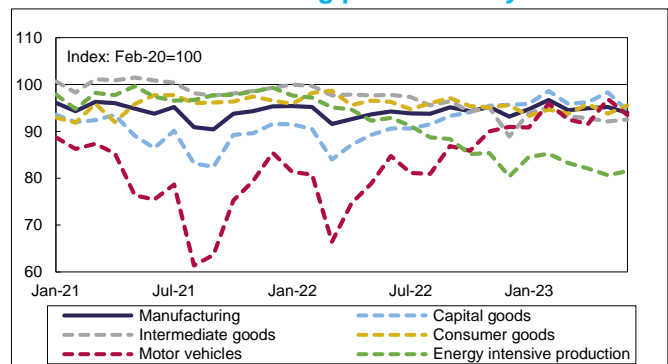
The weakest category of industrial production in the second quarter lay beyond the manufacturing sector, albeit also relating to Germany's energy crisis. The cause was the government's decision to close its remaining three functioning nuclear power

#### Germany: Industrial production by sector



Source: Refinitiv Datastream and Daiwa Capital Markets Europe Ltd.

#### Euro area: Manufacturing production by sub-sector



Source: Refinitiv Datastream and Daiwa Capital Markets Europe Ltd.

plants in mid-April. So, while energy output ticked up 0.6%M/M in June, it was still down more than 20%Y/Y that month, and fell a whopping 10.0%Q/Q in Q2. Finally, like capital goods producers, the construction sector appears very sensitive to higher interest rates. Indeed, construction output fell a steep 2.8%M/M and also 2.8%Y/Y in June, to be down 1.9%Q/Q in Q2. The low levels in June of production in manufacturing, energy and construction raise risks of a further contraction in IP in Q3, which also risks causing a renewed contraction in GDP this quarter. Despite the surprisingly strong growth in new orders in June, which appears to relate to one-off factors, such a contraction in IP would be fully consistent with the July survey indicators. Indeed, the manufacturing new orders PMI fell last month to a highly contractionary 32.7, the lowest since the global financial crisis in March 2019. And the production expectations index on the Commission survey dropped to the lowest level since the euro crisis when excluding the initial pandemic lockdown period in early 2020, with energy-intensive subsectors among others signalling the likelihood of further retrenchment given the weakness of demand.

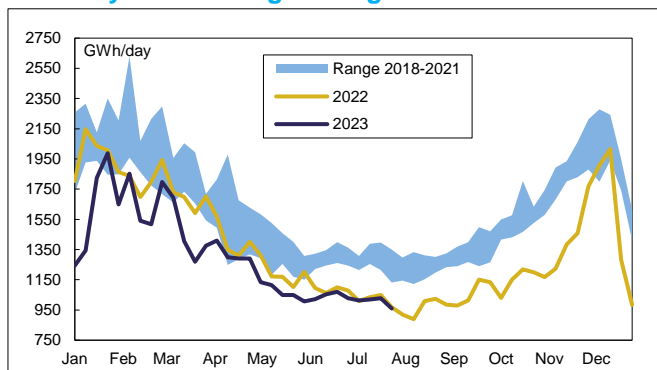
## Sentix indices show modest pickup in euro area investor expectations but Germany lags behind

There was some slightly better news from today's Sentix investor sentiment indices, which represented the first of the August survey results. In particular, having dropped to a seven-month low in July, and contrary to expectations of a further decline this month, the euro area investor confidence index rose 2.6pts in August to -18.9, admittedly still the second-weakest reading this year. The rise in the headline indicator reflected the reduction in pessimism about the outlook for the coming six months, with the respective index up more than 7pts to a four-month high of -17.3. The improvement was thanks not least to a moderation in inflation expectations and associated perceptions of diminished pressure on the ECB to keep raising rates. Current conditions in the euro area were nevertheless also judged still to be weak, unchanged at July's nine-month low of -20.5. Moreover, the aggregate euro area level indices were weighed by ongoing deterioration in Germany, which Sentix judged cemented its role as the sick man of the euro area. Indeed, the German current conditions index fell to a ten-month low of -30.7. And while it edged up for the first month in six, the German expectations index (-26.0) was more than 50% weaker than that of the euro area as a whole and consistent with expectations of recession in the euro area's largest member state.

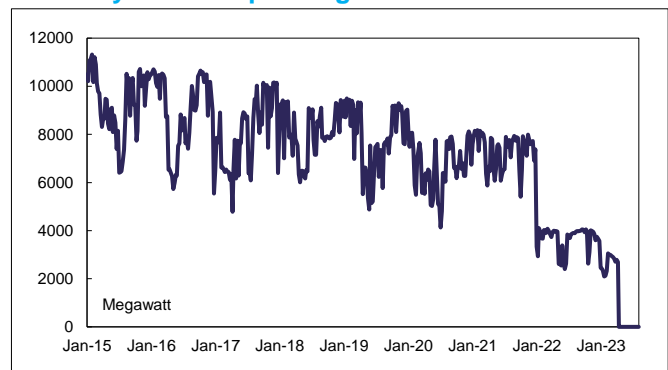
## The day ahead in the euro area

Focus tomorrow will be on the ECB's consumer expectations survey for June, which will provide an update on households' expectations for inflation, income, economic activity and house prices. In May, the median expectation for inflation three years ahead remained stable at 2.5%Y/Y, while the mean expectation edged slightly higher to 4.0%Y/Y. Final German inflation data, meanwhile, are expected to align with the flash data and confirm that inflation eased back in July, with the EU-

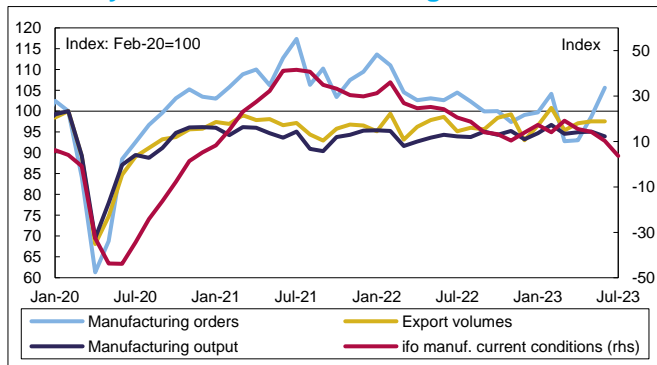
### Germany: Industrial gas usage



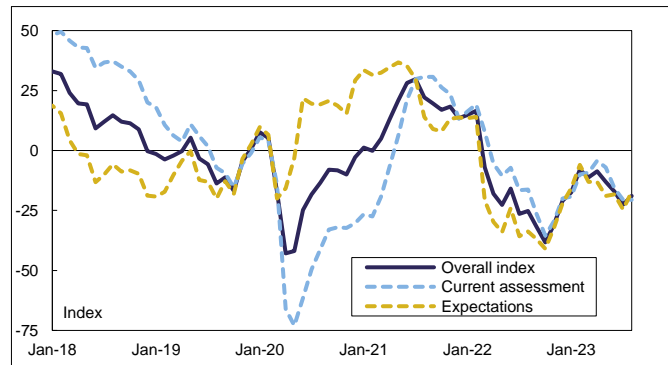
### Germany: Nuclear power generation



### Germany: Selected manufacturing sector indicators



### Euro area: Sentix investor sentiment





harmonised headline rate down a slightly firmer-than-expected 0.3%ppt to 6.5%Y/Y and the national rate down 0.2% to 6.2%Y/Y. We will also get French trade figures for June.

## UK







### The day ahead in the UK

Following a quiet start to the week in the UK, with no economic data to report today, tomorrow's BRC retail sales monitor will provide an update on retail spending in July. Like the [CBI distributive trades survey](#), this is likely to show a notable weakening in sales growth at the start of the third quarter, not least reflecting lower footfall on the High Street due to unusually heavy rainfall that month.

## European calendar

Today's results						
Economic data						
Country	Release	Period	Actual	Market consensus/ <i>Daiwa forecast</i>	Previous	Revised
Euro area	 Sentix investor confidence	Aug	<b>-18.9</b>	-25.0	-22.5	-
Germany	 Industrial production M/M% (Y/Y%)	Jun	<b>-1.5 (-1.7)</b>	-0.5 (-0.2)	-0.2 (0.7)	-0.1 (0.0)
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	
Germany	 07.00	Final HICP (CPI) Y/Y%	Jul	<u>6.5 (6.2)</u>	6.8 (6.4)	
France	 07.45	Trade balance €bn	Jun	-	-8.4	
UK	 00.01	BRC retail monitor, like-for-like sales Y/Y%	Jul	-	4.2	
Auctions and events						
Euro area	 09.00	ECB publishes monthly consumer expectations survey				
Germany	 10.30	Auction: €4.0bn of 2.4% 2028 bonds				
UK	 10.00	Auction: £900mn of 0.125% 2039 index-linked bonds				

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

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