

Euro wrap-up

Overview

- Bunds followed US10s lower even as the flash inflation estimates from various member states eased in June, and German data pointed to loosening labour market conditions.
- Gilts made losses across most of the curve following an upwards revision to UK GDP growth in Q1.
- The coming week will bring flash euro area inflation, unemployment and German IP figures, while general elections will be held in France and the UK.

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Daily bond market movements

Bond	Yield	Change
BKO 2.9 06/26	2.824	+0.022
OBL 2.1 04/29	2.476	+0.036
DBR 2.2 02/34	2.494	+0.049
UKT 0½ 01/26	4.172	-0.035
UKT 0½ 01/29	4.015	+0.008
UKT 4½ 01/34	4.171	+0.042

*Change from close as at 5.00pm BST.
Source: Bloomberg

Euro area

French inflation eases in June, but core inflation moves sideways

Ahead of the flash euro area June inflation estimates in the coming week, figures published today by France, Italy, Spain and Portugal support our view that the uptick in May will prove temporary. In line with expectations, the EU-harmonised measure of French inflation moderated 0.1ppt in June to 2.5%Y/Y, failing to fully reverse the rise in May but nevertheless still one of the softest rates for almost three years. The magnitude of decline in the national CPI rate was slightly larger, taking it down to 2.1%Y/Y, the lowest since August 2021. The limited detail published with today's release suggested the moderation was led by non-core items, with food inflation down to a 2½-year low (0.8%Y/Y) and energy inflation (-0.9ppt to 4.8%Y/Y) partially reversed the increase in May thanks to lower petrol prices. Today's release also confirmed another month of zero core goods inflation. So, as the services CPI rate also moved sideways, at 2.8%Y/Y, core inflation was also steady this month. And with certain services components – including package holidays, recreation and hospitality – likely to be boosted over the summer as Paris hosts the Olympics, French services and therefore core inflation is likely to remain sticky over coming months.

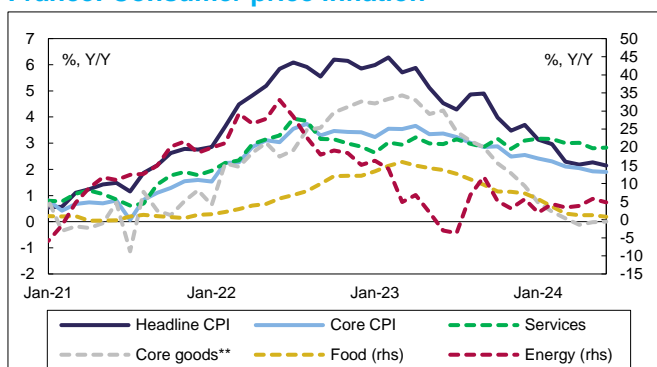
Italian inflation remains extremely subdued, with core inflation down to a more than 2-year low

While Italian HICP inflation edged slightly higher this month, by 0.1ppt to 0.9%Y/Y, this remains one of the lowest rates of the euro area member states. The pickup in June reflected a smaller drag from energy (up 3.1ppts to -8.6%Y/Y). In contrast, but similar to France, food inflation (1.8%Y/Y) maintained a steady downtrend to a 2½-year low, while non-energy industrial goods inflation eased to just 0.5%Y/Y, the softest since the start of 2022. And with the services component also edging lower (3.1%Y/Y) – reflecting moderating hospitality and recreation costs – core HICP inflation fell for the first month in three, by 0.1ppt to 2.1%Y/Y, the lowest for more than two years and 3.4ppts below the peak 16 months ago. Headline HICP inflation also fell back in Spain (3.5%Y/Y) and Portugal (3.1%Y/Y), more than offsetting the acceleration in Belgium (5.5%Y/Y). While the Spanish statistical office suggested that core inflation (excluding fresh foods and energy) merely moved sideways, the equivalent Portuguese rate fell 0.4ppt as hotel prices fell back following a spike seemingly associated with Taylor Swift's event in Lisbon in May. So, while much will depend on the outcome from Germany on Monday, we maintain our view that euro area inflation will at least partially reverse the increase in May, with our expectation for the headline HICP rate to decline 0.2ppt back to 2.4%Y/Y and core inflation (excluding all food and energy) to drop 0.1ppt to 2.8%Y/Y.

ECB survey suggests households more optimistic about the inflation outlook

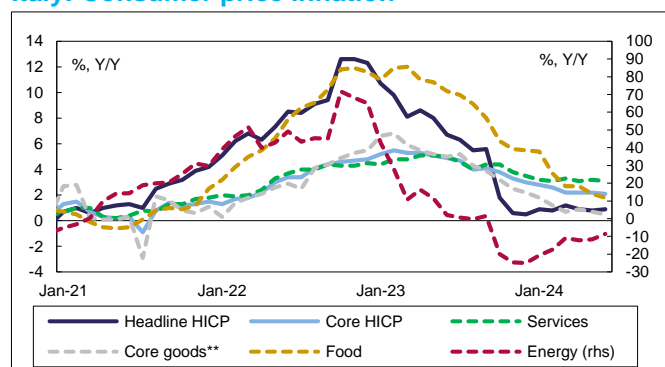
While yesterday's Commission survey measure of consumer price expectations edged up to a four-month high in June, according to the results of the ECB's latest consumer survey, households appear to have largely looked through the uptick in

France: Consumer price inflation*



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

Italy: Consumer price inflation*



*EU harmonised measure. **Non-energy industrial goods. Source: Macrobond and Daiwa Capital Markets Europe Ltd.

actual inflation that month and maintained the view that a gradual disinflationary path will remain in place over the horizon. Indeed, the median forecast for headline inflation twelve months ahead fell for a fourth consecutive month in May, by 0.1ppt to 2.8%Y/Y, the lowest since September 2021. Moreover, household expectations for inflation in three years' time – which arguably matter more for monetary policy decisions – also moderated, with the median forecast for the euro area down 0.1ppt to 2.3%Y/Y, the softest since February 2022 and 0.7ppt below the peak in late 2022. It also fell in France to be bang in line with the ECB's 2% target, moved sideways in Germany (2.1%) and fell to a nine-month low in Spain (2.3%).

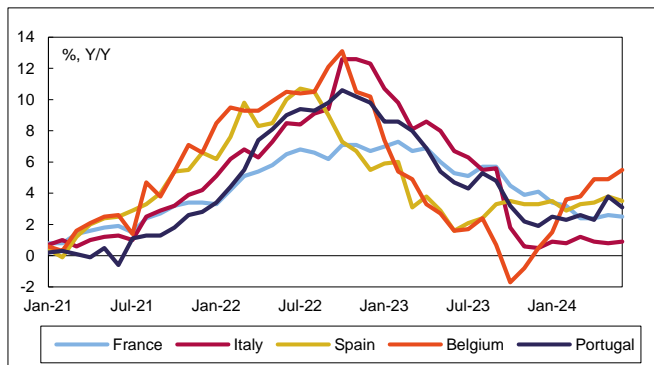
Rising German unemployment claims coincides with a decline in negotiated pay growth

While some Governing Council members continue to flag ongoing tightness in the labour market as an upside risk to the inflation outlook, there are growing signs that conditions are loosening. Today's German jobless claims figures recorded the 18th consecutive monthly increase in June, by 19k to 2.78mn, the highest number of claimants since February 2021. So, having moved sideways for five consecutive months to May, the claimant count rate rose 0.1ppt to a more-than two-year high of 6.0%. The downtrend in the number of job vacancies also accelerated this month, with the drop of 11k the steepest since May 2023 taking it to the lowest for three years. Surveys also suggest that German firms' hiring intentions have deteriorated, with the ifo employment indicators implying a cut in headcount in the manufacturing, construction and retail subsectors. And yesterday's Commission employment intention indices fell back in each of the larger member states, taking the euro area index down to its weakest since March 2021. So, with demand and supply becoming more balanced, pay pressures appear to be gradually diminishing. According to the Indeed tracker, wage growth in the euro area slowed in May (3.35%Y/Y) to the softest in over two years. And looking through monthly volatility, today's German negotiated wage growth estimate published by Destatis saw quarterly growth slow 1.3ppts to 4.3%Y/Y.

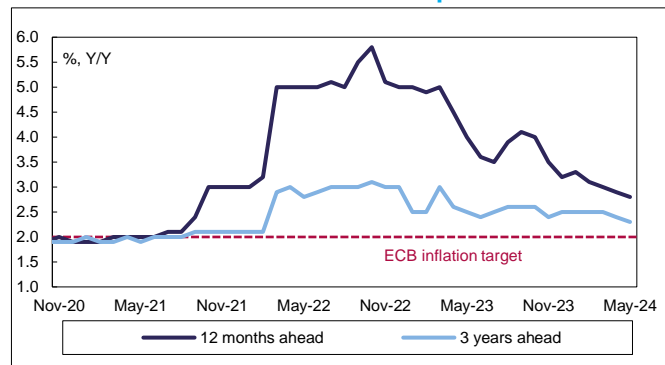
The coming week in the euro area

As markets digest the results of Sunday's first round of voting in the [French general elections](#), it will be a busy week ahead for top-tier economic data, including most notably the flash June inflation estimates from the euro area on Tuesday. In May, the headline HICP rate rose 0.2ppt to a three-month high of 2.6%Y/Y, driven principally by a jump in services inflation due to a significant base effect associated with the introduction a year ago of the German discounted public transport ticket. Other temporary factors – such as package holidays and accommodation costs in Germany as the Euro football championship kicked off – will likely keep services inflation elevated this month. But with core goods, food and energy inflation expected to moderate slightly further, we forecast headline HICP inflation to fully reverse the rise in May to 2.4%Y/Y – the joint-lowest since July 2021 – while core inflation is expected to decline 0.1ppt to 2.8%Y/Y, to be still 0.1ppt above April's rate. Equivalent

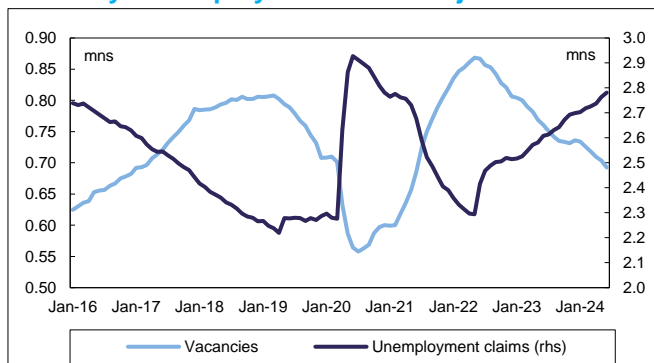
Euro area member states: Headline HICP inflation



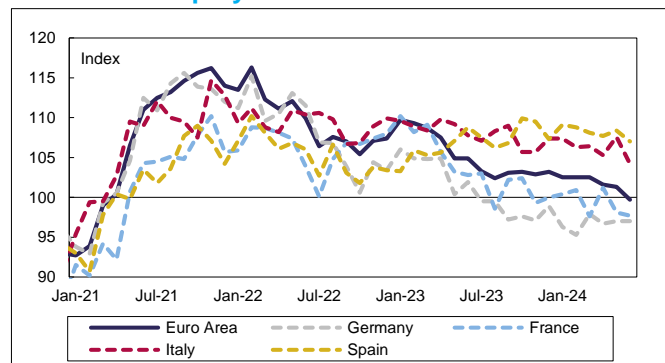
Euro area: Household inflation expectations



Germany: Unemployment claims & job vacancies



Euro area: Employment intentions indices



German figures on Monday will provide a further guide, while euro area producer price inflation data for May (Wednesday) will offer insights into the outlook for goods price pressures.

Among the euro area's other releases, unemployment figures (Tuesday) will provide an update on labour market conditions at the start of Q2, with the jobless rate expected to tick slightly higher in May, by 0.1ppt to 6.5%. In terms of activity figures, euro area retail sales in May (Friday) are expected to report a modest increase following the drop in April (-0.5%M/M). Indeed, French figures published today showed that consumer spending on goods jumped in May by 1.5%M/M – the most since January 2023 – led by a rebound in sales of food and energy. Furthermore, revised German figures suggest that the decline in sales in that country in April was significantly smaller than initially estimated (from -2.0%M/M to -0.2%M/M), suggesting a likely upwards revision to euro area retail sales at the start of Q2. The back end of the week will also focus on the manufacturing sector, with the release of German factory orders and industrial production data for May (Thursday and Friday respectively). Having declined for a fourth successive month in April, we expect factory orders to rise in May. Indicators provide mixed messages about production in May, with truck toll mileage having declined on the month but surveys signalling a notable pickup. Expectations are for a modest increase following the modest drop in April (-0.1%M/M). The final manufacturing (Monday), services (Wednesday) and construction PMI surveys (Thursday) for June are also due.

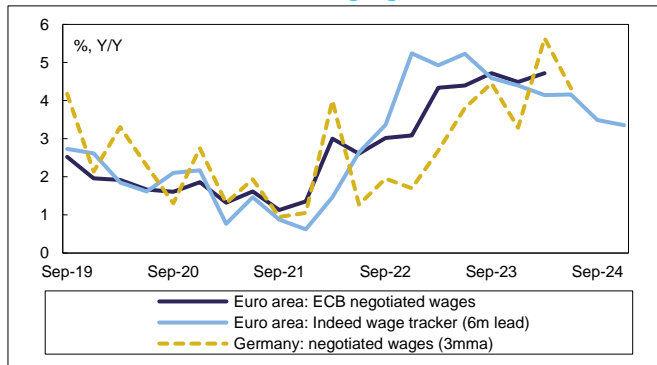
Aside from the data, focus will be on the ECB's central bank forum in Sintra, with the central theme "monetary policy in an era of transformation". ECB President Lagarde will give an introductory speech on Monday evening and participate in a panel discussion with Fed Chair Powell on Tuesday, with Chief Economist Lane and Executive Board member Schnabel to chair panel discussions on drivers of equilibrium interest rates and geopolitical shocks and inflation. The ECB will publish the account from its 6 June monetary policy meeting when the Governing Council cut rates for the first time this cycle.

UK

UK GDP revised higher in Q1 to confirm strongest growth in nine quarter

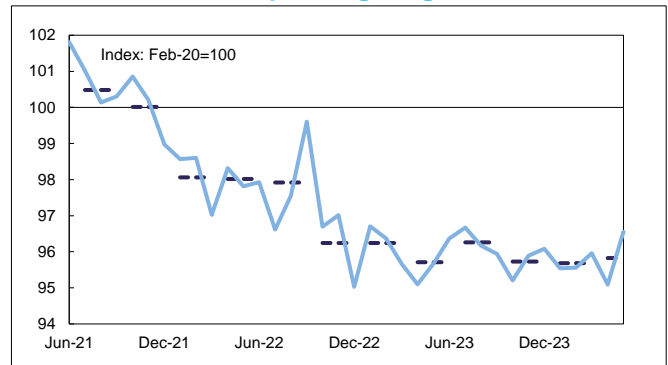
Today's updated UK national accounts figures brought an upwards revision to economic activity in Q1, which had already significantly exceeded expectations in the preliminary release. In particular, GDP growth was revised up by 0.1ppt to 0.7%Q/Q, the most in nine quarters and 0.3ppt above the BoE's projection published in its May Monetary Policy Report. Nevertheless, given the technical recession in the second half of last year, this left GDP up just 0.3%Y/Y to be just 1.8% above the pre-pandemic level in Q419. Moreover, reflecting firm population growth, growth in GDP per head was more moderate in Q1 at 0.5%Q/Q. And, as that marked the first such increase in eight quarters, it was still down 0.7%Y/Y and

Euro area: Measures of wage growth



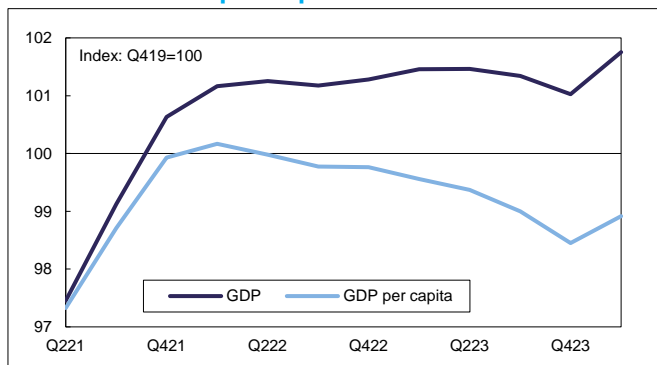
Source: Macrobond and Daiwa Capital Markets Europe Ltd.

France: Consumer spending on goods*



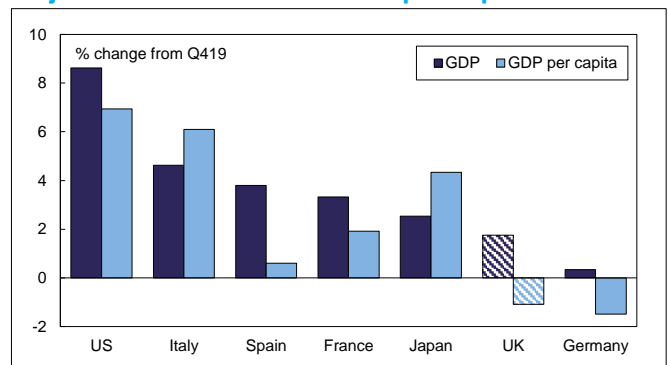
*Dashed dark blue lines represent quarterly averages. Source: Macrobond and Daiwa Capital Markets Europe Ltd.

UK: GDP & GDP per capita



Source: Macrobond and Daiwa Capital Markets Europe Ltd.

Major economies: GDP & GDP per capita vs Q419



Source: Macrobond and Daiwa Capital Markets Europe Ltd.

1.1% below the pre-pandemic level, with a weaker profile only evident in Germany among the G7. Nevertheless, the vigour of the rebound in economic activity in Q1 was encouraging, not least as it tallies with the firmness of survey indicators. And while the PMIs point to somewhat softer recovery momentum towards the end of the second quarter, the upwards revision to the monthly GDP profile in the first quarter and strong retail sales showing in May suggest that the risks to economic growth in Q2 are skewed to the upside. Certainly, today's revision reinforces our expectation for GDP growth of 0.4%Q/Q in Q2.

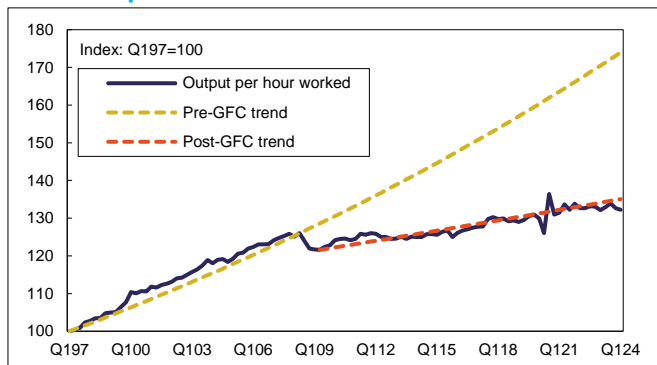
Household consumption revised higher despite an increase in savings

The upwards revision in Q1 in part reflected stronger household consumption (0.4%Q/Q), which contributed 0.3ppt to GDP growth, the most in four quarters. With real household disposable income growth outpacing consumer spending for a fourth consecutive quarter, the household savings ratio jumped to an eleven-quarter high of 11.3%. Given the gradual improvement in consumer confidence, that might point to scope for an acceleration in spending over coming quarters. In contrast, the modestly positive contribution from government spending in Q1 was revised away, while fixed investment was also revised lower. However, investment still rose for a second successive quarter (0.9%Q/Q), supported by a pickup in outlays on private sector dwellings – up for the first quarter in six – and machinery and equipment, while growth in spending on transport goods and overall business investment was softer. Overall, final domestic demand accounted for more than half of GDP growth in Q2. The single largest contribution to GDP growth, however, came from net trade, which is now estimated to add 0.6ppt to GDP growth, the most in six quarters. The upwards revision reflected additional weakness in import volumes (-2.7%Q/Q), while export volumes fell (-1.0%Q/Q) for a fifth successive quarter to extend the dire post-Brexit trend, illustrating how the UK has become a less open economy due to the imposition of Brexit-related trade barriers. Despite a deterioration in the income account, however, the UK's current account deficit moved sideways at 3.1% of GDP, while the underlying deficit (excluding precious metals) narrowed by 0.4ppt to 3.5% of GDP, less than half the pandemic high of 7.5% of GDP in Q122.

The coming week in the UK: Labour to win a landslide, Tories to be in tatters?

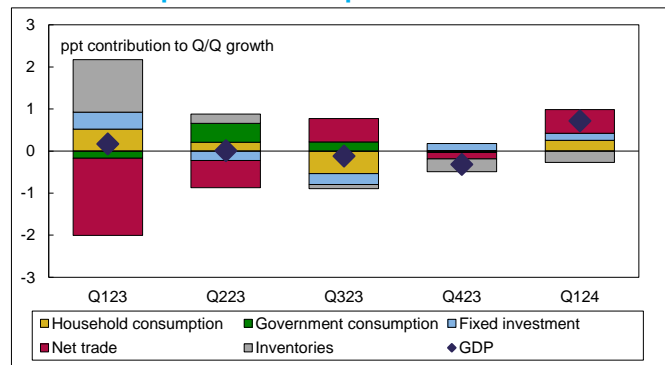
The main event in the UK will undeniably be Thursday's general election. However, there is little doubt that the Labour Party will win comfortably, sending its broadly centrist and relatively technocratic leader Keir Starmer to Downing Street as the successor to five very different Conservative Prime Ministers over the past eight years. Indeed, a landslide win for Starmer's party, with a margin of victory possibly in excess of the 179-seat majority won by Tony Blair's vintage of Labour in 1997, should have been fully priced by the financial markets for some time. That's the message of all opinion polls, which have long reflected the unpopularity of the Conservative party and its track record of scandal and instability, including Liz Truss's Gilt market crisis and Boris Johnson's harmful Brexit deal, tolerance of degraded public infrastructure and services, and apparent prioritisation of divisive culture wars over constructive structural reforms. More recently, a gaffe-prone campaign by

UK: GDP per hour worked



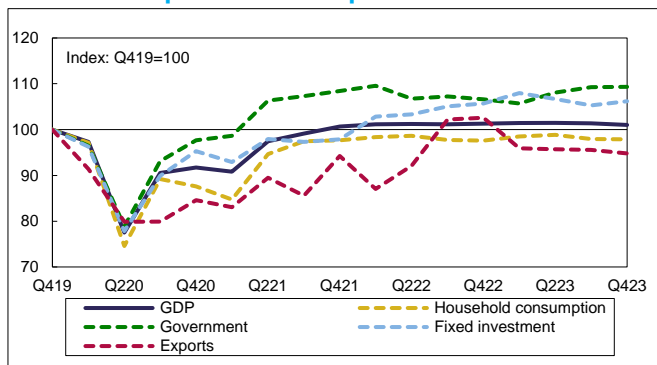
Source: Macrobond and Daiwa Capital Markets Europe Ltd.

UK: GDP expenditure components



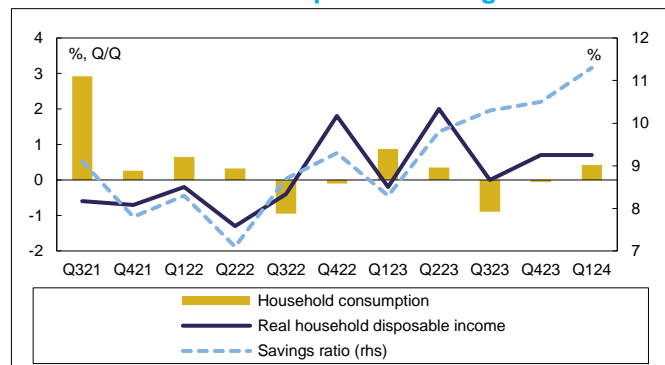
Source: Macrobond and Daiwa Capital Markets Europe Ltd.

UK: GDP expenditure components



Source: Macrobond and Daiwa Capital Markets Europe Ltd.

UK: Household consumption & savings ratio



Source: Macrobond and Daiwa Capital Markets Europe Ltd.

PM Sunak has seemingly rung the final death knell for the current Conservative government. As such, current polls give Labour a lead of roughly 20pts over the Conservatives, with the UK's first-past-the-post system and a probably record extent of tactical voting suggesting that the current ruling party is on track for the lowest number of seats in its history. The main unknowns seemingly relate to quite how big will be the size of the Labour majority, how low will be the number of seats won by the Conservatives, and who among its next possible leadership candidates will manage to hold on to their parliamentary seats. Indeed, if the Conservatives perform particularly poorly and Nigel Farage's populist Reform performs particularly well to raise the risk over coming years of a merger of the two parties into a more extreme French-style right-wing party, investors might have reason to feel more uncomfortable about the outcome.

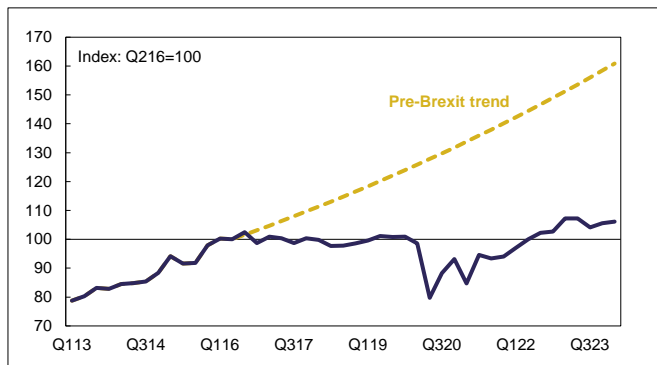
Starmer to offer stability & selected structural reforms, while questions over tax policy remain

Having steered Labour away from far-left policies and expelled his radical predecessor as leader from the party, Starmer and his more-than-ample majority should offer the UK some overdue stability and predictability in policy-making. If so, that should contribute to greater macroeconomic stability too. His priority of correcting the UK's woeful track record on labour productivity and investment – which over recent years has sent the UK alongside Germany to the bottom of the G7 league table in terms of per capita GDP growth having previously rivalled the US near the top – appears appropriate. Labour's manifesto also pledges certain practical structural reforms – including changes to planning regulation to increase housebuilding and boost infrastructure investment, new impetus to the carbon transition, and stronger relations with the EU to open the possibility of somewhat less damaging post-Brexit trading arrangements in certain sectors – which at the margin might also be growth-positive. However, Labour's fiscal policy rules arguably provide insufficient flexibility for it to tackle the UK's significant structural challenges head-on. Notably, its commitment to ensure that government debt as a share of GDP is declining by the fifth year of the forecast will constrain scope to boost public investment. And with a pledge also to avoid increasing rates of income tax, National Insurance Contributions and VAT, Starmer has also limited his room for manoeuvre for funding increased public current expenditure, despite the fact that the Sunak government's public spending projections are unrealistically low. To us, various additional targeted tax-raising measures – perhaps related to capital gains tax and reducing tax relief on savings, and even perhaps some form of windfall tax – seem highly likely on top of existing commitments to remove the special 'non-domiciled' tax status, increase stamp duty on purchases of residential property by non-UK residents, apply VAT and business rates to private schools, and increase tax on carried interest.

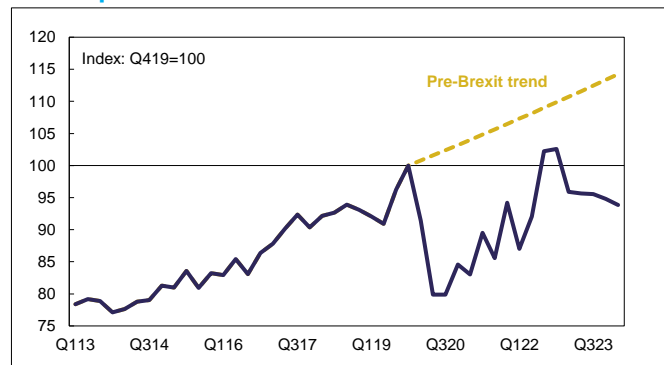
The coming week's data in the UK

In terms of economic data, the coming week's calendar will be relatively thin. Arguably most noteworthy in terms of monetary policy decisions will be the results of the BoE's DMP survey in June (Thursday) that will provide an update on firms'

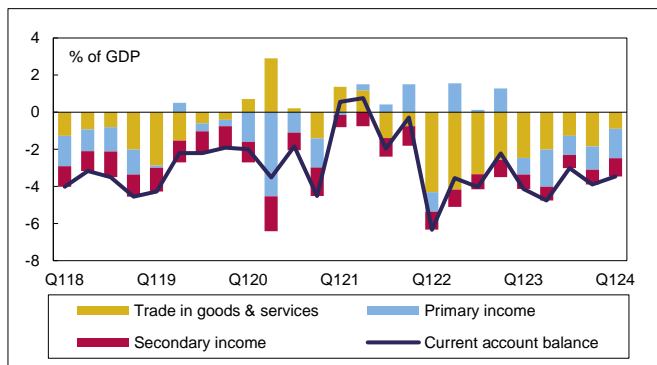
UK: Business investment



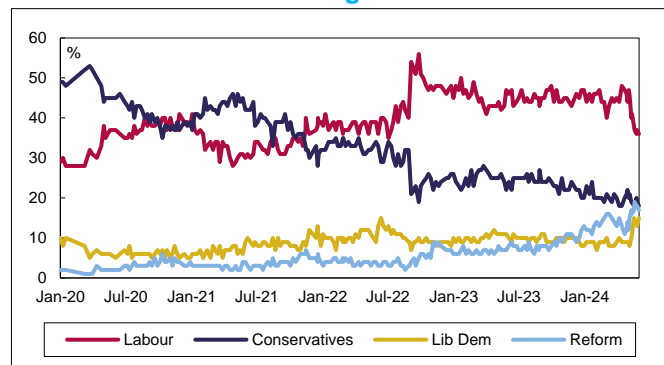
UK: Export volumes



UK: Current account balance












UK: General election voting intentions









expectations for inflation and wage growth. In May, the median forecast for headline CPI one year and three years ahead moved sideways at 2.9%Y/Y and 2.6%Y/Y respectively suggesting that inflation expectations remain well anchored. The BoE's monetary data for May will be published (Monday) along the Nationwide house price survey for June, followed by the BRC's shop price monitor for June on Tuesday. Final June PMI surveys for the manufacturing (Monday), services (Wednesday) and construction (Thursday) are also due.

Daiwa economic forecasts

	2024				2025		2023	2024	2025
	Q1	Q2	Q3	Q4	Q1	Q2			
GDP	%, Q/Q						%, Y/Y		
Euro area 	0.3	0.3	0.3	0.3	0.3	0.4	0.6	0.7	1.4
UK 	0.7	0.4	0.3	0.2	0.2	0.3	0.1	0.9	1.1
Inflation, %, Y/Y									
Euro area									
Headline HICP 	2.6	2.4	2.1	2.4	2.1	1.6	5.4	2.4	1.7
Core HICP 	3.1	2.8	2.7	2.9	2.5	1.7	4.9	2.9	1.7
UK									
Headline CPI 	3.5	2.1	2.1	2.7	2.4	2.0	7.3	2.6	2.1
Core CPI 	4.6	3.6	3.3	3.3	2.8	1.7	6.2	3.7	1.9
Monetary policy, %									
ECB									
Deposit Rate 	4.00	3.75	3.50	3.25	3.00	2.75	4.00	3.25	2.25
Refi Rate 	4.50	4.25	3.65	3.40	3.15	2.90	4.50	3.40	2.40
BoE									
Bank Rate 	5.25	5.25	5.00	4.75	4.50	4.25	5.25	4.75	3.75

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

European calendar

Today's results							
Economic data							
Country	Release	Period	Actual	Market consensus/ Daiwa forecast	Previous	Revised	
Euro area 	ECB consumer expectations survey – 1Y CPI (3Y CPI) Y/Y%	May	2.8 (2.3)	2.8 (2.4)	2.9 (2.4)	-	
Germany 	Unemployment rate % (change 000's)	Jun	6.0 (19)	5.9 (15)	5.9 (25)	-	
France 	Preliminary HICP (CPI) Y/Y%	Jun	2.5 (2.1)	2.5 (2.2)	2.6 (2.3)	-	
	PPI Y/Y%	May	-6.7	-	-6.8	-	
	Consumer spending M/M% (Y/Y%)	May	1.5 (0.9)	0.2 (-0.2)	-0.8 (0.2)	-0.9 (0.0)	
Italy 	Preliminary HICP (CPI) Y/Y%	Jun	09 (0.8)	0.9 (1.0)	0.8 (0.8)	-	
Spain 	Preliminary HICP (CPI) Y/Y%	Jun	3.5 (3.4)	3.5 (3.4)	3.8 (3.6)	-	
UK 	Lloyds business barometer (own price expectations)	Jun	41 (53)	45 (-)	50 (61)	-	
	GDP - final estimate Q/Q% (Y/Y%)	Q1	0.7 (0.3)	0.6 (0.2)	0.6 (0.2)	-	
	Current account balance £bn	Q1	-21.0	-17.6	-21.2	-	
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 1 July 2024					
Euro Area	09.00	Final manufacturing PMI	Jun	45.6	47.3
Germany	08.55	Final manufacturing PMI	Jun	43.4	45.4
	13.00	Preliminary HICP (CPI) Y/Y%	Jun	2.6 (2.3)	2.8 (2.4)
France	08.50	Final manufacturing PMI	Jun	45.3	46.4
Italy	08.45	Manufacturing PMI	Jun	-	45.6
	17.00	New car registrations Y/Y%	Jun	-	-6.6
Spain	08.15	Manufacturing PMI	Jun	-	54.0
UK	07.00	Nationwide house price index M/M% (Y/Y%)	Jun	0.0 (1.2)	0.4 (1.3)
	09.30	Final manufacturing PMI	Jun	51.4	51.2
	09.30	Net consumer credit £bn (Y/Y%)	May	1.5 (-)	0.7 (8.1)
	09.30	Mortgage lending £bn (approvals 000s)	May	1.8 (60.5)	2.4 (61.1)
Tuesday 2 July 2024					
Euro Area	10.00	Preliminary headline (core) HICP Y/Y%	Jun	2.5 (2.8)	2.6 (2.9)
	10.00	Unemployment rate %	May	6.5	6.4
Spain	08.00	Unemployment (employment) change 000s	Jun	-	-58.7 (62.5)
UK	00.01	BRC shop price index Y/Y%	Jun	-	0.6
Wednesday 3 July 2024					
Euro area	09.00	Final services (composite) PMI	Jun	52.6 (50.8)	53.2 (52.2)
	10.00	PPI Y/Y%	May	-4.2	-5.7
Germany	08.55	Final services (composite) PMI	Jun	53.5 (50.6)	54.2 (52.4)
France	08:50	Final services (composite) PMI	Jun	48.8 (48.2)	49.3 (48.9)
Italy	08.45	Services (composite) PMI	Jun	56.5 (-)	54.2 (52.3)
Spain	08.15	Services (composite) PMI	Jun	53.9 (-)	56.9 (56.6)
UK	09.30	Final services (composite) PMI	Jun	51.2 (51.7)	52.9 (53.0)
Thursday 4 July 2024					
Germany	07.00	Factory orders M/M% (Y/Y%)	May	0.8 (-6.0)	-0.2 (-1.6)
	08.30	Construction PMI	Jun	-	38.5
UK	09.00	New car registrations Y/Y%	Jun	-	1.7
	09.30	Construction PMI	Jun	54.0	54.7
	09.30	DMP 3M output price (1Y CPI) expectations Y/Y%	Jun	-	3.9 (2.9)
Friday 5 July 2024					
Euro area	10.00	Retail sales M/M% (Y/Y%)	May	0.2 (0.1)	-0.5 (0.0)
Germany	07.00	Industrial production M/M% (Y/Y%)	May	0.2 (-4.2)	-0.1 (-3.9)
France	07.45	Trade balance €bn	May	-	-7.6
	07.45	Industrial production M/M% (Y/Y%)	May	-1.2 (-1.2)	0.5 (0.9)
Spain	08.00	Industrial production M/M% (Y/Y%)	May	-	0.3 (0.8)

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

The coming week's key events & auctions

Country	BST	Event / Auction
Monday 1 July 2024		
Euro area 	20.00	ECB President Lagarde to introduce the 2024 ECB Forum on Central Banking in Sintra, Portugal.
Tuesday 2 July 2024		
Euro area 	-	ECB's de Guindos (08.30), Schnabel (11.30), President Lagarde and Fed Chair Powell (14.30) discuss euro area inflation, geopolitics and policy in Sintra.
Germany 	10.30	Auction: to sell 0% 2030 and 2050 bonds
UK 	10.00	Auction: £4bn of 3.75% 2027 bonds
Wednesday 3 July 2024		
Euro area 	-	ECB's de Guindos (09.00), Cipollone (10.00), and Chief Economist Lane (11.30) discuss monetary policy, euro area productivity and equilibrium interest rates in Sintra.
Germany 	10.30	Auction: €5bn of 2034 bonds
Thursday 4 July 2024		
Euro area 	12.30	ECB publishes account of June monetary policy meeting
France 	09.50	Auction: to sell bonds
Spain 	09.30	Auction: to sell bonds
UK 	-	General Election – polling day
	09.30	BoE to release Q2 credit conditions and bank liabilities surveys.
Friday 5 July 2024		
Euro area 	12.30	ECB's Lagarde speaks at les rencontres économiques, d'Aix-en-Provence.

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

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