Euro wrap-up

Overview

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- Bunds made gains as euro area export data disappointed, the ZEW survey suggested that investors are a little warier about the German economic outlook, and an ECB survey suggested that credit conditions are very gradually becoming less tight.
- Gilts also followed the global trend higher on a quiet day for economic data from the UK.
- Wednesday will bring updates on inflation in June from the UK and euro area.

Daily bond market movements

Bond	Yield	Change
BKO 2.9 06/26	2.759	-0.027
OBL 2½ 10/29	2.389	-
DBR 2.6 08/34	2.429	-0.040
UKT 0⅛ 01/26	3.952	-0.076
UKT 0½ 01/29	3.890	-0.044
UKT 4⅝ 01/34	4.056	-0.043

*Change from close as at 4:40pm BST.
Source: Bloomberg

Euro area

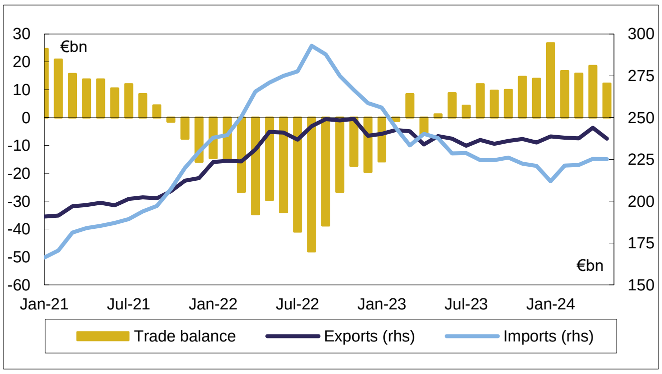
Goods trade deteriorates in May suggesting the net trade will provide a drag on Q2 GDP

Tallying with the drop in manufacturing output in May and the sharp decline in German export shipments that month, today's euro area goods trade data for the middle of Q2 were also underwhelming. Indeed, the headline seasonally adjusted trade surplus narrowed sharply in May, by €6.2bn to €12.3bn, a seven-month low. This narrowing principally reflected the steepest decline in the value of exports for 13 months (-2.6%M/M), with falls in the value of shipments to most of the euro area's major trading partners. Admittedly, having risen by the same magnitude in April, this left export values in the first two months of Q2 trending some 1.1% above the Q1 average. But while the deflators are not yet available for the aggregate figures, the volume of exports reportedly fell sharply to the US and China in May to be trending some way below the Q1 average. Surveys also report a steeper pace of decline in new export orders at the end of the second quarter. And while the value of imports moved broadly sideways in May, this left them more than 3% above the Q1 level. When adjusted for national price data, net goods trade looks to have provided a modest drag on GDP growth last quarter. And the boost from net services trade in Q1 – which added a whopping 0.9ppt due principally to the activities of multi-national corporations in Ireland – also seems highly likely to be at least partly reversed in Q2.

Survey suggests investors are a little warier about the German economic outlook

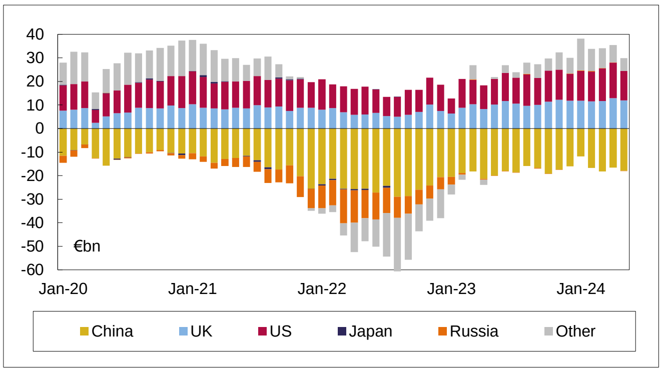
More happily perhaps, contrasting somewhat last week's Sentix survey results, today's July ZEW indices suggested that investor perceptions of economic conditions in Germany have improved somewhat at the start of Q3. Indeed, the survey's current conditions index rose almost 5pts in July to a 12-month high (-68.9), reinforcing the view that the German economic downturn is now well past its bottom. Admittedly, more than 70% of survey recipients judged current conditions still to be bad. Moreover, tallying with the Sentix survey, and probably at least in part related to increased concerns about political risks, the share of respondents expecting conditions to improve over the coming six months fell back below 50%. As such, the survey's expectations balance deteriorated for the first time in a year to a four-month low. At 41.8, however, that remained more than 20pts above the long-run average, strongly suggestive of positive GDP growth in Germany through the second half of the year. Conditions were judged to remain most favourable for firms in IT and services. But they were considered positive for most sectors. Indeed, the retail outlook was judged to be the best in almost 2½ years on expectations of firmer consumption growth. With wholesale energy prices still well down from recent highs, perceptions of chemicals firms also remained favourable. And with more than 80% of survey respondents expecting the ECB to cut rates again over coming months, expectations for the construction sector remained marginally positive too. In contrast, however, sentiment regarding German auto makers remained extremely negative, with the respective index deteriorating to a five-month low amid ongoing concerns about strategic failures, intense competition from abroad and a possible trade war with China related to EV tariffs.

Euro area: Goods trade balance, imports & exports*



*Seasonally adjusted values. Source: Macrobond and Daiwa Capital Markets Europe Ltd.

Euro area: Goods trade balance by country



Source: Macrobond and Daiwa Capital Markets Europe Ltd.

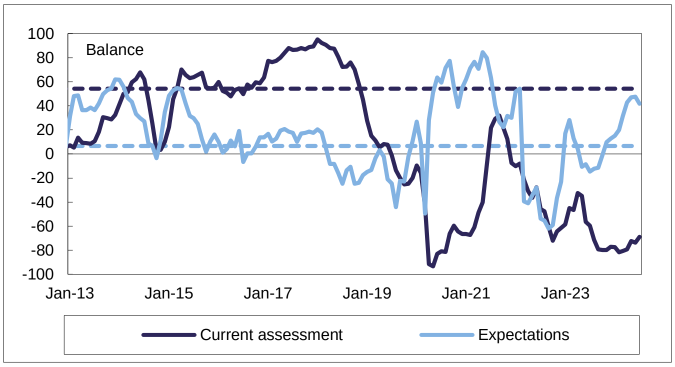
ECB BLS survey signals gradual turn for the better in credit conditions

Ahead of this week's Governing Council policy meeting, the results of the ECB's Bank Lending Survey (BLS) for Q2 broadly aligned with the findings of yesterday's SAFE survey, suggesting that credit standards have eased somewhat from relatively tight levels and loan demand has increased slightly from low levels amid expectations of gradual monetary easing. Certainly, the share of banks reporting a net tightening of credit standards on loans to firms (+2.5%) moderated last quarter to the lowest since Q421 with standards on loans to SMEs no tighter. Banks again reported that climate risks had a net easing impact on credit standards on loans to "green" firms (-25%) and enterprises in transition (-10%) over the past twelve months. But they had a net tightening impact on credit standards to "brown" firms (+44%). And the respective impacts were expected to be somewhat greater over the coming twelve months. Meanwhile, the reported tightening of lending standards on consumer credit in Q2 was the smallest in two years, while banks reported a further net loosening in conditions on mortgage loans amid an increasingly competitive market and gradually improving housing market prospects. This trend was expected broadly to continue this quarter too. Against this more favourable backdrop, demand for loans from households jumped in Q2, with the net increase in mortgage lending (+16%) the highest for three years and consumer credit (13%) the strongest since Q318. And banks expect a further pickup in demand for loans for house purchase in Q3. The BLS also reported an encouraging net increase in demand for business loans among German banks – the most since Q222 – supposedly to support fixed investment plans and finance more working capital and inventories. But across the euro area as a whole, like yesterday's SAFE survey, the BLS reported a weakening in loan demand from firms, although the net decline in Q2 (-7%) was significantly softer than the average over the past year (-31%).

The day ahead in the euro area

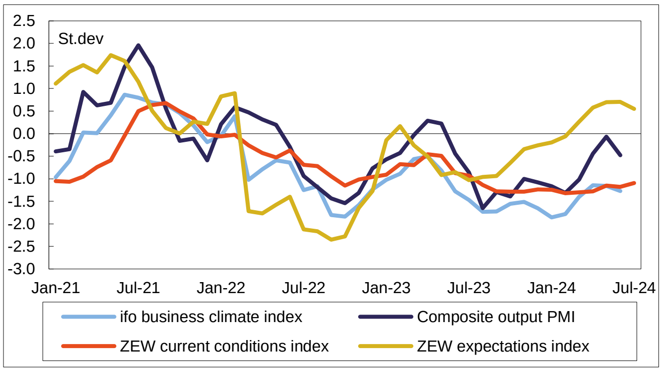
Wednesday will bring final euro area inflation figures for June. Based on updated national figures published by the larger member states – unrevised in Germany (2.5%Y/Y), France (2.5%Y/Y) and Italy (0.9%Y/Y) and only a modest upwards revision in Spain (3.6%Y/Y) – we expect the euro area data to align with the flash estimates, with the headline rate down 0.1ppt from May to 2.5%Y/Y. And while the preliminary release saw the core HICP rate move sideways at 2.9%Y/Y, the granular detail should reinforce the view that recent stickiness in services likely relates to temporary factors.

Germany: ZEW investor survey indices*



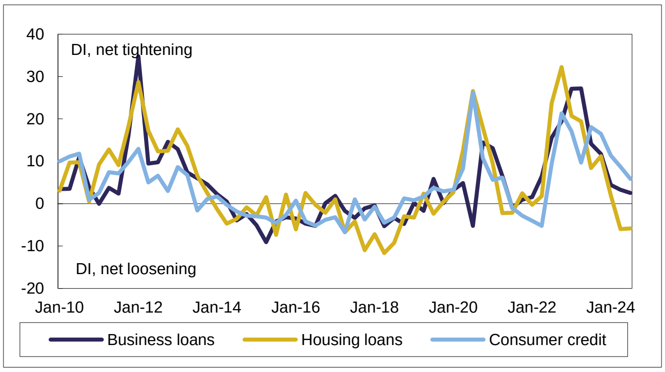
*Dashed lines present pre-pandemic five-year averages. Source: Macrobond and Daiwa Capital Markets Europe Ltd.

Germany: Selected normalised sentiment indices



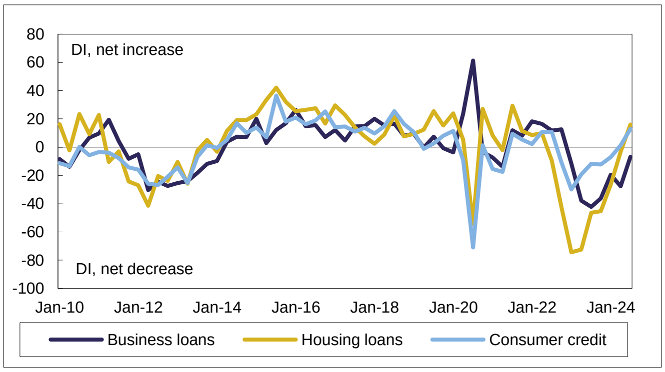
Source: S&P Global, Macrobond and Daiwa Capital Markets Europe Ltd.

Euro area: Bank Lending Survey – credit standards



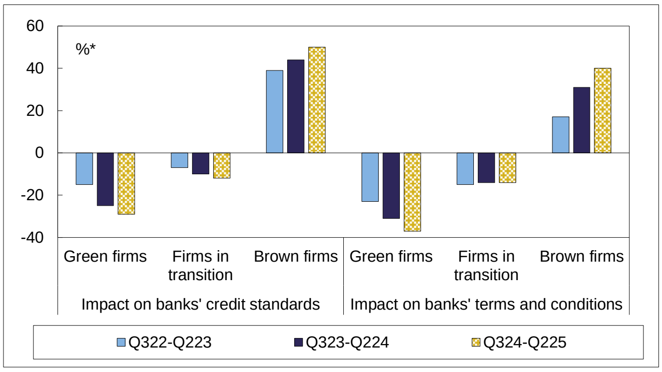
Source: ECB BLS, Macrobond and Daiwa Capital Markets Europe Ltd.

Euro area: Bank Lending Survey – loan demand



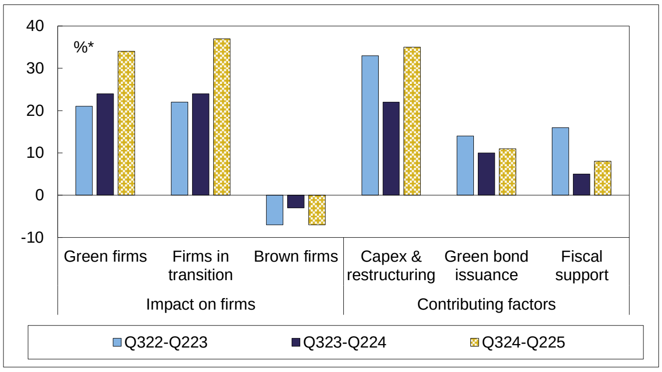
Source: ECB BLS, Macrobond and Daiwa Capital Markets Europe Ltd.

Euro area: Climate change impact on loan standards



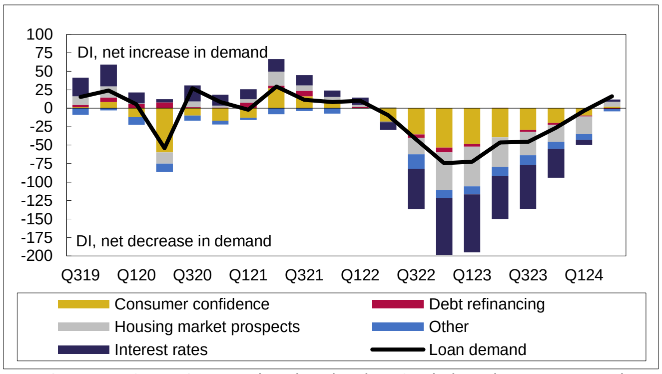
Net % of banks reporting a tightening impact. Source: ECB BLS, Macrobond and Daiwa Capital Markets Europe Ltd.

Euro area: Climate change impact on loan demand



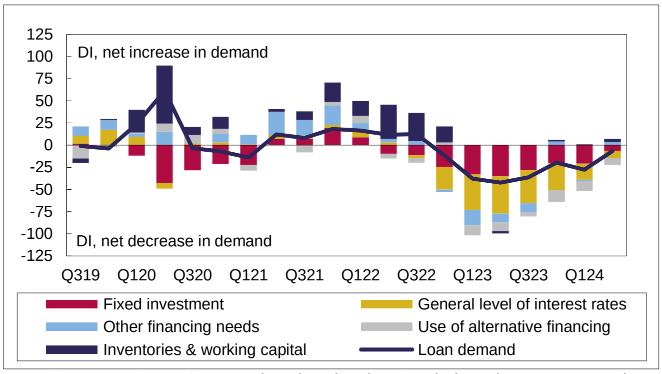
Net % of banks reporting an increase in loan demand. Source: ECB BLS, Macrobond and Daiwa Capital Markets Europe Ltd.

Euro area: Factors affecting housing loan demand



Source: ECB BLS, Macrobond and Daiwa Capital Markets Europe Ltd.

Euro area: Factors affecting business loan demand



Source: ECB BLS, Macrobond and Daiwa Capital Markets Europe Ltd.

UK

The day ahead in the UK

After another quiet day for UK economic data today, focus tomorrow will turn to June's CPI report. Having fallen back to the Bank's 2% target in May for the first time in almost three years, we expect headline inflation to ease slightly further in June, by 0.1ppt to 1.9%Y/Y, in line with the Bloomberg survey consensus. But we see risks to the headline CPI rate to be skewed slightly to the upside. Within the detail, we forecast food inflation to moderate further to its lowest level since October 2021, offsetting a slight upwards impulse from a slightly softer pace of decline in the energy component. And while non-energy goods inflation might tick up, it will remain very subdued close to zero. Of course, of most interest for policymakers will be services inflation, which we expect to edge only marginally lower, by 0.1ppt, to a still elevated 5.6%Y/Y. As such, in line with the consensus, we expect core inflation to move sideways at 3.5%Y/Y. In addition, the latest PPI figures will provide a guide to the outlook for consumer goods inflation, while the ONS house price index for May is also due.

European calendar

Today's results

Economic data

Country	Release	Period	**Actual**	Market consensus/ *Daiwa forecast*	Previous	Revised
Euro area	Trade balance €bn	May	**12.3**	18.1	19.4	18.5
Germany	ZEW investor survey – current situations (expectations) balance %	Jul	**-68.9 (41.8)**	-74.8 (41.0)	-73.8 (47.5)	-
Italy	Final HICP (CPI) Y/Y%	Jun	**0.9 (0.8)**	*0.9 (0.8)*	0.8 (0.8)	-
	Trade balance €bn	May	**6.4**	-	4.8	-

Auctions

Country	Auction
Germany	sold €3.26bn of 2.5% 2029 bonds at an average yield of 2.39%
UK	sold £2.25bn of 4.75% 2043 bonds at an average yield of 4.519%

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

Tomorrow's releases

Economic data

Country	BST	Release	Period	Market consensus/ *Daiwa forecast*	Previous
Euro area	10.00	Final HICP (core HICP) Y/Y%	Jun	*2.5 (2.9)*	2.6 (2.9)
UK	07.00	CPI (core CPI) Y/Y%	Jun	*1.9 (3.5)*	2.0 (3.5)
	07.00	PPI – output (input) prices Y/Y%	Jun	1.8 (1.1)	1.7 (-0.1)
	09.30	House price index Y/Y%	May	-	1.1

Auctions and events

Country	BST	Auction
Germany	10.30	Auction: to sell €1.0bn of 0% 2052 bonds
	10.30	Auction: to sell €1.0bn of 2.5% 2054 bonds
UK	10.00	Auction: to sell £4.0bn of 4.125% 2029 bonds

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

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