

Euro wrap-up

Overview

- Longer-dated Bunds made gains as the flash estimate of German HICP inflation fell below 2%.
- Gilts followed USTs higher on a quiet day for UK economic news.
- Friday will bring the flash estimate of euro area inflation in July as well as the final manufacturing PMIs for the same month and updates on UK house prices and Italian retail sales.

Chris Scicluna

+44 20 7597 8326

Emily Nicol

+44 20 7597 8331

Daily bond market movements

Bond	Yield	Change
BKO 1.9 09/27	1.957	+0.010
OBL 2.2 10/30	2.292	-
DBR 2.6 08/35	2.692	-0.011
UKT 3½ 03/27	3.855	-0.015
UKT 4% 03/30	4.004	-0.033
UKT 4½ 03/35	4.570	-0.031

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

Source: Bloomberg

Euro area

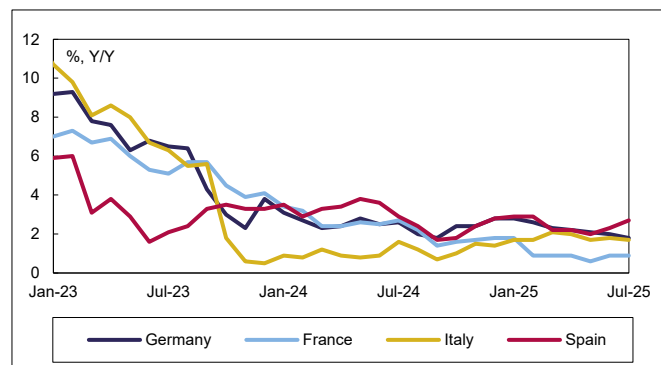
German HICP inflation falls below 2%, with services price pressures moderating

The flash July inflation estimates from the large member states were mixed. But on balance, we maintain our view that the headline euro area HICP rate, due for publication tomorrow, moderated in July, albeit by just 0.1ppt to 1.9%Y/Y. Today's flash German numbers were supportive of this view, with the EU-harmonised measure of inflation falling 0.2ppt to 1.8%Y/Y, a ten-month low and the joint-softest since February 2021. Admittedly, contrasting expectations for a further decline, the national CPI measure moved sideways at 2.0%Y/Y, while the core CPI rate was similarly unchanged at 2.7%Y/Y. This reflected a modest increase in goods price pressures. Having dropped sharply in June, food inflation ticked up slightly, while the annual rate of decline in energy inflation was the softest in four months. Furthermore, our estimate of core goods CPI inflation edged up to a seven-month high. But that was likely in part due to an increase in clothing inflation, which was probably related to the timing of summer discounting and should prove temporary. More encouraging in the national release was a further step down in services inflation to a near-three-year low. The detail from the Lander suggested a moderation in inflation of restaurants and package holidays, while insurance inflation was probably the lowest since early 2024.

Upwards pressure on French and Italian transport services costs likely to prove temporary

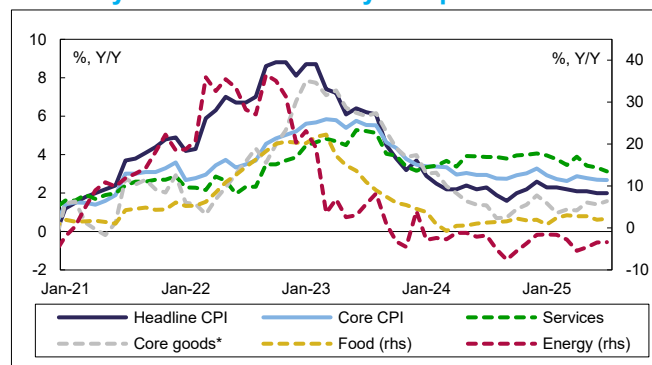
Despite surprising to the upside, headline inflation in France held steady in July at just 0.9%Y/Y, still one of the softest rates in the region. And Italian inflation edged slightly lower, albeit by a smaller-than-expected 0.1ppt to 1.7%Y/Y. In contrast to Germany, the energy components in France and Italy provided a downwards impulse, in part relating to more favourable base effects in regulated gas pricing last month. But this was largely offset by a continued uptrend in food inflation, which rose to the highest level in 17 months in both countries. While there was a decline in Italian hospitality prices and moderation in inflation of certain other services components including recreation and communication, transport costs rose at double the monthly pace compared with a year ago. Higher hotel and transport prices also pushed French services inflation up 0.1ppt to 2.5%Y/Y, an 11-month high. And so, despite an ongoing absence of non-energy industrial goods inflation, French core inflation likely edged slightly higher last month, while the Italian core rate moved sideways. Given these data, we now think that euro area core inflation held steady at 2.3%Y/Y, the joint-lowest level since October 2021. Notwithstanding the pickup in Spanish and Portuguese inflation in July – by 0.4ppt to 2.7%Y/Y and 2.5%Y/Y respectively – and assuming a notable drop in the Netherlands (data also due tomorrow), euro area inflation likely edged back below the ECB's target, albeit with risks seemingly skewed to the upside.

Euro area member states: Headline HICP inflation



Source: Macrobond and Daiwa Capital Markets Europe Ltd.

Germany: CPI inflation & key components



*Non-energy industrial goods.

Source: Macrobond and Daiwa Capital Markets Europe Ltd.

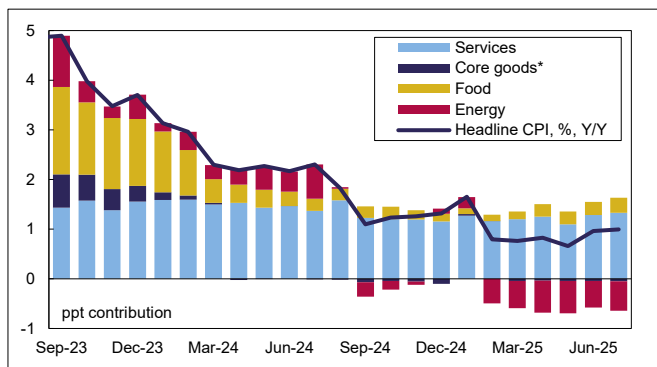
Unemployment rate steady at series low throughout Q2 despite growth slowdown

While GDP growth slowed in Q2, by 0.5ppt to a minimal 0.1%Q/Q, the euro area's labour market appears to have stood firm. The euro area unemployment rate remained in June at the series low of 6.2% for a third successive month. And the number of jobless workers fell 62k to 10.7mn, less than 50k above November's trough. Among the member states, unemployment on the EU-harmonised measure was steady in June in Germany (3.7%) and France (7.0%, matching the two-year low), and fell in Italy (6.3%) and Spain (a 17-year low of 10.4%). Moreover, tallying with the improvement in business sentiment this month, German jobless claims rose in July by just 2k, the least since end-2022. Survey indicators such as the Commission employment expectations indices also suggest that firms are keener to retain or recruit staff than any time since January. However, the services and construction sectors remain most likely to add to headcount with manufacturers and retailers still reluctant to do so. And job growth looks set to remain concentrated in Southern Europe. Indeed, with the number of job vacancies in Germany continuing to decline this month to the lowest level since early 2021 and more than 20% below the 2019 average, the balance of supply and demand in the German labour market remains consistent with continued moderation in pay growth. And the ratio of vacancies to jobless workers in the euro area overall also likely declined further in Q2 similarly back close to levels compatible with more moderate pay growth and on-target inflation.

The day ahead in the euro area

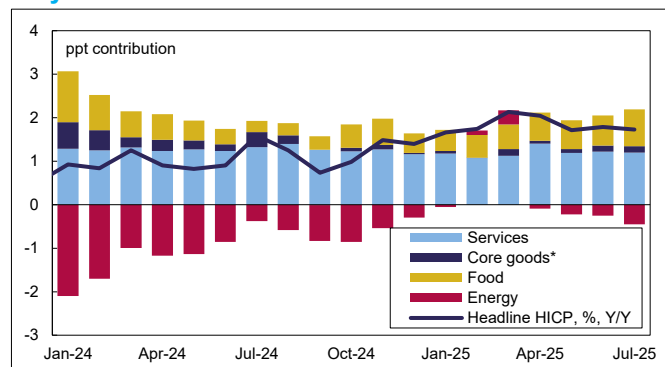
In light of today's member state readings, tomorrow's flash estimate of euro area inflation in July looks likely to have edged modestly lower. This will likely reflect in part the stabilisation in wholesale energy prices this month, which should provide an increased drag from such inflation components in many member states to negate the impact of a base-effect led pick-up in Spain and Portugal. But that effect looks likely to be partially offset by hotter food prices. And an expected uptick in core goods inflation will likely offset a slight moderation in services inflation. As such, we think the headline euro area HICP rate likely eased just 0.1ppt to 1.9%Y/Y, albeit with the risks to that figure skewed slightly to the upside. Elsewhere, tomorrow's euro area final manufacturing PMI is expected to signal another modest expansion in production (50.6) in July, despite relatively flat demand conditions.

France: Contributions to CPI inflation



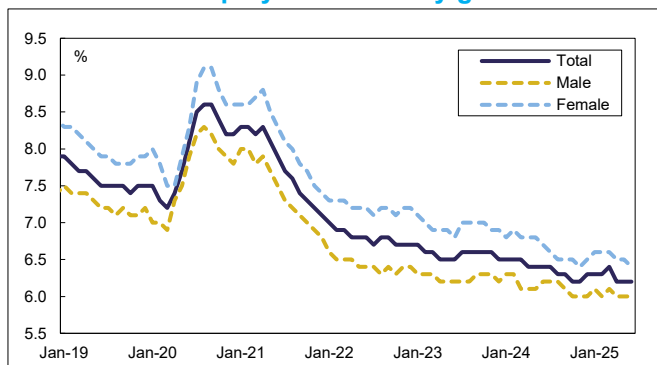
Source: Macrobond and Daiwa Capital Markets Europe Ltd.

Italy: Contributions to HICP inflation



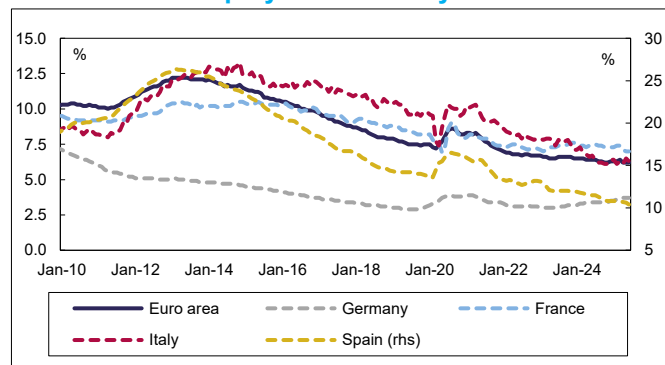
Source: Macrobond and Daiwa Capital Markets Europe Ltd.

Euro area: Unemployment rates by gender



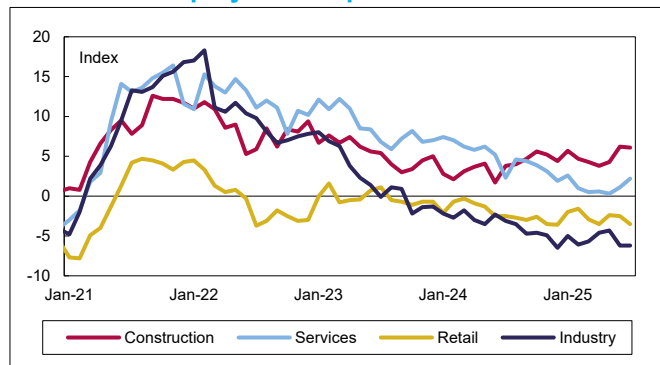
Source: Macrobond and Daiwa Capital Markets Europe Ltd.

Euro area: Unemployment rates by member state



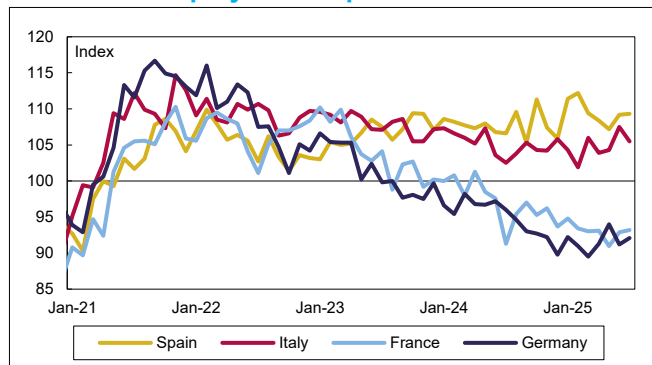
Source: Macrobond and Daiwa Capital Markets Europe Ltd.

Euro area: Employment expectations indices



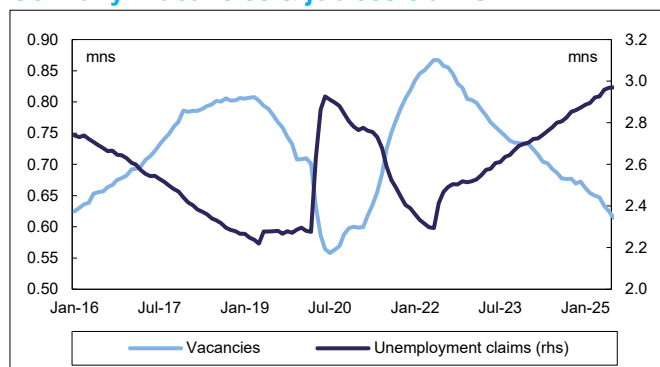
Source: EC, Macrobond and Daiwa Capital Markets Europe Ltd.

Euro area: Employment expectations indices



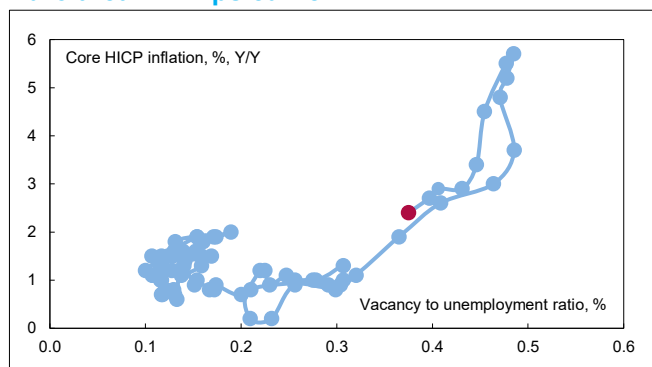
Source: EC, Macrobond and Daiwa Capital Markets Europe Ltd.

Germany: Vacancies & jobless claims



Source: Macrobond and Daiwa Capital Markets Europe Ltd.

Euro area: Phillips curve



Source: Macrobond and Daiwa Capital Markets Europe Ltd.










The day ahead in the UK

Friday will also bring July's final manufacturing PMIs for the UK. From a broader perspective, the flash survey was less upbeat as the composite output PMI pared 1pt to 51.0 amid reports of softer demand. But that change was principally driven by a weakening in the dominant services sector. More optimistically, the headline manufacturing PMI rose by ½pt to 48.2, a six-month high, after manufacturing output was adjudged to have stabilised (50.0) for the first month in nine. Nonetheless, the flash release was also consistent with continued underperformance for manufacturing, with the implied declines in export orders (45.9) and employment (43.4) still downbeat and sharper than those in the services sector. Meanwhile, tomorrow's release of the Nationwide house price index will provide a view of developments in the residential property market at the start of Q3. June saw the steepest monthly price drop since February 2023 (-0.8%M/M). But given the stronger than expected recovery in mortgage lending that month, a rebound in prices in July may be unsurprising. But we also caution that the Rightmove survey, which highlighted the largest decline in asking prices (-1.2%M/M) in any July since the series started in 2002, suggests a more tempered recovery.

European calendar

Today's results

Economic data

Country	Release	Period	Actual	Market consensus/ <i>Daiwa forecast</i>	Previous	Revised
Euro area	 Unemployment rate %	Jun	6.2	6.3	6.3	6.2
Germany	 Preliminary HICP (CPI) Y/Y%	Jul	1.8 (2.0)	1.9 (2.0)	2.0 (2.0)	-
	 Unemployment claims rate % (change 000s)	Jul	6.3 (2)	6.3 (15)	6.3 (11)	- (10)
	 Import prices M/M% (Y/Y%)	Jun	0.0 (-1.4)	-0.2 (-1.6)	-0.7 (-1.1)	-
France	 Preliminary HICP (CPI) Y/Y%	Jul	0.9 (1.0)	0.8 (1.0)	0.9 (1.0)	-
	 PPI Y/Y%	Jun	0.2	-	0.2	-
Italy	 Preliminary HICP (CPI) Y/Y%	Jul	1.7 (1.7)	1.6 (1.5)	1.8 (1.7)	-
	 PPI Y/Y%	Jun	3.9	-	2.8	2.9
UK	 Lloyds business barometer (own price expectations) % balance	Jul	52 (61)	-	51 (61)	-

Auctions










Country	Auction
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- 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
Euro area	 09.00	Final manufacturing PMI	Jul	<u>49.8</u>	49.5
	 10.00	Preliminary headline (core) HICP Y/Y%	Jul	<u>1.9 (2.3)</u>	2.0 (2.3)
Germany	 08.55	Final manufacturing PMI	Jul	<u>49.2</u>	49.0
France	 08.50	Final manufacturing PMI	Jul	<u>48.4</u>	48.1
Italy	 08.45	Manufacturing PMI	Jul	48.7	48.4
	 09.00	Retail sales M/M% (Y/Y%)	Jun	0.3 (1.6)	-0.4 (1.3)
Spain	 08.15	Manufacturing PMI	Jul	51.8	51.4
UK	 00.01	Nationwide house price index M/M% (Y/Y%)	Jun	0.5 (2.2)	-0.8 (2.1)
	 09.30	Final manufacturing PMI	Jul	<u>48.2</u>	47.7

Auctions and events

- Nothing scheduled -

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

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