Euro wrap-up

Overview

- Bunds made losses as euro area inflation ticked higher in July while German jobless claims rose once again.
- Gilts also followed the global trend lower, while UK house price growth slowed at the start of Q3 as higher mortgage rates weighed on activity.
- The coming week will bring June data for euro area retail sales, German factory orders, IP and trade, alongside the final July PMIs.

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Daily bond market movements

Bond	Yield	Change
BKO 2.7 09/28	2.811	+0.053
OBL 2.9 10/31	2.936	+0.054
DBR 3 08/36	3.200	+0.047
UKT 4⅜ 03/28	4.400	+0.070
UKT 4⅛ 03/31	4.594	+0.070
UKT 4¾ 10/35	5.047	+0.064

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

Euro area

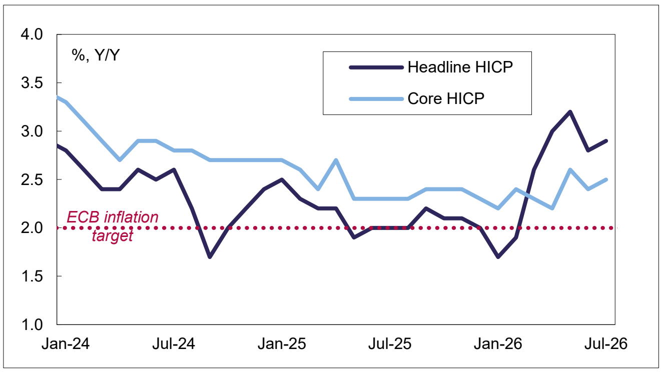
Euro area inflation boosted by energy prices, while uptick in core likely reflects seasonal pressures

After yesterday's stronger-than-expected Q2 GDP outturn and signs of firmer growth momentum at the start of Q3, today's flash euro area inflation estimates further supported our expectation that the Governing Council will hike rates again in September. Admittedly, the headline HICP inflation rate edged only slightly higher in July, by 0.1ppt to 2.9%Y/Y. And, given the soft print in June, it remained some 0.5ppt below the ECB's June baseline projection for Q3. As expected, energy again played a key role, with prices rising for the first time in three months as the renewed uptick in wholesale prices was exacerbated by the unwinding of fiscal support measures. This lifted energy inflation up 1.5ppts to 10%Y/Y, accounting almost fully for the monthly increase in headline inflation. Encouragingly, however, today's release offered little evidence of significant pass-through to the non-energy components. Indeed, prices of food, alcohol and tobacco were unchanged in July having fallen in the previous two months, pushing the annual rate to the softest in five years at 1.2%Y/Y. And while the core components edged slightly higher, this appears to be largely related to seasonal factors. The limited country detail suggests that the reversal in non-energy industrial goods inflation, by 0.2ppt to 0.9%Y/Y, partly reflects an upward impulse on clothing. We suspect that airfares played a role in the uptick in services, by 0.1ppt to 3.3%Y/Y. And the extended heatwave perhaps gave a boost to accommodation inflation too. Overall, core HICP inflation came in a touch firmer than expected, up 0.1ppt to 2.5%Y/Y, albeit in line with the ECB's baseline projection.

Risks to inflation outlook skewed to upside, justifying September rate hike (& probably more)

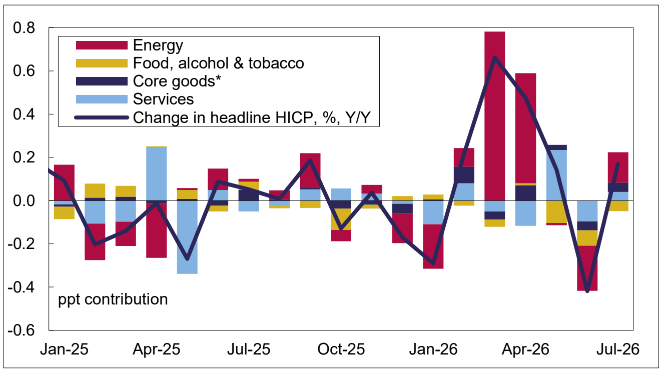
While surveys suggest that households and businesses have recently revised down their price expectations, risks to the near-term inflation outlook clearly remain skewed to the upside. Obviously, much will depend on developments in the Middle East and their effect on energy prices. And the longer the conflict drags on and energy prices remain high, the greater the indirect effects and risks of second-round effects. At the very least, the recent upwards trajectory in pump prices suggests they will add meaningfully to inflation in August, and unfavourable base effects will be reflected in the data through the autumn. And unless wholesale gas futures curves shift significantly lower over the coming month, the ECB's assumption for household energy inflation will likely need to be shifted higher when it is updated in September. Meanwhile, although food inflation has undershot expectations since the start of the conflict, higher input costs and drought will soon change that dynamic. Some of the initial pipeline pressures associated with higher energy prices will also likely be passed along the factory supply chain and into services prices too. So, while it will probably have to make a downwards revision to its projection for headline inflation in Q3, the ECB will also likely revise up its profile thereafter through to end-2027. And so, with the June projections already conditioned on three rate hikes this cycle, we see a strong possibility that the Governing Council will need to hike rates twice more before year-end.

Euro area: Headline & core inflation



Source: Macrobond and Daiwa Capital Markets Europe Ltd.

Euro area: Contributions to change in inflation



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

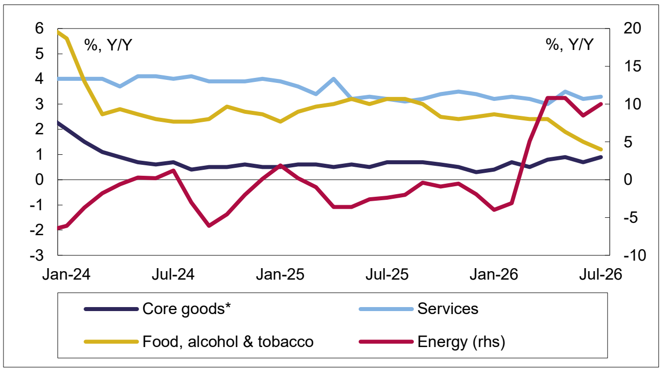
German labour market remains subdued despite third successive quarter of positive GDP growth

While yesterday's German GDP data confirmed a third successive quarter of positive economic growth in Q2 (0.2%Q/Q), today's figures suggested that the labour market continues gradually to soften. On a seasonally adjusted basis, German employment edged down for the third successive month in June and by 30k to 45.67mn, 230k (0.5%) below the level a year earlier and the lowest in almost four years. Jobless claims rose in July and surpassed the symbolically important 3.0mn threshold on an unadjusted basis, to nudge the claimant count unemployment rate back up to 6.4%, matching April's six-year high. Job vacancies increased very slightly for a third successive month and remained above levels a year earlier to raise hopes of some stabilisation in labour demand. But surveys suggest that, on average, firms in most major sectors bar construction, healthcare and social services are seeking increased cuts to headcount. Despite a pickup in production last quarter thanks not least to government support for defence and infrastructure as well as precautionary stock-building, the weakness in labour demand remains most pronounced in industry. And with challenges in Germany's key autos and energy-intensive subsectors appearing potentially existential, consumer fears of unemployment continue to mount, in July reaching their highest level since the Covid pandemic in early 2021. Excluding one-off payments, German negotiated wage growth slowed in July to 2.4%6M/Y, the softest rate in more than two years and below the long-run average. Of course, workers will still seek compensation for the hit to their real incomes from the energy price shock. And so, wage negotiations in the autumn will be watched attentively by the ECB. But concerns about job security amid persistent weak labour demand should ensure that settlements remain moderate, containing risks of second-round inflation effects from pay.

The week ahead in the euro area

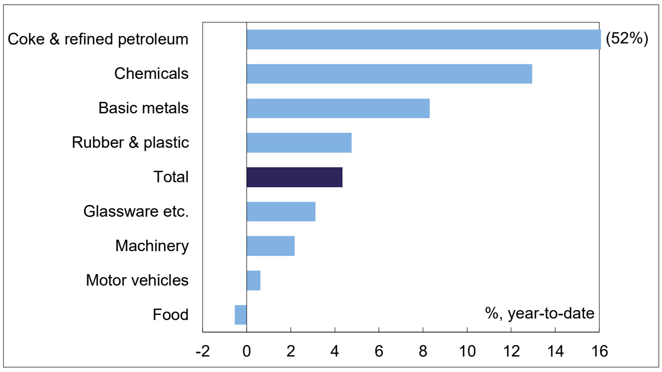
The most significant economic data in the coming week will concern June's activity data. Yesterday's firm [preliminary Q2 GDP] report suggests that they should display continued resilience. Despite the oil shock's detrimental impact on household sentiment and purchasing power, euro area retail sales figures (Thursday) look well placed to confirm an 11th consecutive quarter of growth, if only around ¼%Q/Q. Food (trending 1% above the Q1 average) and core retail volumes (0.3% higher) have thus far proved sufficient to compensate for a sharp drop in fuel sales (-3.4%). And the prospects for June also appear relatively favourable, with easing prices likely to have supported at least partial recovery in fuel and food sales and hot weather likely to have boosted demand for goods such as electrical fans and air conditioners, albeit disproportionately for online retailers. Timelier releases from Germany (Monday) and Italy (Tuesday) will further refine expectations ahead of the aggregate euro area release. For what it's worth, German retail sales growth has generally underperformed its peers, trending broadly flat in April and May despite temporary support from a since-expired energy tax cut. However, German industrial production (Friday) has fared better – trending some 0.5% above the Q1 average – supported by manufacturers' precautionary stock-building and higher defence and infrastructure spending. Although business surveys were wholly more

Euro area: Key HICP inflation components



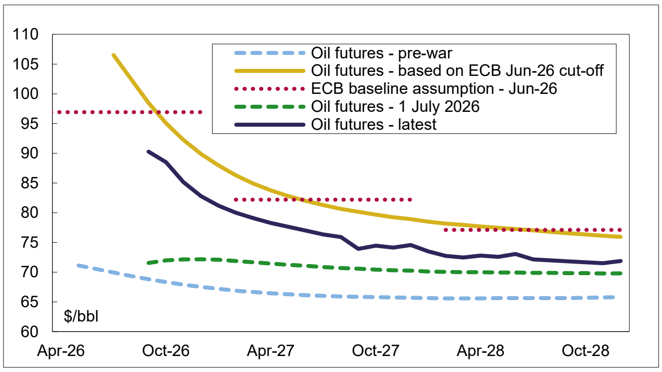
*Non-energy industrial goods.
Source: Macrobond and Daiwa Capital Markets Europe Ltd.

Euro area: PPI inflation, May-26



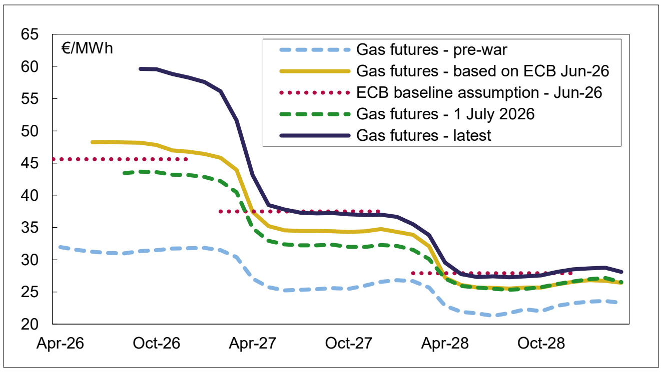
Source: Macrobond and Daiwa Capital Markets Europe Ltd.

Euro area: Brent crude futures & ECB assumptions



Source: Bloomberg, ECB Jun-26 and Daiwa Capital Markets Europe Ltd.

Euro area: Natural gas futures & ECB assumptions



Source: Bloomberg, ECB Jun-26 and Daiwa Capital Markets Europe Ltd.

upbeat this month, sentiment in June was more mixed. Payback for May's strength (0.9%M/M) cannot be discounted, but the ifo survey also suggested that production in energy-intensive subsectors improved somewhat as input price pressures receded. That should help to shore up a partial rebound, after a near-1% drop in Q1.

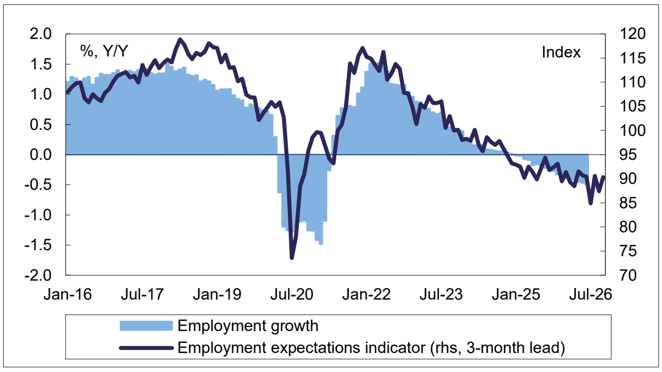
Italian and Spanish IP (Thursday) are likely to confirm a similar pattern in Southern Europe, while goods trade data from Germany and France (also Friday) should also point towards a positive contribution to GDP from net exports last quarter. Prior to that, factory orders data from Germany (Thursday) will provide an indication about production over the coming months. While the boost to manufacturing orders at the onset of the oil shock was expected to be fleeting, the flash manufacturing PMIs (final release on Monday) suggested that demand was the firmest in three months in July, owing to a boost in Germany. With services activity (final release Wednesday) also stronger, market activity in the euro area reportedly expanded (51.9, up 1.9pts) at its fastest since February. The final surveys are expected to affirm that momentum, although to the extent that surveys collected later in July will better reflect the reescalation of conflict in the Middle East, a markdown to activity, or pickup in the price indices, could be possible. Otherwise, the construction PMIs (Thursday) will also reveal whether that improvement extended to all major sectors or, as we expect, extreme temperatures across much of Europe and the ECB's tightening of monetary policy provided headwinds. Finally, consistent with the data from the member states, euro area producer price data will report a drop in the headline rate from May's three-year high of 5.9%Y/Y with still relatively limited pipeline price pressures identifiable beyond the energy-intensive sectors and items dependent on supply via the Strait of Hormuz.

UK

House price growth appears to slow at the start of Q3 as higher mortgage rates weigh on activity

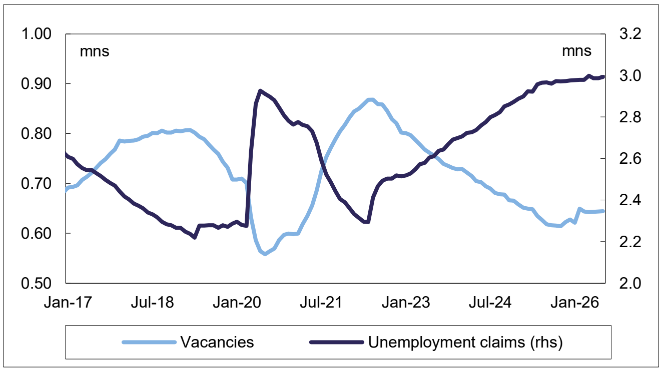
Given the rise in household borrowing rates following the outbreak of conflict in the Middle East, the signs of further softening in housing market momentum from today's Nationwide house price survey for July should have come as little surprise. The survey scraped a first monthly increase for three months (0.1%M/M), but annual price growth slowed to 1.8%Y/Y, down 0.4ppt. Even without Governor Bailey's assertions on Thursday that the MPC is not positioning for a rate hike any time soon, the broader outlook for house prices remains subdued. Indeed, while mortgage rates have edged down slightly from their recent highs, the BoE acknowledged in its Monetary Policy Report that they remain some 80bps above their levels prior to the oil shock, hampering affordability. RICS' latest housing market survey also remained broadly downbeat about its assessment of buyer demand and anticipated downwards pressure on prices over the coming quarter. And while mortgage approvals – which provide a rough indicator to future household borrowing – edged up slightly in June (to 58.2k), that compensated for just a fraction of the near-15%M/M drop in May and remained some 10% below levels in June 2025.

Germany: Employment growth & expectations*



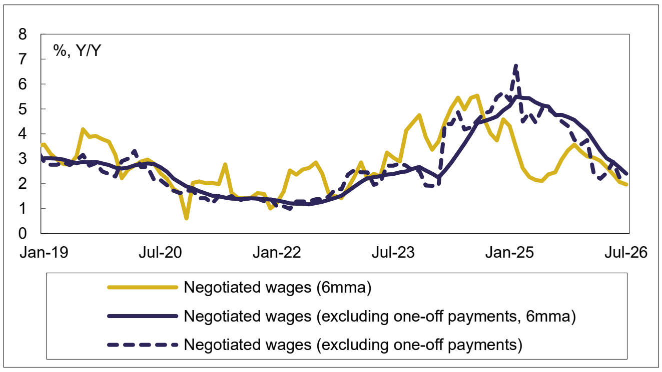
*Business employment expectations index. Source: Macrobond and Daiwa Capital Markets Europe Ltd.

Germany: Jobless claims & vacancies



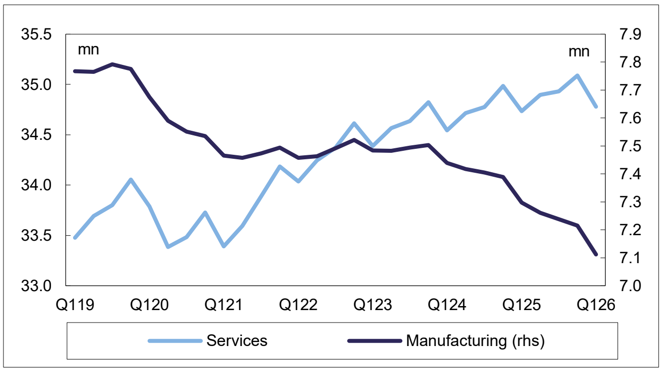
Source: Macrobond and Daiwa Capital Markets Europe Ltd.

Germany: Negotiated wage growth



Source: Macrobond and Daiwa Capital Markets Europe Ltd.

Germany: Employment in services & manufacturing



Source: Macrobond and Daiwa Capital Markets Europe Ltd.

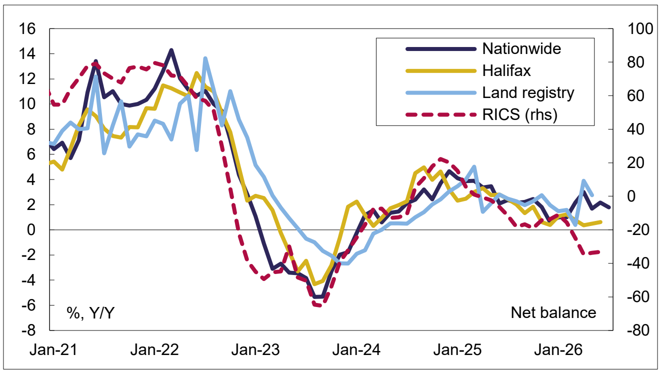
While on the backburner, proposals to shake-up housing taxation likely to reemerge eventually

Of course, new Prime Minister Andy Burnham has repeatedly touted his attentiveness to the 'cost of living' and already announced a temporary VAT cut on electricity bills from Q426. So, measures targeted at improving housing affordability seem likely to be on his policy agenda. Beyond the levers of planning system reform, public construction and new demand-side assistance, Burnham has made no secret of his desire to reform the council tax system, whose property bands were last revalued in April 1991, and stamp duty land tax, which is a damaging friction to property transactions deterring both supply and demand. Intertwined with his broader plans to devolve spending responsibilities to the regions, Burnham was reportedly considering replacing both taxes with an annual flat rate tax (of 0.48%) of a property's value. Fiscal realities dictate that any reform would have to be no more generous than net-neutral in terms of tax-and-spend. But it would certainly shift a greater share of the burden towards areas with higher property valuations, particularly London and the South East, to the benefit of other regions. On average, London house prices (particularly at the top end) have already been falling in real terms for several years and such a tax reform could well represent a further headwind for that market. But reports this week suggested that such reforms have been ruled out for the government's next budget in the autumn. And to the extent that such a significant reform would be both politically and technically complex (if not impossible) to fully implement in a short period, it seems improbable that such a change will be possible before the end of this Parliament, which will conclude in 2029 at the latest. Still, we would not be surprised if similar avenues were explored by the government before that time, or if the groundwork were to be laid out for wider consultation ahead of the next general election.

The week ahead in the UK

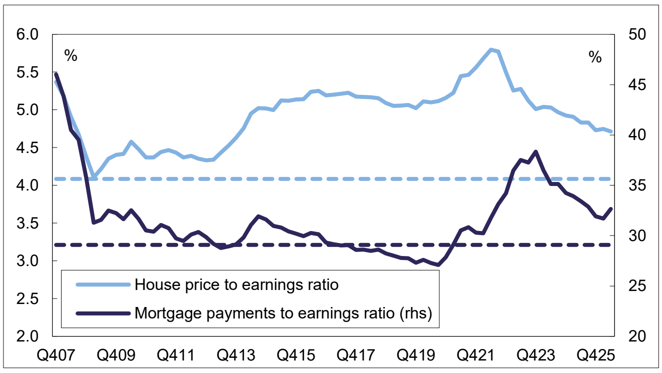
A relatively quiet week ahead for UK economic releases will bring little more than the final July PMIs, with the manufacturing survey due on Monday, the services indices on Wednesday and the construction release on Thursday. The flash PMIs pointed to a broad-based acceleration in underlying activity at the start of Q3, with the headline composite index jumping 2.7pts – the most since February 2023 – to 52.1, a three-month high. The manufacturing output index (53.6) signalled a fourth-successive monthly expansion and the strongest growth since September 2024. And the services index (up 3pts to 51.8) likely benefited from firmer demand for hospitality relating to the prolonged heatwave and the FIFA World Cup. While the survey's message on the near-term outlook for manufacturing and services was more mixed, the flash composite PMIs had suggested that increases in input costs and output prices were the softest in five months. Given the subsequent reescalation in tensions in the Middle East and associated pickup in wholesale energy costs, risks to the final activity and outlook PMIs seem skewed to the downside while upwards revisions to the price indices would not be a surprise. Meanwhile, although it has been a particularly poor guide to the official output data from the sector since March, the construction activity PMI is likely again to point to contraction as tighter financial conditions and persisting uncertainty weigh on demand. Finally, beyond the PMIs, new car registrations figures for July (Wednesday) should point to ongoing solid growth in sales of EVs.

UK: House price growth & survey indicators



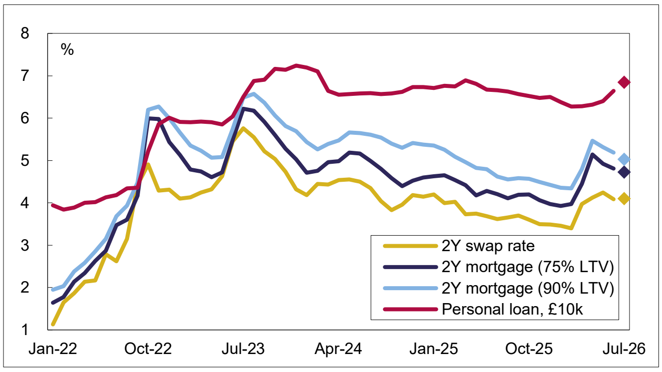
Source: Macrobond and Daiwa Capital Markets Europe Ltd.

UK: First-time buyer housing affordability ratios*



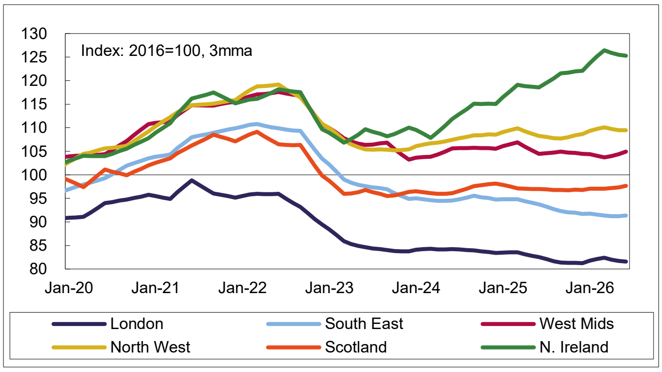
**Dashed lines show long-run averages since Q190.*
Source: Nationwide, Macrobond and Daiwa Capital Markets Europe Ltd.

UK: 2Y swap rate & household interest rates



**Diamonds show provisional data for July 2026.*
Source: BoE Jul-26 MPR and Daiwa Capital Markets Europe Ltd.

UK: Real house prices in selected regions*



**CPI deflated.*
Source: Nationwide, Macrobond and Daiwa Capital Markets Europe Ltd.

Daiwa economic forecast

	2026				2027		2026	2027	2028
	Q1	Q2	Q3	Q4	Q1	Q2			
GDP	**%, Q/Q**						**%, Y/Y**		
Euro area	0.0	0.4	0.2	0.2	0.3	0.4	0.8	1.1	1.4
UK	0.6	0.4	0.1	0.1	0.4	0.3	1.1	1.1	1.4
Inflation, %, Y/Y									
Euro area									
Headline HICP	2.0	3.0	3.1	3.4	3.4	2.7	2.9	2.7	2.0
Core HICP	2.3	2.4	2.5	2.7	2.9	2.8	2.5	2.8	2.2
UK									
Headline CPI	3.1	2.8	3.3	3.5	3.4	2.9	3.2	2.7	2.0
Core CPI	3.2	2.5	2.8	3.0	3.2	3.2	2.9	3.0	2.5
Monetary policy, %									
ECB									
Deposit Rate	2.00	2.25	2.50	2.50	2.50	2.50	2.50	2.25	2.25
Refi Rate	2.15	2.40	2.65	2.65	2.65	2.65	2.65	2.40	2.40
BoE									
Bank Rate	3.75	3.75	3.75	3.75	3.75	3.75	3.75	3.25	3.25

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	Preliminary headline (core) HICP Y/Y%	Jul	**2.9 (2.5)**	*2.9 (2.4)*	2.8 (2.4)	-
Germany	Unemployment claims rate % (change 000s)	Jul	**6.4 (6)**	6.3 (5)	6.3 (-1)	-
France	Preliminary HICP (CPI) Y/Y%	Jul	**2.4 (2.1)**	2.0 (1.8)	2.0 (1.8)	-
	PPI Y/Y%	Jun	**2.6**	-	3.0	3.1
Italy	Preliminary HICP (CPI) Y/Y%	Jul	**2.9 (2.8)**	2.9 (2.8)	3.0 (3.0)	-
	Istat economic (manufacturing) confidence indicator	Jul	**95.6 (89.6)**	-	95.2 (88.4)	95.3 (88.6)
	Istat consumer confidence indicator	Jul	**94.2**	92.8	92.4	-
UK	Nationwide house prices M/M% (Y/Y%)	Jul	**0.1 (1.8)**	0.1 (1.9)	0.0 (2.2)	-

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/ *Daiwa forecast*	Previous
		Monday 3 August 2026			
Euro area	09.00	Final manufacturing PMI	Jul	*52.0*	51.4
Germany	07.00	Retail sales M/M% (Y/Y%)	Jun	-	1.0 (-2.9)
	08.55	Final manufacturing PMI	Jul	*52.2*	50.3
France	08.50	Final manufacturing PMI	Jul	*50.0*	51.2
Italy	08.45	Manufacturing PMI	Jul	52.5	52.2
Spain	08.15	Manufacturing PMI	Jul	50.6	49.7
UK	09.30	Final manufacturing PMI	Jul	*52.8*	52.5
		Tuesday 4 August 2026			
Italy	09.00	Retail sales M/M% (Y/Y%)	Jun	-	0.2 (2.2)
Spain	08.00	Unemployment change (employment net change) 000s	Jul	-	-28.7 (92.5)
		Wednesday 5 August 2026			
Euro area	09.00	Final composite (services) PMI	Jul	*51.9 (51.6)*	50.0 (49.4)
	10.00	PPI Y/Y%	Jun	4.7	5.9
Germany	08.55	Final composite (services) PMI	Jul	*51.2 (49.6)*	49.5 (48.6)
France	07.45	Industrial production M/M% (Y/Y%)	Jun	0.3 (0.6)	-0.1 (3.2)
	08.50	Final composite (services) PMI	Jul	*49.6 (49.8)*	47.2 (46.8)
Italy	08.45	Composite (services) PMI	Jul	52.0 (51.1)	50.8 (50.2)
Spain	08.15	Composite (services) PMI	Jul	53.5 (54.8)	53.3 (54.2)
UK	09.00	New car registrations Y/Y%	Jul	-	11.4
	09.30	Final composite (services) PMI	Jul	*52.1 (51.8)*	49.3 (48.8)
		Thursday 6 August 2026			
Euro area	08.30	Construction PMI	Jul	-	42.8
	10.00	Retail sales M/M% (Y/Y%)	Jun	0.1 (1.0)	0.2 (1.6)
Germany	07.00	Factory orders M/M% (Y/Y%)	Jun	0.8 (6.0)	1.9 (6.2)
	08.30	Construction PMI	Jul	-	44.8
France	07.45	Preliminary wages Q/Q%	Q2	-	0.7
	08.30	Construction PMI	Jul	-	38.2
Italy	08.30	Construction PMI	Jul	-	45.4
	09.00	Industrial production M/M% (Y/Y%)	Jun	0.3 (1.1)	-0.3 (1.1)
Spain	08.00	Industrial production M/M% (Y/Y%)	Jun	-	1.2 (3.4)
UK	09.30	Construction PMI	Jul	40.0	38.4
		Friday 7 August 2026			
Germany	07.00	Industrial production M/M% (Y/Y%)	Jun	0.0 (0.0)	0.9 (0.0)
	07.00	Trade balance €bn	Jun	16.7	19.1
France	06.30	Unemployment rate (mainland unemployment rate) %	Q2	8.2 (8.0)	8.1 (7.9)
	07.45	Trade balance €bn	Jun	-	-6.9

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

The coming week's key events & auctions

Country		BST	Event / Auction
Monday 3 August 2026			
			- Nothing scheduled -
Tuesday 4 August 2026			
Germany		10.30	Auction: to sell up to €6bn of 2.7% 2028 bonds
UK		10.00	Auction: to sell £4.25bn of 4.625% 2032 bonds
		12.00	BoE to publish quarterly Asset Purchase Facility Report for Q226
Wednesday 5 August 2026			
Germany		10.30	Auction: to sell up to €500mn of 2.1% 2029 green bonds
		10.30	Auction: to sell up to €500mn of 2.5% 2035 green bonds
		10.30	Auction: to sell up to €500mn of 1.8% 2053 green bonds
Thursday 6 August 2026			
Euro area		09.00	ECB to publish Economic Bulletin 5/2026
France		09.50	Auction: to sell up to €12.5bn 1.25% 2036, 3.7% 2036, 3.8% 2037 & 0.5% 2044 bonds
Spain		09.30	Auction: to sell 2.6% 2031, 3% 2033, 3.4% 2036 bonds & 2.05% 2039 inflation-linked bonds
Friday 7 August 2026			
			- Nothing scheduled -

**Details to be announced. Source: Bloomberg and Daiwa Capital Markets Europe Ltd.*