Euro wrap-up

Overview

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- While euro area producer prices fell for the first time since before the start of the Iran conflict and the latest French industrial production data were weak, Bunds were little changed.
- Gilts were also little changed from Tuesday's close as the UK's final July services PMIs were consistent with slightly firmer activity and moderating price pressures in the sector.
- Thursday will bring June data for euro area retail sales and German factory orders as well as the July construction PMIs.

Daily bond market movements

Bond	Yield	Change
BKO 2.7 09/28	2.716	+0.008
OBL 2.9 10/31	2.829	+0.004
DBR 3 08/36	3.101	-0.004
UKT 4⅜ 03/28	4.229	-0.001
UKT 4⅛ 03/31	4.418	-0.015
UKT 4¾ 10/35	4.882	-0.013

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

Euro area

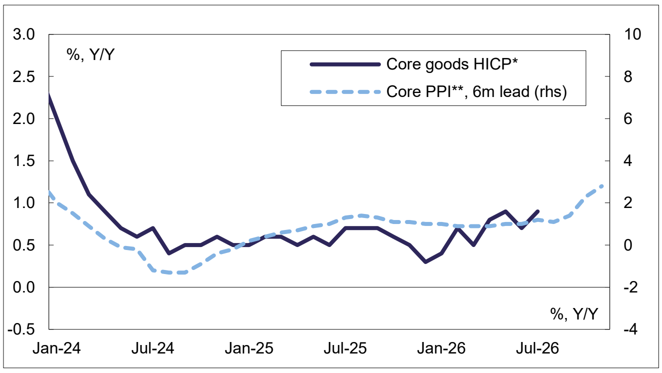
PPI inflation falls in June by most in 14 months with indirect effects of energy shock well contained

With oil and gas prices having moved lower over the course of June, euro area industrial producer prices also fell that month on average for the first time since February. Overall, producer output prices fell 0.3%M/M, more than reversing the rise in May and suggesting a moderation of the inflationary shock from the Middle East. Given the sharp increase in prices a year earlier, industrial PPI inflation slowed 1.3ppt, the most in 14 months, to a three-month low of 4.6%Y/Y. And producer output prices were up 'just' 3.9% from the start of the Iranian conflict at the end of February. Producer energy prices fell for a third successive month and by 1.5%M/M. But they were still 8% above their level ahead of the conflict while producer prices for the extraction of crude petroleum and natural gas were up almost 22% on the same basis. The other detail suggested that the indirect impact of the price shock remains relatively well contained. Prices of intermediate goods rose 0.3%M/M in June, the least since February, albeit remaining some 4.3% above their level that month. And pressures were largely confined to hydrocarbon-intensive sectors such as coke and refined petroleum (up 29.1% since February), chemicals and related items including fertilisers (18.2% on the same basis), as well as metals such as aluminium, and paper and related items. But on the month, many of those prices fell or posted only very modest increases. Beyond the energy shock, AI-related demand pressures were reflected in higher prices of computers and peripheral equipment (up 4.0% since February), circuit boards and electrical wiring. But most notably perhaps, price rises for capital goods and non-food consumer goods were again limited at 0.3%M/M to be up since February by 'just' 1.1% and 0.9% respectively. And prices of manufactured food products fell for a second successive month to be up a mere 0.1% since the onset of the Iranian conflict.

Upside risks to industrial PPI inflation persist but surveys suggest they have passed their peak

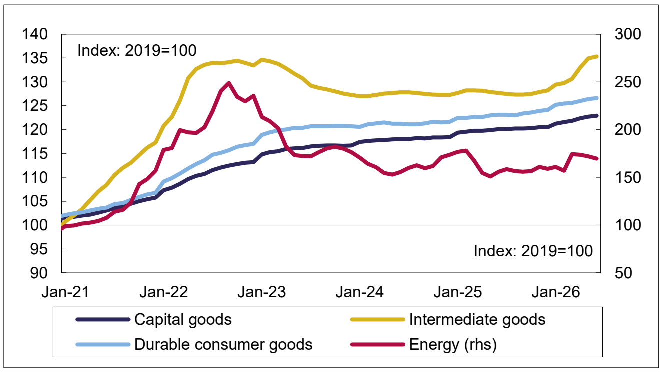
Looking ahead, industrial PPI inflation likely rose moderately in July as energy prices moved higher once more. And despite the better tone to wholesale oil and gas prices this month on hopes of progress towards a deal in the Middle East, there remain upside risks to producer prices from other sources, including AI-related demand to Europe's summer drought. Indeed, with water levels on Europe's major rivers at record lows, shipping freight costs on major arteries such as the Rhine have leapt to record highs, with some of that traffic having to find alternative means of transportation. And for the same reason, interruptions to hydroelectric and nuclear power generation risk introducing a further impulse to electricity prices. Nevertheless, ECB policymakers should take comfort from the moderation in July in the manufacturing PMIs for input costs (68.2) and output prices (57.3) to their lowest levels since February and March respectively. And other survey indicators point to an easing of business price-setting expectations, e.g. the Commission measure of industrial selling-price expectations three months ahead also declined in July to the lowest level since before the conflict kicked off.

Euro area: Consumer & producer goods inflation



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

Euro area: Producer price levels

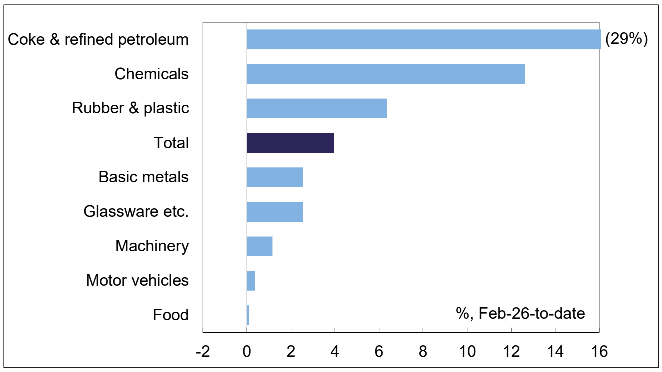


Source: Macrobond and Daiwa Capital Markets Europe Ltd.

Services PMIs point to easing price pressures & stronger activity at the start of Q3

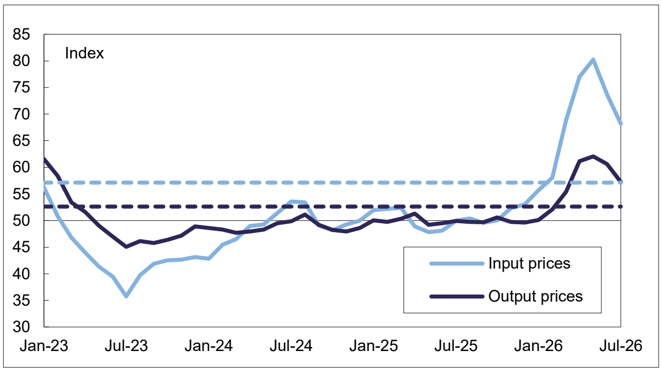
Despite the jump in freight costs and volatility in energy prices, surveys suggest that underlying services inflation pressures continue to ease too. According to today's final result, the services input costs PMI (61.2) was revised slightly lower from the flash estimate, signalling the softest cost inflation in five months. And despite signs of strengthening demand, the services output price PMI (53.9) fell to its lowest level since March, less than 1pt above the average in the six months preceding the Iran conflict. At the same time, likely supported in part by AI-related activity, the headline services activity PMI rose more than 2pts in July to a five-month high of 51.7, some 3½pts above the Q2 average, while growth in new business was reportedly the firmest since December. Encouragingly, activity improved across the member states, albeit to varying degrees, with the Spanish services PMI (up 4pts to 58.3) the strongest in more than three years and the Italian index up to a five-month high (52.5), suggesting ongoing outperformance in Southern Europe. Indeed, the Spanish composite PMI (56.5) was the strongest since December 2024 and 5pts above the long-run average. And the German (51.3), French (49.4) and Italian (52.5) indices rose to four-, five- and eight-month highs respectively. Overall, the euro area composite PMI (52.0) was consistent with GDP growth of 0.3%Q/Q in Q3, underscoring the continued resilience to the shocks from the Middle East.

Euro area: Change in producer prices, Feb-Jun '26



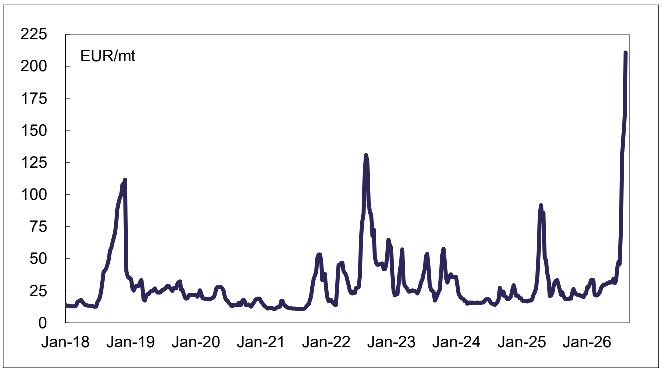
Source: Macrobond and Daiwa Capital Markets Europe Ltd.

Euro area: Manufacturing price PMIs*



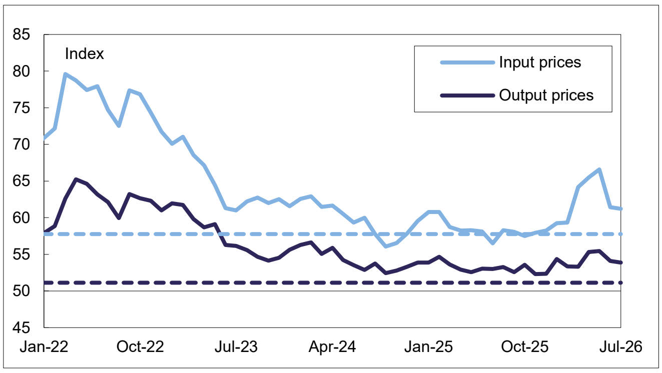
**Dashed lines represent long-run average.*
Source: S&P Global, Macrobond and Daiwa Capital Markets Europe Ltd.

Germany: River Rhine barge freight rate*



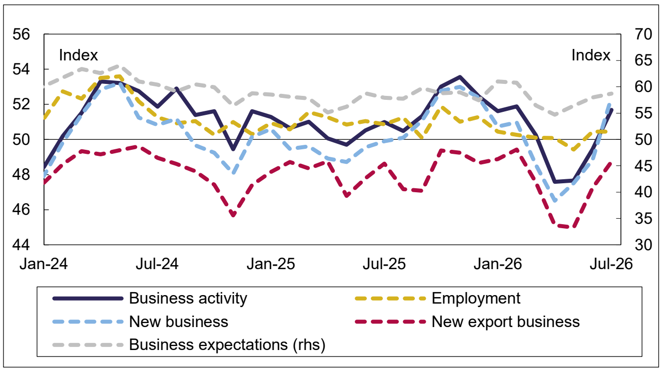
**Cost of transporting a barge of gasoline from Dutch ports to Karlsruhe.*
Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

Euro area: Services price PMIs*



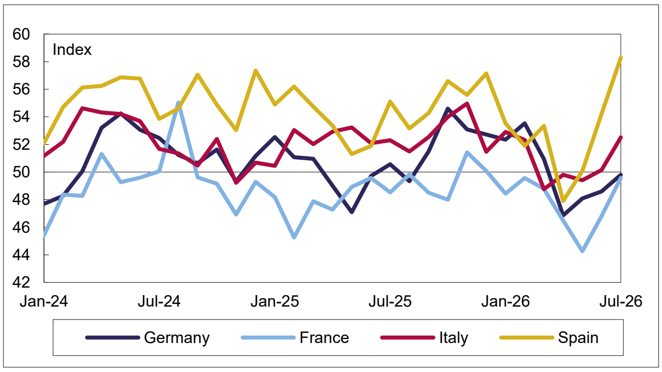
**Dashed lines represent long-run average.*
Source: S&P Global, Macrobond and Daiwa Capital Markets Europe Ltd.

Euro area: Services PMIs



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

Euro area member states: Services activity PMIs



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

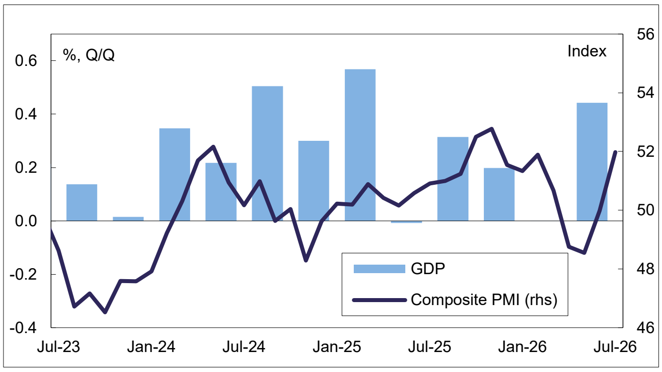
French manufacturing output drops sharply in June, but surveys suggest outlook will improve in Q3

While the French economy returned to growth in Q2 (0.2%Q/Q) as services activity accelerated, today's industrial production figures for June highlighted the continued fragility in the factory sector. Industrial output rose a respectable 0.7%Q/Q, slightly firmer than implied by the national accounts. However, this growth largely reflected a favourable carryover from March and a surge in demand for electricity amid the prolonged heatwave. Indeed, despite a rose of almost 4%M/M in energy output in June, total industrial production increased just 0.1%M/M. By contrast, manufacturing output fell for a second successive month, by a steep 1.0%M/M, to its lowest level in ten months. While this partly reflected another sharp decline in production of coke and refined petroleum due to a shutdown of a refinery for summer maintenance and reduced production elsewhere due to extreme temperatures, the deterioration was relatively broad-based. Although ICT equipment production rebounded from May's decline, output of transport equipment fell sharply (-3.8%M/M) and motor vehicle production slipped to the lowest in 18 months. Chemicals (-3.2%M/M) and electrical equipment (-1.9%M/M) also posted sizeable declines. Today's release also highlighted persistent weakness in construction, where activity fell in June for a fifth month in six (-2.9%M/M) to the lowest level since the first Covid lockdown period in Q220. That is consistent with the signals of recent surveys and likely reflected the phasing out of a government renovation incentive programme as well as higher borrowing costs. In contrast, business surveys suggest that French manufacturers entered Q3 in a more upbeat mood, albeit with production expectations uneven across the subsectors. And while the recovery in services was sustained early in the summer, it remains to be seen to what extent the surge in wildfires and persistent job insecurity will impact demand, particularly in tourism and hospitality.

The day ahead in the euro area

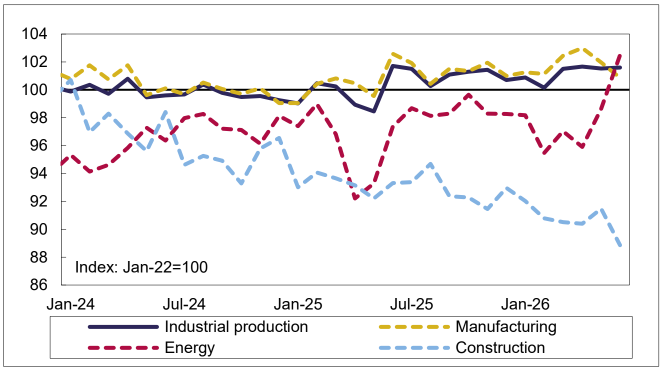
Despite the energy price shock's detrimental impact on household sentiment and purchasing power, June's euro area retail sales release is expected to confirm an 11th consecutive quarter of growth. Indeed, while sales volumes fell back sharply in Germany (-1.1%M/M) and France (-0.5%M/M), growth in Southern Europe suggests that the decline in the region as a whole will be less stark, perhaps just 0.2%M/M. A rebound in fuel sales following their temporary lull in prices is likely to have provided some compensation for lower sales of food and other goods. If so, then retail sales are likely to have expanded by around 0.2%3M/3M in Q2, broadly matching their reserved pace before the Iran conflict. By comparison, industrial production likely fared much better. Italian and Spanish IP data for June will further inform expectations ahead of next week's euro area release. And ahead of Friday's German data, June's factory orders update may continue to reflect rising demand, given that business surveys have maintained momentum. Meanwhile, the construction PMIs will suggest whether the pickup in activity demonstrated by the manufacturing and services PMIs extended to all major sectors. While that survey might suggest that material cost pressures eased somewhat last month, extreme temperatures across much of Europe and tighter monetary policy might have provided headwinds, pointing towards another relatively subdued reading.

Euro area: GDP growth & composite output PMI



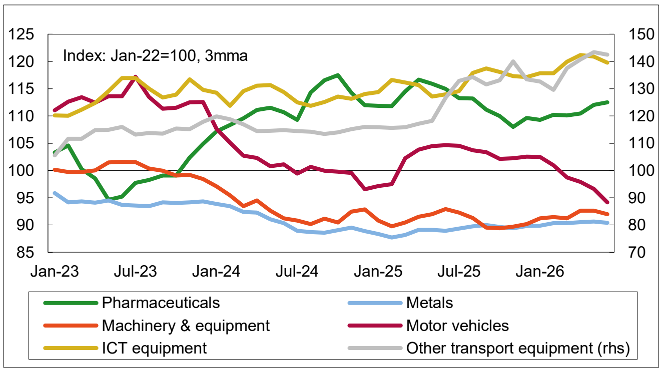
Source: S&P Global, Macrobond and Daiwa Capital Markets Europe Ltd.

France: Industrial production



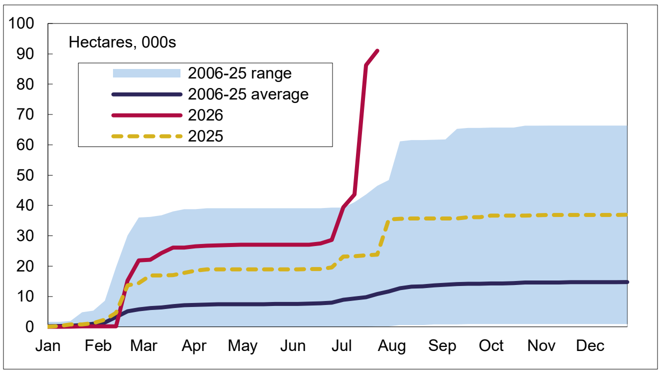
Source: Macrobond and Daiwa Capital Markets Europe Ltd.

France: Manufacturing production by sector



Source: Macrobond and Daiwa Capital Markets Europe Ltd.

France: Cumulative YTD weekly burnt land area



Source: EU Copernicus Emergency Management Service and Daiwa Capital Markets Europe Ltd.

UK

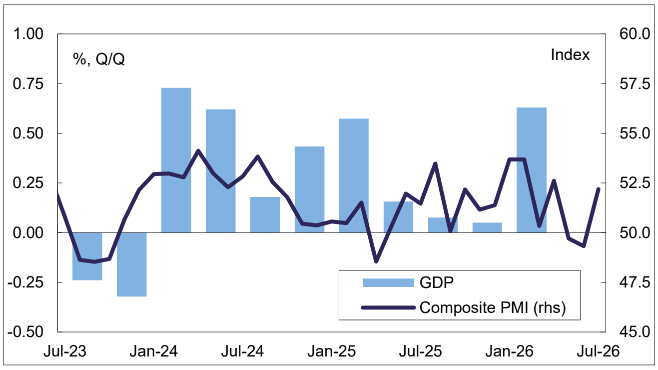
Services PMIs point to improved but still soft growth momentum in July & easing price pressures

Contrasting the modest downwards revision to the final UK manufacturing PMIs, today's services survey signalled somewhat stronger growth than implied in the flash release, likely supported by the prolonged heatwave, England's performance in the FIFA World Cup and renewed optimism following Andy Burnham's confirmation as Prime Minister. In particular, the headline services activity index rose more than 3pts in July to a three-month high of 52.1, albeit remaining relatively subdued compared with the historical average. Growth in new business in the sector remained lacklustre (50.8) as strong demand for technology services was countered by persisting headwinds from geopolitical uncertainty. And while a larger share than in recent months, fewer than half of the surveyed businesses expected output to rise over the coming twelve months. Overall, the composite output PMI rose for the first month in three. But at 52.2, it was still at a level that if sustained would be consistent with little better than stagnation and will likely reinforce the MPC's assessment that underlying GDP growth remains sluggish. Today's survey similarly suggested that labour market conditions remain soft, as firms signalled a continued desire to cut headcount for a 22nd successive month, matching the longest losing run on in the survey's three-decade history. As in the euro area, policymakers will also note that the PMIs suggested a further easing in input price pressures at the start of Q3, with the respective composite index down almost 5pts to a five-month low (65.8). While still some way above the long-run average, the composite output price PMI (56.5) was similarly the softest since February. With the equivalent services measure (55.6) now back close to levels seen at the start of the year, the MPC is likely to remain comfortable keeping Bank Rate on hold. Indeed, we continue to expect the BoE's next move to be a cut rather than a hike, but perhaps not until the second half of next year.

The day ahead in the UK

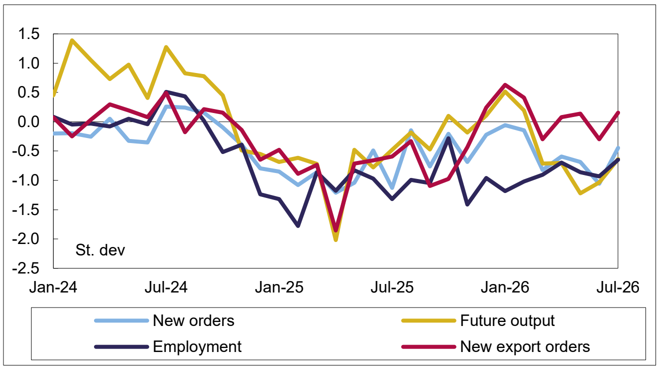
On an otherwise quiet day for UK economic news, July's construction PMIs will provide the sole data release. We caution that the survey does not always provide the most accurate steer to the official output data for the sector. But it was notable that the headline construction activity index (38.4) recorded its 18th consecutive sub-50 reading in June, with civil engineering (22.1) reportedly contracting at its sharpest rate outside of the first pandemic lockdown. A less dramatic pullback in that subsector, perhaps in addition to easing material costs, could provide cause for some improvement in July. However, given the still uncertain outlook, high borrowing costs and the potential for continued weather-related disruption, any upside is likely to be limited.

UK: GDP growth & composite output PMI



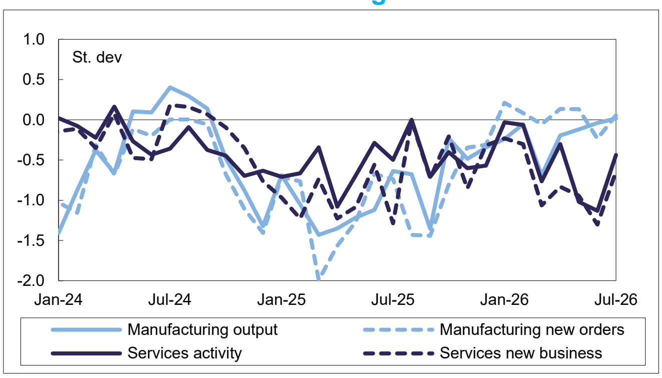
Source: S&P Global, Macrobond and Daiwa Capital Markets Europe Ltd.

UK: Composite PMIs



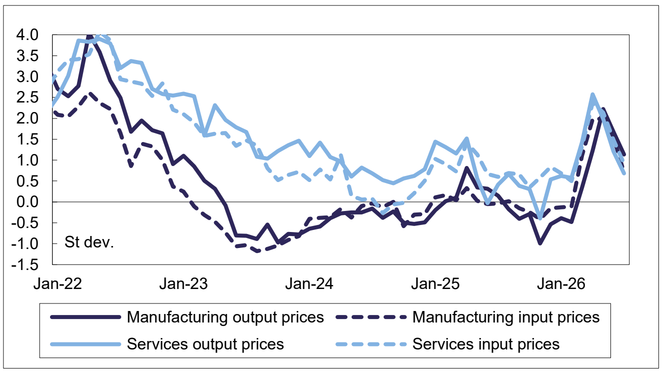
Source: S&P Global, Macrobond and Daiwa Capital Markets Europe Ltd.

UK: Services & manufacturing PMIs



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

UK: Price PMIs



Source: S&P Global, Macrobond 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		Final composite (services) PMI	Jul	**52.0 (51.7)**	*51.9 (51.6)*	50.0 (49.4)	-
		PPI Y/Y%	Jun	**4.6**	4.6	5.9	-
Germany		Final composite (services) PMI	Jul	**51.3 (49.8)**	*51.2 (49.6)*	49.5 (48.6)	-
France		Industrial production M/M% (Y/Y%)	Jun	**0.1 (-0.1)**	0.3 (0.6)	-0.1 (3.2)	- (3.1)
		Final composite (services) PMI	Jul	**49.4 (49.6)**	*49.6 (49.8)*	47.2 (46.8)	-
Italy		Composite (services) PMI	Jul	**52.5 (52.5)**	51.5 (51.0)	50.8 (50.2)	-
Spain		Composite (services) PMI	Jul	**56.5 (58.3)**	53.5 (54.8)	53.3 (54.2)	-
UK		Final composite (services) PMI	Jul	**52.2 (52.1)**	*52.1 (51.8)*	49.3 (48.8)	-
		New car registrations Y/Y%	Jul	**11.7**	-	11.4	-

Auctions

Country		Auction
Germany		sold €490mn of 2.1% 2029 green bonds at an average yield of 2.71%
		sold €472mn of 2.5% 2035 green bonds at an average yield of 3.01%
		sold €310mn of 1.8% 2053 green bonds at an average yield of 3.60%

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

Tuesday's results

Economic data

Country		Release	Period	**Actual**	Market consensus/ *Daiwa forecast*	Previous	Revised
Italy		Retail sales M/M% (Y/Y%)	Jun	**-0.1 (3.1)**	-	0.2 (2.2)	-
Spain		Unemployment change (employment net change) 000s	Jul	**19.5 (79.6)**	-	-28.7 (92.5)	-

Auctions

Country		Auction
Germany		sold €4.552bn of 2.7% 2028 bonds at an average yield of 2.78%
UK		sold £4.25bn of 4.625% 2032 bonds at an average yield of 4.613%

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

Tomorrow's releases

Economic data

Country		BST	Release	Period	Market consensus/ *Daiwa forecast*	Previous
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	0.5 (5.9)	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

Auctions and events

Country		BST	Event
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

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

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