

# Euro wrap-up

## Overview

- Despite an upside surprise from the latest German CPI data and an upbeat euro area economic sentiment survey, Bunds were little changed.
- Gilts made gains at the longer end, with 10Y yields falling to record lows, as a survey signalled a marked deterioration in UK consumer confidence.
- Friday brings preliminary euro area GDP data for Q2 and inflation figures for July, along with further UK consumer and business sentiment surveys, and the results of the latest EU bank stress tests.

**Chris Scicluna**

+44 20 7597 8326

### Daily bond market movements

Bond	Yield	Change*
BKO 0 06/18	-0.613	+0.006
OBL 0 10/21	-0.504	+0.009
DBR 0 08/26	-0.084	-0.004
UKT 1¼ 07/18	0.130	-0.002
UKT 1½ 01/21	0.304	-0.004
UKT 2 09/25	0.717	-0.020

\*Change from close as at 4.30pm BST.  
 Source: Bloomberg

## Euro area

### Economic sentiment firm in July

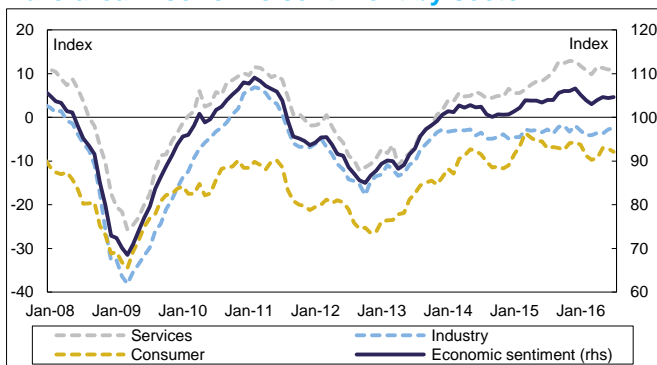
Typically the most reliable guide to economic growth in the euro area is provided by the European Commission's business and consumer surveys. And, consistent with other recent barometers of sentiment such as the PMIs and national surveys, the Commission's results for July released today were consistent with ongoing steady expansion, with the overall euro area economic sentiment indicator (ESI) posting a small increase to 104.6, above the average of the first half of the year and close to the top of the range of recent years. The slight deterioration in consumer confidence flagged by the flash estimate was confirmed, although this still remained above the average of the first half of the year. Meanwhile, contrary to expectations of a decline, business confidence rose to its highest level of the year to-date. Services sector confidence edged up on higher expectations of future demand, while manufacturing confidence posted a larger gain thanks to increased order books. But the most notable improvements in sentiment about the outlook were seen among retailers and construction firms. And financial services firms were more upbeat too. Among other detail, services firms' employment intentions shifted notably higher as did their selling price intentions. But other sectors were less upbeat in those respects. And consumer price expectations fell.

Among the large member states, however, the latest results were very much a mixed bag. Perhaps surprisingly, the most significant improvement in economic sentiment was registered in Italy, although the increase in the respective headline index failed to reverse fully the deterioration the previous month. German sentiment was very slightly improved too, reaching the highest level so far this year. However, France and Spain posted declines, the former to an eleven-month low. Overall, however, the Commission's survey provides further evidence that the ECB has no cause to panic about economic conditions.

### German inflation moves higher

Today also brought the first indication of inflation in July with the preliminary figures from Germany, which provided an upside surprise as the EU-harmonised CPI measure rose 0.2ppt to a six-month high of 0.4%Y/Y. The limited detail available so far on the national measure suggested that the upside surprise came from food inflation, which jumped 1ppt to 1.1%Y/Y while other components were little changed. We expect the equivalent flash euro area headline figure, due tomorrow, to post a smaller rise of 0.1ppt to 0.2%Y/Y, also nevertheless a six-month high with the risks additionally now to the upside, and the euro area core measure to remain at 0.9%Y/Y. Looking ahead, we still expect inflation in the euro area to rise gradually to about 1%Y/Y around the turn of the year, with inflation in Germany possibly set to advance a touch further. Indeed, if a significant upside surprise to inflation above our baseline forecast is going to emerge from anywhere in the euro area it will come from Germany.

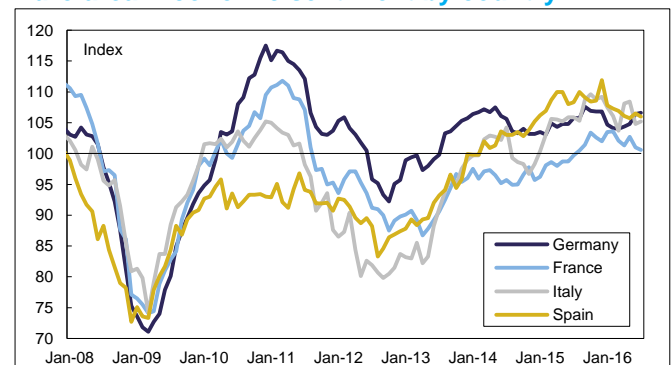
### Euro area: Economic sentiment by sector\*



\*European Commission Economic Sentiment Index.

Source: Thomson Reuters and Daiwa Capital Markets Europe Ltd.

### Euro area: Economic sentiment by country\*



\*European Commission Economic Sentiment Index.

Source: Thomson Reuters and Daiwa Capital Markets Europe Ltd.



Certainly, the country's labour market looks tight, with other data today confirming a further drop in the level of unemployment to a new post-reunification low below 2.7mn, leaving the rate unchanged at the series low of 6.1% on the national measure. Indeed, with business economy labour costs recently rising more than 3%Y/Y, 1.5ppts above the euro area average, Germany currently appears the only member state capable of generating inflation close to the ECB's target over the medium term. However, with prices of services in July up just 1.4%Y/Y, the same as in June, and prices of non-energy goods down 0.7%Y/Y, there is little evidence so far of higher wages feeding through into core inflation in Germany in any meaningful way.

## The day ahead in the euro area and US

The week in the euro area is set to come to an end with the preliminary estimates of Q2 GDP and July inflation. We expect euro area GDP growth to have slowed to 0.3%Q/Q albeit with risks to the downside, while the equivalent figures for France and Spain – the only large member states to publish the figures tomorrow – are also likely to show a slowdown, to 0.2%Q/Q and 0.7%Q/Q respectively. In addition, following today's flash German figure, we maintain our forecast for euro area inflation to have edged up to a six-month high of 0.2%Y/Y albeit with the risks now skewed to the upside, while the French number, also due tomorrow, is expected similarly to rise 0.1ppt to 0.4%Y/Y. German retail sales and French consumer spending data, both for June, are also due. In addition, the EBA is scheduled to publish the results of its stress tests of 53 banks from across the EU, including 39 from the euro area.

Friday will also bring the advance US GDP estimate for Q2. Expectations are for growth to have accelerated to an annualised rate of about 2½%Q/Q, driven principally by private consumption, which would represent the firmest rate for a year. Also due are the Chicago PMI and final University of Michigan consumer confidence survey results, both for July.

## UK

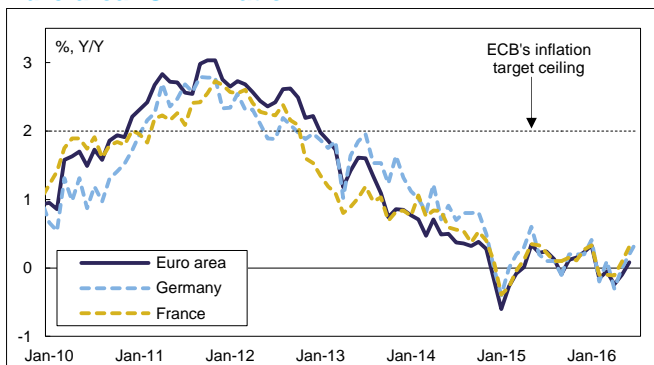
### House prices up, but probably not for long

Today was relatively quiet in the UK although the latest Nationwide house price figures provided the first actual residential property price data since the referendum. The figures surprised on the upside, with house prices up 0.5%M/M in July to take the annual rate to a four-month high of 5.2%Y/Y. But given the lags involved in the sale process, and particularly the fact that the Nationwide data are taken from the mortgage offer stage, these figures do not give a reliable guide to post-referendum conditions. Indeed, the RICS Residential Market Survey released a fortnight ago made clear that the outlook for the housing market has deteriorated significantly. Brexit uncertainty reportedly saw new buyer enquiries fall sharply to the lowest level since mid-2008, while agreed sales also fell sharply after the vote and were expected to decline further. And house prices were expected to fall across the country over the coming few months and, in particular, to be lower in London and eastern England in twelve months' time. So, we expect to see the Nationwide indices – and the other official ONS and Halifax house price measures – to turn south very soon.

### The day ahead in the UK

In the UK, Friday brings the July GfK consumer confidence and Lloyds Business Barometer surveys. Both surveys provided early indications of a marked deterioration in sentiment following the UK referendum, while the Commission's consumer confidence index for the UK released today fell by the most in more than twenty-five years to a three-year low. Also due are BoE bank lending figures for June for which the equivalent BBA figures earlier this week showed a drop in mortgage approvals to the lowest level in fifteen months and a decline in lending to UK businesses for the first time this year.

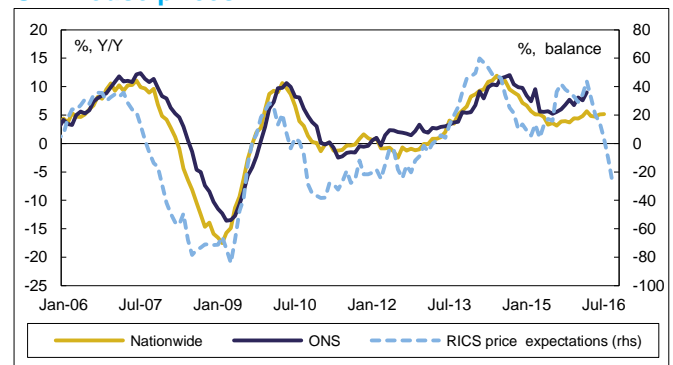
### Euro area: CPI inflation\*



\*German flash estimate for July 2016.

Source: Thomson Reuters and Daiwa Capital Markets Europe Ltd.

### UK: House prices\*










\*Nationwide and ONS house price indices and RICS house price near-term expectations index with three-month lead.

Source: Thomson Reuters and Daiwa Capital Markets Europe Ltd.




## European calendar

### Today's results

#### Economic data

Country	Release	Period	Actual	Market consensus/ <i>Daiwa forecast</i>	Previous	Revised
EMU	 Economic sentiment indicator	Jul	<b>104.6</b>	103.5	104.4	-
	 Services (industrial) sentiment	Jul	<b>11.1 (-2.4)</b>	10.3 (-3.3)	10.8 (-2.8)	<b>10.9 (-)</b>
	 Final consumer confidence	Jul	<b>-7.9</b>	-7.9	-7.2	-
Germany	 Unemployment change `000s (rate %)	Jul	<b>-7.0 (6.1)</b>	-4.0 (6.1)	-6.0 (6.1)	-
	 Preliminary EU-harmonised CPI Y/Y%	Jul	<b>0.4</b>	0.3	0.2	-
Spain	 Unemployment rate %	Q2	<b>20.0</b>	20.3	21.0	-
UK	 Nationwide house price index M/M% (Y/Y%)	Jul	<b>0.5 (5.2)</b>	0.0 (4.5)	0.2 (5.1)	-

















#### Auctions

Country	Auction
Italy sold	 €2bn of 0.45% 2021 bonds (01-Jun-2021) at an average yield of 0.26%
	 €4.5bn of 1.25% 2026 bonds (01-Dec-2026) at an average yield of 1.24%
	 €2bn of floating-rate 2023 bonds (15-Jul-2023) at an average yield of 0.38%

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

### Tomorrow's data releases

#### Economic data

Country	BST	Release	Period	Market consensus/ <i>Daiwa forecast</i>	Previous
EMU	10:00	 GDP – preliminary release Q/Q% (Y/Y%)	Q2	<u>0.3 (1.5)</u>	0.6 (1.7)
	10:00	 Flash CPI estimate Y/Y%	Jul	<u>0.2</u>	0.1
	10:00	 Flash core CPI estimate Y/Y%	Jul	<u>0.9</u>	0.9
	10:00	 Unemployment rate %	Jun	10.1	10.1
Germany	07:00	 Retail sales M/M% (Y/Y%)	Jun	0.1 (1.5)	0.7 (2.6)
France	06:30	 GDP – preliminary release Q/Q% (Y/Y%)	Q2	<u>0.2 (1.6)</u>	0.6 (1.3)
	07:45	 Preliminary EU-harmonised CPI Y/Y%	Jul	0.4	0.3
	07:45	 Consumer spending M/M% (Y/Y%)	Jun	0.2 (2.0)	-0.7 (2.2)
Italy	09:00	 Unemployment rate %	Jun	11.4	11.5
	10:00	 Preliminary EU-harmonised CPI Y/Y%	Jul	-0.2	-0.2
Spain	08:00	 GDP – preliminary release Q/Q% (Y/Y%)	Q2	<u>0.7 (3.1)</u>	0.8 (3.4)
	08:00	 Preliminary EU-harmonised CPI Y/Y%	Jul	-0.8	-0.9
	09:00	 Current account balance €bn	May	-	2.6
UK	00:05	 GfK consumer confidence survey	Jul	-8	-1
	09:30	 Net consumer credit (net lending secured on dwellings) £bn	Jun	1.4 (2.7)	1.5 (2.8)
	09:30	 Mortgage approvals `000s	Jun	65.5	67.0

#### Auctions and events

Country	BST	Auction / Event
- Nothing scheduled -		

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

Access our research blog at:  
<http://www.uk.daiwacm.com/research-zone/research-blog>



Follow us  
[@DaiwaEurope](https://twitter.com/DaiwaEurope)

This research report is produced by Daiwa Securities Co. Ltd., and/or its affiliates and is distributed by Daiwa Capital Markets Europe Limited in the European Union, Iceland, Liechtenstein, Norway and Switzerland. Daiwa Capital Markets Europe Limited is authorised and regulated by The Financial Conduct Authority and is a member of the London Stock Exchange and Eurex Exchange. Daiwa Capital Markets Europe Limited and its affiliates may, from time to time, to the extent permitted by law, participate or invest in other financing transactions with the issuers of the securities referred to herein (the "Securities"), perform services for or solicit business from such issuers, and/or have a position or effect transactions in the Securities or options thereof and/or may have acted as an underwriter during the past twelve months for the issuer of such securities. In addition, employees of Daiwa Capital Markets Europe Limited and its affiliates may have positions and effect transactions in such securities or options and may serve as Directors of such issuers. Daiwa Capital Markets Europe Limited may, to the extent permitted by applicable UK law and other applicable law or regulation, effect transactions in the Securities before this material is published to recipients.

This publication is intended for investors who are not Retail Clients in the United Kingdom within the meaning of the Rules of the FCA and should not therefore be distributed to such Retail Clients in the United Kingdom. Should you enter into investment business with Daiwa Capital Markets Europe's affiliates outside the United Kingdom, we are obliged to advise that the protection afforded by the United Kingdom regulatory system may not apply; in particular, the benefits of the Financial Services Compensation Scheme may not be available.

Daiwa Capital Markets Europe Limited has in place organisational arrangements for the prevention and avoidance of conflicts of interest. Our conflict management policy is available at <http://www.uk.daiwacm.com/about-us/corporate-governance-regulatory>. Regulatory disclosures of investment banking relationships are available at <https://daiwa3.bluematrix.com/sellside/Disclosures.action>.