

# Euro wrap-up

## Overview

- Bunds were little changed as euro area GDP growth was unrevised at 0.3%Q/Q, while there was a modest upward surprise to German Q2 GDP.
- Gilts made gains as UK construction output fell more than expected.
- The coming week brings final euro area CPI for July and the ECB account of its July Governing Council meeting. In the UK, July inflation and retail sales figures will be the first hard data covering the post-Brexit vote period.

**Emily Nicol**

+44 20 7597 8331

**Mantas Vanagas**

+44 20 7597 8318

### Daily bond market movements

Bond	Yield	Change*
BKO 0 09/18	-0.626	+0.004
OBL 0 10/21	-0.549	-0.007
DBR 0 08/26	-0.111	-0.017
UKT 1¼ 07/18	0.129	-0.022
UKT 1½ 01/21	0.159	-0.024
UKT 2 09/25	0.509	-0.029

\*Change from close as at 4.00pm BST.

Source: Bloomberg

## Euro area

### Euro area Q2 GDP growth confirmed at 0.3%Q/Q

Today's second release of euro area GDP data for Q2 saw growth confirmed at 0.3%Q/Q, half the rate seen in Q1 but still broadly in line with the average of the recovery so far to leave output up 1.6% compared with a year earlier. And while there is still no detailed breakdown, the national data suggest that net trade provided a positive contribution for the first quarter in four, while household and government consumption likely supported growth too. Among member states, there was a modest upwards surprise to the preliminary release of German GDP, although growth still moderated from 0.7%Q/Q in Q1 to 0.4%Q/Q, with the weakness principally due to fixed investment, not least a notable decline in construction output after rapid growth in the previous two quarters. Spain's growth of 0.7%Q/Q means that it remained the strongest growing of the larger member states, while the Netherlands economy performed better than expected, recording growth of 0.6%Q/Q for the second successive quarter. And Greece posted growth of 0.3%Q/Q, following a smaller-than-initially-estimated contraction (revised by 0.4ppt to -0.1%Q/Q) in Q1. In contrast, French and Italian GDP were disappointingly flat in Q2, while Portugal continued to expand only moderately (0.2%Q/Q).

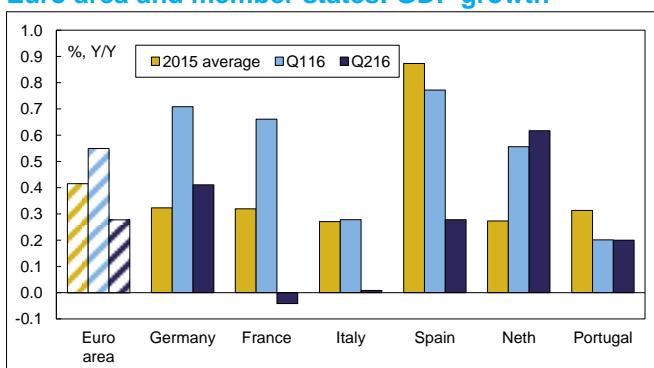
### Despite rising in June, IP declines in Q2

Today also brought a modest upwards surprise to euro area industrial production in June. Despite weakness in France, Italy and Spain, but consistent with solid growth in German IP that month, aggregate industrial output rose 0.6%M/M to leave it 0.4% higher compared with a year earlier. And in the absence of the decline in energy production (-0.7%M/M) the increase would have been stronger with manufacturing output up 0.8%M/M, supported by solid growth in production of capital and consumer goods (1.3%M/M and 0.9%M/M respectively). However, this was not strong enough to fully reverse the decline in May and over the second quarter as a whole manufacturing output was down ½%Q/Q, the first quarterly contraction since Q314. So while the industrial sector accounts for roughly a quarter of GDP, today's release suggests that the sector was a modest drag on the economy in Q2 for just the second quarter in the past 3½ years. Recent surveys, however, suggest that manufacturing confidence improved in July – the Commission's indicator rose to its firmest level for the year – and that overall growth momentum was steady at the start of the third quarter. Indeed, we expect euro area GDP growth to remain stable at 0.3%Q/Q in Q3, with Germany and France a touch firmer than in Q2 but Spain a touch softer.

### Euro area inflation in July might well be revised lower

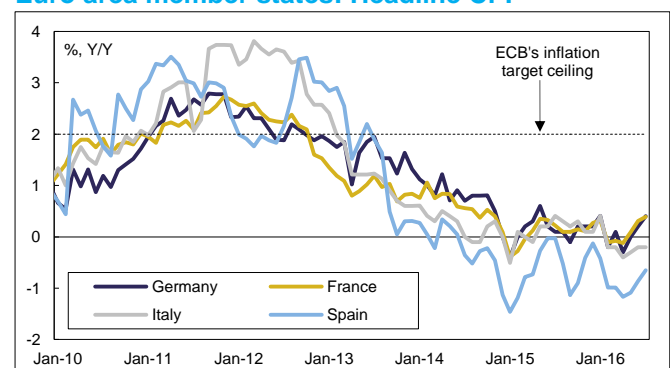
Finally, the flash estimate of July inflation on the EU-harmonised measure in Germany, up 0.3ppt to a six-month high of 0.4%Y/Y, was confirmed today. And this was the same with the French figures, which yesterday confirmed that CPI on an

### Euro area and member states: GDP growth



Source: Thomson Reuters and Daiwa Capital Markets Europe Ltd.

### Euro area member states: Headline CPI\*



\*EU-harmonised measure. Source: Thomson Reuters and Daiwa Capital Markets Europe Ltd.



Follow one of the WSJ's top 50 financial twitter feeds [@DaiwaEurope](https://twitter.com/DaiwaEurope)

equivalent measure rose 0.1ppt to 0.4%Y/Y, its highest since November 2014. But there were downward surprises to both the Italian and Spanish releases, which saw the harmonised headline rates both revised down 0.1ppt from the preliminary readings to -0.2%Y/Y and -0.7%Y/Y. And so, with the initial estimate of euro area CPI having risen to a low 0.2%Y/Y, when revised figures are published on Thursday, they might well see the headline rate revised down to 0.1%Y/Y to leave it unchanged from June.

## The week ahead in the euro area and US

The coming week's calendar looks set to be quieter for euro area top-tier data, with Tuesday's release of June's trade report to be followed on Thursday by balance of payments figures for the same month. Thursday also brings the aforementioned final estimate of euro area inflation for July, which might well see a modest downward revision to headline CPI, while core CPI was likely unchanged at 0.9%Y/Y. Also of interest on Thursday will be the ECB's account from its July Governing Council policy-setting meeting, which will be accompanied by euro area construction output data for June. Of the larger member states, the most noteworthy release will be the German ZEW survey of financial investors for August on Tuesday, while Italian and Spanish trade reports are due on Thursday and Friday respectively.

In the US, there are several releases of note in the coming week, including July CPI and industrial production data on Tuesday. Consumer prices are expected to have moved sideways on the month, to leave the year-on-year CPI rate edging slightly lower by 0.1ppt to 0.9%Y/Y. But excluding food and energy, prices are expected to have increased by 0.2%M/M, which would leave the annual core CPI rate unchanged at 2.3%Y/Y. The minutes from the FOMC's end-July meeting will be the most noteworthy release on Wednesday and will be analysed for further insights into the likelihood of a rate hike in September. Wednesday also sees FOMC voting member Bullard speak at conference, while Dudley will speak publicly on Thursday. Meanwhile, non-voting members Lockhart and Williams are due to speak on Tuesday and Thursday respectively. Meanwhile, other data due the coming week include the latest NAHB housing index, capital inflows data and the Empire Manufacturing index (Monday), housing starts figures (Tuesday) and the Philly Fed and Conference Board's leading indices (Thursday). Supply-wise, the Treasury will sell 5Y TIPS on Thursday.

## UK

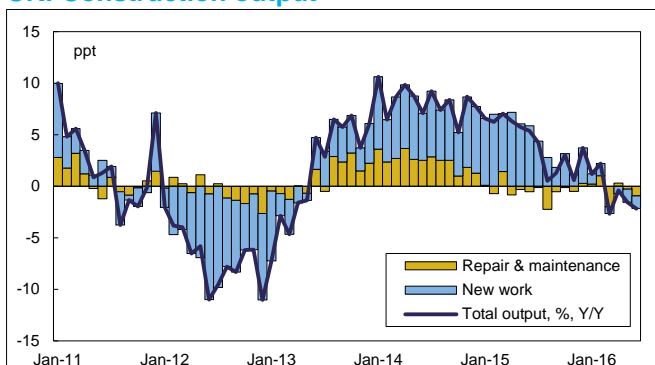
### Construction sector was a drag on GDP growth in Q2

While the construction sector provided a welcome source of support to GDP growth in the early stages of the recovery – with particularly vigorous growth in 2013 and 2014 leaving output in the sector up 16% – it has lost steam over recent quarters. And today's figures confirmed that even ahead of the vote to leave the EU output fell by a further 0.9%M/M in June, recording the fifth monthly decline this year, to leave output down 2.2%Y/Y, the second fastest rate of decline since mid-2013. Although the monthly change was broadly in line with the pace assumed in the preliminary GDP estimate, which suggested a contraction in construction output of 0.4%Q/Q in Q2, today's figures implied a slightly larger decline of 0.7%Q/Q that quarter. Nevertheless, the ONS suggested this would have only a very marginal impact on GDP (0.02ppt). Looking ahead, with storm clouds now gathering over the commercial real estate and housing sectors, the downward trend in construction output growth looks set to continue over coming quarters.

### Housing market is going downhill

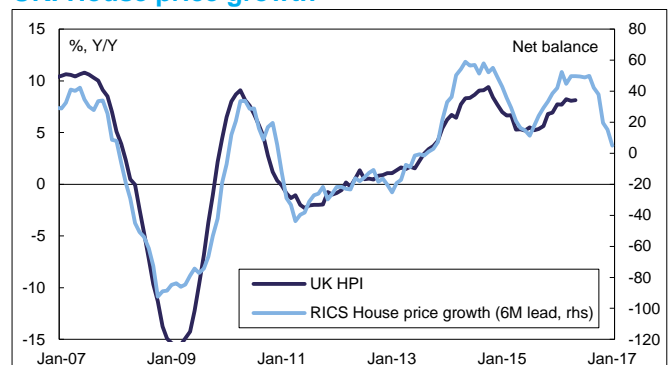
Indeed, yesterday's release of the RICS Residential Market survey provided further evidence that momentum in the housing market is deteriorating rapidly. The previous months' survey, which was conducted in the immediate aftermath of the EU referendum, saw a sharp drop in the balance of agents and surveyors seeing house price increases falling to 15, the lowest

#### UK: Construction output



Source: ONS, Thomson Reuters and Daiwa Capital Markets Europe Ltd.

#### UK: House price growth



Source: ONS, RICS, Thomson Reuters and Daiwa Capital Markets Europe Ltd.








level since the start of 2015. And yesterday's survey for July extended that trend as the price index fell to 5, a level not seen for three years. Continuing weakness on both sides of the market was reported, with the relevant new buyer enquiries and new vendor instructions indices remaining firmly below zero. So it was inevitable that transaction levels decreased for a fourth consecutive month. There were, however, some marginally encouraging developments in the forward-looking indicators. For example, although near-term price expectations remained negative, the pace of decline eased notably. And looking twelve months ahead, the relevant indicator increased from 0 in the previous month to 23, albeit remaining significantly below its recent average. But these are based on surveyor's expectations of price movements, not activity itself, and it remains to be seen whether those expectations prove overly-optimistic against a backdrop of what the rest of the survey suggests is a rapidly cooling housing market.

## The week ahead in the UK

In a week full of major economic data releases, focus will be on July inflation and retail sales figures, on Tuesday and Thursday respectively, which will provide the first hard evidence since the Brexit vote. While headline inflation is expected to have moved sideways at 0.5%Y/Y, we might see the core rate inch down from 1.4%Y/Y recorded in June. But this subdued outturn looks set to prove temporary, with survey evidence overwhelmingly suggesting a significant jump in input prices on the back of recent sterling depreciation. With regard to the retail sector figures, recent surveys provided mixed results about the Brexit impact on High Street sales. Market consensus is for a small increase on a month, following a much steeper pace of decline in June. But even if sales fall by a few tenths, the annual pace of growth should remain at a relatively high level close to 4%Y/Y. Meanwhile, Wednesday's release of labour market data for June will also be worth watching. Having increased by the largest margin in two years in the previous month, employment is likely to have been broadly stable in June, to leave headline three-month employment growth at around 130k, down from 176k previously. And while the headline unemployment rate is expected to be unchanged at 4.9%, average earnings growth looks set to have inched slightly higher to reach a nine-month high of around 2½%Y/Y. Other new economic data in the coming week include the House Price Index on Tuesday and Friday's release of public finance figures for July.

*The next edition of Euro wrap-up will be published on 16 August 2016.*





## European calendar

Today's results						
Economic data						
Country	Release	Period	Actual	Market consensus/ <i>Daiwa forecast</i>	Previous	Revised
EMU	 Industrial production M/M% (Y/Y%)	Jun	<b>0.6 (0.4)</b>	0.5 (0.7)	-1.2 (0.5)	<b>-1.2 (0.3)</b>
	 GDP – second release Q/Q% (Y/Y%)	Q2	<b>0.3 (1.6)</b>	<u>0.3 (1.6)</u>	0.6 (1.7)	-
Germany	 Final EU-harmonised CPI Y/Y%	Jul	<b>0.4</b>	<u>0.4</u>	0.2	-
	 GDP – preliminary release Q/Q% (Y/Y%)	Q2	<b>0.4 (1.8)</b>	<u>0.3 (1.5)</u>	0.7 (1.6)	<b>- (1.9)</b>
Italy	 GDP – preliminary release Q/Q% (Y/Y%)	Q2	<b>0.0 (0.7)</b>	<u>0.1 (0.7)</u>	0.3 (1.0)	-
Spain	 Final EU-harmonised CPI Y/Y%	Jul	<b>-0.7</b>	<u>-0.6</u>	-0.9	-
UK	 Construction output M/M% (Y/Y%)	Jun	<b>-0.9 (-2.2)</b>	-1.0 (-2.1)	-2.1 (-1.9)	<b>-2.0 (-1.6)</b>
Auctions						
Country	Auction					
- Nothing to report -						


Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

## Yesterday's results

## Economic data

Country	Release	Period	Actual	Market consensus/ Daiwa forecast	Previous	Revised
France	 Final EU-harmonised CPI Y/Y%	Jul	0.4	0.4	0.3	-
Italy	 Final EU-harmonised CPI Y/Y%	Jul	-0.2	-0.1	-0.2	-
	 Trade balance €bn	Jun	4.7	-	5.0	-
UK	 RICS house price balance %	Jul	5	6	16	15




















## Auctions

Country	Auction
UK sold	 £850mn of 0.125% 2036 index-linked bonds (22-Nov-2036) at an average yield of -1.722%

Source: Bloomberg and Daiwa Capital Markets Europe Ltd



## Coming week's data calendar

## Key data releases

Country	BST	Release	Period	Market consensus/ Daiwa forecast	Previous
<b>Monday 15 August 2016</b>					
EMU	 14:45	ECB QE net purchases €bn	Weekly	14.0	12.4
UK	 00:01	Rightmove house price index M/M% (Y/Y%)	Aug	-	-0.9 (4.5)
<b>Tuesday 16 August 2016</b>					
EMU	 10:00	Trade balance €bn	Jun	25.5	24.5
Germany	 10:00	ZEW current assessment balance (expectations)	Aug	50.1 (2.5)	49.8 (-6.8)
UK	 09:30	CPI (core) Y/Y%	Jul	0.5 (1.3)	0.5 (1.4)
	 09:30	House Price Index Y/Y%	Jun	-	8.1
<b>Wednesday 17 August 2016</b>					
UK	 09:30	Average earnings incl. bonuses (excl. bonuses) 3M/Y%	Jun	2.4 (2.3)	2.3 (2.2)
	 09:30	ILO unemployment rate 3M%	Jun	4.9	4.9
	 09:30	Employment change 3M/3M '000s	Jun	135	176
	 09:30	Claimant count rate % (change 000s)	Jul	2.2 (9.0)	2.2 (0.4)
<b>Thursday 18 August 2016</b>					
EMU	 09:00	Current account balance €bn	Jun	-	30.8
	 10:00	Construction output M/M% (Y/Y%)	Jun	-	-0.5 (-0.8)
	 10:00	Final CPI (core) Y/Y%	Jul	0.2 (0.9)	0.1 (0.9)
France	 06:30	Unemployment rate %	Q2	10.1	10.2
Italy	 09:30	Current account balance €bn	Jun	-	3.2
UK	 09:30	Retail sales excluding petrol M/M% (Y/Y%)	Jul	0.3 (3.8)	-0.9 (3.9)
	 09:30	Retail sales including petrol M/M% (Y/Y%)	Jul	0.1 (4.2)	-0.9 (4.3)
<b>Friday 19 August 2016</b>					
Spain	 09:00	Trade balance €bn	Jun	-	-0.9
UK	 09:30	Public sector net borrowing excluding interventions £bn	Jul	-1.4	7.8

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

## Coming week's events/auctions calendar

Key events & auctions			
Country	BST	Event / Auction	
<b>Monday 15 August 2016</b>			
- Nothing scheduled -			
<b>Tuesday 16 August 2016</b>			
- Nothing scheduled -			
<b>Wednesday 17 August 2016</b>			
UK		10:30	Auction: To sell £1.25bn of 4.25% 2055 bonds (7-Dec-2055)
<b>Thursday 18 August 2016</b>			
EMU		12:30	ECB publishes account of the monetary policy meeting held on 20-21 July
<b>Friday 19 August 2016</b>			
- 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/Dislosures.action>.