

# Euro wrap-up

## Overview

- Bunds made gains as the ECB account highlighted ongoing concerns about the lack of underlying inflationary pressures.
- Gilts made modest gains despite an upward surprise to UK retail sales growth in July.
- After a relatively quiet day for economic news tomorrow, the coming week brings flash PMIs for August and revised Q2 GDP data from Germany, France, Spain and the UK.

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### Daily bond market movements

Bond	Yield	Change*
BKO 0 09/18	-0.622	-0.005
OBL 0 10/21	-0.523	-0.019
DBR 0 08/26	-0.082	-0.032
UKT 1¼ 07/18	0.138	-0.012
UKT 1½ 01/21	0.194	-0.010
UKT 2 09/25	0.549	-0.014

\*Change from close as at 4.30pm BST.

Source: Bloomberg

## Euro area

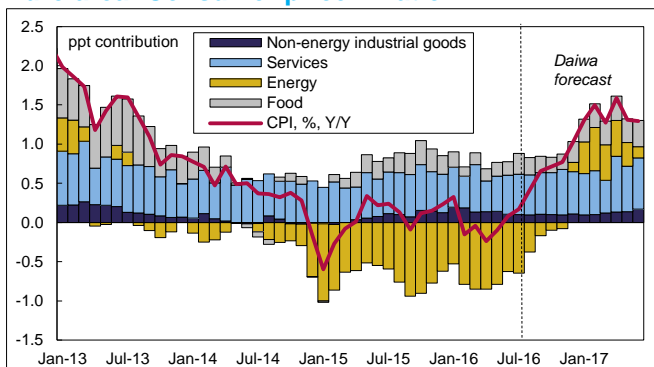
### ECB account acknowledges downside risks

With the ECB's next policy-setting meeting in just three weeks' time, the focus today was on the account of the July Governing Council meeting. While the account noted that financial markets had weathered the initial volatility in the aftermath of the shock Brexit vote with encouraging resistance, members also acknowledged that the vote represented a materialisation of a downside risk, offsetting the improvement in the balance of risks assumed by policymakers at the start June. The Governing Council had however wanted more time to assess the impact of this downside risk before committing to ease policy further, not least as waiting would allow it to refer to its updated economic forecasts. Recent economic sentiment surveys have perhaps been a touch stronger so far in Q3, and so the ECB's forecast might be little changed from the set produced in June. Nevertheless, having also continued to express in the account concern about the continued lack of convincing upward pressures on underlying prices, we would expect the ECB to still forecast inflation to remain well below its 2% target over coming years. So, in a bid to avoid an unhelpful tightening of financial conditions over coming quarters, on balance we expect the ECB to announce in September an extension of its QE programme by a further six months to September 2017. And although the account showed that members concluded that the programme was proceeding smoothly, with a little more than €1.5bn of government, supranational and agency bonds currently ineligible for the ECB to purchase because their yields are below the -0.4% floor, we might well also see Draghi announce revisions to the rules of the programme to ensure its QE targets are deliverable.

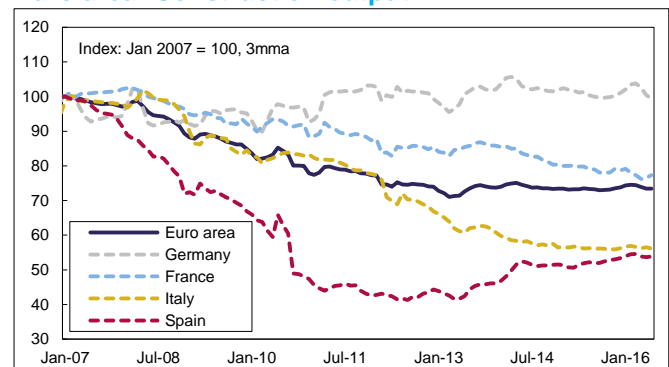
### Euro area CPI confirmed at six-month high

With respect to the latest data, there were no surprises from the handful of new releases, with most notably the final headline numbers for euro area inflation in July unchanged from the flash estimates. Headline CPI was confirmed to have increased by 0.1ppt to 0.2%Y/Y, the highest level since January as food price inflation rose to an eight-month high of 1.4%Y/Y. This was partly offset by a steeper pace of decline in energy prices (down 0.3ppt to -6.7%Y/Y), while non-energy industrial goods inflation remained subdued at 0.4%Y/Y, and services inflation edged only slightly higher by 0.1ppt to 1.2%Y/Y. So, core CPI remained unchanged at 0.9%Y/Y, consistent with a continued absence of meaningful price pressure. As the impact of past declines in energy prices eventually wears off, we expect headline CPI to rise to 1%Y/Y by year-end. But given the subdued growth outlook, we also expect inflation to remain on average below 1.5%Y/Y in 2017.

### Euro area: Consumer price inflation



### Euro area: Construction output



## Euro area construction a drag on GDP growth in Q2

Today's construction output figures, meanwhile, confirmed that the sector moved broadly sideways at the end of Q2. Output was unchanged in both May and June (with the former revised up from an initial decline of ½%M/M). But while there was only a modest decline in April (-0.1%M/M) due to the recent monthly profile, this left construction output down more than 1% over the second quarter as a whole, the first quarterly decline in three and the steepest since Q113. And the weakness reflected a notable decline in building work, down 1½%Q/Q, similarly the sharpest drop for more than three years. So, with industrial output having also contracted by almost ½%Q/Q last quarter, today's data confirm that services once again more than fully accounted for the 0.3%Q/Q overall expansion in Q2. Among the larger member states that have released figures, there was a notable decline in construction output in Germany in Q2, down more than 4%Q/Q, more than fully offsetting the pickup at the start of the year. Meanwhile, Spanish construction was down almost 1½%Q/Q, following growth of almost 2½%Q/Q previously. And although French construction was little changed in Q2, this followed a decline of more than 1½%Q/Q in Q1.

## The week ahead in the euro area and US

The coming week's data calendar will be dominated by August sentiment surveys, kicking off on Tuesday with the flash PMIs and the Commission's consumer confidence indicator. These indices are likely to report that conditions continued to hold up relatively well in the middle of Q3, with most notably the euro area composite PMI expected to signal that the economic expansion in the current quarter was maintained at a similar pace to the 0.3%Q/Q recorded in Q2. Meanwhile, the second release of German Q2 GDP is due on Wednesday. Growth is expected to be confirmed at 0.4%Q/Q, down from 0.7%Q/Q in Q1, with the first official expenditure breakdown likely to show that net trade provided a notable positive contribution, while fixed investment was a drag on growth. This will be followed on Thursday by the German IFO survey for August, which will be accompanied by the French INSEE business sentiment survey for the same month. Friday, meanwhile, brings the latest German and French consumer confidence indicators for August, as well as revised French Q2 GDP figures and the ECB's monthly lending data for July. On the supply side, German will sell 2021 Bunds on Wednesday.

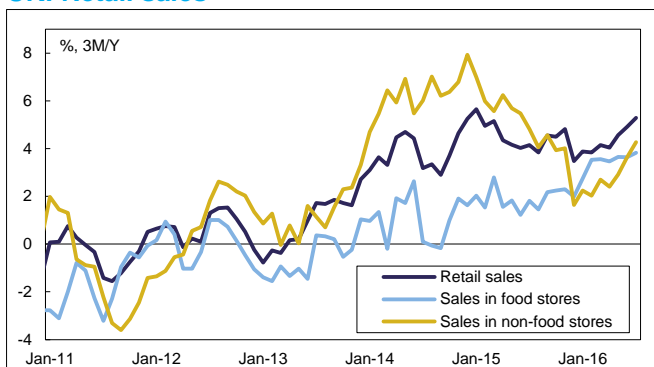
In the US, the data focus in the coming week will be revised Q2 GDP on Friday, which is expected to confirm that growth was little changed from the 1.2%Q/Q annualised rate initially estimated. This will be accompanied by the advance goods trade report for July. But most attention at the end of the week will be on Yellen's speech at the Jackson Hole symposium, with the three-day event getting underway on Thursday evening. Other releases of note include the Chicago Fed national activity index (Monday), new home sales figures (Tuesday), existing homes sales numbers and the FHFA home price index (Wednesday) and durable goods orders (Thursday). Supply-wise, the Treasury will sell 2Y notes on Tuesday, 2Y FRNs and 5Y notes on Wednesday and 7Y notes on Thursday.

## UK

### Retail sales rise after Brexit vote

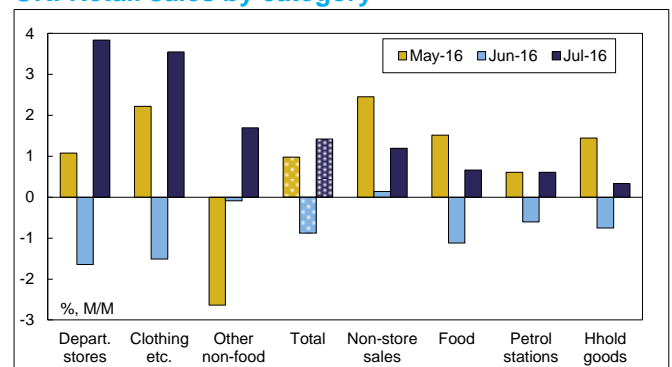
In marked contrast to most major survey data, which have pointed to a sharp fall in economic sentiment and activity following the Brexit vote, today's hard figures from the retail sector showed a rise in sales in July. Sales volumes increased by 1.4%M/M to leave annual growth rising to 5.9%, its highest level since last September. Sales were strong across the board, but growth was mostly driven by department store and clothing categories, which reported an increase of 3.9%M/M and 3.5%M/M respectively. Overall, today's figures give some hope that a downward adjustment to the economy after the Brexit vote will not be as severe as some are expecting. Indeed, given the recent monthly profile, it will take falls in excess of 1%M/M in both August and September to leave retail sales down over the third quarter as a whole.

### UK: Retail sales



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

### UK: Retail sales by category



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








However, there are reasons to believe that today's figures do not fully represent consumers' mood after the referendum. First, the increase in July came after a significant fall of 0.9%M/M in the previous month. And with prices down by 1.0%M/M (auto fuel excluded), seasonal discounting definitely played a role in boosting sales volume, as probably did the final arrival of warmer weather. Given that consumers have become more accustomed to waiting for price reductions, some of the spending in July may well have been pre-planned. Meanwhile, from the BoE's perspective, today's figures probably do not alter its economic outlook assessment, given that it did not lower its forecast for household spending growth this year. So even if household spending does not falter much over coming months, the MPC will remain prepared to cut rates further given its commitment to do so provided the economy pans out as its forecasts expect.

## The week ahead in the UK



The end of a busy week for new economic data in the UK tomorrow brings the release of July public finance figures. Meanwhile, the coming week looks set to be quieter. Most notably, the second release of Q2 GDP, which is likely to confirm the flash estimate of 0.6%Q/Q growth, is due on Friday. The expenditure breakdown will probably show that household spending remained strong and was the main driver of growth, while net trade provided no support. Among other new economic data in the coming week are two CBI surveys – the Industrial Trends is due on Tuesday and the Distributive Trade is out on Thursday – and the BBA data from High Street banks out on Wednesday.

*The next edition of Euro wrap-up will be published on 23 August 2016.*

## European calendar
























Today's results						
Economic data						
Country	Release	Period	Actual	Market consensus/ Daiwa forecast	Previous	Revised
EMU	 Current account balance €bn	Jun	<b>28.2</b>	-	30.8	<b>31.8</b>
	 Construction output M/M% (Y/Y%)	Jun	<b>0.0 (0.6)</b>	-	-0.5 (-0.8)	<b>0.0 (-0.4)</b>
	 Final CPI (core) Y/Y%	Jul	<b>0.2 (0.9)</b>	<u>0.2 (0.9)</u>	0.1 (0.9)	-
France	 Unemployment rate %	Q2	<b>9.9</b>	10.1	10.2	-
Italy	 Current account balance €bn	Jun	<b>7.2</b>	-	3.2	-
UK	 Retail sales excluding petrol M/M% (Y/Y%)	Jul	<b>1.5 (5.4)</b>	0.3 (3.9)	-0.9 (3.9)	-
	 Retail sales including petrol M/M% (Y/Y%)	Jul	<b>1.4 (5.9)</b>	0.1 (4.2)	-0.9 (4.3)	-
Auctions						
Country	Auction					
- Nothing to report -						

*Source: Bloomberg and Daiwa Capital Markets Europe Ltd.*

Tomorrow's data releases						
Economic data						
Country	BST	Release	Period	Market consensus/ Daiwa forecast	Previous	
Spain	 09:00	Trade balance €bn	Jun	-	-0.9	
UK	 09:30	Public sector net borrowing excluding interventions £bn	Jul	-1.9	7.8	
Country	BST	Auction / Event				
- Nothing scheduled -						

*Source: Bloomberg and Daiwa Capital Markets Europe Ltd.*

## Coming week's data calendar

Key data releases						
Country	BST	Release	Period	Market consensus/ <i>Daiwa forecast</i>	Previous	
<b>Monday 22 August 2016</b>						
EMU		14:45 ECB QE net purchases €bn	Weekly	<u>13.0</u>	11.4	
<b>Tuesday 23 August 2016</b>						
EMU		09:00 Preliminary manufacturing PMI	Aug	-	52.0	
		09:00 Preliminary services PMI (preliminary composite PMI)	Aug	-	52.9 (53.2)	
		15:00 Preliminary consumer confidence	Aug	-	-7.9	
Germany		08:30 Preliminary manufacturing PMI	Aug	-	53.8	
		08:30 Preliminary services PMI (preliminary composite PMI)	Aug	-	54.4 (55.3)	
France		08:00 Preliminary manufacturing PMI	Aug	-	48.6	
		08:00 Preliminary services PMI (preliminary composite PMI)	Aug	-	50.5 (50.1)	
UK		11:00 CBI Industrial Trends survey, total orders	Aug	-	-4	
<b>Wednesday 24 August 2016</b>						
Germany		07:00 GDP – second release Q/Q% (Y/Y%)	Q2	<u>0.4 (1.8)</u>	0.7 (1.9)	
UK		09:30 BBA loans for house purchase 000s	Jul	-	40.1	
<b>Thursday 25 August 2016</b>						
Germany		09:00 Ifo business climate index	Aug	-	108.3	
		09:00 Ifo current assessment balance (expectations)	Aug	-	114.7 (102.2)	
France		07:45 Business confidence indicator (production outlook)	Aug	-	102 (3)	
Spain		08:00 GDP – second release Q/Q% (Y/Y%)	Q2	<u>0.7 (3.2)</u>	0.8 (3.4)	
UK		11:00 CBI Industrial Trends survey, retail sales	Aug	-	-14	
<b>Friday 26 August 2016</b>						
EMU		09:00 M3 money supply Y/Y%	Jul	-	5.0	
Germany		07:00 GfK consumer confidence survey	Sep	-	10.0	
France		07:45 Consumer confidence survey	Aug	-	96	
		07:45 GDP – second release Q/Q% (Y/Y%)	Q2	<u>0.0 (1.4)</u>	0.7 (1.3)	
Spain		08:00 Retail sales Y/Y%	Jul	-	5.6	
UK		09:30 GDP – preliminary release Q/Q% (Y/Y%)	Q2	<u>0.6 (2.2)</u>	0.4 (2.0)	
		09:30 Index of services M/M% (3M/3M%)	Jun	-	-0.1 (0.3)	

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

## Coming week's events/auctions calendar

Key events & auctions		
Country	BST	Event / Auction
<b>Monday 22 August 2016</b>		
- Nothing scheduled -		
<b>Tuesday 23 August 2016</b>		
- Nothing scheduled -		
<b>Wednesday 24 August 2016</b>		
Germany		10:30 Auction: To sell €4bn of 0% 2021 bonds (08-Oct-2021)
<b>Thursday 25 August 2016</b>		
Global	-	Jackson Hole symposium starts
<b>Friday 26 August 2016</b>		
Italy		10:00 Auction: To sell bonds

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

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