

Euro wrap-up

Overview

- Bunds were little changed as the final euro area PMIs and the latest retail sales figures signalled stronger growth in Q2.
- Gilts also closed the day little changed, while the UK PMIs signalled a loss of economic momentum at the end of the second quarter.
- Tomorrow will bring the account from the ECB's June policy meeting, while Friday will see the release of industrial production data from Germany, France and the UK as well as trade reports from the latter two countries.

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Daily bond market movements

Bond	Yield	Change*
BKO 0 06/19	-0.601	+0.007
OBL 0 10/22	-0.144	+0.011
DBR 0¼ 02/27	0.472	-0.003
UKT 1¼ 07/19	0.311	-0.009
UKT 0½ 07/22	0.659	-0.004
UKT 4¼ 12/27	1.266	+0.019

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

Euro area

Final PMIs signal stronger growth in Q2

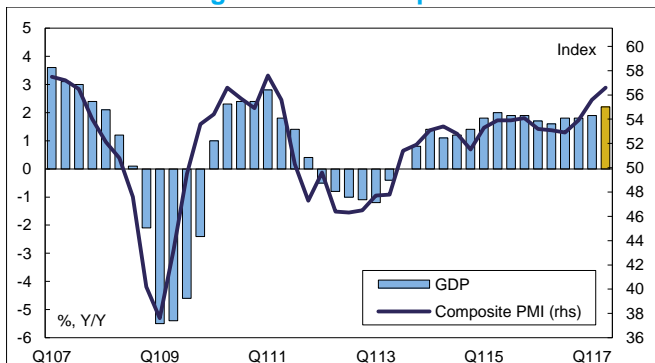
Following the mostly upward revisions to the manufacturing PMIs earlier in the week, today's final June services and composite surveys for the euro area maintained the positive news, with both indices revised notable higher from the flash estimates. Admittedly, the 0.7pt upwards revision to the services PMI was not enough to offset the initial drop, leaving the index at its lowest level since January. And so, the equivalent composite output PMI was likewise still down from May at a four-month low. However, the retreat in June came from a more than six-year high in May and, at 56.3, the index remained at the upper end of the recent trend. Furthermore, over the second quarter as a whole, the average composite PMI was 1pt higher than in Q1 at its strongest level since Q111, a level Markit consider to be consistent with GDP growth of 0.7%Q/Q, a touch above our expectation for growth to have been maintained at 0.6%Q/Q in Q2. But risks to this forecast seem skewed to the upside. And the detail of the survey – with robust orders growth and firms reportedly increasing their workforces at a rate close to the decade highs recorded earlier in the year – remained consistent with ongoing economic recovery over the near term too.

Despite being revised higher from the flash estimates, the headline indicators from Germany and France broadly mimicked the patterns seen in the euro area as a whole, with the respective headline composite PMIs falling to their lowest levels since February and April. But while the equivalent Italian index also edged lower in June, there was a notable improvement in Spain, where that country's composite PMI rose to its strongest level for almost two years. And over the second quarter as a whole, the indices for all the major member states were higher compared with Q1, pointing to a possible acceleration of GDP. But while we forecast a further pick up in German and Spanish economic growth of 0.1ppt to 0.7%Q/Q and 0.9%Q/Q respectively in Q2, we think France and Italy will match the 0.5%Q/Q and 0.4%Q/Q pace of the first quarter.

Retail sales strengthen in May

While retail sales figures for April suggested that spending on the High Street moved broadly sideways at the start of the second quarter, today's release for May signalled a bounce back that month, with sales up 0.4%M/M, to leave them more than 2½% higher than a year earlier. Admittedly, some of this strength reflected a surge in sales of fuel (1.7%M/M), while the increase in sales of non-food products (0.6%M/M) broadly offset previous weakness. But, on average in the first two months of Q2, overall retail sales were up 0.7% compared with the average in Q1. And with recent sentiment surveys suggesting that retailers considered conditions to be the most favourable since late 2015 and consumers seemingly more confident than at any other time over the past sixteen years, conditions appear to be in place for a continued steady upward trend in sales. So, we maintain optimism that private consumption will account for roughly half of GDP growth in the euro area in coming quarters.

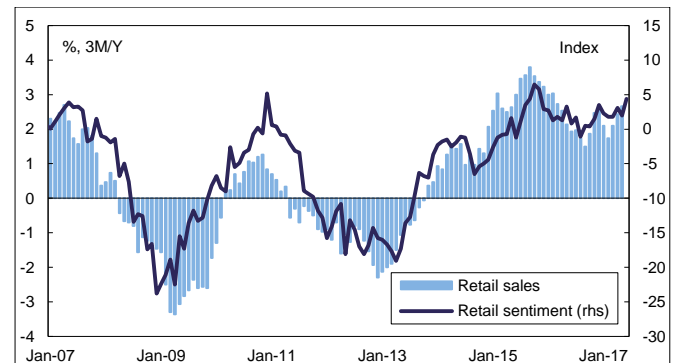
Euro area: GDP growth and composite PMI*



*Q217 GDP growth is Daiwa forecast.

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

Euro area: Retail sales and sentiment



Source: Thomson Reuters and Daiwa Capital Markets Europe Ltd.



The coming two days in the euro area and US

The focus in the euro area tomorrow will be the account from the ECB's June Governing Council meeting which will be analysed for any further insight into the likely timing of the ECB's announcement of a gradual tapering. Data-wise, tomorrow will bring German factory orders figures for May, which will be followed by that country's industrial production release on Friday. In line with the recent improvement in German manufacturing surveys, this is expected to report another month of positive output growth in the sector to leave production 4% higher than a year earlier. Friday will also bring May industrial production data from France and Spain, as well as Italian retail sales figures and French trade numbers.

In the US, meanwhile, tomorrow will bring several releases of note with the non-manufacturing ISM and Markit services PMI for June, the full trade report for May and the latest ADP employment report and weekly jobless claims. Of course, the key labour market report will come on Friday, with non-farm payrolls in June expected to have increase by around 180k bang in line with the average of the past eighteen months, to leave the unemployment rate unchanged at 4.3% its lowest level since 2001. But average hourly earnings growth is still likely to remain no stronger than the recent subdued trend. Friday will also see the Fed publish the latest Monetary Policy Report to the Congress ahead of Fed Chair Yellen's testimony on 12 July. Deputy Chair Fischer is also scheduled to speak tomorrow.

UK

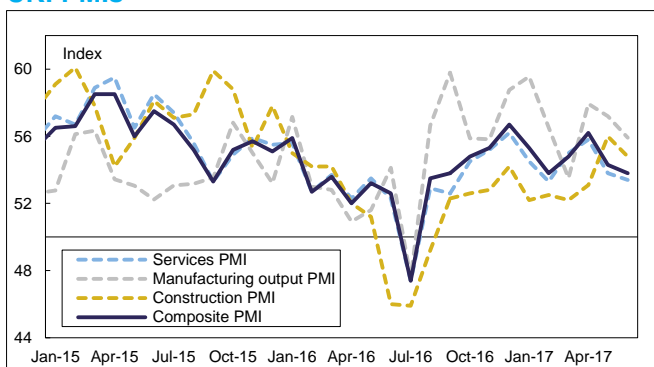
Business sentiment on a downward trend in Q2

Following the disappointing manufacturing and construction surveys earlier this week, today's services PMI completed the hat-trick of softer UK PMI readings, with the headline index falling 0.4pt in June to a four-month low of 53.8, to leave the composite PMI down from 54.3 to 53.8, the joint lowest level since last summer. While the average in the second quarter was unchanged from Q1, June's services index, down by more than 2.0pts since April, signalled that momentum in the largest sector of the economy moderated during Q2. And the survey details suggest further weakness ahead. Indeed, while the outstanding business index was little changed from the previous month, at 51.5, the new business indicator declined by 2.3pts, the steepest in almost a year, to a nine-month low of 54.1. Although the latest PMIs appear to be on the soft side, they were still consistent with an increase in GDP of 0.4%Q/Q in Q2, a slightly stronger pace than our own forecast of 0.3%Q/Q growth. With regards to inflation, the survey suggests that upward pressure on prices continued to ease last month, as the output price indicator declined to its lowest level since the wake of the Brexit referendum. And while today's BRC shop price index suggested that retail price inflation remained on an upward trend in June, the rise in the headline rate from -0.4%Y/Y to -0.3%Y/Y, its highest level for 3½ years, was admittedly modest. Food prices rose at an unchanged pace of 1.4%Y/Y, while the equivalent non-food inflation rate of -1.4%Y/Y was also little changed from the previous couple of months. But while inflationary pressures have been relatively stable over recent months, this likely reflects temporary factors, and with cost pressures continuing to build, we expect to see headline CPI inflation inching higher over coming months to above 3.0%Y/Y.

No recovery in private consumption

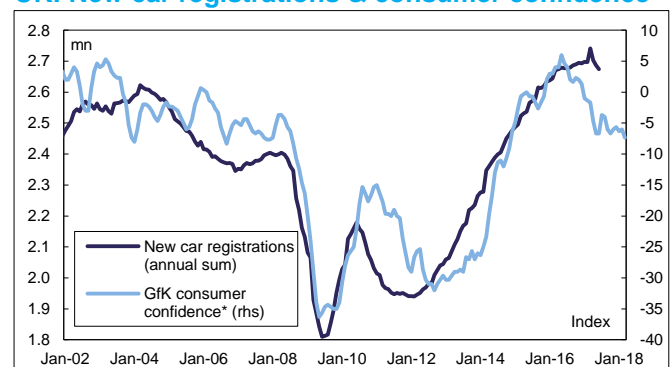
Another reason to be pessimistic about the momentum in the UK economy is the outlook for consumption. Last week's consumer confidence indicator surprised on the downside at the end of the second quarter, while the underlying trend in retail sales remains weak and car sales figures continue to disappoint. Indeed, today's figures showed that new car registrations were down by 4.8%Y/Y in June, having declined by 8.5%Y/Y in the previous month. Looking at private buyers alone, the drop was even steeper, at 7.8%Y/Y. While these figures to some extent reflect weaker demand following Vehicle Excise Duty changes in April, with the year-to-date new private car registrations down by nearly 5% compared to the equivalent period last year, consumers are seemingly becoming more cautious with big-ticket purchases. And with real disposable income set to be squeezed further over coming quarter, we would expect to see overall consumer spending remain weak.

UK: PMIs



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

UK: New car registrations & consumer confidence



*Nine-month lead.











Source: Thomson Reuters and Daiwa Capital Markets Europe Ltd.

The coming two days ahead in the UK











With no major UK economic data releases due tomorrow, focus will turn to Friday when the ONS will release its latest short-term output indicators for May, including industrial production, construction output and trade. Manufacturing output is expected to have risen by about ½%M/M, a slightly stronger pace than in the previous month, while construction activity also looks set to have recovered after a 1.6%M/M decline in April. The headline trade deficit looks set to have risen slightly in May from the four-month low of £2.1bn recorded at the start of Q2.

In the absence of any significant developments, the next edition of the Euro wrap-up will be published on 07 July 2017.

European calendar

Today's results							
Economic data							
Country	Release	Period	Actual	Market consensus/ Daiwa forecast	Previous	Revised	
EMU	 Final services PMI (final composite PMI)	Jun	55.4 (56.3)	54.7 (55.7)	56.3 (56.8)	-	
	 Retail sales M/M% (Y/Y%)	May	0.4 (2.6)	0.4 (2.3)	0.1 (2.5)	- (2.6)	
Germany	 Final services PMI (final composite PMI)	Jun	54.0 (56.4)	53.7 (56.1)	55.4 (57.4)	-	
France	 Final services PMI (final composite PMI)	Jun	56.9 (56.6)	55.3 (55.3)	57.2 (56.9)	-	
Italy	 Services PMI (composite PMI)	Jun	53.6 (54.5)	54.6 (54.7)	55.1 (55.2)	-	
Spain	 Services PMI (composite PMI)	Jun	58.3 (57.7)	56.5 (56.7)	57.3 (57.2)	-	
UK	 BRC Shop Price index Y/Y%	Jun	-0.3	-	-0.4	-	
	 New car registrations Y/Y%	Jun	-4.8	-	-8.5	-	
	 Services PMI (composite PMI)	Jun	53.4 (53.8)	53.5 (53.9)	53.8 (54.4)	- (54.3)	
Auctions							
Country	Auction						
Germany sold	 €3.2bn of 0% 2022 bonds (07-Oct-2022) at an average yield of -0.14%						

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

Tomorrow's data releases								
Economic data								
Country	BST	Release	Period	Market consensus/ Daiwa forecast	Previous			
Germany		07:00	Factory orders M/M% (Y/Y%)	May	1.9 (4.5)	-2.1 (3.5)		
Auctions and events								
Country	BST	Auction / Event						
EMU		12:30	ECB publishes account of the monetary policy meeting held on 8 June					
France		09:50	Auction: To sell 1% 2027 bonds (25-May-2027)					
		09:50	Auction: To sell 2% 2048 bonds (25-May-2048)					
		09:50	Auction: To sell 2.75% 2027 bonds (25-Oct-2027)					
Spain		09:30	Auction: To sell 0.4% 2022 bonds (30-Apr-2022)					
		09:30	Auction: To sell 4.9% 2040 bonds (30-Jul-2040)					
		09:30	Auction: To sell 2.9% 2046 bonds (31-Oct-2046)					
		09:30	Auction: To sell 1% 2030 index-linked bonds (30-Nov-2030)					
UK		10:30	Auction: To sell £2.5bn of 1.25% 2027 bonds (22-Jul-2027)					

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

Friday's data releases

Economic data

Country	BST	Release	Period	Market consensus/ <i>Daiwa forecast</i>	Previous
Germany		07:00 Industrial production M/M% (Y/Y%)	May	0.2 (4.0)	0.8 (2.9)
France		07:45 Trade balance €bn	May	-5.1	-5.5
		07:45 Current account balance €bn	May	-	-3.1
		07:45 Industrial production M/M% (Y/Y%)	May	0.6 (1.4)	-0.5 (0.6)
		07:45 Manufacturing production M/M% (Y/Y%)	May	0.6 (1.4)	-1.2 (1.1)
Italy		09:00 Retail sales M/M% (Y/Y%)	May	0.3 (1.0)	-0.1 (1.2)
Spain		08:00 Industrial production M/M% (Y/Y%)	May	0.5 (2.0)	0.1 (0.7)
UK		08:30 Halifax house price index M/M% (3M/Y%)	Jun	0.2 (3.1)	0.4 (3.3)
		09:30 Visible trade balance £bn	May	-10.9	-10.4
		09:30 Total trade balance £bn	May	-2.5	-2.1
		09:30 Construction output M/M% (Y/Y%)	May	0.7 (1.1)	-1.6 (-0.6)
		09:30 Industrial production M/M% (Y/Y%)	May	0.4 (0.2)	0.2 (-0.8)
		09:30 Manufacturing production M/M% (Y/Y%)	May	0.5 (1.0)	0.2 (0.0)
		13:00 NIESR GDP 3M/3M%	Jun	-	0.2

Auctions and events

Country	BST	Auction / Event
- 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
EMU	PPI Y/Y%	May	3.3	3.5	4.3	-
	ECB public sector asset purchases €bn	Weekly	4.4	-	12.5	-
Spain	Unemployment net change 000s	Jun	-98.3	-114.9	-111.9	-
UK	Construction PMI	Jun	54.8	55.0	56.0	-

Auctions

Country	Auction
Germany sold	€412mn of 0.5% 2030 index-linked bonds (15-Apr-2030) at an average yield of -0.45%

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.eco

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