

Euro wrap-up

Overview

- Bunds made losses as German inflation surprised on the upside and the Commission reported a further significant improvement in economic sentiment.
- Gilts made gains as UK consumers paid down debt and mortgage approvals fell to a record low.
- Tuesday will bring flash estimates of June inflation in the euro area, France and Italy.

Chris Scicluna
+44 20 7597 8326

Emily Nicol
+44 20 7597 8331

Daily bond market movements

Bond	Yield	Change
BKO 0 06/22	-0.707	+0.008
OBL 0 04/25	-0.710	+0.011
DBR 0 08/30	-0.475	+0.010
UKT 0½ 07/22	-0.086	-0.014
UKT 0% 06/25	-0.052	-0.014
UKT 4% 12/30	0.161	-0.011

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

Euro area

Commission survey points to broad-based rebound in activity

As expected, the Commission's June economic sentiment survey results added to evidence of a relatively broad-based recovery in activity following the deep retrenchment of recent months. Indeed, unlike last month when the improvement was concentrated in the industrial sector and consumer confidence, this time all of the headline sectoral indices for the euro area (and all of the equivalent figures for the large member states) rose to their highest levels since March as restrictions continued to be eased. However, while expectations of future production and demand rebounded, the improvement in overall sentiment was perhaps somewhat less than expected, and also inferior to what might have been inferred from last week's less granular [flash PMIs](#). Indeed, while the monthly increase in the euro area Economic Sentiment Indicator (ESI) of 8.2pts was the largest on the series, at 75.7 it suggested that little more than one quarter of the decline in activity from the pre-pandemic level in February to the trough in April had been reversed.

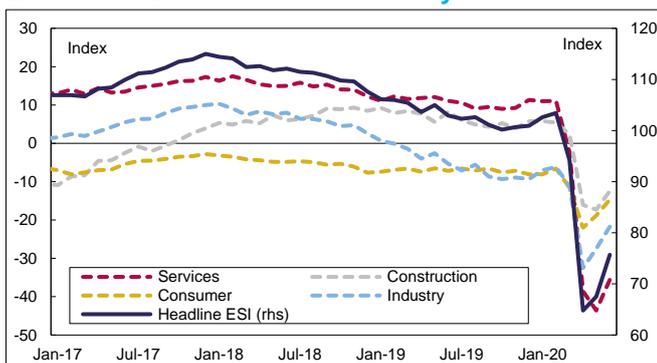
Sentiment still closer to the trough than the peak

Unsurprisingly, the Commission survey suggested that recovery remains weakest in services – having reached a series low in May, the headline index for the sector recovered just 15% of the ground lost since before the coronavirus hit and remained well below the range during the global financial crisis despite stronger demand expectations. Meanwhile, although the respective indicator posted the biggest increase this month as consumer willingness to make major purchases revived, retail sentiment still reversed barely more than one third of the drop from February. And even the ESI for the industrial sector still had more than half of the lost ground left to recover, with much improved production expectations contrasting with a further deterioration in export orders. In terms of other detail, the survey reported a second successive month of greater optimism regards the employment outlook, with roughly half of the initial declines in the respective indices reversed and an easing of consumer fears about unemployment registered too. The ECB will also have been encouraged to see a rebound in selling price expectations in industry, services and retail trade.

Inflation up ahead of expectations in June

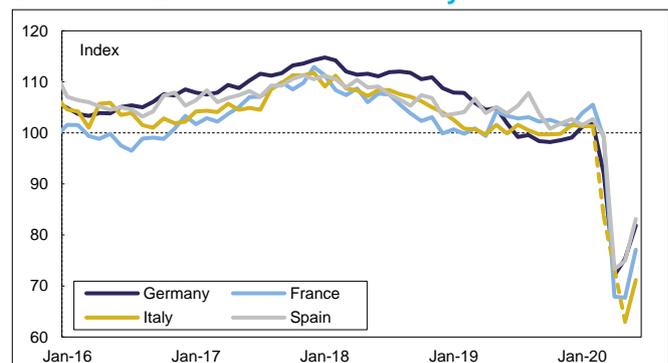
Due almost entirely to the rebound in global oil prices, which in euro terms have been about one third higher so far this month compared to May, the first national estimates of inflation in June – from Germany and Spain – beat expectations. In particular, on the EU-harmonised measure, German inflation fully reversed last month's decline, rising 0.3ppt to 0.8%Y/Y. The detail released on the national measure revealed that the increase in inflation was almost entirely explained by a slower pace of decline in energy prices, with the respective inflation rate up 2.3ppts to -6.2%Y/Y. In contrast, inflation of services,

Euro area: EC sentiment indices by sector



Source: Thomson Reuters and Daiwa Capital Markets Europe Ltd.

Euro area: EC sentiment indices by member state*



*Italy's survey in April-20 was not conducted. Source: Thomson Reuters and Daiwa Capital Markets Europe Ltd.



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food, and non-energy industrial goods registered minimal changes to suggest that core inflation was broadly steady at May's rate of 1.4%Y/Y on the harmonised measure. Both headline and core measures in Germany are set to decline next month due to cuts in VAT, with the main tax rate set to drop 3ppt to 16%, and the reduced rate set to drop 2ppt to 5%. In Spain, inflation on the EU measure rebounded even more sharply, up 0.6ppt to a three-month high of -0.3%Y/Y. While there was even less detail published, the national statistical institute (INES) attributed the rise to increased prices of fuels and electricity. So, Spanish core inflation on the EU measure also seems likely to have remained unchanged, at May's rate of 1.1%Y/Y. Given today's data, tomorrow's flash estimates of euro area inflation are likely to see the headline rate rise 0.3ppt to 0.4%Y/Y, while the core rate might be expected to remain unchanged at 0.9%Y/Y for a third month.

The day ahead in the euro area and US

Looking ahead, alongside the aforementioned euro area flash inflation data, tomorrow will bring preliminary French and Italian inflation figures for June, as well as French consumer spending data for May, which are likely to confirm a notable jump in spending compared with April (+30%M/M), albeit leaving the level still well down from the pre-pandemic level and significantly weaker than a year earlier. Elsewhere, final Spanish Q1 GDP data are expected to confirm a sharp contraction in economic activity in Q120 (-5.2%Q/Q, -4.1%Y/Y). In other news, we will hear from the ECB's Vice President De Guindos and Executive Board member Schnabel who are speaking at separate events, while in the markets, Germany will auction 2027 bonds and Italy will sell fixed and floating rate notes from across the curve.

In the US, the S&P Corelogic home price index for April will be published, as well as the Conference Board's consumer confidence survey for June. In terms of policy commentary, Chair Powell and Treasury Secretary Mnuchin will testify before the House Financial Services Committee on the CARES act, while New York Fed President Williams and Fed Governor Brainard will appear at online events.

UK

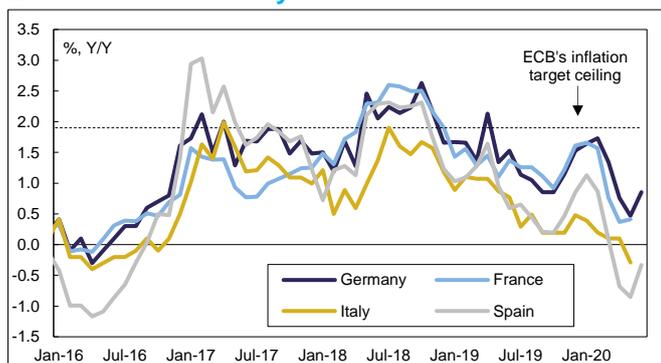
Lending to SMEs jumps...

Broadly consistent with last week's equivalent [euro area data](#), the Bank of England's latest bank lending data showed ongoing strong growth in lending to firms in May. In total, private sector businesses borrowed £11.4bn from banks and financial markets, driven by a jump in borrowing from SMEs as firms took advantage of the government's support facilities such as the Bounce Bank Loan Scheme. In particular, borrowing by SMEs leapt £18.2bn in May – far exceeding the previous largest net increase of £589mn – to see the annual growth in such lending jump 10.6ppts to 11.8%Y/Y. In contrast, larger firms repaid £12.9bn in May, the largest net repayment since the series began in 2011. But this followed exceptionally strong growth in the previous two months – up a cumulative £45.3bn – when firms took advantage of existing credit facilities. So, the total stock of loans to large firms was still up 10.8%Y/Y, the second-strongest annual increase on the series and more than double the rates seen at the end of last year.

...but consumers continue to pay off debt

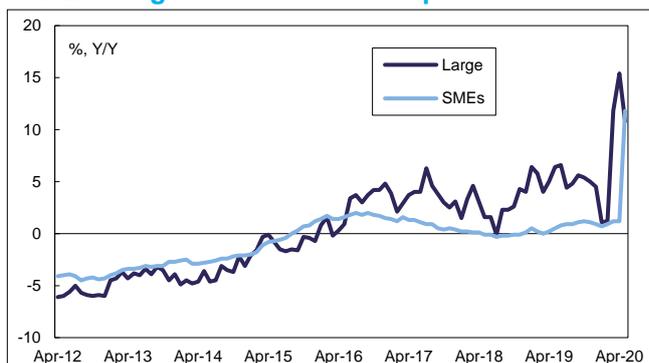
Lending to individuals also fell in May for the second successive month as consumer spending and the housing market remained very subdued. Certainly, demand for consumer credit remained extremely weak, with a net repayment of £4.6bn in May following the cumulative £11.2bn repaid in the previous two months. That left gross new consumer borrowing at just £13.6bn, compared with the average of £25.5bn in the six months to February, and the stock of consumer credit down 25%3M/3M and 3%Y/Y, the steepest such declines since the quarterly series began in the late 1980s. There was a modest increase in lending secured against homes in May (£1.2bn) although this remained weak by recent standards. Indeed, annual growth slowed to 3.1%Y/Y, the softest for more than three years. And a further weakening in approvals for new loans for house purchases, down almost 90% from the pre-pandemic level in February to a record low of 9.3k – around one third the trough during the financial crisis in 2008 – suggests that mortgage lending will remain very subdued for a while yet.

Euro area: Inflation by member states*



*June-20 figures for Germany and Spain are flash estimates.
 Source: Thomson Reuters and Daiwa Capital Markets Europe Ltd.

UK: Lending to non-financial corporations

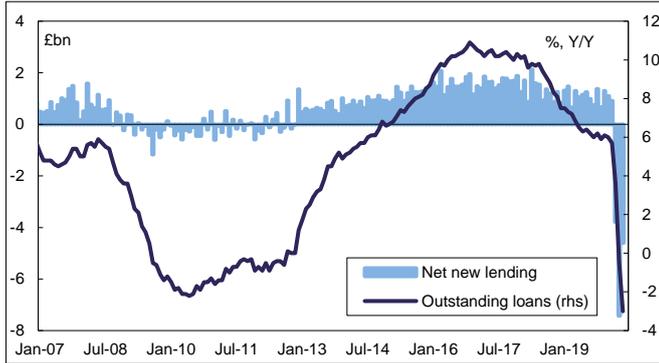


Source: BoE and Daiwa Capital Markets Europe Ltd.

The day ahead in the UK

Tomorrow will be relatively quiet for economic news, with the Lloyds business barometer for June to be accompanied by balance of payments data for Q1 and final Q1 GDP figures, which are expected to confirm that the UK economy contracted at the fastest rate since the global financial crisis, by 2.0%Q/Q, to leave output down 1.6%Y/Y. Likely of most interest will be BoE Chief Economist Haldane’s webinar in the morning discussing ‘the second quarter’, followed by BoE Deputy Governor Cunliffe on ‘central banking in the age of Covid19’ in the afternoon.

UK: Consumer credit



Source: BoE and Daiwa Capital Markets Europe Ltd.

UK: Mortgage lending and approvals



Source: BoE and Daiwa Capital Markets Europe Ltd.

European calendar

Today's results

Economic data

Country	Release	Period	Actual	Market consensus/ Daiwa forecast	Previous	Revised
EMU	 Economic sentiment indicator	Jun	75.7	80.3	67.5	-
	 Services (industrial) confidence	Jun	-35.6 (-21.7)	-24.0 (-18.5)	-43.6 (-27.5)	-
	 Final consumer confidence	Jun	-14.7	-14.7	-18.8	-
Germany	 Preliminary CPI (EU-harmonised CPI) Y/Y%	Jun	0.9 (0.8)	0.6 (0.6)	0.6 (0.5)	-
Spain	 Preliminary CPI (EU-harmonised CPI) Y/Y%	Jun	-0.3 (-0.3)	-0.5 (-0.5)	-0.9 (-0.9)	-
UK	 Net consumer credit £bn (Y/Y%)	May	-4.6 (-3.0)	-3.0 (-)	-7.4 (-0.4)	-
	 Net mortgage lending £bn (approvals '000s)	May	1.2 (9.3)	-1.0 (25.5)	0.3 (15.8)	0.0 (15.9)

Auctions

Country	Auction
- Nothing scheduled -	

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

Tomorrow's data releases

Economic data

Country	BST	Release	Period	Market consensus/ Daiwa forecast	Previous
EMU	 10.00	Flash CPI (core CPI) Y/Y%	Jun	0.3 (0.9)	0.1 (0.9)
France	 07.45	Preliminary CPI (EU-harmonised CPI) Y/Y%	Jun	0.4 (0.5)	0.4 (0.4)
	 07.45	Consumer spending M/M% (Y/Y%)	May	30.0 (-13.5)	-20.2 (-34.1)
Italy	 10.00	Preliminary CPI (EU-harmonised CPI) Y/Y%	Jun	-0.2 (-0.3)	-0.2 (-0.3)
Spain	 08.00	Final GDP Q/Q% (Y/Y%)	Q1	-5.2 (-4.1)	0.4 (1.8)
UK	 00.01	Lloyds business barometer	Jun	-	-33
	 07.00	Final GDP Q/Q% (Y/Y%)	Q1	-2.0 (-1.6)	0.0 (1.1)
	 07.00	Current account balance £bn	Q1	-15.0	-5.6

Auctions and events

Country	BST	Auction / Event
EMU	 12.00	ECB Executive Board member Schnabel scheduled to speak
	 14.00	ILO publishes report on virus impact on the labour market
	 16.00	ECB Vice President De Guindos scheduled to speak
Germany	 10.30	Auction: €3bn of 0% 2027 bonds
Italy	 10.00	Auction: €3bn of 1.85% 2025 bonds
	 10.00	Auction: €1.25bn of 2023 floating rate notes
	 10.00	Auction: 1.65% 2030 bonds
	 10.00	Auction: 0.95% 2030 bonds
UK	 11.00	BoE Chief Economist Haldane speaks at a webinar – The Second Quarter
	 15.00	BoE Deputy Governor Cunliffe scheduled to speak – Central Banking in the Covid-19 Age

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

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