

Euro wrap-up

Overview

- Bunds made gains despite the flash PMIs signalling a pickup in euro area economic growth at end-Q2 amid continued supply bottlenecks and cost pressures.
- Gilts made gains predominantly at the short end of the curve as the flash PMIs suggested that the pace of expansion in the UK economy moderated slightly in June.
- Thursday will bring the BoE's latest monetary policy announcement and national business surveys from Germany and France.

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Daily bond market movements

Bond	Yield	Change
BKO 0 06/23	-0.662	-0.004
OBL 0 04/26	-0.573	-0.013
DBR 0 08/31	-0.182	-0.016
UKT 0 ¹ / ₈ 01/23	0.074	-0.025
UKT 0 ¹ / ₈ 01/26	0.376	-0.009
UKT 4 ³ / ₄ 12/30	0.775	-0.003

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

Source: Bloomberg

Euro area

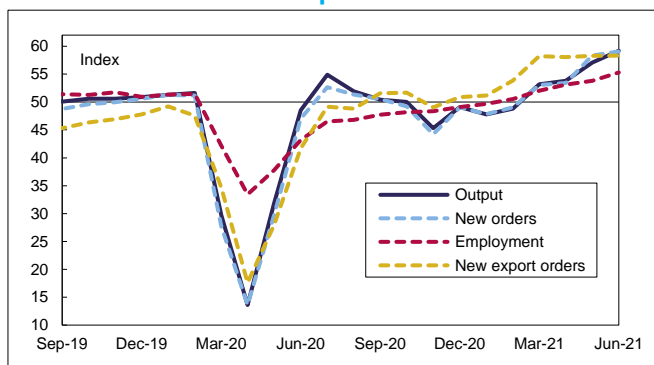
Flash PMIs signal accelerated expansion despite persistent supply bottlenecks

Broadly as expected, the flash euro area PMIs signalled a strengthening of economic expansion at the end of Q2, with the composite output index up 2.1pts in June to a fifteen-year high of 59.2. Thanks to the further relaxation of pandemic restrictions and the accelerated progress with vaccinations, the improvement came principally from the services sector, with the respective activity PMI up 2.8pts to 58.0, the highest in 3½ years. But contrary to expectations, the survey also reported a modest acceleration in manufacturing for the first time since March, with the respective output index up 0.2pts to 62.4, less than 1pt below the series high recorded three months ago. With the pandemic-era PMIs impossible to translate mechanistically into implied rates of GDP growth with any accuracy, however, of most interest in the survey were the signals related to ongoing supply bottlenecks and their consequences. In that respect, the challenges appear to have become no less acute, with a record rise reported in backlogs of work, and further near-record lengthening of supply delivery times and rundown of inventories of goods. Moreover, the respective composite PMIs signalled record increases in prices of both input and output prices, led by manufacturing but now also more visible in services. More happily, the survey also reported a further pickup in job growth to the fastest since the start of 2018.

Germany leads improvement in June, France lags somewhat

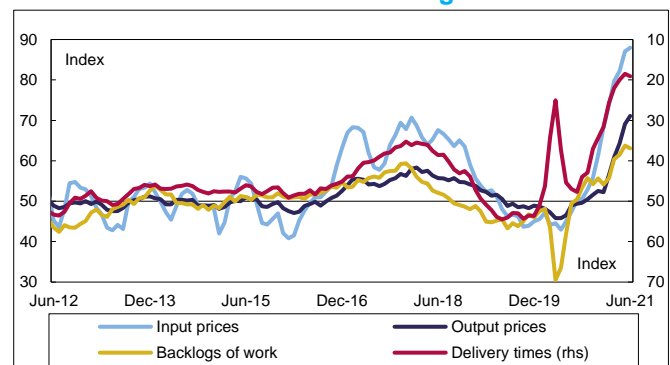
At the country level, the improvement in June was marked in Germany, where the composite output PMI rose more than 4pts – and three times the increase in the consensus forecast – to a more than decade high of 60.4. Likewise, the reported acceleration in German services was impressive, with the respective activity index up more than 5pts to a 10-year high of 58.1, and new work in the sector also up the most in more than a decade. Contrary to expectations, German manufacturing output also reportedly sped up once again, with the respective index up more than 2pts to a historically elevated 65.1 and new orders also reportedly stronger. While increases in German factory prices were the strongest on the series, backlogs in the sector slowed a little from the prior month's record high. In France, however, the flash PMIs slightly disappointed expectations, with the composite output PMI up a trivial 0.1pt to an eleven-month high of 57.1. While that should nevertheless be consistent with a firm increase in French GDP in Q2, the 0.8pt rise in the services PMI to a three-year high of 57.4 was also less than expected. And the French manufacturing output PMI fell back more than 3pts to a four-month low of 55.5 with new order growth softer. Supply bottlenecks remained a challenge in France, with delivery times up to the second-highest on the series albeit growth in backlogs slightly softer. And while the flash PMIs suggested a record rise in German employment intentions in June, the equivalent index in France rose merely to a three-month high.

Euro area: Selected composite PMIs



Source: Markit, Refinitiv and Daiwa Capital Markets Europe Ltd.

Euro area: Selected manufacturing PMIs



Source: Markit, Refinitiv and Daiwa Capital Markets Europe Ltd.

The day ahead in the euro area

Thursday brings further national business surveys – from Germany’s ifo institute and France’s INSEE – which seem highly likely to tally with today’s flash PMIs and point to firm economic expansion at the end of Q2. In particular, the ifo expectations balance, which measures German firms’ optimism about the coming six months, is forecast to rise again in June to a ten-year high of 103.6. And the current assessment balance is expected to rise for the fifth successive month to a new pandemic-era high of 97.2 in June, albeit remaining some 1.6pts below the pre-pandemic level in February 2020. Meanwhile, INSEE’s measure of French business confidence is expected to rise a further 2pts to 110 in June, which would be the highest since January 2018. Final Spanish GDP data for Q1 are expected to confirm the current estimates of contractions of 0.5%Q/Q and 4.3%Y/Y.

UK

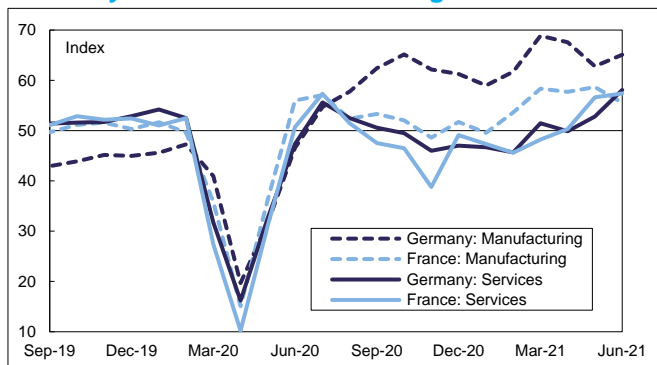
Flash PMIs slip back in manufacturing and services while cost pressures build

Ahead of tomorrow’s BoE monetary policy announcement, the UK’s flash PMIs remained consistent with solid growth at the end of Q2, even though they confounded hopes of a further acceleration in activity. Indeed, the composite output PMI slipped back 1.2pts from the May series high to a three-month low of 61.7. With the final relaxation of pandemic containment measures postponed to July, according to the survey services activity slowed somewhat, with the respective PMI down 1.2pts to a nevertheless still elevated 61.7. Growth in manufacturing output was also reportedly a touch less vigorous with the PMI slipping back 1pt to 62.0. And growth in new orders slowed not least due to a softening in export demand (the respective PMI dropped more than 4pts to 55.4), tallying with yesterday’s [CBI survey](#) to suggest that UK manufacturers are benefiting far less from the rebound in global demand than their peers elsewhere in Europe. More positively, the flash PMIs suggested that firms looked to increase their staff levels at the joint-fastest pace on the series. But as in the euro area, the survey suggested that supply bottlenecks remain challenging, with the indices of input costs and output prices up to series highs amid an increase in supplier delivering times to the second highest on the series, despite a slight easing in backlogs of work.

The day ahead in the UK

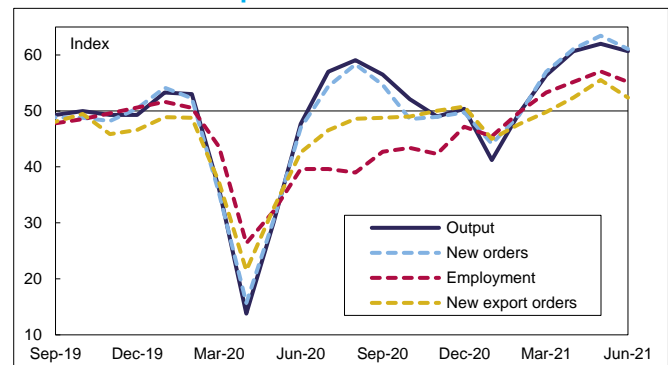
The week’s main event in the UK comes tomorrow in the form of the BoE’s monetary policy announcement. Since the BoE published forecasts following its previous MPC meeting on 6 May, economic activity appears to have improved a touch ahead of expectations. And inflation has also picked up a little ahead of the BoE’s forecast, with the headline measure

Germany & France: Manufacturing & services PMIs*



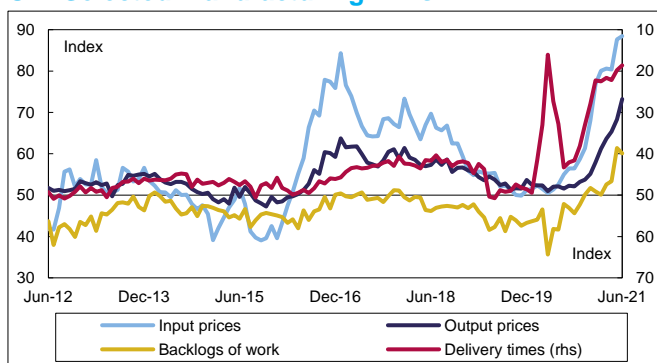
*Manufacturing output PMIs and services activity PMIs. Source: Markit, Refinitiv and Daiwa Capital Markets Europe Ltd.

UK: Selected composite PMI



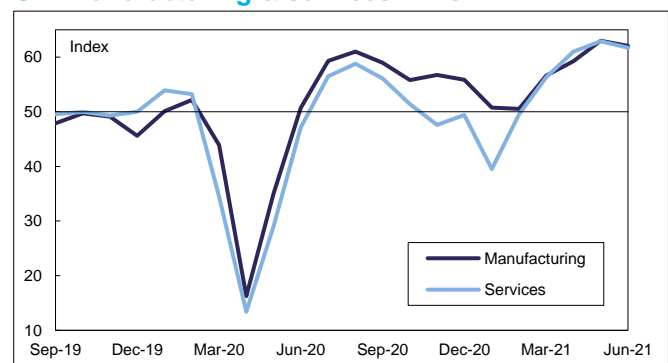
Source: Markit, Refinitiv and Daiwa Capital Markets Europe Ltd.

UK: Selected manufacturing PMIs



Source: Markit, Refinitiv and Daiwa Capital Markets Europe Ltd.











UK: Manufacturing & services PMIs*













*Manufacturing output PMIs and services activity PMIs. Source: Markit, Refinitiv and Daiwa Capital Markets Europe Ltd.

having risen above the target to 2.1%Y/Y and the core measure up to 2.0%Y/Y in May. At last month's meeting, the BoE did not expect its inflation target to be passed until much later in the year. At tomorrow's meeting, however, the MPC will likely continue to judge recent price pressure to be transitory and expect inflation will return close to target over the medium term. But it will also underscore again that the outlook for the economy, including the relative movements in demand and supply, remains highly uncertain, with the recent pickup in new coronavirus cases – to more than four times the rate at the time of the MPC's May meeting – and delay to further economic reopening reminders of the downside risks. So, we do not expect any change to current policy or guidance at the forthcoming meeting. Given his concerns about upside risks to inflation, Chief Economist Haldane – for which this will be his last meeting – will likely vote again for reducing the target stock of asset purchases from £875bn, which will be fulfilled by the end of the year. But while we cannot exclude the possibility that a further policymaker will join him, Haldane will also likely again be the sole MPC member to vote for such a reduction. And the MPC will also repeat that it does not intend to tighten monetary policy at least until there is clear evidence that significant progress is being made in eliminating spare capacity and achieving the 2% inflation target.

European calendar

Today's results						
Economic data						
Country	Release	Period	Actual	Market consensus/ <i>Daiwa forecast</i>	Previous	Revised
EMU	 Preliminary manufacturing (services) PMI	Jun	63.1 (58.0)	62.3 (58.0)	63.1 (55.2)	-
	 Preliminary composite PMI	Jun	59.2	58.8	57.1	-
Germany	 Preliminary manufacturing (services) PMI	Jun	64.9 (58.1)	63.0 (55.7)	64.4 (52.8)	-
	 Preliminary composite PMI	Jun	60.4	57.6	56.2	-
France	 Preliminary manufacturing (services) PMI	Jun	58.6 (57.4)	59.0 (59.5)	59.4 (56.6)	-
	 Preliminary composite PMI	Jun	57.1	59.0	57.0	-
UK	 Preliminary manufacturing (services) PMI	Jun	64.2 (61.7)	64.0 (62.8)	65.6 (62.9)	-
	 Preliminary composite PMI	Jun	61.7	62.5	62.9	-
Auctions						
Country	Auction					
Germany	 sold €2.06bn of 0% 2036 bonds at an average yield of 0.08%					
UK	 sold £400mn of 0.125% 2065 index-linked bonds at an average yield of -2.042%					

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

Tomorrow's releases						
Economic data						
Country	BST	Release	Period	Market consensus/ <i>Daiwa forecast</i>	Previous	
Germany		09.00	Ifo current assessment balance (expectations)	Jun	97.5 (104.0)	95.7 (99.2)
France		07.45	INSEE business confidence	Jun	110	108
		07.45	INSEE manufacturing confidence (production outlook)	Jun	110 (-)	107 (18)
Spain		08.00	Final GDP Q/Q% (Y/Y%)	Q1	-0.5 (-4.3)	0.0 (-8.9)
UK		12.00	BoE Bank Rate %	Jun	<u>0.10</u>	0.10
		12.00	BoE Gilt purchase target £bn	Jun	<u>875</u>	875
Auctions and events						
EMU		12.30	ECB's Panetta scheduled to speak at an online event 'A digital Euro'			
		16.30	ECB's Schnabel scheduled to speak			
UK		12.00	BoE monetary policy announcement			
		12.00	BoE publishes Agents' summary of business conditions Q221			

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

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<https://www.uk.daiwacm.com/ficc-research/recent-blogs>

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