

# Euro wrap-up

## Overview

- Bunds made modest losses as the account of the ECB's June policy meeting confirmed broad consensus in favour of maintaining PEPP purchases at a higher pace but also revealed minorities in favour of slower and faster rates.
- Gilts followed USTs lower despite weaker-than-expected UK GDP data for May.
- The coming week's data will bring updates on euro area industrial output, the UK's labour market, and inflation in both the euro area and UK.

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### Daily bond market movements

Bond	Yield	Change
BKO 0 06/23	-0.685	+0.007
OBL 0 04/26	-0.602	+0.007
DBR 0 08/31	-0.294	+0.014
UKT 0 <sup>1</sup> / <sub>8</sub> 01/23	0.079	+0.017
UKT 0 <sup>1</sup> / <sub>8</sub> 01/26	0.290	+0.032
UKT 4 <sup>3</sup> / <sub>4</sub> 12/30	0.655	+0.044

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

## Euro area

### Broad consensus for ECB's June policy decision

Following yesterday's underwhelming [strategic policy review](#) conclusions, the ECB remained in focus today with the belated publication of the account of the June policy meeting. From Lagarde's press conference, we already knew that last month's decision to maintain net purchases under the PEPP over the coming quarter "at a significantly higher pace than during the first months of the year" had not been unanimous. But today's account clarified that, despite the improved economic outlook, there had been "broad consensus" with "most members" of the Governing Council in favour of the policy decision. The majority agreed that financial conditions were judged to be "too fragile to allow a meaningful reduction in the pace of purchases without risking a disorderly rise in yields" and that the recovery "depended heavily on policy support". Moreover, one Governing Council member – who we suspect was the highly dovish Executive Board member Panetta – stated that "in view of the persistent inflation shortfall projected in the June staff projections, even an increase in asset purchases as the main monetary policy instrument could be justified". In light of yesterday's decision to set an unambiguous 2% medium-term inflation target, the provision of extra monetary stimulus might now seem even more justifiable. However, in her press conference yesterday, Lagarde suggested that the ECB's reaction function had not changed, and so Panetta's position seems unlikely to gain traction

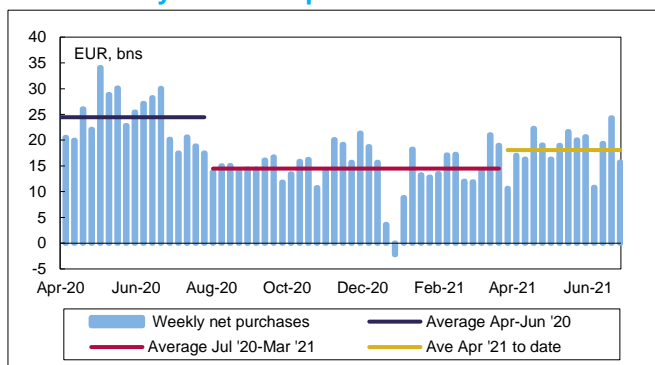
### Cases made for both faster and slower purchases, no change to policy likely on 22 July

Today's account also noted that a minority hawkish view was also expressed last month. According to this position – likely shared by the Presidents of the German, Austrian and Dutch national banks – the improved economic outlook meant that "to provide the same degree of accommodation, asset purchases should be scaled back somewhat". Concerns were also expressed about potential adverse side-effects from current policy settings, including that they might hinder structural change in the corporate sector and resource reallocation in the labour market – the apparent advocacy of a policy of creative destruction despite the still-fragile nature of the recovery. Finally, it was also noted that "property price dynamics were accelerating", something that will be taken into account by the Governing Council in future as it assesses supplementary information on owner-occupied housing costs. Overall, the range of views expressed last month reinforces our expectation that there will be no change to policy at the 22 July Governing Council despite the new inflation target unveiled yesterday.

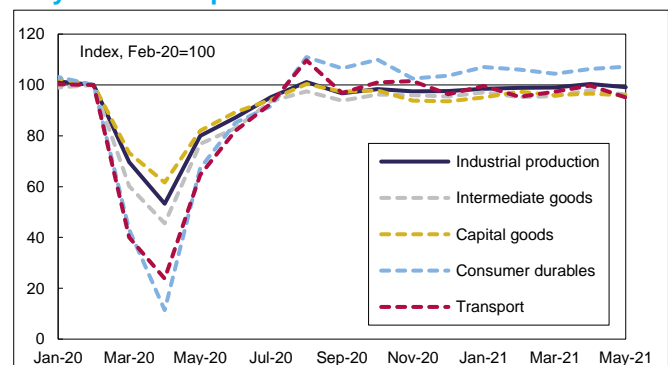
### Italian manufacturing production disappoints in May

Consistent with the weak production figures from [Germany](#) and [France](#) earlier in the week, today's Italian industrial production data fell short of expectations, with total output declining 1.5%M/M in May, fully reversing downwardly revised

#### ECB: Weekly net PEPP purchases



#### Italy: Industrial production



growth in April. The weakness in part reflected a more than 5%M/M drop in energy production that month. But manufacturing output also saw widespread declines too, driven by a slump in autos production (-4.6%M/M) as global supply constraints hit. Nevertheless, given the recent monthly profile, industrial output was still on average so far in Q2 almost 1% higher than the Q1 average and just 0.8% below the pre-pandemic level. And with the exception of consumer non-durables, manufacturing output was trending higher across the key subsectors too.

## The coming week in the euro area

It should be a relatively quiet week ahead for euro area top-tier economic news. Data-wise, the most noteworthy release is likely to be the aforementioned euro area industrial production figures for May on Wednesday. Despite the weakness recorded in the largest three member states, aggregate euro area IP is expected to have moved broadly sideways in May, supported by a surge in output from Spain. Friday, meanwhile, will bring final euro area inflation numbers for June, which are expected to confirm the modest drop in the preliminary headline estimate to 1.9%Y/Y, with the core rate unchanged on the month at 0.9%Y/Y. Revised June inflation figures come from Germany and France on Tuesday, Italy on Thursday and Spain on Wednesday. Finally, Friday will also bring euro area trade data for May car registrations numbers for June.

## UK

### UK GDP growth softer than expected in May despite services rebound

The main economic focus in the UK today was on the release of GDP figures for May. And while these reported the fourth consecutive monthly expansion, growth of 0.8%M/M fell some way short of expectations (the BBG median was almost twice as strong at 1.5%M/M) and followed downwardly revised growth in April (2.0%M/M) to leave the level of output still 3.1% below the February 2020 level. Within the detail, the services sector predictably benefitted from the further easing of restrictions – particularly those affecting hospitality and entertainments – with activity up 0.9%M/M. Indeed, consumer-facing services were up more than 3%M/M in May, of which food and beverage services grew by 34%M/M, to leave the level of such activity a little higher than the August 2020 peak when the Eat Out to Help Out initiative gave a temporary boost, but still almost 9½% below the pre-pandemic level. So, despite the recent recovery, overall services output was still a little more than 3% below the pre-pandemic peak.

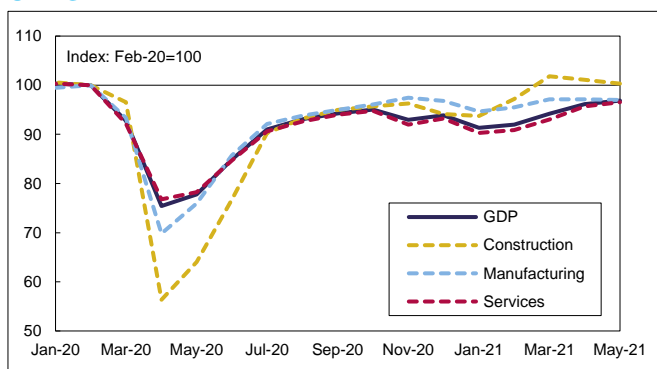
### Manufacturing restrained by supply bottlenecks

Industrial production also grew by 0.8%M/M in May, boosted by the strongest monthly increase in energy output (5.7%M/M) for more than nine years as adverse weather conditions that month increased demand. But contrasting with expectations, manufacturing production fell slightly for the second successive month, with almost half of the subsectors contributing to the decline and export sales down for the first time since January. Like in [Germany](#) and [France](#), manufacturing weakness was dominated by the transport sector, of which output was down 16.5%M/M as microchip shortages disrupted car production – indeed, autos production fell for the third consecutive month and by a whopping 27%M/M, to leave it 35% below the pre-pandemic level. In marked contrast, production of pharmaceuticals surged 25%M/M (following a decline of 14½%M/M in April) to leave it more than 14% higher than the February 2020 level. And overall, given the monthly profile, manufacturing output was still trending in Q2 almost 1½% higher than the Q1 average.

### Construction growth to be strong in Q2 despite weak May

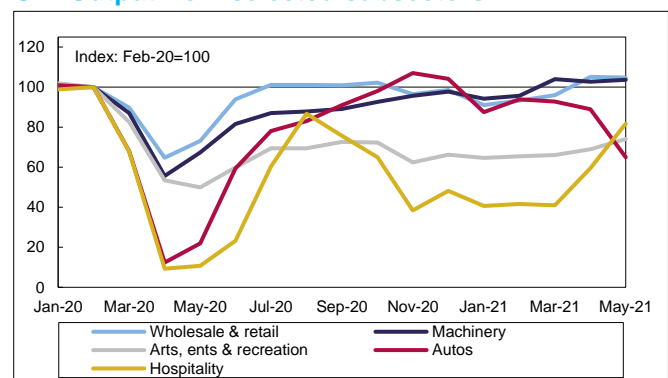
Construction sector output, meanwhile, slipped back for the second successive month in May (down 0.8%M/M), with declines in both repair and maintenance and new work in May. But the recent weakness follows strong growth in February and March (up a cumulative 8½%) particularly in private new housing and infrastructure work. So, despite falling in both April and May, the average level of output in the first two months of Q2 was more than 3% higher than Q1.

#### UK: GDP



Source: Refinitiv and Daiwa Capital Markets Europe Ltd.

#### UK: Output from selected subsectors



Source: Refinitiv and Daiwa Capital Markets Europe Ltd.

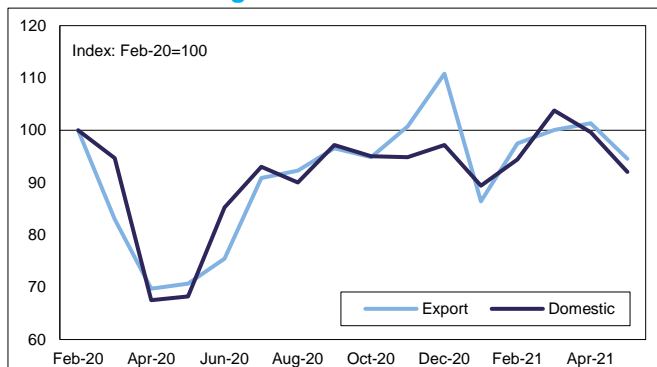
## Growth set to accelerate in Q2 before moderating during the summer

Not least given the weakness at the start of the year and strength in March (upwardly revised to 2.4%/M/M), today's release showed that GDP in April and May was trending 4.3% higher than the average during Q1. And so while we expect to see some payback in the monthly GDP figures in June, not least given evidence of weaker shopping centre footfall amid inclement weather, ongoing supply bottlenecks hitting manufacturing and construction works, and delay in the final easing of lockdown, we forecast quarterly growth of almost 4½%Q/Q in Q2. Positive growth seems likely to be recorded across each of the main subsectors (with services up by more than 5%Q/Q; construction up more than 3%Q/Q; and manufacturing up around 1%Q/Q). While activity in Q3 should be supported by the final unlocking of restrictions and increased tourism – whether it be the return of international travellers or more staycations – significant concerns persist related to supply constraints, the weather remains awful for the time of year, and the recent jump in coronavirus cases associated with the Delta variant risks acting as a deterrent to spending even as restrictions on activity are lifted. As such, we expect the pace of recovery to moderate in the third quarter, with GDP growth forecast to moderate to about 2½%Q/Q, which would leave the level of output about 1.0% below the pre-pandemic level in September.

## The coming week in the UK

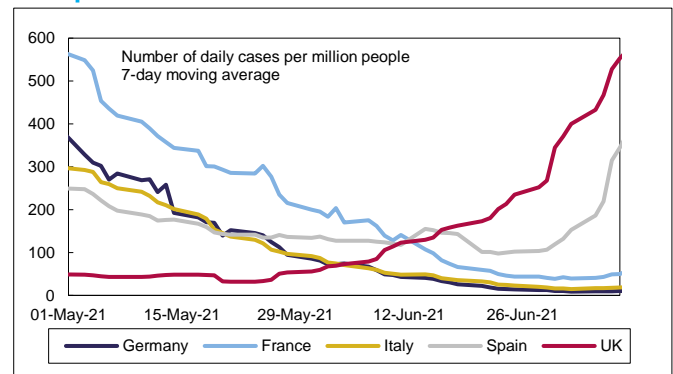
There will be several top-tier UK data releases in the coming week, with June inflation figures due on Wednesday and the latest labour market report on Thursday. Having jumped above the 2.0% target in May for the first time in almost two years, we expect the headline CPI rate to have moved sideways at 2.1%Y/Y in June, with a moderation in non-energy goods inflation likely to be offset by higher services and energy prices. Indeed, given recent developments in oil markets, we see the risks skewed to the upside. Against this backdrop, however, core inflation might well have edged slightly lower from the near-two-year high of 2.0%Y/Y reached in May. With the government's Job Retention Scheme still in full operation in May and the economy continuing to return to some form of post-lockdown normality, we expect to see a further tightening in labour market conditions, including a further notable increase in payrolls and vacancies. The unemployment rate is expected to have moved sideways in the three months to May – although it is worth noting that recent unemployment, employment and inactivity figures will be revised slightly due to methodological changes (the unemployment rate will be nudged up between 0.1-0.2ppt and employment rate revised down by 0.3ppt). Meanwhile, growth in average labour earnings seems highly likely to rise above 6½%Y/Y, supported in part by base and composition effects. Elsewhere, on Tuesday the BoE will publish its latest Financial Stability Report with Thursday bringing its quarterly Credit Conditions and Bank Liabilities surveys. Earlier in the week, the BRC's latest retail sales monitor for June will also be published on Tuesday.

### UK: Manufacturing turnover



Source: ONS and Daiwa Capital Markets Europe Ltd.












### Europe: New Covid-19 cases



Source: Bloomberg and Daiwa Capital Markets Europe Ltd.








**The next edition of the Euro wrap-up will be published on 13 July 2021**

## Daiwa economic forecasts

	2020	2021				2022	2020	2021	2022
	Q4	Q1	Q2	Q3	Q4	Q1			
<b>GDP growth, %, Q/Q</b>									
Euro area 	-0.6	-0.3	1.2	2.4	1.2	1.0	-6.7	4.5	4.6
UK 	1.3	-1.6	4.4	2.5	2.3	1.0	-9.8	6.7	5.9
<b>Inflation</b>									
Euro area									
Headline CPI 	-0.3	1.1	1.8	2.3	2.5	1.4	0.3	1.9	1.5
Core CPI 	0.2	1.2	0.9	1.2	1.5	0.8	0.7	1.2	1.3
UK									
Headline CPI 	0.5	0.6	1.9	2.2	2.8	2.8	0.9	1.9	2.1
Core CPI 	1.3	1.2	1.7	2.0	2.3	2.2	1.4	1.8	1.9
<b>ECB</b>									
Refi Rate % 	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00
Deposit Rate % 	-0.50	-0.50	-0.50	-0.50	-0.50	-0.50	-0.50	-0.50	-0.50
PEPP envelope* (€bn) 	1850	1850	1850	1850	1850	1850	1850	1850	1850
<b>BoE</b>									
Bank Rate % 	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10
Bond purchases** (£bn) 	895	895	895	895	895	895	895	895	895

\*Monthly target €bn, end of period. \*\*Monthly target £bn, end of period. Source: Bloomberg, ECB, BoE and Daiwa Capital Markets Europe Ltd.


















## European calendar

Today's results							
Economic data							
Country	Release	Period	Actual	Market consensus/ Daiwa forecast	Previous	Revised	
Italy 	Industrial production M/M% (Y/Y%)	May	<b>-1.5 (21.1)</b>	0.3 (1.8)	1.8 (79.5)	<b>1.5 (79.0)</b>	
UK 	Monthly GDP M/M% (3M/3M)	May	<b>0.8 (3.6)</b>	<u>1.3 (3.7)</u>	2.3 (1.5)	<b>2.0 (-)</b>	
	Industrial production M/M% (Y/Y%)	May	<b>0.8 (20.6)</b>	1.5 (21.6)	-1.3 (27.5)	<b>-1.0 (27.2)</b>	
	Manufacturing production M/M% (Y/Y%)	May	<b>-0.1 (27.7)</b>	1.0 (29.5)	-0.3 (39.7)	<b>0.0 (39.1)</b>	
	Index of services M/M% (3M/3M%)	May	<b>0.9 (3.9)</b>	1.6 (4.1)	3.4 (1.4)	<b>2.8 (-)</b>	
	Construction output M/M% (Y/Y%)	May	<b>-0.8 (56.5)</b>	1.0 (58.2)	-2.0 (77.9)	<b>-0.7 (79.4)</b>	
	Goods trade balance £bn	May	<b>-8.5</b>	-11.1	-11.0	-	
Auctions							
Country	Auction						
- Nothing to report -							

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.











## The coming week's data calendar

### The coming week's key data releases

Country	BST	Release	Period	Market consensus/ <i>Daiwa</i> <i>forecast/actual</i>	Previous
<b>Monday 12 July 2021</b>					
- Nothing scheduled -					
<b>Tuesday 13 July 2021</b>					
Germany		07.00 Final CPI (EU harmonised CPI) Y/Y%	Jun	2.3 (2.1)	2.5 (2.4)
France		07.45 Final CPI (EU harmonised CPI) Y/Y%	Jun	1.5 (1.9)	1.4 (1.8)
UK		00.01 BRC retail sales monitor, like-for-like sales Y/Y%	Jun	-	18.5
<b>Wednesday 14 July 2021</b>					
Euro area		10.00 Industrial production M/M% (Y/Y%)	May	-0.1 (22.4)	0.8 (39.3)
Spain		08.00 Final CPI (EU harmonised CPI) Y/Y%	Jun	2.6 (2.4)	2.7 (2.4)
UK		07.00 CPI (core CPI) Y/Y%	Jun	<u>2.1 (1.9)</u>	2.1 (2.0)
		07.00 PPI output prices (input prices) Y/Y%	Jun	- (-)	4.6 (10.7)
		09.30 ONS house price index Y/Y%	May	-	8.9
<b>Thursday 15 July 2021</b>					
Italy		09.00 Final CPI (EU harmonised CPI) Y/Y%	Jun	1.3 (1.3)	1.3 (1.2)
UK		07.00 Claimant count rate % (change 000s)	Jun	- (-)	6.2 (-92.6)
		07.00 ILO unemployment rate 3M%	May	4.7	4.7
		07.00 Employment change 3M/3M 000s	May	95	113
		07.00 Average wages (excluding bonuses) 3M/Y%	May	7.1 (6.6)	5.6 (5.6)
<b>Friday 16 July 2021</b>					
Euro area		07.00 EU27 new car registrations Y/Y%	Jun	-	53.4
		10.00 Final CPI (core CPI) Y/Y%	Jun	1.9 (0.9)	2.0 (1.0)
		10.00 Trade balance €bn	May	-	9.4
Italy		09.00 Trade balance €bn	May	-	5.9

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

## The coming week's key events & auctions

Country	BST	Event / Auction
<b>Monday 12 July 2021</b>		
Euro area 	-	ECB President Lagarde and Executive Board member Panetta attend Eurogroup meeting in Brussels
<b>Tuesday 13 July 2021</b>		
Euro area 	-	ECB Vice President de Guindos to speak on the "ECB and the future of monetary policy"
Germany 	10.30	Auction: €5bn of 0% 2023 bonds
Italy 	10.00	Auction: €4.5bn of 2024 bonds
	10.00	Auction: €2.75bn of 0.5% 2028 bonds
	10.00	Auction: €1.75bn of 0.95% 2037 bonds
UK 	07.00	BoE's Financial Stability Report and Policy summary and record
<b>Wednesday 14 July 2021</b>		
Germany 	10.30	Auction: €4bn of 2031 bonds
UK 	18.00	BoE Deputy Governor Ramsden to speak the Strand Group with King's Business School
<b>Thursday 15 July 2021</b>		
France 	09.50	Auction: 0% 2024 bonds
	09.50	Auction: 0% 2026 bonds
	09.50	Auction: 2.75% 2027 bonds
	09.50	Auction: 0.75% 2028 bonds
	10.50	Auction: 0.1% 2031 index-linked bonds
	10.50	Auction: 0.1% 2036 index-linked bonds
Spain 	09.30	Auction: 0.25% 2024 bonds
	09.30	Auction: 0% 2028 bonds
	09.30	Auction: 0.5% 2031 bonds
	09.30	Auction: 4.2% 2037 bonds
UK 	09.30	BoE publishes Bank Liabilities and Credit Conditions Surveys
	11.00	BoE MPC member Saunders to speak on "The inflation outlook"
<b>Friday 16 July 2021</b>		
- Nothing scheduled -		

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

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