Euro wrap-up

Overview

Chris Scicluna
+44 20 7597 8326

- Gilts made significant losses after two members of the BoE's MPC made hawkish comments while data showed significant positive momentum in the UK's labour market.
- On a quiet day for economic news from the euro area, Bunds followed USTs higher at the longer end of the curve.
- Friday will bring final euro area inflation data for June along with goods trade figures for May.

Daily bond market movements

Bond	Yield	Change
BKO 0 06/23	-0.686	+0.001
OBL 0 04/26	-0.626	-0.004
DBR 0 08/31	-0.334	-0.012
UKT 0⅛ 01/23	0.134	+0.062
UKT 0⅛ 01/26	0.355	+0.062
UKT 4¾ 12/30	0.665	+0.039

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

UK

Payrolls jump sharply in June on reopening of the economy

The MPC's forward policy guidance, first introduced last November, states that the BoE 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 sustainably. After yesterday's significant upside surprise to June inflation to well above target – which clearly exceeded the path anticipated in the BoE's May forecast – today's data reported significant momentum in the labour market to suggest that a non-negligible amount of spare capacity has now been used up. Having risen by more than 211k (0.7%) in May, the number of payroll employees jumped a record 356k (1.3%) in June to 28.9 million. That left it 783k (2.8%) above the trough reached in November and just 206k (0.7%) below the pre-pandemic level. And for the first time since the outbreak of Covid-19, the ONS reported that payrolls in some regions (the North East, North West, East Midlands and Northern Ireland) had risen above the pre-pandemic level. Job growth in June was led principally by the sectors that had been most affected by pandemic restrictions, notably hospitality and leisure. Nevertheless, in those sectors payrolls remain still more than 10% below the pre-pandemic levels.

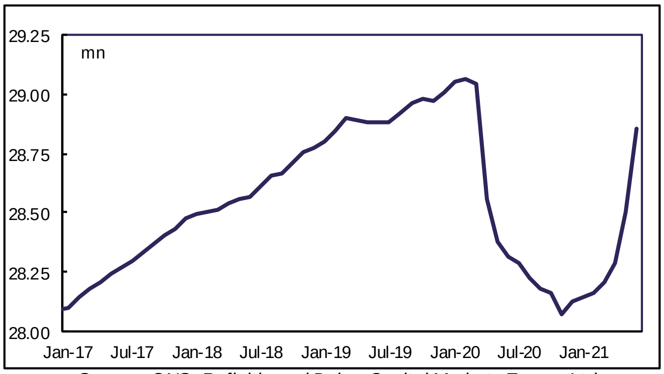
Sharp rise in vacancies but still evidence of spare capacity in the labour market

Meanwhile, in the three months to June, the number of job vacancies rose to 862k, back above the pre-pandemic level for the first time and exceeding that threshold by 77.5k (9.9%). In most sectors with the main exception of retail, vacancies have risen back close to or above the pre-pandemic levels, led by health and social work as well as hospitality. However, the record inflow recorded into work in June implies that staff shortages suggested by media reports and some surveys (e.g. the KPMG/REC report on jobs) need not be widespread. Indeed, online job advert data through to 9 July suggest that the number of vacancies might already have peaked, suggesting that the acceleration in June reflected the impact of sudden reopening of the economy rather than evidence of a marked tightening in the labour market. Moreover, there remains evidence of spare capacity in the labour market in many other indicators. For example, according to the single-month estimates, in May, hours worked were still 4.4% below the pre-pandemic level, while the employment rate of 75.1% was 1.5ppts below the pre-pandemic peak, the inactivity rate of 21.0% was still 1.0ppt above the pre-pandemic trough, and the unemployment rate (16+ years) of 4.8% was 1.3ppts above its trough. With the Business Insights and Conditions Survey suggesting that there were still about 5% of workers on either part-time or full-time furlough in late June, the Resolution Foundation estimates that there are still about 2.7mn workers not working as they had been ahead of the pandemic.

Pay growth figures still exaggerated by special factors

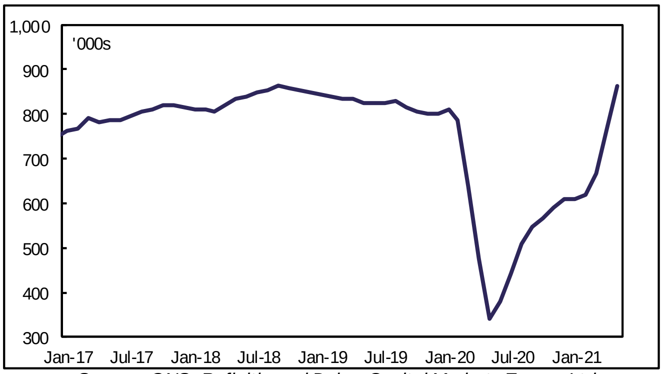
Once again, the labour market data brought some striking figures for wage growth. Growth in average total pay (including bonuses) in the three months to May rose 1.6ppts from the three months to April to 7.3%Y/Y with growth in regular pay

UK: Payrolls



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

UK: Vacancies



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

(excluding bonuses) up 0.9ppt to 6.6%Y/Y. However, these figures remain exaggerated by temporary factors, notably compositional and base effects. Indeed, BoE Governor Bailey recently noted that, even if the level of average earnings had been flat at April's level over the remainder of the year, the growth rate would peak close to 8%Y/Y. And the ONS estimates that base effects account for between 1.8-3.0ppts of the growth in pay, with the compositional effect perhaps adding a further 0.4ppt. So, it judges that the underlying rate of pay growth currently lies somewhere between 3.2-4.4%Y/Y, a range broadly consistent with (albeit perhaps slightly in excess of) that from the second half of 2018 until the pandemic. Notably, the median growth in pay settlements over recent quarters has remained close to 2½%, pointing to moderate wage growth going forward.

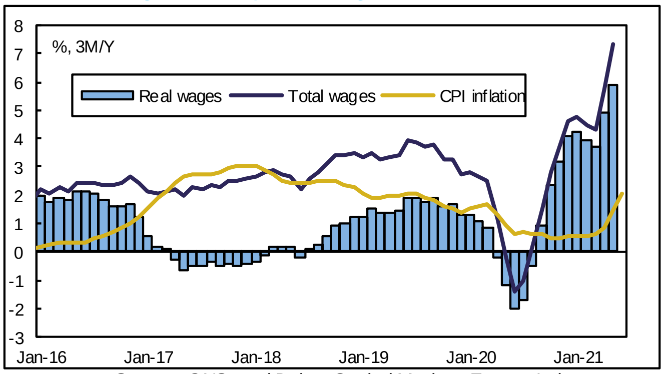
Saunders and Ramsden present case for tighter BoE monetary policy

The first public comments from an MPC member in the wake of yesterday's June figures for UK inflation – which were significantly above the BoE's May forecast path – came from Deputy Governor Jon Cunliffe and were measured. Among other things, he noted the difficulty of assessing the inflation outlook in current circumstances and that the BoE would make an updated assessment of the basis of the relative strength of supply and demand next month. However, yesterday evening Deputy Governor Dave Ramsden struck a rather more hawkish tone than of late. Among other things, he flagged the possibility that the pre-pandemic level of GDP could be surpassed in the present quarter, that the unemployment rate would peak lower than the BoE's forecast of close to 5½% in Q3, and that inflation could rise close to 4%Y/Y later this year. And noting that the downside risks to the outlook had diminished and the risks of inflation remaining persistently above-target had increased, he stated that he "can envisage the conditions for considering tightening being met somewhat sooner than … previously expected". This morning, for similar reasons, external MPC member Michael Saunders was even more explicit about the case for removing policy accommodation sooner rather than later. In particular, he said that he could see the case for curtailing QE in the next month or two rather than close to year-end under the current plans. And he also suggested that Bank Rate might need to be hiked (albeit by a limited amount) next year. So, while the previous lone hawk, former Chief Economist Haldane, has now left the MPC, at least two members appear now to be keen to be actively voting for a change to policy as soon as next month.

The day ahead in the UK

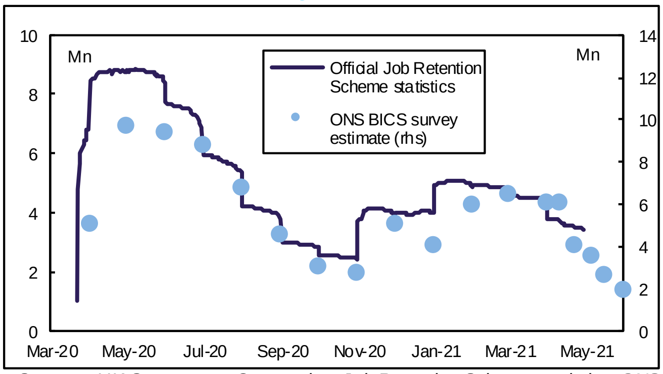
This week's economic calendar ends quietly in the UK, with no data releases or BoE speeches scheduled tomorrow.

UK: Average weekly earnings and inflation



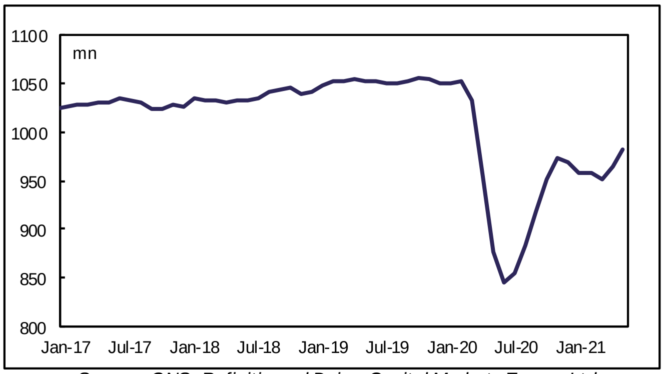
Source: ONS, and Daiwa Capital Markets Europe Ltd.

UK: Workers on furlough



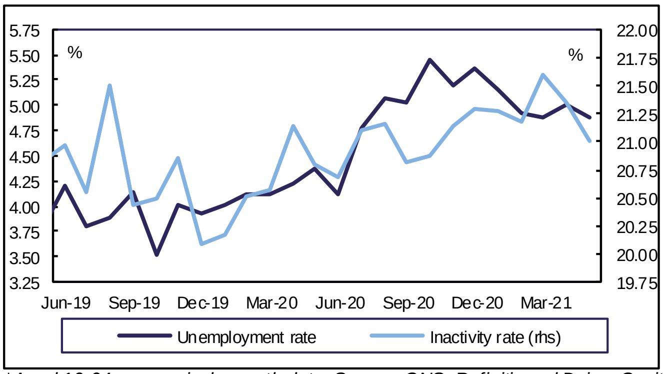
Source: UK Government Coronavirus Job Retention Scheme statistics, ONS and Daiwa Capital Markets Europe Ltd.

UK: Total actual weekly hours worked



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

UK Unemployment and inactivity rates*



**Aged 16-64 years, single-month data. Source: ONS, Refinitiv and Daiwa Capital Markets Europe Ltd.*

Euro area

The day ahead in the euro area

A quiet day for economic data from the euro area brought only the final Italian inflation figures for June, which confirmed the flash estimates. So, on the EU-harmonised HICP measure, the Italian headline rate rose 0.1ppt from May to 1.3%Y/Y, while the associated core rate (excluding energy, food, alcohol and tobacco) also rose 0.1ppt to a still-low 0.3%Y/Y. As in Italy, the final estimates of HICP inflation from Germany (down 0.3ppt to 2.1%Y/Y) and France (up 0.1ppt to 1.9%Y/Y) aligned with their respective flash estimates. So, despite an upwards revision in Spain (up 0.1ppt to 2.5%Y/Y), the final euro area figures due tomorrow will also likely 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. Within the detail, the preliminary release revealed that energy inflation eased back, dropping 0.6ppt from May's near-10-year high to a nevertheless still elevated 12.5%Y/Y. But an increase 0.5ppt in non-energy industrial goods inflation to 1.2%Y/Y (partly due to higher clothes prices but perhaps also broader supply-chain pressures) offset a drop of 0.4ppt to 0.7%Y/Y in services inflation (likely related in part to package tours). Beyond inflation, euro area trade data for May, also out tomorrow, are expected to reveal that growth in the value of imports exceeded that of exports for the fourth successive month. Consequently, the euro area's merchandise trade surplus on an adjusted basis is expected to narrow to a twelve-month low of €9.0bn. EU27 new car registrations for June are also due tomorrow.

European calendar

Today's results

Economic data

Country	Release	Period	Actual	Market consensus/ *Daiwa forecast*	Previous	Revised
Italy	Final CPI (EU harmonised CPI) Y/Y%	Jun	**1.3 (1.3)**	1.3 (1.3)	1.3 (1.2)	**-**
UK	Claimant count rate % (change 000s)	Jun	**5.8 (-114.8)**	- (-)	6.2 (-92.6)	**6.0 (-151.4)**
	ILO unemployment rate 3M%	May	**4.8**	4.7	4.7	**-**
	Employment change 3M/3M 000s	May	**25**	95	113	**-**
	Average wages (excluding bonuses) 3M/Y%	May	**7.3 (6.6)**	7.1 (6.6)	5.6 (5.6)	**5.7 (5.7)**

Auctions

Country	Auction
France	sold €4.46bn of 0% 2024 bonds at an average yield of -0.63%
	sold €2.57bn of 0% 2026 bonds at an average yield of -0.52%
	sold €1.82bn of 2.75% 2027 bonds at an average yield of -0.42%
	sold €1.65bn of 0.75% 2028 bonds at an average yield of -0.3%
	sold €995mn of 0.1% 2031 index-linked bonds at an average yield of -1.43%
	sold €735mn of 0.1% 2036 index-linked bonds at an average yield of -1.21%
Spain	sold €1.29bn of 0.25% 2024 bonds at an average yield of -0.473%
	sold €1.62bn of 0% 2028 bonds at an average yield of -0.082%
	sold €1.42bn of 0.5% 2031 bonds at an average yield of 0.354%
	sold €1.03bn of 4.2% 2037 bonds at an average yield of 0.673%

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

Tomorrow's releases

Economic data

Country	BST	Release	Period	Market consensus/ *Daiwa forecast*	Previous
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	8.0	9.4
Italy	09.00	Trade balance €bn	May	-	5.9

Auctions and events

- Nothing scheduled -

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

Access our research blog at:

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