

# Euro wrap-up

## Overview

- Bunds made modest gains as some positive euro area retail sales figures were counterbalanced by weak German auto sales and production data.
- Shorter-dated Gilts made modest losses as the final UK services PMIs were revised higher.
- Tomorrow brings the BoE's latest monetary policy announcements and updated economic forecasts. German factory orders and French IP data for June are also due.

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### Daily bond market movements

Bond	Yield	Change
BKO 0 06/23	-0.788	-0.008
OBL 0 10/26	-0.768	-0.010
DBR 0 08/31	-0.497	-0.013
UKT 0 <sup>1</sup> / <sub>8</sub> 01/23	0.055	+0.011
UKT 0 <sup>1</sup> / <sub>8</sub> 01/26	0.224	-0.001
UKT 4 <sup>3</sup> / <sub>4</sub> 12/30	0.515	-0.003

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

## Euro area

### Euro area retail sales jump in Q2

Despite a surge in [German retail sales](#) of 4.2%M/M, euro area retail sales growth in June was far more moderate at 'just' 1.5%M/M. Nevertheless, this still marked the second successive month of growth, having jumped 4.1%M/M in May as non-essential stores benefitted from easing lockdown restrictions. As such, this left sales 4.8% above the pre-pandemic level in February 2020, and up 4.0%Q/Q in Q2, more than fully reversing the 3%Q/Q decline in Q1. Moreover, the detail was even more encouraging, with spending on core items up 3.4%M/M, to be more than 8½% higher than the pre-pandemic level and up 7%Q/Q in Q2. Sales of auto fuel rose 3.8%M/M as travel continued to recover. In contrast, food store sales fell for the third consecutive month (-1.5%M/M) likely reflecting the easing of lockdowns and resumption of spending on eating out. Among the member states, the strongest growth in sales was seen in Ireland (9.4%M/M), while France (1.2%M/M) followed Germany in seeing sales move further above their pre-pandemic level. Growth in Italy (0.7%M/M) and Spain (0.5%M/M) was more modest, leaving sales still some way below the February 2020 levels (1.6% and 3.9% respectively). Looking ahead, the modest easing in consumer confidence raises some downside risks to the near-term spending outlook, and it remains to be seen to what extent spending on goods might be substituted for increased spending on services through the summer months. Nevertheless, the recent decline in coronavirus cases in Spain, signs of a peak in French cases, and ongoing progress with vaccination programmes give cause for encouragement. Moreover, in light of the recent monthly profile, even if retail sales were flat in July through September, they would still be up more than 2%Q/Q in Q3.

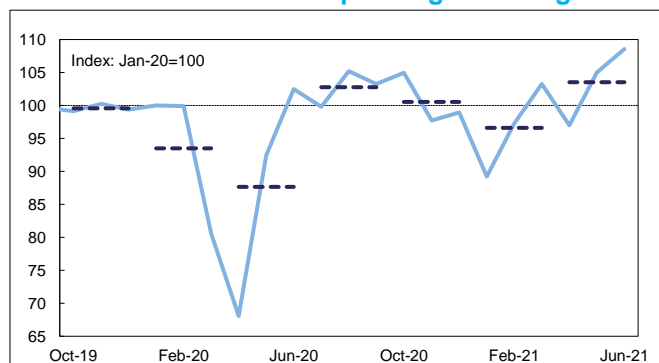
### German car registrations and production remain subdued at start of Q3

While demand will likely remain robust, supply bottlenecks will continue to hamper sales of certain items over the near term. This certainly remains the case in the auto sector, and was evident in today's German car registrations, which fell 24.9%Y/Y in July. While the weakness was clearly exacerbated by base effects associated with the temporary VAT cut last year, sales were also 29% lower than their level in July 2019 and represented the lowest July outturn since 1989. Production of German autos remained subdued in July too, similarly down 25%Y/Y and 30% lower than in July 2019. Indeed, production in the first seven months of the year was up just 7% compared with the same period in 2020 and down almost 40% compared with the average equivalent period in the decade up to the pandemic.

### Euro area services PMI signals accelerated recovery momentum

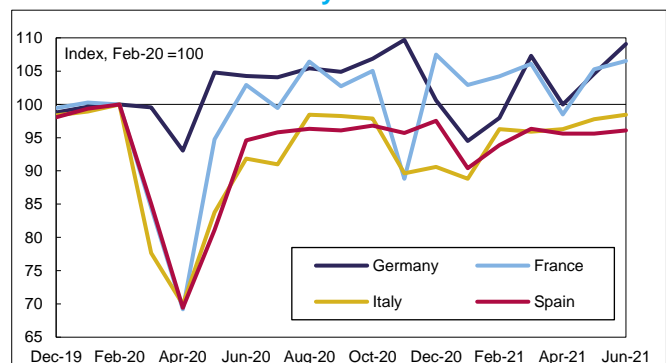
According to the PMIs, the recovery in the services sector gathered momentum at the start of the third quarter. Admittedly, today's final services activity index was revised a touch lower from the preliminary estimate (-0.6pt) to 59.8, but this still marked an increase of 1.5pts from June and the highest reading since mid-2006. While also downwardly revised from the

#### Euro area: Retail sales – spending on core goods\*



\*Dashed lines represent quarterly average. Source: Refinitiv and Daiwa Capital Markets Europe Ltd.

#### Euro area: Retail sales by member state



Source: Refinitiv and Daiwa Capital Markets Europe Ltd.

initial release, firms in the sector reported solid new business – the relevant index, 59.3, was the highest for 14 years – supported by a revival in services exports as international travel resumed. With operating capacities again under pressure in July, firms in the sector reported the strongest jobs growth for almost three years. And while still elevated, the survey hinted that input price inflation might well have reached its peak – the relevant PMI eased 0.1pt to 63.1 – with the output prices PMI also moderating very slightly too (down 0.3pt to 55.4). At the country level, the improvement in July was driven by Germany, which, despite coming in a touch softer than the flash estimate, saw the services activity index jump 4.3pts to 61.8, a series high. Perhaps reflecting the rise in coronavirus infections that month, the French services PMI fell 1pt in July to 56.8, still high but the lowest of the member states. The Italian services PMI, meanwhile, rose for the third consecutive month to 58.0, the highest reading for 14 years. And while the equivalent Spanish index slipped back slightly, at 61.9, it was the second-strongest reading since early 2000.

### Composite output PMI highest in 15 years, price indices at series highs

Overall, the euro area's final composite output PMI was similarly revised slightly lower from the flash, to 60.2, still up 0.7pt from June and the highest in just over 15 years. And a further improvement in the composite new orders balance (60.3) to the highest in 21 years bodes well for the near-term outlook too. But, despite a further reported increase in job creation – the employment PMI was the strongest since mid-2000 – firms reported a record rise in outstanding business and extended the current period of backlog accumulation to five months. Against this backdrop, price pressures remained elevated, with the composite input and output price indices at survey highs.

### The day ahead in the euro area

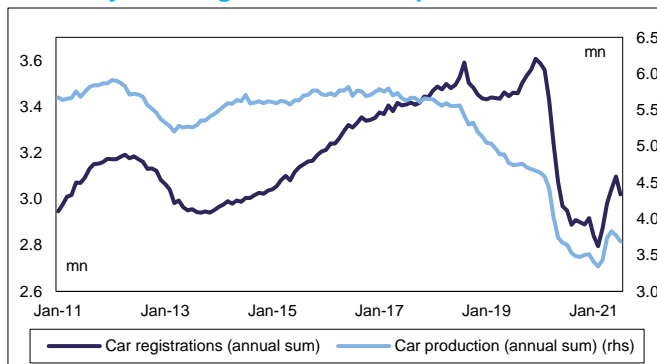
Tomorrow concludes the release of the activity PMIs for July, with the construction sector surveys likely to report that output growth remains constrained in the largest three member states by material shortages and increased costs. Focus will also be on the manufacturing sector, with German factory orders and French IP data for June due for release. While the anticipated rebound in German orders would not fully offset the 3.7%M/M drop in May, this would still leave orders up more than 3½%Q/Q in Q2. In France, meanwhile, production is expected to have fully reversed the 0.3%M/M decline in May.

## UK

### Services PMIs revised up significantly, but still point to a loss of momentum in the sector

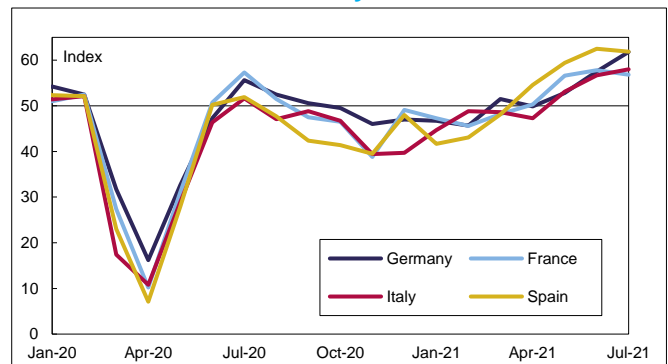
Ahead of tomorrow's monetary policy announcement from the BoE, today's final services PMIs for July provided an updated snapshot of activity at the start of Q3. Happily, the indicators were significantly revised upwards from the preliminary

#### Germany: Car registrations and production



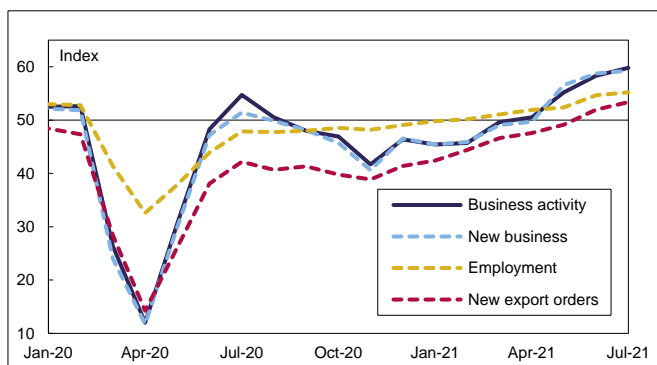
Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

#### Euro area: Services PMIs by member state



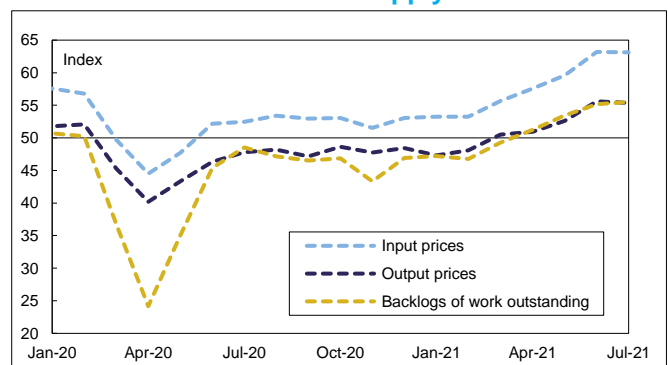
Source: Refinitiv, Markit and Daiwa Capital Markets Europe Ltd.

#### Euro area: Services PMIs – demand side



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

#### Euro area: Services PMIs – supply side



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

estimates. Indeed, the headline services activity PMI was revised up a substantive 1.8pts to a respectable 59.6. That, however, still marked a drop of 2.8pts from June and suggested the softest growth in the sector since March. Moreover, supply constraints and staff shortages were assessed to be more acute than suggested in the preliminary report, with the index of work backlogs in services revised up more than 2pts from the flash estimate, and a level rarely surpassed on the series. And so, price pressures were also judged to have intensified more than previously thought, with the input and output price PMIs both revised up to new series highs. In addition to the impact of supply bottlenecks, a slowdown in housing market transactions, following the tapering of the government's stamp duty holiday last month, was also cited as a factor weighing on services activity. While the respective survey indicator was also revised up from the preliminary report, new business growth was judged to be the softest since February despite an upturn in demand from abroad related to the easing of travel restrictions.

### Composite output PMI down to four-month low as supply bottlenecks bite

In light of the upwards revisions to the services indices, the composite PMIs were also nudged higher from the flash estimates. So, for example, the composite output PMI was revised up a sizeable 1.5pts. But that still left it at a four-month low of 59.2, down 3pts from June. Notably, the survey points to a loss of momentum in manufacturing and services, with supply bottlenecks weighing on activity in both sectors. While the increased backlogs of work should support growth in Q3, the softening of new orders growth points to some slowing into Q4 when the government's support for the economy will be removed. And while the survey suggests the steepest rises in prices charged across the private sector in more than two decades, the softening of growth momentum would seem likely to help ensure that such pressures remain transitory. Overall, therefore, the PMIs are unlikely to prompt a more hawkish response from most members of the MPC at tomorrow's meeting.

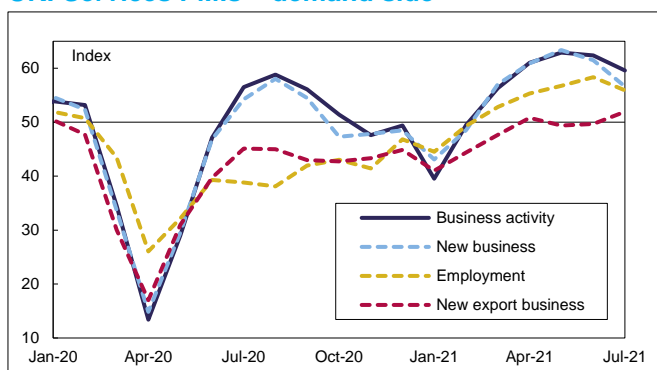
### The day ahead in the UK

All eyes in the UK tomorrow will be on the BoE's latest monetary policy announcement. Hawkish noises from two MPC members – Deputy Governor Ramsden and, in particular, external member Saunders – recently suggested that there was a risk that the QE programme might be brought to an early end at this meeting. However, since then, Deputy Governor Broadbent, and external members Haskel and Vlieghe – the latter for whom this will be the final MPC meeting – have suggested that they see no need to tighten policy yet. And so, we expect the asset purchase target to be left unchanged at £895bn, with the full amount to be reached before the end of the year. The MPC will also maintain its forward guidance, stating 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 sustainably”. The decision not to curtail QE early will reflect the BoE's updated economic forecasts. While both the near-term profile for GDP and inflation will be revised higher than expected in May, the BoE will continue to forecast GDP to slow and inflation to fall back in 2022 to be close to target by the end of the projection horizon.

It is possible – but far from certain – that the BoE will also announce the outcome of its review of its tightening strategy. Up to now, the Bank has stated that it would not start to unwinding quantitative easing before Bank Rate has reached 1.5%. It is possible that the Bank could lower that threshold for Bank Rate, for example to 1.0%, while maintaining rate hikes as the primary tool for tightening policy. Alternatively, it could announce a far more flexible approach, giving itself scope to adjust the mix and sequence of rate hikes and reductions in the stock of purchased assets according to how economic and financial market conditions unfold.

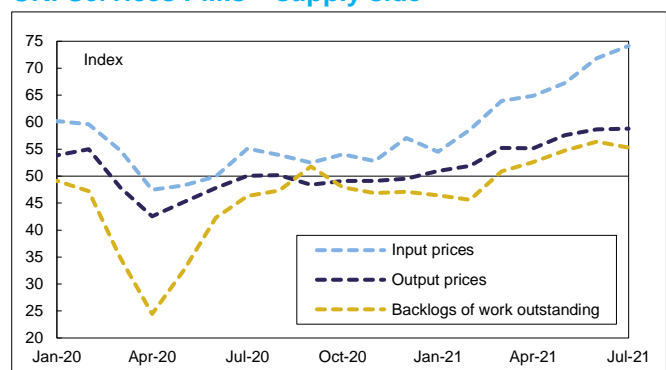
In terms of data, tomorrow will bring UK car registration numbers for July, which are likely to show another solid month of annual growth due to base effects but may also highlight how ongoing supply constraints continue to limit sales. Like the [manufacturing](#) and services PMIs, the equivalent construction survey – also due tomorrow – might also see the headline activity index fall back from the 24-year high (66.3) recorded in June.

#### UK: Services PMIs – demand side



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

#### UK: Services PMIs – supply side












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

# European calendar

## Today's results

### Economic data

Country	Release	Period	Actual	Market consensus/ <i>Daiwa forecast</i>	Previous	Revised
Euro area	 Final services (composite) PMI	Jul	<b>59.8 (60.2)</b>	60.4 (60.6)	58.3 (59.5)	-
	 Retail sales M/M% (Y/Y%)	Jun	<b>1.5 (5.0)</b>	1.7 (4.4)	4.6 (9.0)	<b>4.1 (8.6)</b>
Germany	 Final services (composite) PMI	Jul	<b>61.8 (62.4)</b>	62.2 (62.5)	57.5 (60.1)	-
	 New car registrations Y/Y%	Jul	<b>-24.9</b>	-	24.5	-
France	 Final services (composite) PMI	Jul	<b>56.8 (56.6)</b>	57.0 (56.8)	57.8 (57.4)	-
Italy	 Services PMI (composite)	Jul	<b>58.0 (58.6)</b>	58.3 (59.1)	56.7 (58.3)	-
	 Retail sales M/M% (Y/Y%)	Jun	<b>0.7 (7.7)</b>	1.9 (-)	0.2 (13.3)	<b>-0.1 (13.6)</b>
Spain	 Services (composite) PMI	Jul	<b>61.9 (61.2)</b>	63.3 (63.0)	62.5 (62.4)	-
UK	 Final services (composite) PMI	Jul	<b>59.6 (59.2)</b>	57.8 (57.7)	62.4 (62.2)	-



### Auctions

Country	Auction
Germany	 sold €3.27bn of 0% 2026 bonds at an average yield of -0.76%


Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

## Yesterday's results

### Economic data












Country	Release	Period	Actual	Market consensus/ <i>Daiwa forecast</i>	Previous	Revised
Euro area	 PPI Y/Y%	Jun	<b>10.2</b>	10.3	9.6	-
Spain	 Unemployment change '000s	Jul	<b>-197.8</b>	-	-166.9	-

### Auctions











Country	Auction
UK	 sold £2bn of 1.25% 2051 bonds at an average yield of 0.972%

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

**Tomorrow's releases**
**Economic data**

Country	BST	Release	Period	Market consensus/ <i>Daiwa forecast</i>	Previous
Euro area		08.30 Construction PMI	Jul	-	50.3
Germany		07.00 Factory orders M/M% (Y/Y%)	Jun	2.0 (22.9)	-3.7 (54.3)
		08.30 Construction PMI	Jul	-	47.0
France		07.45 Industrial production M/M% (Y/Y%)	Jun	0.5 (7.5)	-0.3 (20.5)
		07.45 Manufacturing production M/M% (Y/Y%)	Jun	1.4 (-)	-0.5 (22.3)
		08.30 Construction PMI	Jul	-	48.9
Italy		08.30 Construction PMI	Jul	-	57.9
UK		09.00 New car registrations Y/Y%	Jul	-	28.0
		09.30 Construction PMI	Jul	64.0	66.3
		12.00 BoE Bank Rate %	Aug	<u>0.10</u>	0.10
		12.00 BoE Gilt purchases target £bn	Aug	<u>875</u>	875

**Auctions and events**

Euro area		09.00 ECB publishes Economic Bulletin
France		09.50 Auction: 1.5% 2031 bonds
		09.50 Auction: 5.75% 2032 bonds
		09.50 Auction: 1.25% 2034 bonds
Spain		09.30 Auction: 0% 2024 bonds
		09.30 Auction: 0% 2026 bonds
		09.30 Auction: 0.5% 2031 bonds
		09.30 Auction: 1% 2030 index-linked bonds
UK		12.00 BoE monetary policy announcement and publication of Monetary Policy Report
		12.00 BoE publishes monthly Decision Maker Panel data

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

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