

# Euro wrap-up

## Overview

- While euro area industrial production bounced back in May and investors were more upbeat about the German economic outlook, Bunds made modest gains.
- Gilts followed USTs lower ahead of BoE Governor Bailey's annual speech at Mansion House, while a UK retail survey signalled a rebound in sales volumes in June.
- Wednesday will bring UK inflation figures for June and euro area goods trade numbers for May.

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### Daily bond market movements

Bond	Yield	Change
BKO 1.9 09/27	1.878	-
OBL 2.2 10/30	2.263	-0.012
DBR 2.6 08/35	2.714	-0.012
UKT 3% 03/27	3.836	+0.031
UKT 4% 03/30	4.040	+0.030
UKT 4½ 03/35	4.635	+0.035

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

Source: Bloomberg

## Euro area

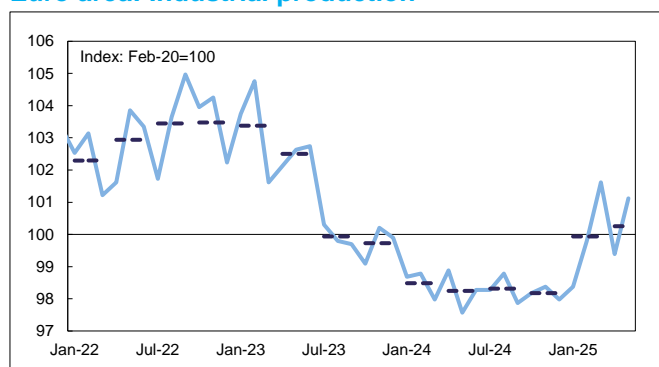
### Euro area industrial production boosted by rebound in pharmaceuticals and autos

As we expected after the rebound in Germany and Ireland, euro area industrial production returned to growth in May, by 1.7%M/M, to mark the fourth monthly increase out of five and take the level to its second highest in almost two years. That also left output up a decent 3.7%Y/Y – the most since September 2022 – and trending some 0.3% above the Q1 average. Admittedly, like in Q1, growth in May was more than accounted for by Germany (2.2%M/M) and Ireland (12.4%M/M). Indeed, when excluding those member states, aggregate output across the remainder of the euro area fell for a second consecutive month (-0.5%M/M). And while total manufacturing production similarly rose sharply that month (1.4%M/M), the rebound was driven by only a few sectors and principally by a marked bounce back in pharmaceuticals (27.7%M/M). Production of ICT equipment also rose (4.9%M/M) to a 17-month high. As such, despite a pull-back in food and furniture, this took output of consumer goods to a new series high, some 10% higher than a year earlier. There was also a notable increase in autos production (5.2%M/M) to a 13-month high, to be tracking a sizeable 6½% above the Q1 average. In contrast, intermediate goods output fell for a second-successive month and by the most since January 2024 (-1.7%M/M), with chemicals and basic metals output the weakest since the global financial crisis. And with the oil price having temporarily spiked in June, we might see production from energy-intensive subsectors fall further at end-Q2. When excluding the energy-intensive subsectors, euro area industrial output in May was the highest for more than two years. And with persisting uncertainties surrounding the EU-US trade negotiations, manufacturers might have continued to front-load production in June, particularly in those subsectors most exposed to the threats of additional US tariff hikes.

### ZEW investor survey most upbeat about the outlook since Russia's invasion of Ukraine

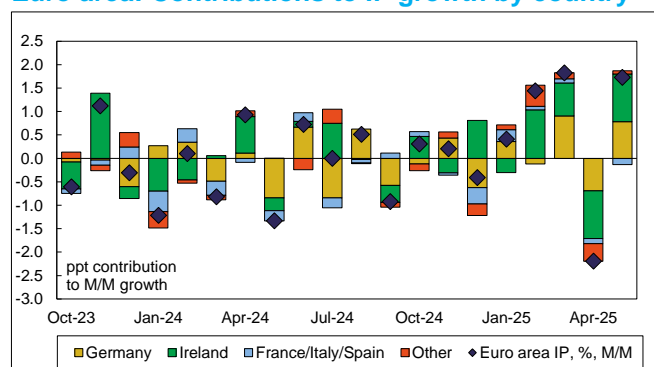
Today's ZEW investor survey was also more encouraging with respect to the near-term German economic outlook, signalling ongoing recovery at the start of Q3 with the prospect of higher public sector spending on defence and infrastructure seemingly offsetting geopolitical and trade risks. Indeed, the survey's current conditions index jumped a further 12.5pts in July – the most since April 2023 – to the highest level for two years. Nevertheless, just 3% of respondents considered conditions to be 'good' this month, with almost two-thirds judging them still to be 'bad'. Moreover, the net balance in (-59.5) was still below the average of the past five years (-54) and substantially lower than the norm in the five years before the pandemic (+54). But investors were also more upbeat about the outlook for the coming six months, with the respective net balance (+52.7) rising to the highest level since the Russian invasion of Ukraine. This in part reflected a further improvement in profit expectations. Indeed, while they were still broadly negative for those sectors most exposed to the highest US tariffs, including autos and steel, the outlook was considered not as downbeat as in the first half of the year. Investors expressed greater optimism about the outlook for many other sectors, including electronics and IT services. And while President

### Euro area: Industrial production\*



Source: Macrobond and Daiwa Capital Markets Europe Ltd.

### Euro area: Contributions to IP growth by country



Source: Macrobond and Daiwa Capital Markets Europe Ltd.

Lagarde recently stated that the ECB's easing cycle is near or at an end, the impact of past easing was still expected to benefit the construction sector going forward too.

## The day ahead in the euro area

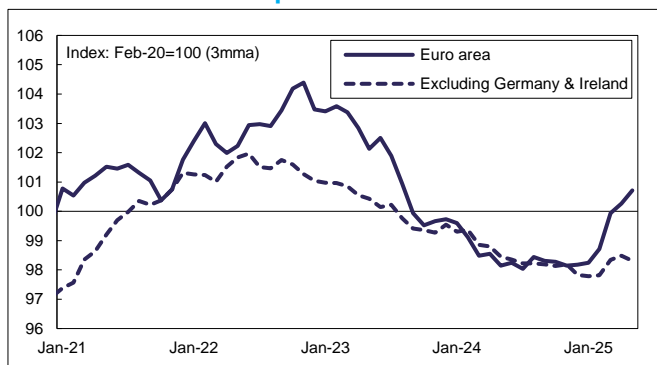
Tomorrow will bring euro area goods trade figures for May. Notwithstanding the rebound in industrial output and significant uncertainty surrounding the Irish trade data, [German and French](#) figures previously published strongly suggest that exports fell for a second successive month in May. Nevertheless, the euro area trade surplus is likely to have widened that month as the decline in imports outstripped that of exports. Wednesday will also bring final June Italian inflation figures ahead of the aggregate euro area detail on Thursday.

## UK

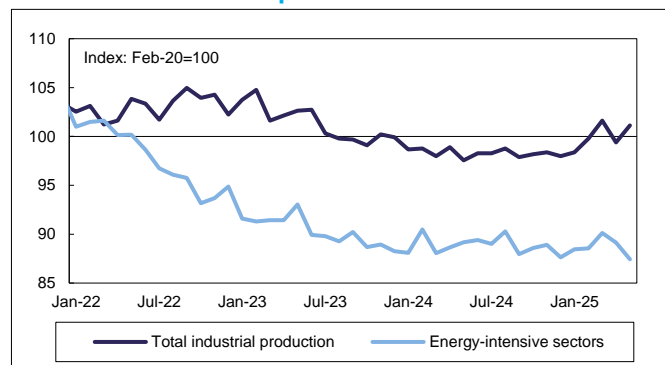
### BRC retail sales values boosted by warm weather and higher food prices

Given the extent of the drop in May – [retail sales](#) having fallen the most in any month since December 2023 – the return of the sunshine in June and the recent recovery in consumer confidence, we expect household spending to return to growth at the end of Q2. This view was reinforced by today's BRC retail monitor, with growth of total sales values accelerating 2.1ppts to 3.1%Y/Y and like-for-like sales up to 2.7%Y/Y, the strongest readings in six months when excluding the Easter-distorted surge in April. Demand for electrical appliances – such as fans – and sporting and leisure equipment was boosted by warm weather, while furniture, computing and health and beauty items also contributed positively. According to the BRC survey, the largest chunk of retail spending was attributed to food sales growth, which rose 0.6ppt to 4.1%Y/Y. But this in part reflected the recent surge in food price inflation – indeed, the BRC's measure of food shop price inflation rose (3.7%Y/Y) the most in fifteen months. This notwithstanding, adjusting for prices, the BRC's measure of sales volumes – up 1.6ppts to 2.7%Y/Y – suggests that retail sales bounced back this month. As such, when the official retail sales figures are published on 25 July, we expect them to show that the retail sector contributed positively to GDP growth in Q2, albeit likely to lesser extent than in Q1 (1.2%Q/Q).

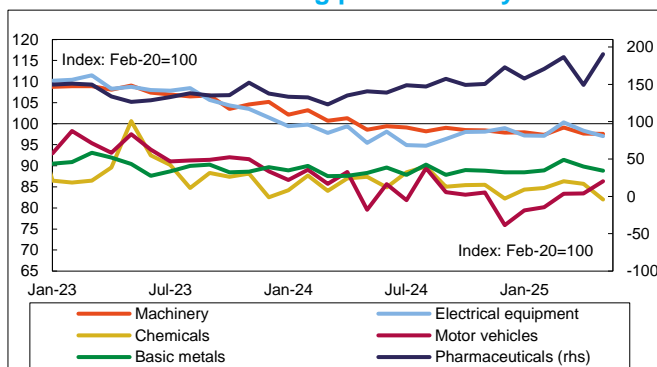
### Euro area: Industrial production



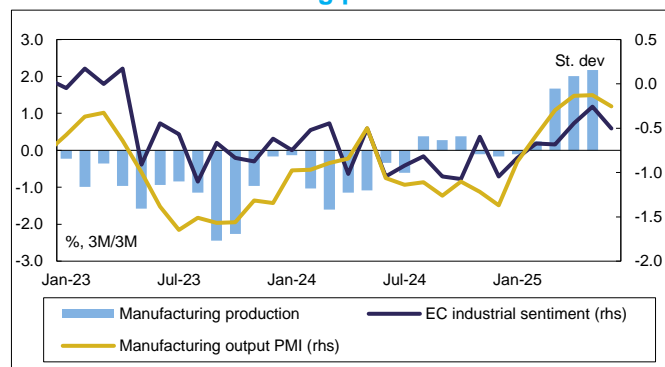
### Euro area: Industrial production



### Euro area: Manufacturing production by subsector



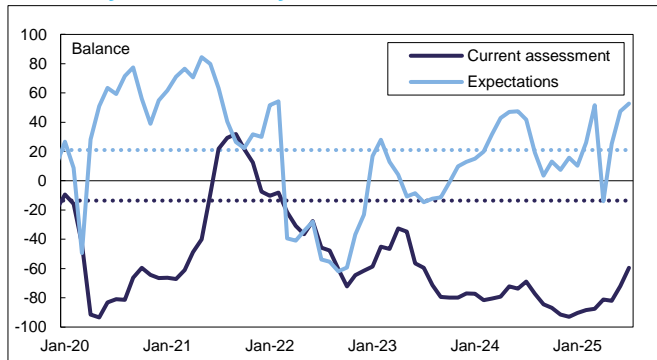
### Euro area: Manufacturing production & PMIs



## The day ahead in the UK

As markets and investors scrutinise tonight's speech by BoE Governor Bailey at Mansion House for any hints for the near-term policy adjustments – to both interest rates and asset purchase programme – tomorrow will also bring June inflation figures, the final reading ahead of the August MPC meeting. Inflation has tracked close to the BoE forecasts in recent months. Indeed, both headline (3.4%Y/Y) and services (4.7%Y/Y) inflation in May aligned with its projection. We, like the BoE, expect headline inflation in June to move sideways. But with the uptick in fuel prices late last month bound to decrease the drag from energy, the BoE may not be surprised by a slight surprise on the upside. We also note the upside risks from food, with the BRC survey flagging more pressure in that component in June after it already overshot the Bank's projection significantly in May. Ultimately, however, we see more downside risks in the services categories to underpin our expectations for June's sidestep in the headline CPI rate despite the possibility of a slight uptick in core goods inflation.

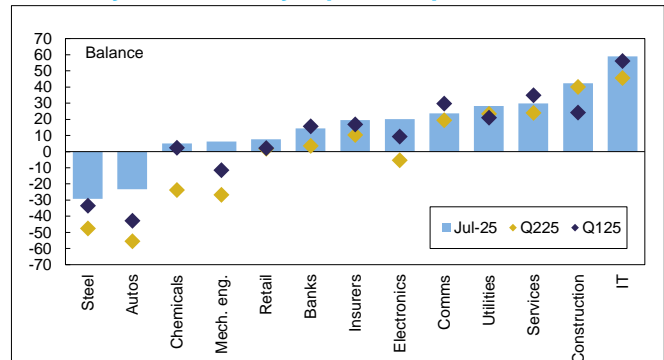
### Germany: ZEW survey – sentiment indices\*



\*Dotted lines represent long-run average.

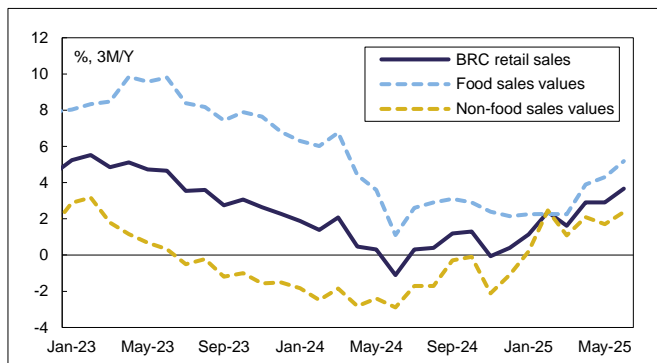
Source: Macrobond and Daiwa Capital Markets Europe Ltd.

### Germany: ZEW survey – profit expectations



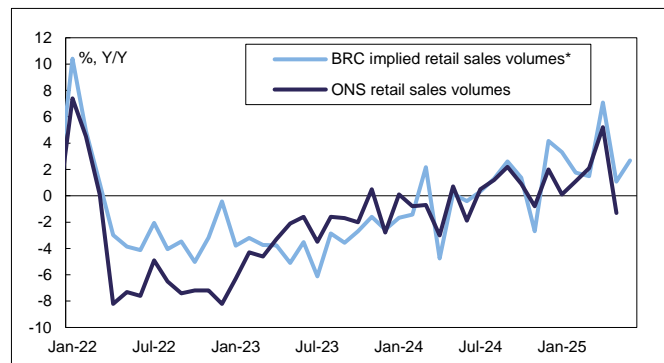
Source: Macrobond and Daiwa Capital Markets Europe Ltd.

### UK: BRC retail sales values



Source: Macrobond and Daiwa Capital Markets Europe Ltd.

### UK: Retail sales volumes



\*Adjusted with BRC shop price inflation.

Source: Macrobond 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	Industrial production M/M% (Y/Y%)	May	1.7 (3.7)	1.5 (3.3)	-2.4 (0.8)	-2.2 (0.2)
Germany	ZEW current situation (expectations) balance	Jul	-59.5 (52.7)	-66.0 (50.7)	-72.0 (47.5)	-
Spain	Final HICP (CPI) Y/Y%	Jun	2.3 (2.3)	2.2 (2.2)	2.0 (2.0)	-
UK	BRC retail monitor – like-for-like sales Y/Y%	Jun	2.7	1.0	0.6	-

### Auctions

Country	Auction
Germany	sold €3.899bn of 2027 bonds at an average yield of 1.87%
UK	sold £1bn of 4.25% 2032 bonds at an average yield of 4.161%

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	10.00	Trade balance €bn	May	14.0	14.0
Italy	09.00	Final HICP (CPI) Y/Y%	Jun	1.7 (1.7)	1.7 (1.6)
UK	07.00	Headline (core) CPI Y/Y%	Jun	3.4 (3.4)	3.4 (3.5)
	09.30	House price index Y/Y%	May	-	3.5

### Auctions and events

Germany	10.30	Auction: to sell €1.5bn of 2.9% 2056 bonds
	10.30	Auction: to sell €1bn of 1.25% 2048 bonds
UK	10.00	Auction: to sell £1.5bn of 4.5% 2034 bonds

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

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