

Euro wrap-up

Overview

- Bunds made losses as German IP beat expectations in May, while OATs underperformed slightly as far-right Marine Le Pen was cleared to contest next year's Presidential Election albeit with electronic monitoring.
- While the BoE proposed to ease bank capital rules, Gilts also made losses.
- Thursday will bring the ECB's account of its June policy meeting, while German goods trade data for May and a UK survey on housing market activity are also due.

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Daily bond market movements

Bond	Yield	Change
BKO 2½ 06/28	2.576	+0.039
OBL 2½ 04/31	2.698	+0.044
DBR 2.9 02/36	2.986	+0.040
UKT 4¾ 03/28	4.161	+0.038
UKT 4¾ 03/31	4.351	+0.043
UKT 4¾ 10/35	4.832	+0.040

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

Euro area

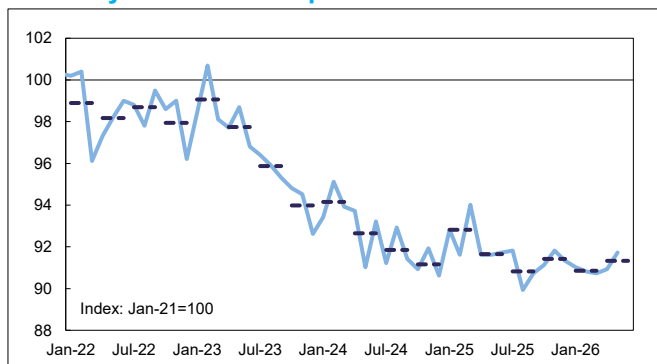
German industry exceeds expectations in May, on track to modestly support GDP in Q2

A stronger-than-expected rise in German industrial production in May, together with firmer factory orders and improving business sentiment, suggests that the economy in Q2 has proved more resilient than previously feared. Today's release reported a second successive monthly increase in output, by 0.9%M/M, taking the level to a six-month high. And that left IP on track in Q2 to largely reverse the 0.6% decline recorded in Q1. The improvement in May was broad-based, with manufacturing output rising for a third month in four and energy production up for a fifth month in six. Admittedly, much of the gain in manufacturing in May reflected a partial rebound in autos (3.1%M/M), which left output in that sector still trending roughly 3% below its Q1 average. Nevertheless, ongoing demand linked to AI-related activity appeared to drive another solid increase in ICT equipment (2.3%M/M). And despite some payback in general and electrical machinery, output in both subsectors maintained a gradual uptrend too. Elsewhere, production of weapons and ammunition surged (19%M/M) to a new series high thanks to increased government defence spending. And despite the energy-intensive nature of the sector, chemicals output rose for a fifth consecutive month, supported in part by higher production of fertilizers amid ongoing supply constraints due to events in the Middle East. Meanwhile, construction activity remained surprisingly firm, rising for a third consecutive month (0.9%M/M) to the highest level in 16 months. While housebuilding and civil engineering edged slightly lower in May, they were still tracking an impressive 2½% and 6½% above their respective Q1 average levels.

Supply constraints cloud near-term outlook, but order backlogs remain supportive

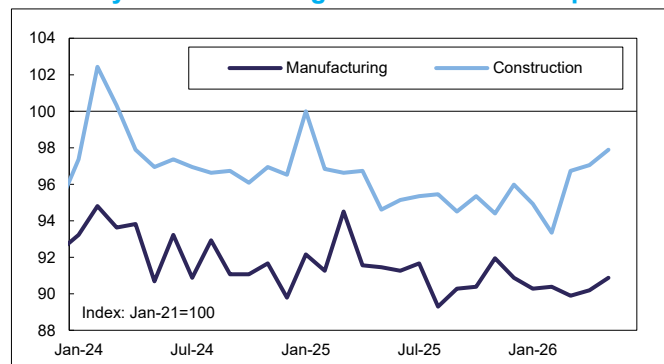
Surveys suggest that manufacturing output was relatively subdued in June, as supply constraints increasingly took their toll. Indeed, an ifo institute survey published today suggested that, despite the gradual reopening of the Strait of Hormuz, almost one third of firms in the chemicals sector reported difficulties sourcing inputs. Conditions also deteriorated sharply for ICT equipment producers amid a worsening shortage of semiconductors. And while industrial gas consumption was almost 10% higher than a year earlier in June to suggest that energy output remained buoyant, truck toll mileage also data point to a moderation in manufacturing activity at the end of Q2. Nevertheless, in many subsectors, the outlook for German manufacturers looks more promising provided supply constraints ease. In April, manufacturers' order books were equivalent to more than 8½ months of production, while core new factory orders in May rose to the highest level in three years. Order backlogs remain particularly elevated in the electrical and ICT equipment sectors and continue to trend higher in non-auto transport equipment. But autos manufacturers continue to face severe challenges from Chinese competition and shifting consumer preferences. According to Germany's auto association VDA, the rise in production (6%Y/Y) and registrations (16%Y/Y) in June was flattered by extra working days compared to a year earlier. Production in the first half of 2026 was down 3%YTD/Y due to weaker exports, while the rise in new car registrations was driven largely by foreign brands.

Germany: Industrial output*



*Dashed dark blue lines represent quarterly average.
Source: Macrobond and Daiwa Capital Markets Europe Ltd.

Germany: Manufacturing & construction output



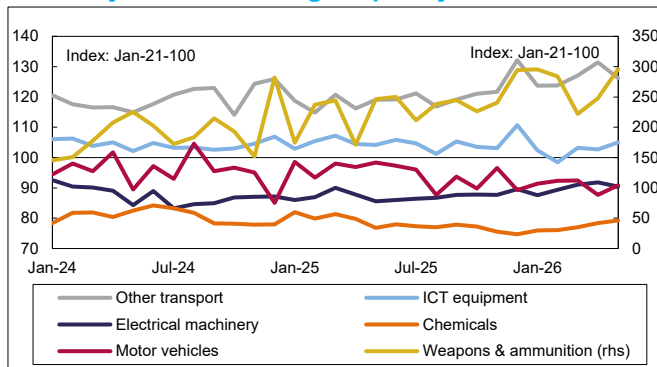
Source: Macrobond and Daiwa Capital Markets Europe Ltd.

The two days ahead in the euro area

While Wednesday should be a quiet day for euro area economic news, French political uncertainty should remain in the spotlight. OATs underperformed on Tuesday, albeit only very slightly, on news that the Court of Appeal of Paris had reduced the ban of far-right leader Marine Le Pen on standing for public office from five years to 15 months (plus 30 months suspended), backdated to last March. That effectively cleared her to contest next year's Presidential election. But the Court also upheld her conviction for embezzling EU funds, handing down a reduced three-year prison sentence, of which two years would be suspended and one spent wearing an electronic bracelet. Le Pen previously stated that she would not stand for the Presidency if required to wear such a monitoring device. Le Pen is scheduled to speak publicly this evening (Tuesday 8pm CET) when she will likely clarify her plans for the election. If she chooses to run, then she will surely receive the backing of her party, the National Rally (RN). If not, her protégé and current RN President Jordan Bardella will take her place.

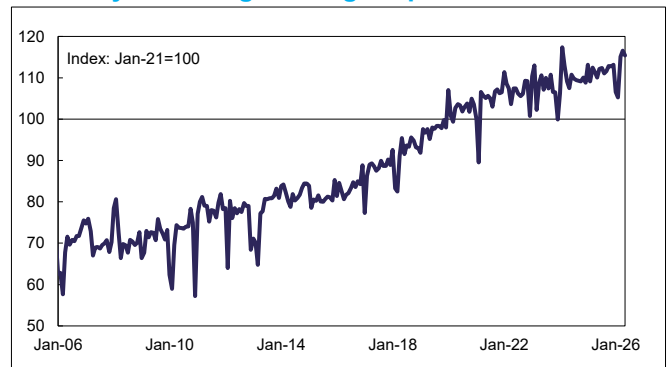
Polls suggest that the choice of candidate might be inconsequential in determining whether the RN candidate will reach the second-round run-off stage of the election, as whichever of the two stands would likely come first in the first round with more than 30% of the vote. But Bardella has recently gained higher poll ratings, with his more pro-business rhetoric and TikTok-friendly persona arguably setting him up as the more competitive of the two in a second-round run-off, which we currently expect to be against a soft-left or centre-right challenger (such as Le Havre Mayor Edouard Philippe). Some investors might hope that Bardella would also be more likely than Le Pen to take his cue from Italian Prime Minister Meloni and advocate a

Germany: Manufacturing output by subsector



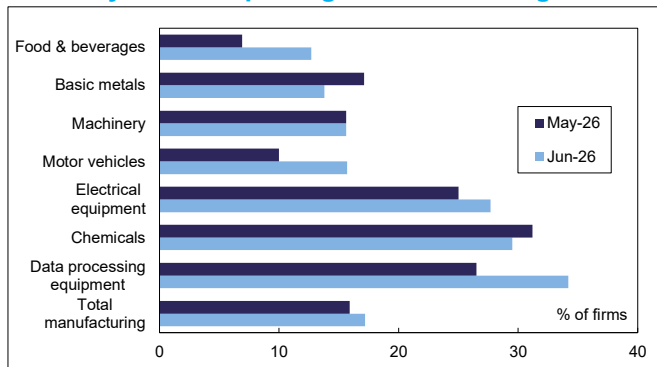
Source: Macrobond and Daiwa Capital Markets Europe Ltd.

Germany: Civil engineering output



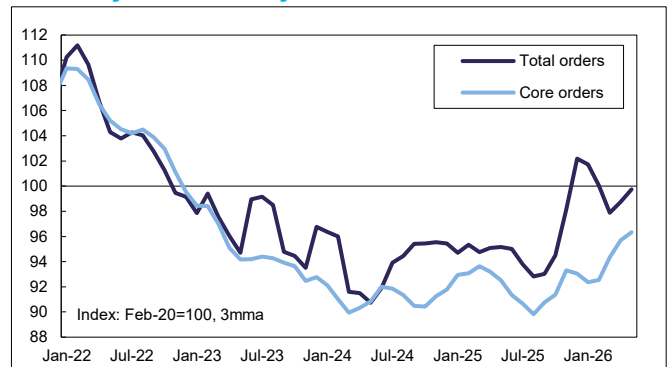
Source: Macrobond and Daiwa Capital Markets Europe Ltd.

Germany: Firms reporting material shortages



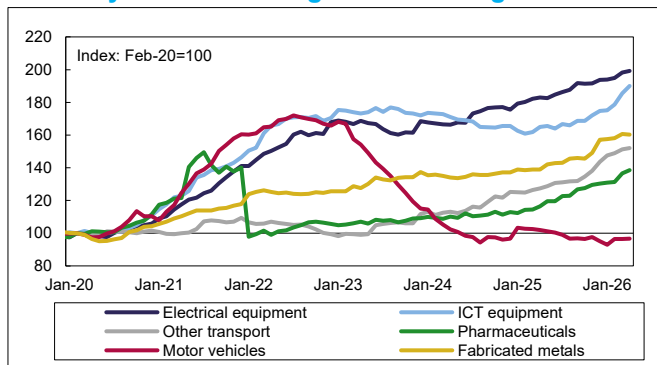
Source: ifo institute, Macrobond and Daiwa Capital Markets Europe Ltd.

Germany: New factory orders*



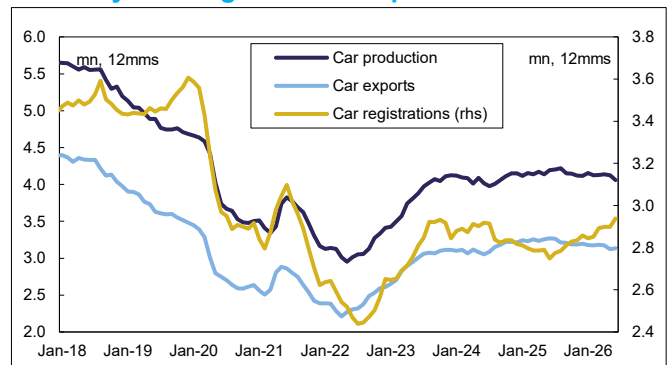
*Core orders exclude large-scale orders.
Source: Macrobond and Daiwa Capital Markets Europe Ltd.

Germany: Manufacturing order backlogs



Source: Macrobond and Daiwa Capital Markets Europe Ltd.

Germany: Car registrations & production



Source: VDA, Bloomberg and Daiwa Capital Markets Europe Ltd.

relatively conservative fiscal policy. But we doubt that either Bardella or Le Pen, or any administration backed by them, would have a credible plan for reducing the budget deficit, which remains on track to remain above 5% of GDP this year. We also suspect that the next French parliament could be as divided as the current one, making continued fiscal policy paralysis beyond next year the most likely scenario. And a President Bardella or Le Pen would be likely to obstruct constructive policy-making at the EU level, inhibiting growth-enhancing structural reforms such as deepening of the Single Market. So, even if Le Pen decides not to stand to leave the path clear for Bardella, we still see the likelihood of underperformance of OATs as next year's Presidential election gradually approaches.

Meanwhile, data-wise, Thursday's German goods trade release will show whether the rebound in autos production in May was also reflected in higher exports that month. German export values rose for three consecutive months to a 3½-year high in April. But the most recent gains look to have been flattered by higher prices while costlier oil imports saw Germany's goods trade surplus narrow to an 18-month low (€14.4bn). Higher oil prices are likely to have remained a headwind in May, as today's French data suggested. Indeed, faced also with the challenge of weaker exports to the US, France's bilateral trade deficit with the US reached its widest in 3½ years. But that was at least offset by a boost in shipments to China, which might hint towards some commensurate support for German manufacturers.






Finally, Thursday's release of the ECB's account of its June Governing Council meeting – which saw it revise up its baseline inflation forecast and unanimously agree a first rate hike since 2023 – will also be of some interest. However, the subsequent decline in energy prices has arguably reduced its relevance for future policy debate, with policymakers at Sintra last week suggesting that they were in no rush to tighten again as soon as July's meeting.

The two days ahead in the UK

The UK economic calendar will remain fairly sparse over the coming two days. Wednesday will bring the findings of one UK jobs survey, while Thursday is likely to bring another downbeat assessment of housing market activity from RICS' surveyors. Data aside, Thursday will also formally kick off the Labour Party leadership contest, albeit with Andy Burnham still the only Labour MP to have formally declared his intention to enter the ballot. It also seems improbable that any other MP will garner the necessary support to put their name forward before the following Thursday's deadline, in which case Burnham could be sworn in as Prime Minister as soon as 17 July.

The next Euro wrap-up will be published on Thursday 9 July 2026

European calendar

Today's results							
Economic data							
Country	Release	Period	Actual	Market consensus/ <i>Daiwa forecast</i>	Previous	Revised	
Germany	 Industrial production M/M% (Y/Y%)	May	0.9 (0.0)	0.1 (-0.6)	0.4 (-0.5)	0.2 (-0.9)	
France	 Trade balance €bn	May	-6.9	-	-5.6	-5.4	
Auctions							
Country	Auction						
Germany	 sold €749mn of 1.3% 2027 green bonds at an average yield of 2.49%						
	 sold €568mn of 2.6% 2041 green bonds at an average yield of 3.31%						
UK	 sold £4bn of 4.125% 2033 bonds at an average yield of 4.519%						





Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

Wednesday's releases

Economic data

Country	BST	Release	Period	Market consensus/ <i>Daiwa forecast</i>	Previous
- Nothing scheduled -					



Auctions and events

Germany		10.30	Auction: to sell up to €6bn of 2036 bonds		
UK		00.01	REC, KPMG and S&P Global UK Report on Jobs for June		
		10.00	Auction: to sell £750mn of 0.125% 2028 bonds		
		10.00	Auction: to sell £750mn of 4.75% 2030 bonds		



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		07.00	May	14.8	14.5
UK		00.01	Jun	-30	-35

Auctions and events

Euro area		12.30	ECB to publish monetary policy account of 10-11 June Governing Council meeting		
UK		20.30	BoE Deputy Governor Breeden joins panel discussion on monetary policy implementation and market functioning, New York		

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

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