Euro wrap-up

Overview

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- Bunds made modest losses at the short end but gains further along the curve as final euro area inflation estimates for June confirmed a softening in the major core components.
- Gilts also largely made modest gains while Andy Burnham predictably cleared the final hurdle to becoming UK Prime Minister on Monday.
- In the coming week, the ECB will keep rates unchanged but maintain the prospect of tighter policy in September, and the flash July PMIs are due along with UK data for inflation and the labour market.

Daily bond market movements

Bond	Yield	Change
BKO 2.7 09/28	2.772	+0.018
OBL 2½ 04/31	2.851	+0.004
DBR 3 08/36	3.120	-0.011
UKT 4⅜ 03/28	4.340	+0.005
UKT 4⅛ 03/31	4.509	-0.006
UKT 4¾ 10/35	4.945	-0.017

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

Euro area

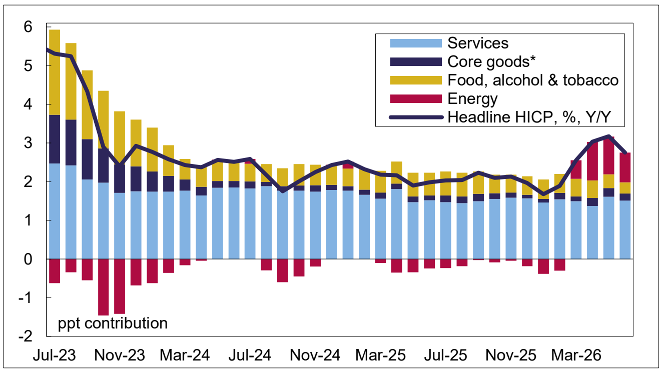
Downside surprise in June inflation data confirmed in final detail

The flash estimate of euro area inflation had initially surprised on the downside, with the headline and core rates down 0.4ppt and 0.2ppt to 2.8%Y/Y and 2.4%Y/Y respectively. Today's final estimates left those rates unchanged to one decimal place. But to two decimal places they were revised down (to 2.75%Y/Y and 2.36%Y/Y) to leave the core rate just 3bps above the average of the prior 12 months and underscoring the broadly favourable nature of the report. Indeed, each main component moderated slightly from May. Half of the drop in the headline inflation rate came from energy, which slowed 2.3ppts to a three-month low of 8.5%Y/Y, a touch below the flash estimate. Prices of petrol and other liquid fuels fell thanks to the improvement in wholesale crude markets. And they more than offset a modest pickup in electricity and gas due in part to the reversal of a tax cut in Spain. Meanwhile, despite recent increases in agricultural input costs, inflation of food, alcohol and tobacco moderated 0.4ppt to a five-year low of 1.5%Y/Y as past pressures continued to dissipate. More importantly, within the core components, non-energy industrial goods inflation eased more than previously thought to a three-month low of 0.7%Y/Y. As for food, there were few signs of indirect effects from the recent energy shock on core goods prices. But pressures in the tech sector were again reflected in certain items such as computers, laptops and tablets (3.8%Y/Y), mobile phones (3.3%Y/Y) and, particularly, external storage devices (42.7%Y/Y). Finally, and perhaps most importantly, services inflation eased 0.3ppt to 3.2%Y/Y. However, roughly half of that decline reflected a moderation in airfares while other volatile components such as accommodation and package holidays also eased. And so, as suggested by smaller declines in alternative indicators such as trimmed means, the drop in the core rate in June probably exaggerated the improvement in underlying inflation.

Despite reescalation in the Middle East, the ECB should hold rates at its July policy meeting

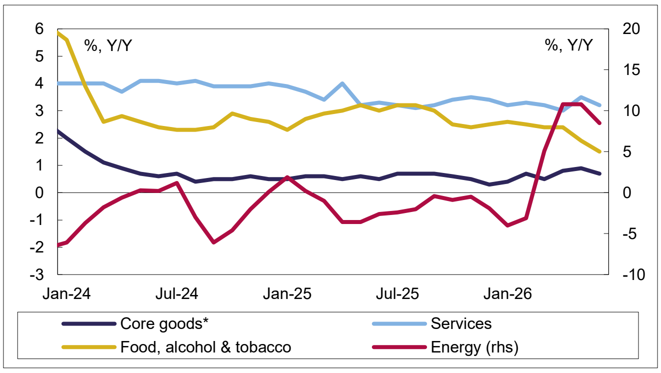
Nevertheless, the softness of June's inflation print, which undershot the ECB's projection as well as the initial market consensus, reinforces our expectation that rates will be left unchanged when the Governing Council meets on Thursday. Indeed, having tightened policy for the first time since 2023 in June, such an outcome looked all but guaranteed until just a few weeks ago. With the tentative peace between the US and Iran having facilitated a gradual resumption to transit via the Strait of Hormuz and downwards pressure on global energy prices, policymakers were cautiously optimistic in Sintra at the start of the month. ECB President Lagarde judged that the upside risks to inflation and downside risks to growth were 'probably more broadly balanced'. So, at the very least, subsequent reescalation of the conflict complicates the equation, even if its consequences thus far have been insufficient to derail expectations for a hold. Brent crude today sat above $85/bbl, roughly $14/bbl higher than two weeks ago but still some way below the levels which prevailed over the Spring. Oil

Euro area: Contributions to headline inflation



*Non-energy industrial goods.
Source: Macrobond and Daiwa Capital Markets Europe Ltd.

Euro area: Inflation of key components



*Non-energy industrial goods.
Source: Macrobond and Daiwa Capital Markets Europe Ltd.

futures prices also remain softer than those assumed in the ECB's June macroeconomic projections. And while some indirect effects were evident in today's price data, second-round effects remain absent, at least for now. On the other hand, the reversal of tax cuts in Germany and Spain have compounded the pickup in crude prices to push petrol prices to seven-week highs. And more importantly perhaps, gas prices have risen above the ECB's baseline assumptions and are currently priced by the markets to remain persistently high due to supply damage in the Middle East and expectations of higher demand to refill inventories before the winter. Influential ECB Board Member Isabel Schnabel (see table below) recently highlighted the latter specifically, alongside additional upside inflation risks such as those raised by the ongoing heatwave.

Lagarde comments likely to be consistent with expectations of further tightening in September

So, the re-intensification of the conflict probably warrants a more hawkish tone from Lagarde in her post-meeting press conference than she used in Sintra. Certainly, she will stress that the outlook remains highly uncertain, with risks to inflation skewed firmly to the upside. While the risks to activity are to the downside, the Governing Council will also take comfort from support from AI-related construction, defence spending and the resilient labour market. The meeting statement will continue to avoid forward guidance, maintaining that rates are not on a pre-set path with decisions remaining data dependent and to be taken on a meeting-by-meeting basis. But while future decisions will be influenced by developments in the Middle East, Lagarde's commentary seems likely to be consistent with market expectations that September will be live for the next rate hike. Indeed, while providing just cause to tighten policy in June, the ECB's latest macroeconomic projections – which foresaw core inflation remaining above 2.0%Y/Y through to Q428 on all scenarios – were conditioned on at least two such moves. Some Governing Council members have expressed that, if the ECB does indeed need to move to a more restrictive policy stance, then doing so sooner rather would be most appropriate. But all will likely be content to wait until September, when the ECB's updated projections will show the extent to which further restrictiveness is necessary, informed by greater clarity on the duration of hostilities and disruption at the Strait of Hormuz and perhaps also the risks of potential second-round effects as we approach Autumn's wage negotiation rounds.

Selected recent quotes from ECB policymakers*

ECB President Christine Lagarde *(29 June)*	"The [US-Iran] conflict has generated significant inflationary pressures…." "Cycles of escalation, negotiation, announced agreements and reversals have moved oil markets rapidly… the durability of [the interim peace] agreement is far from assured…" "We may…more often find ourselves in an intermediate zone, between shocks we can look through and those we must react to forcefully."
Isabel Schnabel *(6 July)*	"Does the decline in oil prices mean that we are back to the pre-war situation? I don't think so…The peace deal is still fragile, markets continue to point to higher oil prices over longer horizons and gas prices are still [higher than before the war]… energy and inventories will need to be refilled… [core inflation] momentum remains strong… [and] we are experiencing new shocks: the heatwave in Europe and Super El Niño may put upwards pressure on food prices."
Chief Economist Philip Lane *(30 June)*	"…for me, second-round effects [are] probably going to take some time. What I'm really focused on is the indirect effects… what we need to look at is how the four months of energy cost increases percolate into food inflation, and into services inflation… that channel is where there is perhaps still uncertainty…"
Joachim Nagel *(11 July)*	"…The geopolitical situation in the Middle East remains very complicated… the fall in energy prices [after the ceasefire] was surprising, at least to me… however, [energy prices today] have risen again because of renewed escalation. This is why we must be very cautious when predicting future monetary policy measures."
Yannis Stournaras *(10 July)*	"[Deescalation in the Middle East], if sustained, could have led to higher growth and lower inflation… hostilities started again, so we are back to square one."
Fabio Panetta *(7 July)*	"Upside risks to inflation continue to coexist with downside risks to growth. This requires constant monitoring of geopolitical developments, energy markets, supply chains, wages and inflation expectations. It also requires that monetary policy avoid committing to a predetermined path."
Pierre Wunsch *(6 July)*	"My hope, and let's see…is that the shock has disappeared… if the origin of the shock disappears before you have significant second-round effects… that doesn't ask for a tightening that would be significant… [but] if we have to [hike again], let's not wait too long."
Emmanuel Moulin *(3 July)*	"We are comfortable in our base scenario… we made sure in our communication that we were not entering into a new cycle of hikes… we will see where we are in July and September, but we have made no commitment..."
Martin Kocher *(1 July)*	"In the coming meetings, the decision will most likely be whether to stick with our current monetary policy or to raise rates further... [the price shock could] be enough to cause some persistence… [depending] on what the wage agreements look like this fall"
Ülo Kaasik *(1 July)*	"At the moment, it seems reasonable to me to have at least one more [hike]… one question is how geopolitics will play out…the other part is what impact the three-month oil price shock is having on other prices…"

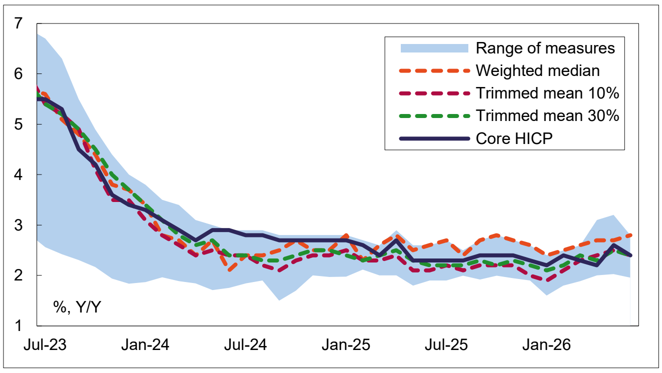
**Light blue shading shows ECB Executive Board members and gold shading for Governing Council members.*
Sources: ECB, National central banks, Reuters, Econostream, Bloomberg & Daiwa Capital Markets Europe Ltd.

The week ahead for euro area data

Besides the ECB's announcement, the coming week will also bring a handful of top-tier data releases. July's business surveys will provide the highlight, with the most prominent of those being the flash euro area PMIs (Friday). The PMIs weakened markedly at the start of the oil shock but offered tentative encouragement about a possible stabilisation last month as cost pressures receded. Nevertheless, at 50.0, the composite output PMI was consistent with stagnation. Support from the manufacturing sector is likely to soften over the coming months as the boost from precautionary stockpiling fades, and reescalation in the Gulf implies that the impact on activity of both uncertainty and inflation risks could be more acute this month. Certainly, whether the latest rise in energy prices has merely prolonged or amplified existing pressures will be of particular interest. But in either case, another signal of broadly stagnant output seems most likely. Indeed, any pronounced improvement in the euro area PMIs is likely to be conditional on signs of recovery in France, whose recent surveys have been distinctly disparaging about services activity. In that regard, the national INSEE survey (Thursday) will give a timelier, and arguably superior, update on conditions. The prospects of a lengthier energy price shock has also hurt the chances of a further recovery in consumer sentiment. We expect the Commission's confidence indicator (Thursday) to be little changed from June (-17.7), when it remained more than 5pts below its pre-war level. Additional detail will not be available with the preliminary release, but a German consumer survey (Friday) will provide some context including signals of consumers' willingness to spend.

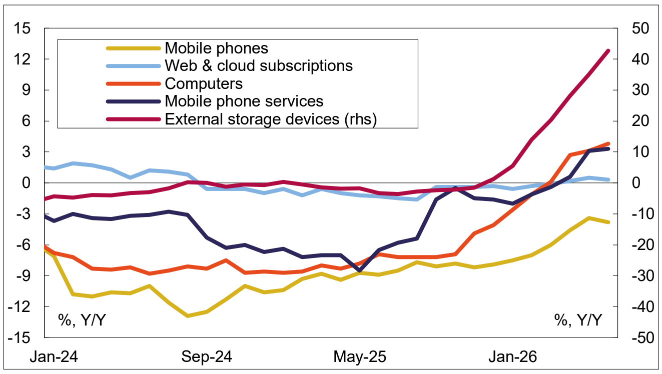
Meanwhile, German (Monday) and Spanish (Friday) producer price data will provide an update on pipeline price pressures last month. Headline PPI in the former rose to three-year high in May (2.2%Y/Y), but should have moderated in June if falling wholesale energy prices translated into some relief for refiners and energy-intensive manufacturers. Of course, policymakers won't take too much reassurance from that fact given the subsequent rebound in energy prices this month. And they will also be cautious not to overinterpret further signs of moderation in June's consumer inflation expectations indices (Friday), particularly at the one-year ahead horizon. Otherwise, the week ahead will bring a handful of other relevant ECB surveys. In particular, the quarterly Bank Lending Survey (BLS) should report that credit conditions tightened further in Q2, and will likely predict them to remain tight this quarter given market expectations of further interest rate hikes. And although bank lending has been resilient since the onset of the US-Iran war, heightened uncertainty will continue to weigh on banks' expectations for loan demand. The ECB's SAFE survey (Monday) will show whether that view is corroborated by businesses themselves. Finally, construction output data (also Monday) are expected to report a third consecutive month of growth in the euro area, reflecting broadly firmer activity across Germany (0.9%M/M), France (1.3%M/M) and the Netherlands (2.0%M/M).

Euro area: Select measures of underlying inflation



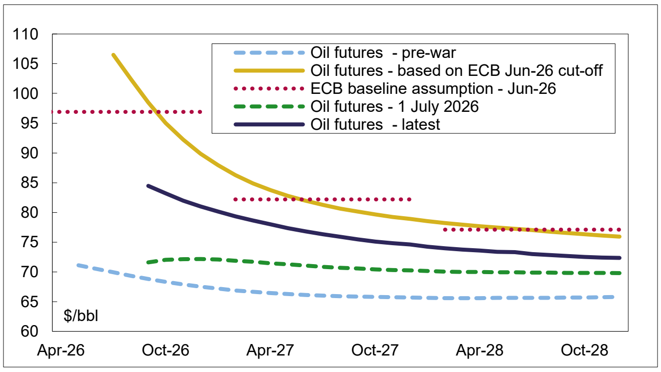
Source: Macrobond and Daiwa Capital Markets Europe Ltd.

Euro area: ICT equipment and services inflation



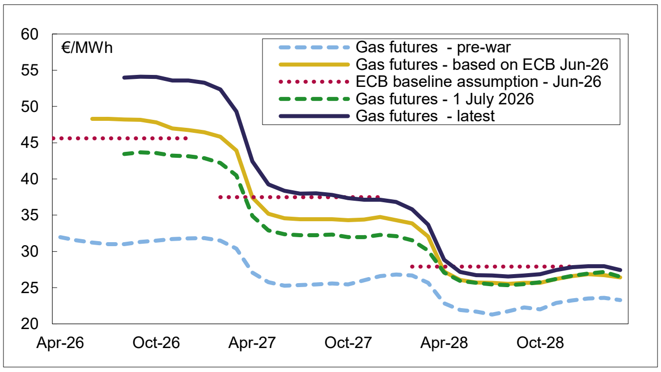
Source: Macrobond and Daiwa Capital Markets Europe Ltd.

Euro area: Brent crude futures & ECB assumption



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

Euro area: Natural gas futures & ECB assumption



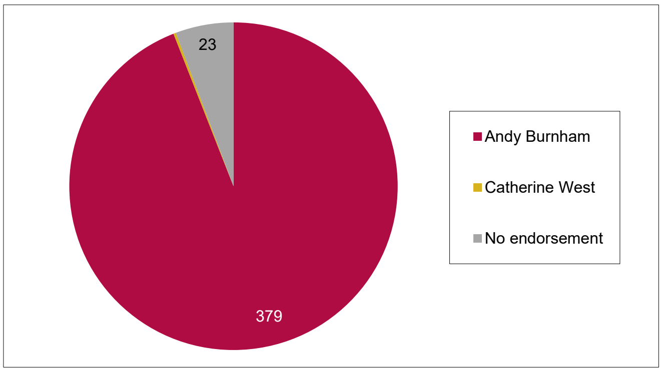
Source: Bloomberg, ECB and Daiwa Capital Markets Europe Ltd.

UK

Andy Burnham formally declared as Labour Party leader, and expected to enter No. 10 on Monday

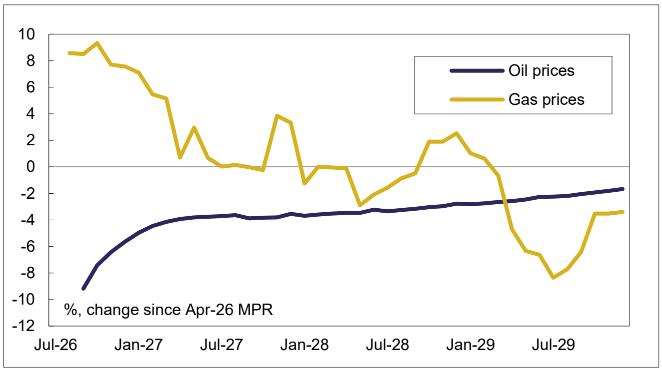
As has been inevitable since his comprehensive win in the Makerfield by-election just four weeks ago, Andy Burnham was finally declared as the new leader of the Labour Party today. While predictable, his victory was nonetheless comprehensive, receiving the blessing from all of the party's affiliated trade unions, and nominations from almost 95% (379) of its MPs with only one vote cast for an alternative candidate. And having cleared the final hurdle, the former Mayor of Greater Manchester will officially succeed Sir Kier Starmer as Prime Minister on Monday. Greater detail about his plans for Government are likely to be revealed shortly thereafter as Burnham tries to hit the ground running. His victory speech offered a few clues, albeit nothing new, reemphasising his vision for greater devolution of powers from Whitehall to the regions. Reports this morning also paid lip-service to his intention to bring struggling utilities under public ownership and approve new gas- and oil-drilling licenses in the North Sea. Burnham also took the opportunity to claim that he would be 'pro-business', echoing his earlier commitment to adhere to the Starmer government's fiscal rules. His cabinet picks will likely be confirmed early in the coming week. But Shabana Mahmood, the socially conservative Home Secretary, has emerged as the bookies' favourite for the Chancellor role. She has been a lawyer by trade, with seemingly little economic experience or strong views about fiscal policy or structural reform. So, we can draw few conclusions as to what her philosophy in the role would be or how she might choose to deliver the politically challenging public spending cuts and/or tax hikes likely to be required to deliver the current plan for deficit reduction. However, to the extent that she might be favoured over an alternative candidate from the soft left of the party such as Ed Miliband, markets appear to have responded favourably to the speculation.

UK: Labour MP's nominations for Party leader



Source: Labour Party and Daiwa Capital Markets Europe Ltd.

UK: Change in oil and gas futures curves



Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

The week ahead in the UK

Beyond politics, ahead of the BoE policy announcement on 30 July, the coming week will bring a host of top-tier economic data. The latest UK labour market (Tuesday) and June inflation data (Wednesday) will be in focus over the first half of the week, before retail sales figures and numerous key survey indicators – July's flash PMIs and GfK consumer confidence indices as well as the latest BoE DMP survey – arrive all at once on Friday. Starting with inflation, the headline CPI rate is widely expected to have moderated last month. In part, those predictions reflect falling auto fuel prices, which should provide some relief to energy inflation. Moreover, receding energy cost pressures also promise some relief to the PPI indices. But as in the euro area, we expect to see further signs of (likely temporary) softness in food inflation as well, while services inflation could benefit from weaker indirect effects. So, overall, we see the headline CPI rate easing to 2.6%Y/Y, a 14-month low and down 0.2ppt from its mark in May, while core inflation may edge back down to 2.5%Y/Y. Such a reading would confirm a non-negligible 0.3ppt undershooting of the BoE's latest projection. But policymakers won't take too much comfort in that. Inflation is due to rise back to around 3%Y/Y at the start of Q3 and natural gas futures curves – now 5-10% higher into early 2027 than the BoE assumed in April – point towards a further rise in household energy tariffs in Q4. Without a meaningful retreat from those levels, CPI inflation could rise closer to 3.5%Y/Y by year-end, which would undoubtably raise concerns about inflationary pressures becoming more embedded.

Of course, evidence of slack in the labour market has provided a vital source of reassurance to most MPC members about the strength of any potential second-round effects. And this week's update is likely to be little different. The risks to the unemployment rate (4.9%3M) seem skewed modestly to the upside. And while the BoE's preferred measure of private sector pay growth should be unchanged (2.9%3M/Y), that remains a 5½-year low and leaves pay growth on track to undershoot the BoE's forecast. That said, policymakers will be hesitant to attach much weight to any of the single-month data in the Labour Force Survey. Indeed, the ONS has acknowledged that the quality of this LFS round will be impaired by an operational issue, which it insists has been resolved and will impact subsequent releases to a lesser extent.

Nonetheless, that data production error perhaps shifts greater emphasis onto the BoE's DMP survey – particularly its forward-looking price- and wage-setting indicators – as well as the price PMIs. Until now, the former has offered some reassurance that wage expectations have not yet been affected by higher inflation expectations, while expected price increases have been mostly sector-specific. And while GDP rose in May, the PMIs flagged a sharp loss of momentum (49.3) at the end of Q2 despite softening price pressures. Owing to renewed cost pressures, we expect another stagnant reading, albeit whilst noting hospitality as a potential benefactor of England's ill-fated World Cup run and repeated heatwaves. Greater demand for football shirts, paddling pools and electric fans, and potentially a boost from cheaper fuel, also pose upside risks to June's retail sales figures. Some surveys, however, suggest that such a boost will be relatively muted, with persistently intense heat hurting footfall but benefitting online retailers. Otherwise, June's public sector net borrowing statistics (Tuesday) will provide an alternative potential flashpoint for discussion about Burnham's potential fiscal options, while the CBI's industrial trends survey (Thursday) will provide a timely update on manufacturing conditions ahead of the flash PMIs release. Finally, the official UK house price index (Wednesday) should revert closer to 2.5%Y/Y in May as weak buyer demand confronts base effects of last year's fading stamp duty distortions.

Daiwa economic forecast

	2026				2027		2026	2027	2028
	Q1	Q2	Q3	Q4	Q1	Q2			
GDP	%, Q/Q						%, Y/Y		
Euro area	-0.2	0.1	0.1	0.2	0.3	0.4	0.2	1.0	1.4
UK	0.6	0.4	0.1	0.1	0.3	0.3	1.1	1.0	1.4
Inflation, %, Y/Y									
Euro area									
Headline HICP	2.0	3.0	2.9	3.0	2.9	2.2	2.7	2.3	2.0
Core HICP	2.3	2.4	2.5	2.7	2.8	2.7	2.5	2.7	2.2
UK									
Headline CPI	3.1	2.7	3.2	3.4	3.3	2.8	3.1	2.7	1.9
Core CPI	3.2	2.5	2.7	2.9	3.0	3.1	2.8	2.9	2.4
Monetary policy, %									
ECB									
Deposit Rate	2.00	2.25	2.50	2.50	2.50	2.50	2.50	2.25	2.25
Refi Rate	2.15	2.40	2.65	2.65	2.65	2.65	2.65	2.40	2.40
BoE									
Bank Rate	3.75	3.75	3.75	3.75	3.75	3.75	3.75	3.25	3.25

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
Euro area	Final headline (core) HICP Y/Y%	Jun	**2.8 (2.4)**	*2.8 (2.4)*	3.2 (2.6)	-
	ECB current account €bn	May	**25.1**	-	15.7	17.5

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/ *Daiwa forecast*	Previous
			Monday 20 July 2026			
Euro area		10.00	Construction output M/M% (Y/Y%)	May	-	0.6 (0.9)
Germany		07.00	PPI Y/Y%	Jun	1.8	2.2
UK		00.01	Rightmove house prices M/M% (Y/Y%)	Jul	-	-0.6 (-0.5)
			Tuesday 21 July 2026			
Germany		10.00	ZEW current situation (expectations) balance	Jul	-77.3 (17.0)	-81.0 (10.5)
UK		07.00	Average wages (excluding bonuses) 3M/Y%	May	4.5 (3.4)	4.4 (3.4)
		07.00	Private sector wages ex. bonuses 3M/Y%	May	*2.9*	2.9
		07.00	Unemployment rate 3M%	May	4.9	4.9
		07.00	Employment 3M/3M change 000s	May	80	100
		07.00	Payrolled employment M/M change 000s	Jun	-6	2
		07.00	Claimant count rate % (change 000s)	Jun	-	4.5 (31.2)
		07.00	Public sector net borrowing £bn	Jun	18.0	23.3
			Wednesday 22 July 2026			
UK		07.00	Headline (core) CPI Y/Y%	Jun	*2.6 (2.5)*	2.8 (2.6)
		07.00	PPI – output (input) prices Y/Y%	Jun	3.5 (8.2)	4.0 (8.7)
		09.30	House price index Y/Y%	May	-	3.8
			Thursday 23 July 2026			
Euro area		05.00	New car registrations Y/Y%	Jun	-	3.3
		13.15	ECB Deposit (Refinancing) Rate %	Jul	*2.25 (2.50)*	2.25 (2.50)
		15.00	Preliminary Commission consumer confidence indicator	Jul	-16.9	-17.7
France		07.45	INSEE business (manufacturing) confidence indicator	Jul	95 (101)	94 (100)
		07.45	INSEE production outlook (own-company) indicator	Jul	-14 (4)	-15 (2)
UK		11.00	CBI industrial trends survey – total orders (selling prices) net balance %	Jul	-	-45 (22)
		11.00	CBI industrial trends survey – business optimism net balance %	Q3	-	-65
			Friday 24 July 2026			
Euro area		09.00	Preliminary services (manufacturing) PMI	Jul	49.9 (51.5)	49.4 (51.4)
		09.00	Preliminary composite PMI	Jul	50.3	50.0
		09.00	ECB consumer expectations survey – 1Y (3Y) -ahead CPI Y/Y%	Jun	3.5 (2.9)	3.5 (2.9)
Germany		07.00	GfK consumer confidence indicator	Aug	-28.5	-29.2
		08.30	Preliminary services (manufacturing) PMI	Jul	49.0 (50.5)	48.6 (50.3)
		08.30	Preliminary composite PMI	Jul	49.8	49.5
France		08.15	Preliminary services (manufacturing) PMI	Jul	47.5 (51.4)	46.8 (51.2)
		08.15	Preliminary composite PMI	Jul	47.9	47.2
Spain		08.00	PPI Y/Y%	Jun	-	10.5
UK		00.01	GfK consumer confidence indicator	Jul	-21	-23
		07.00	Retail sales – incl. auto fuel M/M% (Y/Y%)	Jun	-0.1 (2.5)	1.2 (3.2)
		07.00	Retail sales – excl. auto fuel M/M% (Y/Y%)	Jun	-0.4 (3.3)	1.2 (4.6)
		09.30	Preliminary services (manufacturing) PMI	Jul	49.4 (52.0)	48.8 (52.5)
		09.30	Preliminary composite PMI	Jul	49.7	49.3
		09.30	DMP – 3M output price (1Y CPI) expectations Y/Y%	Jul	4.0 (3.2)	4.1 (3.3)

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

The coming week's key events & auctions

Country	BST	Event / Auction
		Monday 20 July 2026
Euro area	09.00	ECB to publish quarterly Survey on the Access to Finance of Enterprises (SAFE) for Q226
UK	-	Andy Burnham expected to be sworn in as UK Prime Minister
		Tuesday 21 July 2026
Euro area	09.00	ECB to publish quarterly Bank Lending Survey (BLS) for Q226
Germany	10.30	Auction: to sell up to €6bn of 2031 bonds
UK	10.00	Auction: to sell £5bn of 4% 2029 bonds
		Wednesday 22 July 2026
Germany	10.30	Auction: to sell up to €1bn of 2.6% 2041 bonds
	10.30	Auction: to sell up to €1bn of 3.4% 2047 bonds
		Thursday 23 July 2026
Euro area	13.15	ECB monetary policy announcement
	13.45	ECB President Lagarde to hold post-Governing Council meeting press conference
UK	10.00	Auction: to sell bonds*
		Friday 24 July 2026
Euro area	09.00	ECB to publish quarterly Survey of Professional Forecasters (SPF)
	16.30	ECB Chief Economist Lane in conversation on 'Europe's Economic Future', Donegal
UK	09.30	BoE to publish Agents' summary of business conditions for July 2026

**Details to be announced. Source: Bloomberg and Daiwa Capital Markets Europe Ltd.*