Euro wrap-up

Overview

- Bunds made modest losses as German factory orders beat expectations and euro area retail sales displayed continued resilience.
- Gilts followed the global trend lower while the UK construction PMIs showed signs of recovery at the start of Q3.
- Friday will bring June data for German industrial production and trade.

Economics Research Team
+44 20 7597 8331

Daily bond market movements

Bond	Yield	Change
BKO 2.7 09/28	2.753	+0.028
OBL 2.9 10/31	2.871	+0.034
DBR 3 08/36	3.138	+0.029
UKT 4⅜ 03/28	4.293	+0.058
UKT 4⅛ 03/31	4.479	+0.053
UKT 4¾ 10/35	4.937	+0.048

*Change from close as at 5:00pm BST.
Source: Bloomberg

Euro area

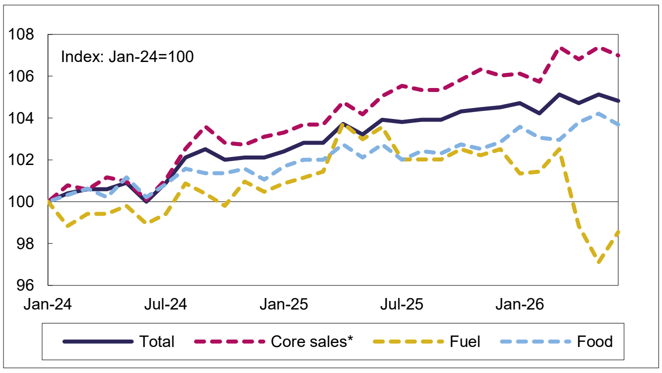
Retail sales display continued resilience, rising again in Q2 despite weakness in June

As expected, following Monday's disappointingly weak German data, euro area retail sales volumes ended Q2 on a subdued note, declining 0.3%M/M in June. As a result, they rose just 0.7%Y/Y, marking the softest year-on-year growth rate in almost two years. Nevertheless, with the level in May nudged higher, sales grew 0.2%Q/Q in Q2 to represent the 11th successive quarter of expansion, albeit the most sluggish since Q424. That reinforces our expectation that consumption rose again last quarter, albeit modestly, Unlike the previous two months, June's sales were buoyed by auto fuel, which rose 1.5%M/M ahead of the month-end expiry of certain temporary national fiscal support measures. In contrast, despite a second month of falling prices, food sales volumes fell for the first month in three (-0.5%M/M). And core sales (i.e. excluding food and auto fuel) dropped 0.4%M/M. But over Q2 as a whole, weakness was concentrated in auto fuel, sales of which plummeted 3.5%Q/Q, the most since Q420, as drivers balked at higher prices at the pump. In contrast, food sales rose 0.7%Q/Q, the most in seven quarters. And core sales rose 0.6%Q/Q, the firmest in three quarters and twice the pace in Q1. That pickup of core sales growth, despite the deterioration in consumer confidence in the wake of the Iran conflict, suggests that the expansion trend should continue in Q3, particularly as surveys point to a pickup in household willingness to make major purchases. Finally, among the member states, growth in Italy, Spain and the Netherlands offset much of the weakness in German and French sales in June. However, over Q2, perhaps surprisingly, sales fell in Spain (-0.3%Q/Q) for a second successive quarter while maintaining an uptrend in the other large member states.

German factory orders jump to 6-month high on strong demand for ICT equipment

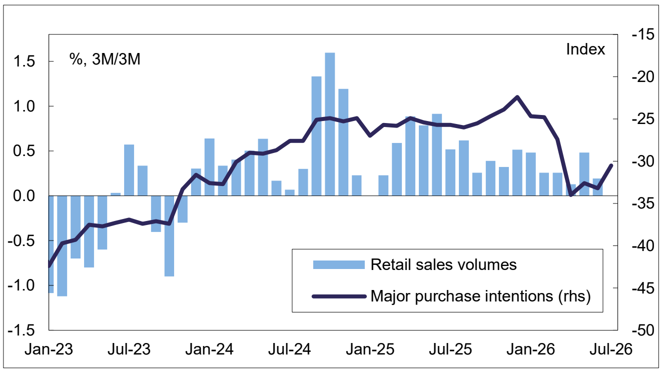
German GDP growth in Q2 appears to have been broad-based, with services, manufacturing and construction all firmer. And positive momentum appears to have been maintained into Q3. Today's data reinforced that view, with new factory orders up in June by a stronger-than-expected 3.1%M/M with both domestic and overseas demand stronger. Indeed, new orders from outside of the euro area rose to the highest level since October 2024. And despite a downwards revision in May, total new orders reached a six-month high, up a chunky 6.5%Y/Y and 1.4%3M/3M above the Q1 average. While Destatis noted that data on large-scale orders were incomplete in June, the monthly increase was nevertheless boosted by bulk domestic orders for machinery and ICT equipment. Orders of engines and turbines were up more than 80%M/M, and those of communication equipment rose more than fourfold to new series highs. Encouragingly, new auto orders rose for the first month in three (3.0%M/M). And while new orders of other transport equipment retreated in the wake of a major contract in May, they were around 12% above their Q1 average. Admittedly, the underlying picture was somewhat less robust. Excluding large-scale items, core orders fell for a third consecutive month in June (-0.5%M/M) and were broadly unchanged in Q2 from Q1. So, some demand momentum has likely softened over recent months in the face of heightened geopolitical uncertainty. And the

Euro area: Retail sales volumes



Source: Macrobond and Daiwa Capital Markets Europe Ltd.

Euro area: Retail sales & consumer confidence



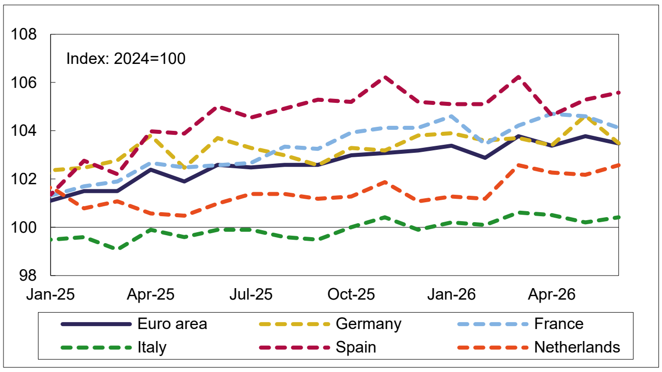
Source: EC, Macrobond and Daiwa Capital Markets Europe Ltd.

decline in manufacturing turnover in June suggests that tomorrow's IP data for the same month will miss the consensus forecast (0.2%M/M). But while supply constraints bind in certain subsectors, the steady rise in order backlogs over recent quarters suggests that production across a range of industries should be well maintained in the second half of the year.

Construction PMIs show signs of stabilising, but demand headwinds persist

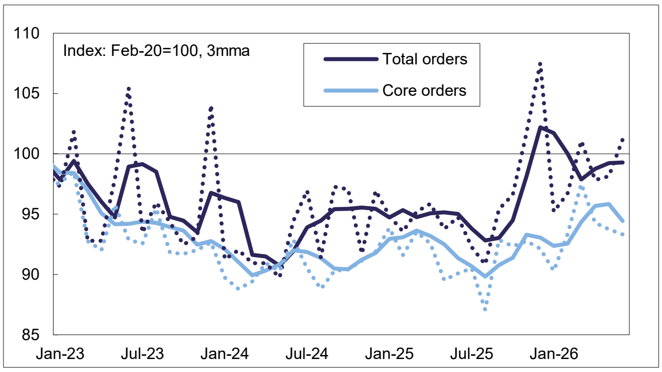
While improving consumer confidence should bolster German services activity and retail spending, surveys suggest that construction could be a key area of weakness over the near term. Firms in the sector are citing geopolitical uncertainty, elevated material costs and higher borrowing rates as constraints on new projects. Indeed, the German construction PMI was more downbeat in July, falling to the joint-lowest level since March 2025 (42.1), while new orders reportedly declined at one of the steepest rates of the past 16 months. However, the picture was not uniformly negative. While housing and commercial activity weakened, civil engineering provided a bright spot, with the respective index rising to its highest level in four months and back above its long-run average, suggesting that the government's infrastructure spending continues to gain traction. And in other member states, construction activity has shown more encouraging signs in July, with the French and Italian PMIs rising to the highest in five and three months respectively, with the latter also moving back above the long-run average. As a result, the aggregate euro area construction PMI increased 1.5pts to a four-month high of 44.3, with improvements across all major sectors. Nevertheless, the survey offered little evidence of sustained turnaround. Indeed, while supplier delivery times shortened and input cost pressures eased somewhat, firms became more pessimistic about the outlook for output over the year ahead, seemingly reflecting a more pronounced decline in new demand.

Euro area member states: Retail sales volumes



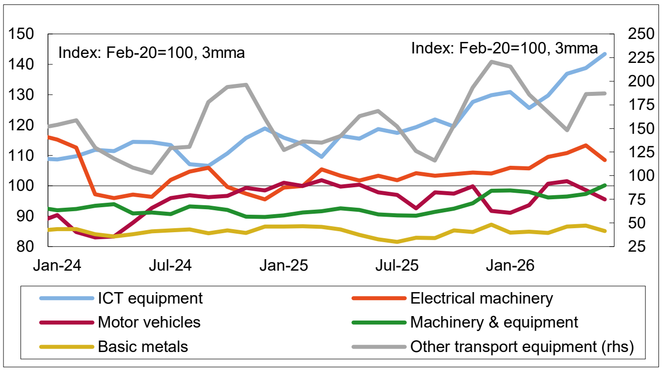
Source: Macrobond and Daiwa Capital Markets Europe Ltd.

Germany: New factory orders*



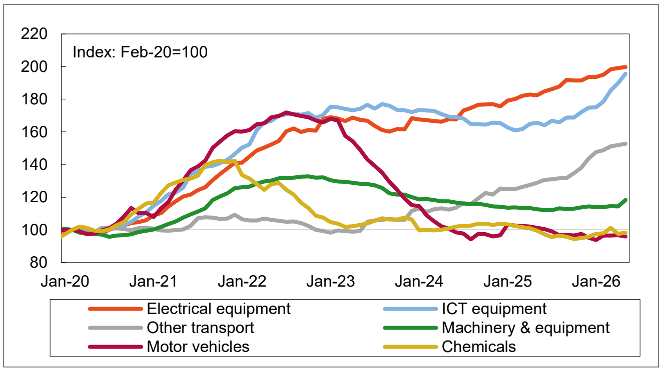
**Core orders exclude large-scale orders. Dotted lines represent single-month data. Source: Macrobond and Daiwa Capital Markets Europe Ltd.*

Germany: New factory orders by sector



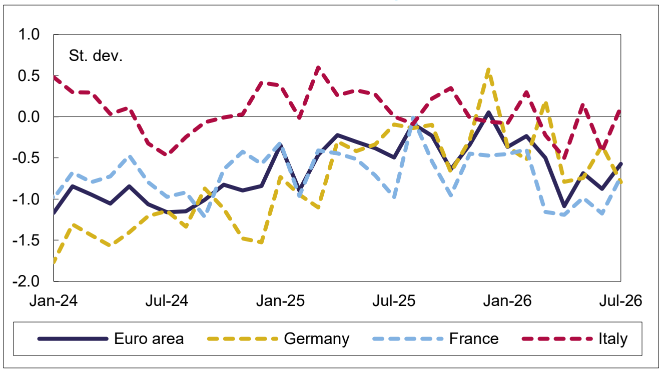
Source: Macrobond and Daiwa Capital Markets Europe Ltd.

Germany: Manufacturing order backlogs



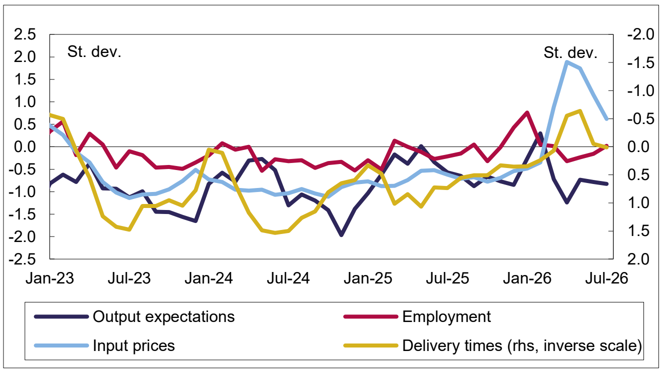
Source: Macrobond and Daiwa Capital Markets Europe Ltd.

Euro area: Construction activity PMIs



Source: S&P Global, Macrobond and Daiwa Capital Markets Europe Ltd.

Euro area: Selected construction PMIs

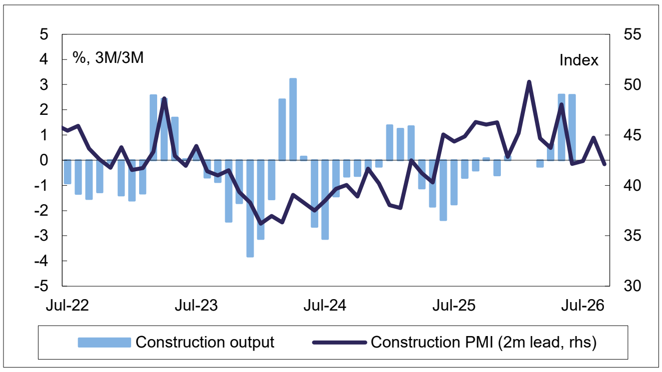


Source: S&P Global, Macrobond and Daiwa Capital Markets Europe Ltd.

The day ahead in the euro area

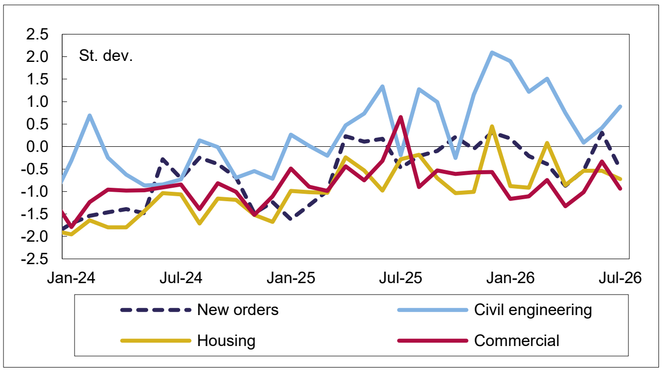
The principal focus of euro area data on Friday will be German industrial production figures for June. Broadly aligning with the pattern in France, today's Italian and Spanish IP releases confirmed that IP in Q2 more than fully reversed their falls in Q1, rising 0.4%3M/3M and 1.7%3M/3M respectively. But it also fell back on the month in both countries (-1.0%M/M and -0.7%M/M respectively) owing to broad-based weakness in manufacturing. And for a second consecutive month, energy production rose firmly to provide some offset (0.8%M/M and 2.5%M/M respectively), likely driven by higher electricity demand amidst the European heatwave. That suggests that the risks to tomorrow's German data are also be skewed to the downside. Despite firm manufacturing orders data (see above) and the solid signals from business surveys, weaker turnover (-1.3%M/M) and truck mileage (-1.7%M/M) also point towards a softer monthly reading. However, barring an unexpectedly sizable drop, German IP should still have risen last quarter, and by at least ¼%3M/3M. Meanwhile, goods trade data from Germany and France should also support expectations that firmer exports contributed positively to GDP in Q2.

Germany: Construction activity & PMI



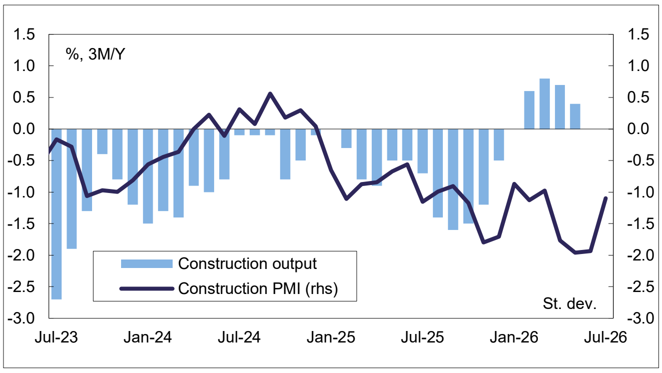
Source: S&P Global, Macrobond and Daiwa Capital Markets Europe Ltd.

Germany: Construction PMIs



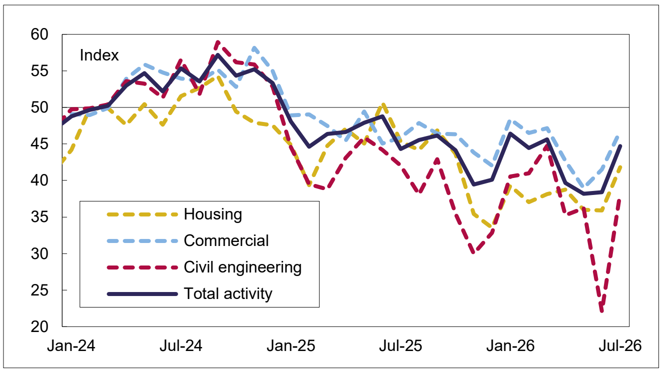
Source: S&P Global, Macrobond and Daiwa Capital Markets Europe Ltd.

UK: Construction output & PMI



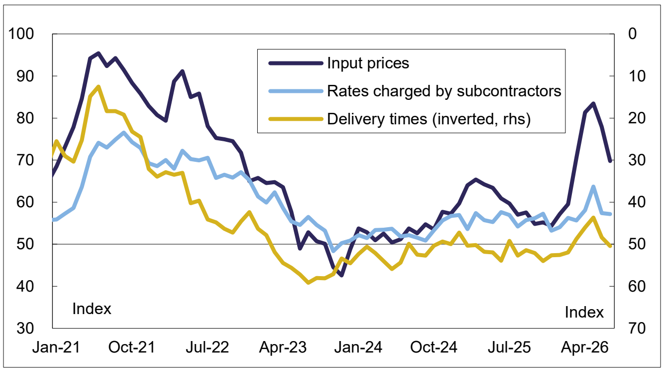
Source: S&P Global, Macrobond and Daiwa Capital Markets Europe Ltd.

UK: Construction subsector activity PMIs



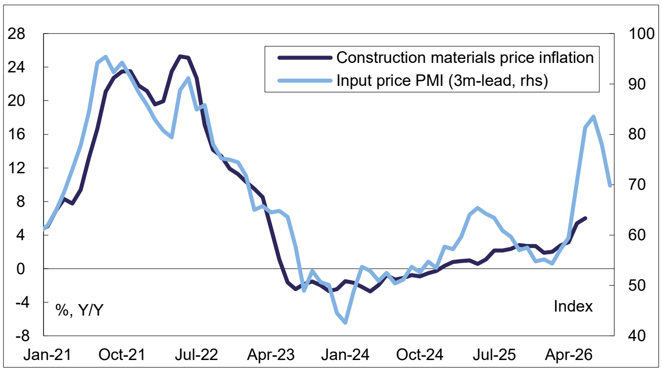
Source: S&P Global, Macrobond and Daiwa Capital Markets Europe Ltd.

UK: Selected construction PMI indicators



Source: S&P Global, Macrobond and Daiwa Capital Markets Europe Ltd.

UK: Materials inflation & input price PMI



Source: UK BEIS, S&P Global, Macrobond and Daiwa Capital Markets Europe Ltd.

UK

UK construction PMIs improved in July, but remain subdued

The UK construction PMIs have been a less-than-perfect guide to building activity in recent months. And next week's GDP data are likely to suggest that output in the sector expanded for the second consecutive quarter in Q2, contrasting the exceptional weakness of the respective PMIs. But as with the equivalent manufacturing and services sector surveys, the construction PMIs were tentatively more upbeat in July. Total activity remained stuck in contractionary territory, for a 17th consecutive month, its longest losing stretch since the GFC. But it showed notable improvement, rising 6pts above the Q2 average to 44.7, consistent with the slowest contraction in four months. The improvement was also broad-based. Most evident was the 16pt rebound in the civil engineering activity PMI (38.7) after its freakishly weak June reading. But the commercial (46.8) and house building activity (41.8) indices also rose more than 5pts each, and the latter to a ten-month high. With anecdotal evidence citing an uptick in tendering opportunities, the new orders index (47.6) saw a similar rally, which also likely supported firms' material purchases (45.3). And adjacent to that, input price pressures reportedly eased too, with material costs rising at their slowest pace in four months (69.8), while supply chains (50.5) were encouragingly stable. As a result, construction firms were the most upbeat about the outlook since February (60.1). Conditions at the start of Q3 remain unsuited to a pickup in momentum, however. An input cost index more than 10pts above pre-war levels and tighter financial conditions continue to weigh on housing activity. And given our expectation for less favourable carryover into Q3, the sector is bound to struggle to replicate its support to GDP in Q3.

The day ahead in the UK

With no economic data scheduled for Friday, it should be a quiet end to the week for the UK.

European calendar

Today's results

Economic data

Country	Release	Period	Actual	Market consensus/ *Daiwa forecast*	Previous	Revised
Euro area	Retail sales M/M% (Y/Y%)	Jun	**-0.3 (0.7)**	0.1 (1.0)	0.2 (1.6)	0.4 (1.9)
	Construction PMI	Jul	**44.3**	-	42.8	-
Germany	Factory orders M/M% (Y/Y%)	Jun	**3.1 (6.5)**	0.5 (5.9)	1.9 (6.2)	0.3 (4.5)
	Construction PMI	Jul	**42.1**	-	44.8	-
France	Construction PMI	Jul	**41.5**	-	38.2	-
	Preliminary wages Q/Q%	Q2	**0.7**	-	0.7	-
Italy	Industrial production M/M% (Y/Y%)	Jun	**-1.0 (-0.6)**	0.3 (1.1)	-0.3 (1.1)	- (1.2)
	Construction PMI	Jul	**49.1**	-	45.4	-
Spain	Industrial production M/M% (Y/Y%)	Jun	**-0.7 (1.1)**	-	1.2 (3.4)	1.0 (3.1)
UK	Construction PMI	Jul	**44.7**	40.0	38.4	-

Auctions

Country	Auction
France	sold €1.996bn of 1.25% 2036 bonds at an average yield of 3.86%
	sold €6.34bn of 3.7% 2036 bonds at an average yield of 3.900%
	sold €2.119bn of 3.8% 2037 bonds at an average yield of 3.95%
	sold €2.04bn of 0.5% 2044 bonds at an average yield of 4.37%
Spain	sold €1.85bn of 2.6% 2031 bonds at an average yield of 3.005%
	sold €1.565bn of 3% 2033 bonds at an average yield of 3.188%
	sold €1.9bn of 3.4% 2036 bonds at an average yield of 3.542%
	sold €728mn of 2.05% 2039 inflation-linked bonds at an average yield of 1.715%

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

Tomorrow's releases

Economic data

Country	BST	Release	Period	Market consensus/ *Daiwa forecast*	Previous
Germany	07.00	Industrial production M/M% (Y/Y%)	Jun	0.2 (0.1)	0.9 (0.0)
	07.00	Trade balance €bn	Jun	17.2	19.1
France	06.30	Unemployment rate (mainland unemployment rate) %	Q2	8.2 (8.0)	8.1 (7.9)
	07.45	Trade balance €bn	Jun	-	-6.9

Auctions and events

- Nothing scheduled -

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

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