

Euro wrap-up

Overview

- Bunds made losses as final euro area inflation data for April flagged persistence in certain services components and ECB Board member Schnabel stated that she didn't see the case for a rate cut in July.
- Gilts followed the global trend lower on a quiet day for UK economic news.
- The coming week will bring the May flash PMIs as well as new data on negotiated wages in the euro area and inflation and retail sales in the UK.

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Daily bond market movements

Bond	Yield	Change
BKO 2.9 06/26	2.982	+0.063
OBL 2.1 04/29	2.558	+0.061
DBR 2.2 02/34	2.513	+0.054
UKT 0½ 01/26	4.290	+0.034
UKT 0½ 01/29	4.006	+0.046
UKT 4% 01/34	4.126	+0.049

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

Euro area

Final April inflation data confirm further moderation in core goods component

As suggested by the data from the larger member states, today's final euro area consumer price data for April confirmed the broadly encouraging findings of the flash release. So, the headline rate of inflation was unchanged from March at 2.4%Y/Y, matching the lowest since July 2021. And that rate would have declined had it not been for increases in the non-core components. Indeed, the pace of decline in energy prices moderated for a fifth month, with the respective component up 1.2ppts to a twelve-month high of -0.6%Y/Y on higher petrol prices and the withdrawal of government support for household bills in countries such as Germany and Spain. Moreover, having reached a 2½-year low in March, inflation of food, alcohol and tobacco rose 0.2ppt to 2.8%Y/Y. However, perhaps reassuringly, the core components continued to decline. Consistent with the absence of pressures in the global factory sector, prices of core goods rose the least in any April in a decade (0.45%M/M) to push the respective annual rate down 0.2ppt to 0.9%Y/Y, the lowest since July 2021. Among other goods items, due to particular weakness in the second-hand category, inflation of motor cars fell to a 3-year low of just 1.6%Y/Y. The furniture component fell to just 0.4%Y/Y, the softest since late 2020. And prices of household appliances were down 1.7%Y/Y, the sharpest annual pace of decline in almost a decade.

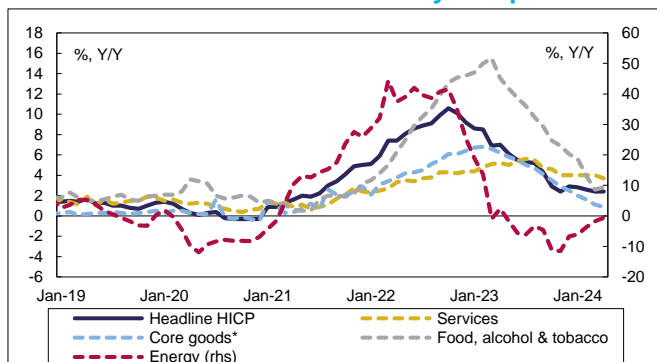
Services inflation down as Easter effect reverses but some pressures persist

Most importantly, services inflation – which remains a key focus of the ECB's Governing Council – dropped 0.3ppt to the lowest since August 2022. But, at 3.7%Y/Y, it remained relatively elevated. Based on the ECB's own seasonally adjusted measure, services prices rose 0.3%M/M, the least in four months but still above rates that would be consistent with the inflation target. And given the strength over recent months, momentum in services appears to have picked up since the end of last year, a development that the hawks might well put down to the pass-through from high wage growth. Indeed, the softening of services inflation in April in part reflected the early timing of Easter, which had contributed to stickiness in the category in the prior month and provided a favourable base effect. So, for example, inflation of air fares fell more than 10ppts into negative territory, while the package holidays component dropped more than 1.0ppt to 5.8%Y/Y and hospitality fell below 5.0%Y/Y for the first time in more than two years. And there remained pressures in certain other services components, not least with insurance inflation up a further 1.8ppts to a new series high of 9.1%Y/Y.

Underlying inflation measures continue to moderate

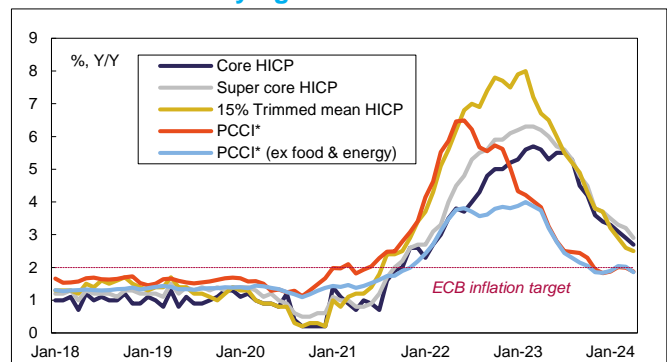
Despite the signs of persistence in certain services components, overall core inflation fell for a ninth successive month to the lowest level since February 2022. Other measures of underlying inflation consistent with a further downtrend in price

Euro area: Headline inflation & key components



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

Euro area: Underlying measures of inflation



*Persistent and Common Component of inflation. Source: Macrobond, ECB and Daiwa Capital Markets Europe Ltd.

pressures included the 15% trimmed mean HICP, which edged down to 2.5%Y/Y, the lowest since October 2021. And the core persistent and common component of inflation (PCCI) – which the Governing Council believes can provide one of the more reliable guides to future inflation – eased back below 2.0%3M/Y, consistent with the inflation target. Moreover, today's detail also showed that the share of the HICP basket with inflation at 2% or higher fell below 54%, more than 35ppts below the peak at the start of 2023 and the lowest since November 2021.

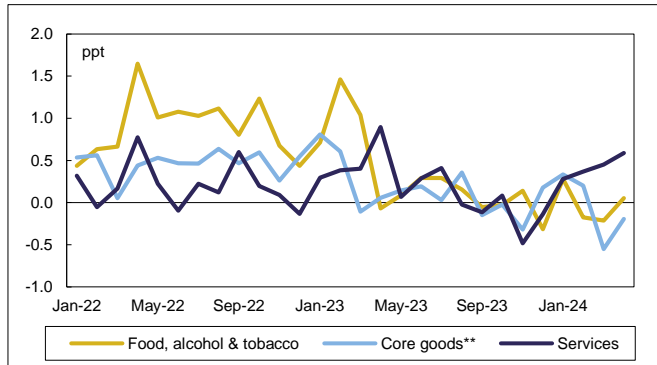
Headline inflation to tick up in May before resuming downtrend from June

Looking ahead, significant base effects will continue to impact the profile of inflation. For example, next month we expect the airfares component to rebound from the Easter-related weakness in April. And transport services inflation will also be boosted by the 'Deutschland ticket', which was introduced in May last year. Base effects related to auto fuels will also contribute to higher energy inflation. So, we expect headline HICP inflation to rise in May, perhaps by 0.2ppt to 2.6%Y/Y. However, the core rate might well edge down slightly further to 2.6%Y/Y. Thereafter, government measures will continue to add to energy inflation in certain counties such as Spain. However, subdued wholesale gas prices should take some of the pressure off that component, while food inflation should resume a gradual downtrend. And with survey indicators such as the PMIs suggesting that firms are less inclined to try to pass on increased costs – including those related to wages – onto customers, we expect both headline and core inflation to gradually lower from June through to October. According to our forecast, however, with services inflation likely to remain above 3.0%Y/Y into early 2025, it might not be until next spring that the headline and core rates fall below to 2.0%Y/Y or below.

Negotiated pay growth remains elevated but reflects one-off payments

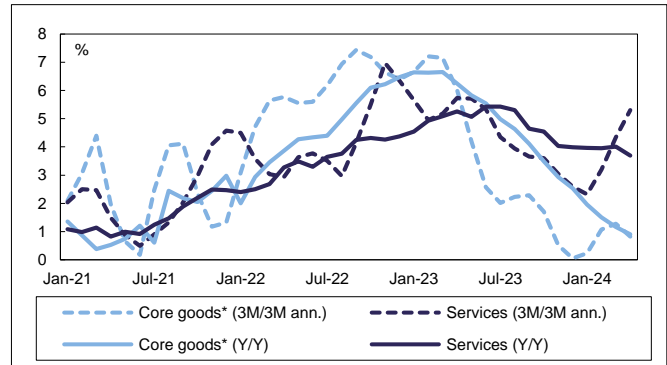
While the May inflation data should be sufficiently tame and consistent with the ECB's projections to give the green light to the first rate cut next month, Governing Council members continue to emphasise that policy decisions thereafter remain uncertain. Certainly, not least given the continued upside skew to risks to the inflation outlook related to historically high pay growth, the more hawkish Governing Council members, such as the highly influential Executive Board member Isabel Schnabel, do not see the case for rate cuts at successive policy meetings from June on. And we maintain an expectation of one rate cut per quarter. But while the closely-watched ECB measure of euro area negotiated wage growth – due to be published on 23 May – is likely to suggest that pay pressures remained elevated at the start of the year, this will principally reflect one-off payments to compensate for above-target inflation over recent years, rather than a pickup in underlying pay pressures which appear to be moderating. For example, in Germany, total negotiated pay growth jumped 5.9%Y/Y in

Euro area: Deviations from long-run price change*



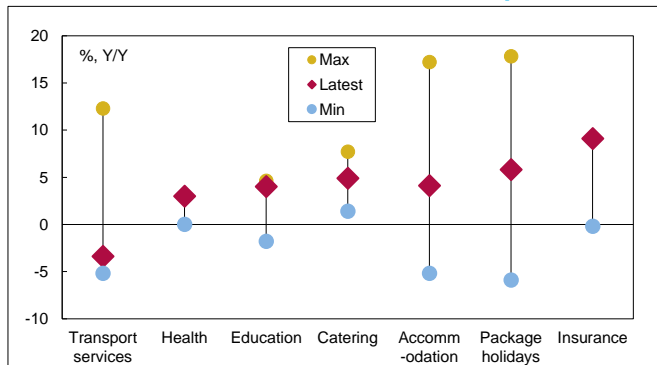
*Monthly change in prices compared to average for the month in the decade before the pandemic. **Non-energy industrial goods. Source: Macrobond and Daiwa Capital Markets Europe Ltd.

Euro area: Core inflation momentum



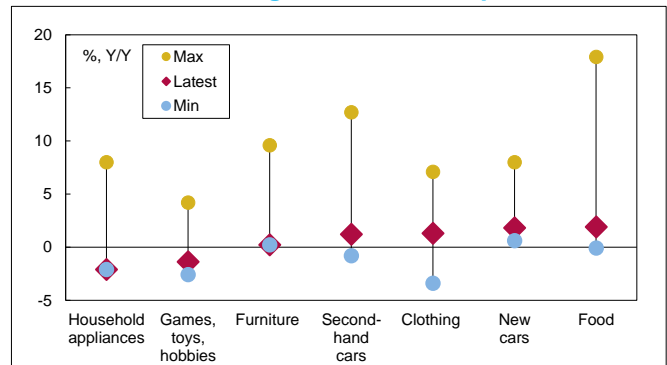
*Non-energy industrial goods. Source: Macrobond and Daiwa Capital Markets Europe Ltd.

Euro area: Selected services HICP components*



*Since 2020. Source: Macrobond and Daiwa Capital Markets Europe Ltd.

Euro area: Selected goods HICP components*



*Since 2020. Source: Macrobond and Daiwa Capital Markets Europe Ltd.

February, the most in eight months, to leave it up 5%Y/Y so far in Q1 compared with 3.6%Y/Y in Q4. But when excluding one-off payments, growth was more stable at 2.6%Y/Y, bang in line with the pre-pandemic five-year average. Elsewhere, negotiated wage growth moderated further in France in Q1, by 0.8ppt to 3.5%Y/Y, the lowest for two years, with equivalent growth in Italy down 1.5ppts to a three-quarter low of 2.8%Y/Y following one-off payments to the public-sector in Q4. And perhaps surprisingly, negotiated wage growth (in France and Italy at least) appears more dynamic in industry than services. Meanwhile, according to the flash figures, overall hourly wage growth in France slowed to just 2.8%Y/Y in Q1 down from 3.1%Y/Y in Q4 and almost 5%Y/Y in H123.

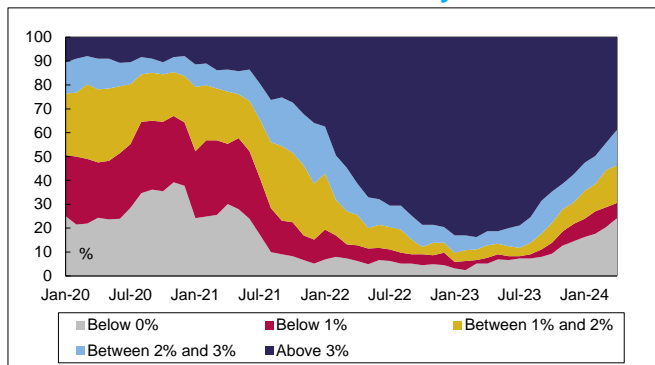
Indeed wage tracker eases to a more than 2-year low in April

Moreover, more timely measures of pay growth suggest that the peak has passed. For example, the Indeed wage tracker suggested that the downtrend was maintained at the start of Q2, with the French measure down to 2.3%Y/Y, the lowest since December 2021, while German growth slowed to a 2½-year low of 3.4%Y/Y. Overall, the euro area Indeed wage tracker eased to just 3.0%Y/Y in April, the softest rate for more than two years and well below the peak of 5.4%Y/Y in September 2022. While the unemployment rate remains at a series low as firms hoard labour in anticipation of a pickup in economic activity, the steady decline in job vacancies is consistent with survey indications that firms are less inclined to hire new workers. As such, the labour market appears to be loosening gradually, which should further reduce upwards pressure on pay and limit risks of inflation persistence over coming quarters.

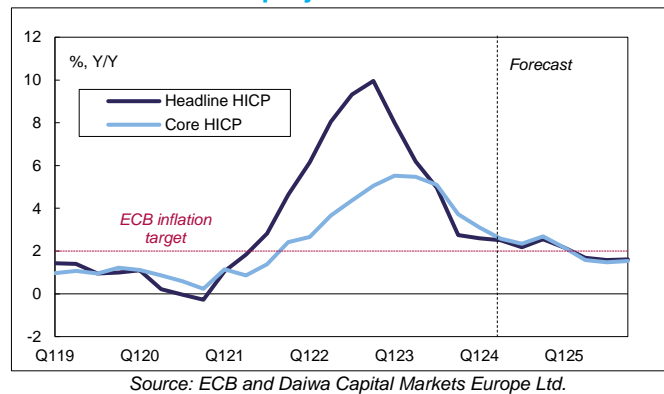
The coming week in the euro area

The most notable euro area economic releases in the coming week will be the flash May PMIs and aforementioned Q1 negotiated wage figures on Wednesday. The euro area composite output PMI surprised to the upside in April rising to an eleven-month high of 51.7, some 2.5pts above the Q1 average and therefore suggestive of a further pickup in recovery momentum at the start of Q2. The improvement was led by services (53.3), but the PMIs also implied the softest contraction in the manufacturing sector (47.3) in a year. While the European Commission's sentiment indices were less upbeat at the start of Q2, expectations are for the composite PMI to have moved broadly sideways in May, therefore signalling that the euro area economy is on track for another quarter of steady GDP growth. The survey's price indices will also be watched. In April, the composite input and output price PMIs ticked slightly higher to 58.2 and 53.7, but remained comfortably below the respective averages in 2023 and well down on the highs recorded in 2022 with the sizeable gap between the two indices suggesting limited scope for firms pass costs onto customers. ECB policymakers will also watch its negotiated wage growth

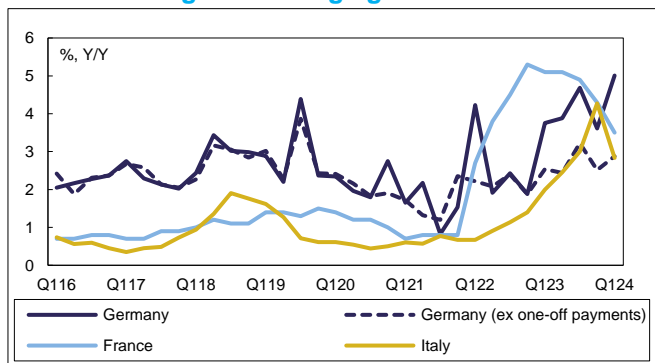
Euro area: Share of HICP basket by inflation rate



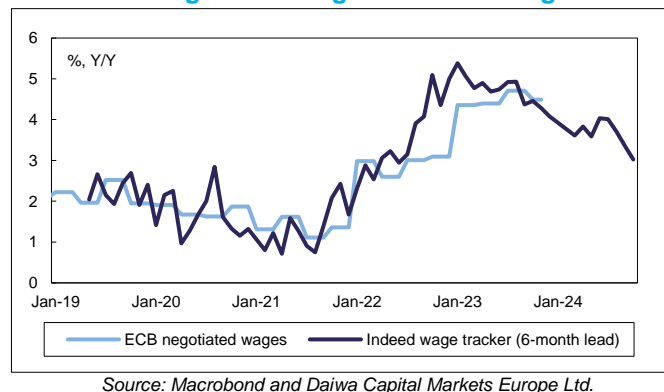
Euro area: Inflation projections



Euro area: Negotiated wage growth



Euro area: Negotiated wages & Indeed wage tracker



indicator for Q1, which might well report only a small moderation from growth of 4.5%Y/Y in Q4. Meanwhile, Wednesday will also bring the Commission's preliminary consumer confidence index for May, which is forecast to rise for a fourth consecutive month (-14.0) to its highest since February 2022 as households benefit from rising real disposable incomes.

Ahead of those data, euro area goods trade and construction output figures for March are due on Tuesday, with the latter expected to have risen for a fourth consecutive month in line with the increase in Germany (+1.0%M/M) and France (+1.1%M/M). Finally, updated German GDP figures for Q1 – to be published on Friday – will likely confirm the findings of the previous release that suggested a return to positive growth at the start of the year (0.2%Q/Q). The expenditure breakdown will likely suggest that growth was supported by construction investment and exports, but that household consumption declined.










UK

The coming week in the UK

In a busy week for UK economic releases, the key focus will be April's inflation report on Wednesday. Given the 12% cut in Ofgem's energy price cap from the start of April, we expect headline CPI to take a notable step down by 1.1ppt to 2.1%Y/Y, which would be bang in line with the BoE's latest projection and mark the lowest rate since July 2021. Due to base effects, food inflation is also expected to slow significantly further to around 4.3%Y/Y to be almost 12ppts below the peak a year ago. But more encouraging for the MPC will be the moderation in core inflation – our expectation is for a drop of 0.7ppt to a 30-month low of 3.5%Y/Y – principally reflecting base effects around the early timing of Easter this year. In particular, we expect services inflation to drop a little more than ½ppt to a near-two-year low of 5.3%Y/Y, while non-energy industrial goods inflation is forecast to decline to a near-four-year low of 0.5%Y/Y.

Meanwhile, the flash PMIs for May, due Thursday, will be watched closely for signs of pass through to consumers from the recent pickup in costs related not least to the hike in the National Living Wage. However, while the composite input price PMI rose 3.5pts in a nine-month high in April, the output price PMI edged down to a seven-month low. In terms of the activity PMIs, the composite output index might well ease back from April's 12-month high (54.1), albeit remaining consistent with ongoing solid recovery momentum in the middle of the second quarter as demand for consumer-facing services was likely boosted by the improved weather conditions. Tallying with recent retail surveys, however, the sales figures for April, due Friday, are expected to start the second quarter on the backfoot as demand on the High Street was dampened by heavy rainfall that month. The latest GfK consumer survey for May will also be published on Friday. And Ofgem's announcement of its July energy tariff cap, also due that will give further insight into the inflation outlook.

Daiwa economic forecasts






















	2024				2025		2023	2024	2025
	Q1	Q2	Q3	Q4	Q1	Q2			
GDP	%, Q/Q						%, Y/Y		
Euro area 	0.3	0.2	0.2	0.3	0.3	0.4	0.5	0.6	1.3
UK 	0.6	0.4	0.3	0.2	0.2	0.3	0.1	0.7	1.0
Inflation, %, Y/Y									
Euro area									
Headline HICP 	2.6	2.4	2.2	2.8	2.5	2.1	5.4	2.5	1.8
Core HICP 	3.1	2.3	2.1	2.5	2.1	1.8	4.9	2.3	1.7
UK									
Headline CPI 	3.5	1.9	2.0	2.3	2.0	1.8	7.3	2.4	1.9
Core CPI 	4.6	3.1	2.8	2.8	2.3	1.7	6.2	3.3	1.8
Monetary policy, %									
ECB									
Deposit Rate 	4.00	3.75	3.50	3.25	3.00	2.75	4.00	3.25	2.25
Refi Rate 	4.50	4.25	3.65	3.40	3.15	2.90	4.50	3.40	2.40
BoE									
Bank Rate 	5.25	5.00	4.75	4.50	4.25	4.00	5.25	4.50	3.50

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

The next edition of the Euro wrap-up will be published on 21 May 2024

The coming week's data calendar

The coming few week's key data releases

Country	BST	Release	Period	Market consensus/ <i>Daiwa</i> <i>forecast/actual</i>	Previous
Monday 20 May 2024					
UK		00.01 Rightmove house price index M/M% (Y/Y%)	May	-	1.1 (1.7)
Tuesday 21 May 2024					
Euro area		10.00 Construction output M/M% (Y/Y%)	Mar	-	1.8 (-0.4)
		10.00 Trade balance €bn	Mar	20.0	17.9
Germany		07.00 PPI Y/Y%	Apr	-3.2	-2.9
UK		11.00 CBI industrial trends survey – total orders (selling price) balance %	May	-20 (25)	-23 (27)
Wednesday 22 May 2024					
Euro area		07.00 New car registrations Y/Y%	Apr	-	-4.9
UK		07.00 Headline (core) CPI Y/Y%	Apr	<u>2.1 (3.5)</u>	3.2 (4.2)
		07.00 Output (input) PPI Y/Y%	Apr	1.1 (-1.5)	0.6 (-2.5)
		07.00 Public sector net borrowing £bn	Apr	18.5	11.0
		07.00 House price index Y/Y%	Mar	-	-0.2
Thursday 23 May 2024					
Euro area		09.00 Preliminary manufacturing (services) PMI	May	46.1 (53.6)	45.7 (53.3)
		09.00 Preliminary composite PMI	May	52.0	51.7
		09.00 Negotiated wages Y/Y%	Q1	-	4.5
		15.00 Preliminary Commission consumer confidence indicator	May	-14.3	-14.7
Germany		08.30 Preliminary manufacturing (services) PMI	May	43.3 (53.5)	42.5 (53.2)
		08.30 Preliminary composite PMI	May	51.0	50.6
France		08.15 Preliminary manufacturing (services) PMI	May	45.8 (51.7)	45.3 (51.3)
		08.15 Preliminary composite PMI	May	51.1	50.5
UK		09.30 Preliminary manufacturing (services) PMI	May	49.5 (54.7)	49.1 (55.0)
		09.30 Preliminary composite PMI	May	54.0	54.1
Friday 24 May 2024					
Germany		07.00 GDP – second estimate Q/Q% (Y/Y%)	Q1	0.2 (-0.2)	-0.5 (-0.2)
France		07.45 INSEE business (manufacturing) sentiment indicator	May	100 (100)	99 (100)
UK		00.01 GfK consumer confidence indicator	May	-18	-19
		07.00 Retail sales, including auto fuel sales M/M% (Y/Y%)	Apr	-0.6 (-0.3)	0.0 (0.8)
		07.00 Retail sales, excluding auto fuel sales M/M% (Y/Y%)	Apr	-0.8 (-1.2)	-0.3 (0.4)

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

The coming week's key events & auctions

Country	BST	Event / Auction
Monday 20 May 2024		
UK	18.00	BoE Deputy Governor Broadbent scheduled to speak at BoE workshop on the transmission of monetary policy
Tuesday 21 May 2024		
Germany	10.30	Auction: €4.0bn of 2.1% 2029 bonds
UK	18.00	BoE Governor Bailey scheduled to give lecture at the LSE
	10.00	Auction: £2.25bn of 4.75% 2043 bonds
Wednesday 22 May 2024		
Germany	10.30	Auction: €4.0bn of 2.2% 2034 bonds
UK	10.00	Auction: £4.0bn of 4.125% 2029 bonds
Thursday 23 May 2024		
- Nothing scheduled -		
Friday 24 May 2024		
Euro area	08.00	ECB's Schnabel scheduled to give keynote speech on "the state contingency of monetary policy transmission"
UK	-	Ofgem to announce energy price cap for July-September 2024

Source: Bloomberg 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 headline (core) HICP Y/Y%	Apr	2.4 (2.7)	<u>2.4 (2.7)</u>	2.4 (2.9)	-
Auctions						
Country	Auction					
- Nothing to report -						

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
Italy	Final HICP (CPI) Y/Y%	Apr	0.9 (0.8)	<u>1.0 (0.9)</u>	1.2 (1.2)	-
	Trade balance €bn	Mar	4.3	-	6.0	-
Auctions						
Country	Auction					
France	sold €4.21bn of 2.5% 2027 bonds at an average yield of 2.84%					
	sold €2.76bn of 2.75% 2029 bonds at an average yield of 2.76%					
	sold €3.19bn of 2.75% 2030 bonds at an average yield of 2.77%					
	sold €1.84bn of 2.5% 2030 bonds at an average yield of 2.73%					
	sold €520mn of 0.1% 2028 index-linked bonds at an average yield of 0.86%					
	sold €798mn of 0.1% 2029 index-linked bonds at an average yield of 0.57%					
	sold €493mn of 0.1% 2032 index-linked bonds at an average yield of 0.64%					
	sold €185mn of 0.1% 2053 index-linked bonds at an average yield of 0.74%					

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

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