

Euro wrap-up

Overview

- Bunds were little changed today as the flash estimate of euro area CPI edged slightly higher in line with expectations, while the latest German unemployment rate fell to a post-reunification low.
- Gilts were also little changed on a quiet day for UK economic data.
- Tomorrow brings final manufacturing PMIs from the euro area, various member states and the UK.

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Daily bond market movements

Bond	Yield	Change*
BKO 0 06/18	-0.514	+0.004
OBL 0 04/21	-0.369	-0.003
DBR 0½ 02/26	0.147	-0.019
UKT 1¼ 07/18	0.435	-0.022
UKT 1½ 01/21	0.907	-0.009
UKT 2 09/25	1.438	+0.003

*Change from close as at 4.30pm BST.

Source: Bloomberg

Euro area

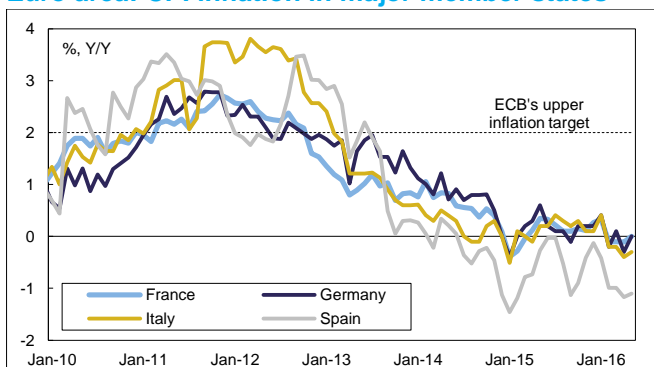
Euro area inflation edges higher in May

Ahead of the conclusion of the ECB's latest Governing Council meeting on Thursday, which will coincide with the publication of updated economic forecasts, the data flow so far this week provided positive economic news for the euro area. For example, the first estimates of inflation in May showed the euro area's headline CPI rising 0.1ppt to -0.1%Y/Y. Perhaps inevitably given the recent tick-up in the oil price, the year-on-year pace of decline in energy prices moderated in May by 0.6ppt to -8.1%Y/Y. Meanwhile, services price inflation was firmer than expected rising 0.1ppt to 1.0%Y/Y and reporting the strongest monthly increase in May since 2008. So, with non-energy industrial goods inflation unchanged at 0.5%Y/Y, core CPI similarly inched 0.1ppt higher to 0.8%Y/Y. Within the largest member states, German inflation figures yesterday surprised on the upside, with the EU harmonised rate rising 0.3ppt to 0.0%Y/Y, while the equivalent French, Italian and Spanish figures aligned with expectations of an increase of 0.1ppt to 0.0%Y/Y, -0.3%Y/Y and -1.1%Y/Y respectively. Looking ahead, not least given the higher oil price, we expect euro area inflation to rise to zero in June and inch steadily higher through the second half of the year to 1%Y/Y by end-2016. Certainly, the Commission's latest sentiment surveys were encouraging about the outlook for inflation, with the indices for selling-price expectations in services and industry both rising markedly in May, with the former at its highest since mid-2011.

Commission's ESI signals ongoing economic expansion

The Commission's latest economic sentiment indicator (ESI) – arguably the most reliable guide to euro area GDP growth – also exceeded expectations with respect to the growth outlook, with the headline index rising 0.7pt to 104.7 in May, the highest level since January to leave the average index so far in Q2 a touch firmer than that seen in Q1, but still well below the levels reached at the end of last year. The detail of the survey was mixed, with the manufacturing-related index unchanged in May (-3.6), while the services-related component declined 0.4pt on the month to 11.3, albeit the latter was still on average so far in Q2 0.8pt higher than in Q1. Meanwhile, construction firms and retailers were reportedly more upbeat about conditions in May, with the latter perhaps associated with the marked improvement in consumer confidence that month. Indeed, this index was confirmed at the flash estimate that had recorded the largest monthly increase since March 2015 to a four-month high of -7.0. This in part reflected greater optimism about the outlook for the labour market over the coming twelve months, with the relevant unemployment indicator falling to its lowest level in ten months. And the survey's assessment of the labour market broadly tallied with the latest hard figures, which confirmed another modest decrease in the number of people unemployed in the region in April, by 63k to 16.42mn, a decline of 1.3mn over the past year to leave the unemployment rate at 10.2%, unchanged on the month but down from 11% in April 2015. Within the country details, there was a notable drop in the French unemployment rate to 9.9% in April, the first single-digit rate since October 2012. In addition, on the national measure, the German unemployment rate fell in May to a new post-reunification low of 6.1%.

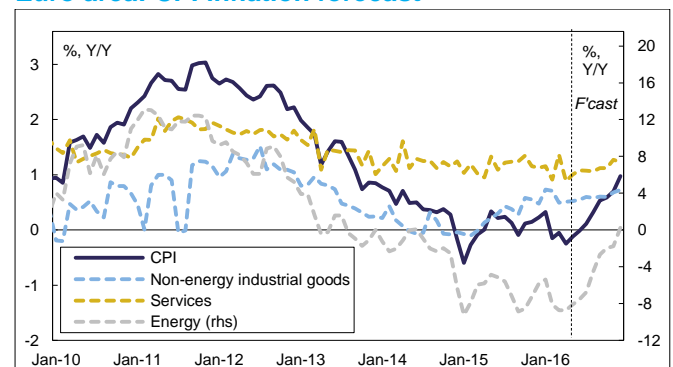
Euro area: CPI inflation in major member states*



*EU harmonised measure.

Source: Datastream and Daiwa Capital Markets Europe Ltd.

Euro area: CPI inflation forecast



Source: Datastream and Daiwa Capital Markets Europe Ltd.



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French ESI outperformed in May after Q1 GDP was revised up

With respect to the country breakdown of the Commission's economic sentiment survey, the French ESI was the outperformer in May, rising 1.5pts to a three-month high of 103.1. However, this still left the average index so far in Q2 slightly weaker than in Q1, suggesting that GDP growth likely moderated in the current quarter from upwardly revised growth of 0.6%Q/Q in Q1. Sentiment was also reported to have improved marginally in Germany and Italy, with the respective ESIs rising to 104.8 and 108.4, their highest levels this year. In contrast, however, there was a reported further deterioration in sentiment in Spain, with that country's ESI falling to 105.7, its lowest level in seventeen months. And with this on average so far in the quarter almost 1½pts lower than in Q1, yesterday's survey suggests that Spanish GDP growth eased in Q2, albeit the economic recovery is likely to have again outperformed the other major member states. Overall, the Commission survey offered cause for optimism that moderate GDP growth will be sustained over the near term. Certainly, the ECB is likely to signal a slightly more upbeat view of the near-term outlook with its GDP forecast likely to be nudged up. And with the oil price now well above the previous assumption (\$34.9pb and \$41.2pb for 2016 and 2017 respectively), the ECB's inflation forecast also seems likely to see an upwards revision when new forecasts are presented on Thursday.

The day ahead in the euro area and US

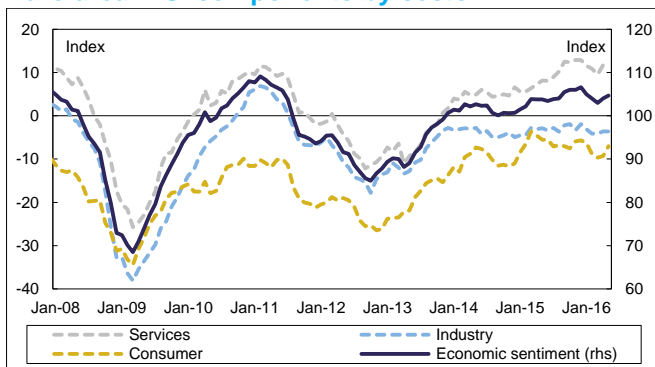
The data focus tomorrow will be the final manufacturing PMIs for May from the euro area and various member states, which are expected to affirm the flash estimates that – in contrast to the Commission's survey – reported a modest decline in the euro area's headline and output PMIs, by 0.2pt to 51.5 and 52.4 respectively. In the US, meanwhile, tomorrow brings the manufacturing ISM, alongside April's construction spending figures and May vehicle sales numbers.

UK

The day ahead in the UK

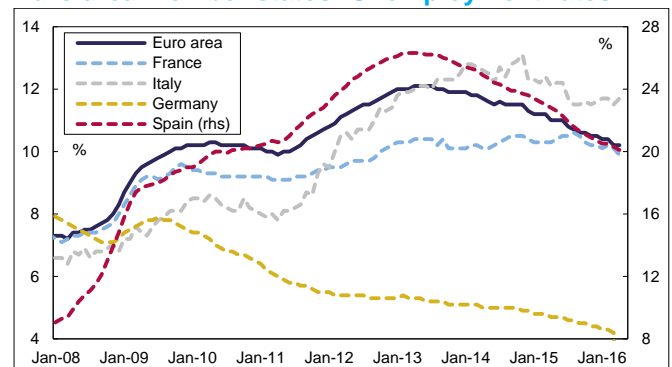
After a quiet start to the holiday-shortened week with no notable economic data out today, the UK data flow resumes tomorrow with the manufacturing PMI survey for May and the BoE's lending figures for April. The headline PMIs were weak across the board in April, and therefore we might well see a small improvement in business sentiment in May. Nevertheless, having fallen to 49.2 the headline manufacturing PMI is expected to have remained below 50 for the second successive month. Meanwhile, after surging in March, new mortgage lending is likely to have dropped significantly in April after the increase in Stamp Duty tax on second properties, while a lower number of mortgage approvals should signal the likelihood of continued moderate housing market activity in the coming months.

Euro area: ESI components by sector



Source: Datastream and Daiwa Capital Markets Europe Ltd.

Euro area member states: Unemployment rates














Source: Datastream 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
EMU	 Unemployment rate %	Apr	10.2	10.2	10.2	-
	 Flash CPI estimate Y/Y%	May	-0.1	<u>-0.2</u>	-0.2	-
	 Flash core CPI estimate Y/Y%	May	0.8	<u>0.8</u>	0.7	-
	 M3 money supply Y/Y%	Apr	4.6	5.0	5.0	-
Germany	 Retail sales M/M% (Y/Y%)	Apr	-0.9 (2.3)	1.0 (1.9)	-1.4 (0.7)	-1.4 (0.6)
	 Unemployment change '000s (rate %)	May	-11 (6.1)	-5 (6.2)	-16 (6.2)	-
France	 Preliminary EU-harmonised CPI Y/Y%	May	0.0	0.0	-0.1	-
Italy	 Unemployment rate %	Apr	11.7	-	11.4	11.5
	 Preliminary EU-harmonised CPI Y/Y%	May	-0.3	-0.3	-0.4	-
	 GDP – final release Q/Q% (Y/Y%)	Q1	0.3 (1.0)	<u>0.3 (1.0)</u>	0.2 (1.1)	-
Spain	 Current account balance €bn	Mar	0.8	-	-1.5	-









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
EMU	 Economic sentiment indicator	May	104.7	104.4	103.9	104.0
	 Services (industrial) sentiment	May	11.3 (-3.6)	11.3 (-3.5)	11.5 (-3.7)	11.7 (-3.6)
	 Final consumer confidence	May	-7.0	<u>-7.0</u>	-9.3	-
	 ECB QE net purchases €bn	Weekly	19.3	<u>18.2</u>	16.9	-
Germany	 Preliminary EU-harmonised CPI Y/Y%	May	0.0	-0.1	-0.3	-
France	 GDP – second release Q/Q% (Y/Y%)	Q1	0.6 (1.4)	<u>0.5 (1.3)</u>	0.5 (1.3)	-
	 Consumer spending M/M% (Y/Y%)	Apr	-0.1 (2.5)	0.0 (2.6)	0.2 (2.7)	1.1 (3.1)
Spain	 Preliminary EU-harmonised CPI Y/Y%	May	-1.1	-1.1	-1.2	-







Auctions

Country	Auction
Italy sold	 €2.5bn of 0.45% 2021 bonds (01-Jun-2021) at an average yield of 0.40%  €3bn of 1.6% 2026 bonds (01-Jun-2026) at an average yield of 1.42%  €2bn of 2023 floating-rate bonds (01-Jun-2023) at an average yield of 0.53%



Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

Tomorrow's data releases

Economic data

Country	BST	Release	Period	Market consensus/ <i>Daiwa forecast</i>	Previous
EMU		09.00 Final manufacturing PMI	May	51.5	51.7
Germany		08.55 Final manufacturing PMI	May	52.4	51.8
France		08.50 Final manufacturing PMI	May	48.3	48.0
Italy		08.45 Manufacturing PMI	May	53.0	53.9
Spain		08.15 Manufacturing PMI	May	52.5	53.5
UK		00.01 BRC shop price index Y/Y%	May	-	-1.7
		07.00 Nationwide house price index M/M% (Y/Y%)	May	0.3 (4.8)	0.2 (4.9)
		09.30 Net consumer credit (net lending secured on dwellings) £bn	Apr	1.6 (3.8)	1.9 (7.4)
		09.30 Mortgage approvals '000s	Apr	67.9	71.4
		09.30 Manufacturing PMI	May	49.6	49.2

Auctions and events

Country	BST	Auction / Event
Germany		10.30 Auction: To sell €4bn of 2021 zero-coupon bonds (09-Apr-2021)
UK		10.30 Auction: To sell £2.75bn of 1.5% 2021 bonds (22-Jan-2021)

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

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