

Euro wrap-up

Overview

- Bunds made modest gains despite a stronger-than-expected German ifo survey, which signalled a firm recovery in Q2.
- Gilts also made gains while UK public borrowing declined in line with expectations and a retail survey suggested that retail sales were broadly in line with seasonal norms in May.
- The coming two days will bring national consumer and business surveys from Germany, France and Italy.

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Daily bond market movements

Bond	Yield	Change
BKO 0 06/23	-0.671	-0.006
OBL 0 04/26	-0.555	-0.022
DBR 0 02/31	-0.167	-0.025
UKT 0 ¹ / ₈ 01/23	0.018	-0.014
UKT 0 ¹ / ₈ 01/26	0.323	-0.016
UKT 4 ³ / ₈ 12/30	0.788	-0.022

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

Source: Bloomberg

Euro area

Strong ifo survey adds to signals of firm rebound in Q2

Broadly consistent with Friday's upbeat [flash PMIs](#), Germany's ifo business survey strongly suggested that economic recovery is once again underway in the euro area's largest economy. In particular, with new cases of Covid-19 falling, more than 44 million vaccine doses administered and some states easing pandemic restrictions once again, the ifo index of current conditions rose for the fourth month in a row, up 1.5pts to a fifteen-month high of 95.7. Moreover, the index of expectations for the coming six months leapt a larger-than-expected 3.7pts to 102.9, matching the best reading since 2011. As a result, the survey's headline business climate index rose 2.5pts to 99.2, above the long-run average and the highest in two years.

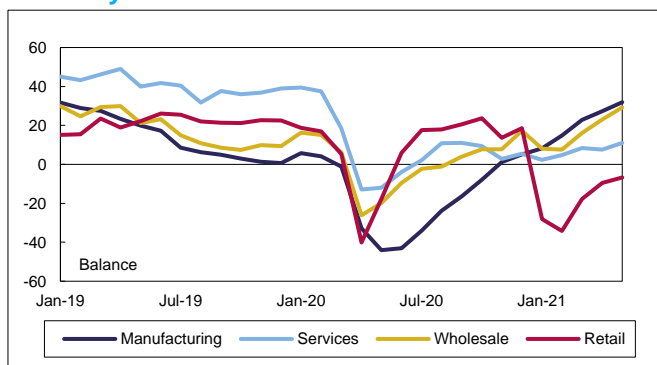
Current conditions judged to be more favourable in every sector

The improvement this month was broad-based, with the indices of current conditions increasing in every sector. Contrasting with the findings of the flash PMIs, which suggested that supply bottlenecks were stifling production somewhat, manufacturers signalled that conditions in May were the best since December 2018. And benefiting from developments in the factory sector, current conditions for wholesalers were similarly judged the most favourable in more than two years and much better than the long-run average. With the relaxation of pandemic restrictions still gradual and geographically limited, however, the respective index for services rose only to its highest since September, and was still a long way below the pre-pandemic level. Likewise, conditions for retailers, who await the green light for reopening on a national basis, were merely the best since December and, on average, remained adverse. And construction firms reported only a modest improvement, albeit judging the situation still to be favourable.

Expectations improving markedly in services and retail

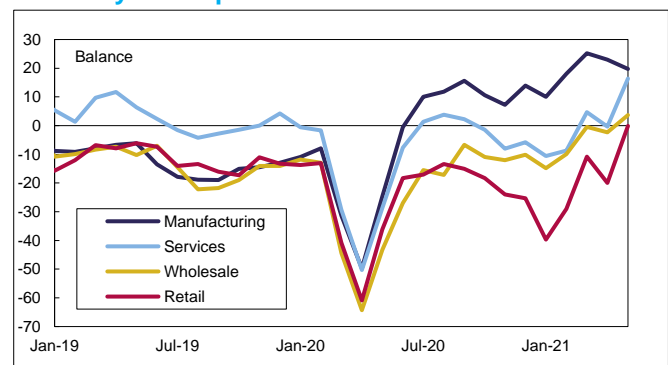
Looking ahead, with some three-quarters of the population expected to have received two doses of vaccine within two months, the anticipation of steady reopening of the economy provided a big boost to expectations in those sectors still affected by restrictions. So, for example, expectations for the coming six months in services leapt to the most favourable since August 2018. And while no better than neutral, expectations in retail were the least adverse since November 2017. Wholesalers were the most upbeat about the outlook since mid-2018. And while firms in the sector were still downbeat and complaining of shortages of materials, expectations among construction firms were the least adverse since the onset of the pandemic. Finally, with rising orders and expectations of increased output prices, manufacturers remain highly upbeat about

Germany: ifo current conditions indices



Source: Refinitiv and Daiwa Capital Markets Europe Ltd.

Germany: ifo expectations indices



Source: Refinitiv and Daiwa Capital Markets Europe Ltd.

the future. Nevertheless, supply-side challenges meant that the ifo index of manufacturers' expectations for the coming six months fell back for a second successive month and to a three-month low having reached a decade high in March.

Consumption weakness more than fully explained drop in GDP in Q1

Today's updated German GDP data made a trivial revision to the size of the contraction in Q1, which was just 0.1ppt sharper than previously thought at 1.8%Q/Q. On a working-day adjusted basis, that left German GDP down 3.1%Y/Y and 5.0% below the pre-pandemic level in Q419. Private consumption more than fully explained the drop in overall output in Q1, falling 5.4%Q/Q in response to the tighter pandemic containment measures. A slowdown in the pace of destocking meant that inventories provided some offset, adding 1.4ppts to GDP growth, while government consumption (0.2%Q/Q) continued to grow. And construction investment (up 1.1%Q/Q) rose close to the previous peak reached in Q120, while investment in machinery and equipment was little changed (-0.2%Q/Q). With imports (3.8%Q/Q) outpacing exports (1.8%Q/Q) due not least to weakness in shipments to the UK, net trade subtracted 0.6ppt from GDP growth. Private consumption and investment in equipment, machinery and intellectual property will rebound somewhat in the current quarter, while construction output should post further growth. With exports likely to accelerate faster than imports, the contribution to GDP growth from net trade in Q2 should become positive too. But with inventories being run down amid supply strains, stock-building is likely to subtract from GDP growth in the current quarter. With further reopening of the economy likely over coming weeks, GDP in Q321 should rise above the Q320 level. And the pre-pandemic level of total economic output will probably be surpassed around the turn of the year.

The coming two days in the euro area

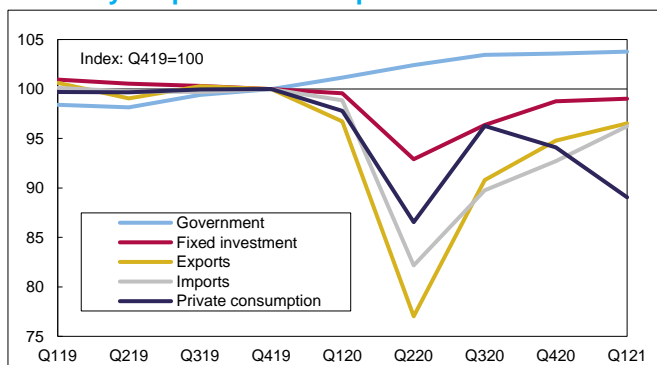
Looking ahead, the focus tomorrow turns to France, where INSEE will publish its latest business and consumer sentiment surveys, which are expected to add to the recent run of upbeat economic confidence indicators. Following today's improved German ifo survey, INSEE's measure of business confidence is expected to rise 2.7pts to 98 in May, the highest level since February last year, albeit still some way off that month's level of 105.3 and also below the long-run average. Manufacturing confidence should rise further above its pre-pandemic and long-run levels to the highest since November 2018. Services sentiment should improve too. And the INSEE consumer confidence indicator is expected to rise 3pts in May to 97, which would be the highest level since March last year. Thursday will bring the equivalent ISTAT Italian economic survey results for May, which are expected to report further improvement in business and consumer sentiment. In particular, confidence among Italian manufacturers is expected to rise to the highest since July 2018 while consumers are expected to be the most upbeat since the onset of the pandemic. The German GfK consumer confidence survey will also likely report improved sentiment, albeit likely merely to the best since last autumn.

UK

UK public borrowing down from a year ago as expected

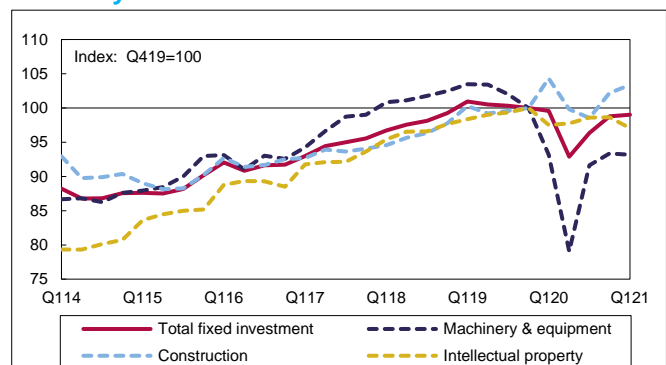
In line with expectations, UK public sector net borrowing (excluding banks) came in at £31.7bn in April, down from the record high of £47.2bn recorded in the same month last year but unsurprisingly still the second highest deficit for April on record. And while updated estimates revised down total borrowing over the past fiscal year by £2.8bn (0.2ppt) to £300.3bn (14.3% of GDP), this was still comfortably a record high in nominal terms and the highest since 1946 as a share of national output. In terms of the monthly update, the improvement in April from a year ago reflected both stronger revenues and lower public spending. Indeed, central government receipts rose £3.8bn (7.0%) compared with April 2020 to £58.0bn, with tax receipts up £7bn (20%), including a notable increase in PAYE income tax contributions (up £2.1bn, 16.4%) as the UK's lockdowns began gradually to ease. Against this backdrop, the government's contribution towards the Coronavirus Jobs Retention Scheme and the Self Employment Income Support Scheme (£5.5bn) was also notably smaller than a year earlier as the number of people on furlough more than halved from the average of more than 8.7mn in April 2020. And overall central

Germany: Expenditure components of GDP



Source: Refinitiv and Daiwa Capital Markets Europe Ltd.

Germany: Fixed investment



Source: Refinitiv and Daiwa Capital Markets Europe Ltd.

government expenditure was down £12.9bn (11.9%) from a year earlier. While today's figures were lower than the OBR's expectations, they do not yet incorporate estimates of future losses from the state-backed emergency loan guarantee schemes, which in due course will be recorded as public spending at the point at which the funds were issued.

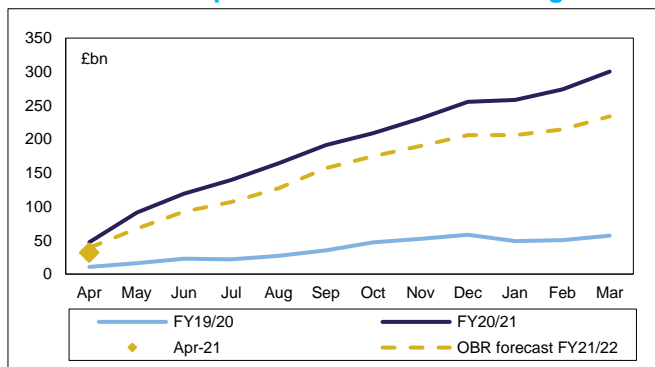
Retail survey suggests sales in line with seasonal norms in May

While last week's official [retail sales figures](#) reported an extreme surge in spending in April as non-essential stores reopened, today's CBI Distributive Trades Survey suggested that sales in May were more in line with seasonal norms. Despite the survey's headline sales index coming in well above most levels registered over the past 2½ years, it still fell short of expectations, dropping by 2ppts from April to +18%, a level which was flattered by the low levels of activity this time last year. Indeed, while today's quarterly survey suggested that retailers had significantly revised up their investment intentions for the coming 12 months – the relevant index was the highest since February 1994 – it also suggested that employment intentions remained weak and overall business sentiment in the sector was still relatively subdued. Grocers, DIY, furniture and non-store retailers continued to report firm sales. However, after a stronger April, clothing outlets reported a drop in sales to significantly below average for the time of year, in part likely reflecting appalling unseasonable weather. It is notable, however, that the survey was conducted just before the reopening of indoor dining in restaurants on 17 May, which retail consultancy Springboard suggested provided a boost to retail footfall during the evening. Overall, however, Springboard estimates that retail footfall last week still remained some 28.7% below that during the equivalent week in 2019, suggesting that conditions on the high street remain far from normal and that online sales remain strongly in favour. Separately, and more happily, the CBI survey suggested that sales for wholesalers and motor traders were above the respective norms for the time of year in May, and that both sectors expect sales to remain strong in June.

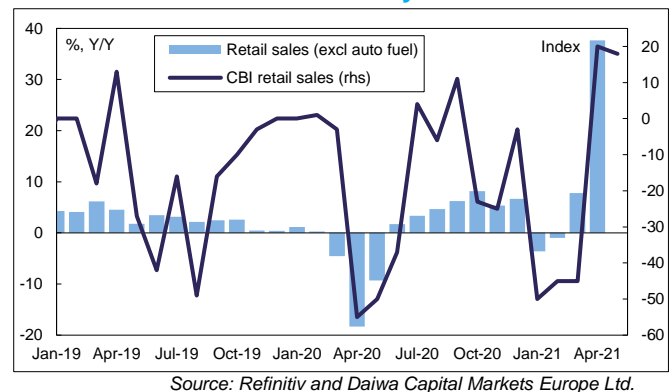
The coming two days in the UK

The coming two days in the UK are set to be very quiet with no top-tier economic data due for release.

UK: Cumulative public sector net borrowing



UK: Retail sales and CBI survey









The next edition of the Euro wrap-up will be published on 27 May 2021

European calendar

Today's results

Economic data

Country	Release	Period	Actual	Market consensus/ <i>Daiwa forecast</i>	Previous	Revised
Germany	 Final GDP Q/Q% (Y/Y%)	Q1	-1.8 (-3.1)	-1.7 (-3.0)	0.5 (-3.3)	-
	 Ifo business climate	May	99.2	98.0	96.8	96.6
	 Ifo current assessment balance (expectations)	May	95.7 (102.9)	95.5 (101.0)	94.1 (99.5)	94.2 (99.2)
Spain	 PPI Y/Y%	Apr	12.8	-	6.3	6.4
UK	 Public sector net borrowing, excluding banks £bn	Apr	31.7	34.9	28.0	26.3
	 CBI distributive trades survey, reported sales	May	18	-	20	-




Auctions

Country	Auction
- Nothing to report -	





Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

Tomorrow's releases

Economic data

Country	BST	Release	Period	Market consensus/ <i>Daiwa forecast</i>	Previous
France	 07.45	INSEE business confidence	May	98	95
	 07.45	INSEE manufacturing confidence (production outlook)	May	105 (-)	104 (2)
	 07.45	INSEE consumer confidence	May	97	94




Auctions and events

EMU	 10.00	ECB's Villeroy speaks at French National Assembly
Germany	 10.30	Auction: €2.5bn of 0% 2036 bonds
Italy	 10.00	Auction: €1.25bn of 0% 2022 bonds
	 10.00	Auction: €1.25bn of 0.4% 2030 index-linked bonds





Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

Thursday's releases

Economic data

Country	BST	Release	Period	Market consensus/ <i>Daiwa forecast</i>	Previous
Germany	 07.00	GfK consumer confidence	Jun	-5.0	-8.8
Italy	 09.00	ISTAT economic sentiment	May	-	97.3
	 09.00	ISTAT consumer confidence (manufacturing)	May	103.7 (106.0)	102.3 (105.4)

Auctions and events

EMU	 10.45	ECB's de Guindos attends virtual conference on financial integration
	 13.00	ECB's Weidmann scheduled to speak at the German Economic Institute
	 14.00	ECB's Schnabel gives a speech at the New Economy Forum
UK	 12.00	BoE's Vlieghe gives a speech 'What government bond yields can tell us about future growth and inflation'

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

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