

Euro wrap-up

Overview

- Despite a very strong Commission sentiment survey, Bunds made modest gains while consumer price expectations remained well-contained and the flash estimate of French inflation in May suggested that underlying price pressures remain subdued.
- Gilts followed USTs higher while a business survey suggested that wage and price expectations remain well-contained despite strong sentiment.
- The coming week brings the flash estimates of euro area inflation in May as well as unemployment, retail sales and bank lending data from the region.

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Daily bond market movements

Bond	Yield	Change
BKO 0 06/23	-0.674	-0.001
OBL 0 04/26	-0.571	-0.013
DBR 0 02/31	-0.186	-0.011
UKT 0 ¹ / ₈ 01/23	0.047	+0.003
UKT 0 ¹ / ₈ 01/26	0.332	-0.012
UKT 4 ³ / ₄ 12/30	0.789	-0.020

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

Source: Bloomberg

Euro area

Commission sentiment index up to 3-year high with improvement across all sectors

Following this week's strong [survey results](#) from the largest member states, as well as the upbeat [flash PMIs](#) a week ago, today's Commission economic sentiment indices (ESIs) for May were bound to signal a significant pickup in recovery momentum. In the event, however, they still beat expectations, with broad-based improvement across sectors and member states. The headline euro area ESI rose 4pts to 114.2, the highest since January 2018 and a level surpassed only twice in the past twenty years. While the German and French ESIs also rose to their best since 2018, the Italian headline index reached its highest level in more than two decades. And, of all the member states to report, only Slovakia's ESI declined. At the sectoral level, for the third successive month, services reported the largest improvement, with the sentiment index rising above the long-run average to the best since December 2019. Retail confidence also rose to the highest since just before the pandemic and above the long-run average as business expectations improved. Buoyed by rising orders, construction firms were the most upbeat since February 2020. And confidence in industry increased to a series high as stock adequacy declined further while new orders rose to the highest since mid-2018. Sentiment in financial services improved to a three-year high.

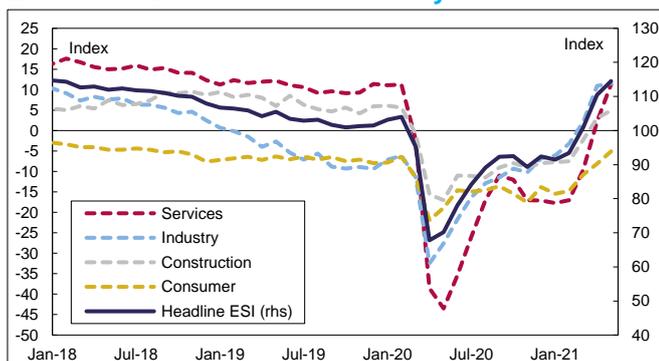
Price expectations very high in industry, but well-contained in services and among consumers

With confidence significantly improved, business employment expectations jumped above the long-run average to the highest since late 2018 with all sectors reportedly adding to headcount at the fast rate since at least the start of the pandemic. And with fears of unemployment likewise down to the lowest since the arrival of Covid-19, the rise in consumer confidence further above its long-run average to the best since October 2018 was confirmed. Within the detail, consumers were much more upbeat about the future, but were slightly less inclined to make major purchases after a significant rise in the respective indicator in April. Nevertheless, with demand expected to pick up and cost pressures strong, businesses' selling-price expectations rose across the sectors. Selling price expectations in industry reached a series high, those in construction rose to their highest in more than twenty years, and retail price expectations were the highest in a decade. But price expectations in services were merely the highest since the start of 2020 and consumer price expectations were also well-contained, rising only to a twelve-month high and still just below their long-run average.

Flash French inflation higher due to energy, core components still subdued despite bottlenecks

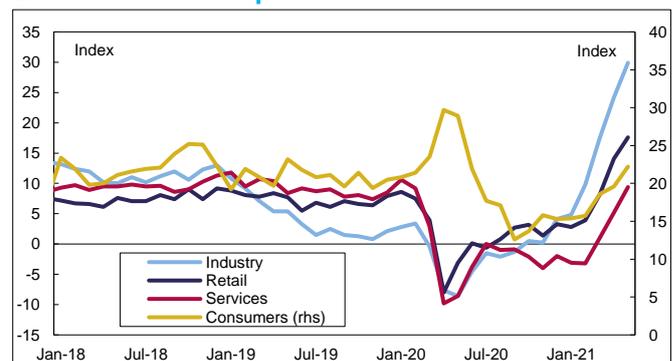
The first estimates of inflation in May, which came today from France, predictably reported further increases in the headline rates, while the detail strongly suggested that underlying price pressures remain subdued. In particular, in line with

Euro area: Economic sentiment by sector



Source: European Commission, Refinitiv and Daiwa Capital Markets Europe Ltd.

Euro area: Price expectations*



*Selling-price expectations except for consumers. Source: European Commission, Refinitiv and Daiwa Capital Markets Europe Ltd.

expectations, inflation on the national CPI measure rose 0.2ppt to 1.4%Y/Y, the highest since February 2020. And the EU-harmonised HICP measure also rose 0.2ppt in May to 1.8%Y/Y, the highest since December 2018. The detail published on the national basis showed that energy was again by far the main driver of the rise in inflation, increasing 3.0ppts to 11.8%Y/Y, the highest since October 2018. As such, energy contributed 0.9ppt to the headline CPI rate, 0.2ppt more than in April. Among the other major components, however, food inflation edged up only very slightly from April's six-year low, by 0.1ppt to -0.2%Y/Y. And while inflation of manufactured goods rose 0.2ppt, at zero percent it was still just 0.1 ppt above the average of the prior twelve months and thus suggested that pressures related to supply bottlenecks remain largely absorbed by margins. Moreover, as services inflation dropped 0.2ppt to a three-month low of 1.0%Y/Y, French core inflation (excluding energy, food and tobacco) on the national basis remained unchanged at a highly subdued 0.7%Y/Y.

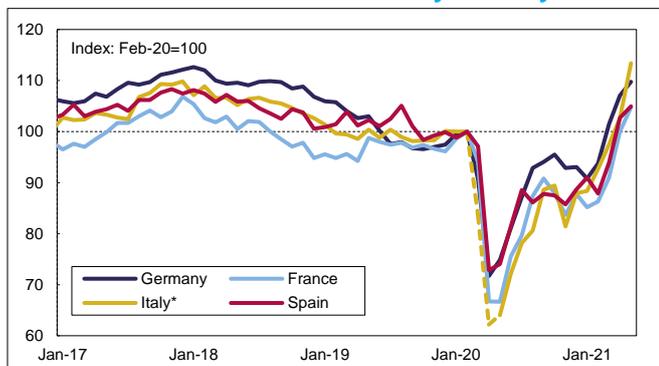
French spending down sharply in April on lockdown

Today's French activity data were weaker than expected, reporting a sharp drop in consumer spending on goods in April and a downwards revision to GDP in Q1. The re-imposition of national lockdown restrictions from the 3rd of the month saw household expenditure on goods drop 8.3%M/M in April to be down 8.6% from the Q1 average. Spending on clothing and textiles halved last month. And expenditure on durable goods dropped more than one tenth with purchases of goods for the home down more than one fifth. Spending on transport goods was down just 2.8%M/M, with smaller declines also in spending on energy and food. The decline in household spending in April left it some 9.5% below the average level in Q419 before the pandemic struck, a significantly smaller fall than those during the lockdowns the prior April (when expenditure dropped by almost one third from the pre-pandemic level) and November 2020 (when it fell 13.6% on the same basis). And not least with the household savings still historically high at above 20% in Q1, we expect spending on both goods and services to rebound quickly as and when the pandemic restrictions are fully removed.

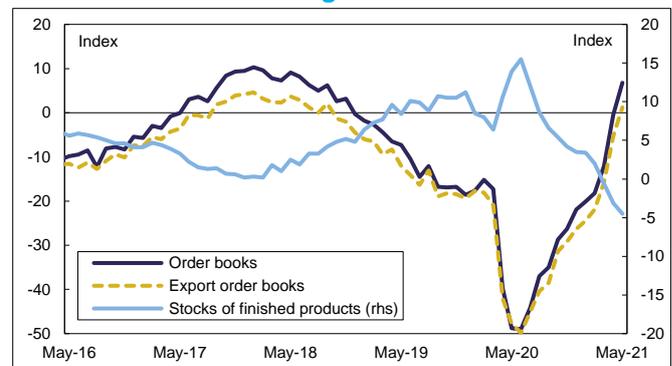
Revisions wipe out French GDP growth in Q1

The French spending numbers for April illustrated the continued significant volatility of economic activity from one month to the next in response to the changing trends in the pandemic and associated restrictions. And significant revisions to the estimate of French GDP in Q1 and all of its components highlighted the difficulty faced in gauging accurately the recent profile and current level of activity. In particular, a downwards revision meant that French economic output contracted 0.1%Q/Q in Q1 having previously been judged to have grown by 0.4%Q/Q. As such, it was 4.7% below the pre-pandemic level in Q419, 0.3ppt more than thought beforehand. Among the expenditure components, household consumption growth was slightly weaker than previously thought at 0.1%Q/Q although the drop the prior quarter was revised down slightly. Fixed investment growth (just 0.2%Q/Q) was a full 2ppts softer than in the preliminary estimate. But net trade on both sides of the

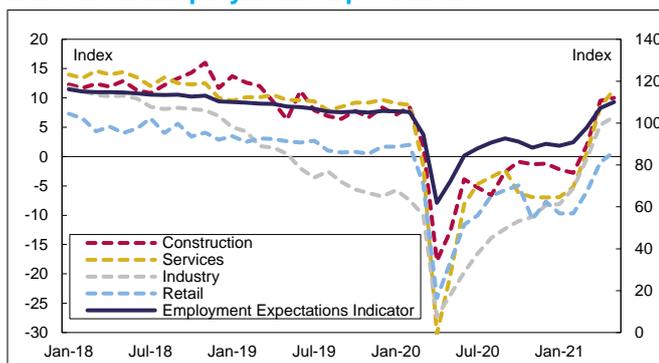
Euro area: Economic sentiment by country



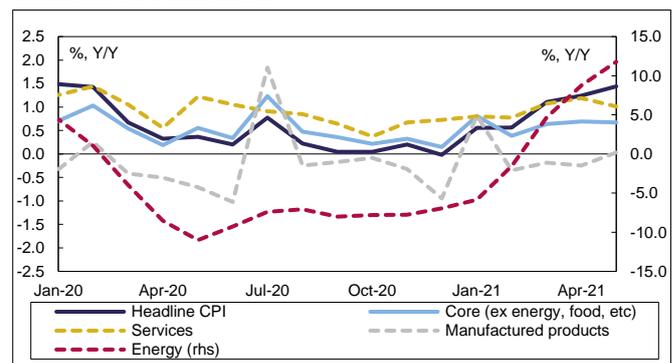
Euro area: Manufacturing new orders and stocks



Euro area: Employment expectations*



France: CPI inflation*



ledger was stronger than previously thought, with exports now down just 0.2%Q/Q and imports up 1.1%Q/Q, while inventories are now thought to have supported growth (a contribution to 0.2ppt). Despite the weak start to Q2 for spending, and lower base, we continue to expect French GDP to post positive growth in Q2 and accelerate markedly in Q3 and Q4.

The week ahead in the euro area

The coming week brings a number of top-tier economic data from the euro area, including the remaining flash estimates of May inflation. The German, Italian and Spanish CPI data are all due on Monday followed by the euro area inflation figures on Tuesday. Principally due to energy prices, we expect the headline euro area CPI rate to rise 0.2ppt to 1.8%Y/Y in May. Core inflation might at most edge up just 0.1ppt to a still-subdued 0.8%Y/Y, as pandemic restrictions continue to weigh on prices of consumer-facing services. Retail sales also feature in the coming week, with the German figures coming on Monday and the euro area numbers released on Friday. After jumping a vigorous 7.7%M/M in March, German retail sales are expected to fall back in April as the country entered stricter lockdown measures. And given that the extended lockdown in France was also reflected in much weaker consumer spending numbers, the aggregate euro area measure of retail sales seems bound to post a significant fall. However, May new car registrations data for France, Italy and Spain will be published on Tuesday, followed by the German figures on Thursday, and these are likely to be firm. Among other noteworthy releases, bank lending data for April are due Monday, labour market data from Germany (for the current month) and the euro area (for April) are due on Tuesday, followed by Spanish unemployment numbers (for May) on Wednesday.

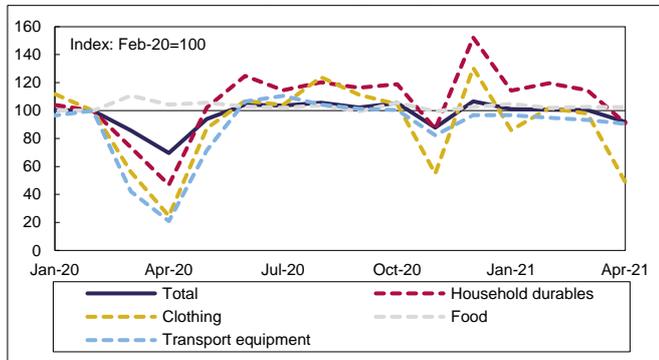
Survey-wise, Tuesday brings the release of the final manufacturing PMIs, which will be followed on Thursday by the final services and composite PMIs. All are expected to align with the upbeat picture painted by the flash data. In particular, the euro area composite PMI rose 3.1pts to 56.9, the highest since February 2018, while the respective new orders index increased to the best since mid-2006. According to the survey, the acceleration in overall euro area economic activity was driven by the services sector albeit with growth in manufacturing continuing to lead the recovery despite worsening supply bottlenecks. Notably perhaps, the factory input and output price gauges rose to the highest levels on the respective series. Friday's construction PMIs for May should also point to an improvement in economic activity.

UK

Lloyds business barometer signals jump in optimism but measured wage and price expectations

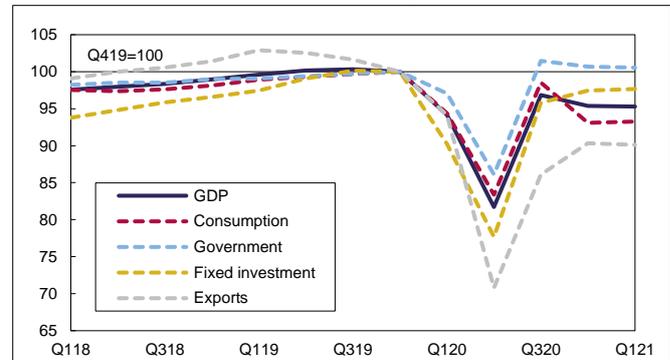
A quiet end to a relatively uneventful week for UK economic data brought the latest Lloyds Business Barometer, which provided more good news about economic sentiment. According to this survey, business optimism regarding the economy

France: Consumer spending on goods



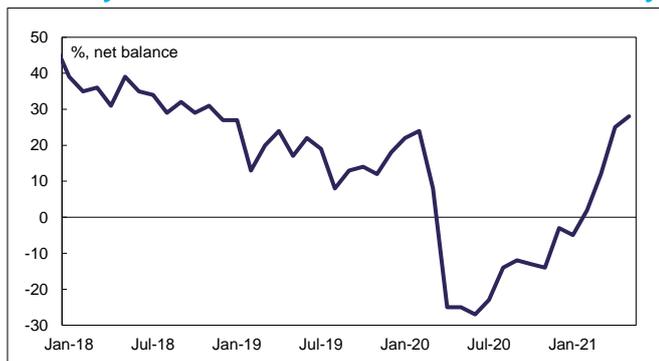
Source: Refinitiv and Daiwa Capital Markets Europe Ltd.

France: GDP and selected components



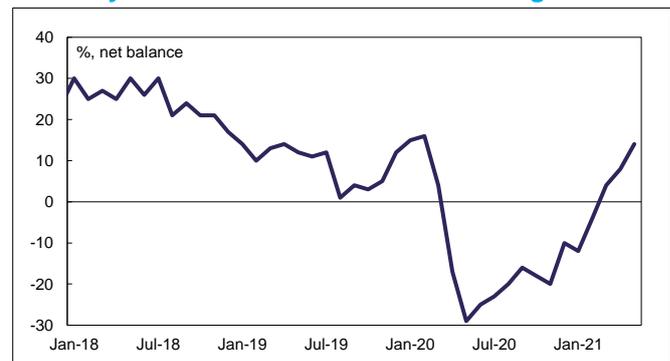
Source: Refinitiv and Daiwa Capital Markets Europe Ltd.

UK: Lloyds business barometer – Business activity



Source: Refinitiv and Daiwa Capital Markets Europe Ltd.

UK: Lloyds business barometer – Staffing levels



Source: Refinitiv and Daiwa Capital Markets Europe Ltd.

rose 5ppts to 37%, the highest since before the Brexit referendum in 2016. Overall business confidence rose 4ppts to a three-year high of 33%. And firms judged their trading prospects for the coming year to be the best since late 2018. Confidence increased across all sectors, with manufacturers (53%) and retailers (44%) leading the way, but firms in construction (35%) and services (26%) also on balance upbeat. While net hiring expectations also rose to the best since 2018, there was no sign of pressure on wage expectations, with one fifth of firms still expecting to freeze pay over the coming year and less than one quarter of firms – a smaller share of firms ahead of the pandemic – expecting pay growth of at least 2%Y/Y. And while firms' price expectations rose, they remained below the averages in 2018 and 2019.

The week ahead in the UK

Following Monday's bank holiday, the UK data calendar begins on Tuesday with the release of the final manufacturing PMI for May, which will be followed on Thursday by the release of the final service sector and composite PMIs. The flash PMIs suggested that economic activity accelerated in May at the strongest rate on the series, with the composite index up 1.3ppts to a record high of 62.0, job creation the strongest since 2014, and growth seemingly broad-based. Unlike the euro area, however, the flash data suggested that the improvement in the UK this month was led by manufacturing, with the respective output PMI up 4ppts to 63.2, the highest in almost eight years. And while it benefited directly from the further relaxation of pandemic restrictions this month, the improvement in services was more modest, with the respective activity PMI up just 0.8pt to 61.8, still nevertheless the best since October 2013. Friday's construction PMI, meanwhile, is also expected to remain close to March's high of 61.7 after moving broadly sideways in April. Other data to be published in the coming week include the latest BoE bank lending figures for April (on Wednesday). In March, households continued making net repayments of consumer credit, while mortgage borrowing was the strongest since the series began in April 1993, driven by the expected ending of the temporary stamp duty tax relief at the end of March, which has now been extended to the end of June. Meanwhile, May data due include the Nationwide house price index on Tuesday, followed by the BRC shop price index on Wednesday and new car registrations on Friday.

The next edition of the Euro wrap-up will be published on 4 June 2021

Daiwa economic forecasts

	2020	2021				2022	2020	2021	2022
	Q4	Q1	Q2	Q3	Q4	Q1			
GDP growth, %, Q/Q									
Euro area 	-0.7	-0.6	1.4	1.8	1.2	1.0	-6.7	3.9	4.3
Germany 	0.5	-1.8	1.8	1.5	1.4	1.0	-5.1	2.6	4.4
France 	-1.5	-0.1	1.0	1.6	1.4	1.2	-8.0	5.5	4.7
Italy 	-1.8	-0.4	1.5	1.7	1.4	1.3	-8.9	4.3	5.1
Spain 	0.0	-1.0	1.6	2.0	1.6	1.5	-10.8	4.9	6.2
UK 	1.3	-1.5	3.5	3.2	2.5	1.0	-9.8	6.6	6.2
Euro area									
Headline CPI 	-0.3	1.1	1.7	1.9	2.1	0.9	0.3	1.7	1.1
Core CPI 	0.2	1.2	0.7	0.8	1.1	0.3	0.7	0.9	0.8
UK									
Headline CPI 	0.5	0.6	1.7	1.8	2.5	2.4	0.9	1.6	1.9
Core CPI 	1.3	1.1	1.3	1.4	1.8	1.7	1.4	1.4	1.7
ECB									
Refi Rate % 	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00
Deposit Rate % 	-0.50	-0.50	-0.50	-0.50	-0.50	-0.50	-0.50	-0.50	-0.50
PEPP envelope* (€bn) 	1850	1850	1850	1850	1850	1850	1850	1850	1850
BoE									
Bank Rate % 	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10
Bond purchases** (£bn) 	895	895	895	895	895	895	895	895	895

*Monthly target €bn, end of period. **Monthly target £bn, end of period. Source: Bloomberg, ECB, BoE 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/ <i>Daiwa</i> <i>forecast/actual</i>	Previous
Monday 31 May 2021					
EMU		09.00 M3 money supply Y/Y%	Apr	9.6	10.1
Germany		13.00 Preliminary CPI (EU-harmonised CPI) Y/Y%	May	2.3 (2.3)	2.0 (2.1)
		- Retail sales* M/M% (Y/Y%)	Apr	-2.8 (8.7)	7.7 (11.6)
Italy		10.00 Preliminary CPI (EU-harmonised CPI) Y/Y%	May	- (1.3)	1.1 (1.0)
Spain		08.00 Preliminary CPI (EU-harmonised CPI) Y/Y%	May	- (2.5)	2.2 (2.0)
Tuesday 01 Jun 2021					
EMU		09.00 Final manufacturing PMI	May	62.8	62.9
		10.00 Preliminary CPI (core CPI) Y/Y%	May	<u>1.8 (0.8)</u>	1.6 (0.7)
		10.00 Unemployment rate %	Apr	8.1	8.1
Germany		08.55 Final manufacturing PMI	May	56.2	55.8
		08.55 Unemployment rate % (change '000s)	May	6.0 (-7.5)	6.0 (9.0)
France		08.50 Final manufacturing PMI	May	59.2	58.9
		- New car registrations* Y/Y%	May	-	569
Italy		08.45 Manufacturing PMI	May	62.2	60.7
		09.00 Preliminary unemployment rate %	Apr	10.0	10.1
		10.00 Final GDP Q/Q% (Y/Y%)	Q1	-0.4 (-1.4)	-1.8 (-6.6)
		17.00 New car registrations Y/Y%	May	-	3276
Spain		08.15 Manufacturing PMI	May	59.1	57.7
		- New car registrations* Y/Y%	May	-	1787
UK		07.00 Nationwide house price index M/M% (Y/Y%)	May	1.0 (9.4)	2.1 (7.1)
		09.30 Final manufacturing PMI	May	66.1	60.9
Wednesday 02 Jun 2021					
EMU		10.00 PPI Y/Y%	Apr	7.3	4.3
Spain		08.00 Unemployment change '000s	May	-	-39.0
UK		00.01 BRC shop price index Y/Y%	May	-	-1.3
		09.30 Net consumer credit £bn (Y/Y%)	Apr	0.8 (-)	-0.5 (-8.6)
		09.30 Net mortgage lending £bn (approvals '000s)	Apr	6.6 (80.0)	11.8 (82.7)
		09.30 M4 money supply Y/Y%	Apr	-	10.8
Thursday 03 Jun 2021					
EMU		09.00 Final services (composite) PMI	May	55.1 (56.9)	50.5 (53.8)
Germany		08.55 Final services (composite) PMI	May	52.8 (56.2)	49.9 (55.8)
		- New car registrations* Y/Y%	May	-	90.0
France		08.50 Final services (composite) PMI	May	56.6 (57.0)	50.3 (51.6)
Italy		08.45 Services (composite) PMI	May	-	47.3 (51.2)
Spain		08.15 Services (composite) PMI	May	-	54.6 (55.2)
UK		09.30 Final services (composite) PMI	May	61.8 (62.0)	61.0 (60.7)
Friday 04 Jun 2021					
EMU		10.00 Retail sales M/M% (Y/Y%)	Apr	-0.8 (25.5)	2.7 (12.0)
Germany		08.30 Construction PMI	May	-	46.2
France		- Construction PMI	May	-	49.8
Italy		- Construction PMI	May	-	57.6
UK		New car registrations Y/Y%	May	-	3176
		09.30 Construction PMI	May	-	61.6

*Approximate date of release. Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

The coming week's key events & auctions

Country	BST	Event / Auction
Monday 31 May 2021		
EMU	 09.30	ECB's Visco scheduled to speak
	 10.00	OECD publishes Economic Outlook
UK	 -	Public holiday – Late Spring
Tuesday 01 Jun 2021		
Germany	 10.30	Auction: €400mn of 0.5% 2030 index-linked bonds
UK	 16.00	BoE Governor Bailey scheduled to speak – 'Building a finance system fit for a clean, resilient and just future'
Wednesday 02 Jun 2021		
Germany	 10.30	Auction: €4bn of 0% 2026 bonds
UK	 10.00	Auction: £2.75bn of 0.25% 2031 bonds
	 11.30	Auction: £2bn 0.875% 2046 bonds
Thursday 03 Jun 2021		
EMU	 -	Public holiday (Germany, Spain and some other member states) – Corpus Christi
France	 09.50	Auction: 0% 2031 bonds
	 09.50	Auction: 0.5% 2044 bonds
	 09.50	Auction: 4% 2055 bonds
	 09.50	Auction: 0.5% 2072 bonds
Spain	 09.30	Auction: fixed-rate bonds
Friday 04 Jun 2021		
EMU	 -	ECB President Lagarde participates in conference on climate change
	 07.30	ECB's Fernandez-Bollo scheduled to speak at the European Forum of Deposit Insurers
UK	 -	G7 financial ministers' meeting

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

Today's results

Economic data						
Country	Release	Period	Actual	Market consensus/ <i>Daiwa forecast</i>	Previous	Revised
EMU	 European Commission economic confidence	May	114.5	112.1	110.3	110.5
	 European Commission final consumer confidence	May	-5.1	-5.1	-8.1	-
	 European Commission industrial confidence (services)	May	11.5 (11.3)	11.4 (6.3)	10.7 (2.1)	10.9 (2.2)
France	 PPI Y/Y%	Apr	7.3	-	4.5	4.6
	 Consumer spending M/M% (Y/Y%)	Apr	-8.3 (32.0)	-4.0 (37.6)	-1.1 (18.7)	-0.3 (16.8)
	 Preliminary CPI (EU-harmonised CPI) Y/Y%	May	1.4 (1.8)	1.4 (1.8)	1.2 (1.6)	-
	 Final GDP Q/Q% (Y/Y%)	Q1	-0.1 (1.2)	0.4 (1.5)	-1.4 (-4.8)	-
Italy	 PPI Y/Y%	Apr	7.9	-	3.0	-
Spain	 Retail sales Y/Y%	Apr	41.0	29.1	14.9	14.3
UK	 Lloyds business barometer	May	33	-	29	-
Auctions						
Country	Auction					
Italy	 sold €3bn of 0% 2026 bonds at an average yield of 0.17%					
	 sold €3.5bn of 0.6% 2031 bonds at an average yield of 0.94%					
	 sold €2bn of 2026 floating-rate bonds at an average yield of -0.07%					

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

Access our research blog at:

<https://www.uk.daiwacm.com/ficc-research/recent-blogs>

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