

Euro wrap-up

Overview

- On a quiet day for economic data from the euro area, longer-dated Bunds made gains even as the hawkish minority on the ECB's Governing Council flagged their concerns about inflation risks.
- Gilts made gains while data confirmed that UK GDP posted further firm growth in April.
- The coming week will bring updates on euro area IP and UK inflation, jobs and retail sales, as well as the final estimates of euro area inflation in May.

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Daily bond market movements

Bond	Yield	Change
BKO 0 06/23	-0.694	+0.001
OBL 0 04/26	-0.634	-0.003
DBR 0 02/31	-0.272	-0.015
UKT 0 ¹ / ₈ 01/23	0.045	-0.009
UKT 0 ¹ / ₈ 01/26	0.289	-0.026
UKT 4 ³ / ₄ 12/30	0.709	-0.036

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

Source: Bloomberg

UK

Services reopening pushes GDP to post-pandemic high in April

Broadly in line with expectations, UK GDP rose 2.3%M/M in April, an acceleration of 0.2ppt from March and the firmest rate in nine months. Growth in April pushed the level of GDP 1.2% above the previous pandemic era peak in October but still left it some 3.7% below the pre-pandemic level in February 2020. UK GDP growth in April was driven by services, for which activity rose a steeper-than-expected 3.4%M/M, which was also the best rate in the sector since July but left the level 4.1% below that before the pandemic. Growth was especially strong in hospitality, up 44.0%M/M as outdoor service resumed, albeit leaving the level still more than 40% below that in February 2020. In addition, the return of pupils back to school for the first full month since November saw education activity rise 11.1%M/M to the highest level since the arrival of Covid-19. And the reopening of non-essential stores helped wholesale and retail output rise 8.9%M/M back above the respective pre-pandemic level.

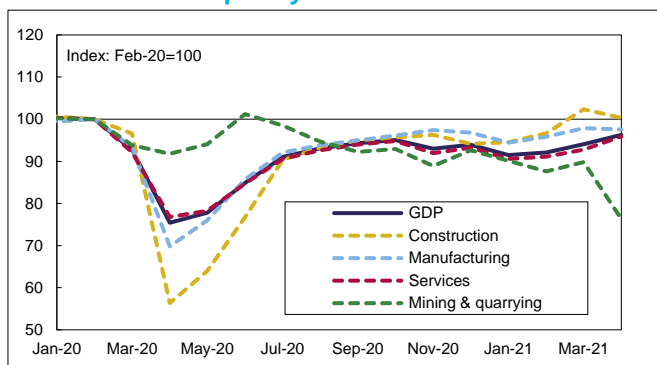
Drop in production in April largely reflects temporary factors

Beyond services, the other major sectors saw declines in production in April, largely reflecting temporary factors. Construction output slipped back 2.0%M/M in April, likely representing payback from vigorous growth of 5.8%M/M in March. Planned maintenance at oil fields saw mining and quarrying output drop a steep 15.0%M/M. And manufacturing output edged down 0.3%M/M, with supply bottlenecks weighing. Production of pharmaceuticals plunged 16.0%M/M back to the lowest level since 2019. And output of transport equipment fell 2.8%M/M, with car production now more than 11% below the pre-pandemic level. Further growth in items such as chemicals (3.8%M/M) and computers and electronics (1.1%M/M) pushed output in those subsectors up 14.1% and 9.4% above their respective levels in February 2020.

Ongoing evidence of trade diversion due to Brexit

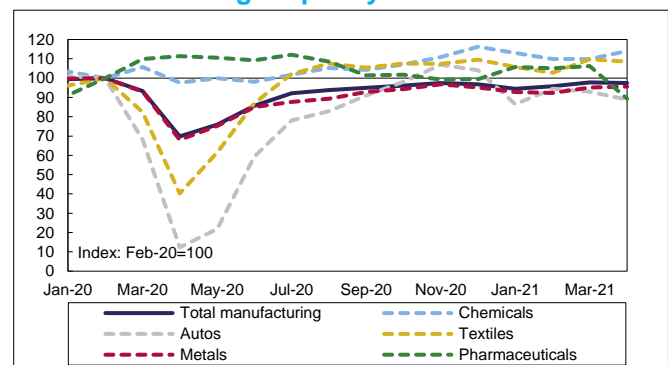
Exacerbating shortages of key inputs, including semiconductors, the ONS cited the closure of the Suez Canal as a restraint on production in April. However, another ONS survey highlighted ongoing burdens related to Brexit, stating that 37% of manufacturers who had also exported in the previous 12 months reported that additional paperwork was still a challenge when exporting in April. Indeed, the latest trade data highlighted ongoing trade diversion due to Brexit. Total goods imports from beyond the EU rose to a new series high in April, and exports to countries beyond the EU rose above the pre-Covid level of February 2020. But shipments to and from the EU remained down 7.5% and 8.2% respectively from that date. Overall, total imports of goods, excluding precious metals, rose £1.4bn (3.9%) in April, while exports on the same basis fell £0.1bn (0.6%). However, looking through the month-to-month volatility, the total trade deficit, excluding precious metals, narrowed by £4.4bn to £3.2bn in the three months to April.

UK: GDP and output by sector



Source: Refinitiv and Daiwa Capital Markets Europe Ltd.

UK: Manufacturing output by sub-sector



Source: Refinitiv and Daiwa Capital Markets Europe Ltd.

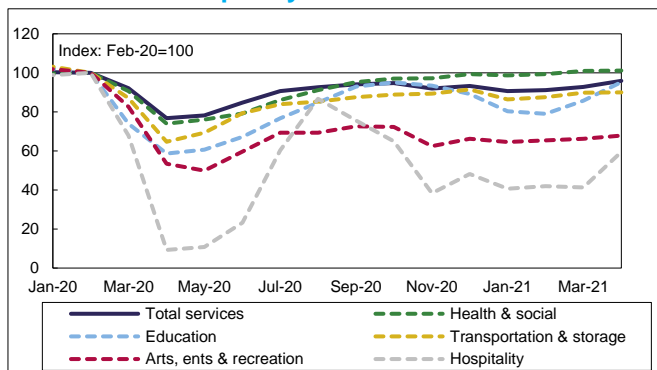
Despite pickup in pandemic, GDP on track to surpass pre-Covid level by year-end

With May having brought the reopening of indoor hospitality and certain leisure activities, and surveys pointing to another decent month for retail, growth in services should remain firm that month. Indeed, the services activity PMI rose to the highest since 2013 in May, as did the equivalent indices for construction and manufacturing output. So, GDP seems bound to have advanced significantly further. And while the recent pickup in the number of new coronavirus cases, due to the delta variant, raises the risk that, on Monday, the Government will delay the full removal of all legal restrictions on social contact to beyond the current scheduled date of 21 June, the arrival of warm summer weather has given a boost to shopping centre footfall this month. So, we maintain our forecast of GDP growth of 3.5%Q/Q in Q2, and – assuming no need to reverse the recent economic reopening over coming months – still expect the pre-pandemic level of GDP to be reached before year-end.

The week ahead in the UK

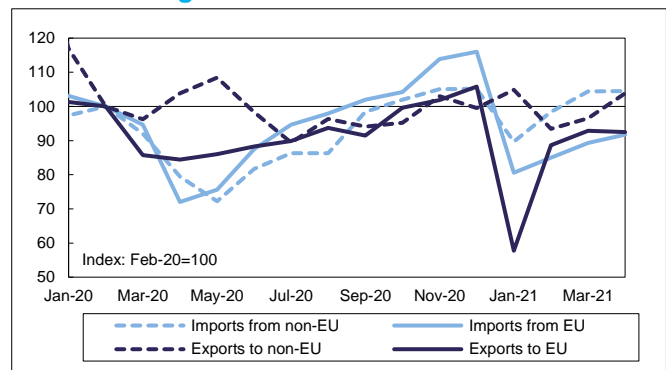
While attention at the start of the week will be on the government's decision as to whether to further relax pandemic containment measures from 21 June, subsequent days will give further clues as to the strength of GDP in May. Most notable will be the latest labour market report (Tuesday) and retail sales data (Friday), as well as inflation figures for May (on Wednesday). With the government's Job Retention Scheme still in operation, the easing in lockdown restrictions resulting in firm GDP growth in April, and further liberalisation occurring in May, we expect to see a further tightening in labour market conditions, including a solid increase in payrolls and vacancies last month. In addition, the unemployment rate is likely to nudge down further in the three months to April – marking the fourth successive decline – from 4.8% in the three months to March. And growth in average labour earnings (excluding bonuses) seem likely to rise above 5.0%Y/Y. Meanwhile, we expect the inflation data to report a rise of 0.3ppt in the headline CPI rate to a seventeen-month high of 1.8%Y/Y in May, thanks in particular to further upward pressure from energy prices, including higher domestic fuel bills. However, we also expect a pick-up in inflation of clothing and footwear as well as certain reopening services to be reflected in an increase in the core CPI measure to 1.5%Y/Y, the highest since July 2020. Finally, with the lockdown measures having eased further on 17 May, with pubs, restaurants and cafes able to serve indoors and many indoor entertainment and leisure facilities also able to reopen, retail sales are expected to have remained firm in May, following the rebound in April. We expect to see growth of around 1½%M/M in retail sales excluding petrol, pushing sales up about 15% from the pre-pandemic level in February 2020 and almost 27% above the level a year earlier.

UK: Services output by sub-sector



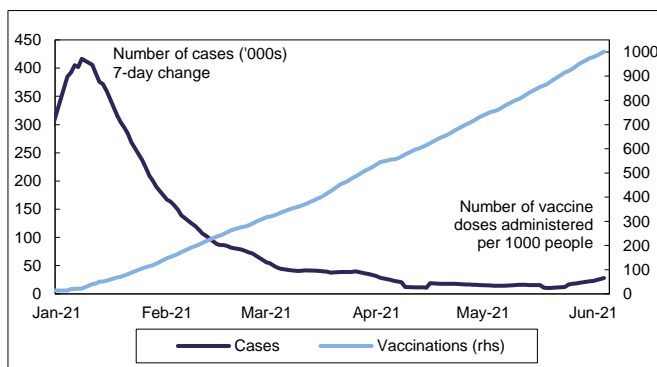
Source: Refinitiv and Daiwa Capital Markets Europe Ltd.

UK: Trade in goods



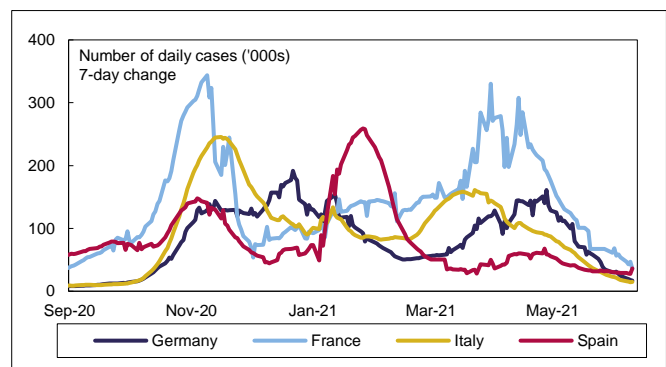
Source: Refinitiv and Daiwa Capital Markets Europe Ltd.

UK: Coronavirus cases and vaccinations



Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

Coronavirus cases in selected euro area countries



Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

Euro area

ECB hawks flag inflation concerns after dovish policy announcements

At yesterday's post-[Governing Council meeting](#) press conference, Christine Lagarde stated that the decision to extend the ECB's net PEPP purchases at a "significantly higher" pace had not been unanimous. And today brought hawkish comment from a couple of members of the Governing Council who are highly likely to have dissented from the majority view. In particular, while yesterday's updated ECB projections foresaw inflation peaking at 2.6%Y/Y in Q421 before falling back below 2.0%Y/Y in Q122, Austrian National Bank President Robert Holzmann claimed (perhaps implausibly) that "if inflation crosses 3%... that would probably mean a rethink of the strategy". And while less forthright, Dutch Governor Klaas Knot flagged the upside risks to the inflation outlook, including uncertainties related to companies' ability to absorb higher costs as well as wages as key.












Bundesbank upgrades German forecasts, but inflation to be back sub-2% by 2023

Another hawk, Bundesbank President Weidmann, flagged that German inflation might well rise above 4.0% towards year-end. But German core inflation, also excluding the impact of the VAT hike, will be little higher than 1.0%Y/Y at that point. And so, while the Bank's updated projections revised up the 2021 headline inflation outlook by 0.8ppt to 2.6%Y/Y, it foresaw inflation falling back below 2% next year to 1.8%Y/Y and a little further to 1.7%Y/Y in 2023. Core inflation (including VAT) is expected to average 1.6%Y/Y this year and edge up only slightly to 1.7%Y/Y in 2023. Meanwhile, just as yesterday's updated ECB projections revised up euro area GDP growth by 0.6ppt in both 2021 and 2022, to 4.6%Y/Y and 4.7%Y/Y respectively, the Bundesbank's updated projections, published today, pushed up the growth outlook for German GDP by 0.7ppt in each year, to 3.7%Y/Y and 5.2%Y/Y respectively, meaning that the pre-pandemic level of growth might well be reached by Q3 this year. The German GDP growth projection for 2023 was revised down 0.1ppt, however, to 1.8%Y/Y

The week ahead in the euro area









The coming week's euro area economic data calendar is relatively quiet with little in terms of new top-tier data to come. Following the mixed national industrial production data of the past week – with Germany and to a lesser extent France posting falls in IP in April, while Italy, Spain and several smaller member states saw an increase in production, despite the significant supply bottlenecks – euro area industrial production data (Monday) are likely to reveal a relatively modest increase in output in April. We expect to see a rise of roughly ½%M/M to a level about 1% below that in February 2020. On Tuesday, final May inflation data from Germany, France and Italy are due for release, followed by the publication on Thursday of final euro area CPI figures for last month. The preliminary May data revealed that German inflation on the EU harmonised measure (HICP) rose 0.3ppt to 2.4%Y/Y, the highest since October 2018. In France, the HICP rate rose 0.2ppt to 1.8%Y/Y, the highest since December 2018, while in Italy the equivalent rate rose 0.3ppt to 1.3%Y/Y, the highest since November 2018. The aggregate euro area measure rose 0.4ppt to 2.0%Y/Y in May, the highest level since October 2018. The core rate edged up 0.2ppt to a more subdued 0.9%Y/Y. Other data due to be published in the coming week include euro area April goods trade figures on Tuesday and aggregate EU new car registrations data for May on Thursday. Survey-wise, the Bank of France is due to publish its latest surveys for industrial sentiment and retail trade on Monday.

Daiwa economic forecasts

	2020	2021				2022	2020	2021	2022
	Q4	Q1	Q2	Q3	Q4	Q1			
GDP growth, %, Q/Q									
Euro area 	-0.6	-0.3	1.2	2.4	1.2	1.0	-6.7	4.5	4.6
UK 	1.3	-1.5	3.5	3.2	2.5	1.0	-9.8	6.6	6.2
Inflation									
Euro area									
Headline CPI 	-0.3	1.1	1.8	2.0	2.3	1.2	0.3	1.8	1.2
Core CPI 	0.2	1.2	0.8	1.0	1.3	0.6	0.7	1.1	1.0
UK									
Headline CPI 	0.5	0.6	1.7	1.8	2.5	2.4	0.9	1.6	2.0
Core CPI 	1.3	1.1	1.3	1.4	1.8	1.7	1.4	1.4	1.7
Interest Rates									
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.























European calendar

Today's results						
Economic data						
Country	Release	Period	Actual	Market consensus/ <i>Daiwa forecast</i>	Previous	Revised
Italy 	Unemployment rate %	Q4	10.4	10.5	9.2	10.0
Spain 	Final CPI (EU-harmonised CPI) Y/Y%	May	2.7 (2.4)	2.7 (2.4)	2.2 (2.0)	-
UK 	GDP M/M% (3M/3M)	Apr	2.3 (1.5)	2.5 (1.6)	2.1 (-1.6)	-
	Industrial production M/M% (Y/Y%)	Apr	-1.3 (27.5)	1.2 (30.5)	1.8 (3.6)	-
	Manufacturing production M/M% (Y/Y%)	Apr	-0.3 (39.7)	1.5 (42.2)	2.1 (4.8)	-
	Construction output M/M% (Y/Y%)	Apr	-2.0 (77.9)	1.0 (83.4)	5.8 (6.0)	-
	Index of services M/M% (3M/3M%)	Apr	3.4 (1.4)	2.8 (1.2)	1.9 (-2.0)	-
	Goods trade balance £bn	Apr	-10.9	-11.7	-11.7	-
Auctions						
Country	Auction	- Nothing to report -				

Source: Bloomberg 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 14 June 2021					
EMU		10.00 Industrial production M/M% (Y/Y%)	Apr	0.4 (37.4)	0.1 (10.9)
France		- Bank of France industry sentiment indicator	Apr	108	107
		- Bank of France retail trade M/M%	May	-	-7.1
Tuesday 15 June 2021					
EMU		10.00 Trade balance €bn	Apr	15.0	13.0
Germany		07.00 Final CPI (EU-harmonised CPI) Y/Y%	May	2.5 (2.4)	2.0 (2.1)
France		07.45 Final CPI (EU-harmonised CPI) Y/Y%	May	1.4 (1.8)	1.2 (1.6)
Italy		09.00 Final CPI (EU-harmonised CPI) Y/Y%	May	1.3 (1.3)	1.1 (1.0)
UK		07.00 Unemployment claimant count rate % (change '000s)	May	-	7.2 (-15.1)
		07.00 Average earnings including bonuses (excluding bonuses) 3M Y/Y%	Apr	4.9 (5.3)	4.0 (4.6)
		07.00 ILO unemployment rate 3M %	Apr	4.7	4.8
		07.00 Employment change 3M/3M, '000s	Apr	140	84
Wednesday 16 June 2021					
EMU		10.00 Labour costs Y/Y%	Q1	-	3.0
UK		07.00 CPI (core CPI) Y/Y%	May	<u>1.8 (1.5)</u>	1.5 (1.3)
		07.00 PPI input (output) prices Y/Y%	May	10.6 (4.5)	9.9 (3.9)
		09.30 House price index Y/Y%	Apr	12.2	10.2
Thursday 17 June 2021					
EMU		10.00 Final CPI (core CPI) Y/Y%	May	2.0 (0.9)	1.6 (0.7)
		07.00 EU27 new car registrations Y/Y%	May	-	218.6
Italy		09.00 Total trade balance €bn	Apr	-	5.2
Spain		08.00 Labour costs Y/Y%	Q1	-	-0.1
Friday 18 June 2021					
Germany		07.00 PPI Y/Y%	May	6.4	5.2
UK		07.00 Retail sales including auto fuel M/M% (Y/Y%)	May	1.6 (28.9)	9.2 (42.4)
		07.00 Retail sales excluding auto fuel M/M% (Y/Y%)	May	1.5 (26.9)	9.0 (37.7)

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

The coming week's key events & auctions

Country	BST	Event / Auction
Monday 14 June 2021		
EMU	 09.00	ECB's Hernández de Cos scheduled to speak about climate change
	 14.00	ECB's Schnabel scheduled to speak at event on 'Climate change, finance and green growth'
Tuesday 15 June 2021		
EMU	 11.00	ECB's Hernández de Cos scheduled to speak about financial integration
	 12.00	ECB Chief Economist Lane gives opening remarks at ECB forecasting conference
	 14.50	ECB's Panetta scheduled to speak at Bundesbank conference
UK	 11.30	Auction: £2bn of 1.25% 2051 bonds
Wednesday 16 June 2021		
Germany	 10.30	Auction: €5bn of 2031 bonds
UK	 10.00	Auction: £2.5bn of 0.625% 2035 bonds
	 13.15	BoE Governor Bailey takes part in conference on the future growth of UK-based financial services
Thursday 17 June 2021		
EMU	 -	Euro area finance ministers scheduled to meet
France	 10.55	Auction: 0% 2027 bonds
	 10.55	Auction: 0.75% 2028 bonds
	 10.55	Auction: 0.5% 2025 bonds
	 10.55	Auction: 0.5% 2029 bonds
	 10.55	Auction: 0.1% 2031 index-linked bonds
	 10.55	Auction: 0.1% 2047 index-linked bonds
	 10.55	Auction: 0.1% 2025 index-linked bonds
Spain	 09.30	Auction: 0% 2024 bonds
	 09.30	Auction: 0% 2028 bonds
	 09.30	Auction: 0.85% 2037 bonds
Friday 18 June 2021		
UK	 09.30	BoE publishes May inflation attitudes survey

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

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

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