

Euro wrap-up

Overview

- Bunds made modest losses as final inflation figures in Germany and France confirmed multi-year highs but Italian inflation was revised down and euro area exports weakened in April.
- Gilts also made modest losses as data pointed to recovery in the UK's labour market.
- Tomorrow will bring UK inflation figures for May, along with Q1 labour costs numbers from the euro area.

Chris Scicluna

+44 20 7597 8326

Daily bond market movements

Bond	Yield	Change
BKO 0 06/23	-0.681	+0.001
OBL 0 04/26	-0.607	+0.011
DBR 0 02/31	-0.233	+0.018
UKT 0 ⁷ / ₈ 01/23	0.081	+0.009
UKT 0 ¹ / ₈ 01/26	0.332	+0.018
UKT 4 ³ / ₄ 12/30	0.759	+0.019

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

Source: Bloomberg

Euro area

Euro area exports weaken in April on supply strains, but imports surge on price effects

Tallying with yesterday's underwhelming [manufacturing output](#) figures, euro area exporters had a weaker start to the second quarter, with the value of merchandise exports dropping 2.3%MM on a seasonally adjusted basis in April. While that followed upwardly revised growth of 2.8%MM in March, it left the value of exports still 0.3% below the Q1 average and 2.9% below the pre-pandemic level in February 2020. In marked contrast, growth in the value of merchandise imports remained strong, up a further 2.4%MM in April. Following growth of 6.3%MM in March, that left the value of imports 7.8% above the average in Q1 and 5.7% above the pre-pandemic level. While exports to the US, China, Japan and UK were all stronger in April – although the latter still lagged well behind those to other major markets – exports to non-euro area EU countries appear to have weakened that month, pointing to the impact of supply-chain disruption. Meanwhile, the value of imports, in particular, was boosted significantly by relative price changes. Indeed, prices of imported manufactured goods rose 1.0%MM in April, the fourth successive monthly increase of that rate or more, to be up 4.6%Y/Y. And total import producer prices rose 1.2%MM to be up 9.8%Y/Y, boosted in part by inflation of 87.0%Y/Y for goods from the mining and quarrying sector but with imported prices of manufactured items rising 4.6%Y/Y, the most in a decade

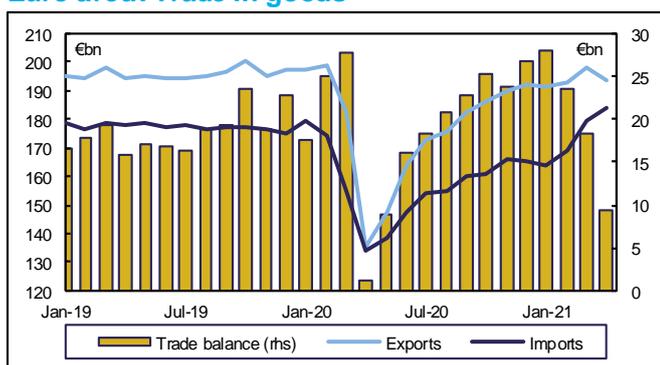
Trade surplus at 11-month low, but net exports to support GDP growth over coming quarters

With the value of imports having exceeded that of exports for the third successive month, the euro area's merchandise trade surplus on an adjusted basis narrowed by almost €9.0bn to an eleven-month low of €9.4bn. Nevertheless, notwithstanding the impact of relative price changes, and the likelihood that supply bottlenecks will weigh on exports for a while yet, we expect growth in the volume of exports to outpace that of imports over the next few quarters. Indeed, new orders of manufactured items from outside of the euro area rose for the fourth successive month in April to be 4.0% above the Q1 average and a sizeable 9.1% above the pre-pandemic level.

German and French inflation data confirms flash estimates, Italian inflation revised down

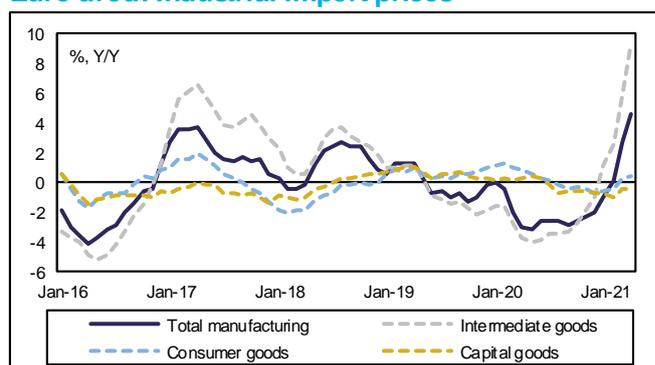
There were no surprises from today's final May inflation figures from Germany and France, although the equivalent Italian data saw a modest downside revision. In particular, as suggested by the flash estimate, Germany's headline national rate jumped 0.5ppt in May to 2.5%Y/Y, a near-decade high. And, on the EU-harmonised measure, German inflation rose 0.3ppt to 2.4%Y/Y, its highest since October 2018. The increase in part reflected stronger energy inflation, which remained boosted by temporary factors relating to the carbon emissions charge introduced at the beginning of the year as well as base effects from the low energy prices a year earlier. But there was also a further uptick in non-energy industrial goods inflation to

Euro area: Trade in goods*



*Seasonally adjusted. Source: Refinitiv and Daiwa Capital Markets Europe Ltd.

Euro area: Industrial import prices



Source: Refinitiv and Daiwa Capital Markets Europe Ltd.

its strongest since September 2018, while services inflation largely reversed the drop recorded in April. As such, core inflation (on the EU measure) also fully reversed the 0.5ppt fall recorded in April, returning back to 1.6Y/Y.

The French inflation figures also aligned with the flash estimates in May, with the EU headline measure confirmed at 1.8%Y/Y, up 0.2ppt from April, the strongest rate since December 2018. The national rate was also up 0.2ppt to 1.4%Y/Y, the firmest since February 2020. Like in Germany, the uptick largely reflected higher energy inflation, while there was also a softer pace of decline in prices of manufactured goods. But services inflation edged slightly lower on the back of a decline in prices of mobile phone services. And so, French core inflation (in the national measure) slipped back below 1%Y/Y in May.

In contrast, the final Italian figures today saw the headline EU measure revised slightly lower from the preliminary estimate to 1.2%Y/Y, up 0.2ppt from April to the firmest reading since 2018. Similar to the largest two member states, the upwards trend reflected higher energy inflation. But with non-energy industrial goods inflation moving sideways at barely above zero and services inflation having edged lower, core inflation (on the EU measure) fell 0.1ppt to 0.1%Y/Y, the lowest since October.

The day ahead in the euro area

Tomorrow will be a quiet day for economic releases in the euro area with only Q1 labour costs data scheduled.

UK

Clear evidence of recovery in UK labour market as economy reopens

With [economic activity](#) rebounding firmly with the relaxation of the most stringent pandemic containment measures affecting retail, leisure and hospitality, the UK's labour market is also starting to recover. Payrolls increased for the sixth successive month in May and by 197k, the most on the series dating back to 2014. That left them up 429k from the pandemic-era trough in November, albeit still some 553k below the pre-pandemic level. In addition, the number of job vacancies in the three months to May 2021 rose to 758k, just 53k below the level in the three months to February 2020 with the strongest quarterly increase registered in hospitality. And when looking at more high frequency data, single month vacancies and weekly online job advertisement surpassed their pre-pandemic levels. On the ILO measure, employment rose 113k in the three months to April, the most since before the pandemic. And the unemployment rate edged down 0.1ppt for the fourth successive month to 4.7%, the lowest since August.

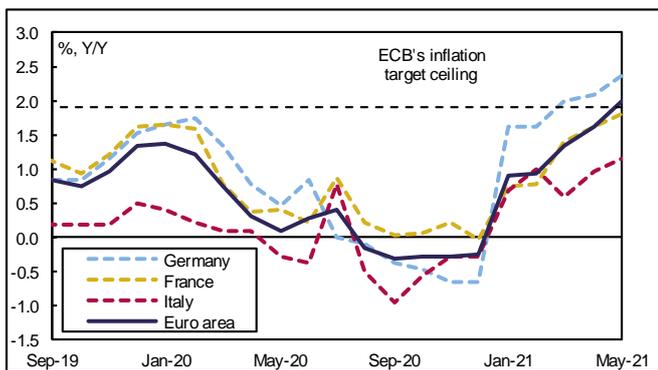
Wage growth highest since 2007, flattered by composition and base effects

Wage growth continues to rebound too, with average total pay growth up 1.3ppts in the three months to April to 5.6%Y/Y, the highest since early 2007, and 4.4%Y/Y in real terms. Excluding bonuses, pay growth over the same period rose 1.0ppt, also to 5.6%Y/Y, the highest on the series dating back more than 20 years. However, the acceleration principally reflects base effects related to the weakness a year earlier – indeed, given the plunge during the first lockdown, total pay on a single-month basis was up 8.4%Y/Y in April. It also reflects compositional effects, i.e. the relative drop in the number and proportion of lower-paid jobs, which the ONS estimates to have added about 2.5ppts to total pay growth. The drop in the share of workers on furlough – from 21.8% of the workforce at end-April 2020 (8.79mn workers) to 'just' 10% (3.5mn) in the final two weeks of April 2021 – also played a role in boosting average pay growth.

Jobs momentum to remain firm despite postponement of further economic reopening

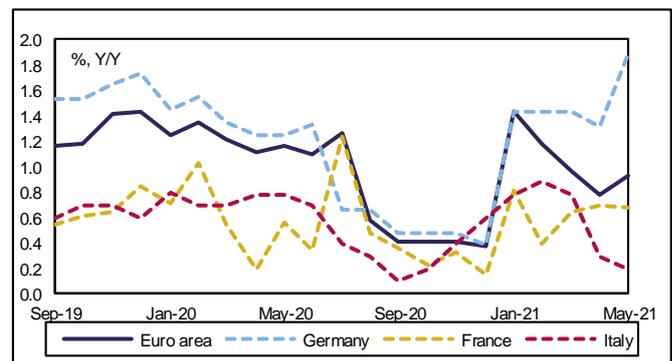
Despite yesterday's confirmation of a one-month postponement to further easing of restrictions – largely affecting large public gatherings, social distancing and continued working from home – all indicators suggest that the positive jobs momentum will be largely maintained over coming months. Indeed, the ONS's most recent bi-weekly business survey implied that the number of workers furloughed in May has now fallen to fewer than 2mn. It remains to be seen whether the redundancy rate – which has fallen back close to pre-pandemic levels – rises once again and the unemployment rate picks up once the furlough scheme comes to an end in September. But the exodus of many EU citizens over the past year or so

Euro area: Inflation in selected member states*



*EU Harmonised Index of Consumer Prices. Source: Refinitiv and Daiwa Capital Markets Europe Ltd.

Euro area: Core inflation in selected member states*



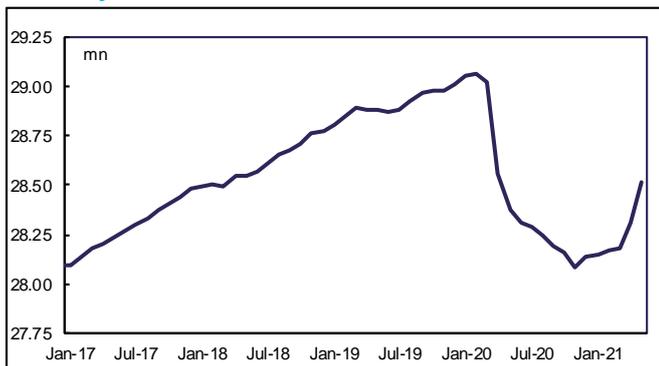
*National core CPI measures for the member states. Source: Refinitiv and Daiwa Capital Markets Europe Ltd.

suggests that many of those not retained by their current employers could be reabsorbed into the labour force relatively quickly. So, we expect the unemployment rate to remain well below the BoE's forecast pandemic-era peak of just under 5½% in Q321. Meanwhile, annual wage growth will be further boosted by base effects over the coming few months – if the level of average pay remains unchanged, the annual rate of increase will rise to 8%YY in the three months to June. At the same time, however, the extent to which compositional factors flatter pay growth will also likely diminish somewhat as employment in hospitality – which saw the greatest increase in vacancies over the past three months – rebounds. And with unit labour cost growth set to be significantly negative this year as productivity rises vigorously with the recovery in economic activity, there seems little reason for the BoE to be troubled by cost pressures emanating from the labour market, unless second-round effects emerge in wage growth in 2022 and beyond.

The day ahead in the UK

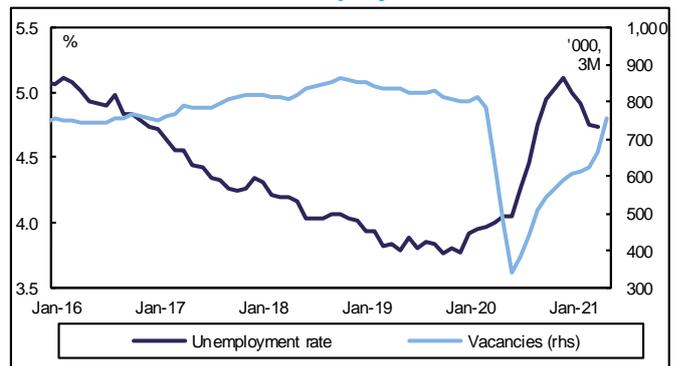
Looking ahead to tomorrow, we expect the latest UK inflation data to report a rise of 0.3ppt in the headline CPI rate in May to a seventeen-month high of 1.8%YY, due principally to further upward pressure from energy prices, including higher domestic fuel bills. However, we also expect a pick-up in inflation of clothing and footwear, while the reopening of certain services should also be reflected in an increase in the core CPI rate to 1.5%YY, which would be the highest since July 2020.

UK: Payrolls



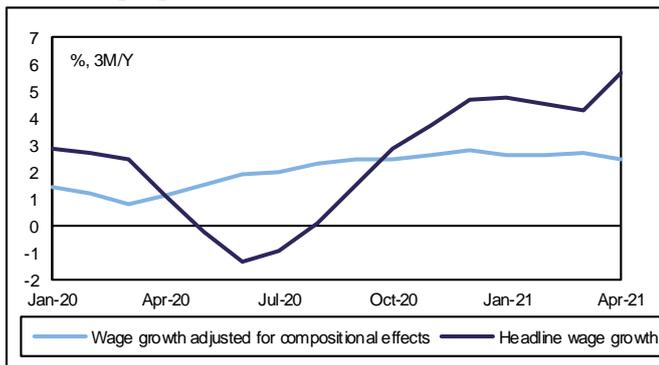
Source: ONS and Daiwa Capital Markets Europe Ltd.

UK: Vacancies and unemployment rate



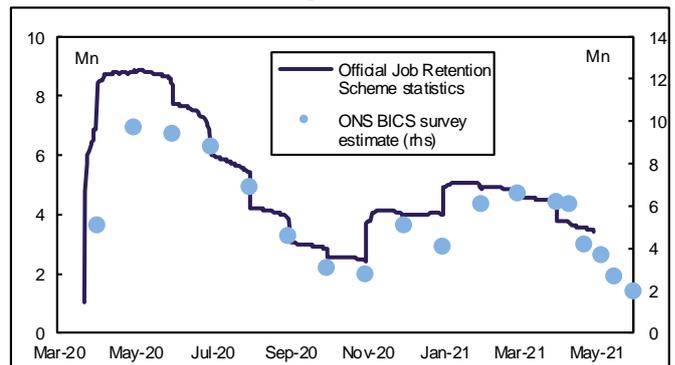
Source: ONS and Daiwa Capital Markets Europe Ltd.

UK: Wage growth



Source: ONS and Daiwa Capital Markets Europe Ltd.

UK: Workers on furlough



Source: UK Government Coronavirus Job Retention Scheme statistics, ONS 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	 Trade balance €bn	Apr	9.4	15.0	13.0	18.3
Germany	 Final CPI (EU-harmonised CPI) Y/Y%	May	2.5 (2.4)	2.5 (2.4)	2.0 (2.1)	-
France	 Final CPI (EU-harmonised CPI) Y/Y%	May	1.4 (1.8)	1.4 (1.8)	1.2 (1.6)	-
Italy	 Final CPI (EU-harmonised CPI) Y/Y%	May	1.3 (1.2)	1.3 (1.3)	1.1 (1.0)	-
UK	 Unemployment claimant count rate % (change '000s)	May	6.2 (-92.6)	-	7.2 (-15.1)	6.4 (-55.8)
	 Average earnings including bonuses (excluding bonuses) 3M Y/Y%	Apr	5.6 (5.6)	4.9 (5.3)	4.0 (4.6)	4.3 (-)
	 ILO unemployment rate 3M %	Apr	4.7	4.7	4.8	-
	 Employment change 3M/3M, '000s	Apr	113	140	84	-

Auctions

Country	Auction
Germany	 sold €4.1bn of 0% 2023 bonds at an average yield of -0.68%
UK	 sold £2.75bn of 0.125% 2028 bonds at an average yield of 0.531%
	 sold £2.0bn of 1.25% 2051 bonds at an average yield of 1.274%

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

Tomorrow's releases

Economic data

Country	BST	Release	Period	Market consensus/ <i>Daiwa forecast</i>	Previous
EMU	 10.00	Labour costs Y/Y%	Q1	-	3.0
UK	 07.00	CPI (core CPI) Y/Y%	May	1.8 (1.5)	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

Auctions and events

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

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

Access our research blog at:

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

This research report is produced by Daiwa Securities Co. Ltd., and/or its affiliates and is distributed by Daiwa Capital Markets Europe Limited. Daiwa Capital Markets Europe Limited is authorised and regulated by The Financial Conduct Authority and is a member of the London Stock Exchange and Eurex Exchange. Daiwa Capital Markets Europe Limited and its affiliates may, from time to time, to the extent permitted by law, participate or invest in other financing transactions with the issuers of the securities referred to herein (the "Securities"), perform services for or solicit business from such issuers, and/or have a position or effect transactions in the Securities or options thereof and/or may have acted as an underwriter during the past twelve months for the issuer of such securities. In addition, employees of Daiwa Capital Markets Europe Limited and its affiliates may have positions and effect transactions in such securities or options and may serve as Directors of such issuers. Daiwa Capital Markets Europe Limited may, to the extent permitted by applicable UK law and other applicable law or regulation, effect transactions in the Securities before this material is published to recipients.

This publication is intended for investors who are MiFID 2 Professional (or equivalent) Clients and should not therefore be distributed to such Retail Clients. Should you enter into investment business with Daiwa Capital Markets Europe's affiliates outside the United Kingdom, we are obliged to advise that the protection afforded by the United Kingdom regulatory system may not apply, in particular, the benefits of the Financial Services Compensation Scheme may not be available.

Daiwa Capital Markets Europe Limited has in place organisational arrangements for the prevention and avoidance of conflicts of interest. Our conflict management policy is available at <http://www.uk.daiwacm.com/about-us/corporate-governance-regulatory>. Regulatory disclosures of investment banking relationships are available at <https://daiwa3.bluematrix.com/sellside/Disclosures.action>.