Euro wrap-up

Overview

- Gilts made losses as the BoE left Bank Rate unchanged and repeated the case for 'gradual and careful' easing ahead amid still elevated pay growth.
- Despite accelerated momentum in euro area construction activity at the start of the year, Bunds made modest gains as German producer prices signalled a continued absence of factory pipeline pressures.
- Friday will bring survey results for euro area and UK consumer confidence, as well as French and UK business sentiment.

Economic Research Team
+44 20 7597 8326

Daily bond market movements

Bond	Yield	Change
BKO 2.2 03/27	2.167	-0.020
OBL 2.4 04/30	2.437	-0.026
DBR 2½ 02/35	2.782	-0.019
UKT 3¾ 03/27	4.230	+0.035
UKT 4⅜ 03/30	4.308	+0.022
UKT 4½ 03/35	4.645	+0.011

*Change from close as at 4:45pm GMT.
Source: Bloomberg

UK

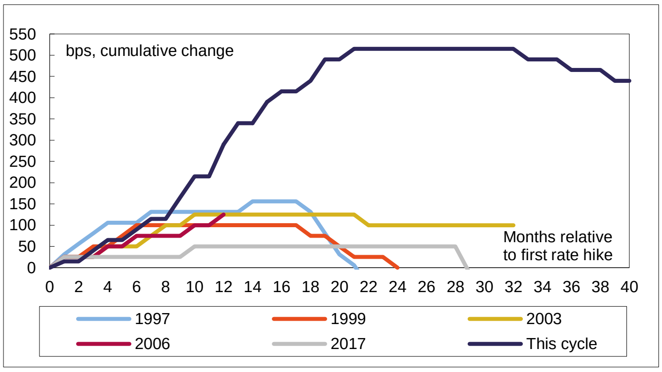
MPC votes 8-1 to leave Bank Rate unchanged, repeating case for 'gradual & careful' easing ahead

As expected, the BoE's MPC left Bank Rate unchanged at 4.50%. Eight members voted in favour of the decision, with only the uber-dove external member Swati Dhingra preferring a further cut of 25bps. So, external member Catherine Mann, who had voted for a 50bps cut in February but had since then sounded more equivocal about the appropriate path for policy, supported the status quo. Perhaps inevitably, the MPC's statement maintained its forward guidance that 'a gradual and careful approach to the further withdrawal of monetary policy restraint is appropriate'. We continue to interpret that to mean one rate cut of 25bps per quarter for as long as the BoE's forecasts remain on track. So, that path for Bank Rate remains our baseline forecast. But the MPC inevitably also flagged heightened uncertainty related, among other things, to US tariffs, geopolitics and associated market volatility. And certainly, the Committee could well be pushed off that one-cut-per-quarter path – in either direction – as events, including the announcement of US 'reciprocal tariffs' and retaliatory measures unfold and impact economic growth and inflation.

Still elevated pay growth remains consistent with BoE's gradual approach to future rate cuts

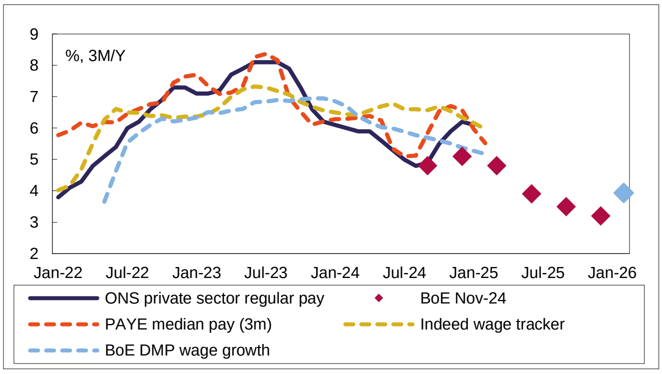
Today's labour market data will likely have reinforced the majority view on the MPC that, for the time being, the pace of easing should remain no faster than one cut per quarter. Having increased to a 13-month high in December, total wage growth (including bonuses) slowed only slightly in the three months to January, by 0.3ppt to 5.8%3M/Y. A moderation in total private sector pay (down ½ppt to 5.9%3M/Y) was partially offset by a rise in public sector pay growth to a nine-month high (5.3%3M/Y). More importantly, excluding bonuses, the BoE's preferred measure of private sector regular pay grew 6.1%3M/Y in January, down just 0.1ppt from December's 12-month high and the BoE's forecast for end-Q125. And regular pay growth was unchanged in services (6.0%3M/Y), with rates in retail and hospitality still particularly strong. But after accelerating at the end of last year, there was a welcome moderation in private regular pay, for which the three-month annualised growth rate slowed a chunky 1.6ppts to 6.1%3M/3M annualised. This remains more than double the average in the two decades before the pandemic and inconsistent with achieving the 2% inflation target over the medium term. But HMRC's figure for median pay also suggested a further moderation in February, with growth slowing to a six-month low of 5.5%3M/Y. The Indeed wage tracker for that month (5.7%Y/Y) was also the softest for almost three years. And, notwithstanding the sizeable increase in the National Living Wage due in April, survey indicators – including the BoE's own DMP survey – still suggest that pay growth will moderate over the coming year – a process that should facilitate further monetary easing.

UK: BoE Bank Rate cycles



Source: Macrobond and Daiwa Capital Markets Europe Ltd.

UK: Measures of pay growth

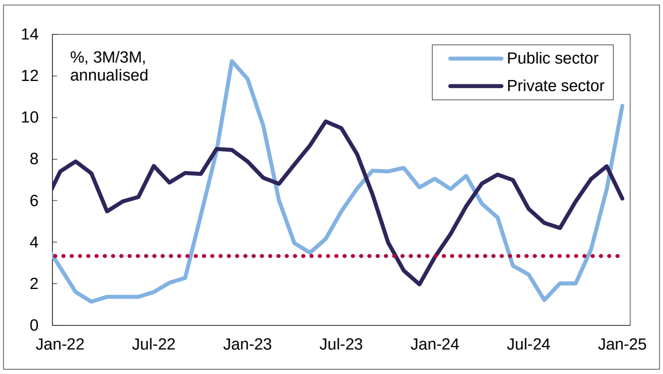


Source: Macrobond, BoE and Daiwa Capital Markets Europe Ltd.

Employment growth surprisingly firm, but declining vacancies and surveys point to weaker demand

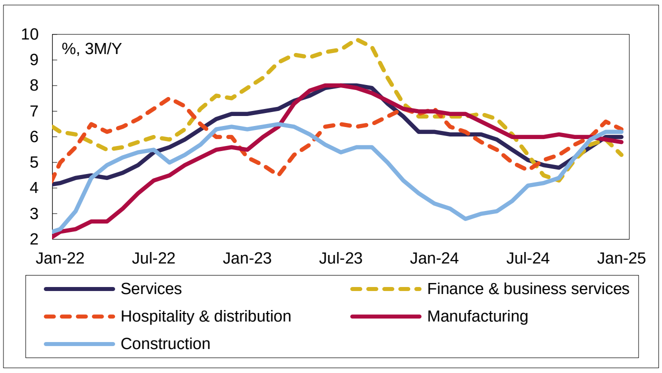
While the number of redundancies rose to a 12-month high at the end of 2024 and surveys have signalled firms' desire to cut headcount since the start of the year, the job market has remained resilient. Indeed, the LFS measure of employment rose a larger-than-expected 144k in the three months to January, reflecting the biggest increase in full-time employees (200k) since late-2023. This left total employment up more than 600k (1.8%) compared with a year earlier. Of course, the reliability of these data remains questionable due to the low survey response rate. And while the number of payrolled employees unexpectedly rose in February (20.5k) by the most in four months, much of the initial rise in January was revised away to leave it up a more modest 67k (0.2%) compared with a year earlier. So, broadly in line with the BoE's projection, the LFS unemployment rate held steady at 4.4% in the three months to January for a third successive month, nevertheless 0.8ppt above the trough in mid-2022. But with the number of vacancies resuming its downtrend of recent years, the ratio of the number of unemployed people per job vacancy remained comfortably below levels ahead of the pandemic, supporting the view that labour market tightness continues gradually to ease. The BoE considers the current VU ratio to be broadly consistent with a labour market that is in balance. However, given heightened economic uncertainties and the squeeze on profit margins from rising labour costs – which will intensify after the increase in employer National Insurance Contributions from April – we continue to expect labour market slack to build over coming quarters, which should help further to restrain underlying pay growth.

UK: Private & public regular pay growth*



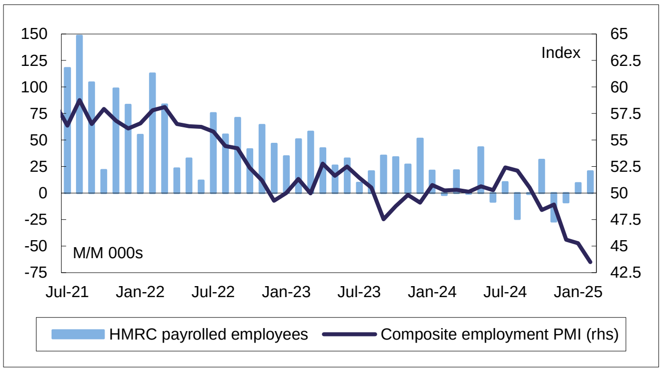
**Dotted red line represents pre-pandemic 20-year average.*
Source: Macrobond and Daiwa Capital Markets Europe Ltd.

UK: Private regular growth



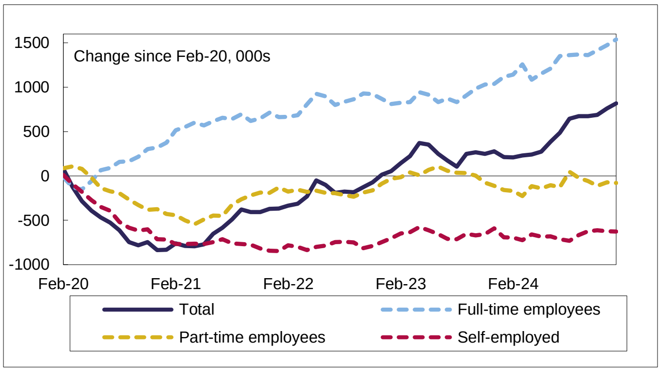
Source: Macrobond and Daiwa Capital Markets Europe Ltd.

UK: Payrolled employees & employment PMI



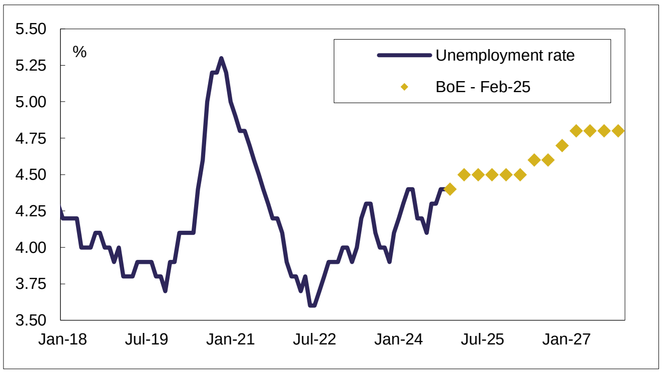
Source: Macrobond, S&P Global and Daiwa Capital Markets Europe Ltd.

UK: Change in employment



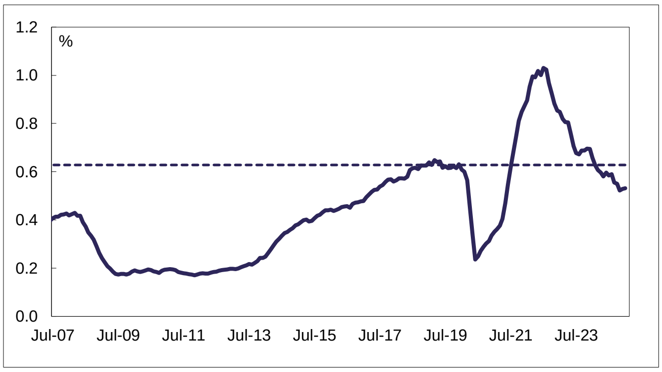
Source: Macrobond and Daiwa Capital Markets Europe Ltd.

UK: Unemployment rate



Source: Macrobond, BoE and Daiwa Capital Markets Europe Ltd.

UK: Vacancy to unemployment ratio*



**Dashed line represents 2019 average.*
Source: Macrobond and Daiwa Capital Markets Europe Ltd.

The day ahead in the UK

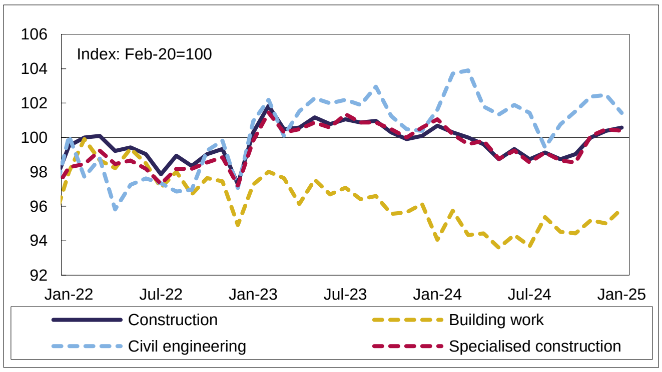
Ahead of next week's flash March PMIs, tomorrow's CBI industrial trends survey is expected to illustrate the ongoing challenges facing manufacturers amid declining new orders. The GfK consumer survey will likely flag subdued confidence in March, with an ongoing preference among households to save than spend. Meanwhile, public finance statistics for February will provide the last update ahead of the Chancellor's Spring Statement (March 26). January's budget surplus (£15.4bn) fell short of the OBR's October forecast, but February's data might well see that shortfall narrow as more receipts from self-assessments filter through.

Euro area

Construction activity expands for a fourth consecutive month for the first time since 2020

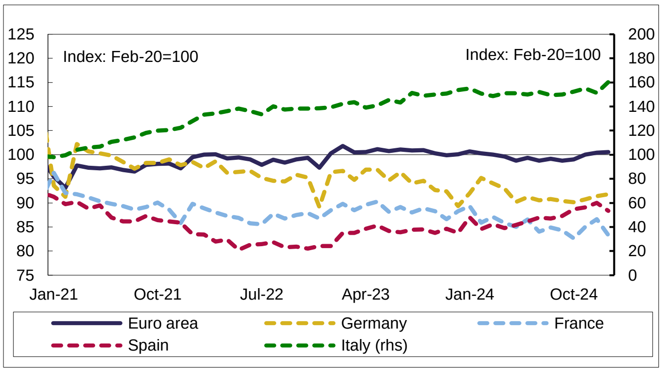
Despite marked declines in France (-3.9%M/M) and Spain (-1.9%M/M), construction activity in the euro area unexpectedly increased at the start of the year. Indeed, growth in Germany (0.4%M/M) and a significant boost from Italy (5.9%M/M) saw aggregate construction output rise a modest 0.2%M/M in January. Following revisions to output in recent months, this marked a fourth successive monthly expansion in the sector for the first time since 2020. While this left the level little changed compared with a year earlier, it was also 0.8% above the Q4 average suggesting the likelihood that construction will make a positive contribution to GDP growth in Q1. And growth on a three-month basis accelerated by 0.5ppt to a 21-month high of 1.4%3M/3M, suggesting accelerated momentum at the start of the year. The expansion tallied with the positive signals from the construction PMIs and Commission sentiment indicators in January, and has been supported not least by the ECB's withdrawal of monetary policy restrictiveness. Certainly, developments in house prices – as evident in preliminary Q4 estimates from France and Spain – point to firmer fundamentals in the residential property market which, alongside favourable affordability indicators, should be conducive of an ongoing recovery in mortgage demand. Like-wise, while still subdued, German and French residential building permits have lifted slightly from their recent lows to signal a further pickup in housebuilding ahead, having risen 0.9%M/M to a 13-month high in January. And while civil engineering work declined 1.0%M/M in January, the Commission survey component for new civil engineering orders rose to the highest since February 2020. Certainly, we assume that some of the weakening in the construction PMIs in February will prove temporary, as long as the euro area economy avoids major new external shocks.

Euro area: Construction output by sector



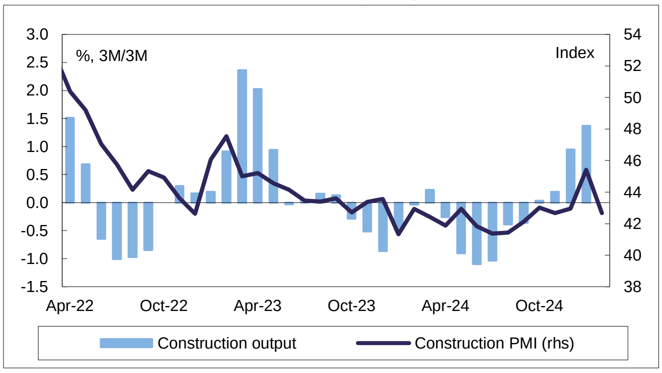
Source: Macrobond and Daiwa Capital Markets Europe Ltd.

Euro area: Construction output by member state



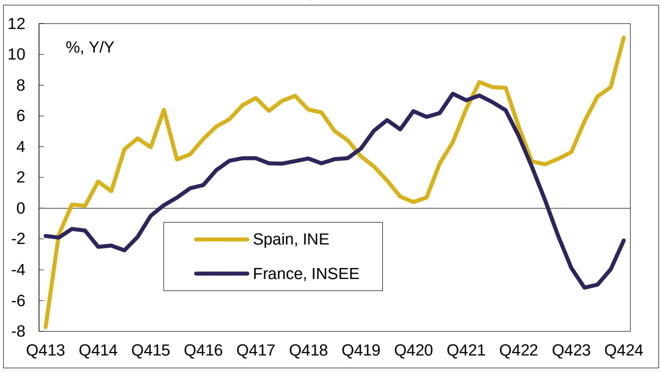
Source: Macrobond and Daiwa Capital Markets Europe Ltd.

Euro area: Construction output growth & PMI



Source: Macrobond, S&P Global and Daiwa Capital Markets Europe Ltd.

Euro area: House price growth*



**Existing housing stock only.*
Source: Macrobond and Daiwa Capital Markets Europe Ltd.

The day ahead in the euro area

Like in the UK, tomorrow will bring an update on consumer confidence in the euro area and business sentiment in France in March. Despite widespread dismay at US foreign policy, more constructive policymaking in Europe, and in particular Germany, might well provide support to the Commission's euro area consumer confidence indicator, which rose to a four-month high in February. Meanwhile, having also risen in February to the highest level since November, the latest INSEE business survey might point to a further modest improvement in business conditions, perhaps taking support from the prospect of an eventual increase in military spending across the region. In this respect, Germany's upper house (Bundesrat) is due to vote and likely ratify the government's bill to amend the debt brake to allow higher spending on military and infrastructure.

Today's results

Economic data

Country	Release	Period	**Actual**	Market consensus/ *Daiwa forecast*	Previous	Revised
Euro area	Construction output M/M% (Y/Y%)	Jan	**0.2 (0.0)**	*-0.7 (-1.4)*	0.0 (-0.1)	0.4 (0.8)
Germany	PPI Y/Y%	Feb	**0.7**	1.0	0.5	-
UK	BoE Bank Rate %	Mar	**4.50**	*4.50*	4.50	-
	Average wages (excluding bonuses) 3M/Y%	Jan	**5.8 (5.9)**	5.8 (5.9)	6.0 (5.9)	6.1 (-)
	Private sector regular wages 3M/Y%	Jan	**6.1**	6.2	6.2	-
	Unemployment rate 3M%	Jan	**4.4**	4.4	4.4	-
	Employment 3M/3M change 000s	Jan	**144**	91	107	-
	Payrolled employees M/M change 000s	Feb	**21**	-21	21	9
	Claimant count rate % (change 000s)	Feb	**4.7 (44.2)**	-	4.6 (22.0)	4.5 (2.8)

Auctions

Country	Auction
France	sold €3.497bn of 2.4% 2028 bonds at an average yield of 2.59%
	sold €3.3bn of 2.75% 2030 bonds at an average yield of 2.8%
	sold €3.481bn of 0% 2032 bonds at an average yield of 3.1%
	sold €3.216bn of 3% 2033 bonds at an average yield of 3.23%
	sold €415m of 0.6% 2034 inflation-linked bonds at an average yield of 1.2%
	sold €781m of 0.1% 2036 inflation-linked bonds at an average yield of 1.45%
	sold €208m of 1.8% 2040 inflation-linked bonds at an average yield of 1.48%
	sold €360m of 0.1% 2053 inflation-linked bonds at an average yield of 1.57%
Spain	sold €1.699bn of 0.5% 2030 bonds at an average yield of 2.757%
	sold €3.189bn of 3.15% 2035 bonds at an average yield of 3.382%
	sold €1.587bn of 3.45% 2043 bonds at an average yield of 3.9%

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

Tomorrow's releases

Economic data

Country	GMT	Release	Period	Market consensus/ *Daiwa forecast*	Previous
Euro area	09.00	Current account balance €bn	Jan	-	38.4
	15.00	Preliminary Commission consumer confidence indicator	Mar	-13.0	-13.6
France	07.45	INSEE business (manufacturing) confidence indicator	Mar	96 (97)	96 (97)
	07.45	Final wages Q/Q%	Q4	*0.4*	0.4
	-	BdF retail sales Y/Y%	Feb	-	-0.7
UK	00.01	GfK consumer confidence indicator	Mar	-20	-20
	07.00	Public sector net borrowing £bn	Feb	-	-15.4
	11.00	CBI industrial trends survey – total orders (selling prices) balance %	Mar	-30 (20)	-28 (19)

Auctions and events

- Nothing scheduled -

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

Access our research blog at:
https://www.uk.daiwacm.com/ficc-research/recent-blogs