

# Euro wrap-up

## Overview

- Gilts made losses after UK inflation data surprised to the upside.
- Bunds followed the global trend lower on a quiet day for euro area economic news.
- Thursday will bring various May business surveys, including the flash PMIs, German ifo and French INSEE sentiment indices, along with the account of the ECB's April policy-setting meeting.

**Emily Nicol**  
+44 20 7597 8331

**Edward Maling**  
+44 20 7597 8030

### Daily bond market movements

Bond	Yield	Change
BKO 1.7 06/27	1.858	+0.023
OBL 2.4 04/30	2.181	+0.032
DBR 2½ 02/35	2.638	+0.034
UKT 3% 03/27	4.066	+0.034
UKT 4% 03/30	4.229	+0.039
UKT 4½ 03/35	4.747	+0.047

\*Change from close as at 4.00pm BST.  
Source: Bloomberg

## UK

### UK inflation surprises to the upside in April, with the headline rate up to 15-month high

The upside surprise in today's UK inflation figures underscored the case for the BoE to continue to take a 'careful and gradual' approach to easing monetary policy. Certainly, it reduces somewhat the probability that the MPC will next cut rates as soon as August. But much will depend on how inflation and the labour market further evolve over coming months. For the time being, we maintain our view that rates will next be cut in August, although we concede that decision will be highly data dependent and finely balanced. Indeed, while the headline CPI rate was widely expected to jump in April, the 0.9ppt rise to a 15-month high of 3.5%Y/Y was a touch larger than the BoE's May MPR projection (3.4%Y/Y) and above the Bloomberg survey consensus and our own forecast (3.3%Y/Y). Due to the scheduled increases in the household energy price cap and water tariffs, the housing, water and fuels component jumped in April by 6ppts to 7.8%Y/Y, the highest since June 2023, accounting for the largest chunk of the monthly rise in the headline CPI rate. In addition, food inflation rose to a 12-month high (4.0%Y/Y). But most importantly perhaps, services inflation was significantly stronger than expected, rising 0.7ppt to 5.4%Y/Y, an 8-month high. So, while non-energy industrial goods inflation remained steady at a subdued 1.1%Y/Y amid an absence of pressures in a range of items including clothing, furniture and household appliances, core inflation jumped 0.4ppt to 3.8%Y/Y, the most in a year.

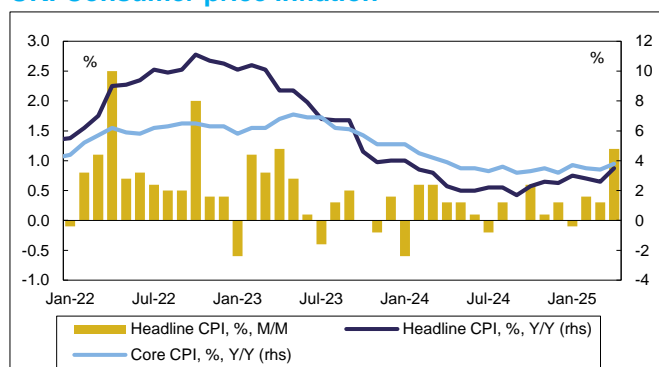
### Surge in services inflation exaggerated by timing of Easter

While annual repricing of certain often-indexed services items added some upside, the detail suggests that – as in the [euro area](#) – base effects around the timing of Easter this year played a significant role in pushing services inflation higher in April. Despite the further step down in oil prices early in the month, airfares jumped a whopping 27.4%M/M – the most in any March or April since 2011 – to push the respective annual rate up 19ppts to a 21-month high of 16.2%Y/Y. Package holidays (5.4%Y/Y) similarly added 0.1ppt to the rise in inflation while the rise in Vehicle Excise Duty added a little more than 0.2ppt. But other services components including hospitality and insurance were again better behaved last month. As such, a measure of underlying services inflation closely watched by the BoE – which excludes indexed and other volatile items including holiday-related components – eased in April, by 0.1ppt to 4.3%Y/Y, still a touch above the low in January but almost one percentage point below the average in 2024 and more than 3ppts below the peak in early 2023.

### Inflation set to peak in the autumn before returning to target in 2026

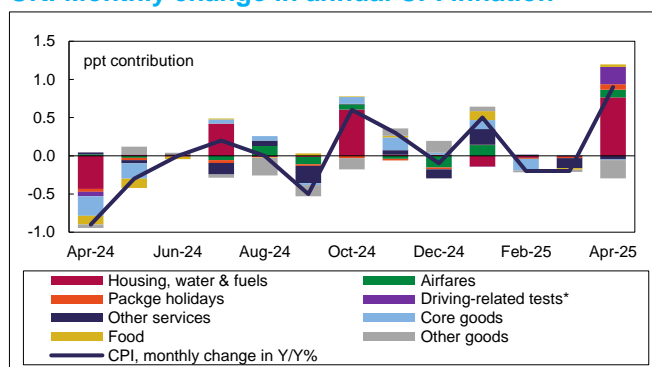
Looking ahead, services inflation should fall in May, back to around 5%Y/Y, as airfares and package holiday prices normalise. And core goods inflation should remain relatively lacklustre at just above 1%Y/Y. Moreover, on 27 May Ofgem will

### UK: Consumer price inflation



Source: Macrobond and Daiwa Capital Markets Europe Ltd.

### UK: Monthly change in annual CPI inflation

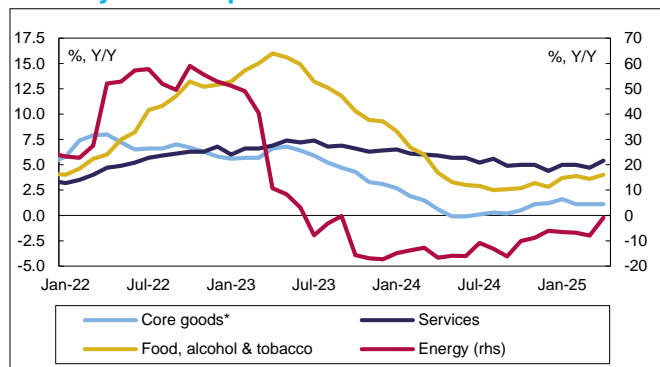


\*Including vehicle excise duty.

Source: Macrobond and Daiwa Capital Markets Europe Ltd.

likely announce a significant cut in the household energy price cap, perhaps by about 7%. But with food inflation set to rise further and the energy component to be subject to a less favourable base effect, headline inflation will likely move sideways around 3½%Y/Y over coming months, before peaking at about 3.7%Y/Y in September in line with the BoE's projection. The prospect of that forthcoming peak might persuade a majority on the MPC not to support a cut in August. However, assuming that [wage growth](#) continues to moderate in line with the loosening labour market, we still expect inflation to fall back below 3%Y/Y at the start of 2026 and be back at the 2%Y/Y target sometime in 2026. Such an outlook would remain consistent with the continued gradual removal of restrictiveness, broadly in line with cuts of 25bps a quarter. So, for now at least, we maintain our view that the MPC will keep Bank Rate on hold at its next policy meeting in June before cutting by 25bps to 4.00% in August when it will be presented with an updated set of macroeconomic projections.

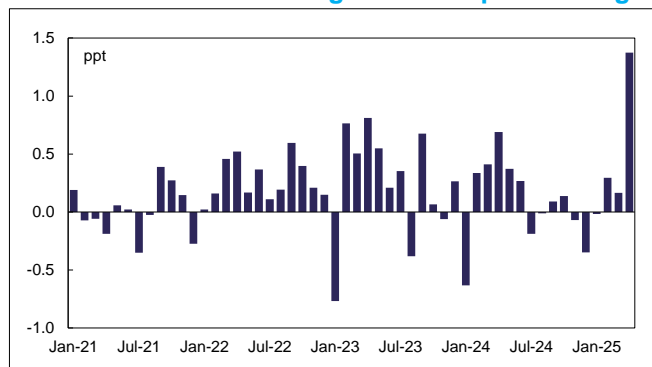
### UK: Key CPI components



\*Non-energy industrial goods.

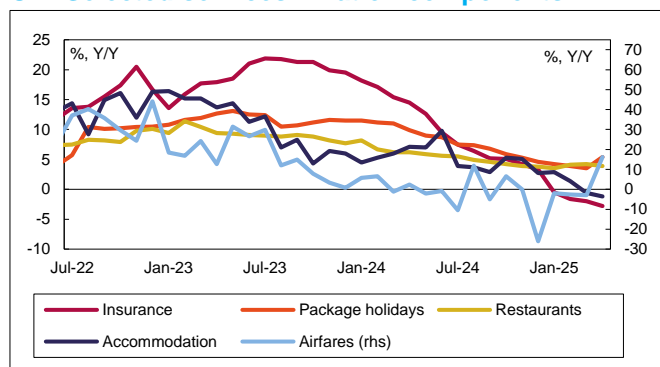
Source: Macrobond and Daiwa Capital Markets Europe Ltd.

### UK: Deviation from average services price change\*



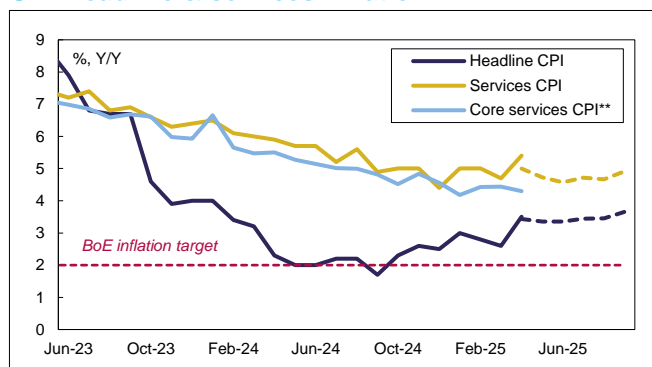
\*Monthly change in prices compared with the average for the month in the decade before the pandemic. Source: Macrobond and Daiwa Capital Markets Europe Ltd.

### UK: Selected services inflation components



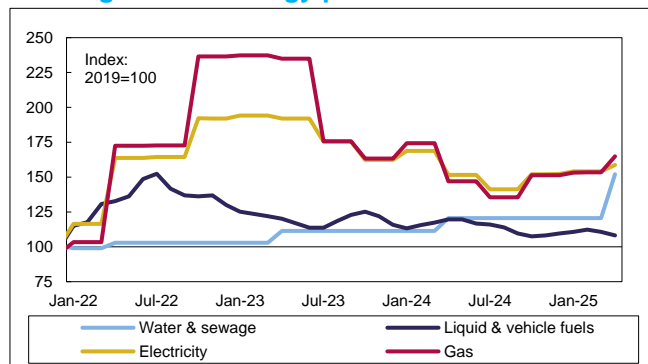
Source: Macrobond and Daiwa Capital Markets Europe Ltd.

### UK: Headline & services inflation\*



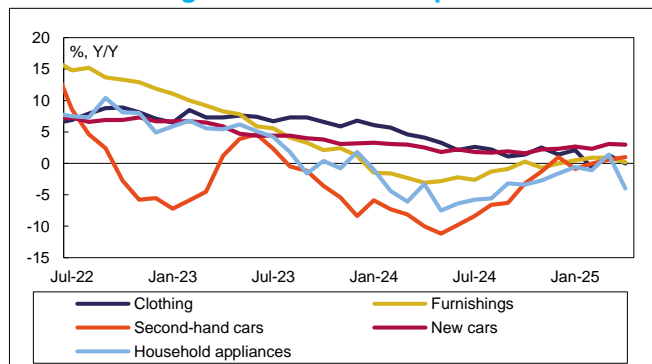
\*Dashed lines are BoE projection from May-25 MPR. \*\*Services excluding indexed and volatile components, rents and foreign holidays Source: Macrobond and Daiwa Capital Markets Europe Ltd.

### UK: Regulated & energy price levels



Source: Macrobond and Daiwa Capital Markets Europe Ltd.

### UK: Selected goods inflation components



Source: Macrobond and Daiwa Capital Markets Europe Ltd.





## The day ahead in the UK

The main UK economic data focus tomorrow will be the May flash PMIs, which will provide an update on business conditions in May. Indeed, in April, the composite output PMI posted its sharpest deterioration (down 3pts) for almost-three years, falling to 48.5 to signal contraction for the first time in 18 months. That weakness was led by services, with the activity index down 3.5pts to 49.0. But manufacturing output also remained weak, while the new export indices for both sectors deteriorated to their weakest levels outside of the pandemic and financial crisis. Given the new trade agreement with the US this month, we expect some improvement in sentiment, although the PMIs will likely still likely point to a slight contraction. Of course, the PMIs have proved to be a poor proxy for predicting GDP growth in recent quarters. But that weakness in the PMIs in May would be consistent with our forecast for a modest contraction in economic output in Q2 (-0.1%Q/Q). The CBI's industrial trends survey will also provide a cross-check on the situation for manufacturing firms in May. But after the upside surprise in April's CPI figures, policymakers will also pay attention to the input and output price PMIs, which increased to the highest levels in 26 and 23 months respectively last month. Meanwhile, April's public finance statistics will provide an update on public sector borrowing at the start of the financial year. Aside from the economic data, hawkish BoE Chief Economist Pill is among a number of Bank speakers on Thursday. As with his speech on Tuesday, his comments will likely seek to justify his vote in May for a 'pause' in the withdrawal of monetary policy restrictiveness.

## The day ahead in the euro area















Thursday's resumption to the euro area data dataflow will also be dominated by May's business surveys, with the flash euro area PMIs, and German ifo and French INSEE business confidence indices all due for release. Notwithstanding the improvement in yesterday's flash consumer confidence index, given little progress in the EU-US trade negotiations, we expect only a modest clawback following the fall in April, to be consistent with broadly stagnating private sector activity amid weak demand. In particular, the euro area composite output PMI is expected to edge up 0.2pt to 50.6. Meanwhile, Germany's ifo business climate indicator may post a fifth consecutive monthly increase, extending an upwards trend that started from last December's 15-year low. The monetary policy account of April's Governing Council meeting (also due tomorrow) is expected to demonstrate that the fresh shocks from US trade policies and deterioration in sentiment motivated the ECB's decision to keep loosening policy in April, particularly as concerns about the sustainability of the disinflation process continued to subside. And we expect May's business surveys to still be compatible with an additional cut in June.

# European calendar








Today's results						
Economic data						
Country	Release	Period	Actual	Market consensus/ <i>Daiwa forecast</i>	Previous	Revised
UK	 Headline (core) CPI Y/Y%	Apr	<b>3.5 (3.8)</b>	<u>3.3 (3.5)</u>	2.6 (3.4)	-
	 House price index Y/Y%	Mar	<b>6.4</b>	-	5.4	5.5
Auctions						
Country	Auction					
Germany	 sold €3.052bn of 2.5% 2035 bonds at an average yield of 2.66%					
UK	 sold £4.25bn of 4% 2031 bonds at an average yield of 4.401%					

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

**Tomorrow's releases**
**Economic data**

Country	BST	Release	Period	Market consensus/ <i>Daiwa forecast</i>	Previous
Euro area		09.00 Preliminary manufacturing (services) PMI	May	49.2 (50.5)	49.0 (50.1)
		09.00 Preliminary composite PMI	May	50.6	50.4
Germany		08.30 Preliminary manufacturing (services) PMI	May	48.8 (49.5)	48.4 (49.0)
		08.30 Preliminary composite PMI	May	50.3	50.1
		09.00 ifo business climate indicator	May	87.3	86.9
		09.00 ifo current assessment (expectations) indicator	May	86.6 (88.0)	86.4 (87.4)
France		07.45 INSEE business (manufacturing) confidence indicator	May	97 (99)	96 (99)
		08.15 Preliminary manufacturing (services) PMI	May	48.9 (47.7)	48.7 (47.3)
		08.15 Preliminary composite PMI	May	48.1	47.8
	-	BdF retail sales Y/Y%	Apr	-	-0.8
UK		07.00 Public sector net borrowing £bn	Apr	17.9	16.4
		09.30 Preliminary manufacturing (services) PMI	May	46.1 (50.0)	45.4 (49.0)
		09.30 Preliminary composite PMI	May	49.3	48.5
		11.00 CBI industrial trends survey – total orders (selling prices) balance %	May	-24 (22)	-26 (23)
		11.00 CBI industrial trends survey – business optimism balance %	May	-	-33

**Auctions and events**

Euro area		12.30 ECB to publish monetary policy account of April 16-17 Governing Council meeting
France		09.50 Auction: to sell up to €12.5bn of 2.4% 2028, 2.7% 2031 & 0% 2032 bonds
		10.50 Auction: to sell up to €2bn of 0.1% 2031, 3.15% 2032, 1.8% 2040 & 0.1% 2053 inflation-linked bonds
Spain		09.30 Auction: to sell 5.15% 2028, 3.1% 2031 & 1% 2042 bonds
UK		11.50 BoE Deputy Governor Breeden participates in panel on "Climate liquidity crisis: the rising financial risks of climate change"
		12.00 BoE MPC External Member Dhingra participates in panel titled "Made in the UK: trade & productivity in British firms 2005-22"
		13.30 BoE Chief Economist Pill gives speech on "Monetary policy and structural tectonic shifts" at OeNB conference, Vienna

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 ("DCME"). DCME is authorised and regulated by The Financial Conduct Authority and is a member of the London Stock Exchange. DCME 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 derivatives 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 DCME and its affiliates may have positions and effect transactions in such the Securities or derivatives or options thereof and may serve as Directors of such issuers. DCME 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 only for investors who are professional clients as defined in MiFID II and should not be distributed to retail clients as defined in MiFID II. Should you enter into investment business with DCME'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.

DCME 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.blumatrix.com/sellside/Disclosures.action>.

**Explanatory Document of Unregistered Credit Ratings**

This report may use credit ratings assigned by rating agencies that are not registered with Japan's Financial Services Agency pursuant to Article 66, Paragraph 27 of the Financial Instruments and Exchange Act. Please review the relevant disclaimer regarding credit ratings issued by such agencies at: [https://drp.daiwa.co.jp/rp-daiwa/direct/reportDisclaimer/credit\\_ratings.pdf](https://drp.daiwa.co.jp/rp-daiwa/direct/reportDisclaimer/credit_ratings.pdf). If you need more information on this matter, please contact the Research Production Department of Daiwa Securities.

**IMPORTANT**

This report is provided as a reference for making investment decisions and is not intended to be a solicitation for investment. Investment decisions should be made at your own discretion and risk. Content herein is based on information available at the time the report was prepared and may be amended or otherwise changed in the future without notice. We make no representations as to the accuracy or completeness. Daiwa Capital Markets Europe Limited retains all rights related to the content of this report, which may not be redistributed or otherwise transmitted without prior consent.