

Euro wrap-up

Overview

- Following yesterday evening's late UST rally, Bunds made gains as the ifo and INSEE surveys further flagged the risks of contractions in German and French GDP this quarter.
- While UK public borrowing exceeded expectations in April, Gilts also made gains as British retail sales fell further than expected that month.
- The coming week will bring flash estimates of inflation in May from the largest euro area member states and the European Commission's economic sentiment survey.

Economic Research Team

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Daily bond market movements

Bond	Yield	Change
BKO 2½ 06/28	2.638	-0.043
OBL 2½ 04/31	2.747	-0.055
DBR 2.9 02/36	3.036	-0.061
UKT 4¾ 03/28	4.326	-0.044
UKT 4¾ 03/31	4.462	-0.057
UKT 4¾ 10/35	4.896	-0.069

*Change from close as at 5.00pm BST.

Source: Bloomberg

Euro area

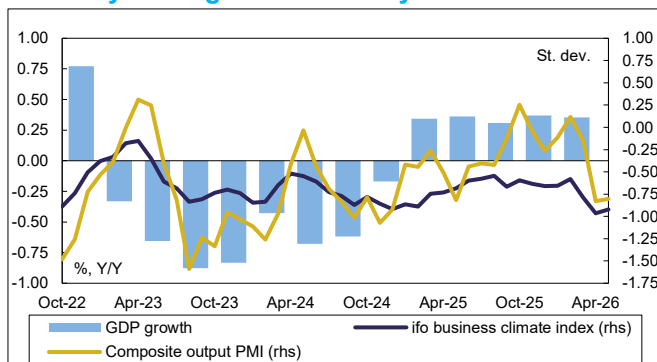
Despite improvement in May, ifo survey adds to evidence that German GDP is contracting in Q2

Today's ifo survey results for May largely validated the findings of yesterday's flash German [PMIs](#), which suggested that activity is contracting albeit slightly less marked than in April. Having fallen sharply over the two prior months, the headline business climate index edged up 0.4pt in May to 84.9, still nevertheless the second-worst reading since the Covid outbreak of 2020. Current conditions were judged to have improved slightly and were even considered somewhat more favourable than at the end of last year. But April aside, expectations for the coming six months have not been more downbeat since 2023. And the survey measures of current conditions and expectations alike remained well below their respective long-run averages. Broadly consistent with the flash PMIs and reports of precautionary frontloading of production to try to dodge future supply disruption, the ifo survey reported a second successive improvement in current conditions in German manufacturing to the best in almost two years. But with new orders falling, expectations in the sector worsened to a 16-month low. Perhaps more so than the PMIs, the ifo survey suggested that conditions in services improved in May, with the institute suggesting that logistics and tourism in particular were not as alarming as in April. However, the business climate in services was still considered the worst in 3½ years bar last month. In addition, the respective index for construction was the worst in more than a year. And in retail, current conditions were considered the worst since the lockdowns of early 2021.

German consumer confidence improves but domestic & external demand likely to dip this quarter

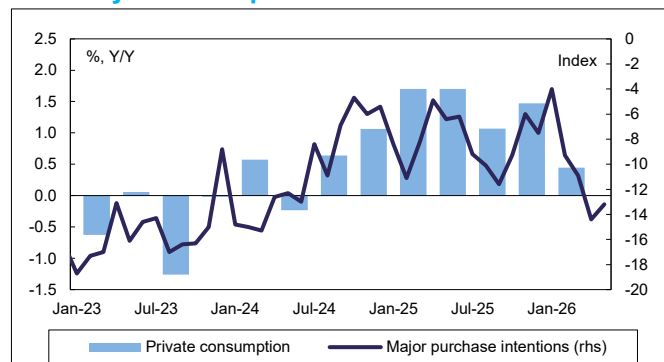
If the ifo survey is to be believed, however, German retailers are not quite as downbeat about the coming six months as they were last month when the respective expectations index plummeted to its lowest level since 2022. And today's GfK survey results suggested that German households are not quite as despondent either. Having in the prior survey fallen to the lowest level since early 2023, the headline GfK consumer confidence index – presented as a forecast for June – rose the most in 13 months, albeit remaining well below the range of the past few years. Within the detail, all key components improved. But the indicator of major purchase intentions was still the second-worst in more than two years. And that left it well below the average in Q1 when German private consumption failed to grow. So, like GDP, we expect household spending to decline in Q2. The deterioration in business sentiment also bodes ill for fixed investment, which already declined a steep 1.5%Q/Q in Q1 on weakness in construction, machinery and equipment. And having unexpectedly added as much as 1.3ppts to GDP growth in Q1 on strength in exports of chemicals, pharmaceuticals, metals and services – for which the latter rose the most in more than three decades – net trade seems likely to offer little support this quarter. A resumption of precautionary inventory accumulation after stocks subtracted a hefty 0.9ppt from growth last quarter will to some extent limit the contraction. But overall, we currently expect German GDP to decline about ¼%Q/Q in Q2.

Germany: GDP growth & survey indices



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

Germany: Consumption & consumer confidence



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

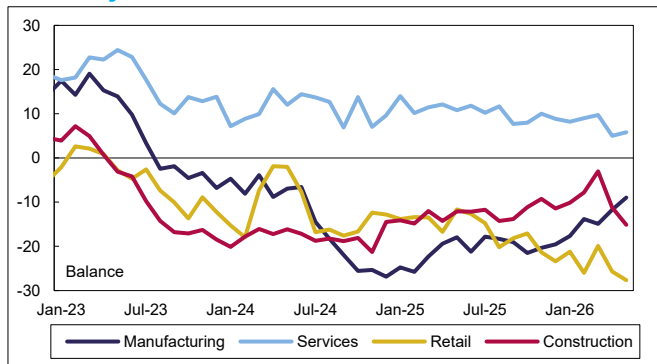
While not as bad as French flash PMIs, INSEE survey portrays weaker growth picture

Although the ifo indices look to have confirmed the suggestion of a slightly slower pace of deterioration in German activity this month, today's INSEE survey – whose larger and more comprehensive sample has tended to give a more accurate guide to French GDP – at least cast some doubt over the extent of the weakness shown by the flash French PMIs. Indeed, the headline business climate index was broadly unchanged (94) from its low level in April, contrasting with the further retrenchment in their composite output PMI (43.5, down 4.1pts). And the INSEE survey also suggested a modest improvement to the outlook for industry (102), relating mostly to a notable pickup in manufacturing output. That pattern looks more consistent with the broader trend of stock accumulation observed in other member states, and contrasts with that sector's flash PMI release. But otherwise, the INSEE survey still paints a dim picture. Business confidence remains heavily subdued, trending at its lowest level in five years and not wholly inconsistent with the PMIs. And after the French unemployment rate rose back above 8% at the start of the year, INSEE also reported that the employment climate (91.7) was the worst since the pandemic troughs and euro crisis before that as firms looked to reassess hiring plans due to high uncertainty and rising non-labour costs. Perhaps unsurprisingly, retailers were the most downbeat (89, down 11pts since March) amongst the sectors. Services (93) also reported a broad deterioration in sentiment, with declines most pronounced in consumer-facing subsectors like accommodation and food (87, down 9pts). Given the gloomier demand expectations and a sharp drop in hiring, selling price expectations in the services were at least more subdued than in April, contrasting the upticks in other sectors.

The week ahead in the euro area

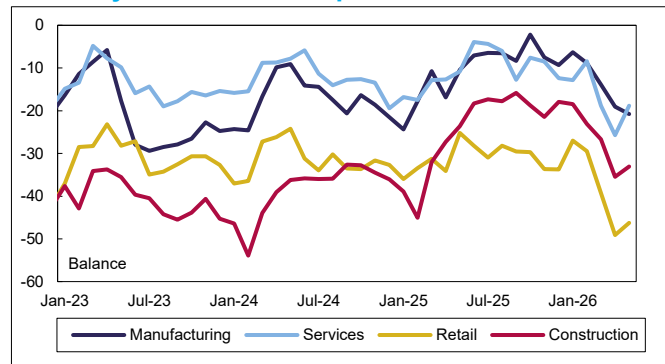
The weakness of this week's economic surveys is likely to have sharpened the attentiveness of policymakers towards the risks to activity stemming from the ongoing oil shock. But additional to the status of the Strait of Hormuz, inflation risks will remain more prominent in determining the ECB's policy response. So, we would grant May's flash inflation estimates from the largest member states (Friday) most seniority amongst the coming week's data. Despite the unrelenting volatility in wholesale oil markets – which have oscillated exclusively above \$100/bbl so far this month, above the average in April – consumer energy prices have showed some signs of stabilisation. To some degree, that trend has reflected policy interventions which should lend themselves to more variation at the member state level. Indeed, the implementation of the temporary *mineralölsteuer* (energy tax) cut in Germany should be sufficient to counter the rising inflation trend this month there, while the withdrawal of support in Italy implies a greater upside risk. Overall, we think that the effects on energy prices in the wider bloc should be small. But unfavourable base effects will take energy inflation higher regardless. And calendar-related distortions in categories such as package holidays and airfares raise broader upside risks across the estimates from the member states too. April PPI data from France, Italy (both Thursday) and Spain (Tuesday) will show the extent to which cost pressures broadened into other inputs.

Germany: ifo current business conditions indices



Source: Macrobond and Daiwa Capital Markets Europe Ltd.

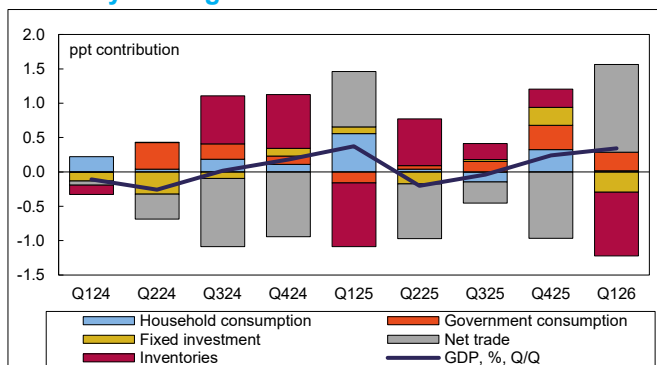
Germany: ifo business expectations indices*



*Coming six months.

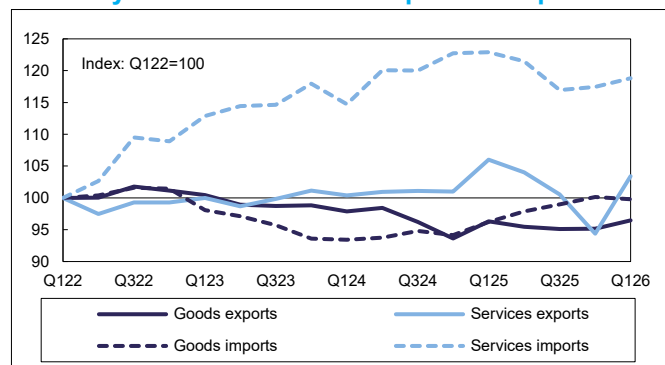
Source: Macrobond and Daiwa Capital Markets Europe Ltd.

Germany: GDP growth & contributions



Source: Macrobond and Daiwa Capital Markets Europe Ltd.

Germany: Goods & services exports & imports

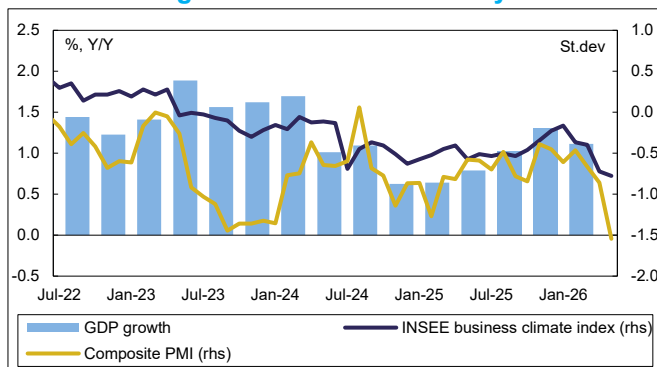


Source: Macrobond and Daiwa Capital Markets Europe Ltd.

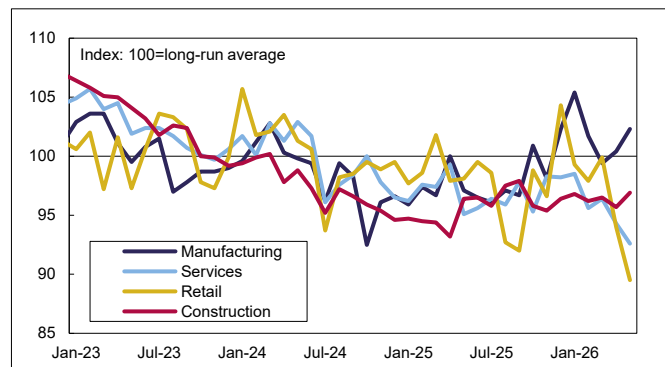
Otherwise, the week ahead will continue the flow of May's business and consumer surveys. In particular, the Commission's economic sentiment indicators (Thursday) will provide another input for policymakers' assessments about May activity. Considering the extent of their deterioration last month, falling to a more than five-year low (93.0), a modest improvement consistent with today's national surveys would be less surprising than another retrenchment akin to the flash PMIs. It will, however, be hoped that the nod to softer price pressures in the PMIs are also apparent. The ESIs will also be expected to confirm a modest uptick in consumer sentiment (-19.0, up 1.6pt), albeit still trending at a greatly subdued level. INSEE's consumer survey (Wednesday) will show whether, like Germany, expectations turned less downbeat in France. Istat's May update (Thursday) will also provide a broader Italian perspective.

In terms of hard activity data, April retail sales data from France (Tuesday) and Spain (Thursday) will provide a first view as to how the oil shock, and trough in consumer confidence, impacted consumption at the start of Q2. We note that support from fuel sales might be due in France after a steep fall in March (-4.9%M/M). Sales in Spain were less impacted but could also benefit from fiscal support measures which kicked in at the start of the month. Still, sales in March had been offset by surprisingly firm core spending, which could have dropped back in both member states in April if it merely reflected a temporary seasonal boost, placing the risks to the downside. The deterioration in survey-based indicators for the German labour market also points towards another non-negligible increase in May's jobless claims (Friday). Their release will also be accompanied by the final Q1 GDP readings from France and Italy (Friday), the latter of which will be accompanied by a first breakdown by expenditure components. Finally, beyond the data, the week ahead will also bring the publication of the ECB's account of its last monetary policy meeting. Of course, more information has become available since then, somewhat diminishing its usefulness. But, given that Belgian Governor Wunsch has already recalled that he had a 'slight preference' to hike at that meeting, we would be surprised if the account failed to express that at least some hawks had hoped for a more proactive approach.

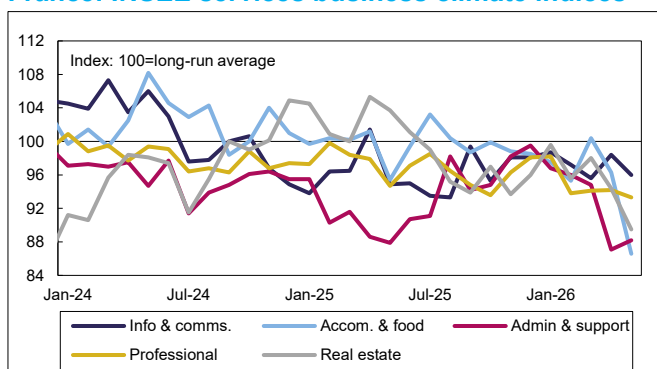
France: GDP growth & business survey indices



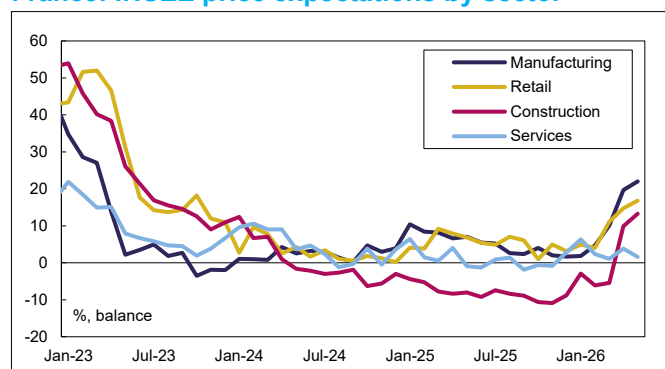
France: INSEE business climate indices



France: INSEE services business climate indices



France: INSEE price expectations by sector



UK

Retail sales fall sharply as spike in petrol prices & weak sentiment hit demand

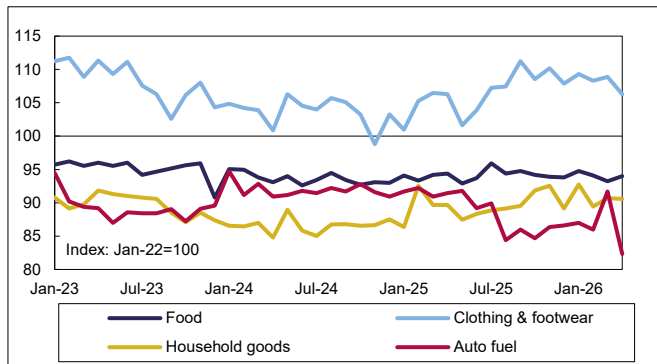
While household spending held up surprisingly well at the onset of the war in the Middle East, today's retail sales figures for April were predictably weak. Total sales volumes fell a steeper-than-expected 1.3%M/M at the start of Q2, the most in 11 months, to leave three-month growth at just 0.5%3M/3M, down from 1.4% in Q1. After firms and consumers rushed to fill up their tanks in March as prices at the pump leapt, the decline was principally driven by sales of auto fuel, which fell the most since 2012 when excluding Covid lockdowns (-10.2%M/M). But the weakness was broad-based. Aside from food – where spending may have been supported by a shift away from eating out – most categories fell. Sales of clothing (-2.4%M/M)

dropped to the lowest level since June 2025 reflecting subdued demand and variable weather conditions, while non-store sales declined the most in five months. Looking ahead, the outlook for consumption remains soft, with real incomes being hit by higher inflation, job insecurity and political uncertainty. The temporary cut on VAT on certain attractions and children's meals may boost to spending on some services over the summer. But household sentiment remains fragile. Indeed, today's GfK consumer confidence survey showed only a modest improvement in the headline index in May for a first month in three – up 2pts to -23 – leaving it still a full standard deviation below the long-run average. Moreover, spending intentions for big-ticket items fell in May to the weakest in 16 months.

Highest public sector net borrowing in any April since 2020 as fiscal rules remain a focus of debate

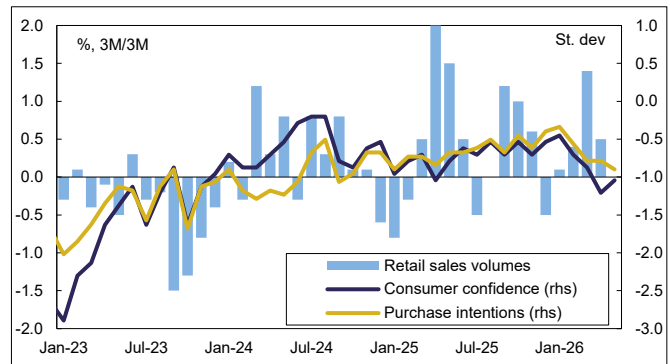
While Rachel Reeves' modest tax and spending measures announced yesterday were broadly cost-neutral, today's public finance figures nevertheless highlighted the challenges facing the current government – and any replacement of Keir Starmer as Prime Minister – in meeting its fiscal targets amid upside risks to inflation and downside risks growth. Public sector net borrowing (PSNB) was the highest in any April since records began in 1993 when excluding 2020 at the onset of Covid-19, reaching £24.3bn, some £4.9bn higher than a year earlier and £3.4bn more than forecast by the Office of Budget Responsibility (OBR). The overshoot was driven by a combination of higher debt interest costs, lower-than-forecast central government receipts and higher-than-expected central government spending. That said, the market response to today's public finance data was muted. Certainly, departmental spending estimates at this time of the year are highly provisional and likely to be revised significantly later in the year. And timelier HMRC cash receipts for April suggested an upwards revision to the ONS numbers for the tax take in due course too. This also follows a modest downwards revision to full-year net borrowing in financial year 2025-26, which is now estimated at £129bn, £3.7bn below the OBR's March-26 forecast and down £22.8bn on the prior financial year. Given that the timing of government revenues looks set to more backloaded than in previous years, the OBR still expects full-year borrowing to fall again this year. But not least due to its impact on inflation and hence debt interest, the energy shock adds significant uncertainties to the OBR's projections. And while Andy Burnham, Starmer's principal threat within the Labour Party, has pledged to stick to the current fiscal rules if he became Prime Minister, we would not be surprised if in due course the commitment to the rules became more relaxed. In particular, a recent proposal by Burnham allies within Labour's soft-left Renewal group advocated excluding from the fiscal rules any borrowing by certain public sector bodies, such as the development corporations involved in the construction of New Towns and the Oxford-Cambridge Arc, or even perhaps future issuance by the National Wealth Fund.

UK: Retail sales volumes



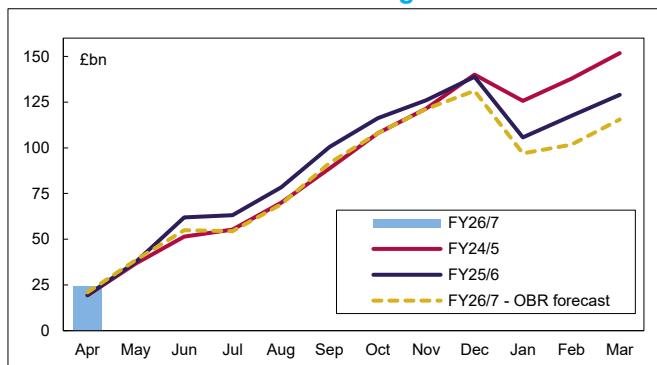
Source: Macrobond and Daiwa Capital Markets Europe Ltd.

UK: Retail sales & consumer confidence indices



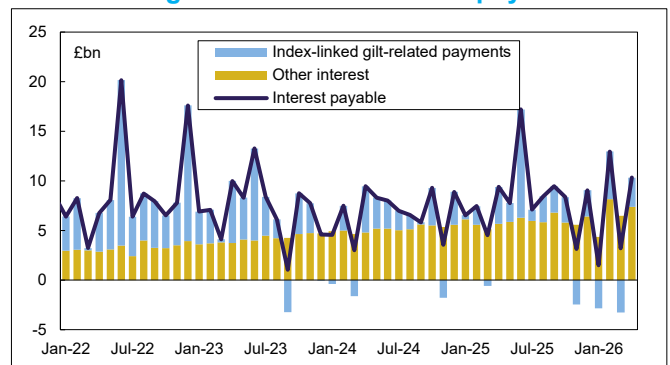
Source: GfK, Macrobond and Daiwa Capital Markets Europe Ltd.

UK: Public sector net borrowing



Source: OBR, ONS, Macrobond and Daiwa Capital Markets Europe Ltd.

UK: Central government net interest payable












Source: Macrobond and Daiwa Capital Markets Europe Ltd.

The week ahead in the UK

With the political furore temporarily subsiding and only a couple of second-tier surveys scheduled after Monday's public holiday, it looks set to be a much quieter week ahead for the UK. Arguably the biggest news of the week will be Ofgem's energy price cap announcement (Wednesday), which will confirm the extent to which household electricity bills will rise at the start of Q3. As Wednesday's inflation data showed, consumers have thus far been shielded from the full effects of the energy shock, with average electricity bills under the price cap having declined by £117 (-6.7%Q/Q) in April owing mostly to a reduction in government policy costs. The subsequent upshift in wholesale gas futures, however, is expected to add at least £200 (~13%Q/Q) from July, more than offsetting that intervention and adding around ½ppt to headline CPI inflation in Q3. In terms of more recent price developments, the BRC's latest shop price survey (Tuesday) will be closely watched for any signs of more immediate price pressures feeding into food and consumer goods prices on the high street this month. And while today's retail sales data fell short of fully corroborating the weakness of the previous CBI trades survey – which had reported its sharpest net decline (-68%) in year-on-year retail sales volumes on the series dating back to mid-1983 – May's indicator (also Tuesday) will provide the most timely view about retailers' prospects for any payback. Based on today's subdued consumer confidence reading, however, a rebound seems unlikely.

Daiwa economic forecast

		2025		2026			2027	2026	2027	2028
		Q4	Q1	Q2	Q3	Q4	Q1			
GDP		%, Q/Q						%, Y/Y		
Euro area		0.2	0.1	0.0	0.1	0.2	0.3	0.6	1.0	1.4
UK		0.2	0.6	0.1	0.0	0.2	0.4	1.0	1.1	1.4
Inflation, %, Y/Y										
Euro area										
Headline HICP		2.1	2.0	3.2	3.1	3.1	3.0	2.9	2.4	2.1
Core HICP		2.4	2.3	2.3	2.4	2.7	3.0	2.4	2.8	2.0
UK										
Headline CPI		3.4	3.1	3.2	3.9	3.9	3.9	3.5	3.0	1.8
Core CPI		3.3	3.2	2.8	3.2	3.4	3.5	3.1	3.1	2.2
Monetary policy, %										
ECB										
Deposit Rate		2.00	2.00	2.25	2.50	2.50	2.50	2.50	2.25	2.25
Refi Rate		2.15	2.15	2.40	2.65	2.65	2.65	2.65	2.40	2.40
BoE										
Bank Rate		3.75	3.75	3.75	4.00	4.00	4.00	4.00	3.50	3.50

Source: Bloomberg, ECB, BoE and Daiwa Capital Markets Europe Ltd.

The next Euro wrap-up will be published on Wednesday 27 May 2026

European calendar

Today's results						
Economic data						
Country	Release	Period	Actual	Market consensus/ <i>Daiwa forecast</i>	Previous	Revised
Euro area	Negotiated wages Y/Y%	Q1	2.46	-	2.95	2.86
Germany	ifo current assessment (expectations) indicator	May	86.1 (83.8)	85.1 (83.5)	85.4 (83.3)	-(83.5)
	ifo business climate indicator	May	84.9	84.2	84.4	84.5
	GfK consumer confidence indicator	Jun	-29.8	-34.0	-33.3	-33.1
	GDP – final estimate Q/Q% (Y/Y%)	Q1	0.3 (0.5)	<u>0.3 (0.5)</u>	0.2 (0.5)	-
	GDP – private consumption Q/Q%	Q1	0.0	-	0.5	-
	GDP – government spending Q/Q%	Q1	1.1	-	1.1	1.5
	GDP – capital investment Q/Q%	Q1	-1.5	-	1.0	1.3
France	INSEE business (manufacturing) confidence indicator	May	94 (102)	94 (99)	94 (100)	-
	INSEE production outlook (own-company) indicator	May	-17 (4)	-17 (6)	-18 (7)	-17 (6)
UK	Retail sales – incl. auto fuel M/M% (Y/Y%)	Apr	-1.3 (0.0)	-0.6 (1.3)	0.7 (1.7)	0.6 (1.4)
	Retail sales – excl. auto fuel M/M% (Y/Y%)	Apr	-0.4 (1.1)	-0.3 (1.7)	0.2 (1.7)	0.1 (1.5)
	GfK consumer confidence indicator	May	-23	-28	-25	-
	Public sector net borrowing £bn	Apr	24.3	20.9	12.6	11.5
Auctions						
Country	Auction	- Nothing to report -				


























Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

The coming week's calendar

The coming week's key events & auctions			
Country	BST	Event / Auction	
Monday 25 May 2026			
UK		-	Spring Bank Holiday – public holiday in the UK
Tuesday 26 May 2026			
Italy		10.00	Auction: to sell up to €2.5bn of 2.2% 2028 bonds
		10.00	Auction: to sell up to €1.5bn of 1.1% 2031 inflation-linked bonds
		10.00	Auction: to sell up to €1bn of 2.25% 2046 inflation-linked bonds
Wednesday 27 May 2026			
Euro area		09.00	ECB to publish biannual Financial Stability Review
Germany		10.30	Auction: to sell up to €1bn of 2.6% 2041 bonds
		10.30	Auction: to sell up to €1bn of 2.9% 2056 bonds
UK		07.00	Ofgem to announce UK energy price cap level for Q326
		10.00	Auction: to sell £4bn of 4.125% 2033 bonds
Thursday 28 May 2026			
Euro area		01.00	ECB Chief Economist Lane participates in fireside chat at the BOJ-IMES monetary policy conference, Tokyo
		12.30	ECB to publish monetary policy account of 29-30 April Governing Council meeting
Italy		10.00	Auction: to sell bonds*
Friday 29 May 2026			
UK		09.20	BoE Governor Bailey to deliver speech at the Reykjavik 2026 economic conference

*Details to be announced. Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

The coming week's key data releases

Country	BST	Release	Period	Market consensus/ <i>Daiwa forecast</i>	Previous
Monday 25 May 2026					
- Nothing scheduled -					
Tuesday 26 May 2026					
France		- Retail sales Y/Y%	Apr	-	0.1
Spain		08.00 PPI Y/Y%	Apr	-	3.4
UK		00.01 BRC shop price index Y/Y%	May	1.1	1.0
		11.00 CBI distributive trades survey – reported retail sales net balance %	May	-50	-68
Wednesday 27 May 2026					
Euro area		05.00 New car registrations Y/Y%	Apr	-	12.4
France		07.45 INSEE consumer confidence indicator	May	82	84
Thursday 28 May 2026					
Euro area		10.00 Commission economic sentiment indicator	May	92.6	93.0
		10.00 Commission services (industrial) confidence indicator	May	0.3 (-8.0)	0.9 (-7.7)
		10.00 Final Commission consumer confidence indicator	May	<u>-19.0</u>	-20.6
France		07.45 PPI Y/Y%	Apr	-	0.2
Italy		09.00 Istat economic (manufacturing) sentiment indicator	May	-	95.2 (87.9)
		09.00 Istat consumer confidence indicator	May	-	90.8
		11.00 PPI Y/Y%	Apr	-	5.4
Spain		08.00 Retail sales Y/Y%	Apr	3.6	4.1
Friday 29 May 2026					
Germany		07.00 Import prices M/M% (Y/Y%)	Apr	1.1 (5.3)	3.6 (2.3)
		08.55 Unemployment claims rate % (change 000s)	May	6.4 (10)	6.4 (20)
		13.00 Preliminary HICP (CPI) Y/Y%	May	2.9 (3.0)	2.9 (2.9)
France		07.45 Preliminary HICP (CPI) Y/Y%	May	2.9 (2.5)	94 (100)
		07.45 Consumer spending M/M% (Y/Y%)	Apr	-	0.7 (0.5)
		07.45 GDP – final estimate Q/Q% (Y/Y%)	Q1	<u>0.0 (1.1)</u>	0.2 (1.2)
		07.45 Total (private sector) payrolls Q/Q%	Q1	- <u>(-0.1)</u>	-0.1 (-0.1)
Italy		09.00 Unemployment rate %	Apr	5.3	5.2
		10.00 Preliminary HICP (CPI) Y/Y%	May	3.3 (3.0)	2.8 (2.7)
		11.00 GDP – final estimate Q/Q% (Y/Y%)	Q1	<u>0.2 (0.7)</u>	0.3 (0.9)
Spain		08.00 Preliminary HICP (CPI) Y/Y%	May	3.5 (3.3)	12.6

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

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