

# Euro wrap-up

## Overview

- Bunds made losses as euro area core inflation fell less than expected in April and GDP surprised on the upside in Q1.
- Gilts followed the global trend lower despite a further fall in a survey measure of UK high street inflation.
- Wednesday will bring the final UK manufacturing PMIs for April with the equivalent figures from the euro area due on Thursday, and euro area unemployment and French IP data out on Friday.

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### Daily bond market movements

Bond	Yield	Change
BKO 2.9 06/26	3.025	+0.078
OBL 2.1 04/29	2.614	+0.068
DBR 2.2 02/34	2.582	+0.051
UKT 0% 01/26	4.483	+0.053
UKT 0½ 01/29	4.247	+0.048
UKT 4% 01/34	4.345	+0.054

\*Change from close as at 5:00pm BST.  
Source: Bloomberg

## Euro area

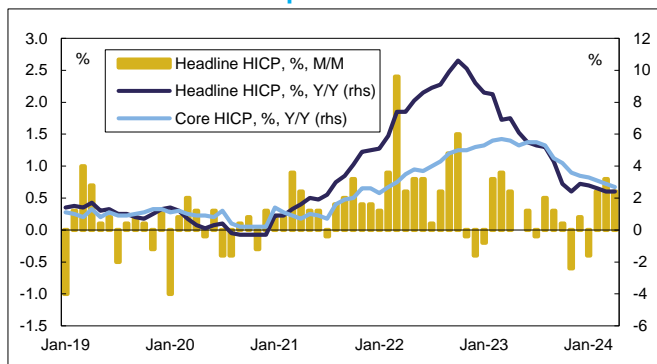
### Headline inflation unchanged in April with core rate down a touch less than expected

As expected, euro area consumer price inflation was unchanged in April at 2.4%Y/Y, matching the lowest rate since July 2021. That headline rate would have declined from March had it not been for a fifth successive moderation in the pace of decline in energy prices, with the respective component up 1.2ppt to a twelve-month high of -0.6%Y/Y on higher petrol prices and the withdrawal of government support for household bills in countries such as Germany and Spain. Moreover, having reached a 2½-year low last month, inflation of food, alcohol and tobacco also rose (up 0.2ppt to 2.8%Y/Y). The core components continued to decline, however. Consistent with the absence of pressures in the global factory sector, prices of core goods rose the least in any April in a decade (0.45%M/M) to push the respective annual rate down 0.2ppt to 0.9%Y/Y, the lowest since July 2021. And in part thanks to the early timing of Easter, which contributed to stickiness in the category in the prior month and resulted in a favourable base effect, services inflation dropped 0.3ppt to 3.7%Y/Y, the lowest since August 2022. As a result, core inflation fell a ninth successive month to the lowest since February 2022. The extent of the decline of 0.2ppt to 2.7%Y/Y, however, was 0.1ppt less than the consensus forecast on the Bloomberg survey.

### Services momentum unlikely to prevent a June rate cut but still too high for comfort

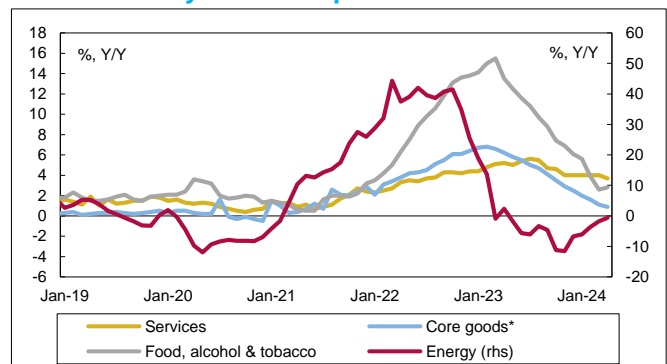
According to the ECB's own seasonally adjusted estimates, core goods prices fell 0.2%M/M in April to leave momentum in that category very weak, below 1.0% annualised on both the 3M/3M and 6M/6M bases. So, the slight disappointment in the core component in April came from services, for which prices rose a seasonally adjusted 0.3%M/M. That was the softest such rate since December. The 6M/6M adjusted annualised rate of services inflation edged up just 0.1ppt to a mere three-month high of 3.4%. But the rate of services price momentum on an adjusted annualised three-month basis rose to a nine-month high of 5.3%. Some of that pressure probably reflects some lingering Easter effects in April. Indeed, while we will only know for sure once the final estimates are published on 17 May, we suspect that air and other travel fares as well as hotel prices were a likely source. So, we expect a cooling in services price momentum and a further slight moderation in overall core inflation in May. And in the absence of an upside surprise in the Q1 negotiated wage data later next month, or a new energy price shock, even a flat core rate in May should be enough to secure a first ECB rate cut of 25bps in June. With services inflation momentum still likely to be a little too high for the comfort of many Governing Council members, and both headline and core inflation at risk of slightly overshooting the ECB's projections for Q2, we would certainly not expect that cut to be accompanied by a pre-commitment to further easing thereafter. But as we expect both headline and core inflation to moderate to below 2½%Y/Y in Q3 and remain on track to fall below target in 2025, we still expect further 25bps cuts in September and December too. Of course, if services momentum remains high over coming months, such additional easing will be postponed.

### Euro area: Consumer price inflation



Source: Macrobond and Daiwa Capital Markets Europe Ltd.

### Euro area: Key HICP components



\*Non-energy industrial goods. Source: Macrobond and Daiwa Capital Markets Europe Ltd.

## Return to growth in Q1 stronger than expected

Certainly, today's first estimate of euro area GDP in Q1 will have diminished the case for aggressive rate cuts over coming months. The data suggested a stronger-than-expected return to growth at the start of the year, following the very mild technical recession in the second half of 2023 amid a broad sideways trend over the previous five quarters. In particular, euro area GDP growth rose 0.3%Q/Q in Q1, the firmest pace since Q322 and 0.2ppt above the ECB's projection. This left economic output up 0.4%Y/Y and almost 3½% above the pre-pandemic benchmark in Q419. Admittedly, output was still some 10% below the pre-pandemic trend and lagging well behind the US, where the level of GDP last quarter stood more than 8½% above the Q419 level. While the April flash PMIs suggest that the positive momentum is being maintained in Q2, the Commission survey, which often provides a more reliable guide to euro area GDP growth, suggests that we might expect to see some negative payback this quarter, particularly as growth in Q1 was inflated by temporary strength in construction related to record warm winter temperatures. So, we expect a moderation in GDP growth in Q2 before a tick up again in the second half of the year as consumption benefits from improved disposable incomes.

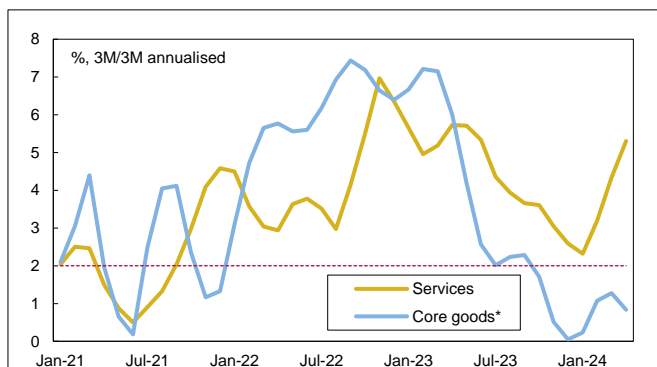
## Widespread expansion across the member states

Positively, the rebound in the euro area GDP in Q1 was felt widely across the region with most member states recording stronger growth than in Q4 and no countries suffering a contraction. Indeed, the German economy bounced back a firmer-than-expected 0.2%Q/Q – the strongest pace for a year – although this was underpinned by a weather-assisted boost to construction. Given a larger-than-previously estimated contraction in Q4 (-0.5%Q/Q), German GDP was still down 0.2%Y/Y and just 0.3% above the Q419 level. Meanwhile, France recorded a fourth consecutive quarterly expansion in Q1, with growth ticking up 0.1ppt to 0.2%Q/Q, to leave economic output up 1.1%Y/Y and more than 2% above the Q419 level. GDP also exceeded expectations in Italy, where it rose for a fourth quarter out of the past five and by 0.3%Q/Q, to leave it up 0.6%Y/Y and some 4.6% above the pre-pandemic benchmark. But of the large member states, the expansion in Q1 was again strongest in Spain, where GDP rose for the fifteenth consecutive quarter, by 0.7%Q/Q, to leave it 3.7% above the Q419 level. Portuguese GDP also rose 0.7%Q/Q to be more than 6% above the level at end-2019. And having contracted in the previous four quarters, Ireland's GDP made a non-negligible contribution to euro area growth, rising 1.1%Q/Q in Q1.

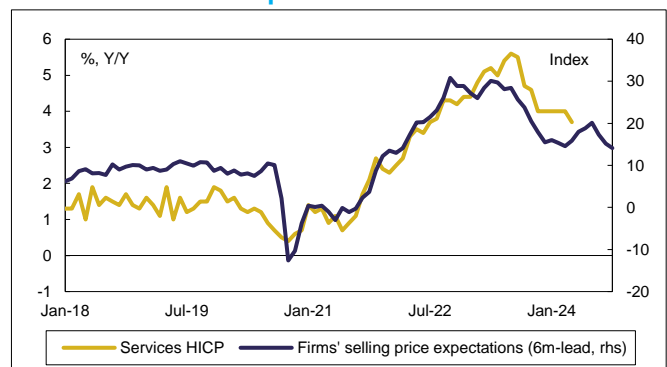
## Fixed investment and consumer spending firmer, but inventories likely remained a drag

Eurostat will not publish an expenditure breakdown of euro area Q1 GDP until June. But the limited information published so far by the national authorities suggests that momentum in final domestic demand improved at the start of 2024, with consumer spending benefitting from a pickup in real disposable incomes and fixed investment perhaps increasing somewhat

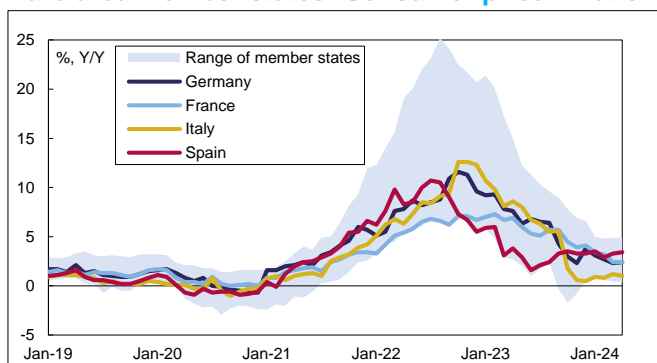
### Euro area: Core inflation momentum



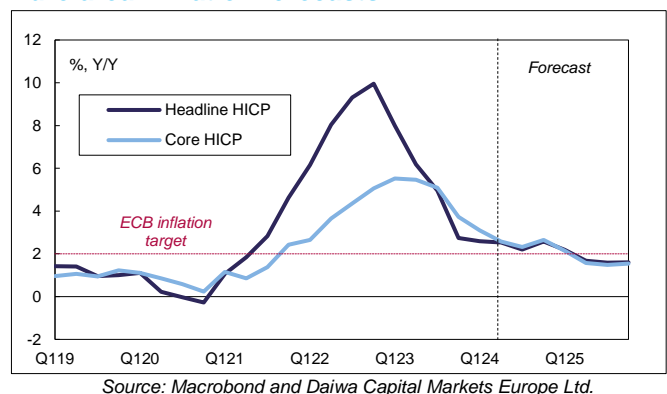
### Euro area: Services price indices



### Euro area member states: Consumer price inflation



### Euro area: Inflation forecasts



too. Net trade also looks to have provided modest support to growth in some member states. But this impact appears to have been partly offset by a further drag from inventories as firms continued to run down stocks, perhaps recognizing the weakness of new orders and falling work backlogs. In Germany, however, Destatis reported that growth in Q1 was led by an increase in construction and exports, although this was partly offset by a drag in household consumption, illustrated by today's data for retail sales, which fell 1.0%3M/3M in Q1 despite a pickup in March (+1.8%M/M). In contrast, however, French and Spanish consumption added 0.2ppt apiece to GDP growth in Q1, with fixed investment adding 0.1ppt and 0.5ppt respectively too. But while net trade added to growth in Spain as services exports benefitted from an increase in the number of overseas visitors, and ISTAT suggested that it also drove growth in Italy, it provided no support in France.

**The coming few days in the euro area**

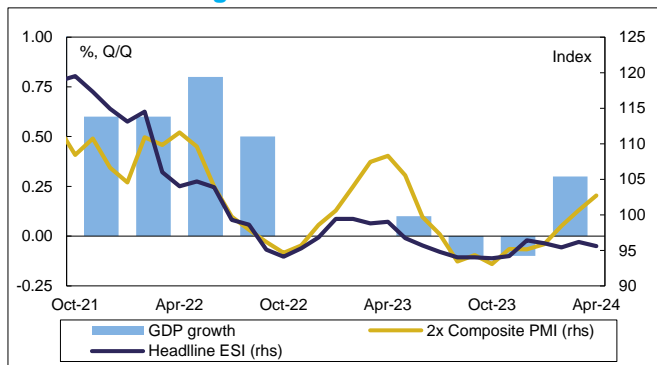
Following the Labour Day holiday across the region tomorrow, it should be a relatively quiet end to the week for euro area data releases. Most notable will be Friday's euro area jobless figures for March, which are likely to point to ongoing resilience in the labour market. In particular, we expect the unemployment rate to remain for a fifth successive month at a series low of 6.5%. The final manufacturing PMIs for April will also be published on Thursday. The flash release saw the euro area manufacturing output index rise to a twelve-month high of 47.3, albeit remaining firmly in contractionary territory. And the detail suggested another notable decline in new orders this month, with the respective index down to a four-month low. With input cost pressures continuing to moderate (albeit at a softer pace amid the pickup in energy prices), the output price PMI implied a further fall for a twelfth consecutive month, suggesting limited pipeline pressures in the factory sector. In addition to the unemployment data, Friday will also bring French industrial production figures for March.

**UK**

**Shop price inflation drops to the lowest since November 2021**

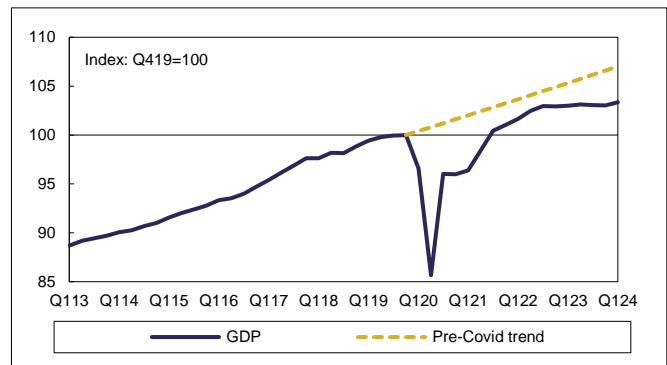
According to the BRC, despite the hike in the National Living Wage at the start of the month, inflation on the UK high street moderated notably further in April amid fierce competition and subdued demand. Overall, the BRC's measure of shop prices fell for a third month out of the past four, down 0.3%M/M. This left shop price inflation down 0.5ppt to 0.8%Y/Y, the lowest since November 2021 and more than 8ppts below last year's peak. There was a further disinflationary trend in food prices, with the BRC's measure (3.4%Y/Y) down to its lowest rate for more than two years. But the downtrend in April principally reflected non-food inflation, which slipped into negative territory (-0.6%Y/Y) for the first time since December 2021, with heavy discounting in clothing (down 1.0ppts to -7.9%Y/Y), DIY & gardening products (down 1.0ppts to 1.7%Y/Y) and health and beauty (down 1.4ppts to 1.5%Y/Y). Given the weakness in demand and relatively subdued consumer confidence, we

**Euro area: GDP growth & sentiment indices**



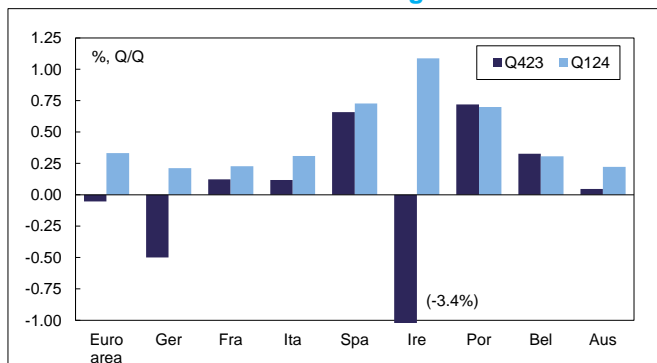
Source: EC, S&P Global, Macrobond and Daiwa Capital Markets Europe Ltd.

**Euro area: GDP level**



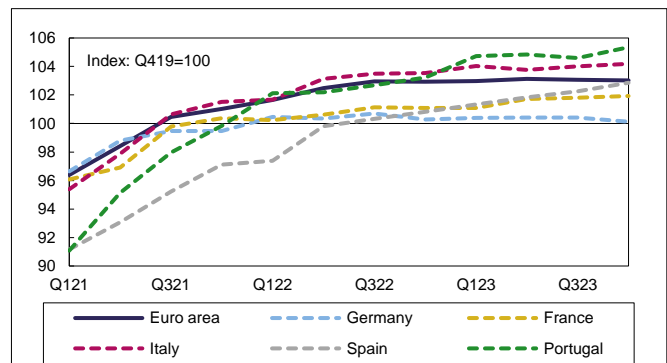
Source: Macrobond and Daiwa Capital Markets Europe Ltd.

**Euro area member states: GDP growth**



Source: Macrobond and Daiwa Capital Markets Europe Ltd.

**Euro area member states: GDP levels**



Source: Macrobond and Daiwa Capital Markets Europe Ltd.

expect the disinflationary trend in core goods to be maintained over coming months. And thanks not least to the steep drop in household energy bills this month, as well as a gradual dissipation of pressures in services, we expect CPI inflation to temporarily drop below the BoE's 2.0% target this quarter.

### Gross mortgage lending and external financing to business up in March

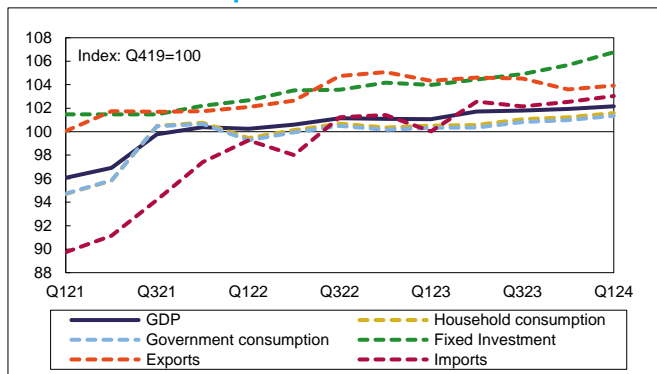
While the effective interest rate on mortgages fell a further 17bps to 4.73% in March – the lowest since last July – various indicators suggest that house prices are now rising. But while mortgage approvals have risen to a six-month high (61.3k), today's mortgage lending figures were on the softer side of expectations. In particular, net lending secured on dwellings was just £0.3bn in March, to leave it down 0.1%Y/Y. Admittedly, gross lending for house purchase picked up to £20.1bn, the highest in thirteen months. But this was in part offset by increased mortgage repayments. And while net lending on a three-month basis returned to positive territory for the first time since October, at £0.7bn it remained well below the pre-pandemic five-year average (£11.2bn) and the recent peak of £25bn in mid-2021. Meanwhile, net consumer credit rose a further £1.6bn in March, bang in line with the average in the previous six months, to leave the outstanding stock of such loans up 8.8%Y/Y. Bank lending to businesses remained weak in March, declining for a second successive month by a net £1.1bn, with annual growth in lending to large firms slowing to just 0.5% and declining to SMEs (-4.7%Y/Y). However, this was more than offset by the largest net increase in other external financing since May 2020 (£10.2bn), reflecting a notable increase in bond issuance last month (£8.0bn) as firms took advantage of lower yields, which hopefully might support business investment over coming months too.

### The coming few days in the UK

The UK's data calendar over the remainder of the week will be relatively quiet, with the release of just the final April PMIs, for which the manufacturing survey will be published tomorrow and the services survey on Friday. According to the flash PMIs, UK economic momentum at the start of Q2 picked up further led predictably by the services sector. Most notably, the composite PMI jumped in April by 1.2pts, well above expectations and the most since December, to an 11-month high of 54.0, bang in line with the average in the two decades before the pandemic. The flash survey also reported a notable increase in cost pressures, although the composite output price PMI fell to an eight-month low, suggesting that these were increasingly being absorbed by margins. Meanwhile, the Nationwide house price survey for April is also due tomorrow and expected to report only a modest increase in prices that month as elevated borrowing costs continue to restrain prospective buyers.

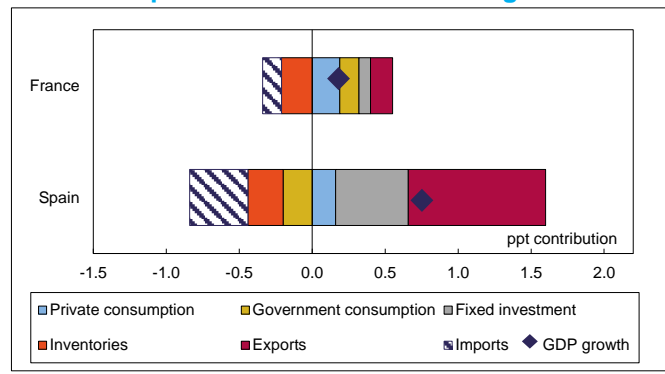
*The next edition of the Euro wrap-up will be published on 3 May 2024*

#### France: GDP & expenditure levels



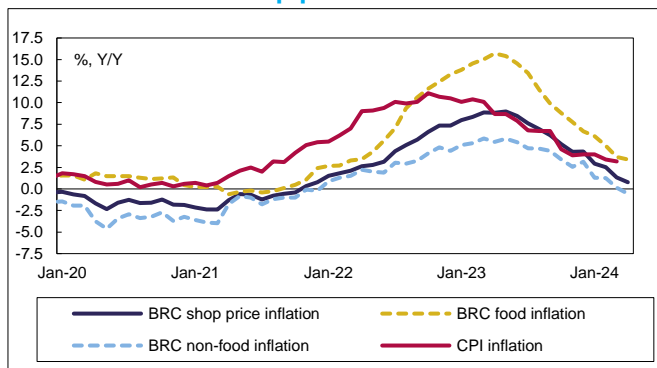
Source: Macrobond and Daiwa Capital Markets Europe Ltd.

#### France & Spain: Contributions to GDP growth



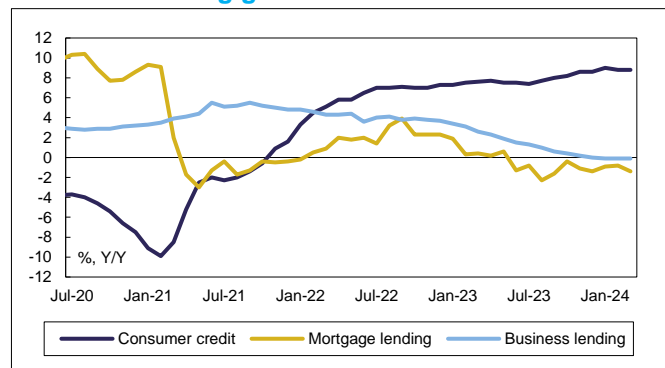
Source: Macrobond and Daiwa Capital Markets Europe Ltd.

#### UK: Consumer & shop price inflation



Source: Macrobond and Daiwa Capital Markets Europe Ltd.

#### UK: Bank lending growth



Source: Macrobond 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
Euro area	Preliminary HICP (core HICP) Y/Y%	Apr	<b>2.4 (2.7)</b>	<u>2.4 (2.5)</u>	2.4 (2.9)	-
	GDP – first estimate Q/Q% (Y/Y%)	Q1	<b>0.3 (0.4)</b>	<u>0.2 (0.2)</u>	-0.1 (0.1)	-
Germany	Retail sales M/M% (Y/Y%)	Mar	<b>1.8 (-2.7)</b>	-	-1.9 (1.7)	-1.5 (-)
	Unemployment change 000s (rate %)	Apr	<b>5.9 (10.0)</b>	5.9 (8.0)	5.9 (4.0)	5.9 (6.0)
France	GDP – first estimate Q/Q% (Y/Y%)	Q1	<b>0.2 (-0.2)</b>	<u>0.1 (-0.2)</u>	-0.3 (-0.2)	-0.5 (-)
	Preliminary HICP (CPI) Y/Y%	Apr	<b>2.4 (2.2)</b>	2.2 (2.1)	2.4 (2.3)	-
Italy	PPI Y/Y%	Mar	<b>-7.5</b>	-	-5.5	-
	Consumer spending M/M% (Y/Y%)	Mar	<b>0.4 (0.5)</b>	0.2 (0.1)	0.0 (-0.8)	0.1 (-0.7)
Spain	GDP – first estimate Q/Q% (Y/Y%)	Q1	<b>0.3 (0.6)</b>	<u>0.1 (0.3)</u>	0.2 (0.6)	0.1 (0.7)
	Preliminary HICP (CPI) Y/Y%	Apr	<b>1.0 (0.9)</b>	-	1.2 (1.2)	-
UK	GDP – first estimate Q/Q% (Y/Y%)	Q1	<b>0.7 (2.4)</b>	<u>0.3 (1.8)</u>	0.6 (2.0)	0.7 (2.1)
	BRC shop price index Y/Y%	Apr	<b>0.8</b>	1.3	1.3	-
UK	Lloyds business barometer (price expectations)	Apr	<b>42 (60)</b>	-	42 (57)	-
	Net consumer credit £bn (Y/Y%)	Mar	<b>1.6 (8.8)</b>	-	1.4 (8.7)	- (8.8)
	Net mortgage lending £bn (mortgage approvals 000s)	Mar	<b>0.3 (611.3)</b>	1.5 (61.5)	1.5 (60.4)	1.6 (60.5)

#### Auctions

Country	Auction
Germany	sold €2.72bn of 2.1% 2029 bonds at an average yield of 2.55%
UK	sold £4.0bn of 4.125% 2029 bonds at an average yield of 4.251%

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

### Tomorrow's releases

#### Economic data

Country	BST	Release	Period	Market consensus/ <i>Daiwa forecast</i>	Previous
UK	07.00	Nationwide house price index M/M% (Y/Y%)	Apr	0.1 (1.2)	-0.2 (1.6)
	09.30	Final manufacturing PMI	Apr	<u>48.7</u>	50.3






#### Auctions and events

Germany	10.30	Auction: €4bn of 2.2% 2034 bonds
UK	10.00	Auction: £3.75bn of 4.625% 2034 bonds



Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

## Thursday's releases

### Economic data

Country	BST	Release	Period	Market consensus/ <i>Daiwa forecast</i>	Previous
Euro area 	09.00	Final manufacturing PMI	Apr	<u>45.6</u>	46.1
Germany 	08.55	Final manufacturing PMI	Apr	<u>42.2</u>	41.9
France 	08.50	Final manufacturing PMI	Apr	<u>44.9</u>	46.2
Italy 	08.45	Manufacturing PMI	Apr	51.4	50.4
Spain 	08.15	Manufacturing PMI	Apr	50.4	51.4





### Auctions and events

Euro area 	12.15	ECB Chief Economist Lane to give virtual lecture at University of Stanford			
France 	09.50	Auction: 3.5% 2033 bonds			
	09.50	Auction: 1.25% 2034 bonds			
	09.50	Auction: 2.5% 2043 bonds			
	09.50	Auction: 3.25% 2055 bonds			

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

## Friday's releases

### Economic data

Country	BST	Release	Period	Market consensus/ <i>Daiwa forecast</i>	Previous
Euro area 	10.00	Unemployment rate %	Mar	6.5	6.5
France 	07.45	Industrial production M/M% (Y/Y%)	Mar	0.3 (1.3)	0.2 (-0.8)
Spain 	08.00	Unemployment change 000s	Apr	-	-33.4
UK 	09.30	Final services (composite) PMI	Apr	54.9 (54.0)	53.1 (52.8)

### Auctions and events

- Nothing scheduled -

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

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