

Euro wrap-up

Overview

- Bunds followed US10s lower as euro area employment growth accelerated in Q1 despite subdued GDP growth, even as German investor sentiment with respect to the outlook deteriorated.
- Despite continued strength in wage growth, Gilts outperformed on evidence of a further loosening of UK labour market conditions.
- Wednesday will bring final euro area inflation estimates for April.

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Daily bond market movements

Bond	Yield	Change
BKO 2.8 06/25	2.627	+0.049
OBL 2.2 04/28	2.296	+0.057
DBR 2.3 02/33	2.345	+0.042
UKT 0% 06/25	3.809	-0.018
UKT 1% 10/28	3.625	-0.004
UKT 3% 01/33	3.813	-0.003

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

Euro area

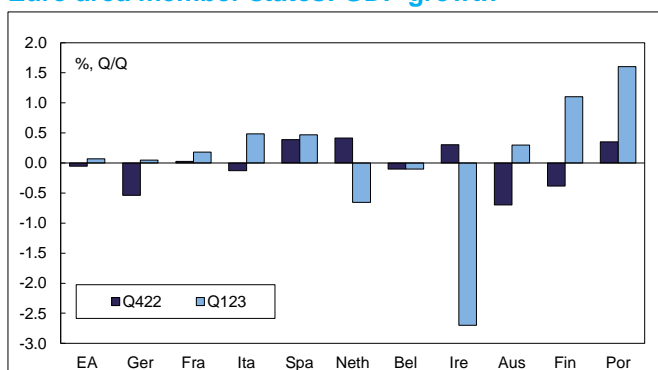
Employment growth accelerated in Q1 when GDP inched higher Q1

Despite the slump in manufacturing output in March reported yesterday, there were no material revisions in today's updated national accounts release. This confirmed that euro area GDP returned to very modest growth in Q1, of 0.1%Q/Q, to leave economic output almost 2½% above the pre-pandemic level and up 1.3%Y/Y. Of the member states to have published figures, roughly half reported positive growth, including France (0.2%Q/Q), Italy (0.5%Q/Q), Spain (0.5%Q/Q) and Portugal (1.6%Q/Q). But Germany's economy stagnated at the start of the year. And the euro area's expansion was held back by the sharp contraction in Ireland (-2.7%Q/Q), which knocked 0.1ppt off the region's GDP growth. Despite the subdued economic recovery, today's employment data suggested that euro area demand for labour remained extremely resilient in the first quarter of the year. Indeed, these confirmed an eighth successive quarterly rise in employment, rising by 1.00mn (0.6%Q/Q), the most since Q321 to 166.06mn. National data highlight ongoing notable job growth in Spain and Germany (despite the stagnation in the latter country's economy). However, together these two accounted for just 40% of the quarterly increase, suggesting that the pickup was widespread among member states. Surveys point to a slight easing in recovery momentum in the labour market in the second quarter. But the region's unemployment rate was at a series low of 6.5% in March, labour market slack was already at a series low of 13.5% – 1.5ppts below the pre-pandemic rate – by the end of last year, when the employment rate also hit a series high. So, the slowdown in job growth likely in part reflects a scarcity of skilled workers, maintaining risks of persistent unit labour cost growth above rates that many Governing Council members will consider consistent with the ECB's inflation target.

Net trade provided support to GDP growth as imports fell sharply

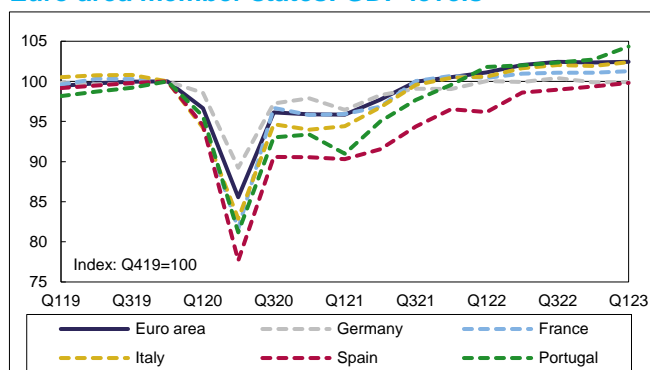
The expenditure breakdown of Q1 GDP will not be available until the release of the third estimate, due in early June. But monthly data and the limited figures available from the member states strongly suggest that household consumption subtracted from GDP growth in Q1. In contrast, net trade appears to have provided the key boost that avoided a contraction in GDP, albeit only because the weakness of domestic demand meant that import volumes fell at a faster pace than exports. Today's monthly euro area goods trade figures saw the value of imports fall sharply for a seventh consecutive month in March, by 7.1%M/M, the most since the early stages of the Covid-19 pandemic, to leave them down more than 9%Q/Q in Q1 and some 23% below last year's peak. Of course, this to a large extent reflects the drop in prices of energy and commodities over recent months. But import volumes were trending in February some 2.7% below the Q4 average consistent with the weakness in household spending. Meanwhile, the value of exports was little changed in March, as solid growth in exports to Japan, Switzerland and UK was offset by a sharp decline to China, to leave them down just 1.3%Q/Q in Q1. As a result, the

Euro area member states: GDP growth



Source: Refinitiv and Daiwa Capital Markets Europe Ltd.

Euro area member states: GDP levels



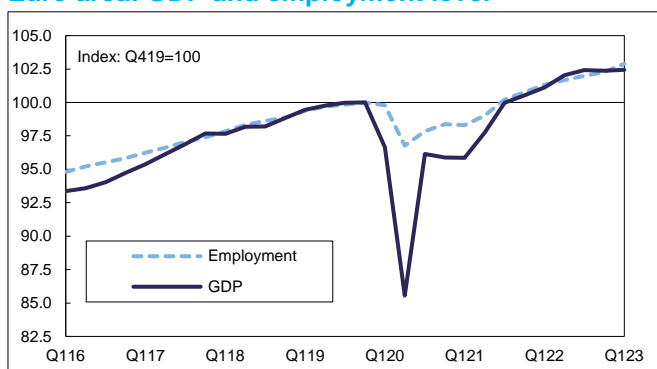
Source: Refinitiv and Daiwa Capital Markets Europe Ltd.

euro area's goods trade balance returned to surplus in March, jumping to €17.0bn, the highest for two years and some €32bn above December's level and €64bn above last year's record deficit.

German investor survey points to increased wariness of near-term outlook

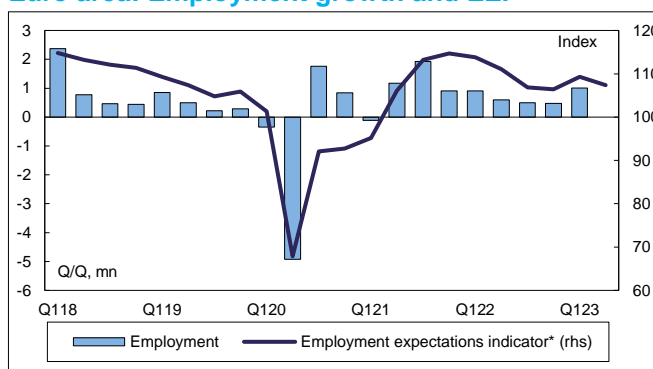
Today's German ZEW survey suggested that investors remained on the whole downbeat about economic conditions in the largest member state. While the current situation balance remained comfortably above the average over the past year (-49.8), it nevertheless slipped back in May, by 2.3pts to -34.8, well below the long-run average (-9.1). Moreover, investors were notably more downbeat about expectations for the coming six months, with the respective index declining 14.8pts to -10.7, the first negative reading since December. ZEW attributed the pessimism in part to expectations of tighter financing conditions amid the ECB's increasingly restrictive monetary policy. And while earnings expectations for banks and insurance firms were little changed compared with April and remained in positive territory, the share expecting profits to improve in those sub-sectors remained notably softer than in February. Moreover, assessments of profitability in a range of other sub-sectors, including construction, autos, steel and retail, remained firmly in negative territory.

Euro area: GDP and employment level



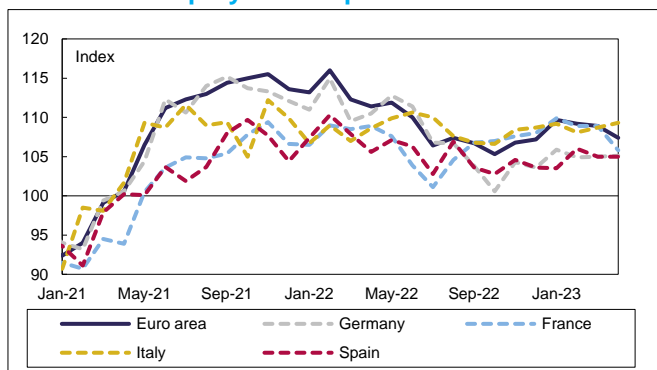
Source: Refinitiv and Daiwa Capital Markets Europe Ltd.

Euro area: Employment growth and EEI



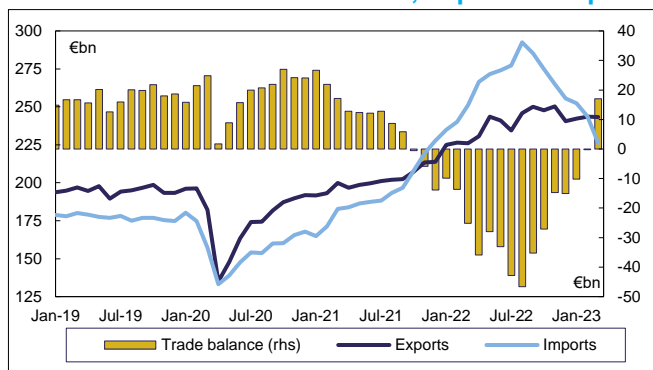
*Q223 figure is April survey result. Source: EC, and Daiwa Capital Markets Europe Ltd.

Euro area: Employment expectations indices



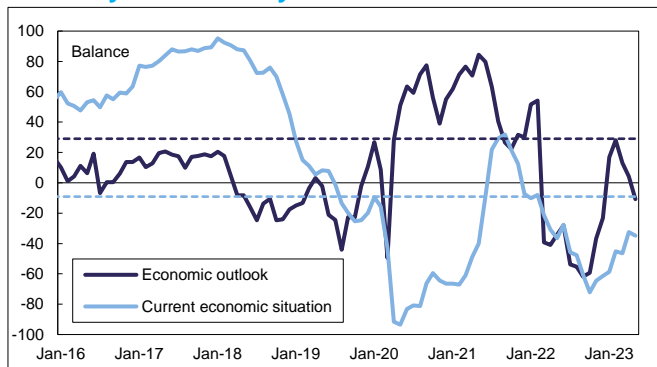
Source: EC, and Daiwa Capital Markets Europe Ltd.

Euro area: Goods trade balance, imports & exports*



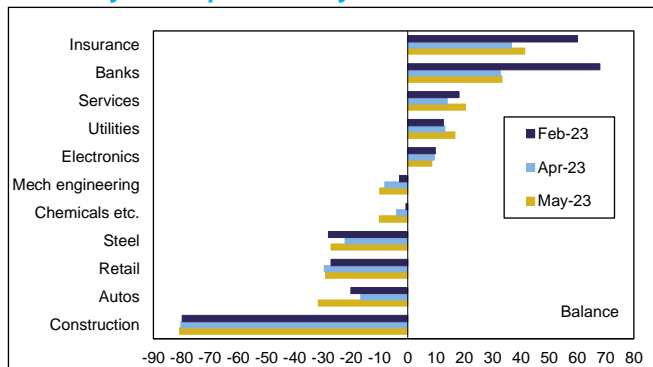
*Seasonally adjusted values. Source: Refinitiv and Daiwa Capital Markets Europe Ltd.

Germany: ZEW survey sentiment indices



Source: Refinitiv and Daiwa Capital Markets Europe Ltd.

Germany: ZEW profitability outlook indices



Source: Refinitiv and Daiwa Capital Markets Europe Ltd.

The day ahead in the euro area

Tomorrow will bring final euro area consumer price figures for April. The flash estimate saw headline inflation unexpectedly tick higher, by 0.1ppt to 7.0%Y/Y, while the core rate edged slightly lower, by 0.1ppt to 7.5%Y/Y. While final numbers from Italy today brought a downwards revision of 0.1ppt to 8.7%Y/Y, the equivalent data from Germany, France and Spain were unrevised from the flash estimates. This release will provide the granular detail, as well various measures of underlying price pressures closely followed by the Governing Council, including the Persistent and Common Component of Inflation (PCCI) and trimmed mean HICP rates. Wednesday will also bring the latest euro area new car registrations figures for April.

UK

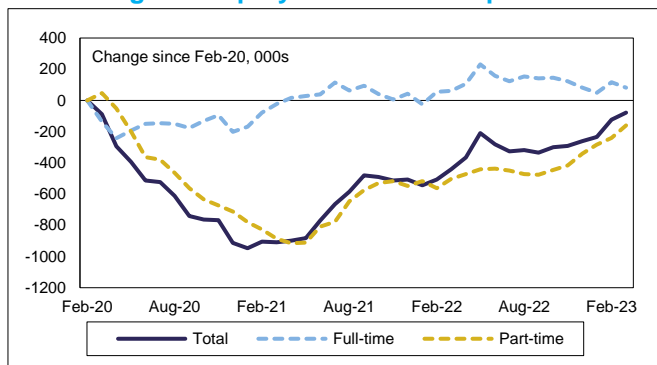
Evidence of a further loosening of UK labour market conditions

Consistent with recent surveys, today's UK data suggested a further loosening of the labour market. Within the detail pointing to a softening of conditions, the number of payrolled employees fell (-136k) in April for the first time since February 2021. While these figures are often significantly revised, we note that the direction of revision is usually down, perhaps underscoring the weakness of this latest reading. And while employment on the ILO measure rose in the three months to March (+182k), this once again reflected a pickup in part-time and self-employed positions, with the number of full-time workers declining on the quarter. Encouragingly for the BoE, the economic inactivity rate – whose rise throughout the pandemic has been a notable structural weakness for the UK economy – fell 0.4ppt on the quarter in Q1. Admittedly, that fall in inactivity was largely driven by young people leaving education, while the number inactive due to long-term sickness rose again to a new record high of 2.55mn. But with higher participation overall, the unemployment rate edged up 0.1ppt in Q1 to 3.9%, back in line with the rate at the start of 2020 ahead of the pandemic. And the number of vacancies fell for the tenth consecutive period in the three months to April, by 55k or almost 5% to the lowest level since August 2021, to push the ratio of jobless workers-to-vacancies up 0.1ppt to 1.2. But while total vacancies were down 214k from a year earlier, they were still 282k above the pre-pandemic level.

Private sector wage growth momentum probably still too high for the BoE's comfort

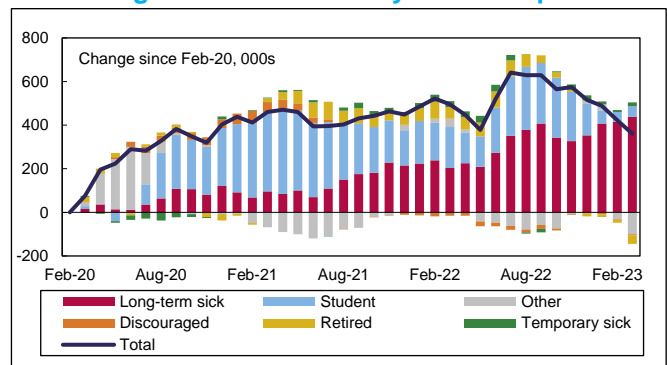
Less encouraging for the BoE, underlying pay growth failed to show convincing signs of significant cooling. While average total pay (including bonuses) was down 0.2ppt on the quarter at 5.8%3M/Y in the three months to March, growth in regular pay (excluding bonuses) was unchanged on the quarter at 6.7%3M/Y. Admittedly, in the private sector, total pay growth was down 0.6ppt on the quarter at 5.9%3M/Y, with regular pay growth down 0.3ppt at 7.0%3M/Y. In contrast, regular pay growth

UK: Change in employment since the pandemic



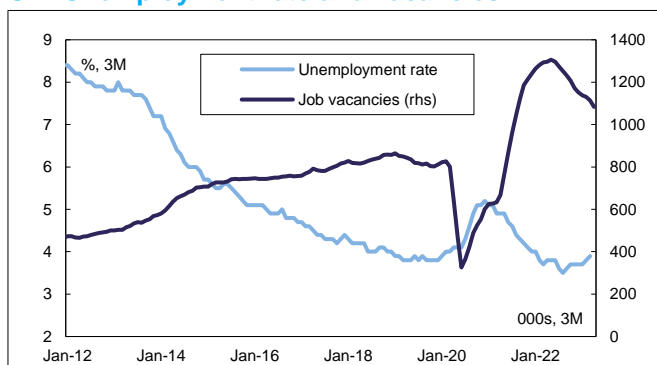
Source: Refinitiv and Daiwa Capital Markets Europe Ltd.

UK: Change in labour inactivity since the pandemic



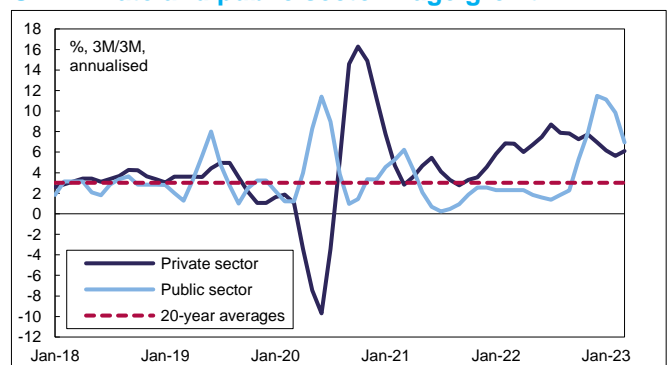
Source: Refinitiv and Daiwa Capital Markets Europe Ltd.

UK: Unemployment rate and vacancies



Source: Refinitiv and Daiwa Capital Markets Europe Ltd.

UK: Private and public sector wage growth














Source: Refinitiv and Daiwa Capital Markets Europe Ltd.

in the public sector leapt 1.3ppts to 5.6%3M/Y, the strongest in almost two decades, as the number of working days lost to strikes was more than double that in February and the most since late-2011. Looking at recent momentum, private sector total pay rose 0.2ppt on the quarter to 1.6%3M/3M. And while it cooled a little further, private regular pay growth was down 0.2ppt on the quarter to 1.5%3M/3M (i.e. about 6% on an annualised basis), to be still perhaps roughly double the required rate to be compatible with achievement of the inflation target over the medium term. Of course, given higher inflation, in real terms, growth in total and regular pay was exceptionally weak, at -3.0%3M/Y for total pay and -2.0%3M/Y for regular pay, and so consistent with still-soft household spending momentum. While there will be one more labour market report published before the BoE's rate-setting decision next month, overall today's pay figures were probably strong enough to prompt a further 25bps rate hike.

The day ahead in the UK

On a day bereft of top-tier UK economic data tomorrow, focus will turn to BoE Governor Bailey's keynote speech at the BCC annual conference for further insights into the near-term monetary policy outlook.




European calendar

Today's results						
Economic data						
Country	Release	Period	Actual	Market consensus/ <i>Daiwa forecast</i>	Previous	Revised
Euro area	 GDP – second estimate Q/Q% (Y/Y%)	Q1	0.1 (1.3)	<u>0.1 (1.3)</u>	-0.1 (1.8)	-
	 Trade balance €bn	Mar	17.0	-	-0.1	-0.2
	 Employment Q/Q% (Y/Y%)	Q1	0.6 (1.7)	-	0.3 (1.5)	-
Germany	 ZEW current assessment (expectations) balance	May	-34.8 (-10.7)	-38.0 (-6.0)	-32.5 (4.1)	-
Italy	 Final HICP (CPI) Y/Y%	Apr	8.7 (8.2)	<u>8.8 (8.3)</u>	8.1 (7.6)	-
UK	 Payrolled employees, monthly change '000s	Apr	-136	25	31	42
	 Unemployment claimant count rate % (change '000s)	Apr	4.0 (46.7)	-	3.9 (28.2)	-(26.5)
	 Average weekly earnings (excluding bonuses) 3M/Y%	Mar	5.8 (6.7)	5.8 (6.8)	5.9 (6.6)	5.8 (-)
	 ILO unemployment rate %	Mar	3.9	3.8	3.8	-
	 Employment change Q/Q, '000s	Mar	182	160	169	-
	 Preliminary output per hour Y/Y%	Q1	-0.6	-	0.0	-
Auctions						
Country	Auction	- Nothing to report -				





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 	07.00	EU27 new car registrations Y/Y%	Apr	-	28.8
	10.00	Final HICP (core HICP) Y/Y%	Apr	<u>7.0 (5.6)</u>	6.9 (5.7)
France 	06.30	ILO unemployment rate %	Q1	7.0	7.0
Italy 	09.00	Trade balance €bn	Mar	-	2.1

Auctions and events

Euro area 	16.50	ECB's de Guindos scheduled to give speech on 'Navigating the wave of inflation'			
Germany 	10.30	Auction: €4bn of 2.30% 2033 bonds			
France 	09.50	Auction: 2.5% 2026 bonds			
	09.50	Auction: 1% 2027 bonds			
	09.50	Auction: 2.75% 2029 bonds			
	10.50	Auction: 0.1% 2029 index-linked bonds			
	10.50	Auction: 0.1% 2036 index-linked bonds			
	10.50	Auction: 0.1% 2053 index-linked bonds			
UK 	10.00	Auction: £3.75bn of 4.125% 2027 bonds			
	10.50	BoE Governor Bailey to give keynote speech at the British Chambers of Commerce global annual conference			

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

Access our research blog at:

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

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