

Euro wrap-up

Overview

- Despite a record monthly drop in euro area producer prices in April, Bunds made losses as the oil price increased following the announcement over the weekend that Saudi would cut oil production again in July.
- Gilts also made losses as the final services PMIs signalled ongoing solid expansion in May, but the price charged index was revised slightly lower.
- Tomorrow will bring euro area retail sales and German factory orders figures for April, as well as European construction PMIs and a UK retail survey for May.

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Daily bond market movements

Bond	Yield	Change
BKO 2.8 12/25	2.863	+0.074
OBL 2.2 04/28	2.396	+0.062
DBR 2.3 02/33	2.373	+0.063
UKT 0% 06/25	4.444	+0.087
UKT 1% 10/28	4.167	+0.067
UKT 3¼ 01/33	4.208	+0.055

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

Source: Bloomberg

Euro area

Euro area producer price inflation falls sharply

After the downside surprise to last Thursday's flash [euro area CPI](#) estimate, today's euro area PPI inflation numbers reported a further marked easing in goods price pressures, with producer prices down for the fourth consecutive month in April and by the steepest monthly drop (-3.2%M/M) on the series. This took the annual inflation rate down to a 27-month low of 1.0%Y/Y, 42ppts below last August's peak and below the long-run average (2.8%). Once again, the downwards impulse largely reflected energy prices – which fell a record 10.1%M/M to take the cumulative decline since September to 30% – for which the annual rate of that component returned to negative territory for the first time since the start of 2021 (-8.9%Y/Y) and was 126ppts below August's peak. But the downwards trend in intermediate prices also accelerated in April, recording the joint-steepest monthly decline (-0.6%M/M) in three years, to take the annual rate (1.2%Y/Y) to the lowest since January 2021. While capital goods prices picked up in April, the annual rate (6.1%Y/Y) still maintained a downwards path to its lowest in fourteen months. And with food prices having taken a further step down, consumer non-durable goods inflation moderated to a thirteen-month low (down 2.7ppts to 10.8%Y/Y), while consumer durable goods inflation fell a further 0.9ppt to 7.3%Y/Y, not least thanks to a further easing in supply constraints. Indeed, when excluding energy, producer price inflation fell 3ppts to 5.1%Y/Y, the lowest in almost two years and some 11ppts below last year's peak.

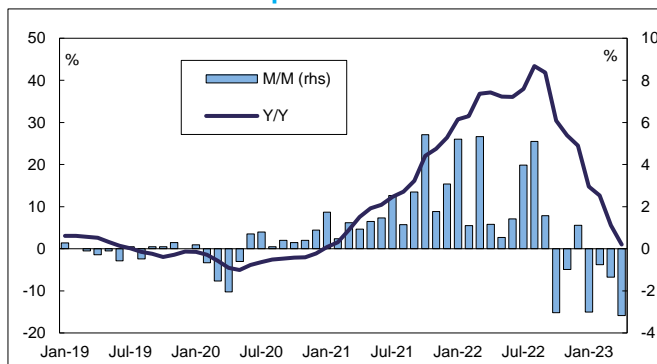
Factory prices should maintain downwards trend, but services price PMIs remain elevated

Given diminishing supplier pricing power amid weakening demand and lower energy costs, the manufacturing PMIs also signalled the steepest decline in euro area factory input prices since the start of 2016, with the index in May almost 15ppts below the pre-pandemic average. This survey also implied the first decline in factory output prices since September 2020. So, we expect producer prices to fall further over coming months and while the pass through will come with a lag, consumer goods inflation should continue to moderate further too. The outlook for services inflation, however, remains less favourable. While the final services PMIs today suggested that the increase in operating costs was the softest since August 2021, the input price index (64.4) was still roughly 8ppts above the pre-pandemic average. Moreover, the services output price PMI (59.1) ticked slightly higher in May to be more than 9ppts above the long-run average, suggesting that solid demand continues to enable services firms to pass on costs to consumers, which will remain a source of concern for the ECB.

Final services PMIs consistent with expansion, but sentix sentiment indices markedly weaker

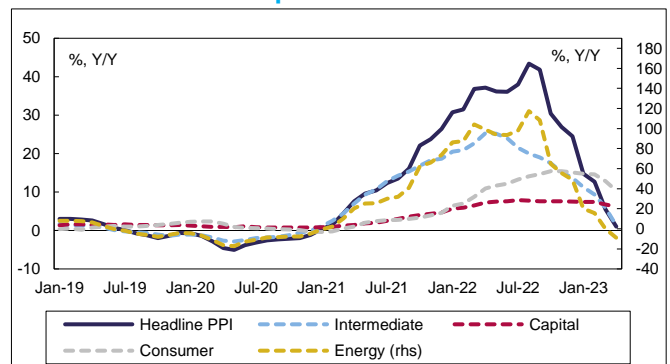
Admittedly, the final May services activity PMI was revised 0.8pt lower from the flash estimate to leave it down more than 1pt from April. But at 55.1 it remained consistent with solid expansion in the sector, with the average level for Q2 so far some

Euro area: Producer price inflation



Source: Refinitiv and Daiwa Capital Markets Europe Ltd.

Euro area: Producer price inflation



Source: Refinitiv and Daiwa Capital Markets Europe Ltd.

2.8pts above the Q1 average. With the manufacturing survey suggesting a steeper pace of contraction in May (46.4), the drop in the euro area's composite PMI was more pronounced, down 1.3pts to 52.8. But this was still the third-highest reading in the past year, leaving the average for the first two months of Q2 (53.5) some 1.5pts above the Q1 average and a level that, before the pandemic, would have been consistent with relatively firm GDP growth of roughly 0.4%Q/Q. Perhaps surprisingly given the weakness in the manufacturing sector, Germany's composite PMI held up relatively well in May, to leave the average so far in Q2 (54.1) some 3pts above the Q1. This contrasts markedly with a further slowing in the pace of expansion in France, where the composite PMI so far in Q2 (51.8) is suggestive of only modest growth. Today's PMIs also reported a notable moderation in Italy's composite measure in May, by more than 3pts to 52.0, due to weaker services and manufacturing output. Admittedly, this still left the average so far in Q2 (53.7) above the Q1 level, but still lagging implied growth in Spain, where the composite PMI is averaging some 55.8 so far in Q2. Of course, the results of the PMI surveys remain at odds with the loss of momentum implied by the [Commission's economic surveys](#). And today's sentix investor survey pointed to a further deterioration in sentiment at the start of June, with the current situation balance declining 7.8pts to a five-month low of -15.8, a level that sentix considers to be consistent with recession, while flagging Germany's economy as a key weakness.

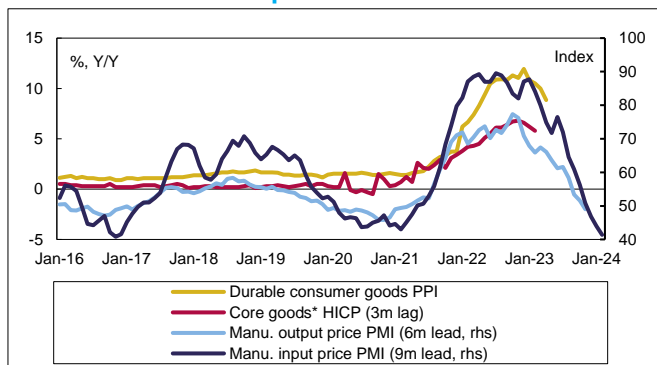
German trade surplus widens as exports beat expectations, but auto firms more downbeat

In terms of the latest German dataflow, today's goods trade figures for April beat expectations. These reported an unexpected improvement in the nominal trade surplus at the start of the second quarter, which rose €3.5bn to €18.4bn, the highest since the start of 2021. This partly reflected a pickup in the value of exports (1.2%M/M) that month, due to a strong increase to other euro area member states (4½%M/M), which helped offset a near-2½%M/M decline in exports to non-EU countries. Of course, given the near-6% plunge in March, the value of exports was still some 1½% below the Q1 average. There was also a further downwards adjustment in the value of imports, which fell for the seventh month out of the past eight, by 1.7%M/M to the lowest level since January 2022. While developments in import prices (-1.7%M/M) suggest that import volumes moved broadly sideways in April, there is likely to be some negative carry over from the sharp drop in March, which should provide some support to GDP growth at the start of Q2. Today's car production figures were also more encouraging, with output up a further 24%Y/Y, while registrations rose 19%Y/Y. Of course, this still remains well below pre-pandemic norms. And while a ifo survey published today suggested that the auto sector remains relatively positive about the current business situation, they were increasingly pessimistic about the outlook over the months ahead.

The day ahead in the euro area

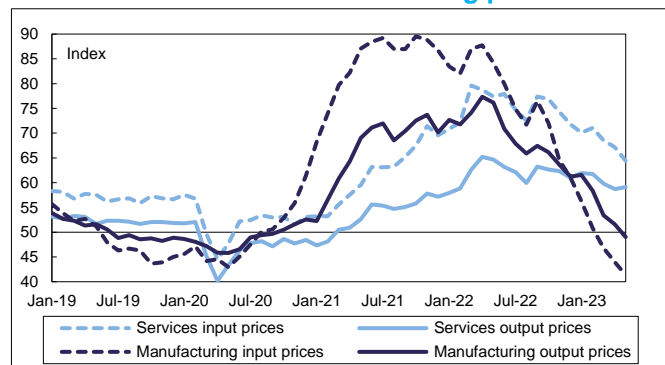
Tomorrow will bring euro area retail sales figures for April. Notwithstanding another solid increase in Irish retail sales, national results have largely come in on the soft side at the start of Q2, with only modest increases in [Germany](#) and Spain and a sharp drop in [French consumer spending](#). As such, sales are likely to have posted only modest growth in April, insufficient to reverse the drop in March (-1.2%M/M). German factory orders data seem bound to report a pickup in April following the

Euro area: Producer price indices



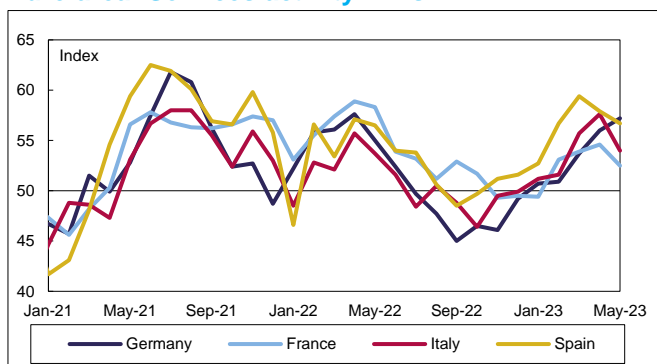
*Non-energy industrial goods. Source: Refinitiv, S&P Global and Daiwa Capital Markets Europe Ltd.

Euro area: Services & manufacturing price PMIs



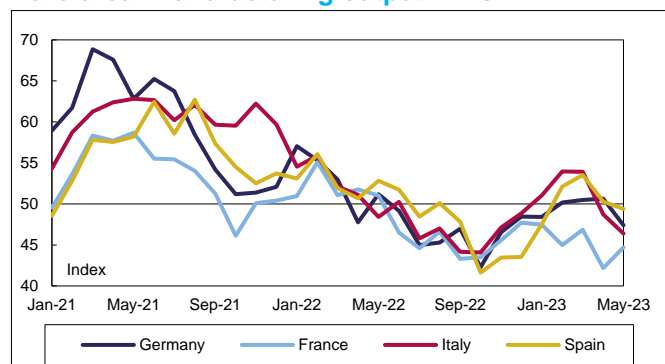
Source: Refinitiv, S&P Global and Daiwa Capital Markets Europe Ltd.

Euro area: Services activity PMIs



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

Euro area: Manufacturing output PMIs



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

plunge recorded in March (-10.7%M/M), albeit still implying lacklustre demand in the manufacturing sector, while the latest construction PMIs are likely to signal contraction in the sector in May. Meanwhile, the ECB will also study the findings of its own consumer expectations survey, which will provide an update on inflation expectations in April.

UK

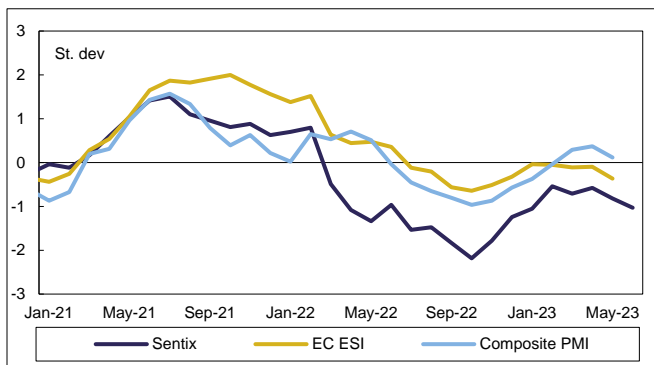
Services PMIs signals ongoing expansion, but a welcome downwards revision to the price indices

Like in the euro area, the final UK services PMIs for May were consistent with a respectable pace of economic expansion, despite easing on the month. In particular, the headline activity index of 55.2 was still the second-strongest reading of the past thirteen months, to leave it trending almost 4pts above the Q1 average, supported by strong growth in consumer-facing industries such as travel, leisure and hospitality. So, despite ongoing contraction in the manufacturing sector (47.7), the composite (54.0) was similarly the second-strongest since March 2022 and on average so far in Q2 (54.5) some 3pts above the Q1 average and a level that, before the pandemic, would have been consistent with GDP growth of 0.3%Q/Q or more this quarter. In terms of those indicators of greatest relevance to near-term BoE decision-making, the final PMIs provided a welcome downward revision to the services prices charged index, by 1.4pts to 60.5, the second-lowest reading in 21 months. However, this was still roughly 9pts above the pre-pandemic average and on the whole consistent with persisting inflationary pressures in the sector.

The day ahead in the UK

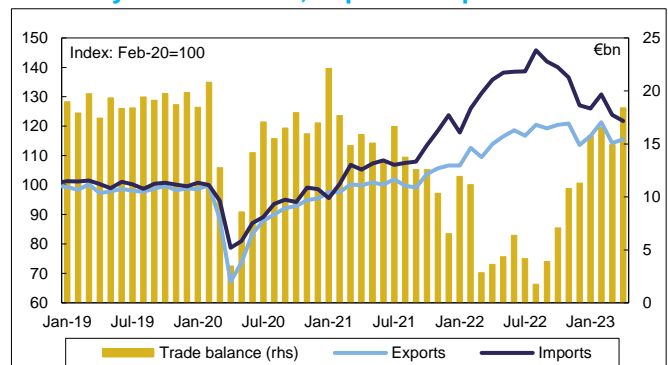
Of course, the composite PMIs fail to capture developments in both the retail and construction sectors, for which tomorrow's releases will provide some update. In particular, the BRC retail sales monitor for May is likely to tally with the findings from the CBI's distributive trades survey that suggested conditions were more challenging on the High Street reflecting not least the extra national holiday for the King's coronation. Meanwhile, the construction PMI is likely to point to a further slowdown in activity in May, with the housing component likely to remain firmly in contractionary territory.

Euro area: Economic sentiment indices



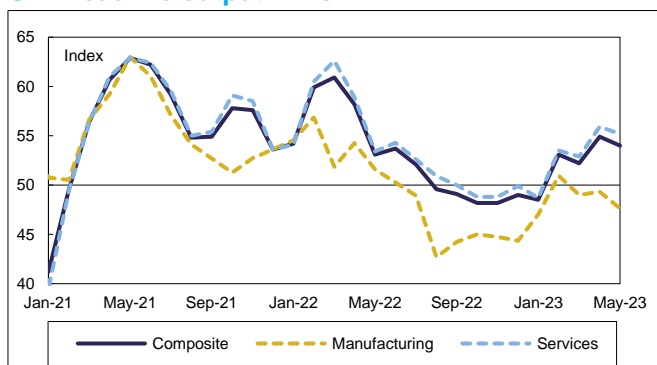
Source: Refinitiv, S&P Global and Daiwa Capital Markets Europe Ltd.

Germany: Goods trade, export & imports*



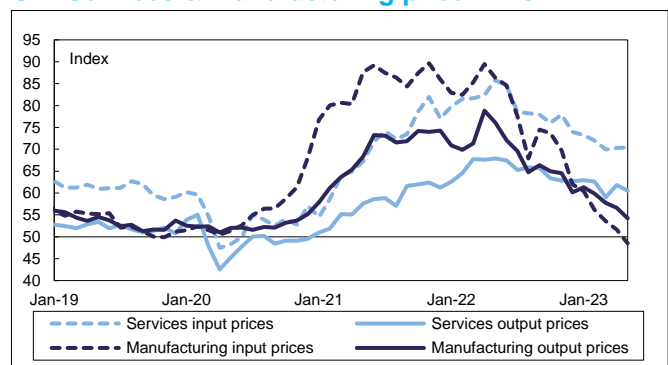
*Nominal figures. Source: Refinitiv and Daiwa Capital Markets Europe Ltd.

UK: Headline output PMIs



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

UK: Services & manufacturing price PMIs














Source: Refinitiv, S&P Global 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	 Final services (composite) PMI	May	55.1 (52.8)	<u>55.9 (53.3)</u>	56.2 (54.1)	-
	 Sentix investor confidence	Jun	-17.0	-15.1	-13.1	-
	 PPI Y/Y%	Apr	1.0	1.7	5.9	5.5
Germany	 Trade balance €bn	Apr	18.4	16.0	16.7	14.9
	 Final services (composite) PMI	May	57.2 (53.9)	<u>57.8 (54.3)</u>	56.0 (54.2)	-
	 New car registrations (production) Y/Y%	May	19.2 (24.0)	-	12.6 (25.5)	-
France	 Final services (composite) PMI	May	52.5 (51.2)	<u>52.8 (51.4)</u>	54.6 (52.4)	-
Italy	 Final services (composite) PMI	May	54.0 (52.0)	-	57.6 (55.3)	-
Spain	 Final services (composite) PMI	May	56.7 (55.2)	-	57.9 (56.3)	-
UK	 Final services (composite) PMI	May	55.2 (54.0)	<u>55.1 (53.9)</u>	55.9 (54.9)	-
	 New car registrations Y/Y%	May	16.7	-	11.6	-










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	 08.30	Construction PMI	May	-	45.2
	 10.00	Retail sales M/M% (Y/Y%)	Apr	0.2 (-3.0)	-1.2 (-3.8)
Germany	 07.00	Factory orders M/M% (Y/Y%)	Apr	2.8 (-8.6)	-10.7 (-11.0)
	 08.30	Construction PMI	May	-	42.0
France	 08.30	Construction PMI	May	-	46.0
Italy	 08.30	Construction PMI	May	-	49.0
Spain	 08.00	Industrial production M/M% (Y/Y%)	Apr	-0.5 (1.9)	1.5 (4.5)
UK	 00.01	BRC retail sales monitor, like-for-like sales Y/Y%	May	5.2	5.2
	 09.30	Construction PMI	May	50.8	51.1

Auctions and events

Euro area	 09.00	ECB publishes its consumer expectations survey
Germany	 10.30	Auction: €400mn of 0.1% 2033 index-linked bonds
	 10.30	Auction: €200mn of 0.1% 2046 index-linked bonds
UK	 10.00	Auction: £2.5bn of 3.75% 2053 bonds

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

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