

Euro wrap-up

Overview

- Bunds made notable losses even as today's German industrial production data suggested a lack of momentum in the sector at the start of Q2.
- Gilts also followed the global trend lower on a quiet day for UK economic releases.
- Thursday will bring updated euro area Q1 GDP data, and May surveys on the UK's residential and labour markets.

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Daily bond market movements

Bond	Yield	Change
BKO 2.8 06/25	2.904	+0.089
OBL 2.2 04/28	2.455	+0.078
DBR 2.3 02/33	2.438	+0.071
UKT 0% 06/25	4.563	+0.084
UKT 1% 10/28	4.247	+0.064
UKT 3% 01/33	4.243	+0.037

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

Source: Bloomberg

Euro area

German IP ekes out modest growth in April, but fails to reverse drop in March

Like [retail sales](#) and [exports](#), German industrial production rose in April, but not sufficiently to reverse fully the drop in March. Given the sharp decline in [manufacturing turnover](#) reported yesterday, industrial production at the start of Q2 was slightly firmer than might have been feared, eking out a modest increase of 0.3%M/M in April. Moreover, the contraction in March was smaller than previously estimated, revised by 1.3ppts, albeit leaving industrial output still down a hefty 2.1%M/M that month. And given the strength in the first two months of the year, IP was still up a seemingly respectable 1.7%3M/3M. But, overall, today's report certainly suggested a lack of momentum in Germany's manufacturing sector in Q2. Much of the little growth reported in industry in April came from a rebound in construction (2.0%M/M), to leave it ½% above the Q1 average. In contrast, manufacturing output rose just 0.1%M/M, to leave it some 4.7% below the pre-pandemic level and 0.6% below the Q1 average. So, the figures flagged the risks of a decline over the second quarter as a whole following growth of more than 1½%Q/Q in Q1.

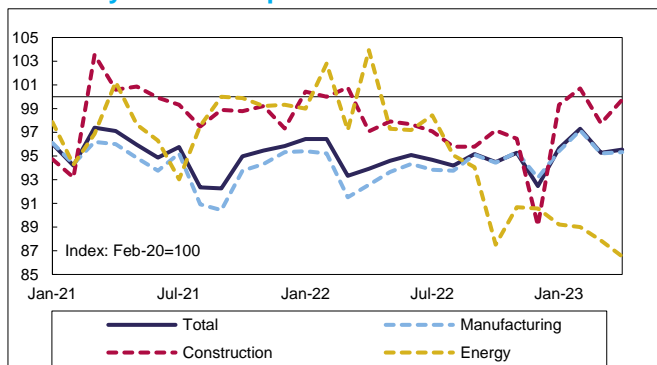
Structural adjustment in the energy-intensive subsector continues

In the absence of the first increase in production in the pharmaceutical sub-sector since December (6.4%M/M), manufacturing output would have contracted for a second successive month in April. Indeed, production of consumer durables fell more than 2%M/M in April. And output of capital goods fell for a second successive month (albeit by just 0.3%M/M). That reflected further declines in autos (-0.8%M/M) to some 8% below the pre-pandemic level, and machinery output (-0.5%M/M) to more than 2% below the pre-pandemic level and the lowest in eleven months. While those declines likely in part reflect payback for strength in earlier months, the structural adjustment in the energy-intensive sector appears to be a lasting phenomenon. Indeed, even as wholesale natural gas prices continued to fall, firms appear to have continued efforts to cut reliance on energy, with industrial gas usage down about 9%Y/Y in April. And so, production in energy-intensive subsectors also fell 1%M/M that month to the second-lowest level since the global financial crisis, to be down almost 13%Y/Y and more than 2% below the Q1 average. Within this category, production of glassware fell to its lowest level since February 2012, while chemicals production maintained a downwards trend to its second-lowest level since the start of 2009. And with manufacturers' gas usage still well below normal levels in May, output in these subsectors appears to have remained very subdued last month despite the further improvement in the terms of trade.

Outlook for the manufacturing sector remains subdued

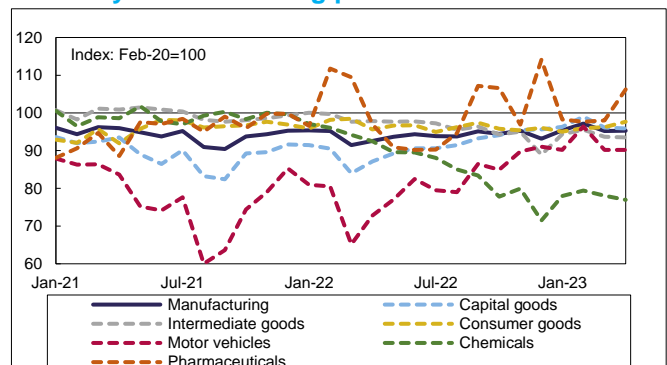
While the latest autos production figures have at least suggested renewed recovery in May as supply-chain strains eased again, a recent ifo institute auto sector report suggested that firms are increasingly pessimistic about the outlook amid

Germany: Industrial production



Source: Refinitiv and Daiwa Capital Markets Europe Ltd.

Germany: Manufacturing production



Source: Refinitiv and Daiwa Capital Markets Europe Ltd.

ongoing concerns about external demand. And so, while backlogs built up during the pandemic remain elevated, auto firms' production expectations for the coming three months were the lowest since April 2022, with the outlook for other sub-sectors generally less upbeat too. Truck-toll mileage maintained a downwards trend in May. And with order books on a steady downwards path but inventories the highest since the first wave of Covid-19, the near-term outlook for production remains subdued. So, while there should be some positive carry from recent developments in the services sector – where activity rose for the third consecutive month in March to be up 0.6%Q/Q in Q1 – there is a non-negligible risk of a further contraction in German GDP in Q2.

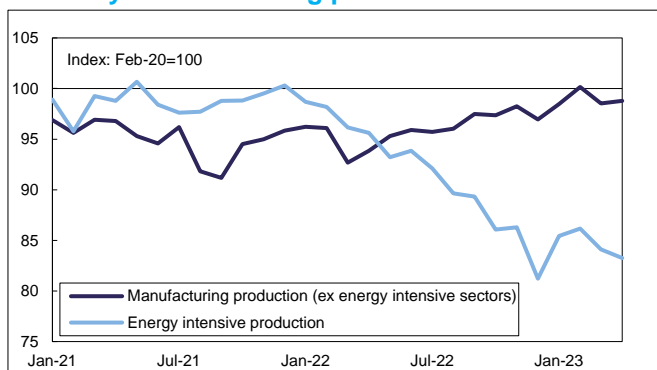
Surge in Irish IP strongly suggests firm growth in euro area production in April

As is often the case, volatility in Irish production was most extreme in April. Total output surged a whopping 21.5%M/M, with manufacturing up an even steeper 70.7%M/M, a series record, for which the so-called "modern sector", comprising chemicals, pharmaceuticals, and crucially ICT and electronic equipment, posted a huge increase of 81.3%M/M. This followed a substantial slump of 27%M/M in March, to leave total output still around 1% below the Q1 average. Taken together with positive growth in France, and in spite of declines in Spain (-1.8%M/M) and Portugal (-5.5%M/M), today's data strongly suggest that euro area industrial production posted solid growth in April, even if it doesn't fully reverse the near-4%M/M recorded in March.

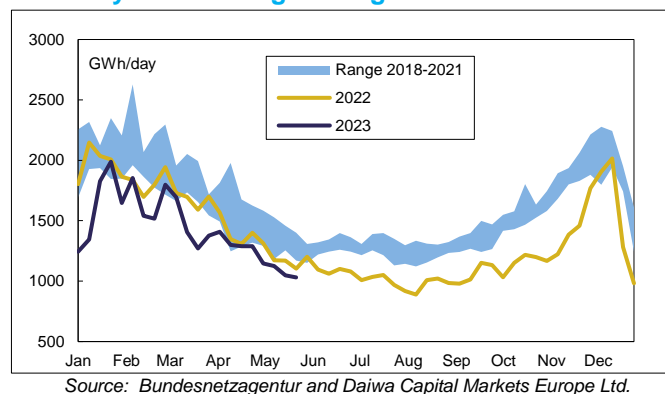
The day ahead in the euro area

Tomorrow will bring updated euro area Q1 GDP figures, which are highly likely to see the modest growth initially reported (+0.1%Q/Q) revised away. Indeed, given the downwards revision in Germany (-0.3%Q/Q), a substantial adjustment in Ireland (from -2.7%Q/Q to -4.6%Q/Q), and today's data reporting negative growth in Greece (-0.1%Q/Q), we now forecast aggregate euro area GDP to have contracted slightly, by 0.1%Q/Q, in Q1. The first expenditure breakdown will show that, despite another decent rise in employment (updated figures tomorrow should confirm growth of 0.6%Q/Q), household consumption contracted for a second successive quarter, while government consumption also fell. But modest contributions from fixed investment and net trade should have provided some offsets.

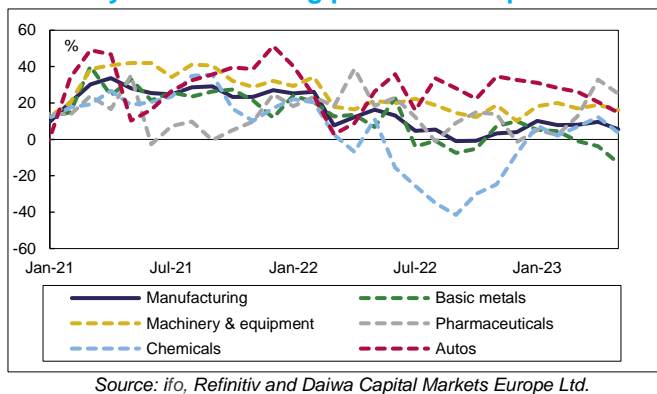
Germany: Manufacturing production



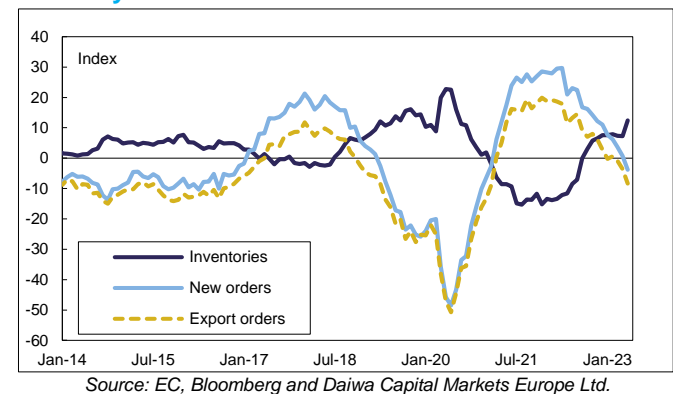
Germany: Industrial gas usage



Germany: Manufacturing production expectations



Germany: New orders and inventories

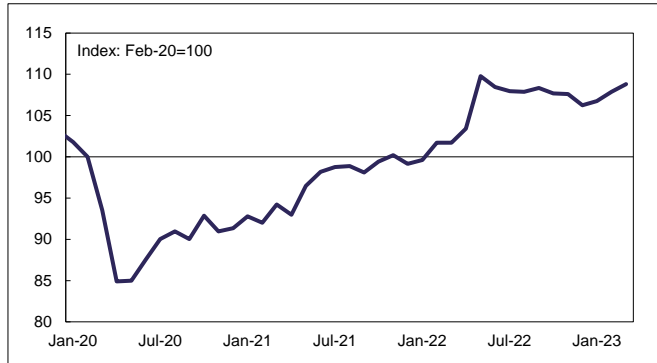


UK

The day ahead in the UK

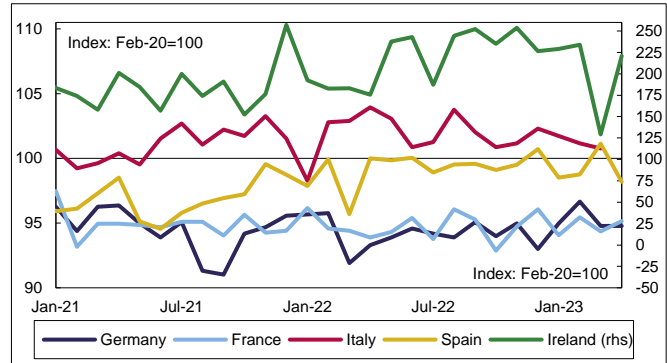
After a quiet day for UK economic news, tomorrow will bring the publication of the RICS residential survey for May. Given renewed increases in interest rates on mortgages, as well as last Friday's [weak mortgage lending](#) figures, we might expect to see an increase in the number of surveyors expecting house prices to fall further over coming months. The REC/KPMG report on jobs will also be watched for evidence of a further slowdown in the jobs market in May. As such, the survey's measure of starting salaries might well point to a further moderation in pay growth having ticked slightly higher in April.

Germany: Services activity



Source: Destatis and Daiwa Capital Markets Europe Ltd.

Euro area member states: Industrial production



Source: Refinitiv and Daiwa Capital Markets Europe Ltd.

European calendar

Today's results

Economic data

Country	Release	Period	Actual	Market consensus/ Daiwa forecast	Previous	Revised
Germany	Industrial production M/M% (Y/Y%)	Apr	0.3 (1.6)	0.6 (1.6)	-3.4 (1.8)	-2.1 (2.3)
France	Trade balance €bn	Apr	-9.7	-7.7	-8.0	-8.4
Italy	Retail sales M/M% (Y/Y%)	Apr	0.2 (3.2)	-	0.0 (5.8)	-
Spain	House price index Q/Q% (Y/Y%)	Q1	0.6 (3.5)	-	-0.8 (5.5)	-

Auctions

Country	Auction
Germany	sold €936mn of 0% 2025 green bonds at an average yield of 2.66%
UK	sold £4bn of 3.5% 2025 bonds at an average yield of 4.874%

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

Tomorrow's releases

Economic data

Country	BST	Release	Period	Market consensus/ Daiwa forecast	Previous
Euro area		10.00 GDP – second estimate Q/Q% (Y/Y%)	Q1	<u>-0.1 (1.2)</u>	-0.1 (1.8)
		10.00 Final employment Q/Q% (Y/Y%)	Q1	<u>0.6 (1.7)</u>	0.3 (1.5)
UK		00.01 RICS house price balance %	May	-39	-39

Auctions and events

UK		00.01 REC/KPMG report on jobs
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Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

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