

Euro wrap-up

Overview

- While Spanish inflation exceeded expectations and euro area unemployment fell to a new series low, Bunds followed USTs higher.
- Gilts followed the global trend higher on a quiet day for UK economic news.
- Friday will bring euro area flash May inflation estimates, April retail spending figures from Germany and France and updated Italian Q1 GDP data.

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Daily bond market movements

Bond	Yield	Change
BKO 2.9 06/26	3.073	-0.021
OBL 2.1 04/29	2.691	-0.025
DBR 2.2 02/34	2.654	-0.034
UKT 0% 01/26	4.443	-0.093
UKT 0½ 01/29	4.236	-0.055
UKT 4% 01/34	4.351	-0.048

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

Euro area

Inflation accelerates in May in Spain and Ireland and remains elevated in Belgium

Like yesterday's [German](#) figures, the flash estimates of Spanish inflation in May came in a touch above expectations, with the EU-harmonised measure up 0.4ppt to a 13-month high of 3.8%Y/Y, 0.1ppt above the Bloomberg consensus. The national CPI measure was up 0.3ppt to 3.6%Y/Y, the highest since February 2023. But Spain's statistical office indicated that the pickup principally reflected a rise in electricity prices due to the final withdrawal of government energy support, while base effects related to a smaller decline in petrol prices compared with a year ago also pushed energy inflation higher. The increase in Ireland's headline HICP rate, by 0.3ppt to a three-month high of 1.9%Y/Y, was also related to a lesser drag from energy prices (+2.7ppts to -3.6%Y/Y). And having jumped in April to a 13-month high of 4.9%Y/Y as the country's energy support package concluded, Belgian HICP inflation moved sideways.

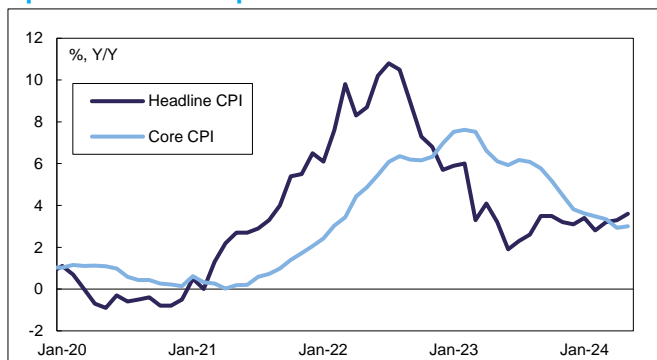
But underlying price pressures remain subdued

When excluding energy and fresh foods, underlying price pressures appear to have been better behaved this month. Certainly, the Spanish core CPI rate only ticked marginally higher – by 0.1ppt to 3.0%Y/Y – for the first month in ten, to leave it still more than 4½ppts below last year's peak. Meanwhile, core inflation maintained a downwards trend in Belgium (-0.5ppt to 2.8%Y/Y, the lowest since December 2021) and Ireland (-0.1ppt to 2.5%Y/Y, the lowest since August 2021). So, while much will depend on developments in France and Italy – for which the equivalent data are also due tomorrow – we maintain our forecast that the euro area headline HICP rate likely ticked higher in May, probably by 0.2ppt to 2.6%Y/Y, but also that core inflation likely moved sideways at 2.7%Y/Y. And although that would leave both headline and core HICP rates on track to be a touch firmer than the ECB's previous projections in March, it would also be no obstacle to a 25bps rate cut next week.

ESIs confirm improvement in consumer confidence but business sentiment softens from Q1

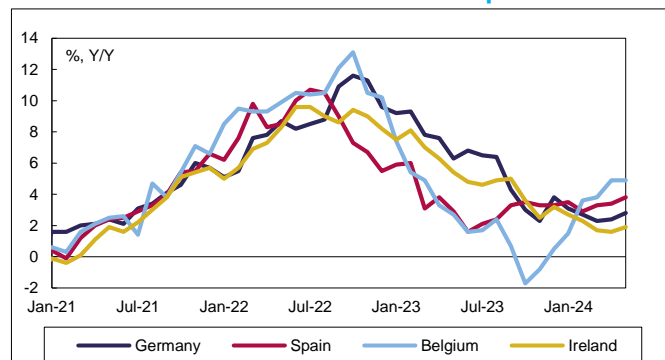
While last week's [flash euro area PMIs](#) for May beat expectations to suggest another quarter of GDP growth at the 0.3%Q/Q rate of Q1, today's Commission survey results were arguably consistent with a slightly softer pace of expansion in Q2. Broadly in line with expectations, the Commission's headline Economic Sentiment Indicator (ESI) for the euro area rose 0.4ppt in May to 96. That was still 4% below the long-run average and about 10% below the pre-pandemic mean, and left the Q2 average 0.2% below the Q1 level. The improvement in consumer confidence to the highest level since the Russian invasion of Ukraine, which had been flagged by the flash estimate, was confirmed, leaving it trending well above the Q1 level. Households were more upbeat about their own finances and the economic outlook, and signalled the greatest

Spain: Consumer price inflation*



*National measure. Source: Macrobond and Daiwa Capital Markets Europe Ltd.

Euro area member states: Consumer price inflation*



*EU-harmonised measure. Source: Macrobond and Daiwa Capital Markets Europe Ltd.

willingness to spend in more than two years. But business sentiment remained firmly below the first-quarter average. While firms in services and manufacturing were more upbeat than last month, their respective ESIs were still trending down from Q1 and firmly below the respective long-run averages. Despite a slight improvement in orders, firms in industry revised down their production expectations while services judged that the outlook for demand was not quite as strong as it appeared last quarter. In addition, retail sentiment was steady below the Q1 average as firms reported a weakening of orders, and construction firms were more downbeat.

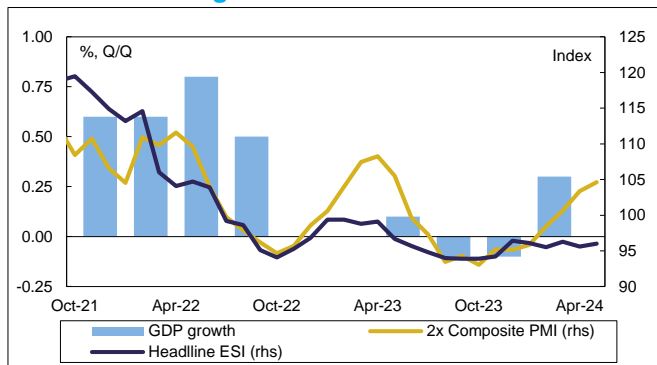
German sentiment improves to an 11-month high but French indicator trending below Q1 level

Among the large member states, the German ESI rose to an 11-month high while the Dutch index reached the highest in almost two years near its long-run mean, with the respective averages in Q2 so far trending well above their Q1 levels. Nevertheless, the German ESI remained more than 7½% below its long-run average, unsurprisingly suggesting that chronic economic challenges in the euro area's largest member state persist despite the recent positive turnaround in growth momentum. Moreover, while it rose 1.5pts on the month and was still above the subdued range of the second half of last year, the French ESI was still trending 3½% below the long-run average and almost 2½% below the Q1 level, echoing the message from the flash PMIs to indicate a softening of GDP growth in Q2 from 0.2%Q/Q last quarter. The equivalent Italian index was also up from April but down on the first quarter, albeit in line with the long-run average to suggest modest expansion in Q2. In contrast, while it fell more than 3pts in May, the Spanish ESI was still 1.1% above the long-run average and trending above the Q1 level to indicate another quarter of firm expansion after bumper growth of 0.7%Q/Q at the start of the year.

Price indices suggest moderating persisting in services but end to disinflationary trend for goods

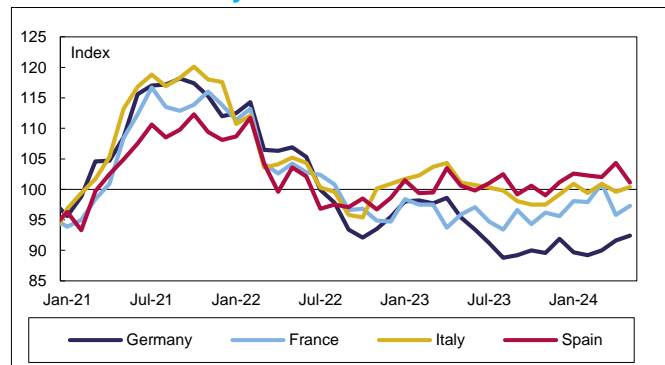
Like its signals on economic growth in the euro area, the Commission survey gave mixed messages on price expectations in the middle of Q2. The survey measure of 12-month consumer inflation expectations picked up to a three-month high above the range in the second half of last year. But it was still a little below the pre-pandemic average to be arguably broadly consistent with the ECB's target. Encouragingly, the indicators of selling-price expectations three months ahead in services and retail fell for a fourth successive month, pointing to a further gradual easing of pressures. But they were still well above the respective long-run averages to point to a degree of ongoing inflation persistence. And while they remained below the long-run mean, three-month selling-price expectations in industry rose to a 13-month high suggesting that the disinflationary trend in the producer goods sector might well now be at an end.

Euro area: GDP growth & sentiment indices



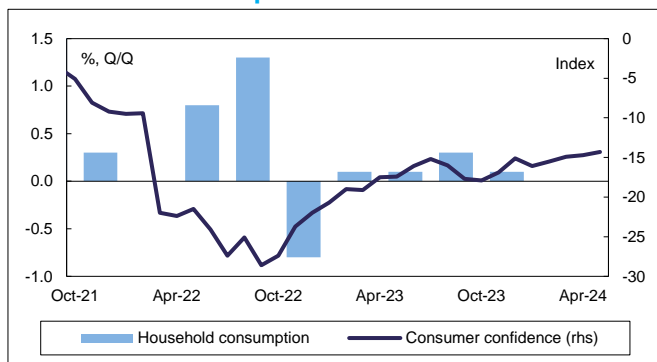
Source: Macrobond, EC, S&P Global and Daiwa Capital Markets Europe Ltd.

Euro area: ESIs by member state



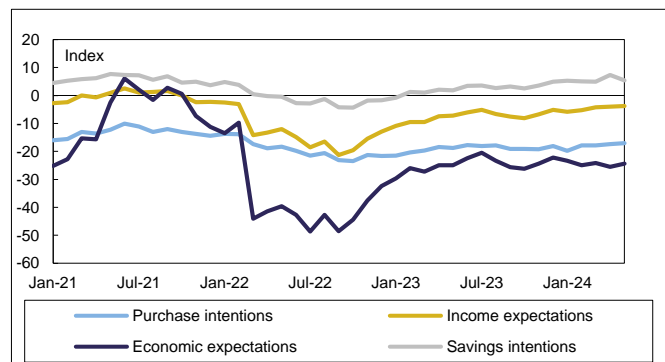
Source: Macrobond, EC and Daiwa Capital Markets Europe Ltd.

Euro area: Consumption & consumer sentiment



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

Euro area: Consumer sentiment indices



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

Unemployment rate falls to new record low in April

With economic output having returned to positive growth in Q1 and surveys signalling ongoing expansion in Q2, today's labour market figures for April reported a second successive monthly decline in the number of people unemployed, by 100k to just below 11.0mn for the first time. As a result, the jobless rate fell for the first month in five, by 0.1ppt to a new series low of 6.4%. That arguably points to a further reduction in labour market slack, which according to Eurostat's estimate narrowed at the end of 2023 to a record low of 12.4%. The decline in joblessness in April was again led by Italy, where it fell a further 55k in April to take the cumulative drop over the past six months to 190k and the unemployment rate down to 6.9%, the lowest since December 2008. The French unemployment rate also fell to a 12-month low of 7.3%, with the Portuguese rate down to an eight-month low of 6.3%. Meanwhile, jobless rates in Germany (3.2%) and Spain (11.7%) moved sideways, with the former just 0.3ppt above the series low and the latter the softest since the global financial crisis.

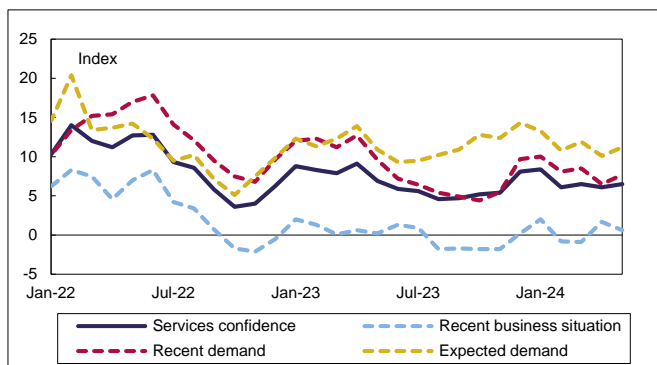
But some signs that labour market is becoming less tight

The extent of labour market tightness in part reflects firms' decisions over recent quarters to hoard labour in anticipation of a recovery in demand. But according to today's Commission survey results, the share of hoarding firms fell to its lowest in thirteen months in May, back in line with the long-run average. Other indicators also suggest that employment growth is set to cool over the near term. For example, the [job vacancy rate](#) declined in Q1 to the lowest since Q321. And today's Commission survey also suggested that hiring intentions have steadily fallen back, with the respective indicator down in May to the lowest for more than three years. So, while the hawks on the Governing Council might continue to flag concerns about labour market tightness to push back on successive interest rate cuts, there are signs that the balance between labour supply and demand is becoming better balanced.

The day ahead in the euro area

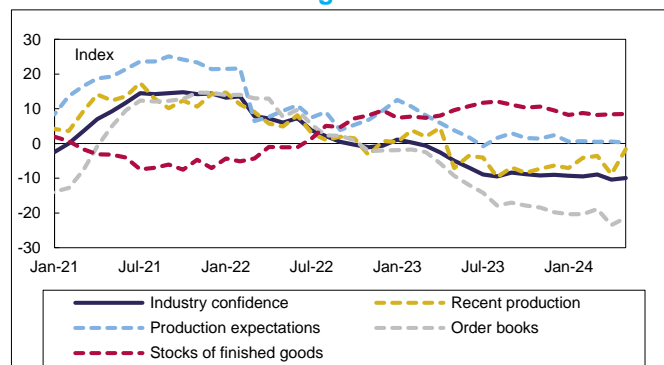
The main focus in the euro area on Friday will be the aforementioned flash estimates of May inflation. Having fallen over the first few months to 2.4%Y/Y in March, the headline HICP rate was unchanged at that level in April. And we expect it to pick back up in May to 2.6%Y/Y, which would point to a slight overshoot of the ECB's projection for Q2. However, the increase would in part be related to unfavourable base effects associated with the introduction of the subsidized Deutschland public transport ticket in May 2023 and withdrawal of energy support measures in Spain. Despite a fall in prices of auto fuel and heating oil this month, energy inflation is likely to rise back into positive territory for the first time since April 2023. And not least due to a fall in prices a year ago, we expect no decline in food inflation either. Among core items, goods inflation should

Euro area: Services sentiment indices



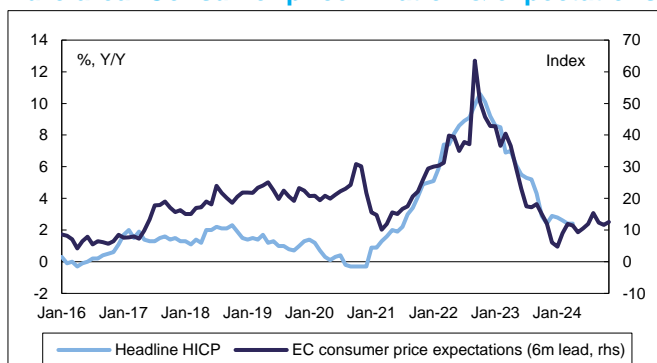
Source: Macrobond, EC and Daiwa Capital Markets Europe Ltd.

Euro area: Manufacturing sentiment indices



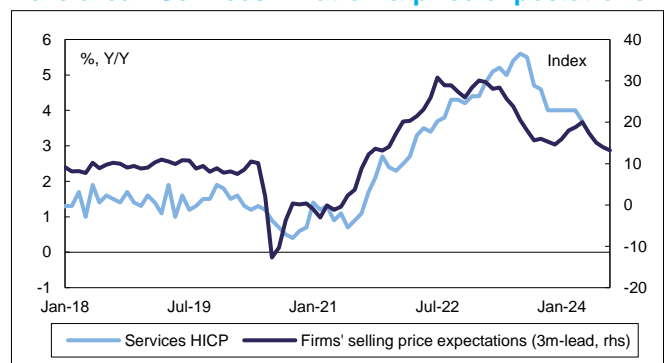
Source: Macrobond, EC and Daiwa Capital Markets Europe Ltd.

Euro area: Consumer price inflation & expectations*



*Twelve-months ahead. Source: Macrobond, EC and Daiwa Capital Markets Europe Ltd.

Euro area: Services inflation & price expectations*



*Three months ahead. Source: Macrobond, EC and Daiwa Capital Markets Europe Ltd.

ease a touch further to the lowest since mid-2021. However, services inflation is likely to rise. As such, we currently expect core inflation to be unchanged at 2.7%Y/Y.

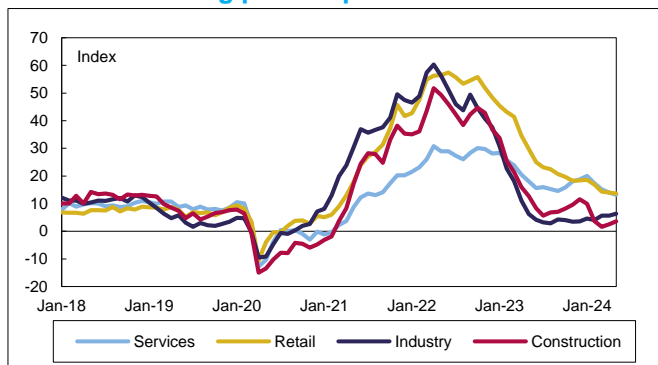
In addition to the inflation data, Friday will also bring German retail sales and French consumer spending numbers for April, along with updated Italian GDP figures for Q1 which will include an official expenditure breakdown for the first time.

UK

The day ahead in the UK

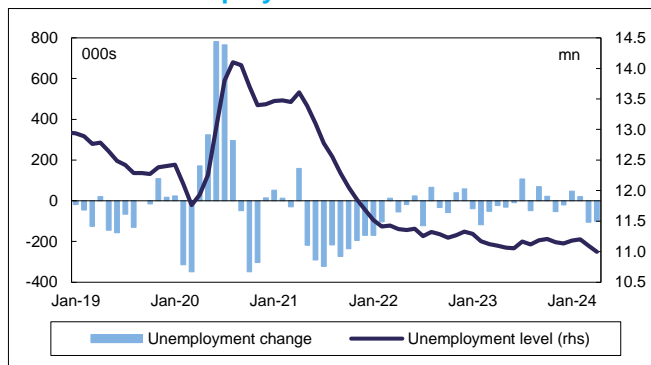
After another day bereft of top-tier economic data, Friday will bring the BoE's monetary figures for April, which are expected to report a pickup in mortgage approvals in April to a two-year high. Growth in consumer credit is likely to remain firm close to 9%Y/Y. The Nationwide house price report for May is also scheduled for release.

Euro area: Selling price expectations*



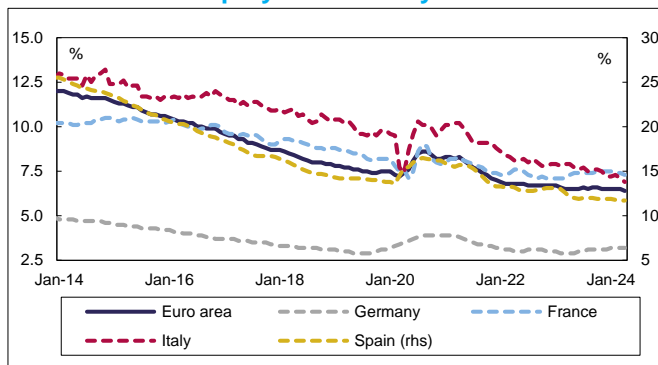
*Three-months ahead. Source: Macrobond, EC and Daiwa Capital Markets Europe Ltd.

Euro area: Unemployment



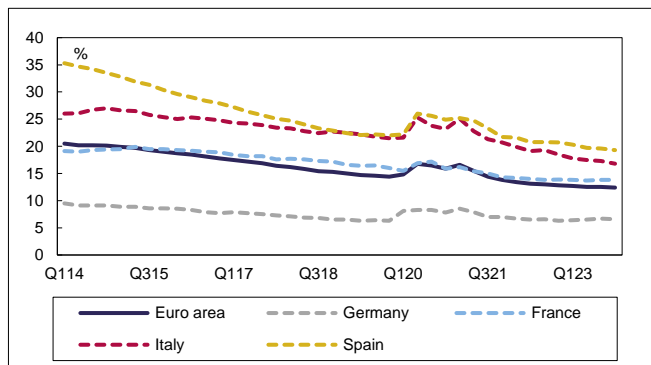
Source: Macrobond and Daiwa Capital Markets Europe Ltd.

Euro area: Unemployment rate by member state



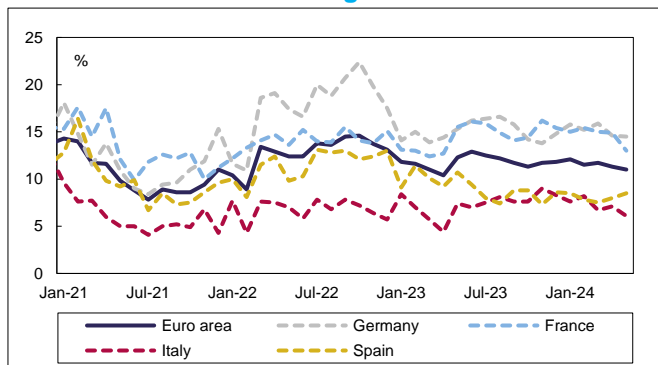
Source: Macrobond and Daiwa Capital Markets Europe Ltd.

Euro area: Labour slack*



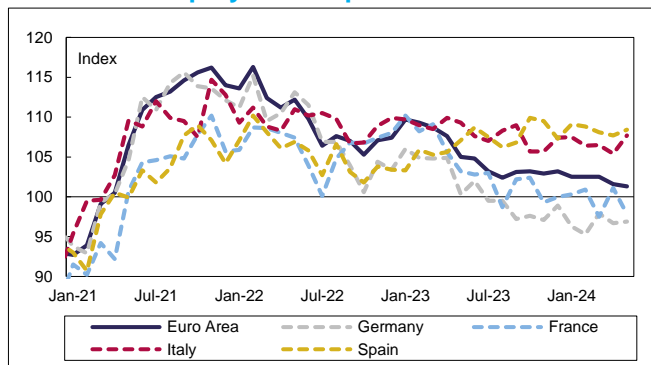
*20-64year olds. Source: Macrobond and Daiwa Capital Markets Europe Ltd.

Euro area: Labour hoarding indices



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

Euro area: Employment expectations indices








Source: Macrobond, EC 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	 Commission's Economic Sentiment Indicator	May	96.0	96.1	95.6	-
	 Commission's industrial (services) confidence indicator	May	-9.9 (6.5)	-9.7 (6.7)	-10.5 (6.0)	-10.4 (6.1)
	 Commission's final consumer confidence indicator	May	-14.3	-14.3	-14.7	-
	 Unemployment rate %	Apr	6.4	6.5	6.5	-
Spain	 Preliminary HICP (CPI) Y/Y%	May	3.8 (3.6)	3.7 (3.6)	3.4 (3.3)	-













Auctions

Country	Auction
Italy	 sold €2.5bn of 3.35% 2029 bonds at an average yield of 3.54%
	 sold €1.5bn of 3.85% 2029 bonds at an average yield of 3.57%
	 sold €3.5bn of 3.85% 2034 bonds at an average yield of 3.97%
	 sold €1.0bn of 2029 floating-rate bonds at an average yield of 4.52%
	 sold €1.0bn of 2032 floating-rate bonds at an average yield of 4.9%

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	 10.00	Preliminary headline (core) HICP Y/Y%	May	<u>2.6 (2.7)</u>	2.4 (2.7)
Germany	 07.00	Retail sales M/M% (Y/Y%)	Apr	-0.3 (2.5)	2.3 (-2.2)
France	 07.45	Preliminary HICP (CPI) Y/Y%	May	2.7 (2.4)	2.4 (2.2)
	 07.45	PPI Y/Y%	Apr	-	-7.5
	 07.45	Consumer spending M/M% (Y/Y%)	Apr	0.2 (1.4)	0.4 (0.5)
	 07.45	GDP – 2 nd estimate Q/Q% (Y/Y%)	Q1	0.2 (1.1)	0.1 (0.8)
Italy	 09.00	GDP – 2 nd estimate Q/Q% (Y/Y%)	Q1	0.3 (0.6)	0.1 (0.7)
	 10.00	Preliminary HICP (CPI) Y/Y%	Apr	0.8 (0.8)	0.9 (0.8)
UK	 00.01	Lloyds business barometer (own price expectations)	May	-	42 (60)
	 07.00	Nationwide house price index M/M% (Y/Y%)	May	0.1 (0.8)	-0.4 (0.6)
	 09.30	Net consumer credit £bn (Y/Y%)	Apr	-	1.6 (8.8)
	 09.30	Mortgage lending £bn (approvals 000s)	Apr	0.5 (61.5)	0.3 (61.3)

Auctions and events

- Nothing scheduled -

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

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