

# Euro wrap-up

## Overview

- Bunds made modest gains as euro area producer goods prices fell for a sixth successive month and the final services PMIs signalled a further easing in price pressures.
- Gilts were little changed while the UK's PMIs signalled a slowdown in recovery momentum and price pressures in the services sector.
- Thursday's ECB monetary announcement will highly likely see the Governing Council cut interest rates by 25bps, but likely revise higher its near-term inflation projection.

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### Daily bond market movements

Bond	Yield	Change
BKO 2.9 06/26	2.967	-0.019
OBL 2.1 04/29	2.547	-0.026
DBR 2.2 02/34	2.497	-0.034
UKT 0½ 01/26	4.323	+0.004
UKT 0½ 01/29	4.082	-
UKT 4½ 01/34	4.176	-

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

## Euro area

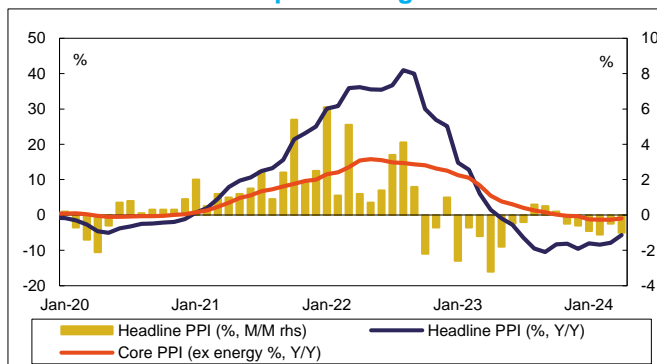
### Industrial producer goods prices down for sixth successive month

With global supply strains now largely absent, the goods sector has been a welcome source of disinflation in the euro area this year. Indeed, with prices unchanged on a seasonally adjusted basis, and six-month momentum down to an annualised rate of just 0.3%, the flash estimate of consumer core goods inflation fell in May to just 0.8%Y/Y, the softest rate since July 2021. Today's producer price inflation figures similarly suggested that pipeline pressures in the factory sector remain minimal. Indeed, overall industrial producer prices fell for a sixth consecutive month in April, and by 1.0%M/M, the second-steepest drop in eleven months. Due to base effects, the annual pace of decline eased by 2.1ppts, but remained sharp at 5.7%Y/Y. And industrial producer prices were down almost 15% from the peak in September 2022. The decline in April reflected another notable drop in energy prices, by 3.6%M/M – the second-biggest since last May – as prices of electricity and gas fell 5.5%M/M. With the decline in energy prices a year earlier significantly larger, however, the annual rate moderated 5.6ppts to -14.7%Y/Y. But the level of producer energy prices was more than 37% below the peak in September 2022.

### Core producer goods prices up in April but surveys suggest that pressures remain minimal

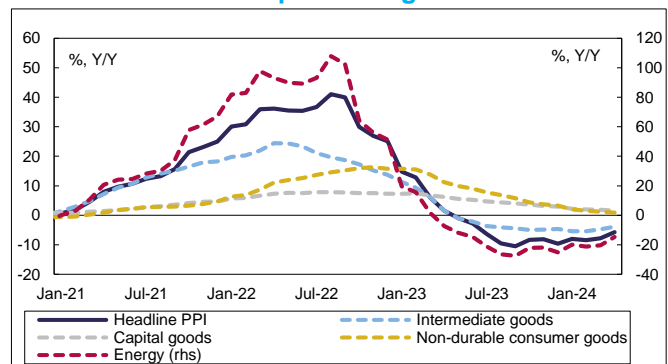
While producer energy prices continued to decline in April, non-energy producer output prices rose for a fourth successive month to suggest that the broader disinflationary trend in the goods sector has now largely run its course. But the increase in such prices of 0.2%M/M was certainly not alarming. And that left the core rate of industrial PPI inflation in negative territory at -1.0%Y/Y. Intermediate goods prices rose 0.3%M/M, the most since January 2023, to push the respective inflation rate up 0.9ppt to -3.9%Y/Y. Energy-intensive subsectors such as chemicals, paper and basic metals subsectors continued to record significant year-on-year declines despite registering price increases on the month. And while prices of capital and non-durable consumer goods were also up on the month, the respective annual rates continued to moderate to 1.5%Y/Y and 0.9%Y/Y respectively, the lowest since April 2021, with the latter reflecting the steepest producer food deflation (-1.4%Y/Y) in almost eight years. While wholesale gas prices have been trending higher since the end of winter, and reached six-month highs in the past week on concerns associated with Norwegian supply disruption, the decline in crude oil prices from April's peak will provide some welcome offset. And survey indicators suggest that price pressures in the goods sector remain broadly absent, with this week's final euro area manufacturing PMIs for both input costs and selling prices remaining below the key 50 mark in May. Indeed, while the respective index suggested that input costs (49.2) fell the least since the downtrend began in March 2023, the output price PMI (48.3) was merely the highest since February and close to the average of the prior six months.

### Euro area: Industrial producer goods inflation



Source: Macrobond and Daiwa Capital Markets Europe Ltd.

### Euro area: Industrial producer goods inflation



Source: Macrobond and Daiwa Capital Markets Europe Ltd.

## Services price PMIs fall to multi-month lows, but remain above the long-run averages

ECB policymakers remain most concerned about the stickiness in services inflation. But consistent with the further moderation in the [Commission's](#) selling price expectations index, today's final services PMIs signalled an easing in inflationary pressures in the middle of Q2. In particular, the input price PMI fell for the second month in three in May and by 1.2pts to a three-year low of 60.5. And encouragingly, the equivalent prices charged component fell the most in 11 months (-1.7pts) to 54.2, the lowest since last September and some 11pts below the peak in April 2022. Nevertheless, like the Commission's survey indices, the services output price PMI still remains above the long-run average, suggesting ongoing persistence in services inflation. And so, while the conclusion of the ECB's monetary policy meeting tomorrow seems highly likely to deliver the first rate cut this cycle, the Governing Council will continue to emphasise that it will want to see further evidence of easing price pressures in the services sector before easing policy further, therefore downplaying the likelihood of successive rates cuts over coming months.

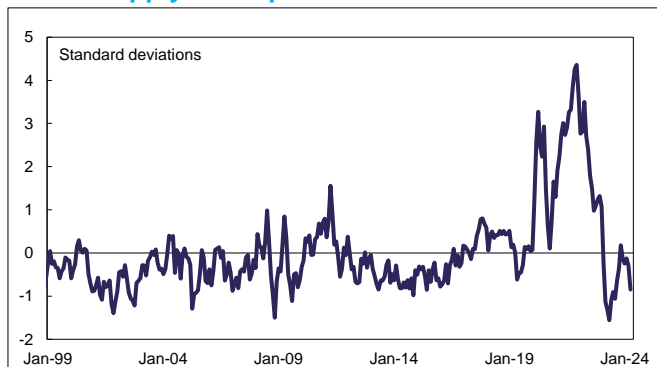
## Services PMI up to a 12-month high in May led by improvements in Germany and Spain

The more hawkish ECB policymakers will point to signs of accelerated recovery momentum to support the case to proceed cautiously when removing policy restrictiveness. Indeed, while today's final services PMIs brought a modest downwards revision from the flash release, the headline activity index (53.2) was nevertheless only marginally below April's 11-month high and averaging more than 3pts above the Q1 level. Moreover, the aggregate index was curbed by a notable decline in France (-2pts to 49.3), where the PMIs often underestimate economic output. In contrast, the German (54.3) and Spanish (56.9) activity PMIs were the strongest in 12 and 13 months respectively. And while the equivalent Italian index (54.2) eased slightly in May it was consistent with steady growth. Encouragingly, the survey also signalled improvement in demand across the larger member states. So, overall, while the manufacturing output PMIs also delivered a modest downwards revision in the final release, the euro area's composite PMI (52.2) was the highest since May last year, trending so far in Q2 some 2.8pts above the Q1 average and a level that is arguably consistent with GDP growth of 0.3%Q/Q.

## French industrial production firmer at start of Q2 amid rebound in machinery output

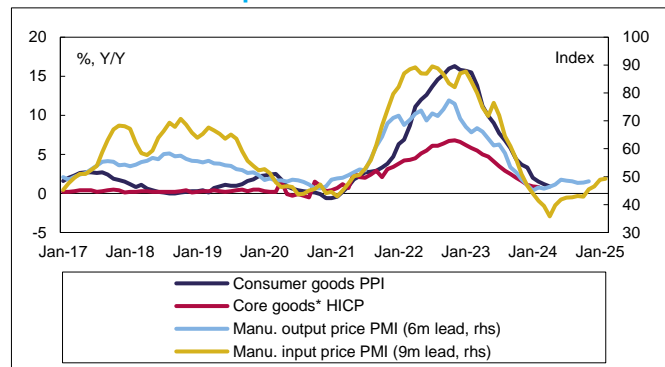
While euro area manufacturing production provided a non-negligible drag on GDP growth in the first quarter, the first of the member state IP releases for April published today suggested a more positive start to Q2. In particular, French industrial production came in a touch firmer than expected, rising 0.5%M/M following a decline of -0.3%M/M in March. Admittedly, given the sharp drop at the start of the year this still left output a touch below December's level, but nevertheless 0.9% higher than a year earlier and 0.5% above the Q1 average. Within the detail, production of capital goods rose for the first

### Global supply chain pressure index



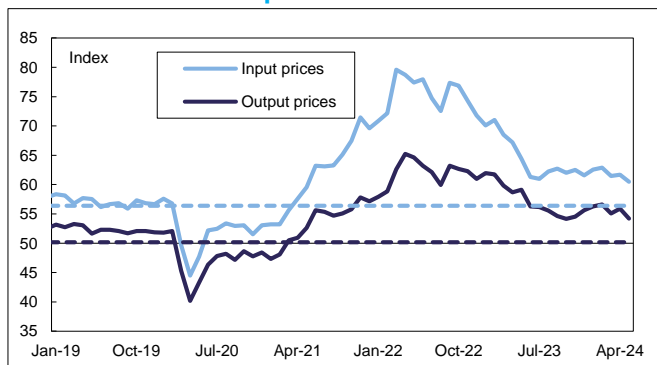
Source: Macrobond, New York Federal Reserve and Daiwa Capital Markets Europe Ltd.

### Euro area: Goods price indicators



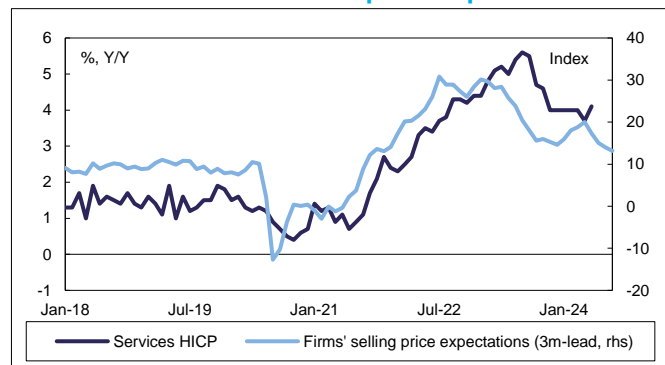
\*Non-energy industrial goods. Source: Macrobond, S&P Global and Daiwa Capital Markets Europe Ltd.

### Euro area: Services price PMIs\*



\*Dashed lines represent pre-pandemic averages. Source: Macrobond, S&P Global and Daiwa Capital Markets Europe Ltd.

### Euro area: Services HICP & price expectations



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

month in five in April (1.0%M/M), led principally by a rebound in machinery (5.2%M/M), electrical equipment (1.8%M/M) and computer, electronic and optical products (1.2%M/M). But despite a modest increase in motor vehicle production, overall transport equipment fell (-4.8%M/M) to a nine-month low. And ongoing weakness in new car registrations in May (-2.5%M/M) raises uncertainties about the near-term production outlook. Intermediate goods output also edged slightly lower in April (-0.5%M/M) as chemicals production reversed growth in earlier months. And consumer durables output (-2.1%M/M) partly reversed strong growth in March, albeit leaving the level still some ½% above the Q1 average. Meanwhile, construction activity rose 1.0%M/M in April, although having fallen sharply in February the level of output was broadly unchanged from the Q1 average.

## The day ahead in the euro area

The main focus tomorrow will be the ECB's monetary policy announcements and publication of updated economic projections. With the Governing Council having signalled clearly that a rate cut is coming this week, we expect the key deposit rate to be cut from its record high by 25bps to 3.75%. But after Friday's [upside surprise to euro area inflation](#) in May, and in particular the significant strength in the services component, the Governing Council will make clear that policy will still remain restrictive for an extended period and that future decisions will remain data dependent. Indeed, the Eurosystem's updated projections will likely nudge up slightly the near-term profile of inflation and GDP. And while inflation will still be expected to return to target on a sustainable basis in H225, in her press conference ECB President Lagarde will likely downplay significantly the chances of a further rate cut in July.

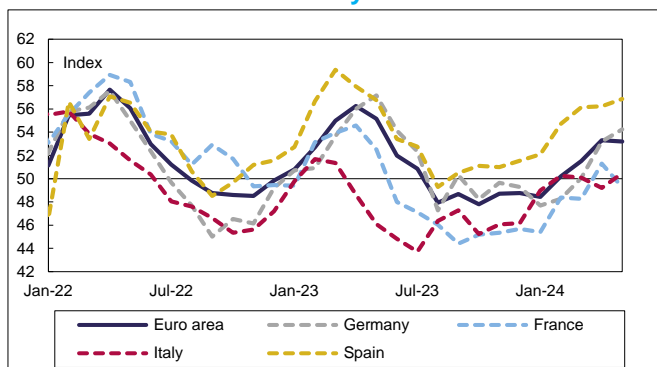
Datavise, euro area retail sales figures for April are likely to report a soft start to the second quarter, with declines in German sales and French household consumption of goods suggesting that aggregate euro area sales fell about ½%M/M. Meanwhile, German factory orders data will provide an update on manufacturing conditions in the largest member state. Following three successive monthly declines, we expect orders to post growth of about ½%M/M in April. But the May construction PMIs are expected to remain consistent with a trend contraction in Germany and the euro area as a whole.

## UK

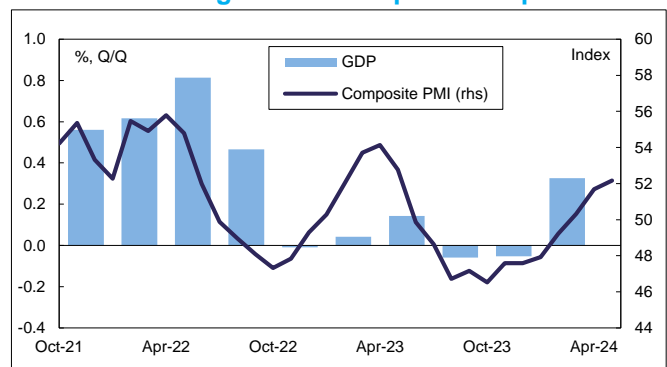
### Services PMIs point to slowing economic momentum and price pressures

Contrasting with the upwards revision to the final manufacturing output PMI (up 0.7pt to a 25-month high of 53.4) earlier in the week, today's final services survey was little changed from the flash release to suggest a notable slowdown in economic

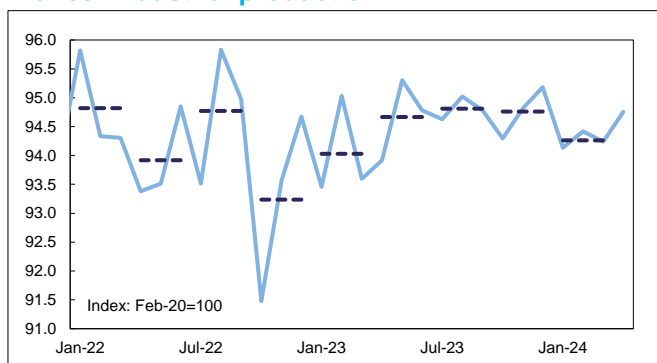
#### Euro area: Services PMIs by member state



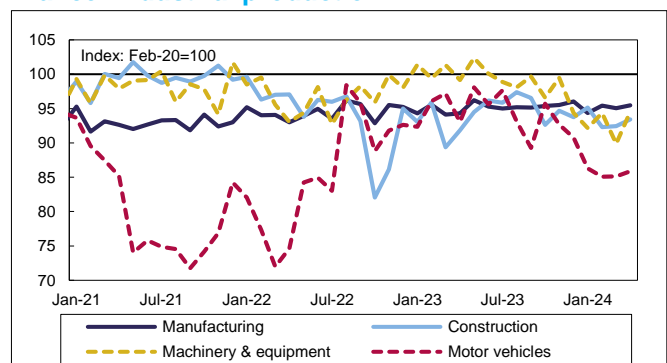
#### Euro area: GDP growth & composite output PMI



#### France: Industrial production\*



#### France: Industrial production



momentum. In particular, the headline activity index fell 2.1pts in May to 52.9, a six-month low, while the new business component fell a steeper 2.7pts to 51.7, similarly the softest since November, on reports of weaker overseas demand as some firms cited difficulties carrying out business with customers in the EU. Admittedly, having reached an 11-month high in April, both indices were still trending a touch above the Q1 average and remained consistent with positive growth. And with services firms more upbeat about the year ahead, they continued to add to their headcount in May. The most encouraging indices in today's survey related to the near-term inflation outlook, as they suggested a notable easing in price pressures in the sector in May. In particular, the input price index was revised even lower from the flash release, to be down 6.2pts to 60.8, the lowest since February 2021 and just 1pt above the pre-pandemic five-year average, implying that the impact of the near-10% hike in the National Living Wage in April has already started to fade. And importantly for BoE policymakers, today's survey further illustrated that firms have limited scope to pass on costs to consumers, with the prices charged component easing to a three-year low (55.3), albeit remaining well above the long-run average.

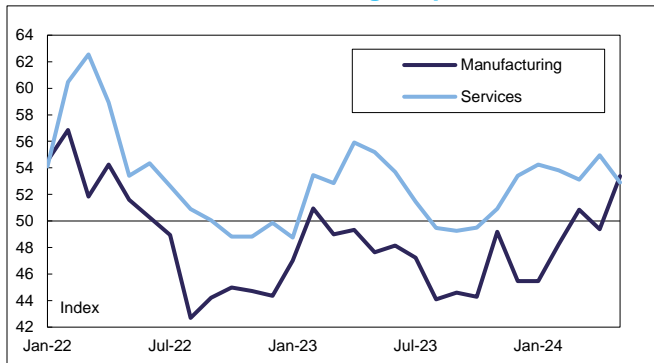
### Private new car registrations maintained a downwards trend in May

Today's new car registrations figures pointed to ongoing moderate recovery in the middle of Q2. In particular, total registrations rose 1.7%Y/Y, up from 1.0%Y/Y but down from average growth around 11%Y/Y in the previous six months. The pickup reflected a rebound in business sales in May, which returned to positive growth (9.5%Y/Y) for the first time in nine months, while fleet registrations continued to rise at a double-digit annual pace (14.0%Y/Y). In marked contrast, however, private registrations fell further in May (-12.9%Y/Y) to remain some 28% below the outturn in the equivalent month in 2019. And despite the recent rise in disposable incomes and further easing in inflation of new cars – to a four-year low of 2.5%Y/Y – the latest consumer confidence survey suggests only limited improvement in households' willingness to make major purchases. As such, we suspect that any recovery in new private car registrations will remain lacklustre.

### The day ahead in the UK

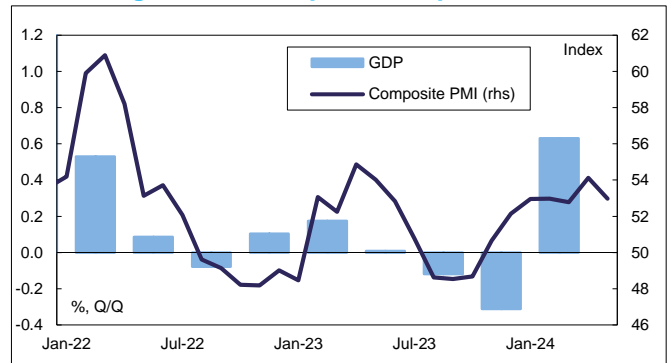
Thursday will bring the results of the BoE's Decision Maker Panel survey for May, which will provide an update on firms' inflation expectations. We expect firms' expectations for CPI inflation to remain well anchored in May after their forecast for three years ahead declined to just 2.6%Y/Y in April. Policymakers will also watch developments in wage expectations, which previously eased to a two-year low of 4.6%Y/Y, albeit remaining above levels consistent with the BoE's 2% inflation target over the medium term. Meanwhile, contrasting with the euro area, the UK construction PMIs are likely to point to ongoing modest expansion in the sector in the middle of Q2.

#### UK: Services & manufacturing output PMIs



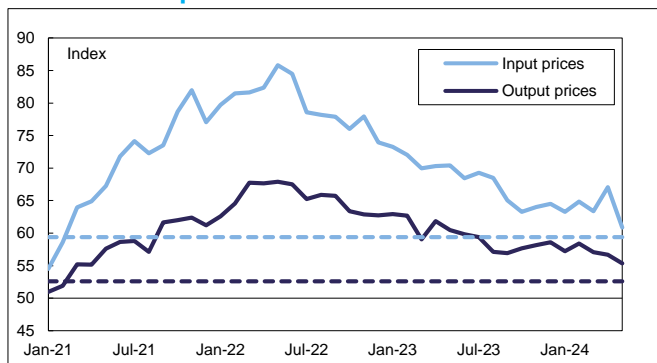
Source: Macrobond, S&P Global and Daiwa Capital Markets Europe Ltd.

#### UK: GDP growth & composite output PMI



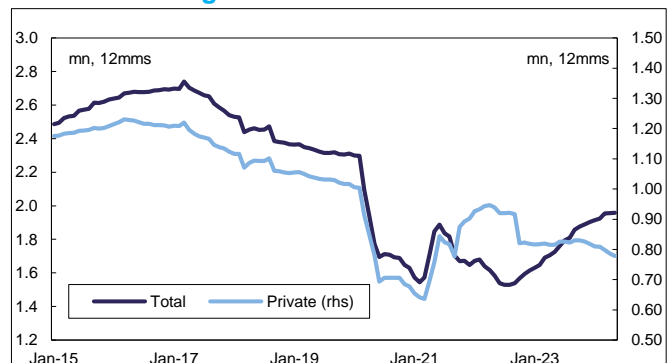
Source: Macrobond, S&P Global and Daiwa Capital Markets Europe Ltd.

#### UK: Services price PMIs\*



\*Dashed lines represent pre-pandemic averages. Source: Macrobond, S&P Global and Daiwa Capital Markets Europe Ltd.

#### UK: New car registrations













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	 Final services (composite) PMI	May	<b>53.2 (52.2)</b>	53.3 (52.3)	53.3 (51.7)	-
	 PPI Y/Y%	Apr	<b>-5.7</b>	-5.3	-7.8	-
Germany	 Final services (composite) PMI	May	<b>54.2 (52.4)</b>	53.9 (52.2)	53.2 (50.6)	-
	 New car registrations (production) Y/Y%	May	<b>-4.3 (-18)</b>	-	19.8 (26)	-
France	 Industrial production M/M% (Y/Y%)	Apr	<b>0.5 (0.9)</b>	0.5 (0.7)	-0.3 (0.7)	-
	 Final services (composite) PMI	May	<b>49.3 (48.9)</b>	49.4 (49.1)	51.3 (50.5)	-
Italy	 Services (composite) PMI	May	<b>54.2 (52.3)</b>	-	54.3 (52.6)	-
Spain	 Services (composite) PMI	May	<b>56.9 (56.6)</b>	-	56.2 (55.7)	-
UK	 New car registrations Y/Y%	May	<b>1.7</b>	-	1.0	-
	 Final services (composite) PMI	May	<b>52.9 (53.0)</b>	52.9 (52.8)	55.0 (54.1)	-












#### Auctions

Country	Auction
Germany	 sold €2.44bn of 2.4% 2030 bonds at an average yield of 2.55%
UK	 sold £4.0bn of 3.75% 2027 bonds at an average yield of 4.505%










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	-	41.9
	 10.00	Retail sales M/M% (Y/Y%)	Apr	-0.4 (0.2)	0.8 (0.7)
	 13.15	ECB deposit (refi) rate %	Jun	<b>3.75 (4.25)</b>	4.00 (4.50)
Germany	 07.00	Factory orders M/M% (Y/Y%)	Apr	0.6 (0.3)	-0.4 (-1.9)
	 08.30	Construction PMI	May	-	37.5
France	 08.30	Construction PMI	May	-	41.6
Italy	 08.30	Construction PMI	May	-	48.5
Spain	 08.00	Industrial production M/M% (Y/Y%)	Apr	-	-0.7 (-1.2)
	 08.00	House prices Q/Q% (Y/Y%)	Q1	-	-1.1 (4.2)
UK	 09.30	DMP 3M output price (1Y CPI) expectations Y/Y%	May	3.9 (2.8)	4.0 (2.9)
	 09.30	Construction PMI	May	-	53.0

#### Auctions and events

Euro area	 13.15	ECB monetary policy announcement
	 13.45	ECB President Lagarde to speak at post-meeting press conference
France	 09.50	Auction: To sell 3% 2034 bonds
	 09.50	Auction: To sell 1.25% 2038 bonds
	 09.50	Auction: 3.25% 2055 bonds
Spain	 09.30	Auction: 2.5% 2027 bonds
	 09.30	Auction: 0.01% 2031 bonds
	 09.30	Auction: 2.05% 2039 bonds
	 09.30	Auction: 4% 2054 bonds

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

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