

Euro wrap-up

Overview

- Bunds had a mixed performance as CDU leader Merz required a second vote in the Bundestag to secure the required majority to become Germany's next Chancellor, while the final April euro area composite output PMI was in line with the Q1 average, but expectations weakened.
- Shorter-dated Gilts made modest gains as the final UK PMIs signalled contraction for the first time in 18 months.
- Wednesday will bring March data for euro area retail sales, German factory orders and French trade, as well as the April construction PMIs.

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Daily bond market movements

Bond	Yield	Change
BKO 2.2 03/27	1.735	-0.013
OBL 2.4 04/30	2.062	+0.004
DBR 2½ 02/35	2.537	+0.020
UKT 3¾ 03/27	3.817	-0.025
UKT 4¾ 03/30	3.966	-0.010
UKT 4½ 03/35	4.511	+0.004

*Change from close as at 5.00pm BST.
Source: Bloomberg

Euro area

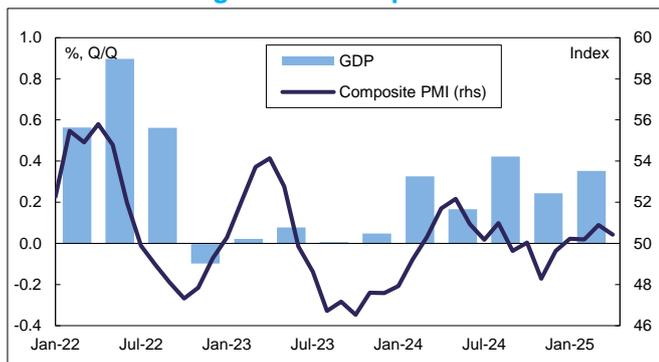
Final April output PMIs bang in line with the Q1 average, but demand is weakening

Despite persisting uncertainty surrounding US tariffs and future trade relations, today's final PMIs suggested that euro area economic activity held up relatively well at the start of Q2. As flagged in the flash release, the headline composite PMI fell in April, but the drop was smaller than initially estimated. Indeed, at 50.4, the index was still the second highest in the past eight months and bang in line with the Q1 average, when GDP growth accelerated 0.4%Q/Q as firms front-loaded production and shipments to the US. And so, today's survey was arguably consistent with further modest expansion in private sector activity, supported by manufacturing, for which the output PMI (51.5) implied the strongest production growth in more than three years. But despite being nudged slightly higher from the flash, the services index (50.1) was the weakest for five months and consistent with stagnation. The German services PMI (49.0) was the softest for 14 months. And the equivalent French index (47.3) similarly implied contraction. In contrast, the Italian services index (52.9) signalled an acceleration in April, with the respective composite PMI (52.2) the strongest in 11 months. And despite slipping to a five-month low, the respective Spanish PMI (53.4) still implied continued outperformance among the larger member states. This notwithstanding, the Spanish composite PMI in April (52.5) was almost 2pts below the Q1 average, suggesting a likely further moderation in growth in Q2. With services firms flagging a decline in new business – by the most since November – and manufacturing production highly likely to report some payback for the strength in Q1, we currently forecast euro area GDP to contract slightly in Q2 (-0.1%Q/Q). And business expectations for the year ahead fell to an 18 month low too.

Investor survey more upbeat in May, but German political disarray adds some uncertainty

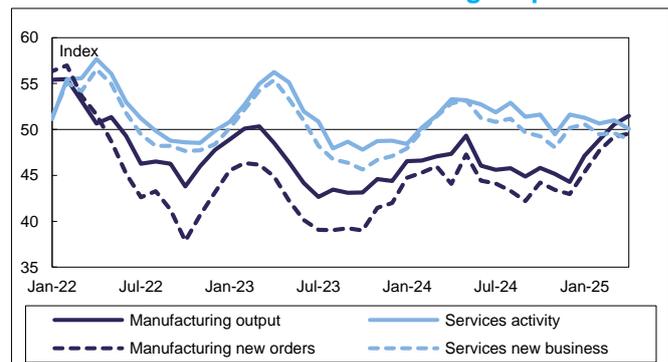
At face value, yesterday's Sentix survey suggested that investors' perceptions of the euro area's economic situation stabilised at the start of May, seemingly buoyed by the recent improvement in mood in European equity markets, likelihood of further monetary policy easing and a measured response so far by EU policymakers in the US trade negotiations. In particular, the current situations balance rose 4pts in May to -19.3, the highest since last August. The expectations balance also jumped a sizeable 19.6pts to an above-average 3.8. But this failed to fully reverse the decline in April, to leave the index some 14pts below March's high, which was buoyed by the agreement of the German government to boost spending on defence and infrastructure. And investor sentiment of Germany's economy might temporarily worsen after CDU leader Merz today initially failed to secure an absolute majority in a parliamentary vote to confirm him as Germany's next Chancellor, the first time in a first-round vote round since the second world war. Admittedly, Merz subsequently secured 326 votes (out of the coalition's 328 in the Bundestag) in a second vote (beating the 316 threshold). But today's actions illustrate a potentially fragile domestic political backdrop in an already challenging global environment, raising some doubts about the potential credibility of the coalition's spending agenda and further adding downside risks to Germany's near-term growth prospects.

Euro area: GDP growth & composite PMI



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

Euro area: Services & manufacturing output PMIs

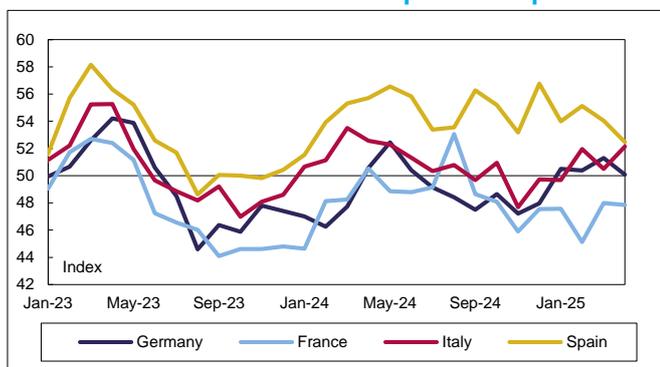


Source: Macrobond, S&P Global and Daiwa Capital Markets Europe Ltd.

French IP moved sideways in Q1 despite rise in autos and pharmaceuticals output

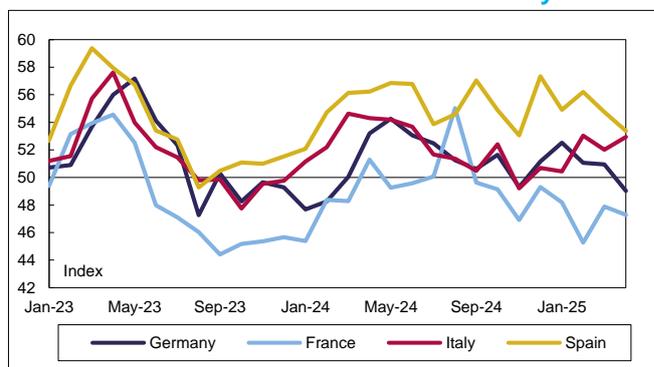
While economic growth was widespread across the euro area in Q1, it was weakest in France (0.1%Q/Q) among the larger member states. This in part reflected subdued factory output in the first quarter, with only some limited signs of front-loading of production perhaps reflecting the relatively smaller share of French exports to the US compared with other countries in the regions such as Germany and Ireland. Indeed, despite rising for a second successive month in March and by 0.6%M/M, manufacturing output merely rose 0.1%Q/Q in Q1. Admittedly, growth in March was driven by the transport sector, with car production (4.3%M/M) up to the highest level in 15 months and rising almost 6%Q/Q over the first quarter as a whole. Output from the pharmaceuticals sector also jumped 4½%Q/Q in Q1. And despite falling in March, production of computer, electronic and optical products was up 0.9%Q/Q in Q1, while output from the food, beverages and tobacco industry was also up for the first quarter in four (1%Q/Q). But output of machinery and equipment and metal products fell sharply in Q1. With construction activity also down in March (-0.9%M/M), total industrial production rose just 0.2%M/M to leave output unchanged over the first quarter as a whole.

Euro area member states: Composite output PMIs



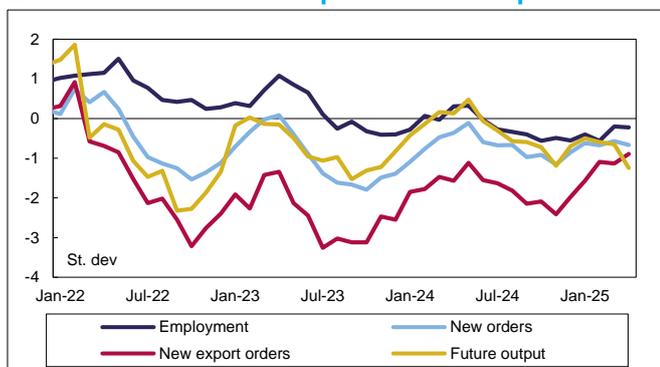
Source: Macrobond, S&P Global and Daiwa Capital Markets Europe Ltd.

Euro area member states: Services activity PMIs



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

Euro area: Selected composite PMI components



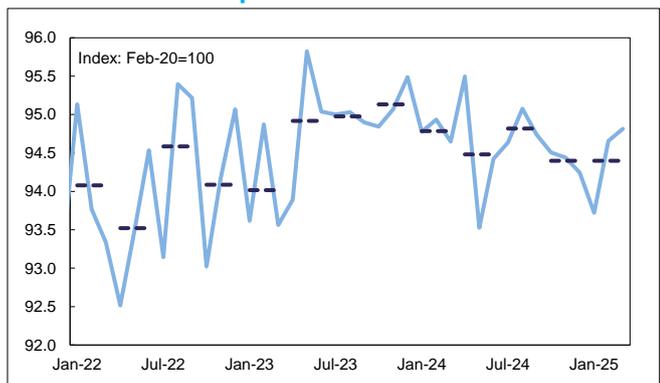
Source: Macrobond, S&P Global and Daiwa Capital Markets Europe Ltd.

Euro area & Germany: Sentix investor survey



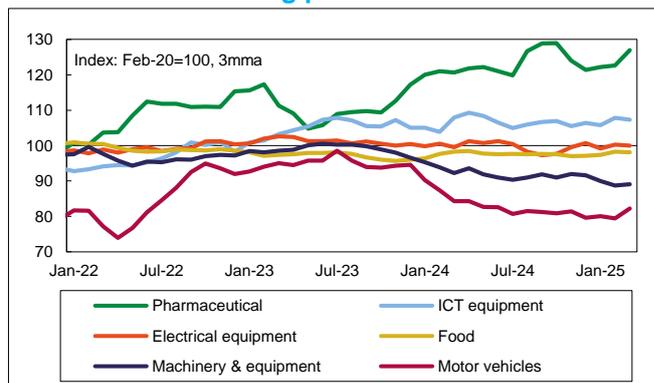
Source: Macrobond and Daiwa Capital Markets Europe Ltd.

France: Industrial production*



*Dashed dark blue lines represent quarterly average.
Source: Macrobond and Daiwa Capital Markets Europe Ltd.

France: Manufacturing production



Source: Macrobond and Daiwa Capital Markets Europe Ltd.

The day ahead in the euro area

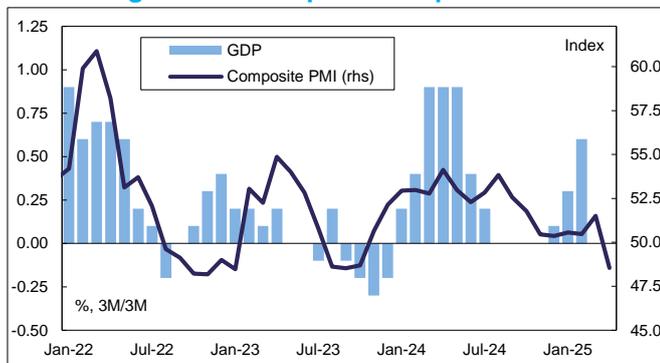
After last week's **Q1 GDP** figures showed that euro area growth accelerated in part because some firms front-ran production and shipments ahead of US tariff hikes, tomorrow's data flow will provide insight into demand developments at the end of the quarter. Euro area retail sales numbers should come in broadly unchanged in March, with slight declines in Germany, France and Spain offset by rises in the Netherlands and Belgium. This would still leave sales up 0.3%3M/3M, supporting our view that household consumption contributed positively to Q1 GDP. But German new factory orders data will likely suggest that underlying goods demand remained subdued in March as economic uncertainties surrounding global trade policies mounted. And although the April construction PMIs might benefit from the ongoing recovery in the housing market and further cut to borrowing costs, the headline euro area activity index is likely to remain sub-50 for a 36th consecutive month, led by ongoing weakness in Germany and France.

UK

UK PMIs signal contraction for the first time in 18 months, but services price pressures rise

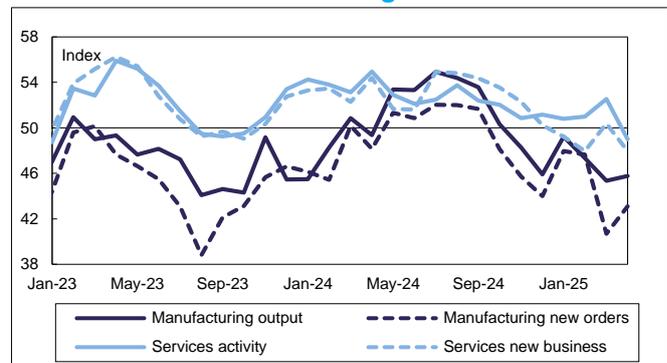
Despite a modest upwards revision from the flash release, today's final PMIs confirmed a notable deterioration in the UK's economy at the start of Q2, reinforcing expectations that the GDP will contract this quarter. In particular, the headline composite PMI was down a chunky 3pts – the most since February 2023 – to 48.5 in April, the first sub-50 contractionary reading in 18 months and almost 4pts below the average in the previous twelve months. Of course, the PMIs have not always been a reliable guide to UK economic growth over recent years and failed to fully capture the likely strength in Q1. Nevertheless, the PMIs suggested that the impact of weaker global growth prospects had hit demand in both the manufacturing and services sectors at the start of Q2. Indeed, while the weakness was more striking in manufacturing, services firms also attributed rising global growth risks and subdued domestic demand to the slump in the activity index (down 3.5pts to 49.0), which ended a 17-month period of expansion and was the weakest since January 2023. New business reportedly fell, with firms in the technology and financial services sectors attributing this to rising risk aversion in the face of ongoing trade negotiations. And with consumer-facing services flagging additional challenges from rising payroll costs, especially in the hospitality and leisure subsectors, services firms were the most downbeat about business expectations for the year ahead since April 2020 and the Brexit referendum in July 2016 before that. While the deterioration in the PMIs might bolster the case to amend on Thursday the BoE's forward guidance for a "careful and gradual" approach to future policy easing, policymakers will also be wary about the potential inflationary impact of the increase in employer National Insurance Contributions and the minimum wage at the start of this month. Indeed, the services input costs PMI

UK: GDP growth & composite output PMI



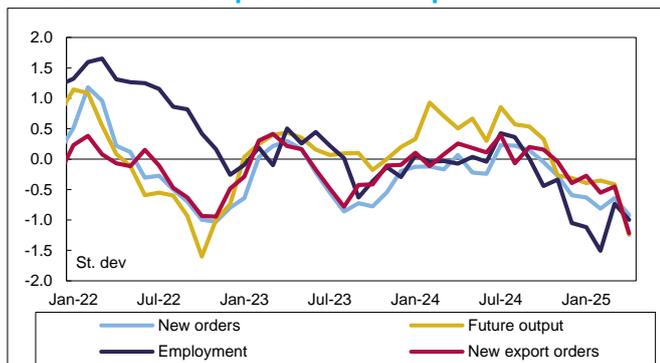
Source: Macrobond, S&P Global and Daiwa Capital Markets Europe Ltd.

UK: Services & manufacturing PMIs



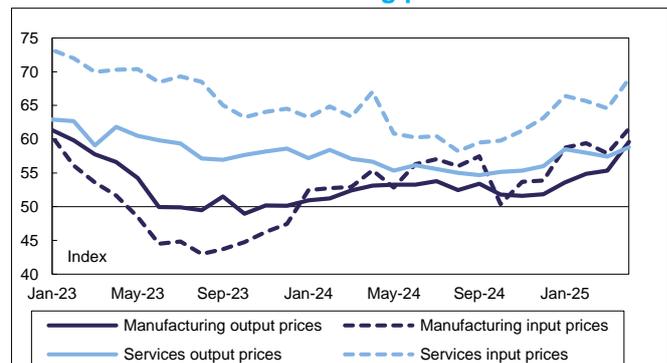
Source: Macrobond, S&P Global and Daiwa Capital Markets Europe Ltd.

UK: Selected composite PMI components



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

UK: Services & manufacturing price PMIs



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

jumped to the highest for almost two years. So, despite softening demand, firms in the sector also reportedly increased their selling prices last month by the most since July 2023.

The day ahead in the UK

Ahead of Thursday's BoE announcements, tomorrow's UK economic news flow will be light, with just the April construction PMIs scheduled for release. While the activity index in March rose from February's more-than five-year low, at 46.4 it was still well below the 2024 average (53.1) and firmly in contractionary territory. And the headline PMI is expected to have softened again in April as a recent slowdown in the housing market weighs on demand in that subsector, while heightened economic uncertainties might also constrain demand for commercial building work.

European calendar

Today's results

Economic data

Country	Release	Period	Actual	Market consensus/ <i>Daiwa forecast</i>	Previous	Revised
Euro area	 Final composite (services) PMI	Apr	50.4 (50.1)	50.1 (49.7)	50.9 (51.0)	-
	 PPI Y/Y%	Mar	1.9	2.3	3.0	-
Germany	 Final composite (services) PMI	Apr	50.1 (49.0)	49.7 (48.8)	51.3 (50.9)	-
France	 Industrial production M/M% (Y/Y%)	Mar	0.2 (0.2)	0.3 (-0.2)	0.7 (-0.4)	1.0 (-0.3)
	 Final composite (services) PMI	Apr	47.8 (47.3)	47.3 (46.8)	48.0 (47.9)	-
Italy	 Composite (services) PMI	Apr	52.1 (52.9)	50.2 (51.3)	50.5 (52.0)	-
Spain	 Unemployment (net employment) M/M change 000s	Apr	-67.4 (69.2)	-	-13.3 (23.1)	-
	 Composite (services) PMI	Apr	52.5 (53.4)	53.0 (54.0)	54.0 (54.7)	-
UK	 New car registrations Y/Y%	Apr	-10.4	-	12.4	-
	 Final composite (services) PMI	Apr	48.5 (49.0)	48.2 (48.9)	51.5 (52.5)	-

Auctions

Country	Auction
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Germany	 sold €3.48bn of 2.4% 2030 bonds at an average yield of 2.07%
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Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

Yesterday's results

Economic data

Country	Release	Period	Actual	Market consensus/ <i>Daiwa forecast</i>	Previous	Revised
Euro area	 Sentix investor confidence indicator	May	-8.1	-11.5	-19.5	-

Auctions

Country	Auction
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- 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	Apr	-	44.8
	10.00	Retail sales M/M% (Y/Y%)	Mar	0.0 (1.8)	0.3 (2.3)
Germany 	07.00	Factory orders M/M% (Y/Y%)	Mar	2.0 (1.1)	0.0 (-0.2)
	08.30	Construction PMI	Apr	-	40.3
France 	07.45	Trade balance €bn	Mar	-	-7.9
	07.45	Preliminary wages (private sector payrolls) Q/Q%	Q1	-	0.4 (-0.3)
	08.30	Construction PMI	Apr	-	43.8
Italy 	08.30	Construction PMI	Apr	-	52.4
	09.00	Retail sales M/M% (Y/Y%)	Mar	-	0.1 (-1.5)
UK 	09.30	Construction PMI	Apr	-	46.4

Auctions and events

France 	09.50	Auction: to sell 3.2% 2035, 1.25% 2038 & 4.5% 2041 bonds			
UK 	10.00	Auction: to sell up to £4.5bn of 4.375% 2030 bonds			

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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