Euro wrap-up

Overview

Chris Scicluna
+44 20 7597 8326

Edward Maling
+44 20 7597 8030

- While more MPC members than expected voted for a cut, Gilts made losses as the BoE left Bank Rate unchanged at 4.25%.
- Bunds also made losses as euro area construction data suggested the sector will provide support to economic growth in Q2.
- Friday will bring updates on consumer confidence and bank lending in the euro area, business conditions in France, and consumer confidence and retail sales in the UK.

Daily bond market movements

Bond	Yield	Change
BKO 1.7 06/27	1.834	+0.002
OBL 2.4 04/30	2.119	+0.018
DBR 2½ 02/35	2.518	+0.023
UKT 3¾ 03/27	3.908	+0.029
UKT 4⅜ 03/30	4.034	+0.031
UKT 4½ 03/35	4.536	+0.043

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

UK

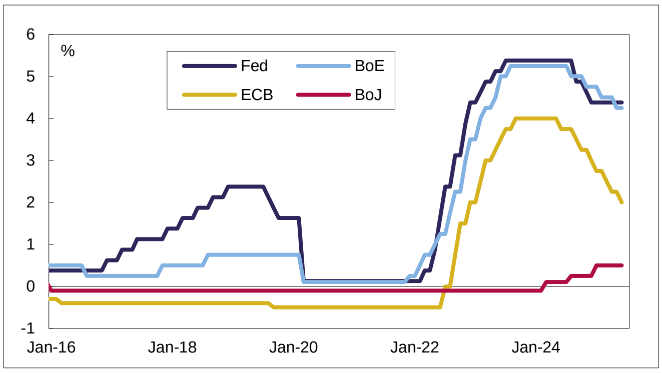
Bank Rate unchanged, but one more MPC member joins doves to reinforce likelihood of August cut

The BoE inevitably left Bank Rate at 4.25% when it announced its latest monetary policy decision today. But, as Deputy Governor Ramsden joined the two established doves (external members Dhingra and Taylor) in voting for a 25bps cut, the 6-3 vote meant that the MPC's majority in favour of the status quo was smaller than had been expected. So, in the absence of major new shocks, only two of the six members who voted for no change today will likely need to change their mind at the next meeting in August to reach a majority in favour of a cut. In our view and according to current swaps market pricing, such an outcome is highly probable. The minutes of today's meeting stated that events in the Middle East and their impact on oil prices had no impact on today's policy decision. But they might yet raise a hurdle to that summer rate cut. The MPC insisted today that it 'will remain sensitive to' and 'vigilant about' those developments and their possible impact on the UK economy. And the MPC left unchanged its forward guidance, insisting that policy is 'not on a pre-set path' and that 'a gradual and careful approach' to rate cuts remains appropriate. However, we continue to interpret that guidance as signalling that cuts of 25bps each quarter through to mid-2026 represent the most plausible path ahead for Bank Rate.

Weakening labour market calls for resumption of rate cuts in Q3 despite rise in energy prices

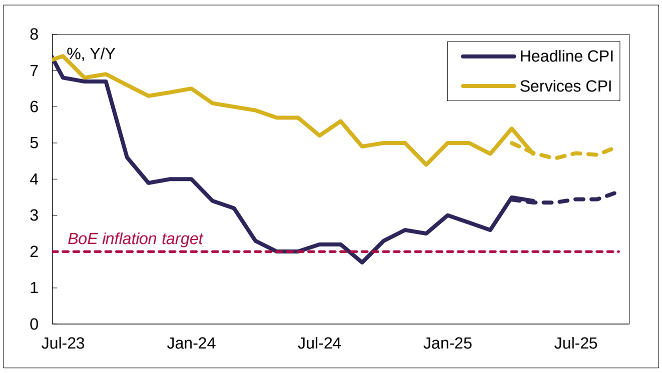
The MPC acknowledged that GDP growth in Q1 (0.7%Q/Q) had been a touch stronger than it anticipated. Bank staff also revised up their expectation of growth in Q2 to about ¼%Q/Q. Moreover, the minutes noted provisional analysis that the direct impact of the US tariff shock on the global economy could be smaller than the MPC assessed last month. But the MPC continued to place significant weight on business surveys, which suggest that underlying GDP growth was softer than implied by the official data in Q1 and remains weak in Q2. The majority on the Committee also acknowledged the 'greater signs' of disinflationary pressures from the labour market, with growing slack evident in declining vacancies relative to unemployment and pay growth on track to slow significantly over the remainder of 2025. With the May CPI reading in line with its expectation, it was also reassured that the disinflationary process continues. Nevertheless, with that headline inflation rate likely to remain elevated through the second half of the year at around 3½%Y/Y, the majority saw no strong case for a rate cut this week. The three members voting for a cut appeared less perturbed by the likely persistence of elevated inflation through H225, not least as it will be principally due to one-off policy measures. And they were more concerned about the 'material' loosening of the labour market, which appeared to increase risks that inflation will undershoot the target over the medium term. As the incoming data before now and then will likely underscore the likelihood that the labour market continues to weaken, a majority should still see a strong case for a rate cut in August even if higher wholesale energy prices demand a modest upwards revision to the Bank's near-term projection of inflation.

Policy rates in major economies*



*Deposit rate for the ECB; FFR midpoint for the Fed.
Source: Macrobond and Daiwa Capital Markets Europe Ltd.

UK: Headline & services CPI inflation*



*Dashed lines represent BoE projection from May MPR.
Source: Macrobond, BoE and Daiwa Capital Markets Europe Ltd.

The day ahead in the UK

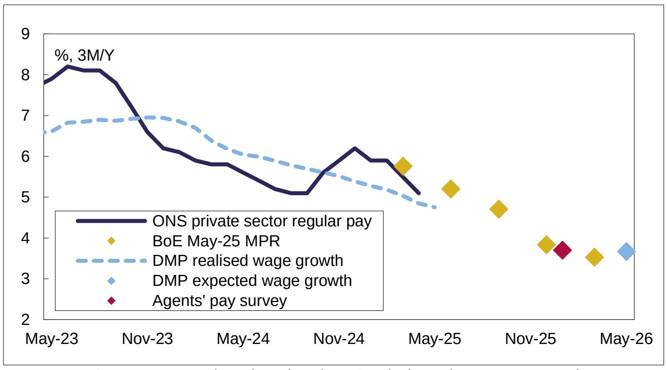
The end of the week will bring data for UK retail sales in May and consumer confidence in June. The latter improved last month, with the GfK index rising 3pts to -20, but that failed to fully reverse April's decline. And this week's BRC survey suggested that spending on the high street was markedly weaker in May. And some payback is surely in order due to the outsized growth in April's retail sales (1.2%M/M) – buoyed by persistently good weather and the timing of Easter – and solid growth throughout Q1. So, we expect retail sales to decline in May, for the first month in four. Diminishing uncertainty about tariffs given the progress towards a bilateral agreement with the US may also lend further upside to June's headline consumer confidence number, though we expect broadly sideways movement in view of headwinds from the weakening labour market and still-elevated inflation. May's public finance statistics are also due.

Euro area

April output data suggests construction likely to add to Q2 GDP growth

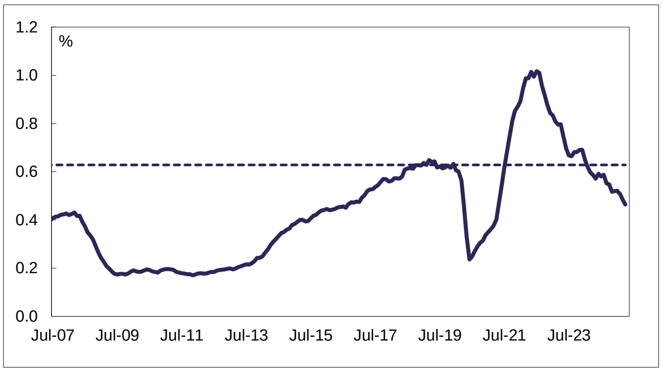
While heightened geopolitical and trade uncertainty have weighed on broader economic sentiment, construction surveys point to continued gradual recovery in the sector. That may be unsurprising, given its sensitivity to monetary policy and broader financial conditions, as well as optimism about a prospective boost in public infrastructure investment in Germany. Even so, today's construction data showed remarkable strength at the start of Q2, with growth of 1.7%M/M in April the fastest in 26 months. It also marked the fourth-highest level since mid-2010, leaving output at the start of Q2 some 1.3% above the Q1 average, to bolster expectations of another positive contribution from construction to GDP growth this quarter. Admittedly, April's increase followed two monthly declines. But while the March level was nudged down slightly, February's weakness is now judged to have been only half as soft as originally thought. So, the estimate of construction output growth in Q1 was also boosted by 0.4ppt to 0.5%Q/Q. And perhaps more encouragingly, April's growth was broad-based across member states. Indeed, discounting the few countries for which data are not yet available, construction output contracted in only Finland and Slovakia (cumulatively just 3% of euro area construction). Meanwhile, Germany (1.4%M/M), Spain (4.3%M/M) and the Netherlands (1.2%M/M) all saw sizeable gains. France rose by less (0.7%M/M), but the uptrend in residential building permits there – to the highest level in more than two years in April – should lend itself to stronger building activity over coming quarters. So too in Germany, where building work has been the chief recent source of weakness, permits rose to a 12-month high in March.

UK: Measure of pay growth



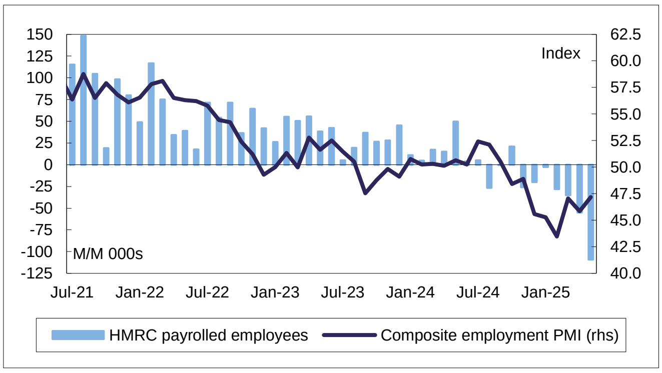
Source: Macrobond and Daiwa Capital Markets Europe Ltd.

UK: Vacancies to unemployment ratio*



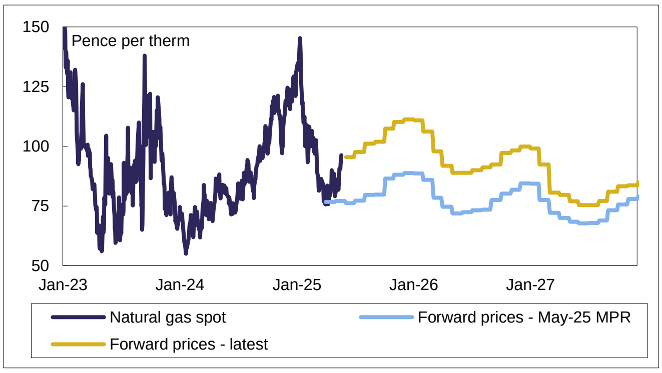
**Dashed line represents 2019 average.*
Source: Macrobond and Daiwa Capital Markets Europe Ltd.

UK: Payrolls & composite employment PMI



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

UK: Natural gas spot & forward prices

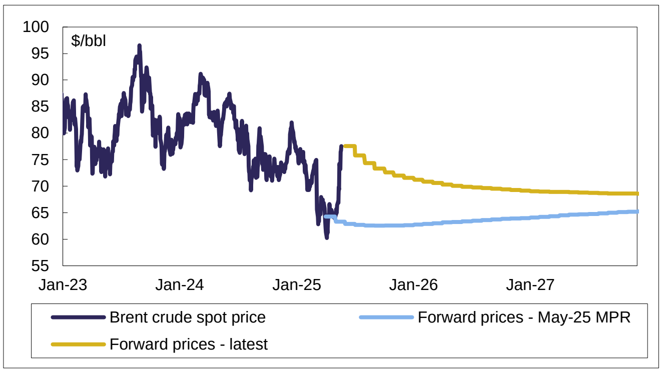


Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

The day ahead in the euro area

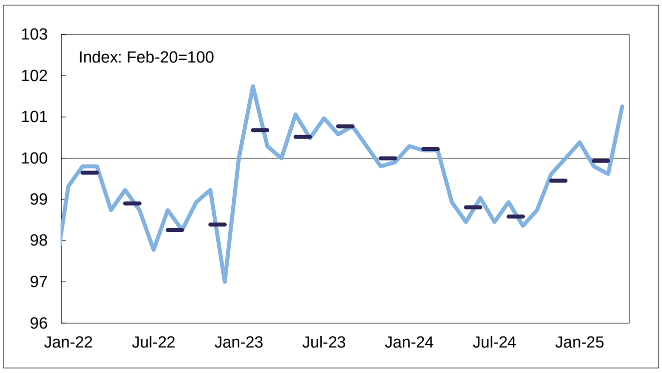
Friday's main data events in the euro area will include May's bank lending figures and the Commission's flash June consumer confidence reading. In both instances, we expect the waning drag from April's initial tariff shock and cumulative ECB easing to offer some support, countering still persistently high uncertainty amid geopolitical tensions. Buoyed by another rate cut this month, we expect further modest improvement in consumer confidence to follow May's partial recovery (up 1.4pts to -15.2). The INSEE business survey – often a reliable guide to French business activity – will also provide an update on economic sentiment at the end of Q2, ahead of next week's flash PMI results. Meanwhile, the transmission of previous rate cuts should also have supported further recovery in business and mortgage lending. Finally, German PPI data will provide a first view of euro area industrial price developments in May, with further downwards pressure from lower energy prices expected ahead of the latest spike in oil and gas prices.

UK: Brent crude oil spot & forward prices



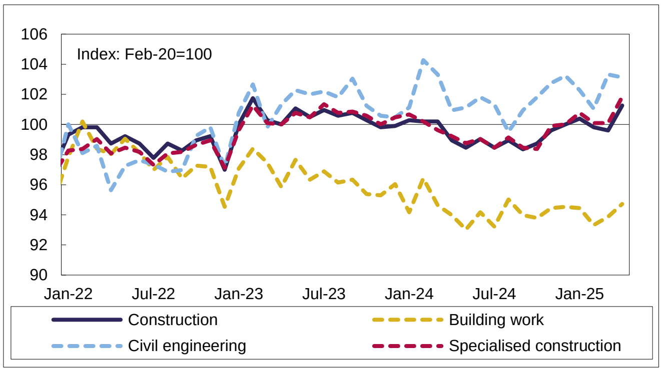
Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

Euro area: Construction output*



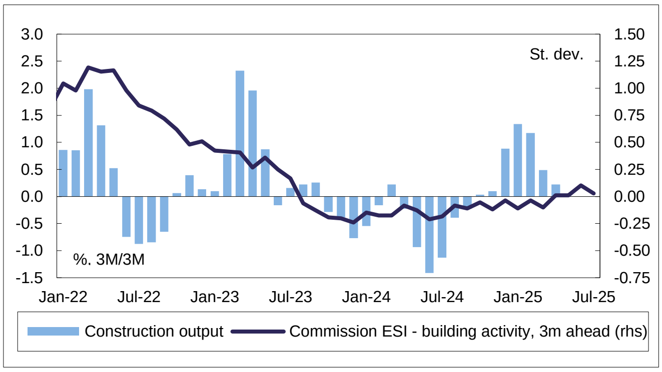
**Dark blue lines show quarterly averages.*
Source: Macrobond and Daiwa Capital Markets Europe Ltd.

Euro area: Construction output by subsector



Source: Macrobond and Daiwa Capital Markets Europe Ltd.

Euro area: Construction output & ESI



Source: Macrobond and Daiwa Capital Markets Europe Ltd.

Daiwa Capital Markets

European calendar

Today's results

Economic data

Country	Release	Period	**Actual**	Market consensus/ *Daiwa forecast*	Previous	Revised
Euro Area	Construction output M/M% (Y/Y%)	Apr	**1.7 (3.0)**	-	0.1 (-1.1)	-0.2 (-1.3)
UK	BoE Bank Rate %	Jun	**4.25**	*4.25*	4.25	-

Auctions

Country	Auction
France	sold €3.739bn of 2.4% 2028 bonds at an average yield of 2.28%
	sold €3.541bn of 2.75% 2030 bonds at an average yield of 2.53%
	sold €4.72bn of 2.7% 2031 bonds at an average yield of 2.69%
	sold €540m of 0.1% 2028 inflation-linked bonds at an average yield of 0.8%
	sold €928m of 0.6% 2034 inflation-linked bonds at an average yield of 1.17%
	sold €218m of 0.1% 2038 inflation-linked bonds at an average yield of 1.44%
Spain	sold €1.868bn of 1.95% 2030 bonds at an average yield of 2.506%
	sold €1.428bn of 3.15% 2033 bonds at an average yield of 2.904%
	sold €2.25bn of 3.2% 2035 bonds at an average yield of 3.208%

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	M3 money supply Y/Y%	May	4.0	3.9
	10.00	Preliminary Commission consumer confidence indicator	Jun	-14.9	-15.2
Germany	07.00	PPI Y/Y%	May	-1.2	2.2 (2.1)
France	07.45	INSEE business (manufacturing) confidence indicator	Jun	96 (98)	96 (97)
	07.45	Final wages Q/Q%	Q1	*0.7*	0.4
	-	BdF retail sales Y/Y%	May	-	0.4
UK	00.01	GfK consumer confidence indicator	Jun	-20	-20
	07.00	Public sector net borrowing £bn	May	18.0	20.2
	07.00	Retail sales – including auto fuel M/M% (Y/Y%)	May	-0.5 (1.7)	1.2 (5.0)
	07.00	Retail sales – excluding auto fuel M/M% (Y/Y%)	May	-0.7 (1.8)	1.3 (5.3)

Auctions and events

Country	BST	Event
Euro Area	09.00	ECB to publish Economic Bulletin 4/2025

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

https://www.uk.daiwacm.com/ficc-research/recent-blogs