

Euro wrap-up

Overview

- Bunds made modest losses as data confirmed that Germany contracted in Q1 at a softer pace than other large member states, while employment in the euro area declined for the first time since the euro crisis.
- Gilts also made losses on a quiet day for UK economic news.
- The coming week's flash PMIs for May will likely show some modest improvements as lockdown measures started to relax. But euro area car registrations and UK retail sales figures for April will be the worst on record. The ECB account from the end-April policy meeting is also due.

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Daily bond market movements

| Bond | Yield | Change |
|--------------|--------|--------|
| BKO 0 03/22 | -0.751 | +0.009 |
| OBL 0 04/25 | -0.732 | +0.011 |
| DBR 0 02/30 | -0.532 | +0.015 |
| UKT 0½ 07/22 | -0.012 | +0.033 |
| UKT 0% 06/25 | 0.074 | +0.031 |
| UKT 4% 12/30 | 0.229 | +0.029 |

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

Euro area

German GDP registers second-largest drop since reunification

The record drop in euro area GDP in Q1, of 3.8%Q/Q, was confirmed today. In addition, the first estimate from Germany revealed that GDP in the euro area's largest member state shrank a somewhat more moderate 2.2%Q/Q, nevertheless the second steepest decline since reunification after the plunge of 4.7%Q/Q in Q109. While no detail of the expenditure breakdown was released, the German statistical authority confirmed that household consumption and capex on machinery and equipment fell sharply. Exports and imports also dropped. But government consumption and construction provided support. Following a (downwardly revised) decline in GDP of 0.1%Q/Q in Q4, the substantive contraction in GDP in Q1 came despite a strong rebound in activity in the first two months of the year, as social distancing measures were imposed from 22 March. As a result, for example, over March as a whole, German retail sales dropped a record 5.8%M/M while manufacturing and mining output fell a record 11.6%M/M.

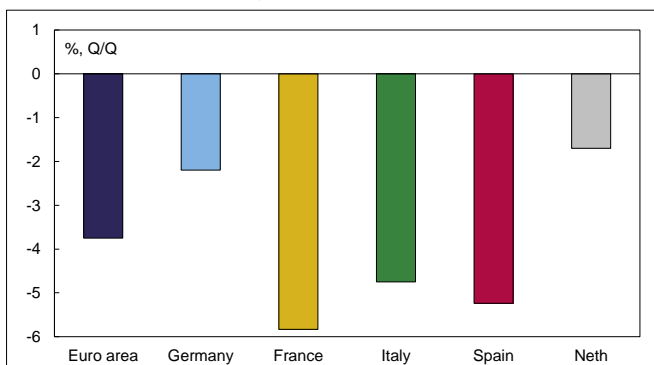
Despite successes, Q2 drop to be far more extreme

With Germany having controlled the spread of Covid-19 with greater success than the other large European countries (with confirmed deaths from the coronavirus of fewer than 8000, less than one quarter the number in the UK), its social distancing rules were able to be less draconian than elsewhere. So, construction output continued to grow in March. And the government was among the first countries to relax its controls. A gradual reopening of non-essential shops began on 20 April. Some states also permitted the reopening of restaurants from 8 May, and other states are set to follow gradually this month. Hotels are gradually re-opening too. In addition, Germany's government intends to ease controls on travel at the country's land borders with France, Switzerland and Austria from tomorrow, and end them completely in mid-June. (The borders with Belgium and the Netherlands are already effectively open). Large public events remain banned, however. And with spending and production having fallen sharply since the restrictions on activity were initially introduced in late March, German GDP is bound to have contracted more significantly in Q2. After all, car production fell an extraordinary 97%Y/Y in April. Much will depend on the evolution for the pandemic. However, we currently expect a decline of up to 10%Q/Q in German Q2. Again, however, that will be significantly smaller than the drop in overall euro area GDP.

Steeper drops in trade and employment ahead

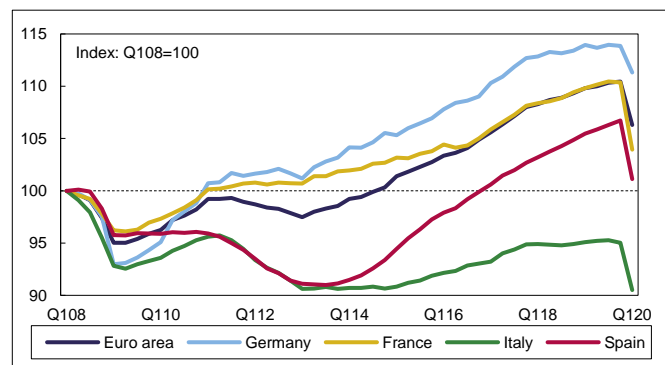
Among today's other data, the hit to euro area goods trade from the pandemic showed up for the first time, with the value of both exports and imports dropping about 9%M/M in March. That represented the steepest decline in imports since the euro was introduced, and the second-steepest decline in exports (beaten only by the fall of a little more than 10%M/M in January

Euro area: GDP in Q120



Source: Thomson Reuters and Daiwa Capital Markets Europe Ltd.

Euro area: GDP level



Source: Thomson Reuters and Daiwa Capital Markets Europe Ltd.



2009). Over Q1 as a whole, the drop in imports (3.5%Q/Q) outpaced that of exports (-2.6%Q/Q) suggesting that net trade might even have provided support to growth in Q1. Of course, trade volumes are likely to have fallen far more steeply in April. Meanwhile, euro area employment dropped in Q1 400k, the most since the global financial crisis. And while government-funded furlough schemes are providing support for tens of millions of workers, and have thus significantly limited the rise in unemployment compared to the US, surveys point to even greater permanent job-shedding ahead. For example, the euro area's composite employment PMI fell almost 15pts to a series low of 33.4 in April, suggesting non-negligible risks of a return to mass unemployment once government support is eventually withdrawn.

The week ahead in the euro area and US

With many member states having started to relax lockdown measures, a key focus in the euro area in the coming week will be the release of May sentiment surveys. Perhaps most notable will be Thursday's flash PMIs, which will be preceded by Germany's ZEW survey (Tuesday) and the Commission's preliminary consumer confidence indicator (Wednesday). Led by Germany, the PMIs are likely to point to some modest improvement in conditions this month from the record lows recorded in April (the headline euro area composite PMI fell more than 16pts to just 13.6), albeit likely still remaining at historically very weak levels. The other highlight of the week will be related to monetary policy, with the account of the end-April ECB Governing Council meeting due to be released on Friday. At that meeting, the ECB cut the interest rate on the forthcoming TLTRO-iii operations and launched an additional new PELTRO funding scheme, but left the asset purchase programmes unchanged. Separately, Chief Economist Lane will speak publicly on monetary policy on Tuesday.

In terms of hard data, euro area new car registrations figures for April (Tuesday) will definitely be dreadful – indeed, national figures already published showed record declines last month in Germany (-61%Y/Y), France (89%Y/Y), Italy (-98%Y/Y) and Spain (97%Y/Y) alike. Meanwhile, after downward revisions to the equivalent French and Spanish data, final euro area inflation figures for April (Wednesday) might bring a downwards revision to the preliminary CPI estimate, which declined 0.3ppt to 0.4%Y/Y, the lowest since September 2016. While the drop from March was due principally to lower oil prices, the flash estimate of the core CPI rate eased 0.1ppt to 0.9%Y/Y. Finally, construction output data for March (Tuesday) will show a sharp decline in activity – while output in the sector in Germany rose 1.8%M/M it plunged 40.1%M/M in France.

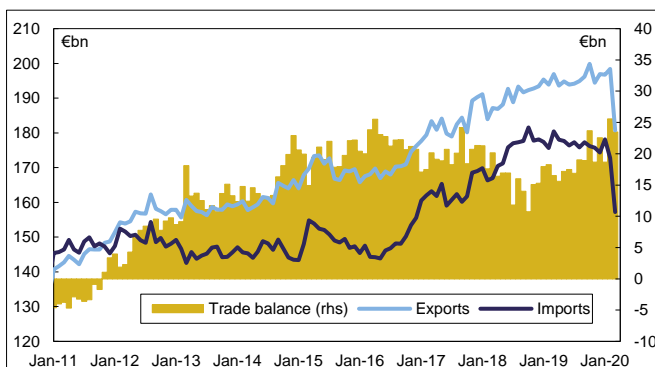
In the US, the economic dataflow will be relatively light, with housing market figures dominating. Among these, the May NAHB indices are due on Monday, April housing starts and building permits data the following day, and existing home sales numbers for the same month are out on Friday. Other May survey data include the Philly Fed indices and flash PMIs (both Thursday). But the most notable release of the week will be the minutes of the FOMC's April meeting (Wednesday).

UK

Housing survey signals significant weakness ahead

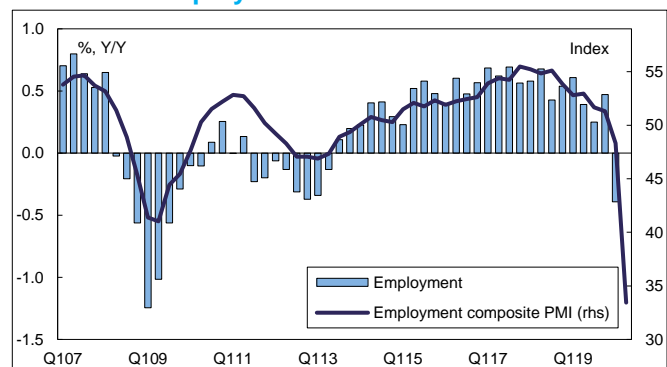
With the housing market having effectively come to a standstill during lockdown, yesterday's RICS survey unsurprisingly presented a bleak assessment of the near-term outlook for the residential market. Indeed, while the headline price balance remained above the low seen in early 2019, at -21%, it was still down more than 30pts from March and pointing to significant price declines. The detail of the report was equally downbeat in what it suggested about the near-term outlook. For example, 80% of surveyors had seen buyers or sellers pull out of transactions over the past month. And despite record low interest rates, sales were expected to remain extremely weak over the near term, with vendors on average anticipating that it would take around six months to return to pre-shutdown levels, and a pickup in prices likely to take longer. Indeed, while a little more than 60% of respondents suggested that a stamp duty holiday might boost sales, they foresaw no impact on prices. Overall, the majority of vendors expected to see a sharp fall in house prices when the market reopened after lockdown, with around 35% forecasting an initial drop of up to 4%, while a further 40% thought it would be larger. While the ONS has temporarily suspended the publication of its House Price Index after the March figures have been released, the RICS survey broadly supports the BoE's judgement for housing market developments under its illustrative economic

Euro area: Goods trade



Source: Thomson Reuters and Daiwa Capital Markets Europe Ltd.

Euro area: Employment*



*Employment PMI for Q220 is outturn for April 2020. Source: Markit, Thomson Reuters and Daiwa Capital Markets Europe Ltd.

scenario published in its Monetary Policy Report. Indeed, the Financial Policy Committee assessed this to be consistent with a peak-to-trough drop in house prices of 16%, with only a gradual recovery thereafter. Moreover, in the event that higher corporate failures push the unemployment rate up an additional 2% above the envisaged peak around 9% this quarter, the BoE suggests that could prompt a further 7% drop in house prices.
















The week ahead in the UK

After a quiet start, the coming week in the UK will bring several top-tier data releases, including the latest reports on the labour market (Tuesday), inflation (Wednesday), retail sales and public finance (both Friday), as well as the May flash PMIs (Thursday). Among the labour market data, the claimant count rate, which will be for April, will provide a better guide to the rise in joblessness during the pandemic than the ILO figure, which will be for the prior month and will be distorted by a drop in participation. However, the 7.5mn workers furloughed under the government's Job Retention Scheme will not show up in either figure. Meanwhile, the inflation figures for April will likely show a notable drop in the headline CPI rate from 1.5%Y/Y to below 1.0%Y/Y (albeit perhaps only just) for the first time since 2016. While prices of petrol and household energy will lead the decline, core inflation is likely to decline from 1.6%%Y/Y in March due to very subdued demand.

Following April's record weakness (the composite PMI fell more than 22pts to just 13.8), the flash PMIs are likely to suggest a modest improvement in activity in May as firms found ways to work around the lockdown measures and looked forward to an easing of restrictions. However, they will remain exceedingly low. Meanwhile, April's retail sales figures will report a new record drop of more than 10%M/M following the previous record drop of 5.8%M/M in March. And April's public finance figures will reveal a massive blowout in the deficit, albeit one which is very difficult to predict with accuracy. With the government having extended the Job Retention Scheme to October, and some guarantees on business loans already being called, the OBR yesterday increased its baseline forecast for public sector net borrowing in the current fiscal year to a record £298.4bn, £25.5bn higher than its projection published just a month ago.

In the absence of any significant economic news, the next edition of the Euro wrap-up will be published on 19 May 2020.

Daiwa economic forecasts









| | 2019 | | 2020 | | | | 2019 | 2020 | 2021 |
|---|-------|-------|-------|-------|-------|-------|-------|-------|-------|
| | Q3 | Q4 | Q1 | Q2 | Q3 | Q4 | | | |
| GDP growth, %, Q/Q | | | | | | | | | |
| Euro area  | 0.3 | 0.1 | -3.8 | -14.0 | 7.0 | 3.0 | 1.2 | -10.0 | 6.5 |
| Germany  | 0.3 | -0.1 | -2.2 | -10.0 | 6.0 | 3.0 | 0.6 | -6.0 | 5.2 |
| France  | 0.3 | -0.1 | -5.8 | -18.0 | 9.0 | 6.0 | 1.3 | -13.5 | 10.0 |
| Italy  | 0.1 | -0.3 | -4.7 | -18.0 | 7.0 | 2.0 | 0.3 | -14.5 | 4.3 |
| Spain  | 0.4 | 0.5 | -5.2 | -18.0 | 9.0 | 4.5 | 2.0 | -13.0 | 8.2 |
| UK  | 0.5 | 0.0 | -2.0 | -20.0 | 10.0 | 4.0 | 1.4 | -12.0 | 7.5 |
| Inflation, %, Y/Y | | | | | | | | | |
| Euro area | | | | | | | | | |
| Headline CPI  | 1.0 | 1.0 | 1.1 | -0.1 | -0.3 | -0.4 | 1.2 | 0.1 | 0.6 |
| Core CPI  | 0.9 | 1.2 | 1.1 | 0.3 | -0.4 | -0.6 | 1.0 | 0.1 | 0.3 |
| UK | | | | | | | | | |
| Headline CPI  | 1.8 | 1.4 | 1.7 | 0.6 | 0.2 | 0.1 | 1.8 | 0.6 | 0.7 |
| Core CPI  | 1.7 | 1.6 | 1.6 | 1.2 | 0.7 | 0.5 | 1.7 | 1.0 | 0.5 |
| Monetary policy | | | | | | | | | |
| ECB | | | | | | | | | |
| Refi Rate %  | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 |
| Deposit Rate %  | -0.50 | -0.50 | -0.50 | -0.50 | -0.50 | -0.50 | -0.50 | -0.50 | -0.50 |
| Net asset purchases*  | 0 | 20 | 107 | 107 | 107 | 107 | 20 | 107 | 20 |
| BoE | | | | | | | | | |
| Bank Rate %  | 0.75 | 0.75 | 0.10 | 0.10 | 0.10 | 0.10 | 0.75 | 0.10 | 0.10 |
| Net asset purchases**  | 0 | 0 | 36 | 36 | 36 | 36 | 0 | 36 | 0 |

*Monthly target €bn, end of period. **Monthly target £bn, end of period.
Source: Bloomberg, ECB, BoE 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 |
|---------|--|--------|----------------------|--|-------------|--------------------|
| EMU |  GDP – second estimate Q/Q% (Y/Y%) | Q1 | -3.8 (-3.2) | -3.8 (-3.3) | 0.1 (1.0) | - |
| |  Preliminary employment Q/Q% (Y/Y%) | Q1 | -0.2 (0.3) | - | 0.3 (1.1) | - |
| |  Trade balance €bn | Mar | 23.5 | 17.0 | 25.8 | 25.6 |
| Germany |  GDP – first estimate Q/Q% (Y/Y%) | Q1 | -2.2 (-2.3) | -2.2 (-2.0) | 0.0 (0.4) | -0.1 (-) |
| France |  Final CPI (EU-harmonised CPI) Y/Y% | Apr | 0.3 (0.4) | 0.4 (0.5) | 0.7 (0.8) | - |
| Italy |  Industrial orders M/M% (Y/Y%) | Mar | -26.5 (-26.6) | - | -4.4 (-2.6) | -4.1 (-2.5) |
| |  Industrial sales M/M% (Y/Y%) | Mar | -25.8 (-25.2) | - | -2.1 (0.9) | -1.7 (1.1) |
| |  Final CPI (EU-harmonised CPI) Y/Y% | Apr | 0.0 (0.1) | 0.0 (0.1) | 0.1 (0.1) | - |





Auctions

| Country | Auction |
|-----------------------|---------|
| - Nothing scheduled - | |



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 |
|---------|--|--------|-------------------|--|-----------|----------|
| Germany |  Final CPI (EU-harmonised CPI) Y/Y% | Apr | 0.9 (0.8) | 0.8 (0.8) | 1.4 (1.3) | - |
| Italy |  Total trade balance €bn | Mar | 5.7 | - | 6.1 | - |
| Spain |  Final CPI (EU-harmonised CPI) Y/Y% | Apr | 1.1 (-0.7) | -0.7 (-0.6) | 0.0 (0.1) | - |
| UK |  RICS house price balance % | Apr | -21 | -25 | 11 | 9 |


























Auctions

| Country | Auction |
|---------|---|
| UK |  sold £3.25bn of 0.625% 2025 bonds at an average yield of 0.037% |
| |  sold £2.25bn of 1.25% 2041 bonds at an average yield of 0.594% |

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

Coming week's data calendar

The coming week's key data releases

| Country | BST | Release | Period | Market consensus/ <i>Daiwa forecast</i> | Previous |
|------------------------------|---|---|--------|--|--------------|
| Monday 18 May 2020 | | | | | |
| - Nothing scheduled - | | | | | |
| Tuesday 19 May 2020 | | | | | |
| EMU |  | 07.00 EU27 new car registrations Y/Y% | Apr | - | -55.1 |
| |  | 10.00 Construction output M/M% (Y/Y%) | Mar | - | -1.5 (-0.9) |
| Germany |  | 10.00 ZEW current assessment balance (expectations) | May | -80.0 (31.0) | -91.5 (28.2) |
| Spain |  | 09.00 Trade balance €bn | Mar | - | -2.1 |
| UK |  | 09.30 Unemployment claimant count rate % (change '000s) | Apr | - | 3.5 (12.2) |
| |  | 09.30 Average earning including bonuses (excluding bonuses) 3M/Y% | Mar | 2.6 (2.6) | 2.8 (2.9) |
| |  | 09.30 ILO unemployment rate 3M% | Mar | 4.4 | 4.0 |
| |  | 09.30 Employment change '000s 3M/3M | Mar | 1 | 172 |
| |  | - CBI industrial trends survey, total orders (selling prices) | May | - | -56 (-11) |
| Wednesday 20 May 2020 | | | | | |
| EMU |  | 10.00 Final CPI (core CPI) Y/Y% | Apr | 0.3 (0.9) | 0.7 (1.0) |
| |  | 15.00 Preliminary consumer confidence | May | -22.0 | -22.7 |
| UK |  | 09.30 CPI (core CPI) Y/Y | Apr | 0.9 (1.3) | 1.5 (1.6) |
| |  | 09.30 PPI input prices (output prices) Y/Y% | Apr | - (-0.5) | -2.9 (0.3) |
| |  | 09.30 ONS house price index Y/Y% | Mar | - | 1.1 |
| Thursday 21 May 2020 | | | | | |
| EMU |  | 09.00 Preliminary manufacturing (services) PMI | May | 38.0 (23.8) | 33.4 (12.0) |
| |  | 09.00 Preliminary composite PMI | May | 23.7 | 13.6 |
| Germany |  | 08.30 Preliminary manufacturing (services) PMI | May | 39.0 (24.0) | 34.5 (16.2) |
| |  | 08.30 Preliminary composite PMI | May | 33.0 | 17.4 |
| France |  | 08.15 Preliminary manufacturing (services) PMI | May | 36.0 (24.0) | 31.5 (10.2) |
| |  | 08.15 Preliminary composite PMI | May | 37.0 | 11.1 |
| UK |  | 09.30 Preliminary manufacturing (services) PMI | May | 35.0 (20.0) | 32.6 (13.4) |
| |  | 09.30 Preliminary composite PMI | May | 16.0 | 13.8 |
| Friday 22 May 2020 | | | | | |
| UK |  | 07.00 Retail sales including fuel M/M% (Y/Y%) | Apr | -16.0 (-21.7) | -5.1 (-5.8) |
| |  | 07.00 Retail sales excluding fuel M/M% (Y/Y%) | Apr | -14.0 (-12.3) | -3.7 (-4.1) |
| |  | 09.30 Public sector net borrowing £bn | Apr | 30.7 | 3.1 |

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

The coming week's key events & auctions

| Country | BST | Event / Auction |
|------------------------------|---|---|
| Monday 18 May 2020 | | |
| UK |  16.00 | BoE's Tenreyro scheduled to speak at a Webinar on the Covid-19 response |
| Tuesday 19 May 2020 | | |
| EMU |  15.00 | ECB Chief Economist Lane scheduled to speak at a Webinar on monetary policy |
| Wednesday 20 May 2020 | | |
| Germany |  10.30 | Auction: €4bn of 0% 2030 bonds |
| France |  09.50 | Auction: index-linked bonds |
| UK |  10.30 | Auction: 0.75% 2023 bonds |
| Thursday 21 May 2020 | | |
| UK |  10.00 | Auction: 0.125% 2028 index-linked bonds |
| |  10.00 | Auction: 4.25% 2032 bonds |
| Friday 22 May 2020 | | |
| EMU |  12.00 | ECB to publish monetary policy account of 29-30 Governing Council meeting |

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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