

# Euro wrap-up

## Overview

- Euro area government bonds made significant gains as data confirmed a record drop in euro area industrial production in April.
- Gilts were little changed as data confirmed a record drop in UK GDP in April and Governor Bailey said that the BoE was “ready to take action”.
- The coming week will bring the latest BoE monetary policy announcement as well as data on UK inflation, retail sales and unemployment, and euro area inflation.

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### Daily bond market movements

Bond	Yield	Change
BKO 0 06/22	-0.688	-0.022
OBL 0 04/25	-0.666	-0.028
DBR 0 02/30	-0.446	-0.029
UKT 0½ 07/22	-0.053	+0.008
UKT 0% 06/25	-0.005	+0.008
UKT 4% 12/30	0.200	+0.005

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

## Euro area

### Euro area IP drops at record rate in April

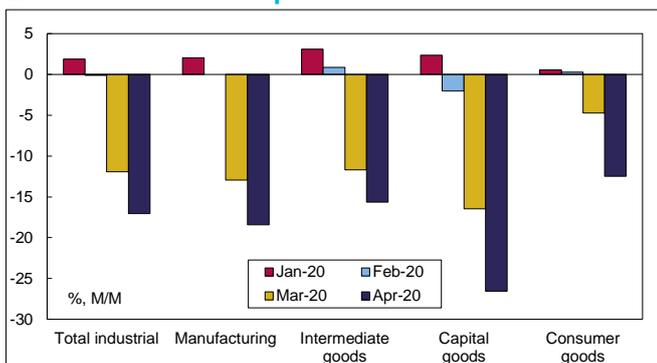
With April having seen activity among member states severely restricted by containment measures, and national releases earlier this week reporting significant double-digit percentage monthly declines, today's aggregate euro area industrial production figures were predictably weak. In particular, production fell by a record 17.1%/M/M in April, following a decline of 11.9%/M/M in March, to leave output 27% lower than the pre-covid peak and 28% lower than a year earlier. As flagged by the large member states, the most significant decline was seen in production of motor vehicles, down a whopping 85%/M/M, following a more than 40%/M/M drop in March to its lowest level by a considerable margin since the series began in 1991. So, overall production of consumer durables was down 29%/M/M, with a similar decline in capital goods production (-26½%/M/M). Output of intermediate goods was down a more 'modest' 15.6%/M/M, as was production of non-durables (-11.9%/M/M). With lockdown measures having been relaxed gradually through May, April will mark the trough. But with surveys still implying exceptionally weak levels of output and declining orders, while national car production figures were still very subdued in May, any near-term recovery in manufacturing output will be extremely restrained.

### French inflation revised higher, but still weak

Final May CPI data for France, also published today, came in above expectations. In particular, the 0.2ppt drop initially estimated in the EU-harmonised measure was revised away to leave headline inflation unchanged on the month at 0.4%/Y/Y, admittedly still the joint-softest reading since August 2016. Meanwhile, inflation on the national measure was estimated to have edged slightly higher on the month, by 0.1ppt to 0.4%/Y/Y. The upwards revision in the national measure in part reflected higher food price inflation (up 0.4ppt from the flash to 3.5%/Y/Y), as well as stronger services inflation, which rose to 1.2%/Y/Y in May, up 0.2ppt from the flash and 0.6ppt from April. As such, while prices of manufactured goods continued to decline (-0.7%/Y/Y), national core inflation rose 0.3ppt to 0.6%/Y/Y. Of course, there is still a significant amount of uncertainty with regards to the accuracy of the French price data, with INSEE noting that roughly four tenths of the basket had been estimated due to the impact of the coronavirus – the largest share of the large member states.

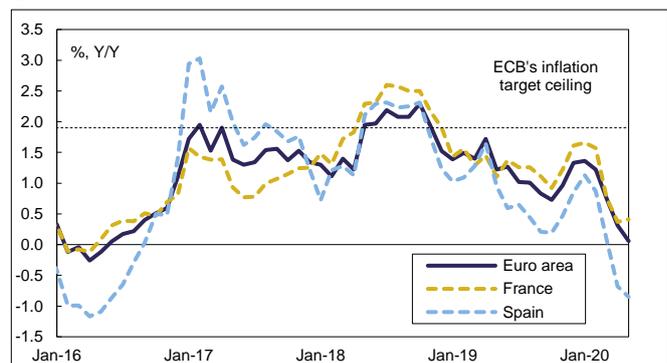
In contrast, final Spanish inflation was unrevised in May, confirming that inflation fell further on the back of lower energy prices, by 0.2ppt to -0.9%/Y/Y, the lowest since the first half of 2016. Indeed, excluding energy and food, core inflation moved sideways at 1.1%/Y/Y. Assuming minimal revisions the coming week's German and Italian figures (down 0.3ppt to 0.5%/Y/Y and 0.3ppt to -0.2%/Y/Y respectively), today's release suggests that we might well see a modest upwards revision to the final euro area headline figure (due Wednesday) from the 0.1%/Y/Y flash estimate. But this would still leave inflation at its lowest since August 2016 and at significant risk of slipping into negative territory over coming months.

### Euro area: Industrial production



Source: Thomson Reuters and Daiwa Capital Markets Europe Ltd.

### Euro area: Inflation\*



\*Flash estimate for May 2020 for the euro area.  
Source: Thomson Reuters and Daiwa Capital Markets Europe Ltd.



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## The coming week in the euro area and US

In the coming week, aggregate euro area data due for release include April trade figures on Monday, followed by construction output numbers for the same month and new car registrations for May on Wednesday. While the car registrations data will be improved from April's record decline, they will remain extremely weak – according to the VDA, German new car registrations were down 50%Y/Y in May following a drop of 61%Y/Y the prior month. Wednesday also brings the aforementioned release of final euro area CPI data for May. There is a risk that headline inflation will be revised slightly higher from the preliminary estimate, which showed that inflation fell from 0.3%Y/Y to 0.1%Y/Y, the lowest rate since 2016. Core inflation might also be nudged higher from the flash figure of 0.9%Y/Y. Final May inflation figures for Italy and Germany will be published on Monday and Tuesday respectively.

In terms of other member state releases, Germany's ZEW investor sentiment survey (due Tuesday) is expected to reveal a further improvement in investor morale in June on the back of the additional fiscal stimulus package and as optimism grows for (admittedly gradual) recovery in the region over the second half of the year. But while the expectations balance is expected to rise to the highest since January 2014, the current situation balance is expected to remain close to record lows. This release will be followed by Italian data for April on industrial orders on Wednesday and trade on Thursday. On the supply side, Germany will sell €5bn of 10Y Bunds on Tuesday, while France will auction fixed-rate and index-linked bonds on Thursday.

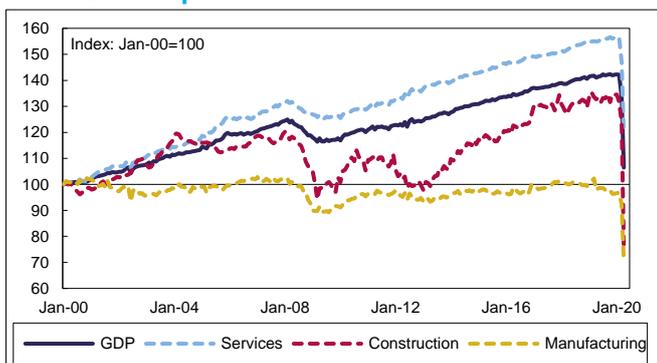
In the US, a key event in the first half of the coming week will be Fed Chair Powell's semi-annual testimony to the Senate's Banking Committee on Tuesday, which will be repeated before Congress on Wednesday. Data-wise, Monday brings the release of the Empire Manufacturing index for June and TICs capital flow data for May. But more interesting will be Tuesday's release of retail sales and industrial production data for May. These are likely to show only moderate improvement from the extreme weakness reported in April, with significantly less than half of the respective declines that month likely to be reversed. That day will also bring the NAHB housing index for June, followed on Wednesday by housing starts for May. The usual weekly claims numbers are due on Thursday, when we will also get the Philadelphia Fed Index for June and leading indicators for May. Meanwhile, the latest current account figures will be released on Friday. In the markets, the US Treasury will auction \$17bn of 20Y bonds on Wednesday and \$15bn of 5Y TIPS on Thursday.

## UK

### GDP down to mid-2002 level

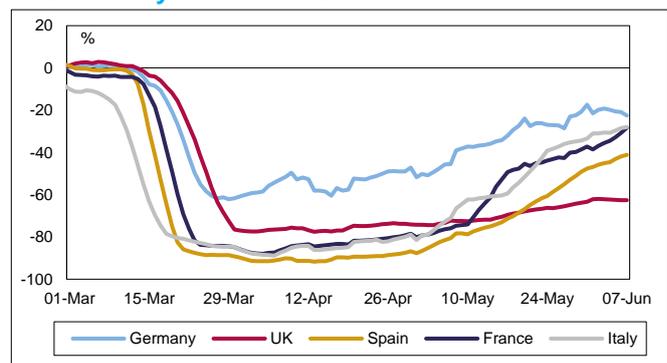
With lockdown measures applying throughout the month, UK GDP plunged 20.4%M/M in April to its lowest level since July 2002. Given the decline of 5.8%M/M in March when restrictions were first introduced, as well as a slight drop in February, economic output was down a little more than 25% from the pre-covid peak in January. That compares to a peak-to-trough decline of "only" about 7% during the global financial crisis. Almost all categories of production inevitably fell sharply in April. Output in construction was down 40.1%M/M (and 43.6% from February), while manufacturing dropped 24.3%M/M (and 27.8% from February) and services fell 19.0%M/M (24.0% from February) – all declines of record proportion. Among the various services, with pubs, restaurants, etc. shut, hospitality was down almost 90%M/M in April. With schools closed, education was down more than one third, as were the arts and leisure subsectors. Activity in wholesale, retail, transport and storage was down more than one quarter. And even output of health and social care was down by more than one fifth. Within the manufacturing sector, with car factories effectively shut, output of motor vehicles was down more than 90%M/M in April. But capital goods production was also down more than one third, and all major categories fell bar pharmaceuticals, which rose by almost one fifth.

### UK: GDP and production levels



Source: Thomson Reuters and Daiwa Capital Markets Europe Ltd.

### UK: Journeys for retail and recreation\*



\* % change from pre-coronavirus average, 7-day rolling average. Source: Google Global Mobility Report and Daiwa Capital Markets Europe Ltd.

## UK facing biggest hit of all developed economies

With the gradual easing of lockdown measures, UK economic output will have increased in May and June. However, with most non-essential stores only set to reopen from 15 June, and pubs, restaurants, most school classes, and many other services still shut, UK GDP still looks likely to decline by more than in any other developed economy in Q2. Various high-frequency data, such as those related to [credit-card spending](#), travel, restaurant reservations and shopping centre footfall support that judgement. We continue to pencil in a drop of more than 15%Q/Q in Q2. That is somewhat better than the BoE's initial estimate of a fall close to 25%Q/Q. But it would nonetheless be the sharpest decline on the series going back to the 1920s. And it would set the stage for the biggest full-year drop in GDP in more than 300 years.

So, while we expect the BoE to ease policy further on Thursday, the UK government is also set to follow its counterparts in Germany and France and announce in due course additional fiscal action to support activity over coming quarters.

## Gloomy outlook for exports after precipitous drop in April

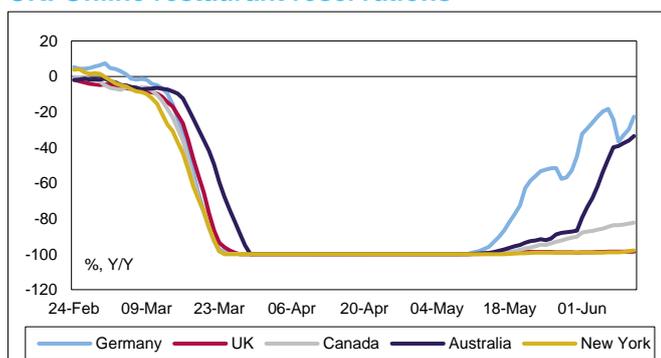
The shock to trade was similarly huge in April. Goods exports fell almost 15%M/M in April while goods imports dropped almost 22%M/M, with shipments of machinery and transport equipment hardest hit. And services trade was even more significantly affected, with exports down more than 24%M/M and imports falling more than 37%M/M. So, the trade balance improved to a modest surplus of £0.3bn from a deficit of £4.0bn in March. Nevertheless, on a three-month basis, exports were hit significantly harder than imports. And so the total trade balance, excluding the distorting effects of shifts in non-monetary gold and other precious metals, deteriorated in the three months to April to a deficit of £1.2bn. As demand recovers, imports will likely outpace exports, and so we expect a deficit to persist throughout the second half of the year. Meanwhile, looking further ahead to the start of next year, yesterday the UK government finally appeared to ditch plans to introduce full border checks on goods arriving from the EU from 1 January, whether or not a trade agreement is reached. That 'light-touch' regime should ensure the continued unimpeded flow of imports from the continent. However, UK exports of goods to the EU will likely face substantive new checks. And the implied costs of such non-tariff barriers will, at the margin, reduce demand for UK exports, compounding any impact of new tariffs that might also apply. Certainly, the outlook for UK exports looks downbeat due to the lasting and highly damaging twin shocks of Covid-19 and Brexit.

## The coming week in the UK

All eyes in the coming week will be on the BoE's monetary policy announcement on Thursday, now back to the usual time of 12:00 BST. While the MPC over recent months eased policy in several ways to support the economy – including reducing Bank Rate to an all-time low of 0.1%, restarting QE and implementing a new lending facility – the extreme hit to activity in March and April and downbeat outlook would suggest that more stimulus is required. Indeed, responding to the GDP data, Governor Andrew Bailey stated that the Bank had to be "ready to take action". With the current asset purchase target set to be reached by the start of next month, we think the MPC will announce at least £100bn of extra Gilt purchases. However, the prospect of persistently low inflation might well intensify the debate among policy makers of the need for additional measures. So, a further cut in Bank Rate to zero on this occasion cannot be ruled out, nor can amendments to the Term Funding Scheme to support lending to SMEs.

On the data front, the coming week brings several top-tier releases, including the latest labour market (Tuesday), inflation (Wednesday), retail sales and public finances figures (both Friday). Within the labour market report, the claimant count is expected to rise further in May, albeit less than the record 856.5K jump in April given that almost 8mn workers continued to receive separate support while furloughed under the government's Job Retention Scheme at the end of last month. Meanwhile, the ILO unemployment rate is expected to have jumped 0.7ppt to 4.6% in the three months to April. The inflation figures for May are expected to show a further 0.2ppt drop in the headline CPI rate to 0.6%Y/Y, due principally to lower petrol and household energy prices. But amid very subdued demand core inflation is also likely to have fallen from 1.4%%Y/Y in April. Friday's retail sales figures are likely to show very modest recovery in May, following a record drop of 18%M/M in April,

### UK: Online restaurant reservations\*



\*% change in bookings, 7-day rolling average. Source: Open Table and Daiwa Capital Markets Europe Ltd.

### Europe: Covid-19 cases and fatalities

		Total	Daily new infections*	Peak daily infections	Peak date	Daily fatalities*
UK		292,860	1,656	16,051	20-Apr	222
France		193,169	584	17,164	16-Apr	46
Spain		242,707	340	22,237	30-Mar	1
Germany		186,933	402	16,014	30-Mar	25
Italy		236,142	329	16,906	23-Mar	81

\*Weekly average to 12-Jun. Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

as Covid-19 restrictions eased only gradually. And May's public finance figures will reveal another month of massive borrowing, probably only ever surpassed by April's record level. Finally, in the markets, the DMO will auction 4Y and 10Y bonds on Tuesday, followed by 3Y and 21Y bonds on Wednesday.

## Daiwa economic forecasts

	2019		2020				2019	2020	2021
	Q3	Q4	Q1	Q2	Q3	Q4			
<b>GDP growth, %, Q/Q</b>									
Euro area 	0.3	0.1	-3.8	-12.0	6.3	3.5	1.2	-8.6	5.4
Germany 	0.3	-0.1	-2.2	-7.5	3.0	2.0	0.6	-5.9	3.5
France 	0.3	-0.1	-5.3	-15.0	9.0	5.5	1.5	-11.1	6.8
Italy 	0.1	-0.2	-5.3	-14.0	7.0	3.0	0.3	-11.9	5.1
Spain 	0.4	0.5	-5.2	-16.0	9.0	5.0	2.0	-11.4	7.9
UK 	0.5	0.0	-2.0	-17.0	8.0	4.0	1.4	-10.1	5.4
<b>Inflation, %, Y/Y</b>									
Euro area									
Headline CPI 	1.0	1.0	1.1	0.2	0.1	-0.1	1.2	0.3	0.8
Core CPI 	0.9	1.2	1.1	0.8	0.3	0.1	1.0	0.6	0.4
UK									
Headline CPI 	1.8	1.4	1.7	0.7	0.3	0.3	1.8	0.8	0.8
Core CPI 	1.7	1.6	1.6	1.3	0.9	0.5	1.7	1.1	0.5
<b>Monetary policy</b>									
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	20	140	140	140	20	140	50
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	58	58	58	0	58	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 	Industrial production M/M% (Y/Y%)	Apr	<b>-17.1 (-28.0)</b>	-18.5 (-28.8)	-11.3 (-12.9)	<b>-11.9 (-13.5)</b>	
France 	Final CPI (EU-harmonised CPI) Y/Y%	May	<b>0.4 (0.4)</b>	0.2 (0.2)	0.3 (0.4)	-	
Spain 	Final CPI (EU-harmonised CPI) Y/Y%	May	<b>-0.9 (-0.9)</b>	-1.0 (-0.9)	-0.7 (-0.7)	-	
UK 	Monthly GDP M/M% (3M/3M%)	Apr	<b>-20.4 (-10.4)</b>	-18.7 (-10.0)	-5.8 (0.1)	-	
	Industrial production M/M% (Y/Y%)	Apr	<b>-20.3 (-24.4)</b>	-15.0 (-19.3)	-4.2 (-8.2)	-	
	Manufacturing production M/M% (Y/Y%)	Apr	<b>-24.3 (-28.5)</b>	-15.6 (-19.9)	-4.6 (-9.7)	-	
	Construction output M/M% (Y/Y%)	Apr	<b>-40.1 (-44.0)</b>	-25.0 (-31.3)	-5.9 (-7.1)	-	
	Index of services M/M% (3M/3M%)	Apr	<b>-19.0 (-9.9)</b>	-20.0 (-10.2)	-6.2 (-1.9)	-	
	Total trade balance (goods trade balance) £bn	Apr	<b>0.3 (-7.5)</b>	-5.5 (-11.0)	-6.7 (-12.5)	<b>-4.0 (-11.9)</b>	
Auctions							
Country	Auction						
- Nothing to report -							

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
<b>Monday 15 June 2020</b>					
EMU		10.00 Trade balance €bn	Apr	-	23.5
Italy		09.00 Final CPI (EU-harmonised CPI) Y/Y%	May	-0.1 (-0.2)	0.0 (0.1)
UK		00.01 Rightmove house price index M/M% (Y/Y%)	Jun	-	-0.2 (2.1)*
<b>Tuesday 16 June 2020</b>					
EMU		10.00 Labour costs Y/Y%	Q1	-	2.4
Germany		07.00 Final CPI (EU-harmonised CPI) Y/Y%	May	0.6 (0.5)	0.9 (0.8)
		10.00 ZEW current assessment balance (expectations)	Jun	-80.0 (60.0)	-93.5 (51.0)
UK		07.00 Claimant count rate % (change '000s)	May	-	5.8 (856.5)
		07.00 Average earnings including bonuses (excluding bonuses) 3M/Y	Apr	1.5 (1.9)	2.4 (2.7)
		07.00 ILO unemployment rate 3M%	Apr	4.6	3.9
		07.00 Employment change 3M/3M '000s	Apr	-110	210
<b>Wednesday 17 June 2020</b>					
EMU		07.00 EU-27 new car registrations Y/Y%	May	-	-76.3
		10.00 Final CPI (core CPI) Y/Y%	May	0.2 (0.9)	0.3 (0.9)
		10.00 Construction output M/M% (Y/Y%)	Apr	-	-14.1 (-15.4)
Italy		09.00 Industrial orders (sales) Y/Y%	Apr	-	-26.6 (-25.2)
UK		07.00 CPI (core CPI) Y/Y%	May	0.6 (1.3)	0.8 (1.4)
		07.00 PPI input prices (output prices) Y/Y%	May	-8.6 (-1.2)	-9.8 (-0.7)
<b>Thursday 18 June 2020</b>					
Italy		09.00 Total trade balance €bn	Apr	-	5.7
UK		07.00 BoE Bank Rate %	Jun	0.10	0.10
		07.00 BoE gilt and corporate purchase bond target £bn	Jun	<u>745</u>	645
<b>Friday 19 June 2020</b>					
Germany		07.00 PPI Y/Y%	May	-0.3 (-2.1)	-1.9
UK		07.00 Retail sales including fuel M/M% (Y/Y%)	May	5.0 (-18.4)	-18.1 (-22.6)
		07.00 Retail sales excluding fuel M/M% (Y/Y%)	May	3.7 (-15.9)	-15.2 (-18.4)
		07.00 Public sector net borrowing £bn	May	47.8	61.4

\*Previous figures are for April. Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

***In the absence of significant economic news, the next edition of the Euro wrap-up will be published on 16 June 2020***

### The coming week's key events & auctions

Country	BST	Event / Auction
<b>Monday 15 June 2020</b>		
- Nothing scheduled -		
<b>Tuesday 16 June 2020</b>		
UK		10.00 Auction: £3bn of 1.5% 2026 bonds
		11.30 Auction: £2bn of 4.75% 2030 bonds
<b>Wednesday 17 June 2020</b>		
Germany		10.30 Auction: €5bn of 2030 bonds
UK		10.00 Auction: £3.75bn of 0.125% 2023 bonds
		11.30 Auction: £2.25bn of 1.25% 2041 bonds
<b>Thursday 18 June 2020</b>		
EMU		09.00 ECB publishes its Economic Bulletin
France		09.50 Auction: 0% 2023 bonds
		09.50 Auction: 0% 2025 bonds
		09.50 Auction: 0% 2026 bonds
		09.50 Auction: 0.75% 2028 bonds
UK		10.50 Auction: €2.5bn of 0.1% 2026 index-linked bonds
		12.00 Bank of England interest rate and asset purchase programme target announcement
<b>Friday 19 June 2020</b>		
- Nothing scheduled -		

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

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