

# Euro wrap-up

## Overview

- While the latest ifo survey suggested improvement in Germany's economy, Bunds made gains as Christine Lagarde stated publicly that "the ECB is closely monitoring the evolution of longer-term nominal bond yields".
- Gilts also made gains as UK PM Johnson announced plans for a gradual reopening of the UK economy over the coming three months.
- Tuesday will bring the latest UK labour market data and final estimates of euro area inflation in January.

**Chris Scicluna**

+44 20 7597 8326

### Daily bond market movements

Bond	Yield	Change
BKO 0 03/23	-0.700	-0.006
OBL 0 04/26	-0.636	-0.022
DBR 0 02/31	-0.347	-0.038
UKT 1¼ 09/22	0.030	-0.017
UKT 0% 06/25	0.259	-0.015
UKT 4¾ 12/30	0.678	-0.018

\*Change from close as at 4:30pm GMT.

Source: Bloomberg

## Euro area

### Improved ifo survey points to pick-up in German momentum in Q1

While German GDP avoided contraction in Q4, rising a minimal 0.1%Q/Q, the recent extension of most nation-wide pandemic containment measures to 7 March made a contraction in the current quarter highly likely. However, although many business groups were critical of that decision to extend restrictions on activity, last [Friday's flash PMIs](#) for February saw Germany's composite PMI rise 0.5pt to 51.3, representing the eighth successive month above the key 50 level. And, today's ifo survey suggested a pickup in business optimism in the middle of the first quarter. Having in January dropped to a four-month low, the survey index of current business conditions rose 1.4pts in February to 90.6, in line with the Q4 average. And after the prior month dropping to a seven-month low, the index for expectations of conditions six-months ahead rose 2.7pts to 94.2, the highest since October. Overall, the ifo business climate index rose 2.1pts to 92.4, similarly a four-month high.

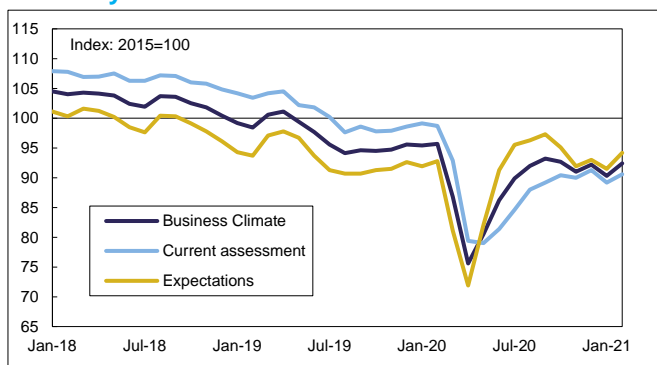
### Manufacturers most upbeat about the future since 2017

Just like the flash PMIs, however, today's survey results were highly uneven. And firms in many sectors are evidently feeling extremely uneasy as Chancellor Merkel continues to prepare her strategy for reopening the economy. Like the flash PMIs, the strengthening of momentum reported in the February ifo indices came largely from manufacturing, for which the headline business climate index rose to the highest since November 2018. Encouragingly, the ifo institute reported improvement across all major branches of the sector, suggesting, for example, that the concerns of auto firms about supply-chain disruption are alleviating. Indeed, manufacturers assessed current conditions to be the best since November 2019, and were the most upbeat about the coming six months since November 2017. Other sectors, however, appear far less ebullient.

### Limited optimism elsewhere as firms await Merkel's plans for reopening the economy

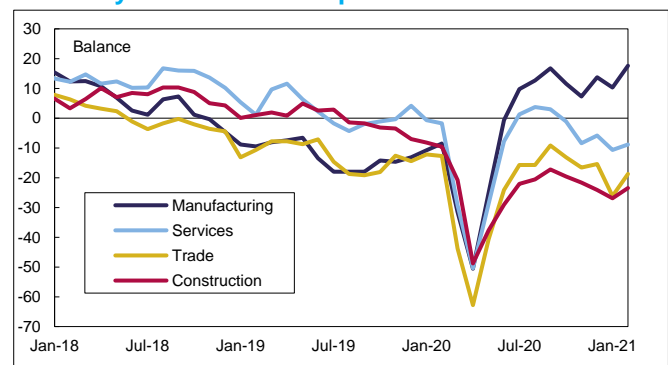
While they were not quite as downbeat as last month, service sector firms remained pessimistic about the coming six months. Indeed, even though the ifo institute reported cautious optimism in tourism, while hairdressers, restaurants and leisure are among the sub-sectors likely soon to benefit from Merkel's plans for reopening, the ifo expectations index for services was still well below the range from June to December last year. In addition, wholesale traders and retailers reported a weakening of sales over the past month while their outlook for the coming six months remained inferior to that at end-2020. And due to the recent harsh winter weather, construction firms reported the weakest current conditions since March 2017. However, while slightly more optimistic than at the turn of the year, they remained no less downbeat about the outlook than the average of the past year.

### Germany: ifo business climate indices



Source: Refinitiv and Daiwa Capital Markets Europe Ltd.

### Germany: ifo business expectations indices



Source: Refinitiv and Daiwa Capital Markets Europe Ltd.

## The day ahead in the euro area

Tomorrow brings the final estimate of euro area inflation which is expected to align with the flash release and confirm that the headline CPI rate jumped to 0.9%Y/Y in January, from -0.3%Y/Y previously, while the core inflation rate rose a record 1.2ppts to 1.4%Y/Y. The leap in inflation in January was broad-based. But it also largely reflects temporary factors, including a reweighting of the price basket to reflect changes to consumption patterns during the pandemic, the reversal of Germany's VAT cut, the introduction of Germany's carbon tax, the timing of France's winter sales, Spain's freak snow storms, and shifts in oil prices. Some of those effects, such as the German tax changes and oil price movements, will persist – and indeed magnify – over coming months. So, euro area inflation is likely to remain elevated throughout 2021, and will probably rise above 2.0%Y/Y in the second half of the year.

## UK

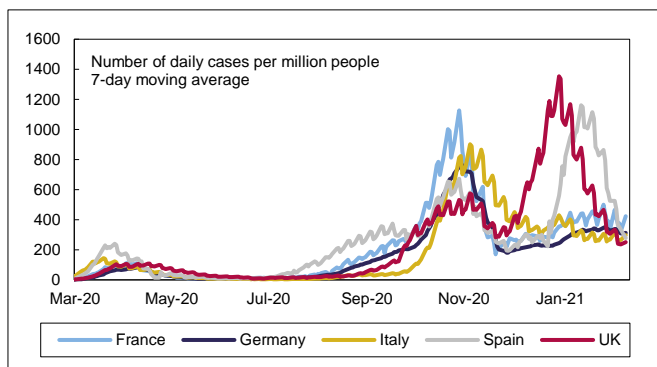
### Johnson plans very gradual economic reopening despite swift vaccine progress

Recent lockdown measures in the UK continue to demonstrate success in limiting the number of new coronavirus cases, for which on a seven-day moving average basis yesterday fell to the lowest since early October. The UK also continues to set the pace in Europe's coronavirus vaccine roll-out. As of yesterday, more than 17.5 million people – accounting for one in three adults – had received at least one jab. All over-50s will be offered at least one dose of vaccine by mid-April while all adults will be offered likewise by end-July. Nevertheless, this afternoon, UK Prime Minister Johnson announced a cautious plan for gradual reopening of the economy. Schools will reopen and some limited outdoors social activity will be permitted from 8 March, while certain outdoor sports activities will be able to resume from the end of next month. However, the reopening of non-essential stores and universities will not be permitted until after the Easter holiday in early April. And reopening of pubs and restaurants for indoor consumption, along with most of the tourist and indoor leisure industry, will not occur before mid-May. Office-workers will be discouraged from returning to the workplace before late June. So, following growth of 1.0%Q/Q in Q4, a contraction in UK GDP in the current quarter appears inevitable. And the recovery seems unlikely to gain vigour until the back end of Q2.

### The day ahead in the UK

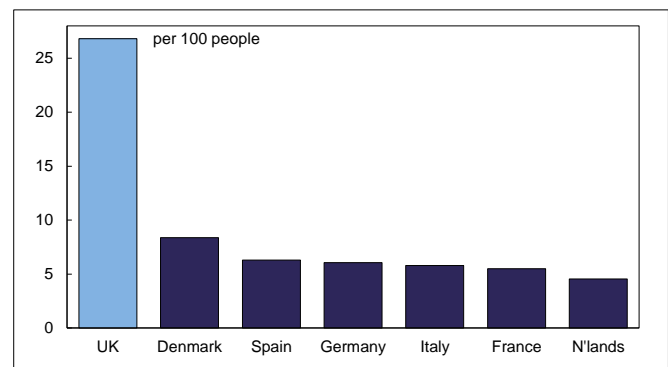
The week's UK economic data highlight comes tomorrow in the form of the labour market report, which is likely to show that the number of payrolls weakened at the start of the year due to the re-imposition of nationwide pandemic containment restrictions. In addition, the ILO unemployment rate is expected to rise 0.2ppt in the three months to December to 5.2%, which would be the highest level since September 2015. And ongoing job cuts will likely be reflected in a further monthly rise in the claimant count rate, which includes those working on low incomes or hours as well as those who are not working at all, from 7.4% in December. Tomorrow's CBI distributive trades survey for February will also be of some interest. With Covid containment restrictions in place and consumer confidence deteriorating, retail sales are expected to have remained weak this month after the sharper-than-expected drop in January.

### Coronavirus cases





Source: John Hopkins, Bloomberg and Daiwa Capital Markets Europe Ltd.

### Coronavirus vaccinations\*














\*Number of single doses administered. Source: Politico 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
Germany	 IFO current assessment balance (expectations)	Feb	<b>90.6 (94.2)</b>	89.0 (91.6)	89.2 (91.1)	<b>- (91.5)</b>
	 IFO business climate	Feb	<b>92.4</b>	90.5	90.1	<b>90.3</b>
Auctions						
Country	Auction	- Nothing to report -				

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

Tomorrow's releases						
Economic data						
Country	GMT	Release	Period	Market consensus/ <i>Daiwa forecast</i>	Previous	
EMU	 10.00	Final CPI (core CPI) Y/Y%	Jan	0.9 (1.4)	-0.3 (0.2)	
Italy	 09.00	Industrial orders M/M% (Y/Y%)	Dec	-	-1.3 (5.3)	
	 09.00	Industrial sales M/M% (Y/Y%)	Dec	-	-2.0 (-4.6)	
UK	 07.00	Unemployment claimant count rate % (change '000s)	Jan	-	7.4 (7.0)	
	 07.00	Average earnings including bonuses (excluding bonuses) 3M/Y%	Dec	4.1 (4.0)	3.6 (3.6)	
	 07.00	ILO unemployment rate 3M%	Dec	5.1	5.0	
	 07.00	Employment change '000s, 3M/3M	Dec	-30	-88	
	 07.00	Preliminary output per hour Y/Y%	Q4	-	4.0	
	 11.00	CBI distributive trades survey, reported sales	Feb	-	-44	
Auctions and events						
Italy	 10.00	Auction: €2.5bn of 0% 2022 bonds				
UK	 10.00	Auction: £2bn of 0.625% 2050 bonds				

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

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