

# Euro wrap-up

## Overview

- While ECB policymakers again spoke of the need to closely monitor nominal yields, Bunds made significant further losses amid some positive economic data.
- Gilts also made big losses on another quiet day for economic news from the UK.
- Friday will bring the first estimates of inflation in February, from France and Spain.

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### Daily bond market movements

Bond	Yield	Change
BKO 0 03/23	-0.660	+0.036
OBL 0 04/26	-0.543	+0.072
DBR 0 02/31	-0.228	+0.079
UKT 1¼ 09/22	0.101	+0.082
UKT 0% 06/25	0.369	+0.099
UKT 4¾ 12/30	0.794	+0.066

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

Source: Bloomberg

## Euro area

### Bond sell-off continues despite ECB “closely monitoring” yields

Despite further comments from ECB policymakers flagging the Governing Council’s readiness to act to restrain yields, the euro area sovereign bond market sell-off continued today. Mindful of recent market developments, at the start of the week President Lagarde noted that “the ECB is closely monitoring the evolution of longer-term nominal bond yields”. And ECB Chief Economist Lane repeated those words today. But in a speech that expanded upon the ECB’s strategy for trying to maintain favourable financing conditions, Lane had a lot more to say about the issue. He underscored that “Ensuring that the risk-free yield curve remains at highly accommodative levels is a necessary (but not sufficient) condition for ensuring that overall financing conditions are supportive enough” to counter the adverse shock of the pandemic on the inflation outlook. And in that context, he added that the two key yield curves most relevant to the ECB in assessing conditions in the economy are the overnight index swap (OIS) curve and the GDP-weighted sovereign bond yield curve.

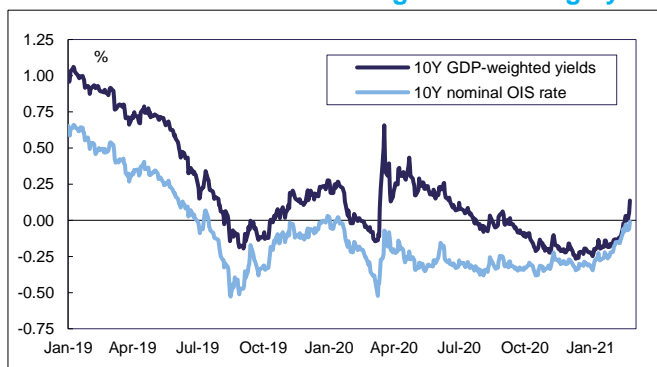
### Financial conditions still highly accommodative, so ECB won’t pull out all the stops (yet)

Of course, those curves have shifted significantly since late last year. Indeed, the 10Y GDP-weighted yield rose more than 8bps today to above 0.13%, the highest in more than eight months and up about 40bps from the recent low on 11 December. Nevertheless, by historical standards, those curves remain at low levels. And, while there are concerns about a recent tightening of lending standards in the banking sector as well as the strength of the euro, overall financial conditions remain highly accommodative thanks not least to exuberant equity markets. So, while Lane also emphasized that the ECB will “purchase flexibly according to market conditions”, and we might expect the ECB to accelerate its pace of buying over the short term, for the time being the Governing Council is more likely to try to slow, rather than halt altogether, the current uptrend in yields.

### Commission sentiment survey beats expectations, buoyed by hopes of an improved outlook

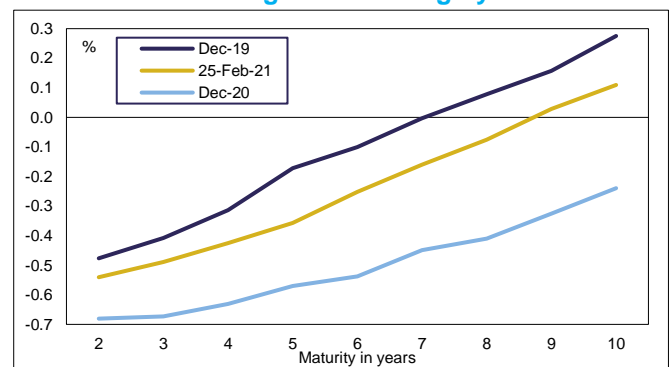
While they predictably highlighted contrasting fortunes between the different sectors, today’s European Commission economic sentiment indices (ESIs) beat expectations, with the headline euro area ESI rising almost 2pts in February to 93.4, the highest since last March. Of the big four member states, the headline ESIs declined only in Spain, with those for Italy and Germany rising by 3.0pts and 4.4pts respectively, benefiting particularly from the continued revival in manufacturing. Indeed, just as the manufacturing PMIs had surprised on the upside, the euro area industrial confidence indicator rose more than expected, reaching the highest since May 2019. Strikingly, the improvement was driven by production expectations and orders, which continued to rise relative to inventories, pointing to optimism about the outlook.

### Euro area: 10Y OIS & GDP-weighted sovereign yield



Source: ECB, Bloomberg and Daiwa Capital Markets Europe Ltd.

### Euro area: GDP-weighted sovereign yield curves\*



\*31-Dec-19, 11-Dec-20 and 25-Feb-21. Source: ECB, Bloomberg and Daiwa Capital Markets Europe Ltd.

## Services sentiment index edges up, contrasting with the PMIs

Contrasting with the message of the PMIs, however, the euro area services confidence indicator also improved, with a modest pick-up in demand expectations reported too. A slight further deterioration in retailers' confidence in the region masked a notable improvement in the expected business situation, while construction confidence edged very slightly higher. Meanwhile, the modest increase in euro area consumer confidence flagged by the flash estimate was confirmed. But the detail published today for the first time highlighted improved assessments of households' future financial conditions and expectations about the general economic situation, which likely supported the increase in expressed intentions to make further purchases. Overall, today's survey results don't change our view that euro area GDP dropped in Q1. But the increases in a range of forward-looking indicators reinforce optimism about prospects for Q2 and beyond.

## Price pressures flagged in manufacturing, less so elsewhere

Like other recent surveys, and tallying with sharp increases in prices of energy, commodities and shipping freight, as well as reports of supply-chain pressures, the Commission survey reported a sharp increase in manufacturing firms' selling price expectations. The Commission reported that these were most acute among producers of intermediate goods. Selling price expectations also rose in retail and construction, albeit with the respective indices remaining below the long-run averages, as did the indices for services, which was little changed on the month. And while they also increased slightly, the index of consumer price expectations for the coming twelve months also remained below its long-run average suggesting fears of a prolonged period of elevated inflation are currently overdone.

## Household and business bank deposits hit new highs

The Commission's survey also reported a renewed increase in willingness among consumers to save to the second-highest level since the pandemic struck. With spending in services and retail hit by continued lockdowns, but incomes relatively steady, that is no surprise. And today's monetary data from the ECB highlighted the ongoing substantive net inflow to bank deposits associated with such saving at the start of the year. In particular, there was a further strong net inflow of euro area household deposits of almost €60bn in January to take the stock above €7.7trn for the first time, with the annual growth rate up 0.4ppt to 9.1%Y/Y, the highest since the Global Financial Crisis in 2008. Meanwhile, the net inflow of deposits placed by non-financial corporations in the euro area edged up to close to €22bn, the highest since July, with the annual growth rate up more than 1ppt to a new series high of 21.8%Y/Y. The total stock of such deposits rose above €3trn for the first time, reflecting large liquidity buffers at many firms as well as an ongoing reticence to invest.

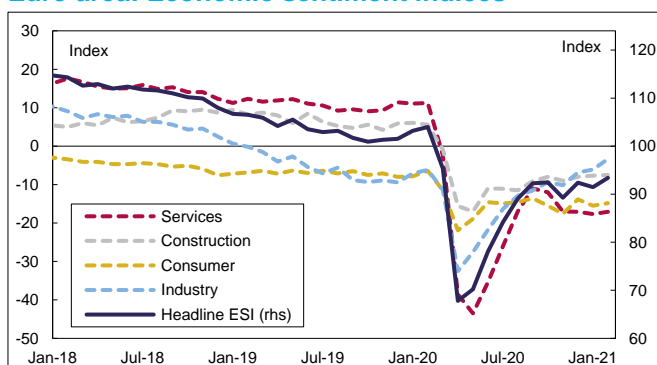
## Lending for house purchase remains firm, while firms continue to repay short-term debt

The ECB's monetary data revealed another solid month in lending to households at the start of this year, although the increase in the net flow on an adjusted basis slowed to €14bn. While loans for house purchase rose to a three-month high back above €20bn, households repaid consumer credit for a third month in a row. Growth in the stock of loans to households slowed just 0.1ppt on an adjusted basis to 3.0%Y/Y, the mode since April. In contrast, the stock of loans to non-financial corporations was unchanged, as firms paid back another €9bn of precautionary short-term loans (maturities less than one year) and €5bn of loans of maturities of between one and five years, but increased their borrowing of longer-term loans by €14bn. After adjusting for sales and securitisations, the stock of new loans to NFCs slowed just 0.1ppt to 7.0%Y/Y.

## The day ahead in the euro area

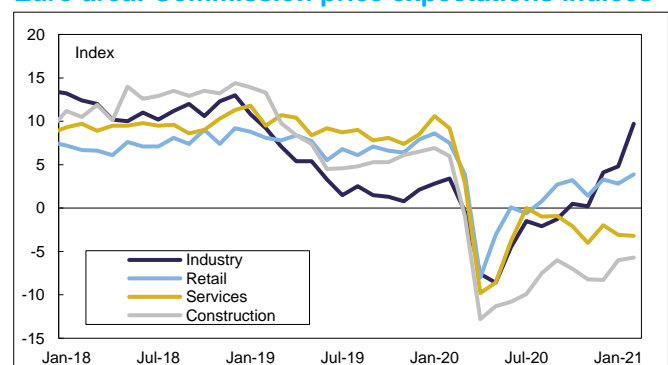
The focus tomorrow will be on the flash inflation estimates for February from France and Spain – the first to come from any member state – which will be closely watched given the steep increases across the euro area in January. The consensus on the Bloomberg survey is for an easing in the French inflation rate of 0.3ppt to 0.5%Y/Y (on the EU-harmonised basis), principally due to the change in timing of the winter sales on prices of clothes and certain other goods. In contrast, the

**Euro area: Economic sentiment indices**



Source: European Commission, Refinitiv and Daiwa Capital Markets Europe Ltd.

**Euro area: Commission price expectations indices**



Source: European Commission, Refinitiv and Daiwa Capital Markets Europe Ltd.

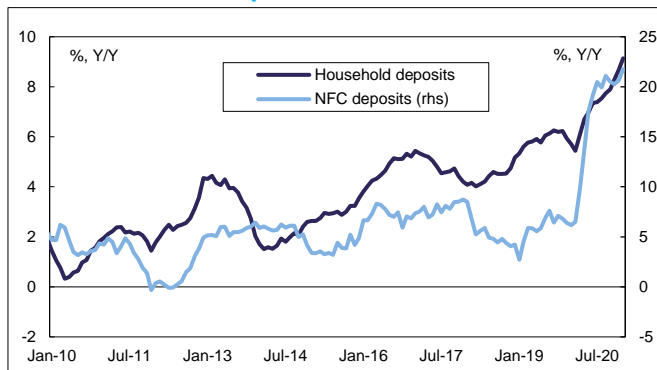
equivalent Spanish measure is expected to edge higher by 0.1ppt to 0.5%Y/Y, despite the easing of the harsh winter weather. Tomorrow also brings the release of French figures for consumer spending on goods, which are expected to reveal a fall in expenditure last month (-4.0%M/M), as pandemic restrictions continued to hamper household spending. Meanwhile, French Q4 GDP data are expected to align with the preliminary estimate, which fell 1.3%Q/Q (and 5.0%Y/Y). In other news, the G20 finance ministers and central bank governors will hold a virtual meeting.

## UK

### The day ahead in the UK

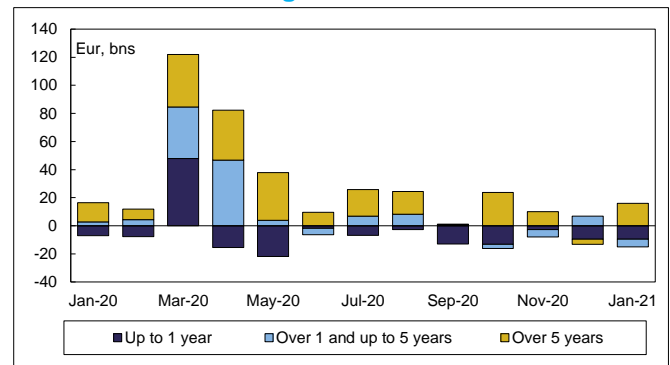
On the data front, tomorrow should be another quiet day for economic news from the UK, with only the Lloyd's business barometer scheduled for release. In January, the survey suggested that overall business confidence dipped, with the headline index falling by three points to -7, albeit some way off the low of -33 recorded in May last year. We will also hear from BoE Deputy Governor Ramsden and the currently bullish Chief Economist Haldane, the latter of whom is due to speak on the inflation outlook.

### Euro area: Bank deposits



Source: ECB, Refinitiv and Daiwa Capital Markets Europe Ltd.












### Euro area: Net lending to non-financial firms



Source: ECB, Refinitiv 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	 M3 money supply Y/Y%	Jan	12.5	12.5	12.3	12.4
	 Final European Commission's consumer confidence	Feb	-14.8	-14.8	-15.5	-
	 European Commission's industrial confidence (services)	Feb	-3.3 (-17.1)	-5.0 (-17.8)	-5.9 (-17.8)	-6.1 (-17.7)
	 European Commission's economic confidence	Feb	93.4	92.0	91.5	-
Germany	 GfK consumer confidence	Feb	-12.9	-14.0	-15.6	-15.5
France	 INSEE consumer confidence	Feb	91	92	92	-
Italy	 ISTAT consumer (manufacturing) confidence	Feb	101.4 (99.0)	101.0 (96.0)	100.7 (95.1)	-(95.6)
	 ISTAT economic confidence	Feb	93.2	-	87.9	88.3
Spain	 PPI Y/Y%	Jan	0.9	-	-1.4	-1.5
Auctions						
Country	Auction					
Italy	 sold €5bn of 0% 2026 bonds at an average yield of 0.11%					
	 sold €1.25bn of 2023 floating rate bonds at an average yield of -0.19%					

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

### Tomorrow's releases

Economic data						
Country	GMT	Release	Period	Market consensus/ <i>Daiwa forecast</i>	Previous	
France	 07.45	Consumer spending on goods M/M% (Y/Y%)	Jan	-4.0 (0.3)	23.0 (3.7)	
	 07.45	Preliminary CPI (EU-harmonised CPI) Y/Y%	Feb	0.3 (0.5)	0.6 (0.8)	
	 07.45	Final GDP Q/Q% (Y/Y%)	Q4	-1.3 (-5.0)	18.5 (-3.9)	
	 07.45	PPI Y/Y%	Jan	-	-1.2	
Spain	 08.00	Preliminary CPI (EU-harmonised CPI) Y/Y%	Feb	0.6 (0.5)	0.5 (0.4)	
UK	 00.01	Lloyd's business barometer	Feb	-	-7	
Auctions and events						
EMU	 08.30	ECB's Schnabel scheduled to speak				
UK	 10.00	BoE Chief Economist Haldane scheduled to speak on the inflation outlook				
	 -	BoE Deputy Governor Ramsden scheduled to speak				
Global	-	G20 finance ministers and central banks governors virtual meeting				

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

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