

Euro wrap-up

Overview

- After France tightened its pandemic containment measures and the coronavirus trend in Germany remained adverse, Bunds made gains despite a further jump in German producer price inflation.
- Despite a further improvement in UK consumer confidence, Gilts also made gains while the latest public borrowing figures again undershot expectations.
- The coming week brings the flash March PMIs along with updates on UK inflation, retail sales and the labour market.

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Daily bond market movements

Bond	Yield	Change
BKO 0 03/23	-0.707	-0.013
OBL 0 04/26	-0.648	-0.027
DBR 0 02/31	-0.296	-0.030
UKT 0 ¹ / ₈ 01/23	0.079	-0.019
UKT 0 ¹ / ₈ 01/26	0.381	-0.030
UKT 4 ³ / ₄ 12/30	0.836	-0.037

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

Source: Bloomberg

Euro area

Coronavirus trends raise downside risks to near-term economic outlook

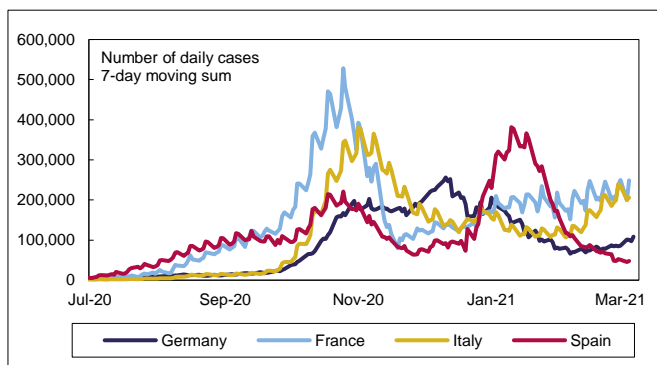
As in the other major economies, the near-term GDP outlook in the euro area remains highly dependent on the evolution of the pandemic and the extent to which vaccination programmes eventually allow an unwinding of containment measures. However, while current trends remain broadly favourable in the US and UK, that is not the case in the euro area. In its updated projections published last week, the ECB accepted that restrictions on activity would be more stringent in the first half of the year than it previously assumed. But its judgement that measures would be relaxed gradually from the end of Q1 and more swiftly in Q2 might still be overoptimistic. In many member states, with vaccination progress still sluggish, the trends in coronavirus cases are worsening and suggestive of a third wave. So, policy-makers are having to adjust their plans accordingly.

At the start of this week, regions accounting for two-thirds of Italians required non-essential retail, restaurants and schools to close until 6 April. Yesterday, French PM Castex announced that Paris and 15 other departments in France accounting for more than 40% of France's GDP would enter a third lockdown lasting four weeks. And in Germany, ahead of Monday's meeting between Chancellor Merkel and regional leaders to discuss containment measures, the Covid-19 seven-day incident rate has risen towards the key threshold (100 new cases per 100k people) at which policymakers had previously agreed to tighten restrictions. So, previous plans to reopen non-essential stores, gyms and the hospitality sector from 28 March seem likely to be shelved with a re-imposition of many measures in some regions likely to be the next step. Given the recent resilience of the economy to many lockdown measures, for the time being, we maintain our euro area GDP growth forecasts of -0.8%Q/Q in Q1 (versus the ECB's forecast of -0.4%Q/Q) and 1.4%Q/Q in Q2 (1.3%Q/Q for the ECB). However, the downside risks appear to have increased.

German producer price inflation up to highest in almost two years

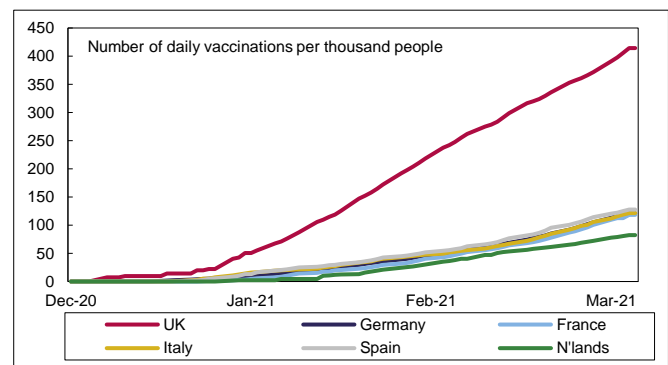
On a quiet end to the week for economic data from the region, German produce price figures for February cast light on some of the current inflationary pressures in the euro area's manufacturing sector. Industrial producer price inflation rose a steep 1.0ppt in February to 1.9%Y/Y, the strongest rate since May 2019. Given recent shifts in oil prices, unsurprisingly energy prices continued to add to pipeline price pressures, rising 3.7%Y/Y, up 3.0ppts on the month and the highest since May 2019. Germany's carbon pricing scheme compounded the impact of higher global energy prices, e.g. adding more than 10ppts to inflation of natural gas sold to large-scale industrial consumers (16.1%Y/Y). However, excluding energy, core producer price inflation still rose 0.5ppt to a two-year high of 1.4%Y/Y. For a second month, intermediate goods saw the

New coronavirus cases



Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

Coronavirus vaccinations



Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

sharpest price increases to be up 3.8%Y/Y, the most since late 2017. That principally reflected higher prices of secondary raw materials, up almost 50%Y/Y, with prices of metals including steel and alloys up more than 10%Y/Y on firmer demand, increased global prices of iron ore, and supply-chain challenges. Among other intermediate items, however, prices of electronic components were down 7.9%Y/Y and prices of fertilisers fell 3.5%Y/Y. And of the other major categories, inflation of durable consumer goods (1.4%Y/Y), capital goods (0.8%Y/Y) and non-durable consumer goods (-2.0%Y/Y) including food (-3.7%Y/Y) were still subdued. Energy price base effects will push producer price inflation higher over the next few months in Germany and the euro area as a whole. But we consider the pipeline pressures to be temporary and unlikely to trigger lasting upwards pressure in underlying consumer price inflation.

The week ahead in the euro area

Looking ahead, the economic data calendar in the coming week focuses on sentiment surveys, which are likely to continue to paint a picture of optimism in manufacturing but continued unease in services. In particular, the preliminary PMIs for March, which will be published on Wednesday, are expected to show the headline euro area manufacturing index move broadly sideways in March from a three-year high of 57.9 last month, with strong growth in Germany in particular. In contrast, the euro area services PMI is expected to remain below the key 50 expansion/contraction level having been little changed at 45.7 in February. Meanwhile, the European Commission's preliminary estimate of consumer confidence is expected to remain close to February's reading of -14.8, suggesting continued unease about the economic outlook. At the end of the week, however, the German ifo business survey for March is expected to reveal a further modest pickup in optimism at the end of the first quarter. Other national sentiment indicators to be published in the coming week include the French INSEE business confidence survey results for March and German GfK consumer sentiment report (Thursday) as well as the Italian ISTAT economic sentiment survey for the current month on Friday.

Beyond the surveys, industrial orders data for Italy are due for release on Tuesday, followed by final Q4 GDP data for Spain on Friday. The preliminary data revealed that Spanish GDP managed to grow in Q4, rising 0.4%Q/Q following growth of 16.4%Q/Q in Q3. That, however, still left Spanish GDP down a steep 9.1%Y/Y, again representing the biggest drop from the pre-Covid level of output in the euro area. In other news, ECB President Lagarde will speak on climate change and innovation issues respectively on Wednesday and Thursday, while Vice President Guindos and Executive Board member Schnabel are due to speak at virtual events on Thursday when the ECB will also publish its Economic Bulletin. On Thursday and Friday, EU Heads will meet for their latest summit with ECB President Lagarde taking part in the Euro Summit.

UK

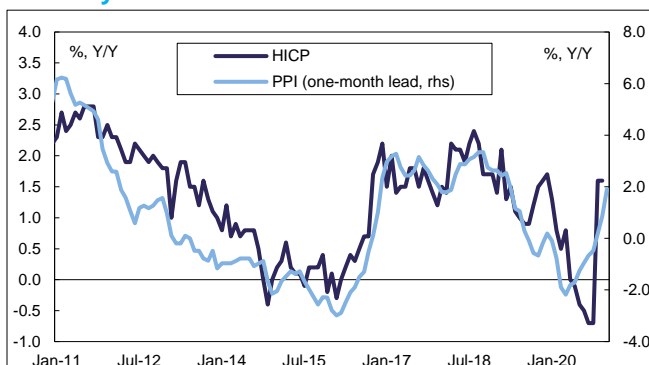
Consumer confidence up to a thirteen-month high

Yesterday's policy statement from the BoE noted several reasons for the MPC to be more upbeat about the near-term economic outlook. Among them was the likelihood that UK consumer spending was likely to be firmer than the BoE had anticipated due to the plans for a gradual relaxation of pandemic containment measures. The improved prospects for private consumption were underscored by today's GfK consumer confidence survey results for March, which reported an increase in the headline sentiment indicator that matched the largest since the outset of the pandemic. In particular, the headline consumer confidence indicator rose 7pts to -16, the highest in thirteen months, albeit still some 9pts below the pre-pandemic level. Within the detail, there were large increases in the indices measuring 12-month expectations for the economic situation and personal finances to the highest in three and four and a half years respectively. The reported improvement in the climate for making major purchases was more moderate, albeit taking the respective index to a thirteen-month high.

Another record month of public borrowing in February

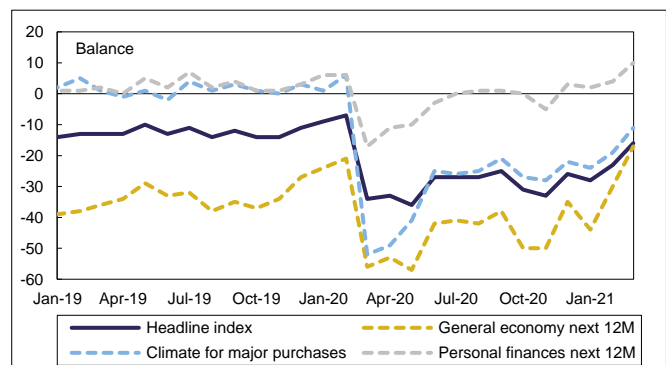
UK public borrowing last month inevitably rose to the highest for any February on the series. However, once again, it came in below expectations at £19.1bn excluding banks. Moreover, the estimate of borrowing over the first ten months of the current

Germany: Inflation measures



Source: Refinitiv and Daiwa Capital Markets Europe Ltd.

UK: Consumer confidence



Source: Refinitiv and Daiwa Capital Markets Europe Ltd.

fiscal year was revised down by £3.5bn to £266.7bn. The increase of more than £17bn in public borrowing from a year earlier was again principally due to extra expenditure, which was up more than £14.2bn (24.3%) year-on-year. Almost a quarter of that rise in spending was due to the Job Retention Scheme, while extra departmental expenditure – including on coronavirus vaccinations and the test-and-trace system – accounted for more than one third. Debt interest payments also picked up as higher inflation fed into payments on index-linked Gilt. In contrast, tax receipts again held up relatively well, falling just 1.4%Y/Y.

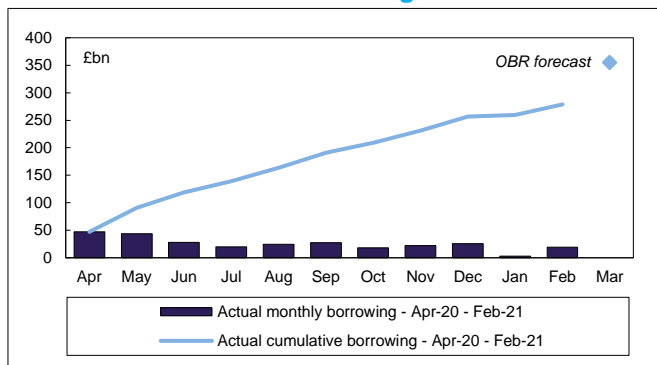
Borrowing in FY20/21 to undershoot OBR forecast but risks of overshooting ahead

Today's figures fail to incorporate estimates of future losses from the state-backed emergency loan guarantee schemes, which in due course will be recorded as public spending at the point at which the funds were issued. In the OBR's central forecast, these losses will add £23.6bn to public spending in the current fiscal year and a further £1.0bn in FY21/22. But even adjusting for such extra spending to come, the OBR's current full-year borrowing forecast of £354bn (about 16.9% of GDP) now looks too high. At the same time, as the government's current spending plans for coming years would require significant (and perhaps politically unpalatable) austerity for many public services. So, while a vigorous recovery over coming quarters could see borrowing fall a little more quickly than expected in FY21/22 (9.7% of GDP), we suspect that public borrowing will overshoot the OBR's forecasts in FY22/23 (4.5% of GDP) and beyond unless taxes are increased further than is currently planned.

The week ahead in the UK

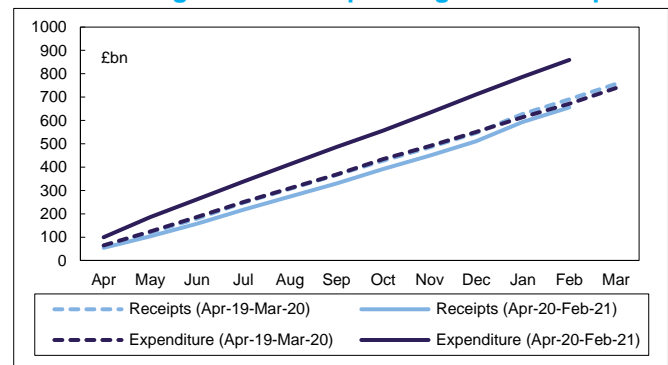
The coming week brings a number of top-tier economic data out of the UK, including the latest labour market report on Tuesday, inflation figures and flash PMIs on Wednesday followed by official retail sales figures on Friday. The headline CPI rate is expected to edge up 0.1ppt to a seven-month high of 0.8%Y/Y in February thanks to further upward pressure from rising energy prices, while the core measure is expected to remain unchanged at 1.4%Y/Y. We see inflation rising further over the summer months due not least to higher oil prices and expect it to peak in November above 2.5%Y/Y. Tuesday's labour market survey is expected to show that the ILO unemployment rate rose 0.1ppt in the three months to January to 5.2% – the highest level since September 2015 – but that ongoing support from the Job Retention Scheme left the number of payrolls little changed last month. Retail sales, meanwhile, are expected to have risen more than 1.0%M/M in February, after plummeting 8.8%M/M in January due to the tighter lockdown measures. And with consumer confidence rising, not least thanks to the ongoing successful coronavirus vaccine rollout in the UK, the outlook for private consumption looks somewhat brighter. Survey-wise, the preliminary manufacturing and services sector PMIs for March, to be published on Wednesday, will, as in the euro area, likely be little changed from February. In other news, on Wednesday BoE Governor Bailey will be a pre-recorded panelist discussing "Unlocking investment for net zero" at an Economist Sustainability Week event.

UK: Public sector net borrowing*



*Excluding banks. Source: ONS and Daiwa Capital Markets Europe Ltd.
















UK: Current government spending & tax receipts



Source: ONS and Daiwa Capital Markets Europe Ltd.




The next edition of the Euro wrap-up will be published on 23rd March 2021

Daiwa economic forecasts

		2020	2021				2022	2020	2021	2022
		Q4	Q1	Q2	Q3	Q4	Q1			
GDP growth, %, Q/Q										
Euro area		-0.7	-0.8	1.4	1.4	1.3	1.1	-6.8	3.5	4.4
Germany		0.3	-1.0	1.2	1.2	1.2	1.0	-5.3	2.5	4.0
France		-1.4	-0.5	1.2	1.4	1.2	1.2	-8.2	5.0	4.5
Italy		-1.9	-0.5	1.5	1.5	1.4	1.2	-8.9	4.0	4.7
Spain		0.4	-1.0	1.5	1.4	1.2	1.2	-11.0	3.9	5.0
UK		1.0	-2.0	3.1	2.7	2.2	1.5	-9.9	4.9	6.6
Euro area										
Headline CPI		-0.3	1.1	1.7	1.9	2.1	0.9	0.3	1.6	1.1
Core CPI		0.2	1.3	1.1	1.1	1.5	0.6	0.7	1.3	0.9
UK										
Headline CPI		0.5	0.9	1.9	2.0	2.4	2.3	0.9	1.8	2.0
Core CPI		1.3	1.5	2.0	2.0	2.1	2.0	1.4	1.9	1.9
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
PEPP envelope* (€bn)		1850	1850	1850	1850	1850	1850	1850	1850	1850
BoE										
Bank Rate %		0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10
Bond purchases** (£bn)		895	895	895	895	895	895	895	895	895

*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	
Germany	 PPI Y/Y%	Feb	1.9	2.0	0.9	-	
UK	 GfK consumer confidence	Mar	-16	-20	-23	-	
	 Public sector net borrowing, excl. Banks £bn	Feb	19.1	21.4	8.8	3.1	
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	GMT	Release	Period	Market consensus/ <i>Daiwa forecast</i>	Previous
Monday 22 March 2021					
EMU		09.00 ECB current account balance €bn	Jan	-	36.7
Italy		09.30 Current account balance €bn	Jan	-	6.7
Tuesday 23 March 2021					
Italy		09.00 Industrial orders M/M% (Y/Y%)	Jan	-	1.7 (7.0)
		09.00 Industrial sales M/M% (Y/Y%)	Jan	-	1.0 (-0.5)
UK		07.00 Unemployment claimant count rate % (change '000s)	Feb	-	7.2 (-20.0)
		07.00 Average earnings including bonuses (excluding bonuses) 3M/Y%	Jan	-	4.7 (4.1)
		07.00 ILO unemployment rate 3M%	Jan	5.2	5.1
		07.00 Employment change '000s 3M/3M	Jan	-167	-114
		11.00 CBI industrial trends survey, total orders	Mar	-20	-24
Wednesday 24 March 2021					
EMU		09.00 Preliminary manufacturing (services) PMI	Mar	57.8 (46.0)	57.9 (45.7)
		09.00 Preliminary composite PMI	Mar	49.1	48.8
		15.00 European Commission's preliminary consumer confidence	Mar	-14.5	-14.8
Germany		08.30 Preliminary manufacturing (services) PMI	Mar	60.5 (46.5)	60.7 (45.7)
		08.30 Preliminary composite PMI	Mar	51.6	51.1
France		08.15 Preliminary manufacturing (services) PMI	Mar	56.5 (45.5)	56.1 (45.6)
		08.15 Preliminary composite PMI	Mar	47.2	47.0
UK		07.00 CPI (core) Y/Y%	Feb	0.8 (1.4)	0.7 (1.4)
		07.00 PPI input prices (output prices) Y/Y%	Feb	2.5 (0.3)	1.3 (-0.2)
		09.30 Preliminary manufacturing (services) PMI	Mar	55.0 (50.8)	55.1 (49.5)
		09.30 Preliminary composite PMI	Mar	51.1	49.6
		09.30 House price index Y/Y%	Jan	8.0	8.5
Thursday 25 March 2021					
EMU		09.00 M3 money supply Y/Y%	Feb	12.5	12.5
Germany		07.00 GfK consumer confidence	Apr	-12.1	-12.9
France		07.45 Insee business confidence	Mar	91	90
		07.45 Insee manufacturing confidence (production outlook)	Mar	98 (-)	97 (-8)
Spain		08.00 PPI Y/Y%	Feb	-	0.9
UK		11.00 CBI distributive trades, reported sales	Mar	-	-35
Friday 26 March 2021					
Germany		09.00 Ifo current assessment (expectations)	Mar	91.3 (95.0)	90.6 (94.2)
Italy		09.00 Istat economic sentiment	Mar	-	93.2
		09.00 Istat consumer (manufacturing) confidence	Mar	100.0 (99.5)	101.4 (99.0)
Spain		08.00 Final GDP Q/Q% (Y/Y%)	Q4	0.4 (-9.1)	16.4 (-9.0)
UK		07.00 Retail sales including fuel M/M% (Y/Y%)	Mar	2.0 (-3.6)	-8.2 (-5.9)
		07.00 Retail sales excluding fuel M/M% (Y/Y%)	Mar	1.8 (-1.5)	-8.8 (-3.8)

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

The coming week's key events & auctions

Country	GMT	Event / Auction
Monday 22 March 2021		
EMU	 15.15	ECB's Schnabel chairs macro-finance conference session
Tuesday 23 March 2021		
UK	 10.00	Auction: £2.25bn of 1.75% 2049 bonds
	 11.50	BoE Governor Bailey participates in the Economist Sustainability week event (pre-recorded)
Wednesday 24 March 2021		
EMU	 15.40	ECB President Lagarde delivers pre-recorded message at conference on climate change
Germany	 10.30	Auction: €4bn of 0% 2031 bonds
UK	 11.30	Auction: £350mn of 0.125% 2056 index-linked bonds
Thursday 25 March 2021		
EMU	 09.00	ECB publishes Economic Bulletin
	 09.00	ECB President Lagarde speaks at BIS conference
	 17.00	ECB's Vice President de Guindos scheduled to speak
	 17.00	ECB's Schnabel scheduled to speak
Italy	 10.00	Auction: fixed rate and index-linked bonds
UK	 09.30	BoE publishes capital issuance – February 2021
Friday 26 March 2021		
EMU	 12.10	ECB President Lagarde participates in the Euro Summit

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

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