

Euro wrap-up

Overview

- Bunds made losses while French sovereign spreads widened as surveys suggested that credit standards on euro area bank loans have eased further and economic sentiment in France remains elevated.
- Gilts also made losses despite data confirming that UK public borrowing fell to a new post-crisis low.
- Ahead of Thursday's ECB policy announcement, the only euro area data of note will be the latest French consumer confidence survey.

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Daily bond market movements

Bond	Yield	Change*
BKO 0 03/19	-0.678	+0.013
OBL 0 04/22	-0.323	+0.032
DBR 0% 02/27	0.374	+0.046
UKT 1% 07/19	0.104	+0.021
UKT 0% 07/22	0.527	+0.027
UKT 4% 12/27	1.083	+0.032

*Change from close as at 4.30pm BST.
Source: Bloomberg

Euro area

Credit standards continued to ease in Q1

Ahead of this week's Governing Council meeting, in which policymakers seem likely to debate whether it's time to change the message on the future direction of monetary policy, and after banks loaded up with more than €230bn of extra liquidity at the final ECB TLTRO II last month, today's euro area bank lending survey might have been expected to illustrate how its measures are helping to boost the supply of credit to the economy. Certainly, financial conditions remain highly accommodative, and the survey reported that credit standards eased further in Q1 on loans to enterprises and households alike. However, competitive pressures appear to have played the most significant role, with margins on new loans narrowing across all loan categories against the backdrop of the negative deposit rate. And banks expect only a slight net tightening of credit standards on loans to enterprises and no further loosening on loans to households in Q2.

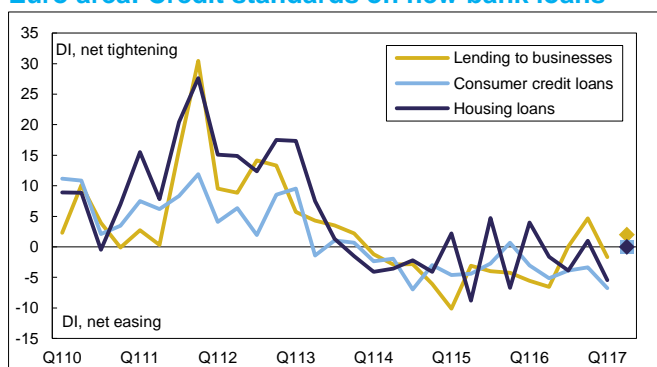
Loan demand rising, particularly from households

With the economic backdrop steadily improving and sentiment strong, demand for new loans unsurprisingly rose again in Q1, and is expected to rise further in Q2 too, albeit at rates down from the end of last year. In addition to the low general level of interest rates, the favourable outlook for the housing market was cited as a key reason for increased demand for housing loans while a rise in demand for durable goods and elevated consumer confidence were drivers of increased demand for consumer credit. Meanwhile, firms cited inventories, working capital and the level of interest rates as key in driving their decisions to increase demand for bank loans, while fixed investment intentions also played a more significant role than in previous quarters. But with many firms cash-rich and hence able to rely on internal financing, and others having increased their issuance of debt securities – perhaps in response to the ECB's corporate bond purchase programme – bank lending to non-financial corporations seems unlikely to accelerate markedly from the recent rates slightly in excess of 2%/Y.

French business sentiment remains elevated

With financial markets remaining upbeat after Sunday's first round of the French Presidential Election, France was also in focus on the data-front today, with the INSEE business climate indices for April adding to evidence that economic momentum in the second-largest euro area member state remains positive. The headline economic confidence indicator moved broadly sideways for the third month at 104, comfortably above its long-run average and just 1pt off December's near-six-year high. And while the services and retail trade indices eased slightly and construction sentiment was stable, the manufacturing confidence index leapt sharply to 108, the highest level since mid-2011. So, despite the uncertainty ahead of the election, all recent major business sentiment surveys, including the composite PMI which rose to a six-year high, suggest that growth was

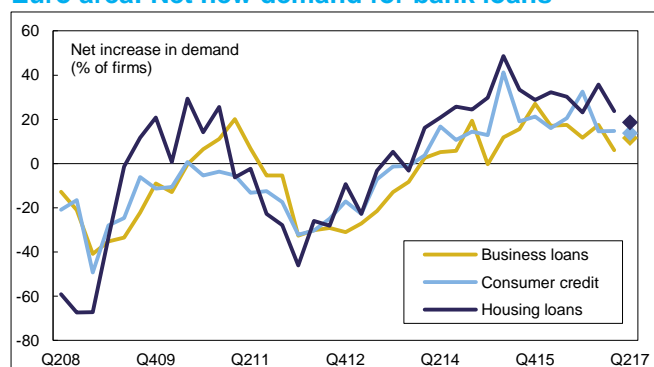
Euro area: Credit standards on new bank loans*



*Diamond represents DI forecast for Q217.

Source: ECB, Thomson Reuters and Daiwa Capital Markets Europe Ltd.

Euro area: Net new demand for bank loans*



*Diamond represents DI forecast for Q217.

Source: ECB, Thomson Reuters and Daiwa Capital Markets Europe Ltd.



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firm in Q1 – we expect first-quarter GDP growth, the first estimate of which is due for release on Friday, to have reached 0.4%Q/Q or higher. And with today's survey signalling that the start to Q2 was similarly strong, and with the likely victory of market-friendly Macron in the second round of the election perhaps set to boost private sector confidence even further, the French economy looks well set to maintain momentum.

The coming two days in the euro area and US

Wednesday is set to be a quiet day in the euro area, with the aforementioned French consumer confidence survey for April the most notable new data release – we expect sentiment to remain close to the near-decade high reached in each of the past three months. Germany's April consumer confidence survey is due the following day, and should also be consistent with buoyant sentiment within the range of recent months. Thursday will also bring the flash estimates of April inflation in Germany and Spain, which are likely to show increases from the previous month on account of the timing of the Easter holidays. Additionally, Italy will sell a range of government bonds.

Thursday's main event, of course, will be the conclusion of the ECB's latest Governing Council meeting. The message from last month's meeting had a more positive tone regarding the state of the euro area economy, and signalled less urgency for further monetary policy action. And with recent upbeat surveys suggesting a notable strengthening of economic recovery momentum, and the balance of risks in the euro area improved following the French election first round, the debate on the Governing Council might be lively, with some members likely judging that it is now appropriate to consider a change of strategy.

But while Draghi will have cause to be broadly optimistic about the outlook for growth and employment, as in his speech in Frankfurt earlier this month, he will insist that the persistent weakness of underlying inflation means that it would be premature to change policy yet. So, while some members wanted a more substantive change last month, this week we expect the ECB's forward policy guidance to be left unchanged, reaffirming that the Governing Council continues to expect rates "to remain at present or lower levels for an extended period of time, and well past the horizon of our net asset purchases". However, that wording seems highly likely to be revised once the ECB updates and probably upgrades its economic forecasts in June, after which the policymakers will start more actively to consider how to amend policy from the start of 2018, with an agreement on the precise way forward to come in September.

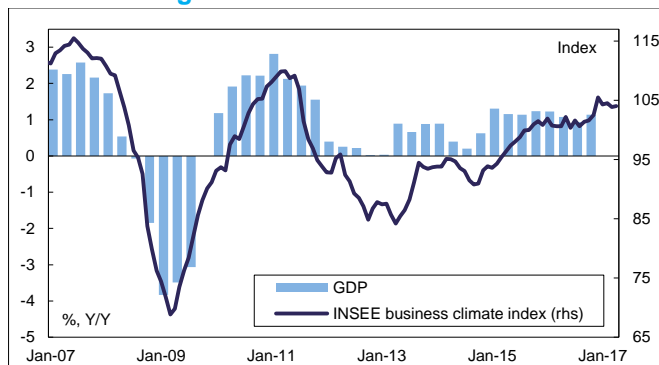
In the US, meanwhile, after a day bereft of noteworthy economic releases tomorrow, Thursday will bring the advance good trade report and durable goods orders figures for March, as well as pending home sales figures for the same month, the latest weekly jobless claims numbers and the Kansas Fed manufacturing activity index for April. Supply-wise, the US Treasury will sell 2Y floating-rate notes and 5Y notes on Wednesday and 7Y notes on Thursday.

UK

Public sector deficit falls to a new post-crisis low

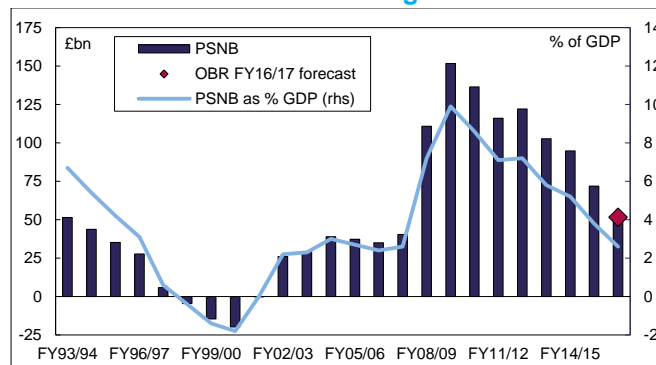
While today's public finance data came in slightly higher than expected, showing that net borrowing was £5.1bn in March, revisions to previous months left total net borrowing in the last financial year as a whole at £52.0bn, £20bn (27.8%) lower compared to FY15/16 and the lowest since FY07/08. And while borrowing slightly exceeded the OBR's November forecast of £51.7bn, it was £3.5bn lower than forecast in March 2016, despite the fact that GDP growth was subsequently weaker than expected. However, growth was tax-rich – compared to FY15/16 central government tax receipts increased in all major categories. Looking ahead, the coming General Election in June seems likely, assuming that the Conservative Party is re-elected, to remove some of the Government's current fiscal constraints, notably over pensions and a moratorium on increasing many personal taxes. And with Brexit looming ever closer and the economy already slowing on the back of weaker household spending, the Chancellor may well need all of that fiscal flexibility if he wants to have any chance of meeting his stated aim of balancing the budget early in the next decade.

France: GDP growth and business sentiment



Source: INSEE, Thomson Reuters and Daiwa Capital Markets Europe Ltd.

UK: Public sector net borrowing*



*Excluding public sector banks.

Source: ONS and Daiwa Capital Markets Europe Ltd.

The coming two days in the UK




No new UK economic data releases are due tomorrow. However, ahead of this Saturday's EU27 summit, where EU leaders are expected to adopt their official position for the forthcoming Brexit negotiations, Prime Minister Theresa May is scheduled to meet the European Commission President Jean-Claude Juncker and the EU's Chief Brexit Negotiator Michel Barnier. Since even before Article 50 was triggered EU leaders have been consistent and united in their approach, insisting that the UK will have to honour its financial commitments to the EU, will have to accept the jurisdiction of EU law, including free movement of people, during any transitional period, and that negotiations about the future trading relationship will start only after substantial progress with regards to matters relating to the separation from the EU is achieved. That has forced Theresa May to soften her tone somewhat – she seems to have accepted that a transitional phase will be needed and that the UK will have to allow free movement of labour to continue during that period (although she has yet to explicitly accept that ECJ oversight will also have to continue during that period). Meanwhile, the only data release of note on Thursday will be the CBI Distributive Trades survey, which is expected to indicate that momentum in the retail sector remained weak in April after a sharp drop in sales in the previous months.

The next edition of the Euro wrap-up will be published on 27 April 2017.

European calendar

Today's results



Economic data

Country	Release	Period	Actual	Market consensus/ Daiwa forecast	Previous	Revised
France	 Business confidence indicator (production outlook)	Apr	104 (1)	104 (3)	104 (3)	-
UK	 Public sector net borrowing excluding interventions £bn	Mar	5.1	3.1	1.8	0.1
Country	Auction					
Germany sold	 €3.2bn of 0% 2019 bonds (15-Mar-2019) at an average yield of -0.69%					

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

Tomorrow's data releases














Economic data

Country	BST	Release	Period	Market consensus/ <u>Daiwa forecast</u>	Previous
France	 07:45	Consumer confidence survey	Apr	100	100
Auctions and events					
Country	BST	Auction / Event			
UK	 10:30	Auction: To sell £800mn of 0.125% 2046 index-linked bonds (22-Mar-2046)			




Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

Thursday's data releases

Economic data

Country	BST	Release	Period	Market consensus/ <i>Daiwa forecast</i>	Previous	
EMU		10:00	Economic sentiment indicator	Apr	108.1	107.9
		10:00	Services (industrial) sentiment	Apr	12.9 (1.3)	12.7 (1.2)
		10:00	Final consumer confidence	Apr	-3.6	-5.0
		12:45	ECB refinancing rate %	Apr	<u>0.00</u>	0.00
		12:45	ECB deposit rate %	Apr	<u>-0.40</u>	-0.40
Germany		07:00	GfK consumer confidence survey	May	9.9	9.8
		13:00	Preliminary EU-harmonised CPI Y/Y%	Apr	1.9	1.5
Italy		09:00	Consumer confidence indicator	Apr	107.4	107.6
		09:00	Manufacturing (economic) confidence	Apr	107.3 (-)	107.1 (105.1)
Spain		08:00	Preliminary EU-harmonised CPI Y/Y%	Apr	2.3	2.1
		08:00	Unemployment rate %	Q1	18.6	18.6
UK		11:00	CBI Distributive Trades survey, retail sales	Apr	6	9
		15:00	BoE corporate bond purchases £bn	Weekly	-	9.7

Auctions and events

Auctions and Events			
Country		BST	Auction / Event
Italy		10:00	Auction: To sell up to €2.5bn of 1.2% 2022 bonds (01-Apr-2022)
		10:00	Auction: To sell up to €2.75bn of 2.2% 2027 bonds (01-Jun-2027)
		10:00	Auction: To sell up to €3.5bn of 2024 floating-rate bonds (15-Oct-2024)

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

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