

Euro wrap-up

Overview

- Bunds were little changed as German industrial output figures disappointed expectations but the country's trade surplus hit a new high.
- Gilts were also little changed as data showed that UK exports remain weak and a survey suggested that UK retailers continue to struggle.
- Wednesday brings UK industrial output figures for March, while Thursday brings the equivalent data for the euro area and the latest BoE MPC statement and Inflation Report.

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Daily bond market movements

Bond	Yield	Change*
BKO 0 03/18	-0.509	+0.005
OBL 0 04/21	-0.385	+0.002
DBR 0½ 02/26	0.114	-0.011
UKT 1¼ 07/18	0.376	-0.024
UKT 1½ 01/21	0.804	-0.014
UKT 2 09/25	1.398	-0.012

*Change from close as at 4.15pm BST.
Source: Bloomberg

Euro area

Disappointing IP data foreshadow a softer Q2

The March industrial output figures from the euro area's three largest member states fell short of expectations, with a weak end to the first quarter likely foreshadowing softer economic growth in Q2. The moderation in the industrial sector was marked in Germany where production in March dropped for the second successive month and by 1.3%M/M, about 1ppt more than expected. The detail was disappointing too, with manufacturing output down about 1%M/M for the second successive month, while construction output fell more than 3%M/M. However, the weakness at the end of the quarter followed an exceptionally strong start to the year. And, as a result, in Q1 as a whole German manufacturing output was still up 2%Q/Q, the most in more than five years, construction output was up more than 3%Q/Q, and overall industrial production was up 1.8%Q/Q. Not least due to the negative 'carry over' from the March figures, some if not all of these growth rates will be much softer – possibly negative – in Q2.

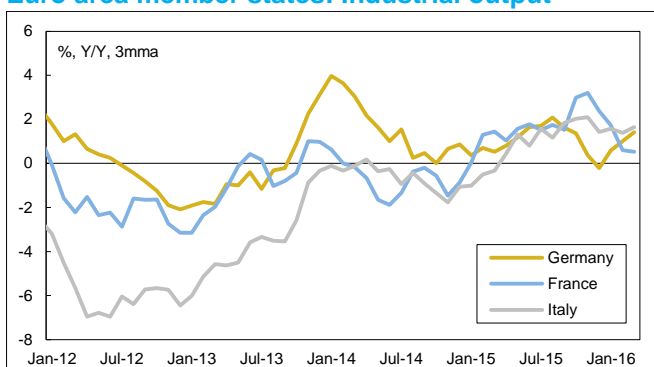
Germany notches new record external surpluses

The latest German goods export figures were better than expected, however, up in nominal terms by almost 2%M/M in March, the most in six months, to post a gain in Q1 for the first quarter in three. At the same time, imports were weaker than expected, falling more than 2%M/M in March to take the average in Q1 below that of Q4. Illustrating the country's large and rising contribution to global imbalances, Germany's trade and current account surpluses both rose to new record highs, of €26bn and more than €30bn respectively, thus remaining on track for another full-year current account surplus comfortably above 8% of GDP in 2016. Moreover, net trade looks to have made a positive contribution to German GDP growth in Q1 for the first quarter in three. And while the outlook for global demand remains subdued, and net trade might be expected to subtract from GDP growth in Q2, German goods exports might inch up further over the near term: thanks to increased orders for capital goods from beyond the euro area, factory orders from abroad rose more than 4%M/M in March, more than offsetting a dip in domestic orders.

French surveys offer cause for cautious optimism

Like in Germany, the French production figures also disappointed expectations, with a drop in overall industrial output for the second successive month in March despite solid gains from energy and construction output. Indeed, French manufacturing production fell almost 1%M/M following a near-1½%M/M drop in February and so retreated 0.7%Q/Q overall in Q1 – a marked contrast from the 0.5%Q/Q growth in GDP in the past quarter. The latest Bank of France business sentiment survey also

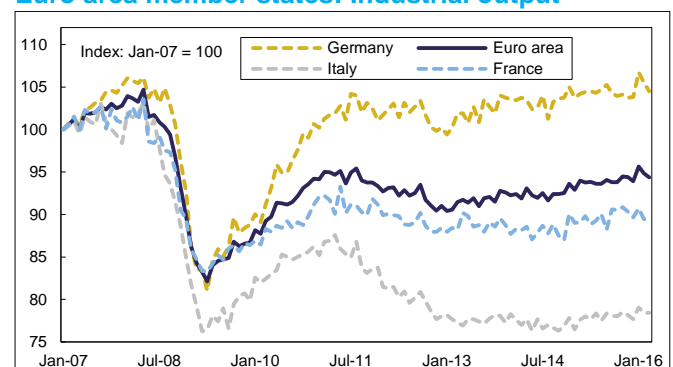
Euro area member states: Industrial output*



*Excluding construction.

Source: Datastream and Daiwa Capital Markets Europe Ltd.

Euro area member states: Industrial output*



*Excluding construction.

Source: Datastream and Daiwa Capital Markets Europe Ltd.



painted a weaker picture than hoped, with the headline index remaining below the long-run average, unsurprisingly suggesting a slowing of French GDP growth in Q2, to 0.3%Q/Q. Nevertheless, following a surge in business investment in the first quarter, a separate survey published today provided cause for optimism about the future, reporting that manufacturers intend to boost further their capital spending this year at the strongest rate since 2011. Elsewhere, following a drop the previous month, Italian industrial production was flat in March. However, thanks to a strong January, it rose 0.6%Q/Q in Q1, the strongest rate in three quarters, to add to evidence of an acceleration in Italian GDP growth in Q1 (preliminary data due on Friday). Overall, euro area industrial production (on the EU measure which excludes construction) likely retreated by about ½%M/M in March, implying a gain in Q1 of about ¾%Q/Q, the most in one year (data due on Thursday).

Another Greek debt drama to be avoided?

While there are further tortuous negotiations to be completed, following yesterday's Eurogroup meeting the probability of another summer of uncertainty about Greece's future in the euro area and a Greek default on its payments of more than €2½bn due to the ECB, IMF and EIB in July appears to have diminished. After the Greek parliament on the weekend adopted further fiscal tightening measures in the form of pension and tax reforms worth about 2% of GDP, yesterday the government committed to legislate a 'contingency mechanism' to implement additional automatic austerity should it appear off-track to meet its annual 3½% of GDP primary surplus targets. In response, the Eurogroup agreed to discuss on 24 May a possible package of measures to enhance the sustainability of Greece's debt, including longer grace and repayment periods to reduce Greece's debt in NPV terms, albeit sadly not in nominal terms. It remains to be seen quite how the still-contrasting views of the Eurogroup, IMF and Greek government will be reconciled. And, given the likely damaging impact of the latest austerity package, the Greek economic outlook remains dire. However, for the time being at least, we expect a deal eventually to be reached that should avoid a repeat performance of last year's unedifying political drama and associated Greek-specific financial stress.

The coming two days in the euro area and the US

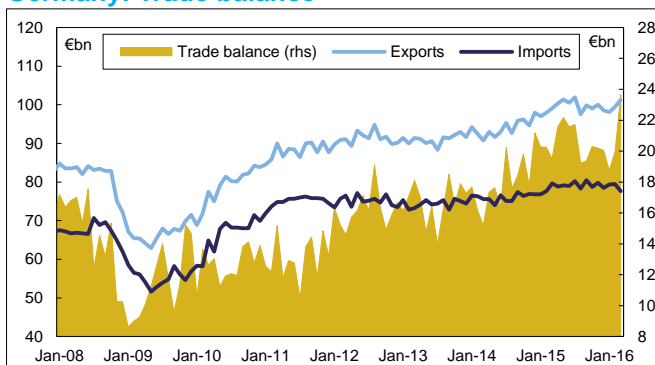
Wednesday should be very quiet for new economic data from the euro area, with no top-tier releases due. But, in addition to the aforementioned euro area March industrial production figures, which we expect to show a decline of about ½%M/M, Thursday brings the final estimate of French inflation in April for which the flash estimate on the EU-harmonised measure was unchanged for the third month at -0.1%Y/Y. In the markets, Germany will sell 2Y bonds on Wednesday and Italy will sell 3Y, 7Y, and 15Y bonds. Meanwhile, in the US, the April Federal Budget statement is due on Wednesday and import price data for the same month are due on Thursday along with the usual weekly claims figures. And the Treasury will sell 10Y bonds on Wednesday and 30Y bonds on Thursday.

UK

Trade subtracts from growth in Q1

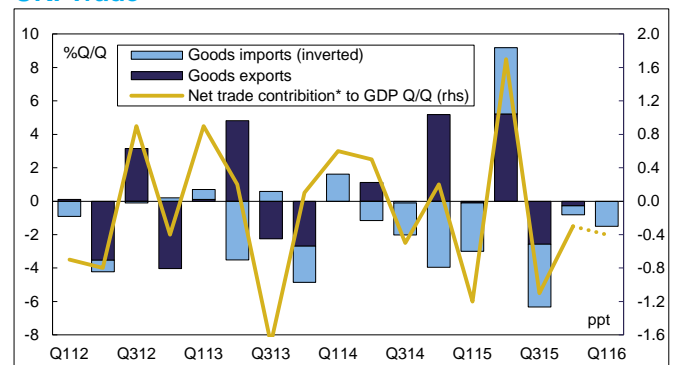
The figures released today showed that the UK trade deficit decreased to £3.8bn in March from the downwardly revised February level of £4.3bn. In terms of the geographical breakdown, while trade in goods with the rest of the EU recorded its highest ever monthly deficit, this was more than offset by an improvement in the non-EU balance. Notwithstanding the more positive monthly figures, the UK's underlying trade position remained weak, with the figures for Q1 showing that the total deficit reached the second-highest level on record of £13.3bn. And, looking at the trade volumes, exports were flat in Q1, but imports rose by 1.5% suggesting that net trade remained a drag on growth in the UK for the fourth quarter in the last five.

Germany: Trade balance



Source: Datastream and Daiwa Capital Markets Europe Ltd.

UK: Trade



*Daiwa forecast for Q116. Source: Datastream and Daiwa Capital Markets Europe Ltd.

Survey suggests that retailers struggled in April












The latest BRC retail sales survey for April, meanwhile, provided further evidence that the UK economy continues to slow, with total sales unchanged compared to a year ago for the second consecutive month and like-for-like sales down 0.9%Y/Y, having fallen by 0.7%Y/Y in March. Growth in non-food sales has slowed abruptly, down to 0.4%3M/Y in April, the lowest since 2012, from 2.6%3M/Y previously on a same-store basis. While unseasonably cold weather probably played a role and some recovery in sales might be expected in May, other indicators from the retail sector also point to weakening demand, partly weighed down no doubt by Brexit uncertainty.

The coming two days in the UK



The most notable economic data tomorrow will be the industrial production figures for March. Output is expected to have increased by 0.5%M/M and the ONS has already hinted that there will be an upward revision to the previous months' figures. Nevertheless, industrial output growth still looks set to have been negative in Q1 as a whole. Meanwhile, Thursday sees the BoE announce its latest monetary policy decision and release its quarterly Inflation Report. While the decision will no doubt see Bank Rate unchanged, the BoE's latest assessment of the economy will be of more interest. There is growing, and increasingly compelling, evidence of a marked slowdown in economic growth. But there is little doubt that this is to a large extent thanks to higher uncertainty ahead of the EU referendum. So while the near-term forecast for growth in the Inflation Report will be revised lower, on the assumption of a Remain vote, the forecast is likely to see a return to a higher growth path once the uncertainty has dissipated. And it remains to be seen how much information the BoE is willing to provide on its assessment of the likely near-term impact on the outlook for GDP growth, inflation and monetary policy of a vote to Leave.

The next edition of Euro wrap-up will be published on 12 May 2016.

European calendar

Today's results						
Economic data						
Country	Release	Period	Actual	Market consensus/ <i>Daiwa forecast</i>	Previous	Revised
Germany	 Industrial production M/M% (Y/Y%)	Mar	-1.3 (0.3)	-0.2 (1.1)	-0.5 (1.3)	-0.7 (2.0)
	 Trade balance €bn	Mar	26.0	20.6	20.3	20.2
	 Imports (exports) M/M%	Mar	-2.3 (1.9)	-0.3 (0.0)	0.4 (1.3)	0.1 (-)
	 Current account balance €bn	Mar	30.4	25.0	20.0	21.1
France	 Bank of France business sentiment indicator	Apr	99	100	99	-
	 Industrial production M/M% (Y/Y%)	Mar	-0.3 (-0.8)	0.7 (0.5)	-1.0 (0.6)	-1.3 (0.4)
	 Manufacturing production M/M% (Y/Y%)	Mar	-0.9 (-1.1)	0.6 (1.2)	-0.9 (1.6)	-1.4 (1.4)
Italy	 Industrial production M/M% (Y/Y%)	Mar	0.0 (0.5)	0.2 (1.3)	-0.6 (1.2)	-0.7 (1.1)
UK	 BRC like-for-like sales Y/Y%	Apr	-0.9	0.5	-0.7	-
	 Visible trade balance £bn	Mar	-11.2	-11.5	-12.0	-11.4
	 Total trade balance £bn	Mar	-3.8	-4.2	-4.8	-4.3
Auctions						
Country	Auction					
- Nothing to report -						




Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

Yesterday's results						
Economic data						
Country	Release	Period	Actual	Market consensus/ <i>Daiwa forecast</i>	Previous	Revised
EMU	 ECB QE net purchases €bn	Weekly	19.8	<u>15.6</u>	17.6	-
Germany	 Factory orders M/M% (Y/Y%)	Mar	1.9 (1.7)	0.6 (0.1)	-1.2 (0.5)	-0.8 (0.7)
Auctions						
Country	Auction					
- Nothing to report -						


Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

Tomorrow's data releases

Economic data

Country	BST	Release	Period	Market consensus/ <i>Daiwa forecast</i>	Previous	
UK		09.30	Industrial production M/M% (Y/Y%)	Mar	0.5 (-0.4)	-0.3 (-0.5)
		09.30	Manufacturing production M/M% (Y/Y%)	Mar	0.3 (-1.9)	-1.1 (-1.8)
		15.00	NIESR GDP 3M/3M%	Apr	-	0.3






Auctions and events

Country	BST	Auction / Event
Germany		10.30 Auction: To sell €5bn of 2018 bonds (15-Jun-2018)








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	Industrial production M/M% (Y/Y%)	Mar	0.0 (0.9)	-0.8 (0.8)
France		07.45	Final EU-harmonised CPI Y/Y%	Apr	-0.1	-0.1
UK		00.01	RICS house price balance %	Apr	35	42
		12.00	BoE bank rate %	May	<u>0.50</u>	0.50
		12.00	BoE asset purchase target £bn	May	<u>375</u>	375

Auctions and events

Country	BST	Auction / Event
Italy		10.00 Auction: To sell up to €2.25bn of 0.1% 2019 bonds (15-Apr-2019)
		10.00 Auction: To sell up to €2.75bn of 0.95% 2023 bonds (15-Mar-2023)
		10.00 Auction: To sell up to €1bn of 3.5% 2030 bonds (01-Mar-2030)
		10.00 Auction: To sell up to €1.5bn of 1.65% 2032 bonds (01-Mar-2032)
UK		12.00 Monetary policy announcement and MPC minutes
		12.00 BoE publishes Inflation Report
EMU		17.40 ECB's Constâncio scheduled to speak in Madrid

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

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