

Euro wrap-up

Overview

- Bunds were little changed as the account of the April ECB policy meeting underscored the likelihood that rates will be unchanged for some time to come.
- Gilts were also little changed despite firmer-than-expected UK retail sales data.
- It should be a relatively quiet end to the week for data with Friday bringing euro area balance of payments figures and a UK industry survey.

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Daily bond market movements

Bond	Yield	Change*
BKO 0 03/18	-0.505	+0.005
OBL 0 04/21	-0.352	+0.009
DBR 0½ 02/26	0.172	+0.004
UKT 1¼ 07/18	0.431	+0.006
UKT 1½ 01/21	0.871	+0.007
UKT 2 09/25	1.436	-0.002

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

Euro area

Construction output falls for the second month

As we expected, euro area construction output fell in March for the second consecutive month, falling 0.9%M/M following a downwardly revised contraction of 0.6%M/M in February. However, matching the pattern observed for industrial production, those declines followed an exceptionally strong January when construction output rose 2.0%M/M, the strongest in two and a half years. Therefore, over the first quarter as a whole, construction output rose 1.1%Q/Q, matching the gain of the previous quarter, driven again by building work while civil engineering activity maintained its recent downwards trend. At the country level, activity in Q1 was particularly strong in Germany (up almost 3½%Q/Q thanks not least to favourable weather) and Spain (up almost 2½%Q/Q) while it dropped more than ½%Q/Q in France and Italy. Looking ahead, a moderate uptrend in the construction sector seems likely to continue in the euro area as a whole, supported by a range of factors including lower interest rates, increased lending for house purchase, falling unemployment, and a gradual rise in house prices. And we expect the trend in construction activity to remain most robust in Germany where house price growth remains firmest. However, not least given the monthly profile of output in Q1, growth in the sector in the second quarter is likely to be much softer.

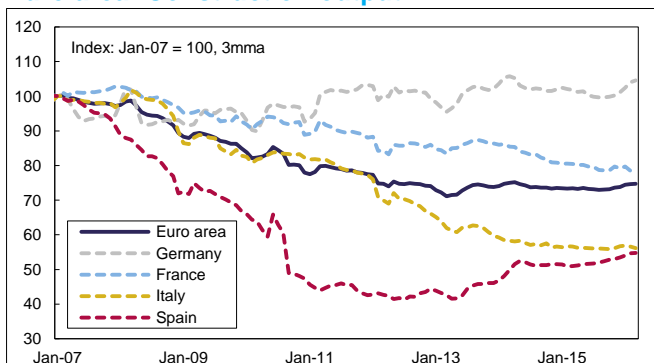
ECB policy on hold for the time being

There was little to get excited about from the account of the ECB's Governing Council April policy meeting published today. Consistent with recent firmer economic data and ongoing easing of bank lending conditions, officials predictably saw 'grounds for cautious optimism'. And they also judged that the recent monetary policy measures were being effective, while patience was needed for their full impact to be felt, not least given that the corporate bond purchases and TLTRO-II facility will only get underway in June. Indeed, with inflation set to rise gradually through the second half of the year, we think that the ECB will now leave policy unchanged for several months to come. We do not expect any further rate cuts, which would face significant opposition among a number of members of the Governing Council, not least given concerns about the possible adverse consequence for banks and confidence as a whole. However, in order to avoid a harmful premature tightening of financial conditions, we do expect the ECB in the second half of the year to extend the end of the asset purchase programme by a further six months to end-September 2017 at the earliest, although that decision might not be taken until December.

The day ahead in the euro area and the US

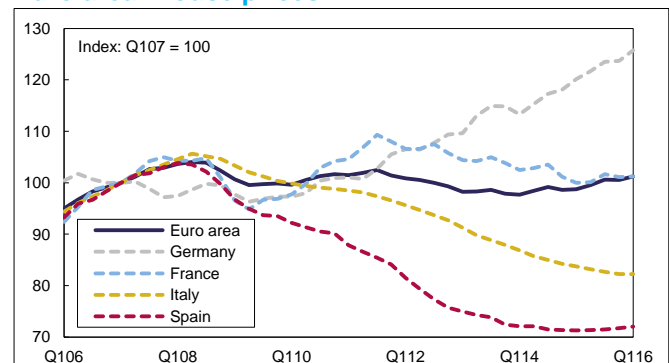
It should be a relatively uneventful end to the week for euro area economic data with the ECB's balance of payments report for Q1 arguably the most notable new release. It will also be relatively quiet data-wise in the US, with just April existing home sales due.

Euro area: Construction output



Source: Datastream and Daiwa Capital Markets Europe Ltd.

Euro area: House prices



Source: Datastream and Daiwa Capital Markets Europe Ltd.



UK

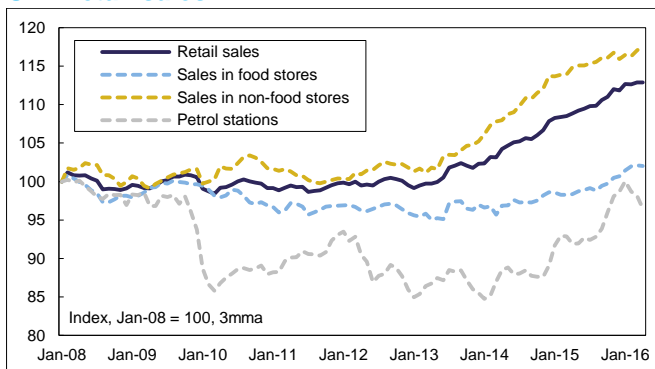
Upward surprise to retail sales growth in April

Following the release of slightly better-than-expected labour market figures yesterday, today's retail sector data also surprised on the upside. While some surveys, including those from the BRC and the CBI, implied relatively subdued growth, sales growth actually increased from the upwardly revised rate of 3.0%Y/Y in March to 4.3%Y/Y in April. And this was in spite of the unhelpful timing of Easter and untypically cold weather, which affected consumers' willingness to spend money on clothing and other seasonal items. However, looking through the monthly volatility, on a 3M/3M basis spending growth fell by 0.6ppt to 0.3%. In addition, the numbers continued to suggest that the operating environment for retailers remained difficult, with sales in nominal terms rising slowly, at only 1.2%Y/Y, albeit up from 0.3%Y/Y in March, with deep retail price deflation seemingly responsible for the strong real growth in real sales. More broadly, while the figures suggest that consumer spending continues to grow, they suggest that consumption growth is continuing to moderate.

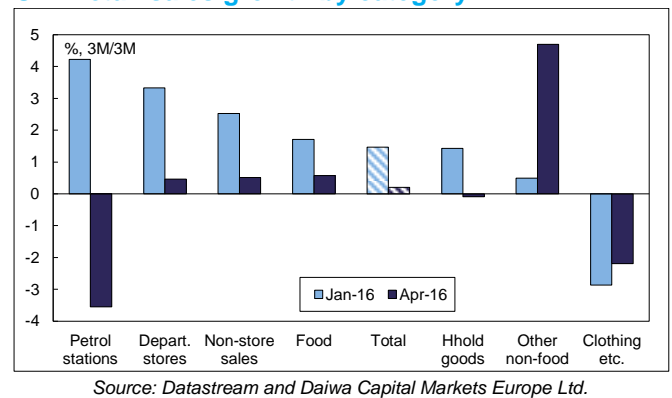
The day ahead in the UK

It will be relatively quiet end of the week, with only the CBI Industrial Trends survey due tomorrow.













UK: Retail sales



UK: Retail sales growth by category



European calendar

Today's results						
Economic data						
Country	Release	Period	Actual	Market consensus/ <i>Daiwa forecast</i>	Previous	Revised
EMU	 Construction output M/M% (Y/Y%)	Mar	-0.9 (-0.5)	-	-1.1 (2.5)	-0.6 (3.4)
France	 Unemployment rate %	Q1	10.2	10.2	10.3	10.2
UK	 Retail sales excluding petrol M/M% (Y/Y%)	Apr	1.5 (4.2)	0.6 (2.0)	-1.6 (1.8)	-0.7 (2.6)
	 Retail sales including petrol M/M% (Y/Y%)	Apr	1.3 (4.3)	0.6 (2.5)	-1.3 (2.7)	-0.5 (3.0)
Auctions						
Country	Auction					
France sold	 €3.0bn of 2019 zero-coupon bonds (25-Feb-2019) at an average yield of -0.36%					
	 €3.2bn of 2021 zero-coupon bonds (25-May-2021) at an average yield of -0.15%					
	 €845mn of 0.1% 2021 index-linked bonds (01-Mar-2021) at an average yield of -0.99%					
	 €345mn of 0.1% 2025 index-linked bonds (01-Mar-2025) at an average yield of -0.61%					
	 €425mn of 0.7% 2030 index-linked bonds (25-Jul-2030) at an average yield of -0.37%					
Spain sold	 €1.4bn of 0.25% 2019 bonds (31-Jan-2019) at an average yield of 0.012%					
	 €560mn of 4.8% 2024 bonds (31-Jan-2024) at an average yield of 1.157%					
	 €484mn of 1.95% 2030 bonds (30-Jul-2030) at an average yield of 2.048%					

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	
EMU	09.00	Current account balance €bn	Mar	-	19.0	
Italy	09.30	Current account balance €bn	Mar	-	1.4	
Spain	09.00	Trade balance €bn	Mar	-	-1.8	
UK	11.00	CBI Industrial Trends survey, total orders	May	-13	-11	
Auctions and events						
Country	BST	Auction / Event				
- Nothing scheduled -						

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

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