Euro wrap-up

Overview

- Despite another weak euro area economic sentiment survey, Bunds made losses, but Spanish bonds made modest gains as the Socialist Party won by far the largest number of seats in Spain's general election.
- Gilts made modest losses on a quiet day for economic news from the UK.
- Tuesday will bring the first estimates of Q1 GDP from the euro area and France, Italy and Spain, and April inflation from the four largest member states.

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Daily bond market movements

Bond	Yield	Change*
BKO 0 12/20	-0.589	+0.016
OBL 0 04/24	-0.420	+0.019
DBR 0¼ 02/29	0.001	+0.022
UKT 1½ 01/21	0.736	+0.009
UKT 1 04/24	0.870	+0.012
UKT 1⅝ 10/28	1.152	+0.010

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

Euro area

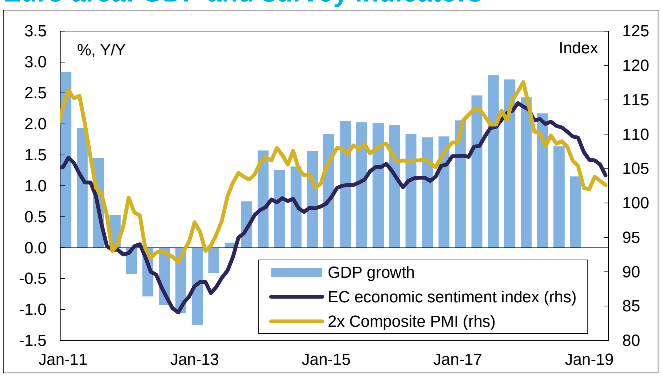
Commission sentiment index down for tenth month in a row

Following the disappointing flash PMIs and national business surveys for April, it was no surprise that today's Commission business and consumer survey also suggested a worsening of confidence for the tenth successive month. However, the headline euro area economic sentiment index fell further than expected, down 1.6pts – the most so far this year – to 104.0, the lowest level since September 2016, with a deterioration reported in each of the four largest member states. Like the PMIs, the Commission survey suggested that pessimism was most evident in the manufacturing sector, with firms taking a dimmer view of order books and the outlook for production. But while services sentiment was unchanged, retailers were more downbeat about both current conditions and expectations for the future, something that tallied with the darker mood among consumers previously indicated in the flash estimate and confirmed today. And construction confidence worsened too, as firms in that sector revised down significantly their employment plans. Finally, the signals on inflation were hardly reassuring either. While retailers' selling price expectations edged up, firms in industry, construction and services were more downbeat in this respect. And to cap a wholly disheartening survey for the ECB, consumer price expectations dropped too. Overall, therefore, the Commission survey – which often provides the most reliable guide to euro area economic activity – added to evidence of a softening of momentum at the start of Q2 in terms of both activity and inflation, suggestive of the need for the ECB to downgrade its economic forecasts once again in early June.

Bank lending slowing gradually too

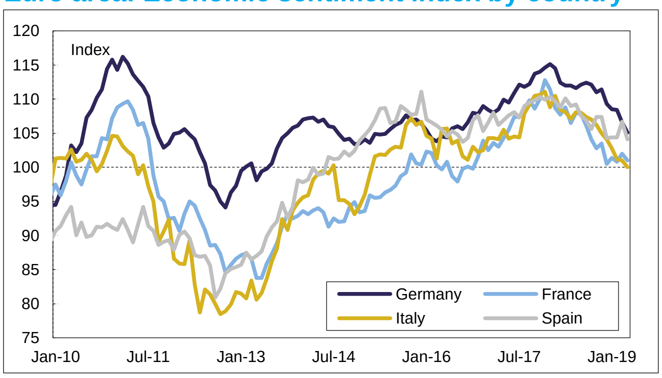
The ECB will also not have been particularly reassured by today's monetary data, which suggested that growth in bank lending moderated at the end of Q1. Indeed, net new loans to non-financial corporations (NFCs) in March slowed to €4.5bn (adjusted for sales and securitisations), well below the 2018 average, to leave the quarterly flow of €22.3bn the lowest since Q217. Growth in the stock of such loans to businesses, at 3.5%Y/Y, was down 0.3ppt from the previous month to be the lowest in eleven months. Similarly, new lending to households also slowed in March, to €13.4bn, leaving the Q1 figure at €46.0bn, the lowest since Q218, and the growth in the stock down to a six-month low of 3.2%Y/Y. Overall, these figures tally with the signals from the real economy, where the slowing in activity would be expected to see a moderation in loan demand – indeed, the ECB's Bank Lending Survey had suggested no increase in net loan demand from NFCs last quarter. And, the figures might suggest a case for incentivizing growth of lending via the pricing of the TLTRO-III loan operations, which will be discussed at the June Governing Council meeting. However, with the net flow of lending to NFCs remaining relatively firm in Germany and France, where many banks hold significant excess deposits, but significantly negative in Italy, where this is not typically the case, the data do not suggest a strong case for ECB action (e.g. tiering) to directly mitigate any adverse impact of the negative deposit rate on credit conditions.

Euro area: GDP and survey indicators



Source: Thomson Reuters, European Commission, Markit and Daiwa Capital Markets Europe Ltd.

Euro area: Economic sentiment index by country



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

Spanish election strengthens Socialists' hand

Spanish government bonds outperformed other euro area sovereigns today as the outcome of yesterday's general election pointed to the likelihood of another government led by the incumbent Socialist party (PSOE). Against the backdrop of an economy that has seen steady growth and rising employment, and following the implementation of some crowd-pleasing measures (e.g. a sharp increase in the minimum wage at the start of the year and reversal of some welfare reforms), it was no surprise that the pro-European PSOE, which had been ruling in a minority capacity since last summer, saw a notable increase in its share of the vote. In the event, it increased its number of seats by 38 from the last general election to take 123 of the 350-seat Congress of Deputies. In sharp contrast, the centre-right establishment Partido Popular (PP), which was previously the largest party in parliament, saw its vote collapse, losing more than half of its seats (from 137 to just 66). The centre-right Citizens was one party to gain at PP's expense, with its tally rising from 32 to 57 seats. And to confirm a further fracturing of the right, the nationalist Vox also took votes off PP, and as such gained headlines as it won seats for the first time. Nevertheless, Vox was still only the fifth largest party in parliament. And with only 24 seats, it won fewer votes than many had predicted and cannot be kingmaker. Finally, the anti-austerity populist left-wing Podemos-United Left alliance lost votes to PSOE, ending up with 43 seats. Overall, the number of seats won by the two national parties on the left rose by 9 to 165, while the number of seats won by the three national parties on the right fell by 22 to 147.

Another minority government on the cards?

Talks to try to form a government will now get underway. But having recently shifted further from its liberal origins in an attempt to unseat PP as the first party of the right, Citizens seems strongly disinclined to cooperate with PSOE. And the election left PSOE and Podemos – who would seem natural left-wing coalition bedfellows – ten seats short of a majority. So, the support – explicit or tacit – of the small regional parties (including the Catalan and/or Basque nationalists) would seem likely to be required to allow a government to be formed. In practice, PSOE might prefer once again to try to govern with a minority, albeit leaving them more vulnerable to defeat on major votes, such as the budget. And uncertainty will certainly reign for a while – negotiations between the parties might be expected to take several weeks, with conclusion highly unlikely until after the end-May European Parliament elections. Nevertheless, the relatively strong showing from the Socialists (and parties of the left more generally) this time around suggests that Spain might in due course see a somewhat more stable and assertive government than over the past few years.

The day ahead in the euro area and US

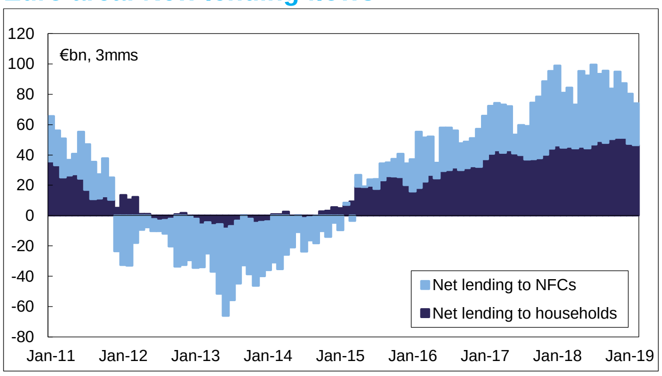
Tuesday will be a particularly busy day for economic data from the euro area with key releases including the first estimates of Q1 GDP and April inflation. The GDP figures will come from the euro area, France, Italy and Spain. We expect growth in the euro area and France to remain unchanged from Q4 at 0.2%Q/Q and 0.3%Q/Q respectively, and anticipate a slight moderation in growth in Spain of 0.1ppt from Q4 to 0.5%Q/Q. But, despite the weakening evident in many recent surveys indicators, the risks to these forecasts seem skewed to the upside as certain temporary factors that weighed on activity in Q4 wear off. In line with the consensus, we also forecast Italian growth of 0.1%Q/Q, which would mark an end to the recession in H218 but also take the year-on-year rate into negative territory. In terms of inflation, the flash estimates of April CPI will come from Germany, France, Italy and Spain, ahead of the equivalent data for the euro area to be published on Friday. Not least due to the impact of the timing of Easter, we expect the headline and core rates to increase from March in each of the aforementioned member states. Among other new data due from the region tomorrow, euro area unemployment data for March and German labour market and consumer confidence figures for April are also notable. In the markets, Germany will sell 2Y Schatz while Italy will sell 5Y and 10Y bonds. In the US, the Conference Board's consumer survey and Chicago PMI reports for April are due alongside pending home sales for March, S&P CoreLogic house price data for February, and the Employment Cost Index for Q1.

UK

The day ahead in the UK

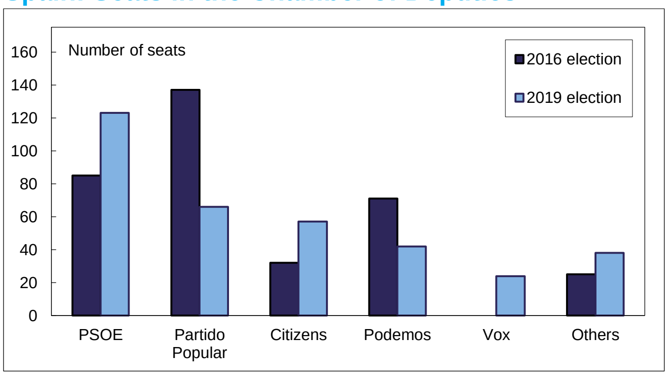
After a quiet start to the week with no new economic data released, Tuesday will bring the GfK consumer confidence survey for April. As Brexit uncertainty has persisted, consumer sentiment has been subdued but broadly stable in recent months, and we are likely to see that trend continue this month. The latest Lloyds Business Barometer survey is also due.

Euro area: New lending flows



Source: Thomson Reuters and Daiwa Capital Markets Europe Ltd.

Spain: Seats in the Chamber of Deputies



Source: Ministry of the Interior and Daiwa Capital Markets Europe Ltd.

European calendar

Today's results							
Economic data							
Country	Release	Period	Actual	Market consensus/ *Daiwa forecast*	Previous	Revised
EMU	M3 money supply Y/Y%	Mar	**4.5**	4.2	4.3	**-**
	Economic sentiment indicator	Apr	**104.0**	105.0	105.5	**105.6**
	Final consumer confidence indicator	Apr	**-7.9**	-7.9	-7.2	**-**
	Services (industrial) confidence	Apr	**11.5 (-4.1)**	11.5 (-2.0)	11.3 (-1.7)	**11.5 (-1.6)**
Auctions and events						
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/ *Daiwa forecast*	Previous
EMU	10:00	GDP – first estimate Q/Q% (Y/Y%)	Q1	*0.2 (1.0)*	0.2 (1.1)
	10:00	Unemployment rate%	Mar	7.8	7.8
Germany	07:00	GfK Consumer confidence indicator	May	10.3	10.4
	08:55	Unemployment change 000s (rate %)	Apr	-7 (4.9)	-7 (4.9)
	13:00	Preliminary EU-harmonised CPI Y/Y%	Apr	1.7	1.4
France	06:30	GDP – first estimate Q/Q% (Y/Y%)	Q1	*0.3 (1.0)*	0.3 (1.0)
	07:45	Consumer spending M/M% (Y/Y%)	Mar	-0.5 (-1.4)	-0.4 (-1.8)
	07:45	Preliminary EU-harmonised CPI Y/Y%	Apr	1.4	1.3
Italy	09:00	Unemployment rate%	Mar	10.7	10.7
	10:00	Preliminary EU-harmonised CPI Y/Y%	Apr	-	1.1
	11:00	GDP – first estimate Q/Q% (Y/Y%)	Q1	*0.1 (-0.1)*	-0.1 (0.0)
Spain	08:00	Preliminary EU-harmonised CPI Y/Y%	Apr	1.5	1.3
	08:00	GDP – first estimate Q/Q% (Y/Y%)	Q1	*0.5 (2.2)*	0.6 (2.3)
	08:00	Retail sales Y/Y%	Mar	1.4	0.8
UK	00:01	GfK consumer confidence indicator	Apr	-13	-13
	00:01	Lloyds business barometer	Apr	-	10
Country	BST	Auction / Event			
Germany	10:30	Auction: to sell €4bn of 2021 zero-coupon bonds (12-Mar-2021)			
Italy	10:00	Auction: to sell 1.75% 2024 bonds (01-Jul-2024)			
	10:00	Auction: to sell 3% 2029 bonds (01-Aug-2029)			
	10:00	Auction: to sell 2025 bonds (15-Jan-2025)			
UK	08:40	BoE's Ramsden scheduled to speak in London			

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

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