

Euro wrap-up

Overview

- Bunds made gains as the flash euro area PMIs pointed to continued subdued GDP growth, despite some signs of improvement in Germany.
- Gilts made also made gains even as the flash UK PMIs surprised on the upside and reduced the likelihood of rate cut at next week's BoE meeting.
- The coming week will bring flash estimates of euro area Q4 GDP and January inflation, as well as the Commission's sentiment survey. The main event in the UK will be Thursday's MPC rate decision and BoE Monetary Policy Report publication.

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Daily bond market movements

Bond	Yield	Change
BKO 0 12/21	-0.621	-0.010
OBL 0 10/24	-0.589	-0.017
DBR 0 02/30	-0.334	-0.023
UKT 3¼ 09/21	0.423	-0.006
UKT 1 04/24	0.389	-0.016
UKT 0% 10/29	0.562	-0.029

*Change from close as at 4:00pm GMT.
Source: Bloomberg

Euro area

Euro area PMIs point to subdued growth

At yesterday's [ECB Governing Council press conference](#), President Lagarde suggested that economic growth in the euro area was likely to remain broadly in line with the recent subdued rates, with the manufacturing sector set to remain a drag. And today's flash January PMIs suggested just that. Indeed, contrasting with an anticipated improvement, the headline composite PMI moved sideways at 50.9, consistent with modest GDP growth at a quarterly rate of 0.1% at the start of 2020. So, while it was 0.8pt above September's recent trough, the composite PMI was still the third-lowest reading since the euro crisis and almost 8pts below its peak two years ago. And the new orders component (up just 0.2pt to 50.8) merely suggested that growth will remain restrained for a while yet. The weakness in January principally reflected a deterioration in the services sector, where the respective activity PMI was down 0.6pt to 52.2 and the new orders and employment components moderated too. There were at least some encouraging signs of stabilisation in the manufacturing sector at the start of the year, with the headline PMI rising 1.5pts to 47.8, a nine-month high, and the new orders index rising 2.4pts to 49.0, its highest since November 2018. So, while consistent with ongoing mild contraction in the sector, today's survey added to evidence that manufacturing's struggles are probably passed the worst.

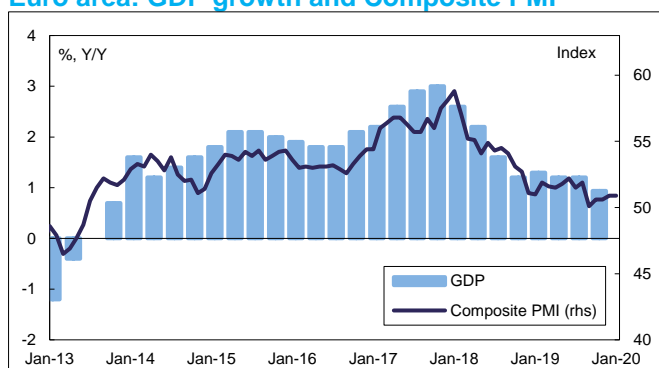
Signs of stabilisation in Germany...

The improvement in manufacturing conditions at the start of the year appears to have been principally observed in Germany, where the flash PMI for the sector rose 1.5pts in January to 45.2. Admittedly, this was still firmly in contractionary territory, but also the highest since last February. And while the pickup in the output PMI was more modest, the new orders component posted the fourth consecutive rise, to leave it 10pts higher than September's low. Germany's headline services PMI also ticked higher to 54.2, which was the strongest for five months to suggest that the sector remains resilient to the weaknesses in manufacturing. As such, the German composite PMI increased 0.9pt to 51.1, the highest since August and comfortably above the average through H219. And encouragingly, firms reported the first positive growth in new orders for seven months, and at the fastest pace since October 2018.

...but no improvement in France, while the periphery is weakening

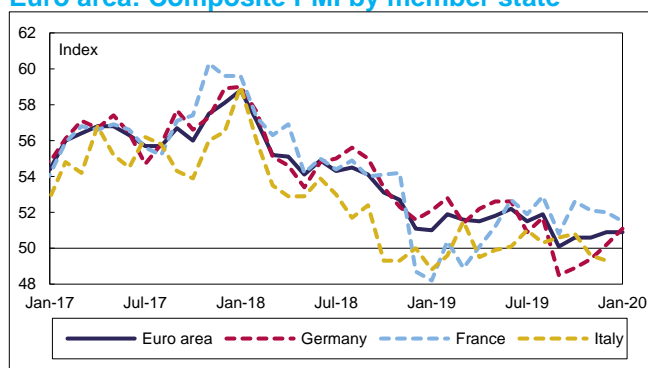
In contrast, France's flash PMIs suggested no meaningful improvement in economic conditions at the start of the year. While the manufacturing PMI rose 0.6pt, at 51.0 it still fell short of November's level and was close to the Q4 average. And the services PMI appeared to show strains from recent industrial unrest, falling 0.7pt to 51.7, the lowest since September. Overall, France's composite PMI slipped 0.5pt to 51.5 in January, similarly a four-month low, to leave it more than ½pt below

Euro area: GDP growth and Composite PMI*



*Flash Composite PMI for January 2020. Source: Markit, Thomson Reuters and Daiwa Capital Markets Europe Ltd.

Euro area: Composite PMI by member state*



*Flash Composite PMI for January 2020 for the euro area, Germany and France. Source: Markit, Thomson Reuters and Daiwa Capital Markets Europe Ltd.



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the Q4 average. Slower growth in new orders – the relevant index fell 1pt to 51.2 – suggested no acceleration in output ahead in France. Elsewhere in the euro area, the PMI survey implied a further deterioration in conditions at the start of the year. While there were no detailed indices published, Markit asserted that output growth beyond Germany and France slowed to its weakest rate for 6½ years, consistent with ‘near-stagnation’, with new orders unchanged.

The week ahead in the euro area and US

The coming week will be a busy one for top-tier euro area economic data, with the flash estimates of Q4 GDP and January inflation (Friday) and the European Commission’s sentiment survey (Thursday) key releases. We currently expect euro area GDP growth in Q4 to have slowed to 0.1%Q/Q, down from upwardly revised growth of 0.3%Q/Q in Q3 and the softest since Q113. While Spain’s economy is likely to have continued to outperform other major member states, with growth likely steady at the 0.4%Q/Q pace seen in the previous two quarters, we expect growth in France to have slowed slightly by 0.1ppt to 0.2%Q/Q. And Italy’s economy likely went broadly sideways at the end of last year.

Friday will also bring the flash estimates of January inflation from the euro area, France and Spain, with the equivalent figures for Germany due on Thursday. We expect headline euro area inflation to have edged slightly higher at the start of the year, by 0.1ppt to 1.4%Y/Y due to higher energy prices. But with underlying price pressures still subdued, core inflation likely slipped back in January by 0.1ppt to 1.2%Y/Y.

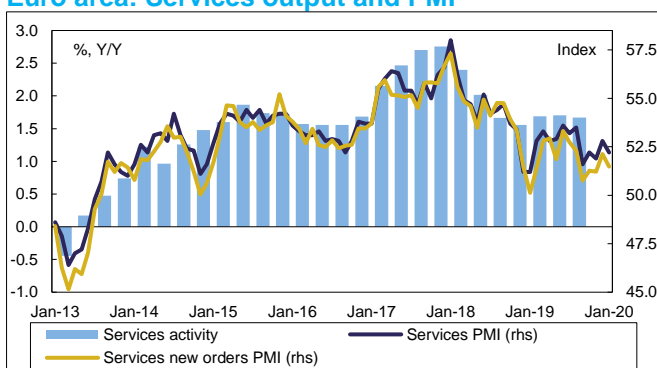
Thursday’s release of the European Commission’s economic sentiment survey – which provides the most comprehensive guide to euro area economic activity – is expected to signal only modest recovery at the start of the year, with the headline index forecast to rise for the third consecutive month but nevertheless remain close to the bottom of the recent range. Indeed, the Commission’s flash estimate of consumer confidence published in the past week suggested no improvement in January. Thursday will also bring the euro area’s unemployment figures for December, with the headline rate expected to be unchanged at 7.5% for a third successive month.

Meanwhile, the first half of the week will be filled with mainly national sentiment indicators, including the German ifo (Monday), German GfK consumer survey and Italian ISTAT business and consumer indices (Wednesday). Germany’s labour market figures for January are also due Thursday. Supply-wise, Italy will sell fixed-rate and index-linked bonds on Tuesday, while Germany will sell 5Y Bunds on Wednesday.

It will be a busy week in the US too, with the conclusion of the Fed’s latest FOMC meeting (Wednesday) to be accompanied by several top-tier data including the first estimate of Q4 GDP (Thursday). Admittedly, the FOMC meeting looks set to be relatively uneventful, with the Fed Funds Rate expected to be left unchanged at 1.50-1.75%. With the first phase of the US-China trade deal having been signed since the Fed last met, and given tentative signs of improvement in certain domestic and overseas economic indicators towards the end of last year, Fed Chair Powell might well note that downside risks appear to have further moderated and therefore reiterate the Committee’s view that the current policy stance remains appropriate.

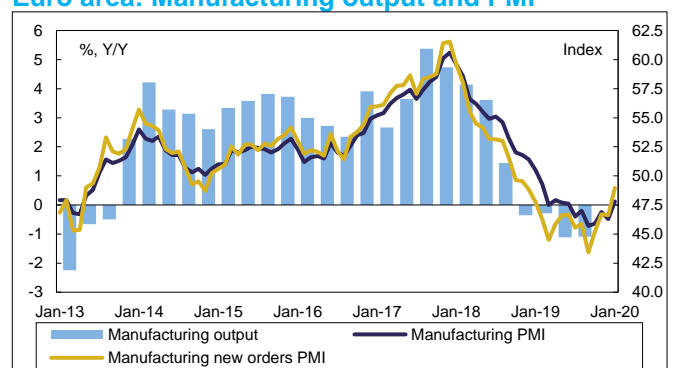
Certainly, Thursday’s GDP release is expected to report continued steady expansion at the end of 2019, with growth in Q4 forecast to be little changed from the near-2%Q/Q annualised rates seen in the previous two quarters. Other key releases include December durable goods orders data and January’s Conference Board’s consumer confidence survey (Tuesday), advance goods trade and inventories figures for December (Wednesday) and personal income and spending figures for the same month (Friday). Meanwhile, housing market releases include new home sales (Monday), Case-Shiller home price indices (Tuesday) and pending home sales figures (Wednesday). In the markets, the Treasury will sell 2Y and 5Y fixed-rate notes on Monday and 7Y fixed-rate and 2Y floating-rate notes on Tuesday.

Euro area: Services output and PMI*



*Flash Services PMI for January 2020. Source: Markit, Thomson Reuters and Daiwa Capital Markets Europe Ltd.

Euro area: Manufacturing output and PMI*



*Flash Manufacturing PMI for January 2020. Source: Markit, Thomson Reuters and Daiwa Capital Markets Europe Ltd.

UK

Flash PMIs significantly beat expectations

Having diminished somewhat following Tuesday's [labour market](#) report, the case for a BoE rate cut next week weakened significantly further today after the flash UK PMIs delivered a big upside surprise. With notable improvements in both manufacturing and services, the composite PMI leapt more than 3pts – the most since August 2016 – to 52.4, the highest since September 2018. The services PMI – the more important of the sectoral indices – was particularly striking, rising 2.9pt to 52.9, likewise a sixteen-month high. Meanwhile, the 1.3pt rise in the manufacturing PMI took it to a 9-month high of 49.8, a level implying that activity has now stabilised in that sector. The detail also suggested that new orders are now rising in aggregate at the strongest rate in sixteen months with employment growth the highest on the survey since July. And firms appear more confident about raising prices, with the composite output price PMI also up sharply to an eight-month high.

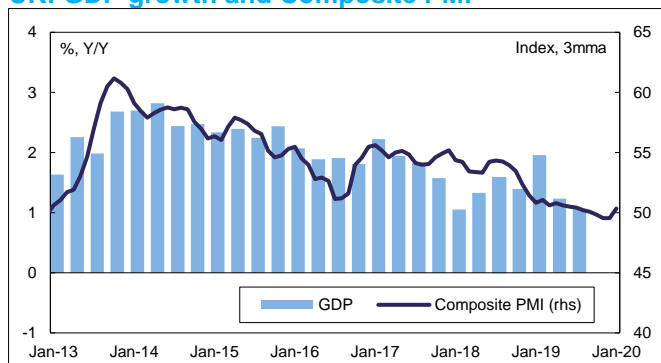
No longer any urgency for BoE to cut rates

Despite the big increase on the month, the composite PMI points to GDP growth in January at a quarterly rate of just 0.2%, still below potential. Coming after a very weak fourth quarter, when economic output possibly contracted, that suggests there remains a case for a BoE rate cut at Mark Carney's final MPC meeting on 30 January. However, the significant improvement in the PMIs and certain [other UK surveys](#), lends support to the BoE's most recent forecast that economic activity would pick up if and when political uncertainty lifted. Developments abroad would also suggest that the risks to the outlook are less skewed to the downside. So, the MPC now has greater freedom to wait for further evidence on recent conditions and the economic outlook – including data for Q4 GDP (on 11 February) and the Government's Budget announcement (on 11 March) – before deciding whether to provide additional stimulus. So, we no longer expect the MPC to vote for a rate cut next week. Instead, we think that a rate cut will come in May, when the initial post-election bounce in activity might well have petered out amid renewed uncertainty surrounding the negotiations over the UK's future relationship with the EU.

The week ahead in the UK

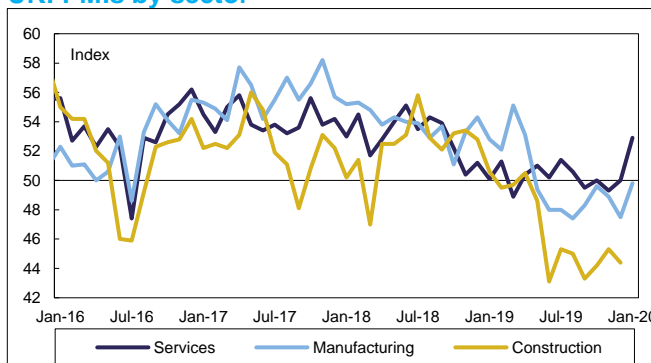
The BoE's policy announcement on Thursday will obviously be the main event in the UK in the coming week. The prior two MPC meetings saw two external members – Haskel and Saunders – vote for a 25bp rate cut. And since the start of the year, three further members – Vlieghe, Tenreyro and Governor Carney, for whom this will be the final MPC meeting – suggested that they would be ready to vote for a rate cut if the economic recovery anticipated in the BoE's November base case forecast was unlikely to materialise. While several recent data releases, including December's retail sales and inflation reports, were weaker than expected, the improvement in the flash January PMIs would suggest that the Bank's updated forecasts will maintain a baseline of economic recovery and inflation moving above target by the end of the projection horizon. Therefore, Haskel and Saunders will likely remain the only two members to vote for a cut at the coming meeting. Meanwhile, economic data due in the coming week include the CBI's retail sales monitor (Tuesday), Lloyds business barometer (Thursday) and GfK consumer confidence survey (Friday), all for January. BoE bank lending figures for December are also due on Friday. In the markets, the DMO will sell 10Y Gilts on Tuesday.

UK: GDP growth and Composite PMI*


















*Flash Composite PMI for January 2020. Source: Markit, Thomson Reuters and Daiwa Capital Markets Europe Ltd.

UK: PMIs by sector*



*Flash Services and Manufacturing PMIs for January 2020. Source: Markit, Thomson Reuters and Daiwa Capital Markets Europe Ltd.

Daiwa economic forecasts





	2019		2020				2021		2019	2020	2021
	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2			
GDP forecasts %, Q/Q											
Euro area 	0.3	0.1	0.2	0.3	0.2	0.2	0.2	0.1	1.2	0.9	0.6
Germany 	0.1	0.1	0.2	0.2	0.2	0.2	0.2	0.0	0.6	0.6	0.6
France 	0.3	0.2	0.3	0.3	0.2	0.2	0.2	0.2	1.3	1.1	0.8
Italy 	0.1	0.0	0.1	0.1	0.0	-0.1	0.0	-0.1	0.2	0.2	-0.1
Spain 	0.4	0.4	0.4	0.4	0.4	0.4	0.4	0.2	1.9	1.6	1.2
UK 	0.4	-0.1	0.3	0.3	0.3	0.3	0.1	0.3	1.3	0.8	0.8
Inflation forecasts %, Y/Y											
Euro area											
Headline CPI 	1.0	1.0	1.3	1.2	1.4	1.4	1.3	1.2	1.2	1.3	1.4
Core CPI 	0.9	1.2	1.2	1.2	1.3	1.2	1.2	1.1	1.0	1.2	1.3
UK											
Headline CPI 	1.8	1.4	1.5	1.0	1.0	1.2	1.6	1.9	1.8	1.2	1.9
Core CPI 	1.7	1.6	1.4	1.4	1.4	1.6	1.8	2.0	1.8	1.4	2.0
Monetary policy											
ECB											
Refi Rate % 	0.00	0.00	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	-0.60	-0.60	-0.50	-0.50	-0.60
Net asset purchases* 	0	20	20	20	20	20	30	30	20	20	30
BoE											
Bank Rate % 	0.75	0.75	0.75	0.50	0.50	0.50	0.50	0.50	0.75	0.50	0.50
Net asset purchases** 	0	0	0	0	0	0	0	0	0	0	0

*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/ Daiwa forecast	Previous	Revised
EMU 	Preliminary manufacturing PMI (services PMI)	Jan	47.8 (52.2)	46.8 (52.8)	46.3 (52.8)	-
	Preliminary composite PMI	Jan	50.9	51.2	50.9	-
Germany 	Preliminary manufacturing PMI (services PMI)	Jan	45.2 (54.2)	44.5 (53.0)	43.7 (52.9)	-
	Preliminary composite PMI	Jan	51.1	50.5	50.2	-
France 	Preliminary manufacturing PMI (services PMI)	Jan	51.0 (51.7)	50.6 (52.2)	50.4 (52.4)	-
	Preliminary composite PMI	Jan	51.5	52.0	52.0	-
UK 	Preliminary manufacturing PMI (services PMI)	Jan	49.8 (52.9)	48.8 (51.1)	47.5 (50.0)	-
	Preliminary composite PMI	Jan	52.4	50.7	49.3	-


































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 27 January 2020					
Germany		09.00 Ifo business climate index	Jan	97.0	96.3
		09.00 Ifo current assessment balance (expectations)	Jan	99.2 (94.9)	98.8 (93.8)
UK		09.30 UK Finance loans for housing £bn	Dec	43.9	43.7
Tuesday 28 January 2020					
UK		11.00 CBI distributive trades survey, reported sales	Jan	5	0
		- Nationwide house price index* M/M% (Y/Y%)	Jan	0.3 (1.5)	0.1 (1.4)
Wednesday 29 January 2020					
EMU		09.00 M3 money supply Y/Y%	Dec	5.5	5.6
Germany		07.00 GfK consumer confidence indicator	Feb	9.6	9.6
France		07.45 Consumer confidence indicator	Jan	102	102
Italy		09.00 Economic sentiment indicator	Jan	-	100.7
		09.00 Consumer confidence indicator (manufacturing)	Jan	110.5 (99.4)	110.8 (99.1)
Spain		08.00 Retail sales Y/Y%	Dec	-	2.9
UK		00.01 BRC shop price index Y/Y%	Jan	-	-0.4
Thursday 30 January 2020					
EMU		10.00 Economic confidence indicator	Jan	101.8	101.5
		10.00 Industrial confidence indicator (services)	Jan	-8.9 (11.2)	-9.3 (11.4)
		10.00 Final consumer confidence indicator	Jan	-8.1	-8.1
		10.00 Unemployment rate %	Dec	7.5	7.5
Germany		08.55 Unemployment change '000s (rate %)	Jan	5.0 (5.0)	8.0 (5.0)
		13.00 Preliminary CPI (EU-harmonised CPI) Y/Y%	Jan	1.7 (1.7)	1.5 (1.5)
Italy		09.00 Preliminary unemployment rate %	Dec	9.7	9.7
UK		00.01 Lloyds business barometer	Jan	-	10
		12.00 BoE Bank Rate %	Jan	<u>0.75</u>	0.75
Friday 31 January 2020					
EMU		10.00 Preliminary GDP estimate Q/Q (Y/Y%)	Q4	<u>0.1 (1.1)</u>	0.3 (1.2)
		10.00 Preliminary CPI (core CPI) Y/Y%	Jan	<u>1.4 (1.2)</u>	1.3 (1.3)
Germany		07.00 Retail sales M/M% (Y/Y%)	Dec	-0.5 (4.9)	1.5 (2.7)
France		06.30 Preliminary GDP Q/Q% (Y/Y%)	Q4	<u>0.2 (1.2)</u>	0.3 (1.4)
		07.45 Consumer spending M/M% (Y/Y%)	Dec	0.0 (1.5)	0.1 (0.2)
		07.45 Preliminary CPI (EU-harmonised CPI) Y/Y%	Jan	1.5 (1.7)	1.5 (1.6)
Italy		09.00 Preliminary GDP Q/Q% (Y/Y%)	Q4	<u>0.1 (0.3)</u>	0.1 (0.3)
Spain		08.00 Preliminary GDP Q/Q% (Y/Y%)	Q4	<u>0.4 (1.7)</u>	0.4 (1.9)
		08.00 Preliminary CPI (EU-harmonised CPI) Y/Y%	Jan	1.0 (1.1)	0.8 (0.8)
UK		00.01 GfK consumer confidence indicator	Jan	-9	-11
		09.30 Net consumer credit (net mortgage lending) £bn	Dec	0.9 (4.1)	0.6 (4.1)
		09.30 Mortgage approvals '000s	Dec	65.7	65.0

*Approximate date of release. Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

The coming week's key events & auctions

Country	GMT	Event / Auction
Monday 27 January 2020		
- Nothing scheduled -		
Tuesday 28 January 2020		
Euro area	 16.00	ECB Economist Lane to participate in panel discussion on 'Fiscal rules in Europe'
Italy	 10.00	Auction: €2bn of 2021 0% bonds
	 10.00	Auction: 0.1% 2023 index-linked bonds
UK	 10.30	Auction: 0.875% 2029 bonds
Wednesday 29 January 2020		
Germany	 10.30	Auction: €4bn of 2025 bonds
Thursday 30 January 2020		
Italy	 10.00	Auction: 5Y and 10Y bonds
UK	 12.30	BoE Governor Carney speaks following policy announcement
Friday 31 January 2020		
Germany	 -	German sovereign debt to be rated by Moody's

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

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<https://www.uk.daiwacm.com/ficc-research/recent-blogs>

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