

Euro wrap-up

Overview

- Bunds made modest losses as the euro area flash PMIs suggested a modest pickup in economic growth in February.
- Gilts closed little changed on the day as the UK flash PMIs also beat expectations.
- The coming week will bring further economic surveys from the euro area and UK, and the first estimates of February inflation in the large member states.

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Daily bond market movements

Bond	Yield	Change
BKO 0 12/21	-0.652	+0.007
OBL 0 04/25	-0.621	+0.014
DBR 0 02/30	-0.438	+0.009
UKT 3¼ 09/21	0.514	-0.007
UKT 1 04/24	0.458	+0.001
UKT 0% 10/29	0.569	-0.008

*Change from close as at 4:30pm GMT.

Source: Bloomberg

Euro area

Flash PMIs beat expectations

Contrary to expectations of renewed deterioration, the euro area flash PMIs improved in February to suggest a modest uptick in economic growth momentum. The headline composite PMI rose a mere 0.3pt, but that was enough to take it to a six-month high of 51.6, broadly consistent with GDP growth of almost 0.2%Q/Q. And the improvement appeared relatively broad based. The headline services PMI reversed the previous 0.3pt drop to match December's four-month high of 52.8, suggesting ongoing resilience in the sector that has been the principal source of economic growth over the past couple of years. And the headline manufacturing PMI rose 1.2pts to a twelve-month high of 49.1, implying further stabilisation in the sector that has been contracting steadily for several quarters.

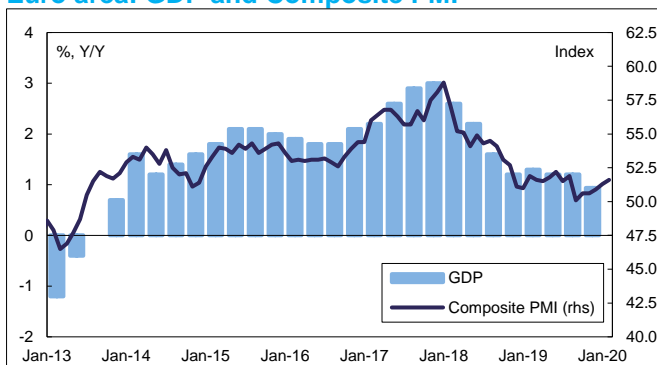
Initial impact of the coronavirus reflected in survey detail

The survey detail was not, however, quite as encouraging as the headline numbers suggested. Indeed, there was clear evidence of an initial impact from the coronavirus, which risks becoming more pernicious over coming months. Due to its arithmetic design, the headline euro area manufacturing PMI was counter-intuitively boosted by a marked lengthening of supplier delivery times, with the biggest shift in the respective index since 2010, to suggest the most widespread delays since end-2018. And manufacturers' new export orders reportedly fell at a notably steeper pace than last month. Nevertheless, benefiting from improved domestic demand, the euro area manufacturing PMIs for output (up 0.4pt to a twelve-month high of 48.4) and total new orders (up 0.2pt to a fifteen-month high of 49.2) ticked up to suggest that the sector was less of a drag on growth. Meanwhile, despite the reported pickup in services activity, inflows of new business into the sector weakened to a three-month low, reportedly due to softer demand for travel, tourism and certain business services on account of the coronavirus outbreak. And, overall, the euro area composite indices also suggested that job growth has slowed to a five-year low, and a softening of inflationary pressures to the softest in more than three years.

Contrasting developments in Germany and France

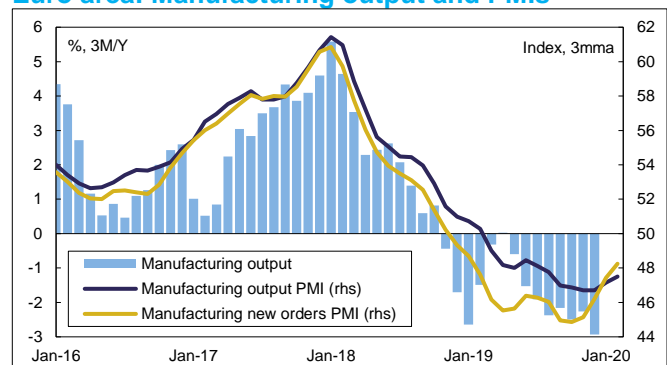
At the country level, the flash February PMIs were rather mixed. Germany's composite PMI edged down 0.1pt from January's five-month high to 51.1, consistent with still-minimal economic growth. Similar to the euro area index, a jump in the German manufacturing PMI – flattered by a sharp increase in supplier delivery times – suggested the softest decline in activity in thirteen months. But German services sector activity reportedly softened significantly to negate the impact on overall economic output. In marked contrast, the French manufacturing PMI dropped below 50 to suggest contraction in the sector for the first time in seven months. But growth in services reportedly accelerated to a five-month high to push the

Euro area: GDP and Composite PMI



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

Euro area: Manufacturing output and PMIs



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



French composite PMI up 0.8pt to 51.9, bang in line with the average of the past six months. However, the flash French PMIs, particularly for services, are often subject to significant revision in the final estimates. And as the adverse impact of the coronavirus seems likely to grow as time goes on, we do expect today's figures to be revised down when the final estimates are published on 4 March.

Underlying inflation softening in the New Year?

The final estimates of euro area inflation in December brought minimal revisions from the flash figures. The headline annual HICP rate was left unchanged at 1.4%Y/Y, up 0.1ppt from December to a nine-month high. But as suggested by the preliminary estimates, the rise largely reflected higher energy inflation (confirmed to have increased by 1.6ppts, a little less than previously thought, to an eight-month high of 1.8%Y/Y). No material changes were made to the estimates of inflation of services (down 0.3ppt to a three-month low of 1.5%Y/Y) or non-energy industrial goods (down 0.2ppt to 0.3%Y/Y, also the lowest since October). So, core inflation was confirmed at 1.1%Y/Y, down 0.2ppt from the prior two months. And calculations based on the detail published for the first time saw 'supercore' measures of inflation, which reflect the most cyclically-sensitive prices, fall back to their lowest since July. As such, today's data suggested that the 'mild' uptrend in underlying inflation cited previously by the ECB might well have softened at the start of the year. And with economic growth set to remain sub-potential over the near term at least, we expect no meaningful rise in underlying inflation – whether measured by core or 'supercore' indicators – over the coming twelve months. And so we also expect the ECB's current inflation target of close to 2.0%Y/Y to remain out of reach for the foreseeable future.

The week ahead in the euro area and US

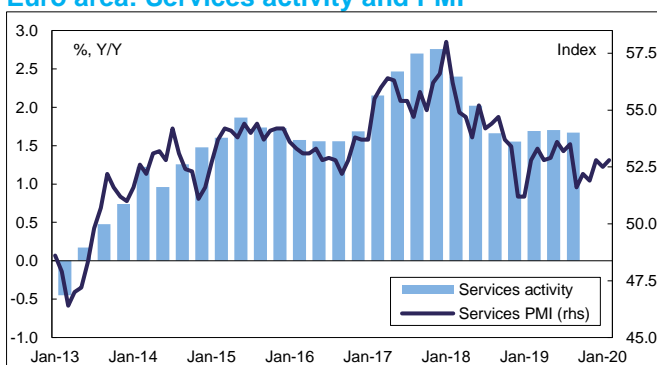
The coming week brings further survey results for February including, on Thursday, the European Commission's economic sentiment indices, which often provide the most reliable guide to activity. If today's PMIs are anything to go by, the Commission's survey should post improvements in the main industry and services confidence indicators. And after yesterday's upside surprise to the Commission's flash estimate of consumer confidence, the headline economic sentiment indicator is highly likely to have risen further from the seven-month high of 102.8 recorded in January. National confidence survey results also due in the coming week include the German ifo indices (Monday), as well as the French INSEE business and consumer indicators (Tuesday and Wednesday respectively).

Separately, the back end of the week will bring the first indications of inflation in February, with the Spanish flash estimates due on Thursday and the equivalent numbers from Germany, France and Italy due on Friday. (The euro area's preliminary CPI estimate for February, which is not due until 3 March, is eventually likely to show that headline inflation eased on the back of lower energy prices, while core inflation likely edged only very slightly higher, albeit to a still subdued 1.2%Y/Y.)

Friday will also bring revised French national accounts figures, which are likely to confirm that GDP growth slowed sharply to -0.1%Q/Q in Q4, the first quarterly contraction in 2½ years. Likely of more interest will be updated German GDP figures on Tuesday, which will bring the first official expenditure breakdown. This is likely to confirm that the euro area's largest economy stagnated in the final quarter of last year as household and government spending slowed. Other releases due at the end of the coming week include German unemployment data for February and French consumer spending for January. ECB Governing Council members due to speak in the coming week include President Lagarde (Wednesday) and Executive Board members Lane, de Guindos, Schnabel and Panetta (all Thursday). In the markets, Italy will sell index-linked and zero-coupon bonds on Wednesday, while Germany will sell 5Y OBLs the following day.

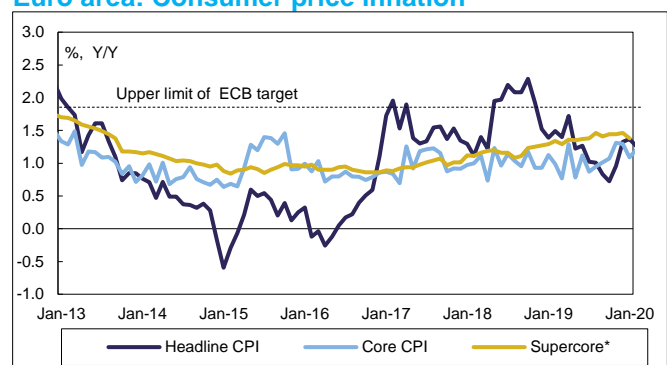
In the US, a relatively quiet start to the coming week will bring the Chicago Fed national activity index on Monday, followed by the Conference Board's consumer confidence survey on Tuesday. That day will also kick off the week's housing market indicators with the FHFA and S&P Corelogic home prices indices for December, followed by new and existing home sales figures for January on Wednesday and Thursday respectively. Thursday will also bring revised Q4 GDP numbers – likely to confirm that growth was little changed from the initial estimate of 2.1%Q/Q annualized – as well as the more timely release of

Euro area: Services activity and PMI



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

Euro area: Consumer price inflation



*Supercore includes the most cyclically sensitive prices but excludes package holidays. Source: Bloomberg, Thomson Reuters & Daiwa Capital Markets Europe Ltd.

durable goods orders data for January. Friday's release of advance goods trade and inventories figures for January will also provide an update on economic activity at the start of the year, while personal income and spending data, including the monthly deflators, for the same month will also be closely watched. Elsewhere, the Fed's Mester, Clarida, Evans and Bullard are also due to speak publicly, while in the markets the Treasury will sell 2Y notes on Tuesday, 5Y notes and 2Y floating-rate notes on Wednesday and 7Y notes on Thursday.

UK

Composite PMI supported by manufacturing improvement

Like in the euro area, the flash UK PMIs for February exceeded expectations and at face value suggested that economic conditions are now much improved from the weakness seen at the end of 2019. For example, the headline manufacturing PMI rose 1.9pts in February to 51.9, with a further notable jump in the output component to 52.8, leaving it more than 7pts higher than December's low and similarly at its highest since last April. So, while the services PMI fell back somewhat (by 0.6pt) to 53.3, the headline composite PMI moved sideways at 53.3, the joint highest reading since September 2018. Admittedly, this was consistent with only a modest recovery in GDP growth in Q1 – Markit's nowcast aligns with our own forecast for growth of 0.2%Q/Q. And the detail of the report illustrated that despite the improved headline numbers, risks to the near-term outlook – related not least to the impact of the coronavirus – are still firmly skewed to downside.

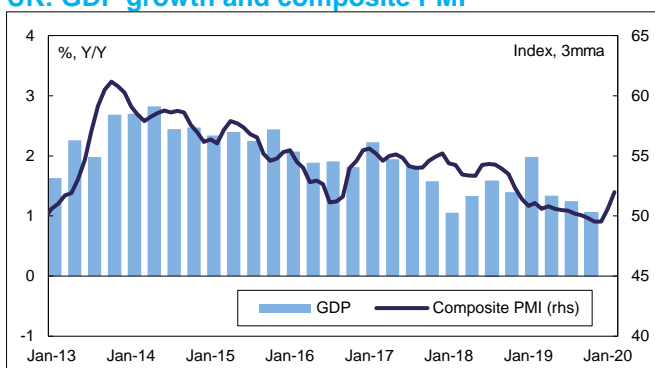
But detail flagged concerns about outlook

The detail of the manufacturing survey did at least imply that output strengthened in February, while a further increase in new orders – the relevant PMI rose 1.4pts to a ten-month high of 52.3 – and a notable pickup in overseas orders suggest a more encouraging near-term production outlook. But like in the euro area, today's survey also suggested that supply chain disruption represents a new headwind for certain manufacturers. For example, the survey's index for stocks of inputs reportedly declined at the steepest pace for over seven years. And, like in the euro area, the headline PMI was boosted by a significant lengthening of suppliers' delivery times – indeed, the 7pt drop in the relevant index was the largest monthly decline since the series started almost three decades ago. The detail of the services survey also flagged possible weakness ahead, with the new business index down 0.7pt as respondents cited reduced tourism-related bookings and cancellations to destinations more directly affected by the outbreak.

The week ahead in the UK

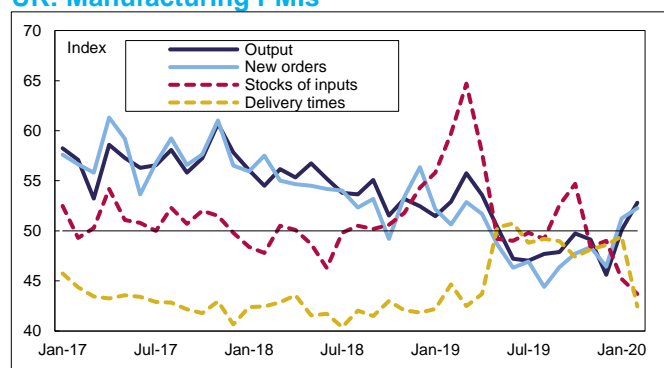
The coming week will be relatively quiet for top-tier economic releases from the UK, with just a couple of surveys providing an update on conditions in the middle of Q1. In particular, Tuesday's CBI distributive trades survey is expected to show that retail sales growth remained relatively subdued in February having signalled no meaningful growth at the start of the year. This would be consistent with still relatively weak consumer confidence, which Friday's GfK survey is likely to confirm – indeed, the headline sentiment index is expected to have fallen very slightly from the seventeen-month high of -9 recorded in January. BoE MPC members scheduled to speak in the coming week include Chief Economist Haldane (Monday and Friday) and Deputy Governor Cunliffe (Thursday). In the markets, the DMO will sell 10Y Gilts on Tuesday.

UK: GDP growth and composite PMI*


















*February figure is flash estimate. Source: Markit, Thomson Reuters and Daiwa Capital Markets Europe Ltd.

UK: Manufacturing PMIs*



*February figures are flash estimates. 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	0.8	0.6
Germany 	0.2	0.0	0.2	0.2	0.2	0.2	0.2	0.0	0.6	0.5	0.6
France 	0.3	-0.1	0.3	0.3	0.2	0.2	0.2	0.2	1.2	0.8	0.8
Italy 	0.1	-0.3	0.2	0.1	0.0	-0.1	0.0	-0.1	0.2	0.0	-0.1
Spain 	0.4	0.5	0.3	0.4	0.4	0.4	0.4	0.2	2.0	1.5	1.2
UK 	0.5	0.0	0.2	0.3	0.3	0.3	0.1	0.3	1.4	0.9	0.8
Inflation forecasts %, Y/Y											
Euro area											
Headline CPI 	1.0	1.0	1.3	1.1	1.3	1.3	1.3	1.2	1.2	1.3	1.3
Core CPI 	0.9	1.2	1.2	1.2	1.2	1.1	1.2	1.1	1.0	1.2	1.2
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	-0.50	-0.50	-0.50	-0.50	-0.50
Net asset purchases* 	0	20	20	20	20	20	20	20	20	20	20
BoE											
Bank Rate % 	0.75	0.75	0.75	0.75	0.75	0.75	0.75	0.75	0.75	0.75	0.75
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/ <i>Daiwa forecast</i>	Previous	Revised
EMU 	Preliminary manufacturing PMI (services PMI)	Feb	49.1 (52.8)	47.5 (52.3)	47.9 (52.5)	-
	Preliminary composite PMI	Feb	51.6	51.0	51.3	-
	Final CPI (core CPI) Y/Y%	Jan	1.4 (1.1)	1.4 (1.1)	1.3 (1.3)	-
Germany 	Preliminary manufacturing PMI (services PMI)	Feb	47.8 (53.3)	44.8 (53.8)	45.3 (54.2)	-
	Preliminary composite PMI	Feb	51.1	50.7	51.2	-
France 	Preliminary manufacturing PMI (services PMI)	Feb	49.7 (52.6)	50.7 (51.3)	51.1 (51.0)	-
	Preliminary composite PMI	Feb	51.9	51.0	51.1	-
Italy 	Industrial sales M/M% (Y/Y%)	Dec	-3.0 (-1.4)	-	0.0 (0.1)	- (0.2)
	Industrial orders M/M% (Y/Y%)	Dec	1.4 (6.0)	-	-0.3 (-4.3)	-0.2 (-)
	Final CPI (EU-harmonised CPI) Y/Y%	Jan	0.5 (0.4)	0.6 (0.5)	0.5 (0.5)	-
UK 	Preliminary manufacturing PMI (services PMI)	Feb	51.9 (53.3)	49.7 (53.4)	50.0 (53.9)	-
	Preliminary composite PMI	Feb	53.3	52.8	53.3	-
	Public sector net borrowing, excluding banks £bn	Jan	-9.8	-11.4	4.8	4.2
























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 24 February 2020					
Germany		09.00 Ifo business climate index	Feb	95.3	95.9
		09.00 Ifo current assessment balance (expectations)	Feb	98.6 (92.1)	99.1 (92.9)
Tuesday 25 February 2020					
Germany		07.00 Final GDP Q/Q% (Y/Y%)	Q4	0.0 (0.4)	0.2 (0.6)
France		07.45 Business confidence indicator	Feb	103	104
		07.45 Manufacturing confidence indicator (production outlook)	Feb	99 (-)	100 (-5)
UK		11.00 CBI distributive trades survey, reported retail sales	Feb	4	0
Wednesday 26 February 2020					
France		07.45 Consumer confidence indicator	Feb	103	104
UK		00.01 BRC shop price index Y/Y%	Feb	-0.2	-0.3
Thursday 27 February 2020					
EMU		09.00 M3 money supply Y/Y%	Jan	5.3	5.0
		10.00 Economic confidence indicator	Feb	102.5	102.8
		10.00 Industrial confidence (services)	Feb	-7.5 (11.0)	-7.3 (11.0)
		10.00 Consumer confidence	Feb	-8.2	-8.1
Italy		09.00 Consumer confidence indicator (manufacturing)	Feb	111.3	111.8 (99.9)
Spain		08.00 Preliminary CPI (EU-harmonised CPI) Y/Y%	Feb	0.8 (0.8)	1.1 (1.1)
Friday 28 February 2020					
Germany		08.55 Unemployment rate % (change '000s)	Feb	5.0 (4.5)	5.0 (-2.0)
		13.00 Preliminary CPI (EU-harmonised CPI) Y/Y%	Feb	1.7 (1.6)	1.7 (1.6)
France		07.45 Preliminary CPI (EU-harmonised CPI) Y/Y%	Feb	1.4 (1.6)	1.5 (1.7)
		07.45 Consumer spending M/M% (Y/Y%)	Jan	0.1 (0.3)	-0.3 (2.0)
		07.45 Final GDP Q/Q% (Y/Y%)	Q4	-0.1 (0.8)	0.3 (1.4)
Italy		10.00 Preliminary CPI (EU-harmonised CPI) Y/Y%	Feb	0.6 (0.4)	0.5 (0.4)
UK		00.01 GfK consumer confidence indicator	Feb	-8	-9
		00.01 Lloyds business barometer	Feb	-	23
		- Nationwide house price index* M/M% (Y/Y%)	Feb	0.4 (2.3)	0.5 (1.9)

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

The coming week's key events & auctions

Country	GMT	Event / Auction
Monday 24 February 2020		
EMU		08.20 ECB President Lagarde scheduled to speak
UK		18.30 BoE Chief Economist Haldane scheduled to speak
Tuesday 25 February 2020		
UK		10.30 Auction: £3.25bn of 0.875% 2029 bonds
Wednesday 26 February 2020		
Germany		11.30 Auction: €4bn of 0% 2025 bonds
Thursday 27 February 2020		
Italy		10.00 Auction: 5Y and 10Y bonds
UK		18.30 BoE's Cunliffe scheduled to speak
Friday 28 February 2020		
UK		11.15 BoE Chief Economist Haldane scheduled to speak

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

Access our research blog at:

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

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