

Overview

- As the coronavirus continued to spread across Europe, Bunds made further modest gains.
- Gilts also made gains as Governor-designate Bailey suggested that the BoE would need to act quickly to address the economic and financial impact of the coronavirus.
- Thursday will bring the German construction PMI and UK car registration data while Friday will bring German factory orders figures.

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Daily bond market movements

Bond	Yield	Change
BKO 0 03/22	-0.850	-0.024
OBL 0 04/25	-0.830	-0.017
DBR 0 02/30	-0.638	-0.009
UKT 0½ 07/22	0.205	-0.024
UKT 0% 06/25	0.253	-0.010
UKT 4% 12/30	0.374	-0.015

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

Euro area

ECB restricts its own activities due to the coronavirus

Reuters reported this morning that the ECB's Governing Council held a special teleconference call last night to assess the impact of the coronavirus outbreak. But despite yesterday's G7 teleconference and the Fed's emergency rate cut, a monetary policy response was not on the agenda. Instead, the call focused merely on operational issues, and was followed today by an announcement that the ECB had banned all non-essential travel for its staff until 20 April. With the exception of its monetary policy press conferences, it also postponed its conferences and all non-essential visits to its site over the same period. And it put on hold its forthcoming "ECB Listens" event in Brussels, organised as part of its strategic policy review. We still don't expect the possibility of monetary easing to be discussed by the Governing Council before next week's scheduled policy meeting. But all the more so now that it is actively curtailing its own demand due to the epidemic, the Governing Council will be well aware of the extent to which the coronavirus is already hitting economic activity in the euro area.

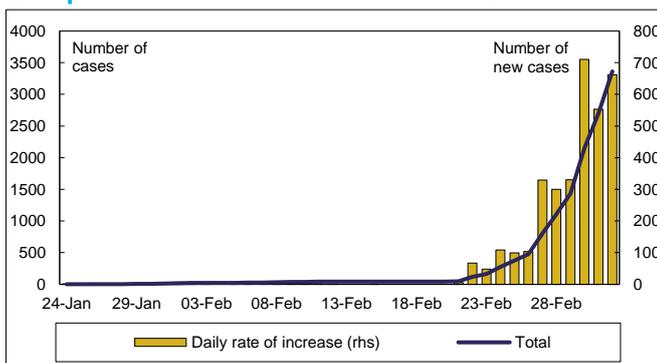
Euro area retail sales & German car registrations subdued

Data-wise, retail sales in the euro area started the year on a positive note, rising in real terms by 0.6%M/M and 1.7%Y/Y. That left growth on a three-month basis steady at a nevertheless subdued 0.2%3M/3M. Moreover, as it reversed merely half of the drop in December, and big question marks hang over prospects for spending in February and March, today's figures suggest risks of a very weak Q1 for retailers. Indeed, sales in January were flattered by stronger spending on food and fuel – excluding those items core sales were up a smaller 0.4%M/M following a similar drop of more than 1.0%M/M in December. Among those countries to publish equivalent data, Germany (up 0.9%M/M in January following a drop of 2.0%M/M previously) and France (up 0.2%M/M following a drop of 1.0%M/M previously) failed to reverse their respective drops in December. Separately, according to the KBA, German new car registrations fell a steep 10.8%Y/Y in February following a decline of 7.3%Y/Y the previous month. We expect a weak first quarter for German car sales to be followed by subdued sales throughout the year, leaving full-year registrations in 2020 well down on last year.

Services PMI not representative of new downside risks

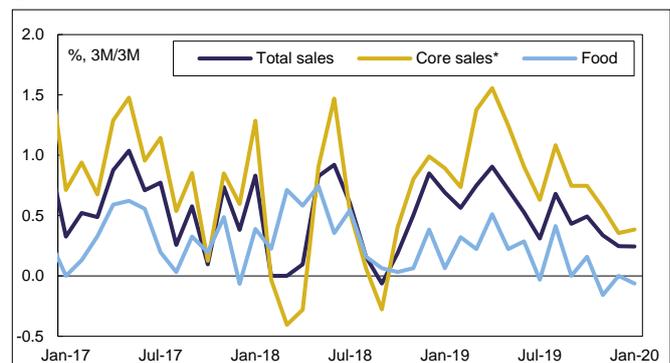
Today's final services PMI reported a modest downwards revision to the euro area's headline activity index in February, by 0.2pt to 52.6, admittedly leaving it 0.1pt higher than in January and slightly above the average of the past six months. But while a little more than 20% of respondent firms submitted their assessments subsequent to the flash release, the coronavirus outbreak across Europe has intensified significantly since the survey was completed (25 February) – indeed, the number of confirmed cases among the four largest euro area member states has risen by almost 9 nine times since then to

Europe: Number of coronavirus COVID-19 cases



Source: WHO and Daiwa Capital Markets Europe Ltd.

Euro area: Retail sales



*Excluding food and fuel. Source: Thomson Reuters and Daiwa Capital Markets Europe Ltd.



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more than 3000. Nevertheless, February's survey was already flagging downside risks to services exports not least due to reduced tourism, with the export orders PMI down 1.1pts on the month to 47.3, the lowest since this component was first compiled in 2014. And with export orders in the manufacturing sector having also fallen, the composite export orders PMI declined a sharp 1.7pts to 47.6. So, while the headline composite output PMI was unchanged at the flash estimate (51.6), which itself was 0.3pt higher than in January, this in no way can reflect the significant worsening of conditions over recent weeks. And with concerns about the impact of the coronavirus continuing to rise, we would expect to see a notable decline in the current month's PMIs (the flash release is due 24 March).

For what it's worth, at the country level, the final German composite PMI was revised down by 0.4pt from the flash to 50.7, while the equivalent French figure was nudged slightly higher to 52.0. And although there was also a pickup in the Italian composite PMI (by 0.3pt), it remained at a paltry 50.7 and consistent with still weak growth. Moreover, with 95% of Italian firms having responded by 24 February, we fully expect a marked decline in the index back into contractionary territory in March.

The coming two days in the euro area and US

After a relatively quiet day for euro area economic data tomorrow – the German construction PMI for February is the only release of note – Friday will bring several releases including German factory orders data for January. While these are expected to report a pickup in orders at the start of the year, this follows a particularly poor end to 2019 where they fell to their lowest level since the start of 2017. So orders will remain considerably lower compared with a year earlier in January. And the coronavirus outbreak over recent weeks seems bound to weigh on orders going forward too. Friday will also bring the latest French trade and Spanish IP figures for January. In the markets, France and Spain will sell bonds with various maturities on Thursday.

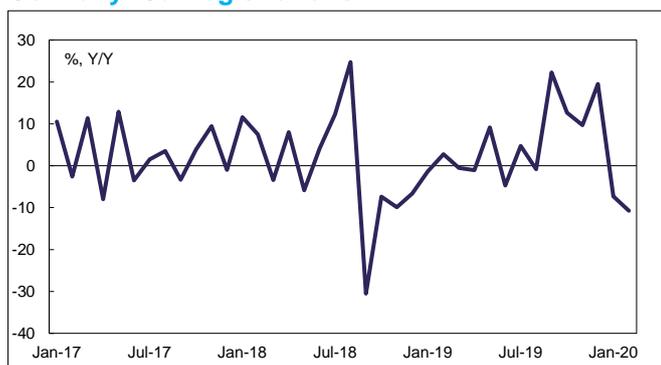
In the US, tomorrow will bring factory orders data for January (including updated durable goods orders), revised productivity and unit labour costs numbers for Q4 and Challenger Job Cuts figures for February. Most attention, however, will be on Friday's BLS labour market report, which is expected to show that non-farm payrolls increased by a solid 175k last month, down from the 225k rise seen in January but in line with the average of 2019. The unemployment rate is expected to be unchanged at 3.6%, while average weekly earnings growth remained close to 3%Y/Y. The end of the week will also bring full-month trade figures for January and consumer credit numbers for the same month. There are several voting FOMC members in action over the remainder of the week, including Kaplan (tomorrow), Williams and Mester (Friday).

UK

Bailey suggests BoE needs to act quickly

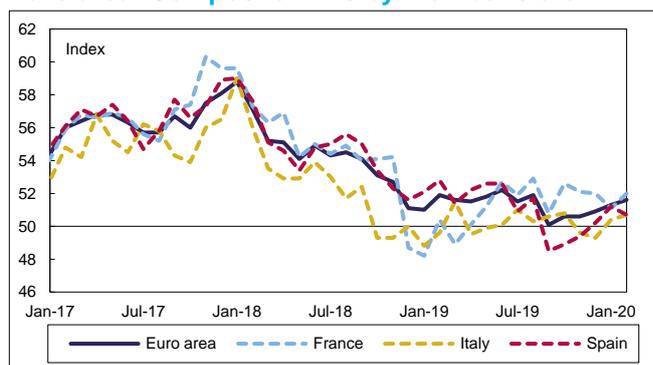
Following yesterday's Fed rate cut and comments from soon-to-depart [Governor Carney](#) that the BoE is ready to take "all necessary steps" to address the risks posed by the coronavirus, financial market expectations of a cut to Bank Rate this month increased further today. While the number of coronavirus cases in the UK remains below the levels in Italy, France and Germany, it still rose more than 50% from yesterday (to 85 at the time of writing), and is expected to reach epidemic proportions. Moreover, comments today from Andrew Bailey, who will succeed Carney as Governor on 16 March, reinforced the impression given by Carney that the BoE is preparing to act soon. In particular, Bailey stated that the BoE would need to coordinate closely with the Government and move very quickly to mitigate the economic and financial risks. In terms of policy specifics, he stated that the BoE would need to facilitate the provision of supply-chain finance to assist affected small and medium-sized companies. But such action would not preclude an easing of monetary policy too. He largely refrained from giving an explicit view on Bank Rate, apart from noting that it could theoretically be cut as low as 0.1%. But there are very strong reasons to expect the BoE to announce a rate cut of at least 25bps, as well as a new special funding scheme, before the end of the month, whether under Carney's or Bailey's leadership.

Germany: Car registrations



Source: Bloomberg, KBA and Daiwa Capital Markets Europe Ltd.

Euro area: Composite PMIs by member state



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

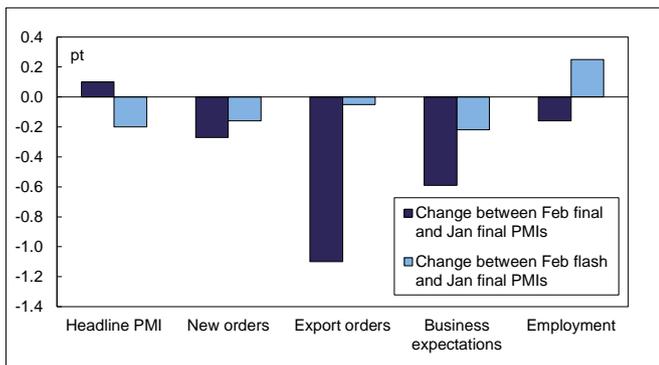
Services PMI flags downside risks ahead

Like in the euro area, there was only a modest downwards revision (0.1pt) to the UK’s final services headline PMI in February. Indeed, the index still stood at 53.2, the second-highest reading for eighteen months, nevertheless 0.7pt lower than in January. And while just 16% of responses incorporated in the final release had not been included in the flash estimates, there were still signs of increased concern about the impact of the coronavirus on certain sectors, most notably related to tourism. For example, the services export orders PMI fell an additional 0.7pt from the flash (more than 4pts in weighted terms) to leave it more than 2½pts lower than January. And the report also suggested that confidence more generally had weakened, despite a pickup in the business expectations PMI to its highest since mid-2014. Taken together with a weaker manufacturing PMI earlier this week, the final composite PMI was revised down by 0.3pt to 53.0. While this remains consistent with a return to positive GDP growth in Q1, like in the euro area, we would expect a notable weakening in overall business conditions this month, and likely beyond.

The day ahead in the UK

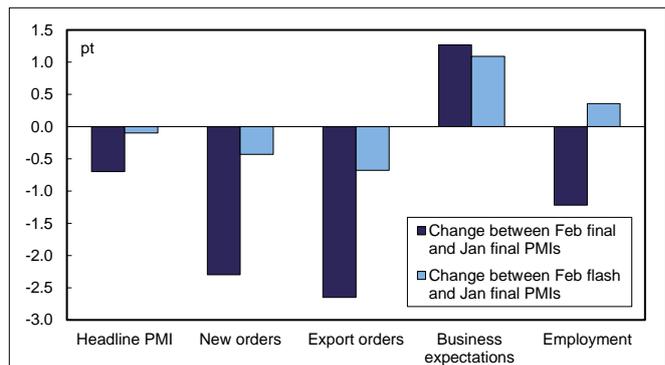
In the UK, tomorrow will bring new car registration figures for February, which are likely to show a further decline on the back of still relatively subdued domestic demand. Friday, meanwhile, will bring the REC/KPMG Report on UK Jobs, which provide an update on labour market conditions last month. But perhaps of greater interest will be BoE Chief Economist Haldane’s speech at an OECD conference tomorrow, while outgoing Governor Carney is due to speak in London. In the markets, the DMO will sell 8Y linkers on Thursday.

Euro area: Services PMI



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

UK: Services PMI



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

In the absence of significant news, the next edition of the Euro wrap-up will be published on 06 March 2020

European calendar

Today's results

Economic data

Country	Release	Period	Actual	Market consensus/ <i>Daiwa forecast</i>	Previous	Revised
EMU	 Final services (composite) PMI	Feb	52.6 (51.6)	52.8 (51.6)	52.5 (51.3)	-
	 Retail sales M/M% (Y/Y%)	Jan	0.6 (1.7)	0.6 (1.1)	-1.6 (1.3)	-1.1 (1.7)
Germany	 Retail sales M/M% (Y/Y%)	Jan	0.9 (1.8)	0.9 (1.5)	-3.3 (0.8)	-2.0 (1.7)
	 Final services (composite) PMI	Feb	52.5 (50.7)	53.3 (51.1)	54.2 (51.2)	-
France	 Final services (composite) PMI	Feb	52.5 (52.0)	52.6 (51.9)	51.0 (51.1)	-
Italy	 Services (composite) PMI	Feb	52.1 (50.7)	51.3 (50.1)	51.4 (50.4)	-
	 Final GDP Q/Q% (Y/Y%)	Q4	-0.3 (0.1)	-0.3 (0.0)	0.1 (0.3)	-
Spain	 Services (composite) PMI	Feb	51.8 (52.1)	52.5 (51.7)	52.3 (51.5)	-
UK	 Final services (composite) PMI	Feb	53.2 (53.0)	53.3 (53.3)	53.9 (53.3)	-

Auctions

Country	Auction
UK	 sold £3.5bn of 0.625% 2025 bonds at an average yield of 0.222%

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

Tomorrow's data releases

Economic data

Country	GMT	Release	Period	Market consensus/ <i>Daiwa forecast</i>	Previous
Germany	 08.30	Construction PMI	Feb	-	54.9
UK	 09.00	New car registrations Y/Y%	Feb	-	-7.3

Auctions and events

Country	GMT	Auction / Event
France	 09.50	Auction: 0% 2029 bonds
	 09.50	Auction: 1.25% 2034 bonds
	 09.50	Auction: 0.75% 2052 bonds
Spain	 09.45	Auction: 0% 2023 bonds
	 09.45	Auction: 0% 2025 bonds
	 09.45	Auction: 0.5% 2030 bonds
	 09.45	Auction: 0.7% 2033 index-linked bonds
UK	 10.30	Auction: £1.1bn of 0.125% 2028 index-linked bonds
	 13.00	BoE Chief Economist Haldane scheduled to speak
	 17.00	BoE Governor Carney scheduled to speak

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

Friday's data releases

Economic data

Country	GMT	Release	Period	Market consensus/ <i>Daiwa forecast</i>	Previous
Germany	 07.00	Factory orders M/M% (Y/Y%)	Jan	1.3 (-5.2)	-2.1 (-8.7)
France	 07.45	Trade balance, €bn	Jan	-4.8	-4.1
Italy	 09.00	Retail sales M/M% (Y/Y%)	Jan	-	0.5 (0.9)
Spain	 08.00	Industrial production M/M% (Y/Y%)	Jan	0.5 (-1.4)	-1.4 (0.8)

Auctions and events

Country	GMT	Auction / Event
EMU	 15.30	ECB's Hernández de Cos scheduled to speak
UK	 00.01	REC/KPMG Report on UK Jobs

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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