Euro wrap-up

Overview

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- While the flash euro area March composite PMI fell to a record low, Bunds made losses and euro area stocks rallied the most since 2008 as risk appetite improved.
- Gilts also made losses and UK equities rallied even as the UK PMIs similarly suggested a record drop in the economic activity.
- Wednesday will bring the final March ifo business survey from Germany along with a March retail survey and February inflation data from the UK.

Daily bond market movements

Bond	Yield	Change
BKO 0 03/22	-0.669	+0.065
OBL 0 04/25	-0.523	+0.038
DBR 0 02/30	-0.331	+0.053
UKT 0½ 07/22	0.119	+0.048
UKT 0⅝ 06/25	0.254	+0.047
UKT 4¾ 12/30	0.469	+0.044

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

Euro area

Flash PMIs signal record drop in activity

Perhaps inevitably, the flash euro area PMIs for March indicated a drop in economic activity sharper than any seen during the global financial crisis in 2009. The headline euro area composite PMI plunged more than 20pts, the most on the series dating back to 1998, to a record low of 31.4. Reflecting the controls on consumer-facing activity, not least in the hospitality and travel sub-sectors, the biggest decline was recorded in the services PMI, which dropped more than 24pts to just 28.4, more than 10pts below the previous record low. The headline manufacturing PMI fell a more moderate 4.4pts to 44.8. But that figure was flattered by the increase in supplier delivery times, reflecting severe supply-chain disruption, which inappropriately contributed positively. A better guide to activity in that sector was provided by the manufacturing output index, which fell more than 9pts to 39.5, suggesting the steepest drop in production since April 2009.

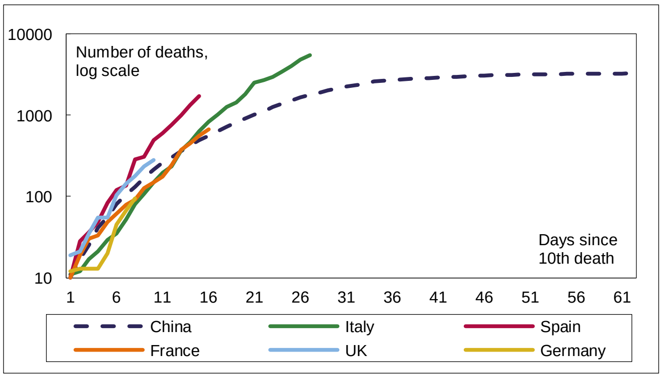
Orders evaporating, jobs and prices being slashed

Among other details, despite the measures implemented by governments to subsidise the wages of furloughed or short-time workers and to support the flow of credit, the euro area employment PMI fell more than 8pts to 43.2, suggesting that jobs are being cut at the fastest rate since July 2009. In addition, the euro area composite new orders PMI fell more than 20pts to a series low of 29.5, with weakness in services and manufacturing alike and from home and abroad, to suggest (predictably) that activity will weaken significantly in Q2. Indeed, the survey measure of expectations of future output in both sectors also dropped sharply to an all-time low. And faced with evaporating demand, the PMIs for output prices in services and manufacturing fell below 50, suggesting the steepest drop in prices since January 2010.

Deep contraction across the euro area

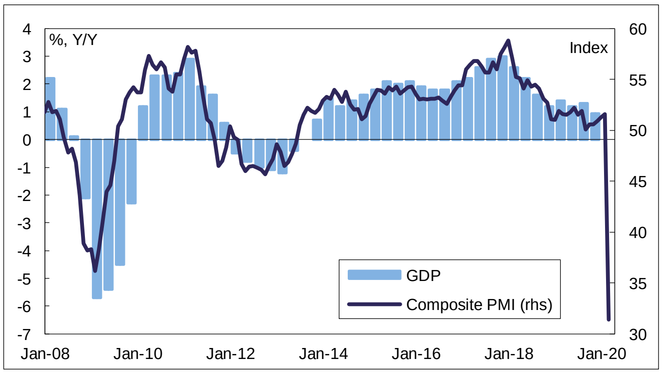
At the country level, the picture painted by the flash PMIs was uniformly gloomy. The French composite PMI fell by a record margin of almost 22pts to just 30.2, a series low. While the French PMI for services also hit a record low, the equivalent index for manufacturing output fell to the lowest since March 2009. At 37.2, the German composite PMI did not fall quite so far as its French equivalent, but was still the lowest since February 2009. And the detail also signalled a record slump in services activity and the steepest drop in manufacturing output since July 2012. And, while no figures were published, Markit reported that the survey suggested an even steeper decline in economic activity in the remainder of the euro area than in France and Germany, with the service sector similarly shrinking at a record pace and manufacturing output falling the most since the global financial crisis. Overall, the survey – whose responses were submitted between 13 and 23 March – points to GDP falling at an annualised pace of around 9% this month. And given the intensification of the Covid-19 outbreak and additional

Europe: Covid-19 deaths by country



Source: WHO and Daiwa Capital Markets Europe Ltd.

Euro area: GDP growth and composite PMI*



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

lockdown measures across the member states over recent days, the PMIs and overall economic activity should be expected to deteriorate further into the second quarter.

The day ahead in the euro area and US

Wednesday will bring the final German ifo survey for March, which is likely to confirm the marked deterioration in conditions reported in the flash release. Indeed, the preliminary headline business climate index dropped more than 8pts, the most since reunification, to 87.7, the lowest level since August 2009. And the final estimate seems likely to be weaker still.

In the US, Wednesday will bring the preliminary release of February's durable goods orders, which might show some initial signs of disruption to demand related to the coronavirus as well as payback for the jump in the commercial aircraft category in the prior month. In the markets, the Treasury will sell 2Y floating-rate notes and 5Y fixed-rate notes while the Fed's UST purchases will continue.

UK

Services PMI plunges in March

As the UK commenced a form of official lockdown yesterday evening – including closure of all stores bar supermarkets, pharmacists and sellers of certain items considered to be essential, and new constraints on freedom of movement – today's flash PMIs for March illustrated the substantial hit already being felt across the UK's economy. Like elsewhere, the blow has been particularly severe to services, with hospitality and tourism principally impacted by travel restrictions previously in place elsewhere in Europe, Asia and US. Indeed, the headline services PMI fell more than 17pts, the most since the series began in 1997, to 35.7, substantially weaker than the lows experienced during the global financial crisis. And with the flash survey having been conducted before the government's decision to close pubs, restaurants and other leisure facilities late on 20 March, the final release (due 3 April) seems bound to be even worse. Even before this, services firms were extremely gloomy about the near-term outlook, with sharp declines in new orders and business expectations to record lows causing companies to cut their workforces by the most since mid-2009.

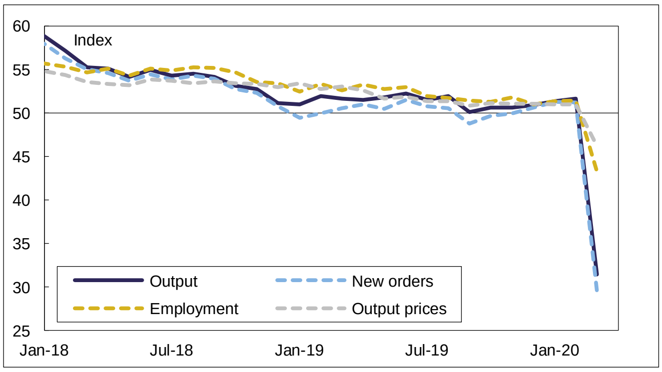
Manufacturing PMI flattered by supply-chain strife

Like in the euro area, the drop in the UK's headline manufacturing PMI was less striking, down 3.7pts to 48.0, a three-month low. But as elsewhere, this masked the full extent of the deterioration in conditions in the sector, as it was flattered by the lengthening of suppliers' delivery times for which the relevant PMI dropped to a record-low 34.8. Indeed, the decline in the survey's output and new orders components – down 8pts to 44.3 and 7pts to 44.9 respectively – better illustrated the deep contraction underway in the sector. And while the CBI's latest industrial trends survey today suggested that the drop in new orders was steeper than in October ahead of the previous Brexit deadline, it also indicated that manufacturers expect output to contract over the coming three months at the steepest pace since early 2009.

Composite PMI at record low

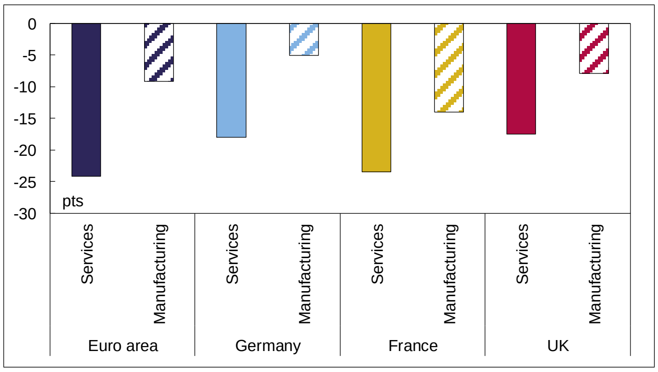
Overall, the composite PMI fell a whopping 15.9pts in March to 37.1, the lowest since the series began in the late 1990s. The survey suggested that new orders declined at the fastest pace since the Global Financial Crisis, while firms' expectations for future output also plunged. And so they also reportedly cut their workforces by the most since 2009. While the government's Coronavirus Job Retention Scheme announced at the end of last week should support to some extent the near-term labour market outlook, while other support measures should support the flow of credit to struggling firms, there is no doubt that the UK's economy is in for a tough time ahead. Markit judged the March composite PMI to be consistent with GDP contracting at a quarterly pace of 1½-2%Q/Q. And with the country set to remain at least in its current form of lockdown for at least the

Euro area: Composite PMI by component*



*March figures are flash estimates. Source: Markit, Thomson Reuters and Daiwa Capital Markets Europe Ltd.

Europe: Monthly change in output PMIs in March*



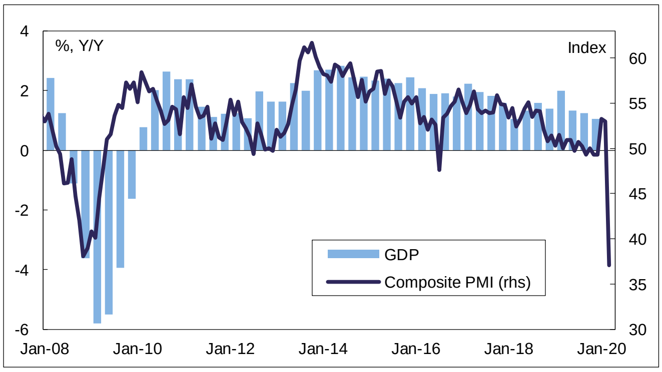
*Figures are flash estimates. Source: Markit, Thomson Reuters and Daiwa Capital Markets Europe Ltd.

coming three weeks, risks that certain other sectors (e.g. construction) could be forced to reduce activity soon, and conditions set to remain extremely challenging once restrictions ease, we anticipate a deep recession in the first half the year with only minimal recovery thereafter. Indeed, we currently expect the peak-to-trough decline to be more severe than the 6% contraction seen during the 2008-09 slump.

The day ahead in the UK

Tomorrow will bring the CBI distributive trades survey for March. While food retailers will have seen a marked increase in sales due to panic buying this month, other retailers are likely to indicate a sharp drop in spending at the end of the first quarter. Wednesday will also bring the latest CPI figures for February. Against the backdrop of the weaker oil price, headline inflation is expected to have fallen to 1.5%Y/Y. But with underlying price pressures subdued, core inflation is likely to have edged slightly lower too.

UK: GDP growth and composite PMI*



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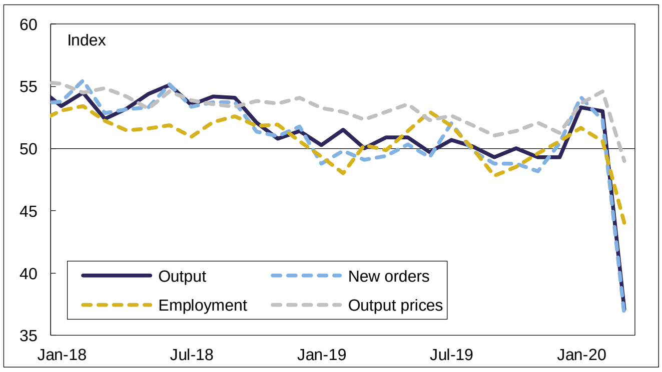
UK: Composite PMI by component*



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European calendar

Today's results

Economic data

Country		Release	Period	Actual	Market consensus/ *Daiwa forecast*	Previous	Revised
EMU		Preliminary manufacturing PMI (services)	Mar	**44.8 (28.4)**	39.0 (39.5)	49.2 (52.6)	-
		Preliminary composite PMI	Mar	**31.4**	38.8	51.6	-
Germany		Preliminary manufacturing PMI (services)	Mar	**45.7 (34.5)**	39.9 (43.0)	48.0 (52.5)	-
		Preliminary composite PMI	Mar	**37.2**	41.0	50.7	-
France		Preliminary manufacturing PMI (services)	Mar	**42.9 (29.0)**	40.6 (40.0)	49.8 (52.5)	-
		Preliminary composite PMI	Mar	**30.2**	38.1	52.0	-
UK		Preliminary manufacturing PMI (services)	Mar	**48.0 (35.7)**	45.0 (45.0)	51.7 (53.2)	-
		Preliminary composite PMI	Mar	**37.1**	45.0	53.0	-
		CBI industrial trends survey, total orders	Mar	**-29**	-35	-18	-

Auctions

Country		Auction
Germany		sold €2.9bn of 0% 2022 bonds at an average yield of -0.65%

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

Tomorrow's releases

Country		GMT	Release	Period	Market consensus/ *Daiwa forecast*	Previous
Germany		09.00	Final ifo business climate index	Mar	87.7	96.0
		09.00	Final ifo current assessment balance (expectations)	Mar	93.8 (82.0)	99.0 (93.2)
UK		09.30	CPI (core CPI) Y/Y%	Feb	1.6 (1.5)	1.8 (1.6)
		09.30	PPI input prices (output prices) Y/Y%	Feb	-0.9 (0.9)	2.1 (1.1)
		09.30	House price index Y/Y%	Jan	2.7	2.2
		11.00	CBI distributive trade survey, total retail sales	Mar	-15	1

Auctions

Country	GMT	Auction/Event
		- Nothing scheduled -

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

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