Euro wrap-up

Overview

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- Bunds largely made modest gains and periphery bonds made losses as the euro area services PMIs plummeted, with an unprecedented plunge in the Italian and Spanish indices.
- Gilts made gains as the final UK services PMIs signalled a record pace of contraction.
- The coming week will bring a Eurogroup videoconference on Tuesday, while the latest sentiment surveys and high-frequency data from various statistical agencies will no doubt paint an extremely gloomy picture.

Daily bond market movements

Bond	Yield	Change
BKO 0 03/22	-0.702	-0.016
OBL 0 04/25	-0.618	-0.008
DBR 0 02/30	-0.442	-
UKT 0½ 07/22	0.098	-0.013
UKT 0⅝ 06/25	0.162	-0.016
UKT 4¾ 12/30	0.317	-0.016

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

Euro area

Plunge in Italian and Spanish services PMIs unprecedented

The euro area economy is undergoing a contraction of historical magnitude for peacetime. We fully expect a cumulative decline in GDP over Q1 and Q2 of more than 15%. In Italy and Spain, where the total number of lives lost has surpassed 25k, the drops in economic activity will be more severe than the total euro area figure. Indeed, today's March services PMIs from those countries showed declines to levels unprecedented in any country. The headline Italian PMI fell by a record amount – almost 35pts – to a historical low of just 17.4. And the index for incoming new business fell by more than 38pts to just 13.4. The employment PMI fell almost 10pts to a series low of 41.7, indicating a record increase in joblessness. Given the deterioration in the manufacturing series reported on Wednesday, the Italian composite output PMI fell by a record 30.5pts to 20.2, also an unprecedented low. Until the release of the Italian results, Spain's services PMIs represented the weakest ever, with the headline index plunging more than 29pts to just 23.0. As in Italy, the detail similarly reported the steepest fall in overall new business in the survey's history, down more than 27pts, likewise to just 23.0. And given the sharp drop in the manufacturing survey, Spain's composite PMI fell more than 25pts to just 26.7.

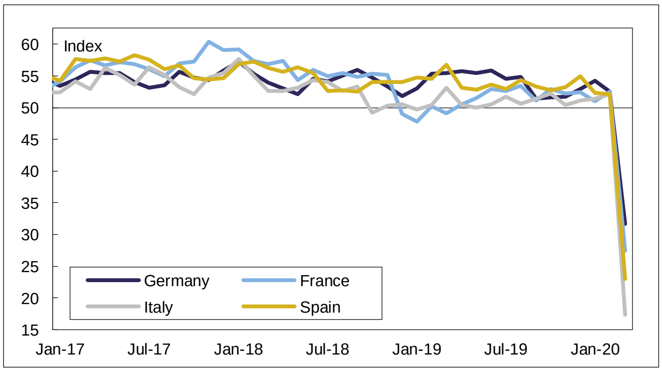
Euro area PMIs revised sharply lower

Services firms are among those most affected by the coronavirus and policies introduced to control its spread. Many sub-sectors, particularly those related to social activity, including hospitality and leisure, are simply shut down. So, it was not a great surprise that the final euro area March services PMIs also confirmed a record decline in the respective headline index. Indeed, this was revised down 2pts from the flash estimate to just 26.4, more than 13pts below the trough during the global financial crisis. So, the euro area's composite PMI was also revised down, by 1.7pts from the flash estimate to 29.7, almost 22pts lower than in February. Of course, lockdowns in the member states started well into the month. And with the number of coronaviruses cases and deaths still rising, they are set to be extended at least to the end of April, and quite possibly into May and beyond. So, the PMIs are likely to drop further in April. And with consumers likely to be reluctant to resume normal activity even once lockdowns are lifted – with the all-important tourism industry in Southern Europe seemingly destined for a terrible summer – significant weakness seems likely to persist for several months yet.

Some retailers benefit from Covid-19 outbreak

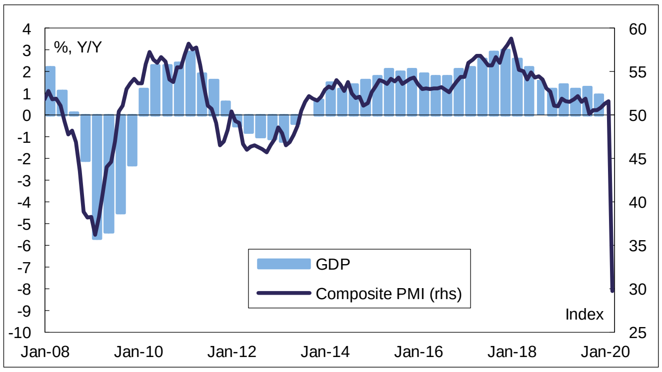
While Covid-19 is bad news for most services firms, some retailers are benefiting from increased household demand. Euro area retail sales rose for the second successive month in February and by 0.9%M/M, matching the highest rate of the past two years, to be up 3.0%Y/Y, the strongest annual rate for a year. Sales growth was positive in most member states to report

Euro area: Services PMIs by member state



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

Euro area: GDP growth and composite PMI



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

data, including Germany (1.2%M/M), France (1.1%M/M) and Spain (0.5%M/M). With household staples seeing strong growth in demand, sales of food, drinks and tobacco jumped 2.4%M/M, the most in more than two decades. Sales of pharmaceuticals and medical goods rose a solid 1.1%M/M. With consumers preferring to avoid face-to-face contact wherever possible, internet and mail order sales rose 5.6%M/M, the most in more than two years. However, sales of auto fuel fell slightly in February. We expect the pattern of sales of the February data to have intensified in March.

German car sales and production plummet

While sales of staple goods have boomed, sales of luxury items have inevitably declined. And sales of new cars have fallen off a cliff. Following the record declines in new car registrations in France, Italy and Spain in March revealed on Wednesday, today's data from the VDA confirmed the steepest decline in Germany since reunification. In particular, German new car registrations fell 38%Y/Y percent year-on-year to 215.1k, similarly the lowest March level since reunification, to leave them down 20%Y/Y over Q1 as a whole. Domestic orders were down 30%Y/Y in March while orders from abroad were down 37%Y/Y. So, car production last month also fell sharply, down 37%Y/Y to be down 20%Y/Y over Q1 as a whole. And with production halted and consumers at home for the time being, the data for April and Q2 will be significantly worse.

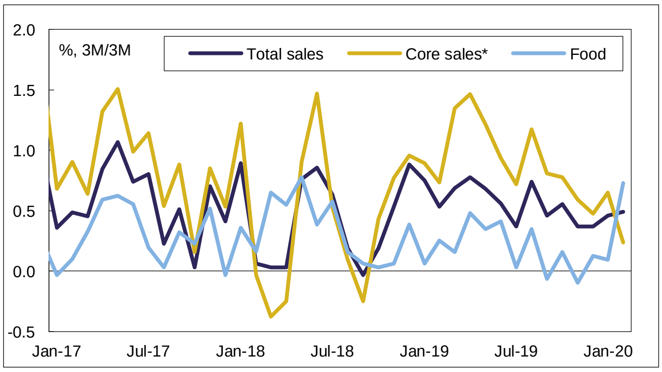
The week ahead in the euro area and US

Increased healthcare costs, support to household incomes and corporate liquidity, and marked declines in GDP, collectively mean that government debt as a share of GDP could rise in some member states by 20 percentage points or more this year. And while borrowing over the near term will in part be absorbed by the ECB's increased asset purchases under its PEPP programme, there are significant concerns over refinancing risks further ahead. Therefore, the main economic event in the euro area in the coming week will be the Eurogroup videoconference meeting on Tuesday evening. There the finance ministers will, for the second time in three weeks, try to agree specific recommendations on new common pandemic crisis support to facilitate funding of the exceptional fiscal measures being taken by member states on a sustainable basis.

Following the previous videoconference, the Eurogroup's chair Mario Centeno reported "broad support" among the finance ministers to make support available via the ESM Treaty, building on the framework of the existing Enhanced Conditions Credit Line (ECCL). The ESM currently has a lending capacity of just €410bn, and the proposal under discussion by the Eurogroup appeared to be based on making available about €240bn, with a limit of just 2% of GDP per member state. Ideally, funds amounting to far more than 2% of GDP would be made available, particularly to the most affected member states, Italy and Spain. And to be of benefit, the loans would need to have minimal conditionality attached, and be of long maturity. In addition, while proposals for issuance of new 'coronabonds' have been rejected in particular by Germany, the Netherlands and Austria, alternative suggestions for a further new one-off commonly-financed fund to provide support will also be considered. The European Commission has also proposed a separate €100bn SURE programme, with €25bn of guarantees from all EU member states, to help provide fund wage subsidies for furloughed workers. And the EIB has proposed its own €200bn credit support programme, similarly requiring €25bn of guarantees from member states.

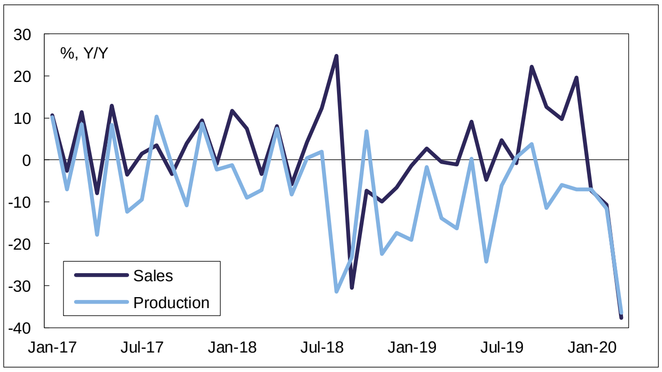
Data-wise, the coming week will bring the release of several reports on production and trade in February, whose relevance has been diminished by the marked intensification of the Covid-19 outbreak in March. So, the more up-to-date and high-frequency data will be more closely watched. Among these, the Sentix investor confidence survey of April, due Monday, will no doubt be characterised by extreme pessimism. The German construction PMI for March, due the same day, will also likely be downbeat. And weekly French labour market data, due on Wednesday will also likely grab headlines, particularly given the applications for temporary support by firms for 4 million workers under the national 'partial unemployment' scheme. That day will also bring the Bank of France's latest business sentiment survey for March. Among the February industrial sector data, German factory orders figures are due Monday ahead of the related IP report the following day. The Italian IP figures will come on Thursday ahead of the French release on Friday. In addition, French trade and Italian retail sales numbers are also due on Tuesday while Germany's February trade data will come on Thursday.

Euro area: Retail sales



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

Germany: New car registrations and production



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

In a quieter week for US economic data, Thursday's release of weekly initial jobless claims figures will no doubt attract most attention. The past week's numbers showed that the number more than doubled from the previous week to 6.65mn (roughly 4% of the labour force) and we would expect another large number. Thursday will also bring the University of Michigan's latest consumer confidence survey for April, which seems bound to fall significantly further in light of the escalation of the Covid-19 crisis in the country over recent weeks. That day will also bring PPI data for March, followed on Friday by CPI numbers for the same month. Given the sharp decline in the oil price, headline inflation is expected to have fallen 0.7ppt to 1.6%Y/Y, a thirteen-month low. In contrast, core inflation is anticipated to have moved sideways at 2.3%Y/Y. Earlier in the week, Wednesday will bring Fed minutes from the 15 March meeting where the FOMC announced a comprehensive support package, including the cutting of the Fed Funds Rate target by 100bps to 0.00-0.25% and pledge to boost its bond holdings by at least $700bn (a move that was superseded by its subsequent announcement on 23 March of potentially unlimited purchases of Treasury securities and agency MBS and a new facility to buy corporate bonds). Meanwhile, February data releases including consumer credit figures (Tuesday) and wholesale trade numbers (Thursday). In the markets, while the Fed will continue with its asset purchase programme, the Treasury will sell 3Y notes on Tuesday, 10Y notes on Wednesday and 30Y bonds on Thursday.

UK

Services PMI implies record decline

Today's final headline services PMI from the UK was unsurprisingly weaker than the initial release, with an additional 16% of firms responding after the initial partial shutdown of the hospitality/leisure sectors was brought into place on 20 March and official lockdown got underway on 23 March. In particular, the headline activity index fell an additional 1.2pts (7½pts in weighted terms) from the flash estimate to 34.5, a drop of 18.7pts from February and the lowest reading on record, well below the trough during the global financial crisis. And with the exception of technology services, which seemingly benefitted from increased demand for home-working services, the weakness was broad based. Moreover, firms were more downbeat about the near-term outlook, with the new orders PMI down a further 1.4pts to 33.7 and a number of firms indicating that new enquiries from overseas had "virtually ceased" in part reflecting the widespread travel restrictions still in place. As such, while several firms had placed staff on furlough, the employment PMI still implied the fastest pace of job cuts since mid-2009.

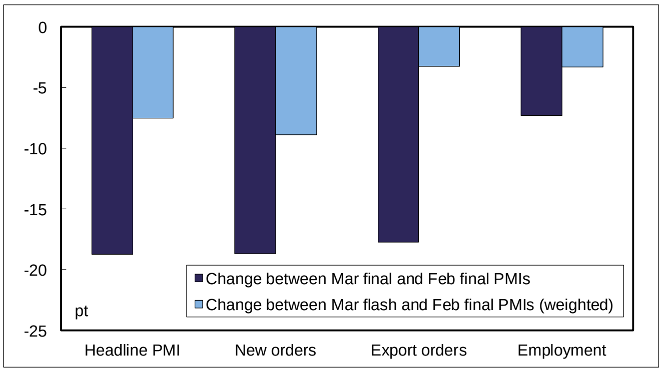
Composite PMI revised even lower

Overall, taken together with the weaker manufacturing PMI earlier in the week, the final composite PMI was revised lower by more than 1pt to a record-low 36.0. This marked a drop of 17pts from February and was more than 2pts lower than the trough seen during the global financial crisis. So, while the average composite PMI in Q1 was consistent with only modest contraction – a reading of 47.4 implied growth of -0.4%Q/Q – we expect to see a more significant decline last quarter, closer to 1½%Q/Q. And with the new orders component having been revised down from the preliminary release and expectations of future output at a series low, the near-term outlook looks increasingly gloomy. Indeed, conditions seem bound to have worsened significantly further in April as a substantial share of economic activity having effectively come to a standstill and the lockdown will inevitably be extended. Indeed, we currently expect a record retrenchment in GDP in Q2, with a double-digit percentage quarterly contraction.

The coming week in the UK

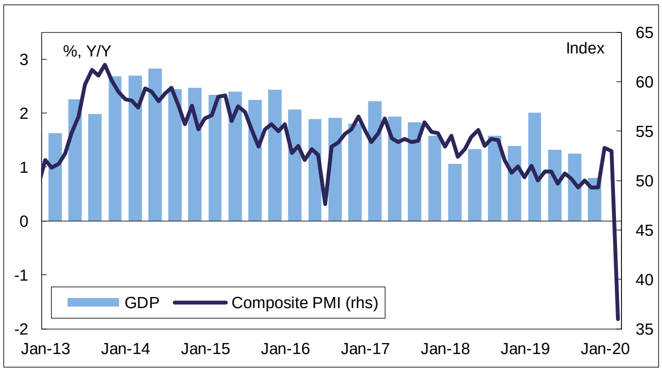
Like in the euro area, the news flow in the UK will continue to be dominated by Covid-19, with the coming week's dataflow set to provide more insight into the initial economic impact. This seems bound to be evident in the latest car registrations figures for March on Monday, which are likely to report a further significant drop in March. Admittedly, given that March is usually a strong month for new registrations, and tighter Covid-19-related restrictions came into place in the UK towards the end of the month, the contraction last month seems unlikely to be as severe as the outturns from France, Italy and Spain.

UK: Services PMI components



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

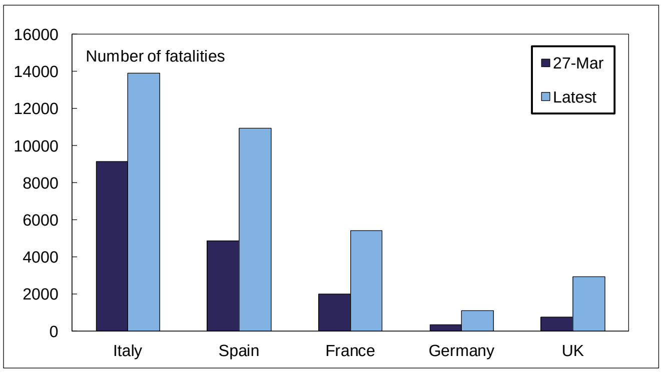
UK: GDP growth and composite PMI



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

Monday will also bring a special final GfK consumer confidence release to reflect the deterioration in conditions through the second half of the month. The construction PMI for March, also due that day, will also weaken. And Wednesday's release of the REC/KMPG Jobs Report for March will no doubt signal a very weak outlook for recruitment prospects over the near term. Likely of most interest, however, will be the ONS' latest weekly release of coronavirus-related survey indicators on Thursday, which should reflect more fully the initial impact of the official lockdown. Of less relevance that day will be the monthly GDP, activity and trade figures for February. Nevertheless, these are likely to show only very modest growth before the coronavirus crisis escalated in Europe, with GDP set to have risen just 0.1%M/M following no growth in January. Thursday will also bring the latest RICS house price balance for March. In the markets, the DMO will sell short- and long-dated Gilts on Tuesday, and 5Y and 10Y Gilts on Wednesday, with the BoE set to buy £13.5bn of Gilts in the secondary market over the course of the week before Friday's bank holiday.

Europe: Covid-19 fatalities by selected countries



Source: WHO and Daiwa Capital Markets Europe Ltd.

Europe: Daiwa economic forecasts*

	Q120	Q220	Q320	Q420	2020	2021
GDP forecasts %, Q/Q						
Euro area	-2.4	-13.1	7.8	3.8	-7.5	3.6
Germany	-1.8	-10.0	6.5	3.5	-5.4	3.8
France	-2.0	-10.5	7.0	3.5	-5.7	3.9
Italy	-3.5	-18.0	9.0	4.0	-12.3	2.3
Spain	-3.0	-19.5	11.0	6.0	-10.8	5.5
UK	-2.0	-12.0	9.0	4.0	-5.8	4.8
Inflation forecasts %, Y/Y						
Euro area						
Headline CPI	1.0	0.2	0.4	0.4	0.5	1.2
Core CPI	1.0	0.3	0.3	0.2	0.5	1.0
UK						
Headline CPI	1.6	0.6	0.5	0.6	0.8	0.9
Core CPI	1.5	0.9	0.8	0.7	1.0	0.8

**Illustrative forecasts assume that lockdowns are eased before the end of Q220.*
Source: Daiwa Capital Markets Europe Ltd.

European calendar

Today's results

Economic data

Country	Release	Period	Actual	Market consensus/ *Daiwa forecast*	Previous	Revised
EMU	Final services PMI (composite PMI)	Mar	**26.4 (29.7)**	28.4 (31.4)	52.6 (51.6)	-
	Retail sales M/M% (Y/Y%)	Feb	**0.9 (3.0)**	0.5 (2.0)	0.6 (1.7)	0.7 (2.2)
Germany	Final services PMI (composite PMI)	Mar	**31.7 (35.0)**	34.5 (37.2)	52.5 (50.7)	-
	New car registrations (production) Y/Y%	Mar	**-38.0 (-37.0)**	-	-11.0 (-12.0)	-
France	Final services PMI (composite PMI)	Mar	**27.4 (28.9)**	29.0 (30.2)	52.5 (52.0)	-
Italy	Services PMI (composite PMI)	Mar	**17.4 (20.2)**	22.5 (25.0)	52.1 (50.7)	-
Spain	Industrial production M/M% (Y/Y%)	Feb	**0.0 (-1.3)**	-	0.2 (-2.1)	0.0 (-2.2)
	Services PMI (composite PMI)	Mar	**23.0 (26.7)**	25.8 (30.8)	52.1 (51.8)	-
UK	Final services PMI (composite PMI)	Mar	**34.5 (36.0)**	35.7 (37.1)	53.2 (53.0)	-

Auctions

Country	Auction
- Nothing scheduled -	

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

Coming week's data calendar

The coming week's key data releases

Country		BST	Release	Period	Market consensus/ *Daiwa forecast*	Previous
			Monday 06 April 2020			
EMU		09.30	Sentix investor confidence	Apr	-30.3	-17.1
Germany		07.00	Factory orders M/M% (Y/Y%)	Feb	-2.0 (0.6)	5.5 (-1.4)
		08.30	Construction PMI	Mar	-	55.8
UK		00.01	Final GfK consumer confidence	Mar	-9	-7
		09.00	New car registrations Y/Y%	Mar	-	-2.9
		09.30	Construction PMI	Mar	44.5	52.6
			Tuesday 07 April 2020			
Germany		07.00	Industrial production M/M% (Y/Y%)	Feb	-0.8 (-3.2)	3.0 (-1.3)
France		07.45	Trade balance €bn	Feb	-	-5.9
Italy		09.00	Retail sales M/M% (Y/Y%)	Feb	-	0.0 (1.4)
UK		09.30	Unit labour costs (output per hour) Y/Y%	Q4	- (0.3)	3.6 (0.1)
			Wednesday 08 April 2020			
France		07.30	Bank of France industrial sentiment survey	Mar	90	96
			Thursday 09 April 2020			
Germany		07.00	Trade balance €bn	Feb	15.5	13.8
Italy		09.00	Industrial production M/M% (Y/Y%)	Feb	-1.6 (-2.3)	3.7 (-0.1)
UK		00.01	RICS house price balance %	Mar	11	29
		07.00	Monthly GDP M/M% (3M/3M%)	Feb	0.1 (0.2)	0.0 (0.0)
		07.00	Index of services M/M% (3M/3M%)	Feb	0.2 (0.3)	0.1 (0.0)
		07.00	Industrial production M/M% (Y/Y%)	Feb	0.2 (-3.0)	-0.1 (-2.9)
		07.00	Manufacturing production M/M% (Y/Y%)	Feb	0.1 (-4.1)	0.2 (-3.6)
		07.00	Construction output M/M% (Y/Y%)	Feb	0.3 (0.3)	-0.8 (1.6)
		07.00	Trade balance £bn	Feb	1.0	4.2
			Friday 10 April 2020			
France		07.45	Industrial production M/M% (Y/Y%)	Feb	-0.3 (-2.8)	1.2 (-2.2)
		07.45	Manufacturing production M/M% (Y/Y%)	Feb	-	1.2 (-2.2)

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

The coming week's key events & auctions

Country		BST	Event / Auction
			Monday 06 April 2020
			- Nothing scheduled -
			Tuesday 07 April 2020
Germany		10.30	Auction: €250mn of 0.5% 2030 index-linked bonds
		10.30	Auction:€250mn of 0.1% 2046 index-linked bonds
UK		10.00	Auction: £3.25bn of 0.125% 2023 bonds
		11.30	Auction: £1.25bn of 1.75% 2057 bonds
			Wednesday 08 April 2020
Germany		10.30	Auction: €4bn of 0% 2030 bonds
UK		00.01	REC/KPMG Report on UK Jobs
		10.30	Auction: £2.75bn of 2% 2025 bonds
		10.30	Auction: £2bn of 4.75% 2030 bonds
			Thursday 09 April 2020
Italy		10.00	Auction: 3Y and 10Y bonds
UK		-	ONS weekly release of coronavirus indicators
			Friday 10 April 2020
			- Nothing scheduled -

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

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