Euro wrap-up

Overview

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- As the Eurogroup's latest videoconference got underway, Bunds made gains and periphery bonds outperformed as Lagarde insisted the ECB would not allow any tightening of financial conditions and urged substantive fiscal support in all parts of the euro area.
- While February UK GDP data were weak, Gilts made significant gains as the BoE temporarily increased the UK Government's "overdraft" facility at the central bank, raising talk of monetary financing.
- The coming week will bring the final estimates of euro area inflation in March and IP in February.

Daily bond market movements

Bond	Yield	Change
BKO 0 03/22	-0.677	-0.024
OBL 0 04/25	-0.576	-0.036
DBR 0 02/30	-0.352	-0.040
UKT 0½ 07/22	0.043	-0.071
UKT 0⅝ 06/25	0.134	-0.066
UKT 4¾ 12/30	0.315	-0.068

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

Euro area

ECB accounts flags differences of opinion

The accounts of the ECB's monetary policy meetings of 11-12 March (when the Governing Council agreed new and more generous liquidity operations and extra QE) and 18 March (when it agreed its new €750bn PEPP asset purchase programme) made clear that the decisions were not made without some differences of opinion. In particular, while there was unanimous agreement on 18 March that extra action was needed, there was some dissent to the precise detail of the policy decision. A "large majority" on the Governing Council supported the PEPP, with "some reservations expressed". Indeed, some members would have preferred simply to augment the existing asset purchase programme or even consider outright monetary transactions (OMTs). A rate cut was also proposed as an alternative. And there were reservations expressed with respect to the crucial decision, and related communication, to consider revising the self-imposed issue and issuer limits. Nevertheless, on this occasion, the hawks were evidently in the minority. And the ECB's resulting purchases of BTPs have proved essential in maintaining Italian bond market access, and broader financial stability, over the subsequent weeks.

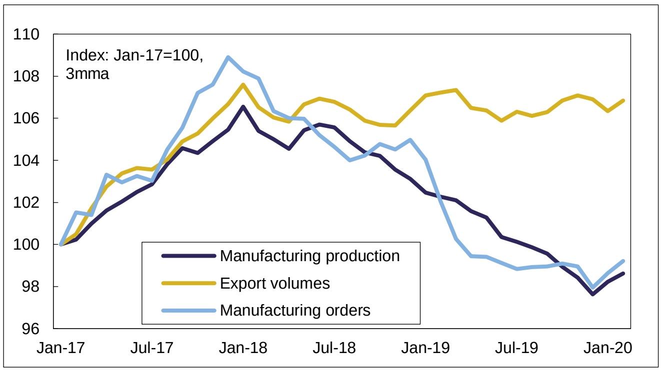
Lagarde calls for Eurogroup deal

Ahead of this evening's Eurogroup videoconference, when once again finance ministers are trying to agree new mechanisms to finance the increased deficits caused by Covid-19, ECB President Lagarde added her voice in support of a deal. In media interviews and articles published across the euro area, she insisted that the ECB "will not tolerate any procyclical tightening of financial conditions", and argued that it "is vital that the fiscal response to this crisis is undertaken with sufficient force in all parts of the euro area", noting that if one country falls short then all member states will be at risk. At the same time, she suggested that coronabonds are unnecessary. So, she implied support for the proposals backed by most member states – enhanced access to the ESM, and new support funds managed by the EIB and Commission. Nevertheless, the two holdouts in the debate – Italy, which continues to insist upon coronabonds and condition-free access to the ESM, and the Netherlands, which wants no consideration of new innovative financial instruments and relatively strict ESM conditionality – appeared yesterday to double down on their respective positions. And with the ECB continuing to support BTPs and also offering a form of back-door debt mutualisation via its asset purchases, there might still be little incentive for either side to make significant concessions. So, another Eurogroup failure today would hardly be a surprise. And leaders might ultimately be called to reach the necessary compromise.

German trade data suggest little disruption in February

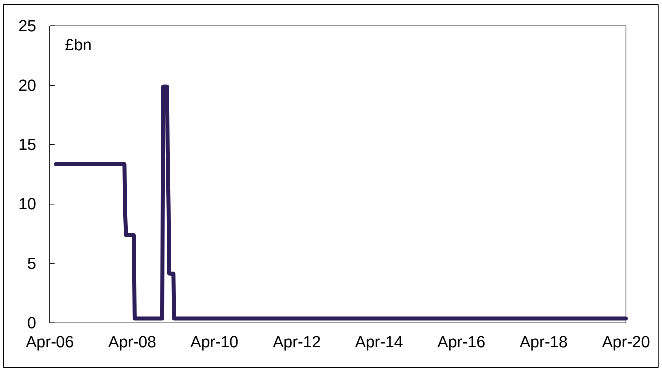
Turning to economic data, the German trade figures for February released today tallied with the respective IP and orders

Germany: Exports, manufacturing output and orders



Source: Thomson Reuters and Daiwa Capital Markets Europe Ltd.

UK: BoE Ways and Means account



Source: BoE and Daiwa Capital Markets Europe Ltd.

data out earlier this week in suggesting little adverse impact of Covid-19 on growth that month. Indeed, exports rose 1.3%M/M in both value and volume terms, the most in five months. With import values falling 1.6%M/M (down 0.6%M/M in volume terms), the trade surplus jumped €7bn to €20.8bn, a four-month high more than €2bn above last year's average. And, looking at all of the data released so far for January and February (including sales, production, construction and trade), it appears that – before Covid-19 sent economic activity into sharp reverse last month – the German economy had been on track for its strongest quarter of economic growth in more than two years. Alas, the opposite is now the case. Indeed, Germany's Federal Employment Agency today announced that the number companies to register for the government's short-time work subsidies had risen 40% over the past week to about 650k, suggesting that several millions of workers are likely to participate.

The coming week in the euro area and US

The coming week should be relatively quiet for euro area economic releases. The flow kicks off on Wednesday with final March CPI figures from France, Italy and Spain, all of which are expected to confirm that headline inflation fell sharply last month on the back of the large drop in energy prices. Equivalent German figures will follow on Thursday, which are also expected to align with the flash estimate that showed headline inflation falling to a lesser extent than other member states in March due a slower pass-through from oil prices. Overall, final euro area inflation data, due on Friday, are expected to confirm the flash release that showed the headline measure declining 0.5ppt to 0.7%Y/Y in March, matching the three-year low reached in October. Flash core inflation eased just 0.2ppt to 1.0%Y/Y. Of somewhat more interest on Friday will be euro area new car registration figures for March, which are likely to report a record year-on-year decline for the region as a whole, not least given the sizeable double-digit declines reported in Germany (38%Y/Y), France (72%Y/Y), Italy (85%Y/Y) and Spain (69%Y/Y). Meanwhile, February releases include euro area industrial production data (Thursday), which are expected to another solid reading before a marked contraction in light of the Covid-19 disruption, while construction output figures (Friday) are likely to have declined following solid growth in January. In the markets, Germany will sell 24Y Bunds on Wednesday, while France and Spain will sell bonds with various maturities on Thursday.

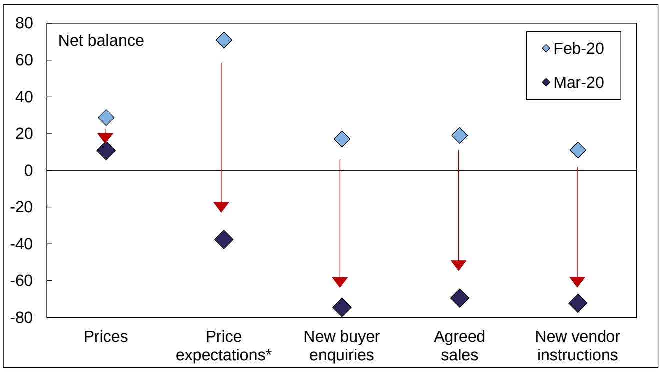
In the US, after tomorrow's release of March CPI figures, which are expected to show headline inflation declining 0.7ppt to 1.6%Y/Y, a thirteen-month low on the back of lower oil prices, it will be a busy week ahead for economic releases. Certainly, retail sales and industrial production data for March (due Wednesday) will be closely watched for the initial impact of Covid-19 on activity. Expectations are for retail sales to have declined at the steepest monthly pace on record, while manufacturing production is forecast to have contracted at a rate close to the trough during the global financial crisis. Wednesday will also bring the Fed's latest Beige Book and Empire Manufacturing survey, followed by the Philly Fed index (Thursday) which will provide an update on business conditions in April. Thursday will also bring another alarming weekly release of jobless claims figures, as well housing starts numbers for March. In the markets, there are no UST bond auctions scheduled in the coming week, but the Fed will continue with its asset purchases.

UK

Direct (but temporary) monetary financing at the BoE

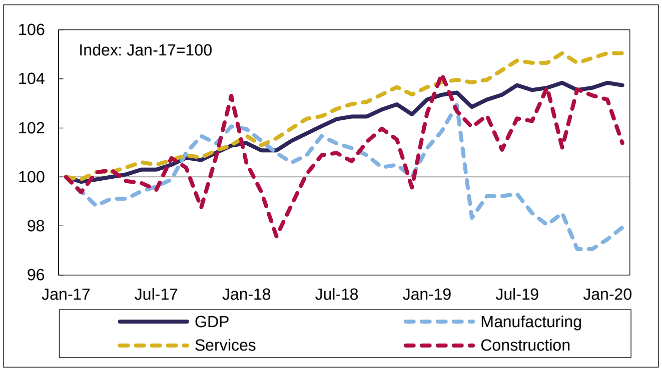
The BoE today announced that it will provide additional liquidity to the UK government via a temporary increase in the use of its Ways and Means (W&M) account, HM Treasury's overdraft facility at the central bank. The move might be considered a form of direct monetary financing of the government by the BoE. And it came as a surprise, since Governor Andrew Bailey had recently appeared keen to downplay the relevance of the W&M account to the current situation. However, it is not unprecedented, as the BoE acted in the same way during the global financial crisis. The size of the direct financing will be far smaller than the BoE's additional secondary market gilt purchases, which will reach about £190bn. And, importantly, the move is planned to be temporary, with the BoE stating that the drawings "will be repaid as soon as possible before the end of the year". Of course, it remains to be seen whether that deadline will be extended in due course, or even eventually become

UK: RICS housing market indicators



**12-months ahead. Source: Thomson Reuters and Daiwa Capital Markets Europe Ltd.*

UK: Monthly GDP and sector components



Source: Thomson Reuters and Daiwa Capital Markets Europe Ltd.

permanent. But, for the time being at least, it is highly unlikely to have a material impact on near-term inflation, or indeed medium-term inflation expectations.

W&M increase justified on cash management grounds

Rather than monetary policy, the case for the increase in the W&M can currently be justified wholly on government cash management grounds. Indeed, the stated purpose of the W&M account is to absorb small day-to-day fluctuations in the government's cashflow, with a weekly limit set at just £370mn since April 2009. During the global financial crisis, however, the facility was increased close to £20bn, and a larger amount than that might be required this time around. Indeed, while the DMO already plans a record amount of gilt sales (£156.1bn) this fiscal year, we expect the remit to be revised up in due course as the full magnitude of the impact of the Covid-19 crisis on the government's deficit becomes clear. In the past three weeks, the government has already received more than one million new applications for its Universal Credit welfare benefits. And demand for the government's Job Retention Scheme wage subsidies could in due course rise to as many as 10mn workers. Most importantly in the context of today's decision, however, the near-term fluctuations in public spending and tax receipts are likely to be far larger than normal and highly unpredictable. So, short-term volatility in overall government cash-flow will also be far greater than in the recent past.

Housing market grinding to a halt

In terms of economic data, today's RICS housing survey for March offered an unsurprisingly downbeat assessment of the initial shock to the residential property market from Covid-19. Among the variables least immediately affected were prices, with the house price balance over the past three months down 18pts to 11%, merely the lowest reading since December. But the detail of report was inevitably much weaker, suggesting that the market was grinding to a halt. For example, newly agreed sales reportedly slumped in March, as did new vendor instructions and buyer enquiries, with the respective indices plunging to their lowest since the series began in the late-1990s. Of course, it was already clear that, with the lockdown in place, the market would effectively have to freeze. But surveyors' expectations for house prices over the coming three months substantially declined – indeed, the balance fell more than 100pts to -82, the weakest since the height of the global financial crisis – and almost 40% of survey respondents anticipate a further fall over the coming twelve months too.

GDP contracted in February despite record underlying trade surplus

Meanwhile, today's monthly GDP figures for February showed that, even before greater Covid-19-related restrictions came into place, UK economic activity was extremely subdued. In particular, GDP contracted 0.1%M/M in February, due principally to a third successive monthly drop in construction output (-1.7%M/M). But services stagnated that month too, with positive contributions from computer programming offset by falls in wholesale and warehousing. So, it was only thanks to modest growth in manufacturing (0.5%M/M), that the outturn wasn't weaker. The weakness of demand was also reflected in a notable fall in imports, which resulted in the first ever underlying trade surplus since comparable records began. Admittedly, GDP was revised marginally higher in January (up 0.1ppt to 0.1%M/M). But this still suggested only very modest growth in the first two months of Q1 compared with the Q4 average, implying little cushioning for the anticipated extreme slump in output bound to have taken place across all three sectors in March. Expect GDP to have declined about 5%Q/Q over the first quarter as a whole, before a record-double-digit percentage contraction in Q2.

The coming week in the UK

A holiday-shortened week ahead will bring only a few UK economic releases, with perhaps most notable the BRC's retail sales monitor for March on Thursday. While grocery sales are likely to have been well supported due to the Covid-19-related panic buying, spending on non-essential items seems bound to have fallen considerably over the past month. As such, we will likely see the largest year-on-year drop since the series began in 1995. Thursday will also bring the ONS' weekly coronavirus indicator release, which will include an update of its bi-weekly business impact of Covid-19 survey. This will be the first to fully reflect the post-UK lockdown period and therefore is bound to report a significant deterioration in firms' assessment of how the current crisis is impacting turnover, jobs and financial resources. The BoE's latest quarterly consumer credit survey is also due on Thursday and is likely to show that banks expect a marked weakening in demand for mortgage lending and consumer credit over the coming quarter. In the markets, the DMO will sell 2029 and 2037 Gilts.

Due to Public Holidays and a light economic data calendar, the next edition of the Euro wrap-up will be published on 16th April 2020

European calendar

Today's results

Economic data

Country		Release	Period	**Actual**	Market consensus/ *Daiwa forecast*	Previous	Revised
Germany		Trade balance €bn	Feb	**20.8**	16.5	13.9	13.8
Italy		Industrial production M/M% (Y/Y%)	Feb	**-1.2 (-2.4)**	-1.7 (-2.3)	3.7 (-0.1)	3.6 (-0.2)
UK		RICS house price balance %	Mar	**11**	10	29	-
		Monthly GDP M/M% (3M/3M%)	Feb	**-0.1 (0.1)**	0.1 (0.1)	0.0 (0.0)	0.1 (-)
		Index of services M/M% (3M/3M%)	Feb	**0.0 (0.2)**	0.2 (0.3)	0.1 (0.0)	-
		Industrial production M/M% (Y/Y%)	Feb	**0.1 (-2.8)**	0.2 (-3.0)	-0.1 (-2.9)	0.2 (-2.8)
		Manufacturing production M/M% (Y/Y%)	Feb	**0.5 (-3.9)**	0.1 (-4.0)	0.2 (-3.6)	0.4 (-3.7)
		Construction output M/M% (Y/Y%)	Feb	**-1.7 (-2.7)**	0.3 (0.2)	-0.8 (1.6)	-0.2 (0.5)
		Trade balance £bn	Feb	**-2.8**	1.0	4.2	2.4

Auctions

Country		Auction
Italy		sold €4.5bn of 0.6% 2023 bonds at an average yield of 0.86%
		sold €3bn of 0.85% 2027 bonds at an average yield of 1.37%
		sold €1.25bn of 1.45% 2036 bonds at an average yield of 2.06%
		sold €750mn of 4.75% 2044 bonds at an average yield of 2.49%

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

Tomorrow's releases

Country		BST	Release	Period	Market consensus/ *Daiwa forecast*	Previous
France		07.45	Industrial production M/M% (Y/Y%)	Feb	0.0 (-2.5)	1.2 (-2.8)
		07.45	Manufacturing production M/M% (Y/Y%)	Feb	0.4 (-2.0)	1.2 (-2.2)

Key events and auctions

Country		BST	Auction/Event
EMU		-	Public holiday – Good Friday
UK		-	Public holiday – Good Friday

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 13 April 2020			
			- Nothing scheduled -			
			Tuesday 14 April 2020			
			- Nothing scheduled -			
			Wednesday 15 April 2020			
France		07.45	Final CPI (EU-harominised CPI) Y/Y%	Mar	0.6 (0.7)	1.4 (1.6)
Italy		09.00	Final CPI (EU-harmonised CPI) Y/Y%	Mar	0.2 (0.1)	0.2 (0.2)
Spain		07.45	Final CPI (EU-harmonised CPI) Y/Y%	Mar	0.1 (0.2)	0.7 (0.9)
			Thursday 16 April 2020			
EMU		10.00	Industrial production M/M% (Y/Y%)	Feb	0.5 (-2.0)	2.3 (-1.9)
Germany		07.00	Final CPI (EU-harmonised CPI) Y/Y%	Mar	1.4 (1.3)	1.7 (1.7)
UK		00.01	BRC retail sales monitor, like-for-like sales Y/Y%	Mar	-	-0.4
			Friday 17 April 2020			
EMU		07.00	EU27 New car registrations	Mar	-	-7.4
		10.00	Final headline CPI (core CPI) Y/Y%	Mar	0.7 (1.0)	1.2 (1.2)
		10.00	Construction output M/M% (Y/Y%)	Feb	-	3.6 (6.0)
Italy		09.00	Trade balance €bn	Feb	-	0.5

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

The coming week's key events & auctions

Country		BST	Event / Auction
			Monday 13 April 2020
EMU		-	Public holiday – Easter Monday
UK		-	Public holiday – Easter Monday
			Tuesday 14 April 2020
			- Nothing scheduled -
			Wednesday 15 April 2020
Germany		10.30	Auction:€1bn of 2.5% 2044 bonds
UK		10.00	Auction: £3bn of 0.875% 2029 bonds
		11.30	Auction: £2bn of 1.75% 2037 bonds
			Thursday 16 April 2020
France		09.50	Auction: Fixed-rate and index-linked bonds
Spain		09.45	Auction: 0% 2023 bonds
		09.45	Auction: 0% 2025 bonds
		09.45	Auction: 1.3% 2026 bonds
		09.45	Auction: 1.85% 2035 bonds
UK		09.30	BoE quarterly credit conditions survey
		10.00	Auction: 1.5% 2026 bonds
		11.30	Auction: 1.75% 2049 bonds
			Friday 17 April 2020
UK		-	UK sovereign credit rating update from Moody's

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

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