

Euro wrap-up

Overview

- As EU leaders discussed plans for a Recovery Fund, Bunds made gains as the flash euro area PMIs slumped to extreme record lows. Periphery bonds rallied after the ECB's announcement late yesterday of a further relaxation of its collateral rules.
- While the DMO announced a huge £180bn of new issuance between May and July, Gilts made gains as the UK PMIs plunged to new record lows.
- Friday will bring the April German ifo business survey and March UK retail sales data.

Chris Scicluna
+44 20 7597 8326

Emily Nicol
+44 20 7597 8331

Daily bond market movements

Bond	Yield	Change
BKO 0 03/22	-0.705	-0.018
OBL 0 04/25	-0.630	-0.015
DBR 0 02/30	-0.433	-0.020
UKT 0½ 07/22	0.062	-0.019
UKT 0% 06/25	0.164	-0.025
UKT 4% 12/30	0.292	-0.035

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

Euro area

Euro area PMIs slump to extreme lows

With lockdown measures having remained in place across much of the region in April, today's flash euro area PMIs for this month unsurprisingly signalled economic contraction of record magnitude for the post-War period. The headline services PMI certainly fell off a cliff, declining a spectacular 14.7pts on the month to a new series low of just 11.7, as firms in hospitality, tourism, and retail were forced to close. But the manufacturing survey also implied a record contraction in the sector, with the output PMI down a whopping 20.1pts to 18.4. And so the composite PMI also slumped to an extreme low of 13.5, almost 25pts below the trough during the global financial crisis. Firms expressed much greater pessimism about the outlook for output over the coming twelve months too. Against this backdrop, even excluding those workers that had been furloughed, today's survey suggested that firms cut jobs at one of the fastest rates in the survey's near-twenty-year history.

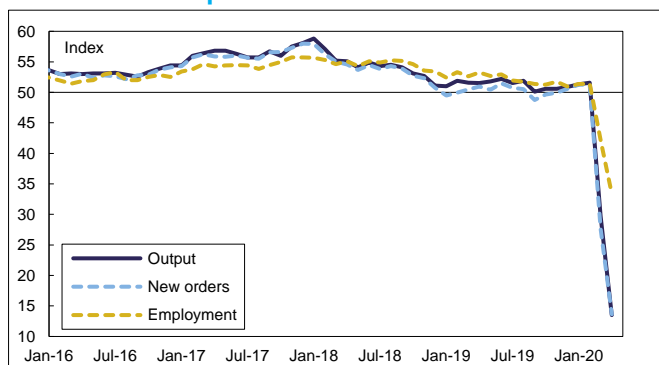
German and French activity collapses

At the country level, the flash German and French indices were unprecedentedly weak, with the composite PMIs at new record lows (17.1 and 11.2 respectively), while Markit indicated that the composite PMI for the rest of the region fell to 11.5. Within the detail, the French services PMI was striking, down a further 17pts from March to just 10.4, a record low for all countries. But the manufacturing output indices for both countries were also down more than 20pts (to 19.4 in Germany and 15.0 in France), with similar declines in the new orders components too. And this tallied with the findings of today's INSEE business survey, which among other things suggested that the industrial capacity utilisation rate has dropped more than 15ppts over the past three months to a record low of 67%. INSEE noted that much manufacturing activity had been temporarily shut down because of the lockdown, but that the agri-food sector had got off most lightly, with capacity utilisation at a somewhat more respectable 75%. Given the large amount of slack, a larger share of manufacturers than in January suggested that production capacity would be sufficient to fulfill order books over coming months, underscoring that the current hit to demand is much greater than the negative shock to potential supply.

GDP to contract sharply in Q2 despite easing lockdowns

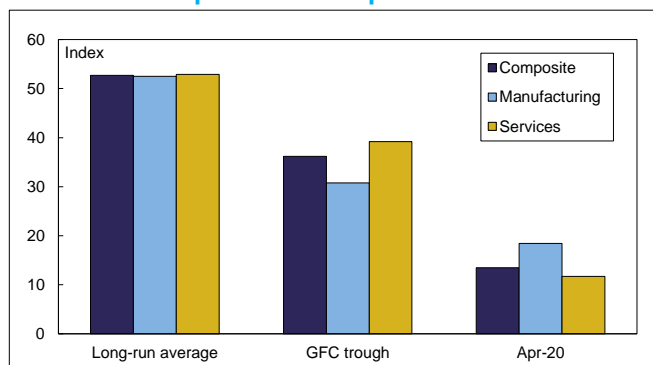
Today's surveys undoubtedly point to a contraction of immense magnitude at the start of Q2. But this was inevitable given that lockdown measures compelled a temporary stop to activity in several sectors. More uncertain is whether the PMIs and other sentiment surveys will signal an improvement in May as countries move to ease restrictions very gradually. Initial findings might suggest it will, with Germany's decision to allow smaller retailers to re-open under strict social distancing conditions at the start of this week having coincided with a significant rise in traffic flow in inner cities. While Italy has extended its lockdown through to early May, it too has allowed some non-essential business to re-open (book

Euro area: Composite PMIs*



*April 2020 figures are flash estimates. Source: Markit, Thomson Reuters and Daiwa Capital Markets Europe Ltd.

Euro area: Output PMIs comparison*



*April 2020 figures are flash estimates. Source: Markit, Thomson Reuters and Daiwa Capital Markets Europe Ltd.



Follow us on twitter [@DaiwaEurope](https://twitter.com/DaiwaEurope)

shops, child clothing stores). Spain has permitted employees from certain sectors unable to work from home to return. And we would expect France in due course to agree to some modest relaxation of restrictions in May. This notwithstanding, GDP will contract sharply over the second quarter as a whole. We currently expect to see significant double-digit quarterly declines in GDP in Q2, by 15%Q/Q or more, in each of the large for member states.

German household confidence collapses

Like business confidence, household sentiment has also taken a big hit. This was illustrated by the results of Germany's GfK consumer confidence survey conducted in the first two weeks of April. While German consumers' overall expectations of the economic outlook deteriorated only slightly further from March's record low, GfK reported a record monthly decline in income expectations and propensity to buy. As a result, its headline index (presented as a forecast for the coming month) fell by a record 25.7pts to -23.4, almost 25pts below the low during the global financial crisis.

German government prepares extra stimulus

Against that gloomy backdrop, the overnight decision by the ruling coalition parties to augment by €10bn its already-huge fiscal support package was welcome. In particular, Germany's government aims to increase the levels and duration of benefits paid to furloughed workers. Workers whose hours have been cut by half or more currently receive between 60 and 67% of net income, that amount will rise to up to 77% after the fourth month of receiving benefits and up to 87% after seven months on the Kurzarbeit scheme. In addition, the coalition intends to provide extra support through the tax system for ailing sectors and SMEs, including a temporary 12ppt VAT cut for restaurants to last for twelve months from 1 July 2020. If the EU leaders agree a substantive Recovery Fund to facilitate government debt refinancing over the coming few years, then other member states such as Italy and Spain would have greater scope to increase near-term fiscal support too.

The day ahead in the euro area and US

Tomorrow, euro area financial markets will respond to the outcome of today's EU leaders' videoconference, which was likely to agree certain principles regarding the proposed Recovery Fund to be implemented from the start of 2021. A large-scale fund of grants to the hardest hit member states, funded by long-term borrowing by the European Commission, would seem most appropriate to support economic activity in the aftermath of the covid-19 crisis without raising refinancing risks. Data-wise, tomorrow will bring yet another sentiment survey from the euro area, with the German ifo likely to echo the downbeat assessment from today's flash PMIs. In particular, the headline business climate index is forecast to fall to a new series low, below the previous trough reached during the global financial crisis. This will principally reflect a plunge in the current assessment balance across the manufacturing, services and construction sectors alike. But the expectations balance might well be supported by the government's fiscal support package and moves to relax lockdown restrictions very gradually. However, this index is unlikely to mirror the rebound seen in the ZEW survey earlier this week.

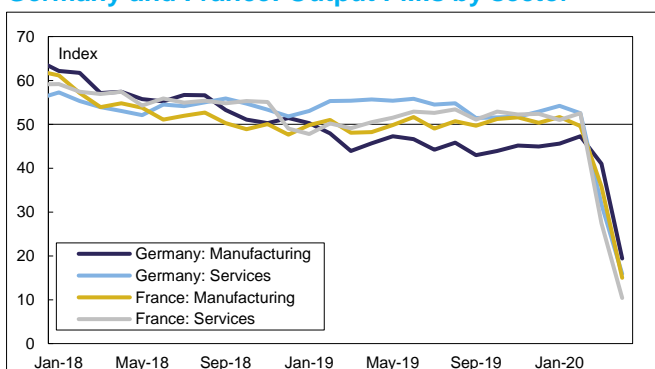
In the US, tomorrow will bring durable goods orders data for March which are expected to report a marked double-digit decline on the month as closures of businesses and heightened economic uncertainty hit demand. The revised University of Michigan's consumer sentiment survey for April might also reveal a downwards revisions from the more-than nine-year low registered in the preliminary release.

UK

Deepest contraction for several centuries?

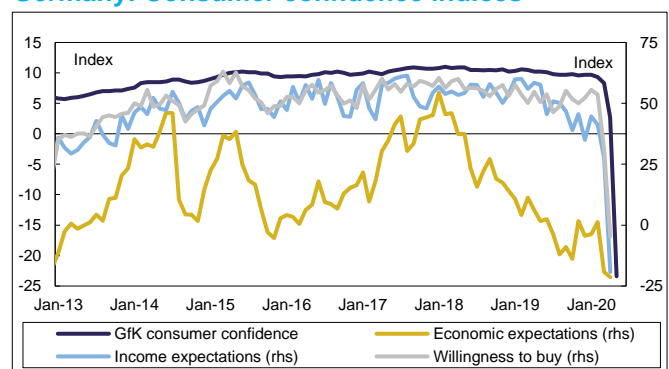
The UK's lockdown measures are inevitably taking their toll on economic activity. Indeed, in a webinar, BoE MPC member Gertjan Vlieghe suggested that the current economic contraction "is faster and deeper than anything we have seen in the past century, or possibly several centuries". That was reflected in the flash April PMIs, for which the composite index plunged

Germany and France: Output PMIs by sector*



*April 2020 figures are flash estimates. Source: Markit, Thomson Reuters and Daiwa Capital Markets Europe Ltd.

Germany: Consumer confidence indices*



*Headline figure for May is survey forecast. Source: GfK, Thomson Reuters and Daiwa Capital Markets Europe Ltd.

more than 23pts – far exceeding the pace of decline during the global financial crisis – to just 12.9, by some margin the lowest on the series dating back two decades. As elsewhere in Europe, services registered the weakest results, with the activity index falling 22pts to 12.3. But the drop of more than 27pts in the manufacturing output PMI to 16.6, also unsurprisingly a record low, was more marked. Markit reported that the small minority of manufacturers reporting output growth were mostly involved in production of medical items, food and drink. And manufacturers of clothing, textiles and cars were hardest hit. Among services, growth was registered by some online retailers and in the public sector, while many hospitality and other consumer-facing firms confirmed a total stop to activity. Among other detail, the PMIs also signalled declines in new orders and employment across the sectors.

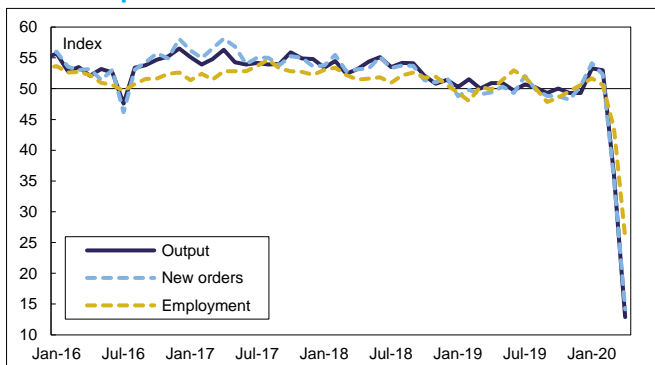
Widespread furloughing of staff

Indeed, Markit reported that around half of all respondents to the PMI survey had cut staffing levels, including by furloughing. The ONS provided additional colour today on the shock to the labour market with the results of its Business Impact of Coronavirus Survey (BICS) for 23 March to 5 April 2020. This reported that 27% of all staff had been furloughed from responding firms that were still trading or had temporarily halted activity over the relevant period. This would suggest that the number of workers to be paid up to 80% of wages under the government's Job Retention Scheme could rise significantly further above the 2.2mn registered by close on Tuesday. But, perhaps more encouragingly, less than 1% of the workforce of firms still trading or temporarily closed had been made redundant. For staff in firms that were continuing to trade, the highest incidences of furloughing were in the hospitality (40%) and construction (32%).

The day ahead in the UK

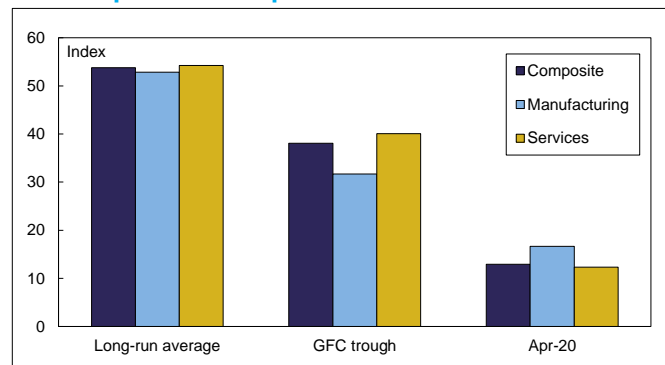
The end of week will bring the official retail sales figures for March, which, in line with recent surveys, are expected to show a marked decline in underlying spending at the end of Q1. Indeed, despite panic buying of food and certain other essential items, total retail sales are forecast to have declined 5%M/M, the most since the series began in the mid-1990s. And tomorrow's GfK consumer confidence survey seems bound to show a further marked deterioration in household sentiment in April, suggesting a sharp weakening in consumption at the start of Q2.

UK: Composite PMI*



*April 2020 figures are flash estimates. Source: Markit, Thomson Reuters and Daiwa Capital Markets Europe Ltd.

UK: Output PMI comparison*
















*April 2020 figures are flash estimates. Source: Markit, Thomson Reuters 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)	Apr	33.6 (11.7)	38.0 (22.8)	44.5 (26.4)	-
	 Preliminary composite PMI	Apr	13.5	25.0	29.7	-
Germany	 GfK consumer confidence	May	-23.4	-1.8	2.7	2.3
	 Preliminary manufacturing PMI (services PMI)	Apr	34.4 (15.9)	39.0 (28.0)	45.4	-
	 Preliminary composite PMI	Apr	17.1	28.5	35.0	-
France	 Business confidence indicator	Apr	62	80	95	94
	 Manufacturing confidence (production outlook)	Apr	82 (-78)	83 (-45)	98 (-33)	-
	 Preliminary manufacturing PMI (services PMI)	Apr	31.5 (10.4)	37.0 (24.5)	43.2 (27.4)	-
	 Preliminary composite PMI	Apr	11.2	24.5	28.9	-
UK	 Public sector net borrowing £bn	Mar	2.3	1.8	-0.4	0.1
	 Preliminary manufacturing PMI (services PMI)	Apr	32.9 (12.3)	42.0 (27.8)	47.8 (34.5)	-
	 Preliminary composite PMI	Apr	12.9	29.5	36.0	-
	 CBI industrial trends, total orders (business optimism)	Apr	-56 (-87)	-51 (-58)	-29 (23)	-

Auctions




Country	Auction
- Nothing to report -	

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

Tomorrow's releases

Country	BST	Release	Period	Market consensus/ <i>Daiwa forecast</i>	Previous
Germany	 09.00	Ifo business climate	Apr	79.7	86.1
	 09.00	Ifo current assessment balance (expectations)	Apr	80.5 (75.0)	93.0 (79.7)
UK	 00.01	Preliminary GfK consumer confidence	Apr	-40	-34
	 07.00	Retail sales including fuel M/M% (Y/Y%)	Mar	-5.0 (-5.0)	-0.3 (0.0)
	 07.00	Retail sales excluding fuel M/M% (Y/Y%)	Mar	-4.0 (-4.8)	-0.5 (0.5)

Key events and auctions

Country	BST	Auction/Event
Italy	 10.00	Auction: up to €1bn of 0.4% 2030 index-linked bonds
	 10.00	Auction: up to €2.75bn of 0% 2021 bonds
	-	Sovereign debt credit rating update by S&P
UK	 -	Sovereign debt credit rating update by S&P

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

Access our research blog at:

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

This research report is produced by Daiwa Securities Co. Ltd., and/or its affiliates and is distributed by Daiwa Capital Markets Europe Limited in the European Union, Iceland, Liechtenstein, Norway and Switzerland. Daiwa Capital Markets Europe Limited is authorised and regulated by The Financial Conduct Authority and is a member of the London Stock Exchange and Eurex Exchange. Daiwa Capital Markets Europe Limited and its affiliates may, from time to time, to the extent permitted by law, participate or invest in other financing transactions with the issuers of the securities referred to herein (the "Securities"), perform services for or solicit business from such issuers, and/or have a position or effect transactions in the Securities or options thereof and/or may have acted as an underwriter during the past twelve months for the issuer of such securities. In addition, employees of Daiwa Capital Markets Europe Limited and its affiliates may have positions and effect transactions in such securities or options and may serve as Directors of such issuers. Daiwa Capital Markets Europe Limited may, to the extent permitted by applicable UK law and other applicable law or regulation, effect transactions in the Securities before this material is published to recipients.

This publication is intended for investors who are not Retail Clients in the United Kingdom within the meaning of the Rules of the FCA and should not therefore be distributed to such Retail Clients in the United Kingdom. Should you enter into investment business with Daiwa Capital Markets Europe's affiliates outside the United Kingdom, we are obliged to advise that the protection afforded by the United Kingdom regulatory system may not apply; in particular, the benefits of the Financial Services Compensation Scheme may not be available.

Daiwa Capital Markets Europe Limited has in place organisational arrangements for the prevention and avoidance of conflicts of interest. Our conflict management policy is available at <http://www.uk.daiwacm.com/about-us/corporate-governance-regulatory>. Regulatory disclosures of investment banking relationships are available at <https://daiwa3.bluematrix.com/sellside/Disclosures.action>.