Euro wrap-up

Overview

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- While France announced plans for a gradual exit from lockdown measures, euro area government bonds made gains as an ECB survey suggested a massive increase in loan demand from liquidity-strained firms.
- Gilts were little changed despite a very gloomy UK retail survey, which highlighted firms' cash-flow difficulties as well as a sharp drop in sales.
- Wednesday will bring the Commission's latest economic sentiment survey as well as flash German inflation data for April and euro area bank lending data for March.

Daily bond market movements

Bond	Yield	Change
BKO 0 03/22	-0.712	-0.013
OBL 0 04/25	-0.656	-0.016
DBR 0 02/30	-0.469	-0.010
UKT 0½ 07/22	0.061	-0.006
UKT 0⅝ 06/25	0.163	-0.007
UKT 4¾ 12/30	0.295	-0.006

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

Euro area

A record surge in demand for business loans

The ECB's latest bank lending survey (BLS), conducted between 19 March and 3 April, reported a sharp leap in business loan demand last quarter as firms sought to maintain liquidity and payments throughout the disruption caused by Covid-19. Loan demand was higher for larger firms than for SMEs, and significantly higher for short-term loans than long-term loans. Among the member states, it was particularly pronounced among firms in Germany and France, but broadly unchanged in Italy and down in Spain. Overall, banks predicted an additional surge in demand for business loans in Q2, by the most on the survey which dates back to 2003, as firms' emergency liquidity needs remained high. At the same time, demand for consumer loans fell back. And demand for housing loans was expected to drop this quarter by the most since the global financial crisis.

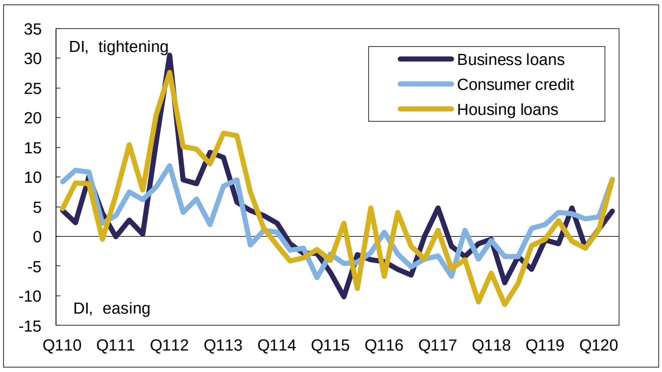
Loan standards have tightened, but not aggressively

In terms of credit supply, banks acknowledged the deterioration in the economic outlook and market financing conditions, as well as adverse impacts on their balance sheets, as factors contributing to a tightening of loan standards in Q1. But with bank capital and liquidity positions still relatively solid, and monetary and regulatory policy having become highly supportive, the BLS also suggested that the overall impact of the pandemic on credit standards so far had been relatively measured and far lower than during the global financial crisis and subsequent euro crisis. It also suggested that credit standards for loans to households tightened somewhat more significantly than those on business loans, whether for SMEs or larger firms. Moreover, banks expect a net easing of credit standards on loans to firms in the current quarter, as the ECB's liquidity support and government credit guarantees kick in more forcefully. Banks displayed a range of views in this respect, however. And overall, they rightly cautioned that they were unable yet to fully evaluate the effects of the Covid-19 crisis.

Survey makes case for even more generous TLTRO-III

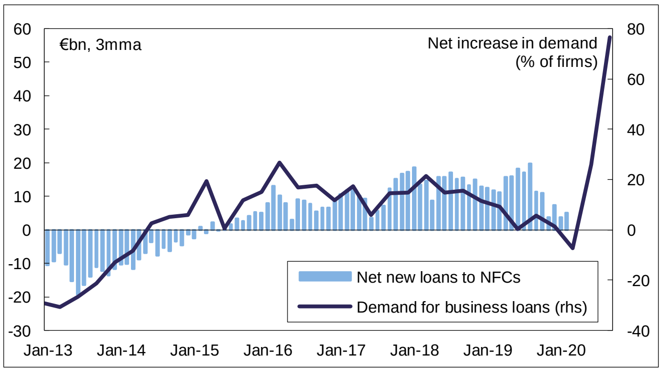
In terms of the impact of recent monetary policy initiatives, banks reported a positive impact on their liquidity and market financing conditions, as well as their lending volumes, from the ECB's new €750bn PEPP programme. The impact on their profitability of the asset purchases was also expected to become more positive over the coming six months. Banks also judged that the PEPP, negative deposit rate and tiering arrangements, and TLTRO-III operations, were all supportive of bank lending. Given perceptions of increased liquidity risks, the survey reported a significant increase in the share of banks planning to participate in future TLTROs for precautionary purposes. As well as refinancing TLTRO-II borrowing, banks also indicated that they would use, to a large extent, the TLTRO-III liquidity for granting loans. And so, the BLS results suggested

ECB Bank Lending Survey: Credit standards



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

ECB Bank Lending Survey: Loan demand*



**Survey measure of loan demand has 3-month lead. Q220 figure is survey forecast measure. Source: ECB, Thomson Reuters & Daiwa Capital Markets Ltd.*

that, if the ECB was keen support the flow of cheap loans to non-financial firms, this week the Governing Council would be wise to consider an immediate further reduction in the interest rate on the TLTRO-III loans, from the current minimum of -0.75% to -1.00%. And while there is no urgency to do so right now as Italian spreads have narrowed significantly from their peak last week and the ECB has scope to continue buying assets at the recent pace for another six months, an augmentation of the PEPP purchase programme at the June meeting, say to €1trn by year end, would also seem necessary.

France joins countries edging to exit lockdown

Given the strains imposed by government lockdowns over the past couple of months, non-financial firms in the euro area will take a modicum of comfort from the announcements of plans by member states to ease lockdown measures. Following last week's reopening of smaller German shops, at the start of the week Italy's PM announced plans to allow firms in manufacturing, construction and wholesale to restart activity from 4 May, further shops to reopen on 18 May, and hairdressers to reopen and bars and restaurants to allow customers to dine in from 1 June. Today, France's PM announced that many shops (but not large shopping malls) would be able to reopen from 11 May, with the reopening of restaurants and cafés from 1 June. Leaders in Spain and Greece were also set to announce exit strategies today. But in every member state, the return to normal will be gradual, e.g. large public gatherings will be cancelled for several months to come. And consumer behavior will likely take several quarters (if not years) to return to pre-pandemic norms. The quarterly drop in GDP in Q2 will still be of record, double-digit percentage magnitude.

French consumers decidedly downbeat about outlook

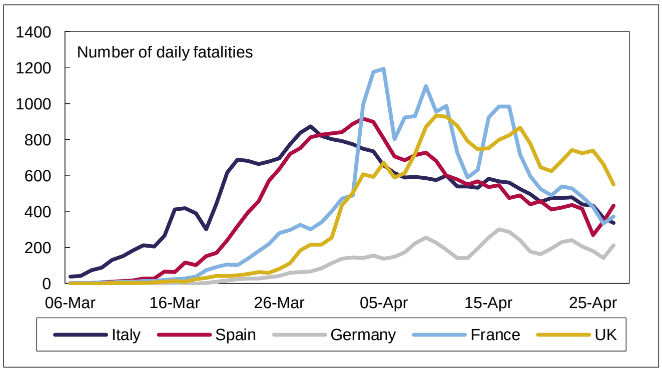
The latest French consumer survey inevitably reported a marked deterioration in sentiment (the survey was conducted from 27 March to 18 April). Indeed, the drop of 8pts in the headline index from March was the sharpest on the series, dating back 48 years. Nevertheless, at 95, it was still well above expectations and merely a fourteen-month low. That might seem encouraging. However, the detail of the survey suggested that sentiment only held up because households appreciated that their standard of living and financial situation over the past year had been better than they had previously judged. In contrast, the forward-looking indicators deteriorated markedly. Among other things, the survey measure of consumers' willingness to make major purchases over the coming twelve months fell by a record amount to a series low (-59). And households' assessment of their future financial situation also declined by a record magnitude, albeit falling merely to the lowest level since May 2014. The worsening in perceptions of financial health is hardly surprising given that more than half of all those employed by the private sector are currently receiving 84% of their usual wages courtesy of the government's 'partial unemployment' scheme. And yesterday's figures showed a record jump in the number of registered job seekers in March of 246.1k, more than three times the previous biggest increase during the global financial crisis, to 3.7mn, the highest level since October 2017. The increase was driven predominantly by temporary workers who are not covered by the government's furlough scheme.

The day ahead in the euro area and US

Tomorrow will bring the European Commission's economic sentiment indicator – the most comprehensive guide to euro area economic activity – for April, which is expected to show a drop in the headline economic sentiment indicator to its lowest level since the global financial crisis. While this will in part reflect weaker consumer confidence, with the flash estimate down 11pts to its lowest since March 2009, business sentiment indicators are likely to report a more marked deterioration, more in line with last week's record-low flash PMIs. Meanwhile, ahead of Thursday's euro area flash CPI figures for April, tomorrow will also bring preliminary data from Germany, which are expected to show that headline inflation fell to just 0.5%Y/Y, a more-than 3½-year low, on the back of weaker energy prices. Wednesday will also bring euro area bank lending figures for March, which might well confirm the pick-up in loan demand flagged in today's ECB survey, as well as Spanish retail sales data for the same month. In the markets, Germany and Italy will sell bonds.

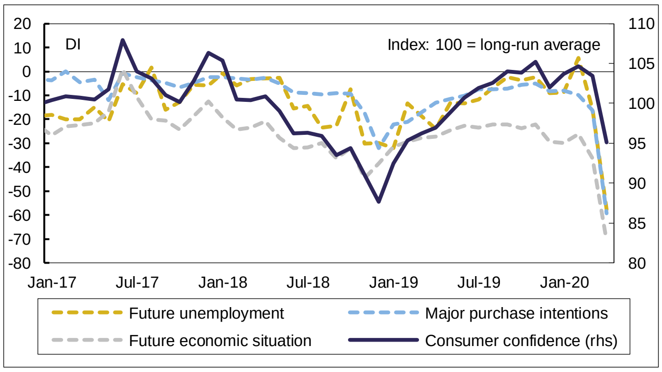
It will be a busy day for US economic events, with the conclusion of the Fed's latest policy-setting meeting to coincide with

Europe: Confirmed Covid-19 fatalities*



*3-day moving average. Source: WHO and Daiwa Capital Markets Europe Ltd.

France: Consumer confidence indicators



Source: Thomson Reuters and Daiwa Capital Markets Europe Ltd.

the first estimate of Q1 GDP. Over the past month or so, the Fed has already announced a comprehensive package of easing measures, including a commitment to make unlimited purchases of USTs and agency MBS if required, a cut in the Fed Funds Rate target range to its effective floor, and the launch of an extensive range of special lending and purchase facilities. So, if there is to be a policy announcement, it would likely involve just a tweak to a recent policy initiative to improve its implementation rather than something completely new. The policy statement and Powell's press conference will, however, no doubt be watched closely for any insight into the Committee's updated thoughts on the economy and expectations for possible future adjustments to its various policy initiatives. In terms of the economic data, the GDP release will provide some insight into the initial hit to activity associated with Covid-19. While a contraction is certainly on the cards, there is a wide range of forecasts – Daiwa America's Chief Economist Mike Moran forecasts a drop of about 2½%Q/Q annualised. March pending home sales figures for March are also due tomorrow.

UK

Retail sales survey signals steeper slump ahead

Following the record decline in last week's official March retail sales figures, today's CBI distributive trades survey unsurprisingly suggested that spending plummeted further at the start of Q2, as the effect of the lockdown weighed even more heavily on demand. Indeed, the headline sales diffusion index fell sharply in April to -55%, matching the trough seen during the global financial crisis and thus representing the joint lowest since the series began in the early 1980s. Perhaps inevitably, the weakness in sales was broad-based with around two-thirds of retailers reporting that the Covid-19 crisis was having a significant negative impact. Indeed, even grocers were more downbeat this month, with the relevant survey balance declining 121ppts to -27% as initial panic-buying of essentials settled down. Internet sales growth also reportedly slowed in April as underlying demand cooled. Moreover, total sales were anticipated to fall at a similar pace in May too, representing the weakest expectations balance in the survey history. And wholesalers suggested that conditions had deteriorated more rapidly than for retailers.

Most retailers facing cash-flow difficulties and laying-off staff

In addition to the usual detail on the level of sales in the latest month, the CBI survey revealed plenty of uncomfortable further detail about conditions in the retail sector. Strikingly 96% of all retailers reported cash-flow difficulties, with 40% facing difficulties meeting tax liabilities. 31% faced constraints on accessing external finance. 44% reported temporarily laying off their staff, including via use of the government's Job Retention Scheme. But 8% had laid staff off permanently. With no concrete plans in place yet to ease the UK lockdown, many shoppers likely to be unwilling to return to the High Street even when restrictions end, and many households suffering a hit to incomes and employment too, retailers will continue to suffer for the foreseeable future as consumers keep a tight rein on their purse strings.

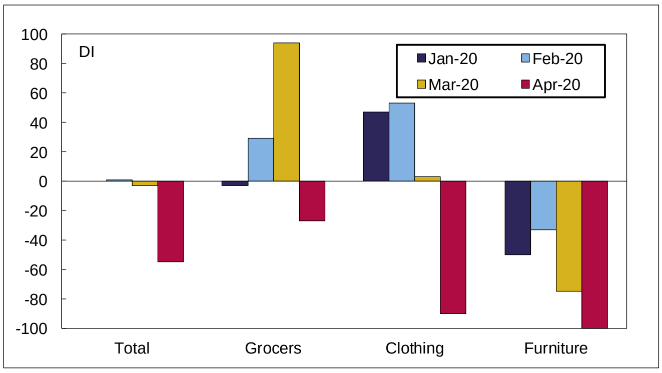
Firms extremely downbeat about the year ahead

Looking at business conditions more generally, the Lloyds business barometer tallied with the downbeat message from last week's flash PMIs. Indeed, the headline optimism indicator fell 38ppts to -32% in April, the lowest reading since the height of the global financial crisis. While firms were understandably more pessimistic about current conditions than they were a month ago, perhaps oddly the relevant index remained above the trough during the Lehman crisis. However, firms were significantly more downbeat about trading prospects over the coming twelve months, with the survey's relevant component falling to a record low (-25%), some way below the GFC trough. Roughly three quarters of respondent firms flagged a negative impact from the coronavirus crisis, with more than a third of those reporting a drop in demand of more than 50%. Against this backdrop, firms' hiring intentions for the year ahead fell to their lowest in nine years, with more than a third of firms anticipating a reduction in their workforce and a little less than one third expecting a pay freeze.

The day ahead in the UK

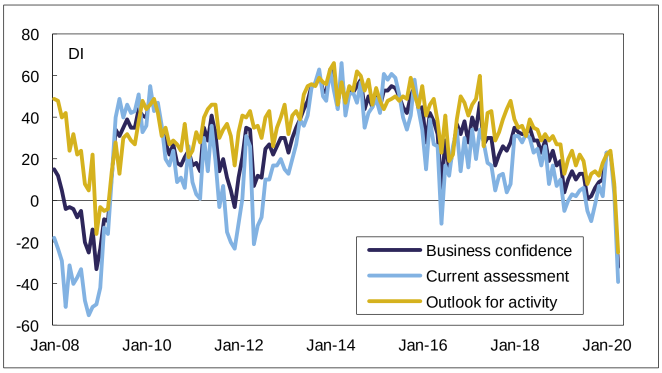
It should be a quiet day for UK economic news tomorrow, with just the BRC shop price index for April due for release.

UK: CBI distributive trades survey



Source: Thomson Reuters and Daiwa Capital Markets Europe Ltd.

UK: Lloyds business barometer



Source: Thomson Reuters and Daiwa Capital Markets Europe Ltd.

European calendar

Today's results

Economic data							
Country		Release	Period	**Actual**	Market consensus/ *Daiwa forecast*	Previous	Revised
France		Consumer confidence	Apr	**95**	80	103	-
Spain		Unemployment rate %	Q1	**14.4**	15.7	13.8	-
UK		Lloyds business barometer	Apr	**-32**	-	6	-
		CBI total distributed sales survey, total sales	Apr	**-55**	-	-3	-
Auctions							
Country		Auction					
UK		sold £1.2bn of 0.125% 2028 index-linked bonds at an average yield of -2.509%					
		sold £3bn of 0.875% 2029 bonds at an average yield of 0.261%					

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

Yesterday's results

Economic data							
Country		Release	Period	**Actual**	Market consensus/ *Daiwa forecast*	Previous	Revised
France		Total jobseekers 000s	Q1	**3333.8**	-	3308.8	**3305.8**
Auctions							
Country		Auction					
		- Nothing to report -					

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

Tomorrow's data releases

Economic data						
Country		BST	Release	Period	Market consensus/ *Daiwa forecast*	Previous
EMU		09.00	M3 money supply Y/Y%	Mar	5.5	5.5
		10.00	Economic sentiment index	Apr	74.0	94.5
		10.00	Industrial confidence (services)	Apr	-25.0 (-26.0)	-10.8 (-2.2)
		10.00	Final consumer confidence	Apr	-22.7	-11.6
Germany		13.00	Preliminary CPI (EU-harmonised CPI) Y/Y%	Apr	0.7 (0.5)	1.4 (1.3)
Spain		08.00	Retail sales Y/Y%	Mar	-4.0	1.8
UK		00.01	BRC shop price index Y/Y%	Apr	-	-0.8
Auctions and events						
Country		BST	Auction / Event			
Germany		10.30	Auction: €4bn of 0% 2030 bonds			
Italy		10.00	Auction €750mn of 2024 floating-rate bonds			
		10.00	Auction €3.75bn of 0.95% 2030 bonds			
UK		10.00	Auction: £3bn of 2.75% 2024 bonds			
		11.30	Auction: £2bn of 1.75% 2049 bonds			

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

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