Daiwa Capital Markets

Euro wrap-up

Overview

Chris Scicluna
+44 20 7597 8326

- Bunds made gains after German policymakers agreed to extend pandemic containment measures for a further four weeks.
- Gilts also made gains even as UK data reported an increase in payrolls and a new twelve-year high in pay growth.
- Wednesday will bring the flash March PMIs and UK inflation figures for February.

Daily bond market movements

Bond	Yield	Change
BKO 0 03/23	-0.720	-0.006
OBL 0 04/26	-0.676	-0.016
DBR 0 02/31	-0.343	-0.030
UKT 0[1]/8 01/23	0.034	-0.025
UKT 0[1]/8 01/26	0.323	-0.039
UKT 4¾ 12/30	0.761	-0.050

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

Euro area

Tightening of German restrictions unlikely to prevent return to growth from Q2 on

As expected in light of the steady uptrend in new coronavirus cases, which saw the seven-day incidence rate surpass the critical threshold of 100 per 100k people, last night's meeting between Chancellor Merkel and regional leaders saw Germany extend its pandemic containment measures through to 18 April. In addition, as in Italy, Germany will enter a stricter lockdown over the Easter holiday period from 1-5 April, when extra restrictions will be placed on many essential stores and citizens will be encouraged to stay at home. Some regions, including the cities of Hamburg and Cologne, had already tightened restrictions over recent days. While the plans mark a U-turn after a gradual easing of restrictions earlier this month, they did not go quite as far as might have been the case, with the controls on non-essential retail not as draconian as Merkel had sought, and German citizens still not compelled to quarantine after returning from foreign travel. Moreover, the measures are still unlikely to prevent a rebound in economic activity in Q2. And assuming swifter implementation of the vaccination programme and a gradual suppression of the pandemic over coming months, that should be followed by further growth in the second half of the year. Notwithstanding the risks posed by possible further mutations of the coronavirus, German GDP should grow between 2.5-3%Y/Y in 2021, allowing the pre-Covid level of German GDP to be reached by Q122.

The day ahead in the euro area

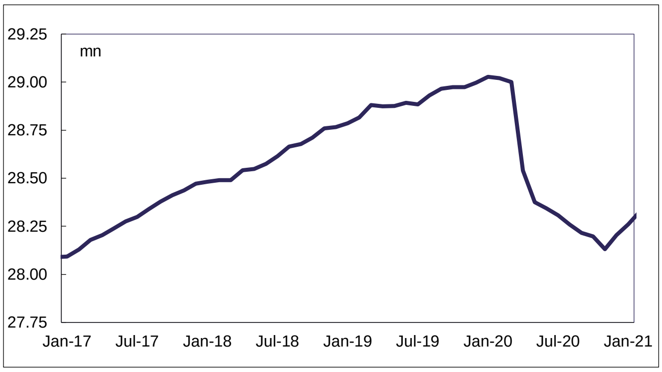
Wednesday will bring the release of the preliminary PMIs for March, which are expected to show little change from February. The headline euro area manufacturing index is likely to move broadly sideways in March from the three-year high of 57.9 last month, with strong growth in the sector likely to be reported in Germany in particular. In contrast, the euro area services PMI is expected to remain below the key 50 expansion/contraction threshold having been little changed at 45.7 in February. The European Commission's preliminary estimate of consumer confidence for March, also due to be published tomorrow, is expected to remain close to February's reading of -14.8, suggesting continued unease about the economic outlook.

UK

Payrolls suggest modest pickup in economic activity in February

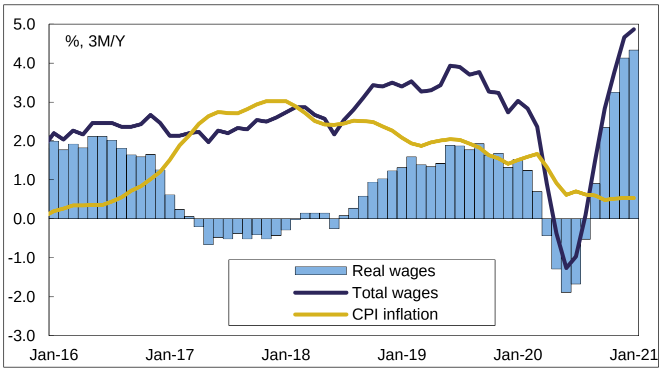
While the various UK labour market data published today pointed in different directions, overall they were largely consistent with stable conditions. Encouragingly perhaps, the ONS reported a third successive monthly increase in the number of payroll employees in February, pointing to a modest pickup in economic activity as businesses and households coped a little better with life under lockdown. The rise of almost 68k was close to the average of the previous two months. But it meant

UK: Payroll employment



Source: ONS and Daiwa Capital Markets Europe Ltd.

UK: Wages and inflation



Source: Refinitiv and Daiwa Capital Markets Europe Ltd.

that there were still 693k (2.4%) fewer workers in payroll employment last month than a year earlier. More than half of that year-on-year decline was explained by the hospitality sector (-368k) while workers under the age of 25 years (-437k) accounted for almost two-thirds of the jobs lost.

But number of vacancies falls back slightly

Among the other data, in the three months to January, the unemployment rate on the ILO measure unexpectedly fell 0.1ppt from the near-5-year high reached the prior month, to 5.0%. But that was still up 1.1ppts from a year earlier. And with the Labour Force Survey measure of employment falling 147k on the quarter, the decline in the ILO unemployment rate reflected an increase in the number inactive, likely reflecting the difficulty of searching for a job during the renewed lockdown. Moreover, the claimant count rate, which includes those working on low incomes or hours as well as those who are not working at all, rose last month for the first time since November, up 0.3ppt to 7.5%, matching August's 24-year high. And the number of vacancies – a key measure of demand – fell 3k to 601k in the three months to February to be still 220k (27%) below the level a year ago.

Pay growth up to new 12-year high

With lower-paid workers more likely to have lost their jobs over the past year, growth in average total pay (including or excluding bonuses) in the three months to January edged up a further 0.1ppt to 4.8%3M/Y (4.2%3M/Y excluding bonuses) in nominal terms – the highest in more than twelve years – to be up 3.9%3M/Y in real terms. There remained significant variation between sectors, with average pay in the finance and business services sector up 7.6%3M/Y but just 2.5% and 2.0% in construction and manufacturing respectively. The ONS estimated that changes in the composition of employment boosted average pay growth by about 1.6ppts, so that underlying total pay growth was likely still close to 3%Y/Y and underlying regular pay growth was still close to 2.5%Y/Y. If sustained, those rates might seem unlikely to generate significantly above-target inflation.

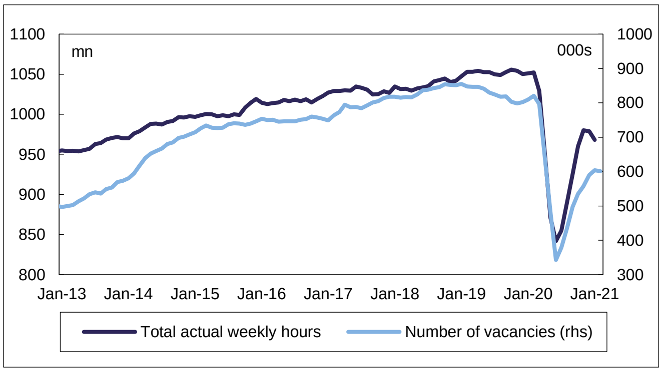
Job Retention Scheme to maintain broad labour market stability through to the autumn

Of course, the broad stability in the labour market reflects the continued support provided by the Government's Job Retention Scheme. HMRC data reported that 4.7mn jobs were furloughed at end-January. And the Business Insights and Conditions Survey suggested a slight increase in the share of the workforce furloughed, to 19%, in the two weeks to 21 February from the prior period. The Budget statement earlier this month confirmed an extension of the Job Retention Scheme to end-September, albeit with the share of salary paid by the Government to be tapered gradually from July on. It also announced a similar extension of support to the self-employed. So, the labour market should remain broadly stable over coming months. Nevertheless, many firms are likely to cut their workforces once the Government's support has been withdrawn. So, based on the Budget proposals, the OBR earlier this month forecast the unemployment rate to peak at 6.5% in Q421. Given the relatively low recent rates of unemployment, we see the risks to that forecast skewed to the downside.

Uncertainties persist over the number of foreign-born workers

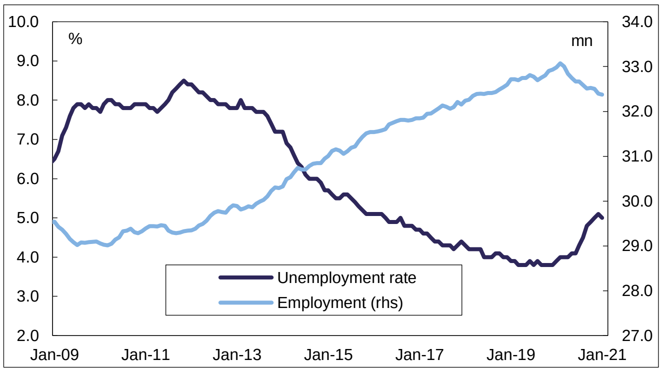
There remain, however, many uncertainties about conditions in the labour market as illustrated by the lack of clarity with respect to the extent of the exodus of foreign-born workers due to the twin shocks of Covid-19 and Brexit. While the Labour Force Survey suggests that the number of foreign-born people in employment dropped almost 800k (14%) between Q419 and Q420, with the number of EU-born workers down almost 500k (20%), payroll data published today suggested that the drop in foreign-born employees was just 4% and the drop in EU-born workers was 7.4%. Some of the difference is likely to be explained by the self-employed, who might have quit the UK in disproportionately large numbers. Nevertheless, regardless of which of those estimates is most accurate, the net emigration of foreign-born workers will likely have reduced the extent of slack in the labour market while also weighing on demand for UK property, not least in London rental markets.

UK: Hours worked and vacancies



Source: ONS, Refinitiv and Daiwa Capital Markets Europe Ltd.

UK: ILO employment and unemployment rate



Source: Refinitiv and Daiwa Capital Markets Europe Ltd.

The day ahead in the UK

In the UK, tomorrow will bring the release of February's inflation figures as well as the March flash PMIs. We expect the headline CPI inflation rate to edge up 0.1ppt to a seven-month high of 0.8%Y/Y in February due to further upward pressure from energy prices, while the core measure is likely to remain unchanged at 1.4%Y/Y. Meanwhile, the preliminary PMIs for March should be slightly improved, with the services and composite PMIs likely to rise back above the key 50 threshold from 49.5 and 49.6 respectively in February.

European calendar

Today's results

Economic data

Country	Release	Period	Actual	Market consensus/ *Daiwa forecast*	Previous	Revised
Italy	Industrial sales M/M% (Y/Y%)	Jan	**2.5 (-1.6)**	-	1.0 (-0.5)	**1.1 (-)**
UK	Unemployment claimant count rate % (change '000s)	Feb	**7.5 (86.6)**	-	7.2 (-20.0)	**- (-20.8)**
	Average earnings including bonuses (excluding bonuses) 3M/Y%	Jan	**4.8 (4.2)**	-	4.7 (4.1)	**-**
	ILO unemployment rate 3M%	Jan	**5.0**	5.2	5.1	**-**
	Employment change '000s 3M/3M	Jan	**-147**	-167	-114	**-**
	CBI industrial trends survey, total orders	Mar	**-5**	-20	-24	**-**

Auctions

Country	Auction
UK	sold £2.25bn of 1.75% 2049 bonds at an average yield of 1.295%

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

Yesterday's results

Economic data

Country	Release	Period	Actual	Market consensus/ *Daiwa forecast*	Previous	Revised
EMU	ECB current account balance €bn	Jan	**30.5**	-	36.7	**-**
Italy	Current account balance €bn	Jan	**0.7**	-	6.7	**-**

Auctions

Country	Auction
	- Nothing to report -

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

Tomorrow's releases

Economic data

Country	GMT	Release	Period	Market consensus/ *Daiwa forecast*	Previous
EMU	09.00	Preliminary manufacturing (services) PMI	Mar	57.8 (46.0)	57.9 (45.7)
	09.00	Preliminary composite PMI	Mar	49.1	48.8
	15.00	European Commission's preliminary consumer confidence	Mar	-14.5	-14.8
Germany	08.30	Preliminary manufacturing (services) PMI	Mar	60.5 (46.5)	60.7 (45.7)
	08.30	Preliminary composite PMI	Mar	51.6	51.1
France	08.15	Preliminary manufacturing (services) PMI	Mar	56.5 (45.5)	56.1 (45.6)
	08.15	Preliminary composite PMI	Mar	47.2	47.0
UK	07.00	CPI (core) Y/Y%	Feb	*0.8 (1.4)*	0.7 (1.4)
	07.00	PPI input prices (output prices) Y/Y%	Feb	2.5 (0.3)	1.3 (-0.2)
	09.30	Preliminary manufacturing (services) PMI	Mar	55.0 (50.8)	55.1 (49.5)
	09.30	Preliminary composite PMI	Mar	51.1	49.6
	09.30	House price index Y/Y%	Jan	8.0	8.5

Auctions and events

EMU	15.40	ECB President Lagarde delivers pre-recorded message at conference on climate change
Germany	10.30	Auction: €4bn of 0% 2031 bonds
UK	11.30	Auction: £350mn of 0.125% 2056 index-linked bonds

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

Access our research blog at:
https://www.uk.daiwacm.com/ficc-research/recent-blogs