# Euro wrap-up

## Overview

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- Bunds made modest losses as the final euro area services and composite PMIs underscored improvement at the start of Q2, producer price inflation picked up to a 2½-year high, and German car production and sales continued to trend below pre-pandemic levels.
- Gilts made losses as UK new car registrations rebounded but similarly remained well down on pre-pandemic levels.
- Thursday brings the latest BoE policy announcement and projections, as well as new data for euro area retail sales and German factory orders.

**Daily bond market movements**

| Bond | Yield | Change |
|---|---|---|
| BKO 0 03/23 | -0.704 | +0.002 |
| OBL 0 04/26 | -0.608 | +0.003 |
| DBR 0 02/31 | -0.231 | +0.009 |
| UKT 0$^1/_8$ 01/23 | 0.042 | +0.006 |
| UKT 0$^1/_8$ 01/26 | 0.351 | +0.006 |
| UKT 4¾ 12/30 | 0.813 | +0.021 |

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

# Euro area

### Somewhat greater clarity on ECB purchase pace until June

Arguably the most notable data from the euro area released so far this week have been the ECB's weekly PEPP asset purchase figures, which helped curb speculation about its targeted pace of buying this quarter. While last week saw significant redemptions (€7.5bn), the second-highest weekly amount of gross purchases since June (€28.5bn) meant that the ECB settled a net €19bn of PEPP purchases last week, pushing its total PEPP holdings above €1.0trn for the first time. Overall, the bank has up to now been averaging close to a net €80bn of monthly PEPP asset purchases since its 11 March Governing Council meeting when the policymakers decided to conduct a "significantly higher pace" this quarter, up from the monthly average of just over €60bn in the prior six months. Despite the Executive Board's deliberate ambiguity about its intentions, we should expect the ECB to continue to buy PEPP assets at roughly that €80bn monthly pace ahead of the 10 June meeting, albeit with continued volatility from week to week.

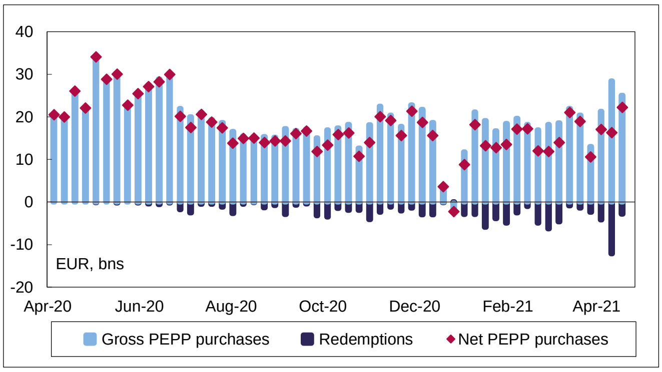
### Will ECB dare to taper before the Fed?

While continuation of purchases at this rate after June would see the €1.85trn envelope exhausted at end-March 2022, in line with the Governing Council's current policy guidance, comments from policymakers raise a clear possibility that the pace will be slowed sooner rather than later. Certainly, some members will try to push for that moderation in the pace of purchase at the June policy meeting. And in public remarks today, ECB Chief Economist Lane noted that the process of adjusting asset purchases would not be "linear". Given concerns of a further upwards shift in yields, appreciation of the euro and unwanted tightening of financial conditions, June might be too soon to reduce the pace of purchases. But, in an interview with La Repubblica published at the start of the week, ECB Vice President de Guindos suggested that the ECB "may start to think about phasing out the emergency mode on the monetary policy side" if and when – as seems likely will be the case by end-July – 70% of Europe's adult population have been vaccinated and the economy more fully reopens and more rapidly recovers. That would likely imply a clear reduction in the pace of purchase from the September Governing Council meeting, which could therefore come ahead of any Fed tapering. And a full phasing out of the PEPP purchases – but not purchases under the regular PSPP – might now seem likely by end-March.

### Euro area services and composite PMIs revised slightly higher, Spanish improvement stands out

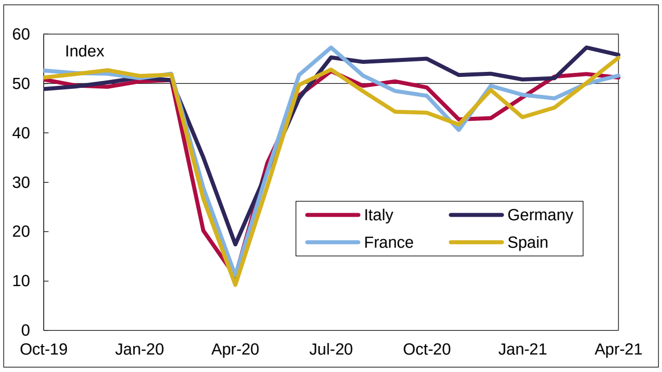
While the final manufacturing PMIs earlier in the week registered only modest downwards revisions – so that the final euro area output PMI dropped just 0.1pt from March's series high to 63.2 – today's final services and composite PMIs for April provided slightly better news than their flash estimates suggesting continued resilience to ongoing restrictions pandemic restrictions. The euro area services activity PMI was nudged up to 50.5, the highest since August and 3.6pts above the Q1

**ECB: Weekly PEPP purchases**




*Source: ECB and Daiwa Capital Markets Europe Ltd.*

**Euro area: Final composite PMIs by country**




*Source: Refinitiv and Daiwa Capital Markets Europe Ltd.*

average to point to broad stability in the sector. And so, the euro area composite output PMI was revised up slightly to 53.8, the best since July, almost 4pts above the Q1 average and a level consistent with an expanding economy for the second successive month. At the country level, however, the services PMIs suggested little change in Germany and France in April, and weakening in Italy, due to the tightening of restrictions. So, the improvement was caused by a significant step change for the better in Spain, where the services activity PMI jumped a hefty 6.5pts to a two-year high of 54.6. And, as such, Spain's composite output PMI (55.2, the best since May 2018) was second only to Germany's (55.8), while those of France (51.6) and Italy (51.2) pointed to only very modest growth at the start of Q2.

## Input price pressures rising but still largely absorbed by margins

As with the flash estimates, the final PMIs highlighted increased pipeline price pressures, with the manufacturing input price index up to the highest in more than a decade (82.2) and at a level that has only been exceeded in two months of the series. And against the backdrop of continued supply shortages, firms in that sector also reportedly passed on higher costs to customers by the most on the series (the manufacturing output price PMI rose to 64.3). Other data released today showed that euro area producer price inflation jumped a hefty 2.8ppts in March to 4.3%Y/Y, the highest since autumn 2018, on rising prices of intermediate goods as well as raw materials and energy. And the PMIs would suggest such price pressures increased further last month. But with consumer prices of non-energy industrial goods up just 0.5%Y/Y in April, the flash April CPI data implied that, for now at least, retailers are not passing on those increased costs to households. Moreover, in services, the pressures are significantly less marked, with the input and output price PMIs merely up to the highest since the first quarter of 2020.

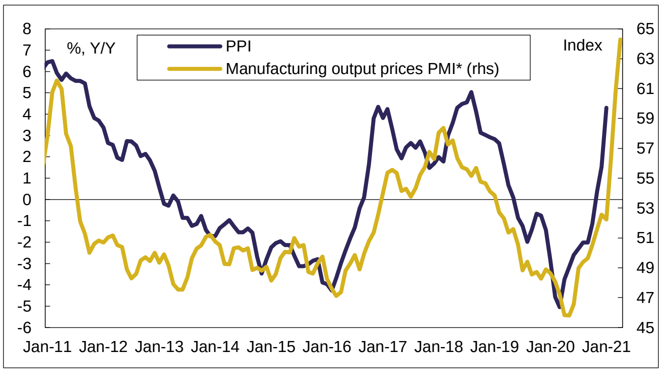
## German car registrations and production still trending well below pre-pandemic levels

Like other large member states (e.g. up 569%Y/Y in France and more than 32-fold from a year ago in Italy), new car registrations in Germany in April were well above their level a year earlier, rising 90.0%Y/Y having jumped 35.9%Y/Y the prior month. Those growth rates were, of course, exaggerated by the extremely low base during the first wave of pandemic. Compared to April 2019, new registrations were still down 26.0%, with registrations in the year to-date also down more than 25% from the first four months of 2019. And registrations were about one fifth below the April average in the decade before the pandemic. Meanwhile, German car production was up more than 25-fold from April 2020. But it was still more than 22% below the level in April 2019, and down 25% on a year-to-date basis from two years ago. And it was about one third below the April average in the decade ahead of the pandemic. Given the tepid recovery in sales so far this year – weighed by the pandemic and January's increase in VAT – as well as ongoing supply-side disruption related not least to semiconductor deliveries, the German auto industry association VDA reduced its production forecast for 2021 to 4 million units, which would represent a full-year rise of a little more than 13%Y/Y.

## The day ahead in the euro area

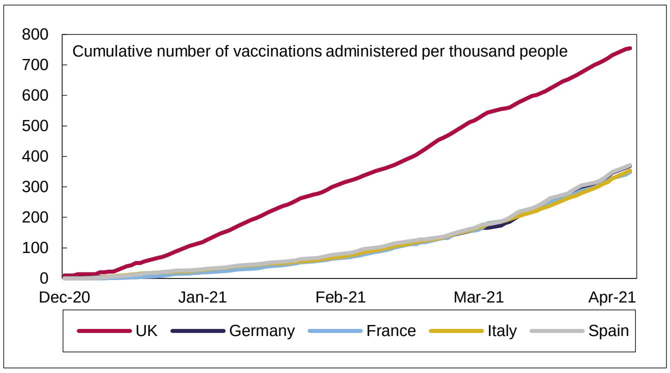
Tomorrow brings the release of March data for euro area retail sales and German factory orders. Following an upside surprise to the German figures, which reported a rebound of 7.7%M/M in March, euro area retail sales are now likely to rise about 2.5%M/M to just below the pre-pandemic level in February 2020. Given the steep drop a year earlier, however, the annual growth rate would then rise to about 10.5%Y/Y following a drop of 2.9%Y/Y in February. German factory orders are also expected to have risen in March, by 1.5%M/M and a whopping 25.5%Y/Y, which would leave them 7.4% higher compared with February 2020, a further sign that activity in the manufacturing sector is accelerating.

### Euro area: Producer price indicators




**PMI has two-month lead. Source: Refinitiv and Daiwa Capital Markets Europe Ltd.*

### Covid-19 vaccinations by country




*Source: Bloomberg and Daiwa Capital Markets Europe Ltd.*

# UK

## Car registrations rebound in April but remain well down on same month in 2019

As in the euro area member states, new car registrations in the UK rebounded in April, albeit with the level remaining well down on pre-Covid norms for the month. In particular, having plunged to just 4321 cars in April 2020, SMMT data showed that new car registrations rebounded to 141.6k last month as English showrooms reopened from the twelfth of the month. That, however, meant that registrations were still down more than 12% from the same month in 2019 and also down almost 13% from the April average in the decade ahead of the pandemic. In the first four months of the year, new car registrations were up 16.2%Y/Y, but down more than 34%Y/Y from the equivalent period of 2019. With demand earlier in the year having been suppressed by pandemic restrictions, consumer confidence having picked up and pent-up demand reflected in historically high household savings, we expect to see new car registrations continue to rebound over coming months. SMMT revised up its own forecast for 2021 as a whole to 1.86m, which would represent growth of 13.9% from 2020 albeit a drop of almost 20% from 2019.

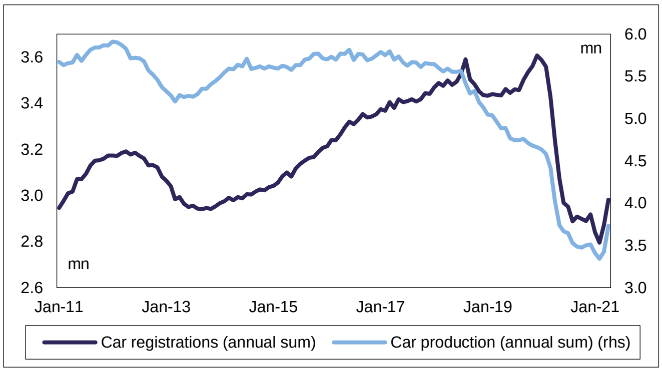
## The day ahead in the UK

The main event in the UK tomorrow will be the BoE's monetary policy announcement, which will be accompanied by updated economic projections in the latest Monetary Policy Report. Recent economic data have largely been stronger than the MPC expected when the last projections were published in February. Indeed, while the BoE forecast a fall in GDP of 4.2%Q/Q in Q1, we currently expect a decline of just 1.5%Q/Q. Thanks to ongoing government support for the labour market, unemployment appears to be undershooting the BoE's projection too. And while CPI inflation, at 0.6%Y/Y in Q1, was slightly below the BoE's forecast, weakness was principally due to clothes discounting, which is likely to prove temporary.
There are many reasons for the BoE to be optimistic about the near-term economic outlook too. The rate of new Covid-19 cases has slowed significantly across the UK while progress with vaccinations has been rapid, with more than half of all adults having received at least one dose already. So, the government has been able to ease restrictions at a faster pace than assumed previously by the BoE. In addition, UK fiscal policy this year and next will be more supportive than it had assumed in the February forecasts, not least due to extensions to the government's business support measures to September and the "super-deduction" tax relief for businesses to encourage investment. Prospects for external demand, particularly from the US, have improved too. So, as Governor Bailey suggested in a radio interview ahead of the March MPC meeting, the BoE will likely bring forward the date to Q421 (from Q122) at which it expects the pre-Covid level of GDP to be surpassed.

The MPC is unlikely to be complacent about the near-term outlook, however. The emergence of new mutations that render vaccines ineffective remains a key risk. Current waves of pandemic in many countries, not least India, provide a reminder that the global economy is not out of the woods just yet. There are also significant uncertainties with respect to the impact of the phasing out of government support measures later in the year, not least on the labour market, in which the full extent of slack is hard to determine. And looking further ahead into 2023, the BoE will have to anticipate a non-negligible tightening of fiscal policy from FY23/4, which could well weigh significantly on economic activity at the end of its projection period. The inflation projection will also be weighed by the market-implied path for Bank Rate, which is now significantly higher than that used to produce the February projections. Indeed, the BoE might still judge that inflation at the end of its projection is unlikely to be significantly above its 2.0%Y/Y inflation target.

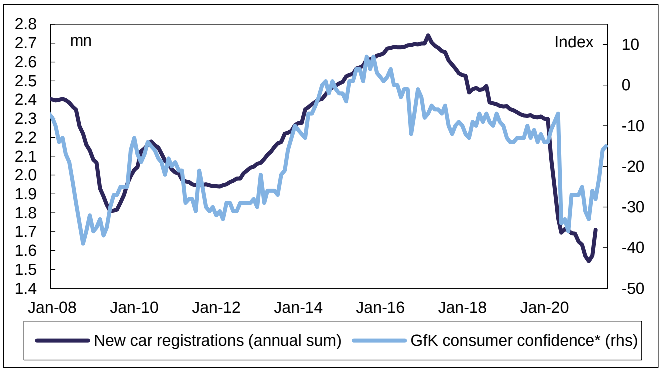
Despite recent upward shifts in market rates, however, the MPC will still judge financial conditions to have remained highly accommodative. By the same token, they will not consider them overly so, and they would not necessarily welcome a significant tightening of conditions just yet. So, with only one member of the MPC (the soon-to-depart Chief Economist Haldane) who might feasibly be considered a hawk, the MPC will probably not yet see the need to taper its Gilt purchases

### Germany: New car registrations and production




*Source: VDA, Refinitiv and Daiwa Capital Markets Europe Ltd.*

### UK: New car registrations and consumer confidence




*Consumer confidence has three-month lead. Source: SMMT, *Refinitiv and Daiwa Capital Markets Europe Ltd.*

from its current pace of £4.2bn per week. Unlike the Fed, however, it will likely continue to signal its expectation to phase them out gradually before year-end. But a decision to start that process seems most likely to come at the 24 June meeting, which is scheduled just three days after the government currently plans to lift all limits on social contact.

Datawise, the final UK service sector and composite PMIs are due tomorrow. The flash release revealed that the composite output PMI rose a hefty 3.6pts to 60, the highest in more than seven years. The services activity PMI similarly jumped to 60.1, to match the highest level since August 2014.

# European calendar

## Today's results

**Economic data**

| Country | Release | Period | **Actual** | Market consensus/ *Daiwa forecast* | Previous | Revised |
|---|---|---|---|---|---|---|
| EMU | Final services (composite) PMI | Apr | **50.5 (53.8)** | 50.3 (53.7) | 49.5 (53.2) | - |
| Germany | PPI Y/Y% | Mar | **4.3** | 4.1 | 1.5 | - |
| | Final services (composite) PMI | Apr | **49.9 (55.8)** | 50.1 (56.0) | 51.5 (57.3) | - |
| | New car registrations Y/Y% | Apr | **90** | - | 35.9 | - |
| France | Final services (composite) PMI | Apr | **50.3 (51.6)** | 50.1 (51.7) | 48.2 (50.0) | - |
| Italy | Services (composite) PMI | Apr | **47.3 (51.2)** | 50.1 (53.0) | 48.6 (51.9) | - |
| | Unemployment change '000s | Apr | **-39.0** | - | -59.1 | - |
| Spain | Services (composite) PMI | Apr | **54.6 (55.2)** | 49.6 (51.6) | 48.1 (50.1) | - |
| UK | New car registrations Y/Y% | Apr | **3176** | - | 11.5 | - |

**Auctions**

| Country | Auction |
|---|---|
| Germany | sold €3.33bn of 0% 2026 bonds at an average yield of -0.61% |
| UK | sold £2.75bn of 0.25% 2031 bonds at an average yield of 0.924% |
| | sold £2bn of 0.875% 2046 bonds at an average yield of 1.322% |

*Source: Bloomberg and Daiwa Capital Markets Europe Ltd.*

## Yeserday's results

**Economic data**

| Country | Release | Period | **Actual** | Market consensus/ *Daiwa forecast* | Previous | Revised |
|---|---|---|---|---|---|---|
| UK | Final manufacturing PMI | Apr | **60.9** | 60.7 | 58.9 | - |
| | Net consumer credit £bn (Y/Y%) | Mar | **-0.5 (-8.6)** | -0.5 (-) | -1.2 (-9.9) | **- (10.0)** |
| | Net mortgage lending £bn (approvals '000s) | Mar | **11.8 (82.7)** | 5.8 (85.5) | 6.2 (87.7) | **6.4 (87.4)** |
| | M4 money supply Y/Y% | Mar | **10.8** | - | 13.6 | **13.7** |

**Auctions**

| Country | Auction |
|---|---|
| Germany | sold €155mn of 0.1% 2046 index-linked bonds at an average yield of -1.27% |
| | sold €423mn of 0.1% 2026 index-linked bonds at an average yield of -1.88% |

*Source: Bloomberg and Daiwa Capital Markets Europe Ltd.*

Daiwa Capital Markets

## Monday's results

**Economic data**

| Country | Release | Period | **Actual** | Market consensus/ *Daiwa forecast* | Previous | Revised |
|---|---|---|---|---|---|---|
| EMU | Final manufacturing PMI | Apr | **62.9** | 63.3 | 62.5 | **-** |
| Germany | Retail sales M/M% (Y/Y%) | Mar | **7.7 (11.0)** | 3.0 (-0.2) | 1.2 (-9.0) | **2.7 (-6.6)** |
| | Final manufacturing PMI | Apr | **66.2** | 66.4 | 66.6 | **-** |
| France | Final manufacturing PMI | Apr | **58.9** | 59.2 | 59.3 | **-** |
| | New car registrations Y/Y% | Apr | **569** | - | 192 | **-** |
| Italy | Manufacturing PMI | Apr | **60.7** | 60.9 | 59.8 | **-** |
| | New car registrations Y/Y% | Apr | **3276** | - | 497 | **-** |
| Spain | Manufacturing PMI | Apr | **57.7** | 59.0 | 56.9 | **-** |
| | New car registrations Y/Y% | Apr | **1787** | - | 128 | **-** |

**Auctions**

| Country | Auction |
|---|---|
| - Nothing to report - | |

*Source: Bloomberg and Daiwa Capital Markets Europe Ltd.*

## Tomorrow's releases

**Economic data**

| Country | BST | Release | Period | Market consensus/ *Daiwa forecast* | Previous |
|---|---|---|---|---|---|
| EMU | 08.30 | Construction PMI | Apr | - | 50.1 |
| | 10.00 | Retail sales M/M% (Y/Y%) | Mar | *2.5 (10.5)* | 3.0 (-2.9) |
| Germany | 07.00 | Factory orders M/M% (Y/Y%) | Mar | 1.5 (25.6) | 1.2 (5.6) |
| | 08.30 | Construction PMI | Apr | - | 47.5 |
| France | 08.30 | Construction PMI | Apr | - | 49.7 |
| Italy | 08.30 | Construction PMI | Apr | - | 56.3 |
| UK | 09.30 | Final services (composite) PMI | Apr | 60.1 (60.0) | 56.3 (56.4) |
| | 12.00 | BoE Bank Rate % | May | *0.10* | 0.10 |
| | 12.00 | BoE Gilt purchase target £bn | May | *875* | 875 |

**Auctions and events**

| Country | BST | Event |
|---|---|---|
| EMU | 09.00 | ECB publishes Economic Bulletin |
| | 11.30 | ECB's de Guindos participates in online Q&A session |
| | 14.15 | ECB's Schnabel scheduled to speak |
| France | 09.50 | Auction: 0% 2031 bonds |
| | 09.50 | Auction: 0.5% 2040 bonds |
| | 09.50 | Auction: 0.75% 2052 bonds |
| Spain | 09.30 | Auction: fixed-rate bonds |
| UK | 12.00 | BoE monetary policy announcement |
| | 12.00 | BoE publishes quarterly Monetary Policy Report |
| | 14.00 | BoE publishes monthly Decision Maker Panel data |

*Source: Bloomberg and Daiwa Capital Markets Europe Ltd.*

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