Daiwa Capital Markets

Euro wrap-up

Overview

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- Bunds followed USTs higher while the ECB's latest bank lending survey reported a tightening in credit standards and German investor confidence continued to deteriorate amid ongoing uncertainties with the Ukraine war.
- Gilts also made gains as the latest UK labour market data saw real regular pay growth decline despite increasing tightness in the market.
- Tomorrow brings UK consumer price inflation figures for March, as well as revised Spanish CPI and Italian IP.

Daily bond market movements

Bond	Yield	Change
BKO 0 03/24	0.054	-0.069
OBL 0 04/27	0.557	-0.064
DBR 0 02/32	0.784	-0.027
UKT 1 04/24	1.499	-0.062
UKT 1¼ 07/27	1.554	-0.058
UKT 4¼ 06/32	1.793	-0.054

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

Euro area

ECB survey shows credit standards tighten amid heightened uncertainties

Ahead of Thursday's Governing Council meeting, today's ECB bank lending survey unsurprisingly implied a marked tightening in credit standards for firms amid heightened uncertainties as well as reduced risk tolerance given the Ukraine war, persisting supply chain disruption and rising price pressures. Overall, a net 6% of banks tightened lending standards on loans to NFCs in the first quarter, with a significantly larger share (21%) expecting to tighten them further in Q2, reflecting additional concerns relating to the anticipation of less accommodative monetary policy. The expected net tightening in Q2 was similar to that observed at the height of the pandemic concerns and in early 2012 as the euro area sovereign debt crisis intensified, although it was still notably smaller that during the global financial crisis. There was a continued net increase in loan demand from firms, although this in part reflected rising financing needs for working capital due to supply bottlenecks and increasing cost burdens, with a smaller positive contribution attributed to the need for fixed investment. And while banks suggested that net loan demand from households increased further in Q1, reflecting low interest rates and increased demand for consumer credit amid higher durable goods consumption, banks expected a net decrease in Q2 amid the uncertain economic outlook.

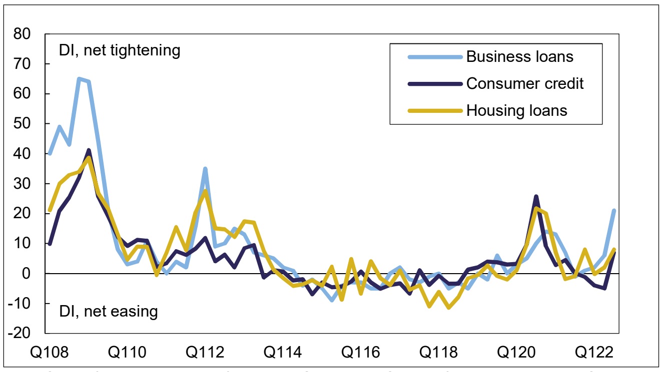
German ZEW survey sees a further notable deterioration at start of Q2

While today's German ZEW survey came in a touch firmer than expectations, it still suggested that investor confidence had fallen markedly further at the start of the second quarter. Consistent with last week's sentix survey, there was another sizeable drop in the current conditions balance in April, with the index down 9.4pts to -30.8, the lowest level since May 2021, some 63pts lower than September's recent peak and well below the long-run average (-7.7). But while the equivalent expectations balance fell by a much smaller 1.7pts – perhaps reflecting the near-halving of the inflation expectations balance from March's record high – the index still stood at -41.0, its lowest since March 2020 and some 95pts lower than the pre-Russian invasion level. Unsurprisingly, this deteriorating outlook was judged to hit substantially the profit outlook for almost all sectors, with the autos and steels sectors the most severely impacted.

The day ahead in the euro area

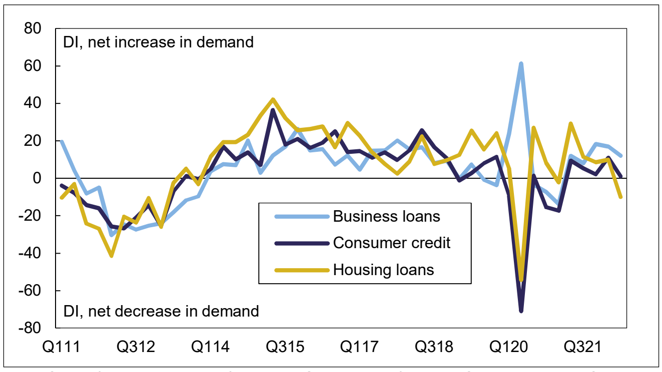
Another relatively quiet day for euro area releases tomorrow brings Italian industrial production numbers for February, which are expected to report a rise in output of 1.0%M/M which would merely reverse part of the 3.4%M/M drop in January, alongside ISTAT's latest monthly economic update. Wednesday will also bring revised Spanish CPI inflation figures for

Euro area: Net change in credit standards*



*Q222 figure is survey forecast. Source: ECB, Refinitiv and Daiwa Capital Markets Europe Ltd.

Euro area: Net change in demand for loans*



*Q222 figure is survey forecast. Source: Refinitiv, ECB and Daiwa Capital Markets Europe Ltd.

March, which are expected to align with the preliminary estimate that showed prices rising at a record monthly pace (3.9%M/M), to leave the annual HICP rate up 2.2ppts to 9.8%Y/Y.

UK

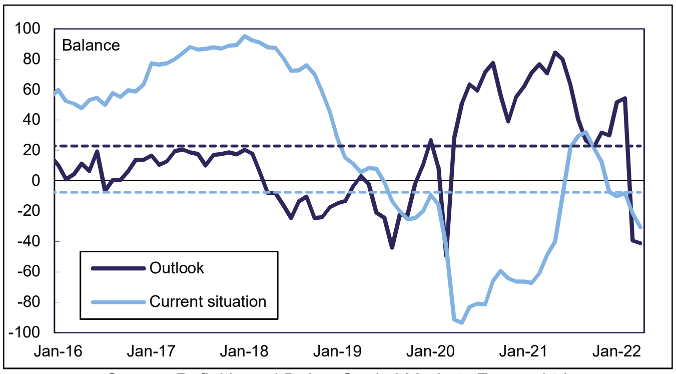
UK labour market tightens further as inactivity and vacancies both rise further

Today's UK labour market report extended recent trends, suggesting increasing tightness even as pay struggles to keep up with rising prices. Despite softer GDP growth in February, the unemployment rate fell 0.1ppt in the three months to February to 3.8%, back to its level at the end of 2019 and a rate that was last lower in 1974. But this principally reflected a further increase in inactivity in February, with the 3M rate now 1.2ppt above that before the pandemic (and the single-month rate the highest for almost five years) due not least to increased long-term sickness. Indeed, while the number of full-time employees continued to rise and self-employment rose for the first month in seven (albeit still remaining some 800k lower than before the pandemic), the number of people in employment rose just 10k in the three months to February, to leave the employment rate down 0.1ppt at 75.5% (with the single-month rate the lowest for seven months). The more timely but highly volatile payroll numbers also reported the softest monthly increase in March (35k) for more than a year, with the increase in February (174k) revised down by 100k from the initial estimate too. But while the pace of increase slowed again, the number of job vacancies rose to a new record high, to 1.288mn, with record levels in half the sectors. So, the ratio of unemployed workers to vacancies – a key measure of labour market tightness – hit a fresh record low.

Additional pay pressures in the private sector, but real wage growth remains negative

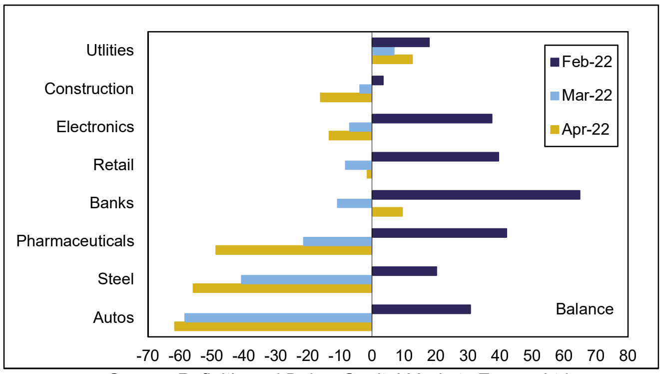
Meanwhile, average total pay (including bonuses) rose 0.6ppt to 5.4%3M/Y in February largely thanks to higher bonuses. However, it was only up a minimal 0.4%3M/Y in real terms. Growth in regular pay (i.e. excluding bonuses) also edged up 0.2ppt to 4.0%3M/Y – back close to the top end of the range between the global financial crisis and the pandemic – with the 3M/3M annualized rate at 5.2% reflecting a jump in underlying private sector wages (up 0.7ppt to 6.3%). In contrast, public sector regular wage growth fell to a three-month low of 3.2%3M/3M ann. And in real terms, underlying pay continued to decline, with total regular wages down a marked 1.0%3M/Y. With inflation set to accelerate markedly further over the near term – to well above 8.0%Y/Y in April – real pay will fall sharply this year, with household real disposable incomes set to decline the most in more than four decades.

Germany: ZEW investor confidence



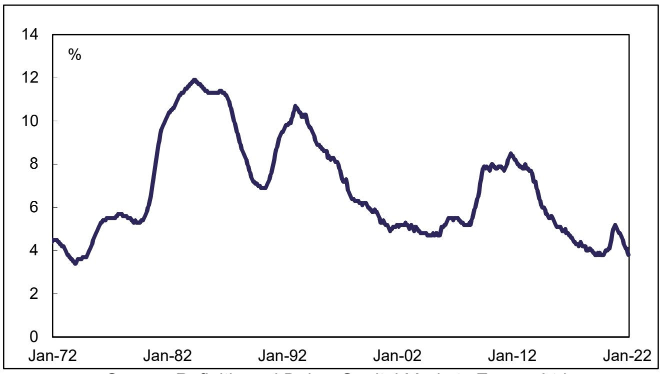
Source: Refinitiv and Daiwa Capital Markets Europe Ltd.

Germany: ZEW investor profit expectations



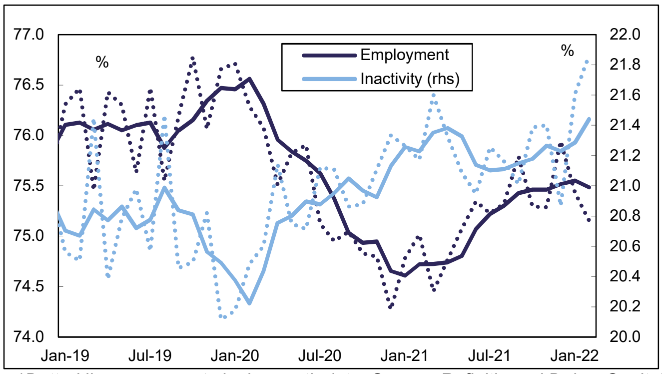
Source: Refinitiv and Daiwa Capital Markets Europe Ltd.

UK: Unemployment rate



Source: Refinitiv and Daiwa Capital Markets Europe Ltd.

UK: Employment and inactivity rates*



**Dotted lines represent single-month data. Source: Refinitiv and Daiwa Capital Markets Europe Ltd.*

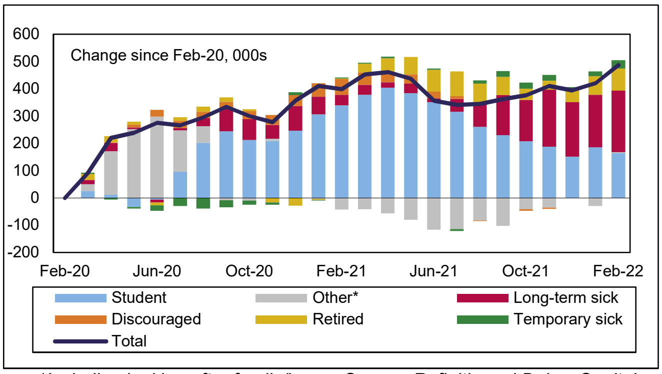
BRC retail sales monitor points to marked slowdown in spending

Against this backdrop, today's BRC retail sales monitor offered a relatively bleak assessment for the retail sector at the end of the first quarter. Indeed, despite a significant boost from higher prices, total sales growth (in nominal terms) slowed sharply in March, down 3.6ppts to 3.1%Y/Y. And like-for-like sales fell 0.4%Y/Y, the most since last September and a drop that would be notably steeper if adjusted for price effects. Admittedly some of this weakness might well reflect increased opportunities to spend on services as the final pandemic restrictions were lifted. Certainly, today's Barclaycard consumer spending numbers suggested that spending on credit cards in March was 17.7% higher than in the same period in 2019 with hospitality reporting particularly strong growth (18.3%) as spending at bars, clubs and pubs jumped (41.7%). But some of that growth can be attributed to the rising popularity of contactless payments that accelerated during the pandemic. And Barclaycard noted that the increase in spending on essentials (18.1%) was largely driven by rising fuel and food prices. Nine out of ten consumers expressed concerns about the negative impact of rising household bills, with more than 40% of drivers changing the way they travel in response to rising fuel prices. With household budgets set to be squeezed further this month by the more than 50% rise in household energy bills and increase in national insurance contributions, we continue to expect much weaker spending on non-essential items over coming months.

The day ahead in the UK

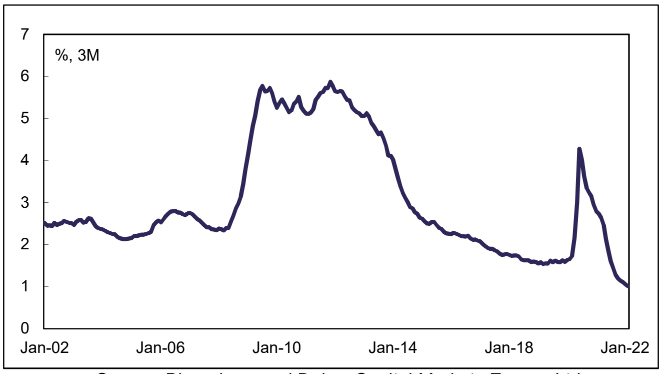
Focus in the UK tomorrow will turn to March's CPI inflation report, which we expect to show the headline CPI rate increased 0.6ppt to 6.8%Y/Y, a fresh 30-year high. While energy prices will continue to exert significant upwards pressure, we also expect prices of non-energy industrial goods and services to rise further, boosting core inflation by 0.3ppt to 5.5%Y/Y, similarly a 30-year high. PPI inflation numbers are also expected to reveal that price pressures at the factory gate remain extremely elevated. The official house price index for February is also due for release.

UK: Inactivity by reason



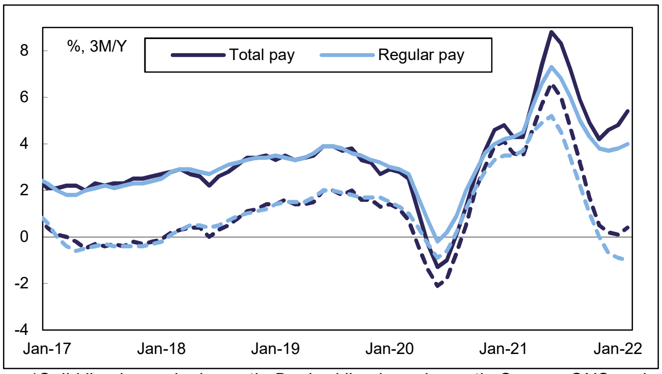
*Including looking after family/home. Source: Refinitiv and Daiwa Capital Markets Europe Ltd.

UK: Unemployment to vacancy ratio



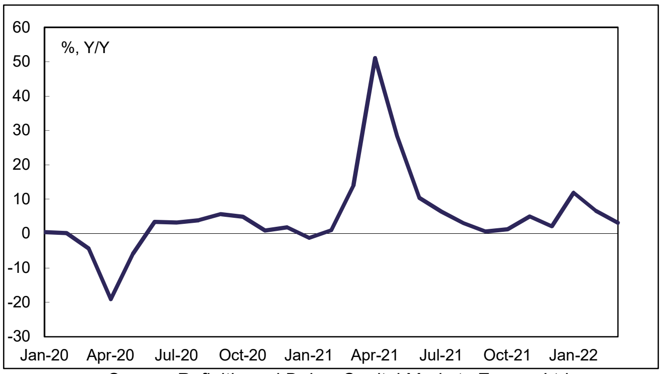
Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

UK: Wage growth*



*Solid line is nominal growth. Dashed line is real growth. Source: ONS and Daiwa Capital Markets Europe Ltd.

UK: BRC retail sales



Source: Refinitiv and Daiwa Capital Markets Europe Ltd.

European calendar

Today's results

Economic data

Country		Release	Period	**Actual**	Market consensus/ *Daiwa forecast*	Previous	Revised
Germany		Final CPI (EU-harmonised CPI) Y/Y%	Mar	**7.3 (7.6)**	*7.3 (7.6)*	5.1 (5.5)	-
		ZEW current situation (expectations) balance	Apr	**-30.8 (-41.0)**	-35.0 (-48.5)	-21.4 (-39.3)	-
UK		BRC retail sales monitor, like-for-like sales Y/Y%	Mar	**-0.4**	-	2.7	-
		Unemployment claimant count rate % (change '000s)	Mar	**4.3 (-46.9)**	-	4.4 (-48.1)	**- (-58.0)**
		Employment change 3M/3M, '000s (Payrolled employees, '000s)	Feb	**10 (35)**	52 (113)	-12 (275)	**- (174)**
		ILO unemployment rate 3M%	Feb	**3.8**	3.8	3.9	-
		Average wages including (excluding) bonuses 3M/Y%	Feb	**5.4 (4.0)**	5.4 (4.0)	4.8 (3.8)	-

Auctions

Country		Auction
Germany		sold €4.5bn of 0% 2024 bonds at an average yield of 0.16%
UK		sold £2.5bn of 1% 2032 bonds at an average yield of 1.925%

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

Tomorrow's releases

Economic data

Country		BST	Release	Period	Market consensus/ *Daiwa forecast*	Previous
Italy		09.00	Industrial production M/M% (Y/Y%)	Feb	1.4 (0.9)	-3.4 (-2.6)
Spain		08.00	Final CPI (EU-harmonised CPI) Y/Y%	Mar	*9.8 (9.8)*	7.6 (7.6)
UK		07.00	CPI (core CPI) Y/Y%	Mar	*6.8 (5.5)*	6.2 (5.2)
		07.00	PPI input (output) prices Y/Y%	Mar	15.1 (11.1)	14.7 (10.1)
		09.30	House price index Y/Y%	Feb	10.1	9.6

Auctions and events

Country		BST	Event
Germany		10.30	Auction: €4bn of 0% 2032 bonds
Italy		10.00	Auction: €3.75bn of 1.2% 2025 bonds
		10.00	Auction: €1.5bn of 0.45% 2029 bonds
		10.00	Auction: €1bn of 3% 2029 bonds
		10.00	Auction: €750mn of 3.1% 2040 bonds
		10.00	Auction: €1bn of 2.15% 2052 bonds

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.