Euro wrap-up

Overview

- Long-term bunds made losses as the ECB reduced the monthly pace of its asset purchases from €80bn to €60bn.
- Gilts also made losses at the longer-end on a quiet day for major economic news in the UK.
- German and UK trade figures are the most notable data releases tomorrow. Meanwhile, French industrial production and UK construction output figures are also due.

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Daily bond market movements

Bond	Yield	Change*
BKO 0 12/18	-0.734	-0.058
OBL 0 10/21	-0.401	-0.038
DBR 0 08/26	0.382	+0.038
UKT 1¼ 07/18	0.105	-0.012
UKT 3¾ 09/21	0.566	-0.005
UKT 1½ 07/26	1.378	+0.019

*Change from close as at 4.35pm GMT.
Source: Bloomberg

Euro area

ECB offers something for (almost) everyone

Today's ECB meeting saw the announcement of an extension in its asset purchase programme (APP) for a further nine months from April 2017 at a pace of €60bn per month, €20bn less per month than the current purchase pace (which will continue through to the end of March 2017). To facilitate these purchases, the ECB also announced some amendments to the parameters of its purchase programme, (a) allowing the purchase of bonds with a remaining maturity of 1 year or more (previously 2 years) and (b) removing the yield floor on purchases (previously -40bps). Both of these measures will have the effect of increasing the universe of bonds that the ECB is able to purchase. The announcement had something for just about everyone. Those looking for a tapering would welcome the forthcoming drop in the monthly purchase amount (although Draghi was at pains to explain that, in the ECB's opinion, this didn't represent a tapering, nor had any member of the Governing Council proposed tapering). But others will welcome the fact that the total additional amount of purchases (€540bn) is larger than if the ECB had simply announced a six-month extension of its current purchase pace (which would have amounted to €480bn). Moreover, the Governing Council (which Draghi indicated had a "very, very broad consensus" on today's decisions) maintained a very dovish tone, promising to increase the size and/or duration of the APP if the outlook becomes less favourable or if monetary conditions tighten.

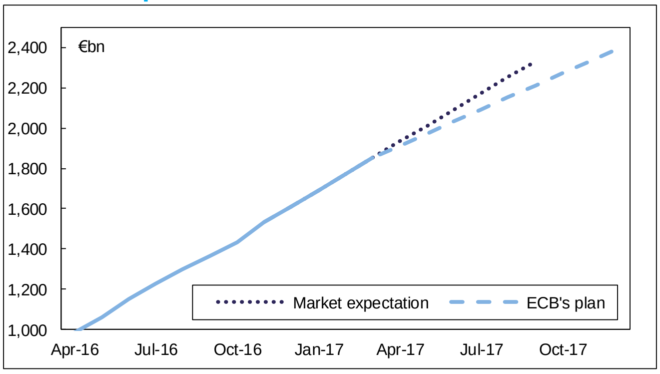
Forecasts suggest question of another APP extension to return

Certainly, the ECB's updated forecasts didn't suggest that it is much more optimistic about the economic outlook despite some recent encouraging survey data in particular. Its GDP forecast for 2017 is only a touch firmer than its previous forecast at 1.7%, while anticipated growth of 1.6% in 2018 is unchanged from before. And growth is not expected to accelerate in 2019, which was included in the ECB's projections for the first time today. And, notwithstanding an anticipated significant short-term pick-up in inflation on the back of higher energy prices, weak underlying price pressures are expected to keep headline inflation below the ECB's target – headline inflation is expected to be just 1.7% in 2019. Certainly, given that Draghi indicated that the Governing Council is looking for a sustained adjustment of the path of inflation 'without undue delay', if these forecasts are borne out, then the question of whether a further extension in the APP is required will return in due course albeit, in the absence of a large negative shock, not until well into 2017.

The day ahead in the euro area and US

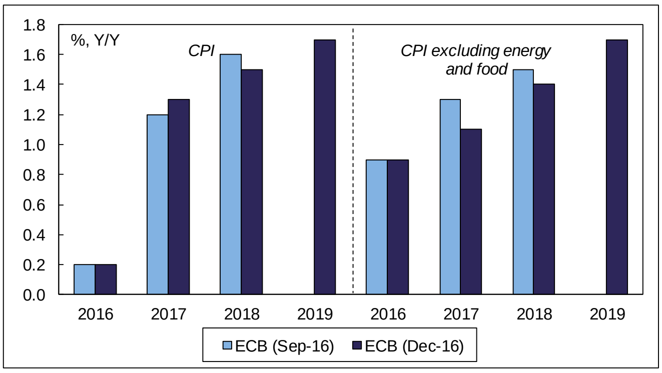
Tomorrow in the euro area brings the latest German trade report for October, along with labour cost figures for Q3. French industrial production data for October are also due. Given the weakness in yesterday's German IP figures risks to the expected increase of ½%M/M in French IP would appear skewed to the downside. But the near-term outlook looks more

ECB asset purchases



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

ECB: Inflation forecasts



Source: ECB and Daiwa Capital Markets Europe Ltd.

positive, at least according to today's Bank of France business sentiment survey, which showed the headline manufacturing indicator rising 2pts on the month to 101, back above the long-run average and equalling the near-five-year high hit in January. And with the services and construction sentiment indicators back at their long-run averages, the Bank of France assessed today's survey to be consistent with GDP growth of 0.4%Q/Q in Q4.

In the US, meanwhile, the week ends with the preliminary reading of the University of Michigan's consumer sentiment survey for December.

UK

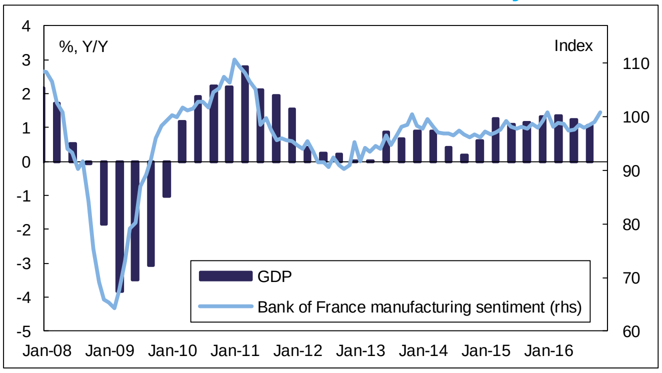
House prices growth continues to pick up

The latest RICS' Residential Market Survey showed that house price growth inched up further in November, with the net balance of 30% of respondents reporting higher prices, up from 23% the previous month and from an 18% average over the last six months. The upward pressure on prices continued to be driven by the lack of new supply, with the relevant indicator little changed at 0%, while new buyer enquiries rose modestly for a third successive month. Against this backdrop, market activity remained muted and price expectations remained positive, although both forward-looking price indicators for three- and twelve-month horizons eased by 4ppt to 14% and 40% respectively. Meanwhile, the indicator for house prices in London, which mirrors central London prices, rose to its highest level since April. However, it remained below zero, continuing to suggest a downward trajectory for prices in the capital, perhaps reflecting long-lasting effects of the Stamp Duty tax changes in recent years as well as Brexit uncertainty.

The day ahead in the UK

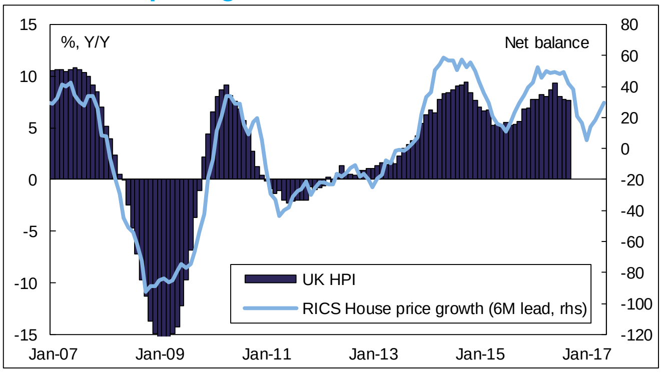
Tomorrow's trade data are expected to show that the headline trade deficit fell in October from £5.2bn to £4.3bn. Meanwhile, figures from the construction sector, also due tomorrow, will probably show that the level of output was up only slightly in October, to leave the annual pace of increase little changed at around 0%Y/Y.

France: Bank of France sentiment survey and GDP



Source: Thomson Reuters and Daiwa Capital Markets Europe Ltd.

UK: House price growth



Source: ONS, 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**
EMU	ECB refinancing rate %	Dec	**0.00**	*0.00*	0.00	**-**
	ECB deposit rate %	Dec	**-0.40**	*-0.40*	-0.40	**-**
	ECB asset purchase target €bn	Dec	**80**	*80*	80	**-**
France	Bank of France manufacturing sentiment indicator	Nov	**101**	100	99	**-**
UK	RICS house price balance %	Dec	**30**	26	23	**-**
	BoE corporate bond purchases £mn	Weekly	**4447**	-	3964	**-**

Country	Auction
- Nothing to report -	

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

Tomorrow's data releases

Economic data

Country	GMT	Release	Period	Market consensus/ *Daiwa forecast*	Previous
Germany	07:00	Trade balance €bn	Oct	22.0	24.2
	07:00	Current account balance €bn	Oct	22.0	24.2
	07:00	Imports (exports) M/M%	Oct	1.1 (0.9)	-0.7 (-1.2)
France	07:45	Industrial production M/M% (Y/Y%)	Oct	0.6 (-0.6)	-1.1 (-1.1)
	07:45	Manufacturing production M/M% (Y/Y%)	Oct	0.7 (0.1)	-1.1 (-0.9)
UK	09:30	Visible trade balance £bn	Oct	-11.8	-12.7
	09:30	Total trade balance £bn	Oct	-4.3	-5.2
	09:30	Construction output M/M% (Y/Y%)	Oct	0.2 (-0.1)	0.3 (0.2)

Auctions and events

Country	GMT	Auction / Event
EMU	15:15	ECB's Coeuré scheduled to speak in Paris

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

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