

# Euro wrap-up

## Overview

- Longer-dated Bunds made losses today as a significant upward surprise in the latest Spanish IP data further added to evidence of a strong end to the year for the euro area's industrial sector.
- Gilts made gains despite an upside surprise to the latest UK industrial output data.
- Tomorrow will bring euro area IP figures for November, along with the first estimate of full-year German GDP growth in 2016.

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### Daily bond market movements

Bond	Yield	Change*
BKO 0 12/18	-0.716	+0.012
OBL 0 10/21	-0.488	-0.015
DBR 0¼ 02/27	0.320	+0.035
UKT 1¼ 07/18	0.171	-0.037
UKT 3¾ 09/21	0.574	-0.029
UKT 1½ 07/26	1.339	-0.022

\*Change from close as at 4.30pm GMT.  
Source: Bloomberg

## Euro area

### Manufacturing surge in France and Spain in mid-Q4

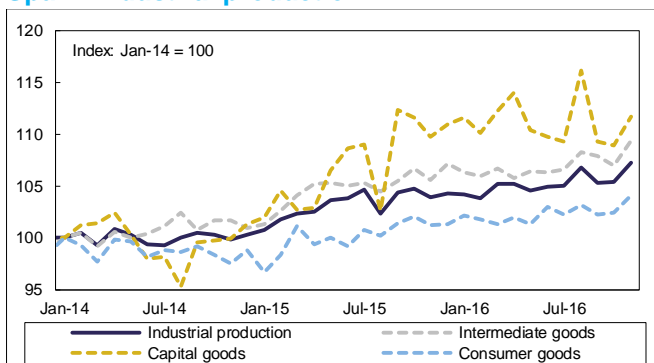
Germany's industrial production data reported earlier in the week broadly aligned with expectations, showing ongoing moderate expansion in the middle of the fourth quarter, with growth of 0.4%M/M a touch above the average rate in the year to date. But the equivalent releases from Spain and France (today and yesterday respectively) surprised significantly on the upside, signalling a strong end to last year for the euro area industrial sector. Indeed, Spanish IP rose 1.7%M/M, the strongest monthly pace since September 2015, to leave output more than 3% higher than a year ago. And manufacturing output was even firmer, up 2.2%M/M, with a notable pickup in production of capital and intermediate goods, by around 2½%M/M, while production of consumer durable goods was up by more than 4%M/M. So, on average over the first two months of Q4 output from the industrial sector was 0.8% higher than the average in Q3, suggesting that Spain's economy likely once again outperformed the other member states in the final quarter of 2016. Indeed, our own forecast for Spanish GDP growth in Q4 aligns with that of the Bank of Spain at 0.7%Q/Q, the same rate as in Q3.

In France, meanwhile, overall industrial production rose 2.2%M/M in November thanks to a jump of 2.3%M/M in manufacturing output, while firmer output from the energy sector was broadly offset by a slight dip in construction activity. The increase saw the annual rate of IP growth rise to 1.8%Y/Y, the highest in seven months, and on average over the first two months of Q4 output from the sector was 0.8% higher than the average in Q3. And with surveys pointing to a buoyant end to the year – e.g. the French manufacturing PMI rose in December to its highest since 2011 on the back of significant increases in the respective indices for output and new orders – fortunes for the sector in the euro area's second largest member state look to have taken a clear turn for the better. Certainly, our expectation for GDP growth in Q4 of 0.4%Q/Q, which would be the firmest since the first quarter of the year, seems subject to upside risks.

### The day ahead in the euro area and US

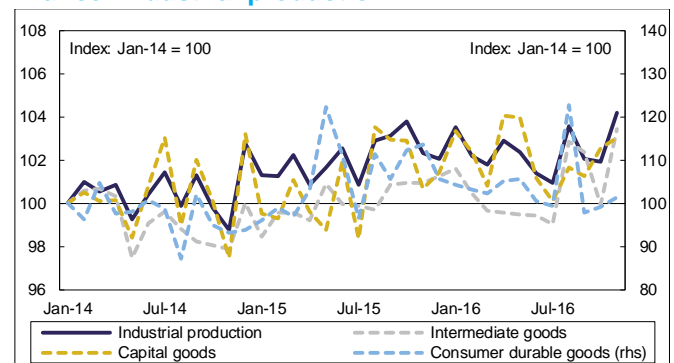
Focus now turns to tomorrow's release of the euro area industrial production figures for November. In the absence of a substantial decline in Italian output, which seems unlikely, euro area output is likely to have grown by more than 1%M/M, which would represent the first increase in three months. Thursday will also bring the first estimate of full-year German GDP growth in 2016, which is expected to pick up to 1.8% in unadjusted terms from 1.7% the previous year. The final estimate of French inflation in December, for which the flash estimate on the EU measure posted a rise of just 0.1ppt to 0.8%Y/Y, is also due. Most notably perhaps, tomorrow will also see the publication of the account of the ECB's monetary policy meeting at which the Governing Council extended the QE programme for a further nine months beyond end-March but at a slower pace of asset purchase. Finally, Italy will sell 3Y, 7Y and 20Y bonds.

### Spain: Industrial production



Source: Thomson Reuters and Daiwa Capital Markets Europe Ltd.

### France: Industrial production



Source: Thomson Reuters and Daiwa Capital Markets Europe Ltd.



In the US, aside from the usual weekly claims figures, Thursday sees the release of December's import and export price indices and the latest Federal budget statement.

## UK

### Services only driver of GDP growth in Q4

Following amendments to the ONS's release calendar, which now includes 'theme days' grouping similar economic data releases together, today saw the release of its short-term economic indicators, including trade, industrial production and construction output data. Most notably, the industrial production figures delivered an upward surprise showing that output increased by 2.1%M/M in November more than fully reversing the 1.1%M/M decrease in the previous month, while manufacturing output was up 1.3%M/M, with both figures representing the second-highest increase in more than four years. The increase in total output was mainly driven by the mining and quarrying sector, which increased by more than 8.0%M/M and accounted for around half of the growth, while pharmaceuticals contributed 0.6ppt to the monthly increase. However, that still left the October-November average level for industrial production about 0.5% lower compared to the Q3 average. And given that a significant component of today's upward surprise reflected large moves in particular sectors some payback, at least in the most volatile components, might be expected in December. Accordingly, the industrial sector is unlikely to have contributed positively to GDP growth in Q4.

Meanwhile, Q4 growth in construction output appears to have been similarly disappointing, with today's figures showing output down for a second consecutive month in November, by 0.2%M/M, to leave the average level in October and November down 0.5% compared to Q3. And an increase of around 1½%M/M is required in December to leave output flat in Q4. This seems unlikely, and therefore, construction is set to have remained a drag on GDP growth for a second successive quarter. Nevertheless, we continue to expect that the services sector once again provided the major contribution to GDP growth in Q4, to leave it at around ½%Q/Q.

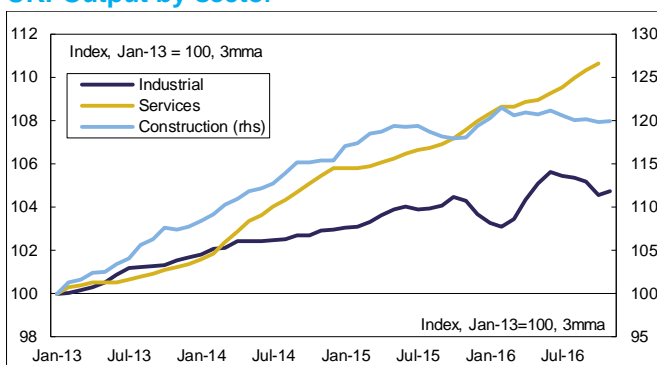
### Trade deficit surged in November

The strong manufacturing output and oil production figures in November were matched by higher goods exports, the value of which increased by 2.8%M/M, while in volume terms they rose by more than 5%M/M, representing one of the steepest jumps in recent history. However, that was not sufficiently strong to outpace import growth of 8.4%M/M and 9.3%M/M respectively, also driven mainly by manufactures and fuels. So the headline trade deficit rose from £1.5bn to £4.2bn, a level close to the upper end of the recent range and about £1bn higher than the average for 2016, with both the EU and non-EU goods trade balances deteriorating. Overall, there remains little convincing evidence that the post-referendum drop in sterling has yet to lead to a pick up in the underlying momentum of export growth, with the pace of 1.1%3M/3M in November, albeit the highest in five months, lower than import growth of 1.8%3M/3M that month.

### The day ahead in the UK

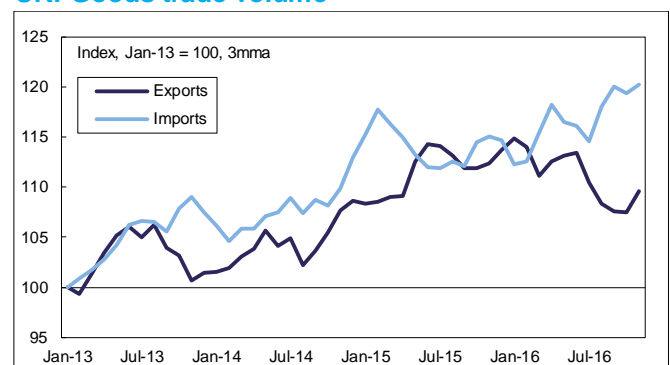
It should be a quiet day, with no new economic data in the UK.

#### UK: Output by sector












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

#### UK: Goods trade volume













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







## European calendar

Today's results						
Economic data						
Country	Release	Period	Actual	Market consensus/ <i>Daiwa forecast</i>	Previous	Revised
Spain	 Industrial production M/M% (Y/Y%)	Nov	<b>1.7 (3.2)</b>	0.4 (1.0)	0.1 (0.5)	- (0.6)
UK	 Visible trade balance £bn	Nov	<b>-12.2</b>	-11.2	-9.7	<b>-9.9</b>
	 Total trade balance £bn	Nov	<b>-4.2</b>	-3.5	-2.0	<b>-1.5</b>
	 Industrial production M/M% (Y/Y%)	Nov	<b>2.1 (2.0)</b>	1.0 (0.7)	-1.3 (-1.1)	<b>-1.1 (-0.9)</b>
	 Manufacturing production M/M% (Y/Y%)	Nov	<b>1.3 (1.2)</b>	0.5 (0.4)	-0.9 (-0.4)	<b>-1.0 (-0.5)</b>
	 Construction output M/M% (Y/Y%)	Nov	<b>-0.2 (1.5)</b>	0.2 (2.0)	-0.6 (0.7)	-
	 NIESR GDP 3M/3M%	Dec	<b>0.5</b>	0.5	0.4	<b>0.5</b>
Country	Auction					
Germany sold	 €4bn of 0.25% 2027 bonds (15-Feb-2027) at an average yield of 0.36%					
UK	 BoE APF operation purchased 1£bn of 7-15Y Gilts (3.08 cover ratio)					

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

Tomorrow's data releases						
Economic data						
Country	GMT	Release	Period	Market consensus/ <i>Daiwa forecast</i>	Previous	
EMU	 10:00	Industrial production M/M% (Y/Y%)	Nov	0.6 (1.6)	-0.1 (0.6)	
Germany	 09:00	GDP Y/Y%	2016	1.8	1.7	
France	 07:45	Final EU-harmonised CPI Y/Y%	Dec	0.8	0.7	
Italy	 09:00	Industrial production M/M% (Y/Y%)	Nov	0.2 (1.9)	0.0 (1.3)	
UK	 15:00	BoE corporate bond purchases £bn	Weekly	-	4.61	
Auctions and events						
Country	GMT	Auction / Event				
EMU	 12:30	ECB publishes the accounts of the Governing Council meeting held on 7-8 December 2016				
Italy	 10:00	Auction: To sell up to €3bn of 0.05% 2019 bonds (15-Oct-2019)				
	 10:00	Auction: To sell up to €1.5bn of 2.25% 2036 bonds (01-Sept-2036)				
	 10:00	Auction: To sell up to €2.75bn of 0.65% 2023 bonds (15-Oct-2023)				
UK	 10:30	Auction: To sell £2.25bn of 2% 2025 bonds (07-Sep-2025)				

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

Yesterday's results						
Economic data						
Country	Release	Period	Actual	Market consensus/ <i>Daiwa forecast</i>	Previous	Revised
France	 Industrial production M/M% (Y/Y%)	Nov	<b>2.2 (1.8)</b>	0.6 (-0.2)	-0.2 (-1.8)	-0.1 (-)
	 Manufacturing production M/M% (Y/Y%)	Nov	<b>2.3 (1.4)</b>	0.7 (-0.2)	-0.6 (-1.5)	-
UK	 BRC retail sales monitor, like-for-like Y/Y%	Dec	<b>1.0</b>	-	0.6	-
Country	Auction					
Germany sold	 €793mn of 0.1% 2026 index-linked bonds (15-Apr -2026) at an average yield of -1.07%					
UK sold	 £750mn of 0.125% 2046 index-linked bonds (22-Mar-2046) at an average yield of -1.532%					
	 BoE APF operation purchased £1bn 15Y+ Gilts (3.62 cover ratio)					

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

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