

Euro wrap-up

Overview

- Bunds were little changed despite the release of some further upbeat economic data.
- Gilts made gains on a quiet day for economic news from the UK.
- While tomorrow should be relatively uneventful, the coming week brings a speech by UK PM May supposedly providing detail on her Brexit policy (Tuesday) as well as the ECB's latest monetary policy meeting (Thursday). The dataflow will include UK and final euro area inflation figures.

Chris Scicluna
+44 20 7597 8326

Mantas Vanagas
+44 20 7597 8318

Daily bond market movements

Bond	Yield	Change*
BKO 0 12/18	-0.715	-
OBL 0 10/21	-0.483	-0.003
DBR 0 08/26	0.313	-0.014
UKT 1¼ 07/18	0.165	-0.010
UKT 3¾ 09/21	0.556	-0.030
UKT 1½ 07/26	1.303	-0.042

*Change from close as at 4.00pm GMT.
Source: Bloomberg

Euro area

Industrial production leaps in November

Following the release of data from various member states, it had already been clear that euro area industrial production picked up in November. In the event, IP growth was stronger than expected, up 1.5%M/M, the most since August, taking the annual rate to 3.2%Y/Y, the highest since January. Production of manufactured goods and energy alike grew close to the aggregate rate, with growth in output of non-durable consumer goods and intermediate goods strongest while production of capital goods and consumer durables was more subdued. Growth in production was also widely spread across the member states, with Portugal and Greece the only to report declines. Following a slight gain in October, on average over the first two months of Q4 euro area manufacturing output was 0.7% higher than the third-quarter average. So, the sector looks bound to have made a positive contribution to euro area GDP growth for the second successive quarter in Q4. And with surveys suggesting that sentiment in the sector is at its highest since 2011, and that order books are the most plentiful in more than five years too, weather-permitting we expect manufacturing production to provide further support to GDP growth in the current quarter too.

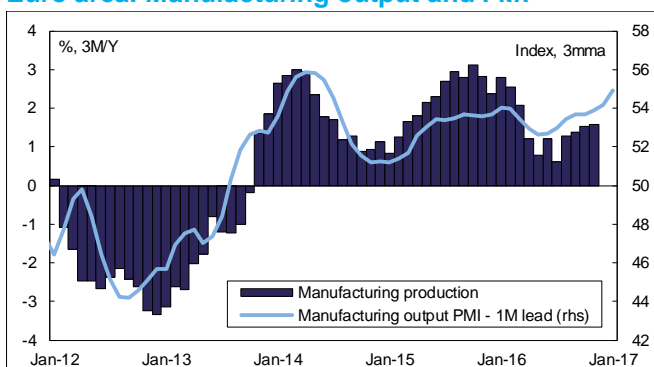
German growth domestically-driven in 2016

The first estimate of full-year German growth in 2016 confirmed a slight acceleration from recent years, up to 1.9%Y/Y (1.8%Y/Y calendar-adjusted) from 1.7%Y/Y in 2015 and the strongest since 2011. And while Germany's external surpluses remained huge with the current account balance likely to have reached about 9% of GDP, domestic demand more than fully accounted for the expansion in GDP. Indeed, each component of domestic final expenditure rose, with a notable acceleration in government consumption (up more than 4%Y/Y) even though the general government budget surplus was little changed at 0.6% of GDP. Additionally, private consumption growth remained steady at the same 2.0%Y/Y pace of the previous year, while gross fixed investment rose for the third consecutive year (up 2.5%Y/Y). With growth of imports outpacing that of exports, net trade subtracted from GDP growth for the first year in three. These initial full-year data add to evidence of an acceleration in German GDP in Q4, which looks set to have reached at least 0.5%Q/Q (data due 14 February).

ECB account shines a little extra light on policy debate

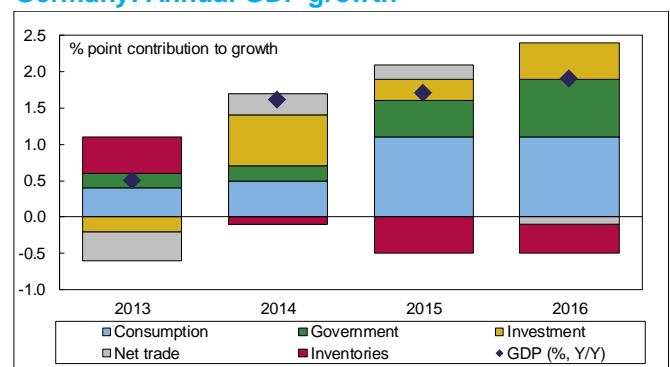
Since the ECB's December policy meeting, when the QE programme was extended by a further nine months from end-March to effectively pre-set policy for the whole year, the euro area dataflow has improved significantly, with economic sentiment reviving and inflation taking a notable step up. But while the upside risks to the economic outlook appear to have increased,

Euro area: Manufacturing output and PMI



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

Germany: Annual GDP growth



Source: Federal Statistical Office and Daiwa Capital Markets Europe Ltd.



the account of that meeting gave little insight into what the ECB might be prepared to do should those positive trends further strengthen significantly. Instead, it made clear that the Governing Council remained perturbed by the lack of an upwards trend in core inflation, which it attributed partly to labour market developments, and was still firmly alive to the downside risks to the economic outlook. The decision to slow the monthly pace of asset purchases to €60bn from April was not unanimous, however, although the majority considered it to be consistent with an improving economic outlook while also providing scope to respond to any renewed deterioration in conditions – by increasing the monthly purchase rate back up to €80bn – should the need arise. The account also confirmed that legal obstacles, as well as communication and reputational concerns, led to the decision not to increase the issue and issuer limits on the purchases, explaining why it instead plumped for removing the -0.40% yield floor. Looking ahead, despite the better recent data, we fully expect the ECB to carry out its QE plans in full this year. But if events pan out as forecast, or even exceed expectations, in the autumn Draghi should at least be ready to signal his intention to taper further the asset purchases from the start of 2018. And over the near term, as a sign that the debate surrounding its monetary policy has shifted, the ECB might well decide to amend its forward guidance, retracting its signal that its policy rates might be cut further.

The week ahead in the euro area and US

With tomorrow set to be relatively uneventful for economic data from the euro area, the main event of the coming week in the euro area will be the ECB's Governing Council meeting on Thursday. However, despite the recent notable improvement in the economic data, after policy was effectively pre-set for 2017 at December's meeting there seems unlikely to be a notable shift just yet. In due course, however, as a sign that the debate surrounding its monetary policy has shifted, the ECB might well decide to amend its forward guidance, retracting its signal that its policy rates might be cut further. But updated economic forecasts would seem to be required before any such change might be made.

Meanwhile, there seems unlikely to be any show-stopping economic data from the euro area in the coming week. However, new releases due include November's trade and balance of payments figures (Monday and Thursday respectively), as well as the German ZEW investor survey for January, euro area new car registrations numbers for December, and latest ECB quarterly bank lending survey (Tuesday). In addition, euro area construction data for November are due on Wednesday alongside the final euro area CPI figures for December, for which the flash headline estimate rose 0.5ppt in December to 1.1%Y/Y, the highest since September 2013 and the preliminary core measure rose 0.1ppt to 0.9%Y/Y.

In the US, tomorrow is set to be busier for economic data, with December's retail sales and producer price numbers due alongside the preliminary University of Michigan consumer confidence survey. In contrast, the economic calendar for the start of the coming week is light with markets closed on Monday for Martin Luther King Day and just the Empire Manufacturing survey due on Tuesday. The most notable new economic data will come on Wednesday with CPI and IP figures for December. Consumer prices are expected to have posted the fifth consecutive monthly increase on the back of higher energy prices, to leave the headline annual rate of CPI rising above 2%Y/Y for the first time since mid-2014. Meanwhile, industrial output is expected to have risen by around ½%M/M to more than fully reverse the decline in November. Wednesday will also bring the latest capital inflows data for November and NAHB housing index for January. Of course, all eyes at the end of the week will be on the inauguration of incoming President Trump. Friday will also see Fed Chair Yellen and FOMC voting member Harker speak publicly.

UK

The week ahead in the UK






After a quiet day today for economic news from the UK, tomorrow brings the BoE Credit Conditions survey for Q4. Global interest rates increased significantly at the end of the last year, and the survey will show to what extent that had bearing on lending conditions in the UK. On the policy front, the newest MPC member Michael Saunders is scheduled to speak. Meanwhile, the coming week is set to be particularly busy, with inflation, labour market, and retail sales figures all due for release. However, the most notable event might well be the speech by Prime Minister May on her Brexit policy scheduled for Tuesday. Meanwhile, the CPI data, out on Tuesday, are set to show that inflation continued to rise sharply at the end of the last year, thanks to higher energy prices and the drop in sterling. We expect the headline rate to have increased by 0.2ppt to 1.4%Y/Y, which would be the highest level since August 2014, while the core rate might also inch higher to 1.5%Y/Y. The messages from Wednesday's release of the latest labour market indicators are likely to be mixed, with the headline three-month employment growth set to have fallen sharply in November despite an anticipated increase in the employment level that month. The unemployment rate, meanwhile, is likely to have remained unchanged at a multi-year low of 4.8%, while wage growth is expected to have accelerated from 2.5%3M/Y in October. Meanwhile, the week should end on a positive note: the release of the figures from the retail sector on Friday will most likely confirm that sales continued growing rapidly in December, having risen at a near-6%Y/Y pace in November. Among other notable economic events the coming week, the ONS House Price index and the RICS Residential Market survey are released on Tuesday and Thursday respectively, while Mark Carney is due to speak on Monday evening.





The next edition of Euro wrap-up will be published on 16 January 2017.

European calendar

Today's results

Economic data


Country	Release	Period	Actual	Market consensus/ <i>Daiwa forecast</i>	Previous	Revised
EMU	 Industrial production M/M% (Y/Y%)	Nov	1.5 (3.2)	0.6 (1.6)	-0.1 (0.6)	0.1 (0.8)
Germany	 GDP Y/Y%	2016	1.9	1.8	1.7	-
France	 Final EU-harmonised CPI Y/Y%	Dec	0.8	0.8	0.7	-
Italy	 Industrial production M/M% (Y/Y%)	Nov	0.7 (3.2)	0.2 (1.9)	0.0 (1.3)	0.1 (-)
UK	 BoE corporate bond purchases £bn	Weekly	4.91	-	4.61	-


Country	Auction
Italy sold	 €3bn of 0.05% 2019 bonds (15-Oct-2019) at an average yield of 0.06%
	 €1.5bn of 2.25% 2036 bonds (01-Sept-2036) at an average yield of 2.53%
	 €2.75bn of 0.65% 2023 bonds (15-Oct-2023) at an average yield of 1.15%
UK sold	 £2.25bn of 2% 2025 bonds (07-Sep-2025) at an average yield of 1.158%

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
Spain	 08:00	Final EU-harmonised CPI Y/Y%	Dec	1.4	0.5

Country	GMT	Auction / Event
Italy	-	Sovereign debt to be rated by DBRS
UK	 09:30	BoE's Saunders scheduled to speak in London
















Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

Coming week's data calendar

Key data releases						
Country		GMT	Release	Period	Market consensus/ <i>Daiwa forecast</i>	Previous
Monday 16 January 2017						
EMU		10:00	Trade balance €bn	Nov	-	19.7
		14:45	ECB public sector asset purchases €bn	Weekly	<u>16.0</u>	11.0
Italy		09:00	Final EU-harmonised CPI Y/Y%	Dec	-	0.1
UK		00:01	Rightmove house price index M/M% (Y/Y%)	Jan	-	-2.1 (3.4)
Tuesday 17 January 2017						
EMU		07:00	EU27 new car registrations	Dec	-	5.8
		10:00	ZEW expectations balance	Jan	-	18.1
Germany		10:00	ZEW current assessment balance (expectations)	Jan	-	63.5 (13.8)
Italy		09:00	Trade balance €bn	Nov	-	4.3
UK		09:30	CPI (core CPI) inflation Y/Y%	Dec	<u>1.4 (1.5)</u>	1.2 (1.4)
		09:30	House price index Y/Y%	Nov	-	6.9
Wednesday 18 January 2017						
EMU		10:00	Construction output M/M% (Y/Y%)	Nov	-	0.8 (2.2)
		10:00	Final CPI (core CPI) Y/Y%	Dec	<u>1.1 (0.9)</u>	0.6 (0.8)
Germany		07:00	Final EU-harmonised CPI Y/Y%	Dec	<u>1.7</u>	0.7
UK		09:30	Average earnings incl. bonuses (excl. bonuses) 3M/Y%	Nov	<u>2.7 (2.7)</u>	2.5 (2.6)
		09:30	ILO unemployment rate 3M%	Nov	<u>4.8</u>	4.8
		09:30	Employment change 3M/3M '000s	Nov	<u>-120</u>	-6
		09:30	Claimant count rate % (change 000s)	Dec	-	2.3 (2.4)
Thursday 19 January 2017						
EMU		09:00	Current account balance €bn	Nov	-	28.4
		12:45	ECB refinancing rate %	Jan	<u>0.00</u>	0.00
		12:45	ECB deposit rate %	Jan	<u>-0.40</u>	-0.40
Italy		09:30	Current account balance €bn	Nov	-	6.1
Spain		09:00	Trade balance €bn	Nov	-	-1.8
UK		00:01	RICS house price balance %	Dec	-	30
		15:00	BoE corporate bond purchases £bn	Weekly	-	4.91
Friday 20 January 2017						
UK		09:30	Retail sales excluding petrol M/M% (Y/Y%)	Dec	-	0.5 (6.6)
		09:30	Retail sales including petrol M/M% (Y/Y%)	Dec	-	0.2 (5.9)

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

Coming week's events/auctions calendar

Key events & auctions			
Country		GMT	Event / Auction
Monday 16 January 2017			
EMU		15:30	ECB's Praet scheduled to speak in Paris
UK		14:50	BoE APF operation: To purchase 3-7Y Gilts
		18:30	BoE's Carney scheduled to speak at London School of Economics
Tuesday 17 January 2017			
EMU		09.00	ECB publishes the Euro Area Bank Lending Survey
Germany		10:30	Auction: To sell €5bn of 0% 2018 bonds (14-Dec-2018)
UK		-	PM May to deliver speech on the Government's Brexit policy
		14:50	BoE APF operation: To purchase 15Y+ Gilts
Wednesday 18 January 2017			
UK		10:30	Auction: To sell £2.75bn of 0.5% 2022 bonds (22-Jan-2022)
		14:50	BoE APF operation: To purchase 7-15Y Gilts
Thursday 19 January 2017			
EMU		12:45	ECB Governing Council policy announcement
		13:30	ECB's Draghi to deliver post meeting press conference
France		09:50	Auction: To sell bonds
		10:50	Auction: To sell index-linked bonds
Spain		09:30	Auction: To sell bonds
Friday 20 January 2017			
EMU		09.00	ECB publishes the Survey of Professional Forecasters

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

Access our research blog at:

<http://www.uk.daiwacm.com/research-zone/research-blog>



Follow us

[@DaiwaEurope](https://twitter.com/DaiwaEurope)

This research report is produced by Daiwa Securities Co. Ltd., and/or its affiliates and is distributed by Daiwa Capital Markets Europe Limited in the European Union, Iceland, Liechtenstein, Norway and Switzerland. Daiwa Capital Markets Europe Limited is authorised and regulated by The Financial Conduct Authority and is a member of the London Stock Exchange and Eurex Exchange. Daiwa Capital Markets Europe Limited and its affiliates may, from time to time, to the extent permitted by law, participate or invest in other financing transactions with the issuers of the securities referred to herein (the "Securities"), perform services for or solicit business from such issuers, and/or have a position or effect transactions in the Securities or options thereof and/or may have acted as an underwriter during the past twelve months for the issuer of such securities. In addition, employees of Daiwa Capital Markets Europe Limited and its affiliates may have positions and effect transactions in such securities or options and may serve as Directors of such issuers. Daiwa Capital Markets Europe Limited may, to the extent permitted by applicable UK law and other applicable law or regulation, effect transactions in the Securities before this material is published to recipients.

This publication is intended for investors who are not Retail Clients in the United Kingdom within the meaning of the Rules of the FCA and should not therefore be distributed to such Retail Clients in the United Kingdom. Should you enter into investment business with Daiwa Capital Markets Europe's affiliates outside the United Kingdom, we are obliged to advise that the protection afforded by the United Kingdom regulatory system may not apply; in particular, the benefits of the Financial Services Compensation Scheme may not be available.

Daiwa Capital Markets Europe Limited has in place organisational arrangements for the prevention and avoidance of conflicts of interest. Our conflict management policy is available at <http://www.uk.daiwacm.com/about-us/corporate-governance-regulatory>. Regulatory disclosures of investment banking relationships are available at <https://daiwa3.bluematrix.com/sellside/Disclosures.action>.