

# Euro wrap-up

## Overview

- Bunds made modest losses as the ECB predictably left policy unchanged.
- Gilts followed USTs lower despite a survey signalling a possible softening of momentum in the UK housing market.
- Friday brings UK retail sales figures for December as well as the latest ECB survey of professional forecasts.

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### Daily bond market movements

Bond	Yield	Change*
BKO 0 12/18	-0.699	+0.018
OBL 0 10/21	-0.451	+0.016
DBR 0 08/26	0.374	+0.019
UKT 1¼ 07/18	0.189	+0.005
UKT 3¼ 09/21	0.602	+0.042
UKT 1½ 07/26	1.394	+0.058

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

## Euro area

### ECB has little new to say on policy

There were no surprises when the ECB's latest policy meeting concluded today. Policy-wise, the Governing Council predictably, and with unanimity, left unchanged its interest rates and the main parameters of its asset purchase programme. And, looking ahead, the Governing Council also left intact its forward guidance, expecting its interest rates to remain at current levels well beyond the end of the asset purchase programme, and leaving the door open to a further rate cut or an increase in QE should conditions demand. There was, however, some additional information on policy, with the ECB clarifying that only public sector bonds (and not covered bonds or asset-backed securities) may now be bought at yields below the deposit rate (-0.40%). And stating that priority will be given to buying bonds with yields above the deposit rate, the Governing Council also confirmed that the amount of purchases of bonds yielding less than -0.40% will vary according to the member state concerned and will also likely vary over time.

### Draghi remains predictably dovish

Consistent with the Governing Council's forward guidance, Draghi maintained a dovish tone in his press conference. While he acknowledged that inflation in the present quarter and in the second quarter of the year will now exceed the ECB's forecast, he emphasised that this was principally due to the higher-than-expected oil price and repeated that there are no signs yet of the convincing upward trend in underlying inflation that is required for it to consider re-evaluating policy. In addition, despite recent upbeat economic data and surveys, due to global factors the Governing Council continued to judge that the risks to the outlook for economic growth remain skewed to the downside. So, it was no surprise that Draghi also confirmed that the Governing Council had not discussed whether it might in due course reduce further the degree of monetary accommodation if the dataflow starts to surprise consistently on the upside. But, of course, that doesn't mean that the ECB wouldn't eventually change to a more hawkish course if it eventually judged it appropriate to do so. And so, while we still expect the ECB to stick to its guns and carry out its QE plans in full throughout 2017, in the second half of the year Draghi will likely signal his intention to reduce further the asset purchases from the start of 2018, perhaps eventually to zero. And over the near term, as a sign that the debate surrounding its monetary policy has shifted, the ECB ought to amend its forward guidance, retracting its signal that its policy rates might be cut further.

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

In the euro area, tomorrow will bring the release of the ECB's latest survey of professional forecasts, which is used by officials to monitor inflation expectations. In addition, Friday will bring German PPI figures for December, which are likely to point to a notable step up in pipeline pressures at the end of last year.

Of course, all eyes in the US tomorrow will be on the inauguration of incoming President Trump. Friday will also see FOMC voting member Harker speak publicly.

## UK

### More challenging year for the housing market?

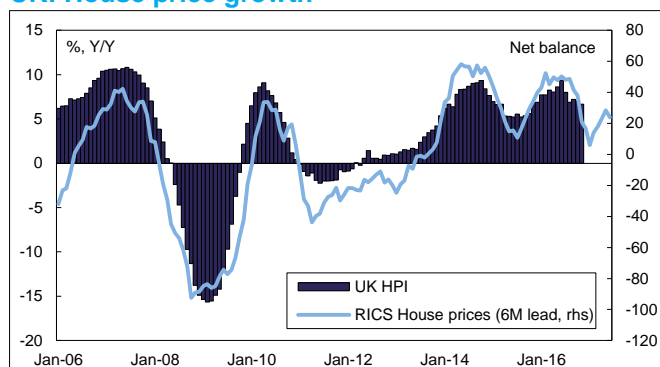
Today's release of the RICS Residential Market Survey showed that upward pressure on house prices eased slightly in December, with the net balance of 24% of respondents reporting higher prices at the end of last year, down from 29% the previous month. London was the only area where prices were reportedly falling, with the relevant indicator remaining below zero for a tenth successive month, and expectations for a recovery over the coming year remained relatively subdued. In terms of activity, having previously hinted at a gradual recovery in market transactions, the survey reported that the number of agreed sales moved sideways in December. And with the near-term price expectation index having fallen to a four-month low against the backdrop of weaker economic momentum expected this year, the housing market outlook for 2017 appears to be more challenging compared to recent years, particularly in the capital where affordability is stretched. However, stronger growth in other regions should provide support, likely keeping aggregate UK house price growth above the pace of increase in incomes.



## The day ahead in the UK

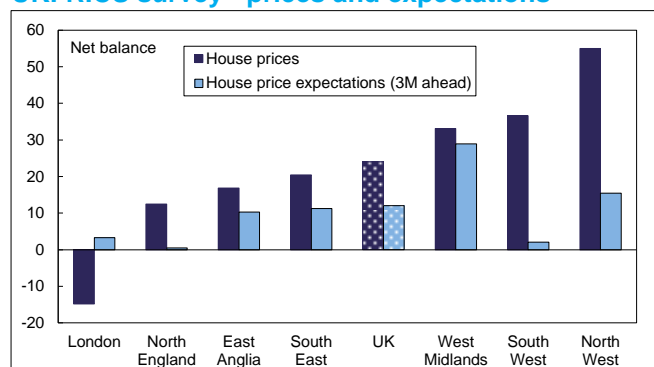
With recent surveys reporting that retail activity increased at the end of the year, tomorrow's official retail sales data should also show that growth picked up further in December, having been only a touch below 6%Y/Y in November.

### UK: House price growth



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

### UK: RICS survey - prices and expectations



Source: RICS, 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	Current account balance €bn	Nov	<b>36.1</b>	-	28.4	<b>28.3</b>
	ECB refinancing rate %	Jan	<b>0.00</b>	<u>0.00</u>	0.00	-
	ECB deposit rate %	Jan	<b>-0.40</b>	<u>-0.40</u>	-0.40	-
	ECB asset purchase target €bn	Jan	<b>80</b>	80	80	-
Italy	Current account balance €bn	Nov	<b>4.6</b>	-	6.1	-
Spain	Trade balance €bn	Nov	<b>-1.2</b>	-	-1.8	-
UK	RICS house price balance %	Dec	<b>24</b>	30	30	<b>29</b>
	BoE corporate bond purchases £bn	Weekly	<b>5.29</b>	-	4.91	-



#### Country Auction

France sold		€4.8bn of 0% 2020 bonds (25-Feb-2020) at an average yield of -0.43%
		€3.1bn of 0% 2022 bonds (25-May-2022) at an average yield of -0.04%
		€950mn of 0.1% 2021 index-linked bonds (25-Jul-2021) at an average yield of -1.38%
		€750mn of 1.85% 2027 index-linked bonds (25-Jul-2027) at an average yield of -0.51%
		€295mn of 0.1% 2047 index-linked bonds (25-Jul-2047) at an average yield of 0.17%
Spain sold		€655mn of 0.25% 2019 bonds (31-Jan-2019) at an average yield of -0.234%
		€966mn of 4.4% 2023 bonds (31-Oct-2023) at an average yield of 0.769%
		€3.2bn of 0.4% 2022 bonds (30-Apr-2022) at an average yield of 0.399%


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
UK		09:30	Retail sales excluding petrol M/M% (Y/Y%)	Dec	-0.4 (7.5)	0.5 (6.6)
		09:30	Retail sales including petrol M/M% (Y/Y%)	Dec	-0.1 (7.2)	0.2 (5.9)

**Auctions and events**

Country		GMT	Auction / Event
EMU		09.00	ECB publishes the Survey of Professional Forecasters

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

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