

Euro wrap-up

Overview

- Bunds made modest gains despite some further upbeat survey results as political uncertainty remained a key theme in several euro area member states.
- Gilts also followed USTs higher on a quiet day for UK economic news.
- The coming week brings the first estimates of euro area Q4 GDP and January inflation. In the UK, meanwhile, focus will be on Thursday's BoE policy announcement and accompanying Inflation Report.

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Daily bond market movements

Bond	Yield	Change*
BKO 0 12/18	-0.663	-0.014
OBL 0 10/21	-0.365	-0.005
DBR 0¼ 12/27	0.462	-0.022
UKT 1¼ 07/18	0.157	-0.030
UKT 3¼ 09/21	0.631	-0.030
UKT 1½ 07/26	1.472	-0.044

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

Euro area

French households increasingly upbeat, despite political uncertainty

Political risks continue to cloud the horizon in the euro area with further twists and turns ahead of key elections this year. In France, for example, the ongoing 'Penelopegate' affair associated with questionable payments to the wife of Presidential election favourite François Fillon, which is now being investigated by a public prosecutor, continues to build a head of steam and adds further to uncertainty about the eventual outcome of the contest. Indeed, last night Fillon stated that he would withdraw his candidacy if preliminary charges were brought against him, while a survey published today suggested that more than 60% of voters now take a dim view of him. But while investor unease about the election outcome has been reflected in recent underperformance of French government bonds relative to Bunds and Spanish bonds, it remains to be seen whether households and businesses will similarly become more cautious. Certainly, while admittedly it was conducted before the allegations against Fillon and his wife were first published, according to the latest French consumer confidence survey households remain unruffled, with the headline sentiment index rising in January back to the long-run average for the first time since 2007. Within the detail, survey respondents were more optimistic about the outlook for their future personal financial situation, while their concerns about unemployment fell to the lowest since mid-2008. And, as was suggested by the equivalent German survey published earlier this week, consumers' perceptions and expectations about inflation have risen, something that might persuade some to bring forward purchases of big-ticket items before price rises start to bite.

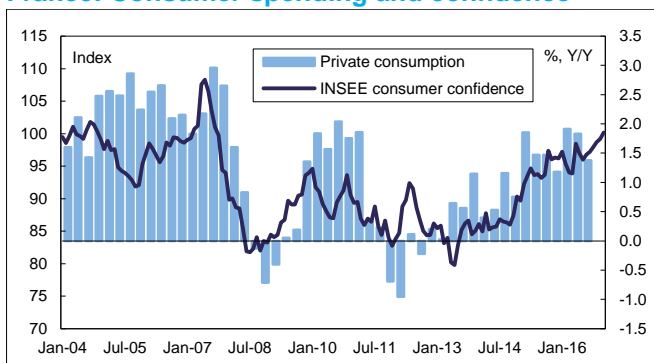
Italian economic sentiment firmer too

Of course, with renewed speculation regarding the possibility of an early general election, uncertainty surrounding the near-term Italian political outlook has also increased. Like in France, however, the latest Italian economic sentiment survey pointed to an improvement in confidence at the start of the year, albeit one concentrated only in selected business sectors. Most notably, manufacturers were reportedly particularly upbeat, with an increase in the respective index to a fifteen-month high. And services and construction firms were also more optimistic than of late. However, retailers were more pessimistic, and that tallied with a deterioration in consumer confidence too. Looking at the survey in the round, overall sentiment appears to have been trending broadly sideways over recent months at levels below the multi-year highs reached a year or so ago, albeit still above the long-run average.

More political noise from the Netherlands

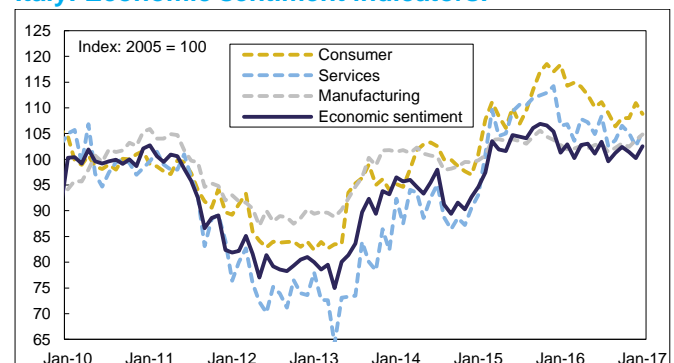
In the Netherlands, meanwhile, yesterday evening brought the resignation of Justice Minister Ard van der Steur, a member of PM Mark Rutte's Liberal Party (VVD), in response to long-running allegations that he had been involved in misinforming the national parliament on a murky affair involving payments to a convicted drug trafficker. Ahead of the general election on 15

France: Consumer spending and confidence



Source: Thomson Reuters and Daiwa Capital Markets Europe Ltd.

Italy: Economic sentiment indicators:



Source: Thomson Reuters and Daiwa Capital Markets Europe Ltd.



March, the affair heaps pressure on Rutte, not least because of suggestions that he too might have questions to answer about his role at the time concerned. It does not, however, change our view that a coalition government of several mainstream, pro-European parties – probably including VVD – will subsequently be formed after the election to keep out of office the far-right nationalist Freedom Party (PVV), which will win by far the largest number of seats. But it underscores the likelihood that the coalition negotiations will be heated and drawn out, leaving a vacuum in policymaking for several weeks and perhaps months after the election. And the chances of Rutte remaining Prime Minister after the election have also likely diminished.

A pickup in lending to the corporate sector

At the euro area level, December's bank lending data confirmed the expected further pickup in growth in credit to the private sector at year-end in response to more favourable demand- and supply-side developments. Growth in total loans to the private sector on an adjusted basis rose 0.1ppt to 2.3%Y/Y, with the vigour in the latest month associated particularly with lending to non-financial corporations, which rose 0.2ppt to 2.3%Y/Y, the strongest rate since 2009, thanks to the biggest monthly net issuance of new loans in ten months. The increase was driven by loans with a maturity of more than five years, while the value of newly issued short-dated loans fell notably. Benefiting from increased lending for house purchase and consumer credit, growth in loans to households was also firmer, up to 2.0%Y/Y, the strongest since 2011. And, with the ECB's recent bank lending survey having signalled further increases in demand for loans across all categories as well as a continued easing of credit terms and conditions, we expect the gradual uptrend in credit expansion to be maintained in the coming quarter too.

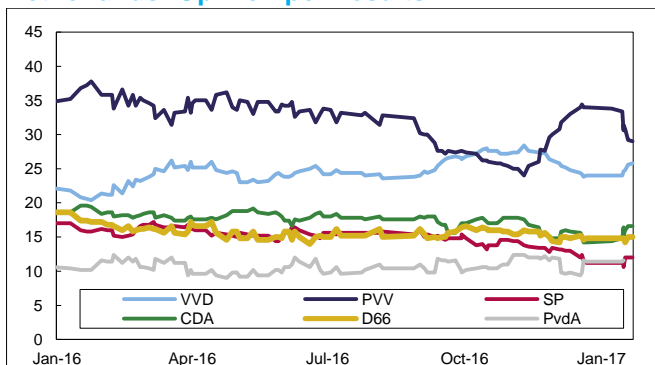
The week ahead in the euro area and US

The coming week brings several top-tier data, including the first estimates of euro area GDP growth in Q416 and euro area inflation in January, both of which are due on Tuesday. In particular, we expect GDP to have risen 0.5%Q/Q, which would be the firmest pace since Q116. Meanwhile, the flash estimate of CPI looks set to rise 0.4ppt to 1.5%Y/Y, which would be the highest since July 2013, albeit with the core measure remaining unchanged at 0.9%Y/Y. The preliminary estimate of German inflation, due Monday, should provide a further guide as to what to expect from the euro area figures. Among other notable releases, the Commission's economic sentiment survey for January – which typically provides the most reliable guide to economic activity – is also due on Monday and seems likely to signal ongoing steady expansion in the first quarter. In addition, German retail sales figures for December and euro area unemployment data for December are due on Tuesday, and the final PMIs for January from the manufacturing sector (Wednesday) and services (Friday) are also scheduled for release.

On the political front, the coming weekend brings the second round of the Presidential primary for the French Socialist Party, which will see the anti-establishment left-wing candidate, former Education Minister Benoît Hamon, up against the centrist former Prime Minister Manuel Valls. Following his victory in the first round, Hamon looks set to win this weekend. However, whoever is victorious, neither candidate would appear to have much hope of qualifying for the second round of the Presidential election in May. Meanwhile, in the markets, Italy will sell a range of bonds on Monday, Germany will sell 5Y Bunds on Wednesday, and France and Spain will sell a range of bonds on Thursday.

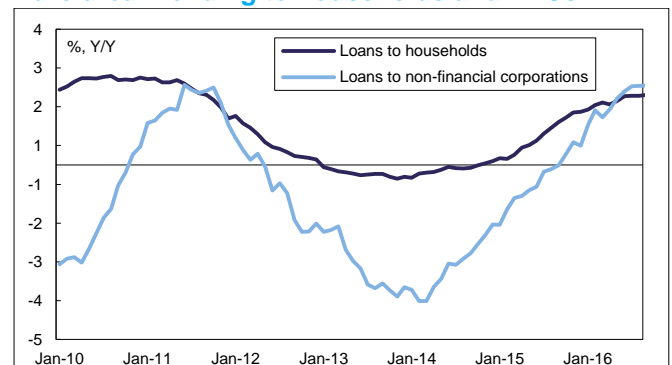
It will be a busy week in the US too, not least with the conclusion of the Fed's latest FOMC meeting on Wednesday. With Fed Chair Yellen among others having recently reiterated that the pace of future tightening will remain gradual and just six weeks having passed since the Committee last raised interest rates, the range for the Fed Funds Rate is widely anticipated to be left unchanged at 0.5-0.75%. But given the more hawkish comments by various FOMC members over recent months, the post-meeting statement will no doubt be closely watched for insights into the near-term policy outlook.

Netherlands: Opinion poll results*



*VVD is the centre-right Liberal People's Party for Freedom and Democracy. PVV is the far-right populist Party for Freedom. SP is the left-wing Socialist Party. CDA is the centrist Christian Democrats. D66 is a centre-left party. PvdA is the centre-left Labour party. VVD and PvdA are currently in coalition government. Source: Various polling organisations and Daiwa Capital Markets Europe Ltd

Euro area: Lending to households and NFCs



Source: Thomson Reuters and Daiwa Capital Markets Europe Ltd.






Among the most noteworthy data releases in the coming week, Monday will bring December's personal income and spending figures as well as the associated deflators, which are closely watched by the Fed. January sentiment indicators due include the Conference Board's consumer index (Tuesday), the manufacturing ISM (Wednesday) and non-manufacturing ISM (Friday). Most attention will inevitably be on Friday's labour market report, which is expected to show that non-farm payrolls increased by about 170k in January, a touch below the 2016 average, to leave the unemployment rate unchanged at 4.7%. Meanwhile, average hourly earnings growth is expected to have slowed very slightly to 2.8%Y/Y. There are no UST bond auctions scheduled in the coming week.

UK

The week ahead in the UK











































With UK GDP growth remaining firm in the second half of the year, a sharp pick-up in inflation towards the end of the year saw expectations that the MPC might eventually tighten monetary policy rise. However, we think that economy will slow notably over the coming quarters, and therefore, the MPC will be prepared to look through the rise in inflation, which we forecast should reach around 3%Y/Y by the end of this year. Certainly, we do not think that the MPC will announce any changes to its policy this coming Thursday. Indeed, we don't expect it to change Bank Rate at all during 2017. Nevertheless, we expect that next week's policy statement will carry a more hawkish tone, and the possibility that one or two MPC members vote to raise rates cannot be discounted entirely. The Inflation Report, meanwhile, seems bound to contain an upward revision to the BoE's growth forecast for the near term, but with Theresa May having announced plans to take the UK out of the single market and the EU's customs union, the BoE will most likely remain downbeat about longer-term growth prospects. Data-wise, the focus in the coming week will be on the January PMIs on Wednesday, Thursday and Friday. Having risen notably in recent months, the indices from all three sectors are expected to show that momentum moderated slightly at the start of the year. Meanwhile, the BoE lending figures release and the GfK consumer confidence survey, both of which are out on Tuesday, are also worth watching.

European calendar

Today's results							
Economic data							
Country	Release	Period	Actual	Market consensus/ Daiwa forecast	Previous	Revised	
EMU	 M3 money supply Y/Y%	Dec	5.0	4.9	4.8	-	
France	 Consumer confidence survey	Jan	100	100	99	-	
Italy	 Consumer confidence indicator	Jan	108.8	110.0	111.1	110.9	
	 Manufacturing (economic) confidence	Jan	104.8 (102.5)	103.3 (-)	103.5 (100.3)	103.7 (100.2)	
Spain	 Retail sales Y/Y%	Dec	2.9	3.2	3.3	3.2	
Country	Auction						
- Nothing to report -							




















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 30 January 2017						
EMU		10:00	Economic sentiment indicator	Jan	107.8	107.8
		10:00	Services (industrial) sentiment	Jan	12.7 (0.2)	12.9 (0.1)
		10:00	Final consumer confidence	Jan	-4.9	-5.1
		14:45	ECB public sector asset purchases €bn	Weekly	<u>17.5</u>	18.5
Germany		13:00	Preliminary EU-harmonised CPI Y/Y%	Jan	2.0	1.7
Spain		08:00	GDP – 1st release Q/Q% (Y/Y%)	Q4	<u>0.7 (3.1)</u>	0.7 (3.2)
Tuesday 31 January 2017						
EMU		10:00	GDP – 1st release Q/Q% (Y/Y%)	Q4	<u>0.5 (1.7)</u>	0.3 (1.7)
		10:00	Unemployment rate %	Dec	<u>9.8</u>	9.8
		10:00	Flash CPI estimate Y/Y%	Jan	1.5	1.1
		10:00	Flash core CPI estimate Y/Y%	Jan	0.9	0.9
Germany		07:00	Retail sales M/M% (Y/Y%)	Dec	0.6 (0.4)	-1.7 (3.2)
		08:55	Unemployment change `000s (rate %)	Jan	-5 (6.0)	-17 (6.0)
France		06:30	GDP – 1st release Q/Q% (Y/Y%)	Q4	<u>0.5 (1.2)</u>	0.2 (1.0)
		07:45	Preliminary EU-harmonised CPI Y/Y%	Jan	1.2	0.8
		07:45	Consumer spending M/M% (Y/Y%)	Dec	0.2 (1.9)	0.4 (3.3)
Italy		09:00	Unemployment rate %	Dec	11.8	11.9
Spain		08:00	Preliminary EU-harmonised CPI Y/Y%	Jan	2.2	1.4
		09:00	Current account balance €bn	Nov	-	2.0
UK		00:01	Lloyds business barometer	Jan	-	39
		00:01	GfK consumer confidence survey	Jan	-8	-7
		09:30	Mortgage approvals `000s	Dec	69.0	67.5
		09:30	Net consumer credit (net lending secured on dwellings) £bn	Dec	1.7 (3.2)	1.9 (3.2)
Wednesday 01 February 2017						
EMU		09:00	Final manufacturing PMI	Jan	55.1	54.9
Germany		08:55	Final manufacturing PMI	Jan	56.5	55.5
France		08:50	Final manufacturing PMI	Jan	53.4	53.5
Italy		08:45	Manufacturing PMI	Jan	53.3	53.2
Spain		08:15	Manufacturing PMI	Jan	55.1	55.3
UK		00:01	BRC shop price index Y/Y%	Jan	-1.0	-1.4
		07:00	Nationwide house price index M/M% (Y/Y%)	Jan	0.0 (4.3)	0.8 (4.5)
		09:30	Manufacturing PMI	Jan	55.9	56.1
Thursday 02 February 2017						
UK		09:30	Construction PMI	Jan	53.8	54.2
		12:00	BoE bank rate %	Feb	<u>0.25</u>	0.25
		12:00	BoE asset purchase target £bn	Feb	<u>435</u>	435
		15:00	BoE corporate bond purchases £bn	Weekly	-	5.76
Friday 03 February 2017						
EMU		09:00	Final services PMI (final composite PMI)	Jan	53.6 (54.3)	53.7 (54.4)
		10:00	Retail sales M/M% (Y/Y%)	Dec	0.3 (1.7)	-0.4 (2.3)
Germany		08:55	Final services PMI (final composite PMI)	Jan	53.2 (54.7)	54.3 (55.2)
France		08:50	Final services PMI (final composite PMI)	Jan	53.9 (53.8)	52.9 (53.1)
Italy		08:45	Services PMI (composite PMI)	Jan	52.5 (53.0)	52.3 (52.9)
		10:00	Preliminary EU-harmonised CPI Y/Y%	Jan	0.8	0.5
Spain		08:15	Services PMI (composite PMI)	Jan	54.7 (55.1)	55.0 (55.5)
UK		09:30	Services PMI (composite PMI)	Jan	55.7 (56.0)	56.2 (56.7)

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

Coming week's events/auctions calendar

Key events & auctions			
Country	GMT	Event / Auction	
Monday 30 January 2017			
Italy		10:00	Auction: To sell up to €2.75bn of 0.35% 2021 bonds (01-Nov-2021)
		10:00	Auction: To sell up to €2.25bn of 2024 floating-rate bonds (15-Feb-2024)
		10:00	Auction: To sell up to €4bn of 2.2% 2027 bonds (01-Jun-2027)
UK		14:50	BoE APF operation: To purchase 3-7Y Gilts
Tuesday 31 January 2017			
EMU		08:00	ECB's Draghi scheduled to speak in Frankfurt
UK		10:30	Auction: To sell 1.5% 2026 bonds
		14:50	BoE APF operation: To purchase 15Y+ Gilts
Wednesday 01 February 2017			
Germany		10:30	Auction: To sell €4bn of 2022 bonds (08-Apr-2022)
UK		14:50	BoE APF operation: To purchase 7-15Y Gilts
Thursday 02 February 2017			
EMU		09:00	ECB publishes Economic Bulletin
		12:15	ECB's Draghi scheduled to speak in Slovenia
France		09:50	Auction: To sell 0.25% 2026 bonds (25-Nov-2026)
		09:50	Auction: To sell 1.5% 2031 bonds (25-May-2031)
Spain		09:30	Auction: To sell 0.25% 2019 bonds (31-Jan-2019)
		09:30	Auction: To sell 1.8% 2024 index-linked bonds (30-Nov-2024)
		09:30	Auction: To sell 1.95% 2030 bonds (30-Jul-2030)
		09:30	Auction: To sell 4.2% 2037 bonds (31-Jan-2037)
UK		12:00	Monetary policy announcement and MPC minutes
		12:00	BoE publishes Inflation Report
Friday 03 February 2017			
- Nothing scheduled -			

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

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