

Euro wrap-up

Overview

- Bunds made modest losses, while data showed a further narrowing of the euro area's current account surplus.
- Gilts also made modest losses despite a disappointing UK retail sales release.
- The coming week will bring the latest ECB Governing Council meeting, the UK government's new Brexit proposal, various euro area sentiment surveys and UK labour market data.

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Daily bond market movements

Bond	Yield	Change*
BKO 0 12/20	-0.580	+0.007
OBL 0 10/23	-0.334	+0.018
DBR 0¼ 02/29	0.263	+0.021
UKT 2 07/20	0.817	-0.008
UKT 0¼ 07/23	0.982	+0.006
UKT 1½ 10/28	1.354	+0.017

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

Euro area

Current account surplus slips back in November but remains sizeable

The euro area's latest balance of payments figures, published today, continued to illustrate the impact of last year's steady deterioration in the region's trade performance on the current account, which in November saw the surplus narrow by €6.5bn to €20.3bn, a nineteen-month low. Indeed, the goods trade surplus on this basis fell for the third consecutive month in November to €18.3bn, its lowest for almost 4½ years. And the services trade and primary income balances also edged slightly lower that month. But in the twelve months to November, the services trade balance was the strongest on record, contrasting with the equivalent goods balance which was the lowest since mid-2015. And the cumulative current account surplus still stood at a large €353bn, 3.1% of GDP, admittedly down ½ppt from the peak in the middle of last year but still close to its level in November 2017.

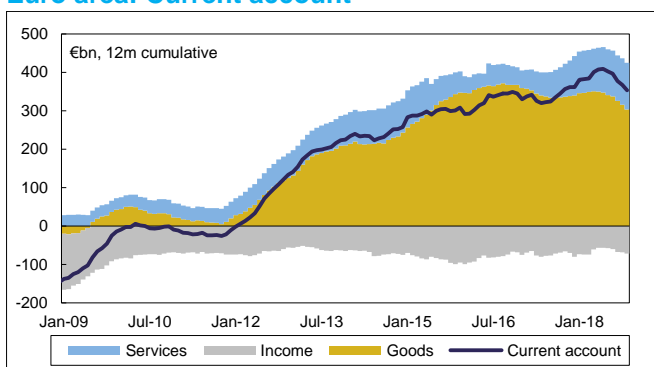
Non-residents continue to scale back net purchases of euro area assets

With respect to the financial account, today's data once again highlighted the reduction in portfolio flows both into and out of the euro area over the past year. For example, in the twelve months to November 2018 net acquisitions of foreign debt securities by euro area residents were down to a 4½-year low of just €145bn, from €457bn in the twelve months to November 2017. Over the same period, euro area residents scaled back their net purchases of foreign equity by more than €190bn to just €14bn. Meanwhile, the decrease in net purchases of euro area equity by non-residents was also striking, by €280bn to €180bn, a near-two-year low. Non-residents also continued to reduce their net holdings of euro area debt, with net selling in the twelve months to November at €43bn. At the country level, meanwhile, there was a notable net selling of French government debt securities by non-residents in November (€12.6bn), although this followed significant increases in the previous quarter. Meanwhile, the steady net selling of Italian government debt since April's elections was maintained in November, with another decline of €8.3bn taking the cumulative drop since April to €96bn. And so the share of Italian government debt held by non-residents fell a further 0.2ppt in October to 30.1%, the lowest for nineteen years.

The week ahead in the euro area and US

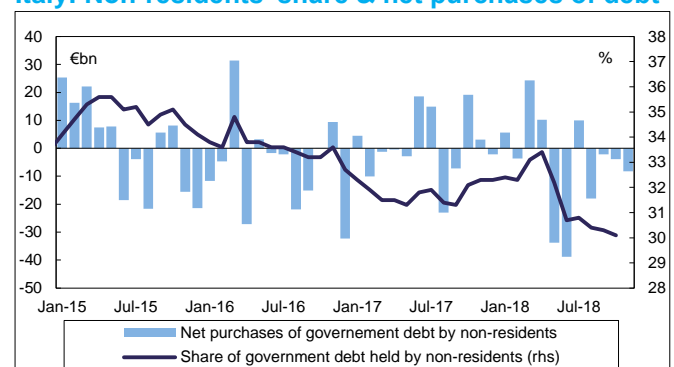
The main event in the euro area in the coming week will be the conclusion of the ECB's latest policy meeting on Thursday. While its policy guidance will undoubtedly be left unchanged, we expect the Governing Council's economic assessment and Draghi's press conference to adopt a more dovish tone. In particular, with the recent dataflow having signalled a further slowdown in economic momentum in the euro area heading into the New Year, Draghi earlier this week admitted that

Euro area: Current account



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

Italy: Non-residents' share & net purchases of debt



Source: Bank d'Italia, ECB and Daiwa Capital Markets Europe Ltd.



uncertainties remain prominent. Indeed, some Governing Council members at December's meeting had already cautioned more strongly about rising downside risks. And Draghi's opening statement on Thursday should acknowledge that the risks to the outlook are now skewed to the downside. However, while Draghi this week hinted that the ECB might struggle to adjust the stance of monetary policy this year, we do not expect to see until March at the earliest any tweaks to the guidance that its key interest rates are expected "to remain at their present levels at least through the summer of 2019, and in any case for as long as necessary". The next policy initiative of the ECB will relate to liquidity, and so the press conference might also see Draghi questioned about whether, and if so what, work is currently underway on future long-term financing operations.

With respect to the dataflow, the coming week will be dominated by January sentiment surveys, including the Commission's flash consumer confidence indicator on Wednesday and the preliminary PMIs on Thursday. Having maintained a downward trend throughout 2018, consumer confidence took a notable step down in December to a 22-month low and a further modest deterioration is expected in January. Business sentiment similarly fell sharply last year, with the euro area composite PMI declining more than 7½pts over the year to its lowest level (51.1) for more than four years. But expectations are for sentiment to have moved broadly sideways in January, with the PMIs forecast to signal little change in momentum in the two largest member states too. Other national business sentiment surveys due include Germany's ZEW (Tuesday), France's INSEE (Wednesday) and Germany's Ifo (Friday). Tuesday will also bring the ECB's latest Bank Lending Survey, while Friday will see the ECB's latest survey of professional forecasts published. In the markets, Germany will sell 5Y bonds on Wednesday and France will sell bonds with various maturities on Thursday.

In the US, the coming week's economic diary remains somewhat uncertain given the government shutdown with numerous delayed reports that could make an appearance if a resolution was suddenly to emerge. As things stand, following Monday's Martin Luther King Jnr holiday, the first scheduled report this week is Tuesday's existing home sales report for December. The Richmond Fed's manufacturing survey will be released on Wednesday while the flash PMI indices for January are released on Thursday, together with the Conference Board's Leading Index for December and the Kansas City Fed manufacturing survey for January. Friday will bring new home sales data for December, while the advance durable goods orders report for December appears likely to be delayed. In the bond market, issuance by the Treasury will be restricted to bills.

UK

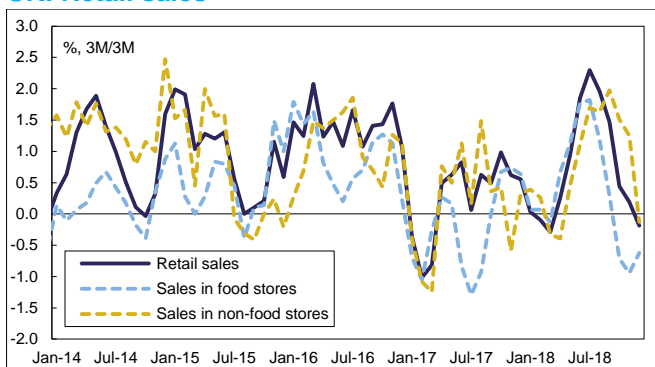
Christmas sales failed to reinvigorate the High Street

With Black Friday discounting in November having attracted savvy buyers to do their Christmas shopping early – total sales were up by 1.3%M/M that month – retail sector figures for December never looked likely to be very strong. And today's data from the ONS showed a decline in sales (on a seasonally adjusted basis) at the end of 2018 of almost 1.0%M/M, with food stores reporting a small increase and non-food stores posting a drop of 2.3%M/M, the steepest in almost four years. So, the figures were consistent with the changing seasonal pattern on the High Street, with November's promotions becoming more important at the expense of the festive period shopping. In line with the recent trend, the figures once again highlighted a shift from bricks and mortar towards internet shopping – indeed, total internet sales were up again, by 2.9%M/M, despite the fact that the household goods category saw a drop of nearly 18%M/M. Over Q4 as a whole, total retail sales posted a small decline of 0.2%Q/Q, which represented the first negative reading on a 3M/3M basis since Q1. The weakness was consistent the deterioration in consumer sentiment in recent months, and so we expect sluggishness in sales to continue this year, in particular if Brexit uncertainty persists. Our forecasts predict a 0.3ppt slowing in private consumption in Q418 to 0.2%Q/Q, with a similar rate of increase in Q119.

The week ahead in the UK

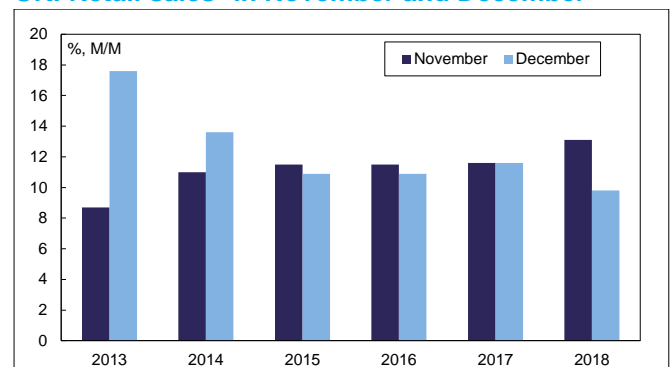
With Theresa May today continuing her consultations with various political groupings – including her Cabinet and EU leaders – all eyes on Monday will be on the tabling in Parliament of the Government's proposal for a new way forward for Brexit. Not

UK: Retail sales



Source: Thomson Reuters and Daiwa Capital Markets Europe Ltd

UK: Retail sales* in November and December


















*Non-seasonally adjusted data. Source: Thomson Reuters and Daiwa Capital Markets Europe Ltd.

least given the fragility of her position as Prime Minister, her limited political skillset, and the sharply opposing views of members of her cabinet and Conservative MPs, there is significant uncertainty as to how much substance she will be prepared to provide. But Monday is also likely to see other MPs table their own proposals to try to shape the way forward on Brexit, whether by simply seeking to express the will of Parliament against a no-deal Brexit, or, more substantively, seeking to demand that the Government request from the EU an extension of the Article 50 notice (perhaps up to the end of the year). However, the Government's and MPs' proposals will not be voted on until 29 January.





The most notable data release in the coming week will be the latest labour market figures, which are due on Tuesday. Most headline numbers are set to be little changed from the previous month. Indeed, three-month employment growth is expected to have remained at around 80k3M/3M in November, up from -5k3M/3M in August but very similar to October's reading, while the headline unemployment rate is also likely to have moved sideways at 4.1%. Similarly, we think that headline growth in average weekly earnings is also likely to be little changed, having posted growth of 3.3%3M/Y in October, which was the strongest rate since the 2008 crisis. Among other new data, the CBI Industrial Trends and Distributive Trade surveys, due on Wednesday and Friday respectively, will be worth watching too. The end of the week will also bring UK Finance lending data from major High Street banks.

Daiwa economic forecasts

	2018				2019				2018	2019	2020
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4			
GDP forecasts %, Q/Q											
Euro area 	0.4	0.4	0.2	0.2	0.3	0.3	0.3	0.3	1.8	1.0	1.0
Germany 	0.4	0.5	-0.2	0.2	0.3	0.3	0.3	0.3	1.5	1.0	1.2
France 	0.2	0.2	0.3	0.2	0.3	0.3	0.3	0.3	1.5	1.0	0.9
Italy 	0.3	0.2	-0.1	0.0	0.1	0.2	0.1	0.2	0.9	0.3	0.5
Spain 	0.6	0.6	0.6	0.5	0.5	0.4	0.4	0.4	2.5	1.9	1.7
UK 	0.1	0.4	0.6	0.2	0.1	0.1	0.4	0.3	1.4	1.0	1.1
Inflation forecasts %, Y/Y											
Euro area											
Headline CPI 	1.3	1.7	2.1	1.9	1.2	1.1	0.8	0.9	1.7	1.0	1.4
Core CPI 	1.0	0.9	1.0	1.0	1.0	1.0	1.1	1.1	1.0	1.1	1.3
UK											
Headline CPI 	2.7	2.4	2.5	2.3	1.9	1.9	1.7	1.7	2.5	1.8	1.9
Core CPI 	2.5	2.0	2.0	1.8	1.8	2.0	1.9	2.0	2.1	1.9	2.0
Monetary policy											
ECB											
Refi Rate % 	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00
Deposit Rate % 	-0.40	-0.40	-0.40	-0.40	-0.40	-0.40	-0.40	-0.40	-0.40	-0.40	-0.40
Net asset purchases* 	30	30	30	15	0	0	0	0	15	0	0
BoE											
Bank Rate % 	0.50	0.50	0.75	0.75	0.75	0.75	0.75	0.75	0.75	0.75	0.75
Net asset purchases** 	0	0	0	0	0	0	0	0	0	0	0




























*Monthly target €bn, end of period. **Monthly target £bn, end of period. Source: Bloomberg, ECB, BoE 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	20.3	-	23.0	26.8
Italy 	Current account balance €bn	Nov	4.8	-	6.1	6.0
UK 	Retail sales excluding auto fuel M/M% (Y/Y%)	Dec	-1.3 (2.6)	-0.8 (3.8)	1.2 (3.8)	1.0 (3.5)
	Retail sales including auto fuel M/M% (Y/Y%)	Dec	-0.9 (3.0)	-0.8 (3.6)	1.4 (3.6)	1.3 (3.4)
Auctions and events						
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 21 January 2019						
Germany		07:00	PPI M/M% (Y/Y%)	Dec	-0.1 (2.9)	0.1 (3.3)
UK		00:01	Rightmove house prices M/M% (Y/Y%)	Jan	-	-1.5 (0.7)
Tuesday 22 January 2019						
EMU		10:00	ZEW expectations indicator	Jan	-	-21.0
Germany		10:00	ZEW current situation (expectations) indicator	Jan	43.5 (-18.5)	45.3 (-17.5)
Spain		09:00	Trade balance €bn	Nov	-	-3.1
UK		09:30	Claimant count rate % (change '000s)	Dec	-	2.8 (2.2)
		09:30	Average weekly earnings (excl. bonuses) 3M/Y%	Nov	<u>3.3 (3.3)</u>	3.3 (3.3)
		09:30	ILO Unemployment rate 3M%	Nov	<u>4.1</u>	4.1
		09:30	Employment change 3M/3M '000s	Nov	<u>80</u>	79
		09:30	Public sector net borrowing excluding interventions £bn	Dec	1.9	7.2
Wednesday 23 January 2019						
EMU		15:00	Final consumer confidence indicator	Jan	-6.5	-6.2
France		07:45	Business sentiment indicator	Jan	102	102
		07:45	Manufacturing confidence (production outlook) indicator	Jan	103 (-9)	104 (-10)
UK		11:00	CBI Industrial Trends Survey, total orders	Jan	5	8
Thursday 24 January 2019						
EMU		09:00	Preliminary services PMI (preliminary composite PMI)	Jan	51.5 (51.4)	51.2 (51.1)
		09:00	Preliminary manufacturing PMI	Jan	51.4	51.4
		12:45	ECB Main Refinancing rate %	Jan	<u>0.00</u>	0.00
		12:45	ECB Marginal Lending Facility rate %	Jan	<u>0.25</u>	0.25
		12:45	ECB Main Deposit rate %	Jan	<u>-0.40</u>	-0.40
Germany		08:30	Preliminary services PMI (preliminary composite PMI)	Jan	52.2 (51.9)	51.8 (51.6)
		08:30	Preliminary manufacturing PMI	Jan	51.5	51.5
France		08:15	Preliminary services PMI (preliminary composite PMI)	Jan	50.5 (51.0)	49.0 (48.7)
		08:15	Preliminary manufacturing PMI	Jan	50.0	49.7
Friday 25 January 2019						
Germany		09:00	Ifo business climate index	Jan	100.6	101.0
		09:00	Ifo current assessment balance (expectations)	Jan	104.2 (97.1)	104.7 (97.3)
UK		09:30	UK Finance mortgage approvals 000's	Dec	38.7	39.4
		11:00	CBI Distributive Trades Survey – retail sales	Jan	1	-13

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

Coming week's events/auctions calendar

Key events & auctions			
Country	GMT	Event / Auction	
Monday 21 January 2019			
- Nothing scheduled -			
Tuesday 22 January 2019			
EMU		09:00	ECB to publish Bank Lending Survey
UK		10:30	Auction: to sell £1.75bn of 1.75% 2037 bonds (07-Sep-2037)
Wednesday 23 January 2019			
Germany		10:30	Auction: to sell €4bn of 2024 bonds (05-Apr-2024)
Thursday 24 January 2019			
EMU		13:30	ECB's Draghi holds a press conference after a monetary policy decision
France		09:50	Auction: to sell 0% 2024 bonds (25-Mar-2024)
		09:50	Auction: to sell 0.5% 2025 bonds (25-May-2025)
		09:50	Auction: to sell 0% 2022 bonds (25-May-2022)
		09:50	Auction: to sell 2022 bonds (25-Feb-2022)
		10:50	Auction: to sell 0.25% 2024 index-linked bonds (25-Jul-2024)
		10:50	Auction: to sell 0.1% 2028 index-linked bonds (01-Mar-2028)
		10:50	Auction: to sell 0.1% 2047 index-linked bonds (25-Jul-2047)
Friday 25 January 2019			
EMU		09:00	ECB Survey of Professional Forecasters

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

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