

Euro wrap-up

Overview

- Despite upside surprises to the flash December estimates of German and French inflation, Bunds followed USTs higher on concerns about events in the Middle East.
- Gilts also made significant gains as UK data indicated ongoing construction sector weakness and subdued consumer credit growth.
- The coming week brings the flash December estimate of euro area inflation, as well as updates on German manufacturing production, exports and orders, and the latest European Commission economic sentiment indices.

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Daily bond market movements

Bond	Yield	Change
BKO 0 12/21	-0.639	-0.016
OBL 0 10/24	-0.560	-0.047
DBR 0 08/29	-0.290	-0.062
UKT 3% 09/21	0.552	-0.015
UKT 1 04/24	0.547	-0.041
UKT 0% 10/29	0.738	-0.053

*Change from close as at 4:30pm GMT.
Source: Bloomberg

Euro area

German and French inflation beats expectations

Ahead of Tuesday's release of the equivalent euro area figures, today's preliminary estimates of German and French inflation in December surprised on the upside. In particular, German inflation on the EU-harmonised HICP measure rose 0.3ppt for the second successive month to a six-month high of 1.5%Y/Y. And French inflation on the same measure rose 0.4ppt to a ten-month high of 1.6%Y/Y. The equivalent figures for Spain, released at the end of 2019, showed a smaller-than-expected rise of 0.3ppt to 0.8%Y/Y. As such, headline euro area inflation is also likely to have increased by 0.3ppt in December to 1.3%Y/Y, which would be the highest since April. Based on the limited information published so far by the national statistical agencies, the increase in headline inflation last month was due to past shifts in petrol and electricity prices. As such, we expect euro area core inflation to remain unchanged, also at 1.3%Y/Y.

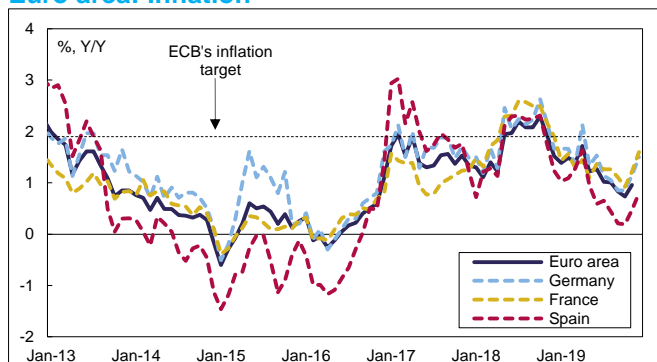
Bank lending to firms slowed in November

The flow of new bank loans to non-financial corporations (NFCs) in the euro area dropped in November to just €2.4bn, more than €12bn below the average of the prior six months. As a result, the annual rate of growth in the stock of loans to NFCs fell 0.4ppt to 3.4%Y/Y, the softest rate in nineteen months, with a weakening reported in Germany, France and Italy. In contrast, thanks to ongoing firm lending for house purchases, net new loans to households edged up slightly to €20.9bn, representing the strongest month since April 2008. So the annual rate of growth in the stock of such loans was unchanged at 3.5%Y/Y, matching the highest in more than a decade. With surveys having suggested no meaningful tightening in credit standards, we suspect that the decline in new loans to NFCs principally reflected demand-side factors, related not least to the uncertain economic environment and recent downtrend in manufacturing production and orders.

The week ahead in the euro area and US

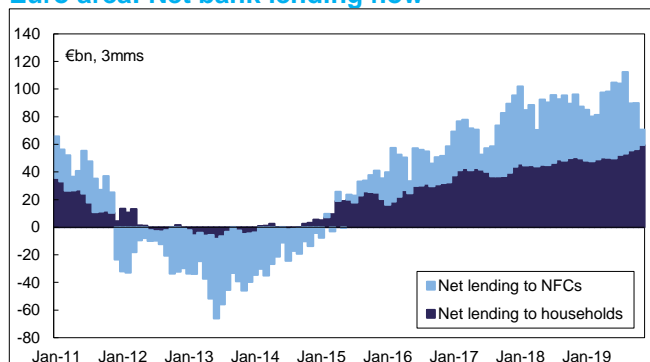
The coming week will be a busy one for economic data from the euro area bringing the results of several December sentiment surveys as well as updates on activity and inflation in November. Monday will see the final services and composite PMIs for December – the flash euro area services PMI rose 0.5pt to a four-month high of 52.4 to suggest ongoing steady (if not vigorous) growth in the sector, but that still left the composite PMI stuck for a third month at 50.6 to match the second-lowest reading since mid-2013. German retail sales figures for November are also due on Monday, with the equivalent euro area data due the following day – following a marked decline in October a rebound in sales is expected in the latest month, with the consensus forecast for growth in the euro area of about ½%M/M. The flash estimate of euro area inflation in December is also due on Tuesday – the headline rate is expected to rise 0.3ppt to 1.3%Y/Y due principally to energy price

Euro area: Inflation*



*HICP inflation. December 2019 flash estimates for Germany, France and Spain.
Source: Thomson Reuters and Daiwa Capital Markets Europe Ltd.

Euro area: Net bank lending flow



Source: Thomson Reuters and Daiwa Capital Markets Europe Ltd.

base effects, and so the core measure is expected to remain unchanged, also at 1.3%Y/Y. Wednesday, meanwhile, will bring the European Commission's economic sentiment indices for December, which often provide the most reliable guide to economic activity. German factory orders figures for November are due the same day, with German IP and trade data for the same month due on Thursday. IP data from France, Italy and Spain will round off the week on Friday.

Beyond the economic data, politics will remain in focus in certain member states. In Spain, following a debate and initial vote this coming weekend, Spain's parliament is scheduled to vote again on Tuesday on the establishment of a new minority left-wing government led by the Socialists (PSOE). With the Catalan separatist party Esquerra Republicana de Catalunya having agreed to abstain, and the populist left Podemos set to vote in favour, the new government will be approved by a simple majority. On the same day in Italy, Prime Minister Conte will hold a meeting with the leaders of the parties making up his coalition government in a bid to reach a compromise on judicial reform – failure to find an agreement could bring the government closer to collapse. Meanwhile, in the bond markets, Germany will sell 10Y Bunds on Wednesday while France and Spain will sell a range of bonds on Thursday.

In the US, a key focus will be the December labour market report, with non-farm payrolls expected to have risen by somewhat less than the 180k average for the first eleven months of the year, having leapt 266k in November partly thanks to returning GM strikers. While revisions to the Household Survey will also be released, the unemployment rate is expected to remain unchanged at 3.5%. And growth in average hourly labour earnings is expected to move sideways at 3.1%Y/Y. Ahead of the official labour market report, the ADP jobs data are scheduled on Wednesday. Other US data due in the coming week include the December non-manufacturing ISM survey results, which will be released on Tuesday along with the final November trade and factory orders figures. Fed speakers include Board of Governors Vice Chair Clarida and New York Fed President Williams, both on Thursday. In the markets, the Treasury will sell 3Y Notes, 10Y Notes and 30Y Bonds on Tuesday, Wednesday and Thursday respectively.

UK

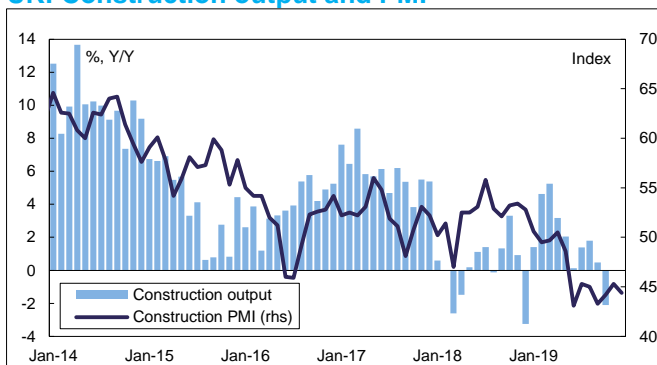
Construction PMI on worst run since the financial crisis

UK construction output has been on a weakening trend over the past year, with output in the sector down 2.1%Y/Y in October to the lowest level in eighteen months. Judging from today's construction PMI survey, the weakness persisted through to the end of the year. The headline index dropped 0.9pt in December to 44.4, just below the average for the second half of the year. The result marked the eighth consecutive sub-50 reading, representing the longest run of contractionary results since the financial crisis. All main sub-sectors reported softer activity, with civil engineering down the most since March 2009, house-building down for a seventh successive month, and commercial work also weak. Nevertheless, firms suggested that they were the most optimistic for nine months about the outlook for twelve-months ahead. Increased public sector investment is likely to boost civil engineering activity while lower mortgage rates and gradually rising house prices (up 1.4%Y/Y on the Nationwide measure, the most in thirteen months, in December) should support housing demand and associated activity. The reduction in no-deal Brexit risks and broader political uncertainty will have provided some support to construction sector order books too. However, ongoing lack of clarity about the future relationship between the UK and EU, and the risk of a significant increase in trade barriers at the end of this year, means that business investment, and related private sector building work, will remain weak.

Consumer credit growth at six-year low

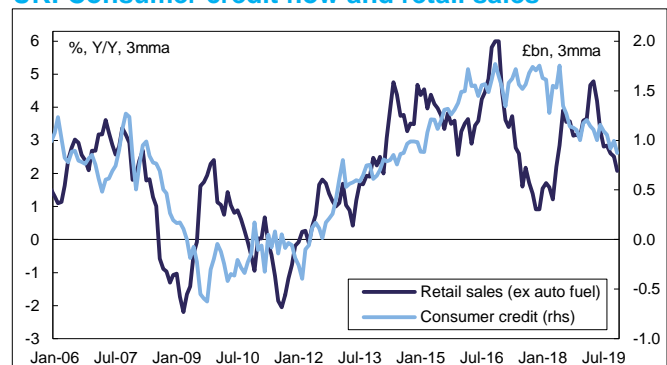
Bank of England data for November point to continued stability in the housing market, with net mortgage borrowing by households at £4.1bn leaving the annual growth rate at 3.3%Y/Y, well within the range of the past three years. Mortgage approvals for future house purchase were unchanged at 65k, again within the narrow range of the past two years albeit obviously well down on pre-financial crisis norms. However, households were again much less willing to borrow in order to

UK: Construction output and PMI



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

UK: Consumer credit flow and retail sales


















Source: Thomson Reuters and Daiwa Capital Markets Europe Ltd.

buy goods and services. The flow of new consumer credit dropped to £0.6bn, the weakest since November 2013, with a net repayment of credit card debt for the first time in more than six years. As such, the annual growth rate of consumer credit slowed to 5.7%Y/Y, the weakest in more than five years. Net new borrowing by businesses was also subdued in November, at just £0.9bn, weighed by the lowest net bond issuance in nine months and a significant drop in new bank lending. So, the annual growth rate in the stock of loans to NFCs slowed to a three-month low of 3.5%Y/Y, with growth in loans to large businesses down to 4.9%Y/Y and those to SMEs still subdued at just 1.0%Y/Y.

The week ahead in the UK











The coming week will be relatively quiet for new UK economic data. Like in the euro area, Monday will bring the final services and composite PMIs for December. In contrast to the better reading in the euro area, the UK's flash services PMI fell for the fourth month out of the past five in December to 49.0, with the latest two observations marking the first successive sub-50 readings in the sector for more than a decade. The flash composite PMI fell 0.8pt in December to 48.5, the second-lowest reading since the height of the Global Financial Crisis, leaving the quarterly average at 49.3 in Q4, the weakest since Q109. Other data due in the coming week include new car registrations figures for December (also on Monday), final Q3 productivity and labour cost data (Wednesday) and the BRC's retail sales survey for December (Thursday). In the markets, the DMO will sell 2029 Gilts on Tuesday and 2028 Linkers on Thursday.

Daiwa economic forecasts

	2019				2020				2019	2020	2021
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4			
GDP forecasts %, Q/Q											
Euro area 	0.4	0.2	0.2	0.1	0.2	0.2	0.2	0.1	1.1	0.7	0.5
Germany 	0.5	-0.2	0.1	0.1	0.1	0.2	0.1	0.1	0.6	0.5	0.4
France 	0.3	0.3	0.3	0.2	0.3	0.3	0.2	0.2	1.3	1.2	0.8
Italy 	0.1	0.1	0.1	0.0	0.0	0.1	-0.1	-0.1	0.2	0.1	0.0
Spain 	0.5	0.4	0.4	0.4	0.4	0.4	0.4	0.3	2.0	1.6	1.1
UK 	0.6	-0.2	0.4	-0.1	0.2	0.2	0.2	0.1	1.3	0.6	0.5
Inflation forecasts %, Y/Y											
Euro area											
Headline CPI 	1.4	1.4	1.0	1.0	1.2	1.1	1.3	1.2	1.2	1.2	1.4
Core CPI 	1.0	1.1	0.9	1.3	1.3	1.3	1.5	1.2	1.0	1.3	1.3
UK											
Headline CPI 	1.9	2.0	1.8	1.5	1.7	1.1	0.9	1.0	1.8	1.3	1.5
Core CPI 	1.9	1.7	1.7	1.7	1.6	1.4	1.2	1.1	1.7	1.3	1.3
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	-0.50	-0.50	-0.50	-0.50	-0.60	-0.60	-0.50	-0.60	-0.60
Net asset purchases* 	0	0	0	20	20	20	30	30	20	30	30
BoE											
Bank Rate % 	0.75	0.75	0.75	0.75	0.75	0.50	0.50	0.50	0.75	0.50	0.25
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/ <i>Daiwa forecast</i>	Previous	Revised
EMU	 M3 money supply Y/Y%	Nov	5.6	5.7	5.6	5.7
Germany	 Unemployment rate % (change '000s)	Dec	5.0 (8.0)	5.0 (4.0)	5.0 (-16.0)	- (-14.0)
	 Preliminary CPI (EU-harmonised CPI) Y/Y%	Dec	1.5 (1.5)	1.4 (1.4)	1.1 (1.2)	
France	 Preliminary CPI (EU-harmonised CPI) Y/Y%	Dec	1.4 (1.6)	1.3 (1.4)	1.0 (1.2)	
Spain	 Unemployment change '000s	Dec	-34.6	-40.0	20.5	
UK	 BRC shop price index Y/Y%	Dec	-0.4	-0.5	-0.5	-
	 Nationwide house price index M/M% (Y/Y%)	Dec	0.1 (1.4)	0.0 (1.4)	0.5 (0.8)	-
	 Construction PMI	Dec	44.4	45.9	45.3	-
	 Net consumer credit (net mortgage lending) £bn	Nov	0.6 (4.1)	1.0 (4.0)	1.3 (4.3)	-
	 Mortgage approvals '000s	Nov	65.0	64.5	64.6	64.7
Auctions						
Country	Auction	- Nothing to report -				

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.









Coming week's data calendar

The coming week's key data releases

Monday 06 January 2020						
EMU		09.00	Final services PMI (composite PMI)	Dec	52.4 (50.6)	51.9 (50.6)
		10.00	PPI Y/Y%	Nov	-1.6	-1.9
Germany		07.00	Retail sales M/M% (Y/Y%)	Nov	1.0 (1.1)	-1.6 (1.4)
		08.55	Final services PMI (composite PMI)	Dec	52.0 (49.4)	51.7 (49.4)
France		08.50	Final services PMI (composite PMI)	Dec	52.4 (52.0)	52.2 (52.1)
Italy		08.45	Services PMI (composite PMI)	Dec	50.5 (49.7)	50.4 (49.6)
Spain		08.15	Services PMI (composite PMI)	Dec	53.9 (52.0)	53.2 (51.9)
UK		09.00	New car registrations Y/Y%	Dec	-	-1.3
		09.30	Final services PMI (composite PMI)	Dec	49.0 (48.5)	49.3 (49.3)
Tuesday 07 January 2020						
EMU		10.00	Retail sales M/M% (Y/Y%)	Nov	0.6 (1.5)	-0.6 (1.4)
		10.00	Preliminary CPI (core CPI) Y/Y%	Dec	1.4 (1.3)	1.0 (1.3)
Italy		10.00	Preliminary CPI (EU-harmonised CPI) Y/Y%	Dec	0.5 (0.5)	0.2 (0.2)
Wednesday 08 January 2020						
EMU		10.00	Economic confidence	Dec	101.5	101.3
		10.00	Industrial confidence indicator (services)	Dec	-8.9 (9.5)	-9.2 (9.3)
		10.00	Final consumer confidence	Dec	-8.1	-7.2
Germany		07.00	Factory orders M/M% (Y/Y%)	Nov	0.2 (-4.7)	-0.4 (-5.5)
France		07.45	Consumer confidence	Dec	104	106
		07.45	Trade balance €bn	Nov	-	-4.7
UK		09.30	Unit labour costs Y/Y%	Q3	-	3.6
Thursday 09 January 2020						
EMU		10.00	Unemployment rate %	Nov	7.5	7.5
Germany		07.00	Industrial production M/M% (Y/Y%)	Nov	0.7 (-3.8)	-1.7 (-5.3)
		07.00	Trade balance €bn	Nov	21.8	21.3
Italy		09.00	Unemployment rate %	Nov	9.8	9.7
UK		00.01	BRC like-for-like retail sales Y/Y%	Dec	-	-4.9
Friday 10 January 2020						
France		07.30	Bank of France industrial sentiment indicator	Dec	96	97
		07.45	Industrial production M/M% (Y/Y%)	Nov	0.1 (0.5)	0.4 (-0.2)
Italy		09.00	Industrial production M/M% (Y/Y%)	Nov	0.0 (-0.6)	-0.3 (-2.4)
Spain		08.00	Industrial production M/M% (Y/Y%)	Nov	0.2 (0.9)	-0.4 (-1.3)

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

The coming week's key events & auctions

Country	GMT	Event / Auction
Monday 06 January 2020		
- Nothing scheduled -		
Tuesday 07 January 2020		
Germany		10.30 Auction: to sell €500mn of 0.50% 2030 index-linked bonds
UK		10.30 Auction: to sell £2.75bn of 0.875% 2029 bonds
Wednesday 08 January 2020		
Germany		10.30 Auction: to sell €5bn of 2030 bonds
Thursday 09 January 2020		
France		09.50 Auction: to sell 0% 2029 bonds
		09.50 Auction: to sell 1.25% 2036 bonds
		09.50 Auction: to sell 1.50% 2050 bonds
Spain		09.45 Auction: to sell bonds
UK		10.30 Auction: to sell £1bn of 0.125% index-linked 2028 bonds
Friday 10 January 2020		
- Nothing scheduled -		

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

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