Economics

Investec Economics

The week ahead: Monday 16 January 2017

- This week's major global event was the first post-election press conference held by US President-elect, Donald Trump. Investors hoping for an endorsement of the 'Trump reflation trade', based on large scale US fiscal stimulus, were left disappointed by Wednesday's event. Rather than laying out a growth-boosting economic plan, the President-elect focused much of his attention criticising what he called the "fake news" media and even (not for the first time) the US intelligence agencies. With Mr Trump setting out such a bellicose stall, the trade-weighted dollar index dropped to its lowest level for a month, as did the US ten-year treasury yield. Meanwhile, the price of gold rose to a two-month high. This does not mean that the 'Trump reflation trade' is over – we note that US stocks actually rose on the day of the press conference, after an initial wobble. And, looking further ahead, we do see the incoming Trump Administration opening the fiscal taps. But this week is a reminder that the Trump Presidency also brings with it downsides as far as investor risk appetite is concerned. Next Friday (20 January) is the big day where Mr Trump is formally inaugurated – markets will be watching out for signals on what sort of Administration begins to take shape.

- Elsewhere in US policy, we might get a further steer on how the Federal Reserve sees the outlook for interest rates. With a number of FOMC members coalescing around the call for three rate hikes this year (we expect a more modest two) we will be watching Chair Janet Yellen's speeches on Wednesday and Friday with interest. In terms of the data, CPI and industrial production numbers will be released on Wednesday. We will also be looking out for whether the January Empire State (Tuesday) and Philly Fed (Thursday) manufacturing surveys hang onto sharp post-election gains – cue valedictory tweets from the President-elect if so.

- At home, Brexit news will rumble on. First, PM Theresa May has announced a 'major' speech on Brexit on Tuesday which will almost certainly have implications for sterling. Second, there is a High Court hearing on whether the Government needs to give one year's notice before leaving the European Economic Area (EEA) (over and above the process for leaving the EU). Essentially, the question is whether the Government needs to trigger Article 127 of the EEA Agreement (over and above Article 50 of the Lisbon Treaty). This might add a further complication to the Brexit process.

- The BoE's Mark Carney will speak on Monday. On monetary policy, Governor Carney will probably set a high bar for shifting away from the MPC's 'neutral policy stance' – ie looking to keep Bank Rate at 0.25% to guard against Brexit headwinds in the face of rising inflation. Next week's data might give us a steer on how the growth/inflation trade-off is evolving, with CPI numbers on Tuesday, followed by labour market data on Wednesday. We only expect a slight rise in inflation for now though (from +1.2% to +1.3%), with sharper rises to come later this year.

- Elsewhere in Europe, the main event will be the ECB policy decision on Thursday (see preview below). We expect to hear little new on the policy outlook, but we wonder how President Draghi will respond to recent rises in headline in inflation rates.

- On the global stage, the World Economic Forum annual meeting kicks off in Davos on Monday. It is difficult to see what credible solutions world leaders will find to key global issues, such as the rising tide of populism, at the Swiss ski resort. However, we do note that Xi Xinping will be the first Chinese Premier ever to attend.

- And on China, we note that Q4 GDP data will be published on Friday. Our central view is for signs of a gentle slowdown and economic rebalancing process to continue and for GDP growth to sit within the authorities' target range of 6.5-7.0%. **CH**

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ECB steady in New Year holding meeting?

The ECB's Governing Council meets for its first meeting of 2017 next week (on Thursday 19 January) with its policy announcement due at 12.45pm and the press conference with President Draghi at 1.30pm.

We expect no headline policy changes after the adjustments made to the ECB's QE plans at its December 8 meeting. In December the GC agreed to extend the QE programme by nine months to December 2017 but with the additional monthly purchases conducted at a pace of €60bn per month, a step down from the current rate of €80bn. The official ECB rates were left unchanged i.e. the deposit rate at -0.40%, the refi rate at 0.00% and the marginal lending rate at +0.25%. We expect these rates to prevail after next week's meeting too.

We would also be very surprised to see any major overhaul in the ECB's thinking on the economic outlook so soon after its December forecast update. Justifying the ECB's continuing accommodative policy stance, the outlooks for GDP and inflation remained relatively lacklustre in the December forecast update. GDP was seen slowing marginally from 1.7% this year and next, to 1.6% in 2018 and 2019. The HICP inflation projection for 2019 was 1.7% which Draghi described as 'not really' compatible with the ECB's inflation target of 'below, but close to 2%'.

Note that December's Euro area inflation figures generated some interest when they climbed to 1.1% (0.9% 'core'), the firmest headline reading since September 2013. However Yves Mersch of the GC, typically a more hawkish ECB member, did his best to calm enthusiasm that inflation was firmly moving upwards. He said that 'statistics from just one month' were 'not going to change our position' whilst cautioning that wages were not growing fast enough to fuel inflationary pressure. We expect President Draghi to also hold his view next week that the continuation of QE (and low rates) remains warranted for now to support the recovery in inflation.

On the specifics of QE purchases, we suspect the debate over whether the ECB will run into difficulties in buying the 'appropriate' mix of bonds will rumble on with no major new news this time around. In December the ECB loosened its purchase rules such that it reduced the minimum maturity for bonds it can purchase to one year from two. Secondly, it decided that when necessary, central banks will be able to buy paper yielding below the deposit rate. These changes are aimed at alleviating potential shortages of assets available for purchase, though with both rule changes taking effect from 2 January 2017, it is still too early to gauge whether they are having the desired effect. We note that against the ECB's capital key rule for purchases, which would see sovereign bond purchases in line with paid in ECB capital, the ECB has been under-purchasing Portuguese and Irish bonds. There had also been talk of impending issues for German bond purchases too. For Germany the issue has been the low levels of yield, with yields up to 5-years running below the -0.4% deposit rate. In Portugal, the constraint is the limit on purchasing more than 33% of any issue, which remains in place.

Finally, we would flag the prospect that the ECB President faces some questioning on the pre-Christmas Italian bank rescue package (for Monti dei Paschi and others) and its adherence with EU rules, particularly on state aid. On Greece, President Draghi may be asked for views on delays in Greece's bailout review, held back in part by Greece's unilateral decision to u-turn on its earlier commitment to end pensioner Christmas bonuses. As usual we would expect Draghi to avoid being drawn into such discussions. **VC**

Weekly Key Indicators

Indicator	Comment
Consumer Price Index (Dec) 09:30 Tuesday 17 January | | **Forecast** | **Last** | CPI (harmonised): +0.2% (1.3% yoy) | +0.2% (1.2% yoy) 'core' CPI: +0.3% (1.4% yoy) | +0.2% (1.4% yoy) RPI: +0.4% (2.3% yoy) | +0.3% (2.2% yoy) RPIX: +0.3% (2.5% yoy) | +0.3% (2.5% yoy)	• CPI inflation firmed to 1.2% from 0.9% in November, partly as winter clothing prices recovered. • For December, we take the view that the main driver will be base effects i.e. changes in December 2015 dropping out of the annual calculations. For example, petrol prices fell back by 1%-1.5% last month, reflecting both a reduction in global crude costs and a rise in sterling during the period. However a 2.8% decline 12 months earlier means that the impact of petrol costs should still be positive, we think by 0.05%. Secondly, while we expect food prices to have increased on the month, our suspicion is that this was muted by a higher pound. Even so, we are factoring in a small upward effect on the CPI measure thanks to a modest *decline* a year ago. Third, airfares rose by a whopping 46% in December 2015, the scale of which we judge will not be repeated this time. In this respect airfares may prove to be a small drag on inflation. • Netting these factors out, we are forecasting a relatively small increase in CPI inflation to 1.3%. However note that we still expect an increase towards 3.5% during the summer, a trend which would be reinforced should sterling continue to languish at current levels. **PS**
Producer Price Index (Dec) 09:30 Tuesday 17 January | | **Forecast** | **Last** | PPI output (nsa): +0.5% (3.1% yoy) | unch (2.3% yoy) PPI output -ex food etc (nsa): +0.3% (2.3% yoy) | unch (2.2% yoy) PPI input (nsa): +2.5% (16.1% yoy) | -1.1% (12.9% yoy)	• Producer input price inflation has been rising from its lows of -14.6% in August 2015 to reach an annual pace of 12.9% in November 2016, helped by the shake out of past energy price falls from the annual calculation, but also the effect of post-Brexit vote falls in the pound pushing up on import costs. • In December 2016 there was a surge in oil prices after November's OPEC gathering saw producers agree to cut oil output for the first time in eight years. Over the month the oil price (Brent crude) was recorded 17.2% up on November's levels. We expect this to be the overriding driver of movements in input prices in the coming month's numbers, given the size of the adjustment, and with movements in other major drivers relatively contained. Our forecast is for a month-on-month rise of 2.5% in the overall producer price index, such that the annual pace of input price inflation would reach 16.1%. • On the output price front (or 'factory gate' price), inflation climbed from +2.1% to +2.3% y/y. With higher import costs feeding into the supply chain as well as the oil price effect this time around we expect to see output prices rise by a 0.5% over the month such that inflation stands at 3.0% y/y. Monthly 'core' PPI inflation should be slightly softer because it strips out the direct effect of December's oil price rise. Here we are forecasting inflation of +0.3% m/m (+2.3% y/y). **VC**
Unemployment (Nov/ Dec) **Average earnings (Nov)** 09:30 Wednesday 18 January | | **Forecast** | **Last** | Unemployment (claimant count mom): +2.0k (2.3%) | +2.4k (2.3%) (ILO 3m-3m): -70k (4.9%) | -16k (4.8%) Headline earnings: +2.6% (3m yoy) | +2.5% (3m yoy)	• Last month's official jobs data showed tentative signs that the labour market could be at a turning point. The level of employment dropped by 6k in the three months to October – the first three-month decline since May 2015. The fall was driven by a rise in inactivity (the number of people neither in nor seeking work) while the unemployment rate held steady, at 4.8%. • It is extremely difficult to say whether this marks the beginning of a Brexit-related slowdown in the labour market. Indeed, such a development would sit at odds with a broader range of economic indicators, including the business surveys and the GDP data, which are holding up remarkably well. • But a read from the (admittedly volatile) 'single-month' employment data, rather than the three-month-moving average numbers normally quoted, point to a particularly weak picture in September and October. Bar a major pickup in November, declines in employment (on a three month basis) are set to become more marked. Meanwhile, our forecast is for the unemployment rate to tick up to 4.9% (mechanically, this is driven by the fact that the number of unemployed people still appears to be falling, but by less than total employment). • Even if past employment gains are beginning to reverse, any drag on wages is likely to take several months to come through. In fact, wage growth has been firming of late. Last month, private sector regular pay growth was estimated to have climbed to +2.8% (3m yoy) – the highest rate since September 2015. Any further rises are likely to be gradual, however, and we expect the main measures of wage growth to remain broadly steady in the

coming release. Our forecast is for headline (whole economy, including bonus) wage growth of +2.6% (3m yoy), a marginal firming from the previous month. **CH**

RICS housing survey
00:01 Thursday 19 January

	Forecast	Last
Prices balance	+30%	+30%

- The RICS housing market survey pointed to firmer house price growth with the 'prices balance', reflecting the number of surveyors seeing increases rather than price reductions, at +30%.
- That was reflective of the third consecutive increase in demand (new buyer enquiries) whilst supply – new instructions to sell – remained subdued. Indeed on the supply picture we note that the November RICS report highlighted the supply shortage as a dominant feature of the market at present.
- We see little evidence of that story having shifted markedly in December, with new supply remaining relatively constrained but with the pace of pick-up in buyer activity slowing now, too. We expect to see a broadly similar price balance of around +30%. **VC**

Retail sales (Dec)
09:30 Friday 20 January

	Forecast	Last
Retail sales	+0.2% (7.3% yoy)	+0.2% (5.9% yoy)
- ex petrol	+0.2% (8.2% yoy)	+0.5% (6.6% yoy)

- Retail sales growth outstripped expectations yet again last month, with +0.2% m/m growth (consensus was for unchanged sales volumes on the month).
- We expect last year's fall in sterling to begin pushing up materially on consumer prices in the coming months, which will squeeze real household incomes and spending.
- But, for now at least, price pressures on the high street remain very muted (the BRC shop price index still points to negative inflation), and households appear to be shrugging off the economic uncertainty associated with Brexit.
- So, looking to December, we expect a decent pace of sales volumes growth to continue, with +0.2% m/m growth (including and excluding fuel).
- Given the 'low-flation' boost to spending volumes seen in recent months, this would deliver remarkable strength, in year-on-year terms. Our forecast is for +7.3% y/y growth (including fuel) and +8.2% y/y (excluding fuel). On both measures, that would be the highest rate of annual growth seen since April 2002. **CH**

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The Week Ahead

Date	Venue	GMT		Indicator/event	For	Investec Forecast	Previous
Mon 16	UK	18:30	♦	Carney speaks at the LSE			
	JA	(23:50)		Private 'core' machinery orders	Nov		+4.1% (-5.6% yoy)
	IT	09:00		HICP (final)	Dec		+0.5% (yoy) (p)
	US			US holiday: Martin Luther King Day			
	WEF			World Economic Forum Annual meeting, Davos (day 1 of 5)			
Tue 17	UK		♦	PM May to deliver major speech on Brexit			
		09:30	♦	CPI	Dec	+0.2% (1.3% yoy)	+0.2% (+1.2% yoy)
		09:30		- core	Dec	+0.3% (1.4% yoy)	+0.2% (+1.4% yoy)
		09:30		RPI	Dec	+0.4% (2.3% yoy)	+0.3% (+2.2% yoy)
		09:30		RPIX	Dec	+0.3% (2.5% yoy)	+0.3% (+2.5% yoy)
		09:30		PPI input	Dec	+2.5% (16.1% yoy)	-1.1% (+12.9% yoy)
		09:30		PPI output	Dec	+0.5% (3.1% yoy)	unch (+2.3% yoy)
		09:30		PPI output 'core'	Dec	+0.3% (2.3% yoy)	unch (+2.2% yoy)
		09:30		ONS house price index	Nov		+6.9% (yoy)
	JA	04:30		Industrial production (final)	Nov		+1.5% (+4.6% yoy) (p)
	EU19	09:00		ECB bank lending survey			
	GE	10:00		ZEW survey: current situation	Jan		+63.5
		10:00		ZEW Survey: economic expectations	Jan		+13.8
	US	13:30		Empire State manufacturing survey	Jan		+9
Wed 18	UK	09:30	♦	Unemployment (claimant count)	Dec	+2.0k (2.3%)	+2.4k (2.3%)
		09:30		Unemployment (ILO)	Nov	-70k 3m/3m (4.9%)	-16k 3m/3m (4.8%)
		09:30		Average earnings	Nov	+2.6% (3m yoy)	+2.5% (3m yoy)
	EU19	10:00	♦	CPI (final)	Dec		+1.1% (yoy) (p)
		10:00		- ex food, energy, alcohol & tobacco (final)	Dec		+0.9% (yoy) (p)
	GE	07:00		HICP (final)	Dec		+1.0% (+1.7% yoy) (p)
		07:00		CPI (final)	Dec		+0.7% (+1.7% yoy) (p)
	US	13:30	♦	CPI	Dec		+0.2% (+1.7% yoy)
		13:30		- ex food & energy	Dec		+0.2% (+2.1% yoy)
		14:15		Industrial production	Dec		-0.4%
		15:00		NAHB housing market index	Jan		+70
		19:00		Fed Beige Book			
		20:00	♦	Fed's Yellen speaks in San Francisco			
		21:00		Long-term investment flows (TIC data)	Nov		$9.4bn
	CA	15:00		Bank of Canada monetary policy decision			unch (0.50%)
Thu 19	UK	00:01	♦	RICS Housing Survey	Dec	+30%	+30% (house price balance)
	EU19	12:45	♦	ECB announcement (& press conference)		unch	QE extension, rates unch
	US	13:30		Philadelphia Fed index	Jan		+21.5
		13:30		Building permits	Dec		+1212k (saar)
		13:30		Housing starts	Dec		+1090k (saar)
		13:30		Weekly jobless claims	14-Jan		+10k (247k)
Fri 20	UK	09:30	♦	Retail sales	Dec	+0.2% (7.3% yoy)	+0.2% (+5.9% yoy)
		09:30		- ex petrol	Dec	+0.2% (8.2% yoy)	+0.5% (+6.6% (yoy)
			♦	High Court hearing on Article 127			
	CH	02:00	♦	GDP	Q4		+1.8% (+6.7% (yoy)
		02:00		Industrial production	Dec		+6.2% (yoy)
		02:00		Fixed asset investment	Dec		+8.3% (ytd, yoy)
		02:00		Retail sales	Dec		+10.8% (yoy)
	GE	07:00		PPI	Dec		+0.3% (+0.1% yoy)
	US		♦	Donald Trump inauguration (Federal holiday)			
		01:00	♦	Fed's Yellen speaks in Stanford (speech is 1am GMT 20 Jan)			
	OPEC			OPEC meeting, Vienna (day 1 of 2)			

Further ahead

Jan	UK	Supreme court ruling on holding a parliamentary vote on triggering 'Article 50'
1 Feb	US	FOMC announcement
2 Feb	UK	MPC announcement (& press conference)
	EU19	ECB announcement

Key

♦ Key event indicator