

ECB's Visco and Coeuré on Possible Policy Action(s)

Summary | Today's News in Detail | Latest Issues of Sovereign Debt Update | Macroeconomic Forecasts | Recent Research

Summary

ECB's Visco and ECB Coeuré on possible policy action(s) – Mr. Visco noted that it is “*not obvious*” whether the ECB will need to take policy action in March, while Mr. Coeuré warned that the euro area is “*closer to the area where inflation expectations could be altered and create downside risks to price stability*”.

ECB's Praet warns about an overburdened ECB – Mr. Praet sees no risk of deflation, and describes the new banking supervision mandate as an “*immense challenge*”, repeating that he favours a more open communication policy.

Germany – Q4 GDP details confirmed 0.4%QQ growth. Net exports added 1.1pp to QQ GDP growth, investment up, private consumption down.

Germany – 2013 government budget posts a small surplus of 0.1% of GDP.

Germany – government to support giving Greece more discretion in third bailout, with the troika defining 20 “*major*” targets instead of 100 smaller projects.

France – labour costs reduction strategy could create 300,000 jobs and add 0.8% to GDP after five years.

France – business confidence unchanged at 100 in February (Mkt. 100, Citi 101). The broader business confidence measure was unchanged at 94 (Mkt. 95).

Italy – Renzi pledges a pro-business agenda before winning confidence vote in Senate, including a “*double-digit*” reduction in the labour tax wedge and a labour market reform.

Spain – PM Rajoy expected to present details on fiscal reform today, notes daily *Expansion*, and to discuss Catalonia's secessionist agenda.

Spain – PPI inflation falls to -1.8% YY in Jan from 0.6% YY in Dec. Falling food PPI likely to translate into lower food CPI in coming months.

Dutch house prices and building permits – house prices fell by 0.5% YY in January 2014, pointing to some stabilisation in price dynamics.

Greece – troika negotiations resume in Athens, but divisions reportedly remain on size of primary surplus and banks' capital needs.

Portugal – a precautionary credit may not be necessary, ESM chief Regling says, if the country builds up enough cash reserves as Ireland did.

25 February 2014

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With thanks to Antonio Montilla

Economics

Western Europe

Industrialised G7 Countries

Recent Research

Euro Economics Weekly — German Inflation: Lower For a Little Longer

21 February 2014

German inflation has been subdued recently, falling to 1.3% YY in January after 1.5% in 2013 and 1.6%pa in the 2000-2012 average. The weakness in German inflation has had two main drivers: First, ‘imported’ inflation has been very weak, deducting up to 1pp from CPI inflation over the last year. Second, domestic price pressures have remained low, as a sluggish economy held down wage pressures.

Ebrahim Rahbari | Guillaume Menuet | Giada Giani | Michael Saunders | Ann O'Kelly

UK Economics Weekly — Still Bullish on UK Growth

21 February 2014

We still expect above-trend (and above-consensus) real GDP growth, with below-target (and below-consensus) inflation for 2014-15. Consensus

See Appendix A-1 for Analyst Certification, Important Disclosures and non-US research analyst disclosures.

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Today's News in Detail

ECB's Visco and ECB Coeuré on possible policy action(s) – Bank of Italy Governor Ignazio Visco indicated in an interview with MNI that it is “*not obvious*” whether the ECB will need to take policy action in March. Mr. Visco argued that “*for the time being there is no deflation, so from that point of view there is not really any indication that we should rush to act*”. On the deposit rate, Mr. Visco remarked that “*if needed, we are ready also to consider going into negative territory with the deposit facility*”, adding that “*I do not think that the Danish experience is a negative experience*”. Executive Board Member Benoît Coeuré, in an interview with Slovenia newspaper *Delo* warned that the euro area is “*closer to the area where inflation expectations could be altered and create downside risks to price stability*”. Comment: these quotes suggest some differences of interpretation about the inflation outlook. Mr. Visco appears to be saying that the ECB has time, while Mr. Coeuré seems to be favouring earlier action, probably on the grounds that being pre-emptive will likely limit the need to be more ambitious later.

[>> Back to the Top](#)

ECB's Praet warns about risk of an overburdened ECB – ECB Executive Board member Peter Praet sees no risk of deflation, but acknowledged that elevated unemployment is dampening confidence across the euro area in an interview with *Le Soir* newspaper. Mr. Praet noted that the challenges to fix the euro area remain substantial, ranging from healthier public finances to structural reforms, with the ultimate aim being to avoid “*a lost generation*”. Mr. Praet complained in an interview with *Handelsblatt* that there is a clear risk of the ECB becoming overburdened by the demands placed upon it given “*the lack of EU institutions capable of acting*”. He described the ECB's new banking supervision mandate as an “*immense challenge*” and repeated that he was favourable to a more open communication policy. Comment: Not giving much away with 10 days to go before the next Governing Council meeting, but suggesting that progress is continuing on the publication of Minutes. We think that the Governing Council will respond to further evidence of its inflation mandate being undershot by lowering its main refinancing rate by 15bp to 10bp, but likely refrain from cutting the deposit rate on this occasion.

[>> Back to the Top](#)

Germany – Q4 GDP details confirmed 0.4%QQ growth, driven mostly by external demand. The detailed reading of Q4 GDP in Germany published by the National Statistical Office confirmed the initial reading of a 0.4% QQ increase, after an unrevised 0.3Q% QQ and 0.7% QQ in Q3 and Q2, respectively. External demand was the main driver of growth, with exports rising by 2.6% QQ, while imports only rose by 0.6% QQ and net trade added 1.1pp to GDP growth in the quarter. Investment grew strongly once again, at 1.4% QQ each for business investment and construction. However, inventories fell substantially, deducting 0.8pp from GDP growth, while private consumption also fell (by 0.1% QQ, the first fall since Q2 2011). In year-on-year terms, the Statistics Office reported that GDP was up by 1.3% in real terms and 3.4% in nominal terms. Comment: this GDP reading showed few signs of rebalancing in the German economy, with the large increase in exports the main driver of GDP growth – probably also a major factor in boosting the continued increase in business investment. However, for 2013 as a whole, the net export contribution in German GDP was roughly zero, making domestic demand the driver of GDP growth. We expect that domestic demand will also be the main driver of GDP growth in 2014-15.

[>> Back to the Top](#)

Germany – general government achieved small budget surplus in 2013.

expectations have been moving in this direction but, in our view, still have a lot further to go. We keep our GDP forecasts at 3.3% for 2014 and 3.2% in 2015, while cutting our Q4-14 CPI forecast to 1.6% YoY from 1.8% last month. We continue to expect the MPC will start to hike rates in Q4 of this year.

Michael Saunders | Ann O'Kelly

UK — Retail Sales Slip, Trend Solid

21 February 2014

The ONS report that retail sales volumes fell 1.5% MoM in January, midway between the consensus forecast (drop of 1.0%) and our forecast (drop of 2.0%). We regard this drop as the reversal of December's outsized gain (2.5% MoM) rather than a sign of adverse effects from the weather or deterioration in the underlying trend. Over the last three months, retail sales volumes rose 1.1% QoQ and 3.8% YoY - the highest YoY growth since 2005.

Michael Saunders

UK — Unemployment Ticks Up, Other Capacity Guides Tighten

19 February 2014

The ONS report that the jobless rate ticked up to 7.2% in Oct-Dec, a tenth above the consensus and two-tenths above our forecast. The split shows that the single-month jobless rate was 7.2% in December, slightly down from 7.4% in November but a little higher than the 7.1% figure for September. Job growth remains strong, with self-employment continuing to grow rapidly, while the numbers of full-time employees also is picking up quite strongly.

Michael Saunders

Scandi Economics Update — Swedish Financial Stability Council Calls for Additional Measures

25 February 2014

Sweden — Financial Stability Council: Additional financial stability measures needed — Moderates' Spring Budget Bill.

Norway — Government reiterates focus on competitiveness — Drop in consumer confidence in 1Q — Norges Bank Watch 2014 — FinMin:

Frankfurter Allgemeine Zeitung reports that the German general government achieved a small budget surplus for the second year in a row, according to data from the National Statistics Office. The surplus would amount to €300m or less than 0.1% of GDP but was better than projections of a small (0.1% of GDP) deficit. The social security fund achieved a surplus of €6.6bn and local authorities one of €3.5bn, while the federal state had a deficit of €6.8bn and the regional states of €3.0bn.

[>> Back to the Top](#)

Germany – government to support giving Greece more discretion in third bailout. *Die Welt* reports that the German government would support giving the Greek government more discretion in implementing reforms in the event of a third bailout, citing unidentified German government officials. The third bailout would define 20 “major” targets instead of 100 smaller projects, and allow the Greek government to decide on how to achieve those targets. According to the government source, the Greek government had not yet done enough to justify paying out the next tranche of the current bailout package, with troika officials returning to Greece yesterday.

[>> Back to the Top](#)

French labour costs reduction strategy could create 300,000 jobs – The High Council of Social Security Financing will review on Wednesday scenarios measuring the impact on GDP and jobs of a €10bn fall in employer labour charges. The first scenario envisages a uniform cut of 2 points in employer social security contributions (134k to 214k jobs), the second scenario would concentrate on medium wages up to 2.1 times the minimum wage (163k to 191k jobs) and the third scenario would target the lowest revenues up to 1.75 times the minimum wage (199k to 303k jobs). Business daily *Les Echos* notes that the report suggests that GDP could be 0.3% to 0.8% higher after five years across most scenarios, but warns that the impact of public spending cuts necessary to finance the measure has not been estimated in the calculation. Comment: we suspect that the government and social partners will probably favour the third scenario, concentrating the cut in labour charges on the lowest wages, given its greater potential in terms of job creation.

[>> Back to the Top](#)

French business confidence unchanged – French industrial sector confidence was stable at 100 in February (Mkt. 100, Citi 101). The important personal output perspectives series that is a good predictor of industrial production dynamics fell by one point to 9. The broader business confidence measure including retail, services, construction and wholesale was unchanged at 94 (Mkt. 95). Comment: this survey highlights the difficulties that the French industrial sector is experiencing, struggling with competitiveness issues and low profitability.

[>> Back to the Top](#)

Italy – Renzi pledges a pro-business agenda before winning confidence vote in Senate. The new Renzi government passed the first confidence vote in the Upper House last night, with 169 out of 308 votes. A second confidence vote is scheduled for today in the Lower House, and it should easily be passed by the new administration. The newly appointed PM pledged to implement several pro-business measures in the first three months of his mandate, including a “double-digit” reduction in the labour tax wedge, the repayment of all government arrears (estimated by the Bank of Italy at around €90bn, or 6% of GDP, before the recent repayments were made) and a labour market reform which would include a new universal unemployment benefit scheme. Renzi also promised a reform of the judicial system in June and to proceed with the electoral reform in parallel with the proposed constitutional changes to abolish the Senate (effectively delaying its implementation due to the long process to change the Constitution). Not many details were provided about how the tax cuts/higher unemployment benefits are

“Norwegian economy vulnerable”

[Tina Mortensen](#)

[>> Back to the Top](#)

intended to be financed), although Renzi promised to stick to sound public finances. Vice-PM Delrio was quoted by local media over last week-end saying that one option could be increasing capital gains tax on short-term government bonds (BOT) as a way of financing lower taxes on labour. Comment: the agenda is surely ambitious, but question-marks remain about Renzi's ability to implement it given a fragmented parliamentary majority. Centrist small coalition parties are against the proposed electoral reform which would force them back into large coalitions and there is still large opposition, including from within Renzi's own party PD, to broad-based spending cuts. A disappointing point in the agenda was in our view the absence of liberalisation in key service sectors, as these would have the largest impact in lifting GDP growth in Italy. Several references in his speech to the May European elections signal Renzi's wish to prove his reformist agenda quickly and ahead of the May electoral confrontation, amid polls currently suggesting PD is losing some support and anti-establishment M5S is gaining ground.

[>> Back to the Top](#)

Spain – PM Rajoy expected to present details on fiscal reform today during his annual report to Congress, daily *Expansion* noted. Mr Rajoy is also expected to focus on recent economic developments pointing to a stronger recovery, as well as to discuss Catalonia's secessionist agenda. In terms of the overhaul of the tax system, PM Rajoy has previously announced that his government is planning to introduce a series of gradual tax cuts starting in 2015, including changes to corporate and personal income taxes. The fiscal reform proposal is being prepared by a panel of experts. Comment: in our view the room for large tax cuts is almost absent, given poor elasticity of tax revenues to GDP at present. We expect the reform will likely include a reduction in nominal corporate taxes, but also an elimination of deductions, possibly implying an overall increase in the effective tax rate.

[>> Back to the Top](#)

Dutch house prices and building permits – CBS, the Dutch national statistics office indicated on Friday that house prices had fallen by 0.5% YY in January 2014, pointing to some stabilisation in price dynamics. On the month, prices were reported to have risen by 0.4% MM. The CBS added that house prices are now similar to their level 11 years ago, having fallen by some 20% since their August 2008 peak. The CBS added that the number of permits for new houses had fallen to a record low of 26,000 in 2013, amounting to falls of 30% compared to 2012 and 70% compared to 2008. Comment: these are increasing signs that the Dutch housing market is bottoming out. Given the high correlation between residential real estate prices and household spending, a large house price gain in 2014 would likely introduce some upside risks to our GDP baseline.

[>> Back to the Top](#)

Greece – troika negotiations resume in Athens, but divisions reportedly remain. Greek government spokesman Simos Kedikoglou reportedly said that the rift between Greek officials and the troika has been bridged considerably since talks were halted in December, but *Ekathimerini* reported that divisions remain on the size of a projected primary surplus for 2013 (with the lenders questioning some of the revenues recorded in the 2013 accounts) and on the implementation of the liberalisation measures. Moreover, the FT yesterday reported that an agreement cannot be found with the ECB and the IMF on the capital needs of the four Greek banks, with the Greek central bank claiming that these will not amount to more than €5-€6bn, while the IMF's internal estimate is reportedly of €20bn (11% of GDP). *Ekathimerini* reports that the Bank of Greece is set to announce the capital requirements of local banks by the end of this week or next week at the latest. Comment: the supposedly last round of bank recapitalisation was due to take place by the end of 2013 but is being delayed by the lack of agreement with the troika on the size and probably by the reluctance

of Greece to accept larger capital needs relative to the resources still available in the bailout package (some €7-€9bn according to the Bank of Greece estimate). Looming elections in May are a key obstacle for the Greek government to make any concession to the troika, amid polls suggesting the ruling party is trailing slightly behind the main opposition party SYRIZA.

[>> Back to the Top](#)

Portugal – a precautionary credit line may not be necessary, ESM chief

Regling says. *Diario economico* reports the head of the ESM saying that any ESM programme would require a memorandum and conditionality, and that if Portugal requests additional assistance this would most likely take the form of an Enhanced Conditions Credit Line (ECCL – an ECCL programme has tougher conditions relative to the blander PCCL or Precautionary Conditioned Credit Line). Regling said a new programme in the form of a precautionary credit line could be avoided if the country builds up a safety net of cash reserves (as Ireland did) ahead of the end of the current bailout programme (due to expire in May). Comment: requesting additional precautionary assistance would probably make more sense in economic terms for Portugal given the associated lower funding costs and still high funding needs in coming years. However, accepting additional conditionality is increasingly difficult politically, amid falling government bond yields and good market access in the past few months.

[>> Back to the Top](#)

Latest Issues of Sovereign Debt Update

ECB Waiting for More Information in March

24 February 2014

ECB stands ready to act, says Draghi. ECB's Praet on low inflation over the medium term. Buba's Weidmann on sterilisation and negative deposit rate. Claudia Buch to succeed Lautenschläger as Buba deputy head. Italy: Renzi's new government faces Senate confidence vote this afternoon. Italy's PDs lose support, M5S gain - latest polls. Moody's upgrades Spain to Baa2 with positive outlook. Spain's trade deficit shrinks, tourist arrivals rise. Greek government considers reducing number of MPs.

Guillaume Mennet | Giada Giani | Ebrahim Rahbari

Spain's Congress Rejects Catalonia's Proposal for Self-Determination Referendum

21 February 2014

Catalonia's proposed referendum rejected by Congress. IMF says Spain's aid programme has worked. Centre-left leads in polls for EP election. ECB wins ECJ ruling on Greek information. EA consumer confidence falls. German real wages fell in 2013. German energy minister Gabriel criticises EU Commission. German tax receipts up in Jan. Up to a quarter of Germans could retire early under new rules. Third Greek bailout may be avoided, says Dijsselbloem. Portugal's current account in surplus in 2013.

Ebrahim Rahbari | Antonio Montilla | Ann O'Kelly

New French-German FTT Proposal Due in May

20 February 2014

French-German revised FTT expected to focus on equities. EP's Bowles says "positive talks" with Greek EU Presidency on SRM. Buba's Weidmann says asset purchases could endanger central bank independence. Italy: Renzi concludes consultations, confidence vote expected Feb 24. Italy's growth slows in 1Q, says Confindustria. French CPI and PMI both lower than expected. Composite PMI rises in Germany, falls slightly in EA. Portugal's programme on track, says IMF. Greek current account in surplus.

EcoFin Approves Political Agreement with EP on Deposit Guarantee Schemes

19 February 2014

EU FinMins confirm political agreement with EU Parliament on deposit guarantee schemes. German FinMin reportedly offers to speed up pooling funds for SRM. EU FinMins start 2014 European Semester. Italy's Renzi finds broad support to form government - EU's Rehn calls on him to respect budget rules. Spain's NPL reach new high. BoS Governor says Spain's economy to grow only modestly. Portugal's debt sustainable, says PM. Slovenia sends restructuring proposal for state-owned bank to EC.

Ebrahim Rahbari | Antonio Montilla | Ann O'Kelly

No Negative Deposit Rate Without Refi Cut – Nowotny

18 February 2014

ECB's Nowotny says negative deposit rate would require refi rate cut too. As expected, no Eurogroup agreement on ESM direct bank recap or SRM. Italy's PM designate Renzi presents 100-day legislative agenda. EA FinMins reject new Greek aid before Aug. Spain's general govt debt at 93.7% of GDP in 2013. Spain's industrial orders rise strongly. Spain's energy tariff deficit rises more than expected. Portugal's PM rules out second bailout. Greece's central govt cash balance improves, deflation slows.

Ebrahim Rahbari | Antonio Montilla | Ann O'Kelly

[>> Back to the Top](#)

Macroeconomic Forecasts

European Economic Forecast Highlights — January 2014

23 January 2014

This companion to Global Economic Outlook and Strategy - January 2014 gives detailed quarterly forecasts for the main European countries to end 2015 and annual forecasts to 2018 for growth, inflation, current balance, fiscal balance, primary balance and government debt.

Ann O'Kelly | Michael Saunders | Guillaume Menuet | Giada Giani | Ebrahim Rahbari

Global Economic Outlook and Strategy — January 2014

22 January 2014

We are pushing up our global growth forecasts this month, and now look for global GDP growth (at current exchange rates) to rise from 2.5% in 2013 to 3.3% in 2014 and 3.4% in 2015, up by 0.1pp for 2013, 0.2pp for 2014 and 0.1pp for 2015 from our previous forecast. This year will, we expect, mark a return to sustained above-average global growth rates, whereas global growth has been below average for three consecutive years (2011-13) and indeed in five of the last six years.

Willem Buiter | Michael Saunders | Robert V DiClemente | Kiichi Murashima

Emerging Markets Macro and Strategy Outlook — The 'Fragile 5': A Progress Report

GEMS, Asia, CEEMEA, Global, Latin America – 24 January 2014

The 'F5' - Brazil, India, Indonesia, South Africa and Turkey - were at the heart of EM's underperformance in 2013, but investors have become more discriminating lately: the IDR, BRL and INR have been the best-performing EM currencies since the start of the year, while the ZAR and TRY have been the worst. We don't pretend to have a full 'theory' of how investors should discriminate among these

economies over the next few months, but some trends are becoming clear.

[Guillermo Mondino](#) | [David Lubin](#) | [Johanna Chua](#)

[>> Back to the Top](#)

Appendix A-1

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