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Developed Markets
Western Europe

Euro Economics Weekly

Low-flation Is Here To Stay*

- The ECB has once again revised its 2014 inflation forecast lower to 0.6%, 0.1pp lower than in June, 0.5pp lower than in Dec-13. Declining commodity prices surely contributed to the inflation undershoot, but we reckon the ECB Staff Projections also largely misjudge the dynamics of core inflation. The new September forecasts still foresee core inflation starting to rise quite speedily, as soon as Q4 14.

- With annual unit labour cost growth around 1%, a large output gap and likely second-round effects from previous commodity price declines and the euro appreciation, we instead expect core inflation to trend slightly lower in 2015. Overall inflation will probably continue undershooting the ECB's projections. This will likely be a key factor, in our view, in their decision to undertake additional monetary policy easing in coming quarters.

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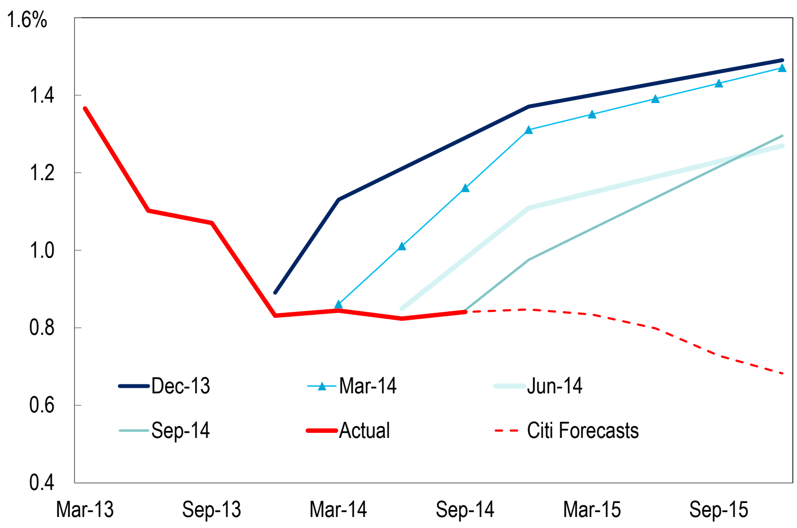
Figure 1. Citi Forecasts

	$/€	Euro Repo	10-yr Bunds	£/€	UK Bank Rate	10-Yr Gilt Bund
4Q 14	1.34	0.05	0.75	0.80	0.50	177
2Q 15	1.33	0.05	1.25	0.79	1.00	177

Source: Citi Research

Figure 2. Euro Area HICP Core Inflation (YY) – ECB Staff Projections in Dec-13, Mar-14, Jun-14 and Sept-14



Note: Core inflation is defined as HICP ex energy, food, alcohol and tobacco.
Sources: ECB Staff Projections and Citi Research

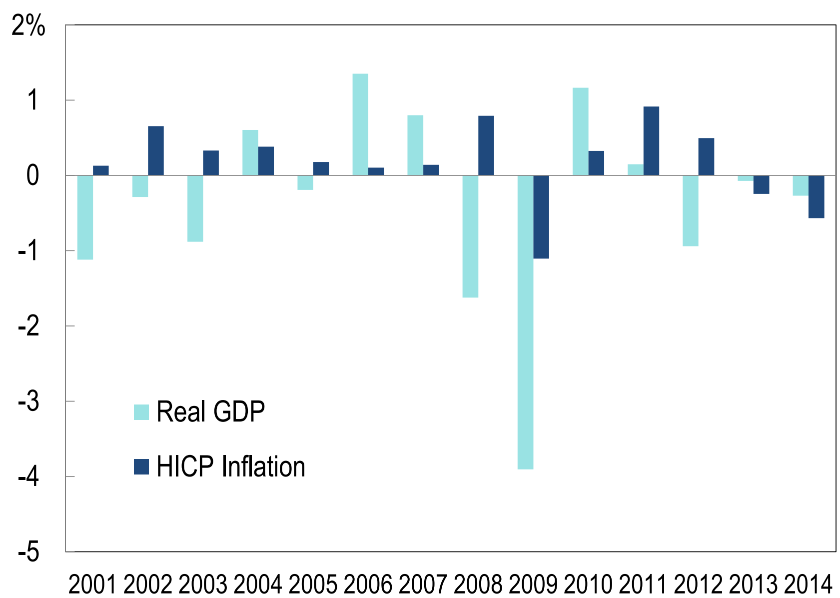
*CORRECTION: Original version showed incorrect Euro Repo rates in Figure 1; these have now been amended.

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

Low-flation Is Here To Stay

2014 inflation set to show largest undershoot relative to ECB forecasts since 2009. The September ECB Staff Projections released this week have once again revised their 2014 average inflation forecast downward to 0.6%, from 0.7% in June and from 1.1% in Dec-13. The 2015 and 2016 forecasts were left unchanged at 1.1% (but still lower than 1.3% estimated last December) and 1.4%, respectively. With the exception of 2009, 2014 will probably record the largest negative forecast error for the ECB inflation projections relative to the prior December estimate since they started being published in 2000 (with an error of 0.5pp if their new forecast is correct, by 0.6pp if our forecast of 0.5% is right) (see Figure 3). In Dec-12 the Staff Projections also overestimated the 2013 inflation outcome, by 0.3pp. This is quite unusual for the ECB as inflation has generally overshot their forecasts up until 2012, with the prior December estimate displaying an average forecasting error of around +0.3pp between 2001 and 2012.

Figure 3. ECB Staff Projections – Errors in Real GDP and Inflation Forecasts (YY), 2001-2014



Note: The forecast error is the difference between realized annual HICP inflation and GDP growth in year t minus the ECB Staff Projections for inflation and GDP made in December of year t-1.
Sources: ECB Staff Projections and Citi Research

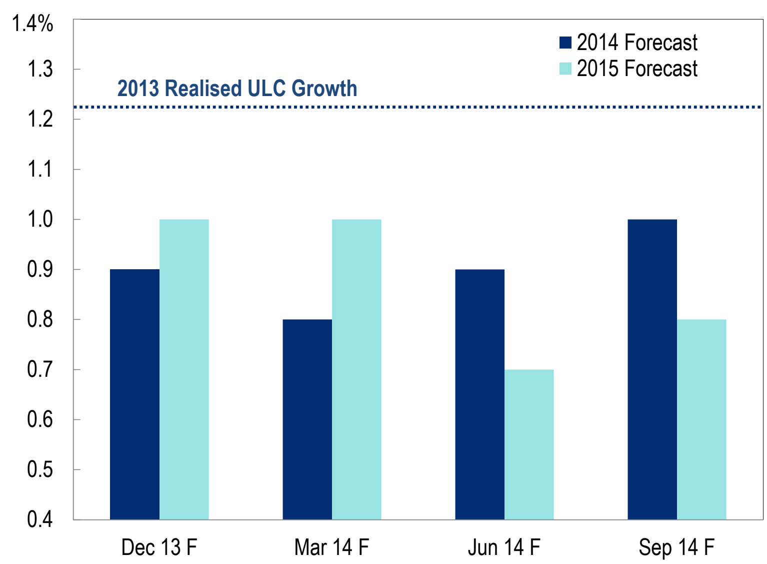
Lower commodity prices mattered, but only to a certain extent. One may argue, as ECB President Draghi did once again at this week's press conference, that the recent inflation undershoot relative to forecasts has been driven by the unexpected, commodity-led, drop in energy and food prices. We agree with this explanation, but only to a certain extent. We have also revised down our 2014 inflation forecast since last December by some 0.4pp because of lower energy and food prices. However, we reckon that, over the past year at least, the ECB Staff Projections have also largely misjudged the underlying dynamics of core inflation.

The theoretical reason to compute core inflation measures is that by excluding the most volatile and/or mainly exogenously-determined items of the basket (generally energy and food prices), one obtains a smoother and more reliable measure of underlying inflationary pressures. Therefore, core inflation is important as a guide for future inflation trends, as it could be seen as the 'anchor' around which headline inflation fluctuates. A lower/higher short-term trajectory for core inflation tends to imply a lower/higher headline inflation forecast one to two years ahead.

Core, not just headline, has largely undershot the ECB forecasts. Since last December the ECB has been publishing its core (ex-energy, food, alcohol and tobacco HICP) inflation forecasts, in addition to the headline figures, alongside a series of other inflation indicators (core HICP inflation net of indirect tax changes, wage, productivity and unit labour costs growth). Figure 2 on the front page reproduces the expected path for core inflation in the ECB forecasting rounds over the past year[1]. Since last December, the ECB has been expecting core inflation to reverse its downward trend and start rising quite speedily from the quarter immediately after the forecasting exercise. In practice, core inflation repeatedly undershot these expectations. In the new September forecasts, the Staff Projections still foresee the core rate to start rising from Q4 14, if the annual core inflation averages of 0.9% in 2014 and 1.2% in 2015 are to be matched.

Core inflation forecast revisions not mirrored into ULC forecast revisions. It is worth noting that the downward revisions to the core inflation rate over the past year did not reflect similar revisions to the assessment for labour market gauges of inflationary pressures. The 2014 unit labour cost (ULC) growth forecast has actually been revised marginally higher from 0.8% in March to 1.0% in September. 2015 ULC growth is still seen at a very subdued pace of 0.8% (see Figure 4). With annual ULC growth below or around 1%, a large output gap and still likely second-round effects from past commodity price declines and the euro appreciation, we reckon that the ECB's core inflation forecasts have been (and remain) way too high. We suspect the ECB's inflation forecasting model (similarly to many other central banks' models) assigns a high coefficient to inflation expectations which persistently drives inflation rates back towards the targeted or expected level (around 2% for the euro area), reducing the importance of other determinants of the inflation dynamic.

Figure 4. Euro Area Unit Labour Costs (YY) – Actual and ECB Staff Projections for 2014 and 2015 in Dec-13, Mar-14, Jun-14 and Sept-14



Sources: ECB and Citi Research

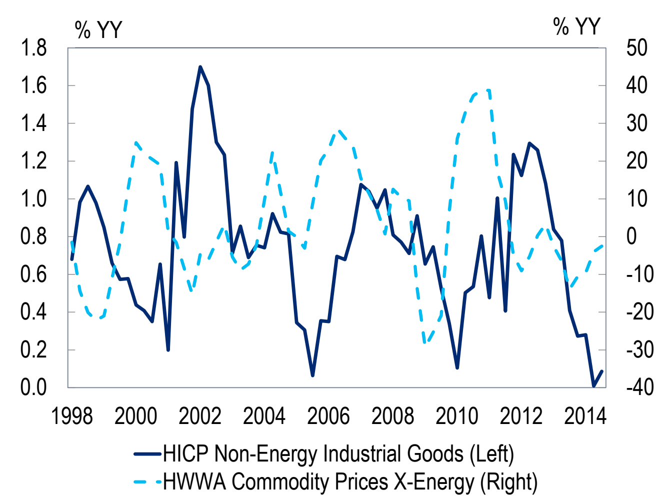
[1] As the ECB forecasts are presented only in terms of annual averages, to reproduce the likely quarterly profile we assumed a linear path for the YY core inflation rate consistent with the projected annual average and with the starting point at the time of the forecasting exercise.

A Two-Way Causality between Headline and Core

Core is the ‘anchor’ for headline, but headline also influences core. As noted above, misjudging the short-term profile for core inflation has meaningful implications for the one-year or even two-year ahead inflation forecasts, as core is generally seen as the ‘anchor’ around which headline fluctuates. At the same time, however, price fluctuations in volatile non-core items should not completely be disregarded as they also tend to feed through gradually into core prices. So, for example, lower oil prices tend to translate into lower petrol prices within one or two months, but they may also gradually affect prices of industrial products via lower input costs. In addition, a varying degree of price indexation to past headline inflation in some European countries also implies that eventually core prices are affected by realised headline rates. Finally, household and business inflation expectations tend to be affected mainly by the prices of frequently purchased items, which happen to be the same volatile items (eg, energy and food) that are excluded from the core measures. To the extent that inflation expectations affect future spending/pricing decisions, this reinforces the causal link from current headline to future core inflation rates.

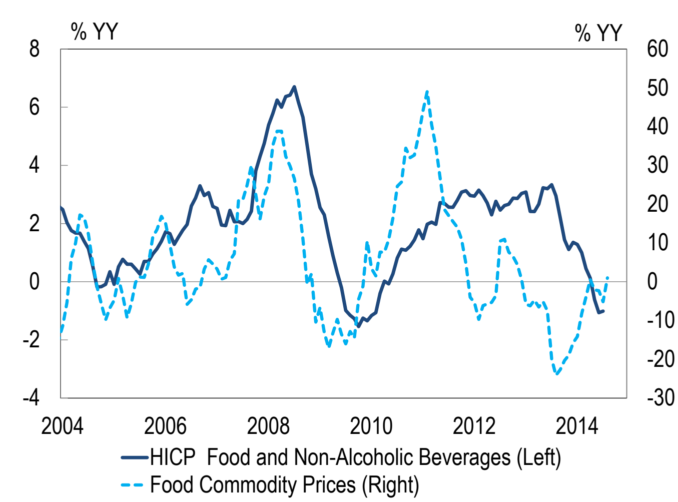
Second-round effects are important in shaping core inflation dynamics. Empirical evidence confirms that changes in energy and food prices have proven to be important drivers of future core inflation developments in the euro area over the past decade or so. The correlation between (euro-denominated) non-energy commodity prices and the non-energy industrial goods HICP is maximised at a five-quarter lag (see Figure 5). Using a simple econometric model for core inflation, we estimate that a 10% drop in non-energy commodity prices translates into a lower core rate by 0.1pp after five-to-six quarters. The estimated elasticity of core to energy commodity prices is similar, but with a slightly longer lag. The ECB’s likely failure to fully capture these second-round effects after the significant and broad-based decline in a whole range of commodity prices (in euro terms) over the past two years may have been an important factor explaining the inflation undershooting relative to their forecasts in recent quarters.

Figure 5. Euro Area – Non-energy Industrial Goods HICP and Euro-Denominated Non-Energy Commodity Prices, 1998-Aug 14



Sources: Eurostat, ECB, Haver Analytics and Citi Research

Figure 6. Euro Area – HICP Food and Food Commodity Prices, 2004-Aug 14



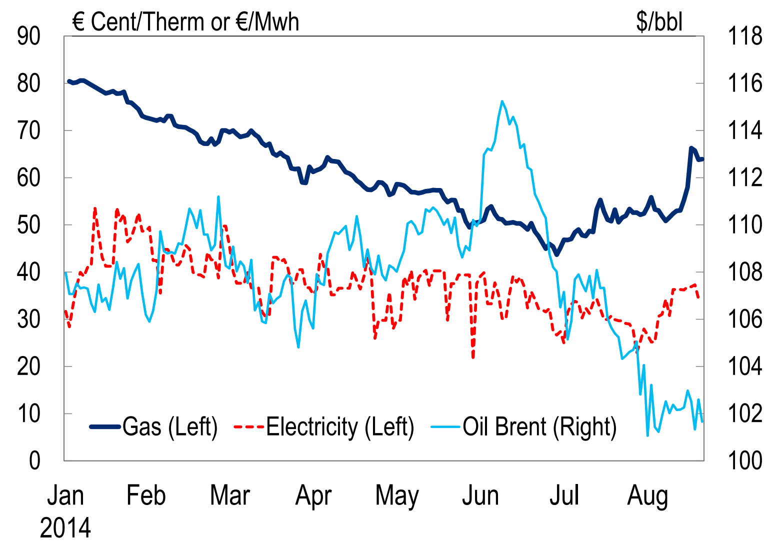
Sources: Eurostat, ECB, Haver Analytics and Citi Research

The inflation outlook

We expect August to mark the cyclical trough for headline inflation at 0.3% YY. Energy prices have in general stabilised over the past month or so, with upside pressures actually emerging in very recent days in gas prices related to the Russia/Ukraine situation (see Figure 7). These should translate into higher energy utility bills during the autumn months. Together with adverse base effects (energy prices were falling in the autumn months of 2013), this will probably push the YY rate in the energy component from October onwards back towards zero by year-end (from -2% YY in August).

Similarly, the **sharp drop in food price inflation seems to have bottomed out** in the Jul-Aug HICP prints (see Figure 6). Food commodity prices had rebounded during the spring, although partly reversed those gains in the past three months. The weather-related ample supply of fruit and vegetables during the spring/summer months should come to an end soon, despite recent speculation about a potentially large impact from the Russian food import ban on the affected products. We estimate the impact of the ban on aggregate food prices to be very small (see Box at the end of this section).

Figure 7. Euro Area – Selected Commodity Energy Prices, Jan-Aug 2014



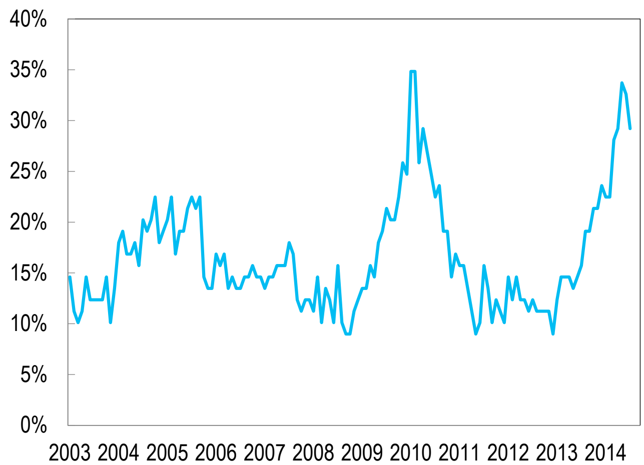
Note: Gas prices are prices at the Zeebrugge hub, 1st expiring contract, € Cent/Therm. Electricity prices are Conti Power Index, €/Mhw. Oil Brent prices, USD/bbl, 1st expiring contract.
Sources: Haver Analytics and Citi Research

Core inflation, on the other hand, has probably not reached its cyclical bottom in our view, in contrast to the ECB's baseline that the downtrend is about to reverse soon. We think the pickup in the core rate in August to 0.9% YY is temporary and driven mainly by a different summer sale calendar in some member states relative to last year (and hence likely to be reversed in September/October).

Underlying inflationary pressures are still easing. We note that other gauges of underlying inflationary pressures aside from the ex-energy and food core inflation rate have continued to ease in the last few months. For example, we monitor the share of the HICP items displaying a negative YY inflation rate (using a 90-item disaggregated split of the HICP). At 34% this share has increased until May to closely match the 2009 peak, before falling slightly in Jun and Jul (see Figure 8). The median YY HICP rate (using the same 90-item disaggregated split of the HICP)

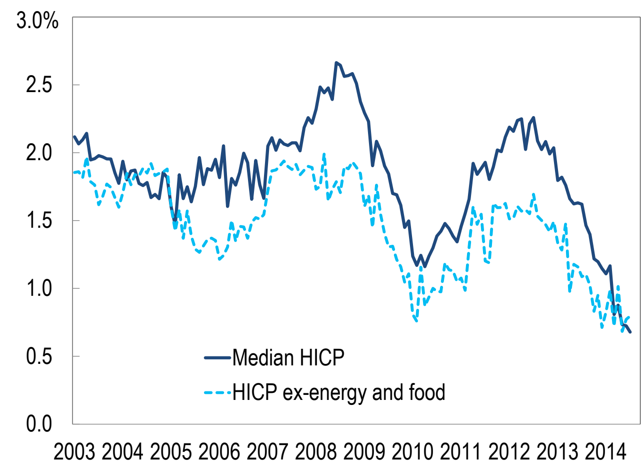
has also continued to trend lower to 0.7% in July, from 1.2% in October 2013 (see Figure 9).

Figure 8. Euro Area – Share of HICP Items With Negative YY Inflation Rate, 2003-Jul 14



Note: the share is computed using a 90-item disaggregated split of the HICP.
Sources: Eurostat, Citi Research

Figure 9. Euro Area – Median HICP and Core Inflation (YY), 2003-Jul 14



Note: the median HICP is computed using a 90-item disaggregated split of the HICP.
Source: Citi Research

Based on the evidence shown in the previous section, we reckon there could still be **some room for second-round effects from past declines in commodity prices to affect core inflation**. Non-energy commodity prices have bottomed out in Q1 14, but the YY rate was still -0.7% in August. Energy commodity price growth was still negative in YY terms in August, although gas prices have risen in recent days.

In addition, **the appreciation of the euro since mid-2012 may not have entirely fed through into consumer prices.** Our model suggests that exchange rate moves impact core inflation with a lag of 6-to-10 quarters. This is similar to some ECB estimates, which indicate that a 10% appreciation of the trade-weighted euro reduces HICP inflation by only 0.2pp in the first year, but by a larger 0.5pp *both* in the second and third year after the shock (with an estimated cumulated effect on the HICP index level of 1.0-1.5pp after three years).[2] This would entail 2014 and 2015 inflation rates to still be negatively affected by the past appreciation of the euro. The 3% depreciation of the effective exchange rate since the March 2014 peak only amounts to barely a third of the 9.4% appreciation of the preceding 21 months.

The **other usual drivers of core inflation also point to persistent downside pressures.** The output gap is still negative and probably quite large, although its actual size may be debatable.[3] Wage growth was still easing in Q1 14, and historically turning points in wage growth have preceded those in core inflation. Overall, we still expect core inflation to drift slightly lower in 2015, in line with the indications of our econometric model. True, the reliability of the model (based on historical relationships) may be questioned the further core inflation moves away from its historical average (of around 1.5% since 2000) and from the central bank target. On the other hand, the model has been a very useful predictor of the downtrend in core inflation until now and we remain confident that the imminent turnaround foreseen in the ECB forecasts will prove once again overly optimistic.

[2] See "The Changing Role of the Exchange Rate in a Globalised Economy", ECB Occasional Paper No 94, Sept 2008.

[3] See "Euro Economics Weekly: The Rise of The Output Gap", 4 April 2014, Citi Research.

We see inflation continuing to undershoot the ECB projections. In sum, we estimate headline inflation to rise only modestly to 0.6% YY by the end of this year. We expect the headline rate to move higher only very slowly in 2015 – annual average estimated at 0.9% YY – and to remain not far from the 1% mark also in 2016, at 1.2%. We see inflation continuing to undershoot the ECB projections (Staff Projections: 1.1% in 2015, 1.4% in 2016). This should be a key input in what we expect to be a decision to undertake more monetary policy easing in coming quarters.

ECB changed its risk assessment on price outlook. We note that the ECB's introductory statement no longer makes the usual reference to the risks to the outlook for price developments as *"limited and broadly balanced over the medium term"*. Instead the September statement says that Governing Council will *"continue to closely monitor the risks to the outlook for price developments"* focusing their attention on the possible repercussions of *"dampened growth dynamics"* and the *"pass-through of our monetary policy measures"*. This change of emphasis suggests to us that the Governing Council will be in a position to act again soon, especially if surveys were to continue to paint a weak economic recovery and market-based inflation expectations were to diverge from the ECB's medium-term target in coming months.

On August 7, 2014, Russia announced the introduction of an import ban on certain meat, fish, dairy, fruit, vegetables and processed food products from the EU, USA, Canada, Australia and Norway. The approximate value of euro area exports of these products to Russia in 2013 was about €2.9bn, based on our calculations. This compares with euro area total (intra and extra EU) exports of these same products of around €108bn, i.e. 2.7% of the total. In addition, we compute total domestic consumption of these products amounted to €464bn at aggregate euro area level in 2013 (we derive this figure using the weight of the banned products in the HICP basket – 8.4% – and multiplying it by total household spending in nominal terms). Therefore, the implied demand affected by the ban amounts to only some 0.5% of total final demand (domestic plus external) for the banned products (disregarding extra-EU imports which should be fairly small). 0.5% should approximately be the extent of oversupply on euro area markets for these products. Even for small, food-exporter countries such as Greece, this share increases only to 0.7%. We reckon oversupply of this magnitude is hardly going to have a meaningful impact on the prices at the aggregate euro area level. Any impact is going to be reduced also by the measures adopted by the EU Commission over the past month to withdraw oversupply in the affected markets.

Figure 10. Key Economic Indicators (8 September – 12 September 2014)

Monday 8 September		Forecast	Last
06:45	Switzerland: Unemployment, Aug		
07:00	Germany: Trade Balance, Jul		
07:00	Germany: Labour Cost Index, 1Q		
07:30	France: Bank of France Business Sentiment, Aug	95	96
08:15	Switzerland: Consumer Prices, Aug		
08:15	Switzerland: Retail Sales, Jul		
09:30	Euro Area: Sentix Investor Confidence, Sep		
11:00	Portugal: GDP Details, 2Q		
Tuesday 9 September		**Forecast**	**Last**
07:45	France: Trade Balance, Jul		
07:45	France: Budget Balance, Jul		
08:30	Netherlands: Industrial Production, Jul		
09:30	UK: Trade Balance – Goods & Services, Jul	£-2.2 Billion	£-2.5 Billion
09:30	UK: Industrial Production, Jul	0.4% MM, 1.5% YY	0.3% MM, 1.2% YY
	Manufacturing Output, Jul	0.5% MM, 2.4% YY	0.3% MM, 1.9% YY
10:00	Greece: Industrial Production, Jul		
Wednesday 10 September		**Forecast**	**Last**
07:45	France: Nonfarm Payrolls, 2Q Final	0.1% QQ, 0.0% YY	-0.1% QQ, -0.3% YY
07:45	France: Industrial Production, Jul	-1.0% MM, -0.9% YY	1.3% MM, -0.4% YY
	Manufacturing Production, Jul	-1.0% MM, -0.3% YY	1.6% MM, 0.1% YY
08:00	Spain: Industrial Production, Jul	1.8% YY	0.5% YY
09:00	Norway: Consumer Prices, Aug	-0.2% MM, 2.2% YY	0.7% MM, 2.2% YY
	CPI-ATE, Aug	-0.3% MM, 2.4% YY	0.6% MM, 2.6% YY
10:00	Greece: Consumer Prices, Aug		
Thursday 11 September		**Forecast**	**Last**
00:01	UK: RICS House Price Survey, Aug		
07:00	Germany: HICP, Aug Final	0.0% MM, 0.8% YY	0.3% MM, 0.8% YY
	National CPI, Aug Final	0.0% MM, 0.8% YY	0.3% MM, 0.8% YY
07:00	Sweden: PES Unemployment Rate, Aug	4.4%	4.3%
07:45	France: HICP, Aug	0.3% MM, 0.4% YY	-0.4% MM, 0.6% YY
	Consumer Prices, Aug	0.3% MM, 0.3% YY	-0.3% MM, 0.5% YY
	CPI Ex Tobacco Index, Aug	126.22	125.81
08:30	Sweden: LFS Unemployment Rate, Aug	7.2% NSA, 7.7% SA	7.1% NSA, 7.7% SA
08:30	Sweden: Consumer Prices, Aug	-0.1% MM, -0.2% YY	-0.3% MM, 0.0% YY
	CPIF, Aug	-0.1% MM, 0.4% YY	-0.2% MM, 0.6% YY
08:30	Sweden: Average House Prices, Aug		
09:00	Euro Area: ECB Monthly Bulletin		
10:00	Greece: Unemployment Rate, Jun		
11:00	Ireland: Consumer Prices, Aug		
Friday 12 September		**Forecast**	**Last**
	Euro Area: Informal EcoFin Meeting of EU Finance Ministers, Milan (to Sep 13)		
07:45	France: Balance of Payments, Jul		
08:00	Spain: HICP, Aug Final	-0.5% YY	-0.4% YY
08:30	Netherlands: Trade Balance, Jul		
09:00	Italy: Industrial Production, Jul	-0.5% MM	0.9% MM
09:00	Norway: Norges Bank Regional Network Report		
09:30	UK: Construction Output, Jul		
10:00	Italy: Consumer Prices, Aug Final		
10:00	Euro Area: Industrial Production, Jul	0.2% MM	-0.3% MM
10:00	Euro Area: Employment, 2Q		
11:00	Ireland: Trade Balance, Jun		
	Euro Area: Informal Meeting of EA Finance Ministers, Milan		
During the Weekend		**Forecast**	**Last**
	EU: Informal Meeting of EU Finance Ministers, Milan		
Sep 14	Sweden: General Election		

Sources: National statistical offices, central banks and Citi Research

Figure 11. Economic Indicators – Comments: Euro Area, Germany, France, Italy and Spain

Euro Area

Sep 12 10:00 London Time	***Industrial Production, Jul***	**Forecast: 0.2% MM**	**Prior: -0.3% MM**

Industrial output likely expanded marginally in July, after two consecutive declines (-0.3% MM in June, -1.1% MM in May). The unusual calendar of holidays in May/Jun has induced some higher-than-normal volatility at the country level in recent months. But the underlying trend is clearly weakening relative to 4Q13/1Q14, in line with the indications from the manufacturing PMI.

Germany

Sep 11 07:00 London Time	***HICP, Aug Final***	**Forecast: 0.0% MM, 0.8% YY**	**Prior: 0.3% MM, 0.8% YY**
	National CPI, Aug Final	**Forecast: 0.0% MM, 0.8% YY**	**Prior: 0.3% MM, 0.8% YY**

We expect the final readings for German inflation in August to confirm the flash readings for both the national definition and the HICP at 0.8%. The August reading therefore left inflation stable compared to July and was in line with market expectations, but the uptick in the inflation readings for most of the individual states that reported suggest that a small uptick for the nationwide index may have been only narrowly avoided. For now, the CPI on the national definition remains at its lowest level since January 2010 (the HICP was weaker in May 2014), and the decline in recent months is mostly accounted for by reductions in energy prices.

France

Sep 8 07:30 London Time	***Bank of France Business Sentiment, Aug***	**Forecast: 95**	**Prior: 96**

The Bank of France sentiment survey of the industrial sector is likely to record a second successive one-point drop in August to 95 (-0.5 SD). With the flash manufacturing PMI reported to have declined for a fifth successive month in August to a 15-month low and the INSEE industrial confidence survey having revealed a one-point drop to an 11-month low, we would be surprised if the BdF survey were to behave much differently. Note that news of the French government reshuffle would have been too recent to be incorporated in the survey.

Sep 10 06:30 London Time	***Non-Farm Payrolls, 2Q Final***	**Forecast: 0.1% QQ, 0.0% YY**	**Prior: -0.1% QQ, -0.3% YY**

We expect the second estimate to confirm that the French economy created private sector jobs for the second time in the past four quarters. The services sector was the only provider of new jobs (+32.3k) although many originated from the interim sector. The construction and industry sector shed jobs for the 9th and 13th successive quarters, respectively, while public sector employment likely remained stable. With surveys suggesting little confidence in the government's ability to steer the economy towards a higher activity path and fiscal tightening in 2015 still in the pipeline, it remains difficult to envisage much acceleration in French GDP growth in the second half.

Sep 10 07:45 London Time	***Industrial Production, Jul***	**Forecast: -1.0% MM, -0.9% YY**	**Prior: 1.3% MM, -0.4% YY**
	Manufacturing Production, Jul	**Forecast: -1.0% MM, -0.3% YY**	**Prior: 1.6% MM, 0.1% YY**

We look for a drop in industrial production in July after a sizeable uptick in June. Anecdotal evidence ranging from a clear drop in capacity utilisation (lowest in 14 months), a three-month low in industrialists' assessment of recent output and a ten-month low in the ratio of orders to stocks points to a lower entry point for the third quarter, highlighting downside risks to our modest uptick in Q3-14 GDP. More constructive government announcements relating to supply side reforms and the need to support businesses should help, later in the second half.

Sep 11 07:45 London Time	***CPI – EU Harmonised, Aug***	**Forecast: 0.3% MM, 0.4% YY**	**Prior: -0.4% MM, 0.6% YY**
	Consumer Prices, Aug	**Forecast: 0.3% MM, 0.3% YY**	**Prior: -0.3% MM, 0.5% YY**
	CPI Ex Tobacco Index, Aug	**Forecast: 126.22**	**Prior: 125.81**

The HICP headline inflation rate is expected to hit a new cycle low of 0.4% YY in August. A similar trend is expected for the CPI inflation rate set to fall to a 58-month low of 0.3% YY. Prices are expected to rise in August (+0.3% MM), driven by higher manufacturing goods prices at the end of the summer discounting period. But volatile prices such as energy and food are expected to have fallen in August. Core CPI inflation likely stabilised around 0.6% YY, its lowest level since Mar-11. While favourable base effects are expected to push inflation rates modestly higher in the fourth quarter, the outlook for inflation will likely remain muted in 2015, averaging around 1.1% in our baseline.

Italy

Sep 12 09:00 London Time	***Industrial Production, Jul***	**Forecast: -0.5% MM**	**Prior: 0.9% MM**

Industrial output in July likely reversed the June gain, declining by 0.5% MM. The manufacturing PMI has been falling since April and in August actually slipped below the 50 mark. We reckon the manufacturing sector likely remained in recessionary territory in 3Q, due to weak export growth and lacking domestic demand. GDP is likely to have stagnated in 3Q, after contracting in both 1Q and in 2Q.

Spain

Sep 10 08:00 London Time	***Industrial Production, Jul***	**Forecast: 1.8% YY**	**Prior: 0.5% YY**

Fairly strong survey data (manufacturing PMI stood at 53.9 in July, 0.7 sd above its long-term average) suggest industrial production probably bounced back in July – we project by 0.9% MM after falling by 0.8% MM and 0.6% MM in June and May, respectively. We expect this will translate into a YY figure (WDA) in July of +1.8% (vs. +0.5% in June). Going forward, rises in both new and existing orders suggest that further output growth is likely in coming months.

Sep 12 08:00 London Time	***HICP, Aug Final***	**Forecast: -0.5% YY**	**Prior: -0.4% YY**

According to the flash estimate, inflation fell further to -0.5% YY in August (from -0.4% in Jul), the lowest YY growth since Oct 2009. We think lower fuel prices together with adverse base effects have likely pushed the YY inflation rate in the energy component into negative territory in August, while further weak dynamics in fresh food prices may have also continued. We expect core CPI inflation (excluding fresh food and energy) to have remained broadly unchanged in August (at -0.1% YY recorded in July). August should represent the trough in the inflation profile for 2014, but we project HICP inflation to remain close to zero on average this year.

Sources: National Statistical Offices, National Central Banks, Bloomberg, and Citi Research forecasts

Figure 12. Economic Indicators – Comments: Sweden, Norway and UK

Sweden			
Sep 11 07:00 London Time	***PES Unemployment Rate, Aug***	**Forecast: 4.4%**	**Prior: 4.3%**
	Short-term indicators point to ongoing improvement on the labour market ahead. In line with the seasonal pattern, we expect the registered unemployment rate to rise in August.		
Sep 11 08:30 London Time	***LFS Unemployment Rate, Aug***	**Forecast: 7.2% NSA, 7.7% SA**	**Prior: 7.1% NSA, 7.7% SA**
	Unemployment on the LFS measure finally seems to be trending lower after being higher than expected during the first half of the year. Such a development is also well in line with the downward trend in registered unemployment according to the unemployment offices' statistics. Ahead, lead indicators suggest that the labour market will continue to improve.		
Sep 11 08:30 London Time	***Consumer Prices, Aug*** **CPIF, Aug**	**Forecast: -0.1% MM, -0.2% YY** **Forecast: -0.1% MM, 0.4% YY**	**Prior: -0.3% MM, 0.0% YY** **Prior: -0.2% MM, 0.6% YY**
	With the July reading, actual core inflation has been in line with or above consensus expectations for four consecutive months, supporting our view that Sweden has passed the period of ultra-low inflation readings, which dominated at the outset of the year. Food prices explained the slightly higher than expected inflation outcome in July. CPIF remained 0.2 percentage points above the Riksbank's forecast, but with international prices on both food and petrol having declined over the last 1-2 months CPIF inflation will likely return to the Riksbank's forecast over the next 2-3 months. The decline in food prices has accelerated after Russian import restrictions, suggesting that risks for inflation towards the end of the year are skewed to the downside.		
Sep 11 08:30 London Time	***Average House Prices, Aug***		
	Real estate prices for one- or two-dwelling buildings increased by more than 32% during the three-month period May–Jul 2014, compared to the previous period Feb-Apr 2014. In annual terms, home prices gained 6% during the last three month period May-Jul 2014, compared to the same period a year earlier. House prices have increased gradually since 2013, and the uptrend looks set to continue this year; short-term indicators point to ongoing upward near-term pressures. Ahead, we expect house prices gradually to level out next year with macroprudential measures restraining lending and the Riksbank starting to hike rates in early-2016. With the focus back on inflation, we do not expect a continued moderate increase in housing (and lending) will have immediate implications for monetary policy.		
Norway			
Sep 10 09:00 London Time	***Consumer Prices, Aug*** ***CPI-ATE, Aug***	**Forecast: -0.2% MM, 2.2% YY** **Forecast: -0.3% MM, 2.4% YY**	**Prior: 0.7% MM, 2.2% YY** **Prior: 0.6% MM, 2.6% YY**
	Core inflation surprisingly inched higher in July, to stand at an above-target rate of 2.6% YY. July is normally a month where inflation declines due to strong seasonal effects, e.g. summer sales of clothing. Combined with base effects from the sharp acceleration a year ago, we (and Norges Bank) had expected a rather marked downshift in annual inflation in July this year. Instead, headline inflation jumped 0.7% MM amid soaring food prices, and, in turn, lifted the annual rate by 0.3pp to 2.2% YY. Ahead, food inflation will likely outweigh Norges Bank's expectations, pointing to an upward revision of the Bank's CPI forecast (and, hence, the conditional interest rate path) in the upcoming September MPR. Combined with firm economic activity indicators since the June monetary policy meeting, a rate cut should be off the agenda.		
Sep 12 09:00 London Time	***Norges Bank's Regional Network Report***		
	The June Regional Network Report (resembles the Fed's Beige Book) showed a slight improvement in output momentum in the Norwegian economy over the past three months (0.87 vs. 0.68 in Mar), marginally in excess of expectations back in March (of 0.82). Meanwhile, the report suggested only minimal improvement in the coming six months (from 0.87 in May to 0.89). In line with the improvement in monthly activity data of late, we expect the upcoming RNR to be a tad more upbeat than in June.		
United Kingdom			
Sep 9 09:30 London Time	***Trade Balance – Goods & Services, Jul***	**Forecast: £-2.2 Billion**	**Prior: £-2.5 Billion**
	The trade deficit has averaged £2.1bn per month so far this year, slightly down from £2.4bn per month in 2013 and £2.8bn in 2012. Although the growth of exports of goods is sluggish, import volumes have been flat, while import prices are falling and the surplus on trade in services is rising. We look for the July figure to be similar to the average of the year to date.		
Sep 9 09:30 London Time	***Industrial Production, Jul*** ***Manufacturing Output, Jul***	**Forecast: 0.4% MM, 1.5% YY** **Forecast: 0.5% MM, 2.4% YY**	**Prior: 0.3% MM, 1.2% YY** **Prior: 0.3% MM, 1.9% YY**
	Manufacturing output already has expanded for five quarters in a row, and business surveys suggest that output continues to expand rapidly. Accordingly we look for another solid monthly gain and such a figure would already put IP in July 0.3%-0.4% above the 2Q average – hence pointing to another quarter of solid growth.		

Sources: National Statistical Offices, National Central Banks, Bloomberg, and Citi Research forecasts

Figure 13. Key Economic Indicators (15 September – 19 September 2014)

		Forecast	Last
During The Week		**Forecast**	**Last**
07:00	Germany: Insolvencies, Jun (by Sep 17)		
Monday 15 September		**Forecast**	**Last**
08:15	Switzerland: Producer & Import Prices, Aug		
08:30	Netherlands: Retail Sales, Jul		
09:00	Norway: Trade Balance, Aug		
10:00	Euro Area: Trade Balance, Jul		
Tuesday 16 September		**Forecast**	**Last**
08:00	Spain: Labour Costs, 2Q		
09:30	UK: Consumer Prices, Aug	0.3% MM, 1.4% YY	-0.3% MM, 1.6% YY
	CPI Ex Food, Drink, Tobacco, Energy, Aug	0.4% MM, 1.7% YY	-0.4% MM, 1.8% YY
	Retail Prices, Aug	0.4% MM, 2.4% YY	-0.1% MM, 2.5% YY
	RPIX – Ex Mortgages, Aug	0.4% MM, 2.4% YY	-0.1% MM, 2.6% YY
09:30	UK: Producer Input Prices, Aug	-0.4% MM, -6.8% YY	-1.6% MM, -7.3% YY
09:30	UK: Producer Output Prices, Aug	0.0% MM, -0.2% YY	-0.1% MM, -0.1% YY
	Output Prices Ex Tax, Aug	0.0% MM, 0.1% YY	0.1% MM, 0.2% YY
	Excluding Food, Drink, Tobacco, Energy, Aug	0.0% MM, 0.9% YY	0.0% MM, 0.9% YY
10:00	Germany: ZEW Economic Expectations, Sep		
10:00	Euro Area: Labour Cost Index, 2Q		
10:00	Euro Area: Job Vacancies, 2Q		
Wednesday 17 September		**Forecast**	**Last**
07:00	EU-27: New Car Registrations, Aug		
07:30	Sweden: Riksbank Minutes		
09:00	Italy: Trade Balance, Jul-Aug		
09:30	UK: LFS Unemployment, 3-M Average, May-Jul	-122,000 QQ, 6.3% Rate	-132,000 QQ, 6.4% Rate
	LFS Unemployment, Single Month, Jul	6.0% Rate	6.4% Rate
	Claimant Count Unemployment, Aug	-30,000 MM, 2.9% Rate	-33,600 MM, 3.0% Rate
	Average Earnings Ex Bonus, May-Jul	0.9% YY	0.7% YY
09:30	UK: MPC Minutes of Sep 4 Meeting		
10:00	Euro Area: HICP, Aug Final		
10:00	Euro Area: Construction Output, Jul		
NA	Spain: Trade Balance, Jul		
19:00	US: FOMC Outcome		
Thursday 18 September		**Forecast**	**Last**
	Scotland: Referendum on Independence		
07:00	Switzerland: Trade Balance, Aug		
08:30	Switzerland: SNB Monetary Policy Assessment		
08:30	Sweden: GDP Details, 2Q Final		
08:30	Netherlands: Consumer Confidence, Sep		
08:30	Netherlands: Unemployment, Aug		
09:00	Norway: Norges Bank Monetary Policy Outcome		
09:30	UK: Retail Sales Volumes, Aug	1.0% MM, 4.7% YY	0.1% MM, 2.6% YY
10:00	Italy: Current Account, Jul		
10:00	Greece: Unemployment Rate, 2Q		
11:00	UK: CBI Industrial Trends Survey – Output Expectations, Sep	+30%	+31%
	CBI Order Books, Sep	+10%	+11%
	CBI Selling Prices, Sep	-1%	-1%
Friday 19 September		**Forecast**	**Last**
07:00	Germany: Producer Prices, Aug		
07:45	France: Wages, 2QF		
08:30	Netherlands: Consumer Spending, Jul		
09:00	Euro Area: Balance of Payments, Jul		
14:00	Belgium: Consumer Confidence, Sep		
During the Weekend		**Forecast**	**Last**
	G20: Meeting of Finance Ministers and Central Bankers, Cairns, Australia		

Source: Citi Research

Figure 14. Recent Research

Euro Area - Sovereign Debt Update		
ECB Acts to Firmly Anchor Inflation Expectations	European Economics Team	Sep 5, 2014
ECB to Move Closer Towards QE	European Economics Team	Sep 4, 2014
ECB's Liikanen: No Limits to Non-Conventional Tools	European Economics Team	Sep 3, 2014
Draghi and Hollande Agree on Economic Risks	European Economics Team	Sep 2, 2014
Merkel Calls Draghi after his Comments on Fiscal Policy	European Economics Team	Sep 1, 2014
Euro Area		
Euro Area - ECB Cuts Rates and Announces Asset Purchase Programme	Guillaume Menuet	Sep 4, 2014
Euro Area - Euro Area: What Are The Prospects For Fiscal Easing?	Ebrahim Rahbari	Sep 3, 2014
Euro Area - Inflation Hit a New 5-Year Low	Giada Giani	Aug 29, 2014
Euro Area - ECB Preview: Will Draghi Highlight Downside Risks to Inflation?	Guillaume Menuet	Aug 28, 2014
Euro Area - ECB Draghi Notes Fall in Inflation Expectations	Guillaume Menuet	Aug 26, 2014
Global Economic Forecasts – August 2014	Michael Saunders	Aug 26, 2014
Euro Area - PMIs Suggest Very Little Room for Economic Rebound in H2 14	Giada Giani	Aug 21, 2014
Euro Area - SPF Survey: Downward Drift In 2014-15 Inflation Expectations	Guillaume Menuet	Aug 14, 2014
Euro Area: NFC Net Borrowing Falling More Slowly	Antonio Montilla	Aug 12, 2014
European Economic Indicators – Week Ahead	Michael Saunders	Aug 8, 2014
Euro Area - ECB – Happy To Wait And See, For Now	Giada Giani	Aug 7, 2014
Italy - Why is the Economy Underperforming so Badly?	Giada Giani	Aug 6, 2014
Europe: Monthly Inflation Profiles for Selected Countries	Ann O'Kelly	Jul 31, 2014
European Economic Forecast Highlights, July 2014	Ann O'Kelly	Jul 31, 2014
Spain: Economic Recovery Strengthens in Q2	Antonio Montilla	Jul 31, 2014
Euro Area: Lending Survey Records Improving Credit Demand	Ebrahim Rahbari	Jul 31, 2014
Euro Area: Periphery-Core Rebalancing Continues in July	Ebrahim Rahbari	Jul 30, 2014
New 2015 ECB Calendar: Governing Council Meetings	Guillaume Menuet	Jul 18, 2014
Euro Economics Weekly		
Is the Period of German Outperformance Over?	Ebrahim Rahbari	Aug 29, 2014
ECB QE: Why, When and How?	Guillaume Menuet	Aug 22, 2014
What's Behind the Periphery Growth Outperformance?	Giada Giani	Aug 15, 2014
How Might Russia Developments Affect The Eurozone Economy?	Ebrahim Rahbari	Aug 1, 2014
France: More Reforms to Jump Start Confidence?	Guillaume Menuet	Jul 25, 2014
Public Debt Sustainability: Has It Really Been Restored?	Giada Giani	Jul 18, 2014
Why Banking Union Matters: Then and Now	Ebrahim Rahbari	Jul 11, 2014
Is The Euro Area Recovery at Risk of Faltering?	Guillaume Menuet	Jul 4, 2014
Weak Pay Trends Imply Further Inflation Undershoot	Giada Giani	Jun 27, 2014
A Great Rotation towards Eurozone Portfolio Assets?	Ebrahim Rahbari	Jun 20, 2014
Labour Market Slack	Giada Giani	Jun 13, 2014
ECB TLTRO: Ambitious But Probably Not Enough, QE Lies Ahead	Guillaume Menuet	Jun 6, 2014
Negative Deposit Rate: Limiting Risks, Limited Upside	Ebrahim Rahbari	May 30, 2014
Soft Growth, Low HICP And Weak SPF Point To ECB Cut In June	Guillaume Menuet	May 23, 2014
Long Live (s) The Rise of the Current Account Surplus	Ebrahim Rahbari	May 16, 2014
Chief Economist Publications		
Global Economic Outlook and Strategy — August 2014	Willem Buiter	Aug 20, 2014
Scandi and Swiss		
Scandi Economics Update	Tina Mortensen	Sep 5, 2014
Sweden - Unanimous Riksbank on Hold in September;	Tina Mortensen	Sep 4, 2014
Denmark - Back to Negative Interest Rates	Tina Mortensen	Sep 4, 2014
Switzerland - More Hints of Economic Slowdown	Michael Saunders	Sep 2, 2014
UK		
UK - REC Survey Suggests Labour Market Remains Buoyant	Michael Saunders	Sep 5, 2014
UK - Services PMI and GDP Revisions	Michael Saunders	Sep 3, 2014
UK - YouGov Poll Shows Rising Support for Independence	Michael Saunders	Sep 3, 2014
UK - YouGov Report Slight Rise in Inflation Expectation	Michael Saunders	Sep 2, 2014
UK Economics Weekly		
Rewriting the Economy's Past and Present	Michael Saunders	Aug 29, 2014
Scottish Independence Referendum: Less Than A Month To Go	Michael Saunders	Aug 22, 2014
Change in Rate View	Michael Saunders	Aug 15, 2014
IR to Signal Shift in the MPC's Outlook	Michael Saunders	Aug 8, 2014

Source: Citi Research

Appendix A-1

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