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Global

Global Economic Outlook and Strategy

Global Economic Outlook and Strategy – January 2015

- We have already made some fairly extensive revisions to our economic forecasts since our end-2014 growth outlook, and make more revisions in this publication. The overall effect is to cut 0.1 percentage point off our 2015 global growth forecast, and we now expect global growth (at current exchange rates) of 3.0% this year and 3.4% in 2016, after 2.7% growth in 2014. This reflects the recent major upward revision to our 2015 US growth forecast (to 3.6% from 3.0%) and modest upgrades to forecasts for the euro area and Japan, driven by the real income boost from lower oil prices plus support from loose (and in some cases loosening) monetary policies. Against that, we make downward revisions to growth prospects in Switzerland (after the recent CHF surge) and a relatively large downgrade to our overall EM growth forecast, driven in particular by major commodity producers.

- With very low inflation (or even negative inflation) and some slack remaining, we expect that advanced economy monetary policy will continue to loosen overall. It is virtually certain that the ECB will launch QE, most likely on 22 January. We expect an initial program of around €600bn focused on government bonds, to be completed over two years, with limited direct mutualisation of any losses. We regard such a program as far from optimal: our preference would be for a bigger program, over a shorter period, with full mutualisation of any losses agreed at the outset. But a limited program may well be needed to get wide support. Such a program may well achieve the ECB's balance sheet aims but, even with further euro weakness, we doubt it will be enough to break the economy out of "low-flation". Hence, ECB QE probably will be scaled up further over time. We also expect the BoJ to expand QE further around midyear. Other smaller European countries are likely to test the limits of the sub-zero bound on policy rates: with Sweden likely to cut rates below zero while Switzerland cuts further below zero. We still pencil in the first Fed hike for late-2015, but are postponing our forecast for the first BoE hike to early 2016. Even beyond that, UK and US tightening is likely to be fairly gradual.

- Political risk remains a recurring theme, with the upcoming Greek election (25 January) and the UK election (7 May) notable landmarks.

Figure 1. Currency and Interest Rate Forecasts, as of 21 January 2015

	Current	1Q 15F	2Q 15F	3Q 15F	4Q 15F	1Q 16F	2Q 16F
United States: Federal Funds	0.25	0.25	0.25	0.25	0.50	0.50	0.75
10-Yr. Treasuries (Period Ave.)	1.81	1.95	2.20	2.35	2.55	2.65	2.65
Euro Area: US$/€	1.15	1.14	1.12	1.10	1.08	1.05	1.02
Euro Repo Rate	0.05	0.05	0.05	0.05	0.05	0.05	0.05
10-Yr. Bunds (Period Ave.)	0.47	0.55	0.55	0.65	0.65	0.75	0.75
Japan: ¥/US$	117	118	124	129	132	134	136
Call Money	0.10	0.10	0.10	0.10	0.10	0.10	0.10
10-Yr. JGB (Period Ave.)	0.24	0.25	0.35	0.40	0.45	0.50	0.50

F: Forecast. Note: All forecasts are for end of period, unless specified. Source: Citi Research

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

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Figure 2. Forecast Highlights and Changes

Global	We are trimming 0.1 percentage point off our 2015 global growth forecast, with a sharp downgrade to EM growth (especially commodity producers) outweighing upgrades to AE growth including the US, Japan and Euro Area.
United States	We recently raised our GDP growth forecast to 3.6% for 2015 because of the temporary, but possibly prolonged boost from the continued decline in the price of oil. With headline inflation approaching zero in mid-2015 and core inflation remaining below 2%, changes in the monetary policy stance will depend largely on the Fed's projections for the duration of the robust growth ahead. In any event, the path toward interest rate normalization will be gradual.
Euro Area	We look for real GDP growth to accelerate from 1.3% in 2015 to a six-year high of 1.9% in 2016. The much lower oil price together with EUR/USD falling towards parity around mid-2016 will support faster economic activity. With the likely imminent announcement of an ECB sovereign bond QE program, we expect financing conditions to loosen further. We believe that the limited and transitory inflation rebound will lead to further iterations of QE around mid-16.
China	We forecast the official reported GDP data will show growth at 6.9% this year, but underlying growth could improve amid the oil dividend. The lower oil price will likely take roughly 2 quarters to benefit the economy and may boost GDP growth by 0.4-0.9ppt this year. Policy rate/RRR cuts are possible before the Chinese New Year (Feb 19). We expect the RMB will weaken against the US dollar but strengthen in REER terms, and the government will aim to turn reforms into growth momentum.
Japan	We expect the economy will grow at a solid pace in coming quarters — mostly thanks to lower oil prices. However, if as we anticipate, core inflation approaches 0%, driven by falling oil prices, the BoJ will likely implement additional easing measures in the form of increased purchases of JGBs and ETFs in this summer.
United Kingdom	The UK economy is set for fairly strong economic growth with ultra-low inflation as the collapse in oil prices feeds through. Indeed, with cuts in household gas prices, YoY CPI inflation may well turn slightly negative in H1-2015, and is likely to stay below 1% YoY until yearend. As a result, we are postponing our forecast for the first hike from Q4-15 to Q1-16.
Canada	Tumbling crude oil prices threaten to derail the Canadian expansion. The BoC in a surprise move cut rates at its January meeting in response. Hence, we further delay our call for the next BoC interest rate hike from 1Q 2016 to 3Q 2016.
Australia	We continue to forecast 2.9% growth for the Australian economy in 2015. Risks come from the pace of rebalancing between mining and non-mining activity. But early signs suggest that the RBA can continue emphasise policy stability over the need to cut rates further. We retain our view from last year that the cash rate target will remain at 2.50% for all of 2015 before a hike in Q1 2016.
Emerging Asia (ex-China)	Growth momentum remains subdued and inflation benign, prompting India to deliver an earlier-than-expected cut and the RBI will likely do more, while Korea is proving more resistant as it accepts lower potential growth. Malaysian assets have underperformed on the back of oil/fiscal worries, but the economy is buffered by a competitive manufacturing sector and strong balance sheet. The positive lift from the oil price decline from this net importing region remains elusive so far.
CEEMEA	CEEMEA is caught between the strongly disinflationary pressures produced by falling oil prices, and the continuing appreciation of the US dollar. Where monetary policy is concerned, it is likely that interest rate risks are tilted to the downside - but not for commodity exporters.
Lat Am	President Rousseff has decided to tackle the deterioration in Brazil's fiscal accounts by appointing an austere MoF. Growth is expected to remain disappointing as a result of a tighter fiscal and monetary policy mix. In Mexico, we expect real GDP growth to accelerate to 3.4% in 2015 and expect some monetary tightening later in the year. Lastly, conditions remain fragile in Argentina and Venezuela, with the latter being severely negatively affected by the drop in oil prices.

Source: Citi Research

Figure 3. Selected Countries — Industrial Production Forecasts (Pct.), 2014-2016F

	2014F	2015F	2016F
World	3.4	3.6	4.1
United States	4.3	4.4	4.0
Japan	2.1	3.3	3.4
Euro Area	0.6	1.2	3.4
United Kingdom	1.7	1.8	2.0
Canada	3.0	-0.3	-0.6
China	8.3	7.4	7.1
India	3.9	5.9	7.0
Korea	-0.3	2.7	3.8
Brazil	-2.8	-0.2	1.8

Source: Citi Research

Overview — Oil, QE and Political Risks

Michael Saunders

We have already made some fairly extensive revisions to our economic forecasts since our end-2014 growth outlook, and make more revisions in this publication. The overall effect is that we are cutting 0.1 percentage point off our 2015 global growth forecast, and now expect global growth (at current exchange rates) of 3.0% this year and 3.4% in 2016, after 2.7% growth in 2014. This compares to our previous forecasts of 3.1% and 3.4% for 2015 and 2016, respectively.

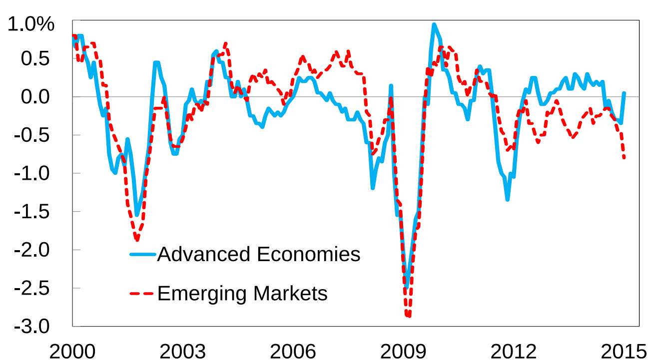
Within that, we are lifting our 2015 advanced economy (AE) growth forecast to 2.4% from 2.1%. This reflects the recent major upward revision to our 2015 US growth forecast (to 3.6% from 3.0%) and modest upgrades to forecasts for the euro area and Japan. In this report we also sharply cut our 2015 Swiss growth forecast in response to the recent CHF surge, and now expect a severe recession and deflation this year. We also are sharply cutting our EM growth forecasts, and now expect growth of 3.9% this year and 4.7% in 2016, versus prior forecasts of 4.4% and 4.9% respectively, with notably large cuts to forecasts in Russia, Brazil and Mexico. Our EM growth forecasts have been trending down since mid-2011, but this month's downgrade is the equal seventh-biggest monthly downgrade of the last 15 years: all the larger downgrades came in the global downturns of 2001 and 2008.

We highlight three main themes: the causes and effects of lower oil prices; prospects for QE (and options beyond QE) by the ECB, BoJ and other central banks aiming for stimulus with policy rates at zero; and political risks.

Implications of Lower Oil Prices

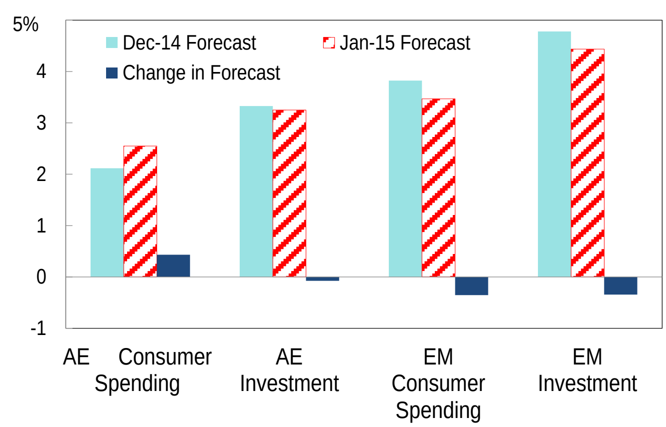
We regard the sharp drop in global oil prices, with Brent down from an average of $110/barrel in Q2-2014 to just below $50 now, as a mix of a positive supply shock from the expansion of shale and collapse of OPEC discipline, and the reflection of a negative demand shock from sluggish global growth and disappointing EM growth over the last couple of years[1]. This oil price decline, if sustained, is likely to have three major effects: (1) a sharp drop in global inflation in the next year or two; (2) a major redistribution of income from oil-producing countries and companies (and governments of oil-producing countries) to oil consumers; (3) greater likelihood of further stimulus or a low for longer approach among AE central banks.

Figure 4. Global – Six-Month Sum of Revisions to Citi GDP Growth Forecasts for Current Year and Next Year, 2000-15



Source: Citi Research

Figure 5. Global – Citi Forecasts for 2015 YoY Growth in Real Consumer Spending and Investment Spending in AEs and EMs

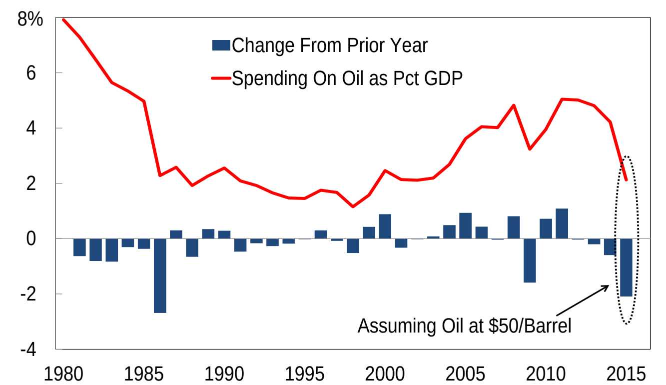


Source: Citi Research

[1] See also "*Understanding the Plunge in Oil Prices: Sources and Implications*", World Bank, January 2015.

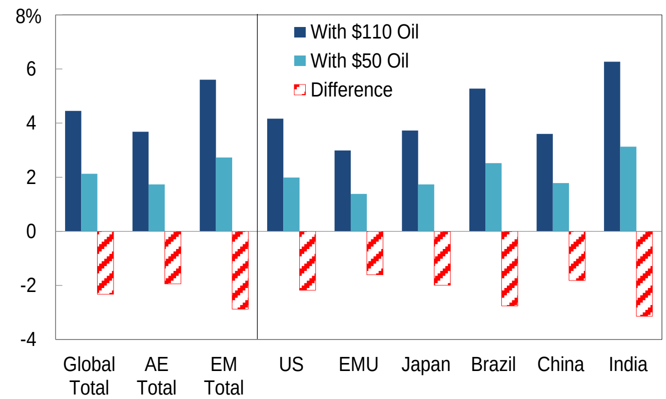
The redistribution of incomes from oil producers to oil consumers generated by the drop in global oil prices now equals roughly USD2tn, 2.3% of global GDP. This estimate is based on global oil consumption at 90 million barrels per day, the 2013 level, and comparing an oil price of $50/barrel (close to current levels) with $110/barrel (the average level of Brent in 2012-13, and also in Q2-2014). In effect, this reverses the rise in the global oil bill of the last decade. Taking aggregate global oil consumption and using Brent as a benchmark for global oil prices, we estimate that aggregate global spending on oil (ex taxes) by households, businesses and government rose from an average of 2.0% of global GDP in 1986-2004 to a peak of roughly 5% of global GDP in 2011-12, and 4-5% of global GDP in 2013-14. If oil prices stay around $50, the aggregate global oil bill (ex tax) will be around 2.1% of global GDP in 2015, similar to the 1986-2004 average and well below recent years.

Figure 6. Global – Spending On Oil Consumption as Pct Global GDP, 1980-2015



Note: 2015 figure is based on $50 oil, IMF nominal GDP forecast and 2013 levels of oil consumption. Source: Citi Research

Figure 7. Global – Aggregate Spending on Oil (Ex tax) At Oil Prices (Brent) of $110/Barrel and $50/Barrel, as Pct 2015 Nominal GDP



Note: Figures are based on $50 oil, IMF nominal GDP forecast and 2013 levels of oil consumption. Sources: IMF, EIA and Citi Research

As a whole, spending on oil is a slightly bigger share of GDP in EMs than in AEs, and hence the aggregate saving in the oil bill with oil at $50 rather than $110 is greater for EMs as a whole (2.9% of GDP) than for AEs (1.9% of GDP). But there is considerable cross-country variation, reflecting differences in energy intensity and in oil's role among energy sources. For example, both the US and Japanese economies are more oil-intensive than Europe, while India's economy is much more oil-intensive than China. However, while some oil-importing EM countries will be major beneficiaries of low oil prices, overall EM growth will be hit by probable severe economic weakness in some major oil producers (eg Russia, Venezuela), as well as side effects of more widespread weakness in commodity prices (eg Brazil).

As well as redistributing incomes, the oil price decline cuts CPI inflation directly, and we have cut our 2015 AE inflation forecast by 1.0 percentage point (from 1.3% YoY to 0.3%) since the end-2014 outlook. This is the second biggest one-month change to our AE inflation forecast for the current and next year of the last 15 years, exceeded only by that of Nov-08. In theory, one might expect AE central banks would look through the direct disinflationary effects of lower oil prices, because these effects will fade at the monetary-policy relevant horizon of 1½-3 years ahead. However, in practice, we expect that AE central banks will not take this approach, but instead will regard the drop in oil prices as justifying extra stimulus or a low for longer stance.

There is widespread anxiety over global growth prospects, of which lower oil prices is a symptom. And, in countries which already faced inflation close to (or below) zero (eg euro area, Japan, Sweden, Switzerland), the oil price plunge is likely to

cause a run of negative YoY inflation figures in coming quarters. This could raise risks that inflation expectations get destabilised to the downside, hence expanding the adverse effects of "lowflation" or deflation (eg inability to get perceived ex ante real rates low enough, worries over future debt burdens). As a result, we expect the ECB will start QE very soon, with the BoJ likely to expand its QE program in the next quarter or two. Moreover, ECB and BoJ QE may well produce disinflationary spillovers for other AEs via FX appreciation versus the yen and euro. Finally, even for AEs that are growing quite strongly (eg US, UK), the oil price plunge offers policymakers the chance to ensure that output gaps close with little risk that inflation expectations surge higher, and to probe whether — amidst modest pay growth — labour market slack is higher than implied by a comparison of the jobless rate with estimates of equilibrium. We pencil in the first Fed hike for late-2015, and are postponing our forecast for the first BoE hike to early 2016. With monetary accommodation reinforcing the boost to real incomes from lower oil prices, we are lifting our forecast for 2015 AE consumer spending growth to 2.5% from 2.1% previously, with especially strong growth likely in the US and UK.

ECB QE and Beyond

In our view, it is a virtual certainty that the ECB will launch QE soon, most likely at the Jan 22 meeting, in response to sluggish economic growth, weakness in inflation, and falling inflation expectations. We expect an initial program of around €600bn focused on government bonds, to run over two years, with limited direct mutualisation of any losses. Our preference would be for a bigger program, over a shorter period, with full and explicit mutualisation of any losses agreed at the outset. In particular, if QE initially comes with limited mutualisation, its effectiveness in achieving spread compression may be somewhat diluted by worries over the interplay between the creditworthiness of sovereigns and central banks. But a more limited program may well be needed to get wide support.

A QE program along these lines, plus the TLTRO program and ABS/covered bond purchases, may well achieve the ECB's stated aim of re-expanding the Eurosystem's balance sheet to roughly €3tn, the early-2012 level. And, provided the euro falls significantly (our base is that it will fall below parity against the USD over the next year or two), gains in import prices may well lift CPI inflation to about 1½% YoY in 2016-17. However, we doubt that this scenario would be enough to achieve broader aims of closing the output gap and preventing a further period of relatively low inflation (albeit probably not deflation) in coming years. As a result, we suspect that QE will be expanded over time, perhaps with several iterations (QE2, QE3 etc).

We do not expect that limited mutualisation (if this is what occurs) will prevent the ECB from expanding QE further. To be sure, with limited mutualisation, individual central banks could face losses on their QE holdings. These might come through a mix of: (1) negative carry if the ECB hikes rates above current bond yields; (2) capital losses if bonds are sold at lower prices than at purchase; (3) writedowns in the event of a sovereign debt default or restructuring.

Most likely, individual governments would feel the need to cover any losses by their central bank (although in theory a central bank can operate with negative capital or cover any losses from future seignorage revenues). In this case, it is useful to consider the consolidated balance sheet of the government and central bank.

Barring sovereign restructuring, QE is only likely to cause significant fiscal losses for the central banks concerned if nominal GDP growth picks up sharply, and in that case the fiscal gains from higher nominal GDP growth for the consolidated public

sector would most likely dwarf any QE losses[2]. For example, consider the case of an EA central bank that buys sovereign debt equal to 25% of its own GDP at a yield of 1.5% financed by reserves (initially yielding roughly zero). Initially, it makes a carry gain of roughly 150bp, equal to 0.3-0.4% of nominal GDP per year (potentially cutting the fiscal deficit by that amount). If the ECB hikes rates to, say, 2.5%, the central bank would make a carry loss of 100bp (equal to 0.25% of nominal GDP per year), potentially lifting the fiscal deficit by that amount. But, it is surely unlikely that the ECB would hike so much unless euro area nominal GDP growth rises markedly. If that country's nominal GDP growth rises by 2 percentage points, then with a tax/GDP ratio of 46.5% (the EA average), revenues would rise by 0.9% of GDP in the first year, 1.8% of GDP in the second year and so forth. The fiscal gains from higher tax revenues would far outweigh possible carry losses on the QE bonds, even if that country's nominal growth picks up somewhat less than the EA average. The same point holds in net present value terms (ie gauging capital losses on sovereign bonds against the net present value of future tax revenues generated by higher nominal GDP growth). Hence, we expect that national governments will be willing to guarantee to backstop their individual central banks to a level that allows a large QE program.

To be sure, the picture would be messier in the event of sovereign debt restructuring, with a government then potentially needing to restructure outstanding debt heavily and then take on extra debt to cover its central bank losses. This would not be a major issue if QE never exceeds its likely initial program size of, say, €600bn with a non-mutualised amount of, say, €300bn. But, in a worst-case scenario, if the eventual scale of the non-mutualised asset purchases under several QE programs were to be significantly larger, an NCB that had to purchase just the debt of its high-credit risk sovereign could become insolvent, if its sovereign defaulted on its debt and prospects for recapitalisation by that same sovereign would be poor. It may not be possible for an insolvent NCB to remain a viable member of the Eurosystem, because it would cease to be an acceptable counterparty for commercial banks and for the rest of the Eurosystem, through Target2. Without ex-post mutualisation by the rest of the Eurosystem, the other euro area governments or international institutions with deep pockets, the insolvent NCB could no longer participate in the operations of the euro system and its government would effectively be forced to exit the euro area.

So the combination of each NCB purchasing only its own sovereign debt and no mutualisation could, if QE becomes very large and persistent, pose an existential threat to the euro area. A possible safeguard is to limit the purchases of the NCBs (and their collateralised lending and repo operations), to good quality assets only (say, nothing less than investment grade, unless the sovereign issuing the sub-investment grade debt is fully compliant with a Troika- or European Commission-approved adjustment programme). This would permit large-scale QE, even if there were no mutualisation of losses, while limiting risks of insolvency for NCBs from nations with sovereigns that are at material risk of insolvency. Something on these lines is likely. But, we suspect that if the fiscal and financing position of individual governments worsens so much as to make major sovereign restructuring likely, the euro area would of necessity adopt a framework of greater fiscal mutualisation anyway.

As government bond yields for Japan, the euro area and several smaller European countries approach zero along the whole yield curve, the wider question of policy options for extra stimulus in addition to QE may become relevant. Broadly, we see five major options if the sovereign yield curve is at (or below) zero across all

[2] See speech by BoE then-Deputy Governor Charlie Bean on this issue, October 2009.

maturities: (1) the central bank can keep buying bonds, perhaps pushing yields below zero; (2) the central bank buys other domestic assets with a non-zero yield (eg credit, equities); (3) the central bank buys foreign assets to depreciate the currency; (4) the central bank cuts its relevant policy rate below zero; (5) the government loosens fiscal policy which, if done in conjunction with QE, approaches “helicopter money”. Some, or all of these may come into play for the ECB, BoJ and perhaps some others if growth and inflation stay weak. For example, the SNB has already cut its policy rate to minus 75bp and, with severe deflation likely, may well cut even further[3]. The key point is that, just as the zero bound on policy rates did not exhaust options for monetary stimulus, central banks continue to have options even at the zero bound across sovereign yields. The effectiveness of these options is uncertain, and all may have some adverse side-effects. But options do exist.

Political Risks

The Greek election is the most immediate of a series of political risks (including the May 7 UK election) that are likely through this year. Opinion polls suggest that Syriza will win the Greek election (25 January) – but not by enough to form a majority without coalition partners. We consider Grexit risks to be low, because the incentives for both creditor countries and the new Greek government to keep Greece inside the Eurozone seem very strong. However, Syriza’s demands — a face value haircut to the officially-held Greek government debt, exit from the bailout program and end to austerity — appear incompatible with the views of the creditors. As a result, Greece is likely headed for a long period of politically-induced uncertainty even after the elections, and Grexit cannot be ruled out.

[3] See “Did the SNB score an own goal? Francly, yes”, Willem Buiter, 16 January 2015, Citi for a discussion of options to make it easier for central banks to set a highly negative interest rate.

Figure 8. Citi Global Economics Team *(For Informational Purposes Only)*

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Source: Citi Research

Figure 9. Selected Countries — Economic Forecast Overview (Percent), 2014-2019F

	GDP Growth						CPI Inflation						Central Bank Policy Rates					
	2014F	2015F	2016F	2017F	2018F	2019F	2014F	2015F	2016F	2017F	2018F	2019F	2014F	2015F	2016F	2017F	2018F	2019F
Global	2.7	3.0	3.4	3.4	3.4	3.3	2.6	1.9	2.7	2.9	3.0	3.0	2.40	2.43	2.49	2.77	3.10	3.41
Based on PPP weights	*3.2*	*3.4*	*3.9*	*4.0*	*4.0*	*4.0*	*3.4*	*2.9*	*3.4*	*3.6*	*3.7*	*3.7*	*3.38*	*3.51*	*3.47*	*3.65*	*3.85*	*4.03*
Industrial Countries	1.7	2.4	2.4	2.1	2.1	2.1	1.4	0.3	1.7	1.8	1.8	1.8	0.36	0.30	0.57	1.07	1.65	2.30
United States	2.4	3.6	3.0	2.5	2.5	2.5	1.3	0.3	1.8	1.9	2.2	2.2	0.25	0.29	0.75	1.63	2.38	3.02
Japan	0.2	1.1	1.9	0.5	1.0	1.0	2.8	1.0	1.0	2.1	1.2	1.3	0.13	0.10	0.10	0.10	0.30	0.50
Euro Area	0.8	1.3	1.9	1.9	1.8	1.8	0.4	-0.1	1.6	1.5	1.4	1.5	0.16	0.05	0.05	0.07	0.50	1.46
Canada	2.4	2.0	1.8	2.1	2.0	1.9	1.9	0.4	2.1	1.9	2.0	2.0	1.00	0.75	0.94	1.88	2.44	2.75
Australia	2.8	2.9	3.2	3.4	3.3	2.8	2.5	2.1	3.0	2.2	2.4	2.4	2.50	2.50	3.13	3.75	4.19	4.75
New Zealand	3.2	2.8	2.5	1.9	3.2	2.3	1.2	1.0	1.9	1.8	1.9	2.0	3.25	3.56	4.00	4.25	4.50	5.00
Germany	1.5	1.5	2.0	1.8	1.8	1.8	0.9	0.0	1.7	1.8	1.8	1.8						
France	0.3	0.9	1.8	1.9	2.0	2.1	0.6	0.1	1.7	1.5	1.5	1.5						
Italy	-0.4	0.4	1.1	1.1	0.9	0.9	0.2	-0.2	1.2	1.1	0.9	1.0						
Spain	1.4	2.2	2.2	2.1	1.8	1.8	-0.2	-1.0	1.2	0.8	0.7	0.8						
Greece	0.8	1.5	1.7	1.7	1.9	1.9	-1.4	-1.7	-0.3	-0.1	0.1	0.3						
Ireland	5.0	4.4	7.8	6.4	4.6	4.3	0.3	1.0	1.1	1.6	1.7	1.7						
Portugal	0.9	1.7	2.1	2.1	2.0	1.8	-0.2	-0.4	1.1	0.8	0.8	0.9						
Netherlands	0.7	1.4	1.9	2.0	2.0	2.0	0.3	0.0	1.7	1.6	1.5	1.7						
Belgium	1.0	1.2	1.8	1.9	2.2	2.1	0.5	-0.4	1.4	1.4	1.7	1.8						
Denmark	0.9	1.4	1.7	1.8	2.1	1.9	0.6	0.6	1.5	1.8	1.9	1.9	0.20	0.00	0.10	0.15	0.60	1.56
Norway	2.6	1.6	1.9	2.2	2.4	2.4	2.0	2.4	2.6	2.4	2.4	2.5	1.49	0.90	0.76	1.08	1.67	2.23
Sweden	1.9	2.3	2.6	2.6	2.4	2.3	-0.2	0.1	1.3	2.1	2.2	2.2	0.47	-0.22	-0.14	0.22	1.05	1.71
Switzerland	1.9	-0.9	-0.3	0.8	1.5	1.5	0.0	-2.5	-0.8	-0.9	-0.8	-0.2	-0.06	-1.50	-0.75	-0.25	0.00	0.00
United Kingdom	2.6	3.0	3.0	2.8	2.5	2.1	1.5	0.3	1.6	1.7	1.8	1.9	0.50	0.50	1.04	2.04	3.00	3.25
Emerging Markets	4.1	3.9	4.7	5.1	5.0	4.9	4.4	4.3	4.2	4.4	4.5	4.5	5.35	5.50	5.18	5.13	5.06	4.88
China	7.4	6.9	6.7	7.1	6.8	6.5	2.0	1.5	1.9	2.7	3.0	3.0	2.97	2.38	2.25	2.38	2.63	2.75
Taiwan	3.6	3.6	3.8	4.0	4.0	4.0	1.2	1.2	1.8	1.8	1.8	1.8	1.88	1.88	2.19	2.63	3.13	3.63
India	5.6	6.5	7.0	7.1	7.1	7.4	6.8	5.5	5.5	5.5	5.5	5.5	8.00	7.50	7.00	7.00	7.00	7.00
Indonesia	5.1	5.1	5.3	5.6	5.9	5.8	6.3	6.8	4.6	4.3	4.3	4.0	5.75	5.75	5.75	5.75	5.38	5.10
Korea	3.3	3.4	3.7	3.8	3.4	3.2	1.3	1.4	2.4	2.8	2.7	2.6	2.35	2.00	2.16	2.50	2.75	2.63
Czech	2.3	2.5	3.1	3.2	3.1	2.6	0.4	0.6	2.2	1.5	1.8	1.8	0.05	0.05	0.05	0.38	1.29	2.29
Hungary	3.4	2.5	1.5	1.9	2.5	2.0	-0.2	0.0	2.4	3.1	3.0	3.3	2.39	2.10	3.04	3.62	4.02	4.50
Poland	3.3	3.4	3.6	3.5	3.2	3.0	0.0	-0.2	2.4	2.5	2.5	2.5	2.39	1.58	1.90	3.25	3.50	3.50
Romania	2.8	3.0	3.0	3.0	3.0	3.0	1.1	1.5	2.6	2.5	2.5	2.5	3.19	2.25	3.06	4.19	4.50	4.50
Russia	0.6	-3.0	1.5	2.2	2.2	2.2	7.8	12.5	6.8	5.8	5.1	4.7	7.90	15.50	9.00	6.54	5.54	5.00
Turkey	2.9	3.3	3.4	3.5	3.6	3.5	8.9	5.5	7.0	6.2	6.0	5.7	9.08	7.63	8.81	9.00	9.00	8.50
Nigeria	6.2	4.5	6.2	6.5	6.7	6.0	8.1	11.0	8.8	9.9	9.2	8.7	13.00	13.50	12.00	9.00	9.00	9.00
South Africa	1.6	2.4	2.8	3.4	3.5	3.9	6.1	5.1	5.0	5.5	5.4	5.2	5.57	5.75	6.17	6.75	7.00	7.00
Argentina	0.0	-1.0	1.0	2.5	3.0	3.0	NA	18.3	32.9	32.5	24.0	12.0	22.87	23.51	37.80	38.00	29.00	17.00
Brazil	0.0	0.1	1.6	2.5	2.5	2.5	6.3	6.7	6.0	5.2	5.0	5.0	11.02	12.31	10.48	10.00	10.00	10.00
Mexico	2.2	3.4	4.4	4.5	4.6	5.0	4.0	3.6	3.6	3.6	3.6	3.6	3.21	3.08	3.94	5.00	5.75	6.25
Venezuela	-4.0	-4.4	1.9	1.9	1.8	1.6	61.3	70.3	80.0	85.0	90.0	95.0	14.50	14.50	18.00	18.00	18.00	18.00

Note: For inflation, we use the PCE deflator in the US, GDP deflator in Ireland. For Indonesia we refer to the FasBI rate to reflect actual money market rates
Source: Citi Research

Figure 10. Selected Countries — Economic Forecast Overview (Percent), 2014-2019F

	Current Balance (Pct of GDP)						Fiscal Balance (Pct of GDP)						Government Debt (Pct of GDP)					
	2014F	2015F	2016F	2017F	2018F	2019F	2014F	2015F	2016F	2017F	2018F	2019F	2014F	2015F	2016F	2017F	2018F	2019F
Global	0.6	0.6	0.4	0.4	0.3	0.2	-3.3	-3.4	-3.1	-2.8	-2.6	-2.5	86	86	85	85	84	83
Based on PPP weights	*0.7*	*0.7*	*0.5*	*0.3*	*0.2*	*0.1*	*-3.5*	*-3.7*	*-3.4*	*-3.1*	*-2.9*	*-2.8*	*76*	*76*	*76*	*76*	*75*	*74*
Industrial Countries	-0.2	0.1	-0.1	0.1	0.2	0.2	-3.7	-3.3	-3.1	-2.7	-2.5	-2.4	112	111	111	110	110	109
United States	-2.2	-1.4	-1.4	-0.8	-0.8	-0.7	-4.4	-4.1	-4.5	-4.3	-4.4	-4.6	106	106	106	106	106	106
Japan	0.6	2.7	2.4	2.0	2.0	2.0	-7.3	-6.6	-6.2	-5.4	-5.0	-4.6	244	247	249	252	255	256
Euro Area	2.5	2.7	2.4	2.2	2.0	1.9	-2.5	-2.2	-1.8	-1.4	-1.0	-0.7	95	95	94	93	92	90
Canada	-2.2	-3.5	-3.0	-2.4	-2.2	-2.2	-0.1	-0.1	0.0	0.1	0.1	0.3	88	87	86	84	83	83
Australia	-3.2	-4.2	-4.4	-3.8	-2.6	-3.6	-3.1	-2.5	-1.9	-1.2	-0.6	-0.2	32	34	33	33	34	35
New Zealand	-3.0	-4.5	-4.2	-4.7	-4.6	-5.5	-1.3	-0.2	0.1	1.1	2.3	1.5	35	34	33	34	31	31
Germany	7.3	7.6	6.7	6.5	6.0	5.9	0.3	0.2	0.1	0.1	0.1	0.1	75	73	71	69	67	65
France	-1.0	-0.4	0.1	-0.2	-0.4	-0.8	-4.3	-4.0	-3.5	-3.0	-2.5	-1.9	96	99	99	99	98	97
Italy	1.6	1.6	1.7	1.7	1.7	1.7	-3.0	-2.9	-2.1	-1.5	-0.8	-0.5	132	133	133	132	131	130
Spain	-0.2	0.5	0.5	0.7	1.0	1.1	-5.6	-4.5	-3.3	-2.4	-1.8	-1.2	97	100	100	100	99	98
Greece	1.4	1.1	1.1	1.0	1.2	1.4	-1.7	-1.7	-1.2	-1.1	-0.8	-1.1	178	179	176	173	170	166
Ireland	5.9	6.8	9.2	10.2	10.1	9.9	-3.8	-2.6	-0.6	1.3	2.8	3.9	110	108	99	91	82	74
Portugal	0.1	0.3	0.5	0.7	0.8	0.8	-4.2	-3.3	-2.5	-1.8	-1.2	-0.7	135	133	131	129	126	124
Netherlands	10.6	8.9	7.7	6.2	4.9	3.8	-1.9	-1.5	-1.3	-1.0	-0.8	-0.5	69	69	68	67	65	64
Belgium	0.1	-0.2	0.1	0.1	0.0	-0.1	-2.8	-2.7	-2.4	-1.9	-1.1	-0.5	106	108	107	105	102	99
Denmark	6.8	6.3	6.1	6.2	6.1	5.7	2.0	-2.5	-2.3	-1.5	-1.1	-0.9	42	44	45	45	44	44
Norway	9.3	9.8	10.1	10.3	10.2	10.1	9.7	9.0	9.3	9.2	9.0	9.0	NA	NA	NA	NA	NA	NA
Sweden	5.9	5.8	5.6	5.6	5.6	5.5	-2.3	-1.9	-1.0	-0.5	0.0	0.2	42	43	42	41	39	37
Switzerland	11.2	8.5	7.6	7.7	7.3	6.8	0.7	-0.1	-0.7	-1.2	-1.3	-1.4	47	47	46	46	46	48
United Kingdom	-5.4	-5.1	-5.3	-5.0	-4.6	-4.2	-5.4	-4.0	-1.9	-0.4	0.6	1.5	88	89	88	86	82	78
Emerging Markets	1.7	1.3	1.1	0.7	0.5	0.2	-2.8	-3.5	-3.1	-2.8	-2.7	-2.6	46	48	48	49	48	49
China	2.5	2.7	2.5	2.0	1.8	1.5	-2.1	-2.5	-2.5	-2.5	-2.5	-2.5	53	54	55	55	55	55
Taiwan	12.0	11.0	8.0	8.0	8.0	8.0	-1.4	-1.6	-1.3	-1.0	-1.0	-1.0	39	39	38	38	38	38
India	-1.2	-0.2	-0.8	-0.9	-0.9	-0.9	-6.7	-6.4	-6.1	-5.8	-5.5	-5.2	69	67	66	64	62	62
Indonesia	-3.1	-2.6	-2.5	-2.8	-2.6	-2.4	-2.4	-2.0	-1.8	-1.8	-1.7	-1.6	26	27	27	27	27	26
Korea	6.6	7.2	6.7	4.8	4.1	3.7	0.9	0.3	0.2	0.6	0.8	1.1	36	37	39	40	40	41
Czech	0.0	0.2	-0.8	-2.9	-1.6	-1.2	-1.9	-2.3	-2.0	-1.7	-1.4	-1.0	44	42	42	42	41	40
Hungary	4.2	4.7	4.0	3.3	3.2	3.4	-2.6	-2.4	-2.1	-2.2	-2.4	-2.1	78	77	76	75	74	73
Poland	-1.2	-1.6	-2.3	-2.6	-2.9	-3.5	-2.9	-2.3	-2.2	-2.2	-2.2	-2.2	47	47	47	47	46	46
Romania	-0.5	-1.8	-2.2	-2.5	-3.5	-3.5	-2.0	-1.9	-2.1	-2.3	-2.5	-2.5	42	42	43	43	43	43
Russia	3.2	3.2	2.3	1.4	0.4	-0.5	0.0	-2.6	-1.5	-1.0	-1.0	-1.0	12	13	14	14	14	15
Turkey	-5.6	-4.3	-4.8	-4.8	-4.7	-4.7	-1.3	-1.5	-2.9	-3.3	-3.3	-3.3	36	36	35	35	33	33
Nigeria	1.3	-2.5	-0.6	-0.2	0.1	0.8	-2.0	-2.7	-2.3	-2.1	-1.7	-1.5	NA	NA	NA	NA	NA	NA
South Africa	-5.3	-4.4	-4.1	-3.3	-2.8	-1.9	-4.1	-4.1	-3.5	-2.9	-1.9	-1.2	50	51	51	51	48	46
Argentina	-1.0	-1.4	-1.2	1.0	1.0	0.0	-3.7	-4.7	-3.7	-0.5	-1.0	-1.0	38	46	54	52	51	51
Brazil	-4.0	-3.8	-3.7	-3.6	-3.5	-3.4	-6.1	-5.3	-4.5	-3.9	-3.7	-3.6	63	67	67	67	66	65
Mexico	-2.2	-2.2	-2.6	-2.6	-2.5	-2.5	-3.6	-3.5	-3.5	-3.0	-2.5	-2.5	42	43	43	43	42	42
Venezuela	4.4	2.4	4.2	2.0	2.0	2.0	-12.3	-12.9	-12.7	-13.0	-12.6	-12.7	44	50	51	51	52	53

Note: Fiscal deficit and debt figures for all countries are general government debt and deficits. For Spain, fiscal deficits include the effect of financial support for banks. For Greece, we assume further reductions in the cost of official loans. Source: Citi Research

Figure 11. Selected Countries — Economic Forecast Overview (Percent), 2014-2016F

	Private Consumption Growth			Investment Growth			Export Growth			Import Growth		
	2014F	2015F	2016F	2014F	2015F	2016F	2014F	2015F	2016F	2014F	2015F	2016F
Global	2.2	2.8	3.0	3.9	3.8	4.9	3.4	3.4	4.5	2.7	3.5	4.4
Industrial Countries	1.6	2.5	2.4	3.6	3.3	4.1	3.0	3.3	3.6	2.9	3.4	3.6
United States	2.5	3.6	3.1	6.1	6.0	6.2	3.2	4.0	3.0	3.6	4.0	4.6
Japan	-1.1	0.6	1.5	4.2	3.1	4.0	8.0	5.1	3.6	6.7	2.4	2.5
Euro Area	0.9	1.6	1.6	2.0	1.8	3.1	3.3	3.2	3.9	3.4	3.8	3.3
Canada	2.7	2.8	2.0	0.5	-0.1	0.8	5.0	3.3	3.9	1.5	3.0	3.0
Australia	2.5	3.0	3.6	-5.5	-6.7	2.8	6.9	8.3	7.1	-0.5	2.9	4.6
New Zealand	3.3	2.6	2.5	4.0	2.8	1.5	1.8	1.0	3.4	7.7	4.8	3.4
Germany	1.2	2.1	1.9	2.9	1.1	3.2	3.8	2.8	2.8	3.6	4.2	3.5
France	0.6	1.2	1.5	-1.7	-0.6	2.3	2.1	3.1	4.1	3.5	2.9	2.3
Italy	0.3	0.7	0.8	-2.5	0.0	2.2	1.8	2.6	3.6	0.3	2.4	3.1
Spain	2.3	2.9	1.9	2.8	4.4	3.7	4.8	5.9	5.0	8.2	8.4	4.4
Greece	0.3	0.8	0.9	-4.3	3.5	5.4	10.2	5.6	4.4	7.4	2.9	3.1
Ireland	0.6	1.9	2.4	9.0	8.6	8.7	12.4	7.9	8.0	11.3	7.2	4.4
Portugal	2.1	2.3	1.6	2.3	2.8	2.1	2.7	5.4	6.1	6.0	5.0	4.2
Netherlands	-0.1	0.8	1.0	1.4	1.9	2.3	3.9	3.2	3.4	3.9	2.8	2.8
Belgium	0.9	1.0	1.3	3.9	3.1	2.7	3.4	4.3	4.1	2.8	4.7	3.9
Denmark	0.4	1.6	1.9	2.2	2.4	2.9	2.9	2.1	3.5	3.9	2.9	3.6
Norway	1.7	1.8	2.0	1.8	-0.5	0.4	2.6	3.5	4.1	1.7	1.6	1.9
Sweden	2.4	2.8	2.7	4.7	4.2	4.0	2.2	3.4	4.9	5.0	4.5	4.6
Switzerland	1.0	1.8	1.5	1.1	2.3	1.5	-9.5	-5.5	-2.2	-10.9	-4.0	0.5
United Kingdom	2.4	3.5	3.3	7.3	7.7	7.5	-0.8	3.3	4.8	0.7	3.8	5.3
Emerging Markets	3.6	3.5	4.2	4.2	4.4	5.8	3.9	3.5	5.7	2.3	3.7	5.4
China	7.6	7.1	7.1	7.5	6.0	6.3	6.1	6.7	5.2	0.6	4.0	4.0
Taiwan	2.6	3.2	3.4	2.2	1.8	3.2	4.7	5.2	5.1	4.4	3.5	3.8
India	5.5	7.0	7.0	2.5	6.5	8.5	11.0	9.3	9.3	9.5	9.0	9.3
Indonesia	5.3	4.1	4.4	4.9	6.1	6.3	-1.3	4.2	4.1	-4.0	2.5	2.6
Korea	1.9	2.6	3.0	3.8	3.9	5.5	3.3	4.7	7.0	2.6	4.2	7.8
Czech	1.6	2.3	2.5	3.3	4.9	7.6	7.5	5.6	8.6	8.4	5.9	10.1
Hungary	1.6	2.6	2.2	11.0	3.5	-1.0	6.6	6.0	6.2	7.5	6.4	6.0
Poland	3.0	3.0	3.2	9.0	6.1	6.0	4.3	4.0	6.0	6.8	4.8	7.0
Romania	5.0	3.5	3.5	-6.0	4.0	1.7	7.1	4.0	4.6	5.8	4.1	4.0
Russia	0.5	-4.0	1.0	-3.5	-5.6	2.5	0.0	-1.0	1.0	-3.0	-5.0	4.6
Turkey	1.3	3.2	3.5	0.9	1.9	2.4	6.2	4.4	4.5	-0.9	3.5	4.0
South Africa	1.0	1.4	2.2	-0.2	1.0	5.4	1.3	1.9	5.9	-1.5	-1.2	7.1
Argentina	-1.1	-0.7	1.4	-3.1	-5.7	-1.2	-5.7	-2.5	-0.2	-6.2	-3.4	-0.6
Brazil	0.8	0.5	1.7	-7.2	-1.2	3.9	2.7	1.8	1.5	-0.1	0.1	2.4
Mexico	2.0	3.5	4.3	2.4	6.0	7.7	6.4	6.8	9.9	4.7	7.3	8.9

Source: Citi Research

Figure 12. Selected Countries — Changes in Economic Forecasts (Percentage Points), 2014-2016F

	GDP Growth			CPI Inflation			Current Balance (Pct of GDP)			Fiscal Balance (Pct of GDP)		
	2014F	2015F	2016F	2014F	2015F	2016F	2014F	2015F	2016F	2014F	2015F	2016F
Global		-0.1		-0.1	-0.6	-0.1	-0.2	-0.2	-0.4	-0.1	-0.3	-0.1
Based on PPP weights		*-0.2*	*-0.1*	*-0.1*	*-0.5*	*-0.1*	*-0.2*	*-0.1*	*-0.3*	*-0.2*	*-0.3*	*-0.2*
Industrial Countries		0.3	0.1		-1.0		-0.1	-0.2	-0.4	0.1		0.1
United States	0.1	0.6	0.2	-0.1	-1.1			-0.2	-0.6			
Japan	-0.1	0.2	0.1	-0.1	-0.4	-0.1	0.5	2.0	2.0	0.7	-0.1	0.2
Euro Area		0.2	0.3	-0.1	-0.9	0.1	-0.2	-0.3	-0.4		0.1	0.1
Canada		-0.4	-0.5	-0.1	-1.4	0.1	-0.1	-1.5	-1.2		-0.2	-0.2
Australia	-0.5	-0.2			-0.5	0.7	0.1	0.1	0.2		-0.7	-0.9
New Zealand	-0.3	-0.1	0.1	-0.9	-1.2	0.3	1.2	0.9	0.8	0.3	0.2	-0.4
Germany		0.4	0.4		-1.1	-0.1	-0.1	-0.1				0.1
France		0.2	0.2		-0.8		-0.4	-0.4	-0.4		0.2	0.2
Italy		0.1	0.1		-0.7	0.1					0.1	0.1
Spain	0.1	0.2	0.1	-0.1	-1.2	0.5	-0.1				0.2	0.4
Greece				-0.1	-0.4	-0.4				0.2	0.4	0.6
Ireland	-0.5		2.6	-0.1			1.9	3.0	5.0	-0.2	-0.2	0.7
Portugal	0.1	0.2	0.1	-0.1	-0.6	0.4	-0.4	-0.4	-0.4	0.1	0.1	0.2
Netherlands		0.1	0.2	-0.1	-0.9	0.2	-0.2	-0.7	-1.4	0.1	0.3	0.4
Belgium	0.1	0.2	0.2	-0.1	-1.5	-0.3	0.7	-0.1	-0.2	0.2	0.1	0.3
Denmark	0.2	0.3			-0.5		0.7	0.7	0.7	2.8		
Norway		-0.3	-0.3		0.3	0.5	-1.5	-1.7	-1.9	-0.4	-0.7	-0.2
Sweden	-0.1	0.1	0.1		-0.4	-0.4			0.2	-0.2	-0.7	-0.7
Switzerland	0.6	-2.9	-2.7		-2.1	-0.9	-2.0	-4.0	-4.8	0.2	-1.0	-2.0
United Kingdom	-0.4				-1.0	-0.4	-0.7	-0.9	-1.0	0.2	0.8	1.3
Emerging Markets	-0.1	-0.5	-0.2			-0.1	-0.3	-0.2	-0.3	-0.4	-0.6	-0.4
China	0.1				-0.4	-0.3						
Taiwan				-0.2	-0.5	-0.2						
India				-0.4	-0.7	-0.5	0.4	1.1	0.5			
Indonesia					-0.4			0.1	0.2			
Korea	-0.1	-0.1			-0.2	-0.2	0.4	1.3	1.4			-0.1
Czech		0.2	0.1		-0.6	0.1	-0.2	0.8	0.3			
Hungary	0.1		-0.3	-0.2	-1.7	-0.4		0.9	0.7	0.2		
Poland					-1.0		0.6	1.6	1.6		0.1	
Romania				-0.1	-0.7		0.7	0.2		-0.3	0.1	0.4
Russia	0.1	-2.0	-0.2	0.3	4.9	1.0	-0.1	-0.3	-0.4		-1.6	-0.9
Turkey	-0.2				-1.2		-0.1	0.8	0.7	0.7	1.4	0.1
Nigeria		-0.3	-0.1		1.1	-0.5	-1.1	-1.6	-1.2		-0.3	-0.3
South Africa	0.2	0.2			-0.5	-0.2		0.3				
Argentina					-4.3	-1.9						
Brazil	-0.1	-0.4	-0.2		0.2	-0.1		0.5	0.4	-0.6	-0.6	-0.1
Mexico	-0.2	-0.5						-0.2	-0.2			
Venezuela		-2.2							0.1		-0.3	

Note: For Ireland we use the GDP deflator rather than the CPI. Source: Citi Research

Figure 13. Selected Countries — Economic Forecast Overview (Percent), 2014-2019F

	10-Year Yields						Exchange Rates Versus U.S Dollar						Exchange Rate Versus Euro					
	2014F	2015F	2016F	2017F	2018F	2019F	2014F	2015F	2016F	2017F	2018F	2019F	2014F	2015F	2016F	2017F	2018F	2019F
Industrial Countries																		
United States	2.55	2.30	2.65	2.70	2.70	2.70	NA	NA	NA	NA	NA	NA	1.33	1.11	1.00	1.00	1.08	1.16
Japan	0.55	0.36	0.55	0.65	1.25	1.50	108	126	137	137	132	127	141	140	137	137	143	148
Euro Area	1.23	0.60	0.88	0.95	1.04	1.30	1.33	1.11	1.00	1.00	1.08	1.16	NA	NA	NA	NA	NA	NA
Canada	2.23	1.63	2.11	2.50	2.45	2.35	1.10	1.23	1.28	1.27	1.22	1.17	1.47	1.37	1.28	1.27	1.32	1.36
Australia	3.79	3.59	4.39	5.25	5.75	6.25	0.90	0.75	0.71	0.72	0.75	0.79	1.47	1.48	1.42	1.39	1.44	1.48
New Zealand	4.46	4.38	5.35	5.73	6.00	6.50	0.83	0.70	0.66	0.65	0.65	0.65	1.60	1.58	1.52	1.54	1.66	1.79
Germany	1.23	0.60	0.88	0.95	1.04	1.30												
France	1.66	0.80	1.08	1.15	1.24	1.50												
Italy	2.87	1.70	1.98	1.95	1.94	2.10												
Spain	2.66	1.55	1.78	1.80	1.84	2.05												
Greece	6.63	6.48	4.88	4.70	4.29	4.05												
Ireland	2.28	1.10	1.38	1.45	1.54	1.80												
Portugal	3.68	2.35	2.63	2.45	2.29	2.30												
Netherlands	1.45	0.65	0.93	1.00	1.09	1.35												
Belgium	1.70	0.80	1.08	1.15	1.24	1.50												
Denmark	1.40	0.76	1.03	1.20	1.29	1.55	NA	NA	NA	NA	NA	NA	NA	NA	NA	NA	NA	NA
Norway	2.49	1.49	1.83	1.80	1.89	2.15	6.29	7.77	8.50	8.37	7.49	6.74	8.36	8.63	8.50	8.36	8.11	7.86
Sweden	1.73	0.98	1.48	1.45	1.54	1.80	6.87	8.40	9.25	9.17	8.31	7.57	9.12	9.33	9.25	9.15	8.99	8.82
Switzerland	0.70	0.08	0.18	0.25	0.35	0.45	0.92	0.92	1.08	1.11	1.04	0.98	1.22	1.02	1.08	1.11	1.13	1.14
United Kingdom	2.57	1.96	2.75	3.00	3.50	3.75	1.65	1.48	1.36	1.34	1.41	1.47	0.81	0.75	0.74	0.74	0.77	0.79
Emerging Markets																		
China	3.97	3.51	3.59	3.81	4.06	4.19	6.16	6.27	6.17	6.09	6.08	6.07	8.19	6.96	6.17	6.08	6.57	7.07
Taiwan	1.62	1.68	1.83	2.09	2.39	2.69	30.31	32.09	32.07	31.27	30.00	28.73	40.28	35.64	32.08	31.21	32.45	33.47
India	8.50	8.00	7.50	7.50	7.50	7.50	61.02	63.52	64.33	62.44	58.87	55.30	81.07	70.54	64.35	62.33	63.67	64.42
Indonesia	8.10	8.11	8.35	8.45	8.25	7.93	11866	13042	13067	12807	12474	12140	15765	14482	13072	12784	13491	14142
Korea	3.19	2.62	2.96	3.08	3.05	2.90	1053	1127	1140	1110	1058	1007	1399	1251	1140	1108	1145	1173
Czech	1.57	0.86	1.78	2.21	2.57	2.91	20.7	25.2	27.4	26.5	23.7	21.2	27.5	28.0	27.4	26.5	25.6	24.7
Hungary	4.81	3.73	4.38	4.65	5.15	5.30	232	290	320	322	301	282	309	322	320	322	325	329
Poland	NA	NA	NA	NA	NA	NA	3.15	3.82	4.13	4.07	3.69	3.37	4.19	4.25	4.13	4.06	3.99	3.93
Romania	NA	NA	NA	NA	NA	NA	3.34	3.89	3.99	3.76	3.49	3.26	4.44	4.31	3.99	3.75	3.77	3.79
Russia	NA	NA	NA	NA	NA	NA	38.6	63.7	66.1	62.3	53.2	44.2	51.3	70.7	66.1	62.2	57.6	51.5
Turkey	NA	NA	NA	NA	NA	NA	2.19	2.45	2.57	2.61	2.63	2.64	2.91	2.73	2.57	2.61	2.84	3.08
Nigeria	NA	NA	NA	NA	NA	NA	165	207	215	219	225	231	219	229	215	219	243	269
South Africa	8.06	8.04	8.14	8.38	8.77	9.00	10.85	11.94	12.23	11.95	11.35	10.75	14.41	13.26	12.24	11.93	12.28	12.53
Argentina	NA	NA	NA	NA	NA	NA	8.09	9.83	14.07	18.00	21.20	22.85	10.75	10.92	14.08	17.97	22.93	26.62
Brazil	12.00	12.25	12.75	11.88	10.75	10.75	2.35	2.85	2.97	3.00	3.00	3.00	3.13	3.17	2.97	2.99	3.24	3.49
Mexico	6.02	6.20	6.25	6.28	6.37	6.87	13.3	14.4	13.9	13.5	13.0	12.5	17.7	16.0	13.9	13.5	14.1	14.6
Venezuela	15.83	19.00	19.00	19.00	19.00	19.00	6.29	12.00	21.36	39.09	73.49	141.83	8.36	13.33	21.37	39.02	79.48	165.22

*Per USD except Euro Area, Australia, New Zealand, United Kingdom. For China we use 5Y bond yields. Source: Citi Research

Figure 14. Selected Emerging Market Countries — Economic Forecast Overview, 2014-2016F

	GDP Growth			CPI Inflation			Current Balance (% of GDP)			Fiscal Balance (% of GDP)		
	2014F	2015F	2016F	2014F	2015F	2016F	2014F	2015F	2016F	2014F	2015F	2016F
Asia	6.2	6.1	6.1	2.9	2.3	2.6	2.7	3.0	2.6	-2.5	-2.6	-2.5
China	7.4	6.9	6.7	2.0	1.5	1.9	2.5	2.7	2.5	-2.1	-2.5	-2.5
Hong Kong	2.3	2.6	3.0	4.4	4.4	3.9	0.6	2.9	2.4	1.3	0.7	1.0
India	5.6	6.5	7.0	6.8	5.5	5.5	-1.2	-0.2	-0.8	-6.7	-6.4	-6.1
Indonesia	5.1	5.1	5.3	6.3	6.8	4.6	-3.1	-2.6	-2.5	-2.4	-2.0	-1.8
Korea	3.3	3.4	3.7	1.3	1.4	2.4	6.6	7.2	6.7	0.9	0.3	0.2
Malaysia	5.7	5.0	5.1	3.2	2.6	3.0	5.3	4.0	5.0	-3.5	-3.2	-2.5
Mongolia	6.5	9.0	8.0	12.8	11.1	8.9	-7.8	0.0	-5.8	-8.1	-7.2	-6.5
Pakistan	5.4	4.5	4.3	8.6	7.0	7.5	-1.8	0.0	-1.3	-7.9	-8.2	-7.5
Philippines	6.3	6.5	7.3	4.2	2.6	3.1	4.0	5.9	5.7	-0.6	-1.4	-1.3
Singapore	2.8	3.0	3.0	1.0	0.1	1.4	18.0	18.0	17.0	-0.3	0.2	1.5
Sri Lanka	7.7	7.2	7.1	3.3	2.8	5.0	-3.0	-2.6	-2.1	-5.4	-5.2	-5.2
Taiwan	3.6	3.6	3.8	1.2	1.2	1.8	12.0	11.0	8.0	-1.4	-1.6	-1.3
Thailand	0.5	3.0	3.8	1.9	1.0	2.1	3.9	7.0	5.1	-2.7	-2.4	-2.3
Vietnam	6.0	6.2	6.4	4.1	3.8	4.5	5.5	4.7	3.9	-6.4	-6.0	-5.7
Latin America	0.8	1.2	2.8	7.6	7.7	7.9	-2.8	-2.9	-2.9	-4.6	-4.5	-4.1
Argentina	0.0	-1.0	1.0	NA	18.3	32.9	-1.0	-1.4	-1.2	-3.7	-4.7	-3.7
Brazil	0.0	0.1	1.6	6.3	6.7	6.0	-4.0	-3.8	-3.7	-6.1	-5.3	-4.5
Chile	1.5	2.5	4.0	4.4	2.9	3.0	-1.3	-2.4	-3.0	-2.0	-2.2	-1.9
Colombia	4.8	3.8	4.0	2.8	3.0	3.1	-4.5	-4.6	-4.6	-1.6	-1.5	-1.5
Costa Rica	3.0	2.5	3.5	4.5	4.4	4.5	-5.5	-4.8	-4.8	-6.7	-7.3	-8.0
Dominican Republic	6.8	5.4	4.8	3.1	1.9	3.0	-3.7	-3.0	-3.2	-4.0	-3.6	-4.5
El Salvador	2.0	2.2	2.5	1.2	0.7	1.8	-6.0	-5.4	-5.6	-3.4	-3.6	-3.5
Mexico	2.2	3.4	4.4	4.0	3.6	3.6	-2.2	-2.2	-2.6	-3.6	-3.5	-3.5
Panama	6.2	5.5	6.5	2.7	1.1	2.1	-9.0	-8.5	-6.7	-4.5	-3.5	-3.0
Peru	2.5	3.8	4.6	3.3	2.6	2.6	-5.6	-4.8	-5.9	0.5	-2.7	-1.7
Venezuela	-4.0	-4.4	1.9	61.3	70.3	80.0	4.4	2.4	4.2	-12.3	-12.9	-12.7
Europe	1.4	0.0	2.4	6.1	7.7	5.6	0.2	0.0	-0.7	-1.5	-2.5	-2.1
Bulgaria	1.5	1.2	2.0	-1.4	1.4	1.3	0.2	-0.5	-1.5	-3.7	-3.8	-2.0
Croatia	-0.7	0.3	1.3	-0.2	0.2	1.5	1.0	0.5	-0.5	-5.5	-5.6	-5.4
Czech Republic	2.3	2.5	3.1	0.4	0.6	2.2	0.0	0.2	-0.8	-1.9	-2.3	-2.0
Hungary	3.4	2.5	1.5	-0.2	0.0	2.4	4.2	4.7	4.0	-2.6	-2.4	-2.1
Kazakhstan	3.7	3.0	4.0	6.6	6.3	5.7	1.9	1.2	1.1	-2.4	-2.2	-1.9
Poland	3.3	3.4	3.6	0.0	-0.2	2.4	-1.2	-1.6	-2.3	-2.9	-2.3	-2.2
Romania	2.8	3.0	3.0	1.1	1.5	2.6	-0.5	-1.8	-2.2	-2.0	-1.9	-2.1
Russia	0.6	-3.0	1.5	7.8	12.5	6.8	3.2	3.2	2.3	0.0	-2.6	-1.5
Serbia	-2.0	-0.6	1.5	2.1	2.5	4.0	-6.5	-5.0	-4.5	-7.8	-6.0	-4.5
Slovakia	2.4	2.6	3.2	-0.1	0.6	2.2	0.5	0.0	0.3	-2.9	-2.8	-2.2
Turkey	2.9	3.3	3.4	8.9	5.5	7.0	-5.6	-4.3	-4.8	-1.3	-1.5	-2.9
Ukraine	-6.5	-3.0	1.9	12.1	17.5	8.6	-3.7	-2.6	-2.0	-10.0	-6.0	-4.0
Africa/Mideast	3.7	2.1	3.7	4.4	4.9	4.9	5.5	-0.8	0.2	-3.0	-7.3	-6.0
Bahrain	4.8	-2.4	1.5	2.5	2.1	2.2	5.8	-3.5	-2.4	-4.3	-8.5	-6.5
Egypt	3.2	3.4	4.3	10.1	8.9	8.7	-2.0	-2.3	-3.0	-11.7	-10.6	-10.4
Ghana	4.6	4.0	6.0	15.2	13.2	8.0	-8.9	-7.8	-8.3	-9.8	-7.6	-6.5
Iraq	0.1	6.0	4.2	2.5	5.0	5.0	-5.8	-8.7	-5.4	-4.5	-10.0	-8.6
Israel	2.4	2.2	2.5	0.5	0.3	1.4	2.0	1.9	3.3	-3.0	-3.3	-2.5
Jordan	3.6	3.8	4.3	3.0	4.0	4.2	-8.9	-4.5	-6.0	-6.4	-6.8	-6.8
Kenya	5.2	6.0	6.2	6.9	5.5	6.1	-12.3	-8.9	-8.5	-6.2	-6.0	-5.6
Kuwait	3.7	2.1	2.2	3.0	3.5	3.5	34.5	13.5	13.6	12.8	-12.2	-9.7
Lebanon	0.8	1.5	2.0	1.1	1.8	2.5	-27.9	-21.6	-20.7	-9.5	-9.6	-9.6
Nigeria	6.2	4.5	6.2	8.1	11.0	8.8	1.3	-2.5	-0.6	-2.0	-2.7	-2.3
Oman	5.0	-2.3	2.7	1.0	0.9	1.2	6.8	0.4	4.6	-1.9	-8.8	-5.3
Qatar	5.6	3.8	4.1	3.0	3.5	4.5	30.5	15.7	14.4	-2.6	-13.3	-12.9
Saudi Arabia	3.4	-3.3	1.7	2.9	3.0	3.4	12.1	-2.0	0.2	-1.8	-8.9	-6.2
South Africa	1.6	2.4	2.8	6.1	5.1	5.0	-5.3	-4.4	-4.1	-4.1	-4.1	-3.5
Tanzania	7.1	7.2	6.4	6.1	3.9	5.4	-13.7	-13.1	-12.5	-6.2	-6.5	-5.5
UAE	4.0	4.0	4.4	2.0	2.4	2.9	8.6	3.3	3.1	NA	NA	NA
Uganda	6.1	6.5	6.9	4.3	3.1	6.6	-9.7	-10.1	-11.0	-5.3	-5.6	-5.3
Zambia	6.5	6.0	6.1	7.8	7.5	6.8	0.5	-0.8	-1.5	-5.3	-5.0	-5.2
Total	4.1	3.9	4.7	4.4	4.3	4.2	1.7	1.3	1.1	-2.8	-3.5	-3.1

Source: Citi Research

Figure 15. Short Rate Forecasts (End of Period), as of 21 January 2015 (Percent)

	Current	1Q 15F	2Q 15F	3Q 15F	4Q 15F	1Q 16F	2Q 16F
United States	0.25	0.25	0.25	0.25	0.50	0.50	0.75
Japan	0.10	0.10	0.10	0.10	0.10	0.10	0.10
Euro Area	0.05	0.05	0.05	0.05	0.05	0.05	0.05
Canada	0.75	0.75	0.75	0.75	0.75	0.75	0.75
Australia	2.50	2.50	2.50	2.50	2.50	2.75	3.00
New Zealand	3.50	3.50	3.50	3.50	3.75	4.00	4.00
Denmark	0.05	0.00	0.00	0.00	0.00	0.10	0.10
Norway	1.25	1.00	0.75	0.75	0.75	0.75	0.75
Sweden	0.00	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25
Switzerland	-0.75	-1.50	-1.50	-1.50	-1.50	-0.75	-0.75
United Kingdom	0.50	0.50	0.50	0.50	0.50	0.75	1.00
China	2.75	2.50	2.25	2.25	2.25	2.25	2.25

Source: Citi Research

Figure 16. 10-Year Yield Forecasts (Period Average), as of 21 January 2015 (Percent)

	Current	1Q 15F	2Q 15F	3Q 15F	4Q 15F	1Q 16F	2Q 16F
United States	1.81	1.95	2.20	2.35	2.55	2.65	2.65
Japan	0.24	0.25	0.35	0.40	0.45	0.50	0.50
Euro Area (Bunds)	0.47	0.55	0.55	0.65	0.65	0.75	0.75
Canada	1.48	1.40	1.60	1.65	1.85	1.95	1.95
Australia	2.60	2.60	2.65	2.85	2.95	3.15	3.40
New Zealand	3.40	3.35	3.20	3.45	3.60	4.05	4.10
Denmark	0.53	0.75	0.70	0.80	0.80	0.90	0.90
Norway	1.38	1.50	1.40	1.50	1.55	1.65	1.70
Sweden	0.75	0.85	0.85	1.05	1.15	1.35	1.35
Switzerland	-0.21	0.05	0.05	0.10	0.10	0.15	0.15
United Kingdom	1.54	1.65	1.80	2.15	2.25	2.40	2.60

Source: Citi Research

Figure 17. 10-Year Yield Spread Forecasts (Period Average), as of 21 January 2015 (Percent)

	Spread vs. US$						Spread vs. Germany					
	Current	1Q 15F	2Q 15F	3Q 15F	4Q 15F	1Q 16F	Current	1Q 15F	2Q 15F	3Q 15F	4Q 15F	1Q 16F
United States	NA	NA	NA	NA	NA	NA	133	141	166	171	192	192
Japan	-157	-171	-186	-196	-212	-217	-23	-30	-20	-25	-20	-25
Euro Area (Germany)	-133	-141	-166	-171	-192	-192	NA	NA	NA	NA	NA	NA
Canada	-32	-55	-61	-71	-71	-71	101	85	106	101	121	121
Australia	79	66	46	51	41	51	212	207	212	222	232	242
New Zealand	159	142	101	112	107	142	293	283	268	283	298	334
France	-113	-121	-146	-151	-172	-172	20	20	20	20	20	20
Italy	-12	-31	-56	-61	-82	-82	121	110	110	110	110	110
Spain	-29	-51	-76	-71	-92	-102	104	90	90	100	100	90
Netherlands	-128	-136	-161	-166	-187	-187	6	5	5	5	5	5
Belgium	-104	-121	-146	-151	-172	-172	30	20	20	20	20	20
Austria	-126	-136	-161	-166	-187	-187	8	5	5	5	5	5
Finland	-132	-136	-161	-166	-187	-187	1	5	5	5	5	5
Ireland	-59	-91	-116	-121	-142	-142	74	50	50	50	50	50
Portugal	101	34	9	4	-17	-17	234	175	175	175	175	175
Greece	777	659	484	329	208	208	910	800	650	500	400	400
Denmark	-128	-121	-151	-156	-177	-177	6	20	15	15	15	15
Norway	-43	-46	-81	-86	-102	-102	90	95	85	85	90	90
Sweden	-106	-111	-136	-131	-142	-132	27	30	30	40	50	60
Switzerland	-201	-191	-216	-226	-247	-252	-68	-50	-50	-55	-55	-60
United Kingdom	-27	-30	-40	-20	-30	-25	106	111	126	151	161	166

Source: Citi Research

Figure 18. Emerging Market Countries — Short Rates Actual and Forecast of Additional Rate Moves (End of Period), as of 21 January 2015

	Current Rate	Mar 15F	Jun 15F	Sep 15F	Dec 15F	Mar 16F	Total Cumulative Rate Moves Expected
Romania	2.50	25	0	0	0	50	75
Mexico	3.00	0	0	0	50	25	75
Philippines	4.00	0	0	0	0	50	50
Chile	3.00	0	0	0	0	25	25
South Africa	5.75	0	0	0	0	25	25
Hungary	2.10	0	0	0	0	25	25
Turkey	8.29	-54	-75	50	75	25	21
Indonesia	5.75	0	0	0	0	0	0
Korea	2.00	0	0	0	0	0	0
Thailand	2.00	0	0	0	0	0	0
Israel	0.25	-25	0	0	25	0	0
China	2.75	-25	-25	0	0	0	-50
Poland	2.00	-50	0	0	0	0	-50
India	7.75	0	-25	0	-25	-25	-75
Brazil	11.75	75	0	0	-75	-75	-75
Russia	17.00	0	0	-200	-200	-200	-600

Source: Citi Research

Figure 19. Foreign Exchange Forecasts (End of Period), as of 21 January 2015

	vs. USD							vs. EUR						
	Current	Mar 15F	Jun 15F	Sep 15F	Dec 15F	Mar 16F	Jun 16F	Current	Mar 15F	Jun 15F	Sep 15F	Dec 15F	Mar 16F	Jun 16F
United States	NA	NA	NA	NA	NA	NA	NA	1.15	1.14	1.12	1.10	1.08	1.05	1.02
Japan	117	118	124	129	132	134	136	135	135	139	142	142	140	138
Euro Area	1.15	1.14	1.12	1.10	1.08	1.05	1.02	NA	NA	NA	NA	NA	NA	NA
Canada	1.20	1.20	1.22	1.25	1.26	1.27	1.28	1.39	1.37	1.37	1.37	1.35	1.33	1.30
Australia	0.82	0.80	0.76	0.73	0.72	0.71	0.71	1.41	1.42	1.47	1.52	1.50	1.47	1.43
New Zealand	0.78	0.75	0.71	0.68	0.67	0.66	0.66	1.48	1.52	1.57	1.63	1.61	1.58	1.54
Norway	7.61	7.74	7.73	7.73	7.91	8.13	8.37	8.78	8.83	8.68	8.53	8.50	8.50	8.50
Sweden	8.13	8.29	8.34	8.40	8.60	8.85	9.11	9.37	9.46	9.36	9.27	9.25	9.25	9.25
Switzerland	0.86	0.85	0.90	0.95	0.99	1.03	1.07	0.99	0.97	1.01	1.04	1.06	1.07	1.08
United Kingdom	1.51	1.52	1.50	1.47	1.44	1.41	1.37	0.76	0.75	0.75	0.75	0.75	0.74	0.74
China	6.21	6.23	6.26	6.29	6.27	6.23	6.19	7.2	7.1	7.0	6.9	6.7	6.5	6.3
India	61.9	62.8	63.3	63.9	64.1	64.2	64.3	71.3	71.6	71.1	70.5	68.9	67.1	65.3
Korea	1077	1107	1122	1137	1140	1140	1140	1242	1263	1259	1255	1226	1192	1158
Poland	3.75	3.79	3.80	3.82	3.89	3.98	4.08	4.32	4.32	4.27	4.21	4.18	4.16	4.14
Russia	65.4	64.0	63.6	63.2	63.9	64.7	65.6	75.4	73.0	71.4	69.8	68.7	67.7	66.6
South Africa	11.59	11.69	11.88	12.07	12.13	12.17	12.21	13.37	13.34	13.33	13.31	13.04	12.72	12.40
Turkey	2.34	2.38	2.43	2.49	2.52	2.54	2.56	2.70	2.71	2.73	2.75	2.71	2.65	2.60
Brazil	2.62	2.78	2.83	2.89	2.92	2.94	2.96	3.02	3.17	3.18	3.19	3.14	3.07	3.00
Mexico	14.6	14.7	14.5	14.2	14.1	14.1	14.0	16.9	16.8	16.2	15.7	15.2	14.7	14.2

Source: Citi Research

Figure 20. Foreign Exchange Forecasts (End of Period), as of 21 January 2015

	vs. JPY						
	Current	Mar 15F	Jun 15F	Sep 15F	Dec 15F	Mar 16F	Jun 16F
United States	117	118	124	129	132	134	136
Japan	NA	NA	NA	NA	NA	NA	NA
Euro Area	135	135	139	142	142	140	138
Canada	98	99	101	104	105	105	106
Australia	96	95	95	94	94	95	96
New Zealand	91.2	89.1	88.4	87.3	87.8	88.6	89.3
Norway	15.4	15.3	16.0	16.7	16.7	16.4	16.2
Sweden	14.4	14.3	14.8	15.4	15.3	15.1	14.9
Switzerland	137	140	138	136	133	130	127
United Kingdom	178	180	185	190	189	188	186
China	19	19	20	21	21	21	22
India	1.90	1.89	1.95	2.02	2.05	2.08	2.11
Korea	9.19	9.34	9.07	8.81	8.66	8.53	8.41
Poland	31.3	31.3	32.5	33.8	33.8	33.6	33.2
Russia	1.8	1.9	1.9	2.0	2.1	2.1	2.1
South Africa	10.1	10.1	10.4	10.7	10.9	11.0	11.1
Turkey	50.2	49.9	50.9	51.8	52.3	52.7	53.1
Brazil	44.7	42.7	43.7	44.7	45.1	45.5	45.9
Mexico	8.0	8.1	8.6	9.1	9.3	9.5	9.7

Source: Citi Research

Country Commentary

United States

William Lee

Peter D'Antonio

Beyond the boost to real incomes from lower oil prices, incoming data highlight the US economy's momentum, with solid gains in jobs, income, consumption, and industrial output. In addition, we expect an extra lift to US growth this year from the decline in crude oil prices from above $100 per barrel last summer to below $50 per barrel ($25 below our Dec-14 assumption). As a significant net oil importer (despite the rise in domestic production), the US economy will benefit by about $140 billion in net foreign transfers. Consequently, we recently raised our 2015 growth forecast to 3.6% from 3.0% previously, led by a pickup in consumer spending. We anticipate a return to a slower, albeit still above-potential, pace in 2016. The oil price plunge is likely to cut headline YoY inflation close to zero by midyear. This will probably be a temporary decline in measured inflation, and core inflation should not be similarly affected by the energy price plunge. However, core inflation may be restrained by USD appreciation, which may be prolonged by the monetary policy divergence between the Fed and other major central banks. We estimate underlying inflation likely will stay near 1.5% in coming quarters and remain well below the Fed's 2% target through 2016. We still expect monetary policy normalization will begin late this year. The December FOMC meeting confirmed our view that the current "zero rate" setting is not appropriate for an economy growing well above potential. Indeed, the Fed may use the temporary boost to growth from lower oil prices to begin raising rates sooner than our Dec-15 call. However, we and the Fed have emphasized that it is the pace of normalization — not the timing of the first hike — that will matter most for the yield curve, asset prices, and economic growth. The pace will be guided by developing economic and financial conditions and, regardless of the liftoff date, the pace of tightening likely will be gradual.

Figure 21. United States — Economic Forecasts, 2014-2016F

					2014		2015				2016	
		2014F	2015F	2016F	3Q	4QF	1QF	2QF	3QF	4QF	1QF	2QF
GDP	SAAR				5.0	3.0	3.5	3.4	3.1	2.8	2.8	2.9
	YoY	2.4	3.6	3.0	2.7	2.6	4.0	3.7	3.3	3.2	3.0	2.9
Domestic Demand	SAAR				4.1	2.7	3.6	3.7	3.3	3.2	3.2	3.3
	YoY	2.4	3.4	3.3	2.7	2.7	3.5	3.5	3.3	3.5	3.3	3.2
Consumption	SAAR				3.2	3.8	4.0	3.8	3.2	2.9	3.1	3.2
	YoY	2.5	3.6	3.1	2.7	2.7	3.4	3.7	3.7	3.5	3.2	3.1
Business Investment	SAAR				8.9	2.1	6.3	6.1	6.4	6.1	5.9	6.0
	YoY	6.1	6.0	6.2	7.6	5.5	6.7	5.8	5.2	6.2	6.1	6.1
Housing Investment	SAAR				3.3	2.0	4.3	9.7	12.5	11.4	10.2	7.4
	YoY	1.5	6.5	9.9	-0.7	2.1	4.6	4.8	7.1	9.4	10.9	10.4
Government	SAAR				4.4	-1.1	0.2	0.4	0.3	0.5	0.2	0.5
	YoY	-0.1	0.6	0.4	0.3	1.0	1.3	1.0	-0.1	0.4	0.4	0.4
Exports	SAAR				4.6	5.0	3.7	2.6	2.1	2.4	3.0	3.5
	YoY	3.2	4.0	3.0	3.8	2.6	6.0	4.0	3.4	2.7	2.5	2.8
Imports	SAAR				-0.9	4.6	3.6	4.6	4.5	3.9	4.2	5.1
	YoY	3.6	4.0	4.6	3.4	4.2	4.6	2.9	4.3	4.2	4.3	4.4
PCE Deflator	YoY	1.3	0.3	1.8	1.5	1.1	0.2	0.1	0.2	0.8	1.8	1.7
Core PCE Deflator	YoY	1.4	1.6	1.8	1.5	1.4	1.5	1.5	1.6	1.7	1.8	1.7
Unemployment Rate	%	6.2	5.3	5.1	6.1	5.7	5.5	5.3	5.2	5.2	5.2	5.1
Federal Gov't Balance (Fiscal Year)	$Bn	-483	-450	-550								
	% of GDP	-2.8	-2.5	-2.9								
General Gov't Balance (Cal Year)	% of GDP	-4.4	-4.1	-4.5								
Federal Debt	% of GDP	73	73	73								
General Gov't Debt	% of GDP	106	106	106								
Current Account	US$bn	-390	-255	-266	-443	-357	-260	-250	-255	-256	-257	-262
	% of GDP	-2.2	-1.4	-1.4	-2.5	-2.0	-1.4	-1.4	-1.4	-1.4	-1.4	-1.4
S&P 500 Profits (US$ Per Share)	YoY	8.0	7.5	NA	8.7	8.2	9.5	5.4	7.4	8.0	NA	NA

Notes: F Citi forecast. E Citi Estimate. YoY Year-to-year percent change. SAAR Seasonally adjusted annual rate. Domestic demand excludes inventories and net exports.
Sources: Bureau of Economic Analysis, Bureau of Labor Statistics, I/B/E/S, Treasury Department, *Wall Street Journal* and Citi Research forecasts

Japan

Kiichi Murashima

Naoki Iizuka

We expect 2015 will be a year of solid growth and virtually no inflation for the Japanese economy. Japanese companies and consumers will most likely enjoy a dramatic improvement in the terms of trade, driven by sharply lower oil prices — i.e., transfer of income from oil producers in the order of nearly Y10trn (2% of GDP) — in 2015. Most notably, consumer spending, the main culprit behind the technical recession of 2014, is likely to recover at a relatively solid pace, with steady growth in employment, a moderate rise in per-capita wages and a levelling-out in the CPI — caused by falling oil prices — expected to push up real total employment income.

The halving of oil prices is a complete game changer for an inflation outlook. Core inflation (excluding fresh food but including energy) will likely at least approach 0% and may turn negative, albeit temporarily, depending upon oil prices and the yen/dollar rate in coming months. As a base-case scenario, we expect core inflation will decline to +0.3% YoY in Q3 under the assumptions that oil prices will go back to high-$50s per barrel and the yen will weaken to above the ¥130/$ mark late this year. Even apart from the direct impact from energy, however, inflation remains quite tame, with the CPI excluding food and energy up just 0.4% YoY in November.

In this context, we continue to expect the Bank of Japan (BoJ) to implement additional easing measures in July 2015. When the BoJ expanded quantitative and qualitative easing in October 2014, policymakers pointed to an emerging risk that a decline in inflation, driven by sluggishness in demand in the wake of the tax hike and falling oil prices, will spill over to a renewed deflationary mindset. If (as seems likely in our view) headline inflation approaches 0% in coming quarters, the BoJ will probably act again in order to prevent a spillover to inflation expectations. In that event, increased purchases of JGBs and ETFs will likely continue to be the centrepiece, in our view.

Figure 22. Japan — Economic Forecasts, 2014-2016F

					2014		2015				2016	
		2014F	2015F	2016F	3Q	4QF	1QF	2QF	3QF	4QF	1QF	2QF
Real GDP	YoY	0.2	1.1	1.9	-1.2	-0.1	-1.0	1.3	2.3	2.0	1.9	1.9
	SAAR				-1.9	3.0	2.1	2.2	1.9	1.8	1.6	2.3
Domestic Demand	YoY	0.0	0.7	1.7	-1.5	-1.3	-2.3	1.0	2.0	2.0	1.8	1.8
	SAAR				-1.8	1.5	2.3	2.3	1.9	1.6	1.3	2.1
Private Consumption	YoY	-1.1	0.6	1.5	-2.7	-2.2	-3.6	2.1	2.1	2.0	1.6	1.5
	SAAR				1.5	2.1	2.6	2.2	1.6	1.7	0.9	1.8
Business Investment	YoY	4.2	3.1	4.0	1.8	2.1	-2.3	3.9	5.6	5.4	4.8	4.2
	SAAR				-1.5	5.3	6.7	5.3	5.1	4.4	4.2	3.1
Housing Investment	YoY	-5.0	-3.6	4.7	-12.2	-15.8	-17.0	-5.4	3.9	7.1	6.8	5.1
Public Investment	YoY	2.9	-4.4	-3.5	1.1	-1.0	-1.0	-3.5	-6.0	-7.0	-6.0	-5.0
Exports	YoY	8.0	5.1	3.6	7.5	10.1	4.6	6.1	5.7	4.0	3.8	3.5
	SAAR				5.2	11.1	4.3	3.9	3.6	4.2	3.3	2.9
Imports	YoY	6.7	2.4	2.5	4.9	1.8	-2.8	4.0	4.3	4.6	3.6	2.8
	SAAR				3.0	2.2	5.8	4.9	4.2	3.5	1.8	1.9
CPI	YoY	2.8	1.0	1.0	3.3	2.7	2.7	0.6	0.3	0.5	0.8	1.0
Core CPI	YoY	2.6	0.9	1.0	3.2	2.7	2.6	0.4	0.3	0.5	0.8	1.0
Nominal GDP	YoY	1.5	1.8	2.4	-0.9	0.8	0.6	1.0	0.3	0.6	0.6	0.7
Current Account	¥ tn	2.7	13.3	12.1	2.6	11.1	14.7	13.6	12.5	12.3	12.5	12.0
	% of GDP	0.6	2.7	2.4	0.5	2.3	3.0	2.7	2.5	2.5	2.5	2.4
Unemployment Rate	%	3.6	3.4	3.2	3.6	3.5	3.5	3.5	3.4	3.3	3.3	3.3
Industrial Production	YoY	2.1	3.3	3.4	-1.0	-1.3	-1.5	3.1	6.2	5.6	3.6	3.8
Corporate Profits (Fiscal Year)	YoY	12.5	22.5	12.5								
General Govt. Balance (Fiscal Year)	% of GDP	-7.3	-6.6	-6.2								
General Govt Debt	% of GDP	244	247	249								

F Citigroup forecast. SAAR Seasonally adjusted annual rate. YoY Year-to-year percent change. Corporate profits are TSE-I nonfinancials consolidated recurring profits. Source: Citi Research

Euro Area

Guillaume Menuet

Ebrahim Rahbari

Antonio Montilla

We are adding 0.1pp to our 2015 real GDP estimates to 1.3% compared to our 2015 Year Ahead forecasts (6 Jan), a 0.2pp cumulative adjustment versus the forecast in Prospects for 2015 (Dec 1). Our 2016 growth forecast (1.9%) is unchanged versus the Jan 6 forecast (but up from 1.6% in *Prospects*), and this would be the fastest expansion since 2010. Lower oil prices will lift real incomes, while we also anticipate a significant weakening in the euro effective exchange rate (partly through a depreciation of EUR/USD to parity by mid-2016) — which should help to support exports and corporate investment. We would also note that in recent years, downside inflation surprises have tended to be followed by upward real GDP surprises in the next year. Hence our more constructive GDP trajectory in 2015-16 after negative inflation surprises in 2014, and very likely in 2015 too.

The rapid drop in oil prices will also weigh noticeably on euro area inflation throughout 2015, before base effects and currency-induced gains in import prices lead to a temporary rebound in headline HICP rates in 2016. We now estimate that YoY inflation will probably be slightly negative on average in 2015 at -0.1%, compared to our forecast of a 0.8% gain two months ago, given that Brent is down from $80 per barrel to less than $50 since then. Turning to 2016, we envisage a temporary rebound in CPI inflation to 1.6% (versus 1.5% previously). We expect that the ECB will announce a €600bn QE programme on Jan 22, supported by a comfortable majority of Governing Council members. However, we see significant risks that the ECB will underwhelm at the first attempt, with the programme likely to be probably more conservative than investors would desire, partly to maximize the number of 'Yes' votes, but also because of the likely reluctance to pre-commit. A 'hybrid programme' based on partial mutualisation of sovereign risk would still be positive compared to one relying solely on national central banks assuming their respective sovereign issuer risk. Overall, we suspect that the limited amount of inflation likely to be generate by QE1, will probably lead to another QE programme (similar to the Fed, BoE and BoJ), possibly by mid-2016.

Figure 23. Euro Area — Economic Forecasts, 2014-2016F

					2014		2015				2016	
		2014F	2015F	2016F	3Q	4QF	1QF	2QF	3QF	4QF	1QF	2QF
Real GDP	YoY	0.8	1.3	1.9	0.8	0.7	0.8	1.1	1.4	1.8	1.8	1.9
	SAAR				0.6	0.6	1.8	1.6	1.8	2.0	2.0	2.0
Final Domestic Demand	YoY	0.9	1.4	1.6	0.9	0.8	1.0	1.4	1.5	1.6	1.7	1.6
Private Consumption	YoY	0.9	1.6	1.6	1.1	1.2	1.5	1.7	1.5	1.6	1.6	1.5
Government Consumption	YoY	0.9	0.9	0.6	1.1	0.7	0.8	0.8	0.8	1.1	1.0	0.7
Fixed Investment	YoY	0.7	1.3	2.9	0.1	-0.3	-0.2	1.0	1.9	2.3	2.6	2.8
Business Equipment	YoY	2.0	1.8	3.1	1.8	0.9	1.3	1.4	2.1	2.5	2.9	3.1
Construction	YoY	-0.9	0.5	2.5	-2.0	-1.9	-2.0	0.6	1.6	2.0	2.3	2.4
Stocks (Contrib. to Y/Y GDP Growth)		-0.1	0.1	0.0	-0.3	0.0	-0.1	0.1	0.1	0.1	0.1	0.0
Exports	YoY	3.3	3.2	3.9	3.3	3.1	3.6	3.0	3.1	3.3	3.4	3.8
Imports	YoY	3.4	3.8	3.3	3.1	3.7	4.2	3.8	3.5	3.5	3.4	3.3
CPI	YoY	0.4	-0.1	1.6	0.4	0.2	-0.5	-0.4	-0.2	0.5	1.5	1.7
CPI Ex Unprocessed Food & Energy	YoY	0.9	0.8	1.0	0.9	0.7	0.7	0.7	0.8	0.9	1.0	1.0
Unemployment Rate	YoY	11.3	10.8	10.1	11.0	10.7	11.7	10.9	10.6	10.1	11.1	10.2
Current Account Balance	€bn	252.7	272.4	253.1								
	% of GDP	2.5	2.7	2.4								
General Government Balance	€bn	-252.5	-225.3	-190.7								
	% of GDP	-2.5	-2.2	-1.8								
Primary Balance	% of GDP	0.3	0.7	1.1								
General Government Debt	€bn	9,591.8	9,796.6	9,987.4								
	% of GDP	95.3	95.3	94.4								
Gross Operating Surplus	YoY	1.9	3.8	2.6								

We publish further details of our European forecasts monthly in European Economic Forecast Highlights. Sources: Eurostat and Citi Research

Germany

Ebrahim Rahbari

The turnaround in sentiment and the fall in oil prices has led us to revise up our German growth forecasts and we now expect growth of 1.5% in 2015 and 2.0% in 2016 (from 1.1% and 1.6% previously). Recently, (modest) German growth has been mostly consumption-based and we continue to expect growth in coming years to be domestically-driven. Meanwhile, inflation is falling fast in Germany, too, and is likely to be negative soon, with inflation for 2015 as a whole likely to be around zero.

France

Guillaume Menuet

We raise our 2015-16 real GDP forecasts to 0.9% and 1.8% respectively, versus 0.7% and 1.6% previously. The main developments in the last few months have been a modest pick-up in sentiment surveys, accompanied by some resurgence in the abysmal popularity ratings of the French President. The much lower euro and oil price plunge are likely to support consumer spending and lift corporate profits, albeit with a lag. Households' discretionary spending is also likely to increase, in our view, as lower inflation will boost real disposable incomes. Concerns about rising levels of taxes will likely be partially allayed by promises of a decrease in fiscal pressure for households, leading to a modest drop in the household saving ratio. The main uncertainty for the forecast is the impact of the terrorist attacks on confidence.

Italy

Antonio Montilla

Short-term indicators suggest the Italian economy remained in recession in Q4 14, and we expect real GDP QQ growth to be at best 0.1% in Q1. Export growth remains subdued while the recent pick-up in real disposable income (due to "lowflation" and the personal income tax cut introduced in May 2014) has failed so far to cause a rebound in consumer spending. Yet, we expect that improved financial conditions (due to ECB QE) and a more supportive fiscal stance together with the decline in oil prices will support domestic demand in coming years. We have revised up our real GDP forecasts to 0.4% in 2015 and 1.1% in 2016 (from 0.3% and 1.0% respectively, previously). We expect the presidential elections starting on Jan 29 will not be destabilising in policy or market terms (unlike the Greek case, the government has a sufficient majority to elect a candidate), and that Italian politics will remain relatively stable in 2015.

Figure 24. Germany, France and Italy — Economic Forecasts, 2014-16F

		Germany			France			Italy		
		2014F	2015F	2016F	2014F	2015F	2016F	2014F	2015F	2016F
Real GDP	YoY	1.5	1.5	2.0	0.3	0.9	1.8	-0.4	0.4	1.1
Final Domestic Demand	YoY	1.5	1.8	2.1	0.4	0.9	1.4	-0.4	0.4	0.9
Private Consumption	YoY	1.2	2.1	1.9	0.6	1.2	1.5	0.3	0.7	0.8
Government Consumption	YoY	1.2	1.6	1.5	1.9	1.7	0.3	-0.3	-0.3	0.1
Fixed Investment	YoY	2.9	1.1	3.2	-1.7	-0.6	2.3	-2.5	0.0	2.2
Exports	YoY	3.8	2.8	2.8	2.1	3.1	4.1	1.8	2.6	3.6
Imports	YoY	3.6	4.2	3.5	3.5	2.9	2.3	0.3	2.4	3.1
CPI	YoY	0.9	0.0	1.7	0.6	0.1	1.7	0.2	-0.2	1.2
Unemployment Rate	%	5.0	5.0	4.8	9.8	10.1	9.8	12.8	13.2	12.8
Current Account	€bn	210.5	222.8	203.4	-22.1	-8.9	1.9	25.6	26.8	27.6
	% of GDP	7.3	7.6	6.7	-1.0	-0.4	0.1	1.6	1.6	1.7
General Govt. Balance	€bn	8.3	5.3	2.7	-91.6	-85.1	-77.2	-47.8	-47.7	-35.4
	% of GDP	0.3	0.2	0.1	-4.3	-4.0	-3.5	-3.0	-2.9	-2.1
Primary Balance	% of GDP	2.1	1.9	1.7	-2.1	-1.8	-1.4	1.7	1.4	1.9
General Govt. Debt	% of GDP	74.8	72.8	70.9	96.1	99.1	99.3	131.5	133.2	132.7
Gross Trading Profits	YoY	1.2	0.4	2.0	1.9	3.6	4.5	NA	NA	NA

F Citi forecast. YoY Year-to-year growth rate. Note: The German annual figures are derived from quarterly Bundesbank data and adjusted for working days. Forecasts for GDP and its components are calendar adjusted. Sources: Deutsche Bundesbank, Statistisches Bundesamt, INSEE, ISTAT and Citi Research

Spain

Antonio Montilla

We are revising up our real growth forecasts to 2.2% for both 2015 and 2016, from 2.0% and 2.1% respectively previously, mainly reflecting the impact of falling oil prices on domestic demand. The recovery continues to be driven by private consumption (supported by a record-low household saving rate) and business investment, despite ongoing private deleveraging pressures. We estimate Q1 real GDP growth to rise to 0.6% QQ (largest since Q4 2007), supported by the cuts in both personal and corporate income taxation as well as negative inflation. We expect the government to overshoot its fiscal deficit targets in coming years.

Greece

Ebrahim Rahbari

The outlook for Greece continues to be dominated by political factors. The prospect of opposition far-left Syriza party winning the upcoming parliamentary election on January 25 has revived concerns about potential government default and Grexit. In our view, Grexit is not the most likely outcome, even if Syriza leads the next Greek government, as the mutual incentives of Eurozone creditors and the Greek government to keep Greece in the Eurozone are very high. Political uncertainty may be a drag on growth, but the fall in oil prices should still allow Greece to eke out positive growth (we continue to expect 1.5% growth in 2015 and 1.7% in 2016).

Ireland

Michael Saunders

The economy is booming, fuelled by a mix of strong job gains, supply-side flexibility and loose monetary policy. GDP growth in 2014 probably was about 5% YoY, and – with house prices up 16% YoY and the composite PMI more than one standard deviation above the average since 2000 -- we expect growth of 4%+ in 2015. Fiscal policy remains cautious, and is predicated on relatively pessimistic assumptions about potential growth. As a result, the public debt/GDP ratio is likely to continue to fall rapidly, dropping below 100% next year.

Portugal

Antonio Montilla

We are edging up our GDP growth forecasts by 0.2pp to 1.7% in 2015 and by 0.1pp to 2.1% in 2016. Private consumption and investment should continue to expand at a relatively steady pace, while we expect export growth to benefit from the weaker euro and some pick-up in growth of Portugal's main trading partners. The public debt-to-GDP ratio is likely to start falling in 2015 (after peaking at around 135% in 2014), although we expect the fiscal deficit to stay above the 2.7% of GDP target.

Figure 25. Spain, Greece, Ireland and Portugal — Economic Forecasts, 2014-16F

		Spain			Greece			Ireland			Portugal		
		2014F	2015F	2016F	2014F	2015F	2016F	2014F	2015F	2016F	2014F	2015F	2016F
Real GDP	YoY	1.4	2.2	2.2	0.8	1.5	1.7	5.0	4.4	7.8	0.9	1.7	2.1
Final Domestic Demand	YoY	2.0	2.7	2.0	-0.4	0.9	1.3	2.4	2.4	3.4	1.6	1.9	1.3
Private Consumption	YoY	2.3	2.9	1.9	0.3	0.8	0.9	0.6	1.9	2.4	2.1	2.3	1.6
Government Consumption	YoY	0.5	0.5	0.5	-0.7	0.2	0.3	1.2	-2.5	0.3	-0.6	-0.5	-0.2
Fixed Investment	YoY	2.8	4.4	3.7	-4.3	3.5	5.4	9.0	8.6	8.7	2.3	2.8	2.1
Exports	YoY	4.8	5.9	5.0	10.2	5.6	4.4	12.4	7.9	8.0	2.7	5.4	6.1
Imports	YoY	8.2	8.4	4.4	7.4	2.9	3.1	11.3	7.2	4.4	6.0	5.0	4.2
CPI	YoY	-0.2	-1.0	1.2	-1.4	-1.7	-0.3	0.3	1.0	1.1	-0.2	-0.4	1.1
Unemployment Rate	%	24.4	22.6	21.1	26.5	25.2	24.4	11.4	9.9	8.7	13.9	12.4	11.0
Current Account	€bn	-2.1	5.1	5.1	2.5	1.9	1.9	10.9	13.3	19.5	0.2	0.5	0.9
	% of GDP	-0.2	0.5	0.5	1.4	1.1	1.1	5.9	6.8	9.2	0.1	0.3	0.5
General Govt. Balance	€bn	-58.9	-48.4	-36.2	-3.1	-3.1	-2.2	-7.0	-5.1	-1.3	-7.3	-5.8	-4.5
	% of GDP	-5.6	-4.5	-3.3	-1.7	-1.7	-1.2	-3.8	-2.6	-0.6	-4.2	-3.3	-2.5
Primary Balance	% of GDP	-2.3	-1.5	-0.5	2.3	2.3	2.7	0.3	1.2	3.0	0.8	1.9	2.5
General Govt. Debt	% of GDP	97.3	99.9	100.5	178.0	178.5	176.3	110.4	108.0	98.7	134.9	133.2	130.9

Note: Source: Citi Research

Netherlands

Guillaume Menuet

We are raising our Dutch GDP forecasts, pencilling in a stronger contribution from domestic demand as a result of the drop in oil prices. We also expect that the further loosening in financial conditions will contribute to a faster recovery, and anticipate that house prices will increase further in 2015 and 2016, alongside a drop in unemployment. The tight fiscal stance is likely to curb the recovery in demand, but ensure that the budget deficit continues to narrow steadily.

Belgium

Guillaume Menuet

The Belgian government has been facing a series of strikes throughout December, with widespread demonstrations against the new administration's austerity plans designed to raise competitiveness and reduce public sector debt. Business confidence has been treading water in the last couple of months. We suspect that the government is unlikely to back down, given the need for further budgetary adjustments as indicated by the European Commission in granting Brussels three more months to demonstrate its ability to "take the necessary measures".

Slovakia

Jaromir Sindel

Our momentum guide worsened in November on the back of weaker industrial production and retail sales. Hence, we keep our forecast of milder GDP growth at 0.4% QoQ in 4Q14 after 0.6% in 3Q14. However, with lower oil prices, benign labour market trends and somewhat stronger foreign demand outlook, we are lifting our forecasts for 2015 and 2016 GDP growth by 0.1%pt each year to 2.6% YoY and 3.2% respectively. The likely ECB QE program may indirectly cover 30-65% of ARDAL's issuance needs in 2015 and 2016.

Slovenia

Jaromir Sindel

Given the poor performance of our momentum guide in 4Q14, we keep our forecast of a mild quarterly GDP contraction in 4Q14. However, foreign demand and oil price trends should support GDP growth in 2015. Although the cash deficit is likely to be virtually unchanged and is likely to reach -3.5% of GDP in 2015, the government is sticking to its goal of narrowing the general government deficit to 2.8% of GDP in 2015. We assume the privatization process will continue, although it is likely to increase coalition tensions.

Figure 26. Netherlands, Belgium, Slovakia and Slovenia — Economic Forecasts, 2014-16F

		Netherlands			Belgium			Slovakia			Slovenia		
		2014F	2015F	2016F	2014F	2015F	2016F	2014F	2015F	2016F	2014F	2015F	2016F
Real GDP	YoY	0.7	1.4	1.9	1.0	1.2	1.8	2.4	2.6	3.2	2.4	1.8	2.3
Final Domestic Demand	YoY	0.3	0.8	1.1	1.4	1.3	1.5	3.3	2.5	2.8	1.4	1.1	1.4
Private Consumption	YoY	-0.1	0.8	1.0	0.9	1.0	1.3	2.3	2.0	2.4	0.6	1.3	1.3
Government Consumption	YoY	0.1	0.0	0.3	0.1	0.4	0.9	4.0	2.5	1.9	-0.6	-0.4	-0.8
Investment (Ex Stocks)	YoY	1.4	1.9	2.3	3.9	3.1	2.7	5.6	3.8	4.6	5.5	1.4	3.7
Exports	YoY	3.9	3.2	3.4	3.4	4.3	4.1	5.3	4.9	7.3	5.4	7.9	7.6
Imports	YoY	3.9	2.8	2.8	2.8	4.7	3.9	6.4	5.8	7.6	4.7	7.2	7.2
CPI (Average)	YoY	0.3	0.0	1.7	0.5	-0.4	1.4	-0.1	0.6	2.2	0.2	-0.4	2.8
Unemployment Rate	%	8.3	7.7	7.2	8.5	8.4	8.2	12.8	11.8	11.1	9.6	9.2	8.8
Current Account	% of GDP	10.6	8.9	7.7	0.1	-0.2	0.1	0.5	0.0	0.3	3.5	5.0	5.0
General Govt Balance	% of GDP	-1.9	-1.5	-1.3	-2.8	-2.7	-2.4	-2.9	-2.8	-2.2	-4.2	-2.9	-2.5
Primary Balance	% of GDP	-0.3	0.0	0.1	0.3	0.5	0.7	-2.1	-1.9	-1.3	-1.3	-0.1	0.5
General Govt Debt	% of GDP	69.2	69.3	68.2	106.1	107.9	106.9	54.6	54.8	52.6	81.9	79.4	77.8

F Citi forecast. YoY Year-on-year growth rate. Sources: National sources and Citi Research forecasts

United Kingdom

Michael Saunders

The coming year is likely to mark a major transition for the UK. The initial stages of recovery, in 2010-12, were characterized by sluggish real growth, relatively high inflation, high unemployment (well above the 5.1% average of 2000-07), falling real wages, and rising public debt/GDP ratio. The last two years (2013-2014) have seen stronger real growth, with below-consensus inflation. But real wages have continued to fall (until late-2014), the public debt ratio is still rising, and unemployment remains relatively high. We expect strong (and above-consensus) real GDP growth of about 3.0% YoY for 2015, with a similar pace in 2016. But, in other ways, 2015 is likely to differ significantly from recent years, with record lows in CPI inflation (and perhaps even a brief period of negative YoY inflation), the jobless rate back to or below 5%, and a return to significant real wage gains. Moreover, the public debt/GDP ratio is likely to soon start to fall (probably in 2016). In addition, we expect 2015-16 will highlight improvements in some aspects of the economy's underlying performance, with faster productivity gains, a further rise in profits, and more evidence that the equilibrium jobless rate has fallen. With lower oil prices and the prospect of lower household gas prices, CPI inflation may well turn briefly negative in H1 and is likely to stay below 1% YoY until yearend. As a result, we now expect the MPC will keep rates on hold all year (versus previous forecast of a Q4-15 hike), unless sterling weakens sharply or the domestic economy overheats markedly.

Political worries are likely to rise as the election (May 7) approaches, and persist afterwards. At present, the most likely outcome is either a multi-party coalition or a minority government and both would be relatively weak. The main parties have broadly similar fiscal plans for the next 2-3 years, but a Conservative-led government would pose Brexit risks, while a Labour-led one would pose risks over business tax and regulation. Either scenario would create some uncertainties that may hit business investment, and we have tried to build this into our forecast.

Figure 27. United Kingdom — Economic Forecasts, 2014-2016F

					2014		2015				2016	
		2014F	2015F	2016F	3Q	4QF	1QF	2QF	3QF	4QF	1QF	2QF
Real GDP	YoY	2.6	3.0	3.0	2.5	2.9	3.1	3.0	3.1	3.0	3.0	3.1
	SAAR				2.7	2.9	3.1	3.4	2.8	2.6	3.3	3.5
Domestic Demand	YoY	3.1	3.2	3.2	2.4	2.4	2.8	3.4	3.1	3.6	3.4	3.3
(Incl. Inventories)	SAAR				4.2	1.0	4.0	4.3	3.0	3.0	3.4	3.7
Private Consumption	YoY	2.4	3.5	3.3	2.5	3.1	3.4	3.9	3.6	3.3	3.4	3.2
	SAAR				3.8	4.0	3.8	3.8	2.7	3.1	3.9	3.3
Government Consumption	YoY	1.3	0.2	-1.1	1.9	1.1	0.7	0.0	-0.3	0.2	-0.1	-0.5
	SAAR				1.2	-3.2	-0.6	2.7	-0.1	-1.0	-2.1	1.3
Investment	YoY	7.3	7.7	7.5	6.4	6.1	6.5	6.9	8.8	8.5	8.0	7.8
	SAAR				0.6	8.3	10.8	8.2	7.8	7.4	8.5	7.4
Exports	YoY	-0.8	3.3	4.8	-0.9	2.6	2.4	3.7	4.1	2.8	3.8	4.7
	SAAR				2.6	8.9	1.7	1.8	4.4	3.5	5.4	5.5
Imports	YoY	0.7	3.8	5.3	-1.4	0.5	1.3	4.4	4.4	5.0	5.2	5.4
	SAAR				5.2	2.2	5.0	5.2	5.0	4.8	5.8	6.1
Unemployment Rate	%	6.2	5.3	4.3	6.0	5.8	5.6	5.5	5.2	4.9	4.7	4.4
CPI Inflation	YoY	1.5	0.3	1.6	1.5	0.9	0.2	0.0	0.2	0.8	1.6	1.7
Merch. Trade	£bn	-120.8	-121.2	-124.7								
	% of GDP	-6.7	-6.5	-6.4								
Current Account	£bn	-96.8	-96.2	-103.5								
	% of GDP	-5.4	-5.1	-5.3								
PSNB	£bn FY	-95.0	-72.7	-34.2								
	% of GDP	-5.2	-3.8	-1.7								
General Govt. Balance	% of GDP	-5.4	-4.0	-1.9								
Government Primary Balance		-3.2	-1.7	0.7								
Public Debt	% of GDP	88.2	89.4	88.1								
Gross Nonoil Trading Profits	YoY	12.5	8.2	3.9								

Source: Citi Research

Switzerland

Michael Saunders

The SNB's surprise decision to end its CHF 1.20/€ FX cap — and the subsequent sharp appreciation of the CHF — has probably set the stage for severe deflation and recession in Switzerland. We expect real GDP to fall by about 1% this year and to again fall slightly in 2016, with CPI inflation of roughly minus 2.5% this year and continued (albeit milder) deflation in later years. This would represent the biggest YoY decline in prices for any advanced economy over the last 35 years, apart from the steep deflation in HK during 1999-2003. In response, we expect the SNB will move its policy rate into even more deeply negative territory, with the likelihood of some kind of additional policies to inhibit capital inflows (perhaps through taxation) if the currency stays around parity versus the euro.

Sweden

Tina Mortensen

With modest growth, low and undershooting inflation plus falling inflation expectations, we continue to believe that the Riksbank will cut rates at the 11 February meeting and prepare a QE program to launch in subsequent months. The early 22 March election has been cancelled after the government and the Alliance parties reached an agreement, making it possible for minority governments to get their budgets through Parliament. Under the agreement, the opposition's budget will apply this year, but the government will be allowed to make some smaller changes.

Denmark

Tina Mortensen

GDP growth looks set to be positive in 2014, the first year of expansion since 2011. House prices are rising and private consumption is picking up, and should continue to get support from lower oil prices. We are lifting our 2015 GDP forecast by 0.3pp to 1.4% Y/Y, and expect a further pick-up in growth next year. Deflation is likely to also be a topic in Denmark, albeit only temporarily, driven by lower oil prices and tax changes. To keep pace with ECB's extraordinary measures, the DNB may well be forced to cut the CD-rate deeper into negative territory.

Norway

Tina Mortensen

The Norwegian economy is well prepared to handle lower oil prices, given the country's large wealth fund and scope to loosen fiscal policy (within the fiscal rules) despite reduced revenues from oil production. Nevertheless, the drop in oil prices will inevitably weigh on growth for a period, although the weaker NOK should boost non-oil exports. We expect fiscal policy to turn moderately more expansionary and forecast a 25bp rate cut in both March and May.

Figure 28. Switzerland, Sweden, Denmark and Norway — Economic Forecasts, 2014-2016F

		Switzerland			Sweden			Denmark			Norway		
		2014F	2015F	2016F	2014F	2015F	2016F	2014F	2015F	2016F	2014F	2015F	2016F
Real GDP	YoY	1.9	-0.9	-0.3	1.9	2.3	2.6	0.9	1.4	1.7	2.6	1.6	1.9
Final Domestic Demand	YoY	1.0	1.9	1.5	2.7	2.9	2.5	0.9	1.6	1.7	2.1	1.5	1.8
Private Consumption	YoY	1.0	1.8	1.5	2.4	2.8	2.7	0.4	1.6	1.9	1.7	1.8	2.0
Government Consumption	YoY	1.1	1.4	1.2	1.5	1.8	0.9	0.9	0.9	0.6	3.1	2.4	2.4
Investment (Ex Stocks)	YoY	1.1	2.3	1.5	4.7	4.2	4.0	2.2	2.4	2.9	1.8	-0.5	0.4
Exports	YoY	-9.5	-5.5	-2.2	2.2	3.4	4.9	2.9	2.1	3.5	2.6	3.5	4.1
Imports	YoY	-10.9	-4.3	0.5	5.0	4.5	4.6	3.9	2.9	3.6	1.7	1.6	1.9
CPI (Average)	YoY	0.0	-2.5	-0.8	-0.2	0.1	1.3	0.6	0.6	1.5	2.0	2.4	2.6
Unemployment Rate	%	3.2	3.4	4.0	8.0	7.6	7.3	6.6	6.5	6.3	3.5	4.0	4.2
Current Account	% of GDP	11.2	8.5	7.6	5.9	5.8	5.6	6.8	6.3	6.1	9.3	9.8	10.1
General Govt Balance	% of GDP	0.7	-0.1	-0.7	-2.3	-1.9	-1.0	2.0	-2.5	-2.3	9.7	9.0	9.3
General Govt Debt	% of GDP	46.7	46.8	46.3	42.2	43.1	42.5	42.3	44.0	44.9	NA	NA	NA

Source: Citi Research

Canada

Dana M. Peterson

Tumbling crude oil prices threaten to derail the Canadian expansion, dampen CPI inflation, and delay the resumption of BoC policy tightening. Risks to the Canadian inflation outlook have shifted from neutral to negative in our view. The BoC in a surprise move cut rates at its January meeting in response. Hence, we further delay our call for the next BoC interest rate hike from 1Q 2016 to 3Q 2016. The BoC also has additional cause to wait if US Fed tightening lifts global bond yields.

The oil shock's near-term effect on the Canadian economy is mixed: consumers and firms benefit from cheaper energy costs, while conventional and shale oil producers are being forced to cut production and investment. But if oil prices remain depressed at current levels, then the net effect will be negative for Canada. Even oil sands producers, who are less sensitive to price declines, might be compelled to reduce production beyond this year if crude oil prices do not settle at higher levels.

Protracted weakness in the oil sector and supportive industries like construction, finance, and housing, likely would reduce Canada's terms-of-trade, limit exports, erode corporate profits, and hinder investment. Without investment, conventional and shale producers would be unable to operate effectively and oil sands producers may fail to bring new phases of their operations online. Households may be subject to layoffs, lower incomes, and reduced net worth — moderating consumption. The anticipated mild correction in the housing market may also morph into a recession.

As GDP growth ebbs, input costs decline, and retail competition intensifies, firms will be hard pressed to lift prices. Both total and core CPI inflation are unlikely to converge on the BoC's 2-percent target until late 2017. Downside risks include: (1) weak global growth; (2) low commodity prices; (3) failure of the internal demand rotation to come to fruition; and (4) household imbalances. Upside risks include (1) cheaper energy prices; (2) US outperformance; and (3) further CAD depreciation.

Figure 29. Canada — Economic Forecast, 2014-2016F

					2014		2015				2016	
		2014F	2015F	2016F	3Q	4QF	1QF	2QF	3QF	4QF	1QF	2QF
Real GDP	YoY	2.4	2.0	1.8	2.6	2.4	2.6	2.1	1.8	1.6	1.6	1.6
	SAAR				2.8	2.0	1.9	1.7	1.5	1.3	1.7	2.1
Final Domestic Demand	YoY	1.6	1.7	1.5	1.8	1.9	2.3	1.8	1.4	1.3	1.3	1.4
	SAAR				2.8	1.3	1.7	1.5	1.1	0.9	1.5	1.9
Private Consumption	YoY	2.7	2.8	2.0	2.8	2.6	3.1	2.8	2.6	2.6	2.2	2.0
	SAAR				2.8	2.0	3.4	3.0	2.2	1.7	2.0	2.0
Government Spending	YoY	-0.1	0.6	0.8	0.0	0.4	0.7	0.5	0.6	0.5	0.6	0.8
	SAAR				0.3	0.7	0.5	0.5	0.6	0.5	1.0	1.0
Private Fixed Investment	YoY	0.5	-0.1	0.8	1.1	1.4	1.7	0.5	-1.3	-1.5	-0.9	0.2
	SAAR				5.9	-0.3	-1.7	-1.7	-1.5	-1.0	0.8	2.7
Exports	YoY	5.0	3.3	3.9	7.4	4.9	5.6	2.1	1.5	3.9	3.9	3.8
	SAAR				6.9	-5.6	3.7	4.0	4.2	3.5	3.7	3.9
Imports	YoY	1.5	3.0	3.0	2.5	2.2	4.2	2.6	2.4	2.9	2.9	3.0
	SAAR				4.0	0.4	3.0	3.1	3.0	2.5	3.0	3.3
CPI	YoY	1.9	0.4	2.1	2.1	1.9	0.2	0.3	0.5	0.7	2.2	2.0
Core CPI	YoY	1.8	2.0	1.6	2.0	2.2	2.2	2.1	2.0	1.8	1.7	1.6
Unemployment Rate	%	6.9	6.8	6.8	6.9	6.6	6.8	6.7	6.8	6.8	6.9	6.9
Current Account Balance	C$bn	-43.4	-70.3	-63.9	-33.6	-54.6	-70.5	-72.5	-71.4	-66.7	-66.5	-66.5
	% of GDP	-2.2	-3.5	-3.0	-1.7	-2.7	-3.5	-3.6	-3.5	-3.3	-3.2	-3.2
Net Exports (Pct. Contrib.)		1.0	0.0	0.2	0.9	-1.9	0.2	0.2	0.3	0.3	0.2	0.1
Inventories (Pct. Contrib.)		-0.3	0.2	0.0	-1.0	2.3	0.0	0.0	0.0	0.1	0.0	0.0
Budget Balance (Fiscal Year)	% of GDP	-0.1	-0.1	0.0								
Federal Budget Debt	% of GDP	30.9	30.2	29.0								
General Govt. Debt	% of GDP	87.8	87.4	85.6								

F Citi forecast. YoY Year-to-year percent change. SAAR Seasonally adjusted annual rate. Sources: Statistics Canada and Citi Research forecasts

Australia

Paul Brennan

Joshua Williamson

Low interest rates will continue to support strong housing investment and reasonable consumer spending but the key issue is whether weak consumer confidence, the declining terms of trade and subdued wealth effects continue to restrain domestic demand growth. Early evidence since our last update in November looks promising. The fall in energy costs and pick-up in employment should lift confidence and therefore spending. Importantly, a stronger consumer would probably encourage a pick-up in non-mining business investment. Underlying CPI inflation is likely to be in the bottom half of the 2%-3% target band for most of the year. This will allow the RBA to cut rates again if growth looks like disappointing the Bank's forecasts. But the economy still remains in-line with official growth expectations and a further fall in the exchange rate should help the external sector contribute to growth this year. We forecast 2.9% economic growth in 2015. So while the market looks for a rate cut we continue to forecast no change this year and the first interest rate increase in Q1 2016.

New Zealand

Paul Brennan

Joshua Williamson

We forecast 2.8% growth in 2015 from a healthy mix of consumption, investment and employment. Dairy price falls to the end of 2014 will drag the terms of trade lower in the first half of the year. However, dairy prices are finally showing signs of stabilising, which could support the terms of trade and rural incomes in the second half of the year. Strong population growth will keep the demand for housing solid and an ongoing concern for the RBNZ. But there is little market based inflation elsewhere. Labour force gains and a pickup in business investment are adding to the supply side of the economy, so there is arguably less capacity pressure than previously feared. These capacity gains and the assistance from falling petrol prices will help keep yearly CPI inflation at the bottom of the RBNZ's 1% to 3% target band on average this year. The RBNZ remains well ahead of inflation in the current cycle. Although we don't forecast another increase in the OCR until December 2015 the risk is that the next interest rate increase is pushed out to the first half of 2016.

Figure 30. Australia and New Zealand — Economic Forecast, 2014-2016F

	Australia			New Zealand		
	2014F	2015F	2016F	2014F	2015F	2016F
Real GDP[a]	2.8	2.9	3.2	3.2	2.8	2.5
Real GDP (4Q versus 4Q)	2.2	2.6	3.5	3.0	2.9	2.3
Real Final Domestic Demand	1.2	1.5	2.4	3.7	2.5	3.0
Private Consumption	2.5	3.0	3.6	3.3	2.6	2.5
Govt. Current & Capital Spending[b]	2.1	2.5	2.4	3.0	2.5	3.1
Housing Investment	7.9	8.1	2.8	15.5	5.0	-7.0
Business Investment[c]	-5.5	-6.7	-2.8	4.0	2.8	1.5
Exports of Goods & Services	6.9	8.3	7.1	1.8	1.0	3.4
Imports of Goods & Services	-0.5	2.9	4.6	7.7	4.8	3.4
CPI	2.5	2.1	3.0	1.2	1.0	1.9
CPI (4Q versus 4Q)	1.7	2.7	2.6	0.8	1.4	2.0
Unemployment	6.3	6.3	6.1	5.3	5.1	4.9
Merch. Trade, BOP (Local Currency, bn)	-1.6	-24.8	-25.1	2.5	0.8	-1.6
Current Account, (Local Currency, bn)	-51.0	-70.4	-78.2	-7.0	-10.7	-10.4
Percent of GDP	-3.2	-4.2	-4.4	-3.0	-4.5	-4.2
Budget Balance[d] (Local Currency, bn)	-49.7	-41.8	-33.6	-3.0	-0.5	0.2
Percent of GDP	-3.1	-2.5	-1.9	-1.3	-0.2	0.1
General Govt. Debt (% of GDP)[e]	32.1	33.5	33.3	35.0	33.6	33.4
Gross Operating Surplus	2.7	3.7	8.5	NA	NA	NA

BOP Balance of payments basis. CPI Consumer Price Index. F Citi forecast. NA Not available. [a]Averaged-based GDP in Australia and New Zealand. [b] In New Zealand excludes capital spending. [c] In New Zealand includes government capital spending. [d] Fiscal year ending June. Australia's underlying cash balance. [e] Australia and New Zealand Budget definition and forecasts. Sources: ABS, StatsNZ, NZIER and Citi Research forecasts

China

Minggao Shen

Shuang Ding

The Chinese economy will probably remain soft in 2015 with an extended investment slowdown. In our view, fixed asset investment growth may gradually normalize towards low teen digits in coming years and to single digits in the medium term, largely due to slower pace of re-leveraging and then de-leveraging in the economy. Chinese leaders have said that the marginal effect of stimulus is diminishing. On the one hand, the government might have lowered its growth target for 2015 to 7%, signaling their intention to tolerate slower growth but avoid major short-term pain. On the other hand, the government may be willing to accept sub-target GDP growth provided the job market remains relatively stable. We continue to forecast the official data will show growth at 6.9% this year, but the underlying growth could improve amid the drop in oil prices.

Various crosscurrents may pull the economy in different directions this year. According to our estimate, the falling oil price often takes two quarters to benefit the economy. Citi expects the average Brent oil price to drop by 37% in 2015; cost savings from which would be equivalent to roughly 4% of the fiscal revenue and boost GDP growth rate by 0.4-0.9ppt. Weak investment in infrastructure and property sectors may continue to weigh on fixed asset investment growth. Consumption growth relies mainly on the mass market and the pace of urbanization. Net exports, a key stabilizer of the economy last year, may remain supportive in 1H but less in 2H due to base effects. Credit defaults are likely scattered again with a focus on the potential risks of local government debt restructuring.

Chinese policy-makers will have to prove they are able to manage the balance between cyclical and structural policies this year. Last year's growth slowdown was partly intended as the authorities tried to avoid stimulating the economy. But we expect 2 more rate cuts in 1H and possibly 3-4 RRR cuts for the whole year to align policy with lowflation and trim the downside risks in the economy. Some monetary easing is likely before the Chinese New Year. Within the two-way bet framework, the RMB may well weaken against the US dollar but strengthen in REER terms. On structural policies, China aims to turn reform measures into growth momentum this year, and fiscal, hukou and SOE reforms announced last year are expected to be implemented with an investment angle.

Figure 31. China — Economic Forecasts, 2014-2016F

					2014		2015				2016	
		2014	2015F	2016F	3Q	4Q	1QF	2QF	3QF	4QF	1QF	2QF
Real GDP	YoY	7.4	6.9	6.7	7.3	7.3	6.7	6.8	7.0	6.9	7.0	6.8
Real Final Domestic Demand	YoY	7.6	6.6	6.7								
Consumption	YoY	7.6	7.1	7.1								
Fixed Capital Formation	YoY	7.5	6.0	6.3								
Industrial Production	YoY	8.3	7.4	7.1	8.0	7.6	7.0	7.2	7.6	7.8	7.6	7.2
Exports	YoY	6.1	6.7	5.2	13.0	8.6	8.0	7.0	6.0	6.0	6.0	5.0
Imports	YoY	0.6	4.0	4.0	1.1	-1.6	4.0	4.0	4.0	4.0	4.0	4.0
Merchandise Trade Balance	$bn	383	460	508	128	150	38	107	146	168	50	118
FX Reserves	$bn	3,840	4,174	4,447	3,888	3,840	3,838	3,910	4,021	4,174	4,174	4,247
Current Account	% of GDP	2.5	2.7	2.5								
Fiscal Balance	% of GDP	-2.1	-2.5	-2.5								
General Govt. Debt*	% of GDP	53.1	54.2	54.9								
Urban Unemployment Rate	%	4.1	4.1	4.3	4.1	4.1	4.2	4.2	4.2	4.2	4.3	4.3
CPI	YoY	2.0	1.5	1.9	2.0	1.5	1.2	1.3	1.5	1.9	2.1	1.9
Exchange Rate (end period)	CNY/$	6.21	6.27	6.11	6.14	6.21	6.23	6.26	6.29	6.27	6.23	6.19
1-Yr Deposit Rate (end period)	%	2.75	2.25	2.25	3.00	2.75	2.50	2.25	2.25	2.25	2.25	2.25

Note: F Citi forecast. E Citi estimate. YoY Year-to-year percent change. SAAR Seasonally adjusted annual rate. * General Govt. Debt includes the debt of central, local government and Ministry of Railway. Sources: Haver Analytics and Citi Research forecasts

India

Rohini Malkani

Anurag Jha

It has been an eventful start for India in 2015, with the government accelerating the pace of reforms and the RBI commencing its rate easing cycle. These developments are consistent with our 2015 Prospects - Surprises in Store, where we expected the process of normalization to continue into 2015. To recap: In 2013, the current account deficit (CAD) came off from 4.7% of GDP to 1.7%; In 2014, CPI inflation fell from double digits to 5% currently; and in 2015 we believe normalization will be evident in interest rates and growth.

There are signs of a rebound in manufacturing activity, as indicated by recent PMI data and industrial output. Furthermore, the government has stepped up the pace of reforms by: (1) introducing a constitutional amendment bill for Goods & Services tax in the winter session of parliament; (2) passing key legislation as ordinances in the area of land acquisition, coal block auctions, insurance, and mining. The ongoing reforms, coupled with continued de-bottlenecking of stalled investments and easier monetary stance, are likely to revive investment demand, prompting us to maintain our GDP estimates of 5.6% in FY15 and 6.5% in FY16.

On the monetary side, the sharp decline in inflation and benign inflation outlook has led the RBI to reduce the Repo rate by 25bps to 7.75% in an inter-policy meeting. As disinflationary pressure continues on account of softer commodity prices and supply-side measures, we expect CPI inflation to come down to 5.5% in FY16 from 6.8% in FY15 i.e. below RBI's glide path target. Consequently, we expect the RBI to reduce the repo rate by an additional 75bps by the end of FY16. We continue to expect 10-year bond yields to soften towards 7.5%.

On the external front, after factoring in new commodity forecasts by our global team, we now expect the FY16 and FY17 CAD at 0.2% and 0.8% of GDP respectively. Our assumptions include (1) Gold imports at 850 tonnes in FY16 and 875 tonnes in FY17 (2) crude price at US$60/bbl in FY16 and US$70/bbl in FY17. To the extent that weaker commodity prices reflect weakness in global demand, we believe exports and capital flows will also moderate, leading to a BoP surplus of US$60-70bn in FY16/17. We expect INR to stabilize close to its fair value range of 62-64.

Lastly on the fiscal side, while near term targets are challenging, fiscal consolidation could continue over a medium term on: (1) structural reforms on taxation, expenditure management (2) lower crude prices and (3) growth revival.

Figure 32. India — Economic Forecasts, FY 2014/15-2016/17F

		FY 14/15F	FY 15/16F	FY 16/17F
Real GDP	YoY	5.6	6.5	7.0
Final Domestic Demand	YoY	4.6	6.7	7.3
Private Consumption	YoY	5.5	7.0	7.0
Fixed Investment	YoY	2.5	6.5	8.5
Exports	YoY	11.0	9.3	9.0
Imports	YoY	9.5	9.0	9.3
Wholesale Price Index	YoY	3.0	2.5	2.5
Consumer Price Index	YoY	6.8	5.5	5.5
Current Account	US$ bn	-24	-5	-20
	% of GDP	-1.2	-0.2	-0.8
Consolidated Fiscal Balance	% of GDP	-6.7	-6.4	-6.1
Centre Fiscal Balance	% of GDP	-4.1	-4.0	-4.0
US Dollar Exchange Rate	Average	63.0	64.1	64.5

Sources: Haver Analytics and Citi Research forecasts

Korea

Jaechul Chang

The MPC decided unanimously to keep the rate stable at the January meeting, unlike our call for 25bps cut and the market's expectation of possible minority views for a rate cut. We expected the January MPC meeting to take an easing stance with downgrades to the growth and inflation outlook, as it did last October. That call was based on our view that the economy would stay weak in 1H15, especially in 1Q, amidst disinflationary pressure and weak economic sentiment, leading annual growth to stay below the potential level (which the OECD estimate at slightly above 3.5%). On the day of the January MPC meeting, the BoK announced its downgrade of 2015 forecasts for growth and inflation to 3.4% and 1.9%, both 0.5%p lower than previous ones. However, it attributed the growth slowdown to unexpectedly low growth in 4Q14 that lowered the recovery path in 2015. The BoK Governor at the press conference also said the economy would expand at a speed of potential growth level of 3.4% in this year. He added it is undesirable to employ monetary easing to manage low inflation due to supply shocks such as the declines of oil price. With the BoK's hawkish views on growth and inflation, particularly with its assumption that potential growth is about 3.4%, we changed our call for the BoK's policy rate from a cut to no change in this year.

Indonesia

Helmi Arman

The pace of subsidy reform has progressed faster than expected, and politics have improved with the opposition being hampered by internal rifts. The plunge in oil prices led the government to cut fuel prices by 10% in early January and 13% in mid-January. YoY inflation will likely fall back to the low 7%s from March; indeed, base effects will kick in at the end of the year, reducing YoY inflation to around 4% by our estimates. However, in the meantime, policymakers will remain cautious on cutting interest rates amid an environment of broad dollar strengthening. As the oil price slide so far has outpaced the slide in non-oil commodities, we expect the current account deficit to narrow but remain above 2% of GDP; ie to $22.6bn (equivalent to 2.6% GDP), from previously $25.4bn. Lower oil prices may cut household expenditure on fuel but the savings may not necessarily be allocated for discretionary spending. Households still have to get used to higher electricity and LPG prices which over the past year has risen in excess of 30%. We maintain our GDP growth forecast for 2015 at 5.1%.

Figure 33. Korea and Indonesia — Economic Forecasts, 2014-2016F

		Korea			Indonesia		
		2014F	2015F	2016F	2014F	2015F	2016F
Real GDP	YoY	3.3	3.4	3.7	5.1	5.1	5.3
Final Domestic Demand	YoY	2.6	3.1	3.8	5.0	4.7	4.9
Private Consumption	YoY	1.9	2.6	3.0	5.3	4.1	4.4
Fixed Investment	YoY	3.8	3.9	5.5	4.9	6.1	6.3
Exports	YoY	3.3	4.7	7.0	-1.3	4.2	4.1
Imports	YoY	2.6	4.2	7.8	-4.0	2.5	2.6
Consumer Price Index	YoY	1.3	1.4	2.4	6.3	6.8	4.6
Unemployment Rate	%	3.5	3.5	3.4	5.9	6.1	6.0
Current Account	US$ bn	93.3	98.1	95.0	-26.7	-22.6	-24.1
	% of GDP	6.6	7.2	6.7	-3.1	-2.6	-2.5
Fiscal Balance	% of GDP	0.9	0.3	0.2	-2.4	-2.0	-1.8
US Dollar Exchange Rate	Average	1053	1127	1140	11866	13042	13067

Source: Haver Analytics and Citi Research forecasts

Hong Kong

Adrienne Lui

The economy will need to ride through impacts of US rate normalization and China's slowdown-easing process in 2015. The consumer slowdown remains our biggest concern, but a pickup in global trade should benefit HK's logistic sector. The latest Policy Address (PA) emphasizes efforts to increase land/housing supply in the mid- to long-term. Citi expects that home prices will rise by 8% YoY in 2015. The upcoming Budget Speech is likely to include increases in government service fees to offset some of the welfare commitments proposed in the PA, and we think only limited alleviation measures will be offered this year. The end of the EUR/CHF peg has led the HKD to test the strong-end of its trading band, but we continue to believe that the HKD peg will remain intact until a one-off shift to peg to the CNY when the CNY is fully convertible. Political anxiety likely to stay elevated in 1H-15.

Singapore

Kit Wei Zheng

The initial data for 4Q GDP growth disappointed (1.5% YoY, 1.6% QoQ SAAR), bringing 2014 GDP growth to 2.8% YoY. Risks to our 2015 forecast (3.0%) are to the downside. We are cutting our 2015 headline inflation forecasts (to 0.1% YoY from 0.6% previously), below MAS's forecast of 0.5-1.5%, with downside risks from oil prices. With lackluster growth against a backdrop of intensifying disinflation, we see a 30-40% chance of an MAS slope reduction in 2015, possibly in April, but would need to see cracks in the labour market to have stronger conviction over MAS easing. MAS may conduct de-facto easing by allowing the NEER to fall below the midpoint of the band. The government may ride on the disinflationary trend to call for early elections in 2H15, possibly implying an expansionary fiscal stance in the Budget on Feb 23rd.

Taiwan

Adrienne Lui

In the near term, exports and manufacturing could moderate on a seasonal slowdown in tech demand, China's drag as well as uncertainties associated with commodity prices. However, we expect a modest export recovery in 2H will keep 2015 GDP growth steady at 3.6% YoY. The net effect of currency depreciation and lower oil prices will keep inflation benign and reduce the import drag on GDP. Investment decisions continue to await tech products launches and a breakthrough in FTA negotiations. Limited cross strait developments is likely after December's 'warm up battle' of KMT-DPP at the Local Elections. Fiscal spending is likely increase in a pre-election year but it will also be hard for the ruling government to pass major policies. We expect the CBC will hold interest rates until 1Q-16, while long-term bond yields may creep up if USD yields rise.

Figure 34. Hong Kong, Singapore and Taiwan — Economic Forecasts, 2014-2016F

		Hong Kong			Singapore			Taiwan		
		2014F	2015F	2016F	2014F	2015F	2016F	2014F	2015F	2016F
Real GDP	YoY	2.3	2.6	3.0	2.8	3.0	3.0	3.6	3.6	3.8
Final Domestic Demand	YoY	1.2	1.7	1.7	0.3	0.9	-0.2	2.6	2.5	1.9
Private Consumption	YoY	1.9	1.7	1.5	1.5	0.5	-0.1	2.6	3.2	3.4
Fixed Investment	YoY	-1.4	2.2	2.7	-1.2	-0.4	-2.3	2.2	1.8	3.2
Exports	YoY	2.3	4.4	5.0	3.3	3.6	3.7	4.7	5.2	5.1
Imports	YoY	2.1	3.9	4.5	2.0	2.4	2.7	4.4	3.5	3.8
CPI	YoY	4.4	4.4	3.9	1.0	0.1	1.4	1.2	1.2	1.8
Unemployment Rate	%	3.3	3.6	3.5	2.0	2.2	2.3	4.0	3.9	3.9
Current Account	US$ bn	1.7	8.5	7.5	54.9	54.3	53.0	60.4	58.0	45.0
	% of GDP	0.6	2.9	2.4	18.0	18.0	17.0	12.0	11.0	8.0
Fiscal Balance	% of GDP	1.3	0.7	1.0	-0.3	0.2	1.5	-1.4	-1.6	-1.3
US Dollar Exchange Rate	Average	7.75	7.77	7.76	1.27	1.36	1.37	30.31	32.09	32.07

Source: Citi Research

Russia

Ivan Tchakarov

Ekaterina Vlasova

We recently cut our 2015 Russian GDP growth forecast to -3.0% from -1.0%, reflecting Citi's new oil price forecasts. Citi's commodity strategists now see Brent averaging $63bbl this year ($80bbl previously) with a $60-65 range in their baseline scenario. If our baseline scenario materializes, 2015 will be the 5th consecutive year of decelerating GDP performance. Plenty of downside risks may weigh on our baseline scenario, including lower-than-forecast oil prices and the increasing likelihood that Russia loses its investment grade status in 2015. More broadly, Russia has been affected by a myriad of structural problems well before the Ukraine crisis and the current sanction-based backdrop will only provide a cyclical overlay to the struggling economy, in our view. One positive risk is the possibility that geopolitical tensions ease as Russia and the West find some common ground in resolving the situation in Ukraine. We foresee private consumption as the main casualty of the deeper recession and forecast that it will contract by 4.0%, marking the first negative growth since 2009. Investment will continue to be hampered by broader uncertainty, while net exports will be the only balm to the sore wound of a recessionary economy. The Central Bank of Russia's transition to a free float in late 2014 will allow the RUB to respond more nimbly to market forces in 2015, thus facilitating the economic adjustment to shocks, but at the cost of heightened currency volatility.

Turkey

Ilker Domac

Gultekin Isiklar

Turkish assets had a good start to the year. Lower oil prices and greater acknowledgment of the likely cyclical decline in annual inflation have played an important role in boosting the performance of the lira and bonds. This backdrop, including the likely improvement in the current account balance thanks to the plunge in oil prices, has raised expectations of monetary policy easing, leading investors to focus on the timing and the magnitude of the possible rate cuts by the CBT. Despite the CBT's surprise 50bp cut in the one-week repo rate at the January MPC meeting, the CBT hinted that it is likely to keep money market rates at elevated levels — well above the one-week repo rate (7.75%). Looking ahead, we believe that a sustained decline in the interbank o/n rate would be a leading indicator for further easing. Provided that the lira continues to perform well, we expect the CBT to bring its average funding rate (currently at 8.4%) to as low as 7.00% in 1H 2015. Depending on the performance of the lira, surprises in both directions cannot be ruled out. Nonetheless, we think that the CBT will be forced to reverse its stance in the second half of 2015, with inflation creeping up and the Fed rate hike cycle beginning in 4Q.

Figure 35. Russia and Turkey — Economic Forecast, 2014-2016F

		Russia			Turkey		
		2014F	2015F	2016F	2014F	2015F	2016F
Real GDP	YoY	0.6	-3.0	1.5	2.9	3.3	3.4
Final Domestic Demand	YoY	-0.5	-3.6	1.1	1.7	3.0	3.2
Private Consumption	YoY	0.5	-4.0	1.0	1.3	3.2	3.5
Fixed Investment	YoY	-3.5	-5.6	2.5	0.9	1.9	2.4
Exports	YoY	0.0	-1.0	1.0	6.2	4.4	4.5
Imports	YoY	-3.0	-5.0	4.6	-0.9	3.5	4.0
CPI	YoY	7.8	12.5	6.8	8.9	5.5	7.0
Unemployment Rate	%	5.7	6.5	6.0	10.0	10.8	10.9
Current Account	US$ bn	60.3	40.3	30.4	-45.2	-33.5	-39.8
	% of GDP	3.2	3.2	2.3	-5.6	-4.3	-4.8
Fiscal Balance	% of GDP	0.0	-2.6	-1.5	-1.3	-1.5	-2.9
US Dollar Exchange Rate	Average	38.6	63.7	66.1	2.19	2.45	2.57

Sources: Haver Analytics and Citi Research forecasts

Hungary

Eszter Gargyan

Incoming data from November suggests that the economy — driven by industrial exports and accelerated EU-fund absorption — has held up well, and GDP growth has likely remained around 3.0% YoY in 4Q14, bringing 2014 annual GDP growth to 3.4% YoY. We expect growth to slow this year and the next as industrial exports are likely to lose momentum following an initial rebound in 1Q15, given that new car producer capacities will be fully utilized and external demand may weaken. The ongoing recovery in household consumption — helped by a reduction in the household FX debt burden — may be muted by the uncertain impacts of Sunday shop closure. Moreover, fixed investment is unlikely to provide another strong stimulus to growth, following record high absorption of EU funds in 2014. The above factors suggest that GDP growth may slow to around 2.5% this year, with downside risks to the outlook. The oil price slump and soft food prices may keep headline CPI in negative territory until 2H15, helping to postpone the beginning of rate hikes. We do not expect rate cuts to resume amidst rising external risk factors, as the NBH remains concerned about HUF volatility due to Hungary's continued high external debt exposure.

Poland

Piotr Kalisz

Cezary Chrapek

Despite the modest drop in the PMI in December, the index was at its second-highest level since March 2014 after the rebound from depressed levels in 2H14. However, monthly indicators on economic activity for November stayed weak, including industrial and construction output as well as retail sales growth. Despite a probable further mild slowdown in GDP growth in 4Q14 and 1Q15, a healthy situation in the labour market, lower fuel prices, a weak zloty and very low interest rates should be enough to keep economic growth well above 3% in 2015 as a whole. The increase in mortgage debt service costs for households after CHF weakening will be fairly insignificant in macro terms and will be more than offset by the decline in the fuel prices. At its last meeting in January, the MPC left interest rates unchanged but the tone of the communique was much more dovish than previously. Given that deflation is likely to be deeper (with CPI likely to fall 1.2-1.5% YoY in Feb/Mar) and will likely extend until the summer, we expect the MPC to cut interest rates further. In our base case scenario, we expect 50bps of rate cuts but most likely in March (at the earliest), as the SNB's decision to free the CHF rate resulted in increased volatility in the FX market and some concerns about financial stability. This will likely stop the Council from faster and more aggressive easing. Moreover, any sign of significant zloty depreciation would limit the scale of rate cuts from the MPC.

Figure 36. Hungary and Poland — Economic Forecasts, 2014-2016F

		Hungary			Poland		
		2014F	2015F	2016F	2014F	2015F	2016F
Real GDP	YoY	3.4	2.5	1.5	3.3	3.4	3.6
Final Domestic Demand	YoY	3.8	2.6	1.0	4.3	3.5	3.9
Private Consumption	YoY	1.6	2.6	2.2	3.0	3.0	3.2
Fixed Investment	YoY	11.0	3.5	-1.0	9.0	6.1	6.0
Exports	YoY	6.6	6.0	6.2	4.3	4.0	6.0
Imports	YoY	7.5	6.4	6.0	6.8	4.8	7.0
CPI	YoY	-0.2	0.0	2.4	0.0	-0.2	2.4
Unemployment Rate	%	7.5	6.8	6.5	11.7	10.8	10.0
Current Account	US$ bn	5.7	5.4	4.3	-6.4	-7.5	-10.7
	% of GDP	4.2	4.7	4.0	-1.2	-1.6	-2.3
Fiscal Balance	% of GDP	-2.6	-2.4	-2.1	-2.9	-2.3	-2.2
Euro Exchange Rate	Average	309	322	320	4.19	4.25	4.13

Source: Citi Research

Czech Republic

Jaromir Sindel

The new data and assumptions suggest a slightly stronger growth outlook. For the first time since August 2014, we are slightly raising our 2015 GDP growth forecast by 0.2%pt to 2.5% YoY. This reflects a better dynamics in late-2014, the improved outlook on foreign demand, weaker koruna and lower oil prices. By contrast, we are cutting our 2015 CPI forecast by 0.6%pt to 0.6%YoY due to lower oil prices. Despite such a low inflation outlook, CNB's Governor and Chief Economist are not calling for a higher EURCZK floor. We think that the impact of ECB QE on the Czech koruna will be worth watching, together with the CNB Board's assessment of how ECB QE could limit external disinflationary pressures in the Czech economy. Wage data for 1H15 also will be important for CNB's Bank Board. If they are weak and hopes for stronger foreign demand prove misplaced, speculation might intensify over a possible hike in the CNB's EURCZK floor. We keep our outlook for a weaker koruna compared to its performance in 2014, though we do not assume a hike in the EURCZK floor. We continue to expect the CNB will exit this floor by 4Q16, with the first hike in policy rate in 1Q17, but we expect a milder increase in the policy rate than before and we see a risk of later exit from the FX intervention mode if the ECB's QE program is prolonged beyond 2016. Light bond issuance, together with the ECB's QE, are likely to be supportive for 10y yields.

Romania

Ilker Domac

Gultekin Isiklar

The NBR started the year with a 25bp rate cut, bringing the policy rate to 2.50%. The Governor's remarks in the aftermath of the January Board Meeting suggests to us that the NBR is probably considering additional easing, thanks in part to lower oil prices. Against this backdrop and with the soft December inflation reading, we believe that a 25bp cut in the February meeting is likely. In this respect, we believe that the new *Inflation Report* (to be discussed on February 4, 2015) will shed more light on the nature and the magnitude of the possible easing for the remainder of the year. Turning to the growth outlook, the revised data of 2.9% YoY for the first nine months of 2014 points to a moderately higher GDP growth than what was announced previously (2.8% YoY). In particular, the final 3Q data, along with other indicators, suggest to us that private consumption and — to a lesser extent — investment seem to be gaining some traction. Against this backdrop, we look for a moderate pick-up in economic activity this year with GDP growth reaching 3.0% from an estimated 2.8% in 2014.

Figure 37. Czech Republic and Romania — Economic Forecasts, 2014-2016F

		Czech Republic			Romania		
		2014F	2015F	2016F	2014F	2015F	2016F
Real GDP	YoY	2.3	2.5	3.1	2.8	3.0	3.0
Final Domestic Demand	YoY	2.0	2.6	3.7	2.4	3.4	3.0
Private Consumption	YoY	1.6	2.3	2.5	5.0	3.5	3.5
Fixed Investment	YoY	3.3	4.9	7.6	-6.0	4.0	1.7
Exports	YoY	7.5	5.6	8.6	7.1	4.0	4.6
Imports	YoY	8.4	5.9	10.1	5.8	4.1	4.0
CPI	YoY	0.4	0.6	2.2	1.1	1.5	2.6
Unemployment Rate	%	6.1	5.6	5.3	5.5	5.5	5.5
Current Account	US$ bn	0.0	0.4	-1.6	-1.0	-3.1	-3.6
	% of GDP	0.0	0.2	-0.8	-0.5	-1.8	-2.2
Fiscal Balance	% of GDP	-1.9	-2.3	-2.0	-2.0	-1.9	-2.1
EURCZK, USDRON	Average	27.5	28.0	27.4	3.3	4.1	4.5

Sources: Haver Analytics and Citi Research forecasts

Brazil

Marcelo Kfoury

Dilma Roussef started her second term with a turnaround in the conduct of fiscal policy. The appointment of a recognized fan of pro-austerity MoF, Joaquim Levy, was the first sign of this reversal. The announcement has been followed by several fiscal measures since the end of last year, including public spending cuts and tax hikes, making us feel more comfortable with our 1% and 2% of GDP primary fiscal surplus forecasts for this year and next, respectively — from an equilibrium in 2014. Part of the fiscal tightening will likely have unfavorable side effects on inflation, especially for monitored prices (energy, public transportation). Thus, we expect 2015 (yearend) CPI inflation to stand at 6.8%, surpassing the 6.5% upper bound of the central bank's target band for the first time since 2003. Given this challenging scenario in terms of inflation, we expect the central bank will hike the Selic rate to 12.5% by 2015 yearend. The tighter fiscal and monetary policy mix probably will lead to the second year in a row of roughly nil GDP growth. On the FX front, lower liquidity and commodity prices point to a weaker BRL ahead. Finally, we continue to envisage a slight improvement in the current account (and also in the trade balance) this year, after a deficit of roughly 4% of GDP in 2014.

Mexico

Sergio Luna Martinez

Recent data points to a continued recovery in economic activity in 4Q14, as we had anticipated. Nevertheless, we have noticed new elements of uncertainty regarding 2015 global outlook, with the oil price slump being the most important. Although Mexico is being a net exporter of oil, we only expect a modest negative impact. The fiscal effects will be limited due to the government's hedging strategy. Also relevant is the arbitrage between international and local gasoline prices and an indirect economic hedge arising from better US growth prospects and higher USDMXN levels — inversely related to oil prices. Moreover, we estimate that Mexico's Oil Stabilization Fund may cover foregone revenues. On the activity front, we expect the improved US growth outlook to have spillover effects on Mexico via higher exports, offsetting lower investment business confidence. All in all, we maintain our 2014 and 2015 GDP growth forecast at 2.2% and 3.4%, respectively. Meanwhile, 2014 yearend annual inflation stood at 4.1%. We maintain our 2015 yearend inflation forecast at 3.3% YoY. An environment of lower inflation and a closing output gap - albeit still in negative territory — may provide room for Banxico to hike rates shortly before the Fed. This view is supported by the recent statement by Governor Carstens about the high probability of observing higher interest rate this year.

Figure 38. Brazil and Mexico — Economic Forecasts, 2014-2016F

		Brazil			Mexico		
		2014F	2015F	2016F	2014F	2015F	2016F
Real GDP	YoY	0.0	0.1	1.6	2.2	3.4	4.4
Final Domestic Demand	YoY	-0.4	-0.1	1.7	2.1	3.8	4.8
Private Consumption	YoY	0.8	0.5	1.7	2.0	3.5	4.3
Fixed Investment	YoY	-7.2	-1.2	3.9	2.4	6.0	7.7
Exports	YoY	2.7	1.8	1.5	6.4	6.8	9.9
Imports	YoY	-0.1	0.1	2.4	4.7	7.3	8.9
CPI	YoY	6.3	6.7	6.0	4.0	3.6	3.6
Unemployment Rate	%	4.9	5.3	5.8	4.9	4.6	4.4
Current Account	US$ bn	-87.2	-75.5	-76.8	-28.3	-28.3	-36.8
	% of GDP	-4.0	-3.8	-3.7	-2.2	-2.2	-2.6
Fiscal Balance	% of GDP	-6.1	-5.3	-4.5	-3.6	-3.5	-3.5
US Dollar Exchange Rate	Average	2.35	2.85	2.97	13.31	14.38	13.93

Source: Citi Research

Argentina

Guillermo Mondino

We believe current macroeconomic conditions are fragile. The steady deterioration in fiscal accounts and the monetary financing of the deficit can only be partially neutralized through increased “sterilization” via the issuance of short-term debt by the central bank. However, because 2015 is an electoral year, the authorities are likely to refrain from “sterilizing” heavily, in order to boost private credit growth. As a result, pressure on the FX market should reemerge. Nevertheless, the government is determined to maintain a very slow pace of crawl in the official FX rate and tight capital controls. The inconsistency between the FX policy and money printing is bound to increase pressure on international reserves. The modest current depreciation and low level of economic activity should keep inflation from accelerating, though it will eventually rebound later. We expect consumer prices to rise by roughly 37% this year. The inconsistency in the macroeconomic program also leads us to foresee a higher movement in the official USDARS during 2H15 to 12 by the end of 2015. We expect GDP will shrink by about 2.5% this year.

Venezuela

Munir Jalil – [pubs fix color, please]

Over the past month, the government released data on economic activity for the first three quarters of 2014, showing an annual drop of 4%. At the same time, official inflation has reached 63.6% as of November. That being said, the steep reduction in oil prices is creating an even more challenging scenario for the government. In particular, we calculate that with an average price for the Venezuelan basket of oil of USD50, the financial needs in excess of what is entering the country as exports are USD32.1 billion. This suggests that the government will face difficulties for the financing of imports and debt payments. As a consequence of this severe cash-flow problem, scarcity of goods has intensified over the past few weeks, translating into people having to wait on long lines to buy groceries and basic goods. The longer this situation persists, the higher the probability of demonstrations. On the FX front, the government announced in mid-December that a new FX system will be put in place, but the details remain unknown. We believe that as part of the FX announcements, the government will go back to a two tier system where the CENCOEX rate (currently at USDVEF6.3) will be increased to USDVEF12 and the SICAD I and SICAD II markets will be unified around an exchange rate that should be between USDVEF35-52.

Figure 39. Argentina and Venezuela — Economic Forecasts, 2014-2016F

		Argentina			Venezuela		
		2014F	2015F	2016F	2014F	2015F	2016F
Real GDP	YoY	0.0	-1.0	1.0	-4.0	-4.4	1.9
Final Domestic Demand	YoY	-1.0	-1.2	0.9	-4.7	-3.6	0.6
Private Consumption	YoY	-1.1	-0.7	1.4	-5.0	-4.0	0.2
Fixed Investment	YoY	-3.1	-5.7	-1.2	-6.0	-5.0	0.4
Exports	YoY	-5.7	-2.5	-0.2	-1.0	-1.0	4.6
Imports	YoY	-6.2	-3.4	-0.6	-5.0	-1.0	-1.0
CPI	YoY	-	18.3	32.9	61.3	70.3	80.0
Unemployment Rate	%	8.6	8.9	9.5	7.0	8.0	8.5
Current Account	US$ bn	-5.1	-6.6	-5.9	14.9	6.9	12.4
	% of GDP	-1.0	-1.4	-1.2	4.4	2.4	4.2
Fiscal Balance	% of GDP	-3.7	-4.7	-3.7	-12.3	-12.9	-12.7
US Dollar Exchange Rate	Average	8.09	9.83	14.07	6.29	12.00	21.36

Sources: Haver Analytics and Citi Research forecasts

Saudi Arabia

Farouk Soussa

As our oil price forecast for 2015 was cut to US$63 per barrel in January, from US$80 previously, we have updated our forecasts for all GCC countries accordingly (see GCC Macro View — GCC oil exporters: updated macro forecasts, 13 January). We now expect total Saudi government revenues to fall by some 33% in 2015, which we think will inevitably lead to sharper expenditure cuts and a wider deficit than we had previously been projecting. Although the Kingdom announced a budget of SAR860bn, up from the SAR855bn in spending budgeted for 2014, in reality we expect spending to fall sharply. Actual spending in 2014 overshot the budget by almost SAR250bn, at SAR1.1tr, and we believe that the overshoot this year which will be much smaller, in the order of SAR900bn. This represents an 18% decline in spending, most of which will come from capital expenditure. As a result, economic growth will suffer, and we have penciled in a contraction of the non-oil economy of 5% YoY this year, with the overall economy shrinking by 3.3% (oil production is expected to remain flat). This is the first time Saudi Arabia will post negative growth since 1999, according to our data.

In response to the lower oil price environment, we expect Saudi Arabia will pursue a combination of fiscal consolidation and economic reform on the one hand, while smoothing consumption to a great extent using its exceptional fiscal space. The kingdom has close to US$500bn in sovereign reserves, which will allow it to finance expected deficits and drive forward modest growth in the medium term. It also has virtually no public debt.

United Arab Emirates

Farouk Soussa

The UAE is also vulnerable to the drop in oil prices, but less so than regional peers. In Abu Dhabi, we expect government expenditure to continue growing at between 2%-4% YoY, thanks to a lower breakeven oil price for the budget and a high level of investment income that we think will keep public finances in positive territory during our forecast period. That said, growth will fall as the rate of expenditure growth Declines. In Dubai, we have cut our growth expectations as regional liquidity and economic activity declines, providing headwinds to Dubai's model as a hub for the region. A potential deal between the P5+1 and Iran provides some upside risk, but we also see downside risks emanating mainly from the property sector.

Figure 40. Saudi Arabia and United Arab Emirates — Economic Forecasts, 2014-2016F

		Saudi Arabia			United Arab Emirates		
		2014F	2015F	2016F	2014F	2015F	2016F
Real GDP	YoY	3.4	-3.3	1.7	4.0	4.0	4.4
Final Domestic Demand	YoY	8.0	8.1	8.1	4.7	4.7	4.8
Private Consumption	YoY	5.0	5.0	5.0	5.0	5.0	5.0
Fixed Investment	YoY	10.0	10.0	10.0	5.0	5.0	5.0
Exports	YoY	-6.7	-31.1	9.6	13.0	14.0	14.0
Imports	YoY	10.0	-5.0	5.0	15.0	15.0	15.0
CPI	YoY	2.9	3.0	3.4	2.0	2.4	2.9
Current Account	US$ bn	90.0	-12.5	1.5	37.2	15.1	15.4
	% of GDP	12.1	-2.0	0.2	8.6	3.3	3.1
Fiscal Balance	% of GDP	-1.8	-8.9	-6.2	NA	NA	NA
US Dollar Exchange Rate	Average	3.75	3.75	3.75	3.67	3.67	3.67

Source: Citi Research

Egypt

David Cowan

We now expect parliamentary elections to be completed by the end of April, finalizing President Abdelfattah el Sisi's political roadmap. And with the holding of a major investment conference in March, the focus for the rest of the year will be on pushing ahead with policies to drive an economic recovery. But the recovery could be constrained by weaker private consumption as private remittances from the Gulf come under pressure, although official Gulf support — which has allowed the CBE to stabilise the exchange rate and slowly clear foreign exchange shortages — will continue for political reasons. Instead, the challenge for the government will be to get new engines of growth moving ahead, notably a recovery in tourism and a pick-up in agricultural and investment. With the fiscal deficit remaining wide, we expect inflationary pressures to remain robust in 1H 2015 with an easing of inflation in 2H depending on the implementation of the proposed VAT and whether further cuts in fuel subsidies are implemented despite the sharp fall in the global oil price. Given ongoing official transfers from the Gulf, we expect only a cautious and gradual weakening of EGP, at least in part in response to a stronger USD.

South Africa

David Cowan

The sharp fall in the global oil price in recent months has given the South African economy a bit more breathing space than seemed the case in late 2014 when it seems to be flirting with stagflation. But the ongoing difficulty of resolving the electricity supply constraint and weak consumer confidence still means that we expect only a slow rebound in real GDP growth in 2015, even if inflation does seem set to follow a downward trend during the year. This should give the SARB more policy flexibility to normalize monetary policy by leaving the Repo rate unchanged. And while the lower oil price will also help reduce the current account deficit, the main concern to this overall outlook would still be a sharp fall in the ZAR. At present we expect the ZAR to remain under pressure, at least in part due to USD strength. But we do not expect that FX will be great enough to force a change in the monetary policy stance in 2015 unless there was perhaps a surprise rate hike in the US. Indeed, gradual rand depreciation should eventually help to drive a slow rebalancing of the economy towards more export-driven growth. As with monetary policy, the scope for a major change in fiscal policy is also limited without a quicker economic recovery. Although the recent Medium-Term Budget Statement did not change the proposed path of fiscal consolidation and put off any tax announcements until the February budget, we think the government will have little choice but to raise the current 14% VAT rate over the next 18 months even if this negatively impacts on the slow recovery.

Figure 41. Egypt, Nigeria and South Africa — Economic Forecast, 2014-2016F

		Egypt			Nigeria			South Africa		
		2014F	2015F	2016F	2014F	2015F	2016F	2014F	2015F	2016F
Real GDP	YoY	3.2	3.4	4.3	6.2	4.5	6.2	1.6	2.4	2.8
Final Domestic Demand	YoY	4.5	3.6	4.6	NA	NA	NA	0.9	1.4	2.5
Private Consumption	YoY	3.9	2.8	2.1	NA	NA	NA	1.0	1.4	2.2
Fixed Investment	YoY	1.6	9.9	19.4	NA	NA	NA	-0.2	1.0	5.4
Exports	YoY	-2.8	5.6	6.0	NA	NA	NA	1.3	1.9	5.9
Imports	YoY	4.8	7.2	6.7	NA	NA	NA	-1.5	-1.2	7.1
CPI	YoY	10.1	8.9	8.7	8.1	11.0	8.8	6.1	5.1	5.0
Unemployment Rate	%	14.2	14.5	13.5	NA	NA	NA	25.0	24.6	24.2
Current Account	US$ bn	-5.5	-6.9	-9.9	7.4	-12.9	-3.4	-17.8	-15.0	-15.1
	% of GDP	-2.0	-2.3	-3.0	1.3	-2.5	-0.6	-5.3	-4.4	-4.1
Fiscal Balance	% of GDP	-11.7	-10.6	-10.4	-2.0	-2.7	-2.3	-4.1	-4.1	-3.5
US Dollar Exchange Rate	Average	7.08	7.29	7.46	164.9	206.67	215.25	10.85	11.94	12.23

Source: Citi Research

Sovereign Ratings

Michael Saunders

Peter Goves

The *Sovereign Ratings Outlook* is a joint product between the Citi economics and rate strategy teams, with input from various other research teams. We aim to forecast the direction and scale of sovereign debt ratings (local currency), as well as any changes in the ratings outlook, for a range of countries. These are our judgments over the ratings outlook, rather than model-determined recommendations. All economic and fiscal forecasts are consistent with those published in Citi's monthly "*Global Economic Outlook and Strategy*" or other research. We do not aim to make a judgment on the financial market implications of ratings changes, except in so far as we expect any such market implications to affect other sovereign ratings.

Given economic updates in this publication and based on rating agency criteria, we highlight our economists' and strategists' main expectations for sovereign ratings over the near (2-3 quarters) and longer (2-4 years) term.

Figure 42. Advanced Economies — Sovereign Long-Term Debt Ratings and Citi Ratings Forecasts

	S&P Ratings				Moody's Ratings			
Country	Current Rating	Current Outlook	Citi Near Term (Up to 9 Mths) Forecast Rating	Citi Long Term (Next 2-4 Years) Forecast Rating & Outlook	Current Rating	Current Outlook	Citi Near Term (Up to 9 Mths) Forecast Rating	Citi Long Term (Next 2-4 Years) Forecast Rating & Outlook
US	AA+	Stable	AA+ (Stable)	AA+	Aaa	Stable	Aaa (Stable	Aaa
Canada	AAA	Stable	AAA (Stable)	AAA	Aaa	Stable	Aaa (Stable)	Aaa
Japan	AA-	Neg	AA- (Neg)	A+ ↓	A1	Stable	A1 (Stable)	A1
Germany	AAA	Stable	AAA (Stable)	AAA	Aaa	Stable	Aaa (Stable)	Aaa
France	AA	Neg	AA (Neg)	AA	Aa1	Neg	Aa1 (Neg)	Aa1
Italy	BBB-	Stable	BBB- (Stable)	BBB-	Baa2	Stable	Baa2 (Stable)	Baa2
Spain	BBB	Stable	BBB (Stable)	BBB	Baa2	Pos	Baa1 (Stable) ↑	Baa1 ↑
Austria	AA+	Stable	AA+ (Stable)	AA+	Aaa	Stable	Aaa (Stable	Aaa
Belgium	AA	Stable	AA (Stable)	AA	Aa3	Stable	Aa3 (Stable)	Aa3
Greece	B	Stable	B- (Stable)	B	Caa1	Stable	Caa1 (Stable)	Caa1
Ireland	A	Stable	A (Stable)	A+ ↑	Baa1	Stable	Baa1 (Pos)	A2 ↑↑
Netherlands	AA+	Stable	AA+ (Stable)	AA+	Aaa	Stable	Aaa (Stable)	Aaa
Portugal	BB	Stable	BB (Pos)	BB+ ↑	Ba1	Stable	Ba1 (Stable)	Baa3 ↑
UK	AAA	Stable	AAA (Stable)	AAA	Aa1	Stable	Aa1 (Stable)	Aa1
Switzerland	AAA	Stable	AAA (Stable)	AAA	Aaa	Stable	Aaa (Stable)	Aaa
Sweden	AAA	Stable	AAA (Stable)	AAA	Aaa	Stable	Aaa (Stable)	Aaa
Denmark	AAA	Stable	AAA (Stable)	AAA	Aaa	Stable	Aaa (Stable)	Aaa
Norway	AAA	Stable	AAA (Stable)	AAA	Aaa	Stable	Aaa (Stable)	Aaa
EU	AA+	Stable	AA+ (Stable)	AA+	Aaa	Stable	Aaa (Stable	Aaa
ESM	Not rated				Aa1	Stable	Aa1 (Stable)	Aa1

Note: Arrows denote expected ratings changes from the current rating. (Neg) denotes negative outlook. (Neg W) denotes negative watch. SD means Selective Default. (P) means Provisional. The number of arrows denotes the expected change in ratings notches from the current level. We show a maximum of five arrows even for countries where we expect more than five notches of ratings change. NA Not available. Sources: Moody's, S&P and Citi Research

Expected Ratings Issues

Michael Saunders

Peter Goves

For our full aggregated calendars please see our *Euro Rates Strategy - Moody's and S&P Sovereign Credit Ratings Calendars for 2015*

Fewer rating transitions expected this year: One key theme pertinent to the 2015 outlook for sovereign credit quality is the ongoing stabilization of EMU ratings. This was already apparent in 2013, as there were no rating upgrades/downgrades by Moody's of 2012 ratings. Indeed in 2014, there were several upgrades, not least the restoration of investment grade status for Ireland (which is now rated Baa1/A-). In addition, we also expect fewer rating transitions. Quite simply, and unlike 2013 and before, 2014 saw the vast majority of ratings outlooks being restored from "negative" to "stable". Out of all 19 EMU sovereigns, 17 have stable outlooks, 1 has a negative outlook (France) and 1 has a positive outlook (Spain).

Figure 43. Upcoming Rating Calendar

Date	Agency	Sovereign
23 Jan 15	Moody's	France
23 Jan 15	Moody's	United Kingdom
23 Jan 15	S&P	Belgium
30 Jan 15	Moody's	EFSF
30 Jan 15	Moody's	ESM
06 Feb 15	Moody's	Finland
13 Feb 15	Moody's	Italy

Sources: Citi Research, Moody's and Bloomberg

We expect Spain to be rated higher than Italy by Moody's too

One of our key strategic themes remains Spain's economic and market outperformance relative to other periphery sovereigns (*Why Spain Is Likely to Decouple Further From the Periphery*). Due to higher growth prospects (2.2% in 2015, Italy 0.4% in 2015), successful reform implementation, falling unit labour costs and debt ratio stabilization we expect Spain to be rated higher than Italy in 2015 by Moody's. Indeed Spain is now already rated higher than Italy by S&P which downgraded Italy from BBB to BBB- on 5 December (*S&P upgrades Ireland, downgrades Italy – market implications*). For 2015, note that Moody's rates Spain Baa2 with a positive outlook and we expect an upgrade sometime next year – possibly on 20 February when it next features on Moody's calendar.

We expect France to remain AA/Aa1 despite the negative outlook(s)

France next features on Moody's calendar this week on 23 January and the prospect of another downgrade will continue to linger in 2015 – note France is rated with a negative outlook by both Moody's (since November 2012) and S&P (since October 2014, *S&P revises France's AA outlook to negative*). Implementation risks of the reform agenda clearly remain and the decision to delay the 3% deficit target (again) to 2017 is credit negative in our view. However, provided the commitment to engage with structural reform and boost potential GDP remains strong and ongoing, we believe this is likely to be looked on favourably by the rating agencies. Our base case is for France to remain AA/Aa1 over the medium term but for both Moody's and S&P to leave France on negative outlook.

We no longer expect an upgrade of the UK

The UK is on Moody's calendar on 23 January and we had previously penciled in a restoration of the UK's Aaa status by Moody's given the strong growth rebound and prospect for the debt/GDP ratio to stabilize. However, fiscal performance has been disappointing, due to undershoots in tax receipts despite falling unemployment. Combined with prospects of rising political uncertainty and the escalating *Brexit debate,* we no longer expect an upgrade in 2015. We see the UK remaining Aa1.

Ireland now stable but upgrade pressure to build over the longer term

Ireland was upgraded by S&P from A- to A on the 5 December (*S&P upgrades Ireland, downgrades Italy – market implications*). It is now rated stable by both Moody's (Baa1) and S&P (A). Given this and the various upgrades the sovereign has enjoyed, we expect no further upgrades over the next 12 months. However, we do not rule out upgrades over the longer term should positive fundamental momentum be sustained over 2015.

Yield and Spread Forecast Commentary

Amitabh Arora

US: We expect the US rates curve to flatten in excess of forwards, with the long end outperforming in an environment of low inflation risk premium and lower term premiums. The front end of the curve is expected to sell off in excess of forwards. The selloff is likely to be tempered by expectations of a more gradual pace of hikes.

Alessandro Tentori

Core Europe: We continue to see a very mild rise in Bund yields for 2015 (0.65% by Dec 15), reflecting both the negligible risk of a spike in inflation as well as the weak potential growth environment. Other factors such as demographics, productivity trends, real interest rates and political risks will likely contribute to our medium-term scenario ("low-for-longer"), despite a short-term expectation of a post-QE sell off in core EGBs. The curve will retain most of its directional bias after the small liquidity cliff due to expiring LTROs. We do expect the front-end to look through that particular Q1 episode and Eonias and Schaetze are likely to reflect the liquidity boost from QE going into the second half of the year. In general, we expect core paper to benefit from ECB's purchases, while the exact re-pricing of QE premia and the curve dynamics will depend in large part from the details of the program. Also, differences in the floating amounts (rather than outstanding amounts) will matter for the performance of smaller core issuers vs France.

Peter Goves

EMU Periphery: ECB QE remains our central driver of periphery markets in 2015. We expect further tightening of the periphery in Q1 given Citi's base case for an ECB announcement on sovereign bond buying. Looking further ahead, Spain has a general election in December which we think could cause some softness in Q3. There are also regional Spanish elections and a separate election in Catalonia (September). Fundamentally, we maintain that relative prospects are likely to keep Spain trading at a tighter 10yr spread to Germany than Italy (targeting 90bp in Bono-Bunds and 110bp in BTP-Bunds in Q1). There are also prospects for ongoing political uncertainty in Greece and we remain cautious until a government is formed after the election on 25th January and until Troika negotiations are resolved.

Jamie Searle

UK: Gilt yields continue to trend lower, driven by falling inflation, risk aversion, offside positioning and growing expectations of ECB QE. We expect the low-yield environment to be sustained for the first half of the year as the global yield-grab environment dominates other drivers. However, domestic policy is likely to reassert itself in the second half of the year. We have postponed our forecast for the first UK rate hike from Nov-15 to Q1-16 (vs market expectations of summer 2016) and front-end gilt yields are likely to rise quite sharply if this gets priced-in, flattening the gilt curve.

Takeki Fukushima

Japan: We remain bullish on JGBs for the near term, due to a lack of sellers. Domestic investors are likely to keep unrealized profits until the next fiscal year (starting in April) so that the BoJ's purchases will keep squeezing the market. In addition, the market is likely to price in additional easing by the BoJ if equities lose the gains since QQE2 was announced last October. The short- to middle-maturity sector is also likely to remain attractive to be swapped into USD compared to declining UST yields. We see larger risk of spike in volatility (especially in the super-long sector) around the fiscal yearend, but, may still be too far away to price in.

Figure 44. Interest Rate and Bond Market Forecasts as of 21 January 2015

		Quarterly Average (Unless Specified)					
	Current	1Q 15F	2Q 15F	3Q 15F	4Q 15F	1Q 16F	2Q 16F
US							
Policy Rate (Fed Funds) End Quarter	0.25	0.25	0.25	0.25	0.50	0.50	0.75
3-Month Libor	0.23	0.25	0.25	0.30	0.40	0.55	0.80
2 Year Treasury Yield	0.46	0.55	0.85	1.20	1.55	1.80	1.95
5 Year Treasury Yield	1.26	1.45	1.70	1.95	2.20	2.35	2.40
10 Year Treasury Yield	1.81	1.95	2.20	2.35	2.55	2.65	2.65
30 Year Treasury Yield	2.43	2.45	2.55	2.70	2.85	2.90	2.90
2-10 Year Treasury Curve, bp	135	140	135	115	100	85	70
2 Year Swap Spread (Swap Less Govt), bp	24	25	26	29	30	30	30
10 Year Swap Spread (Swap Less Govt), bp	12	14	16	19	20	20	20
30 Year Swap Spread (Swap Less Govt), bp	-8	-7	-5	-3	-2	-2	-2
30 Year Mortgage Yield	3.66	3.90	4.25	4.45	4.70	4.85	4.90
10 Year Breakeven Inflation, bp	161	173	187.5	195	202.5	205	205
Euro Area							
Policy Rate End Quarter	0.05	0.05	0.05	0.05	0.05	0.05	0.05
Overnight Rate (EONIA)	-0.08	0.00	-0.10	-0.15	-0.15	-0.15	-0.15
3-Month (EURIBOR)	0.03	0.00	0.00	0.00	0.00	0.00	0.00
2 Year Schatz Yield	-0.15	-0.05	-0.10	-0.15	-0.15	-0.15	-0.15
5 Year Bobl Yield	-0.04	0.00	0.00	0.05	0.10	0.10	0.10
10 Year Bund Yield	0.48	0.55	0.55	0.65	0.65	0.75	0.75
30 Year Bund Yield	1.16	1.25	1.25	1.40	1.40	1.50	1.50
2-10 Year Bund Curve, bp	63	60	65	80	80	90	90
10 Year BTP-Bund Spread, bp	120	110	110	110	110	110	110
10 Year Bono-Bund Spread, bp	105	90	90	100	100	90	90
2 Year BTP-Schatz Spread, bp	55	20	20	20	20	20	20
2 Year Bono Schatz Spread, bp	49	20	20	20	20	20	20
10 Year OAT-Bund Spread, bp	20	20	20	20	20	20	20
10 Year Swap Spread (Swap Less Govt.), bp	27	30	25	30	25	20	20
10 Year Breakeven Inflation, bp	77	100	105	115	120	130	130
5y5y Implied Vol, bp	64	63	63	65	65	67	67
Japan							
Policy Rate End Quarter	0.10	0.10	0.10	0.10	0.10	0.10	0.10
3-Month Libor	0.10	0.10	0.10	0.10	0.10	0.10	0.10
2 Year Treasury Yield	-0.03	0.00	0.00	0.05	0.10	0.10	0.10
5 Year Treasury Yield	0.01	0.05	0.10	0.10	0.15	0.20	0.20
10 Year Treasury Yield	0.24	0.25	0.35	0.40	0.45	0.50	0.50
30 Year Treasury Yield	1.11	1.20	1.30	1.40	1.45	1.50	1.50
2-10 Year Treasury Curve, bp	27	25	35	35	35	40	40
2 Year Swap Spread (Swap Less Govt.), bp	14	17	14	13	13	12	12
10 Year Swap Spread (Swap Less Govt.), bp	20	20	17	15	16	17	17
10 Year Breakeven Inflation, bp	73	70	70	75	90	95	95
UK							
Policy Rate End Quarter	0.50	0.50	0.50	0.50	0.50	0.75	1.00
3-Month Libor	0.56	0.55	0.55	0.55	0.55	1.00	1.25
2 Year Treasury Yield	0.40	0.50	0.80	1.15	1.35	1.55	1.85
5 Year Treasury Yield	1.07	1.10	1.40	1.65	1.75	1.90	2.10
10 Year Treasury Yield	1.54	1.65	1.80	2.15	2.25	2.40	2.60
30 Year Treasury Yield	2.20	2.35	2.45	2.75	2.85	2.95	3.15
2-10 Year Treasury Curve, bp	114	115	100	100	90	85	75
10 Year Swap Spread (Swap Less Govt.), bp	6	8	10	15	18	20	20
10 Year Breakeven Inflation, bp	258	245	255	285	290	300	310
Australia							
Policy Rate End Quarter	2.50	2.50	2.50	2.50	2.50	2.75	3.00
3-Month Libor	2.74	2.70	2.70	2.80	2.90	3.20	3.40
2 Year Treasury Yield	2.17	2.25	2.15	2.45	2.60	2.90	3.35
5 Year Treasury Yield	2.24	2.15	2.17	2.29	2.49	2.90	3.24
10 Year Treasury Yield	2.59	2.60	2.67	2.84	2.94	3.15	3.39
2-10 Year Treasury Curve, bp	42	35	52	39	34	25	4
10 Year Swap Spread (Swap Less Govt.), bp	37	40	40	45	45	50	60

Source: Citi Research

Commodities Market Outlook

Edward L Morse

Aakash Doshi

The commodity outlook for 2015 begins where it ended 2014: under pressure despite a conscious uncoupling and evolving market correlations as major changes to supply, demand, geopolitical risk, inflation and currency movements are enhancing price volatility and shifting expectations for most commodities including crude oil, grains, gold and copper. The post-commodity super cycle dynamic challenges the broader market perception of the past decade that commodities generally behave in a uniform manner. Instead what are unfolding are major divergences among individual commodities (e.g .iron ore and copper) and between commodities and other asset classes (e.g. gold and USD). Citi's price outlook expects heightened seasonality and the possibility of v-shaped price recoveries and sell-offs for the various sectors, with investor and corporate attention particularly centered around the energy complex.

Energy

After December's 19% decline, oil prices fell another 15% YTD, and are finding some support at $50/bbl; yet market sentiment remains overwhelmingly bearish. $50/bbl oil is unsustainable in our view; corporate capital expenditures are being slashed, petrostate government revenues nearly halved and almost 50% of future upstream projects are facing questionable economics. The question is not "if" but "when" markets will balance, and Citi's base case expectation is that this occurs in 2H'15, with a rebound in store for winter 2015-16 or early 2016

But for now, the market is locked in a race between running out of crude storage space and a meaningful supply response, and it looks like it could go to the wire. Given the inability of supply and demand to respond in the very near-term, the market remains oversupplied to the tune of ~1-m b/d, and with Russia, Iraq and the FSU increasing crude exports, this is leaving an overhang of West African crude in the market, with 30-m bbls of Nigerian crude still unsold in its February loading program. The contango in the Brent curve is starting to incentivize barrels onto more expensive "floating storage", with 50-60-m bbls of the tanker fleet already having been potentially lined up. This means that further price downside should materialize if more barrels end up on VLCCs (oil tankers that carry around 2-m bbls of crude). Meanwhile the supply response is already in motion.

US rig counts, particularly in the Bakken, are falling, maintenance capex is being cut which should raise declines rates on existing fields globally, and the 700-900k b/d of crude produced by US "stripper wells" could see shut-ins by year-end. 3Q'15 is when the material changes are expected to become tangible both on the supply and demand side, yet macro weakness remains a risk to the downside, which could challenge Citi's outlook for 1.2-m b/d of expected annual oil demand growth. Brent prices could return to the $60-70/bbl range by year-end or into early 2016 – with further weakness in the interim. Meanwhile, limited storage space in the Atlantic Basin is creating incentives to move crude oil barrels into the US; with the Brent futures curve in steep contango, but WTI in modest contango, front month Brent-WTI price spreads are almost at parity. Indeed, WTI traded briefly above Brent recently. Thus, despite ample inventory levels in the US – whether one looks at the US Gulf Coast, or in Cushing, Oklahoma - the narrow Brent-WTI differential is keeping US crude imports high, and limiting crude exports, reflecting the need for distressed Atlantic Basin barrels to be pushed into US on-land storage, where there is more capacity than in tankage-constrained Europe and West Africa. But as US on-land storage fills up too, WTI could move into steeper contango, pressuring front month prices down further below Brent. Whatever happens, oil prices are in for a bumpy ride in 2015.

The world has also become awash in natural gas. In North America, strong production growth is keeping the market oversupplied so that prices remain depressed this winter. With production growth showing no signs of slowing down, gas inventory levels before the start of the 2015-16 and 2016-17 winters are projected to set all-time highs, likely exceeding practical storage limits. This expectation should put pressure on prices to drive up natural gas demand for power generation in an effort to work off the excess gas. Despite low oil and gas prices, cuts in producer capex do not appear enough to sizably slow gas production growth. Low oil prices and over-supply are also driving prices in European and Asian LNG lower. UK's NBP prices could test or even fall below last year's lows this coming summer, as current forwards are already indicating prices in the mid-$6/MMBtu range. However, gas prices are still not sufficiently low to induce more or even a stabilization of demand: prices might have to fall by another third to make gas adequately competitive with coal in power generation. In Asia, LNG prices at just above $9/MMBtu are a far cry from the ~$20 range seen in the last two winters. Despite the current price fall due to lower oil prices and weak demand, LNG prices are still more expensive than other fuels, such as naphtha and fuel oil. Nuclear restarts in Japan should limit demand further, keeping prices low.

Metals

It has not been a happy new year for base metals and for copper in particular. A combination of US dollar strength, oil price weakness, and continued China growth concerns finally broke copper's downside resistance in the second week of the new year. Growing LME selling pressure from macro-funds from early January, plus the knock-on effect of Chinese funds short selling Shanghai futures (SHFE) copper from January 12th onwards, and a liquidation of generalist investors' commodity index exposures, collapsed LME copper prices to 6 year lows of $5,353/tonne on January 14th. We continue to hear the refrain from investors that copper is the new oil. However, there is a key difference between the market fundamentals of oil and copper, the former suffering from a ballooning supply-led surplus, while the latter patently is not.

Copper forward curves on both the LME and SHFE markets remain resolutely backwardated, suggesting tightness still exists in the global copper market. Chinese physical premia for metal in bonded warehouses are now at their highest since mid-November despite China's record high November refined copper output and resurgent import volumes. Also telling is the growing arbitrage margin between LME and SHFE prices, with the SHFE 3-month price discount to LME hitting new highs in the past week, pointing to growing Chinese copper import buying opportunities, which we expect to see acted on post Lunar New Year. Indeed, we continue to believe that fundamentals for copper remain supportive. Chinese copper end-use sectors actually saw surging activity in 2014, belying the weak PMI and IP (Industrial Production) reads during the second half of the year. Sectors ranging from air-conditioners, transformers, power equipment and power cables, to household goods such as TVs, electric cookers, microwave ovens, micro-computers and mobile phone equipment have seen manufacturing rates accelerating in the year to November 2014 versus 2013 rates. Strong consumer confidence in China, signs of housing start improvements, and an expected pick-up in energy infrastructure spend versus the fraud probe-hampered grid investment last year, point to a year of strong Chinese copper consumption. On the supply side, we expect mine production to disappoint, much as it did through 2014, where the out-turn for the year should be less than 3% growth versus consensus expectations at the start of the year of 5-6%. Reductions in 2015 production guidance for major copper mines have been coming thick and fast, with Rio cutting Kennecott's expected output by 100,000 tonnes, BHP cutting 150,000 tonnes from Escondida's

2015 outlook, while Glencore has cut guidance at Minera Alumbrera by 50,000 tonnes.

We expect copper fundamental to be supportive of prices in the second half of the year, with levels recovering to over $7,000/t. However, we have scaled back H1 expectations in light of the recent price pull-back, with levels in Q1 now projected to average $6,240/t. Where copper leads, other base metals tend to follow, with the sector as a whole seeing sharp macro-fund driven sell-offs in the second week of January. This has resulted in a rebasing of most of our Q1 and Q2 price projections.

Precious Metals

Gold prices saw a significant step-up in their trading range in the second week of January to the mid-$1,200s level despite a stronger US dollar and the ongoing collapse in developed economies inflation expectations as measured by forward break-evens (which have, in their own right, moved tick-for-tick with lower crude oil prices). This phenomenon may suggest ongoing long USD and gold positions versus short Euro and short Yen legs in advance of Greek elections and in anticipation of outright QE in the Eurozone and ongoing easing in the BoJ (despite the recent squaring on light positioning in USDJPY where the consensus move is still towards 1.25-1.30). The de-pegging of the Swiss Franc from the Euro on Thursday January 15th added to upside gold momentum while the Euro went into freefall as markets read the removal as an indicator that ECB QE was a step closer.

Weaker-than-expected US retail sales (even stripping out lower gasoline price impacts) for December really helped buttress gold as US front-end rates rallied hard and core bond yields across most of the OECD settled at all-time nominal lows. Extreme yield compression and growth concerns continue to support yellow metal prices as investors have now shifted expectations of an FOMC rate lift-off out to September/4Q'15 from a June target just a few weeks back. We have therefore lifted our 2015 gold price expectations, with Q1 levels now projected average $1,250/oz. versus the year-to-date average price of c$1,220/oz. (which happened to be our 'old' gold 2015 average price target). While silver has benefitted from renewed investor attraction to gold, the same cannot be said for the PGMs, and platinum in particular. Whilst fundamentals remain supportive for palladium, sluggish demand and improving cost dynamics for South African platinum miners weight on platinum prices through the end of Q4 2014 and into the first quarter of this year. As a result we have pulled down our average Q1 platinum price expectation to $1,265/oz., but left palladium expectations unchanged.

Bulks

Bulk commodity prices have come under pressure from depreciating currencies of major exporters, lower oil prices, and falling freight costs. Cost support has thus been reduced and in the context of weak demand and oversupplied markets, prices are likely to fall to new lower cost-support levels. This is particularly true of thermal coal in the Atlantic Basin, where prices have declined sharply as the largest suppliers (Colombia and Russia) have seen costs fall over $10/t while demand is threatened by coal-to-gas power switching. In the Pacific, the market is only marginally better given weak Chinese demand and China imposing a 6% tariff on imports and removing tariffs on exports.

While iron ore prices have held up to start the year, January is typically the weakest month of the year for supply as well as the peak restocking season. We expect prices to fall with rising supply from Australia and Brazil, reduced costs for marginal producers, and poor prospects for Chinese steel demand.

Grains

International food prices have continued to decline in recent months and crop prices are for the most part expected to remain in a significantly lower trading band in 2015 versus the high and volatile marketing cycle of 2010 – 1H'14. The world is awash with staple grain supply on back-to-back bumper Northern Hemisphere harvests, while sugar, dairy and cooking oil prices have all weakened in the past year on improving output, cheaper feedstock and stable demand trends.

To be sure, the critical and market-moving US Department of Agriculture (USDA) annual crop reports published this month affirm the Citi Research bearish-to-neutral 2015 price outlook for agriculture commodities such as corn, soybeans and wheat. Crop prices increased unexpectedly earlier this winter on strong early season export commitments and biofuel production even as markets were entering peak inventory season. Benchmark grain prices have since declined c5-10% in the first half of January. Broker markets suggest it was not farmer or producer-origin selling, which given the large physical overhang of US quarterly grain stocks, a looming Latin American oilseed loading program in 2Q'15, larger global wheat supply and the CONAB upgrade to the Brazilian maize production outlook should further temper price cheer as those supplies are marketed and US trade commitments from earlier in the 2014/15 cycle begin clearing this quarter.

Forward curves for the benchmark grains complex began the year higher than the 2015 Citi price forecasts of $3.85/bu corn, $9.75/bu soybean and $5.35/bu wheat but are now all trading more 'in-line' with the Citi view. With one of the most critical annual agriculture market data releases now out of the way, investors are likely to focus next on spring planting intentions and weather and crop insurance levels with increasing scrutiny into March. Absent a tail event, cereal prices should stay compressed over the next several months. Low oil prices and depreciating (non US) FX are likely to buttress farmer margins upstream, while significantly (50%+) lower retail gasoline and diesel prices can hinder the growth of biofuel demand for grain crops downstream.

Figure 45. Citi Commodities Research 6-12 Month Sector Outlook*

	Bullish	Neutral	Bearish
Energy	Brent Crude	WTI, HH Natural Gas	
Base Metals	Nickel, Copper, Lead	Aluminum, Zinc	
Precious Metals	Palladium, Gold	Platinum, Silver	
Bulks	Thermal Coal	Met Coal	Iron Ore
Agriculture	Coffee	Corn, Wheat, Cocoa	Cotton, Soybeans

Source: Citi Research, *subject to revision

Figure 46. Citi Commodity Price Forecast*

		Point Prices																			Annuals	
		0-3M	6-12M		Q3 2013	Q4 2013	Q4 2014E	Q1 2015E	Q2 2015E	Q3 2015E	Q4 2015E	Q1 2016E	Q2 2016E	Q3 2016E	Q4 2016E	2012	2013	2014E	2015E	2016E	2017E	2018E
Energy				**5Y Cyclical**																		
NYMEX WTI	USD/bbl	52.0	50.0	81.0	108.0	97.6	74.0	52.0	47.0	58.0	61.0	63.0	58.0	63.0	64.0	94.1	98.0	93.0	55.0	62.0	79.0	82.0
ICE Brent	USD/bbl	60.0	58.0	85.0	112.0	109.3	78.0	60.0	55.0	65.0	70.0	70.0	67.0	70.0	73.0	111.7	108.7	100.0	63.0	70.0	85.0	85.0
Henry Hub N	USD/MMBtu	2.90	2.80	5.50	3.55	3.85	3.80	2.90	2.60	2.70	2.80	2.80	2.90	3.00	3.10	2.75	3.73	4.40	2.70	3.00	4.70	4.70
Base Metals				**LT Price**																		
LME Aluminu	USD/MT	1,870	2,000	2,200	1,827	1,815	1,976	1,850	1,920	1,950	2,000	2,050	2,090	2,110	2,130	2,049	1,888	1,893	1,930	2,095	2,200	2,300
LME Copper	USD/MT	6,500	7,200	6,200	7,096	7,161	6,574	6,240	6,600	7,000	7,100	7,350	7,600	7,850	8,000	7,945	7,352	6,829	6,735	7,700	8,200	8,400
LME Lead	USD/MT	1,950	2,250	2,200	2,116	2,134	2,011	1,880	2,000	2,100	2,250	2,400	2,300	2,390	2,500	2,072	2,158	2,113	2,060	2,400	2,450	2,360
LME Nickel	USD/MT	19,000	22,500	21,000	13,996	13,980	15,926	16,000	19,000	21,500	22,500	24,500	25,000	25,000	26,500	17,592	15,105	16,950	19,750	25,250	26,000	24,500
LME Tin	USD/MT	20,000	21,000	20,000	21,284	22,951	19,902	19,600	20,500	20,700	21,000	22,600	23,000	23,000	23,500	21,108	22,340	21,902	20,450	23,025	24,000	23,000
LME Zinc	USD/MT	2,250	2,350	2,100	1,896	1,932	2,242	2,200	2,280	2,320	2,350	2,380	2,395	2,350	2,400	1,963	1,940	2,165	2,290	2,380	2,350	2,320
Precious Metals				**LT Price**																		
COMEX Gold	USD/T. oz	1,270	1,240	1,050	1,330	1,274	1,201	1,250	1,230	1,235	1,240	1250.0	1250.0	1260.0	1280.0	1,669	1,416	1,266	1,240	1,260	1,340	1,400
Silver	USD/T. oz	17.3	16.8	16.5	21.5	20.8	16.5	16.9	16.7	16.8	16.8	16.9	16.9	17.2	17.6	31.2	24.0	19.1	16.8	17.2	18.6	20.0
Platinum	USD/T. oz	1,300	1,400	1,763	1,456	1,397	1,231	1,265	1,325	1,375	1,410	1450.0	1500.0	1580.0	1630.0	1,552	1,490	1,385	1,345	1,540	1,763	1,880
Palladium	USD/T. oz	840	900	780	729	725	788	830	865	885	900	900.0	905.0	915.0	920.0	645	728	803	870	910	950	980
Bulk Commodities				**5Y Cyclical**																		
Hard Coking	USD/MT	107	115	170	143	142	111	108	110	114	120	123	126	128	130	191	148	115	113	127	150	145
Thermal Coa	USD/MT	53	53	90	77	82	63	56	53	53	56	60	63	65	67	94	84	71	55	64	85	100
Iron Ore Spo	USD/MT	60	55	81	133	135	74	66	56	53	58	60	62	62	65	128	135	97	58	62	73	80
Agriculture																						
CBOT Corn	USd/bu	360	388	N/A	512	430	355	360	375	400	400	420	440	435	400	695	578	410	385	425	450	N/A
CBOT Soybe	USd/bu	1,000	980	N/A	1,405	1,304	975	1,000	1,010	950	950	950	960	950	940	1,465	1,406	1,245	975	950	1,040	N/A
CBOT Wheat	USd/bu	515	540	N/A	650	655	520	515	530	550	540	560	560	570	530	750	684	580	535	555	570	N/A
NYB-ICE Cot	USd/lb	55.0	60.0	N/A	85.6	80.3	60.0	55.0	60.0	59.0	59.0	60	60	60	60	80.0	84.0	76.0	58.0	60.0	N/A	N/A
ICE Coffee	USd/lb	215	225	N/A	118	110	195	215	225	225	240	225	225	225	225	175	125	175	225	225	N/A	N/A
ICE Cocoa	USD/MT	2,900	2,800	N/A	2,420	2,706	2,925	2,900	2,800	2,800	2,600	2600	2600	2600	2600	2,348	2,400	3,000	2,775	2,600	N/A	N/A

Source: Citi Research, *subject to revision

Appendix A-1

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