

## ECB's Visco: Fresh Inflation Declines Would Require Rapid QE Launch

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

### Summary

**ECB's Visco says fresh inflation declines would require rapid QE launch**, noting that such an operation would aim to bring the ECB's balance sheet to "desired levels".

**ECB's Nowotny: broad economic conditions will be key input in any QE decision.** Latest purchase figures from the ECB showed it bought €187m worth of ABS last week as well as €3.829bn worth of covered bonds.

**Germany: Bundesbank monthly report calls for sticking to EU fiscal rules**, noting that proposals that countries which do not need further consolidation to meet EU fiscal rules should loosen their budgets, while respecting the rules, "are not persuasive."

**Italy: PM Renzi meets with former PM Prodi**, reportedly discussing a potential candidacy of Mr Prodi as President of Italy.

**Spain: government approves new unemployment benefit assistance** for long-term unemployed.

**EU's Moscovici: Greece has come a long way and not repaying its debt would be "suicidal".**

**Greece: Syriza lead narrows in GPO Poll for Mega Channel**, with 28% of support (from 26.7% reported in October) vs. 23.1% for the ruling New Democracy party (from 20.2% reported in October).

### Today's News in Detail

**ECB's Visco: fresh inflation declines would require rapid QE launch** - Bank of Italy governor Ignazio Visco told the Italian parliament on Monday that "if new inflation figures confirm the persistence or even the worsening of the risks to price stability in the euro area, then it would be necessary to start rather quickly further interventions to buy bonds on a large scale". He added that such an operation would aim to bring the ECB's balance sheet to "desired levels". Mr. Visco warned that the effect of oil price falls on inflation "will be worse in coming months", adding: "At the ECB, many of us support moving to contain these risks." Comment: the two contingencies laid out by President Draghi with respect to inflation expectations and balance sheet dynamics are likely to be triggered very soon, in our view, probably on Jan 22. With a majority of Governing Council members already in favour of non-standard measures, we think that the

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16 December 2014

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With thanks to Ann O'Kelly

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Economics

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Western Europe

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Industrialised G7 Countries

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### Recent Research

#### Euro Economics Weekly — Will Political Risk Matter in 2015?

12 December 2014

Recent developments in Greece have highlighted political risks in the Eurozone. The situation in Greece is unique and we do not expect events there to trigger a major crisis in the Eurozone, but political risks are likely to rise in the Eurozone more broadly in 2015. In Greece, Syriza could become the first non-mainstream party in the Eurozone to lead a government, should early elections take place in January 15. In Spain, the popularity of the leftist Podemos party is rising, but we do not expect it to be part of the next Spanish government. In Portugal, an opposition victory is still likely to lead to another mainstream coalition. The large rise in political fragmentation in the Eurozone implies weaker mandates for governments, raises the risk of political inaction and instability, and increases the likelihood of market- and business-unfriendly policies. Such risks are likely

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obstacles to additional stimulus are relatively modest at this stage, especially in light of a lower take-up in the 2nd TLTRO.

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**ECB's Nowotny: broad economic conditions will be key input in any QE decision** – Speaking after the presentation of the Austrian Central Bank's semi-annual financial stability report, Mr. Nowotny noted that the ECB will make sure it is not tightening, that the approval of QE will "*always depend on the broad economy*" and that "*nobody in the Council will approve QE without conditions*". He also said it is not the ECB's goal to have uniform rates across the euro area. The latest weekly purchase figures from the ECB showed it bought 187 million euros worth of asset-backed securities last week as well as 3.829 billion euros worth of covered bonds. Comment: the ECB cannot allow its balance sheet to shrink as it would amount to an unwanted tightening of its monetary policy stance. The remark about conditionality probably refers to the structure of a programme (maturities, amounts, etc), rather than any fiscal objectives since there cannot be any quid pro quo when fighting deflation, in our view.

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**Germany: Bundesbank monthly report calls for sticking to EU fiscal rules.** Bloomberg reports that the monthly bulletin of the Bundesbank called on the European Commission to enforce its budget rules, noting that proposals that countries which do not need further consolidation to meet EU fiscal rules should loosen their budgets, while respecting the rules, "*are not persuasive*." The report notes that EU economic forecasts do not signal a deflationary spiral so "*a slightly more restrictive orientation for aggregate demand that would result from all countries following the fiscal rules is acceptable*." Regarding Germany, the report notes that its fiscal stance in the coming year will be "*noticeably eased. An additional budgetary easing as recommended by the commission does not appear to be advisable*" in the face of the economic situation, high debt ratios and demographic change. According to the report, the German economy had a "*modest start*" to Q4, though "*initial signs are emerging that economic growth could strengthen*." The report also noted that the purchasing power of households will be boosted by the drop in oil prices, but the drop in oil prices could also mean that the inflation rate could temporarily approach zero, even in Germany.

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**Italy: PM Renzi meets with former PM Prodi.** PM Matteo Renzi met with former PM Romano Prodi on Monday to discuss international politics, including Libya and Ukraine, as well as the European economy, daily Ansa reports. In addition, Mr Renzi reportedly discussed the potential candidacy of Mr Prodi for President of Italy if incumbent Giorgio Napolitano decides to resign in coming months. Comment: the potential resignation of Mr Napolitano (who is aged 89) in coming months is likely to prove challenging for Mr Renzi, as it will need to secure agreement from both the dissident left-wing part of his own PD party (for which Mr Prodi seems the preferred candidate) as well as the opposition.

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**Spain: government approves new unemployment benefit assistance.** PM Mariano Rajoy signed an agreement with trade unions and employers setting up a new unemployment benefit for long-term unemployed. The assistance (€426 per month, i.e. 65% of the social income) will be available for those that have continued looking for work over the past 12 months, and have exhausted other unemployment benefits in the past 6 months. The new benefit will be paid out for six months. The government estimates a total cost of €1.15bn (If all estimated 450,000 unemployed who are entitled to the regime take part).

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**EU's Moscovici: Greece has come a long way and not repaying its debt**

to rise further even after 2015.

Ebrahim Rahbari | Tina M Fordham |  
Guillaume Menuet | Michael Saunders |  
Antonio Montilla

## UK Economics Weekly — Looking Back...What Were The Surprises of 2014?

12 December 2014

For the second year in a row, the UK has had the opposite of stagflation, with above-consensus real GDP growth and below-consensus inflation. 2014 saw the biggest inflation undershoot (versus consensus) of the last 25 years. The labour market again proved surprisingly flexible, with below-consensus pay growth (fourth year in a row) and below-consensus unemployment (third year in a row). We expect many of these themes will carry over into 2015, with the oil price collapse helping to ensure above-consensus real GDP growth, very low inflation (we expect CPI inflation will average just 1.1% in 2015) and another sharp drop in unemployment. But, unlike the last few years, we expect 2015 will also see a marked rise in real wages. We wish all our readers a Merry Christmas and a Happy New Year. The next edition of UK Economics Weekly will be published week commencing 5 January 2015.

Michael Saunders | Ann O'Kelly

## Sweden — Riksbank Forecast: Stable Rate, Lower Rate Path

12 December 2014

The Riksbank gathers for its two-day monetary policy meeting on Monday (15 Dec), and will announce its interest rate decision on the following day. After the 25bp rate cut in October, we expect a unanimous Riksbank to leave the repo rate unchanged at zero percent next week. As the Riksbank has emphasized little tolerance for downside surprises to inflation, we reckon that the downward pressures on the Bank's CPIF inflation forecasts from lower oil prices and the decline in Prospera wage and inflation expectations on all horizons from already depressed levels in December will sit uncomfortably with the Riksbank. In turn, we expect the Central Bank to lower its conditional interest rate path in the December Monetary Policy Update,

would be **“suicidal”**. The *Financial Times* reports that EU Economic and Monetary Affairs Commissioner Moscovici said that he wanted to give a political signal that there was progress in Greece, during an interview in Athens after meeting with PM Samaras. Moscovici said that *“the Greek government made a huge effort to reform the economy.”* He added that *“the eurozone is about obligations, mutual obligations. When one has a debt, the debt needs to be reimbursed”*, noting that *“the idea of contemplating not reimbursing debt is, in my view, suicidal, with a risk of default. It’s not against Syriza. It’s for the reality.”* Moscovici said that he expected *“a new relationship”* between the Greece and the EU, noting that *“of course we cannot go with the troika as it is”* as he knew the current weaknesses which required a *“more balanced approach.”* Separately, German newspaper *Bild* reports that the IMF calls for further reforms (to strengthen tax investigation, to increase the sales tax for hotels to 13% from 6.5%, and to abolish excessive early-retirement rights) before it would sign off on the next tranche of the current bailout. Greek central bank governor Stournaras noted in a speech that the liquidity of the Greek government bond market was quickly diminishing.

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**Greece: Syriza lead narrows in GPO Poll for Mega Channel.** Bloomberg reports that main opposition Syriza party gets 28% in a survey of voting intentions for Anatropi news talk show, published on the website of Greece’s Mega Channel. PM Antonis Samaras’s New Democracy party came second with 23.1% and the Communist Party of Greece is third with 5.5%. Pasok, Samaras’s junior coalition partner, and To Potami, have 5.1% each of voting intentions, while the far right Golden Dawn party got 5% and the Independent Greeks party 2.7%. In the previous GPO survey published on October 14, Syriza got 26.7% of voting intentions vs 20.2% for New Democracy.

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## Latest Issues of Sovereign Debt Update

### Greece: Syriza’s Lead Narrows in Two Opinion Polls

15 December 2014

Greece: Syriza’s lead narrows, FinMin applies for precautionary credit line. ECB’s Draghi to ask for reforms at EU Council meeting. ECB relaxed about low TLTRO take-up, SSM endorses bank capital plans. Weidmann says QE advantages don’t outweigh costs. German FinMin: balanced budgets through 2018. France: Poll confirms voters’ appetite for reforms. Italy: 60% participation in General Strike. Spanish banks’ borrowing from Eurosystem falls. Portugal: opposition PS ahead of ruling coalition - poll.

[Guillaume Menuet](#) | [Ebrahim Rahbari](#) | [Antonio Montilla](#)

### 2nd ECB TLTRO Take-Up Below Expectations at €129.8bn

12 December 2014

TLTRO take-up insufficient to compensate for maturing 3-Y LTROs. ECB moves to 6-week cycle for new Economic Bulletin. ECB’s Liikanen stresses importance of ability to act over unanimity. Germany: economy recovering with “low dynamism”. France: deficit trajectory adjusted down, EC gives long list of insufficient actions. French pension system shortfall likely, says watchdog. Italy: IP falls again. Greek PM slams Syriza for reviving Grexit fears, Syriza hits back. Portugal’s HICP at 0% YY.

[Ebrahim Rahbari](#) | [Guillaume Menuet](#) | [Antonio Montilla](#)

### “1% Economics” Unsustainable, Warns ECB’s Coeuré

11 December 2014

ECB’s Hansson: too early to say if QE decision in Jan. ECB’s Angeloni: capital

postponing initial tightening by one quarter to 3Q 2016, and revising down the optimal rate path 4Q-17 end-point of 1.75% by around 15-20bp.

[Tina Mortensen](#)

### UK — Construction Slips, Previous Data Revised Up – As Usual

12 December 2014

The ONS report that construction output fell 2.2% MM in October, but at the same time revised up the September figure from 1.8% MM to 2.2% MM. This pattern of a soft figure for the latest month coupled with an upward revision to earlier data occurs quite frequently for the construction output data. We stress that there is nothing inherently wrong with having data revisions. But, in interpreting data, it probably is useful to know if there is a revisions bias - and for these data, at present, such a bias does seem to exist. With business surveys suggesting that the trend in construction output remains buoyant, we expect the weakness in these data will probably be revised or reversed in coming months.

[Michael Saunders](#)

### Norway — Dovish Norges Bank: Cuts by 25bp and Signals More Could Come

11 December 2014

Norges Bank surprisingly cut the key policy rate by 25bp to 1.25% and lowered its conditional interest rate path by more than expected at today’s monetary policy meeting, indicating a 48% probability of another near-term interest rate cut. In addition, initial tightening was postponed further from 4Q-16 to 1Q-17. The Bank’s dovish stance was motivated by a *“notably weaker”* outlook for the domestic economy *“than envisaged earlier”*, due in particular to softer-than-expected activity in the petroleum industry, but also to the heightened uncertainty surrounding the global and domestic growth outlook. With the large downward revision to the Bank’s growth outlook and its expectations of a significant strengthening of the NOK, the Bank will have to turn substantially more pessimistic on growth or inflation pressures decrease for it to lower rates

gap for many banks "tip of iceberg". Germany: DIW head says ECB should buy sovereign debt. Euro Working Group approves 2-month extension for Greece. Greece: reform progress hailed, PM says Syriza provoking "terror" among investors. France: reform bill approved by cabinet, CPI slows. Italy's NPL ratio rises. Spain: population falls, house transactions rise. Portugal: goods exports rise.

Guillaume Menuet | Ebrahim Rahbari | Antonio Montilla

## ECB's Praet and Makúch Offer Strong Hints About QE

10 December 2014

ECB's Praet and Makúch on QE. EU agrees contributions to Single Resolution Fund. Greece's presidential candidate Dimas. Merkel to limit inflation-induced tax rises. France: "Law on Growth and Activity" in cabinet today, IP and employment data disappoint. Italy: IMF's Lagarde highlights areas where progress needed. Italy's banks reduce CB borrowing. Spain's govt presents €53bn work of projects to Juncker plan. Portugal: growth may exceed 2%, says EconMin.

Ebrahim Rahbari | Guillaume Menuet | Antonio Montilla

## Greek PM Calls Presidential Election for December 17

9 December 2014

Greek PM calls snap presidential election. Eurogroup approves 2-month extension for Greece. ECB's weekly asset purchases. Coeuré says dissent at ECB meeting on communication, not on stance. Nowotny says GC focusing on govt bonds QE. Dijsselbloem on incentives for structural reform. Merkel rules out cooperation with euro-sceptic AfD. Eurogroup on 2015 French budget. Spain: house prices, bank plans for TLTRO. Dutch CB lowers GDP forecast. Portugal's economic conditions improving - Dijsselbloem.

Ebrahim Rahbari | Guillaume Menuet | Antonio Montilla

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## Macroeconomic Forecasts

### European Economic Forecast Highlights, December 2014

3 December 2014

This companion to the December issue of Global Economic Outlook and Strategy - Prospects for Economies and Financial Markets in 2015 and Beyond gives more detailed forecasts for the main European countries to 4Q16. Figures 21-22 give annual forecasts to 2018 for growth, inflation, current balance, fiscal balance, primary balance and government debt and Figure 23 shows the change in forecasts from last month. Figure 24 shows forecast unemployment to 2019, and Figures 25-27 compare our forecasts with those of other institutions.

Ann O'Kelly | Michael Saunders | Guillaume Menuet | Ebrahim Rahbari | Tina Mortensen

### Europe — Europe: Monthly Inflation Profiles for Selected Countries

2 December 2014

Updated monthly inflation forecasts for Euro Area, Germany, France, Italy, Spain, UK, Sweden and Switzerland.

Ann O'Kelly | Michael Saunders | Guillaume Menuet | Ebrahim Rahbari | Tina Mortensen

### Global Economic Forecasts — December 2014

3 December 2014

This file shows summary forecasts as published in Citi's Global Economic Outlook and Strategy

Michael Saunders

again in March, in our view. However, having learned our lesson, we caution that one should never underestimate a dovish Central Bank.

Tina Mortensen

## Switzerland — SNB On Hold, Projects Renewed Deflation

11 December 2014

The SNB kept policy on hold, with the mix of zero rates and CHF1.20/€ cap seen since late-2011, and repeated its standard language: *"the SNB will continue to enforce the minimum exchange rate with the utmost determination."* The SNB is actually a little more optimistic on the growth outlook than in September.

Nevertheless, the SNB still judges that there is plenty of spare capacity in the economy. In addition, the SNB has (for the fifth consecutive quarter) again cut its inflation forecast – and now expects renewed mild deflation. Against this backdrop, we expect the SNB to keep rates on hold for several years.

Michael Saunders

## Sweden — Long-term Inflation Expectations Drift Lower in December

10 December 2014

According to the quarterly survey among all market participants, Swedish inflation expectations slipped further on all horizons in December. Most noteworthy, long-term inflation expectations slipped 0.1pp to 1.72%, the lowest reading since 2Q 1999 and also widening the gap versus the 2% inflation target. This will clearly prove a concern for the Riksbank – recall that low actual inflation and falling inflation expectations from already depressed levels were key drivers behind the recent repo rate cuts. Today's outcome is an important element supporting the case for additional monetary easing. With the policy rate now at zero, the Riksbank has effectively used up its options for conventional monetary policy easing. We expect that the Riksbank's first options for further stimulus (if needed) would be forward guidance (with a 1.5% CPIF threshold), coupled with a cut in the repo rate to -25bp in the next five-six months. This is our base case.

## Global Economic Outlook and Strategy — Prospects for Economies and Financial Markets in 2015 and Beyond

1 December 2014

In this "Prospects" edition, Citi's research team presents updated forecasts for economies, interest rates, FX rates, commodity prices and sovereign ratings around the world for 2015 and beyond. Overview essays discuss the drift into secular stagnation, whether globalization is stalling, political issues for 2015, emerging market strains, advanced economy "low-flation" and long-run projections for the size of major economies. We are cutting 0.1 percent off our global growth forecast for 2015 and 0.2 percent off for 2016, and expect only a modest pick up in global growth in 2015, led by advanced economies. Major monetary policy divergence is likely, with QE by the ECB and BoJ, widespread nearterm monetary easing across emerging markets, but (in late-2015) tightening by the Fed and BoE. We forecast further major USD appreciation, breaching €1.10/\$ and ¥125/\$ in 2015, with levels of €1.00/\$ and ¥135/\$ likely over the next 2-3 years.

Willem Buiter | Guillermo Mondino | Michael Saunders | William Lee | Kiichi Murashima

## Emerging Markets Macro and Strategy Outlook — Prospects For 2015 And Beyond

1 December 2014

EM's prospects in 2015 will be governed by familiar themes: i) China's slowdown and its consequences; ii) the impact of falling commodity prices; and iii) the prospect of US monetary tightening. EM will face a challenging, though not insurmountable, year. After all, returns from (and flows into) EM were positive in 2014 in spite of a wide set of challenges. Weaker commodity prices in EM the last few quarters have had a notable effect on macroeconomic performance across the group of EM commodity exporters; so it is now possible to argue that a principal dividing line in EM is between manufacturing-based economies and commodity-based ones. On balance we expect EM spreads to widen by 15bp next year but with significant volatility, and with particular difficulty for quasi-sovereigns. In local markets, our themes are broadly negative on EMFX and more constructive on duration.

Guillermo Mondino | David Lubin | Johanna Chua

## Foreign Exchange Forecasts — EUR/USD Parity Breach – November 2014

21 November 2014

The multi-year USD rally looks set to have legs as divergence in economic performance and monetary policies continues. We see 10-20% more USD upside vs. G10 currencies over the next couple of years. EUR/USD should find support in the low 1.20s short term but cut through, like a hot knife in butter, medium to long term. We expect parity to be approached and maybe breached over two years. BoJ QE acceleration announced on 31 October surprised the market and pushed USD/JPY sharply higher. We may get near term consolidation sometime given how overbought the USD is. But portfolio rebalancing and ongoing money base expansion should push USD/JPY towards 125-135 longer term. EM currencies are likely more protected by carry and lack of local quantitative easing. We expect USD gains of 5-6% vs. EM over 6-12m.

Jeremy Hale | Maximilian Moldaschl | Guillermo Mondino | Alexander Demyanets

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Tina Mortensen

## Euro Area — Greece: Snap Presidential Elections Highlight Political Uncertainty in Wake of Troika Decision To Extend Bailout

9 December 2014

Greek PM Samaras called an early Presidential election for December 17 in the wake of likely bailout extension by two months until end-February. The final round of a potential three-stage presidential vote would take place on Dec 29. The current coalition government has the support of 155 MPs, 25 short of the majority needed to elect a new president. If the current parliament fails to elect a new President, early parliamentary elections will be triggered, probably in the 2nd half of January. An average of recent polling trends suggest that far-left Syriza would win parliamentary elections, even though perhaps without a majority in parliament. A potential follow-up bailout programme is to be negotiated by mid-February, and its conclusion could therefore depend on the outcome of a potential parliamentary election. However, the new developments highlight major political uncertainties in Greece that were already there in any case rather than raising them.

Ebrahim Rahbari | Tina M Fordham

## UK — UK Production, Interest Rate and Mortgage Data

9 December 2014

The ONS report that manufacturing output fell 0.7% MM in October. We note, however, that these data are often volatile and also are often revised. Business surveys (which are not so weak) often give a better real-time guide to the underlying trend in output growth than the ONS data. Second, the BoE report that key household fixed mortgage rates fell to new record lows in November. The sharp recent drop in mortgage rates, plus the boost to real incomes from lower oil prices, probably will give a powerful further stimulus to the economy in coming months. Third, the PRA report that the share of new mortgage loans with high LTVs and high income multiples fell slightly in Q3. The signs that macroprudential policy is

biting are likely to lessen any pressure on the MPC to use tighter monetary policy to rein in the riskier parts of lending.

[Michael Saunders](#)

## **Scandi Economics Update — Riksbank Forecast: Stable Rates, Lower Rate Path**

**16 December 2014**

**Sweden** — After the 25bp rate cut in October, we expect a unanimous Riksbank to leave the repo rate unchanged at zero percent. As the Riksbank has emphasized little tolerance for downside surprises to inflation, we reckon that the downward pressures on the Bank's CPIF inflation forecasts from lower oil prices and the decline in Prospera wage and inflation expectations on all horizons from already depressed levels will make the Riksbank lower its conditional interest rate path (announcement at 8.30 UK time).

**Sweden** — The Swedish Trade Union Confederation, LO, calls on PM Löfven to cancel the early election scheduled for 22 March.

**Sweden** — FinMin Andersson sees increased downside risks to the government's economic forecasts after "weaker development in Europe".

**Sweden** — An Inizio poll shows that the economy and immigration are key issues for voters in the March election.

[Tina Mortensen](#)

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# Appendix A-1

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