Global Economic Outlook and Strategy

April 2012

- We are once again edging up our 2012 global growth forecast, for the third consecutive month. We now expect that global growth (at current exchange rates) will slow from 3.0% in 2011 to 2.6% in 2012 (up from 2.5% last month, 2.4% in February and 2.3% in January), rebounding to 3.0% in 2013 (unchanged from last month). We again lift our 2012 growth forecasts for Japan and the euro area, although we still expect the euro area to suffer renewed recession this year. PPP-weighted, we expect global growth of 3.1% in 2012, rising to 3.5% in 2013.

- Even with this small upgrade, we remain cautious about growth prospects. Global growth is likely to undershoot the IMF base case (3.5% in 2012 and 4.1% in 2013, PPP-weighted). Household deleveraging will continue to cap demand in many economies, the EMU crisis remains unresolved and the short-term liquidity support for periphery EMU sovereigns from the ECB's 3-year LTROs is probably past its peak. We expect that Spain will enter a Troika programme this year, most likely focused on recapitalizing and restructuring the banks. In our view, Portugal and Ireland are both likely to need a second bailout, while Italy's fiscal and economic outlook is also weak.

- The major central banks are likely to keep policy loose and in some cases loosen further. We expect that renewed EMU strains will prompt the ECB to launch at least one more multi-year LTRO and continue to pencil in one or two more rate cuts by end-2013. Fed officials have tempered market expectations for extra QE but the chance that growth could disappoint this year keeps alive the option for further asset purchases. In China, we expect that YoY growth will slow further in Q2, but that a mix of fiscal loosening, credit easing and targeted easing in the low-end property market will lift growth in Q3. We expect a further series of sovereign ratings downgrades this year, including Italy, Spain, Ireland and Portugal, with a wider range of downgrades (including the US and Japan) over the next 2-3 years. We only expect one rating upgrade: we think Greece will soon exit from the "default" rating to a low rating – but further debt restructuring looks likely later on.

Figure 1. Currency and Interest Rate Forecasts (End of Period, Unless Specified), as of 18 Apr 2012

	18 Apr 2012	2Q 12 Forecast	3Q 12 Forecast	4Q 12 Forecast	1Q 13 Forecast	2Q 13 Forecast	3Q 13 Forecast
United States: Federal Funds	0.25	0.25	0.25	0.25	0.25	0.25	0.25
10-Yr. Treasuries (Period Ave.)	2.01	2.25	2.35	2.45	2.55	2.65	2.85
Euro Area: US$/€	1.31	1.30	1.29	1.27	1.25	1.26	1.27
Euro Repo Rate	1.00	1.00	1.00	1.00	0.75	0.75	0.50
10-Yr. Bunds (Period Ave.)	1.75	1.75	1.70	1.75	1.80	2.00	2.25
Japan: Yen/US$	81	81	81	80	80	81	82
Call Money	0.10	0.10	0.10	0.10	0.10	0.10	0.10
10-Yr. JGB (Period Ave.)	0.95	0.95	1.00	1.20	1.30	1.40	1.40

Source: Citi Investment Research and Analysis

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With thanks to Jan Maguire

Next issue 23 May, 2012

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 from Last Month

Global	We are once again edging up our 2012 global growth forecast, for the third consecutive month. But, even with this small forecast upgrade, we continue to urge against excess optimism over growth prospects.
United States	Recovery remains on a modest track, although some payback from weather-induced gains has begun to surface. Fed officials have tempered expectations of more QE in favour of highly accommodating rate guidance but additional asset purchases could be forthcoming if declines in unemployment stall.
Euro Area	We have revised up our 2012 GDP and inflation forecast in April and no longer expect the ECB to cut rates this year. However, with a further escalation of the sovereign debt crisis under way, the ECB is likely to provide additional multi-year LTROs in the course of 2012 and with inflation likely to come down, we expect the ECB to cut rates in 2013.
China	We keep our 2012 GDP growth forecast of 8.4%, but are cutting the forecast for Q2 growth from 8.2% to 7.9% YoY, to reflect a slower pace of policy easing so far in the year. We expect a rebound of growth in Q3 supported by more accommodative policies since March. Average 2012 inflation is revised up from 3.3% to 3.5% to account for more ambitious price reforms.
Japan	The cyclical economic outlook is improving and we are revising up our 2012 growth forecast to 2.0% from 1.5% in the March forecast. However, the BoJ is likely to take additional easing measures sooner or later with inflation expected to remain barely positive in coming quarters.
United Kingdom	With the weak economy and continued EMU crisis, we continue to expect the MPC will expand QE further.
Canada	The BoC has adopted a rather hawkish tone, stating that some modest withdrawal of the present considerable degree of monetary policy stimulus may become appropriate. The shift from a previously neutral policy tack raised market expectations of a full rate hike before yearend. However, we remain cautious about the outlook, and therefore retain our call for resumed tightening in 1Q 2013.
Australia	Our forecasts are unchanged this month and we still anticipate a pick-up in activity as the year develops, assuming the RBA cuts rates next month.
Emerging Asia (ex China)	Asia's recent economic data confirm a rather stable growth path, with manufacturing looking relatively resilient. However, the outlook could be undermined by China growth worries, EMU financial stress and some "payback" from weather-related US gains in early 2012. Central banks are likely to remain on hold with a rising chance the slightly more hawkish rhetoric will dissipate. Singapore is the only key exception, with the "surprise" MAS slope steepening in April.
CEEMEA	Our CEEMEA forecasts have hardly changed this month. The key issues to watch in the coming weeks are, we think: i) signs of greater confrontation between Hungary and the EU; ii) Turkey's ability to manage what seems to be an informal exchange rate corridor during a period of volatile risk appetite; iii) the risk of a more serious disappointment in data on Poland's economic activity; iv) the growing risk of a foreign exchange shortage in Egypt; and v) the ability of Ukraine to 'muddle-through' without a new IMF programme.

Source: Citi Investment Research and Analysis

Figure 3. Global — Summary of Views of Citi's Market Strategists

	Equities	G10 Rates	Credit	Securitized Products	FX †	Commodities	Global Macro Strategy †
Overall View	Cheap valuations, stabilising EPS, easy monetary policy support further upside	The sell-off has fully reversed and we now expect trading ranges to re-establish themselves	Reducing exposure to neutral	Short, high-quality sectors optimise defensive positioning. Off-the-run sectors offer upside	USD higher	A more challenging 2Q 12 with potential for sharper rebound in 2H 12	Risk assets underpinned by liquidity
Most-Favoured Region/Sector	EM, Japan, Asia Pac ex Japan/ IT, Industrials, Utilities	10yr EUR	Low-beta core non-fins and US banks	US CMBS senior tranches	4USD	Precious Metals	USD, Gold
Least-Favoured Region/Sector	US, Australia/ Healthcare, Telecoms, Cons. Disc	>10yr USD	French corporates and periphery sub-debt	Spanish and Irish RMBS	EUR, AUD, CHF	Bulk Commodities, Copper, Silver, Coffee	Core FI
Key Risks	Escalation of EMU crisis, hard landing in China, sharply higher core government bond yields	Stronger data ends policy status quo. Renewed EMU tensions	Sovereign crisis; bank runs; global slowdown;	Regulation	US economic disappointment / QE3	EMU contagion, oil shock double-dip,risk-off financial outflows China hard landing	EMU breakup, China growth, US fiscal, US economic disappointment / QE3

Source: Citi Investment Research and Analysis
† Summary view from our Global Macro Strategy Market Commentary team (see page 56 for definition of market commentary). The authors are not independent research analysts and may have knowledge of the Firm's positions and/or the Firm's interest in one or more of the securities referenced herein.

Overview: Modest Growth, Wide Divergences

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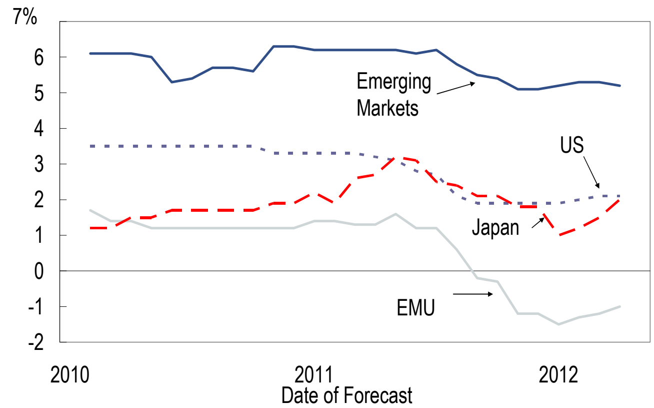
We are once again edging up our 2012 global growth forecast, for the third consecutive month. We now expect that global growth (at current exchange rates) will slow from 3.0% in 2011 to 2.6% in 2012 (up from 2.5% last month, 2.4% in February and 2.3% in January), rebounding to 3.0% in 2013 (unchanged from last month). PPP-weighted, we expect global growth will slow from 3.7% in 2011 to 3.1% in 2012, rising again to 3.5% in 2013.

We are again edging up our 2012 global growth forecast slightly…

…with upward revisions for the euro area and Japan

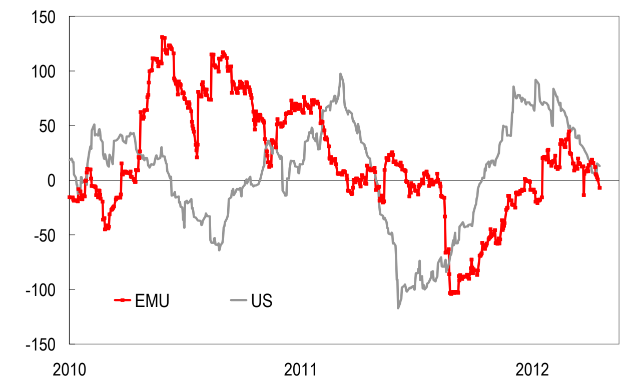
Within that, we are again (for the third month in a row) lifting our growth forecasts in Japan and the euro area: we now expect 2.0% growth in Japan this year, versus 1.5% last month, 1.2% in February and 1.0% in January. We expect euro area GDP growth will be about -1.0% this year, versus -1.2% last month and -1.5% in January. Our 2012 GDP growth forecasts for the US and China are unchanged, at 2.1% and 8.4% respectively.

Figure 4. Global — Citi 2012 Growth Forecasts By Region, 2011-12



Source: Citi Investment Research and Analysis

Figure 5. US and EMU — Citi Economic Surprise Indices, 2010-12



Source: Citi Investment Research and Analysis

We continue to urge caution over growth prospects

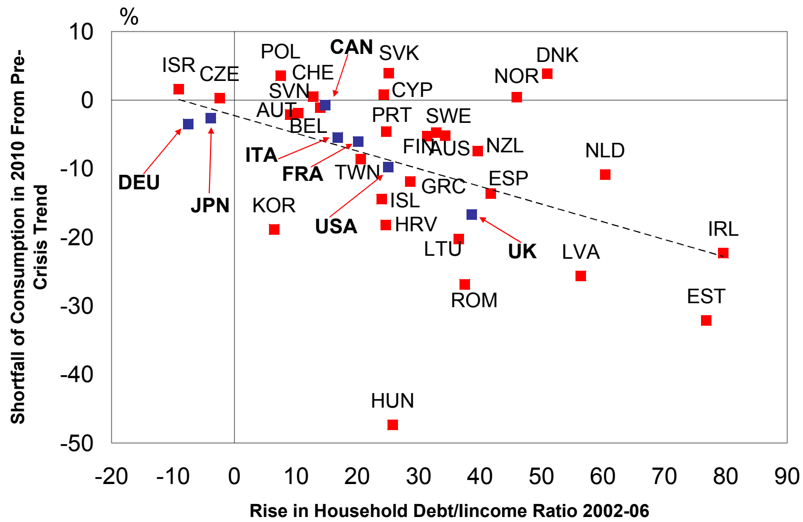
Even with this small forecast upgrade, we continue to urge against excess optimism over growth prospects. Our forecasts are clearly below the IMF base case, which is for global growth of 3.5% in 2012 and 4.1% in 2013 (PPP-weighted), mainly reflecting our gloomier view on the euro area. Moreover, the Citi Economic Surprise Indices have weakened again in recent weeks, and the euro area ESI is now negative again. Global growth is modest, with wide divergences. The expansion will continue to be capped by two major headwinds.

Household deleveraging is likely to remain a widespread drag across advanced economies

First, private sector deleveraging (especially among households) is likely to continue to cap private spending across many advanced economies. Household debt levels remain elevated across many advanced economies and, as the IMF recently argued, the aftermath of boom/bust cycles in household debt and house prices typically sees a prolonged period (several years) of modest growth and balance sheet repair. "*Housing busts preceded by larger run-ups in gross household debt are associated with deeper slumps, weaker recoveries, and more pronounced household deleveraging*."[1] This process of household deleveraging is much further advanced in the US than in most other boom/bust countries: for example, the gross household debt/income ratio rose by 43 percent between 1997 and 2007 for the US and has since reversed roughly half of that. By contrast, only about one quarter of the rise in the debt/income ratio has reversed in the UK, while household debt/income ratios have not yet fallen significantly in other countries with big household debt booms — implying that an extended drag from household deleveraging still lies ahead.

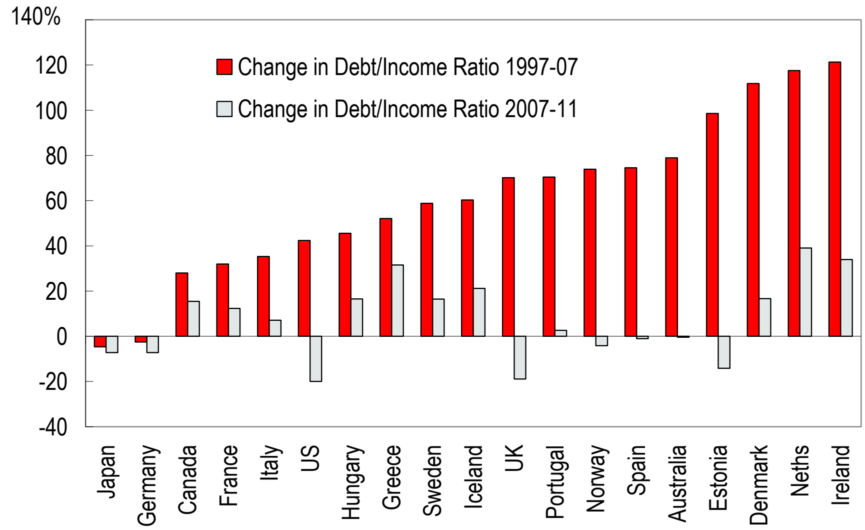
[1] See IMF World Economic Outlook, April 2012.

Figure 6. Selected Countries — Change in Household Debt/Income Ratio 2002-06, and Shortfall of Real Consumer Spending in 2010 Versus Pre-Recession Trend



Note: Each point represents a country. G7 countries shown in blue. Dotted line is fitted.
Sources: IMF and Citi Investment Research and Analysis

Figure 7. Selected Countries — Change in Household Debt/Income Ratio 1997-2011



Note: Latest data for Estonia is 2010. Sources: IMF and Citi Investment Research and Analysis

The ECB's 3-year LTROs produced a massive short-term liquidity fix…

Second, the EMU crisis remains unresolved and is likely to cause further episodes of heightened risk aversion. The ECB's massive 3-year LTROs produced a huge wave of government bond purchases among periphery country banks (especially banks from Spain, Italy and Portugal). For example, Spanish banks' net government bond purchases totaled €61.5bn between Dec-11 and Feb-12, versus €34.1bn in the whole period Jan-04 to Nov-11. Net purchase by Italian banks surged to €22bn-€23bn per month in both January and February this year, far above the prior peak (€15.8bn, March 2009). Net government bond purchases by Portuguese banks rose to €4.2bn in Feb-12, also a record high (previous peak was €3.9bn in Dec-10).

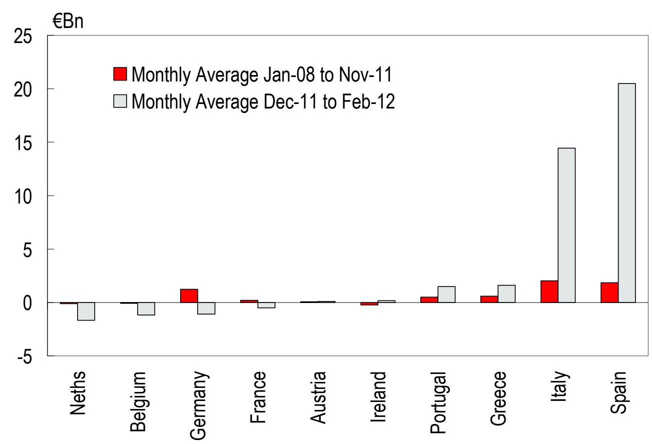
…but that effect appears to be past its peak and the periphery countries continue to face deep-seated economic problems

However, the recycling of LTRO funds into periphery country government debt seems to have passed its peak, with notably lower demand at recent government debt auctions. Moreover, in our view, the periphery countries face deep-seated economic problems, which cannot be cured by a temporary liquidity fix: the details differ from country to country, but the general problem is that the periphery countries (Spain, Italy, Greece, Portugal, Ireland) are probably unable, in our view, to return themselves to fiscal sustainability (defined here, generously, as public debt/GDP ratios below 100%) by the end of this decade. The elevated level of yields needed to attract sufficient funding for the periphery governments makes it even harder to achieve fiscal sustainability, especially given knock-on effect of high government yields on private borrowing costs.

Intra-EMU imbalances were reflected in soaring current account deficits pre-crisis

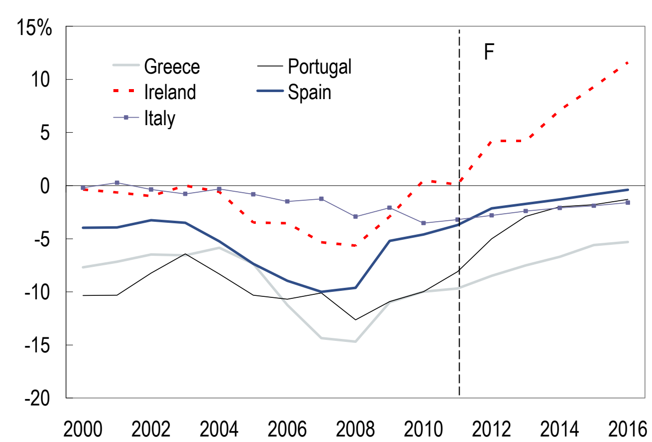
In our view, it is useful to analyse the problems of the EMU countries as a combined crisis of the balance of payments, banks and fiscal position. The periphery countries ran growing — and in some cases huge — current account deficits in the boom, which at the time were easily financed by large capital inflows (especially from the rest of the euro area). These current account deficits were better predictors of the sovereign crisis than fiscal data. With escalating debts and justified caution among creditors, the periphery countries in turn have faced "sudden stops" in capital inflows since 2008[2], triggering sharp retrenchment in domestic demand and fiscal policy. With exports capped by poor external competitiveness and low export exposure to high growth emerging markets, most of the periphery countries continue to run current account deficits and, with adequate private inflows less forthcoming, financing gaps are generating high yields, official funding needs and growing Target liabilities.

Figure 8. Selected EMU Countries — Banks' Net Government Debt Purchases Split By Nationality of Bank, Monthly, €bn, 2008-Feb 2012



Sources: ECB and Citi Investment Research and Analysis

Figure 9. Selected EMU Countries — Current Account Balances as Pct of GDP, 2000-16F



F Citi forecasts. Sources: IMF and Citi Investment Research and Analysis

Fiscal tightening in the periphery countries is likely to exacerbate growth undershoots

The periphery countries do not really have a viable option of deferring fiscal tightening and aiming for growth. Currently, all the periphery countries are implementing heavy fiscal tightening aimed at cutting budget deficits. However, the resultant drag on domestic demand — exacerbated by a varying mix of high private debts (especially Spain, Ireland, Portugal), weak banking systems (all five countries) and supply-side weaknesses (especially Greece, Italy, Spain, Portugal) — is likely to continue to produce extended economic weakness that will lead to persistent overshoots in fiscal deficits and public debts.

[2] See "*Sudden Stops in the Euro Area*", Bruegel Policy Contribution, March 2012.

Fiscal positions may be further worsened by the burden of bank recapitalization (already happened in Greece and Ireland, likely to occur in Spain, possibly Italy and — again— Ireland). If these countries react to deficit overshoots with ever-greater fiscal tightening then, rather than achieve fiscal sustainability, the consequences are likely to be even deeper economic depressions, leading to escalating banking losses, capital flight and loss of popular support. Supply-side reforms are unlikely to yield quick enough benefits to change this outlook: such reforms may limit the medium-term deterioration in potential growth but generally do little to boost demand (and the shortfall of demand is the immediate problem).

Even a return to current account surplus — as in Ireland — may not enable periphery countries to regain normal market access

Moreover, for the EMU periphery, even the achievement of a current account surplus may not be enough to ensure that the government can be funded at a sustainable yield. For example, Ireland's current account has swung from a deficit of 5.6% of GDP in 2008 to surpluses of 0.5% of GDP in 2010 and 0.1% of GDP in 2011. However, external balance has been achieved largely via a collapse in domestic demand (down 27% since Q4-07), which has cut imports. This leaves the economy far from internal balance (ie zero output gap and normal unemployment) and hence with a still-huge fiscal deficit and weakened banks. Even if a country's savings exceed investment (ie it has a current account surplus), capital mobility is so high inside EMU that domestic savings may easily flow elsewhere if that country has an unsustainable fiscal path, weak economy or weak banking system.

The LTROs have left the weak banking systems even more closely linked to weak sovereigns

The LTROs provided short-term scope for governments to issue debt at relatively low yields, but have not solved these underlying economic problems. Indeed, with the widespread "home bias" in periphery banks' purchases of government debt, the LTROs have left the weak periphery sovereigns and weak periphery banks even more closely entwined. The EBA's late-2011 estimate that Spanish banks need to raise an extra €26bn to cover exposure to periphery debt now looks too low: with the recent rise in periphery yields, we estimate a €30bn capital shortfall based on the banks' Sep-11 level of bond holdings — and the actual shortfall probably is even higher given the 38% rise in Spanish banks' holdings of government debt since Sep-11.

We expect recurring strains across the EMU periphery countries

With the downward effect on yields of the 3-year LTROs receding, we expect recurring strains across the EMU periphery. For Greece, the upcoming elections (May 6) are likely to produce a hung parliament and we continue to believe the probability of Greek EMU exit is about 50%[3]. For Portugal, we continue to expect a second bailout will be needed, and that sizeable sovereign debt restructuring is likely (on top of restructuring of local government debts)[4]. In Ireland, the economy has fallen back into recession and is likely to markedly undershoot government and IMF forecasts, leading to deficit overshoots[5]. We doubt the government will be able to regain normal access at a viable yield and suspect that a second bailout will be needed beyond 2013. For Spain, severe fiscal austerity is likely to further exacerbate the recession, fuelling continued weakness in the housing and construction sectors. We believe the government will seek a Troika-led programme to recapitalize and restructure the banking system later this year[6]. In turn, we expect a series of further sovereign ratings downgrades across the periphery countries.

[3] See "Rising Risks of Greek Euro Area Exit", Willem Buiter and Ebrahim Rahbari, Citi, February 2012.
[4] See "Portugal — Second Bailout and Debt Restructuring Likely", Juergen Michels and Guillaume Menuet, Citi, 24 February 2012.

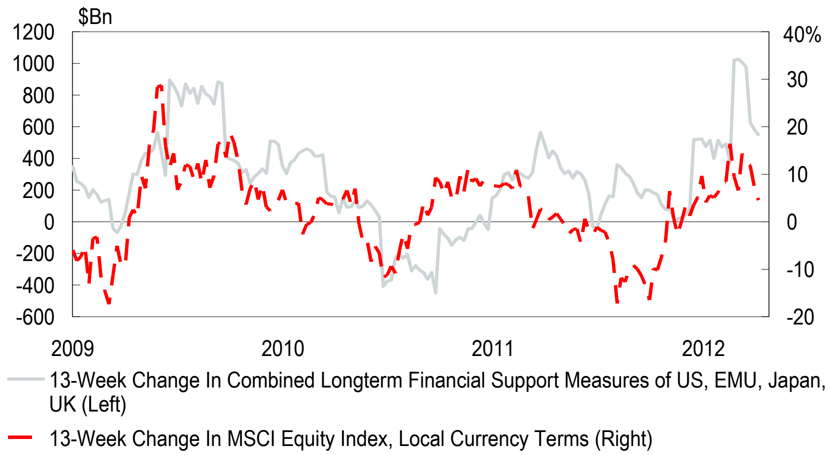
[5] See "Ireland — Tough Times Ahead", Michael Saunders, Citi, 17 February 2012.
[6] See "Focus on Spain", Guillaume Menuet and Ebrahim Rahbari, Citi, 3 April 2012.

There are extra downside risks not fully captured in our forecasts

Moreover, there are major downside risks that are not fully captured in our forecasts, but which have the potential to worsen the outlook.

- First, we assume roughly stable oil prices, but Middle East tensions could well cause a spike, which hits real incomes among oil consumers — even if briefly — and triggers renewed business caution.
- Second, the extent of China's slowdown remains unclear. The economy is likely to slow further in Q2 and there is a risk that – especially if policy loosening remains gradual – the H2 recovery will be delayed or less powerful than we currently expect.
- Third, our forecast assumes that the large US fiscal tightening on tap for 2013 — which potentially could reach 3½% of GDP — will be forestalled, with effective fiscal tightening of about 1% of GDP in 2013.
- Fourth, our forecast implies only limited resolution of the chronic economic imbalances inside EMU and the current account imbalances between creditor and debtor nations — not just the US and China but more broadly. Our base case assumes these are either financed or managed without extreme turmoil, for example by official programmes in EMU, FX reserve recycling and private capital flows in the rest). But there are sizeable risks that the actual path will not be so smooth, for example if Greece were to leave EMU or US-China trade tensions rise.

Figure 10. Selected Countries — Combined Central Bank Balance Sheet Measures and Equity Prices, 13-Week Changes, 2009-12



Note: We sum the ECB's LTRO program, US Fed outright holdings of securities excluding Treasury bills, Bank of Japan asset and BoE APF Gilt holdings. Sources: Datastream and Citi Investment Research and Analysis

We expect that central banks will keep policy loose, and some may loosen further

Against this background, we expect that major central banks will keep policy loose for an extended period, and in some cases loosen further. Central banks have not run out of policy ammunition, and have scope to expand balance sheet measures (and in some cases, to cut rates) if needed. The ECB's recent LTROs suggest that central bank action continues to have powerful traction on risk assets. We expect that worsening EMU tensions around Spain and Italy will prompt the ECB to implement at least one more multi-year LTRO later this year, and — with the weak

economy and an eventual drop in inflation — we pencil in one or two ECB rate cuts by end-2013 (although we have delayed the next cut from H2-2012 to H1-2013). Fed officials have tempered market expectations for additional QE but the chance that growth could disappoint this year has kept alive the option for further asset purchases. In the UK, we continue to pencil in a large further expansion of QE in response to underperforming economy.

We expect core government bond yields to stay ultra-low in 2012 and 2013…

Our forecast implies that core government bond yields are likely to stay ultra-low this year and in 2013. The IMF recently argued that the very low level of core government bond yields owes a lot to portfolio demand for safe assets from central banks, private banks and other investors, and that such low yields may pose problems: "*Considerable upward pressures on the demand for safe assets at a time of declining supply entails sizable risks for global financial stability*."[7]

…and we regard the low level of yields as a benign side effect of difficult economic conditions and exceptional policy stimulus

By contrast, we regard the ultra low level of long term yields as a relatively benign factor. To be sure, portfolio preferences may play a role in keeping yields low. But, we believe the main factor is the depressed state of advanced economies — reflected in the high level of private savings, weak credit demand, central bank balance sheet expansion measures and the prospect of a long period of ultra-low policy rates in the US, Europe and Japan — plus EMU worries. In our view, the low level of core yields is mainly driven by economic weakness and policy measures aimed at overcoming such weakness. It is the economic factors that cause low longterm yields which are a problem, not the low level of yields itself. At the margin, such low yields help support risk assets: indeed, this is a key rationale for recent central bank balance sheet expansion measures. Far from being a problem, ultra-low core yields are part of the solution to the current sluggish pace of advanced country economic growth.

Figure 11. Selected Countries — Industrial Production Forecasts (Pct.), 2011-13F

	2011	2012F	2013F
World	**3.7%**	**3.2%**	**3.7%**
United States	4.1	3.6	3.2
Japan	-3.5	5.6	3.4
Euro Area	3.6	-2.2	0.0
United Kingdom	-1.2	-0.9	1.3
Canada	3.5	-0.1	0.6
China	13.9	11.8	12.1
India	3.9	5.0	6.1
Korea	6.9	6.7	7.9
Brazil	0.3	0.5	3.0

Source: Citi Investment Research and Analysis

[7] See IMF Financial Stability Report, April 2012.

Figure 12. Selected Countries — Economic Forecast Overview (Percent), 2011-2016F

	GDP Growth						CPI Inflation						Short-Term Interest Rates					
	2011	2012F	2013F	2014F	2015F	2016F	2011	2012F	2013F	2014F	2015F	2016F	2011	2012F	2013F	2014F	2015F	2016F
Global	**3.0**	**2.6**	**3.0**	**3.5**	**3.8**	**4.1**	**3.7**	**3.1**	**3.0**	**3.0**	**3.0**	**3.0**	**2.52**	**3.75**	**3.98**	**2.70**	**3.04**	**3.45**
Based on PPP weights	*3.7*	*3.1*	*3.5*	*3.9*	*4.1*	*4.3*	*4.2*	*3.5*	*3.4*	*3.3*	*3.3*	*3.3*						
Industrial Countries	**1.3**	**1.0**	**1.3**	**2.0**	**2.3**	**2.7**	**2.3**	**1.9**	**1.6**	**1.5**	**1.6**	**1.6**	**0.76**	**0.68**	**0.61**	**0.69**	**1.08**	**1.66**
United States	**1.7**	**2.1**	**2.0**	**3.0**	**3.5**	**4.0**	**2.5**	**2.1**	**1.8**	**2.1**	**2.2**	**2.2**	**0.25**	**0.25**	**0.25**	**0.40**	**1.15**	**2.10**
Japan	**-0.7**	**2.0**	**1.6**	**1.5**	**1.5**	**1.2**	**-0.3**	**0.1**	**0.2**	**0.3**	**0.4**	**0.5**	**0.10**	**0.10**	**0.10**	**0.13**	**0.48**	**0.75**
Euro Area	1.5	-1.0	-0.2	0.8	1.2	1.7	2.7	2.8	1.9	1.3	1.1	1.2	1.19	1.00	0.63	0.50	0.50	0.75
Canada	2.5	2.0	2.3	2.8	3.2	3.6	2.9	2.1	1.8	2.0	2.0	2.0	1.00	1.00	1.63	2.19	2.50	3.00
Australia	2.0	3.4	3.9	4.3	3.8	3.6	3.4	2.6	3.4	2.9	2.7	2.5	4.63	4.06	4.44	5.00	5.25	5.75
New Zealand	1.3	1.8	2.3	3.0	3.2	3.4	4.0	1.6	2.4	2.6	2.9	2.8	2.50	2.50	3.69	4.75	5.50	5.50
Germany	3.1	0.9	1.6	1.5	1.8	1.7	2.3	2.2	2.3	2.3	2.2	2.2						
France	1.7	0.1	0.5	1.1	1.5	1.9	2.3	2.5	1.6	1.3	1.8	1.6						
Italy	0.4	-2.2	-0.9	0.4	0.7	1.8	2.9	3.6	2.0	0.2	0.0	0.9						
Spain	0.7	-2.7	-1.3	0.9	0.9	1.4	3.1	2.0	1.7	0.8	0.7	1.1						
Greece	-6.9	-6.5	-2.4	1.0	2.1	2.0	3.1	1.3	-0.3	0.2	1.0	1.1						
Ireland	0.7	-0.8	0.3	2.3	2.9	3.4	-0.4	0.2	0.0	0.3	0.5	0.5						
Portugal	-1.6	-5.4	-3.0	0.4	1.3	1.2	3.6	3.1	2.0	0.7	0.2	0.4						
Netherlands	1.3	-1.5	0.4	1.2	1.5	1.5	2.3	2.6	1.8	1.6	1.9	1.8						
Belgium	1.9	0.0	1.1	1.7	2.1	1.8	3.5	2.9	1.7	1.9	2.3	2.3						
Denmark	1.1	0.7	1.2	1.4	1.6	1.8	2.7	2.0	1.5	1.5	1.6	1.8	1.30	0.60	0.43	0.55	0.60	1.00
Norway	2.7	2.5	2.9	2.7	2.7	2.9	1.3	1.7	2.0	2.0	2.0	2.3	2.10	1.50	1.60	1.90	2.40	2.90
Sweden	4.0	0.7	1.9	2.6	2.7	2.7	2.9	1.2	1.9	1.9	2.1	2.0	1.80	1.20	1.10	1.60	2.10	2.50
Switzerland	1.9	0.7	0.9	1.5	1.6	1.6	0.2	-1.2	-1.3	-0.9	0.5	0.8	0.44	0.00	0.00	0.00	0.00	0.00
United Kingdom	0.6	0.2	1.0	1.5	2.2	3.2	4.5	2.8	2.0	1.9	1.7	1.7	0.50	0.50	0.50	0.50	1.04	2.04
Emerging Markets	**6.1**	**5.2**	**5.8**	**5.8**	**5.9**	**5.9**	**6.1**	**5.1**	**5.1**	**5.1**	**5.1**	**4.9**	**5.69**	**8.84**	**9.32**	**5.73**	**5.84**	**5.88**
China	**9.2**	**8.4**	**8.6**	**7.7**	**7.6**	**7.5**	**5.4**	**3.5**	**3.5**	**4.5**	**5.0**	**4.5**	**3.22**	**3.50**	**3.63**	**4.13**	**4.75**	**5.00**
Taiwan	4.0	3.5	4.2	4.5	4.5	4.5	1.4	1.9	2.1	1.8	1.8	1.8	0.70	0.87	1.08	1.25	1.50	1.75
India	6.9	7.0	7.5	8.2	8.3	8.5	9.0	7.0	6.5	6.0	6.0	6.0	8.20	7.80	7.50	7.50	7.50	7.50
Indonesia	6.5	6.2	6.5	6.7	6.9	6.7	5.4	5.8	5.3	4.6	5.5	5.3	5.43	3.75	3.75	4.00	4.13	4.63
Korea	3.6	3.7	4.4	3.7	4.0	4.2	4.0	3.1	3.4	3.1	3.0	3.2	3.19	3.25	3.81	4.25	4.63	4.88
Czech Republic	1.7	-0.4	1.6	2.8	3.6	3.7	1.9	3.3	2.8	2.2	2.0	1.6	0.75	0.75	0.85	1.33	1.65	2.50
Hungary	1.7	0.0	1.4	2.1	2.0	1.8	3.9	5.6	3.5	3.5	3.1	3.3	6.04	6.98	6.35	6.00	5.94	5.02
Poland	4.3	2.7	2.4	3.1	3.4	3.4	4.3	3.9	2.7	2.5	2.5	2.5	4.22	4.50	4.08	4.35	4.75	4.75
Romania	2.5	1.7	3.2	4.2	4.3	4.3	5.8	2.8	2.7	2.5	2.5	2.5	6.19	5.06	5.00	5.00	5.00	5.00
Russia	4.3	3.5	4.0	4.0	4.0	4.1	8.4	5.3	7.0	5.8	5.5	5.0	8.12	7.81	6.85	6.00	5.96	5.42
Turkey	8.5	2.5	4.3	4.9	4.6	4.6	6.5	9.6	7.0	6.0	5.9	5.4	6.00	5.75	6.31	8.00	7.56	7.50
Nigeria	7.8	7.4	7.0	7.2	6.9	7.2	10.8	12.2	10.0	10.3	9.5	9.0	8.90	15.00	12.50	10.50	10.00	9.50
South Africa	3.1	2.9	3.8	4.4	4.4	4.5	5.0	6.0	5.4	5.3	5.4	5.5	5.50	5.75	7.25	8.00	8.00	8.00
Argentina	8.9	3.0	3.0	2.0	2.0	3.5	9.8	9.6	12.2	15.0	15.0	16.5	18.37	13.46	17.71	16.00	14.00	13.00
Brazil	2.7	3.3	4.5	4.5	4.5	4.5	6.6	5.2	5.4	4.5	4.0	4.0	11.71	9.31	10.29	10.00	9.00	8.25
Mexico	3.9	3.5	3.6	3.6	3.8	3.7	3.4	4.1	3.7	3.9	3.8	3.7	4.50	4.13	4.40	5.29	6.00	6.25
Venezuela	4.2	4.0	3.4	4.0	3.0	2.5	27.1	26.1	28.6	32.9	30.7	30.7	13.30	14.40	14.40	13.00	12.90	12.70

Note: For inflation, we use the PCE deflator in the US, wholesale price index in India, GDP deflator in Ireland. For Indonesia we refer to the FasB1 rate to reflect actual money market rates. Source: CIRA.

Figure 13. Selected Countries — Economic Forecast Overview (Percent), 2011-2016F

	Current Balance (Pct of GDP)						Fiscal Balance (Pct of GDP)						Government Debt (Pct of GDP)					
	2011	**2012F**	**2013F**	**2014F**	**2015F**	**2016F**	**2011**	**2012F**	**2013F**	**2014F**	**2015F**	**2016F**	**2011**	**2012F**	**2013F**	**2014F**	**2015F**	**2016F**
Global	**0.3**	**0.1**	**0.2**	**0.1**	**0.1**	**0.2**	**-4.9**	**-4.2**	**-3.3**	**-2.7**	**-2.4**	**-2.1**	**80**	**82**	**83**	**82**	**81**	**79**
Based on PPP weights	*0.6*	*0.3*	*0.3*	*0.0*	*0.1*	*0.1*	*-4.3*	*-3.9*	*-3.1*	*-2.6*	*-2.3*	*-2.2*						
Industrial Countries	**-0.8**	**-0.8**	**-0.7**	**-0.5**	**-0.3**	**-0.3**	**-6.9**	**-5.7**	**-4.4**	**-3.6**	**-3.0**	**-2.6**	**105**	**110**	**114**	**115**	**115**	**115**
United States	**-3.1**	**-3.3**	**-3.2**	**-2.9**	**-3.0**	**-3.0**	**-9.4**	**-7.8**	**-5.9**	**-4.6**	**-4.0**	**-4.0**	**98**	**104**	**106**	**108**	**108**	**108**
Japan	**2.1**	**1.3**	**1.9**	**2.0**	**2.0**	**2.0**	**-10.7**	**-10.8**	**-8.4**	**-8.2**	**-7.8**	**-7.4**	**228**	**236**	**243**	**247**	**252**	**255**
Euro Area	**-0.3**	**-0.3**	**-0.3**	**-0.1**	**0.1**	**0.2**	**-4.1**	**-3.3**	**-2.4**	**-1.8**	**-1.1**	**-0.4**	**88**	**94**	**97**	**97**	**95**	**93**
Canada	-2.8	-1.5	-1.6	-1.9	-1.8	-1.5	-1.4	-1.2	-0.5	-0.1	0.2	0.4	79	78	77	77	75	73
Australia	-2.3	-2.9	-5.0	-4.9	-3.5	-3.2	-3.4	-1.8	0.2	0.3	1.2	1.7	6	7	7	6	6	5
New Zealand	-4.0	-5.2	-7.6	-6.9	-5.8	-5.5	-8.0	-6.0	-3.0	-0.9	0.2	0.9	21	27	30	30	30	29
Germany	5.8	5.0	4.4	4.7	4.8	5.1	-1.0	-0.6	-0.3	-0.1	0.4	0.8	81	81	80	78	75	72
France	-2.3	-2.0	-1.1	-0.4	0.2	0.4	-5.2	-4.4	-3.4	-2.2	-1.0	-0.3	85	91	95	96	94	91
Italy	-3.2	-2.8	-2.4	-2.1	-1.9	-1.6	-3.9	-2.6	-1.7	-1.6	-1.0	0.2	121	129	132	132	132	129
Spain	-3.5	-2.8	-2.2	-1.8	-1.6	-1.4	-8.5	-6.3	-5.3	-4.3	-3.7	-2.6	72	84	92	95	97	97
Greece	-9.6	-8.5	-7.5	-6.7	-5.6	-5.3	-9.3	-7.4	-6.2	-4.3	-3.5	-3.2	165	164	177	181	180	176
Ireland	0.1	4.2	4.2	7.1	9.3	11.6	-9.8	-9.6	-9.7	-7.7	-6.2	-6.1	105	117	127	131	132	133
Portugal	-8.1	-5.0	-2.9	-2.0	-1.8	-1.3	-4.0	-5.8	-3.5	-2.4	-2.1	-2.0	106	119	103	106	108	109
Netherlands	9.0	10.0	9.5	8.5	7.5	7.1	-4.7	-4.5	-3.5	-2.3	-1.5	-1.0	65	70	73	73	73	71
Belgium	-0.8	-0.2	0.3	1.0	2.0	2.4	-3.7	-2.9	-1.7	-1.0	-0.3	0.1	97	110	115	112	108	104
Denmark	6.5	5.4	5.2	3.7	3.3	3.5	-2.5	-5.2	-3.9	-2.6	-2.1	1.0	45	49	52	53	54	51
Norway	14.0	14.3	14.9	15.2	15.8	16.5	12.0	12.5	13.5	15.0	17.0	18.5	NA	NA	NA	NA	NA	NA
Sweden	7.2	7.5	7.8	6.7	6.9	7.3	0.1	-0.4	-0.2	0.5	1.5	1.9	37	37	36	34	31	27
Switzerland	15.0	13.8	14.0	14.2	14.7	15.7	0.6	0.2	-0.2	0.0	-0.1	-0.2	53	52	51	51	51	51
United Kingdom	-1.9	-1.6	0.2	1.1	1.7	2.0	-8.3	-6.5	-7.4	-6.6	-5.8	-4.5	83	88	94	99	102	103
Emerging Markets	**2.3**	**1.8**	**1.6**	**0.9**	**0.8**	**0.8**	**-1.5**	**-1.7**	**-1.6**	**-1.4**	**-1.5**	**-1.6**	**34**	**34**	**33**	**33**	**32**	**31**
China	**2.8**	**2.0**	**1.5**	**1.0**	**1.0**	**1.0**	**-1.3**	**-2.0**	**-1.5**	**-1.0**	**-1.0**	**-1.0**	**15**	**16**	**15**	**15**	**14**	**13**
Taiwan	8.8	8.7	8.4	8.0	8.0	8.0	-1.9	-1.6	-1.3	-1.0	-0.7	-0.7	39	39	40	42	43	44
India	-4.0	-4.0	-3.3	-2.7	-2.4	-1.9	-8.4	-8.0	-7.7	-7.0	-6.5	-6.0	69	69	68	66	64	63
Indonesia	0.2	-0.7	-0.8	-1.1	-1.0	-0.9	-1.2	-1.8	-0.7	-0.3	-0.5	-0.5	26	25	24	23	23	22
Korea	2.5	1.1	0.7	0.6	-0.3	-0.3	1.5	1.4	1.2	1.6	1.4	2.1	33	33	32	30	28	26
Czech Republic	-2.9	-3.8	-2.5	-2.8	-2.9	-2.2	-3.1	-3.1	-2.8	-2.3	-1.5	-0.5	41	44	45	44	43	40
Hungary	1.7	1.2	1.5	2.0	2.2	2.1	4.2	-3.2	-3.0	-3.3	-2.9	-2.7	81	78	78	77	77	77
Poland	-4.1	-3.7	-3.9	-5.1	-5.3	-4.9	-5.1	-3.3	-2.7	-1.9	-1.7	-1.7	54	53	52	50	49	48
Romania	-4.2	-4.5	-4.7	-5.0	-5.0	-5.0	-4.1	-2.0	-2.0	-2.5	-2.3	-2.0	39	39	39	39	38	37
Russia	5.2	5.2	2.1	-1.0	-1.0	-1.0	2.0	0.3	0.1	-0.1	-1.1	-1.1	8	8	8	8	8	8
Turkey	-10.0	-8.5	-8.3	-7.5	-6.8	-6.0	-1.3	-2.2	-2.5	-2.5	-2.7	-3.0	41	41	39	39	38	36
Nigeria	5.9	5.2	6.0	4.6	3.7	3.1	-3.0	-2.1	-2.0	-2.4	-2.8	-2.3	NA	NA	NA	NA	NA	NA
South Africa	-3.4	-4.7	-5.6	-6.6	-6.3	-5.8	-5.0	-4.8	-4.2	-3.6	-3.5	-3.5	38	41	42	43	43	42
Argentina	0.4	0.3	0.2	-0.5	-0.5	-0.5	-1.6	-3.0	-3.0	-1.3	-0.6	0.1	49	49	49	52	53	53
Brazil	-2.1	-2.1	-2.4	-2.7	-3.0	-3.3	-2.6	-1.9	-2.6	-2.4	-2.2	-2.5	63	63	63	64	64	65
Mexico	-0.8	-1.6	-1.9	-2.5	-2.4	-2.6	-2.5	-2.2	-2.0	-1.9	-1.9	-1.8	40	40	38	38	38	37
Venezuela	9.1	6.9	8.4	7.3	7.9	7.6	-5.0	-5.0	-4.0	-5.2	-5.0	-4.8	43	36	36	37	37	38

Note: Fiscal deficit and debt figures for all countries are general government debt and deficits. We assume sovereign debt restructuring in Portugal in 2012-13. Source: Citi Investment Research and Analysis

Figure 14. Selected Countries — Changes in Economic Forecast from the Previous Month (Percentage Points), 2011-2013F

	GDP Growth			CPI Inflation			Current Balance (Pct of GDP)			Fiscal Balance (Pct of GDP)		
	2011	2012F	2013F	2011	2012F	2013F	2011	2012F	2013F	2011	2012F	2013F
Global		**0.1**						**-0.1**	**-0.1**	**0.1**	**0.1**	
Based on PPP weights									*-0.1*	*0.1*		
Industrial Countries		**0.2**	**0.1**					**-0.1**	**-0.1**		**0.1**	**0.1**
United States								**-0.3**	**-0.3**			
Japan		**0.5**	**0.2**		**0.1**			**-0.3**	**-0.3**		**0.1**	**0.1**
Euro Area		**0.2**			**0.3**					**0.1**	**0.1**	**0.2**
Canada								0.2	0.2	0.4	0.3	0.4
Australia												
New Zealand	-0.2	0.5										
Germany						0.1		-0.2	-0.5		0.4	0.7
France		0.4			-0.3					0.3	0.1	
Italy		0.1	-0.5		0.5	0.3		-0.1	-0.2			-0.3
Spain			-0.1		-0.3	-0.1	0.2	0.2	0.1		0.3	-1.3
Greece									-0.1	-0.1	-1.0	-2.5
Ireland	-0.1	-0.5	0.3	0.4			-0.5	1.4	0.7	0.2		0.1
Portugal		-0.1				-0.2					-1.1	1.4
Netherlands			0.1				0.9	2.7	2.2	0.2		0.3
Belgium		0.3	0.3				-0.1	1.8	1.6		-0.1	0.2
Denmark												
Norway												
Sweden												
Switzerland		0.6				0.4		0.2	0.3		0.2	0.3
United Kingdom	-0.3		0.1		0.4	0.1	0.7		0.4	0.2	0.2	0.4
Emerging Markets		**-0.1**	**-0.1**			**-0.1**	**0.1**	**0.3**	**-0.1**			**-0.1**
China					**0.2**	**-0.2**						
Taiwan		-0.2			0.5	0.4					0.4	0.5
India							-0.5	-0.4	-0.1	-0.4	-0.3	-0.2
Indonesia											-0.3	
Korea					-0.2	0.1			-0.3	1.1		
Czech Republic			-0.2		-0.1	0.2		-0.2	0.9	0.6	0.6	0.3
Hungary							0.2	-0.2	-0.1	0.7		
Poland				0.1	0.1	0.1		-0.5	0.1			
Romania			0.1		0.2	0.7	-0.1			0.3		
Russia					-0.2	0.2	-0.3	2.0	1.5	1.2	0.6	0.6
Turkey	0.3				0.1		0.2	-0.1	-0.4			
Nigeria	0.7	0.7	0.5		1.3	-0.4		-0.1		0.2	0.7	
South Africa												
Argentina	-0.3	-1.0	-2.0								-1.0	-1.0
Brazil					-0.3	-0.1						
Mexico		0.2	0.1									
Venezuela					-1.4	-1.9		0.1	0.3			

Source: Citi Investment Research and Analysis

Figure 15. Selected Countries — Economic Forecast Overview and Exchange Rate Forecasts (Percent), 2011-2016F

	10-Year Yields						Exchange Rates Versus U.S. Dollar*						Exchange Rate Versus Euro					
	2011	2012F	2013F	2014F	2015F	2016F	2011	2012F	2013F	2014F	2015F	2016F	2011	2012F	2013F	2014F	2015F	2016F
Industrial Countries																		
United States	**2.80**	**2.25**	**2.75**	**3.10**	**3.35**	**3.75**	**NA**	**NA**	**NA**	**NA**	**NA**	**NA**	**1.39**	**1.30**	**1.27**	**1.31**	**1.33**	**1.35**
Japan	**1.12**	**1.03**	**1.40**	**1.50**	**1.75**	**1.75**	**79**	**81**	**82**	**85**	**85**	**85**	**110**	**105**	**104**	**111**	**113**	**115**
Euro Area	**2.71**	**1.75**	**2.10**	**2.50**	**2.75**	**3.00**	**1.39**	**1.30**	**1.27**	**1.31**	**1.33**	**1.35**	**NA**	**NA**	**NA**	**NA**	**NA**	**NA**
Canada	2.78	2.36	3.11	3.50	3.45	3.75	1.01	0.99	0.97	0.97	0.97	0.97	1.39	1.28	1.23	1.27	1.29	1.31
Australia	4.63	4.31	5.00	5.25	5.50	6.00	1.01	1.02	0.97	0.90	0.89	0.88	1.37	1.27	1.31	1.46	1.50	1.55
New Zealand	4.74	4.26	5.10	5.30	5.70	6.30	0.77	0.81	0.73	0.63	0.63	0.62	1.79	1.60	1.74	2.07	2.12	2.17
Germany	2.71	1.77	2.10	2.50	2.75	3.00												
France	3.31	3.12	3.10	3.20	3.35	3.50												
Italy	5.19	5.67	4.87	4.90	4.95	4.70												
Spain	5.43	5.70	4.87	4.80	4.75	4.50												
Netherlands	3.04	2.30	2.54	2.80	3.00	3.25												
Belgium	4.21	3.58	3.32	3.40	3.55	3.70												
Denmark	2.80	1.70	2.10	2.60	2.95	3.25												
Norway	3.07	2.20	2.55	3.10	3.45	3.75	5.66	5.82	5.92	5.73	5.63	5.53	7.84	7.55	7.50	7.50	7.49	7.48
Sweden	2.66	1.66	2.03	2.55	2.85	3.25	6.60	6.80	6.87	6.61	6.49	6.37	9.14	8.82	8.72	8.65	8.63	8.62
Switzerland	1.53	0.80	1.15	1.55	1.60	1.80	0.90	0.93	0.97	0.96	0.97	0.98	1.25	1.20	1.22	1.26	1.29	1.32
United Kingdom	3.00	2.10	2.50	3.00	3.35	3.65	1.59	1.57	1.57	1.65	1.68	1.71	0.87	0.83	0.81	0.79	0.79	0.79
Emerging Markets																		
China	**3.52**	**3.17**	**3.42**	**3.80**	**4.42**	**4.67**	**6.46**	**6.28**	**6.18**	**6.10**	**6.07**	**6.04**	**8.45**	**8.15**	**7.84**	**7.98**	**8.07**	**8.17**
Taiwan	1.38	1.35	1.50	1.60	1.70	1.80	29.47	29.44	28.60	28.37	28.85	29.33	38.53	38.20	36.27	37.10	38.37	39.68
India	8.40	8.25	8.25	8.25	8.25	8.25	49.19	52.88	52.95	50.91	50.55	50.22	64.30	68.61	67.14	66.56	67.24	67.93
Indonesia	7.20	5.98	5.75	6.00	6.25	6.50	8768	9317	9333	9283	9233	9183	11462	12088	11835	12137	12281	12421
Korea	3.90	3.88	4.39	4.88	5.40	5.70	1108	1136	1065	982	984	988	1449	1474	1351	1284	1309	1336
Czech Republic	3.68	3.34	3.20	3.42	3.82	4.00	17.7	19.1	19.5	18.2	17.4	16.6	23.1	24.7	24.8	23.8	23.2	22.5
Hungary	7.63	8.46	8.00	7.74	7.52	6.99	201	227	226	221	215	209	263	294	287	289	286	282
Poland	NA	NA	NA	NA	NA	NA	2.96	3.19	3.19	2.98	2.93	2.88	3.87	4.14	4.04	3.90	3.90	3.90
Romania	NA	NA	NA	NA	NA	NA	3.05	3.27	3.38	3.14	3.00	2.86	3.98	4.24	4.29	4.10	3.98	3.87
Russia	NA	NA	NA	NA	NA	NA	29.4	30.2	32.1	31.9	31.2	30.6	38.4	39.2	40.7	41.7	41.6	41.3
Turkey	NA	NA	NA	NA	NA	NA	1.89	1.78	1.84	1.80	1.73	1.66	2.46	2.31	2.33	2.35	2.30	2.24
Nigeria	NA	NA	NA	NA	NA	NA	156	160	165	163	165	164	204	208	209	213	219	222
South Africa	8.24	8.25	8.90	9.15	9.20	9.20	7.26	8.06	8.61	9.11	9.42	9.74	9.49	10.45	10.91	11.90	12.54	13.18
Argentina	NA	NA	NA	NA	NA	NA	4.13	4.55	5.45	6.79	7.54	8.36	5.39	5.91	6.91	8.88	10.02	11.31
Brazil	11.45	10.71	10.77	9.88	8.75	8.25	1.67	1.82	1.75	1.71	1.74	1.78	2.18	2.36	2.21	2.24	2.32	2.41
Mexico	6.87	6.52	7.50	8.10	8.00	8.00	12.5	12.9	12.4	12.3	12.6	12.8	16.3	16.8	15.7	16.1	16.7	17.3
Venezuela	13.65	12.54	12.73	13.90	13.80	13.70	4.30	4.30	6.50	6.50	9.75	9.75	5.60	5.53	8.26	8.51	12.99	13.21

*Per USD except Euro Area, Australia, New Zealand, United Kingdom. Note: All foreign exchange forecasts are consistent with the rolling forecasts presented in Figure 86. Source: Citi Investment Research and Analysis

Figure 16. Short Rates (End of Period), as of 18 Apr 2012 (Percent)

	Current	2Q 12	3Q 12	4Q 12	1Q 13	2Q 13	3Q 13
United States	**0.25**	**0.25**	**0.25**	**0.25**	**0.25**	**0.25**	**0.25**
Japan	**0.10**	**0.10**	**0.10**	**0.10**	**0.10**	**0.10**	**0.10**
Euro Area	**1.00**	**1.00**	**1.00**	**1.00**	**0.75**	**0.75**	**0.50**
Canada	1.00	1.00	1.00	1.00	1.25	1.50	1.75
Australia	4.25	4.00	4.00	4.00	4.25	4.50	4.50
New Zealand	2.50	2.50	2.50	2.50	3.00	3.50	4.00
Denmark	0.70	0.70	0.60	0.60	0.35	0.35	0.10
Norway	1.50	1.50	1.50	1.50	1.50	1.50	1.50
Sweden	1.50	1.50	1.25	1.00	1.00	1.00	1.00
Switzerland	0.00	0.00	0.00	0.00	0.00	0.00	0.00
United Kingdom	0.50	0.50	0.50	0.50	0.50	0.50	0.50
China	**3.50**	**3.50**	**3.50**	**3.50**	**3.75**	**3.75**	**3.75**

Note: The rates shown are overnight rates, except for Denmark, where it is the central bank's lending rate; Switzerland, where it is the SNBs three-month LIBOR target; and China, where it is the one-year deposit rate. Source: Citi Investment Research and Analysis

Figure 17. 10-Year Yield Forecasts (Period Average), as of 18 Apr 2012 (Percent)

	Current	2Q 12	3Q 12	4Q 12	1Q 13	2Q 13	3Q 13
United States	**2.01**	**2.25**	**2.35**	**2.45**	**2.55**	**2.65**	**2.85**
Japan	**0.95**	**0.95**	**1.00**	**1.20**	**1.30**	**1.40**	**1.40**
Euro area (Germany)	**1.75**	**1.75**	**1.70**	**1.75**	**1.80**	**2.00**	**2.25**
Canada	2.08	2.30	2.40	2.50	2.85	3.05	3.25
Australia	3.88	4.20	4.30	4.50	4.80	5.00	5.10
New Zealand	4.01	4.10	4.25	4.50	4.70	4.90	5.10
Denmark	1.72	1.71	1.65	1.70	1.75	1.95	2.25
Norway	2.29	2.18	2.13	2.20	2.30	2.50	2.80
Sweden	1.81	1.69	1.60	1.65	1.70	1.90	2.15
Switzerland	0.77	0.80	0.75	0.80	0.85	1.05	1.30
United Kingdom	2.08	2.10	2.10	2.15	2.20	2.40	2.65

Note: Bond yields measured on local market basis (semi-annual for the United States, United Kingdom, Canada, Australia, and New Zealand; annual for the rest). The 10-year yield for the euro area is the Bund yield. Source: Citi Investment Research and Analysis

Figure 18. 10-Year Yield Spreads (Period Average), as of 18 Apr 2012

	Spread vs. US$						Spread vs. Germany					
	Current	2Q 12	3Q 12	4Q 12	1Q 13	2Q 13	Current	2Q 12	3Q 12	4Q 12	1Q 13	2Q 13
United States	**NA**	**NA**	**NA**	**NA**	**NA**	**NA**	**27**	**51**	**66**	**72**	**77**	**67**
Japan	**-107**	**-131**	**-136**	**-127**	**-127**	**-127**	**-80**	**-80**	**-70**	**-55**	**-50**	**-60**
Euro Area	**-27**	**-51**	**-66**	**-72**	**-77**	**-67**	**NA**	**NA**	**NA**	**NA**	**NA**	**NA**
Canada	7	5	5	5	30	41	34	56	71	77	107	107
Australia	190	198	198	209	229	239	217	249	265	280	306	306
New Zealand	203	188	193	209	219	229	230	239	260	280	296	296
France	101	99	74	58	33	33	127	150	140	130	110	100
Italy	347	379	364	248	223	213	373	430	430	320	300	280
Spain	388	419	374	258	223	213	414	470	440	330	300	280
Netherlands	24	9	-11	-17	-27	-22	50	60	55	55	50	45
Belgium	154	139	114	88	63	53	180	190	180	160	140	120
Denmark	-29	-55	-71	-77	-82	-72	-3	-4	-5	-5	-5	-5
Norway	27	-8	-23	-27	-27	-17	54	43	43	45	50	50
Sweden	-20	-57	-76	-82	-87	-77	6	-6	-10	-10	-10	-10
Switzerland	-124	-146	-161	-167	-172	-162	-111	-95	-95	-95	-95	-95
United Kingdom	7	-16	-26	-32	-37	-27	33	35	40	40	40	40

NA Not applicable. Note: Spreads calculated on annual basis (except those of the United Kingdom, Canada, Australia and New Zealand over the United States).
Source: Citi Investment Research and Analysis

Figure 19. Emerging Market Countries — Short Rates Actual and Forecast of Additional Rate Moves (End of Period), as of 18 Apr 2012

Country	Current Rate (%)	Jun 12	Sep 12	Dec 12	Mar 13	Jun 13	Total Cumulative Rate Moves Expected
South Africa	5.50	0	50	50	50	0	150
Brazil	9.75	-75	0	0	100	50	75
Korea	3.25	0	0	0	25	25	50
Thailand	3.00	0	0	0	25	25	50
Philippines	4.00	0	0	0	25	25	50
Israel	2.50	0	0	0	25	0	25
China	3.50	0	0	0	25	0	25
Turkey	5.75	0	0	0	0	0	0
Indonesia	5.75	0	0	0	0	0	0
Mexico	4.50	-50	0	0	25	25	0
Czech	0.75	0	0	0	0	0	0
Chile	5.00	0	-25	-25	0	25	-25
Romania	5.25	-25	0	0	0	0	-25
Poland	4.50	0	0	0	-25	-25	-50
Hungary	7.00	0	0	-25	-25	0	-50
India	8.00	0	-25	0	0	-50	-75
Russia	8.00	-25	0	0	-50	-50	-125

Source: Citi Investment Research and Analysis

Figure 20. Foreign Exchange Forecasts (End of Period), as of 18 Apr 2012

	vs. USD						vs. EUR					
	Current	Jun 12	Sep 12	Dec 12	Mar 13	Jun 13	Current	Jun 12	Sep 12	Dec 12	Mar 13	Jun 13
United States	**NA**	**NA**	**NA**	**NA**	**NA**	**NA**	**1.31**	**1.30**	**1.29**	**1.27**	**1.25**	**1.26**
Japan	**81**	**81**	**81**	**80**	**80**	**81**	**106**	**105**	**104**	**102**	**100**	**102**
Euro Area	**1.31**	**1.30**	**1.29**	**1.27**	**1.25**	**1.26**	**NA**	**NA**	**NA**	**NA**	**NA**	**NA**
Canada	1.00	0.99	0.99	0.98	0.98	0.97	1.30	1.29	1.27	1.24	1.22	1.23
Australia	1.04	1.03	1.02	1.01	1.00	0.98	1.26	1.26	1.26	1.25	1.25	1.29
New Zealand	0.82	0.82	0.81	0.80	0.78	0.75	1.59	1.59	1.59	1.60	1.60	1.69
Norway	5.80	5.81	5.86	5.93	5.99	5.95	7.58	7.55	7.54	7.52	7.50	7.50
Sweden	6.79	6.80	6.86	6.93	6.99	6.92	8.87	8.85	8.82	8.79	8.75	8.73
Switzerland	0.92	0.92	0.94	0.95	0.97	0.97	1.20	1.20	1.20	1.21	1.21	1.22
United Kingdom	1.59	1.57	1.56	1.55	1.54	1.56	0.82	0.83	0.83	0.82	0.82	0.81
China	**6.30**	**6.31**	**6.28**	**6.25**	**6.22**	**6.20**	**8.20**	**8.20**	**8.10**	**7.90**	**7.80**	**7.80**
India	51.3	53.2	53.6	53.8	54.0	53.4	67.1	69.2	69.0	68.3	67.6	67.3
Korea	1135	1148	1138	1125	1112	1082	1484	1493	1464	1427	1393	1364
Poland	3.20	3.19	3.22	3.26	3.29	3.23	4.18	4.15	4.14	4.13	4.12	4.07
Russia	29.6	29.8	30.5	31.2	32.0	32.1	38.7	38.7	39.2	39.6	40.1	40.5
South Africa	7.95	8.08	8.19	8.29	8.39	8.53	10.39	10.51	10.52	10.51	10.50	10.75
Turkey	1.80	1.76	1.78	1.81	1.85	1.84	2.35	2.29	2.29	2.30	2.31	2.32
Brazil	1.84	1.84	1.82	1.80	1.77	1.76	2.40	2.39	2.34	2.28	2.22	2.21
Mexico	13.2	13.2	13.0	12.8	12.5	12.4	17.2	17.2	16.7	16.2	15.7	15.7

Note: All foreign exchange forecasts are consistent with the rolling forecasts presented in Figure 85. Source: Citi Investment Research and Analysis

Figure 21. Foreign Exchange Forecasts (End of Period), as of 18 Apr 2012

	vs. JPY					
	Current	Jun 12	Sep 12	Dec 12	Mar 13	Jun 13
United States	**81**	**81**	**81**	**80**	**80**	**81**
Japan	**NA**	**NA**	**NA**	**NA**	**NA**	**NA**
Euro Area	**106**	**105**	**104**	**102**	**100**	**102**
Canada	81	82	82	82	82	83
Australia	84	83	82	81	80	79
New Zealand	66.6	66.5	65.3	63.9	62.6	60.6
Norway	14.0	13.9	13.8	13.6	13.4	13.6
Sweden	11.9	11.9	11.8	11.6	11.5	11.7
Switzerland	88	88	86	85	83	84
United Kingdom	128	127	126	124	123	126
China	**13**	**13**	**13**	**13**	**13**	**13**
India	1.58	1.52	1.50	1.49	1.48	1.52
Korea	14.02	14.17	14.11	14.00	13.89	13.35
Poland	25.3	25.4	25.1	24.7	24.3	25.1
Russia	2.7	2.7	2.6	2.6	2.5	2.5
South Africa	10.2	10.0	9.9	9.7	9.5	9.5
Turkey	45.0	46.1	45.4	44.3	43.4	44.0
Brazil	44.0	44.0	44.4	44.7	45.1	46.2
Mexico	6.2	6.1	6.2	6.3	6.4	6.5

Note: All foreign exchange forecasts are consistent with the rolling forecasts presented in Figure 85. Source: Citi Investment Research and Analysis

Country Commentary

United States

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Economic activity appears to have advanced at a slightly better than expected pace since the start of the year, aided in part by a mild winter. But with much of the added output landing in inventories and final demand still modest, we expect a slower second quarter. Employment continues to rise and, along with supportive policies, has fostered perceptions that recovery is less vulnerable. The drags from housing and state and local retrenchment are also diminishing. Although some signs of a payback from weather-induced gains have surfaced, income and spending remain on a track consistent with 2% growth. The chance of major fiscal restraint looms as a key medium-term threat.

The Fed's two-pronged strategy of highly accommodating rate guidance and Operation Twist has been a notable success in anchoring interest rates. Officials have tempered market expectations for additional QE but the chance that growth could disappoint this year has kept alive the option for further asset purchases. Despite better hiring, policymakers have cautioned that unemployment remains too high and global threats to financial stability are unresolved. Broad tax hikes and spending cuts that could undermine growth are on tap for 2013 but forestalling action is unlikely before late this year or next.

Competitive pressures and economic slack have kept underlying inflation in check but rising gasoline prices have pushed up headline measures again. Fed officials continue to cite stable inflation expectations as a steadying factor. An improving job market may be just beginning to buoy wage growth.

Figure 22. United States — Economic Forecasts, 2011-2013F

					2011	2012F				2013F		
		2011	2012F	2013F	4Q	1QF	2QF	3QF	4QF	1QF	2QF	3QF
GDP	SAAR				3.0%	2.6%	1.2%	2.1%	2.3%	1.2%	1.5%	3.0%
	YoY	1.7%	2.1%	2.0%	1.6	2.2	2.1	2.2	2.0	1.7	1.8	2.0
Domestic Demand	SAAR				1.3	1.9	1.8	1.9	2.3	0.6	1.4	2.9
	YoY	1.9	1.9	1.8	1.4	1.8	1.9	1.7	2.0	1.7	1.5	1.8
Consumption	SAAR				2.1	2.4	2.0	2.0	2.4	1.1	1.6	2.7
	YoY	2.2	2.0	1.9	1.6	1.7	2.0	2.1	2.2	1.9	1.8	1.9
Business Investment	SAAR				5.2	1.0	4.4	5.5	5.8	6.4	5.3	6.2
	YoY	8.8	5.6	5.9	8.2	7.9	6.4	4.0	4.2	5.5	5.7	5.9
Housing Investment	SAAR				11.7	7.6	7.2	13.2	11.8	12.5	14.5	17.0
	YoY	-1.3	8.2	13.6	3.5	6.1	6.9	9.9	9.9	11.1	13.0	13.9
Government	SAAR				-4.1	-0.2	-1.6	-1.4	-1.4	-5.6	-3.4	-0.7
	YoY	-2.1	-1.5	-2.7	-2.8	-1.3	-1.5	-1.8	-1.2	-2.5	-3.0	-2.8
Exports	SAAR				2.7	4.6	5.2	5.2	5.7	5.9	5.6	5.6
	YoY	6.7	4.5	5.7	4.7	3.9	4.3	4.4	5.2	5.5	5.6	5.7
Imports	SAAR				3.7	3.9	3.5	3.5	4.0	2.6	3.5	4.2
	YoY	4.9	3.2	3.6	3.6	2.5	3.1	3.6	3.7	3.4	3.4	3.6
PCE Deflator	YoY	2.5	2.1	1.8	2.7	2.3	2.0	1.9	2.0	1.8	1.7	1.7
Core PCE Deflator	YoY	1.4	1.8	1.7	1.8	1.9	1.8	1.7	1.7	1.7	1.6	1.6
Unemployment Rate	%	9.0	8.0	7.8	8.7	8.3	8.1	8.0	7.8	7.9	7.9	7.8
Federal Gov't Balance (Fiscal Year)	$Bn	-1297	-1175	--875								
	% of GDP	-8.7	-7.6	-5.5								
General Gov't Balance (Cal Year)	% of GDP	-9.4	-7.8	-5.9								
Federal Debt	% of GDP	68	74	78								
General Gov't Debt	% of GDP	98	104	106								
Current Account	US$bn	-473	-524	-529	-496	-528	-533	-510	-526	-507	-526	-530
	% of GDP	-3.1	-3.3	-3.2	-3.2	-3.4	-3.4	-3.2	-3.3	-3.2	-3.3	-3.3
S&P 500 Profits (US$ Per Share)	YoY	14.4	3.3	4.5	8.9	5.5	4.6	-0.6	3.8	3.0	4.0	3.5

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

Japan

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We are revising up our 2012 growth forecast again, this time driven mainly by domestic demand, and now expect 2.0% growth, versus 1.5% in the March forecast. Consumer spending continues to surprise to the upside thanks to newly-introduced subsidies for eco-car purchases and a modest improvement in labour market conditions. Reconstruction demand from the earthquake is also materializing gradually. Meanwhile, exports remain range-bound so far, but there are emerging signs of a gradual pickup. We expect GDP growth to accelerate to an annual rate of mid-2% in the second half on average thanks to moderately faster global growth, reconstruction demand and resilience in consumer spending.

The BoJ left policy unchanged early April, but this intensified market expectation for additional easing at the April 27th meeting. With the BoJ's core inflation forecast for fiscal 2013, which will be published at the meeting, expected to fall short of its price stability goal of 1%, the view is strong that the BoJ will be forced to take additional measures to ensure that the price stability goal is accomplished. However, the BoJ Governor showed scepticism towards setting a rigid deadline (i.e. by fiscal 2013) for achieving the price stability goal by citing the examples of the BoE and Fed. There are some doubts over whether the BoJ will move again at the next meeting just because its CPI forecast falls short of 1%. Assuming that the BoJ takes additional action later this month, the most likely option is to increase the size of the asset purchase program, more concretely, JGB purchases. By extending the program by, say six months, the total size of JGB purchases would increase by ¥8-9trn.

Debates about the consumption tax hike are a key policy issue this year. Given significant uncertainties surrounding the tax hike, we have yet to reflect in our forecasts the government's plan to hike the tax rate to 8% in April 2014 and to 10% in October 2015. However, if the plan is implemented, GDP growth in 2013 will probably be pushed up by nearly 2% thanks to frontloaded demand ahead of price hikes but growth in 2014 will worsen due to a resulting decline in spending as well as a permanent negative impact on real household income.

Figure 23. Japan — Economic Forecasts, 2011-13F

					2011	2012F				2013F		
		2011	2012F	2013F	4Q	1QF	2QF	3QF	4QF	1QF	2QF	3QF
Real GDP	YoY	-0.7%	2.0%	1.6%	-0.6%	1.9%	2.4%	1.4%	2.2%	2.0%	2.0%	1.4%
	SAAR				-0.7	2.6	1.0	2.9	2.4	1.9	0.7	0.7
Domestic Demand	YoY	0.1	2.5	1.4	0.5	2.9	2.6	2.3	2.3	1.9	1.7	1.1
	SAAR				2.0	2.9	1.5	2.8	2.2	1.2	0.5	0.5
Private Consumption	YoY	0.0	1.7	0.8	0.6	2.5	2.0	1.3	1.3	0.8	0.8	0.8
	SAAR				1.4	2.9	-0.4	1.3	1.2	0.9	-0.2	1.3
Business Investment	YoY	1.0	3.6	3.4	4.5	4.0	4.5	5.0	1.0	3.0	3.6	3.5
	SAAR				20.7	-3.8	1.4	3.3	3.2	4.4	3.5	3.0
Housing Investment	YoY	5.1	5.2	6.4	2.9	1.1	6.8	4.0	8.8	11.9	8.4	5.7
Public Investment	YoY	-3.2	8.0	-3.8	0.2	6.1	4.5	9.4	12.0	6.0	-1.5	-9.0
Exports	YoY	0.0	1.2	4.5	-1.6	-1.2	5.8	-1.7	2.4	3.8	4.5	4.8
	SAAR				-11.8	0.8	1.3	3.5	4.0	6.2	4.3	4.5
Imports	YoY	5.8	4.7	3.0	5.8	5.4	6.4	3.7	3.4	3.1	2.7	2.8
	SAAR				4.3	2.5	5.1	3.1	2.8	1.6	3.3	3.7
CPI	YoY	-0.3	0.1	0.2	-0.3	-0.1	0.2	0.0	0.1	0.1	0.2	0.2
Core CPI	YoY	-0.3	0.1	0.2	-0.2	0.0	0.1	0.0	0.1	0.1	0.2	0.2
Nominal GDP	YoY	-2.8	0.9	1.4	-2.3	0.1	1.6	0.5	1.5	1.6	1.7	1.2
Current Account	¥ tn	9.6	6.4	9.2	6.8	6.6	5.4	6.3	7.2	8.7	9.2	9.3
	% of GDP	2.1	1.3	1.9	1.4	1.4	1.1	1.3	1.5	1.8	1.9	1.9
Unemployment Rate	%	4.6	4.5	4.4	4.5	4.5	4.5	4.5	4.4	4.4	4.4	4.4
Industrial Production	YoY	-3.5	5.6	3.4	-2.8	3.0	8.2	4.7	6.4	3.9	3.8	3.5
Corporate Profits (Fiscal Year)	YoY	-17.0	22.5	18.0								
General Govt. Balance (Fiscal Year)	% of GDP	-10.7	-10.8	-8.4								
General Govt Debt	% of GDP	228	236	243								

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 Investment Research and Analysis

Euro Area

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With indications of a somewhat smaller decline in 1Q GDP, we have revised up our GDP forecast for 2012 from -1.2% to -1.0%, a third consecutive upward revision. However, with extra austerity measures in the pipeline and the continuing deleveraging in the private sector, we expect the euro area to stay in recession. For 2013 we left our forecast unchanged at -0.2%. In the periphery countries particularly we expect a weaker economic performance. Consequently, budget deficits are likely to exceed the governments' targets. Partly due to high inflation at the beginning of the year and with additional indirect tax increases to come, we have also revised up our inflation forecast from 2.5% to 2.8% for 2012.

Recent developments in Spain are a powerful reminder that the sovereign debt crisis is far from being over. As we argued in the Focus on Spain, we expect that the country will need some IMF/EU support. While there has been an agreement on increasing the ESM/EFSF lending capacity and the IMF is likely to get more firepower as well, in our view, the facilities are still too small to be able to fully fund Spain and Italy if necessary. Furthermore, the upcoming elections in France and Greece are likely to get market attention and in our view the outcome of the Greek election is key regarding the country's EMU membership.

Given the limited capacity of support measures by the ESM/EFSF and the IMF, the ECB probably needs to make further contributions. While several ECB officials highlighted their willingness to take further measures, the ECB probably will wait until governments have taken extra action. In our view it looks more likely that the ECB provides additional multi-year LTROs rather than re-activating the SMP programme substantially. Regarding interest rates, with inflation rates – although mainly related to energy and indirect tax increases – clearly above the ECB's target of "below but close to 2%", a rate cut in 2012 looks less likely. However, with ongoing economic weakness ahead and some Council members already concerned about deflation, we expect the next ECB rate move to be a cut.

We publish further details of our European forecasts monthly in European Economic Forecast Highlights

Figure 24. Euro Area — Economic Forecasts, 2011-13F

					2011	2012F				2013F		
		2011	2012F	2013F	4Q	1QF	2QF	3QF	4QF	1QF	2QF	3QF
Real GDP	YoY	1.5%	-1.0%	-0.2%	0.7%	-0.5%	-1.0%	-1.3%	-1.1%	-0.6%	-0.4%	-0.1%
	SAAR				-1.3	-1.8	-1.1	-1.2	-0.6	0.0	-0.1	0.5
Final Domestic Demand	YoY	0.5	-1.6	-0.6	-0.3	-1.2	-1.4	-1.9	-1.8	-1.3	-0.8	-0.4
Private Consumption	YoY	0.2	-1.0	-0.3	-0.6	-1.0	-0.7	-1.3	-0.9	-0.6	-0.4	-0.2
Government Consumption	YoY	0.1	-2.0	-1.6	-0.3	-0.9	-1.8	-2.5	-2.9	-2.5	-1.8	-1.1
Fixed Investment	YoY	1.6	-2.8	-0.6	0.6	-2.2	-3.0	-3.2	-3.0	-1.9	-0.8	-0.3
— Business Equipment	YoY	3.3	-1.6	0.6	1.3	-0.8	-1.7	-2.2	-1.8	-0.9	0.4	0.8
— Construction	YoY	-0.3	-4.1	-1.2	-0.3	-3.9	-4.4	-4.2	-3.9	-2.6	-1.7	-0.7
Stocks (Contrib. to Y/Y GDP Growth)		0.0	-0.2	0.0	-0.2	-0.3	-0.3	-0.1	0.0	0.0	0.0	-0.1
Exports	YoY	6.3	1.7	3.9	3.6	2.2	1.7	1.0	2.0	3.1	3.5	4.2
Imports	YoY	4.0	0.0	3.1	0.6	-0.1	-0.4	-0.6	1.0	2.1	2.9	3.5
CPI	YoY	2.7	2.8	1.9	2.9	2.7	3.0	3.0	2.6	2.2	1.8	1.7
Core CPI	YoY	1.4	1.9	1.5	1.6	1.5	2.0	2.1	1.9	1.9	1.4	1.4
CPI Ex Energy and Food	YoY	1.7	2.1	1.6	2.0	1.9	2.4	2.2	2.0	1.9	1.6	1.5
Unemployment Rate	YoY	10.2	11.0	11.1	10.5	10.8	10.9	11.0	11.1	11.1	11.1	11.1
Current Account Balance	EUR bn	-29.2	-26.4	-24.8								
	% of GDP	-0.3	-0.3	-0.3								
General Government Balance	EUR bn	-389.2	-311.0	-235.7								
	% of GDP	-4.1	-3.3	-2.4								
General Government Debt	EUR bn	8334.2	8926.4	9300.8								
	% of GDP	88.3	94.0	96.6								
Gross Operating Surplus	YoY	2.6	-0.6	0.3								

Sources: Eurostat and Citi Investment Research and Analysis

Germany

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With mixed sentiment and activity data we have left our GDP forecast for 2012 unchanged. After a roughly unchanged GDP reading in 1Q we expect a recovery in the course of the year backed by improving domestic and foreign demand. On the domestic side, we expect a broad based increase including gains in construction spending and private consumption. With high energy prices and increasing wages, which are likely to lead to modest increases in unit labour costs, we expect German inflation to remain above 2%. While there seems now a broad based agreement in Parliament on the ESM, the opposition parties, whose support is required to get a 2/3 majority in parliament, ask for amendments to the fiscal compact. In any case the outcome of the upcoming state election in NRW on May 13 will be important for the stability of Angela Merkel's centre-right coalition.

France

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The first round of the Presidential elections (22 April) will likely show that President Nicolas Sarkozy and Socialist challenger François Hollande will make it to the second and final round on 6 May. The first round vote remains too close to call, with Sarkozy on 27% and Hollande on 28%, but we still believe that Hollande is more likely to be elected President, which should pave the way for a legislative election win for the Left in early June (10 & 17). Markets will likely react negatively to the news, particularly if the Far Left candidate Jean-Luc Mélenchon were to come in third place, enabling his party and its communist allies to influence policies, albeit at the margin. We are revising our forecast upwards from -0.3% to +0.1%, owing to the less negative start to 2012 (Q1 expected to be 0.0%), suggesting that France will avoid falling back into recession. We leave our 2013 GDP forecast at 0.5%.

Italy

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With thanks to Carla Clifton

We revised our prospects for the Italian economy this year up slightly as we expect Q1's GDP data to come in a little better than we expected last month. However, we revised our outlook for 2013 down from a contraction of 0.4% to a contraction of 0.9%. The deterioration in the country's outlook in 2013 reflects the effect of expected additional fiscal tightening and the possible delay in the start of the implementation of key labour market reforms, which will mean that the initial pain associated with the reforms is likely to be pushed into next year.

Figure 25. Germany, France and Italy — Economic Forecasts, 2011-13F

		Germany			France			Italy		
		2011	2012F	2013F	2011	2012F	2013F	2011	2012F	2013F
Real GDP	YoY	3.1%	0.9%	1.6%	1.7%	0.1%	0.5%	0.4%	-2.2%	-0.9%
Final Domestic Demand	YoY	2.4	1.1	1.6	0.9	0.0	0.4	-0.3	-3.1	-1.7
Private Consumption	YoY	1.4	1.0	1.5	0.4	0.0	0.5	0.2	-2.2	-1.1
Fixed Investment	YoY	6.6	1.8	3.3	3.0	-0.4	0.4	-1.2	-4.8	-1.9
Exports	YoY	8.4	3.1	4.6	5.0	3.1	4.2	6.4	0.2	1.2
Imports	YoY	7.5	3.6	4.7	4.8	0.3	3.4	1.3	-5.2	-1.8
CPI	YoY	2.3	2.2	2.3	2.3	2.5	1.6	2.9	3.6	2.0
Unemployment Rate	%	6.0	5.4	5.3	9.2	9.4	9.2	8.4	9.8	11.0
Current Account	€bn	147.7	130.0	119.5	-46.8	-40.4	-23.8	-50.4	-44.5	-36.7
	% of GDP	5.8	5.0	4.4	-2.3	-2.0	-1.1	-3.2	-2.8	-2.4
General Govt. Balance	€bn	-26.7	-15.9	-7.8	-104.7	-90.2	-71.0	-61.7	-40.3	-26.9
	% of GDP	-1.0	-0.6	-0.3	-5.2	-4.4	-3.4	-3.9	-2.6	-1.7
General Govt. Debt	% of GDP	81.3	81.3	80.2	84.8	91.4	95.3	120.9	128.8	131.8
Gross Trading Profits	YoY	1.5	-1.6	3.5	3.0	0.0	1.0	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, and Citi Investment Research and Analysis

Spain

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With thanks to Carla Clifton

We continue to expect the Spanish economy to contract by 2.7% this year and by 1.3% in 2013, more than 1pp below official forecasts and driven by fiscal tightening and private deleveraging. Moderate export growth will be insufficient to compensate for the weakness of domestic demand. The recently announced central government budget implies substantial deficit reduction this year, but is unlikely to allow Spain to meet its deficit targets of 5.3% and 3.0% of GDP for 2012 and 2013, respectively.

Greece

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With thanks to Carla Clifton

We leave our forecast for Greek GDP unchanged. We continue to expect the Greek economy to contract substantially this year driven by a sharp fall in household and government expenditure as the Government tries to implement fiscal tightening worth around 4.5% of GDP as required by the Troika. Over the 2013-2014 period, we expect the Greek economy to continue to perform poorly as the Government attempts to implement the promised €11bn worth of fiscal tightening to reduce the deficit to 2.1% in 2014. The outcome of the 6 May general election will be crucial regarding the country's EMU membership.

Ireland

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We are cutting our 2012 GDP forecast to minus 0.8% YoY from minus 0.3% last month, and edging up our 2013 forecast from zero to plus 0.3%. The downward revision to 2012 reflects the weaker-than-expected Q4 outturn (minus 0.2% QoQ) plus continued weakness in early-2012 data for retail sales, industrial production and new orders. At this stage, we assume that some of this weakness reflects greater-than-expected destocking and that this will unwind a little in 2013. Further out, there is some support for growth from the continued improvement in competitiveness, with the real exchange rate now at the lowest since 2002. The big picture is still that economic weakness is likely to produce a series of debt and deficit overshoots versus official forecasts.

Portugal

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With thanks to Carla Clifton

We downgraded our forecast for Portuguese GDP this year slightly to -5.4% (from -5.3% last month) to reflect the quicker than anticipated deterioration in the labour market and left our forecast for 2013 unchanged at -3.0% to reflect the likely adoption of further austerity measures. We further believe that Portugal will miss its deficit target this year given last year's slippage, net of the effect of one-off measures. We expect that the country needs a second Troika programme this year and we expect a PSI-style debt restructuring in 2013.

Figure 26. Spain, Greece, Ireland and Portugal — Economic Forecasts, 2011-13F

		Spain			Greece			Ireland			Portugal		
		2011	2012F	2013F	2011	2012F	2013F	2011	2012F	2013F	2011	2012F	2013F
Real GDP	YoY	0.7%	-2.7%	-1.3%	-6.9%	-6.5%	-2.4%	0.7%	-0.8%	0.3%	-1.6%	-5.4%	-3.0%
Final Domestic Demand	YoY	-1.7	-6.0	-4.0	-9.6	-8.4	-3.6	-3.0	-6.0	-2.1	-5.3	-8.4	-4.4
Private Consumption	YoY	-0.1	-3.0	-2.3	-7.1	-7.2	-3.6	-2.7	-1.7	-2.2	-3.9	-6.7	-3.5
Fixed Investment	YoY	-5.1	-9.8	-6.2	-20.6	-11.3	0.1	-10.6	-21.3	-17.6	-11.5	-15.9	-7.9
Exports	YoY	9.1	2.1	4.6	-0.8	1.2	2.0	4.1	2.8	3.9	7.4	1.8	3.2
Imports	YoY	-0.1	-9.2	-3.7	-8.0	-10.5	-2.0	-0.6	-0.9	2.9	-5.4	-7.3	-0.7
CPI	YoY	3.1	2.0	1.7	3.1	1.3	-0.3	-0.4	0.2	0.0	3.6	3.1	2.0
Unemployment Rate	%	21.6	24.3	25.7	17.3	22.6	24.9	14.4	15.1	16.7	12.7	15.6	17.3
Current Account	€bn	-37.8	-29.8	-23.8	-21.1	-17.7	-13.9	0.1	6.5	6.6	-13.9	-8.1	-4.6
	% of GDP	-3.5	-2.8	-2.2	-9.6	-8.5	-7.5	0.1	4.2	4.2	-8.1	-5.0	-2.9
General Govt. Balance	€bn	-90.4	-67.0	-57.8	-20.0	-14.8	-12.4	-18.1	-16.1	-13.5	-6.9	-4.5	-4.9
	% of GDP	-8.5	-6.3	-5.3	-9.3	-7.4	-6.2	-9.8	-9.6	-9.7	-4.0	-5.8	-3.5
General Govt. Debt	% of GDP	71.8	84.0	91.8	165.1	164.1	176.8	105.4	116.9	127.0	105.8	119.2	102.8

F Citi forecast. YoY Year-to-year growth rate. For Ireland we show the GDP deflator rather than the CPI. Sources: ISTAT, INE, Haver Analytics, Eurostat, and CIRA

Netherlands

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There are some signs of a recovery in exports, but the outlook for domestic demand remains poor, as the housing market correction continues. We expect that falling consumption and construction spending will keep the economy in recession. While there is some progress in the negotiations of the minority government coalition and the supporting PVV on extra budget cuts, at the time of writing there was still no agreement. As the other opposition parties, which the government needs for the approval of the ESM and the fiscal compact, are against extra near-term austerity we doubt that deficit will fall below 3% of GDP by 2013, as requested by the EDP.

Belgium

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Despite recent government efforts to construct a budget that would shrink the general government deficit to less than 3% of GDP for 2012, attention is turning to the 2013-15 period when the objective is to balance the books. The country's High Council of Finance estimates that the government will need to find savings worth around 1% of GDP per year to hit the target. Interestingly, the Council also recommended spreading fiscal tightening over time, if GDP growth were to fall short of the government's baseline. We are revising up our 2012 GDP forecast to 0.0% from -0.3%, taking on board the modest improvement in business confidence.

Slovakia

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The new left-wing SMER-SD government remains vocally committed to fiscal consolidation. While the previous government made consolidation particularly on the expenditure side, the new government probably will focus on lifting revenues. However, in our view, these measures probably will not be enough to prevent the deficit rising this year. Therefore, we expect a warning from the European Commission after midyear, which is likely to fasten the consolidation effort (including, eventually, spending cuts).

Slovenia

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Both, government debt and the deficit, rose slightly more than we expected in 2011. The deterioration in government finances reflects the capital injections into public enterprises and gradual, but sizeable increase of social benefits. The centre-right wing government of PM Janez Jansa (SDS) introduced a list of austerity measures to achieve an ambitious fiscal goal to cut the fiscal deficit to 3% of GDP in 2013 from 6.4% in 2011 (5.1% excluding the capital transfers). However, the government effort is likely to be hit on three fronts: i) referendums; ii) recession; iii) banking sector.

Figure 27. Netherlands, Belgium, Slovakia and Slovenia — Economic Forecasts, 2011-2013F

		Netherlands			Belgium			Slovakia			Slovenia		
		2011	2012F	2013F	2011	2012F	2013F	2011	2012F	2013F	2011	2012F	2013F
Real GDP	YoY	1.3%	-1.5%	0.4%	1.9%	0.0%	1.1%	3.3%	1.5%	2.1%	0.2%	-1.2%	1.3%
Final Domestic Demand	YoY	0.7	-1.6	-0.2	2.1	-0.5	0.3	0.6	0.7	1.4	-2.6	-2.6	0.1
Public Consumption	YoY	0.2	-0.9	-0.3	0.8	0.3	0.0	-3.5	-1.1	-0.7	-0.9	-2.3	-0.4
Private Consumption	YoY	-1.1	-1.2	0.1	0.8	-0.1	0.4	-0.4	-0.5	0.9	-0.1	-0.9	0.8
Investment (Ex Stocks)	YoY	1.3	-1.5	0.4	5.1	-0.5	0.7	5.7	4.4	3.5	-10.2	-5.2	-1.5
Exports	YoY	3.8	0.8	3.4	4.8	1.2	2.6	10.8	3.2	4.6	7.8	-2.1	1.8
Imports	YoY	3.5	0.2	3.0	5.2	0.6	2.0	4.5	3.1	3.8	4.7	-2.9	1.6
CPI (Average)	YoY	2.3	2.6	1.8	3.5	2.9	1.7	3.9	3.5	2.9	1.8	1.9	2.7
Unemployment Rate	%	5.3	6.2	6.4	7.2	7.7	8.1	13.2	13.7	13.6	8.2	9.5	10.4
Current Account	% of GDP	9.0	10.0	9.5	-0.8	-0.2	0.3	0.2	0.3	0.2	-1.5	-0.8	0.3
General Govt Balance	% of GDP	-4.7	-4.5	-3.5	-3.7	-2.9	-1.7	-4.8	-4.8	-3.2	-6.4	-4.3	-3.2
General Govt Debt	% of GDP	65.2	70.0	72.9	96.7	110.4	114.9	43.3	46.3	47.8	47.6	51.8	53.6

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

UK

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Our UK forecasts are little changed from last month, and we continue to look for GDP growth of about 0.2% this year and about 1% in 2013. This is the third month in a row with little change to our forecasts, and follows a series of downgrades from May-2011 to early 2012. Weakness in construction output and industrial production in January and February, along with other data, suggest that Q1 GDP growth (released on 25 April) will be around zero QoQ, with the YoY rate slowing to 0.3% from 0.4% in Q4-2011. Such a figure would confirm that this is the worst recession/recovery cycle of the last 100 years (outside World Wars 1 and 2), with real GDP still about 4% below the pre-recession peak after 16 quarters: whereas even in the 1930s the economy had surpassed its prerecession peak at this stage. Growth is also, once again, markedly underperforming versus the MPC's forecasts (the Feb-12 Inflation Report projected 0.4% growth in Q1).

We disagree with the MPC's view that the economy's underperformance just reflects high inflation and the EMU crisis. In particular, nominal GDP and nominal domestic demand have slowed markedly, to well below normal growth rates. New IMF research highlights that household debt booms are usually followed by extended economic weakness and household deleveraging, and we believe the MPC understate this drag for the UK. As a result, we believe further economic underperformance is likely. With the EMU crisis also still bubbling away, we continue to expect further QE in the UK.

The fiscal deficit will fall sharply, to 6-7% of GDP in 2012/13, because of the absorption of the pension fund of the state-owned postal service. The deficit will then rebound to an underlying level of about 7% of GDP in 2013/14. The medium-term trend is of a gently falling deficit, with the general government gross debt/GDP ratio likely to reach about 100% in 2014 or 2015.

Figure 28. United Kingdom — Economic Forecasts, 2011-2013F

					2011	2012				2013		
		2011	2012F	2013F	4Q	1QF	2QF	3QF	4QF	1QF	2QF	3QF
Real GDP	YoY	0.6%	0.2%	1.0%	0.4%	0.3%	0.1%	0.0%	0.5%	0.8%	1.4%	1.0%
	SAAR				-1.2	0.2	-1.1	2.0	0.8	1.5	1.4	0.4
Domestic Demand	YoY	-0.8	-0.6	-0.2	-0.7	0.4	-0.7	-1.3	-1.0	-0.9	0.1	0.2
(Incl. Inventories)	SAAR				-2.0	0.5	-3.2	-0.5	-0.6	0.7	0.7	-0.1
Consumption	YoY	-1.2	1.1	1.2	-1.0	0.1	1.0	1.7	1.5	1.4	1.3	1.1
	SAAR				1.7	1.6	1.9	1.5	1.0	1.0	1.6	0.8
Investment	YoY	-1.2	-4.9	-9.5	-1.0	0.7	-2.3	-6.5	-11.7	-12.4	-10.3	-8.0
	SAAR				-2.2	3.2	-12.0	-14.0	-22.0	-0.4	-3.1	-5.0
Exports	YoY	4.6	2.1	6.2	0.7	-1.6	1.7	4.2	3.9	6.5	7.0	5.6
	SAAR				6.4	-3.5	4.3	10.1	5.2	6.6	6.1	4.3
Imports	YoY	1.2	-0.3	2.3	-1.3	-0.1	-0.3	-0.1	-0.8	0.9	2.5	2.8
	SAAR				3.6	-2.4	-2.9	1.6	0.8	4.1	3.7	2.6
Unemployment Rate	%	8.1	9.4	10.3	8.4	8.9	9.2	9.7	10.0	10.3	10.3	10.4
CPI Inflation	YoY	4.5	2.8	2.0	4.7	3.5	3.0	2.7	2.3	2.1	2.1	2.0
Merch. Trade	£bn	-99.5	-85.6	-62.1								
	% of GDP	-6.6	-5.6	-3.9								
Current Account	£bn	-29.0	-24.2	2.5								
	% of GDP	-1.9	-1.6	0.2								
PSNB	£bn FY	-126.0	-103.2	-119.9								
	% of GDP	-8.3	-6.7	-7.5								
General Govt. Balance	% of GDP	-8.3	-6.5	-7.4								
Public Debt	% of GDP	82.9	88.3	94.2								
Gross Nonoil Trading Profits	YoY	3.5	-5.6	8.8								

Note: Fiscal deficit shown excluding financial interventions. F Citi forecast. YoY Year-to-year growth rate. Sources: ONS and Citi Investment Research and Analysis

Switzerland

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We are lifting our forecast for 2012 growth to 0.7% from 0.1% last month and minus 0.2% two months ago, following continued gains in recent surveys. Within that, we expect growth of about 0.1% QoQ in Q1, the same pace as Q4. With deflation likely to continue for an extended period, the SNB is likely to continue to keep 3-month libor rates at close to zero and strongly defend the CHF1.20/EUR level.

Sweden

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Sentiment indicators signal a slowdown rather than a recession, suggesting that the sharp decline in Q4 GDP exaggerates the underlying weakness. CPIF inflation is expected to rise slightly this year from the current low level of 1.1% y/y (but to stay below the 2% CPI target), partly due to rising petrol prices, while declining mortgage rates will lower headline CPI. The Riksbank is expected to continue to cut rates to 1% this year due to rising unemployment and low inflation. Swedish public finances remain extremely strong in an international comparison, leaving room for an expansionary fiscal policy in case needed.

Denmark

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Denmark is in for a prolonged period of limited economic expansion. Exports are set to slow substantially this year, while the reimbursement of contributions to the voluntary early retirement pension scheme following the adoption of the retirement reform by the government is likely to lend a hand to private consumption. However, the fragile housing market, stagnating labour market and continued balance sheet deleveraging will likely continue to weigh on consumer spending. Investment activity likely bottomed in 2011 and is expected again this year to be driven largely by public initiatives as part of the government's "kick-start" stimulus package.

Norway

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A recovery in private consumption since the turn of the year and continued high activity in the oil sector support momentum in the Norwegian economy. Mainland GDP growth (excl. oil/gas and shipping) is set to outpace most other European economies this and next year. Norges Bank cut interest rates in mid-March by 25bp to 1.5%, reflecting concerns over a weaker global growth outlook, low domestic inflation, a strong krone and continued financial market unrest. Unless the NOK appreciates strongly, the policy rate should remain stable for the reminder of the year. Domestic conditions do not warrant a lower policy rate and low rates could fuel a housing bubble.

Figure 29. Switzerland, Sweden, Denmark and Norway — Economic Forecasts, 2011-2013F

		Switzerland			Sweden			Denmark			Norway		
		2011	2012F	2013F	2011	2012F	2013F	2011	2012F	2013F	2011	2012F	2013F
Real GDP	YoY	1.9%	0.7%	0.9%	4.0%	0.7%	1.9%	1.1%	0.7%	1.2%	2.7%	2.5%	2.9%
Final Domestic Demand	YoY	1.8	1.7	0.1	2.8	0.4	1.9	-0.3	1.1	1.1	3.2	2.6	2.9
Public Consumption	YoY	1.7	1.2	0.9	1.8	0.8	1.2	-0.7	0.8	0.1	1.6	2.3	2.2
Private Consumption	YoY	1.0	1.1	0.3	2.1	0.6	2.0	-0.2	0.9	1.3	2.3	2.0	2.4
Investment (Ex Stocks)	YoY	3.9	3.7	-0.9	6.3	-0.5	2.7	0.3	2.5	2.1	8.4	4.6	5.4
Exports	YoY	3.4	0.4	2.5	7.0	0.3	3.8	7.1	1.1	2.7	1.2	2.4	4.8
Imports	YoY	1.9	0.0	1.2	6.3	0.2	3.8	5.4	1.0	2.7	1.9	3.0	3.5
CPI (Average)	YoY	0.2	-1.2	-1.3	2.9	1.2	1.9	2.7	2.0	1.5	1.3	1.7	2.0
Unemployment Rate	%	3.1	3.3	3.8	7.5	7.8	8.0	7.6	7.7	7.8	3.3	3.4	3.4
Current Account	% of GDP	15.0	13.8	14.0	7.2	7.5	7.8	6.5	5.4	5.2	14.0	14.3	14.9
General Govt Balance	% of GDP	0.6	0.2	-0.2	0.1	-0.4	-0.2	-2.5	-5.2	-3.9	12.0	12.5	13.5
General Govt Debt	% of GDP	53	52	51	36.9	36.6	35.7	45.4	49.4	52.0	NA	NA	NA

[a] For Norway, mainland GDP. F Citi forecast. YoY Year-on-year growth rate. Sources: National sources and Citi Investment Research and Analysis

Canada

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The outlook for Canada is marginally improved, reflecting positive inroads towards the containment of the EA crises, somewhat more robust demand from the U.S. and temporary lifts from unseasonably warm weather in North America. The Canadian economy also performed somewhat better than expected in the later half of 2011 and very early this year. Nonetheless, we maintain our anticipation of lackluster activity ahead amid moderating foreign and domestic demand.

The European recession, deceleration of Asian growth to more sustainable levels, U.S. fiscal consolidation and household deleveraging, and the strong Canadian dollar will weigh on Canadian exports. Internally, a less robust capex revival, smaller government, and softer consumer spending amid modest labour market growth and mounting debt, should dampen domestic demand.

Risks remain two-sided. Contagion and reduced risk appetite stemming from the EA sovereign debt and banking crises are the main threat to the outlook. Other downside risks include the possibility of extremely weak U.S. demand amid fiscal restraint; and Canadian consumer retrenchment under the weight of massive debt obligations and/or on account of a disorderly unwind in housing market activity.

Meanwhile, upside risks include faster-than-expected EM growth and higher global commodity price inflation; above-forecast U.S. activity; and leverage-driven Canadian consumer spending. A sharper-than-anticipated slowdown in Asian growth and rising oil prices are emerging risks to the inflation outlook.

The BoC has adopted a rather hawkish tone, stating that some modest withdrawal of the present considerable degree of monetary policy stimulus may become appropriate. The shift from a previously neutral policy tack raised market expectations of a full rate hike before yearend. However, we remain cautious about the outlook, and therefore retain our call for resumed tightening in 1Q 2013.

Figure 30. Canada — Economic Forecast, 2011-2013F

					2011	2012F				2013F		
		2011	2012F	2013F	4Q	1QF	2QF	3QF	4QF	1QF	2QF	3QF
Real GDP	YoY	2.5%	2.0%	2.3%	2.2%	1.8%	2.4%	1.8%	2.0%	2.0%	2.2%	2.4%
	SAAR				1.8	2.0	1.6	1.9	2.6	2.0	2.3	2.7
Final Domestic Demand	YoY	3.0	1.8	2.6	2.1	2.0	1.7	1.8	1.9	2.3	2.6	2.8
	SAAR				2.1	1.5	1.5	2.0	2.7	2.9	2.9	2.8
Private Consumption	YoY	2.2	1.9	2.3	1.8	1.9	1.9	1.9	1.8	2.2	2.3	2.4
	SAAR				2.9	1.0	1.8	2.0	2.5	2.4	2.4	2.4
Government Spending	YoY	0.5	-2.3	0.6	-1.5	-2.5	-2.8	-2.5	-1.5	0.1	0.7	0.9
	SAAR				-3.1	-5.4	-1.5	0.1	1.0	0.9	0.9	0.9
Private Fixed Investment	YoY	9.3	6.0	5.9	8.1	7.1	5.9	5.6	5.3	5.0	5.7	6.2
	SAAR				6.3	8.0	4.0	4.0	5.3	6.9	6.6	6.0
Exports	YoY	4.4	5.5	3.4	4.5	5.4	7.5	4.6	4.5	2.9	3.0	3.5
	SAAR				4.6	8.1	1.9	3.8	4.4	1.6	2.5	5.7
Imports	YoY	6.5	2.6	4.5	5.3	3.8	1.1	2.5	3.0	3.7	4.4	4.7
	SAAR				2.2	1.6	2.0	4.0	4.5	4.5	4.5	5.5
CPI	YoY	2.9	2.1	1.8	2.7	2.4	2.3	2.1	1.8	1.8	1.1	1.7
Core CPI	YoY	1.7	2.0	2.0	2.0	2.2	2.1	2.0	1.9	1.9	2.0	2.2
Unemployment Rate	%	7.5	7.2	6.9	7.5	7.4	7.3	6.9	7.2	7.1	7.0	6.6
Current Account Balance	C$bn	-48.3	-27.5	-29.6	-41.3	-24.6	-25.3	-29.5	-30.6	-26.5	-31.3	-3.2
	% of GDP	-2.8	-1.5	-1.6	-2.4	-1.4	-1.4	-1.6	-1.7	-1.4	-1.7	-1.7
Net Exports (Pct. Contrib.)		-1.3	0.7	-0.8	0.7	2.0	-0.2	-0.4	-0.5	-1.5	-1.1	-0.5
Inventories (Pct. Contrib.)		0.2	-0.3	0.2	-1.0	0.0	0.2	0.2	0.1	0.3	0.3	0.2
Budget Balance (Fiscal Year)	% of GDP	-1.4	-1.2	-0.5								
Federal Budget Debt	% of GDP	33.5	33.2	32.3								
General Govt. Debt	% of GDP	79.0	77.9	76.6								

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

Australia

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The significant turbulence in the economy resulting from major structural changes arising out of the commodity boom and associated high AUD is complicating assessments of the outlook. On balance, our forecasts are unchanged this month and we still anticipate a pick-up in activity as the year develops. Growth in the first quarter probably was below trend, but unemployment remains low at 5.2% and the March labour force report surprised with an outsized rebound in employment. The roll-out of major commodity projects continues apace. However, confidence, particularly amongst consumers, is weak which could undercut prospects for spending. Subdued asset prices and credit growth are further negatives for the consumer. The federal government's Budget next month is expected to be a drag on growth as the government attempts the largest shift in the budget balance in more than 40 years. Assuming a favourable Q1 CPI (due late this month), we expect the RBA to cut the cash rate 25bp at the May Board meeting.

New Zealand

The Q4 2011 GDP data showed that it has taken three years for the level of real output to retrace the losses incurred in just over one year of recession. Even with a small upgrade in our forecasts, the economic recovery is likely to continue at a sub-trend pace in 2012 of 1.8%. This outlook implies little risk of demand pressure on the CPI, which should ensure that monetary policy remains highly accommodative. The risk is that our forecast Q1 2013 policy tightening gets pushed out to Q2. Key signposts for such a change would be if the currency remains a headwind to economic rebalancing and if the Christchurch reconstruction efforts get further delayed. The risk from the latter signpost has increased as the Canterbury region recently experienced another earthquake.

Figure 31. Australia and New Zealand — Economic Forecast, 2011-2013F

	Australia			New Zealand		
	2011	2012F	2013F	2011F	2012F	2013F
Real GDP[a]	2.0%	3.4%	3.9%	1.3%	1.8%	2.3%
Real GDP (4Q versus 4Q)	2.3	3.8	3.7	1.8	2.5	2.0
Real Final Domestic Demand	4.1	4.0	4.4	2.3	1.7	2.8
Consumption	3.4	3.1	3.2	2.5	2.3	2.1
Govt. Current & Capital Spending[b]	-0.6	0.8	3.2	1.8	1.3	1.3
Housing Investment	1.1	-0.8	4.5	-12.0	7.4	12.6
Business Investment[c]	16.9	13.4	9.3	6.9	0.1	5.0
Exports of Goods & Services	-1.6	8.9	8.0	2.4	4.0	1.6
Imports of Goods & Services	11.6	8.9	8.0	6.0	2.7	3.7
CPI	3.4	2.6	3.4	4.0	1.6	2.4
CPI (4Q versus 4Q)	3.1	3.4	3.1	1.8	2.2	2.4
Unemployment	5.1	5.4	4.9	6.5	6.4	5.6
Merch. Trade, BOP (Local Currency, bn)	18.1	5.8	-19.1	3.3	2.4	-0.4
Current Account, (Local Currency, bn)	-32.6	-43.3	-79.6	-8.3	-10.8	-16.3
Percent of GDP	-2.3	-2.9	-5.0	-4.0	-5.2	-7.6
Budget Balance[d] (Local Currency, bn)	-47.7	-25.5	3.0	-15.9	-12.1	-6.5
Percent of GDP	-3.4	-1.8	0.2	-8.0	-5.9	-3.1
General Govt. Debt (% of GDP)[e]	5.9	7.2	6.7	20.9	26.8	30.0
Gross Trading Profits[f]	6.2	5.4	7.3	NA	NA	NA

BOP Balance of payments basis. CPI Consumer Price Index. F Citigroup 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. [f]Company gross operating surplus. Source: NZIER and Citi Investment Research and Analysis.

China

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Growth decelerated sharply, but is expected to rebound in H2. GDP grew by 8.1% YoY (7.3% SAAR) in Q1, down from 8.9% YoY in Q4/2011, roughly in line with our expectation. The slowdown appears to have been driven by weaker domestic and external demand, as investment and consumption both slowed and the contribution of net exports to growth turned to -0.8ppt from -0.5ppt in 2011. The slowdown is in large part policy driven, as fiscal, monetary and property policies were all tightened last year. Policies have been eased recently, featuring more fiscal spending, increased credit to support projects under construction, and targeted easing in the low-end property market. However, the pace of policy easing has been slower than expected, prompting us to adjust downward the Q2 growth from 8.2% to 7.9% YoY. With more determined policy actions since Mar, we expect growth to trough in Q2, and start to rebound in Q3.

CPI inflation rebounded, still within the tolerable range. Consumer prices rose by 3.6% YoY in March, relative to 3.2% YoY in February. Quarterly inflation continued the downward trend, with Q1 inflation falling to 3.8% YoY from 4.6% YoY in Q4-2011. In March, nonfood prices rose more than expected largely reflecting the direct impact of the gasoline and diesel price hike during the month. Inflation is likely to stay in the 3-4% range for most of the year, and this should not be a hindrance for policy easing. Reflecting more ambitious tone from the authorities on price reforms, including for electricity, natural gas and water, we revised our forecast for 2012 annual average inflation up from 3.3% last month to 3.5%.

Widening RMB trading band may increase currency volatility amid a general trend of slow appreciation. The PBOC widened the CNYUSD trading band from ±0.5% to ±1% this month. The move reflects China's view that RMB is getting closer to equilibrium level. Economic fundamentals still argue for further appreciation, although the room and incentive for fast appreciation are weaker when trade surplus declines and inflation appears subdued. We expect 1-2% RMB appreciation in the next 12 months against a relatively strong USD. A wider band is expected to lead to more volatility of RMB, but PBOC can still influence the value of RMB by the daily fixing and through market intervention.

Figure 32. China — Economic Forecasts, 2011-2013F

					2011		2012F				2013F	
		2011	2012F	2013F	3Q	4Q	1QF	2QF	3QF	4QF	1QF	2QF
Real GDP	YoY	9.2%	8.4%	8.6%	9.1%	8.9%	8.1%	7.9%	8.8%	8.6%	8.8%	8.5%
Real Final Domestic Demand	YoY	10.4	9.5	9.2								
Consumption	YoY	10.0	9.7	9.7								
Fixed Capital Formation	YoY	10.8	9.2	8.7								
Industrial Production	YoY	13.9	11.8	12.1	13.8	12.8	11.6	11.4	11.9	12.3	12.4	12.0
Exports	YoY	20.3	6.5	13.1	20.6	14.3	7.6	4.2	5.5	8.8	11	12
Imports	YoY	24.8	9.1	15.1	24.8	20.1	6.9	6.1	9.6	13.3	13	14
Merchandise Trade Balance	$bn	155	120	98	63	48	1	40	47	32	-8	36
FX Reserves	$bn	3,181	3,413	3,530	3,202	3,181	3,305	3,370	3,408	3,413	3,405	3,441
Current Account	% of GDP	2.8	2.0	1.5								
Fiscal Balance	% of GDP	-1.3	-2.0	-1.5								
General Govt. Debt	% of GDP	15.3	15.6	15.3								
Urban Unemployment Rate	%	4.1	4.2	4.1	4.1	4.1	4.2	4.2	4.2	4.2	4.1	4.1
CPI	YoY	5.4	3.5	3.5	6.3	4.6	3.8	3.6	3.0	3.7	3.8	3.3
Exchange Rate (end period)	CNY/$	6.29	6.25	6.14	6.38	6.29	6.30	6.31	6.28	6.25	6.22	6.20
1-Yr Deposit Rate (end period)	%	3.50	3.50	3.75	3.50	3.50	3.50	3.50	3.50	3.50	3.75	3.75

Note: F Citi forecast. E Citi estimate. YoY Year-to-year percent change. SAAR Seasonally adjusted annual rate. *Based on official data. The ratio was roughly 50% in 2010 if the debt of Ministry of Railway and local government debt as audited by the National Auditing Office are included. Sources: Haver Analytics and Citi Investment Research and Analysis

India

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Given the limited room on both the monetary and fiscal front, trends in FY13 GDP will likely remain in the 7% range. Two critical variables remain: (a) whether recent policy efforts by the PMO to encourage investments indeed play out and (b) the direction of oil prices. While lower rates would help, key to the investment cycle is the implementation of steps proposed to resolve bottlenecks plaguing investments. We believe that with the prime minister's office driving the effort, it raises the possibility of ministries, state governments, PSUs and Coal India finally coming together and resolving the issues at hand.

A widening current account deficit (due to higher gold/oil imports) coupled with a slowdown in capital flows (risk off/ deleveraging) resulted in India's 3Q FY12 overall BoP going deep in the red to US$12.8bn v/s a surplus of US$5.7bn in 1HFY12. The Jan/Feb "risk-on" rally will have a positive impact on the 4QFY12 no's and we expect the full year deficit to moderate to -US$4.2bn. Going forward for FY13, we maintain our view of the CAD widening to US$80.1bn ~4% of GDP (this incorporates crude at USD 125/bbl). However given the non-conducive environment for foreign investment, we have lowered our numbers on the capital account. We expect the drawdown in reserves to continue and pressure on the INR to persist.

Thanks to the base effect, near-term inflation trends are likely to be benign in the 6.5% to 7% range, but trends in the latter half of the year could edge up due to some pass through of tariffs and BoP pressures resulting in a weaker rupee. The RBI, in its annual policy meeting, surprised positively by cutting its key policy rates by 50bps – higher than expectations of a 25bps cut. However, it has highlighted that the economy is likely to revert close to its post-crisis trend in FY13, which does not leave much room for monetary policy easing without aggravating inflation risks. Taking into account the above and our FY13 expectations for growth and inflation at 7% and 7.4%, we could see at best one more rate easing later this year. However this will be data/event dependent.

India's top down macro story has de-rated over the last year. Growth expectations are now in the 6.5%-7% range v/s 8%-9% a year ago. Moreover, India's deficits – both fiscal and current account have deteriorated. The combined fiscal deficit (including the SEB losses) is at ~9% of GDP while the current account deficit is at ~4% of GDP. This coupled with global factors have resulted in a revision to our INR/USD estimates to 54 in 6-12mos and 51 in the long term (next 2-3 years).

Figure 33. India — Economic Forecasts, FY2012/13-2014/5F

		FY 12/13F	FY 13/14F	FY 14/15F
Real GDP	YoY	7.0%	7.5%	8.2%
Final Domestic Demand	YoY	6.3	7.1	7.8
Private Consumption	YoY	6.5	6.7	7.0
Fixed Investment	YoY	6.5	8.0	10.0
Exports	YoY	13.5	15.0	11.0
Imports	YoY	8.3	10.8	9.3
Wholesale Price Index*	YoY	7.4	6.5	6.0
Consumer Price Index	YoY	7.0	6.5	6.0
Current Account	US$ bn	-76	-75	-74
	% of GDP	-4.0	-3.3	-2.7
Consolidated Fiscal Balance	% of GDP	-8.0	-7.7	-7.0
Centre Fiscal Balance	% of GDP	-5.5	-5.0	-4.5
US Dollar Exchange Rate	Average	53.8	51.8	50.8

Note: * In India, policymakers look at the wholesale price index. Sources: Haver Analytics and Citi Investment Research and Analysis

Korea

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Export growth declined rapidly to +3.0%YoY in 1Q12 on the back of the economic slowdown in China and the sluggish European economy. Export growth to China and euro area in 1Q12 fell further to +4.7%YoY and -10.7%YoY from +17.8%YoY and +1.9%YoY in 4Q11. The sharp contraction of exports also led import growth to slow to +7.5%YoY from +13.4%YoY in the previous quarter and narrowed the trade surplus to US$1.7bn, which is about one-fifth of average quarterly trade surplus in 2011. The jobless rate in 1Q12 rose to +3.5%, 0.2%p higher than in 4Q11 as the manufacturing sector continued to shed jobs and job seekers increased along with the opening of government jobs. Meanwhile, headline CPI inflation in Mar dropped to +2.6%YoY from +3.1% in Feb due to the government's free school meal policy, college tuition cuts and high base effects from a year ago. However, we still see rising inflationary pressures from industrial goods and public services. In addition, the expected inflation surveyed by the BoK in Mar remained elevated at +3.9%YoY. Despite hawkish views at the last two MPC meetings, the BoK seems to maintain its current neutral stance to minimize the uncertainties on economic growth and inflation which could be brought on by an early change in policy rate.

Indonesia

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Uncertainty on inflation has been prolonged following the Parliament's decision to vote for a higher oil price threshold of $120.75/bl (6MMA) as a pre-requisite before any fuel price hike. We still think the hike will eventually go through, but Indo crude would have to stay at least $124/bl in April and May or rise more than 5.1% in Apr (vs. $128/bl in Mar) as a pre-condition. In the meantime inflation expectations may remain elevated and hoarding could intensify, making fuel supply scarcity a risk that should be more closely watched. Although the risk of a subsidy budget overrun is substantial, risks to the overall budget deficit (and new bond issuances) look contained. We calculate the overrun can reach Rp65-70tn, but the government has some backstops to tap into e.g. the compensatory subsidies (Rp30.6tn) and unspent funds from the line ministry expenditure budgets which we estimate at Rp37tn. We do not expect a policy rate change this year but BI may eventually raise reserve requirements when fuel prices are raised or inflation expectations climb further. IDR bonds have been trading sideways and with the trade surplus still expected to be suppressed (fuel imports + softer coal prices), we expect the IDR to end the year weaker at Rp9,369/US$. However the FDI outlook is still sanguine; corporate actions in the equity market could provide near term support for the IDR.

Figure 34. Korea and Indonesia — Economic Forecasts, 2011-2013F

		Korea			Indonesia		
		2011	2012F	2013F	2011	2012F	2013F
Real GDP	YoY	3.6%	3.7%	4.4%	6.5%	6.2%	6.5%
Final Domestic Demand	YoY	1.3	2.1	4.1	5.7	7.0	7.1
Private Consumption	YoY	2.3	1.4	4.3	4.7	4.5	4.8
Fixed Investment	YoY	-1.1	3.6	5.1	8.8	11.4	11.4
Exports	YoY	9.5	6.8	9.3	13.6	9.0	12.0
Imports	YoY	6.5	5.0	8.9	13.3	11.6	15.0
Consumer Price Index	YoY	4.0	3.1	3.4	5.4	5.8	5.3
Unemployment Rate	%	3.4	3.3	3.2	6.6	6.3	6.0
Current Account	US$ bn	27.7	12.5	9.3	2.1	-6.3	-8.6
	% of GDP	2.5	1.1	0.7	0.2	-0.7	-0.8
Fiscal Balance	% of GDP	1.5	1.4	1.2	-1.2	-1.8	-0.7
US Dollar Exchange Rate	Average	1108	1136	1065	8763	9317	9333

Sources: Haver Analytics and Citi Investment Research and Analysis

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Slowing external and domestic demand likely to weigh on 1Q's GDP growth (Citi E: 1.2%YoY). Inflation appears to be cooling, but we worry that transportation fee hikes and food prices shocks will keep CPI average at 4% YoY for 2012. Labour market tightness continues to pressure wages, but the recent trends of growing labour force and hiring caution by businesses will probably lift the jobless rate slightly. Risk appetite has been losing steam lately and is reflected in the HKD retreating away from the strong end of the trading band and the HSI giving back some of its earlier gains. 3M HIBOR likely remain on a very gradual uptrend given global monetary accommodation. The political dust is settling, with the newly elected Chief Executive CY Leung – who has pledged to increase affordable housing, eliminate unfair business practices and alleviate income disparity in his 5 year term starting 1 July.

Singapore

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The sharper-than-expected 9.9%QoQ SAAR rebound in 1Q12 GDP poses small upside risks to our above-consensus 2012 GDP forecast of 3.6% (consensus: 2.5%). With the V-shaped recovery in GDP, wider positive output gap and 1%-pt hike in its forecasts for both headline and core inflation, MAS "surprised" markets by steepening the SGD NEER policy band slope "slightly" and restoring a narrower width, partly reversing the Oct 2011 easing decision. The calibrated nature of the move is predicated on MAS's expectations of only "modest growth" ahead, mirrored in the 16.8% MoM sa decline in Mar NODX, but further tightening in Oct 2012 is possible if these expectations prove too dovish. Despite a marginal drop in home prices in 1Q11, with the V-shaped rebound in home sales and downward pressure on interest rates, risks of another round of property cooling measures may be rising.

Taiwan

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Exports remained in contraction in 1Q12 but showed better momentum in March to suggest a brighter outlook in 2Q12 and beyond. Meanwhile, the government announced it will raise gasoline prices by an average of 10.7% and utility prices by a range from 16.9% to 35%. We believe these one-off price hikes will likely add to CPI inflation by around 1ppt and erode consumers' purchasing power. Accordingly we raise our 2012 CPI forecast to 1.9% (from 1.4% last month) but lower our GDP forecast to 3.5% (from 3.7%). Interbank overnight rates rose in April after standing still for several months, suggesting the CBC is biased towards tightening. However we still believe the CBC will hold rates unchanged in June. Equity markets suffered from the capital gains tax and other tax reform that will follow.

Figure 35. Hong Kong, Singapore and Taiwan — Economic Forecasts, 2011-2013F

		Hong Kong			Singapore			Taiwan		
		2011	2012F	2013F	2011	2012F	2013F	2011	2012F	2013F
Real GDP	YoY	5.0%	3.0%	4.2%	4.9%	3.6%	5.0%	4.0%	3.5%	4.2%
Final Domestic Demand	YoY	7.5	3.3	1.9	3.4	1.8	3.9	1.3	1.3	3.1
Private Consumption	YoY	8.4	3.1	2.0	4.1	2.8	4.1	3.0	2.8	3.3
Fixed Investment	YoY	7.3	4.0	2.0	3.3	1.9	4.3	-3.8	-2.4	4.9
Exports	YoY	4.2	2.8	7.0	2.6	3.8	6.0	4.5	3.7	6.0
Imports	YoY	4.6	2.6	6.1	2.4	4.5	6.6	-0.6	0.7	5.1
CPI	YoY	5.3	4.0	2.9	5.2	3.8	3.2	1.4	1.9	2.1
Unemployment Rate	%	3.4	3.7	3.6	2.0	2.3	2.0	4.4	4.3	4.2
Current Account	US$ bn	12.4	34.3	34.1	57.1	41.7	41.2	41.3	42.7	45.3
	% of GDP	5.1	13.1	12.2	21.9	15.0	13.0	8.8	8.7	8.4
Fiscal Balance	% of GDP	3.5	0.8	0.7	1.5	1.0	1.0	-1.9	-1.6	-1.3
US Dollar Exchange Rate	Average	7.78	7.76	7.76	1.26	1.24	1.20	29.40	29.44	28.60

Sources: Haver Analytics and Citi Investment Research and Analysis

Russia

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Current account reached a record high of US$43bn in 1Q due to oil prices trading above US$120/bbl, but capital outflows of US$38bn drained most of it. The Central Bank increased its interventions, buying US$4bn of FX in March and US$1bn during the first week of April, showing capital outflows have started to decelerate. The capital account is likely to strengthen in 2Q due to increased foreign borrowing and less severe outflows. While tight liquidity and the still reasonable balance of payments outlook are supportive for the ruble in the short run, we see little fundamental reason for strengthening beyond current levels. We estimate the ruble is more sensitive to oil price declines, while rising prices bring little change to the exchange rate. We expect the ruble basket to return to 35-36 at end-2012. The 12%YoY gain in real wages in January-February increased consumer confidence, and should support spending in the near-term. Annual GDP growth could accelerate above the base case of 3-3.5% to 4%+ if oil prices remain close to US$120-125 until year-end. We expect inflation to accelerate back to about 6.5-7% by year-end from 3.8% in March as a result of postponed state-regulated price adjustments. The Central Bank has recently left interest rates unchanged, while tuning the structure of its monetary operations to limit the volatility of the money market rates.

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The government has finally announced the much-awaited incentive scheme aimed at narrowing the wide current account deficit, through reducing import dependence, and promoting investment in less developed areas. Specifically, the package includes generous incentives in the form of tax exemptions and reductions in the employer's contribution of the social security tax/premium. There are also interest subsidies for certain regions, as well as some additional income tax reductions for the poorest region. What is our take? We are sceptical about the effectiveness of the package in generating a strong supply response for at least three reasons. *First*, this initiative alone is unlikely to address Turkey's well-recognized structural weaknesses (such as rigid labour markets and highly regulated product markets), which undermine the country's competitiveness/productivity. *Second*, given the highly complex nature of the subsidy scheme, whether the bureaucracy has the implementation and monitoring capacity remains an open question. *Third*, even if one believes the package will be effective in narrowing the current account gap, it would take time. Given the authorities' reluctance to contain domestic demand, this means Turkey will need to live with a wide current account deficit in the near-term, which leaves the country at the mercy of global financial markets.

Figure 36. Russia and Turkey — Economic Forecasts, 2011-2013F

		Russia			Turkey		
		2011	2012F	2013F	2011	2012F	2013F
Real GDP	YoY	4.3%	3.5%	4.0%	8.5%	2.5%	4.3%
Final Domestic Demand	YoY	1.7	1.5	2.0	9.8	1.6	4.5
Private Consumption	YoY	6.3	5.3	5.3	7.7	1.0	4.5
Fixed Investment	YoY	8.0	6.8	9.0	18.3	2.3	4.9
Exports	YoY	0.4	1.0	2.7	6.5	1.8	5.5
Imports	YoY	20.3	4.3	5.8	10.6	-1.4	6.2
CPI	YoY	8.4	5.3	7.0	6.5	9.6	7.0
Unemployment Rate	%	6.6	7.5	7.5	9.8	10.2	10.2
Current Account	US$ bn	98.8	102.6	44.8	-77.2	-69.4	-72.9
	% of GDP	5.2	5.2	2.1	-10.0	-8.5	-8.3
Fiscal Balance	% of GDP	2.0	0.3	0.1	-1.3	-2.2	-2.5
US Dollar Exchange Rate	Average	29.4	30.2	32.1	1.68	1.78	1.84

Sources: Haver Analytics and Citi Investment Research and Analysis

Hungary

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The exchange of official letters between the Hungarian government and the EC continue in order to clear preconditions and provide a green light to official loan aid talks. The Hungarian government is visibly in no rush to deliver requirements and continues its dual talk to keep up market hopes and issue lc papers in an effort to create more funding buffers, which under unchanged conditions may last until around year-end without Eurobond issuance. The government will publish its updated convergence report in the second half of April, presenting detailed fiscal austerity measures of about 1.5% of GDP that will be needed to ensure the 2.2% of GDP deficit target for 2013 remains on track. Although we have turned slightly more optimistic on the growth outlook and no longer project a recession this year, we believe new fiscal austerity measures are unlikely to deliver a meaningful decline in risk premia in the absence of an IMF deal. Given that at current funding costs the economy's growth potential is too low to put the public debt ratio on a declining path we expect funding constraints will finally force the government to compromise and finalize an agreement in 2H12. The delay in loan talks, together with the rising inflation outlook, is likely to postpone rate cuts to 4Q12.

Poland

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Recent data releases suggest the economy is gradually slowing and the deterioration in the labour market is likely to limit price pressures. The manufacturing PMI fluctuates around the key 50 level while industrial output growth remains at low levels, due to weak domestic and export orders. However, the Monetary Policy Council turned more hawkish and signalled that, in the absence of more convincing signs of slowdown and disinflation, it could consider policy tightening at one of its upcoming meetings. Although we don't share the MPC's inflation concerns, the tone of the statement suggests interest rates are unlikely to fall this year. We expect relatively hawkish rhetoric in the coming months, but given uncertain growth outlook in the euro area, chances for ECB easing at some stage and our forecast of slower GDP growth in Poland, we expect policy tightening will be avoided and the base rate will remain at 4.5% until end-2012. In politics, pension reform plans have contributed to tensions within the government but coalition parties have eventually decided to support an increase in the retirement age. This should have substantial positive fiscal consequences, albeit only in the long term (2020 and beyond).

Figure 37. Hungary and Poland — Economic Forecasts, 2011-2013F

		Hungary			Poland		
		2011	2012F	2013F	2011	2012F	2013F
Real GDP	YoY	1.7%	0.0%	1.4%	4.3%	2.7%	2.4%
Final Domestic Demand	YoY	-1.2	-1.8	-0.8	3.6	2.8	2.0
Private Consumption	YoY	0.0	-1.5	-0.5	3.1	2.2	2.5
Fixed Investment	YoY	-5.4	-2.3	0.5	8.7	5.6	1.0
Exports	YoY	8.4	4.5	6.4	5.9	4.8	4.5
Imports	YoY	6.3	3.3	5.2	4.8	2.5	2.3
CPI	YoY	3.9	5.6	3.5	4.3	3.9	2.7
Unemployment Rate	%	11.6	11.8	11.0	12.5	12.9	11.7
Current Account	US$ bn	2.0	1.6	2.0	-21.2	-18.8	-20.9
	% of GDP	1.7	1.2	1.5	-4.1	-3.7	-3.9
Fiscal Balance	% of GDP	4.2	-3.2	-3.0	-5.1	-3.3	-2.7
US Dollar Exchange Rate	Average	201	227	226	2.96	3.19	3.19

Sources: Haver Analytics and Citi Investment Research and Analysis

Czech Republic

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We have kept our 2012 GDP forecast virtually unchanged at -0.4%YoY, but we have changed the structure. While there was a larger foreign trade surplus in 4Q11, it suggests a stronger contraction of domestic demand, which is also likely to pass-through into 2012. As such, we expect both consumption and fixed investment to decline somewhat. The fall in private consumption reflects higher CPI growth on VAT hikes (while wages are likely to increase a bit more, real wages are likely to contract along with lower employment) and tough fiscal consolidation on both spending and taxes (with another hike in VAT in 2013, plus hikes in direct taxes). Coalition tensions eased somewhat after some noise in recent weeks, but we expect them to continue. However, all coalition parties have a vested interest in continuing to cooperate with each other. Hence fiscal tightening is likely to remain on track and, after the better than expected 2011 fiscal deficit data, we expect the government deficit to remain around 3% of GDP in 2012-2013. However, the level of public debt was revised upward (owing to reclassifications), which probably limits chances for a sovereign rating upgrade. We expect fiscal debt to peak below 45% of GDP in 2013. We keep our CNB policy rate forecast at 0.75% until mid 2013 as the CPI is likely to ease to 3.6%YoY in April and domestic demand remains lacklustre. The balance of payments remains supportive for the koruna, which however is likely to be temporarily hit later this year owing to the EMU crisis.

Romania

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Recent growth indicators suggest that economic activity continues to lose momentum following the softer 4Q GDP reading. Sentiment indicators also paint a similar picture, thereby raising concerns about the sustainability of the economic recovery. The noted backdrop, coupled with the low March inflation reading and the benign outlook, is likely to lead the NBR keeping its easing bias during the remainder of the year, provided that exchange rate stability is not threatened. Slippages in the implementation of fiscal policy and structural reforms supported by the EU-IMF program ahead of the upcoming elections emerge as additional risk factors that could lead the NBR to revise its current stance. With these risk factors in mind, we expect the Bank to bring its policy rate to 5.0%, or even lower if the leu permits, by the end of 2012. However, the possibility of lower interest rates and the pause in the external adjustment (with the 12-month rolling trade deficit stuck at around €10.0bn) paint a more challenging picture for the leu, which seems to have been lagging behind its peers in the region since the beginning of the year. Looking ahead, the evolution of the leu and growth indicators will gain additional importance for the markets and policymakers, as elections approach.

Figure 38. Czech Republic and Romania — Economic Forecasts, 2011-2013F

		Czech Republic			Romania		
		2011	2012F	2013F	2011	2012F	2013F
Real GDP	YoY	1.7%	-0.4%	1.6%	2.5%	1.7%	3.2%
Final Domestic Demand	YoY	-1.0	-0.9	1.1	1.9	1.1	2.9
Private Consumption	YoY	-0.7	-0.5	0.9	1.3	1.1	2.9
Fixed Investment	YoY	-1.5	-1.0	2.2	6.2	1.5	3.5
Exports	YoY	11.1	1.5	2.9	10.5	5.4	4.2
Imports	YoY	7.4	-0.3	2.8	11.5	4.8	3.2
CPI	YoY	1.9	3.3	2.8	5.8	2.8	2.7
Unemployment Rate	%	8.5	8.9	9.0	5.4	5.2	5.2
Current Account	US$ bn	-6.3	-7.6	-5.2	-7.9	-8.1	-9.0
	% of GDP	-2.9	-3.8	-2.5	-4.2	-4.5	-4.7
Fiscal Balance	% of GDP	-3.1	-3.1	-2.8	-4.1	-2.0	-2.0
US Dollar Exchange Rate	Average	24.6	24.7	24.8	4.24	4.35	4.23

Sources: Haver Analytics and Citi Investment Research and Analysis

Brazil

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Activity data continue to point toward stronger growth in 1Q12. We keep our 1Q12 GDP growth forecast of 0.8% QoQ, higher than the 0.3% figure seen in the previous quarter. Looking ahead, meaningful monetary, credit and fiscal stimuli point to a further acceleration in coming quarters, with GDP likely to expand above potential growth during the second half of this year. All in all, we maintain our 2012 and 2013 GDP growth forecasts at 3.3% and 4.5%, respectively. In terms of inflation, despite the favourable surprise in March's CPI, we continue to expect year-end 2012 and 2013 CPI inflation at 5.3% and at 5.6%, respectively, both above the mid point target of 4.5%. Copom likely has finished the easing cycle with the Selic rate at 9%. Given the increasing risks on the inflation front, we expect it to begin the tightening cycle next year, raising the Selic up to 10.50% in the first three Copom meetings of 2013. On FX front, the government maintains a tough stance about tighter capital controls over FX markets, trying to keep BRL at a more depreciated level than that suggested by fundamentals. On the fiscal side, the primary surplus should remain at a level consistent with a downward trend in public debt/GDP.

Mexico

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Economic activity began 2012 on a solid footing, with the Global Index of Economic Activity (a proxy for monthly GDP) up 4.4% y/y in January versus 3.9% in 2011. More recent information, such as that of industrial production for the month of February, suggests a bit of a deceleration in external demand but probably compensated by a more robust domestic market. Thus, we now expect GDP growth of 4.1% y/y in 1Q12 instead of 3.7% before; as a consequence, we revised up our GDP growth forecast to 3.5% for 2012 as a whole from 3.3% before. Inflation meanwhile has declined in annual terms, to 3.7% in March versus 3.9% in February, although mostly on the back of favourable results for non-core prices. Accordingly, we still expect annual inflation to rise in the coming months, reaching its peak at around 4.4% in 3Q. This, along with the fact that the presidential election will take place in July, suggests that for monetary policy purposes, if a one-off adjustment in the policy rate is deemed necessary, it should take place soon. Our reading of the last set of Banxico's minutes suggests that this is indeed the case for the majority of the board and, therefore, we now call for a 50bp cut by Banxico on April 27 after which, we see the central bank remaining on hold at 4% for the rest of the year. In line with this, and taking into account recent episodes of global risk aversion, we now see the USD/MXN closing 2012 at 12.80 versus our previous forecast of 12.25.

Figure 39. Brazil and Mexico — Economic Forecasts, 2011-2013F

		Brazil			Mexico		
		2011	2012F	2013F	2011	2012F	2013F
Real GDP	YoY	2.7%	3.3%	4.5%	3.9%	3.5%	3.6%
Final Domestic Demand	YoY	3.8	3.9	4.8	5.0	4.2	4.3
Private Consumption	YoY	4.1	4.1	4.8	4.6	3.8	3.8
Fixed Investment	YoY	4.7	4.2	6.5	8.7	6.6	7.3
Exports	YoY	4.5	5.8	6.2	6.7	7.0	8.7
Imports	YoY	9.7	8.4	7.0	6.8	7.6	10.8
CPI	YoY	6.6	5.2	5.4	3.4	4.1	3.7
Unemployment Rate	%	6.1	6.3	6.5	5.3	5.2	5.3
Current Account	US$ bn	-48.6	-51.4	-65.4	-8.7	-18.5	-25.3
	% of GDP	-2.1	-2.1	-2.4	-0.8	-1.6	-1.9
Fiscal Balance	% of GDP	-2.6	-1.9	-2.6	-2.5	-2.2	-2.0
US Dollar Exchange Rate	Average	1.67	1.82	1.75	12.44	12.94	12.40

Sources: Haver Analytics and Citi Investment Research and Analysis

Argentina

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Virtually every activity indicator now shows that GDP growth is slowing sharply; including official estimators, which have been systematically overestimating growth during the last couple of years. Needless to say, the government's anti-market posture in response to the slowdown— exchange controls, trade protectionism, increased fiscal dependence on the central bank, and hostility towards foreign investment (e.g the actions taken recently by the national government and several provinces against Repsol-YPF)—does not help. On this basis, we are revising our official 2012 GDP forecast to 3% from 4%, below the benchmark needed to trigger a payment on the warrant in 2013. Additionally, we expect our in-house real GDP estimator to report a 1% growth rate for both 2012 and 2013. While we keep our 2012 year-end ARS/USD forecast unchanged at 4.8, we believe that the probability of a step devaluation increases significantly next year. We are, therefore, revising our forecasts for 2013 official GDP growth to 3% from 4.0% last month. For further details, please refer to our Argentina Macro View - Going South.

Venezuela

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President Chávez is leading the race for the presidency, according to the first polls since Henrique Capriles was officially elected as the opposition candidate. There are nevertheless significant differences between polls; in one, Mr. Chávez's lead over Mr. Capriles is statistically small, whereas in the other the difference is closer to 13 percentage points. On a related note, President Chávez continues with his radiation treatment. Although official statements have not provided more details about the President’s health condition, his health continues to be of concern. Meanwhile, the economic recovery continues with the impulse provided by heavy levels of fiscal spending, while inflation has not accelerated despite the putting in place of the law of costs and fair prices. We anticipate inflation will eventually pick up as the result of decreases in availability of products. For the time being there are no announcements of new dollar-denominated debt issuance, but we do not discard this possibility as it is necessary to guarantee SITME’s operations after July.

Figure 40. Argentina and Venezuela — Economic Forecasts, 2011-2013F

		Argentina			Venezuela		
		2011	2012F	2013F	2011	2012F	2013F
Real GDP	YoY	8.9%	3.0%	3.0%	4.2%	4.0%	3.4%
Final Domestic Demand	YoY	12.0	3.3	3.8	7.6	3.4	1.7
Private Consumption	YoY	10.7	2.8	2.8	4.0	8.0	0.7
Fixed Investment	YoY	-	-	-	4.4	-7.0	2.2
Exports	YoY	4.3	1.9	2.1	4.7	8.2	5.2
Imports	YoY	17.8	5.2	6.5	15.4	3.6	-0.9
CPI	YoY	9.8	9.6	12.2	27.1	26.1	28.6
Unemployment Rate	%	8.1	7.8	8.2	6.5	6.4	6.6
Current Account	US$ bn	1.8	1.5	1.1	27.2	25.7	30.6
	% of GDP	0.4	0.3	0.2	9.1	6.9	8.4
Fiscal Balance	% of GDP	-1.6	-3.0	-3.0	-5.0	-5.0	-4.0
US Dollar Exchange Rate	Average	4.13	4.55	5.45	4.3	4.3	6.5

Sources: Haver Analytics and Citi Investment Research and Analysis

Saudi Arabia

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Concerns regarding global oil supply prompted Saudi Arabia to maintain its highest production in over 30 years as it repeatedly seeks to demonstrate that it will compensate for any supply shortfalls. March figures show Saudi production steady at 9.7mbpd, and we believe this is likely to be maintained for the rest of 2012, meaning an increase in average production of around 5% over last year. This has prompted us to raise our GDP growth forecast to 7.1% in 2012, from 5.9% previously. With oil prices likely to average US$110 per barrel this year, we think the surge in production will result in record fiscal revenues. Expenditures will once again overshoot budget (although will remain lower than 2011 levels due to the one-off nature of many such expenditures), but the net result will be a budget surplus of around 16.5% of GDP in 2012, up from just under 14% in 2011. We believe growth in the non-oil economy will remain strong, around 8.5%, on the back of continued high government expenditure and increased domestic demand. We continue to expect progress on passing of the mortgage law in 2012, which we believe will create a significant boost to the local housing sector and domestic demand. Meantime, inflation remains sticky, flat at 5.4% in March, but we continue to expect demand side pressure to pose a significant threat to price stability in the coming months.

United Arab Emirates

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The Central Bank issued a circular in April updating its rules on large exposures. As of the date of the circular (4th April), UAE banks will have to limit their exposure to the local emirate governments and their non-commercial entities to 100% of their capital base. No individual exposure can exceed 25%. The motivation for the regulations is to ring-fence the domestic financial system from concerns over the sustainability of public sector debt in certain emirates. Local banks are a key source of liquidity for GREs and help support their refinancing strategies. That said, we do not believe the likelihood of strict enforcement of the rules is high, and see sufficient ambiguity in the regulations to provide scope for regulatory forbearance. Meanwhile, Dubai Drydocks has applied for insolvency protection under Dubai Decree 57, having lost a lawsuit the previous month to one of its minority creditors, Monarch Capital. This will be the first test of the insolvency regime since its establishment in 2009. DIC, a private equity arm of Dubai Holding Group, finally reached an agreement with creditors over the restructuring of US$2.5bn in debt.

Figure 41. Saudi Arabia and United Arab Emirates — Economic Forecasts, 2011-2013F

		Saudi Arabia			United Arab Emirates		
		2011	2012F	2013F	2011	2012F	2013F
Real GDP	YoY	6.8%	7.1%	6.5%	5.3%	0.5%	3.4%
Final Domestic Demand	YoY	7.7	7.8	7.9	3.0	3.4	3.4
Private Consumption	YoY	3.9	5.0	5.0	1.0	2.0	2.0
Fixed Investment	YoY	13.5	10.0	10.0	5.0	5.0	5.0
Exports	YoY	10.7	15.0	1.5	13.0	13.0	13.0
Imports	YoY	1.4	15.0	15.0	15.0	15.0	15.0
CPI	YoY	5.0	7.0	8.0	0.9	1.1	1.3
Current Account	US$ bn	154.3	183.1	160.9	48.7	11.9	20.7
	% of GDP	26.8	29.2	24.4	15.0	3.5	5.7
Fiscal Balance	% of GDP	13.7	20.5	12.2	-	-	-
US Dollar Exchange Rate	Average	3.75	3.75	3.75	3.67	3.67	3.67

Sources: Haver Analytics and Citi Investment Research and Analysis

Nigeria

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After a prolonged period of political consolidation following the 2011 elections, there have been tentative signs in early 2012 that the reform effort of the new administration is getting under way. The first step was in January when the government only partially backtracked on its plan to raise in domestic petrol prices, but there has also been a slow build in reserves and the start of progress with electricity sector reform. Despite slow progress with reform and the ongoing political uncertainties in Nigeria, notably in the north due to the activities of Boko Haram, we still expect growth to remain robust in 2012-13 driven by strong activity in the south of the country. Meanwhile, the combination of improved fiscal discipline, clamping down on capital flight, higher interest rates and recovering oil production has allowed the Central Bank of Nigeria (CBN) to maintain naira stability in early 2012. We expect the CBN to maintain naira stability in 2012, unless there is a significant fall in the oil price, which, coupled with easing food price inflation, should help reduce inflationary pressures as the year progresses and even allow some modest cuts in its monetary policy rate in early 2013.

South Africa

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The 22 February budget highlighted the unfavourable external environment facing the country and that growth, which is now officially forecast at only 2.7% in 2012, will remain sub-par and only start to really recover into 2013. Although the Treasury remains committed to budget deficit reduction and debt stabilisation – focusing more on micro policy steps to foster stronger growth – weak revenue growth and pressure from the public wage bill mean that a significant reduction in the deficit is only likely in 2013. In the meantime, even with weak housing sector growth and rising inflation eroding household purchasing power, the ongoing monetary stimulus is supporting resilient consumer spending, while corporate finances are healthy and there are signs of an upturn in private investment. We expect no immediate change in the monetary policy stance, with a rate hike unlikely before 2H12 and only gradual normalisation afterwards, although inflation will probably hover around the top end of the 3%-6% target range in the next 15 months. However, we think it is unlikely to make a sustained breach of the upper limit, even if rand fragility and wage stickiness pose upside risks. Poor export performance and the high import content of capital spending suggest that the current account deficit will gradually widen, after being kept low by favourable terms of trade.

Figure 42. Egypt, Nigeria and South Africa — Economic Forecast, 2011-2013F

		Egypt			Nigeria			South Africa		
		2011	2012F	2013F	2011	2012F	2013F	2011	2012F	2013F
Real GDP	YoY	1.8%	3.0%	3.9%	7.8%	7.4%	7.0%	3.1%	2.9%	3.8%
Final Domestic Demand	YoY	2.9	3.7	3.8	NA	NA	NA	4.6	3.3	4.0
Private Consumption	YoY	5.0	0.2	1.5	NA	NA	NA	4.9	2.8	3.3
Fixed Investment	YoY	-5.6	9.9	3.4	NA	NA	NA	4.3	4.4	5.7
Exports	YoY	3.7	-3.8	6.3	NA	NA	NA	5.9	5.3	6.2
Imports	YoY	8.1	-2.3	5.5	NA	NA	NA	9.1	6.7	7.0
CPI	YoY	10.2	10.4	11.3	10.8	12.2	10.0	5.0	6.0	5.4
Unemployment Rate	%	12.1	13.0	14.5	NA	NA	NA	26.0	25.7	25.2
Current Account	US$ bn	-5.4	-6.8	-8.8	15.9	16.5	21.9	-13.6	-18.8	-23.0
	% of GDP	-2.3	-2.7	-3.3	5.9	5.2	6.0	-3.4	-4.7	-5.6
Fiscal Balance	% of GDP	-10.1	-9.0	-7.3	-3.0	-2.1	-2.0	-5.0	-4.8	-4.2
US Dollar Exchange Rate	Average	5.94	6.07	6.63	155	160	165	7.26	8.06	8.61

Source: Citi Investment Research and Analysis

Figure 43. Selected Emerging Market Countries — Economic Forecast Overview, 2011-2013F

	GDP Growth			CPI Inflation			Current Balance (% of GDP)			Fiscal Balance (% of GDP)		
	2011	2012F	2013F	2011	2012F	2013F	2011	2012F	2013F	2011	2012F	2013F
Asia	**7.2%**	**6.9%**	**7.3%**	**5.7%**	**4.2%**	**4.1%**	**2.3%**	**1.6%**	**1.2%**	**-2.2%**	**-2.6%**	**-2.2%**
China	9.2	8.4	8.6	5.4	3.5	3.5	2.8	2.0	1.5	-1.3	-2.0	-1.5
Hong Kong	5.0	3.0	4.2	5.3	4.0	2.9	5.1	13.1	12.2	3.5	0.8	0.7
India*	6.9	7.0	7.5	9.0	7.0	6.5	-4.0	-4.0	-3.3	-8.4	-8.0	-7.7
Indonesia	6.5	6.2	6.5	5.4	5.8	5.3	0.2	-0.7	-0.8	-1.2	-1.8	-0.7
Korea	3.6	3.7	4.4	4.0	3.1	3.4	2.5	1.1	0.7	1.5	1.4	1.2
Malaysia	5.1	5.0	5.3	3.2	2.5	2.8	11.5	10.5	9.0	-5.0	-5.0	-4.7
Pakistan	2.8	3.1	4.2	10.5	11.0	11.0	-2.8	-3.6	-3.8	-6.5	-6.2	-5.5
Philippines	3.7	4.6	5.0	4.8	3.5	4.0	3.1	3.1	2.4	-2.0	-2.8	-2.0
Singapore	4.9	3.6	5.0	5.2	3.8	3.2	21.9	15.0	13.0	1.5	1.0	1.0
Sri Lanka	8.3	7.4	7.6	6.8	7.5	7.0	-7.9	-6.9	-5.9	-7.0	-6.2	-5.3
Taiwan	4.0	3.5	4.2	1.4	1.9	2.1	8.8	8.7	8.4	-1.9	-1.6	-1.3
Thailand	0.1	4.7	5.0	3.8	2.9	3.3	3.4	-1.3	-0.5	-1.5	-3.8	-2.7
Vietnam	5.9	5.0	5.6	18.6	10.4	8.0	-1.1	-1.2	-3.7	-5.0	-4.8	-4.5
Latin America	**4.2%**	**3.6%**	**4.2%**	**7.0%**	**6.3%**	**6.6%**	**-1.0%**	**-1.3%**	**-1.5%**	**-2.3%**	**-2.1%**	**-2.4%**
Argentina	8.9	3.0	3.0	9.8	9.6	12.2	0.4	0.3	0.2	-1.6	-3.0	-3.0
Brazil	2.7	3.3	4.5	6.6	5.2	5.4	-2.1	-2.1	-2.4	-2.6	-1.9	-2.6
Chile	6.0	4.2	5.0	3.3	3.7	3.2	-1.3	-1.9	-1.9	1.6	0.7	0.6
Colombia	5.9	5.0	4.5	3.4	3.5	3.7	-3.0	-3.1	-2.9	-2.9	-3.0	-2.5
Mexico	3.9	3.5	3.6	3.4	4.1	3.7	-0.8	-1.6	-1.9	-2.5	-2.2	-2.0
Panama	10.6	7.0	7.0	5.9	5.6	3.2	-12.7	-11.8	-10.2	-2.3	-2.7	-1.5
Peru	6.9	5.5	6.5	3.4	3.7	2.9	-1.3	-2.4	-2.8	1.7	1.2	-0.3
Venezuela	4.2	4.0	3.4	27.1	26.1	28.6	9.1	6.9	8.4	-5.0	-5.0	-4.0
Europe	**5.0%**	**2.8%**	**3.7%**	**6.7%**	**5.6%**	**5.8%**	**-0.1%**	**-0.25**	**-1.4%**	**-0.3%**	**-1.2%**	**-1.1%**
Czech Republic	1.7	-0.4	1.6	1.9	3.3	2.8	-2.9	-3.8	-2.5	-3.1	-3.1	-2.8
Hungary	1.7	0.0	1.4	3.9	5.6	3.5	1.7	1.2	1.5	4.2	-3.2	-3.0
Kazakhstan	7.5	6.3	6.3	8.3	5.0	6.4	7.6	1.9	2.3	5.9	1.7	3.0
Poland	4.3	2.7	2.4	4.3	3.9	2.7	-4.1	-3.7	-3.9	-5.1	-3.3	-2.7
Romania	2.5	1.7	3.2	5.8	2.8	2.7	-4.2	-4.5	-4.7	-4.1	-2.0	-2.0
Russia	4.3	3.5	4.0	8.4	5.3	7.0	5.2	5.2	2.1	2.0	0.3	0.1
Slovakia	3.3	1.5	2.1	3.9	3.5	2.9	0.2	0.3	0.2	-4.8	-4.8	-3.2
Turkey	8.5	2.5	4.3	6.5	9.6	7.0	-10.0	-8.5	-8.3	-1.3	-2.2	-2.5
Ukraine	5.1	3.0	4.5	8.0	3.4	7.2	-5.2	-7.7	-4.4	-3.8	-3.4	-3.5
Africa/Mideast	**5.9%**	**4.1%**	**5.1%**	**5.5%**	**6.1%**	**6.0%**	**11.6%**	**11.0%**	**13.3%**	**2.3%**	**3.5%**	**2.8%**
Bahrain	3.2	3.0	3.9	-0.4	3.0	3.5	11.6	29.2	21.4	-1.2	4.8	5.1
Egypt	1.8	3.0	3.9	10.2	10.4	11.3	-2.3	-2.7	-3.3	-10.1	-9.0	-7.3
Ghana	14.4	7.5	6.5	8.7	10.2	11.6	-8.6	-7.5	-4.8	-5.4	-5.6	-4.7
Iraq	9.4	12.4	11.2	5.6	5.0	6.0	-5.1	31.9	65.2	15.8	16.0	24.0
Israel	4.9	2.7	3.0	3.4	2.6	2.7	0.1	-1.5	-1.0	-2.7	-3.2	-2.7
Jordan	2.3	2.5	3.0	4.4	5.0	5.0	-11.3	-6.0	-5.2	-3.9	-8.0	-9.5
Kenya	4.7	5.2	5.8	12.1	11.5	8.5	-8.2	-7.5	-6.5	-5.5	-5.0	-4.9
Kuwait	4.3	0.2	2.5	4.7	5.0	5.0	47.5	45.6	46.8	17.1	17.1	13.9
Lebanon	6.0	3.5	4.3	5.1	6.0	5.0	-14.7	-11.1	-12.0	-6.4	-7.5	-8.6
Nigeria	7.8	7.4	7.0	10.8	12.2	10.0	5.9	5.2	6.0	-3.0	-2.1	-2.0
Oman	4.9	3.0	4.5	4.0	3.0	3.0	3.4	2.6	21.3	5.4	4.4	3.9
Qatar	18.1	6.0	8.3	3.0	3.0	3.0	38.7	33.5	29.5	8.1	4.9	2.9
Saudi Arabia	6.8	7.1	6.5	5.0	7.0	8.0	26.8	29.2	24.5	13.7	20.5	12.2
South Africa	3.1	2.9	3.8	5.0	6.0	5.4	-3.4	-4.7	-5.6	-5.0	-4.8	-4.2
Tanzania	6.3	6.7	7.0	12.7	15.7	7.4	-8.5	-7.8	-9.1	-7.8	-6.2	-5.8
UAE	5.3	0.5	3.4	0.9	1.1	1.3	15.0	3.5	5.7	NA	NA	NA
Uganda	5.7	4.5	6.1	18.6	16.4	6.0	-4.0	-8.9	-8.0	-7.2	-5.5	-5.2
Zambia	6.6	6.5	6.9	8.7	7.5	8.0	4.2	1.2	-2.5	-3.2	-4.2	-5.2
Total	**6.1%**	**5.2%**	**5.8%**	**6.1%**	**5.1%**	**5.1%**	**2.3%**	**1.8%**	**1.6%**	**-1.5%**	**-1.7%**	**-1.6%**

* Note: In India, policymakers look at the wholesale price index. Sources: National sources and Citi Investment Research and Analysis

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Source: Citi Investment Research and Analysis.

Figure 45. Citi Global Strategy and Macro Team *For Informational Purposes Only*

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Source: Citi Investment Research and Analysis.

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Sovereign Ratings Outlook

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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. This publication does 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. The full piece is released roughly once per quarter, with a brief summary in the "*Global Economic Outlook and Strategy*".

Figure 46. Advanced Economies — Sovereign Long-Term Debt Ratings and Citi Ratings Forecasts

	S&P Ratings				Moody's Ratings			
Country	Current Rating	Current Outlook	Citi Nearterm (Up to 9 Months) Forecast Rating	Citi Longterm (Next 2-3 Years) Forecast Rating & Outlook	Current Rating	Current Outlook	Citi Nearterm (Up to 9 Months) Forecast Rating	Citi Longterm (Next 2-3 Years) Forecast Rating & Outlook
US	AA+	Neg	AA+ (Neg)	AA ↓	Aaa	Neg	Aaa (Neg)	Aa1 ↓
Canada	AAA	Stable	AAA	AAA	Aaa	Stable	Aaa	Aaa
Japan	AA-	Neg	AA- (Neg)	A+ ↓	Aa3	Stable	Aa3	A1 ↓
Germany	AAA	Stable	AAA	AAA (Neg)	Aaa	Stable	Aaa	Aaa (Neg)
France	AA+	Neg	AA+ (Neg)	AA ↓	Aaa	Neg	Aaa (Neg)	Aa1 ↓
Italy	BBB+	Neg	BBB ↓	BBB- ↓↓	A3	Neg	Baa1 ↓	Baa3 ↓↓↓
Spain	A	Neg	BBB+ ↓↓	BBB ↓↓↓	A3	Neg	Baa1 ↓	Baa2 ↓↓
Austria	AA+	Neg	AA+ (Neg)	AA ↓	Aaa	Neg	Aaa (Neg)	Aa1 ↓
Belgium	AA	Neg	AA (Neg)	AA- ↓	Aa3	Neg	Aa3 (Neg)	Aa3
Finland	AAA	Neg	AAA (Neg)	AA+ ↓	Aaa	Stable	Aaa	Aaa (Neg)
Greece	SD		CCC ↑↑↑↑	CCC ↑↑↑↑	C		Caa2 ↑↑↑↑	Caa2 ↑↑↑↑
Ireland	BBB+	Neg	BBB- ↓↓	BB ↓↓↓↓	Ba1	Neg	Ba1 (Neg)	Ba3 ↓↓
Netherlands	AAA	Neg	AAA (Neg)	AA+ ↓	Aaa	Stable	Aaa	Aaa (Neg)
Portugal	BB	Neg	B+ ↓↓	CCC ↓↓↓↓↓	Ba3	Neg	B1 ↓	Caa2 ↓↓↓↓↓
UK	AAA	Stable	AAA	AAA (Neg)	Aaa	Neg	Aaa (Neg)	Aaa (Neg)
Switzerland	AAA	Stable	AAA	AAA	Aaa	Stable	Aaa	Aaa
Sweden	AAA	Stable	AAA	AAA	Aaa	Stable	Aaa	Aaa
Denmark	AAA	Stable	AAA	AAA	Aaa	Stable	Aaa	Aaa
Norway	AAA	Stable	AAA	AAA	Aaa	Stable	Aaa	Aaa

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. In the outlook we have not included an extension of the actual EFSF lending beyond the now targeted €440bn maximum capacity. In the event that a substantial extension of the EFSF takes place and is likely to incur sizeable fiscal costs, various Euro Area countries may be at risk of downgrade. NA Not available.

Sources: Moody's, S&P and Citi Investment Research and Analysis

Key Expected Ratings Issues

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Citi continues to expect further downgrades over the longer-term (2-3 years, see Figure 46) Our view is predicated on many factors from deteriorating economic prospects, failure to meet fiscal targets and various idiosyncratic factors including political risks. Our broad views remain largely unchanged and reflect the fact that for many of the countries covered in *Citi's Sovereign Ratings Outlook*, S&P and Moody's already have many on Negative Outlook. We continue to adjust our view on likely short-term rating migration to accommodate new information provided by the rating agencies, our longer-term expectations and the ongoing fundamental and market dynamics.

We highlight key changes since we last published as well as our economists' and strategists' main expectations for sovereign ratings over the near-term.

Spain: We believe that following the 2.5% of GDP deficit overshoot for 2011, Spain will not hit the 5.3% of GDP deficit target in 2012. In our view, the Government's debt stock for 2012 is likely to increase to 84% of GDP. In addition, government bond yields remain elevated after the recent Budget 2012 announcements and, while Spanish banks are unlikely to run out of LTRO-based liquidity just yet, the boost to their purchases of Spanish government debt has probably peaked. We expect that Spain will need to enter some form of a troika programme late in 2012, largely focussed on measures to recapitalise and restructure the banks (*Focus on Spain*). Overall, we expect a two-notch downgrade of the Spanish Sovereign later this year by S&P and a one-notch downgrade by Moody's.

Italy: Over the short-term (next 9 months), we believe that Italy will be downgraded further by one notch to BBB by S&P and to Baa1 by Moody's to reflect slow progress with the implementation of the reform agenda. While the recent criticism of the Monti government's labour market reform might be overstated by the approaching regional elections in May, the falling public support for PM Mario Monti in opinion polls suggests that the government will face increasing difficulties in going ahead with the implementation of structural reforms.

Portugal: Over the short-term (next 6-9 months), we believe that Portugal will be downgraded further by two notches to B+ by S&P and by one notch to B1 by Moody's to reflect the deeper than anticipated recession and the sharp increase in unemployment which will make achieving this year's deficit target almost impossible. With the resulting risks of a negative market reaction, it is likely to become more evident to the Troika that Portugal will be unable to access the markets in the 2nd half of next year as targeted under the Troika programme.

Ireland: We continue to doubt that the current tight fiscal policies will return Ireland to a sustainable fiscal path (*Ireland — Tough Times Ahead*). After strong economic growth in early 2011, the economy recently has slipped back into recession and we expect that continued economic underperformance will cause government revenues to undershoot - and the deficit to overshoot - versus official forecasts in 2012 and beyond. We maintain that downward pressure on Ireland's rating is likely to emerge and look for S&P's rating to move towards BBB- later in 2012.

UK: We regard the UK as a relatively weak AAA and still see risks that S&P will put the UK on "negative outlook" at some stage. However, in light of their recent comments[8], we have postponed such a move from "the next 2-3 quarters" to "the next 2-3 years"

[8] S&P RatingsDirect: "*Ratings On The United Kingdom Affirmed at 'AAA/A-1+'; Outlook Stable*", 13 April 2012

Rates Strategy

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The past month has seen a sharp increase in market volatility. 10yr US Treasuries have traded as low as 1.98% and as high as 2.36% and the rolling average monthly trading range has risen from about 20-25bp in Q1 to about 40bp at the time of writing. We believe that this increased volatility in core rates markets is due to a relative decline in the ranges that EMU spreads are trading and a concomitant shift of focus towards domestic macro-economic fundamentals. In our view the recent widening of Spanish spreads was not the cause for the sell-off in equity markets, but equally the weak US employment report and the ensuing equity weakness was not entirely responsible for the move in Spain. These were, in our opinion, coincident reactions in a market in which confidence had got a little ahead of itself.

Our broader outlook for rates markets is still for range trading with a geographical divergence. The sell-off in 10yr Treasuries saw the old 1.80%-2.10% range broken to the upside and we are now probably looking at a range that will be more like 1.90%-2.35%. Meanwhile the latest rally has seen 10yr Bund yields making new lows so we expect the old 1.75%-2.00% range to become something more like 1.60%-1.90%. Such a move would imply a 10yr US Treasury-Bund spread of about 40bp against the current level of 25bp. Over the course of the year we expect the centre of the US range to continue to edge up towards 2.50% but believe that Bunds will hold around current levels, further widening the spread.

EMU spreads made new lows in the aftermath of LTRO2 but have since re-widened, led by Spain on renewed concerns over the ability and commitment to meeting deficit targets and the health of the banking sector. We think that the sell-off in Bonos may, however, be getting overdone. Much of the challenge Spain faces are within the banking sector rather than at the sovereign level and we note that Spain has now completed 47% of its gross issuance. Perhaps more significantly we estimate that by the end of April Spain will have completed almost all of its expected net financing requirement for 2012. This means that the remainder of the year's issuance will be offset by coupon and redemption payments. We do not want to underestimate the severity of the challenges facing EMU and we certainly expect a protracted period of high stress, further ratings downgrades and volatile spreads. We do not, however, expect a repeat of the November 2011 episode in which the market began to price an EMU break-up at the current time.

Yield curves remain quite directional, with the US and UK curves bull flattening and bear steepening. We expect this to persist. We continue to think, however, that the 5yr-10yr sector of the German curve looks to steep relative to other curves.

Figure 47. Interest Rate and Bond Market Forecasts (End of Period), as of 18 April 2012

		Forecast End Period					
	Current	2Q 12	3Q 12	4Q 12	1Q 13	2Q 13	3Q 13
US							
Policy Rate (Fed Funds) End Quarter	0.25	0.25	0.25	0.25	0.25	0.25	0.25
3-Month Libor	0.47	0.48	0.50	0.55	0.65	0.75	0.90
2 Year Treasury Yield	0.27	0.35	0.40	0.50	0.65	0.85	1.00
5 Year Treasury Yield	0.82	1.10	1.25	1.40	1.50	1.70	1.85
10 Year Treasury Yield	2.01	2.30	2.45	2.50	2.60	2.75	3.00
30 Year Treasury Yield	3.09	3.50	3.65	3.70	3.80	4.00	4.25
2-10 Year Treasury Curve	174	195	205	200	195	190	200
2 Year Swap Spread (Swap Less Govt.), bp	30	40	40	35	35	35	35
10 Year Swap Spread (Swap Less Govt.), bp	11	15	20	22	24	25	25
30 Year Swap Spread (Swap Less Govt.), bp	-30	-35	-40	-50	-50	-50	-50
30 Year Mortgage Yield	3.88	4.05	4.20	4.35	4.50	4.70	4.85
10 Year Breakeven Inflation	225	235	235	235	235	240	240
Euro Area							
Policy Rate	1.00	1.00	1.00	1.00	0.75	0.75	0.50
Overnight Rate (EONIA)	0.35	0.35	0.35	0.35	0.20	0.20	0.15
3-Month Libor	0.66	0.67	0.58	0.50	0.50	0.50	0.50
2 Year Treasury Yield	0.13	0.15	0.20	0.25	0.25	0.35	0.50
5 Year Treasury Yield	0.68	0.70	0.75	0.75	0.85	1.00	1.25
10 Year Treasury Yield	1.75	1.75	1.70	1.75	1.80	2.00	2.25
30 Year Treasury Yield	2.39	2.60	2.65	2.65	2.75	2.80	2.95
2-10 Year Treasury Curve	162	160	150	150	155	165	175
10 Year BTP-Bund Spread	372	375	350	325	300	250	200
10 Year Swap Spread (Swap Less Govt.), bp	47	50	50	45	40	35	30
10 Year Breakeven Inflation	178	170	175	180	190	195	200
Japan							
Policy Rate	0.10	0.10	0.10	0.10	0.10	0.10	0.10
3-Month Libor	0.20	0.20	0.20	0.20	0.20	0.20	0.20
2 Year Treasury Yield	0.11	0.10	0.10	0.15	0.15	0.20	0.20
5 Year Treasury Yield	0.30	0.30	0.35	0.45	0.55	0.65	0.65
10 Year Treasury Yield	0.95	0.95	1.00	1.20	1.30	1.40	1.40
30 Year Treasury Yield	1.92	1.95	2.00	2.15	2.20	2.30	2.30
2-10 Year Treasury Curve	84	85	90	105	115	120	120
2 Year Swap Spread (Swap Less Govt.), bp	24	24	26	28	28	30	30
10 Year Swap Spread (Swap Less Govt.), bp	2	2	4	7	8	10	10
10 Year Breakeven Inflation	NA	NA	NA	NA	NA	NA	NA
UK							
Policy Rate	0.50	0.50	0.50	0.50	0.50	0.50	0.50
3-Month Libor	1.02	1.00	0.90	0.85	0.85	0.90	1.00
2 Year Treasury Yield	0.40	0.40	0.40	0.40	0.40	0.50	0.60
5 Year Treasury Yield	0.94	1.00	0.95	1.00	1.00	1.15	1.30
10 Year Treasury Yield	2.08	2.10	2.10	2.15	2.20	2.40	2.65
30 Year Treasury Yield	3.25	3.25	3.10	3.00	3.00	3.15	3.35
2-10 Year Treasury Curve	168	170	170	175	180	190	205
10 Year Swap Spread (Swap Less Govt.), bp	30	25	35	35	40	40	40
10 Year Breakeven Inflation	278	265	250	260	275	285	300
Australia							
Policy Rate	4.25	4.00	4.00	4.00	4.25	4.50	4.50
3-Month Libor	4.28	4.20	4.20	4.40	4.50	4.70	4.70
2 Year Treasury Yield	3.34	3.60	3.90	4.00	4.30	4.60	4.75
5 Year Treasury Yield	3.42	3.80	4.00	4.10	4.40	4.70	4.90
10 Year Treasury Yield	3.88	4.20	4.30	4.50	4.80	5.00	5.10
2-10 Year Treasury Curve	54	60	40	50	50	40	35
10 Year Swap Spread (Swap Less Govt.), bp	80	80	75	70	65	60	60

Source: Citi Investment Research and Analysis

Credit Outlook

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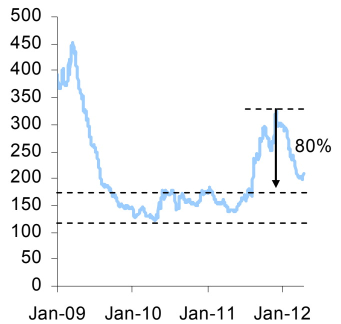
A lot changed in Q1 2012 and for the credit outlook it wasn't for the better:

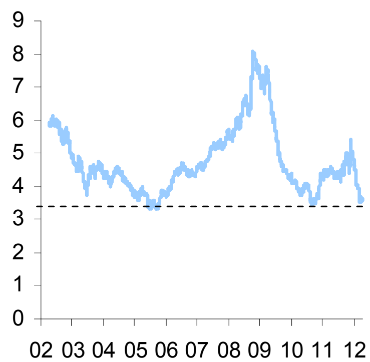
- The iBoxx € Corporate index returned 5.6% in total (4.0% in spread returns) in Q1 alone – enough that many funds have met their full-year targets. It must be tempting to scale back and lock in the performance.
- In spread terms, the iBoxx € index retraced more than 80% of the way back to the range from H1 2011 (Figure 48).
- Yields on IG credit are near historic lows (see Figure 49). When was the last time we saw corporate bonds issued with a 2% coupon handle?
- New issue premia got to rock-bottom levels in March – in fact some recent issues priced tight to secondaries. Now most are substantially wider than re-offer.
- By the end of Q1, cash prices on financial sub debt had in many cases reached levels where the LME exercises that were a key support don't work any longer.
- Relative value on periphery credits doesn't look compelling – many corporates remain comparatively tight versus their sovereigns.
- US economic surprises indices started Q1 at +83. Now it's at +5 (see Figure 50).
- The long-awaited rating actions to reflect changes in Moody's assessment of the banking sector are likely to occur over the next few weeks. Some banks will likely see their sub debt fall into high yield; others are likely to lose their prime short-term ratings with uncertain implications on their liquidity given the possibility of collateral calls. A few banks that fall to triple-B may at least temporarily lose the ability to roll funding arrangements with some counterparties.
- Elections in France (22 April and 6 May) and Greece (6 May) are approaching with the parties favoured by markets not looking strong in opinion polls.
- But worst of all, the European sovereign crisis seems on the verge of entering a new phase as spreads on Spain push to their highest levels since November.

Figure 48. iBoxx spread retracing to old range? (bp)



Source: CIRA, Markit

Figure 49. iBoxx yield at historic low (%)



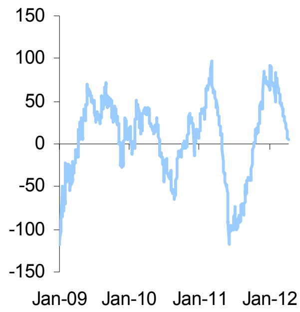
Source: CIRA, Markit

Add all of these factors together and it may seem hard to be anything but outright bearish. But to our minds, the real questions are 1) whether the news flow is really more negative than what the market was already discounting, 2) whether investors are really longer than they ideally want to be.

Much of the news flow surrounds "old" stories that ought to be largely discounted by the market. The widening in Spain and Italy is harder to disregard. However, while we readily acknowledge that the tail risk to the system is higher than at any point this year, we struggle to make a Spanish/Italian funding crisis our base case this side of summer. If there is the will, we believe there is also the ability to absorb the necessary sovereign issuance domestically for the time being.

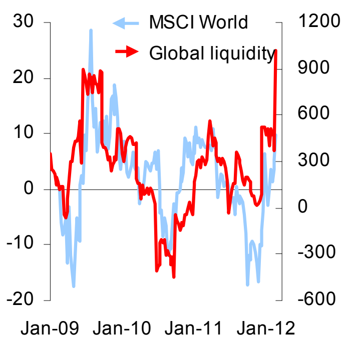
In any case, we prefer looking at market vulnerabilities over trying to second-guess the next trigger. If there is a large consensus long as there was in the middle of last year, then it is much more likely that negative headlines trigger risk reduction and wider spreads than if positions are balanced.

Figure 50. Citi US economic surprises index



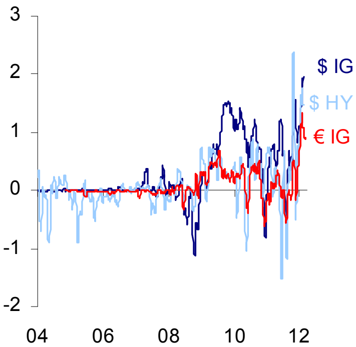
Source: CIRA. CESIUSD Index <go> on Bloomberg.

Figure 51. MSCI World (%) vs global liquidity ($bn), 3m changes



Source: CIRA, Haver Analytics

Figure 52. Mutual fund flows in credit, $bn



Source: CIRA, EPFR

Most of the positioning indicators appear far less stretched than in the run up to the selloff a year ago.

At the broadest level, the Q1 rally doesn't seem disproportionate to the amount of liquidity that has been injected in recent months. Figure 51 shows the three-month change in aggregate central bank holdings of securities (where we have included the LTROs) against the change in MSCI World equity index over the same period. If anything, the recent rally appears modest from that perspective.

In credit, both European and US mutual fund inflows have been exceptionally strong YTD. In Europe, they have been substantially higher than they were during the big rally in 2009 (see Figure 52). Even more spectacularly, inflows into HY mutual funds global of $30.7bn in Q1 alone were only just shy of the record $31.8bn for the whole of 2009!

Moreover, back in 2009 the outstanding in the credit market was expanding at the fastest pace ever. In contrast in 2012, the outstanding is actually shrinking in Europe as banks use LTRO liquidity to fund redemptions. YTD IG unsecured issuance in euros is a negative €33bn. For the full year we expect it will be -€165bn, equivalent to a 6.5% contraction in market size. Such a technical imbalance is not a hard ceiling on credit spreads widening. But without an immediate negative catalyst credit looks likely to be well supported.

With technicals and fundamentals pointing in opposite directions, a nervous, volatile trading range is our base case going into summer. But against the Spanish/Italian risks is not a high conviction call. And the upside in that modal scenario has to be weighed against the much bigger downside in our risk scenario.

Therefore, we reckon it makes sense to reduce the directional exposure in portfolios. We recommended scaling back longs and moving up in credit quality from early March. The recent deterioration in the market sentiment towards Spain and Italy is prompting us to cut exposure further to neutral. The question is how?

- We think the wrong thing to do here is to hedge with index or single-name CDS. CDS protection at these wider levels could prove a very poor hedge for cash positions still near the tights. Time and time again we have seen how the consensus response rapidly turns into the collective pain trade. CDS leads the initial movement wider or tighter, but then gradually cash spreads catch up.
- Of course, that means crossing the bid-offer and the lack of liquidity in cash. We'd argue the right place to do that is not by increasing shorts in the periphery, where many bonds have already widened substantially. Conversely, many 'true core' bonds remain tightly held, giving little reduction in beta-weighted exposure.
- We think the place to lighten up here is on corporates and financials in the weaker core countries, like France, Belgium and Austria. To date they have not really widened relative to German corporates. Yet as we saw last year they are likely to underperform during periods of severe market stress.
- Similarly, the widening in financials has been concentrated in sub debt. If the selloff continues, we think risk / reward will increasingly start to weigh on senior.
- To hedge systemic tail risks our preferred trades are still super senior protection, 3s5s curve flatteners in the CDS indices and recoupling trades between debt and equity markets.

We think there will be better times to take strong directional views later in the year – when spreads are at either extremity, when the data is trending in a more uniform direction, when the politics are clearer, when technicals and fundamentals are less diametrically opposed.

Global Equity Strategy

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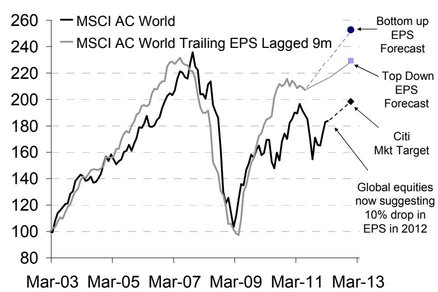
Global equities are up 9% year-to-date. Attractive valuations and healthy corporate performance mean that we are still bullish, only less so after such a strong start to the year. Some shorter-term consolidation may be appropriate heading into the summer with further European woes proving the obvious catalyst for investors to take off some risk. We would be buyers into weakness. For end-2012, we target 360 on the MSCI ACWI benchmark, implying 10% upside from current levels.

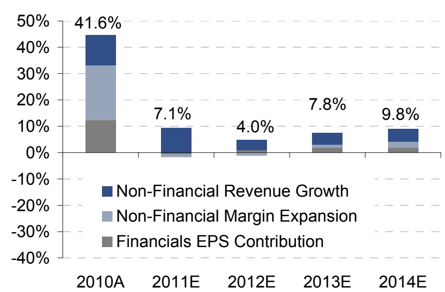
The close lead/lag relationship between global share prices and trailing EPS suggests that the market is still expecting EPS to be down around 10% in 2012 (see Figure 53). We have upgraded our global EPS forecasts (see Figure 54) and now expect 4% growth this year and 8% in 2013 (previously we were forecasting 0% and 10%). So we are still more cautious than the analyst consensus. While this suggests more analyst downgrades to come, we would highlight that our global Earnings Revision Index has recently turned positive. On a net basis, analysts have stopped downgrading. It certainly supports our view that macro-driven fears of a global EPS double-dip are overdone.

Figure 53. **MSCI AC World Price vs EPS (9m Lagged)**



Sources: MSCI, CIRA

Figure 54. **Top-down Global EPS Growth Forecasts**



Sources: CIRA, Factset

While we think there is more upside from here, investors shouldn't be anticipating the gains we had during the 2009 rally. Back then, there were both a re-rating of stock markets and a recovery in global EPS, both from depressed levels. Currently, valuations are low, but global profits are not depressed like they were in 2009. Our forecast is for a moderate rise in EPS over the next two years. This should mean that the current rally will look more like the one we had in 2010-11.

The Eurozone crisis still remains a concern, but the liquidity provided by the central bank seems to have removed the tail risks. Strong macro data in the US have also helped offset the uncertainties coming out of Eurozone. In addition, cheap valuations limit the downside risk when pullbacks occur. Even after the 20% increase, global equities are trading at 18x CAPE while the long-term average is 24x.

Our key regional and global sector recommendations are summarised in Figure 56. We started 2012 with an allocation towards those regions with a combination of strong earnings and GDP trends, cheap valuation, and easy monetary policy (real rates vs GDP). We still look for regions with these qualities, which is why we are becoming marginally more cautious on European equities. We downgrade the UK to Neutral from Overweight. While it stands out as one of the cheapest markets in the world, the UK is suffering weakening EPS and GDP trends in the short-term. In addition, while the UK had the easiest monetary conditions in 2011, this is no longer the case with slowing inflation/economic growth and easier policy elsewhere.

We remain Overweight Global Emerging Markets. Valuations remain attractive in EM and the region should benefit from easier monetary policy this year. We are also Overweight Japan. In the medium term, we believe earnings growth in Japan will remain robust, so supporting our Overweight. We are Neutral on Europe ex UK equities. While sovereign concerns will continue to weigh on growth, liquidity provisions by the central bank should help support equity markets. We are Underweight the US. While solid earnings should support US equities, we believe regions offering cheaper valuations will outperform. Joining the US amongst our Underweights is Australia, which we downgrade from Neutral. The Australian market underperformed in 1Q and we expect more as global equity indices rise, albeit at a slower pace. We found Australia has tended to underperform (in local currency) a rising global equity benchmark.

Figure 55. Strategists' Forecasts

Region	Index	Current Level (12 Apr 12)	End 2012 Target	Exp Gain (%)
US	S&P 500	1388	1425	3%
Pan Euro	DJ Stoxx600	257	285	11%
UK	FTSE 100	5710	6200	9%
Japan	Topix	810	960	19%
Asia xJpn	MSCI Asia x JP	514	585	14%
Australia	S&P/ASX 200	4281	4750	11%
GEMs	MSCI EM	1025	1225	20%
LATAM	MSCI Latam	4039	4900	21%
CEEMEA	MSCI EM EMEA	341	350	3%
Global	**MSCI ACWI**	**326**	**360**	**10%**

Source: MSCI, CIRA

In line with our view of slower gains in markets, we have tempered our global sector allocation by lowering its inherent beta. We have taken profits on our Overweight position on Financials and downgrade to Neutral. The sector outperformed at the start of the year, which has been the typical period of contrarian outperformance. However, Financials no longer look as strikingly cheap as they did a quarter ago. Also, deleveraging and weak demand in Europe are likely to keep a lid on performance. In place of Financials, we have upgraded Global Industrials. This keeps our cyclical bias, but lowers our exposure to financial leverage and beta. Industrial companies have successfully de-leveraged and aggregate cash balances are at record levels. In contrast to Financials, they benefit from solid earnings trends.

We have upgraded global Utilities to Overweight in place of Consumer Staples, which we downgrade to Neutral. The global Utilities sector has been a serial underperformer. But it now seems to be enjoying stabilising earnings momentum along with cheap valuations. Our analysts note that political risks remain in Europe, while the US sector, which is a much larger component of the global benchmark, looks to be an attractive contrarian allocation for investors. The sector has a dividend yield of 4.5%. The earnings outlook for Consumer Staples remains sound and is supported by considerable barriers to entry and growing EM exposure. But it stands out as being amongst the most expensive across the world. Still, amongst the consumer sectors we prefer Staples to Discretionary (which includes Autos, Media and Retailers). Consumer Discretionary remains our least favoured cyclical, in part because valuations are high and earnings revisions could be weakening.

Figure 56. Regional And Global Sector Recommendations

Overweight	Neutral	Underweight
Global Emerging Markets	Europe ex-UK	US
Asia Pac ex-Japan	UK ↓	Australia ↓
Japan		

Overweight	Neutral	Underweight
Industrials ↑	Consumer Staples ↓	Consumer Disc
IT	Energy	Health Care
Utilities ↑	Financials ↓	Telecoms ↓
	Materials	

Source: CIRA

Securitized Products Strategy

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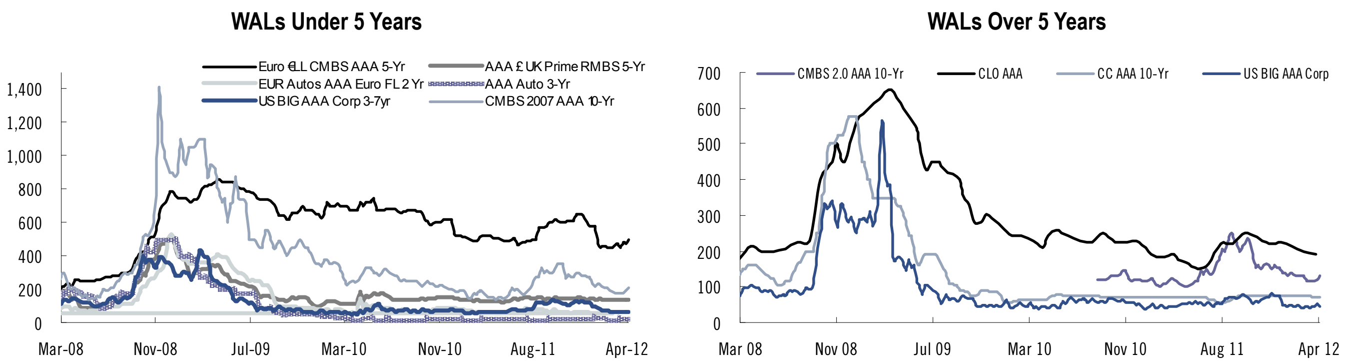
A credit barbell portfolio best addresses the current market's mixed signals in our view. Several of our securitized products strategists recommend this approach in their sectors. In consumer ABS, this strategy would blend a mix of short generic triple-As with selected off-the-run sectors to improve the average portfolio spread. In Europe, for the higher-yielding side of the barbell position we recommend first-pay short WAL UK nonconforming RMBS and select opportunities in European CMBS.

The barbell strategy appears appropriate for dealing with the possible end of the market's risk-on sentiment. There appears to be a growing market concern that a second-half selloff might repeat. Indeed, the risk-on trade may prove to be fleeting, as Q2 profit-taking moves in, and markets are also shifting to a more cautionary sentiment. Concerns about still elevated US unemployment, European sovereign debt and commodity price volatility are keeping triple-A spreads range-bound, yet still in demand.

Figure 57. Selected Securitized Products Sectors — Spread Performance, Mar 08-Apr 12



Source: Citi Investment Research and Analysis

Signs of Weakness in Secondary Markets, As Issuance Remains Resilient

Although investor demand remains healthy, there are signs of weakness across the sectors. In the non-agency market, for example, synthetics have sold off with the recent selloff in equities. Cash prices generally lag synthetics and could face some downward pressure.

Still, new issue markets are holding up well, despite recent softness in some secondary sectors. In CMBS, for example, fixed-rate conduit issuance has reached $4.1 billion so far this year across four multi-borrower deals. Three fixed-rate single-borrower deals, totaling $1.1 billion, have also priced. In consumer ABS, notable recent new issue off-the-run ABS includes a 7YR private label credit card at swaps + 140bp, a 2YR dealer floorplan transaction at LIBOR + 50bp, and another private label credit card deal offering guidance in the LIBOR + 43–45bp area for a 5YR floater.

Selected Securitized Products Recommendations

- **Italian and Portuguese RMBS best of Peripheries.** Italian and Portuguese RMBS offer the best relative value among the periphery EA countries, in our view. Italian RMBS balances strong fundamentals with potential upside in comparison to covered bonds and bank senior unsecured bonds. Portuguese RMBS offers stronger relative value than Portuguese covered bonds.

- **Auto subs top value in consumer ABS.** Auto subordinates (our top pick) tightened by 25–50bp during the last month and have room to go, in our view. Among on-the-run sectors, auto subs offer the most pickup relative to the 10YR adjusted mean spread. At current spreads of swaps + 100–175bp for single-A and triple-B auto ABS, the pickup is 90–117bp to the mean.

- **Better quality, fixed-rate non-agency paper.** We prefer better quality, fixed rate paper because of high carry, a strong investor base, and lower supply risks. The lower credit sectors are at greatest risk of further declines if there is more macro weakness.

- **Longer-term opportunity in CMBS.** We find 2005 AJs, 2007 AMs, 3.0 junior triple-As, and 2005 and 2006 dupers the most attractive at the moment. These sectors have widened the most relative to their recent tights. While the current concerns of the eurozone and Maiden Lane III may pressure spreads wider in the near term, opportunities across the CMBS sectors will present themselves for longer term investors.

Cautionary Sensibility Persists

Fed officials upgraded their assessment of current economic and financial conditions during March. Even so, incoming data remains mixed and policy makers are keeping further easing options open. The Federal Reserve Chairman Ben Bernanke recently stated that "the US is still far from having fully recovered".

The US unemployment rate dropped to 8.2% from 8.3%. While some sectors (like manufacturing) show solid gains, seasonal distortions affected the data. Our economists continue to project payroll gains to average 175,000 during 2012, compared to the comparable 2011 average gain just above 153,000 (projecting a 7.8% unemployment rate by Q4 2012)[9].

Sector Relative Value and Allocation Recommendations

Our securitized products strategists have mixed views on the market, ranging from bullish to neutral, and Figure 58 shows Citi strategists' recommendations for major structured products sectors on a scale of -3 (maximally bearish) to +3 (maximally bullish). The table also incorporates the strategists' most current thinking about value and presents one or two trade ideas.

Figure 58. Sector Relative Value and Asset Allocation Recommendations — Selected Sectors, April 2012

Sector	Strategist Recommendation	Spreads Relative to Long-Term Averages	Comments
CABS	0	Fair	Remain market weighted. Subordinate auto ABS is our top pick. We also like senior auto lease ABS.
CMBS	0	Fair	2005 AJs, 2007 AMs, 3.0 junior triple-As, and 2005 and 2006 dupers are the most attractive at the moment. These sectors have widened the most relative to their recent tights.
Agency MBS	+1	Fair	We recommend overweighting lower coupons (30yr 3.5s) vs swaps to get long the mortgage basis. Supply/demand technicals look favourable going forward. Strong march sell-off performance suggests MBS should be able to withstand some reduction in QE3 probability.
European Securitized Products	0	Cheap to Fair	Market weight. We prefer combining stable, short sectors with select off-the-run opportunities, for a credit barbell. We like autos, UK Credit Cards, UK prime RMBS, with higher yielding CMBS seniors and off-the-run opportunities in first pay short WAL UK NCRMBS.

Source: Citi Investment Research and Analysis

[9] "US: Economic Forecast Highlights - March 2012", Robert V. DiClemente et al, 22 Mar 2012

Commodity Outlook and Forecast

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After an uneven 2011, commodities have generally gained strength in the first quarter of 2012 thanks to relatively balanced fundamentals and underlying macroeconomic support. However, the sector has also seen increasing differentiation reflecting idiosyncratic demand and supply factors and unfolding tail risks. This uneven performance is expected to continue throughout the year.

Energy in particular held pole positions on either extreme of the performance spectrum, with gasoline outperforming +26% due to Atlantic refinery shutdowns while US natural gas underperformed -29% from a supply glut and weak demand from unusually mild weather (see Figure 60).

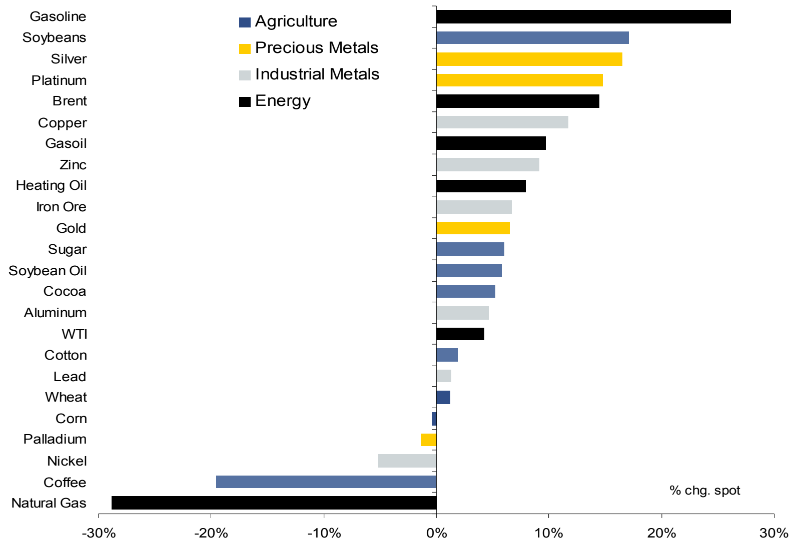
Figure 59. 2Q'12 Commodity Price Forecast

		Recent Spot	5Y Cyclical	Q1_2012	Q2_2012E	Q3_2012E	Q4_2012E	2012E	Q1_2013E	Q2_2013E	Q3_2013E	Q4_2013E	2013E
Energy													
NYMEX WTI	USD/bbl	102.8	81.0	103.0	105.0	115.0	105.0	106.0	N/A	N/A	N/A	N/A	113.0
ICE Brent	USD/bbl	121.8	85.0	118.4	125.0	130.0	125.0	125.0	N/A	N/A	N/A	N/A	120.0
Henry Hub Natural Gas	USD/MMBtu	2.0	N/A	2.5	2.4	2.6	2.3	2.5	3.1	3.5	3.8	3.7	3.6
Base Metals													
LME Aluminum	USD/MT	2,059	2,500	2,216	2,250	2,300	2,350	2,279	2,350	2,380	2,420	2,400	2,388
LME Copper	USD/MT	7,997	7,500	8,314	8,500	8,550	8,600	8,491	8,500	8,360	8,340	8,300	8,375
LME Lead	USD/MT	2,065	2,300	2,118	2,100	2,175	2,250	2,161	2,300	2,250	2,250	2,300	2,275
LME Nickel	USD/MT	18,292	22,000	19,721	18,500	19,000	20,500	19,430	22,550	22,475	23,000	23,250	22,819
LME Tin	USD/MT	22,187	24,500	22,986	22,500	23,000	23,500	22,997	25,000	26,000	26,500	25,000	25,625
LME Zinc	USD/MT	1,981	2,300	2,042	2,050	2,150	2,240	2,121	2,275	2,300	2,280	2,350	2,301
Precious Metals													
Gold	USD/T. oz	1,659	1,050	1,691	1,680	1,740	1,760	1720.0	1820	1890	1840	1790	1835
Silver	USD/T. oz	31.4	15	32.7	31.0	29.5	29.0	30.6	28.3	27.5	26.8	26.0	27.1
Platinum	USD/T. oz	1,583	1,500	1,604	1,675	1,725	1,725	1682.0	1725.0	1725.0	1725.0	1725.0	1725.0
Palladium	USD/T. oz	647	600	683	750	870	900	801.0	925.0	925.0	925.0	925.0	925.0
Bulk Commodities													
Hard Coking Coal (benchmark Asia)	USD/MT	285	220	235	215	235	245	233	235	235	230	225	231
Thermal Coal Asia (NEWC)	USD/MT	105	105	116	114	120	125	119	130	135	140	140	136
Iron Ore Spot (TSI)	USD/MT	149	100	142	160	150	145	149	140	140	135	135	138
Agriculture													
Corn	USd/bu	629	N/A	641	660	640	620	640	600	610	590	600	600
Wheat	USd/bu	624	N/A	643	650	630	630	638	640	660	700	700	675
Soybeans	USd/bu	1,437	N/A	1,272	1,425	1,400	1,380	1,369	1325	1305	1305	1275	1,303
Rice	USD/cwt	15.31	N/A	14.31	15.15	15.05	15.10	14.90	15.15	15.20	15.25	15.00	15.15
Cotton	USd/lb	92	N/A	93	90	90	90	91	N/A	N/A	N/A	N/A	90
Sugar	USd/lb	23.4	N/A	24.5	24.0	24.0	25.0	24.4	N/A	N/A	N/A	N/A	24.0
Coffee	USd/lb	179	N/A	205	185	185	180	189	N/A	N/A	N/A	N/A	200
Cocoa	USD/MT	2,248	N/A	2,308	2,275	2,315	2,300	2,300	N/A	N/A	N/A	N/A	2,400

Source: Citi Investment Research and Analysis

Going forward, commodities should reflect overall improving economic and risk conditions but also faces headwinds from weaknesses in Europe and continuing systemic risks. The outlook for China remains a critical determinant of commodity direction, particularly in the industrial metals given its predominant position in global commodity demand (see Figure 61). China has thus far managed a softer-than-expected slowdown than some had anticipated and its inventory management has also supported prices for copper, iron ore, and other commodities. A soft landing in Chinese growth (Citi has not changed its forecast for +8.4% real GDP growth in 2012) should provide strong but not necessarily robust tailwinds.

Figure 60. Individual Commodity Performance: 1Q 2012



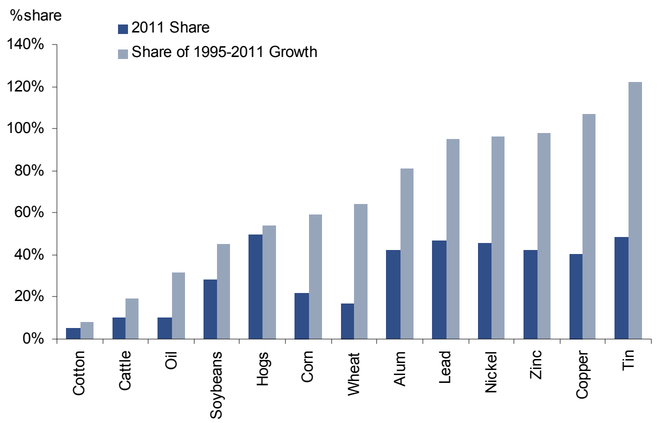
Source: Bloomberg, Citi Investment Research and Analysis

Tail risks abound for the foreseeable future, whether arising from a re-escalation of the eurozone sovereign debt crisis and new fears of financial contagion, politically-induced supply disruptions in oil, from weather-related factors in bulk commodity producers like Australia, or from moisture and heat conditions impacting the agriculture sector, where improved inventories may be just short of enough. Detailed outlooks and price forecasts for individual commodities are provided in the Q2 2012 Commodity Update[10].

Financial flows into commodities from passive indices and exchange-traded products (ETPs) were also generally supportive since the beginning of the year, following the general "risk-on" rally that also saw equities broadly perform strongly thanks to positive economic data and heavy liquidity injections by the world's central banks. Interestingly, financial investment in energy commodities was initially negative but reversed course in February and has now contributed a net $4bn of net long investment since January 2012. Together with positive length in the metals and agricultural commodities, we estimate some $15bn of new long-biased investment has entered commodities for Q1 2012.

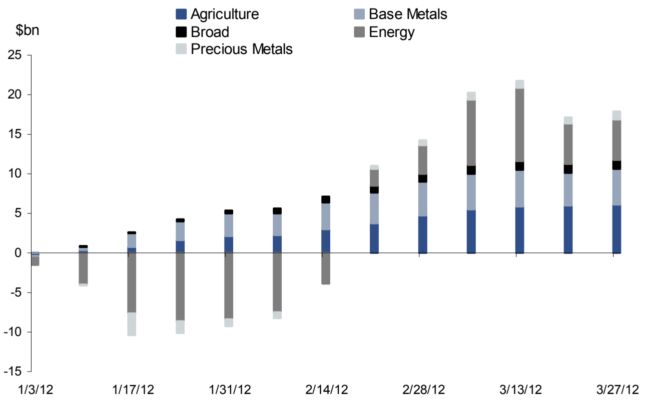
[10] Morse, Edward L. "Q2 2012 Commodity Update - Unfolding Tail Risks..." Citigroup: 16 April 2012.

Figure 61. Share of China in Global Commodity Demand and Growth



Source: Citi Investment Research and Analysis

Figure 62. Estimated Cumulative Financial Net Flows since Jan-12



Source: Citi Investment Research and Analysis

In crude oil, forecasts were revised upwards at the end of March. Current ICE Brent trading levels appear range-bound, but price risk remains slanted to the upside. Markets are torn between supply disruptions and geopolitical tensions exacerbating with Iran versus policy actions from Saudi Arabia to increase output and the possibility of strategic stockpile release in the US and Europe. Inventories are building, but remain low where visible (except for the US). China and Saudi Arabia have both been building crude stocks, but these are largely invisible to the market. As Saudi inventories move out of their storage and into OECD inventories their weight on the market should increase, but the seasonal rise in crude demand should ensure that they get absorbed fairly easily. Crude markets globally (excluding onshore US) appear strong, with robust backwardation and decent physical premiums. Given that the market is currently trading the trough of global crude demand and is still fairly firm, it is hard to get too bearish on crude although some of the aforementioned policy responses have softened the bullish tinge.

Industrial commodity prices are forecast to be range bound over the short and medium term. In the near term, traded levels are likely to be driven by supply shocks and cost inflation rather than a significant demand shock. In the medium term, we expect to see the transition to later cycle commodities, which should benefit the base metals and precious over bulk commodities. The conviction calls are in palladium and nickel on the bullish side and copper and silver on the bearish side.

On precious metals, gold should see underlying support from the low real interest rate environment and continued financial interest by central banks and private investors. While potentially one of the key beneficiaries if certain systemic tail risk scenarios come to pass, gold and precious metals more generally also face significant volatility if a flight-to-quality or flight-to-liquidity drives sudden liquidations of holdings. Our forecast sees gold averaging $1720/t oz for 2012 and $1835/t oz for 2013.

On the aggregate, we forecast range bound agriculture prices with a slightly bullish to neutral bias for the sector on a fundamental basis, expecting corn and oilseeds to set the tone. Cal'12 prices for key grains and soybeans were upgraded although a less constructive view is held for the thinly traded soft commodity complex. Official government data point to adverse La Niña weather patterns significantly impacting 11/12 South American production of maize and oilseeds, an ongoing concern that appears likely to tighten US export markets this summer and potentially into 2013. Chinese stockpiling and import demand should further strain balances and support prices. Vis-à-vis the forward curve, soybeans and coarse grains appear more favourable and bullish against a robustly supplied wheat market. On a prompt month basis, we still favour the old corn crop against wheat and view soybeans as having the potential to break out above $1500/bu.

Citi Foreign Exchange Forecasts

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† This author is not an independent research analyst and may have knowledge of the Firm's positions and/or the Firm's interest in one or more of the securities referenced herein.

Market Commentary

This market commentary has been prepared by a member of the Institutional Clients Group of Citi. The information in this communication is not intended to constitute "research" as that term is defined by applicable regulations.

** For specific trade ideas associated with this sector review, please contact the contributors listed at the end of this piece.

- USD strength overall is still our central forecast over the medium term
- A lower EUR is predicted on cyclical grounds and relatively easier ECB policy
- CAD is expected to be most resilient in the G10 dollar bloc, with AUD going to parity in the medium term
- In Europe, Sterling still looks cheap and should outperform the euro over 6-12 months. SEK and NOK should also find support vs. EUR
- Growth concerns around China likely means a flat-lining CNY, which in turn could constrain upside potential in many EM Asian currencies vs. the USD

These forecasts are a joint venture between Citi's foreign exchange, global macro and technical strategy groups and our developed and emerging markets economists. Under normal circumstances, we expect to present Forecasts on a monthly schedule although we may offer intra month updates if circumstances dictate.

While these forecasts should be considered the best guide to Citi's short to medium term views on the outlook for the exchange rates covered, individual analysts within various strategy teams may offer separate trade ideas in spot, forward, options or futures when this seems appropriate for technical, tactical or strategic reasons.

Figure 63. Citi Foreign Exchange Forecasts

		Market data			Forecasts			Returns**	
		spot	3m Fwd	12m Fwd	0-3 mos	6-12 mos	long-term	3 mos rtn	12 mos rtn
G10									
Euro	EURUSD	1.31	1.31	1.31	1.30	1.25	1.30	-0.6%	-4.8%
Japanese yen	USDJPY	81	81	80	81	80	85	0.2%	-0.5%
British Pound	GBPUSD	1.59	1.58	1.58	1.57	1.53	1.65	-1.2%	-2.9%
Swiss Franc	USDCHF	0.92	0.92	0.91	0.92	0.97	0.96	0.5%	6.0%
Australian Dollar	AUDUSD	1.04	1.03	1.00	1.03	1.00	0.90	0.4%	0.0%
New Zealand Dollar	NZDUSD	0.82	0.82	0.80	0.82	0.78	0.63	0.1%	-3.0%
Canadian Dollar	USDCAD	1.00	1.00	1.01	0.99	0.98	0.97	-1.0%	-3.2%
Dollar Index*	DXY	79.89	79.86	79.74	80.22	82.24	80.17	0.4%	3.1%
G10 Crosses									
Japanese yen	EURJPY	106	106	106	105	100	111	-0.5%	-5.3%
Swiss Franc	EURCHF	1.20	1.20	1.20	1.20	1.21	1.25	-0.1%	1.0%
British Pound	EURGBP	0.82	0.83	0.83	0.83	0.81	0.79	0.5%	-1.9%
Swedish Krona	EURSEK	8.87	8.91	9.02	8.85	8.75	8.65	-0.7%	-3.0%
Norwegian Krone	EURNOK	7.58	7.61	7.72	7.55	7.50	7.50	-0.8%	-2.8%
Norwegian Krone	NOKSEK	1.17	1.17	1.17	1.17	1.17	1.15	0.1%	-0.1%
Australian Dollar	AUDNZD	1.26	1.25	1.24	1.26	1.28	1.43	0.2%	3.0%
Australian Dollar	AUDJPY	84	83	80	83	80	77	0.5%	-0.6%
Asia									
Chinese Renminbi	USDCNY	6.30	6.31	6.33	6.31	6.22	6.11	-0.1%	-1.8%
Hong Kong Dollar	USDHKD	7.76	7.76	7.75	7.75	7.76	7.75	-0.1%	0.1%
Indonesian Rupiah	USDIDR	9177	9277	9598	9400	9350	9300	1.3%	-2.6%
Indian Rupee	USDINR	51.3	52.5	54.7	53.5	54.0	51.0	1.9%	-1.2%
Korean Won	USDKRW	1135	1142	1156	1150	1110	980	0.7%	-4.0%
Malaysian Ringgit	USDMYR	3.06	3.08	3.12	3.08	2.98	2.90	0.1%	-4.4%
Philippine Peso	USDPHP	42.7	43.0	43.4	43.0	42.0	41.5	0.1%	-3.1%
Singapore Dollar	USDSGD	1.25	1.25	1.24	1.25	1.21	1.17	0.2%	-2.8%
Thai Baht	USDTHB	30.8	31.0	31.4	31.0	30.2	30.0	0.2%	-3.7%
Taiwan Dollar	USDTWD	29.5	29.4	29.2	29.7	28.8	28.2	0.9%	-1.2%
EMEA									
Czech Koruna	EURCZK	24.8	24.8	24.9	24.5	25.2	24.0	-1.2%	1.2%
Hungarian Forint	EURHUF	298	302	313	298	285	290	-1.2%	-8.8%
Polish Zloty	EURPLN	4.18	4.23	4.36	4.15	4.12	3.90	-1.9%	-5.5%
Israeli Shekel	USDILS	3.75	3.77	3.80	3.80	3.95	3.90	0.8%	3.8%
Russian Ruble	USDRUB	29.6	30.0	31.2	29.8	32.1	32.2	-0.8%	3.1%
Russian Ruble Basket		33.7	34.2	35.6	33.8	35.8	36.5	-1.1%	0.6%
Turkish Lira	USDTRY	1.80	1.84	1.94	1.75	1.85	1.82	-4.6%	-4.6%
South African Rand	USDZAR	7.95	8.06	8.40	8.10	8.40	9.00	0.5%	0.1%
LATAM									
Brazilian Real	USDBRL	1.84	1.87	1.95	1.84	1.77	1.70	-1.6%	-9.5%
Chilean Peso	USDCLP	485	491	506	495	500	490	0.7%	-1.2%
Mexican Peso	USDMXN	13.2	13.3	13.6	13.2	12.5	12.2	-0.6%	-8.0%
Colombian Peso	USDCOP	1779	1800	1848	1830	1800	1850	1.7%	-2.6%

* The DXY forecasts are implied from the forecasts of the constituent crosses.
** Returns are relative to forwards

Source: Citi Investment Research and Analysis

Overview

USD performance has been rather mixed since our last forecast round in mid-March. The dollar is generally stronger against many EM currencies (Figure 64), which is not surprising given the increasing fears around growth in China. But the USD has been slightly weaker in most G10 crosses, which is unusual given the rise in global risk aversion in recent weeks.

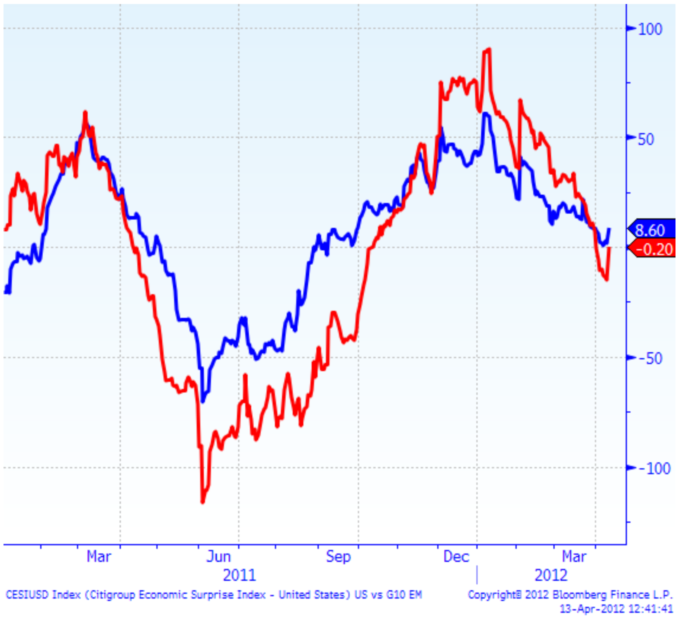
The fact that the US dollar has not performed better might be attributed to a softer patch of US economic data, particularly relative to consensus expectations. The latter is evident in Citi's Economic Surprise Index, where the US ESI has been trending down towards zero in recent months. Differences between the US and G10/ EM regional ESIs have also been declining and are currently close to zero (Figure 65).

Furthermore, US Treasuries rallied in response to some of the disappointing macro data. To the extent that higher US yields had become a cyclical support for the USD previously, the recent decline in US rates may have been a negative for the currency too.

Figure 64. USD vs. G10 (Blue), Asia (Black), Latam (Red), CEEMEA (Green) (Equally-Weighted Baskets, Lower Means Stronger USD, 3 Jan 2012 = 100)

Sources: Citi and Bloomberg

Figure 65. Differences in ESIs Between US and G10 (Blue) and EM (Red)



Sources: Citi and Bloomberg

Yet, while risk assets have run into some turbulence in recent weeks, with global equities falling back to early February levels, we expect risk appetite will recover and upwards pressure on US term rates will resume. Our central scenario is still one of a modest recovery, and our leading indicators suggest that consensus growth expectations could still be revised up slightly.

In particular, US growth should continue to hold up well even if downside growth risks in the Euro Area periphery remain significant and uncertainties persist about

the degree of the slowdown in China. As a result, the USD should perform well throughout the remainder of 2012, especially against European currencies including those in the CEEMEA region.

Elsewhere, CNY remains pivotal for both Asian and China-sensitive Latam FX within EMs and AUD within the G10. USD/CNY has basically flat-lined since the end of December and 12-month NDFs are once again pricing in depreciation of the Renminbi. We are some way off the late 2008-early 2009 period when global trade was collapsing and NDFs priced in sharp depreciation of the Chinese currency. But recent weaker global trade volumes combined with domestic Chinese growth pressures do suggest that USD/CNY is more likely to move sideways rather than trend further downwards in the near term. If so, this should constrain the upside potential in related currencies versus the USD.

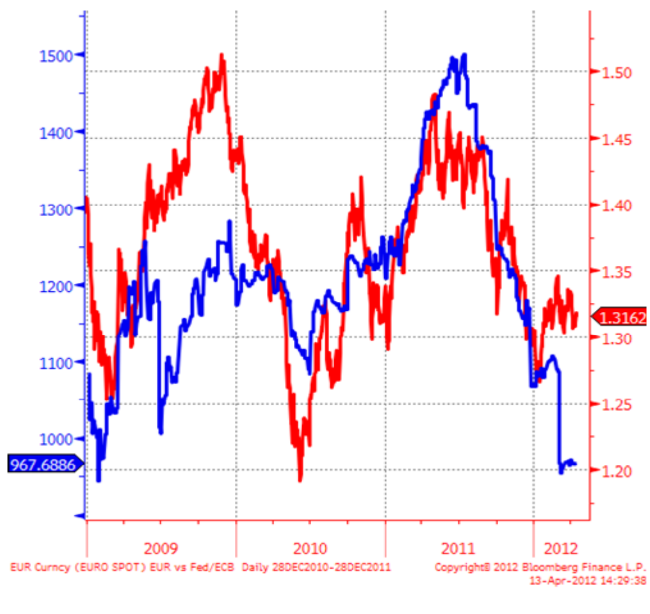
G10 Exchange Rates

EUR/USD – Downward Pressures Remain

EUR/USD has traded in a 1.30-1.35 range since late January. On balance, however, we think the cross is still facing downwards pressure and will likely break through the lower end of this range this year. Our 0-3 and 6-12 months forecasts are unchanged from last month, at 1.30 and 1.25, respectively.

Recently we have highlighted how two key drivers have had opposite pulls on the cross. On one side, a move towards relatively easier monetary policy by the ECB compared to the Fed has exerted downwards pressure. By contrast, the general improvement in risk appetite helped to ease risk premiums around the EMU periphery and support a higher EUR. As a result, our forecasts saw little movement in EUR/USD in the near term.

Figure 66. EUR/USD (Red) vs. Ratio of Fed and ECB Balance Sheets (Blue)



Source: Bloomberg

Figure 67. EUR/USD (Red) vs. Spain 5y CDS Spread (Black, inverted)

Source: Bloomberg

Despite the recent rally in US rates markets, cross-market rate differentials still point to a lower EUR/USD. Further ECB accommodation is likely later this year via rate cuts and possibly more LTROs, which should depress the EU-US rate spread and lead to a weaker euro. In our baseline case, we do not forecast Fed easing, though a move towards QE3 would clearly be a risk to this view (Figure 66).
With the situation in the troubled EMU periphery flaring up, the risk premium in EUR has arguably started to rise once again. For instance, the single currency has been correlated with Spain CDS spreads (Figure 67). The recent deterioration in Spanish credit quality and widening in spreads also suggests that EUR/USD should be lower. Ultimately, a weaker EUR over the medium term may help to mitigate the adverse growth effects of fiscal tightening in the periphery countries even if it does not address intra-Euro Area imbalances.

Finally, from a technical standpoint, EUR/USD continues to trade in a multi-month downwards sloping channel. If it can break recent support at around the 1.30 level, 1.25 or lower looks like a plausible target.

USD/JPY – Stable For Now

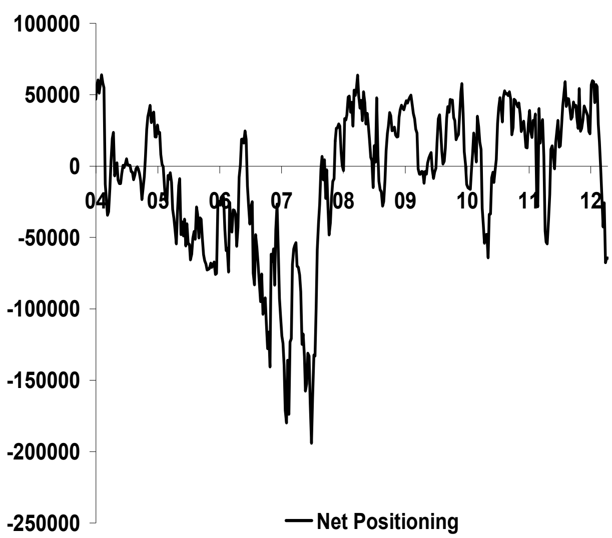
USD/JPY has retraced nearly 40% of its sharp move higher between February and mid-March, correcting what was an overshoot in our opinion. Our forecasts are for the yen to basically flat-line over the next 12 months.

One important factor is that we doubt that the BoJ will provide enough stimulus for a weaker yen, while support for the cross is unlikely to come from bear flattening in the US curve (Figure 69). The BoJ left rates unchanged at its April meeting, and we don't expect any additional easing at the next meeting in a fortnight's time. However, if the recent slide in USD/JPY continues, then the BoJ may ease again.

Policy sensitivity about the yen would be understandable: although the share of exports in GDP is relatively low, at 18% including goods and services, exports have done much of the heavy-lifting for growth in the last couple of cycles. Should exports growth stay weak – they have fallen in year-on year terms in ten of the last twelve months – then continued deterioration in trade flows (with imports still rising from reconstruction demand and nuclear energy replacements) could act to push the yen weaker, although Japan still has a cushioning income account surplus.

Flows also support a broadly steady yen. Citi's PAIN index suggests that short term money have sold JPY against USD or other currencies. Also, in the last few weeks USD/JPY has headed down even though JPY shorts have continued to accumulate (Figure 68). In other words, maintaining shorts must be getting tougher. Local Japanese investors, meanwhile, have been basically quiet, and although retail investors are regaining the risk appetite, we have yet to see meaningful outflows. Overall our point forecasts are: 0-3 months at 81 and 6-12 months at 80.

Figure 68. Net CFTC F&O Positioning in JPY as of April 3rd



Sources: Bloomberg, CFTC and Citi

Figure 69. USD/JPY: Regressed on US-Japan Rate Differentials

Sources: Reuters EcoWin and Citi

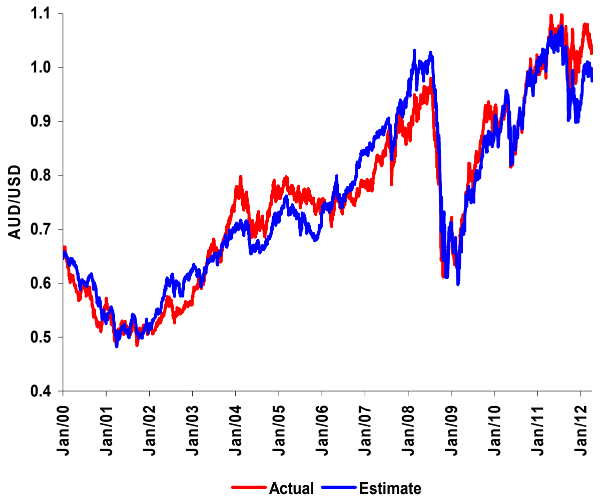
Dollar Bloc – CAD Outperformance, AUD Still Vulnerable

Having failed to regain previous highs when peaking near 1.09 earlier this year, AUD/USD has trended lower in a tight downwards sloping channel ever since. We expect the pace of depreciation will slow, though we are still looking for a move back to parity in the 6-12 month horizon.

For some considerable time, the Australian dollar has looked overvalued against traditional metrics. Citi's WERM model estimate of long run fair value is 0.87, while some other PPP estimates are even lower. Of course, such valuation estimates can be trumped by risk appetite and other market drivers in the short to medium term. But, as we have previously shown, focusing on market drivers such as risk appetite, carry, terms of trade/commodity prices and the performance of other Asian currencies, we still find that AUD/USD is expensive, with our market-based model putting fair value below parity too (Figure 70).

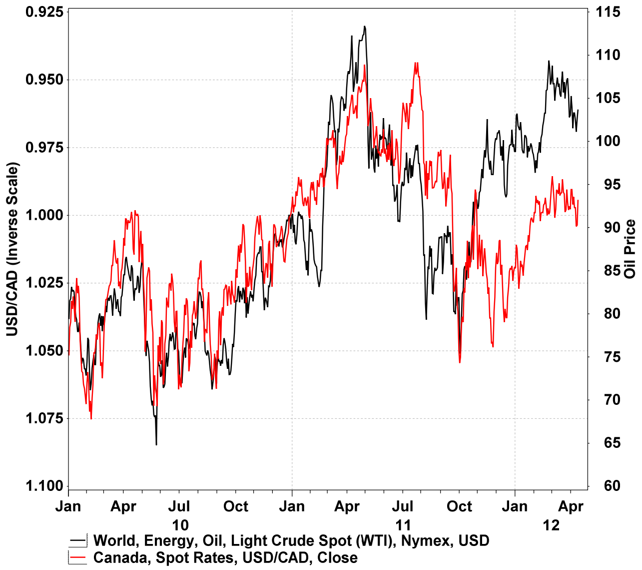
Meanwhile, concerns around China's slowing economy have continued to come to the forefront in recent weeks – for example, the latest GDP print disappointed expectations and Citi's China ESI continues to be in negative territory after falling sharply in mid-March (see Figure 76). Key commodity prices produced in Australia have also remained depressed, and AUD is yet to respond fully to this. The risk of further RBA cuts, reducing the carry appeal of AUD/USD, could also undermine the cross.

Figure 70. AUD/USD vs. Estimate Modelled on Market Drivers



Sources Bloomberg and Citi

Figure 71. USD/CAD (inverted) vs. Oil Prices



Source: Reuters EcoWin

The NZD has held up better recently, trading in a 0.80-0.84 sideways range since the beginning of February. Our short term forecasts see this trading range prevailing. Nonetheless, NZD is also significantly rich to long term metrics. Our WERM model for example estimates fair value at 0.62, compared to spot above 0.82 currently. NZD/USD has also diverged from rate differentials. In directional terms, our medium and longer term forecasts thus see a similar outlook as for AUD, expecting a move below 0.80 in 6-12 months.

Turning to CAD, the story is somewhat different to its two $ bloc peers. First, CAD is more linked to the (outperforming) US and less to (slowing) China/other Asian economies. Recent Canadian data has been better, with for e.g. the March employment print beating expectations strongly, and the loan officer survey continuing to improve. Second, the commodity link is more to oil prices, which are expected to remain at elevated levels (Figure 71). Finally, from a valuation aspect, USD/CAD is hovering close to long term WERM fair value at 0.97. The tight trading range around parity held since the beginning of February is not too surprising as a result.

Carry is less of a positive for the Canadian dollar, but with market rate expectations roughly flat (a view Citi's economists agree with) rate differentials seem to be less of a driver for USD/CAD at the current juncture, especially since current rate differentials are roughly consistent with spot based on historical relationships. Overall, our forecasts see only very mild CAD appreciation in the short and medium term, expecting the recent trading range to broadly hold.

European Crosses

GBP – Stable vs. USD & EUR Basket

As we have highlighted in several previous *Forecasts*, Sterling continues to be extraordinarily stable versus a 50:50 basket of EUR and USD, albeit recently moving towards the top end of the range held since 2010 (Figure 72). We continue to see this range broadly holding over the short and medium term.

In the meantime, the two conflicting forces that the GBP has faced remain in place. On the one hand, Sterling is the cheapest G10 currency, with the latest WERM estimate putting fair value on Cable at 1.72 and EUR/GBP at 0.79. On the other, GBP is struggling with poor economic prospects and the associated monetary policy ease/ fiscal tightening.

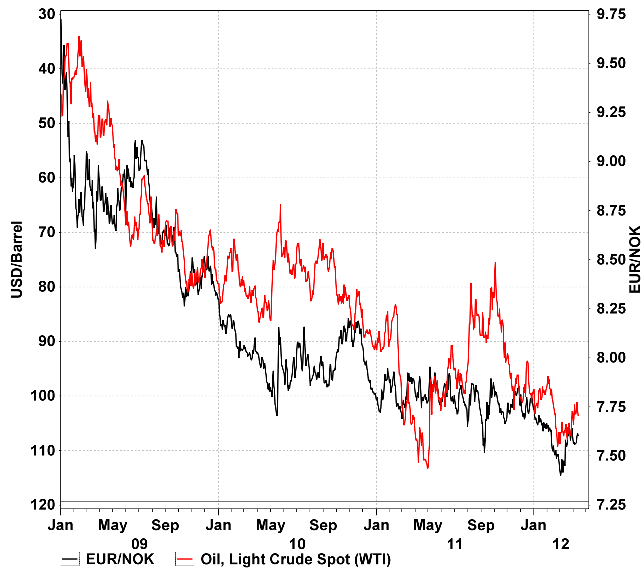
Indeed, Citi economists expect UK GDP growth to slow to 0.2% in 2012, and for the MPC to increase the UK QE program further. This could act as a drag on the exchange rate, especially when combined with ongoing restrictive fiscal policy and fears over the fragility of the UK recovery.

We have kept our medium term forecast unchanged, and continue to expect EUR/GBP to more or less track developments in EUR/USD. Thus with EUR/USD forecasted at 1.25, EUR/GBP will trade around 0.81 and GBP/USD around 1.53 in 6-12 months. This leaves the 50:50 basket roughly stable.

Figure 72. GBP vs. Average of USD and EUR (Higher = Stronger GBP)

Source: Reuters EcoWin

Figure 73. EUR/NOK and Oil Prices



Source: Reuters EcoWin

Scandis – Range Trading Given Proximity To Long Term Fair Value

EUR/SEK has continued to trade in its 8.75-8.95 range established earlier this year. Rather unusually, this has occurred during risk-on for most of this period – equities moving higher and VIX grinding lower have historically coincided with SEK rallies. Increasing focus on fragile local fundamentals is probably playing a role here. Recent data has been weaker, with especially the latest industrial production print missing expectations sharply. Indeed, Citi economists expect Swedish GDP growth to slow to 0.7% in 2012 from 4.0% a year earlier, with weaker exports to the depressed EA countries a major drag. The Riksbank will thus likely continue to ease policy, especially since inflation is forecast to stay well below the 2% central bank target. Citi expects 50bp of cuts to the repo rate in the remainder of this year, and with only around half of that priced into rate markets, this reduction in carry could weigh on SEK.

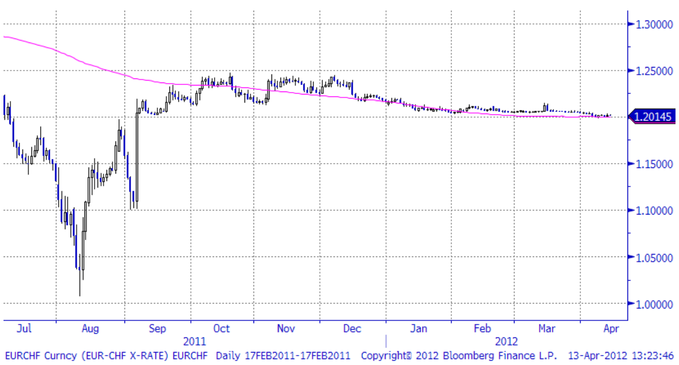
But increasing focus on Sweden's fragile fundamental of course needs to be weighed against the situation in the Euro Area. Thus, overall, we expect the recent EUR/SEK trading range to hold for some time, forecasting 8.85 in the short term and 8.75 in 6-12 months. Also note that SEK remains close to its long term fair value (WERM) at 8.61.

Turning to Norway, after rallying quite sharply following the 25bp rate cut in mid-March, EUR/NOK has, for now, found a new trading range at higher levels. As we highlighted in our last *Forecasts*, given this rate cut was unexpected and given the ECB is unlikely to move rates in the near term, the move higher in EUR/NOK will likely persist over the short term. Having previously raised our 0-3m forecast to 7.55 to reflect this, we are leaving our forecasts unchanged this month. Over the medium term, ECB rate cuts will likely weaken the EUR again, pulling EUR/NOK back towards fair value just below 7.50 on our WERM estimate. Sustained higher oil prices are also likely to support NOK medium term (Figure 73).

CHF – 1.20 Peg Still Holds

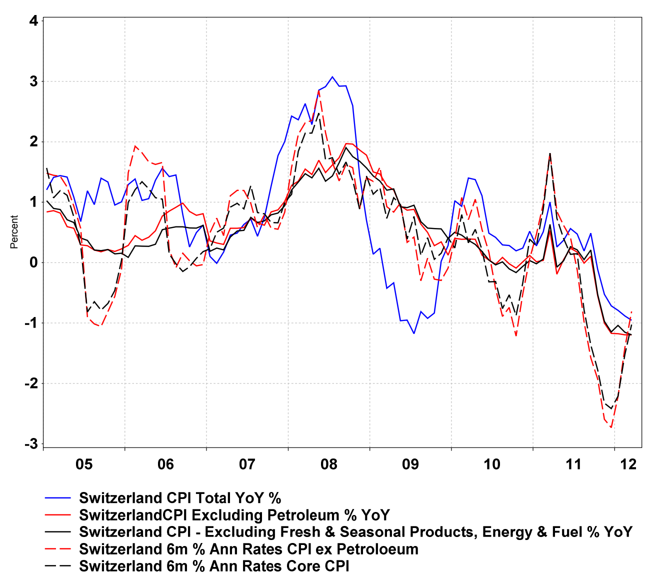
Since our last *Forecasts* in mid-March, EUR/CHF has continued to edge towards the 1.20 peg. Realised volatility has continued to be extraordinarily low (Figure 74), something we expect to continue while the 1.20 peg holds. Our forecasts show EUR/CHF hovering in a tight 1.20-1.21 range in the short to medium term.

Figure 74. EUR/CHF Approaching Peg With Little Realised Volatility



Source: Bloomberg

Figure 75. Swiss Inflation Negative



Source: Reuters EcoWin

Whilst recent data have surprised on the upside – the Swiss ESI is now positive and increasing – deflation risks continue to be evident with the March CPI print coming in at -1% YoY (Figure 75). Furthermore, with the Swiss Franc still highly overvalued according to many of our metrics (e.g. our EUR/CHF WERM estimate puts long term fair value at 1.34), we expect the SNB to continue to defend the existing 1.20 floor. We see the brief dips below the 1.20 peg recently as anomalies.

EM Exchange Rates

EM FX has underperformed vs. the US dollar in recent weeks, in line with the performance of EM risk assets. The sharp reversal in the fortunes of EM FX – which

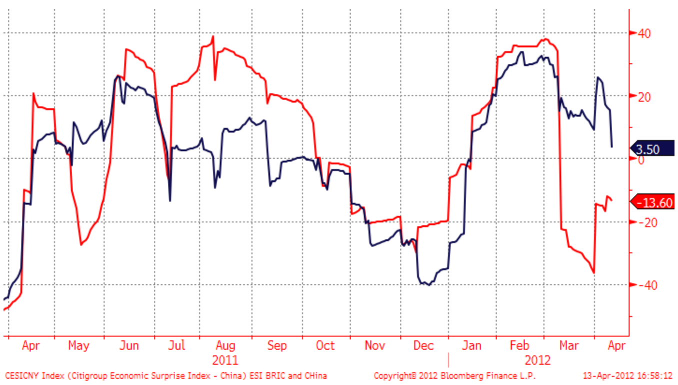
were the top global performers against the US dollar until the end of February – is driven by two chief factors.

The first is a rise in global risk aversion that has tended to impact EMs more. The second and related factor is mounting concern surrounding continued Chinese expansion (Figure 76), causing CNY to flat-line since the end of December and driving corresponding devaluations in commodity and China-sensitive Latam.

Since the end of February when broad USD strength vs. EM became more apparent, CEEMEA has weakened the most and Asia the least. The relative strength of Asian FX is surprising in the context of a flat-lining CNY, however, and indeed the general preference of central banks in the region for weaker exchange rates.

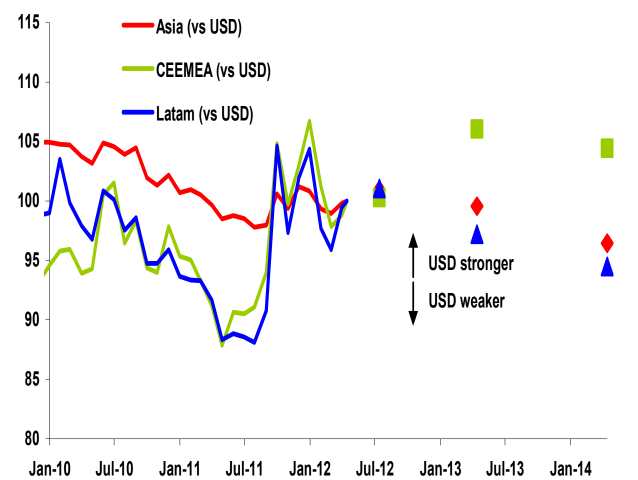
Our forecasts this month reflect a shift in this pecking order in the near term: CEEMEA does relatively better, while Asia and Latam weaken (Figure 77). Drilling down to individual crosses, USD/INR is expected to return the most in the next three months, and USD/TRY the least (i.e., approximately -4%).

Figure 76. China (Red) vs. BRICs ESI (Blue)



Source: Citi and Bloomberg

Figure 77. GDP Weighted FX Forecast Paths



Source: Citi and Bloomberg

EM Asia – China Leads, Others Follow

The heavily managed USD/CNY has essentially flat-lined since the end of December, in both spot and fixings and 12 month NDFs have once again broken through the daily fixing to the upside. We forecast this flat-lining in spot to be sustained in the near-term. Although not without exception (see below), Chinese data has been generally weak, and the PBoC has limited "trend appreciation" with similar growth concerns in the past (Figure 78). As discussed in our March *Forecasts*, CNY is pivotal for EM and especially Asian FX, and we have adjusted most of our near term forecasts to show continued underperformance of regional crosses.

Figure 78 shows an equally weighted basket of Asian exchange rates against the CNY, which strengthened until the end of February, by around 3.4%. This basket has since come off by about 1.4%. Appreciation of Asian FX through January and February was less than observed in 2009/10, for instance, with USD/CNY similarly on hold. But the focus then was on US weakness and global trade volumes were

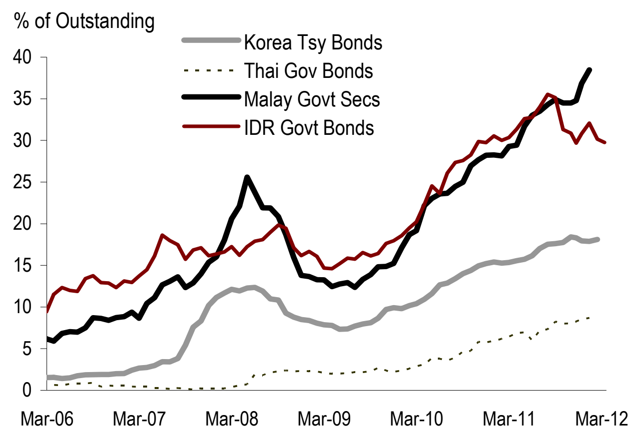
recovering strongly – the opposite of the current scenario. While we are not forecasting a repeat of H2 2008, when collapsing global trade led to sharp depreciations in Asian FX vs. CNY, the similarity in the source of the problem (i.e., weak external demand) suggests that the Asia basket could fall back to end-2011 levels.

The latest round of Chinese data has been more muddled than in recent months when data was ubiquitously weak. For instance, industrial production, loans data, exports growth and the official PMI were stronger than expected in March – but GDP growth softened, money supply growth was lower than expectations, imports were weak and the HSBC PMI was considerably lower. Equally, the trend of both data and inflation is generally downwards. Our near-term forecasts show USD/CNY hovering around the 50 day average of 6.31. Political pressures around the upcoming US elections could see some nominal appreciation later this year.

Figure 78. USD/CNY (Black) and Equally Weighted Asia vs. CNY (Red)

Source: Citi and Bloomberg

Figure 79. Foreign Ownership of Bond Markets



Source: Citi and Bloomberg

TWD stands out in EM Asia for its outperformance since late February – both vs. its main export competitors (KRW and JPY) and its chief export market (CNY). This is because the CBC has been actively keeping USD/TWD in a tight trading range, partly to ameliorate inflation pressures from domestic fuel price hikes. Going forward, however, we doubt that there is much room for TWD to strengthen against its peers, given hefty export dependence. Taiwan is the most vulnerable Asian EM to changing external demand, based on the share of exports in GDP and the expected net export contribution to growth. Reflecting this, our forecasts have USD/TWD at 29.7 in the near term, slightly above 3m forwards.

Since mid-January, USD/KRW has moved in a relatively tight trading band, of less than 3%. Although we expect the won to remain under pressure, including from escalating tensions with North Korea, it is likely to struggle to break 1150, which is also our 0-3 month point forecast. Downside, meanwhile, is limited by likely intervention from the BoK when USD/KRW approaches 1110-1140. To be sure, although the BoK is sounding hawkish (despite sharply lower inflation in March), it has shown a clear “preference” for a relatively weak USD/KRW. Recent data, including the FKI business survey which provides a good lead on GDP, has been weak. So, although KRW is structurally supported by its “twin surpluses” on the current and fiscal accounts – cyclical concerns, including ultra-sensitivity to China, dominate. We have raised our forecasts for USD/KRW this month in both the near and medium term.

The Malaysian ringgit has retraced almost half its mid-December to end-February rally, and is the second worst performing Asian currency (after only INR) since March 1st. We expect it to hover around 3.08 over the next three months. Acting against an MYR rebound are: one of the most export dependant economies around, with exports nearly 100% of GDP; a rich real effective exchange rate, which is unusual in EM Asia; and sharp increases in foreign bond holdings, which could quickly reverse if China/EM concerns continue to mount (Figure 79).

Both PHP and THB are also expected to stay soft in the near term. The hawkish tone of policymakers in each was triggered chiefly by higher oil prices in our view, which have since drifted lower. Our view is that BSP and BoT will be willing to accommodate peso and baht weakness, respectively. With limited monetary policy wiggle room given low prevailing interest rates, and obvious downside risks to growth in each, keeping exchange rates competitive remains a near term policy priority. Our forecasts show USD/PHP at 43 in 0-3 months, in line with forward rates. USD/THB is expected at 31.0 over the same period.

The latest MAS decision to steepen the slope of the band and restore a narrower width caught markets by surprise. USD/SGD gapped lower by around 50bps following the decision, bringing the NEER to about 90bps above the midpoint. With a 2% width, the topside of the band would be 1.235 presently, 1.22 in 6 months and 1.21 by year end. We forecast USD/SGD around current spot in the next three months, at 1.25, and 1.21 in 6-12 months.

IDR and INR are expected to fare worst in coming months, both relative to spot and respective forwards. IDR is no longer expected to be the strongest Asian currency 0-3 months ahead. It hasn't traded well all year and with the backing down on fuel subsidies, mounting tension in dollar funding markets, heavy foreign bond ownership (1/3rd of the total – see Figure 79), sticky inflation and increased political jostling, things look more wobbly than we anticipated. We see USD/IDR at 9400 in 0-3 months, with only moderate recovery thereafter.

INR, meanwhile, stays the most beleaguered currency in Asia, and has been the worst performer over the last 1, 3 and 12 months. We expect this to be broadly sustained, with USD/INR forecast at 53.5 0-3 months ahead and 54 in 6-12 months. With its high fiscal deficit, rising current account deficit and poor public debt ratios, it is one of the few Asian economies that shares similar features with the more heavily indebted Western European countries. Continued falls in both real activity data (note the latest set of ultra weak industrial production numbers) and money growth add to our concerns. The saving grace is that, unlike many others in its region, a mostly closed capital account and high captive domestic savings means that both bond markets and banks are to some extent protected.

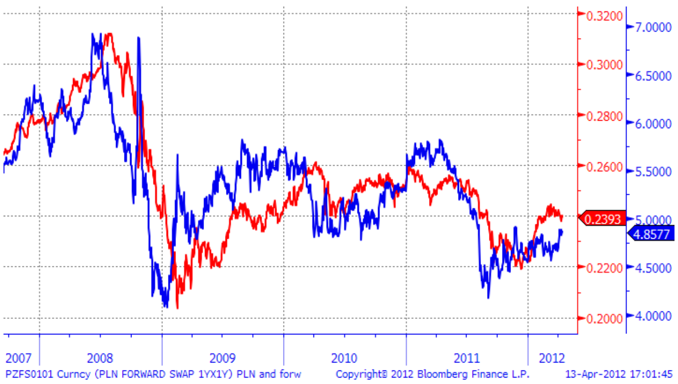
CEEMEA – Poles Apart

Having held up better than its Asian and Latam counterparts earlier in the year, the worst EM spot returns since the generalised US rally began six weeks ago have been clustered in CEEMEA. While we doubt that this lasts for some (TRY, RUB and PLN) others, notably ZAR, are forecast to stay under pressure.

We have long argued USD/ZAR needs to move above 8.0, and the recent risk-off move has helped that along and seems likely to push it higher in the coming weeks. USD/ZAR has been trading in a relatively tight upward sloping channel since early March, and our projections have USD/ZAR at 8.10 in the next three months and 8.40 in the 6-12 month timeframe. Factors underpinning our bearishness include: commodity terms of trade that remain under pressure; continued relative richness of ZAR on a real effective basis; a weak macro backdrop; and political concerns.

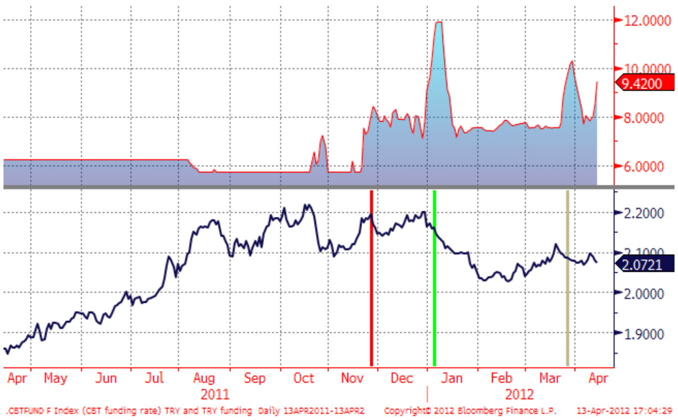
HUF, meanwhile, stays weak short-term for all the reasons outlined in recent *Forecasts,* including large policy credibility gaps, a deeply imbalanced (and export-led) economy and our expectation that progress on the badly needed IMF loan is likely to be slow at best. The ECB and the EC are unlikely to fully accept the proposed changes on infringement issues, so further talks may be needed to reach a compromise, extending the process. Positioning could allow for further legs down in EUR/HUF: investors bought quite heavily into EUR/HUF in recent sell offs, so if significant positive news did come up in Hungary, some may be forced out of their longs. On balance, we expect EUR/HUF to trade above 285 for the forecast horizon, and around 300 in the near term.

Figure 80. EUR/PLN (Red) and 1y1y Forwards (Blue)



Source: Bloomberg

Figure 81. CBRT Effective Funding Rate (Top) and TRYBASK (Bottom)



Source: Citi and Bloomberg

PLN, by contrast, looks better and is expected to appreciate relative to current spot. PLN continues to be pulled in different directions by two powerful forces. On the one hand, official intervention and more hawkish rhetoric from the central bank should lead to PLN strength (Figure 80). But on the other hand, relatively deep exposure to what transpires in Europe is a clear risk. The latter feeds through to PLN through a number of channels: the banks, which are largely owned by Western Europe and where 60% of housing loans are in forex; foreign ownership in the Polish government bond market, which continues to fluctuate near record highs; and trade, of course.

For now, we see better real activity data and sentiment dominating – and remember that in Great Recession, Poland was one of the few economies to escape recession altogether. Our forecasts show PLN strengthening steadily through the forecast horizon, and to 4.15 in the next three months.

CZK should find support from a different combination of similar factors. Although it is the most export sensitive in CEEMEA, low foreign penetration in the local bond market, virtually no foreign exchange loans and a recently more hawkish central bank should prop up the currency. We expect the koruna to remain in the range of 24.5-25.2 against the euro over a twelve month forecast horizon.

Tight liquidity, active foreign borrowings and current oil prices should keep the rouble strong for the rest of the second quarter, and our forecasts have the RUB basket at 33.8 and 35.8 for the coming 0-3 and 6-12 months respectively. We are cognisant, however, that the risks of capital outflow remain high – and that notwithstanding recent sell-offs, the basket is trading remarkably close to its post 2008 lows (i.e., RUB stronger), leaving it as one of the top performers in EM in the year to date. Should capital outflows continue to offset the beneficial effects of a

cushioning current account surplus, the rouble would likely come under fresh pressure.

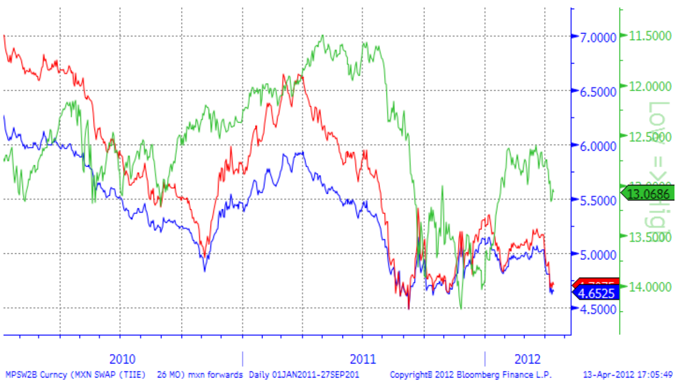
It is TRY, however, that is expected to be the real outperformer in its cohort. TRY continues to trade as a lower beta currency in the region, as idiosyncratic central bank policy continues to push TRY to stronger levels within the current informal “band” of 1.70-1.80. The CBT has tightened its policy stance and pushed its effective funding rate from around 7.5% to as high as 10.3%, so carry remains compelling (Figure 81). And, with better than expected data – on the current account, GDP growth, industrial production and even inflation – and fears of an oil price surge fading, TRY is forecast to be the best performing EM currency in the next three months. Over the medium term, however, the authorities' apparent reluctance to address Turkey’s twin macroeconomic challenges – a wide current account gap and elevated inflation – muddies the outlook, and USD/TRY should push past 1.80 to 1.85.

Latam – Weakening Bias

In Latam, we have a bias for weaker currencies in the near term, relative to current spot. Unlike e.g., CEEMEA, where more idiosyncratic factors are in play, Latam FX is highly China and commodity-sensitive. On balance, central banks in the region have a preference for weaker exchange rates and are also sounding more dovish. Indeed the shift in Latam central banks’ tones since our last FX round has been notable. The Mexican central bank sounds much more dovish, as does the central bank of Colombia, and Chile should soon follow suit. We expect the BCdoB, meanwhile, to cut the SELIC rate to an historical low at its meeting next week.

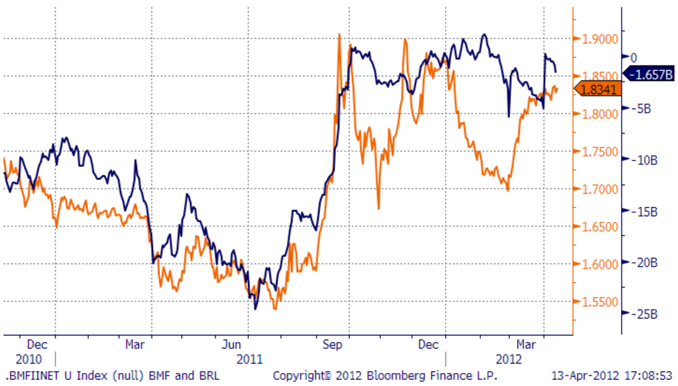
Our USD/MXN forecasts have been subject to the greatest revision since our last *Forecasts*, and we now see USD/MXN at 13.2 in the next three months, and 12.5 six- twelve months’ ahead. Indeed, USD/MXN could trade even higher in the very near term, particularly if US data disappoints further before the next FOMC meet. Underpinning our bearishness is a combination of factors, including: developments in Spain (not least from dominant Spanish banks in the region); headwinds from unfavourable positioning (MXN is a consensus long); and a central bank that has suddenly turned more dovish (see Figure 82, we now expect a 50bp cut this month). At the current juncture, these factors outweigh the structural positives, including strong local data, limited China vulnerability, firm oil prices and a cheap REER.

Figure 82. MXN and Forwards



Blue – TIIE 26m fwd; Red – 1y1y fwd; Green – USD/MXN spot
Source: Bloomberg

Figure 83. Net Positioning (Blue) Favours USD/BRL (Orange)



Source: Citi and Bloomberg

We also keep a negative bias on USD/COP, which we expect to underperform most in Latam in the next three months, relative to current spot. COP is up by over 9% so

far this year vs. USD – four times more than BRL – and like the Brazilians, the central bank has fervently voiced its preference for a weaker exchange rate. The 1750 level looks difficult to break, especially as we expect the central bank to soon step up its FX purchases. Of course, as in 2009, central bank intervention will be calibrated as it has very limited sterilization capabilities – and, as was the case then, take some time to meaningfully weaken COP and forward points. Our forecasts have USD/COP at 1830 in the next three months, and 1800 in the medium term.

Brazil outperforms in Latam throughout the forecast horizon, relative to forwards. Investors are already quite long USD/BRL, which should restrain further appreciation in the cross (Figure 83). We doubt there will be further aggressive measures from either the central bank or the government as long as USD/BRL holds above roughly 1.80, although the central bank will probably continue to intervene at the margin. There has been talk of widening the IOF tax to also include FDI, chiefly to "catch" disguised portfolio flows. But we doubt that this materialises in the current scenario. The costs of such a tax almost certainly outweigh the benefits, not least because Brazil's heavily underinvested economy needs to attract foreign inflows and boost its investment rate. Our forecasts have USD/BRL at 1.84 in the next three months.

Finally, CLP, which is the most overtly China-sensitive and commodity-exposed Latam currency around. Unlike Brazil which is also linked to both China and commodities but is a fundamentally domestic demand driven economy, Chilean growth is led by exports where both copper and China dominate. USD/CLP has been trading in a tight 2% band since early March, but, with our commodites strategists expecting an additional correction in copper prices and growing risks surrounding continued Chinese expansion, we expect CLP to break through 490 in coming months. The outperformance of CLP over AUD has also been fairly extreme, also pointing to CLP weakness. Our forecasts have USD/CLP at 495 in 0-3 months time, and 500 over 6-12 months.

Contributors

** *Citi Foreign Exchange: Forecasts is* a joint venture between Citi's foreign exchange, global macro and technical strategy groups and our developed and emerging markets economists. The analysts listed below have contributed to these forecasts in one form or another.

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Figure 85. Citi Quarterly Interpolated Forecasts

Quarterly Interpolated Forecasts

	Currency	Spot	Jun-12	Sep-12	Dec-12	Mar-13	Jun-13	Sep-13	Dec-13	Mar-14	Jun-14
G10-US Dollar											
Euro	EURUSD	1.31	1.30	1.29	1.27	1.25	1.26	1.27	1.29	1.30	1.30
Japanese yen	USDJPY	81	81	81	80	80	81	82	84	85	85
British Pound	GBPUSD	1.59	1.57	1.56	1.55	1.54	1.56	1.59	1.61	1.64	1.65
Swiss Franc	USDCHF	0.92	0.92	0.94	0.95	0.97	0.97	0.96	0.96	0.96	0.96
Australian Dollar	AUDUSD	1.04	1.03	1.02	1.01	1.00	0.98	0.95	0.93	0.90	0.90
New Zealand Dollar	NZDUSD	0.82	0.82	0.81	0.80	0.78	0.75	0.71	0.67	0.64	0.63
Canadian Dollar	USDCAD	1.00	0.99	0.99	0.98	0.98	0.97	0.97	0.97	0.97	0.97
Dollar Index*	DXY	79.89	80.17	80.79	81.46	82.14	81.78	81.26	80.74	80.24	79.96
G10 Crosses											
Japanese yen	EURJPY	106	105	104	102	100	102	105	108	110	111
Swiss Franc	EURCHF	1.20	1.20	1.20	1.21	1.21	1.22	1.23	1.24	1.25	1.26
British Pound	EURGBP	0.82	0.83	0.83	0.82	0.82	0.81	0.80	0.80	0.79	0.79
Swedish Krona	EURSEK	8.87	8.85	8.82	8.79	8.75	8.73	8.70	8.68	8.65	8.65
Norwegian Krone	EURNOK	7.58	7.55	7.54	7.52	7.50	7.50	7.50	7.50	7.50	7.50
Norwegian Krone	NOKSEK	1.17	1.17	1.17	1.17	1.17	1.16	1.16	1.16	1.15	1.15
Australian Dollar	AUDNZD	1.26	1.26	1.26	1.27	1.28	1.31	1.35	1.39	1.42	1.43
Australian Dollar	AUDJPY	83.9	83.5	82.4	81.3	80.2	79.3	78.4	77.5	76.6	76.3
EM Asia											
Chinese Renminbi	USDCNY	6.30	6.31	6.28	6.25	6.22	6.20	6.17	6.14	6.11	6.10
Hong Kong Dollar	USDHKD	7.76	7.75	7.75	7.76	7.76	7.76	7.76	7.75	7.75	7.75
Indonesian Rupiah	USDIDR	9177	9368	9386	9369	9352	9339	9327	9314	9302	9289
Indian Rupee	USDINR	51.3	53.2	53.6	53.8	54.0	53.4	52.6	51.8	51.1	50.9
Korean Won	USDKRW	1135	1148	1138	1125	1112	1082	1049	1017	985	981
Malaysian Ringgit	USDMYR	3.06	3.08	3.05	3.02	2.98	2.96	2.94	2.92	2.90	2.91
Philippine Peso	USDPHP	42.7	43.0	42.7	42.4	42.0	41.9	41.8	41.6	41.5	41.5
Singapore Dollar	USDSGD	1.25	1.25	1.24	1.23	1.21	1.20	1.19	1.18	1.17	1.17
Thai Baht	USDTHB	30.8	31.0	30.8	30.5	30.2	30.1	30.1	30.0	30.0	30.0
Taiwan Dollar	USDTWD	29.5	29.7	29.4	29.1	28.8	28.7	28.5	28.4	28.2	28.3
EM Europe											
Czech Koruna	EURCZK	24.77	24.54	24.70	24.94	25.17	24.94	24.64	24.34	24.04	23.86
Hungarian Forint	EURHUF	298	298	294	290	286	286	287	289	290	289
Polish Zloty	EURPLN	4.18	4.15	4.14	4.13	4.12	4.07	4.02	3.96	3.91	3.90
Israeli Shekel	USDILS	3.75	3.79	3.84	3.89	3.94	3.94	3.93	3.91	3.90	3.86
Russian Ruble	USDRUB	29.6	29.8	30.5	31.2	32.0	32.1	32.1	32.2	32.2	32.0
Russian Ruble Basket	RUB	33.7	33.8	34.4	35.0	35.7	35.9	36.1	36.3	36.5	36.5
Turkish Lira	USDTRY	1.80	1.76	1.78	1.81	1.85	1.84	1.84	1.83	1.82	1.81
South African Rand	USDZAR	7.95	8.08	8.19	8.29	8.39	8.53	8.68	8.83	8.98	9.07
EM Latam											
Brazilian Real	USDBRL	1.84	1.84	1.82	1.80	1.77	1.76	1.74	1.72	1.70	1.71
Chilean Peso	USDCLP	485	494	496	498	500	498	495	493	490	490
Mexican Peso	USDMXN	13.2	13.2	13.0	12.8	12.5	12.4	12.4	12.3	12.2	12.3
Colombian Peso	USDCOP	1779	1823	1821	1811	1801	1811	1823	1836	1848	1857

* The DXY forecasts are implied from the forecasts of the constituent crosses.

Source: Citi Investment Research and Analysis

Figure 86. Citi Annual Forecasts

Annual Forecasts

	Currency	Spot	2012*	2013*	2014*	2015*	2016*
G10-US Dollar							
Euro	EURUSD	1.31	1.30	1.27	1.31	1.33	1.35
Japanese yen	USDJPY	81	81	82	85	85	85
British Pound	GBPUSD	1.59	1.57	1.57	1.65	1.68	1.71
Swiss Franc	USDCHF	0.92	0.93	0.97	0.96	0.97	0.98
Australian Dollar	AUDUSD	1.04	1.02	0.97	0.90	0.89	0.88
New Zealand Dollar	NZDUSD	0.82	0.81	0.73	0.63	0.63	0.62
Canadian Dollar	USDCAD	1.00	0.99	0.97	0.97	0.97	0.97
Dollar Index**	DXY	79.89	80.34	81.47	79.84	78.86	77.92
G10 Crosses							
Japanese yen	EURJPY	106	105	104	111	113	115
Swiss Franc	EURCHF	1.20	1.20	1.22	1.26	1.29	1.32
British Pound	EURGBP	0.82	0.83	0.81	0.79	0.79	0.79
Swedish Krona	EURSEK	8.87	8.82	8.72	8.65	8.63	8.62
Norwegian Krone	EURNOK	7.58	7.55	7.50	7.50	7.49	7.48
Norwegian Krone	NOKSEK	1.17	1.17	1.16	1.15	1.15	1.15
Australian Dollar	AUDNZD	1.26	1.26	1.33	1.42	1.42	1.41
Australian Dollar	AUDJPY	83.9	83.2	78.8	76.2	75.3	74.3
EM Asia							
Chinese Renminbi	USDCNY	6.30	6.28	6.18	6.10	6.07	6.04
Hong Kong Dollar	USDHKD	7.76	7.76	7.76	7.75	7.75	7.75
Indonesian Rupiah	USDIDR	9177	9317	9333	9283	9233	9183
Indian Rupee	USDINR	51.3	52.9	52.9	50.9	50.6	50.2
Korean Won	USDKRW	1135	1136	1065	982	984	988
Malaysian Ringgit	USDMYR	3.06	3.05	2.95	2.91	2.94	2.96
Philippine Peso	USDPHP	42.7	42.7	41.8	41.6	41.7	41.8
Singapore Dollar	USDSGD	1.25	1.24	1.20	1.17	1.18	1.19
Thai Baht	USDTHB	30.8	30.8	30.1	30.0	30.0	30.0
Taiwan Dollar	USDTWD	29.5	29.4	28.6	28.4	28.8	29.3
EM Europe							
Czech Koruna	EURCZK	24.77	24.74	24.77	23.79	23.15	22.52
Hungarian Forint	EURHUF	298	294	287	289	286	282
Polish Zloty	EURPLN	4.18	4.14	4.04	3.90	3.90	3.90
Israeli Shekel	USDILS	3.75	3.81	3.93	3.84	3.68	3.51
Russian Ruble	USDRUB	29.6	30.2	32.1	31.9	31.2	30.6
Russian Ruble Baske	RUB	33.7	34.2	36.0	36.6	36.7	36.9
Turkish Lira	USDTRY	1.80	1.78	1.84	1.80	1.73	1.66
South African Rand	USDZAR	7.95	8.06	8.61	9.11	9.42	9.74
EM Latam							
Brazilian Real	USDBRL	1.84	1.82	1.75	1.71	1.74	1.78
Chilean Peso	USDCLP	485	494	496	490	490	490
Mexican Peso	USDMXN	13.2	12.9	12.4	12.3	12.6	12.8
Colombian Peso	USDCOP	1779	1811	1818	1861	1895	1928

*Averages of end-quarter data shown in quarterly interpolation table.
** The DXY forecasts are implied from the forecasts of the constituent crosses.

Source: Citi Investment Research and Analysis

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