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Developed Markets
Western Europe

Euro Economics Weekly

Is the Period of German Outperformance Over?

- We cut our German growth forecasts once again, to 1.3% for 2014 and 1.6% for 2015 (from 1.6% and 2.0% previously). Including this revision, we have now cut our forecasts for cumulative German growth in 2014-15 by 1.6% since June. Prospects for exports and export-sensitive investment have deteriorated in particular. Germany is more vulnerable to external risks than other large Eurozone countries, in part because its export exposure is higher, including to currently stressed EM economies, such as Russia.
- But we acknowledge some uncertainty about the causes of the full extent of the weakening. Domestic demand prospects are also deteriorating. This is probably in part due to the adverse external influences, but appears to extend beyond business investment. For now, we expect these drags to be temporary, and for rising real wage growth, supportive financial conditions and a strong construction sector to return Germany to 0.4-0.5%QQ growth in 2015.
- In the near-term, weak German growth weighs on growth prospects for the rest of the Eurozone, and we believe makes it more likely that the ECB will announce a quantitative easing programme, likely in Q4.

Ebrahim Rahbari
+44-20-7986-6522
ebrahim.rahbari@citi.com

Guillaume Menuet
+44-20-7986-1314
guillaume.menuet@citi.com

Giada Giani
+44-20-7986-3281
giada.giani@citi.com

Michael Saunders
+44-20-7986-3299
michael.saunders@citi.com

Antonio Montilla
+44-20-7986-3282
antonio.montilla@citi.com

Ann O'Kelly
+44-20-7986-3297
ann.okelly@citi.com

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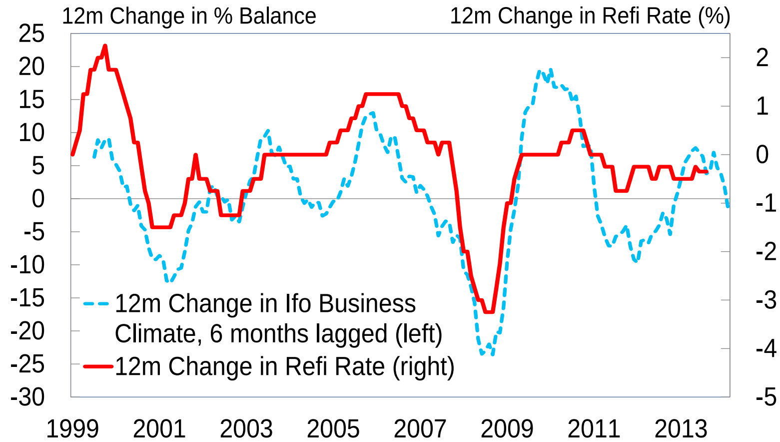
Ebrahim Rahbari

Figure 1. Citi Forecasts

	$/€	Euro Repo	10-yr Bunds	£/€	UK Bank Rate	10-Yr Gilt Bund
4Q 14	1.34	0.15	0.75	0.80	0.50	177
2Q 15	1.33	0.15	1.25	0.79	1.00	177

Source: Citi Research

Figure 2. Euro Area and Germany — 12-Month Change in ECB Refi Rate (%) and 12-Month Change in Ifo Business Climate (% Balance), 1999–2014



Sources: ECB, Ifo and Citi Research

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

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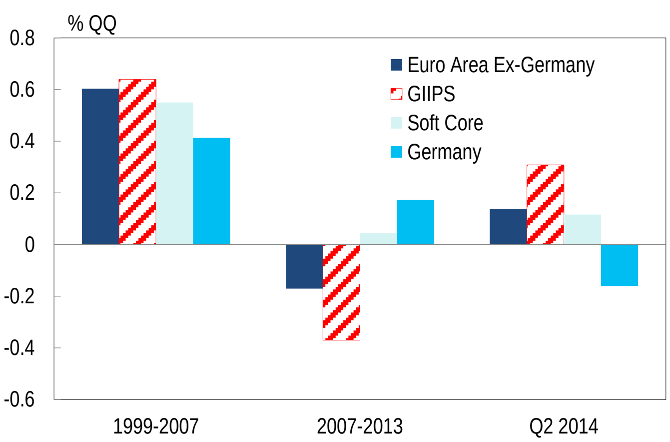
The End of German Outperformance?

We have long held the view that a combination of solid (public and private sector) balance sheets, very supportive financial conditions, a robust labour market with rising wage growth, and a strong housing market would allow Germany to grow at above-trend rates in 2014 and beyond and outgrow most other countries in the Eurozone. We have been revising down our German growth forecasts since June in light of the 0.2% contraction in German Q2 GDP, downward revisions to past data and a fairly steady flow of weak German data. Here, we revise our growth forecasts once more, to 1.3% in 2014 and 1.6% in 2015 (from 1.6% and 2.0%, respectively, most recently and 2.2% and 2.5% in June). We expect German GDP to grow by only 0.1-0.2%QQ on average in H2 and cannot rule out another contraction in Q3, which would put Germany technically into recession. German growth is thus unlikely to be much above Eurozone growth (and perhaps below) in the remainder of 2014 and likely to be lower than growth in recovering periphery countries, such as Ireland, Portugal or Spain. We stress two risks to this outlook: First, the relatively large sensitivity of German growth to external risks means that long-lasting or intensifying external weakness, or a larger impact of such external weakness on domestic demand, could lower our forecasts further. Second, if sentiment recovers (perhaps in part due to fading external risks), domestic demand may recover and push German growth back towards 2% growth earlier than we currently expect.

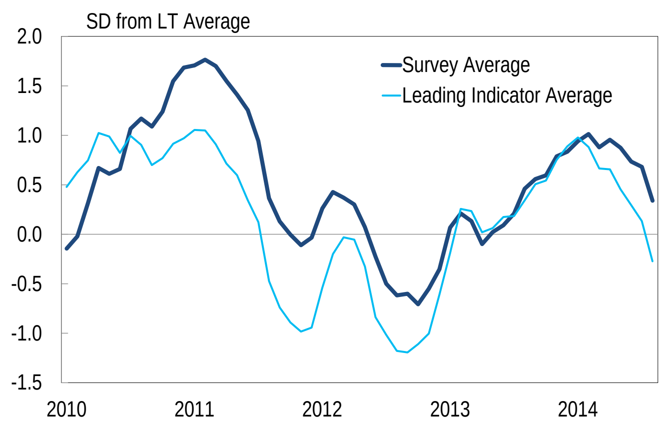
Figure 3. Selected Countries – Average Real GDP Growth (%QQ), 1999-2014 Q2



Note: GIIPS and Soft Core are GDP-weighted average of (Greece, Ireland, Italy, Portugal and Spain) and of (Austria, Belgium, Finland, France, Netherlands), respectively. For Ireland, Q2 2014 is Citi forecast.

Sources: Eurostat, Statistisches Bundesamt and Citi Research

Figure 4. Germany – Average of Ifo, ESI, ZEW, PMI and LEI Survey (SD from Long-Term Average), 2010 – 2014



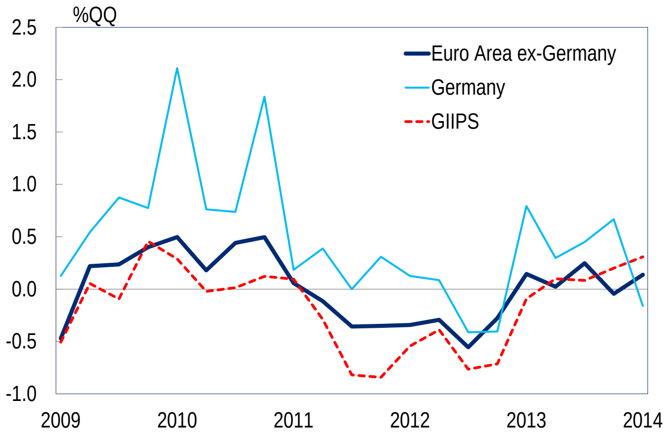
Note: Survey average is the simple average of the headline survey indicators (in standard deviations from long-term average). Leading Indicator Average is the average of the expectations components of the Ifo and ZEW surveys and the OECD's leading economic indicator (LEI). For the LEI, we assume that in July and August, it evolved in line with the average of the ZEW and Ifo expectations components.

Sources: Ifo, ZEW, European Commission, Markit, OECD and Citi Research

From Sick Man to Growth Engine

Between the start of EMU in 1999 and 2007, German GDP grew by 1.7% pa on average, compared to 2.2% pa for the Eurozone as a whole and 2.6% for the GIIPS countries (Greece, Ireland, Italy, Portugal and Spain). By contrast, between 2007 and 2013, Germany grew by 0.7% pa on average whereas real GDP for the Eurozone as a whole shrank by 0.3% pa and by 1.5% pa for the GIIPS countries. Q2 2014 (when German GDP fell by 0.2%QQ, Eurozone GDP was flat and GDP in the GIIPS countries grew by 0.3%QQ) was only the second quarter during which the Eurozone outgrew Germany (in QQ% terms) since the first quarter of 2009. The other instance was in Q1 2013, when German GDP fell by 0.4%QQ and Eurozone GDP fell by 0.2%QQ.

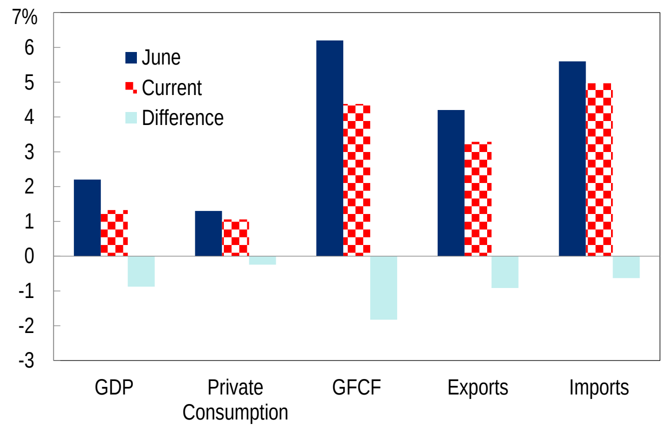
Figure 5. Selected Countries – Real GDP Growth (%QQ), 2009 - 2014



Note: GIIPS is GDP-weighted average of Greece, Ireland, Italy, Portugal and Spain. For Ireland, Q2 2014 is Citi forecast.

Sources: Eurostat, Statistisches Bundesamt and Citi Research

Figure 6. Germany – Citi Forecasts for 2014 Real Growth, June 2014 and Latest

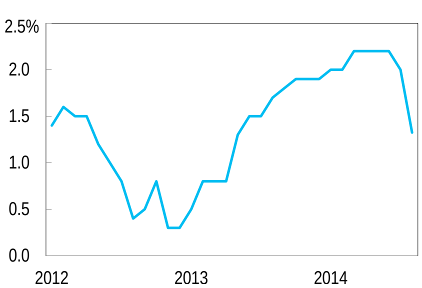


Source: Citi Research

Distorted Q2, But Weakening Momentum Is Still Evident

Two factors exaggerated the weakness in German Q2 GDP, in our view: the payback from temporary boosts to activity in Q1 (when GDP grew by 0.7%QQ) and a distortion from a higher-than-usual number of 'bridge days' (holidays falling on Tuesdays or Thursdays, prompting many employees to take an additional day off which are not reflected in the calendar-adjustment of GDP and various other economic data). In Q1, the average temperature in Germany was around 2.5 degrees centigrade warmer than the average Q1 temperature over the past twenty years, roughly a 1 ½ standard deviation difference. Even though the effects of unusual weather on GDP are difficult to assess, the Bundesbank estimated that the mild winter might have temporarily boosted German GDP (in particular construction activity) in Q1 by 0.3pp and potentially weighed on GDP growth in Q2 by a similar margin. The effects of bridge days are also difficult to estimate precisely, but according to the Bundesbank might have deducted 0.1pp off Q2 GDP (there was roughly one more bridge day in Q2 this year than usual). An additional factor may have been the transition to the new ESA 2010 methodology, which lowered estimates of German GDP growth for 2013 (and 2012) and may also have been a factor in the downward revision of Q1 growth to 0.7%QQ (from 0.8%QQ).

Figure 7. Germany – Citi Forecasts for 2014 Real GDP Growth (%), 2012-14



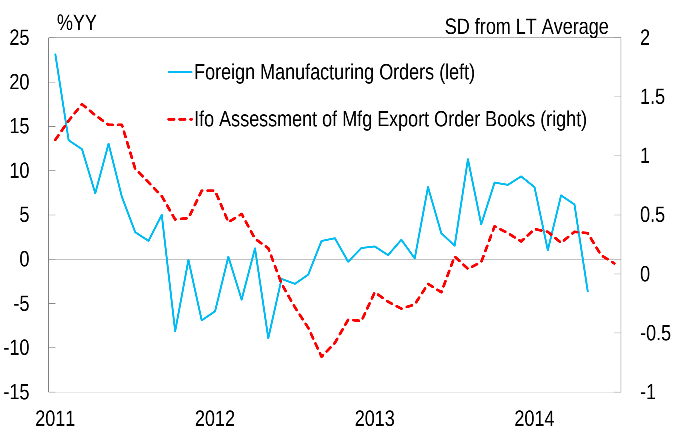
Sources: Citi Research

But even if we allowed for these two effects, GDP growth in Germany in Q2 would still only have been 0.2%QQ, compared with 0.7%QQ headline growth in Q1 or 0.4QQ% using the Bundesbank estimate for weather-adjusted growth. Furthermore, the outlook has weakened quite sharply too. For example, the average of the headline indices of the ZEW survey, the Ifo survey, the Composite PMI, the European Commission's ESI and the OECD's leading economic indicator (LEI) was 0.3 standard deviations (sd) above its long-term (LT, 1995-2014) average in August (assuming the LEI evolved in line with the other indicators), compared to 1.0 sd in March-May. The forward-looking components of the ZEW and the Ifo alone have weakened even more: in August, the average of the two was 01-0.2 sd *below* its LT average, whereas it had been more than 1 sd above its LT average in February. At its last available reading in June, the LEI for Germany was 0.1 sd above its LT average, compared to 0.5 sd in February.

Leading indicators and the limited data available for Q3 suggest that growth in Q3 will only be around 0.1%QQ according to our estimates. The IMK research institute in August put the probability of a recession in Germany (i.e. for growth in Q3 to be negative after the contraction in Q2) at 25%, sharply rising from below 10% in July, even though it also noted higher-than-usual uncertainty around its estimate. We have revised down our forecasts sharply since June (Figure 7), by 0.8pp each for 2014 and 2015. Lower growth in exports and export-sensitive business investment are the main drivers of our forecast revisions, but we have also revised down our forecasts of private consumption (Figure 6).

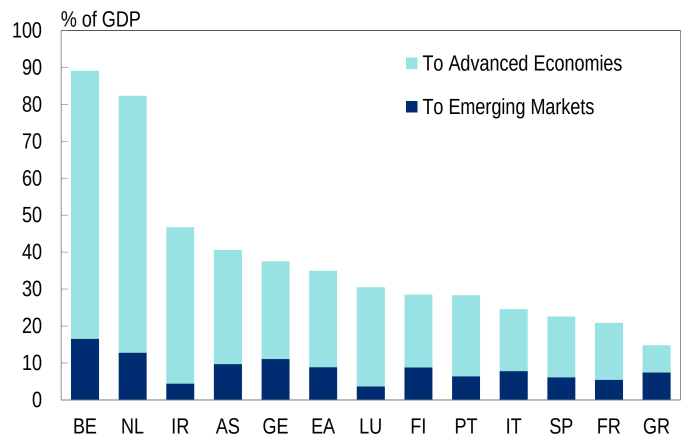
Germany's External Vulnerability

Figure 8. Germany – Foreign Manufacturing Orders (%YY) and Ifo Manufacturing Export Order Assessments (SD from Long-Term Average), 2011 – 2014



Sources: German Economy Ministry, Ifo and Citi Research

Figure 9. Selected Countries – Goods Exports to Advanced Economies and Emerging Markets (% of GDP), 2013



Sources: IMF and Citi Research

At least some of the weakness in Germany's recent performance has been 'imported', in our view. For example, Germany's nominal goods exports to Russia fell by 18%YY in May and Germany's export exposure to Russia is larger than in other major Eurozone countries. Total goods exports were stronger (they grew by 2.5%YY in Q2, similar to Q1) and German exports have been stronger in real terms and including services than for goods alone recently, but there are increasing signs that Germany's export prospects are weakening. For example, foreign manufacturing orders in Germany fell a combined 5.2% in May and June (latest available data) and were nearly 4%YY lower than a year ago in June. Survey assessments of export orders have also weakened (Figure 8).

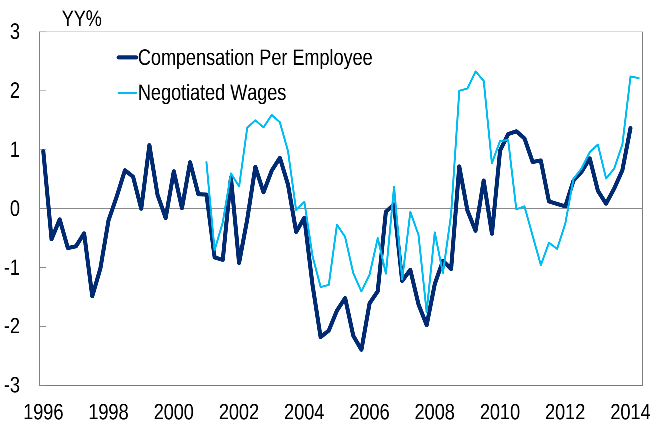
But beyond the latest high-frequency indicators, a key point is that German growth is relatively sensitive to adverse external shocks. In 2013, German exports of goods alone amounted to roughly 38% of GDP, compared to 21% for France, 23% for Spain and 25% for Italy. The share of German goods exports that are destined for EMs is relatively similar to that of other large Eurozone countries at around 30%, but that still implies a higher export exposure to EMs relative to GDP for Germany (11%) than for France (6%), Spain (7%) or Italy (8%).

We have long expected the net export contribution to German GDP growth to be negative in 2014 and beyond, based on strong import demand and a gradual deterioration in external competitiveness, as wage growth picks up in Germany. Long-lasting or intensifying external weakness would make a more significant dent into German growth prospects and remains a source of downside risk in our projections. So far, we have little indication that German export competitiveness is

eroding, but should the net export contribution remain negative even when domestic demand is weak, this would be a sign that German exports are becoming less competitive. Historically, investment in Germany has been sensitive to export prospects, and weak exports, perceptions of rising geopolitical risks and deteriorating sentiment more broadly are likely to weigh on investment prospects, too, Thus, it is worth noting that domestic orders for German capital goods fell by a combined 6.8% in May-June, and (along with weakening sentiment) suggesting that business investment in Germany is likely to contract in Q3.

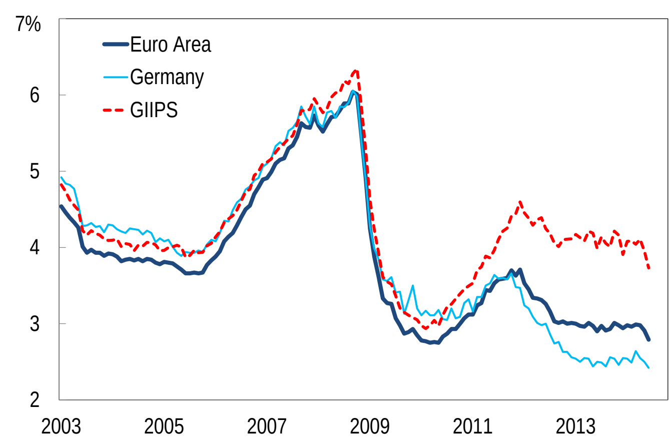
What About Domestic Demand?

Figure 10. Germany – Real Wage Growth (%YY), 1996 - 2014



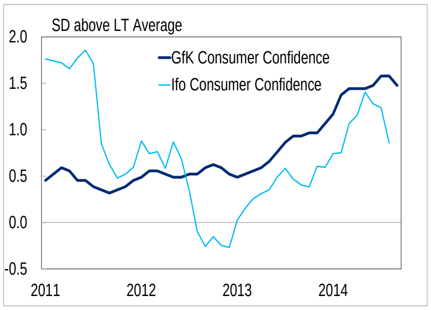
Note: Deflated by HICP.
Sources: Eurostat, Bundesbank and Citi Research

Figure 11. Selected Countries – Non-Financial Corporation Composite Cost of Borrowing Indicator (%), 2003-2014



Note: GIIPS are GDP-weighted average of Greece, Ireland, Italy, Portugal and Spain.
Sources: ECB and Citi Research

Figure 12. Germany – Consumer Confidence (SD above LT Average), 2011-14



Sources: GfK, Ifo and Citi Research

We had expected domestic demand to be the main driver of German outperformance in 2014 and beyond. In the previous section, we already noted that external factors are weighing on investment prospects. Recent (and broad-based) declines in consumer confidence indicators (both GfK and Ifo/EC), and indeed weak retail sales data for July, suggest that external weakness is also likely to seep into domestic demand prospects beyond their impact on business investment. In Q2, domestic demand was probably flat and we have also revised down our forecasts for domestic demand growth, to 1.6% for 2014 and 2.0% for 2015 (from 1.8% and 2.5%).

A key question is therefore whether Germany lost its growth engine (exports) without domestic demand growing strongly enough to replace it. In our view, the essential elements of the narrative of rebalancing in the German economy towards domestic demand growth are mostly intact and we still expect domestic demand to be the main driver of German growth. But the prospects for domestic demand to grow are not quite as favourable, at least in the near-term, as we thought previously, and the downside risks are larger, in our view. This also implies that domestic demand in Germany may not grow fast enough to compensate for potential external weakness and still outperform the periphery countries in recovery mode. Here we reiterate the three main factors that underlie our expectation of fairly robust domestic demand (by German standards) in Germany in coming years: i) a robust labour market, ii) very easy financial conditions, and iii) a strong housing and construction sector. In addition, in the near-term positive population growth and a slight loosening of the fiscal stance compares favourably with the poor demographic and fiscal outlook in many other Eurozone countries.

The Labour Market Remains Strong

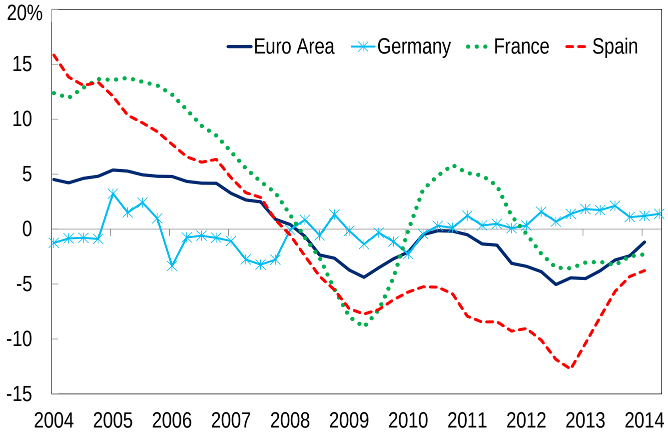
Germany's labour market remains robust. Harmonised unemployment in Germany stood at 5.1% of the labour force in Q2, thus remaining at the lowest value since at least 1991, even though trend declines in hours worked exaggerate the increase in employment since the global financial crisis. Employment grew by 0.4%QQ in Q1 (seasonally-adjusted). In Q2 job growth probably slowed, but monthly data suggest it remained close to 1%YY and survey indicators such as employment expectations in the ESI survey or the Ifo survey remain 0.5-1.0 SD above their long-term averages. Furthermore, wage growth is gradually picking up, too. In nominal terms, compensation per employee in Germany was 2.5%YY higher in Q2 (roughly twice its historical average) and negotiated wages rose by 3.5%YY (highest growth rate since the mid-1990s). In real (CPI-deflated) terms, these are close to the highest growth rates for around two decades for both measures. In our view, high employment and growing real wages are likely to boost private consumption eventually, even if the process has been slower than we had expected. By contrast, Eurozone unemployment remains extremely high (at 11.5% for the Eurozone average and 18.5% on average in GIIPS countries). Eurozone employment growth turned marginally positive in Q1 (at +0.1 YY% growth) for the first time since Q4 2011, but would still have been negative without job growth in Germany and remained negative in GIIPS countries on average.

Financial Conditions And Housing

Financial conditions in Germany also remain very supportive, both internally and externally. German non-financial corporations (NFCs) generate sizable financial surpluses (3.3% of GDP in Q1) and therefore often do not need to rely on external funding. External funding conditions are favourable too. For example, according to the Ifo credit constraint survey, credit constraints for German firms remain close to their record-lows (the data start in 2003). The average borrowing rate for NFCs in Germany in June 2014 was at its lowest level since at least 2003 and 40bp below the Eurozone average in nominal terms, and in contrast to the pre-crisis period where German NFC borrowing costs were above the Eurozone average. In real (CPI-deflated terms), the differences are larger: German NFC borrowing rates are 90bp below the EA average and 240bp below the GIIPS's (whereas they were 70bp and 100bp higher pre-crisis, respectively) and that difference has yet to decline materially from its recent peak. Bank lending standards eased modestly in Q2 for the Eurozone as a whole, but had tightened much more sharply (in the Eurozone periphery in particular), in the period since the financial crisis than in Germany.

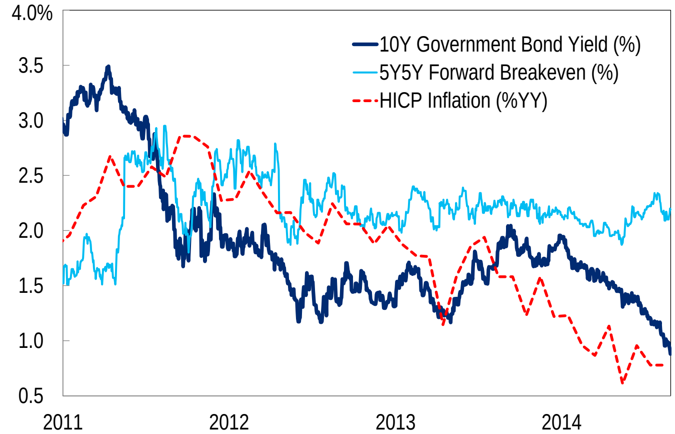
Construction investment in Germany most likely fell quite sharply in Q2, but mostly as a payback to the 3.6%QQ rise in Q1. Overall, housing and construction remain a source of strength for the German economy (we expect construction investment to grow by around 4% pa in 2014-15). Housing permits are still growing at double-digit growth rates. A composite construction indicator (the simple average of the construction components of the PMI, ESI, Ifo and ZEW surveys) is below its recent highs, but remains more than 1 SD above its LT (post-1999) average. Meanwhile, German house prices are still rising (even though at only modest rates), the population is growing and real house prices remain cheap in historical comparison. By contrast, in much of the euro area, the construction sector remains subdued. According to ECB data, house prices are currently still falling in nominal and real terms in all of the large EA economies except Germany (France, Italy, the Netherlands and Spain) as well as a number of other countries. Construction activity in the Eurozone is rebounding from low levels in a number of countries where it had collapsed, but is contracting in France, Italy and the Netherlands among others, leaving overall construction activity outside of Germany very subdued.

Figure 13. Germany and the Euro Area – Real House Price Growth (%YY), 2004-14



Sources: Eurostat, IMF and Citi Research

Figure 14. Germany – 10Y Sovereign Bond Yield, 5y5y Forward Breakeven Rate and HICP Inflation (%), 2011-2014



Sources: Bloomberg, Statistisches Bundesamt and Citi Research

Could German Bad News Pave the Road for QE?

Weaker German growth should also impede growth prospects for the mostly demand-deficient remainder of the Eurozone. But weak German growth and persistently low German inflation make additional easing by the ECB more likely. German inflation in August remained at 0.8%YY and is likely to be only around 1% in 2014 as a whole, much lower than our and consensus expectations at the beginning of the year that it would reach 1.5%. Market-based long-term expectations for German inflation have also ticked down in August after steadily rising for most of the previous three months. And 10Y Bund yields have steadily been falling (and roughly halved) over the last year, probably at least in part due to expectations that inflation would remain low and growth weak (even though safe haven demand for German assets and expectations of further ECB easing have also played a role).

In theory, the ECB might still announce further easing even if German economic data and prospects are not weak. But weak German data make additional ECB easing more likely, in our view, for two reasons. First, low growth and low inflation in Germany make it even likelier that growth and inflation in the Eurozone will remain very subdued, even if a few countries manage to modestly outgrow Germany. At its September ECB meeting, we expect the ECB to revise down its expectations for Eurozone growth in 2014 to a mere 0.8% (in line with our forecast), and further downgrades may follow. Second, even though even the German representatives on the ECB Governing Council in principle decide on the appropriate monetary stance for the Eurozone as a whole, we consider it likely that downside risks to the German growth and inflation outlook would reduce their opposition to a quantitative easing programme and perhaps even lead them to openly support such a decision.

Overall, the weaker German outlook therefore reinforces our view that the ECB is likely to announce a broad-based asset purchase programme in coming months – we currently expect such an announcement in Q4. On the other hand, we do not expect the German government to ease fiscal policy in response to weaker German growth.

Figure 15. Key Economic Indicators (1 September – 5 September 2014)

		Forecast	Last
During The Week		**Forecast**	**Last**
08:00	UK: Halifax House Prices, Aug		
Monday 1 September		**Forecast**	**Last**
07:00	Germany: GDP Details, 2Q	-0.2% QQ, 1.2% YY	0.7% QQ, 2.2% YY
07:30	Sweden: Manufacturing PMI, Aug	54.9	55.2
08:00	Norway: Manufacturing PMI, Aug	50.4	50.6
09:00	Norway: Credit Indicator C2, Jul	5.4% YY	5.4% YY
09:00	Euro Area: Manufacturing PMI, Aug Final	50.8	51.8
09:30	UK: Manufacturing PMI, Aug	56.0	55.4
09:30	UK: Mortgage Approvals, Jul	68.0K MM, 10.3% YY	67.2K MM, 14.2% YY
10:00	Greece: GDP Details, 2Q		
10:00	Cyprus: GDP Details, 2Q		
	Italy: Budget Balance, Aug		
Tuesday 2 September		**Forecast**	**Last**
06:45	Switzerland: GDP, 2Q		
08:00	Spain: Unemployment, Aug	-45K MM	-30K MM
09:30	UK: Construction PMI, Aug		
10:00	Euro Area: Industrial Producer Prices, Jul		
14:00	Belgium: GDP Details, 2Q	0.1% QQ, 1.1% YY	0.4% QQ, 1.2% YY
Wednesday 3 September		**Forecast**	**Last**
07:30	Sweden: PMI Services, Aug	57.3	60.1
09:00	Euro Area: Services PMI, Aug Final	53.5	54.1
	Composite PMI, Aug Final	52.8	53.8
09:30	UK: Services PMI, Aug	58.5	59.1
10:00	Euro Area: Retail Sales, Jul	-0.5% MM, 0.7% YY	0.4% MM, 1.9% YY
10:00	Euro Area: GDP Details, 2Q	0.0% QQ	0.2% QQ
Thursday 4 September		**Forecast**	**Last**
06:30	France: Mainland Unemployment Rate, 2Q	9.8%	9.7%
07:00	Germany: Incoming Orders, Jul	0.2% MM, 1.3% YY	-1.7% MM, 5.8% YY
08:30	Netherlands: Consumer Prices, Aug		
08:30	Sweden: Riksbank Interest Rate Decision	Unchanged at 0.25%	0.25%
09:00	Norway: Labour Costs, 2Q		
12:00	UK: MPC Outcome		
12:45	Euro Area: ECB Outcome (Press Conference at 13:30)		
Friday 5 September		**Forecast**	**Last**
07:00	Germany: Industrial Production, Jul	2.1% MM, 1.3% YY	-1.8% MM, 1.2% YY
07:45	France: Consumer Confidence, Aug	86	86
08:15	Switzerland: Industrial Production, 2Q		
08:30	Sweden: Industrial Production, Jul	0.3% MM	1.0% MM
08:30	Sweden: Services Production, Jul	0.4% MM	0.1% MM
09:00	Norway: Manufacturing Production, Jul	-0.5% MM	1.7% MM

Source: Citi Research

Figure 16. Economic Indicators – Comments: Euro Area, Germany and France

Euro Area			
Sep 1 09:00 London Time	*Manufacturing PMI, Aug F*	Forecast: 50.8	Prior: 51.8
	The flash PMI estimate, showing a drop of 1.0 point MM, should be confirmed in the final reading. The manufacturing PMI is now clearly below the Jan peak of 54.0, marginally below its long-run average (-0.1SD) and, with the exception of a small rise in April, it has been falling every month since February. The August decline has likely been larger in the euro area periphery countries (namely Italy and Spain) than in Germany and France, based on the flash estimates available so far.		
Sep 3 09:00 London Time	*Services PMI, Aug F* *Composite PMI, Aug F*	Forecast: 53.5 Forecast: 52.8	Prior: 54.1 Prior: 53.8
	Composite PMI likely to be confirmed down by a full point in August relative to July, entirely reversing the July gain, on evidence that economic weakness is now extending from the manufacturing sector to the services sector as well. The August drop is likely to have been more pronounced in the periphery than in Germany or France (actually French composite PMI was up, according to the flash estimate). The composite PMI at around these levels has been consistent in the past with GDP growth of around 0.3%-0.4% QQ in Q3.		
Sep 3 10:00 London Time	*Retail Sales, Jul*	Forecast: -0.5% MM, 0.7% YY	Prior: 0.4% MM, 1.9% YY
	Retail spending likely decelerated in July, after three consecutive monthly gains. The retail sector sentiment surveys have been signalling a slowdown in activity in the past two/three months, and this should get reflected in the hard data for July, after retail sales grew by 0.4% QQ in Q2 14.		
Sep 3 10:00 London Time	*GDP, Q2 Details*	Forecast: 0.0% QQ	Prior: 0.2% QQ
	The second GDP reading for Q2 will confirm the euro area recovery stalled, showing a flat real GDP level relative to Q1. The breakdown details released for the first time will likely show private consumption expanded at a slightly faster rate than in previous quarters (by 0.3% QQ), but this was likely offset by a drop in investment and no growth in public consumption. Exports have probably rebounded in Q2 (by around 1% QQ), after a depressed Q1 reading (+0.2% QQ), but the net export contribution to GDP growth has probably been minimal. The overall pace of export growth (+2.7% YY estimated for Q2) remains quite subdued by historical standards and partly explains the weak recovery.		
Germany			
Sep 1 07:00 London Time	*GDP, Q2 Details*	Forecast: -0.2% QQ, 1.2% YY	Prior: 0.7% QQ, 2.2% YY
	We expect the first detailed reading of Q2 2014 GDP in Germany to confirm the flash estimate of -0.2% QQ growth, bringing YoY growth down to 1.2%. The German statistical office noted in its press release that both private and public consumption still grew, but that investment (and in particular construction investment) fell during Q2 and net trade deducted from GDP growth. Even though the Q2 reading was distorted by some temporary influences, it is clear that the momentum in German activity has moderated. Both soft and hard data remain weak in Germany as we enter Q3, leading us to expect growth to return to positive territory in H2 but only moderately so.		
Sep 4 07:00 London Time	*Factory Orders*	Forecast: 0.2% MM, 1.3% YY	Prior: -1.7% MM, 5.8% YY
	German industrial orders fell sharply in June, in particular due to very weak large orders (excluding large orders, industrial orders in June rose 4.1% MM vs a 3.2% fall including large orders). Such a large decline is invariably followed by a sizable increase of 1.5-3%. However, we are more cautious and expect the continued weakness in German sentiment to suggest a smaller-than-usual rebound in July, which would leave the July level still 1.6% lower than the Q2 average (which was itself lower than the Q1 average).		
Sep 5 07:00 London Time	*Industrial Production incl Construction (SWDA)*	Forecast: 2.1% MM, 1.3% YY	Prior: -1.8% MM, 1.2% YY
	We expect industrial production (including construction) in Germany to be pretty much flat in July. In June, IP rose slightly, but it did so for the first time in four months. But weak orders and sentiment data suggest that IP is likely to remain weak, with IP in Q2 1.5% below Q1 and the July level 0.5% lower still.		
France			
Sep 4 06:30 London Time	*ILO Mainland Unemployment Rate (2Q)* *Mainland Unemployment Change (000s)*	Forecast: 9.8% Forecast: 45K	Prior: 9.7% Prior: 23K
	Mainland unemployment likely rose by around 45k in the second quarter, almost double the 1Q increase to taking the jobless rate to a four-quarter high of 9.8%. With GDP having flat-lined in the first half of 2014, we estimate that the jobless rate will remain on an upward trajectory until Q3 when we forecast it to peak at 10%. We see upside risks to this forecast base on the recent deterioration in private employment expectations based on the July surveys.		
Sep 5 07:45 London Time	*Consumer Confidence Indicator, Aug*	Forecast: 86	Prior: 86
	Consumer confidence is expected to be unchanged at 86 (-1.6 standard deviation below its historical average) in August. We doubt that low-income households will have incorporated just yet in their expectations President Hollande's latest promises of tax cuts. Although low inflation is supporting purchasing power gains, the persistent uptrend in unemployment is likely to act as a negative influence in sentiment.		

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

Figure 17. Economic Indicators – Comments: Spain, Belgium and Sweden

Spain			
Sep 2 08:00 London Time	*Registered Unemployment, Aug ('000)*	Forecast: -45K MM	Prior: -30K MM
	We expect the number of jobless claimants to fall by 44.5K in August, after MM declines of 29.8K and 122.7K in July and June respectively, with the job market continuing to be supported by the labour-intensive summer season. The seasonally-adjusted series should also show an improvement (we estimate registered unemployment fell by 1% MM in Aug in SA terms), after a weak reading in July (of +0.6% MM). While the improvements in the labour market have been quite sizable in the past year, the drop in jobless claimants is probably overestimating the gains (compared, for example, with the labour force survey), due to fewer unemployed being able to access unemployment benefits.		
Belgium			
Sep 2 14:00 London Time	*GDP, 2Q F*	Forecast: 0.1% QQ, 1.1% YY	Prior: 0.4% QQ, 1.2% YY
	We lowered our 2014-15 GDP growth forecasts by 0.2pp each to 1.1% and 1.3% respectively. Although the flash estimate of Q2 GDP showed a fifth successive gain, the pace of economic activity slowed to 0.1% QQ and 1.1% YY, mirroring the trend of declining business and consumer confidence in Q2-14. Indications of further deterioration in July surveys are part of the reason behind our decision to cut our forecasts. On the political front, parties are continuing to negotiate to form a government coalition, a situation that should help limit fiscal uncertainty.		
Sweden			
Sep 1 07:30 London Time	*Manufacturing PMI, Aug*	Forecast: 54.9	Prior: 55.2
	The manufacturing PMI gained 0.4 point to 55.2 in July, and now stands slightly above its long-term average of 54.4, signalling a modest recovery for industry. NIER manufacturing sentiment also recovered slightly in July, but with a reading of 101.0 still signals a cautious recovery for the sector. With the escalation of the crisis in Ukraine and new sanctions in Russia, we reckon this has probably driven the manufacturing PMI a tad lower in August =- as has also been the case in Germany and the euro area. The trend in hard data remains weak compared to sentiment indicators; industrial production slipped by 1.2% QQ in 4Q-13, by 0.3% QQ in 1Q-14, and by 0.7% in 2Q.		
Sep 3 07:30 London Time	*Services PMI, Aug*	Forecast: 57.3	Prior: 60.1
	The services sector PMI jumped 5.5 points to 60.1 in July, the highest reading since April 2011. The series, though, is very volatile and one gets a more precise picture by looking at three-month moving averages. On this basis, the services PMI ticked slightly higher, to 57.7 in the three-month period May-July, the highest level in three years. Service sector sentiment, according to NIER, has been mixed, with sentiment in private services having ticked gradually lower since the outset of the year to stand below the long-term average (98.7 in July), while retail trade confidence remains well above the historical average (110.0 in July). In August, we expect the services PMI to fall, partly as a payback after a larger-than-expected rebound in July.		
Sep 4 08:30 London Time	*Riksbank Interest Rate Decision*	Forecast: Unchanged at 0.25%	Prior: 0.25%
	We expect the Riksbank board to keep the key policy rate, the repo rate, unchanged at 0.25%, while at the same time lowering its conditional interest rate path and, in turn, postpone the timing of initial tightening to 1H-16. With the somewhat disappointing development in domestic economic activity indicators since the July meeting, the downward trend in inflation expectations, intensified geopolitical risks and expected QE easing by the ECB, we acknowledge that the Riksbank could decide to cut rates again, and see a small chance of this happening already at the September meeting.		
Sep 5 08:30 London Time	*Industrial Production, Jul*	Forecast: 0.3% MM	Prior: 1.0% MM
	Manufacturing production managed to recover only partly in June, after the 3.0% MM plunge in May, and the trend, hence, remains weak with no signs of recovery taking place. This is weaker than other indicators. For instance, companies signal an increase in production as well as in order intake according to various business surveys, but there is still no clear turnaround in hard data		
Sep 5 08:30 London Time	*Services Production, Jul*	Forecast: 0.4% MM	Prior: 0.1% MM
	While the industrial sector continues to struggle, developments in services production are more encouraging; although production only gained a meagre 0.1% MM in June (after a 1.0% MM drop in the previous month), the trend is still healthy. In line with sentiment indicators, we expect the healthy trend in service sector production to continue. We note, though, that production data has not been a reliable indicator for GDP over the last year or so. That said, ongoing strength in service sector production supports our forecast of ongoing recovery for GDP in the second half of the year.		

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

Figure 18. Economic Indicators – Comments: Norway and United Kingdom

Norway			
Sep 1 08:00	*Manufacturing PMI, Aug*	Forecast: 50.4	Prior: 50.6
London Time	Escalation of the crisis in Ukraine and new sanctions in Russia may have driven the manufacturing PMI a tad lower in August, in line with the developments seen in German and euro area manufacturing PMIs. We note, though, that the PMI tends to be very volatile, and is not closely watched by Norges Bank as there often are problems with the seasonal adjustment procedure (especially around holidays). PMI also covers a very small sample compared to e.g. Norges Bank's own Regional Network Report (RNR) and the quarterly BTS, and has little value in predicting actual production.		
Sep 1 09:00	*Credit Growth Indicator C2, Jul*	Forecast: 5.4%	Prior: 5.4%
London Time	The latest lending survey showed that household credit demand was up further in 2Q, likely reflecting the recovery in the housing market. Meanwhile, this has not been reflected in the monthly credit growth indicator for households, which fell 0.1pp to 6.7% YY in 2Q. With positive house price growth in the past five months, a large downward correction on the housing market has become more remote, suggesting that household credit demands could pick up in the near term. The latest lending survey also showed a pick-up in credit demand from non-financial enterprises. The monthly development in corporate credit growth, meanwhile, moderated further in 2Q from 3.3% YY in 1Q to 3.0% YY.		
Sep 5 09:00	*Manufacturing Production, Jul*	Forecast: -0.5% MM	Prior: 1.7% MM
London Time	Momentum in manufacturing production improved further in June and with a surprise 1.7% MM gain, quarterly growth improved to 1.3% in 2Q, up from 1.2% QQ in the first quarter. Manufacturing surveys, meanwhile, send mixed signals; the sentiment indicator in the latest 2Q Business Tendency Survey surprisingly improved from 6.6 to 7.5, hence, nearly matching the 4Q-13 outcome, which was the strongest since early-2012. In addition, the level is slightly above the historical average and is consistent with above-trend production growth. Manufacturing PMI, on the other hand, has been subdued lately with the three-month average standing at 49.9 in 2Q, hence, signalling stagnation. We expect a payback in manufacturing production in July following the strong June gain.		
United Kingdom			
Sep 1 09:30	*Manufacturing PMI, Aug*	Forecast: 56.0	Prior: 55.4
London Time	The July survey showed the manufacturing PMI falling by 1.7 points, the biggest MM decline since Feb-2013 (when it fell 2.9 points). We look for a reversal of part of that drop, leaving the index close to the H1 average (56.6). Indeed, it is worth noting that the Feb-2013 decline was followed by a 2.1-point rise in March 2013.		
Sep 1 09:30	*Mortgage Approvals, Jul*	Forecast: 68.0K MM, 10.3% YY	Prior: 67.2K MM, 14.2% YY
London Time	Mortgage approvals rebounded in June after softer readings in April and May (which may have been capped by the lengthier approval process caused by the late-April Mortgage Market Review). We look for another uptick this month, consistent with other signs that housing activity remains buoyant.		
Sep 3 09:30	*Services PMI, Aug*	Forecast: 58.5	Prior: 59.1
London Time	The trade deficit has averaged £2.1bn per month so far this year, slightly down from £2.4bn per month in 2013 and £2.8bn in 2012. Although the growth of exports of goods is sluggish, import volumes have been flat, while import prices are falling and the surplus on trade in services is rising. We look for the July figure to be similar to the average of the year to date.		

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

Figure 19. Key Economic Indicators (8 September – 14 September 2014)

Monday 8 September		Forecast	Last
06:45	Switzerland: Unemployment, Aug		
07:00	Germany: Trade Balance, Jul		
07:00	Germany: Labour Cost Index, 1Q		
07:30	France: Bank of France Business Sentiment, Aug		
08:15	Switzerland: Consumer Prices, Aug		
08:15	Switzerland: Retail Sales, Jul		
09:30	Euro Area: Sentix Investor Confidence, Sep		
10:00	Portugal: GDP Details, 2Q		
Tuesday 9 September		**Forecast**	**Last**
07:45	France: Trade Balance, Jul		
07:45	France: Budget Balance, Jul		
08:30	Netherlands: Industrial Production, Jul		
09:30	UK: Trade Balance – Goods & Services, Jul	£-2.2 Billion	£-2.5 Billion
09:30	UK: Industrial Production, Jul	0.4% MM, 1.5% YY	0.3% MM, 1.2% YY
	Manufacturing Output, Jul	0.5% MM, 2.4% YY	0.3% MM, 1.9% YY
10:00	Greece: Industrial Production, Jul		
Wednesday 10 September		**Forecast**	**Last**
07:45	France: Nonfarm Payrolls, 2Q		
07:45	France: Industrial Production, Jul		
08:00	Spain: Industrial Production. Jul		
09:00	Norway: Consumer Prices, Aug		
10:00	Greece: Consumer Prices, Aug		
Thursday 11 September		**Forecast**	**Last**
00:01	UK: RICS House Price Survey, Aug		
07:00	Germany: Consumer Prices, Aug Final		
07:00	Sweden: PES Unemployment Rate, Aug		
07:45	France: Consumer Prices, Aug		
08:30	Sweden: Consumer Prices, Aug		
08:30	Sweden: Unemployment, Aug		
09:00	Euro Area: ECB Monthly Bulletin		
10:00	Greece: Unemployment Rate, Jun		
Friday 12 September		**Forecast**	**Last**
	Euro Area: Informal EcoFin Meeting of EU Finance Ministers, Milan (to Sep 13)		
07:45	France: Balance of Payments, Jul		
08:00	Spain: Consumer Prices, Aug Final		
08:30	Netherlands: Trade Balance, Jul		
09:00	Italy: Industrial Production, Jul		
09:00	Norway: Norges Bank Regional Network Report		
09:30	UK: Construction Output, Jul		
10:00	Italy: Consumer Prices, Aug Final		
10:00	Euro Area: Industrial Production, Jul		
10:00	Euro Area: Employment, 2Q		
	Euro Area: Informal Meeting of EA Finance Ministers, Milan		
During the Weekend		**Forecast**	**Last**
	EU: Informal Meeting of EU Finance Ministers, Milan		
Sep 14	Sweden: General Election		

Sources: National statistical offices, central banks and Citi Research

Figure 20. Recent Research

Euro Area - Sovereign Debt Update		
France's Hollande calls for euro area 'growth' summit	European Economics Team	Aug 29, 2014
Merkel Urges Reforms in France, But Hints at Some Budgetary Flexibility	European Economics Team	Aug 28, 2014
German FM: Draghi's fiscal comments 'overinterpreted'	European Economics Team	Aug 27, 2014
France: New government likely this afternoon	European Economics Team	Aug 26, 2014
Euro Area		
Euro Area - ECB Preview: Will Draghi Highlight Downside Risks to Inflation?	Guillaume Menuet	Aug 28, 2014
Euro Area - ECB Draghi Notes Fall in Inflation Expectations	Guillaume Menuet	Aug 26, 2014
Global Economic Forecasts – August 2014	Michael Saunders	Aug 26, 2014
Euro Area - PMIs Suggest Very Little Room for Economic Rebound in H2 14	Giada Giani	Aug 21, 2014
Euro Area - SPF Survey: Downward Drift In 2014-15 Inflation Expectations	Guillaume Menuet	Aug 14, 2014
Euro Area: NFC Net Borrowing Falling More Slowly	Antonio Montilla	Aug 12, 2014
European Economic Indicators – Week Ahead	Michael Saunders	Aug 8, 2014
Euro Area - ECB – Happy To Wait And See, For Now	Giada Giani	Aug 7, 2014
Italy - Why is the Economy Underperforming so Badly?	Giada Giani	Aug 6, 2014
Europe: Monthly Inflation Profiles for Selected Countries	Ann O'Kelly	Jul 31, 2014
European Economic Forecast Highlights, July 2014	Ann O'Kelly	Jul 31, 2014
Spain: Economic Recovery Strengthens in Q2	Antonio Montilla	Jul 31, 2014
Euro Area: Lending Survey Records Improving Credit Demand	Ebrahim Rahbari	Jul 31, 2014
Euro Area: Periphery-Core Rebalancing Continues in July	Ebrahim Rahbari	Jul 30, 2014
New 2015 ECB Calendar: Governing Council Meetings	Guillaume Menuet	Jul 18, 2014
Euro Area - ZEW Survey Confirms Downside Risks to Economic Activity	Guillaume Menuet	Jul 15, 2014
Portugal - One Lender Causes Widespread Market Turbulence	Giada Giani	Jul 10, 2014
Euro Area - Financial Conditions Improve in Q2, But Remain Tight	Giada Giani	Jul 9, 2014
Euro Economics Weekly		
ECB QE: Why, When and How?	Guillaume Menuet	Aug 22, 2014
What's Behind the Periphery Growth Outperformance?	Giada Giani	Aug 15, 2014
How Might Russia Developments Affect The Eurozone Economy?	Ebrahim Rahbari	Aug 1, 2014
France: More Reforms to Jump Start Confidence?	Guillaume Menuet	Jul 25, 2014
Public Debt Sustainability: Has It Really Been Restored?	Giada Giani	Jul 18, 2014
Why Banking Union Matters: Then and Now	Ebrahim Rahbari	Jul 11, 2014
Is The Euro Area Recovery at Risk of Faltering?	Guillaume Menuet	Jul 4, 2014
Weak Pay Trends Imply Further Inflation Undershoot	Giada Giani	Jun 27, 2014
A Great Rotation towards Eurozone Portfolio Assets?	Ebrahim Rahbari	Jun 20, 2014
Labour Market Slack	Giada Giani	Jun 13, 2014
ECB TLTRO: Ambitious But Probably Not Enough, QE Lies Ahead	Guillaume Menuet	Jun 6, 2014
Negative Deposit Rate: Limiting Risks, Limited Upside	Ebrahim Rahbari	May 30, 2014
Soft Growth, Low HICP And Weak SPF Point To ECB Cut In June	Guillaume Menuet	May 23, 2014
Long Live (s) The Rise of the Current Account Surplus	Ebrahim Rahbari	May 16, 2014
Euro Economics Weekly - How Might QE Affect Financial Conditions?	Giada Giani	May 9, 2014
ECB: Reaction Function Points to Looser Stance Ahead	Guillaume Menuet	May 2, 2014
Chief Economist Publications		
Global Economic Outlook and Strategy — August 2014	Willem Buiter	Aug 20, 2014
Scandi		
Scandi Economics Update	Tina Mortensen	Aug 29, 2014
Sweden - Election Update: Uncertain Government Constellation;	Tina Mortensen	Aug 22, 2014
Sweden - Riksbank Forecast: Stable Rates, Lower Interest Rate Path;	Tina Mortensen	Aug 22, 2014
Norway - Mainland GDP Growth At Well-Above Trend In 2Q	Tina Mortensen	Aug 21, 2014
UK		
UK - Key Results in the European Commission Survey	Michael Saunders	Aug 28, 2014
UK - Update on Under-Employment	Michael Saunders	Aug 22, 2014
UK - Scottish Independence Referendum: Less Than A Month To Go	Michael Saunders	Aug 22, 2014
UK - Retail Sales and Fiscal Data	Michael Saunders	Aug 21, 2014
UK - MPC Split On Rate Decision	Michael Saunders	Aug 20, 2014
UK - CPI and PPI Inflation Both Weaken	Michael Saunders	Aug 19, 2014
UK Economics Weekly		
Scottish Independence Referendum: Less Than A Month To Go	Michael Saunders	Aug 22, 2014
Change in Rate View	Michael Saunders	Aug 15, 2014
IR to Signal Shift in the MPC's Outlook	Michael Saunders	Aug 8, 2014
UK Economics Weekly - Is Sterling Really Over-Valued?	Michael Saunders	Aug 1, 2014
Economy Likely to Outperform Further	Michael Saunders	Jul 11, 2014

Source: Citi Research

Appendix A-1

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