

Global Economic Outlook and Strategy

March 2014



- Our global growth forecasts (at current FX rates) are unchanged this month, at 3.1% for 2014 and 3.4% for 2015, after 2.5% in 2013. Within that, we again trim our aggregate EM growth forecasts, with reductions of two tenths to our 2014 forecast and one tenth to our 2015 forecast. This mainly reflects a large cut to our Russia GDP forecast, prompted by heightened uncertainty and the CBR's recent rate hike. Our forecasts for aggregate advanced economy (AE) growth are again slightly higher this month, and we look for AE growth to pick up from about 1.2% YoY in 2013 to about 2.1% in 2014 and a little higher in 2015. Within that, we make further forecast upgrades for Europe, including the euro area, UK and Sweden, while cutting Japan growth forecasts for the second month in a row. We believe risks to our EM growth forecasts in general remain to the downside, with sluggish world trade growth, domestic EM imbalances, and the prospect of continued Fed tapering.
- The spillovers from the Russia-Ukraine crisis are likely to keep geo-political tensions high nearterm, and probably create additional downside risks for growth in Russia and closely-linked neighbouring countries. Nevertheless, Europe's high reliance on Russia for oil and gas (and Russia's reliance on the revenues from fuel exports to Europe) gives both the EU and Russia an incentive to avoid outright trade sanctions. Imports from Russia account for nearly 20% of total EU energy consumption, and higher shares for both oil and gas consumption. If this link is interrupted, there could be sizable downside economic risks on both sides.
- The major central banks are likely to follow divergent paths. We expect easing from the BoJ, ECB and PBOC in Q2/Q3 in response to softer economic data (especially for China and Japan) and low inflation (especially for the ECB). However, rising capacity use is likely to prompt the BoE to hike rates late this year, with the Fed hiking in H2-2015. By contrast, a range of EM central banks are also likely to hike rates in 2014-15, but in general this reflects pressure to rein in inflation and correct imbalances amidst disappointing growth — and such tightening will probably add to downside EM growth risks.

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With thanks to Jan Maguire

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Figure 1. Currency and Interest Rate Forecasts, as of 26 March 2014

	26 Mar 2014	2Q 14F	3Q 14F	4Q 14F	1Q 15F	2Q 15F	3Q 15F	4Q 15F
United States: Federal Funds	0.25	0.25	0.25	0.25	0.25	0.25	0.75	1.00
10-Yr. Treasuries (Period Ave.)	2.76	2.85	3.10	3.35	3.50	3.60	3.70	3.75
Euro Area: US\$/€	1.38	1.39	1.39	1.40	1.40	1.40	1.40	1.41
Euro Repo Rate	0.25	0.10	0.10	0.10	0.10	0.10	0.10	0.10
10-Yr. Bunds (Period Ave.)	1.64	1.65	1.70	1.80	1.90	1.90	2.00	2.00
Japan: Yen/US\$	102	106	106	107	109	110	112	114
Call Money	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10
10-Yr. JGB (Period Ave.)	0.61	0.55	0.70	0.85	0.95	1.05	1.15	1.10

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

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

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Figure 2. Forecast Highlights and Changes

■ Global	Our aggregate global growth forecasts are unchanged this month, with another EM downgrade balanced by upgrades among some advanced economies, especially in Europe.
■ United States	The harsh winter weather dampened growth at the start of the year, but we expect most of the weakness will be reversed in coming months. Fiscal drag is dissipating and Fed policy is intent on holding down rates. The economy has enough headroom to expand at an above average pace over the forecast horizon, especially with financial conditions providing a significant tailwind. Rate hikes are not expected until mid-2015, with inflation remaining below the Fed's 2% target.
■ Euro Area	We add 0.2ppt and 0.3ppt to our 2014 and 2015 GDP forecasts to 1.3% and 1.6%, respectively. Yet headwinds remain in the form of the persistently strong euro, recent wobbles in EM markets and the risks of further disruption related to Crimea. We expect the ECB to cut its main refi rate to 0.1% in June, and lower its deposit rate to -0.1%, reacting to an extension of very low credit growth, persistently low HICP rates and weak medium term inflation prospects.
■ China	We maintain our 2014 growth forecast at 7.3%, assuming a recovery in global demand, as well as measured policy easing in 2Q when quarterly growth is likely to fall to around 7%YoY. We cut our annual inflation forecast for 2014 from 3.2% to 2.6%, and no longer expect benchmark rate hikes in 2014-15.
■ Japan	We expect the Bank of Japan to decide on additional easing measures in June or July after having seen soft economic data for April (due out in late May), the first month after the consumption tax hike in April.
■ United Kingdom	We are again raising our above-consensus growth forecast for 2014-15, and still expect the MPC to start to hike rates in Q4 this year, and now expect the initial tightening cycle to carry rates up to 2.5% in late 2015 (2.0% previously).
■ Canada	Canadian growth and inflation continue to beat expectations. Hence, we maintain our call for fixed rates and a neutral bias for now. Policy tightening should resume in 3Q 2015.
■ Australia	The risks are now more evenly balanced. Our GDP growth forecast for 2014 is steady this month at 2.9% and we have raised our 2015 forecast to 3.0% (+0.2ppt on last month). This brings the rate hike risk into the back end of 2014 rather than further out into 2015.
■ Emerging Asia (ex China)	Slowing EM growth (esp China) and frigid US weather undermined export-driven growth, though the impact of latter is probably temporary and the former should be cushioned if China eases policy in 2Q, as we expect. Thailand & Vietnam cut rates, and our timetable for Malaysia rate hike has been pushed back. Meanwhile, the Philippines should start tightening policy soon and Indonesia is not done. India and Indonesia are benefiting from election-related optimism but favorable outcomes already seem to be priced in.
■ CEEMEA	Central Europe continues to look like a relative safe-haven in CEEMEA, while a number of other countries are suffering either a) downside risks to growth that result from the need to shrink current account deficits (Turkey, South Africa); or b) downside risks to growth that result from weak macro fundamentals and political risk (Russia).
■ Lat Am	GDP will likely increase by 1.3% in Brazil this year, while some additional monetary tightening (25bps) is likely. In Mexico, lower-than-anticipated growth and contained inflationary pressures should prevent Banxico from hiking interest rates this year. Argentina is going through a period of calm, but the chances that pressures on the FX front re-emerge are not negligible. Social unrest continues in Venezuela and, despite recent announcements, we continue to see output dropping 1% this year and inflation accelerating to 75%.

Source: Citi Research

Figure 3. Selected Countries — Industrial Production Forecasts (Pct.), 2013-15F

	2013F	2014F	2015F
World	2.2%	3.9%	4.1%
United States	2.6	3.2	4.3
Japan	-0.6	5.3	1.2
Euro Area	-0.7	2.0	3.1
United Kingdom	-0.3	1.3	1.5
Canada	1.4	1.2	1.7
China	9.7	8.8	8.5
India	0.7	3.9	5.3
Korea	0.4	5.3	4.2
Brazil	1.2	1.2	2.0

Source: Citi Research

Overview: Russia Strains, Wider EM Worries

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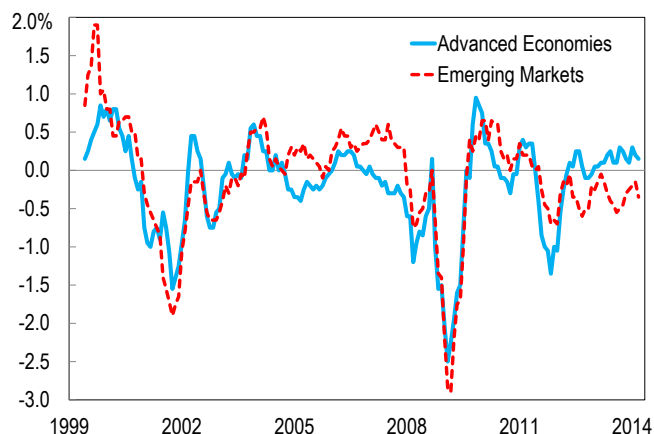
We again cut EM growth forecasts and lift AE forecasts, especially in Europe

We recently cut our Russia growth forecast sharply, and heightened strains probably pose additional downside risks

Our global growth forecasts (at current FX rates) are unchanged this month, at 3.1% for 2014 and 3.4% for 2015, after 2.5% in 2013. Within that, we again trim our aggregate EM growth forecasts, with reductions of two tenths to our 2014 forecast and one tenth to our 2015 forecast. This continues the trend of steady EM forecast downgrades, and in all we have cut our 2014 EM growth forecast by ½% over the last six months and by 1¼% since mid-2011. However, whereas recent EM forecast downgrades generally have been broad-based, this month's revision largely reflects a large cut to our Russia GDP forecast, reflecting heightened uncertainty and the CBR's recent rate hike. Our forecasts for aggregate advanced economy (AE) growth are again slightly higher this month, and we look for AE growth to pick up from about 1.2% YoY in 2013 to about 2.1% in 2014 and a little higher in 2015. Within that, we make further forecast upgrades for the European economies, including the euro area, UK and Sweden, while (for the second month in a row) cutting our Japan growth forecasts.

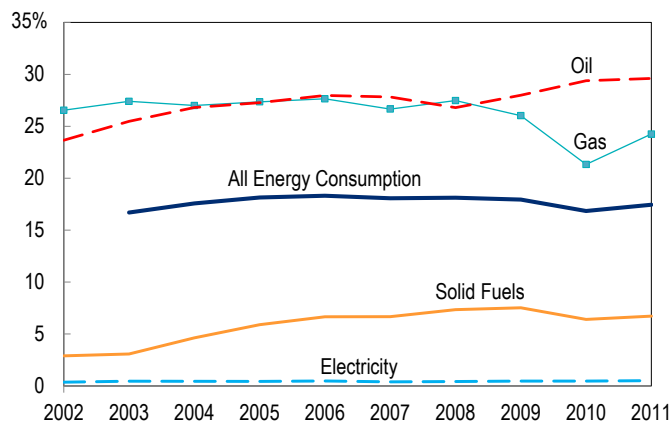
We recently cut our 2014 Russia growth forecast to 1.0% from 2.6%¹, and do not change that forecast further in this publication. Nor have we trimmed forecasts for Russia's neighboring CEE economies. But, we suspect that risks for 2014-15 growth are to the downside, given external sanctions and heightened tensions vis a vis the US and EU². In our view, the sanctions imply new willingness to target individuals linked to Russian President Vladimir Putin and key sectors of the Russian economy. The Russian reaction has been modest so far. The Kremlin has instituted travel bans on a group of nine US Senators and White House officials, while Prime Minister Dmitri Medvedev raised the specter of Ukraine's \$16 billion debt to the Russian gas industry. At this stage, there are only limited signs yet of broader repercussions for Western businesses that operate in Russia (although this may be a factor in the dip in German business confidence readings).

Figure 4. Global — Six-Month Sum of Revisions to Citi GDP Growth Forecasts for Current and Next Year, 1999-2014



Source: Citi Research

Figure 5. EU27 — Imports of Energy Products from Russia as Pct Total Energy Consumption, 2002-11



Note: The chart shows combined imports of oil, gas, solid fuels and electricity identified as sourced from Russia, converted to an equivalent number of tonnes of oil, as a share of total energy consumption, including nuclear, renewables etc. Sources: Eurostat and Citi Research

¹ See "We cut 2014E GDP growth to 1.0% from 2.6% previously", Russia Macro View, Ivan Tchakarov, 10 March 2014, Citi.

² See "Stronger US Sanctions and EU Moves to Strengthen Ties with Kiev: A New Phase in Russia-Ukraine Crisis?", Global Political Insights, Tina Fordham and Matthew Dabrowski, 21 March 2014, Citi.

The Russia-EU energy links play a crucial role for both parties

One factor that may limit the escalation of sanctions for both the EU and Russia is Russia's role as a major energy exporter to EU countries. Imports identified as sourced from Russia account for 17-18% of total energy consumption for the EU as a whole (2011 Eurostat data, in terms of thousands of tonnes of oil equivalent), roughly 30% of EU oil consumption, and 24% of EU gas use. Russia's role in EU energy supply has remained roughly constant in recent years and, allowing for some possible under-recording of fuel products through third countries, may be even greater than Eurostat data show. Among individual EU countries, imports from Russia account for 21% of total energy use in Germany, 18% in Italy, 7% in France and 2% for the UK — but above 25% of energy use in Austria, Bulgaria, the Czech Republic, Finland, Slovakia and Sweden. At the same time, revenues from fuel exports are crucial to Russia's fiscal position³. In our view, neither side can afford for these flows to be severed for any significant period. But we remain alert to risks that the crisis could rapidly move to a more acute phase.

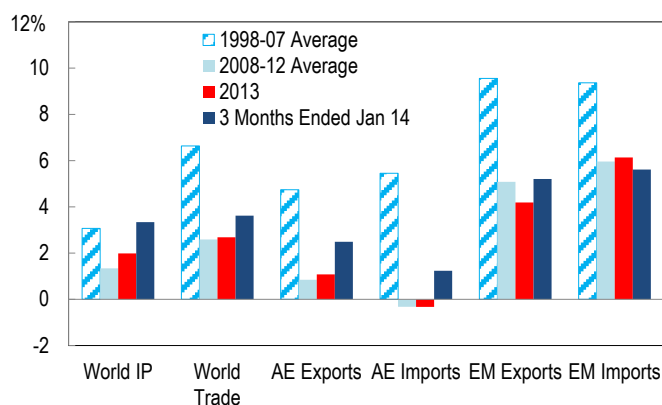
Risks to our EM growth forecasts more broadly probably remain to the downside

More broadly, even after the long series of EM forecast downgrades, we suspect that risks to our growth forecasts lie to the downside in a range of EM countries. This reflects the mix of sluggish world trade growth, still-elevated real exchange rates in some cases, plus less favourable global liquidity and risk premia amidst Fed tapering, as well as the prospect of possible Fed hikes next year.

Despite the pickup in global economic growth, world trade growth remains well below the precrisis norm

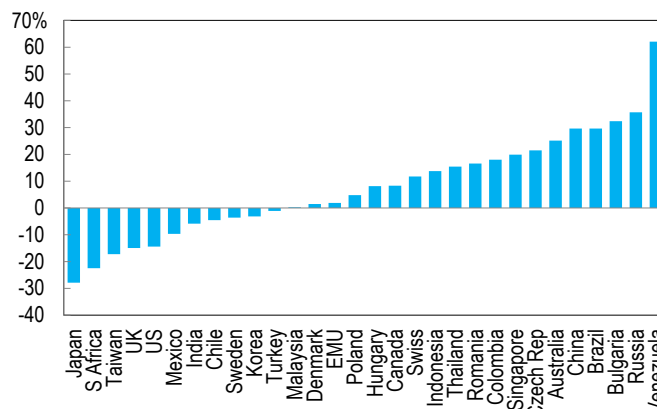
CPB data suggest that even though global IP growth now slightly exceeds the precrisis norm, world trade growth remains modest, at 3.6% YoY in the three months ended January (and 2.9% YoY in Jan-14 alone) — a little above last year's average pace (2.7% YoY) but far below the precrisis norm (1998-07 average was 6.6% YoY). In particular, AE import growth (1.2% YoY in the three months ended Jan-14) remains far below the pre-crisis norm (5.5% YoY over 1998-07), with notable weakness in imports for both the US and euro area. Moreover, the gap between export growth for EM and AE economies has narrowed from 4-5 percentage points in 1997-12 to 2-3 pp at present, with EM export growth no longer outperforming world trade as much as in the precrisis period. Aggregate EM export growth (volume terms) was 5.2% YoY in the three months ended Jan-14, similar to the 2008-12 average (5.1% YoY) and well below the 1998-07 average (9.6% YoY).

Figure 6. Global — World Trade and Industrial Production Growth, YoY, 1998-2014



Sources: CPB and Citi Research

Figure 7. Real Exchange Rates — Deviation from 1998-07 Average, March 2013



Note: Real exchange rates are deflated by CPIs.
Sources: BIS, Datastream and Citi Research

³ The IMF estimates that oil and gas revenues in 2014 will be 9.0% of GDP and 25% of total general government revenues. Source: IMF Article IV Report, October 2013.

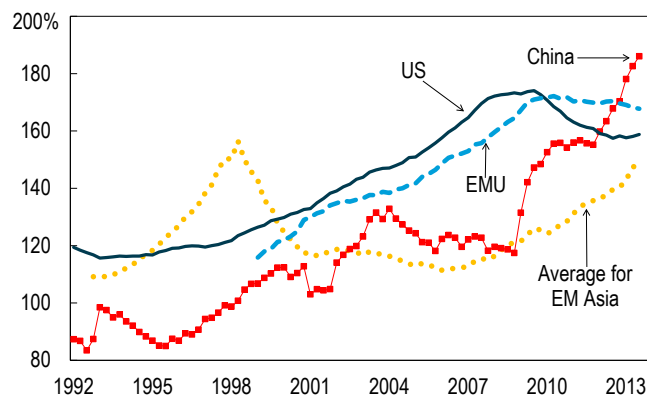
The boost from AE recovery to EM export growth probably will remain relatively modest

Various factors probably lie behind this shift to lower world trade growth and reduced EM export outperformance, including the sluggish growth of AE spending on investment and consumer durables, the trend to software-heavy but hardware-light personal computers, and changes in real exchange rates. Even with significant EM currency depreciation over the last year, the real exchange rates of a range of key EM economies (e.g. China, Indonesia, Russia, Brazil) remain significantly (10%-plus) above the averages of 1998-07, whereas real exchange rates for the US, UK and Japan are well below their precrisis averages. Under these conditions, the boost from AE recovery to export-oriented EMs may well continue to disappoint.

China's economic growth remains highly credit dependent

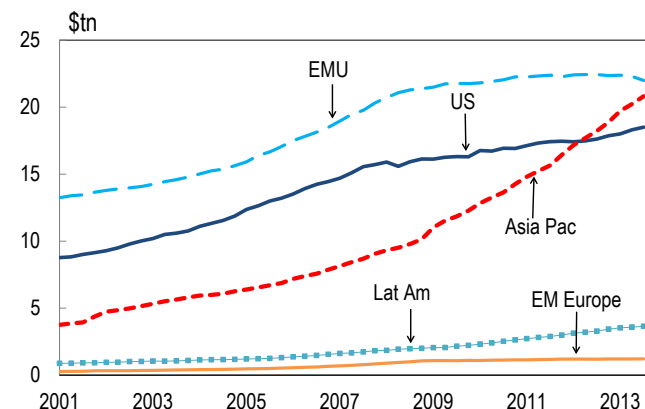
Moreover, we continue to have medium-term worries about the sustainability of China's credit-dependent and investment-intensive growth model (and of wider EM Asia credit trends). The Chinese authorities' use of strong credit growth to maintain high GDP growth in the face of sluggish external demand has lifted private sector debt (combining the gross unconsolidated debts of households and non-financial companies) from 119% of GDP in Q3-08 to 186% of GDP in Q3-13. This ratio now comfortably exceeds the precrisis peaks in the US (174% of GDP in 2009) and euro area (172% of GDP in 2010) although it is still below the peaks in the UK (209% in 2009) and Spain (233% in 2010). In China, the level of total social financing (a broader credit aggregate that also includes lending to non-bank financial companies) exceeds 200% of annual GDP. Prior experience suggests that such rapid debt buildups usually are associated with wasteful resource misallocation (and indeed China's TFP growth was roughly zero last year) plus sizeable potential losses among both lenders and debtors⁴.

Figure 8. Selected Countries — Private Sector Debt as Pct GDP, 1992-2013



Note: We show the gross unconsolidated debts of the household and non-financial corporate sectors as a pct of the 4-quarter average of nominal GDP. EM Asia represented here by HK, Indonesia, Korea, Malaysia, Singapore, Thailand.
Sources: BIS, DataStream and Citi Research

Figure 9. Global — Bank Credit Outstanding to Non-Bank Borrowers, By Borrower Region, USD in Trillions, 2001-13



Note: Data is in trillions of USD, measured at constant end-Q3 2013 exchange rates. Data include domestic credit and cross-border credit. Sources: BIS and Citi Research

There are mixed signals on China's authorities' willingness to rein in the credit boom

There are mixed signals over how far the authorities are willing to cool China's credit boom. On one side, Premier Li Keqiang recently reaffirmed the government 7.5% growth target for 2014, and stressed the primary role of investment spending in stabilizing growth, while the government is aiming for substantial further urbanisation⁵. These commitments probably could only be fulfilled by further inflating

⁴ See, for example, "Reassessing the impact of finance on growth", Cecchetti and Kharroubi, BIS, July 2012.

⁵ See "2014 NPC: Reform in a Growth Context", *China Macro Flash*, 5 March 2014 and "Urbanization Revisited", *China Macro View*, 17 March 2014, Minggao Shen and Shuang Ding, Citi.

We expect the Chinese authorities will react to a further economic slowdown by renewed credit easing

the credit boom. On the other hand, the authorities seem to be aiming to rein in some signs of credit excess, and the monthly flow of new TSF in Jan-Feb dipped by 2.5% from a year ago (bringing TSF growth down from 17.9% YoY in Dec-13 to 17.1% in Feb-14. The authorities' recent willingness to expand the daily FX bands and allow modest FX depreciation also may be aimed at trying to discourage speculative capital inflows (which have helped fuel domestic liquidity)⁶.

With signs that the economy is slowing (we expect China's GDP growth in Q1 to be about 7.3% YoY versus 7.7% YoY in Q4-13)⁷, the authorities are likely to soon face a dilemma over how far to seek to rein in credit growth and credit excesses. If the authorities seek to maintain real GDP growth above 7% YoY (i.e. accepting only a modest undershoot of the growth target), then this is likely to require rapid credit growth, continued resource misallocation, increasing worries over worsening credit quality and inevitable speculative excess. However, if the authorities genuinely seek to rein in credit growth — for example reducing credit growth to match the recent pace of nominal GDP growth at about 10% YoY — then real GDP growth probably will weaken a lot further, putting the 7.5% growth target far out of reach. We suspect that in practice, the authorities will loosen credit policies in Q2, while also fully utilizing the fiscal automatic stabilizer, to stop GDP growth falling below 7%. But if, as seems likely, the credit bubble expands further nearterm, China's potential future economic downside risks will expand. In this context, we shall keep a close eye on FX trends: if the authorities allow significant further nearterm FX depreciation (which is not our base case) then this might be a sign that they are seeking to cushion GDP growth against a much sharper nearterm deflation of the credit bubble.

The BoJ is likely to loosen further as evidence of renewed economic weakness and modest pay growth comes through, whereas growth prospects still seem to be improving in Europe

We are cutting our Japan GDP growth forecast for 2014 to 0.9% from 1.2% in February and 1.6% in January. Pre-emptive purchases ahead of the April consumption tax hike probably will boost Q1 GDP. However, the economy seems to have only limited underlying momentum going into the upcoming fiscal tightening (which we estimate at 1.7% of GDP for FY 2014 and 1.0% of GDP in FY 2015). Moreover, a survey by JTUC-Rengo shows base salaries up by just 0.44% on average across 320 major labour unions, which points to limited pay growth in the spring 2014 wage round⁸. We expect that GDP will fall significantly in Q2 and that the BoJ will ease again around midyear as evidence of weakness comes through. By contrast, growth prospects in Europe still seem to be improving, with a recovery in investment and reasonably solid business surveys⁹. We also slightly mark up our 2014 US growth forecast this month and, with a rebound in some recent indicators, are more confident that the early-2014 weakness was largely temporary and weather-related. As this weather effect fades, we look for a burst of US growth in Q2 and Q3 that will pull the jobless rate down close to 6% by yearend.

Neither the Fed or ECB are likely to respond to EM growth downgrades at this stage

Against this backdrop, we do not at present believe that the downtrend in EM growth forecasts — and continued downside risks — will prompt monetary policy easing from US or EU central banks. Fed tapering is likely to continue at the recent steady pace unless US growth and inflation prospects worsen sharply, although we believe that low inflation will allow the Fed to defer any move to actual tightening until H2-2015. We still lean to a further and final ECB rate cut in June, triggered by a further inflation undershoot versus ECB forecasts. But, with growth picking up, the window for ECB easing may be closing unless new disinflationary shocks emerge.

⁶ See "The Renminbi and Beijing's 'Chi-lemma'", David Lubin, 24 March 2014, Citi.

⁷ See "Official Mfg PMI May Be Stable at 50.2 in Mar", "China Macro Flash: Shuang Ding, Serena Wang and Minggao Shen, 24 March 2014, Citi.

⁸ See "Corporate behavior does not change so easily", *Japan Economics Weekly*, Kiichi Murashima and Naoki Iizuka, 20 March 2014, Citi.

⁹ See "Upside Risks To Q2 GDP", *Euro Economics Weekly*, Guillaume Menuet, 21 March 2014, Citi.

Figure 10. Selected Countries — Economic Forecast Overview (Percent), 2013-2018F

	GDP Growth						CPI Inflation						Short-Term Interest Rates					
	2013F	2014F	2015F	2016F	2017F	2018F	2013	2014F	2015F	2016F	2017F	2018F	2013	2014F	2015F	2016F	2017F	2018F
Global	2.5	3.1	3.4	3.6	3.5	3.4	2.6	2.9	3.1	3.4	3.4	3.4	2.14	2.34	2.52	2.99	3.48	3.63
<i>Based on PPP weights</i>	<i>3.0</i>	<i>3.5</i>	<i>3.8</i>	<i>4.0</i>	<i>4.0</i>	<i>3.9</i>	<i>3.1</i>	<i>3.3</i>	<i>3.5</i>	<i>3.9</i>	<i>3.9</i>	<i>3.9</i>	<i>2.71</i>	<i>2.97</i>	<i>3.20</i>	<i>3.61</i>	<i>4.04</i>	<i>4.02</i>
Industrial Countries	1.2	2.1	2.4	2.4	2.2	2.0	1.3	1.6	1.6	1.5	1.4	1.6	0.46	0.37	0.56	1.16	1.85	2.43
United States	1.9	2.8	3.1	3.2	2.7	2.2	1.1	1.4	1.7	2.2	2.3	2.2	0.25	0.25	0.50	1.65	3.00	3.75
Japan	1.5	0.9	1.0	1.2	1.2	1.0	0.4	2.9	1.6	1.6	0.7	1.0	0.10	0.10	0.10	0.10	0.10	0.50
Euro Area	-0.4	1.3	1.6	1.6	1.7	1.6	1.4	0.7	0.7	1.1	1.2	1.6	0.50	0.16	0.10	0.11	0.42	0.92
Canada	2.0	2.3	2.7	2.7	2.6	2.4	0.9	1.9	1.8	2.0	2.0	2.0	1.00	1.00	1.19	2.13	2.50	2.75
Australia	2.4	2.9	3.0	3.1	3.4	3.3	2.4	3.1	2.5	2.4	2.4	2.4	2.69	2.50	3.44	4.44	4.50	4.75
New Zealand	2.7	3.2	2.7	2.4	2.6	2.7	1.1	2.1	2.2	2.2	2.2	2.4	2.50	3.31	4.38	4.75	4.75	5.00
Germany	0.5	2.2	2.3	2.2	1.9	1.7	1.5	1.4	1.8	2.0	2.2	2.3						
France	0.3	1.0	1.2	1.5	1.7	1.8	1.0	1.1	1.2	1.3	1.3	1.5						
Italy	-1.8	0.6	0.9	0.7	0.7	0.7	1.3	0.3	-0.4	0.1	0.6	1.0						
Spain	-1.2	0.9	1.2	1.5	1.7	1.8	1.5	0.0	0.1	0.3	0.4	0.9						
Greece	-3.9	-0.9	0.8	1.4	1.6	1.6	-0.9	-1.9	-2.2	-1.4	-0.6	0.5						
Ireland	-0.3	1.3	2.9	2.6	2.8	2.8	0.4	0.8	1.0	1.1	1.6	1.7						
Portugal	-1.4	1.5	1.7	1.4	1.5	1.6	0.5	-0.7	-0.8	-0.1	0.4	1.0						
Netherlands	-0.8	1.2	1.3	1.6	1.9	2.0	2.6	0.6	1.2	1.4	1.5	1.8						
Belgium	0.2	1.3	1.4	1.5	1.9	2.1	1.1	0.7	1.0	1.1	1.6	2.0						
Denmark	0.4	1.0	1.5	1.8	1.7	1.9	0.8	1.5	1.7	1.8	1.9	2.0	0.20	0.20	0.25	0.47	0.78	1.00
Norway	2.1	1.9	2.1	2.4	2.8	2.8	2.1	2.0	2.1	2.1	2.2	2.4	1.50	1.50	1.71	2.08	2.74	3.33
Sweden	1.5	2.6	2.7	2.9	2.9	2.7	0.0	0.2	1.3	2.4	2.3	2.0	0.99	0.75	0.98	1.42	2.18	2.80
Switzerland	2.0	1.7	1.9	2.1	2.0	2.0	-0.2	-0.1	0.9	1.1	1.2	1.2	0.00	0.00	0.00	0.00	0.25	1.00
United Kingdom	1.8	3.5	3.6	2.5	2.1	2.3	2.6	1.6	1.8	2.1	2.1	2.0	0.50	0.54	1.67	2.50	2.71	3.21
Emerging Markets	4.5	4.5	4.9	5.3	5.4	5.3	4.7	4.8	5.3	5.1	5.1	4.9	4.78	5.31	5.45	5.66	5.79	5.27
China	7.7	7.3	7.0	7.5	7.3	7.0	2.6	2.6	3.2	3.8	4.0	3.8	3.00	3.00	3.00	3.13	3.50	3.75
Taiwan	2.1	3.2	3.8	4.2	4.5	4.5	0.8	1.3	1.9	1.8	1.8	1.8	1.88	1.88	2.19	2.63	3.13	3.63
India	4.9	5.6	6.2	6.6	6.9	7.0	9.6	8.3	7.5	7.0	6.5	6.5	7.75	8.00	8.00	7.50	7.00	7.00
Indonesia	5.8	5.3	5.5	5.7	5.9	5.7	6.4	6.4	5.7	5.4	5.3	5.5	4.65	5.94	6.44	6.25	6.00	6.00
Korea	3.0	3.7	3.9	4.0	3.6	3.8	1.3	2.1	3.0	3.1	3.0	2.9	2.56	2.50	3.13	3.75	4.13	4.25
Czech Republic	-0.9	1.9	2.5	2.9	2.9	3.2	1.4	0.8	2.0	1.7	2.0	2.0	0.05	0.05	0.08	0.75	1.54	2.54
Hungary	1.1	2.1	1.5	1.4	1.6	2.0	1.7	0.7	2.9	3.0	2.8	2.2	4.38	2.75	3.88	4.00	4.00	4.00
Poland	1.6	3.4	3.6	3.6	3.5	3.2	0.9	1.0	2.7	2.7	2.5	2.5	2.95	2.50	3.15	4.15	4.32	4.00
Romania	3.5	3.0	3.4	3.6	3.6	3.6	4.0	2.4	3.4	2.6	2.5	2.5	4.69	3.50	4.50	5.00	5.00	5.00
Russia	1.3	1.0	2.3	2.5	2.5	2.6	6.8	6.0	5.2	4.9	4.7	4.4	5.50	6.25	5.29	5.13	4.83	4.56
Turkey	4.0	2.3	3.5	3.9	4.1	4.1	7.5	7.7	7.4	6.8	6.5	6.1	6.16	11.05	10.63	9.75	9.50	9.00
Nigeria	6.5	6.6	6.4	6.4	7.0	6.2	8.5	8.8	10.6	10.8	9.9	9.2	11.75	11.75	12.50	11.25	9.00	9.00
South Africa	1.9	2.4	2.8	3.1	3.6	3.6	5.8	6.5	6.1	5.5	6.0	6.0	5.00	6.08	7.00	8.25	8.50	8.50
Argentina	4.9	1.0	1.5	-2.0	3.5	3.0	10.6	NA	30.5	50.0	30.0	20.0	17.16	29.02	34.41	37.00	37.00	0.00
Brazil	2.3	1.3	1.8	2.5	3.0	3.0	6.2	6.1	5.9	5.6	5.5	5.5	8.44	10.92	11.96	11.50	11.00	11.00
Mexico	1.1	3.3	4.0	4.4	4.5	4.6	3.8	4.2	3.6	3.6	3.6	3.6	3.94	3.50	3.94	5.40	6.42	6.75
Venezuela	1.5	-1.0	1.9	1.9	1.9	1.9	38.5	62.5	82.1	60.0	60.0	60.0	14.50	14.50	14.50	14.80	14.80	14.80

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

Source: Citi Research

Figure 11. Selected Countries — Economic Forecast Overview (Percent), 2013-2018F

	Current Balance (Pct of GDP)						Fiscal Balance (Pct of GDP)						Government Debt (Pct of GDP)					
	2013F	2014F	2015F	2016F	2017F	2018F	2013F	2014F	2015F	2016F	2017F	2018F	2013F	2014F	2015F	2016F	2017F	2018F
Global	0.7	0.8	0.6	0.2	0.1	0.0	-3.7	-3.0	-2.5	-2.3	-2.3	-1.9	89	87	87	86	85	84
<i>Based on PPP weights</i>	0.5	0.5	0.3	0.0	-0.2	-0.2	-3.7	-3.1	-2.7	-2.5	-2.5	-2.1	80	81	80	79	78	77
Industrial Countries	-0.1	0.0	0.1	0.0	0.0	0.1	-4.8	-3.5	-2.7	-2.5	-2.3	-2.2	116	114	115	114	114	113
United States	-2.3	-2.0	-1.5	-1.8	-1.7	-1.4	-5.7	-3.9	-3.0	-3.4	-3.4	-3.8	105	107	106	106	106	106
Japan	0.7	0.4	0.3	0.6	0.8	0.8	-9.8	-8.0	-6.2	-5.8	-5.4	-5.0	244	246	251	255	258	260
Euro Area	2.3	2.3	2.1	2.1	1.9	1.8	-2.9	-2.4	-2.0	-1.6	-1.3	-0.9	96	98	98	97	95	94
Canada	-3.2	-2.5	-2.4	-2.0	-1.7	-1.8	-0.9	-0.1	0.3	0.4	0.4	0.4	96	95	93	90	87	85
Australia	-2.9	-2.7	-2.5	-2.4	-2.4	-2.1	-1.2	-3.0	-2.1	-1.4	-1.0	-1.5	30	32	34	33	33	34
New Zealand	-3.4	-4.2	-5.4	-5.0	-5.4	-6.6	-2.9	-1.6	-0.4	0.5	1.2	2.2	40	39	36	37	37	34
Germany	7.4	6.3	5.0	4.5	4.0	3.8	0.0	0.0	0.0	-0.1	0.0	0.1	80	77	75	72	69	67
France	-1.6	-0.9	-0.3	0.2	-0.1	-0.3	-4.1	-3.4	-2.8	-2.4	-1.9	-1.5	94	96	96	96	95	94
Italy	0.8	1.1	1.2	1.3	1.4	1.5	-3.0	-2.9	-2.5	-1.9	-1.6	-1.3	133	138	139	140	139	138
Spain	0.7	0.9	0.9	1.1	1.1	1.3	-7.0	-5.9	-4.7	-3.5	-2.7	-2.0	94	100	103	105	105	105
Greece	0.7	1.8	2.3	2.7	3.1	3.1	-3.7	-3.5	-2.4	-2.0	-1.7	-1.6	176	186	191	193	192	191
Ireland	6.6	9.2	9.6	9.0	8.5	7.8	-7.2	-5.7	-3.3	-2.6	-2.0	-1.3	124	123	123	119	116	112
Portugal	0.4	2.2	2.5	2.6	2.7	2.7	-5.5	-4.1	-3.4	-2.8	-2.4	-2.3	129	135	138	139	139	138
Netherlands	10.4	10.1	9.8	9.5	9.0	8.6	-3.9	-3.4	-2.5	-1.5	-0.2	1.1	75	77	77	76	74	70
Belgium	-1.7	-0.1	0.6	0.8	0.6	0.4	-3.0	-2.5	-1.3	-0.6	-0.1	0.5	102	103	101	99	96	91
Denmark	7.3	6.8	5.8	5.5	5.7	5.6	-1.2	-1.3	-2.4	-1.4	-1.0	-0.9	46	46	47	47	46	45
Norway	10.6	11.2	11.5	11.9	12.2	12.6	11.4	11.9	11.0	10.0	10.0	9.0	NA	NA	NA	NA	NA	NA
Sweden	6.2	5.9	5.6	5.6	5.4	5.3	-1.4	-1.6	-1.0	-0.3	0.5	1.2	39	39	39	37	35	32
Switzerland	12.0	11.0	10.0	10.5	10.5	10.5	0.2	0.5	0.7	1.0	1.1	0.9	48	46	45	45	44	44
United Kingdom	-3.5	-2.8	-3.2	-3.5	-3.2	-2.9	-7.1	-5.4	-3.6	-1.6	-0.7	0.2	94	96	96	94	92	89
Emerging Markets	1.9	1.8	1.3	0.6	0.2	0.0	-2.1	-2.3	-2.3	-2.1	-2.2	-1.5	45	45	45	44	44	43
China	2.0	2.0	1.5	0.8	0.5	0.5	-1.9	-2.1	-2.0	-2.0	-2.0	-2.0	54	54	53	52	51	50
Taiwan	11.7	11.0	10.2	8.0	8.0	8.0	-1.5	-1.4	-0.8	-0.6	-0.6	-0.6	40	40	39	39	39	38
India	-2.0	-2.3	-2.5	-2.2	-2.3	-2.3	-6.9	-6.7	-6.5	-6.2	-5.9	-5.5	70	68	66	65	63	61
Indonesia	-3.3	-2.5	-2.1	-1.7	-1.5	-1.6	-2.2	-2.2	-1.7	-1.9	-2.0	-2.0	24	26	25	25	25	25
Korea	5.4	3.7	3.1	2.3	1.6	0.7	0.8	0.9	1.5	1.7	1.9	1.7	33	31	29	27	26	25
Czech Republic	-1.4	1.1	0.8	0.6	0.5	-0.3	-2.4	-2.9	-2.9	-2.8	-2.5	-2.0	46	46	47	48	48	48
Hungary	2.1	2.6	2.0	1.8	1.5	1.5	-2.6	-2.9	-2.9	-2.9	-3.0	-3.0	79	81	80	79	78	77
Poland	-1.5	-2.5	-3.5	-4.4	-4.6	-4.3	-4.2	5.7	-2.3	-2.2	-2.2	-2.2	54	47	46	45	44	44
Romania	-1.1	-2.5	-4.2	-4.5	-4.5	-4.5	-2.5	-2.3	-2.3	-2.3	-2.3	-2.3	43	42	41	40	39	39
Russia	1.6	1.8	1.2	-0.2	-1.2	-2.2	-2.0	-4.4	-4.9	-0.9	-0.9	-0.9	7	10	13	13	12	12
Turkey	-7.8	-5.2	-5.3	-5.1	-4.1	-3.2	-1.2	-2.8	-3.2	-3.3	-3.3	-3.3	38	38	37	36	35	33
Nigeria	7.0	4.4	2.6	2.1	2.0	1.2	-2.6	-2.9	-2.9	-2.7	-2.5	-2.4	NA	NA	NA	NA	NA	NA
South Africa	-5.8	-5.1	-3.9	-3.4	-3.1	-2.7	-4.3	-4.2	-4.2	-3.7	-3.0	-2.0	46	47	48	49	49	49
Argentina	-0.6	-0.5	-0.4	3.0	1.0	1.0	-2.4	-3.1	-2.3	0.0	-0.5	-1.0	40	48	56	54	53	52
Brazil	-3.7	-4.0	-4.1	-4.1	-4.1	-4.0	-3.3	-3.7	-2.8	-3.1	-3.1	-3.1	57	58	57	58	58	58
Mexico	-1.8	-2.1	-1.8	-1.4	-1.5	-1.5	-2.4	-3.5	-2.5	-2.0	-2.0	-2.0	38	38	38	37	37	37
Venezuela	3.3	4.0	5.1	3.0	3.0	3.0	-11.9	-11.1	-10.3	-12.0	-12.1	-11.5	42	41	40	41	42	43

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

Figure 12. Selected Countries — Changes in Economic Forecasts (Percentage Points), 2013-2015F

	GDP Growth			CPI Inflation			Current Balance (Pct of GDP)			Fiscal Balance (Pct of GDP)		
	2013F	2014F	2015F	2013	2014F	2015F	2013F	2014F	2015F	2013F	2014F	2015F
Global					-0.1							
<i>Based on PPP weights</i>	0.1				-0.1	-0.1						
Industrial Countries		0.1	0.1				0.1	-0.1	-0.1			
United States		0.2			-0.1		-0.1					
Japan	-0.1	-0.3			0.1		0.1	0.2	0.2			
Euro Area		0.2	0.3				0.1	-0.2	-0.5			0.1
Canada	0.2				0.2		0.1					
Australia			0.2		-0.1	0.4	0.1	0.3	0.6			
New Zealand							-0.1					
Germany		0.2	0.2		-0.1	-0.1	0.1		-0.5			
France		0.1	0.1		0.1		-0.1	-0.1	-0.2		0.2	0.3
Italy	0.1	0.3	0.6			-0.1	-0.1	-0.2	-0.4	0.1	-0.1	-0.1
Spain			0.1		0.1	0.1	0.1	0.2	0.2	-0.1	-0.1	-0.1
Greece	-0.2	0.1	0.4		0.4	-0.1		-0.1	-0.1		0.2	0.3
Ireland	-0.4	-0.9	0.6	-0.3			-1.8	0.5	1.8	-0.1	-0.7	-0.4
Portugal			0.5	0.1	-0.1	0.1					0.4	
Netherlands		0.2	0.4		-0.2	-0.1	0.2	0.2	0.9	-0.1		0.3
Belgium		0.1	0.1		-0.2					0.1	0.2	0.3
Denmark		-0.2					0.1	0.1	0.1	-0.5	0.2	
Norway		-0.3	-0.3				-1.3	-1.0	-1.0	0.1	0.1	
Sweden	0.6	0.3			-0.3	-0.5						
Switzerland		-0.3	-0.1		0.1		-0.2	-1.9	-2.7		-0.1	-0.1
United Kingdom	-0.1	0.2	0.4			-0.1	0.2	0.4	0.2	-0.3	0.1	0.6
Emerging Markets		-0.2	-0.1		-0.2	-0.2	-0.1		0.1			-0.1
China					-0.6	-0.5	-0.2			0.1	-0.1	-0.5
Taiwan												
India									-0.3			
Indonesia					-0.1							
Korea	0.2					-0.1	-0.4	-0.4	-0.2	-0.1	-0.1	-0.1
Czech Republic	0.2		0.1		-0.5	-0.3	-0.8	1.1	1.2			
Hungary		0.2			-0.1		0.1	0.1				
Poland					-0.4	-0.1						
Romania	0.1		0.1									
Russia		-1.6	-0.4		0.3	0.3		0.6	0.3		-0.1	
Turkey												
Nigeria										-0.5		
South Africa			-0.1		0.4	0.4		-0.4	0.3	-0.1		0.1
Argentina												
Brazil	0.2				0.1	-0.1		-0.1	-0.3			
Mexico		-0.5			-0.1	-0.1	-0.1	-0.1	-0.1			
Venezuela					-0.7	0.7						

Source: Citi Research

Figure 13. Selected Countries — Economic Forecast Overview and Exchange Rate Forecasts (Percent), 2013-2018F

	10-Year Yields						Exchange Rates Versus U.S. Dollar*						Exchange Rate Versus Euro					
	2013	2014F	2015F	2016F	2017F	2018F	2013	2014F	2015F	2016F	2017F	2018F	2013	2014F	2015F	2016F	2017F	2018F
Industrial Countries																		
United States	2.35	3.00	3.65	3.75	4.10	4.25	NA	NA	NA	NA	NA	NA	1.33	1.39	1.41	1.41	1.41	1.41
Japan	0.71	0.68	1.06	1.25	1.50	1.50	98	106	111	115	115	115	130	147	156	162	162	162
Euro Area	1.60	1.71	1.95	2.20	2.45	2.70	1.33	1.39	1.41	1.41	1.41	1.41	NA	NA	NA	NA	NA	NA
Canada	2.26	2.79	3.53	3.60	3.90	3.90	1.03	1.14	1.15	1.14	1.13	1.11	1.37	1.58	1.62	1.61	1.59	1.57
Australia	3.65	4.45	4.83	5.50	5.50	5.80	0.97	0.91	0.93	0.94	0.94	0.94	1.37	1.52	1.51	1.50	1.50	1.50
New Zealand	3.98	5.04	5.58	5.65	5.80	6.00	0.82	0.86	0.86	0.84	0.80	0.77	1.62	1.61	1.63	1.69	1.76	1.83
Germany	1.60	1.71	1.95	2.20	2.45	2.70												
France	2.12	2.36	2.60	2.85	3.10	3.35												
Italy	4.23	3.49	3.48	3.73	3.98	4.23												
Spain	4.48	3.38	3.35	3.60	3.85	4.10												
Netherlands	1.89	1.99	2.20	2.45	2.70	2.95												
Belgium	2.33	2.43	2.65	2.90	3.15	3.40												
Denmark	1.73	1.78	2.05	2.35	2.70	2.95	NA	NA	NA	NA	NA	NA	NA	NA	NA	NA	NA	NA
Norway	2.57	2.88	2.94	3.05	3.30	3.55	5.88	5.94	5.62	5.40	5.23	5.07	7.81	8.25	7.89	7.61	7.38	7.15
Sweden	2.10	2.44	2.65	2.80	2.95	3.20	6.51	6.37	6.25	6.15	6.00	5.85	8.65	8.85	8.78	8.67	8.46	8.24
Switzerland	0.82	1.01	1.10	1.20	1.40	1.60	0.93	0.89	0.90	0.91	0.91	0.91	1.23	1.24	1.27	1.29	1.29	1.29
United Kingdom	2.34	3.13	3.60	3.75	3.90	4.05	1.56	1.69	1.73	1.74	1.74	1.74	0.85	0.82	0.81	0.81	0.81	0.81
Emerging Markets																		
China	3.68	4.49	4.49	4.61	4.99	5.24	6.15	6.18	6.04	6.01	6.03	6.05	8.17	8.59	8.49	8.47	8.50	8.53
Taiwan	1.46	1.76	2.14	2.50	2.80	3.10	29.68	30.37	29.99	29.58	29.05	28.52	39.43	42.21	42.14	41.71	40.96	40.21
India	8.25	8.50	8.50	8.00	7.50	7.50	58.57	62.59	63.62	61.76	58.70	55.63	77.80	86.98	89.40	87.09	82.76	78.44
Indonesia	6.97	8.48	8.75	8.75	8.75	8.75	10449	11807	12096	11664	10830	9997	13881	16409	16997	16446	15271	14096
Korea	3.00	3.52	4.03	4.30	4.55	4.75	1095	1073	1064	1042	1021	1000	1454	1491	1496	1469	1440	1410
Czech Republic	2.09	2.26	2.50	2.61	2.97	3.20	19.6	19.8	19.3	18.6	18.1	17.5	26.0	27.6	27.1	26.2	25.5	24.7
Hungary	5.92	6.33	6.74	6.50	6.50	6.50	223	232	235	234	234	234	297	322	330	330	330	330
Poland	4.05	4.65	4.97	5.15	4.99	0.48	3.16	3.07	2.97	2.83	2.80	2.78	4.20	4.27	4.17	3.99	3.95	3.92
Romania	NA	NA	NA	NA	NA	NA	3.33	3.27	3.20	3.11	3.06	3.00	4.42	4.54	4.49	4.39	4.32	4.24
Russia	NA	NA	NA	NA	NA	NA	31.9	38.2	38.7	38.0	38.0	38.0	42.3	53.1	54.3	53.6	53.6	53.6
Turkey	NA	NA	NA	NA	NA	NA	1.91	2.34	2.45	2.48	2.43	2.38	2.53	3.25	3.45	3.50	3.43	3.36
Nigeria	NA	NA	NA	NA	NA	NA	159	165	169	171	175	180	212	229	237	241	247	254
South Africa	7.20	7.89	8.04	8.14	8.38	8.77	9.65	11.39	11.60	11.43	11.27	11.10	12.82	15.82	16.29	16.12	15.89	15.65
Argentina	NA	NA	NA	NA	NA	NA	5.45	8.89	11.81	18.62	26.06	27.39	7.24	12.35	16.59	26.25	36.74	38.63
Brazil	9.98	12.84	13.92	12.96	11.75	11.75	2.16	2.53	2.73	2.72	2.53	2.34	2.87	3.51	3.83	3.84	3.57	3.29
Mexico	5.67	6.75	7.38	7.60	7.95	8.00	12.8	13.2	12.9	12.6	12.5	12.4	17.0	18.4	18.1	17.8	17.6	17.5
Venezuela	10.81	14.55	15.54	15.50	15.50	15.50	5.99	10.58	19.80	31.28	49.43	78.10	7.96	14.70	27.82	44.11	69.69	110.12

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

Figure 14. Short Rates (End of Period), as of 26 March 2014 (Percent)

	Current	2Q 14	3Q 14	4Q 14	1Q 15	2Q 15	3Q 15	4Q 15
United States	0.25	0.25	0.25	0.25	0.25	0.25	0.75	1.00
Japan	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10
Euro Area	0.25	0.10	0.10	0.10	0.10	0.10	0.10	0.10
Canada	1.00	1.00	1.00	1.00	1.00	1.00	1.25	1.50
Australia	2.50	2.50	2.50	2.50	2.75	3.25	3.75	4.00
New Zealand	2.75	3.25	3.50	3.75	4.00	4.25	4.50	4.75
Denmark	0.20	0.20	0.20	0.20	0.20	0.20	0.20	0.20
Norway	1.50	1.50	1.50	1.50	1.50	1.75	1.75	2.00
Sweden	0.75	0.75	0.75	0.75	0.75	1.00	1.00	1.25
Switzerland	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00
United Kingdom	0.50	0.50	0.50	0.75	1.25	1.50	2.00	2.50
China	3.00	3.00	3.00	3.00	3.00	3.00	3.00	3.00

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

Figure 15. 10-Year Yield Forecasts (Period Average), as of 26 March 2014 (Percent)

	Current	2Q 14	3Q 14	4Q 14	1Q 15	2Q 15	3Q 15	4Q 15
United States	2.76	2.85	3.10	3.35	3.50	3.60	3.70	3.75
Japan	0.61	0.55	0.70	0.85	0.95	1.05	1.15	1.10
Euro Area (Germany)	1.64	1.65	1.70	1.80	1.90	1.90	2.00	2.00
Canada	2.50	2.60	2.90	3.15	3.40	3.50	3.55	3.65
Australia	4.18	4.40	4.50	4.60	4.70	4.75	4.95	4.95
New Zealand	4.57	4.90	5.10	5.40	5.50	5.60	5.60	5.60
Denmark	1.59	1.70	1.77	1.90	2.00	2.00	2.10	2.10
Norway	2.90	2.85	2.85	2.95	3.00	2.90	2.95	2.90
Sweden	2.12	2.35	2.45	2.55	2.65	2.60	2.70	2.65
Switzerland	0.92	1.00	1.00	1.05	1.10	1.10	1.10	1.10
United Kingdom	2.76	3.00	3.25	3.40	3.50	3.55	3.65	3.70

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 Research

Figure 16. 10-Year Yield Spreads (Period Average), as of 26 March 2014

		Spread vs. US\$					Spread vs. Germany					
	Current	2Q 14	3Q 14	4Q 14	1Q 15	2Q 15	Current	2Q 14	3Q 14	4Q 14	1Q 15	2Q 15
United States	NA	NA	NA	NA	NA	NA	114	122	142	158	163	173
Japan	-217	-232	-242	-253	-258	-258	-103	-110	-100	-95	-95	-85
Euro Area	-114	-122	-142	-158	-163	-173	NA	NA	NA	NA	NA	NA
Canada	-26	-25	-20	-20	-10	-10	88	97	122	137	153	163
Australia	144	158	143	127	122	117	258	280	285	285	286	291
New Zealand	184	209	204	209	205	205	298	331	347	367	368	378
France	65	-57	-77	-93	-98	-108	52	65	65	65	65	65
Italy	65	58	28	2	-3	-23	177	180	170	160	160	150
Spain	57	53	18	-18	-23	-33	169	175	160	140	140	140
Netherlands	-82	-97	-117	-133	-138	-148	30	25	25	25	25	25
Belgium	-54	-47	-72	-88	-93	-103	58	75	70	70	70	70
Austria	-93	-92	-112	-128	-133	-143	19	30	30	30	30	30
Finland	-88	-97	-117	-133	-138	-148	24	25	25	25	25	25
Ireland	29	18	-22	-48	-63	-73	141	140	120	110	100	100
Portugal	140	138	103	72	57	37	252	260	245	230	220	210
Denmark	-117	-115	-132	-148	-153	-163	5	5	7	10	10	10
Norway	14	-7	-27	-48	-63	-78	126	120	115	115	110	100
Sweden	-64	-47	-67	-83	-93	-103	48	70	75	75	75	70
Switzerland	-184	-187	-212	-233	-243	-253	-72	-65	-70	-75	-80	-80
United Kingdom	0	15	15	5	0	-5	112	137	158	163	163	168

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 Research

Figure 17. Emerging Market Countries — Short Rates Actual and Forecast of Additional Rate Moves (End of Period), as of 26 March 2014

Country	Current Rate (%)	Jun 14	Sep 14	Dec 14	Mar 15	Jun 15	Total Cumulative Rate Moves Expected
South Africa	5.50	50	50	0	0	50	150
Hungary	2.60	-10	0	50	75	25	140
Brazil	10.75	25	0	0	100	0	125
Philippines	3.50	0	25	25	25	25	100
Indonesia	5.75	25	0	0	25	25	75
Malaysia	3.00	0	50	0	0	0	50
Korea	2.50	0	0	0	25	25	50
Thailand	2.00	0	0	0	25	25	50
Poland	2.50	0	0	0	50	0	50
Peru	4.00	0	0	0	50	0	50
Mexico	3.50	0	0	0	0	25	25
Israel	0.75	-25	0	75	-25	0	25
Turkey	10.26	74	50	0	-50	-50	24
Chile	4.00	0	0	0	0	0	0
India	8.00	0	0	0	0	0	0
China	3.00	0	0	0	0	0	0
Russia	7.00	-50	-50	-50	-25	0	-175

Note: For Turkey we use the average funding rate of the CBT instead of the 1-week repo rate. Source: Citi Research

Figure 18. Foreign Exchange Forecasts (End of Period), as of 26 March 2014

	vs. USD							vs. EUR						
	Current	Jun 14	Sep 14	Dec 14	Mar 15	Jun 15	Sep 15	Current	Jun 14	Sep 14	Dec 14	Mar 15	Jun 15	Sep 15
United States	NA	NA	NA	NA	NA	NA	NA	1.38	1.39	1.39	1.40	1.40	1.40	1.41
Japan	102	106	106	107	109	110	112	141	146	148	150	152	155	157
Euro Area	1.38	1.39	1.39	1.40	1.40	1.40	1.41	NA	NA	NA	NA	NA	NA	NA
Canada	1.13	1.14	1.14	1.15	1.15	1.15	1.15	1.55	1.57	1.59	1.61	1.61	1.61	1.62
Australia	0.91	0.91	0.92	0.92	0.92	0.93	0.93	1.52	1.52	1.52	1.52	1.52	1.51	1.51
New Zealand	0.86	0.86	0.87	0.87	0.87	0.86	0.86	1.61	1.61	1.61	1.61	1.62	1.63	1.64
Norway	6.08	6.00	5.89	5.78	5.71	5.65	5.58	8.39	8.31	8.20	8.09	8.01	7.93	7.85
Sweden	6.42	6.40	6.34	6.28	6.27	6.25	6.24	8.86	8.87	8.83	8.80	8.79	8.78	8.77
Switzerland	0.88	0.89	0.89	0.89	0.90	0.90	0.91	1.22	1.24	1.24	1.25	1.26	1.27	1.27
United Kingdom	1.65	1.68	1.71	1.73	1.73	1.73	1.74	0.84	0.82	0.82	0.81	0.81	0.81	0.81
China	6.23	6.24	6.15	6.08	6.06	6.05	6.03	8.6	8.6	8.6	8.5	8.5	8.5	8.5
India	60.9	61.9	63.2	64.3	64.0	63.8	63.5	84.0	85.8	88.0	90.0	89.8	89.5	89.3
Korea	1080	1066	1073	1079	1073	1067	1061	1490	1477	1495	1511	1505	1499	1493
Poland	3.04	3.06	3.09	3.10	3.05	2.99	2.94	4.20	4.24	4.30	4.34	4.27	4.20	4.13
Russia	36.3	38.1	38.8	39.4	39.1	38.8	38.5	50.0	52.8	54.1	55.1	54.8	54.5	54.2
South Africa	10.86	11.34	11.53	11.70	11.66	11.62	11.58	14.98	15.72	16.07	16.38	16.34	16.31	16.28
Turkey	2.24	2.33	2.37	2.40	2.42	2.44	2.46	3.09	3.23	3.30	3.36	3.40	3.43	3.46
Brazil	2.33	2.51	2.58	2.65	2.68	2.71	2.74	3.21	3.47	3.60	3.72	3.76	3.81	3.86
Mexico	13.2	13.3	13.2	13.1	13.0	12.9	12.9	18.3	18.4	18.4	18.3	18.2	18.2	18.1

Source: Citi Research

Figure 19. Foreign Exchange Forecasts (End of Period), as of 26 March 2014

	vs. JPY						
	Current	Jun 14	Sep 14	Dec 14	Mar 15	Jun 15	Sep 15
United States	102	106	106	107	109	110	112
Japan	NA	NA	NA	NA	NA	NA	NA
Euro Area	141	146	148	150	152	155	157
Canada	91	93	93	93	95	96	97
Australia	93	96	97	99	101	102	104
New Zealand	87.5	91.1	92.1	93.2	94.1	95.1	96.0
Norway	16.8	17.6	18.1	18.5	19.0	19.5	20.1
Sweden	15.9	16.5	16.8	17.1	17.4	17.7	18.0
Switzerland	116	118	119	120	121	122	124
United Kingdom	169	178	181	185	188	191	194
China	16	17	17	18	18	18	19
India	1.68	1.70	1.68	1.67	1.70	1.73	1.76
Korea	10.56	10.09	10.09	10.07	9.87	9.67	9.48
Poland	33.6	34.5	34.5	34.6	35.7	36.9	38.1
Russia	2.8	2.8	2.7	2.7	2.8	2.8	2.9
South Africa	9.4	9.3	9.2	9.2	9.3	9.5	9.7
Turkey	45.7	45.3	44.9	44.6	44.9	45.2	45.5
Brazil	43.9	42.1	41.2	40.4	40.5	40.7	40.8
Mexico	7.7	7.9	8.1	8.2	8.4	8.5	8.7

Source: Citi Research

Country Commentary

United States

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Harsh winter weather dampened growth in the first quarter. Employment, housing, and discretionary spending have been hardest hit. We think most, but not all, of this lost activity will be made up quickly, leading to a burst of growth in the spring and summer. Some indicators, such as industrial production already are showing a return to normal, but most data remain depressed. The rebound in growth will continue to drive down the unemployment rate toward 6% this year. The economy has key supports from ample slack and a strong financial tailwind.

The Fed continues to shift policy accommodation away from asset purchases and toward anchoring forward rates. The Fed cut QE by \$10 billion for the third time, setting the bar extremely high for changing that pace of taper. Also, the Fed ended its reliance on quantitative forward guidance. Unfortunately, policymakers have struggled to communicate that these changes are not intended to signal an earlier exit from near-zero policy rates. We continue to expect preparations for rate hikes in the spring of 2015, with modest tightening beginning in the summer. We see two-way risks here: continued low inflation could delay tightening, while a faster recovery and wage gains could speed up exit.

The commitment to the current low policy rate was made contingent on inflation, suggesting that the outlook for inflation has gained in importance. Inflation recently has been well below the Fed's medium-term goal of 2%. Tradable goods prices actually have declined in the past year, reflecting the global slowdown. Inflation is likely to edge up over time, underpinned by domestic demand, tightening labor markets and an eventual pickup in global growth.

Figure 20. United States — Economic Forecasts, 2013-2015F

					2013	2014				2015		
		2013F	2014F	2015F	4QF	1QF	2QF	3QF	4QF	1QF	2QF	3QF
GDP	SAAR				2.8%	1.2%	3.5%	3.4%	3.1%	3.2%	2.8%	3.2%
	YoY	1.9	2.8	3.1	2.6	2.6	2.9	2.7	2.8	3.3	3.1	3.1
Domestic Demand	SAAR				1.5	2.1	3.4	3.6	3.0	3.0	2.9	3.0
	YoY	1.5	2.5	3.1	1.6	2.0	2.3	2.6	3.0	3.2	3.1	3.0
Consumption	SAAR				2.9	2.2	3.4	3.4	3.0	3.0	3.0	3.1
	YoY	2.0	2.7	3.1	2.2	2.2	2.6	3.0	3.0	3.2	3.1	3.0
Business Investment	SAAR				6.9	1.6	6.1	6.6	5.5	4.9	4.2	4.4
	YoY	2.8	4.9	5.1	2.9	4.5	4.8	5.3	4.9	5.8	5.3	4.8
Housing Investment	SAAR				-8.5	0.9	9.4	16.1	10.6	11.2	11.2	12.2
	YoY	12.1	4.9	11.9	6.7	3.8	2.7	4.1	9.1	11.8	12.2	11.3
Government	SAAR				-5.2	2.3	0.6	0.1	0.0	0.1	0.1	0.0
	YoY	-2.2	-0.3	0.1	-2.4	-0.8	-0.5	-0.6	0.7	0.2	0.1	0.0
Exports	SAAR				9.5	0.2	6.5	5.0	4.7	4.9	5.0	5.5
	YoY	2.7	4.9	5.1	4.9	5.3	5.0	5.3	4.1	5.3	4.9	5.0
Imports	SAAR				1.5	0.9	2.5	3.6	4.6	5.2	5.3	5.1
	YoY	1.4	2.4	4.7	2.8	2.9	1.8	2.1	2.9	4.0	4.7	5.1
PCE Deflator	YoY	1.1	1.4	1.7	1.0	1.1	1.5	1.5	1.7	1.7	1.7	1.7
Core PCE Deflator	YoY	1.2	1.5	1.8	1.2	1.2	1.5	1.6	1.7	1.8	1.8	1.8
Unemployment Rate	%	7.4	6.4	5.9	7.0	6.6	6.5	6.2	6.1	6.0	6.0	5.9
Federal Gov't Balance (Fiscal Year)	\$Bn	-680	-500	-450								
	% of GDP	-4.1	-2.9	-2.5								
General Gov't Balance (Cal Year)	% of GDP	-5.7	-3.9	-3.0								
Federal Debt	% of GDP	72	73	73								
General Gov't Debt	% of GDP	105	107	106								
Current Account	US\$b	-379	-349	-280	-324	-370	-354	-343	-330	-307	-288	-271
	% of GDP	-2.3	-2.0	-1.5	-1.9	-2.1	-2.0	-1.9	-1.8	-1.7	-1.6	-1.5
S&P 500 Profits (US\$ Per Share)	YoY	6.1	6.7	7.2	7.4	6.1	6.2	6.1	8.5	NA	NA	NA

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

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We revise down our GDP growth forecast for 2014 from 1.2% as of February to 0.9% this month, mostly reflecting weaker-than-expected net exports. Despite the earlier yen depreciation, export volumes remain range-bound, probably due to virtually flat growth in Asia and companies' tendency to deal with rises in overseas demand by increasing foreign production rather than exports from Japan. Meanwhile, despite the Abe Administration's strong prompting, the hike in base salaries in the spring wage negotiations was modest even at large firms whose business conditions are relatively favorable, suggesting that companies remain cautious about increasing fixed compensation. We expect the consumption tax hike in April will erode badly the real purchasing power of household nominal income.

Core inflation continued to surprise to the upside in 2013. In our view, the main reason for this surprise is the significantly higher sensitivity of the core CPI to the yen/dollar rate. Japan's dependence on imports ("import penetration") has risen substantially over time. But it also indicates that if the yen stabilises at a certain level, core inflation will start tailing off again in the future. In addition, the output gap is likely to widen after the consumption tax hike and this will probably reduce pricing power of the corporate sector. We currently expect core inflation to peak around April and to fall gradually in the second half of this year.

With this backdrop, we expect the BoJ to decide on additional easing measures in June or July. A number of economic data which will reflect economic activity after the consumption tax hike are slated for release in late May. If the BoJ wants to see them before acting, the earliest timing would be the June meeting (a policy meeting in May will be held on 20–21, before the data announcements). We expect the BoJ to increase monthly JGB purchases by around 2 trillion yen and annual ETF purchases (currently 1 trillion yen) by 2-3 trillion yen.

Figure 21. Japan — Economic Forecasts, 2013-2015F

					2013	2014				2015		
		2013F	2014F	2015F	4QF	1QF	2QF	3QF	4QF	1QF	2QF	3QF
Real GDP	YoY	1.5%	0.9%	1.0%	2.5%	2.1%	0.3%	0.6%	0.8%	0.1%	1.3%	1.9%
	SAAR				0.7	2.8	-3.3	2.3	1.5	-0.1	1.6	4.7
Domestic Demand	YoY	1.8	1.0	0.7	2.9	3.0	0.6	0.4	0.1	-0.6	1.4	1.7
	SAAR				2.7	3.0	-5.7	1.7	1.5	0.3	2.1	3.0
Private Consumption	YoY	1.9	0.2	0.5	2.3	2.6	-0.7	-0.6	-0.6	-1.9	1.5	2.3
	SAAR	-	-	-	1.6	5.5	-10.0	1.2	1.6	0.1	3.1	4.4
Business Investment	YoY	-1.5	4.0	4.2	0.9	3.6	3.2	4.2	4.9	4.2	4.5	4.5
	SAAR				3.0	7.0	2.4	4.3	5.8	4.2	3.8	4.3
Housing Investment	YoY	8.8	-0.3	1.7	10.4	7.9	0.9	-3.4	-6.0	-2.7	5.2	5.5
Public Investment	YoY	11.6	2.9	-8.7	20.6	12.5	6.9	0.0	-6.0	-6.5	-9.5	-10.5
Exports	YoY	1.6	3.2	4.4	6.9	3.2	1.6	3.7	4.5	4.8	4.3	4.5
	SAAR				1.7	2.2	5.4	5.6	4.8	3.4	3.3	6.6
Imports	YoY	3.3	3.7	2.7	9.1	8.9	4.0	2.1	0.0	0.6	5.2	3.6
	SAAR				14.7	3.9	-10.7	2.1	5.6	6.4	6.6	-4.0
CPI	YoY	0.4	2.9	1.6	1.4	1.6	3.7	3.2	3.0	2.8	0.8	0.8
Core CPI	YoY	0.4	2.7	1.6	1.1	1.3	3.3	3.1	3.0	2.8	0.8	0.8
Nominal GDP	YoY	1.0	2.4	1.4	0.4	0.9	0.6	0.4	0.7	0.0	0.4	0.6
Current Account	¥ tn	3.4	2.1	1.3	0.2	0.0	3.1	3.1	2.2	1.2	-0.2	1.7
	% of GDP	0.7	0.4	0.3	0.0	0.0	0.6	0.6	0.5	0.2	0.0	0.3
Unemployment Rate	%	4.0	3.7	3.6	3.9	3.7	3.7	3.8	3.7	3.6	3.6	3.7
Industrial Production	YoY	-0.6	5.3	1.2	5.7	8.3	5.8	4.3	3.0	0.2	1.6	2.0
Corporate Profits (Fiscal Year)	YoY	45.0	10.0	12.5								
General Govt. Balance (Fiscal Year)	% of GDP	-9.8	-8.0	-6.2								
General Govt Debt	% of GDP	244	246	251								

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

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Euro Area

The euro area is enjoying a modest recovery but the persistently strong euro, together with recent wobbles in emerging markets and the risks of further disruption related to the situation in Crimea, suggest that headwinds remain. Nevertheless, surveys confirm that private sector sentiment is improving and, together with signs of reduced financial fragmentation and a pickup in retail sales, we expect GDP growth to pick up from 0.3% QQ in 4Q-13 to 0.4% QQ in 1Q-14. Our survey based model suggests there are **upside risks to Q2 GDP**. As a result, we add 0.2pp to our 2014 and 0.3pp to 2015 GDP forecasts to 1.3% and 1.6%, respectively, expecting **the increase in equipment investment to be quite broad-based** across Eurozone countries in the next 1-2 years. We turn more constructive about Germany, Italy and Spain in 2014-15, but still expect France to underperform its largest neighbours.

Some progress has been achieved with respect to banking union in recent months. In particular, the ECB presented details of 'Phase 2' of its Asset Quality Review (AQR), with some of the next steps to include until late March "*bare minimum reviews*" of key drivers of balance sheet valuations. In addition, there have been agreements between member states and the European parliament about the Single Resolution Mechanism (SRM) and the Resolution fund. Full pooling of the fund will be achieved after 8 years and the decision-making process of the SRM was streamlined, reducing the involvement of the EU Council and the plenary of the Resolution board. While the compromise appears to constitute progress relative to the original proposal by the EU Council, concerns remain regarding its ability to take resolution decisions efficiently and to have the necessary resolution resources.

In the meantime, inflation remains muted, while the output gap is large. We see risks of a lower headline inflation print of 0.6% YoY in March, which would put pressure on the ECB to discuss cutting rates as early as the April meeting. We suspect that a decision to cut, while possible next month, is more likely to be taken later in the second quarter when the Governing Council reviews another set of staff projections confirming that the medium-term price inflation target is unlikely to be met, and possibly more evidence of a drift lower in long-term inflation expectations.

Figure 22. Euro Area — Economic Forecasts, 2013-2015F

		2013F	2014F	2015F	2013	2014				2015		
					4QF	1QF	2QF	3QF	4QF	1QF	2QF	3QF
Real GDP	YoY	-0.4%	1.3%	1.6%	0.5%	1.1%	1.2%	1.4%	1.6%	1.6%	1.6%	1.5%
	SAAR				1.1	1.5	1.7	1.4	1.7	1.5	1.6	1.4
Final Domestic Demand	YoY	-0.7	1.0	1.4	0.3	0.8	1.0	1.0	1.2	1.3	1.3	1.4
Private Consumption	YoY	-0.5	0.9	1.4	0.3	0.6	0.8	0.9	1.1	1.3	1.3	1.4
Government Consumption	YoY	0.3	0.3	0.3	0.4	0.2	0.3	0.1	0.5	0.5	0.4	0.3
Fixed Investment	YoY	-2.8	2.3	2.6	0.1	2.2	2.5	2.5	2.0	2.4	2.6	2.7
Business Equipment	YoY	-1.7	3.2	3.2	1.5	3.1	3.2	3.6	2.8	3.4	3.2	3.2
Construction	YoY	-3.7	1.5	2.3	-1.4	0.9	1.7	1.5	1.8	2.1	2.3	2.5
Stocks (Contrib. to Y/Y GDP Growth)		-0.2	0.2	0.2	-0.2	0.0	0.3	0.1	0.5	0.4	0.3	0.2
Exports	YoY	1.3	3.0	3.2	2.6	4.1	2.4	3.0	2.4	2.8	3.0	3.3
Imports	YoY	0.1	2.9	3.5	1.9	3.8	2.8	2.5	2.8	3.2	3.4	3.6
CPI	YoY	1.4	0.7	0.7	0.8	0.7	0.9	0.6	0.8	0.8	0.7	0.7
CPI Ex Unprocessed Food & Energy	YoY	1.3	0.9	0.5	1.0	1.0	1.0	0.8	0.7	0.6	0.5	0.5
Unemployment Rate	YoY	12.1	11.8	11.3	12.0	12.0	11.9	11.7	11.7	11.6	11.4	11.2
Current Account Balance	EUR bn	221.4	225.8	214.0								
	% of GDP	2.3	2.3	2.1								
General Government Balance	EUR bn	-279.9	-239.1	-197.6								
	% of GDP	-2.9	-2.4	-2.0								
Primary Balance	% of GDP	0.1	0.6	1.1								
General Government Debt	EUR bn	9,222.1	9,558.9	9,736.5								
	% of GDP	96.3	97.8	97.5								
Gross Operating Surplus	YoY	1.5	3.3	3.0								

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

Germany

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We are raising our growth forecasts for 2014 and 2015 to 2.2% and 2.3%, respectively (from 2.0% and 2.1%), with upward revisions also in later years. Growth has probably been very strong in Q1 (we expect 0.7%QQ, and it could be even higher), reflecting mild weather, a likely rebound in inventories and pickup in private consumption. For later years, we expect that supportive financing conditions will provide an ongoing boost to consumer spending and investment. However, there are also some downside risks for German growth, if EM weakness intensifies or tensions with Russia-related tensions escalate (which are not our base case).

France

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The French government faces a crucial few weeks: i) municipal elections on 23/30 March; (ii) the need to provide details of Responsibility Pact proposals on the arbitrage between lower labour charges and more jobs, iii) details of the €50bn of expenditure savings to be made over 2015-17 as part of the Stability Programme (15 April), iv) conclusions from the fiscal reform debates, v) draft law on decentralisation/regionalisation, and vi) confidence vote in parliament in the second half of April. A change of PM is probably not currently imminent, barring disastrous municipal election results. We lift our 2014 and 2015 GDP forecasts only modestly, up 0.1pp to 1.0% and 1.2%, respectively, still **underperforming its peers** noticeably.

Italy

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We are lifting our 2014-2015 GDP growth forecasts, assuming that the recently-announced tax cuts (0.8% of GDP) will support consumer spending and business investment. Spending cuts are smaller, fuzzier and likely to be delayed. The fiscal deficit will probably stay around 3% of GDP for the third consecutive year, despite the cyclical revenues recovery. Moreover, given Italy's underperformance within the euro area, scope for a cyclical upswing from pent-up demand is probably quite large. Inflation is likely to fall further due to ample slack and the strong euro. Medium-term GDP growth prospects remain poor, as the necessary supply-side reforms are not yet on the table. This implies the debt-to-GDP ratio is likely to stabilize only towards the end of our forecast horizon, at around 140%.

Figure 23. Germany, France and Italy — Economic Forecasts, 2013-15F

		Germany			France			Italy		
		2013F	2014F	2015F	2013F	2014F	2015F	2013F	2014F	2015F
Real GDP	YoY	0.5%	2.2%	2.3%	0.3%	1.0%	1.2%	-1.8%	0.6%	0.9%
Final Domestic Demand	YoY	0.7	2.2	2.6	0.3	0.7	0.7	-2.6	0.4	0.9
Private Consumption	YoY	1.0	1.6	2.4	0.4	0.7	0.8	-2.6	0.3	1.0
Government Consumption	YoY	0.7	1.2	1.5	1.7	0.8	0.1	-0.8	-0.5	-0.8
Fixed Investment	YoY	-0.6	5.1	4.4	-2.1	0.6	1.3	-4.6	2.2	3.0
Exports	YoY	1.0	3.7	3.3	0.6	2.0	2.6	0.0	2.8	2.2
Imports	YoY	1.0	4.2	5.3	0.8	1.7	1.5	-2.9	1.6	2.4
CPI	YoY	1.5	1.4	1.8	1.0	1.1	1.2	1.3	0.3	-0.4
Unemployment Rate	%	5.3	5.0	4.7	9.9	9.8	9.5	12.2	12.6	12.3
Current Account	€bn	201.7	174.7	144.1	-33.9	-19.7	-6.5	12.1	16.8	18.7
	% of GDP	7.4	6.3	5.0	-1.6	-0.9	-0.3	0.8	1.1	1.2
General Govt. Balance	€bn	-0.5	1.2	-1.2	-84.3	-71.6	-59.4	-46.4	-46.1	-39.3
	% of GDP	0.0	0.0	0.0	-4.1	-3.4	-2.8	-3.0	-2.9	-2.5
Primary Balance	% of GDP	2.4	2.3	2.1	-1.5	-0.8	-0.1	2.3	2.1	2.4
General Govt. Debt	% of GDP	79.5	77.4	74.7	93.7	95.6	96.3	132.6	137.7	138.7
Gross Trading Profits	YoY	2.4	5.4	5.0	1.1	3.4	3.2	NA	NA	NA

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

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Spain

We keep our forecast for 2014 real GDP at 0.9% but raise 2015 by 0.1pp to 1.2% to reflect stronger domestic demand (due to neutral fiscal policy) and robust exports. Buoyant survey data, gains in registered employees, and a pick-up in retail sales suggest the economic recovery is maintaining momentum in Q1 14. Inflation is likely to fall further, while the fiscal deficit will probably remain slightly above target.

Greece

We expect GDP growth to turn positive only in late 2014, against official forecasts of +0.6% for 2014 GDP. We have lifted our 2015 GDP growth forecast to 0.8% from 0.4%, assuming that the government will use some of the primary surplus to retain political support. But private sector liquidity remains poor, the household saving rate is highly negative and export growth lags periphery peers. Deflation is likely to persist, amid newly agreed reforms to enhance internal competition. Further debt relief on official loans is likely in coming quarters, but probably will fall short of an outright debt write-off. The public debt ratio is likely to rise further in coming years.

Ireland

We are pulling this year's GDP growth forecast down to 1.3% from 2.2% last month following the weak Q4 GDP data (down 2.3% QoQ). However, Ireland's GDP data are often volatile from quarter to quarter, and the Q4 slide followed strong gains of 1.1% and 2.1% QoQ in Q2 and Q3 of 2013 respectively. Trends in business surveys and employment (up 3.2% YoY) suggest that the economy's underlying momentum is improving and we expect growth of about 0.7% QoQ in Q1. The planned rundown of the government's cash reserves should allow the general government debt/GDP ratio to fall slightly this year, although the debt ratio will only fall further in coming years if there is a sustained pickup in real and nominal GDP growth.

Portugal

We retain our forecast of improving GDP growth in 2014-2015, helped by ongoing export gains, earlier-than-expected employment gains and a further reduction in the fiscal drag. With 2013 fiscal targets outperformed, we assume some planned spending cuts will not be adopted. Inflation will likely fall further, reflected in low nominal GDP growth, hence keeping the public debt-to-GDP ratio rising slightly in the next couple of years. We expect a "clean exit" from the bailout programme in May, as political costs of a precautionary credit line likely outweigh its benefits.

Figure 24. Spain, Greece, Ireland and Portugal — Economic Forecasts, 2013-15F

		Spain			Greece			Ireland			Portugal		
		2013F	2014F	2015F	2013F	2014F	2015F	2013F	2014F	2015F	2013F	2014F	2015F
Real GDP	YoY	-1.2%	0.9%	1.2%	-3.9%	-0.9%	0.8%	-0.3%	1.3%	2.9%	-1.4%	1.5%	1.7%
Final Domestic Demand	YoY	-2.7	0.5	1.0	-6.4	-0.6	0.1	-0.2	1.3	0.4	-2.4	1.0	1.2
Private Consumption	YoY	-2.0	1.2	1.2	-5.8	-0.7	0.2	-1.1	0.5	0.4	-1.6	1.1	1.2
Government Consumption	YoY	-2.3	-0.9	0.1	-4.0	0.6	-0.6	-0.6	-2.8	-2.5	-1.7	-0.6	0.8
Fixed Investment	YoY	-5.0	0.0	1.2	-12.8	-1.3	0.8	4.9	10.4	4.1	-6.2	2.5	1.5
Exports	YoY	4.9	5.8	5.2	1.3	1.8	2.7	0.1	5.0	3.8	6.2	4.3	3.9
Imports	YoY	0.4	4.3	4.9	-5.3	-2.0	0.2	1.0	6.7	1.7	2.9	3.8	2.6
CPI	YoY	1.5	0.0	0.1	-0.9	-1.9	-2.2	0.4	0.8	1.0	0.5	-0.7	-0.8
Unemployment Rate	%	26.4	25.6	24.5	27.2	27.5	26.4	13.1	11.4	10.7	16.3	14.7	13.6
Current Account	€bn	7.1	9.3	9.7	1.2	3.2	4.0	10.9	15.4	16.8	0.7	3.7	4.3
	% of GDP	0.7	0.9	0.9	0.7	1.8	2.3	6.6	9.2	9.6	0.4	2.2	2.5
General Govt. Balance	€bn	-71.4	-60.4	-49.2	-6.7	-6.1	-4.2	-11.8	-9.5	-5.7	-9.1	-7.0	-5.8
	% of GDP	-7.0	-5.9	-4.7	-3.7	-3.5	-2.4	-7.2	-5.7	-3.3	-5.5	-4.1	-3.4
Primary Balance	% of GDP	-3.5	-2.4	-1.3	0.4	0.5	0.9	-2.8	-0.7	1.8	-1.1	0.1	0.9
General Govt. Debt	% of GDP	94.4	100.0	103.2	176.3	185.6	191.0	124.0	122.7	122.6	128.8	135.4	137.5

F Citi forecast. YoY Year-to-year growth rate. For Ireland we show the GDP deflator rather than the CPI, for Spain fiscal deficits include the effect of financial support for banks in 2013 (€2.8bn). Sources: INE, Haver Analytics, Eurostat and Citi Research forecasts

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Netherlands

The Dutch government suffered a heavy defeat in the municipal elections in March, with the Liberals and coalition partners Labour both seeing significant drops in their shares of the national vote. Meanwhile, the economy is recovering, as the intensity of private sector deleveraging and fiscal consolidation moderates. We raise our 2014 and 2015 GDP forecasts by 0.2pp & 0.4pp to 1.2% and 1.3%, respectively on better private sector investment prospects and faster growth in real household disposable income thanks to a low inflation profile extending well into 2015.

Belgium

The main parties are busy finalising their manifestos ahead of the May legislative elections. Finance Minister Koen Geens indicated earlier in March that there was a broad consensus to shift part of the fiscal burden away from labour to strengthen Belgium's competitive position, by mulling a VAT rate hike. This strategy, if implemented in 2H-14, would take on board the recommendations made by the EC in its in-depth review and the IMF's latest Article IV report. We add 0.1pp to our 2014 and 2015 GDP forecasts to 1.3% and 1.4%, respectively.

Slovakia

The second round of the Presidential election will take place on 29 March, and it seems like a close call as to who will win. We keep our GDP forecast of 2%YoY in 2014 unchanged after solid growth in 4Q13. Our forecast remains below the MinFin's outlook of 2.3%. The risks look balanced — with a possible positive surprise in construction activity versus downside risks from the Ukraine-Russia crisis and large errors in the BoP on the other. If there were sizeable downward GDP revisions in September, this could push the government's debt-to-GDP ratio above 57%, hence activating the debt brake rule. MinFin's gross borrowing requirements for 2014 will be covered by 58% in 1Q14.

Slovenia

We are lifting our 2014 GDP growth forecast to 0.4%YoY from -0.9% after a smaller-than-expected contraction in 2013. However, the strong contribution of inventories and temporary tax-related purchases to growth in 4Q13 limit our optimism. Export orders have improved and manufacturing capacity use is rising, but poor credit availability and fiscal consolidation remain headwinds for recovery. Fiscal performance has been mixed, but it should be supported by new taxes while the MinFin has already started pre-financing for 2015. The possible need to recapitalize some smaller local banks remains a risk for the fiscal position; this issue may become clearer in late April.

Figure 25. Netherlands, Belgium, Slovakia and Slovenia — Economic Forecasts, 2013-15F

		Netherlands			Belgium			Slovakia			Slovenia		
		2013F	2014F	2015F	2013F	2014F	2015F	2013F	2014F	2015F	2013F	2014F	2015F
Real GDP	YoY	-0.8%	1.2%	1.3%	0.2%	1.3%	1.4%	0.9%	2.0%	2.5%	-0.9%	0.4%	1.4%
Final Domestic Demand	YoY	-2.2	1.0	0.7	0.1	1.1	1.1	-0.8	1.6	2.1	-2.2	-0.2	1.2
Private Consumption	YoY	-2.1	0.0	0.5	0.7	1.1	0.8	-0.1	1.0	1.8	-2.9	-1.4	-0.4
Government Consumption	YoY	-0.7	-0.2	0.0	0.7	0.3	0.8	1.4	1.5	1.2	-2.0	-1.2	0.4
Investment (Ex Stocks)	YoY	-4.9	5.4	2.1	-2.5	1.9	2.3	-4.3	3.3	3.7	-0.2	2.4	1.0
Exports	YoY	1.3	1.0	2.4	1.8	3.0	3.6	4.5	6.2	6.8	2.7	4.5	5.5
Imports	YoY	-0.5	1.5	2.0	1.0	2.6	3.8	2.9	6.4	6.7	1.3	4.2	5.4
CPI (Average)	YoY	2.6	0.6	1.2	1.1	0.7	1.0	1.4	0.3	1.5	1.8	0.7	1.1
Unemployment Rate	%	8.3	8.8	8.6	8.4	8.3	8.1	14.1	13.3	12.7	10.1	10.1	10.1
Current Account	% of GDP	10.4	10.1	9.8	-1.7	-0.1	0.6	2.4	2.8	2.6	6.3	3.0	2.6
General Govt Balance	% of GDP	-3.9	-3.4	-2.5	-3.0	-2.5	-1.3	-2.7	-3.3	-2.7	-14.4	-4.0	-3.5
Primary Balance	% of GDP	-1.9	-1.4	-0.5	0.5	1.0	2.3	-1.2	-1.8	-1.2	-11.7	-1.1	-0.7
General Govt Debt	% of GDP	75.3	76.9	77.0	101.9	102.6	101.3	54.4	57.0	56.4	72.5	77.1	78.6

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

United Kingdom

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We are lifting our UK growth forecasts (which already were well above consensus) to 3.5% for 2014 (highest since 2003) and 3.6% for 2015, from 3.3% and 3.2% respectively last month. Business investment in recent quarters was revised up markedly in the recent GDP release, which makes us more confident that the handover from a falling savings rate to business investment is underway. Second, with inflation pulled down by weakness in import prices and utility prices, the outlook for real incomes and consumer spending is improving. We expect that real personal disposable income will rise by about 2.5% this year, the highest gain since 2006. Third, the housing market remains very strong, with rapid gains in house prices — and this is likely to keep the household savings rate drifting down and support construction output (which has risen by 3.9% in the last two months). The Budget may also reinforce the strong growth outlook, with measures to lift real incomes, investment and exports. We believe that risks are roughly balanced, with downside risks from EM and upside risks from a virtuous circle between the loose policy stance, improving credit availability, plus gains in jobs, incomes and asset prices.

CPI inflation is now down to 1.7% YoY, the lowest since 2009, and may tick a little lower to a trough of 1.4-1.5% YoY during 2014, reflecting weakness in utility prices and imported costs. Inflation is likely to stay well below the 2% target throughout this year, and a little below target still for most of 2015. However, with the strong upturn in growth and rising capacity use, we suspect that the inflation undershoot ultimately will be quite short-lived unless there is a major external disinflationary shock. The MPC have routinely hiked rates with inflation below target, reacting to capacity use, and we expect they will act the same in this cycle. We continue to expect the first hike to come in Q4 this year but, with the stronger growth outlook and rising capacity use, now expect the first stage of the tightening cycle to carry rates up to 2.5% in late 2015 (whereas last month we envisaged a pause at 2.0%).

Figure 26. United Kingdom — Economic Forecasts, 2013-2015F

					2013	2014					2015		
		2013F	2014F	2015F	4QF	1QF	2QF	3QF	4QF	1QF	2QF	3QF	
Real GDP	YoY	1.8%	3.5%	3.6%	2.7%	3.2%	3.4%	3.6%	4.0%	4.1%	3.9%	3.5%	
	SAAR				2.7	3.6	3.8	4.2	4.2	4.0	3.1	2.8	
Domestic Demand	YoY	1.9	3.7	4.2	2.8	4.3	4.0	2.9	3.8	3.9	4.5	4.5	
(Incl. Inventories)	SAAR				1.2	4.9	1.8	3.8	4.6	5.2	4.4	3.8	
Private Consumption	YoY	2.4	3.2	3.7	2.4	2.4	3.3	3.2	3.8	3.8	3.8	3.8	
	SAAR				1.7	3.6	4.2	3.5	3.8	3.7	4.0	3.6	
Government Consumption	YoY	0.9	2.1	0.0	1.9	3.5	1.9	1.5	1.3	0.5	0.2	-0.2	
	SAAR				1.3	3.2	0.9	0.9	0.4	-0.1	-0.5	-0.5	
Investment	YoY	-0.5	11.2	14.3	8.7	10.9	9.8	11.5	12.6	14.8	15.1	14.3	
	SAAR				10.0	10.4	12.0	13.5	14.3	19.7	12.9	10.3	
Exports	YoY	0.8	1.5	5.0	0.7	0.4	-1.3	2.9	3.9	5.5	5.0	4.9	
	SAAR				1.7	-1.0	5.5	5.4	6.0	5.0	3.5	4.9	
Imports	YoY	0.4	2.5	7.4	0.4	3.9	0.8	1.2	4.1	5.4	7.4	8.4	
	SAAR				-3.6	4.1	0.0	4.6	7.7	9.4	8.1	8.3	
Unemployment Rate	%	7.6	6.7	5.1	7.2	7.0	6.9	6.6	6.2	5.8	5.3	4.8	
CPI Inflation	YoY	2.6	1.6	1.8	2.1	1.7	1.7	1.5	1.6	1.8	1.8	1.9	
Merch. Trade	£bn	-108.3	-98.4	-104.9									
	% of GDP	-6.7	-5.7	-5.8									
Current Account	£bn	-56.8	-47.7	-58.3									
	% of GDP	-3.5	-2.8	-3.2									
PSNB	£bn FY	-106.8	-83.5	-57.2									
	% of GDP	-6.5	-4.8	-3.1									
General Govt. Balance	% of GDP	-7.1	-5.4	-3.6									
Government Primary Balance		-3.5	-1.8	0.1									
Public Debt	% of GDP	93.9	96.2	95.7									
Gross Nonoil Trading Profits	YoY	6.9	13.7	4.5									

Note: Fiscal deficit shown excluding financial interventions, RM and APF transfers. F Citi forecast. YoY Year-to-year growth rate. Sources: ONS and Citi Research forecasts

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Switzerland

GDP growth in Q4 was quite soft, at just 0.2% QoQ. However, business surveys remain buoyant and we expect stronger growth in Q1. Growth is domestic-led, with domestic demand up 2.9% YoY in Q4 (highest gain since 2010) and investment up 4.3% YoY. With rising capacity use and low borrowing costs, we expect investment (and domestic demand in general) to remain strong, keeping GDP growth at about 2% in 2014. The period of currency-induced deflation is probably nearly over, with CPI inflation likely to turn positive next year. The SNB is likely to keep policy on hold for a while but it is quite plausible in our view that the SNB will hike before the ECB.

Sweden

We are lifting our 2014 GDP forecast by three-tenths to 2.6% YoY, given the strong upturn in 2H-13, recent business surveys and labour market trends. Nevertheless, there are still potential headwinds from Sweden's high EM exposure, modest growth in key EMU export markets, and the need for eventual fiscal tightening to meet the government's fiscal target. With low inflation, low capacity use and low external interest rates, the Riksbank is likely to keep rates on hold until around mid-2015.

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Denmark

The economy shrank in 4Q-13, with GDP falling by 0.5% Q/Q. The drop was, however, exaggerated by temporary effects from the weather and lower investment in ships. We continue to see moderately accelerating growth ahead, driven by both domestic demand and exports. With economic growth set to outpace potential in 2014-15, unemployment should begin to edge lower and the sizeable output gap to slowly start closing. As EUR/DKK has stayed above 7.462 during most of Jan-Feb and all of March, we expect the DNB would not match any further ECB easing. If the ECB does not cut again, the DNB may well hike during this year.

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Norway

With softer data, the deteriorating jobs market and cooler housing, we are cutting our mainland GDP growth forecast by 0.3pp for 2014-15 (to 1.9% Y/Y and 2.1% Y/Y, respectively). The previous boost from oil and housing is diminishing, while the ongoing erosion in external competitiveness suggests that Norway's nonoil sector will be unable to gain fully from global recovery. The supportive fiscal stance and low policy rates should ensure a soft landing rather than an abrupt economic downturn. We only expect minor adjustments from Norges Bank at the 27 March monetary policy meeting, suggesting initial tightening around mid-2015.

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Figure 27. Switzerland, Sweden, Denmark and Norway — Economic Forecasts, 2013-2015F

		Switzerland			Sweden			Denmark			Norway		
		2013F	2014F	2015F	2013F	2014F	2015F	2013F	2014F	2015F	2013F	2014F	2015F
Real GDP	YoY	2.0%	1.7%	1.9%	1.5%	2.6%	2.7%	0.4%	1.0%	1.5%	2.1%	1.9%	2.1%
Final Domestic Demand	YoY	2.3	2.8	2.7	1.3	2.1	2.4	0.4	1.1	1.5	2.5	1.9	2.1
Private Consumption	YoY	2.3	2.2	1.8	2.0	2.3	2.7	0.0	1.1	1.7	2.1	1.6	2.3
Government Consumption	YoY	3.0	1.6	0.7	1.9	1.2	0.8	0.9	0.7	0.7	1.6	2.6	3.0
Investment (Ex Stocks)	YoY	1.8	5.0	6.2	-1.2	3.0	3.6	0.9	2.0	2.3	4.8	1.8	0.4
Exports	YoY	2.0	3.1	4.0	-0.9	2.7	4.6	1.0	2.8	3.1	-0.5	1.3	3.0
Imports	YoY	1.6	6.0	6.1	-1.0	2.6	4.1	1.5	1.9	3.4	2.2	1.4	2.4
CPI (Average)	YoY	-0.2	-0.1	0.9	0.0	0.2	1.3	0.8	1.5	1.7	2.1	2.0	2.1
Unemployment Rate	%	3.1	2.9	2.6	8.0	7.8	7.5	7.0	6.9	6.7	3.5	3.7	4.1
Current Account	% of GDP	12.0	11.0	10.0	6.2	5.9	5.6	7.3	6.8	5.8	10.6	11.2	11.5
General Govt Balance	% of GDP	0.2	0.5	0.7	-1.4	-1.6	-1.0	-1.2	-1.3	-2.4	11.4	11.9	11.0
General Govt Debt	% of GDP	48.2	46.4	45.4	38.9	39.4	39.0	45.8	45.9	46.9	NA	NA	NA

^a For Norway, mainland GDP. F Citi forecast. YoY Year-on-year growth rate. Sources: National sources and Citi Research forecasts

Canada

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Despite repeated shocks and lingering uncertainties, the economy continues to outperform expectations. Importantly, the expansion is gaining momentum. Real GDP grew just shy of 3% annualized in 4Q — lifting growth for all of 2013 to an above-forecast pace of 2.0% y/y. Severe winter weather in Canada and the US dampened activity in 1Q 2014, but most of the loss should be recovered in 2Q and 3Q. Key supports to the expansion continue to include diminished tail risks abroad, reduced fiscal restraint in the US, the cheaper CAD, and North American energy infrastructure expansion. Internal demand rotation, commodity price volatility, softer EM growth and domestic competitiveness worries likely will remain as headwinds.

CPI inflation remains below the Bank of Canada's 2% target, with slack and intense retail store competition in particular weighing on prices. But various other factors that dampened inflation over the last few years continue to fade. Moreover, there is increasing likelihood that both total *and* core CPI will converge on the target by the end of 2015, when aggregate supply and demand return to balance. Central bankers have expressed reassurance from recent inflation developments and subsequently softened their rhetoric regarding the importance of downside inflation risks at the March policy meeting. On balance, firming CPI inflation profiles suggest that the BoC will keep rates on hold with a neutral bias for some time. We continue to anticipate resumed tightening in 3Q 2015.

Risks to the inflation outlook are two-sided, but roughly balanced. Upside risks include stronger-than-anticipated Advanced Economy growth; greater momentum in domestic demand amid improving business confidence; and sustained domestic housing market strength that reinforces existing imbalances. Downside risks include setbacks in the Euro Area recovery; weaker-than-expected global (especially EM) demand that restrains Canadian exports; and domestic consumer retrenchment linked to household debt and/or disorderly unwind of housing market activity

Figure 28. Canada — Economic Forecast, 2013-2015F

		2013			2014F					2015F		
		2013	2014F	2015F	4Q	1QF	2QF	3QF	4QF	1QF	2QF	3QF
Real GDP	YoY	2.0%	2.3%	2.7%	2.7%	2.3%	2.4%	2.4%	2.3%	2.6%	2.6%	2.7%
	SAAR				2.9	1.5	2.6	2.5	2.4	2.8	2.8	2.8
Final Domestic Demand	YoY	1.4	1.7	2.1	1.2	1.5	1.5	1.7	1.9	2.1	2.1	2.1
	SAAR				1.2	1.6	2.0	2.1	1.9	2.3	2.2	2.1
Private Consumption	YoY	2.2	2.5	2.4	2.4	2.7	2.5	2.5	2.3	2.4	2.4	2.4
	SAAR				3.0	2.0	2.5	2.7	2.1	2.5	2.5	2.5
Government Spending	YoY	0.4	-0.6	0.3	-0.2	-0.5	-0.6	-0.6	-0.5	0.0	0.2	0.4
	SAAR				-0.4	-1.5	-0.5	-0.2	0.1	0.5	0.5	0.5
Private Fixed Investment	YoY	0.4	2.1	3.4	-0.4	0.9	1.7	2.3	3.6	3.5	3.4	3.4
	SAAR				-1.9	4.1	3.8	3.2	3.4	3.8	3.2	3.1
Exports	YoY	2.1	2.8	4.9	3.1	2.1	2.0	3.2	4.0	4.7	4.9	5.0
	SAAR				1.7	1.9	4.5	4.8	4.7	4.9	5.1	5.5
Imports	YoY	1.1	1.9	3.2	1.3	1.1	1.2	2.3	2.8	3.0	3.2	3.3
	SAAR				0.9	2.5	2.5	3.3	3.0	3.3	3.3	3.5
CPI	YoY	0.9	1.9	1.8	0.9	1.4	2.0	2.0	2.3	1.8	1.7	1.8
Core CPI	YoY	1.2	1.7	1.9	1.2	1.4	1.5	1.8	2.1	1.9	1.9	1.9
Unemployment Rate	%	7.1	6.8	6.5	7.0	7.0	6.9	6.7	6.8	6.8	6.6	6.2
Current Account Balance	C\$bn	-60.8	-49.0	-48.8	-64.0	-47.0	-52.6	-45.3	-51.2	-48.9	-52.5	-46.8
	% of GDP	-3.2	-2.5	-2.4	-3.4	-2.4	-2.7	-2.3	-2.6	-2.4	-2.6	-2.3
Net Exports (Pct. Contrib.)		0.3	0.2	0.4	0.2	-0.2	0.5	0.4	0.4	0.4	0.5	0.6
Inventories (Pct. Contrib.)		0.3	0.4	0.1	1.4	0.1	0.0	0.0	0.1	0.1	0.1	0.1
Budget Balance (Fiscal Year)	% of GDP	-0.9	-0.1	0.3								
Federal Budget Debt	% of GDP	32.5	31.2	29.5								
General Govt. Debt	% of GDP	95.7	95.3	93.3								

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

Australia

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Our GDP growth forecast for 2014 is steady this month at 2.9% and we have raised our 2015 forecast to 3.0% (+0.2ppt on last month). Economic activity will therefore be closer to trend by late this year, which is around six months ahead of the RBA's timing. The upgrade reflects a slightly improved outlook for consumer spending but a substantially better dwelling investment profile. But the updates to the outlook were not all positive. We have brought forward the timing of the drop-off in mining capex, reflecting developments in commodity markets and further cost cutting in coal and iron ore projects. Non-mining investment still looks like a story for 2015. With slightly higher growth forecasts, the output gap has narrowed. This has pushed our average underlying inflation forecast from the mid-point to inside the top half of the RBA's 2.0% to 3.0% target band. The risks to the economic outlook are now more evenly balanced compared to more downside risks only a few months ago. So while we have not moved the timing of the first RBA interest rate increase, there is more risk that this occurs in Q4 this year than further out in 2015.

New Zealand

The RBNZ surprised with a more hawkish policy statement to accompany the 25bp rate increase. It contained an upwardly-revised GDP growth estimate and pull-forward in the timing of when the CPI will hit the 2.0% mid-point target by one-year to June 2014. We suspect that economic activity will surpass the RBNZ's 3.0% forecast this year and look for a 3.2% gain. Construction work, which tapered off in Q4, will return as a strong influence on activity, supported by rising migration while incomes will continue to receive a boost from the positive terms of trade shock. We keep our year-end OCR forecast of 3.75% but have lifted lift our year-end 2015 forecast from 4.50% to 4.75%. The prospect that the RBNZ will lead other developed central banks in raising interest rates will probably maintain upside pressure on the exchange rate. There is little the RBNZ can do about this apart from continuing to note publicly that *"the exchange rate remains a headwind to the tradeables sector"*. However, dairy exports appear largely insensitive to the currency's strength, implying a further narrowing in the export base elsewhere.

Figure 29. Australia and New Zealand — Economic Forecast, 2013-2015F

	Australia			New Zealand		
	2013F	2014F	2015F	2013F	2014F	2015F
Real GDP ^a	2.4%	2.9%	3.0%	2.7%	3.2%	2.7%
Real GDP (4Q versus 4Q)	0.3	2.8	3.0	3.1	3.1	2.1
Real Final Domestic Demand	0.9	2.1	1.7	4.4	5.2	4.0
Private Consumption	2.0	2.8	3.2	3.7	3.1	3.0
Govt. Current & Capital Spending ^b	1.1	2.1	2.4	1.3	3.0	2.8
Housing Investment	2.0	9.1	10.0	15.0	16.0	14.4
Business Investment ^c	0.5	-5.1	-7.6	9.3	11.4	5.6
Exports of Goods & Services	6.8	7.5	8.0	1.0	1.5	2.5
Imports of Goods & Services	-2.8	1.8	3.9	8.7	7.6	4.7
CPI	2.4	3.1	2.5	1.1	2.1	2.2
CPI (4Q versus 4Q)	2.7	2.6	2.6	1.6	2.1	2.3
Unemployment	5.8	6.2	5.9	6.0	5.3	5.0
Merch. Trade, BOP (Local Currency, bn)	4.4	9.4	12.1	1.4	-0.1	-2.5
Current Account, (Local Currency, bn)	-45.7	-44.1	-43.2	-7.5	-9.6	-13.0
Percent of GDP	-2.9	-2.7	-2.5	-3.4	-4.2	-5.4
Budget Balance ^d (Local Currency, bn)	-18.7	-48.7	-36.0	-6.4	-3.8	-0.9
Percent of GDP	-1.2	-3.0	-2.1	-2.9	-1.6	-0.4
General Govt. Debt (% of GDP) ^e	30.2	32.1	33.5	39.8	39.0	36.3
Gross Operating Surplus	2.7	5.9	6.6	NA	NA	NA

BOP Balance of payments basis. CPI Consumer Price Index. F Citi forecast. NA Not available. ^aAveraged-based GDP in Australia and New Zealand. ^bIn New Zealand excludes capital spending. ^cIn New Zealand includes government capital spending. ^dFiscal year ending June. Australia's underlying cash balance. ^eAustralia and New Zealand Budget definition and forecasts. Sources: ABS, StatsNZ, NZIER and Citi Research forecasts

China

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Growth may fall toward the government's bottom line by the middle of the year. The market has been bearish about China's economy due to a string of negative news since the beginning of the year: weakening PMIs; a couple of defaults involving trust loans and corporate bonds; RMB depreciation; negative export growth and trade deficit in Feb; intensifying PPI deflation; and weakness in real activity data. According to our estimate, even assuming a decent IP pick-up in March and stable growth of the service sector, GDP growth in 1Q may decelerate to about 7.3%YoY, from 7.7% YoY in 4Q2013. Our credit conditions index, which tends to lead GDP growth by 6 months, suggests growth may flirt with 7%YoY in 2Q. While it appears the government can tolerate growth slightly below 7.5% this year, we think quarterly growth of about 7%YoY would still prompt policy easing.

The government probably will react by fine-tuning macro policies and supporting demand. There are signs that weak demand has contributed to the recent fall in financing costs. The government may advance investment in selected areas, including social housing, irrigation, railways in central and western regions, and energy-saving and environment protection. Since the government no longer has a binding budget revenue target, revenues probably would be allowed to underperform and the deficit to overshoot if the economy slows more than expected. In other words, fiscal policy may provide support even without revising the budget. The PBOC can employ a range of tools to bring down the cost of capital, for example cutting the RRR, if there are capital outflows. If rising housing inventory in smaller cities threatens investment, the government may act to boost demand, including easing of purchase restrictions and government buybacks.

We keep our 2014 GDP growth forecast at 7.3% but cut our inflation forecast. We think export momentum has been stronger than headlines suggest if distortions are removed, and external demand may become a tailwind as the US steps out of the winter-related soft patch. But generally tighter fiscal and monetary policies this year (even considering possible policy easing) are likely to slow infrastructure and property investment. In light of weakening growth and subdued inflation prospects, we cut our 2014 inflation forecast from 3.2% YoY to 2.6%, and no longer expect benchmark rate hikes in 2014-15, as the one-year deposit rate in real terms will stay positive in 2014 and will not be significantly negative in 2015 even with stable rates.

Figure 30. China — Economic Forecasts, 2013-2015F

		2013	2014F	2015F	2013F	2014F				2015F		
					4QF	1QF	2QF	3QF	4QF	1QF	2QF	3QF
Real GDP	YoY	7.7%	7.3%	7.0%	7.7%	7.3%	7.0%	7.1%	7.4%	7.4%	7.2%	6.8%
Real Final Domestic Demand	YoY	8.3	7.2	7.1								
Consumption	YoY	7.8	7.1	7.6								
Fixed Capital Formation	YoY	8.9	7.3	6.6								
Industrial Production	YoY	9.7	8.8	8.5	10.0	9.0	8.4	8.6	9.2	9.2	8.8	8.0
Exports	YoY	7.9	6.3	6.7	7.5	0.2	7.0	8.0	9.0	8.0	7.0	6.0
Imports	YoY	7.3	6.1	7.3	7.1	8.5	6.0	5.0	5.0	6.0	7.0	8.0
Merchandise Trade Balance	\$bn	259	279	286	91	3	75	81	119	14	81	76
FX Reserves	\$bn	3,821	4,080	4,276	3,821	3,905	3,955	4,002	4,080	4,064	4,120	4,171
Current Account	% of GDP	2.0	2.0	1.5								
Fiscal Balance	% of GDP	-1.9	-2.1	-2.0								
General Govt. Debt*	% of GDP	53.7	54.0	53.5								
Urban Unemployment Rate	%	4.1	4.2	4.3	4.1	4.2	4.2	4.2	4.3	4.3	4.3	4.3
CPI	YoY	2.6	2.6	3.2	2.9	2.3	2.6	2.6	2.8	3.1	3.0	3.0
Exchange Rate (end period)	CNY/\$	6.05	6.08	6.01	6.05	6.25	6.24	6.15	6.08	6.06	6.05	6.03
1-Yr Deposit Rate (end period)	%	3.00	3.00	3.00	3.00	3.00	3.00	3.00	3.00	3.00	3.00	3.00

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

India

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As discussed in the latest [India Macroscope - Looking Beyond Elections](#), India's elections will remain a major focus until the 16 May results. Expectations are up, and so are equity and currency markets, which have also been buoyed by genuine progress in shrinking the twin deficits (i.e. current account and fiscal). There clearly is a feel-good factor in the markets. Based on recent assembly elections and trends in opinion polls, many believe that the anti-incumbency factor is strong and there exists a high possibility of a BJP victory (220+ seats), especially since the BJP has made significant progress in battleground states such as UP and Bihar, which represent 120 seats of the total 543.

However, it is still an uphill task for the economy. While growth has likely bottomed, with GDP growth likely to pick up to 5.6% in FY15 from 4.9% in FY14, the shallow recovery is dependent on 'unlocking investments' and managing non-performing loans (NPLs) in the banking sector. India's private-sector leverage is up from 40% of GDP in FY03 to 70% currently, asset quality is down, and with further asset pressures ahead, there is banking system risk and 'ability-to-grow' overhang. The extent of stress and the challenge of capital will limit any economic uptick. An investor-friendly election outcome would help alleviate concerns, but any unexpected election result or new financial market weakness would add to challenges.

On the monetary front, thanks to the reversal of the vegetable price shock, both the inflation indices surprised on the downside, with the latest CPI coming in at 8.1% and WPI at 4.7%. We maintain our view that WPI and CPI inflation will average 5.5% YoY and 8.3% YoY respectively in FY14/15. With inflation likely to trend in line with the "RBI's glide-path", we expect an extended pause in policy rates. We expect 10y bond yields to remain range-bound in 8.7-9% on tight liquidity, upcoming supply, and less recourse to OMOs.

Lastly, we maintain our positive outlook on the external front. We expect the FY14 CAD at US\$36.8bn or 2% of GDP. Going forward for FY15, the resumption of iron ore exports and potentially lower coal/metal scrap imports should partially offset a pick-up in gold and/or capital goods and we expect the CAD to stay comfortable at US\$46.7bn or 2.3% of GDP. Despite an improved CAD and recent increase in capital flows, we expect the INR to stay in the 60-64 range due to: (1) Challenging EM environment and (2) Dip in forward adjusted reserves.

Figure 31. India — Economic Forecasts, FY2013/14-2015/16F

		FY 13/14F	FY 14/15F	FY 15/16F
Real GDP	YoY	4.9%	5.6%	6.2%
Final Domestic Demand	YoY	3.0	4.6	6.3
Private Consumption	YoY	4.1	5.5	7.0
Fixed Investment	YoY	0.2	2.5	5.0
Exports	YoY	8.0	11.0	9.0
Imports	YoY	-1.6	9.5	9.3
Wholesale Price Index	YoY	6.0	5.5	5.0
Consumer Price Index	YoY	9.6	8.3	7.5
Current Account	US\$ bn	-37	-47	-58
	% of GDP	-2.0	-2.3	-2.5
Consolidated Fiscal Balance	% of GDP	-6.9	-6.7	-6.5
Centre Fiscal Balance	% of GDP	-4.6	-4.1	-4.0
US Dollar Exchange Rate	Average	61.8	64.3	63.2

Sources: Haver Analytics and Citi Research forecasts

Korea

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In February, headline CPI inflation posted 1.0% YoY, 0.1%p lower than in January as supply-side deflation continues. However, expected inflation has stayed high at 2.9%YoY for six months. Inflation is likely to pick up gradually in coming months as base effects caused by free childcare and free school meals fade and processed food prices rise. Meanwhile, the jobless rate in February unexpectedly soared to 3.9% (seas adj) due to increases in job-seeking along with job openings in the public sector and government efforts to increase female and youth employment. Job growth remains steady, at over 110K MoM following 207K MoM in January. The jobless rate might stay higher, at around 3½% in coming months. However, that might not lead policymakers to employ further accommodative measures since job growth in services and manufacturing sectors is expected to continue. The newly-appointed BoK Governor Lee passed his personal hearing at the National Assembly. At the hearing, he revealed his view that the current policy rate is low enough to support economic recovery, and that household debt trends are worrying but are unlikely to trigger a financial crisis.

Indonesia

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In early March, the IDR recovered 8% from its weak point in February. The improving trend of the current account deficit, along with increased market transparency, has led to a decline in risk premia on LCY bonds. This has been topped by the long-awaited nomination of Jakarta Governor Joko Widodo as a presidential hopeful from the PDIP party. Widodo is widely expected to accelerate the pace of reform in Indonesia if elected to the presidency. However in terms of taking stock on the economy, we still see significant challenges ahead. The reversal in the CA deficit has been mainly a result of the downturn in domestic demand growth, which slowed to 5.1% YoY in 2013 from 6.1% in the 2012. Meanwhile reforms are still urgently needed but have not been fully implemented. Recent adjustments to the policy mix have not yet spearheaded a game-changing rebound in manufacturing exports. We believe a tight bias on monetary policy is still warranted, and we still see another 25bps hike this year. We also doubt the sustainability of a continued strengthening of Indonesia's trade weighted exchange rate, as it may risk a resurgence of imports -- which would complicate efforts to achieve BI's current account deficit target of 2.5% of GDP.

Figure 32. Korea and Indonesia — Economic Forecasts, 2013-2015F

		Korea			Indonesia		
		2013F	2014F	2015F	2013F	2014F	2015F
Real GDP	YoY	3.0%	3.7%	3.9%	5.8%	5.3%	5.5%
Final Domestic Demand	YoY	2.8	3.1	3.7	5.1	4.9	4.5
Private Consumption	YoY	2.0	2.9	3.3	5.3	5.1	4.4
Fixed Investment	YoY	4.2	4.3	4.6	4.7	3.5	6.1
Exports	YoY	4.3	5.9	7.3	5.3	4.0	5.7
Imports	YoY	1.6	6.6	7.5	1.2	2.3	3.1
Consumer Price Index	YoY	1.3	2.1	3.0	6.4	6.4	5.7
Unemployment Rate	%	3.1	3.3	3.1	6.3	6.5	6.3
Current Account	US\$ bn	70.7	52.4	46.6	-28.5	-20.9	-19.3
	% of GDP	5.4	3.7	3.1	-3.3	-2.5	-2.1
Fiscal Balance	% of GDP	0.8	0.9	1.5	-2.2	-2.2	-1.7
US Dollar Exchange Rate	Average	1095	1073	1064	10449	11807	12096

Sources: Haver Analytics and Citi Research forecasts

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Hong Kong

The recent CNH depreciation likely is temporary, therefore we do not expect a large contraction in RMB deposits in HK. The HKD will likely also stay softer with China/RMB worries and choppy equity markets. We also think that cross-border lending to China by Chinese banks will continue, given still-ongoing liquidity tightness in China. This is a key focus for the policymakers, who are closely monitoring liquidity in the system and lending standards. EFN yields have reacted after the FOMC surprise and likely will continue to trend up with US yields as the Fed normalizes policies. Property price easing is likely to continue as markets worry about higher rates, but a price fall would be unlikely to trigger any loosening of property-cooling measures. Lower private rental pass through likely also can help reduce inflation in 2014. We expect 1Q GDP will likely remain flat at about 3% YoY, given the improvements in PMI business conditions readings.

Singapore

The economy started 2014 on a weak note, possibly declining on a sequential basis in 1Q14. Manufacturing likely declined sequentially in Jan-Feb, as positive sequential growth in Jan-Feb NODX levels versus 4Q13 may have been met by inventory drawdowns. Sea and air transport volumes were also weak in Jan-Feb. That said, this GDP profile remains within MAS's expectations for volatility around a mild expansion trend this year and, along with rising core inflation trends (also within expectations), leaves no strong grounds for the central bank to change its monetary policy stance in April. In the medium term, domestic disinflationary forces are building in rentals, road transport prices, demand-pull pressures from deleveraging, and a loss of cost competitiveness.

Taiwan

We think 1Q GDP likely dipped to about 2.3% YoY. The TWD depreciated further along with the CNH, which in turn likely will help exports. Export trends remained weak in Jan-Feb, but even-weaker imports supported the trade surplus, which is of slight consolation for its contribution to 1Q GDP. We believe trade flows could firm in 2Q as various tech product launches begin. Foreign investors' inflows could resume if the service pact with China is passed, although the passage of the pact by the cabinet panel was met by other political setbacks as students occupied the Legislative Yuan. Benign inflation will likely allow the CBC to maintain maximum accommodation to support the economy in 2014. 10-year Government yields will likely edge up along with global long-end yields, but the magnitude of increase will likely be mild to reflect the thus-far lackluster domestic recovery.

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Figure 33. Hong Kong, Singapore and Taiwan — Economic Forecasts, 2013-2015F

		Hong Kong			Singapore			Taiwan		
		2013F	2014F	2015F	2013F	2014F	2015F	2013F	2014F	2015F
Real GDP	YoY	2.9%	3.4%	3.8%	4.1%	3.4%	4.0%	2.1%	3.2%	3.8%
Final Domestic Demand	YoY	3.8	2.2	2.3	1.9	2.9	2.1	2.2	1.8	2.4
Private Consumption	YoY	4.2	2.1	2.4	2.7	1.9	2.0	1.8	1.6	2.8
Fixed Investment	YoY	3.3	2.6	2.8	-2.6	1.2	1.0	5.3	2.8	3.4
Exports	YoY	6.5	5.2	6.3	3.6	3.5	3.2	3.8	4.6	6.2
Imports	YoY	6.9	4.8	5.7	3.0	2.7	2.8	4.0	3.9	5.2
CPI	YoY	4.3	3.9	4.0	2.4	1.8	1.4	0.8	1.3	1.9
Unemployment Rate	%	3.4	3.1	3.1	1.9	1.8	1.8	4.2	4.0	3.9
Current Account	US\$ bn	7.5	9.0	11.6	54.4	55.3	58.2	57.4	56.4	56.2
	% of GDP	2.8	3.1	3.9	18.4	18.0	18.0	11.7	11.0	10.2
Fiscal Balance	% of GDP	0.8	1.3	0.7	1.1	-0.3	0.2	-1.5	-1.4	-0.8
US Dollar Exchange Rate	Average	7.76	7.76	7.75	1.25	1.29	1.28	29.68	30.37	29.99

Sources: Haver Analytics and Citi Research forecasts

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Russia

The rising tensions in Ukraine make for a very challenging backdrop for the Russian economy, creating substantial downside risks to economic performance. The combination of more subdued investment and consumption spending related to heightened uncertainty, and tighter monetary policy, led us to downgrade our 2014 GDP forecast from 2.6% to 1.0% (1.3% in 2013). Investment spending will be the key avenue via which market volatility will affect growth performance. Our more positive view on 2014 GDP was critically dependent on the assumption that government-led oil and gas investment would come out of its 2013 doldrums, with new projects coming on stream. However, given the uncertain backdrop, we now have much less confidence of this scenario playing out, even if, in principle, the government may feel more pressure to 'take control' of SOE investment. Consumer spending will also feel the pain. While consumption is the only bright spot in Russian macro, it has been slowing recently as fears that the consumer boom might turn into a bubble have led to more restrictive regulatory behaviour. Broader uncertainty will probably now further weigh on consumer spending. The CBR was right, in our view, to hike rates by 150bp to 7.00% to limit contagion, but this will also come at the cost of stronger headwinds to growth (even if the CBR fully unwinds the hike by year-end). More generally, Russia faces a tight fiscal-monetary policy mix, which creates an unfavourable background to the economy.

Turkey

All eyes are on the March 30 local elections, which will be followed by the first round of presidential elections on August 10th. It is widely believed that the performance of the AKP at the upcoming local elections is likely to have an important bearing on the PM's decision to run for the presidency and the timing of the general elections (originally scheduled for June 2015). Regarding the March 30 local elections, the average of the recent polls put the AKP at about 45%, followed by the CHP (28%) and the MHP (15%). It will be interesting to see whether the severe headwinds which the AKP has faced since the December 17 events will affect its performance. Turning to economics, while the production side seems resilient, we believe domestic demand is on track to weaken considerably. Specifically, the relatively sharp drop in consumer confidence, coupled with a tighter monetary policy stance and the lira depreciation, signals a significant drop in consumer spending. Against this backdrop, we expect GDP growth to decelerate to about 2.3% this year from an estimated 4% in 2013. It is worth underlining that global and political headwinds raise the risks associated with our 2014 growth forecast.

Figure 34. Russia and Turkey — Economic Forecast, 2013-2015F

		Russia			Turkey		
		2013F	2014F	2015F	2013F	2014F	2015F
Real GDP	YoY	1.3%	1.0%	2.3%	4.0%	2.3%	3.5%
Final Domestic Demand	YoY	2.4	1.9	2.7	4.5	-3.2	3.4
Private Consumption	YoY	4.3	3.2	3.1	4.6	-1.5	3.2
Fixed Investment	YoY	-0.3	0.0	3.5	4.4	-11.7	4.0
Exports	YoY	1.5	2.0	2.1	1.9	9.6	4.4
Imports	YoY	5.5	4.5	5.0	8.1	-10.4	4.0
CPI	YoY	6.8	6.0	5.2	7.5	7.7	7.4
Unemployment Rate	%	5.5	5.7	5.8	9.8	9.5	9.5
Current Account	US\$ bn	34.0	33.3	24.3	-64.9	-39.1	-42.0
	% of GDP	1.6	1.8	1.2	-7.8	-5.2	-5.3
Fiscal Balance	% of GDP	-2.0	-4.4	-4.9	-1.2	-2.8	-3.2
US Dollar Exchange Rate	Average	31.9	38.2	38.7	1.91	2.34	2.45

Sources: Haver Analytics and Citi Research forecasts

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Hungary

Incoming growth indicators have surprised to the strong side and so far there are no signs of a negative impact from the Russian-Ukraine confrontation on the European growth outlook. Therefore we have upped our 2014 GDP forecast from 1.9%YoY to 2.1% based on an upward revision to exports and investment. Signs of tightening labour market conditions and a sharper pickup in household consumption are still missing, which suggests that inflation pressures are likely to remain low. Inflation trends suggest that, even after the elimination of regulated utility price cuts, CPI may remain close to the NBH's 3% official target. The soft inflation outlook and a reduction in household FX debt exposure (unhedged household FX loans are down from 25% of GDP peak to around 10% of GDP) have increased the NBH's tolerance to FX weakness. We expect that renewed waves of a global EMFX sell off may continue to weigh on the HUF and force the NBH to halt rate cuts in the spring. Given the NBH's dovish bias and willingness to tolerate weaker FX, the beginning of a gradual rate hiking cycle may be postponed to late 2014. We expect the base rate to reach around 3% by end-2014 and 4% by mid-2015 as headline CPI rises towards to 2.5-3%.

Poland

4Q 2013 GDP growth accelerated to 2.7%YoY from 1.9% in 3Q13 and monthly data for early 2014 confirm further improvement. The February PMI index rose to 55.9 — the highest level since Dec 2010, reflecting increasing new orders. Consequently, industrial and construction output growth accelerated in February and there was a further improvement in wage and employment growth. We expect these trends to continue, resulting in a further acceleration of GDP growth in coming quarters, with an annual average growth in 2014 of 3.4%YoY vs. 1.6% in 2013. At the same time, as recent inflation data surprised to the downside, we currently expect a much lower inflation path than a few months ago. We forecast CPI growth to only slightly exceed 1.5% at year-end and to hit the inflation target of 2.5% at the turn of Q1 or Q2 2015. The MPC extended its forward guidance, signaling no change of interest rates at least until 3Q this year. Taking this into account, along with low inflation and despite stronger growth, we currently expect the first rate hike in early 2015, which is still slightly earlier than expected by the market. Stronger GDP growth has been reflected in favourable budget trends at the start of the year and will likely translate into lower borrowing needs this year. Lighter bond supply later this year, lower inflation, and prospects that rates will only rise next year will likely delay any increase in bond yields. Meanwhile, QE tapering by the Fed and weakening of EM currencies in coming months probably will also negatively impact the zloty.

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Figure 35. Hungary and Poland — Economic Forecasts, 2013-2015F

		Hungary			Poland		
		2013F	2014F	2015F	2013F	2014F	2015F
Real GDP	YoY	1.1%	2.1%	1.5%	1.6%	3.4%	3.6%
Final Domestic Demand	YoY	1.4	1.5	0.5	0.7	3.0	3.6
Private Consumption	YoY	-0.1	0.7	1.0	0.8	2.7	3.2
Fixed Investment	YoY	2.1	3.1	0.0	-0.4	4.7	6.0
Exports	YoY	5.3	4.8	4.6	4.3	5.9	6.5
Imports	YoY	5.3	4.6	4.1	0.7	6.7	7.5
CPI	YoY	1.7	0.7	2.9	0.9	1.0	2.7
Unemployment Rate	%	9.1	8.6	8.5	13.4	12.4	11.7
Current Account	US\$ bn	2.9	3.3	2.7	-7.8	-13.9	-21.8
	% of GDP	2.1	2.6	2.0	-1.5	-2.5	-3.6
Fiscal Balance	% of GDP	-2.6	-2.9	-2.9	-4.2	5.7	-2.3
Euro Exchange Rate	Average	297	322	330	4.20	4.27	4.17

Sources: Haver Analytics and Citi Research forecasts

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Czech Republic

Despite stronger 4Q13 GDP data (1.9%QoQ), we maintain our 2014 growth forecast at 1.9%YoY owing to less benign carry-over effects (GDP contracted 0.9%YoY in 2013, less than the flash estimate of -1.1%) accompanied by mixed implications from the 4Q data. In particular, the forward buying of tobacco contributed strongly to GDP growth in 4Q13 (1.4%pts QoQ), and this is likely to unwind during 2014. However, value added growth was healthy and our analysis suggests the forward buying effect in fixed investment and private consumption (owing to FX intervention) was not too large in 4Q. Our CPI forecast is below the CNB's projection for both 2014 and 2015. However, we do not think this has major policy implications, as the difference mainly reflects lower regulated and fuel prices. There is an upside risk to our forecast if a weaker USD does not materialize. We still expect the CNB to start its exit strategy in 2Q15, but we moved the first hike earlier to 4Q15 reflecting a weaker koruna in our forecast. On the fiscal front, we will watch the Finance Minister's tax proposal, although it is line with the Government's statement and is not game-changing in terms of fiscal policy. We estimate the MinFin's issuance calendar for 2Q14 points to primary issuance of CZK130bn in 1H14. We think this would leave the MinFin's GBR for 2014 covered by 55%.

Romania

Following the National Liberal Party's decision to withdraw from the ruling alliance, PM Ponta reorganized the government, which was approved by Parliament on 4 March. This development has in turn alleviated concerns about the political outlook and the fate of the EU-IMF supported economic program. Regarding the growth outlook, we expect the key growth drivers to switch from net exports to domestic demand, with GDP growth at 3.0% in 2014 compared with an estimate of 3.5% in 2013. Private investment in particular is likely to benefit from the likely acceleration in the absorption of EU funds. Moreover, developments to date suggest the best of inflation is probably behind us. Specifically, a quick glance at the CPI components suggests service and nonfood prices remain sticky, while there are hints that a reversal on food inflation may be under way — all of which lead us to look for a year-end inflation of 4.0% YoY. Against this backdrop, we expect the NBR to keep rates on hold at 3.5% during the remainder of the year.

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Figure 36. Czech Republic and Romania — Economic Forecasts, 2013-2015F

		Czech Republic			Romania		
		2013F	2014F	2015F	2013F	2014F	2015F
Real GDP	YoY	-0.9%	1.9%	2.5%	3.5%	3.0%	3.4%
Final Domestic Demand	YoY	-0.6	1.1	2.6	-0.7	1.8	3.3
Private Consumption	YoY	-0.1	0.5	1.8	1.4	1.5	3.5
Fixed Investment	YoY	-3.3	2.3	5.1	-5.6	3.2	3.5
Exports	YoY	0.1	6.5	6.4	12.4	5.5	4.5
Imports	YoY	0.5	5.7	6.4	2.2	3.0	4.0
CPI	YoY	1.4	0.8	2.0	4.0	2.4	3.4
Unemployment Rate	%	7.0	6.3	5.5	5.3	5.5	5.5
Current Account	US\$ bn	-2.9	2.3	1.7	-2.0	-5.1	-9.3
	% of GDP	-1.4	1.1	0.8	-1.1	-2.5	-4.2
Fiscal Balance	% of GDP	-2.4	-2.9	-2.9	-2.5	-2.3	-2.3
EURCZK, USDRON	Average	26.0	27.6	27.1	3.3	3.3	3.2

Sources: Haver Analytics and Citi Research forecasts

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Brazil

The energy situation is becoming more serious, and chances of rationing are increasing significantly. This may reduce the probability that President Rousseff is reelected in the first round. While her victory is still assumed in our base case scenario, the likelihood of an alternative outcome is increasing. We keep our GDP growth forecast at 1.3% in 2014, despite the better-than-expected 0.7 QoQ growth in 4Q13, as we do not see drivers to boost growth ahead. Regarding monetary policy, we expect another 25bps hike in April, driving the Selic rate to 11%. Furthermore, we continue to expect the Central Bank to resume the tightening cycle in 2015, increasing the Selic rate by an additional 100bps (to 12%) in 1H15. We forecast annual CPI inflation to stand at 6.1% in 2014-yearend and at 5.8% in 2015, both above the 4.5% mid-point target but still below the target band's 6.5% upper bound. In terms of fiscal policy, we do not expect a significant adjustment this year and the primary surplus should remain below the 2013 level (1.5% against 1.9% of GDP in 2013). On the external accounts, we expect the current account deficit to be around USD80 billion, despite an improvement in the trade balance reflecting the weaker BRL and the improvement in global growth scenario. Finally, it is worth mentioning S&P's decision to downgrade Brazil's sovereign rating to BBB- (from BBB) with stable outlook (see [Brazil Macro Flash](#), March 25, 2014).

Mexico

Industrial production grew by 0.7% YoY and 0.5% MoM in January. This positive performance was boosted by manufacturing output, up 2.5% YoY and 2.3% MoM, despite the negative effect from the severe weather in the U.S. However, retail sales and formal sector employment in February suggest slower internal market growth. All things said, we have revised our 1Q14 GDP growth forecast to 2.7% from 3.3% YoY before. For 2014 as a whole, we now see economic growth at 3.3%, from 3.8% previously. Meanwhile, annual headline inflation fell to 4.23% in February from 4.48% in January. In our view, inflation risks are declining and there are no traces of second-round effects stemming from the fiscal reform. We thus expect annual inflation to keep falling in coming months, reaching a trough of 3.75%, after which it should rebound due to the low annual comparison base. We have adjusted our headline annual inflation forecast for end-year 2014 to 4.0%, from 4.15% previously. This combination — fewer inflation risks and still a negative output gap — are consistent with our expectation of Banxico keeping its policy rate unchanged at 3.5%. On the reform front, Congress has already passed pending secondary legislation on Competition Policy, Telecommunications, Universal Pensions and Unemployment Insurance. Additionally, we are confident the secondary legislation on energy reform will be ready before the end of April.

Figure 37. Brazil and Mexico — Economic Forecasts, 2013-2015F

		Brazil			Mexico		
		2013	2014F	2015F	2013F	2014F	2015F
Real GDP	YoY	2.3%	1.3%	1.8%	1.1%	3.3%	4.0%
Final Domestic Demand	YoY	2.9	1.3	1.6	1.4	3.6	4.4
Private Consumption	YoY	2.3	1.7	1.9	2.5	3.4	4.1
Fixed Investment	YoY	6.3	-0.8	1.1	-1.8	4.9	7.0
Exports	YoY	2.5	2.5	6.8	1.4	7.4	8.6
Imports	YoY	8.4	2.3	4.4	1.2	7.1	8.6
CPI	YoY	6.2	6.1	5.9	3.8	4.2	3.6
Unemployment Rate	%	5.5	5.8	6.0	5.0	4.8	4.8
Current Account	US\$ bn	-81.4	-82.5	-81.7	-22.3	-27.4	-25.8
	% of GDP	-3.7	-4.0	-4.1	-1.8	-2.1	-1.8
Fiscal Balance	% of GDP	-3.3	-3.7	-2.8	-2.4	-3.5	-2.5
US Dollar Exchange Rate	Average	2.16	2.53	2.73	12.76	13.22	12.89

Sources: Haver Analytics and Citi Research forecasts

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Argentina

The external front has remained calm during the last two months, following the step devaluation in the official FX market which took place in January. In the meantime, the authorities have continued to work on normalizing relationships with international creditors, reaching an agreement (which has to be ratified by Congress) with Repsol and resuming talks with the Paris Club — official negotiations were set to start in the second half of May. However, from a fundamental point of view, little has changed. The rise in nominal interest rates which took place in the beginning of this year has been largely offset by the acceleration in inflation, with consumer prices increasing by 35% in the last 12 months according to private estimates. Additionally, the authorities have not delivered any fiscal tightening, and subsidy cuts continue to be delayed. In the absence of fundamental changes in the main economic variables, tensions in the FX front could resume in 2H14, exacerbating the tradeoff between external/financial sustainability and economic activity. The normalization of Argentina's relationships with the investor community is good news, but it is likely to be a long process and dollar inflows will likely drop in the second semester due to seasonal factors.

Venezuela

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Social unrest continued affecting the country throughout February and most of March, with violent events adding to the already-challenging economic environment. While we believe that the peak of this bout of politically-motivated social unrest has been reached, we cannot rule out additional social unrest as a consequence of the challenging economic situation faced by Venezuelans, namely high levels of inflation and scarcity. The main economic development continues to be the announcement of SICAD II (complementing SICAD I auctions). We think this alternative mechanism could ease some of the pressure in the fiscal accounts from the government and PDVSA. Even so, uncertainty on the sources of foreign currency to be offered in this market, and thus scope to reduce USD shortages in the country, are high. Therefore, we are keeping our -1% GDP growth forecast for this year, while we continue to see inflation at 75% at yearend. It is important to note that both SICAD I and SICAD II systems are alternative distribution mechanisms for USD and hence their ability to generate additional supply of foreign currency is limited to oil revenues and the stock of USD-denominated debt. For that reason, we expect an eventual USD-denominated debt issuance announcement. We think that the USD-denominated issuance is more likely to come from the sovereign first and in an amount that could be around USD3-4 billion.

Figure 38. Argentina and Venezuela — Economic Forecasts, 2013-2015F

		Argentina			Venezuela		
		2013F	2014F	2015F	2013F	2014F	2015F
Real GDP	YoY	4.9%	1.0%	1.5%	1.5%	-1.0%	1.9%
Final Domestic Demand	YoY	6.0	0.8	1.6	-0.2	-1.1	0.7
Private Consumption	YoY	6.0	2.1	2.1	3.8	0.1	0.3
Fixed Investment	YoY	5.7	-3.7	-0.3	-3.5	-3.5	0.9
Exports	YoY	-0.1	-1.6	-1.5	-3.8	1.3	4.2
Imports	YoY	8.6	-1.9	0.0	-4.6	-0.7	-1.0
CPI	YoY	10.6	NA	30.5	38.5	62.5	82.1
Unemployment Rate	%	7.1	7.7	8.1	5.6	5.7	5.8
Current Account	US\$ bn	-2.9	-1.9	-1.6	12.2	14.9	18.2
	% of GDP	-0.6	-0.5	-0.4	3.3	4.0	5.1
Fiscal Balance	% of GDP	-2.4	-3.1	-2.3	-11.9	-11.1	-10.3
US Dollar Exchange Rate	Average	5.45	8.89	11.81	5.99	10.58	19.80

Sources: Haver Analytics and Citi Research forecasts

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Saudi Arabia

Fitch upgraded its ratings on Saudi Arabia by one notch to AA in March, putting it one notch above the ratings of S&P and Moody's. We believe the rating action is warranted given Saudi Arabia's fiscal and external strength, but consider the timing to be questionable given our view that the Kingdom, like the other GCC oil producers, faces a tightening in fiscal conditions in the medium term. We expect the public finances and external balances will remain robust in the near term: the current account surplus looks set to remain in double digits in 2014, while we expect the fiscal surplus will narrow from around 10% this year to a still-healthy 5% in 2014. That said, we think rising expenditures and an expected leveling off in oil revenues and production present a challenge in the medium- to long-term. We forecast the fiscal breakeven oil price will rise to over US\$90 per barrel in 2014 and will continue to rise, resulting in forecast deficits as early as 2016. Although Saudi has ample resources to finance expected deficits from current cash reserves, the outlook does underscore the need for structural reform to set public finances on a long-term sustainable footing.

United Arab Emirates

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We continue to harbor concerns regarding the pace of asset price inflation in Dubai. The Dubai Financial Market all-shares index gained over 108% in value in the course of 2013, and the real estate market continues to surge, with Cluttons data showing that the average selling price of mid-range villas rose 42% during 2013. These growth rates have persisted in the first two months of 2014. We believe that the award of Expo in November 2013 is fuelling further exuberance in the market, which has been accompanied by the announcement of a large number of new real estate projects. For now, construction activity remains contained to new developments in prime locations, such as on the Palm or in the Downtown area. Moreover, corporate leverage is on the decline. Should, however, we see a surge in construction activity in less-prime areas, accompanied by aggressive off-plan sales strategies, and a sharp rise in borrowing, we believe the potential for further property-led volatility in the Dubai economy will become increasingly likely.

Figure 39. Saudi Arabia and United Arab Emirates — Economic Forecasts, 2013-2015F

		Saudi Arabia			United Arab Emirates		
		2013F	2014F	2015F	2013F	2014F	2015F
Real GDP	YoY	3.7%	4.2%	6.1%	3.7%	4.0%	4.0%
Final Domestic Demand	YoY	8.0	8.0	8.1	4.7	4.7	4.7
Private Consumption	YoY	5.0	5.0	5.0	5.0	5.0	5.0
Fixed Investment	YoY	10.0	10.0	10.0	5.0	5.0	5.0
Exports	YoY	-1.2	1.0	1.3	14.0	13.0	14.0
Imports	YoY	15.0	15.0	15.0	15.0	15.0	15.0
CPI	YoY	3.5	3.5	4.1	1.5	1.3	1.6
Current Account	US\$ bn	134.5	106.4	75.8	107.3	93.8	80.0
	% of GDP	18.2	13.7	9.3	26.2	21.4	17.0
Fiscal Balance	% of GDP	7.4	5.1	0.4	NA	NA	NA
US Dollar Exchange Rate	Average	3.75	3.75	3.75	3.67	3.67	3.67

Sources: Haver Analytics and Citi Research forecasts

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Nigeria

Although political uncertainty is set to rise towards the February 2015 elections, we still expect growth to remain robust at over 6% in 2014. But, while the finance minister, Ngozi Okonjo-Iweala, remains firmly committed to maintaining fiscal discipline despite the approaching elections, the fiscal picture could deteriorate, notably in 2H 2014 if supplementary budgets are passed or there is no recovery in oil production. The rising political tension is also clear from the recent suspension of Lamido Sanusi as central bank governor, which also means that the naira is likely to remain under pressure in coming months. How the CBN responds to this will be crucial in understanding its overall commitment to naira stability going forward. But while we expect greater naira volatility on a day-to-day basis in 2014, we still expect only limited overall naira depreciation, unless there is a major change to the oil price-production equation or reserves really comes under pressure.

South Africa

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We continue to expect GDP growth of only 2.4% this year but acknowledge downside risk to this. Higher inflation and tighter monetary policy will probably weigh on the economy, while unexpected electricity shortages will likely dampen production growth. Limited capital expansion is weighing heavily on private investment which, in turn, means little upside for job creation. To compensate, wage negotiations probably will remain at above-CPI levels which, together with the currency, food prices and rental yields will probably push inflation back above the SA Reserve Bank's 6% target ceiling in March, keeping it above the target until Q1 15. The SARB expects a more prolonged breach until Q2 15, which was key to its proactive 50bp rate hike in January. We expect the MPC to pause in March, signaling a slower hiking cycle than usual. This is also enabled by a relatively dovish macro backdrop versus January. However, we believe another 50bp rate hike in May is on the cards, as a signal that the SARB is still intent on normalizing policy rates in order to manage inflation expectations. We think a final 50bp hike in July has an even chance of transpiring. In total, this expected 150bp in hikes will slow household consumption and fixed investment. The current account deficit is narrowing, printing 5.1% of GDP in Q4-13 thanks to more meaningful import compression. Still, electricity difficulties will keep exports at bay and we only expect a slow narrowing this year to 4.7% of GDP on average. While a smaller current account deficit is ZAR-positive, it still requires sizeable capital flows in a global environment where liquidity is drying up. What's more, political noise remains elevated in H1-14 given the upcoming national elections on 7 May 2014. Both factors are key reasons why the ZAR is likely to remain undervalued over coming months.

Figure 40. Egypt, Nigeria and South Africa — Economic Forecast, 2013-2015F

		Egypt			Nigeria			South Africa		
		2013F	2014F	2015F	2013F	2014F	2015F	2013F	2014F	2015F
Real GDP	YoY	2.0%	2.9%	3.4%	6.5%	6.6%	6.4%	1.9%	2.4%	2.8%
Final Domestic Demand	YoY	3.1	4.2	6.1	NA	NA	NA	2.9	2.3	3.1
Private Consumption	YoY	2.7	3.5	5.1	NA	NA	NA	2.6	2.3	3.0
Fixed Investment	YoY	3.0	8.9	10.3	NA	NA	NA	4.7	2.3	4.1
Exports	YoY	2.9	2.0	6.0	NA	NA	NA	4.2	6.5	5.6
Imports	YoY	2.3	4.7	13.4	NA	NA	NA	4.7	6.5	6.8
CPI	YoY	9.5	9.2	7.1	8.5	8.8	10.6	5.8	6.5	6.1
Unemployment Rate	%	13.5	14.2	14.5	NA	NA	NA	24.7	25.0	24.6
Current Account	US\$ bn	-4.2	-3.5	-6.2	22.4	15.8	10.7	-20.4	-16.6	-13.8
	% of GDP	-1.7	-1.3	-2.2	7.0	4.4	2.6	-5.8	-5.1	-3.9
Fiscal Balance	% of GDP	-11.6	-10.9	-9.4	-2.6	-2.9	-2.9	-4.3	-4.2	-4.2
US Dollar Exchange Rate	Average	6.87	7.11	7.54	159.2	164.73	168.83	9.65	11.39	11.60

Sources: Haver Analytics and Citi Research forecasts

Figure 41. Selected Emerging Market Countries — Economic Forecast Overview, 2013-2015F

	GDP Growth (%)			CPI Inflation (%)			Current Balance (% of GDP)			Fiscal Balance (% of GDP)		
	2013F	2014F	2015F	2013F	2014F	2015F	2013F	2014F	2015F	2013F	2014F	2015F
Asia	6.3	6.2	6.2	3.7	3.5	3.8	2.1	2.0	1.5	-2.3	-2.3	-2.1
China	7.7	7.3	7.0	2.6	2.6	3.2	2.0	2.0	1.5	-1.9	-2.1	-2.0
Hong Kong	2.9	3.4	3.8	4.3	3.9	4.0	2.8	3.1	3.9	0.8	1.3	0.7
India	4.9	5.6	6.2	9.6	8.3	7.5	-2.0	-2.3	-2.5	-6.9	-6.7	-6.5
Indonesia	5.8	5.3	5.5	6.4	6.4	5.7	-3.3	-2.5	-2.1	-2.2	-2.2	-1.7
Korea	3.0	3.7	3.9	1.3	2.1	3.0	5.4	3.7	3.1	0.8	0.9	1.5
Malaysia	4.7	5.0	4.9	2.1	3.5	4.5	3.8	4.4	4.0	-3.9	-3.5	-3.0
Mongolia	11.7	11.0	8.0	10.5	13.7	12.0	-31.0	-24.6	-18.2	-4.0	-2.8	-2.3
Philippines	7.2	6.9	7.3	2.9	4.3	4.0	3.5	3.5	2.9	-1.4	-1.8	-1.6
Singapore	4.1	3.4	4.0	2.4	1.8	1.4	18.4	18.0	18.0	1.1	-0.3	0.2
Sri Lanka	7.3	7.2	7.4	6.9	5.4	6.5	-3.3	-2.5	-2.0	-5.9	-5.5	-5.2
Taiwan	2.1	3.2	3.8	0.8	1.3	1.9	11.7	11.0	10.2	-1.5	-1.4	-0.8
Thailand	2.9	1.8	4.1	2.2	2.3	2.8	-0.7	2.3	-1.1	-1.8	-1.2	-1.8
Vietnam	5.4	5.7	5.9	6.6	5.8	7.2	4.9	3.7	2.5	-5.3	-4.5	-4.0
Latin America	2.4	2.1	2.8	7.3	8.9	10.2	-2.6	-2.8	-2.5	-3.2	-3.6	-2.8
Argentina	4.9	1.0	1.5	10.6	NA	30.5	-0.6	-0.5	-0.4	-2.4	-3.1	-2.3
Brazil	2.3	1.3	1.8	6.2	6.1	5.9	-3.7	-4.0	-4.1	-3.3	-3.7	-2.8
Chile	4.0	3.5	4.5	1.8	3.2	3.1	-3.5	-3.8	-4.0	-0.3	-0.4	-0.4
Colombia	4.3	4.6	5.0	2.0	2.3	3.4	-3.3	-3.5	-3.6	-1.4	-1.3	-0.7
Costa Rica	3.2	3.5	4.0	5.2	3.6	4.6	-5.5	-5.7	-5.9	-6.5	-7.0	-7.5
Dominican Republic	4.1	4.5	4.5	4.8	4.0	4.6	-4.4	-4.8	-5.0	-4.1	-4.0	-4.2
Ecuador	4.0	4.1	4.5	2.7	2.9	3.1	-1.8	-2.2	-1.5	-2.4	-1.9	-1.5
El Salvador	1.8	2.2	2.5	0.8	0.8	1.8	-6.1	-6.3	-5.7	-4.2	-4.1	-3.7
Mexico	1.1	3.3	4.0	3.8	4.2	3.6	-1.8	-2.1	-1.8	-2.4	-3.5	-2.5
Panama	8.0	6.2	5.5	4.0	2.7	2.8	-10.2	-10.0	-9.2	-3.5	-3.0	-3.0
Peru	5.0	5.7	6.2	2.8	2.7	2.5	-5.2	-5.6	-1.5	0.8	0.0	0.0
Venezuela	1.5	-1.0	1.9	38.5	62.5	82.1	3.3	4.0	5.1	-11.9	-11.1	-10.3
Europe	1.9	1.7	2.9	5.3	5.0	5.0	-1.3	-0.7	-1.1	-2.2	-2.4	-3.6
Bulgaria	0.9	1.5	2.5	0.9	-0.2	2.5	2.1	-0.8	-0.5	-1.9	-2.0	-1.2
Croatia	-1.0	0.7	1.5	2.2	0.6	2.8	0.2	0.0	-0.5	-5.5	-5.5	-5.0
Czech Republic	-0.9	1.9	2.5	1.4	0.8	2.0	-1.4	1.1	0.8	-2.4	-2.9	-2.9
Hungary	1.1	2.1	1.5	1.7	0.7	2.9	2.1	2.6	2.0	-2.6	-2.9	-2.9
Kazakhstan	6.0	5.0	6.0	5.7	6.0	5.7	-0.2	1.0	1.4	3.2	2.4	2.2
Poland	1.6	3.4	3.6	0.9	1.0	2.7	-1.5	-2.5	-3.6	-4.2	5.7	-2.3
Romania	3.5	3.0	3.4	4.0	2.4	3.4	-1.1	-2.5	-4.2	-2.5	-2.3	-2.3
Russia	1.3	1.0	2.3	6.8	6.0	5.2	1.6	1.8	1.2	-2.0	-4.4	-4.9
Serbia	2.5	1.2	2.0	7.9	4.9	6.3	-5.0	-4.9	-5.5	-7.2	-5.5	-5.0
Slovakia	0.9	2.0	2.5	1.4	0.3	1.5	2.4	2.8	2.6	-2.7	-3.3	-2.7
Turkey	4.0	2.3	3.5	7.5	7.7	7.4	-7.8	-5.2	-5.3	-1.2	-2.8	-3.2
Ukraine	-0.1	-2.4	2.1	-0.3	4.2	5.8	-9.3	-7.4	-5.2	-6.1	-4.1	-3.2
Africa/Mideast	3.8	4.6	5.3	4.3	4.4	5.0	12.7	10.7	8.4	1.6	1.0	-0.7
Bahrain	4.3	4.0	4.1	3.3	2.3	2.0	5.3	2.4	-1.5	-2.2	-3.3	-5.5
Egypt	2.0	2.9	3.4	9.5	9.2	7.1	-1.7	-1.3	-2.2	-11.6	-10.9	-9.4
Ghana	7.4	4.6	6.5	11.7	12.7	7.7	-12.7	-13.4	-13.3	-10.8	-8.9	-7.4
Iraq	3.1	10.4	11.6	1.9	3.4	6.0	13.5	13.8	12.8	-0.6	2.0	2.9
Israel	3.2	3.4	3.5	1.5	1.2	3.0	1.2	1.9	1.7	-2.7	-3.0	-2.5
Jordan	3.0	4.0	4.5	5.5	4.0	5.0	-15.2	-14.2	-11.9	-8.2	-10.1	-9.9
Kenya	5.1	5.5	6.1	5.4	7.1	6.7	-7.8	-7.6	-7.5	-7.0	-5.5	-4.5
Kuwait	4.3	3.9	3.9	2.6	3.1	4.5	51.0	49.5	47.8	26.8	27.0	21.0
Lebanon	1.4	2.0	2.4	2.1	4.4	5.0	-4.5	-5.3	-6.0	-10.0	-9.3	-8.7
Nigeria	6.5	6.6	6.4	8.5	8.8	10.6	7.0	4.4	2.6	-2.6	-2.9	-2.9
Oman	5.7	5.2	4.7	2.1	1.9	3.0	10.4	8.2	6.4	9.5	8.0	5.8
Qatar	5.6	5.9	6.1	3.1	2.5	3.5	30.1	25.8	20.9	8.2	4.3	1.2
Saudi Arabia	3.7	4.2	6.1	3.5	3.5	4.1	18.2	13.7	9.3	7.4	5.1	0.4
South Africa	1.9	2.4	2.9	5.8	6.1	5.7	-5.8	-4.7	-4.2	-4.2	-4.2	-4.3
Tanzania	6.8	7.0	8.1	7.9	6.6	6.8	-10.2	-14.1	-12.4	-5.0	-5.2	-5.9
UAE	3.7	4.0	4.0	1.5	1.3	1.6	26.2	21.4	17.0	NA	NA	NA
Uganda	5.0	5.2	5.5	5.5	6.0	6.1	-12.0	-13.9	-14.9	-3.4	-3.3	-3.5
Zambia	6.0	6.4	6.3	7.0	7.0	7.3	0.2	-1.0	-1.5	-7.1	-5.9	-5.1
Total	4.5	4.5	4.9	4.7	4.8	5.3	1.9	1.8	1.3	-2.1	-2.3	-2.3

Sources: National sources and Citi Research forecasts

Sovereign Ratings

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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. All economic and fiscal forecasts are consistent with those published in Citi's monthly "*Global Economic Outlook and Strategy*" or other research. We do not aim to make a judgment on the financial market implications of ratings changes, except in so far as we expect any such market implications to affect other sovereign ratings.

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

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

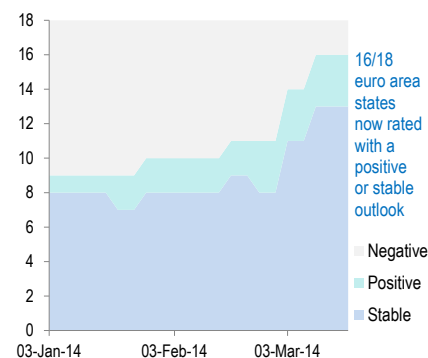
Country	S&P Ratings				Moody's Ratings			
	Current Rating	Current Outlook	Citi Near-term (Up to 9 Months) Forecast Rating	Citi Longterm (Next 2-4 Years) Forecast Rating & Outlook	Current Rating	Current Outlook	Citi Near-term (Up to 9 Months) Forecast Rating	Citi Longterm (Next 2-4 Years) Forecast Rating & Outlook
US	AA+	Stable	AA+ (Stable)	AA+	Aaa	Stable	Aaa (Stable)	Aaa
Canada	AAA	Stable	AAA (Stable)	AAA	Aaa	Stable	Aaa (Stable)	Aaa
Japan	AA-	Neg	AA- (Neg)	A+ ↓	Aa3	Stable	Aa3 (Stable)	A1 ↓
Germany	AAA	Stable	AAA (Stable)	AAA	Aaa	Stable	Aaa (Stable)	Aaa
France	AA	Stable	AA (Stable)	AA	Aa1	Neg	Aa1 (Neg)	Aa2 ↓
Italy	BBB	Neg	BBB (Neg)	BBB- ↓	Baa2	Stable	Baa2 (Stable)	Baa3 ↓
Spain	BBB-	Stable	BBB- (Stable)	BBB ↑	Baa2	Pos	Baa2 (Pos)	Baa1 ↑
Austria	AA+	Stable	AA+ (Stable)	AA+	Aaa	Stable	Aaa (Stable)	Aaa
Belgium	AA	Stable	AA (Stable)	AA	Aa3	Stable	Aa3 (Stable)	Aa3
Finland	AAA	Stable	AAA (Stable)	AAA	Aaa	Stable	Aaa (Stable)	Aaa
Greece	B-	Stable	B- (Stable)	B-	Caa3	Stable	Caa3 (Stable)	Caa3
Ireland	BBB+	Positive	A- (Stable) ↑	A- ↑	Baa3	Positive	Baa2 (Stable) ↑	A3 ↑↑↑
Netherlands	AA+	Stable	AA+ (Stable)	AA+	Aaa	Stable	Aaa (Stable)	Aaa
Portugal	BB	Neg	BB+ (Pos) ↑	BBB- ↑↑	Ba3	Stable	Ba2 (Pos) ↑	Baa3 ↑↑↑
UK	AAA	Neg	AAA (Stable)	AAA	Aa1	Stable	Aa1 (Pos)	Aaa ↑
Switzerland	AAA	Stable	AAA (Stable)	AAA	Aaa	Stable	Aaa (Stable)	Aaa
Sweden	AAA	Stable	AAA (Stable)	AAA	Aaa	Stable	Aaa (Stable)	Aaa
Denmark	AAA	Stable	AAA (Stable)	AAA	Aaa	Stable	Aaa (Stable)	Aaa
Norway	AAA	Stable	AAA (Stable)	AAA	Aaa	Stable	Aaa (Stable)	Aaa
EU	AA+	Stable	AA+ (Stable)	AA+	Aaa	Stable	Aaa (Stable)	Aaa
ESM	Not rated				Aa1	Neg	Aa1 (Neg)	Aa2 ↓
EFSF	AA	Stable	AA (Stable)	AA	Aa1	Neg	Aa1 (Neg)	Aa2 ↓

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

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Figure 43. Euro Area “Outlooks” (Moody’s)



Sources: Moody's and Citi Research

Figure 44. Upcoming rating calendar

Date	Sovereign	Rating Agency	Current Rating	Current Outlook
28-Mar-14	Austria	S&P	AA+	Stable
28-Mar-14	Estonia	Moody's	A1	Stable
28-Mar-14	Luxembourg	S&P	AAA	Stable
04-Apr-14	Greece	Moody's	Caa3	Stable
04-Apr-14	Slovakia	Moody's	A2	Stable
11-Apr-14	Finland	S&P	AAA	Stable
25-Apr-14	Cyprus	S&P	B-	Stable
25-Apr-14	EFSF	S&P	AA	Stable
25-Apr-14	France	S&P	AA	Stable

Sources: Citi Research, Moody's, S&P

Expected Ratings Issues

Overview — lots of activity in Q1: It has been a busy start to the year for the rating agencies. In a distinct break from 2011-2013, Q1-2014 has already seen 2 upgrades (Ireland, Spain) and a variety of outlooks moved from “negative” to “stable”. In fact, Moody's now rates 16 out of the 18 euro area states with a positive or stable outlook, from just 9 at the beginning of the year (see Figure 43). Our key message is that we think such dynamics can continue given the drop in EMU deficit trends, improving growth data and diminishing systemic EMU risks.

Spain vs. Italy: Spain is on positive outlook by Moody's (which recently *upgraded* the sovereign by one notch to Baa2), indicating the prospect for a further upgrade over the medium term — although given Spain's (still rising) debt to GDP, the rating is likely to be confined to the lower end of the IG spectrum for several years. Conversely, Italy has a weaker growth outlook and a much higher debt stock to service as detailed by Citi economists and the rating agencies. Given concerns about Italy's ability to confront its competitive issues and that political uncertainties have not completely disappeared, we do not expect upgrades of Italy. Over the longer-term, we actually expect downgrade pressure to remain. Based on our economic expectations, this would put Italy on a different rating trajectory to Spain.

Portugal — a return to market is a credit positive: Risks to Portugal's growth outlook are now to the upside and bond yields continue to tumble (10yr Portugal is now around 4.25% from a high of over 7.5% over the last 12 months and an all-time peak of over 16% in early 2012). We now expect that Portugal can and will exit its Troika programme without the need for extra official support. We expect rating agencies increasingly to acknowledge this and, in doing so, we expect an upgrade by Moody's and S&P later this year.

Ireland — successfully auctioning bonds: Moody's upgraded Ireland from Ba1 Stable (sub-IG) to Baa3 Pos (IG) on 17 January. Ireland is now rated Investment Grade by all three rating agencies with a positive outlook by both Moody's and S&P. Since we last published Ireland has also successfully engaged capital markets in a 10yr auction (*Ireland's first auction since 2010 is an important milestone*). We continue to expect another upgrade of Ireland by both agencies later this year.

Greece — we expect bond issuance soon: The Greek banking sector has now accessed capital markets (a 3yr €0.5bn transaction by Piraeus bank). Furthermore, the recent Troika negotiations have removed some bailout hurdles and the improvement in market sentiment and investor confidence is ongoing. The Greek Finance Minister was quoted by Reuters on 26 March saying that Greece is ‘almost ready’ to return to the bond markets and issuance would be “probably after” the European Parliament elections on 25 May. This will likely be viewed positively by the rating agencies and could result in its rating outlooks being revised to positive.

France — outlook still negative: France remains on negative outlook by Moody's which rates France one notch higher than S&P (AA). We agree that downside risks remain and continue to think Moody's will likely rate France Aa2 in the years ahead.

Germany and Austria — now stable by Moody's: Both Germany and Austria had their outlook revised from negative to stable over March by Moody's. We do not anticipate any changes in their ratings over the near or medium term.

UK — Given the strong performance of the UK economy, S&P will likely return its outlook on the UK's AAA rating back to stable in 2014. The next opportunity for this to occur is on 6 June. We also see the growing possibility that Moody's places the UK back onto positive outlook and ultimately upgrades the rating from Aa1 to Aaa.

US — The US is rated AA+ Stable by S&P and Aaa Stable by Moody's and we do not anticipate any change in the US rating over the long term.

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Yield and Spread Forecast Commentary

US: The US yield curve flattened significantly over the past month as the FOMC sent a hawkish signal by revising up rate projections for 2015 and 2016 following its March meeting. Following the meeting, front-end yields sold off and 2y-5y yields are now trading near the top of their 6 month range. On the other hand, 10y note and 30y bond yields were largely rangebound as improving economic data and expectations of a faster Fed hiking cycle were balanced out by concerns over China and Eastern Europe. The market is not yet in line with the Fed's new median expectations, and we believe there is still room for yields to climb higher. We have raised our forecasts across the curve, and our 10y forecasts are currently about 40bps above forwards for Q4 2015.

Core Europe: Citi expects the ECB to cut the refi-rate by 15bp and the deposit rate by 10bp in 2Q14. The ECB are also forecasted to introduce a fixed rate LTRO in 2H14. We expect further loosening of monetary policy to result in front-end yields moving lower. 10yr Bunds are largely caught in between two opposing forces: low HICP (bullish for Bunds) and the prospect of higher UST yields (bearish for Bunds). Overall we expect this to result in 10yr Bunds range trading between 1.6% and 2% in the coming quarters. We expect 10yr OAT-Bund spreads to widen from current levels and average 65bp over the next year.

EMU Periphery: Appetite for EMU peripheral bonds remains strong from both domestics and non-domestic participants and we see few reasons for a change in sentiment. We expect BTP-Bono spreads to be locked in a tight range for the foreseeable future and for 10yr BTP and Bonos spreads to Bunds to reach 150bps. We expect Ireland to conduct further bond auctions in 2H14 and for Ireland-Germany spreads to tighten to 100bp over the next 12months. Portugal is expected to make a clean exit from its Troika programme in May and 10yr PGB-Bund spreads are forecasted to reach 200bp by end-2015. The Greece Finance minister was quoted by Reuters on 26 March saying that Greece is likely to issue bonds soon after the European elections on 25 May. Such events are likely to galvanize further spread tightening in these markets.

UK: Citi expects the MPC to raise policy rates at a steady pace from November 2014 and not pause until 2.5% is reached around end-2015 (previously we anticipated a pause at 2%). This should drive gilt yields higher over the forecast period. The front-end, which currently lacks sufficient risk premium in our view, has significant scope to re-price in the coming quarters. This should drive bear flattening in 2s10s. We also expect LDI demand — which is unlikely to be significantly impacted by the pension reforms announced in the Budget — to continue to be an important driver for the long-end. Further de-risking is likely to mean that 10s30s bear flattens by more than the usual beta would imply. On a cross-market basis, we expect the 10yr gilt-Bund spread to continue to trend wider.

Japan: We expect JGB yields continue to decline close to 50bp in 2Q. The consumption tax hike in April is likely to cause a renewed downturn in the economic recovery and Citi expect additional easing by the BoJ in June or July -- with further increase in JGB purchases. We expect 10yr to remain rich in the curve as the BoJ continues to emphasise this sector in its purchases, while swap spreads are likely to tighten as demand for a hedge against a sell-off in rates decreases. Meanwhile, we expect yields will bottom out in summer if equity markets trend higher and the yen continues to depreciate. In the Citi's scenario, the 10yr JGB yield is expected to cross 1% in spring 2015, although the upward trend of yields probably will be ended again by the another consumption tax hike in 4Q2015.

Figure 45. Interest Rate and Bond Market Forecasts as of 26 March 2014

	Quarterly Average							
	Current	2Q 14F	3Q 14F	4Q 14F	1Q 15F	2Q 15F	3Q 15F	4Q 15F
US								
Policy Rate (Fed Funds) End Quarter	0.25	0.25	0.25	0.25	0.25	0.25	0.75	1.00
3-Month Libor	0.23	0.23	0.23	0.23	0.30	0.65	0.85	1.05
2 Year Treasury Yield	0.43	0.50	0.70	0.90	1.15	1.40	1.60	1.85
5 Year Treasury Yield	1.74	1.85	2.10	2.40	2.60	2.75	2.95	3.10
10 Year Treasury Yield	2.76	2.85	3.10	3.35	3.50	3.60	3.70	3.75
30 Year Treasury Yield	3.60	3.70	3.90	4.05	4.20	4.25	4.25	4.30
2-10 Year Treasury Curve	233	235	240	245	235	220	210	190
2 Year Swap Spread (Swap Less Govt), bp	14	20	20	20	20	20	20	20
10 Year Swap Spread (Swap Less Govt), bp	12	15	15	15	15	15	15	15
30 Year Swap Spread (Swap Less Govt), bp	-3	-5	-5	-5	-5	-5	-5	-5
30 Year Mortgage Yield	4.40	4.45	4.70	5.00	5.25	5.40	5.60	5.70
10 Year Breakeven Inflation	215	240	235	235	240	235	235	235
Euro Area								
Policy Rate End Quarter	0.25	0.10	0.10	0.10	0.10	0.10	0.10	0.10
Overnight Rate (EONIA)	0.17	0.10	0.00	0.00	0.00	0.00	0.00	0.00
3-Month (EURIBOR)	0.32	0.20	0.15	0.15	0.15	0.15	0.15	0.15
2 Year Schatz Yield	0.20	0.05	0.05	0.10	0.10	0.10	0.10	0.10
5 Year Bobl Yield	0.70	0.50	0.50	0.50	0.60	0.60	0.60	0.60
10 Year Bund Yield	1.64	1.65	1.70	1.80	1.90	1.90	2.00	2.00
30 Year Bund Yield	2.51	2.55	2.55	2.55	2.55	2.55	2.60	2.60
2-10 Year Bund Curve	144	160	165	170	180	180	190	190
10 Year BTP-Bund Spread	175	180	170	160	160	150	150	150
10 Year Bono-Bund Spread	170	175	160	140	140	140	140	140
2 Year BTP-Schatz Spread	55	50	50	50	50	50	50	50
2 Year Bono Schatz Spread	52	50	50	50	50	50	50	50
10 Year OAT-Bund Spread	52	65	65	65	65	65	65	65
10 Year Swap Spread (Swap Less Govt.), bp	22	25	20	20	20	20	20	20
10 Year Breakeven Inflation	140	135	140	140	145	145	150	150
Japan								
Policy Rate End Quarter	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10
3-Month Libor	0.14	0.15	0.15	0.15	0.15	0.15	0.15	0.15
2 Year Treasury Yield	0.07	0.05	0.10	0.15	0.20	0.20	0.20	0.20
5 Year Treasury Yield	0.19	0.15	0.20	0.30	0.35	0.40	0.45	0.40
10 Year Treasury Yield	0.61	0.55	0.70	0.85	0.95	1.05	1.15	1.10
30 Year Treasury Yield	1.69	1.65	1.75	1.85	1.90	1.95	2.00	2.00
2-10 Year Treasury Curve	54	50	60	70	75	85	95	90
2 Year Swap Spread (Swap Less Govt.), bp	12	10	12	14	15	15	15	15
10 Year Swap Spread (Swap Less Govt.), bp	18	15	20	22	25	25	30	25
10 Year Breakeven Inflation	119	105	100	100	110	115	115	115
UK								
Policy Rate End Quarter	0.50	0.50	0.50	0.75	1.25	1.50	2.00	2.50
3-Month Libor	0.52	0.55	0.55	1.00	1.55	1.70	2.10	2.55
2 Year Treasury Yield	0.68	0.85	1.30	1.50	1.80	2.10	2.40	2.60
5 Year Treasury Yield	1.97	2.25	2.65	2.75	2.85	2.90	3.05	3.10
10 Year Treasury Yield	2.76	3.00	3.25	3.40	3.50	3.55	3.65	3.70
30 Year Treasury Yield	3.53	3.60	3.80	3.85	3.90	3.95	4.00	4.05
2-10 Year Treasury Curve	208	215	195	190	170	145	125	110
10 Year Swap Spread (Swap Less Govt.), bp	-2	10	15	15	20	20	25	25
10 Year Breakeven Inflation	303	310	320	325	340	345	350	350
Australia								
Policy Rate End Quarter	2.50	2.50	2.50	2.50	2.75	3.25	3.75	4.00
3-Month Libor	2.66	2.60	2.60	2.75	2.95	3.45	4.00	4.25
2 Year Treasury Yield	2.83	2.80	2.95	3.15	3.50	3.70	4.00	4.05
5 Year Treasury Yield	3.53	3.75	3.95	4.10	4.35	4.45	4.65	4.60
10 Year Treasury Yield	4.18	4.40	4.50	4.60	4.70	4.75	4.95	4.95
2-10 Year Treasury Curve	135	160	155	145	120	105	95	90
10 Year Swap Spread (Swap Less Govt.), bp	32	35	40	40	45	45	50	50

Source: Citi Research

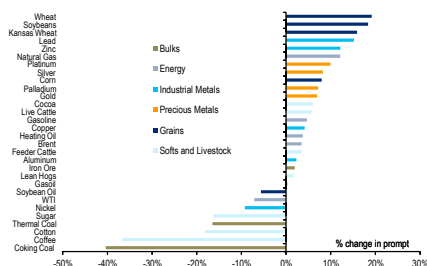
Commodities Market Outlook

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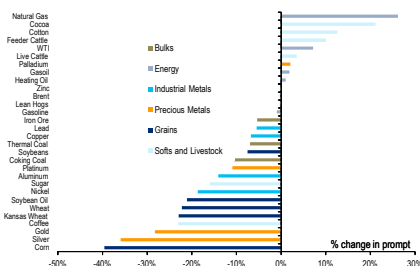
Commodities have outperformed most other asset markets by a wide margin in the first quarter of the year to date, a dramatic change from the prior two years, suggesting a return to the more normal historical lack of correlation that provides an underlying investor rationale for the group. Despite generally neutral-to-bearish fundamental balances and tepid flows in and out of the investment group, two other trends emerged suggesting a return to more normal times. First, the strong negative correlation between the US dollar and commodities has also dissipated and returned to a historically more normal random relationship between the two as prevailed for several years before the middle of the last decade, especially after 2007. Second, the historical blend of some commodities rising and others falling in value, which facilitated the efficiency of rules of rebalancing commodity index baskets, has also come back to the fore. If these trends continue it should re-awaken investor interest in the asset class.

Figure 46. 2012 Nominal Price Change



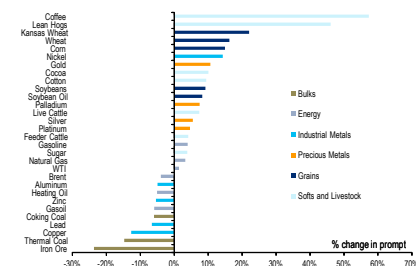
Sources: Bloomberg and Citi Research

Figure 47. 2013 Nominal Price Change



Sources: Bloomberg and Citi Research

Figure 48. 2014 YTD* Nominal Price Change



Sources: Bloomberg and Citi Research, *through 20th March

Of the roughly 27 active contract markets that Citi regularly tracks nearly 20 commodities showed increases in value during Q1 to date, while less than 10 declined and most of those price drops were marginal. Bulks led the charge lower on Asian growth concerns and of the major traded metals, copper declined the most, due to special circumstances in China and the winding down of securitized financings; but aluminum, zinc, gasoil and lead also fell, and there was actually a modest decline in both Brent crude oil and heating oil. Commodity strength in Q1 was in agriculture across the board due to both geopolitical tensions in the Black Sea but more notably the Brazilian drought, nickel due to the Indonesian export ban, and the entire PGM group. Gold also came to the fore and was in the middle of the outperforming pack, as purchasing of the asset increased as a safe haven with the rise in macro risk, especially over the crisis in Ukraine, as well as a result of increased inflationary concerns for food and fuel in emerging markets and in advanced economies.

Oil markets have remained within the same \$106-111/bbl range that has defined the Brent market for six months now. This range has held despite the extreme winter in the US which drained energy inventories across the board, and the Ukrainian crisis injecting a new source of geopolitical tensions to the oil market, one that looks unlikely to be resolved in the immediate future.

Physical crude markets have remained firm with the Asian bid for Atlantic Basin crude barrels still strong; Chinese net crude imports were 10% higher y/y in January and February. Brent flat price and spreads have started to ease in recent weeks as the peak of refinery maintenance season approaches in Europe and Asia, which is reducing the bid for North Sea barrels. Russian refinery maintenance will also increase the amount of Urals (a competing crude to Brent) available which could

further weigh on oil prices. This adds to the impressive 2-m b/d y/y increase in global oil supply seen in February. OPEC crude supply has also moved into y/y surplus, despite ongoing turmoil in Libya, as Iraqi exports have jumped to record highs whilst non-OPEC growth remains robust, led by North America. Some seasonal weakness is expected in April and May, as has been the case over the past few years. Yet structural declines in North Sea crude production and an increased bid from South Korea and China for North Sea continue to support Brent prices. OECD product inventories are low, but weak refining margins indicate a market comfortable with these levels on a combination of relatively sluggish non-OECD demand and comfortable levels of non-OECD inventories. We expect prices to come under more pressure as the year progresses and Iraqi production continues higher and Iranian barrels come back to the market assuming negotiations with the P5+1 continue to progress.

WTI has been receiving support from the continued draw down of crude inventories at the storage hub of Cushing, Oklahoma, due to the new Keystone Gulf Coast pipeline — formerly part of the Keystone XL pipeline — which started at the beginning of this year. But these barrels are making their way to the US Gulf Coast region, where stocks are now building rapidly. While regional refineries are on the cusp of returning from spring maintenance, the next few weeks may see new record stock levels in the PADD III area, which could pressure US Gulf Coast prices downwards, with a knock-on effect on WTI relative to Brent. Come the summer, a new Cushing-to-Gulf Coast pipeline, high refinery runs and increasing exportability of crude could cause the Brent-WTI price spread to narrow as WTI strengthens. While crude supply continues to grow, it looks as though US crude export policy could open up more quickly than thought. Whether this keeps up with the US shale revolution, combined with growing deep water Gulf of Mexico production this year, should drive how heavily WTI discounts against Brent. Citi has a neutral-to-bullish view for WTI into the summer, though 2Q'14 could see a period of weakness as PADD III crude stocks hit new record highs. 4Q'14 looks bearish as fall refinery maintenance sets in, unless lumpy import/export adjustments continue to be made.

Differentiated prices in all three major global gas markets this winter should continue in the rest of the year, illustrating the transport friction that still exists in this increasingly global market. US gas prices, as pointed out below, should stay elevated because of a multi-year low in gas inventories after a cold winter. In contrast, a mild winter in Europe is leaving behind significantly higher-than-normal gas inventories so that, despite the tension in Ukraine causing a brief price spike, much of the forward curve is now below even the pre-Ukrainian crisis low. Gas demand should fall y/y, from 520-bcm/yr in 2013 to 503-bcm/yr in 2014, due to declining gas demand for power generation and industrial uses. In particular, rising renewables generation in a market with flat-to-lower electricity demand growth reduces the need for both gas- and coal-fired generation. The decline in European and Asian coal prices, having fallen below the \$80/ton threshold, also puts downward pressure on European gas prices, as gas remains uncompetitive as a fuel for power generation. However, the seeming divergence between European and global LNG prices this winter could be changing.

North American natural gas inventories continue to decline due to the lingering cold, where some locations are reaching depletion levels, and the prospect of refilling gas storage becomes harder the further that gas inventories fall. Prices need to be high to cut demand and encourage production. However, prices have fallen in the last few weeks due partly to low gas demand for power generation and the belief that this could continue through spring and summer. Some also believe that production could rise significantly. However,

the market might be ignoring the impact of sharply lower Northeast prices in spring/summer on keeping regional gas demand high. The same Northeast region that is expected to provide nearly all of the robust production growth needed is also constrained by lack of pipeline takeaway capacity. Hence, with demand cuts likely not as deep as expected and production growth not as strong as needed, prices would likely have to edge higher again to encourage storage refill.

Global LNG prices surged in winter to nearly \$20/MMBtu but that was on thin trading, coinciding with a bulge in spot Chinese imports. Prices have since come off and the decline is expected to continue. Q2'14 forwards of the Japan-Korea Marker, a global LNG benchmark, are now averaging ~\$16/MMBtu and the summer strip in the mid-\$15 range. Japan's Nuclear Regulatory Authority has accelerated inspection of two nuclear plants and it is possible that after these two plants come online in late Q2/early Q3, other nuclear units could come back in trios in successive quarters. Although oil should initially be displaced, lower LNG demand from Japan and Europe should put a drag on the global LNG market. Although reservoir levels in Brazil are low, which ordinarily should raise LNG imports, the election later this year could prompt the government to keep energy prices weaker by keeping hydro generation running, but at the expense of further depleting reservoir levels, with spillover effects into 2015.

Growing Chinese macro concerns over the past month finally impacted the industrial metals complex, with copper the metal most in the firing line. Concerted shorting of both the SHFE and LME copper market saw dramatic price declines, with LME prices falling by 10% between March 7th and March 12th, while SHFE prices fell by 11% over the same period. Indeed, SHFE open interest also increased by 30% between those dates, reflecting the dramatic surge in fund short interest. The major concern for the copper market has been the continued viability of collateralized copper financing deals and whether significant volumes of collateralized metal would reappear in the marketplace. The concerns have been driven by a number of factors including the local attempts to clamp down on shadow banking, China's first corporate bond default by the solar cell producer Shanghai Chaori prompting growing corporate credit concerns, and lastly the engineered weakening of the RMB/USD exchange rate. However, at the time of writing we are not aware of any copper financing deals being broken, which is not surprising given that letters of credit associated with such deals typically last between 90-180 days, meaning such deals are not subject to any form of 'margin call'. We believe the selloff is to some extent overdone, and expect a modest recovery from this week's lows as shorts are taken off. However, we now expect copper to remain in the \$6,400-6,800/t range over the next month as China concerns continue to unfold.

Nickel has been the one positive stand in the base space over recent weeks, with prices rallying by over 16% between January 12, the date of the start of the Indonesian ore export ban, and year-to-date highs of \$16,385/t seen during trading on March 19. Citi has been an almost lone voice consistently predicting firstly, the high probability of a restrictive ore export ban being introduced and adhered to; secondly, a market moving in deficit from 2015; and thirdly a sharp uplift in nickel prices in 2014. So far, two out of the above three expectations appear to have occurred. We continue to expect more price upside to come as the ore ban increasingly constrains Chinese NPI production into the second half of the year.

Geopolitics and macro risk have been an increasingly supportive influence on gold investment sentiment and thus prices over the last two weeks, with COMEX levels trading up to \$1,392/oz. in mid-March. Underlying the geopolitical environment has been a supportive physical gold market, particularly with regards to China where turnover on the Shanghai gold exchange has picked up steam from

the early month lows, suggesting still robust retail investor/jewellery demand for the precious metal. Additionally, in the week to March 14, we saw the largest net physical inflow into gold ETFs since November 2012 of ~12.35 tonnes. However, despite this generally positive environment, we remain cautious on the short-term outlook, forecasting prices to average \$1,330/oz. over the next quarter. Indeed, the March FOMC meeting and announcement of a further \$10Bn of asset purchase tapering brought a positive US economy back into investor focus, resulting in a sharp pull back in yellow metal prices on the back of renewed dollar strength. However, we expect continued geopolitical tensions and strong physical demand from China in particular to continue to provide some market support. In contrast to gold, palladium in particular has found renewed strength this month, trading up to \$799/oz. on March 21st, prompted largely we believe by the rush to launch two new physically backed South African listed ETFs before the end of March. The launch of these new ETF products into a market with limited available above-ground stocks, and on-going South African production disruption due to strikes (the current wave of strikes in the PGMs sector began on January 25 and show little sign of imminent settlement), combined with very strong underlying auto sector demand growth, present a very bullish price case for the metal.

Iron ore prices plummeted in early March, spurred by concerns following the default of Shanghai Chaori Solar and poor trade data. The sell-off fed into a weak physical market, as unseasonably dry weather in Western Australia saw no material export disruption since the start of the year. In the coming months, supply should increase further due to expansions at the top three Australian miners, while Chinese demand is expected to continue to weaken. Thermal coal prices have also sold off, moving below the lows hit in 2013, as Citi anticipated. The market remains weak due to strong supply growth from Australia as producers seek to lower unit costs and the impending resumption of exports from Colombia's Drummond mine. Spring should see the US market loosen, while the Chinese market continues to weaken. The keys to watch going forward are: 1) whether Indonesia manages to halt the growth of its exports; 2) how much and when Indian demand picks up.

Price strength for staple grains can persist in the short-term but should give way to marked weakness later in 2Q and persist through 2H'14 assuming normal US weather. Soft commodities such as Arabica coffee and cocoa should remain in an elevated trading range in the quarters ahead on deficit supply/demand balances. Robust US export sales, transport congestion on grain shipments, poor winter wheat ratings and Brazilian drought conditions have bid cereal prices this quarter. Levels could trade higher in the short-term until supply makes its way to market. To be sure, US quarterly stocks that print at the end of this month could surprise to the upside for corn at north of 7-bn bushels, suggesting ample domestic inventories. Furthermore, private surveys already indicate the United States Department of Agriculture (USDA) has grossly underestimated the size of spring sowing for the row crops including corn (92-mn agency versus consensus 93.5-mn) and especially soybeans (79.5-mn agency versus ~82-mn Citi and consensus).

Strong planting conditions in the US where farm-belt drought conditions are expected to dissipate and improve could begin more heavily weighing on old-crop and harvest price outlooks on potentially record levels of output for corn and soy this year. As the Brazilian oilseed reaping advances, it should materialize into a large loading program this May/June which should continue to discount LatAm basis and possibly lead to cancellation of US cargoes. Corn and wheat market strength has been buttressed by Black Sea geopolitics but there have not been meaningful disruptions of physical grains trade for the time being—rather it is an impetus for consumers to buy US supplies which should start being sourced

more heavily from South America in coming months. Emerging market grown softs including cocoa and coffee are likely to trade higher this year. We expect premium Arabica coffee prices to average between \$1.50-\$2.25/lb over the next several quarters (or up 50-100% year/year) as crop damage in Brazil (which accounts for a third of global output) has deteriorated since January and during the February flowering stage. Cocoa balances appear in deficit for 2013/14 following a hefty old-crop shortfall and we expect prices to trade north of \$3,000/MT on ICE for most of this year as global chocolate demand and grindings keep surprising to the upside.

Source: Citi Research, *subject to revision; please see www.citivelocity.com for individual market reports (i.e. cocoa, cotton prices updated in early March, etc.)

[illegible]

Figure 50. Citi Global Economics Team

For Informational Purposes Only

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Source: Citi Research.

Notes

Notes

Appendix A-1

Analyst Certification

The research analyst(s) primarily responsible for the preparation and content of this research report are named in bold text in the author block at the front of the product except for those sections where an analyst's name appears in bold alongside content which is attributable to that analyst. Each of these analyst(s) certify, with respect to the section(s) of the report for which they are responsible, that the views expressed therein accurately reflect their personal views about each issuer and security referenced and were prepared in an independent manner, including with respect to Citigroup Global Markets Inc and its affiliates. No part of the research analyst's compensation was, is, or will be, directly or indirectly, related to the specific recommendation(s) or view(s) expressed by that research analyst in this report.

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