

# Euro Economics Weekly

## What do the US Pickup and China Slowdown Mean for Euro Area Growth?

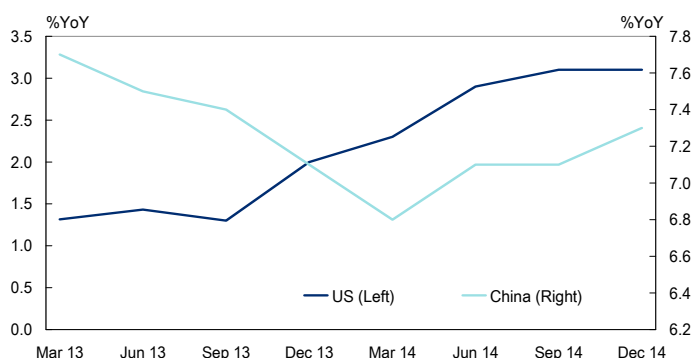
- Net exports still offer the best hope for growth in the euro area. We find that the expected pickup in US growth and slowdown in Chinese growth probably leave intact the growth prospects for euro area exports. The changes to the US and Chinese growth trajectory leave the joint contribution of US and Chinese growth to world GDP growth broadly unchanged at 1.3-1.5pp/year in 2013-14, similar to 2012. What is more, the US is still a much more important export sales market than China for the euro area as a whole, as well as all 12 euro area countries we consider. We estimate that the response of euro area GDP or export growth to shocks to US growth has also been higher than for shocks to Chinese growth.
- Across euro area countries, the importance of exports to the US vs China is highest for Ireland, and lowest for Finland, France, and Germany. We also estimate Ireland to be most sensitive to shocks to US growth. Of the other periphery countries, Greece has the highest export exposure to the US, while Portugal and Spain have relatively low exposure. In addition to its comparatively large exposure to China, Germany's external prospects are also threatened by pressures on its competitiveness from the large yen depreciation and rising labour costs.

Figure 1. Citi Market Forecasts

	\$/€	Euro Repo	10-yr Bunds	£/€	U.K. Bank Rate	10-yr Gilt-Bund	SKr/€	SEK Policy Rate	NOK/€	NOK Policy Rate	SFr/€	CHF Policy Rate	CHF Spread vs Bunds
4Q 13	1.29	0.25	1.50	0.88	0.50	76	8.87	1.00	7.94	1.50	1.25	0.00	-70
2Q 14	1.29	0.25	1.50	0.88	0.50	91	8.82	1.00	7.86	1.50	1.26	0.00	-73

Source: Citi Research

Figure 2. US and China – Real GDP Growth (%YoY), 2013 – 2014F



Sources: BEA, China National Bureau of Statistics and Citi Research

**Ebrahim Rahbari**

+44-20-7986-6522

ebrahim.rahbari@citi.com

**Guillaume Menuet**

+44-20-7986-1314

guillaume.menuet@citi.com

**Giada Giani**

+44-20-7986-3281

giada.giani@citi.com

**Michael Saunders**

+44-20-7986-3299

michael.saunders@citi.com

**Ann O'Kelly**

+44-20-7986-3297

ann.okelly@citi.com

With thanks to Alexander Demyanets

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or jan.maguire@citi.com

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Ebrahim Rahbari



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## US, China and Euro Area Growth

**The expected pickup in US growth and slowdown in Chinese growth leave intact prospects for euro area export growth.**

**Overall, these changes leave the joint contribution of US and Chinese growth to world GDP broadly unchanged.**

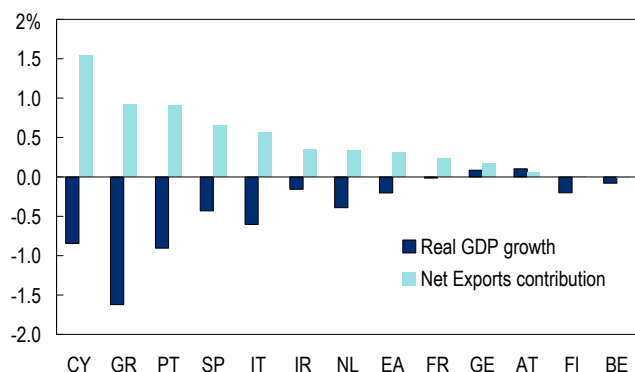
**The US is still a much more important export sales market than China.**

**Across euro area countries, Ireland is likely to benefit most from the changes in external dynamics, while Germany is probably most vulnerable.**

US growth is expected to pick up in the course of this year, while Chinese growth is slowing more quickly than expected.<sup>1</sup> Given that net trade has been a major factor to moderate the euro area recession and remains its best hope for generating positive growth in the quarters ahead, we investigate the implications of the changes in external dynamics for growth of euro area GDP and exports. We find that the expected upturn in US growth and the slowdown in Chinese growth probably leave the prospects for externally-driven growth in the euro area intact.<sup>2</sup>

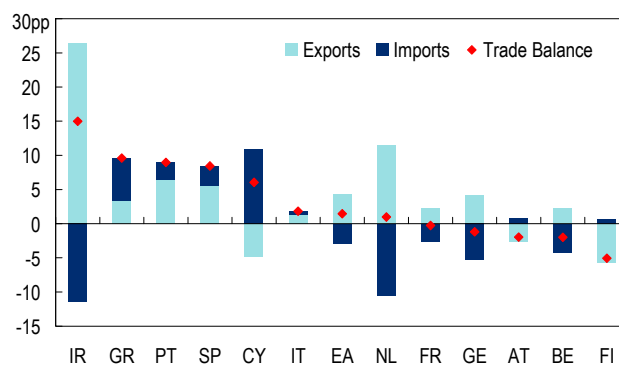
First, the US growth pickup and the Chinese slowdown are relatively modest — the joint contribution from the US and China to world GDP growth is expected to be 1.3-1.5pp in 2013-14, just as in 2012, and China accounts for a relatively constant three fifths of the joint contribution. Second, the US is a much bigger source of export demand for the euro area than China currently — more than twice as large in 2012 and having grown more quickly over the last few years. We find empirically that shocks to US growth have tended to affect growth of euro area GDP and exports more strongly than Chinese growth shocks. Potentially associated rises in Treasury yields or commodity prices are found to have had limited effects on euro area growth since 2000. However, it is possible, perhaps plausible, that continued euro strength (at least partly due to yen weakness) and weaker-than-expected EM (not just China) growth could cap external growth prospects for the euro area. Ireland looks set to benefit most from a change in the external dynamics, while Germany looks most vulnerable.

**Figure 3. Selected Countries — Average Quarterly Real GDP Growth and Net Exports Contribution (%QQ), 2011 Q2 — 2013 Q1**



Note: Exports are exports of goods and services. Exports and GDP are in constant 2005 EUR.  
Sources: Eurostat and Citi Research

**Figure 4. Selected Countries — Change in Trade Balance (% of GDP), 2008-2013**



Note: Trade balance is difference of exports and imports of goods and services, computed as four quarter sums relative to GDP.  
Sources: Eurostat and Citi Research

**Net exports have added roughly 1pp annually to real GDP growth in the euro area in recent years.**

The positive contributions of net exports to GDP have substantially moderated the recent euro area (EA) recession. Since the post-financial crisis trough in Q2 2009, net trade has on average added 0.2pp each quarter (0.9pp annualised) to EA GDP growth, and the contribution has been slightly higher than that over the last 8-10 quarters. Without net trade, the EA recession of the last 8 quarters would thus have roughly doubled in depth (see Figure 3). In Q2, net trade probably made a sizable contribution to EA GDP, too (we estimate a contribution of 0.2pp). Positive net trade

<sup>1</sup> See e.g. [U.S. Economics Weekly: Market and Policy Comments - Fundamentals Overtaking Fiscal Headwinds](#), Robert DiClemente et al, 2 Aug 2013, Citi, and [China Macro View - Outlook for 2H: Tighter Credit to Extend the Downtrend](#), Shuang Ding et al, 8 Jul 2013, Citi.

<sup>2</sup> See also [Euro Economics Weekly - German Exports — Down But Not Out](#), Ebrahim Rahbari et al, 19 Jul 2013, Citi, and [Euro Economics Weekly - Spain's External Rebalancing](#), Giada Giani et al, 14 June 2013, Citi

contributions have driven the EA's overall trade balance (for goods and services) to 2.3% of GDP for the four quarters to Q1 2013 (in current euros), from roughly balanced trade in 2008.<sup>3</sup>

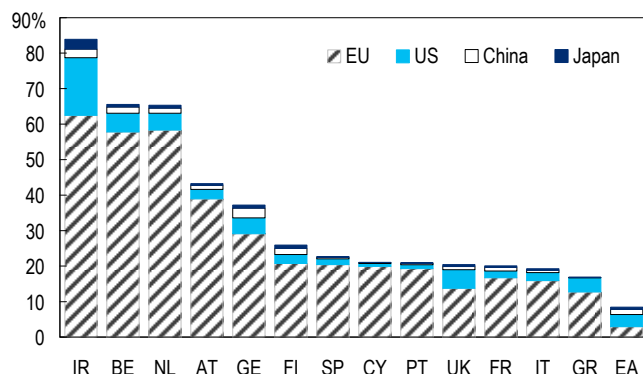
Some of the contribution of net trade has been due to import compression, but export growth has played a major role (see Figure 4). Exports to the US and China are an important — but by no means dominant — source of export demand for the EA. Of the two, the US is by some distance the more important export market. For the four quarters ending in Q1 2013, exports to the US account for 13% of total EA exports outside of the euro area (3.4% of EA GDP), and exports to China for 5.5% (1.5%).

**Euro area (EA) exports to the US are more than twice as large as EA exports to China, and have grown more quickly in recent years.**

**The relative importance of US exports to Chinese exports is highest for Ireland and Greece, while it is lowest for Finland, France, and Germany.**

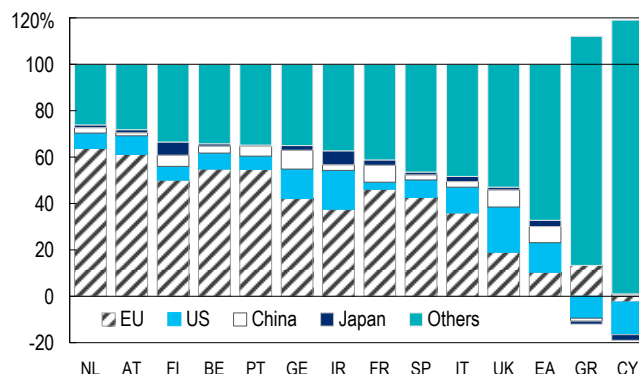
Exports to the US are larger than exports to China for *all* 12 EA countries we consider.<sup>4</sup> The relative importance of exports to the US and to China varies quite significantly across EA countries — for Greece, exports to the US were ten times the value of exports to China in 2012 (in current euros) and in Ireland more than five times, whereas in Germany, France or Finland, the ratio was less than 1.5.<sup>5</sup> Among the EA periphery countries, Greece was also the country with the largest exports relative to GDP except for Ireland. The bilateral EA trade *balance* of the euro area is negative with respect to China to the same tune as it is positive for the US (-0.7% of GDP vis-à-vis China and 0.8% of GDP vis-à-vis the US for the four quarters up to Q1), even though it has improved vis-à-vis both countries in recent years (i.e. grown more positive vs the US and less negative vs China).<sup>6</sup>

**Figure 5. Selected Countries — Exports by Destination (% of GDP), 2013 Q1**



Note: 4Q sum of exports of goods and services and GDP in current EUR. For Portugal, goods exports only (from IMF DOTS). EA data exclude intra-EA trade.  
Sources: Eurostat, IMF DOTS and Citi Research

**Figure 6. Selected Countries — Contribution to Export Growth by Destination (% of total), 2011 Q1-2013 Q1**



Note: 4Q sum of exports of goods and services and GDP in current EUR. For Portugal, goods exports only (from IMF DOTS). EA data exclude intra-EA trade.  
Sources: Eurostat, IMF DOTS and Citi Research

<sup>3</sup> See also [Global Economics View - Slow trade, fast trade transformation](#), Ebrahim Rahbari and Deimante Kupciuniene, 11 Mar 2013, Citi

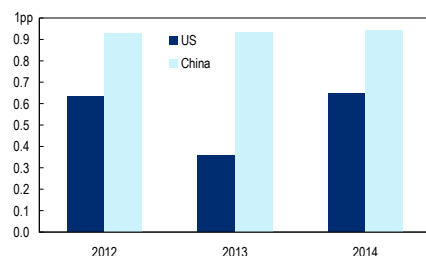
<sup>4</sup> These are Austria, Cyprus, Finland, France, Germany, Greece, Ireland, Italy, Netherlands, Portugal, Slovenia, and Spain.

<sup>5</sup> Here we include exports to Hong Kong as exports to China. For Chinese exports alone, the difference is even more dramatic.

<sup>6</sup> The interpretation of bilateral trade balances are subject to some pitfalls. For an illustration for the case of the US-China bilateral trade balance, see Xing, Y (2011), "How the iPhone widens the US trade deficit with China", voxu.org, 10 April 2011.

**US growth and China slowdown are likely to leave the joint US-China contribution to world GDP growth relatively stable**

**Figure 7. Selected Countries — Contribution to Global Real Growth (pp), 2012-14**



Sources: National Sources and Citi Research Forecasts (as Jul-13)

**We use a VAR model to estimate the effect of US and Chinese growth shocks on euro area growth. We find that:**

- i) **Both shocks have substantial effects on euro area growth, particularly in recent years**
- ii) **The effects of shocks to US growth are larger than for Chinese growth shocks.**

Looking ahead, the growth outlook for the US is brightening, while Chinese growth is slowing. After a downward revision for the recent past, Q2 real GDP growth in the US picked up to 1.7%SAAR, and our Citi colleagues expect it to rise at an annualised rate approaching 3% in H2 2013. Meanwhile, growth in China slowed to 7.5%YY in Q2 and is likely to approach a 7%YY rate in H2, according to our colleagues in China (see Figure 2 on the Front Page). These changes in trend are likely to affect euro area countries in various ways, including through changed trade prospects. But several factors are worth noting:

First, the changes in the US and Chinese growth trajectory are rather modest on an annual basis. After the recent upward revision of US GDP growth for 2012 to 2.8%, the US contribution to world GDP growth is in fact expected to drop slightly from 0.6pp in 2012 to 0.4pp in 2013, but to rise back up to 0.6pp in 2014.<sup>7</sup> In China, despite the ongoing slowdown, the contribution to world GDP growth is expected to remain pretty constant — and high — at 0.9pp per year, leaving the joint US-Chinese contribution at 1.3-1.5pp/year each year in 2012-14.

Second, it is worth noting that for the euro area, the contribution of exports to the US to the growth of total exports in recent years has already been much larger than the contribution of exports to China — in fact, in nominal terms, exports to China barely outgrew total EA exports over the last two years. In recent quarters, the growth in EA exports to both countries has fallen quite sharply, but export growth to the US has generally outperformed exports to China.

We use a vector auto regression (VAR) approach to more systematically consider the impact that shocks to Chinese and US growth have on real GDP growth in the euro area.<sup>8</sup> According to our estimates, **shocks to both US and China growth have substantial effects on euro area growth, but the effect of US growth shocks tend to be somewhat larger.** We estimate that a 1pp shock to US real GDP growth has tended to raise EA growth by 1.3pp after four quarters during our sample (2000-2013 Q1), while the effect of a 1pp shock to Chinese growth has on average been about 0.9pp.<sup>9</sup> We stress that the model we use is rather simple, and that it is likely that the estimated responses will also capture other shocks not explicitly included in the model. We therefore consider the quantitative results as indicative rather than definitive, even though the results we highlight qualitatively hold across various specifications and time samples.

Subject to these caveats, **our results also indicate that the effects of US and Chinese shocks on EA growth have risen over time.** For the pre-crisis sample (estimated for 2000-2006 data), our results suggest that shocks to both US and Chinese growth raised EA growth by much lower amounts than in the full sample, and the effect of US and Chinese shocks in the pre-crisis period were quite similar in size. In the 2007-2013 period, the effect of both types of shocks was much larger,

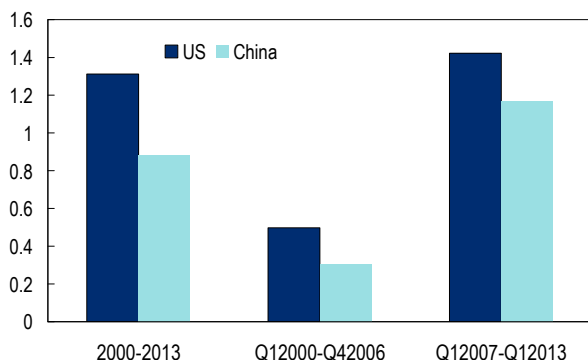
<sup>7</sup> In terms of real GDP at market exchange rates.

<sup>8</sup> Our approach relies on a three variable first-order structural VAR of quarterly real GDP growth in the US, China and the euro area (in that order). We identify shocks through a Cholesky decomposition and the sample is Q1 2000 to Q1 2013. In terms of results, we mainly focus on the cumulative four quarter impulse responses to individual shocks. For a similar approach, see [Emerging Markets Macro and Strategy Outlook - Tug O' War: China And US\\*](#), Guillermo Mondino et al, 22 Jul 2013, Citi.

<sup>9</sup> Note that even a cumulative response of more than 1pp does not mean that, say, US shocks have larger effects on EA growth than shocks to EA growth themselves. The 1pp shock is only the initial impulse, which gets propagated over time, including through the interaction with the other variables (for instance, a shock to EA growth affects US growth which in turn affects EA growth, etc). In our regressions, we tend to find that shocks to the EA growth have larger effects on EA growth over time than shocks to US or Chinese growth (in our baseline, the estimated effect over four quarters to a 1pp shock in EA growth was 1.6pp).

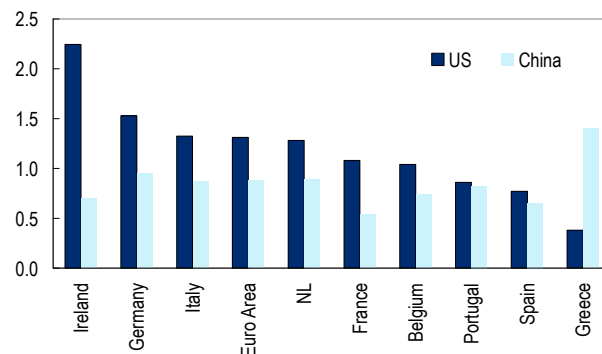
reaching 1.1pp and 0.8 for US and Chinese shocks, respectively. The change in the sensitivity to external shocks is rather intuitive, as the large degree of slack in the EA economy post-financial crisis implies that external impulses have been much more powerful in boosting GDP growth than in the pre-crisis period.

**Figure 8. Euro Area — Estimated effect of a 1pp shock to US and Chinese growth on Euro Area Growth (%), 2000-Q1 2013**



Note: Estimates are based on a three-variable first-order VAR of US, Chinese and EA real GDP growth. Shocks are identified through a Cholesky decomposition and effects are the cumulative impulse responses after four quarters.  
Sources: Eurostat and Citi Research

**Figure 9. Selected Countries — Estimated effect of a 1pp shock to US and Chinese growth on Real GDP Growth (%), 2000-Q1 2013**



Note: Estimates are based on a three-variable first-order VAR of US, Chinese and individual EA country real GDP growth. Shocks are identified through a Cholesky decomposition and effects are the cumulative impulse responses after four quarters.  
Sources: Eurostat and Citi Research

**As expected, the effects of US and Chinese growth shocks are larger on euro area countries which are more open**

**The relative importance of US shocks vs Chinese shocks is highest in Ireland, but is also high in Germany according to our estimates**

**Effects of US and Chinese growth shocks on euro area exports are much larger than the effects on overall GDP growth**

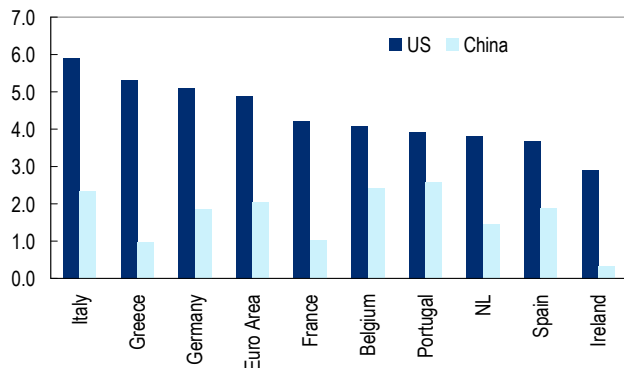
Results vary somewhat across countries, but the effect of US shocks on growth is larger than for Chinese shocks in most individual countries.<sup>10</sup> For the latter sample period, there are a number of countries for which the effect of Chinese shocks on growth was larger. The estimated responses are also generally larger for countries with larger degrees of trade openness (as measured by the sum of exports and imports relative to GDP), such as the Netherlands, Ireland and Germany, particularly for the responses to US shocks. Across the 9 countries we consider, except for one outlier (Greece, see also footnote 10), Germany's sensitivity to Chinese growth shocks is the largest — signifying a roughly 0.9pp increase in German GDP in response to a 1pp Chinese growth shock. This is, of course, consistent with the fact that Germany's exports to China relative to GDP are relatively large compared to other EA countries.

The effects of US and Chinese growth on the EA are not limited to effects on EA trade and exports, but the trade channel is likely an important part of the overall response. If we replaced real GDP growth rates by real export growth rates in the regressions above, the estimated coefficients are generally much larger — more than three times as large for the US shock and more than twice as large for China shocks. The countries with the largest response to US growth shocks in our estimation were Italy, Greece and Germany, while Portuguese, Belgian and Italian exports were most responsive to a Chinese growth shock. Note that one should not a priori expect more open countries to be more responsive in this estimation (unlike in the exercise above), as the responses are percentage responses relative to the average level — and the latter would already incorporate the higher openness. The response of German exports to a Chinese growth shock is close to the effect for the EA as a whole. Given that the share of exports to China is higher for Germany than for the EA as a whole, this is somewhat surprising. However, one explanation is that business investment in Germany is very closely linked to export growth, implying

<sup>10</sup> The apparent major exception is Greece which is estimated to be much more affected by Chinese growth shocks than US shocks. However, the coefficients and impulse responses in the Greek case are statistically insignificant, so we consider this result as largely spurious.

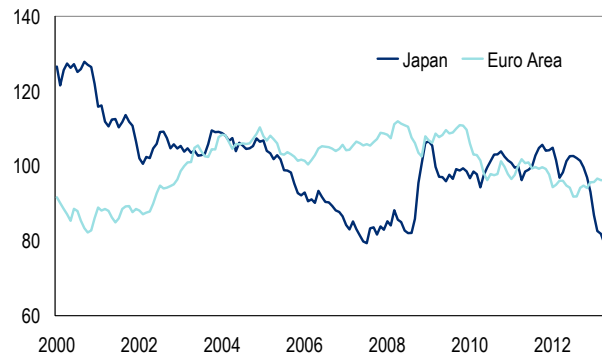
that the response of exports alone underestimates the total externally-driven impulse to German growth from a shock to Chinese (or US) growth. The close link between German exports and investment was also a topic emphasised by the IMF in its recent Article IV report on Germany.<sup>11</sup>

**Figure 10. Euro Area Countries — Estimated effect of a 1pp shock to US and Chinese growth on Real Exports (%), 2000-Q1 2013**



Note: Estimates are based on a three-variable first-order VAR of US, Chinese and EA country real exports of goods and services. Shocks are identified through a Cholesky decomposition and effects are the cumulative impulse responses after four quarters. Sources: Eurostat and Citi Research

**Figure 11. Japan and the Euro Area — Real Effective Exchange Rates (2000=100), 2000-2013**



Note: Broad real effective exchange rates. Sources: BIS and Citi Research

#### Shocks to US treasury yields or commodity prices are found to have relatively little effect

Other potential effects on euro area growth of changes in US and Chinese growth could come through their effects on Treasury yields or commodity prices. The impulse responses to US and Chinese shocks should in principle already capture the effects of these driven by US and Chinese growth shocks. We also included US rates and commodity prices separately (and individually) in our regressions to tease out their direct and indirect effects on EA growth more explicitly, but found that their effects are small. In any case, the effect of both factors may be different in the current environment than in the historical experience. First, for interest rates, we expect monetary policy divergence in the US and EA to be reflected in a divergence in market interest rates — for instance, our colleagues in rates strategy expect 10Y US Treasury rates to exceed 10Y Bund yields by 115bp at-end of 2013 and by 145bp by end-2014.<sup>12</sup> On commodity prices, the current US upturn is associated (and to some extent even driven) by an increase in energy supply as a result of the so-called 'energy revolution' in North America, which should moderate and maybe even negate any upside pressure to commodity prices.<sup>13</sup> In addition, slowing growth in China and tentative rebalancing away from investment towards consumption should imply less energy- and commodity-intensive growth in China.

#### We currently expect a slowdown, not a collapse of EM growth or import demand

Of course, the EM slowdown is not limited to China alone. Euro area goods exports to EM as a whole exceeded exports to the US by a factor of 4.5 in 2012, according to IMF DOTS data. But while EM growth has underperformed expectations, our current forecasts do not imply a collapse in EM growth — we currently expect growth in EM ex-China to be 3.5% in 2013 and accelerate to 4.2% in 2014, after growing by 3.4% in 2012. A modest slowdown in EM growth rates more generally —

<sup>11</sup> See <http://www.imf.org/external/pubs/ft/scr/2013/cr13255.pdf>.

<sup>12</sup> See [European Rates Weekly - Forward guidance: what next for markets?](#), Alessandro Tentori et al, 1 Aug 2013, Citi, and also [Euro Economics Weekly - Low\(er\) ECB Rates: For How Long?](#), Guillaume Menuet et al, 26 Jul 2013, Citi.

<sup>13</sup> See [Citi GPS: ENERGY 2020: TRUCKS, TRAINS & AUTOMOBILES](#), Edward Morse et al, Jun 2013, Citi, and [Energy Commodities - Curb Your Enthusiasm – 3Q'13 Outlook](#), Edward Morse et al, 15 Jul 2013, Citi.

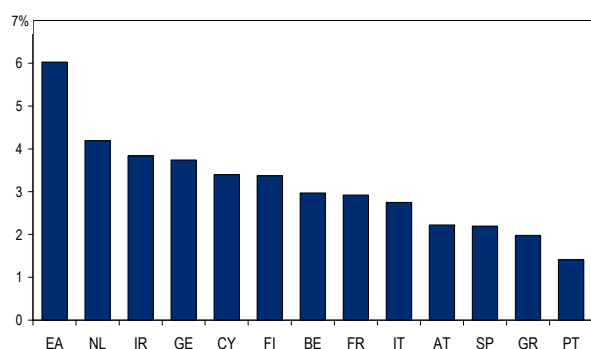


**A strong euro and the weak yen raise risks that the euro area could lose competitiveness in export markets, even as growth in export markets remains robust**

which is subject to material downside risk, in our view — would likely still offer growth opportunities for EA exports to EM countries in coming quarters.

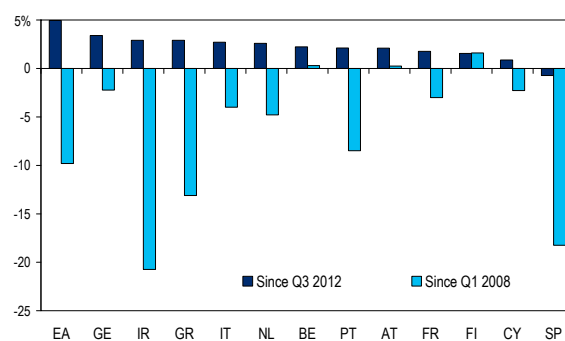
However, even if growth of export markets is robust, there is a risk that the export market *share* of EA countries may fall. In particular, the sharp depreciation of the yen (down 34%YY vs the euro in July and 22%YY in real trade-weighted terms in Q2) and the overall strength of the euro may hurt EA competitiveness in export markets. On the former, this is not because Japan is a large export market — Japanese exports are only about 0.6% of EA GDP. Rather, Japan is a potential competitor in many export markets.

**Figure 12. Euro Area Countries — Share of Japan in Broad Real Effective Exchange Rate (%), 2013**



Sources: BIS and Citi Research

**Figure 13. Euro Area Countries — Changes in the ULC-deflated Harmonised Competitiveness Indicator (%), 2008-2013**



Note: ULC are unit labour costs.  
Sources: ECB and Citi Research

**Germany may be most vulnerable on the competitiveness front, given intense competition with Japanese exporters and rising domestic labour costs.**

One illustration that Japan's significance for EA trade exceeds its share of EA trade is the so-called 'double-weighted' trade shares used by the ECB in the calculation of its Harmonised Competitiveness Indicators (HCI) or the BIS for its effective exchange rates. In these indices, Japan's share in the EA's real effective exchange rate is not limited to Japan's share of EA trade, but also takes into account Japan's share in each of the EA's export markets (the same of course applies to any other country). Since the export markets of Japan and the EA overlap relatively heavily, this raises Japan's weight in the calculation of the BIS real effective exchange rate for the EA to 6.0% (Figure 12), compared to 14.3% for the US and 5.3% for China, and far in excess of the share of Japan in EA exports (2.4%).<sup>14</sup> Among EA countries, Japan's weight in these indices (signifying greater competition with Japan) is highest for the Netherlands, Ireland, and Germany, and lowest for Portugal, Greece, and Spain.

The yen depreciation, as well as the recent appreciation of the euro against many EM currencies, has also implied that the euro area's real exchange rate has appreciated — by 5% in the three quarters up to Q2 2013, if deflated by relative consumer prices, and also by 5% in the two quarters up to Q1 2013, deflated by unit labour costs (Figure 13). Across EA countries, Germany appears once again to be most vulnerable in this dimension, as the nominal strength of the euro is combined with robust increases in domestic wages, while in many other EA countries, notably the EA periphery, a weakness in unit labour costs should moderate some of the nominal euro strength.

<sup>14</sup> See <http://www.bis.org/statistics/eer/>. To our knowledge, the ECB does not publish the weights it currently uses in computing the HCIs, but it uses a similar approach. See Hubrich, K. and T. Karlsson (2010), 'Trade Consistency in the Context of the Eurosystem Projection Exercises: An Overview', ECB Occasional Paper No 108, March 2010, <http://www.ecb.int/pub/pdf/scopops/ecbocp108.pdf>

**Key Economic Indicators (12 August – 16 August 2013)**

<b>Monday 12 August</b>		<b>Forecast</b>	<b>Last</b>
07:45	France: Balance of Payments, Jun		
08:15	Switzerland: Retail Sales, Jun		
08:30	Netherlands: Trade Balance, Jun		
09:30	Italy: General Government Debt, Jun		
	Greece: GDP NSA, 2Q		
<b>Tuesday 13 August</b>		<b>Forecast</b>	<b>Last</b>
00:01	UK: RICS House Price Survey, Jul		
07:00	Germany: HICP, Jul Final	1.9% YY	1.8% YY
	National CPI, Jul Final	1.9% YY	1.9% YY
08:00	Spain: HICP Final, Jul	1.9% YY	2.2% YY
08:30	Netherlands: Retail Sales, Jun		
08:30	Sweden: Consumer Prices, Jul	-0.3% MM, -0.1% YY	-0.2% MM, -0.1% YY
	CPIF, Jul	-0.2% MM, 1.0% YY	-0.1% MM, 0.9% YY
09:00	Norway: Retail Sales, Jun	-0.3% MM	1.8% MM
09:30	UK: Consumer Prices, Jul	-0.1% MM, 2.7% YY	-0.2% MM, 2.9% YY
	CPI ex Food, Drink, Tobacco, Energy, Jul	-0.1% MM, 2.0% YY	-0.2% MM, 2.3% YY
	Retail Prices, Jul	-0.1% MM, 3.0% YY	-0.1% MM, 3.3% YY
	RPIX – Excludes Mortgages, Jul	-0.1% MM, 3.1% YY	-0.1% MM, 3.3% YY
09:30	UK: Producer Input Prices, Jul		
09:30	UK: Producer Output Prices, Jul		
10:00	Euro Area: Industrial Production, Jun	1.1% MM	-0.5% MM
10:00	Germany: ZEW Current Situation, Aug	11.5	10.6
	ZEW Economic Sentiment, Aug	38.5	36.3
<b>Wednesday 14 August</b>		<b>Forecast</b>	<b>Last</b>
06:30	France: GDP Flash Estimate, 2Q	0.1% QQ, -0.2% YY	-0.2% QQ, -0.4% YY
07:00	Germany: GDP Flash Estimate, 2Q	0.6% QQ	0.1% QQ
07:45	France: Nonfarm Payrolls, Flash Estimate, 2Q	-0.1% QQ, -0.6% YY	-0.1% QQ, -0.7% YY
07:45	France: HICP, Jul	-0.3% MM, 1.1% YY	0.2% MM, 1.0% YY
	Consumer Prices, Jul	-0.3% MM, 1.1% YY	0.2% MM, 0.9% YY
	CPI ex Tobacco Index, Jul	125.43	125.78
08:15	Switzerland: Producer & Import Prices, Jul		
08:30	Netherlands: GDP Flash Estimate, 2Q		
08:30	Netherlands: Unemployment, Jul		
08:30	Sweden: Industrial Production, Jun	0.6% MM	-2.6% MM
09:30	UK: Claimant Count Unemployment, Jul	-10,000 MM, 4.4% Rate	-21,200 MM, 4.4% Rate
	LFS Unemployment, Apr-Jun	+50,000 QQ, 8.0% Rate	-57,000 QQ, 7.8% Rate
09:30	UK: MPC Minutes		
10:00	Euro Area: GDP Flash Estimate, 2Q	0.2% QQ, -0.9% YY	-0.4% QQ, -1.2% YY
10:00	Portugal: GDP Flash Estimate, 2Q		
11:00	Ireland: Goods Exports and Imports, Jun		
<b>Thursday 15 August</b>		<b>Forecast</b>	<b>Last</b>
09:00	Norway: Trade Balance, Jul		
09:30	UK: Retail Sales Volumes, Jul		
<b>Friday 16 August</b>		<b>Forecast</b>	<b>Last</b>
09:00	Euro Area: Balance of Payments, Jun		
10:00	Euro Area: HICP, Jul Final	1.6% YY	1.6% YY
10:00	Euro Area: Trade Balance, Jun		
10:00	Italy: Current Account, Jun		

Sources: National statistical offices, central banks and Citi Research



## Economic Indicators

### Euro Area

Aug 13 10:00 London Time	<b>Industrial Production, Jun</b>	<b>Forecast: 1.1% MM</b>	<b>Prior: -0.5% MM</b>
	After a decline in May, industrial activity seems to have rebounded in June across most of the major countries in the euro area (with the exception of France), based on the data available so far. Germany is likely out-performing most of the others, with a rebound of 2.5% MM. The improvement in industrial activity reflects better economic sentiment indicators and better external trade data. If our forecast is correct, industrial output would have increased by 1.4% QQ in 2Q, the strongest reading since 4Q 10.		
Aug 14 10:00 London Time	<b>GDP, Q2 Flash</b>	<b>Forecast: 0.2% QQ; -0.9% YY</b>	<b>Prior: -0.4% QQ; -1.2% YY</b>
	After six consecutive quarters of negative quarterly growth, euro area GDP has probably posted a gain in 2Q 13. The contraction in domestic demand should have eased significantly relative to previous quarters, mainly due to a less negative reading on investment spending. Less negative headwinds from fiscal tightening in major peripheral countries are probably also contributing to support households' disposable income. Exports have also rebounded in 2Q, after two quarterly declines. Country-wise, economic strength still stems mainly from core countries, while peripheral countries are probably generally still posting negative growth rates (albeit smaller than before).		
Aug 16 10:00 London Time	<b>HICP, Jul F</b>	<b>Forecast: 1.6% YY</b>	<b>Prior: 1.6% YY</b>
	Inflation remained stable at 1.6% YY in July, according to the flash estimate. Although favourable base effects should have pushed the headline rate lower in July, the breakdown details are likely to show that some above-average gains in food prices probably contributed to keep the headline rate higher. Core inflation (ex. unprocessed food and energy) should have eased from 1.3% to 1.2% YY in July. The headline rate is likely to subside slightly in coming months.		

### Germany

Aug 13 07:00 London Time	<b>HICP, Jul Final</b>	<b>Forecast: 1.9% YY</b>	<b>Prior: 1.8% YY</b>
	<b>National CPI, Jul Final</b>	<b>Forecast: 1.9% YY</b>	<b>Prior: 1.9% YY</b>
	We expect the final reading for German inflation in July to confirm the flash readings at 1.9% for both the CPI and the HICP measure, boosted by food prices that were rising at more than 5% YY. Unless food prices continue to rise very quickly, inflation in Germany should moderate in the coming months.		
Aug 13 10:00 London Time	<b>ZEW Current Situation, Aug</b>	<b>Forecast: 11.5</b>	<b>Prior: 10.6</b>
	<b>ZEW Economic Sentiment, Aug</b>	<b>Forecast: 38.5</b>	<b>Prior: 36.3</b>
	We assume both the current situation and the economic sentiment indicators of the ZEW poll of financial market participants will show an improvement in August. Stronger industrial production at the end of 2Q and further improvements in sentiment readings in July are likely to have boosted the current assessment, while economic sentiment was probably supported by strong export orders as well as the lack of signs of financial market stress of late.		
Aug 14 07:00 London Time	<b>GDP Flash Estimate, 2Q</b>	<b>Forecast: 0.6% QQ</b>	<b>Prior: 0.1% QQ</b>
	We expect German GDP to rise by 0.6% QQ in 2Q. Data have in fact been quite mixed in Germany over this quarter. IP in 2Q was 2.8% higher than in 1Q and we think that the very large increase in IP outweighed relatively modest retail sales and PMI readings (both roughly flat in the quarter), and a small reduction in Germany's trade balance relative to 1Q.		

### France

Aug 14 06:30 London Time	<b>Gross Domestic Product, 2Q P</b>	<b>Forecast: 0.1% QQ, -0.2% YY</b>	<b>Prior: -0.2% QQ, -0.4% YY</b>
	France will likely print a positive 2Q estimate for the first time in three quarters, although it will not be enough to push the YY rate into positive territory. Modest gains in household consumption and government spending will likely be offset by a sixth successive decline in gross fixed capital formation, implying a 0.0ppt domestic demand contribution. The economy is essentially trading water at the end of the first half, in our view. The main obstacles to a better economic outlook remain the lack of confidence and poor profitability dynamics for the corporate sector.		
Aug 14 07:45 London Time	<b>Non-Farm Payrolls, 2Q P</b>	<b>Forecast: -0.1% QQ, -0.6% YY</b>	<b>Prior: -0.1% QQ, -0.7% YY</b>
	We look for another modest quarterly drop in non-farm payrolls, representing the loss of around 15k jobs in 2Q-13. We look for some stabilisation in 3Q and anticipate limited job creation in 4Q based on the improvement seen in the various employment expectations series compiled by the Banque de France in May, when our composite index rose to its highest level this year, and equalled its long-term average. We suspect however that more labour market reforms will be needed to kick start the job creation cycle.		
Aug 14 07:45 London Time	<b>CPI – EU Harmonised, Jul</b>	<b>Forecast: -0.3% MM, 1.1% YY</b>	<b>Prior: 0.2% MM, 1.0% YY</b>
	<b>Consumer Price Index, Jul</b>	<b>Forecast: -0.3% MM, 1.1% YY</b>	<b>Prior: 0.2% MM, 0.9% YY</b>
	<b>CPI Ex Tobacco Index, Jul</b>	<b>Forecast: 125.43</b>	<b>Prior: 125.78</b>
	Inflation is expected to have risen modestly to a four-month high of 1.2% YY in July, reflecting a small uptick in core CPI to 0.9% YY (due to unfavourable base effects) compared to the recent 0.6% YY April cycle low. There are downside risks to this forecast given the volatility in the price of clothing and footwear items related to seasonal sales. Neither energy nor unprocessed food prices are expected to have shown much momentum in July. Headline inflation rates are forecast to fluctuate in a 0.8% to 1.1% range in 2H-13, averaging around 0.9%.		

### Spain

Aug 13 08:00 London Time	<b>HICP, Jul F</b>	<b>Forecast: 1.9% YY</b>	<b>Prior: 2.2% YY</b>
	As we expected, inflation eased in July to 1.9% YY, according to the flash estimate. The breakdown details will likely show this was driven by favourable base effects in the health component (after a large one-off price increase in July 2012) and lower price increases in the energy component relative to last year. Core CPI inflation likely eased to 1.9% from 2.0%. Inflation is likely to continue falling further in coming months, once the effect of the VAT rate hike in September 2012 exits the annual comparison. We expect inflation to decline to below 1% YY by year-end.		

## Economic Indicators

### Sweden

Aug 13	<b>Consumer Prices, Jul</b>	<b>Forecast: -0.3% MM; -0.1% YY</b>	<b>Prior: -0.2% MM; -0.1% YY</b>
08:30	<b>CPIF, Jul</b>	<b>Forecast: -0.2% MM; 1.0% YY</b>	<b>Prior: -0.1% MM; 0.9% YY</b>
London Time			

Inflation pressure continues to be very low and most indications are that inflation will remain low during the next 1-2 years. Although having weakened somewhat of late, we expect the krona (in KIX-terms) to remain strong in a historical perspective, which will help limit inflation ahead. Rising energy and commodity prices have kept inflation up in recent years, but looking ahead we will probably see negative contributions to inflation from these factors both this and next year. The rate of pay increases is now also slowing compared to 2013, which will also contain inflation.

Aug 14	<b>Industrial Production, Jun</b>	<b>Forecast: 0.6% MM</b>	<b>Prior: -2.6% MM</b>
08:30			
London Time			

Industrial production was markedly weaker than expected in May (-2.6% MM), at the same time as the previous month turned out even weaker than suggested by the initial data (the April outcome was lowered by 0.6pp to show a decrease of 1.1% M/M). Hence, momentum remains weak; industrial production was 0.9% below the 1Q average in April and May combined, which compares with a 0.1% Q/Q drop in 1Q 2013 and a 2.6% Q/Q decline in 4Q 2012. Ahead, the above-50 PMI reading in July (51.3), including the well-above 50 readings for the orders index as well as the production index, point to a mild recovery. The NIER survey confirms this picture. In other words, we expect the manufacturing sector to recover gradually throughout the year, but it will be a bumpy road and some setbacks should be expected in periods.

### Norway

Aug 13	<b>Retail Sales, Jun</b>	<b>Forecast: -0.3% MM</b>	<b>Prior: 1.8% MM</b>
9:00			
London Time			

Following a strong rebound in June, we expect a downward correction in retail sales in June. However, with supportive fundamentals in place, consumption growth should stay robust ahead (relatively firm labour market, solid real disposable income, low interest rates and ongoing house price gains, albeit moderating).

### United Kingdom

Aug 13	<b>Consumer Prices, Jul</b>	<b>Forecast: -0.1% MM, 2.7% YY</b>	<b>Prior: -0.2% MM, 2.9% YY</b>
09:30	<b>CPI Ex Food, Drink, Tobacco, Energy, Jul</b>	<b>Forecast: -0.1% MM, 2.0% YY</b>	<b>Prior: -0.2% MM, 2.3% YY</b>
London Time	<b>Retail Prices, Jul</b>	<b>Forecast: -0.1% MM, 3.0% YY</b>	<b>Prior: -0.1% MM, 3.3% YY</b>
	<b>RPIX – Excludes Mortgages, Jul</b>	<b>Forecast: -0.1% MM, 3.1% YY</b>	<b>Prior: -0.1% MM, 3.3% YY</b>

We expect the YY CPI inflation rate to edge down to 2.7% YY in July from 2.9% in June, as base effects swing round from adverse in June to more helpful in July. Looking forward, we expect the headline CPI rate will fall close to the 2.0% target around the end of this year.

Aug 14	<b>Claimant Count Unemployment, Jul</b>	<b>Forecast: -10,000 MM, 4.4% Rate</b>	<b>Prior: -21,200 MM, 4.4% Rate</b>
09:30	<b>LFS Unemployment, Apr-Jun</b>	<b>Forecast: +50,000 QQ, 8.0% Rate</b>	<b>Prior: -57,000 QQ, 7.8% Rate</b>
London Time			

The single month figures already have shown the jobless rate at 8.0% in April and May and we expect this release will show the average for 2Q rising to 8.0% from 7.8% in 1Q (which was depressed by the weather-related drop in the participation rate in March).

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

## Key Economic Indicators (19 August – 23 August 2013)

Monday 19 August		Forecast	Last
	Greece: Current Account, Jun		
Tuesday 20 August		Forecast	Last
07:00	Germany: Producer Prices, Jul		
08:30	Netherlands: Consumer Confidence, Aug		
09:00	Norway: GDP, 2Q		
10:00	Euro Area: Construction Output, Jun		
14:00	Belgium: Consumer Confidence, Aug		
Wednesday 21 August		Forecast	Last
09:30	UK: Public Sector Net Borrowing – PSNB ex, Jul		
11:00	UK: CBI Industrial Trends Survey, Aug		
Thursday 22 August		Forecast	Last
07:00	Switzerland: Trade Balance, Jul		
08:30	Sweden: Unemployment, Jul		
08:30	Netherlands: Consumer Spending, Jun		
09:00	Euro Area: Flash PMIs, Aug		
Friday 23 August		Forecast	Last
07:00	Germany: GDP Details, 2Q		
07:00	Germany: Deficit, Jan-Jun (Maastricht Basis)		
09:30	UK: GDP (2 <sup>nd</sup> Release), 2Q		
09:30	UK: Services Output, Jun		
09:30	UK: BBA Mortgage Advances for House Purchase, Jul		
15:00	Euro Area: Consumer Confidence, Aug Flash		

Sources: National statistical offices, central banks and Citi Research

Title	Author	Date
<b>Euro Area — Sovereign Debt Crisis Update</b>		
Euro Area Growth and Inflation Expectations Fall in Q3	Ebrahim Rahbari /Giada Giani	Aug 9, 2013
German Economy Gathers Momentum Going Into Q3	Ebrahim Rahbari /Giada Giani	Aug 8, 2013
Polls Continue to Suggest Close German Election Result	Ebrahim Rahbari /Giada Giani	Aug 7, 2013
Greek FinMin rules out another debt restructuring	Ebrahim Rahbari /Giada Giani	Aug 6, 2013
Italy's Political Tensions Unlikely to Lead to Snap Election	Ebrahim Rahbari /Giada Giani	Aug 5, 2013
<b>Euro Area</b>		
European Economic Forecast Highlights - July 2013	Ann O'Kelly	Jul 18, 2013
The euro area isn't working — labour market reforms in the euro area and why they won't solve the euro area job crisis;	Ebrahim Rahbari and Deimante Kupciuniene	Jul 11, 2013
Taking Stock of Labour Market Rigidities and Reforms in the Euro Area	Ebrahim Rahbari and Deimante Kupciuniene	Jul 11, 2013
ECB - Unanimous Governing Council Enacts Forward Guidance	Guillaume Menuet	Jul 4, 2013
<b>Euro Economics Weekly</b>		
Low(er) ECB Rates: For How Long?	Guillaume Menuet	July 26, 2013
German Exports — Down But Not Out	Ebrahim Rahbari	July 19, 2013
On Italy's Fiscal Woes and Euro Area's Dismal Labour Market	Giada Giani	July 12, 2013
France a Year On: How Much Progress?	Guillaume Menuet	July 5, 2013
Small steps towards banking union: the ECB should be pleased	Guillaume Menuet	Jun 28, 2013
Slovenia: ESM Assistance for Bank Recap Would Make Sense	Guillaume Menuet	Jun 21, 2013
Spain's External Rebalancing	Giada Giani	Jun 14, 2013
Financial Conditions Neutral, At Best, on Growth	Giada Giani	Jun 7, 2013
ECB: Focus on Collateral Rules rather than Direct Purchases	Guillaume Menuet	May 31, 2013
Removing Grexit from the Baseline Scenario	Giada Giani	May 24, 2013
Watching for Positive Surprises: Favour GIPS over France	Guillaume Menuet	May 17, 2013
Euro Area Disinflationary Pressures	Giada Giani	May 10, 2013
Italy and Spain — "We Will Die of Austerity Alone"	Giada Giani	May 3, 2013
<b>Chief Economist Publications</b>		
Global Economic Outlook and Strategy - July 2013	Willem Buiter	Jul 17, 2013
<b>Ireland</b>		
Ireland - Back in Recession	Michael Saunders	Jun 28, 2013
<b>Scandi</b>		
Scandi Economics Update	Tina Mortensen	Aug 9, 2013
Denmark - Faltering Recovery	Tina Mortensen	Jul 17, 2013
Sweden - Inflation Bang on Riksbank Forecast in June	Tina Mortensen	Jul 11, 2013
<b>UK</b>		
UK - More on BoE Guidance	Michael Saunders	Aug 7, 2013
UK - MPC Start Forward Guidance	Michael Saunders	Aug 7, 2013
UK - YouGov Report Little Change in Inflation Expectations	Michael Saunders	Jul 19, 2013
UK - MPC Minutes And Labour Market Data	Michael Saunders	Jul 17, 2013
<b>UK Economics Weekly</b>		
Guidance on Guidance	Michael Saunders	Jul 19, 2013
Improving — Can Do Better	Michael Saunders	Jul 12, 2013
The MPC's Declaration of (Monetary) Independence	Michael Saunders	Jul 5, 2013
Carney's Challenge	Michael Saunders	Jun 28, 2013
Selloff Reinforces the Case for Forward Guidance	Michael Saunders	Jun 21, 2013
Growing, But Not (Yet) Really Recovering	Michael Saunders	Jun 14, 2013
A Nation of Workers	Michael Saunders	Jun 7, 2013

Source: Citi Research

## Appendix A-1

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