Italian PM Letta Expected to Win Confidence Vote Today

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

2 October 2013

Guillaume Menuet
+44-20-7986-1314

Ebrahim Rahbari
+44-20-7986-6522

Giada Giani
+44-20-7986-3281

Economics

Western Europe

Industrialised G7 Countries

Summary

Today's ECB Meeting – No change in rates. We anticipate the Governing Council will leave its key interest rates unchanged again today, and reiterate that its monetary policy stance will "*remain accommodative for as long as necessary*".

Italy: Berlusconi's PdL close to split, ensuring government survival — PM Letta speaks to the Upper House (where he needs PdL votes) at 9.30 today, and the crucial vote will follow. Comment: it seems likely that the government will win the confidence vote. The key uncertainty is the extent of the split within PdL, with the possibility that some dissidents may create a new Centre-right party, increasing the likelihood of a Letta administration possibly surviving until 2015.

Italy: timely approval of 2014 Budget law is key for rating — Rating agency DBRS said that timely approval of the budget would be a key factor in their rating decision. Comment: we think the 2014 budget will be approved even if the Letta government falls, as a new technocrat PM would likely be appointed to deliver a budget before year-end. A DBRS downgrade (from A- rating) would imply higher haircuts to Italian government bonds posted as collateral at the ECB.

Germany: Grand Coalition negotiations could last until 2014 — *Handelsblatt* quotes SPD general secretary Nahles as not ruling out that coalition negotiations with the CDU/CSU could last beyond year-end. Comment: It looks as if it will take some time for a new German government to be formed. In the meantime, there will probably be little reform or other policy momentum originating in Germany.

EU's Rehn calls on Germany and France to do more — EU's Rehn called on Germany and France to "*implement what the EU Council has recommended to them*". Mr. Rehn asked Paris for more information on how a planned increase in employer contributions in the pension reform will be compensated so that "*the already high cost of labour does not rise further*". EU budget commissioner Lewandowski called for Germany to boost domestic demand.

France's multi-annual budget programme based on sizeable spending cuts — the structural budget deficit effort would amount to 0.9% of GDP in 2014 and 2015, but would likely be eased somewhat to 0.6% of GDP in 2016 and 0.3% of GDP in 2017. From 2015, all effort is expected to rely on expenditure savings.

French government mulling changes to planned 2014 VAT rates — Budget Minister Cazeneuve indicated that the planned cut in the lower VAT rate could be suspended to protect the purchasing power of lower income households.

Spain: Financial programme likely to end in 2013 — EU's Rehn said Spain may not need further assistance for its banking sector after 2013. Registered unemployment rose by 26k in September. Labour Minister Báñez confirmed the government plans to use €6.2bn from the pension reserve fund.

Greece – PM calls for quick decision on debt relief. **Slovakia –** Central

Recent Research

UK — YouGov Reports Slight Drop In Inflation Expectations

We report here the results of the September YouGov survey of inflation expectations among the general public, carried out during 20-22 September with a sample size of 2,017 people. The median for inflation expectations in the year ahead edged down to 2.5% in September from 2.6% in the last two months. The median for inflation expectations in the longer term (next 5-10 years) also fell slightly, to 3.3% YoY in September, having crept up from 3.3% in July to 3.4% in August.

Michael Saunders +44-20-7986-3299

UK — Osborne Speech

Chancellor George Osborne's speech to the Conservative Party Conference confirms that the Help to Buy measures will start this month rather than (as previously planned) in early 2014, and that there will be a new "Help to Work"

government deficit close to plan in 2013. **Slovenia –** Worse economic prospect for 2014 due to delay in banking sector resolution

Today's News in Detail

Today's ECB Meeting – No change in rates. We argue that the ECB is under no pressure to alter its very accommodative monetary policy stance. With inflation pressures contained, a slow recovery and negative private sector credit dynamics, we expect the refi rate to remain stable at 0.5% until the end of 2016. We anticipate the Governing Council will leave its key interest rates unchanged again today, and reiterate that its monetary policy stance will "*remain accommodative for as long as necessary*", in line with the forward guidance provided in July and reiterated at the August and September meetings. Hence the introductory statement should make a reference to the fact that the Governing Council will expect the "*key ECB interest rates to remain at present or lower levels for an extended period of time*". We believe that another LTRO is probably only a matter of time – we suggest in the next 3 to 6 months: for details, see ***Euro Economics Weekly - New ECB LTRO? Not Like Waiting for Godot.***

>> Back to the Top

Italy – Berlusconi's PdL close to a split, ensuring government survival. Deputy PM PdL Angelino Alfano called yesterday for a united PdL to back the government in today's confidence vote, reportedly opposing his leader, Silvio Berlusconi, who intends to vote it down. A senior PdL MP, Carlo Giovanardi, said yesterday at least 40 MPs are ready to support the government, suggesting a new parliamentary group being formed independent from Mr Berlusconi. PM Letta yesterday rejected the PdL ministers' resignations, in a sign of renewed government unity. Media report that in his speech in front of the parliament today, PM Letta will stress the need for clear parliamentary support for his administration (not just a small fringe of departing PdL MPs) to ensure his government lasts at least until spring 2015. Letta will give his speech to the Senate (where he needs the PdL votes to pass) at 9.30 this morning and the confidence vote will follow. Comment: while it seems likely that the government will pass the confidence vote today, the key uncertainty remains the extent of the split within PdL. If this results in the departure of a few PdL MPs, the government coalition will remain very fragile and still dependent on Berlusconi's juridical problems. If instead PdL dissidents merge into a new centre-right political force, the chances of a longer and more stable survival for the Letta administration increase notably, possibly taking it until 2015. Even in that case, however, it remains to be seen the extent of the divergence between the new political movement and the other main coalition party, the centre-left PD.

Italy – pressures mount on all fronts to resolve political crisis. Confindustria issued a note yesterday saying that renewed political instability may cause 1% lower GDP growth in 2014 and 2015. According to the simulations by the employers' association, the new round of political instability will prevent Italy from exiting recession, with 2014 GDP falling by 0.3% (against a baseline scenario for GDP to grow by 0.7%) and another negative effect of 0.9% on GDP growth in 2015. These simulations are based on the developments observed in late 2012-early 2013, when increasing political uncertainty pushed the government bond spread wider (by 100bp) and froze investment decisions. Wider bond yields would be transmitted into tighter financing conditions. European institutions are also sounding more worried about Italian politics. EU Commissioner Olli Rehn said that political instability in Italy is jeopardising the economic recovery in the whole euro area, not just in Italy itself. OECD general secretary Gurria also said political turmoil in Italy is putting the nascent recovery in the Italian economy at risk.

scheme for long-term unemployed people. But the speech also contains three extra eye-catching announcements. It is not clear how the Chancellor intends to pay for these, especially in the context of rising debt service payments caused by higher gilt yields.

Michael Saunders +44-20-7986-3299

UK — Recovery in Mortgages, But Not In Business Lending

The number of mortgage approvals for home purchase rose to 62.2K in August, up from 47.7K a year earlier and the highest since Feb-08. This fits in with other signs that the housing market is recovering quite strongly. But, while housing and mortgage lending are recovering markedly, business lending remains weak and credit availability for SMEs remains poor. .

Michael Saunders +44-20-7986-3299

UK — Deloitte CFO Survey Shows Broadening Expansion

The quarterly Deloitte CFO survey shows signs that the economic recovery is gathering pace and broadening. Like money markets, CFOs seem to expect rate hikes to come rather earlier than implied by the BoE. Fully 82% of CFOs expect that Bank Rate will rise in 2015 or earlier, whereas only 15% expect the first hike in 2015 and 4% expect the first hike after 2016. But, there is no sign that these expectations of earlier hikes are denting optimism.

Michael Saunders +44-20-7986-3299

Euro Economics Weekly — New ECB LTRO? Not Like Waiting for Godot

Despite some suggestions that the ECB is not yet willing to commit to offering another LTRO, we believe that the case is compelling enough to expect some announcement over the next 3 to 6 months, possibly as early as December. In our view, the only issues that still need to be resolved by the Governing Council are the exact timing and length of the facility as well as its interest rate characteristics.

Guillaume Menuet +44-20-7986-1314

>> Back to the Top

Italy – timely approval of the 2014 Budget law is key for rating, DBRS said. DBRS rating agency said the timely approval of the budget would be a key factor they would consider in their rating decision on Italy. DBRS reportedly said that the political turmoil may also stall necessary reforms. DBRS's rating is particularly important because, among the four rating agencies the ECB uses to set collateral rules for banks' funding, DBRS assigns Italy the highest mark of single-A. This means that a DBRS downgrade would imply higher haircuts applied on Italian government bonds posted as collateral at the ECB. Comment: we think the budget approval will proceed even if the current government falls, as a new technocrat PM may then be appointed to deal with the budget approval before year-end. However, the budget will likely be more of a technical exercise to ensure the fiscal targets are met – which at present does not require a great deal of fiscal tightening – but without clear policy directions (for example much-needed spending cuts to allow for lower taxes).

Italy – state sector borrowing kept widening in Sept, to €15bn, about €4bn above the level of Sept 2012. The Italian Treasury said the higher deficit in September stemmed mainly from the repayment of government arrears (which increased by about €4bn during the month of September to a total of €11.2bn). The YTD state budget deficit widened further to €75.9bn (4.9% of GDP), against €45.3bn in the same period of 2012. Comment: while the comparison with 2012 is particularly unfavourable due to several one-off deficit-reducing measures undertaken last year at the peak of the sovereign debt crisis, the YTD cash deficit numbers are the worst since records began in 1998. While some items are not going to affect the accrual deficit, data suggest that the government fiscal deficit in 2013 is likely to exceed the target of 3% of GDP.

>> Back to the Top

Germany: Grand Coalition negotiations could last until 2014: *Handelsblatt* quotes SPD general secretary Nahles as not ruling out that coalition negotiations with the CDU/CSU could last beyond the year-end. By October 22, the German parliament would be constituted (the constitution allows a maximum of 30 days to pass for that to happen post-election), but a new German government would be very unlikely to be ready at that stage. The SPD has meanwhile decided to let a party convention decide on starting formal coalition negotiations if and once exploratory talks with the CDU/CSU have been successful. Until a new government is found, the old government remains in power in a caretaker capacity, which technically has the same rights as a regular government but no longer carries a parliamentary majority. Comment: It does look as if it will take some time before a new German government will be found. In the meantime, there will probably be little reform or other policy momentum originating in Germany. However, for European questions or crisis situations, the German government would probably retain some room for manoeuvre, as Chancellor Merkel would simply need to find a majority of votes, and even during the last term she usually sought to win the opposition's approval for major euro area decisions.

Germany: Unemployment rises in September. The number of unemployed persons rose (seasonally adjusted) by 25k in September to 2.98m. Before seasonal adjustment, there was a decrease of 97K, which is lower than is usual during the month. The unemployment rate according to the national definition rose in seasonally-adjusted terms to 6.9% from 6.8% in August (non-seasonally-adjusted, it fell from 6.8% to 6.6%). The head of the Labour Agency noted that while the general labour market situation in Germany remained benign, *"structural issues"* were becoming more obvious.

>> Back to the Top

EU's Rehn wants more details about France's pension reform – EU

UK Economics Weekly — The Squeeze on Living Standards

The unprecedented squeeze on living standards continues. Real wages are down 1-2% YoY and have now been falling for 5-6 years. We suspect that real wages will continue to fall in YoY terms in H2 this year, and probably also in 2014. We expect that the decline in real wages will not prevent the economy picking up, with recovery driven more by housebuilding, exports and lower savings than by real wage gains. But, to some people, it may not feel like much of a recovery for a while.

Michael Saunders +44-20-7986-3299

Global Political Insights — Showdown, Shutdown or Meltdown? Political Risks on the Rise in US, Italy, Greece, Germany, as Geopolitical Risks Decline

The past forty-eight hours have seen a significant rise in the developed-markets political risk temperature, with a US government shutdown now considerably more likely and Eurozone political risks on the rise. Political developments in Italy and Greece over the weekend have added to pressure on fragile ruling coalitions, making early elections more likely. Compounding the Eurozone political risk outlook is complications to the coalition-forming process in Germany.

Tina M Fordham +44-20-7986-9860

Global Economics View — Forward Guidance: More than Old Wine in New Bottles and Cheap Talk?

Based on the recent experience in Canada, the US, the euro area and the UK, the best approach to signaling longer-term monetary policy intentions, in an operational manner, typically has three components.

Willem Buiter +1-212-816-2363

Norway — Two-Party Blue-Blue Minority Government

The norm of minority governments over the past 50 years looks set to continue in the next election period; yesterday, the Conservative Party leader, Erna

Economic and Monetary Affairs Commissioner Rehn welcomed the efforts being made by France *"to put public finances onto a sustainable path, and the moves to remove some of the long-standing bottlenecks to growth and employment*". However, Mr. Rehn noted that *"there remains much to be done, and some important details are still missing before we can make a full assessment of the measures that have been announced*". In particular, Mr. Rehn asked for more information on how a planned increase in employer contributions in the pension reform will be compensated so that *"the already high cost of labour does not rise further*", according to Reuters. Mr. Rehn is meeting with French PM Jean-Marc Ayrault and Finance Minister Pierre Moscovici today. Comment: countries have to submit their budget plans before the middle of October for the Commission to be able to comment on them by November in the aftermath of their new Autumn Forecasts (Nov 5). With enhanced surveillance as part of the six-pack and two-pack legislation, member states have to be much more thorough in how they present their multi-annual fiscal consolidation programmes and the associated structural reforms designed to meet their national reform programme objectives. In France's case the very strong focus of the Commission on competitiveness suggests that the scrutiny will be maintained for some time.

EU budget commissioner calls for German boost to domestic demand: EU budget commissioner Lewandowski called for measures to boost domestic demand in an interview with *Handelsblatt*. He favoured, for instance, investments in infrastructure to help the rebalancing in Europe. He criticised Germany's position of supporting a reduction in the EU budget in 2014.

>> Back to the Top

France's multi-annual budget programme based on sizeable spending cuts. The French government released its updated multi-annual budgetary adjustment programme on Tuesday, showing that the structural budget deficit effort would amount to 0.9% of GDP in 2014 and 2015, but would likely be eased somewhat to 0.6% of GDP in 2016 and 0.3% of GDP in 2017. This would be enough to bring the structural deficit in line with the medium term objective of a balanced structural equilibrium. In order to achieve this target, the government intends to limit public expenditure growth to 0.2% per year, after 0.4% in 2014 and 1.7% in 2013. Comment: compared to expenditure savings of €15bn expected in the 2014 budget, the trajectory implies that the efforts for 2015-17 will need to be around €18bn per annum. This poses the question of where the government is to find those savings. In our opinion, this will only be achievable through a significant reform of local authorities after the May 2014 municipal elections and further efforts in terms of mean-testing for social security.

>> Back to the Top

French government mulling some alterations to the planned VAT changes on 1 January 2014 – The government is envisaging, as part of an exercise to protect the purchasing power of less wealthy households, suspending the planned lowering of the reduced VAT rate from 5.5% to 5%. Budget minister Bernard Cazeneuve indicated on RMC radio that a strong consensus within parliament would be required for a change in the planned VAT changes which were already voted as part of the 2013 budget. Business daily *Les Echos* indicates that the expected lowering of the reduced rate would have cost the government €750mn in revenues, which could be used to increase the tax thresholds of lower income households by around 2%, exceeding the projected rate of inflation. Comment: the planned cut in the lower rate of VAT would have lowered the inflation headline rate by 0.1ppt if passed on in full by businesses to their final customers. At the margin, this introduces a very slight upward bias to our 1.7% 2014 CPI baseline.

>> Back to the Top

Spanish financial programme likely to end in 2013 – EU commissioner, Olli

Solberg, said that she would negotiate a two-party minority government with the right-wing anti-immigrant Progress Party after the September general election. Ms. Solberg had aimed to form a four-party government, but the Christian Democrats and Liberals opted out. Both parties, though, agreed to support the new government in Parliament.

Tina Mortensen +44-20-7986-3284

Scandi Economics Update —

Norway — Incoming government to offer tax breaks to encourage savings — September PMI point to healthy momentum in manufacturing.
Sweden — PMI jumps in September.
Denmark — September currency reserves, no intervention expected.

Tina Mortensen +44-20-7986-3284

Rehn, said on Tuesday that Spain may not need a further assistance programme for its banking sector after 2013. Mr Rehn noted that the Commission was looking at other possible arrangements. The statements come after the troika successfully concluded its fourth review of the Spanish bank bailout programme this week. Comment: €41bn of financial help from the ESM have been used for bank recap so far. The current facility will expire on 31 December 2013 and no formal decision has been taken yet on whether to close it or extend it (probably with some additional conditionality attached) into 2014, but Rehn's comments suggest that at least the Commission would be comfortable in closing the facility, in line with the intention of the Spanish government.

Spain – registered unemployment rises by 26k in September, lowest Sept increase since 2007. In seasonally-adjusted terms, jobless claims declined by 0.5% MM, after a similar drop was observed in August. Comment: registered unemployment, however, has recently been less representative of the developments in the labour market than the labour force survey, due to changes in the criteria to access jobless claims and probably to the rising share of long-term unemployed, not eligible any more for jobless claims. Total unemployment (as measured by the labour force survey) stood at 5.9mln in 2Q 13, against 4.72mln jobless claimants.

Spain to tap reserve fund to pay pensions this year – Labour's Minister Fatima Báñez stated on Tuesday that the government is planning to use €6.2bn of the pension reserve fund to be able to pay pensions in the next three months. This amount will add to the €5.5bn already tapped earlier this year, and the €7.0bn used in 2012, leaving the reserve fund with €53.2bn by the end of 2013. Despite the reserve fund, Spain's pension system has been accumulating deficits in the past few years and the cumulated losses will amount to €36.5bn by the end of 2013, the Labour minister said. Comment: The pension reserve fund was designed as a cushion to cover the effects of ageing population and the withdrawals are unlikely to be added into the accrual deficit figures (therefore resulting into a lower fiscal deficit for 2013). The pension system together with the high level of unemployment in Spain is likely to continue to be a major driver of fiscal deficits in the years to come. The social security system has lost 3.2m contributors since 2007, and is expected to post a deficit of 1.4% of GDP in 2013 (up from 1.0% of GDP in 2012) and of 1.1% in 2014.

>> Back to the Top

Greece – PM calls for quick decision on debt relief. Reuters reports that PM Samaras said yesterday that a delay by European policymakers on agreeing some form of debt restructuring on Greek official loans would risk fuelling political unrest. Samaras argued that debt relief – as promised by the European peers last year – is needed to ensure a stable economy and a stable government. However, Samaras said that given the ongoing debate within the Eurozone a resolution would not materialise *"for some time"*. Comment: the discussion on another very controversial debt rebate for Greece is unlikely to start before a new German government takes office (see above).

>> Back to the Top

Slovakia – Central government deficit close to plan in 2013.

Jaromir Sindel +42 0 233 061 485

The 12m cumulative central government cash deficit widened to 4.4% of GDP in September: this compares to -5.2% a year ago (primary deficit at -3% vs. -3.5% a year ago). Though the year-to-date deficit reached €1.98bn in September 2013 and is narrower by €0.6bn compared to the same period in 2012, it slightly worsened compared to August, when the YTD deficit was narrower by 0.76bn. This mild worsening reflects a larger contraction on the revenue side (-3.2% YY YTD), while the contraction on the expenditure side eased to -8%. As in previous months, the contraction on the revenue side reflects

a lower inflow from EU funds, although tax collection improved by 5% YY, supported by higher VAT and CIT. Moreover, the MinFin said that revenues from dividends worsened in YY terms, but are expected to improve in the rest of 2013. A recent narrowing of deficits eased concerns of a larger deficit this year than the planned -€3bn owing to underperformance on the revenue side that was initially expected to increase by 4% this year. A recent underperformance of revenues compared to the seasonal pattern suggests the risk of a deficit wider by €100mn (0.1% of GDP), while recent dynamics suggest even a narrowing compared to plan of some €300mn (0.5% of GDP) which is close to the recent updated MinFin outlook on the 2013 deficit at €2.8bn.

Slovakia - Further consolidation measures necessary to avoid risk of enforced balanced budget. However, government plans to continue with fiscal consolidation due to a large output gap**.** As result, the government targets for the general government deficit are 2.9% of GDP in 2014, -2.57% in 2015 and -1.5% in 2016 (owing to a positive output gap) after -2.94% this year. However, this plan requires large surpluses in the remaining parts of government (€300-600mn) and particularly further consolidation measures of €0.7-€1.5bn in 2014-16, otherwise the cash central government deficits would widen by €0.8-€1bn in the next three years. However, government has prepared consolidation measures (particularly more effective governance and combatting the grey economy) worth €500-€600mn. Government debt is expected to increase to 54.7% of GDP in 2013 and almost 57% in 2014. According to the debt rule, the government will have to freeze 3% of expenditures excluding debt services, EU related expenditure and social expenditures in 2015, will have to propose no growth in expenditure for 2016 and if the government debt breaches 57% of GDP in 2014, the government will have to propose a balanced budget in 2016 that would require consolidation of more than €3bn. Moreover, there is a risk that government debt will breach the 57% ratio to GDP due to ESA2010 methodology (applied already in 2014) according to Ludovit Odor, a representative of the Fiscal Council.

>> Back to the Top

Slovenia – Worse economic prospect for 2014 due to later banking sector resolution

Jaromir Sindel +42 0 233 061 485

Government forecasting institute IMAD worsened its GDP outlook for 2014 to -0.8% YY from -0.2% initially, after a 2.4% contraction this year, followed by a recovery of 0.4% in 2015. The worsening IMAD forecast reflects later banking resolution, which also forced us to cut our GDP forecast for 2014 to -0.5% (-0.3% initially) after -2.2% in 2013, despite improving our outlook on foreign demand (even slightly above consensus in 2014), which we expect to support recovery of export growth to almost 4% YY in 2014, while IMAD assumes 3%. Comment: It is more than clear that the later banking resolution is applied, the worse the economic outlook is likely to be, which will definitely put the Slovene economy into an adverse circle that will finally require more fiscal consolidation. In other words, the political representatives should find a way to quickly privatize all state-owned banks once the recapitalization requirements are announced. While the EC/ECB mission, which is currently in Slovenia, is unlikely to result in an ESM bailout (as the asset quality review and stress test exercises will be finished by end October and policy proposals by end November), the mission will evaluate the fulfillment of the Council recommendations from June this year, which however, included among others also the banking sector resolution and fiscal consolidation, which we think will be not positive for Slovenia due to fiscal consolidation based on the revenue side, which we discussed in *Euro Area: Sovereign Debt Crisis Update* of 30 September.

>> Back to the Top

Latest Issues of Sovereign Debt Crisis Update

Pressure Rises on Banks' Sovereign Bond Holdings

EBA's Enria and Bundesbank's Weidmann call for regulatory changes to treatment of banks' sovereign bond holdings. Italy: possible split within PdL, Fitch warning on political instability. Germany: Grand Coalition talks begin Friday. Portugal's 2013 debt ratio projection revised higher. Greece: 2014 Budget decisions delayed to end-Oct. Spanish banks further stabilised, say Troika. Spain's 2014 Budget draft handed to Parliament. Ireland: draft forecasts from EC add pressure on Budget negotiations.

Guillaume Menuet +44-20-7986-1314

Italian Political Crisis Intensifies

Italy's governing coalition breaking up, confidence vote expected Wednesday. In Greece, extremist right party Golden Dawn's leaders arrested. Portugal's municipal elections deliver blow to governing coalition. Germany's SPD votes to start coalition talks, plans member referendum. Germany's CDU gains in polls, rejects tax increases. Grand coalition likely after Austrian election. EU Commission welcomes French 2014 budget. Spain's 2014 budget unveiled. Spanish banks to increase provisions.

Guillaume Menuet +44-20-7986-1314

Coeuré Says Forward Guidance is to Limit Market Volatility

ECB's Coeuré and Constancio on forward guidance. ECB's Asset Quality Review to focus on four areas of bank lending, says FT. Germany: SPD party convention today to vote on holding on exploratory coalition talks, Green party faces leadership decisions. Italy's PM Letta to call confidence vote next week. Spain probably exited recession in 3Q. Portugal's Constitutional Court rejects part of 2012 labour market reform.

Guillaume Menuet +44-20-7986-1314

French 2014 Budget Unveiled

French 2014 Budget details. French unemployment drops unexpectedly in Aug. Germany: CDU-Green coalition talks come closer. Italy's PdL MPs vote to resign if Berlusconi ousted. Italy's new fiscal projections indicate fiscal consolidation is over. Portugal's central government deficit widens in Jan-Aug. Greek government seeks debt re-profiling, not haircuts. Greek privatisation targets to be revised down again. Italian and French consumer confidence rises. We lift growth forecasts for euro area.

Guillaume Menuet +44-20-7986-1314

ECB Downplays Near-Term LTRO Option

ECB's Coeuré and Constancio on LTRO options, Mersch on Asset Quality Review. Germany's opposition SPD positions itself post election. Germany's CDU does not rule out tax increases as part of coalition negotiations. Italy's government repays debt arrears of €11.3bn. Italian exports still failing to recover. Spain's public sector wages to be frozen in 2014 budget, central govt deficit rises to 4.62% of GDP. Businesss confidence falls in France, rises in Germany but less than expected.

Guillaume Menuet +44-20-7986-1314

>> Back to the Top

Macroeconomic Forecasts

European Economic Forecast Highlights — September 2013

Western Europe

This companion to Global Economic Outlook and Strategy - September 2013 contains detailed more quarterly forecasts for main European countries to end 2014, as well as annual forecasts to 2017.

Ann O'Kelly +44-20-7986-3297

Global Economic Outlook and Strategy — September 2013

Global, Pan Asia, GEMS, Americas, EMEA, Asia, Australia

We have a slight tilt to forecast upgrades this month, and we look for growth of 2.5% in 2013 (up a tenth from last month) and 3.2% in 2014 (unchanged). Over the last six months as a whole, we have raised our 2014 growth forecast for advanced economies by 0.5%, while cutting our 2014 EM forecast by 0.5%. Our forecasts are below consensus in all four BRIC countries. The recovery in advanced economies is unlikely to cause early tightening, given ample slack. .

Willem Buiter +1-212-816-2363

Emerging Markets Macro and Strategy Outlook — Will DM's Recovery Be EM-friendly?

GEMS, Asia, CEEMEA, Latin America, Global

Of the EM central banks that have held policy meetings since last week's FOMC, the governors of the two largest - India's and South Africa's - have both emphasized the temporary nature of the relief that emerging economies will enjoy from the Fed's decision. If that's the case, and if capital flows to EM continue to become scarcer, the market will rely more and more on signs that EM can export its way out of its problems. There is some good news: strengthening export growth from China and Korea in August was part of the story behind the EM rally that we've seen since early September. But we have some reasons to question whether the EM export recovery we'll see will be really robust. This makes us cautious about the economic environment EM is about to enter. While export data seem likely to continue to recover, we think the recovery might be a shallow one, and thus not a reason to discount the growth risks that have plagued EM in the past couple of years.

David Lubin +44-20-7986-3302

>> Back to the Top

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.

IMPORTANT DISCLOSURES

Analysts' compensation is determined based upon activities and services intended to benefit the investor clients of Citigroup Global Markets Inc. and its affiliates ("the Firm"). Like all Firm employees, analysts receive compensation that is impacted by overall firm profitability which includes investment banking revenues.

For important disclosures (including copies of historical disclosures) regarding the companies that are the subject of this Citi Research product ("the Product"), please contact Citi Research, 388 Greenwich Street, 28th Floor, New York, NY, 10013, Attention: Legal/Compliance [E6WYB6412478]. In addition, the same important disclosures, with the exception of the Valuation and Risk assessments and historical disclosures, are contained on the Firm's disclosure website at https://www.citivelocity.com/cvr/eppublic/citi_research_disclosures. Valuation and Risk assessments can be found in the text of the most recent research note/report regarding the subject company. Historical disclosures (for up to the past three years) will be provided upon request.

NON-US RESEARCH ANALYST DISCLOSURES

Non-US research analysts who have prepared this report (i.e., all research analysts listed below other than those identified as employed by Citigroup Global Markets Inc.) are not registered/qualified as research analysts with FINRA. Such research analysts may not be associated persons of the member organization and therefore may not be subject to the NYSE Rule 472 and NASD Rule 2711 restrictions on communications with a subject company, public appearances and trading securities held by a research analyst account. The legal entities employing the authors of this report are listed below:

Citigroup Global Markets Ltd	Guillaume Menuet; Ebrahim Rahbari; Giada Giani; David Lubin; Ann O'Kelly; Tina Mortensen; Tina M Fordham
Citigroup Global Markets Inc	Willem Buiter

OTHER DISCLOSURES

For securities recommended in the Product in which the Firm is not a market maker, the Firm is a liquidity provider in the issuers' financial instruments and may act as principal in connection with such transactions. The Firm is a regular issuer of traded financial instruments linked to securities that may have been recommended in the Product. The Firm regularly trades in the securities of the issuer(s) discussed in the Product. The Firm may engage in securities transactions in a manner inconsistent with the Product and, with respect to securities covered by the Product, will buy or sell from customers on a principal basis.

Securities recommended, offered, or sold by the Firm: (i) are not insured by the Federal Deposit Insurance Corporation; (ii) are not deposits or other obligations of any insured depository institution (including Citibank); and (iii) are subject to investment risks, including the possible loss of the principal amount invested. Although information has been obtained from and is based upon sources that the Firm believes to be reliable, we do not guarantee its accuracy and it may be incomplete and condensed. Note, however, that the Firm has taken all reasonable steps to determine the accuracy and completeness of the disclosures made in the Important Disclosures section of the Product. The Firm's research department has received assistance from the subject company(ies) referred to in this Product including, but not limited to, discussions with management of the subject company(ies). Firm policy prohibits research analysts from sending draft research to subject companies. However, it should be presumed that the author of the Product has had discussions with the subject company to ensure factual accuracy prior to publication. All opinions, projections and estimates constitute the judgment of the author as of the date of the Product and these, plus any other information contained in the Product, are subject to change without notice. Prices and availability of financial instruments also are subject to change without notice. Notwithstanding other departments within the Firm advising the companies discussed in this Product, information obtained in such role is not used in the preparation of the Product. Although Citi Research does not set a predetermined frequency for publication, if the Product is a fundamental research report, it is the intention of Citi Research to provide research coverage of the/those issuer(s) mentioned therein, including in response to news affecting this issuer, subject to applicable quiet periods and capacity constraints. The Product is for informational purposes only and is not intended as an offer or solicitation for the purchase or sale of a security. Any decision to purchase securities mentioned in the Product must take into account existing public information on such security or any registered prospectus.

Investing in non-U.S. securities, including ADRs, may entail certain risks. The securities of non-U.S. issuers may not be registered with, nor be subject to the reporting requirements of the U.S. Securities and Exchange Commission. There may be limited information available on foreign securities. Foreign companies are generally not subject to uniform audit and reporting standards, practices and requirements comparable to those in the U.S. Securities of some foreign companies may be less liquid and their prices more volatile than securities of comparable U.S. companies. In addition, exchange rate movements may have an adverse effect on the value of an investment in a foreign stock and its corresponding dividend payment for U.S. investors. Net dividends to ADR investors are estimated, using withholding tax rates conventions, deemed accurate, but investors are urged to consult their tax advisor for exact dividend computations. Investors who have received the Product from the Firm may be prohibited in certain states or other jurisdictions from purchasing securities mentioned in the Product from the Firm. Please ask your Financial Consultant for additional details. Citigroup Global Markets Inc. takes responsibility for the Product in the United States. Any orders by US investors resulting from the information contained in the Product may be placed only through Citigroup Global Markets Inc.

The Citigroup legal entity that takes responsibility for the production of the Product is the legal entity which the first named author is employed by. The Product is made available in Australia through Citi Global Markets Australia Pty Ltd. (ABN 64 003 114 832 and AFSL No. 240992), participant of the ASX Group and regulated by the Australian Securities & Investments Commission. Citigroup Centre, 2 Park Street, Sydney, NSW 2000. The Product is

made available in Australia to Private Banking wholesale clients through Citigroup Pty Limited (ABN 88 004 325 080 and AFSL 238098). Citigroup Pty Limited provides all financial product advice to Australian Private Banking wholesale clients through bankers and relationship managers. If there is any doubt about the suitability of investments held in Citigroup Private Bank accounts, investors should contact the Citigroup Private Bank in Australia. Citigroup companies may compensate affiliates and their representatives for providing products and services to clients. The Product is made available in Brazil by Citigroup Global Markets Brasil - CCTVM SA, which is regulated by CVM - Comissão de Valores Mobiliários, BACEN - Brazilian Central Bank, APIMEC - Associação dos Analistas e Profissionais de Investimento do Mercado de Capitais and ANBID - Associação Nacional dos Bancos de Investimento. Av. Paulista, 1111 - 11º andar - CEP. 01311920 - São Paulo - SP. If the Product is being made available in certain provinces of Canada by Citigroup Global Markets (Canada) Inc. ("CGM Canada"), CGM Canada has approved the Product. Citigroup Place, 123 Front Street West, Suite 1100, Toronto, Ontario M5J 2M3. This product is available in Chile through Banchile Corredores de Bolsa S.A., an indirect subsidiary of Citigroup Inc., which is regulated by the Superintendencia de Valores y Seguros. Agustinas 975, piso 2, Santiago, Chile. The Product is made available in France by Citigroup Global Markets Limited, which is authorised and regulated by Financial Services Authority. 1-5 Rue Paul Cézanne, 8ème, Paris, France. The Product is distributed in Germany by Citigroup Global Markets Deutschland AG ("CGMD"), which is regulated by Bundesanstalt fuer Finanzdienstleistungsaufsicht (BaFin). CGMD, Reuterweg 16, 60323 Frankfurt am Main. Research which relates to "securities" (as defined in the Securities and Futures Ordinance (Cap. 571 of the Laws of Hong Kong)) is issued in Hong Kong by, or on behalf of, Citigroup Global Markets Asia Limited which takes full responsibility for its content. Citigroup Global Markets Asia Ltd. is regulated by Hong Kong Securities and Futures Commission. If the Research is made available through Citibank, N.A., Hong Kong Branch, for its clients in Citi Private Bank, it is made available by Citibank N.A., Citibank Tower, Citibank Plaza, 3 Garden Road, Hong Kong. Citibank N.A. is regulated by the Hong Kong Monetary Authority. Please contact your Private Banker in Citibank N.A., Hong Kong, Branch if you have any queries on or any matters arising from or in connection with this document. The Product is made available in India by Citigroup Global Markets India Private Limited, which is regulated by Securities and Exchange Board of India. Bakhtawar, Nariman Point, Mumbai 400-021. The Product is made available in Indonesia through PT Citigroup Securities Indonesia. 5/F, Citibank Tower, Bapindo Plaza, Jl. Jend. Sudirman Kav. 54-55, Jakarta 12190. Neither this Product nor any copy hereof may be distributed in Indonesia or to any Indonesian citizens wherever they are domiciled or to Indonesian residents except in compliance with applicable capital market laws and regulations. This Product is not an offer of securities in Indonesia. The securities referred to in this Product have not been registered with the Capital Market and Financial Institutions Supervisory Agency (BAPEPAM-LK) pursuant to relevant capital market laws and regulations, and may not be offered or sold within the territory of the Republic of Indonesia or to Indonesian citizens through a public offering or in circumstances which constitute an offer within the meaning of the Indonesian capital market laws and regulations. The Product is made available in Israel through Citibank NA, regulated by the Bank of Israel and the Israeli Securities Authority. Citibank, N.A, Platinum Building, 21 Ha'arba'ah St, Tel Aviv, Israel. The Product is made available in Italy by Citigroup Global Markets Limited, which is authorised and regulated by Financial Services Authority. Via dei Mercanti, 12, Milan, 20121, Italy. The Product is made available in Japan by Citigroup Global Markets Japan Inc. ("CGMJ"), which is regulated by Financial Services Agency, Securities and Exchange Surveillance Commission, Japan Securities Dealers Association, Tokyo Stock Exchange and Osaka Securities Exchange. Shin-Marunouchi Building, 1-5-1 Marunouchi, Chiyoda-ku, Tokyo 100-6520 Japan. If the Product was distributed by SMBC Nikko Securities Inc. it is being so distributed under license. In the event that an error is found in an CGMJ research report, a revised version will be posted on the Firm's Citi Velocity website. If you have questions regarding Citi Velocity, please call (81 3) 6270-3019 for help. The Product is made available in Korea by Citigroup Global Markets Korea Securities Ltd., which is regulated by the Financial Services Commission, the Financial Supervisory Service and the Korea Financial Investment Association (KOFIA). Citibank Building, 39 Da-dong, Jung-gu, Seoul 100-180, Korea. KOFIA makes available registration information of research analysts on its website. Please visit the following website if you wish to find KOFIA registration information on research analysts of Citigroup Global Markets Korea Securities Ltd. http://dis.kofia.or.kr/fs/dis2/fundMgr/DISFundMgrAnalystPop.jsp?companyCd2=A03030&pageDiv=02. The Product is made available in Korea by Citibank Korea Inc., which is regulated by the Financial Services Commission and the Financial Supervisory Service. Address is Citibank Building, 39 Da-dong, Jung-gu, Seoul 100-180, Korea. The Product is made available in Malaysia by Citigroup Global Markets Malaysia Sdn Bhd (Company No. 460819-D) ("CGMM") to its clients and CGMM takes responsibility for its contents. CGMM is regulated by the Securities Commission of Malaysia. Please contact CGMM at Level 43 Menara Citibank, 165 Jalan Ampang, 50450 Kuala Lumpur, Malaysia in respect of any matters arising from, or in connection with, the Product. The Product is made available in Mexico by Acciones y Valores Banamex, S.A. De C. V., Casa de Bolsa, Integrante del Grupo Financiero Banamex ("Accival") which is a wholly owned subsidiary of Citigroup Inc. and is regulated by Comision Nacional Bancaria y de Valores. Reforma 398, Col. Juarez, 06600 Mexico, D.F. In New Zealand the Product is made available to 'wholesale clients' only as defined by s5C(1) of the Financial Advisers Act 2008 ('FAA') through Citigroup Global Markets Australia Pty Ltd (ABN 64 003 114 832 and AFSL No. 240992), an overseas financial adviser as defined by the FAA, participant of the ASX Group and regulated by the Australian Securities & Investments Commission. Citigroup Centre, 2 Park Street, Sydney, NSW 2000. The Product is made available in Pakistan by Citibank N.A. Pakistan branch, which is regulated by the State Bank of Pakistan and Securities Exchange Commission, Pakistan. AWT Plaza, 1.1. Chundrigar Road, P.O. Box 4889, Karachi-74200. The Product is made available in the Philippines through Citicorp Financial Services and Insurance Brokerage Philippines, Inc., which is regulated by the Philippines Securities and Exchange Commission. 20th Floor Citibank Square Bldg. The Product is made available in the Philippines through Citibank NA Philippines branch, Citibank Tower, 8741 Paseo De Roxas, Makati City, Manila. Citibank NA Philippines NA is regulated by The Bangko Sentral ng Pilipinas. The Product is made available in Poland by Dom Maklerski Banku Handlowego SA an indirect subsidiary of Citigroup Inc., which is regulated by Komisja Nadzoru Finansowego. Dom Maklerski Banku Handlowego S.A. ul.Senatorska 16, 00-923 Warszawa. The Product is made available in the Russian Federation through ZAO Citibank, which is licensed to carry out banking activities in the Russian Federation in accordance with the general banking license issued by the Central Bank of the Russian Federation and brokerage activities in accordance with the license issued by the Federal Service for Financial Markets. Neither the Product nor any information contained in the Product shall be considered as advertising the securities mentioned in this report within the territory of the Russian Federation or outside the Russian Federation. The Product does not constitute an appraisal within the meaning of the Federal Law of the Russian Federation of 29 July 1998 No. 135-FZ (as amended) On Appraisal Activities in the Russian Federation. 8-10 Gasheka Street, 125047 Moscow. The Product is made available in Singapore through Citigroup Global Markets Singapore Pte. Ltd. ("CGMSPL"), a capital markets services license holder, and regulated by Monetary Authority of Singapore. Please contact CGMSPL at 8 Marina View, 21st Floor Asia Square Tower 1, Singapore 018960, in respect of any matters arising from, or in connection with, the analysis of this document. This report is intended for recipients who are accredited, expert and institutional investors as defined under the Securities and Futures Act (Cap. 289). The Product is made available by The Citigroup Private Bank in Singapore through Citibank, N.A., Singapore Branch, a licensed bank in Singapore that is regulated by Monetary Authority of Singapore. Please contact your Private Banker in Citibank N.A., Singapore Branch if you have any queries on or any matters arising from or in connection with this document. This report is intended for recipients who are accredited, expert and institutional investors as defined under the Securities and Futures Act (Cap. 289). This report is distributed in Singapore by Citibank Singapore Ltd ("CSL") to selected Citigold/Citigold Private Clients. CSL provides no independent research or analysis of the substance or in preparation of this report. Please contact your Citigold//Citigold Private Client Relationship Manager in CSL if you have any queries on or any matters arising from or in connection with this report. This report is intended for recipients who are accredited investors as defined under the Securities and Futures Act (Cap. 289). Citigroup Global Markets (Pty) Ltd. is incorporated in the Republic of South Africa (company registration number 2000/025866/07) and its

registered office is at 145 West Street, Sandton, 2196, Saxonwold. Citigroup Global Markets (Pty) Ltd. is regulated by JSE Securities Exchange South Africa, South African Reserve Bank and the Financial Services Board. The investments and services contained herein are not available to private customers in South Africa. The Product is made available in Spain by Citigroup Global Markets Limited, which is authorised and regulated by Financial Services Authority. 29 Jose Ortega Y Gasset, 4th Floor, Madrid, 28006, Spain. The Product is made available in the Republic of China through Citigroup Global Markets Taiwan Securities Company Ltd. ("CGMTS"), 14 and 15F, No. 1, Songzhi Road, Taipei 110, Taiwan and/or through Citibank Securities (Taiwan) Company Limited ("CSTL"), 14 and 15F, No. 1, Songzhi Road, Taipei 110, Taiwan, subject to the respective license scope of each entity and the applicable laws and regulations in the Republic of China. CGMTS and CSTL are both regulated by the Securities and Futures Bureau of the Financial Supervisory Commission of Taiwan, the Republic of China. No portion of the Product may be reproduced or quoted in the Republic of China by the press or any third parties [without the written authorization of CGMTS and CSTL]. If the Product covers securities which are not allowed to be offered or traded in the Republic of China, neither the Product nor any information contained in the Product shall be considered as advertising the securities or making recommendation of the securities in the Republic of China. The Product is for informational purposes only and is not intended as an offer or solicitation for the purchase or sale of a security or financial products. Any decision to purchase securities or financial products mentioned in the Product must take into account existing public information on such security or the financial products or any registered prospectus. The Product is made available in Thailand through Citicorp Securities (Thailand) Ltd., which is regulated by the Securities and Exchange Commission of Thailand. 18/F, 22/F and 29/F, 82 North Sathorn Road, Silom, Bangrak, Bangkok 10500, Thailand. The Product is made available in Turkey through Citibank AS which is regulated by Capital Markets Board. Tekfen Tower, Eski Buyukdere Caddesi # 209 Kat 2B, 23294 Levent, Istanbul, Turkey. In the U.A.E, these materials (the "Materials") are communicated by Citigroup Global Markets Limited, DIFC branch ("CGML"), an entity registered in the Dubai International Financial Center ("DIFC") and licensed and regulated by the Dubai Financial Services Authority ("DFSA") to Professional Clients and Market Counterparties only and should not be relied upon or distributed to Retail Clients. A distribution of the different Citi Research ratings distribution, in percentage terms for Investments in each sector covered is made available on request. Financial products and/or services to which the Materials relate will only be made available to Professional Clients and Market Counterparties. The Product is made available in United Kingdom by Citigroup Global Markets Limited, which is authorised and regulated by Financial Services Authority. This material may relate to investments or services of a person outside of the UK or to other matters which are not regulated by the FSA and further details as to where this may be the case are available upon request in respect of this material. Citigroup Centre, Canada Square, Canary Wharf, London, E14 5LB. The Product is made available in United States by Citigroup Global Markets Inc, which is a member of FINRA and registered with the US Securities and Exchange Commission. 388 Greenwich Street, New York, NY 10013. Unless specified to the contrary, within EU Member States, the Product is made available by Citigroup Global Markets Limited, which is regulated by Financial Services Authority.

Pursuant to Comissão de Valores Mobiliários Rule 483, Citi is required to disclose whether a Citi related company or business has a commercial relationship with the subject company. Considering that Citi operates multiple businesses in more than 100 countries around the world, it is likely that Citi has a commercial relationship with the subject company.

Many European regulators require that a firm must establish, implement and make available a policy for managing conflicts of interest arising as a result of publication or distribution of investment research. The policy applicable to Citi Research's Products can be found at https://www.citivelocity.com/cvr/eppublic/citi_research_disclosures.

Compensation of equity research analysts is determined by equity research management and Citigroup's senior management and is not linked to specific transactions or recommendations.

The Product may have been distributed simultaneously, in multiple formats, to the Firm's worldwide institutional and retail customers. The Product is not to be construed as providing investment services in any jurisdiction where the provision of such services would not be permitted.

Subject to the nature and contents of the Product, the investments described therein are subject to fluctuations in price and/or value and investors may get back less than originally invested. Certain high-volatility investments can be subject to sudden and large falls in value that could equal or exceed the amount invested. Certain investments contained in the Product may have tax implications for private customers whereby levels and basis of taxation may be subject to change. If in doubt, investors should seek advice from a tax adviser. The Product does not purport to identify the nature of the specific market or other risks associated with a particular transaction. Advice in the Product is general and should not be construed as personal advice given it has been prepared without taking account of the objectives, financial situation or needs of any particular investor. Accordingly, investors should, before acting on the advice, consider the appropriateness of the advice, having regard to their objectives, financial situation and needs. Prior to acquiring any financial product, it is the client's responsibility to obtain the relevant offer document for the product and consider it before making a decision as to whether to purchase the product.

With the exception of our product that is made available only to Qualified Institutional Buyers (QIBs) and other product that is made available through other distribution channels only to certain categories of clients to satisfy legal or regulatory requirements, Citi Research concurrently disseminates its research via proprietary and non-proprietary electronic distribution platforms. Periodically, individual Citi Research analysts may also opt to circulate research posted on such platforms to one or more clients by email. Such email distribution is discretionary and is done only after the research has been disseminated via the aforementioned distribution channels. Citi Research simultaneously distributes product that is limited to QIBs only through email distribution.

The level and types of services provided by Citi Research analysts to clients may vary depending on various factors such as the client's individual preferences as to the frequency and manner of receiving communications from analysts, the client's risk profile and investment focus and perspective (e.g. market-wide, sector specific, long term, short-term etc.), the size and scope of the overall client relationship with Citi and legal and regulatory constraints.

Citi Research product may source data from dataCentral. dataCentral is a Citi Research proprietary database, which includes Citi estimates, data from company reports and feeds from Reuters and Datastream.

the Firm has not reviewed the linked site. Equally, except to the extent to which the Product refers to website material of the Firm, the Firm takes no responsibility for, and makes no representations or warranties whatsoever as to, the data and information contained therein. Such address or hyperlink (including addresses or hyperlinks to website material of the Firm) is provided solely for your convenience and information and the content of the linked site does not in anyway form part of this document. Accessing such website or following such link through the Product or the website of the Firm shall be at your own risk and the Firm shall have no liability arising out of, or in connection with, any such referenced website.

ADDITIONAL INFORMATION IS AVAILABLE UPON REQUEST