13 June 2014 │ 16 pages

Developed Markets
Western Europe

Euro Economics Weekly

Labour Market Slack

- Euro area unemployment has been mildly declining since mid-2013, which is earlier in the cycle than in past recoveries. However, this has been driven by a sizable slowdown in labour force dynamics relative to recent trends, reflecting an aging population and, most likely, an increase in discouraged workers. Job growth has started in Q4 13, but remains feeble even relative to the sub-par GDP dynamics. We expect it to remain so in coming quarters as vacancy rates are still close to record lows and firms will probably first attempt to use up the buffer of unused working hours before starting hiring in full force.
- A falling working-age population may keep driving the unemployment rate lower, but broader measures of under-utilisation of labour point to a bigger slack in the labour market than official unemployment suggests, especially in the periphery. This implies an even longer time span for spare capacity to be absorbed and for wage pressures to start re-emerging.

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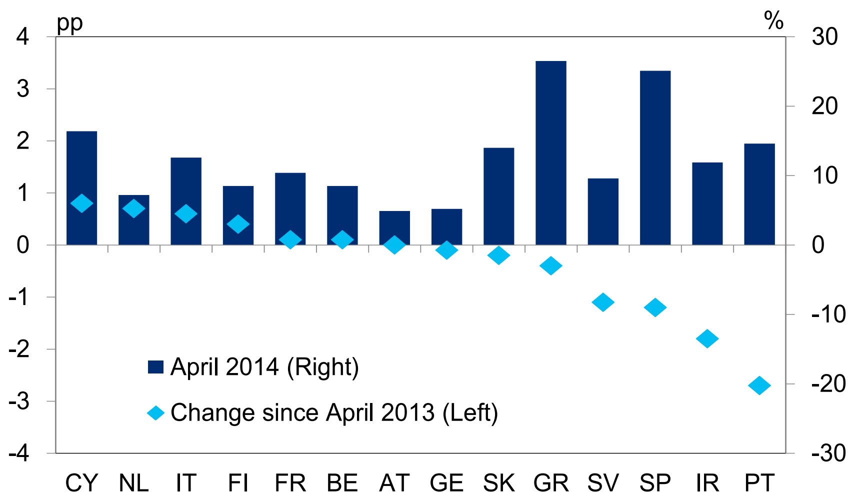
Figure 1. Citi Forecasts

	$/€	Euro Repo	10-yr Bunds	£/€	UK Bank Rate	10-Yr Gilt-Bund	SKr/€	SEK Policy Rate	NOK/€	NOK Policy Rate	SFr/€	CHF Policy Rate	CHF Spread vsBunds
3Q 14	1.38	0.10	1.60	0.80	0.50	142	9.11	0.50	8.06	1.50	1.24	0.00	-65
1Q 15	1.35	0.10	1.70	0.79	1.25	183	9.18	0.50	7.97	1.50	1.25	0.00	-68

Source: Citi Research

Figure 2. Euro Area – Unemployment Rate (% of Labour Force), April 2014



Sources: Eurostat and Citi Research

Labour Market Slack

Labour market dynamics are key to assess recovery sustainability and degree of economic slack

The unemployment rate is not a closely-watched indicator in the euro area, certainly far less so than in the UK or US. However, labour market dynamics are still important to follow especially in the current phase of the economic cycle because (a) they are key in assessing the sustainability of the recovery via job creation, and (b) provide additional gauges of the degree of slack in the economy. Recent unemployment data (which included sizable revisions to recent historical data) show that the euro area unemployment rate already started to decline in mid-2013, broadly coinciding with the first expansion in GDP. While this is earlier in the cycle than during past recoveries, we note that it has been partly driven by a decline in the labour force rather than a sizable pickup in job growth. We expect job growth to remain modest in coming quarters as firms will probably first attempt to raise hours worked before starting new hiring in full force. Falling working-age population may continue to drive the official unemployment rate lower, but broader measures of under-utilisation of labour suggest that the amount of slack in the labour market may be somewhat larger than indicated by the headline unemployment rate, especially in the periphery. This implies an even longer time span for the slack to be absorbed and for wage pressures to start re-emerging.

EA unemployment rate started to decline in mid-2013, led by the periphery…

According to the monthly data from Eurostat (based on the ILO definition of unemployment), euro area unemployment declined to 11.7% in Apr-14 from a historical peak of 12.0% in Q3 13 (highest since records began in 1970). The decline has been mainly due to the periphery countries, where the unemployment rate was (and still is) higher than the average (see Figure 2 on the front page). Portugal is topping the list in terms of jobless rate declines over the past year (-2.7pp since Apr 13), followed by Ireland (-1.8pp), Latvia, Spain and Estonia (-1.2pp) and Greece (-0.4pp). The jobless rate has remained broadly unchanged since April 13 in core countries like Germany (-0.1pp) and France (+0.1pp), while it kept rising in Finland (+0.4pp), Italy (+0.6pp), the Netherlands (+0.7pp) and Cyprus (+0.8pp).

…and earlier than in previous cycles

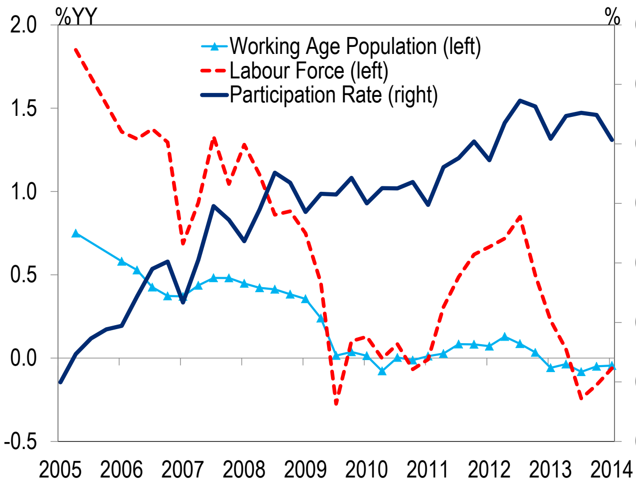
The 0.3pp decline at the euro area level, albeit still modest, occurred only two quarters after GDP posted the first positive post-recession print (in Q2 13) and with GDP growth still very subdued (sub-1% annualised rate in Q2-Q4 13 on average). This decline happened unusually early in the cycle when compared with previous cycles. In 2005, the jobless rate peaked (at 9.3%) six quarters after the economy was expanding by an average 2% QQ annualised rate. The mid-Nineties cycle was even longer, as the unemployment rate only started to subside in Q3 98, after remaining flat at around the peak of 10.5% for the previous five years in the aftermath of the 1992-1993 recession. Similarly, long stretches of the unemployment rate stuck around the peak occurred in the Eighties. Even during the short-lived economic recovery in 2010, the jobless rate temporarily inched lower in Q3 10, after 5 quarters of QQ annualised GDP growth at 2%.

A structurally lower labour force growth

What's been driving the unemployment rate lower?

Official euro area data on the Q1 14 labour force survey (LFS) are not yet available, but we use the available country information to infer recent developments in the euro area job market. These suggest that the unemployment rate has been falling as a result of only a modest expansion in employment and a significant slowdown in labour force dynamics relative to the recent trends. We estimate that in Q1 14 employment (LFS definition) grew by around 400K relative to the same quarter of 2013, while the labour force declined by almost 100K. This compares with an average annual rate of expansion in the labour force of around 800K in 2011-2012 and of 1.6mln in the 2001-2009 period (see Figure 3). Theoretically, if the labour force had continued to grow at the same rate of the previous two years, the unemployment rate would have kept edging higher in the past four quarters.

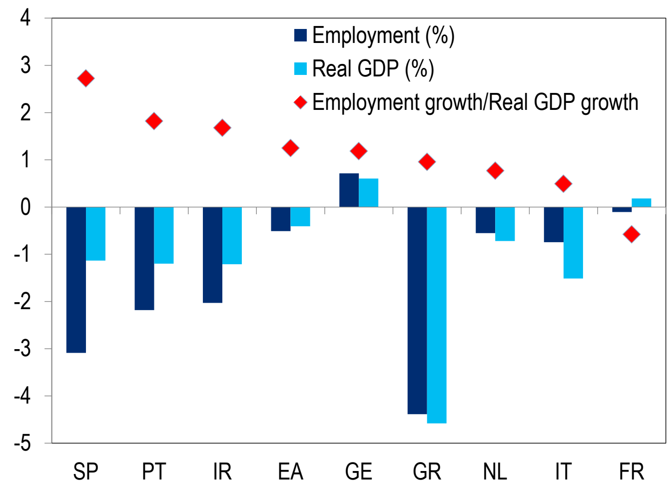
Figure 3. Euro Area – Population (%YY), Labour Force (% YY) and Participation Rate (%), 2005- 1 2014F



Note: For age group 15-75. Participation rate is the ratio between labour force and working age population of the same age group. Q1 14 is a Citi forecast.

Sources: Eurostat, and Citi Research

Figure 4. Euro Area – Average Annualised QQ Growth (%) in Employment and Real GDP, Q1 2008–Q1 2014



Note: Red dots correspond to the ratio of average employment growth and average real GDP growth (both in QQ SAAR terms) over Q1 2008- Q1 2014.

Sources: Eurostat, National Sources, and Citi Research

A sizable slowdown in labour force growth relative to recent trends due to an aging population…

Obviously the labour force dynamic is not an independent variable relative to the employment dynamic, as the participation rate (i.e., the percentage of the population in working age that is either working or actively looking for a job) also tends to be affected by labour market conditions (falling during downturns as job search becomes more difficult). However, the main driver behind the labour force slowdown in 2013 has been a decline in working-age population. Within the 15-64 year old age bracket, the euro area population has shrunk by 0.3% YY in 2013 (or by around 650K), while within the 15-74 age bracket population growth was broadly flat (-120K). This implies a significant impact of population aging, with the first cohort of baby-boomers (born right after the WWII and now aged 65-69) starting to fall out of working-age range. In the 15 years before the financial crisis (1996-2009), the population in working age rose by an average of 0.6% per annum. A trend of reduced foreign immigration is also contributing to reduce the working-age population growth relative to the pre-2009 period. The reduction of the working-age population due to demographics, which is set to continue and become more pronounced over the next decades, is a meaningful change which will affect the future dynamics of the jobless rate in the euro area, unless major immigration inflows will offset these demographic trends.

…and to a smaller extent a rise in discouraged workers

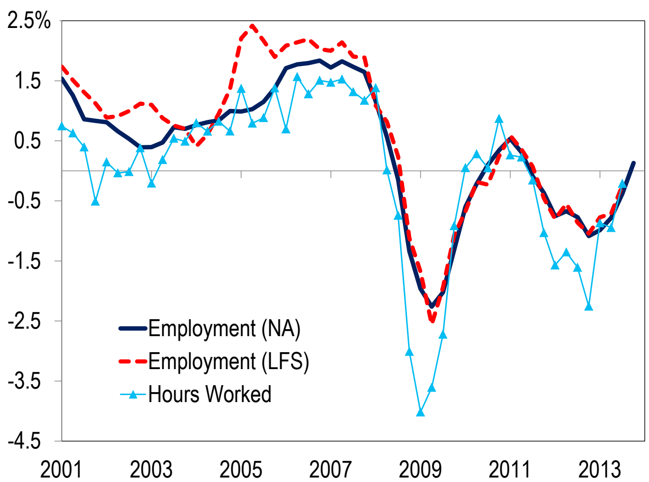
The participation rate has to a smaller extent also contributed to the slowdown in the labour force. The participation rate has moved broadly sideways (at around 63.5% for 15-74 years old, 72% for the 15-64 group) over the past couple of years, in contrast to the uptrend observed in 2011-12 and relative to the pre-crisis years (see Figure 3). The slowdown in participation rates has been mainly concentrated in the central groups of the age distribution (between 30 and 55 years old), while activity rates for the over-55s have actually increased faster than in pre-recession years (due to stricter requirements to access retirement benefits introduced with the pension reforms). The downtrend in the youngest part of the population (aged 15-24) has come to a halt during the recession. These data seem to suggest that more difficult access to the job market may have raised the share of discouraged workers among the part of the population with the highest participation rates (i.e. 30-55 years old). As further evidence, the share of the inactive population (aged 15 to 64) declaring that the main reason for their inactivity is that they think there is no work available has increased from 3.9% in 2007 to 6.2% in 2013.

Jobs in the Euro Area During the Recession

Job creation in the EA has started in Q4 13, mirroring a reduced drag from the periphery

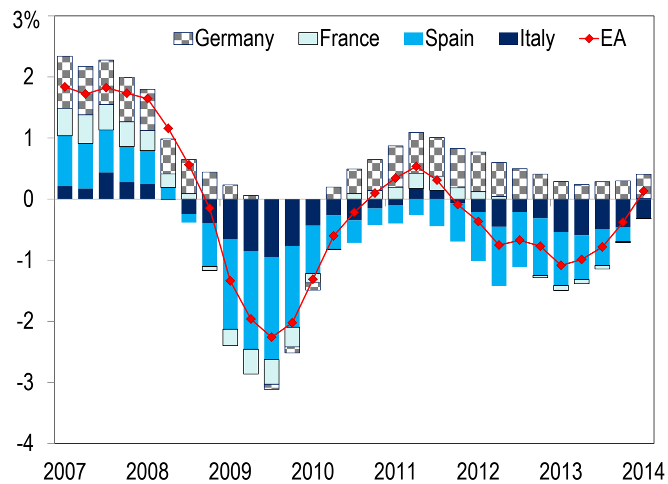
Data released this week showed that total euro area employment (on the national account definition) rose by 0.1% QQ in Q1 14, after a similar gain in Q4 13. Labour force survey data (up to Q4 13 for the euro area, Q1 14 available only for some countries) are showing a similar picture (see Figure 5). Mirroring developments in the unemployment rate, the main contribution to the stabilisation in employment at the euro area level is stemming from a less negative drag from the periphery, mainly from Spain, but also from Portugal and Greece despite their smaller size (see Figure 6). These three countries together were subtracting around 1pp from the annual growth rate of euro area employment in 2012 while their contribution is currently close to zero. Interestingly, Spanish data on employment flows show that it has been the much reduced pace of job destruction (flows out of total employment are at record-low levels), rather than a meaningful pick-up in job creation, which explains the recent modest gains in total employment. We suspect a similar trend applies to the other peripheral countries. Among the main euro area countries, employment growth is still negative in Italy (albeit less than in 2013), marginally negative in France, and positive but only slightly accelerating in Germany.

Figure 5. Euro Area – Different Measures of Labour Input (%YY), 2001–Q1 2014



Note: National Accounts (NA) and Labour Force Survey (LFS)
Sources: Eurostat and Citi Research

Figure 6. Euro Area – Employment Growth (YY%) by Country, 2007–Q1 2014



Note: Employment from National Accounts.
Sources: Eurostat and Citi Research

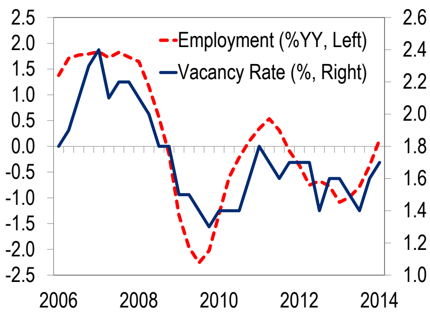
Employment to grow faster in those periphery countries where the job adjustment has been deeper

The recent improvement in employment dynamics in the periphery is the result of the much larger adjustment in the workforce in these countries (relative to the rest of the euro area and relative to their GDP dynamic) over the past five years. Spain, followed by Ireland and Portugal, stands out in terms of employment elasticity relative to GDP during the downturn, with workforce falling almost three times faster than real GDP since Q1 08 (employment fell twice faster than GDP in Portugal and Ireland). For most of the other countries, employment elasticity during the recession was roughly around one, meaning employment growth has moved one-for-one with real GDP (Figure 4). We reckon that employment will grow faster in those periphery countries where the job adjustment has been deeper. However, it is worth noting that in these same countries wage growth is generally more subdued (in some cases outright negative) relative to the euro area average – most likely a factor explaining the better job dynamics. This will limit the benefits of positive job dynamics in terms of disposable incomes.

Positive but feeble job growth so far, even when assessed against a sub-par GPD dynamic

At the euro area aggregate level, the employment dynamic over the past year has been quite feeble even when assessed against GDP growth. Employment (national account definition) expanded by an average annualised rate of 0.2% QQ since Q2 13, against an average real GDP growth of 0.9% QQ. This is a remarkably low elasticity when compared with the much higher responsiveness of employment to GDP during the downturn – around one over the entire 5-year period between Q2 08 and Q2 13. Employment elasticity to GDP was significantly higher during the recession than in the 1999-2007 period (of around 0.6) and even relative to the last major job-shedding recession in 1992-1993 (although in that case the employment decline spanned a much longer horizon than the contraction in activity).

Figure 7. Euro Area – Employment (YY%) and Vacancy Rate (%), 2006–Q1 2014



Note: Employment from National Accounts.
Sources: Eurostat and Citi Research

When labour input is measured by the number of hours worked, the adjustment during the recession has been even more severe (elasticity close to 2). This may partly offer an explanation for the feeble employment recovery observed so far. The extensive usage of reduced working time schemes (mainly in Germany and Italy) limited the impact of the recession on jobs. More recently, total hours worked have picked up more strongly than employment (probably by slightly more than GDP, although Q1 14 data are not yet available). This may indicate that there is a buffer of unused labour input in terms of working hours which could be used before hiring can start more vigorously. In the case of Italy, for example, the number of hours currently authorised for use as temporary layoffs/reduced-hour schemes (the so-called CIG) has stabilized recently but it still represents 3.5% of total hours worked.

Employment growth to remain weak and concentrated in countries with weakest wage dynamics

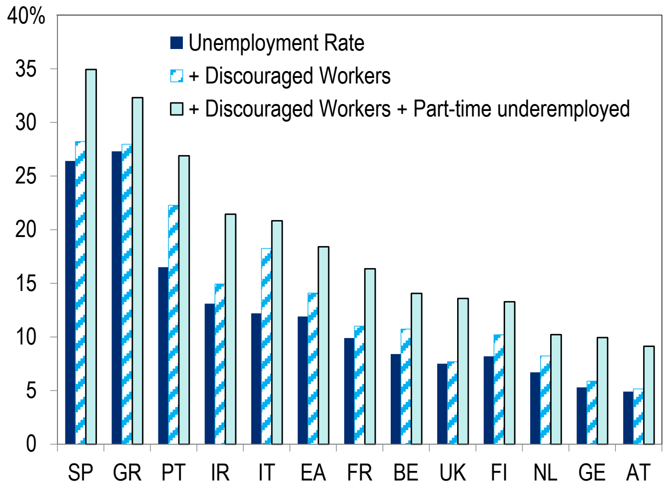
Other indications that hiring is not about to start in full force are given by the vacancy rates, which remain fairly close to their record lows (see Figure 7). Overall, we project weakness in employment growth at the euro area level to persist in the coming quarters, expanding by just 0.3% in 2014 and by 0.8% in 2015. Moreover, employment growth is likely to be concentrated, beyond Germany, in those periphery countries where wage growth is weakest. Therefore, labour income is set to improve but it is unlikely to be able to underpin a meaningful recovery in private consumption. On the other hand, even a modest employment expansion will probably still be enough to reduce the unemployment rate to around 10.5% by the end of next year, thanks to an even more subdued growth of the labour force.

Measures of labour market slack

Even with the unemployment rate expected to fall over the coming quarters, the degree of slack in the labour market is likely to remain very ample, delaying well into the future the timing when the job market may start putting upside pressure on wages and prices. We have discussed recently how the current estimates of structural unemployment for the euro area (i.e. the level below which the unemployment rate starts to create inflationary pressures, or NAIRU) may be excessively high[1]. Here we present alternative, broader, measures of unemployment which take into account not only those that meet the ILO criteria for unemployment (i.e. being without work, actively seeking work, and being available for work).

[1] See Euro Economics Weekly "The Rise of The Output Gap", Citi Research, 4 April 2014.

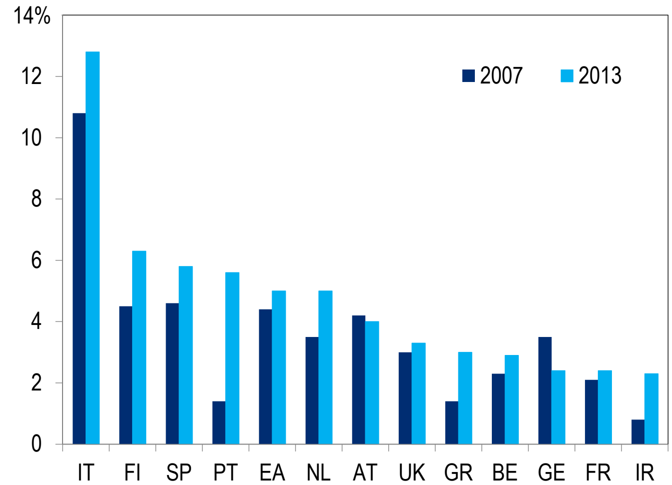
Figure 8. Euro Area – Various Measures of Unemployment Rate (%), 2013



Note: Discouraged workers are the inactive population (aged 16-74) declaring as main reason of inactivity that they think work is not available. Part-time underemployed are part-time workers wanting to work more hours. Data based on Labour Force Survey.

Sources: Eurostat, and Citi Research

Figure 9. Euro Area – Additional Potential Labour Force (% of Active Population Aged 15-74), 2007-2013



Note: Additional potential labour force is the sum of persons seeking work but not immediately available plus persons available to work but not currently seeking.

Sources: Eurostat, and Citi Research

The slack in the labour market seems larger when discouraged workers are accounted for in unemployment…

The first measure expands the concept of unemployment by including a proxy for discouraged workers by using Eurostat data on the share of inactive population (aged 15-74) declaring as the main reason of inactivity that they think work is not available. Including this group into unemployment would imply an unemployment rate of 14.1% in 2013, compared with 11.9% based on the headline figure (see Figure 10). While normally higher than the standard unemployment rate, this indicator has also increased by some 0.6pp more than the headline unemployment rate since 2008, suggesting a larger increase in labour market slack than reported by the headline rate.

…and even larger when underemployed part-time workers are also taken into account

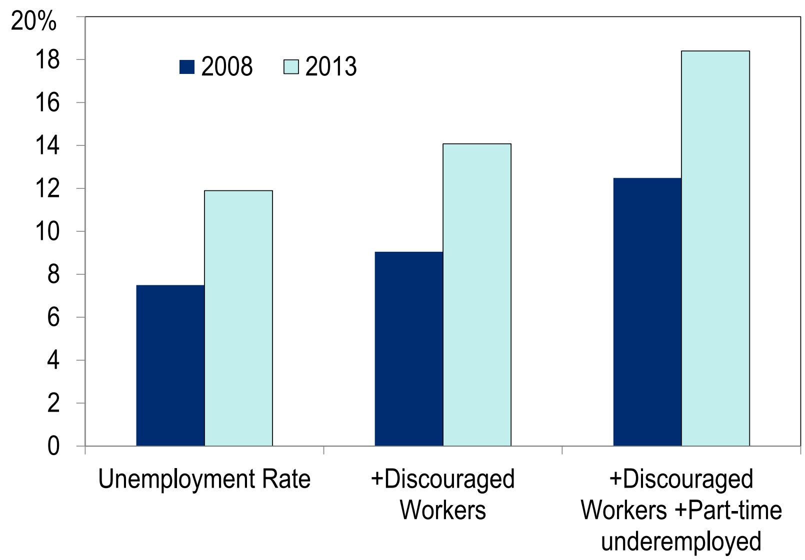
A second measure accounts also for underemployed part-time workers, i.e., those part-time workers that declare they are available to work for longer hours. Similarly to the previous measure, this broader measure is structurally higher than standard unemployment rate (standing at 18.4% in 2013), but it also rose faster since 2008 (by 1.5pp more than official unemployment rate). There is quite a differentiated picture across the euro area countries (see Figure 8). According to this broader measure of unemployment, Spain, not Greece, is the euro area country with the highest unemployment rate (34.9% in 2013, up from 16.4% in 2008), followed by Greece (32.3%, from 10.1% in 2008) and Portugal (26.9%). The largest discrepancy between actual unemployment rate and this broader measure is reported in Portugal (10.6pp), followed by Italy (8.6pp), Spain (8.5pp) and Ireland (8.3pp), suggesting that in these countries the degree of labour market slack may be more severely underestimated by looking at just the unemployment rate.

Additional potential labour force is sizable, and bigger than in 2008, in some countries

Finally we look at measures of the potential additional labour force, i.e., persons that are currently not part of the labour force, but are still loosely associated with it. These are people seeking a job but not immediately available to work and those available to work but not actively seeking. In a broader sense, these groups may still represent a form of unmet demand for employment. In Q4 13, these groups amounted to 5% of the actual labour force (aged 15-74) in the euro area, again up slightly relative to the 4.4% in Q4 07. Dispersion is again very wide across euro member states, with Italy reporting by far the highest share of potential additional

labour force (12.8% in Q4 13, up from 10.8% in Q4 07), followed by Finland (6.3% from 4.5% in Q4 07) and Spain (5.8%, from 4.6%) (see Figure 9).

Figure 10. Euro Area – Different Measures of Slack in the Labour Market (% of Labour Force), 2008-2013



Sources: Eurostat and Citi Research

Ample spare capacity in the labour market means wage pressures are delayed well into the future

All of these measures suggest that the increase in the degree of under-utilisation of labour during the 2008-2012 may have been larger than the headline unemployment rate suggests. Partly this may result in a slower decline in the unemployment rate in coming years, as people currently not part of the labour force will progressively start looking for a job as the market conditions improve. Partly this may imply a slower pace for employment growth as extension of working hours of part-time jobs partly substitute for new hiring. Either way, the ample slack in the labour market is likely to persist for several years, delaying further into the future the time when wage pressures will start to emerge.

Key Economic Indicators (16 June – 20 June 2014)

		Forecast	Last
Monday 16 June		**Forecast**	**Last**
09:00	Norway: Trade Balance, May		
10:00	Euro Area: HICP, Final, May		
Tuesday 17 June		**Forecast**	**Last**
06:545	Switzerland: SECO Economic Forecasts, Jun		
07:00	Sweden: Registered Unemployment Rate, May	3.9%	4.1%
07:00	EU-27: New Car Registrations, May		
08:00	Spain: Labour Costs, 1Q		
08:15	Switzerland: Producer and Import Prices, May		
09:00	Italy: Trade Balance, Apr		
09:30	UK: Consumer Prices, May	0.1% MM, 1.7% YY	0.4% MM, 1.8% YY
	CPI Ex Food, Drink, Tobacco, Energy, May	0.1% MM, 1.7% YY	0.5% MM, 2.0% YY
	Retail Prices, May	0.2% MM, 2.5% YY	0.4% MM, 2.5% YY
	RPIX – Excludes Mortgages, May	0.2% MM, 2.6% YY	0.4% MM, 2.6% YY
09:30	UK: Producer Input Prices, May	-0.4% MM, -4.7% YY	-1.1% MM, -5.5% YY
09:30	UK: Producer Output Prices, May	0.1% MM, 0.7% YY	0.0% MM, 0.6% YY
	Ex Food, Drink, Tobacco, Energy, May	0.1% MM, 1.1% YY	0.0% MM, 1.0% YY
10:00	Germany: ZEW Economic Expectations, Jun	38.1	33.1
	ZEW Current Situation, Jun	60.1	62.1
10:00	Euro Area: Labour Cost Index, 1Q		
10:00	Euro Area: Job Vacancies, 1Q		
Wednesday 18 June		**Forecast**	**Last**
08:00	Sweden: Consumer Confidence, Jun	101.2	100.4
	Manufacturing Confidence, Jun	97.4	94.5
09:00	UK: Bank of England Minutes of Jun 5 Meeting		
10:00	Euro Area: Construction Output, Apr		
19:00	US: FOMC Outcome		
Thursday 19 June		**Forecast**	**Last**
08:30	Switzerland: SNB Monetary Policy Assessment & Press Conference		
09:00	Norway: Norges Bank Sight Deposit Rate	Unchanged at 1.50%	1.50%
08:30	Netherlands: Unemployment, May		
09:30	UK: Retail Sales Volumes, May	0.6% MM, 5.4% YY	1.3% MM, 6.9% YY
10:00	Italy: Current Account Balance, Apr		
11:00	UK: CBI Industrial Trends – Output Expectations, Jun	+30%	+32%
	CBI Order Books, Jun	+1%	0%
	CBI Selling Prices, Jun	+5%	+4%
14:00	Belgium: Consumer Confidence, Jun		
14:00	Euro Area: Eurogroup Meeting, Luxembourg		
Friday 20 June		**Forecast**	**Last**
	EU: EcoFin Meeting, Luxembourg		
07:00	Germany: Producer Prices, May	-0.3% MM, -0.9% YY	-0.1% MM, -0.9% YY
08:30	Netherlands: Consumer Confidence, Jun		
08:30	Netherlands: Consumer Spending, Apr		
09:00	Euro Area: Monthly Balance of Payments (ECB), Apr		
09:00	Italy: Industrial Orders, Apr		
09:30	UK: Public Sector Net Borrowing (Ex RM, APF& Fin. Intervent'ns), May	£12.0 Billion Deficit	Year Ago: £13.1 Billion Deficit
	Fiscal Year To Date, Apr-May	£23.5 Billion Deficit	Year Ago: £22.6 Billion Deficit
	Greece: Current Account, Apr		
15:00	Euro Area: Flash Consumer Confidence, Jun	-6.5	-7.1

Sources: National statistical offices, central banks and Citi Research

Economic Indicators

Euro Area

Jun 20 15:00 London Time	***Consumer Confidence, Jun Flash***	**Forecast: -6.5**	**Prior: -7.1**

With ongoing moderate improvements in the labour market and inflation remaining very low, we estimate consumer confidence continued to improve in June, to 0.8 sd above its long run average and at its highest level since 2007.

Germany

Jun 17 10:00 London Time	***ZEW Economic Sentiment, Jun***	**Forecast; 38.1**	**Prior: 33.1**
	ZEW Current Situation, Jun	**Forecast: 60.1**	**Prior: 62.1**

We expect the ZEW index of financial market analysts to show a slight moderation in June for the current conditions component and a rebound in the economic sentiment index. The current conditions index has risen six months in a row and is now at the highest level since July 2007 (and 1.5 std above its LT average), whereas the economic sentiment index has weakened of late, falling for five consecutive months to a level that is only slightly above the LT average

Jun 20 07:00 London Time	***Producer Prices, May***	**Forecast: -0.3% MM, -0.9% YY**	**Prior: -0.1% MM, -0.9% YY**

We expect producer prices to be lower in May on a monthly basis and remain roughly 1% lower than a year before. As in previous months, we suspect energy prices and the exchange rate to be the main driver of the downward pressure on prices.

Sweden

Jun 17 07:00 London Time	***Registered Unemployment Rate, May***	**Forecast: 3.9%**	**Prior: 4.1%**

Unemployment on the LFS measure remains sticky, driven by a combination of strong population growth and an upward trend in labour force participation. The development in unemployment has been somewhat weaker than expected by the Riksbank back in April; in the first quarter, the LFS jobless rate overshot the Central Bank's forecast by 0.1pp and the April reading was 0.2pp above the Bank's 2Q average forecast. The upturn in LFS unemployment contrasts with recent developments in registered unemployment, which has declined for the past six months. Employment growth was flat on the month in April, but this follows a 0.3% M/M gain in both February and March. Short-term indicators point to ongoing solid growth in employment, and in turn LFS unemployment will likely start to decline soon.

Jun 18 08:00 London Time	***Consumer Confidence, Jun***	**Forecast: 101.2**	**Prior: 100.4**

Despite the uptick in consumer confidence in May, the indicator is still slightly on the low side compared to our private consumption forecast. This is somewhat worrying as household spending is expected to be the main growth driver behind economic recovery. Strong income growth, an improving labour market and higher asset prices, meanwhile, suggest that consumer confidence should improve further ahead. Improved sentiment during the second half of 2013 has partly been reflected in hard data. Household inflation is expected to stay at a low level (1.1%).

Jun 18 08:00 London Time	***Manufacturing Confidence, Jun***	**Forecast: 97.4**	**Prior: 94.5**

The Economic Tendency Indicator (ETI) slipped 3.6 points to 98.8 in May, and being 1.2 points below the historical average, the indicator now suggests that activity in the Swedish economy is slightly below a normal level. With a 7.8 points drop to 94.5, manufacturing confidence accounted for the bulk of the decrease, and with an outcome well below the long-term average, the survey suggests that recovery in manufacturing remains weak and somewhat bumpy. However, weakness in May was largely driven by lower expected production volumes and increased concerns over inventory levels, while current conditions actually improved a tad (both for production and orders). At the same time, confidence in domestic sectors remained broadly stable at fairly high levels, suggesting that underlying sentiment probably is somewhat stronger than suggested by the ETI. In June, we expect to see recovering manufacturing sentiment.

Norway

Jun 19 09:00 London Time	***Norges Bank: Sight Deposit Rate***	**Forecast: Unchanged at 1.50%**	**Prior: 1.50%**

At the June monetary policy meeting, we expect Norges Bank to leave the key policy rate stable at 1.50%, in line with market pricing and indications from the March conditional interest rate path. In terms of changes to the conditional interest rate path in the new Monetary Policy Report, we expect the Bank to make some fine-tuning to the longer-end of the path (revise it lower)

United Kingdom

Jun 17 09:30 London Time	***Consumer Prices, May***	**Forecast: 0.1% MM, 1.7% YY**	**Prior: 0.4% MM, 1.8% YY**
	CPI Ex Food, Drink, Tobacco, Energy, May	**Forecast: 0.1% MM, 1.7% YY**	**Prior: 0.5% MM, 2.0% YY**
	Retail Prices, May	**Forecast: 0.2% MM, 2.5% YY**	**Prior: 0.4% MM, 2.5% YY**
	RPIX – Excludes Mortgages, May	**Forecast: 0.2% MM, 2.6% YY**	**Prior: 0.4% MM, 2.6% YY**

We expect a slight decline in YY CPI inflation as the Easter-related boost in air fares and fares for sea travel unwinds. However, the YY CPI inflation rate probably is around its low, and we do not expect a major new downtrend in coming months. Surveys suggest that capacity use and labour costs are picking up, while the disinflationary effects from food, energy and utilities is largely over.

Jun 17 09:30 London Time	***Producer Input Prices, May***	**Forecast: -0.4% MM, -4.7% YY**	**Prior: -1.1% MM, -5.5% YY**

The continued appreciation of sterling may well cause a further modest drop in input prices, although commodity prices in USD terms are trending up – with the CRB index at a 2-year high.

Jun 17 09:30 London Time	***Producer Output Prices, May***	**Forecast: 0.1% MM, 0.7% YY**	**Prior: 0.0% MM, 0.6% YY**
	Output Prices Ex Tax, May	**Forecast: 0.1% MM, 0.7% YY**	**Prior: 0.0% MM, 0.6% YY**
	Excluding Food, Drink, Tobacco, Energy, May	**Forecast: 0.1% MM, 1.1% YY**	**Prior: 0.0% MM, 1.0% YY**

Surveys suggest that manufacturers' price expectations are stronger than a year ago and hence we expect that output price inflation will start to tick higher. Indeed, a figure in line with our forecast would put the six-month annualised rate for the series ex tax at 1.3%.

Economic Indicators

United Kingdom Continued

Jun 19 09:30 London Time	***Retail Sales Volumes, May***	**Forecast: 0.6% MM, 5.4% YY**	**Prior: 1.3% MM, 6.9% YY**
	The weather in May was relatively warm and wet, with both rainfall and average daily temperature above average for that month. The effects of this on retail sales growth are hard to predict, because in May there is a negative correlation between rainfall and sales (ie wet weather hurts sales) and a positive correlation between temperature and sales (ie warm weather helps sales). On balance we go for another solid gain but with the possibility of erratic moves in clothing sales either way.		
Jun 17 11:00 London Time	***CBI Industrial Trends Survey, Jun***		
	Monthly Output Expectations Net Balance, Jun	**Forecast: +30%**	**Prior: +32%**
	Monthly Order Books Net Balance, Jun	**Forecast: +1%**	**Prior: 0%**
	Monthly Selling Prices Net Balance, Jun	**Forecast: +5%**	**Prior: +4%**
	Recent surveys have shown order books one standard deviation above average, with even greater strength in output expectations. We expect another buoyant reading this month, and this is likely to be reflected in continued rapid gains in manufacturing output.		
Jun 20 09:30 London Time	***Public Sector Net Borrowing, May***	**Forecast: £12.0 Billion Deficit, £23.5 Billion Deficit Fiscal Year To Date**	
	(Ex RM, APF and Financial Intervention)	**Year Ago: £13.1 Billion Deficit, £22.6 Billion Deficit Fiscal Year To Date**	
	The April fiscal data showed unusual weakness in income tax revenues, which may be connected in some way to shifts in the timing of bonuses a year ago around the drop in the top income tax rate from 50% to 45%. We look for the deficit this month to be a little lower than a year ago, with revenues boosted by the strength of the economy.		

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

Key Economic Indicators (23 June – 27 June 2014)

During the Week		**Forecast**	**Last**
07:00	UK: Nationwide House Prices, May		
07:00	Germany: Retail Sales, May (by Jun 30)		
07:00	Germany: Import Prices, May (by Jun 30)		
Monday 23 June		**Forecast**	**Last**
09:00	Euro Area: Flash PMIs, Jun		
Tuesday 24 June		**Forecast**	**Last**
07:00	Switzerland: Trade Balance, May		
08:30	Netherlands: Producer Confidence, Jun		
09:00	Germany: ifo Business Climate, Jun		
09:00	Italy: Contractual Wages, May		
09:30	UK: BBA Mortgage Advances May		
	Spain: Budget Balance, May		
14:00	Belgium: Business Confidence, Jun		
Wednesday 25 June		**Forecast**	**Last**
07:00	Germany: GfK Consumer Confidence, Jul		
07:45	France: Industrial Confidence, Jun		
08:00	Spain: Producer Prices, May		
08:30	Netherlands: GDP Details, 1Q		
09:00	Norway: LFS Unemployment, Apr		
09:00	Italy: Retail Sales, Apr		
10:00	Italy: Consumer Confidence, Jun		
11:00	UK: CBI Retail Survey, Jun		
Thursday 26 June		**Forecast**	**Last**
	European Council (to 26 June)		
07:45	France: Consumer Confidence, Jun		
08:00	Spain: Producer Prices, May		
08:30	Sweden: Producer Prices, May		
17:00	France: Jobseekers, May		
Friday 27 June		**Forecast**	**Last**
00:01	UK: GfK Consumer Confidence, Jun		
	European Council, continued		
07:45	France: Consumer Spending, May		
07:45	France: GDP Details, 1Q		
07:45	France: Producer Prices, May		
08:00	Switzerland: KOF Economic Barometer, Jun		
08:00	Spain: HICP, Jun Flash		
08:00	Spain: Retail Sales, May		
08:30	Sweden: Trade Balance, Apr		
08:30	Sweden: Retail Sales, May		
09:00	Italy: Business Confidence, Jun		
09:30	UK: Balance of Payments, 1Q		
09:30	UK: GDP, 1Q (3rd Release)		
09:30	UK: Service Sector Output, Apr		
10:00	Euro Area: Business and Consumer Confidence, Jun		
13:00	Germany: Consumer Prices, Jun Flash		

Sources: National statistical offices, central banks and Citi Research

Publication Title	Author	Date
Euro Area — Sovereign Debt Update		
BuBa's Weidmann Warns of "Sweet Poison" of Government Bond Purchases	European Economics Team	Jun 13, 2014
ECB's Mersch: ABS To Be Part Of The Solution	European Economics Team	Jun 12, 2014
ECB Officials on Risks of "Low-flation"	European Economics Team	Jun 11, 2014
Weidmann Acknowledges Risks of Un-Anchored Inflation Expectations	European Economics Team	Jun 10, 2014
ECB to Assess Efficacy of New Measures by Year-End	European Economics Team	Jun 9, 2014
Euro Area		
Spain - Housing Adjustment: Are We Nearly There?	Antonio Montilla	Jun 13, 2014
Italy - Q1 GDP Details And April Industrial Output	Giada Giani	Jun 10, 2014
ECB - Door firmly open to additional stimulus and QE in late 2014	Guillaume Menuet	Jun 5, 2014
Europe - Monthly Inflation Profiles for Selected Countries	European Economics Team	Jun 5, 2014
Euro Area - Inflation Surprises Once Again to the Downside	Giada Giani	Jun 3, 2014
Euro Area - Economic Sentiment Strengthens, But France Stays Weak	Ebrahim Rahbari/Antonio Montilla	May 28, 2014
Euro Area - Weak M3 but fall in private sector loans eases in April	Ebrahim Rahbari/Antonio Montilla	May 28, 2014
Italy - Q1 GDP Downward Surprise and Political Uncertainty	Giada Giani	May 23, 2014
European Economic Forecast Highlights - May 2014	Ann O'Kelly	May 22, 2014
Euro Area - Q1 GDP Disappoints Probably Due To Exceptionally Mild Winter	Giada Giani	May 15, 2014
Euro Area - No Pickup in NFC Net Borrowing in Q1	Antonio Montilla/Ebrahim Rahbari	May 15, 2014
ECB - Comfortable with a June rate cut (and a negative depo rate)	Guillaume Menuet	May 8, 2014
Euro Area - Strong PMIs Argue Against ECB Rate Cut on Thursday	Guillaume Menuet	May 6, 2014
Spain - A Wider Output Gap Reduces the Need for Fiscal Austerity	Giada Giani	May 6, 2014
Euro Economics Weekly		
ECB TLTRO: Ambitious But Probably Not Enough, QE Lies Ahead	Guillaume Menuet	Jun 6, 2014
Negative Deposit Rate: Limiting Risks, Limited Upside	Ebrahim Rahbari	May 30, 2014
Soft Growth, Low HICP And Weak SPF Point To ECB Cut In June	Guillaume Menuet	May 23, 2014
Long Live (s) The Rise of the Current Account Surplus	Ebrahim Rahbari	May 16, 2014
Euro Economics Weekly - How Might QE Affect Financial Conditions?	Giada Giani	May 9, 2014
ECB: Reaction Function Points to Looser Stance Ahead	Guillaume Menuet	May 2, 2014
Private Deleveraging: Picking Up, but Hurting Less	Ebrahim Rahbari	Apr 25, 2014
Portugal: "Clean Exit" or Precautionary Credit Line?	Giada Giani	Apr 17, 2014
France: Will Valls Succeed Where Others Have Failed?	Guillaume Menuet	Apr 11, 2014
The Rise of The Output Gap	Ebrahim Rahbari	Apr 4, 2014
Italy — Some Short-Term Optimism	Giada Giani	Mar 28, 2014
Euro Area: Upside Risks To Q2 GDP	Guillaume Menuet	Mar 21, 2014
The Eurozone Investment Recovery	Ebrahim Rahbari	Mar 14, 2014
Internal Devaluation in the Periphery	Giada Giani	Feb 7, 2014
Chief Economist Publications		
Global Economics View - The Long-Run Decline in Advanced-Economy Investment	Willem Buiter	Jun 12, 2014
Global Economic Outlook and Strategy - May 2014	Willem Buiter	May 21, 2014
Scandi and Switzerland		
Scandi Economics Update	Tina Mortensen	Jun 13, 2014
Sweden - Strong Labour Market Data in May	Tina Mortensen	Jun 13, 2014
Sweden - IMF: Urgent that Sweden Does More to Address Private Debt	Tina Mortensen	Jun 13, 2014
Norway - Investment Survey Indicates Large Drop in Oil Investments in 2015	Tina Mortensen	Jun 12, 2014
Sweden - Lower Inflation Supports July Rate Cut Expectations	Tina Mortensen	Jun 12, 2014
Norway - Core CPI Eases Slightly, Overshoot vs. NB Forecast a Stable 0.2pp	Tina Mortensen	Jun 10, 2014
Norway - RNR Points to Ongoing Moderate Growth, in line with NB Forecast	Tina Mortensen	Jun 9, 2014
UK		
UK - Carney Speech	Michael Saunders	Jun 13, 2014
UK - Nation of Workers	Michael Saunders	Jun 11, 2014
UK - March of the Makers Continues	Michael Saunders	Jun 10, 2014
UK - REC Survey Suggests Labour Market Still Tightening	Michael Saunders	Jun 6, 2014
UK Economics Weekly		
Implications for the UK of ECB Easing;	Michael Saunders	Jun 6, 2014
Inflation Downtrend Probably Over	Michael Saunders	May 30, 2014
Will Macro-Pru Allow "Low for Longer"?	Michael Saunders	May 23, 2014
UK Economics Weekly - Where Next for the MPC?	Michael Saunders	May 16, 2014

Source: Citi Research

Appendix A-1

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