Citi Research

Economics

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Developed Markets

Western Europe

Euro Economics Weekly

Could Eurozone Politics Return to the Fore?

- May's EU Parliamentary elections will provide an opportunity to test the support of populist NEAP's — the new, extreme or alternative parties that have seen a significant increase in support over the past two years. Early polling data suggest they could double their number of seats in the next EU Parliament to 20-25%, potentially acting as an obstacle to further integration. Yet, their impact on the current legislative agenda should be fairly limited given the difficulty in these parties joining forces, while mainstream groupings retain a large majority.

- We focus on Greece and Italy where fresh national elections could be triggered by the EU vote, even after this week's Italian government reshuffle. Early elections in Italy would probably represent a positive development on the expectation that a fresh mandate for centre-left PD Renzi would raise hopes for some progress on the reform agenda. However, early elections in Greece would probably be bad news, potentially derailing bailout negotiations and lowering hopes for near-term recovery.

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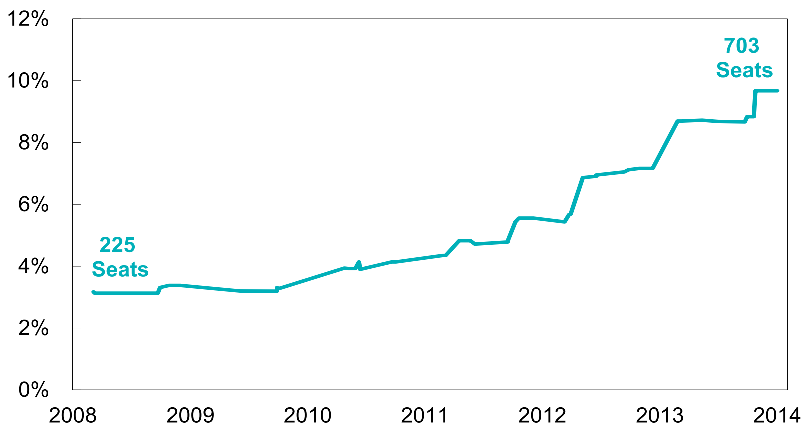
Figure 1. Citi Market Forecasts

	$/€	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
2Q 14	1.39	0.00	1.70	0.80	0.50	158	8.71	0.75	8.12	1.50	1.24	0.00	-73
4Q 14	1.40	0.00	1.80	0.80	0.75	183	8.79	0.75	7.95	1.50	1.26	0.00	-77

Source: Citi Research

Source: Citi Research

Figure 2. Eurosceptic Parliamentarians in EU Legislatures (No. of Seats and Pct. of Total), 2008-Jan 2014



Source: Citi Research, based on statistics from the 28 European Union national parliaments

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Giada Giani

Could Eurozone Politics Return to the Fore

2014 eurozone political risk temperature lower, but risks remain

The combination of OMT, the modest growth pickup and few scheduled elections this year contributed to our assessment of an improved eurozone political risk outlook for 2014. But the increased turbulence in Italian politics this week shows that some political risks remain. The risk of early elections in Greece and Italy cannot be ruled out, while May's European Parliamentary elections will likely see a significant boost in the number of eurosceptic MEPs in parliament. We also note that the German Constitutional Court decision to refer the legality of the OMT to the European Court of Justice could, if market conditions deteriorated, increase political risks. We will continue to be cautious about eurozone political risks into the 2015 elections cycle, particularly with unemployment remaining high.

Eurosceptic parties may end up getting 20-25% of seats in EU Parliament

This year's most significant EU political signpost is the May European Parliamentary elections, which will provide an opportunity to test the support of populist NEAP's — the new, extreme or alternative parties that have seen a significant increase in support over the past two years[1]. Eurosceptic parliamentarians in EU legislatures have tripled since the financial crisis began (see Figure 2 on the front page). Preliminary polling data suggest they may end up controlling 20-25% of the seats in the next European Parliament, from 13% at present, potentially acting as an obstacle to further European integration and increasing the risk of populist legislation. Note, however, that the EP lacks the power to interfere over bailouts. Although such an increase in the representation of fringe parties would be a clear negative, we think their direct impact on actual policy in the Eurozone may be somewhat limited in the near-term. This is partly because the NEAPs from different EU countries are a diverse bunch and seem unlikely to unify behind a concrete legislative agenda, while the mainstream groupings will retain a large majority (with NEAP's presence possibly enforcing more cooperation among them). Rather, a strong performance from non-mainstream parties in EP elections could spell trouble ahead for the national election cycle that will resume in 2015.

Polls suggest NEAP's support will increase, but mainstream parties together would retain a large majority

Opinion polls measuring voting intentions for the EU Parliament are still scant. Figure 3 reproduces data collected by an Italian website (ScenariPolitici.com) that put together several opinion polls conducted in January (and then averaged them) on voting intentions in each one of the 28 EU member states. Using these data and the allocation by country of the 751 seats up for grabs in the EU Parliament, they projected MEPs seat allocation for the next EU Parliament election. These data suggest that the percentage of MEPs not affiliated to any European political group would increase from 4% in the current parliament, to 11% in the new one. This group would include among others representatives of Italy's M5S, Greece's Golden Dawn, Germany's AfD and France's Front National.

In addition, the far-left group of the political spectrum (United Left) is also expected to gain seats relative to the current distribution, moving from 5% to 8% (this group includes among others Greece's SYRIZA). Adding the hard eurosceptic group (mainly represented by UK's UKIP), the share of extremist and alternative parties may rise to about 23% of the seats, up from 13% at present. These data also suggest a neck –and-neck position between the two largest European political groups — European People's Party (EPP) and the Socialists & Democrats (S&D) — both at around 30%. The Socialists would be gaining some 4ppt relative to the 2009 election and the centre-right group would be some losing 6ppt.

[1] EU Parliamentary election will be held between 21 and 25 May in all 28 EU member states.

The worry that these groups may team up to support an anti-EU agenda may be overblown…

Despite the attempts of Geert Wilders of Dutch PVV and Marine Le Pen of France's Front National to put together a hardline bloc, several of the NEAP parties have already expressed deep reservations about working with one another. Political scientist Cas Mudde, an expert on both European politics and fringe political movements, points to the European far-right's history of disorganization. Many of the non-affiliated parties, like Hungary's Jobbik or the British National Party, are alleged to be actively racist or anti-Semitic, which would probably rule out an alliance even with a right-wing party like France's Front National, let alone moderate eurosceptic or left-wing groups.[2]

Figure 3. Latest Polling Suggests a Sizeable Gain for Nationalist Parties in the Next European Parliament

Abbrev.	Group Name	Ideology	Typical Member Party	Current Polling	Change in Seats (Last)
GN	European United Left-Nordic Green Left	Left-wing	Syriza (Greece)	59	↑24 (35)
S&D	Progressive Alliance of Socialists and Democrats	Social democratic	PSOE (Spain)	219	↑24 (195)
Greens-EFA	The Greens-European Free Alliance	Greens	The Greens (Germany)	33	↓25 (58)
ALDE	Alliance of Liberals and Democrats for Europe	Liberal	VVD (Netherlands)	64	↓21 (85)
EPP	European People's Party	Christian democratic	Forza Italia (Italy)	222	↓53 (275)
ECR	European Conservatives and Reformists	Conservative, soft eurosceptic	Law and Justice (Poland)	42	↓14 (56)
EFD	Europe of Freedom and Democracy	Eurosceptic	UKIP (UK)	33	←→ (33)
NI	Independents	Mixed, mostly nationalist	Front National (France)	79	↑50 (29)
			Total Seats	**751**	**766**

Sources: ScenariPolitici.com and Citi Research

…but watch out for the reactions of national governments to stop the bleeding of votes towards the NEAPs

In the end, the European Parliament's subordinate position in the EU political system means that the policy ramifications of a resurgent European fringe should be limited. Although the Lisbon Treaty expanded some of the EP's duties, it is still not the sole legislative authority in the Union. The Treaty explicitly gives the EP that authority jointly with the Council. Nor can the EU Parliament introduce most legislation on its own accord: only the Commission can do that. This puts it in a subordinate position to what a parliament's role is in, say, the UK or the other member states. We argue that the bigger worry for markets is the reactions of the national governments as they lose support to the NEAPs and move to stop the bleeding. The textbook case is Prime Minister David Cameron's support for an in-out referendum on British EU membership, as he seeks to maintain Tory support against a challenge from the resurgent eurosceptic UK Independence Party.

Swiss referendum on immigration has placed the issue on European stage

We might expect similar reactions to the victorious February 9 referendum in Switzerland that would set quotas on immigration. Though the referendum itself has had little to no impact on Swiss capital markets, many European NEAPs are winning support with an anti-immigration stance. Now that Switzerland has placed the issue on the European stage, national leaders will attempt to counteract or co-opt the NEAPs' positions, with unforeseen consequences for policy and European integration in the middle term.

Italy and Greece as main sources of potential political risks

We reckon the EU election will have meaningful implications for domestic politics in Italy and Greece. In fact, the upcoming confrontation with the EU ballot was probably a reason behind the change at the helm of the Italian government this week, amid a falling consensus for PD-led government. With both Italy and Greece still struggling (more than others) to see economic optimism spreading through the economy, we think these two prominent cases are worth a closer look.

[2] Cas Mudde. "The Le Pen-Wilders Alliance and the European Parliament: Plus Ça Change, Plus C'est La Même." *The Monkey Cage* blog. *The Washington Post*. February 11, 2014. "A European Shutdown? The 2014 European Elections and the Great Recession." *The Monkey Cage* blog. *The Washington Post*. November 4, 2013.

Italy — a new government, again

PM Letta resigns, to be replaced by his party leader Matteo Renzi

The clash between the newly-elected reformist leader of the ruling party PD, Matteo Renzi, and his fellow party member, PM Enrico Letta, has escalated this week and finally led to Letta handing in his resignation from Prime Minister to President Napolitano on Friday. The President will consult the leaders of the parties in parliament (reportedly over the weekend) after which he will likely give the mandate to Renzi to create a new government. Renzi's proposal for government must pass through both houses of parliament, which should happen early next week. Besides the battle between the two senior members of PD, the change at the helm of the Italian government was probably induced by a constantly decreasing consensus for the Letta administration in recent months due to its perceived inaction on key economic reforms, especially after the departure of Silvio Berlusconi from the governing coalition which suggested more room for manouvre. Calls for a change of strategy from the business community had intensified in recent weeks, while Renzi's proposal for electoral reform created further divisions among the coalition parties, probably also contributing to the end of the Letta administration.

Italian political landscape remains very fluid

A change of government was probably inevitable also because of the significant changes in the political landscape over the past 12 months, since the last election in Feb 13. The coalitions that backed the formation of the Letta government in April 2013 no longer exist: centre-right PdL has split, with Mr Berlusconi's re-launched Forza Italia moving into the opposition ranks and only a small fraction of the former PdL still supporting the government (redenominated Nuovo Centrodestra, NCD). The centrist coalition led by Mario Monti also broke up (although its MPs are still officially supporting the government), while Renzi's PD leadership has changed the shape of Italy's single largest party.

Figure 4. Italy — Voting Intentions, Latest Polling Average for the Italian Chamber of Deputies, February 2013

Alignment	Party Grouping	% Vote	Change Since Feb. 2013 Election
Center-Left	*Partito Democratico* (Renzi/Letta)	31%	↑ 6% (25%)
	Sinistra Ecologia Liberta (Vendola)	3%	↔ (3%)
	Others	1%	↔ (1%)
Center-Right	*Forza Italia* (Berlusconi)	22%	↔ (22%)
	Nuovo Centrodesta (Alfano)	5%	—
	Lega Nord (Salvini)	4%	↔ (4%)
	Others	6%	↓ 2% (4%)
Center	*Scelta Civica* (Monti)	2%	↓ 9% (11%)
Outsider	Five Star Movement	22%	↓ 5% (26%)

Sources: Termometro Politico and Citi Research

A new Renzi-led government is a positive for Italy and short-term rating outlook…

We think the government reshuffle is a positive for Italy, as Renzi's reformist agenda, his ability to speak to a broader audience than traditional PD voters and his ability to reach agreements with the main centre-right opposition party should raise hopes for progress on the reform agenda. Renzi's ability to agree a controversial, long-pending, electoral reform in less than a month with Silvio Berlusconi bodes well for his ability to push through other much-needed reforms in the future. Over the past two years, Italy has been lagging behind most of the other periphery euro area countries on the structural reform agenda and this has been one of the main factors weighing negatively on its sovereign rating. The appointment of a new government with a strong reformist agenda may at least buy some time before rating agencies reassess the political situation and take new rating decisions.

…although Renzi retains some weaknesses of his predecessor

However, Renzi retains some weaknesses of his predecessor. First, despite pledging to stay in office until the end of the current legislature (2018), he will have to rely on the same parliamentary majority, in particular on the support of the small centrist parties which hold the balance of power in the Senate. The small centre-right party NCD may well still oppose Renzi's electoral reform proposal (which most likely would force them back into a coalition with Berlusconi ahead of new elections). Second, although he was elected in PD primaries with a large majority and an unexpectedly large turnout, like his predecessor Renzi still lacks the democratic legitimacy normally obtained through the ballot boxes.

Risks of a surprisingly positive result by populist M5S at the EU election should not be underestimated

The upcoming EU election will represent the first crucial test for the new government. All mainstream parties fear that the populist anti-establishment 5 Star Movement (M5S) will muster another unexpectedly large success (as it did in Feb-13), amid voters' ever-growing discontent with the political elite and still widespread concerns about the economy. The likelihood of a protest vote in favour of M5S in EU elections may be higher than in the national ballots, as voters express their discontent without impacting too much domestic politics. Two recent polls (by IPR marketing on 5 February and by Tecne' on 13 February) which specifically asked voting intentions at the EU election suggest this could actually be the case. Both polls show M5S at around 25.5%, not far from PD's 27.5-29.5% range — a gap that is significantly smaller than the average gap between PD and M5S at the national polls (11ppt on average in January). Therefore, while data suggest a large M5S victory is unlikely, a fluid political landscape, lack of specific polls on voting intentions in the EU election and the poorm track-record of polls in predicting last year's M5S success all suggest some caution in drawing quick conclusions (see Figure 4).

Early elections are still possible as soon as May…

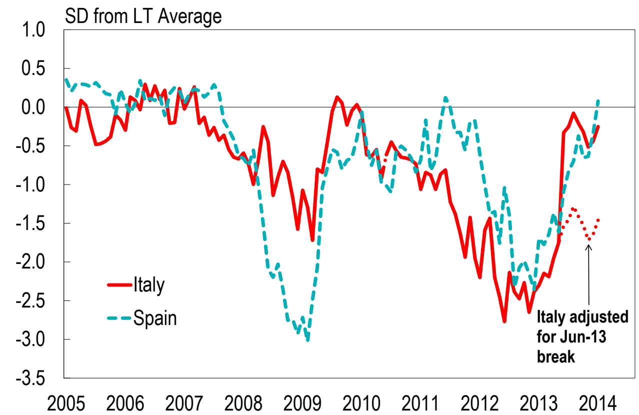
PD fears it could lose out from being the only main Italian party defending the European cause during the electoral campaign, since both M5S and Berlusconi's Forza Italia are likely to campaign strongly on anti-European grounds. If M5S posts an unexpected electoral success in May or/and PD suffers a severe defeat, we reckon that chances of fresh elections later on this year will increase considerably, especially if in the meantime Renzi has been able to push through electoral reform. In fact, we think early elections are still possible (although less likely now than a week ago) as soon as in May, on the same day as the EU election.[3]

…but even early elections would probably be better than trying to preserve the status quo

However, we think that even in case of early elections becoming necessary as PD looks for a fresh democratic mandate, this would be better for Italy than trying to preserve the status quo (although without an electoral reform and abolition of the Senate the risk of hung parliaments remains, see Box). The last 18 months' political impasse, due to an unworkable broad-coalition in power, has widened further the gap between Italy and the other periphery countries in the progress on the reform agenda. Capitalizing on his recent increase in popularity, Mr Renzi may have a chance to bring in a stable centre-left coalition, possibly also getting some support among M5S and centrist voters.

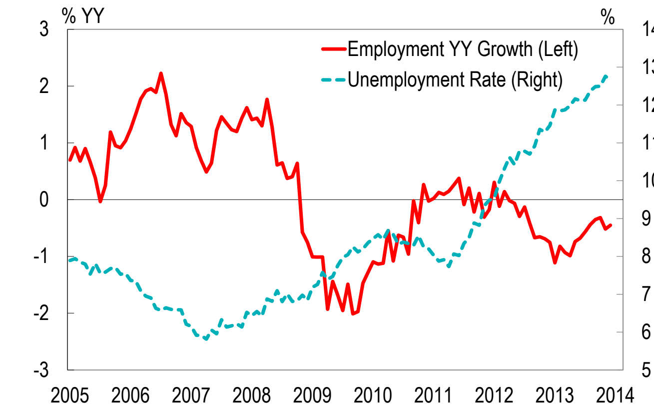
[3] The time window for the President to dissolve the Parliament and call national elections is a minimum of 45 days before the vote, meaning there is time to decide until late March/early April.

Figure 5. Italy and Spain — Consumer Sentiment, 2005-Jan 14



Sources: EU Commission, Haver Analytics and Citi Research

Figure 6. Italy — Labour Market Indicators, 2005-Dec 13



Sources: Haver Analytics and Citi Research

The economy is surely not helping the chances of success for the ruling party PD

The economy, on the other hand, may not offer much support to Mr. Renzi. The Italian recovery has been lagging behind other euro area countries. The consumer confidence index appears to have moved back close to its long-run average (-0.3 SD in Jan-14), but we argue this is a misleading indicator at present because of a change in methodology which produced a break in the series in Jun-13 (when the index jumped from -1.8 to -0.3 standard deviations below its LT mean). When we adjusted for this break (assuming that the June MM change was in line with the MM trend of the previous five months), the level of consumer confidence has really stopped improving since last summer.[4] Italy seems to be lagging far behind relative to the gains in consumer sentiment recorded in other periphery countries, such as Spain (see Figure 5). Similarly, labour market data up to December have yet to show any sign of stabilization, as employment continues to fall (albeit slower than in 2012-early 2013) and the unemployment rate is still rising (see Figure 6).

An electoral system to guarantee better governability

Relative to the old system, Renzi's proposal for a new electoral law includes a key feature — that is a run-off ballot between the first two parties/coalitions, when no one reaches a certain minimum percentage of votes (currently agreed at 37%). If one party/coalition exceeds this threshold in the first round (but is still short of 50%), that party/coalition would be granted a *"winner's bonus"* and obtain a parliamentary majority. A second proposal by Renzi is the abolition of the Senate in its current form — a necessary complementary step for a workable electoral system. At the moment the Senate is elected in regional constituencies, while the Lower House is elected in national constituencies — something that could still lead to hung parliaments even with the new electoral law proposal. In the new setting, instead, senators will no longer be elected but the Senate will be formed with representatives of regional and local authorities. More importantly, senators will not be called to cast a confidence vote on new governments and will not vote for budgets. Mr. Renzi has said the proposal has the support of the main political parties.

[4] We argue that there was no particular reason for consumer confidence to behave in a significantly different way in June 2013 relative to the previous months. Other assumptions about the MM change in June (taking for example the average change in the other euro area countries and applying it to Italy) would lead to a very similar conclusion.

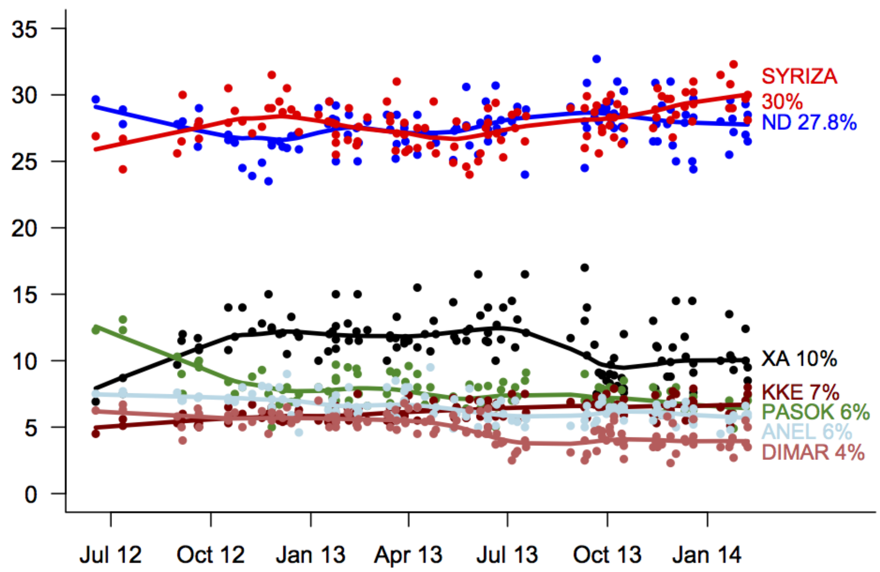
If approved, the new institutional framework would enforce the formation of two main coalitions (a centre-right and a centre-left one) before the election and this would reduce sharply the chances of the M5S party being involved in the next government (given its opposition with teaming up with any mainstream party). An agreement on the electoral system should be seen as an important step for Italy, in our view, as the political impasse of the last couple of years shows the inability of broad-coalitions (ie, centre-right and centre-left together) to come to agreements of any sort. The new system would improve governability and raise hopes that any future government (either a centre-left or a centre-right one) could be able to adopt more relevant economic reforms. The abolition of the Senate requires a constitutional change and hence 2/3 majority in parliament: this implies an approval process of a few months, definitely too long for it to be ready for potential early elections in May (for which the electoral reform law could be ready).

Greece — EU elections may lead to national early elections later this year

EU election likely to be a much riskier business for Greece than for Italy

EU elections, on Sunday May 25, will be held jointly with municipal elections in Greece. The Greek governing coalition's majority has been further eroded since the last national elections in July 2012, with only a one-seat parliamentary majority left. Compliance with bailout conditionality on structural reforms has stalled since last summer and troika negotiations on the current review have been on hold since last September, while recent comments by European policymakers suggest no deal may be reached at least until March. Despite delaying unpopular policy decisions, the main ruling parties — centre-right New Democracy and Socialist PASOK — have been losing popularity in the last few months, while the main opposition left party, SYRIZA, is gaining support and it is now leading the polls, albeit by a small margin. The other extremist opposition party, Golden Dawn, has lost some support during the autumn, but it remains well anchored at around 10% of voting intentions and well ahead of centre-left PASOK (see Figure 7), that has seen its support collapse in recent years.

Figure 7. Greece — Voting Intentions, Jun 2012-Feb 2014

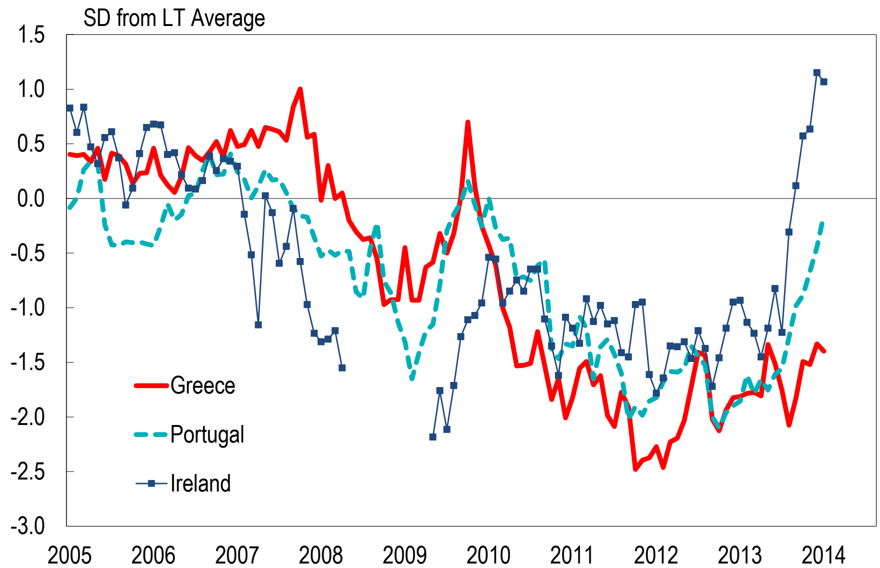


Note: Poll Trend of 120 surveys conducted by major Greek pollsters through February 7, 2014.
Source: Citi Research.

Slight improvements in the business sector not yet feeding through to the rest of the economy

We think that government weakness and lack of perceived improvements in the economy are largely weighing on the incumbents' popularity. As a common feature with Italy, Greek consumer confidence improved markedly in H2 12, but has failed to post further meaningful gains throughout 2013. This is in sharp contrast with other bailed-out countries such as Portugal or Ireland (see Figure 8). The mildly positive economic signs from the Greek business sector (manufacturing PMI rose to 51.2 in Jan-14) have hardly spread to the rest of the economy so far. According to Q3 non-financial account data, the household sector's saving rate is still largely negative (at -5.2% of disposable income), and real private consumption was still falling by around 8% YY, although retail sales data suggest a less negative reading for Q4. Moreover, November job market data released this week showed that net employment creation was still very negative (-3.1%YY vs. -2.1% YY in Sept-13) although less so than a year before. There are few signs that the tourism and export-driven mild improvement in the economy will spread to other economic sectors in the next few months.

Figure 8. Greece, Ireland and Portugal — Consumer Sentiment, 2005-Jan 14



Sources: EU Commission, Haver Analytics and Citi Research

Positive primary surplus key strength for government ahead of election

The main positive achievement the Greek government can present ahead of the election is a yet-to-be-confirmed fiscal primary surplus in 2013 (of €1.5bn or 0.8% of GDP, according to government estimates). If confirmed, this would be a key attainment, as the government could already start pledging some of these resources to be redistributed to voters. More importantly, the government is now trying to leverage the achieved fiscal primary surplus to reach an agreement on further debt relief from European creditors ahead of the elections. Debt relief on bilateral loans (€53bn out of the total €215bn disbursed so far) — 20-year maturity extension and 50bp interest rate cut reportedly under discussion — may serve to boost popularity for the government if agreed before the elections, although they would do little to reduce Greece's public debt burden.

In our view, however, it is difficult to believe that beyond further verbal support for Greece and promises for future debt relief, European creditors are willing to approve more concrete actions before the May election, given the lack of progress on conditionality by Greece and given how sensitive the issue is among eurosceptic parties in creditor countries[5].

The economy and troika negotiations crucial in shaping electoral outcome

If, as we suspect, progress on both fronts is slow and not noticeable enough to markedly reverse the current polls, we think there is a growing probability that ruling parties ND and PASOK will suffer a severe defeat at the May EU and municipal elections. This could precipitate a government crisis and force early elections later on this year. In the event of early elections, SYRIZA is likely to obtain a much better result relative to the two ruling parties compared to the Jul-12 outcome and will necessarily be involved in the formation of the next Greek government. If not because of a defeat of ruling parties in the EU election in 2014, early elections are still likely in 2014/early 2015, as SYRIZA has already said they would attempt to prompt early elections by blocking any candidate for President of the Republic put forward by the ruling parties (the election of the President requires a 2/3 majority in Parliament).

SYRIZA victory would take debt write-off back on the table of negotiations

While it remains uncertain what would happen in this case, SYRIZA's positions have clearly moved relative to the last time Greece went to the polls in mid-2012. Calls for Greece to leave the monetary union have been absent from the public debate, but a SYRIZA-led government would definitely take the troika negotiations to a different level compared to the current government. SYRIZA leader Alexis Tsipras said recently that if elected his party would seek a debt write-off of 60% of GDP, and it would refuse to take on additional loans. It would also use the threat of stopping paying interest on the official loans, Tsipras said, in case a consensual solution is not reached on the debt write off.

[5] See "Europe Sovereign Debt Crisis – Greece: Third Bailout Not To Be Agreed Until Mid-Year", 4 February 2014.

Key Economic Indicators (17 February – 21 February 2014)

		Forecast	Last
Monday 17 February		**Forecast**	**Last**
10:00	Italy: Current Account, Dec		
10:00	Greece: HICP, Jan		
	Euro Area: Eurogroup Meeting, Brussels		
Tuesday 18 February		**Forecast**	**Last**
	EU: EcoFin Meeting, Brussels		
07:00	EU-27: New Car Registrations, Jan		
08:30	Sweden: Consumer Prices, Jan	-0.9% MM, 0.0% YY	0.3% MM, 0.1% YY
	CPIF, Jan	-0.8% MM, 0.7% YY	0.35 MM, 0.8% YY
09:00	Italy: Trade Balance, Dec		
09:00	Euro Area: Current Account, Dec		
09:00	Norway: Trade Balance, Jan		
09:30	UK: Consumer Prices, Jan	-0.4% MM, 2.1% YY	0.4% MM, 2.0% YY
	CPI Ex Food, Drink, Tobacco, Energy, Jan	-0.6% MM, 1.9% YY	0.1% MM, 1.7%YY
	Retail Prices, Jan	-0.4% MM, 2.6% YY	0.5% MM, 2.7% YY
	RPIX – Excludes Mortgages, Jan	-0.4% MM, 2.7% YY	0.5% MM, 2.8% YY
09:30	UK: Producer Input Prices, Jan	-0.6% MM, -2.9% YY	0.1% MM, -1.2% YY
09:30	UK: Producer Output Prices, Jan	0.2% MM, 0.8% YY	0.0% MM, 1.0% YY
	Ex Food, Drink, Tobacco, Energy, Jan	0.1% MM, 0.8% YY	0.1% MM, 1.0% YY
10:00	Germany: ZEW Current Situation, Feb	38.2	41.2
	ZEW Economic Sentiment	59.7	61.7
Wednesday 19 February		**Forecast**	**Last**
08:30	Netherlands: Consumer Spending, Dec		
09:30	UK: LFS Unemployment, Oct-Dec	-194K QQ, 7.0% Rate	-167K QQ, 7.1% Rate
	Claimant Count Unemployment, Dec	-30K MM, 3.6% Rate	-24K MM, 3.7% Rate
09:30	UK: MPC Minutes		
10:00	Euro Area: Construction Output, Dec		
	Greece: Current Account, Dec		
Thursday 20 February		**Forecast**	**Last**
07:00	Switzerland: Trade Balance, Jan		
07:00	Germany: Producer Prices, Jan	0.4% MM, -0.6% YY	0.1% MM, -0.5% YY
07:45	France: HICP, Jan	-0.4% MM, 1.0% YY	0.4% MM, 0.8% YY
	Consumer Prices, Jan	-0.4% MM, 0.8% YY	-0.3% MM, 0.7% YY
	CPI Ex Tobacco Index, Jan	125.21	125.82
08:30	Netherlands: Consumer Confidence, Feb		
08:30	Netherlands: Unemployment, Jan		
09:00	Italy: Industrial Orders, Dec		
09:00	Euro Area: Manufacturing PMI, Feb Flash	54.2	54.0
	Services PMI, Feb Flash	52.5	51.6
	Composite PMI, Feb Flash	53.6	52.9
11:00	UK: CBI Industrial Trends Survey – Output Expectations, Feb	+24%	+23%
	CBI Order Books, Feb	+6%	-2%
	CBI Selling Prices, Feb	+10%	+20%
11:00	Ireland: Consumer Prices, Jan		
15:00	Euro Area: Consumer Confidence, Feb Flash	-10.5	-11.7
Friday 21 February		**Forecast**	**Last**
08:00	Sweden: Consumer Confidence, Feb	103.7	103.2
	Manufacturing Confidence, Feb	106.9	108.2
09:00	Italy: Consumer Prices, Jan Final		
09:30	UK: Retail Sales Volumes, Jan	-2.0% MM, 4.0% YY	2.6% MM, 5.3% YY
09:30	UK: Public Sector Net Borrowing, Jan	£7.0 Billion Surplus	Year Ago: £6.7 Billion Surplus
	Fiscal Year to Date	Apr13-Jan14: £86.4 Billion Deficit	Apr12-Jan13: £94.3 Billion Deficit
	Spain: Trade Balance, Dec		

Sources: National statistical offices, central banks and Citi Research

Economic Indicators

Euro Area

Feb 20 09:00 London Time	***Manufacturing PMI, Feb Flash*** ***Service PM, Feb Flash*** ***Composite PMI, Feb Flash***	**Forecast: 54.2** **Forecast: 52.5** **Forecast: 53.6**	**Prior: 54.0** **Prior: 51.6** **Prior: 52.9**
	PMIs likely posted another increase in February, confirming the positive momentum in the euro area economy. Manufacturing PMI probably edged higher only slightly, given two large monthly gains in Dec and Jan. Services PMI on the other hand may have risen by a larger extent, as it is still catching up with previous improvements in the manufacturing sector. At these levels – 53.5 for the composite PMI – PMIs in the past have been consistent with quarterly GDP growth of around 0.4% QQ.		
Feb 20 15:00 London Time	***Consumer Confidence, Feb***	**Forecast: -10.5**	**Prior: -11.7**
	With households' unemployment expectations rising slightly in the past couple of months, in contrast with the constant improvements seen in 2013 and recent declines in equity prices, we expect the February consumer sentiment to still post a gain but a smaller one than in previous months. Much reduced fiscal austerity and falling inflation have mainly contributed to the improvement in consumer confidence over the past year or so.		

Germany

Feb 18 10:00 London Time	***ZEW Current Situation, Feb*** ***ZEW Economic Sentiment, Feb***	**Forecast: 38.2** **Forecast: 59.7**	**Prior: 41.2** **Prior: 61.7**
	We expect the ZEW survey to be weaker in February for both the current indicator and the expectations reading. The current situation reading registered a large increase in January, but recent data have in fact been somewhat soft (even though some of the data was released after the ZEW survey had already been carried out). Meanwhile, the economic sentiment index has been around multi-year highs in recent months which makes a small correction likely.		
Feb 20 07:00 London Time	***Producer Prices, Jan***	**Forecast: 0.4% MM, -0.6% YY**	**Prior: 0.1% MM, -0.5% YY**
	We expect producer prices to rise on seasonal factors in December. Unit labour costs are rising, but the strong euro, low energy prices and still-weak external conditions (weakening the price of intermediate goods imports) continue to resist upward price pressures for producers.		

France

Feb 20 07:45 London Time	***CPI – EU Harmonised, Jan*** ***Consumer Price Index, Jan*** ***CPI Ex Tobacco Index, Jan***	**Forecast: -0.4% MM, 1.0% YY** **Forecast: -0.4% MM, 0.8% YY** **Forecast: 125.21**	**Prior: 0.4% MM, 0.8% YY** **Prior: -0.3% MM, 0.7% YY** **Prior: 125.82**
	French headline annual inflation rates are expected to increase only modestly in January despite the VAT rate hike that came into effect on January 1, 2014. This decision dates back from the 2013 budget, when the government needed to find revenues to finance its Competitiveness Pact, giving firms a tax credit designed to lower their labour costs. Given the weakness of economic activity in the 2H-13 (GDP growth expected to average 0.1% QQ), we are lowering our forecast of the VAT pass-through, expecting most of it to be absorbed by reducing profit margins.		

Sweden

Feb 18 08:30 London Time	***Consumer Prices, Jan*** ***CPIF, Jan***	**Forecast: -0.9% MM; 0.0% YY** **Forecast: -0.8% MM; 0.7% YY**	**Prior: 0.3% MM; 0.1% YY** **Prior: 0.3% MM; 0.8% YY**
	In January, we expect to see a reversal of the high December prices for travel, clothes and vegetables. Swedish January CPI is notoriously difficult to predict, partly due to the annual impact of revisions to weightings and the historic forecast errors this month are twice as large as for the average month. For comparison, the Riksbank's CPI forecast is 0.0% and it sees CPIF at 0.6% YY.		
Feb 21 08:00 London Time	***Consumer Confidence, Feb***	**Forecast: 103.7**	**Prior: 103.2**
	Rising home prices and an improving labour market should continue to support confidence. Current levels of consumer confidence suggest that private consumption will accelerate this year		
Feb 21 08:00 London Time	***Manufacturing Confidence, Feb***	**Forecast: 106.9**	**Prior: 108.2**
	Following strong gains in recent months (confidence at highest level since Jun-11), we expect manufacturing confidence to fall slightly back in February. We note that hard data in Sweden now slowly has started to catch up with sentiment data.		

United Kingdom

Feb 18 09:30 London Time	***Consumer Prices, Jan*** ***CPI Ex Food, Drink, Tobacco, Energy, Jan*** ***Retail Prices, Jan*** ***RPIX – Excludes Mortgages, Jan***	**Forecast: -0.4% MM, 2.1% YY** **Forecast: -0.6% MM, 1.9% YY** **Forecast: -0.4% MM, 2.6% YY** **Forecast: -0.4% MM, 2.7% YY**	**Prior: 0.4% MM, 2.0% YY** **Prior: 0.1% MM, 1.7% YY** **Prior: 0.5% MM, 2.7% YY** **Prior: 0.5% MM, 2.8% YY**
	We expect CPI inflation will stay around the 2% target in these figures, although base effects from a fairly weak core CPI reading a year ago may prevent the YY rate from slipping further. Food price inflation may well slow further, but we factor in a small rise in household gas and electricity prices this month. Looking forward, CPI inflation is likely to remain around the 2% target in coming months, averaging perhaps a little below 2% over the year as a whole.		
Feb 18 09:30 London Time	***Producer Input Prices, Jan***	**Forecast: -0.6% MM, -2.9% YY**	**Prior: 0.1% MM, -1.2% YY**
	With the stronger pound and slightly weaker commodity prices, we expect to see another decline in input prices (the eighth in the past 10 months), producing the sharpest YY decline in input prices since 2009. This disinflationary backdrop will, we expect, help cap CPI inflation in the next year or two.		

Economic Indicators

United Kingdom continued			
Feb 18	***Producer Output Prices, Jan***	**Forecast: 0.2% MM, 0.8% YY**	**Prior: 0.0% MM, 1.0% YY**
09:30	***Output Prices Ex Tax, Jan***	**Forecast: 0.2% MM, 0.9% YY**	**Prior: -0.1% MM, 1.1% YY**
London Time	***Excluding Food, Drink, Tobacco, Energy, Jan***	**Forecast: 0.1% MM, 0.8% YY**	**Prior: 0.1% MM, 1.0% YY**
	The output price data are not seasonally adjusted and often record a relatively high gain in January on start-of-year price hikes. So we would focus more on the YY change than the MM change as a guide to the trend and expect that base effects from the 0.4% MM gain seen a year ago will bring the YY rate a little lower this month.		
Feb 19	***LFS Unemployment, Oct-Dec***	**Forecast: -194,000 QQ, 7.0% Rate**	**Prior: -167,000 QQ, 7.1% Rate**
09:30	***Claimant Count Unemployment, Jan***	**Forecast: -30,000 MM, 3.6% Rate**	**Prior: -24,000 MM, 3.7% Rate**
London Time			
	We expect this release will show the jobless rate falling to the MPC's 7% threshold, with the single month LFS figure for December falling well below 7%. The single month figure for September already fell to 7.1% and, with the LFS based on a rolling 3-month sample, the people surveyed in December will be largely the same as those surveyed in September. Hence, with rapid job growth (4Q is likely to see record job growth of about 280K QQ), we expect the single month figure to be down to about 6.7%. The 3-month average is likely to fall below 7% soon.		
Feb 20	***CBI Industrial Trends Survey, Feb***		
11:00	***Monthly Output Expectations Net Balance, Feb***	**Forecast: +24%**	**Prior: +23%**
London Time	***Monthly Order Books Net Balance, Feb***	**Forecast: +6%**	**Prior: -2%**
	Monthly Selling Prices Net Balance, Feb	**Forecast: +10%**	**Prior: +20%**
	This year, as often happens, the January survey showed a dip in order books but price expectations rising. We expect these trends – which seem to be a seasonal norm – to unwind a bit in the February survey. A reading in line with our expectations would put both output expectations and order books about one standard deviation above average, and hence would be consistent with continued rapid output growth.		
Feb 21	***Retail Sales Volumes, Jan***	**Forecast: -2.0% MM, 4.0% YY**	**Prior: 2.6% MM, 5.3% YY**
09:30			
London Time	The January retail sales data are often quite volatile, producing either a gain of more than 1% MM, or a decline, in 13 of the last 15 years (the most of any month and compared to an average of seven such readings across all other months). For this year, we expect the January figures to show a large drop, largely reversing the erratic gain in December, although leaving volumes in the last three months up by 0.9% from the prior three months.		
Feb 21	***Public Sector Net Borrowing, Jan***	**Forecast: £7.0bn surplus, £86.4 billion deficit fiscal year to date**	
09:30	***(Ex RM, APF and Financial Intervention)***	**Year Ago: £6.7bn surplus, £94.3 billion deficit fiscal year to date**	
London Time			
	The January figures usually benefit from a seasonal surge in payments of income tax and corporation tax, and we expect another surplus this time. Given seasonal factors, the best comparison is versus a year ago and on that basis we expect a modest improvement of £0.3bn or so.		

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

Key Economic Indicators (24 February – 28 February 2014)

During the Week		Forecast	Last
07:00	Germany: Retail Sales, Jan (by 28 Feb)		
07:00	Germany: Import Prices, Jan (by 28 Feb)		
07:00	UK: Nationwide House Prices, Feb		
Monday 24 February		**Forecast**	**Last**
08:30	Netherlands: Producer Confidence, Feb		
09:00	Germany: ifo Business Climate, Feb		
10:00	Euro Area: HICP, Jan Final	0.7% YY	0.8% YY
14:00	Belgium: Business Confidence, Feb		
Tuesday 25 February		**Forecast**	**Last**
07:00	Germany: GDP Details, 4Q		
07:45	France: Business Confidence, Feb		
08:00	Spain: Producer Prices, Jan		
09:00	Italy: Retail Sales, Dec		
09:30	UK: BBA Mortgage Advances, Jan		
10:00	Italy: Consumer Confidence, Feb	98.5	98.0
10:00	EU Commission's Winter Economic Forecasts		
11:00	UK: CBI Retail Survey, Feb		
Wednesday 26 February		**Forecast**	**Last**
07:00	Germany: GfK Consumer Confidence, Mar		
08:30	Sweden: Retail Sales, Jan	0.5% MM	-0.8% MM
09:00	Norway: LFS Unemployment Rate, Dec	3.5%	3.5%
09:00	Italy: Contractual Wages, Jan		
09:30	UK: GDP, 4Q (2nd Release)	Provisional: 0.7% QQ, 2.8% YY	3Q: 0.8% QQ, 1.9% YY
09:30	UK: Service Sector Output, Dec	0.3% MM, 3.1% YY	0.4% MM, 2.6% YY
17:00	France: Jobseekers, Jan		
Thursday 27 February		**Forecast**	**Last**
06:45	Switzerland: GDP, 4Q		
07:45	France: Consumer Confidence, Feb		
08:00	Spain: GDP Details, 4Q		
08:15	Switzerland: Unemployment Rate, 4Q		
08:30	Sweden: Household Lending, Jan	5.0% YY	4.9% YY
08:30	Sweden: Trade Balance, Jan		
08:55	Germany: Unemployment, Feb		
09:00	Italy: Business Confidence, Feb	98.0	97.7
09:00	Euro Area: M3, Jan	1.2% YY	1.0% YY
09:30	UK: Migrations Statistics Quarterly Report		
10:00	Euro Area: Economic Sentiment, Feb	101.3	100.9
13:00	Germany: Consumer Prices, Feb Flash		
Friday 28 February		**Forecast**	**Last**
00:01	UK: GfK Consumer Confidence, Feb		
07:45	France: Consumer Spending, Jan		
07:45	France: Producer Prices, Jan		
08:00	Spain: HICP, Feb Flash		
08:00	Switzerland: KOF Economic Barometer, Feb		
08:30	Sweden: GDP, 4Q	0.4% QQ	0.1% QQ
08:30	Sweden: Producer Prices, Jan		
09:00	Norway: Registered Unemployment Rate, Feb	2.9%	3.0%
09:00	Norway: Retail Sales, Jan	0.1% MM	0.1% MM
09:00	Italy: Unemployment Rate, Jan	12.7%	12.7%
10:00	Italy: HICP, Jan Flash	0.5% YY	0.6% YY
10:00	Euro Area: Unemployment Rate, Jan	12.0%	12.0%
10:00	Euro Area: HICP, Feb Flash	0.6% YY	0.7% YY
10:00	Greece: Retail Sales, Dec		
	Spain: Current Account, Dec		

Sources: National statistical offices, central banks and Citi Research

Title	Author	Date
Euro Area – Sovereign Debt Update		
Renzi to Become Italy's New Prime Minister	European Economics Team	Feb 14, 2014
ECB's Coeuré: Negative Deposit Rate a "Very Possible Option"	European Economics Team	Feb 13, 2014
Reports Suggest Renzi to Replace Letta as Italy's PM as Soon as Today	European Economics Team	Feb 12, 2014
Italy – Government Rejects Publicly Funded Bad Bank	European Economics Team	Feb 11, 2014
France Gears Up for Political Battle for a Lower Euro	European Economics Team	Feb 10, 2014
Euro Area		
Euro Area - German Constitutional Court Leaves OMT in Limbo	Ebrahim Rahbari	Feb 7, 2014
ECB: No Change, But Action Likely In March -	Ebrahim Rahbari	Feb 6, 2014
Euro Area - Assessing Vulnerabilities to an EM Slowdown	Michael Saunders	Feb 3, 2014
ECB Preview - ECB Likely to Resist Pressure to Act at February Meeting	Guillaume Menuet	Jan 31, 2014
Euro Area - Inflation Surprises Once Again to the Downside in January	Giada Giani	Jan 31, 2014
Euro Area - Bank Lending Survey Confirms Supply-Side Improvement	Guillaume Menuet	Jan 30, 2014
Euro Area - Weak Money Supply But Stabilisation In Credit Dynamics	Guillaume Menuet	Jan 29, 2014
European Economic Forecast Highlights - January 2014	Ann O'Kelly	Jan 23, 2014
Euro Area - Composite Flash PMIs – Strong Start To 2014	Guillaume Menuet	Jan 23, 2014
Euro Economics Weekly		
ERS: An Alternative Solution to OMT?	Guillaume Menuet	Feb 7, 2014
The Euro Area Now and Japan Then: Separated by One Large Shock	Ebrahim Rahbari	Jan 31, 2014
Spain Is Becoming More German	Giada Giani	Jan 24, 2014
Belgium: Politics the Likely Main Wild Card in 2014	Guillaume Menuet	Jan 17, 2014
Germany 2014 Outlook: Recovery And Rebalancing	Ebrahim Rahbari	Jan 10, 2014
2014 Outlook: GDP Risks, Credit Dynamics and Inflation Update	European Economics Team	Jan 6, 2014
Spain: 2014 Outperformer?	Giada Giani	Dec 13, 2013
Why Is France Underperforming? And How To Fix It	Guillaume Menuet	Dec 6, 2013
Is Deflation Good or Bad for the Eurozone Periphery?	Ebrahim Rahbari	Nov 29, 2013
Is This the End of Austerity?	Giada Giani	Nov 22, 2013
Recovery Watch: SME Lending is Key	Guillaume Menuet	Nov 15, 2013
One Shock Away from Deflation	Giada Giani	Nov 8, 2013
Why the ECB Should Worry About the Strong Euro	Ebrahim Rahbari	Nov 1, 2013
Italy and Spain Look Well Positioned For Job Growth	Guillaume Menuet	Oct 25, 2013
Portugal – What After June 2014?	Giada Giani	Oct 18, 2013
Chief Economist Publications		
Global Economic Outlook and Strategy - January 2014	Willem Buiter	Jan 22, 2014
Scandi		
Scandi Economics Update	Tina Mortensen	Feb 14, 2014
Sweden - Non-Event Riksbank Meeting, But Some Interesting Aspects	Tina Mortensen	Feb 13, 2014
Norway - Stronger-Than-Expected 4Q Mainland GDP	Tina Mortensen	Feb 12, 2014
Sweden - Recovery Underway In Manufacturing, Surprise Drop In Services	Tina Mortensen	Feb 7, 2014
UK		
UK - BoE Inflation Report	Michael Saunders	Feb 12, 2014
UK - Household Interest Rates Still Drifting Lower	Michael Saunders	Feb 11, 2014
UK - MPC – All Eyes on the Inflation Report	Michael Saunders	Feb 6, 2014
UK - PMI Edges Down, Still Points to Solid Growth;	Michael Saunders	Feb 5, 2014
UK - Highlights of the BoE Data and EC Survey	Michael Saunders	Jan 30, 2014
UK - GDP Data Show Solid Growth	Michael Saunders	Jan 28, 2014
UK Economics Weekly		
How Vulnerable Is the UK to EM Strains?	Michael Saunders	Feb 7, 2014
Is Growth Credit-Led?	Michael Saunders	Jan 31, 2014
After Forward Guidance…"Fuzzy Guidance"	Michael Saunders	Jan 24, 2014
What Will the MPC Say When Unemployment Hits 7%?	Michael Saunders	Jan 17, 2014
Inflation Convergence and Divergence	Michael Saunders	Jan 10, 2014

Source: Citi Research

Notes

Notes

Appendix A-1

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