Finance Ministers of France and Germany Meet in Berlin

20 October 2014

Guillaume Menuet
+44-20-7986-1314

Ebrahim Rahbari
+44-20-7986-6522

Antonio Montilla
+44-20-7986-3282

With thanks to Ann O'Kelly

Economics

Western Europe

Industrialised G7 Countries

Summary

The Finance Ministers and Economy Ministers of France and Germany meet today in Berlin, to work on a compromise ahead of the EU Council Summit in Brussels on Friday Oct 24.

Italy's Economy Minister Pier Carlo Padoan says he is confident that Europe will accept the Italy's proposed 2015 budget.

Bundesbank President Weidmann says ECB's ABS program may transfer risk to taxpayers and that a balanced budget makes *"perfect sense"* for Germany.

ECB's Nowotny does not see need to act when the economy is growing.

ECB's Coeuré encourages use of fiscal policy in countries with no debt sustainability concerns, says ABS purchases will start within days

ECB's Mersch stresses importance of safeguarding the price stability mandate

EU countries divided over proposed financial transactions tax. The issue may be discussed at an EU finance ministers' meeting on November 7.

Euro Area – Level of 2010 nominal GDP revised up by 3.5% after ESA2010 introduction. EA real GDP growth was revised to 0.3% QQ in Q1 14 (from 0.2% reported previously) and to 0.1% QQ in Q2 14 (from a flat QQ reading).

Euro Area Construction output bounces back in August, rising by 2.3% YY.

German federal tax revenues rose by 4.7% YY in September, with Jan-Sep tax revenues up by 3.0% YY.

German producer price inflation fell by 1.0% YY in September, according to the German National Statistics Office. This is the same pace of price decline as in August and in line with consensus expectations.

Spanish data: NPL ratio rises in August to 13.25% from 13.15% in July, the third MM uptick in the NPL ratio since the start of the year. **Public debt rises in August to €1tr (96.1% of GDP),** 0.4ppt of GDP above July 2014

Greece: precautionary credit line is under negotiation, PM Samaras says.

Greece: Polls show Syriza 4-8pp ahead of New Democracy (ND).

Portugal – Economic activity coincident indicator deteriorates further in September

Today's News in Detail

French and German Finance Ministers meet in Berlin today, working on a

Recent Research

Euro Economics Weekly — How Much Will the Weaker Euro Boost Eurozone Growth?

17 October 2014

The euro has fallen by around 5% in trade-weighted terms since March 2014 and we expect it to depreciate by another 5% over the coming 12 months. A 10% depreciation of the euro has historically been associated with a 5% increase in Eurozone exports and up to 1% higher GDP over three years. However, we think that the actual boost to exports will likely be smaller this time, mostly because subdued global growth and uncertain demand for exports may lead firms to raise margins rather than increase production. The ECB has talked down the euro and actual and expected ECB actions are a major driver of the euro weakening. We stress that the benefits from the weaker euro will likely be small, and at least in part be offset by weaker global growth. Should recent market turbulence persist, pressure on the ECB would rise to

compromise ahead of the EU Council summit in Brussels on Friday Oct 24. French business daily *Les Echos* writes in Monday's edition that a compromise will likely be discussed today in Berlin when French Finance Minister Michel Sapin and Economy Minister Emmanuel Macron will visit their German counterparts. The newspaper notes that the negotiation will involve asking Germany to allocate €50bn to infrastructure investment over three years to match France's €50bn of expenditure savings over 2015-17. Paris also wants a green light from Berlin about the €300bn pan-Europe investment programme proposed by European Commission President-elect Jean-Claude Juncker. Speaking about the 2015 budget, Mr. Macron noted that he was "*totally sure at this stage*" that the European Commission would not return a negative verdict. The article mentions that *Der Spiegel* reported that Berlin was doing its utmost to avoid a rejection of France's budget by the European Commission. Speaking on France Info radio on Monday, Mr. Sapin noted that growth is too slow "*also in Germany*". Mr. Sapin stressed that "*we must not go all out for deficit reduction, we have to slow it down because we must be in harmony with the needs of the French economy - we must moreover support growth*". Comment: Some agreement is necessary between Paris and Berlin on this difficult subject at a time when both GDP growth and inflation are largely absent. Protecting the small amount of nominal GDP growth that the euro area is enjoying is crucial in our view, given the associated risks in terms of debt sustainability. With the growing threat posed in France, by the rise of the extremes, and in particularly the National Front, we believe that a deal is likely, but that France might have to make a few concessions in terms of quickening the pace of structural reforms as well as broadening their scope.

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Italy: Economy Minister Pier Carlo Padoan said he was confident Europe would accept the country's budget in an interview with Italian business daily *Il Sole 24 Ore,* according to Reuters. The newswires have quoted numerous EU sources in the past few days suggesting that the risk of rejection was significant as the plan does not do enough to reduce Italy's debt burden estimated to be more than 130% of GDP. Reuters notes that former head of IMF fiscal affairs Carlo Cottarelli saying on Friday after his resignation as head of Italy's public spending review that he had been isolated and faced "*enormous difficulties*" due to government bureaucrats hampering his work of carefully targeted cuts.

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Bundesbank President Weidmann says ECB's ABS program may transfer risk to taxpayers and that a balanced budget makes "*perfect sense*" for Germany. Bloomberg reports that Bundesbank President Weidmann says that "*purchases of asset-backed securities are problematic when they imply a transfer of risks from banks to the balance sheet of the central bank*", noting that such purchases "*could amount to a transfer of risks from banks to the taxpayer. And this would run counter to everything we have strived to achieve in banking regulation over the last years*". Weidmann added that "*the higher the target for the expansion of the Eurosystem's balance sheet, the higher the risks of overpaying for the assets*". Weidmann also said that the rationale of ECB asset purchases suggests a "*shift from programs specifically aimed at credit easing towards a quantitative-easing philosophy*". Meanwhile he said that the risk of the euro area "*becoming enmeshed in a deflationary… scenario is considered to be low*" and that therefore "*the Governing Council…has to judge whether additional stimulus is needed or would be effective, and what unintended side-effects would come with the measures*". Regarding the German economy, Weidmann said that "*pursuing a balanced budget makes perfect sense*", as "*Germany is not in need of stimulus*" even after economic growth forecasts were revised lower, and that "*costly stimulus measures could even backfire via negative confidence effects*". Weidmann said that "*there is no need for a debt-financed fiscal stimulus, but for a structural shift of government expenditures from consumption to investment*". He deliver further easing sooner

Ebrahim Rahbari | Guillaume Menuet | Michael Saunders | Antonio Montilla | Ann O'Kelly

UK Economics Weekly — Will "Low-flation" Persist?

17 October 2014

The UK economy looks rather like the US in terms of real GDP growth and the falling jobless rate. But, in terms of inflation, the UK seems to be more in the European "low-flation" camp. CPI inflation probably will stay low nearterm, with a low of perhaps 1.0% YY in December this year. However, we expect that the UK's flirtation with "low-flation" will ultimately prove to be temporary. Barring new external disinflationary shocks, we expect that CPI inflation will rise close to the 2% target in late 2015 and into 2016. The current position is more like 1998 than 2008 in our view, and low inflation will boost real consumers' incomes and give a further impetus to consumer spending. Moreover, labour market slack is shrinking fast. We suspect that markets have now gone too far in pricing in a "low for longer" interest rate outlook.

Michael Saunders | Ann O'Kelly

Norway — Stable Policy Rate and a Relatively Neutral Statement

17 October 2014

At the upcoming monetary policy meeting on 23 October, we expect Norges Bank to keep the key policy rate stable at 1.50%, in line with indications from the September MPR. On the basis of the very few data releases out since the latest meeting, we reckon the Central Bank will broadly confirm the picture painted of the current economic situation in Norway. Meanwhile, the Bank is expected to note the decline in money market premiums and bank lending margins plus the depreciation of the NOK since the September meeting, all factors indicating upside risks to the Bank's conditional interest rate path. With lower foreign interest rates and turbulence on financial markets amid global growth worries acting as offsets, we expect Norges Bank to issue a relatively neutral statement in October.

Tina Mortensen

said that "*the periphery's share of German imports is very low*" so that "*the boost to the peripheral countries from an increase in German public investment is therefore likely to be negligible*". He noted that instead a "*push to EU GDP could potentially stem from an EU-US trade agreement*" and that the "*the current debate in Italy and France about their fiscal stance is not reassuring*". Comment: These remarks highlight how difficult it is going to be for Mr. Weidmann to shift his opposition to fiscal stimulus unless the situation deteriorates further.

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Austrian central bank governor Ewald Nowotny remarked, speaking about the ECB's leeway for action, that "*one surely has further opportunities*". However, Mr. Nowotny added that "*we are not in recession, we have positive growth rates. It is not as if the ECB has to open the emergency pharmacy now*". Mr. Nowotny also dismissed as "*nonsense*" concerns that ABS purchases will transfer risk from lenders to the ECB, arguing that "*when we look at the balance sheet of the ECB the possible portion of ABS is so small ... that it is in no way to compare with a 'bad bank'*." Comment: There are clearly some strong disagreements between Governing Council members about the ABS purchase programme, with Mr. Weidmann leading the charge against its activation, while others argue that its modest size limits the risks to the ECB's balance sheet. We find it interesting that some ECB members try to downplay the size aspect when President Draghi and the Governing Council have decided to make balance sheet expansion the ECB's main tool in trying to bring inflation back to target.

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Executive Board member Benoit Coeuré said governments could help counteract lower prices with "*fiscal policy, when it is available without questioning long-term debt sustainability*". Mr. Coeuré insisted that the euro area remains on a recovery path, expecting "*growth to be positive in the third and fourth quarter*". Separately, Mr. Coeuré, who also spoke in Riga, suggested that the ECB would begin buying ABS within days. Comment: These remarks suggest that the Governing Council might have to shift its stance when the first estimates of Q3 GDP are released on 14 Nov, since there is a real risk of economic activity having contracted in the quarter.

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Executive Board member Yves Mersch remarked in Zurich that "*a central bank with a clear price stability mandate to safeguard price stability needs to act forcefully when push comes to shove*". Comment: A very important statement from Mr. Mersch, in our view, simply restating the obligation that the ECB faces to deliver on its price stability mandate. With the output gap not shrinking meaningfully, business surveys signaling further softening in economic activity in the next few quarters, persistently low inflation and some likely difficulties in expanding the balance sheet by relying only on private sector asset purchases, we continue to believe that the ECB will do more and launch a full QE programme later this year or early in 2015.

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EU countries divided over proposed financial transactions tax. *Handelsblatt* reports that the eleven countries that have in principle agreed to introduce a financial transactions tax are "*in part deeply divided*", based on an internal report of the German Finance Ministry, noting that these differences "*complicate a plan to finalise an agreement by the end of 2014, and perhaps endanger them*". According to the report, France and Italy have proposed to discuss the topic at the EU finance ministers' meeting on November 7. Among the contentious issues are the domicile rules, with France and Italy suggesting that the tax should only be due on securities issued by a company that is domiciled in one of the 11 countries.

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Norway — Bank Lending Survey: Lower Lending Margins

16 October 2014

The latest bank lending survey from Norges Bank shows that household credit demand decreased somewhat in third second quarter, weaker than expectations of unchanged demand at the end of 2Q. We find the decline a bit surprising given that several large banks have lowered mortgage rates since the 2Q survey. From a monetary policy point of view, today's report offers no big surprises. Ahead, we reckon Norges Bank will continue to look at risks related to financial stability. In other words, signs of an ongoing build-up of household debt (combined with lower mortgage rates) will continue to be an important factor arguing against additional monetary policy easing ahead.

Tina Mortensen

UK — Labour Market Data

15 October 2014

With strong job growth and a slight slowdown in labour supply, the jobless rate continues to fall rapidly, dropping to 6.0% in June-August from 6.5% three months earlier and 7.7% 12 months earlier. The drop in the jobless rate over the last year (1.7 percent) is the sharpest decline since 1988-89. The MPC estimate that the equilibrium jobless rate for the UK is 5.1%, and we expect that threshold for full employment is likely will be reached during 2015. Indeed, even assuming continued high inflows of foreign workers plus a renewed rise in the participation rate, we expect the jobless rate will fall below 5% around the middle of 2015 (ie Q2 or Q3).

Michael Saunders

UK — CPI Inflation Tumbles

14 October 2014

CPI inflation fell to 1.2% YY in September from 1.5% YY in August, well below our and the consensus forecast of 1.4% YY. The headline inflation rate is the lowest since 2009 (when VAT was cut), while CPI inflation excluding the effects of tax changes (1.1% YY) is the lowest since 2004. Q3

Euro Area – Level of 2010 nominal GDP revised up by 3.5% after ESA2010 introduction. Eurostat published on Friday the first estimate of the national accounts across EA countries after the introduction of the new ESA2010 methodology. The level of EA aggregate nominal GDP was revised upward on average by 3.4% per year over the period 1997-2013 (3.5% for 2010). Eurostat noted that the value of GDP was higher mainly due to the inclusion of R&D spending into investment (added 1.9pp in 2010), as well as other methodological changes (e.g. the inclusion of expenditure on weapons systems into investment, and the inclusion of illegal activities into the national accounts, among others). Across countries, the impact of the changes on the level of 2010 nominal GDP ranged from 9.5% in Cyprus and 7.6% in the Netherlands to 0.2% in Luxembourg and -0.1% in Latvia, Eurostat noted. In addition, Eurostat revised up marginally real GDP growth for the EA aggregate in Q1 2014 (to 0.3% QQ vs. 0.2% QQ reported previously) and Q2 2014 (to 0.1% QQ vs. 0.0% QQ reported previously).

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Euro Area – Construction output bounces back in August, rising by 2.3% YY after falling by 0.2% YY in July and rising by 0.4% YY in June. On a monthly basis, construction output rose by 1.6%, largest MM pickup since Dec 2013. Construction output continued to rise strongly in Spain (up by 18.6% YY in August and 19.4% YY on average in Jan-Aug), while it went up by 1.3% YY in France (largest rise since Mar 2014). In Germany, construction output fell by 2.6% YY, largest YY decline since Mar 2013.

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German federal tax revenue rose by 4.7% YY in September. Bloomberg reports that the German Finance Ministry noted that federal tax revenues rose by 4.7% YY in September. Year to date, tax revenues are thus up 3.0% YY, compared to a full-year estimate for revenue growth of 3.4% YY made on May 8. The Finance Ministry stated that it was too early to draw conclusions from the federal Jan-Sep budget deficit of €18.8bn, which compares with a full-year target of €6.7bn and said that the German general government budget (including the state and local budget and the social security fund) are likely to be balanced in 2014 and 2015. Regarding the economic outlook, the Finance Ministry report said that the slowdown in economic activity in the middle of the year is likely to be temporary and that sentiment indicators suggest continued "*moderate*" increases in employment, supported by domestic demand.

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Spain: NPL ratio rises in August to 13.25% from 13.15% in July – data from Bank of Spain (BoS) showed, marking the third MM increase in the Non-Performing Loan ratio since the start of the year. The rise in the NPL ratio was driven by a further deterioration in the pace of decline in total lending to the private non-financial sector, falling by 6.7% YY (largest YY decline since Apr-14) from -6% YY in July. The amount of impaired loans was 1.9% above August 2013 levels, easing from 3.2% YY in July and 5.4% YY in June. Overall the NPL ratio is 0.4pp lower than the level at the start of the year. The decline in 2014 in the NPL ratio partly reflects an accounting change in the calculation of total loans. Comment: We expect the NPL ratio to continue stabilising over coming months, although most likely remaining at high levels for a while amid ongoing deleveraging pressures.

Spain: Public debt rises in August to €1tr (96.1% of GDP), 0.4ppt of GDP above July 2014, data from Bank of Spain showed. On an annual basis, gross public debt is up by 6.1%. Comment: Last month the Bank of Spain adjusted the 2013 public debt-to-GDP ratio from 94.4% to 92.1% to reflect the introduction of the ESA2010 methodology in the national accounts (which implied a revision of 3% in the level of 2013 nominal GDP).

inflation (which averaged 1.44% YY) turned out well below the MPC's forecast for Q3 in the August Inflation Report (1.81% YY). This is the sixth consecutive quarter with inflation below the MPC's quarter-ahead forecast, the longest series of undershoots since BoE independence in 1997. At this stage, we expect CPI inflation to average just 1.2% YY in Q4 this year and 1.3% YY in H1-2015, with an average of 1.5% YY for 2015 as a whole.

Michael Saunders

Sweden — Marked Inflation Undershoot, October Rate Cut Our Base Case

14 October 2014

Contrary to expectations, inflation eased further in September; the Riksbank's preferred measure of underlying inflation, which excludes the effects of temporary interest rate changes (CPIF) moderated from 0.5% YY in August to 0.3% YY, the second weakest gain since Feb-04 (CPIF stood at 0.0% YY in March this year). Compared to the Riksbank's (and our) forecast, core inflation undershot by a massive 0.4pp after being spot on in August. With several board members having expressed very limited tolerance for downward surprises in inflation given already muted price pressures, it will be very difficult for the Riksbank to argue against a near-term interest rate cut, in our view. Hence, we now expect the Riksbank to cut the repo rate by 20bp to 0.05% (on par with the ECB's refi rate) at the upcoming 28 October monetary policy meeting.

Tina Mortensen

Spain — Catalonia Referendum: Will it Happen? If So, What?

10 October 2014

Over the last few days the Catalan government has announced its intentions to continue with preparations to hold an independence referendum in the region on 9 November 2014, despite the rejection of the ballot by the Spanish Congress and the fact that the Constitutional Court has already deemed the referendum illegal twice this year. Polling data suggest support for independence has been fading recently,

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Greece – a precautionary credit line is under negotiations, PM Samaras says. Speaking last Friday to reporters in Milan, Greek PM Antonis Samaras said that Greece is negotiating with its international creditors over a possible precautionary credit line that would be available should market borrowing costs continue to spike, Bloomberg reports. Mr. Samaras said however that Greece does not need a new memorandum, noting that a precautionary credit line is only part of the negotiations. Mr. Samaras remarked that "*the only source of concern is the political risk*", Bloomberg reports. Comment: Renewed turbulence in Greek politics has reignited market concerns around Greek assets. We reckon Greece will eventually accept some form of external monitoring by official creditors, possibly agreeing on a precautionary credit after the current EFSF programme expires in Dec-14 (for more see Euro Economics Weekly of 3 October 2014: ***Greece — Six Crucial Months Ahead***

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Greece: polls show Syriza 4-8pp ahead of New Democracy (ND). Two new opinion polls conducted by the University of Macedonia and Kapa Research showed voting intentions for opposition party Syriza standing around 27.5%, well ahead the support for the ruling ND (at 19.8% for University of Macedonia and 23.5% for Kapa Research). The two polls report also 6.5% support for ultra nationalist Golden Dawn, while support for the recently created party To Potami was shown at 7.5% (University of Macedonia) and 5.6% (Kapa Research). In addition, the poll conducted by Kapa Research showed that 50.8% of those polled would prefer the current Parliament to elect the new President in the upcoming elections in Feb 2015 (vs. 42.3% preferring early elections).

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Portugal: economic activity coincident indicator deteriorates further in September, falling by 1.2% YY, largest YY decline since Jul 2013, and following a 0.7% YY drop in August, data from the Bank of Portugal (BoP) showed. In addition, the BoP private consumption coincident indicator rose by 1.1% YY in September, lowest YY expansion since Dec 2013. Overall the economic activity coincident indicator fell by 0.7% YY in Q3 (after a 0.5% YY rise in Q2).

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Latest Issues of Sovereign Debt Update

ECB To Sign Off on Covered Bonds Law

17 October 2014

ECB to sign off on covered bonds law. ECB's Nowotny sees downside risks to growth. ECB reduces haircuts on Greek govt bonds. Euro Area final HICP. France and Italy urge need for expansive measures, Merkel stresses adherence to budget rules. OECD says already implemented reforms in France will add 1.6pp to GDP after 5 years. Spain's household saving rate slips, industrial activity bounces back. ESM head on Greece's bailout exit. Belgium: unions protest at planned expenditure cuts.

Antonio Montilla | Guillaume Menuet | Ebrahim Rahbari

Italian Government Unveils Expansionary 2015 Budget

16 October 2014

Italian govt unveils expansionary 2015 Budget Bill, as fiscal deficit widens in 1H14. Italy's 5 Star Movement wants referendum on euro membership. German states call for higher public spending but Merkel sticking to balanced budget. BuBa's Dombret wants end to tax breaks for bank debt. French EconMin Macron confirms labour reform and modest privatisation. Spain's fiscal watchdog warns on risks to 2015 deficit target. Greek state budget deficit falls again. Portugal with some evidence that most Catalans would prefer calling off the referendum and finding an alternative legal solution. We expect the independence referendum not to take place and instead believe early regional elections are likely to be called. In the long-run we continue to see greater fiscal autonomy within Spain as a more likely outcome.

Antonio Montilla | Giada Giani | Tina M Fordham

Scandi Economics Update — Riksbank Jansson says "Deepening Inflation a Fallback"

20 October 2014

Sweden — The deepening deflation in September (headline inflation fell 0.4% YY after a 0.2% YY decline in Aug) is a clear setback that may prompt a response, said Riksbank Deputy Governor Jansson in an interview late last week.
Sweden — Riksbank job target faces huge legal obstacles.
Sweden — Sweden's hunt for a foreign submarine – presumed to be Russian – according to Financial Times, has entered its fourth day.
Norway — Norges Bank's interest rate decision on Thursday will likely be a non-event; we expect the Bank to keep the key policy rate stable at 1.50% and to issue a relatively neutral statement.

Tina Mortensen

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approves 2015 budget bill.

Antonio Montilla | Guillaume Menuet | Ebrahim Rahbari

ECJ Opinion on OMT Case by Jan 14, 2015

15 October 2014

ECJ opinion on OMT case by Jan 14, 2015. German govt cuts GDP forecasts for 2014-15. French and German Finance and Economy Ministers to discuss investment possibilities. Fitch puts France's rating on negative watch. Italy's draft 2015 budget not compatible with EU requirements, say sources. Moody's confirms Italy's rating. Catalonia referendum called off, "consultative" vote instead. Portugal: revised 2015 deficit target.

Antonio Montilla | Guillaume Menuet | Ebrahim Rahbari

ECJ Hearing on OMT Today

14 October 2014

ECB hearing today on OMT. Dijsselbloem remarks after Eurogroup meeting. BuBa's Weidmann for budgetary rules to be enforced. Schaeuble says EU growth may need EIB capital increase. French FinMin Sapin says no changes likely to French 2015 Budget. Italy's 2015 Budget sees €30bn saving measures. Italian GDP growth likely negative in 3Q - Istat head. Catalonia independence referendum seemingly called off, replaced by "consultation of citizens". EA FinMins sceptical on Greece's early bailout exit.

Antonio Montilla | Guillaume Menuet | Ebrahim Rahbari

ECB’s Draghi and Weidmann Clash over Monetary Policy

13 October 2014

German Focus magazine claims Draghi finds cooperating with BuBa's Weidmann "almost impossible". S&P revises outlook to negative for EFSF and for France. French PM says only French govt can decide budget. French EconMin says New Deal is necessary. German govt to shift spending towards investment. Italy's draft budget under pressure from EC. Spain: Catalonia referendum unlikely to happen. Belgium: Govt sworn in. Greek govt wins confidence vote, poll shows Syriza ahead. S&P downgrades Finland.

Guillaume Menuet | Ebrahim Rahbari | Antonio Montilla

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Macroeconomic Forecasts

Europe — Europe: Monthly Inflation Profiles for Selected Countries

14 October 2014

Updated monthly inflation forecasts for France, Italy, Spain, UK, Sweden and Switzerland.

Ann O'Kelly | Michael Saunders | Guillaume Menuet | Giada Giani | Ebrahim Rahbari

Europe — European Unemployment Rates – Forecasts to 2018

25 October 2014

This note gives our forecasts for annual unemployment rates in selected European countries to 2018.

Ann O'Kelly | Michael Saunders | Guillaume Menuet | Giada Giani | Ebrahim Rahbari

European Economic Forecast Highlights, September 2014

25 September 2014

This companion to the September issue of Global Economic Outlook and Strategy gives more detailed forecasts for the main European countries to 1Q16,

as well as annual forecasts to 2018 for growth, inflation, current balance, fiscal balance, primary balance, and government debt. We also show our forecasts in comparison with those of the European Commission, the OECD and the IMF.

Ann O'Kelly | Michael Saunders | Guillaume Menuet | Giada Giani | Ebrahim Rahbari

Global Economic Outlook and Strategy — September 2014

24 September 2014

This publication contains Citi's updated forecasts and commentary for major economies, central bank policy and financial markets. Our global growth forecasts continue to drift down, and we are cutting 0.1 percent off our 2015 forecast this month, with the biggest monthly downgrade since mid-2011 to our overall forecast for EM growth in the current year and next year. The ECB and BoJ are both likely to ease further via new asset purchase programs in the next couple of quarters. By contrast, both the BoE and Fed are likely to hike rates in the next 12 months. We look for further weakness in the euro and yen against the US dollar and sterling. We highlight three other themes: medium-term China worries, sluggish world trade growth and political independence movements.

Willem Buiter | Guillermo Mondino | Michael Saunders | William Lee | Kiichi Murashima

Emerging Markets Macro and Strategy Outlook — Time for another tantrum?

26 September 2014

EM is showing a faint echo of May 2013, the start of the 'taper tantrum', when it was faced with two shocks: expectations of a more unfriendly US monetary policy, and an uncertain outlook for commodity exports. These two forces are back. But last year's distinction between 'deficit' (sell) and 'surplus' (buy) countries is morphing into a distinction between commodity and manufactured goods exporters. In the former group, we see deteriorating terms of trade, worse export performance, wider current account deficits, lower levels of investment efficiency, more depreciated currencies and bigger inflation problems. Among the Fragile 5, the manufacturing exporters (India, Turkey) have achieved decisive current account improvements while deficits are either bigger or only marginally smaller in commodity exporters. That may have been acceptable early this year when risk-appetite towards EM was stable, but if last year's 'taper tantrum' is repeated, these countries' failure to adjust will be punished.

Guillermo Mondino | David Lubin | Johanna Chua

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Appendix A-1

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