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Europe

Sovereign Ratings Outlook

July 2012

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With thanks to Jan Maguire

- Citi economists and strategists continue to expect further near-term rating downgrades in the euro area, and a broader range of downgrades over the longer term including the US, UK and Japan. We do not expect any upgrades among advanced economies, other than a technical one for Greece exiting from expected default status.

- We expect a wide series of ratings downgrades among EMU countries in the next 2-3 quarters, with at least a one-notch downgrade by at least one major agency for Austria, Belgium, France, Germany, Greece, Ireland, Italy, the Netherlands, Portugal and Spain. Ratings in periphery countries are likely to be hit by economic weakness, with resultant adverse debt and deficit trends over time. In addition, we now believe the probability that Greece will leave EMU over the next 12-18 months is about 90% (versus 50-75% previously). As before, we assume, for the sake of argument, that Grexit will occur on 1 January 2013, but stress this is an assumption rather than a forecast of the precise date. Grexit, if it occurs, is likely to intensify capital flight from periphery countries. For the core countries, as Moody's recently highlighted, sovereign ratings are likely to be hit by worries that the worsening EMU crisis will eventually lead to greater fiscal burden sharing, rising bank recapitalization costs, or adverse effects from economic weakness on the fiscal outlook. Over the longer term, we expect further downgrades among many EMU countries.

- With economic weakness and fiscal slippage, the UK's AAA sovereign rating is also likely to come under question. We expect that S&P will put the UK on Negative Outlook in the near term, and if growth remains elusive then the UK will probably lose its AAA status from at least one major agency over the next 2-3 years. The US is currently on Negative Outlook by both Moody's and S&P and we continue to expect a one-notch downgrade over the next 2-3 years. We also envisage downwards ratings pressure for Japan over the next 2-3 years, predicated on longer-term debt sustainability trends. The pool of solid AAAs is likely to become smaller and smaller, with only Canada, the Australasian countries, Switzerland and the Scandis likely to remain AAA Stable over the near term and longer term.

Figure 1. Global — Expected Sovereign Ratings Changes (measured from current ratings by S&P and/or Moody's), 2012-14

Forecast NearTerm Ratings Ratings Changes (Next 2-3 Quarters)		Forecast Longterm Ratings Ratings Changes (Next 2-3 years)	
Upgrades	Downgrades	Upgrades	Downgrades
	Austria, Belgium, France, Germany, Greece, Ireland, Italy, Netherlands, Portugal, Spain	Greece	Austria, Belgium, France, Germany, Ireland, Italy, Japan, Netherlands, Portugal, Spain, UK, US

Source: Citi Research

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This publication is a joint product between the Citi economics and rate strategy teams, with input from various other research teams. We aim to forecast the direction and scale of sovereign debt ratings (local currency), as well as any changes in the ratings outlook, for a range of countries. These are our judgments over the ratings outlook, rather than model-determined recommendations. All economic and fiscal forecasts are consistent with those published in Citi's monthly "*Global Economic Outlook and Strategy*" or other research. This publication does not aim to make a judgment on the financial market implications of ratings changes, except in so far as we expect any such market implications to affect other sovereign ratings. The full publication is released roughly once per quarter, with a briefer monthly summary in the "*Global Economic Outlook and Strategy*".

Given economic updates in this publication and based on rating agency criteria, we highlight our economists' and strategists' main expectations for sovereign ratings over the near (2-3 quarters) and longer (2-3 years) term. Citi economists and strategists continue to expect further downgrades over the near term in the euro area, and a broader range of downgrades over the longer term (see Figure 2).

Figure 2. Advanced Economies — Sovereign Long-Term Debt Ratings and Citi Ratings Forecasts

	S&P Ratings				Moody's Ratings			
Country	Current Rating	Current Outlook	Citi Near-term (Up to 9 Months) Forecast Rating	Citi Longterm (Next 2-3 Years) Forecast Rating & Outlook	Current Rating	Current Outlook	Citi Near-term (Up to 9 Months) Forecast Rating	Citi Longterm (Next 2-3 Years) Forecast Rating & Outlook
US	AA+	Neg	AA+ (Neg)	AA ↓	Aaa	Neg	Aaa (Neg)	Aa1 ↓
Canada	AAA	Stable	AAA	AAA	Aaa	Stable	Aaa	Aaa
Japan	AA-	Neg	AA- (Neg)	A+ ↓	Aa3	Stable	Aa3	A1 ↓
Germany	AAA	Stable	AAA (Neg W)	AA+ ↓	Aaa	Neg	Aa1 ↓	Aa1 ↓
France	AA+	Neg	AA+ (Neg W)	AA (Neg) ↓	Aaa	Neg	Aa1 ↓	Aa1 (Neg) ↓
Italy	BBB+	Neg	BBB ↓	BBB- ↓↓	Baa2	Neg	Ba1 (Neg) ↓↓	Ba2 ↓↓↓
Spain	BBB+	Neg	BBB ↓	BBB - ↓↓	Baa3	Neg W	Ba1 (Neg) ↓	Ba2 ↓↓
Austria	AA+	Neg	AA+ (Neg W)	AA (Neg) ↓	Aaa	Neg	Aa1 ↓	Aa1 (Neg) ↓
Belgium	AA	Neg	AA (Neg W)	AA- ↓	Aa3	Neg	A1 ↓	A1 ↓
Finland	AAA	Neg	AAA (Neg W)	AAA (Neg)	Aaa	Stable	Aaa (Neg)	Aaa (Neg)
Greece	CCC	Stable	D ↓↓↓↓	CCC ↑↑↑↑	C		C	Caa2 ↑↑↑↑
Ireland	BBB+	Neg	BBB- ↓↓	BB ↓↓↓↓	Ba1	Neg	Ba2 ↓	Ba3 ↓↓
Netherlands	AAA	Neg	AAA (Neg W)	AA+ (Neg) ↓	Aaa	Neg	Aa1 ↓	Aa1 (Neg) ↓
Portugal	BB	Neg	B+ ↓↓	CCC ↓↓↓↓↓	Ba3	Neg	B1 ↓	Caa2 ↓↓↓↓↓
UK	AAA	Stable	AAA (Neg)	AA+ ↓	Aaa	Neg	Aaa (Neg)	Aa1 ↓
Switzerland	AAA	Stable	AAA	AAA	Aaa	Stable	Aaa	Aaa
Sweden	AAA	Stable	AAA	AAA	Aaa	Stable	Aaa	Aaa
Denmark	AAA	Stable	AAA	AAA	Aaa	Stable	Aaa	Aaa
Norway	AAA	Stable	AAA	AAA	Aaa	Stable	Aaa	Aaa

Note: Arrows denote expected ratings changes from the current rating. (Neg) denotes Negative Outlook. (Neg W) denotes negative watch. SD means Selective Default. (P) means Provisional. The number of arrows denotes the expected change in ratings notches from the current level. We show a maximum of five arrows even for countries where we expect more than five notches of ratings change. NA Not available. Sources: Moody's, S&P and Citi Investment Research and Analysis

Key Expected Ratings Issues

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We expect the ratings of many core EMU sovereigns to be downgraded in the next 2-3 quarters, including Germany. These moves reflect the higher probability (90%) we see of Greece's exit from the euro zone and the increased likelihood we see that this will happen relatively soon (next 2-3 quarters), the weak economic backdrop, broad-based fiscal slippage and bank stresses, plus recent comments by Moody's. Our views also reflect the fact that Moody's and S&P already have many EMU countries on Negative Outlook.

On 23 July, Moody's placed Germany and the Netherlands on Negative Outlook (at Aaa Negative Outlook, these sovereign are now rated the same as France and Austria by Moody's). Moody's cited[1] two core reasons for the change in outlook:

- Increased susceptibility to event risk due to the rising probability of a Greek exit.
- Increased likelihood that greater collective support for other euro area sovereigns, most notably Spain and Italy, will be required. Moody's placed on Negative Outlook those Aaa euro area sovereigns whose balance sheets are expected to bear the main financial burden of support.

A Greek exit would exert downward ratings pressure on core EMU sovereigns

Furthermore, in terms of what could put Aaa ratings under downgrade pressure, Moody's specifically cites the following: "*Germany's Aaa rating could potentially be downgraded if Moody's were to observe a prolonged deterioration in the government's fiscal position and/or the economy's long term strength that would take debt metrics outside scores that are commensurate with a Aaa rating. This could happen if…any country were to exit the European monetary union, as such an event is expected to set off a chain of financial sector shocks and associated liquidity pressures for sovereigns that would entail very high cost for wealthy countries…*".

A pan-European review of all EMU sovereigns is likely in a Greek exit scenario

Citi expects Greece to leave EMU within the next 2-3 quarters (see our latest *Global Economic Outlook and Strategy July 2012*). In the near term (next 2-3 quarters) therefore, we expect at least one major agency to downgrade the core EMU countries by one notch following a Credit Negative Watch review period. Both major agencies also stress that a Greek exit would constitute a "defining" moment in the euro project and effectively break the assumption of irreversibility. In addition, given Citi's base case that Spain and Italy are likely to enter some form of Troika programme by end-2012 regardless of whether Greece leaves EMU, we expect at least a one notch downgrade by one major rating agency of Italy and Spain. Over the longer term, we expect that persistent economic weakness and adverse fiscal trends will prompt further downgrades among EMU periphery countries.

Globally, Citi continues to expect downwards rating pressure in the US and Japan over the longer term

Over the longer term, the pool of solid AAAs is likely to shrink further, with only Canada, the Australasian countries, Switzerland and the Scandis likely to remain AAA Stable over the near term and longer term. The UK will probably be placed on "Negative Outlook" by S&P in coming quarters as weak economic data increasingly impacts fiscal data, and over the longer term the UK may well lose its AAA status if growth remains elusive and fiscal consolidation is partly delayed. The US is currently on Negative Outlook by both Moody's and S&P and we continue to expect a one-notch downgrade over the next 2-3 years. We also envisage downwards ratings pressure for Japan over the next 2-3 years, predicated on longer-term debt sustainability trends.

[1] Moody's Announcement: "*Moody's changes the outlook to negative on Germany, the Netherlands, Luxembourg and affirms Finland's Aaa stable rating*". 23 July 2012.

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Citi Ratings Outlook: US

	Current	Near-Term	Long-Term
S&P	AA+ (Neg)	AA+ (Neg)	AA
Moody's	Aaa (Neg)	Aaa (Neg)	Aa1

Source: Citi Investment Research and Analysis

With budget outlays growing at barely 1% and revenues climbing at a 5% pace, the federal deficit for the year ending September is declining slowly but still heading toward a historically high level of about 7½% of GDP. Due to sizable structural imbalances driven in part by rising health care costs and demographics, continued economic expansion and modest fiscal restraint will not prevent rising overall public debt burdens. Even large-scale tax increases scheduled under current law would leave federal debt on a higher path in ten years than anytime in the past half century preceding the recent stretch of outsized deficits. An unfortunate sequence of the failed Bowles-Simpson effort, the subsequent debt limit impasse of a year ago and the Supercommittee's inability to reach agreement last fall has contributed to a widespread loss of confidence in US fiscal policymaking. Moreover, the approaching elections have placed important decisions on hold despite the impending convergence of massive tax increases and across the board spending cuts scheduled for next January. At the same time, Treasury's need to seek increased borrowing authority early next year will likely be a source of additional turmoil and uncertainty given sharp political divisions. In the absence of credible progress toward medium-term fiscal consolidation, we are keeping our expectations on how the US rating might evolve unchanged from our April view.

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Citi Ratings Outlook: Canada

	Current	Near-Term	Long-Term
S&P	AAA	AAA	AAA
Moody's	Aaa	Aaa	Aaa

Source: Citi Investment Research and Analysis

The fiscal and political situations in Canada remain stable. Hence, we maintain that rating agencies will likely retain Canada's AAA status in both the near and the long term. In March, Federal and provincial governments released budgets for 2012, which largely called for additional tightening to strengthen the nation's fiscal position. Much of the savings are anticipated to come from restrained government program spending as well as moderately improved Canadian economic prospects. These actions are placing additional drag on real output this year, but should be favourable for the Canadian economy over the longer term.

The Federal government's fiscal outlook continues to anticipate smaller deficits over FY2012-13 through FY2014-15 span and larger surpluses in fiscal years 2015-16 and 2016-17. The government also continues to expect that Canada will be well ahead of schedule regarding its G-20 commitments to halve deficits by 2013 and stabilize or reduce total government debt-to-GDP ratios by 2016. The government's assumptions are cast against a backdrop of domestic growth projections that are roughly in line with our own, reflecting Canada's continued resilience amid external weakness and uncertainties. The likelihood that the Canadian government will accomplish its fiscal aims, holding all else equal, is high given the Conservative party's multi-year mandate.

In response to persistent strength in the Canadian housing market, and ongoing concern about distended sales and prices in select cities, the Federal government instituted a fourth round of macroprudential policy tightening of the mortgage market in early July. Past initiatives focused on curtailing speculative home purchases and excessive use of HELOCs. The latest measures address refinancing, and the purchase of ultra-expensive homes by marginal buyers. The government has also increased its oversight of the Canada Mortgage and Housing Corporation, the public mortgage insurer, and bolstered the resources of private insurers.

These initiatives aim to limit the risk to the financial system, taxpayers, and the economy from the outsized degree of debt held in aggregate by Canadian households. In response to these policies and the central bank's noted penchant for reduced monetary policy accommodation, the Bank of Canada's base-case is now for a marked reduction in Canadian housing activity ahead. However, two-sided risks remain. On the one hand, housing strength could persist delaying the inevitable correction that needs to take place. On the other hand, a sharp downturn in home prices might severely curb consumer spending and/or negatively impact the financial system and other parts of the economy amid a wave of defaults.

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Citi Ratings Outlook: Japan			
	Current	**Near-Term**	**Long-Term**
S&P	AA- (Neg)	AA- (Neg)	A+
Moody's	Aa3	Aa3	A1

Source: Citi Investment Research and Analysis

We are keeping our outlook on Japan's ratings unchanged from our last publication. This highlights the chance of a one notch downgrade by both S&P and Moody's agencies over the longer term from AA- to A+ and from Aa3 to A1, respectively.

Over the near term, we expect Japan's sovereign ratings to be kept unchanged by rating agencies. Most importantly, the consumption tax hike bill, calling for a tax rate hike to 8% in April 2014 from 5% currently and to 10% in October 2015, is likely to pass the Upper House of the Parliament in August following the approval by the Lower House in late June. To be sure, a 5% point hike in the tax rate increases tax revenues by only about ¥13tn (2.7% of GDP), meaning that the bill is just a small step towards fiscal reform, given that the fiscal deficit of the general government as a percentage of GDP this year is expected to be 10.5%. However, the approval of the bill likely will reduce the possibility of downgrades in the immediate future.

However, we continue to expect a downgrade over the longer term. First, even with a 5% point hike in the tax rate, the primary balance of central and local governments would stay in deficit of around 3% of GDP in 2020, significantly falling short of the government's goal. Second, there are increasing signs that Japanese politicians do not put much weight on spending cuts, which are an essential element in fiscal reform, in our view. The government plans to introduce a supplementary budget including public works spending in the special session of the Parliament this autumn. Lastly, the tax rate hike in April 2014, if implemented, would have a significant negative impact on the economy by way of a payback to frontloaded spending in 2013 ahead of the tax hike and erosion in real disposable income caused by higher prices. As a result, we figure that the second tax hike slated just 18 months after the first hike will be politically difficult to implement. In that case, concerns over Japan's fiscal sustainability likely will intensify among investors and credit agencies.

On balance, the approval of the consumption tax hike bill is an important step towards fiscal reform but probably will be insufficient to prevent a sovereign downgrade over the longer term.

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Citi Ratings Outlook: Germany

	Current	Near-Term	Long-Term
S&P	AAA	AAA (Neg W)	AA+
Moody's	Aaa (Neg)	Aa1	Aa1

Source: Citi Investment Research and Analysis

With Moody's putting Germany's Aaa rating on Negative Outlook, it has become obvious that Germany's rating is suffering from the sovereign debt crisis. Moody's explicitly mentioned that a country leaving the euro area would be a sufficient condition for a downgrade of Germany's rating. In addition to the increasing involvement of Germany in the rescue facilities, Moody's also believes the impact of a further escalation of the sovereign debt crisis would probably require further government assistance to the domestic banking sector, particularly if a country were to leave EMU. Since we now expect that Grexit will happen with a 90% probability, most likely in the next 2-3 quarters, we expect that Germany will be put on negative watch and then downgraded by Moody's to Aa1. We expect a similar action by S&P, although they may act a little less quickly than Moody's. After the one-notch downgrade, we expect no further rating action over the next 2-3 years, given the country's solid economic fundamentals.

While all parties represented in the German parliament are willing to take further measures supporting periphery countries, Germany is unlikely to agree to far-reaching mutualisation of sovereign debt. With the opposition parties against an easy use of the ESM to recapitalize banks directly and similar views shared by coalition MPs, Germany is likely to delay the use of the proposed new tool for the ESM (see Euro Economics Weekly - Assessing Germany's Resilience). The delay of the interim verdict of the country's constitutional court to September 12 highlights that even the participation of Germany in the ESM and the Fiscal Compact is not straightforward in respect of the German constitution. Therefore, it might be that in addition to additional requests from the court to involve the German parliament in the ESM decision-making, the court could highlight that there are limits regarding the size of Germany's exposure to the rescue facilities.

While Germany is negatively affected by the recession in the periphery euro area countries, we expect that Germany will avoid falling into recession. While still favourable global demand and the weaker euro exchange rate should continue to lead to an expansion of German exports, we expect that solid domestic demand will keep Germany on a modest expansionary path. We expect GDP to increase by 1.2% in 2012 and by 0.8% in 2013. Ongoing gains in employment and wages not only fuel private consumption, they also propel tax revenues and ease general government expenditure pressure. We expect that the general government deficit will shrink further from 1.0% of GDP in 2011 to 0.3% in 2012 and 0.2% in 2013. Even when taking into account further stock flow adjustments, reflecting the developments of the German bad banks and the contributions to the EFSF, we think the German debt to GDP ratio will peak at around 82.8% in 2012.

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Citi Ratings Outlook: France

	Current	Near-Term	Long-Term
S&P	AA+ (Neg)	AA+ (Neg W)	AA (Neg)
Moody's	Aaa (Neg)	Aa1	Aa1 (Neg)

Source: Citi Investment Research and Analysis

France's current ratings are expected to remain under pressure over the near term and long term. Both S&P and Moody's have the French sovereign on "Negative Outlook". In its recent report[2], Moody's noted that it would "*downgrade France's government debt rating in the event of an unsuccessful implementation of economic and fiscal policy measures, leading to the failure of the government's attempt to stabilise and reverse the high public debt ration, generating a further weakening of the debt metrics against peers an further reducing France's resiliency to potential economic and financial shocks*". S&P had previously lowered France's credit rating by one notch to AA+ on January 13, largely reflecting the general deterioration in Europe's creditworthiness and the "*highly integrated economic and financial environment of the European Economic and Monetary Union*."

The new government's decision to take supplementary measures to maximise its chance of hitting the budget deficit target of 4.5% of GDP in 2012 was necessary and will probably be interpreted positively by rating agencies, suggesting that a rating action is not imminent. However, with Grexit as our baseline, we argue that France's rating will be affected in the near term. During the next six to nine months, we expect that Moody's will place the sovereign rating on watch for a possible downgrade, to be followed by a one-notch cut to Aa1. For S&P, their lower starting point suggests that the likelihood of an additional cut is more limited.

We believe that the economy will stay weak to end-2013 as the government attempts to reduce the budget deficit to 3% of GDP in 2013, relying heavily on tax increases instead of expenditure cuts. In our *Euro Economics Weekly - France: Hard Choices Lie Ahead*, we argue that "*the strategy to increase the fiscal pressure from already elevated levels could easily backfire given the fragility of the growth outlook and depressed levels of economic confidence. But slashing public spending without enough time to review where the axe needs to fall could also have serious political consequences in a country where the preservation of the social model is taken very seriously*." We conclude that "*structural reforms will need to be implemented in the near term to boost the economy's potential growth rate, without which the debt trajectory would become problematic*".

Hence, over the long term, we expect both rating agencies to maintain a Negative Outlook on France's sovereign rating, essentially because of some continued fragility in the euro area crisis management framework and overly optimistic GDP baselines. For S&P, we envisage another one-notch move to AA, with Negative Outlook.

[2] Moody's Credit Opinion: Government of France, 24 May 2012

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Citi Ratings Outlook: Italy

	Current	Near-Term	Long-Term
S&P	BBB+ (Neg)	BBB	BBB-
Moody's	Baa2 (Neg)	Ba1 (Neg)	Ba2

Source: Citi Investment Research and Analysis

After Italy's sovereign rating was downgraded one notch to A3 and put on Negative Outlook by Moody's in February as part of the agency's broader review on European sovereign credit quality, Moody's further downgraded Italy's sovereign debt rating by two notches to Baa2 with Negative Outlook on 13 July. This was a larger and earlier move than we had expected. According to Moody's, the downgrade chiefly reflected two factors: the increase in funding costs which the country is experiencing and the deterioration of the country's near-term economic outlook.

S&P last downgraded the Italian sovereign rating by one notch to BBB+ (Negative Outlook) from A- in January 2012. According to S&P's, their downgrade reflected the agency's view that Italy's external financing costs had risen markedly and were likely to remain elevated for an extended period of time.

Over the near term (next 6-9 months), we believe that Moody's will downgrade Italy's sovereign rating further by two notches to Ba1 and expect S&P to downgrade Italy further by one notch to BBB. This reflects our expectation that the situation in Greece will escalate further, probably culminating in a Greek exit from the euro. In addition, we expect that weakness in Italy's economic and fiscal outlook will result in continued market strains, leading the country to seek external assistance from the EFSF/ ESM before the end of 2012.

Over the longer term (next 2-3 years) we expect S&P to lower Italy's sovereign rating by one further notch to BBB-. We expect the S&P downgrade to reflect the agency's response to the further deterioration in the financing conditions facing the Italian sovereign. We also expect Moody's rating of the Italian sovereign to migrate down by a further one notch to Ba2 over the longer term as it becomes apparent that Italy's debt sustainability problem will not be easily eradicated. Both potential growth and actual growth are likely to stay weak and the prospects for further growth-enhancing structural reform will probably fade with the resumption of normal politics post 2013. The general government debt/GDP ratio is likely to rise above 130% of GDP in 2013E and higher thereafter.

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Citi Ratings Outlook: Spain

	Current	Near-Term	Long-Term
S&P	BBB+ (Neg)	BBB	BBB-
Moody's	Baa3 (Neg W)	Ba1 (Neg)	Ba2

Source: Citi Investment Research and Analysis

Moody's downgraded Spain by three notches to Baa3 from A3 on June 13, 2012, and left it on review for possible further downgrade. S&P downgraded Spain by two notches from A to BBB+ on April 26, and has it on Negative Outlook, while Fitch also downgraded Spain by three notches (Negative Outlook) on June 7.

We expect another downgrade by both S&P (to BBB) and Moody's (to Ba1) later in the year, with Moody's keeping Spain on Negative Outlook. For Moody's, this further downgrade implies loss of Investment Grade status. Over the longer term, we think that further downgrades are likely by both S&P and Moody's, implying that Spain would settle at the lower end of the Investment Grade spectrum for S&P and move further into speculative territory for Moody's.

On June 13, Moody's noted that its review for possible downgrade would *"focus on the outcome of the ongoing external audits of the Spanish banking system, the conditionality and details of the EFSF/ESM loan agreement, and the specific execution strategy developed for the banking system's recapitalisation"*[3]. It also noted that it *"will also consider any further initiatives at the euro area level"*. On July 16, Moody's said that it considered the revised fiscal targets for Spain and the most recent set of austerity measures announced to be credit positive, as *"Spain's revised fiscal stance is more credible and the country is more likely to meet the new targets. The revisions also signal a more flexible stance on the part of the other euro area countries."*[4] In addition, developments since June 14 hold out the prospect that the Spanish bank bail-out will be transferred off the government's books once the ESM obtains the option to provide direct capital injections. We therefore consider it likely that Moody's will not downgrade Spain at the conclusion of its current review process and instead will affirm its Baa3 rating.

However, we consider that, even with the latest set of austerity measures, the revised deficit target for 2012 is still unlikely to be hit, while we expect an overshoot of around 1% of GDP relative to the targets for 2013 and 2014. Moreover, on June 13, Moody's noted that *"Spain's rating - as well as the ratings of other euro area countries - could be adversely affected if the risk of a Greek exit from the euro area were to rise further."* As discussed in the GEOS Overview, we now think that Grexit is more likely and probably will occur soon, while the Spanish sovereign will need to use rescue facilities at the sovereign level. We therefore expect Moody's to downgrade Spain by one notch to Ba1 over the next 6-9 months. We also expect a one-notch downgrade in the near term by S&P.

Over the longer term (next 2-3 years), we expect that Spain's economy will remain weak, with a further uptrend in the general government debt/GDP ratio. As a result, we expect that Spain will be downgraded by a further notch by both S&P and Moody's to BBB- and Ba2, respectively. For S&P, which follows slightly different ratings criteria from Moody's, Spain would thus settle at the lower end of the Investment Grade spectrum, while for Moody's it would descend further into speculative territory.

[3] See http://www.moodys.com/research/Spain-Government-of-Credit-Opinion--COP_704550

[4] See http://www.moodys.com/research/Spains-New-Measures-to-Achieve-More-Realistic-Fiscal-Targets-Are-Issuer-Comment--PBC_143914

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Citi Ratings Outlook: Austria

	Current	Near-Term	Long-Term
S&P	AA+ (Neg)	AA+ (Neg W)	AA (Neg)
Moody's	Aaa (Neg)	Aa1	Aa1 (Neg)

Source: Citi Investment Research and Analysis

Austria weathered last year's slowdown in economic activity reasonably well, and, while sentiment indicators signal a deterioration in economic activity, the country probably will avoid a recession. To us, the government's official forecast of 0.6% for 2012 and the target of a limited increase in the general government deficit from 2.6% of GDP in 2011 to 3.0% in 2012 looks reasonable. However, the GDP forecast of 1.3% for 2013 looks too optimistic to us and we doubt that the government will be able to reach the targeted reduction in the deficit ratio to 2.1% in 2013, despite approval of a multi-year consolidation package with a total volume of 2.5% of GDP for the period 2012 to 2016.

Recent reports by the rating agencies emphasised that with the country's banking sector's high exposure to Central and Eastern European countries and sizable exposure to the euro area periphery countries, Austria's general government budget position remains vulnerable. Eurostat data show that the country's contingent liabilities (outside the general government account) with respect to financial institutions of 5.7% of GDP are not particularly large. However, recent comments by Finance Minister Maria Fekter – saying that the government is unwilling to create a bad bank to pool stressed assets of the banks that are fully or partly held by the sovereign because it would markedly lift the government's debt ratio – highlight the sensitivity of the sovereign in respect of the banking sector. Further problems in the banking sector are likely to increase the pressure on the Austrian sovereign, although the ability of the ESM to lend directly to banks may limit this burden on the sovereign.

While we do not expect Moody's to downgrade Austria's Aaa rating with Negative Outlook in the late Q3 re-assessment, we expect Moody's to downgrade Austria to Aa1, following a period of being under negative watch, after a likely Greek exit from the euro area. Given the country's vulnerabilities with respect to the banking sector, we believe that Moody's will put in place a Negative Outlook on Austria's Aa1 rating over the longer term. As a reaction to Grexit, we also expect S&P to downgrade Austria by one notch to AA+, but it will probably take somewhat longer (i.e. not within the next 9 months) before the downgrade is implemented. Over time we expect that S&P will assign a Negative Outlook to the AA rating.

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Citi Ratings Outlook: Belgium

	Current	Near-Term	Long-Term
S&P	AA (Neg)	AA (Neg W)	AA-
Moody's	Aa3 (Neg)	A1	A1

Source: Citi Investment Research and Analysis

Belgium has been one of the soft core member states enjoying a significant rally in its spreads versus the German benchmarks, and in our view appears to be well positioned to join the select group of countries with negative nominal yields at the short end of the curve. With the new government busy working towards achieving its objective of reducing the budget deficit to less than 3% of GDP in 2012, investors have been expressing some optimism about the sixth-largest euro area economy, essentially putting behind them the complicated political situation that left the country without a government for nearly 18 months. Our GDP forecast envisages that the economy will slow during the remainder of 2012, like most of its core and soft-core peers.

Belgium's rating strengths are well known: according to S&P the country is a wealthy, export-orientated and competitive economy with a strong track record of fiscal consolidation since the 1990. We agree with their assessment. Nevertheless, our lower baseline GDP forecast (particularly for 2013, requiring the government to identify additional measures to continue to shrink the budget deficit), combined with the uncertainty over how much the sovereign might have to bear with respect to its bank recapitalisation effort and a Grexit scenario, point to some downside rating risks. We believe that Moody's will likely put the sovereign rating on review for possible downgrade, and implement a one notch cut to A1 in the next 6-9 months. Over the long term, we believe that the downward rating pressure will remain limited, with Belgium continuing to enjoy a high confidence level (AA- & A1).

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Citi Ratings Outlook: Greece

	Current	Near-Term	Long-Term
S&P	CCC	D	CCC
Moody's	C	C	Caa2

Source: Citi Investment Research and Analysis

S&P moved Greece out of the SD rating into a triple C rating (outlook stable) on 2 May to reflect the conclusion of the debt restructuring deal. S&P said that its assigned CCC rating reflected the reduction and the improved maturity of Greece's sovereign debt, brought about by the distressed debt exchange. The agency acknowledged that Greece's sovereign debt exchange has alleviated near-term funding pressures. However, Greece's debt burden remains high and S&P warned that "*this adjustment has implementation risks given the likely further contraction of the sovereign's GDP this year and next, which will likely result in persistent social pressures*."[5]

Over the near term (next 6-9 months) we expect Greece's sovereign rating to be downgraded further, reflecting our view that Greece will leave the euro area with about 90% probability, and believe the most likely timeframe for Greece to leave is in the next 2-3 quarters, probably following the September assessment. According to Moody's June 2012 assessment, a Greek exit from the euro area would result in large losses to investors due to the redenomination of government debt and private debt securities issued under Greek law and would result in severe disruption of the country's banking system and major dislocations in the real economy. Under such a scenario, S&P argued that the CCC rating would fall further to D. Moody's already rates Greece as C, its lowest rating.

Over the longer term (2 to 3 years), we expect the Greek sovereign rating to rest around CCC, which is at the lower end of sub-investment grade. Even once the initial adverse effects on growth of Grexit fade, we expect the country's default history and the reintroduction of exchange rate risk to keep Greece's funding costs high.

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Citi Ratings Outlook: Netherlands

	Current	Near-Term	Long-Term
S&P	AAA (Neg)	AAA (Neg W)	AA+ (Neg)
Moody's	Aaa (Neg)	Aa1	Aa1 (Neg)

Source: Citi Investment Research and Analysis

While the Dutch parliament approved a package in order to reduce the general government deficit to 3% of GDP in 2013, apart from the 2-point VAT rate hike scheduled for October 2012, most of the other measures are not approved yet and will depend on the outcome of the early election which will take place on September 12. Recent polls suggest that there will be an inconclusive election outcome, with large support for far-right and left parties. Therefore it will probably be very difficult to form a new government which will go ahead in implementing the compromise fiscal measures agreed at end-April.

With the recent revisions, the GDP data show a modest increase in activity (0.3% QQ) in 1Q, after three consecutive negative quarters. Nevertheless, we expect the Dutch economy to move back into recession in 2012, with domestic demand undermined by the ongoing correction in the housing sector and deleveraging by households. We expect that GDP will fall by about 1.4% in 2012 and by a further 0.6% in 2013, and hence believe the country will fail to achieve the targeted

[5] Source: S&P Research Update, 2 May 2012.

reduction in the deficit to 3.0% of GDP in 2013, even if the proposed austerity measures are fully implemented. We expect a with a deficit ratio of about 4.7% of GDP in 2012 and 3.7% of GDP in 2013. Including the country's commitments to the European rescue facilities (EFSF and ESM) the debt ratio will continue to increase from 65.2% of GDP in 2011 to 73% in 2012E and about 76% in 2013E.

Moody's highlighted the increased likelihood that the Netherlands will have to contribute more to the euro area rescue facilities, and potential negative effects of the crisis on the Dutch banking sector, as the main driver behind the decision to put the Netherlands on Negative Outlook. However, Moody's also put some weight on the country's weak growth performance, high household debt and housing correction. As is the case with the other Aaa Negative Outlook countries, we expect that Grexit will prompt Moody's to put the Netherlands on Negative Watch, followed by a one notch ratings downgrade. S&P is likely to follow a similar path but perhaps a little later. We expect that both rating agencies will put the country under negative watch in the longer term, reflecting political uncertainty and ongoing weak economic growth partly caused by the overhang of high household debt.

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Citi Ratings Outlook: Portugal

	Current	Near-Term	Long-Term
S&P	BB (Neg)	B+	CCC
Moody's	Ba3 (Neg)	B1	Caa2

Source: Citi Investment Research and Analysis

S&P downgraded Portugal's sovereign rating by two notches from BBB- to BB (Negative Outlook) in January as part of the agency's broader review of the euro area economies. Moody's followed soon after with a one-notch downgrade of Portugal's sovereign rating to Ba3, also with Negative Outlook, on February 13.

Over the near term (next 6-9 months), we believe that Portugal will be downgraded further by two notches to B+ by S&P and by one notch to B1 by Moody's to reflect adverse fiscal trends and contagion from the crisis in Spain – the country's largest trading partner – and from Grexit. Moreover, we also expect it to become clear to the Troika that, in spite of Portugal's efforts to meet the 4.5% of GDP deficit target for 2012, the country is unlikely to be able to fund itself in the markets (apart from issuing bills) as early as in the second half of next year (as assumed under the current programme). The weak economy will likely lead to fiscal slippage due to lower-than-anticipated tax revenues and higher-than-expected social security payments as unemployment reaches new record highs. Moreover, the crisis in Greece and Spain will probably keep market appetite for euro area periphery sovereign risk very low. As a result, we expect Portugal to be granted a second programme (or an extension of the first programme) in the next 9 months to fully cover its medium- and long-term funding needs to at least the end of 2014.

Over the longer term (next 2-3 years) we expect S&P and Moody's both to downgrade Portugal down to the mid CCC range. This reflects our view that Portugal will have to go through some form of debt restructuring to bring its debt stock to sustainable levels. We expect that the debt restructuring will happen at some point in 2013-15.

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Citi Ratings Outlook: Denmark

	Current	Near-Term	Long-Term
S&P	AAA	AAA	AAA
Moody's	Aaa	Aaa	Aaa

Source: Citi Investment Research and Analysis

From the very strong starting point (surplus of 5% of GDP in 2005-06), Denmark's fiscal position has worsened markedly in recent years. Had it not been for unexpected and extraordinary revenues from taxation of pension yields (amid surprisingly high returns on equity and bond investments), the 2011 budget deficit would have landed at an estimated 4% of GDP instead of the 1.9% of GDP outturn. The government has used its fiscal scope to support growth, and will continue to do so (as part of its "kick-start" stimulus package), pushing the deficit to above 3% of GDP this year. Government debt is still comparatively low in a European context (46.5% of GDP). Hence in the near term the fiscal outlook appears relatively good. If Denmark does not get back on track in terms of growth (currently generated exclusively by public spending/investment) there could be some risks of a worse debt profile in the medium term. Nevertheless, we regard Denmark as a fairly solid AAA.

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Citi Ratings Outlook: Finland

	Current	Near-Term	Long-Term
S&P	AAA (Neg)	AAA (Neg)	AAA (Neg)
Moody's	Aaa	Aaa (Neg)	Aaa (Neg)

Source: Citi Investment Research and Analysis

Finland is the only euro area country (except for Luxembourg), which is both AAA-rated and meets all of the Maastricht Treaty requirements. The fiscal deficit was 0.8% of GDP in 2011, the lowest in the euro area, and second only to Sweden (0.9% of GDP surplus) in the EU. Public debt reached 48.5% of GDP. However, with a deteriorating economic outlook and an ageing population, the public debt ratio is set to rise in coming years. Finland is currently rated AAA, but with a Negative Outlook by S&P, suggesting that over the longer term, downward pressure on the rating is more likely than in the other Nordic countries, which are all rated AAA Stable. As part of the plan to bring public finances onto a sustainable path, the 2012 budget implies a mild fiscal contraction this and next year, with focus on increasing labour force participation in the context of a shrinking labour supply. In the longer term, Finland faces challenges from the rapidly aging population, slowing productivity growth, and eroding competitiveness (has worsened significantly in recent years, with contracting export market shares and a small current account deficit in 2011, the first in nearly two decades). Finland continues to have one of the lowest risk premia versus Germany in the euro area (the 10-year bond spread has narrowed from about 50bp during 2H 2011 to 35bp in 2Q 2012), and, although Finland's triple-A rating remains on Negative Outlook by S&P, we believe that the effects of a possible downgrade are likely to be limited given Finland's comparatively low level of public debt.

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Citi Ratings Outlook: Sweden

	Current	Near-Term	Long-Term
S&P	AAA	AAA	AAA
Moody's	Aaa	Aaa	Aaa

Source: Citi Investment Research and Analysis

We regard Sweden as a solid AAA. Swedish government finances are strong in a European context and the budget balance is expected to remain around zero this and next year before gradually rising above the government's target in 2015 (which stipulates that the general government fiscal balance should average 1% of GDP over the business cycle). Sweden's general government debt level is low (below 40% of GDP) and has been falling since 2001 (except in 2009), and probably will continue to fall in the next few years. The next election is in 2014, and none of the main political parties are proposing significant fiscal stimulus or retrenchment. The government has made it clear that it prioritizes safety margins in the budget over stimulating demand, underscoring its image as a prudent guardian of public finances. However, with a marked growth slowdown and rising unemployment this year, we expect the government to make greater use of its fiscal flexibility. Recent comments from Finance Minister Borg also suggest that the Autumn Budget Bill will be more expansionary than previously indicated.

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Citi Ratings Outlook: Norway

	Current	Near-Term	Long-Term
S&P	AAA	AAA	AAA
Moody's	Aaa	Aaa	Aaa

Source: Citi Investment Research and Analysis

We regard Norway as a solid AAA. Norway found large oil resources in the North Sea in the early 1970s. On the back of this, it has a large fiscal surplus, likely to be around 13% of GDP this year. The use of oil revenues is limited to an amount equivalent to an estimated 4% real return on the assets of the value of the Government Pension Fund Global (GPFG, was introduced in 2001). Overspending relative to the rule was quite common in the earlier years of its existence, though adherence to the rule has become easier as the fund's size has grown in recent years. The spending of oil revenues is set to undershoot the fiscal policy rule, at 3.5% of the Government Pension Fund – Global (GPFG), for a third consecutive year in 2012. To be sure, the "undershooting" is not a result of active budget measures, but rather higher-than-anticipated oil prices, which in turn have implied a higher-than-expected value of the GPFG. Fiscal stimulus this year will amount to 0.75% of trend-GDP, but should the Norwegian economy deteriorate markedly, the government will likely add more stimulus (fiscal policy added 2%-points to mainland GDP in 2009). The Norwegian government is selling bonds, but has colossal financial assets and hence a net asset/GDP ratio of more than 150% of annual GDP.

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Citi Ratings Outlook: UK

	Current	Near-Term	Long-Term
S&P	AAA	AAA (Neg)	AA+
Moody's	Aaa (Neg)	Aaa (Neg)	Aa1

Source: Citi Investment Research and Analysis

We regard the UK as a weak AAA. The underlying fiscal deficit (excluding effects of the transfer of the pension assets of the state-owned postal service) has risen by about £4bn YoY in April-June, with receipts of income tax and corporation tax hit by the weak economy. We expect that the underlying fiscal deficit will rise slightly over the full year, overshooting the official forecast by £10bn-£15bn (0.6%-1% of GDP). Adverse cyclical effects probably will persist in coming years, with the drag from household deleveraging and the EMU crisis likely to keep growth well below the OBR's existing forecasts. As a result, we expect that the general government gross debt/GDP ratio will continue to climb, rising from 82.5% at end-2011 to over 100% of GDP in 2014 or 2015. That puts the UK out of line with other AAA-rated sovereign borrowers.

Moreover, the UK's commitment to its fiscal consolidation timetable is likely to come under question if, as we expect, the EMU crisis worsens and continues to cast a deep shadow over UK growth prospects. At present, the UK plans structural fiscal tightening of about 1½% of GDP per year in both the 2013/14 and 2014/15 fiscal years, after tightening of about 0.3% of GDP in the current fiscal year (2012/13). But, with the private sector deleveraging and little chance of export-led growth (given the EMU crisis) in our view there is a respectable case for the government to defer some of the fiscal tightening planned for 2014 and 2015 further into the future. Such a move would be consistent with the UK's key fiscal rule, which is to eliminate the cyclically adjusted current account deficit on a rolling five-year horizon. But, it would imply that more of the UK's fiscal tightening will be deferred until after the next election (for which the last possible date is mid-2015). A longer timetable for fiscal consolidation is sensible in economic policy terms, in our view. However, with the coalition's poor opinion poll ratings, and Labour's ambiguous stance on fiscal consolidation, there inevitably will be sizeable political uncertainties as to whether the path back to fiscal sustainability will actually be maintained if much of the tightening is deferred until post-2015.

Moody's and Fitch already have put the UK on "Negative Outlook", citing risks that economic underperformance will prevent the deficit falling as fast as the government hopes. S&P have reaffirmed the UK's status as a AAA, with a "stable outlook", emphasising the government's success in hitting its fiscal targets so far and the UK's strong policy framework rather than risks of economic slippage. However, with the weak economic outlook and adverse fiscal trends, we are bringing an expected move to a "Negative Outlook" from S&P into our near-term forecast (2-3 quarters ahead), whereas previously we put this in our longer term forecast (2-3 years ahead). Moreover, with economic weakness, the rising debt/GDP ratio and risks that much of the UK's fiscal consolidation will not be completed by the next election, we now pencil in a one-notch downgrade by both major agencies for the next 2-3 years.

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Citi Ratings Outlook: Ireland

	Current	Near-Term	Long-Term
S&P	BBB+ (Neg)	BBB-	BB
Moody's	Ba1 (Neg)	Ba2	Ba3

Source: Citi Investment Research and Analysis

Ireland

There are complex cross-currents in the outlook for Ireland's sovereign rating. First, the CSO recently revised up 2011 GDP growth from 0.7% to 1.4%, and nominal GDP growth was surprisingly strong in Q1-2012 (up 4.3% YoY) – with the first YoY rise in nominal domestic demand since Q4-07. These trends help explain the recent resilience in revenues. Second, real GDP growth in Q1-2012 was (as expected) very weak, down 1.1% QoQ, and Ireland's high export exposure to the euro area points to risks that the economy will underperform official forecasts going forward – hence hitting future revenue growth. Third, the end-June Eurogroup statement hinted at the possibility that Ireland may be able to achieve some form of debt relief on the country's large bank recapitalisation costs (which have totalled more than 40% of annual GDP). However, it is unclear whether this would be merely a maturity extension and coupon reduction on the promissory notes (which could cut the deficit by about 1% of GDP per year in coming years but would not greatly affect the debt/GDP ratio) or whether there will be a much bigger shift of existing bank recapitalisation costs from the Irish government to the ESM.

Our base case is for the economy to underperform official forecasts, hence leading to medium-term deficit and debt overshoots. We have not included any promissory note deal or shift of bank recapitalisation costs from the Irish government's balance sheet to the ESM. We expect that Ireland will need, and get, some form of second bailout extending beyond the current programme (which is scheduled to end in late 2013). We do not expect this will include PSI initially, but some form of PSI will be likely eventually if European partners insist that the bank bailout costs remain in full on the Irish government's balance sheet. Conversely, if all or most of the bank bailout costs can be removed from Irish government debt, then Ireland may well not need PSI at all. Our forecast of further ratings downgrades therefore has considerable risks on both sides, and if the government is successful in shifting bank bailout costs off its own balance sheet then Ireland's sovereign debt may even be upgraded over time (although it could still get caught up in a general post-Grexit downgrade).

Figure 3. Selected Countries — Economic Forecast Overview (Percent), 2011-2016F

	GDP Growth						CPI Inflation						Short-Term Interest Rates					
	2011	2012F	2013F	2014F	2015F	2016F	2011	2012F	2013F	2014F	2015F	2016F	2011	2012F	2013F	2014F	2015F	2016F
Global	**3.0**	**2.5**	**2.8**	**3.4**	**3.7**	**3.9**	**3.6**	**2.7**	**2.7**	**3.0**	**2.8**	**2.8**	**2.48**	**2.30**	**2.22**	**2.48**	**2.77**	**3.16**
Based on PPP weights	*3.6*	*3.0*	*3.3*	*3.8*	*4.0*	*4.2*	*4.2*	*3.1*	*3.0*	*3.3*	*3.1*	*3.1*						
Industrial Countries	**1.3**	**1.1**	**1.1**	**1.9**	**2.3**	**2.6**	**2.3**	**1.7**	**1.5**	**1.9**	**1.5**	**1.6**	**0.76**	**0.56**	**0.46**	**0.60**	**0.95**	**1.55**
United States	**1.7**	**1.9**	**2.0**	**3.5**	**3.5**	**4.0**	**2.5**	**1.7**	**1.6**	**2.1**	**2.2**	**2.2**	**0.25**	**0.25**	**0.25**	**0.40**	**1.15**	**2.10**
Japan	**-0.7**	**2.7**	**2.1**	**0.3**	**1.5**	**1.2**	**-0.3**	**0.2**	**-0.1**	**2.7**	**0.3**	**0.5**	**0.10**	**0.10**	**0.10**	**0.10**	**0.10**	**0.27**
Euro Area	**1.5**	**-0.6**	**-0.9**	**0.6**	**1.0**	**1.4**	**2.7**	**2.3**	**1.8**	**1.2**	**0.9**	**1.0**	**1.19**	**0.69**	**0.25**	**0.25**	**0.31**	**0.75**
Canada	2.4	2.0	2.2	2.7	3.2	3.5	2.9	1.7	1.8	2.0	2.0	2.0	1.00	1.00	1.63	2.19	2.50	3.00
Australia	2.1	3.7	3.4	3.8	3.8	3.6	3.4	1.8	3.2	2.9	2.7	2.5	4.75	3.56	3.44	4.50	5.00	5.25
New Zealand	1.3	2.3	2.8	3.0	3.2	3.4	4.0	1.5	2.2	2.6	2.9	2.8	2.50	2.50	2.94	4.00	5.00	5.50
Germany	3.1	1.2	0.8	0.8	1.3	1.5	2.3	2.0	2.2	2.5	2.2	2.2						
France	1.7	-0.2	-0.2	0.9	1.2	1.8	2.1	2.0	1.3	1.3	1.7	1.5						
Italy	0.5	-2.5	-2.2	0.0	0.7	0.7	2.9	3.0	1.8	0.1	-0.1	0.8						
Spain	0.7	-1.8	-3.3	0.2	1.3	1.9	3.1	1.8	2.1	0.8	0.8	1.3						
Greece	-6.9	-7.5	-10.1	-1.1	4.5	4.3	3.1	1.0	15.1	19.0	6.3	6.0						
Ireland	1.4	-0.7	0.6	2.6	2.3	2.4	0.2	0.8	0.2	0.5	0.6	0.7						
Portugal	-1.6	-4.6	-5.6	-0.8	1.4	2.1	3.6	2.5	1.5	0.6	0.0	0.1						
Netherlands	1.1	-1.4	-0.6	0.7	1.1	1.4	2.3	2.8	2.5	1.6	1.9	1.8						
Belgium	2.0	0.2	-0.2	0.8	1.5	1.9	3.5	2.5	1.3	1.9	2.2	2.2						
Denmark	1.0	0.7	1.3	1.6	1.7	1.8	2.8	2.5	1.7	1.5	1.6	1.8	1.30	0.16	-0.30	0.00	0.41	1.00
Norway	2.5	3.0	2.9	2.7	2.7	2.9	1.3	0.9	1.7	2.0	2.4	2.5	2.10	1.50	1.90	2.30	2.90	3.30
Sweden	4.0	0.4	1.9	2.4	2.5	2.7	3.0	1.2	1.6	2.2	2.1	2.0	1.80	1.20	1.10	1.60	2.10	2.50
Switzerland	2.1	1.4	0.8	1.1	1.1	1.1	0.2	-0.9	-1.4	-0.9	0.4	0.7	0.22	0.00	0.00	0.00	0.00	0.00
United Kingdom	0.7	-0.5	0.3	0.9	1.5	2.3	4.5	2.5	1.8	1.8	1.5	1.5	0.50	0.50	0.50	0.50	0.50	1.04
Emerging Markets	**6.0**	**4.9**	**5.5**	**5.7**	**5.7**	**5.7**	**6.0**	**4.5**	**4.6**	**4.7**	**4.7**	**4.6**	**5.6**	**5.2**	**5.0**	**5.3**	**5.4**	**5.4**
China	**9.2**	**7.9**	**8.0**	**7.6**	**7.3**	**7.0**	**5.4**	**2.7**	**2.9**	**3.8**	**4.0**	**4.0**	**3.2**	**3.5**	**3.0**	**3.6**	**4.0**	**4.0**
Taiwan	4.0	2.4	3.6	4.5	4.5	4.5	1.4	1.9	2.1	1.8	1.8	1.8	0.8	0.9	0.9	1.0	1.2	1.4
India	6.5	6.4	6.9	7.1	7.3	7.4	8.9	7.4	6.5	6.0	6.0	6.0	8.2	7.8	7.5	7.5	7.5	7.5
Indonesia	6.5	6.1	6.3	6.7	6.5	6.7	5.4	4.4	4.7	5.3	5.8	5.4	5.4	3.8	4.2	4.5	4.6	5.1
Korea	3.6	2.8	3.6	3.8	4.0	4.2	4.0	2.8	3.0	3.1	3.0	3.2	3.2	3.1	2.6	3.3	4.0	4.4
Czech Republic	1.7	-1.1	0.6	2.0	2.2	2.8	1.9	3.5	2.6	1.4	1.7	1.6	0.8	0.6	0.3	1.0	1.6	2.3
Hungary	1.7	-0.9	0.8	2.0	2.0	1.8	3.9	5.6	3.9	3.5	3.1	3.3	6.0	6.9	5.8	5.5	5.4	5.0
Poland	4.3	2.7	2.4	3.1	3.4	3.4	4.3	3.9	2.6	2.5	2.5	2.5	4.2	4.7	4.3	4.4	4.8	4.8
Romania	2.5	1.3	3.0	4.2	4.3	4.3	5.8	2.8	2.7	2.5	2.5	2.5	6.2	5.3	5.0	5.0	5.0	5.0
Russia	4.3	3.5	4.0	4.1	4.0	4.2	8.4	5.1	6.9	5.8	5.5	5.0	8.1	8.0	7.1	6.0	6.0	5.4
Turkey	8.5	2.5	4.3	4.6	4.6	4.6	6.5	9.1	7.0	6.0	5.9	5.4	6.0	5.8	6.3	8.0	7.6	7.5
Nigeria	7.8	7.4	6.8	7.2	6.9	7.2	10.8	12.4	9.8	10.3	9.5	9.0	8.9	15.0	12.5	10.5	10.0	9.5
South Africa	3.1	2.7	3.6	4.2	4.4	4.2	5.0	5.8	5.0	5.2	5.3	5.3	5.5	5.3	5.0	5.3	5.5	5.5
Argentina	8.9	1.5	3.0	2.0	2.0	3.5	9.8	9.8	11.8	15.0	15.0	18.0	13.5	13.3	17.7	22.0	25.0	25.0
Brazil	2.7	1.8	4.5	4.5	4.5	4.5	6.6	5.1	5.2	4.5	4.0	4.0	11.7	8.5	7.9	9.4	9.0	8.3
Mexico	3.9	3.9	3.8	3.5	3.6	3.7	3.4	4.0	3.9	3.9	3.8	3.7	4.5	4.5	4.5	4.6	5.5	6.4
Venezuela	4.2	5.0	3.5	4.0	3.0	2.5	27.1	23.3	27.8	31.9	29.9	29.9	13.3	14.4	14.4	13.0	12.9	12.7

Note: For inflation, we use the PCE deflator in the US, wholesale price index in India, GDP deflator in Ireland. For Indonesia we refer to the FasB1 rate to reflect actual money market rates. Source: Citi Research

Figure 4. Selected Countries — Economic Forecast Overview (Percent), 2011-2016F

	Current Balance (Pct of GDP)						Fiscal Balance (Pct of GDP)						Government Debt (Pct of GDP)					
	2011	2012F	2013F	2014F	2015F	2016F	2011	2012F	2013F	2014F	2015F	2016F	2011	2012F	2013F	2014F	2015F	2016F
Global	**0.3**	**0.1**	**-0.1**	**-0.2**	**-0.1**	**-0.1**	**-4.9**	**-4.3**	**-3.4**	**-2.9**	**-2.6**	**-2.3**	**81**	**82**	**82**	**82**	**81**	**79**
Based on PPP weights	*0.5*	*0.2*	*0.0*	*-0.2*	*-0.2*	*-0.1*	*-4.3*	*-4.0*	*-3.3*	*-2.8*	*-2.5*	*-2.3*						
Industrial Countries	**-0.7**	**-0.9**	**-0.9**	**-0.7**	**-0.6**	**-0.5**	**-6.9**	**-5.9**	**-4.5**	**-3.7**	**-3.1**	**-2.8**	**107**	**112**	**115**	**115**	**116**	**116**
United States	**-3.1**	**-3.2**	**-3.2**	**-3.1**	**-3.2**	**-3.2**	**-9.6**	**-8.1**	**-5.9**	**-4.9**	**-4.0**	**-4.0**	**103**	**107**	**110**	**112**	**112**	**112**
Japan	**2.0**	**1.0**	**1.2**	**1.7**	**1.7**	**1.7**	**-10.7**	**-10.5**	**-7.9**	**-6.6**	**-6.2**	**-5.8**	**228**	**235**	**240**	**241**	**246**	**250**
Euro Area	**0.0**	**0.2**	**0.2**	**0.3**	**0.4**	**0.6**	**-4.1**	**-3.3**	**-2.8**	**-2.4**	**-1.8**	**-1.3**	**87**	**96**	**96**	**95**	**95**	**93**
Canada	-2.8	-2.7	-2.2	-1.7	-1.1	-0.5	-1.4	-1.2	-0.5	-0.1	0.2	0.4	85	85	84	83	81	79
Australia	-2.3	-4.1	-5.3	-4.9	-3.5	-3.2	-3.4	-3.0	0.1	0.1	0.3	0.4	6	10	9	9	8	7
New Zealand	-4.2	-5.0	-7.0	-6.4	-5.8	-5.5	-9.2	-4.1	-3.6	-0.9	0.1	0.9	22	27	31	34	35	36
Germany	5.7	5.2	3.7	3.6	3.4	3.2	-1.0	-0.3	-0.2	-0.4	-0.2	0.0	81	83	82	81	79	77
France	-2.2	-1.9	-1.1	-0.3	0.3	0.4	-5.2	-4.4	-3.8	-3.5	-2.6	-1.8	86	93	99	101	100	99
Italy	-3.2	-2.3	-1.8	-1.5	-1.3	-1.2	-3.9	-2.9	-2.9	-2.5	-2.0	-1.6	120	129	136	138	138	138
Spain	-3.5	-2.9	-2.3	-1.9	-1.7	-1.4	-8.9	-6.5	-5.9	-4.5	-3.6	-2.3	69	93	93	96	97	96
Greece	-9.8	-7.7	-3.4	0.7	2.4	3.0	-9.1	-11.0	-5.2	-2.2	-0.6	-3.7	165	157	437	382	103	92
Ireland	1.1	0.1	2.5	5.2	6.9	8.4	-12.8	-8.3	-8.6	-6.0	-4.9	-5.0	108	120	127	128	128	129
Portugal	-8.1	-4.5	-2.5	-1.5	-1.4	-1.0	-4.2	-5.0	-5.8	-5.8	-3.4	-2.3	108	123	138	93	96	96
Netherlands	8.5	9.7	9.6	8.6	7.6	7.2	-4.7	-4.6	-3.7	-3.7	-2.9	-2.3	65	73	76	79	79	79
Belgium	-1.0	-1.3	-0.8	0.0	0.9	1.4	-3.7	-2.8	-2.6	-2.3	-1.5	-1.1	98	112	119	118	115	112
Denmark	6.6	5.5	5.4	4.0	3.5	3.7	-1.9	-3.5	-2.0	-1.9	-1.7	0.5	47	49	49	50	50	48
Norway	14.0	14.3	14.9	15.2	15.8	16.5	13.8	13.6	14.0	15.0	17.0	18.5	NA	NA	NA	NA	NA	NA
Sweden	7.0	7.0	7.2	7.3	7.2	7.3	0.1	-0.1	-0.2	0.6	1.2	1.5	37	37	36	33	31	28
Switzerland	14.8	12.4	11.1	10.4	10.4	10.5	0.7	0.5	0.1	0.2	-0.1	-0.4	52	51	50	50	50	50
United Kingdom	-1.9	-2.6	-1.4	-0.4	0.4	0.9	-8.4	-6.9	-8.2	-7.7	-7.3	-6.3	83	88	96	102	107	110
Emerging Markets	**2.1**	**1.7**	**1.1**	**0.5**	**0.5**	**0.4**	**-1.4**	**-1.8**	**-1.8**	**-1.7**	**-1.8**	**-1.7**	**33**	**32**	**32**	**31**	**30**	**29**
China	**2.8**	**2.0**	**1.5**	**1.0**	**1.0**	**1.0**	**-1.3**	**-2.4**	**-1.5**	**-1.0**	**-1.0**	**-1.0**	**15**	**16**	**16**	**16**	**15**	**15**
Taiwan	8.8	8.7	8.4	8.0	8.0	8.0	-1.9	-1.6	-1.6	-1.3	-1.0	-0.7	39	39	40	42	43	44
India	-4.0	-3.5	-2.6	-2.2	-1.7	-1.1	-8.4	-8.0	-7.7	-7.0	-6.5	-5.0	69	69	68	66	64	63
Indonesia	0.2	-1.9	-1.2	-0.9	-1.0	-0.9	-1.2	-1.8	-0.7	-1.0	-0.5	-0.5	26	25	24	23	23	22
Korea	2.4	1.8	1.9	1.2	0.2	-0.7	1.5	1.2	1.5	1.6	1.5	2.2	33	33	32	31	29	27
Czech Republic	-3.0	-2.9	-1.9	-2.6	-1.9	-1.4	-3.1	-3.2	-3.1	-2.3	-1.5	-0.5	41	45	47	47	46	45
Hungary	1.7	1.9	2.7	2.5	2.2	2.0	4.3	-3.1	-3.7	-3.0	-3.0	-3.0	81	78	79	78	78	78
Poland	-4.3	-3.8	-4.5	-5.2	-5.3	-4.9	-5.1	-3.1	-2.5	-1.8	-1.5	-1.5	54	52	50	48	47	45
Romania	-4.4	-4.5	-4.7	-5.0	-5.0	-5.0	-4.1	-2.4	-2.2	-2.5	-2.3	-2.0	39	39	39	39	38	37
Russia	5.3	5.7	2.4	-1.0	-1.0	-1.0	2.0	0.3	0.1	-0.1	-1.1	-1.1	8	9	8	8	8	8
Turkey	-10.0	-7.5	-7.0	-6.5	-6.0	-5.6	-1.3	-2.2	-2.5	-2.5	-2.7	-3.0	41	41	39	39	38	36
Nigeria	3.4	2.3	3.5	3.0	1.9	1.3	-3.1	-2.2	-2.1	-2.6	-3.0	-2.6	NA	NA	NA	NA	NA	NA
South Africa	-3.4	-4.7	-5.6	-6.6	-6.3	-5.8	-5.0	-4.8	-4.2	-3.6	-3.5	-3.5	38	41	42	43	43	42
Argentina	0.0	0.3	-0.8	-1.0	-1.0	-1.0	-1.7	-2.8	-3.0	-3.0	-3.0	-3.0	40	38	40	41	42	43
Brazil	-2.3	-2.3	-2.7	-2.9	-3.2	-3.5	-2.6	-1.9	-2.7	-2.5	-2.3	-2.6	54	54	55	55	56	56
Mexico	-0.8	-1.0	-1.4	-2.5	-2.4	-2.6	-2.5	-2.2	-2.0	-1.9	-1.9	-1.8	40	40	38	38	38	37
Venezuela	9.1	7.2	4.1	6.3	6.7	6.1	-5.0	-5.0	-4.0	-5.2	-5.0	-4.8	43	34	35	36	36	37

Note: Fiscal deficit and debt figures for all countries are general government debt and deficits. We assume sovereign debt restructuring in Portugal in 2014 and Greece in 2015. Source: Citi Research

Notes

Notes

Appendix A-1

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