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Editors: Mauro Giorgio Marrano, Economist (UniCredit Bank Milan)
Chiara Silvestre, Economist (UniCredit Bank Milan)

Contents

3	Monthly recap
4	Annual macroeconomic forecasts
5	Quarterly GDP and CPI forecasts
6	Comparison of annual GDP and CPI forecasts
7	Global G10 FI/FX forecasts
	Eurozone
8	Eurozone
10	Germany
12	France
14	Italy
16	Spain
18	Austria
20	Greece
22	Portugal
	Other EU
24	UK
26	Sweden
28	Poland
30	Czech Republic
32	Hungary
	Others
34	US
36	Switzerland
38	Russia
40	Turkey
42	China
44	Global indicators

Monthly recap

- **EMU:** The March round of surveys was generally disappointing, particularly the PMIs, which weakened significantly. However, not all news from last month was negative: the EuroCOIN indicator continued to improve, while hard data in January-February seem consistent with a tentative stabilization in economic activity. Overall, the information availabe thus far indicates the emergence of some downside risks to our GDP forecasts, although visibility remains low. Concurrently, inflation remains on a downward trend, mostly driven by a rapid deceleration in energy prices. The latest weakish data have been reflected in a perceptibly more dovish ECB rhetoric. For the time being, we maintain our forecast for a steady refi rate. However, the risk of a further (final) 25bp cut has significantly increased.

- **US:** Shifting growth from the second to the first quarter. Having stressed the upside risks to our 1Q13 GDP call for several weeks, we are now raising our growth forecast for the first quarter to 3.0% (annualized) from 1.5%. Most importantly, consumer spending weathered the expiration of the payroll tax cut much better than expected. That said, we still do not think that the consumer can completely shrug off the drag from tighter fiscal policy. Accordingly, we are lowering our 2Q13 forecast to 1.8% from 2.8%. The 2013 average still goes up to 2.2% from 2.0%. Low inflation rates and the temporary growth slowdown in the second quarter suggest that the Fed will continue to buy long-term assets at least until the end of this year.

- **CEE:** The CEE economy is also showing signs of recovery, with the PMIs and industry in some economies ticking up in 1Q, although this follows a particularly weak 4Q last year. In many of the newer EU states, there are signs that credit growth has bottomed and although any recovery will be gradual, credit should at least be much more neutral for economic activity this year. Turkey is already seeing an acceleration in credit growth, a trend which poses a risk to domestic demand, while Russia is seeing credit growth slow. Meanwhile, central banks continue to ease monetary conditions. Despite all of the above, however, policy makers are showing impatience with the pace of recovery and in some economies this is impacting the quality of policy making.

- **China:** Recent activity data in China disappointed, showing that the recovery eased over the first three months of this year. While we still see room for some improvement up until this summer based on additional fiscal accomodation and unfolding re-stocking needs, and underpinned by still rising business climate indices, economic growth will level off thereafter. A gradually improving global economy will be outpaced by the recent step-up in measures to rein in house price increases and financial risks, both of which are increasingly weighing on domestic demand. Given the slower start to the year and the weaker momentum, we revise down our 2013 annual GDP growth forecast from 8% to 7¾%.

Table 1: Annual macroeconomic forecasts

	GDP (%)			CPI inflation (%)			Central Bank Rate (EoP)			Government budget balance (% GDP)			Government gross debt (% GDP)			Current account balance (% GDP)		
	2012	2013	2014	2012	2013	2014	2012	2013	2014	2012	2013	2014	2012	2013	2014	2012	2013	2014
Eurozone	-0.5	-0.1	1.2	2.5	1.8	1.7	0.75	0.75	1.00	-3.2	-2.8	-2.6	92.9	94.7	94.3	1.2	1.3	1.4
Germany	0.9	0.8	1.5	2.0	1.3	1.4	-	-	-	0.2	0	-0.2	81.7	79.2	76.9	6.4	5.9	5.5
France	0	0.5	1.3	2.0	1.2	2.0	-	-	-	-4.8	-3.7	-3.1	90.2	92.3	93.4	-2.4	-2.0	-1.7
Italy	-2.4	-1.1	0.7	3.0	1.7	1.7	-	-	-	-3.0	-2.2*	-2.0	127.0	128.1*	126.8*	-0.6	-0.1	0.0
Spain	-1.4	-1.4	0.4	2.4	2.9	2.7	-	-	-	-7.0**	-6.0	-5.1	84.1	91.4	98.7	-1.1	0.5	1.4
Austria	0.8	0.9	1.5	2.4	2.2	1.9	-	-	-	-2.5	-2.3	-1.7	73.4	74.1	73.7	1.8	1.4	1.8
Greece	-6.5	-4.5	0.2	1.5	0.4	0.7	-	-	-	-6.0**	-5.0	-4.2	156.9	179.0	175.0	-2.9	-1.2	-0.3
Portugal	-3.2	-2.5	0.4	2.8	1.4	1.7	-	-	-	-4.9***	-5.5	-4.0	121.0	123.5	124.3	-1.6	-0.6	-0.4
Other EU																		
UK	0.3	0.9	1.4	2.8	2.7	2.3	0.50	0.50	0.75	-6.6	-6.9	-6.1	90.0	94.0	97.1	-3.7	-2.7	-2.4
Sweden	1.2	1.4	2.4	0.9	0.4	1.8	1.00	1.00	1.50	-0.5	-0.5	0	38.2	36.5	35.3	7.2	7.5	7.3
Poland	2.0	1.7	2.3	3.7	1.4	2.4	4.25	3.25	3.50	-3.5	-3.8	-3.0	55.7	57.2	57.1	-3.5	-2.9	-3.3
Czech Rep.	-1.2	0.4	2.2	3.3	1.7	1.7	0.05	0.05	0.50	-4.4	-2.9	-3.0	45.8	47.7	48.7	-2.4	-2.2	-1.8
Hungary	-1.7	-0.1	0.9	5.6	3.0	4.1	5.75	4.00	5.00	-2.1	-3.0	-3.4	78.0	78.1	77.1	1.0	1.5	1.5
Others																		
US	2.2	2.2	2.6	2.1	1.9	2.5	0.25	0.25	0.25	-8.7	-6.9	-5.6	107.2	111.3	113.5	-3.1	-3.0	-3.1
Switzerland	1.0	1.4	1.8	-0.7	-0.1	0.7	0	0	0.50	0.5	0.3	0.3	36.5	35.8	34.7	13.1	12.0	11.0
Russia	3.4	3.6	3.9	5.1	6.3	5.1	5.50	5.25	5.00	0	-1.0	-0.5	10.2	11.2	12.0	4.0	1.6	0.4
Turkey	2.7	3.4	3.9	8.9	6.7	6.3	5.50	5.50	7.00	-2.1	-2.4	-2.9	36.9	35.3	34.7	-6.1	-6.8	-7.5
China	7.8	7.8	7.7	2.7	2.8	3.3	6.00	6.00	6.00	-1.3	-1.7	-1.5	-	-	-	2.6	2.7	3.0

*Fiscal deficit and debt projections do not yet include the impact of the payment of arrears by the public administration.
**Does not include the impact of the bank recapitalization cost (including this cost the figure would be -10.0% for both Spain and Greece).
***Consistent with the Eurostat ruling against the use of revenues from the airport concession for the purpose of deficit reduction.

Source: UniCredit Research

Table 2: Quarterly GDP and CPI forecasts

REAL GDP (% QOQ, SA)

	3Q12	4Q12	1Q13	2Q13	3Q13	4Q13	1Q14	2Q14	3Q14	4Q14
Eurozone	-0.1	-0.6	0	0.2	0.3	0.3	0.3	0.3	0.4	0.4
Germany	0.2	-0.6	0.3	0.5	0.5	0.4	0.4	0.3	0.3	0.4
France	0.1	-0.3	0.2	0.2	0.3	0.4	0.3	0.3	0.4	0.4
Italy	-0.2	-0.9	-0.2	0.1	0.1	0.2	0.2	0.2	0.3	0.3
Spain	-0.3	-0.7	-0.5	-0.2	0.1	0.2	0.1	0.1	0.1	0.2
Austria	0.1	-0.1	0.1	0.5	0.6	0.5	0.3	0.2	0.2	0.3
Other EU										
UK	1.0	-0.3	0.1	0.2	0.3	0.3	0.4	0.3	0.5	0.5
Sweden	0.3	0	0.3	0.5	0.6	0.6	0.6	0.6	0.6	0.7
Poland (% yoy)	1.4	1.1	0.4	1.3	2.0	2.9	2.9	2.2	2.2	2.0
Czech Rep.	-0.3	-0.2	0	0.5	0.6	0.6	0.5	0.6	0.5	0.6
Hungary	-0.4	-0.9	0	0.2	0.4	0.3	0.1	0.1	0.1	0.2
Others										
US (annualized)	3.1	0.4	3.0	1.8	2.8	2.8	2.7	2.6	2.5	2.5
Switzerland	0.6	0.2	0.3	0.4	0.5	0.5	0.4	0.4	0.4	0.4
Russia	0.4	1.2	0.8	0.8	0.9	1.1	0.9	0.8	1.0	1.1
Turkey	0.2	0.7	0.9	0.9	0.9	0.9	1.0	1.0	1.0	1.0
China (% yoy)	7.4	7.9	7.7	8.0	7.9	7.5	7.9	7.9	7.7	7.2

CPI INFLATION (% YOY)

	3Q12	4Q12	1Q13	2Q13	3Q13	4Q13	1Q14	2Q14	3Q14	4Q14
Eurozone	2.5	2.3	1.9	1.7	1.7	1.7	1.7	1.7	1.6	1.6
Germany	2.0	2.0	1.5	1.4	1.2	1.2	1.2	1.3	1.4	1.5
France	2.0	1.7	1.1	1.0	1.2	1.5	1.9	2.1	1.9	1.9
Italy	3.2	2.5	1.9	1.3	1.7	1.8	1.7	2.0	1.6	1.6
Spain (HICP)	2.8	3.2	3.1	3.3	2.6	2.9	2.7	2.6	2.5	2.3
Austria	2.3	2.8	2.5	2.3	2.1	1.7	2.0	2.1	2.0	1.7
Other EU										
UK	2.4	2.7	2.8	2.9	2.8	2.4	2.3	2.3	2.4	2.3
Sweden	0.6	0.1	0	0.1	0.4	0.9	1.3	1.6	2.0	2.2
Poland	3.9	2.9	1.4	0.9	1.3	1.6	2.5	2.3	2.3	2.5
Czech Rep.	3.4	2.9	1.8	1.7	1.8	1.6	1.5	1.7	1.7	1.8
Hungary	6.6	5.0	3.0	2.7	2.8	2.7	3.0	3.0	4.5	4.3
Others										
US	1.7	1.9	1.7	1.9	2.0	2.0	2.3	2.4	2.5	2.6
Switzerland	-0.5	-0.3	-0.4	-0.3	-0.2	0.2	0.6	0.7	0.8	0.7
Russia	5.2	5.0	5.6	6.4	6.6	6.4	6.0	5.5	5.2	5.1
Turkey	9.0	6.8	7.1	6.8	6.6	6.5	6.0	6.3	6.4	6.4
China	1.9	2.5	2.4	2.6	2.9	3.2	3.2	3.2	3.4	3.5

Source: UniCredit Research

Table 3: Comparison of annual GDP and CPI forecasts

GDP (%)

	UniCredit			IMF (Apr-13)			European Commission (Feb-13)			OECD (Nov-12)		
	2012	2013	2014	2012	2013	2014	2012	2013	2014	2012	2013	2014
Eurozone	-0.5	-0.1	1.2	-0.6	-0.3	1.1	-0.6	-0.3	1.4	-0.4	-0.1	1.3
Germany	0.9	0.8	1.5	0.9	0.6	1.5	0.7	0.5	2.0	0.9	0.6	1.9
France	0	0.5	1.3	0	-0.1	0.9	0	0.1	1.2	0.2	0.3	1.3
Italy	-2.4	-1.1	0.7	-2.4	-1.5	0.5	-2.2	-1.0	0.8	-2.2	-1.0	0.6
Spain	-1.4	-1.4	0.4	-1.4	-1.6	0.7	-1.4	-1.4	0.8	-1.3	-1.4	0.5
Austria	0.8	0.9	1.5	0.8	0.8	1.6	0.7	0.7	1.9	0.6	0.8	1.8
Greece	-6.5	-4.5	0.2	-6.4	-4.2	0.6	-6.4	-4.4	0.6	-6.3	-4.5	-1.3
Portugal	-3.2	-2.5	0.4	-3.2	-2.3	0.6	-3.2	-1.9	0.8	-3.1	-1.8	0.9
Other EU												
UK	0.3	0.9	1.4	0.2	0.7	1.5	0	0.9	1.9	-0.1	0.9	1.6
Sweden	1.2	1.4	2.4	1.2	1.0	2.2	1.0	1.3	2.7	1.2	1.9	3.0
Poland	2.0	1.7	2.3	2.0	1.3	2.2	2.0	1.2	2.2	2.5	1.6	2.5
Czech Rep.	-1.2	0.4	2.2	-1.2	0.3	1.6	-1.1	0	1.9	-0.9	0.8	2.4
Hungary	-1.7	-0.1	0.9	-1.7	0	1.2	-1.7	-0.1	1.3	-1.6	-0.1	1.2
Others												
US	2.2	2.2	2.6	2.2	1.9	3.0	2.2	1.9	2.6	2.2	2.0	2.8
Switzerland	1.0	1.4	1.8	1.0	1.3	1.8	1.0	1.4	1.9	0.8	1.1	2.3
Russia	3.4	3.6	3.9	3.4	3.4	3.8	3.4	3.7	3.9	3.4	3.8	4.1
Turkey	2.7	3.4	3.9	2.6	3.4	3.7	2.5	3.0	3.8	2.9	4.1	5.2
China	7.8	7.8	7.7	7.8	8.0	8.2	7.8	8.0	8.1	7.5	8.5	8.9

CPI INFLATION (%)*

	UniCredit			IMF (Apr-13)			European Commission (Feb-13)			OECD (Nov-12)		
	2012	2013	2014	2012	2013	2014	2012	2013	2014	2012	2013	2014
Eurozone	2.5	1.8	1.7	2.5	1.7	1.5	2.5	1.8	1.5	2.4	1.6	1.2
Germany	2.0	1.3	1.4	2.1	1.6	1.7	2.1	1.8	1.7	2.1	1.9	2.0
France	2.0	1.2	2.0	2.0	1.6	1.5	2.2	1.6	1.5	2.2	1.3	1.2
Italy	3.0	1.7	1.7	3.3	2.0	1.4	3.3	2.0	1.7	3.2	1.9	0.9
Spain	2.4	2.9	2.7	2.4	1.9	1.5	2.4	1.7	1.0	2.2	1.2	0.4
Austria	2.4	2.2	1.9	2.6	2.2	1.9	2.6	2.2	1.9	2.4	1.9	1.6
Greece	1.5	0.4	0.7	1.0	-0.8	-0.4	1.0	-0.8	-0.4	1.0	-0.2	-0.8
Portugal	2.8	1.4	1.7	2.8	0.7	1.0	2.8	0.6	1.2	2.7	0.8	1.0
Other EU												
UK	2.8	2.7	2.3	2.8	2.7	2.5	2.8	2.6	2.3	2.6	1.9	1.8
Sweden	0.9	0.4	1.8	0.9	0.3	2.3	0.9	1.1	1.6	1.0	0.9	1.7
Poland	3.7	1.4	2.4	3.7	1.9	2.0	3.7	1.8	2.3	3.6	2.1	2.1
Czech Rep.	3.3	1.7	1.7	3.3	2.3	1.9	3.5	2.1	1.6	3.2	2.0	2.1
Hungary	5.6	3.0	4.1	5.7	3.2	3.5	5.7	3.6	3.3	5.8	4.8	3.9
Others												
US	2.1	1.9	2.5	2.1	1.8	1.7	2.1	1.8	2.2	2.1	1.8	2.0
Switzerland	-0.7	-0.1	0.7	-0.7	-0.2	0.2	-	-	-	-0.6	0.1	0.2
Russia	5.1	6.3	5.1	5.1	6.9	6.2	7.7	7.4	7.4	5.0	6.4	4.3
Turkey	8.9	6.7	6.3	8.9	6.6	5.3	8.0	7.7	5.6	9.1	6.9	6.1
China	2.7	2.8	3.3	2.6	3.0	3.0	-	-	-	2.6	1.5	1.4

*UniCredit forecasts refer to CPI with the exception of Spain, where HICP is used. IMF and OECD inflation forecasts refer to the CPI except for eurozone countries, where HICP is used. EC inflation forecasts refer to the HICP, except for the US and Russia, where CPI is used. Please note that in the UK, CPI and HICP coincide.

Source: IMF, European Commission, OECD, UniCredit Research

Table 4: Global G10 FI/FX forecasts

EU	Current	Jun-13	Sep-13	Dec-13	Mar-14	Jun-14	Sep-14	Dec-14
Key rate	0.75	0.75	0.75	0.75	0.75	0.75	0.75	1.00
3M	0.21	0.45	0.55	0.65	0.75	0.85	0.95	1.10
2Y	0.01	0.25	0.40	0.55	0.75	1.00	1.25	1.50
5Y	0.31	0.85	1.00	1.20	1.38	1.60	1.88	2.10
10Y	1.24	1.75	1.90	2.05	2.20	2.40	2.60	2.80
30Y	2.17	2.60	2.75	2.85	2.95	3.10	3.25	3.40
2/10	123	150	150	150	145	140	135	130
2/5/10	-32	-15	-15	-10	-10	-10	-5	-5
10/30	93	85	85	80	75	70	65	60
2Y SwSp	-41	-35	-35	-35	-30	-30	-25	-25
10Y SwSp	-33	-30	-30	-30	-25	-25	-25	-25
10Y BTP/bund	311	295	275	260	245	230	215	200
US								
Key rate	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25
3M	0.28	0.35	0.35	0.35	0.35	0.35	0.35	0.35
2Y	0.22	0.35	0.45	0.55	0.65	0.80	1.20	1.60
5Y	0.69	1.05	1.18	1.38	1.53	1.70	2.10	2.45
10Y	1.71	1.95	2.10	2.30	2.50	2.70	3.00	3.30
30Y	2.89	3.05	3.15	3.30	3.45	3.60	3.85	4.10
2/10	148	160	165	175	185	190	180	170
2/5/10	-27	-10	-10	-5	-5	-5	0	0
10/30	118	110	105	100	95	90	85	80
2Y SwSp	-15	-10	-10	-10	-5	-5	-5	-5
10Y SwSp	-17	-10	-10	-5	0	0	0	0
UK								
Key rate	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.75
10Y	1.70	2.10	2.20	2.35	2.50	2.70	2.90	3.10
SZ								
Key rate	0	0	0	0	0	0	0	0
10Y	0.63	0.75	0.90	1.05	1.20	1.40	1.60	1.80

	Current	Jun-13	Sep-13	Dec-13	Mar-14	Jun-14	Sep-14	Dec-14
EUR-USD	1.31	1.36	1.38	1.40	1.40	1.41	1.42	1.43
EUR-JPY	127	135	139	144	144	147	148	150
EUR-GBP	0.85	0.90	0.91	0.93	0.93	0.94	0.95	0.95
EUR-SEK	8.37	8.80	8.85	8.95	8.95	9.00	9.00	9.00
EUR-NOK	7.51	7.50	7.53	7.55	7.57	7.60	7.63	7.65
EUR-CHF	1.22	1.26	1.27	1.28	1.28	1.29	1.30	1.30
EUR-AUD	1.26	1.26	1.27	1.27	1.27	1.26	1.26	1.24
EUR-NZD	1.54	1.56	1.57	1.56	1.54	1.53	1.53	1.51
EUR-CAD	1.34	1.43	1.45	1.46	1.43	1.41	1.39	1.39
USD-JPY	98	99	101	103	103	104	104	105
GBP-USD	1.53	1.51	1.51	1.50	1.50	1.50	1.50	1.50
USD-SEK	6.41	6.47	6.41	6.39	6.39	6.38	6.34	6.29
USD-NOK	5.75	5.51	5.46	5.39	5.41	5.39	5.37	5.35
USD-CHF	0.93	0.93	0.92	0.91	0.91	0.91	0.92	0.91
AUD-USD	1.04	1.08	1.09	1.10	1.10	1.12	1.13	1.15
NZD-USD	0.85	0.87	0.88	0.90	0.91	0.92	0.93	0.95
USD-CAD	1.02	1.05	1.05	1.04	1.02	1.00	0.98	0.97

Source: Bloomberg, UniCredit Research

Eurozone

Marco Valli,
Chief Eurozone Economist
(UniCredit Bank Milan)
+39 02 8862-8688
marco.valli@unicredit.eu

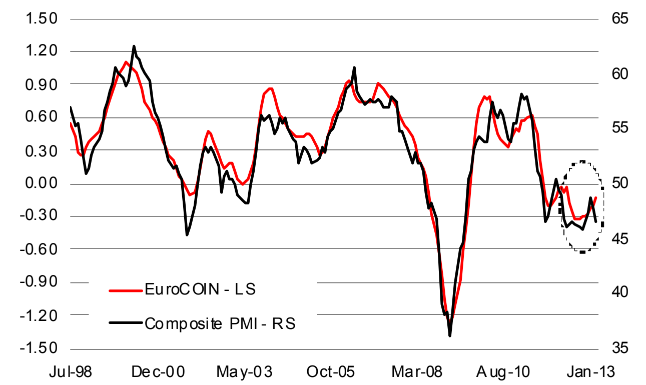
- The March round of survey indicators was soft. PMIs were a real disappointment: the composite index deteriorated for the second consecutive month and fell to 46.5 vs. 47.9, only slightly above the cyclical low hit towards the end of 2012. On balance, national business surveys were only slightly weaker than expected – the German Ifo was down somewhat after the previous strong gains, the French INSEE was stable, and the Italian ISTAT indicator rose marginally. On a positive note, the EuroCOIN recorded the largest monthly increase since the beginning of its upward trend last summer. At the current level, the Composite PMI signals a GDP contraction of 0.3% qoq (with momentum pointing south), while the EuroCOIN is consistent with -0.1% qoq (and momentum pointing north). Overall, risks to our GDP forecasts seem skewed to the downside, but more evidence is needed to assess the underlying trend of the eurozone economy.

- Hard data up to February have come in broadly as expected, and show tentative signs of stabilization in economic activity. For January-February, IP is 0.2% below the 4Q12 average. This follows a large 2.1% qoq contraction at end-2012. The performance of retail trade has also improved, and in the first two months of the year sales are slightly up vs. 4Q12, when they dropped 1.5% qoq. We stick to our view that GDP will post zero growth in 1Q13, although risks are tilted to the downside.

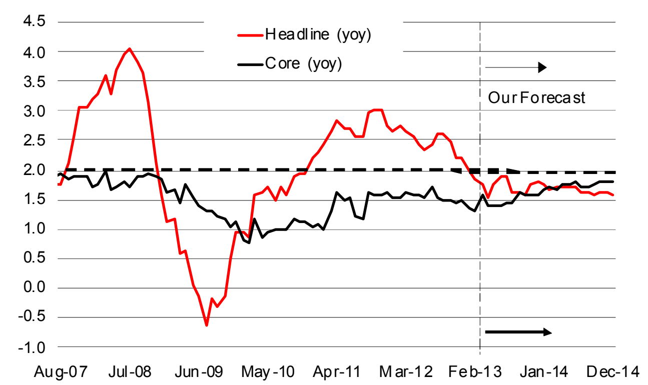
- In March, CPI slowed to 1.7% yoy vs. 1.8%. Energy subtracted 0.2pp from the overall rate, while core inflation re-accelerated by 0.2pp to 1.5%. This is probably due to Easter falling early, which temporarily pushed up the price of holiday-sensitive items. We expect most of this Easter-related effect to be reversed in April, when inflation is likely to continue to slow (in the 1.5% area), also helped by a further deceleration in energy inflation, which seems set to approach zero. In our projections, April marks the low point in the inflation path. In yearly average terms, we see inflation at 1.8% this year and at 1.7% in 2014.

- The latest weak data have made the ECB more cautious. The central bank still sees a gradual recovery starting in 2H13, but confidence in the baseline scenario has weakened. The more dovish tone was reflected in a seemingly bigger split in the Governing Council about a rate cut. While in March the decision to keep rates on hold was taken by "prevailing consensus", on 4 April the discussion was "extensive", indicating that the rate-cut camp had gained new members. For the time being, we maintain our forecast for a steady refi rate. However, another round of disappointing soft data could be enough to trigger a 25bp cut in May. Alternatively, any lack of improvement from current levels in the next couple of months would probably be consistent with a 25bp cut at the June meeting.

MIXED EVIDENCE IN MARCH



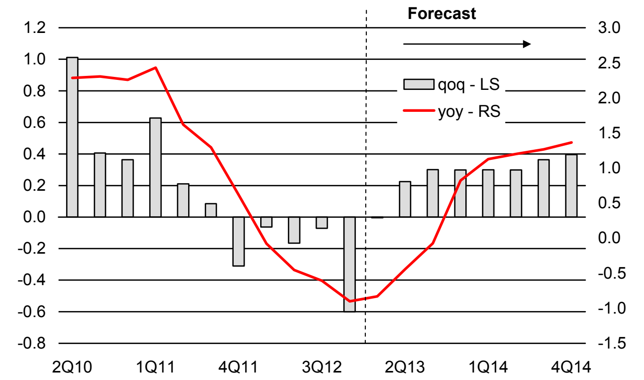
INFLATION KEEPS SLOWING



Source: Eurostat, Markit, UniCredit Research

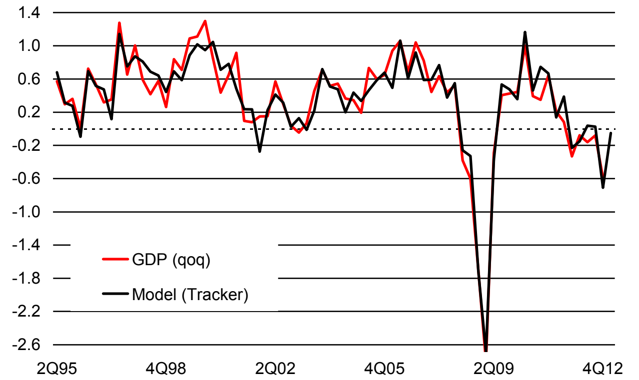
Eurozone

GDP



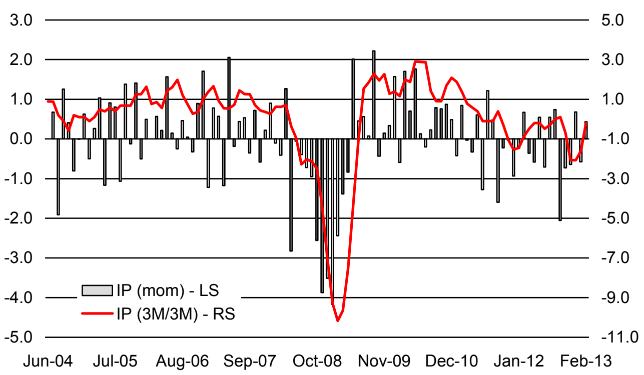
- We see some downside risks to our GDP forecasts.

GDP TRACKER



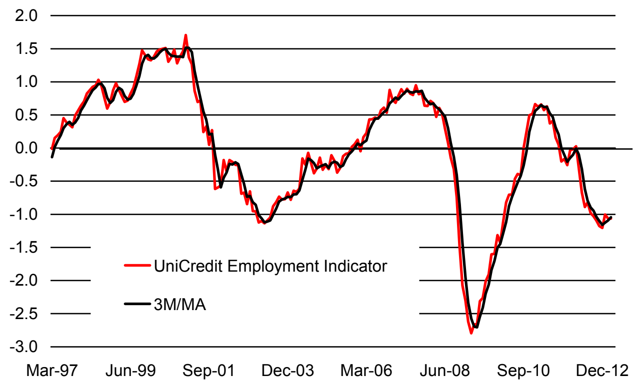
- The eurozone may have avoided a contraction in 1Q13.

INDUSTRIAL PRODUCTION



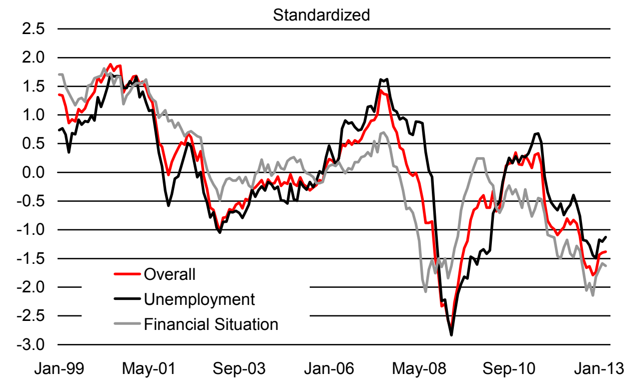
- Industrial activity: signs of stabilization confirmed.

EMPLOYMENT



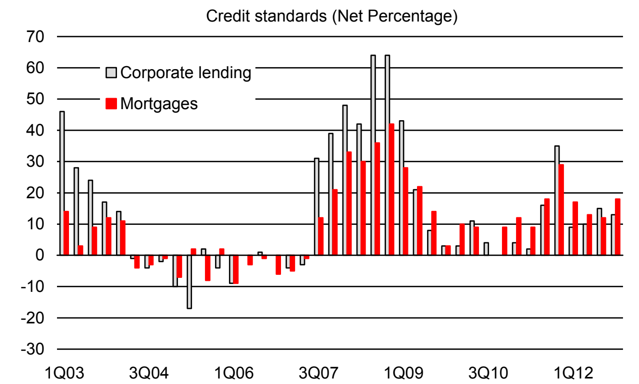
- Employment indicator shows signs of bottoming out, no recovery.

CONSUMER CONFIDENCE



- Modest recovery.

BANK LENDING SURVEY



- Credit conditions remain tight.

Source: Bloomberg, EC, ECB, Eurostat, Markit, UniCredit Research

Germany

Alexander Koch, CFA
(UniCredit Bank)
+49 89 378-13013
alexander.koch1@unicreditgroup.de

Dr. Andreas Rees,
Chief German Economist
(UniCredit Bank)
+49 89 378-12576
andreas.rees@unicreditgroup.de

- The recent releases of hard data in the industrial sector showed the first signs of a turnaround, thereby confirming overall optimistic business sentiment surveys in the last few months.

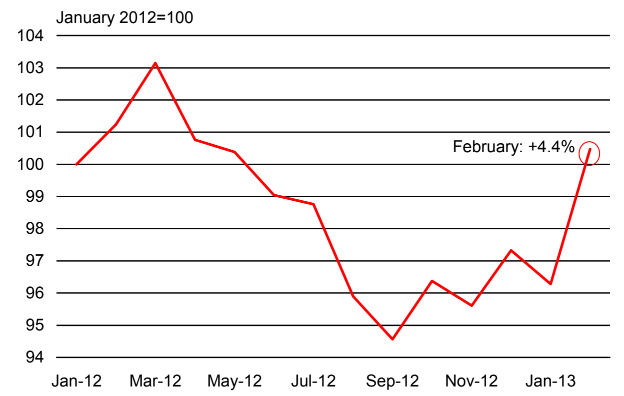
- Especially encouraging was the strong rise in new orders in February (+2.3% mom) and its balanced composition. Both domestic and foreign demand rose to nearly the similar extent, thereby putting the German economy on a solid footing. Domestic new orders of capital goods even jumped 4.4% mom (see left chart below), thereby signaling companies' increasing willingness to expand their capex again. The latest figure confirms our view that substantial pent-up demand in machinery and equipment building up last year due to the eurozone crisis will now start unloading.

- Positive signals also came from retail sales in January-February on average (plus 1.7% compared to 4Q12). Although retail sales are usually prone to heavy ex-post revisions and tend to be volatile, private consumer expenditures should have contributed markedly to overall GDP growth in 1Q13. Key drivers of robust private consumption are the strong labor market and rising wages. From November 2012 to February (latest available data), employment rose by about 30,000 per month on average (see right chart below). Although this does not match the pace of job creation in 2011 (plus 47,000 per month), the reacceleration on the labor market bodes well for purchasing power. The same message can be derived by looking at recent collective bargaining rounds in the construction and public sector. In the latter, for instance, the wage rise will be 2.6% for 2013 and 2.9% for 2014.

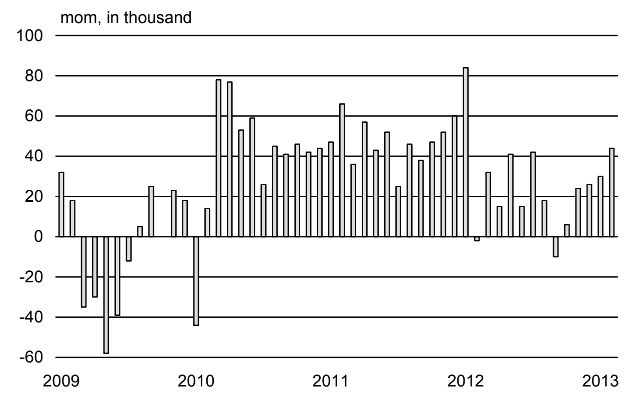
- Based on our GDP tracker, the so far available hard data indicate a rise in real GDP by 0.2% to 0.3% qoq in 1Q13. We therefore stick to our forecast of plus 0.3% (release of official GDP figure on 15 May).

- In March, the forward-looking Ifo business expectations component declined for the first time after six consecutive rises on a monthly basis. The payback does not necessarily herald a turnaround in the business cycle. Special circumstances like the Italian election outcome and the turbulence in Cyprus may have put a dampener on companies' mood as well. However, business expectations should be closely watched in the next two months.

DOMESTIC CAPITAL GOODS ORDERS REBOUNDING STRONGLY



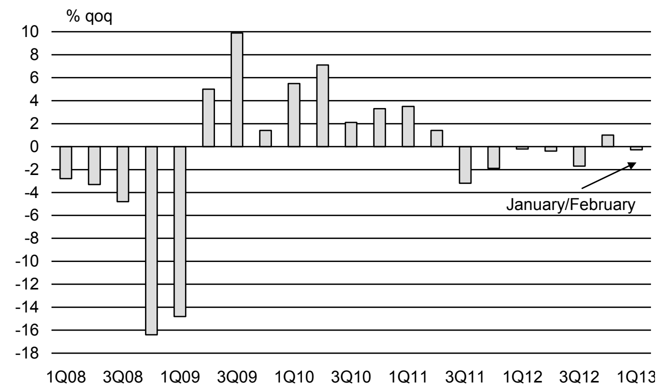
GERMAN EMPLOYMENT RISING SIGNIFICANTLY AGAIN



Source: Feri, UniCredit Research

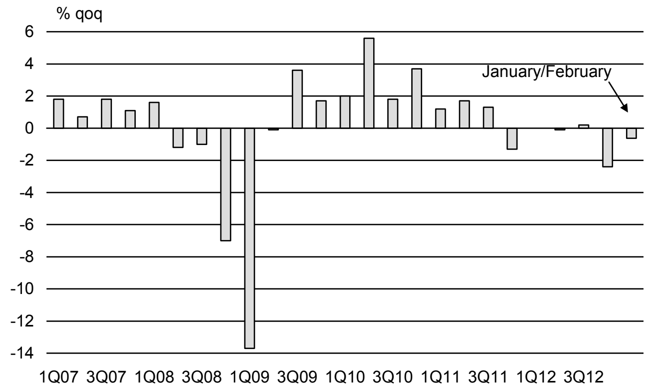
Germany

NEW ORDERS



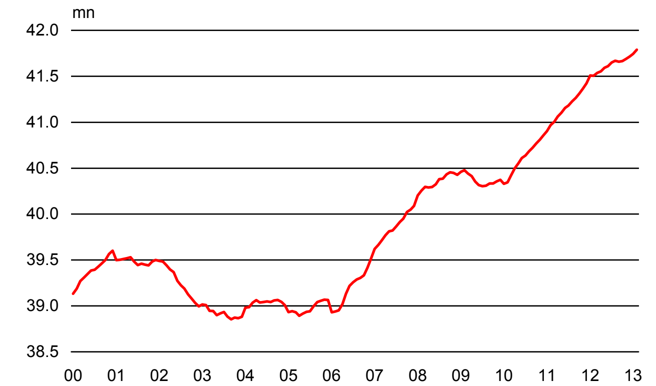
- Despite the strong rise in February, new orders in January and February combined were slightly down compared to 4Q12.

PRODUCTION



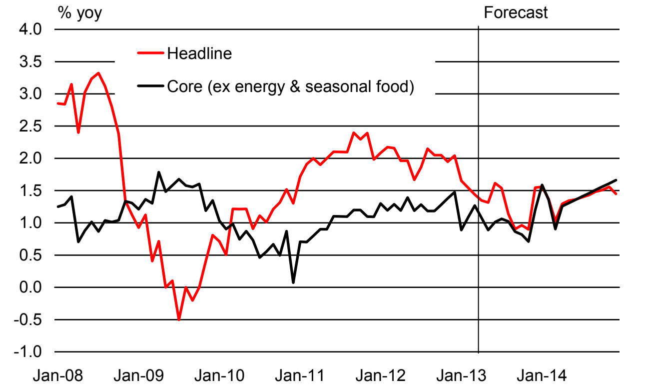
- Manufacturing production in January-February fell moderately compared to 4Q12.

EMPLOYMENT



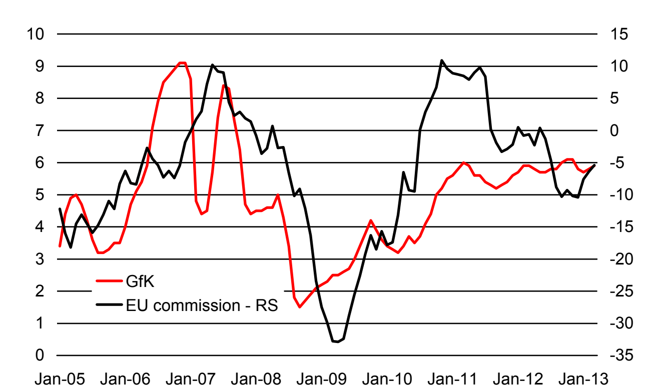
- Job creation accelerated again in recent months.

INFLATION



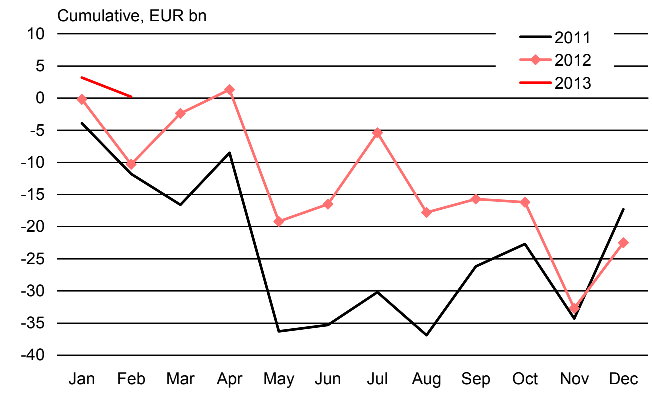
- The annual headline rate fell to 1.4% yoy and hence to its lowest level since December 2010.

CONSUMER CONFIDENCE



- Overall, consumer confidence recently increased slightly again, thanks to the labor market and wage agreements.

FEDERAL BUDGET BALANCE



- The federal budget balance showed an improvement at the start of 2013 thanks to further rising tax revenues.

Source: Bundesbank, GfK, EU Commission, FSO, Ministry of Finance, UniCredit Research

France

Tullia Bucco,
Economist
(UniCredit Bank Milan)
+39 02 8862-2079
tullia.bucco@unicredit.eu

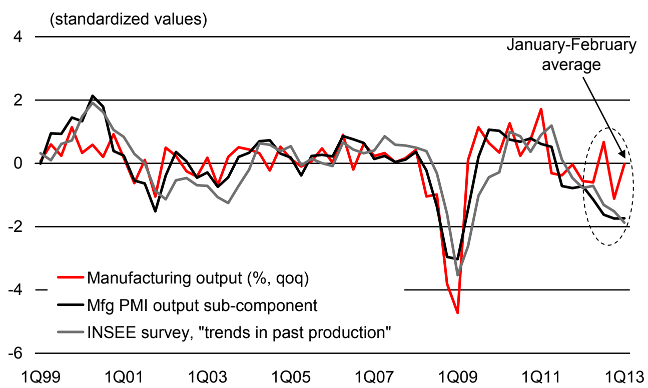
- Hard and soft data so far available indicate a material risk that France failed to emerge from recession in the first quarter. Industrial output showed a broad stabilization up to February, although sectoral survey data remain weak and do not yet point to a convincing recovery in output. Most importantly, surveys portray a very subdued picture for the services sector, also relative to other eurozone countries – in March, the services PMI fell to the lowest level since February 2009, although this possibly overestimates the pace of contraction in sectoral output. Overall, we think that the main drag on economic activity is the tighter fiscal stance and deteriorating labor market, which are weighing on private consumption as well as residential investment. Construction data point to a clear deepening in the pace of sectoral recession, with the January-February average down by more than 3.0% compared to 4Q12. At present, we see clear downside risks to our forecast for a modest recovery in economic activity already in the first quarter of the year.

- According to estimates by the INSEE, the general government deficit settled at 4.8% in 2012, marginally above the 4.5% reading previously announced by the government. The 4.8% reading includes, among other things, the cost of Dexia's recapitalization (EUR 2.6bn) and a EUR 6.5bn contribution to the capital of the ESM. General government debt rose from 85.8% to 90.2% in 2012.

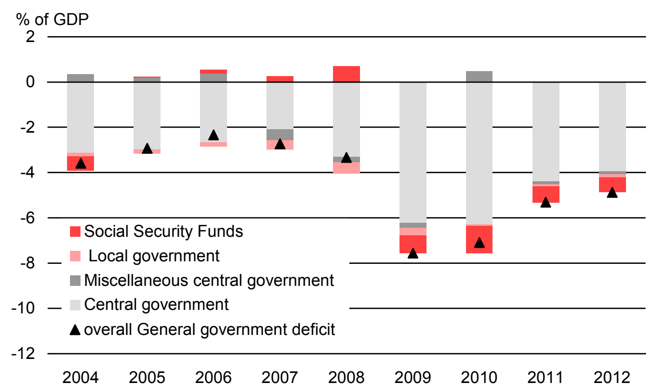
- The government is in the process of finalizing the multi-annual budgetary plan up to 2017. This currently involves negotiations with the European Commission to obtain a one-year delay to the achievement of a 3.0% deficit target, in order to allow automatic stabilizers to cushion the slowdown in economic activity. Finance Minister Moscovici recently aligned government forecasts with the European Commission, acknowledging that the 2013 deficit will most likely be closer to 3.7% than 3.0% due to lower-than-expected GDP growth (now seen at 0.1% vs. 0.8% previously envisaged). This implies that the government will have to come up with additional austerity measures to meet the 3% target by 2014. These measures will most likely consist of stronger spending cuts, given that the tax burden rose to nearly 50% last year.

- On the policy front, it is worth highlighting that the National Assembly recently adopted the law transposing the January agreement between social parties on labor market reform. The agreement consisted of several measures intended to facilitate labor market adjustment to a cyclical downturn. No major amendments were made to the draft law, but few Socialists and the Green party abstained from voting. The bill was then passed on to the Senate, with the objective of becoming law by mid-May.

MANUFACTURING OUTPUT FARED BETTER THAN EXPECTED



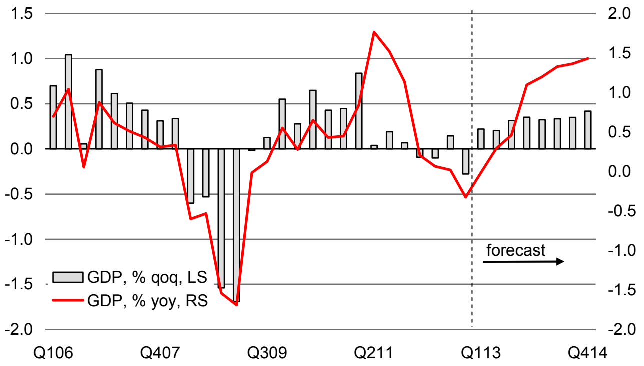
SOCIAL SECURITY CONTINUED TO WEIGH ON TOTAL DEFICIT



Source: INSEE, Markit, UniCredit Research

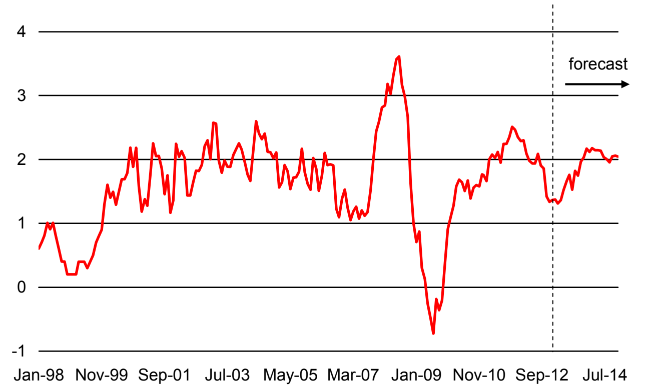
France

GDP



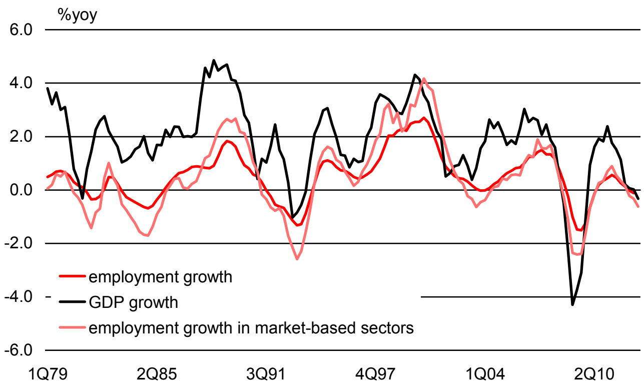
■ We currently see downside risks to our forecast for modest recovery in economic activity already in 1Q13.

INFLATION



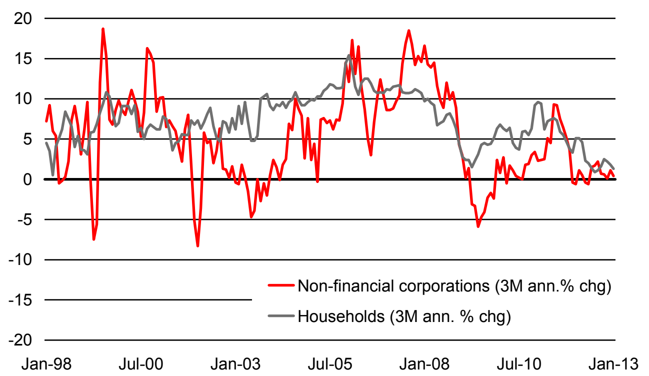
■ CPI edged down 0.1pp to 1.0% in March. We currently estimate inflation averaging 1.2% in 2013.

EMPLOYMENT



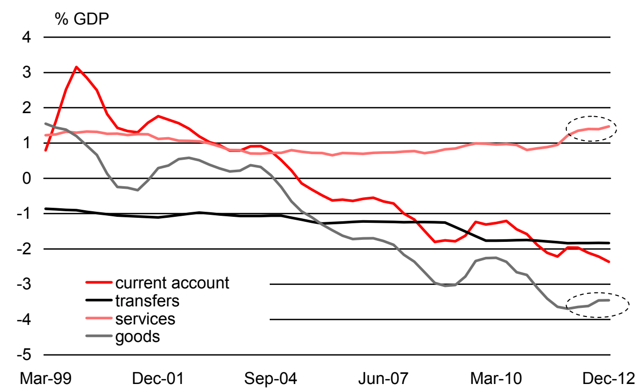
■ Employment continues to contract. At the end of last year, private-sector employment shrank by 0.3% qoq.

LENDING TO THE PRIVATE SECTOR



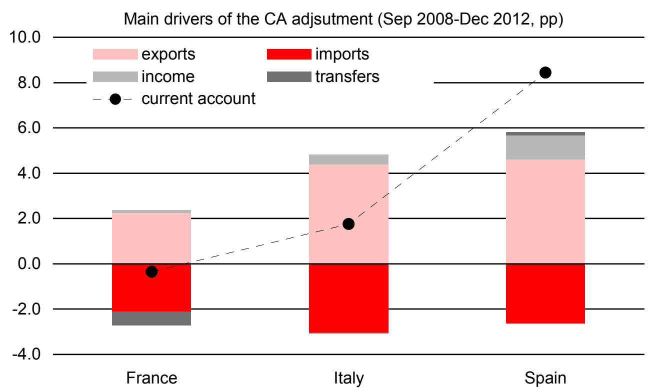
■ Lending growth to the private sector remains subdued but marginally positive.

CURRENT ACCOUNT



■ The C/A settled at 2.4% of GDP in 2012.

CURRENT ACCOUNT – MAIN DRIVERS



■ Exports nearly totally offset the drop in imports and transfers.

Source: INSEE, Markit, Banque de France, UniCredit Research

Italy

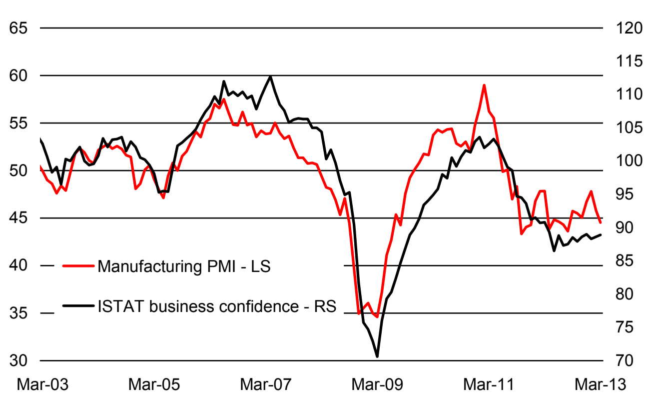
Loredana Federico, Economist (UniCredit Bank Milan)
+39 02 8862-3180
loredana.federico@unicredit.eu

- Business surveys were disappointing in March. The ISTAT business confidence indicator showed only a marginal improvement, returning to last December's level. The manufacturing PMI declined further in March, to 44.5 from 45.8, with domestic demand being a strong drag on performance, as indicated by the very large gap between the export orders index (down to 50.5 from 51.5, but still in expansionary territory), and the overall orders index (41.1 vs. 42.8). On face value, business surveys continue to suggest underlying weakness in industrial activity and point to a contraction in industrial output in March (and, probably, for the beginning of 2Q). Bad news also came from the service PMI – the 1Q average is 44.3, down from 45.4 in 4Q12 – which remains consistent with further weakness in service activity in the quarter.

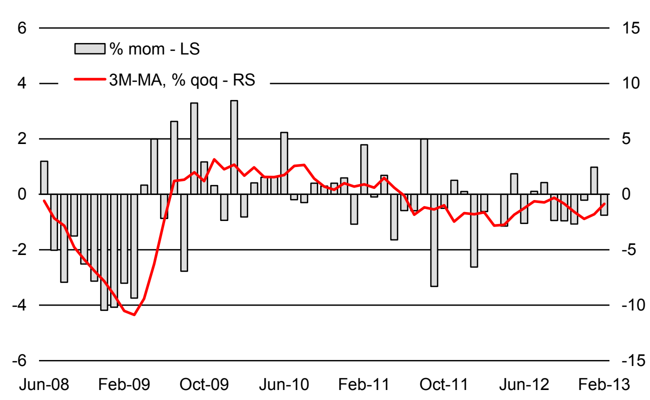
- Industrial production in January-February showed a broad stabilization with respect to the 4Q12 average, mainly thanks to the solid increase in January. Still, other hard data such as car registrations, recorded another sizeable contraction in 1Q (-7.0% qoq vs. -4.1% in 4Q12). Overall, soft and hard data available so far confirm some downside risks to our projection of a -0.2% GDP reading in 1Q. Looking ahead, given the delay of soft indicators in resuming a clear upward trend, risks to our GDP forecast for 2Q13 (envisaging a marginal positive growth) and for the year as a whole are skewed to the downside. Still, conditions for a modest economic recovery in 2H13 seem to remain in place, also thanks to the recently adopted decree law to inject liquidity in the economy by unblocking payment arrears to companies.[1]

- Mario Monti's caretaker government approved the stability program contained in the 2013 Economic and Financial Document, highlighting that public finances are on a sustainable path and that the fiscal consolidation was pursued powerfully to achieve a balanced budget in structural terms in 2013. The new government growth and fiscal projections already embody the impact of the decree on the payment of arrears. In particular, the GDP projection for 2013 was revised down to -1.3% (vs. the previous -0.2%), while the 2014 forecast was revised up slightly to +1.3% (vs. +1.1%). The fiscal deficit targets were increased to 2.9% (vs. 1.8%) in 2013 and to 1.8% (vs. 1.5%) in 2014, with a 0.5pp impact in 2013 coming from the payment of arrears. The primary surplus is expected to reach 3.8% in 2014 from 2.4% in 2013, while the debt/GDP ratio is projected to rise from 127.0% in 2012 to 130.4% in 2013 and to subsequently start declining in 2014 (to 129.0%).

BUSINESS SURVEYS: DISAPPOINTING IN MARCH



IP RECESSION IS LIKELY TO HAVE EASED IN 1Q

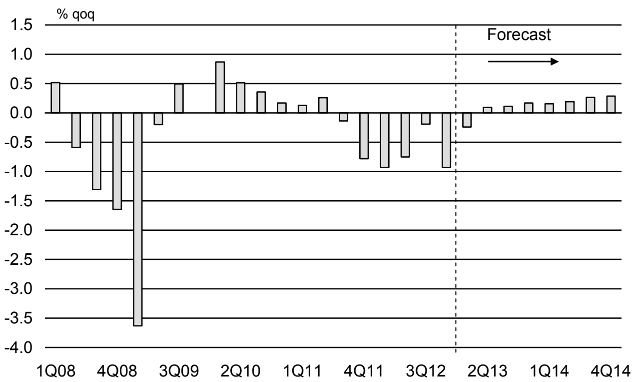


Source: ISTAT, Markit, UniCredit Research

[1] For more on this, please refer to "Italy set to repay EUR 40bn of arrears" – Economic Flash, 9 April.

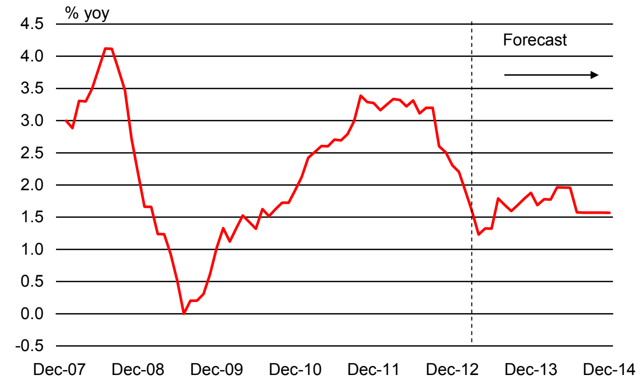
Italy

GDP



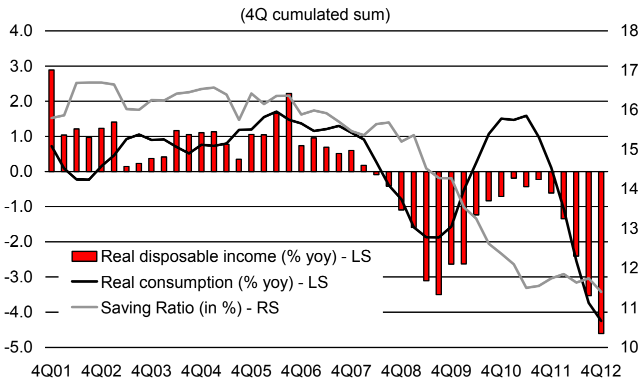
■ We acknowledge some downside risks to our forecast of a 0.2% GDP contraction in 1Q13 and marginal positive growth in 2Q13.

INFLATION



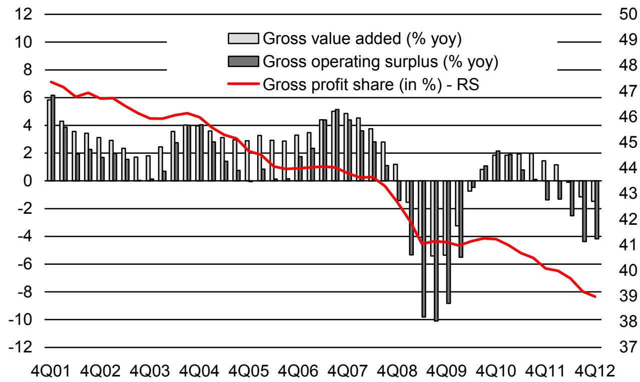
■ Inflation slowed further to 1.6% in March.

HOUSEHOLDS: INCOME AND SAVINGS



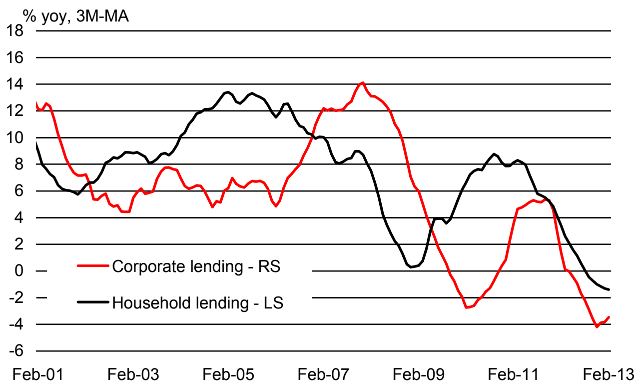
■ The reduction in household consumption went hand in hand with the decline in disposable income.

NFCS: GROSS OPERATING SURPLUS



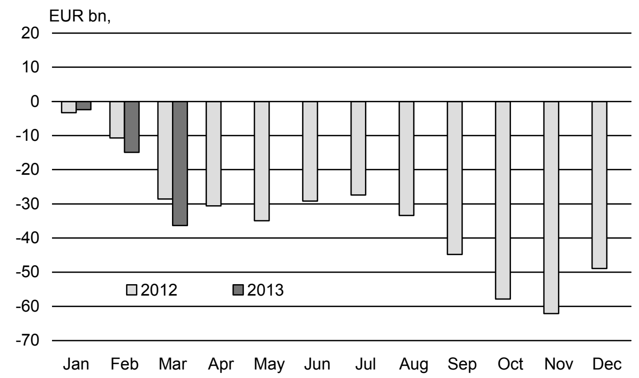
■ Corporate sector internal financing hampered by a sizeable contraction in operating profits.

LENDING TO HOUSEHOLDS AND CORPORATES



■ Household and corporate lending growth remained in negative territory in February.

STATE SECTOR BORROWING REQUIREMENT



■ The state sector borrowing requirement in the first three months of the year was slightly higher than that recorded in the same period of 2012.

Source: ISTAT, Bank of Italy, UniCredit Research

Spain

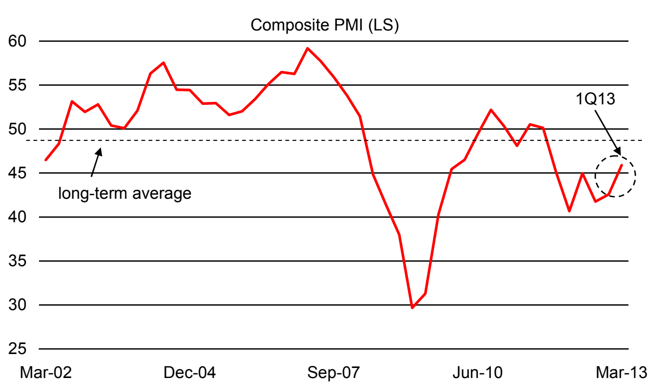
Tullia Bucco, Economist (UniCredit Bank Milan)
+39 02 8862-2079
tullia.bucco@unicredit.eu

- The latest business surveys and hard data suggest that the pace of recession slowed down at the beginning of the year. Admittedly, indications from PMIs need to be taken with a pinch of salt as they have failed to accurately track GDP over the past few quarters and keep hovering at very subdued levels. Still, the 2.6pp increase in the 1Q13 composite PMI (from 42.9 to 45.5) is a positive sign. Concerning hard data, industrial production data up to February suggest that the pace of recession is gradually easing, along with expectations – output up to February was down 1.0% compared to the 4Q12 average, when IP slumped 2.0%. Over the same period, retail sales broadly stabilized following the tumble recorded at the end of last year (-6.8% qoq). Overall, these data appear supportive of our expectation that 4Q12 GDP (-0.8% qoq) most likely represented the low point of the recession, and the pace of recession will ease in 1Q13 (to -0.5% qoq). Our quarterly GDP profile foresees economic activity gradually recovering in the coming months, with GDP possibly returning to positive territory in 2H13.

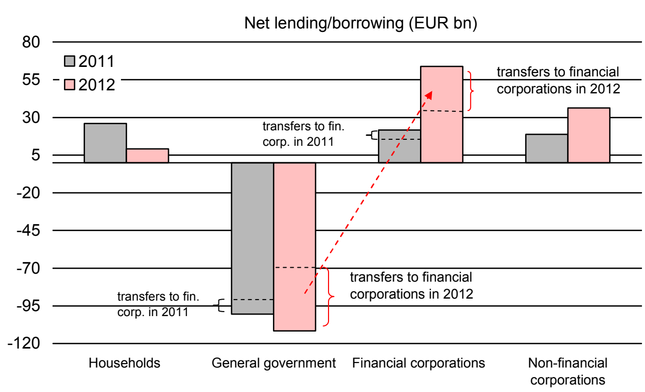
- Eurostat recently asked Spain to raise its 2012 deficit forecast (excluding bank recapitalization costs) from 6.74% to 6.98%, arguing that the government did not correctly account for some tax refunds. The issue concerns EUR 5bn of tax refunds due in 2012, which the government paid out in January 2013. Eurostat will publish its 2012 deficit estimates on 22 April. The impact of the revision to the deficit is small, but rating agencies assessed it negatively. Moody's pointed out that the government's credibility regarding fiscal consolidation is being undermined by frequent revisions to deficits numbers. We recall that the government is planning to submit its multi-year fiscal plan to the EC by the end of the month, including new deficit and GDP forecasts.

- The European Commission recently reiterated that progress with respect to the fulfillment of the reform agenda announced in September 2012 has been slow. The Commission called on the government to step up the effort regarding the creation of an independent fiscal authority, the approval of the long-overdue electricity sector law, the deregulation of professional services and a new pension reform.

PMIS SIGNAL THAT THE WORST MAY BE BEHIND US



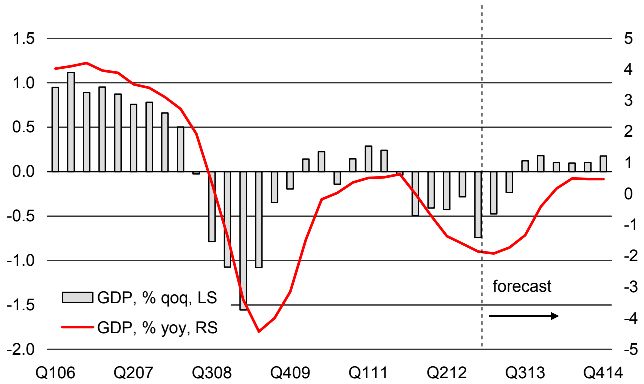
BANK RECAP WEIGHED ON GOVERNMENT NET BORROWING



Source: Markit, Spanish Treasury, UniCredit Research

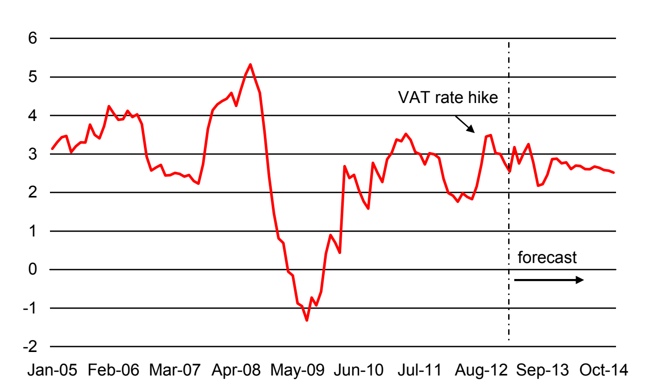
Spain

GDP



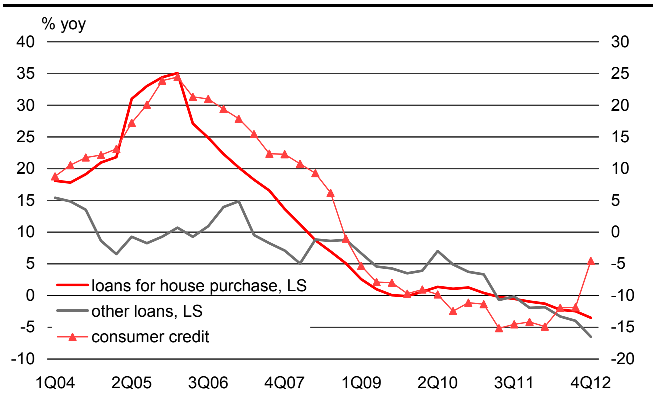
- We expect GDP to resume expanding in 2H13.

INFLATION



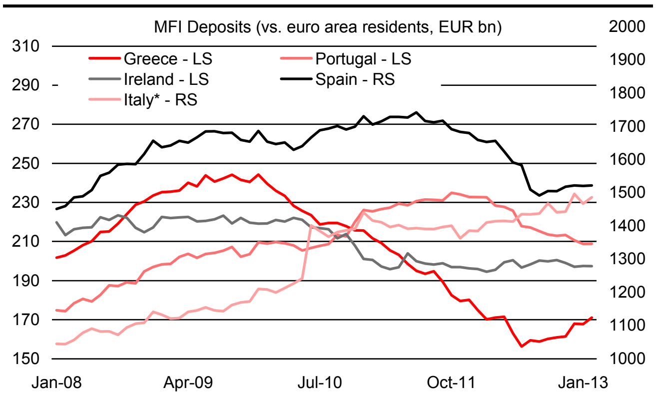
- In March, harmonized inflation edged down by 0.3pp to 2.6%.

HOUSEHOLD CREDIT GROWTH



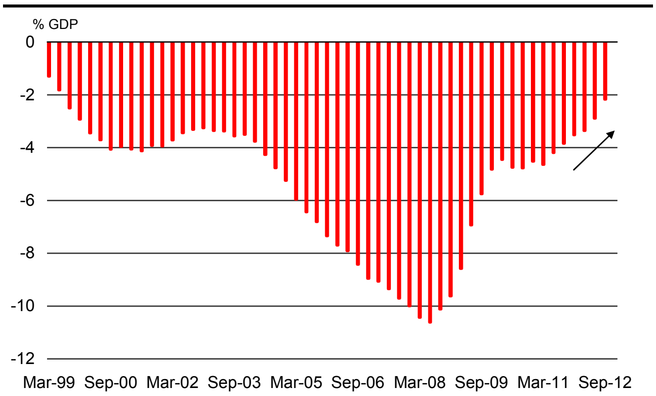
- The contraction in lending to households deepened further in 4Q12, with lending for consumer credit being the only exception.

BANK DEPOSITS



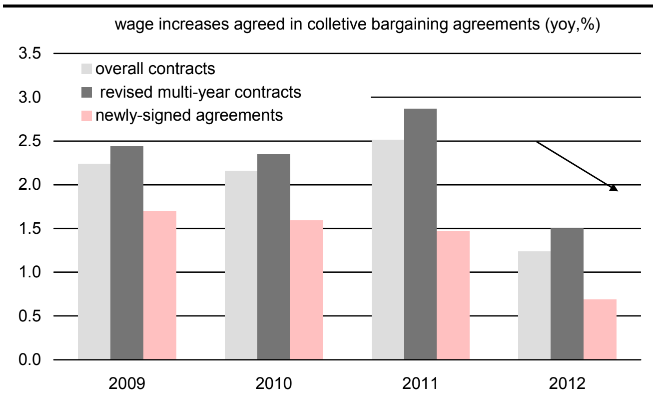
- The decline in deposits came to a halt in August 2012 and we have since been witnessing a moderate increase.

CURRENT ACCOUNT



- The C/A deficit has been shrinking steadily, settling at only 0.8% of GDP by end-2012.

NEGOTIATED WAGES



- Reforms of the collective bargaining framework have started to bear fruit.

Source: Bank of Spain, Eurostat, INE, UniCredit Research

Austria

Stefan Bruckbauer,
Head and Chief Economist Austria
(Bank Austria)
+43 505 05 41951
stefan.bruckbauer@
unicreditgroup.at

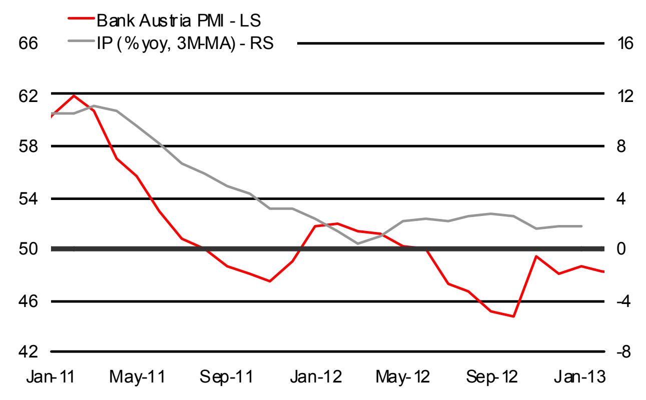
Walter Pudschedl,
Economist
(Bank Austria)
+43 50505 41957
walter.pudschedl@
unicreditgroup.at

- The upswing in Austrian industry will still take some time. The Bank Austria Purchasing Managers' Index fell by 0.2 points to 48.1 in March. It has therefore returned to the level at the end of 2012 and is below the growth threshold of 50 points for the ninth consecutive month. With its slight decline in March and the stagnation since the turn of the year, the Bank Austria Purchasing Managers' Index is currently sending a clear signal that the expected economic recovery has still not kicked into gear. Following the slight decline in GDP in the final quarter of 2012, there are now signs that the Austrian economy has simply stagnated since the beginning of the current year.

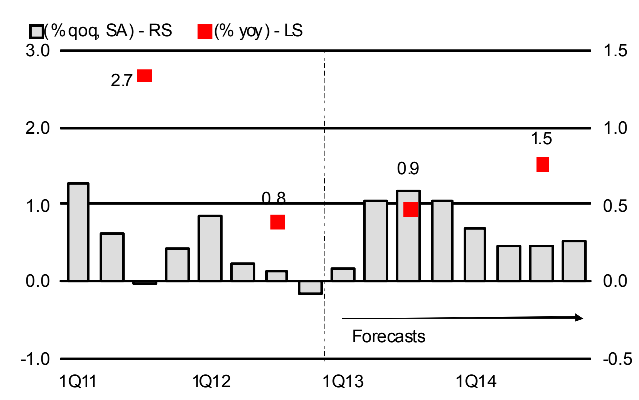
- After the weak first quarter, we expect a noticeable economic upswing in the spring on the back of an industrial recovery and we continue to anticipate 0.9% economic growth for 2013 as a whole because our forecast includes a reasonably weak start to the year. Although risks have slightly increased in recent weeks, it is still too early to give up hope of an upswing in 2013. However, we have lowered our expectations for Austrian industrial growth to an annual average of 1% in 2013, following a revised 1.8% in 2012.

- Austria's budget deficit in 2012 came in better than expected, mainly due to better results of the budgets of the Austrian regional governments. At 2.5% of GDP, the deficit was at the same level as in the previous year. In 2012, the rise in taxes and social insurance led to an increase of 4.4% in government revenues; the cost of the rescue package for Austrian banks was responsible for an increase of 4.4% in public spending compared with 2011. Without these expenditures for banks, Austria's budget deficit would have been much smaller, namely 1.6% of GDP. Public debt in relation to GDP increased from 72.5% in 2011 to 73.4% in 2012, which is also well below the last official estimate of 74.6%. In 2013, Austria's budget deficit is expected to decline slightly to 2.3%, followed by a further decline to 1.7% in 2014, whereas the debt-to-GDP ratio is estimated to rise to 74.1% in 2013 and to fall to 73.7% in the following year. Nevertheless, the new European system of national and regional accounts (ESA 2010) will come into effect in autumn 2014 ex post facto 2013, which will lead to a statistical reclassification. The new rules currently under discussion will tend to result in a stricter, narrower interpretation of market activities of government-owned companies, which may lead to an upward revision of past deficit and debt levels. We estimate the maximum public debt effect of ESA 2010 reclassification in Austria at around 4% of GDP.

STILL ONLY MODERATE INDUSTRIAL GROWTH



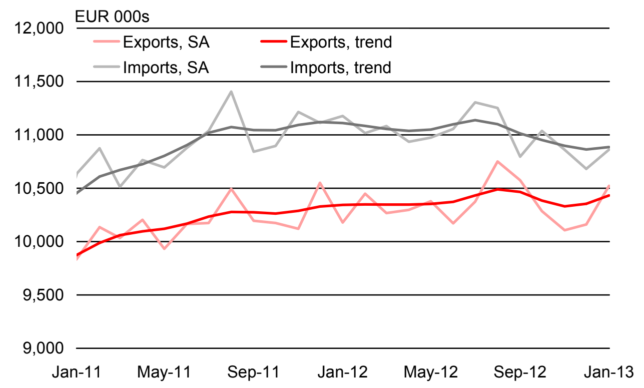
SLUGGISH GDP GROWTH IN 1Q13 EXPECTED AT BEST



Source: Statistik Austria, UniCredit Research

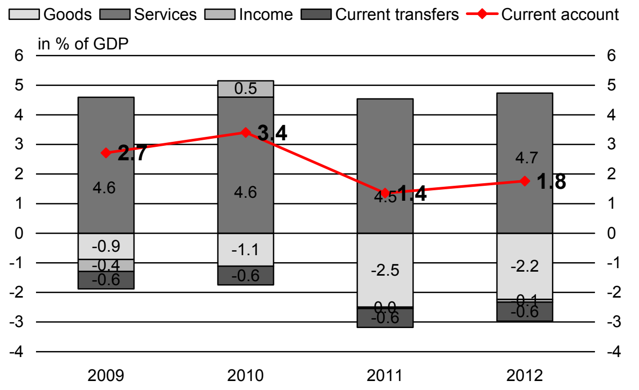
Austria

EXPORTS AND IMPORTS VOLUME



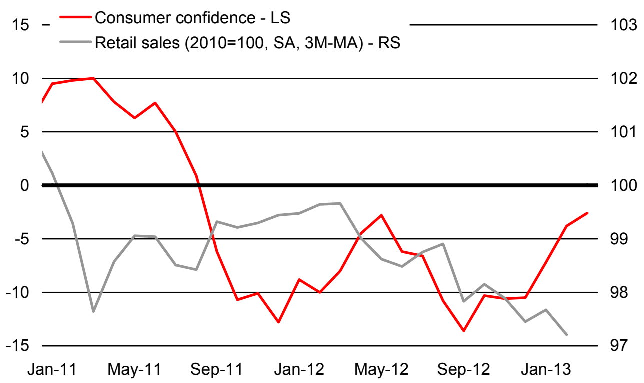
- After a weak development in 4Q12, foreign trade showed some fresh impetus in January, with exports growing by 7% yoy (nsa).

CURRENT ACCOUNT



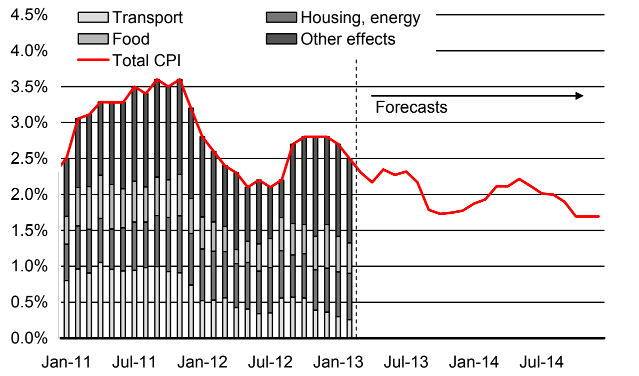
- Current account surplus increased to 1.8% of GDP in 2012 due to a lower trade deficit and a higher services surplus than 2011.

RETAIL TRADE



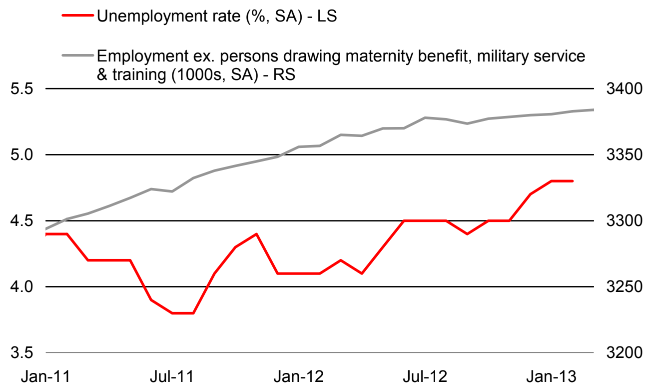
- Consumer confidence improved significantly in 1Q13, raising hopes of a recovery in retail trade.

INFLATION



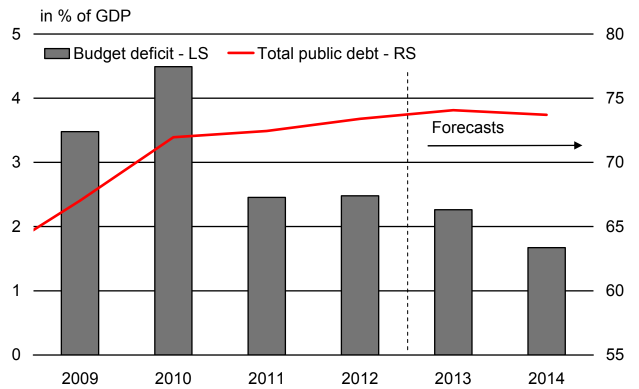
- Oil prices started to dampen inflation in Austria in early 2013. We assume an average decline to 2.2% for 2013.

LABOR MARKET



- Employment stagnated, while unemployment further increased in 1Q13, although the unemployment rate is still the lowest in the EU.

PUBLIC FINANCES



- According to the first official data, both the budget deficit and total public debt in 2012 were lower than expected.

Source: Statistik Austria, UniCredit Research

Greece

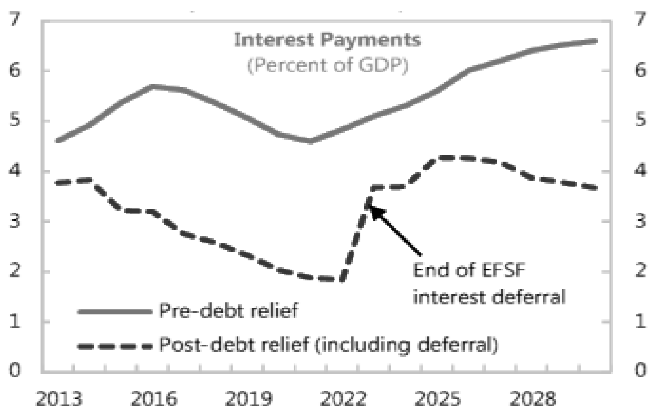
Tullia Bucco, Economist (UniCredit Bank Milan)
+39 02 8862-2079
tullia.bucco@unicredit.eu

- On 3 April, the Troika returned to Athens after a short break in discussions, which had been necessary for the completion of technical work on a few outstanding issues. At the time of writing, parties reached an agreement on a one-year extension of the special real estate levy collected through electricity bills, and on the placement of 15k public workers into the so-called labor mobility scheme over the next two years (4k workers should be transferred this year, and the remaining 11k next year). The Troika accepted Greek demands for oath-breaking civil servants who leave their posts to be replaced with new recruits. Following these agreements, the Greek government should obtain the unlocking of the last EUR 2.8bn installment of the 4Q12 tranche shortly. The disbursement of the EUR 6bn loan tranche (originally scheduled for 1Q13) will probably take place in May provided all agreed fiscal measures for 2013 and 2014 are in place.

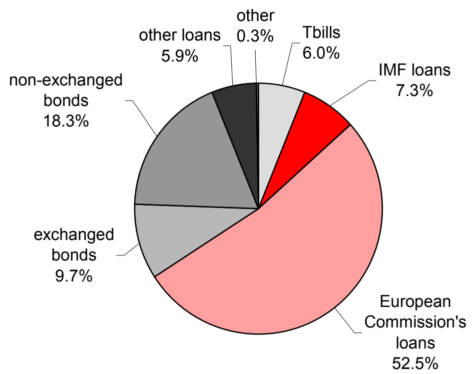
- The central bank of Greece recently suspended the merger of the National Bank of Greece with Eurobank as the two lenders failed to raise sufficient capital from private sources. Admittedly, this was the trickiest issue since the two lenders announced their intention to merge. According to the Bank of Greece's bank recapitalization report released in December, they needed EUR 15.6bn in fresh capital. The central bank's decision reportedly also reflected fears that the merger could concentrate risk by creating a too-big-to-fail lender with assets close to 100% of GDP. On the occasion of the latest mission review (as of January), the Troika also expressed some reservations about the merger's compliance with EU anti-trust laws, given that the new entity would have controlled around 40% of system deposits. The country's financial stability fund (HFSF) is now expected to recapitalize the two lenders separately. The National Bank of Greece and Eurobank announced that they will step up their efforts to find (separately) private investors to participate in the capital increase and thereby maintain their private status after the injection of HFSF funds.

- The national statistics office announced that the 2012 general government deficit settled at 10% of GDP (EUR 19.4bn). This reading includes the cost of the banking sector recapitalization, equal to 4% of GDP. The primary budget deficit net of support to the banking sector was approximately 1.0%. General government debt declined from 170% to 157%. This follows the PSI and the package of upfront debt relief measures, including a maturity extension on existing loans, granted by the Troika.

DEFICIT INTEREST PAYMENTS WERE REDUCED SHARPLY



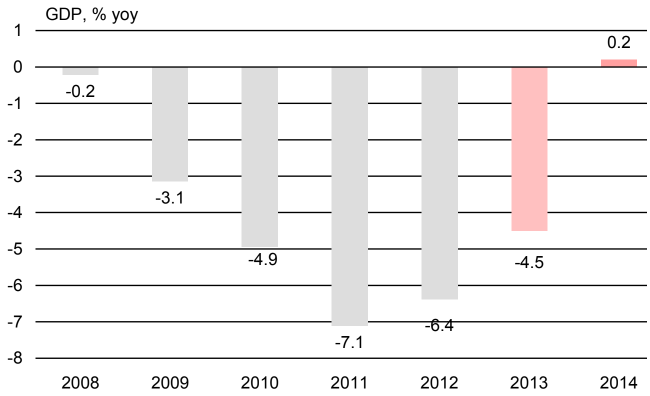
2012 GENERAL GOVERNMENT DEBT BY INSTRUMENT



Source: IMF, UniCredit Research

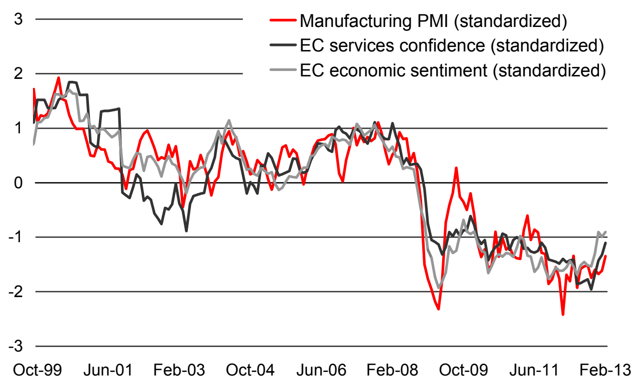
Greece

GDP



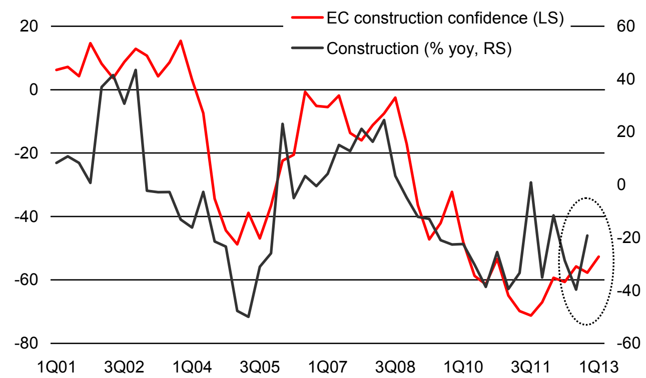
■ Greece may exit recession next year.

SURVEYS



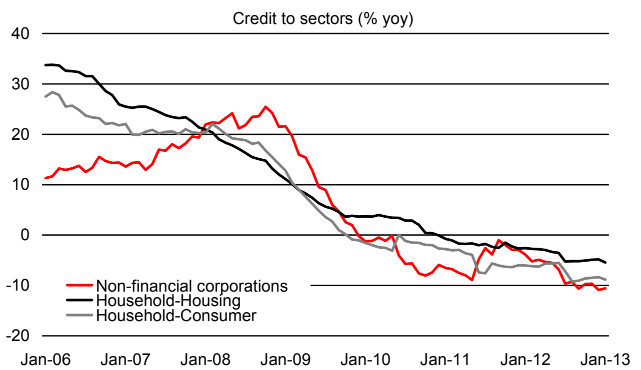
■ Sentiment is improving, albeit from very low levels.

CONSTRUCTION



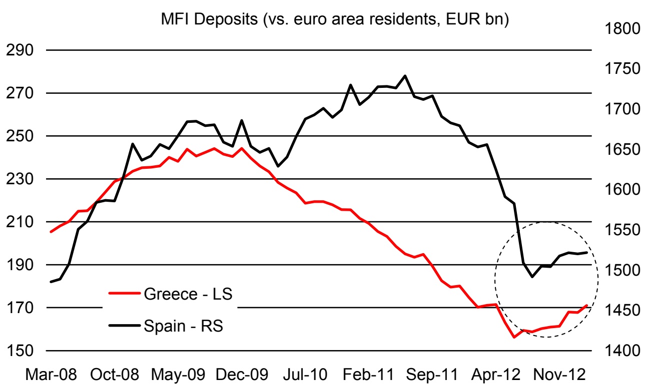
■ The EC survey of construction activity suggests that sectoral output fared well in 1Q13.

CREDIT GROWTH



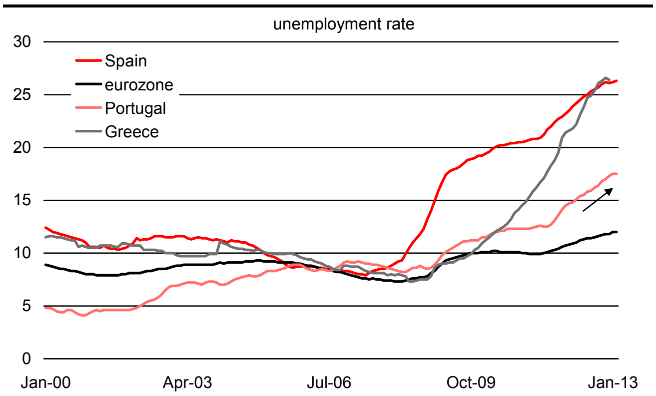
■ Credit continues to shrink, albeit at a modest pace and especially for NFCs.

DEPOSITS



■ There has been a reflow of deposits since the last summer.

UNEMPLOYMENT RATE



■ The unemployment rate is skyrocketing, having reached 26.4% at end-2012.

Source: Elstat, EC, Markit, Eurostat, ECB, Central Bank of Greece, UniCredit Research

Portugal

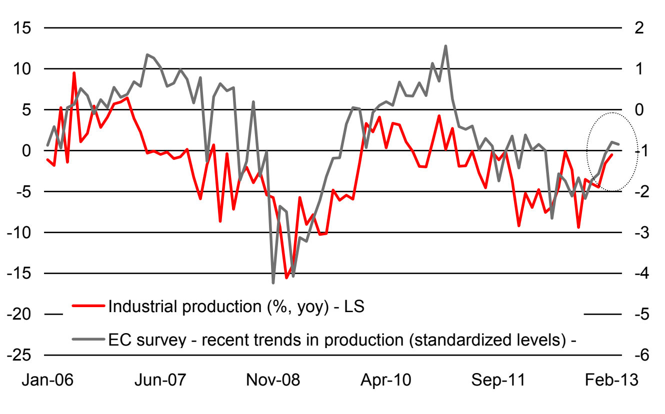
Tullia Bucco,
Economist
(UniCredit Bank Milan)
+39 02 8862-2079
tullia.bucco@unicredit.eu

- The few surveys and available hard data suggest that the pace of recession slowed down in the first quarter, and that the slump in economic activity recorded in 4Q12 (-1.8% qoq) may have marked the low point of the recession. Industrial production posted a firm increase in January-February, with the average over this two-month period settling at 2.0% above the previous quarter (when output tumbled by 3.8% qoq). However, the decline in February exports completely offset January's sharp increase, although import growth stabilized at the January (soft) level. Nevertheless, the European Commission survey suggests that the outlook for exports remains relatively favorable. Our quarterly profile foresees GDP recovering gradually in the coming quarters, with the economy returning to modest positive growth at the turn of the year. We expect GDP to shrink by 2.5% in 2013, after -3.2% in 2012.

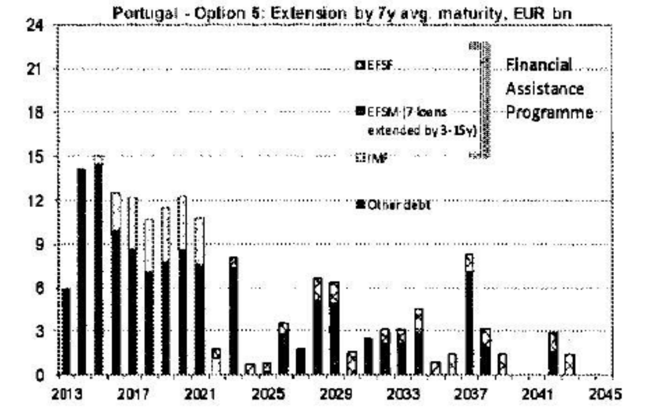
- The Portuguese government's commitment to budget consolidation recently faced a new test as the constitutional court challenged the fairness of some of the already announced spending cuts for 2013 (worth up to EUR1.3bn). Prime Minister Coelho swiftly announced that the resulting deficit shortfall will be filled via cost reduction measures across ministries (up to EUR 600mn) and new spending cuts in health and education, social security and public companies. Thanks to this prompt response, the government got the (conditional) green light from the ECOFIN for the long-pledged maturity extension of the EFSM and EFSF loans. The extension issue has been pressing for both Ireland and Portugal as they aim to quickly recover full market access – a key condition to become OMT-eligible.

- EU Finance Ministers ultimately decided to grant both Ireland and Portugal a 7-year extension to the maximum average maturity of EU loans. This reportedly seemed the best compromise to accommodate the constraints and preferences of debtors and creditors. We recall that Greece obtained a 15-year extension last year. According to the Troika's calculations, a 7-year maturity extension would entail an extension of EU loans to Portugal to an average maturity of approximately 22 years, allowing a significantly smoother redemption profile. Most importantly, by removing redemptions falling due between 2024 and 2027, the new amortization plan provides Portugal with room to return to the debt market with a new issuance at the 10Y tenor.

REBOUND IN IP AT THE BEGINNING OF THE YEAR



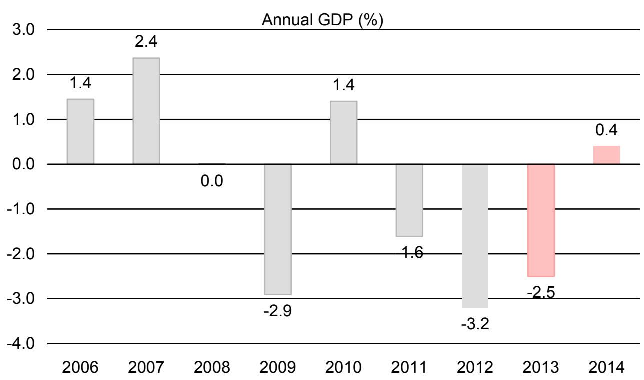
GREENLIGHT GIVEN TO SMOOTHER REDEMPTION PROFILE



Source: Eurostat, IMF, UniCredit Research

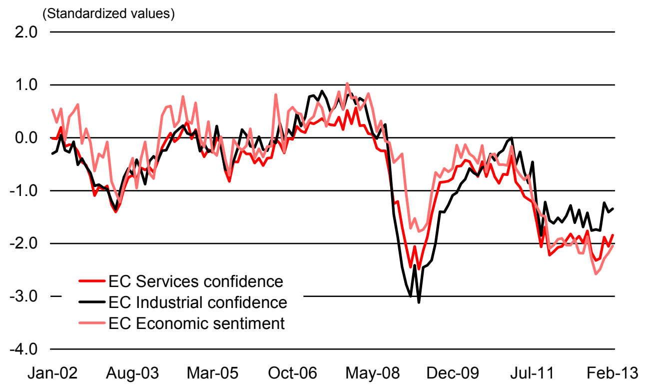
Portugal

GDP



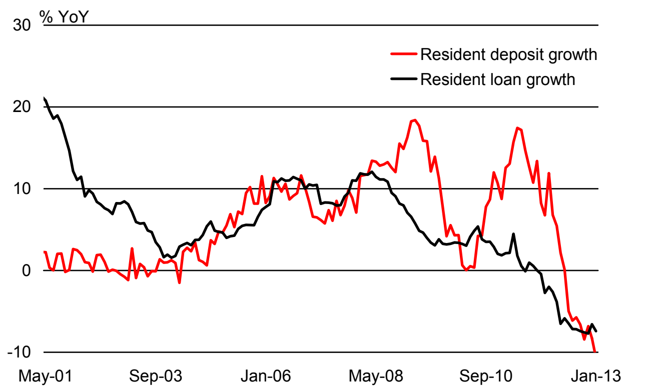
■ Recession to stretch into 2013.

SURVEYS



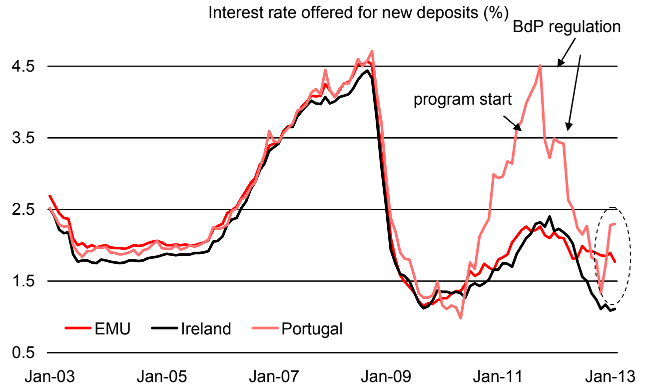
■ Sentiment shows signs of improvement, albeit from low levels.

DEPOSIT AND LOAN GROWTH



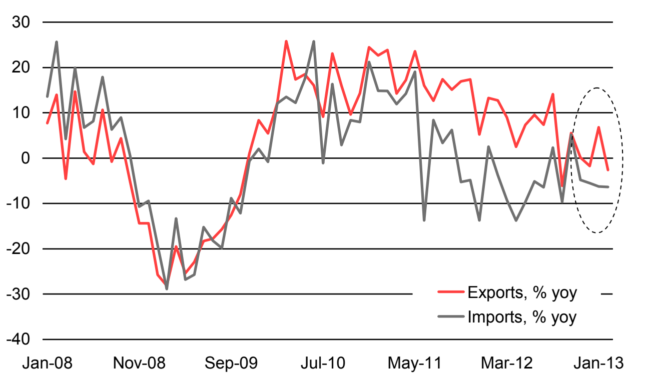
■ Deposit growth continues to slow…

DEPOSIT RATES



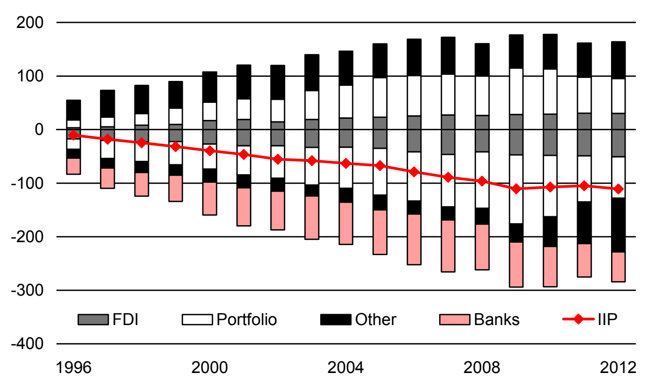
■ …partly explained by regulatory changes to offered interest rates. However, interest on new deposits recently rebounded.

EXPORT/IMPORT GROWTH



■ The decline in February exports offset January's sharp increase, although import growth stabilized at soft levels.

NET IIP



■ External deleveraging is only just beginning.

Source: INE, Bank of Portugal, UniCredit Research

UK

Mauro Giorgio Marrano, Economist (UniCredit Bank Milan)
+39 02 8862-8222
mauro.giorgiomarrano@unicredit.eu

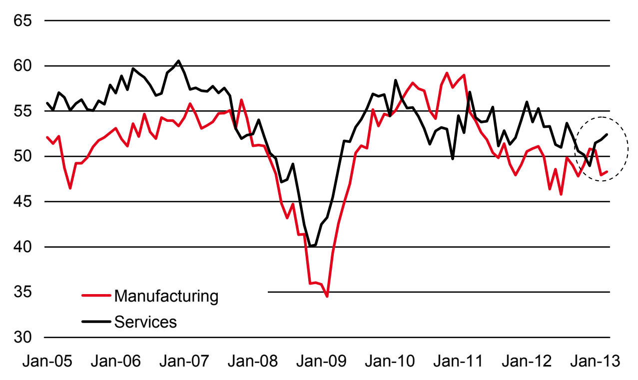
- Data over the past month were broadly consistent with our GDP forecast of a +0.1% qoq expansion in 1Q13, although risks remain to the downside. The PMIs confirmed the relatively better shape of the services sector compared to manufacturing in 1Q13 (see left chart below). The services PMI rose further from 51.8 to 52.3 in March, while the manufacturing index, after tumbling from 50.7 to 47.9 in February, rose to 48.3. Our composite PMI suggests a GDP growth rate in line with our forecast (see right chart). The ONS index of services rose 0.3% mom in January, while IP, after falling 1.3% mom in January, surprised to the upside, rebounding 1.0% mom.

- CPI inflation remained stable at 2.8% in March. Looking forward, we expect inflation to hover around that level in the first half of 2013, before slowing somewhat in the remainder of the year, although still remaining above target due the impact of sterling's recent depreciation and the persistent upward contribution from administered and regulated prices.

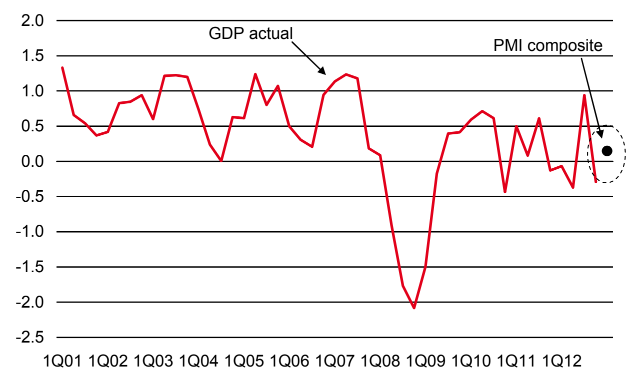
- On 20 March, Chancellor Osborne presented his 2013 budget, alongside changes to the Bank of England's remit and the Office of Budget Responsibility's (OBR) new macroeconomic and fiscal forecasts. The BoE's new remit, while reconfirming the inflation target of 2% as measured by the CPI and the primacy of price stability, "mandates" the MPC to consider Fed-like forward guidance. On the fiscal front, the government did not backtrack on fiscal consolidation. The updated macroeconomic and fiscal forecasts showed lower GDP growth in 2013 and 2014 (from 1.2% to 0.6% and 2.0% to 1.8%, respectively) and some deterioration of the fiscal outlook over the whole forecast horizon.

- As expected, the BoE remained on hold on both asset purchases and the Bank rate, in line with expectations. The MPC is likely to have remained divided on the need for more QE as in the past two months, with some members stressing the need to support the early signs of economic recovery, but with the majority highlighting the risk that further QE could increase inflation expectations, lead to an unwarranted depreciation of sterling, and most probably be ineffective in boosting growth. Looking forward, we expect the BoE to remain on hold on QE for the foreseeable future, barring a deterioration in the growth outlook.

SERVICES PMI REMAINS RELATIVELY RESILIENT



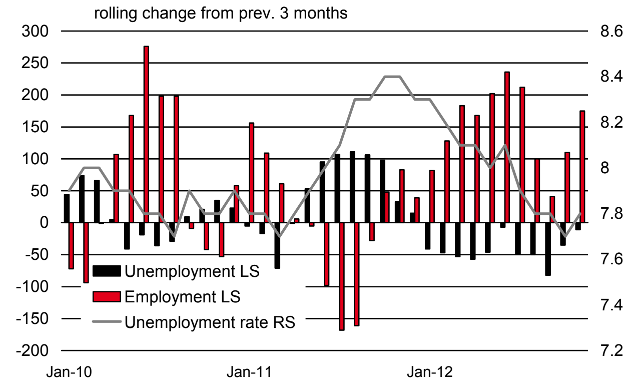
WE STILL EXPECT MODEST POSITIVE GROWTH IN 1Q



Source: Office for National Statistics, Markit, UniCredit Research

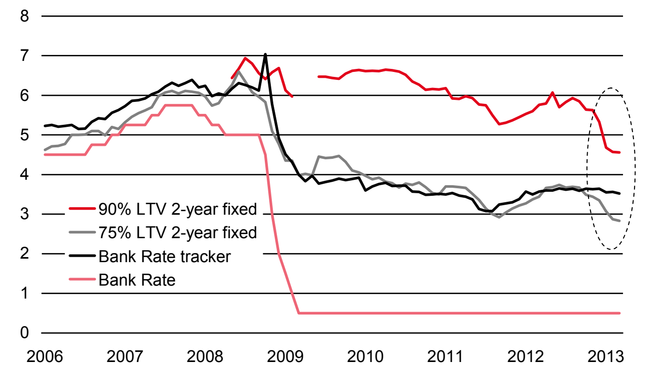
UK

LABOR MARKET



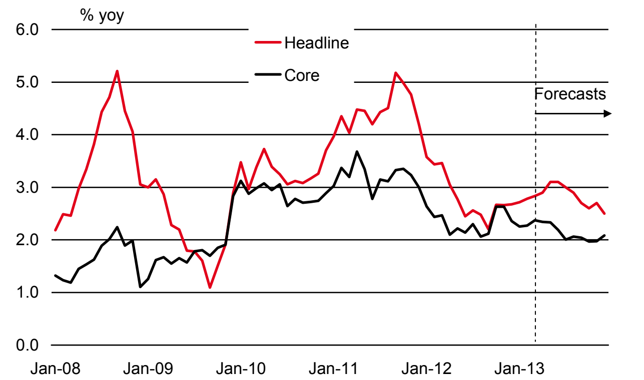
- Labor market continues to be relatively resilient.

QUOTED MORTGAGE RATES



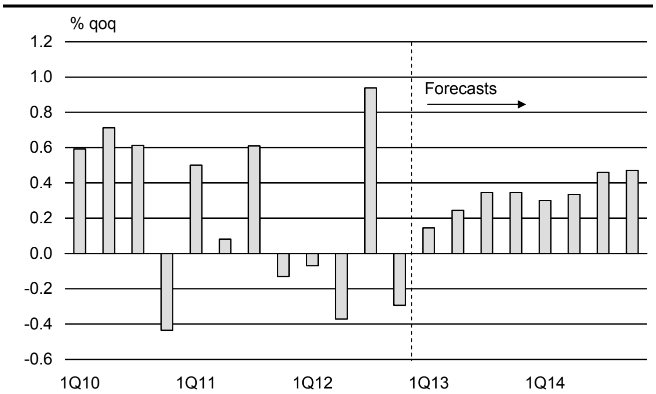
- Mortgage rates for the most popular products continued their downward trend in February.

CPI INFLATION (FORECAST FOR 2013)



- Inflation remained stable at 2.8% in March.

GDP FORECASTS



- We expect a very gradual recovery starting in 1Q13, but downside risks have increased.

CONSUMER CONFIDENCE

- Consumer confidence remained stable at -26 in March.

STERLING EFFECTIVE EXCHANGE RATE

- The sterling effective exchange rate appears to have halted the downward trend started in January.

Source: Office for National Statistics, Bank of England, Gfk, Markit, UniCredit Research

Sweden

Chiara Silvestre, Economist (UniCredit Bank Milan)
chiara.silvestre@
unicreditgroup.de

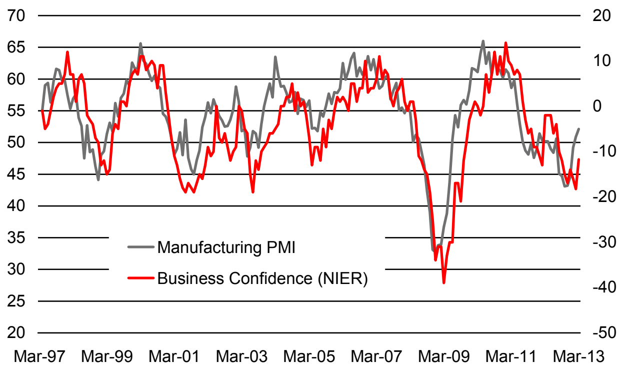
- Business surveys improved further in March (see left chart). The NIER manufacturing confidence indicator rose from -11 to -10, the second consecutive improvement, while the manufacturing PMI increased from 50.9 to 52, the third increase in a row. Regarding hard data, IP posted a marginal increase in February (0.5% mom) after the strong January contraction (-1.1% mom), while the service production index rose by 0.9% mom in February vs. 0.5% mom in previous month. Overall, business surveys and hard data released over the past month remain broadly consistent with our GDP forecast of a 0.3% qoq (1.4% yoy) expansion in 1Q13.

- Consumer confidence and retail sales data point to a further strengthening in private consumption in 1Q13 (private consumption rose 0.9% qoq in 4Q12). The consumer confidence indicator (CCI) rose further from -1.0 to 2.8 in March, bringing the CCI average for 1Q13 to -0.4 (from -7.5 in 4Q12). The index is now marginally below its historical average (see right chart). Average retail sales in January and February were 1.6% higher than the average for 4Q12. Looking forward, we expect private consumption to continue to support the recovery, although some factors – such as the high level of household indebtedness (now at 173% of disposable income), a potential correction in house prices, combined with rising unemployment – could curb households' consumption upswing.

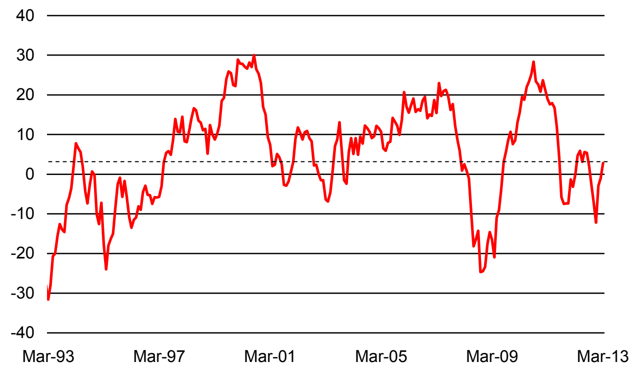
- In March, CPIF inflation, which excludes mortgage interest costs, slowed slightly to 0.9% vs. 1.0% previous month, while CPI inflation was 0.0%, up from -0.2% in February. Looking forward, we expect CPIF inflation to oscillate around 1% during 2013, while CPI inflation will likely resume a gradual accelerating trend at the end of spring.

- High unemployment, low inflation and low inflation expectations might increase pressure on the Riksbank to cut rates. However, we think that the Riksbank will probably continue to assign more weight to the recent positive developments, which include the easing in financial market tensions, the improvement in consumer and business sentiment in Sweden, the continued recovery in the US, and signs of strengthening in world growth. Hence, we expect the Riksbank to remain on hold at the April meeting, also on the back of concerns about rising household indebtedness.

BUSINESS SURVEYS IMPROVED FURTHER



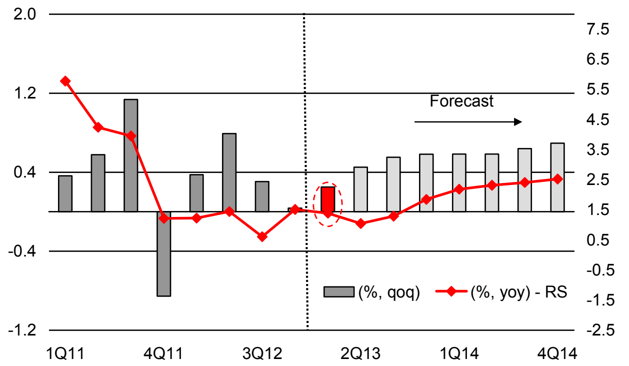
CONSUMER CONFIDENCE CONTINUES TO RISE



Source: NIER, Statistics Sweden, UniCredit Research

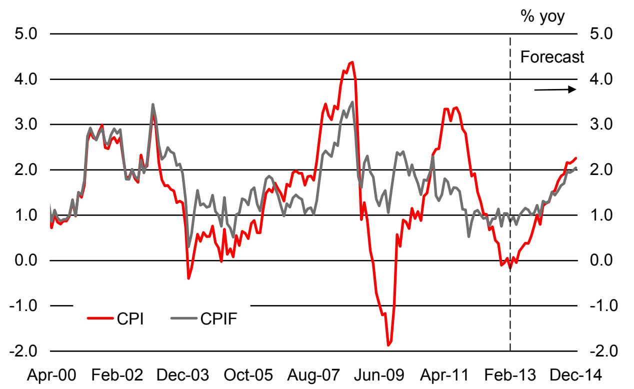
Sweden

GDP



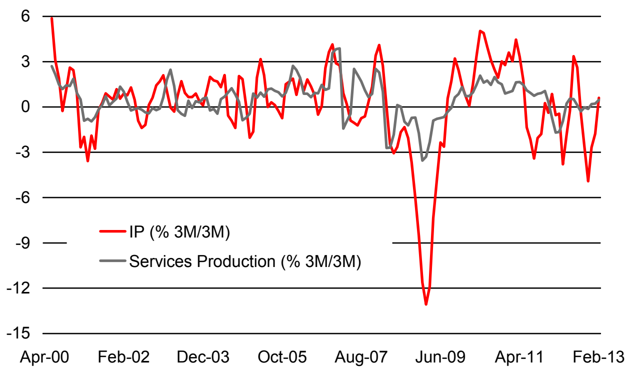
- We expect sluggish growth in 1H13 and a more sustained recovery in 2H13.

INFLATION



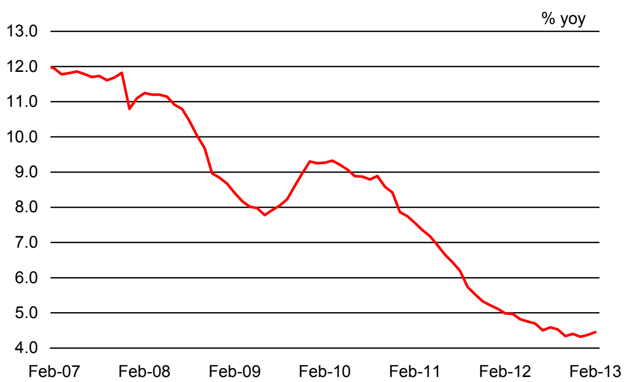
- In March, CPI inflation was 0.0%, up from -0.2% in February, while the CPIF inflation edged down to 0.9% (from 1.0% in February).

INDUSTRIAL PRODUCTION AND SERVICES PRODUCTION



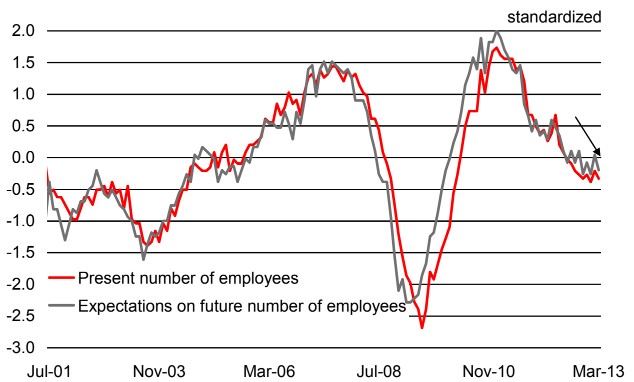
- In February, both services and industrial production indices increased vs. the previous month. The 3M/3M rate rebounded from -1.8% to 0.6% for IP and accelerated from 0.2% to 0.5% for services production.

LENDING TO HOUSEHOLDS



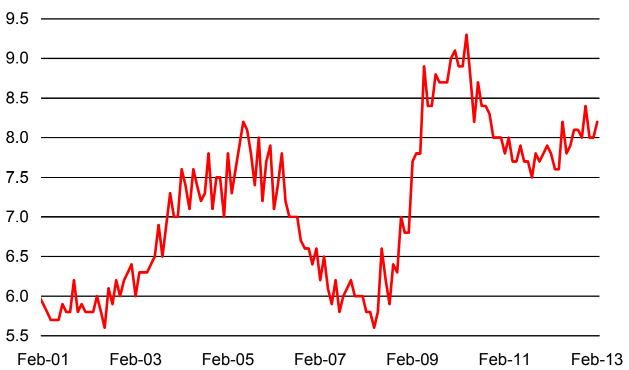
- Loans to households accelerated from 4.5% yoy to 4.6% yoy in February (vs. 4.5% in January) and appear to have reached a turning point.

LABOR MARKET SURVEY INDICATORS



- The NIER survey points to a further decline in employment in total industry.

UNEMPLOYMENT RATE



- The unemployment rate (SA) is currently high at 8.2% and will likely hover around 8% level in the coming months.

Source: NIER, Statistics Sweden, Swedbank and Silf, UniCredit Research

Poland

Marcin Mrowiec,
Head of Macroeconomic Research Bureau (Bank Pekao)
+48 22 524-5914
marcin.mrowiec@pekao.com.pl

- The high-frequency data due to be released in April will permit a preliminary assessment of the economic performance in the first quarter of 2013. Still subdued industrial output growth and sharply contracting construction-assembly production suggest that GDP growth remained weak in the first three months of this year. We forecast that fixed investments contracted by about 4% yoy, while we see some upside risks to our estimate of a 1.5% yoy decline in individual consumption.

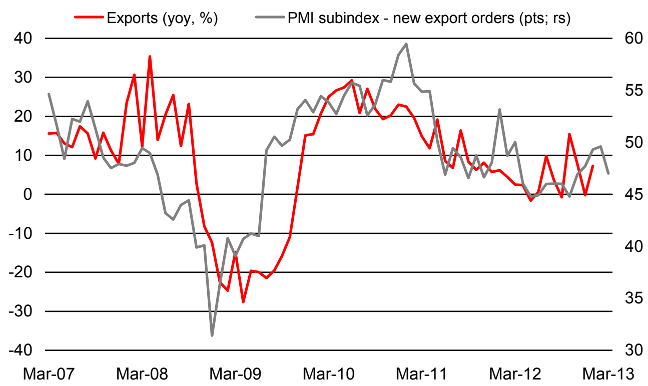
- The declining domestic demand and the unfavorable conditions in the labor market (falling employment, sluggish rise in real wages, rising unemployment) translate into the lack of inflationary pressure. Headline inflation is to run below the NBP target of 2.5%, and even the lower band of acceptable deviations from the target of 1.5% for the next few months and its bottom is foreseen below 1% yoy.

- The Monetary Policy Council kept interest rates unchanged. The decision was in line with expectations. The governor of the NBP, M. Belka, said that the Council maintained a "wait and see" approach. He said that the statement was not promising a rate cut next month, but if inflation remains below 1% in the long term, the MPC would consider a cut. We expect that in the coming months the MPC will not change interest rates. However, we believe that the discussion on a possible restart of monetary easing may take place in July, by way of publication of the new inflation projection.

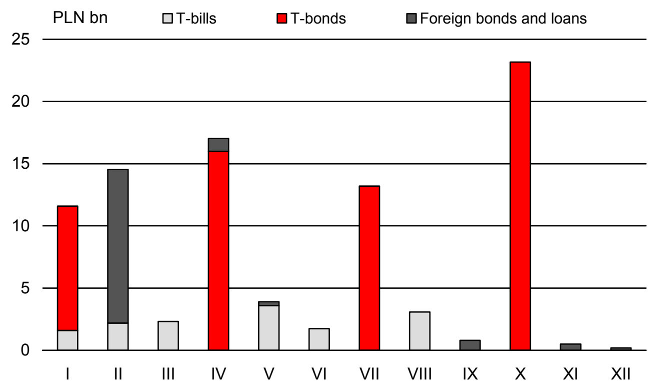
- Both internal factors (stronger decline in inflation, rising expectations for the continuation of the interest rates cycle) and expansionary policies of main central banks led to another rally on the domestic bond market. In the coming weeks, Polish benchmarks may follow German Bunds and we see a risk of moderate profit-taking and higher yields at the long end of the curve. We expect a little bit steeper curve and yields in the range of 3.05-3.15% (2Y), 3.10-3.25% (5Y) and 3.50-3.65% (10Y).

- Strong rally of domestic FI supported Polish zloty. Although the rate is still sentiment driven and the global sentiment may support risky assets, we see a risk of profit-taking on the PLN. Local factors like the pessimistic fiscal outlook and also calls for further monetary easing may affect the zloty in coming weeks. We forecast the EUR-PLN closer to 4.15 and the USD-PLN near the key technical zone 3.19-3.20.

NEW EXPORT ORDERS ARE STILL STAGNATING



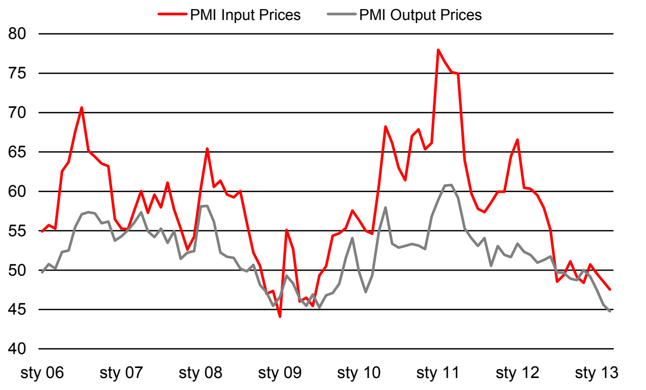
APRIL WILL SEE SIZEABLE T-BOND ROLLING OVER



Source: GUS, UniCredit Research

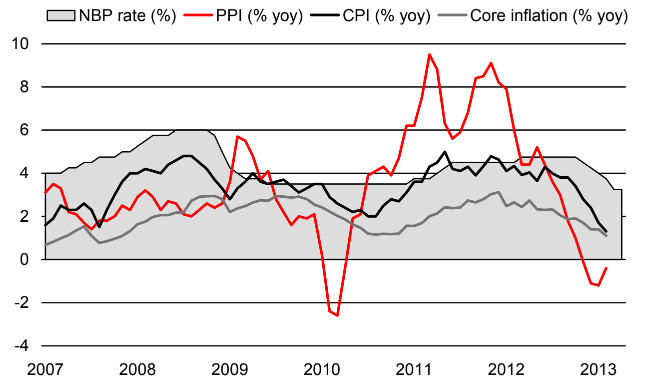
Poland

PMI INPUT PRICES AND PMI OUTPUT PRICES



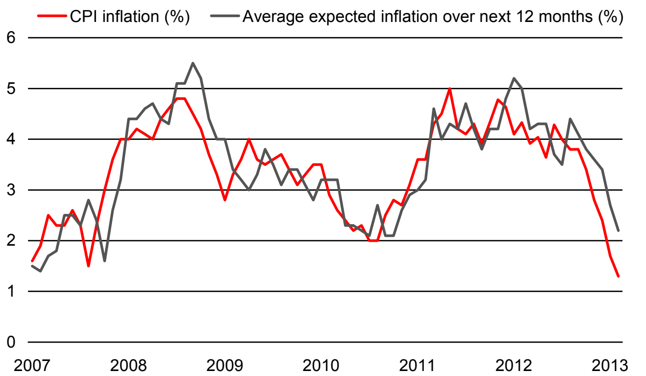
- Both PMI input as well as output prices suggest continued declines of CPI.

INFLATION



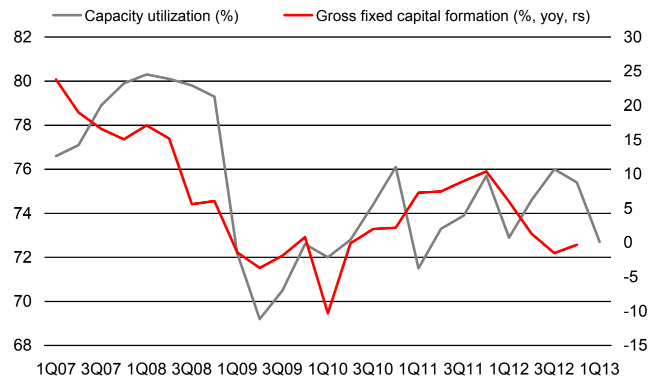
- Inflation should fall on all levels at least till June.

INFLATION EXPECTATIONS



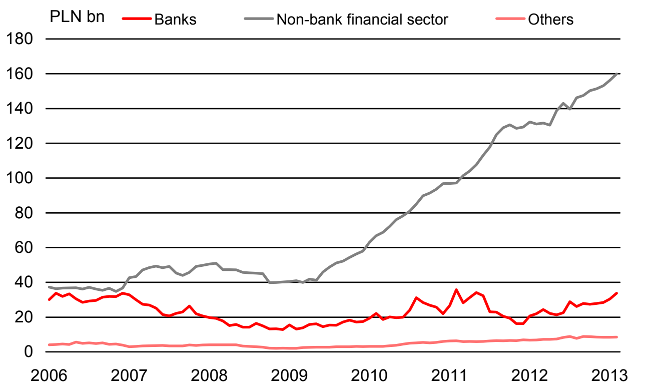
- Inflation expectations are also declining.

CAPACITY UTILIZATION AND INVESTMENTS



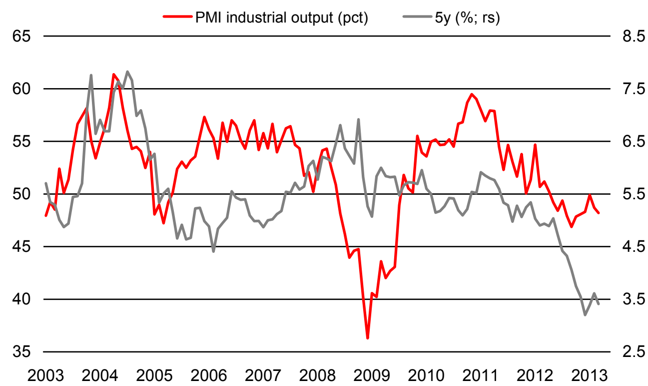
- Falling capacity utilization will mean lower appetite for new investments.

STRUCTURE OF NON-RESIDENT HOLDINGS OF POLGBS



- The good news about the structure of holders of POLGBs is that there's an increasing share of long-term holders of debt.

PMI INDUSTRIAL OUTPUT AND 5Y T-BOND BENCHMARK YIELD



- As we look for an improvement in yoy industrial output, T-bond yields might be under pressure in the coming months.

Source: GUS, NBP, PFSA, Markit, UniCredit Research

Czech Republic

Pavel Sobisek,
Chief Economist
(UniCredit Bank Czechia)
+420 955 960-716
pavel.sobisek@unicreditgroup.cz

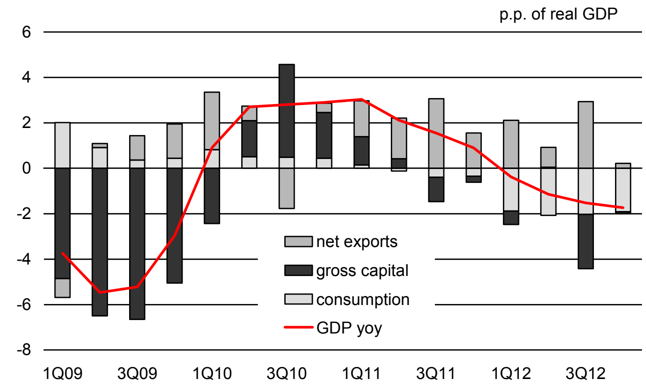
- Economic activity remained depressed in 1Q13, as evidenced by a majority of short-term indicators. The seasonally-adjusted mom industrial output was not overly negative, coming in at -0.1% and 1.6% for January and February respectively, but new industrial orders saw sharp yoy declines of 7.6% and 10.2%, unadjusted, for the same months. Manufacturing PMI hit an 11-month high of 49.9 in February, but dipped to 49.1 in March. Construction output saw a purely weather-related spike of 2.3% yoy in February. Trade balance improved yoy only marginally during the January-February period, with the volumes on both exports and imports declining yoy. As the terms of trade turned positive, the contribution of net exports to GDP probably stalled.

- Retail sales were down 0.6% and 4.7% yoy unadjusted for January and February, suggesting that private consumption barely recovered from its 2012 slump. New car registrations were down 16.8% yoy in the whole of 1Q13, with March posting a decline of 19.4% yoy, meaning that retail sales probably saw yet another bad month. Extremely cold weather in March probably contributed to consumers holding back on their spending.

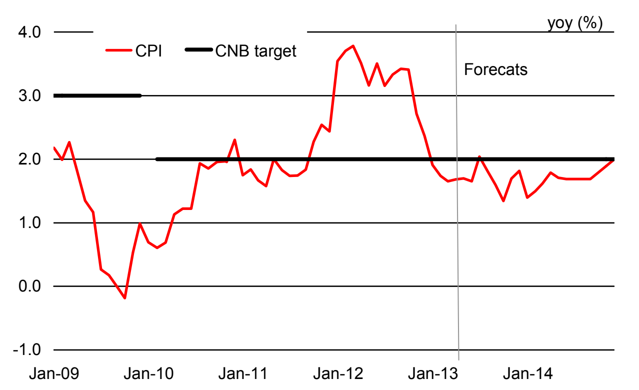
- March CPI remained unchanged at 1.7% yoy for the second month running. This implies that inflation has firmly settled below the central bank's 2% target. With a decline in natural gas prices in the pipeline for 2Q13, we see an increasing chance that CPI will stay below the target level at least for the coming 12 months.

- The CNB has made no changes to its policy setting or its rhetoric, stressing again that interventions to weaken the CZK could be used to ease monetary conditions if needed. On the fiscal front, the central government budget remained in surplus at CZK 14bn (0.4% of GDP) at the end of March. While the picture was blurred by a number of extraordinary items, the 25% yoy rise in VAT collection was genuine. We attribute this primarily to the implementation of new measures for tackling tax evasion. Hence, public sector finance appears to be on course to meet this year's deficit target of 2.9% of GDP.

CONSUMPTION WAS A DRAG ON GDP OVER THE WHOLE OF 2012



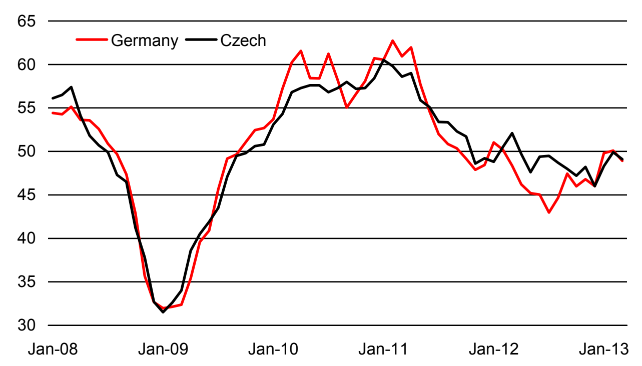
INFLATION SETTLED FIRMLY BELOW THE CNB'S 2% TARGET



Source: CZSO, UniCredit Research

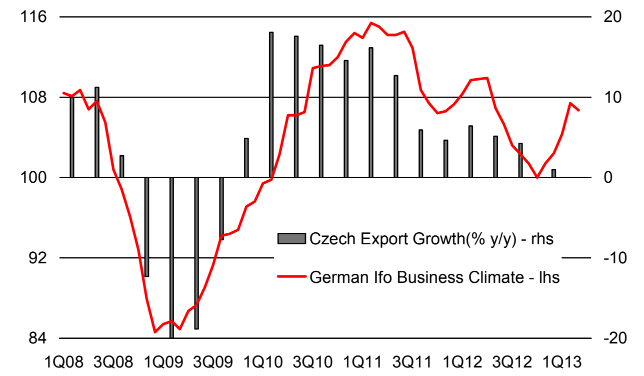
Czech Republic

MANUFACTURING PMI FOR THE CZECH REP AND GERMANY



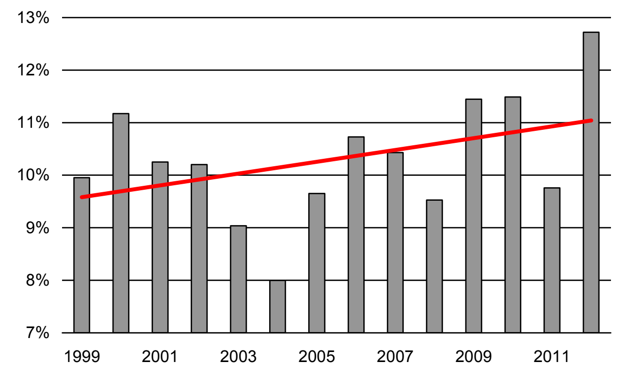
- Manufacturing PMI is struggling to overcome the 50-mark. Correlation with German PMI has been on the rise lately.

GERMAN IFO AND CZECH EXPORT GROWTH



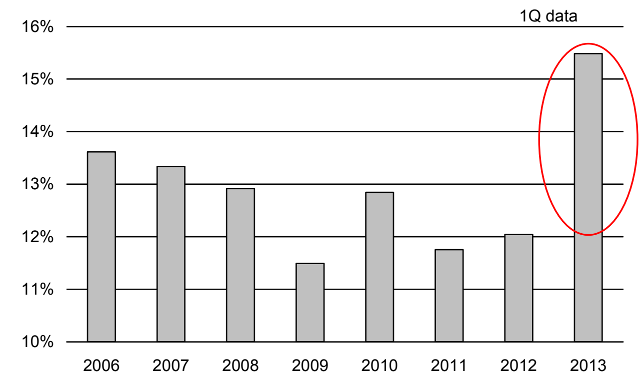
- Shifts in German business confidence are reflected in Czech export opportunities. The latest Ifo hike looks promising for 2Q13.

HOUSEHOLD SAVINGS RATIO



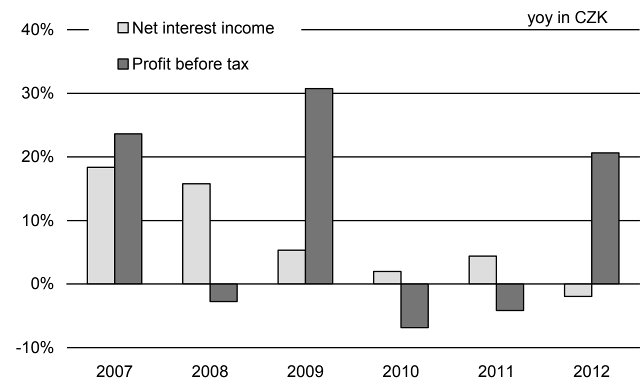
- Household saving ratio hit an all-time high in 2012, as economic recession and tax hikes depressed consumer confidence.

SHARE OF VAT COLLECTION ON PRIVATE CONSUMPTION



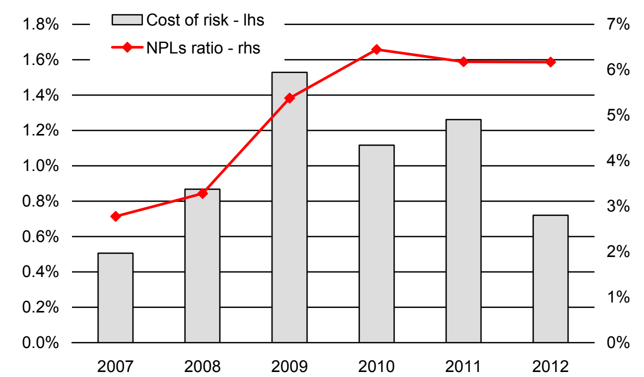
- VAT collection improved by 25% yoy in 1Q13. We attribute this primarily to new measures for tackling tax evasion.

BANKING SECTOR NET INCOME AND EARNINGS BEFORE TAX



- Banking profits improved in 2012 on lower provisions but net interest income shrank due to extremely low interest rates.

BANKING SECTOR NPL RATIO AND COST OF RISK



- In 2012, the banking sector cost of risk approached pre-crisis levels, as the NPL ratio stabilized.

Source: CZSO, CNB, UniCredit Research

Hungary

Dan Bucşa,
Economist
(UniCredit Bank London)
+44 207 826-7954
dan.bucsa@unicredit.eu

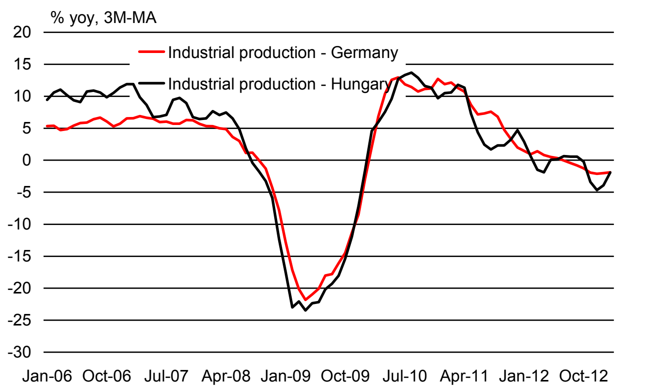
- Annual CPI inflation fell to 2.2% in March amid a third consecutive monthly decline in electricity and gas prices (for a total negative contribution of -1.3pp to the headline figure so far in 2013). Weak demand continues to weigh on the prices of durable goods (-2.2% yoy) and food (+3.4% yoy, one of the lowest rates in CEE countries due to the poor harvest in 2012). With the prospect of a better harvest in 2013 inflation will probably end 2013 close to the target, despite planned hikes in administered prices. Moreover, potential additional cuts to energy prices could push headline inflation close to 2% by the end of the year, a record low since the end of the communist regime. Since most of the disinflation this year has administrative and supply-side causes, we still believe that inflation will rise again in 2014 due to a negative base effect, as well as pre-election spending and the need to raise additional tax revenues in order to limit the budget deficit to 3% of GDP.

- The National Bank of Hungary (NBH) continues to pursue its easing cycle and we believe now that it could stop at 4.0%, with risks that the base rate may be cut to as low as 3.5%. The good risk appetite for Hungarian bonds, low inflation and poor growth support further rate cuts, but the risk of a rapid reversal is high.

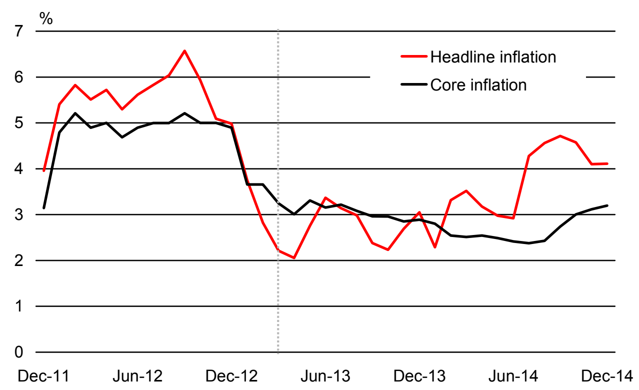
- The NBH announced the launch of the Funding for Growth Scheme (FGS), a set of measures aimed at spurring lending and reducing the FX exposure of SMEs and banks. While the measures are still subject to negotiations with banks, the NBH aims to: **1.** Boost lending to SMEs by lending HUF 250bn (EUR 0.83bn or 0.8% of GDP) to banks at 0%. The loan margin will be capped at 2pp. **2.** Reduce the FX exposure of SMEs by converting FX loans into HUF. Another HUF 250bn line will be provided to banks under the same conditions (0% cost, 2% maximum interest charged by banks on loans). The central bank is willing to provide FX out of its FX reserves for banks to repay their short-term foreign liabilities. **3.** Reduce short-term external debt by HUF 1,000bn (EUR 3.3bn or almost 20%) by using its FX reserves. While bold in purpose, the FGS could have limited results: demand remains weak and its structure is skewed towards cash-strapped companies, increasing the risk of adverse selection.

- Industrial production fell by 1.1% yoy in February (working-day adjusted). Without the working day adjustment, IP was down 5.4% yoy, since 2012 was a leap year. On seasonally adjusted data, IP was up 0.3% mom (after +2.9% mom in January). Industrial sales were down 1.9% mom (sa), with domestic sales down 2.0% mom and export sales falling 0.6% mom. IP is improving in Hungary after a very weak 4Q12, but the improvement is very slow due to a weaker-than-expected recovery of foreign demand.

TENTATIVE RECOVERY OF INDUSTRIAL PRODUCTION



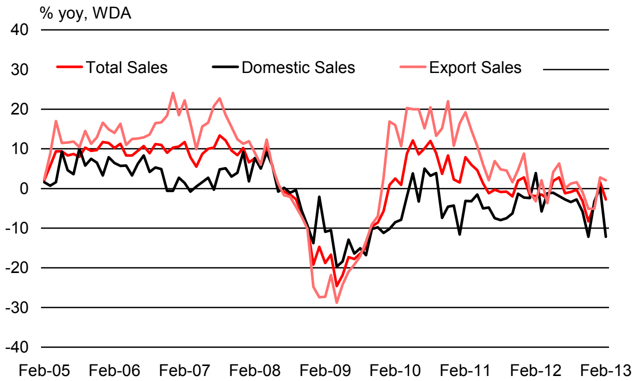
INFLATION FALLING ON ENERGY AND GAS PRICE CUTS



Source: KSH, UniCredit Research

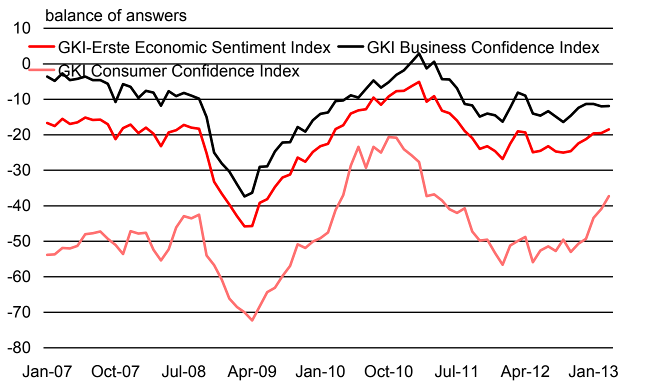
Hungary

INDUSTRIAL SALES



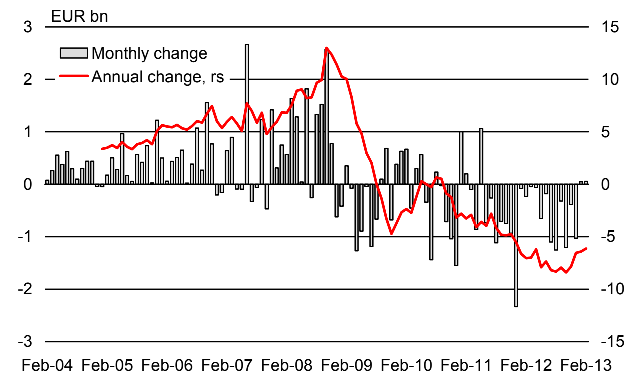
- Domestic demand remained a drag on industrial sales in February.

CONSUMER AND BUSINESS CONFIDENCE



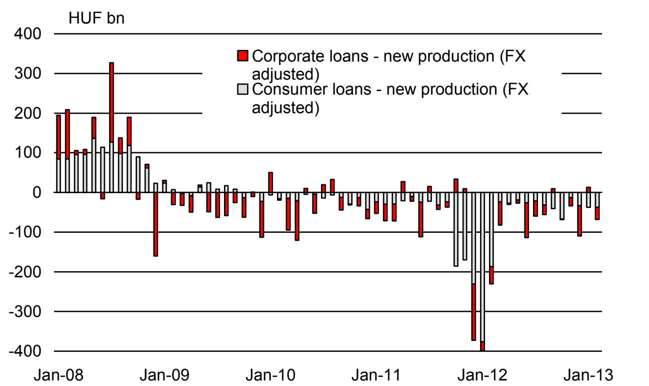
- A further improvement in consumer confidence is not matched by retail sales, but bodes well for the government's approval ratings.

BANK DELEVERAGING



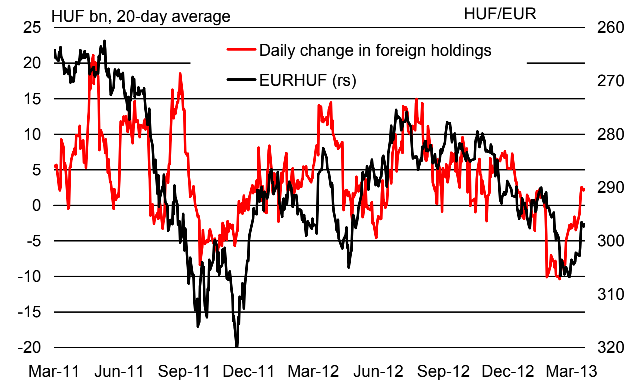
- The foreign liabilities of the banking system rose in January and February after declining for 19 consecutive months...

NEW LENDING



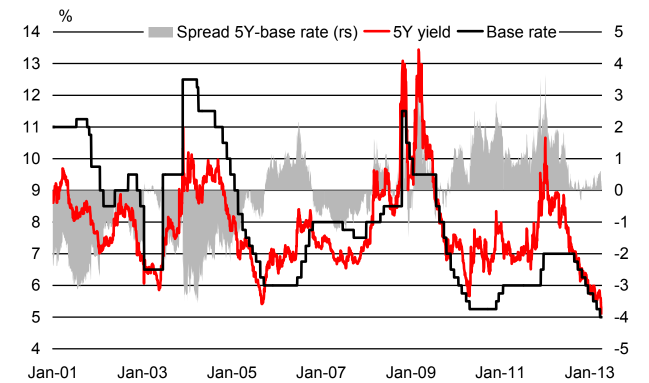
- …nevertheless, lending is not recovering yet.

HUF AND NET BOND PURCHASES BY FOREIGN INVESTORS



- The HUF receives support from renewed interest in HGBs, brought about by better risk appetite for CEE assets.

SCOPE FOR MORE MONETARY POLICY EASING



- Supportive markets allow the NBH to extend its rate-cutting cycle.

Source: KSH, NBH, AKK, Haver, UniCredit Research

US

Dr. Harm Bandholz, CFA
(UniCredit Bank New York)
+1 212 672-5957
harm.bandholz@unicredit.eu

- Shifting growth from the second to the first quarter. Having stressed the upside risks to our 1Q13 GDP call for several weeks, we are now raising our growth forecast for the first quarter to 3.0% from 1.5%. Most importantly, consumer spending expanded much faster than expected, as the combination of labor market progress and the renewed pick-up in private borrowing allowed households to weather the drag from higher payroll taxes and costlier fuel (see left chart below).

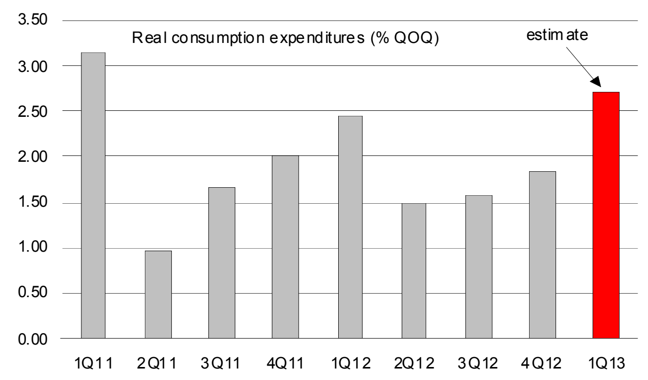
- That said, we still do not think that the consumer – and thus the economy – can completely shrug off the drag from tighter fiscal policy. Accordingly, we are lowering our 2Q13 forecast to 1.8% from 2.8%. The 2013 average still goes up to 2.2% from 2.0%. Moreover, it is important to emphasize that the pick-up in growth after a sluggish 4Q12 occurred even faster than we had expected (2Q13). Most market participants had projected a growth rebound only for the second half of the year.

- The impending slowdown in the current quarter is now indicated by several factors. The manufacturing and non-manufacturing ISMs dropped in March from multi-month highs, retail sales fell, capex orders declined and the NAHB housing market index eased for the third straight month. We do not think, however, that any of these developments is a concern for the medium-term outlook, in particular, as most of the declines come on the back of strong gains in the previous couple of months.

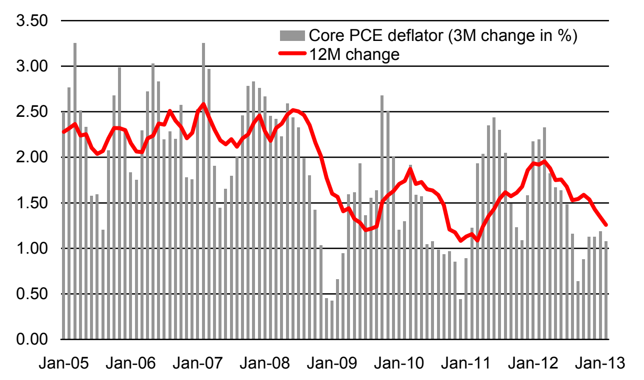
- Employment gains also took a breather in March. But while the increase in nonfarm payrolls (88,000) was less than half as strong as in the previous six months, the number of total working hours rose faster than the 6M average, as companies ramped up average working time. Total labor demand, therefore, continued to rise solidly. The jobless rate fell to 7.6%, the lowest since late 2008. But this is largely due to a statistical fluke as another 500,000 people left the labor force, and the participation rate fell to its lowest level since 1978.

- At its latest FOMC meeting, in mid-March, the Fed said that it will continue to buy USD 85bn in long-term securities per month. Low inflation rates (see right chart) and the temporary growth slowdown in the second quarter suggest that the Fed will maintain its current policy stance. We expect that the asset-purchase program (QE3) will be continued until the end of this year.

CONSUMPTION REBOUND – DESPITE HIGHER TAXES



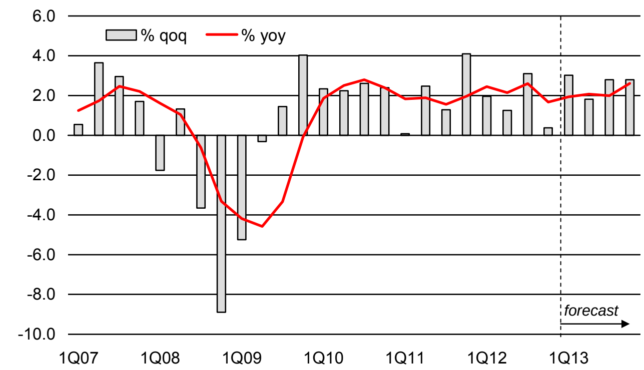
CORE INFLATION TRENDING LOWER



Source: BEA, BLS, UniCredit Research

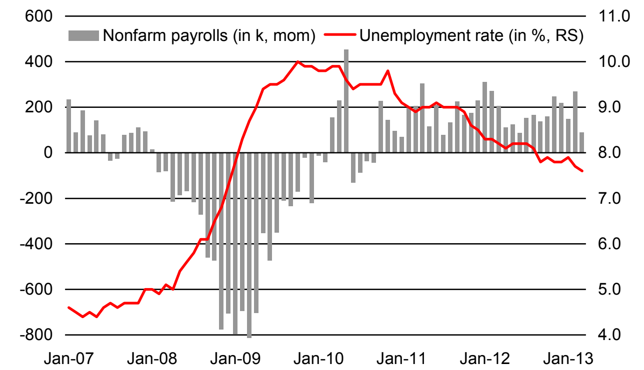
US

REAL GDP, ANNUALIZED RATES OF CHANGE



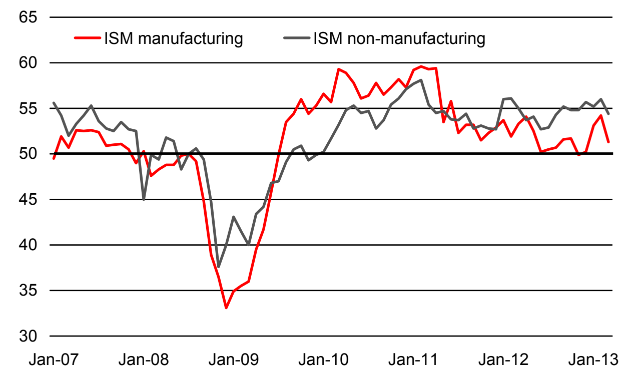
- GDP growth likely bounced back in 1Q13 (+3%) from the disappointing 4Q12. For 2013 as a whole, we expect 2.2%.

NONFARM PAYROLLS AND UNEMPLOYMENT RATE



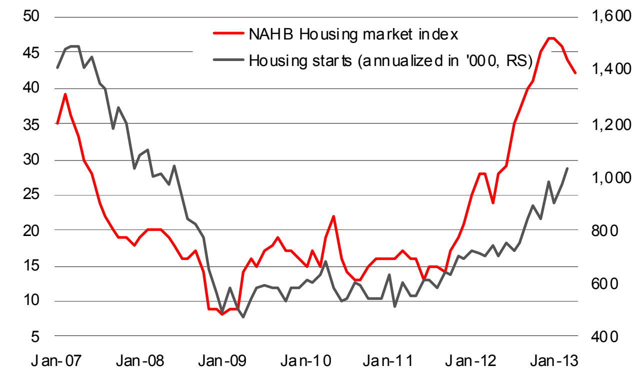
- Nonfarm payrolls rose only 88,000 in March, while the jobless rate fell to 7.6%, the lowest since late 2008.

PMIS



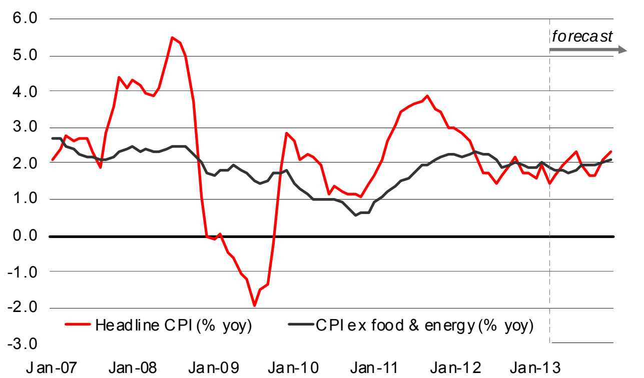
- The manufacturing and non-manufacturing ISMs dropped again in March after hitting multi-month highs in February.

HOUSING MARKET INDEX AND HOUSING STARTS



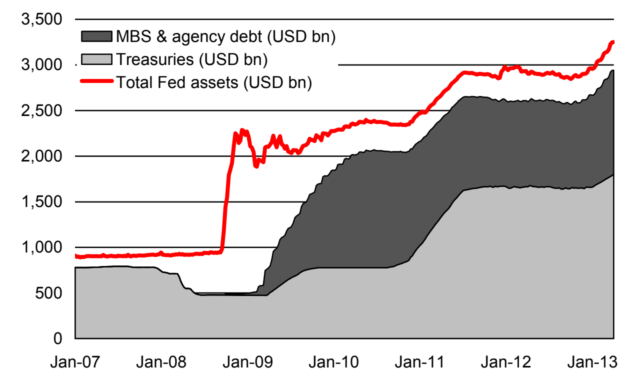
- The NAHB index fell for the third straight month in March. Its level still signals further increases in construction activity.

CONSUMER PRICE INDEX



- Due to lower energy prices, the headline inflation rate fell again to 1.5% yoy in March, while the core rate eased to 1.9%.

FED'S BALANCE SHEET



- The size of the Fed's balance sheet rose to USD 3¼tn, as the Fed continues its large-scale asset purchase program.

Source: BEA, BLS, Federal Reserve, Institute for Supply Management, NAHB, Census Bureau, UniCredit Research

Switzerland

Alexander Koch, CFA
(UniCredit Bank)
+49 89 378-13013
alexander.koch1@unicreditgroup.de

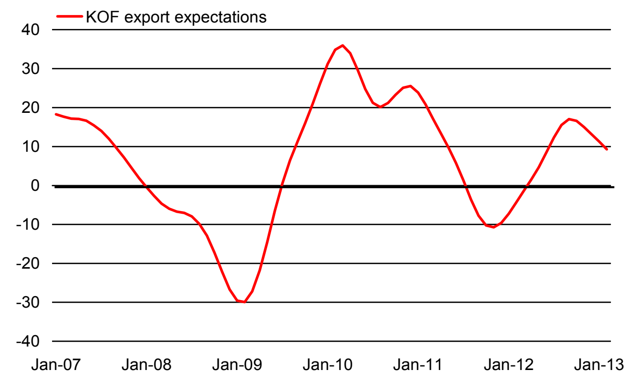
- The Swiss economy maintained its positive growth momentum at the end of 2012. GDP was up 0.2% qoq, primarily supported by robust consumption. Private consumption alone contributed 0.6pp to quarterly growth. Investment was also slightly up qoq, and net services exports contributed moderately, likely driven by the positive impact of higher commodity prices on margins in the important commodity-trading sector, as Switzerland is the world's biggest commodity trading hub. In contrast, net goods exports (without valuables) were a substantial drag, subtracting 0.7pp. The weakness in goods exports was in line with the generally negative dynamic in global industry in the final quarter.

- Notwithstanding the prolonged recession in the EMU periphery, stronger demand from other regions led to an acceleration in Swiss real goods exports in the first two months of 2013. The latest sizeable correction in the Industry PMI underscores that the headwinds for recovery remain substantial. But reassuring signals from Asia and expectations that the US will continue its gradual recovery despite fiscal consolidation kept export expectations of Swiss firms overall in positive territory in March (see left chart). Together with the continuously robust environment for domestic demand, we stick to our forecast of modest growth acceleration throughout 2013. For the first quarter, our GDP Tracker currently even signals some upside risks to the +0.3% qoq GDP growth forecast.

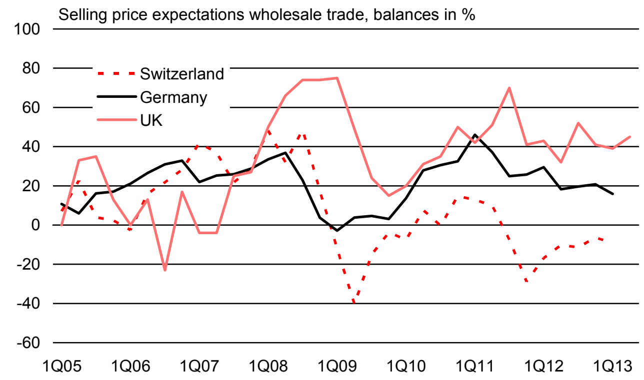
- Despite the comparatively sound economic situation, the annual inflation rate fell from -0.3% to -0.6% in March, driven by lower energy prices. And although the preceding massive exchange rate appreciation has now largely fed through to consumer prices, downward pressure on the elevated domestic price level is still reflected in selling price expectations (see right chart). Accordingly, deflation should peter out only gradually, in line with the SNB's risk assessment that there are currently no inflationary tendencies in Switzerland over the medium-term horizon.

- Consequently, the SNB reiterated at its March monetary policy meeting that it is still far away from an exit from the minimum-rate policy. Concerning the strong housing market dynamics, the SNB is relying on other non-conventional measures. Tighter capital rules and bank self-regulation have already been implemented. And in February, the SNB initiated the activation of the countercyclical buffer at 1% of risk-weighted residential mortgage loans in order to achieve a preventive effect on housing market dynamics.

LOWER BUT STILL POSITIVE EXPORT EXPECTATIONS



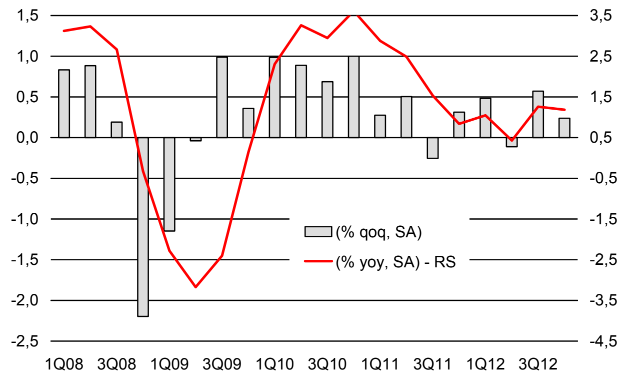
NO INFLATIONARY TENDENCIES



Source: KOF, Thomson Datastream, Feri, UniCredit Research

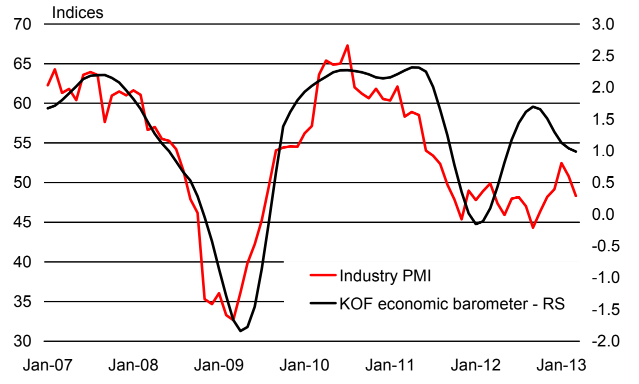
Switzerland

GDP



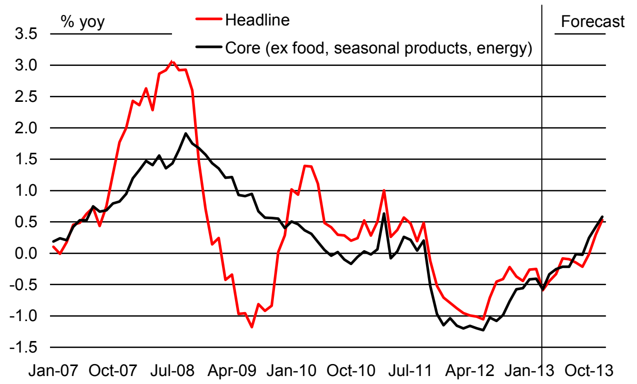
- The Swiss economy maintained positive growth momentum in 4Q12, supported by robust consumption.

BUSINESS SENTIMENT



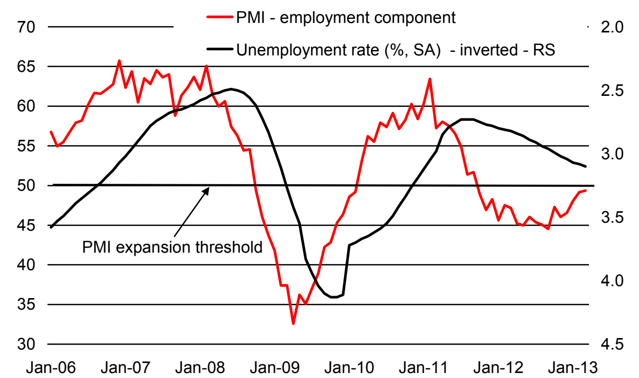
- Despite the latest pronounced correction to the PMI, business sentiment levels continue to signal positive growth dynamics.

INFLATION



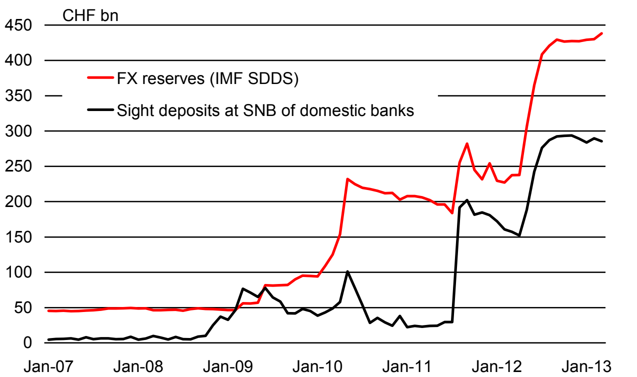
- Swiss inflation fell to -0.6% yoy in March, driven by lower energy prices.

LABOR MARKET



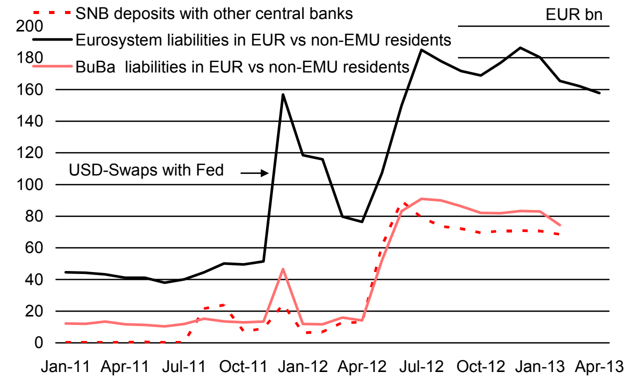
- Employment plans in industry improved to just below the 50-threshold, supporting the overall robust labor market situation.

FX RESERVES



- The rise in the SNB's FX reserves on a CHF basis in March was driven by the stronger USD, not by new currency purchases.

FX CURRENCY MANAGEMENT



- A large amount of the EUR reserves purchased in 2012 is still parked at central banks and will be invested only gradually.

Source: SECO, KOF, Thomson Datastream, Bloomberg, UniCredit Research

Russia

Artem Arkhipov,
Head of Macroeconomic Analysis and Research (UniCredit Russia)
+7 495 258-7258 ext. -7558
Artem.Arkhipov@unicredit.ru

Olga Ponomarenko (UniCredit Russia)
+7 495 258-7258
olga.ponomarenko@unicredit.ru

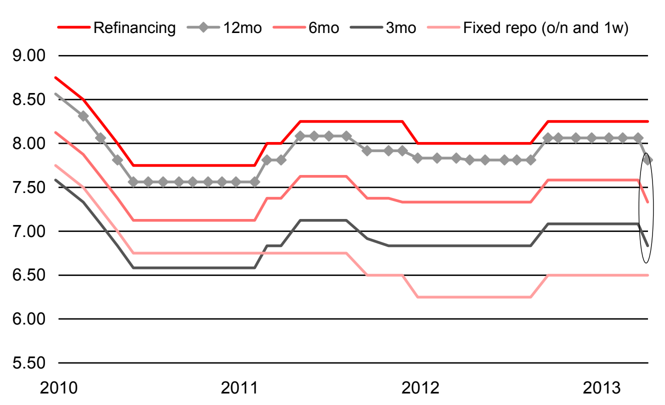
- The easing cycle has been launched. The CBR cut long-term (3-12 months) rates at its latest meeting in early April. Even though the long-term operations make up only less than 25% of CBR's refinancing volumes, this segment is likely to be increasing further as the collateral shortage will induce banks to use forms of refinancing other than overnight and 1-week repo. As was previously indicated by Chairman Ignatiev, the CBR would start cutting rates when inflation started decelerating. In March, CPI slowed down to 7% from 7.3% yoy in February, although it still remained above the 5-6% target range. With the cuts, the CBR indicated it expected inflation to return to the target range over the medium term.

  We expect the easing cycle to last for at least a quarter. New Chairwoman Nabiullina takes office at the end of June, and she repeatedly emphasized that her nomination implied 'policy continuity'. This makes us anticipate cuts in July and probably further down the road. Under our base-case scenario, we expect 50-75bp cuts in the long term and refinancing rates first, with a 25-50bp reduction in the key overnight repo auction rate following thereafter – probably at the hands of the new CBR head.

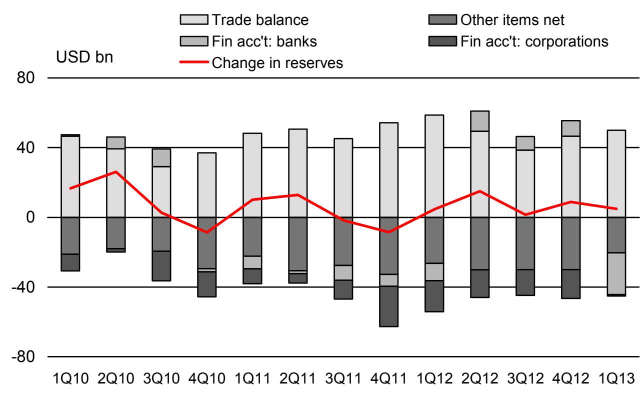
- The MinFin announced that it would buy FX for the Reserve Fund from the market in 2H13. The Ministry used to convert RUB into currency through the balance sheet operations of the CBR, and without any effect on the market. This year, the MinFin transferred some RUB 800bn into the Reserve Fund. So the market might see strong demand for currency: for example, the CBR sells RUB 2-5bn in FX interventions if the ruble appreciates by 0.5-1RUB/basket to drive it back to the middle of the target range. The lack of clarity and the perception of the MinFin as a structural buyer for the ruble drive the currency towards depreciation.

  This will add to the ruble's untypical weakness in 1Q, which is related to the weaker current account that lost some 30% yoy of its surplus, and banks' accumulation of assets abroad. That said, over 2013 we see the government as the main driving force for the balance of payments. Apart from the MinFin's FX purchases, we see two major factors. **1.** Euroclearability of corporate bonds could become a supporting factor for the ruble. **2.** A budget deficit might result in high dividend payouts of the state-controlled enterprises and/or accelerated privatization. While the former is a drag on the ruble (especially in June and September), the latter is likely to be positively perceived by the foreign investors.

THE EASING CYCLE STARTS WITH THE LONG END



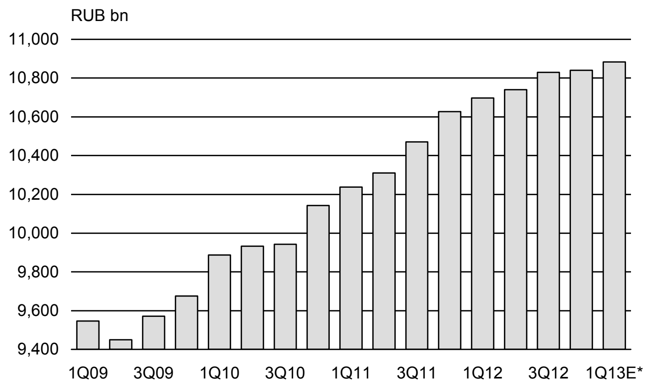
IT IS THE GOVERNMENT WHICH WILL AFFECT BOP IN 2013



Source: Bank of Russia, Customs Service, UniCredit Research

Russia

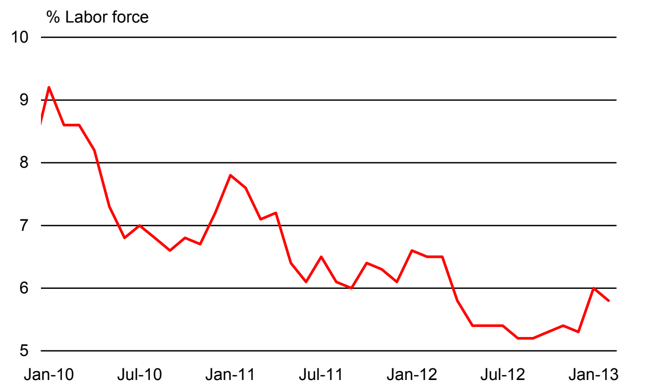
GDP (SEASONALLY-ADJUSTED QUARTERLY DATA)



*MinEcon estimate

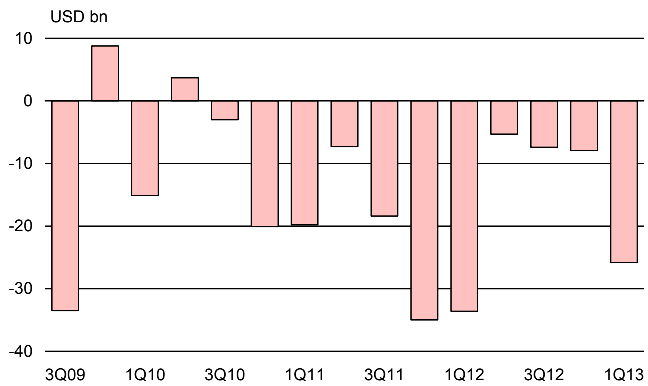
- Weaker domestic demand and stagnating exports are weighing on GDP that was estimated to have grown only 1% yoy in 1Q.

UNEMPLOYMENT



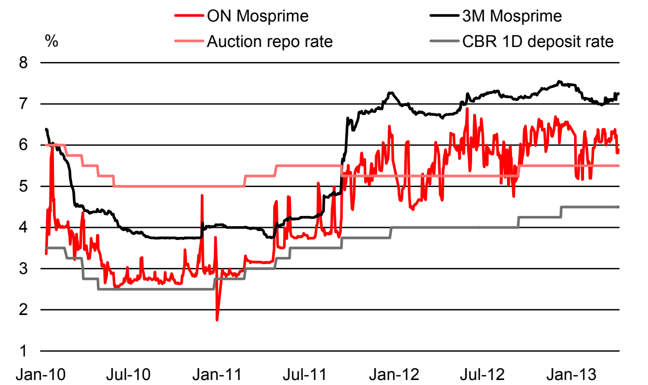
- However, unemployment remains far below historical levels.

CAPITAL OUTFLOW



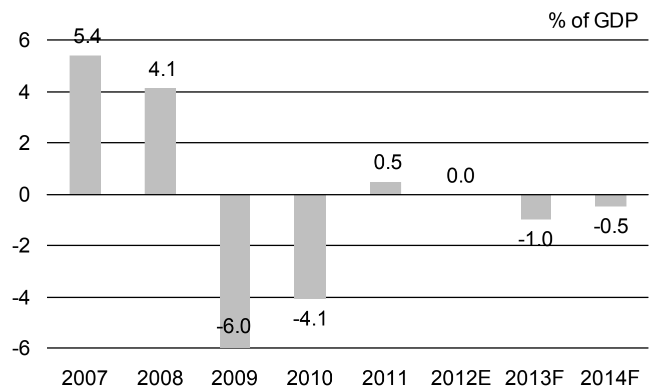
- Capital outflows are back to last year's levels, mostly driven by banks.

MONEY MARKET RATES



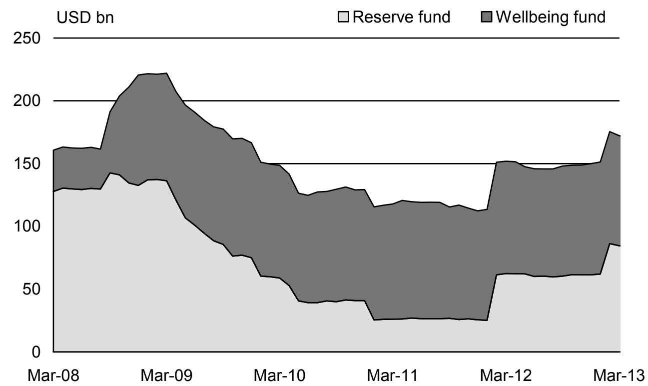
- The CBR provided some relief on the longer end, but overnight rates are still dominated by liquidity withdrawals of the budget.

BUDGET BALANCE



- While the Federal budget balance is likely to come in line with the fiscal rule, regional budgets are coming under pressure.

STATE FUNDS ACCUMULATION



- The difference between USD 110/bbl (base case) and 91/bbl cutoff price implies Reserve Fund will receive almost as much as in 2012.

Source: Ministry of Finance, Bloomberg, Bank of Russia, Federal Statistics Service, UniCredit Research

Turkey

Gillian Edgeworth,
Chief EEMEA Economist
(UniCredit Bank London)
+44 207 826-1772
gillian.edgeworth@unicredit.eu

Carlos Ortiz,
Economist
(UniCredit Bank London)
+44 20 7826-1228
carlos.ortiz@unicredit.eu

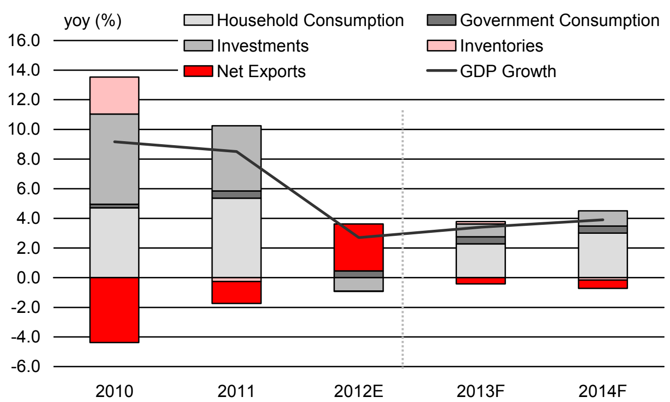
- The Turkish economy has had a number of pieces of data in the past month that come against April's aggressive 50bp policy rate cut. Inflation for March came in above expectations at 7.3% yoy. This can be attributed to food prices, but it does not escape the fact that the H and I indices of core inflation stood at 6.3% and 5.8% yoy, respectively. On a 3M/3M sa and annualized basis, both measures of core inflation accelerated (by 6.9% and 6.6%, respectively). With this in mind, it becomes very unlikely that the CBT will manage to slow inflation sufficiently over the rest of this year to meet either its projection of 5.3% or its target of 5.0%. This will certainly increase pressure to revise its projection upwards in its next inflation report, expected at the end of this month.

- Recent PMI data is also not all bad. The manufacturing PMI fell in both February and March, while the detail was not particularly encouraging. On a more positive note, the 1Q average was still almost one point higher than in 4Q, while the PMI has been above its long term average for seven consecutive months. The PMI suggests that the 1.6% mom gain in IP posted for February should be followed by further gains in the months ahead.

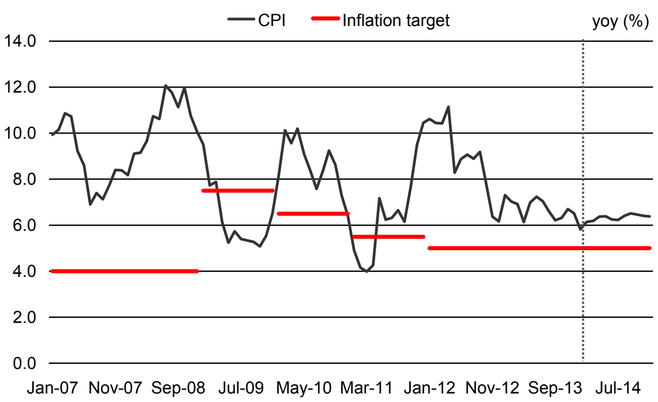
- February C/A data was weak. For the second consecutive month, the C/A deficit was wider than for the same period last year. YTD the deficit stands at USD 10.9bn, up 0.9bn from the first two months of 2012. The energy deficit is no longer widening but the 12-month gold surplus is down USD 1.0bn in the last two months to USD 4.7bn. The C/A deficit, less gold and energy, is also beginning to widen again, capturing a slowdown in exports but an acceleration in imports. Within the financing component, the composition also remains weak. We estimate short-term capital inflows in February at USD 6.5bn compared with long-term inflows at USD 0.6bn. Over the past 12 months, 80% of all C/A financing has been short term.

- Despite all of the above, uncertainty on the pace of GDP growth is an increasing concern, in particular for the government. Headline GDP data in 4Q, at 2.2% yoy, was not welcome. There were positives in the detail, including good export performance and a drag from inventories, but this was not sufficient to stop the government from increasing public pressure on the CBT to act. Of more concern to us is the balance between domestic and external demand. Any recovery in domestic demand needs to be accompanied by an improvement in industry and exports if the C/A deficit and TRY are not to be put at (further) risk. However, an uncertain global backdrop remains, while the government's concerns are centered on headline growth rather than its composition.

GDP GROWTH TO RECOVERY GRADUALLY



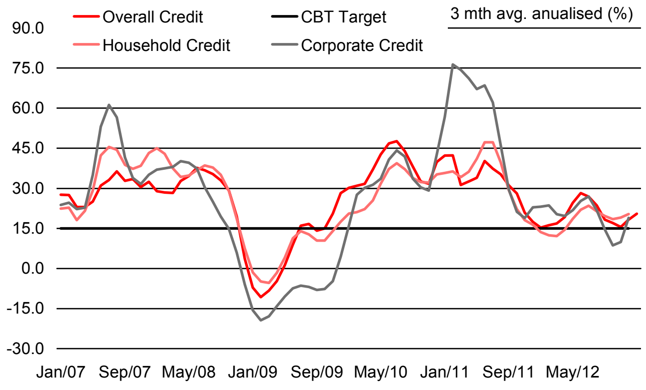
INFLATION REMAINS OFF TARGET



Source: CBT, TurkStat, UniCredit Research

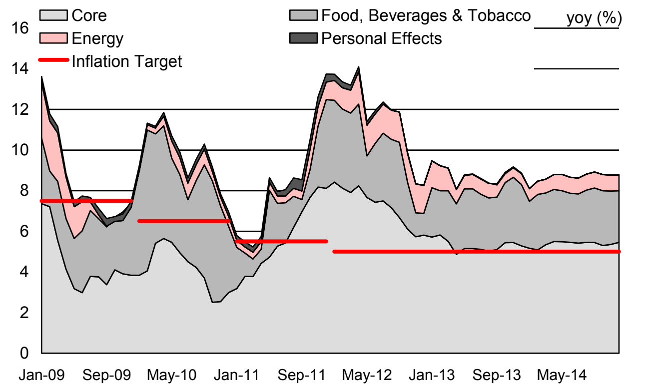
Turkey

CREDIT GROWTH VS. TARGET



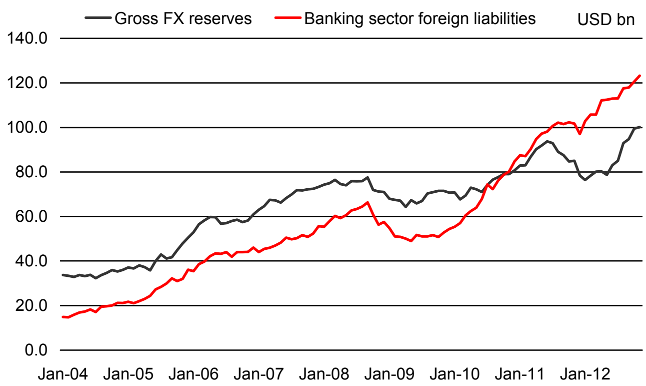
■ The impact of slowing credit growth has fed through to domestic demand.

DIFFERENT CONTRIBUTIONS TO INFLATION VS. TARGET



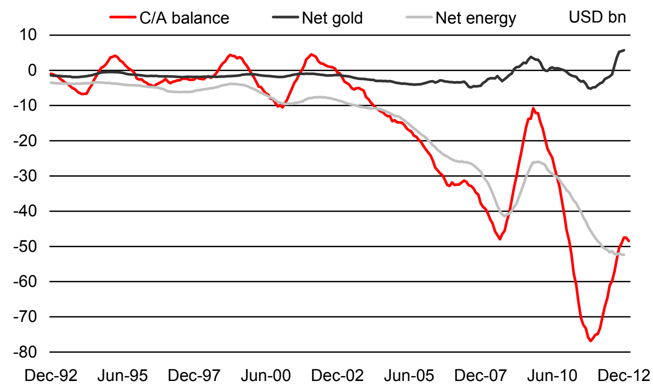
■ Inflation this year will remain above target on account of rising food prices.

FX RESERVES VS. EXTERNAL BANK BORROWING



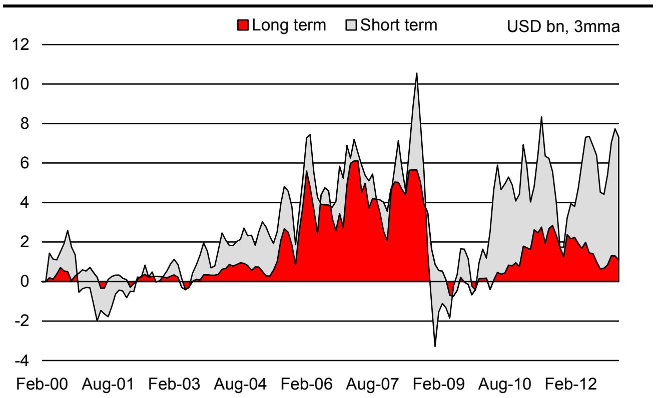
■ FX reserves cannot keep pace with external bank borrowing.

C/A BALANCE



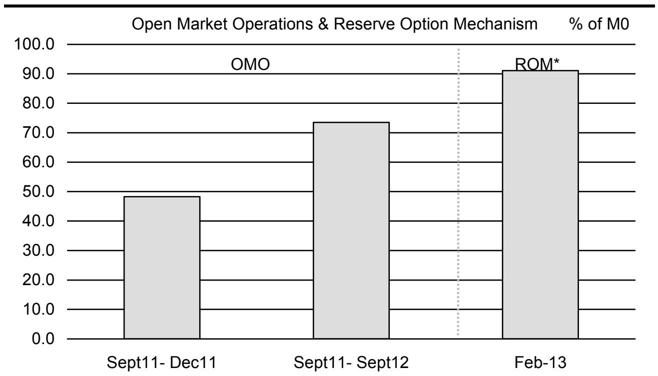
■ The C/A deficit less gold and energy is beginning to widen again, capturing a slowdown in exports and acceleration in imports.

FOREIGN CAPITAL INFLOWS



■ Over the past 12 months, 80% of all C/A financing has been short term.

OMO VS. ROM ON FX & GOLD



*ROM includes both FX and Gold Reserve Requirements

■ Via its ROM, related both to FX and gold, the CBT has the potential to absorb 90% of M0, well above that via OMOs.

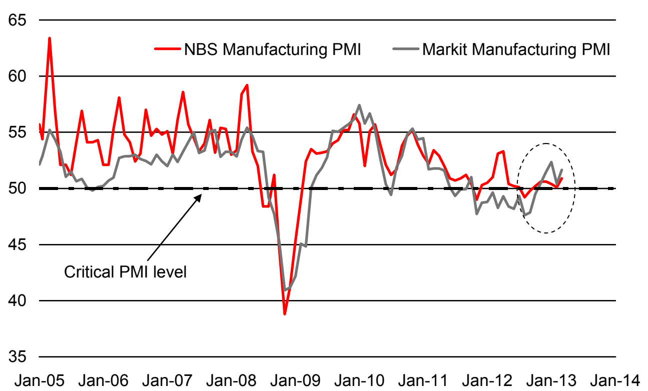
Source: CBT, TURKSTAT, UniCredit Research

China

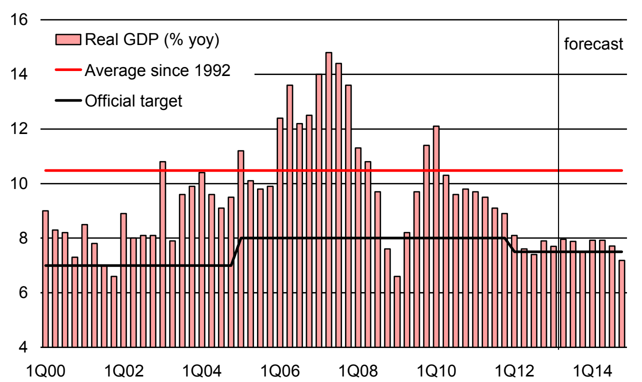
Nikolaus Keis, Economist (UniCredit Bank)
+49 89 378-12560
nikolaus.keis@unicreditgroup.de

- China's most recent data activity came in on a weaker note, showing that the recovery eased in (late) 1Q13. Real GDP over the first three months of the year grew by a less-than-expected 7.7% yoy (4Q12: +7.9%; 2012: +7.8%). With no detailed quarterly breakdown available so far, monthly figures imply that private sector spending, the core segment targeted by the "new" development strategy, is still lagging.
- Retail sales, although holding up well in March, fell 3pp in 1Q13 versus 4Q12, partly because of the government's recent attempt to reduce excessive banqueting and gift-giving. Capex spending is lagging, too, showing that the substantially increased liquidity over the last six months did not fuel corporate investment activity. Weak final domestic demand, ample spare capacity and the destocking process not yet finished caused March industrial production growth to slide further into single-digit territory (8.9% yoy versus 10% earlier this year).
- It was, therefore, still the "old-fashioned" pattern fueling economic growth. State-mandated infrastructure investment soared to 25% yoy so far this year (4Q12: +15%), nominal export growth roughly doubled to a hard-to-believe 20%, while housing activity accelerated on the back of further rising house prices – although March property investment showed some (insufficient) slowdown following the step-up in restrictive measures over recent months.
- While staying restrictive on housing as well as on local government spending and shadow banking in order to further reduce house price and financial risks, more policy accommodation is still needed for the recovery to gain traction again. Chinese authorities already hinted at further (selective) steps to boost private consumption. Furthermore, monetary policy will not be tightened any time soon (as some analysts have speculated).
- A supportive economic policy as well as upcoming restocking needs is the main reason why we still expect the economy to gain some more traction, with real GDP growth accelerating to the 8%-region up until this summer. This is also underpinned by again improving survey results like the NBS's quarterly business climate and entrepreneur confidence indices or PMIs readings. But economic growth should level off thereafter, as a gradually improving global economy will roughly be balanced by the recent step-up in measures to rein in house price increases and financial risks, both of which are increasingly weighing on domestic demand.
- Nevertheless given the slower start to the year and weaker momentum carrying over to 2Q13, we revise down our full year GDP forecasts from 8% to 7¾% in 2013/14.

BUSINESS CLIMATE IS STILL IMPLYING A MODEST RECOVERY...



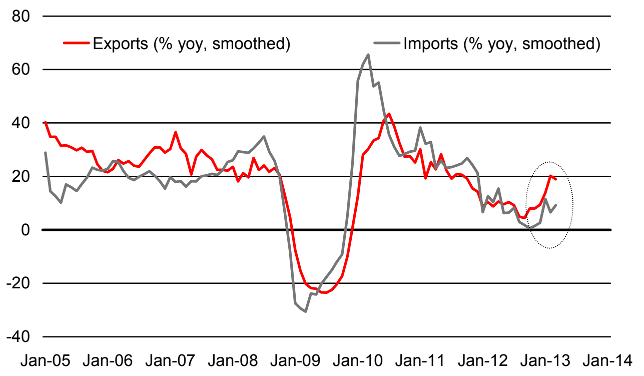
...WITH GDP GROWTH TO FLUCTUATE IN THE 7½%-8% REGION



Source: Thomson Datastream, Feri, UniCredit Research

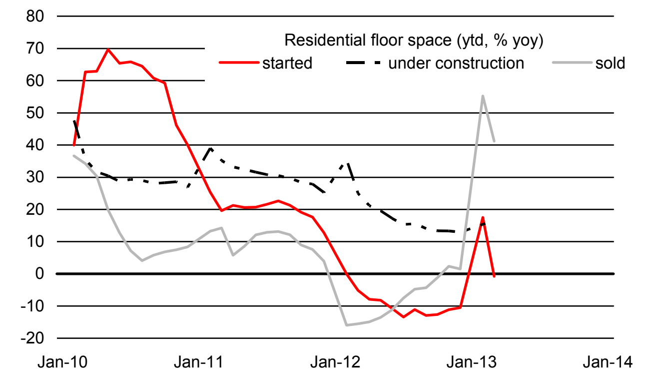
China

EXTERNAL ECONOMY



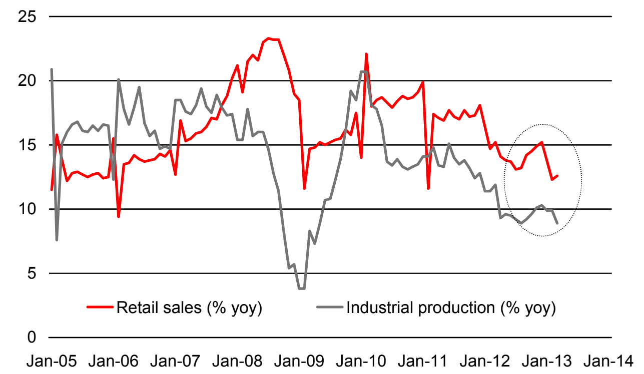
- Nominal exports soared earlier this year to hard-to-believe levels, but started to normalize more recently.

HOUSING



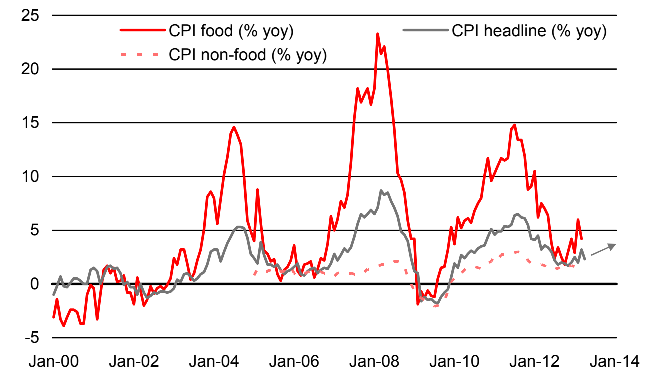
- Housing strengthened significantly (as did public investment), but weakened more recently after rules & restrictions were tightened.

RETAIL SALES AND INDUSTRIAL PRODUCTION



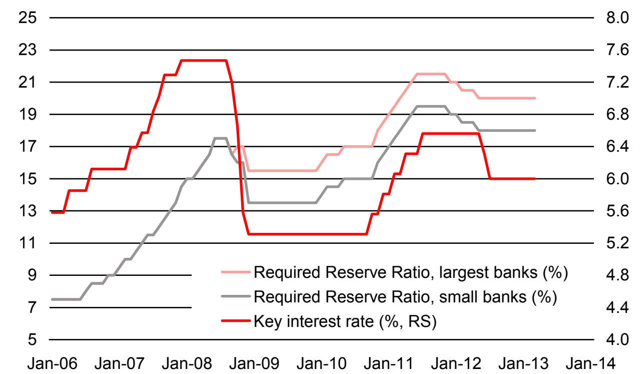
- Nevertheless, private and business spending are still lagging, thus further delaying a weak and bumpy economic recovery.

CPI



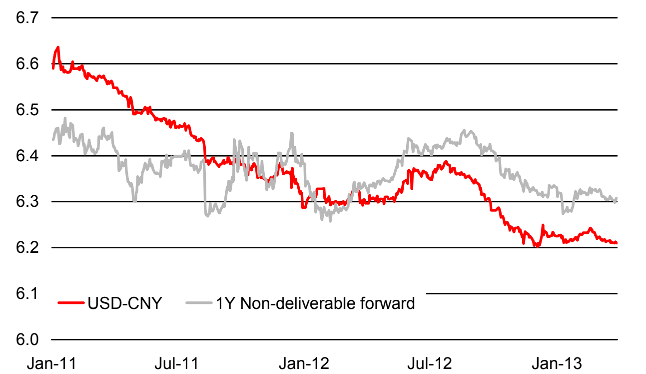
- Disinflation has come to an end, with food and housing driving CPI higher. But price pressure will not be worrying...

MONETARY POLICY



- ...so that the central bank can remain on the sidelines with its interest rate policy. However, credit measures will be tightened.

USD-CNY

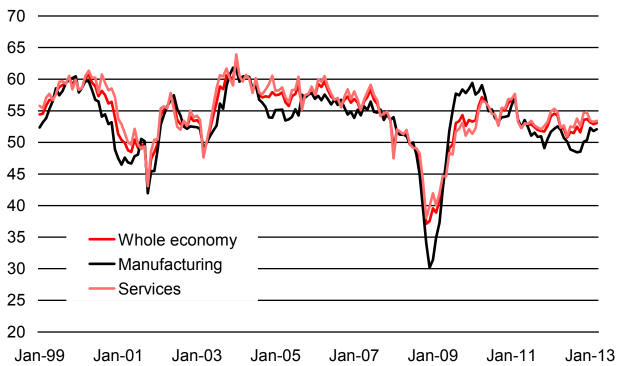


- After fluctuating sideways over recent months, the CNY resumed its appreciation trend, not least on the back of a weakening JPY.

Source: Thomson Datastream, Feri, UniCredit Research

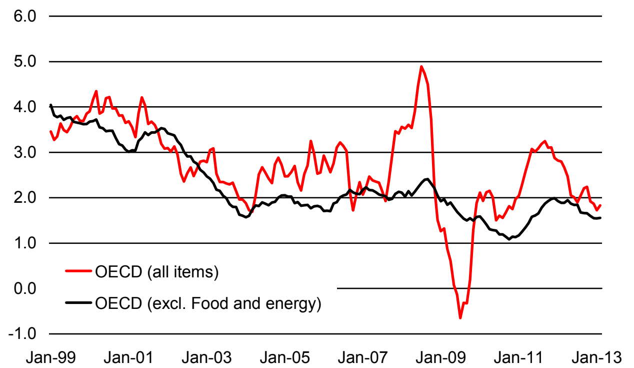
Global indicators

GLOBAL PMI OUTPUT



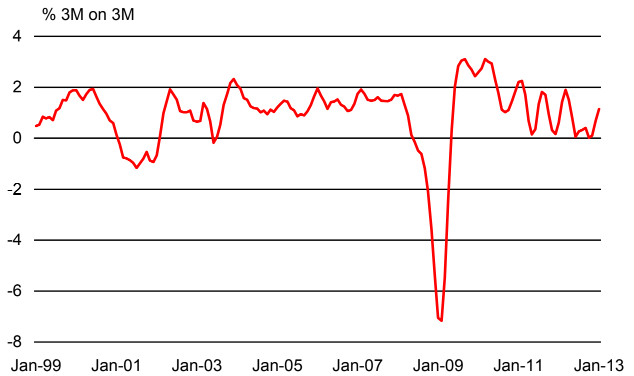
- The global composite PMI edged up from 52.9 to 53.1 in March. The manufacturing output index rose from 51.8 to 52.1, while the services index was up from 53.2 to 53.4.

CPI INFLATION



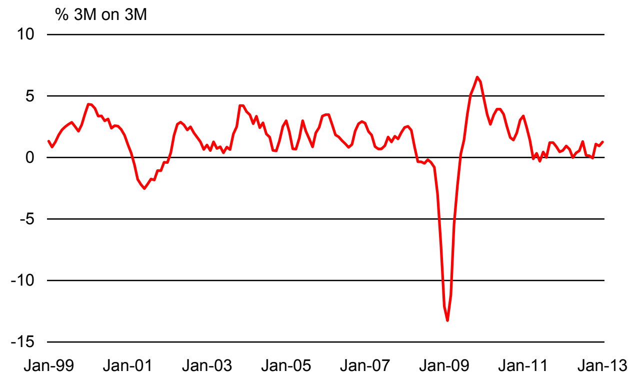
- Headline inflation in OECD economies edged up from 1.7% yoy to 1.8% yoy in February, while the core rate accelerated from 1.5% yoy to 1.6% yoy.

INDUSTRIAL PRODUCTION



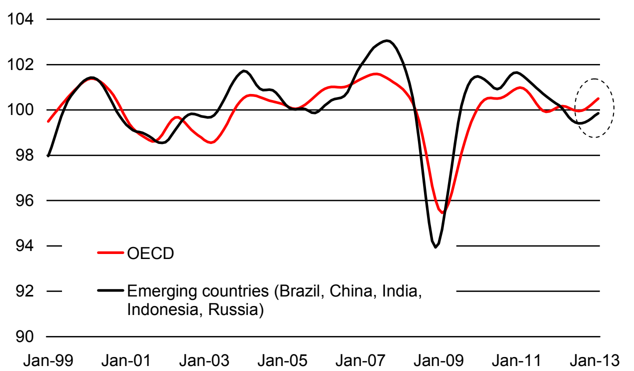
- Global IP was unchanged in January. The 3M/3M rate accelerated from 0.7% to 1.1%.

WORLD TRADE



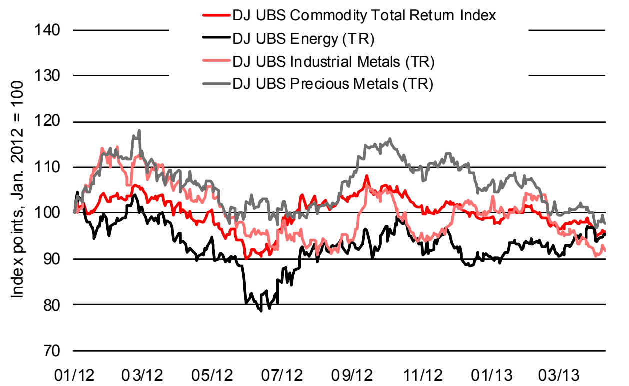
- World trade rose 1.9% mom in January. The 3M/3M rate accelerated from 0.9% to 1.3%.

OECD COMPOSITE LEADING INDICATORS



- OECD leading indicators for the OECD and emerging economies (aggregated) edged up further in March.

COMMODITIES



- We expect only a sideways movement in the Brent oil price over the next two years, due to stronger supply from North America (shale oil) and Iraq. Precious metals will remain in an upward trend.

Source: CBP Netherlands, OECD, UniCredit Research

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f) Zagrebačka banka d.d., Trg bana Jelačića 10, HR-10000 Zagreb, Croatia
Regulatory authority: Croatian Agency for Supervision of Financial Services, Miramarska 24B, 10000 Zagreb, Croatia

g) UniCredit Bank Czech Republic (UniCredit Bank Czechia), Na Príkope 858/20, CZ-11121 Prague, Czech Republic
Regulatory authority: CNB Czech National Bank, Na Příkopě 28, 115 03 Praha 1, Czech Republic

h) Bank Pekao, ul. Grzybowska 53/57, PL-00-950 Warsaw, Poland
Regulatory authority: Polish Financial Supervision Authority, Plac Powstańców Warszawy 1, 00-950 Warsaw, Poland

i) ZAO UniCredit Bank Russia (UniCredit Russia), Prechistenskaya emb. 9, RF-19034 Moscow, Russia
Regulatory authority: Federal Service on Financial Markets, 9 Leninsky prospekt, Moscow 119991, Russia

j) UniCredit Bank Slovakia a.s. (UniCredit Slovakia), Šancova 1/A, SK-813 33 Bratislava, Slovakia
Regulatory authority: National Bank of Slovakia, Imricha Karvaša 1, 813 25 Bratislava, Slovakia

k) UniCredit Tiriac Bank (UniCredit Tiriac), Bucharest 1F Expozitiei Boulevard, RO-012101 Bucharest 1, Romania
Regulatory authority: National Bank of Romania, 25 Lipscani Street, RO-030031, 3rd District, Bucharest, Romania

l) ATF Bank, 100 Furmanov Str., KZ-050000 Almaty, Kazakhstan
Agency of the Republic of Kazakhstan on the state regulation and supervision of financial market and financial organisations, 050000, Almaty, 67 Aiteke Bi str., Kazakhstan

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UniCredit Research*

Michael Baptista
Global Head of CIB Research
+44 207 826-1328
michael.baptista@unicredit.eu

Dr. Ingo Heimig
Head of Research Operations
+49 89 378-13952
ingo.heimig@unicreditgroup.de

Economics & FI/FX Research

Erik F. Nielsen, Global Chief Economist
+44 207 826 1765
erik.nielsen@unicredit.eu

Economics & Commodity Research

European Economics

Marco Valli, Chief Eurozone Economist
+39 02 8862-8688
marco.valli@unicredit.eu

Dr. Andreas Rees, Chief German Economist
+49 89 378-12576
andreas.rees@unicreditgroup.de

Stefan Bruckbauer, Chief Austrian Economist
+43 50505-41951
stefan.bruckbauer@unicreditgroup.at

Tullia Bucco, Economist
+39 02 8862-2079
tullia.bucco@unicredit.eu

Chiara Corsa, Economist
+39 02 8862-2209
chiara.corsa@unicredit.eu

Dr. Loredana Federico, Economist
+39 02 8862-3180
loredana.federico@unicredit.eu

Mauro Giorgio Marrano, Economist
+39 02 8862-8222
mauro.giorgiomarrano@unicredit.eu

Alexander Koch, CFA
+49 89 378-13013
alexander.koch1@unicreditgroup.de

Chiara Silvestre, Economist
chiara.silvestre@unicredit.eu

US Economics

Dr. Harm Bandholz, CFA, Chief US Economist
+1 212 672-5957
harm.bandholz@unicredit.eu

China Economics

Nikolaus Keis, Economist
+49 89 378-12560
nikolaus.keis@unicreditgroup.de

Commodity Research

Kathrin Goretzki, Economist
+49 89 378-15368
kathrin.goretzki@unicreditgroup.de

Jochen Hitzfeld, Economist
+49 89 378-18709
jochen.hitzfeld@unicreditgroup.de

EEMEA Economics & FI/FX Strategy

Gillian Edgeworth, Chief EEMEA Economist
+44 207 826-1772
gillian.edgeworth@unicredit.eu

Artem Arkhipov, Head, Macroeconomic Analysis and Research, Russia
+7 495 258-7258
artem.arkhipov@unicredit.ru

Anca Maria Aron, Economist, Romania
+40 21 200-1377
anca.aron@unicredit.ro

Dan Bucşa, Economist
+44 207 826-7954
dan.bucsa@unicredit.eu

Hrvoje Dolenec, Chief Economist, Croatia
+385 1 6006 678
hrvoje.dolenec@unicreditgroup.zaba.hr

Hans Holzhacker, Chief Economist, Kazakhstan
+7 727 244-1463
h.holzhacker@atfbank.kz

Ľubomír Koršňák, Chief Economist, Slovakia
+421 2 4950 2427
lubomir.korsnak@unicreditgroup.sk

Catalina Molnar, Chief Economist, Romania
+40 21 200-1376
catalina.molnar@unicredit.ro

Marcin Mrowiec, Chief Economist, Poland
+48 22 656-0678
marcin.mrowiec@pekao.com.pl

Carlos Ortiz, Economist, EEMEA
+44 207 826-12288
carlos.ortiz@unicredit.eu

Mihai Patrulescu, Senior Economist, Romania
+40 21 200-1378
mihai.patrulescu@unicredit.ro

Kristofor Pavlov, Chief Economist, Bulgaria
+359 2 9269-390
kristofor.pavlov@unicreditgroup.bg

Pavel Sobisek, Chief Economist, Czech Republic
+420 955 960-716
pavel.sobisek@unicreditgroup.cz

Dmitry Veselov, Ph.D., Economist, EEMEA
+44 207 826-1808
dmitry.veselov@unicredit.eu

Global FI Strategy

Michael Rottmann, Head, FI Strategy
+49 89 378-15121
michael.rottmann1@unicreditgroup.de

Dr. Luca Cazzulani, Deputy Head, FI Strategy
+39 02 8862-0640
luca.cazzulani@unicredit.eu

Chiara Cremonesi, FI Strategy
+44 20 7826-1771
chiara.cremonesi@unicredit.eu

Elia Lattuga, FI Strategy
+39 02 8862-2027
elia.lattuga@unicredit.eu

Kornelius Purps, FI Strategy
+49 89 378-12753
kornelius.purps@unicreditgroup.de

Herbert Stocker, Technical Analysis
+49 89 378-14305
herbert.stocker@unicreditgroup.de

Global FX Strategy

Dr. Vasileios Gkionakis, Global Head, FX Strategy
+44 207 826-7951
vasileios.gkionakis@unicredit.eu

Armin Mekelburg, FX Strategy
+49 89 378-14307
armin.mekelburg@unicreditgroup.de

Roberto Mialich, FX Strategy
+39 02 8862-0658
roberto.mialich@unicredit.eu

Publication Address

UniCredit Research
Corporate & Investment Banking
UniCredit Bank AG
Arabellastrasse 12
D-81925 Munich
Tel. +49 89 378-18927

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www.research.unicreditgroup.eu

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