

Friday Notes

August 22, 2008

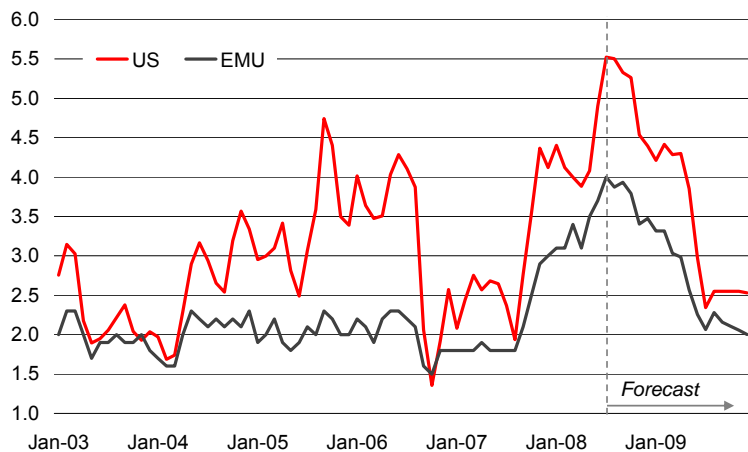
Economics & Commodity Research

Inflation: No all-clear yet

- **Relief.** The consolidation in commodity prices, first and foremost crude oil, is bringing relief on the inflation front. The direct effects should push the August inflation numbers in the eurozone, scheduled for release at the end of next week, below the recent highs.
- **Pressure.** It is, however, definitely too soon to sound the all-clear. Even though inflation should now have peaked, commodity prices remain high, suggesting further limited pass-through effects in the coming months (pages 7-9). In the US, the core rate will likely still even edge slightly higher (pages 4-6).
- **Risk.** We think it will be next spring before we see noticeable relief for inflation. Until then, the annual rate will probably moderate only gradually. Above all in the eurozone, wage demands should, therefore, remain very high, thereby eliciting continuing warnings from the ECB on second-round effects.
- **Dampener.** Support for the inflation watch-dogs is coming from cyclical downward forces. The US labor market has been weakening for some time now, in the eurozone the trend reversal appears to have been completed, and even the strong labor market upswing in Germany will probably run out of steam soon (pages 10-12), thereby reducing the probability of excessive wage settlements.
- **Further topics:**
 - **Weekly Comment:** Just a breather (page 2).
 - **Data outlook:** EMU: Renewed decline in the business climate; US: House prices continue to fall (page 13).
 - **Market outlook:** EUR/USD stabilizes (page 23).

IT WILL TAKE TIME FOR INFLATION TO COME DOWN

Consumer prices in %, y-o-y



Source: Thomson Datastream, UniCredit Global Research

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MIB MACRO FORECASTS

in % y-o-y	2007	2008	2009
GDP EMU	2.6	1.4	1.0
CPI EMU	2.1	3.7	2.6
GDP Germany	2.6	1.7	0.9
CPI Germany	2.3	2.8	1.8
GDP Italy	1.4	0.1	0.4
CPI Italy	1.8	3.6	2.6
GDP US	2.2	1.6	1.4
CPI US	2.9	4.5	3.1

MIB FI/FX FORECASTS

2008/09	30-Sept	31-Dec	31-Mar	30-June
EMU 3M	4.96	4.95	4.80	4.65
EMU 10Y	4.15	4.10	4.00	3.90
US 3M	2.85	3.05	3.50	3.65
US 10Y	4.10	4.20	4.30	4.40
EUR-USD	1.49	1.45	1.42	1.38
USD-JPY	111	112	113	115
Oil Price	122	125	120	135

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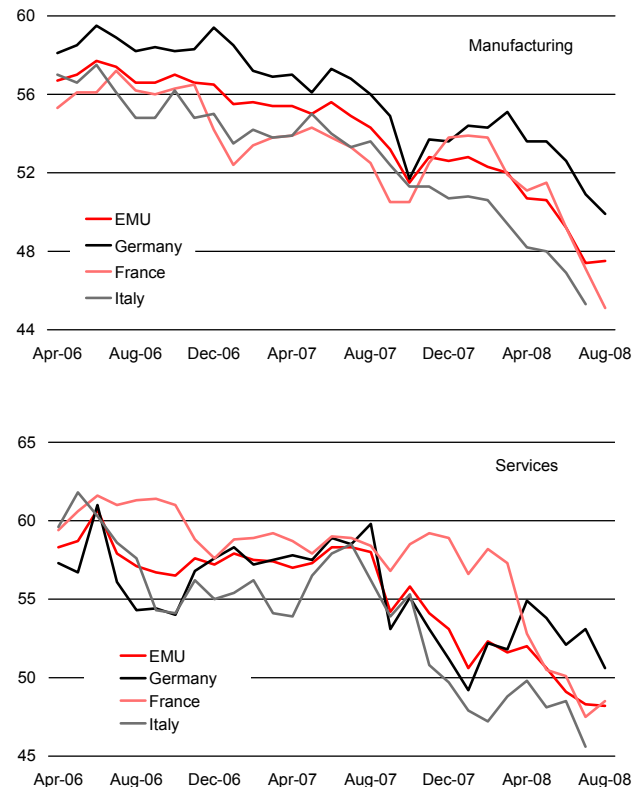
Just a breather

Eurozone PMI data confirmed that the eurozone is flirting with a technical recession. Our baseline forecast suggests that this embarrassment should be narrowly avoided, but the pain on the real economy cannot be, and the ECB will still need to lower its growth projections next month. With the correction in commodity prices already starting to cool inflationary pressures, it is increasingly evident that the next rate move will be down - even though ECB rhetoric indicates that this is unlikely to happen before Q2 next year. Rate cuts should materialize sooner in the UK, where uncertainty on the timing and magnitude of monetary easing is, however, much higher. The USD rally has taken a breather, as renewed concerns on Fannie and Freddie have come as a painful reminder of the unresolved fragilities in the housing and financial sector; oil prices have recouped some of their recent losses, hand in hand with the USD movement. After the sharp turn in sentiment of the last few weeks, markets are taking a step back to reassess the relative value bet on US versus eurozone (and much of the rest the world) as well as the directional bet on whether the global economy is headed for a soft landing or a belated crash. I would still bet on a soft landing, and on a renewed downward trend in EUR/USD and oil prices. US dollar and oil had bolted too fast and a consolidation was in order - but this is just a breather before the long-distance challenge. This weekend the markets will look to Jackson Hole for guidance from US policy-makers. I expect the key message to remain the same: hawkish but unhurried on monetary policy, more emphasis and urgency on targeted measures to support housing and finance, and concerned recognition of the fact that the economic outlook remains extremely difficult to decipher.

August PMIs dropped further in Germany and France, undershooting market expectations, but the Eurozone PMIs stabilized, a positive and puzzling surprise suggesting that either Spain or/and Italy have rebounded, or the Eurozone is really more than the sum of the parts... French manufacturing was particularly disappointing (a 2 percentage point drop), confirming that France is joining Italy and Spain in a slump. Germany's manufacturing PMI dropped below the critical 50 threshold with the fourth decline in five months; together with a sharp drop in the services index, this signals a very high probability that the Ifo will fall further next week. Overall, the data confirm the picture of an inexorable slow-down in all the main Eurozone countries, as consumers batten down the hatches and foreign demand weakens, leading firms to scale back investment plans. Our proprietary EMU composite indicator points to +0.1% growth in Q3, which would spare us the embarrassment of a technical recession but would still force the ECB to lower its growth forecasts next month. Moreover, this +0.1% baseline is still uncomfortably close to a dip in negative territory.

ONGOING WEAKNESS

PMIs



Source: Feri, UniCredit Global Research

Input prices decelerated markedly, confirming that the correction in commodity prices is cooling inflationary pressures before any meaningful second round effects have had a chance to show up in core inflation. ECB officials meanwhile are ratcheting up the anti-inflation rhetoric, a strong signal that they will not lower their guard until they are confident that the commodity price correction is sustained and that price pressures already in the pipelines will not feed through into the core rate. I believe this is the right strategy, although I remain concerned that the insistent denials that slowing growth will help cool inflation may harm the ECB's credibility.

Today's data seem to confirm that swings in commodity prices tend to feed through much more quickly into inflation and inflation expectations than into activity indicators. If that is the case, we should see a significant decline in headline inflation accompanied by a persistent further weakening of GDP growth before lower energy and food prices start cushioning the fall and preparing the ground for a recovery. The next ECB move will have to be a cut. On current data and ECB rhetoric trend, Q2 next year still seems the best bet.

The Bank of England has provided a much more pragmatic, balanced and candid assessment of the balance of risks to growth and inflation, both in the August MPC minutes released yesterday and in the latest inflation report. The BOE has warned that short-term risks to both inflation and growth have worsened, with producer prices on an upswing, sharp rises in utility tariffs in the pipeline, and a rapid deterioration in housing and credit conditions. The Bank has also shown it takes inflation risks very seriously, with one MPC member actually voting for an immediate rate hike (ECB-style) to preempt second round effects. At the same time, however, the BOE seems more confident that the weakening labor market should continue to keep wage pressures at bay, and has openly recognized the risk that a worse-than-forecast plunge in economic activity might push inflation well below target in the medium term. Unusual volatility in some data (see the bounce in July retail sales) complicates the policy assessment further, but in the UK as well the next rate move will have to be a cut, most likely in January.

Uncertainty on the timing and magnitude of UK rate moves is, I believe, much higher than in the eurozone. The policy rate starts at a higher level, and the economy is in much more desperate need of help. Should inflation decline faster than expected, or the labor market deteriorate at an accelerating pace, we might see a faster and deeper easing cycle than is currently priced in, and in that scenario the downside for sterling would widen significantly even after the recent losses.

The USD is taking a breather, as the less gloomy eurozone PMI releases coincide with heightening concerns on the fate of Fannie and Freddie. The GSE's (Government Sponsored Enterprises) woes underscore the two critical vulnerabilities of the US economic outlook: a housing sector that has not yet touched bottom, and a beleaguered financial sector. The US outlook remains particularly uncertain, and it is not surprising that after a sharp repricing of the US vs. eurozone over the last couple of weeks, the market is now stepping back to reassess this relative value trade. I remain of the view that EUR/USD is likely to consolidate just below 1.50 before making another push lower, a move for which the upcoming presidential election could provide the decisive impulse. Oil prices have taken back some of their recent losses, again moving hand in hand with the swing in the USD. I had warned last week that, after the sudden turning point in market sentiment on the USD and on commodities, we were likely to see renewed volatility rather than a smooth adjustment, and I still believe that the downward trend in EUR/USD and oil prices will prevail in the coming months.

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US inflation moderating more slowly than it accelerated

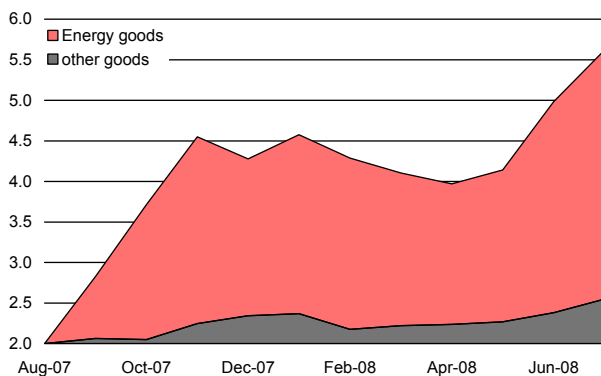
- Rising energy prices have pushed US consumer price inflation to its highest level in 17 years. Unfortunately, inflation is now not moderating as rapidly as it accelerated – despite the correction in oil prices.
- Reasons are that first, gasoline prices have fallen more slowly than crude oil prices. Second, seasonal factors anticipate a decline in gasoline prices, and third, core inflation is likely to accelerate slightly further.
- We think it will be spring before the inflation situation starts to improve sustainably. Core inflation will probably moderate slightly, and headline inflation should even pull back strongly.
- Nevertheless, falling oil prices combined with lower inflation expectations have reduced the near-term pressure for interest rate hikes. The Fed has more time to monitor the development of the economy and financial markets before it finally starts the tightening cycle.

Inflation at 17-year high

In July, the US inflation rate rose to 5.6%, which is the highest reading in 17 years. Since the cyclical low in August 2007 (2.0%), the inflation rate has, therefore, almost trebled. The main reason for this is the surge in energy prices. In July, the energy component of the CPI was up 30% y-o-y, and between April and July it even increased by an annual rate of 80%! Energy prices are, therefore, responsible for 85% of the rise in inflation since August 2007 (cf. chart).

ENERGY PRICES DRIVING INFLATION

Consumer Price Index, in % y-o-y



Source: BLS, Thomson Datastream, UniCredit Global Research

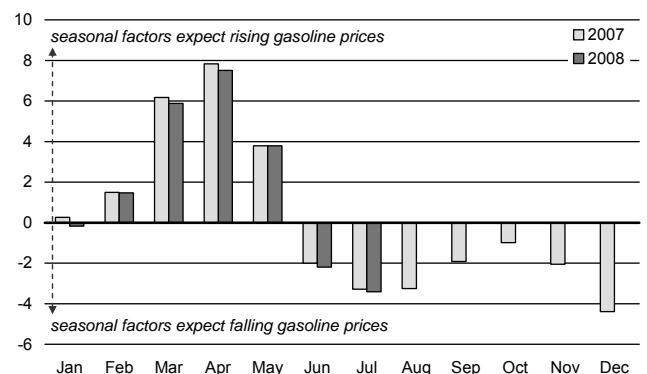
Near-term relief from falling oil prices smaller than hoped for

Against this backdrop, the recent pullback in the price of oil is very reassuring. Since mid-July, for example, the price for a barrel of West Texas Intermediate has fallen by over USD 30, or 22%. Thanks to this development, the inflation situation in the US will moderate – albeit not as rapidly as could be suspected given the strong pullback in the oil price.

Gasoline prices, the most important energy good for US consumers, have, for example, fallen only 9% since mid-July, and the average monthly decline between August and July is even only 6½%. Furthermore, the seasonal factors “expect” gasoline prices to decrease after the driving season. In the past year, the seasonal factor for the month of August was -3¼%. Accordingly, the seasonally-adjusted decline in gasoline prices would be reduced to a meager 3¼%. For the five months between August and December, seasonal factors expect gasoline prices to decline by a total of 12% (cf. chart).

SEASONAL FACTORS EXPECT FALLING GASOLINE PRICES

Seasonal factors for gasoline prices in %



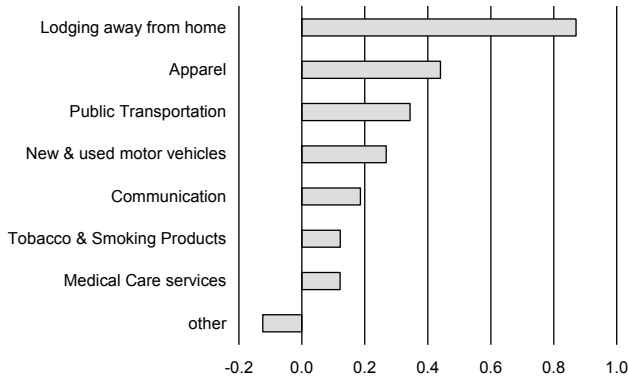
Source: BLS, Thomson Datastream, UniCredit Global Research

Core inflation accelerating

Alongside energy prices, core inflation has also accelerated. In the last three months alone, consumer prices ex food and energy have risen an annualized 3½%; between January and April, the increase was still 1¼%. Above all four sectors are responsible for this acceleration: Lodging away from home, apparel, public transportation and new & used motor vehicles (cf. chart on the next page).

WHICH SECTORS ARE RESPONSIBLE FOR THE RISE IN CORE INFLATION?

Contribution to the rise in the core inflation rate (3M rate) between April and July in percentage points



Source: BLS, Thomson Datastream, UniCredit Global Research

Higher inflation in the public transportation sector (primarily airline fares) reflects the pass-through of high energy prices on to consumers. Indirectly, the higher prices for lodging away from home may also be a result of these more expensive flights. If fewer and fewer households can afford to travel by air and prefer to vacation in the US, that would namely fuel demand for hotels in the US. This explanation is, however, not entirely satisfactory, particularly since higher gasoline prices have also increased the cost of traveling in the US, and they should have lowered the budget for holiday trips in general. The strong increase in apparel prices is likely the result of higher producer and import prices for textiles. It is hard to understand, however, the development of car prices. Since unit sales are still falling in the double digits, there is no rational explanation why prices of new and used motor vehicles are now rising more strongly again than at the beginning of the year.

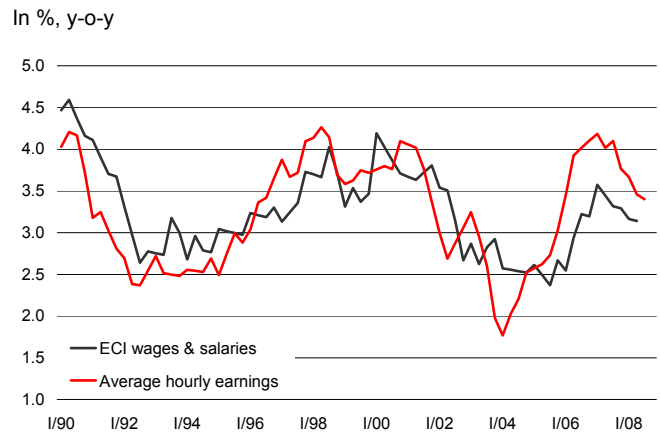
The accelerated increase in consumer prices ex food and energy over the past three months is a burden for the coming months and will see the core inflation rate accelerate further slightly. By the beginning of Q2 2009, we expect the core rate to accelerate to 2¾% from currently 2½%. This development reflects both a (limited) feed-through of the high energy prices and the persisting cost pressure from high producer and import prices for consumer goods.

Relief will begin in spring

Core inflation should then moderate again in the course of Q2 2009. As stated, the feed-through of higher energy prices into the prices of other goods has been rather limited so far. The latest Fed Beige Book corroborates that sluggish domestic demand is making it hard for most companies to pass on higher production costs to consumers. Furthermore, wage

pressure has continued to weaken in recent months. "Thanks" to the weak labor market, there is, therefore, no trace of second-round effects (cf. chart). Finally, the USD has firmed. Against the currencies of the most important trading partners, the USD has appreciated more than 7% since mid-July. That should slow the rise in prices of imported consumer goods.

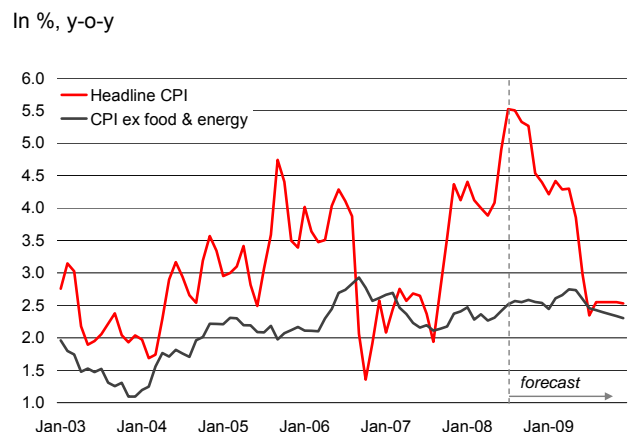
WAGE GROWTH SLOWING



Source: BLS, Thomson Datastream, UniCredit Global Research

Since, at the same time, we expect only a moderate increase (+8%) in energy prices in the coming year, headline inflation will also moderate appreciably. In two stages (because of basis effects), inflation is likely to slow from currently 5.6% to 2½% by mid-2009.

INFLATION HAS PEAKED



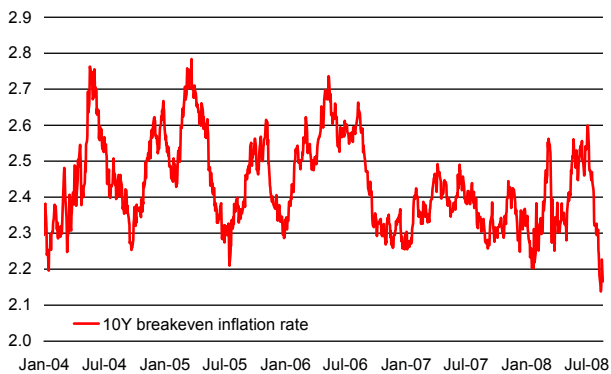
Source: BLS, Thomson Datastream, UniCredit Global Research

Fed remains on hold

Falling energy prices and slower rising wages have, in the short term, taken some of the pressure off the Fed to raise interest rates – despite still rising core inflation. This is all the more true since inflation expectations have weakened across the board in recent weeks. The breakeven inflation rate derived from inflation-indexed bonds (TIPS) even fell to a new five-year low of 2.14% at the beginning of August (cf. chart). But other indicators (Survey of Professional Forecasters, consumer surveys) also demonstrate that inflation expectations have pulled back from their highs.

INFLATION EXPECTATIONS HAVE PLUMMETED

Inflation expectations in %
 (derived from inflation-indexed bonds)



Source: Bloomberg, UniCredit Global Research

As a result, the Fed has more time to monitor the development of the economy and financial markets before finally raising rates. While we expect the first rate move at the end of the current year, we do, however, see the danger of weaker economic data and persisting problems on financial markets postponing the normalization of monetary policy until the beginning of 2009.

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German inflation: Pipeline pressure remains high

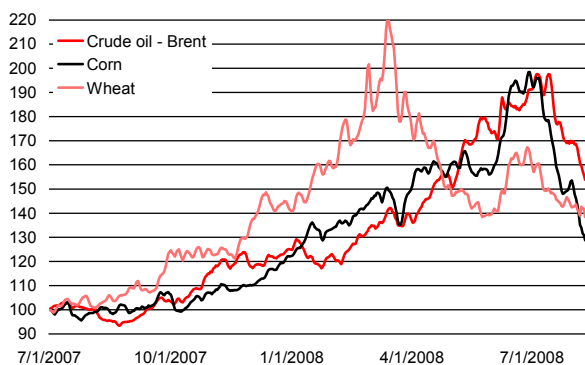
- The recent correction in commodity prices is bringing relief for fuel and food prices. These direct effects should lower the inflation rate in August.
- It is, however, still not possible to sound the final all-clear on the inflation front. Pipeline pressure remains high. Corporate selling price expectations continue to point to lagging, indirect price increases.
- Barring a further strong pullback in commodity prices, the inflation rate will moderate only slowly. As a result, the ECB will remain vigilant until further notice, primarily also because of rising wage demands.

Correction on commodity markets

Until only recently, it had appeared commodity prices knew only one direction: upwards. But there has been an impressive change in this situation in recent weeks. Alongside the oil price, prices of above all agricultural commodities have corrected appreciably (cf. chart). The consolidation on commodity markets is bringing relief on the inflation front. After inflation had spiked to a 15-year high in July, the preliminary numbers for August being released at the end of the month should bring a tangible pullback in inflation, helped by lower prices for fuel and heating oil.

CONSOLIDATION ON THE COMMODITY MARKETS

Futures prices, index (1.7.2007 = 100)



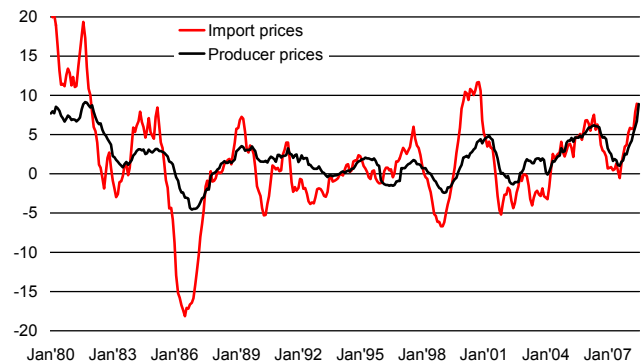
Source: Bloomberg, UniCredit Global Research

Inflationary pressure still high

The consolidation does not, however, mean it is possible to sound a general all-clear on the inflation front. This was also reflected in the ECB comments after the recent interest rate decision. Even though the central bank took note of the price declines, it still described commodity prices as high and volatile. It also said that forecasting commodity prices is one of the most difficult exercises. And commodity prices across the board remain, in fact, well above pre-year levels. Contrary to the direct, dampening effects of commodity prices on consumer prices, the pressure in the pipeline therefore remains high. The upstream price stages point to a steep upward trend until July. Despite the strong EUR exchange rate until recently, the annual rate for import prices is currently a very high 8.9%. Producer price inflation in July (also 8.9%) even hit its highest level in almost 27 years (cf. chart).

HIGH UPSTREAM INFLATION PRESSURE

In % y-o-y

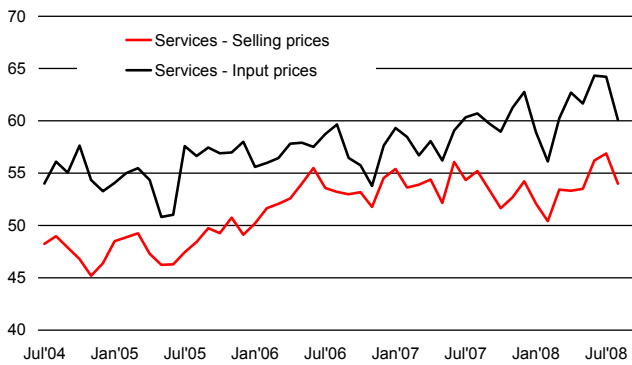
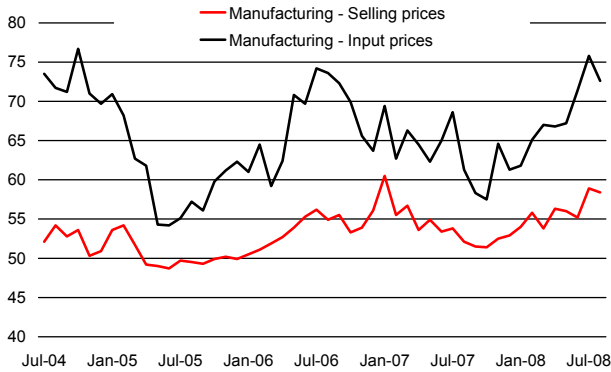


Source: Feri, UniCredit Global Research

The surge in input prices in industry and at service companies over the past year points to further, delayed price increases for the coming months. Even though the persisting weakness of consumer demand should prevent the incremental costs being passed on in full, the increased pressure on margins will compel many companies to raise prices. This is underpinned by selling price expectations. Even after the recent correction in commodity prices, the number of firms planning to raise prices remains high in August (cf. chart on the next page).

EXPECTATIONS FOR SELLING PRICES REMAIN ELEVATED

PMIs

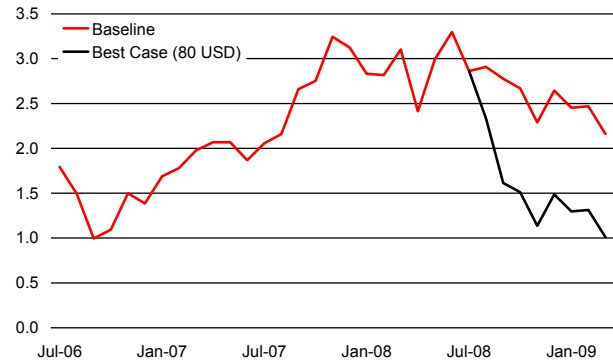


Source: Feri, UniCredit Global Research

Accordingly, the dynamic in core consumer prices (ex energy and food) should remain at a heightened level for the time being. Even though we do not expect any further acceleration in the annual rate of consumer prices, under current conditions we do not see clear relief either until next spring. Only a further strong and sustained correction in commodity prices, which we do not however anticipate, could rapidly push the inflation rate below the 2% mark and put an end to inflation concerns. We calculate a pullback in the oil price to USD 80 per/barrel would see the inflation rate fall rapidly towards the 1% mark (cf. chart in the next column).

INFLATION SCENARIOS

Consumer prices, in % y-o-y



Source: Feri, UniCredit Global Research

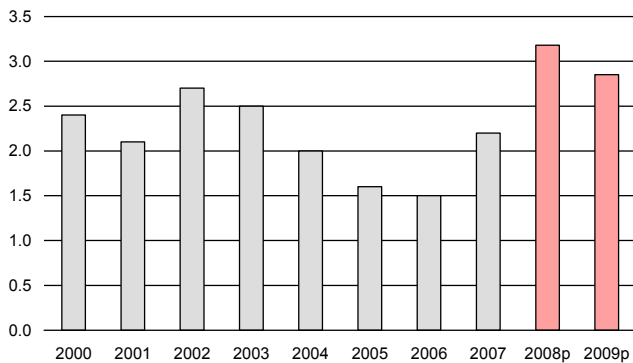
Wage-price spiral remains in check

Apart from this scenario, inflation risks will persist for the near future. Furthermore, stubborn inflation, which in all probability will not permit any perceptible rise in real incomes this year either, caused wage demands for the next round of collective bargaining to increase further. The next key collective wage agreement in the metalworking and electrical engineering industry for roughly 3.2 mn employees expires at the end of October. Even though there is no official wage demand so far, IG-Metall chief Berthold Huber has announced a markup to the 6.5% demanded in the previous year. And the delegate meeting of the Ludwigsburg region has agreed on a proposal of 9% plus a one-time payment of EUR 1,000. Factors arguing against realization of the very high wage demands are, however, the strong deterioration in business expectations and the related trend reversal on the labor market expected at the latest by the end of the year (cf. Research Note on page 10). In respect to the macroeconomic environment, the probability of excessive wage settlements has, therefore, declined considerably.

And even though the collective wage agreements concluded so far for this and next year show substantially higher wage increases overall compared to the moderate previous years, they do not so far point to the heightened danger of strong second-round effects. Based on our calculations, the key agreements concluded so far for calendar year 2009 even point to a slight slowdown in the growth rate of collectively agreed upon wages compared to this year to close to 3.0% (cf. chart on the next page).

HIGHER WAGE SETTLEMENTS

Collective-agreed wages in key sectors, in % y-o-y, based on the calendar year



Source: WSI, UniCredit Global Research

In summary, we expect the consolidation in commodity prices combined with the weak outlook for growth in the coming quarters will see the inflation rate moderate steadily, albeit slowly because of the still high pipeline pressure in the short term. The remaining upside risks - which for the euro zone as a whole are similar to those for Germany - will, however, prevent the ECB from scaling back its rhetoric in the coming months. The No. 1 inflation watchdog should remain vigilant.

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Germany: Labor market upswing running out of steam

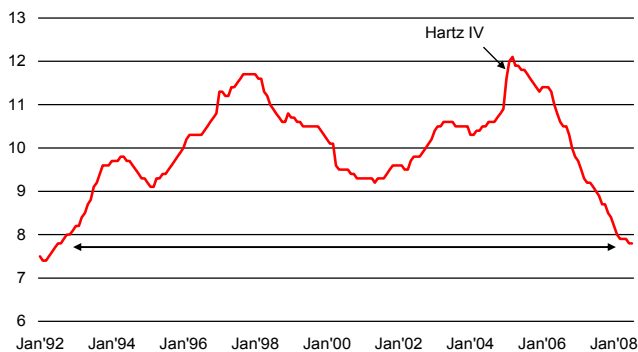
- So far, the labor market has been unimpressed by the dark clouds gathering on the economic horizon. In July, the unemployment rate fell to its lowest level since 1992.
- The Beveridge curve in addition suggests that the strong efforts undertaken by German industry to improve competitiveness have halted the rise in structural unemployment.
- A cyclical weakening of the lagging indicator labor market is, however, inevitable. By the end of the year at the latest, we expect the rise in employment to end.

Labor market still in an upswing

The German economy has turned on a dime. In spring, the economy contracted 0.5% q-o-q, the first decline in almost four years. Even though the weakness is attributable in part to a technical correction – special factors had provided the growth dynamic with strong support at the beginning of the year – the latest growth numbers nevertheless already reflect the cyclical downswing forces. This is underscored by the slump in the leading indicators, whose levels now indicate a heightened recession risk. The German economic boom has screeched to a halt. The only good news recently still came from the labor market. We also expect the labor market numbers for August, scheduled for release next week, to show a renewed decline of an adjusted 15,000. The important employment subject to social security contributions number has increased strongly since the low at the beginning of 2006, by roughly 1.4 mn. And at 7.8%, the adjusted unemployment rate has fallen to its lowest level since June 1992.

STRONG DECLINE IN UNEMPLOYMENT

Unemployment rate in %, sa



Source: Feri, UniCredit Global Research

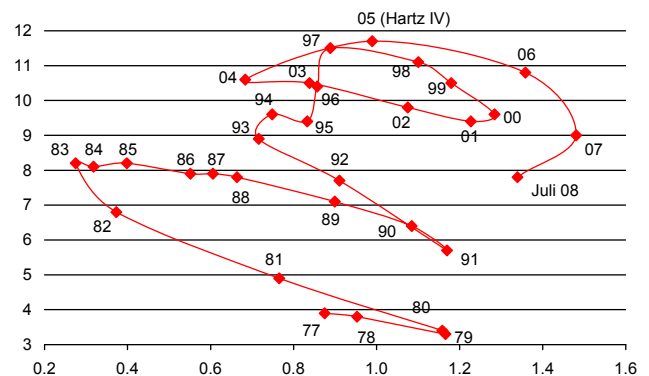
The labor market is, however, traditionally a lagging economic indicator. It reacts with a certain time lag to turning points in the growth dynamic. And recently there has been mounting evidence that the success story will end soon.

Rise in structural unemployment halted

The number of vacancies, a reliable leading indicator for the labor market, already peaked some time ago. In the past, a trend reversal in the ratio of vacancies to the labor force has reliably indicated cyclical turning points on the labor market. This correlation is found in the concept of the Beveridge curve (named after the economist William Beveridge (1879-1963)). The Beveridge curve is a graphical representation of the relationship between the unemployment rate and the job vacancy rate, with the unemployment rate normally being plotted on the Y axis (cf. chart). In principle, the curve slopes downwards to the right, since a lower vacancy rate normally reflects higher unemployment, and vice versa.

BEVERIDGE CURVE

X axis: job vacancy rate; Y axis: unemployment rate



Source: Feri, UniCredit Global Research

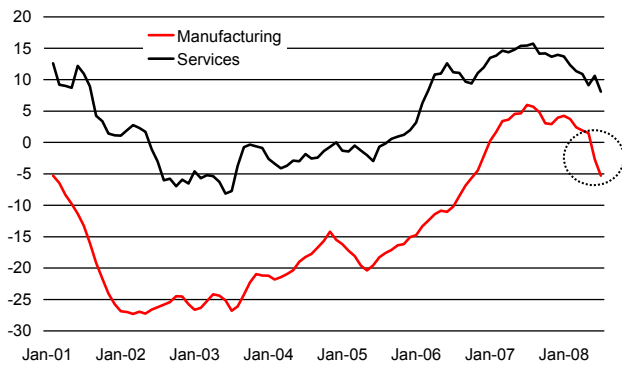
The Beveridge curve for the German labor market has shifted clearly outward since the 70s. That means that with the same job vacancy rate the level of unemployment has increased. This development reflects the rise in structural unemployment. The extensive efforts undertaken by German industry to improve competitiveness since the high-tech bubble burst have, however, prevented any further outward drift of the Beveridge curve. The structural factors that made the outstanding performance of German industry possible in recent years have not vanished, despite the current deterioration in the outlook for growth. This should also provide support over the medium term, and in the process help forestall a renewed increase in the still high structural unemployment.

Cyclical trend reversal ahead

Nevertheless, a cyclical downswing on the labor market appears inevitable. The rapid end of the boom phase in German industry has already had a strong negative impact on corporate hiring plans in manufacturing (cf. chart). The unexpectedly rapid reduction of the comfortable order cushion, exacerbated by the unfavorable prospects for growth in the most important trading partner countries, clearly suggests hiring plans will also become increasingly cautious in the coming months. Accordingly, strong job creation in the services sector should also level off, not least because the high level of inflation is hurting private consumption.

TREND REVERSAL IN EMPLOYMENT PLANS

Employment plans, EU Commission survey



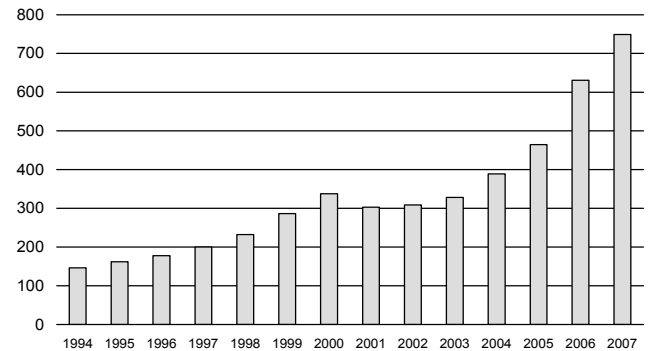
Source: Feri, UniCredit Global Research

Temporary employment being put to the test

This also applies in special measure to the dynamic temporary employment sector, which has made a material contribution to the pronounced upturn on the labor market. Since the extensive liberalization of temporary employment under the Schröder administration, the number of temporary employees has increased rapidly. Similar to the regime in many other countries, the time limit on temporary employment was abolished in 2003. As a result, temporary employment has become much more appealing as an instrument to circumvent Germany's extensive protection against termination that still applies to permanent employment relationships. Since the abolition of the time limit on temporary employment, the number of temporary employees more than doubled by the end of 2007 to approximately 750,000 (cf. chart in the next column). Since the beginning of the current labor market upswing, temporary employment has increased by an average of 30% in the last two years. In contrast, the already gratifyingly strong dynamic in employment subject to social security contributions totaled 'only' 2% per year.

SURGE IN TEMPORARY EMPLOYMENT

Temporary employees at the end of the year, in thousands

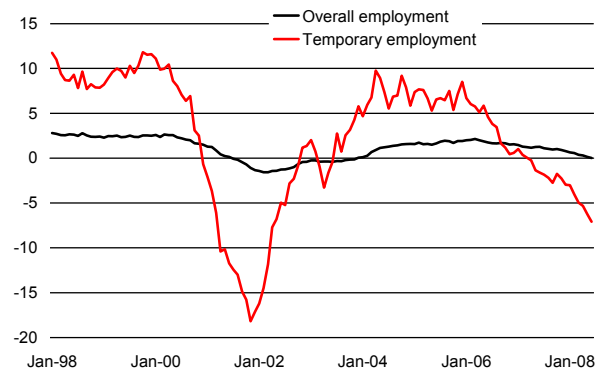


Source: BZA, UniCredit Global Research

The deterioration in the outlook for growth will also impact the temporary employment sector. It is, however, still a bone of contention whether the increase in temporary employment will exacerbate or dampen the anticipated labor market slowdown. On the one hand, companies can rapidly reduce the number of temporary employees on a decline in capacity utilization. On the other hand, the flexibility of the instrument temporary employment could reduce corporate caution over hiring plans during more uncertain times. Unfortunately, data for the temporary employment sector in Germany are still relatively meager, thereby making near-term conclusions about its impact on employment more difficult. A glance at the cycle of the temporary employment industry in the US does, however, suggest that in an economic downswing phase temporary employment leads the development of overall employment, and the decline in temporary employment is disproportionately strong. Recently, the situation in the US temporary employment industry also turned much earlier (cf. chart).

US TEMPORARY EMPLOYMENT AMPLIFIES LABOR MARKET CYCLES

US employment, in % y-o-y



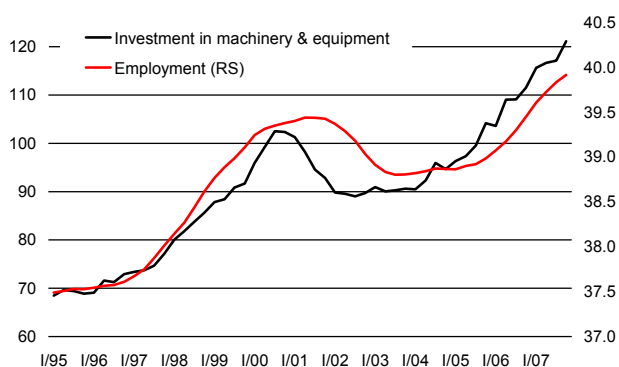
Source: Feri, UniCredit Global Research

Labor market upswing will be over by the end of the year the latest

The development of employment in Germany is very closely correlated with the dynamic of corporate investment (cointegration, cf. chart). In the short term, the development of employment can fluctuate around the investment trend. These deviations are, however, eliminated again over time (error correction mechanism).

LONG-TERM CORRELATION

Employment in mn



Source: Feri, UniCredit Global Research

Our error correction model for forecasting the development of employment tracks the actual dynamic on the labor market relatively reliably. It indicates a trend reversal in employment by the beginning of 2009. Until then, it still shows a further increase in employment, albeit at a much slower pace. But the expiry of declining-balance depreciation for business investments at the end of last year probably helped the investment dynamic recently on advance effects. Accordingly, there is the risk that the slowdown in investment in machinery and equipment, suggested by official statements after the release of the preliminary growth numbers for the second quarter, will continue, amplified by the recent slump in the dynamic of foreign demand in industry. As a result, we see the risk of the rise in employment already ending later this year. All told, we expect 2008 will still bring a further tangible decline in unemployment of roughly 300,000, after 600,000 in the previous year. In the coming year, however, a net total of roughly 150,000 jobs should then be lost in the course of the year.

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Data Monitor Europe – Preview of the coming week

Tuesday, August 26

GERMANY, IFO BUSINESS CLIMATE

August	MIB	Cons.	July	June
Index	97.2	97.2	97.5	101.2

The disappointing development of new orders in industry as well as private consumption, which is being hit hard by high inflation, have recently triggered a slump in business sentiment. The strong correction in the oil price as well as the marked depreciation of the EUR in recent weeks will probably have provided business expectations with at least temporary support in August. The still high situation component should, in contrast, continue to weaken steadily. Overall, we expect a slight fall in the business climate in August.

GERMANY, GDP

II/08	MIB	Cons.	I/08	IV/07
in % q-o-q	-0.5	-0.5	1.3	0.3
in % y-o-y	1.7	1.7	2.6	1.7

The August 14 Flash estimate will probably be confirmed. The release of the detailed components should show a very strong correction in construction. According to officials, demand for investment in machinery and equipment has also slowed. Private consumption, which is being hit by the high level of inflation, was presumably also a drag. The sole support in the spring was net exports, but only because imports were down much more strongly than exports.

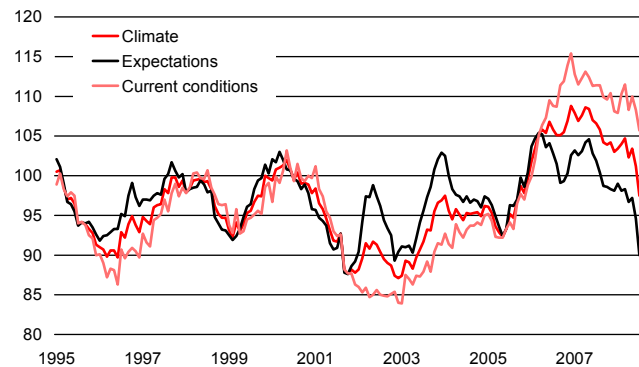
GERMANY, GFK CONSUMER CLIMATE

September	MIB	Cons.	Aug	July
Index	2.3	2.0	2.1	3.6

The strong price increases, primarily for consumer staples, have recently triggered a slump in income expectations. The growing concerns about the economy have also had a negative impact on the willingness-to-buy. The recent correction in oil and fuel prices has, however, brought some temporary relief. We therefore expect a slight improvement in the consumer climate at a still low level.

NOTICEABLE DETERIORATION IN CORPORATE SENTIMENT

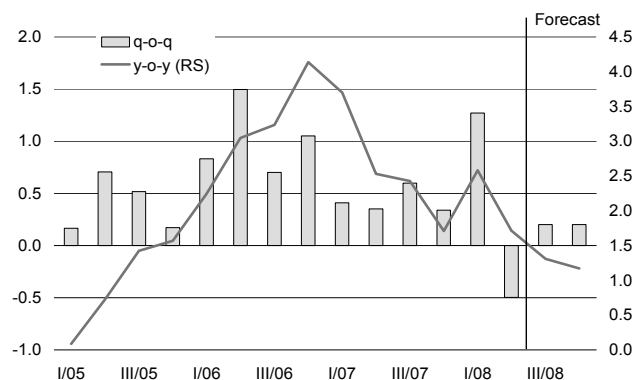
Ifo index



Source: Feri, UniCredit Global Research

ECONOMY HEADING SOUTH

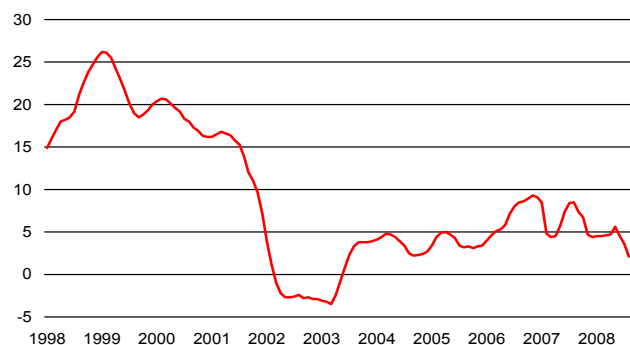
GDP, real, in %



Source: Feri, UniCredit Global Research

CONSUMER SENTIMENT REMAINS MUTED

Gfk consumer climate



Source: Thomson Datastream, UniCredit Global Research

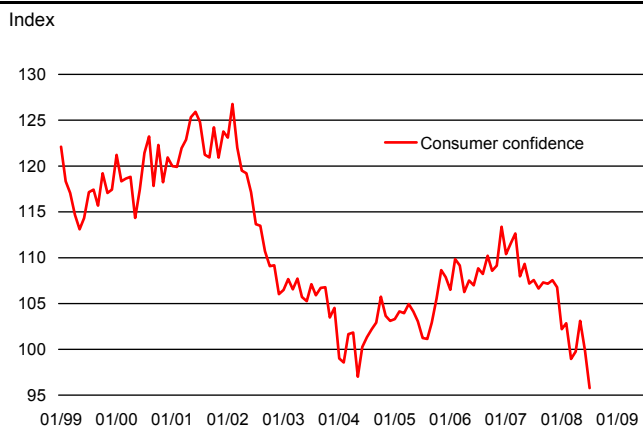
Wednesday, August 27

ITALY, CONSUMER CONFIDENCE

August	MIB	Cons.	Jul	Jun
	97.5	96.6	95.8	99.9

After having plunged to its historical low in July (at 95.8) we expect Italy's consumer confidence to have rebounded in August, rising to 97.5. The decline in fuel prices and likely moderation in food inflation might have had a positive impact on sentiment, offsetting the depressing effect of the negative GDP growth in Q2.

TEMPORARY RECOVERY IN SENTIMENT



Source: ISAE, UniCredit Global Research

Thursday, August 28

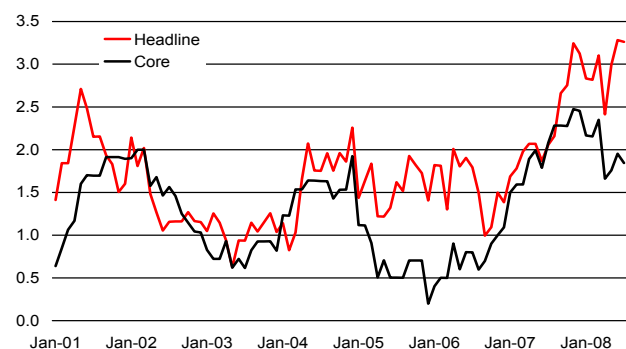
GERMANY, CONSUMER PRICES (FLASH)*

August	MIB	Cons.	July	June
in % m-o-m	-0.5	-0.2	0.6	0.3
in % y-o-y	2.9	3.2	3.3	3.3

The correction in fuel and heating oil prices should have triggered a tangible m-o-m decline in consumer prices in August. As a result, the annual headline rate will probably also dip slightly below the 3% mark again. Consequently, inflation has presumably already peaked. But the inflationary pressure will remain high in the short term and prevent a further pullback in the inflation rate in the coming months (cf. also Research Note on page 7).

CORE RATE BELOW THE 2% MARK

Consumer prices in % y-o-y



Source: Feri, UniCredit Global Research

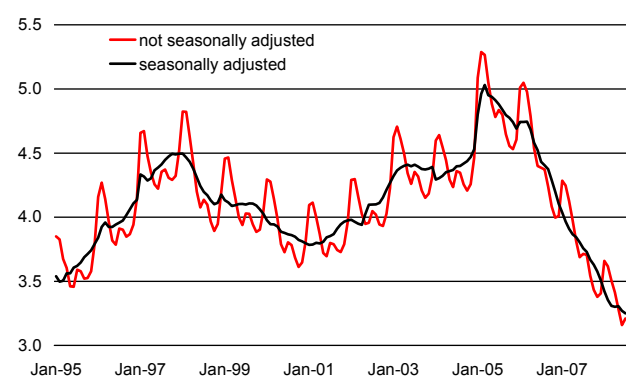
GERMANY, UNEMPLOYMENT

August	MIB	Cons.	July	June
in '000 m-o-m, sa	-15	-10	-20	-36
in '000 m-o-m, nsa	-30	-	50	-123

After the end of the summer holidays in several federal states, unemployment should have declined in August on seasonal effects. The adjusted number will probably also have declined further despite the deterioration in the outlook for growth, albeit at a slower pace. As a lagging economic indicator, the labor market will probably increasingly run out of steam in the coming months. By the end of the year at the latest, we expect a trend reversal for employment (cf. also Research Note on page 10).

DOWNWARD TREND STILL INTACT

Unemployment in mn

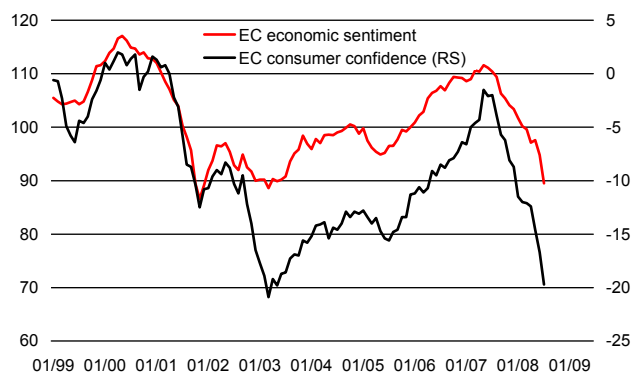


Source: Feri, UniCredit Global Research

EMU, ECONOMIC CONFIDENCE

August	MIB	Cons.	July	June
	89.1	88.9	89.5	94.8

Economic confidence should decline further in August, coming in at 89.1. Sentiment among manufacturers and consumers seems more vulnerable: manufacturers are facing rising levels of stocks and worsening expectations for domestic and foreign demand, while consumers are seeing their purchasing power dragged down by the inflation spike and are starting to get concerned about labor market prospects.

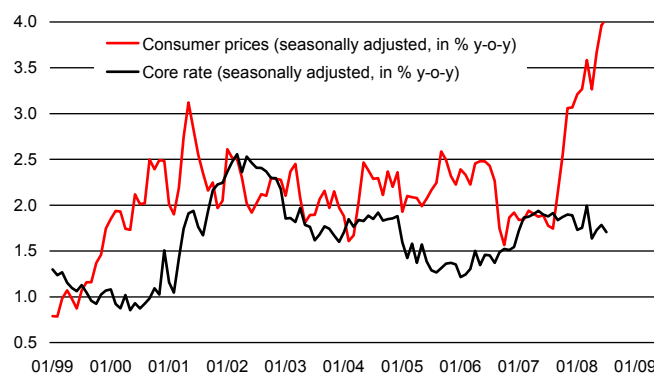
DECLINING FURTHER


Source: European Commission, UniCredit Global Research

Friday, August 29
EMU, CONSUMER PRICES (FLASH)

August	MIB	Cons.	July	June
In %, y-o-y	3.9	3.9	4.0	4.0

We expect the inflation rate in August to edge down to 3.9%, mostly because of lower energy prices. As a matter of fact, barring any renewed and abrupt increase in oil prices, we reckon that the June-July outcome may well represent the peak in inflation in this cycle.

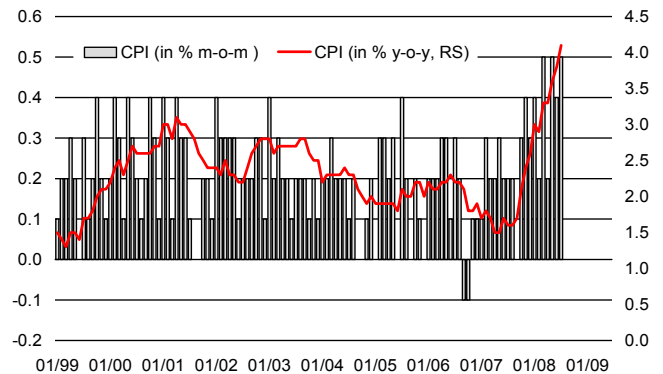
INFLATION HAS PEAKED


Source: Eurostat, UniCredit Global Research

ITALY, CONSUMER PRICES

August	MIB	Cons.	July	June
In %, y-o-y	3.8	4.0	4.0	3.8

Italy's consumer prices should remain unchanged in August from the previous month, bringing the yearly growth rate down to 3.8%. The deceleration is mostly attributable to lower transport costs, thanks to falling fuel prices in the month. Core components should remain well behaved and food inflation has likely entered a downward trend. Thereafter, we expect inflation to stabilize at the current level in the short term.

INFLATION HAS PEAKED


Source: Istat, UniCredit Global Research

* Earliest possible release date.

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Data Monitor US - Preview of the coming week

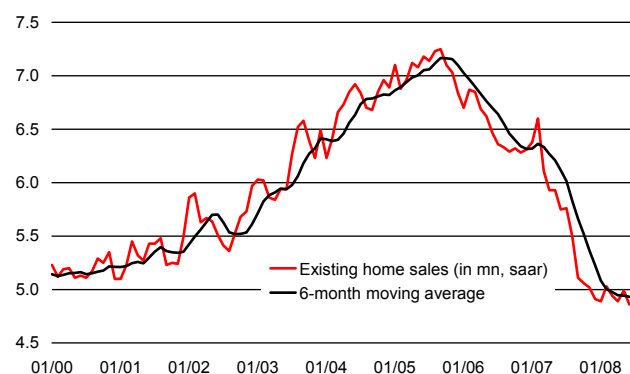
Monday, August 25

EXISTING HOME SALES

July	MIB	Cons.	June	May
In mn annualized	5.00	4.90	4.86	4.99

After dropping 2½% in June, existing home sales likely rebounded in July. Such a movement has been signaled by the Pending Home Sales Index, which rose 5¼%. Overall, it seems as if home sales have finally found a bottom. Partly due to the soaring numbers of foreclosures, home sales have been particularly robust in California, Florida, and Arizona during the last six months.

EXISTING HOME SALES HAVE BOTTOMED OUT



Source: Thomson Datastream, UniCredit Global Research

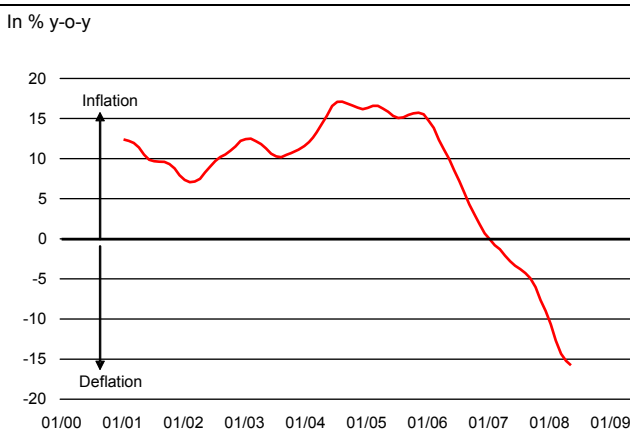
Tuesday, August 26

S&P/CASE SHILLER HOME PRICE INDEX

June	MIB	Cons.	May	Apr
In % y-o-y	-16.2	-16.2	-15.8	-15.2

High inventories of homes for sale continue to exert downward pressure on home prices. However, the monthly decline in the Case Shiller index has decelerated during the last two months. As the monthly numbers are calculated as a smoothed three-month average, we expect another rather benign drop in June. Due to basis effects, the y-o-y reading will continue to decline by August, before it starts to improve.

HOUSE PRICES CONTINUE TO DROP



Source: Thomson Datastream, UniCredit Global Research

NEW HOME SALES

July	MIB	Cons.	June	May
In thousands annualized	525	525	530	533

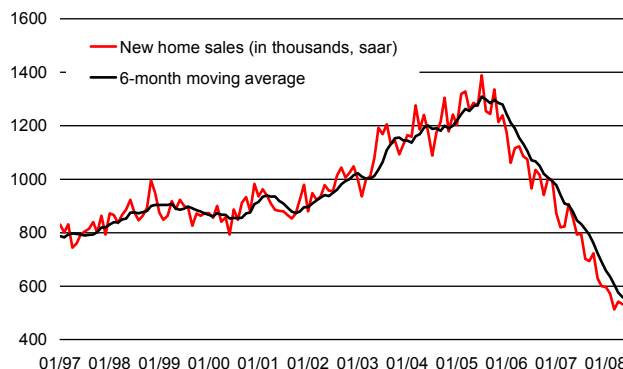
The situation on the market for new homes remains bleak. The latest NAHB Housing Market Index stayed at an all-time low of 16, and according to reporting homebuilders, the traffic of prospective buyers continued to decline. As a result, we expect sales of new homes to decrease further. Nevertheless, as the supply of new homes is shrinking even faster, the excess supply of unsold new homes is gradually coming off its peak.

CONSUMER CONFIDENCE – CONFERENCE BOARD

August	MIB	Cons.	July	June
	53.0	53.0	51.9	51.0

All consumer confidence indicators have risen from their multi-year lows in June, and the daily Rasmussen survey signals that this improvement has continued in August. Main reason is the ongoing decline in gas prices, which fell by more than 7% since early July. The weak labor market, on the other hand, impedes a bigger increase in consumer confidence. This is particularly true for the Conference Board's index, which puts a lot of weight on the labor market and income situation of households.

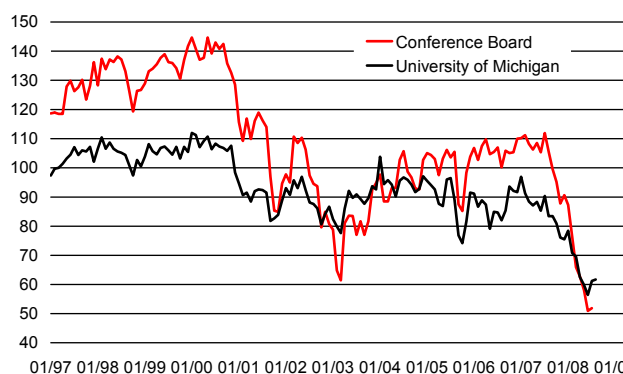
BLEAK OUTLOOK FOR HOMEBUILDERS



Source: Thomson Datastream, UniCredit Global Research

CONSUMER CONFIDENCE REMAINS SUPPRESSED

Consumer confidence index



Source: Thomson Datastream, UniCredit Global Research

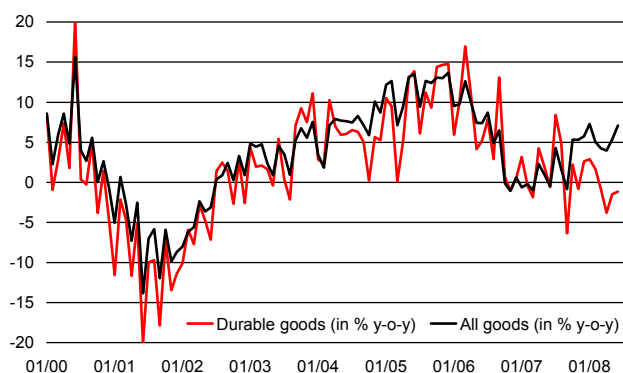
Wednesday, August 27

DURABLE GOODS ORDERS

July	MIB	Cons.	June	May
In % m-o-m	0.2	0.1	0.8	0.1

Car sales and orders tend to move together month to month. And we know that July was another poor month for car sales. Airplane orders are also being hurt by the energy price explosion, and many existing orders are being cancelled or renegotiated. On the other hand, the manufacturing sector benefits from solid demand for commodity and export goods. Net on net, we expect another mild increase in new orders.

STRONG EXPORTS PREVENT A SLUMP IN NEW ORDERS



Source: Thomson Datastream, UniCredit Global Research

Thursday, August 28

REAL GDP, PRELIMINARY

II/08	MIB	Cons.	I/08	IV/07
in % q-o-q annualized	2.8	2.8	0.9	-0.2
in % y-o-y	-	-	2.5	2.3

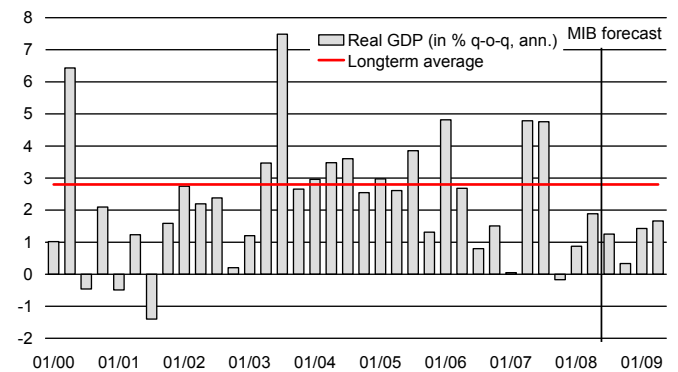
The US economy likely grew much faster than the initially reported 1.9% in Q2. The upward revision of net exports alone will lift GDP growth by almost three quarters of a percentage point. In addition, inventory and private consumption data were better than initially reported.

INITIAL JOBLESS CLAIMS

August 23	MIB	Cons.	Aug 16	Aug 09
in thousands	430	-	432	445

Since the last week of July, initial jobless claims have been between 450k and 460k. While this elevated level may signal a further deterioration of the labor market situation, we think that it mostly reflects the impact of the government's "Emergency unemployment compensation program." If this is the case, initial claims will move back towards 400k during the next few weeks.

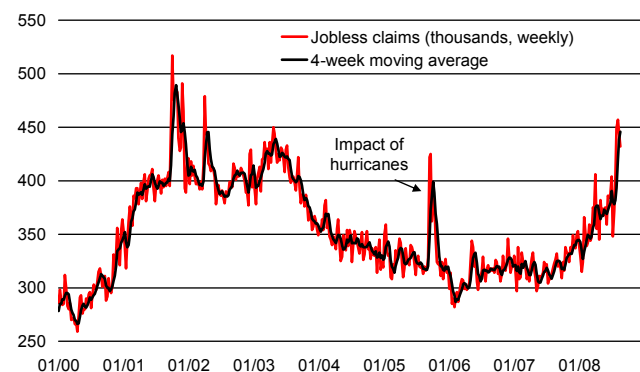
SUB PAR GROWTH AHEAD



Source: Thomson Datastream, UniCredit Global Research

THE IMPACT OF THE GOVERNMENT'S EMERGENCY PROGRAM

In thousands



Source: Thomson Datastream, UniCredit Global Research

Friday, August 29

PERSONAL INCOME & OUTLAYS

July	MIB	Cons.	June	May
Income, in % m-o-m	-0.7	0.0	0.1	1.8
Spending, in % m-o-m	-	0.2	0.6	0.8

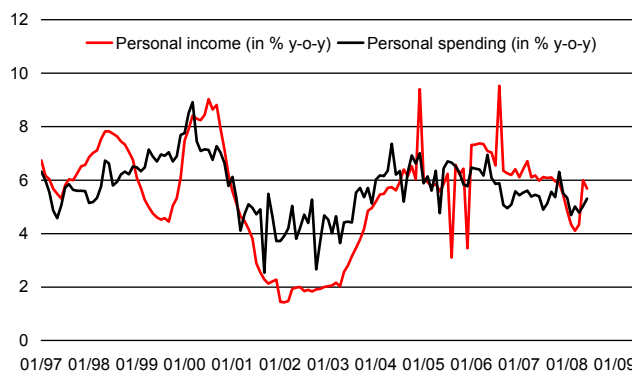
In month one after the tax rebates, personal income will drop noticeably. However, as households have so far spent only a quarter of their rebates, we expect the fiscal stimulus will continue to support consumption in Q3. As a result of this consumption smoothing, the savings rate, after jumping to 5% in May, will become negative in July. We expect a drop to -¾% or even -1%.

CORE PERSONAL EXPENDITURE PRICE INDEX

July	MIB	Cons.	June	May
in % m-o-m	0.3	0.3	0.3	0.2
in % y-o-y	2.5	2.4	2.3	2.2

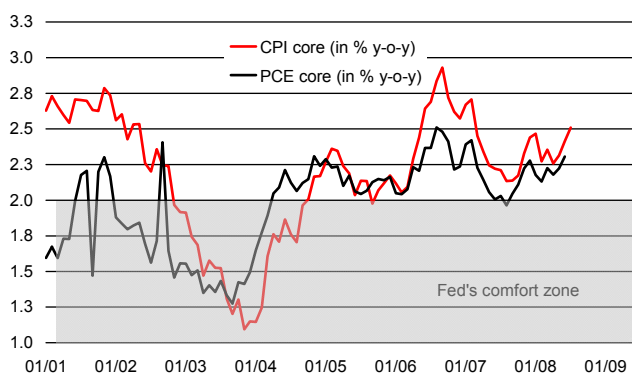
The core CPI was up 0.3% in July, despite a benign 0.1% increase in owners' equivalent rent. As this component has a much smaller weight in the core PCE basket, we predict a "high" 0.3% rise, lifting the y-o-y rate to 2.5% - the highest level in almost two years. Above all, we expect higher prices for apparel and public transportation.

MONTH ONE AFTER THE TAX REBATES



Source: Thomson Datastream, UniCredit Global Research

CORE INFLATION ON THE RISE



Source: Thomson Datastream, UniCredit Global Research

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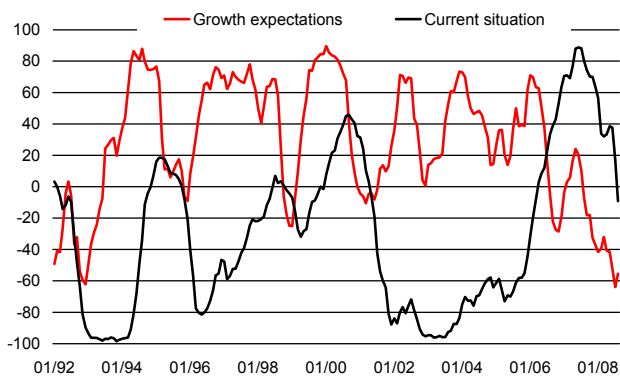
Review Europe

Germany: Situation deteriorates

In August, the ZEW growth expectations for Germany staged a surprisingly strong recovery, from -63.9 to -55.5. It was the first increase after four consecutive declines. The recent strong correction in the oil price as well as the weaker EUR probably bolstered the expectations of financial market experts that the German economy will be over the worst in six months. This does not, however, change the fact that the growth dynamic will be weak in the second half of 2008. This is underscored by the fact that the ZEW situation component plummeted at the same time from 17.0 to -9.0. This was the strongest decline since the time series was launched in December 1991 and the lowest reading since February 2006.

SHARP DECLINE IN THE SITUATION ASSESSMENT

ZEW index



Source: Feri, UniCredit Global Research

The bleak prospects for growth in the remainder of the year are also reflected in the renewed marked decline in the PMIs. The preliminary index reading for manufacturing in August fell from 50.9 to 49.9 and, therefore, below the expansion threshold; the reading for the services sector fell from 53.1 to 50.6. As a result, the probability of a further decline in the Ifo business climate index this coming Tuesday has also increased substantially.

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Review US

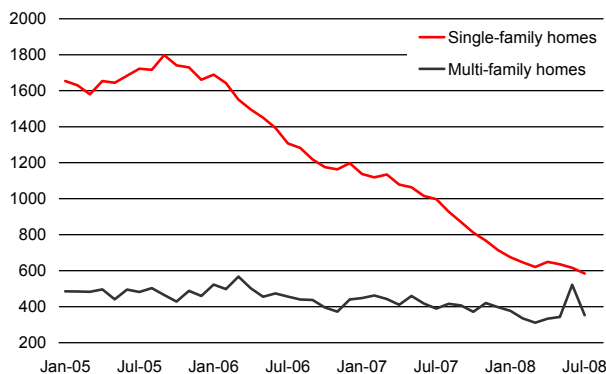
Housing slump continues

US housing starts and building permits dropped significantly in July after soaring in June. Starts fell back to an annualized 965k units, and building permits dropped to 937k units. The noticeable declines in July are a correction of the exaggerated strength in previous months rather than the beginning of a renewed downturn. In fact, building permits, which are the leading indicator of residential construction activity, were still slightly higher than the cyclical low reached in March. The short-term volatility was caused almost exclusively by permits for multi-family apartment buildings. They plunged 32.4% in July, after jumping 52.2% in June (cf. chart). Permits for new single-family homes, in contrast, have shown a steadier decline.

In a separate report, the NAHB Housing Market Index stayed at its all-time low of 16 points in August, underpinning the gloomy mood among homebuilders.

SLIDE IN PERMITS FOR SINGLE-FAMILY HOMES GOES ON

Building permits, in k units at annual rates



Source: Census Bureau, Thomson Datastream, UniCredit Global Research

Producer prices soared in July

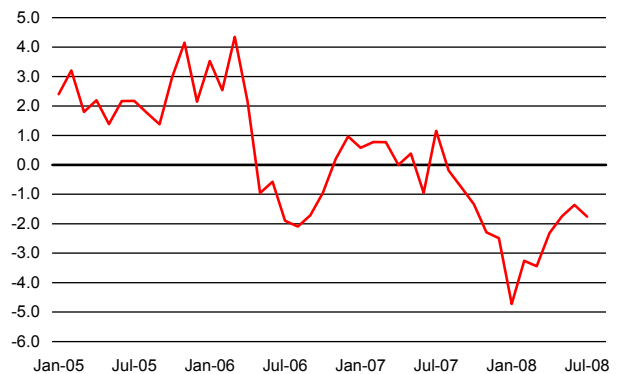
The producer price index (PPI) for finished goods soared another 1.2% in July, lifting the y-o-y rate to a new 27-year high of 9.8%. While energy prices went up another 3.1%, the PPI ex food & energy also increased an elevated 0.7%. As a result, the y-o-y rate rose to 3.5%, the highest in 17 years. Strangely enough, prices for cars increased another 1.4% after rising 2.2% in June. It is important to note that the reporting week for the PPI report is in the middle of the month. In July, oil prices marked their all-time high of USD 147 per barrel exactly then. Hence, the August report is likely to show a significant drop in producer prices, mirroring the plunge in energy prices.

Leading Indicators show biggest monthly decline in a year

The Index of Leading Indicators dropped 0.7% in July, the fastest decline since last August. Behind the noticeable decline were lower stock prices, weaker building permits and the surge in initial jobless claims. Higher interest rate spreads and an improved consumer confidence, in contrast, supported the index. The monthly decline in the Index of Leading Indicators was exaggerated by two factors. First, the increase in initial jobless claims was caused partly by the government's "emergency unemployment compensation program". Second, the significant drop in building permits was a correction of an unsustainable increase in the previous month. While the less volatile six-month change in the Index of Leading Indicators fell to -1.8% from -1.4%, it remains much more benign than the maximum drop of -4.7% between July 2007 and January 2008 (cf. chart).

THE TREND IS UP

Index of Leading Indicators, annualized 6M change in %



Source: Conference Board, Thomson Datastream UniCredit Global Research

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Fixed Income Outlook

- This week, financial worries dominated the scene: in the first part of the week, equity markets registered a sluggish performance across the board and curves steepened on both sides of the Atlantic.
- Next week, the agenda will be quite busy in terms of data. However, both in the US and in the eurozone we do not expect major departures from the current scenario.

Financial worries: the same old story

Once again, it is all about financial worries. In the eurozone, a better-than-expected ZEW did not manage to have a relevant impact on yields, while bad news from the financial sector pushed investors to safe-haven assets: equity markets registered a sluggish performance and the curve remained on a steepening trend (with some flattening towards the end of the week). In the U.S., the story has been pretty much the same, with the 2/10Y spread steepening.

Next week, the agenda will be quite busy in terms of data calendar on both sides of the Atlantic. In the U.S., another round of housing data, consumer confidence, durable goods orders, the preliminary release of GDP and PCE are scheduled: as we expect mixed evidence from the growth data, the market tone will be set by the FOMC minutes (out on Tuesday) and by the performance of equity markets. Should the FOMC minutes be in line with the previous one and reiterate the view that the Fed is concerned about both downside risks to growth and upside risks to inflation (as we expect), the market impact would be limited.

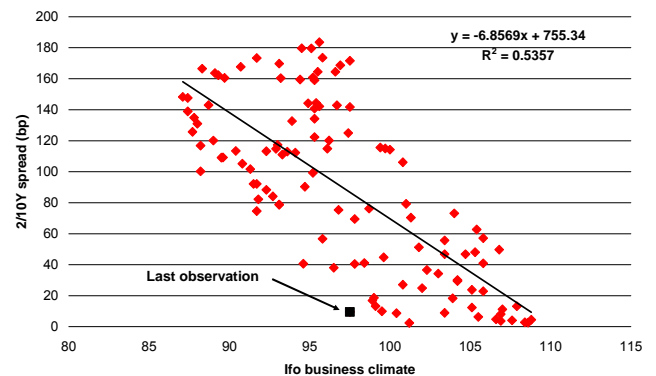
In the eurozone, Ifo, consumer confidence and the unemployment rate are scheduled for next week, while on the inflation side, we have the flash estimate of the August CPI. We expect growth data to confirm the overall picture of a deteriorating economic outlook, with a limited market impact. As for the CPI, we expect a deceleration from last month's peak (Forecast: 3.9%). The first chart shows the results of a model relating the Ifo with the level of the 2/10Y spread. Last month, the Ifo reading was 97.5, a level consistent with a 2/10Y spread trading in the 80bp area. This time, we expect the Ifo at 97.2. Our model suggests that we should observe a steepening of the curve. The second chart shows the spread between the refi rate and the 2Y Bund yield. It highlights that:

During the first phase of the last tightening cycle (November 1999/October 2000), the 2Y/refi rate spread collapsed to around current levels and started moving on an increasing trend a few months after, as investors started to anticipate rate cuts.

In the first phase of the current tightening cycle, the 2Y/refi spread has followed the same path, moving on an increasing trend as the market started to expect rate cuts. The movement was reversed by a hawkish Trichet, hiking rates by 25bp in July and sending back the spread to trade in its lowest range. The spread is now trading in the -30bp area, above both the minimum level touched during the past hiking cycle and in the present hiking cycle.

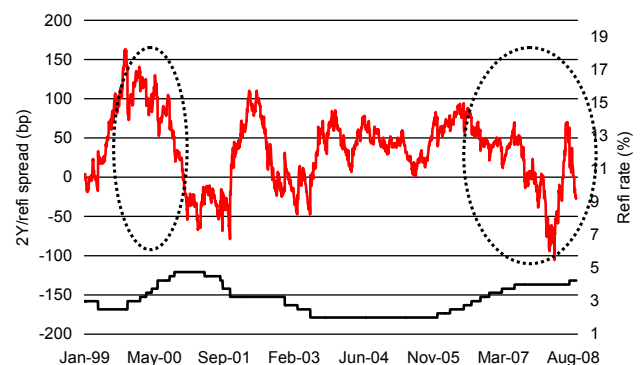
Our analysis hints at a further decrease in yields at the 2Y tenor and a steepening of the EU curve. However, as at the moment the market is not discounting the chance of a near term rate cut, we still do not see the case for a rally at the front end and a further steepening of the curve in the near term.

IFO SIGNALS A STEEPER 2/10Y SPREAD



Source: Bloomberg, UniCredit Global Research

2Y/REFI SPREAD: STILL SOME WAY TO GO



Source: Bloomberg, UniCredit Global Research

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Forex Outlook

- This week, the key word in the EUR-USD path has been stabilization. After hitting fresh lows at 1.4630 on Tuesday, the EUR-USD recovered some ground on increasing oil prices, and came back to trade in the 1.48 area.
- Next week, we expect the EUR-USD to remain around current levels, with some risks of further downward pressures should the FOMC minutes be more skewed to the hawkish side.

EUR-USD: a pause after the thunderstorm

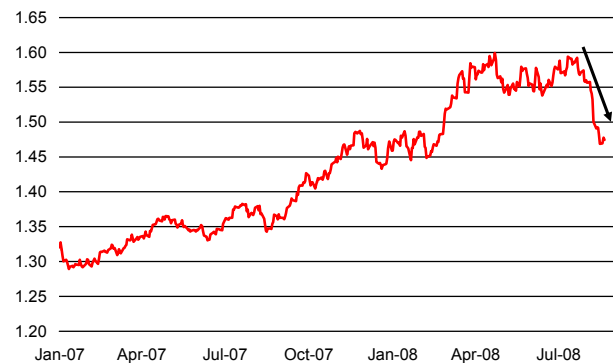
This week, the key word in the EUR-USD movement has been stabilization. After hitting fresh lows at 1.4630 on Tuesday, the EUR-USD recovered some ground on slightly increasing oil prices and came back to trade in the 1.48 area.

Next week, the data calendar will be quite full both in the U.S. and in the eurozone. In the U.S., we expect growth data (another round of housing data, consumer confidence, durable goods orders, preliminary release of the GDP and PCE) to show mixed evidence. The FOMC minutes out on Tuesday should reiterate the “downside risks to growth and upside risks to inflation” story, but with slightly more emphasis on the hawkish side.

In the eurozone, we expect growth data (Ifo, consumer confidence and unemployment rate) to confirm the gloomy economic outlook, while the flash estimate of the CPI should show some deceleration on the back of the decrease in oil prices (Forecast: 3.9%).

In this scenario, we do not expect further downside pressure on the EUR-USD to come from the eurozone: the last two weeks' steep slide already incorporates the eurozone gloomy scenario and it seems quite unlikely that a deceleration in the CPI, mainly driven by a sharp decrease in oil prices, could have a strong impact on the EUR either. If anything, risks are for a further slight appreciation of the greenback should the market read the FOMC minutes as being more skewed to the hawkish side. However, we would regard this movement as transitory for the time being. If, on the one hand, it is true that the market seems to have bought the dollar strength story, on the other hand, we are still not observing an abrupt diversion of monetary policy expectations on the two sides of the Atlantic. This coupled with the uncertainty coming from the financial markets that still manage to threaten investors' mood (see the first part of this week in equity markets) will keep the EUR-USD around the current level in our view, at least in the near term. We have certainly come to a turning point in the EUR-USD path: it is only a matter of time for the greenback to appreciate further versus the EUR.

EUR-USD STABILIZING AFTER THE SHARP SLIDE



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MIB View – Our Global Picture

Global economy

- The ongoing financial market crisis and record-high commodity prices are taking their toll: The global economic slowdown is more pronounced than had been expected in late 2007. A global recession is, however, rather unlikely – although the risks have risen. At roughly 3½%, global GDP in 2009 will post its slowest growth since 2002 (2008: +3.8%, 2007:+4.8%).
- At the same time, global growth is becoming more balanced at lower levels. For the US, we expect real GDP growth in 2009 of a meager 1½%, while the eurozone economy should expand by only 1%. Emerging Asia and China continue to lead the growth rankings (2009: roughly +8%).

US

- GDP growth in H1 2008 was surprisingly solid. The services sector was still hiring, while the export sector profited from the weak USD. In addition, massive fiscal policy impulses also lent a helping hand. This will also be felt in Q3. But toward year-end, the US economy will barely grow. Nevertheless, a full-fledged recession seems unlikely.
- The Fed substantially tightened its anti-inflation rhetoric after having lowered its target rate by 325 bp since September 2007 to 2%. But the FOMC cannot hike the key rate – not yet. We expect the first move in December this year (+50 bp) followed by another 100 bp in 2009. This will help the real target rate out of negative territory. Therefore, the Fed tightening cycle in 2009 is just a normalization of monetary policy.

Eurozone

- After almost three years of sustained expansion, growth in 2008 will fall substantially below potential with +1.4% (2007: +2.6%). The reasons for the slowdown are tighter credit conditions, poorer consumer sentiment and the (after effects) of the EUR appreciation up until recently.
- Exports and investment will, therefore, be affected the most. Private consumption will probably hold its own. But at the same time, inflation continues to rise, driven by soaring oil and food prices. Discretionary spending is, therefore, being hit substantially. Core inflation is also drifting up. Higher inflation is fueling wage demands.
- Therefore, the ECB hiked its refi rate in early July by 25 pb to 4.25%, but will remain on the sidelines thereafter over the next few months. Ultimately however, the ECB will be forced to cut rates, although we now expect the

first step only in spring 2009. But the economic slowdown, and thus the easing cycle should be more pronounced than previously envisaged – not least because of the July refi rate hike.

Government bond markets

- Still substantial risk aversion combined with poor macro-economic and corporate news will see government bond yields stay around current levels for the time being.
- But as financial markets start to normalize this summer, US yields will rise again – although only gradually.
- Bund yields should also stay at their current low levels short term, but decline slightly over the rest of this year given our expectations that markets will start to price in rate cuts later on.

Exchange rates

- The EUR appreciation/USD depreciation seems to have come to an end. Short term, EUR-USD is expected to pull back further – helped by the expectation of ECB rate cuts in 2009. At the end of 2008, EUR-USD should trade at 1.45 followed by 1.38 in mid-2009.
- JPY will also weaken in the remainder of 2008 and in 2009.

OUR MACRO FORECASTS

in % y-o-y	2007	2008	2009
GDP EMU	2.6	1.4	1.0
CPI EMU	2.1	3.7	2.6
GDP Germany	2.6	1.7	0.9
CPI Germany	2.3	2.8	1.8
GDP Italy	1.4	0.1	0.4
CPI Italy	1.8	3.6	2.6
GDP US	2.2	1.6	1.4
CPI US	2.9	4.5	3.1

OUR FI, FX & OIL PRICE FORECASTS

2008/09	30-Sept	31-Dec	31-Mar	30-June
EMU 3M (%)	4.96	4.95	4.80	4.65
EMU 10Y (%)	4.15	4.10	4.00	3.90
US 3M (%)	2.85	3.05	3.50	3.65
US 10Y (%)	4.10	4.20	4.30	4.40
EUR-USD	1.49	1.45	1.42	1.38
USD-JPY	111	112	113	115
Oil Price	122	125	120	135

Macro Forecasts

GDP, real (% , y-o-y)	2002	2003	2004	2005	2006	2007	2008f	2009f
World economy *	2.9	3.8	4.9	4.4	5.0	4.8	3.7	3.5
Industrialized countries *	1.5	1.9	3.1	2.5	2.9	2.6	1.6	1.4
US	1.6	2.5	3.6	2.9	2.8	2.0	1.6	1.4
Euro area	0.9	0.8	1.9	1.8	2.9	2.7	1.4	1.0
Germany **	0.0	-0.2	0.7	1.0	3.2	2.6	1.7	0.9
France	1.1	1.1	2.2	1.9	2.4	2.1	1.1	1.0
Italy	0.5	0.0	1.4	0.7	1.9	1.4	0.1	0.4
Spain	2.7	3.0	3.2	3.5	3.9	3.8	1.5	0.8
Austria	0.9	1.2	2.3	2.0	3.3	3.3	2.3	1.3
UK	2.1	2.8	3.3	1.8	2.9	3.0	1.4	0.9
Switzerland	0.4	-0.2	2.5	2.4	3.2	3.1	2.1	1.2
Sweden	2.0	1.8	3.3	3.3	4.4	2.9	1.9	1.6
Japan	0.3	1.6	2.7	1.9	2.4	2.0	1.0	0.9
Developing countries *	5.3	6.6	7.8	7.5	8.1	8.2	7.0	6.6
Asia	6.9	8.1	8.6	9.0	9.6	9.7	8.2	7.9
China	9.1	10.0	10.1	10.4	11.1	11.5	9.8	8.1
India	4.6	6.9	7.9	9.1	9.7	9.2	7.9	8.0
Latin America	0.4	2.1	6.2	4.6	5.5	5.6	4.4	3.6
Brazil	2.7	1.1	5.7	3.2	3.8	5.4	4.8	3.7
Central and Eastern Europe	4.7	6.4	7.6	6.3	7.5	7.2	5.8	5.5
Russia	4.7	7.3	7.2	6.4	7.4	8.1	6.8	6.3

Consumer prices, CPI (% , y-o-y)	2002	2003	2004	2005	2006	2007	2008f	2009f
US	1.6	2.3	2.7	3.4	3.2	2.9	4.5	3.1
core rate (ex food & energy)	2.3	1.5	1.8	2.2	2.5	2.3	2.4	2.3
Euro area, HICP	2.2	2.1	2.1	2.2	2.2	2.1	3.7	2.6
core rate (ex food & energy)	2.4	1.8	1.8	1.4	1.4	1.9	1.8	1.8
Germany	1.4	1.0	1.7	1.6	1.6	2.3	2.8	1.8
France	1.9	2.1	2.1	1.7	1.7	1.5	3.2	2.0
Italy	2.5	2.7	2.2	1.9	2.1	1.8	3.6	2.6
Spain	3.1	3.0	3.0	3.4	3.6	2.8	4.6	3.0
Austria	1.7	1.3	2.0	2.1	1.7	2.2	3.1	2.2
UK	1.3	1.4	1.3	2.0	2.3	2.3	3.8	2.6
Switzerland	0.6	0.6	0.8	1.2	1.1	0.7	2.6	1.5
Sweden	2.2	1.9	0.4	0.5	1.4	2.2	3.8	3.1
Japan	-0.9	-0.2	0.0	-0.3	0.2	0.1	1.4	1.0

GDP, real (% , q-o-q)	I/07	II/07	III/07	IV/07	I/08f	II/08f	III/08f	IV/08f
US (annualized)	0.0	4.8	4.8	-0.2	0.9	1.9	1.3	0.3
Euro area	0.8	0.3	0.6	0.4	0.7	-0.2	0.2	0.3
Germany	0.4	0.4	0.6	0.3	1.3	-0.5	0.2	0.2
France	0.6	0.6	0.7	0.4	0.4	-0.3	0.2	0.3
Italy	0.3	0.0	0.2	-0.4	0.5	-0.3	0.0	0.0
Spain	1.0	0.9	0.7	0.8	0.3	0.1	-0.1	0.2
Austria	0.8	0.8	0.7	0.6	0.8	0.4	0.3	0.3
UK	0.7	0.8	0.6	0.6	0.3	0.2	-0.1	0.2
Switzerland	0.7	1.0	0.9	1.0	0.3	0.3	0.2	0.2
Sweden	0.5	0.7	0.6	0.8	0.4	0.4	0.3	0.3
Japan	1.0	-0.4	0.2	0.6	0.8	-0.6	0.3	0.2

Consumer prices, CPI (% , y-o-y)	I/07	II/07	III/07	IV/07	I/08f	II/08f	III/08f	IV/08f
US	2.4	2.6	2.4	4.0	4.2	4.3	5.1	4.4
core rate (ex food & energy)	2.6	2.3	2.1	2.3	2.4	2.3	2.4	2.4
Euro area, HICP	1.9	1.9	1.9	2.9	3.4	3.6	4.1	3.8
core rate (ex food & energy)	1.8	1.9	1.9	1.9	1.8	1.7	1.8	1.9
Germany	1.8	2.0	2.3	3.0	2.9	2.8	2.9	2.5
France	1.2	1.2	1.3	2.3	2.9	3.3	3.5	3.0
Italy	1.7	1.6	1.6	2.4	3.1	3.6	4.0	3.8
Spain	2.5	2.4	2.4	4.0	4.5	4.7	5.2	4.3
Austria	1.7	1.9	2.0	2.8	3.3	3.3	3.2	2.8
UK	2.8	2.6	1.8	2.1	2.4	3.4	4.8	4.7
Switzerland	0.1	0.5	0.6	1.7	2.5	2.6	2.7	2.4
Sweden	1.9	1.8	1.9	3.1	3.2	3.8	4.2	3.9
Japan	-0.1	-0.1	-0.2	0.5	0.9	1.4	1.6	1.4

Comments: * The GDP shares used for aggregation are based on the purchasing-power-parity (PPP) valuation of country GDPs
 GDP Gross Domestic Product, HICP Harmonized Index of Consumer Prices, CPI Consumer Price Index, f forecast, ** GDP growth unadjusted, 2008: 2.0%

Interest & Exchange Rate Forecasts (I)

INTEREST RATE FORECASTS (% , END QUARTER)

2008/09	current	end-Q3	end-Q4	end-Q1	end-Q2
Eurozone bond market					
Refi rate	4.25	4.25	4.25	4.25	4.00
3M Euribor	4.96	4.96	4.95	4.80	4.65
2Y	4.12	3.95	3.80	3.60	3.40
5Y	4.08	4.00	3.90	3.75	3.60
10Y	4.18	4.15	4.10	4.00	3.90
30Y	4.61	4.60	4.60	4.60	4.55
10Y swap spread (in bp)	52	45	40	40	40
US Treasury Market					
Fed funds target rate	2.00	2.00	2.50	3.00	3.00
3M USD Libor	2.81	2.85	3.05	3.50	3.65
2Y	2.32	2.85	3.10	3.60	3.80
5Y	3.08	3.50	3.70	4.00	4.20
10Y	3.84	4.10	4.20	4.30	4.40
30Y	4.47	4.65	4.75	4.80	4.85
10Y swap spread (in bp)	70	75	65	60	60
Japan					
Target rate	0.50	0.50	0.50	0.50	0.50
3M JPY Libor	0.87	0.80	0.80	0.80	0.80
10Y JGB	1.46	1.55	1.60	1.65	1.70
United Kingdom					
Repo rate	5.00	5.00	5.00	4.75	4.50
3M GBP Libor	5.76	5.80	5.70	5.40	5.10
10Y Gilt	4.57	5.15	5.10	5.00	4.80
Switzerland					
3M CHF Libor mid target rate	2.75	2.75	2.75	2.50	2.25
3M CHF Libor	2.75	2.75	2.75	2.50	2.25
10Y Swissie	2.87	3.40	3.30	3.20	3.00

EXCHANGE RATE FORECASTS (END QUARTER)

	current	end-Q3	end-Q4	end-Q1	end-Q2
EUR-USD	1.4860	1.49	1.45	1.42	1.38
EUR-JPY	162.09	165	162	160	159
EUR-GBP	0.7956	0.79	0.78	0.77	0.75
EUR-CHF	1.6201	1.62	1.62	1.60	1.60
USD-JPY	109.09	111	112	113	115
GBP-USD	1.8675	1.89	1.86	1.84	1.84
USD-CHF	1.0903	1.09	1.12	1.13	1.16

COMMODITY PRICE FORECASTS

	current	end-Q3	end-Q4	end-Q1	end-Q2
Oil price (Brent, USD/b)	120.64	122	125	120	135
DJ-AIG commodity price index	396.43	460	470	480	490

Interest & Exchange Rate Forecasts (II)

INTEREST RATE FORECASTS (% , END QUARTER)

2008/09	current	end-Q3	end-Q4	end-Q1	end-Q2
Sweden					
Key rate	4.50	4.75	4.75	4.75	4.75
3M rate	5.12	5.30	5.30	5.20	5.20
10Y government bond yield	4.10	4.60	4.60	4.50	4.40
10Y spread to Bunds (in bp)	-7	45	50	50	50
Norway					
Key rate	5.75	5.75	5.75	5.75	5.75
3M rate	6.55	6.40	6.30	6.25	6.25
10Y government bond yield	4.67	4.80	4.70	4.60	4.50
10Y spread to Bunds (in bp)	49	65	60	60	60
Canada					
Key rate	3.00	3.00	3.00	3.00	3.25
3M rate	3.34	3.60	3.60	3.60	3.80
10Y government bond yield	3.60	3.70	3.80	3.90	4.00
10Y spread to Bunds (in bp)	-58	-45	-30	-10	10
Australia					
Key rate	7.25	6.75	6.25	6.00	5.75
3M rate	7.35	7.20	6.60	6.40	6.10
10Y government bond yield	5.79	5.95	5.70	5.60	5.60
10Y spread to Bunds (in bp)	162	180	160	160	170
New Zealand					
Key rate	8.00	7.50	7.00	6.75	6.50
3M rate	8.30	7.90	7.40	7.10	7.80
10Y government bond yield	6.09	6.00	5.80	5.70	5.60
10Y spread to Bunds (in bp)	192	185	170	170	170

EXCHANGE RATE FORECASTS (END QUARTER)

	current	end-Q3	end-Q4	end-Q1	end-Q2
EUR-SEK	9.3660	9.35	9.30	9.25	9.20
EUR-NOK	7.9351	7.95	7.89	7.86	7.78
EUR-CAD	1.5496	1.58	1.57	1.55	1.53
EUR-AUD	1.6972	1.69	1.71	1.71	1.70
EUR-NZD	2.0779	2.07	2.07	2.09	2.06
USD-SEK	6.3029	6.28	6.41	6.51	6.67
USD-NOK	5.3402	5.34	5.44	5.54	5.64
USD-CAD	1.0429	1.06	1.08	1.09	1.11
AUD-USD	0.8755	0.88	0.85	0.83	0.81
NZD-USD	0.7152	0.72	0.70	0.68	0.67
EUR-USD	1.4860	1.49	1.45	1.42	1.38

Economic Event & Data Release Calendar

Date	Time (ECB)	Country	Indicator	Period	MIB est.	Consensus (Bloomberg)	Prev. period
22 August to 29 August 2008							
Fri, 22 Aug '08	16:00	US	Fed's Bernanke Speaks on Financial Stability at Jackson Hole				
Mon, 25 Aug '08	8:00	JN	BOJ Governor Shirakawa to Speak in Osaka				
	8:00	GE	Import price index (in % y-o-y)	Jul	9.4	9.2	8.9
	8:00	GE	Import price index (in % m-o-m)	Jul	0.7	0.5	1.5
	16:00	US	Existing home sales (in mn)	Jul	5.0	4.9	4.9
Tue, 26 Aug '08		UK	House price (Nationwide, in % y-o-y)	Aug		-9.6	-8.1
	8:00	GE	Real GDP (in % y-o-y)	Q3	1.7	1.7	1.7
	8:00	GE	Real GDP (in % q-o-q)	Q3	-0.5	-0.5	-0.5
	8:10	GE	GfK consumer confidence	Sep	2.3	2.0	2.1
	8:45	FR	Building permits (in % y-o-y, smoothed)	Jul			-15.3
	8:45	FR	Housing starts (in % y-o-y, smoothed)	Jul			-28.2
	10:00	GE	ifo business climate (index)	Aug	97.2	97.2	97.5
	15:00	US	S&P/Case-Shiller home priceindex (in % y-o-y)	Jun	-16.2	-16.2	-15.8
	16:00	US	Conference Board consumer confidence	Aug	53.0	53.0	51.9
	16:00	US	New home sales (in thousands)	Jul	525.0	525.0	530.0
	16:00	US	OFHEO house price index (in % m-o-m)	Jun		-0.4	-0.3
Wed, 27 Aug '08	9:25	EMU	ECB's Papademos Speaks in Buenos Aires				
	9:30	IT	Consumer confidence (ISAE, index)	Aug	97.5	96.6	95.8
	13:00	US	MBA mortgage applications	Aug 22			-1.5
	14:30	US	Durable goods orders ex transportation (in % m-o-m)	Jul		-0.5	2.0
	14:30	US	Durable goods orders (in % m-o-m)	Jul	0.2	0.1	0.8
	14:35	US	Atlanta Fed's Lockhart to Speak on Inflation at Georgia State				
	17:30	SZ	SNB's Hildebrand Holds Speech in Zurich				
Thu, 28 Aug '08		GE	Consumer price index, CPI (national, in % y-o-y)*	Aug	2.9	3.2	3.3
		GE	Consumer price index, CPI (national, in % m-o-m)*	Aug	-0.5	-0.2	0.6
	3:30	JN	BOJ Board Member Suda to Speak in Kanazawa, Japan				
	9:55	GE	Unemployment rate (in %)	Aug	7.8	7.8	7.8
	9:55	GE	Unemployment change (in thousands)	Aug	-15.0	-10.0	-20.0
	10:00	IT	Producer price index, PPI (in % y-o-y)	Jul		8.8	8.2
	10:00	GE	Retail PMI	Aug			46.4
	10:00	EMU	Retail PMI	Aug			46.0
	10:00	EMU	M3 money supply (in % y-o-y, 3M moving average)	Jul		9.5	9.9
	10:00	EMU	M3 money supply (in % y-o-y)	Jul	9.8	9.0	9.5
	11:00	EMU	European Commission economic sentiment (index)	Aug	89.1	88.9	89.5
	11:00	EMU	European Commission consumer confidence climate (index)	Aug		-20.0	-19.7
	11:00	EMU	European Commission business climate (index)	Aug		-0.4	-0.2
	14:30	US	PCE deflator (in % q-o-q annualized)	Q2		2.1	2.1
	14:30	US	Real GDP (in % q-o-q annualized)	Q2	2.8	2.8	1.9
	14:30	US	Initial jobless claims (in thousands)	Aug 22	430.0		432.0
	18:00	EMU	ECB's Bini Smaghi Speaks at Conference in Cortina, Italy				
Fri, 29 Aug '08	1:01	UK	Consumer confidence (GfK, index)	Aug		-41.0	-39.0
	1:15	JN	PMI (Nomura)	Aug			47.0
	1:30	JN	Unemployment rate (in %)	Jul		4.1	4.1
	1:30	JN	Core consumer price index (in % y-o-y)	Jul		0.1	0.1
	1:30	JN	Consumer price index (in % y-o-y)	Jul		2.2	2.0
	7:00	JN	Tankan survey small business	Aug			39.9
	10:00	EMU	ECB's Klaus Liescher Holds Closing Press Conference in Vienna				
	10:00	IT	Retail sales (in % m-o-m)	Jun		-0.1	0.2
	11:00	IT	Consumer price index (in % y-o-y)	Aug	3.8	4.0	4.1
	11:00	EMU	Consumer price index, CPI (in % y-o-y, flash estimate)	Aug	3.9	3.9	4.1
	11:00	EMU	Unemployment rate (in %)	Jul	7.3	7.3	7.3
	11:30	SZ	KOF business climate	Aug		0.8	0.9
	14:30	US	PCE core inflation (in % m-o-m)	Jul	0.3	0.3	0.3
	14:30	US	Personal expenditures (in % m-o-m)	Jul		0.3	0.6
	14:30	US	Personal income (in % m-o-m)	Jul	-0.7	0.0	0.1
	15:45	US	Chicago Purchasing Managers Index	Aug		49.8	50.8
	16:00	US	University of Michigan consumer confidence	Sep		62.0	61.7

*: Asterisked releases are scheduled on or after the date shown sa = seasonal adjusted, nsa = not seasonally adjusted, wda = working day adjusted

Economic Event & Data Release Calendar – The week after

Date	Time (ECB)	Country	Indicator	Period	MIB est.	Consensus (Bloomberg)	Prev. period
01 September to 05 September 2008							
Mon, 01 Sep '08		UK	House price (HBOS, in % 3M y-o-y)	Aug			-8.8
	9:30	SZ	Manufacturing PMI (index)	Aug			54.1
	9:45	IT	Manufacturing PMI (index)	Aug			45.3
	9:50	FR	Manufacturing PMI (index)	Sep			45.1
	9:55	GE	Manufacturing PMI (index)	Sep			49.9
	10:00	IT	Large industry employment (in % y-o-y)	Jun			-0.1
	10:30	UK	Mortgage approvals (in thousands)	Jul			36
	10:30	UK	Manufacturing PMI (index)	Aug			44.3
	18:00	IT	New car registration (in % y-o-y)	Aug			-10.88
	19:00	IT	Budget balance (EUR bn)	Aug			2.2
	20:45	US	Fed's Hoenig Speaks in Argentina on Financial Turmoil				
Tue, 02 Sep '08	3:00	JN	BOJ Governor Shirakawa to Speak in Nagoya				
	7:45	SZ	Real GDP (in % q-o-q)	Q2			0.3
	7:45	SZ	Consumer price index (in % y-o-y)	Aug			3.1
	7:45	SZ	Consumer price index (in % m-o-m)	Aug			-0.4
	9:45	SZ	Real GDP (in % m-o-m)	Q2			3
	11:00	EMU	Producer price index, PPI (in % y-o-y)	Jul			8
	11:00	EMU	Producer price index, PPI (in % m-o-m)	Jul			1
	16:00	US	Construction spending (in % m-o-m)	Jul			-0.4
	16:00	US	ISM manufacturing (index)	Aug	50.0		50.0
	18:30	SZ	SNB's Jordan Holds Speech in Bern				
Wed, 03 Sep '08	9:30	IT	Business confidence overall (ISAE, index)	Aug			83.5
	9:45	IT	Services PMI (index)	Aug			45.6
	9:50	FR	Services PMI (index)	Sep			48.5
	9:55	GE	Services PMI (index)	Sep			50.6
	10:00	EMU	Composite PMI (index)	Sep			48
	10:00	EMU	Services PMI (index)	Sep			48.2
	10:00	EMU	Manufacturing PMI (index)	Sep			47.5
	10:30	UK	Services PMI (index)	Aug			47.4
	11:00	EMU	Private consumption (in % q-o-q)	Q2			0.2
	11:00	EMU	Government consumption (in % q-o-q)	Q2			0.4
	11:00	EMU	Gross fixed capital formation (in % q-o-q)	Q2			1.6
	11:00	EMU	Real GDP (in % q-o-q)	Q3			1.5
	11:00	EMU	Real GDP (in % y-o-y)	Q3			-0.2
	11:00	EMU	Retail sales (volume, in % m-o-m)	Jul			-3.1
	16:00	US	New orders (in % m-o-m)	Jul			1.7
	20:00	US	Fed Releases Beige Book Economic Report				
Thu, 04 Sep '08	12:00	GE	Industrial orders (in % m-o-m)	Jul			-2.9
	13:00	UK	Bank of England repo rate (in %)	Aug 22		5	5
	13:45	EMU	ECB refi rate (in %)	Jan 1			4.25
	14:15	US	ADP employment index (change in thousands m-o-m)	Aug			9
	14:30	US	Initial jobless claims (in thousands)	Aug 29	425		
	14:30	US	Unit labor costs (in % q-o-q annualized)	Q3			1.3
	14:30	US	Non-farm productivity (in % q-o-q annualized)	Q3			2.2
	16:00	US	ISM Non-manufacturing (index)	Aug	49.5		49.5
	20:00	US	Fed's Yellen Speaks in Salt Lake City on U.S. Economy				
Fri, 05 Sep '08	8:45	FR	Budget balance (EUR bn)	Jul			-32.814
	8:50	EMU	ECB's Trichet, Stark, Bini Smaghi Speak in Frankfurt				
	10:00	IT	Trade balance (EUR bn)	Jun			-59.9
	12:00	GE	Industrial production (in % m-o-m)	Jul			0.2
	14:30	US	Average weekly hours	Aug			33.6
	14:30	US	Average hourly earnings (in % m-o-m)	Aug			0.3
	14:30	US	Unemployment rate (in %)	Aug	5.6		5.7
	14:30	US	Non-farm payrolls (change in thousands m-o-m)	Aug	-60		-51
	21:55	US	Fed's Yellen Speaks in Los Angeles on U.S. Economy				

*: Asterisked releases are scheduled on or after the date shown sa = seasonal adjusted, nsa = not seasonally adjusted, wda = working day adjusted

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