

2nd quarter 2009

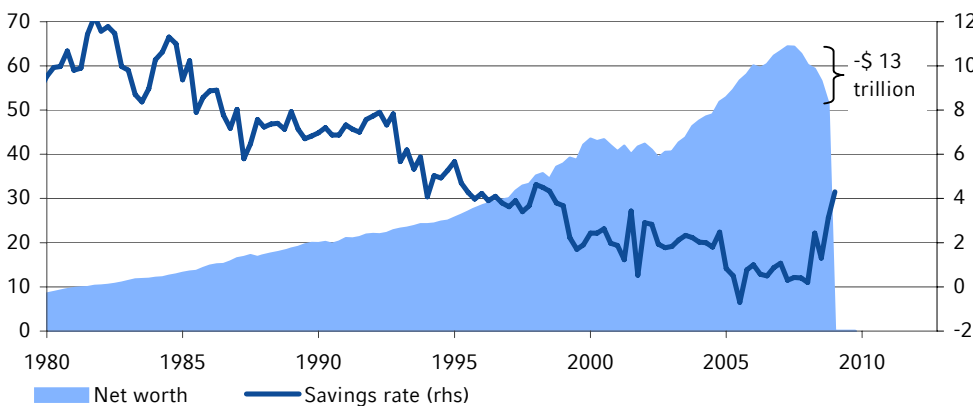
Economic Trends



- **USA: Sustained reanimation of the economy**
- **Germany: Dramatic collapse, unusual recovery**
- **Bond Market: Between two extremes**

Who's afraid of big numbers? The Fed could increase its balance sheet to US\$4 trillion in an attempt to reanimate the financial system. Other balance sheets, for example those of US households, are currently contracting rapidly: falling house and share prices have cut their net worth (assets minus debt) by 20% or US\$13 trillion since 2007. People wanting to accrue assets are going to have to think about saving again. The savings ratio is likely to continue to increase, which would be bad for consumption, but necessary if global imbalances are to be unwound.

USA: Net worth and savings ratio of households
US\$ trillions and % of disposable income



Source EcoWin, WestLB Research

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Editorial

The global patient

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The job of economists is to describe, explain, forecast and advise. It is common knowledge that forecasting is currently a particularly difficult task; nevertheless, this is what we attempt to do in every other section of our Economic Trends. But first of all we would like to draw an analogy – an image, so to speak – that may help to describe and explain the current situation of the global economy and the financial markets, and the way in which economic policy is responding.

The patient is seriously ill

The patient, i.e. the global economy and parts of the financial system, is in intensive care. A host of doctors – experts from every area of specialisation – are intently examining the patient, and they all agree in principle: this is someone who has overindulged over a period of many years, has lost his sense of balance and has ultimately suffered a severe fall – the price paid for pushing himself for far too long. Some of the doctors admit that they unwittingly contributed to such an excessive lifestyle by giving the wrong advice. Things did not look so bad only a few months ago. But the patient's state of health has deteriorated rapidly since last autumn, and it is now clear that he is suffering from a severe and protracted illness, one that is complex and rare and not fully understood. Less serious cases of this illness have occurred from time to time: Japan had a serious bout of it in the 1990s, and another case ended in a catastrophe in the years after 1929.

There is basically agreement on the therapy, but opinions differ on the details

The specialists in attendance basically agree on the appropriate therapy: it is necessary to give stimulants to ensure revival in the short term, and in the long term it is essential that the patient adopt a healthier lifestyle. For everything else the following principle applies: ask any three doctors for their opinion and you're sure to get at least three different answers. The controversy about correct dosages is a case in point: some experts believe in administering massive amounts of stimulants, guided by the motto 'a lot helps a lot'. These include unconventional remedies that have seldom been tested before, and even when they have – for example, in Japan – then only with limited success. These medications are extremely expensive, and the risks and the possible side-effects are enormous. But what counts first and foremost is making sure that the patient does not come to even greater harm, whatever the cost may be. Other experts warn that the effects of such an indulgent lifestyle cannot be cured simply by administering excessive doses of stimulants. Rather, the patient has to change his lifestyle, build up reserves, take fewer risks and submit to stricter supervision. But what is to be regulated, how much regulation is needed, and what are the side-effects?

Conference is a success, but the patient is still ill

The doctors have convened a series of high-level conferences to discuss these issues, and have come to a decision. During a quiet evening by the fireside, they own up to how little they all know about the ailment and how unsure they are of the course it will take. They try to hide this from the outside world to avoid panic from spreading. Moreover, experts do not voice doubt in public. Despite their differences of opinion, vaguely worded communiqués are the best way to find a (i.e. the lowest) common denominator.

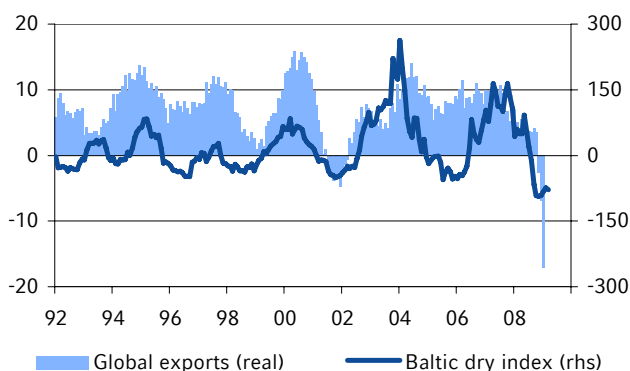
General public plagued by uncertainty

The general public is plagued by uncertainty. People cannot understand how things could get this far out of hand, and they cannot assess the effects, costs, risks and side-effects of this therapy. And they will have to face up to the fact that all the experts' prognoses so far about the course of the ailment have been too optimistic. Maintaining a sense of confidence and optimism under these circumstances is difficult, but urgently necessary.

Macro outlook – summary of the key points

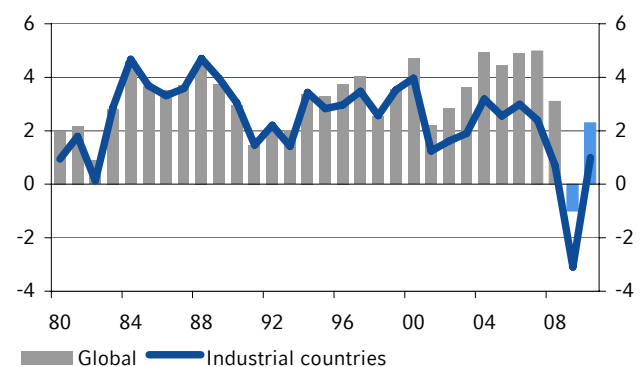
- World economy:** We expect global economic output to contract by 1.1% this year (industrialised states -3.2%; emerging and developing countries +1.2%). This may not sound much, but it is in fact unprecedented in the post-war period. Some indicators that have risen several times of late, such as the Ifo expectations, the ISM index for the manufacturing sector in the USA and the corresponding index for China, support our expectation that the economies of many industrialised states will cease to contract in Q4 at the latest. We thereby presuppose that a meltdown of the financial system will continue to be avoided, that conditions will gradually improve, and that only then will the low key rates and the stimulus packages start to take effect. When the recovery comes, it may be more or less a 'forced' and unsustainable recovery. The years of plenty and stability for the world economy are over.

Freight rates and global exports
%, y-o-y



Source EcoWin, WestLB Research

Economic growth
%, y-o-y



Source EcoWin, WestLB Research forecasts

- USA:** The predominantly weak economic data confirm that economic activity in the first quarter of this year continued to slow. Nevertheless, the first rays of light are appearing. Some key sentiment indicators have moved slightly off their lows. The order situation has also improved somewhat for the first time in half a year; this lends support to the expectation that the downturn is gradually decelerating. As key drivers such as consumption, foreign trade and investments are all weak, economic policy is pulling out all the stops to kick-start the economy. Given the massive fiscal and monetary stimuli, we still believe there is a chance of a slow, fairly weak recovery in H2.
- Eurozone:** The severe contraction in eurozone economic output is likely to continue in H1. However, some indicators such as the PMIs are beginning to bottom out. Fiscal stimuli should bring about at least a weak rise in aggregate production in the second half of the year, as the stimulus packages are currently still being expanded. Impetus from government and private consumption can therefore be expected in H2. Overall GDP may decline by 2.8% this year and grow weakly by 1.0% in 2010.

- **Germany:** The economy is currently in the midst of an unprecedented downturn, driven by the collapse in industry. We still expect the economy to steady during the latter part of the year – as ifo business expectations, for example, are indicating. We expect GDP to contract by 3.5% for the full year 2009, and we believe 1% growth is attainable in 2010. If it turns out that economic output shrank by even more in the first few months of this year than at the end of 2008, we will have to revise our 2009 forecast downward.
- **Emerging markets:** All regions are affected by the downturn. Among the BRIC states, signs are pointing to recession in Russia and Brazil and to a marked slowdown in growth in China and India. In our view neither Asia, Central and Eastern Europe, nor Latin America will be able to drive a recovery. Economic activity in these countries may not revive on a sustained basis until demand in the industrialised states picks up and more private capital starts flowing into the emerging economies.
- **Fixed-income markets:** We expect the ECB's key rate to bottom out at 1%. Long-term bond yields are torn between economic weakness on the one hand, and the high funding requirements of governments combined with fears of long-term inflation on the other. We expect yields on 10Y Bunds to move in a band between 2.8% and 3.3% over the coming months. If our economic scenario of a subdued recovery from the second half of the year proves correct, only high yields would be compatible with it. Our 12-month forecast remains unchanged at 3.8%.
- **Foreign exchange markets:** The huge uncertainties about economic trends and the stability of the financial system are reflected in marked volatility in many currencies. The support measures in the USA and the UK are likely to benefit the dollar and sterling. However, we remain sceptical about the greenback in the longer term, given the enormous structural imbalances. The deep recession in Japan will probably weigh increasingly on the yen. We believe the Swiss franc could continue to depreciate slightly. Bleak economic prospects, interest rate cuts and unresolved payment problems may mean that important Central European currencies will tend to show weakness.
- **Oil market:** The steep drop in oil prices over recent months has come to a halt. Prices have moved sideways since the start of the year, albeit with high level of volatility. In our view, the latest leap in oil prices over the \$50 mark will not be sustainable at the present time. There are plenty of arguments pointing to crude prices rising at only a moderate pace in the future.

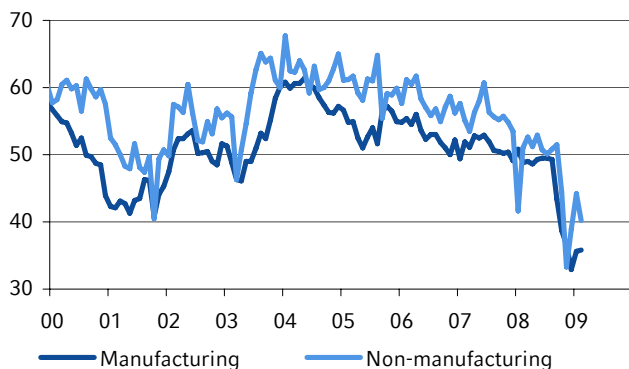
USA

Sustained reanimation of the US economy

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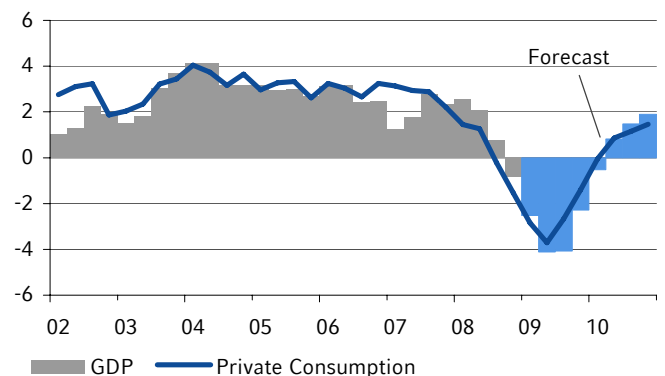
The prevalingly negative economic figures are increasingly confirming that economic activity slowed significantly again in the first quarter of this year. Following the severe slump in the final quarter of 2008, the economy is now threatening to slide yet further into recession. Despite the fact that the economic picture is very gloomy at the moment, there are nevertheless some signs of light at the end of the tunnel. Some important sentiment indicators have edged up off their lows, fuelling hopes that the pace of the downturn is set to slow gradually. Nevertheless, important driving forces such as private consumption, foreign trade and capital expenditure are still lacking, so the U.S. government and the Fed are pulling all the levers to get the economy moving again. The next few months will show whether their attempts at reanimation are a success. Given their massive fiscal and monetary policy stimuli, we continue to see a chance of a slow and tentative recovery in the second half of the year.

ISM indices
in points



Source EcoWin, WestLB Research

Real GDP and private consumption
in % y-o-y



Source EcoWin, WestLB Research forecast

No prospect of improvement until the financial system stabilises

The financial sector remains pivotal here, however. We do not believe there will be any sustained economic recovery until it stabilises. For this reason, the politicians are very sharply focused on reviving lending, which has seized up. The US central bank has been relying increasingly here on unconventional monetary policy measures ('credit easing') since it cut the key rate to near zero. Besides providing generous amounts of liquidity and lendings to banks, it is concentrating on buying up securities such as commercial paper and securities backed by mortgages and other forms of credit (MBS, ABS).

The Fed has expanded its purchasing programme enormously

Some of the programmes are far from being exhausted. Several have not really got going yet and have not, therefore, been able to have much of an impact so far. Cases in point are the MBS programme, and especially the Term Asset-Backed Securities Lending Facility (TALF), which can furnish up to one trillion dollars of liquidity for loans to consumers and smaller companies. Nevertheless, true to the motto 'think big' the Fed has opted for another huge increase in the size of its programme for buying-up agency securities and mortgage-backed bonds in order to lend further support to the mortgage-lending and housing markets.

But this does not mean that the US central bank's tool box is empty yet. Following in the footsteps of the UK, it now intends to purchase US Treasuries (up to \$300bn in the next six months) in order to exert indirect downside pressure on interest rates in other segments of the capital and credit markets.

New programmes – use and authorisation

| Assets supplying reserves | Announced authorisation (in \$bn) | Week ending: 25.3.2009* |
|--|--------------------------------------|-------------------------|
| US Treasuries | 300 | 474.7 |
| Agency Debt (Fannie Mae, Freddie Mac etc.) | 200 | 50.4 |
| Mortgage-backed securities | 1,250 | 236.2 |
| Term Auction Facility | 600 | 468.6 |
| Primary Dealer Credit Facility (PDCF) | No announced limit | 20.2 |
| Asset-Backed Commercial Paper (ACBCP) Money Market Mutual Fund (MMMF) Liquidity Facility (AMLF) | No announced limit | 6.8 |
| Loans to AIG | 60 | 43.2 |
| Term Asset-Backed Securities Lending Facility (TALF) | 1000 | 4.7 |
| Commercial Paper Funding Facility | No announced limit | 241.3 |
| Money Market Investor Funding Facility (MMIFF) | 540 | 0 |
| Maden Lane I (Assets from Bear Stearns) | 29 | 26.3 |
| Maden Lane II (Purchase of MBS from AIG) | 22,5 | 18.5 |
| Maden Lane III (Purchase of CDOS) | 30,0 | 27.6 |
| Central Bank Liquidity Swaps | No announced limit | 327.8 |

* Averages of daily figures

Source US Federal Reserve Bank, WestLB Research

Taking toxic assets off the banks' balance sheets ...

All these measures do not, however, solve the banking system's core problem: the negative impact that the large volumes of troubled assets are having on banks' balance sheets. On 23 March US Treasury Secretary Tim Geithner gave concrete details of his long-awaited balance-sheet detox plan. The Private-Public Partnership Investment Program, which is to be launched with funds of between \$75bn and \$100bn drawn from the existing TARP bailout package, is supposed to free banks of toxic and illiquid securities initially totalling \$500bn, subsequently rising to as much as \$1 trillion. Nationalisation of the banks will be avoided as far as possible. A large part of the risk involved in buying such assets is to be borne by the state and the deposit insurance agency, the FDIC. Private investors, by contrast, enjoy the prospect of relatively risk-free profits.

... increases the probability that the financial sector will stabilise

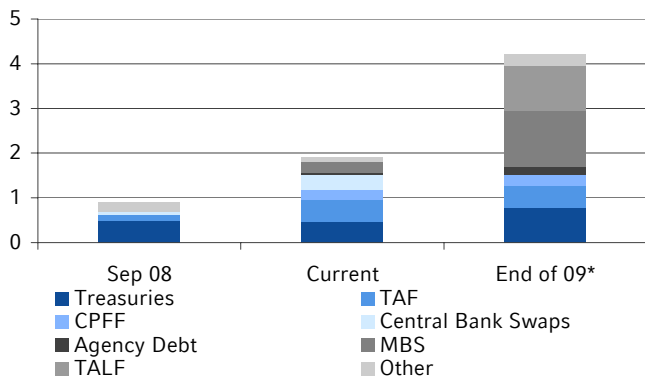
It is still too early to predict the repercussions of all these measures on the financial economy and ultimately on the real economy. It remains unclear whether the incentives will be enough to attract sufficient private capital, whether the banks will be able to get rid of their toxic assets and restore their ability to lend. It is also uncertain how long it will take before the measures bite. Despite these uncertainties, we believe there is an increased probability that lending will recover gradually in the USA. Combined with the \$789bn economic stimulus package launched by the government in February, this increased lending is likely to lead to a stabilisation and a slight recovery in the US economy in the second half of the year. Overall, however, aggregate economic output will probably contract by over 3% this year. We assume that US households will go through a longer phase of consolidation, so private consumption will not be able to develop the momentum needed to drive the US economy. For the coming year we therefore expect growth of just 1%.

Liquidity glut and inflation worries

Massive inflation of the Fed's balance sheet

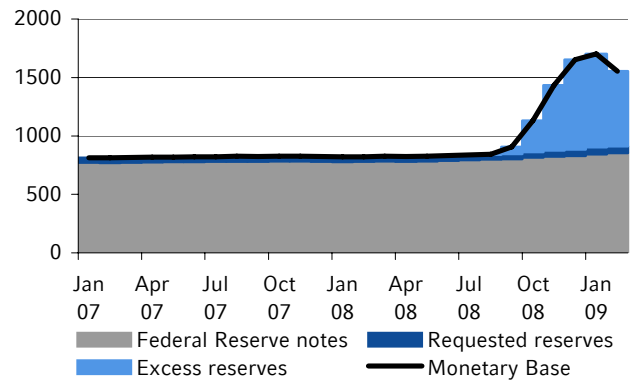
The huge increase in the Fed's operations has led to a substantial lengthening and structural change of its balance sheet. Before the financial crisis broke, the asset side of the US central bank's balance sheet consisted mainly of US government bonds (over 80%). These now account for only one quarter of its balance sheet. The short-term credit facility TAF accounts for a good one quarter, commercial paper for one tenth, swap transactions with other central banks for one sixth. If all the measures that have been announced recently are fully utilised, the Fed's balance sheet would more or less double. Compared to the beginning of September 2008 – in other words before the Lehman insolvency – it would increase fourfold.

Fed's balance sheet
in \$bn



Source EcoWin, *WestLB Research forecasts

Monetary base and components
in \$bn

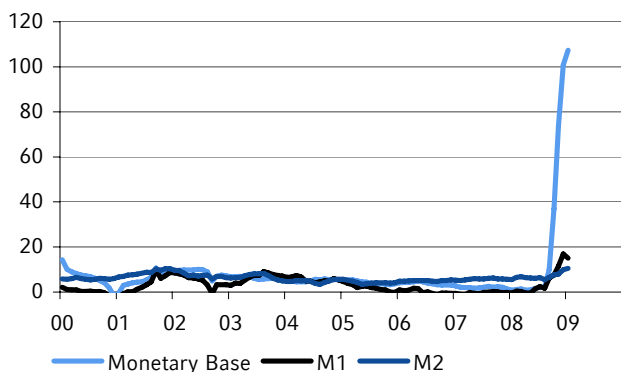


Source EcoWin, WestLB Research

... and the monetary base

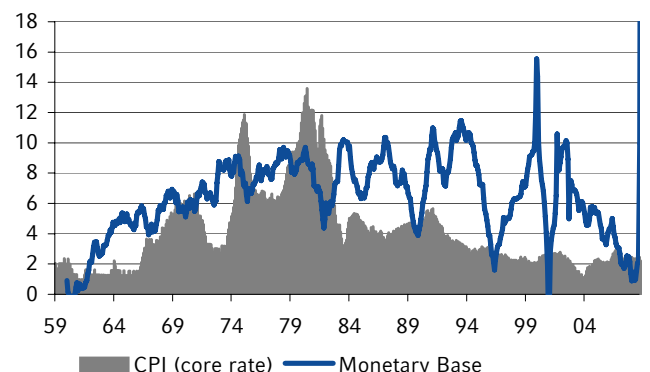
The generous provision of liquidity by the Fed together with its various purchasing programmes have already led to a huge increase in the supply of central bank funds in the narrowest definition – the so-called monetary base. The year-on-year increase in the monetary base, which is made up of the required reserves the banks are obliged to hold together with the excess reserves deposited voluntarily with the Fed and cash, is now over 100%. The increases in other, broader monetary aggregates such as M1 or M2 are, by contrast, far smaller at 'only' 15% and 10%.

Monetary aggregates
in % y-o-y



Source EcoWin, WestLB Research

Monetary base and core CPI 1959 to 08/2008
in % y-o-y



Source EcoWin, WestLB Research

All this is increasingly stoking concern that the liquidity glut induced by the Fed will lead sooner or later to a steep increase in inflation. Some even see a risk of hyperinflation. In our view, although these inflation worries are not fully unfounded and inflation rates may even overshoot temporarily in the longer term, we believe fears of a dramatic increase in inflation or even hyperinflation are overdone.

In the short term the risks of deflation are greater than a revival of inflation

Under normal circumstances the combination of debt-funded support packages for the economy and the banks and ultra-loose monetary policy (low key rates, liquidity glut) leads sooner or later to (high) inflation. If central banks feed excess liquidity into the banking system at extremely low interest rates they create a risk of inflation, if the banks lend generously to fund consumer spending and capital expenditure. So far, however, many banks have been lending little, partly due to the slackening demand for credit caused by the economic downturn. Instead of lending, they have been reinvesting their borrowed and excess liquidity with the Fed. At the moment, the banks' deposits with the Fed add up to almost \$800bn. Before the crisis they were no more than \$10bn to \$30bn.

So far, therefore, the liquidity has not found its way into the real economy. The fiscal policy stimuli are small compared to the current demand shortfall and inflation is unlikely to increase as long as capacity is not fully utilised. In the short term we rate the danger of deflation as far greater than that of a resurgence of inflation.

In the medium term inflation could possibly rise steeply

The risk that inflation will increase steeply in the medium to longer term cannot be ruled out, however. As soon as the economy finds its feet again and the crisis in the financial markets has been overcome, monetary and fiscal policy will have to rein in the expansionary stimuli. Fiscal policy will have to reduce the high budget deficit and debt. As a rule, however, it is impossible to push through tax increases and expenditure cuts fast. It is 'easier' to turn monetary policy around as the decision lags are far shorter. Fed Chairman Ben Bernanke has sketched out the exit strategy in several speeches: the Fed intends to throttle back the liquidity supply and will also raise the key rate sooner or later. Some of the newly-created instruments are designed to reduce the liquidity supply automatically due to their limited and – in some cases – short maturities. As the situation eases in the credit markets, individual credit programmes can be wound down, which will lead to a contraction of the central bank's balance sheet. Where possible, the Fed has already set loan interest and other conditions in such a way that the loans will become increasingly unattractive for borrowers when the markets return to normal. In addition, since October 2008 – when it was authorised to pay interest on balances held with it – the Fed has had an instrument that is intended to make holding required and excess reserve balances attractive.

Most difficult thing: timing and pace of the exit-strategy

The most difficult thing will be to time the exit correctly and to judge the pace at which and extent to which business is reverting to normal. The politicians cannot be sure that the turnaround has really been achieved at a certain point in time. If they wait too long, there is a danger that inflation rates will temporarily overshoot levels that could otherwise have been avoided. The US central bank will then have to use the key rate to steer against this accordingly.

Eurozone

In step with the USA

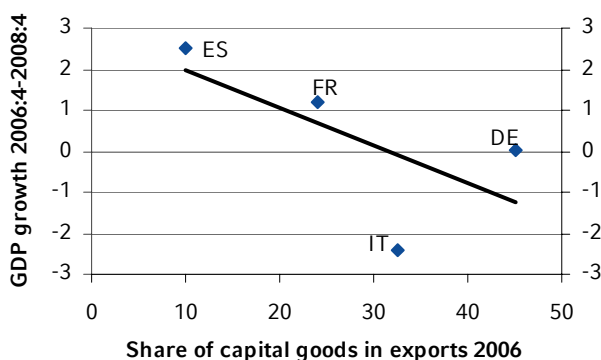
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The eurozone economy went on to collapse towards the end of last year, having slipped into recession in the spring of 2008. Gross domestic product contracted 1.5% q-o-q in Q4. Slowing foreign trade was responsible for most of this, accounting for 0.9 percentage point of the decline in output. This underlines that the present global recession is having a particularly negative impact on exports of manufactured goods, especially of capital goods. The concentration on capital goods was an advantage in the previous upturn – and one from which Germany, for example, benefited. However, it has become a disadvantage in the present recession due to the severe downturn in global demand for capital goods.

Unwanted inventory
accumulation at the companies

The sharp downturn in the global economy in the fourth quarter seemed to take eurozone companies by surprise. According to a survey carried out by the European Commission, manufacturing companies said their inventories were too high, but their stocks nevertheless increased by more than they wished in the final quarter of 2008. This bodes ill for the beginning of 2009, since companies are likely to be all the more intent on depleting their stocks to hand.

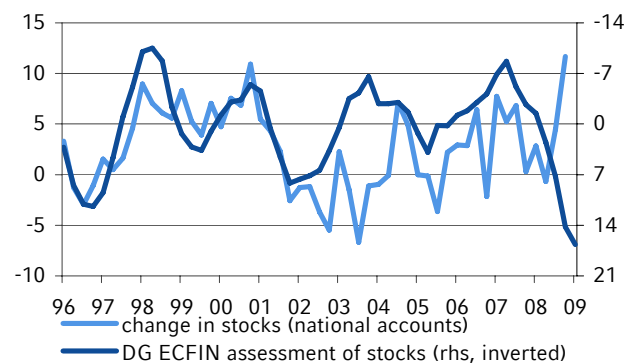
Capital goods as % of exports, and GDP growth



Source EcoWin, WestLB Research

Assessment of stocks in manufacturing industry, and accumulation of inventory

index points (normalised) and €bn



Source EcoWin, WestLB Research

Private consumption likely to
stagnate this year

Much will depend initially on private consumption, but households already reduced their spending last year. There is no sign of consumer spending recovering for the time being, and it is unlikely to stage a turnaround until household expectations for economic growth and for jobs improve. According to a recent survey, this is not yet the case. Incomes are likely to post sluggish growth for the rest of the year, since the unemployment rate has now risen steeply in the eurozone and is probably above its inflation-equilibrium level – the so-called NAIRU. Consumption will therefore probably stagnate this year. With investments and exports also slowing, a relatively severe downturn is looming in the eurozone. We expect GDP to contract by 2.8%.

Is an upturn without the USA possible in the current situation? In previous cycles, the US economy led the eurozone economy by several quarters. The fact that the eurozone went into recession in Q2 last year, before the USA, may therefore be surprising at first sight.

But quarterly rates of change in gross domestic product are very volatile and must always be seen in relation to trend growth, which is higher in the USA than in the eurozone.

Conspicuous parallel between the eurozone and the USA

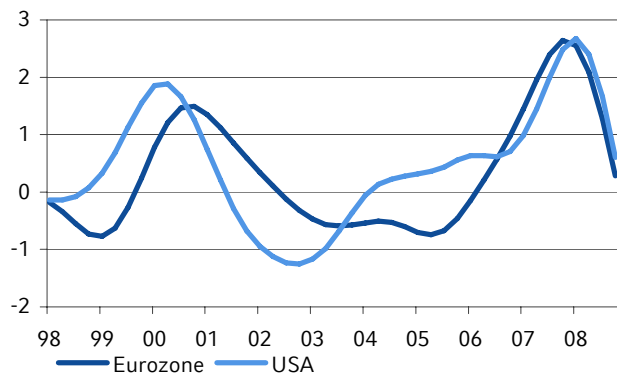
Based, therefore, on the long-term trend of GDP growth rate, the current cycle shows a conspicuous parallel between the USA and the eurozone. The positive output gap in both currency zones, which is created when growth is above the trend rate, was almost closed towards the end of last year. Thus the downturn in the USA – in terms of the trend growth rate – was comparable to that in the eurozone. This parallel between the two economies is plausible – after all, the financial markets crisis has been a global shock, in the course of which banks' earnings have suffered world-wide. This makes it clear that the economies will only be able to recover in step with each other, namely when the crisis in the financial markets abates.

Inflation to fall below zero in the summer

Little inflationary pressure until well into next year

The inflation rate has already come down significantly as a result of the fall in the oil price. In February it was 1.2%, which was 2.8 percentage points below the peak charted in summer 2008. The oil price has now stopped falling; thus energy prices may be expected to drive month-on-month inflation rates higher in individual months. But inflation on a year-on-year basis is likely to continue to fall until some time in the summer, and may even fall below zero at times.

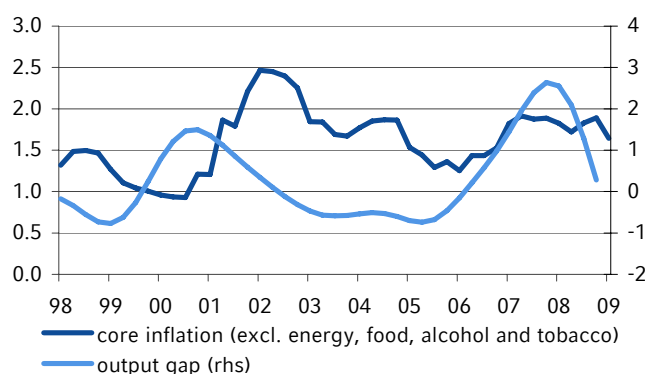
Eurozone and USA: output gap* as % of trend GDP



* estimated with the Baxter-King filter

(Negative) output gap may squeeze prices; core inflation rate may fall to 1%

Eurozone: core inflation rate and output gap % y-o-y change and as % of trend GDP



Source EcoWin, WestLB Research

Source EcoWin, WestLB Research

Since energy prices may become less important for inflation in H2, attention may focus increasingly on the core inflation rate. Because the output gap closed towards the end of last year, sluggish demand may exert pressure on prices in the future. In previous economic cycles the core inflation rate reacted very late to the economic trend in some cases. The pressure on prices is therefore likely to increase within the forecast period, as the (negative) output gap opens due to the sluggish economic trend that we expect to see. We believe the core rate will fall to 1% in the course of the year. So although price pressure is likely to be extremely limited, deflation may still be a long way off.

Germany

Dramatic collapse, unusual recovery

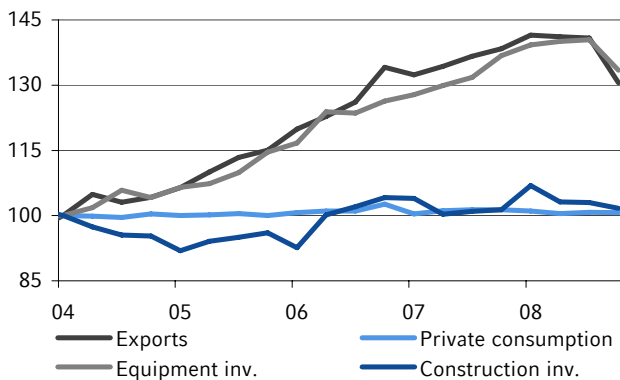
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The German economy suffered its sharpest collapse in post-war history during the winter months of 2008-09. Gross domestic product contracted by 2.1% in the final quarter of 2008 and is likely to have shrunk by a similar amount in the first quarter of 2009. The negative impact of shrinking exports and of German companies' much reduced capital expenditure has been exacerbated by a significant reduction in investment in construction. Construction output slowed more than usual for the season because of the cold weather.

Inventory depletion curbs
GDP growth

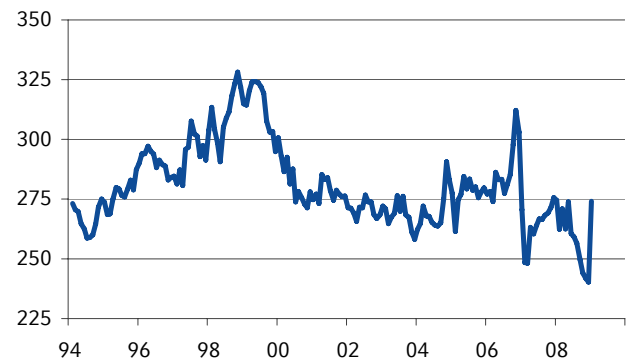
Inventory depletion presumably had a considerable dampening effect on aggregate economic output at the beginning of the year. Unlike in many other countries, German companies had built up their stocks towards the end of the year. In the first instance, they made use of lower commodity prices to buy in raw materials and inputs on favourable terms; this led to intentional accumulation of inventory. Companies were then unable to scale down their production fast enough to keep pace with the unusually rapid downturn in demand, and the unintentional accumulation of inventory that this caused led to a steep fall in industrial output at the beginning of this year.

Germany: demand components of GDP
Q1 2004 = 100



Source EcoWin, WestLB Research

Germany: new car registrations*
'000



*) Seasonally adjusted

Source EcoWin, WestLB Research

Positive impact of
private consumption

Private consumption, however, has probably had a slightly positive impact. So far the increase in unemployment has remained within bounds, and last year's pay rises are still having an effect. What is more, available real incomes have increased significantly, since inflationary pressures have abated appreciably. In addition, the wreckage premium on used vehicles for new car purchases has caused sales of new cars to accelerate.

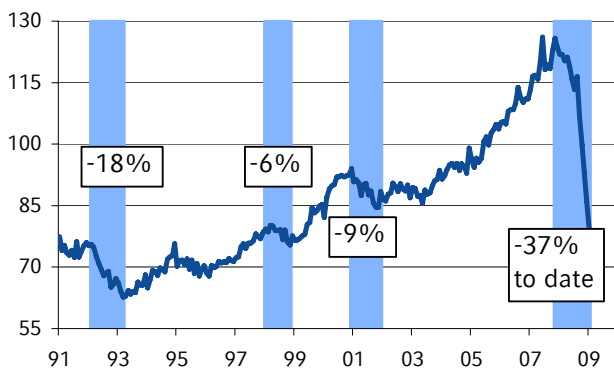
Previous strength has become
a weakness

The German economy is currently having to contend with a factor that was its trump card in the preceding upswing: the large contribution made to GDP by exports and the high share of capital goods in the industry. The collapse in world trade, and the substantial reduction in investment world-wide caused by the crisis in financial markets, have pulled the rug out from under the feet of German industry. Orders have fallen by 37% overall since the end of 2007 – foreign orders by 42%, and domestic orders by 31%. Manufacturers of capital goods have seen the sharpest fall in orders.

Industrial output continues to decline, but not as fast as before

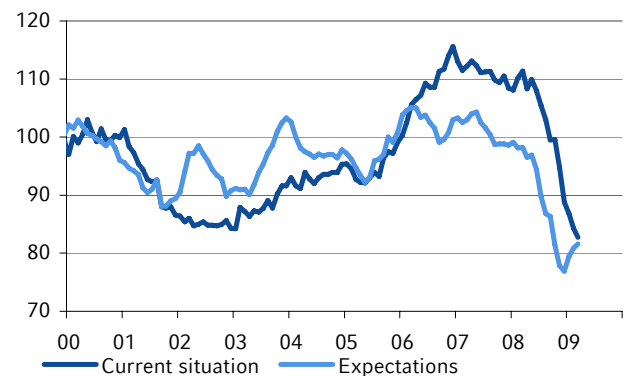
German companies have throttled back industrial output by around 20% so far. Further production cutbacks – and thus lower exports as well as reduced capital expenditure on plant and equipment – are therefore inevitable. However, the rate at which output is declining is likely to slow in the near future, as production usually tracks only around half of the corresponding change in demand. Naturally, given the substantial uncertainty surrounding future economic trends, it is impossible to rule out the possibility that incoming orders, and thus production, will continue to contract at the present rate. However, expectations that the many economic stimulus programmes that have been launched around the world will lead at least to stabilisation of industrial demand argue against this. German companies are likely to benefit from these programmes. Purchasing incentives in the crisis-stricken automobile industry, which are being granted in other countries too, are already having a significant impact. In February, for example, Volkswagen reported easily its best month – measured in terms of orders – since German reunification.

Germany: industrial orders
2005 = 100



Source EcoWin, WestLB Research

Germany: ifo business climate index
index points



Source EcoWin, WestLB Research

Improvement in the ifo business expectations justifies cautious optimism

The flood of bad economic news has caused many to entertain increasing doubts as to whether the economy will be able to stabilise or stage a slight recovery in the second half of the year. We estimate that there are indeed signs that it will be able to do so. For example, the expectations of companies polled by the ifo Institute with regard to the business outlook have, for three consecutive months, improved on the previous month. This indicates an imminent turnaround, according to a rule of thumb. The ZEW Indicator of Economic Sentiment has improved continuously since October; it has risen by 60 points overall. The purchasing managers' indices for manufacturing industry and the service sector have also stabilised recently – albeit at low levels.

The German government's economic stimulus package is stoking expectations of an improvement

We believe that the world economy will gradually stabilise in the second half of the year due to the unusually strong stimuli coming from fiscal and monetary policy, but exports are initially unlikely to contribute to growth. Experience teaches that capital expenditure too will remain weak as a result. Expectations of an improvement are thus based mainly on the German government's economic stimulus measures, which are clearly reflected in the ifo survey, for example. The strongest positive signals are coming primarily from the retail trade and from the building and civil engineering industry. The bullishness of the retail trade is based mainly on the automobile wreckage premium and the tax breaks (including the tax refunds resulting from court decisions on commuter tax relief), while the construction industry should benefit from the increase in public expenditure on infrastructure.

Fiscal measures (€bn)

| | 2009 | 2010 |
|--|-------------|-------------|
| Economic stimulus package I | 4.0 | 8.0 |
| Economic stimulus package II | | |
| Public infrastructure investment | 8.0 | 10.0 |
| Decrease in unemployment insurance contribution | 3.0 | 6.0 |
| Tax cuts | 3.0 | 5.0 |
| One off bonus for children | 1.5 | |
| Other measures (e.g. environmental bonus for new cars, short time work) | 1.8 | 2.0 |
| Miscellaneous | | |
| Commuter allowance | 6.0 | 1.5 |
| German Family Support Act (e.g. increase in child benefit) | 2.3 | 2.2 |
| Changes to welfare benefits (e.g. housing benefits, student grants, entitlement period for unemployment benefit - ALG I) | 2.3 | 2.2 |
| Overall effect | 31.9 | 36.9 |

Source Ministry of Finance, WestLB Research

Increased public expenditure underpins investment in building

However, it would run counter to past experience to expect the entire volume of fiscal measures to impact the economic cycle. Experience teaches that a substantial part of tax relief for households will go towards savings. Nor will all of the €18bn of public infrastructure expenditure marked for the next two years reach the construction industry. We assume that more than half of this amount will have an impact; this would be around 5% of investment in building. Because of planning times and the time taken to place orders, a positive effect is unlikely to occur before the second half of the year. Experience shows that this will then be spread over several quarters. As a result, we expect increasing investment in building deep into H1 2010.

Possible stabilisation of the economy in the second half of the year, but no upswing

This is likely to be enough to stop gross domestic product shrinking, and to trigger a slight economic recovery. But the dynamism of the recovery is likely to remain limited in the absence of incisive stimuli from exports and investment. There is no sign at the moment of an upswing in which gross domestic product would grow faster than production potential.

Increasing pressure on companies' profits

Our forecast would have substantial repercussions on the earnings of many companies. Since the earnings outlook is relatively bleak, they may have to cut costs massively if they are to attain their profit targets. The increased use of short-time working measures has so far staved off a broad wave of lay-offs: the number of unemployed has increased by 135,000 overall since the end of last year.

Short-time working may no longer suffice to prevent a notable increase in unemployment in the medium term, particularly in 2010. The number of registered unemployed is likely to increase to around 4m by the end of this year; it may be around 4.5m at the end of 2010. This would mean that consumption would no longer be able to prop up the economy in the coming year, despite tax relief.

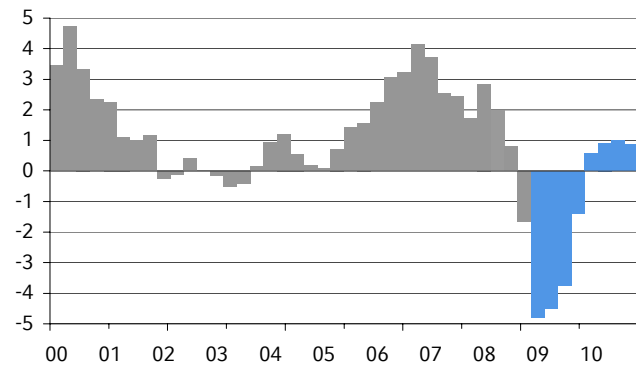
Appreciable decline in GDP in 2009E, slight improvement in 2010E

We expect gross domestic product to decline by 3.5% this year and we believe that an increase of 1% is feasible for 2010. If economic output has contracted by more in the first few months of this year than at the end of 2008, then we shall not be able to avoid lowering our forecast for FY 2009.

However, it would be even more serious if the economic stimulus package failed to have an impact and if the situation in the financial markets did not at least stabilise. In this case, the recession would inevitably continue next year too, and the aggregate state

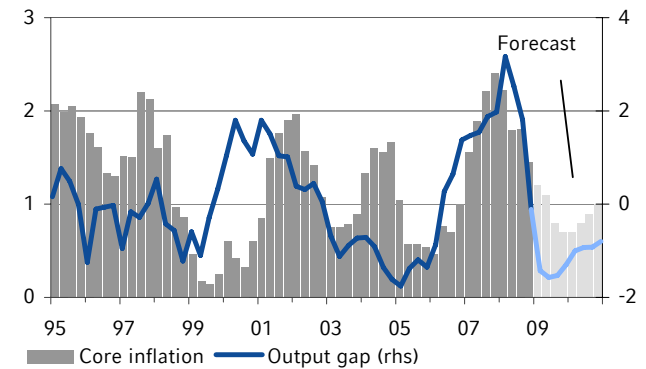
deficit would then probably increase even more steeply than we already forecast for this year and next – although measured in terms of gross domestic product the deficit ratios of 3% and 4% might remain well below those in the USA.

Germany: gross domestic product % y-o-y change



Source EcoWin, WestLB Research forecasts

Germany: core inflation rate and output gap % y-o-y change



Source EcoWin, WestLB Research forecasts

Unusual times = unusual forecasts

Our economic forecast is unusual in a historical context. Unlike in the past, we expect recovery to be driven not by exports or foreign demand, but by investment in building and hence by domestic demand. A similar outcome was seen at the beginning of the 1980s when capital expenditure and private consumption – caused then too by fiscal stimuli – ushered in the cyclical turnaround. But then too it took some time before growth accelerated. It would be unusual if the economy were to recover only very slowly and tentatively, despite highly expansionary fiscal and monetary policy and despite considerable relief due to lower crude oil prices. However, empirical studies carried out by the National Bureau of Economic Research (NBER) show that recessions after financial markets and banking crises are deeper than 'normal' economic downturns, and that it takes a lot longer for the economy to return to its starting point. To this extent, our economic forecast for Germany, which may appear unusual at first sight, is not so very unusual in an international context after all.

Inflationary pressure should remain low

Our economic scenario, with its initially narrowing output gap, suggests there will be little upward pressure on prices for goods and services, as manufacturers are unlikely to develop any pricing power in the near term. Pay settlements will no doubt be far lower than in previous years, given rising unemployment and pressure on companies to restructure, and this should keep domestic inflationary pressure in check. With crude oil and commodity prices barely rising, we forecast that the inflation rate for 2010 will not go significantly above 1% after an average of around 0.5% this year.

UK

Bank of England's drastic steps

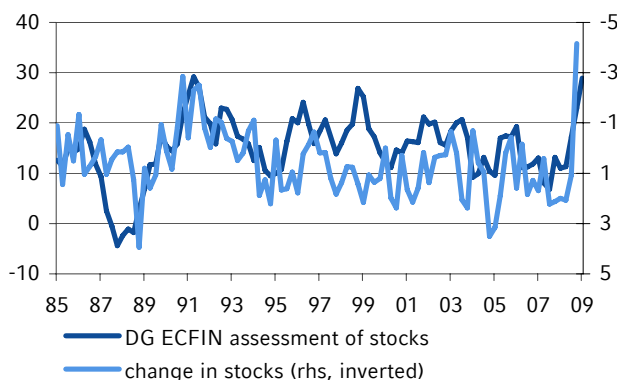
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The UK economy slipped into recession in Q3 2008. The 1.6% q-o-q decline in overall economic output registered at the end of the year was the most serious drop since 1980. The only positive effect in Q4 stemmed from public-sector consumption, which at any rate is higher than overall investment spending, and the contribution from foreign trade. The foreign trade deficit shrank because imports fell even more sharply than exports. This was due to collapsing domestic demand, which is now being fuelled solely by public-sector consumption and has a smaller proportion of imports.

Significant reduction of inventories in Q4 may not be unintentional

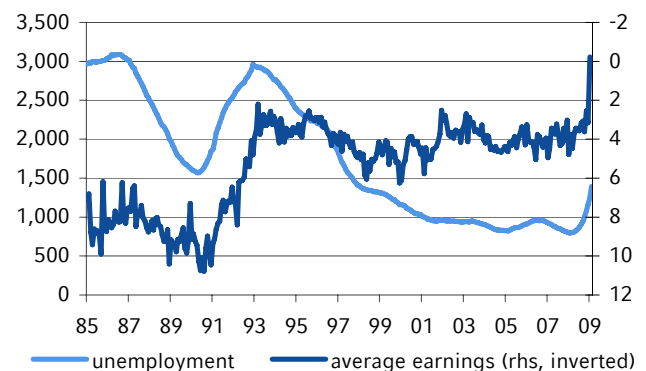
However, one striking feature at the end of 2008 was the pronounced reduction of inventories, which alone cut growth by 1.6 percentage points in Q4. A retrospective major correction of this component is improbable (the UK, unlike Germany, actually collects inventory statistics). So there could be a corresponding countertrend in Q1 2009 if inventories were reduced to an unintentionally large extent. Yet surveys indicate that inventories (at least in manufacturing industry) are still reckoned to be too high. Inventories are therefore likely to have been cut further at the start of the year, and to have had a negative impact on the economy in addition to that of structural factors like the ongoing real estate crisis.

UK: Inventory evaluation and change in inventories
Balance in %age points and fbn



Source EcoWin, WestLB Research

UK: Unemployed persons and average earnings
(‘000 and % y-o-y growth)



Source EcoWin, WestLB Research

Increase in unemployment is already depressing wages – threat of deflation is increasing

The recession has now triggered accelerated job losses. The unemployment rate stood at 6.6% of the workforce at the end of last year, its highest level since 1997. This is already depressing wages in the labour market: average earnings fell in q-o-q terms at the start of this year, for the first time since this metric started to be recorded in 1991.

The threat of a prolonged negative price trend is therefore looming in the UK, and the Bank of England has moved swiftly in response. Firstly, it has lowered the bank rate from 5.75% at the end of 2007 to a mere 0.5%, its lowest level since the founding of the BoE in the 17th Century.

The Bank of England then adopted unconventional fiscal policy and started in mid-March to buy up government bonds. The envisaged volume for three months is £75bn, but the Chancellor has granted the BoE a total budget of £150bn.

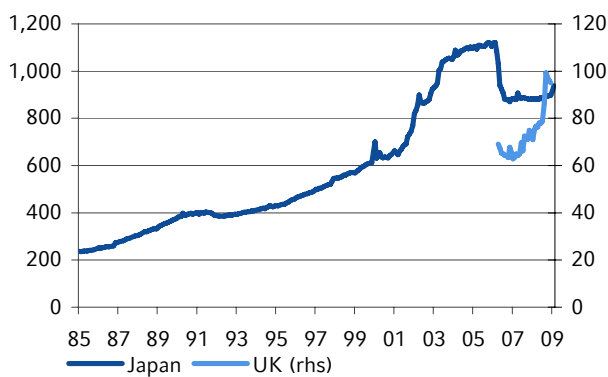
BoE is dramatically expanding the monetary base – lending should stabilise over the course of the year

A comparison with the Bank of Japan, which some years ago applied the same instrument to bring the Japanese economy out of deflation, can be used to measure the potential effectiveness of the UK’s so-called quantitative easing. Between 2001 and 2006, the Bank of Japan expanded the so-called monetary base – i.e. the amount of currency in circulation – and commercial banks’ reserves with the BoJ by just over 70%. The £75bn that the BoE has envisaged for the buying up of government bonds would increase the UK’s monetary base by a similar percentage, but in just three months. The programme is also extraordinarily large in terms of the volume of government securities in circulation, and particularly of the medium- to long-term maturities the BoE intends to buy. Accordingly, long-end yields softened by as much as 60 basis points following the announcement of the programme. In our view, the monetary stimulus (commercial banks can use deposits at the central bank to make loans) should help to stabilise lending to households and companies. This activity weakened considerably in the period leading up to the start of the year.

Gradual economic recovery towards the end of the year is becoming more likely

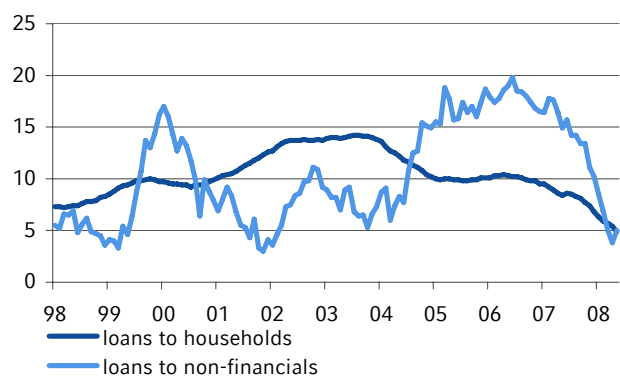
The Bank of England’s policy change may also make the mild recovery we had expected to see towards the end of the year more likely. This is suggested by the reaction in fiscal policy; this has now become far more expansive than during the recessions in the early 1980s and 1990s. The sharp devaluation of Sterling should also bolster exports, since the first signs of a hesitant recovery in sentiment are starting to emerge. Sentiment among purchasing managers in the service sector, which is so important to the UK, recently improved for the third time in succession – even though output in this industry is still set to diminish for the time being. Accordingly, we have left our GDP forecasts for the UK unchanged: we continue to expect overall economic output to rise by 0.5% next year, following a drop of 2.7% this year.

Japan and UK: Monetary bases
¥bn and £bn respectively



Source EcoWin, WestLB Research

UK: Growth of lending to households and companies
% y-o-y



Source EcoWin, WestLB Research

Switzerland

Caught in the crossfire of two global crises

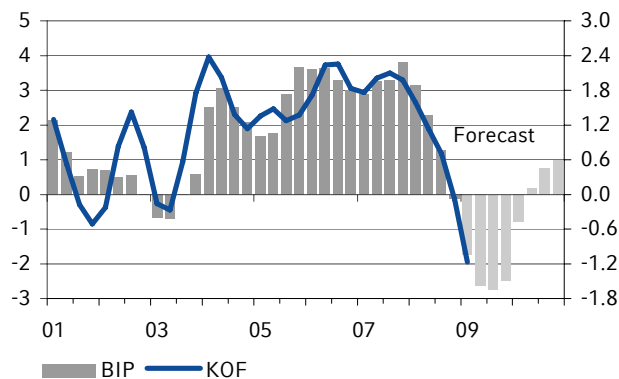
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The Swiss economy has been pushed into recession by the global economic slump and the financial markets crisis, which has persisted for the last 1¾ years. GDP declined successively in Q3 and Q4 following only slight growth in the first half of 2008. The 0.3% q-o-q decline towards the end of the year was moderate relative to that for Germany (-2.1%) because the low level of unemployment meant that consumption remained relatively robust.

Strong integration into international trade

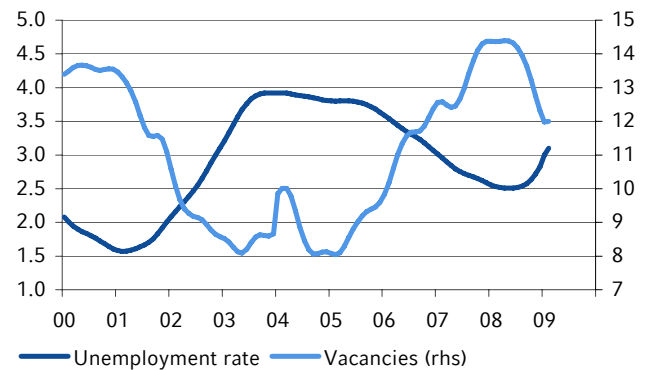
The Swiss economy, like that of Germany, is closely integrated into international trade, and is thus caught in the crossfire triggered by the worldwide economic slump. A burdening factor in this context is the severe recession in Germany, which is far and away Switzerland's most important trading partner. The significant firming of the Swiss franc, which rose at the end of October to around CHF/EUR 1.44, its highest level ever vs the euro, also proved millstone. The resulting slump in exports seen recently was worse than in previous recessions.

Switzerland: GDP and KOF index
% y-o-y and index points



Source EcoWin, WestLB Research forecast

Switzerland: Unemployment rate and job vacancies
% and '000



Source EcoWin, WestLB Research

Gloomy sentiment among exporting companies; unemployment weighs on firms supplying the home market

Bleak economic prospects around the world are having a considerable impact on sentiment among Swiss exporting companies. The current situation is assessed largely as being 'quite unfavourable' following the latest KOF economic survey, and the decline in the first quarter is expected to be just as severe as that recorded at the end of last year. Domestic-oriented companies assess their business situation as being significantly better than this. However, even these companies' situation is becoming increasingly bleak. Their sentiment is likely to deteriorate in the months ahead, as the still relatively low unemployment rate will in all probability continue to climb. As in Germany, the increased spread of short-time working in Switzerland is unlikely to prevent unemployment from rising.

Finance industry accounts for a high share of value creation

The second big factor weighing on the Swiss economy is the result of the global financial crisis. The value created by the financial sector (banks and insurance industry) contracted in all four quarters of last year. This is all the more serious given that the financial sector's contribution to value creation in Switzerland of around 12.5% is significantly higher than in Germany (4.2%), for example. Swiss financial institutions continue to assess their business situation as extremely difficult and to expect further

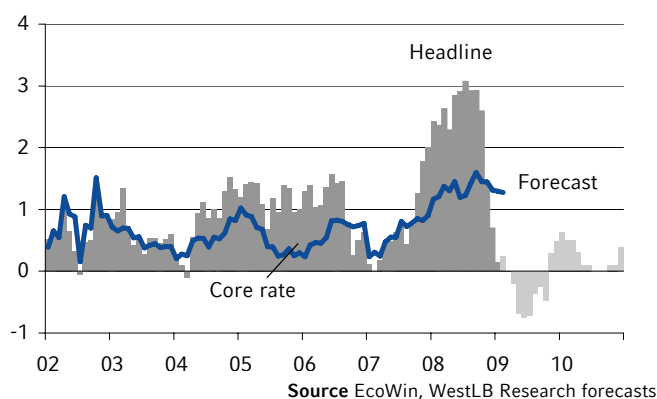
declines, as an end to the financial markets crisis is currently not in sight. Besides the turmoil on the financial markets, the debate about easing bank secrecy and the significant resultant outflow of managed assets could prove to be a burden on the way the economy develops in future.

Recession set to continue for now; stabilisation unlikely before the end of the year

Overall, recessionary forces in Switzerland are likely to retain the upper hand for the time being. We cannot expect the economy to become stable before the end of the year at the earliest. The intensity of the retarding effects is then likely to gradually weaken, and the government's anti-cyclical spending will probably kick in at the same time. As Switzerland's key trading partners are unlikely to experience a real upswing, growth momentum will probably remain subdued well into next year. We expect GDP to increase slightly (+0.3%) in 2010, following a decline of 2.5% this year. Our forecast assumes that the financial markets will gradually stabilise. Should this fail to materialise or the situation become even more acute, then the economic slump in Switzerland would probably turn out to be even worse.

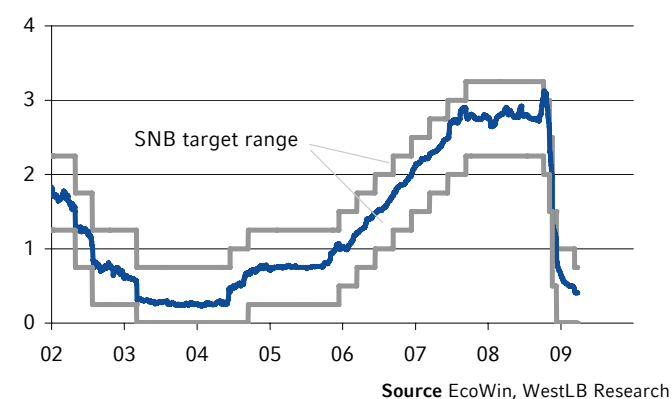
Switzerland: Consumer prices

% y-o-y



Switzerland: 3-month Libor

%



Low inflationary pressure to continue this year

Inflation has now tapered off markedly. It was still more than 3% in July 2008, but amounted to a mere 0.2% in February. In all likelihood, the rate will drop below 0% this spring and increase again slowly towards the end of the year at the earliest. Given the low level of growth momentum, inflationary pressure is likely to remain weak.

De facto zero-interest policy for the foreseeable future

The Swiss National Bank markedly eased its monetary policy in the middle of March, lowering its 3-month Libor target band to 0-0.75%, due to the significant deterioration of the economic environment and concerns about a phase of negative inflation rates that could last several years. The SNB is targeting a rate of 0.25%. In addition, it has intervened in the currency markets to prevent the Swiss franc from firming against the euro. The SNB may also make full use of its arsenal of unconventional measures. For example, it has announced additional repo transactions and the purchase of CHF bonds issued by private borrowers. We expect base rates to remain at the present level for the foreseeable future.

Key data for Switzerland

| | 2005 | 2006 | 2007 | 2008 | 2009E | 2010E |
|----------------------------|------|------|------|------|-------|-------|
| GDP (in % y/y) | 2.5 | 3.4 | 3.3 | 1.6 | -2.5 | 0.3 |
| Consumer prices (in % y/y) | 1.2 | 1.1 | 0.7 | 2.4 | -0.2 | 0.2 |
| Unemployment rate (in %) | 3.8 | 3.3 | 2.8 | 2.5 | 3.5 | 4.2 |

Source EcoWin, WestLB Research forecasts

Japan

Its worst recession, and little sign of improvement

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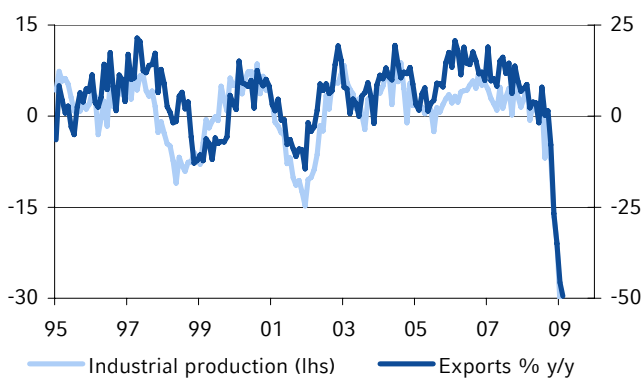
Japan is undergoing its worst recession since the Second World War. Real GDP may well shrink this year at the fastest rate since 1955. Export-driven industrial production was recently 30% down y-o-y, and exports themselves were down 50%. This devastating picture is reflected in corporate earnings. According to a Finance Ministry survey, corporate profits in Q4 2008 were down more than 50% y-o-y overall. The last time this happened was 1955. The manufacturing sector is particularly hard hit, with a -90% drop. One prominent example is the Toyota group, which may well report the first loss in the company's history.

Demand in main export markets has collapsed, as have industrial output, investment and corporate earnings

The USA and the EMU, two of Japan's three main export markets, are in recession, and whether the third, China, will be able to prevent a prolonged slowdown in growth is anything but certain. We basically do not expect these regions to mount a strong recovery either this year or next. Given this, the prospects for corporate investment activity are very bleak. Companies were still expanding their investments up to the start of 2008, due to high levels of capacity utilisation in the previous four years. Since then, however, firms have reacted to falling demand by reining in investment. Capital expenditure was already cut by a total of about 4% in 2008. In our view, the current slump in capacity utilisation of roughly 35% y-o-y will cause a wide-ranging contraction of investment in machinery and equipment as part of a longer period of adjustment. We assume investment will decline by close to 20% in 2009 and we do not expect it to pick up again until towards the end of 2010.

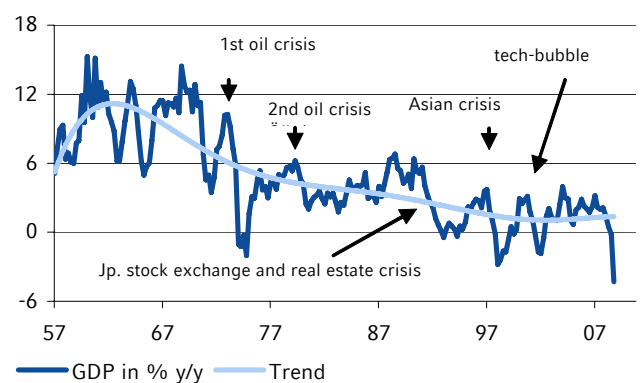
Japan: Exports and industrial production growth

% y-o-y



Japan: GDP growth since 1957

% y-o-y



Source EcoWin, WestLB Research

Source EcoWin, WestLB Research

Consumption too is likely to ease off considerably

But problems with foreign trade and investment are not Japan's only concerns. The poor economic situation is likely to intensify the traditionally high propensity of Japanese consumers to save. A current barometer of economic sentiment gives a picture of consumer confidence: last December this index dived to its lowest point since its inception in 1982. The chief reasons for this trend, besides the economic environment, are the worsening situation in the labour market, and decreases in wages and salaries.

The labour market is deteriorating, and remuneration is falling

The growth in average non-farm payrolls has been in decline since the summer of 2008. Since last winter, the trend has even become clearly negative in y-o-y terms. In the manufacturing sector, which employs about 20% of the workforce, wages have been decreasing for the past six months. The situation in the construction and trade sectors, which account for roughly 30% of the workforce, is only slightly better. Here too, it can be assumed that the situation will continue to worsen. The tension in the labour market is described by the 'jobs-to-application' ratio, which has been in decline since 2007, and by the increase in unemployment. The proportion of part-time workers and temps has more than doubled since 1984 – from 15% to 34%. These workers are the first to be hit, but permanent staff too are now being made redundant. In many cases, the loss of a job also means the loss of company housing. One problem is that while the labour market has become more flexible, Japan's very patchy social security system has been left fundamentally unchanged. This is likely to heighten Japanese consumers' concerns, and may arguably be reflected in a disposition to spend that is even weaker than during the last recession. The government's consumer spending cheques will not change this, because the dislocations are far too serious.

Political situation is not very encouraging

The political situation in Japan is also anything but encouraging. The governing and opposition parties in the lower and upper houses of the Japanese parliament are at odds with each other and are standing in the way of some important economic measures. There is also dissent within the parties themselves, and the approval rating for the country's current prime minister Taro Aso recently dropped below the 10% mark. Only a short time ago, he announced that early elections (originally scheduled for September) might be held once the budget for FY2009 was passed and the economic stimulus programmes were implemented. We feel the earliest possible date would be in the summer, although this is unlikely to ease the situation.

Collapse looks likely to continue

We expect Japanese GDP to contract by 5.5% in 2009 following -0.7% in 2008, and for 2010 we expect only slight growth of less than 1%. However, in the event that the growth situation in the main exporting markets does not brighten up significantly, there is much more of a downside risk attached to these forecasts than an upside risk.

Japan

| | 2004 | 2005 | 2006 | 2007 | 2008 | 2009E | 2010E |
|---|------|------|------|------|------|-------|-------|
| GDP (in % y/y) | 2.7 | 1.9 | 2.1 | 2.4 | -0.7 | -5.5 | 1.0 |
| Consumer prices (in % y/y) | 0.0 | -0.3 | 0.2 | 0.1 | 1.4 | -1.0 | -0.5 |
| Unemployment rate (in %) | 4.7 | 4.4 | 4.1 | 3.9 | 4.0 | 4.7 | 5.2 |
| Current account bal. (in % of GDP) | 3.7 | 3.6 | 3.9 | 4.8 | 3.2 | 2.1 | 2.4 |
| Budget Balance (in % of GDP) ¹⁾ | -6.0 | -6.5 | -5.6 | -4.9 | -6.2 | -8.8 | -7.5 |

Source: National statistics. – 2009-10: WestLB forecasts. – ¹⁾ Total government.

Emerging markets – CEE

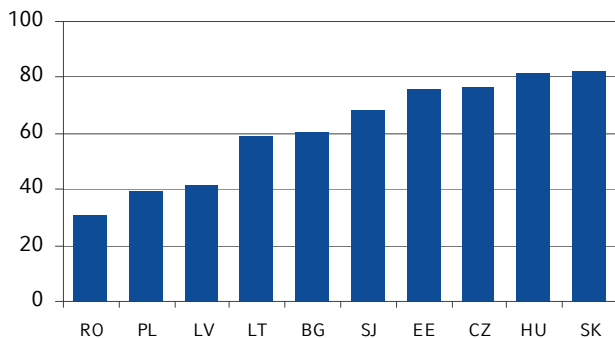
Lifeline from the West

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While the new EU member economies were still growing last year at a rate of 4.3%, they look set to contract this year. Being generally small open economies, these countries are extremely dependent upon exports. Only Poland and Romania have an export ratio (exports as a percentage of GDP) of less than 40%. By contrast, with export ratios of more than 70%, Slovakia, Hungary, Estonia and the Czech Republic are most dependent upon exports. A slump in the demand for exports, as in H2 2008, therefore feeds through very strongly into these countries' growth rates. To make matters worse, the Baltic states and Bulgaria have fixed exchange-rate systems, and Slovakia and Slovenia are part of the Eurozone. This means that these countries also do not have the option of devaluing their currencies in order to improve their international competitiveness and stimulate demand for exports. Only Poland and Romania have domestic demand that is large enough to cushion the effects of the downturn triggered by export markets.

Export dependence

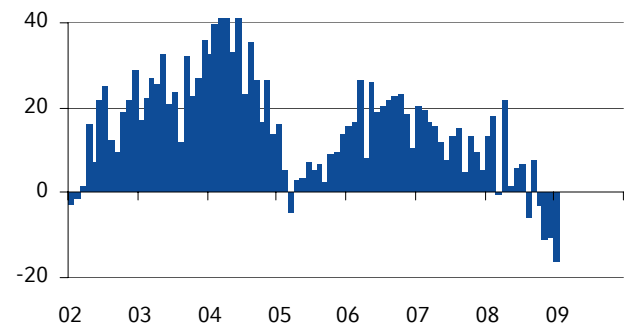
Exports as a % of gross domestic product, as of 2008



Source EcoWin, WestLB Research

Poland: Exports

in % y/y



Source EcoWin, WestLB Research

Drying up of capital inflows is slowing growth

Besides the close trade links, the financial ties have also grown considerably since the EU accession in 2004. The region has benefited from high inflows of capital in the form of direct foreign investment. However, in the course of the international economic downturn the earnings situation of corporates (the potential investors) has deteriorated and the lending conditions for the financing of investments have become stricter. For this reason, the inflow of direct investments is likely to be far less this year. There is also a decrease in portfolio investments because risk aversion in general, and with regard to Eastern Europe in particular, has increased. Payment difficulties, like those experienced in Hungary or Latvia, are putting off potential investors – despite potentially attractive rates of return. The capital inflows in the banking sector (i.e. from the Western European parent organisations to the Eastern European subsidiaries) are likely to diminish or in some cases may even reverse because the Western European banks themselves are suffering from liquidity constraints. The shortage of capital may well therefore also lead to more restrictive lending to domestic firms and private households. In turn, this will probably also curb domestic demand.

Fiscal policy stimulus is modest

Monetary and fiscal policy can only do so much

Major economic stimulus programmes, as in the West, are few and far between in the Eastern EU countries. This is chiefly because the CEE states are shying away from increasing their national budget deficits to levels regarded as normal for Western European countries at the moment. They fear that they will become even less attractive for investors and no longer be able to finance their deficits. In addition, a major expansion of their national deficits would undermine their ability to join the EMU at some point in the near future. The European Monetary Union is still regarded as a haven of stability and efforts to join it have been redoubled since the outbreak of the crisis. A significant economic revival brought about by fiscal policy stimuli is therefore not on the cards in the new EU states. In countries bound by IMF requirements (like Hungary, Latvia and Romania), fiscal policy is even restrictive.

Currency turmoil slowing rate-cutting cycle

Thus, monetary policy is the key instrument to cushion the downturn. Since Q4 2008, key rates in the major CEE countries have also dropped significantly. However, the rate-cutting cycle was slowed down by the turmoil on the currency market. The considerable drop in the exchange rate of key CEE currencies has resulted in the central banks taking a more cautious approach. As a result, this is also likely to delay the stimulating effect of their expansive monetary policy measures. Moreover, monetary policy in countries with fixed exchange rates (i.e. the Baltic states and Bulgaria) can only do so much anyway.

Central and Eastern Europe: GDP (% y-o-y)

| | 2000-08 | 2006 | 2007 | 2008 | 2009E | 2010E |
|---------------------------|---------|------|------|------|-------|-------|
| total | 6.1 | 7.2 | 7.0 | 4.5 | -1.9 | 2.1 |
| New EU members since 2004 | 4.8 | 6.7 | 6.3 | 4.3 | -1.3 | 1.4 |
| Poland | 4.1 | 6.2 | 6.7 | 4.9 | 0.7 | 1.5 |
| Czech Republic | 4.4 | 6.8 | 6.0 | 3.2 | -1.5 | 1.8 |
| Hungary | 4.0 | 4.0 | 1.1 | 0.6 | -3.5 | 0.5 |
| Russia | 7.0 | 7.4 | 8.1 | 5.6 | -2.0 | 3.0 |
| Turkey | 5.2 | 6.9 | 4.6 | 2.1 | -1.5 | 2.0 |

Source EcoWin, WestLB Research Forecasts

A recovery will come from the West

Just as the economic upturn moved from West to East, a recovery is also likely to come from this direction. As the downturn is impacting Central Europe with a time lag, several countries are likely to slip into recession in the course of this year. Risk aversion will probably ease once stabilisation takes hold in the West, thus rekindling increased capital investment activity in this region. Based on a gradual revival in the demand for exports, growth rates will probably move up towards trend growth by 2011. In countries affected by severe imbalances, such as Latvia and Hungary, the adjustment process will probably be somewhat more protracted.

Emerging markets – Asia

The job market is an added drag on growth

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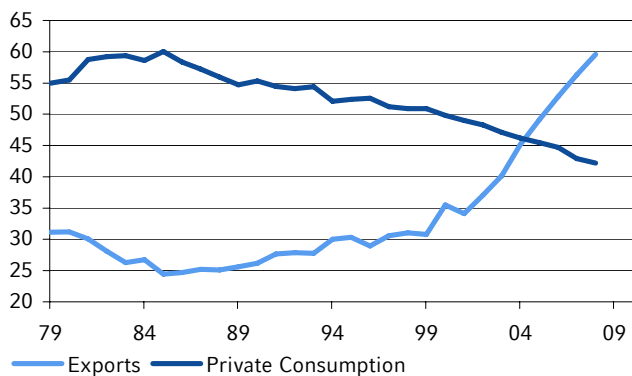
The economy slumps

The economies of virtually all Asian countries slumped in the fourth quarter and there is no sign of improvement in the current quarter. On the contrary: Asian exports are falling unprecedentedly fast due to the fundamental downturn in demand. This – in conjunction with the precipitous fall in industrial output seen in many countries – forebodes a significant contraction of GDP. South Korea's exports have fallen recently by 17% and those of China by 26%, while exports from Taiwan have slumped 29%. Asian countries' high levels of economic openness, and their deep integration into the global value-added chain, are pulling the region ever more deeply down in the wake of the world-wide recession.

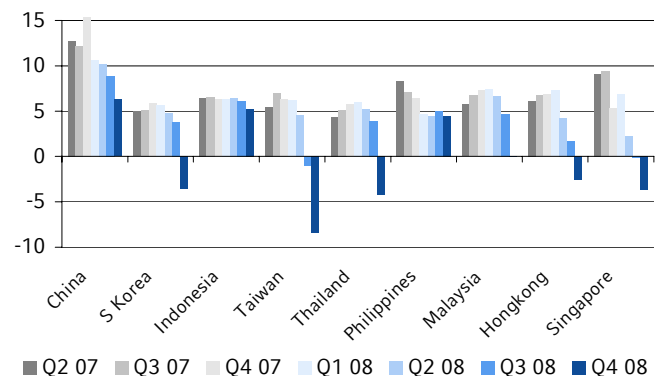
Economic stimulus packages everywhere

Asian governments are mounting increasing efforts to halt the downtrend. Malaysia and China, for example, have put together extensive economic stimulus packages equivalent to 10% and 13% of their respective nominal gross domestic product. Nevertheless, we do not believe that these packages will bring about a trend reversal. The negative effects of the world-wide purchasing restraint are simply too devastating to be mitigated by stimulating domestic demand. The influence of private consumption is limited here anyway. The contribution made by consumption to gross domestic product in Asia has been contracting since the mid-1980s and is now only 43% on average, while exports account for almost two-thirds of GDP.

Asia: exports and consumption
as % of GDP



Asia: GDP growth
% y-o-y change



Source EcoWin, WestLB Research

Source EcoWin, WestLB Research

Unemployment is increasing ...

The negative effect of foreign trade is not the only problem. The situation in the job market too may deteriorate severely due to the collapse in exports, the fall in commodity prices and the corresponding decline in industrial production. The latest report (Global Employment Trends – January 2009) published by the International Labour Organisation (ILO) includes a risk scenario of 51m additional jobless world-wide. The unemployment rate rose from 4.8% in Asia in 2007 to 5.0% in 2008 and the ILO expects it to rise sharply again in 2009. The ILO forecast is based on the outlook published last November by the International Monetary Fund (IMF), which still forecast global economic growth of 2.2% for 2009.

... and is an additional drag on growth via consumption

Given our growth forecast of -1.1%, and given that the IMF has now revised down its forecast (from -0.5% to -1.0%), this ILO risk scenario looks fairly realistic. The employment situation in Asia is very likely to deteriorate significantly, reversing at least part of the advances in affluence achieved in the past few years. As a result, governments' stimulus packages will have to contend with a substantial deterioration in employment and incomes, and as a result will hardly be able to bring about a strong revival in consumption. Indeed, in the light of the dramatic collapse in growth we assume that the deterioration in employment and incomes will greatly undermine consumer confidence and the propensity to consume. This would put additional downside pressure on growth.

Protectionism in the employment market, too

The protectionist measures that are currently being implemented in Asia underline the explosiveness of the crisis in the job market and the risk of social unrest that it harbours. China, for example, is using export subsidies and import duties in order to protect domestic production. These are, however, only indirect measures. South Korea, for instance, has significantly reduced quotas for foreign workers in order to protect its domestic employees directly. In Malaysia, foreigners may now be hired only in exceptional cases. When jobs are cut it is foreign workers who have to be laid off first. Similar examples from Australia, Spain and the UK round off this new picture of protectionism, which goes beyond typical trade restrictions and underlines justified concern about a severe deterioration of the job market.

Overall, this development puts the finishing touches to our forecast of a deep economic downturn in Asia. We forecast growth of only around 3% for 2009, after 6.7% in 2008 (Asia ex Japan, New Zealand and Australia). Economic output will probably decline by 1% in the emerging markets and the newly industrialised economies (NIEs) ex China and India.

Positive environment for direct investment

Although these forecasts are fraught with risks, there are also opportunities. Direct investment projects aimed at cutting costs in the home country, which have been put on ice, could soon look attractive again. Given the crisis, the governments and administrations of most Asian countries will undoubtedly support foreign investment projects more than ever, and be prepared to make corresponding concessions – as long as the projects create jobs. The worries of foreign companies that the cost of labour could rise in Asia are probably a thing of the past for the time being. Thus renascent direct investment could contribute to a lacklustre recovery in 2010 – after all, the crisis has done nothing to diminish Asia's locational advantages in the global labour market. Conditions are now probably even more conducive than before in the light of the employment situation, and governments and administrations are likely to be better disposed than ever to foreign investment.

Asia-Pacific: GDP (% y-o-y)

| | 2000-08 | 2006 | 2007 | 2008 | 2009E | 2010E |
|--------------------------------------|------------|------------|------------|------------|------------|------------|
| Total | 5.8 | 7.2 | 8.0 | 5.0 | 1.1 | 4.2 |
| Ex Japan, Australia, New Zealand | 7.5 | 9.1 | 9.7 | 6.7 | 3.0 | 5.6 |
| Emerging markets* ex China and India | 5.0 | 5.8 | 6.0 | 3.5 | -1.1 | 2.5 |
| China | 10.0 | 11.6 | 13.0 | 9.0 | 5.8 | 7.0 |
| India | 7.2 | 9.9 | 9.2 | 7.4 | 4.0 | 6.0 |
| South Korea | 4.9 | 5.1 | 5.0 | 2.7 | -3.5 | 1.3 |

* including NIEs (HK, S'pore, S Korea)

Source EcoWin, WestLB Research forecasts

Latin America

Greater resilience is no defence against slump

Holger Sandte
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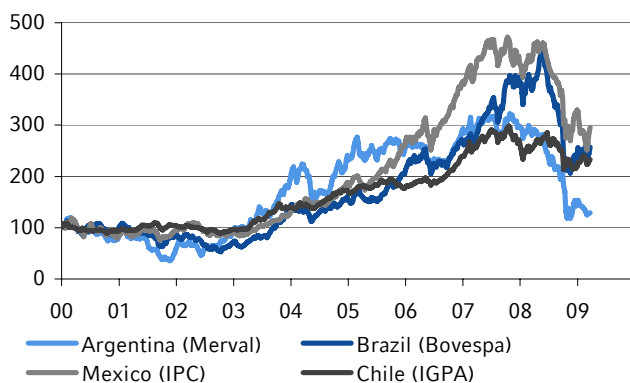
Strong growth in domestic demand ...

... is over

Latin America, like Central and Eastern Europe, accounts for about 8% of global GDP, and Brazil and Mexico generate close to two-thirds of this share. The region's unusually rapid economic growth of 5% p.a. since 2004 has been accompanied by current account surpluses – unlike in Central and Eastern Europe. Exports of commodities account for around one-quarter of the region's GDP; for Mexico, Venezuela and Chile the figure is even greater. Given this, it may come as a surprise that the region's prodigious growth in recent years has been borne chiefly by domestic demand, despite the boom in raw materials prices. The improvement in the terms of trade (the relationship between export and import prices) is not included in the calculation of real GDP, but has resulted in additional revenue for households, companies and governments alike, and has thus brought more spending options.

There has been economic mismanagement in some countries (e.g. Ecuador and Venezuela), but this does not hold true for the region as a whole. Many countries have accrued considerable currency reserves, improved their debt ratios and given themselves fiscal policy options. However, even Latin America will not be able to remain immune to the global downturn, and we believe the region will suffer a 1.3% reduction in economic output this year.

Latin America: Share indices in local currencies
1.1.2002 = 100

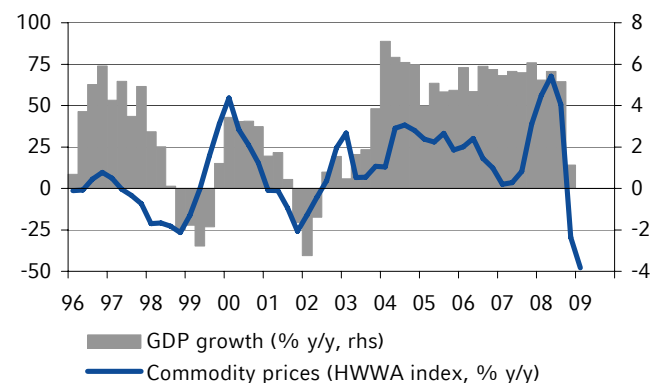


Source EcoWin, WestLB Research

Numerous negatives impacting this crisis-hardened region

Economic and financial crises are nothing unusual for the continent, as Mexico (1982 and 1994) and Argentina (1989 and 2001) prove. But unlike these and other crises, this time the negative effects are primarily imported rather than home-grown, although they are nonetheless serious: The fall in commodity prices has brought a marked deterioration in the terms of trade. There is also the usual pattern that applies to emerging economies (though not just to them): less foreign demand, diminishing credit availability, reduced capital inflows and bleak expectations. In some countries, e.g. Mexico, a sharp drop in remittances from nationals employed abroad, chiefly in the USA, is playing a role. The region last experienced a contraction in GDP in 2002 (-0.2%) following the Argentinean default.

Latin America: Economic growth and prices of raw materials



Source EcoWin, WestLB Research

Many of the figures for the past few months suggest the setback will be greater this time. For instance, industrial production was recently 17% down y-o-y in Brazil, and nearly 7% down in Mexico. Consumption and investment too have already either slowed or are dropping across the board.

Sharp cuts in base rates

In quite a few countries, base rates were still being raised last year; they are now being cut virtually everywhere. However, in doing this central banks will have to have regard to weakened currencies. Brazil's traditionally high base rate could drop this year into single digits for the first time. Taking Chile as an example shows how dramatically economic activity has slowed in recent months: The Chilean central bank has cut its key rate by no less than 600 basis points since the start of the year. Chile is by far the largest producer of copper, arguably the most economically sensitive industrial metal. The price of copper has dropped by more than two-thirds since last summer, and Chilean copper exports have roughly halved.

Mexico facing multiple problems

Mexico is undergoing a harsh downturn on account of the US recession and the drop in the price of oil. Exports to the USA, which account for about one-quarter of the country's GDP, have simply collapsed. Mexico is the world's tenth-largest automobile producer: vehicles are its most important export product after crude oil. Revenues from both auto and oil exports in January were about 50% down y-o-y. Even in Q4 2008, GDP was in decline in y-o-y terms. We expect it to contract by between 3% and 4% in 2009.

Brazil: Expansive fiscal policy softening the recession

Unlike Chile and Mexico, Brazil is not a particularly open economy, with an export ratio of merely 14%. Raw materials exports account for little over 10% of GDP. Brazil's GDP in Q4 2008 was still up on Q4 2007, but only just. Compared to Q3 2008, it was sharply down. Despite welcome support from an expansive fiscal policy, it will be difficult to prevent the country's economic output this year from shrinking by about 2%.

Rather a laggard than an engine of growth in the next upturn

Latin America should return to the path to growth once the global (industrial) economy comes back onstream, triggering more demand for raw materials and in turn causing prices to rise. But to all intents and purposes it will chiefly be a laggard economy that requires external pump priming – as during the last upturn. The region itself lacks the prerequisites to become a driving force of a recovery of the global economy. It accounts for too little of global economic activity, major parts of its industrial sector are not internationally competitive, and there is no evidence of other engines of growth. It may well take two or three years for the region to return to its growth path of about 4% p.a.

Latin America: GDP (% y-o-y)

| | 2000-08 | 2006 | 2007 | 2008 | 2009E | 2010E |
|--------------|---------|------|------|------|-------|-------|
| total | 3.4 | 5.5 | 5.6 | 4.0 | -1.4 | 2.5 |
| Brazil | 3.5 | 3.9 | 5.7 | 5.1 | -2.0 | 2.0 |
| Mexico | 2.8 | 5.1 | 3.3 | 1.3 | -3.5 | 1.5 |
| Argentina | 3.5 | 8.5 | 8.7 | 6.0 | 0.5 | 3.0 |
| Chile | 4.3 | 4.6 | 4.7 | 3.2 | -1.5 | 3.0 |
| Venezuela | 4.7 | 10.3 | 8.4 | 4.8 | 0.0 | 4.0 |

Source EcoWin, WestLB Research Forecasts

Fixed-income markets

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Steeper yield curve

Between two extremes

Despite the hefty shocks that have reverberated around the financial markets and the global economy in recent months, the yield on 10Y Bunds has on balance hardly moved. It started the year at 2.96% and most recently was just eight points higher at 3.04%. The widespread flight by investors into safe havens has ensured buoyant demand for government paper – especially Bunds. However, high government funding requirements both now and in the future, combined with the associated fears of inflation, have prevented sharp rises in prices and falls in yields. In addition, the ECB has yet to follow the other major central banks and adopt a policy of directly buying government bonds. The yield curve has steepened considerably from the short end following the ECB's rate cuts.

FORECASTS

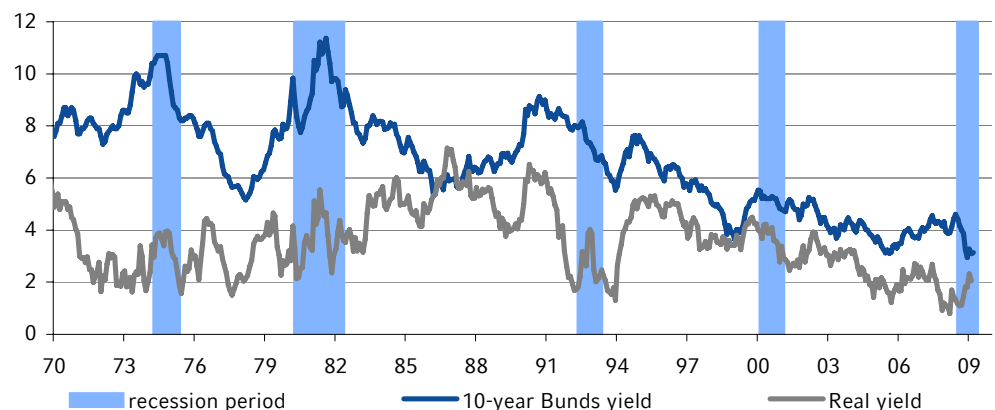
| in % | current | in 3 months | in 6 months | in 12 months |
|----------------|---------|-------------|-------------|--------------|
| Main refi rate | 1.50 | 1.00 | 1.00 | 1.00 |
| 3M money | 1.52 | 1.30 | 1.20 | 1.20 |
| 10Y Bunds | 3.04 | 3.20 | 3.20 | 3.80 |
| Fed funds rate | 0.25 | 0.25 | 0.25 | 0.25 |
| 10Y Treasuries | 2.72 | 2.70 | 3.00 | 4.00 |

Deflation looks a bigger threat than inflation

In our view, the current level of long-term yields is fundamentally reasonable. The real interest rate is near 2%, which is not unusual for periods of recession. The future trend may hinge largely on the expected economic picture and on expectations as to how the ECB will act in terms of unconventional monetary policy steps. The balance of opinion among market players and the public is moving between two extremes. In the deflation scenario, yields fall – as they have done in Japan – because the gap between macroeconomic demand and potential supply cannot be closed, despite all the stimulus packages. In the inflation scenario, ultra-loose monetary and fiscal policies result in expectations of ever higher inflation and yields over time. We currently believe the danger of a slide into deflation is considerably greater. At the same time, however, we consider that the massive monetary and fiscal stimulus, combined with steps to stabilise the financial sector, will avert genuine deflation in the USA and the eurozone.

Yield on 10Y Bunds

%



Source EcoWin, WestLB Research

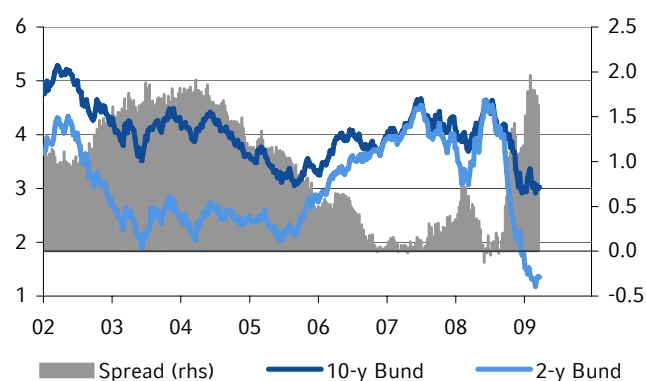
If this assessment proves correct, there would be no scope for long-term bond yields to slide towards 2.5% unless the ECB decided to buy up paper in the bond market directly. However, we do not expect it to do so. The ECB is likely to continue along the path it has taken so far and to provide banks with liquidity at a fixed, low rate via a broad range of refinancing transactions.

The ECB is certainly acting unconventionally and is taking account of the fact that businesses in the eurozone obtain financing mainly from banks rather than from the capital market – unlike those in the Anglo-Saxon economies. The ECB is permitted to buy government bonds in the secondary market – but of which member states? Germany, or Greece – or all issuers, in proportion to their relative weightings? For the ECB, buying government and even non-government securities directly in the market raises so many practical and politically tricky questions, that we believe it will take this step only in the very worst case (deflation). And as we have already said, we do not expect this to materialise.

Yields may remain around 3% for the time; possibly higher on economic recovery in the future

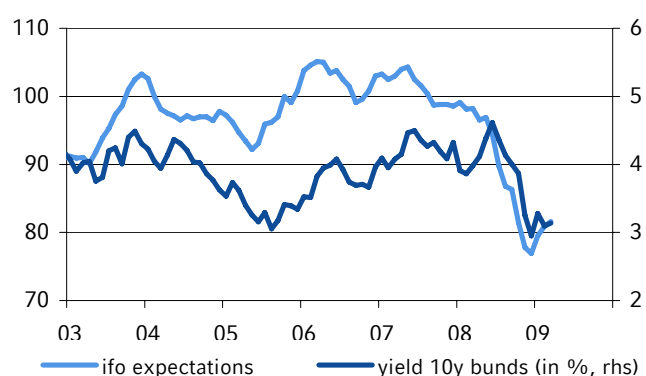
We expect the yield on 10Y Bunds to move in a band between 2.8% and 3.3% over the coming months. If our scenario of an – albeit muted – economic recovery from the second half of this year proves correct, only higher yields would be compatible. Our 12-month forecast remains 3.8%.

Yield on Bunds %



Source EcoWin, WestLB Research

Yield on 10Y Bunds and Ifo business expectations % , index points



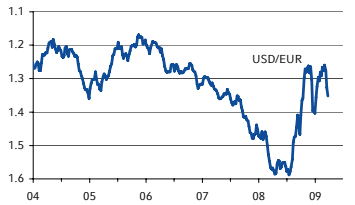
Source EcoWin, WestLB Research

High levels of inflation and interest rates: possible but not inevitable, if sensible policies are pursued

High inflation and high interest rates in the long term?

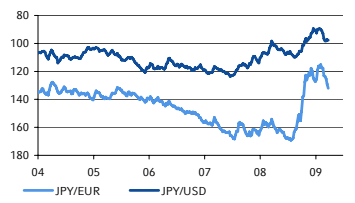
Some consider it absolutely inevitable that debt-funded stimulus and bank support programmes, combined with the ultra-loose monetary policies of many central banks, must end in (high) inflation sooner or later. It would be naïve to rule out this risk in the medium to long term. So much has happened in the past 18 months that nobody ever thought could happen. All the same, we expect that, after the end of the financial and economic crisis, the major central banks will take action to siphon off liquidity so quickly, and to raise rates to such an extent, that inflation rates will overshoot the inevitable level for no more than a brief period, i.e. not on a sustained basis. This would not be simple, as central banks would probably come into conflict with governments. However, inflation is better tackled by economic policy than by deflation. We would therefore willingly swap our acute concerns about possible deflation for longer-term fears about possible inflation. The markets are likely to remain unsure for a long period as to how high inflation may rise. This points to rising risk premiums for inflation in interest rates. As we believe that the danger of inflation is ultimately controllable, we expect the yield on 10Y Bunds to climb to around 5% in the next upturn rather than to 8% or 10%. But that will be a topic for 2010.

Currencies



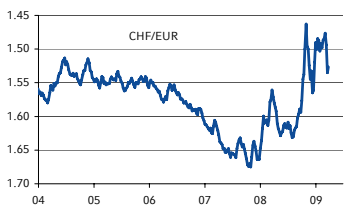
Source EcoWin, WestLB Research

- USD/EUR:** The dollar has temporarily been under substantial pressure since the US central bank announced that it would buy US Treasuries directly. This seems to have been a transitory undershooting, as the greenback is already firming now that the Geithner plan to buy toxic credits and securities from banks' balance sheets has taken concrete form. We believe that the latest measures by the US government and central bank to stabilise the financial sector and the economy will gradually bear fruit in the next few months, preventing a massive slide in the dollar exchange rate and possibly even allowing it to advance against the euro over the next few months – especially as the eurozone has difficulties of its own to contend with. We expect that the dollar will tend to chart a slightly firmer trend in the next few months, before disenchantment sets in as US growth turns out not to be very sustainable after all.



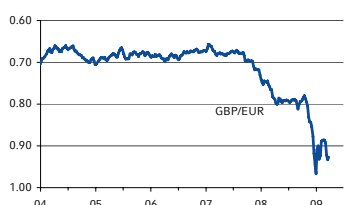
Source EcoWin, WestLB Research

- USD/JPY:** The firming of the yen appears to be over. The Japanese currency managed to chart a steep rise towards the end of last year, climbing as far as JPY 87.3/USD, but it has clearly changed course since the end of January. The yen has softened against the dollar and against the euro, and this is reflected in the Bank of Japan's trade-weighted index. The winding up of carry trades strengthened the yen in the past, but we now assume the Japanese currency will take its lead from the real economy. Against the backdrop of the worst recession in Japan's post-war history, and given the deteriorating trade balance, the yen looks likely soon to cross the 100 per dollar threshold and then to weaken to JPY 120/USD over a 12-month horizon.



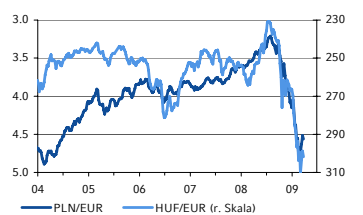
Source EcoWin, WestLB Research

- CHF/EUR:** The SNB's interest rate cut and intervention in the foreign exchange market on 12 March put an end to the bull run that had brought the franc to all-time highs against the euro. Since then the franc has been trading around CHF/EUR 1.53. We expect volatile trading over the next few months in a range between CHF/EUR 1.50 and 1.55. The likelihood that the Swiss key rate will be left unchanged at the current level, whereas the ECB will probably cut rates again, argues against further depreciation. However, the SNB may counter further safe haven inflows, and thus a renewed firming, by intervening energetically in the currency markets. So we see potential for the franc to weaken a little in the medium term. On the one hand, we expect a gradual stabilisation in the financial markets; on the other hand, the eurozone economy is likely to recover sooner than its Swiss counterpart.



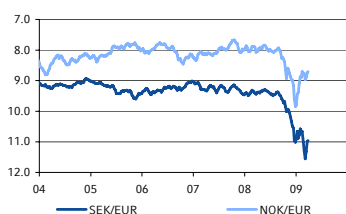
Source EcoWin, WestLB Research

- GBP/EUR:** Sterling has shed 5% against the euro since the end of February, following its temporary appreciation. The purchases of government bonds by the Bank of England that have occurred in the meantime have apparently led to lower interest rate expectations and have increased averseness to risk. However, we believe the magnitude of the measures taken by the Bank of England will be sufficient to help stabilise lending in H2. Sterling is likely to appreciate a little as the economy charts a slight upside movement.



Source EcoWin, WestLB Research

■ **PLN/EUR, CZK/EUR and HUF/EUR:** The major Central European currencies have continued their downward trend and have been subject to considerable fluctuations since the start of the year. The Polish zloty and the Czech koruna have recovered from their lows. However, the major central European currencies are likely to remain weak over the next six months, for several reasons: clouds are gathering over the region's economies, key rates will probably be cut further, payment problems remain unresolved in some countries, and averseness to risk lingers on. In Poland, the continued slashing of base rates to bolster the economy is likely to be on the agenda in the months to come. In addition, the Polish government is attempting to push ahead with entering the ERM II soon and joining the euro as planned in 2012. Hungary is one of the three countries to be most seriously affected by the crisis and still has payment problems to combat. In view of this, the Hungarian central bank may well adopt a very cautious approach to rate cuts. However, it has re-affirmed that it will do everything in its power to prevent a further weakening of the forint. We do not expect a significant and sustained firming of central European currencies over a one-year horizon, until signs emerge of the crisis coming to an end in the west and of a gradual recovery leading to reduced averseness to risk.



Source EcoWin, WestLB Research

■ **SEK/EUR and NOK/EUR:** Scandinavian countries, with their relatively small and open economies, have been affected relatively badly by the turmoil in financial markets and the global downturn. The Swedish economy has been in a deep recession since last year, and unemployment is rising rapidly. The massive cuts in key rates in the past few months have caused the region's currencies to depreciate significantly against the euro. The Norwegian krone and the Swedish krona charted new all-time lows at the beginning of this year, from which they have now managed to recover at least a little. But the Swedish krona will probably take a long time to regain its previous level. The overdue consolidation and the global recession are now feeding off each other in Sweden after years of constant growth. The Norwegian krona is likely to benefit, by 2010 at the latest, from an oil price that may be slightly higher by then.

Oil market

Oil price bottoming out

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The sharp drop in oil prices over recent months has come to an end; there has been a sideways – albeit volatile – trend in oil prices since the start of the year. In our view, the latest leap in prices above the US\$50 mark is unlikely to be sustained in the current climate. There is much to suggest that crude oil prices will climb only moderately in future.

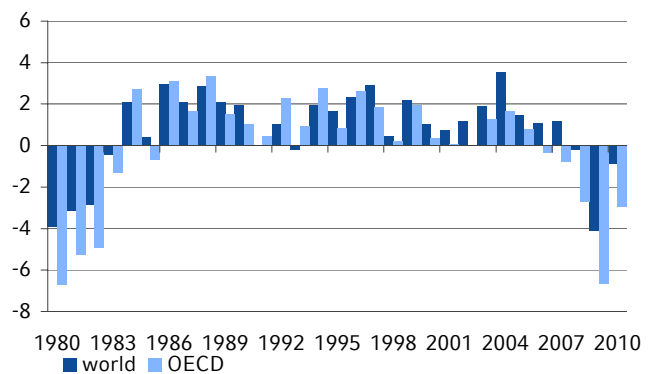
OPEC shows united front

OPEC's steadfastness in actually implementing the agreed cuts in crude oil production has come as a surprise to market observers. Almost 80% of the planned reduction by 4.2m barrels per day has already been implemented, led by Saudi Arabia and Qatar, with compliance rates of 100% and 83% respectively. Countries that are less stringent in adhering to the agreements include Iran and Venezuela, both of which are suffering from the decline in oil prices because of their public spending policies. Their compliance rates are only 45% and 42% respectively. The fact that the level of compliance with agreements differs among OPEC countries could explain why no further output cuts were decided at the OPEC meeting in mid-March. Nonetheless, OPEC's intervention has probably halted the drop in oil prices to a considerable degree.

Trend in Brent oil price since 2006
US\$ per barrel



Changes in consumption of crude oil
% y-o-y (figures for years after 2008 are forecasts)



Source EcoWin, WestLB Research

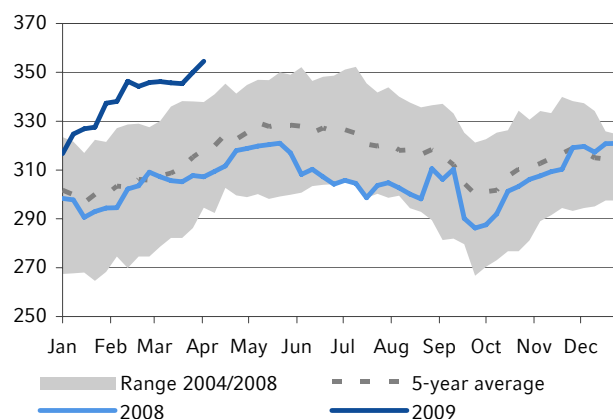
Source EcoWin, WestLB Research forecasts

Sharper fall in demand for crude oil likely

Overall, the markets still fear that there will be a further decline in demand for oil, given the economic setting. There is currently some evidence that the economic downturn across the world is slowing, but we believe it is far too soon to talk of a major recovery, and we have adjusted our forecasts for crude oil demand accordingly. We now assume that demand from OECD countries will contract by some 6% this year and 3% next year. This would lead to a fall in global demand of over 4% this year and almost 1% in 2010. There seems to be a certain amount of oversupply on the oil market at present, despite OPEC's production cuts and reduced output from other oil producers. This is clearly reflected in US crude oil inventories, for example, which since the start of 2009 have surpassed the highest previous levels of the past five years.

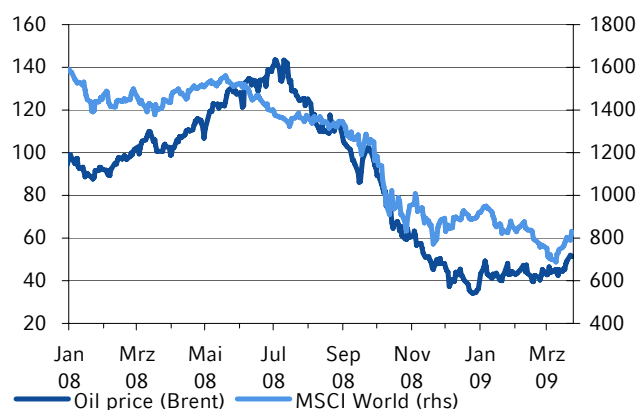
Oil prices may remain low as long as the supply overhang prevails; sustained higher prices may not be possible until the oversupply has been eliminated. This would require either more drastic production cuts than we have seen to date, or a more rapid recovery in economic activity, and thus in demand. Both scenarios seem rather unlikely in the current setting.

US crude oil inventories
m barrels



Source EcoWin, WestLB Research

Oil price vs MSCI World
US\$ per barrel; index points



Source EcoWin, WestLB Research

Oil price as a leading indicator of the upswing?

Overall, we assume that the oil price will be highly volatile in the months ahead. The oil market, like the equity markets, acts as a type of leading indicator. The announcement of the latest US economic package triggered a strong rally in both the equity and crude oil markets, for example. However, setbacks seem inevitable, given the persistent uncertainty, as economic data remain largely negative.

Weak dollar to buoy the oil price?

There is another factor, as there has been in the past, that could influence the trend in oil prices over the coming months. Last summer we saw that a weak (strong) dollar consistently led to higher (lower) oil prices (in US\$). Current uncertainty regarding the US economy suggests that the dollar will remain volatile, and this volatility could extend to the trend in the oil price. We expect the dollar to weaken in the long term; this could bode well for a rise in the oil price.

Oil price may average US\$ 50 this year

The global economy should pick up slightly in the second half-year, according to our forecasts, but a sustained recovery is unlikely before late 2010 in our view. Consequently, we expect that the trend in the oil price will be rather moderate. We believe price surges such as those seen in the past two weeks are likely throughout this period. However, oil producers' hopes of a marked rise in prices may be repeatedly dashed. We project that the price of a barrel of Brent will average US\$ 50 this year, and we look for a moderate climb in 2010.

Forecasts

| (US\$/b) | 2007 | 2008 | 2009E | 2010E | 2009E | | | |
|----------|-------|--------|-------|-------|-------|----|----|----|
| | | | | | Q1 | Q2 | Q3 | Q4 |
| Brent | 72.92 | 97.35 | 50 | 60 | 44 | 49 | 52 | 53 |
| WTI | 72.53 | 101.93 | 51 | 62 | 42 | 51 | 54 | 55 |

Source EcoWin, WestLB Research estimates

Forecast tables

Growth and inflation

| | GDP ¹⁾ Annual change (%) | | | | Consumer prices ²⁾ Annual change (%) | | | |
|--|--|------------|-------------|------------|--|------------|-------------|------------|
| | 2007 | 2008* | 2009* | 2010* | 2007 | 2008* | 2009* | 2010* |
| Industrialised countries | 2.4 | 0.7 | -3.2 | 0.8 | 2.1 | 3.4 | -0.1 | 1.7 |
| USA | 2.0 | 1.1 | -3.3 | 0.8 | 2.9 | 3.8 | -1.0 | 2.0 |
| Canada | 2.7 | 0.5 | -2.0 | 1.5 | 2.1 | 2.4 | 0.3 | 2.0 |
| Australia | 4.0 | 2.1 | -0.3 | 1.0 | 2.3 | 4.5 | 2.3 | 2.3 |
| New Zealand | 3.1 | 0.4 | -1.5 | 1.5 | 2.4 | 4.0 | 2.0 | 2.0 |
| Japan | 2.4 | -0.7 | -5.5 | 1.0 | 0.1 | 1.4 | -0.5 | 0.3 |
| Switzerland | 3.3 | 1.6 | -2.5 | 0.3 | 0.7 | 2.4 | -0.2 | 0.2 |
| Norway | 3.2 | 2.0 | -1.5 | 1.0 | 0.7 | 3.4 | 3.0 | 2.0 |
| EU | 3.0 | 1.1 | -2.6 | 0.8 | 2.2 | 3.6 | 1.0 | 1.8 |
| EMU | 2.6 | 0.7 | -2.8 | 1.0 | 2.1 | 3.3 | 0.5 | 1.5 |
| Germany | 2.5 | 1.3 | -3.5 | 1.0 | 2.3 | 2.6 | 0.5 | 1.0 |
| France | 2.1 | 0.7 | -2.0 | 0.9 | 1.6 | 3.2 | 0.0 | 1.4 |
| Italy | 1.5 | -1.0 | -3.6 | 0.5 | 2.0 | 3.5 | 0.5 | 2.0 |
| Spain | 3.7 | 1.2 | -2.2 | 0.5 | 2.8 | 4.1 | 0.0 | 2.0 |
| Netherlands | 3.5 | 2.0 | -2.5 | 1.0 | 1.6 | 2.2 | 1.3 | 1.8 |
| Belgium | 2.6 | 1.1 | -2.3 | 0.9 | 1.8 | 4.5 | 1.0 | 2.0 |
| Austria | 3.1 | 1.8 | -1.5 | 0.6 | 2.2 | 3.2 | 0.5 | 1.6 |
| Greece | 4.0 | 2.9 | -0.2 | 1.0 | 3.0 | 4.2 | 1.5 | 2.7 |
| Portugal | 1.9 | 0.0 | -2.5 | 0.4 | 2.4 | 2.7 | 0.0 | 2.0 |
| Finland | 4.2 | 0.9 | -2.0 | 1.2 | 1.6 | 3.9 | 1.5 | 1.8 |
| Ireland | 6.0 | -2.3 | -9.0 | -1.0 | 2.9 | 3.1 | 0.0 | 1.5 |
| UK | 3.0 | 0.7 | -2.7 | 0.5 | 2.3 | 3.5 | 0.0 | 2.5 |
| Denmark | 2.0 | -1.3 | -3.2 | 0.8 | 1.7 | 3.6 | 1.5 | 2.2 |
| Sweden | 2.7 | -0.5 | -3.5 | 0.5 | 2.2 | 3.3 | -0.2 | 1.3 |
| | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 |
| New EU members | 6.3 | 4.3 | -1.3 | 1.4 | 3.8 | 5.8 | 2.9 | 2.8 |
| Poland | 6.7 | 4.9 | 0.7 | 1.5 | 2.6 | 4.2 | 2.5 | 2.0 |
| Czech Republic | 6.0 | 3.2 | -1.5 | 1.8 | 2.9 | 6.3 | 1.5 | 2.5 |
| Romania | 6.0 | 7.4 | -4.0 | 2.0 | 4.9 | 7.9 | 5.0 | 4.0 |
| Hungary | 1.1 | 0.6 | -3.5 | 0.5 | 8.0 | 6.1 | 3.5 | 3.6 |
| Slovak Republic | 10.5 | 6.6 | 1.8 | 3.0 | 1.9 | 4.0 | 2.0 | 3.0 |
| Bulgaria | 6.2 | 6.0 | 0.8 | 2.0 | 7.6 | 12.0 | 3.5 | 3.5 |
| South/Eastern Europe excl. EU members | 7.4 | 4.6 | -2.1 | 2.4 | | | | |
| Russia | 8.1 | 5.6 | -2.0 | 3.0 | | | | |
| Turkey | 4.6 | 2.1 | -1.5 | 2.0 | | | | |
| Asia excl. Japan | 9.7 | 6.7 | 3.0 | 5.6 | | | | |
| China | 13.0 | 9.0 | 5.8 | 7.0 | | | | |
| India | 9.2 | 7.4 | 4.0 | 6.0 | | | | |
| Asian emerging countries ³⁾ | 6.0 | 3.5 | -1.1 | 2.5 | | | | |
| Latin America | 5.6 | 4.0 | -1.4 | 2.5 | | | | |
| Brazil | 5.7 | 5.1 | -2.0 | 2.0 | | | | |
| World | 5.0 | 3.1 | -1.1 | 2.3 | | | | |

¹⁾ Working day-adjusted data except for Germany.

²⁾ EU (except for Germany): Harmonised consumer price index.

³⁾ ASEAN, plus Hong Kong, South Korea and Taiwan.

Source National Statistics; OECD. - * 2008-10: WestLB forecast

Key figures

| Germany | | | | | | | | | |
|-----------------------------|------|-------|------|------|------|------|------|------|------|
| | 2008 | 2009 | 2010 | 2008 | | 2009 | | | |
| | | | | Q3 | Q4 | Q1 | Q2 | Q3 | Q4 |
| Real GDP (% y/y)** | 1.3 | -3.5 | 1.0 | 0.8 | -1.6 | -4.8 | -4.5 | -3.8 | -1.4 |
| Real GDP (% q/q) | | | | -0.5 | -2.1 | -1.7 | -0.2 | 0.2 | 0.3 |
| Domestic demand (% y/y) | 1.7 | -1.0 | 0.9 | 1.3 | 1.6 | | | | |
| Private consumption (% y/y) | -0.1 | 0.5 | 0.0 | -0.6 | -0.6 | | | | |
| Public consumption (% y/y) | 2.0 | 2.0 | 1.7 | 2.1 | 2.1 | | | | |
| Gross fixed invest. (% y/y) | 4.4 | -5.3 | 1.0 | 4.4 | -0.5 | | | | |
| Plant & equipment (% y/y) | 5.9 | -11.0 | -0.2 | 6.5 | -2.4 | | | | |
| Construction (% y/y) | 3.0 | -1.3 | 1.6 | 2.0 | 0.3 | | | | |
| Other (% y/y) | 6.6 | 3.3 | 3.3 | 6.2 | 6.1 | | | | |
| Inventories (% points) | 0.5 | -0.5 | 0.2 | 0.4 | 1.7 | | | | |
| Net exports (% points) | -0.4 | -2.5 | 0.1 | -0.6 | -3.5 | | | | |
| Exports (% y/y) | 2.7 | -12.0 | 2.3 | 3.1 | -5.6 | | | | |
| Imports (% y/y) | 4.0 | -8.5 | 2.3 | 4.9 | 1.5 | | | | |
| Consumer prices (% y/y) | 2.6 | 0.5 | 1.0 | 1.1 | 1.3 | 0.8 | 0.0 | -0.4 | 0.2 |
| Budget balance (% of GDP) | -0.1 | -3.0 | -4.0 | | | | | | |
| Unemployment rate (%) | 7.8 | 8.3 | 9.8 | | | | | | |

** quarterly data are working-day adjusted, annual data not adjusted.

| Eurozone | | | | | | | | | |
|------------------------------------|------|------|------|------|------|------|------|------|------|
| | 2008 | 2009 | 2010 | 2008 | | 2009 | | | |
| | | | | Q3 | Q4 | Q1 | Q2 | Q3 | Q4 |
| Real GDP (% y/y) | 0.7 | -2.8 | 1.0 | 0.6 | -1.3 | -2.8 | -3.4 | -2.9 | -1.1 |
| Real GDP (% q/q) | | | | -0.2 | -1.5 | -0.9 | -0.8 | 0.2 | 0.3 |
| Consumer prices (% y/y) | 3.3 | 0.5 | 1.5 | 3.8 | 2.3 | 1.0 | 0.2 | 0.0 | 0.9 |
| Budget balance (% of GDP) | -1.8 | -4.1 | -3.9 | | | | | | |
| Unemployment rate (%) | 7.5 | 8.7 | 9.8 | | | | | | |
| Current account balance (% of GDP) | -0.7 | -0.4 | -0.1 | | | | | | |

| USA | | | | | | | | | |
|------------------------------------|------|-------|------|------|------|------|------|------|------|
| | 2008 | 2009 | 2010 | 2008 | | 2009 | | | |
| | | | | Q3 | Q4 | Q1 | Q2 | Q3 | Q4 |
| Real GDP (% y/y) | 1.1 | -3.3 | 0.8 | 0.7 | -0.8 | -2.5 | -4.1 | -4.0 | -0.1 |
| Real GDP (% q/q) | | | | -0.1 | -1.6 | -1.4 | -0.9 | -0.1 | 0.2 |
| Real GDP (% q/q ann.) | | | | -0.5 | -6.3 | -5.6 | -3.7 | -0.3 | 0.9 |
| Consumer prices (% y/y) | 3.8 | -1.0 | 2.0 | 5.2 | 1.5 | -0.2 | -1.0 | -2.0 | -0.6 |
| Budget balance (% of GDP) | -5.3 | -11.0 | -8.0 | | | | | | |
| Unemployment rate (%) | 5.8 | 8.8 | 9.0 | | | | | | |
| Current account balance (% of GDP) | -4.7 | -4.5 | -4.2 | | | | | | |

Source: EcoWin, WestLB Research; 2009-10: WestLB forecast

Interest rates and yields (%)

| | | current 30.03.09 | in 3 months | in 6 months | in 12 months |
|-------------|--------------------------|---------------------|----------------|----------------|-----------------|
| EMU | Main Refinancing Rate | 1.50 | 1.00 | 1.00 | 1.00 |
| | 3-Month Deposits | 1.52 | 1.30 | 1.20 | 1.20 |
| | 10-Year Bund | 3.04 | 3.20 | 3.20 | 3.80 |
| USA | Fed Funds Target | 0.25 | 0-0,25 | 0-0,25 | 0-0,25 |
| | 3-Month Deposits | 1.21 | 1.20 | 1.20 | 1.20 |
| | 10-Year US-Treasury | 2.72 | 2.70 | 3.00 | 4.00 |
| Canada | Overnight Rate | 0.50 | 0.50 | 0.50 | 0.50 |
| | 3-Month Deposits | 1.00 | 1.20 | 1.00 | 1.00 |
| | 10-Year Government Bonds | 2.82 | 3.00 | 3.20 | 4.10 |
| Australia | Cash Rate | 3.25 | 2.75 | 2.75 | 2.75 |
| | 3-Month Deposits | 3.68 | 3.40 | 3.30 | 3.10 |
| | 10-Year Government Bonds | 4.64 | 4.20 | 4.30 | 5.00 |
| New Zealand | Cash Rate | 3.00 | 3.00 | 2.50 | 2.50 |
| | 3-Month Deposits | 3.79 | 4.50 | 3.30 | 3.00 |
| | 10-Year Government Bonds | 5.40 | 4.70 | 4.80 | 5.60 |
| Japan | Call Rate | 0.10 | 0.10 | 0.10 | 0.10 |
| | 3-Month Deposits | 0.61 | 0.70 | 0.70 | 0.70 |
| | 10-Year Government Bonds | 1.33 | 1.30 | 1.30 | 1.50 |
| UK | Bank Rate | 0.50 | 0.50 | 0.50 | 0.50 |
| | 3-Month Deposits | 1.67 | 1.20 | 0.90 | 0.90 |
| | 10-Year Government Bonds | 3.19 | 3.30 | 3.30 | 3.80 |
| Sweden | Repo Rate | 1.00 | 0.50 | 0.50 | 0.50 |
| | 3-Month Deposits | 1.13 | 0.80 | 0.70 | 0.70 |
| | 10-Year Government Bonds | 3.12 | 3.00 | 3.00 | 3.60 |
| Norway | Overnight Deposits | 2.00 | 2.00 | 1.50 | 1.50 |
| | 3-Month Deposits | 2.97 | 2.30 | 1.70 | 1.70 |
| | 10-Year Government Bonds | 3.82 | 3.80 | 3.90 | 4.60 |
| Switzerland | Repo Rate | 0.38 | 0.25 | 0.25 | 0.25 |
| | 3-Month Deposits | 0.40 | 0.30 | 0.30 | 0.30 |
| | 10-Year Government Bonds | 2.16 | 2.10 | 2.10 | 2.70 |
| Poland | 2w Repo Rate | 3.75 | 3.25 | 2.75 | 2.00 |
| | 3-Month Deposits | 4.14 | 3.50 | 3.10 | 2.40 |
| | 10-Year Government Bonds | 6.29 | 5.90 | 5.90 | 6.10 |
| Czech Rep. | 2w Repo Rate | 1.75 | 1.50 | 1.25 | 1.25 |
| | 3-Month Deposits | 2.45 | 2.20 | 1.80 | 2.00 |
| | 10-Year Government Bonds | 5.64 | 4.90 | 4.80 | 5.00 |
| Hungary | Base Rate | 9.50 | 9.00 | 8.00 | 6.50 |
| | 3-Month Deposits | 9.73 | 8.90 | 7.90 | 6.60 |
| | 10-Year Government Bonds | 12.16 | 11.50 | 10.00 | 8.00 |

Source EcoWin, WestLB Research

Foreign exchange

| | | current 30.03.09 | in 3 months | in 6 months | in 12 Months |
|----------|---------------|---------------------|----------------|----------------|-----------------|
| vs. Euro | USD/EUR | 1.32 | 1.30 | 1.30 | 1.40 |
| | CAD/EUR | 1.65 | 1.61 | 1.66 | 1.89 |
| | AUD/EUR | 1.94 | 2.00 | 2.17 | 2.55 |
| | NZD/EUR | 2.34 | 2.36 | 2.36 | 2.80 |
| | JPY/EUR | 127.93 | 130.00 | 137.00 | 161.00 |
| | GBP/EUR | 0.93 | 0.90 | 0.86 | 0.82 |
| | SEK/EUR | 10.97 | 10.50 | 10.00 | 9.90 |
| | NOK/EUR | 8.95 | 8.80 | 8.70 | 8.50 |
| | CHF/EUR | 1.52 | 1.52 | 1.53 | 1.56 |
| | PLN/EUR | 4.73 | 4.75 | 4.75 | 4.20 |
| | CZK/EUR | 27.47 | 28.50 | 28.50 | 27.00 |
| | HUF/EUR | 308.65 | 300.00 | 300.00 | 270.00 |
| | vs. US Dollar | CAD/USD | 1.25 | 1.24 | 1.28 |
| USD/AUD | | 0.68 | 0.65 | 0.60 | 0.55 |
| USD/NZD | | 0.56 | 0.55 | 0.55 | 0.50 |
| JPY/USD | | 96.97 | 100.00 | 105.00 | 115.00 |
| USD/GBP | | 1.42 | 1.44 | 1.51 | 1.71 |
| SEK/USD | | 8.31 | 8.08 | 7.69 | 7.07 |
| NOK/USD | | 6.78 | 6.77 | 6.69 | 6.07 |
| CHF/USD | | 1.15 | 1.17 | 1.18 | 1.11 |
| PLN/USD | | 3.58 | 3.65 | 3.65 | 3.00 |
| CZK/USD | | 20.82 | 21.92 | 21.92 | 19.29 |
| HUF/USD | | 233.95 | 230.77 | 230.77 | 192.86 |

Source EcoWin, WestLB Research

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