

Economic Cycles

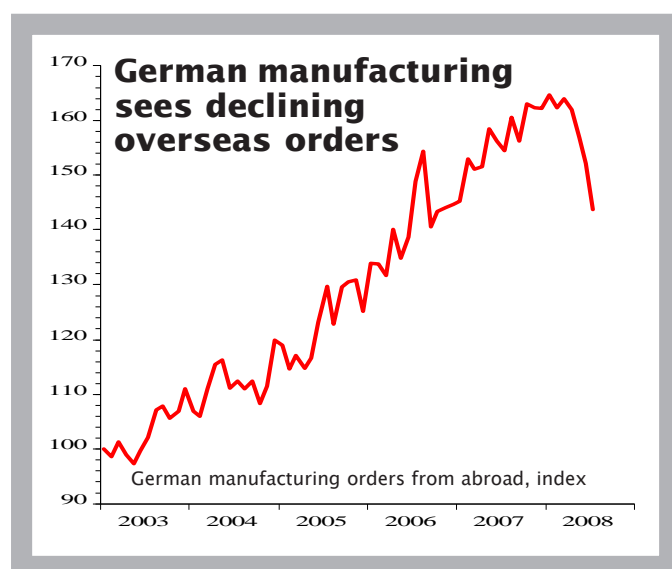
One size does not fit all

Exports drive German growth

The collapse in the German unemployment rate in recent years has been due to a surge in German capacity as utilisation rates rose to meet the strong external demand for goods from the US, Europe and Asian economies. German consumer spending has barely grown over the last five years.

Capex runs into the sand

But now, globally, corporates might delay investment projects. Not because of lack of credit, but much more because of greater uncertainty caused by the sharp decline in share prices over the last quarter - following the 1987 crash, capex growth suffered a sharp setback for two quarters, and the same could happen this time. For the US, Stephen Gallagher expects business investment to decline at an accelerating pace over the coming six months, the first drop in business investment in this economic downturn. In Japan also, Glenn Maguire is looking for a decline in business investment over the coming months. Even Chinese capex growth is likely to slow further.



German unemployment to edge higher

German manufacturing firms are already seeing declining overseas orders - most probably of consumer goods, because of the US and European consumer slowdown over the summer months. However, even if these consumer goods exports recover, as US consumer spend lifts due to lower energy bills, German exports may remain in the doldrums because capital goods exports are likely to head lower. So, the pick-up in exports

that propelled German employment is now running out of steam. And so the German unemployment rate may increase by around 0.5% over 2009.

Modest rate cuts from the ECB

With inflation rates collapsing and unemployment rising in the core European economies during 2009, the ECB is likely to ease rates, albeit grudgingly and modestly over the coming months. However, if the decline in capex proves to be temporary and modest as SG economists anticipate, then German exports may start to recover by the second half of 2009, probably putting a stop to any further easing. That may suit Germany, but not all of its eurozone colleagues.

The Irish solution

The Irish banks' share price index has now fallen by 70% from its 2006 level, whereas the US banks' share price index has fallen by only 20% from its 2006 level. Worries that declining share prices could spark a run on bank deposits led the Irish Parliament to approve a bill guaranteeing all customer deposits, including money market deposits. Though this move may stem or even reverse the outflow of deposits, and make it easier for the Irish banks to borrow in the money markets, it does not solve the bigger problem of collapsing house prices, and capital erosion at Irish banks.

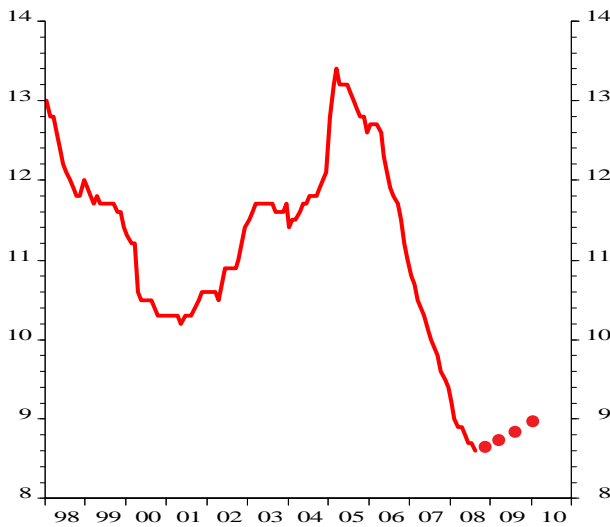
The Irish problem

Housing starts in Ireland are now running at a quarter of the pace of two years ago; consumer spending is falling; unemployment is rising; and house prices are already down 13% from the peak reached in early 2007. Ireland needs substantially lower rates to reverse these negative trends, but the likelihood is of only modest rate cuts from the ECB.

The Hong Kong parallel

The collapse in Hong Kong property prices between 1998 and 2003 provides a classic example of tying monetary policy to the fortunes of a larger economy. Hong Kong property prices declined by 32% in 1998 as the shock from the Asian tiger crisis reverberated through the region. In 1999 and 2000, the Fed raised rates forcing the Hong Kong monetary Authority to raise rates; property prices fell another 20%!

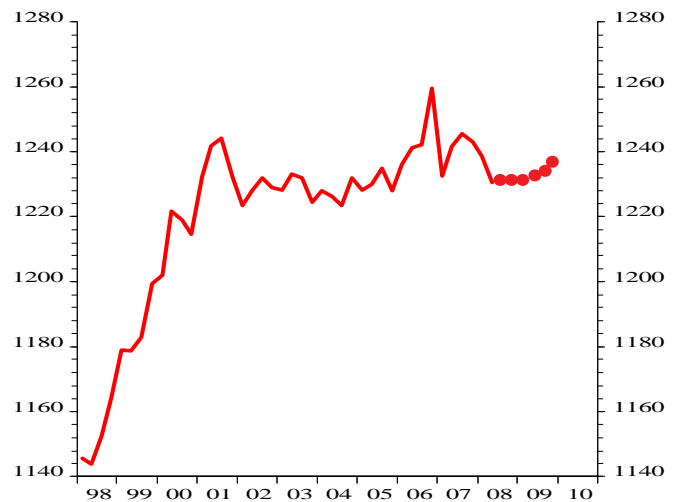
German unemployment declined in recent years ...



German unemployment rate, %

Source: Datastream, SG Economic Research

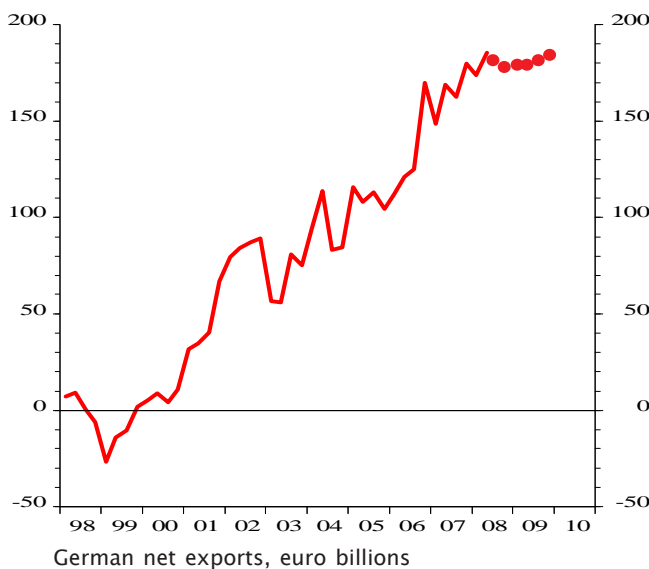
... not due to consumer spending



German consumer spending, euro billion

Source: Datastream, SG Economic Research

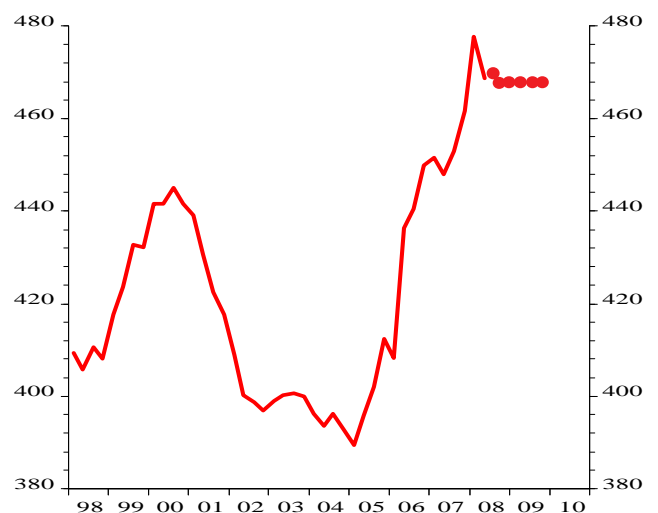
... but due to a surge in exports



German net exports, euro billions

Source: Datastream, SG Economic Research

... that led to a build up of capacity in German manufacturing

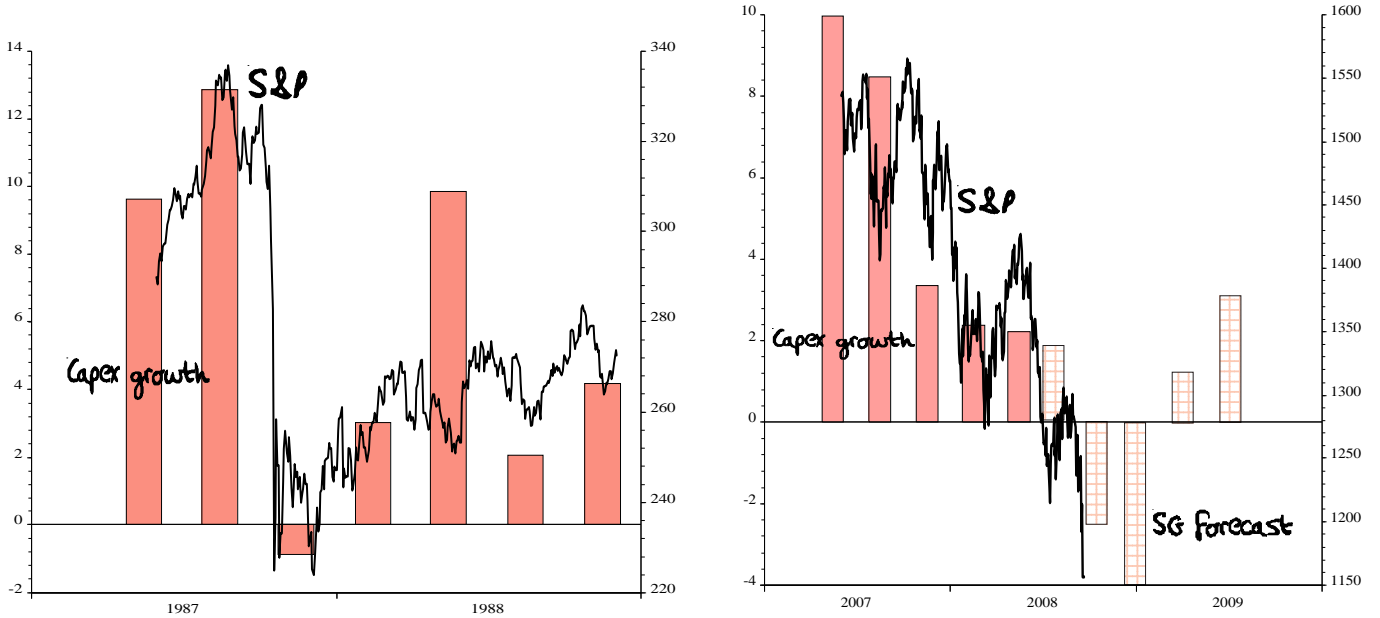


German capital expenditure, euro billions

Source: Datastream, SG Economic Research

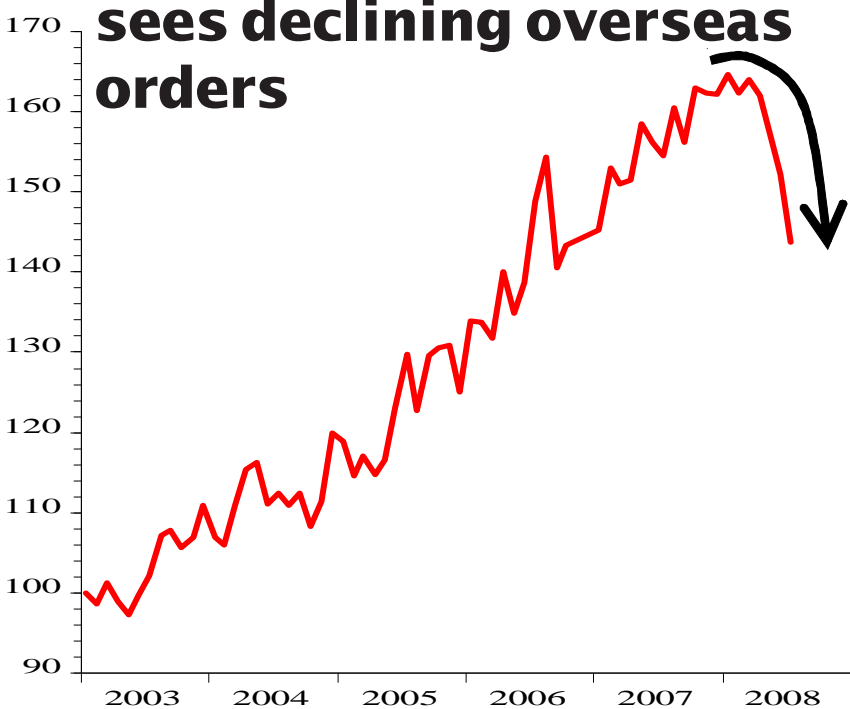
Capex runs into the sand

Now, corporates might delay investment projects. Not because of lack of credit, but much more because of greater uncertainty caused by the sharp decline in share prices over the last quarter - following the 1987 crash, capex growth suffered a sharp setback for two quarters, and the same could happen this time.



S&P Composite Index (Right hand scale)
 ■ US business investment, % change over 1 quarter, annualised
 Source: Datastream, SG Economic Research

German manufacturing sees declining overseas orders

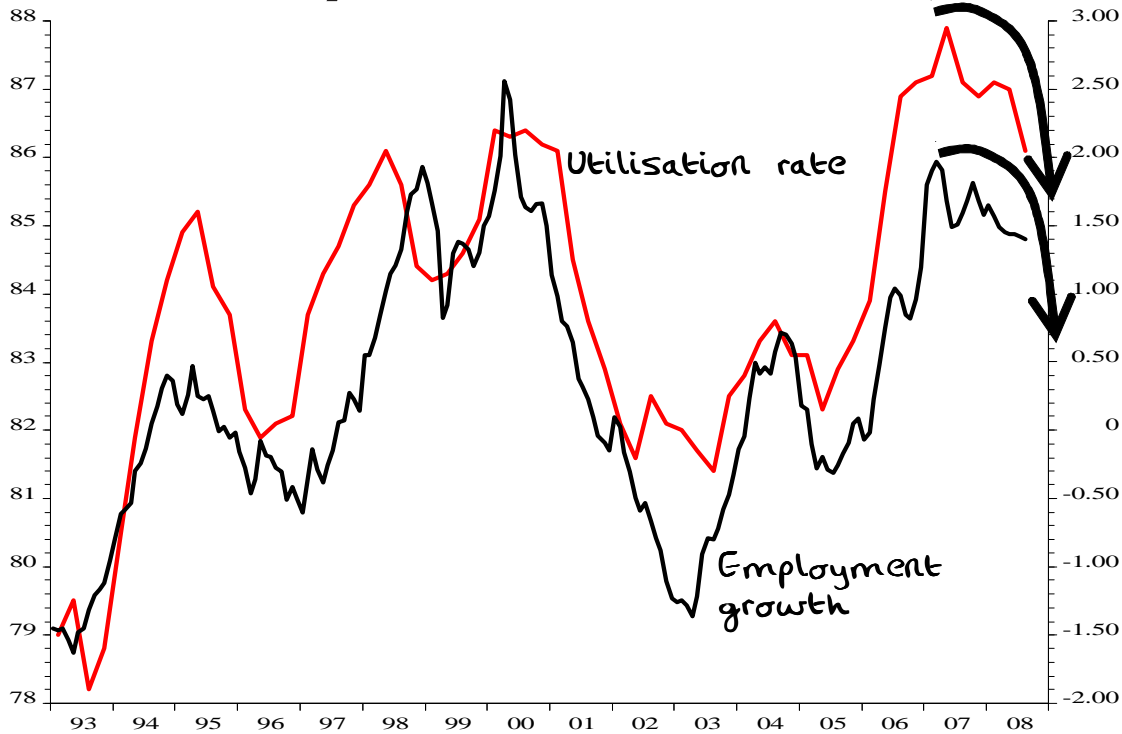


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However, even if these consumer goods exports recover, as US consumer spend lifts due to lower energy bills, German exports may remain in the doldrums because capital goods exports are likely to head lower.

German manufacturing orders from abroad, index
 Source: Datastream, SG Economic Research

German employment growth to slow dramatically



So, the pick-up in exports that propelled German employment is now running out of steam. And so the German unemployment rate may increase by around 0.5% over 2009.

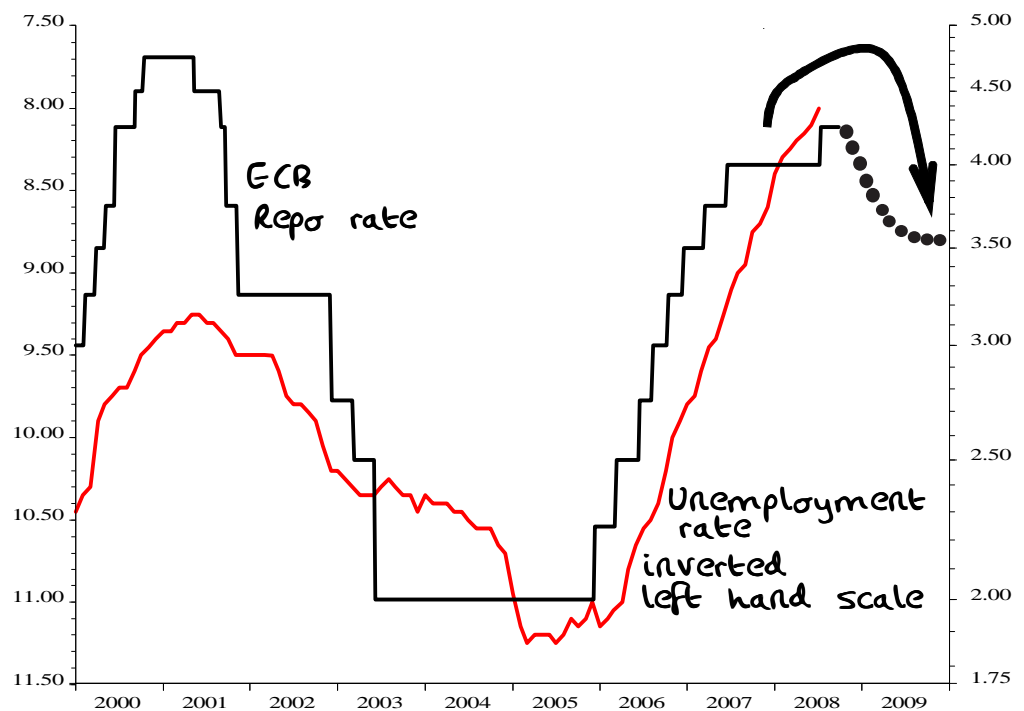
German manufacturing utilisation rate, %
German employment, % change over 1 year, (Right Hand Scale)
Source: Datastream, SG Economic Research

Modest rate cuts from the ECB

With inflation rates collapsing and unemployment rising in the core European economies during 2009, the ECB is likely to ease rates, albeit grudgingly and modestly over the coming months.

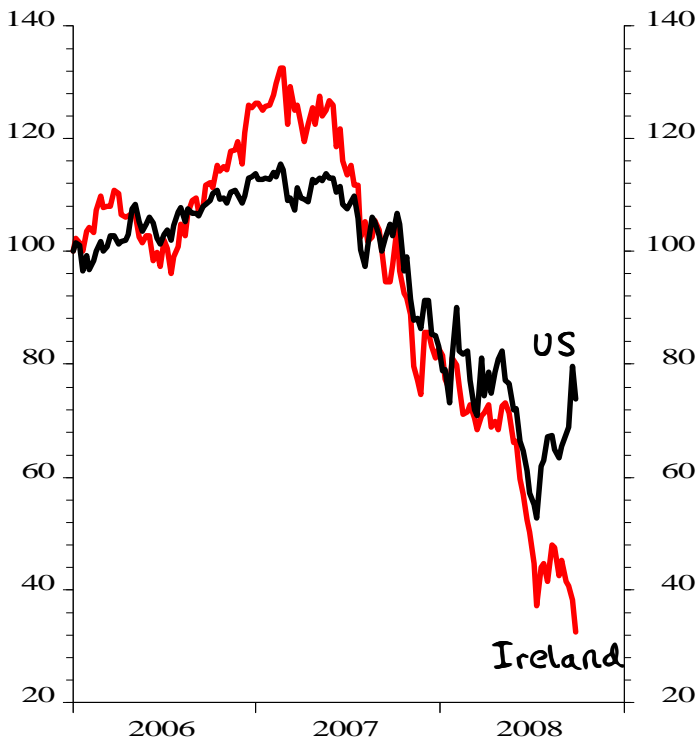
However, if the decline in capex proves to be temporary and modest as SG economists anticipate, then German exports may start to recover by the second half of 2009, probably putting a stop to any further easing.

That may suit Germany, but not all of its eurozone colleagues.



Core Europe unemployment rate, %, inverted scale
ECB Repo Rate, % (Right Hand Scale)
Source: Datastream, SG Economic Research

The Irish solution



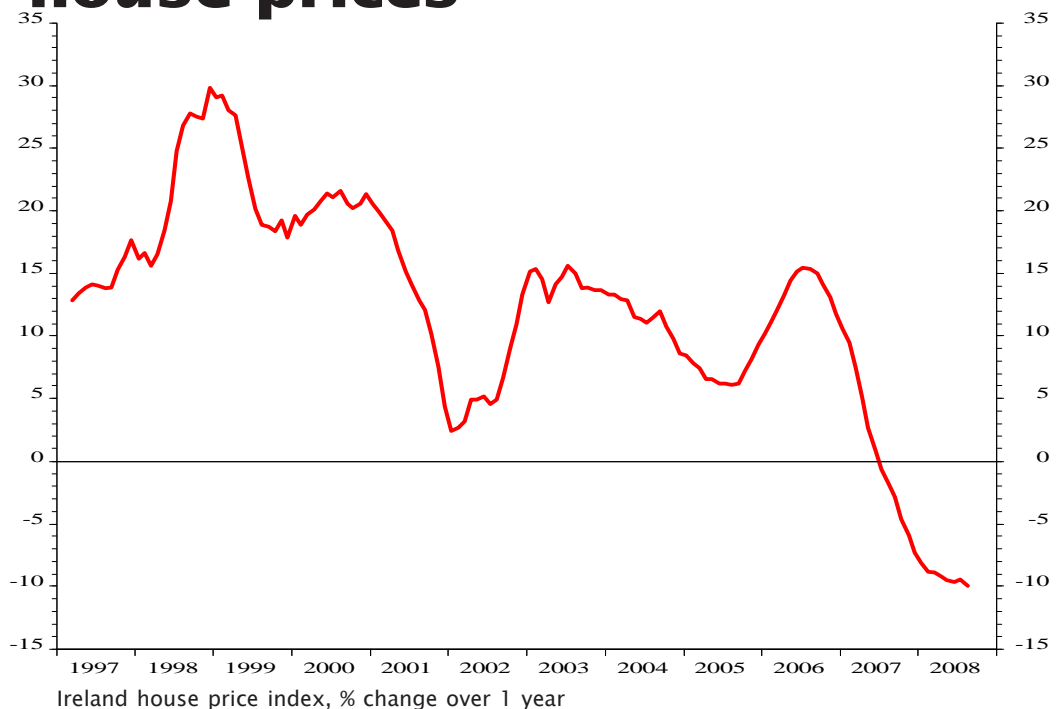
The Irish banks' share price index has now fallen by 70% from its 2006 level, whereas the US banks' share price index has fallen by only 20% from its 2006 level.

Worries that declining share prices could spark a run on bank deposits led the Irish Parliament to approve a bill guaranteeing all customer deposits, including money market deposits.

Irish bank share price index
US bank share price index
Source: Datastream, SG Economic Research

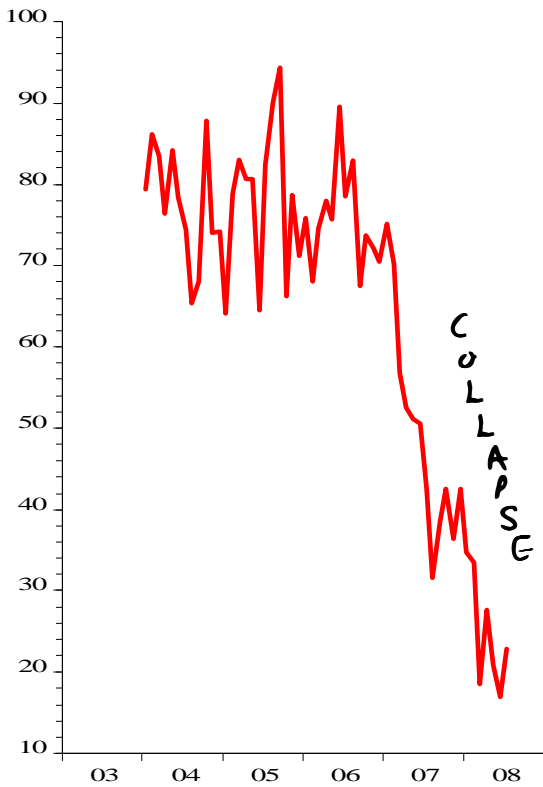
Banks battered by declining house prices

Though the Irish government move may stem or even reverse the outflow of deposits, and make it easier for the Irish banks to borrow in the money markets, it does not solve the bigger problem of collapsing house prices, and capital erosion at Irish banks.



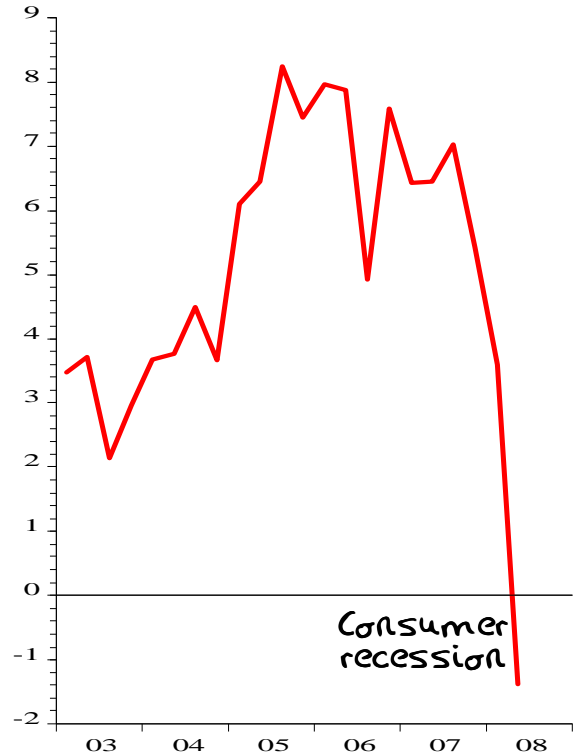
Ireland house price index, % change over 1 year
Source: Datastream, SG Economic Research

Irish housing starts have collapsed ...



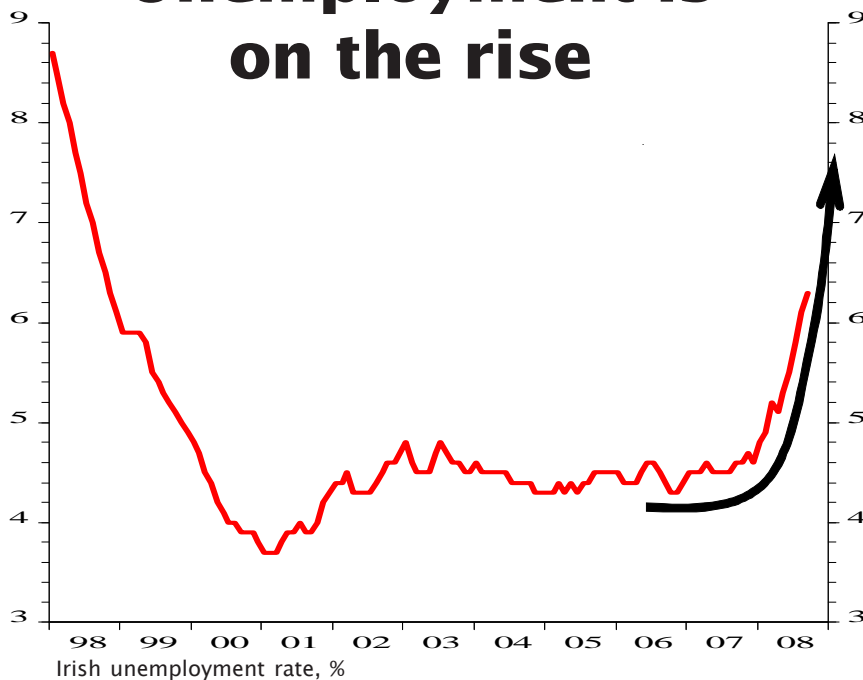
Irish housing starts, thousands, annual rate
Source: Datastream, SG Economic Research

... as has consumer spending



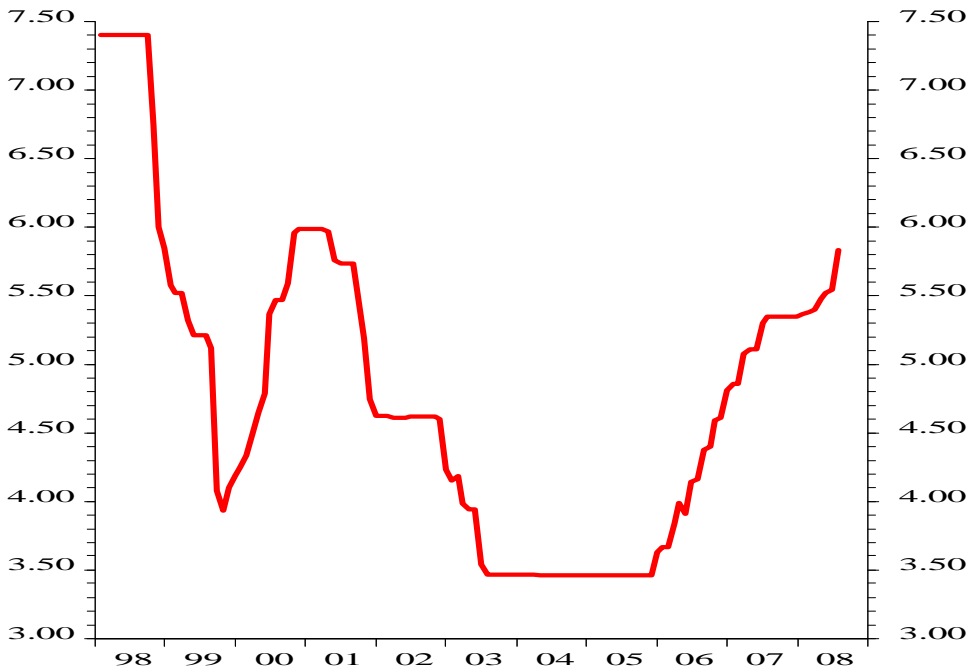
Irish real consumer spending, % change over 1 year
Source: Datastream, SG Economic Research

Unemployment is on the rise



Irish unemployment rate, %
Source: Datastream, SG Economic Research

Ireland needs substantial rate cuts ...

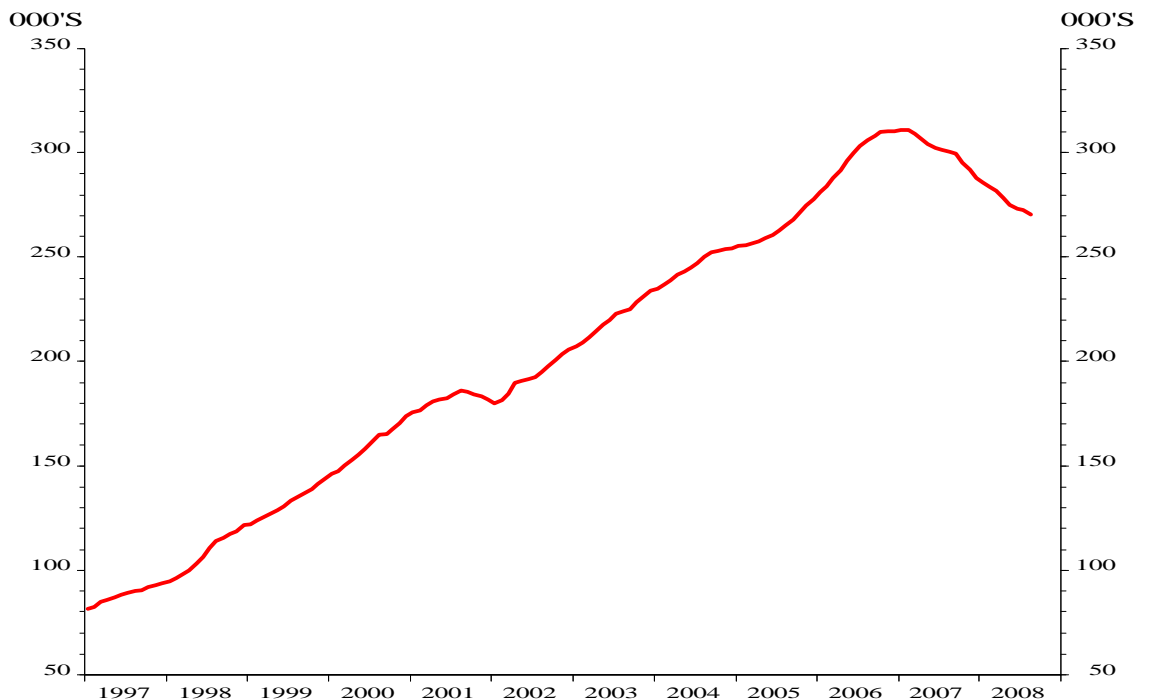


Ireland: average mortgage rate, %
Source: Datastream, SG Economic Research

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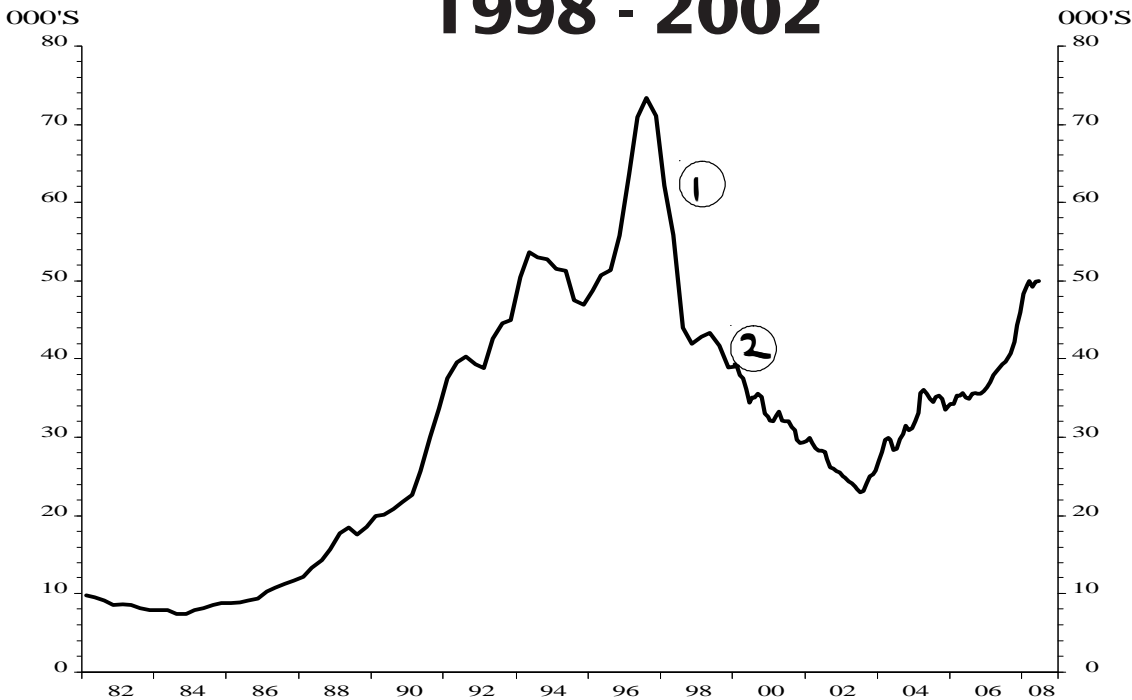
Ireland needs substantially lower rates to reverse these negative trends, but the likelihood is of only modest rate cuts from the ECB.

... to reverse the decline in house prices



Ireland house price in EUR
Source: Datastream, SG Economic Research

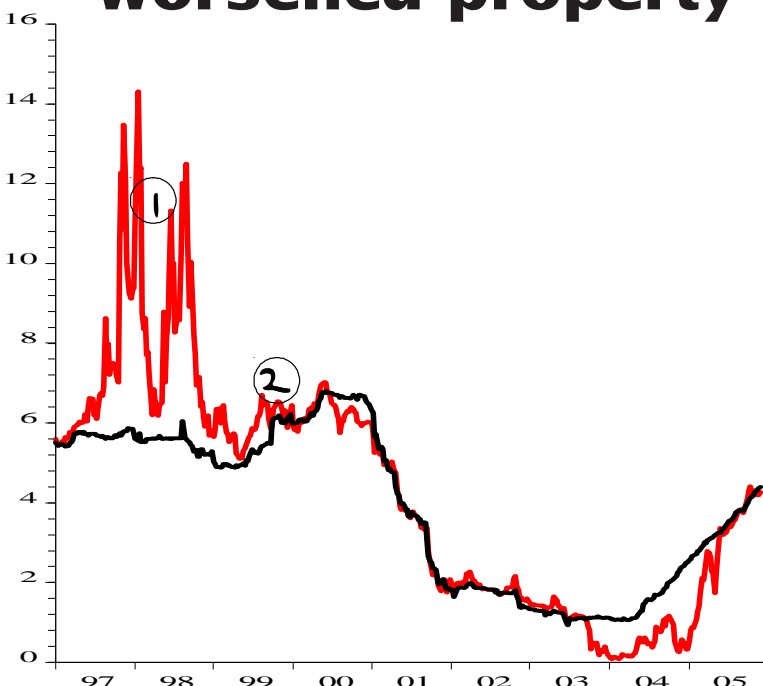
Hong Kong property price collapse 1998 - 2002



HK house prices in HKD for apartments less than 40m²

Source: *Datastream, SG Economic Research*

Higher rates in 1999 and 2000 worsened property crisis



HK Interbank rate 3 months

US Libor 3 months

Source: *Datastream, SG Economic Research*

The collapse in Hong Kong property prices between 1998 and 2003 provides a classic example of tying monetary policy to the fortunes of a larger economy.

Hong Kong property prices declined by 32% in 1998 as the shock from the Asian tiger crisis reverberated through the region.

In 1999 and 2000, the Fed raised rates forcing the Hong Kong monetary Authority to raise rates; property prices fell another 20%!

Newsflow of economic stories

Our proprietary newsflow indicator shows the number of newspaper and newswire articles which report economic strength. This is expressed as a percentage of all economic news stories. Trends in newsflow reflect *sentiment* towards trends in the underlying economy. For example, in the UK, the percentage of strong economic news stories is now at 28%. At the peak of the cycle in March 2006, 66% of all news stories related to economic strength.

World Newsflow of Economic Stories



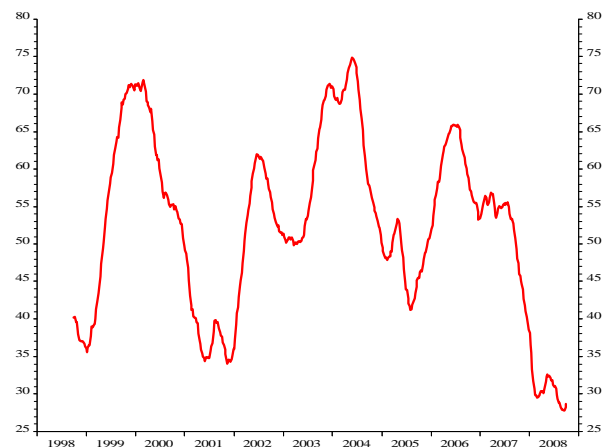
US Newsflow of Economic Stories



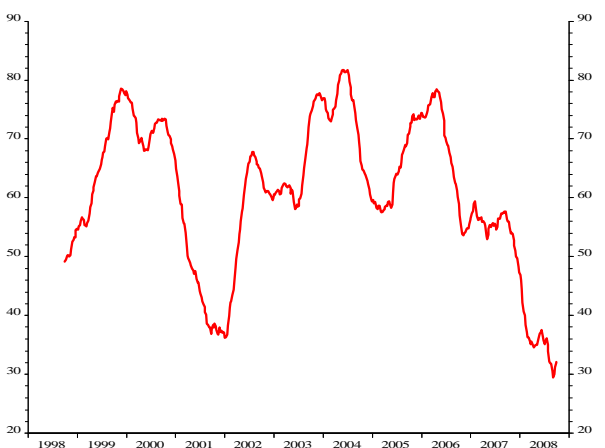
Eurozone Newsflow of Economic Stories



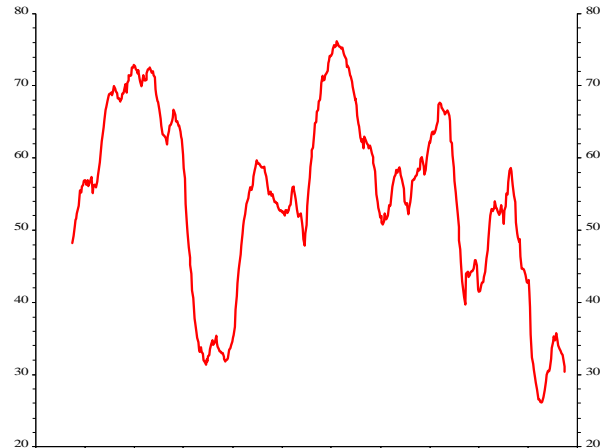
UK Newsflow of Economic Stories



Japan Newsflow of Economic Stories

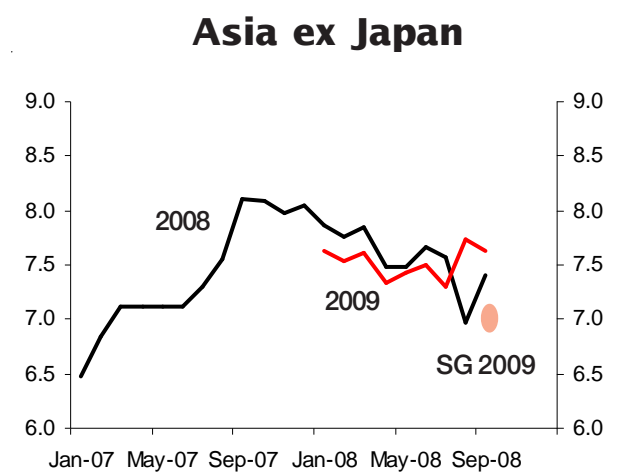
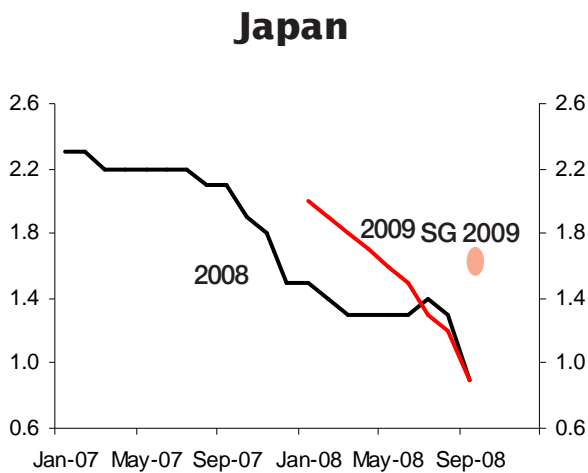
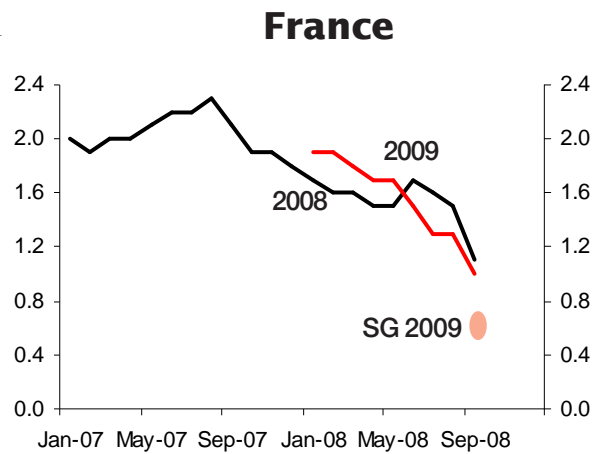
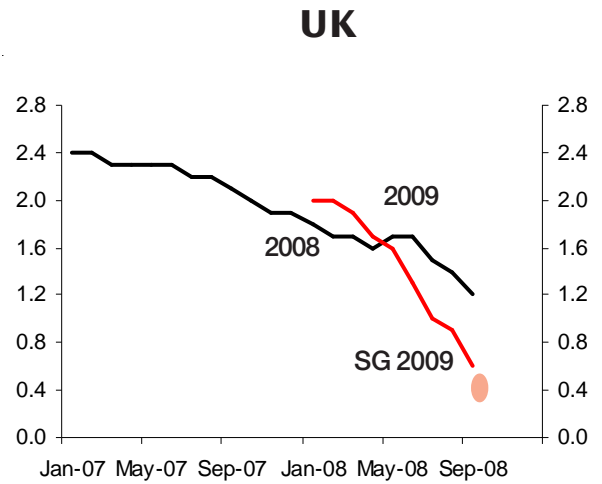
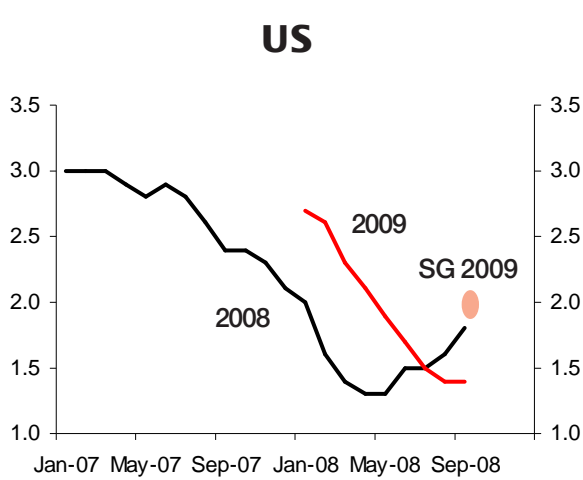


Pacific Rim Newsflow of Economic Stories



Source: Factiva, SG Economic Research

Consensus GDP growth forecasts



● SG forecast for 2009 in August 2008

Source: Datastream, SG Economic Research, Consensus Economics

SG GDP growth and inflation forecasts

	Real GDP				Inflation			
	2006	2007	2008	2009	2006	2007	2008	2009
<i>real world</i> World (current \$ weights)	4.1	3.9	2.9	2.6	3.0	3.1	5.1	3.7
World (PPP weights)	5.5	5.4	3.8	3.5	3.4	3.8	5.9	4.3
Industrialised countries (PPP)	2.8	2.4	1.4	1.3	2.4	2.1	3.7	2.6
Emerging countries (PPP)	8.3	8.4	6.7	6.1	4.5	5.5	8.5	6.3
USA <i>economists world</i>	2.8	2.0	1.8	1.8	3.2	2.9	4.7	3.3
Japan	2.4	2.0	1.0	1.5	0.1	0.0	0.9	1.5
Canada	3.1	2.7	1.2	2.2	2.0	2.1	2.8	2.4
Australia	2.9	4.2	2.5	2.5	3.5	2.3	4.5	4.0
New Zealand	1.7	3.1	0.6	1.3	3.4	2.4	4.3	3.9
EU 27	3.4	3.1	1.6	1.0	2.3	2.4	3.8	2.4
Euro zone	2.9	2.6	1.1	0.5	2.2	2.1	3.5	2.0
France	2.0	2.0	0.9	0.6	1.9	1.6	3.4	2.1
Germany	3.2	2.6	1.4	0.4	1.8	2.3	3.0	1.8
Italy	1.9	1.4	0.0	0.2	2.2	2.0	3.8	2.4
Netherlands	3.4	3.5	2.2	1.0	1.5	1.7	1.6	1.1
Spain	3.9	3.8	1.4	0.5	3.6	2.8	4.5	2.5
Denmark	3.9	1.7	1.3	1.1	1.9	1.7	3.1	2.4
Norway	2.5	3.7	3.1	2.1	2.3	0.7	3.5	2.7
Sweden	4.0	3.0	2.1	2.0	1.4	2.2	3.7	2.7
Switzerland	3.2	3.1	2.0	1.5	1.1	0.7	2.5	1.5
UK	2.9	3.1	1.1	0.4	2.3	2.3	3.8	2.8
East. Europe	7.1	7.3	6.4	5.5	8.5	8.4	10.6	7.5
Russia	7.3	8.1	7.4	6.2	9.8	9.1	14.0	9.5
Total Asia ex Japan	9.7	9.8	7.7	7.0	3.4	4.8	7.8	5.2
China	11.6	11.9	9.5	8.5	1.5	4.8	7.0	4.0
HK	7.0	6.1	5.5	5.0	2.0	2.0	5.0	3.5
India	9.8	9.3	7.5	7.0	5.8	6.4	11.0	8.5
Indonesia	5.5	6.2	6.0	5.5	13.1	6.4	11.0	8.0
S. Korea	5.1	5.0	4.3	4.0	2.2	2.5	5.0	3.0
Malaysia	6.0	6.0	5.5	5.0	3.6	2.0	5.0	4.0
Philippines	5.0	6.9	6.0	5.0	6.3	2.8	7.0	5.0
Singapore	8.2	7.7	5.5	4.5	1.0	2.1	5.0	3.0
Taiwan	5.0	4.3	4.0	3.5	0.6	1.8	4.0	2.0
Thailand	5.0	4.0	5.0	4.5	4.6	2.2	5.0	4.0
Vietnam	8.0	8.0	5.5	7.0	7.5	8.3	23.0	18.0
Latam	5.4	5.6	4.5	4.5	4.8	5.3	7.0	7.0
Brazil	3.7	5.4	4.6	4.4	3.3	4.1	4.4	4.2
Mexico	5.0	3.0	2.7	3.5	3.6	4.0	3.8	3.5

Note: Average over calendar year

Source: Datastream, SG Economic Research, Consensus Economics

SG Central Bank rate, yield and FX forecasts

Central Bank Rate Forecasts

		current	3 mths	6 mths	9 mths	1 yr
US	Fed Funds rate	2.00	1.50	1.50	1.50	1.50
Canada	Overnight rate	3.00	3.00	3.00	3.00	3.00
Euro zone	Refi rate	4.25	4.00	3.75	3.50	3.50
UK	Bank rate	5.00	4.50	4.00	3.75	3.50
Japan	Overnight call rate	0.50	0.50	0.50	0.50	0.75
Australia	Cash rate	7.00	6.75	6.50	6.00	5.75
New Zealand	Cash rate	7.50	7.25	7.00	6.75	6.50

10 year bond yields

	current	6 mths	1 yr
US	3.62	3.90	4.30
Canada	3.64	3.95	4.55
Euro zone	3.85	3.95	4.05
UK	4.29	4.15	4.05
Japan	1.46	1.50	1.90
Australia	5.27	5.65	5.80
New Zealand	5.67	5.95	6.05

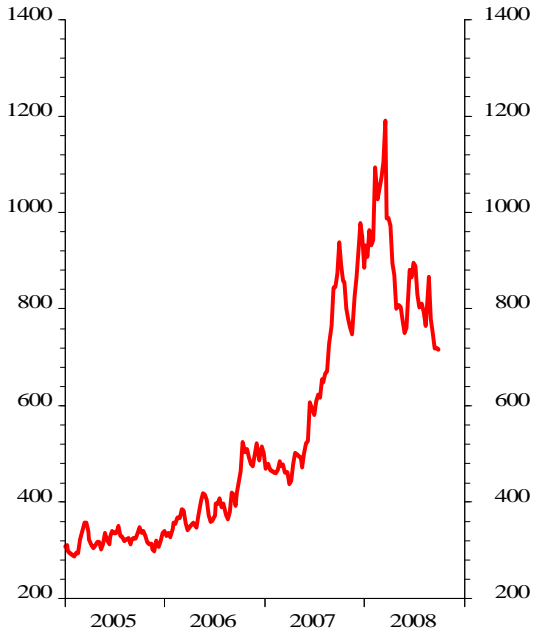
FX rates

	current	6 mths	1 yr
USD per EUR	1.38	1.40	1.30
CAD per USD	1.08	1.05	1.15
GBP per EUR	0.78	0.82	0.83
USD per GBP	1.76	1.71	1.57
JPY per USD	105.2	110	115
USD per AUD	0.79	0.82	0.78
USD per NZD	0.66	0.64	0.61

Source: Bloomberg, SG Economic Research

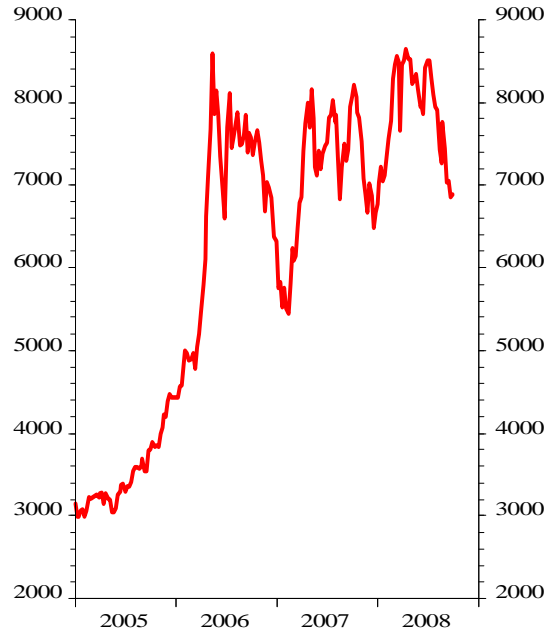
Commodity prices

Wheat



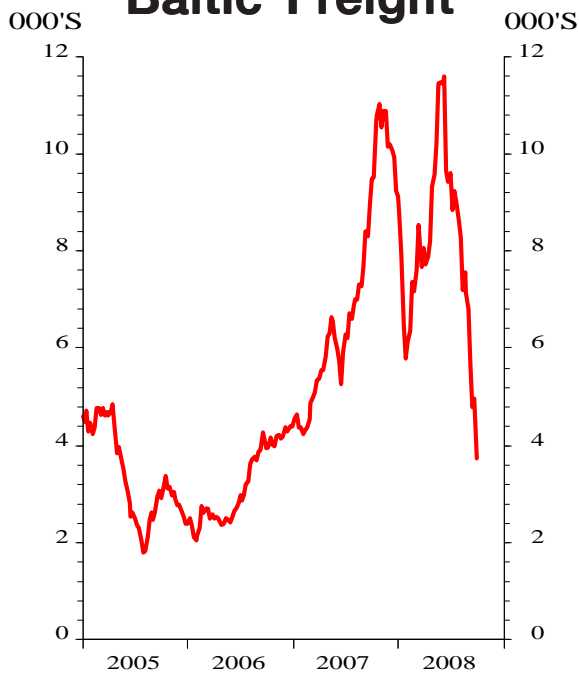
CBT Wheat, near month future, \$/bushel

Copper



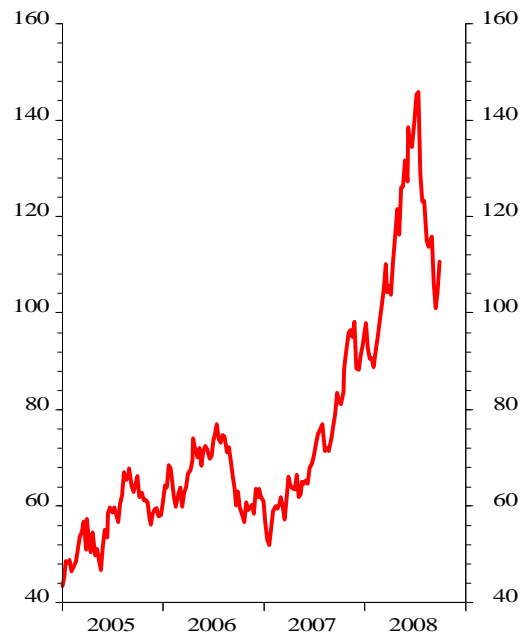
CMX Copper near month future, \$/£

Baltic Freight



Baltic dry freight

Crude oil



West Texas Intermediate, near month future, \$/bbl

Economic releases for week of Oct 6 - Oct 10

WEEK			Period	Previous	SG Forecast	Consensus
UK		HBOS House Price 3Mths/Year	SEP	-10.9%	na	-12.5%
			SEP	-1.8%	na	-1.7%
Monday 6-Oct-2008						
			Period	Previous	SG Forecast	Consensus
04:00	Japan	BoJ Monetary Policy Meeting				
08:30	UK	Industrial Production (MoM)	AUG	-0.4%	-0.3%	-0.1%
08:30		Industrial Production (YoY)	AUG	-1.9%	-2.1%	-1.9%
08:30		Manufacturing Production (MoM)	AUG	-0.2%	-0.4%	-0.2%
08:30		Manufacturing Production (YoY)	AUG	-1.4%	-1.8%	-1.6%
12:30	Canada	Building Permits (MoM)	AUG	1.8%	na	-1.0%
13:00	US	Volcker Ferguson speaks in New York on Financial Supervision				
15:30		Treasury's Ryan speaks in New York at Industry Conference				
16:00		Fed's Evans Speaks on Economic Outlook in Texas				
23:50	Japan	Official Reserve Assets (USD bln)	SEP	996.7	na	na
Tuesday 7-Oct-2008						
			Period	Previous	SG Forecast	Consensus
	Japan	BOJ Target Rate		0.50%	0.50%	0.50%
03:30	Australia	Reserve Bank's Interest Rate Decision	OCT	7.00%	6.75%	6.50%
05:00	Japan	Coincident Index CI	AUG P	103.5	na	100.7
05:00		Leading Index CI	AUG P	91.4	na	89.2
07:30	Sweden	Budget Balance (SEK bln)	SEP	0	na	na
08:00	Norway	Ind Prod Manufacturing SA (MoM)	AUG	0.1%	na	na
08:00		Ind Prod Manufacturing NSA (YoY)	AUG	3.7%	na	na
08:00		Industrial Production SA (MoM)	AUG	1.2%	na	na
08:00		Industrial Production NSA (YoY)	AUG	1.9%	na	na
10:00	Germany	Factory Orders (MoM) (sa)	AUG	-1.7%	-1.0%	0.5%
10:00		Factory Orders (YoY) (sa)	AUG	na	-6.1%	na
13:30	Eurozone	ECB's Trichet Speaks in Evian, France				
15:00	US	Fed's Stern Speaks in Chicago on Financial Shock				
16:30		Bernanke Speaks to Economics Conference in Washington				
18:00		Minutes of FOMC Meeting	Sept-16			
19:00		Consumer Credit (USD bln)	AUG	4.6	na	6
Wednesday 8-Oct-2008						
			Period	Previous	SG Forecast	Consensus
00:30	Australia	Investment Lending	AUG	2.3%	na	na
05:00	Japan	BOJ Monthly Report	Oct-07			
05:00		Eco Watchers Survey: Current	SEP	28.3	na	na
05:00		Eco Watchers Survey: Outlook	SEP	32	na	na
06:45	France	Central Govt. Balance (EUR bln)	AUG	-51.4	na	na
06:45		Trade Balance (EUR bln)	AUG	-4.8	na	-4.5
07:30	Sweden	Industrial Orders s.a. (MoM)	AUG	1.0%	na	na
07:30		Industrial Orders n.s.a. (YoY)	AUG	1.6%	na	na
07:30		Industrial Prod. s.a. (MoM)	AUG	1.2%	na	na
07:30		Industrial Prod. n.s.a. (YoY)	AUG	0.9%	na	na
09:00	Eurozone	Euro-Zone GDP s.a. (QoQ)	2Q F	0.7%	-0.2%	-0.2%
09:00		Euro-Zone GDP s.a. (YoY)	2Q F	2.1%	1.4%	1.4%
09:00		Euro-Zone Gross Fix Cap (QoQ)	2Q F	1.5%	-1.2%	na
09:00		Euro-Zone Household Cons (QoQ)	2Q F	0.0%	-0.2%	na
09:30	UK	BRC September Shop Price Index				
10:00	Germany	Industrial Production (MoM) (sa)	AUG	-1.8%	0.8%	-0.5%
10:00		Industrial Prod. (YoY) (sa)	AUG	-0.6%	-1.5%	na
11:00	Switzerland	Swiss Government Announces Bond Auction Results				
11:00	US	MBA Mortgage Applications	Oct-03	-23.0%	na	na
11:45		Philadelphia Fed's Plosser speaks on Fed Policies in New York				
14:00		Pending Home Sales (MoM)	AUG	-3.2%	na	-1.1%
23:50	Japan	Machine Orders (MoM)	AUG	-3.9%	na	-2.7%
23:50		Machine Orders (YoY)	AUG	-4.7%	na	-2.3%

continued on following page ...

Economic releases for week of Oct 6 - Oct 10

Thursday 9-Oct-2008		Period	Previous	SG Forecast	Consensus	
	China	Business Climate Index	3Q	137.4	na	na
	US	ICSC Chain Store Sales (YoY)	SEP	1.7%	na	na
00:30	Australia	Employment Change, K	SEP	14.6	na	0
00:30		Participation Rate	SEP	65.2%	na	65.2%
00:30		Unemployment Rate	SEP	4.1%	na	4.3%
06:00	Germany	Wholesale Price Index (MoM)	SEP	-1.8%	na	na
06:00		Wholesale price Index (YoY)	SEP	7.4%	na	na
06:00		Current Account (EUR bln)	AUG	11.8	na	9
06:00		Exports SA (MoM)	AUG	-1.7%	na	0.5%
06:00		Imports SA (MoM)	AUG	7.4%	na	-2.0%
06:00		Trade Balance, (EUR bln)	AUG	13.9	na	12
07:30	Sweden	Activity Index Level	AUG	123.6	na	na
07:30		CPI - Headline Rate (MoM)	SEP	0.2%	na	na
07:30		CPI - Headline Rate (YoY)	SEP	4.3%	na	na
07:30		CPI - Underlying Infl. (MoM)	SEP	0.1%	na	na
07:30		CPI - Underlying Infl. (YoY)	SEP	3.2%	na	na
07:30		CPI Level	SEP	301.98	na	na
08:00	Eurozone	ECB Publishes Monthly Report	OCT			
08:30	UK	Trade Balance Non EU (GBP mln)	AUG	-4726	-4600	-4600
08:30		Visible Trade Balance (GBP mln)	AUG	-7667	-7700	-7600
09:00	Switzerland	SNB Publishes Quarterly Bulletin	3Q			
11:00	UK	Bank of England Interest Rate Decision		5.00%	4.75%	4.75%
12:30	US	Initial Jobless Claims, K	Oct-04	497	na	na
12:30	India	Wholesale Price Index (YoY)	Sep-27	12.2%	na	na
14:00	US	Wholesale Inventories	AUG	1.4%	na	0.4%
17:30		Fed's Stern Speaks in Minneapolis on Financial Shock				
20:00		Boston Fed's Rosengren Speaks at University of Wisconsin				
23:50	Japan	BoJ Monetary Policy Meeting Minutes	SEP			
Friday 10-Oct-2008		Period	Previous	SG Forecast	Consensus	
	China	Entrepreneur Confidence Index	3Q	134.8	na	na
	India	Industrial Production (YoY)	AUG	7.1%	na	na
06:45	France	Industrial Production (MoM)	AUG	1.2%	na	-0.7%
06:45		Industrial Production (YoY)	AUG	-2.0%	na	-2.5%
06:45		Manufacturing Production (MoM)	AUG	1.5%	-0.8%	-0.9%
06:45		Manufacturing Production (YoY)	AUG	-2.3%	-3.0%	na
08:00	Italy	Industrial Production sa (MoM)	AUG	-1.1%	na	1.3%
08:00		Industrial Production nsa(YoY)	AUG	-0.6%	na	-6.8%
08:00		Industrial Production wda(YoY)	AUG	-3.2%	na	-4.0%
08:00	Norway	CPI (MoM)	SEP	0.1%	na	na
08:00		CPI (YoY)	SEP	4.5%	na	na
08:00		CPI Underlying (MoM)	SEP	-0.1%	na	na
08:00		CPI Underlying (YoY)	SEP	2.8%	na	na
08:00		Producer Prices incl.Oil (MoM)	SEP	-1.3%	na	na
08:00		Producer Prices incl.Oil (YoY)	SEP	33.8%	na	na
08:00	Sweden	AMV Unemployment Rate	3Q	3.0%	na	na
11:00	Canada	Net Change in Employment, K	SEP	15.2	na	12.5
11:00		Unemployment Rate	SEP	6.1%	na	6.2%
12:30		Int'l Merchandise Trade (CAD bln)	AUG	4.9	na	4.7
12:30	US	Import Price Index (MoM)	SEP	-3.7%	na	-2.5%
12:30		Import Price Index (YoY)	SEP	16.0%	na	na
12:30		Trade Balance (USD bln)	AUG	-62.2	-58	-59.3
14:00	Canada	Business Outlook Future Sales	3Q	4.0%	na	na

Source: Datastream, SG Economic Research, Bloomberg

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