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And now for the hard part…

Policymakers may have averted a prolonged spell in the financial wilderness…

…but the progress seen so far could yet prove to be the easiest part of the recovery…

…with a number of formidable, structural challenges awaiting on the horizon

By Stuart Green and Janet Henry

HSBC

And now for the hard part…

Meltdown averted, key challenges await

Given the gravity of the situation confronting policymakers in the dark days of last autumn, the positive developments seen since should not be downplayed. Due to the nature of the current crisis, conditions across both the financial markets and the real economy were always likely to prove more intertwined than usual, and both areas have seen substantial improvements in recent months. Although still subdued when compared to the 'norm' of recent years, risk appetite has made a welcome return, credit conditions have staged a cautious recovery and measures of both business and consumer confidence have bounced off exceptionally low levels. A spell in the financial wilderness now looks less likely for the major economies and our forecasts reflect this, with a slowly improving cyclical picture factored in for the rest of 2009 and 2010 across many regions.

However, financial markets, we suspect, may be about to find out that it's often better to travel than arrive. Despite all the developments of the past year, we believe that the most formidable challenges may lie ahead, and that the more demanding questions are yet to be answered. It now seems likely that the worst outcomes which threatened last autumn have been averted, but it's far from certain that a solid, durable recovery will emerge over the coming twelve months or, when abstracting from the cycle entirely, just what economic underpinnings remain.

The 'needs must' approach adopted by policymakers last autumn has presented investors with issues that will beguile for many years to come, while the worst excesses accumulated during the 'boom' years may be difficult to work off during the 'bust'. The need for possibly painful structural adjustment, both within and outside of the financial sectors of the major economies, and the threat of more onerous regulation, now loom large. What lies in wait over the economic horizon, therefore, remains a source of major anxiety. Indeed, given the extent to which activity collapsed around the turn of the year, the progress seen to date could yet prove to be the 'easiest' part of the recovery, with the hard part of any broader return to health yet to begin.

An underwhelming forecast

Our forecasts acknowledge both the most recent improvement in higher frequency data releases, and the more structural constraints that are likely to be encountered over the coming years. With the first quarter GDP data generally proving weaker than expected, our global 2009 GDP forecast has been lowered slightly to -2.3% from -1.9% previously, but most regions have seen an upward revision to their 2010 prospects, and the global growth forecast has risen in turn to 2.2% from the previous 1.6% estimate.

Europe, both East and West, has proved the exception here, with no significant upgrade forthcoming, except in the UK. The forecast for developed economy growth of just 1.2% next year, meanwhile, is distinctly underwhelming given the extent to which GDP has now contracted, particularly as many industrial sectors are still following a path more closely aligned to depression than recession. More optimistically, the apparent early success of China's fiscal stimulus is expected to sustain the clear out-performance of Asia, and emerging markets more generally, in 2010.

HSBC growth and inflation forecasts

GDP	'For those in Peril' (1 April 2009)		Latest	
	2009	2010	2009	2010
World	**-1.9**	**1.6**	**-2.3**	**2.2**
Developed	**-3.0**	**0.5**	**-3.4**	**1.2**
Emerging	**1.7**	**4.9**	**1.1**	**5.3**
US	-1.6	0.5	-1.9	1.9
UK	-3.8	-0.3	-3.8	1.6
Eurozone	-3.2	-0.1	-4.3	0.1
Japan	-6.5	1.6	-6.3	1.2
Brazil	0.1	2.6	-0.3	4.1
Russia	-2.8	2.3	-7.9	2.5
India	6.2	8.0	6.0	7.5
China	7.8	8.5	7.8	8.5
Inflation	**'For those in Peril' (1 April 2009)**		**Latest**	
	2009	**2010**	**2009**	**2010**
World	**0.8**	**1.6**	**0.9**	**1.8**
Developed	**-0.3**	**0.7**	**-0.1**	**0.9**
Emerging	**4.6**	**4.7**	**4.5**	**5.0**
US	-1.0	0.6	-0.6	0.8
UK	1.6	1.1	1.8	2.1
Eurozone	0.5	1.2	0.5	1.3
Japan	-1.4	-1.0	-1.4	-1.1
Brazil	4.6	4.3	4.4	4.8
Russia	12.2	11.5	11.6	11.5
India	6.9	4.7	7.0	5.8
China	-0.2	1.0	-0.6	0.8

Source: HSBC

Reshaping the future, and the past

Financial crises have a nasty habit of not only lowering expectations for future growth, but also challenging the assessment of earlier growth and the factors that drove this. Clearly, the prospect for a further rise in household sector indebtedness within the developed world now appears wholly dubious, not only due to the apparent willingness of individuals to pay down debt levels, but also because of the impaired ability of the financial system to facilitate any further increase.

The degree of adjustment seen in the US household sector to date has actually been fairly quick, reflecting among other factors the extraordinary decline in policy interest rates of the past year, and the equally dramatic fall in oil prices, factors that have consumers to pay down debt without curtailing spending too drastically. However, the lesson from earlier financial crises, which may yet be replicated elsewhere, is that once underway, this process of adjustment can be prolonged, painful and extremely disruptive to the establishment of a broader economic recovery.

Assuming the burden

It is important to remember that the often large-scale government intervention in financial sectors over the past year may not automatically lead to increased fiscal burdens, but the very volatile conditions across government bond markets have recently served as a powerful reminder of the fiscal challenges that now await many economies. Both the discretionary fiscal packages and the fiscal implications of economic downturn have proved hugely costly. But the ultimate bill facing taxpayers will remain unknown for years to come due to the government guarantees that have been extended to the various corners of financial markets. Given the looming demographic challenges, the current financial crisis and the 'lost' output (and therefore tax revenues) it implies have proved exceptionally poorly timed. Indeed, persistently higher government borrowing and a skyward trajectory of debt-to-GDP ratios could yet prove the most visible consequences of the credit bust and economic collapse of the past 18 months. Should the perception of the public finances deteriorate sufficiently, fiscal policy itself may lose some of its current efficacy, requiring ever greater government interventions to produce the desired objective and, presumably, ever larger economic distortions.

Navigating future challenges

The present and anticipated outperformance of China appears to be providing a substantial bid to commodity prices, given that the economy's more intensive (and likely rising) commodity demand per unit of GDP growth. For most economies, the influence of energy costs upon inflation is expected to move from the recently substantial negative to a positive by the final quarter of the year. But given the economic current fragility, the risks associated with rising oil prices appear much more acute with regard to growth rather than inflation, particularly within the Eurozone. Moreover, with substantial spare capacity having developed across the major economies and unemployment approaching multi-year highs, the current cyclical position appears far from conducive to the development of underlying inflationary pressures. As a result, our 2010 global inflation forecast has increased only marginally to 1.8% from 1.6% previously.

Such disinflationary forces are expected to hamper the relative performance of developed market equities, and we remain underweight as result, with credit continuing as our preferred asset class. But with the recent (and in our opinion misplaced) concerns over an imminent reversal of monetary policy having provided the opportunity, we have shifted some exposure into long-dated Treasuries, gilts and core European bonds, which we expect to benefit from a growing realisation of the substantial obstacles that exist between the current turnaround in sentiment and the formation of a strong, sustained economic recovery.

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Contents

Key forecasts

Key forecasts

	GDP				Inflation			
	2007	2008	2009f	2010f	2007	2008	2009f	2010f
World (nominal GDP weights)	**3.6**	**1.7**	**-2.3**	**2.2**	**2.8**	**4.3**	**0.9**	**1.8**
World (PPP weights)	**5.4**	**3.1**	**-0.8**	**3.3**	**3.7**	**5.4**	**1.6**	**2.4**
Developed	**2.4**	**0.7**	**-3.4**	**1.2**	**2.1**	**3.2**	**-0.1**	**0.9**
Emerging	**7.9**	**5.5**	**1.1**	**5.3**	**5.5**	**8.1**	**4.5**	**5.0**
North America	**2.1**	**1.1**	**-1.9**	**1.8**	**2.8**	**3.7**	**-0.5**	**0.9**
US	2.0	1.1	-1.9	1.9	2.9	3.8	-0.6	0.8
Canada	2.5	0.4	-2.5	1.1	2.1	2.4	0.4	1.7
Latin America	**5.0**	**3.3**	**-3.1**	**3.2**	**5.7**	**8.1**	**5.7**	**6.1**
Mexico	3.6	1.3	-5.9	2.6	3.8	6.5	4.1	3.6
Brazil	5.7	5.1	-0.3	4.1	4.5	5.9	4.4	4.8
Argentina	8.7	5.5	-2.2	2.9	17.6	21.1	16.5	18.0
Chile	4.7	3.2	-1.1	2.5	7.8	7.1	0.1	3.0
Western Europe	**2.7**	**0.7**	**-4.1**	**0.4**	**2.1**	**3.3**	**0.7**	**1.4**
Euro-15	**2.6**	**0.6**	**-4.3**	**0.1**	**2.1**	**3.3**	**0.5**	**1.3**
Germany	2.6	1.0	-5.9	0.5	2.3	2.7	0.3	0.8
France	2.3	0.3	-2.8	-0.4	1.6	3.2	0.2	1.5
Italy	1.5	-1.0	-5.3	-0.4	2.0	3.5	1.1	1.9
Spain	3.7	1.2	-3.2	-0.1	2.8	4.1	-0.6	1.3
Other Western Europe	**2.9**	**0.9**	**-3.2**	**1.3**	**2.0**	**3.4**	**1.4**	**1.8**
UK	3.0	0.7	-3.8	1.6	2.3	3.6	1.8	2.1
Norway	3.2	2.1	-1.1	0.8	0.7	3.8	2.0	1.6
Sweden	2.7	-0.4	-4.5	1.0	2.2	3.5	-0.1	1.1
Switzerland	3.3	1.6	-2.1	0.2	0.7	2.4	-0.6	0.6
EMEA	**5.8**	**4.1**	**-3.4**	**2.5**	**7.3**	**10.9**	**8.0**	**7.3**
Czech Republic	5.8	3.1	-2.1	1.5	2.8	6.4	1.6	1.8
Hungary	1.2	0.6	-5.9	-0.6	8.0	6.1	4.7	4.0
Poland	6.7	4.8	0.6	1.2	2.5	4.2	3.7	2.6
Russia	8.1	5.6	-7.9	2.5	9.0	14.1	11.6	11.5
Turkey	4.7	1.1	-4.4	2.0	8.8	10.4	6.6	9.1
Ukraine	7.9	2.1	-18.0	5.5	12.8	25.2	17.0	9.0
Egypt*	7.1	7.2	4.3	4.1	11.1	11.7	16.5	9.7
Israel	5.3	4.0	-0.6	2.9	3.4	3.8	2.5	1.5
Saudi Arabia	3.4	4.3	-0.1	3.9	4.1	9.9	5.4	4.0
UAE	5.2	7.0	-1.2	4.3	11.1	13.5	4.5	4.0
South Africa	5.1	3.1	-0.9	2.0	7.1	11.5	7.3	5.9
Asia-Pacific	**6.0**	**3.1**	**-0.5**	**4.4**	**2.2**	**4.1**	**0.5**	**1.2**
Japan	2.4	-0.7	-6.3	1.2	0.0	1.5	-1.4	-1.1
Australia	4.0	2.3	0.2	2.6	2.3	4.3	2.0	2.8
New Zealand	3.1	-1.0	-0.3	2.3	2.4	3.9	1.8	2.4
Asia ex Japan	**9.8**	**6.7**	**4.3**	**6.9**	**4.4**	**6.7**	**2.0**	**3.1**
China	13.0	9.0	7.8	8.5	4.8	5.9	-0.6	0.8
Asia ex Japan & China	**6.9**	**4.6**	**0.9**	**5.3**	**4.1**	**7.3**	**4.0**	**4.8**
Hong Kong	6.4	2.5	-4.5	2.4	2.1	4.3	0.9	1.4
India	9.3	7.5	6.0	7.5	6.4	8.3	7.0	5.8
Indonesia	6.3	6.1	3.8	5.3	5.8	10.2	5.7	8.3
Malaysia	6.2	4.6	-3.8	6.3	2.0	5.4	0.4	3.2
Philippines	7.1	3.8	1.0	3.0	2.8	9.3	3.5	4.8
Singapore	7.8	1.1	-6.0	5.3	2.1	6.5	-0.3	2.3
South Korea	5.1	2.2	-2.3	3.6	2.5	4.7	2.7	3.2
Taiwan	5.7	0.1	-5.1	4.4	1.8	3.5	-0.7	1.2
Thailand	4.9	2.6	-3.5	3.5	2.2	5.5	-1.4	2.7
Vietnam	8.5	6.2	4.5	6.5	8.3	23.0	7.5	10.1

Notes: Calendar year; except for * which is based upon Egyptian fiscal year (July-June); Global and regional aggregates are calculated using chain nominal GDP (USD) weights
Source: HSBC

Monetary & fiscal policy assumptions

Monetary policy

	Q3 2008	Q4 2008	Q1 2009	Q2 2009	Q3 2009f	Q4 2009f	Q1 2010f	Q2 2010f
US								
Targeted Fed funds	2.00	0.00 to 0.25	0.00 to 0.25	0.00 to 0.25	0.00 to 0.25	0.00 to 0.25	0.00 to 0.25	0.00 to 0.25
Japan								
Overnight call rate	0.50	0.10	0.10	0.10	0.10	0.10	0.10	0.10
Eurozone								
Repo rate	4.25	2.50	1.50	1.00	1.00	1.00	1.00	1.00
UK								
Bank rate	5.00	2.00	0.50	0.50	0.50	0.50	0.50	1.00
Canada								
Overnight rate	3.00	1.50	0.50	0.25	0.25	0.25	0.25	0.25

Source: HSBC

Fiscal policy

Country	2009	2010
US	We estimate a federal budget deficit of USD1.7 trillion for FY2009 (12% of GDP), which is USD125bn lower than the CBO's mid-June deficit estimate. With only three months left in the fiscal year, the CBO's allocation of USD125bn for additional financial stabilization efforts is increasingly unlikely to be needed in FY2009. Total outlays are still expected to rise to over 26% of GDP, up from 21% in FY2008. Major items include defense spending (4.9% of GDP), Social Security (4.8%), and non-defense discretionary outlays (4.2%).	We assume a FY2010 federal budget deficit of USD1.3trillion, or around 9% of GDP. Non-defense discretionary outlays could rise even further, to nearly 5% of GDP, as additional expenditures related to the 2009 fiscal stimulus package are initiated.
Japan	We estimate that the government's fiscal stimulus package, announced on April 10th, will boost GDP by 1.1%. In FY2009 alone, the package will probably increase GDP by 0.8%. The front-loading of government investment will probably begin in the April-June quarter, and will be concentrated in the second half of this year.	In its initial budget for FY2010, which will be debated later this year, the Japanese government will probably include measures to prevent sharp declines in personal consumption and public investment, and a relapse of the economy, after the record-levels of stimulus provided in FY2009.
Eurozone	Given the recession across the Eurozone, the automatic stabilisers are adding to government spending as will the ongoing costs of dealing with the financial crisis and the sizeable stimulus packages in France and Germany in particular. We expect the budget deficit in the Eurozone to widen to nearly 6% of GDP in 2009 with virtually every economy within it exceeding the 3% Maastricht limit.	A further discretionary fiscal stimulus will be delivered (smaller than the roughly 1% boost in 2009) and the ongoing rise in unemployment implies higher spending on benefits. However, the stabilisation in the economy should limit the deterioration in the deficit in 2010, which is nonetheless expected to widen to about 6.5% of GDP.
Germany	The fiscal measures planned for 2009 and 2010 were announced in autumn 2008. The second fiscal package (approved in February 2009), together with the paying back of the commuter tax relief, comprise around EUR45bn each year. Recently the government increased fiscal stimuli for 2009 by a further EUR5bn	Health and nursing social insurance contributions are now tax deductible following the Supreme Court's decision, generating a tax relief of around EUR9bn. Overall, the deficit should move from 4.6% of GDP in 2009 to 6.1% in 2010.
France	Additional public spending, the decline in GDP and automatic stabilisers push up our public deficit forecast to 7.1% of GDP in 2009. Following the decision of INSEE and Eurostat, the sums generated by the Société de Financement de l'Economie Française to grant loans to banks and raise capital in the markets with a government guarantee will now add to the public debt.	The rising unemployment rate and weaker profile of GDP are expected to lead to the deficit widening to 7.8% of GDP in 2010. We forecast public debt at 82.7% of GDP, in the absence of any further bank recapitalisations or refinancing.
Italy	Italy's high debt burden (about 106% of GDP in 2008) precludes a meaningful stimulus. A EUR 80bn package, which involves higher infrastructure spending, was announced but much of the money is slated for bank recapitalisations. Nonetheless, we expect the sharp contraction in GDP to widen the deficit to 5.8% of GDP.	Even in the absence of a fiscal stimulus the deficit will widen further and the government debt-to-GDP ratio appears set to rise to 119%.
UK	With public sector borrowing having already risen rapidly, the Chancellor has limited the proposed fiscal measures to a stimulus equivalent to around 1% of GDP. We think it more likely that public sector borrowing rises to over 13% of GDP in 2009.	Without a fiscal stimulus package we expect public sector borrowing of more than 12% of GDP. Net debt looks set to rise towards 85% of GDP in 2012 and this is assuming that the contingent liabilities such as government-guaranteed ABS do not incur any actual cost.
Canada	There is some concern that the stimulus package will be slow to get off the ground given the emphasis on infrastructure spending, which tends to suggest that the bulk of the stimulus package will land in 2010 rather than 2009.	

Source: HSBC

And now for the hard part…

- Policymakers may have averted a prolonged spell in the financial wilderness…
- …but the progress seen so far could yet prove to be the easiest part of the recovery…
- …with the developed world at risk of disappointing in 2010 and beyond.

An unlikely tale

It's often said that it's better to travel than arrive, and financial markets have certainly experienced a remarkable, often incredible journey over the past twelve months. A script of financial implosion, industrial collapse and then apparent recovery within such a short time frame would typically be dismissed as overly far-fetched. Yet such a synopsis barely does justice to the events of the past year.

Models of finance that were once accepted without question have been declared bankrupt, while the pre-eminent position of market-based systems has faced a level of scrutiny not seen for several decades. As the worst of the crisis gripped, a 'needs must' was adopted by policymakers, leading to a blurring of the traditional distinctions between private and public sectors, as well as the introduction of new and radical measures that would have seemed almost inconceivable only several months earlier.

So far at least, the results of the policymakers' endeavours appear encouraging. Although the longevity of the rally in equity markets and riskier assets more generally is open to conjecture, a recovery has nevertheless emerged. Credit conditions have similarly (and as a consequence) improved, while measures of both business and consumer confidence – although still at a level more consistent with stagnation than growth – have bounced from exceptionally low levels. Given the gravity of the situation presented to policymakers last autumn, such positives should not be downplayed. The more excitable may talk of Armageddon having been averted, but a prolonged spell in the financial wilderness certainly threatened last year. At the very least, the so-called 'negative feedback loop' - where deteriorating financial conditions and economic weakness threatened to feed upon each other with gathering ferocity – now appears to have been stemmed.

Stuart Green
Economist
HSBC Bank plc
+44 207 9971 6718
stuart1.green@hsbcib.com

Janet Henry
Economist
HSBC Bank plc
+44 207 9971 6711
janet.henry@hsbcib.com

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Out of the loop, but not out of the woods

Yet despite all such developments, we believe that the most formidable challenges lie ahead, and that the more fundamental questions are yet to be addressed. While the worst outcome may have been averted, it's not certain that a solid recovery will emerge or, when abstracting from the cycle entirely, what economic underpinnings remain.

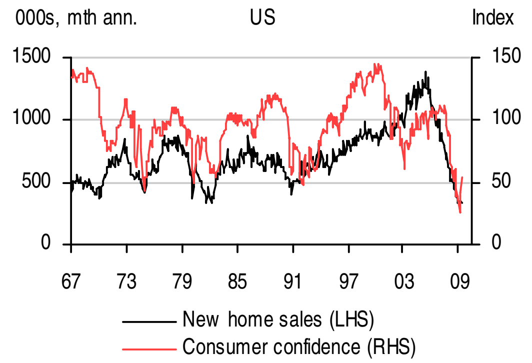
Such doubts will of course surround any fledgling recovery, but they seem especially relevant to the current juncture. Indeed, following the earlier, catastrophic collapse in economic activity, the recovery seen to date could well prove to be the 'easiest' phase of any upturn, with progress likely to become more uncertain as we head into 2010. Credit conditions, although improved, are still far worse than what could be considered as 'normal', while the readjustment of balance sheets in some household sectors may only be in its infancy. Plummeting rates of capacity utilisation point to a need for ongoing and undoubtedly painful structural adjustment within the major economies, aggravating the current rise in unemployment. The rising fiscal burden and eventual reversal of unconventional policies, meanwhile, will be issues that beguile for years to come, and a wave of more impinging regulation is presumably in store for financial markets. After the rollercoaster journey of the past two years, therefore, what lies in wait over the economic horizon is still a source of major anxiety.

An uneasy truce

Given the extent to which output collapsed around the turn of the year, and the subsequent scope for recovery, an improving cyclical picture and ongoing structural concerns could easily coexist during the summer and autumn months. Having fallen by more than 35 per cent over the year to February, Japanese industrial production could well post a number of significant monthly gains in output – similar to the 5.9% increases seen in April and May – before the recovery appears sustained or even meaningful. Indeed, the profile of industrial production in many countries is still more closely following a path of recession, even depression, than recovery. Business confidence could similarly improve through to the autumn, while still remaining well below the levels one would normally expect to see during the emergence from such a deep recession.

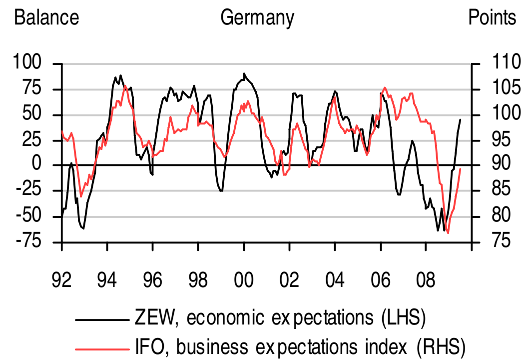
Charts 1 and 2 simply illustrate the recent path of a number of the more closely watched cyclical indicators – US new home sales, US consumer confidence, the German IFO and ZEW surveys – highlighting the fact that although a recovery has developed in recent months, the current level is still far below the long-term average. The ZEW

1. US consumer confidence still very depressed



Source: Thomson Financial Datastream

2. ZEW survey bucking the trend



Source: Thomson Financial Datastream

survey is the one indicator to buck this trend, but its currently positive level arguably relates more to the stabilisation of financial markets from unprecedented levels of stress than the immediate economic prospects.

Pluses and minuses

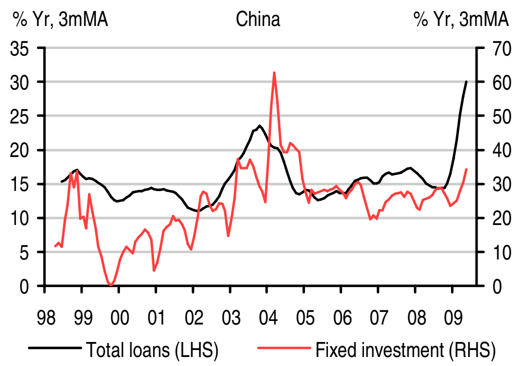
In essence, the sustainability or otherwise of the recent improvement in activity and risk appetite will not be quickly proved or disproved. But it is still instructive to detail both the major sources of optimism at present, alongside the more structural, underlying difficulties that could yet combine to derail the current recovery.

In particular, the more optimistic arguments at present are typically formed around two key, interrelated trends; namely the bounce back in a range of economic indicators, albeit from exceptionally weak levels, and an improvement in the broader financial landscape. A discussion of financial conditions is however interesting in that it encapsulates both elements of the short-term improvement/longer-term negatives argument, while the challenges posed by the risk of household de-leveraging and rising government indebtedness are of an altogether more negative slant.

A revival in the Middle Kingdom…

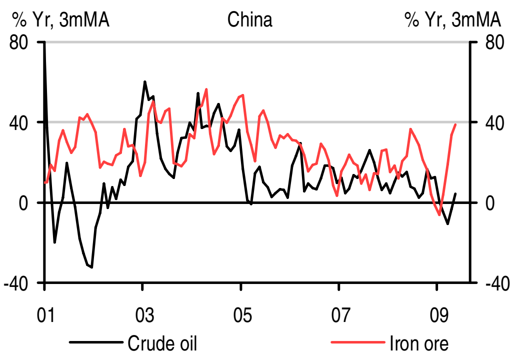
Among the hard data, probably the clearest signs of improvement to have emerged in recent months have come from China. Credit growth and fixed asset investment, in particular, have rebounded strongly (chart 3), bolstered by the RMB4trn fiscal stimulus. Such a strong rebound in lending (up 30% over the year to May) inevitably raises concerns about another round of non-performing loans a few years down the road, or whether this type of investment growth will support medium-term potential growth, especially given China's already very high investment-to-GDP ratio. However, such concerns appear less applicable to the current situation, given that much of this investment is in badly-needed infrastructure in the less-developed parts of China, and that many projects were already in the pipeline and have simply been brought forward. Moreover, low government debt and high domestic savings mean that the government is well placed to deliver such stimulus, and further large public sector projects appear likely if external demand fails to come through in any meaningful sense in the next year or two. Another year of 8%-plus GDP growth in 2010 would therefore be no surprise. But the potential benefit of a robust China to many parts of the rest of the world, such as the G7, is much less obvious.

3. Upsurge in China's credit growth



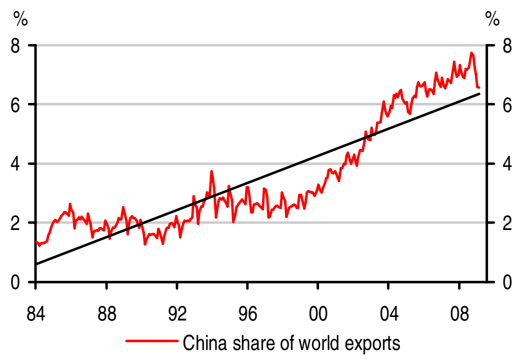
Source: CEIC

4. Import volumes of commodities rising again



Source: Thomson Financial Datastream, HSBC

5. China's share of world exports has grown rapidly...



Source: Thomson Financial Datastream, HSBC

…is boosting commodity imports…

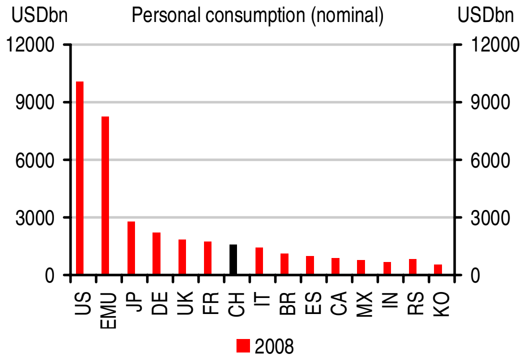
This question of the role played by China within Asia's trade cycle has assumed a much sharper focus of late given the combination of strong Chinese domestic demand and the collapse in global trade. At first glance, the sharp rebound in China's fixed investment (up 34% year-on-year in May) certainly sits oddly with the continued collapse in imports (down 25% over the same period), but the steep decline in import values is at least partly explained by commodity prices, which are still much lower than a year ago. China's import volumes of iron ore and oil are, in fact, among the few that have shown any significant revival recently and the ongoing infrastructure investment suggests this is set to continue, bringing obvious benefits to its main suppliers of these products: India, Russia, Australia, Brazil, South Africa and the Middle East. Other areas of high government spending such as energy conservation should also prompt greater imports of specialist machinery and equipment and new technology, providing some benefits to the likes of Japan, Germany and the US (see *Riding on China's recovery* by Qu Hongbin, 27 May 2009). But any support from China will likely prove only a modest positive when placed against the weakness of investment spending in the excess-capacity-ridden developed world.

…but with limited impact on world trade…

Beijing is also attempting to "crowd in" household spending by increasing social welfare spending on those areas people feel the greatest need to accumulate savings for, such as education and retirement. Over time, a more substantive social safety net should make households feel more confident about lowering their very high savings rate, allowing China to follow the growth model of other more developed Asian countries which have seen their savings rates decline over time. However, the impact over the next two years will, at best, be modest, particularly in terms of its impact on world trade growth.

An 8% growth rate is strong by international comparisons, but well below China's 10.7% average growth rate over the last six years. Besides, retail sales growth in China has remained fairly robust throughout the past year but has done little to offset the collapse in demand elsewhere. As chart 6 shows, China's total consumer spending in US dollar terms is still less than one sixth that of the US. As we have discussed in the past, China accounts for a much larger share (in percentage point terms) of global consumer spending growth than such figures alone suggest, due the relatively strong rate of expansion in China vis-à-vis the rest of the world. But it is not particularly import-intensive growth, as a much larger share of most Chinese households' spending is on basic items such as food and housing than in developed economies. To put the numbers in chart 6 into context: for every 1% point rise in the US household savings rate, China's consumer spending growth would have to accelerate by nearly 7% points to compensate.

6. ...but China's consumer spending cannot offset weak developed world

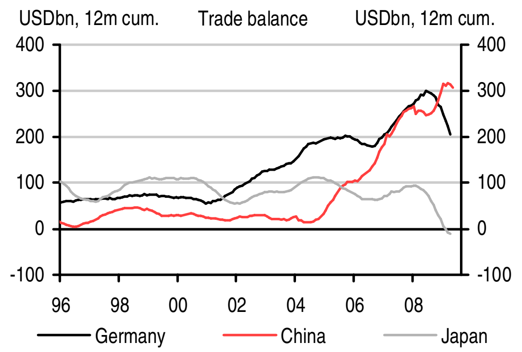


Source: Thomson Financial Datastream, HSBC

…or indeed global imbalances

A related point is that, despite its relative domestic demand out-performance, China is playing a smaller role in the removal of global trade imbalances than the other two countries in the world which have historically had the largest surpluses. Japan's trade surplus has recently turned to deficit, while Germany's has started to shrink (chart 7). China, in contrast has continued to grow its surplus. In the first five months of 2009 the surplus amounted to USD89bn, 15% more than in the same period of 2008, as the narrowing surpluses in trade with the US and Europe were more than offset by shrinking deficits with other Asian countries and Saudi Arabia.

7. No sign yet of China's trade surplus shrinking



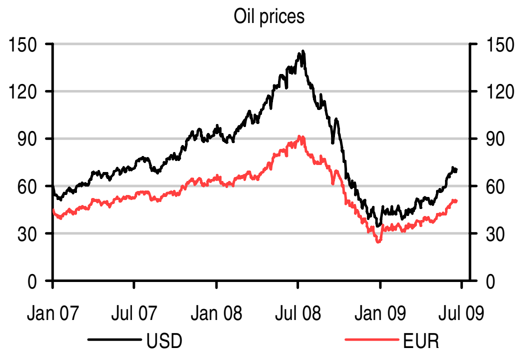
Source: Thomson Financial Datastream, HSBC

Fears of trade protectionism seem to have abated a little recently but, if this imbalance continues to grow, such fears could quickly return, especially given China's announcement in mid-June regarding the requirement that all companies being awarded these big stimulus projects must be located in China. Such moves should be seen as part of a tit-for-tat process that also includes the 'Buy America' movement and other examples of the artificial obstructions to trade that may be imposed, even if tariffs and quotas remain thankfully absent.

The rise in oil prices…

The revival in China's fixed investment growth may not yet be apparent in world trade growth, but certainly seems to be influencing global oil prices, given China's relatively intensive demand for commodities per unit of growth. Since the trough in late December, the oil price has doubled in both dollar and euro terms. It is hard to say how much of this is demand driven but, even if improving demand is the primary reason, such a rise in oil prices tends to be adverse for global growth as it implies a redistribution of income from oil consumers to oil producers which tend to have a lower propensity to consume. China's exporters will be a big beneficiary of the positive terms of trade effects felt by oil producers as will parts of the EU but the potential for a renewed squeeze on real incomes in many countries is clearly growing.

8. Doubling-up



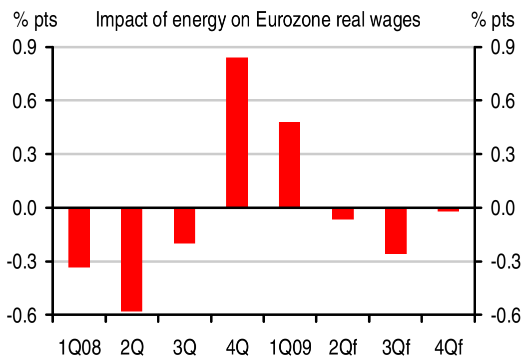
Source: Thomson Financial Datastream

…implies the end of the boost to real incomes…

In all of the major economies energy is detracting significantly from the annual change in consumer prices and will continue to do so over the next few months. But with oil prices having risen steadily since the start of the year, the consumer price index is drifting up again, suggesting the boost to quarterly real wages is now over. Indeed, assuming oil prices remain at current levels, energy will be detracting from the quarterly change in real wages as early as Q3 (chart 9).

Around the turn of the year we expect to see inflation in the US and Eurozone back above 1% while our economists in Asia are forecasting that inflation in Asia (ex Japan and China) could hit 6.5% by early or mid-2010 (see *Inflation Stations*, 18 June 2009). But for now the risks from rising oil prices still appear to be much more acute with regard to growth than to inflation, particularly in the Eurozone, where much of the recent resilience in consumer spending in Germany and France in particular is explained by the energy price drop. A further increase in oil prices at a time of rising unemployment would take its toll on consumer spending.

9. Income boost from lower energy costs is starting to wane



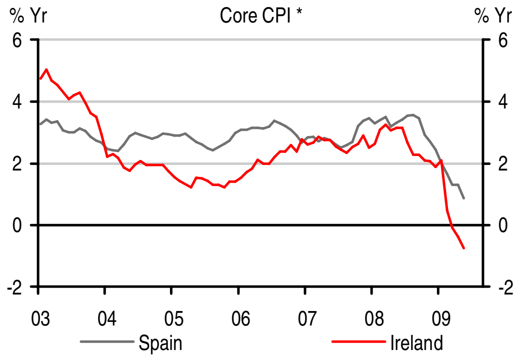
Source: HSBC calculations based on the inflation contributions from all of the energy components of HICP. A positive value denotes a period when energy is detracting from inflation (% point contribution to the q-o-q change) and therefore boosting real wages. Forecasts are based on stable oil prices of EUR49/barrel.

…but spare capacity makes it hard to generate inflation

Higher oil prices could also raise inflation expectations, as in H1 2008 when they rose to such a degree that it prompted the ECB to raise rates in July 2008. A repeat of this appears highly unlikely given the degree of slack in the economy and the much lower potential for a wage response. Wage growth in the US and UK has already slowed sharply and although nominal wage growth in the Eurozone has recently held up fairly well, this is primarily a consequence of the delayed labour market adjustment in the major economies which we expect to come through later this year. In Eurozone countries where employment and consumer spending have already fallen sharply – notably Spain and Ireland – so has core inflation (chart 10).

The same point applies to the developed world generally given that the unemployment rate is now higher than the peak during the early 1990s recession (chart 11). Looking at capacity more broadly, the global output gap, which we expect to exceed 4% of global GDP by the end of 2009, also suggests that the cyclical position of the global economy is not conducive to generating inflationary pressures (chart 12). Judging by their recent communications, this view is also shared by the major central banks, for whom the prospect of rising structural unemployment and a perhaps prolonged reallocation of resources across their respective economies will represent substantial analytical challenges.

10. Lack of inflation reflects economic weakness

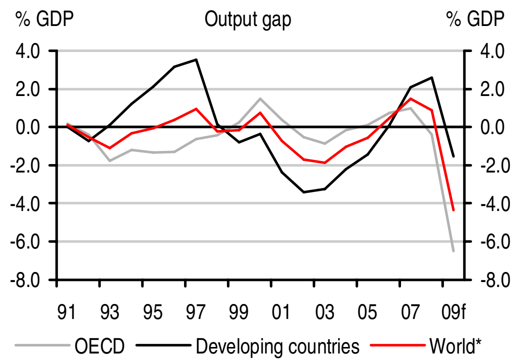


Source: Eurostat, HSBC
*Note: Core measure is CPI ex energy and seasonal food

11. Rising spare capacity in labour markets...

Source: Thomson Financial Datastream, HSBC

12. ...and the broad economy



Source: OECD, HSBC
Note: * world figures are using GDP weights

Woods and trees

The same is also true of the current trends within financial market conditions which, given the origins of the current crisis, have long been viewed as central to the prospects for a sustained economic recovery. Whereas many previous recessions may have been caused by an aggressive tightening of monetary policy, and eventually curtailed by a reversal of this trend, no such 'easy' signals would emerge this time around. Such realities, of course, have introduced more than a hint of circularity to the situation, with the prospects for economic growth, and by extension financial market sentiment, being perceived as dependent upon developments across financial markets.

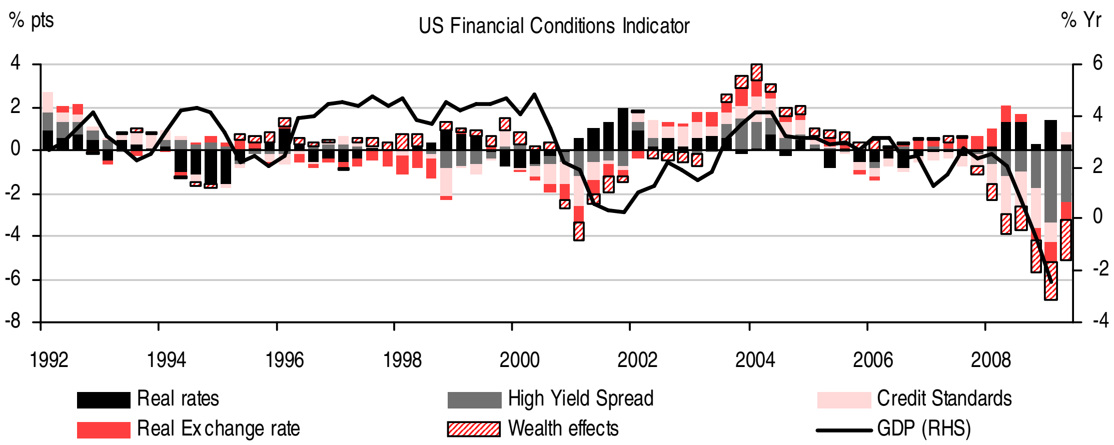
Fortunately, however, a number of indicators – whether relating to corporate bond spreads, LIBOR rates or implied default levels – have shown substantial, uncontroversial improvement in recent months. Perhaps most tellingly, demand for some of the liquidity measures that were hastily introduced by central banks over the past 18 months has fallen - considerably in some cases – suggesting that the sense of fear and suspicion that stalked markets around the turn of the year has indeed been dispelled.

Big improvement, small cheer

In many cases, however, market conditions are still at more distressed levels than those prevailing before the Lehman bankruptcy and emergency rate cuts of September/October last year, and very substantially worse than the incredibly benign conditions that existed back in mid-2007. Interest rate spreads at the riskier end of the credit spectrum may have almost halved from the peaks observed at the end of 2008, but they remain at a level almost double the average of the three years preceding the crisis. Other areas, such as the commercial paper market, have failed to register even such a qualified recovery. Overall, evidence of a restoration of financial market health remains patchy at best, blurring in turn the outlook for a solid, sustainable recovery in economic conditions to emerge.

All of this makes the task of economic forecasting more troublesome than usual at present, and perhaps explains in part the wide disparity of opinion over the sustainability or otherwise of the 'green shoots' that have emerged to date. But rather than make comparisons with recent history – where the pricing and availability of credit may have reflected either overly optimistic or pessimistic expectations – it may be more instructive to gauge how the current set of conditions would, over the course of an economic cycle, be expected to influence growth.

13. Credit and wealth destruction hitting US growth hard



Source: OECD, HSBC. Chart shows estimated impact of changes in real short and long-term interest rates, high yield corporate bond spreads, lending standards, the real exchange rate and wealth effects upon the annual rate of GDP growth.

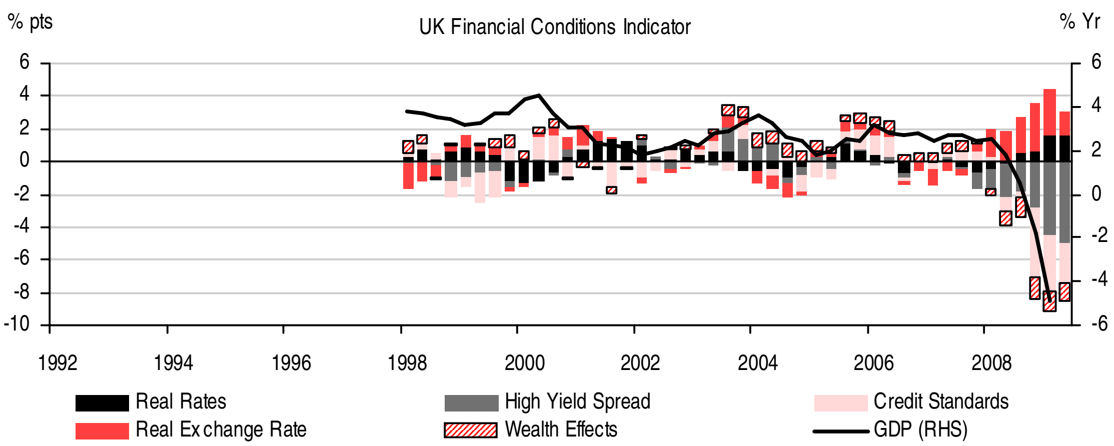
Recent history of little value

On the whole, broad measures of financial conditions – such as those recently developed by the OECD, which charts 13 and 14 are based upon for the US and UK respectively – are still much more consistent with economic contraction than expansion, even allowing for the recent, marked improvement in financial market trends.

The latest data for the second quarter indicate that the positive impact derived from the very low level of real interest rates in the US and the minor improvement in bank lending attitudes is being more than offset by the very negative combination of elevated credit spreads and wealth destruction. For the UK, meanwhile, the very pronounced decline in GDP appears to track the deterioration in financial conditions closely. Were it not for the positive influence generated by a record low level of interest rates and a very marked depreciation of sterling, this slump in activity would doubtless have proved even more alarming.

Although the volatile environment of late makes drawing precise conclusions impossible, and indeed very unwise, the broad evidence would

14. Without sterling's impact, the UK outlook would be far worse



Source: OECD, HSBC. Chart shows estimated impact of changes in real short and long-term interest rates, high yield corporate bond spreads, lending standards, the real exchange rate and wealth effects upon the annual rate of GDP growth.

tend to suggest that financial conditions are on an aggregate basis still a negative for growth. During the short-term, concerns will naturally focus on the ability to sustain the recent improvement in activity once the impetus provided by a stabilisation of the inventory cycle fades. But on a more medium to longer-term perspective, one of the more pressing tasks for both policymakers and investors appears to be determining what may constitute the new 'normal' in post-bubble conditions and, more fundamentally, how such assumptions will influence perceptions of trend growth within the major economies.

Reshaping the future, and the past

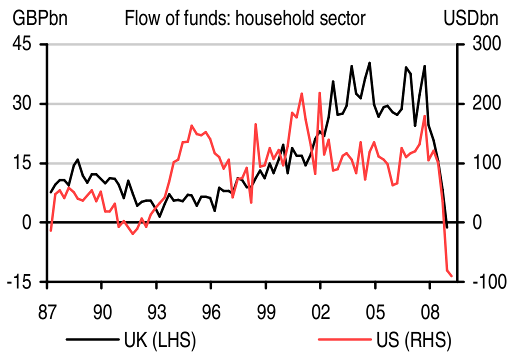
Financial crises have a nasty habit of not only lowering expectations of the scope for future growth, but also re-shaping the assessment of earlier growth and the factors that drove this. What appeared to be a modest and sustainable expansion at the time may eventually be deemed a credit-fuelled, asset-price-inflated boom that was always doomed to failure. Comparisons between the present day and 1990s Japan perhaps are now slightly commonplace, and the messages provided risk being overlooked as a result. But one of the more salutary points must be the manner in which estimates of the productive potential of the economy were successively downgraded as the expected recovery failed to emerge.

From a historical standpoint, estimates of trend or potential growth rates are typically extremely vulnerable during the current stage of the economic cycle, as each of the drivers of the earlier upturn – and their likely longevity - are subjected to ever greater scrutiny. Clearly, the prospect for a further rise in household sector indebtedness within the major economies now appears wholly dubious. This is due not only to the apparent willingness of individuals to pay down debt levels, but also because of the impaired ability of the financial system to facilitate further increases as securitisation markets remain subdued and a wave of more onerous regulation threatens.

Undoubtedly the key concern about the medium-term outlook is that large parts of the developed world will be weighed down by private and public sector debts, leaving the economy delivering a sub-par growth performance relative to past history until the level of indebtedness has been lowered to more sustainable rates. Again, these anxieties will not be quickly proved or disproved, and a wide range of opinions will as a result persist for some time yet. Those of a more optimistic slant will argue that the current levels of indebtedness need not prove unsustainable, and that new channels of demand can be created to help absorb the increased issuance of government debt. But even these benign scenarios will not be without consequence. The ability for household expenditure to grow in advance of income, for instance, would still be removed, while any artificial channelling of funds will necessarily remove them from elsewhere and impinge upon economic efficiency.

Recent balance sheet adjustment has been rapid…

15. Collapse in household credit has been exceptional



Source: Thomson Financial Datastream, HSBC

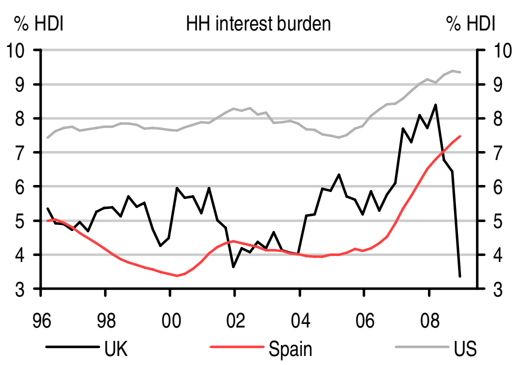
These key issues, therefore, cannot be ignored, particularly as the degree of adjustment in the US household sector over the past year has actually been fairly quick, with the savings rate having risen to 6.9%, back towards its average of the last 50 years. The UK household savings ratio has risen moderately, while even Spain has seen a marked turnaround in the household financial balance. The unusually rapid pace of this de-leveraging reflects three key factors:

1 The exceptional contraction in credit in late 2008 and early 2009. Flow of funds data for both the US and UK showed a net fall in new lending in Q4 for first time since these series began (see chart 15). Demand for credit will have played a role in this given the collapse in confidence post-Lehman which is borne out by the bank lending surveys. However, many households will have had no choice but to curtail their borrowing.

2 The dramatic reduction in interest rates has lowered the interest burden sharply, particularly in the UK (see chart 16), allowing households to pay down significant amounts of debt merely by keeping monthly payments unchanged.

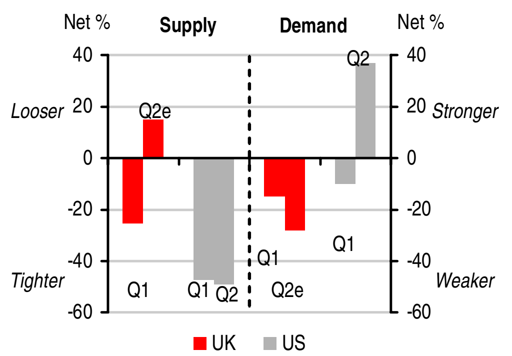
3 The boost to real incomes from the fall in oil prices meant households were able to pay down debt without curtailing spending too dramatically.

16. Interest burden has fallen sharply in UK



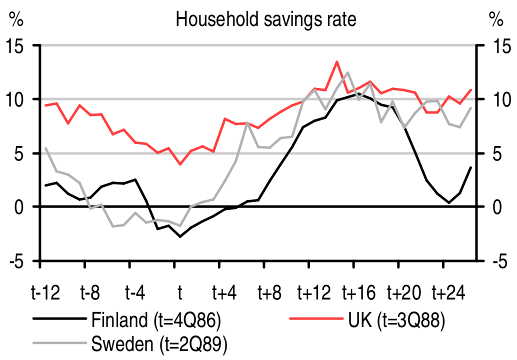
Note: Spain data are for 12-mth period up to current quarter while UK and US data are just for current quarter. Also variable rate mortgages in UK are re-set every month but usually only once a year in Spain. Source: Bank of Spain, ONS, Federal Reserve

17. The shifting patterns of supply and demand



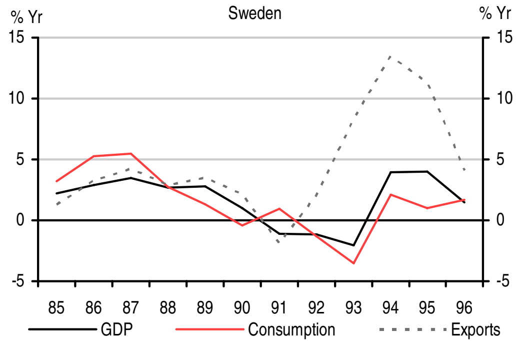
Source: BoE Credit conditions survey, US Bank Lending survey

18. Sweden's balance sheet adjustment took four years...



Source: Thomson Financial Datastream, HSBC

19. ...and consumer spending lagged the recovery in GDP



Source: Thomson Financial Datastream, HSBC

…but over-indebtedness is a constraint

These developments notwithstanding, household debt levels are still high. The key questions are: how far does the household debt-to-income ratio have to fall? Over what time period? And what does that mean for consumption and GDP growth while the adjustment is underway?

There are no clear answers to these questions as they depend in turn on;

Whether consumers choose to keep paying down debt: This could be in response to a number of factors, including: a debt level that is simply viewed to be too high relative to expected future income; a past or future fall in household wealth; high unemployment; concern over pensions; and the prospect of higher taxes in response to current burgeoning government deficits.

Whether a lack of availability of new credit means they are forced to: The recent early repayments of TARP money in the US notwithstanding, many banks are still rebuilding capital, shrinking balance sheets and likely to be exposed to increased regulation that will all curb credit availability. Even loans that are being extended tend to require more collateral, with lower loan-to-value ratios and income multiples on offer.

There is no set model for how de-leveraging proceeds. Each economy's experience of lowering its debt burden tends to have its own domestic characteristics. In the past three decades alone there have been several different ways in which the de-leveraging process has taken place in various countries and in all three of those discussed below the de-leveraging process continued well into the recovery.

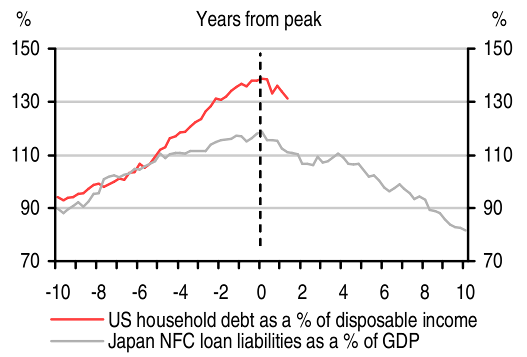
Sweden: "relatively" short and sharp

The most often-quoted example, and one on which we have written copiously ourselves, is Sweden. The household balance sheet adjustment there, as well as those in the UK and Finland, took at least four years, during which time, household savings rates rose by 9% points or more (chart 18). The Swedish example shows that even if households continue to pay down debt for a protracted period, this does not preclude a recovery in the economy. Sweden actually had a stronger average GDP growth rate in the first two years of the recovery (albeit after a three-year recession) than in the boom before the bust (chart 19). However, during the first few years of that recovery, consumer spending grew at less than half the rate registered during the boom. Instead, the driver of growth was exports, which makes the global reach of the current downturn a particular problem. It is notable that consumer spending growth did not start growing in line with overall GDP growth again until 1996 when the debt-to-income ratio started to rise again. This type of recovery is similar to that incorporated in our UK forecast, whereby a further gradual rise in the household savings rate implies consumer spending will expand at a more modest rate than for much of the past decade while the 20% or so fall in the exchange rate allows net exports to play a role in the recovery.

Japan: prolonged adjustment

A second example is that of Japan. Japan's reputation as a persistently high saver over the past decade or so does not refer to its households, whose savings rate has been in decline, but instead refers to the corporate sector, which has undergone a prolonged de-leveraging (chart 20). In a recent economic letter, the San Francisco Fed[1] compared the rapid rise in the indebtedness of Japan's non-financial corporate sector with that of America's household sector. After Japan's bubbles burst, private non-financial companies undertook a decade-long de-leveraging, reducing their collective debt-to-GDP ratio from 125% in 1991 to 95% in 2001. Firms massively reduced their spending on investment, shifting their financial balance from deficit to a large and growing surplus.

20. Japan's firms de-leveraged for a decade



Source: Thomson Financial Datastream, HSBC, FRBSF

There are clearly differences, which we have discussed in the past, but if US households were to undertake a similar de-leveraging, their debt-to-income ratio would need to drop to around 100% over the next 10 years. That would return it to the level that prevailed in 2002. The FRBSF estimates[2] that the household saving rate would need to rise to 10% by the end of 2018 and that a rise in the saving rate of this magnitude would subtract about three-quarters of a percentage point from annual consumption growth each year, relative to a baseline scenario in which the saving rate did not change.

Germany: ongoing de-leveraging

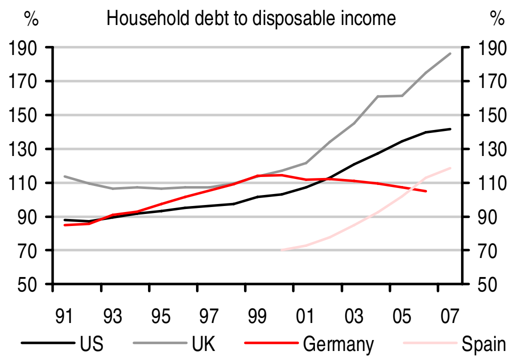
A less obvious example of de-leveraging than the two above is that of Germany. Given its reputation as a nation of thrifty consumers, some may be surprised to learn that as recently as 1999, German households had a higher debt-to-income ratio than either the US or the UK. Subsequently German households continually raised their savings rate, but the persistent squeeze on real wages throughout most of the past decade (as companies strived to restore the competitiveness lost by locking into the euro at an uncompetitive rate) has meant that the de-leveraging process has been quite protracted.

Clearly Germany did not have the option of a weaker exchange rate that Sweden and the UK benefited from in the early 1990s and today. Nor do debtors in Germany benefit from lower short rates to the same extent as in the UK or even US, as the bulk of mortgages are on fixed long-term rates. Instead Germany had a prolonged period of exceptionally weak nominal income growth (despite several rounds of tax cuts) which made it very difficult for households to lower their indebtedness ratio. During the six years to 2006 the ratio fell by less than 10 percentage points despite high savings and very weak consumer spending relative to the previous decade (chart 21).

1 FRBSF Economic Letter, Number 2009-16, 15 May 2009, http://www.frbsf.org/publications/economics/letter/2009/el2009-16.pdf

2 Assuming an effective interest rate on existing household debt of 7%, a future nominal growth rate of disposable income of 5% and that 80% of future saving is used for debt repayment

21. German households' debt burden remains high



Source: OECD

The German example may not represent a particularly useful model for future balance sheet adjustments in the US and UK, especially as Germany also had some unique structural issues which contributed to the high savings rate. But the similarities with Spain are clear. The decline in wage growth in Spain has lagged the fall in inflation but, as mentioned above, headline inflation is already negative and core inflation is slowing sharply. As in Ireland, wages will have to follow, which will make the reduction of the real debt burden a difficult and protracted adjustment.

A very visible challenge

While this particular adjustment will doubtless proceed slowly, the very volatile conditions across the government bond markets since the turn of the year have in contrast served as a powerful reminder of the longer-term fiscal challenges created by the almost ‘domino effect’ of financial crisis, economic weakness and the desire to reflate economies through substantial stimulus packages.

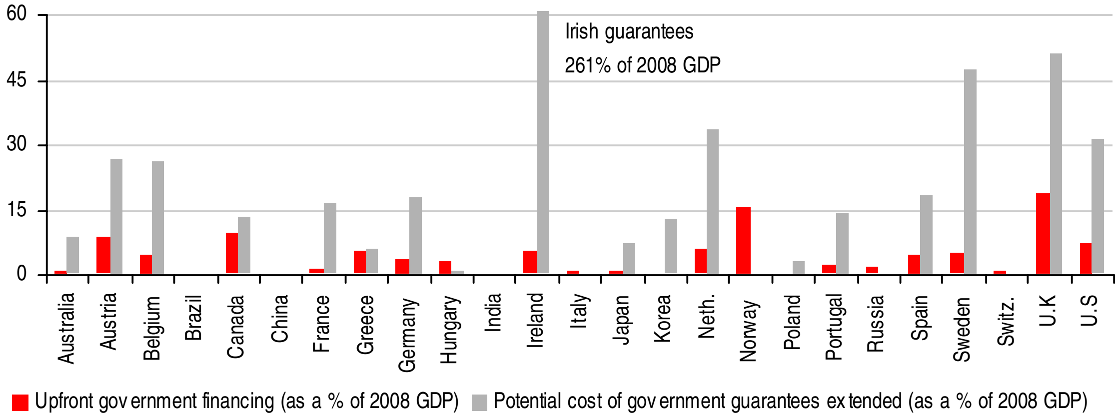
Across the major economies, the announced discretionary fiscal measures have averaged around 0.5 per cent of GDP in 2008, 2.0 per cent in 2009 and roughly 1.5 per cent in 2010, with a clear preference being demonstrated for such stimulus to be delivered through increased government expenditure rather than reduced taxation. But it is also important to highlight the role that non-discretionary expenditure has also played in the deterioration of the public finances, particularly within those countries (i.e. Germany, France and Japan) that employ a relatively high social safety net. The fiscal commitments produced by automatic stabilisers can often dominate the announced discretionary measures, even if the opposite is true with regard to attention levels. Meanwhile, for those countries with financial sectors that are disproportionately large in relation to GDP, such as the UK and US, the loss of corporate taxation over the coming years will also pose substantial challenges.

Assuming the burden…

Even allowing for the scale of such figures, however, it is arguably the implications of the government assistance extended to the various financial sectors that has caused the greatest alarm among investors. Whether the result of capital injections, the ring-fencing of the most doubtful areas of balance sheets or the guaranteeing of new capital issues, fiscal obligations have been extended to virtually every corner, often creating the impression that risk has merely been transferred from the private to public sector than diminished at all. Estimates of future government debt levels have, to put it bluntly, experienced something of a rout over the past 18 months, with the IMF now forecasting the 2014 debt-to-GDP ratio of the major economies to be some 36 percentage points higher than that registered in 2007. Even this looks rather conservative compared with the track record of previous financial crises across the developed and emerging world which, according to the recent work by economists Reinhart & Rogoff, typically led to government debt levels almost doubling in real terms[3]. And while no ‘optimum’ level exists for these debt-to-GDP ratios from a theoretical

3 See 'The Aftermath of Financial Crises', Carmen M. Reinhart & Kenneth S. Rogoff

22. Financial sector assistance - Money upfront and potential IOUs



Source: IMF, HSBC

standpoint, changes of this magnitude developing within a relatively short time are rarely well received by investors, or indeed rating agencies.

…whatever that entails

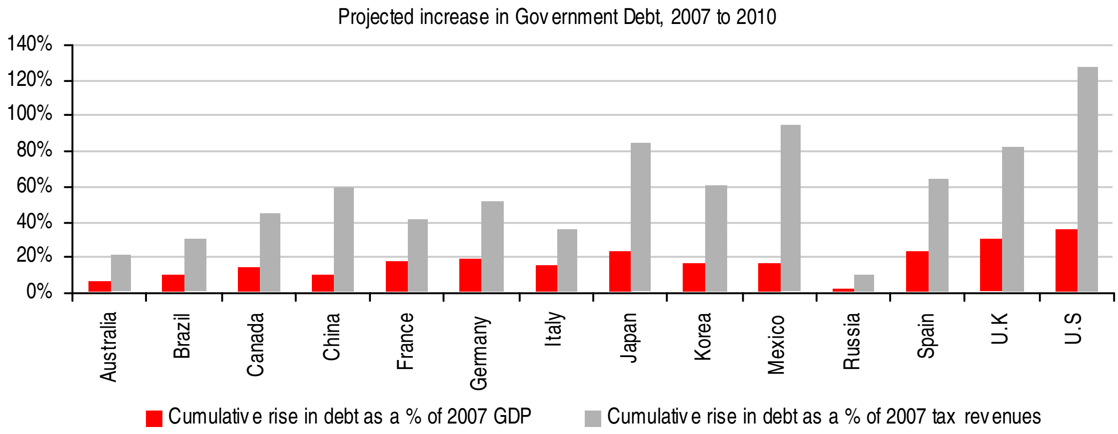
It is of course important to remember that government involvement within the financial sector will not automatically result in a rising fiscal burden. Had governments not stepped into the breach last autumn to counter the worst market failures, the resulting economic downturn and (due to the automatic stabilisers) ultimate fiscal cost could have been far worse than that we face today. Moreover, a further rehabilitation of market conditions could, on occasion, actually achieve positive returns for taxpayers. The purchase of equity or the provision of loans, for instance, should typically not influence the fiscal balance (the surplus or deficit on normal government operations), but only increase overall indebtedness, making the recovery rate on this outlay crucial to the ultimate impact upon public finances. A strong recovery would make the current level of scrutiny on the fiscal position seem overdone or, conversely, much worse news could yet emerge should the recent outlays ultimately turn into dead losses.

Money back not guaranteed!

Rather frustratingly, however, the experiences of the financial crises of the past two decades have been so mixed that no 'typical' recovery rate can be applied to the current situation. The Resolution Trust Corporation is believed to have recouped around 75 per cent of the roughly USD400bn spent on asset purchases at the start of the 1990s, while the Swedish authorities are commonly believed to achieved a recovery rate much closer to 100 per cent. But the evidence from elsewhere shows that during even periods as long as five to ten years, no significant amounts may be returned. Overall, given the vast scale of the contingent liabilities that have now been assumed, the exact cost of the various clean-up and ring-fencing operations – and the ability to finance such commitments given the concomitant declines in asset-related, corporate sector and personal taxation revenues – will remain worryingly uncertain for some time yet.

Such anxieties are neatly encapsulated by chart 22, using IMF data to show the initial outlay already committed by governments when providing assistance to the financial sector, and the overall size of the guarantees extended. If the public finances look bad now, much worse may

23. Projected increase in debt – size of tax base provides a new angle



Source: HSBC, IMF. Chart shows money values of projected increase in government debt as a % of 2007 GDP, and as a % of 2007 tax revenues

follow should governmental guarantees become binding. Furthermore, it is worth focussing upon the economic and financial conditions that would likely exist during such a period.

A question of supply and demand

A heightened level of financial uncertainty would presumably lead to an increased level of demand for government debt, allowing the increased issuance to be more easily absorbed for a period, while the likely imposition of heightened capital requirements upon commercial banks could yet generate substantive demand for government paper, possibly over a number of years. But from the opposite perspective, the very conditions that would lead to substantially higher government commitments related to the financial sector would also create a significant deterioration in the public finances, raising the degree of investor scrutiny still further.

Indeed, despite the current preoccupation with the potential cost of the assistance extended to the financial sector, it could yet prove to be the cyclical impact of recession, and the potentially permanent 'loss' of output (and therefore tax revenue) should economic recovery disappoint, that inflict the fiercest blow to the public finances.

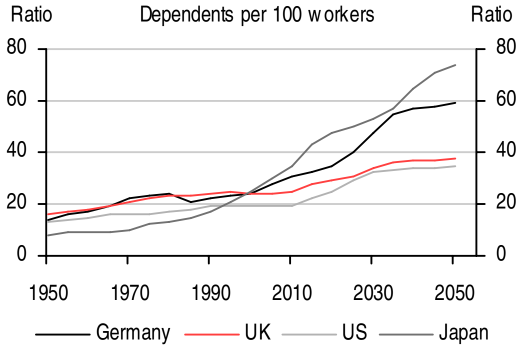
Again, the issue of trend growth becomes of crucial importance here, given its ability to rearrange the fiscal landscape, an issue covered at length in our recent research[4].

Overall, given both the upside and downside risks to the outlook, rising government debt levels and the need to signal a return to more sustainable fiscal positions are likely to remain front and centre of market attention for some time yet. The relative scale of such fiscal challenges is perhaps best illustrated by expressing the increase in government debt-to-GDP ratios that is expected to occur between 2007 and 2010 as a proportion of an economy's tax burden/revenues.

Although debt ratios are often seen as entirely comparable across countries, the differing structures of economies and the ease with which existing taxation/expenditure can be diverted towards the paying down of debt need to be acknowledged, creating the need for some 'normalisation' process to occur. On this basis, shown in Chart 23, what already appeared to be quite onerous projected increases in debt levels over the next few years become even more worrisome for countries with relatively low tax burdens, such as the United States, with the near

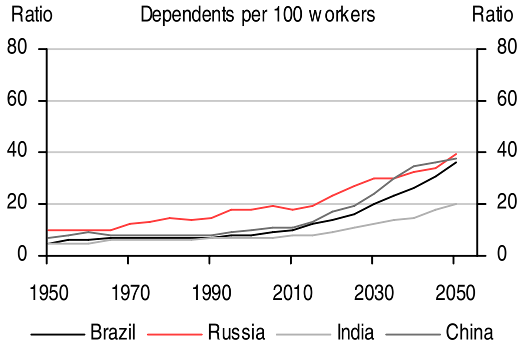
4 See 'And when the money runs out', by Stephen King,

24. Old-age dependency ratios about to head north...



Source: United Nations, HSBC

25...although the impact on the BRICs is more modest



Source: United Nations, HSBC

USD5trn increase in debt far surpassing the total tax revenue generated in 2007.

It's all in the timing

Financial crises are rarely well-timed, but from a fiscal perspective at least the timing of the current episode could yet prove particularly unfortunate, such are the additional demands upon the public finances that are likely to result from the process of demographic change over the next few decades. By its very nature, the issue of demographics will not preoccupy the thoughts of investors or policymakers on a day-to-day basis, but when overlaid to the events of the past two years, the topic increasingly demands attention.

Using the latest projections from the United Nations, chart 24 highlights the very marked increase in old-age dependency ratios (the ratio of the population of over 65s versus those of working age) that is expected to occur over the coming two decades for both the leading developed and emerging economies. Substantial differences are apparent between the major economies, with the expected increase in the US dependency ratio appearing almost insignificant next to that of Japan. The projections for the BRIC nations (see Chart 25), meanwhile, are more tightly clustered, although the demographic facing India appear to be the least demanding of the four.

The projected costs of this transition, detailed in table 26 using data from the OECD, are truly concerning and highlight the need for the major economies to achieve a sustained run of budget surpluses at a time when their ability to do so has been significantly impaired. However, outside of some externally imposed discipline, such as that displayed during the lead up to monetary union in Western Europe during the 1990s and across Eastern Europe more recently, the track record on fiscal austerity provides precious little reassurance.

26. A ticking time-bomb: increases in public spending on healthcare and pensions, 2005-2050

Country (% GDP)	Health	Long-term care	Pensions	Total
US	3.4	1.7	1.8	7.0
Japan	4.3	2.2	0.6	7.1
Germany	3.6	1.9	2.0	7.5
France	3.5	1.7	2.1	7.3
Italy	3.8	2.9	0.4	7.0
UK	3.6	1.9	1.7	7.2
Canada	4.1	2.1	1.7	7.9

Source: OECD Economic Outlook, Interim Report, March 2009-05-13

Persistently higher government borrowing and a skyward trajectory of debt-to-GDP ratios, therefore, could prove the most visible consequences of the credit bust and economic collapse of the past 18 months. As long as government bond yields remain below nominal GDP growth rates over the longer term – something which still appears more likely than not – this increased indebtedness is not clearly or technically unsustainable. But the dynamics around government finances will remain extremely troubling over the medium term.

Difficult decisions will need to be made with regard to expenditure and taxation, while new sources of demand for government paper will need to be cultivated. Governments may be presented with a very different set of incentives with regard to matters such as inflation and exchange rate stability than markets have become accustomed in recent decades, while what appear to be unconventional policy measures today could become all too familiar as the fiscal challenges mount. Indeed, should the perception of the public finances deteriorate sufficiently, fiscal policy itself may lose some of its current efficacy, requiring ever greater government interventions to produce the desired objective and, presumably, ever larger economic distortions.

Concluding themes

So far at least, the results of policymakers' traditional and unconventional measures appear encouraging. The improvement in financial conditions, revival in business and consumer confidence and the scale of the collapse in activity around the turn of the year all point to an improving cyclical picture during the rest of this year. But it remains far from certain that a solid recovery will emerge once the impetus provided by the stabilisation of the inventory cycle fades.

Over the medium term, we expect large parts of the developed world to be weighed down by private- and public-sector debts, leaving the economy delivering a sub-par growth performance relative to past history until the level of indebtedness has been lowered to more sustainable rates. True, the recent readjustment of balance sheets in some household sectors has been unusually rapid, but it still may only be in its infancy. The de-leveraging experiences of Sweden, Japan and Germany continued for anything from three years to more than a decade after the recession ended.

Lower trend growth will only add to the growing fiscal challenge. The cost of assistance extended to the financial sector has grabbed the headlines, but it seems likely that it will be the cyclical impact of recession, and the potentially permanent 'loss' of output (and therefore tax revenue) should economic recovery disappoint, that will inflict a more damaging blow to the public finances. Moreover the timing of the current episode could hardly be worse such are the additional demands upon the public finances that are likely to result from ageing populations over the next few decades.

Our global GDP forecast for 2009 has been lowered further, from -1.9% to -2.3%, with a slightly larger downgrade having come through in our forecasts for the emerging world rather than the developed. However, the clear out-performance of Asia is expected to continue. In 2010 we now expect global growth of 2.2% (previously 1.6%) with growth of 1.2% in the developed world and 5.3% in the emerging world. The only region that has not really participated in this upgrade is Europe, neither East nor West, partly reflecting the strength of the euro and our expectation of further euro appreciation ahead.

Our global inflation projection for 2009 remains unchanged at 0.8% and our 2010 forecast has edged up only slightly from 1.6% to 1.8% reflecting the recent rise in commodity prices.

As Richard Cookson argues in *Growing questions,* June 2009, a combination of lower-trend growth and ongoing disinflation implies somewhat lower nominal growth in the coming years which could hamper the performance of developed equities. Hence, we remain underweight. We remain overweight credit and have recently shifted more into long-dated Treasuries, gilts and core European bonds: a call supported by our view that US 10-year yields will head back below 3% in the first half of 2010.

Global economic forecasts

GDP

Annual

% Year	2001	2002	2003	2004	2005	2006	2007	2008	2009f	2010f
World (Nominal GDP weights)	**1.6**	**1.9**	**2.5**	**3.7**	**3.2**	**3.7**	**3.6**	**1.7**	**-2.3**	**2.2**
World (PPP weights)	2.4	3.0	3.9	5.0	4.7	5.3	5.4	3.1	-0.8	3.3
Developed	**1.2**	**1.3**	**1.8**	**2.9**	**2.3**	**2.7**	**2.4**	**0.7**	**-3.4**	**1.2**
Emerging	**3.2**	**4.5**	**5.7**	**7.0**	**6.8**	**7.6**	**7.9**	**5.5**	**1.1**	**5.3**
North America	**0.8**	**1.6**	**2.5**	**3.6**	**2.9**	**2.8**	**2.1**	**1.1**	**-2.0**	**1.8**
US	0.8	1.6	2.5	3.6	2.9	2.8	2.0	1.1	-1.9	1.9
Canada	1.8	2.9	1.9	3.1	3.0	2.9	2.5	0.4	-2.5	1.1
Latin America	**0.1**	**0.4**	**2.1**	**5.2**	**3.9**	**4.9**	**5.0**	**3.3**	**-3.1**	**3.2**
Mexico	-0.2	0.8	1.4	4.0	3.1	4.9	3.6	1.3	-5.9	2.6
Brazil	1.3	2.7	1.1	5.7	3.2	4.0	5.7	5.1	-0.3	4.1
Argentina	-4.4	-10.9	9.0	8.9	9.2	8.5	8.7	5.5	-2.2	2.9
Chile	3.5	2.2	3.9	6.0	5.6	4.6	4.7	3.2	-1.1	2.5
Western Europe	**1.9**	**1.1**	**1.1**	**2.1**	**1.8**	**2.9**	**2.7**	**0.7**	**-4.1**	**0.4**
Euro-15	**1.9**	**0.9**	**0.8**	**1.8**	**1.7**	**2.9**	**2.6**	**0.6**	**-4.3**	**0.1**
Germany	1.4	0.0	-0.2	0.7	0.9	3.2	2.6	1.0	-5.9	0.5
France	1.8	1.1	1.1	2.3	1.9	2.4	2.3	0.3	-2.8	-0.4
Italy	1.7	0.5	0.1	1.4	0.8	2.1	1.5	-1.0	-5.3	-0.4
Spain	3.6	2.7	3.1	3.3	3.6	3.9	3.7	1.2	-3.2	-0.1
Other Western Europe	**2.0**	**1.8**	**2.0**	**2.8**	**2.2**	**3.0**	**2.9**	**0.9**	**-3.2**	**1.3**
UK	2.5	2.1	2.8	2.8	2.1	2.8	3.0	0.7	-3.8	1.6
Norway	2.1	1.4	0.8	3.3	1.8	1.5	3.2	2.1	-1.1	0.8
Sweden	1.2	2.4	2.0	3.5	3.3	4.5	2.7	-0.4	-4.5	1.0
Switzerland	1.2	0.4	-0.2	2.5	2.5	3.4	3.3	1.6	-2.1	0.2
EMEA	**1.7**	**3.1**	**5.7**	**6.4**	**5.9**	**6.3**	**5.8**	**4.1**	**-3.4**	**2.5**
Czech Republic	2.5	1.9	3.6	4.6	6.5	6.4	5.8	3.1	-2.1	1.5
Hungary	4.1	4.4	4.3	4.7	3.9	4.0	1.2	0.6	-5.9	-0.6
Poland	1.2	1.4	3.9	5.3	3.6	6.2	6.7	4.8	0.6	1.2
Russia	5.1	4.7	7.3	7.2	6.4	7.7	8.1	5.6	-7.9	2.5
Turkey	-5.7	6.2	5.3	9.4	8.4	6.9	4.7	1.1	-4.4	2.0
Ukraine	9.2	5.2	9.6	12.1	2.6	7.1	7.9	2.1	-18.0	5.5
Egypt*	3.5	3.2	3.2	4.1	4.5	6.8	7.1	7.2	4.3	4.1
Israel	-0.4	-0.6	2.3	5.2	5.3	5.2	5.3	4.0	-0.6	2.9
Saudi Arabia	1.0	0.1	7.7	5.3	5.6	3.1	3.4	4.3	-0.1	3.9
UAE	3.5	2.6	11.9	7.4	10.5	9.4	5.2	7.0	-1.2	4.3
South Africa	2.7	3.7	3.1	4.9	5.0	5.3	5.1	3.1	-0.9	2.0
Asia/Pacific	**2.3**	**3.2**	**3.9**	**5.1**	**4.8**	**5.3**	**6.0**	**3.1**	**-0.5**	**4.4**
Japan	0.2	0.3	1.5	2.7	1.9	2.0	2.4	-0.7	-6.3	1.2
Australia	2.1	4.2	3.0	3.8	2.8	2.8	4.0	2.3	0.2	2.6
New Zealand	2.4	4.7	4.4	4.4	2.8	2.6	3.1	-1.0	-0.3	2.3
Asia-ex-Japan	**5.3**	**6.8**	**7.1**	**8.0**	**8.2**	**9.1**	**9.8**	**6.7**	**4.3**	**6.9**
China	8.3	9.1	10.0	10.1	10.4	11.6	13.0	9.0	7.8	8.5
Asia ex-Japan & China	**3.2**	**5.2**	**4.9**	**6.3**	**6.4**	**7.0**	**6.9**	**4.6**	**0.9**	**5.3**
Hong Kong	0.5	1.8	3.0	8.5	7.1	7.0	6.4	2.5	-4.5	2.4
India**	4.6	4.6	7.3	7.3	9.2	9.9	9.3	7.5	6.0	7.5
Indonesia	3.6	4.5	4.8	5.0	5.7	5.5	6.3	6.1	3.8	5.3
Malaysia	0.3	4.4	5.4	7.3	5.3	5.8	6.2	4.6	-3.8	6.3
Philippines	1.8	4.4	4.9	6.4	5.0	5.3	7.1	3.8	1.0	3.0
Singapore	-2.3	4.0	2.9	8.7	8.7	8.4	7.8	1.1	-6.0	5.3
South Korea	4.0	7.2	2.8	4.6	4.0	5.2	5.1	2.2	-2.3	3.6
Taiwan	-2.2	4.6	3.5	6.2	4.2	4.8	5.7	0.1	-5.1	4.4
Thailand	2.2	5.3	7.0	6.4	4.7	5.2	4.9	2.6	-3.5	3.5
Vietnam	6.9	7.1	7.3	7.8	8.4	8.2	8.5	6.2	4.5	6.5

Notes: * = based upon Egyptian fiscal year (July-June); ** = calendar year. We now calculate the weighting system using chain nominal GDP (USD) weights
Source: HSBC

HSBC

Quarterly

% Quarter & % Year		Q1 08f	Q2 08	Q3 08	Q4 08	Q1 09	Q2 09f	Q3 09f	Q4 09f	Q1 10f	Q2 10f
North America											
US*	*% Quarter*	0.9	2.8	-0.5	-6.3	-5.5	1.1	2.2	3.3	1.2	1.4
	% Year	2.5	2.1	0.7	-0.8	-2.5	-2.9	-2.3	0.1	1.9	2.0
Canada*	*% Quarter*	-0.7	0.3	0.4	-3.7	-5.4	-3.6	0.7	0.8	1.6	1.6
	% Year	1.7	0.7	0.3	-1.0	-2.1	-3.1	-3.0	-1.9	-0.1	1.2
Latin America											
Mexico	*% Quarter*	1.2	0.2	-0.6	-2.5	-5.9	-0.9	4.4	2.2	-1.2	0.1
	%Year	2.6	2.9	1.7	-1.6	-8.2	-9.9	-5.5	-0.2	5.0	5.5
Brazil	*% Quarter*	1.9	1.6	1.4	-3.7	-0.8	1.2	1.7	1.3	1.1	0.8
	% Year	6.1	6.2	6.8	1.3	-1.8	-3.8	-3.8	1.5	5.4	4.9
Argentina	*% Quarter*	0.8	2.3	1.5	-5.2	-2.3	0.8	3.2	2.3	-1.4	0.5
	% Year	8.5	7.8	6.9	-0.8	-3.8	-5.2	-3.7	3.9	4.9	4.6
Chile	*% Quarter*	1.6	1.5	-0.8	-2.0	-0.6	-0.5	2.0	3.0	-2.0	1.2
	% Year	3.4	4.6	4.6	0.2	-2.1	-4.6	-1.2	3.9	2.4	4.2
Western Europe											
Euro-15	*% Quarter*	0.7	-0.3	-0.4	-1.8	-2.5	-0.6	0.1	0.3	-0.2	0.0
	% Year	2.1	1.4	0.4	-1.7	-4.8	-5.1	-4.7	-2.7	-0.4	0.2
Germany	*% Quarter*	1.5	-0.5	-0.5	-2.2	-3.8	-0.3	0.2	0.3	0.0	0.2
	% Year	2.8	2.0	0.8	-1.8	-6.9	-6.8	-6.1	-3.7	0.1	0.7
France	*% Quarter*	0.4	-0.4	-0.2	-1.5	-1.2	-0.6	0.1	0.3	-0.5	-0.4
	% Year	1.9	1.0	0.1	-1.7	-3.2	-3.4	-3.1	-1.4	-0.7	-0.5
Italy	*% Quarter*	0.5	-0.6	-0.8	-2.1	-2.6	-0.8	-0.1	0.0	-0.2	0.1
	% Year	0.4	-0.3	-1.3	-3.0	-6.0	-6.2	-5.6	-3.6	-1.2	-0.3
Spain	*% Quarter*	0.4	0.1	-0.3	-1.0	-1.9	-0.7	-0.2	0.3	-0.5	0.1
	% Year	2.7	1.8	0.9	-0.7	-3.0	-3.8	-3.7	-2.4	-1.0	-0.2
Other Western Europe											
UK	*% Quarter*	0.8	-0.1	-0.7	-1.8	-2.4	-0.2	0.5	0.7	0.2	0.4
	% Year	2.5	1.8	0.5	-1.8	-4.9	-5.1	-3.9	-1.4	1.2	1.9
Norway	*% Year*	3.5	3.2	1.2	0.5	-0.3	-1.5	-1.0	-1.8	-1.3	0.5
Sweden	*% Year*	2.2	1.2	0.2	-5.1	-6.4	-6.0	-5.2	0.0	1.0	0.9
Switzerland	*% Year*	3.4	2.4	1.2	-0.4	-1.6	-2.6	-2.5	-1.9	-1.1	0.2
EMEA											
Czech Republic	*% Year*	5.3	4.6	4.7	0.7	-3.4	-2.8	-1.8	-0.5	0.5	1.0
Hungary	*% Year*	1.8	2.1	1.3	-2.5	-6.7	-6.4	-5.8	-4.3	-2.5	-1.0
Poland	*% Year*	6.0	5.8	4.8	2.9	1.4	1.3	1.6	1.9	2.3	2.5
Russia	*% Year*	8.7	7.5	6.0	1.2	-9.8	-10.6	-8.9	-2.8	2.6	2.8
Turkey	*% Year*	7.3	2.8	1.2	-6.2	-11.3	-7.3	-2.9	3.8	2.2	1.9
Ukraine	*% Year*	6.3	6.2	6.4	-8.0	-23.0	-22.7	-21.0	-8.0	8.0	7.0
Egypt**	*% Year*	7.3	6.8	5.8	4.1	4.3	2.8	3.5	4.1	4.0	4.9
Israel	*% Year*	4.3	2.8	4.6	-0.7	0.6	-2.0	-1.5	0.6	2.0	2.8
South Africa	*%Year*	1.6	5.0	0.2	-1.8	-1.3	-1.0	-0.6	-0.5	0.9	1.4
Asia/Pacific											
Japan	*% Quarter*	0.4	-0.6	-0.7	-3.6	-3.4	0.1	0.5	0.7	0.2	0.2
	% Year	1.3	0.6	-0.3	-4.3	-8.8	-7.8	-6.6	-2.5	1.5	1.7
Australia	*% Quarter*	0.8	0.3	0.2	-0.6	0.4	-0.3	0.2	0.6	0.8	0.9
	% Year	3.4	3.0	2.2	0.8	0.4	-0.3	-0.3	0.9	1.2	2.5
New Zealand	*% Year*	0.7	-0.9	-1.5	-2.3	-1.9	-1.0	0.2	1.4	1.8	2.3
Asia-ex-Japan											
China	*% Year*	10.6	10.1	9.0	6.8	6.1	7.2	8.4	8.5	9.0	8.7
Asia ex-Japan & China											
Hong Kong	*% Year*	7.3	4.1	1.5	-2.6	-7.8	-5.6	-5.4	0.6	2.2	2.3
India	*% Year*	8.6	7.8	7.7	5.8	5.8	5.6	5.7	6.8	6.7	7.4
Indonesia	*% Year*	6.2	6.4	6.4	5.2	4.4	3.2	3.4	4.1	4.4	5.8
Malaysia	*% Year*	7.4	6.6	4.8	0.1	-6.2	-5.6	-4.0	0.8	7.6	6.9
Philippines	*% Year*	3.9	4.2	4.6	2.9	0.4	1.1	1.8	0.8	0.9	3.9
Singapore	*% Year*	6.7	2.5	0.0	-4.2	-10.1	-7.5	-5.9	-0.1	5.4	5.4
South Korea	*% Year*	5.5	4.3	3.1	-3.4	-4.2	-4.2	-2.8	2.1	3.1	4.1
Taiwan	*% Year*	6.2	4.6	-1.0	-8.6	-10.2	-8.7	-4.5	3.5	5.5	4.6
Thailand	*% Year*	6.0	5.3	3.9	-4.2	-7.1	-4.8	-2.4	0.6	3.0	3.0
Vietnam	*% Year*	7.5	5.8	6.5	5.7	3.1	4.0	5.0	6.0	6.0	6.5

Note: * = quarter-on-quarter data has been annualised; ** = based up[on Egyptian fiscal year (July – June)
Source: HSBC

HSBC

Consumer prices

Annual

% Year	2001	2002	2003	2004	2005	2006	2007	2008	2009f	2010f
World	**2.5**	**2.1**	**2.2**	**2.5**	**2.7**	**2.7**	**2.8**	**4.3**	**0.9**	**1.8**
Developed	**2.0**	**1.4**	**1.8**	**1.9**	**2.3**	**2.3**	**2.1**	**3.2**	**-0.1**	**0.9**
Emerging	**4.7**	**5.1**	**4.2**	**4.8**	**4.4**	**4.4**	**5.5**	**8.1**	**4.5**	**5.0**
North America	**2.8**	**1.6**	**2.3**	**2.6**	**3.3**	**3.1**	**2.8**	**3.7**	**-0.5**	**0.9**
US	2.8	1.6	2.3	2.7	3.4	3.2	2.9	3.8	-0.6	0.8
Canada	2.5	2.2	2.7	1.9	2.2	2.0	2.1	2.4	0.4	1.7
Latin America	**4.9**	**10.7**	**5.7**	**6.0**	**5.1**	**4.2**	**5.7**	**8.1**	**5.7**	**6.1**
Mexico*	4.4	5.7	4.0	5.2	3.3	4.1	3.8	6.5	4.1	3.6
Brazil*	7.7	12.5	9.3	7.6	5.7	3.1	4.5	5.9	4.4	4.8
Argentina*	-1.5	41.0	3.7	6.1	12.3	9.8	17.6	21.1	16.5	18.0
Chile*	2.6	2.8	1.1	2.4	3.7	2.1	7.8	7.1	0.1	3.0
Western Europe	**2.2**	**2.1**	**2.0**	**1.9**	**2.1**	**2.1**	**2.1**	**3.3**	**0.7**	**1.4**
Euro-15	**2.4**	**2.3**	**2.1**	**2.2**	**2.2**	**2.2**	**2.1**	**3.3**	**0.5**	**1.3**
Germany	1.8	1.4	1.0	1.8	1.9	1.8	2.3	2.7	0.3	0.8
France	1.8	1.9	2.2	2.3	1.9	1.9	1.6	3.2	0.2	1.5
Italy	2.3	2.6	2.8	2.3	2.2	2.2	2.0	3.5	1.1	1.9
Spain	2.8	3.6	3.1	3.1	3.4	3.6	2.8	4.1	-0.6	1.3
Other Western Europe	**1.6**	**1.4**	**1.5**	**1.1**	**1.7**	**2.0**	**2.0**	**3.4**	**1.4**	**1.8**
UK	1.3	1.3	1.4	1.3	2.0	2.3	2.3	3.6	1.8	2.1
Norway	3.0	1.3	2.5	0.5	1.5	2.3	0.7	3.8	2.0	1.6
Sweden	2.4	2.2	1.9	0.4	0.5	1.4	2.2	3.5	-0.1	1.1
Switzerland	1.0	0.6	0.6	0.8	1.2	1.1	0.7	2.4	-0.6	0.6
EMEA	**10.4**	**9.8**	**7.4**	**6.2**	**6.6**	**6.0**	**7.3**	**10.9**	**8.0**	**7.3**
Czech Republic	4.7	1.8	0.7	2.5	1.9	2.6	2.8	6.4	1.6	1.8
Hungary	9.2	5.2	4.7	6.8	3.6	3.9	8.0	6.1	4.7	4.0
Poland	5.5	2.0	0.8	3.5	2.1	1.0	2.5	4.2	3.7	2.6
Russia*	21.6	15.8	13.7	10.9	12.7	9.7	9.0	14.1	11.6	11.5
Turkey	54.4	45.0	25.3	8.6	8.2	9.6	8.8	10.4	6.6	9.1
Ukraine*	12.0	0.8	5.2	9.0	10.3	9.1	12.8	25.2	17.0	9.0
Egypt**	2.4	2.4	3.2	14.3	8.9	4.2	11.1	11.7	16.5	9.7
Israel*	1.4	6.5	-1.9	1.2	2.4	-0.1	3.4	3.8	2.5	1.5
Saudi Arabia	-1.1	0.2	0.6	0.3	0.4	2.3	4.1	9.9	5.4	4.0
UAE	2.7	2.9	3.1	7.0	9.0	10.5	11.1	13.5	4.5	4.0
South Africa	5.7	9.7	5.4	1.4	3.5	4.6	7.1	11.5	7.3	5.9
Asia/Pacific	**0.9**	**0.3**	**1.0**	**1.8**	**1.4**	**2.0**	**2.2**	**4.1**	**0.5**	**1.2**
Japan	-0.8	-0.9	-0.2	0.0	-0.3	0.2	0.0	1.5	-1.4	-1.1
Australia	4.4	3.0	2.8	2.3	2.7	3.5	2.3	4.3	2.0	2.8
New Zealand	2.6	2.7	1.8	2.3	3.0	3.4	2.4	3.9	1.8	2.4
Asia-ex-Japan	**2.4**	**1.4**	**2.2**	**3.7**	**3.1**	**3.6**	**4.4**	**6.7**	**2.0**	**3.1**
China	0.7	-0.8	1.2	3.9	1.8	1.5	4.8	5.9	-0.6	0.8
Asia ex-Japan & China	**3.9**	**3.2**	**3.0**	**3.6**	**4.2**	**5.2**	**4.1**	**7.3**	**4.0**	**4.8**
Hong Kong	-1.6	-3.0	-2.6	-0.4	0.9	2.0	2.1	4.3	0.9	1.4
India	4.3	4.0	3.7	3.9	4.0	6.3	6.4	8.3	7.0	5.8
Indonesia	11.5	11.9	6.7	6.1	10.5	13.1	5.8	10.2	5.7	8.3
Malaysia	1.4	1.8	1.1	1.4	3.0	3.6	2.0	5.4	0.4	3.2
Philippines	6.8	2.9	3.5	6.0	7.7	6.3	2.8	9.3	3.5	4.8
Singapore	1.0	-0.4	0.5	1.7	0.5	1.0	2.1	6.5	-0.3	2.3
South Korea	4.1	2.8	3.5	3.6	2.8	2.2	2.5	4.7	2.7	3.2
Taiwan	0.0	-0.2	-0.3	1.6	2.3	0.6	1.8	3.5	-0.7	1.2
Thailand	1.6	0.7	1.8	2.8	4.5	4.6	2.2	5.5	-1.4	2.7
Vietnam	-0.3	4.1	3.1	7.8	8.3	7.5	8.3	23.0	7.5	10.1

Note: * = end-year values. We now calculate the weighting system using chain nominal GDP (USD) weights
Source: HSBC

HSBC

Quarterly

% Year	Q1 08	Q2 08	Q3 08	Q4 08	Q1 09	Q2 09	Q3 09f	Q4 09f	Q1 10f	Q2 10f
North America										
US	4.1	4.4	5.3	1.6	0.0	-1.0	-1.9	0.3	1.0	0.9
Canada	1.8	2.3	3.4	2.0	1.2	-0.3	-0.5	1.3	1.7	2.0
Latin America										
Mexico	3.9	4.9	5.5	6.2	6.2	6.0	5.3	4.5	4.2	3.7
Brazil	4.7	6.1	6.3	5.9	5.6	4.6	4.6	4.4	4.6	4.3
Argentina	22.7	27.1	25.2	21.1	17.9	16.1	16.3	16.5	17.2	17.5
Chile	8.0	8.9	9.3	8.6	5.0	2.5	1.0	0.1	1.5	2.1
Western Europe										
Euro-15	**3.4**	**3.6**	**3.8**	**2.3**	**1.0**	**0.2**	**-0.1**	**0.9**	**1.4**	**1.4**
Germany	3.1	3.0	3.3	1.6	0.8	0.1	-0.5	0.7	0.9	0.8
France	3.3	3.7	3.6	2.0	0.7	-0.2	-0.2	0.5	1.3	1.5
Italy	3.3	3.8	4.1	2.9	1.4	0.9	0.7	1.5	2.5	2.0
Spain	4.5	4.7	5.0	2.5	0.5	-0.9	-1.5	-0.5	0.5	1.3
Other Western Europe										
UK	2.4	3.3	4.9	3.9	3.0	2.0	1.0	1.2	2.5	2.1
Norway	3.5	3.2	4.7	3.6	2.4	2.4	1.5	1.8	1.6	1.7
Sweden	3.2	3.9	4.4	2.4	0.8	-0.5	-0.5	-0.3	1.0	1.0
Switzerland	2.5	2.7	3.0	1.6	0.0	-0.8	-1.1	-0.5	0.4	0.6
EMEA										
Czech Republic	7.4	6.8	6.6	4.7	2.2	1.5	1.1	1.4	1.4	1.5
Hungary	6.9	6.8	6.3	4.3	3.0	3.1	5.9	6.5	6.1	4.9
Poland	4.3	4.4	4.7	3.8	3.2	3.1	2.8	2.9	2.2	1.9
Russia	12.9	14.9	14.9	13.8	13.7	12.9	10.9	9.5	8.0	7.0
Turkey	9.2	10.6	11.1	10.1	7.9	6.0	6.5	7.4	9.1	9.8
Ukraine	22.5	30.2	25.8	22.6	20.4	16.3	15.0	13.6	10.3	9.0
Egypt	14.4	20.2	21.5	18.3	12.1	10.1	9.0	11.3	10.7	8.6
Israel	3.7	4.8	5.8	3.8	3.6	3.0	1.4	2.5	2.0	1.4
South Africa	9.9	11.6	13.4	11.2	8.4	8.0	6.6	6.3	6.3	5.7
Asia/Pacific										
Japan	1.0	1.4	2.4	1.0	-0.4	-1.3	-2.1	-2.0	-1.4	-1.1
Australia	4.2	4.5	5.0	3.7	2.5	2.0	1.5	2.0	2.5	2.8
New Zealand	3.4	4.0	5.1	3.4	3.0	1.8	0.8	1.7	2.1	2.5
China	8.0	7.8	5.3	2.5	-0.6	-1.1	-0.6	0.1	0.4	0.7
Hong Kong	4.6	5.7	4.6	2.3	1.7	0.2	-0.4	1.9	1.2	1.8
India	6.3	7.8	9.0	10.2	9.4	7.8	6.0	5.0	5.0	5.5
Indonesia	6.5	9.0	12.0	11.5	8.6	6.1	3.9	4.5	7.1	8.0
Malaysia	2.6	4.9	8.4	5.9	3.7	1.0	-3.0	0.1	2.7	3.5
Philippines	5.5	9.7	12.2	9.7	6.9	4.0	1.0	1.9	3.6	4.5
Singapore	6.6	7.5	6.6	5.4	2.1	-1.0	-1.2	-1.2	0.5	2.7
South Korea	3.8	4.8	5.5	4.5	3.9	2.7	1.7	2.6	3.2	3.6
Taiwan	3.6	4.2	4.5	1.9	0.0	-0.5	-0.9	-1.2	0.7	0.9
Thailand	5.0	7.5	7.3	2.1	-0.2	-3.2	-2.8	0.5	2.1	2.7
Vietnam	16.4	24.5	27.7	23.6	14.5	6.3	3.0	6.1	9.0	11.0

Source: HSBC

Short rates

3 month money

End period		2005	2006	2007		2008			2009			2010	
		Q4	Q4	Q4	Q2	Q3	Q4	Q1	Q2	Q3f	Q4f	Q1f	Q2f
North America													
	US (USD)	4.5	5.3	4.7	2.8	4.5	1.4	1.4	0.6	0.7	0.7	0.7	0.7
	Canada (CAD)	3.4	4.2	4.5	3.4	4.1	1.9	1.0	0.6	0.4	0.4	0.4	0.4
Latin America													
	Mexico (MXN)	8.0	7.2	7.3	7.6	8.3	8.2	7.0	4.6	4.5	4.5	4.9	5.5
	Brazil (BRL)	17.4	12.8	11.2	12.7	14.0	13.0	10.3	8.9	8.9	8.9	8.9	8.9
	Argentina (ARS)*	4.8	7.1	10.0	10.7	11.5	15.7	12.6	12.0	13.0	14.0	14.2	14.4
	Chile (CLP)*	4.5	5.3	6.5	7.9	8.5	8.3	2.3	1.6	1.6	1.3	1.6	1.9
Western Europe													
Euro-15		2.5	3.7	4.6	4.9	5.3	2.9	1.6	1.1	1.1	1.1	1.2	1.4
Other Western Europe													
	UK (GBP)	4.6	5.3	5.9	5.9	6.3	2.8	1.6	1.2	1.1	1.1	1.3	1.5
	Sweden (SEK)	2.0	3.3	4.7	5.0	5.5	2.5	1.1	1.0	0.9	0.9	0.9	1.1
	Switzerland (CHF)	1.0	2.1	2.6	2.8	3.0	0.6	0.6	0.3	0.3	0.3	0.3	0.5
	Norway (NOK)	2.6	3.9	5.9	6.6	7.7	4.0	3.0	2.0	2.0	2.0	2.0	2.0
EMEA													
	Hungary (HUF)	6.3	8.1	7.6	8.8	8.7	10.0	9.8	9.6	8.8	8.1	7.2	6.6
	Poland (PLN)	4.6	4.2	5.1	6.7	6.6	5.9	4.3	4.2	3.0	3.3	3.3	3.3
	Russia (RUB)*	5.9	5.9	6.3	5.4	8.3	20.6	14.5	10.5	9.0	8.5	8.0	8.0
	Turkey (TRY)	13.8	17.6	16.0	19.3	19.1	15.5	12.5	9.5	10.0	10.5	11.0	11.5
	Ukraine (UAH)	6.6	7.6	6.6	16.4	18.0	20.0	26.0	16.0	16.0	14.0	12.0	11.0
	South Africa (ZAR)	7.0	9.2	11.3	12.4	12.1	11.4	8.8	7.4	7.2	7.2	7.3	7.3
Asia/Pacific													
	Japan (JPY)	0.1	0.6	0.9	1.0	1.1	1.0	0.7	0.6	0.6	0.6	0.6	0.6
	Australia (AUD)	5.8	6.5	7.3	7.8	7.3	4.1	3.2	3.5	3.1	3.2	3.2	3.3
	New Zealand (NZD)	7.7	7.7	8.9	8.7	8.0	6.0	3.8	3.2	2.6	2.7	2.7	2.8
Asia-ex-Japan													
	China (CNY)	1.7	1.8	3.3	3.3	3.3	1.7	1.7	1.4	1.4	1.4	1.4	1.4
Asia ex-Japan & China													
	Hong Kong (HKD)	4.2	3.9	3.5	2.3	3.7	1.0	0.9	0.4	0.5	0.5	0.5	0.5
	India (INR)	6.3	8.2	8.0	9.4	11.0	8.5	8.5	4.3	6.1	6.3	6.3	6.5
	Indonesia (IDR)	12.8	9.5	7.8	9.2	9.9	12.0	8.6	7.5	7.0	6.9	6.8	6.7
	Malaysia (MYR)	3.2	3.7	3.6	3.7	3.7	3.4	2.1	2.0	2.0	2.0	2.0	2.0
	Philippines (PHP)	5.2	4.8	3.7	6.0	5.7	6.1	4.4	4.0	5.0	6.0	6.0	6.0
	Singapore (SGD)	3.3	3.4	2.4	1.3	1.9	1.0	0.7	0.6	0.6	0.7	0.8	0.9
	South Korea (KRW)	4.0	4.8	5.7	5.4	5.8	4.7	2.4	2.4	2.2	2.2	2.5	2.7
	Taiwan (TWD)	1.6	1.8	2.2	2.2	2.3	1.0	0.4	0.6	0.7	0.8	1.1	1.1
	Thailand (THB)	4.5	5.3	3.9	3.7	4.0	3.0	1.8	1.4	1.4	1.4	1.4	1.4

Note: * = 1-month money
Source: HSBC

Long rates

10-year bond yields

End period		Q4 05	Q4 06	Q4 07	Q2 08	Q3 08f	Q4 08f	Q1 09f	Q2 09f	Q3 09f	Q4 09f	Q1 10f	Q2 10f
Americas													
	US	4.4	4.7	4.0	4.0	3.8	2.3	2.7	3.5	3.3	3.0	2.5	2.5
	Canada	4.0	4.1	4.0	3.7	3.8	2.7	2.7	3.4	3.4	3.5	3.5	3.6
	Chile	5.3	5.4	6.3	7.8	7.3	5.3	5.0	4.0	3.8	3.8	4.6	5.3
Western Europe													
Euro-15		**3.3**	**4.0**	**4.4**	**4.8**	**4.4**	**3.5**	**3.6**	**3.7**	**3.9**	**3.8**	**3.2**	**3.2**
	Germany	3.3	3.9	4.3	4.6	4.0	2.9	3.0	3.4	3.6	3.5	2.9	2.9
	France	3.3	4.0	4.4	4.8	4.3	3.3	3.6	3.7	3.9	3.8	3.2	3.2
	Italy	3.5	4.2	4.6	5.1	4.9	4.4	4.4	4.4	4.3	4.2	3.6	3.6
	Spain	3.3	4.0	4.4	4.9	4.6	3.8	3.8	4.1	4.3	4.2	3.6	3.6
Other Western Europe													
	UK	4.1	4.7	4.5	5.1	4.4	3.1	3.2	3.7	3.5	3.5	3.2	3.2
	Sweden	3.3	3.8	4.3	4.5	3.8	2.4	3.0	3.5	3.5	3.5	3.4	3.4
	Switzerland	1.9	2.5	3.0	3.3	2.5	2.1	1.9	2.3	2.2	2.3	2.5	2.5
	Norway	3.6	4.3	4.7	5.1	4.4	3.8	3.8	4.1	3.9	3.9	3.9	3.9
EMEA													
	Hungary	7.0	6.7	7.2	8.5	8.2	8.2	12.0	9.8	9.8	9.0	8.0	7.5
	Poland	5.1	5.2	5.7	6.6	5.9	5.4	6.2	6.2	6.1	6.0	5.9	5.7
	Russia	6.8	6.5	6.3	6.7	7.8	11.3	14.3	10.1	10.6	11.1	10.1	9.1
	South Africa	7.5	7.7	8.4	10.7	8.8	7.3	8.6	9.0	9.3	9.5	9.5	9.5
Asia/Pacific													
	Japan	1.5	1.7	1.5	1.6	1.5	1.2	1.3	1.4	1.6	1.6	1.5	1.5
	Australia	5.2	5.9	6.3	6.5	5.4	4.0	4.4	5.5	5.4	5.1	4.8	4.8
	New Zealand	5.8	5.8	6.4	6.4	5.8	4.9	4.8	5.9	5.8	5.5	5.2	5.2
Asia-ex-Japan													
	Hong Kong	4.2	3.7	3.4	3.5	2.9	1.2	1.9	2.6	2.5	2.0	1.9	1.9
	India	7.1	7.6	7.8	8.7	8.7	5.3	7.0	7.0	6.2	6.4	6.7	7.0
	Indonesia*	13.3	9.4	9.2	13.2	13.0	11.8	11.7	11.1	9.0	9.3	9.3	9.3
	Philippines	10.2	6.4	6.4	9.2	8.1	7.3	7.8	8.1	9.3	9.3	9.3	9.3
	Singapore*	3.0	3.0	2.3	2.6	2.4	1.4	1.4	1.2	1.2	1.3	1.5	1.6
	South Korea*	5.0	4.8	5.6	5.4	5.8	4.3	4.7	4.8	4.3	4.5	4.5	4.5
	Vietnam*	8.8	8.3	8.7	19.7	15.9	10.0	9.2	9.6	8.5	8.5	8.5	8.5

Note: * = 5-year bond yield
Source: HSBC

Exchange rates vs USD

Exchange rates vs USD

End period		2005	2006	2007		2008			2009			2010	
		Q4	Q4	Q4	Q2	Q3	Q4	Q1	Q2	Q3f	Q4f	Q1f	Q2f
Americas													
	Canada (CAD)	1.17	1.16	0.99	1.01	1.06	1.23	1.26	1.16	1.15	1.20	1.20	1.20
	Mexico (MXN)	10.63	10.80	10.92	10.31	10.95	13.81	14.21	13.17	13.75	14.00	14.00	13.75
	Brazil (BRL)	2.34	2.14	1.77	1.59	1.91	2.34	2.31	1.95	2.05	2.10	2.15	2.20
	Argentina (ARS)	3.03	3.06	3.15	3.02	3.13	3.45	3.71	3.79	4.01	4.20	4.40	4.61
	Chile (CLP)	514	532	498	525	552	639	584	530	565	575	600	625
Western Europe													
	Eurozone (EUR=)	1.18	1.32	1.46	1.58	1.40	1.39	1.33	1.40	1.45	1.50	1.50	1.50
Other Western Europe													
	UK (GBP=)	1.72	1.96	1.99	1.99	1.78	1.44	1.43	1.65	1.60	1.61	1.61	1.61
	Sweden (SEK)	7.96	6.84	6.46	6.02	6.97	7.91	8.27	7.75	7.59	7.50	7.50	7.50
	Norway (NOK)	6.77	6.23	5.43	5.09	5.91	7.00	6.75	6.44	5.86	5.67	5.33	5.33
	Switzerland (CHF)	1.32	1.22	1.13	1.02	1.12	1.06	1.14	1.09	1.08	1.05	1.07	1.07
EMEA													
	Czech Republic (CZK)	24.6	20.9	18.2	15.2	17.4	19.3	20.7	18.5	18.6	17.3	17.0	16.7
	Hungary (HUF)	214.0	190.6	172.9	149.2	172.2	191.3	232.4	194.3	193.1	183.3	180.0	180.0
	Poland (PLN)	3.26	2.90	2.46	2.13	2.41	2.96	3.52	3.18	2.76	2.53	2.47	2.40
	Russia (RUB)	28.8	26.4	24.5	23.5	25.2	29.4	34.0	31.3	32.1	32.5	30.8	32.5
	Turkey (TRY)*	1.35	1.42	1.17	1.22	1.27	1.54	1.66	1.54	1.65	1.71	1.63	1.60
	Ukraine (UAH)	5.05	5.05	5.05	4.53	5.07	7.80	8.20	7.50	7.90	8.50	8.50	8.00
	Israel (ILS)	4.60	4.17	3.95	3.30	3.55	3.78	4.16	3.94	3.90	3.80	3.77	3.75
	South Africa (ZAR)	6.34	7.05	6.83	7.83	8.28	9.25	9.51	7.72	9.75	10.50	11.00	11.50
Asia/Pacific													
	Japan (JPY)	118	119	112	106	106	91	99	96	100	105	105	105
	Australia (AUD=)	0.73	0.79	0.88	0.96	0.79	0.70	0.69	0.81	0.77	0.80	0.82	0.82
	New Zealand (NZD=)	0.68	0.71	0.77	0.76	0.67	0.58	0.57	0.65	0.60	0.62	0.62	0.62
	China (CNY)	8.07	7.81	7.31	6.86	6.85	6.82	6.83	6.83	6.80	6.80	6.80	6.80
	Hong Kong (HKD)	7.75	7.77	7.80	7.80	7.77	7.75	7.75	7.75	7.80	7.80	7.80	7.80
	India (INR)	45.0	44.2	39.4	43.0	47.0	48.6	50.6	48.0	54.0	54.0	54.0	54.0
	Indonesia (IDR)	9825	8996	9393	9218	9469	11027	11550	10235	12000	12000	12000	12000
	Malaysia (MYR)	3.78	3.53	3.31	3.26	3.45	3.46	3.65	3.54	3.90	3.90	3.90	3.90
	Philippines (PHP)	53.0	49.1	41.3	44.8	47.2	47.5	48.3	48.2	52.0	53.0	53.0	53.0
	Singapore (SGD)	1.66	1.53	1.44	1.36	1.44	1.43	1.52	1.45	1.55	1.56	1.56	1.56
	South Korea (KRW)	1008	930	936	1048	1207	1263	1375	1283	1400	1200	1200	1200
	Taiwan (TWD)	32.8	32.6	32.4	30.4	32.1	32.9	33.9	32.8	34.0	33.0	32.5	31.5
	Thailand (THB)	41.0	36.0	33.7	33.5	34.0	34.9	35.5	34.0	35.5	37.0	38.0	39.0
	Vietnam (VND)	15896	16050	16217	16110	16800	16900	17776	17798	18050	18200	18200	18200

Note: Turkish currency (until then coded TRL) shed 6 zeros of its exchange rate in January 2005
Source: HSBC

Exchange rate vs EUR & GBP

Exchange rate vs EUR & GBP

End period		2005	2006	2007	2008			2009				2010	
		Q4	Q4	Q4	Q2	Q3	Q4	Q1	Q2	Q3f	Q4f	Q1f	Q2f
vs EUR													
Americas													
	US (USD)	1.18	1.32	1.46	1.58	1.40	1.39	1.33	1.40	1.45	1.50	1.50	1.50
	Canada (CAD)	1.38	1.53	1.44	1.60	1.49	1.72	1.67	1.63	1.67	1.80	1.80	1.80
Europe													
	UK (GBP)	0.69	0.67	0.73	0.79	0.79	0.97	0.93	0.85	0.91	0.93	0.93	0.93
	Sweden (SEK)	9.39	9.02	9.45	9.48	9.79	10.99	10.98	10.87	11.00	11.25	11.25	11.25
	Switzerland (CHF)	1.55	1.61	1.66	1.60	1.57	1.48	1.51	1.53	1.57	1.57	1.60	1.60
	Norway (NOK)	7.99	8.21	7.94	8.02	8.30	9.73	8.96	9.03	8.50	8.50	8.00	8.00
	Czech Republic (CZK)	29.0	27.5	26.6	23.9	24.5	26.8	27.4	26.0	27.0	26.0	25.5	25.0
	Hungary (HUF)	252	251	253	235	242	266	309	272	280	275	270	270
	Poland (PLN)	3.84	3.83	3.60	3.35	3.39	4.12	4.67	4.46	4.00	3.80	3.70	3.60
	Russia (RUB)	34.0	34.8	35.9	37.0	35.5	40.8	45.2	43.9	46.5	48.8	46.2	48.8
Asia/Pacific													
	Japan (JPY)	139	157	163	167	149	126	131	135	145	158	158	158
	Australia (AUD)	1.61	1.67	1.67	1.64	1.78	1.99	1.91	1.73	1.88	1.88	1.83	1.83
	New Zealand (NZD)	1.73	1.87	1.90	2.07	2.10	2.38	2.33	2.17	2.42	2.42	2.42	2.42
Africa													
	South Africa (ZAR)	7.48	9.30	9.99	12.33	11.63	12.85	12.63	10.83	14.14	15.75	16.50	17.25
vs GBP													
Americas													
	US (USD)	1.72	1.96	1.99	1.99	1.78	1.44	1.43	1.65	1.60	1.61	1.61	1.61
	Canada (CAD)	2.01	2.28	1.96	2.02	1.90	1.77	1.80	1.91	1.84	1.93	1.93	1.93
Europe													
	Eurozone (EUR)	0.69	0.67	0.73	0.79	0.79	0.97	0.93	0.85	0.91	0.93	0.93	0.93
	Sweden (SEK)	13.66	13.39	12.86	11.97	12.43	11.37	11.85	12.76	12.15	12.08	12.08	12.08
	Norway (NOK)	11.62	12.19	10.81	10.14	10.54	10.07	9.68	10.60	9.39	9.13	8.59	8.59
	Switzerland (CHF)	2.26	2.39	2.25	2.03	2.00	1.53	1.63	1.79	1.73	1.69	1.72	1.72
Asia/Pacific													
	Japan (JPY)	203	233	222	211	189	130	142	159	160	169	169	169
	Australia (AUD)	2.34	2.48	2.27	2.07	2.26	2.06	2.06	2.04	2.08	2.01	1.96	1.96
	New Zealand (NZD)	2.52	2.78	2.59	2.61	2.67	2.46	2.51	2.54	2.67	2.60	2.60	2.60
Africa													
	South Africa (ZAR)	10.89	13.80	13.60	15.58	14.76	13.29	13.63	12.72	15.61	16.91	17.72	18.52

Source: HSBC

Consumer spending

Consumer spending

% Year	2001	2002	2003	2004	2005	2006	2007	2008f	2009f	2010f
World	**2.5**	**2.4**	**2.4**	**3.3**	**3.1**	**3.3**	**3.3**	**1.5**	**-0.6**	**1.6**
Developed	**2.3**	**2.0**	**2.0**	**2.7**	**2.4**	**2.5**	**2.3**	**0.5**	**-0.8**	**0.9**
Emerging	**3.5**	**4.0**	**4.4**	**6.2**	**6.6**	**6.7**	**7.3**	**5.5**	**0.4**	**4.5**
North America	**2.5**	**2.8**	**2.8**	**3.6**	**3.1**	**3.1**	**2.9**	**0.4**	**-0.4**	**2.0**
US	2.5	2.7	2.8	3.6	3.0	3.0	2.8	0.2	-0.3	2.1
Canada	2.3	3.6	3.0	3.3	3.7	4.1	4.6	3.0	-1.8	0.3
Latin America	**1.0**	**0.1**	**1.8**	**5.5**	**5.2**	**5.9**	**5.2**	**3.5**	**-3.4**	**2.5**
Mexico	2.5	1.6	2.2	5.6	4.8	5.7	3.9	1.5	-6.5	1.6
Brazil	0.7	1.9	-0.8	3.8	4.5	5.3	6.3	5.4	0.7	3.3
Argentina	-5.7	-14.4	8.2	9.5	8.9	7.8	9.0	6.1	-2.9	3.7
Chile	2.9	1.9	4.0	7.2	7.4	7.1	3.9	4.3	-1.4	3.2
Western Europe	**2.2**	**1.4**	**1.6**	**1.9**	**1.8**	**2.0**	**2.0**	**0.6**	**-1.3**	**-0.4**
Euro-15	**2.0**	**0.9**	**1.2**	**1.5**	**1.6**	**1.8**	**1.6**	**0.3**	**-1.0**	**-0.5**
Germany	1.9	-0.8	0.1	-0.2	0.2	1.2	-0.3	-0.1	0.5	-0.1
France	2.5	2.3	2.1	2.3	2.5	2.6	2.4	1.0	0.4	-0.5
Italy	0.7	0.2	1.0	0.8	1.2	1.3	1.2	-0.9	-2.2	-0.2
Spain	3.4	2.8	2.9	4.2	4.2	3.9	3.5	0.1	-4.1	-1.3
Other Western Europe	**2.5**	**2.9**	**2.5**	**3.0**	**2.2**	**2.4**	**3.1**	**1.2**	**-2.1**	**0.1**
UK	3.1	3.5	3.0	2.9	1.9	2.1	3.1	1.2	-3.1	-0.3
Norway	1.8	2.7	2.5	5.1	3.9	4.9	6.0	1.2	-1.1	0.9
Sweden	0.5	2.6	2.0	2.3	2.7	2.5	3.1	-0.4	-1.5	1.1
Switzerland	2.3	0.1	0.9	1.6	1.8	1.6	2.1	1.7	0.1	-0.3
EMEA	**2.8**	**5.3**	**5.9**	**8.5**	**7.9**	**7.9**	**8.6**	**8.0**	**-1.9**	**3.1**
Czech Republic	2.3	2.2	6.0	2.9	2.5	5.4	4.5	2.7	2.1	1.6
Hungary	5.7	9.9	7.8	3.2	3.8	1.3	-1.8	-0.1	-6.5	-1.8
Poland	2.3	3.0	2.6	4.0	2.7	5.0	5.0	5.4	1.8	2.5
Russia	9.5	8.9	7.5	12.1	11.8	11.3	13.6	11.5	-8.0	2.0
Turkey	-6.6	4.7	10.2	11.0	7.9	4.6	4.1	0.3	-1.1	2.6
Ukraine	9.6	9.5	12.6	12.2	16.6	14.4	17.1	15.5	-20.0	2.0
Egypt*	4.0	2.7	2.3	2.1	4.7	6.4	4.2	7.6	3.4	3.5
Israel	2.7	1.1	1.3	5.0	3.4	4.8	6.7	3.9	-0.2	2.7
Saudi Arabia**	0.6	0.3	3.7	5.8	9.5	13.4	14.0	20.0	7.0	7.5
UAE**	5.3	21.6	10.5	29.1	16.4	12.2	18.0	20.0	6.0	9.0
South Africa	3.5	3.2	3.5	6.7	6.9	8.3	6.6	2.3	-1.2	1.4
Asia/Pacific	**3.1**	**2.9**	**2.4**	**3.4**	**3.6**	**3.7**	**3.8**	**2.6**	**1.0**	**3.0**
Japan	1.7	1.1	0.4	1.6	1.3	1.5	0.7	0.6	-1.3	0.0
Australia	2.9	3.9	3.6	5.9	3.0	3.2	4.3	2.2	1.3	2.2
New Zealand	2.0	4.4	6.0	5.9	4.8	2.5	4.1	0.2	-1.2	1.6
Asia-ex-Japan	**5.2**	**5.2**	**4.7**	**5.3**	**6.5**	**6.4**	**7.5**	**5.0**	**3.4**	**6.1**
China	6.2	6.2	6.5	7.2	8.5	8.7	9.0	8.9	8.0	8.5
Asia ex-Japan & China	**4.8**	**4.8**	**3.8**	**4.3**	**5.4**	**5.2**	**6.6**	**2.6**	**0.6**	**4.5**
Hong Kong	1.9	-0.9	-1.3	7.0	3.0	5.9	8.5	1.7	-1.6	1.4
India	6.1	2.9	8.1	5.2	7.1	6.3	8.5	2.9	5.0	7.0
Indonesia	3.5	3.8	3.9	5.0	4.0	3.2	5.0	5.3	4.8	5.1
Malaysia	2.4	4.4	6.6	10.5	9.1	6.8	10.4	8.5	-0.3	5.2
Philippines	3.6	4.1	5.3	5.9	4.8	5.5	5.8	4.7	1.7	2.6
Singapore	4.7	4.9	0.9	5.9	3.1	4.0	5.2	2.4	-3.5	4.3
South Korea	5.7	8.9	-0.4	0.3	4.6	4.7	5.1	0.9	-2.6	2.6
Taiwan	0.7	2.6	1.5	4.5	3.0	1.8	2.3	-0.3	-0.4	2.1
Thailand	4.1	5.4	6.4	6.1	4.9	3.0	1.6	2.5	-0.4	2.5
Vietnam	4.5	7.6	8.0	7.1	7.3	8.3	9.6	7.3	3.0	6.0

Note: * = based upon Egyptian financial year (July-June). We now calculate the weighting system using chain nominal GDP (USD) weights. ** = Nominal data only.
Source: HSBC

HSBC

Investment spending

Investment spending

% Year	2001	2002	2003	2004	2005	2006	2007	2008f	2009f	2010f
World	**-0.3**	**-1.0**	**4.2**	**7.3**	**7.9**	**7.1**	**6.6**	**4.7**	**-7.2**	**5.4**
Developed	**-1.1**	**-2.8**	**2.0**	**4.5**	**5.0**	**3.4**	**1.5**	**-1.4**	**-16.6**	**-1.6**
Emerging	**2.7**	**5.9**	**12.2**	**16.4**	**16.4**	**16.7**	**18.4**	**16.7**	**8.4**	**14.3**
North America	**-2.5**	**-4.7**	**3.6**	**7.3**	**7.0**	**2.4**	**-2.5**	**-4.4**	**-19.1**	**-6.8**
US	-3.0	-5.2	3.4	7.3	6.8	2.0	-3.1	-5.0	-19.9	-7.2
Canada	3.0	1.3	6.3	8.0	9.0	7.1	3.7	0.9	-11.7	-3.5
Latin America	**-3.8**	**-5.4**	**1.0**	**10.6**	**8.6**	**10.2**	**10.4**	**9.4**	**-9.7**	**4.7**
Mexico	-5.6	-0.6	0.4	8.0	7.5	9.8	7.2	4.9	-9.2	2.1
Brazil	0.4	-5.2	-4.6	9.1	3.6	9.8	13.5	13.8	-8.7	7.3
Argentina	-15.7	-36.4	38.2	34.4	22.7	18.2	13.6	8.2	-13.1	5.9
Chile	4.3	1.5	5.7	10.0	23.9	2.3	12.0	19.5	-12.0	6.0
Western Europe	**0.6**	**-0.7**	**1.1**	**2.7**	**3.4**	**5.7**	**5.1**	**-0.4**	**-9.4**	**-1.2**
Euro-15	**0.6**	**-1.4**	**1.3**	**2.0**	**3.1**	**5.3**	**4.7**	**-0.3**	**-9.3**	**-1.4**
Germany	-3.4	-6.2	-0.3	-1.3	1.3	8.5	4.5	4.6	-11.2	0.2
France	2.3	-1.7	2.2	3.3	4.5	4.4	6.5	0.4	-4.7	-1.2
Italy	2.4	3.7	-0.9	1.5	1.4	3.2	1.6	-2.9	-12.6	-2.6
Spain	4.4	3.4	5.2	5.2	6.5	7.7	5.0	-2.8	-12.3	-1.8
Other Western Europe	**0.7**	**1.8**	**0.6**	**5.2**	**4.2**	**7.3**	**6.5**	**-0.9**	**-9.4**	**-0.9**
UK	2.6	3.6	1.1	4.9	2.2	6.0	6.8	-2.5	-12.6	-1.4
Norway	-1.2	-1.2	0.2	10.1	13.0	11.8	8.5	3.8	-7.6	-0.8
Sweden	-0.3	-1.8	1.5	5.1	8.9	9.5	7.7	2.4	-8.9	-3.1
Switzerland	-3.5	-0.5	-1.2	4.5	3.8	4.7	5.4	-1.7	-5.6	-0.1
EMEA	**-2.3**	**1.9**	**7.2**	**10.2**	**11.4**	**14.9**	**17.5**	**10.0**	**-6.2**	**4.0**
Czech Republic	6.6	5.1	0.4	3.9	1.8	6.0	10.8	-0.1	-3.5	0.5
Hungary	5.1	10.1	2.1	7.7	5.6	-3.2	1.5	-2.6	-6.1	0.0
Poland	-9.7	-6.3	-0.1	6.4	6.5	14.9	17.6	7.9	0.8	3.5
Russia	10.3	2.8	12.8	12.6	10.6	18.0	21.1	10.3	-20.0	1.0
Turkey	-30.0	14.7	14.2	28.4	17.4	13.3	5.4	-4.6	-9.2	3.3
Ukraine	6.2	3.4	12.2	-2.2	-0.3	18.7	24.8	10.0	-22.5	0.0
Egypt*	-2.2	5.5	-8.7	6.2	14.2	13.3	31.8	15.5	6.9	5.7
Israel	-5.1	-13.7	-10.7	4.0	2.9	6.4	15.5	3.8	-4.7	0.5
Saudi Arabia**	2.3	1.6	15.6	5.6	25.1	19.1	22.8	23.0	5.0	8.0
UAE**	4.8	3.7	17.1	11.1	15.5	29.0	25.0	26.0	-5.0	8.0
South Africa	3.5	3.7	9.1	8.9	8.9	13.8	17.1	10.2	5.0	7.1
Asia/Pacific	**1.9**	**2.8**	**7.9**	**10.7**	**12.1**	**10.8**	**13.0**	**13.4**	**1.2**	**14.9**
Japan	-0.9	-4.9	-0.5	1.5	3.4	0.6	1.3	1.8	-28.8	9.8
Australia	-4.9	17.1	8.9	8.0	7.9	5.1	9.5	8.3	-8.4	-3.1
New Zealand	-1.2	10.9	10.2	13.5	3.7	-0.3	4.8	-4.1	-16.9	4.6
Asia-ex-Japan	**6.6**	**10.5**	**16.6**	**19.4**	**19.3**	**18.3**	**20.0**	**19.4**	**14.2**	**17.3**
China	13.0	16.9	27.7	27.6	27.2	24.5	25.8	26.1	20.0	20.0
Asia ex-Japan & China	**1.5**	**4.8**	**5.5**	**9.4**	**8.3**	**8.1**	**9.0**	**4.9**	**-1.0**	**8.6**
Hong Kong	2.9	-4.6	1.0	2.7	4.1	7.1	3.4	-0.3	-1.4	8.9
India	4.3	7.7	9.7	18.9	17.6	14.5	12.9	8.2	8.0	13.0
Indonesia	6.5	4.7	0.6	14.7	10.9	2.6	9.4	11.7	1.6	6.4
Malaysia	-2.8	0.3	2.7	3.1	5.0	7.5	9.6	0.8	-8.9	4.9
Philippines	-13.0	2.3	3.6	2.8	-6.6	3.9	10.9	2.9	-1.9	4.0
Singapore	-3.9	-11.4	-3.2	10.2	-2.0	13.3	19.2	13.7	-10.4	5.7
South Korea	0.3	7.1	4.4	2.1	1.9	3.4	4.2	-1.7	-5.1	5.6
Taiwan	-19.9	1.1	1.7	19.5	1.2	0.9	1.9	-10.6	-17.9	3.8
Thailand	1.1	6.5	12.1	13.2	10.5	3.9	1.3	1.1	-8.8	5.8
Vietnam	10.7	12.9	11.9	10.4	9.7	9.9	23.0	13.2	3.0	6.3

Note: * = based upon Egyptian financial year (July-June). We now calculate the weighting system using chain nominal GDP (USD) weights, ** = Nominal data only.
Source: HSBC

HSBC

Exports

Export volume growth (GDP basis)

% Year	2001	2002	2003	2004	2005	2006	2007	2008f	2009f	2010f
World	**0.5**	**3.0**	**5.2**	**10.8**	**8.4**	**10.1**	**8.3**	**4.0**	**-14.4**	**1.1**
Developed	**0.6**	**1.3**	**1.7**	**7.6**	**5.6**	**8.1**	**5.5**	**1.9**	**-15.8**	**-0.9**
Emerging	**0.1**	**7.4**	**14.1**	**18.0**	**14.0**	**13.9**	**13.1**	**7.7**	**-12.1**	**4.1**
North America	**-4.8**	**-1.4**	**0.4**	**8.6**	**5.8**	**7.2**	**6.8**	**4.0**	**-18.5**	**-8.7**
US	-5.4	-2.3	1.3	9.7	7.0	9.1	8.4	6.2	-18.8	-10.0
Canada	-3.0	1.2	-2.3	5.0	1.9	0.8	1.1	-4.7	-17.1	-3.2
Latin America	**0.0**	**1.9**	**7.4**	**16.0**	**12.5**	**11.8**	**9.7**	**9.2**	**-15.7**	**3.2**
Mexico	-3.7	1.4	2.7	11.5	6.8	10.9	5.7	1.4	-16.3	0.1
Brazil	5.7	3.7	21.1	32.0	22.6	16.5	16.6	23.2	-17.9	5.4
Argentina	4.3	0.7	4.4	2.0	20.0	6.0	8.0	0.0	-15.7	8.9
Chile	7.2	1.6	6.0	13.3	4.3	5.5	7.8	3.1	1.5	3.4
Western Europe	**3.7**	**1.6**	**1.2**	**6.4**	**5.4**	**8.4**	**4.7**	**1.1**	**-14.3**	**0.5**
Euro-15	**4.0**	**1.8**	**1.2**	**6.7**	**4.9**	**8.1**	**6.0**	**0.9**	**-15.5**	**0.2**
Germany	6.8	4.3	2.4	9.4	7.9	13.1	7.7	2.2	-17.4	0.9
France	2.5	1.4	-1.2	3.7	3.4	5.0	2.5	-0.5	-12.5	-2.1
Italy	2.2	-2.8	-1.5	3.6	2.0	6.5	4.0	-3.7	-19.9	0.7
Spain	4.2	2.0	3.7	4.2	2.5	6.7	4.9	0.7	-20.0	-1.6
Other Western Europe	**2.4**	**1.0**	**1.3**	**5.6**	**7.1**	**9.3**	**0.8**	**1.7**	**-10.5**	**1.5**
UK	3.0	1.0	1.8	4.8	8.1	11.0	-4.1	0.8	-13.4	0.2
Norway	4.1	-0.4	-0.4	0.6	0.2	-0.5	2.4	1.3	-6.0	-0.3
Sweden	0.7	1.2	4.0	10.8	7.1	8.5	6.0	1.7	-11.4	3.2
Switzerland	0.5	-0.1	-0.5	7.9	7.3	9.9	9.4	2.3	-13.2	1.6
EMEA	**1.7**	**3.0**	**10.5**	**11.9**	**6.5**	**8.1**	**7.3**	**5.7**	**-10.4**	**3.9**
Czech Republic	11.2	2.1	7.2	20.7	11.8	15.5	15.0	6.7	-23.0	2.2
Hungary	8.1	3.9	6.2	15.7	11.6	17.7	15.9	4.6	-15.5	3.2
Poland	1.0	7.4	20.8	18.6	2.6	12.3	4.9	5.8	-10.2	2.5
Russia	3.6	9.6	12.5	11.8	6.5	7.3	6.4	3.0	-8.0	2.0
Turkey	3.9	6.9	6.9	11.2	7.9	6.6	7.3	2.6	-6.3	4.2
Ukraine	2.9	9.1	10.3	13.8	-11.2	-4.9	3.2	4.0	-40.0	10.0
Egypt*	3.3	-7.8	11.8	27.6	20.2	21.3	23.3	28.8	8.9	11.3
Israel	-11.2	-2.3	8.2	18.2	4.3	5.9	8.5	8.0	-7.1	4.5
Saudi Arabia	-3.5	-4.4	13.7	3.1	4.7	-2.6	-4.1	6.0	-11.9	4.2
UAE**	0.6	-1.3	10.7	5.5	6.9	8.4	4.0	4.3	-4.5	4.8
South Africa	2.4	1.0	0.1	2.9	8.0	6.0	7.5	1.7	-8.5	3.5
Asia/Pacific	**-2.1**	**9.4**	**14.2**	**18.6**	**14.3**	**14.5**	**13.7**	**6.7**	**-13.4**	**4.9**
Japan	-6.8	7.4	9.2	14.0	7.0	9.7	8.4	1.7	-21.6	8.0
Australia	2.2	0.0	-1.2	4.3	2.3	3.3	3.3	3.9	1.6	5.0
New Zealand	3.4	6.4	2.1	5.8	-0.3	1.8	3.8	-1.7	-2.5	3.6
Asia-ex-Japan	**-0.7**	**10.9**	**17.2**	**21.2**	**17.3**	**16.4**	**15.6**	**8.0**	**-12.1**	**4.3**
China	7.5	18.0	32.0	32.0	29.0	25.0	23.8	11.2	-14.0	2.0
Asia ex-Japan & China	**-3.2**	**8.5**	**11.8**	**16.5**	**11.6**	**11.5**	**10.5**	**5.8**	**-10.7**	**6.0**
Hong Kong	-1.7	9.0	12.8	15.4	10.6	9.4	8.3	2.7	-18.6	-2.8
India	-1.6	14.4	19.0	28.0	31.1	21.1	20.6	24.6	-10.6	6.7
Indonesia	0.6	-1.2	5.9	13.5	16.6	9.4	8.5	9.5	-11.4	8.5
Malaysia	-7.5	4.5	5.7	2.3	8.3	6.6	4.5	1.3	-15.1	6.6
Philippines	-3.4	4.1	4.8	15.0	4.8	13.4	5.6	-1.9	-8.7	3.8
Singapore	-4.0	7.2	13.7	20.6	11.7	11.7	8.7	1.3	-15.5	6.1
South Korea	-3.4	12.1	14.5	19.7	7.8	11.4	12.6	5.7	-7.0	5.5
Taiwan	-7.8	10.6	10.4	14.4	7.6	10.3	8.8	0.0	-13.9	8.7
Thailand	-4.2	12.0	7.0	9.6	4.2	9.1	7.1	5.4	-11.7	5.0
Vietnam	4.0	11.2	20.6	31.4	22.5	22.1	22.7	29.9	-5.4	12.2

Note: * = based upon Egyptian financial year (July-June). We now calculate the weighting system using chain nominal GDP (USD) weights
Source: HSBC

Industrial production

Industrial production

% Year	2001	2002	2003	2004	2005	2006	2007	2008f	2009f	2010f
World	**0.1**	**2.7**	**4.6**	**6.3**	**5.3**	**6.3**	**5.8**	**1.5**	**-7.8**	**3.9**
Developed	**-2.4**	**-0.4**	**1.0**	**2.6**	**2.0**	**2.9**	**2.2**	**-2.2**	**-13.8**	**0.9**
Emerging	**3.5**	**6.9**	**9.3**	**10.8**	**9.2**	**10.2**	**10.1**	**5.8**	**-0.7**	**7.5**
North America	**-3.4**	**0.1**	**1.2**	**2.4**	**3.1**	**2.1**	**1.4**	**-2.4**	**-9.9**	**0.4**
US	-3.4	-0.1	1.3	2.5	3.3	2.3	1.5	-2.2	-10.1	0.3
Canada	-3.5	2.1	0.2	1.5	1.6	0.2	0.2	-4.1	-7.9	1.4
Latin America	**-0.8**	**0.7**	**2.2**	**7.3**	**3.9**	**4.6**	**5.3**	**1.8**	**-6.9**	**5.1**
Mexico	-3.5	-0.1	-0.2	3.7	2.6	5.3	3.1	-0.7	-8.9	2.9
Brazil	1.6	2.7	0.1	8.3	3.1	2.8	6.0	3.1	-7.0	8.0
Argentina	-2.9	-8.3	13.4	10.7	8.0	8.4	7.5	3.8	-3.8	3.0
Chile	0.6	10.9	5.3	10.2	6.0	3.3	6.0	-0.2	-3.5	1.2
Western Europe	**0.0**	**-0.7**	**0.2**	**1.9**	**1.0**	**3.4**	**2.9**	**-1.8**	**-14.4**	**0.9**
Euro-15	**0.4**	**-0.4**	**0.3**	**2.1**	**1.4**	**4.0**	**3.4**	**-1.7**	**-15.6**	**0.8**
Germany	-0.2	-1.3	0.2	2.5	2.9	5.8	5.8	0.0	-16.9	1.7
France	0.9	-1.8	-1.1	1.4	0.2	1.4	1.5	-2.5	-16.5	-2.8
Italy	-1.1	-1.3	-0.6	-0.4	-0.8	3.7	2.1	-3.3	-19.2	1.4
Spain	-1.3	0.1	1.3	1.7	1.2	3.9	2.0	-7.5	-15.1	0.9
Other Western Europe	**-1.2**	**-1.7**	**-0.3**	**1.4**	**-0.3**	**1.5**	**1.3**	**-2.2**	**-10.7**	**1.3**
UK	-1.5	-1.7	-0.6	0.9	-1.1	0.7	0.1	-2.6	-10.7	1.5
Norway	-0.6	0.0	-1.9	-1.1	-0.3	-2.2	-1.3	0.2	-1.9	-0.5
Sweden	0.1	-0.2	1.8	4.1	2.4	3.7	4.1	-3.7	-14.9	2.2
Switzerland	-0.7	-5.1	0.4	4.0	2.7	7.8	9.5	1.2	-12.0	0.3
EMEA	**2.4**	**3.7**	**7.0**	**7.9**	**4.6**	**6.3**	**6.1**	**2.2**	**-11.8**	**2.9**
Czech Republic	5.0	5.0	5.9	9.8	6.4	9.8	8.5	-1.5	-18.0	2.5
Hungary	5.0	2.6	6.4	8.3	7.0	10.6	8.5	4.9	-18.2	3.5
Poland	0.6	0.8	8.7	12.7	4.0	12.0	9.7	3.9	-11.1	1.5
Russia	4.9	3.7	7.0	6.6	4.0	4.4	4.1	0.8	-13.2	1.9
Turkey	-8.7	9.5	8.8	9.7	5.4	5.8	5.4	-0.9	-9.7	3.0
Ukraine	14.2	7.0	15.8	12.5	3.1	6.2	10.2	-3.1	-24.0	4.0
Egypt*	6.8	7.1	2.7	6.5	5.8	5.3	8.9	13.7	3.8	4.7
Israel	-5.0	-1.8	-0.3	6.9	3.6	8.5	4.3	7.0	-5.5	3.9
Saudi Arabia	-1.3	-3.9	13.4	6.6	6.1	2.8	2.7	4.5	-6.3	4.0
UAE	3.0	-1.4	12.7	6.7	5.6	10.3	8.0	6.4	-1.6	5.0
South Africa	2.9	4.6	-2.0	3.3	4.2	4.9	5.5	1.0	-16.6	4.2
Asia/Pacific	**2.2**	**6.8**	**9.4**	**10.7**	**9.3**	**10.7**	**10.1**	**5.5**	**-2.1**	**7.8**
Japan	-6.8	-1.3	3.3	5.5	1.1	4.8	2.8	-3.4	-27.0	2.3
Australia	0.3	2.5	-0.1	0.2	1.8	0.4	3.3	2.6	-3.5	2.0
New Zealand	-0.1	5.4	3.2	5.0	-2.1	-1.5	2.0	-0.8	-2.4	2.3
Asia-ex-Japan	**4.9**	**9.2**	**11.4**	**12.4**	**11.5**	**12.5**	**12.1**	**7.6**	**3.6**	**9.3**
China	9.7	12.7	16.7	16.3	15.9	16.2	17.1	12.9	9.5	12.0
Asia ex-Japan & China	**-0.8**	**6.1**	**5.9**	**8.7**	**6.1**	**6.4**	**5.9**	**2.0**	**-5.9**	**5.1**
Hong Kong	-4.4	-9.7	-9.2	2.9	2.5	2.2	-1.6	-6.4	-6.3	-6.8
India	2.7	5.8	7.0	8.4	8.2	11.5	8.5	2.6	2.1	8.1
Indonesia	3.3	5.3	5.3	6.4	4.6	4.6	4.7	3.7	2.0	4.6
Malaysia	-5.9	4.3	8.4	11.3	5.2	6.7	3.1	1.4	-8.9	6.8
Philippines	2.9	3.5	4.2	5.0	5.3	4.2	3.3	4.3	-2.1	1.5
Singapore	-11.6	8.4	-30.3	13.9	9.5	11.9	5.9	-4.2	-8.9	7.0
South Korea	0.6	8.0	5.5	10.4	6.3	8.4	6.9	3.1	-6.6	7.2
Taiwan	-8.4	7.1	8.7	8.4	3.8	4.7	7.8	-1.8	-16.5	6.0
Thailand	1.4	6.9	10.4	8.3	5.2	6.0	6.2	3.9	-2.2	4.3
Vietnam	16.2	14.2	19.8	17.6	25.5	16.0	11.6	11.8	5.2	11.5

Source: HSBC

Wage growth

Wage growth

% Year	2001	2002	2003	2004	2005	2006	2007	2008f	2009f	2010f
World	**6.0**	**5.8**	**5.8**	**5.2**	**5.8**	**6.1**	**6.7**	**6.9**	**3.7**	**4.8**
North America	**4.0**	**3.6**	**3.5**	**3.7**	**3.2**	**3.1**	**3.3**	**3.0**	**2.7**	**2.9**
US	4.2	3.7	3.7	3.8	3.2	3.1	3.4	3.0	2.8	3.0
Canada	1.4	2.1	1.4	2.1	3.2	3.0	3.2	2.8	1.8	1.5
Latin America	**5.1**	**6.6**	**7.1**	**5.6**	**9.3**	**8.8**	**10.1**	**11.1**	**6.5**	**6.9**
Mexico	9.3	6.1	4.9	4.4	4.5	4.3	4.3	4.5	4.1	3.7
Argentina	-4.0	7.6	12.1	9.3	20.3	18.9	22.7	25.2	12.0	14.5
Chile	5.3	6.8	6.6	2.9	5.0	5.4	7.3	8.5	4.6	3.6
Western Europe	**4.2**	**3.6**	**3.3**	**2.8**	**2.8**	**3.0**	**3.2**	**3.9**	**3.5**	**3.1**
Euro-15	**3.8**	**3.2**	**2.8**	**2.4**	**2.5**	**2.6**	**2.9**	**3.6**	**3.1**	**2.7**
Germany	1.9	2.6	2.0	1.3	1.1	1.2	1.3	2.8	2.6	1.9
France	2.5	2.5	2.4	2.5	2.8	2.8	2.6	3.0	2.6	2.4
Italy	2.6	2.1	2.2	2.8	3.1	2.9	2.3	3.4	2.5	2.2
Spain	3.5	3.8	3.9	2.8	2.6	3.4	3.9	4.8	1.9	2.1
Other Western Europe	**4.4**	**3.7**	**3.5**	**4.1**	**3.8**	**4.0**	**4.0**	**3.8**	**2.6**	**2.1**
UK	4.5	3.5	3.4	4.4	4.0	4.1	3.9	3.6	2.5	2.0
Norway	4.5	5.2	4.7	4.2	3.5	4.1	5.7	6.0	3.8	3.2
Sweden	3.7	3.5	2.9	2.5	2.9	3.0	3.6	3.9	2.2	2.2
EMEA	**19.6**	**16.5**	**12.4**	**10.0**	**12.4**	**13.1**	**14.8**	**12.8**	**1.6**	**6.3**
Czech Republic	3.5	3.5	6.8	6.7	5.3	6.5	7.3	8.3	4.5	5.3
Hungary	18.2	18.2	12.1	6.2	8.7	8.2	8.0	7.5	5.0	5.5
Poland	5.3	2.3	4.7	-8.1	3.2	5.0	9.1	10.3	3.2	4.5
Russia	21.0	16.6	10.4	10.6	12.6	13.5	17.2	9.7	-6.0	2.0
Turkey	31.8	37.2	23.0	13.4	12.2	11.5	9.5	8.5	5.5	7.5
Ukraine	34.9	20.7	23.0	27.6	36.5	29.4	29.7	32.0	5.0	12.0
Israel	7.1	-4.2	-3.0	2.5	1.0	1.6	2.1	-0.8	0.0	2.5
South Africa	8.8	9.5	8.1	7.5	6.5	9.1	8.9	12.4	6.5	8.0
Asia/Pacific	**6.8**	**7.5**	**8.5**	**7.8**	**8.7**	**12.2**	**13.4**	**14.4**	**7.1**	**9.9**
Japan	-1.6	-2.9	-0.8	-0.7	0.6	0.2	-0.7	0.4	-3.5	0.5
Australia	3.6	3.3	3.6	3.5	4.1	4.0	4.1	4.1	3.9	3.8
New Zealand	1.9	2.2	2.3	2.3	2.8	3.2	3.2	3.5	3.2	3.4
Asia-ex-Japan	**9.4**	**10.6**	**11.1**	**10.0**	**10.7**	**11.7**	**13.1**	**13.8**	**7.5**	**9.3**
China	11.7	12.6	13.6	12.3	12.3	14.0	16.2	17.0	9.0	11.0
Asia ex-Japan & China	**3.3**	**4.6**	**3.8**	**3.3**	**4.8**	**4.2**	**3.7**	**4.0**	**2.8**	**3.7**
Hong Kong	0.0	0.0	-1.3	-2.5	2.6	1.3	0.3	4.0	1.0	1.0
Philippines	10.8	10.4	0.4	3.6	8.5	7.9	4.5	5.3	3.8	4.5
Singapore	2.7	1.2	3.6	2.6	4.3	3.5	4.1	5.0	2.5	4.0
South Korea	5.7	11.5	9.4	6.5	6.4	5.6	5.9	4.2	2.8	4.8
Taiwan	0.0	-0.7	1.5	1.8	1.3	1.1	2.3	0.0	2.2	2.3
Thailand	1.0	-0.8	2.2	2.3	6.9	6.2	3.0	10.2	4.0	4.9

Note: Global and regional aggregates are calculated using the World Bank's 2004 PPP weights
Source: HSBC

Budget balance

Budget balance

% GDP	2001	2002	2003	2004	2005	2006	2007	2008f	2009f	2010f
North America	**0.6**	**-2.4**	**-3.2**	**-2.9**	**-1.9**	**-1.0**	**-1.4**	**-4.2**	**-14.4**	**-6.8**
US	0.5	-2.7	-3.6	-3.2	-2.1	-1.2	-1.6	-4.6	-15.4	-7.2
Canada	1.3	0.8	0.7	0.7	0.8	1.0	0.7	-0.1	-3.2	-1.9
Latin America	**-2.3**	**-2.6**	**-2.3**	**-0.7**	**-0.8**	**-0.6**	**-0.3**	**-0.2**	**-2.1**	**-1.7**
Mexico	-0.7	-1.2	-0.6	-0.2	-0.1	0.1	0.0	-0.1	-2.3	-2.2
Brazil	-3.3	-4.2	-4.7	-2.4	-3.0	-2.9	-2.2	-1.5	-2.4	-2.0
Argentina	-3.2	-1.5	0.5	2.6	1.8	1.8	1.1	1.4	-0.3	0.6
Chile	-0.4	-1.0	-0.4	2.1	4.6	7.7	8.8	5.2	-2.9	-3.0
Western Europe	**-1.0**	**-2.2**	**-2.8**	**-2.6**	**-2.2**	**-1.0**	**-0.5**	**-1.6**	**-6.6**	**-7.2**
Euro-15	**-1.8**	**-2.6**	**-3.1**	**-3.0**	**-2.5**	**-1.3**	**-0.6**	**-1.4**	**-5.7**	**-6.5**
Germany	-2.8	-3.7	-4.0	-3.8	-3.2	-1.6	0.1	-0.1	-4.6	-6.1
France	-1.6	-3.2	-4.1	-3.6	-3.0	-2.4	-2.7	-3.2	-7.1	-7.8
Italy	-3.1	-3.0	-3.5	-3.5	-4.2	-3.3	-1.5	-2.7	-5.8	-6.4
Spain	-0.7	-0.5	-0.2	-0.4	1.0	2.0	2.2	-3.8	-8.4	-8.4
Other Western Europe	**1.9**	**-0.9**	**-2.0**	**-1.5**	**-1.2**	**-0.2**	**-0.2**	**-2.5**	**-9.5**	**-9.3**
UK	0.8	-1.8	-3.0	-3.1	-3.3	-2.3	-2.4	-5.4	-13.2	-12.6
Norway	13.3	9.2	7.3	11.1	15.1	18.5	17.4	20.0	14.0	11.5
Sweden	1.7	-1.4	-1.2	0.6	2.1	2.2	3.5	2.8	0.5	-0.4
EMEA	**-2.3**	**-3.2**	**-2.1**	**-0.4**	**2.4**	**3.0**	**1.9**	**2.9**	**-5.9**	**-4.4**
Hungary	-4.1	-9.0	-7.2	-6.5	-7.8	-9.1	-4.9	-3.3	-4.0	-4.0
Poland	-4.2	-4.9	-4.4	-4.5	-2.5	-2.4	-1.4	-1.9	-3.0	-2.9
Russia	3.0	1.4	1.7	4.4	7.5	7.4	5.4	4.1	-8.4	-4.7
Turkey	-12.1	-11.4	-8.8	-5.4	-1.3	-0.5	-1.6	-1.5	-7.4	-5.6
Ukraine	-0.3	0.5	0.2	-3.3	-1.1	-0.7	-1.4	-1.3	-5.3	-4.6
Egypt*	-5.9	-10.2	-9.1	-9.1	-9.6	-8.2	-7.5	-6.8	-8.1	-9.5
Israel	-4.5	-3.8	-5.5	-3.9	-1.9	-0.9	0.0	-2.1	-6.3	-5.3
Saudi Arabia	-3.9	-2.9	4.5	11.4	18.4	21.7	12.5	31.7	-2.5	-2.1
UAE	-10.6	-10.8	-4.5	-0.4	7.7	11.6	11.6	15.7	1.9	2.8
South Africa	-0.7	-0.7	-2.5	-2.0	-0.5	0.2	0.7	-0.3	-5.3	-5.3
Asia/Pacific	**-4.1**	**-4.1**	**-3.4**	**-2.5**	**-2.4**	**-1.2**	**-0.4**	**-1.9**	**-5.1**	**-4.9**
Japan	-6.8	-8.3	-7.7	-5.5	-6.1	-1.0	-1.4	-3.5	-10.2	-10.5
Australia	-0.1	1.3	1.8	1.1	1.5	1.5	1.6	1.8	-1.5	-1.5
New Zealand	2.1	3.2	3.8	4.3	4.5	3.7	3.7	2.5	0.1	0.1
Asia-ex-Japan	**-3.5**	**-3.2**	**-2.6**	**-2.0**	**-1.8**	**-1.4**	**-0.2**	**-1.7**	**-4.0**	**-3.8**
China	-2.3	-2.6	-2.2	-1.3	-1.2	-1.0	0.6	-0.4	-2.5	-3.1
Asia ex-Japan & China	**-4.5**	**-3.7**	**-3.0**	**-2.6**	**-2.3**	**-1.8**	**-1.1**	**-3.1**	**-5.6**	**-4.5**
Hong Kong	-4.9	-4.8	-3.2	1.7	1.0	4.0	7.7	0.1	-4.0	-1.9
India	-6.7	-6.4	-4.9	-4.1	-4.2	-3.6	-2.8	-6.3	-7.0	-6.0
Indonesia	-2.5	-1.3	-1.7	-1.0	-0.5	-0.9	-1.3	-0.1	-3.0	-2.0
Malaysia	-5.5	-5.6	-4.4	-4.1	-3.6	-3.3	-3.2	-4.8	-9.0	-6.5
Philippines	-4.0	-5.3	-4.7	-3.8	-2.7	-1.1	-0.2	-0.9	-3.8	-4.3
Singapore	2.2	0.8	-1.1	-1.9	-0.8	-0.2	0.6	1.7	2.7	-3.3
South Korea	1.2	3.3	1.1	0.7	0.4	0.4	3.8	1.2	-4.0	-1.3
Taiwan	-6.4	-4.2	-2.7	-2.8	-0.6	-0.6	-0.2	-0.8	-4.5	-3.5
Thailand	-2.6	-1.4	0.3	0.0	0.3	1.2	-2.3	-1.1	-6.3	-6.1
Vietnam	-4.9	-4.8	-4.9	-4.9	-4.9	-5.0	-5.0	-5.0	-8.0	-7.0

Note: * = based upon Egyptian financial year (July-June). Global and regional aggregates are calculated using the World Banks' 2004 PPP weights
Source: HSBC

HSBC

Current account

Percentage										
% GDP	2001	2002	2003	2004	2005	2006	2007	2008f	2009f	2010f
North America	**-3.4**	**-3.9**	**-4.3**	**-4.8**	**-5.4**	**-5.5**	**-4.8**	**-4.2**	**-2.0**	**-1.1**
US	-3.9	-4.4	-4.8	-5.4	-6.0	-6.1	-5.3	-4.6	-2.0	-1.2
Canada	2.3	1.7	1.2	2.3	1.9	1.4	1.0	0.5	-1.4	0.2
Latin America	**-3.2**	**-0.2**	**0.9**	**1.1**	**1.1**	**1.3**	**0.5**	**-1.0**	**-0.7**	**-1.5**
Mexico	-2.8	-2.2	-1.0	-0.7	-0.5	-0.5	-0.8	-1.4	-1.9	-2.2
Brazil	-4.2	-1.5	0.8	1.8	1.6	1.3	0.1	-1.8	-1.1	-1.8
Argentina	-1.4	9.0	6.3	2.3	3.1	3.8	2.7	2.4	3.0	0.8
Chile	-1.6	-0.9	-1.1	2.2	0.8	4.6	4.4	-2.0	-0.4	-2.0
Western Europe	**-0.1**	**0.7**	**0.6**	**0.9**	**0.4**	**0.2**	**0.3**	**-0.3**	**-0.6**	**-0.4**
Euro-15	**-0.4**	**0.6**	**0.3**	**0.8**	**0.1**	**-0.1**	**0.1**	**-1.0**	**-1.2**	**-1.0**
Germany	0.0	2.0	1.9	4.7	5.1	6.5	7.9	6.6	4.1	4.3
France	2.0	1.3	0.9	0.6	-0.4	-0.5	-1.0	-1.9	-1.2	-1.7
Italy	-0.1	-0.8	-1.3	-0.9	-1.7	-2.6	-2.4	-3.4	-2.9	-2.7
Spain	-3.9	-3.3	-3.5	-5.3	-7.4	-9.0	-10.0	-9.5	-8.1	-6.2
Other Western Europe	**1.0**	**1.0**	**1.7**	**1.3**	**1.3**	**1.1**	**0.9**	**1.8**	**1.1**	**1.3**
UK	-2.1	-1.7	-1.6	-2.1	-2.6	-3.4	-2.9	-1.7	-1.4	-1.1
Norway	16.1	12.6	12.3	12.7	16.3	17.3	16.0	19.5	11.0	9.5
Sweden	5.1	4.7	7.2	6.7	7.0	8.5	8.6	7.8	7.4	6.9
Switzerland	7.7	8.3	12.8	12.9	13.6	15.0	10.0	9.3	6.2	7.4
EMEA	**3.5**	**2.8**	**3.0**	**4.1**	**5.1**	**3.7**	**1.9**	**1.3**	**-0.3**	**-0.8**
Czech Republic	-5.3	-5.5	-6.2	-5.2	-1.3	-2.6	-3.1	-3.4	-2.7	-2.6
Hungary	-6.1	-7.0	-8.7	-8.7	-7.3	-7.8	-6.6	-9.0	-4.8	-5.0
Poland	-2.8	-2.5	-2.1	-4.1	-1.6	-2.3	-3.8	-7.2	-3.3	-4.3
Russia	11.0	8.4	8.3	10.0	11.1	9.5	6.0	5.9	3.6	2.1
Turkey	1.7	-0.7	-2.6	-4.0	-4.7	-6.1	-5.8	-5.7	-2.0	-2.3
Ukraine	3.7	7.5	5.8	10.5	3.1	-1.6	-4.0	-7.0	-8.3	-8.9
Egypt*	0.0	0.7	2.4	4.3	3.2	1.6	1.7	0.5	-1.8	-1.4
Israel	-1.5	-1.2	1.2	2.2	3.2	5.1	2.6	0.8	2.0	1.7
Saudi Arabia	5.1	6.3	13.1	19.7	28.5	27.7	24.9	30.8	7.6	9.0
UAE	9.4	4.7	8.5	9.9	18.2	21.5	18.6	12.1	2.7	7.2
South Africa	0.1	0.6	-1.3	-3.2	-3.8	-6.4	-7.3	-7.4	-5.1	-5.7
Asia/Pacific	**2.0**	**2.8**	**3.0**	**2.8**	**3.7**	**5.2**	**6.0**	**3.9**	**2.9**	**2.6**
Japan	2.2	2.9	3.2	3.7	3.6	3.9	4.9	3.2	2.8	4.1
Australia	-2.0	-3.7	-5.3	-6.1	-5.8	-5.3	-6.3	-4.3	-3.8	-4.5
New Zealand	-2.8	-3.9	-4.3	-6.4	-8.5	-8.8	-8.2	-8.9	-7.5	-8.0
Asia-ex-Japan	**2.2**	**3.1**	**3.4**	**3.0**	**4.1**	**5.9**	**6.7**	**4.4**	**3.3**	**2.5**
China	1.3	2.4	2.8	3.6	7.2	9.5	11.0	8.6	5.1	4.4
Asia ex-Japan & China	**3.0**	**3.8**	**4.0**	**2.5**	**1.1**	**2.3**	**2.4**	**0.1**	**1.4**	**0.6**
Hong Kong	4.5	8.3	9.2	8.9	12.4	11.4	10.8	10.9	9.6	9.7
India	0.8	1.5	1.6	0.1	-1.9	-1.1	-1.0	-3.2	-2.2	-2.5
Indonesia	4.2	3.9	3.4	0.6	0.1	3.0	2.4	0.1	0.6	-0.3
Malaysia	8.3	8.4	12.8	12.1	15.0	16.3	15.7	17.6	12.3	10.2
Philippines	1.9	6.9	0.9	1.1	2.0	4.5	4.8	2.5	1.4	-0.6
Singapore	16.2	17.7	31.0	26.4	27.5	25.4	23.5	14.8	10.3	9.0
South Korea	1.7	1.0	2.0	4.1	1.9	0.6	0.6	-0.7	2.1	-0.1
Taiwan	6.5	8.9	10.0	6.0	4.9	7.2	8.6	6.3	8.9	8.3
Thailand	5.4	5.5	5.6	1.7	-4.3	1.1	5.9	-0.1	4.0	2.1
Vietnam	2.1	-1.7	-4.9	-2.1	-1.1	-0.3	-9.8	-11.6	-5.6	-4.7

Note: * = based upon Egyptian financial year (July-June). Global and regional aggregates are calculated using the World Banks' 2004 PPP weights
Source: HSBC

Balance

USDbn	2001	2002	2003	2004	2005	2006	2007	2008f	2009f	2010f
North America	**-381.0**	**-446.0**	**-511.0**	**-609.0**	**-689.9**	**-753.6**	**-703.6**	**-646.2**	**-275.8**	**-101.7**
US	-398.0	-459.0	-522.0	-631.0	-710.9	-771.6	-718.6	-653.7	-260.2	-103.8
Canada	17.0	13.0	11.0	22.0	21.0	18.0	15.0	7.5	-15.5	2.1
Latin America	**-45.8**	**-13.5**	**4.4**	**12.0**	**16.2**	**24.1**	**7.7**	**-39.6**	**-23.5**	**-48.6**
Mexico	-17.7	-14.1	-7.2	-5.2	-4.4	-4.4	-8.2	-15.7	-16.3	-20.6
Brazil	-23.2	-7.6	4.2	11.7	14.0	13.6	1.6	-28.3	-15.5	-27.4
Argentina	-3.8	8.8	8.1	3.4	5.6	8.0	7.1	7.8	9.0	2.4
Chile	-1.1	-0.6	-0.8	2.1	1.0	6.8	7.2	-3.4	-0.7	-3.0
Western Europe	**7.7**	**89.9**	**98.9**	**131.1**	**84.5**	**62.5**	**81.0**	**67.6**	**47.8**	**51.5**
Euro-15	**-19.0**	**56.2**	**38.4**	**75.3**	**10.4**	**-16.2**	**17.8**	**-69.5**	**-27.4**	**-19.7**
Germany	0.4	42.5	47.0	125.2	138.8	193.0	258.3	252.8	214.1	220.2
France	25.0	20.0	16.0	12.0	-9.0	-11.0	-25.0	-55.0	-37.4	-37.1
Italy	-0.6	-9.9	-19.9	-15.9	-28.6	-49.0	-50.9	-76.0	-62.0	-53.8
Spain	-22.7	-23.5	-31.6	-53.7	-80.9	-112.9	-142.3	-161.6	-118.7	-124.8
Other Western Europe	**26.6**	**33.7**	**60.5**	**55.8**	**74.1**	**78.7**	**63.1**	**137.1**	**75.1**	**71.2**
UK	-29.7	-28.4	-30.2	-45.7	-58.6	-83.3	-80.9	-35.7	-32.4	-26.4
Norway	26.5	25.6	27.1	32.0	48.4	59.8	61.3	84.6	42.8	28.5
Sweden	10.8	12.5	22.6	23.5	24.4	34.1	38.5	37.1	31.8	31.1
Switzerland	19.0	24.0	41.0	46.0	49.0	60.0	42.0	43.0	25.7	31.1
EMEA	**41.7**	**32.4**	**50.4**	**87.1**	**162.6**	**166.9**	**121.5**	**147.3**	**16.6**	**6.9**
Czech Republic	-3.1	-4.6	-5.8	-5.6	-1.6	-3.7	-5.2	-6.8	-5.5	-6.0
Hungary	-3.0	-4.9	-6.8	-8.6	-8.1	-8.7	-8.9	-13.1	-6.5	-7.7
Poland	-5.4	-5.0	-4.6	-10.4	-4.8	-7.9	-15.9	-37.7	-16.5	-25.0
Russia	33.6	29.1	35.8	59.9	84.3	94.3	77.2	98.9	43.9	28.0
Turkey	4.0	-1.0	-8.0	-14.0	-22.0	-32.0	-38.0	-41.6	-11.9	-16.1
Ukraine	1.4	3.2	2.9	6.8	2.5	-1.7	-5.6	-12.6	-8.9	-10.4
Egypt*		0.6	1.9	3.4	2.9	1.8	2.3	0.9	-3.6	-3.0
Israel	-1.7	-1.3	1.4	2.7	4.2	7.2	4.2	1.6	3.6	3.5
Saudi Arabia	9.4	12.0	28.1	49.3	90.0	98.9	95.0	150.4	29.7	39.2
UAE	6.5	3.5	7.5	10.5	24.4	35.1	37.0	27.9	5.7	17.1
South Africa	0.1	0.7	-2.2	-6.9	-9.2	-16.4	-20.6	-20.5	-13.5	-12.8
Asia/Pacific	**165.6**	**223.9**	**256.8**	**307.6**	**363.8**	**502.2**	**649.7**	**540.6**	**426.6**	**424.2**
Japan	86.7	117.7	131.1	170.2	165.0	174.7	202.9	157.7	131.8	187.2
Australia	-7.0	-16.0	-29.0	-37.0	-41.0	-40.0	-57.0	-42.9	-29.7	-37.8
New Zealand	-1.4	-2.5	-3.5	-6.0	-9.2	-8.7	-11.1	-11.5	-7.8	-9.1
Asia-ex-Japan	**87.3**	**124.7**	**158.1**	**180.4**	**249.0**	**376.2**	**514.8**	**437.2**	**332.3**	**284.0**
China	17.4	35.4	45.9	68.7	160.8	253.3	371.8	372.0	240.0	230.0
Asia ex-Japan & China	**69.8**	**89.3**	**112.3**	**111.8**	**88.2**	**122.9**	**143.0**	**65.2**	**92.3**	**54.0**
Hong Kong	7.5	13.6	14.7	14.7	22.1	21.7	22.4	23.5	19.6	20.6
India	3.4	7.1	8.8	0.8	-14.7	-9.3	-11.3	-38.0	-24.1	-30.3
Indonesia	6.9	7.8	8.1	1.6	0.3	10.8	10.5	0.3	2.7	-1.4
Malaysia	7.0	8.0	13.0	15.0	21.0	25.0	29.0	39.1	23.2	20.1
Philippines	1.3	5.3	0.7	0.9	2.0	5.3	7.1	4.2	2.1	-0.9
Singapore	11.0	11.7	21.8	29.0	33.2	35.5	39.3	27.3	16.6	15.0
South Korea	8.0	5.4	11.9	28.2	15.0	5.4	5.9	-6.4	16.3	-1.3
Taiwan	18.9	26.4	30.5	19.7	17.6	26.3	33.0	24.6	31.0	32.2
Thailand	5.1	4.7	4.8	2.8	-7.6	2.3	14.1	-0.2	10.0	5.0
Vietnam	0.7	-0.6	-1.9	-1.0	-0.6	-0.2	-7.0	-9.2	-5.2	-5.0

Note: * = based upon Egyptian financial year (July-June).
Source: HSBC

HSBC

US

Enough adjustment?

The official recession may soon be over. Consumers have cut back enough, as saving ratios have climbed to high enough levels, as long as asset prices can stabilize. On this front, stock prices have risen while house prices are still falling, but housing valuations appear cheap enough that a bottoming is in sight.

We stick with our view that GDP could rise as early as the second quarter, building up some strength in the second half of the year, but it will be a jobless recovery for a while, so unemployment will keep rising to nearly 10%. This should set the stage for a sizable decline in core inflation in 2010, down to under 1%. As a result, the Fed will not need to raise rates in 2010, providing a bullish backdrop for 10-year note yields despite the recent sell-off in response to deficit concerns. This will help keep mortgage rates low.

The loosening of financial conditions has been more than we anticipated over the past three months, and we have taken out our “double-dip recession” scenario for the first half of 2010, and now look for slight growth rather than a slight decline. This has had the effect of raising our 2010 year-average forecast from 0.5% to 1.9%. However, 2010 growth will nevertheless be constrained and below trend, because significant financial headwinds remain and deleveraging will continue (but not enough to produce another recession, in our view).

Much of the upgrade to 2010 growth, however, is likely to be productivity-led, so we have not changed our unemployment forecasts much. Indeed, payrolls could stay negative for much of this year and not stabilize until later in 2010, keeping wage growth and core inflation very low.

Ian Morris
Economist
HSBC Securities (USA) Inc.
+1 212 525 3115
ian.morris@us.hsbc.com

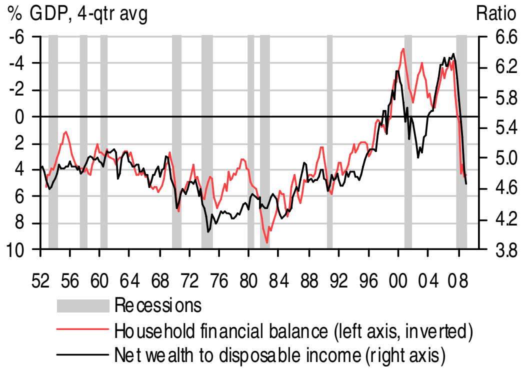
Ryan Wang
Economist
HSBC Securities (USA) Inc.
+1 212 525 3181
ryan.wang@us.hsbc.com

% q-o-q annualised

	2008	2009f	2010f	Q1 09	Q2 09	Q3 09f	Q4 09f	Q1 10f	Q2 10f
Consumer spending	0.2	-0.3	2.1	1.6	0.3	3.0	2.0	2.0	2.0
Government consumption	2.9	2.4	4.8	-3.5	4.0	7.0	8.0	5.0	5.0
Private fixed investment	-5.0	-19.9	-7.2	-37.3	-17.2	-7.4	-9.0	-8.8	-3.1
Housing	-20.8	-22.2	0.6	-38.7	-25.0	2.0	5.0	2.0	2.1
Stockbuilding (ppt contribution)	-0.3	-0.3	0.4	-2.3	0.9	0.9	0.3	0.3	-0.3
Domestic demand	-0.3	-2.7	2.1	-3.8	-3.8	-2.6	-0.5	1.9	2.4
Exports	6.2	-18.8	-10.0	-28.7	-12.5	-33.3	-14.9	-4.9	-2.3
Imports	-3.5	-20.0	-6.1	-34.1	-19.3	-15.9	-18.3	1.9	1.7
GDP (year)	1.1	-1.9	1.9	-2.5	-2.9	-2.3	0.1	1.9	2.0
GDP (% quarter annualised)	-	-	-	-5.7	1.1	2.2	3.3	1.2	1.4
Industrial production (% year)	-2.2	-10.1	0.3	-11.6	-12.2	-9.9	-6.4	-1.1	1.0
Unemployment (%)	5.8	9.1	9.8	8.1	9.0	9.5	9.7	9.8	9.8
GDP deflator (% year)	2.2	1.2	0.7	2.1	1.5	0.6	0.7	0.2	0.7
Consumer prices (% year)	3.8	-0.6	0.8	0.0	-1.0	-1.9	0.3	1.0	0.9
Employment costs (% year)	3.0	2.0	2.0	1.1	2.5	2.0	2.0	2.0	2.0
Current account (USDbn)	-654	-260	-104	-293	-236	-289	-223	-184	-171
Current account (% GDP)	-4.6	-2.0	-1.2	-2.1	-1.5	-2.5	-2.0	-1.8	-1.7
Budget balance (USDbn)	-492	-1882	-1346	-	-	-	-	-	-
USD effective (1990 = 100)	83.9	88.6	88.5	92.1	87.3	86.8	88.0	88.0	88.0
3-month money (%)	2.9	0.8	0.8	1.4	0.6	0.7	0.7	0.7	0.7
10-year bond yield (%)	3.4	3.1	2.5	2.7	3.5	3.3	3.0	2.5	2.5

Source: HSBC

Household financial balance and net wealth-to-income

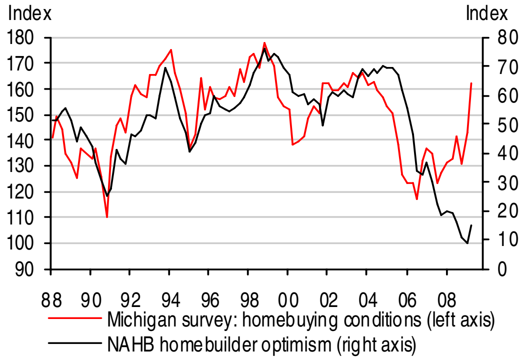


Source: Haver Analytics, Federal Reserve

Household finances close to where they should be based on consumer wealth

- Household net worth relative to disposable income continued to slip in Q1, falling to 4.7 from 4.9 in Q4 08
- Given that equity prices bottomed in early March, the downward adjustment to household wealth may be nearly complete, assuming that home price declines are in the process of slowing down
- This in would in turn suggest that the upward adjustment in household saving may also be close to done, again on the assumption that asset prices can stabilize

Home-buying conditions and homebuilder optimism

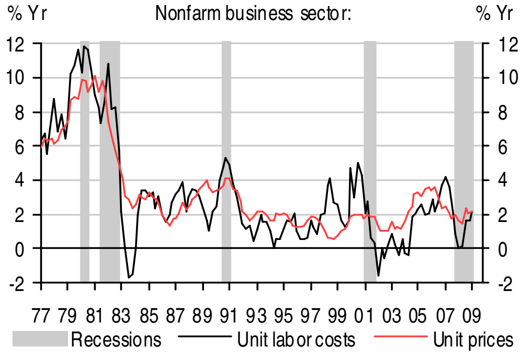


Source: University of Michigan Survey of Consumers, National Association of Homebuilders

Homebuilder optimism may be starting to get a lift

- According to the University of Michigan survey, households have become increasingly positive on home-buying conditions since last October
- The key factors cited include low prices with good buys available, along with low interest rates. The latest Beige Book indicated an uptick in home sales in eight out of 12 districts. Real estate agents also pointed to declining house prices and low rates, along with the tax credit for first-time home buyers
- Homebuilder optimism is taking longer to recover but the NAHB has doubled from the all-time low of eight back in January. Builders are seeing more prospective buyer traffic and are less pessimistic about sales prospects. As a result, new construction activity appears to have stabilized, based on the recent housing starts and building permits data.

Unit labor costs and unit prices



Source: Haver Analytics, Bureau of Labor Statistics

Low unit labor costs should help keep a lid on inflation

- Productivity growth in the US has been relatively strong, running at 1.9% year-on-year through Q1. Hourly compensation growth has been moderate and should remain so, given rising unemployment
- These forces have helped keep unit labour costs under wraps, running at around 2% year-on-year
- Low wages and the large amount of spare labour capacity should put downward pressure on prices, and we expect core inflation to fall below 1% in 2010

HSBC

Canada

Primordial soup

A persistent global recession remains a thorn in the side of the Canadian economy. The main culprit remains loss of demand from the US, but the global nature of the downturn means that this demand is not being replaced by strength in other areas of the world. Domestic demand is still hampered by an uncertain consumer and businesses that keep shedding capacity – that is, jobs – and inventory.

But as the economy enters the second half of 2009, there are signs of economic stabilization. Of particular note, existing home sales have bounced back to pre-recession levels. Commodity markets are once again showing signs of life. Recent bankruptcies in the auto sector are expected to open up on a more stable production platform in the near future. Business and consumer confidence have both improved. And of course the potential for US economic recovery in H2 2009 will provide the cover story for Canada.

Having driven overnight rates down to 25bp and pledged to keep them there until the end of Q2 2010, the Bank of Canada has largely removed the guesswork. With rate policy having reached its boundary, speculation has circulated about a potential program of quantitative easing. Despite the onset of deflation, continued recession and a determined bid in the Canadian dollar that might scupper a resurgence in business confidence, we feel the potential for QE is remote.

Markets are fickle, and the rally in the Canadian dollar may end as quickly as it began. Deflation is transitory and by the BoC's own forecasts, the economy is performing ahead of plan. Financial-market recovery is clearly under way and the banking sector is stable.

Stewart Hall*
Economist
HSBC Securities (Canada) Inc.
+1 416 868 7523
stewart.hall@hsbc.ca

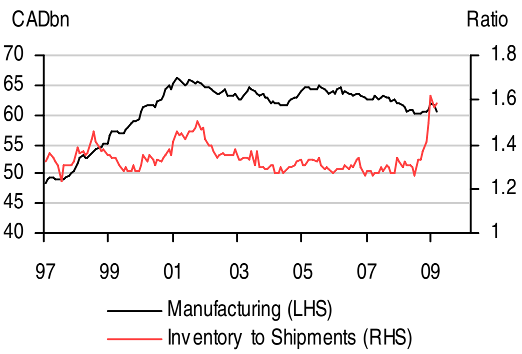
*Employed by a non-US affiliate of HSBC Securities (USA) Inc, and is not registered/ qualified pursuant to NYSE and/ or NASD regulations

% Year

	2008	2009f	2010f	Q1 09	Q2 09	Q3 09f	Q4 09f	Q1 10f	Q2 10f
Consumer spending	3.0	-1.8	0.3	-0.8	-1.8	-2.5	-1.9	-1.1	-0.1
Government consumption	3.7	2.8	5.6	2.0	1.7	3.2	4.5	6.2	6.7
Investment	0.9	-11.7	-3.5	-9.4	-11.9	-14.0	-11.5	-6.7	-4.4
Stockbuilding (% GDP)	0.9	-0.6	-0.1	-0.4	-0.9	-0.6	-0.4	-0.4	-0.2
Domestic demand	2.4	-4.5	1.0	-3.3	-5.3	-5.7	-3.9	-0.8	1.0
Exports	-4.7	-17.1	-3.2	-14.8	-17.4	-19.1	-17.0	-8.7	-4.5
Imports	0.8	-20.6	-2.9	-17.0	-21.6	-23.7	-20.0	-9.1	-3.9
GDP	0.4	-2.5	1.1	-2.1	-3.1	-3.0	-1.9	-0.1	1.2
GDP (% quarter annualised)	-	-	-	-5.4	-3.6	0.7	0.8	1.6	1.6
Industrial production	-4.1	-7.9	1.4	-8.0	-9.2	-8.8	-5.8	-0.7	2.0
CPI	2.4	0.4	1.7	1.2	-0.3	-0.5	1.3	1.7	2.0
Average earnings	2.9	2.4	1.3	2.2	2.5	2.6	2.2	1.9	1.2
Unemployment (%)	6.2	8.5	9.4	7.6	8.3	8.8	9.3	9.4	9.4
Current account (CADbn)	8.1	-21.6	3.0	-9.1	-5.0	-5.0	-2.5	-2.0	-0.5
Trade account (CADbn)	46.9	10.6	30.4	0.5	3.1	2.8	4.2	4.9	6.5
Budget balance (CADbn)	-2.0	-50.0	-30.0	-	-	-	-	-	-
CAD/USD	1.08	1.18	1.20	1.26	1.16	1.15	1.20	1.20	1.20
3-month money (%)	3.2	0.5	0.7	1.0	0.6	0.4	0.4	0.4	0.4
10-year bond yield (%)	3.4	3.2	3.6	2.7	3.4	3.4	3.5	3.5	3.6

Source: HSBC

De-stocking to continue

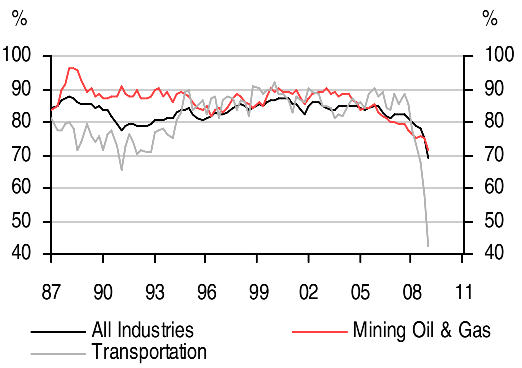


Source: Thomson Financial Datastream

Right sizing in keeping with the themes of recession.

- Inventories remain high. Goods producers have been working towards reducing stocks to a level more in keeping with the downturn in both domestic and external demand.
- The auto sector bankruptcies of Q2 are also expected accelerate the run down in inventories.
- The de-stocking process is expected reduce GDP by 1.5 percentage points in 2009 and continue to act as an economic drag into 2010.

Falling off a cliff. Capacity utilization rates have sunk to new historical lows

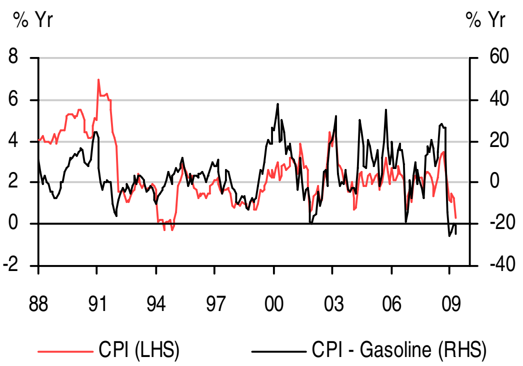


Source: Thomson Financial Datastream

Running at less than ¾ speed.

- It is reasonable to assume that some of the capacity that has since been idled has in fact been lost for good. The restructuring in the auto sector is a case in point, with the view that a good share of the capacity losses will in fact prove permanent. The various auto sector bankruptcies will have accelerated this adjustment.
- The other side of the capacity story relates to global demand. Metals and mining have seen capacity being hit by the broader shift into recession across the economy.
- Yet we can reasonably expect to see capacity brought back on-line in the commodity sector as we see prices for many commodities move higher.

Transitory deflation



Source: Thomson Financial Datastream

CPI YoY is expected to decline in Q2 by -0.3% and Q3 by -0.5%.

- The great bulk of the current deflation story is the base effect created by the rapid surge in gasoline prices in 2008 followed by the equally impressive crash in 2009.
- From the standpoint of consumer inflation expectations, as petrol is a high frequency purchase it tends to reinforce pricing trends in the mind of the consumer.
- Inflation has turned to deflation, with both Q2 2009 and Q3 2009 forecast to see outright price declines. And with the economy running at less than ¾ speed (capacity utilization rates hit 69.3% in Q1 2009) inflation is expected to remain benign. But gasoline prices are once again on the march, heading higher into the 2009 summer driving season.

Mexico

An elusive target

The consensus forecast for 2009 GDP growth remains fluid. We revised our 2009 projection to -5.9% in May from- 3.3% previously, and the consensus figure compiled by the central bank later converged on to our projection (surveyed growth rate of -5.8%). At present, there are more negative views than our own, and we certainly recognize the downside risks to our projection.

The Q1 2009 GDP data showed a strong decline of 8.2% in year-on-year terms, and we estimate that the annual rate of contraction could actually accelerate to 9.9% in the second quarter. The economy suffered a double whammy in the second quarter because of seasonal factors (Easter Week effect) and the impact of the measures taken to counter the AH1N1 virus outbreak. We estimate that this rate of contraction may continue at a 5.5% pace in Q309, before moving towards zero growth in Q4 2009.

Fiscal issues have taken centre stage due to fears of a downgrade by rating agencies. Lower oil prices and production imply a fiscal deterioration which is difficult to solve without revisiting oil industry and fiscal reforms. The former reform is necessary to increase oil investment and production, and the second to raise non-oil revenues. Given that these may prove unpopular from a political perspective, progress may be difficult on this front, risking a one-notch downgrade.

Inflation is declining slowly and monetary policy may become more conservative. We look for inflation to reach 4.1% by end-2009 given that the exchange rate has been relatively stable, but we do not rule out some further bouts of volatility here, with implications for monetary policy in turn. However, in absence of these pressures, we expect a further rate reduction of 25bp in July, to reach 4.5% at end-2009.

Sergio Martin*
Economist
HSBC México, S.A
+52 55 5721 2164
sergio.martinm@hsbc.com.mx

*Employed by a non-US affiliate of HSBC Securities (USA) Inc, and is not registered/ qualified pursuant to NYSE and/ or NASD regulations

% Year

	2005	2006	2007	2008	2009f	2010f
Private consumption	4.8	5.7	3.9	1.5	-6.5	1.6
Public consumption	2.4	1.7	2.1	0.6	3.7	2.5
Gross capital formation	7.5	9.8	7.2	4.9	-9.2	2.1
GDP	3.1	4.9	3.6	1.3	-5.9	2.6
Industrial production	2.6	5.3	3.1	-0.7	-8.9	2.9
Unemployment (%)	3.8	4.3	4.8	4.9	8.4	6.6
Consumer prices*	3.3	4.1	3.8	6.5	4.1	3.6
Exports (USDbn)	214.2	249.9	271.9	291.3	206.5	221.7
Imports (USDbn)	221.8	256.1	281.9	308.6	225.9	242.0
Current account (USDbn)	-4.4	-4.4	-8.2	-15.7	-16.3	-20.6
Current account (% GDP)	-0.5	-0.5	-0.8	-1.4	-1.9	-2.2
Budget balance (% GDP)	-0.1	0.1	0.0	-0.1	-2.3	-2.2
MXN/USD	10.8	11.0	10.9	11.4	13.9	13.8
3-month money (%)	9.3	7.3	7.4	7.9	5.4	5.3

Note: * = end-year,
Source: HSBC

HSBC

Brazil

The crisis in the rear mirror

The data are confirming our view that a gradual but steady recovery began in Brazil in Q2 2009. Consumption should sustain the recovery, as wealth destruction has been negligible in Brazil, real income growth has been safeguarded by falling inflation and the rise in unemployment has been relatively mild.

The Q1 2009 GDP data showed a second seasonally adjusted quarterly decline, of 0.8%, after the 3.6% slide in Q4 2008, which tends to confirm the consumption-led recovery. Both household and government consumption, which together account for 78% of Brazilian GDP, produced positive results on both a year-on-year and a quarterly basis.

Fixed-asset investment plunged 12.6% q-o-q and 14.0% y-o-y, more than offsetting the positive contribution of consumption. That decline should moderate by the end of the year, when we expect some of the slack in the economy to be taken up. We expect the high frequency data to show a string of positive monthly readings in the second half of 2009, although the year-on-year readings will remain in negative territory, given the high basis of comparison from Q3 2008.

Despite this steady recovery, CPI should remain close to the central bank's target, given ample spare capacity and the recent appreciation of the Brazilian real. We have lowered our inflation forecast for 2009 to 4.4% from 4.6% previously. The persistence of low capacity utilisation will enable the monetary policy committee to implement some additional easing, and we expect the Selic rate to reach 9.0% in July, remaining there until the end of the year. This would mean a reduction of some 475bp from the peak of the rate cycle and a record low real interest rate in modern Brazilian history. The fiscal position, meanwhile, remains on track, with the lower primary surplus being partly offset by reduced interest payments on public debt – about 30% of domestic public debt is indexed to the monetary policy rate.

André Loes*
Economist
HSBC Bank Brasil S.A.
+55 11 3371 8184
andre.a.loes@hsbc.com.br

*Employed by a non-US affiliate of HSBC Securities (USA) Inc, and is not registered/ qualified pursuant to NYSE and/ or NASD regulations

% Year

	2005	2006	2007	2008	2009f	2010f
Private consumption	4.5	5.3	6.3	5.4	0.7	3.3
Gross capital formation	3.6	9.8	13.5	13.8	-8.7	7.3
GDP	3.2	4.0	5.7	5.1	-0.3	4.1
Industrial production	3.1	2.8	6.0	3.1	-7.0	8.0
Unemployment (%)	9.9	10.0	9.3	7.9	8.9	8.5
Consumer prices*	5.7	3.1	4.5	5.9	4.4	4.8
Exports (USDbn)	22.6	16.5	16.6	23.2	-17.9	5.4
Imports (USDbn)	17.1	24.1	32.0	43.6	-19.8	12.2
Current account (USDbn)	14.0	13.6	1.6	-28.3	-15.5	-27.4
Current account (% GDP)	1.6	1.3	0.1	-1.8	-1.1	-1.8
Budget balance (% GDP)	-3.0	-2.9	-2.2	-1.5	-2.4	-2.0
BRL/USD	2.39	2.16	1.90	1.90	2.13	2.19
3-month money	19.0	14.8	11.7	12.7	9.3	9.0

Note:* Year end. Source: HSBC

HSBC

Argentina

With a little help from my friends

A significant part of the external shock that hit Argentina has been reversed in the past three months. Since middle March, soy prices have risen by over 45% and the Brazilian real strengthened from 2.3 to 1.9 per dollar, greatly improving the Argentine external account estimates. Those changes – reflecting a more encouraging view of the global economy – imply better growth forecasts, especially for 2010.

Nevertheless, uncertainties remain. The June mid-term elections have become a test for the Kirchner administration. Though our base scenario includes a victory for the government in the key province of Buenos Aires, the vote in the interior of the country – strongly affected by conflict with farmers – could cost the government its majority in the lower chamber, which it now holds with close allies.

In addition, the pace of fiscal expenditure – outlays are growing twice as fast as revenues – and wage inflation inertia remain issues that need to be addressed after the election to achieve a sustainable growth path. Though we expect some fiscal restraint, we believe most of the adjustment will take place through devaluation rather than significantly decelerating public expenditure.

More uncertainties lie in the willingness and ability of the government to resume access to the capital markets and to re-establish closer ties with the IMF, two factors that are linked to some extent. Nevertheless, potential debt management operations could conceivably reduce by half the dollar-denominated financial needs for 2010-2012, leaving most of the rest in official creditors' hands, that being a relatively easy rollover. Therefore, we deem a credit event as unlikely in the near future. In any case, the improved external environment leads us to raise our 2010 growth expectation to 2.9% from the previous estimate of 1.2%.

Javier Finkman*
Economist
HSBC Bank Argentina S.A
+54 11 4344 8144
javier.finkman@hsbc.com.ar

Ramiro D Blázquez*
Economist
HSBC Bank Argentina S.A
+54 11 4348 5759
ramiro.blazquez@hsbc.com.ar

*Employed by a non-US affiliate of HSBC Securities (USA) Inc, and is not registered/ qualified pursuant to NYSE and/ or NASD regulations

% Year

	2005	2006	2007	2008	2009f	2010f
Consumption	8.9	7.8	9.0	6.1	-2.9	3.7
Gross capital formation	22.7	18.2	13.6	8.2	-13.1	5.9
GDP	9.2	8.5	8.7	5.5	-2.2	2.9
Unemployment (%)	11.6	10.2	7.5	8.0	10.7	9.2
Industrial production	8.0	8.4	7.5	3.8	-3.8	3.0
Consumer prices*	12.3	9.8	17.6	21.1	16.5	18.0
Exports (USDbn)	40.0	46.5	55.9	70.0	56.2	61.2
Imports (USDbn)	28.7	34.2	44.8	57.4	42.3	53.7
Current account (USDbn)	5.6	8.0	7.1	7.8	9.0	2.4
Current account (% GDP)	3.1	3.8	2.7	2.4	3.0	0.8
Budget balance (% GDP)	1.8	1.8	1.1	1.4	-0.3	0.6
ARS/USD	2.94	3.08	3.12	3.19	3.93	4.72
1-month money (%)*	4.8	6.7	8.2	11.6	12.9	14.5

Source: HSBC. *Previous methodology estimates

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Chile

Reaping the fruits of good behaviour

Economic activity continues to show the effects of the global financial crisis. In Q1, GDP contracted 2.1% y-o-y, led by consumption, exports and investment. The latest result for the monthly GDP proxy (IMACEC) showed a 4.6% y-o-y drop in April, well below the gloomiest forecasts, for about a 3.6% decline y-o-y, according to the BCCH survey. In addition, the seasonally adjusted series shows that economic activity has yet to level out, with a 0.7% m-o-m decline. May CPI fell 0.3% m-o-m, highlighting that deflationary trends remain unabated. As a matter of fact, on the back of its openness and a small number of administered prices, Chile has shown the most rapid process of disinflation among Latin American countries. Accordingly, annual inflation has dropped from 9.9% in October 2008 to the current 3%, in line with the central bank's mid-target rate.

Chile has aggressively loosened its monetary policy stance this year, cutting its target rate by 700bp, and is also carrying out a sizeable fiscal stimulus. These expansive policies, combined with the rebound in copper prices, should place the economy back on the track of growth starting in Q3. Thus, even though we expect GDP to drop 1.1% in 2009, we believe output could end the year rising at an annualized pace of almost 13%.

Consequently, while there is some room for further monetary easing, the loosening cycle may now have drawn to a close following the latest decline in the policy rate to just 0.75%.Finally, the significant fall in imports should lead to an improvement of the current account deficit in 2009, which we forecast at 0.4% of GDP. Following a pick-up in domestic consumption, the external gap should widen, climbing to a 2% of GDP deficit in 2010.

Ramiro Blazquez*
Economist
HSBC Bank Argentina, S.A
+54 114348 5759
ramiro.blazquez@hsbc.com.ar

*Employed by a non-US affiliate of HSBC Securities (USA) Inc, and is not registered/ qualified pursuant to NYSE and/ or NASD regulations

% Year

	2005	2006	2007	2008	2009f	2010f
Private consumption	7.4	7.1	3.9	4.3	-1.4	3.2
Fixed investment	23.9	2.3	12.0	19.5	-12.0	6.0
GDP	5.6	4.6	4.7	3.2	-1.1	2.5
Industrial production	6.0	3.3	6.0	-0.2	-3.5	1.2
Unemployment (%)	9.3	8.0	7.0	7.7	10.2	9.8
Consumer prices*	3.7	2.1	7.8	7.1	0.1	3.0
Exports (USDbn)	41.3	58.0	67.6	66.5	54.1	58.4
Imports (USDbn)	30.5	35.8	43.9	57.6	46.1	51.8
Current account (USDbn)	1.0	6.8	7.2	-3.4	-0.7	-3.0
Current account (% GDP)	0.8	4.6	4.4	-2.0	-0.4	-2.0
Budget balance (% GDP)	4.6	7.7	8.8	5.2	-2.9	-3.0
CLP/USD	552	534	519	538	576	619
3-month money (%)**	4.5	5.3	6.5	8.3	1.3	3.4

Note: * = end-year; ** = end-year 90-day deposit rate
Source: HSBC

HSBC

Eurozone

Playing catch-up

The contraction in GDP in the Eurozone has so far been deeper than in the US and UK, but in many ways the Eurozone still has some catching up to do. The inventory adjustment, particularly in Germany, is less advanced. Job losses, except in Spain and Ireland, are way behind the collapse in activity. Meanwhile consumer spending, while outperforming this year, appears set to fade in 2010. The slower rate of ECB policy rate reductions and slower pass-through by the banks means that households in the likes of Italy and Spain (where variable rate mortgages are the norm) will increasingly see the benefit of sharply lower interest payments. There will be greater pass-through in the Eurozone during the rest of this year but the impact on consumption is expected to be dominated by the ongoing rise in unemployment. Our growth outlook is virtually unchanged from our last quarterly update. Our reduced 2009 forecast simply reflects the worse-than-expected Q1 GDP. We continue to expect GDP growth to turn mildly positive in Q3 as exports and industrial production start to expand again and the infrastructure element of the French and German fiscal packages start to kick in. We continue to see 2010 growth around zero, albeit with an improvement over the course of the year. On rates, the ECB's refi rate appears set to remain at 1% for at least the next year. Although we expect the output gap to stay very large, we have pencilled in a very modest rate rise (50bps) in late 2010 in what would be a nod towards normalisation from an exceptionally low level.

Janet Henry*
Economist
HSBC Bank plc
+44 20 7991 6711
janet.henry@hsbcib.com

Astrid Schilo*
Economist
HSBC Bank plc
+44 20 7991 6708
astrid.schilo@hsbcib.com

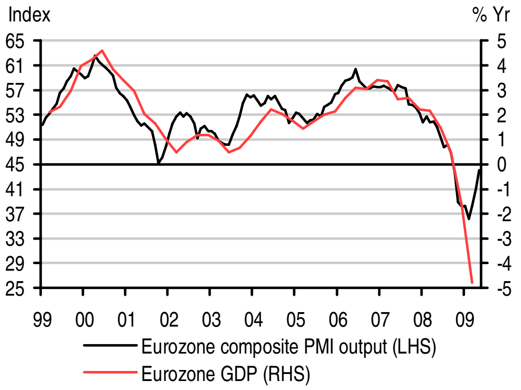
*Employed by a non-US affiliate of HSBC Securities (USA) Inc, and is not registered/ qualified pursuant to NYSE and/ or NASD regulations

% Year

	2008	2009f	2010f	Q1 09	Q2 09	Q3 09f	Q4 09f	Q1 10f	Q2 10f
Consumer spending	0.3	-1.0	-0.5	-1.1	-0.9	-1.0	-0.8	-0.6	-0.7
Government consumption	1.9	2.0	2.2	1.7	1.6	2.0	2.4	3.0	2.5
Fixed investment	-0.3	-9.3	-1.4	-10.4	-11.0	-10.1	-5.7	-2.6	-1.0
Final domestic demand	0.5	-2.2	-0.1	-2.7	-2.7	-2.4	-1.2	-0.2	-0.1
Stockbuilding (% GDP)	0.0	-0.6	-0.4	-0.5	-0.6	-0.5	-0.5	-0.3	-0.3
Domestic demand	0.6	-2.8	0.1	-3.1	-3.0	-3.1	-2.1	0.0	0.3
Exports	0.9	-15.5	0.2	-15.5	-17.4	-17.7	-11.2	-3.0	0.0
Imports	1.0	-12.1	-0.3	-11.7	-12.8	-14.0	-9.7	-2.5	-0.4
GDP	0.6	-4.3	0.1	-4.8	-5.1	-4.7	-2.7	-0.4	0.2
GDP (% quarter)	-	-	-	-2.5	-0.6	0.1	0.3	-0.2	0.0
Industrial production	-1.7	-15.6	0.8	-18.7	-18.6	-15.5	-9.3	-1.6	1.6
Unemployment (%)	7.6	9.7	11.3	8.7	9.5	10.1	10.6	11.0	11.3
Wages	3.6	3.1	2.6	3.5	3.1	2.9	2.8	2.7	2.7
Inflation	3.3	0.5	1.3	1.0	0.2	-0.1	0.9	1.4	1.4
M3	9.5	4.0	3.8	5.6	4.0	3.5	3.0	3.0	3.5
Current account (% GDP)	-1.0	-1.2	-1.0	-	-	-	-	-	-
Budget balance (% GDP)	-1.4	-5.7	-6.5	-	-	-	-	-	-
Debt (% GDP)	67.4	75.6	83.1	-	-	-	-	-	-
ECB Refi rate	2.50	1.00	1.50	1.25	1.00	1.00	1.00	1.00	1.00
3-month money (%)	4.4	1.4	1.6	1.6	1.1	1.1	1.1	1.2	1.4
10-year bond yield (%)	4.2	4.0	3.4	3.6	3.7	3.9	3.8	3.2	3.2
USD/EUR*	1.39	1.50	1.50	1.33	1.40	1.45	1.50	1.50	1.50

Source: HSBC
Note: * weighted average of the 'Big 4'

Contraction in GDP to ease sharply in Q2

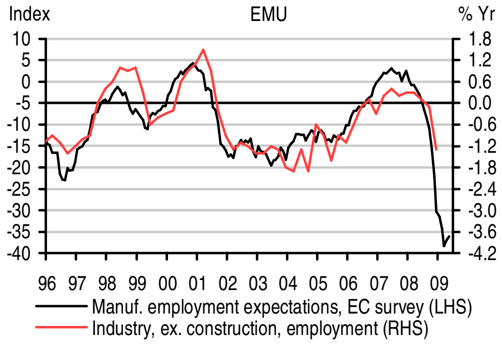


Source: Markit Economics, Eurostat

PMIs and GDP

- As elsewhere, the industrial recession in the Eurozone is showing signs of abating. Industrial production fell 7.6% q-o-q in Q1 but the manufacturing PMI recovered strongly in April and May. The new orders/stock outstanding ratio suggests this trend will continue in the next couple of months.
- GDP contracted for a fourth consecutive quarter in Q1 and at -2.5% q-o-q it was the worst yet. Another much more modest decline (-0.5% q-o-q) is on the cards for Q2.
- A much smaller drag from the inventory adjustment, as well as a pick up in public investment, in France and Germany in particular, could see GDP turn mildly positive in Q3.

Many more job losses ahead

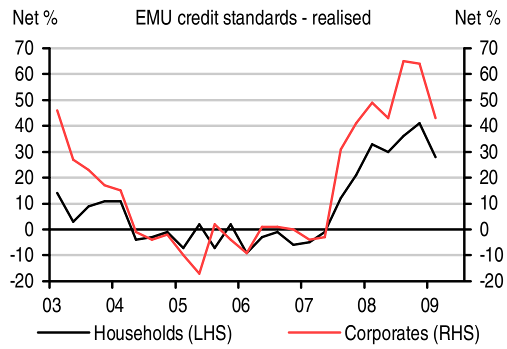


Source: European Commission, Thomson Financial Datastream, Eurostat, and HSBC

Unemployment and consumption

- Job losses in the Eurozone have started to pick up, with the unemployment rate having risen to 9.2% in April from a trough of 7.2% in March 2008.
- However, the extent of the labour adjustment is someway behind that of the US and UK, partly because of government policies aimed at keeping workers in their jobs for longer.
- Together with the sharp decline in inflation, such policies have helped to limit the decline in consumer spending in several large Eurozone economies, where there is also less pressure for a household balance sheet adjustment. Nonetheless, the delayed rise in unemployment will be a drag on consumption throughout 2010.

Credit standards no longer being tightened as aggressively



Source: ECB Bank Lending survey

Interest rates and bank lending

- The ECB's policy rate (the refinancing rate) was cut to 1% in May and although the council has not entirely ruled out further cuts, we believe that this is likely to be the trough.
- The latest bank lending survey showed that the number of banks still tightening standards has fallen a little and the ECB's latest moves to extend the maturity provision to 12 months and make EUR60bn of covered bond purchases are aimed at supporting the banks further.
- However, in the latest ECB meeting, Mr Trichet urged banks to take full advantage of government measures to support their recapitalisation, in order to support lending in the medium term.

HSBC

Germany

Hung-over – without going to the party

Going into the crisis, relatively low levels of debt led many to believe that Germany was well placed to weather the storm. In fact, we forecast a GDP decline of 5.9% in 2009, one of the worst in the G7 and only surpassed by our forecast of a 6.3% decline in Japanese GDP. Moreover, this is considerably worse than the experience of those at the epicentre of the crisis – the 'housing-bubble' economies of the US and UK.

This is accounted for by Germany's reliance on net trade: 85% of the forecast slump in growth in 2009 [is this our forecast or an industry forecast?] (5.1 percentage points of our expected decline) is due to an expected 17% decline in exports and a 9% decline in imports. Such weakness is prompting a sharp contraction in domestic business investment – machinery and equipment investment fell by 16.2% q-o-q in Q1.

Consumer spending has so far held up, largely due to support from various fiscal packages, but also because the collapse in activity has not yet affected German employment. However, we expect employment to decline by more than one percentage point by the end of 2009 and also in 2010. Consequently, the support from consumer spending is likely to fade by year end.

The public sector deficit is likely to increase to 4.6% (2009) and 6.1% (2010) of GDP.

Overall, whilst forward looking indicators imply that the worst has passed, weakness in investment and net exports will continue to be a drag in the coming quarters. Whilst the *level* of activity should stabilise, we do not expect a significant recovery through 2010.

Lothar Hessler*
Economist
HSBC Trinkaus & Burkhardt AG
+49 211 910 2906
lothar.hessler@hsbctrinkaus.de

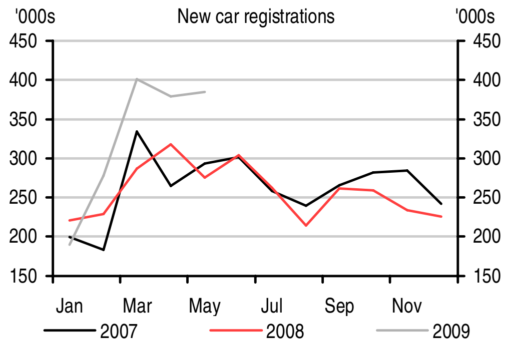
*Employed by a non-US affiliate of HSBC Securities (USA) Inc, and is not registered/ qualified pursuant to NYSE and/ or NASD regulations

% Year

	2008	2009f	2010f	Q1 09	Q2 09	Q3 09f	Q4 09f	Q1 10f	Q2 10f
Consumer spending	-0.1	0.5	-0.1	-0.1	0.6	0.6	0.9	0.3	0.0
Government consumption	1.8	1.3	2.5	0.8	0.7	1.4	2.3	2.6	2.8
Investment	4.6	-11.2	0.2	-11.8	-11.8	-12.1	-9.2	-0.7	0.4
Machinery & equipment	5.1	-21.4	-2.5	-19.7	-22.5	-23.5	-19.9	-4.9	-2.5
Construction	2.0	-4.1	1.9	-7.3	-4.1	-3.4	-1.2	1.9	2.3
Stockbuilding (% GDP)	-0.8	0.3	0.4	0.3	0.2	0.4	0.2	0.1	0.1
Domestic demand	0.8	-0.8	0.3	-1.1	-0.1	-1.0	-1.0	0.4	0.6
Exports	2.2	-17.4	0.9	-17.5	-19.6	-19.7	-12.2	-2.1	1.3
Imports	3.9	-8.5	0.6	-7.3	-7.8	-11.2	-7.4	-1.6	1.1
GDP	1.0	-5.9	0.5	-6.9	-6.8	-6.1	-3.7	0.1	0.7
GDP (% quarter)	-	-	-	-3.8	-0.3	0.2	0.3	0.0	0.2
Industrial production	0.0	-16.9	1.7	-19.7	-19.7	-17.0	-10.6	1.7	3.0
Unemployment (%)	7.8	8.4	10.1	8.1	8.3	8.5	8.8	9.6	10.1
Average earnings	2.8	2.7	1.9	3.1	2.8	2.5	2.3	2.1	2.0
Producer prices	5.5	-3.3	0.7	0.8	-3.6	-6.0	-4.2	-1.1	1.2
Consumer prices	2.7	0.3	0.8	0.8	0.1	-0.5	0.7	0.9	0.8
Current account (EURbn)	164.9	99.3	105.0	19.3	25.0	25.0	30.0	30.0	25.0
Current account (% GDP)	6.6	4.1	4.3	3.3	4.2	4.1	5.0	5.0	4.2
Budget balance (% GDP)	-0.1	-4.6	-6.1	-	-	-	-	-	-
3-month money (%)	4.4	1.4	1.6	1.6	1.1	1.1	1.1	1.2	1.4
10-year bond yield (%)	3.9	3.4	2.9	3.0	3.4	3.6	3.5	2.9	2.9

Source: HSBC

The car scrapping scheme has been successful...

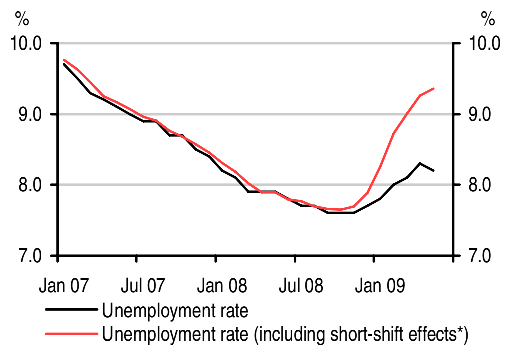


Source: Kraftfahrt- Bundesamt (KBA)

...but this is a temporary boost

- The government introduced a car scrappage scheme providing a subsidy of EUR2,500 for each new car bought if trading in a car at least nine years old. This has been successful in boosting new car registrations in Germany which were up by almost 40% to around 385,000 in the year to May, the second-best result for that month since the reunification boom in 1991. But while at a cost to the government of EUR 5bn, some of this stimulus has simply served to benefit the producers of cars imported to Germany.
- The scrapping bonus is likely to give a temporary boost to industrial production, but with the machinery and car production sectors having an almost equal weighting (each around 12.5%), we are unlikely to see sustained growth in overall industrial production until a stronger global recovery is underway.

German unemployment is distorted by the short-shift initiative...

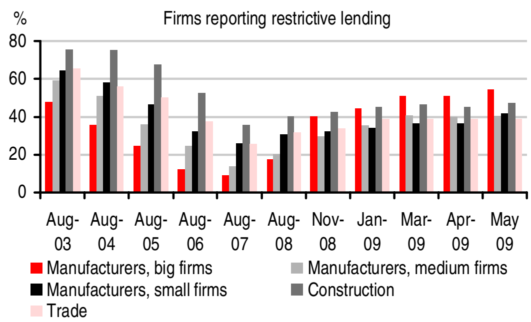


Source: Federal Labour Office, HSBC

...but this will come through in unemployment if economic activity does not rebound

- On a seasonally-adjusted basis unemployment is expected to rise to 8.4% in 2009 after 7.8% in 2008. The figure would have been considerably higher (9.4%) if those workers placed on 'short shifts' had been made unemployed.
- The 'short-shift' scheme is a government initiative which reimburses workers for around two-thirds of the income lost due to a reduction in hours worked. This encourages firms to maintain the total number of staff and instead reduce hours worked, limiting the spillover to the real economy.
- There were around 1.25 million workers on short shifts in March 2009.
- The government extended the short-shift allowance to 24 months but we are still likely to see a notable jump in the unemployment rate around the turn of the year, which will restrain consumer spending.

There are ongoing credit restrictions for corporates....



Source: ifo institute

...as issues in the banking sector remain

- Despite the recent improvement in financial markets, the percentage of companies stating that lending was restrictive has increased appreciably of late, according to the latest ifo survey. This is clearly driven by concerns about the level of capacity and the impact on profitability as conditions have been particularly tightened for the manufacturing industry.
- Moreover, there are ongoing concerns about the ownership of toxic securities in the banking sector which will continue to serve as a drag on corporate lending and thus investment.
- One example is "Landesbanken" which, at the will of the Federal Government, will have to contract its balance sheet radically by the end of 2010. The Land banks' balance sheets are to be cleaned up by setting up bad banks and removing toxic assets.

HSBC

France

Unemployment and public deficit worsen

Consumer spending held up in the first quarter of 2009 and last quarter of 2008 rising 0.2% q-o-q. In contrast, business investment declined by 3.2% q-o-q in Q1 2009 and exports by 6% q-o-q in Q1 2009. The property crisis continued to weigh on residential investment, which contracted by 1.5%. And stockbuilding made a substantial negative contribution to GDP, trimming GDP growth by 0.8 percentage points.

Destocking will continue to push economic activity down until later in the year. Destocking was particularly marked in the automobile sector and intermediate goods sectors, and is likely to spread to other sectors, particularly durable goods. In the 1993 and 1975 recessions, stockbuilding weighed on GDP growth for four straight quarters. We therefore expect a contraction in industrial production and investment until the end of 2009.

The resilience of consumer spending is attributed to fiscal stimulus measures, particularly the abolition of two of the three annual income tax payments (those scheduled for May and September) and the car-scrapping incentive. In 2010, consumer spending is expected to falter as rising energy prices and unemployment squeeze disposable income. In addition, a worsening public deficit will lead to uncertainty over future income and could push the savings rate up. We expect it to rise from 15.9% in the final quarter of 2008 to 17.5% in Q2 2010. This uncertainty will also depress demand for housing, offsetting the positive impact of lower borrowing rates. In addition, housing prices have not yet fallen enough to substantially improve household solvency. Although the stimulus plan and an end to destocking could push GDP up at the year end, it will not be enough to deliver a sustained recovery into 2010.

Mathilde Lemoine*
Economist
HSBC France
+33 1 40 70 32 66
mathilde.lemoine@hsbc.fr

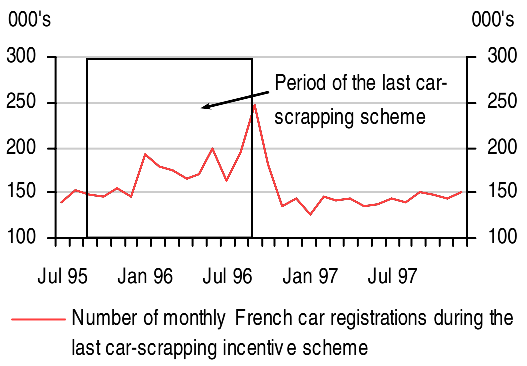
*Employed by a non-US affiliate of HSBC Securities (USA) Inc, and is not registered/ qualified pursuant to NYSE and/ or NASD regulations

% Year

	2008	2009f	2010f	Q1 09	Q2 09	Q3 09f	Q4 09f	Q1 10f	Q2 10f
Consumer spending	1.0	0.4	-0.5	0.5	0.6	0.5	0.1	-0.3	-0.8
Government consumption	1.1	2.4	2.0	1.3	2.1	2.7	3.5	4.2	2.4
Investment	0.4	-4.7	-1.2	-7.1	-7.6	-4.4	0.7	-0.2	0.7
Stockbuilding (% GDP)	0.6	-0.9	-2.6	-0.6	-1.0	-1.0	-1.0	-0.9	-0.8
Domestic demand	0.7	-1.6	0.2	-2.1	-2.5	-1.8	-0.1	0.5	0.4
Exports	-0.5	-12.5	-2.1	-12.9	-12.3	-13.7	-11.0	-5.3	-3.4
Imports	0.6	-7.9	0.2	-8.6	-8.6	-8.6	-5.8	-0.7	-0.2
GDP	0.3	-2.8	-0.4	-3.2	-3.4	-3.1	-1.4	-0.7	-0.5
GDP (% quarter)	-	-	-	-1.2	-0.6	0.1	0.3	-0.5	-0.4
Manufacturing output	-3.1	-18.0	-2.7	-18.1	-18.7	-19.9	-15.0	-7.6	-4.7
Unemployment (%)	7.4	9.8	11.3	8.7	9.8	10.3	10.6	10.9	11.2
Average earnings	3.0	2.3	2.3	2.6	2.2	2.1	2.2	2.3	2.3
Consumer prices	3.2	0.2	1.5	0.7	-0.2	-0.2	0.5	1.3	1.5
Trade account (EURbn)	-54.3	-46.7	-53.9	-12.9	-11.1	-10.9	-11.7	-12.7	-13.0
Current account (% GDP)	-1.9	-1.2	-1.7	-	-	-	-	-	-
Budget balance (% GDP)	-3.2	-7.1	-7.8	-	-	-	-	-	-
3-month money (%)	4.4	1.4	1.6	1.6	1.1	1.1	1.1	1.2	1.4
10-year bond yield (%)	4.1	4.0	3.4	3.6	3.7	3.9	3.8	3.2	3.2

Source: HSBC, Thomson Financial Datastream

Car-scrapping incentive: ...

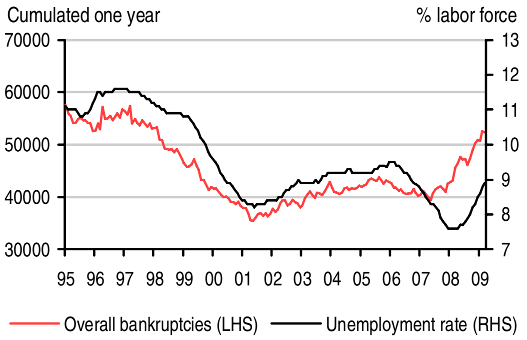


Sources INSEE, HSBC

... a temporary effect on consumer spending

- The car-scrapping incentive in France, as in Germany, is supporting the automobile industry. The average monthly increase in vehicle purchases from December 2008 to May 2009 was 3.6% compared with an average monthly contraction of 2% from January 2008 to November 2008.
- But, as revealed by previous incentive measures, this effect is only temporary and will come to an end when the current incentive plan expires in December 2009.
- The last car-scrapping incentive introduced in September 1995 showed a 33% increase in new registrations compared with the average observed in 1993. But when the initiative ended in October 1996, new registrations contracted by 31%.

Bankruptcies ...

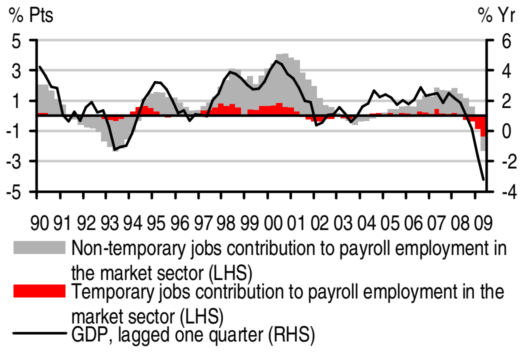


Sources: INSEE, Eurostat, HSBC

... could continue to rise

- Bankruptcies rose by almost 20% y-o-y in the Q1 2009, most notably in the construction and property sectors, where failures rose by 51% y-o-y in Q1 2009, but also in the intermediate goods and transport sectors.
- As domestic demand deteriorates, bankruptcies are likely to rise. As regards lending criteria, the latest BdF survey shows that one quarter of banks tightened their lending criteria in Q1 2009 – mainly for SMEs. In Q2 2009, the position could stabilise as 82.9% of banks surveyed said that their lending criteria remained virtually unchanged.

Job losses escalate ....



Source: Sources: INSEE, HSBC

... particularly outside the temporary sector in Q1 09

- The job losses in Q4 2008 and Q1 2009 were much higher than during the previous recessions in the 1990s and during the 1970s oil crisis: 117,300 jobs were lost in Q4 2008 and 192,500 in Q1 2009.
- As expected, job losses affected the temporary employment sector and the automobile industry first, but are now spreading to fixed-contract and permanent jobs. Although temporary employment was to blame for 80% of payroll job losses for much of 2008, it was only responsible for 42% in the first quarter of 2009.
- All in all, the unemployment rate could increase to 11.8% by the end of 2010, which is likely to restrict French domestic demand, therefore limiting the potential to improve the production capacity utilisation rate, which is currently running at 69.2%.

Italy

Signs of stabilisation but not growth

The first quarter of 2009 was a repeat of the broadly-based contraction in Q4, except of a greater magnitude. GDP fell by a massive 2.6% q-o-q, after -2.1% in Q4 and the decline in consumer spending and, particularly, exports (-11.8% q-o-q), intensified.

Signs of stabilisation have come through recently, notably in the property market and industrial production, which even eked out a monthly increase in April, albeit after a string of shockingly weak monthly declines. However, GDP is still unlikely to turn positive until Q4 at the earliest. Given the very high public-debt-to-GDP ratio, the scope for fiscal stimulus has been much more modest than in the other large Eurozone countries so, unlike France and Germany, Italy will not get a lift from public investment in the second half of this year. Italy's banks are mostly well capitalised and their lower reliance on wholesale funding and exposure to structured products means they have escaped the worst of the financial crisis. However, lending standards are tight and, given the sharp deterioration in corporate profits, investment by Italy's relatively highly indebted corporate sector is set to continue falling throughout 2009.

Many households will continue to benefit from the pass-through of lower interest rates but as the household debt-to-income ratio is low (at around 60%), the impact will not be as big as in Spain or the UK. Besides, the boost to real incomes will continue to be offset by higher unemployment. In view of the sharper than expected decline in Q1 we have lowered our 2009 GDP forecast to -5.3%. We expect a gradual recovery in the course of 2010 but the full-year figure will likely show a contraction of about 0.4%.

Janet Henry*
Economist
HSBC Bank plc
+44 20 7991 6711
janet.henry@hsbcib.com

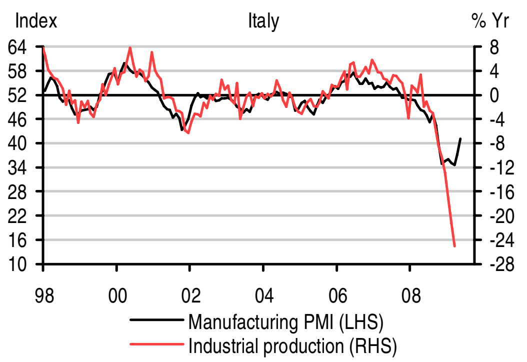
*Employed by a non-US affiliate of HSBC Securities (USA) Inc, and is not registered/ qualified pursuant to NYSE and/ or NASD regulations

% Year

	2008	2009f	2010f	Q1 09	Q2 09	Q3 09f	Q4 09f	Q1 10f	Q2 10f
Consumer spending	-0.9	-2.2	-0.2	-2.6	-2.2	-2.4	-1.6	-0.6	-0.3
Government consumption	0.6	0.3	0.5	0.8	0.1	0.2	0.3	0.4	0.6
Investment	-2.9	-12.6	-2.6	-12.6	-14.6	-13.6	-9.2	-5.4	-3.0
Stockbuilding (% GDP)	0.4	-0.1	-0.2	-0.1	-0.2	-0.1	0.0	0.0	0.0
Domestic demand	-1.3	-4.3	-0.5	-4.8	-4.8	-4.6	-3.1	-1.2	-0.5
Exports	-3.7	-19.9	0.7	-21.7	-22.7	-20.8	-14.0	-2.0	0.8
Imports	-4.5	-15.9	0.4	-17.0	-17.8	-16.7	-11.7	-2.2	0.3
GDP	-1.0	-5.3	-0.4	-6.0	-6.2	-5.6	-3.6	-1.2	-0.3
GDP (% quarter)	-	-	-	-2.6	-0.8	-0.1	0.0	-0.2	0.1
Industrial production	-3.3	-19.2	1.4	-21.1	-23.4	-20.3	-11.2	-1.4	2.9
Unemployment (%)	6.8	8.0	9.2	7.4	7.8	8.2	8.6	8.9	9.1
Hourly wage rate	3.5	2.8	2.2	3.7	2.6	2.4	2.3	2.2	2.2
Consumer prices	3.5	1.1	1.9	1.4	0.9	0.7	1.5	2.5	2.0
Current account (EURbn)	-53.6	-44.2	-41.0	-13.2	-12.0	-8.0	-11.0	-12.0	-11.0
Current account (% GDP)	-3.4	-2.9	-2.7	-	-	-	-	-	-
Budget balance (% GDP)*	-2.7	-5.8	-6.4	-	-	-	-	-	-
3-month money (%)	4.4	1.4	1.6	1.6	1.1	1.1	1.1	1.2	1.4
10-year bond yield (%)	4.7	4.8	4.3	4.4	4.4	4.3	4.2	3.6	3.6

Note: * = state sector cash balance
Source: HSBC

IP vs PMI

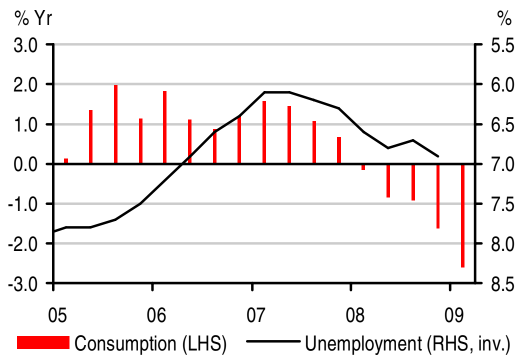


Source: Markit Economics, Thomson Financial Datastream

PMIs and production

- Following the collapse early in the year, the level of IP looks to have stabilised in April, rising 1.1% m-o-m, but annual production was still down nearly 25% y-o-y.
- The industrial decline has been driven by the weakness of domestic demand, the collapse in exports and, in Q1, the inventory adjustment which finally seemed to get underway.
- First quarter GDP was even worse than Q4 at -2.6% q-o-q, and although the decline is likely to abate markedly by mid-year, we do not expect the economy to resume expanding in q-o-q terms until 2010.

Rising unemployment is constraining consumption

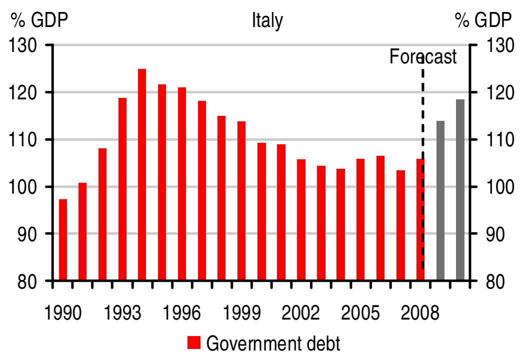


Source: Thomson Financial Datastream

Consumption and unemployment

- Consumer spending has fallen sharply over the past year but the car sales programme, which incentivised consumers to trade in old cars for less-polluting models, has supported a recovery in car sales since March and consumer confidence has revived a little.
- In addition households are benefiting from the sharp cuts in interest rates as 70% of Italy's mortgage stock is at variable rates.
- Hence the contraction in consumer spending (-1.1% in Q1) should moderate despite the ongoing rise in unemployment .

The debt stock is growing again



Source: Eurostat, HSBC forecasts

Budget deficit and debt

- Italy's planned fiscal stimulus in 2009 is very small, amounting to less than 0.2% of GDP but the loss of revenue and higher spending associated with the prolonged recession mean the budget deficit will increase markedly.
- We expect the deficit to widen to 5.8% of GDP in 2009 and more than 6% in 2010.
- Although this is a smaller deficit than many in the region, including that of France, Italy will continue to have by far the highest government debt-to-GDP ratio in the Eurozone.

HSBC

Spain

Still rebalancing

The contraction in the Spanish economy now looks worse than that experienced in the 90s, as household and corporate demand continues to contract. This trend should continue this year, although the monetary stimulus is expected to provide some relief in the second half of the year.

The contraction in private consumption slightly accelerated in the first quarter of this year (-1.7% q-o-q), most likely due to the rising unemployment rate and high mortgage rates, which still do not reflect the ECB's interest rate cuts. While mortgage rates follow the 12 month Euribor, they are only re-set once a year, so it will take some time to feed into the economy. In addition, lower interest rates are unlikely to be passed on to new mortgage products as banks have expanded their margins. Households should benefit from most of the monetary policy easing by Q4 of this year.

On the labour market, unemployment is expected to continue rising, but at a slower pace.

Investment spending is likely to continue to contract although at a slower rate. Non-performing loans are rising rapidly (434% y-o-y in Q4), mainly in the construction sector, so this is unlikely to turn around any time soon.

Spanish inflation (June -1.1% y-o-y) is now below Germany's (June -0.1% y-o-y), as both core and headline inflation are trending down. The former is linked to energy effects, while the latter is most likely due to the weakness of domestic demand. Looking forward, we believe inflation should pick up a bit, but stay below its long-term average of 2.9%.

Astrid Schilo*
Economist
HSBC Bank plc
+44 20 7991 6708
astrid.schilo@hsbcib.com

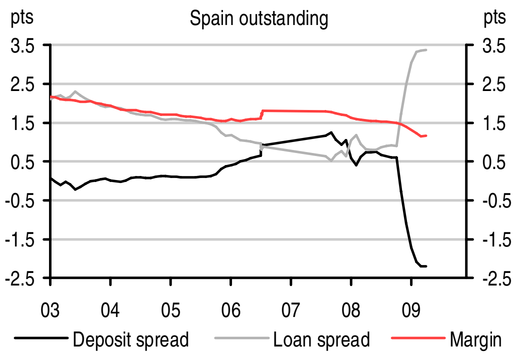
*Employed by a non-US affiliate of HSBC Securities (USA) Inc, and is not registered/ qualified pursuant to NYSE and/ or NASD regulations

% Year

	2008	2009f	2010f	Q1 09	Q2 09	Q3 09f	Q4 09f	Q1 10f	Q2 10f
Consumer spending	0.1	-4.1	-1.3	-4.0	-4.8	-4.2	-3.2	-2.2	-1.7
Government consumption	5.3	5.0	4.6	5.4	5.3	4.6	4.6	5.7	4.7
Investment	-2.8	-12.3	-1.8	-13.3	-14.1	-13.0	-8.6	-4.7	-1.8
Stockbuilding (% GDP)	0.2	-0.6	-0.8	0.1	-0.9	-1.0	-0.8	-1.2	-1.1
Domestic demand	0.2	-5.4	-0.4	-5.0	-6.4	-6.0	-4.0	-2.6	-0.7
Exports	0.7	-20.0	-1.6	-19.0	-21.8	-23.9	-14.9	-4.3	-2.5
Imports	-2.5	-22.1	-2.1	-22.3	-24.7	-25.0	-15.8	-5.1	-2.7
GDP	1.2	-3.2	-0.1	-3.0	-3.8	-3.7	-2.4	-1.0	-0.2
GDP (% quarter)	-	-	-	-1.9	-0.7	-0.2	0.3	-0.5	0.1
Industrial production	-7.5	-15.1	0.9	-21.5	-17.2	-14.0	-6.5	0.4	0.1
Unemployment (%)	11.3	19.3	21.8	17.4	19.0	20.0	20.8	21.4	21.7
Average earnings	4.8	1.9	2.1	2.0	1.7	2.0	1.9	2.1	2.3
Consumer prices	4.1	-0.6	1.3	0.5	-0.9	-1.5	-0.5	0.5	1.3
Trade account (EURbn)	-94.1	-52.0	-44.0	-14.0	-13.0	-13.0	-12.0	-11.5	-11.5
Current account (EURbn)	-104.5	-85.8	-66.0	-23.3	-22.0	-22.0	-18.5	-18.0	-16.5
Current account (% GDP)	-9.5	-8.1	-6.2	-	-	-	-	-	-
Budget balance (% GDP)	-3.8	-8.4	-8.4	-	-	-	-	-	-
3-month money (%)	4.4	1.4	1.6	1.6	1.1	1.1	1.1	1.2	1.4
10-year bond yield (%)	4.4	4.4	3.9	3.8	4.1	4.3	4.2	3.6	3.6

Source: HSBC

Banks keep rates high on deposits ...

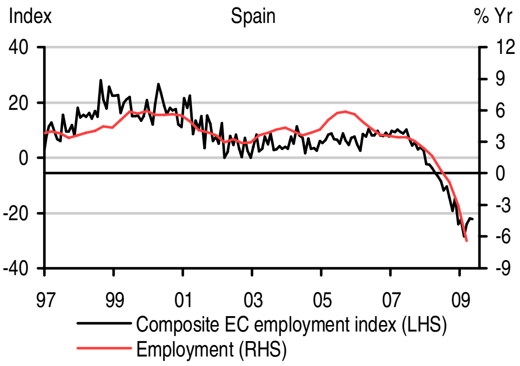


Note: spreads with respect to 3mth Euribor; deposits only with agreed maturity
Source: BoS,, HSBC

... as they need it as a funding base

- ECB rate cuts are relatively slow to feed into outstanding loan rates, which means that banks' loan spreads remain rather high on the loan side, while deposits spreads suffer. In other words, rates remain relatively high for savers and debtors.
- In the chart opposite, we're admittedly over-simplifying things. We only use deposits with an agreed maturity, and more importantly, all spreads are with respect to 3mth Euribor. Mortgages for example follow 12mth Euribor, and for corporates, the maturity spectrum is wide.
- However, it is also clear that banks keep a high loan spread on new mortgage loans, which illustrates that banks do not pass on the ECB's rate cuts in their entirety. High new deposit rates to attract retail deposits can also be observed. Checking with our banking analysts for Spain, the trend we're depicting reflects developments observed on a micro level.

Employment has been contracting ...



Source: Datastream, HSBC

... but are there some hopes of stabilisation?

- The rise in the Spanish unemployment rate has been one of the most extreme in Europe.
- Employment has fallen by 7% since its peak in Q3 2007. The decline is much more extreme for the construction sector, where employment has collapsed by 29% in the same period.
- In fact, the construction sector has eliminated more jobs in 6 quarters than it had built up in 18 quarters preceding the peak in Q3 2007.
- Given the structural changes Spain has to undergo it is difficult to be optimistic, but there is some early evidence in the survey data, especially for the construction sector, that the pace of labour shedding might be slowing.

Spain export orders recovering in line with EMU ...

Source: Markit, HSBC

... despite its lack of competitiveness

- Economists, including ourselves, have been writing about the lack of competitiveness of the Spanish economy, reflected in high unit labour costs and slow productivity.
- However, Spain's export order manufacturing PMI hasn't slumped by as much as Germany's, and is now still at the same level as Germany's.
- Another point is that the underlying volumes are much smaller for Spain than for Germany, on an absolute and relative to GDP basis. So if Spain wanted to grab some market share, it still would need to sharpen its competitiveness.
- But with a smaller export share of GDP, exports would need to expand more rapidly to support GDP growth.

HSBC

UK

This might just work

Towards the end of last year there seemed little hope for the overindebted UK economy, as a vicious cycle between the banking sector and real economy looked unbreakable. Indeed, the final quarter of 2008 and the first quarter of 2009 combined saw an unprecedented decline in real GDP.

But the policy response has been similarly unprecedented, which should give rise to some recovery in GDP by the end of the year, see *This Might Just Work* (15 April 2009), for more details.

Interest rate cuts have provided a massive boost to real disposable income. This has lowered the impact on final demand of households wanting to increase saving. In the past few months monetary policy has been extended to quantitative easing. More than anything this provided an important signal that the BoE had further ammunition beyond the zero bound in nominal interest rates. The Asset Purchase Facility has been large and pre-emptive, and the early signs are promising in terms of the improvement in confidence, asset prices and corporate bond issuance.

On top of this, sterling is still more than 20% below the peak seen in 2007. At the moment this appears to be encouraging import substitution but some recovery in world trade should see a larger stimulus from net exports.

Adding all this together we have considerably more confidence that the policy stimulus will work to offset some of the headwinds from higher debt and ongoing deleveraging in the financial sector. So these forecasts raise our outlook for GDP towards year end and lower our outlook for unemployment. We expect the BoE to ease off the monetary policy gas, raising rates to 2% by the end of next year. This is still an extremely accommodative policy rate which would not hinder a sustainable recovery.

Karen Ward*
Economist
HSBC Bank plc
+44 20 7991 3692
karen.ward@hsbcib.com

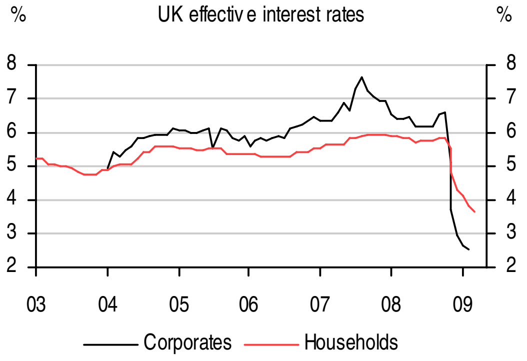
*Employed by a non-US affiliate of HSBC Securities (USA) Inc, and is not registered/ qualified pursuant to NYSE and/ or NASD regulations

% Year

	2008	2009f	2010f	Q1 09	Q2 09	Q3 09f	Q4 09f	Q1 10f	Q2 10f
Consumer spending	1.2	-3.1	-0.3	-3.0	-3.6	-3.5	-2.1	-1.1	-0.2
Government consumption	2.8	2.1	1.6	2.8	2.2	2.1	1.4	1.6	1.6
Investment	-2.5	-12.6	-1.4	-13.1	-13.6	-12.4	-11.2	-4.4	-1.8
Stockbuilding (% GDP)	-0.4	-1.1	1.1	-2.2	-1.9	-1.1	1.0	1.5	1.5
Domestic demand	0.5	-4.7	1.1	-5.7	-6.0	-4.9	-2.0	0.4	1.4
Exports	0.8	-13.4	0.2	-11.6	-15.2	-15.2	-11.4	-4.3	0.8
Imports	-0.6	-14.9	-1.6	-13.6	-16.8	-17.0	-12.0	-6.0	-0.8
GDP	0.7	-3.8	1.6	-4.9	-5.1	-3.9	-1.4	1.2	1.9
GDP (% quarter)	-	-	-	-2.4	-0.2	0.5	0.7	0.2	0.4
Manufacturing output	-2.6	-10.7	1.5	-13.1	-12.8	-11.1	-5.9	0.3	2.0
Unemployment (%) - ILO	5.7	7.7	8.7	7.0	7.6	8.0	8.4	8.6	8.7
Average earnings	3.6	1.2	3.2	0.1	1.3	1.5	2.0	3.8	3.0
RPI	4.0	-1.3	2.9	-0.1	-1.4	-2.3	-1.6	1.7	2.5
CPI	3.6	1.8	2.1	3.0	2.0	1.0	1.2	2.5	2.1
Current account (% GDP)	-1.7	-1.4	-1.1	-	-	-	-		
PSNB (% GDP)	-5.4	-13.2	-12.6	-	-	-	-		
USD/GBP**	1.44	1.61	1.61	1.43	1.65	1.60	1.61	1.61	1.61
GBP/EUR**	0.97	0.93	0.93	0.93	0.85	0.91	0.93	0.93	0.93
Base rate (%)**	2.00	0.50	2.00	0.50	0.50	0.50	0.50	0.50	1.00
10-year bond yield (%)**	4.2	3.5	3.2	3.2	3.7	3.5	3.5	3.2	3.2

Notes: *corporate capital allowance changes in April 08 is likely to affect investment spending, ** end-quarter estimates
Source: HSBC

Debt service costs have fallen dramatically ...

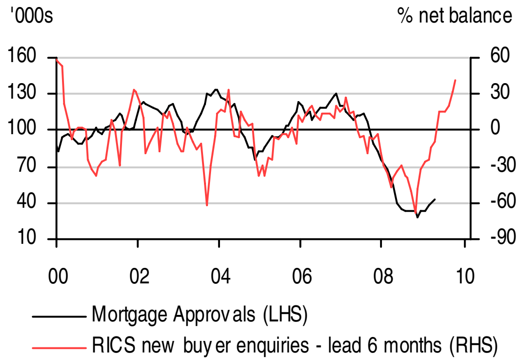


Source: Thomson Financial Datastream

... alongside the fall in BoE Bank Rate

- UK households have more debt than any other country in the G7. But the upside is that both household and corporate debt is financed on short-term interest rates. With the 525bp decline in the BoE Bank Rate, debt servicing costs have fallen dramatically and by a far greater amount than that seen in the US and Eurozone.
- In addition, the structure of the mortgage market will mean the exit from the BoE's quantitative easing programme has a more limited real economy impact. A reversal in these policies, and a potential rise in longer-term interest rates, will have a limited impact on the day-to-day debt servicing costs of UK households and corporates.

Housing demand is increasing ...



Source: Bank of England, Royal Institute of Chartered Surveyors

... although the prices will be restrained

- Households feel more confident about the economic outlook and nowhere is this more evident than in the housing market where new buyer enquiries have surged according to the RICS survey.
- There is still a question of mortgage availability but the government's lending targets, coupled with the attractive margins on new lending, should see credit conditions loosen over the course of the year and housing market activity continue to improve.

The stimulus from weaker sterling ...

Source: Thomson Financial Datastream

... could be underestimated

- While sterling has risen 15% from the low seen at the end of last year, in trade-weighted terms it is still down 21% from the peak seen in 2007.
- The UK's manufacturing sector is often underestimated. The UK is still the seventh-largest manufacturer in the world and contributes twice as much to UK GDP as financial services.
- Many investors are concerned about the sustainability of domestic demand when interest rates rise. Sterling is very unlikely to return to previous highs and growth in net trade will compensate for weaker consumer and government spending.

HSBC

Norway

Relative outperformer

The pace of contraction in Norway has been much more modest than elsewhere in Europe. First quarter GDP fell by a less-than-expected 0.4% q-o-q (-0.3% y-o-y) with stock building and government expenditure the major drags while the pace of decline in consumer spending moderated. A further contraction is expected in Q2 before the q-o-q change in GDP turns positive in Q3 due to the demand impetus from policy measures.

According to the finance ministry, the government has the most expansionary fiscal budget in more than 30 years. To curb growth in unemployment, the government plans to increase the spending of oil revenues by a further NOK9.5bn to a total of NOK130bn (3% of non- oil GDP) during the 2009 fiscal year. Government expenditure will therefore contribute positively to Norway's growth while consumption growth should show further signs of stabilization. The decline in investment, which has recently gained momentum after the very strong investment of the previous two years, is expected to continue for longer.

The Norges Bank has followed an active monetary policy, lowering the key policy rate by a total of 4.25 percentage points since October 2008 to 1.5%. Its own projections point to rates falling as low as 1% later this year, but it appears increasingly likely that the current level will be the trough given the recent news on inflation. Partly because the contraction in Norway's economy has been more modest than elsewhere, inflation has been slower to fall. Core inflation edged up to 2.9% in May, above the central bank's 2.5% target.

Janet Henry*
Economist
HSBC Bank plc
+44 20 7991 6711
janet.henry@hsbcib.com

*Employed by a non-US affiliate of HSBC Securities (USA) Inc, and is not registered/ qualified pursuant to NYSE and/ or NASD regulations

% Year

	2008	2009f	2010f	Q1 09	Q2 09	Q3 09f	Q4 09f	Q1 10f	Q2 10f
Consumer spending	1.2	-1.1	0.9	-2.2	-1.9	-0.7	0.3	0.5	0.9
Government consumption	3.8	6.3	6.1	5.0	6.1	6.9	7.3	7.2	6.4
Investment	3.8	-7.6	-0.8	-5.5	-6.5	-9.3	-9.2	-2.5	-1.0
Stockbuilding (% GDP)	2.3	1.3	0.5	2.5	1.5	1.0	0.3	0.0	0.3
Domestic demand	3.3	-2.1	0.8	-1.4	-1.2	-1.1	-0.5	1.4	1.8
Exports	1.3	-6.0	-0.3	-4.4	-6.0	-5.7	-7.7	-3.2	-0.5
Imports	4.4	-11.2	-1.0	-9.7	-11.2	-13.5	-10.5	-4.9	-1.5
GDP	2.1	-1.1	0.8	-0.3	-1.5	-1.0	-1.8	-1.3	0.5
GDP (% quarter)	-	-	-	-0.4	-1.1	-0.2	0.0	0.0	0.7
Industrial production	0.2	-1.9	-0.5	0.3	-3.4	-1.0	-3.4	-3.0	0.0
Unemployment (%)	2.6	3.8	4.7	3.1	3.7	4.0	4.2	4.5	4.7
Average earnings	6.0	3.8	3.2	3.3	3.9	4.7	3.1	3.2	3.2
Consumer prices	3.8	2.0	1.6	2.4	2.4	1.5	1.8	1.6	1.7
Current account (% GDP)	19.5	11.0	9.5	12.3	11.3	10.5	10.0	9.0	9.0
Budget balance (% GDP)	20.0	14.0	11.5	-	-	-	-	-	-
NOK/EUR**	9.7	8.5	8.0	8.96	9.03	8.50	8.50	8.00	8.00
3-month money (%)	6.1	2.4	2.3	3.0	2.0	2.0	2.0	2.0	2.0
10-year bond yield (%)	4.4	3.9	3.9	3.8	4.1	3.9	3.9	3.9	3.9

Note: * = total GDP; ** = end-year
Source: HSBC

HSBC

Sweden

Signs of improvement

Sweden is set to undergo its worst ever economic contraction in 2009. GDP fell by a much-worse-than-expected 0.9% q-o-q (-6.4% y-o-y) in Q1 which is the main reason for lowering our 2009 forecast to 4.5% (from 3.3%). The only positive contribution to GDP growth in Q1 came from higher government spending, which we expect to remain positive, at least until the end of 2009, given the expansionary fiscal stance of the government. The fall in household consumption continued in Q1, albeit at a more modest rate (-0.2% q-o-q) than in H2 2008.

We continue to expect the pace of contraction to moderate from Q2 onwards and for GDP growth to turn positive by early 2010 as domestic demand firms and net exports are supported by the 15% fall in the trade-weighted SEK over the past year. In addition, to boost spending, the government is introducing cuts in personal taxes, corporate taxes and employers' social security contributions. Retail sales are currently increasing and the confidence is rising amongst households and businesses. But this is unlikely to give rise to a quick revival of consumer spending given the expected rise in unemployment.

The ongoing problems in Latvia continue to raise concerns about the Swedish banking system. Sweden's banks have outstanding loans to the Baltic states equivalent to 15% of Sweden's GDP, and any losses would be further compounded if any of the Baltic countries are forced to devalue.

The Riksbank has remained very active, having cut its policy rate to 0.5% in April from 4.25% in October 2008. Further cuts to 0.25% and other unconventional measures cannot be ruled out.

Janet Henry*
Economist
HSBC Bank plc
+44 20 7991 6711
janet.henry@hsbcib.com

Urvashi Nangia*
Bangalore

*Employed by a non-US affiliate of HSBC Securities (USA) Inc, and is not registered/ qualified pursuant to NYSE and/ or NASD regulations

% Year

	2008	2009f	2010f	Q1 09	Q2 09	Q3 09f	Q4 09f	Q1 10f	Q2 10f
Consumer spending	-0.4	-1.5	1.1	-2.5	-2.1	-1.3	-0.1	0.3	0.9
Government consumption	1.1	3.1	2.5	2.1	3.0	3.2	4.3	3.8	2.9
Investment	2.4	-8.9	-3.1	-9.4	-9.6	-9.2	-7.3	-4.4	-3.5
Stockbuilding (% GDP)	0.1	-0.3	0.1	-0.5	-0.4	-0.2	-0.1	-0.1	-0.1
Domestic demand	-0.1	-2.4	1.0	-3.8	-3.5	-2.1	-0.2	0.7	0.9
Exports	1.7	-11.4	3.2	-13.7	-14.5	-11.5	-5.2	0.5	3.8
Imports	3.1	-11.8	3.7	-13.0	-15.3	-12.1	-6.6	-0.5	4.3
GDP	-0.4	-4.5	1.0	-6.4	-6.0	-5.2	0.0	1.0	0.9
GDP (% quarter, sa)	-	-	-	-0.9	0.4	0.3	0.2	0.1	0.2
Industrial production	-3.8	-15.0	2.2	-17.4	-17.9	-15.0	-9.1	-1.6	2.4
Unemployment (%)	6.2	8.5	9.4	7.9	8.5	8.7	9.0	9.2	9.3
Average earnings	4.1	2.2	2.2	2.5	2.3	2.0	2.0	2.0	2.0
Consumer prices	3.5	-0.1	1.1	0.8	-0.5	-0.5	-0.3	1.0	1.0
Current account (% GDP)	7.8	7.4	6.9	9.0	6.6	7.8	6.2	7.0	6.4
Budget balance (% GDP)	2.8	-1.4	-1.4	-	-	-	-	-	-
State debt (% GDP)	38.1	39.4	40.8	-	-	-	-	-	-
SEK/USD	6.71	7.77	7.50	8.27	7.75	7.59	7.50	7.50	7.50
EUR/SEK	9.91	11.01	11.25	10.98	10.87	11.00	11.25	11.25	11.25
3-month money (%)	4.4	1.0	1.2	1.1	1.0	0.9	0.9	0.9	1.1
10-year bond yield (%)	3.7	3.9	4.2	3.0	3.5	3.5	3.5	3.4	3.4

Source: HSBC

HSBC

Switzerland

Limiting the damage

Swiss GDP held up better in Q1 (-0.8% q-o-q) than that of most of its European neighbours, notably when compared with Germany (-3.8% q-o-q). We expect the global recession to play catch-up with Switzerland, and hence the SNB will continue its ultra-loose monetary policy.

At the beginning of this year, GDP support emanated from modest consumption growth and sustained government expenditure, while investment contracted by much less than expected (-0.4% q-o-q). Equipment investment even rose by 0.1% q-o-q, something which is a little at odds with the global collapse in industrial output and Swiss exports. Hence, we believe that industry is not yet out of woods, and project further weakness on the investment side. Private consumption growth is also set to fade as the weakening of the labour market gains traction.

The general assumption for a small open economy is that its fate is decided externally, and not domestically. But this certainly has not led to inaction on behalf of the SNB. On the contrary. The SNB was quick to push interest rates close to zero, with the target of the CHF 3mth LIBOR rate currently at 0.25%. And at the time of writing, the SNB sets the repo rate, which it uses to steer money market rates, at 0.05% for its one week maturity. With interest rates effectively at 0%, in March the SNB embarked on currency intervention to weaken the CHF, and a corporate bond purchase programme (in CHF). Intervention against the CHF, with an eye on EUR-CHF, at least on a verbal basis, is expected to be continued. Deflation fears are the official justification for the “stabilisation” of the currency, and indeed, CPI inflation is set to contract this year, and only recover slowly next year.

Astrid Schilo*
Economist
HSBC Bank plc
+44 20 7991 6708
astrid.schilo@hsbcib.com

*Employed by a non-US affiliate of HSBC Securities (USA) Inc, and is not registered/ qualified pursuant to NYSE and/ or NASD regulations

% Year

	2008	2009f	2010f	Q1 09	Q2 09	Q3 09f	Q4 09f	Q1 10f	Q2 10f
Consumer spending	1.7	0.1	-0.3	0.6	0.1	-0.1	-0.2	-0.5	-0.5
Government consumption	0.0	3.4	1.6	4.6	4.0	2.6	2.2	1.3	1.5
Investment	-1.7	-5.6	-0.1	-6.3	-7.4	-6.0	-2.6	-2.2	0.0
Stockbuilding (% GDP)	-1.3	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6
Final domestic demand	0.7	-0.9	0.0	-0.6	-1.3	-1.2	-0.5	-0.7	-0.1
Exports	2.3	-13.2	1.6	-11.9	-16.7	-16.0	-7.5	-1.9	2.0
Imports	-0.2	-5.1	1.3	-3.9	-8.2	-6.7	-1.4	-1.1	1.6
GDP	1.6	-2.1	0.2	-1.6	-2.6	-2.5	-1.9	-1.1	0.2
GDP (% quarter)	-	-	-	-0.8	-1.0	-0.1	0.0	0.0	0.2
Industrial production	1.2	-12.0	0.3	-11.7	-16.8	-11.7	-7.3	-3.0	0.3
Unemployment (%)	2.6	3.7	5.2	3.1	2.8	3.0	3.0	4.0	5.0
Consumer prices	2.4	-0.6	0.6	0.0	-0.8	-1.1	-0.5	0.4	0.6
Current account (EURbn)	31.0	20.7	25.0	5.7	4.6	5.0	5.4	5.5	5.3
Current account (% GDP)	9.3	6.2	7.4	6.5	5.8	6.2	6.3	6.4	6.6
SFR/USD*	1.06	1.05	1.07	1.14	1.09	1.08	1.05	1.07	1.07
SFR/EUR*	1.48	1.57	1.60	1.51	1.53	1.57	1.57	1.60	1.60
3-month money (%)	2.3	0.4	0.8	0.6	0.3	0.3	0.3	0.3	0.5
10-year bond yield (%)	2.7	2.1	2.7	1.9	2.3	2.2	2.3	2.5	2.5

Note: * = end-year
Source: HSBC

Hungary

Bajnai focuses on reform

Juliet Sampson*
Economist
HSBC Bank plc
+44 20 7991 5651
juliet.sampson@hsbcib.com

*Employed by a non-US affiliate of HSBC Securities (USA) Inc, and is not registered/ qualified pursuant to NYSE and/ or NASD regulations

In April, Gordon Bajnai, who had served as Economy Minister for a year, replaced embattled Prime Minister Ferenc Gyurcsany. Bajnai demanded unconditional backing for his budget cuts and reform agenda in exchange for agreeing to take a job that many view as a poisoned chalice. The deal has worked so far, coinciding with a period of market stabilisation.

Bajnai's reform measures focus on tax and pension changes with a view to lowering the cost of employment and increasing the employment participation rate. End-year pension bonuses will be eliminated and pension premiums and adjustments will be tied to GDP. Tax measures include a rise in the lower threshold of personal income tax and a VAT hike from 20% to 25% to take effect from July. The VAT hike will boost CPI from 3.8% in May to above 7.0% at year-end, before falling back towards 2% in 3Q 2009.

Hungary's economic decline is severe. GDP shrank 6.7% in 1Q 2009 and is set to remain in negative territory through 2010 before returning to growth in 2011. Investment and household consumption are in deep decline; government spending is severely constrained. Net exports have improved as the fall in exports (-18.6% in a volume basis in Q1) has outpaced the collapse in imports (-22.0%). The extent of the decline in output owes much to pro-cyclical fiscal and monetary policy. Restrictive policy is necessitated, on the fiscal side, by the need to fulfil IMF/EU lending conditions and to demonstrate budget credibility to the markets; and, on the monetary policy side, to ensure stability of the forint. Some stability has returned to markets in recent weeks, but the NBH is likely to ease only gradually, to avoid a return to the chaotic market conditions of Q1.

% Year

	2005	2006	2007	2008	2009f	2010f
Consumer spending	3.8	1.3	-1.8	-0.1	-6.5	-1.8
Government consumption	0.2	4.4	-2.2	-2.1	-1.2	-0.5
Fixed investment	5.6	-3.2	1.5	-2.6	-6.1	0.0
Exports	11.6	17.7	15.9	4.6	-15.5	3.2
Imports	6.8	14.6	13.1	4.0	-19.0	1.2
GDP	3.9	4.0	1.2	0.6	-5.9	-0.6
Industrial production	7.0	10.6	8.5	4.9	-18.2	3.5
Unemployment*	7.3	7.5	7.7	7.8	11.5	11.5
Consumer prices	3.6	3.9	8.0	6.1	4.7	4.0
Current account (% GDP)	-7.3	-7.8	-6.6	-9.0	-4.8	-5.0
Budget balance (% GDP)**	-7.8	-9.1	-4.9	-3.3	-4.0	-4.0
HUF/USD*	214.0	190.6	172.9	191.3	183.3	173.3
HUF/EUR*	252.5	251.4	252.8	265.9	275.0	260.0
3-month money (%)*	6.3	8.1	7.5	10.0	8.1	4.5
10-year yield (%)*	7.0	6.7	7.1	8.2	9.0	7.0

Note: * = year-end; ** Cash deficit rather than European Standard Accounting budget deficit
Source: HSBC

Poland

Staying positive

The Polish economy has slowed dramatically in recent months and looks set to remain weak in the quarters ahead. But compared with its neighbours in Central Europe, Poland is outperforming, and economic activity is likely to remain in positive territory for the year.

Poland benefits from the lower proportion of exports in the economy, around 33% compared with close to 70% for Hungary and the Czech Republic, and the relative health of the domestic labour market. Domestic demand has remained relatively firm: household consumption grew 3.3% in Q1, in contrast to much of the world, even as imports fell. Unemployment has risen, but at 11.0% in April it is only marginally higher than the 10.5% rate a year earlier. Personal income tax cuts have helped sustain demand as well.

It is not clear whether domestic demand will remain as strong through the rest of the year. Pressure will be put on public spending in the months ahead as the government tries to rein in the deficit, which has widened through April. Investment has dropped off.

Monetary policy has been accommodative in spite of currency weakness. Interest rates have been cut by 225bp to 3.75% since October and the dovish MPC appears likely to continue easing. Inflation may be slowing; there are signs of price stickiness, with CPI rising to 4.0% in April (after dropping to 2.8% in January). Prices should resume their fall and allow the easing to resume by the end of Q2. In the meantime, lower interest rates have prevented the zloty from recovering as much as other regional currencies. It has probably not helped the currency, either, that the government's plan to join ERMII in Q2, part of its 2012 euro-adoption target, has slipped.

Juliet Sampson*
Economist
HSBC Bank plc
+44 20 7991 5651
juliet.sampson@hsbcib.com

*Employed by a non-US affiliate of HSBC Securities (USA) Inc, and is not registered/ qualified pursuant to NYSE and/ or NASD regulations

% Year

	2005	2006	2007	2008	2009f	2010f
Consumer spending	2.7	5.0	5.0	5.4	1.8	2.5
Government consumption	6.6	4.3	1.9	0.0	1.1	2.5
Fixed investment	6.5	14.9	17.6	7.9	0.8	3.5
Exports	2.6	12.3	4.9	5.8	-10.2	2.5
Imports	-1.6	15.0	7.0	6.2	-12.5	2.5
GDP	3.6	6.2	6.7	4.8	0.6	1.2
Industrial production	4.0	12.0	9.7	3.9	-11.1	1.5
Unemployment (%)*	17.6	14.9	11.4	9.5	12.0	11.0
Consumer prices	2.1	1.0	2.5	4.2	3.7	2.6
Current account (% GDP)	-1.6	-2.3	-3.8	-7.2	-3.3	-4.3
Budget balance (% GDP)	-2.5	-2.4	-1.4	-1.9	-3.0	-2.9
PLN/USD	3.2	3.1	2.8	2.4	3.0	2.4
PLN/EUR	4.0	3.9	3.8	3.4	4.2	3.6
3-month money (%)*	4.6	4.2	5.7	5.9	3.3	4.0
10-year bond yield (%)*	5.1	5.2	5.9	5.4	6.0	5.5

Note:* = year-end
Source: HSBC

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Romania

Kubilay Ozturk*
Economist
HSBC Bank plc
+44 20 7991 1360
kubilay.ozturk@hsbcib.com

*Employed by a non-US affiliate of HSBC Securities (USA) Inc, and is not registered/ qualified pursuant to NYSE and/ or NASD regulations

Bowing to recession

The Romanian economy shrank by 6.2% y-o-y in the first quarter as household consumption plunged and gross capital formation fell precipitously due to de-stocking. While the looming sizeable recession was heralded by the sharp economic slowdown in Q4of last year, the rapid pace of economic deterioration seen since then is striking. Looking ahead, household consumption and investments will remain subdued through the rest of year as credit extension, wage growth and cross-border private capital inflows continue to retreat while the unemployment rate soars. The economy is likely to start recording positive growth from the first quarter of 2010.

The IMF-led external loan package secured by the centre-left coalition government in March has boosted confidence in the Romanian economy. The leu has stayed firm and the CDS spreads have come down from their peaks since the conclusion of financial support, although positive momentum has recently petered out following Latvian contagion fears and recently elevated risk aversion.

The budget deficit recorded at 2.2% (of GDP) in January-May remains in line with the quarterly ceiling (2.7%) set by the IMF deal while further fiscal tightening (around 1% of GDP) is likely to be needed in the second half of 2009 to meet the full-year target of 4.6% (in cash terms). The government, however, may appear reluctant to enact such cuts ahead of the November presidential elections, in which the two strongest contenders are from each of the coalition parties. Hence, the risk for fiscal slippage appears high and subsequent delays in loan disbursements are probable.

Emboldened by the IMF package, the National Bank of Romania (NBR) lowered its key rates by 50bp in May and in June to 9%and shifted to a dovish bias. The scale of cumulative easing is 125bp so far and assuming the IMF programme is kept on track, further measured cuts are likely; however aggressive moves should not be expected as the banking system remains vulnerable due to the high weight of foreign currency lending in total loans (c60%) and a high FX loan-to-deposit ratio (1.85).

% Year

	2005	2006	2007	2008	2009f	2010f
Consumer spending	10.0	12.8	11.6	9.1	-4.1	1.4
Fixed investment	15.3	19.9	28.9	19.3	-11.1	2.3
Exports	7.2	9.8	7.8	18.9	-17.0	3.0
Imports	16.0	22.7	27.8	17.1	-18.5	2.5
GDP	4.1	7.9	6.2	7.1	-3.8	1.6
Industrial production	-2.5	9.4	10.1	2.6	-7.0	3.0
Unemployment (%)*	5.9	5.2	4.1	4.4	8.0	8.5
Consumer prices	9.0	6.6	4.8	7.9	5.9	4.1
Current account (% GDP)	-8.9	-10.4	-13.9	-12.6	-7.5	-7.0
Budget balance (% GDP)**	-1.2	-2.2	-2.5	-5.4	-5.5	-5.0
RON/USD*	3.11	2.56	2.45	2.89	2.91	2.61
RON/EUR*	3.68	3.38	3.57	4.03	4.25	3.80
3-month money (%)*	6.4	8.0	8.0	14.7	10.0	8.5

Source: HSBC

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Russia

Slow recovery after a deep recession

Alexander Morozov*
Economist
HSBC Bank (RR), Moscow
+7 495 783 8855
alexander.morozov@hsbc.com

*Employed by a non-US affiliate of HSBC Securities (USA) Inc, and is not registered/ qualified pursuant to NYSE and/ or NASD regulations

Output in the Russian economy has been declining through May. Extrapolating the trend of the manufacturing and services PMI surveys, it may take another two to three months to reach bottom. Meanwhile, the rate of GDP contraction has deepened to 10% year-on-year in April, according to MOED estimates.

Any encouraging signs relate mostly to improving business sentiment rather than to hard economic data. Inflation has been decelerating because of tighter liquidity and falling domestic and foreign demand. The CBR is now intent on resisting currency appreciation as devaluation expectations have disappeared. Lower inflation and a stronger currency have allowed the authorities to ease monetary policy, with 150bp of policy rate cuts delivered between April and early June and more likely to follow.

Large companies have reported an improved access to credit, but banking-sector assets continue to fall and the problem of rising non-performing loans is still to be resolved. But improving interest rate dynamics may yet reduce lending costs to an affordable level for the real economy, and oil prices have almost doubled, which should translate into better overall economic performance after a lag. Given these trends, the outlook looks slightly more positive, but the recovery still has to be seen in the data and any upturn promises to be slow. It may take a several years before output returns to pre-crisis levels.

Overall, we expect low-single-digit growth rates over the coming years, rather than the high-single-digit rates Russia recorded in 2003-2008, for several reasons. First, following a period of above-trend growth, the world economy may grow only moderately in coming years as various imbalances are worked off, and the same argument applies to Russia. Second, credit and commodities – the key drivers of Russia's economic growth in the recent past – have lost momentum and may need time to recuperate. Finally, future domestic demand growth in Russia is likely to constrained by institutional deficiencies that will work to slow the pace of the necessary restructuring of enterprises.

% Year

	2005	2006	2007	2008	2009f	2010f
GDP	6.4	7.7	8.1	5.6	-7.9	2.5
Industrial production	4.0	4.4	4.1	0.8	-13.2	1.9
Consumer prices	12.7	9.7	9.0	14.1	11.6	11.5
Current account (USDbn)	84.3	94.3	77.2	98.9	43.9	28.0
Current account (% GDP)	11.1	9.5	6.0	5.9	3.6	2.1
Foreign exchange reserves (USDbn)	175.9	295.6	465.9	412.5	394.7	409.7
Overall fiscal balance (% GDP)	7.5	7.4	5.4	4.1	-8.4	-4.7
RUB/USD*	28.4	27.0	25.3	25.4	32.3	33.4
1-month money (%)*	4.7	4.8	4.9	10.1	12.6	10.1

Note: * = year average
Source: HSBC

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Turkey

IMF remains an option

With the global economic outlook stabilising and financial markets recovering from their lows in early-May, the Turkish government appears more reluctant to sign up to a new IMF arrangement. While the negotiations continue, it appears an IMF deal has moved to a back burner.

The apparent disagreement regarding the fiscal framework relates to the sustainability of public debt. While Turkey's public debt-to-GDP ratio of 39.5% in 2008 was significantly below the Maastricht threshold of 60%, the debt has a short maturity, around 25 to 30 months; incurs high real interest rates of c6% to 7%; and is fairly large compared with the on-shore private credit stock of roughly 35% of GDP. The widening budget deficit and rising public debt (we forecast figures of 7.4% and 46.5% of GDP, respectively, for this year), therefore, risk crowding out the supply of credit to the private sector in the absence of strong external financing. The IMF is believed to be demanding that the primary balance is raised back to a surplus of 2% of GDP over the medium term from the roughly 2% deficit in 2008. This requires significant, ongoing fiscal consolidation efforts.

Aside from numerical hurdles, there are also conceptual differences between the IMF and Turkish government in their approach to structural fiscal reform areas. Hence, negotiations will likely linger for a while longer and the government is working on 'no IMF' scenarios as well. We think this is a risky strategy, since external financing is an issue for Turkish corporates and banks still repaying external debt. In the meantime, higher global commodity prices suggest that the current account deficit will widen again. This, coupled with a large budget gap, would leave Turkey vulnerable as a twin-deficit country, particularly with the global environment remaining fairly precarious.

Dr. Murat Ulgen*
Economist
HSBC Turkey
+90 212 376 4619
muratulgen@hsbc.com.tr

*Employed by a non-US affiliate of HSBC Securities (USA) Inc, and is not registered/ qualified pursuant to NYSE and/ or NASD regulations

% Year

	2005	2006	2007	2008	2009f	2010f
Consumer spending	7.9	4.6	4.1	0.3	-1.1	2.6
Government consumption	2.5	8.4	6.5	1.8	1.4	1.6
Fixed investment	17.4	13.3	5.4	-4.6	-9.2	3.3
Stockbuilding (% GDP)	-0.8	-0.8	0.2	0.2	-2.7	-2.6
Domestic demand	9.4	7.0	4.7	0.3	-4.0	2.5
Exports	7.9	6.6	7.3	2.6	-6.3	4.2
Imports	12.2	6.9	10.7	-3.1	-10.0	7.3
GDP	8.4	6.9	4.6	1.1	-4.4	2.0
Industrial production	5.4	5.8	5.4	-0.9	-9.7	3.0
Consumer Prices	8.2	9.6	8.8	10.4	6.6	9.1
Producer prices	2.7	11.6	5.9	8.1	7.1	7.2
Current account (% GDP)	-4.7	-6.1	-5.8	-5.7	-2.0	-2.3
Budget deficit (% GDP)	-1.3	-0.5	-1.6	-1.5	-7.4	-5.6
TRY/USD**	1.35	1.47	1.27	1.34	1.64	1.61
3-month money (%)*	13.8	17.6	16.0	15.5	10.5	12.0

Note: * = year end; ** = starting in January 2005, when the Turkish currency (until then coded TRL) shed 6 zeros off its exchange rate
Source: HSBC

Saudi Arabia

The tide begins to turn

The pick-up in global energy prices over the past quarter has significantly enhanced the near-term outlook for Saudi Arabia. The addition of USD10/b and USD15/b to our assumed oil price for 2009 and 2010 respectively have been sufficient to turn anticipated current account shortfalls into surpluses. Although we continue to see budget deficits, oil prices of USD60/b and USD65/b result in shortfalls equivalent to less than USD10bn a year rather than the USD30bn we foresaw earlier.

We had never regarded those deficits as presenting significant funding challenges and had expected the government to maintain an expansionary fiscal stance. Nevertheless, growing confidence in the resilience of oil prices in what remains a weak demand environment will enhance sentiment and likely encourage a further loosening of the government's fiscal stance.

The Saudi equity market has already reacted to the changing external environment. In time, we expect to see economic activity pick up speed. However, we suspect it will be 2010 before the domestic economy really begins to gain speed. The private sector remains subdued, held back most notably by credit availability – SAMA data show that bank lending has been stagnant or contracted m-o-m since the end of Q3 2008 despite sharp cuts in Saudi policy rates and reductions in commercial-bank reserve requirements. The results of HSBC's quarterly business confidence surveys also paint the picture of a private sector where sentiment is fragile after several years of rapid growth.

Inflation has fallen away, dropping almost six percentage points in six months to stand at 5.2% in April. Although there may be some further easing as domestic demand continues to moderate and the base effect makes itself felt, we suspect the pace of decline is set to moderate. In part, this marks the expected dollar-driven weakness of the SAR, but we also expect the tight real estate market is likely to keep upward pressure on rents.

Simon Williams*
Economist
HSBC Bank Middle East Limited, Dubai
+971 4423 6925
simon.williams@hsbc.com

*Employed by a non-US affiliate of HSBC Securities (USA) Inc, and is not registered/ qualified pursuant to NYSE and/ or NASD regulations

% Year

	2005	2006	2007	2008	2009f	2010f
Consumer spending*	9.5	13.4	14.0	20.0	7.0	7.5
Government consumption*	18.4	18.4	3.5	14.0	10.0	10.0
Fixed investment*	25.1	19.1	22.8	23.0	5.0	8.0
Stocks*	-15.8	31.8	-2.7	15.0	-5.0	-5.0
Exports*	45.6	16.0	12.2	38.8	-38.5	11.0
Imports*	35.1	29.3	28.2	30.0	-8.0	5.0
GDP	5.6	3.1	3.4	4.3	-0.1	3.9
Consumer prices	0.4	2.3	4.1	9.9	5.4	4.0
Current account balance (USDbn)	90.0	98.9	95.0	150.4	29.7	39.2
Current account balance (% GDP)	28.5	27.7	24.9	30.8	7.6	9.0
Budget balance (% GDP)	18.4	21.7	12.5	31.7	-2.5	-2.1
SAR/USD	3.75	3.75	3.75	3.75	3.75	3.75
3-month money (%)**	5.0	4.9	4.0	3.0	0.9	1.4

Note: * Nominal growth. ** End year.
Source: HSBC

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South Africa

Juliet Sampson*
Economist
HSBC Bank plc
+44 20 7991 5651
juliet.sampson@hsbcib.com

*Employed by a non-US affiliate of HSBC Securities (USA) Inc, and is not registered/ qualified pursuant to NYSE and/ or NASD regulations

Zuma takes charge

By the time May's parliamentary elections were held, there was little surprise in the ANC's win or in Jacob Zuma's becoming prime minister. More newsworthy was the ANC's failure to gain a two-thirds parliamentary majority in spite of the poor result for the newly founded centre-right COPE party. Zuma has reassured some by retaining a few trusted hands, like ex-Treasury head Trevor Manual, as head of a new National Planning Commission, and Prahvin Gordhan, who takes over from Manual at the Treasury. However, Zuma has balanced these with powerful appointments from COSATU and SACP ranks to key economic roles.

South Africa avoided many of the initial market woes associated with the credit crunch, but the economy has noticeably weakened in the past two quarters. After slowing to 1.0% growth in Q4 2008, GDP declined 1.3% y-o-y in Q1 and 6.4% q-o-q annualised. Weakness in manufacturing has been evident since Q4, but a decline in mining shifted the balance in Q1. Services are also suffering and agriculture has fallen on base effects. A revival in commodities prices and improved harvests point to a possible bottoming of the downturn, as does an increase in government spending. However, recovery looks set to be slow and weak.

As for monetary policy, interest rates have plummeted as the SARB responded to signs of weak growth and softening inflation, cutting by a total of 450bp since December. Further easing is possible, though rate cuts will have to slow. There has been an increasing amount of talk of a possible change to, or elimination of, the inflation- targeting regime and it seems increasingly possible that it will become a victim of the shift in the balance of power from the centre-right towards the left. The SARB is also considering a change to its policy of non-intervention in the foreign currency markets.

% Year

	2005	2006	2007	2008	2009f	2010f
Consumer spending	6.9	8.3	6.6	2.3	-1.2	1.4
Government consumption	4.8	5.1	4.8	5.0	7.5	9.0
Fixed investment	8.9	13.8	17.1	10.2	5.0	7.1
Exports	8.0	6.0	7.5	1.7	-8.5	3.5
Imports	10.3	18.9	10.0	2.2	-11.0	3.5
GDP	5.0	5.3	5.1	3.1	-0.9	2.0
Industrial production	4.2	4.9	5.5	1.0	-16.6	4.2
M3	24.0	23.1	23.6	14.5	6.0	10.5
Consumer prices	3.5	4.6	7.1	11.5	7.3	5.9
Current account (% GDP)	-3.8	-6.4	-7.3	-7.4	-5.1	-5.7
Budget balance (% GDP)	-0.5	0.2	0.7	-0.3	-5.3	-5.3
ZAR/USD	6.40	7.03	7.01	8.37	9.54	11.63
3-month money (%)*	7.0	9.2	11.3	11.4	7.2	8.4
10-year bond yield (%)*	7.5	7.7	8.4	7.3	9.5	9.5

Note: * = index 1995 = 100 (end year)
Source: HSBC

Japan

New excess to limit growth

Japan's business cycle bottomed out in February-March. The replenishment of private inventories and global fiscal stimulus packages should support growth in the second half of this year. We expect real GDP to grow slightly q-o-q in April-June, before growing decisively in the final two quarters of this year. However, we estimate that Japan's negative output gap exceeded 7% in January-March. Therefore, Japanese companies are likely to continue to restrain capital investment and employment throughout 2009-2010. Weak employment will erode personal consumption, which, along with fixed capital investment, makes up about 70% of GDP. Thus, the impact of a bottoming out of industrial production, which makes up about 20% of GDP, will be limited. We assume overseas economies will at least stabilise and that additional fiscal measures in the FY2010 initial budget will mitigate the negative rebound from the record-large stimulus packages in FY2009. Even so, we expect an increase of just 1.2% in real GDP in 2010, following a 6.3% decline in 2009.

Deflationary pressure is likely to persist through 2010, reflecting the negative large output gap. We expect core CPI to decline 1.4% in 2009 and 1.1% in 2010.

Seiji Shiraishi*
Economist
HSBC Securities (Japan) Limited
+81 3 5203 3802
seiji.shiraishi@hsbc.com.jp

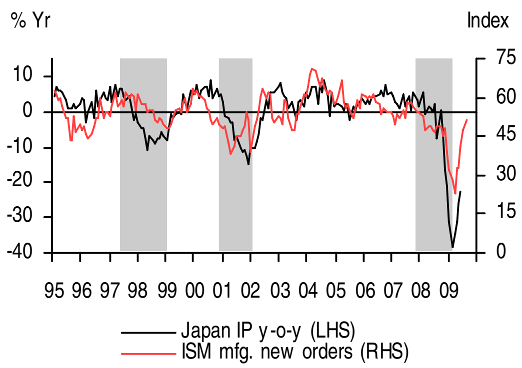
*Employed by a non-US affiliate of HSBC Securities (USA) Inc, and is not registered/ qualified pursuant to NYSE and/ or NASD regulations

% Year

	2008f	2009f	2010f	Q1 09	Q2 09	Q3 09f	Q4 09f	Q1 10f	Q2 10f
Consumer spending	0.6	-1.3	0.0	-2.8	-1.3	-1.2	-0.7	0.2	-0.1
Government consumption	0.8	0.8	0.5	0.6	1.2	1.7	-0.1	0.1	0.5
Investment	-5.0	-13.2	-3.3	-14.9	-14.5	-13.4	-10.0	-4.2	-2.6
Private non-residential	-4.0	-20.9	-7.9	-20.9	-22.1	-21.5	-18.2	-12.0	-8.7
Private residential	-7.6	-3.3	-0.1	0.6	0.6	-4.4	-9.2	-3.4	-0.4
Public	-6.9	8.9	9.4	0.4	4.0	11.3	20.2	22.5	17.2
Stockbuilding (% GDP)	0.5	0.8	0.8	0.8	0.7	0.8	0.8	0.8	0.8
Domestic demand	-0.9	-3.3	-0.6	-4.7	-3.7	-2.9	-2.8	-0.7	-0.4
Exports	1.8	-28.8	9.8	-36.5	-32.4	-30.1	-14.4	16.9	11.4
Imports	0.9	-13.8	-6.1	-14.9	-11.0	-11.9	-17.1	-5.4	-6.9
GDP	-0.7	-6.3	1.2	-8.8	-7.8	-6.6	-2.5	1.5	1.7
GDP (% quarter)	-	-	-	-3.8	0.1	0.5	0.7	0.2	0.2
Industrial production (% year)	-3.4	-27.0	2.3	-34.6	-29.5	-26.6	-16.4	9.5	1.4
Unemployment rate	4.0	5.2	6.1	4.7	5.0	5.4	5.7	6.0	6.1
Wholesale prices	4.6	-6.5	-0.9	-1.8	-7.4	-10.2	-6.5	-3.4	0.0
CPI	1.5	-1.4	-1.1	-0.4	-1.3	-2.1	-2.0	-1.4	-1.1
M2+CDs	2.1	1.8	2.0	1.8	1.8	1.8	1.9	2.0	2.0
Current account (JPYtrn)	16.3	13.4	19.7	2.4	3.2	3.6	4.1	4.2	4.8
Current account (% GDP)	3.2	2.8	4.1	2.1	2.6	3.1	3.2	3.6	4.0
Budget balance (% GDP)	-3.5	-10.2	-10.5	-	-	-	-	-	-
JPY/USD	117	101	101	99	96	100	105	105	105
3-month money (%)	1.0	0.6	0.6	0.7	0.6	0.6	0.6	0.6	0.6
Benchmark bond (%)	1.4	1.5	1.5	1.3	1.4	1.6	1.6	1.5	1.5

Source: HSBC

Industrial production bottomed

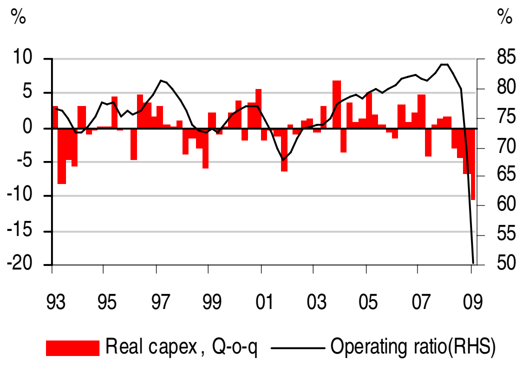


Note: Gray shadings show recession periods. ISM leads IP by 3 months. Numbers for May. and June09 are based on survey projections.
Source: MoF, METI

… but tertiary activities not

- Industrial production grew m-o-m in March, April and May and further growth is expected in June. The Japanese business cycle is determined mainly by industrial production, so there is a strong possibility that Jan-Mar was the cyclical bottom. This improvement is mainly due to progress in inventory adjustment, especially in the troubled machinery sector. The new orders component of US manufacturers ISM index, a strong leading indicator of Japanese IP, indicates that IP will continue to improve at least through autumn.
- By contrast, non-manufacturers' activity has kept deteriorating even in recent months, which indicates that the weakness in the manufacturing sector has been filtering into the non-manufacturing sector through manufacturers' adjustments in employment and capital expenditure.

Excess capacity

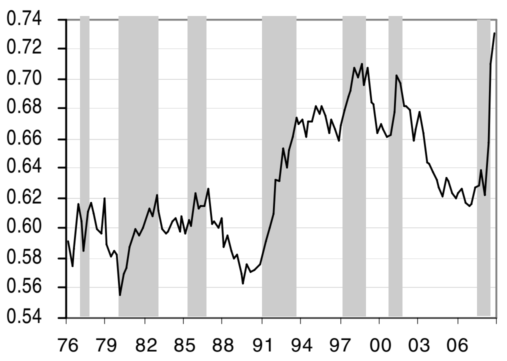


Source: Cabinet Office, MHLW, MIC,HSBC

Operating rate is too low for capex to increase

- The output gap is estimated to have reached -7.3% of potential GDP in Q109, bringing on new excess problems (capacity and labour) and persistent deflation in Japan. The large output gap will persist for years as the actual growth rate will not be able to exceed the potential rate sizably on a sustained basis.
- In the past, real business fixed investment did not increase q-o-q when the capacity utilization rate was under 73%, and it was 50.4% in March. To raise the real capacity utilisation rate from 50% to over 73%, Japanese industrial production would have to increase by nearly 50%, relative to its level in March, assuming no change in capacity. Japanese companies are likely to scrap their capacity first before increasing capex.

Unprecedented high labour's share



Note: Labour's share: Labour costs / (Recurring profits + personnel expences + depreciation cost + interest and discount paid). Gray shadings show recession period.
Source: MoF, HSBC

… leads persistent personnel expenses cuts

- Labour's share rose to a record high level of 73% in Jan-Mar, which indicates that Japanese companies will cut personnel expenses more aggressively hereafter. The unemployment rate will rise to 6% early next year.
- Reflecting this labour surplus, cash earnings per employee are dropping at an increasing rate, falling by 3.9% y-o-y in March. Listed Japanese companies are expected to cut their summer bonuses by almost 20% this year. Thus, cash earnings per employee are likely to drop much more this year than the 6% they fell in 2002, after the collapse of the IT bubble.

Australia

Signs of hope

Contrary to market expectations, the Australian economy expanded by 0.4% q-o-q in the first quarter of the year, thereby averting a technical recession. Exports increased sharply as China's demand for commodities boomed, something we think will continue through the year. At the same time, consumer spending picked up as interest-servicing costs and petrol prices fell. With no net job losses in the economy yet, consumer confidence is making a comeback, which should provide a floor to household spending.

Investment, however, remains a drag, though dwelling construction should improve by the end of the year given healthy immigration, historically low mortgage rates and first home-owner grants. We have already seen building approvals increase on a sequential basis since the beginning of the year. Government infrastructure spending will also support investment towards the end of the 2009. Overall, we look for the Australian economy to expand by 0.2% in 2009, with growth accelerating to 2.6% in 2010.

On the external account, we think exports will hold up while imports will be dragged down by the poor performance of investment. This should see the current account deficit improve in 2009.

After 425bp of easing, the Reserve Bank of Australia kept rates unchanged at 3% in June, citing continued evidence of stabilisation in the global economy and the clear turnaround in China. Together with the expected pick-up in inflation from the end of the year, we believe that 3% will represent the floor in rates.

Prakriti Sofat*
Economist
HSBC Singapore
+65 6239 2870
prakritisofat@hsbc.com.sg

*Employed by a non-US affiliate of HSBC Securities (USA) Inc, and is not registered/ qualified pursuant to NYSE and/ or NASD regulations

% Year

	2008	2009f	2010f	Q1 09	Q2 09	Q3 09f	Q4 09f	Q1 10f	Q2 10f
Consumer spending	2.2	1.3	2.2	0.8	1.3	1.5	1.6	1.6	2.0
Government consumption	3.7	2.6	3.2	2.5	2.2	2.8	3.0	3.2	3.2
Investment	8.3	-8.4	-3.1	-1.3	-7.7	-11.5	-13.2	-9.7	-4.8
Final domestic demand	4.4	-1.3	0.3	0.5	-1.2	-2.1	-2.4	-1.2	0.4
Stockbuilding (% GDP)	0.4	-0.9	0.3	-1.2	-1.3	-1.1	0.0	0.2	0.2
Domestic demand	3.8	-2.1	2.1	-1.4	-2.6	-3.3	-1.2	0.1	1.9
Exports	3.9	1.6	5.0	3.5	-0.6	0.8	2.7	1.8	5.4
Imports	10.3	-13.8	4.6	-10.3	-16.9	-18.3	-9.8	-1.6	4.5
GDP	2.3	0.2	2.6	0.4	-0.3	-0.3	0.9	1.2	2.5
GDP (% quarter)	-	-	-	0.4	-0.3	0.2	0.6	0.8	0.9
Industrial production	2.6	-3.5	2.0	-3.6	-5.0	-4.5	-1.0	1.0	2.0
CPI	4.3	2.0	2.8	2.5	2.0	1.5	2.0	2.5	2.8
Unemployment	4.2	6.1	6.6	5.2	5.8	6.5	7.0	7.5	6.5
Average earnings	4.1	4.0	3.9	4.1	4.0	4.0	3.9	3.9	3.9
Current account (AUDbn)*	-51.1	-42.0	-52.0	-18.5	-28.0	-36.0	-42.0	-44.0	-44.0
Current account (% GDP)	-4.3	-3.8	-4.5	-	-	-	-		
Budget balance (% GDP)	1.8	-1.5	-1.5	-	-	-	-		
USD/AUD	0.84	0.76	0.82	0.69	0.81	0.77	0.80	0.82	0.82
3-month money (%)	6.8	3.2	4.0	3.2	3.5	3.1	3.2	3.2	3.3
10-year bond (%)	5.5	5.1	5.5	4.4	5.5	5.4	5.1	4.8	4.8

Note: Quarterly data are a four-quarter rolling sum; * = quarter annualised
Source: HSBC

HSBC

New Zealand

It's a long recession

Prakriti Sofat*
Economist
HSBC Singapore
+65 6239 2870
prakritisofat@hsbc.com.sg

*Employed by a non-US affiliate of HSBC Securities (USA) Inc, and is not registered/ qualified pursuant to NYSE and/ or NASD regulations

The New Zealand economy contracted for the fifth consecutive quarter in Q1 2009, falling 1% q-o-q, pulled down by the weakness in consumer spending and investment. With consumer confidence making a comeback in the second quarter and house prices declining less rapidly, we think some stabilisation is on the cards. Unfortunately the same cannot be said about business investment given that investment intentions remain at very low levels. However, residential investment may turn sooner than anticipated as fewer New Zealanders are leaving the country given the poor overseas employment outlook. We have already seen housing sales start to improve.

After 575bps of easing the Reserve Bank of New Zealand kept the policy rate unchanged at 2.5% in June. Although admittedly the economy remains within a protracted recession, some positives are emerging. Signs of stabilizing global economic activity and a greater pass through of the massive policy easing already delivered – existing fixed-rate mortgages are coming up for re-pricing and the easing of fiscal policy – should allow the economy to grow in the latter part of the year. Consequently we expect GDP to contract by 0.3% in 2009 with growth picking up to 2.3% next year. Against this backdrop we expect the current policy rate of 2.5% to represent the bottom of the cycle, but we do not expect any change from this level until well into 2010.

On the external account, given the dominance of food in New Zealand's exports, we think overall exports will hold up reasonably well, while imports will be dragged down by the poor performance of investment. This should see the current account deficit improve in 2009.

% Year

	2005	2006	2007	2008	2009f	2010f
Consumer spending	4.8	2.5	4.1	0.2	-1.2	1.6
Government consumption	3.9	4.9	3.6	4.0	3.6	2.9
Investment	3.7	-0.3	4.8	-4.1	-16.9	4.6
Final domestic demand	4.4	2.2	4.2	-0.3	-3.5	2.6
Stockbuilding (% GDP)	1.1	0.3	0.6	1.0	-0.6	-0.6
Domestic demand	4.2	1.4	4.5	0.1	-5.0	2.6
Exports	-0.3	1.8	3.8	-1.7	-2.5	3.6
Imports	5.5	-2.6	8.4	2.6	-18.1	4.3
GDP	2.8	2.6	3.1	-1.0	-0.3	2.3
Consumer prices	3.0	3.4	2.4	3.9	1.8	2.4
Current account (% GDP)	-8.5	-8.8	-8.2	-8.9	-7.5	-8.0
Budget balance (% GDP)	4.5	3.7	3.7	2.5	0.1	0.1
Unemployment*	3.8	3.7	3.7	3.9	6.0	5.6
NZD/USD	0.70	0.64	0.75	0.70	0.57	0.60
3-month money (%)	7.2	7.6	8.4	8.0	2.9	2.8
10-year bond yield (%)	5.9	5.8	6.3	6.1	5.7	5.3

Note: * Year end. Source: HSBC

HSBC

China

Recovery gaining momentum

The May data have beaten market expectations, with industrial production (IP) growth accelerating to 8.9% y-o-y, the highest rate since last October, confirming that the infrastructure-led recovery is gaining momentum. Surging fixed asset investment (FAI) has offset the deeper contraction in exports (-26.4% year to May versus -22.6% in April) and boosted demand for construction materials. Real growth in urban FAI continued to accelerate from 40.5% in April to 46% in May, the strongest rise since February 2004. This led to the big jump in IP growth, particularly for heavy industries, which accounted for around 70% of the rebound in overall IP growth. Meanwhile, both auto and housing sales continued to rebound in May, rising by 23.8% and 75.3% year-on-year, respectively, versus 18.5% and 63.7% in April. In addition, overall consumer spending also remains steady. Retail sales growth accelerated to 16.6% y-o-y in May in volume terms from 16.3% y-o-y in April.

With an easing monetary bias in place, rapid credit growth should support infrastructure investment, pushing GDP growth above 8% in H2. This implies a substantial increase in demand for construction materials, machinery and energy. Given that China's import dependence ratios for such products are generally above 50%, commodity-exporting nations and those developed countries that can supply China with advanced machinery are best positioned to benefit from a China recovery. For commodities exporters, the gain will not just come from Chinese demand, but recovering commodity prices will also improve their terms of trade, allowing them in turn to buy more Chinese manufactured products. Together with China's latest initiatives to strengthen trade and investment links with Latin America and the Middle East, we expect trade flows between China and other main emerging markets to rise, setting the stage for a new world trade order.

Qu Hongbin*
Economist
The Hongkong and Shanghai Banking Corporation Limited (HK)
+852 2822 2025
hongbinqu@hsbc.com.hk

*Employed by a non-US affiliate of HSBC Securities (USA) Inc, and is not registered/ qualified pursuant to NYSE and/ or NASD regulations

% Year

	2005	2006	2007	2008f	2009f	2010f
Consumer spending	8.5	8.7	9.0	8.9	8.0	8.5
Government consumption	12.9	11.7	14.3	12.0	18.0	16.0
Fixed asset investment	27.2	24.5	25.8	26.1	20.0	20.0
Exports	29.0	25.0	23.8	11.2	-14.0	2.0
Imports	17.0	20.0	17.8	8.5	-10.0	1.0
GDP	10.4	11.6	13.0	9.0	7.8	8.5
Industrial production (ex-small enterprises)	15.9	16.2	17.1	12.9	9.5	12.0
Consumer prices	1.8	1.5	4.8	5.9	-0.6	0.8
Current account (% GDP)	7.2	9.5	11.0	8.6	5.1	4.4
Budget balance (% GDP)	-1.2	-1.0	0.6	-0.4	-2.5	-3.1
CNY/USD	8.18	7.93	7.54	6.88	6.81	6.80
1-year time deposit (%)	2.3	2.4	3.3	3.8	2.0	2.0
1-year lending (%)	5.6	5.9	6.8	7.0	4.9	4.8

Source: HSBC

Hong Kong SAR

Imported liquidity boom

Quantitative easing around the globe has spilled over into Hong Kong. Huge capital has flown into the asset markets of the territory since March. Together with the release of the pent-up capital since last December, we have seen both the equity and property markets roaring.

Nevertheless, the real economy remains sluggish. For example, retail sales value contracted 4.4% y-o-y over the first four months this year compared with growth of 1% in Q4 2008. Although the pace of contraction slowed in April, possibly because consumer sentiment improved on the booming asset markets, we expect the deteriorating labour market and consequent decline in household income to weigh on private consumption.

Local interest rates have plunged – one-month HIBOR fell as low as 0.05% in late May – on the excess liquidity. But the lower interest rate did not spur more lending. Banks remain conservative.

Loan growth has decelerated from double digits in 2008 to 2.9% y-o-y in Q1 2009 and contraction was recorded in March and April. Although banks may become less conservative in lending in coming months, we do not expect the trend to reverse significantly. Companies are still too bearish on the business outlook to expand.

There are signs the trade sector could reach the bottom soon. For example, monthly growth of Taiwan's export orders (sa), a leading indicator for China's exports, has rebounded from negative to positive territory in April. However, the developed economies are yet to recover, so their demand is unlikely to improve meaningfully.

We believe the recent liquidity boom has had limited impact on the real economy, so we maintain our real GDP forecast of a 4.5% decline y-o-y for 2009.

Janus Chan*
Economist
The Hongkong and Shanghai Banking Corporation Limited (HK)
+852 2996 6975
januschan@hsbc.com.hk

*Employed by a non-US affiliate of HSBC Securities (USA) Inc, and is not registered/ qualified pursuant to NYSE and/ or NASD regulations

% Year

	2005	2006	2007	2008f	2009f	2010f
Consumer spending	3.0	5.9	8.5	1.7	-1.6	1.4
Government consumption	-3.2	0.2	3.0	1.8	3.3	2.1
Fixed investment	4.1	7.1	3.4	-0.3	-1.4	8.9
Stockbuilding (% GDP)	-0.3	-0.1	0.8	0.6	-0.2	0.0
Domestic demand	1.5	5.9	7.9	0.8	-2.2	3.3
Exports	10.6	9.4	8.3	2.7	-18.6	-2.8
Imports	8.0	9.1	9.2	2.0	-18.4	-2.6
GDP	7.1	7.0	6.3	2.5	-4.5	2.4
Industrial production	2.5	2.2	-1.6	-6.4	-6.3	-6.8
Unemployment (%)	5.6	4.8	4.0	3.6	5.9	6.6
Retail sales	6.8	7.3	12.8	10.5	-4.0	3.0
Consumer prices	0.9	2.0	2.0	4.3	0.9	1.4
Goods & services balance (% GDP)	12.4	11.4	10.8	10.9	9.6	9.7
Budget balance (% GDP)	1.0	4.0	7.7	0.1	-4.0	-1.9
HKD/USD	7.77	7.77	7.80	7.77	7.79	7.80
3-month money (%)	3.1	4.3	4.3	2.4	0.6	0.5
Prime rate (%)	6.2	7.9	7.6	5.3	5.0	5.0

Source: HSBC

HSBC

India

A need for prudence

India looks to be on the road to recovery after a comparatively shallow downturn. Motor-vehicle sales and cement production have been trending higher for some time, but they have not always been good guides to the wider economy. Recent big improvements in the PMI and better industrial production numbers offer more solid grounds for hope. Although boosted by strong government consumption, January-March GDP also provided a pleasant surprise in growing by 5.8% y-o-y, not too distant from China's 6.1% increase for the same period.

As the impact of election-related spending wanes, other drivers will be needed to prevent the recovery from stalling. Luckily, there are several. In particular, the effects of the Reserve Bank's interest rate reductions have yet to be felt but will be in time as commercial banks show a greater willingness to pass on the reductions in the form of both lower lending and deposit rates. Additional oil and gas will also be pumped from Indian fields as the year progresses, and the country will benefit to some extent from the expected recovery in regional and world trade. Overall, we are happy to stick with our projections for 6.2% GDP growth in 2009/10, improving to 8% in 2010/11. These remain above consensus but to a lesser extent than three months ago.

Rather than the growth outlook, our bigger concerns relate to the fiscal position and inflation. A central government deficit of more than 6% of GDP in 2008/09 and a general government shortfall around 10% of GDP, with little indication as to how it will be brought down over the medium term, is attracting the attention of the rating agencies as well as keeping a floor under bond yields. Future divestments of government stakes in publicly-owned companies might help the situation but only temporarily.

As for India's key wholesale price measure, we expect a rapid transformation from deflation to inflation during the second half of this year as the impact of the strong rises in commodity prices are felt. This in turn will lead the RBI to start raising rates from the April-June quarter of next year.

More broadly, we expect the market to be disappointed by the speed and magnitude of economic reform.

Robert Prior-Wandesforde*
Economist
The Hongkong and Shanghai Banking Corporation Limited, Singapore branch
+65 6239 0840
robert.prior-wandesforde@hsbc.com.sg

*Employed by a non-US affiliate of HSBC Securities (USA) Inc, and is not registered/ qualified pursuant to NYSE and/ or NASD regulations

% Year

	2005	2006	2007	2008	2009f	2010f
GDP*	9.2	9.9	9.3	7.5	6.0	7.5
GDP (Financial year)**	9.5	9.7	9.0	6.7	6.2	8.0
Consumer prices	4.0	6.3	6.4	8.3	7.0	5.8
Current account (% GDP)	-1.9	-1.1	-1.0	-3.2	-2.2	-2.5
Budget balance (% GDP)	-4.2	-3.6	-2.8	-6.3	-7.0	-6.0
Broad money supply	16.1	19.6	21.8	20.1	18.0	18.0
INR/USD	44.0	45.1	40.7	44.6	51.7	54.0
3-month money (%)	5.7	7.0	8.3	9.2	6.9	6.7
Prime rate (%)	10.5	11.3	13.0	12.9	10.8	11.3

Note: * = calendar year; ** = based upon Indian fiscal year (April-March)
Source: HSBC

HSBC

Indonesia

Riding the storm well

Although Indonesia's growth slowed to 4.4% y-oy in the first quarter, this was much better than we were expecting and leaves the country a major outperformer in the ASEAN region. More interestingly, household consumption expenditure growth accelerated in Q1 to 5.8% year-on-year – the highest growth rate in a decade – as real disposable incomes got a boost from election-related cash handouts and softening inflation.

With consumer confidence on an upward trend, we expect household consumption to remain robust. There are, however, some weak points in the economy, mainly exports but also investment. The latter should drag down imports, limiting net trade's detraction to growth. For the year as a whole we have raised our average GDP forecast to 3.8% in 2009 from 2.5%. GDP is expected to accelerate to 5.3% next year helped by the region's recovery.

On the policy front Bank Indonesia (BI) has cut rates by a cumulative 250bp to 7%. However the pass through to the economy has been smaller, with lending rates having come off by roughly 100bp, putting pressure on BI to do more. Recent statements indicate that with inflation expected to be lower in the near-term, the central bank still has room to ease monetary policy, but not by that much. We now expect the bottom in rates to be 6.5% from 7% previously.

Inflation will, however, become an issue from Q4 onwards, once again because of commodity price effects. The bias would then be for rates to head up and we are pencilling in 50bp of hikes in the second half of 2010. However it may be time for BI to look more at core inflation than at the headline inflation rate.

The Presidential elections are scheduled for 8 July and in all likelihood Susilo BambangYudhoyono will come back to power, suggesting a steady economic policy and, ultimately, a positive result for investors.

Prakriti Sofat*
Economist
The Hongkong and Shanghai Banking Corporation Limited, Singapore branch
+65 6230 2879
prakritisofat@hsbc.com.sg

*Employed by a non-US affiliate of HSBC Securities (USA) Inc, and is not registered/ qualified pursuant to NYSE and/ or NASD regulations

% Year

	2005	2006	2007	2008	2009f	2010f
Consumer spending	4.0	3.2	5.0	5.3	4.8	5.1
Government consumption	6.6	9.6	3.9	10.4	11.6	5.4
Fixed investment	10.9	2.6	9.4	11.7	1.6	6.4
Stockbuilding (% GDP)	1.9	1.6	0.0	0.2	-0.1	-0.1
Domestic demand	6.3	3.2	4.1	7.7	4.3	5.4
Exports	16.6	9.4	8.5	9.5	-11.4	8.5
Imports	17.8	8.6	9.0	10.0	-14.0	9.5
GDP	5.7	5.5	6.3	6.1	3.8	5.3
Industrial production	4.6	4.6	4.7	3.7	2.0	4.6
Unemployment (%)	10.6	10.8	9.7	8.8	9.2	9.8
Consumer prices	10.5	13.1	6.4	10.2	5.7	8.3
Current account (% GDP)	0.1	3.0	2.4	0.1	0.6	-0.3
Budget balance (% GDP)	-0.5	-0.9	-1.3	-0.1	-3.0	-2.0
IDR/USD	9,840	9,135	9,176	9,730	11,799	12,000
3-month money (%)	9.0	11.9	8.1	9.3	8.1	6.7

Source: HSBC

HSBC

Malaysia

Short, sharp recession

We knew the Malaysian economy was weak in the first quarter, but not quite as bad as the GDP numbers revealed. The 6.2% y-o-y contraction was far worse than anything seen since the Asian crisis and, according to our estimates, consistent with an annualised 20% decline in q-o-q, seasonally adjusted terms. Private consumption fell 0.7%, fixed investment dropped 10.8% and exports plunged 15% all in y-o-y terms. The only crumb of comfort came from an unprecedented fall in inventories.

Despite the terrible start to the year, we have only made a small downward adjustment to our 2009 year average GDP growth forecast, from a 3.5% decline to a 3.8% decline. We have *raised* next year's number to a 6.3% gain from 5.5% growth previously. This reflects our heightened optimism in a strong, sustainable regional trade recovery starting from the second quarter of this year. Not only have several key short-term lead indicators gone vertical recently, but the hard data in several Asian countries have shown clear signs of improvement. Malaysia is also the key beneficiary within the region of stronger commodity prices and has yet to feel the full effects of either Bank Negara's interest rate cuts or the government's extra infrastructure spending. By early June, only MYR1.4bn of the MYR7bn November stimulus package had actually been spent with the rest in the pipeline.

On a more structural basis, we were encouraged by the new prime minister's recent liberalisation measures, including the dropping of the 30% bumiputra equity requirement in 27 service sectors. Also, with the governing UMNO party doing badly in the polls and a credible opposition in place, further reforms can be expected. This in turn bodes well for the country's chances of raising the investment share in GDP, which at little more than 20%, is too low to generate 6%-plus real growth on a sustained basis.

Inflation will turn to deflation in June but this will prove a short-term phenomenon. We suspect Bank Negara has now stopped reducing rates.

Robert Prior-Wandesforde*
Economist
The Hongkong and Shanghai Banking Corporation Limited, Singapore branch
+65 6239 0840
robert.prior-wandesforde@hsbc.com.sg

*Employed by a non-US affiliate of HSBC Securities (USA) Inc, and is not registered/ qualified pursuant to NYSE and/ or NASD regulations

% Year

	2005	2006	2007	2008	2009f	2010f
Consumer spending	9.1	6.8	10.4	8.5	-0.3	5.2
Government consumption	6.5	5.0	6.5	10.9	6.3	5.3
Fixed investment	5.0	7.5	9.6	0.8	-8.9	4.9
Stockbuilding (% GDP)	-0.7	0.1	-0.8	-1.5	-3.9	-0.9
Domestic demand	5.5	7.7	8.5	6.0	-4.1	8.8
Exports	8.3	6.6	4.5	1.3	-15.1	6.6
Imports	8.9	8.1	6.0	1.9	-16.9	9.0
GDP	5.3	5.8	6.2	4.6	-3.8	6.3
Industrial production	5.2	6.7	3.1	1.4	-8.9	6.8
Unemployment (%)	3.6	3.3	3.2	3.3	3.7	3.7
Consumer prices	3.0	3.6	2.0	5.4	0.4	3.2
Current account (% GDP)	15.0	16.3	15.7	17.6	12.3	10.2
Budget balance (% GDP)	-3.6	-3.3	-3.2	-4.8	-9.0	-6.5
MYR/USD	3.78	3.64	3.41	3.34	3.75	3.90
3-month interbank rate (%)	2.9	3.7	3.6	3.6	2.2	2.1

Source: HSBC

HSBC

Philippines

Brace for fiscal slippage

The effects of global financial frailty are now more pronounced in the Philippines: the economy shrank a seasonally adjusted 2.3% q-o-q in Q1. The economy is feeling the pinch from weakening external demand and foreign inflows. The country's hitherto stable external payment position may soon be unhinged as remittances begin to feel the chill from severe global headwinds. Despite some upside to our annual forecast – a 10.4% decline compared with a 20% decline previously – after considering positive growth in Q1 and the lagged effect of recession in the developed world, we stick to our forecast of a full 20% y-o-y contraction in the fourth quarter.

External upheaval also percolates through the real economy more broadly. The unemployment rate remains high, and the underemployment rate climbed to 18.9% in April, mirroring the rising tide of returning Overseas Filipino Workers. Private consumption growth has reached a historical low of 0.8% y-o-y in Q1. Still, we maintain our GDP growth forecast of 1% for 2009, taking into account the impact of abating inflation and the stimulus package (4.1% of GDP). The biggest challenge for the country is potential austerity on the fiscal front: slowing growth and structural bottlenecks have weakened revenue collection, while expenditure is rising because of pump priming. Moreover, political uncertainties around the resurrection of charter-change debate may exacerbate fiscal positioning. So, we see further deterioration in the fiscal metrics: the deficit may reach PHP292 billion (3.8% of GDP). This raises concern over the mounting debt-burden, which entails a future bias towards fiscal tightening.

To address growth concerns, central bank officials are likely to maintain an easing bias, not least because inflation is falling. But, we don't expect more than a 25bp cut (to 4%) given the fear of exchange rate volatility ultimately raising headline price pressures.

Frederic Neumann*
Economist
The Hongkong and Shanghai Banking Corporation Limited (HK)
+852 2822 4556
fredericnaumann@hsbc.com.hk

*Employed by a non-US affiliate of HSBC Securities (USA) Inc, and is not registered/ qualified pursuant to NYSE and/ or NASD regulations

% Year

	2005	2006	2007	2008	2009f	2010f
Consumer spending	4.8	5.5	5.8	4.7	1.7	2.6
Government consumption	2.3	10.4	6.6	3.2	12.2	9.2
Fixed investment	-6.6	3.9	10.9	2.9	-1.9	4.0
Stockbuilding (% GDP)	0.3	0.5	0.8	0.6	0.5	0.9
Domestic demand	2.0	5.7	7.0	4.0	1.7	3.6
Exports	4.8	13.4	5.4	-1.9	-8.7	3.8
Imports	2.4	1.8	-4.1	2.4	-10.2	4.0
GDP	5.0	5.3	7.1	3.8	1.0	3.0
Industrial production	5.3	4.2	3.3	4.3	-2.1	1.5
Unemployment (%)*	8.0	7.9	7.2	7.5	8.7	7.7
Consumer prices	7.7	6.3	2.8	9.3	3.5	4.8
Current account (% GDP)	2.0	4.5	4.8	2.5	1.4	-0.6
Budget balance (% GDP)	-2.7	-1.1	-0.2	-0.9	-3.8	-4.3
PHP/USD	55.0	50.9	45.2	45.3	50.4	53.0
3-month money (%)	6.1	5.2	3.4	5.6	4.9	6.0

Note: * Since Sep 2005, the ILO definition of unemployment has been adopted by official sources.
Source: HSBC

HSBC

Singapore

Heading for a "V"?

There are now tentative signs that Singapore's worst ever recession is over and we expect a strong V-shaped recovery to follow during the rest of this year.

Aside from big improvements in regional and global lead indicators, the country enjoyed a 17% rise in the level of non-oil domestic exports between January and May as well as better industrial production data. There are also plenty of anecdotal tales of the property market picking up, while financial services activity looks to be returning to more normal levels, construction continues to boom and tourist arrivals are falling less sharply.

Signs of a recovery, although still tentative at this stage, have arrived a little earlier than we expected and we have actually opted to raise our year average GDP growth projections for Singapore to -6% (from -7%) for 2009 and +5.3% (from +4.5%) for 2010. The former is at the bullish-end of the government's -6% to -9% forecast range.

Unfortunately, the recovery won't prevent unemployment from rising further in the next few months, while falling monthly earnings are also putting downward pressure on personal incomes. Consequently, consumer spending looks set to lag the upturn, although the government's job credit and training schemes as well as high personal savings and a bout of "good" deflation, brought about by huge year-on-year commodity price drops, should cushion the blow. The strong improvement in equity markets over recent months might, in time, also provide a positive wealth effect.

If we are right in our growth views then a further fiscal stimulus package is unlikely this year, while the Monetary Authority of Singapore will probably maintain the status quo at its October meeting rather than re-centre the currency band by moving it lower again.

Robert Prior-Wandesforde*
Economist
The Hongkong and Shanghai Banking Corporation Limited, Singapore branch
+65 6239 0840
robert.prior-wandesfore@hsbc.com.sg

*Employed by a non-US affiliate of HSBC Securities (USA) Inc, and is not registered/ qualified pursuant to NYSE and/ or NASD regulations

% Year

	2005	2006	2007	2008	2009f	2010f
Consumer spending	3.1	4.0	5.2	2.4	-3.5	4.3
Government consumption	9.6	6.6	2.2	8.1	4.5	5.2
Fixed investment	-2.0	13.3	19.2	13.7	-10.4	5.7
Stockbuilding (% GDP)	-1.4	-1.7	-3.2	2.8	5.6	5.3
Domestic demand	7.0	6.8	6.9	15.9	-1.7	4.5
Exports	11.7	11.7	8.7	1.3	-15.5	6.1
Imports	11.4	11.9	8.3	6.1	-14.8	5.9
GDP	8.7	8.4	7.8	1.1	-6.0	5.3
Industrial production	9.5	11.9	5.9	-4.2	-8.9	7.0
Unemployment (%)	3.2	2.7	2.2	2.1	3.6	3.8
Consumer prices	0.5	1.0	2.1	6.5	-0.3	2.3
Current account (% GDP)	27.5	25.4	23.5	14.8	10.3	9.0
Budget balance (% GDP)	-0.8	-0.2	0.6	1.7	2.7	-3.3
SGD/USD	1.67	1.58	1.49	1.40	1.52	1.56
3-month money (%)	2.2	3.4	2.7	1.5	0.7	0.9
Prime rate (%)	5.3	5.3	5.3	5.4	5.4	5.4

Source: HSBC

South Korea

Better data, at last

Confidence has returned to Korea. Industrial production and the services sector are showing tentative signs of improvement, while leading indices suggest that the recovery will endure. Still, it is unclear whether these trends will be sufficient to overcome the near-term external and internal challenges: exports continue to contract at over 20% year-on-year, although IT shipments are showing signs of life due to strong LCD and handset demand from China and the US.

Meanwhile, domestic demand still grapples with powerful headwinds. First, even though banks maintained credit growth through the crisis, a period of consolidation will eventually have to follow. Second, unemployment has stayed muted as firms hoarded labour, but sluggish output will nevertheless fuel lay-offs in the months ahead. Third, household debt remains elevated: while not a source of potential banking sector instability, high leverage will nevertheless restrain the pace of consumption growth. Lastly, fiscal spending measures and tax cuts are expected to drag the fiscal deficit upward to some 4% of GDP this year, pushing gross public debt to 36% of GDP from 29% only a few years ago.

Korea, in short, faces structural challenges, which will prevent a rapid rebound in domestic demand. We recently raised our GDP growth forecasts to -2.3% from -3.7% for 2009, in light of better than expected data over the last two quarters. But we still expect only a gradual rebound to 3.6% growth in 2010, a pace well below potential for the Korean economy. Price pressures will stabilize with sluggish domestic demand, and we therefore expect the Bank of Korea to stay on hold for at least another 12 months.

Frederic Neumann*
Economist
The Hongkong and Shanghai Banking Corporation Limited (HK)
+852 2822 4556
fredericneumann@hsbc.com.hk

*Employed by a non-US affiliate of HSBC Securities (USA) Inc, and is not registered/ qualified pursuant to NYSE and/ or NASD regulations

% Year

	2005	2006	2007	2008	2009f	2010f
Consumer spending	4.6	4.7	5.1	0.9	-2.6	2.6
Government consumption	4.3	6.6	5.4	4.2	6.3	3.5
Fixed investment	1.9	3.4	4.2	-1.7	-5.1	5.6
Stockbuilding (% GDP)	0.8	1.1	0.8	1.5	-0.4	0.0
Domestic demand	3.9	4.9	4.5	-0.1	-2.0	3.6
Exports	7.8	11.4	12.6	5.7	-7.0	5.5
Imports	7.6	11.3	11.7	3.7	-10.9	6.9
GDP	4.0	5.2	5.1	2.2	-2.3	3.6
Industrial production	6.3	8.4	6.9	3.1	-6.6	7.2
Unemployment (%)	3.7	3.5	3.2	3.2	4.0	4.0
Retail sales	4.3	4.9	4.4	0.1	3.0	4.5
Consumer prices	2.8	2.2	2.5	4.7	2.7	3.2
Current account (% GDP)	1.9	0.6	0.6	-0.7	2.1	-0.1
Budget balance (% GDP)	0.4	0.4	3.8	1.2	-4.0	-1.3
KRW/USD	1,026	950	929	1,127	1,311	1,200
3-month CD yield (%)	3.6	4.5	5.2	5.5	2.6	2.7
5-year treasury yield (year-end)	4.7	4.9	5.4	5.2	4.5	4.5

Source: HSBC

HSBC

Taiwan

The worst is behind us

Taiwan's economy is certainly the most exposed in Asia to the current global slowdown. In the first quarter, real GDP contracted by a record 10.2% y-o-y after -8.6% in Q4 2008 – a far more severe recession than Taiwan suffered during the 2001 tech bust.

On the brighter side, however, recently improving data suggest that the island's economy has bottomed out and that a gradual recovery is materialising. To be sure, external demand from the developed market is bound to remain weak for the rest of the year, but deepening cross-straits economic relations, such as tourism and procurement missions, will serve as a buffer to mitigate the island's slump in domestic demand and exports. Overall, we believe the worst is behind us, but the recovery process is bound to be slow and Taiwan is still far from having fully bounced back: we still expect the economy to contract by 5.1% in 2009, after growing by just 0.1% in 2008.

In 2010, a gradual rise in demand from the developed countries will help to sustain the recovery in the island's industrial production and exports. We expect the island's economy to expand by 4.4% in 2010. However, 2010 growth will be constrained and below trend because economic conditions elsewhere remain fragile and the island's domestic demand is not sufficient to deliver a robust recovery.

Mild deflation will persist over the course of 2009 in the wake of sluggish domestic demand and lower commodity prices. Nevertheless, inflationary pressure is likely to return in 2010 with global economic conditions recovering, something that will affect headline prices in particular through rising costs for commodities. Also, low interest rates and abundant liquidity will likely inflate asset prices. We therefore expect Taiwan's inflation to rise 1.2% y-o-y in 2010 after -0.7% in 2009. Furthermore, we expect policy-makers to step into a tightening cycle in 2010, with the policy rate rising to 1.75% by the end of next year from 1.25% currently.

Frederic Neumann*
Economist
The Hongkong and Shanghai Banking Corporation Limited (HK)
+852 2822 4556
fredericneumann@hsbc.com.hk

Christopher Wong*
Economist
The Hongkong and Shanghai Banking Corporation Limited (HK)
+852 2996 6917
christopherwong@hsbc.com.hk

*Employed by a non-US affiliate of HSBC Securities (USA) Inc, and is not registered/ qualified pursuant to NYSE and/ or NASD regulations

% Year

	2005	2006	2007	2008	2009f	2010f
Consumer spending	3.0	1.8	2.3	-0.3	-0.4	2.1
Government consumption	1.1	-0.4	0.9	1.1	3.4	2.0
Fixed investment	1.2	0.9	1.9	-10.6	-17.9	3.8
Stockbuilding (% GDP)	0.1	0.3	0.4	0.3	-0.9	-0.6
Domestic demand	1.7	1.5	2.2	-2.4	-4.9	2.7
Exports	7.6	10.3	8.8	0.0	-13.9	8.7
Imports	3.8	5.6	3.8	-4.0	-16.6	7.1
GDP	4.2	4.8	5.7	0.1	-5.1	4.4
Industrial production	3.8	4.7	7.8	-1.8	-16.5	6.0
Unemployment (%)	4.1	3.9	3.9	4.1	5.8	6.0
Consumer prices	2.3	0.6	1.8	3.5	-0.7	1.2
Current account (% GDP)	4.9	7.2	8.6	6.3	8.9	8.3
Budget balance (% GDP)	-0.6	-0.6	-0.2	-0.8	-4.5	-3.5
TWD/USD	32.3	32.6	32.7	31.4	33.4	31.8
3-month CD (%)	1.4	1.6	2.0	2.1	0.6	1.2
Prime rate (%)	3.7	4.0	4.1	4.4	2.8	2.8

Source: HSBC

HSBC

Thailand

Timing the turn

The Thai economy contracted by 7% in year-on-year terms in Q1 – the worst fall since the 1998 crisis – pulled down by the collapse in investment, exports and consumption. However things are beginning to look better with monthly manufacturing and exports data showing signs of improvement, and business confidence turning. Overall then, growth is set to improve in sequential terms given stabilising global activity indicators and increasing policy pass through, although average annual growth will still be a dismal -3.5% in 2009. For 2010 we look for GDP to rise by 3.5%.

The improving growth outlook should ensure that the current policy rate of 1.25% proves to be the bottom in this cycle, barring a new shock to the global picture or a political development at home. However, as inflation starts picking up from Q4 onwards, we think the central bank will hike rates by 75bp in H2 2010.

Given that monetary policy has been somewhat blunted in this cycle, as commercial banks have passed on less than half of the policy easing, the key support to growth has to come from the government. Here it is heartening to know that 70% of the THB1.4trn (16% of 2009 GDP) second stimulus plan (spent over the next 3-years) is in 'shovel ready' projects and, once the funds are in hand, disbursal should take place in a timely fashion. The big spending, however, means that the budget deficit is going to widen substantially, with the bond market no doubt feeling pressures of supply.

On the external accounts, with imports expected to contract by more than exports – given favourable price effects – the trade surplus will remain sizeable. However tourism and foreign direct investment flows are expected to be lacklustre. This, together with the policy bias, points towards a weaker currency, and we look for USD/THB to rise to 37 by year-end.

Prakriti Sofat*
Economist
The Hongkong and Shanghai Banking Corporation Limited, Singapore branch
+65 6230 2879
prakritisofat@hsbc.com.sg

*Employed by a non-US affiliate of HSBC Securities (USA) Inc, and is not registered/ qualified pursuant to NYSE and/ or NASD regulations

% Year

	2005	2006	2007	2008	2009f	2010f
Consumer spending	4.9	3.0	1.6	2.5	-0.4	2.5
Government consumption	11.4	2.4	9.2	0.5	6.9	6.5
Fixed investment	10.5	3.9	1.3	1.1	-8.8	5.8
Stockbuilding (% GDP)	2.0	0.3	0.1	1.4	-0.3	0.1
Domestic demand	7.5	1.3	2.0	3.5	-3.9	4.2
Exports	4.2	9.1	7.1	5.4	-11.7	5.0
Imports	8.9	3.3	3.4	7.5	-14.3	6.2
GDP	4.7	5.2	4.9	2.6	-3.5	3.5
Industrial production	5.2	6.0	6.2	3.9	-2.2	4.3
Unemployment (%)	1.9	1.5	1.4	1.4	2.5	3.3
Consumer prices	4.5	4.6	2.2	5.5	-1.4	2.7
Current account (% GDP)	-4.3	1.1	5.9	-0.1	4.0	2.1
Budget balance (% GDP)	0.3	1.2	-2.3	-1.1	-6.3	-6.1
THB/USD	40.6	37.6	34.7	33.5	35.5	38.8
3-month interbank rate (%)	3.3	5.2	4.0	3.6	1.7	1.8

Source: HSBC

Vietnam

The worst is over

Prakriti Sofat*
Economist
The Hongkong and Shanghai Banking Corporation Limited, Singapore branch
+65 6230 2879
prakritisofat@hsbc.com.sg

*Employed by a non-US affiliate of HSBC Securities (USA) Inc, and is not registered/ qualified pursuant to NYSE and/ or NASD regulations

Economic growth in the first quarter was just 3% y-o-y, the lowest in a decade. However we believe that things are going to start improving from the second quarter onwards given the impact of the massive policy easing, the bulk of which was delivered in the later part of 2008. At the same time the government has increased the size of its fiscal stimulus plan by USD2bn to USD8bn (8.6% of 2009 nominal GDP), including USD5.2bn on infrastructure projects.

Arguably the most successful policy response, however, has been the introduction of a 4ppt interest rate subsidy for corporates, which has encouraged some USD18bn worth of loan creation in the first half of the year, the same as we saw in the whole of 2008. The fact that so much lending has gone through so quickly suggests an element of pent-up demand, so growth should improve. However, in the coming quarters we will have to look into the quality of that lending and hence the likely repercussions for the banking system.

On the inflation front things have cooled off very rapidly, with our forecast for year average inflation being 7.5%. Note, however, that price pressures are expected to start building from the end of the year as the rise in commodity prices feeds through.

Vietnam saw a trade surplus in the first quarter, largely on the back of massive re-exports of gold, but we are now back to deficits. The latter are something we expect to continue given that the country still remains in early stages of development and hence has to import large quantities of capital/intermediate goods. Nevertheless the deficit is going to be much smaller this year than it was in 2008. For the currency we think some further depreciation is in order given weakening remittances, foreign direct investment and tourist inflows.

% Year

	2005	2006	2007	2008	2009f	2010f
Consumer spending	7.3	8.3	9.6	7.3	3.0	6.0
Government consumption	8.1	8.6	9.0	5.8	6.5	6.0
Fixed investment	9.7	9.9	23.0	13.2	3.0	6.3
Exports - Goods	22.5	22.1	22.7	29.9	-5.4	12.2
Imports - Goods	15.7	33.4	41.2	28.5	-15.1	13.0
GDP	8.4	8.2	8.5	6.2	4.5	6.5
Industrial production	25.5	16.0	11.6	11.8	5.2	11.5
Unemployment (%)	5.3	4.8	4.6	4.7	5.4	5.3
Consumer prices	8.3	7.5	8.3	23.0	7.5	10.1
Current account (% GDP)	-1.1	-0.3	-9.8	-11.6	-5.6	-4.7
Budget balance (% GDP)	-4.9	-5.0	-5.0	-5.0	-8.0	-7.0
VND/USD	15,866	16,006	16,096	16,759	17,962	18,200
Short-term lending rate (%)	7.8	7.8	8.3	8.5	7.0	8.0
5-year interest rate (%)*	8.8	8.3	8.7	10.0	8.5	8.5

Note: * end-year. Source: HSBC

Notes

Disclosure appendix

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Issuer of report
HSBC Bank plc
8 Canada Square, London
E14 5HQ, United Kingdom
Telephone: +44 20 7991 8888
Fax: +44 20 7992 4880
Website: www.research.hsbc.com

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[245274]

Global Economics Research Team

Global

Stephen King
Global Head of Economics
+44 20 7991 6700 stephen.king@hsbcib.com

Stuart Green
+44 20 7991 6718 stuart1.green@hsbcib.com

Europe

Janet Henry
Chief European Economist
+44 20 7991 6711 janet.henry@hsbcib.com

Astrid Schilo
+44 20 7991 6708 astrid.schilo@hsbcib.com

Germany
Lothar Hessler
+49 21 1910 2906 lothar.hessler@hsbctrinkaus.de

France
Mathilde Lemoine
+33 1 4070 3266 mathilde.lemoine@hsbc.fr

United Kingdom
Karen Ward
+44 20 7991 3692 karen.ward@hsbcib.com

North America

Ian Morris
+1 212 525 3115 ian.morris@us.hsbc.com

Ryan Wang
+1 212 525 3181 ryan.wang@us.hsbc.com

Stewart Hall
+1 416 868 7523 stewart_hall@hsbc.ca

Global Emerging Markets

Philip Poole
+44 20 7992 3683 philip.poole@hsbcib.com

Wietse Nijenhuis
+44 20 7992 3680 wietse.nijenhuis@hsbcib.com

Asia Pacific

Qu Hongbin
+852 2822 2025 hongbinqu@hsbc.com.hk

Robert Prior-Wandesforde
+65 6239 0840 robert.prior-wandesforde@hsbc.com.sg

Frederic Neumann
+852 2822 4556 fredericneumann@hsbc.com.hk

Seiji Shiraishi
+81 3 5203 3802 seiji.shiraishi@hsbc.co.jp

Prakriti Sofat
+65 6230 2879 prakritisofat@hsbc.com.sg

Janus Chan
+852 2996 6975 januschan@hsbc.com.hk

Song Yi Kim
+852 2822 4870 songyikim@hsbc.com.hk

Christopher Wong
+852 2996 6917 christopherwong@hsbc.com.hk

Yukiko Tani
+81 3 5203 3827 yukiko.tani@hsbc.co.jp

Sophia Ma
Associate

Sun Junwei
Associate

Emerging Europe, Middle East and Africa

Juliet Sampson
+44 20 7991 5651 juliet.sampson@hsbcib.com

Kubilay Ozturk
+44 20 7991 6045 kubilay.ozturk@hsbcib.com

Alexander Morozov
+7 495 783 8855 alexander.morozov@hsbc.com

Murat Ulgen
+90 21 2366 1625 muratulgen@hsbc.com.tr

Simon Williams
+971 4507 7614 simon.williams@hsbc.com

Latin America

Jonathan Heath
Chief Economist, Latin America
+52 55 5721 2176 jonathan.heath@hsbc.com.mx

Argentina
Javier Finkman
Chief Economist, South America ex-Brazil
+54 11 4344 8144 javier.r.finkman@hsbc.com.ar

Ramiro D Blazquez
Senior Economist
+54 11 4348 5759 ramiro.d.blazquez@hsbc.com.ar

Brazil
Andre Loes
Chief Economist
+55 11 3371 8184 andre.a.loes@hsbc.com.br

Tatiana G Gomes
Senior Economist
+55 11 3371 8183 tatiana.g.gomes@hsbc.com.br

Mexico
Sergio Martin
Chief Economist
+52 55 5721 2164 sergio.martinm@hsbc.com.mx

Central America
Lorena Dominguez
Economist
+52 55 5721 2172 lorena.dominguez@hsbc.com.mx

Principal contributors

Stuart Green*
Economist
HSBC Bank plc
+44 20 7991 6718
Stuart1.green@hsbcib.com

Stuart Green is HSBC's Global Economist. Prior to joining HSBC in August 2007, Stuart worked as an economist at a number of the world's largest financial institutions, covering the UK, European and US economies.

Janet Henry*
Economist
HSBC Bank plc
+44 20 7991 6711
Janet.henry@hsbcib.com

Janet Henry was appointed as HSBC's Chief European Economist in April 2007. She joined HSBC in 1996 in Hong Kong where she worked as an Asian Economist in the run-up to, and aftermath of, the Asian crisis before moving back to London in 1999 where she was a Global Economist for eight years. Janet's career began at the Economist Intelligence Unit where she worked as an Asian economist for over four years in London and Hong Kong after graduating with an Economics degree from University College London.

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