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Economic Weather Forecast for Europe 2012

London, May 2012

Economic Weather Map

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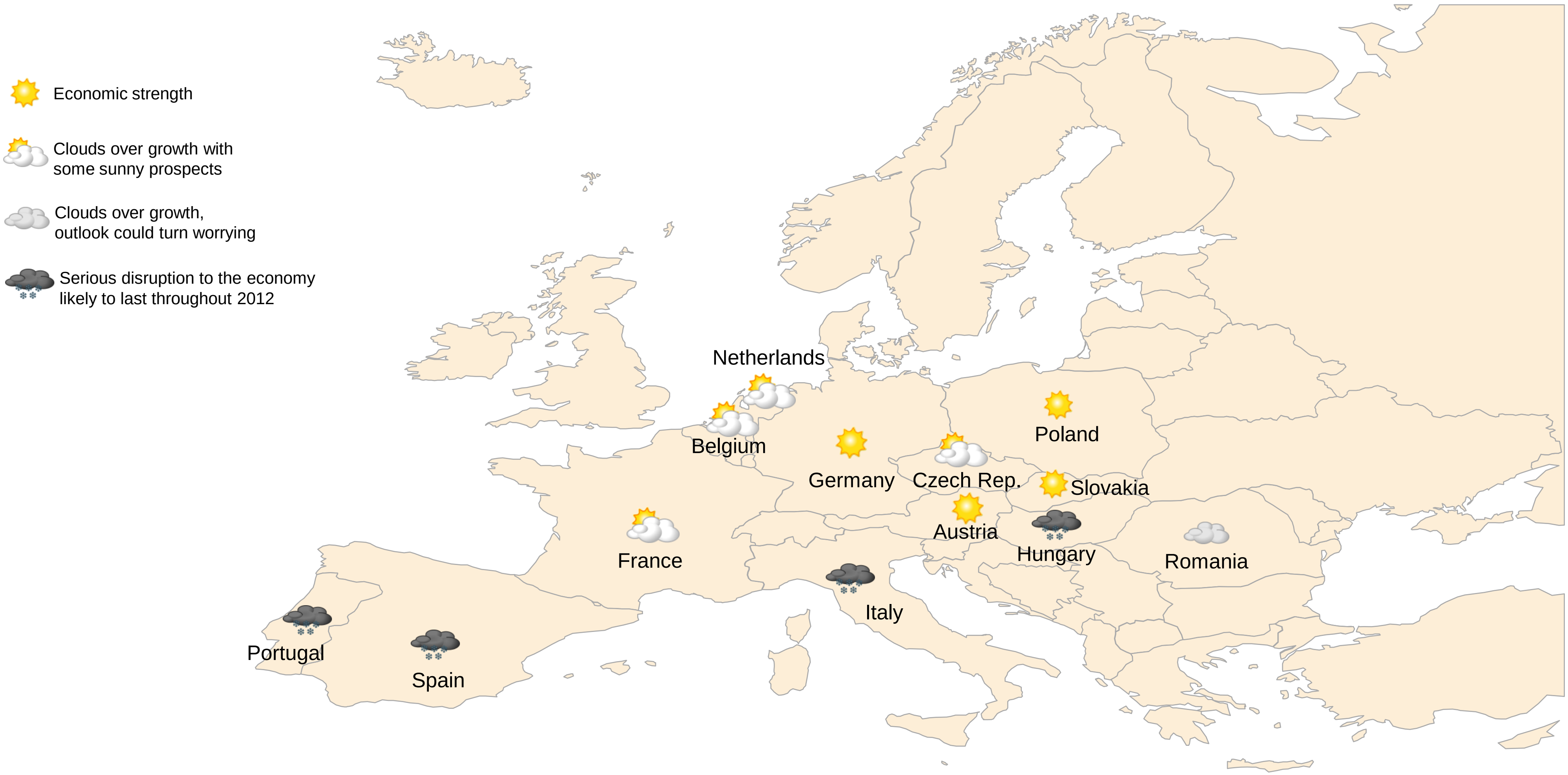
Based on economic growth, inflation, unemployment and credit / bank stress



Source: Petrus Advisers analysis.

Executive Summary

- Our macro analysis is based on several economical and financial indicators :
  - Expected GDP growth and inflation
  - Labour market changes and unemployment forecast
  - Banks and credit environment (government bond yields, bank ROEs and the changes in nonperforming loans to total loans ratio)

- Austria and Germany are expected to show relatively strong performance. The latest statistics confirm that Germany grew by a 0.5% in on a quarter to quarter basis in Q1 2012 [1], equivalent of 1.7% year over year[1]
- The major outliers are :
  - the Netherlands, which is expected to have a contraction of GDP for the year 2012 of 0.9%; and
  - Hungary expected to show a decrease in its GDP of more than 0.3% as forecasted by European Commission[2]
- Italy, Portugal and Spain are expected to experience contracting economic activity, significant unemployment rates will persist
- Central Europe provides mixed quarterly results and similarly the forecasts vary country to country.
  - Czech Republic surprised on the downside with a 1% quarter on quarter decrease[3] in Q1 2012, due to one-off factors
  - Poland and Slovakia continue to show strong export driven growth (forecasted GDP growth in 2012 of 2.7% and 1.8% respectively)
  - Hungary remains the sick man of Central Europe with no indicators for positive developments in 2012

Source: Petrus Advisers analysis, Financial Times , Barclays, European Commission.

1) *tradingeconomics.com.*
2) *European Commission.*
3) *Barclays.*

Core EU Countries

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Stabilizing pan-european growth rates

Germany

- Surprising strong GDP growth in Germany in the first quarter 2012 by 0.5%[1] year over year fueled primarily by domestic consumption on the back of good unemployment figures and the growing real income
- Moreover renewed fears of Greek exit from Eurozone drive the 10 year German government bond yields to new historical lows of 1.4%[2]
- With inflation at 2.3% and not showing signs of acceleration and the oil prices down it is likely that the internal consumption may provide further fuel to the economy without a real danger of inflation picking-up

Austria

- Has one of the lowest unemployment rates amongst the EU countries with 4.2%[3] in 2011, which together with a solid corporate and household balance sheet may drive the domestic consumption and investments higher
- Economic growth expected at 0.8% for 2012

France

- Troubled by weak consumption and high unemployment of around 10%[3]
- There are indications that the demand might increase in the near term, but the weak labour market is expected to continue putting weight on the growth

Source: Petrus Advisers analysis, Financial Times, European Commission.

1) *Financial Times.*
2) *tradingeconomics.com.*
3) *European Commission.*

Peripheral Europe

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Continued issues

Spain

- Stagnant economy and one of the highest unemployment rates in Europe, Spain remains the focus point of speculation
- Downgrade of 16 of its banks, rescue of market leader Bankia, potentially the Hypo Real Estate of Spain
- Lower labor costs due to highest unemployment rate in EU give Spain a strong support to the export. This may create a case for stabilization of the economy in 2013 – 2014 and reversal in unemployment rates, reported at 24.4%[2] at the end of first quarter 2012

Portugal

- Good pupil of the Troika demands? Despite increasing unemployment, current government is keeping the austerity measures in place (2012 deficit / GDP forecast at 4.7%)[3]
- Portuguese banks seem to be in a relatively stable position, with some of the large banks recently raising new equity capital and the existence of an unused €12bn[4] package to provide liquidity to Portuguese banks.

Italy

- Austerity measures and low economic confidence translating into weak consumption elevated costs of the sovereign debt
- Italy has one of the highest NPLs ratios in the EU.
- No major positive surprises from Italy expected, the forecasted contraction of the economy by 1.4%[3] in 2012

Source: Petrus Advisers analysis, Financial Times, European Commission, tradingeconomics.com, www.agenciafinanceira.iol.pt.

1) *Financial Times.*
2) *tradingeconomics.com.*
3) *European Commission.*
4) *www.agenciafinanceira.iol.pt.*

CEE Countries

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Delivering mixed results

Czech Republic

- Disappointing : Q1 2012 GDP -1% quarter over quarter and -1% year over year[1], against expectation of moderate growth by analysts. Hence GDP expected flat in 2012 however forecasted to grow by 2.1% again in 2013
- Lower output in construction, both public and private spending and a slowdown in net export growth due to lower demand in export countries and inflation picked up in 2012 due to food, energy and hike in VAT (3.3% expected headline inflation for 2012)
- However healthy financial sector (Czech Republic is a net creditor and loan to deposit ratio at the level of 70% roughly), low indebtedness of households, and government bond yields in national currency at low levels (currently at as low as 3.3%) as a result of the government's commitment to the fiscal discipline (estimated 3.1% fiscal deficit for 2011 and expected to stay at that level going forward)[2]
- In combination with expected increase in domestic and external demand in later years underpins good macro-outlook for 2013 and onwards

Slovakia

- Positive : Q1 2012 GDP growth of 0.8% quarter over quarter and 3.1% year over year vs. consensus of 0.2% and 2.6% respectively[3]
  - Export - expansion of car production, automotive posted +25% year over year growth in Q1 2012[3]
  - Banks with generally healthy liquidity however weak internal demand

Source: Petrus Advisers analysis, Barclays, RCB, IMF, European Commission.

1) *Barclays.*
2) *IMF.*
3) *RCB.*

CEE Countries (cont.)

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Delivering mixed results

Hungary

- Negative : Q1 2012 GDP contraction of 1.3% quarter on quarter and -0.7% (on seasonally and calendar adjusted basis -1.5%) year over year vs. consensus of -0.5% year over year[1]
- Export brings GDP slowdown
- Weak private and public consumption due to austerity measures (also financial transaction tax impact for the future)
- Construction industry dropped heavily
- Agro – late season and 30% growth in 2011 helped GDP adding 0.9% to overall GDP growth, in 2012 agro expected to fall back by 10%[1]
- Mercedes and Audi expanding however Nokia and Malev and some others closing down, netto zero impact on GDP
- Spring forecast of -0.3% for 2012 and 1% for 2013 by EU Commission[2], may be too optimistic

Poland

- Stability : 25bps hike in the NBP interest rate in May 2012 is rather surprising given that there are no signs of accelerating inflation[3]
- Poland retains solid GDP growth, strong internal demand leads to expected GDP growth of 2.7%[2] for 2012

Romania

- Flat : Q1 2012 GDP of -0.1% quarter on quarter and 0.3% year over year, consensus was +1.2% year over year[3]
- External demand indications point to lower export
- In our view, EU Commission forecasts of 1.4% and 2.9%[2] for 2012, 2013, may be too optimistic

Source: Petrus Advisers analysis, Barclays, European Commission, RCB.

1) Barclays.

2) European Commission.

3) RCB.

Key Statistics

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all figures in %	GDP				Unemployment				Inflation				10 y gov bonds yield			NPLs / Loans			Bank's ROE			Loans / Deposits
	2010	2011		2012 F	2010	2011		2012 F	2010	2011		2012 F	May-11		May-12	2010		2011	2010		2011	2010
Austria	2.3	3.1	🔴 ⇩	0.8	4.4	4.2	🟡 ⇧	4.3	1.7	3.6	🟢 ⇩	2.4	3.8	🟢 ⇩	2.5	2.8	🟡 ⇩	2.7	7.9	🟢 ⇩	1.4	1.2
Germany	3.7	3.0	🔴 ⇩	0.7	7.1	6.0	🟡 ⇩	5.5	1.2	2.5	🟡 ⇩	2.3	3.4	🟢 ⇩	1.4	3.7		n/a	8.8		n/a	1.0
Poland	3.9	4.3	🔴 ⇩	2.7	9.6	9.6	🟡 ⇧	9.8	2.5	4.3	🟡 ⇩	3.7	6.3	🟢 ⇩	5.5	8.8	🟡 ⇩	8.2	13.2	🔴 ⇧	16.6	1.2
Czech Republic	2.7	1.7	🔴 ⇩	0.0	7.3	6.7	🟡 ⇧	7.2	1.5	1.9	🔴 ⇧	3.3	4.2	🟢 ⇩	3.3	5.4	🟡 ⇧	5.5	19.7	🟡 ⇩	18.7	0.8
Slovak Republic	4.2	3.3	🔴 ⇩	1.8	14.4	13.4	🟡 ⇩	13.2	0.7	4.1	🟢 ⇩	2.9	4.3	🟢 ⇩	3.7	5.8	🟡 ⇩	5.6	12.6	🔴 ⇧	14.5	0.8
Hungary	1.3	1.7	🔴 ⇩	-0.3	11.2	11.0	🟡 ⇩	10.6	4.9	3.9	🔴 ⇧	5.5	8.0	🟡 ⇧	8.5	9.8	🔴 ⇧	13.3	1.2	🟢 ⇩	-3.9	1.5
Italy	1.8	0.4	🔴 ⇩	-1.4	8.4	8.4	🔴 ⇧	9.5	1.6	2.9	🟡 ⇧	3.2	4.8	🟡 ⇧	5.8	10.0	🔴 ⇧	11.0	3.7	🟢 ⇩	2.2	1.3
Spain	-0.1	0.7	🔴 ⇩	-1.8	20.1	21.6	🔴 ⇧	24.4	2.0	3.1	🟢 ⇩	1.9	5.3	🟡 ⇧	6.3	8.2	🔴 ⇧	11.8	7.9	🟡 ⇩	7.5	1.1
Portugal	1.4	-1.6	🔴 ⇩	-3.3	10.8	12.7	🔴 ⇧	15.5	1.4	3.6	🟡 ⇩	3.0	8.5	🔴 ⇧	11.8	5.2	🔴 ⇧	6.9	7.5	🟢 ⇩	2.3	1.5
Ireland	-0.4	0.7	🟡 ⇩	0.5	13.6	14.4	🟡 ⇩	14.3	-1.6	1.1	🟡 ⇧	1.7	10.0	🟢 ⇩	8.2	8.6	🔴 ⇧	14.7	-66.5	🔴 ⇧	-8.6	1.6
Romania	-1.6	2.5	🔴 ⇩	1.4	7.3	7.2	🟡 ⇩	7.2	6.1	5.8	🟢 ⇩	3.1	7.5	🟢 ⇩	6.9	11.9	🔴 ⇧	14.1	-1.7	🟢 ⇩	-3.4	1.2
Netherlands	1.7	1.2	🔴 ⇩	-0.9	4.5	4.5	🔴 ⇧	5.7	0.9	2.5	🟡 ⇧	2.5	n/a		6.7	2.8	🟡 ⇩	2.7	7.1	🟢 ⇩	5.4	1.0
Belgium	2.2	1.9	🔴 ⇩	0.0	8.3	7.2	🟡 ⇧	7.6	2.3	3.5	🟡 ⇩	2.9	3.7	🟢 ⇩	1.9	2.8	🟡 ⇧	2.8	10.7	🟢 ⇩	0.7	1.2
France	1.7	1.7	🔴 ⇩	0.5	9.8	9.7	🟡 ⇧	10.2	1.7	2.3	🟡 ⇩	2.1	4.3	🟢 ⇩	3.3	3.8	🟡 ⇩	3.7	12.0	🔴 ⇧	13.1	0.7

Source: Petrus Advisers analysis., IMF, Eurostat, EBF, tradingeconomics.com, bloomberg.com, forexpros.com, National Bank of Romania.

1) *GDP, Unemployment and Inflation - actuals and forecasts taken from European Commission 2012 Spring Forecast.*
2) *10 year government bonds yield taken from tradingeconomics.com, bloomberg.com, forexpros.com and National Bank of Romania.*
3) *NPLs / Loans and Bank's ROE taken from IMF.*

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