

Revisions since last month (in brackets forecasts as per previous month)

	GDP 2010				GDP 2011				CPI 2010				CPI 2011			
	SLAM		Consensus		SLAM		Consensus		SLAM		Consensus		SLAM		Consensus	
USA	3.2%	(3.5%)	3.3%	(3.2%)	2.5%		3.1%		1.9%	(2.1%)	2.0%	(2.1%)	2.0%		1.9%	
Euro Area	0.9%	(1.0%)	1.1%	(1.2%)	1.3%	(1.6%)	1.5%		1.3%	(1.2%)	1.3%	(1.2%)	1.2%	(0.9%)	1.4%	
Japan	3.1%	(2.4%)	2.4%	(2.2%)	1.2%	(1.3%)	1.7%	(1.6%)	-0.7%	(-0.4%)	-1.0%	(-1.1%)	0.0%	(0.1%)	-0.2%	
UK	1.1%	(1.3%)	1.3%		1.5%	(1.8%)	2.3%		2.9%	(2.3%)	2.9%	(2.7%)	2.4%	(0.6%)	1.8%	(1.7%)
Switzerland	2.0%	(2.1%)	1.9%	(1.8%)	1.6%		1.9%		1.2%	(1.1%)	1.0%		0.8%		1.0%	(1.1%)

USA – Healing labour market

GDP Growth

Swiss Life Asset Management	Consensus
2010: 3.2%	2010: 3.3%
2011: 2.5%	2011: 3.1%

Over the past four weeks, macroeconomic data managed to surprise market participants positively in most of the cases. Although this did not fall on fertile grounds with investors worried about a debt crisis, incoming indicators underlined the sustainability but also the differing speed of the recovery in developed countries with the US once again exhibiting stronger dynamics. Although first quarter GDP was reported at a lower level than what we had built into our front-loaded growth path, the composition of growth was sound and highlighted a broadening of the recovery across the economy. The contribution to total GDP growth by personal consumption was twice as strong as in the preceding quarter. Pent-up demand by private households was satisfied on the back of improving labour market conditions and sound income perspectives. Strong payroll growth in the private sector in April and the re-entering of formerly discouraged workers into the labour force, which temporarily caused the unemployment rate to slide up a notch, substantiate a rather constructive outlook for personal consumption over the coming quarters. As a matter of fact, our own forecast for second quarter average payroll gain of 250,000 per month likely gets dwarfed by the actual figures. The unemployment rate should drop to 9.0% or even below till the end of the year from 9.9% currently. Federal Reserve policy makers just stated that the natural rate of unemployment was between 5.0 and 5.3 percent. Should this NAIRU however have risen more than they estimate, as more workers lost their jobs on a permanent basis, the central bank runs the

Source for Consensus Estimates: Consensus Economics Inc. London, 10 May 2010

risk of sitting at the zero line for the fed funds rate while full employment is not as far away as they think. Although capital spending by businesses was rather tepid thus far in this recovery phase and its contribution to growth certainly below average, durable goods orders do not point at a renewed faltering of corporate activity. In line with the strong industrial revival we have witnessed since the cyclical lows, the manufacturing PMI has reached former record levels and should start to roll over. Although the latest reading for May slipped slightly from elevated levels, the employment subcomponent continued its upward trajectory, rising to a six-year high of 59.8 from 58.5 in April. The supply overhang in the market for new homes has largely been worked off, actually dropping below the long-term average. Home buyers rushed to sign contracts before the expiration of the homebuyer tax credits on 30 April, yet they have time until the end of June to actually close the sale. This will hold up sales figures over the next months. We expect the post-tax credit housing “hangover” to be shallow, similar to what was the case following the cash-for-clunkers auto sales initiative.

Inflation

Swiss Life Asset Management	Consensus
2010: 1.9%	2010: 2.0%
2011: 2.0%	2011: 1.9%

The huge seasonal factor for gasoline prices in April led to a negative contribution from this component and caused the headline rate to drop back to 2.2%. Equally so, industrial commodities prices have moderated substantially over the past weeks. Despite a healing labour market and rising capacity utilisation rates, we are still far from levels that would cause price pressures to rise.

Euro Area – Fiscal straight-jacket

GDP Growth

Swiss Life Asset Management	Consensus
2010: 0.9%	2010: 1.1%
2011: 1.3%	2011: 1.5%

In the face of drastic fiscal austerity measures, some non-core member countries risk to fall back into recession. Yet, given the strong economic momentum, the risks to our own forecast do not emanate primarily from the private sector but from economic policy. Countries of the periphery did not only drop into the debt trap due to the cyclical downturn and irresponsible fiscal policy, but they have structural shortcomings to tackle such as persistently high unit labour costs which undercut competitiveness. Growth-wise, the weakness of the periphery can be compensated by strong fundamentals in core Europe, as export-oriented sectors benefit from Euro weakness and an environment of record low interest rates. Sentiment as well as real activity data have remained robust across the region. Companies' order books are well stocked, PMIs remain on high levels and the labour market has started to heal in many of the member countries. In all likelihood, it will be the Spanish economy, with a weight of 12% in Eurozone GDP, which will tip the scales of growth forecasts. The private sector in Spain will have to deleverage further and house-price to income ratios are still on elevated levels. In the light of tightening fiscal policies, we have lowered our growth forecast for the current and for next year.

Inflation

Swiss Life Asset Management	Consensus
2010: 1.3%	2010: 1.3%
2011: 1.2%	2011: 1.4%

A hike in the VAT, as implemented already in Greece and announced for Spain and Finland, causes a one time shift of the general price level to the upside, distributed over a couple of months as companies channel price increases over to consumers. Together with the Euro weakness, such tax increases constitute an upside risk to our inflation forecast. Nevertheless, headline inflation will drop below 1% at year end and core inflation will moderate to potentially close this year at 0%.

Japan – Not so much change in the political system

GDP Growth

Swiss Life Asset Management	Consensus
2010: 3.1%	2010: 2.4%
2011: 1.2%	2011: 1.7%

Japan emerges from recession at the fastest pace of all developed economies. According to the latest official data, GDP expanded at a stunning 4.9% annualised rate in the first quarter. This triggers a marked upward revision to our forecast for average annual growth in calendar year 2010. Such a performance ensures any government in the world a high popularity. But not in Japan, where prime minister Hatoyama had to resign on broken promises in other fields than the economy. Despite last year's landslide election win by the Democratic Party, institutional changes in Japan's political system apparently remain out of reach. Hatoyama is most likely replaced by finance minister Kan who is said to favour fiscal reform and to consider an increase in the consumption tax. Combined with fiscal consolidation in other major economies around the globe, such domestic measures will weigh on growth next year and potentially thereafter. This judgement leads to a sub-consensus forecast for growth in 2011. At present though, improvements across monthly indicators remain broad-based and include workers' cash earnings and household spending. Industrial sentiment remained robust in the second quarter with the PMI improving both in April and May.

Inflation

Swiss Life Asset Management	Consensus
2010: -0.7%	2010: -1.0%
2011: 0.0%	2011: -0.2%

The last available figure for nationwide inflation dates back to April and came in lower than we have assumed. Consequently, we reduce our forecast for average annual consumer price inflation slightly. The drop in consumer prices was exacerbated by a government waiver on high school tuition fees. That means that our view of abating downward pressure on prices is not put in question. In the meantime, upside risks for next year's forecast are growing in the case that the consumption tax rate is indeed increased under the new prime minister.

UK – Marked upward revision in inflation forecast

GDP Growth

Swiss Life Asset Management	Consensus
2010: 1.1%	2010: 1.3%
2011: 1.5%	2011: 2.3%

The impressively fast formation of Britain's new coalition government disproved fears of a hung parliament so far. While fiscal consolidation is imperative for the new government, it is still uncertain how they will go about it. Rolling back the state was the ruling parties' priority measure to cut the budget deficit to a more sustainable level during the election campaign. The new Chancellor Osborne will deliver an emergency budget on June 22. At present he still seems committed to the 80/20 rule, which would involve 80% of cuts to be made through public spending restraint and 20% through tax measures. Tax measures will include a permanent increase of the value added tax rate to 20% next year. Until then, the economic recovery is likely to gather momentum. Most importantly, this assessment is based on PMI surveys staying near record highs, steadily improving labour market data and annual house price increases of almost 10%. The impact of fiscal consolidation will be felt next year and thereafter. Most likely, consensus estimates will follow our downward revision in the months to come.

Inflation

Swiss Life Asset Management	Consensus
2010: 2.9%	2010: 2.9%
2011: 2.4%	2011: 1.8%

A severe upside revision to our inflation forecast is inevitable as we have underestimated inflation in the UK through the past two months. Furthermore, we now incorporate a VAT rate hike although the exact timing of such a step remains unknown until June 22. At present, we believe that two thirds of the tax increase will be passed on to consumers. We think that the resulting price increases will affect the consumer price index during the first three months after the introduction of the measure which we expect for January 2011.

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Switzerland – Losing out on the weakening Euro

GDP Growth

Swiss Life Asset Management	Consensus
2010: 2.0%	2010: 1.9%
2011: 1.6%	2011: 1.9%

At 0.4%, first quarter 2010 GDP growth came in below our expectation of 0.7%. As this number was accompanied by an upward revision to growth during the last quarter 2009, the resulting need to adjust our forecast for average annual growth is limited. The outlook remains unchanged as fiscal consolidation around the globe forms part of our base case scenario since many months. Consequently we have positioned ourselves near the low end of available forecasts for 2011 since the start of the year. Additional risks come with the Euro depreciation through the past twelve months. According to the OECD's new macroeconomic model, European OECD members outside the EMU like the UK, Sweden and Switzerland suffer most from such an exchange-rate shock. Surprisingly enough, business sentiment seems largely unaffected by the unfavourable exchange rate versus neighbouring Europe so far. Quite in contrast, Switzerland's Purchasing Managers Index (PMI) reached a record high level last month. Like elsewhere, we expect the PMI to roll over in the coming months. Despite mildly improving labour market conditions, we see limited potential for accelerating consumer spending as pent-up demand inherited from the global recession is small. In this country, consumers actually hardly stopped shopping during the crisis.

Inflation

Swiss Life Asset Management	Consensus
2010: 1.2%	2010: 1.0%
2011: 0.8%	2011: 1.0%

Inflationary pressure from heating oil and gasoline eased as the recent market turmoil led to a drop in energy prices. Fiscal consolidation throughout Europe will most likely reinforce deflationary fears in the coming quarters.

