8 October 2010

Weekly

Intesa Sanpaolo
Research Department

Macroeconomic and
Fixed Income Research

Luca Mezzomo
Economist

Giovanna Mossetti
Economist - USA and Japan

Paolo Mameli
Economist – Euro Area

Alessio Tiberi
Economist

Asmara Jamaleh
Economist – Forex Market

Alessandra Gaia
Research Assistant

Viewpoint

As expected, the October ECB meeting produced no particular developments. Only after the December meeting will it be clear whether the exceptional measures are to be further extended.

Ireland: two months that will decide the country's fate

The shock revision to the 2010 deficit and debt estimates has raised serious concerns about the sustainability of Ireland's public finances. If in the next four years the country neared the deficit targets agreed with the European Union, long-term sustainability would be a joke. The drafting by mid-November of a credible package of measures delivering a break-even primary balance in a few years, without triggering an economic depression, will be very complex. But it is a challenge Ireland can no longer avoid.

Forex markets

The weak dollar continues to be the dominant (and destabilising) theme. Japanese authorities in trouble after JPY hit new highs vs. USD despite the expansionary monetary measures.

The week's market movers

Due out in the Euro area are the industrial production figures for August in France, Italy and the Euro area, which should show a gain, though more moderate than in the first seven months of the year. The inflation data in France might surprise on the downside, while the Euro area price data should confirm a rise of two-tenths to 1.8% in September, with the core CPI steady at 1%.

The coming week is packed with data and events in the United States. The price figures for September (CPI, PPI, import) should confirm stabilisation, with some indications of a reversal in the disinflationary process. Retail sales should confirm moderate growth in consumption, while household confidence should be up slightly. The trade deficit should widen again in August. The Empire should show signs of a moderate improvement in October. The FOMC's September minutes should confirm a bias towards fresh quantitative easing measures.

Priced on 08.10.2010

Viewpoint

As expected, the October ECB meeting produced no particular developments. Only after the December meeting will it be clear whether the exceptional measures are to be further extended.

- No particular news emerged from the ECB governing council meeting: official interest rates remained unchanged and were deemed "*appropriate*", as expected; moreover, there was no announcement regarding the unconventional measures.

- The ECB remains cautiously optimistic about the recovery: expansion will continue "at a moderate pace", thanks also to the fact that a double-dip for the global economy is not in the offing (the latest round of European macroeconomic data was again positive, notably for German industry, showing output growth of no less than 1.7% mom and orders growth of 3.4% mom in August). However, risks to the economic outlook are "slightly" tilted to the downside, mainly in the form of renewed market tensions. On inflation, the recent rise in prices (to 1.8% yoy in August) was expected and next year a fall is expected, even though risks to the outlook for price developments are "slightly" tilted to the upside.

- According to the ECB, banks must use earnings to strengthen their capital base and expand lending. Trichet construed the reduced demand for liquidity among banks at the ECB auctions (since the start of October the net destruction of liquidity has totalled EUR 79Bn as the effect of renewals falling short of maturities, which has driven up money market rates substantially) as a sign of market "normalisation", not planned by the ECB (and therefore not to be interpreted as a sign of less expansionary monetary policy) but endogenously determined by the banks. Implicitly, Trichet envisaged that the critical cases of banks requiring major cash injections should be addressed by national governments and not by the central bank.

- Trichet repeatedly voiced concern (slightly more accentuated than the usual rhetoric) over the excessive volatility of the forex market (during the press conference the EUR/USD cross topped 1.40 for the first time since February, although it later fell back). Trichet added his voice to the calls on China urging more rapid CHY appreciation.

- Despite the "hawkish" remarks heard in recent weeks from several central bankers (Stark, Weber, Nowotny, Mersch) in favour of the withdrawal of full allotment probably as early as of January 2011, Trichet said the ECB had not changed its stance from the previous month and that it remained quite cautious since it is too early to "declare victory" against the crisis. According to Trichet, the unconventional measures (by which the ECB alludes principally to full allotment) are still needed because market normalisation is under way but still has a long way to go, and no ECB member "challenges need" for unconventional measures (at least for now). In any event, Trichet confirmed that the future evolution of the exit strategy would be reviewed at year-end.

- In conclusion, Trichet partially corrected the statements made by individual members (last week Stark said that some unconventional measures expiring at year-end would not be extended), putting off any decision to the December meeting and confirming that in any case the ECB would be extremely cautious in "calibrating" the withdrawal of the stimulus measures. The rise in the Eonia following the recent auctions (it climbed to 0.88% on 30 September) has almost entirely subsided (to the current 0.44%): in our view the level of ultrashort-term rates will remain well below the refi rate as long as full allotment at the weekly auctions is maintained. Conversely, the rise in rates on longer maturities should prove more persistent, notably one-month rates (the interbank rate is currently 0.65% vs. 0.52% last week), which for now are pinned down by the retention of the exceptional auction, which is one of the unconventional measures deployed by the ECB. The withdrawal of full allotment might be gradual and involve the one/three month auctions first and only thereafter the ordinary one-week auctions.

Ireland: two months that will decide the country's fate

Luca Mezzomo
Alessandra Gaia

The shock revision to the 2010 deficit and debt estimates has raised serious concerns about the sustainability of Ireland's public finances. If in the next four years the country neared the deficit targets agreed with the European Union, long-term sustainability would be a joke. The drafting by mid-November of a credible package of measures delivering a break-even primary balance in a few years, without triggering an economic depression, will be very complex. But it is a challenge Ireland can no longer avoid.

According to the statement made on 30 September by Irish Finance Minister Brian Lenihan, in 2010 Ireland's public deficit might reach the alarming level of 32% of GDP and the public debt 98.6%. The total cost of the bailout of the country's banks tops EUR 40Bn and might climb to EUR 50Bn in stress scenarios. The capital requirement of Anglo Irish Bank alone amounts to EUR 29.3Bn according to central bank estimates, rising to EUR 34.3Bn in a stress scenario. In the wake of the cost, deemed "exceptional", of the Irish bank bailouts, on Wednesday 6 October rating agency Fitch downgraded Ireland's debt from AA- to A+, while Moody's is also mulling a possible downgrade from the current Aa2.

The fiscal correction plan is a real challenge for the former "Celtic Tiger", in view too of the fragility of the macroeconomic situation. GDP contracted by 3.6% in 2008 and by 7.6% in 2009; the rebound in first quarter 2010 (+2.2% qoq, the first gain after eight negative quarters) did not continue in the second, which recorded a contraction of -1.2% qoq. According to Eurostat data, Ireland has an unemployment rate of 13.6%, the highest in over 15 years, and has the third-highest level of unemployment in the Euro area. The subdued trend in consumption and still stagnant foreign trade are not encouraging signs vis-à-vis the country's economic recovery. Will Ireland be able to structure a fiscal consolidation plan that is at once credible and sustainable?

Ireland has been in trouble before...

In his testimony to the European parliament on 28 September, Trichet, after calling on all Euro area countries to exercise the utmost vigilance in respect of fiscal policy, said with regard to Ireland that the country had shown in the past that it could rise to challenges. The ECB governor seemed to be referring to the crisis and subsequent fiscal correction implemented in the period 1987-1988. In the space of just three years, Ireland's deficit was slashed from 10.6% in 1986 to 2.6% in 1989, while the debt fell from 122% to 93% of GDP. At the same time, Ireland enjoyed years of vigorous economic growth which produced the boom of the 1990s, earning it the "Celtic Tiger" moniker. The success of the fiscal consolidation programme implemented in 1987-1988 came after numerous failures. In the first half of the 1980s, the failed attempts to turn around the public finances merely resulted in increased fiscal pressure and poor economic growth, without managing to keep the public debt under control. Underpinning the success of the measures introduced in 1987-88 were several political peculiarities: the fiscal correction came after the 1987 elections when the Fianna Fail party, despite failing to secure an absolute majority of seats, ousted the Fine Gael and Labour coalition. The minority Fianna Fail government succeeded in pressing on with the fiscal consolidation plan thanks to the support from members of the opposition. The opposition Fine Gael party applied the "Tallaght Strategy", i.e. a policy of not obstructing the economic reforms implemented by the government as long as these reforms were crucial to the nation's socio-economic well-being. Cuts were made in current spending across various sectors: in healthcare, social security and pensions. The primary balance, adjusted for the effects of the cycle, improved by 5.2% of GDP in three years, while the cuts to current primary expenditure amounted to 77%. Public transfers fell by 2.6% of GDP and public sector pay was cut by 1.5% of GDP. Public sector employment was reduced by 7% between 1986 and 1989. According to expectations at the time, the corrective measures would probably have brought about a consolidation of the public finances, followed in all likelihood by a period of economic difficulty, and would definitely not have led to a trend reversal in the Irish economy and to a period of robust growth, as actually came about.

Fiscal correction: 1987/88 compared with 2009/2010

	First quarter 1987	First quarter 2010
Governing party	Fianna Fail	Fianna Fail
Number of seats of governing party	81	77
- Percentage of seats vs. total	48.8	46.6
Deficit (% GDP)	-9.5	-32.0*
Public debt (% GDP)	126.3	98.6*
Unemployment (%)	16.5	12.9
	1986	2009
GDP (annualised yoy %)	+0.35	-7.6

Note: (*) The data refer to 2010 according to the "Ministry statement on Banking" of 30 September 2010.
Source: Oxford economic forecast. Intesa Sanpaolo calculations

Fiscal consolidation measures

In 2010 Ireland implemented fiscal consolidation measures totalling 2.5% of GDP; according to the EU Commission, together with the correction measures approved in 2009, the new measures would cut the 2010 deficit by no less than 4.25 percentage points. In the projections published five months ago, however, the Commission forecast that, without further measures, the 2011 deficit would remain above 12% of GDP, despite high economic growth (3.0%, vs. current estimates of 2.0-2.5%), and the structural deficit (i.e. excluding both cycle effects and one-off measures), estimated at -10.2%, would actually deteriorate vs. 2009.

The programme agreed with the European Union[1] was based on the assumption that "a large part of Ireland's deficit is permanent, or structural" and that the recovery in 2011-14 would be export-driven, i.e. less profitable in terms of tax receipts. For this reason it envisaged corrective measures totalling 2% of GDP per annum out to 2014, which up until several months ago was deemed sufficient to return the deficit to 3% of GDP by year-end 2014. One-third of the correction (EUR 1Bn p.a. between 2011 and 2012) would come from cuts in public investments. However, the stability programme was vague about how the correction targets would be met, and in June the Commission called on the Irish government "to set out the measures underpinning the consolidation effort". The government had put off pinpointing the measures until the next budget, although it envisaged measures on income tax, social spending, social security and tax on real estate.

Ireland's stability plan – December 2009 update

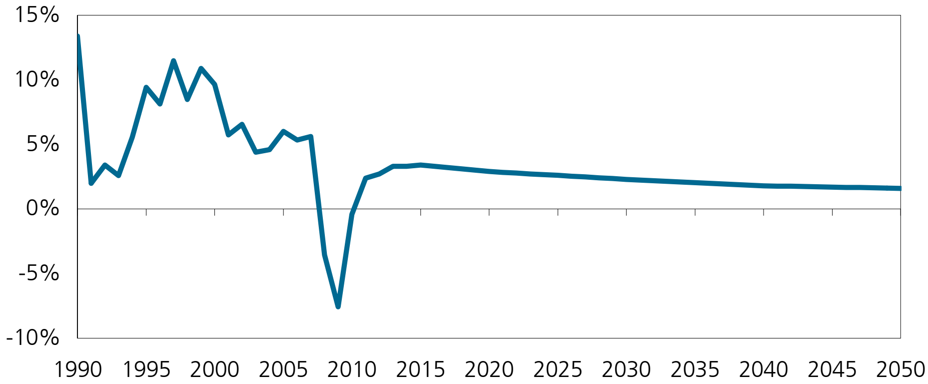
	2009	2010	2011	2012	2013	2014
Revenues	34.2	35.2	35.5	36.3	36.7	37.1
Expenditure	45.9	46.8	45.5	43.5	41.5	40.0
- salaries	18.7	16.7	15.8	15.0	14.4	14.0
- social spending	16.3	17.8	17.3	16.6	16.1	15.6
- capital spending	4.8	4.5	3.8	3.8	3.7	3.6
- debt interest	2.1	2.9	3.4	3.8	3.9	3.9
Deficit (State)	-10.2	-10.8(*)	-9.9	-7.1	-4.8	-2.8

Note: (*) the 2010 deficit is now estimated at 32% of GDP, following one-off charges for the recapitalisation of Anglo Irish Bank. The trend in 2010 tax receipts should be in line with the forecasts. The debt interest estimate, on the other hand, took no account either of the growth in the debt due to bank bailouts or of the sharp rise in risk premia that ensued. Source: Ireland – Stability Programme Update, December 2009.

[1] See: *Ireland – Stability Programme Update*, December 2009; and *Communication from the Commission to the Council: Assessment of the Action taken in response to the Council Recommendations of 2 December 2009*, COM(2010) 329, 15.6.2010, pp 15ss.

According to the latest news[2], however, the government is now said to be convinced of the need to achieve EUR 4Bn of savings in 2011, while the total for the following three years could rise to EUR 6-7Bn. The central bank reckons that the correction in respect of 2011 would have to be in excess of EUR 3Bn[3]. A four-year public finance consolidation plan will be presented early in November, followed by the 2011 budget on 7 December.

Historical GDP growth and EC projections for future potential GDP



Source: Eurostat and European Commission (*Sustainability Report 2009*).

The sustainability challenge can be met, but it will transform the country's growth model

Up until a few months ago, Ireland received benign treatment from the markets on account of the positive view they took of the effectiveness of government action at other challenging times in the past, and also because they expected that, after the crisis, the country would return to the high growth rates seen in past decades. High nominal growth helps absorb the debt and facilitates deficit reduction. In reality, as early as year-end 2009 the EU Commission adopted potential growth estimates well below the average rate seen in recent decades, fluctuating between 4% and 9.5%. The outlook adopted for the long-term sustainability analysis factors in potential growth of 3.4%, steadily falling thereafter to 1.6% in 2050. A reduction in trend growth seems likely owing both to demographic factors (population ageing) and also because several hugely important drivers of the last 20 years are no longer in play: the vast increase in financial leverage and the property market boom, massive foreign direct investment, plus huge transfers from the EU (even as much as 3% of GDP) used to fund infrastructure expansion. The growth model had already deteriorated in the period 2001-2006, driven by drugged demand-side growth and thus characterised by growing financial imbalances and the erosion of competitiveness[4]; today the economy has to confront the recovery with a stricken banking system in need of downsizing, without the prospect that lending might power growth. Secondly, the question of sustainability is compounded by the growth in the level of the debt, now standing at 98%, and by the rise in risk premia. Currently, the nominal cost of new debt is 2% for six-month bonds, rising to 4% on the two-year maturity; the cost tops 5% as of the five-year maturity. With a real cost of debt of 2-2.5%, Ireland would have to achieve a break-even primary balance merely to stabilise the debt/GDP ratio – which implies a correction amounting to at least 10 points of the structural balance relative to the situation expected in 2011. Lastly, the EU Commission estimates that ageing-related spending will rise from 17.5% in 2010 to 20.3% in 2030 and to 26.2% of GDP in 2050 – increases in excess of those expected for the EU average.

---

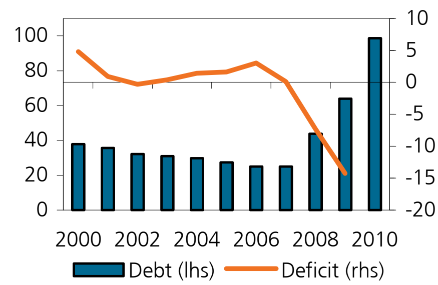
[2] Reuters, "Ireland eyes 4 bln euros 2011 budget savings – reports", 3 October 2010.

[3] Central Bank of Ireland, *Quarterly Bulletin Q4*, October 2010, p. 8.

[4] See: Klaus Regling and Max Watson, *A Preliminary Report on the Sources of Ireland's Banking Crisis*, May 2010.

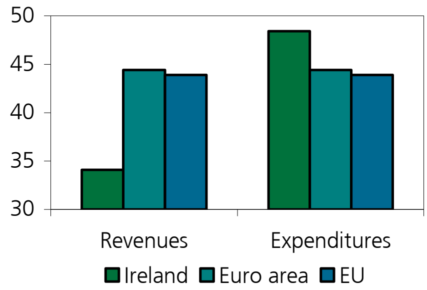
If we assume that the government manages in 2014 at least to near the deficit targets agreed with the European Union, reducing the debt/GDP ratio towards 60% of GDP would be relatively easy, even assuming a sharp fall in potential growth, as in the above-mentioned EU Commission estimates. Pensions reform cutting the weight of ageing-related expenditure by two points in 2050 would be enough to avoid substantial hikes in fiscal pressure or cuts to the public spending/GDP ratio; without pensions reform, other compensatory increases in fiscal pressure and/or cuts in other spending items would obviously be required, although they would be relatively small in size given the extended time horizon. In both cases it is likely that Ireland will be forced to review its growth model and resign itself to a level of fiscal pressure more in line with the EU average.

Government deficit and debt (% of GDP)



The 2010 figure is the most recent government estimate.
Source: Eurostat and Irish government

Fiscal pressure very low compared to the EU average



Source: Eurostat

The toughest challenge is the fiscal correction in the coming years

The real issue is the 2011-14 consolidation path, which will require a considerable increase in fiscal pressure (3.4 points even in the old stability programme) and swingeing spending cuts.

On the one hand, any delay in implementation would rapidly drive up the debt and interest expense, increasing the long-term fiscal pressure and primary spending cut targets; in addition, there would be an increased likelihood of extreme scenarios connected with a loss of confidence among investors.

On the other hand, diligent implementation of the plan reduces aggregate demand-side growth and produces negative retroactions on the budget results. The mix of measures in the long-term programme due in November will therefore have to be such as to ensure fiscal multipliers as far as possible below 1 – e.g. by targeting the disposable income of cohorts and sectors with a high propensity to save, or taxing goods transactions where demand is inelastic.

Assuming the government manages to put together a credible package of measures, there will still be an implementation risk connected with Fianna Fail's thin parliamentary majority – even though we believe the stakes are so high that the budget would be passed. It will be recalled that the severe measures of the 1980s were passed without a robust parliamentary majority. Lastly, there is the risk that bank recapitalisation may end up close to the stress scenario estimates, which are EUR 5Bn higher in the case of Anglo Irish.

But there are not only negatives. Compared with Greece at the start of 2010, Ireland at least has the advantage of greater flexibility in terms of market access thanks to large liquidity reserves, estimated at EUR 20Bn, and therefore it is less likely that the country would be forced to activate the EU assistance mechanisms, provided November's fiscal consolidation plan stands up.

Forex markets

The weak dollar continues to be the dominant (and destabilising) theme. Japanese authorities in trouble after JPY hit new highs vs. USD despite the expansionary monetary measures.

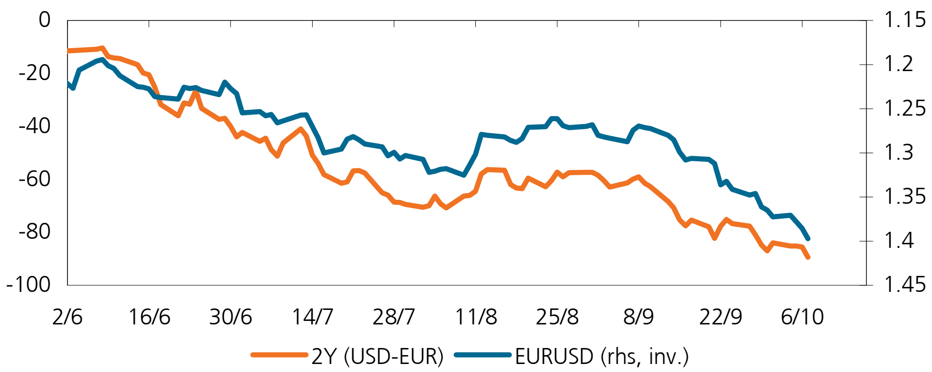
Luca Mezzomo

The week was entirely dominated by the weakness of USDD, which has fallen 0.7% in effective nominal exchange rate terms since last Friday. In consequence, EUR and JPY appreciated by 1.0% and 0.6% respectively, again on the forex index. USD is 6% down on the 2009 average and JPY is a massive 12% stronger. EUR is in an unusual situation: despite its strength vs. USD, it is still 7% below 2009 average levels.

The dollar remains weak mainly on account of the signals arriving from the Federal Reserve. The case for implementing fresh quantitative easing appears to have ample support on the FOMC, while the opposition (Plosser, Hoenig, Fisher) looks somewhat isolated. Unfortunately, the possible flood of dollars – and the definite prospect of extremely accommodating monetary conditions – is destabilising the global currency system. In addition to the rise in commodity prices, the flight out of USD stimulates capital outflows towards the emerging markets, where there is a growing risk of speculative bubbles and unsustainable lending dynamics. As evidence of this, Brazil has started to discourage non-resident investments in bonds by hiking the tax on bond purchases. With such clear signals from the central bank, moreover, it would take major surprises from the macroeconomic data for interest rates and the dollar exchange rate to move up. The volatility of exchange rates will, regrettably, remain a problem for a long time to come.

JPY – The situation remains sensitive in the case of yen, which is once again trading at highs vs. USD after 14 days of virtually uninterrupted appreciation. The monetary authorities have tolerated the movement without intervening, but on Friday, with USD at 82, Finance Minister Noda said the government was watching foreign exchange movements very closely and might once again resort to "*robust*" measures, including fresh intervention on the forex market if necessary. Noda stressed that the action taken on 15 September was intended to "*limit excessive movements*" and that the aim was not to achieve a "*certain level*" for the currency via long-term, big-ticket measures. Note that the expansionary measures adopted by the Bank of Japan (token rate cut, quantitative easing) have not had any negative effects on JPY.

2Y USD-EUR swap spread and cross



Source: calculations on Thomson Reuters data

EUR – Even though the tensions on the Eonia have subsided and the ECB has not announced an acceleration in the exit strategy, the trend in rate spreads continues to be favourable to EUR. Since there not yet any incontrovertible signs of overvaluation (as mentioned above, the effective exchange rate is weaker than in 2009), further appreciation cannot be ruled out.

Having overcome the resistances at 1.40, the limits could be 1.41 and even 1.44. Should the movement consolidate, then at the end of the month we may see the first repercussions of this appreciation on business sentiment, but it will still be too little to bet on a trend reversal. For now, the first incursion above 1.40 was followed by a limited retracement, taking it to the current level of 1.3855. The main supports are 1.3855 and 1.3797. The question of the diversification of China's currency reserves has resurfaced with official expressions of interest in the Italian market, which follow those in respect of the Greek market seen in recent weeks. The other potentially hot topic, namely the sovereign debt risk in the Euro area, is not expected to produce crucial developments until the presentation of Ireland's fiscal correction plan, scheduled for the first half of November.

GBP – Nor was there any real news from the Bank of England: rates on hold, APF unchanged. We remain negative on the medium-term outlook given the risks of a slowdown stemming from the fiscal tightening and the possibility of further monetary easing in the coming months. In the short term the cross with EUR could soon climb past 0.8800.

Exchange rate forecasts

	08.10.2010	1m	3m	6m	12m	24m
EUR/USD	1.3906	1.40	1.33	1.27	1.30	1.35
USD/JPY	82.37	84	93	100	98	97
GBP/USD	1.5870	1.50	1.45	1.43	1.50	1.55
EUR/CHF	1.3445	1.33	1.35	1.40	1.44	1.45
EUR/SEK	9.2967	9.15	9.30	9.20	9.00	8.90
EUR/NOK	8.0950	7.90	7.82	7.60	7.50	8.00
EUR/DKK	7.4556	7.45	7.45	7.46	7.46	7.46
USD/CAD	1.0164	1.03	0.96	1.00	1.04	1.12
AUD/USD	0.9756	0.97	0.93	0.88	0.86	0.82
NZD/USD	0.7471	0.74	0.72	0.68	0.65	0.58
EUR/JPY	114.52	118	123	127	127	131
EUR/GBP	0.8759	0.93	0.92	0.89	0.86	0.87
EUR/CAD	1.4137	1.44	1.28	1.27	1.35	1.51
EUR/AUD	1.4254	1.44	1.43	1.44	1.51	1.65
EUR/NZD	1.8605	1.89	1.85	1.87	2.00	2.31

Source: Thomson Reuters and Intesa Sanpaolo calculations

Projections: chg. %

	1m	3m	6m	12m	24m
EUR/USD	0.7%	-4.4%	-8.7%	-6.5%	-2.9%
USD/JPY	2.0%	12.4%	21.4%	19.0%	18.3%
GBP/USD	-5.5%	-8.6%	-9.6%	-5.2%	-2.3%
EUR/CHF	-1.1%	0.4%	4.1%	7.1%	7.8%
EUR/SEK	-1.6%	0.0%	-1.1%	-3.2%	-4.3%
EUR/NOK	-2.4%	-3.4%	-6.1%	-7.3%	-1.2%
EUR/DKK	-0.1%	-0.1%	0.1%	0.1%	0.1%
USD/CAD	1.3%	-5.6%	-1.7%	2.3%	10.1%
AUD/USD	-0.6%	-4.7%	-9.8%	-11.9%	-16.0%
NZD/USD	-0.9%	-3.6%	-9.0%	-13.0%	-21.8%
EUR/JPY	2.7%	7.5%	10.9%	11.3%	14.8%
EUR/GBP	6.6%	4.7%	1.1%	-1.3%	-0.6%
EUR/CAD	2.0%	-9.7%	-10.2%	-4.4%	6.9%
EUR/AUD	1.3%	0.4%	1.3%	6.1%	15.5%
EUR/NZD	1.6%	-0.8%	0.3%	7.5%	24.2%

Source: Thomson Reuters and Intesa Sanpaolo calculations

The week's market movers

Due out in the Euro area are the industrial production figures for August in France, Italy and the Euro area, which should show a gain, though more moderate than in the first seven months of the year. The inflation data in France might surprise on the downside, while the Euro area price data should confirm a rise of two-tenths to 1.8% in September, with the core CPI steady at 1%.

The coming week is packed with data and events in the United States. The price figures for September (CPI, PPI, import) should confirm stabilisation, with some indications of a reversal in the disinflationary process. Retail sales should confirm moderate growth in consumption, while household confidence should be up slightly. The trade deficit should widen again in August. The Empire should show signs of a moderate improvement in October. The FOMC's September minutes should confirm a bias towards fresh quantitative easing measures.

Monday 11 October

Euro area

- Italy. Industrial production is expected to be up 0.4% mom in August after the weak 0.1% mom posted in July. Output would thus be up in every month of 2010. Year-on-year, output would accelerate to 10.2% from 1.7% yoy (to 7% from 4.8% yoy adjusted for working days). The level of production would rise over 10% above the March 2009 lows, but would still be well short (-18%) of the pre-crisis highs. The improved sentiment among firms according to the August ISAE survey (despite dipping slightly in September) suggests further growth in output, although the fall recorded in factory orders in July signals that in any case the figure will likely not be outstanding. The cycle in industry remains expansionary, though less buoyant than in 1H10.
- France. Industrial production should slow to 0.4% mom in August from 0.9% mom before. The year-on-year movement would fall to 3.7% from 5.5% yoy. August might lack the contribution of transportation and coke and oil products which were crucial to industrial production growth in July. In any event, the PMI manufacturing for France, which posted gains in August and September, remains set to the bullish side, indicating that the cycle in industry remains expansionary.

Tuesday 12 October

United States

- The Fed publishes the minutes of the September FOMC meeting. The revision to the macroeconomic forecasts should show lower inflation and growth at year-end 2010 and year-end 2011 vs. the July forecasts, plus a higher unemployment rate. The minutes reveal the wide-ranging debate on new quantitative stimulus measures, with discussion of both method and size. The September meeting featured numerous interventions by most of the committee and an assessment of the participants' views is already possible before reading the minutes; the minutes might give some indication of the conditions demanded by the dissenters/sceptics if they are to vote for a new programme. Specifically, there might be some information on flexible schemes and/or schemes contingent on the macro data, as indicated in Bullard's speech. The statement and the speeches denote a strong chance of intervention as early as November: the minutes might give indications on the conditions demanded for intervention, although the statement and recent speeches indicate that, barring a marked improvement in the data, a fresh round of quantitative easing is very likely.

Wednesday 13 October

Euro area

- France. The index of consumer prices on the national measure might be down -0.1% mom in September after +0.2% mom in August. The core index is also expected to be down –0.1%

mom. Energy prices should have fallen in September, while fresh food, after falling in August, might show some upward pressures. Year-on-year inflation would thus accelerate to 1.6% from 1.4% yoy in August. On the harmonised measure, consumer prices are expected to be steady in September, giving year-on-year inflation of 1.8% from 1.6% yoy before. Inflation is expected to be little changed in the coming months, remaining broadly in line with Euro area dynamic.

- Industrial production in the Euro area is expected to be up 0.9% mom in August, accelerating from the previous month. The year-on-year movement adjusted for working days would thus accelerate to 7.7% from 7.2% yoy. Output would still remain at the early 2003 levels, however. The figure was driven by robust and stronger-than-expected growth in Germany (+1.7% mom), while the dynamic should be more modest in the other major economies. In general, after two quarters of robust growth (+2.4% qoq in the first quarter, +2.5% qoq in the second), industrial production might slow to 1% qoq in 3Q10.

United States

- Import prices are expected to be down -0.2% mom in September, after +0.6% mom in August. The expected fall is due to the correction in oil prices last month. Ex oil, prices are expected to be up 0.2% mom.

Thursday 14 October

United States

- The PPI is expected to be up 0.2% mom (3.8% yoy) in September; the core PPI should be up 0.1% mom (1.5% yoy), in line with the trend seen in recent months. Energy prices should be down after a sharp rise in August (+2.2% mom). By contrast, food prices should be up sharply (after -0.7% mom), in light of the data on import prices and agricultural commodities. Core intermediate goods prices should accelerate, lending weight to the view that the disinflation process is virtually over.

- The trade balance should show the deficit widening to USD -46Bn in August, from USD -42.8Bn in July. The data should show a correction in exports and a sharp acceleration in imports, after the growth in export and fall in imports in July. Durable goods deliveries signal a reduction in exports after the increase in July, especially in aircraft. Port activity indicates growth in imports vs. weakness in exports.

Friday 15 October

Euro area

- Consumer prices in the Euro area should be confirmed at +0.2% mom in September, as in August. Inflation would thus accelerate to 1.8% yoy from 1.6% yoy. Consumer prices ex the more volatile items would slow to 0.2% from 0.3% mom and year-on-year core inflation would remain steady at 1% yoy. Between now and year-end we expect headline inflation to be steady at 1.8% yoy, while the core CPI dynamic should be far more moderate (it might fall to 0.9% yoy).

United States

- The CPI is expected to be up 0.2 % mom (1.2% yoy) in September, after +0.3% mom in July and August (which followed three straight contractions). The core CPI should be up 0.1% mom (0.9% yoy), after an unchanged figure in August. Petrol prices remained broadly steady in September, but the seasonal correction gives a positive contribution. Energy should be up sharply, with a fall in natural gas after hikes in the previous months. In respect of food prices, increases are on the way in import prices and the PPI: the food component should be driven up in 4Q10. With regard to other prices, housing should be steady as in August, while the volatile “lodging away from home” component should be forced down by hotels and pushed up by university accommodation fees; healthcare should continue the recent trend, rising by

0.2% mom. Upside risks come from school books, tuition fees and other controlled prices, plus autos; downward corrections might come from apparel. The message from prices is in our view one of stabilisation, but the Fed's view is one of concern and the reading of the data, despite positive monthly movements, will leave it inclined towards expansionary monetary policy action.

- Retail sales are expected to be up 0.5% mom in September, after +0.4% mom before. Sales ex auto should show a smaller gain (+0.4% mom), after +0.6% mom in August. Petrol should help buoy sales during the month. Auto sales were satisfactory in September at 11.7M vs. 11.5M in August and are in line with a sales growth trend under way since September 2009, after the end of the scrappage scheme. Weekly sales were weak in September, but overall the trend in disposable income is consistent with consumption growth in line the recent trend (at least until the question of unemployment benefit extensions surfaces again at the end of November).

- The NY Fed Empire index for October is expected to rise to 8 from 4.1 in September, returning close to the August level (7.1). Prices paid, orders and deliveries should be up; the labour market indications should be steady or down on August and September (around 14.5), below the level seen in the spring. Expectations six months forward might rise form 14.9 in September, but without revisiting the August levels (22.8).

- Household confidence as measured by the Univ. of Michigan in October (preliminary) should rise to 69 from 68.2 in the final September reading. Current conditions rose to 79.6 from 78.4, expectations to 60.9 from 59.1. Both components should be up in October. Inflation expectations need watching, since in recent months they fell to 2.2% from 2.7% on a one-year time horizon, despite virtual stability on a five-year horizon. The Fed is placing considerable emphasis on the movement in inflation expectations to determine the price dynamic and justify possible quantitative easing.

Calendar of macroeconomic data and events

Calendar of macroeconomic data (11 - 15 October)

Date		Time	Country	Data release	*	Period	Previous		Consensus	Intesa Sanpaolo
Mon	10/11	08.45	FRA	Industrial Production (MoM)	*	AUG	0.9	%	0.2	0.4
		10.00	ITA	Industrial Production wda(YoY)		AUG	4.8	%		7.0
		10.00	ITA	Industrial Production sa (MoM)	*	AUG	0.1	%	-0.3	0.4
Tue	10/12	07.00	JAP	Consumer Confidence Households		SEP	42.4			
		08.00	GER	Consumer Price Index (YoY) (final)		SEP	1.3	%	1.3	1.3
		08.00	GER	Consumer Price Index (MoM) (final)		SEP	-0.1	%	-0.1	-0.1
		08.00	GER	CPI - EU Harmonised (YoY) (final)	*	SEP	1.3	%	1.3	1.3
		08.00	GER	CPI - EU Harmonised (MoM) (final)	*	SEP	-0.2	%	-0.2	-0.2
		10.30	GB	CPI (YoY)		SEP	3.1	%	3	
		10.30	GB	CPI (MoM)		SEP	0.5	%	0.1	
Wed	10/13	01.50	JAP	Machine Orders (MoM)		AUG	8.8	%	-3.9	
		07.30	FRA	CPI - EU Harmonised (YoY)	*	SEP	1.6	%	2.0	1.8
		07.30	FRA	CPI - EU Harmonised (MoM)	*	SEP	0.2	%	0.2	0.0
		10.30	GB	Average Earnings		AUG	1.5	%	1.6	
		10.30	GB	Claimant Count Rate		SEP	4.5	%	4.5	
		10.30	GB	Jobless Claims Change		SEP	2.3	k	2.7	
		11.00	EUR	Euro-Zone Ind. Prod. sa (MoM)	*	AUG	0.0	%	0.7	0.9
		14.30	USA	Import Price Index (MoM)		SEP	0.6	%	-0.2	-0.2
Thu	10/14	09.00	SPA	CPI (EU Harmonised) (MoM)		SEP	0.3	%		0.0
		14.30	USA	Trade Balance		AUG	-42.8	bln	-43.4	-46.0
		14.30	USA	PPI Ex Food & Energy (MoM)	*	SEP	0.1	%	0.1	0.2
		14.30	USA	Producer Price Index (MoM)		SEP	0.4	%	0.2	0.1
		14.30	USA	Initial Jobless Claims		week	445	k		
Fri	10/15	06.30	JAP	Industrial Production (MoM) (final)		AUG	-0.3	%		
		10.00	ITA	Trade Balance Eu (Euros)		AUG	1900	mln		
		10.00	ITA	Trade Balance (Total) (Euros)		AUG	1750	mln		
		11.00	EUR	Euro-Zone Trade Balance sa		AUG	-0.2	bln		
		11.00	EUR	Eurostat Core MUICP YoY NSA		SEP	1.0	%	1.0	1.0
		11.00	EUR	Eurostat MUICP All Items YoY NSA (final)		SEP		%	1.8	1.8
		11.00	EUR	Eurostat MUICP All Items MoM NSA		SEP	0.2	%	0.2	0.2
		11.00	ITA	CPI - EU Harmonized (YoY) (final)		SEP	1.6	%	1.6	1.6
		11.00	ITA	CPI - EU Harmonized (MoM) (final)		SEP	0.5	%	0.5	0.5
		11.00	ITA	CPI (NIC incl. tobacco) (YoY) (final)		SEP	1.6	%	1.6	1.6
		11.00	ITA	CPI (NIC incl. tobacco) (MoM) (final)		SEP	-0.2	%	-0.2	-0.2
		14.30	USA	CPI Ex Food & Energy (YoY)		SEP	0.9	%	0.9	0.9
		14.30	USA	CPI Ex Food & Energy (MoM)	**	SEP	0	%	0.1	0.1
		14.30	USA	Consumer Price Index (YoY)		SEP	1.1	%	1.2	
		14.30	USA	Consumer Price Index (MoM)	*	SEP	0.3	%	0.2	0.2
		14.30	USA	Empire Manufacturing	*	OCT	4.1		7.0	8
		14.30	USA	Retail Sales Less Autos	**	SEP	0.6	%	0.3	0.5
		14.30	USA	Advance Retail Sales	**	SEP	0.4	%	0.4	0.4
		15.55	USA	U. of Michigan Confidence (prelim.)	*	OCT	68.2		69.0	69.0
		16.00	USA	Business Inventories		AUG	1.0	%	0.5	

(?) First likely date; (**) very important; (*) important

Source: Intesa Sanpaolo Research Department

Calendar of macroeconomic data (18 – 22 October)

Date		Time	Country	Data release	*	Period	Previous		Consensus	Intesa Sanpaolo
Mon	10/18	01.50	JAP	Tertiary Industry Index (MoM)		AUG	1.6	%		
		15.00	USA	Net Long-term TIC Flows		AUG	61.2	bln		
		15.15	USA	Capacity Utilization		SEP	74.7	%		
		15.15	USA	Industrial Production		SEP	0.2	%		
		16.00	USA	NAHB Housing Market Index		OCT	13			
Tue	10/19	11.00	GER	ZEW Survey (Econ. Sentiment)	**	OCT	-4.3			
		11.00	GER	Zew Survey (Current Situation)		OCT	59.9			
		14.30	USA	Building Permits		SEP	569	k		
		14.30	USA	Housing Starts	*	SEP	598	k		
Wed	10/20	07.00	JAP	Leading Index CI (final)		AUG	99.1			
		08.00	GER	PPI (YoY)		SEP	3.2	%		
		08.00	GER	PPI (MoM)		SEP	0.0	%		
		10.00	ITA	Industrial Sales n.s.a. (YoY)		AUG	8.9	%		
		10.00	ITA	Industrial Sales s.a. (MoM)		AUG	-2.7	%		
		10.00	ITA	Industrial Orders n.s.a. (YoY)		AUG	0.7	%		
		10.00	ITA	Industrial Orders s.a. (MoM)		AUG	-3.0	%		
Thu	10/21	06.30	JAP	All Industry Activity Index (MoM)	*	AUG	1.0	%		
		08.45	FRA	Business Confidence Indicator	*	OCT	98			
		10.30	GB	Retail Sales (YoY)		SEP	0.4	%		
		10.30	GB	Retail Sales (MoM)		SEP	-0.5	%		
		14.30	USA	Initial Jobless Claims		week				
		16.00	EUR	Euro-Zone Consumer Confidence (flash)	*	OCT	-11			
		16.00	USA	Leading Indicators		SEP	0.3	%		
		16.00	USA	Philadelphia Fed.	*	OCT	-0.7			
Fri	10/22	10.00	GER	IFO - Business Climate	**	OCT	106.8			
		10.00	GER	IFO - Expectations		OCT	103.9			
		10.00	GER	IFO - Current Assessment		OCT	109.7			
		10.00	ITA	Retail Sales (YoY)		AUG	1.7	%		
		15.00	BEL	Business Confidence Level. Sa	*	OCT	-3.4			

(?) First likely date; (**) very important; (*) important
Source: Intesa Sanpaolo Research Department

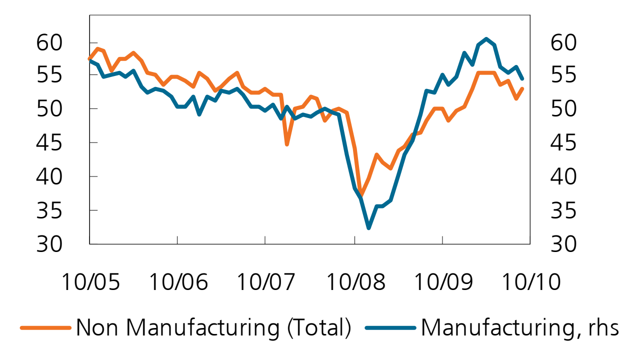
Calendar of events (11 - 15 October)					
Date		Time	Country	*	Event
Mon	10/11	01:00	GB		BOE's King to Speak in Washington
		01:00	GB		BOE's Tucker Speaks in Washington
		14:00	USA		Fed's Dudley to Speak at IIB Event in Washington
		18:00	EUR	*	ECB's Trichet Speaking in Washington
		20:45	USA		Fed's Yellen Speaks on Fed Challenges in Denver
Tue	10/12	10:30	GB		BOE's Miles Speaks in Dublin
		17:45	USA		Fed's Hoenig to Speak at NABE in Denver on U.S. Economy
		18:20	EUR	*	ECB's Trichet Speaking in New York
		20:00	USA	*	Fed Releases Minutes from Sept. 21 FOMC Meeting
Wed	10/13	10:10	USA	*	Bernanke Discusses Business Innovation in Pittsburgh
		11:00	ITA		Bank of Italy Releases August Public Finance Supplement
		19:40	GB		BOE's Sentance Speaks in London
Thu	10/14	10:00	EUR	*	ECB Publishes Oct. Monthly Report
		12:00	GER		ECB's Weber Speaks on Fiscal Policy Challenges, Berlin
		12:30	EUR		ECB's Mersch Speaking in London
		17:00	JAP		Bank of Japan to Hold Quarterly Branch Managers' Meeting
		23:00	USA		Fed's Kocherlakota Speaks in Bloomington, Minnesota
Fri	10/15	01:00	GB		BOE's Fisher Speech Released
		08:00	JAP		BOJ Governor Shirakawa to Speak in Tokyo
		10:45	EUR		ECB's Stark Speaking in Stuttgart
		11:00	ITA		Bank of Italy Releases the Quarterly Economic Bulletin
		14:15	USA	*	Bernanke Speaks at Boston Fed Conference
		15:15	USA		Fed's Lockhart Speaks on U.S. Economic Outlook in Atlanta
		17:30	USA		San Francisco Fed's John Williams at Boston Fed Conference
		18:30	USA		Former Fed Vice Chairman Kohn Speaks on Economy
Sat	10/16	13:00	EUR	*	ECB's Trichet Speaking in Marrakech
		14:15	USA		Fed's Rosengren Speaks at Boston Fed Conference

(**) very important; (*) important

Source: Intesa Sanpaolo Research Department

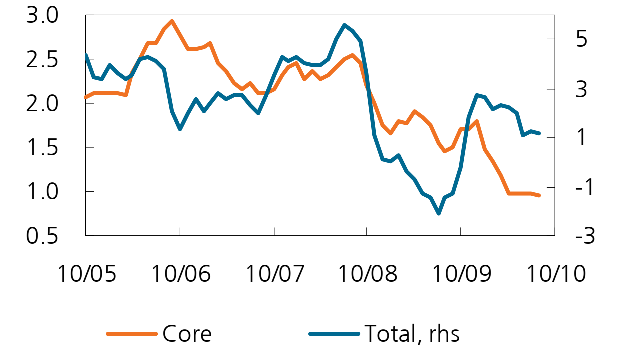
United States

ISM surveys



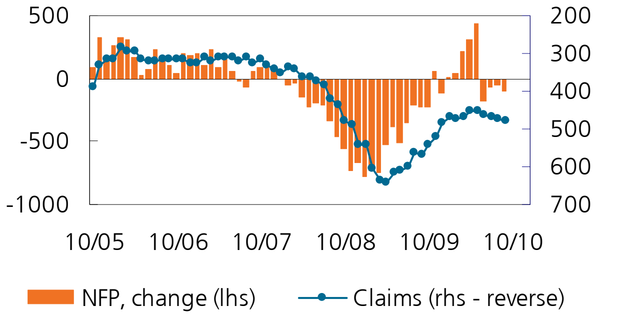
Source: EcoWin

CPI – y/y % change



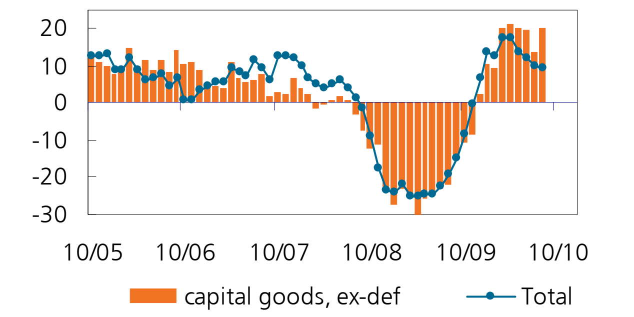
Source: EcoWin

Nonfarm payrolls & jobless claims ('000)



Source: EcoWin

New orders – y/y % change



Source: EcoWin

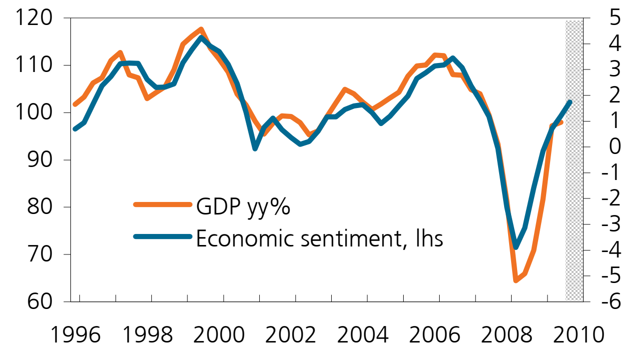
Forecast Table

	2009	2010	2011	2009 4	2010 1	2010 2	2010 3	2010 4	2011 1	2011 2	2011 3
GDP (1996 US$,y/y)	-2.6	2.8	2.5	0.2	2.4	3.0	3.2	2.5	2.2	2.4	2.6
q/q annual rate				5.0	3.7	1.7	2.3	2.2	2.5	2.7	3.0
Private consumption	-1.2	1.6	2.3	0.9	1.9	2.2	1.9	2.4	2.4	2.4	2.4
Fixed investment - nonresid.	-17.1	5.0	8.6	-1.4	7.8	17.2	3.9	7.7	8.5	9.0	9.5
Fixed investment - residential	-22.9	0.5	4.0	-0.8	-12.3	25.6	-4.4	4.5	3.5	3.5	4.0
Government consumption	1.6	0.6	0.1	-1.4	-1.6	3.9	0.2	-0.9	-0.3	-0.1	0.3
Export	-9.5	11.9	9.2	24.4	11.4	9.1	9.7	5.1	9.7	10.8	10.6
Import	-13.8	12.3	7.0	4.9	11.2	33.5	5.3	3.3	6.1	5.9	6.5
Stockbuilding (% contr. to GDP)	-0.6	1.4	-0.1	0.7	0.6	0.2	0.1	-0.1	-0.1	-0.1	0.0
Current account (% of GDP)	-2.7	-3.2	-3.5	-2.9	-3.1	-3.3	-3.3	-3.3	-3.3	-3.5	-3.6
Federal Deficit (% of GDP)	-9.5	-9.8	-9.1								
Gov. Debt (% of GDP)	84.4	92.7	98.6								
CPI (y/y)	-0.3	1.6	1.7	1.5	2.4	1.8	1.3	0.9	0.8	1.5	2.0
Industrial production	-9.3	5.3	3.8	6.9	7.1	6.5	4.5	2.8	2.8	3.2	4.8
Unemployment (%)	9.3	9.7	9.3	10.0	9.7	9.7	9.6	9.7	9.7	9.5	9.2

Note: Percentage annualised growth rates over previous period. if not otherwise specified.
Source: EcoWin. Intesa Sanpaolo

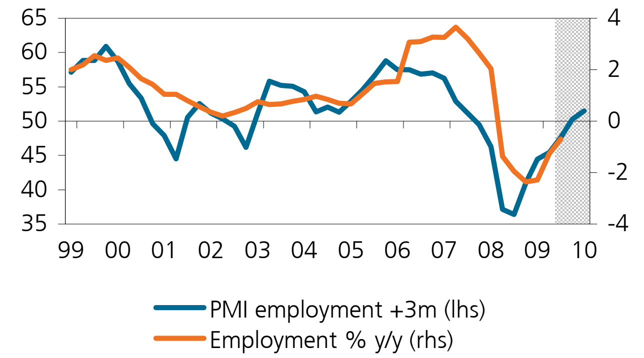
Euro Area

GDP



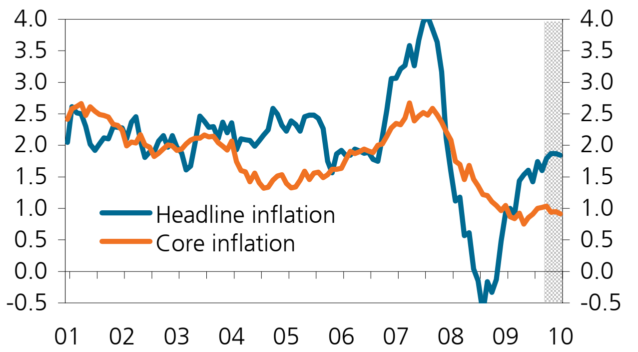
Source: EUROSTAT, UE Commission

Employment



Source: EUROSTAT, Royal Bank of Scotland, Markit Economics

Inflation



Source: Eurostat, Intesa Sanpaolo forecast

Inflation forecasts

	2009	2010	2011
January	1.1%	1.0%	1.9%
February	1.2%	0.9%	1.9%
March	0.6%	1.4%	1.7%
April	0.6%	1.5%	1.7%
May	0.0%	1.6%	1.7%
June	-0.1%	1.4%	1.8%
July	-0.6%	1.7%	1.7%
August	-0.2%	1.6%	1.6%
September	-0.3%	1.8%	1.6%
October	-0.1%	1.9%	1.6%
November	0.5%	1.9%	1.5%
December	0.9%	1.8%	1.4%

Source: Eurostat

Macro forecasts

				2009	2010				2011		
	2009	2010	2011	4	1	2	3	4	1	2	3
GDP (constant prices, y/y)	-4.0	1.6	1.7	-2.0	0.8	1.9	1.8	2.0	2.2	1.6	1.6
- q/q change				0.2	0.3	1.0	0.3	0.4	0.5	0.4	0.4
Private consumption	-1.1	0.5	0.9	-0.4	0.3	0.5	0.7	0.6	0.7	0.9	1.1
Fixed investment	-11.3	-1.1	2.3	-9.6	-4.9	-1.2	0.3	1.8	2.8	1.8	2.2
Government consumption	2.4	1.1	1.1	1.7	1.2	1.1	0.8	1.2	1.3	1.0	1.1
Export	-13.1	9.7	8.6	-5.2	5.6	11.6	11.0	10.8	10.7	7.8	8.0
Import	-11.8	9.5	7.0	-7.0	4.8	12.1	10.2	11.0	8.6	6.2	7.1
Stockbuilding (% contr. to GDP)	-0.7	1.2	-0.3	-0.9	1.1	1.7	0.8	1.0	0.0	-0.2	-0.2
Current account (% of GDP)	-0.8	-0.3	0.2	0.0	-0.4	0.0	-0.2	0.0	0.2	0.5	0.0
Deficit (% of GDP)	-6.3	-6.7	-5.9								
Debt (% of GDP)	76.0	78.8	83.4								
CPI (y/y)	0.3	1.5	1.7	0.4	1.1	1.5	1.7	1.8	1.8	1.7	1.6
Industrial production (y/y)	-14.9	6.8	2.2	1.2	2.4	2.5	1.0	0.1	0.0	0.7	0.9
Unemployment (%)	9.4	10.1	9.9	9.9	9.9	10.1	10.1	10.2	10.1	10.0	9.9
3-month Euribor	1.2	0.8	1.2	0.7	0.7	0.7	0.9	1.0	1.0	1.1	1.2

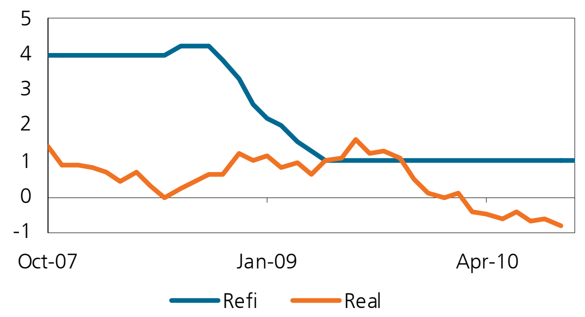
Note: Percentage annualised growth rates over previous period, if not otherwise specified.
Source: EcoWin, Intesa Sanpaolo

Interest Rates Forecasts

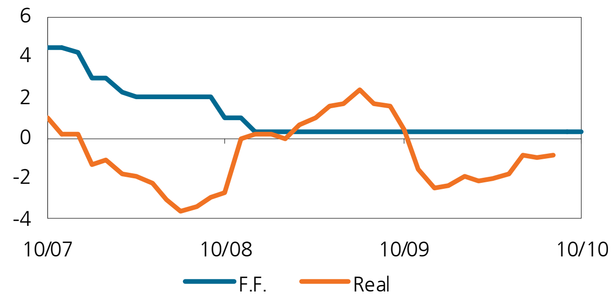
Eurozone	Mar-10	Jun-10	Sep-10	8/10	Dec-10	Mar-11	Jun-11	Sep-11
Refi rate	1.00	1.00	1.00	1.00	1.00	1.00	1.00	1.00
1m Euribor	0.40	0.49	0.63	0.75	0.77	0.91	1.08	1.15
3m Euribor	0.63	0.77	0.89	0.97	0.96	1.01	1.08	1.20

United States	Mar-10	Jun-10	Sep-10	8/10	Dec-10	Mar-11	Jun-11	Sep-11
Fed Funds	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25
3m Libor USD	0.29	0.53	0.29	0.29	0.30	0.30	0.30	0.30

Eurozone



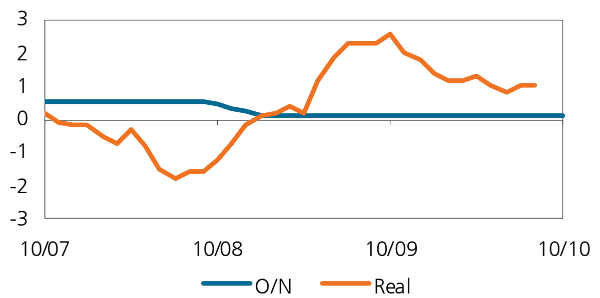
United States



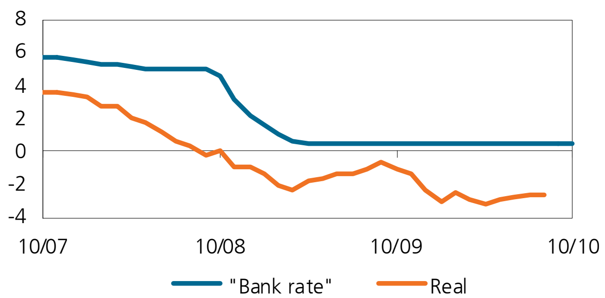
Japan	Mar-31	Jun-30	Sep-30	8/10	Dec-31	Mar-31	Jun-30	Sep-30
O/N target	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10
3m Libor JPY	0.24	0.24	0.22	0.20	0.25	0.40	0.45	0.45

United Kingdom	Mar-31	Jun-30	Sep-30	8/10	Dec-31	Mar-31	Jun-30	Sep-30
Base rate	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50
3m Libor GBP	0.65	0.73	0.73	0.74	0.65	0.75	0.75	0.80

Japan



United Kingdom



Source: Intesa Sanpaolo elaborations on Thomsons Reuters data

Intesa Sanpaolo Research Department – Head of Research Gregorio De Felice		
Tel. +39 02 879+(6) – 02 8021 + (3)		
Macroeconomic & Fixed Income Research		
Luca Mezzomo	62170	luca.mezzomo@intesasanpaolo.com
Fixed Income		
Sergio Capaldi	62036	sergio.capaldi@intesasanpaolo.com
Chiara Manenti	62107	chiara.manenti@intesasanpaolo.com
Macroeconomics		
Anna Maria Grimaldi	62118	anna.grimaldi@intesasanpaolo.com
Paolo Mameli	62128	paolo.mameli@intesasanpaolo.com
Giovanna Mossetti	62110	giovanna.mossetti@intesasanpaolo.com
Alessio Tiberi	32834	alessio.tiberi@intesasanpaolo.com
Forex Markets		
Asmara Jamaleh	62111	asmara.jamaleh@intesasanpaolo.com
Research Assistant		
Alessandra Gaia	62149	alessandra.gaia@intesasanpaolo.com
Simonetta Melotto	62102	simonetta.melotto@intesasanpaolo.com

Appendix

Analyst Certification

The financial analysts who prepared this report, and whose names and roles appear on the first page, certify that:

(1) The views expressed on companies mentioned herein accurately reflect independent, fair and balanced personal views;

(2) No direct or indirect compensation has been or will be received in exchange for any views expressed.

Specific disclosures:

The analysts who prepared this report do not receive bonuses, salaries, or any other form of compensation that is based upon specific investment banking transactions.

Important Disclosures

This research has been prepared by Intesa Sanpaolo S.p.A. and distributed by Banca IMI S.p.A. Milan, Banca IMI SpA-London Branch (a member of the London Stock Exchange) and Banca IMI Securities Corp (a member of the NYSE and NASD). Intesa Sanpaolo S.p.A. accepts full responsibility for the contents of this report. Please also note that Intesa Sanpaolo S.p.A. reserves the right to issue this document to its own clients. Banca IMI S.p.A. and Intesa Sanpaolo S.p.A. are both part of the Gruppo Intesa Sanpaolo. Intesa Sanpaolo S.p.A. and Banca IMI S.p.A. are both authorised by the Banca d'Italia, are both regulated by the Financial Services Authority in the conduct of designated investment business in the UK and by the SEC for the conduct of US business.

Opinions and estimates in this research are as at the date of this material and are subject to change without notice to the recipient. Information and opinions have been obtained from sources believed to be reliable, but no representation or warranty is made as to their accuracy or correctness.

Past performance is not a guarantee of future results.

The investments and strategies discussed in this research may not be suitable for all investors. If you are in any doubt you should consult your investment advisor.

This report has been prepared solely for information purposes and is not intended as an offer or solicitation with respect to the purchase or sale of any financial products. It should not be regarded as a substitute for the exercise of the recipient's own judgement.

No Intesa Sanpaolo S.p.A. or Banca IMI S.p.A. entities accept any liability whatsoever for any direct, consequential or indirect loss arising from any use of material contained in this report.

This document may only be reproduced or published together with the name of Intesa Sanpaolo S.p.A. and Banca IMI S.p.A..

Intesa Sanpaolo S.p.A. and Banca IMI S.p.A. have in place a Joint Conflicts Management Policy for managing effectively the conflicts of interest which might affect the impartiality of all investment research which is held out, or where it is reasonable for the user to rely on the research, as being an impartial assessment of the value or prospects of its subject matter. A copy of this Policy is available to the recipient of this research upon making a written request to the Compliance Officer, Intesa Sanpaolo S.p.A., 90 Queen Street, London EC4N 1SA.

Intesa Sanpaolo S.p.A. has formalised a set of principles and procedures for dealing with conflicts of interest ("Research Policy"). The Research Policy is clearly explained in the relevant section of Banca IMI's web site (www.bancaimi.com).

Member companies of the Intesa Sanpaolo Group, or their directors and/or representatives and/or employees and/or members of their households, may have a long or short position in any securities mentioned at any time, and may make a purchase and/or sale, or offer to make a purchase and/or sale, of any of the securities from time to time in the open market or otherwise.

Intesa Sanpaolo S.p.A. issues and circulates research to Qualified Institutional Investors in the USA only through Banca IMI Securities Corp., 245 Park Avenue, 35th floor, 10167 New York, NY,USA, Tel: (1) 212 326 1230.

Residents in Italy: This document is intended for distribution only to professional investors as defined in art.31, Consob Regulation no. 11522 of 1.07.1998 either as a printed document and/or in electronic form.

Person and residents in the UK: This document is not for distribution in the United Kingdom to persons who would be defined as private customers under rules of the FSA.

US persons: This document is intended for distribution in the United States only to Qualified Institutional Investors as defined in Rule 144a of the Securities Act of 1933. US Customers wishing to effect a transaction should do so only by contacting a representative at Banca IMI Securities Corp. in the US (see contact details above).

Valuation Methodology

Trading Ideas are based on the market's expectations, investors' positioning and technical, quantitative or qualitative aspects. They take into account the key macro and market events and to what extent they have already been discounted in yields and/or market spreads. They are also based on events which are expected to affect the market trend in terms of yields and/or spreads in the short-medium term. The Trading Ideas may refer to both cash and derivative instruments and indicate a precise target or yield range or a yield spread between different market curves or different maturities on the same curve. The relative valuations may be in terms of yield, asset swap spreads or benchmark spreads.

Coverage Policy And Frequency Of Research Reports

Intesa Sanpaolo S.p.A. trading ideas are made in both a very short time horizon (the current day or subsequent days) or in a horizon ranging from one week to three months, in conjunction with any exceptional event that affects the issuer's operations.

In the case of a short note, we advise investors to refer to the most recent report published by Intesa Sanpaolo S.p.A's Research Department for a full analysis of valuation methodology, earnings assumptions and risks. Research is available on IMI's web site (www.bancaimi.com) or by contacting your sales representative.