Current Issues

International topics

Deutsche Bank Research

January 29, 2009

Economic outlook 2009

German economy in stormy waters

Germany is experiencing an economic recession unlikely to be overcome before the end of 2009 at the earliest. Gross domestic product (GDP) is expected to contract by around 2 ½%. This is by far the strongest economic downturn of the post-war period. The global financial crisis is causing great uncertainty. Stabilising effects of falling commodity prices and monetary and fiscal policies will only be felt with a time lag.

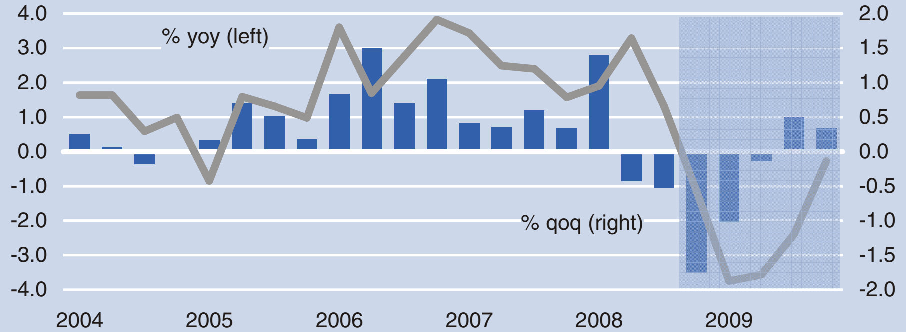
The dramatic downswing of the world economy started after the subprime bubble burst in the US property market. The US economy has been in recession since the beginning of 2008. We forecast a contraction of 2 ¼% for the US economy in the current year. Only around the end of 2009 do we expect the situation to gradually stabilise.

The emerging markets have meanwhile also been caught in the economic downdraught. After having soared for one year and a half, commodities prices collapsed in the second half of 2008. On top of the global financial crisis this added to the emerging markets' economic woes. Following the 7.9% achieved in 2007, EM growth looks set to be more than halved (good 3%) in 2009. We expect the industrialised countries to see real GDP to contract by 2 ¼% and the world economy as a whole to shrink by a good 1%, after expanding by 2% in 2008.

More than one-quarter of Germany's economic output stems from exports, if imported inputs are taken into account. Besides the loss of major sales markets, the strength of the euro represents another burden which has only been alleviated somewhat in the last few months. Export expectations in Germany's industrial sectors have hit an all-time low. For the first time since 1993 real exports will decline markedly in 2009 (-8%). Shrinking foreign demand together with declining profits in many sectors will lead to investment in plant and equipment contracting by 10%. Given the pronounced drop in employment and simultaneously rising savings ratios, private consumption will likely edge down for the third consecutive year.

Germany: Economic growth

Real GDP



Sources: Federal Statistical Office, DB Research

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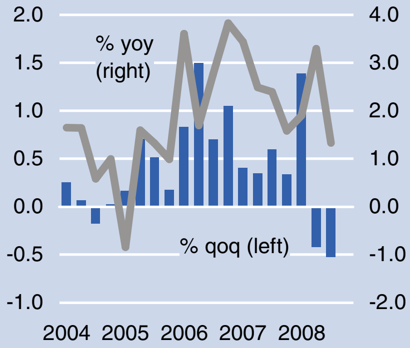
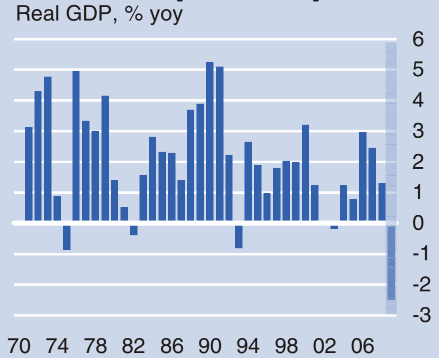
Real GDP



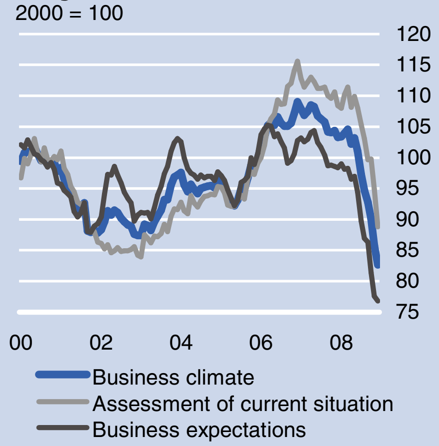
Source: Federal Statistical Office 1

Germany: Strongest contraction in past-war period
Real GDP, % yoy



Sources. Federal Statistical Office, DB Research 2

ifo business climate at 15-year low
2000 = 100



Source: ifo 3

Summary

For the first time in five years Germany is back in recession. Economic output has been shrinking since the second quarter of 2008, thus meeting the standard definition of recession. We expect the decline in real GDP to continue until mid-2009 at least. After GDP growth of 1.3% in 2008, the contraction forecast for the current year will probably amount to 2 ½%. This would represent the deepest recession in Germany's post-war history. Even in the wake of the two oil crises in the 1970s and 80s the German economy contracted by merely 0.9% and 0.4%, respectively. The recession periods that followed in 1993 (-0.8%) and 2003 (-0.2%) were also relatively mild.

Early signs of a downswing

Although the world economy had already slowed markedly in 2007, the ifo business climate index remained surprisingly high up until early summer 2008. Only in mid-2008 did sentiment deteriorate considerably. When the financial crisis escalated further in September 2008, the index went into free fall. At present, it stands at its lowest level in 15 years. Other economic indicators such as order intake or the purchasing managers' index (PMI) also paint a dismal picture.

The reasons for the downswing were not so much home-made as external in nature.

— In line with global demand, German exports weakened considerably in the course of the dramatic economic downturn in the US, which with a time lag also affected the dynamically growing emerging markets and the euro area.

— This development was exacerbated by the strength of the euro, which peaked around mid-2008, hurting German exporters' price competitiveness.

— In addition the long period of high energy and food prices reduced households' purchasing power, so private consumption once more failed to support the economy in 2008.

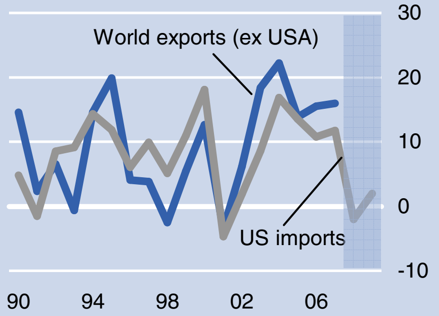
— The negative effects of the international financial crisis, which had taken a dramatic turn for the worse following the collapse of Lehman Brothers in mid-September 2008, brought money markets and markets for short-term corporate credit almost to a complete standstill.

External environment increasingly weaker

The issue of whether the global economy can decouple from developments in the US gave rise to heated debate again last year. It was hoped that major German sales markets would continue their dynamic growth trajectory. Many economists argued that the emerging markets were strong enough to keep the global economy afloat in the event of a US downswing. In fact, the emerging markets have gained considerable weight in the global economy in the past few years. Current developments show, however, that the saying that "the rest of the world catches cold when the US sneezes" is still applicable. Only this time, the US is seriously ill. It took some time for the US flu to spread to Asia and Europe. The strong downswing in the US which was triggered by the property market crisis infected the global economy not only through direct trade links – with by far the largest current account deficit in the world the Americans are still the most free-spending consumers of the world – but also through

US consumers: The world's top customers

% yoy



Sources: IMF, DB Research 4

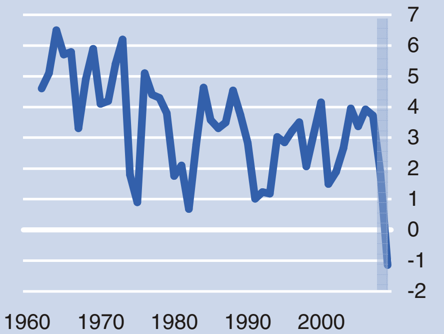
ifo world business climate

Figures above 5 signal a positive trend

Source: ifo 5

Global growth

Real global GDP, % yoy



Sources: IMF, DB Research 6

confidence and finance channels, which have become increasingly important over the past few years.

Global economy to contract in 2009

The ifo business climate index for the world's regions reveals that economic activity slowed markedly on all continents in 2008. The decline was particularly pronounced in Asia. For 2009 we expect no more than about 4% growth in Asia, down from 7% in 2008 and almost 10% in 2007. But other regions, too, will see growth decelerate. All major industrialised countries are already in recession. In the euro zone, real GDP looks set to shrink by 2 ¼%. The UK economy also expected to contract by 3%. All in all the world economy will shrink by a good 1% in 2009. This would be the worst performance in many decades, as growth was still positive even during the oil crises of the 1970s and 80s. In light of the obviously persisting strong dependence of the world economy on the US, an end to the US property market crisis is a precondition for a recovery of the global economy.

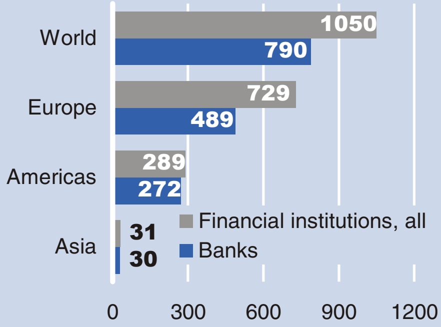
Adjustment continues in US property market

This may take more than a year, though. After the bubble burst on the US housing market, house prices slumped at double-digit rates, mortgage default rates rose to nearly 20% in the subprime segment and residential construction investment fell to its lowest level in 13 years. Property prices have not yet bottomed out. At present, new residential construction in the US is roughly 900,000 units short of demand, which implies that the gap between current vacancy rates and their trend rate of over 1 million units could be closed in around 1 year.

Negative wealth effects dampen US consumption

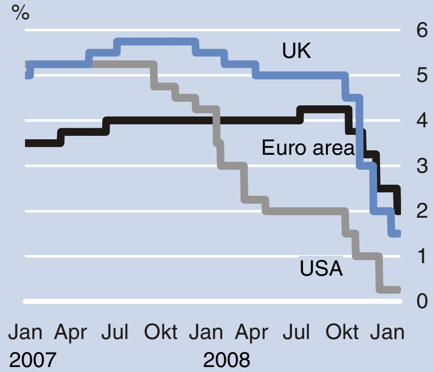
Even though this would create a new equilibrium on the US residential market, it would also mean that overall economic growth remains clearly below potential, as negative wealth effects will continue to weigh on private consumption for a long time. The financial situation of households was very tight even before the financial crisis worsened recently. Due to easier lending standards especially in the mortgage segment, indebtedness had grown dramatically on rising property prices. This was used in part to finance consumption, with the savings ratio dropping to almost zero. We forecast house prices to fall by another 10% this year (-20% in 2008), bringing down households' real estate wealth by a total of 25% or USD 6,000 bn by the end of 2009. Through wealth effects this alone will dampen consumption expenditure by 1 ½%. As a result and in light of quickly rising unemployment we expect private consumption to shrink by around 2 ¼%. Despite the new economic stimulus programme promised by the new US president, Barack Obama, with a volume of more than USD 800 bn or over 5 ½% of GDP, real GDP looks set to decline by nearly 2 ¼% this year. This would be the deepest recession in post-war history also for the US. To be sure, we assume the situation in the US to stabilise in H2 2009 and the economy to return to a growth path in 2010. However, at a mere 1% growth will remain clearly below potential given the structural problems and ongoing adjustment.

Write-downs following financial crisis
USD bn



Source: Bloomberg 7

Key interest rates
%



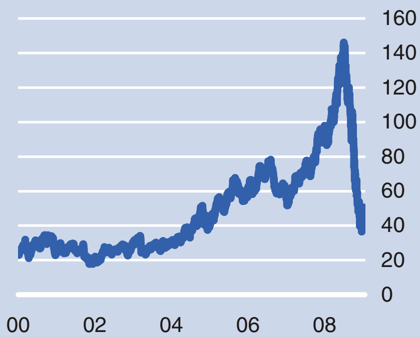
Sources: Fed, ECB, Bank of England 8

Global growth

Real GDP, % yoy	2007	2008	**2009**
USA	2.0	1.2	-2.2
Japan	2.4	-0.3	-3.6
Euro area	2.6	0.8	-2.1
Asia	9.7	6.6	4.3
Latin America	5.5	4.2	0.8
Eastern Europe	6.7	4.7	1.0
Middle East	5.3	5.6	2.9
World	3.6	1.9	-1.2

Sources: IMF, DB Research 9

Oil price
Brent Blend, USD/bbl.



Source: Global Insight 10

2009 is not 1929

An IMF analysis shows that recessions turn out considerably longer and deeper if preceded by a financial markets or banking crisis. The loss of growth in such a recession has averaged 4 ½% in the past. Similar or even higher shortfalls are also to be expected in the current crisis. However, we believe the current recession to be manageable so it will not result in a 1929-style depression.

Certainly there are parallels to be drawn between 1929 and today. The origins of the current financial crisis lie in the US property market crisis which shook investors and financial markets throughout the world when the value of mortgage securitisations and special investment vehicles slumped. This led to global write-downs in the order of over USD 1,000 bn, with around USD 790 bn alone affecting banks, which led to tighter lending standards. Back in 1929 and this time the US property market experienced a boom which ended abruptly. Then and today, the crisis spread quickly because of financial innovations. In 1929 stocks were bought on credit; in the current crisis loans were securitised. However, there are also important differences between today and 1929. Back then the central banks even reduced the money supply and the US president as well as politicians in other countries stubbornly refused to counter the onset of the economic crisis with state support. By contrast, the last few months have seen dramatic cuts in interest rates, rescue packages for the banking sector and multiple measures to stimulate the economy almost all over the world and to a degree that has never been seen before. The US Fed, for instance, has brought down its key interest rate from 5.25% to 0-¼% (its lowest level ever) since September 2007, and the Bank of England has cut its base rate by 350 basis points over only three months. After some initial hesitation, the ECB also took determined action, cutting its refinancing rate by a total of 225 basis points to currently 2% since October 2008. We expect the ECB to continue to loosen the monetary reins until March 2009 with the refinancing rate likely to fall to 1%.

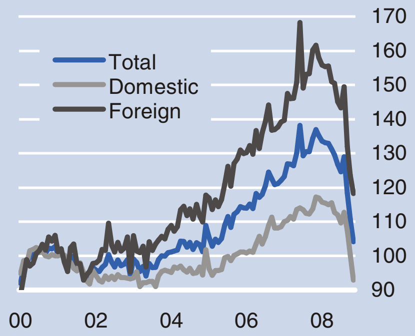
Strong relief from collapsing oil price

Besides political action the marked decline in the price of oil over the last few weeks as well as considerably lower commodities prices have provided some hope for the consumer countries' economies. After having soared from mid-2007 and peaked at USD 146 per barrel, the price of North Sea oil (Brent Blend) has since dropped by more than 70% to temporarily below USD 40 bbl in only a few weeks on collapsing growth expectations. Moreover, food prices have fallen by an average 30% from their peak in mid-2008 (HWWI food price index). To be sure, the recent rollercoaster ride of oil prices demonstrated once again the considerable risks inherent in oil price forecasts. Should the oil price continue to fluctuate between USD 40 and 50 per barrel, however, its annual average would only be half as high as in 2008. This would bring relief of more than EUR 10 bn or nearly 1% of private consumption for German households, and thus help cushion the economic downturn.

Setback for world's export champion Germany

Exports, a particularly important sector for the German economy, have been hurt massively by the deteriorating external environment. Subtracting foreign inputs, goods exports contributed nearly 22% to GDP in 2007, and about one in four jobs depends on exporting industry in Germany. With an export volume in excess of

Germany: Collapsing orders
2000 = 100

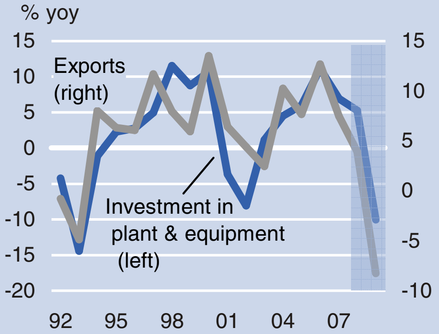


Source: Federal Statistical Office **11**

Germany: Exports & expectations
* %, ** % yoy (mov. 2M avg.)

Sources: ifo, Federal Statistical Office **12**

Germany: Exports & investment
% yoy



Sources: Federal Statistical Office, DB Research **13**

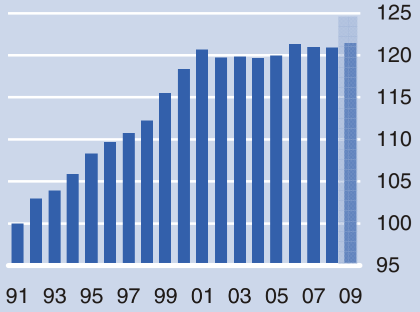
EUR 1,000 bn, Germany narrowly claimed the title of world exports champion for the sixth time in a row. But over the last few months foreign orders have slumped as a result of the global downswing. Most recently, they were roughly one-quarter below their pre-year level. Hence, export growth – which had still amounted to more than 8% in 2007 – slowed noticeably in 2008 and even turned negative at the end of the year. This is also reflected in export expectations that hit their lowest level in 33 years at the end of 2008. As the strong euro – which peaked around the middle of 2008 – will likely continue to weigh on German exports for some time to come because of a 2-3 quarter lag, we expect the current year to see real exports of goods and services decline by a good 8%, following growth of 3.9% in 2008. This would be the first annual average decline in 16 years.

Excursus:

Financial markets and banking crisis – effects on the real economy

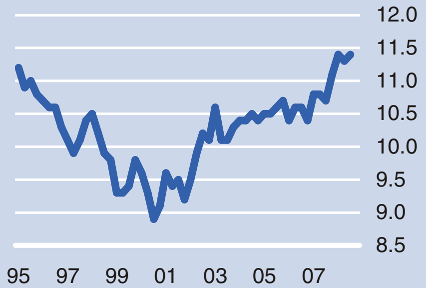
Financial market and banking crises affect the activities of companies, households and banks via different transmission channels. In severe crises there are also huge effects on the activities of the state sector (tax revenues, social security spending as well as support and stimulus packages). Bank lending is influenced decisively by the institutions' equity positions. Certainly, capital measures have contributed to achieving a slight increase in German banks' equity capital in the course of last year despite write-offs of more than EUR 60 bn. However, the banks are currently seeking to increase their equity ratios through de-leveraging, i.e. by reducing the ratio of business volume to equity capital, which restricts their lending capacities. In addition, refinancing costs of banks have increased substantially – despite the ECB's pronounced rate cuts – through high risk premiums for bank bonds and the drying-up of the interbank market. The deteriorating profit outlook and possible valuation losses are weighing on corporate balance sheets, which makes borrowing even more difficult (balance-sheet channel). However, at 65% the internal financing ratio of companies was in line with its long-term average in 2007 and likely rose further in the first half of 2008, which will limit the effect of rising funding costs. Apart from high financing costs, the lower market value of listed companies in relation to the replacement price of their assets reduces their propensity to invest (Tobin's q). Generally speaking, household spending reacts to a lesser degree to financial market crises than corporate investment does. This is attributable for one thing to the fact that only a small part of consumption is financed by debt and, for another, the larger share of quasi-fixed household spending (rent, food etc.). Over the last few years, households have reduced their debt somewhat both in absolute terms and in relation to disposable income. Higher financing costs would therefore hardly hurt consumption. As only just under 15% of Germans (over the age of 14) own stocks, shares in mutual funds or certificates, negative wealth effects will have only a minor impact on consumption through the decline in prices over the past months. However, the negative effect on confidence triggered by the financial market turmoil will probably be considerable. The households' saving ratio could thus rise by another half of a percentage point to 12% this year.

Germany: Real private consumption
1991 = 100



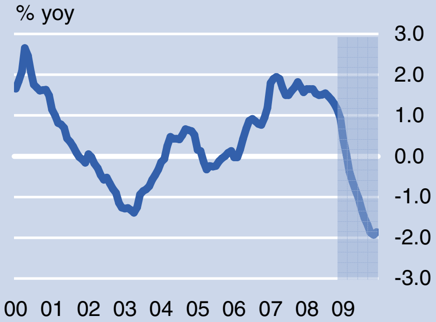
Sources: Federal Statistical Office, DB Research 14

Germany: Savings ratio
% of disposable income



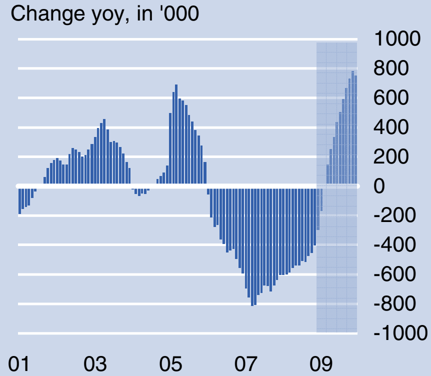
Source: Deutsche Bundesbank 15

Germany: Employment
% yoy



Sources: Federal Employment Agency, DB Research 16

Germany: Jobless total
Change yoy, in '000



Sources: Federal Statistical Office, DB Research 17

Export slump to hurt investment, too

The slump of exports will also hurt investment, as German companies have begun to reconsider their investment plans in light of slowing global demand. We therefore expect investment in plant and equipment to fall by about 10% this year, after rising by 5.3% in 2008. This forecast is supported by declining capacity utilisation in manufacturing which recently returned to its long-term average after almost three years of over-utilisation. As industrial production continues to decline – besides the slump in foreign orders there has also been a substantial drop in domestic orders below the pre-year level – capacity utilisation looks set to decline further. Moreover, corporate earnings will likely take a beating in many sectors. The financial crisis is also contributing to investment being scaled down. Numerous financial institutions have tightened lending conditions, resulting in generally higher financing costs.

Construction activity, which had still flourished in early 2008, ground to a halt in the further course of the year. Given the increasingly uncertain income and employment outlook, private residential construction will likely shrink this year. Also, the planned economic stimulation measures including faster realisation of infrastructure investment will hardly suffice to compensate for this decline. So for 2009 we expect overall construction investment to fall by 4%, after an increase of over 2.7% in 2008.

Private consumption – another disappointing year

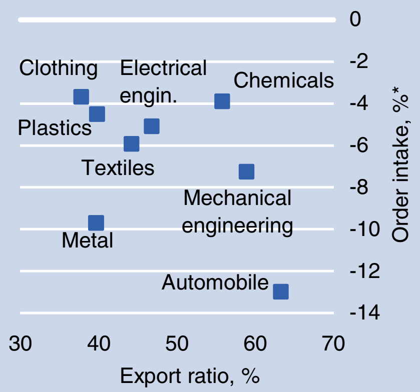
Hopes voiced at the end of 2007 that private consumption could rise more strongly on higher wage deals and rising employment and thus put overall economic growth on a broader basis were not fulfilled last year as a result of dramatically higher oil and commodity prices. Even though consumers are feeling considerable relief from the recent oil price slump, hopes for a noticeable boost to consumption will likely be disappointed again this year.

Wages will likely rise as strongly as in 2008 (+3%) this year, as many collective agreements last from 2008 into 2009. In addition, the government's recently agreed stimulus packages and the relief from the reinstalled commuter allowance will increase private households' income. However, a negative wage drift, substantial job losses in the course of the recession and a rising savings ratio (expected to come in half of a percentage point higher given growing uncertainty) will likely cause real private consumption to grow only moderately (almost ½%). So private consumption will likely remain more or less at its 2001 level, after having expanded by 1.9% p.a. in real terms between 1991 and 2001.

Job losses just a matter of time

Despite the recession the labour market proved robust up until the end of 2008, even though the increase in employment flattened in the course or last year and the jobless total rose in December for the first time in three years. However, the labour market is a lagging indicator which reacts with a time-lag to changes in economic growth. Most recent company surveys reveal a substantial decline in staffing plans, so we expect a good 750,000 jobs to be lost by the end of 2009. The jobless total will then likely exceed 4 million at the beginning of 2010, pushing up the unemployment rate to 9 ½% from close to 8% in 2008.

Germany: Export ratio & orders by sector



* Jun/Oct vs. Jan/May 2008

Sources: Federal Statistical Office, DB Research **18**

Germany: Business expectations

Balance of positive and negative company reports

Source: ifo **19**

Germany: Industrial production

% yoy	2007	2008	**2009**
Foodstuffs	2,1	0	0
Textiles	0,8	-5	-12
Clothing	-11	-17	-12
Chemicals	5	-2	-8
Plastics	6,6	-2	-9
Metal engineering	5,3	0	-8
Mechanical engin.	9,4	5	-8
Electrical engin.	10	4	-8
Automobile	7,2	-4	-15
Manufacturing	6,5	0,5	-9

Sources: Federal Statistical Office, DB Research **20**

German industry caught in a downdraught

Manufacturing in Germany benefited strongly from the last economic upswing. Production rose by an inflation-adjusted 6% in 2006 and by as much as 6.5% in 2007. Full order books still ensured stability in the first half of 2008. Especially capital goods sectors such as mechanical and electrical engineering were able to sell their products easily on the world markets. But the first difficulties already became visible in the first half of last year: business expectations were cloudier and the high price of oil was an additional burden.

The worsening economic outlook in many important export markets forced a large number of companies to reconsider their plans for expansion. Most existing orders were still completed but new orders failed to come in.

Individual sectors depend strongly on exports

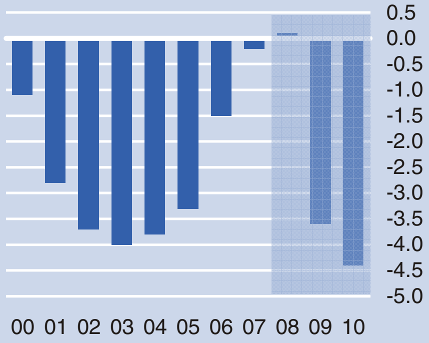
In the downturn, the heavy dependence on exports quickly became a boomerang: there is an obvious connection between a sector's reliance on exports and the degree to which it is hurt by slower business activity. Within a mere six months, order volumes fell by 13% in the car industry, by nearly 9% in mechanical engineering and by 11% in metal processing. For now, there is no evidence that the decline has bottomed out.

Three aspects need to be considered in this connection: first, the adjustment took place from a very high level. The car industry had seen its longest ever upswing, and mechanical engineering had raised output volumes by as much as 30% since 2005. Second, many companies used the crisis as an opportunity for restructuring. They now have a stronger equity base and their production costs are internationally competitive thanks to the wage restraint exercised in earlier years. So many companies are now better equipped to withstand this deep recession. Third, there are automatic stabilisers at work (e.g. low oil prices and interest rates) which will help the capital goods sectors, in particular. Government measures to stimulate the economy will also cushion the downturn.

Industry in reverse gear in 2009

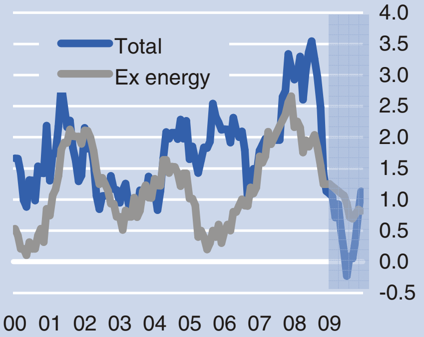
Nonetheless we expect output to slump in 2009: except for the food industry, which is nearly immune to economic downswings, all major sectors will likely head south in 2009. In the textile and clothing industry, the structural problems are being exacerbated by the recession. Raw materials and semi-finished goods (chemicals, plastics, metal products) reflect the enormous drop in output in the automobile sector. All in all, we expect manufacturing to see output decline by an inflation-adjusted 8%. In light of this strong contraction we do not look for positive impetus from the construction sector; construction output is likely to decrease strongly, too. However, given the stimulus packages and the fact that the construction sector did not boom in the recent years, the decline will come in smaller than in manufacturing. Output will be considerably weaker in 2009 than in the last downturn in 2002/2003 as there is not only a lack of foreign momentum but the situation in other countries even represents an additional burden. Only around the end of 2009 will the worst be over, and 2010 may even see modest growth again.

Germany: Budget
Overall public sector, % GDP



Sources: Federal Statistical Office, DB Research 21

Germany: Prices
Consumer price index, % yoy



Sources: Federal Statistical Office, DB Research 22

Germany: Growth

% yoy	2007	2008	**2009**
Real GDP	2.5	1.3	-2.5
Private consumption	-0.4	0.0	0.4
Gov't expenditure	2.2	2.2	2.5
Fixed investment	4.1	3.9	-7.0
Investment in M&E	6.9	5.3	-10.0
Construction	1.8	2.7	-4.0
Exports	7.5	3.9	-8.3
Imports	5.0	5.2	-5.2
Consumer prices	2.3	2.8	0.6
Budget bal., % of GDP	-0.2	0.1	-3.6
Unemployment rate, %	9.0	7.8	9.0

Sources: Federal Statistical Office, DB Research 23

Public finances: Deficits rising above 3% of GDP

After a remarkable consolidation phase – the overall budget deficit of 4% of GDP in 2003 had disappeared entirely by 2008 – the economic downturn as well as government programmes to save banks and stimulate the economy will make public finances look considerably worse this year. The economic recession alone will likely create a budget deficit of 1 ½%. Taking the discretionary measures into consideration, the budget deficit will likely exceed markedly the Maastricht limit of 3% in 2009. However, this would not violate the reformed stability and growth pact. In 2010 the deficit will probably widen further to above 4% of GDP as our growth forecast of 1% still remains below potential.

We believe the recently agreed package of measures to stimulate the economy to be a step in the right direction. Among other things, it foresees improved depreciation regulations for small and medium-sized companies, higher tax deductions for private households for work done by tradespeople, a one-year exemption from vehicle tax following the purchase of a new car, an expansion of bank lending to SMEs, a prolongation of funding for short-time work and speedier realisation of infrastructure investment in the transport sector. At best, however, it will provide a small counterweight to the economic downturn. This has been recognised by the German government, which recently passed a second economic stimulus package worth EUR 50 bn, or roughly 2% of GDP. Major measures planned for 2009/2010 include additional infrastructure investment in the order of EUR 17.5 bn, cuts in personal income tax and social-security contributions to the tune of EUR 15.8 bn, a reduction in health-insurance contributions by 0.6 of a percentage point as well as subsidies for individual industries and short-time work. Even though this package obviously caters to the interests of the various government coalition partners, such a bundle of measures could prove beneficial in light of the theoretical and empirical uncertainties in analysing the effects of different strategies.

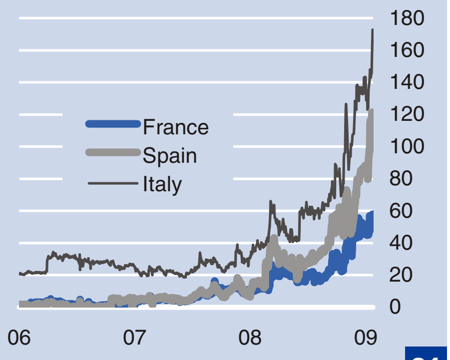
Deflation debate misses the point

After the spectre of inflation had haunted consumers and monetary policy decision-makers until the summer of last year – in July 2008 the rate of price increase stood at 3.5% – inflation slowed to slightly above 1 by the end of 2008. However, this slowdown in inflation, just like the preceding acceleration, was mostly due to oil price movements. Core inflation (excluding the volatile prices of energy and food) continued to hover around the 1% mark, which we also expect to see in the current year. So headline inflation will likely return to almost zero by the summer or will even be negative as a result of low oil prices, and amount to a good ½% on an annual average, down from 2.8% in 2008. This will fuel the recently intensified deflation debate further. In light of the stable core rate of inflation, however, we think this debate misses the point.

Deepest recession in post-war history

All in all we expect the German economy to continue to shrink at least until the middle of 2009. Stabilisation could set in gradually in the second half of the year, when the effects of monetary easing and fiscal stimulation kick in. Nonetheless, the economy will contract by about 2 ½% on average in 2009 and thus see the deepest recession in the post-war period. In 2010 the slight upturn will likely continue, but growth looks set to remain moderate, at 1%, as weak US growth rates will hardly provide a strong external impulse.

EMU: Yield spreads
Spread vs. 10Y Bunds, bp

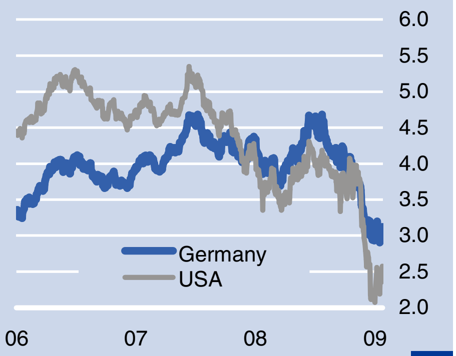


Source: DB Research **24**

Germany: Stock market volatility
Implicit volatility, VDAX

Source: Bloomberg **25**

Yields
10Y government bonds, %



Source: DB Research **26**

Risks to growth outlook extremely high at present

Given the uncertainty surrounding the financial crisis, there are very large downside risks to our growth outlook at this point in time. A new escalation of the financial crisis could speed up the economic downswing in the US once more and induce real US GDP to contract much more strongly than assumed so far. This would have repercussions for the emerging markets, Europe and of course Germany. However, the crises of 1987, 1997 and 2001 all turned out considerably less dramatic than forecast at their peak – so this should at least give rise to some hope.

Tensions persist on financial markets

Hopes that the situation on the financial markets, which had escalated dramatically following the collapse of Lehman Brothers, would calm down once the rescue packages for the banking sector had been agreed have so far failed to materialise. Most recently, market sentiment was clouded by drastically more pessimistic economic forecasts. The spreads between money market rates and key interest rates – reflecting the degree of uncertainty on the interbank market – have narrowed but are still much wider than the long-term average. Spreads between government and corporate bonds remain unchanged, at a level nearly three times as high as before the financial crisis. Even within EMU, yield spreads have widened to record levels since the introduction of the euro – and not only in the problem countries. Moreover, stock market volatility remains at crisis levels, which is a reflection of extreme uncertainty in the stock market and explains part of the low valuations. Up to now, safe investment in the form of government bonds of the most liquid markets have been sought after; accordingly, these yields have dropped temporarily to record lows (actual: 10Y Bund yields 3 ¼%; 10Y Treasuries 2 ½%).

In our scenario depicting gradual recovery around the end of 2009, stocks with current P/E ratios of around 8 (Dax) are very attractive on a medium-term horizon, while bonds look set to lose out, especially if deflation forecasts prove wrong. Over the next few months, however, more bad news will probably pour in from the business and financial sectors, so bonds will likely continue to be overvalued compared with stocks for the time being.

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