



Global Economy Report

May 2013



Global Economy Report

The Global Economy Report is prepared in cooperation by the Macroeconomic Research Division of Banca Aletti and the Global Governance Programme of the Robert Schuman Center for Advanced Studies of the European University Institute.

The objective of the Report is to provide an analysis of the current and expected macroeconomic and financial conditions at the global level, with also a focus on key economic areas such as Europe, the USA and ASIA.

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Report closed on May 20 2013



EXECUTIVE SUMMARY

- ❖ A big question at the moment is the extent of the recovery in the USA. After a stronger than expected Q1, the March/April data have become definitely weaker, incorporating the impact of Sequestration. Thanks to growth in Equity and in real estate, and to a modest variation of total households' debt in the past quarters, the households' net wealth is almost at the pre-crisis levels. The adjustment process in households' balances is at a good point, but not complete. Now households are adjusting spending priorities in order not to lose the progress accomplished. Thus, Q2 should be much weaker than Q1, although the improvement in investment intentions gives hope for the final part of the year. The unemployment rate will further drop, but we'll remain well above NAIRU.
- ❖ Overall, forecasts for growth in the USA are at 1.9% for 2013 and 2.7% for 2014. The principal risks are in fiscal policy and a possibly lower than expected global growth.



EXECUTIVE SUMMARY

- ❖ We expect inflation in the USA to remain below 2% for the whole forecasting period, thanks to the output gap accumulated during the Great Recession and in these three and a half years of weak recovery. The risks on our forecasts are on the downside if the correction on commodities were to continue, in line with the global slowdown. Overall, average headline CPI should be about 1.5% in 2013 and 1.7% in 2014, with the average core CPI at 1.8% in 2013 and in 2014.
- ❖ In terms of monetary policy, after the March FOMC, in which the Fed communicated that it's considering possible increases in the asset acquisition programme, we lengthened the estimates for QE3. As a matter of fact, we expect further acquisitions of Treasuries and MBS at the current rate of 85 bln USD per month, in total, till the end of the year. From 2014 we'll see a decrease in the acquisition rate and a definite suspension of the plan by mid 2014.



EXECUTIVE SUMMARY

- ❖ In the Euro area, in the first quarter of 2013, aggregate income decreased for the sixth quarter in a row (-0.2%). GDP diminished in France (-0.2%) and in Italy (-0.5%), while in Germany the increase was modest (+0.1%).
- ❖ The April survey of leading indicators confirms overall weakness and projects the persistence of recessive conditions also in the second quarter of the year.
- ❖ The element of highest concern is the noticeable worsening of the economic climate in Germany, where all components of the PMI index are simultaneously (and unexpectedly) below 50.
- ❖ Between April and June, we foresee again a declining evolution for aggregate income, due to modest growth in Germany and decreases in France and Italy. The average growth estimate for Eurozone for 2013 was cut by a tenth to -0.8%, as that for 2014, at +0.9%. The growth risks are downward.

EXECUTIVE SUMMARY

❖ Our average yearly GDP growth estimates for 2013 are at -0.5% for France, -1.8% for Italy, +0.1% for Germany, all below consensus. We highlight the negative revision on Germany's estimate by two tenths, motivated by the unexpected worsening of qualitative surveys in April. In 2014, the three major economies of the Union will simultaneously return to growth.

❖ Inflation continues to slow down, due to the current correction in international prices of raw materials, the lower than expected macro scenario and the great contraction of the qualitative surveys on prices. The general index slowed down at 1.2% in April (minimum since February 2010) and the core at 1.0% (minimum since February 2011). This has determined a reduction in our inflation forecasts, which are now at 1.4% in 2013 (decreased by 0.4% vs previous month), and 1.3% in 2014 (decreased by 0.3%).



EXECUTIVE SUMMARY

- ❖ For China, the economic recovery is slower than expected, with industrial production and retail sales that accelerated modestly in April and barely recuperated from the minimums of 2012. Qualitative indicators weakened, although in an expansion area. In the second quarter of 2013 there could be a new growth slowdown (our estimate is +7.5%), thus lowering the forecast for average yearly GDP growth of 8%.
- ❖ Chinese inflation accelerated in April, +2.4%, but only in the food component, which is rather volatile. Net of food, the price evolution is lower than expected. The risks are growing, above all for the pressure on the residential compartment, thus limiting the potential for further expansionary monetary policy.



EXECUTIVE SUMMARY

- ❖ In Japan the economic context is improving. Growth in the first quarter was at 3.5% annualized, higher than expected. The expansive impulse will last for the whole year, thanks to the extraordinary support of fiscal and monetary policy, which will insure a 1.9% growth in the yearly average (four tenths higher than in our previous forecast).
- ❖ In Australia, the RBA unexpectedly cut rates by 25 bp at its May meeting to 2.75%. The decision was justified by global growth slightly below trend this year. The Australian Economy is expected to grow below trend this year as well. At the same time, inflation is influenced by the exchange rate, with the Aussie dollar that remains stronger than expected, bringing a slowdown both in growth and inflation.





EXECUTIVE SUMMARY

GROWTH AND INFLATION FORECASTS

| | 2009 | 2010 | 2011 | 2012 | 2013E | 2014E |
|-------------------------|------|------|------|-------------|------------|-------|
| GDP (%YOY) | | | | | | |
| US | -3,1 | 2,4 | 1,8 | 2,2 | 1,9 | 2,7 |
| EUROZONE | -4,4 | 2,0 | 1,4 | -0,5 | -0,8 | 0,9 |
| GERMANY | -5,1 | 4,2 | 3,0 | 0,7 | 0,1 | 1,4 |
| FRANCE | -3,1 | 1,7 | 2,0 | 0,0 | -0,5 | 0,8 |
| ITALY | -5,5 | 1,8 | 0,4 | -2,4 | -1,8 | 0,4 |
| JAPAN | -5,5 | 4,7 | -0,6 | 2,0 | 1,9 | 2,0 |
| BRASIL | -0,3 | 7,6 | 2,8 | 0,9 | 3,1 | 3,6 |
| RUSSIA | -7,8 | 4,3 | 4,3 | 3,4 | 3,1 | 3,6 |
| INDIA | 6,4 | 8,9 | 7,5 | 5,2 | 5,1 | 6,1 |
| CHINA | 9,2 | 10,4 | 9,3 | 7,8 | 8,0 | 8,0 |
| AUSTRALIA | 1,4 | 2,6 | 1,4 | 3,6 | 2,6 | 3,0 |
| COREA | 0,3 | 6,3 | 3,6 | 2,0 | 2,8 | 3,8 |
| INFLATION (%YOY) | | | | | | |
| US | -0,4 | 1,6 | 3,2 | 2,1 | 1,9 | 2,0 |
| EUROZONE | 0,3 | 1,6 | 2,7 | 2,5 | 1,4 | 1,3 |
| GERMANY | 0,2 | 1,2 | 2,5 | 2,1 | 1,7 | 1,8 |
| FRANCE | 0,1 | 1,7 | 2,3 | 2,2 | 1,2 | 1,6 |
| ITALY | 0,8 | 1,6 | 2,9 | 3,3 | 1,8 | 1,7 |
| JAPAN | -1,3 | -0,7 | -0,3 | 0,0 | 0,1 | 2,2 |
| BRASIL | 4,9 | 5,0 | 6,6 | 5,4 | 6,0 | 5,7 |
| RUSSIA | 11,7 | 6,9 | 8,5 | 5,1 | 6,4 | 5,6 |
| INDIA | 10,8 | 12,1 | 8,9 | 9,3 | 9,0 | 8,3 |
| CHINA | -0,7 | 3,3 | 5,4 | 2,7 | 3,0 | 3,5 |
| AUSTRALIA | 1,8 | 2,9 | 3,3 | 1,8 | 2,6 | 2,6 |
| KOREA | 2,8 | 3,0 | 4,0 | 2,2 | 2,4 | 3,0 |

Banca Aletti Forecast

Cons. Bloomberg (Mag 13)

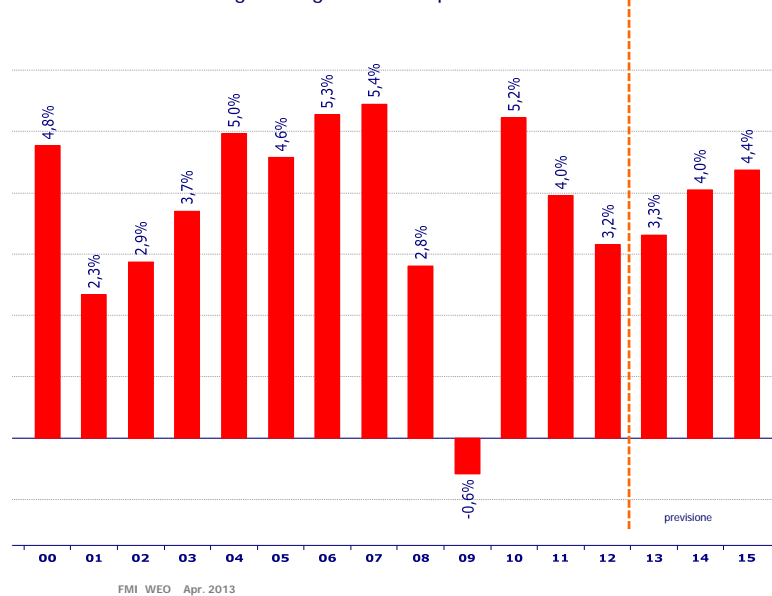
FOCUS ON THE GLOBAL ECONOMY



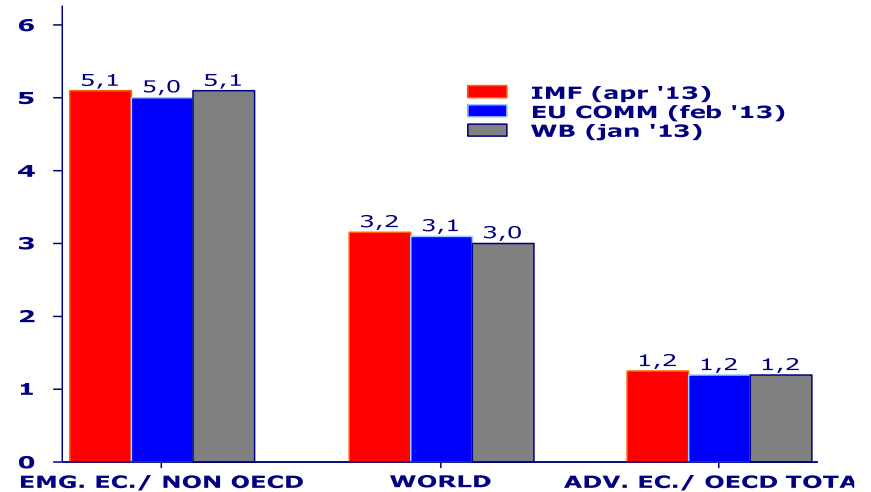
The IMF expects the total income for this year to grow by 3.3%, while in 2014 it will increase up to 4%. According to IMF, the fall of Eurozone and the fiscal cliff in the US are the risks that authorities and those in charge of economic policies avoided with success, as acknowledged by markets and by the improvement of global financial stability. Nevertheless, critical situations remain: in Eurozone a scenario of strong economic stress due to the adjustment for financial imbalances, worsened in the periphery by insufficient access to credit. In the US and Japan there are medium term risks due to fiscal policies that don't target public debt.

IMF - GLOBAL ECONOMIC GROWTH

Annual Average Change – at fixed prices



2012 IMF - EU COMM. - WB



FMI WEO
EU COMMISSION
WORLD BANK

Apr. 2013
winter 2013
Jan. 2013

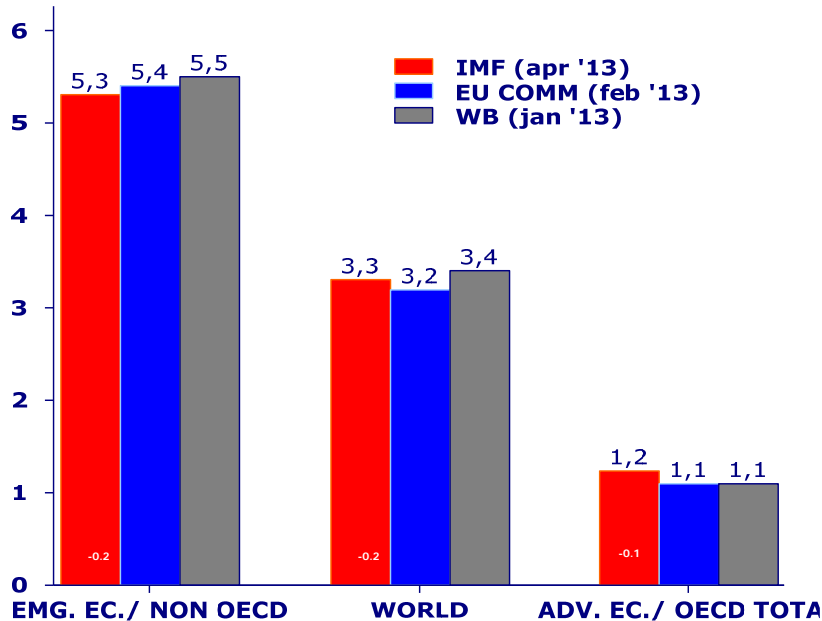


ECONOMIC GROWTH FORECASTS

In 2013, expected income for the industrialized economies should have a limited growth, around 1.2%, while that of the emerging economies should increase by 5.3%. In 2014, growth should be stronger, thanks to the 5.7% pull from emerging economies and to the improvement in industrialized economies, growing at 2.2%.

2013 IMF - EU COMM. - WB

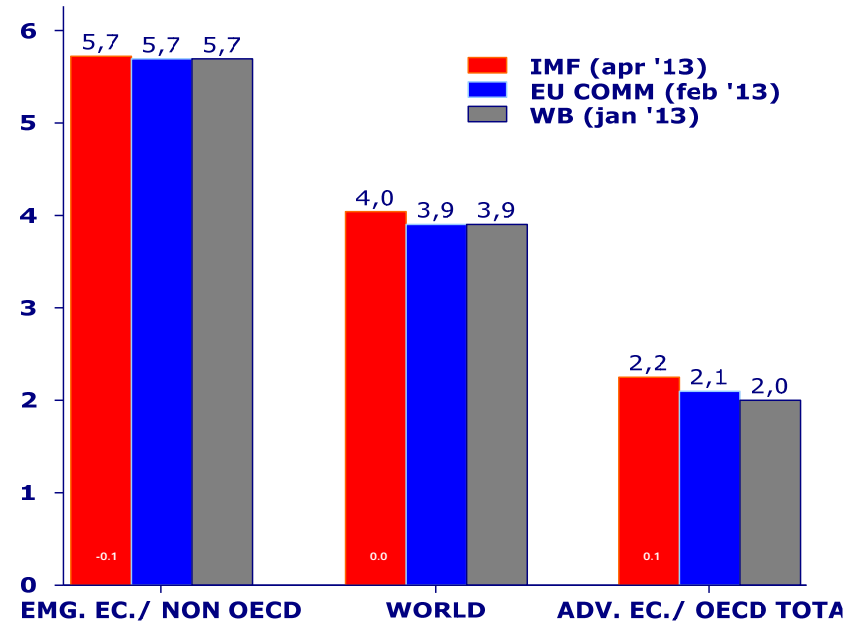
Annual Average Changes – at fixed prices



In the IMF column we also report changes on previous forecast

2014 IMF - EU COMM. - WB

Annual Average Changes – at fixed prices

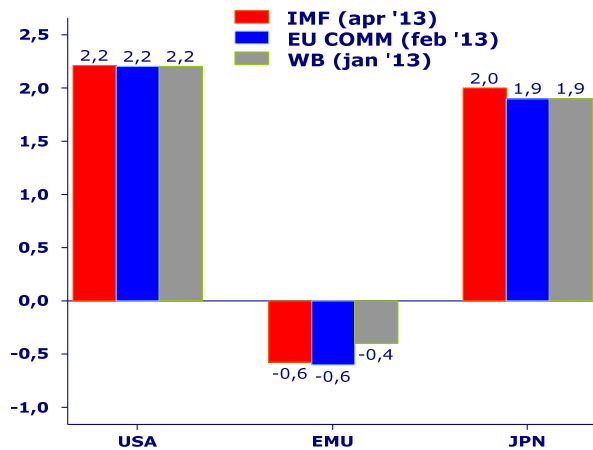


ECONOMIC GROWTH FORECASTS

Among industrialized economies low demand will find scarce support from economic policy, whose only aim is to reduce debt. The fiscal adjustments should continue, but gradually and with an accommodating monetary policy, waiting for structural reforms already in place to stimulate growth potential. For the US, IMF estimates a growth of 1.9% (from 2.2% in 2012), subject to risks relating to restrictive fiscal policy. In 2014 growth is expected to be at 3%. As for Japan, growth should be at 1.6%, thanks to the extraordinary expansive economic policy, with more evident effects on the following year, when the expected income increase is 1.4%. For Eurozone, the phase of income contraction started last year (-0.6%), should continue this year with a 0.3% decrease; while in 2014 the Eurozone should turn positive, with a GDP growth of 1.1%.

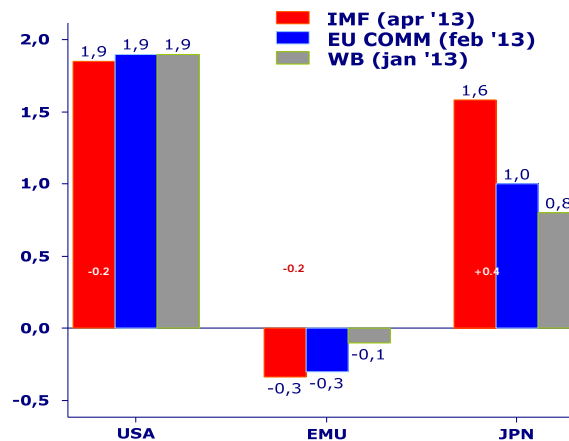
2012 IMF - EU COMM. -WB

Annual Average Change- at fixed prices



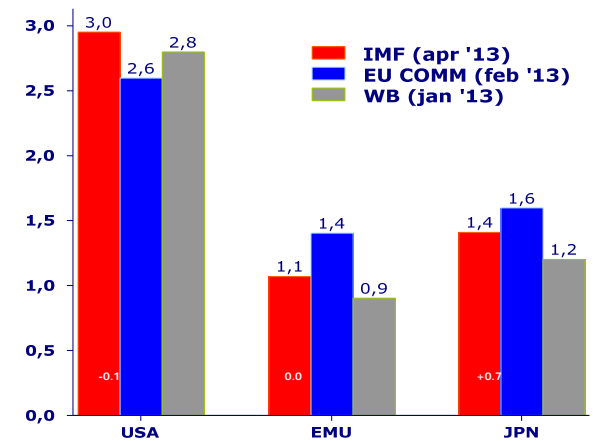
2013 IMF - EU COMM. -WB

Annual Average Change- at fixed prices



2014 IMF - EU COMM. -WB

Annual Average Change- at fixed prices



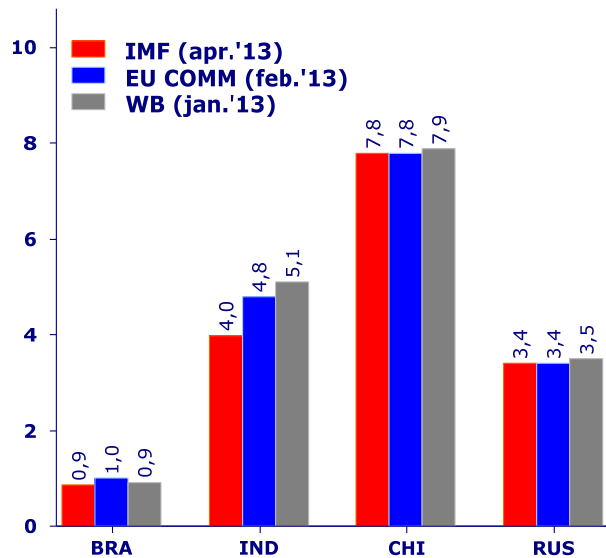
In the IMF column we also report changes on previous forecast

FMI WEO update Apr. 2013
EU COMMISSION winter 2013
WORLD BANK Jan. 2013

As for emerging markets, the expected economic growth, less intense than previous indications, is still very solid. Relatively to the 2013-2014 period, the IMF has cut its growth estimates for BRIC countries. In 2013 the forecasts on Brazil were cut by 0.5% to 3%, those for India by 0.2% to 5.7%, those on China by 0.1% to 4%, those for Russia by 0.3% at 3.4%. As for next year, revisions are mixed: Brazil has a positive correction of 0.1% to 4%, Russia remains at 3.8%, as the estimate on India was cut by 0.1% to 6.2% and that on China was lowered by 0.3% to 8.2%.

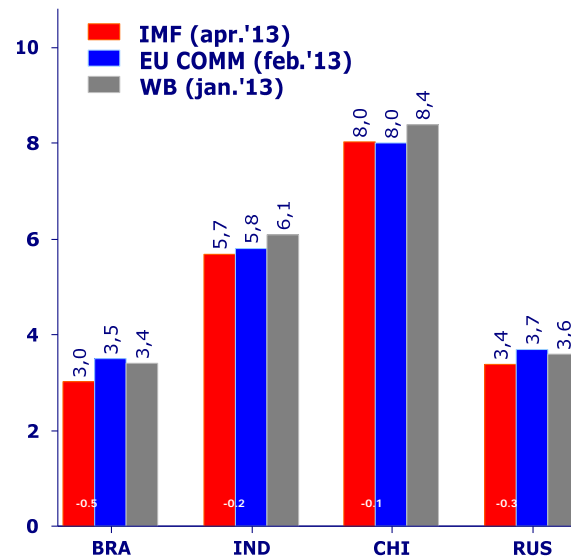
2012 IMF - EU COMM. -WB

Annual Average Change– at fixed prices



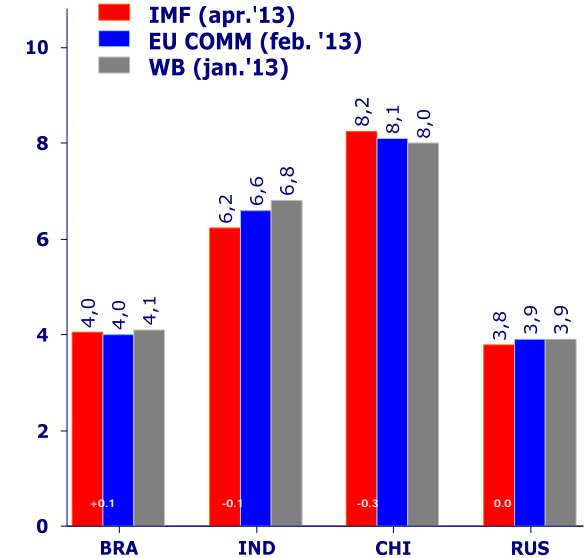
2013 IMF - EU COMM. -WB

Annual Average Change– at fixed prices



2014 IMF - EU COMM. -WB

Annual Average Change– at fixed prices



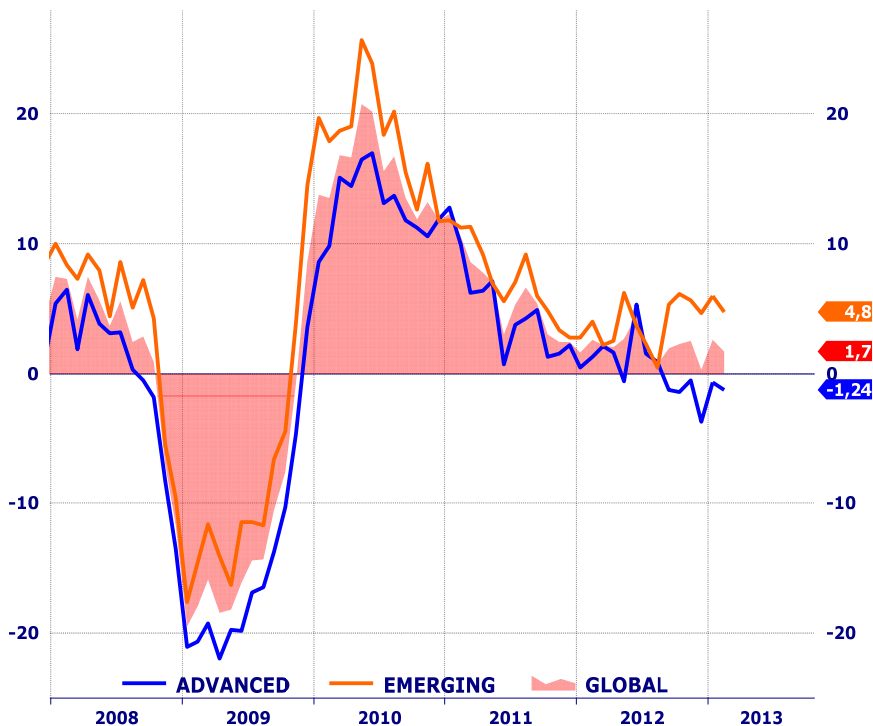
FMI WEO update Apr. 2013
EU COMMISSION winter 2013
WORLD BANK Jan. 2013

INTERNATIONAL TRADE

At the beginning of the year, international trade expressed in volumes exported showed an annual increase of 1.7%, a still low figure, but better than at the end of 2012. This growth is due to emerging markets whose index grew by 4.8%. The figure relative to industrialized markets is still negative (-1.2%), however the trend highlights a reduction of negativity. Based on the leading indicator (PMI global manufacturing-new orders) there is a high probability that exchanges will intensify in the near future.

INTERNATIONAL TRADE – EXPORT

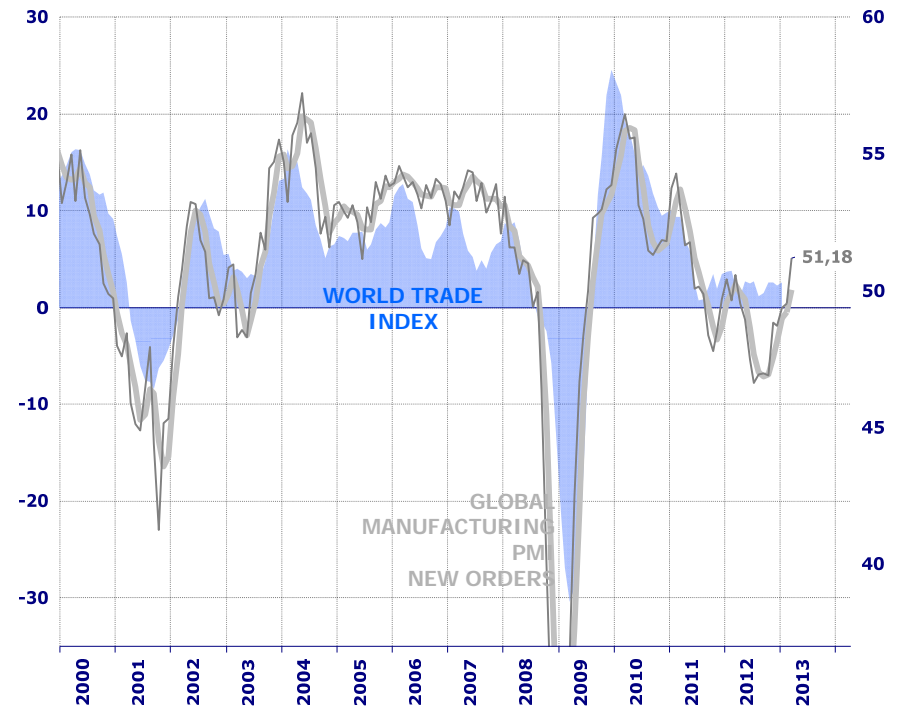
CPB indexes Export volumes, yearly changes



| | | | | |
|------------------------|--------|-------|------|------|
| 2.57 | -12.54 | 16.03 | 5.92 | 1.98 |
| dati medi annui EXPORT | | | | |

INTL. TRADE AND LEADING INDICATOR

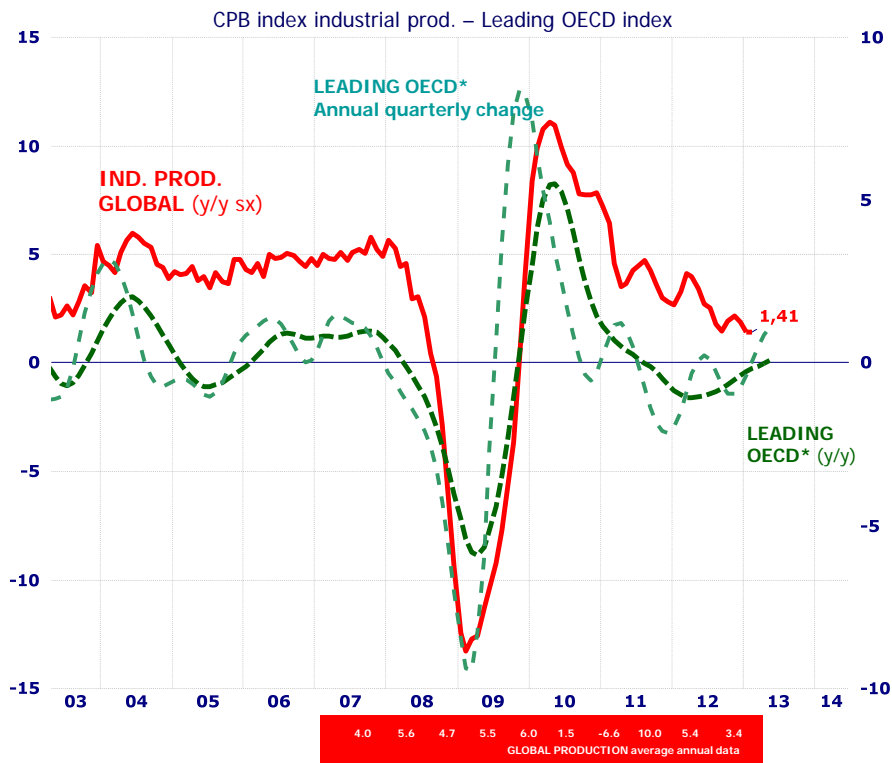
World trade quarterly index 6m average, annualized– PMI new orders export



| | | | | | | | | | | | | |
|--|------|-----|-----|------|-----|-----|-----|-----|-------|------|-----|-----|
| 13.1 | -0.2 | 3.1 | 5.8 | 10.4 | 7.3 | 8.9 | 6.7 | 2.3 | -12.6 | 15.1 | 5.8 | 2.2 |
| dati medi annui COMMERCIO INTERNAZIONALE | | | | | | | | | | | | |

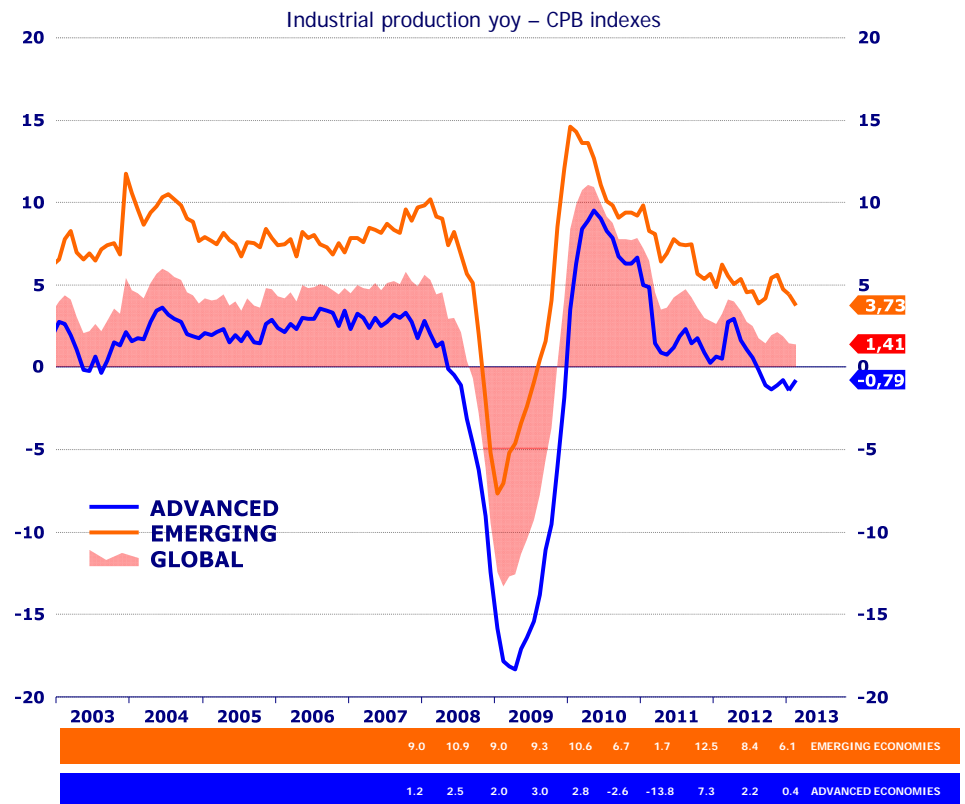
Global industrial activity remained at the low growth levels of the end of 2012, registering a 1.4% annual growth in February, stimulated by emerging markets (however production is modest at 3.7%) and dragged down from the contraction of industrialized economies (-0.8%). The forecasts are improving, so we continue to presume a consolidation, followed by an acceleration.

IND. PRODUCTION GLOBAL AND LEADING



LEADING OECD*: Advanced industrial Economies + BRIC + South Africa + Indonesia

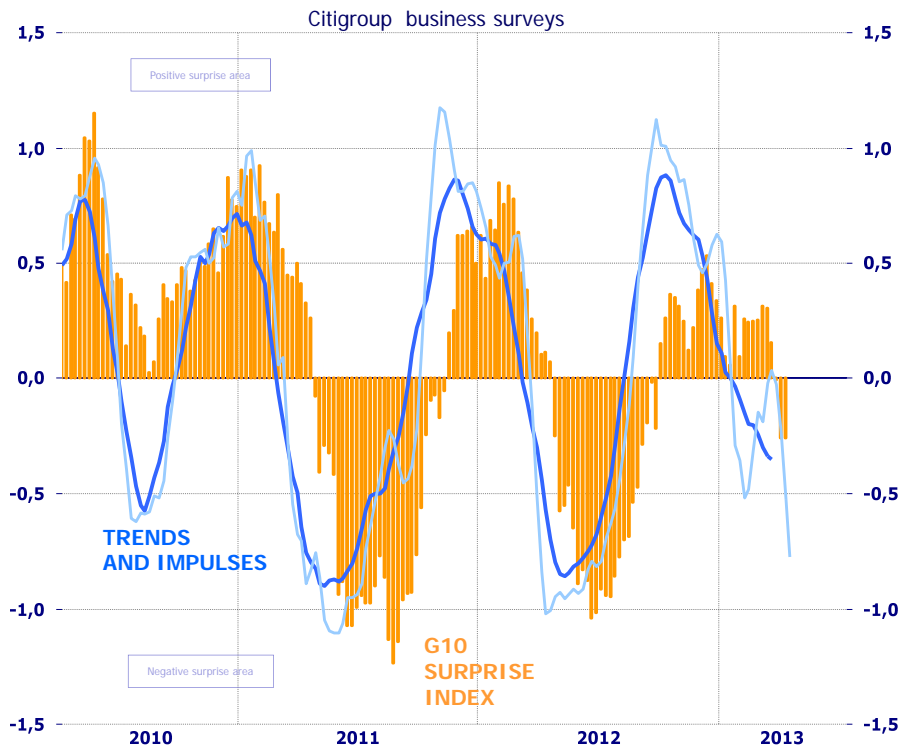
INDUSTRIAL PRODUCTION



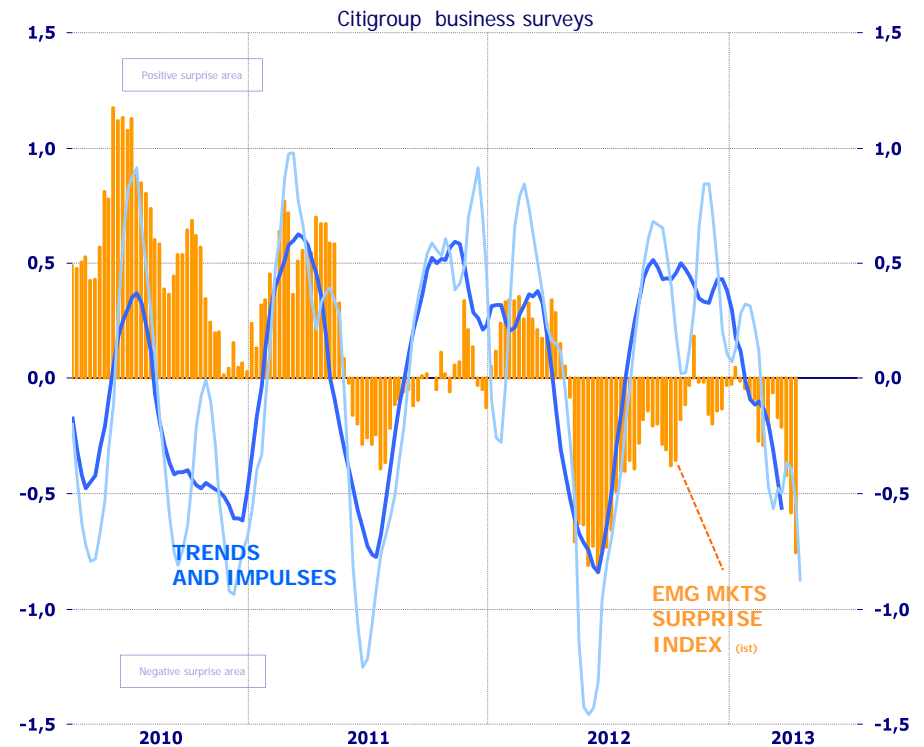
ECONOMIC ACTIVITY

Analysts' expectations compared to effective economic data are markedly different, with mostly negative surprises for G10 and a net worsening for Emerging Markets already below expectations. Both indicators are decreasing as hadn't happened since many months ago and our analysis foresees no inversion in this trend in the short term.

G10 ECONOMIC SURPRISE INDEX



EMERGING MKTS ECONOMIC SURPRISE INDEX

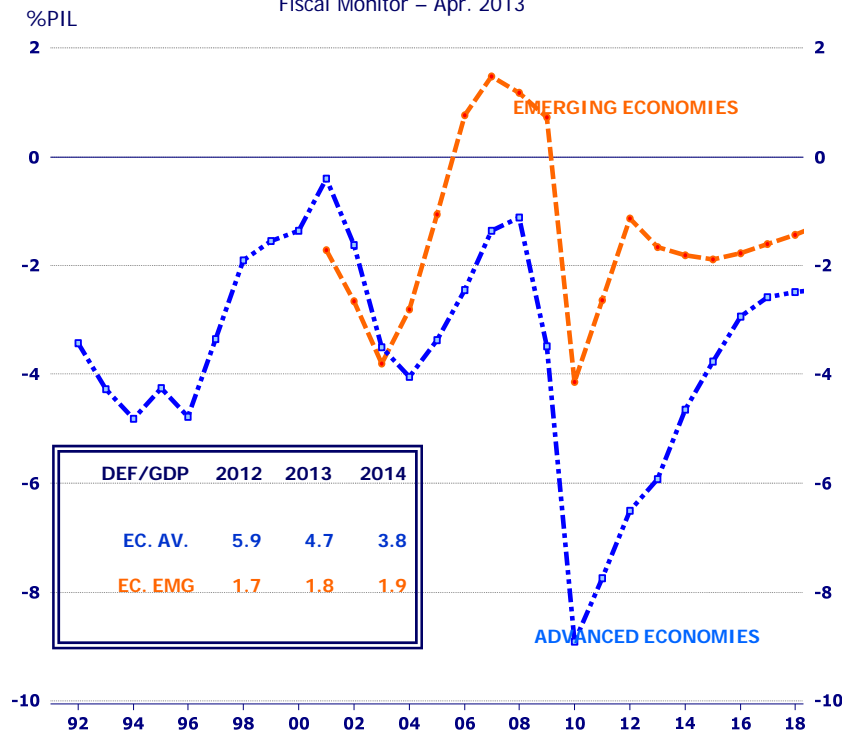


PUBLIC FINANCE

The efforts to reduce the imbalances in public finances will manage to invert the growth trend of public debt versus GDP only starting in 2014. If Japan and the US suffer a primary deficit, around half of all major industrialized economies have a primary surplus lower than 2%, insufficient to stabilize debt. Many countries, mostly in Europe, suffer from an unfavourable differential between interest rates and growth rates. The opposite phenomenon happens in many emerging countries, in spite of the decrease in growth rates, so that their decreasing trend in Debt/GDP will continue.

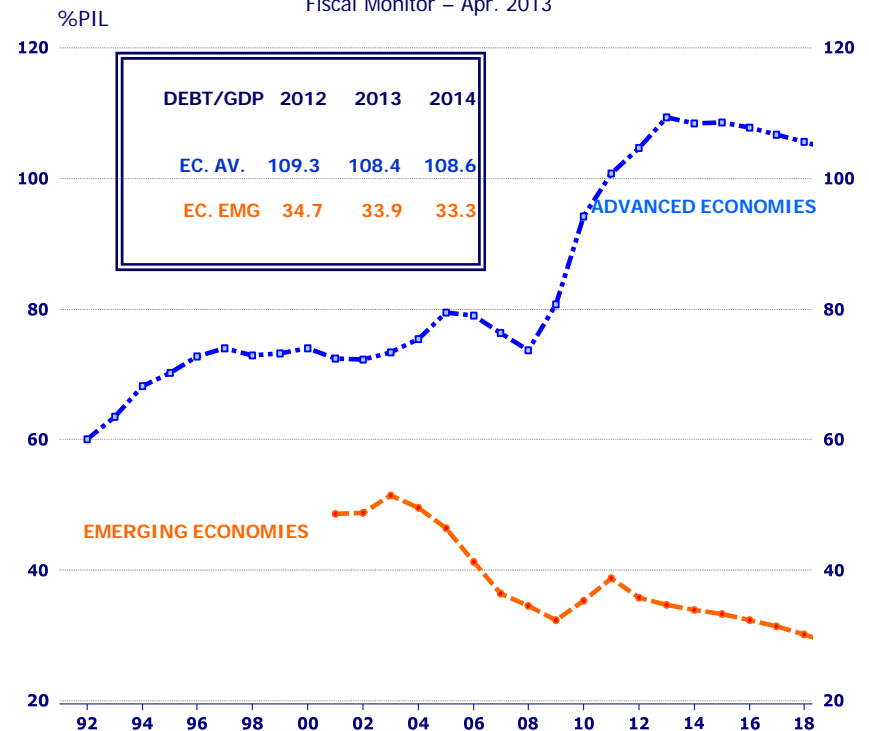
DEFICIT/GDP – IMF ESTIMATES

Fiscal Monitor – Apr. 2013



DEBT/GDP – IMF ESTIMATES

Fiscal Monitor – Apr. 2013

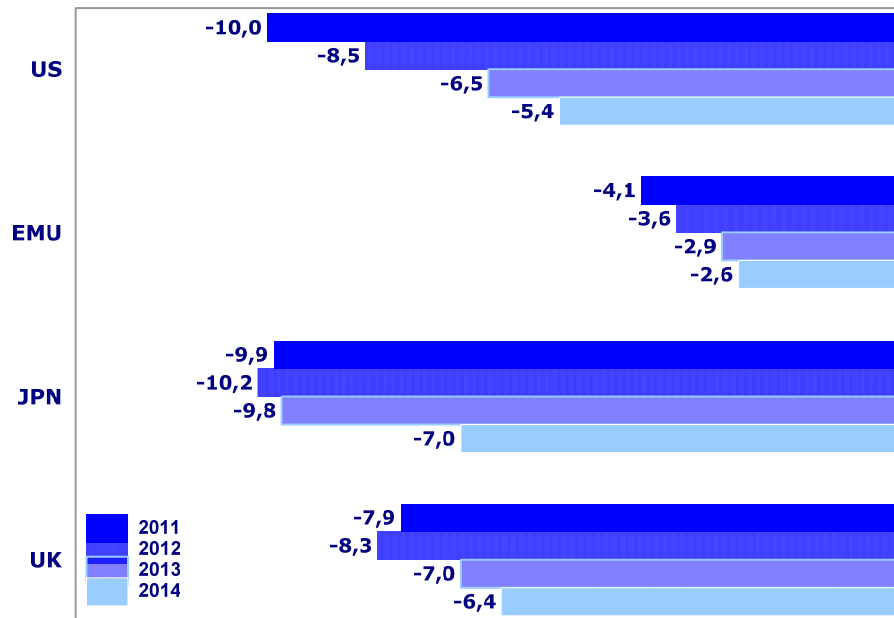


PUBLIC FINANCE

As to the principal advanced economies, also the most recent data from the European Commission indicates that the current deficit contraction should bring Eurozone to 2.8-2.7%, with the US at 6.6-5.9%, the UK at 7.4-6% and Japan at 9.1-8%. This year the Eurozone debt according to IMF shows a trend under 95%, progressively diverging from the still growing ratio in other countries, with the US at over 110% and Japan at over 240%, countries where the structural balance is not a strategic target yet. Also for the UK, the goal of balancing public finances is still very difficult due to low economic growth and inflation which is not under control, thus Moody's downgrading from Aaa to Aa1.

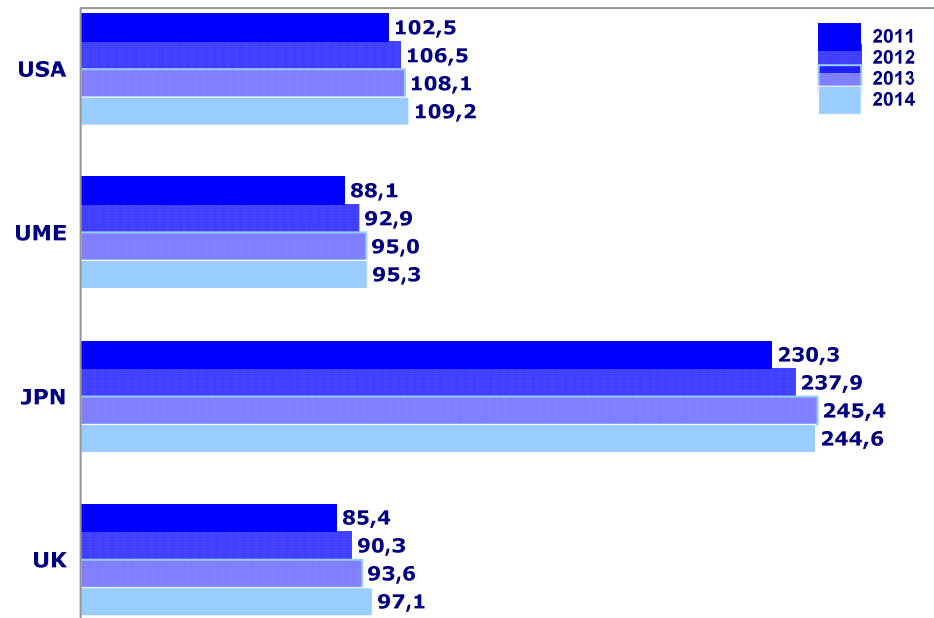
DEFICIT /GDP DATA AND ESTIMATES – 2011-2014

Source IMF – Fiscal Monitor Apr. 2013



DEBT /GDP DATA AND ESTIMATES – 2011-2014

Source IMF – Fiscal Monitor Apr. 2013

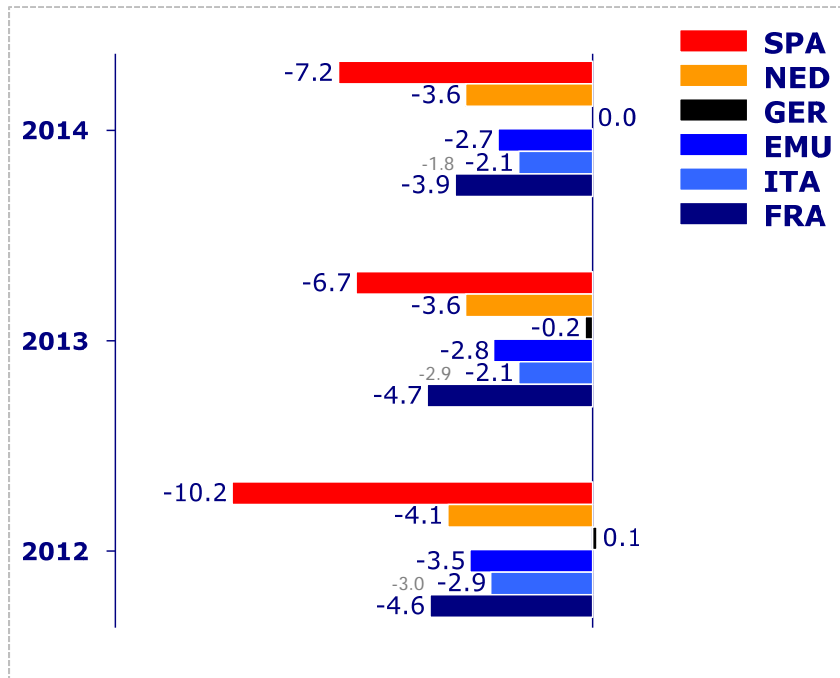


PUBLIC FINANCE EUROZONE

Among Eurozone countries, the bad cycle, the rise in interest rates in early 2012 and the Euro crisis have produced negative effects on public finances. With great effort, Spain will reach a 6.7% deficit this year (from 10.2%), while France will remain at over 4.5%; as for Italy, in March the Government indicated a growing public deficit in absolute value at 2.9% (8 p.p. Higher than EU Commission forecasts) for this year, but a 1.8% reduction (3 pp less) for 2014. With the exception of Germany, the debt/GDP ratio grows for all the major countries of the area.

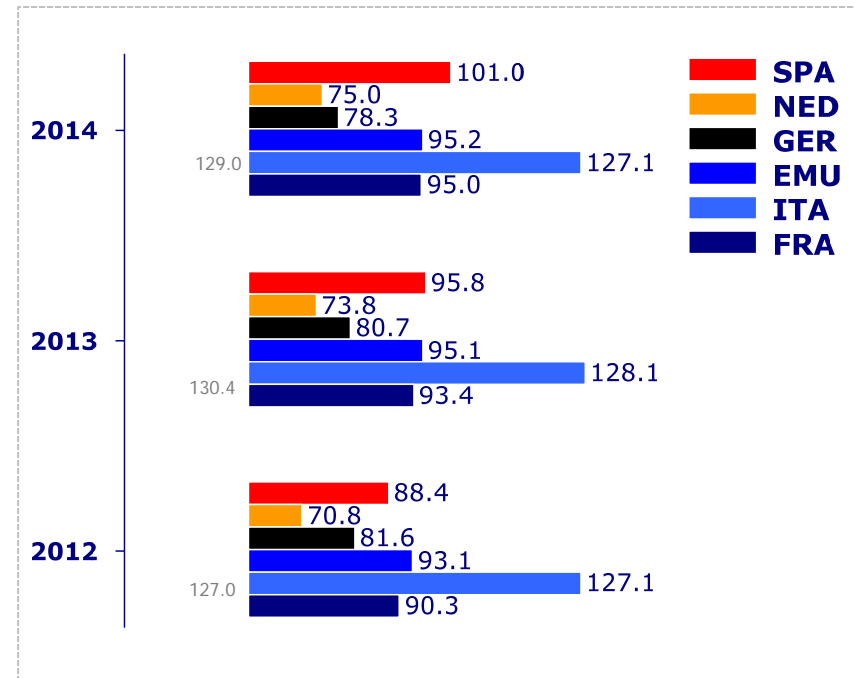
DEFICIT /GDP DATA AND ESTIMATES– 2012-2014

Source EU COMMISSION – Winter forecast Feb. 2013



DEBT /GDP DATA AND ESTIMATES– 2012-2014

Source EU COMMISSION – Winter forecast Feb. 2013



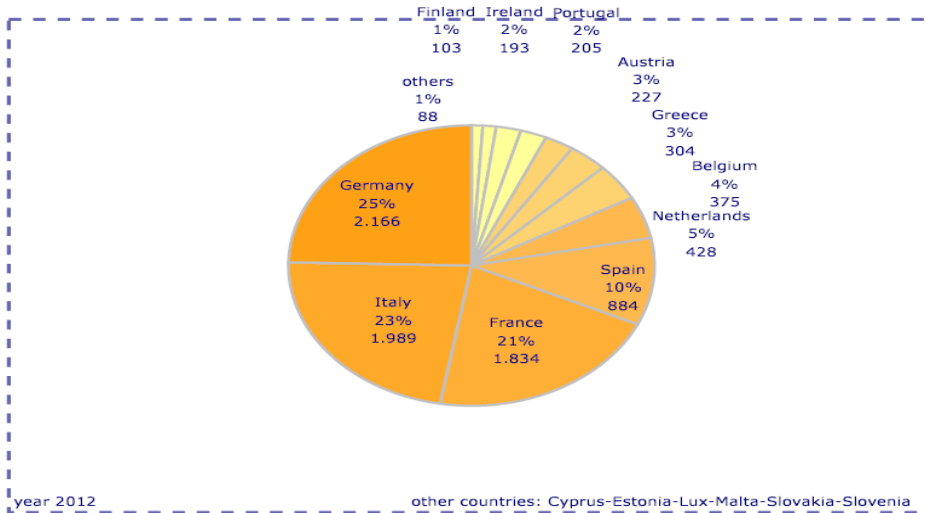
Above and in the following pages, Italy has different data from EU Commission forecasts (in the graphs next to the original figure) mostly due to change in debt, that comprises expense to cover outstanding public administration debt toward private vendors.



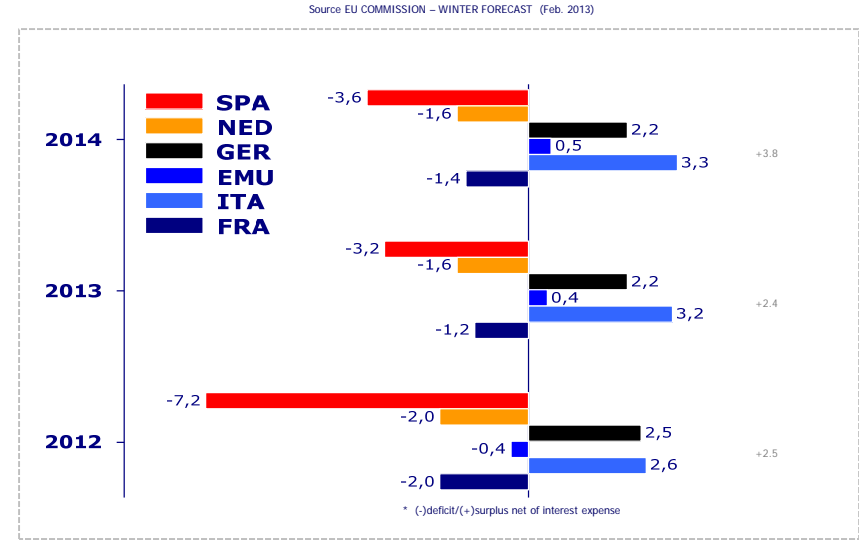


PUBLIC FINANCES EUROZONE

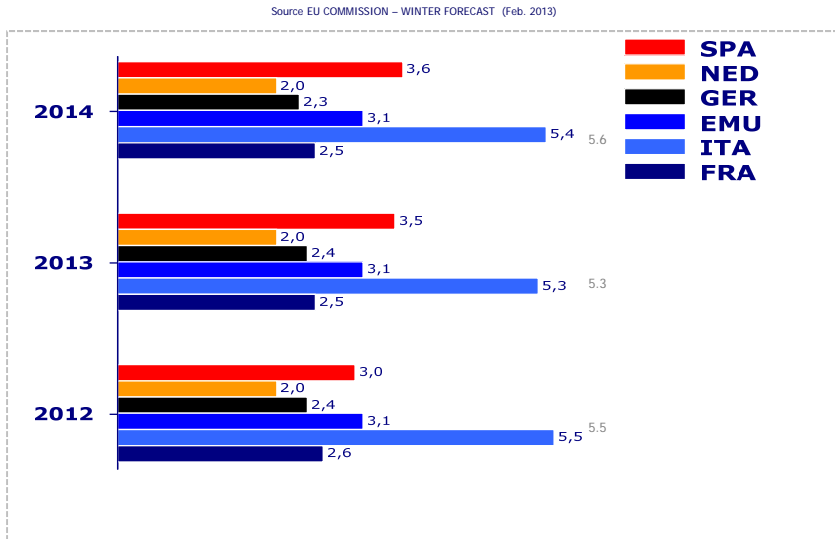
DEBT EUROZONE 2012 – MEMBER STATES



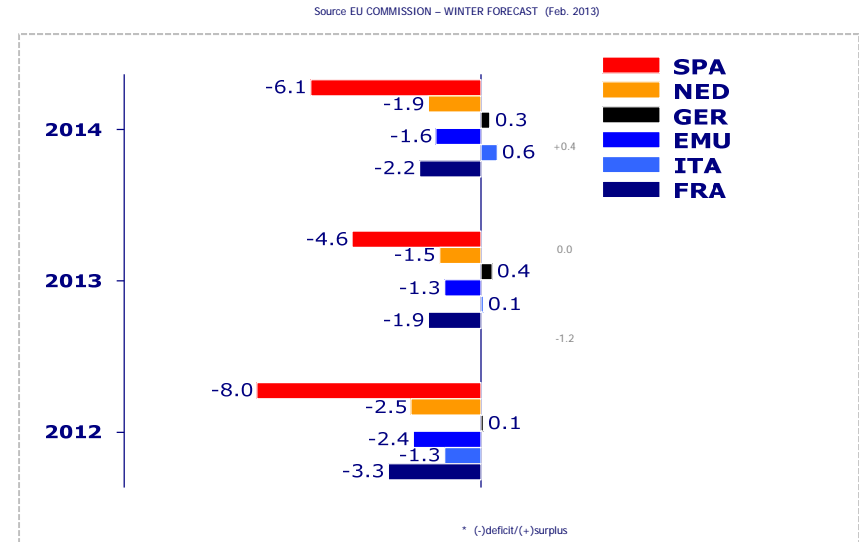
BUDGET – PRIMARY BALANCE* 2012-2014



INTEREST EXPENSE ESTIMATES 2012-2014



BUDGET – BALANCE ~CYCLE* 2012-2014

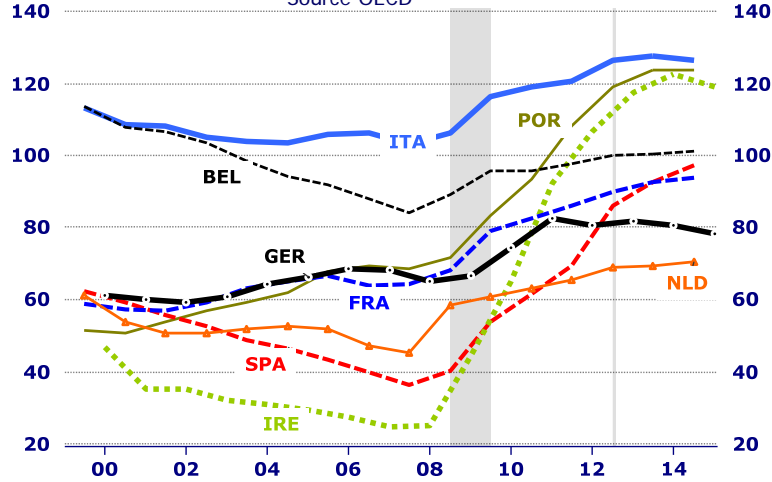




EUROZONE CRISIS

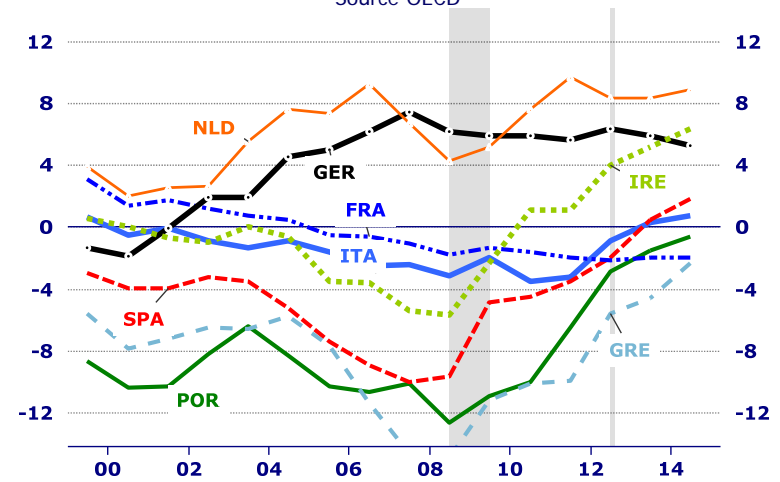
DEBT/GDP

Source OECD



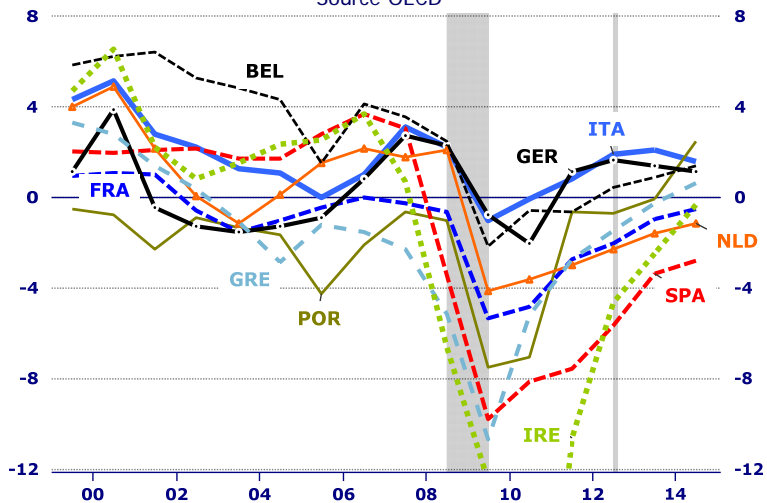
CURRENT ACCOUNTS/GDP

Source OECD



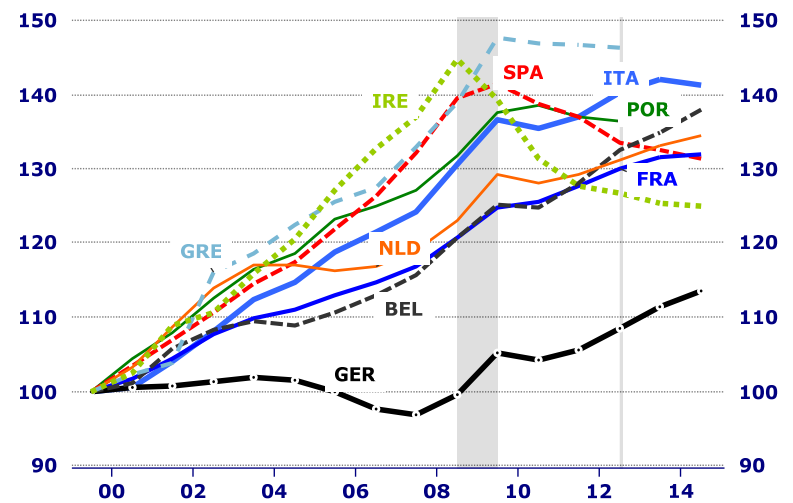
PRIMARY BALANCE ADJ. PER CYCLE

Source OECD



LABOUR COST

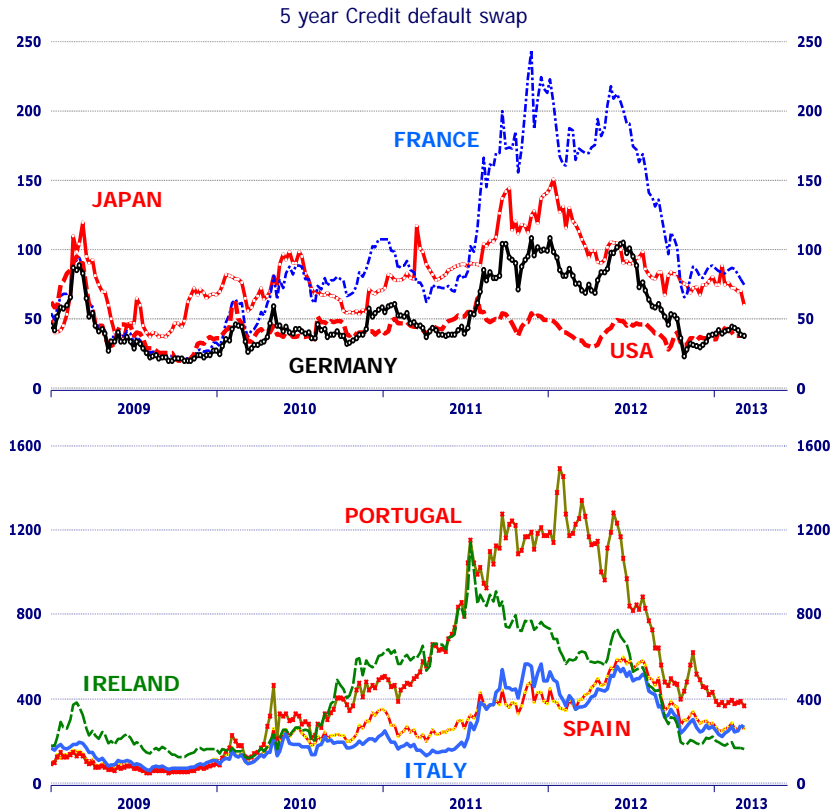
Base indexes 100- Source OECD



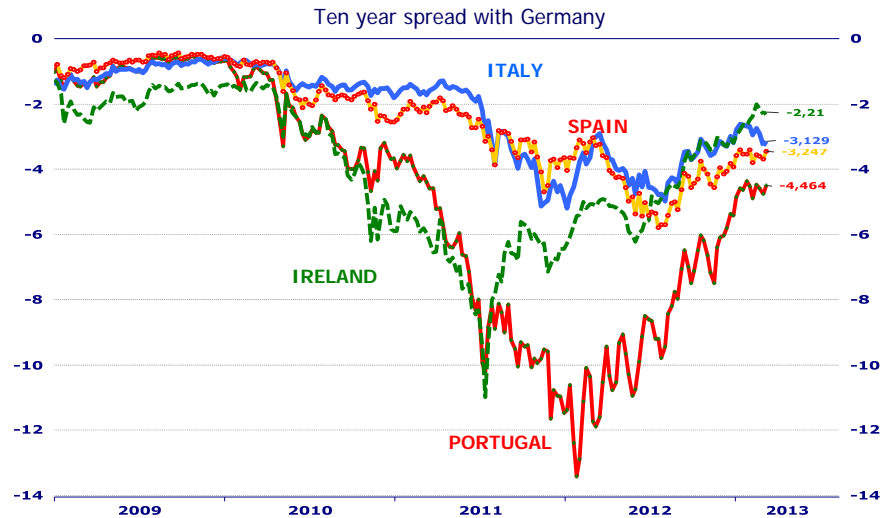
PUBLIC DEBT AND SOLVENCY

In Europe, the UK debt was downgraded first by Moody's (Aa1 from Aaa) and then by Fitch from the maximum AAA to the lowest AA+, due to the financial difficulties the country is going through for low growth. The credit lines opened to Ireland and Portugal have been renewed for seven years with the aim of supporting the two economies that are proceeding with the adjustment plan but with difficulty. Italy should exit the infraction procedure for excessive deficit and has obtained the possibility to increase its deficit (without exceeding the 3% limit) to partly reimburse the business credits accumulated in the past years by the Public Administration.

COUNTRY RISK – 5 YEAR CDS



COUNTRY RISK AND RATING



| | Moody's | S&P | Fitch |
|----------|---------|--------|-------|
| Italy | Baa2 | BBB+ u | BBB+ |
| Spain | Baa3 | BBB- | BBB |
| Ireland | Ba1 | BBB+ | BBB+ |
| Portugal | Ba3 | BB | BB+ |
| Greece | C | B- | B- |
| France | Aa1 | AA+ | AAA |
| Germany | Aaa | AAA | AAA |
| Japan | Aa3 | AA- | AA- |
| USA | Aaa | AA+ | AAA |

Source Bloomberg, rating 05/16/2013

After deep uncertainty and with the usual confused modus operandi, Europe decided Cyprus's bailout, fifth Eurozone country to receive help from the Union and from the IMF for a situation of profound crisis of the banking sector, where -without the international intervention- the State would've become insolvent. The E.U. and the IMF decided on a 10 billion euro loan, while Cyprus decreed it guarantees deposits up to 100 thousand euros, but will tax deposits over that limit. The main points of the deal are the restructuring and sale of Laiki bank: a Bad bank will absorb all bad debts, corporate bonds and non insured deposits, while insured deposits will go into Bank of Cyprus.

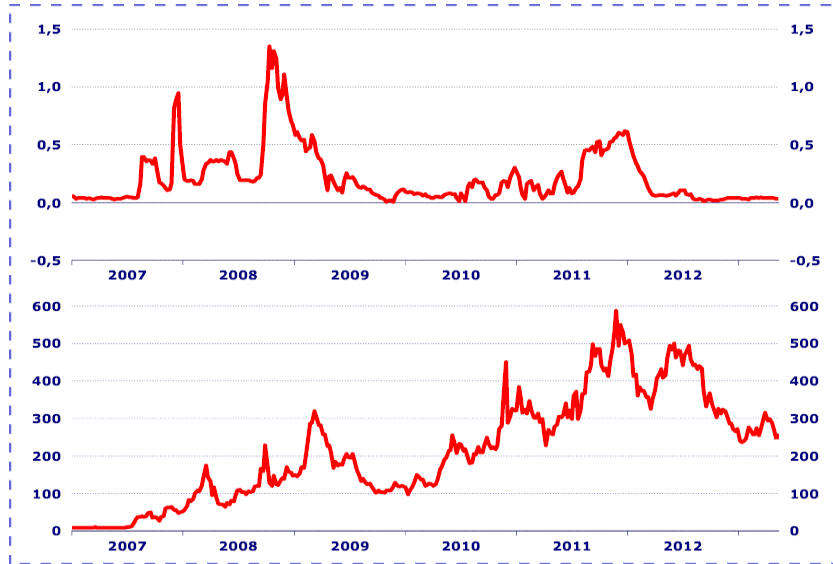
EURODOLLAR AND PUBLIC DEBT CRISIS





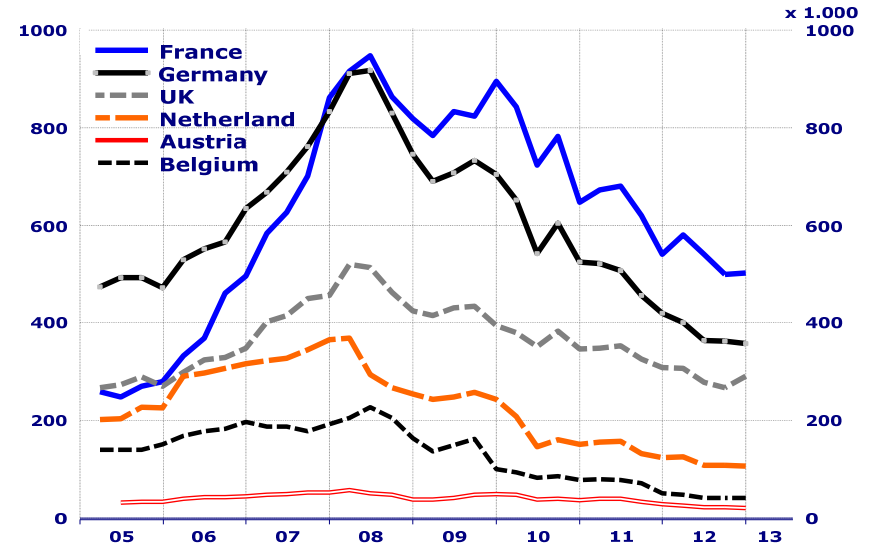
MONETARY POLICY AND FINANCIAL CONDITIONS

OIS SPREAD & CDS €BANKS



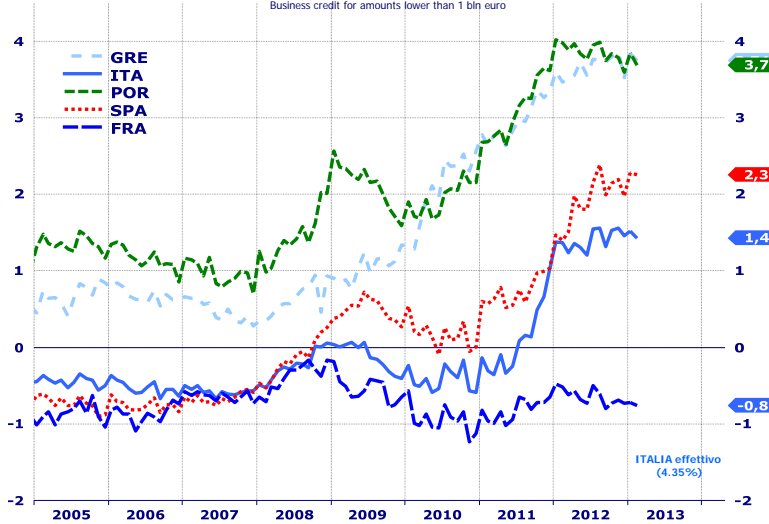
BANKS' COMMITMENTS EXPOSURE vs PERIPHERALS

€ bin Banks, aggregate data vs Italy, Ireland, Greece, Spain, Portugal



INTEREST RATES' SPREAD vs GERMANY

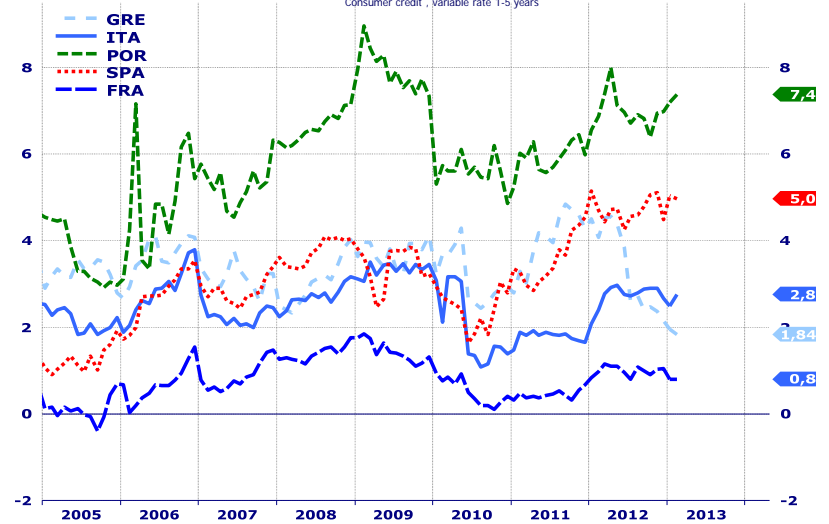
Business credit for amounts lower than 1 bin euro



ITALIA effettivo (4,35%)

INTEREST RATES' SPREAD vs GERMANY

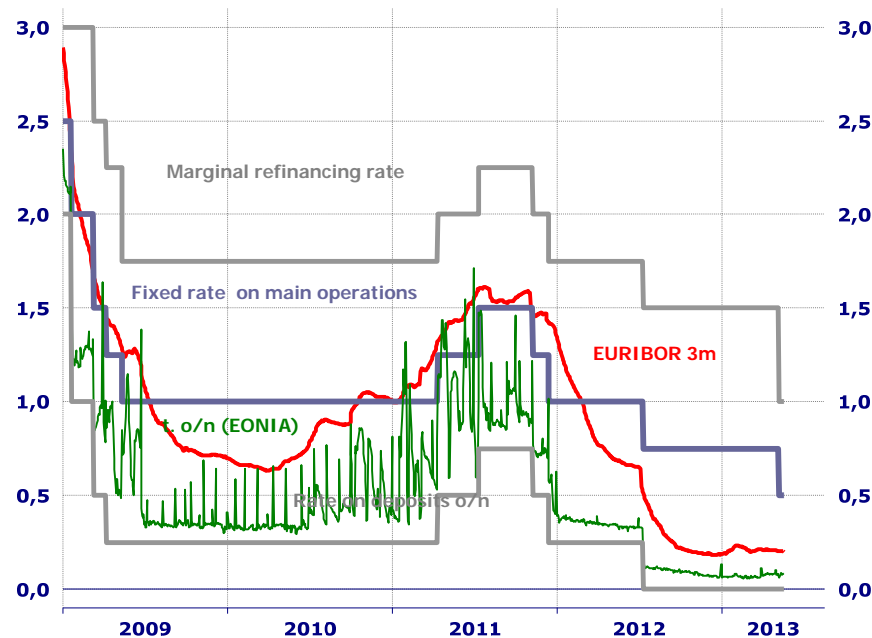
Consumer credit - variable rate 1-5 years



MONETARY POLICY AND FINANCIAL CONDITIONS

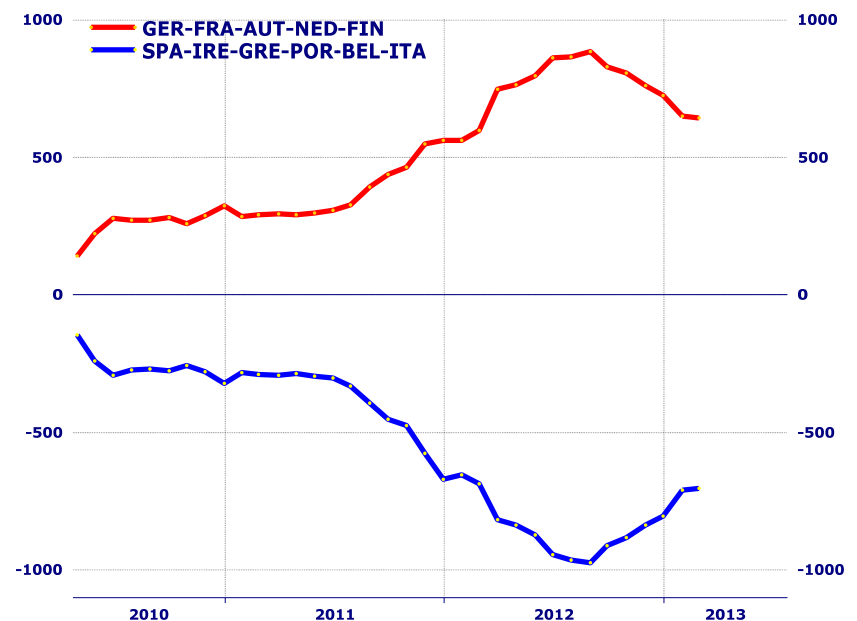
The mid-April Ecofin in Dublin definitely approved the political agreement for centralizing credit vigilance transferring this task to the ECB, A basic step towards the banking union. The path to implement this plan remains full of hurdles, with issues ranging from modifying the Treaty to the risk of member state governments introducing rules that amplify discretionary interventions in case of restructuring banks. Again in April, the principal European authorities (Parliament, Commission and Council) approved new rules on fiscal control and policy. The "Two Pack" regulatory package includes general measures for Eurozone member states and specific rules for countries under special procedure for excessive deficit. It also includes measures for countries under great financial stress that are applying for or have already applied for a regime of fiscal support.

ECB – OFFICIAL INTEREST RATES' CORRIDOR



EUROZONE - BALANCES TARGET2

COUNTRIES CREDITORS vs DEBTORS (€ bln)

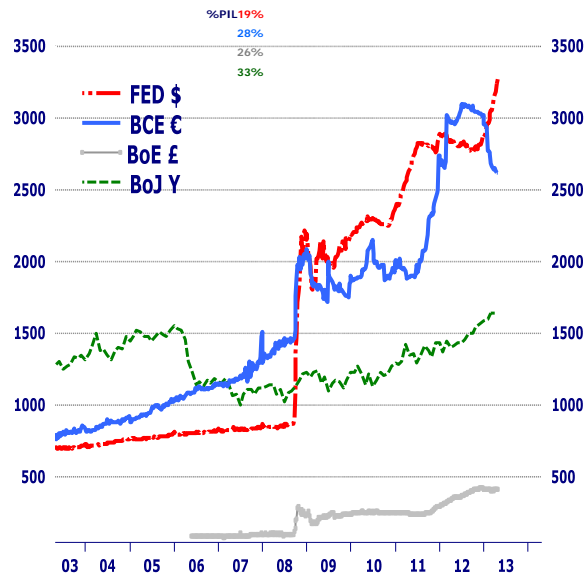


MONETARY POLICY AND FINANCIAL CONDITIONS

In a regime of monetary policy that President Draghi defined very accommodative, the financial system in the Eurozone offers less critical conditions, as shown also by the speedy restitution of liquidity that banks had previously borrowed. However, a condition of inadequacy of banks' capital remains, so that in certain countries credit crunch dynamics are stronger. The ECB reduced interest rates by 0.50%, a measure deemed insufficient considering the bad transmission system from centre to periphery and the severe credit crunch in certain countries.

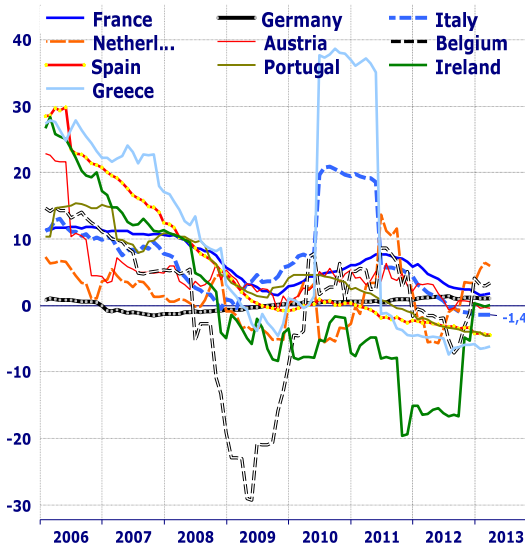
CENTRAL BANKS BUDGET

Total assets, local currency and as %GDP



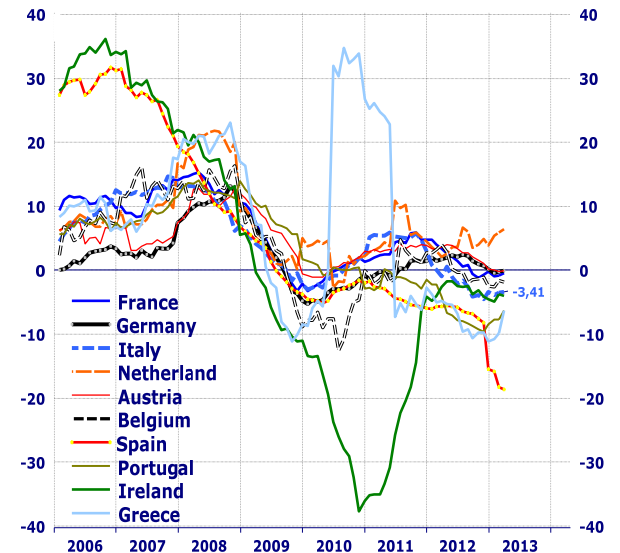
BUSINESS CREDIT

Annual growth rate



FAMILY CREDIT

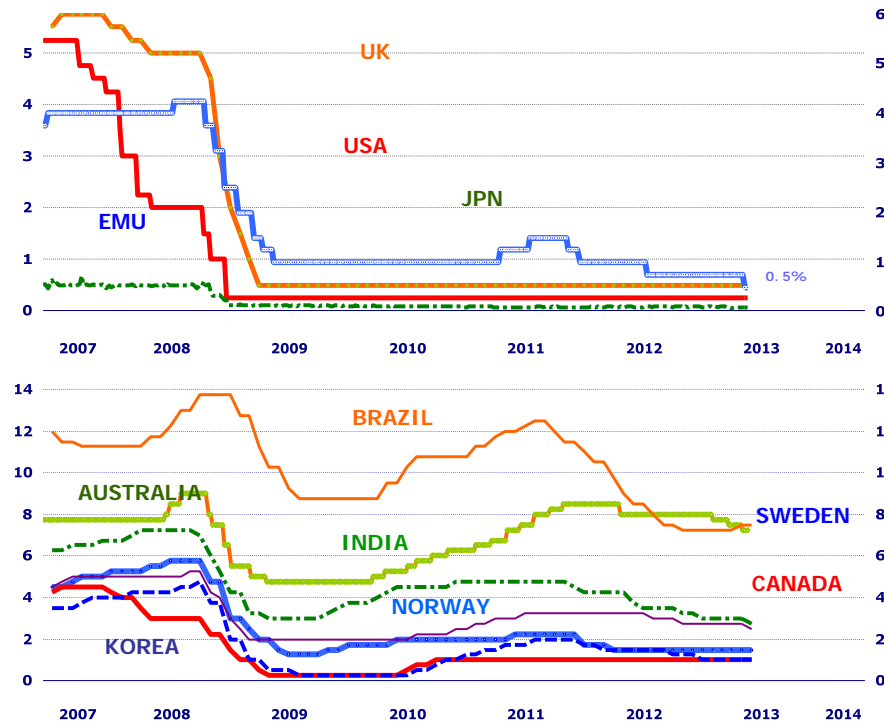
Annual growth rate



MONETARY POLICY

The FED confirmed in May its quantitative easing program with purchases worth 85 billion dollars per month. However, the Statement had some slight, though important, changes. In fact, the FOMC stated it's ready to either increase or decrease the monthly pace of asset purchases according to changes in the outlook for the labour market and for inflation. Moreover, at its April meeting, the BoJ strengthened its unconventional measures of monetary policy, with the objective of giving a quantitative and qualitative monetary stimulus to the economy, aiming to bring inflation to 2% in 2 years time. With this target, BoJ will double the monetary base, will also double JGBs and ETFs holdings and it will lengthen the duration of JGBs withheld.

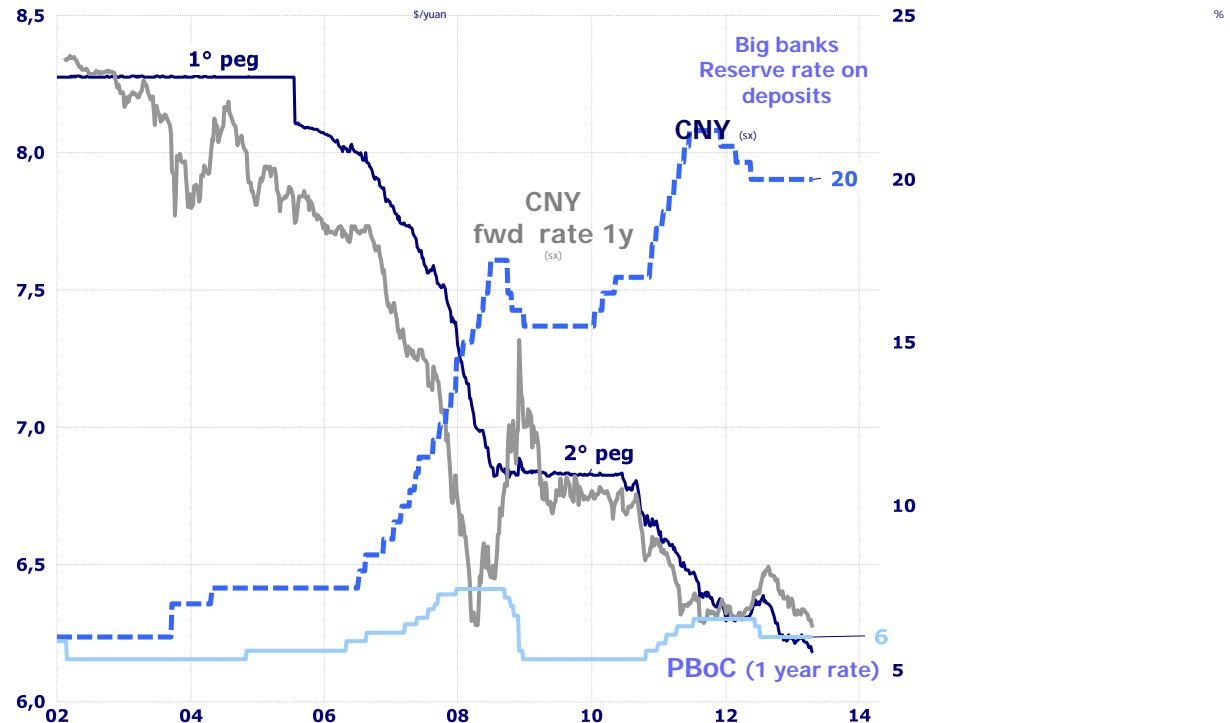
OFFICIAL REFERENCE RATES



MONETARY POLICY

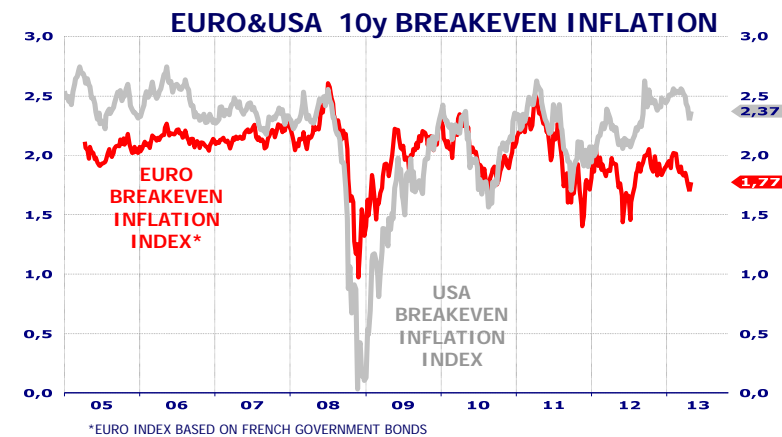
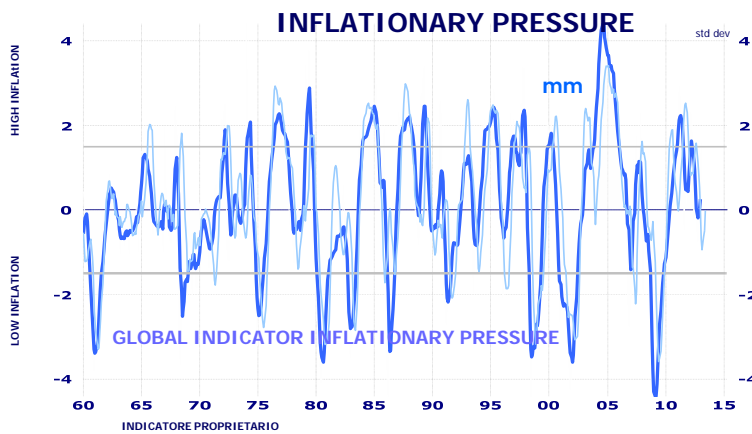
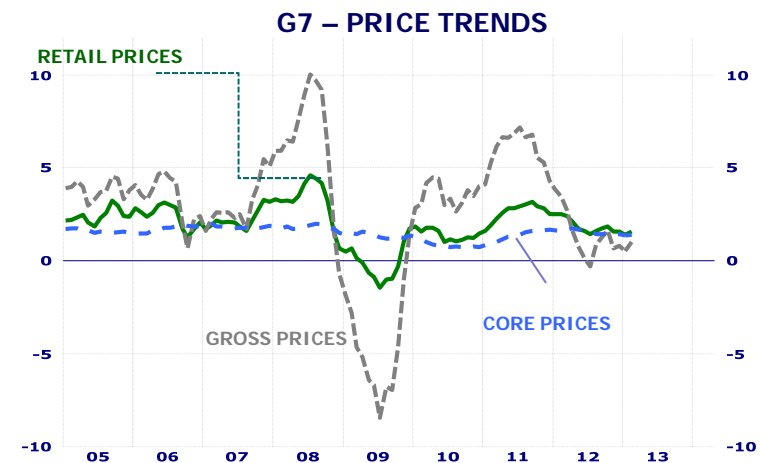
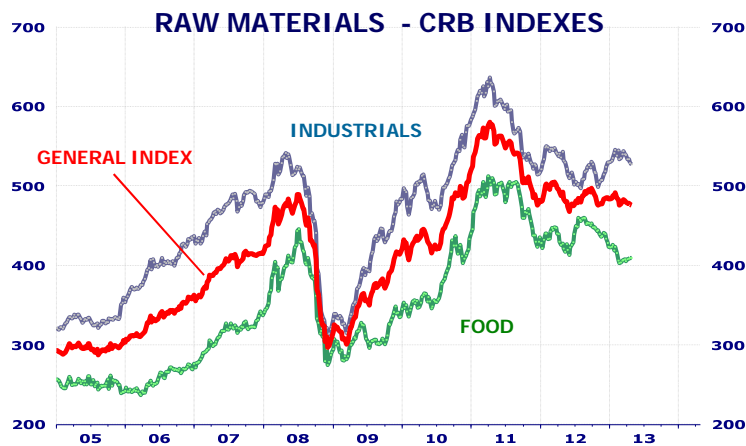
In early 2013, the Reserve Bank of India reduced the interest rate by 25 bp to 7.75% and the Central Bank of Turkey reduced its rate at 5%. In Brazil, the monetary authority increased the rate to 7.5% to contrast inflation, while the central banks of Korea and Australia also lowered their reference rates.

CHINA - INTEREST RATES AND EXCH. RATE



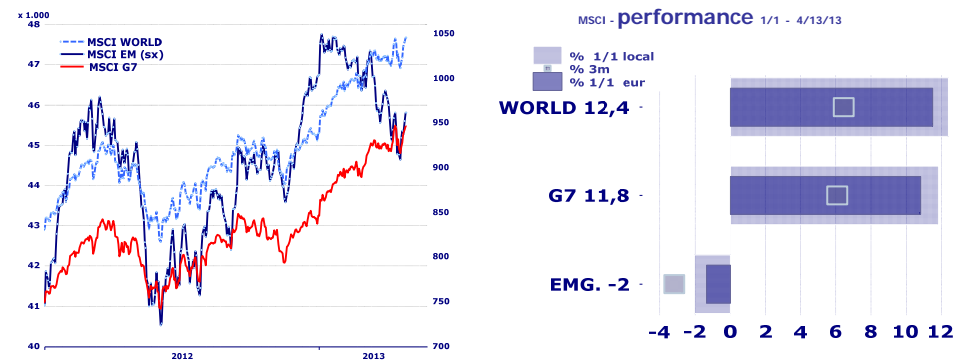
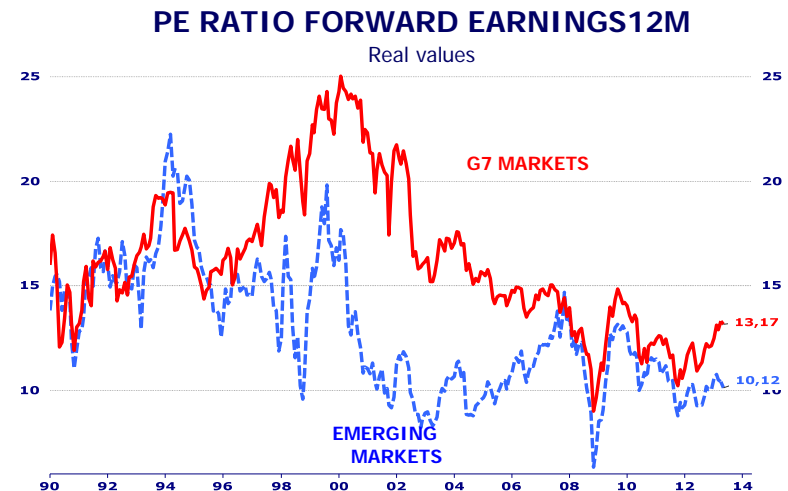
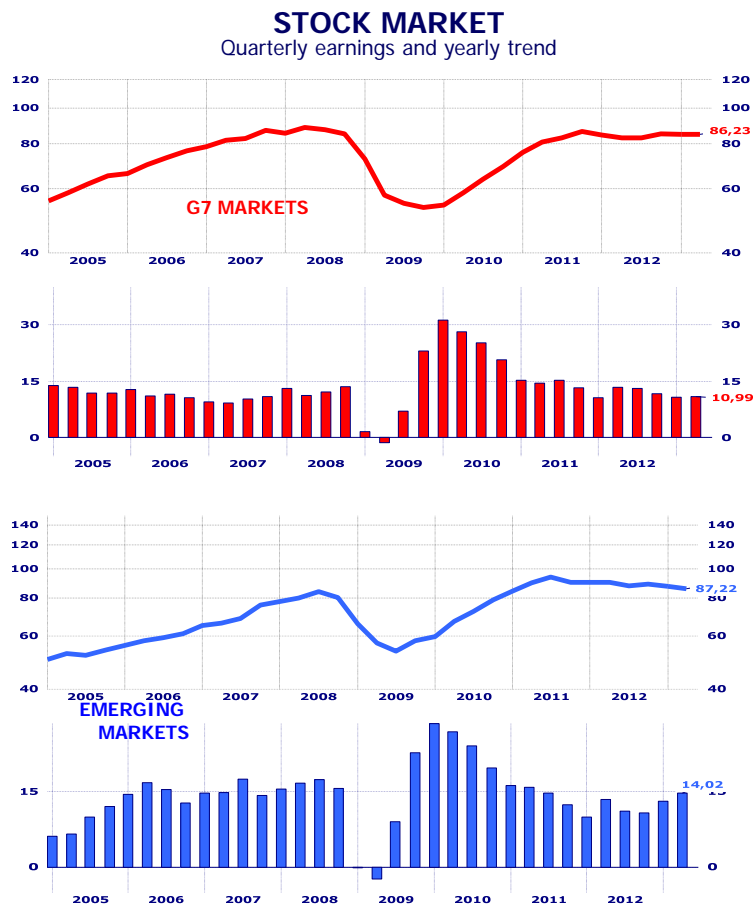
INFLATION

Among advanced economies the trend of gross industrial prices is slightly growing but the forecasts for a limited pressure on retail and core prices is confirmed. The indicator of general inflationary pressure has contained the bearish momentum, but there remains a downward trend.



MSCI WORLD - G7 - EMERGING MARKETS

The global stock market has improved since the beginning of the year, while the EM. MARKETS MSCI confirmed the negative trend. Quarterly earnings are growing by 11% for G7 countries and 14% for EM. The MSCI G7 index is about 13 times earnings, while the MSCI EM. MKTS is at about 10. For the coming weeks we expect an interim phase, with probable absorption of negative impulses that should start a new impulsive phase, probably more solid for emerging markets.



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