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PRESS RELEASE

Nordic Outlook: On the cusp of a global recession – sharp interest rate cuts in Europe

The ongoing credit crisis will continue to dominate the global economy, as tighter credit conditions and falling home prices hamper growth. Next year, growth in the OECD will be the lowest since the early 1990s. Looking ahead, emerging economies will also be affected to a greater degree by secondary effects from the slowdown in industrialised countries. Overall, the world economy will grow by 3 per cent in 2009, which is close to a recession at the global level. Inflation will gradually turn downward, and combined with ever weaker economic conditions this will open the door for interest rate cuts in Europe on a broad front in 2009.

The Swedish economy is now rapidly weakening. This year GDP growth will be 1.4 per cent and next year 0.9 per cent. Job growth will decelerate and unemployment will climb to 7.3 per cent in 2010. The labour market slowdown, combined with declining inflation next year, will enable the Riksbank to begin cutting its key interest rate in February 2009. By the end of next year, the repo rate will stand at 3.50 per cent. Sustained by strong finances, the government will implement fiscal stimulus measures of around SEK 40 billion in both 2009 and 2010. By 2010, public finances will have swung into a deficit of nearly 1½ per cent of GDP.

The American economy will decelerate once again as the positive impact of the federal stimulus package and foreign trade fades. Households are squeezed by tighter lending practices, further home price declines and continued labour market weakening. Lower energy prices will provide some relief, but the Federal Reserve's earlier interest rate cuts are only partly reaching consumers. GDP growth will be 1.6 per cent this year and 0.6 per cent in 2009. The Fed's key rate will remain at 2.0 per cent for another year.

Economic conditions in Western Europe are now in a steep decline. Euro zone growth will end up below 1 per cent next year. In the United Kingdom, the slump will be even deeper. High inflation will delay interest rate cuts by the European Central Bank until March 2009. By the end of next year, the ECB's refi rate will be 3.25 per cent. Significant regional differences in the euro zone are a complicating circumstance for monetary policymakers. Weak public finances and the restrictions imposed by the Stability Pact are also constraining fiscal stimulus measures in many countries.

The US dollar will continue to recover against the euro as economic weakening in Western Europe becomes ever clearer. Interest rate cuts in Europe next year will mean smaller short-term interest rate spreads, providing further support for the

dollar. Falling commodity prices will have the same effect. By the end of 2009, the EUR/USD rate will drop to 1.37. Bond yields will fall further, in the wake of weak growth and lower key interest rates.

The Swedish economy is weakening on a broad front as the international slowdown deepens. Growth will end up well below trend both this year and next; 2008-2010 will thus be Sweden's weakest three-year period since the 1990s economic crisis. The labour market slowdown is becoming ever more apparent, and next year there will be a clear upturn in unemployment. Inflation will soon peak but remain high in the coming year. Lower energy prices and progressively more subdued labour cost pressures will cause inflation to turn downward during 2009. Because of an increasingly listless economy and a gradual decrease in the inflation threat, the **Riksbank will begin cutting its key interest rate in February** next year, to 3.50 per cent by the end of 2009 and to 3.0 per cent a few months into 2010. The krona will mainly keep pace with the euro but will weaken against the dollar and thus also in trade-weighted terms.

Strong central government finances will open the way for sizeable fiscal stimulus measures during the next couple of years. We expect stimulus packages of around SEK 40 billion in both the 2009 budget and the budget for 2010, an election year. Due to the combined effect of these measures and weak economic performance, public finances will rapidly weaken and will reach a deficit equivalent to 1.3 per cent of GDP in 2010. The overall deterioration in public sector finances in 2007-2010 will thus total about 5 per cent of GDP.

Key figures, Swedish economy
Year-on-year percentage change

	2007	2008	2009	2010
GDP, adjusted for work days	2.9	1.4	0.9	1.8
Unemployment (%) (ILO definition)	6.2	6.2	7.0	7.3
CPI inflation	2.2	3.9	3.2	1.7
Public financial saving (% of GDP)	3.5	2.9	0.4	-1.3
Repo rate (December)	4.00	4.75	3.50	3.00
Exchange rate, EUR/SEK (December)	9.43	9.45	9.45	9.30

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For further information, please contact:

Robert Bergqvist, telephone +46 8 506 23016

Håkan Frisén, +46 8 763 80 67

Mattias Bruer, +46 8 763 85 07

Bo Enegren, +46 8 763 85 94

Mikael Johansson, +46 8 763 80 93

Tomas Lindström, +46 8 763 82 97

Press contact: Elisabeth Lennhede, +46 70 763 99 16, elisabeth.lennhede@seb.se