



RESEARCH SHOWS ONE IN THREE BANKING CRISES HAVE NO LASTING IMPACT ON GLOBAL ECONOMY: FIDELITY INTERNATIONAL

- According to IMF research, an economy has suffered a permanent loss of output of 10% seven years following an “average” banking crisis
- However, there is a very wide dispersion of possible outcomes with about one in three causing no lasting damage. There are reasons to believe this could be one of the happier outcomes.

London, 16 February 2010 - One-third of the 88 banking crises that have occurred across the world in the last four decades have had no negative long-term impact on the country’s economy and indications are that this crisis could also buck the consensus view that there will be permanent damage, says **Trevor Greetham, Director of Asset Allocation and Manager of Fidelity's Multi Asset Funds.**

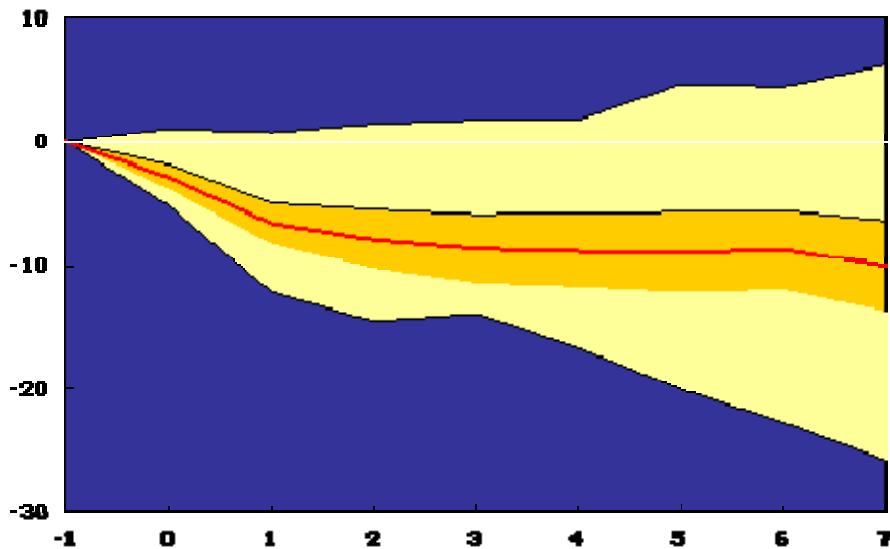
Speaking at the [Fidelity Investment Forum](#), which focused on the power of independent thinking, Greetham outlined why he believes the consensus view on the future of the global economy is overly pessimistic and why there will be a sustained and strong recovery.

According to IMF research, an economy has suffered a permanent loss of output of 10% seven years following an “average” banking crisis. However, in about one in three of the cases they studied there was no permanent damage with the economy often ending up in better shape than when the financial crisis started (see chart below).

Greetham believes it is likely policy makers will successfully steer the global economy away from permanent and lasting damage as a result of:

- Near zero interest rates and massive monetary injections to inflate asset prices
- The largest peace-time fiscal stimulus package in history with almost all countries contributing, especially China
- Early recognition of banking losses and forced recapitalisation of the banking system

Output Losses after Banking Crises (per capital GDP; percent deviation from pre-crisis trend)



Source: International Monetary Fund (IMF), Oct09. 66 Banking crises. Figure reports mean difference from pre-crisis trend (over $t=-10$ to $t=-3$; $t=-1$ normalized to 0; crisis begins at $t=0$). Inner shading indicates 90% confidence interval for the mean; outer shading indicates inter-quartile range.

He said: “We know that about one in three financial crises have no negative long-term impact. The question is whether the policy makers will be successful in avoiding a permanent loss of output this time around. There’s a good chance they will be.”

In the case of a positive outcome:

- Disinflationary growth can last longer
- Interest rates stay low for longer
- Taxes don’t rise as much as feared

Greetham said: “Things always look at their worst at the trough of an economic cycle. For example, by assuming there is a permanent loss of output, the UK Treasury turned a large cyclical budget deficit into a structural problem at the stroke of a pen. There is huge uncertainty around that assumption that is not widely appreciated.

“If there is no significant permanent loss of output, then there is a huge amount of spare capacity to use up before we need worry about a serious rise in inflation. We could see strong growth for years, good profits and, importantly, taxes may not need to



rise anything like as much as people currently fear because tax revenues will be strong again.”

Supporting his view that the economic recovery will be V-shaped, Greetham pointed to the fact that business confidence has recovered quickly, and is still rising, lead indicators for global trade are the most powerful they have been since the mid-1970s and firms are starting to boost depleted inventories resulting in a large upswing in manufacturing. However, he warned the future was not without risks.

He said: “The markets will have to absorb a likely peaking out in the rate of recovery in 2010 and we are also likely to see initial steps to tighten fiscal and monetary policy in a wide range of countries. This could result in some choppy waters for equity investors.

“Near term, we are also seeing a sharp rise in inflation. I see the strongest economic recovery in a generation and that will keep pushing commodities prices higher. However, looking to the second half of this year or early next year, I think it is unlikely we will have used up all the spare capacity we have in terms of high unemployment and empty factories. If you look at history, when you have had spare capacity, even when there is a recovery going on, inflation tends to drop.”

Greetham’s multi-asset funds are underweight government bonds, overweight commodities, stocks and property with a tilt towards the emerging markets and Asia, reflecting his view that the economy is currently in ‘overheat’ phase.

But he warned investors that the next few years will be fast moving and flexible tactical asset allocation or diversification across a wide range of asset classes will remain essential. He said: “There is so much volatility in the economic cycle at the moment. You can be certain 2010 will not be a dull year.”

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