

Manufacturing Barometer™

Business outlook report
Third quarter 2009

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Quarterly highlights

In the third quarter of 2009, PricewaterhouseCoopers interviewed 60 US-based industrial manufacturing executives about their current business performance, the state of the economy, and their expectations for business growth over the next 12 months. We then compared their responses with results from prior quarters to see how the panel's 12-month outlook has changed. The final step was to compare their views with a wider panel to show how the industry differs from the broader population.

Key findings:

- **Forecast turns fair.** Industrial products manufacturers surveyed forecast negative revenue growth in 2009, at minus 8.6 percent. However, a turnaround is expected over the next 12 months. Fifty-seven percent forecast positive revenue growth – with 12 percent estimating double-digit growth, and the remaining 45 percent anticipating single-digit growth. Still, 17 percent forecast zero growth, and another 17 percent expect negative revenue growth. A composite revenue growth rate of 2.2 percent is forecast for the next 12 months.
 - **International sales fuel momentum.** Panelists marketing abroad forecast an upturn in the contribution of international sales to total revenue over the next 12 months, up 4 points to 34 percent from the prior quarter's survey low of 30 percent.
 - **Optimism trumps pessimism.** Looking at the next 12 months, 48 percent of industrial manufacturers surveyed are optimistic about the US economy's prospects, and only 13 percent are pessimistic. A year ago, 66 percent were pessimistic. Similarly, 45 percent of panelists who market abroad are optimistic about prospects for the world economy, and only 13 percent are pessimistic. A year ago, 63 percent of this international segment was pessimistic.
 - **Workforce reductions abating.** Over the next 12 months, fewer respondents are planning net layoffs compared with the prior quarter, with planned composite reductions of minus 0.8 percent versus 2.2 percent in the prior quarter. Twenty-five percent plan to add workers, but 28 percent plan to reduce their number of full-time employees. Forty-seven percent will stay about the same.
 - **Spending will pick up, albeit conservatively.** More panelists are planning major new investments of capital over the next 12 months, up 10 points to 37 percent. But the level of projected spending dropped sharply from 6.2 percent to 3.9 percent of sales. Increased budgeting expenditures also rose sharply to 68 percent, with a focus on new product or service introductions, research and development, and business acquisitions. Plans for M&A activity also rose sharply to 38 percent, focused on intent to purchase another business.
 - **Legislation and taxation policies elicit concern.** Apprehension about market demand dipped 7 points to 75 percent but remained the chief barrier to growth over the next 12 months. Two other potential barriers rose sharply – legislative/regulatory pressures, climbing 16 points to 58 percent, and taxation policies, rising 10 points to 53 percent. Decreasing profitability fears dropped 8 points to 42 percent, but that number remains high.
 - **Gross margins shape up.** In third quarter 2009, 40 percent of panelists reported gross margins up and 25 percent down – a net 15 percent with higher margins. That figure is the first net positive this year among these panelists and a reversal of the prior quarter, when a net 22 percent reported lower margins. Costs and prices remained lower.
- A quarter-over-quarter comparison of key indicators shows the business outlook for the next 12 months and how the views of the panel have changed each quarter (see chart 1.1). On the next page, key highlights are discussed from a special section added to this quarter's survey. The pages that follow provide a detailed look at each question for the past five quarterly surveys.

Special topic: looking past the economic crisis

With all eyes watching for signs of a recovery we incorporated questions to learn what is on the minds of the panelists as they try to position themselves for a successful outcome.

- **Slow climb out of the recession.** Only 7 percent of panelists said they expect their organizations will begin to recover from the recession by the end of 2009. Sixty-eight percent said their business will not recover until 2010 – with 23 percent predicting it will happen in the first half and 45 percent in the second half of the year. This is consistent with the revenue forecast (see chart 4.1), where 57 percent project revenue growth by the third quarter of 2010. Despite the optimism shared by the majority, 17 percent still do not expect their businesses to begin growing again until 2011.
- **A strategy for the rebound.** As industrial products manufacturers prepare for recovery in 2010, they said it will be important to leverage: operational efficiency/cost reduction; supply chain management; and finances, working capital, and liquidity. Talent management also will be important.
- **Lessons learned.** In retrospect, based on what these senior executives have observed during the recession, they believe their companies should have focused more on: mergers and acquisitions, new product or service introductions, and research and development. This group of industrial manufacturing executives said more thorough planning in those areas would have allowed them to better cope with today's economic environment.

Key indicators for the business outlook

Chart 1.1 Key indicators for the business outlook

A quarter-over-quarter comparison of the survey's key indicators shows how the 12-month outlook has changed each quarter. The change column indicates the movement of opinion over the past two quarters.

Business outlook, next 12 months among industrial manufacturers	2008		2009			Change	Page
	3Q '08	4Q '08	1Q '09	2Q '09	3Q '09	2Q - 3Q '09	
Optimistic about US economy	6%	5%	16%	43%	48%	↑	7
Optimistic about world economy	7%	4%	12%	43%	45%	=	9
Expect positive revenue growth	54%	25%	34%	43%	57%	↑	19
Average growth rate expected	2.8%	-2.4%	-0.7%	-0.4%	2.2%	↑	19
Planning major new investments	34%	33%	24%	27%	37%	↑	23
New investments as a % of sales	6.1%	8.3%	5.4%	6.2%	3.9%	↓	23
Planning to hire	12%	10%	10%	17%	25%	↑	21
New workers as a % of workforce (net)	-4.0%	-3.2%	-1.8%	-2.2%	-0.8%	↑	21
Expected barriers to growth							
• Lack of demand	82%	85%	95%	82%	75%	↓	25
• Legislative/ Regulatory pressures	36%	37%	44%	42%	58%	↑	25
• Taxation policies	22%	30%	40%	43%	53%	↑	25
• Decreasing profitability	64%	62%	69%	50%	42%	↓	25
• Competition from foreign markets	34%	25%	39%	35%	38%	↑	25
• Monetary exchange rate	36%	38%	37%	23%	28%	↑	25
• Oil/energy prices	62%	25%	21%	28%	25%	↓	25
• Capital constraints	26%	37%	44%	40%	22%	↓	25
• Higher interest rates	30%	13%	15%	12%	12%	=	25
• Pressure for increased wages	20%	10%	7%	3%	10%	↑	25
• Lack of qualified workers	26%	3%	7%	3%	8%	↑	25

Economic views

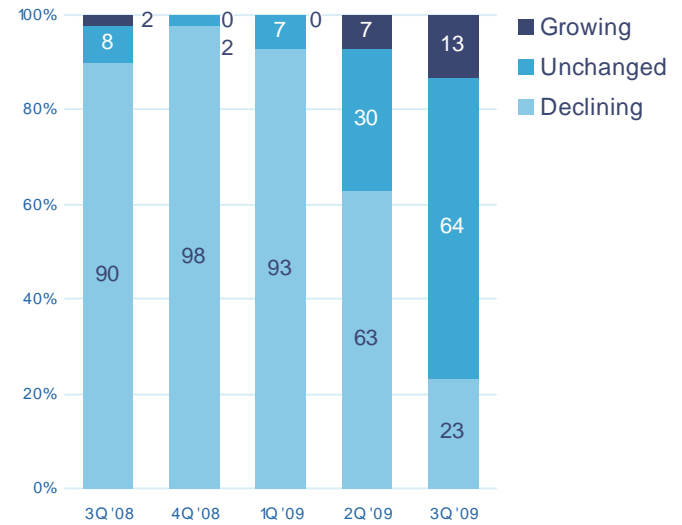
View of the US economy, this quarter

Which best describes your view of the US economy this quarter?

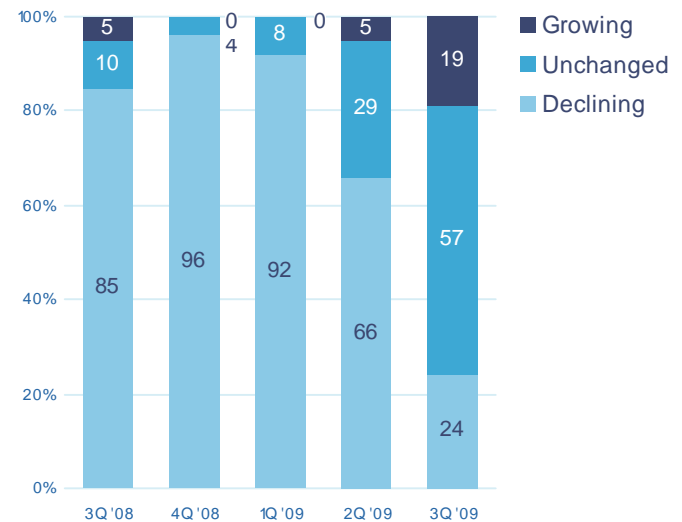
For the previous four quarters, an overwhelming majority of respondents viewed the economy as declining. However, in third quarter 2009, only 23 percent of panelists believed the US economy declined, down 40 points from last quarter's 63 percent. Showing a hint of optimism, 13 percent said they believe it grew, but 64 percent said they believe it did not change.

Chart 2.1 View of the US economy, this quarter

Industrial manufacturers



All respondents



Note: In 3Q 2009 Industrial manufacturers n=60, All respondents, n=110

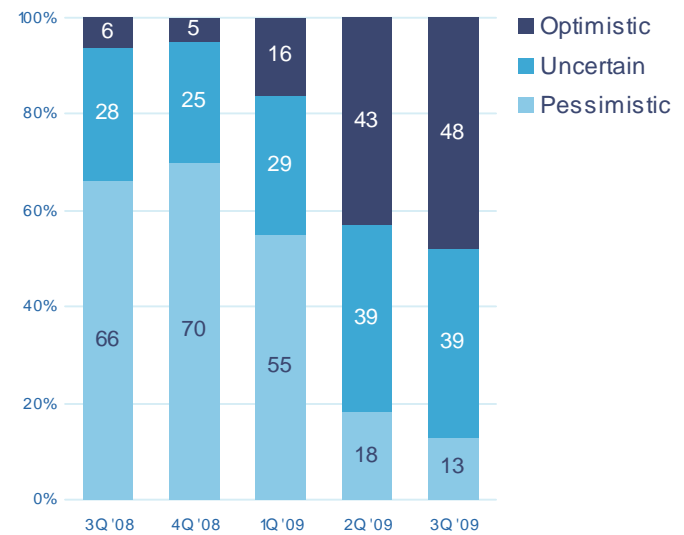
View of the US economy, next 12 months

Looking at the next 12 months, how do you feel about the prospects for the US economy?

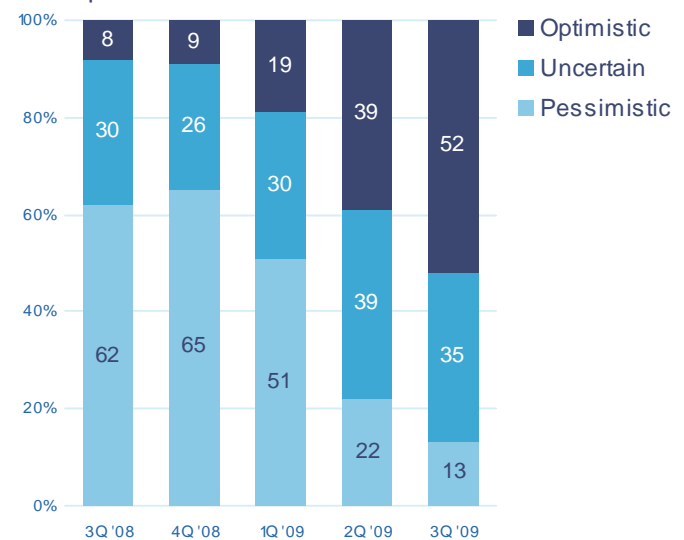
Looking ahead, 48 percent of respondents expressed optimism about the 12-month outlook for the US economy, ahead of the prior quarter's 43 percent and well ahead of last year's dismal 6 percent. Only 13 percent remain pessimistic, and 39 percent are uncertain.

Chart 2.2 View of the US economy, next 12 months

Industrial manufacturers



All respondents



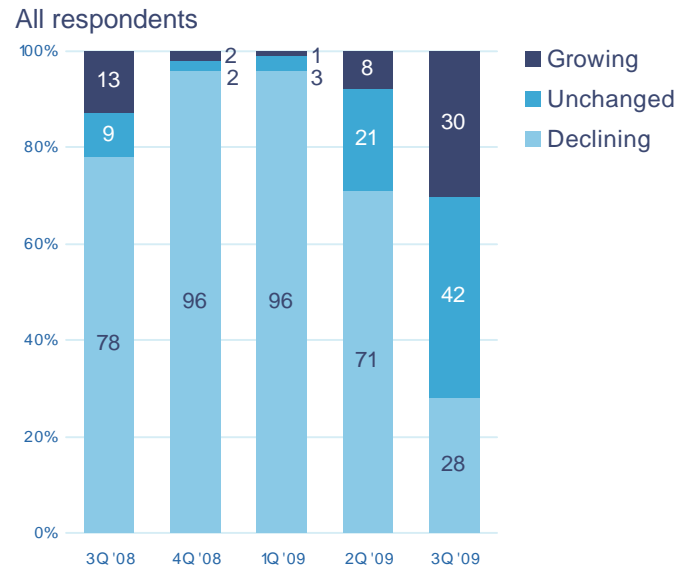
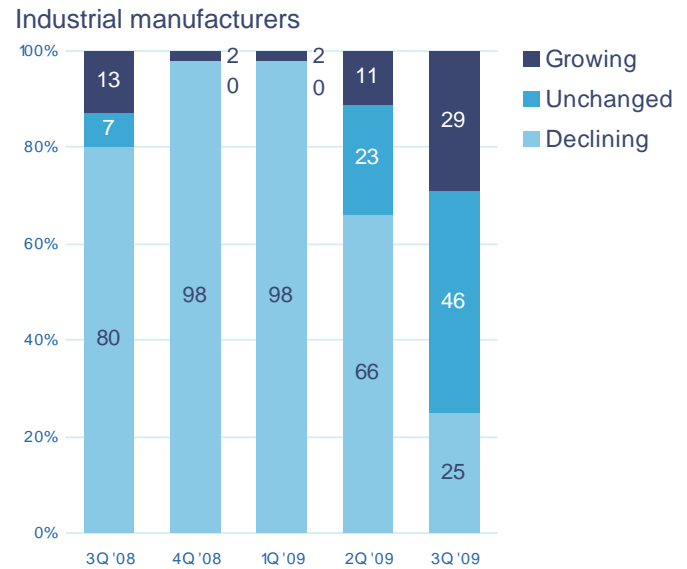
Note: In 3Q 2009 Industrial manufacturers n=60, All respondents, n=110

View of the world economy, this quarter

Which best describes your view of the world economy this quarter? (international marketers only)

In a turnabout, only 25 percent of panelists continued to view the world economy as declining in the third quarter, down 41 points from the prior quarter. On the positive side, 29 percent view it as growing, and 46 percent see it as unchanged.

Chart 2.3 View of the world economy, this quarter



Note: In 3Q 2009 those marketing abroad, Industrial manufacturers n=56, All respondents, n=98

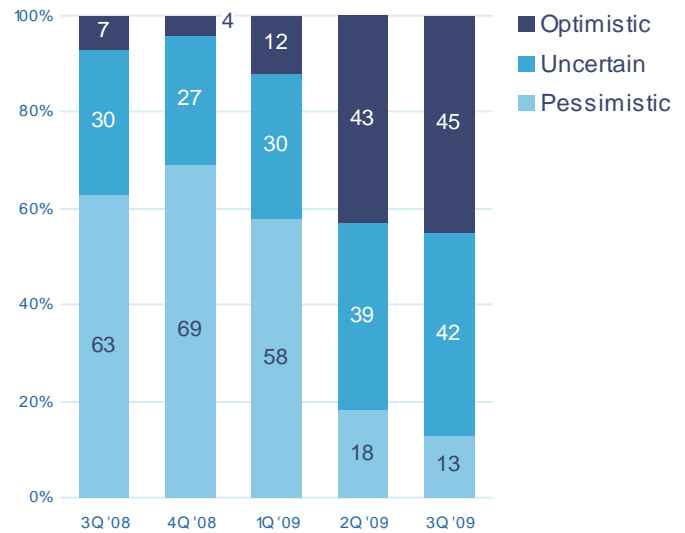
View of the world economy, next 12 months

Looking at the next 12 months, how do you feel about the prospects for the world economy? (international marketers only)

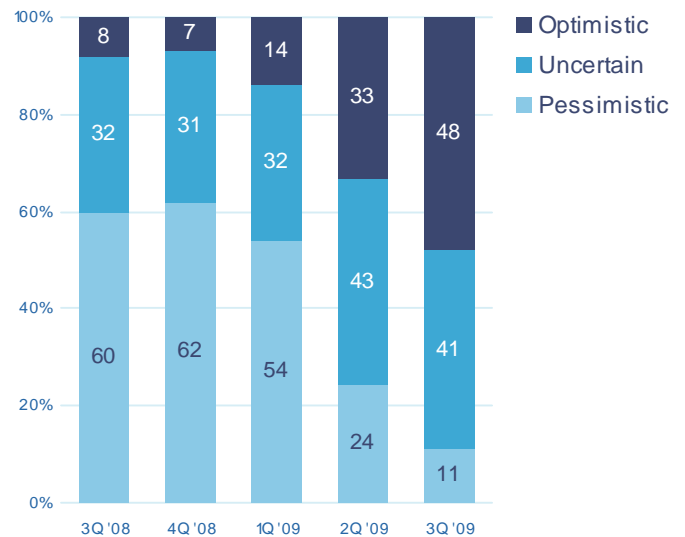
Of US-based industrial manufacturers who market abroad, 45 percent are optimistic about the prospects for the world economy over the next 12 months – up from 43 percent last quarter. Forty-two percent are uncertain, and only 13 percent said they are pessimistic.

Chart 2.4 View of the world economy, next 12 months

Industrial manufacturers



All respondents



Note: In 3Q 2009 those marketing abroad, Industrial manufacturers n=56, All respondents, n=98

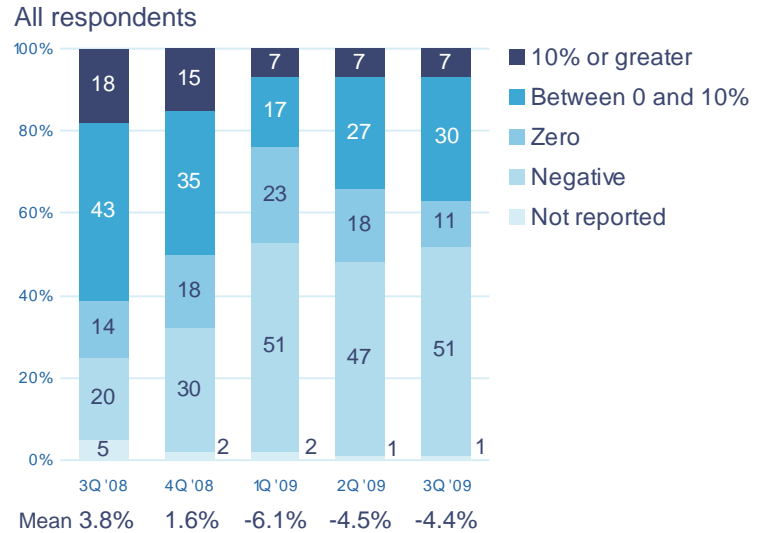
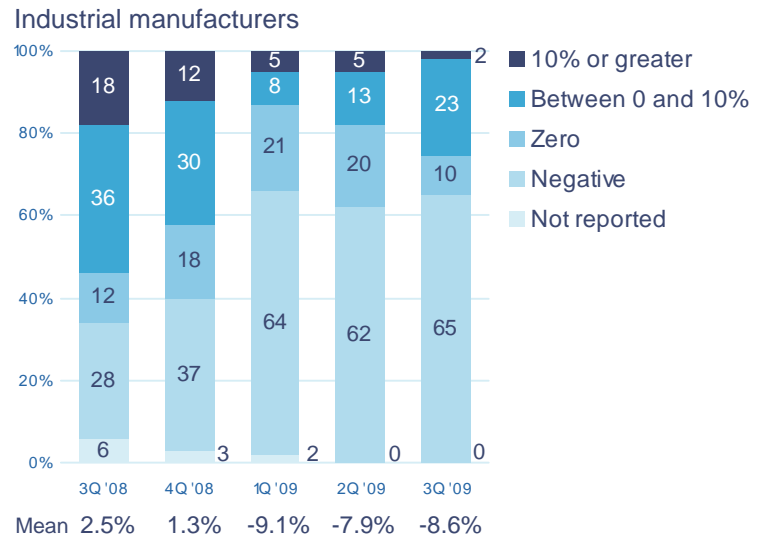
Company performance

Company revenue growth, calendar year

What is your company's estimated revenue growth rate for the calendar year?

In the third quarter, only 25 percent of US-based industrial manufacturers surveyed expect positive growth in 2009, with 2 percent forecasting double-digit growth and 23 percent forecasting single-digit growth. Overall, the composite average growth estimate dipped slightly from minus 7.9 percent in the prior quarter to minus 8.6 percent.

Chart 3.1 Company revenue growth, calendar year



Note: In 3Q 2009 Industrial manufacturers n=60, All respondents, n=110

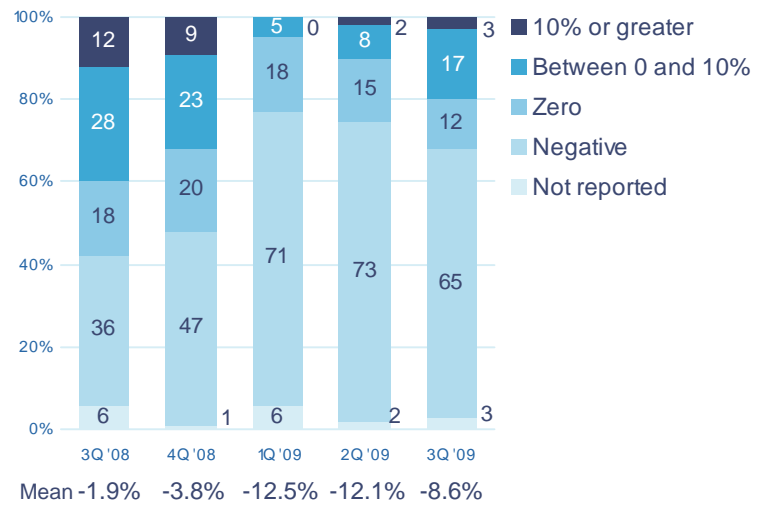
Industry growth, calendar year

What is your industry's estimated growth rate for the calendar year?

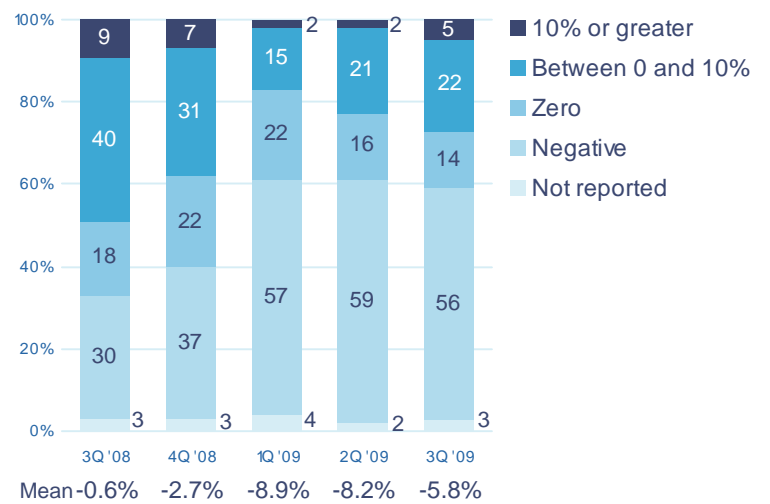
Industry growth for the calendar year improved over the prior quarter but is expected to remain low for 2009, at an average minus 8.6 percent. Sixty-five percent of panelists expect negative industry growth in 2009. Only 20 percent expect to be on the positive side, with 12 percent expecting zero growth.

Chart 3.2 Industry growth, calendar year

Industrial manufacturers



All respondents



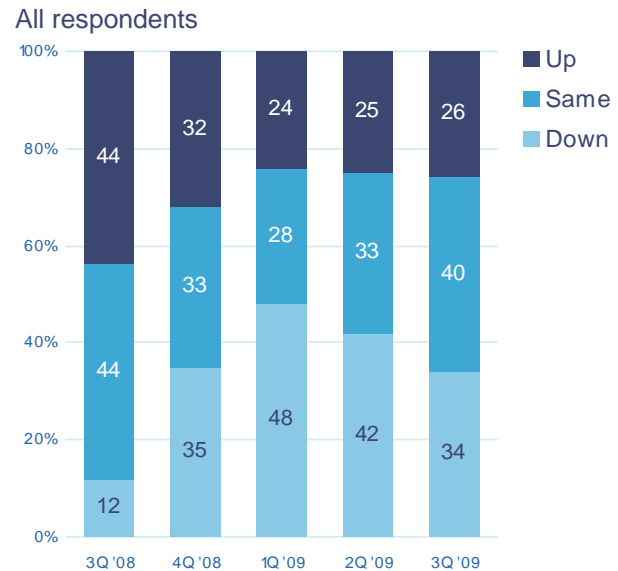
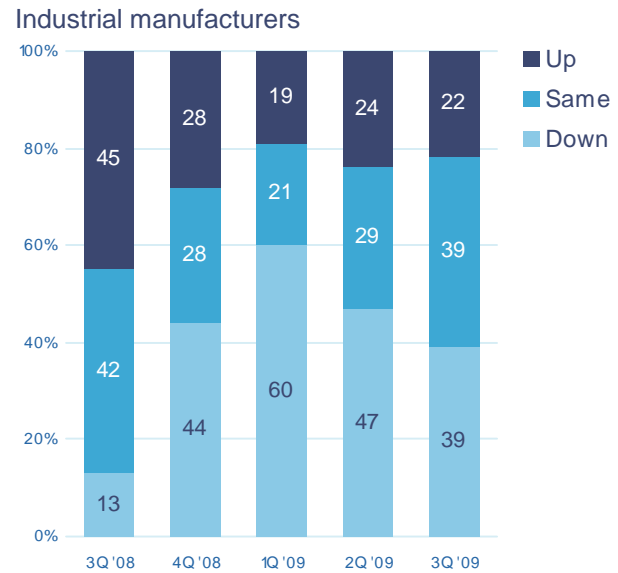
Note: In 3Q 2009 Industrial manufacturers n=60, All respondents, n=110

International sales

Are international sales up, down, or the same compared with three months ago?

For US-based industrial manufacturers that sell abroad, international markets showed a slight improvement in third quarter 2009. However, the 22 percent that reported an increase in sales abroad represent a low number compared with last year's 45 percent. The number reporting a decrease fell to 39 percent from 47 percent in the prior quarter.

Chart 3.3 International sales



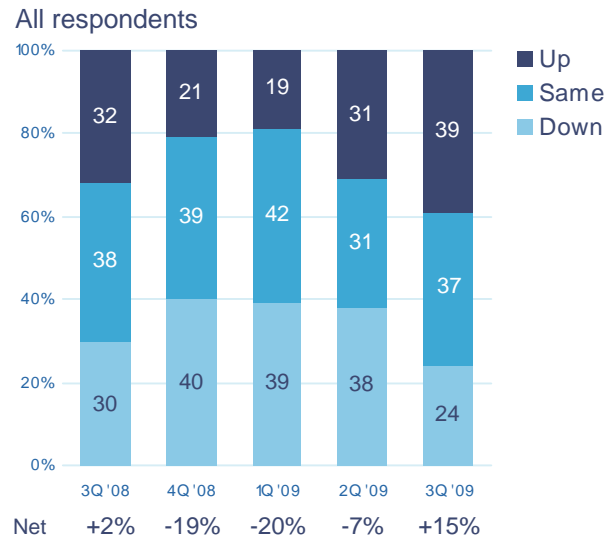
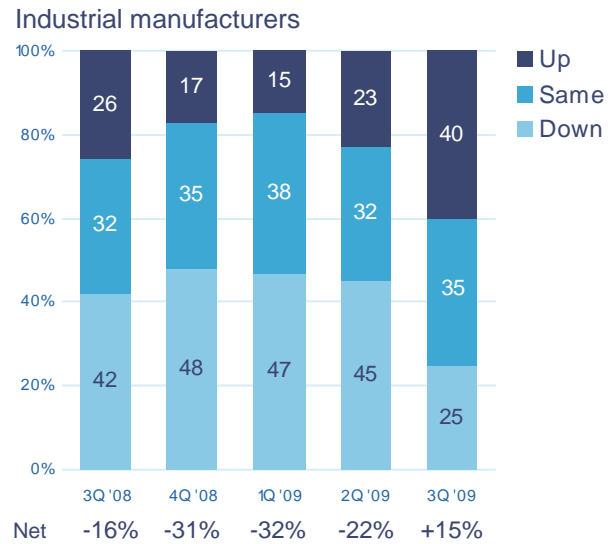
Note: In 3Q 2009 those marketing abroad, Industrial manufacturers n=56, All respondents, n=98

Changes in gross margins

Are gross margins up, down, or the same compared with three months ago?

In third quarter 2009, gross margins were higher for 40 percent of panelists and lower for 25 percent, for a net plus 15 percent. This is the first positive net change since fourth quarter 2007.

Chart 3.4 Changes in gross margins



Note: In 3Q 2009 Industrial manufacturers n=60, All respondents, n=110

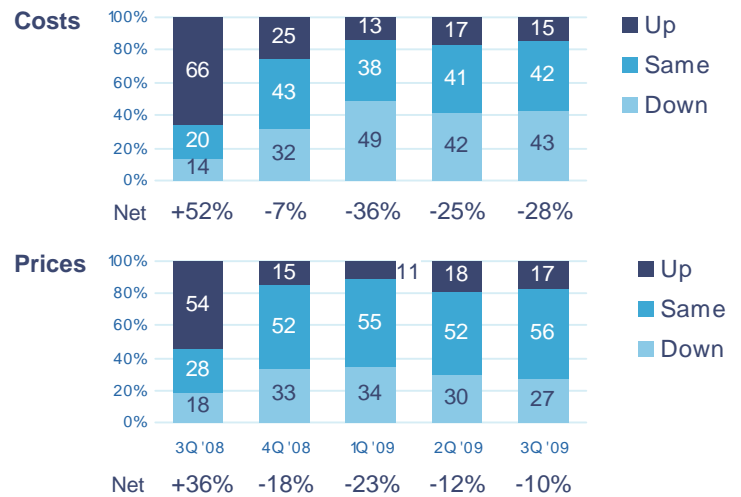
Changes in costs and prices

Are costs up, down, or the same compared with three months ago? Prices?

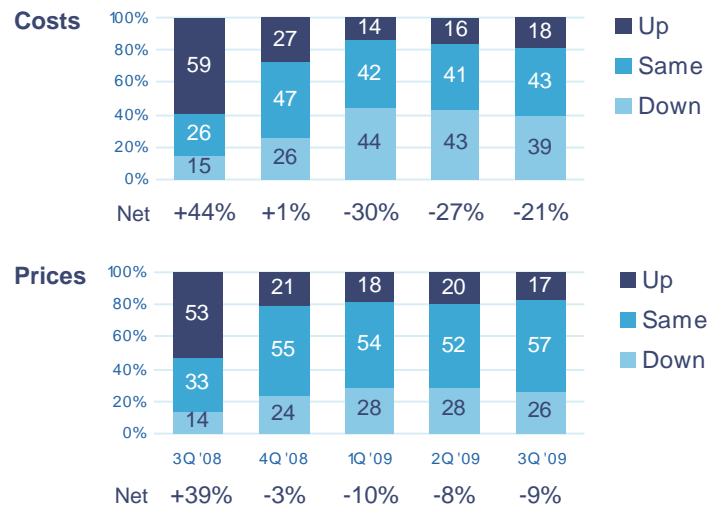
In third quarter 2009, costs and prices continued to show a net decrease. Only 15 percent of US-based industrial manufacturers reported higher costs, and 43 percent reported lower costs – for a net minus 28 percent. On the pricing side, only 17 percent raised prices, and 27 percent lowered them, for a net minus 10 percent.

Chart 3.5 Changes in costs and prices

Industrial manufacturers



All respondents



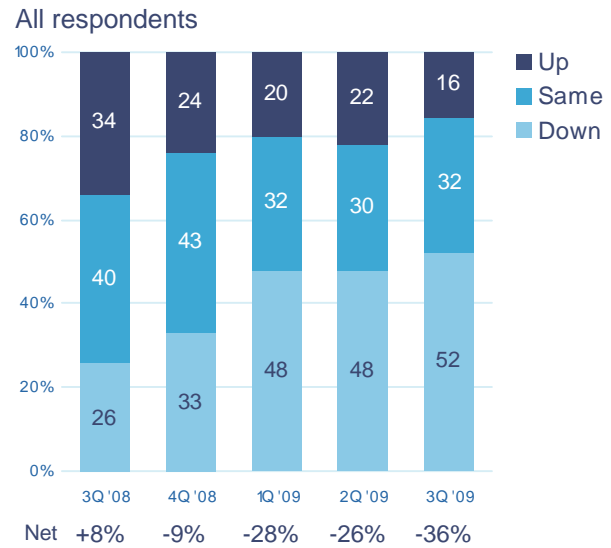
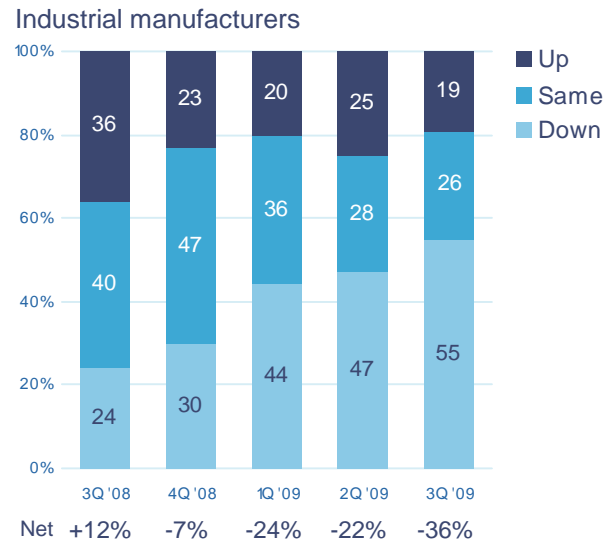
Note: In 3Q 2009 Industrial manufacturers n=60, All respondents, n=110

Inventory movement

Are finished inventories as a percent of sales up, down, or the same compared with three months ago? (product companies only)

Inventory is down for 55 percent of US-based industrial manufacturers and up for only 19 percent, for a net minus 36 percent.

Chart 3.6 Inventory movement



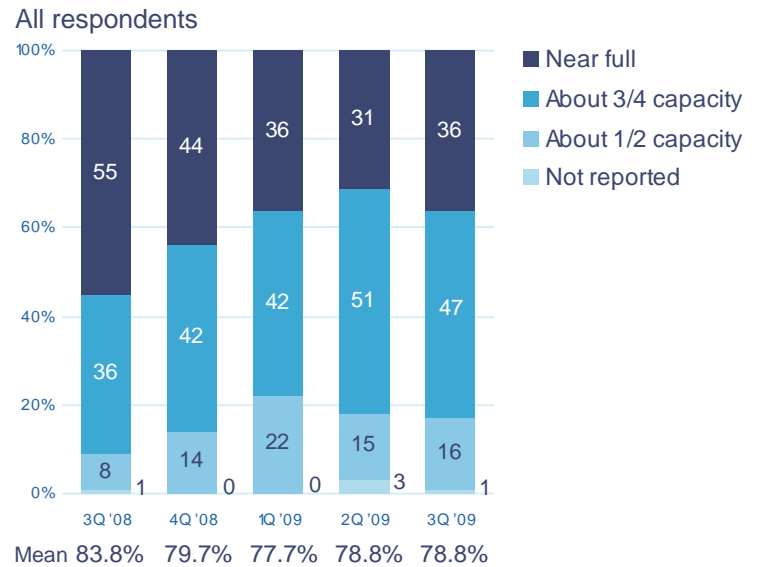
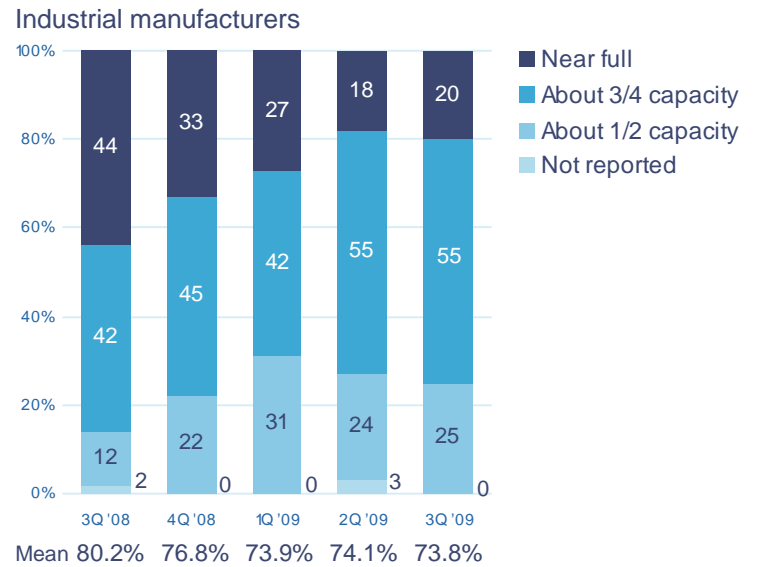
Note: In 3Q 2009 Industrial manufacturers n=60, All respondents, n=110

Level of operating capacity

What is your organization's current operating capacity?

Operating capacity is an estimate of the current level of permanent staffing compared with what is needed for full-capacity output. In third quarter 2009, the average level of operating capacity for US-based industrial manufacturers remained low, at an estimated 73.8 percent. A year ago, operating capacity was at 80.2 percent. This quarter, only 20 percent of industrial manufacturers claimed to be at or near capacity.

Chart 3.7 Level of operating capacity



Note: In 3Q 2009 Industrial manufacturers n=60, All respondents, n=110

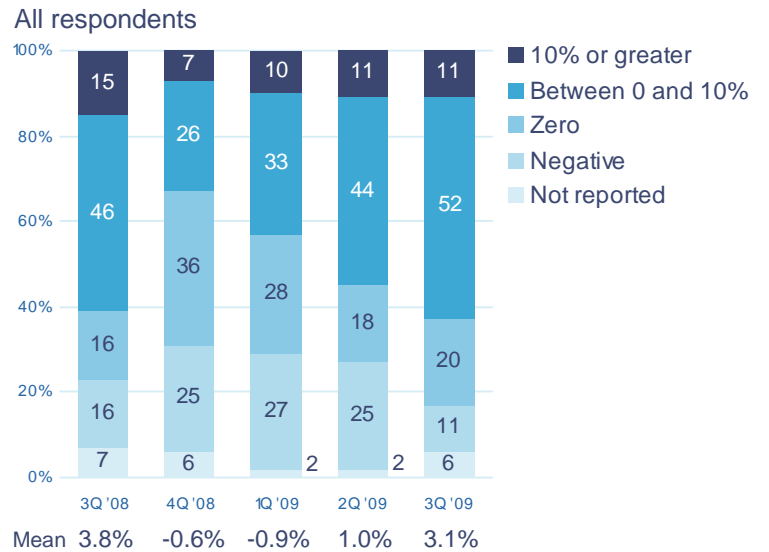
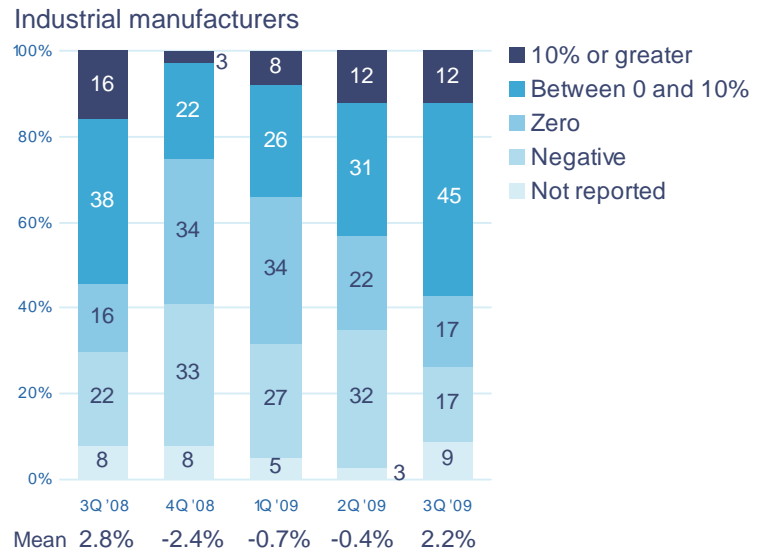
Business outlook, next 12 months

Revenue growth, next 12 months

What is your organization's estimated revenue growth rate for the next 12 months?

Looking ahead at the next 12 months, 57 percent of panelists expect positive growth – with 12 percent forecasting double-digit growth, and 45 percent forecasting single-digit growth. The projected average growth rate is a plus 2.2 percent, notably better than the prior quarter's projected minus 0.4 percent.

Chart 4.1 Revenue growth, next 12 months



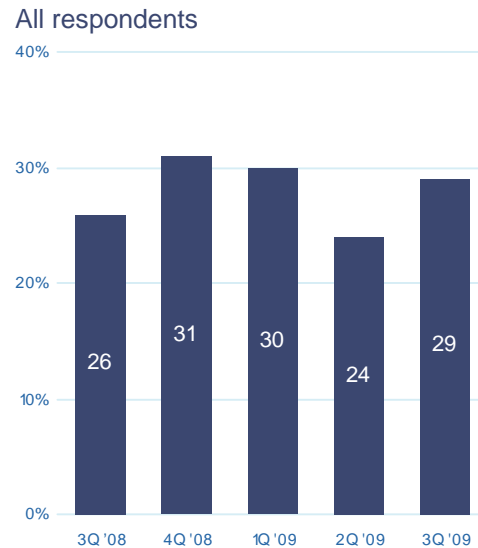
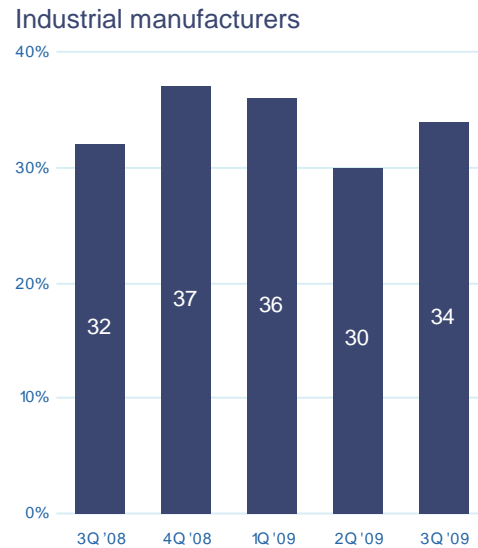
Note: In 3Q 2009 Industrial manufacturers n=60, All respondents, n=110

International sales, next 12 months

What percent of your business's total revenue over the next 12 months do you expect to be derived from international sales?

Of respondents selling abroad, the projected contribution of international sales to total revenue is 34 percent over the next 12 months, up from the prior quarter's 30 percent and in line with last year's 32 percent. International industrial products marketers still expect to draw a solid share of their revenue from world markets, ahead of the all-industry consensus.

Chart 4.2 International sales, next 12 months



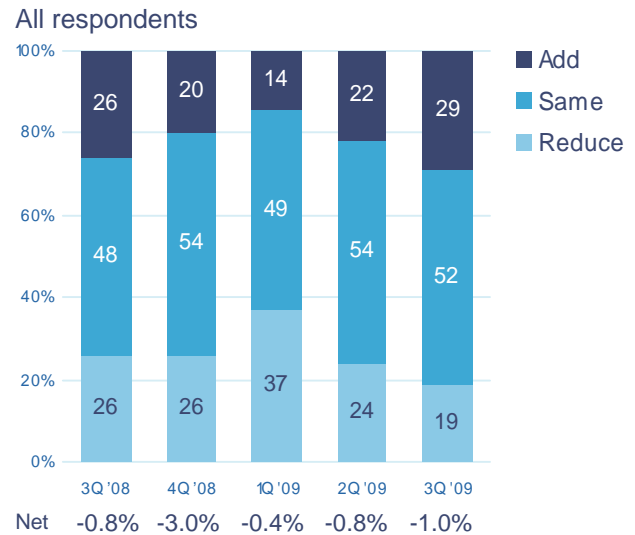
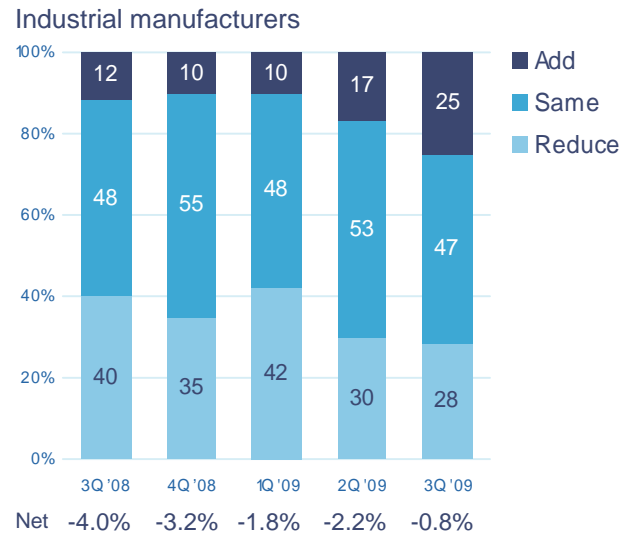
Note: In 3Q 2009 those marketing abroad, Industrial manufacturers n=56, All respondents, n=98

Percent planning to hire

Do you plan to add or reduce the number of full-time equivalent employees over the next 12 months?

Twenty-five percent of respondents plan to add employees to their workforces over the next 12 months, and 28 percent plan to reduce the number of full-time equivalent employees. The net workforce projection remains negative, at minus 0.8 percent but is an improvement over last quarter's minus 2.2 percent.

Chart 4.3 Percent planning to hire



Note: In 3Q 2009 Industrial manufacturers n=60, All respondents, n=110

Percent planning to hire by type of employee

What types of employees do you plan to add or reduce over the next 12 months?

Of the 25 percent of respondents planning to hire within the next 12 months, the most sought-after employees will be professionals/technicians, white collar workers, and sales/marketing people.

Chart 4.4 Percent planning to hire by type of employee

Industrial manufacturers

	3Q '08	4Q '08	1Q '09	2Q '09	3Q '09
Planning to hire (net)	12%	10%	10%	17%	25%
• Professionals/technicians	6%	5%	7%	7%	15%
• White collar support	2%	3%	---	---	12%
• Sales/marketing	4%	2%	3%	3%	10%
• Skilled labor	4%	3%	---	8%	8%
• Production workers	2%	2%	2%	5%	8%

All respondents

	3Q '08	4Q '08	1Q '09	2Q '09	3Q '09
Planning to hire (net)	26%	20%	14%	22%	29%
• Professionals/technicians	18%	11%	10%	11%	20%
• White collar support	10%	8%	2%	4%	11%
• Sales/marketing	11%	6%	5%	6%	14%
• Skilled labor	8%	5%	3%	8%	9%
• Production workers	6%	6%	4%	6%	11%

Note: In 3Q 2009 Industrial manufacturers n=60,
All respondents, n=110

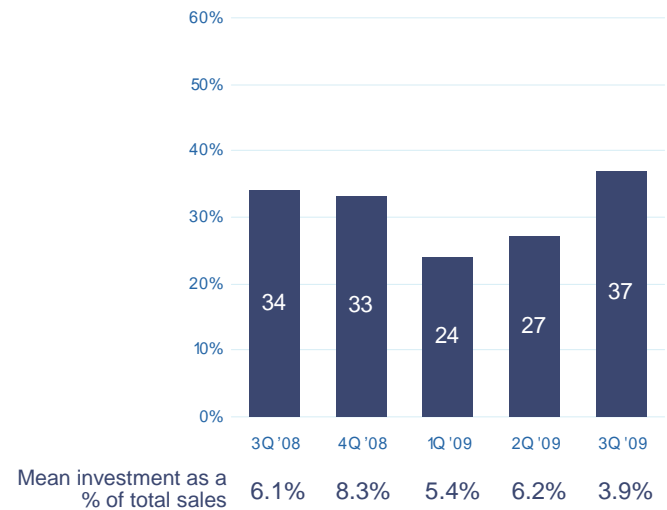
Percent planning major new investments of capital

Are you actively planning any major new investments of capital over the next 12 months? If so, what percent of total sales do you expect to invest?

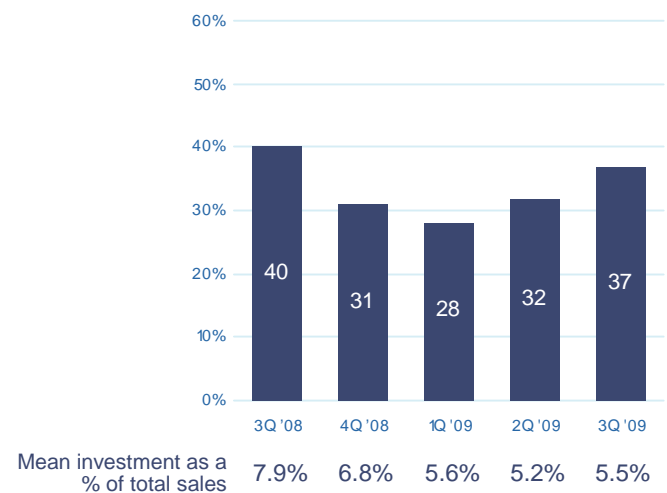
More US-based industrial products manufacturers interviewed are planning new capital investments, but at a lower rate of investment. Thirty-seven percent plan major new investments of capital during the next 12 months, compared with 27 percent last quarter and 34 percent last year. However, the mean investment as a percentage of total sales dropped to 3.9 percent from 6.2 percent last quarter and 6.1 percent a year ago.

Chart 4.5 Percent planning major new investments of capital

Industrial manufacturers



All respondents



Note: In 3Q 2009 Industrial manufacturers n=60, All respondents, n=110

Percent planning to increase operational spending

Over the next 12 months, where do you expect to increase spending?

Looking at the next 12 months, 68 percent of respondents plan to increase operational spending, well above last quarter's 53 percent. Among increased expenditures, new product or service introductions lead the way, followed by research and development, and business acquisitions.

Chart 4.6 Percent planning to increase operational spending

Industrial manufacturers					
	3Q '08	4Q '08	1Q '09	2Q '09	3Q '09
Percent planning to increase spending (net)	64%	57%	53%	53%	68%
• New product or service introduction	26%	23%	29%	30%	40%
• Research and development	24%	15%	15%	18%	35%
• Business acquisition	26%	18%	8%	18%	33%
• Geographic expansion	20%	30%	13%	17%	22%
• Facilities expansion	20%	18%	11%	8%	18%
• Information technology	24%	28%	13%	12%	17%
• Marketing & sales promotion	14%	7%	5%	10%	7%
• Advertising	12%	2%	3%	7%	3%
• Internet commerce	12%	3%	3%	2%	3%
All respondents					
	3Q '08	4Q '08	1Q '09	2Q '09	3Q '09
Percent planning to increase spending (net)	69%	58%	58%	56%	67%
• New product or service introduction	30%	21%	33%	29%	34%
• Research and development	17%	15%	14%	16%	29%
• Business acquisition	25%	22%	11%	24%	29%
• Geographic expansion	23%	28%	16%	22%	24%
• Facilities expansion	24%	20%	12%	16%	17%
• Information technology	29%	33%	18%	17%	27%
• Marketing & sales promotion	18%	14%	13%	17%	15%
• Advertising	15%	10%	10%	12%	14%
• Internet commerce	13%	7%	7%	7%	8%

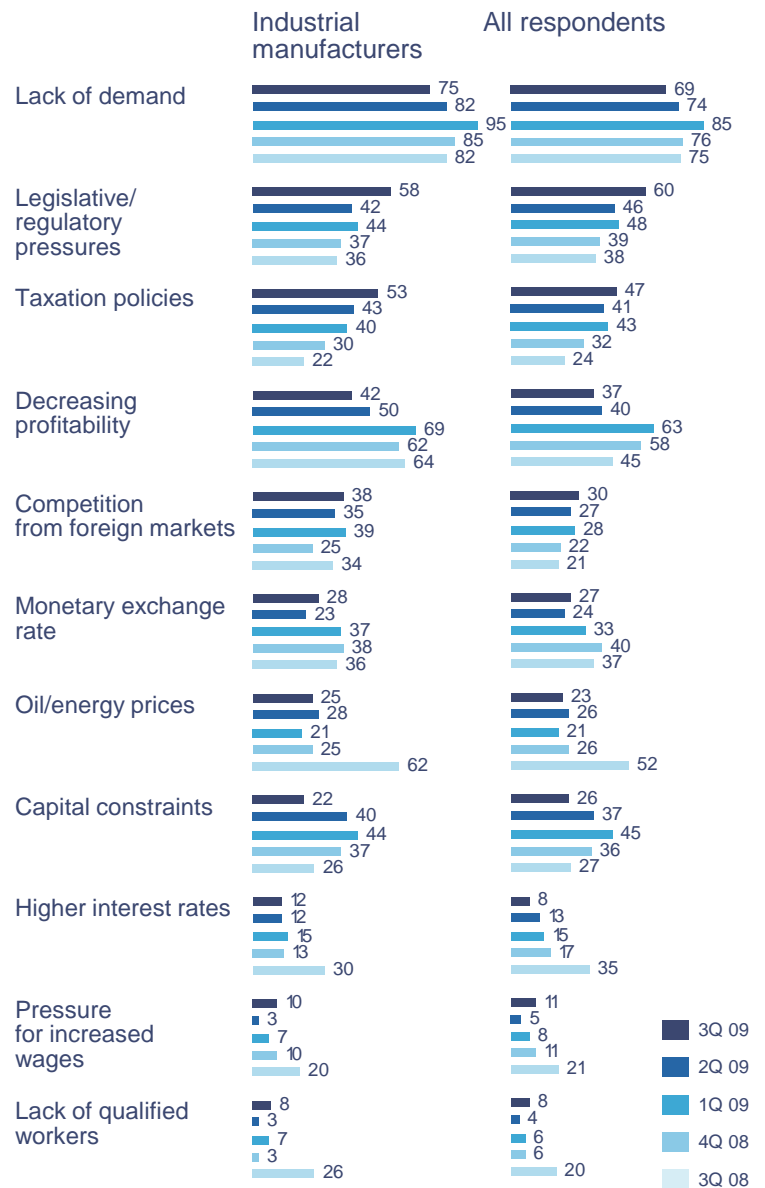
Note: In 3Q 2009 Industrial manufacturers n=60, All respondents, n=110

Expected barriers to business growth

Over the next 12 months, will any of the following represent barriers to business growth?

Concern about lack of demand is lower but still the chief barrier concerning respondents, cited by 75 percent. Concerns about legislative/regulatory pressures rose 16 points to 58 percent, along with taxation policies, which climbed 10 points to 53 percent. Decreasing profitability dipped 8 points but remains high, at 42 percent. On the positive side, concern about capital constraints as a potential barrier to growth over the next 12 months dropped sharply to 22 percent.

Chart 4.7 Expected barriers to business growth



Note: In 3Q 2009 Industrial manufacturers n=60, All respondents, n=110

Plans for M&A and other business initiatives

Over the next 12 months, do you expect to participate in any of the following new business initiatives?

Plans for M&A activity during the next 12 months among US-based industrial manufacturers rose from 28 percent in the previous quarter to 38 percent in the third quarter. This was primarily driven by an interest in purchasing another business, which jumped from 25 percent to 37 percent. New strategic alliances remained high, rising to 33 percent. But plans to expand to new markets abroad sank 12 points to 15 percent.

Chart 4.8 Plans for M&A and other business initiatives

Industrial manufacturers

	3Q '08	4Q '08	1Q '09	2Q '09	3Q '09
New business initiatives (net)	70%	60%	55%	52%	70%
• M&A activity (net)	32%	32%	15%	28%	38%
- Purchase another business	28%	25%	10%	25%	37%
- Sale part/all own business	2%	8%	7%	5%	5%
- Equity carve-out/spin-off	4%	3%	2%	3%	2%
• New strategic alliance	32%	30%	27%	30%	33%
• New joint venture	28%	25%	20%	23%	22%
• Expand to new markets abroad	32%	32%	18%	27%	15%
• New facilities abroad	20%	20%	13%	13%	15%
• Close/reduce facilities abroad	10%	13%	19%	10%	15%
• Reduce activity in markets abroad	16%	15%	16%	13%	12%

All respondents

	3Q '08	4Q '08	1Q '09	2Q '09	3Q '09
New business initiatives (net)	63%	60%	58%	54%	63%
• M&A activity (net)	32%	33%	21%	32%	36%
- Purchase another business	27%	27%	16%	30%	34%
- Sale part/all own business	5%	9%	4%	7%	6%
- Equity carve-out/spin-off	5%	5%	3%	5%	3%
• New strategic alliance	30%	27%	25%	31%	33%
• New joint venture	26%	25%	20%	24%	21%
• Expand to new markets abroad	26%	30%	18%	28%	18%
• New facilities abroad	13%	16%	13%	11%	11%
• Close/reduce facilities abroad	5%	9%	16%	6%	9%
• Reduce activity in markets abroad	12%	12%	15%	13%	12%

Note: In 3Q 2009 Industrial manufacturers n=60.

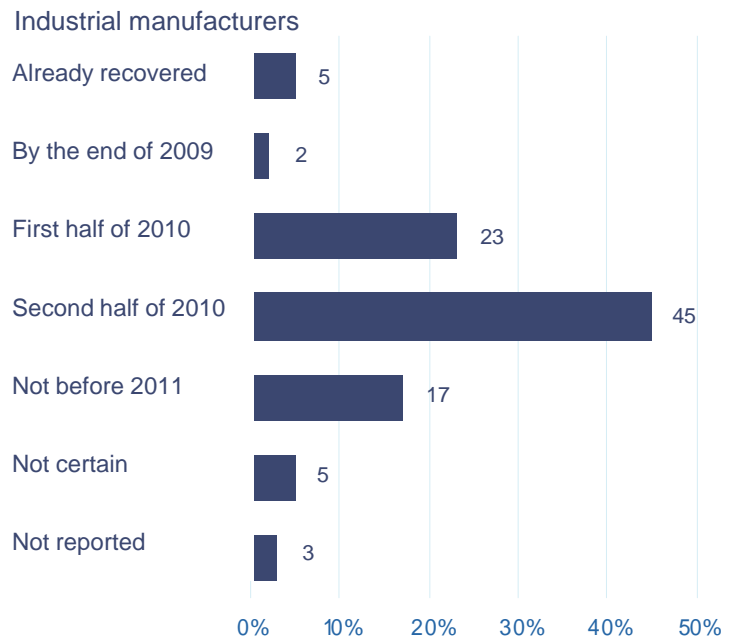
Special topic: looking past the economic crisis

Expectations for economic recovery

When do you expect your own business to recover?

While many economic forecasters predicted a recovery (a stabilization of the US economy) during fourth quarter 2009, most senior executives of industrial products manufacturing companies expect their own organization to regain strength later. Twenty-three percent of panelists expect to see growth pick up in the first half of 2010, and 45 percent say it will likely not happen until the latter half of the year. Only 5 percent believe their organizations have already recovered, and 2 percent say theirs will do so by the end of 2009. Finally, 17 percent believe their organizations are unlikely to recover until 2011.

Chart 5.1 Expectations for recovery



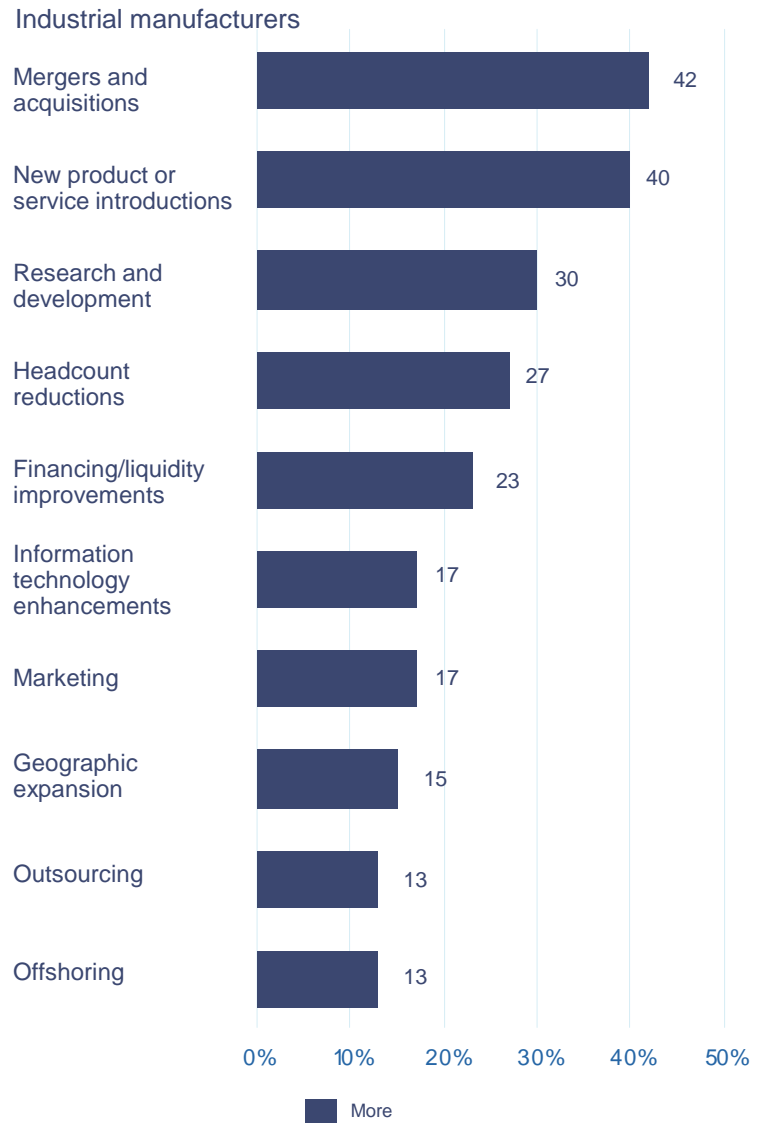
Note: In 3Q 2009 Industrial manufacturers n=60.

Business focus before the economic downturn

To better cope with today's economic environment, do you think your company should have focused more, less, or about the same on the following?

Based on what senior executives of industrial products manufacturers have learned during the recession, 42 percent believe their companies should have focused more on mergers and acquisitions, 40 percent say the focus belonged on new products and services, and 30 percent believe they would have been wise to devote more attention to research and development.

Chart 5.2 Business focus before the economic downturn



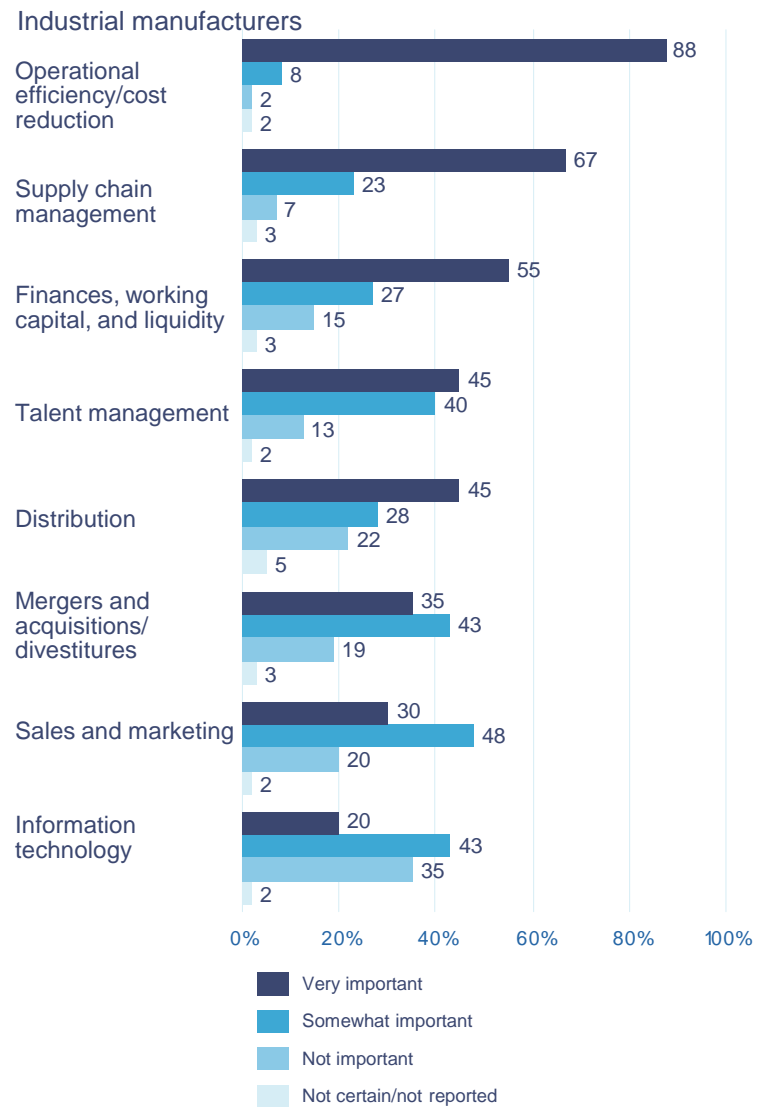
Note: In 3Q 2009 Industrial manufacturers n=60.

Business focus to prepare for recovery

How important is it to leverage the following areas as your company prepares for recovery?

Respondents identified three critical areas to leverage as their companies prepare for recovery: operational efficiency/cost reduction; supply chain management; and finances, working capital, and liquidity. Talent management and distribution ranked high as well.

Chart 5.3 Business focus to prepare for recovery



Note: In 2Q 2009 Industrial manufacturers n=60, All respondents, n=110

Survey demographics and research methodology

Demographics

Who	Senior executives of US-based, industrial manufacturing organizations	
Interview dates	July 17, 2009 to October 12, 2009	
	Industrial manufacturers (60)	All respondents (110)
Average number of employees	4,139	4,180
Average business unit revenue	\$2.29 billion	\$2.65 billion
Average enterprise revenue	\$6.42 billion	\$10.13 billion
Market capitalization	\$5.69 billion	\$9.89 billion
Industry sectors	Products 100% Manufacturing 100% Trade/Distribution --- All other --- Services ---	Products 79% Manufacturing 68% Trade/Distribution 2% All other 9% Services 21%

Methodology

PricewaterhouseCoopers' Manufacturing Barometer is a quarterly telephone survey conducted by the independent research firm BSI Global Research Inc. Our regular survey panel consists of senior executives from a geographically balanced sample of large companies in the United States. Ninety-five percent of the panelists hold titles such as president, CEO, CFO, VP of finance, treasurer, controller, internal audit director or other related title.

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About the research:

The Manufacturing Barometer is one in a series of quarterly business outlook surveys from PricewaterhouseCoopers. The survey provides a view on the 12-month outlook for revenue growth, new investments, new hiring plans, emerging business barriers and more. In addition to the business outlook, we hear from our panelists about special issues they face as the business climate changes. Results of the quarterly business outlook surveys and special issue surveys are available from www.barometersurveys.com.

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