Global Views

Weekly commentary on economic and financial market developments

October 5, 2012

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Psst! Hey Buddy, Need A Bail-Out?

- **Please see our full indicator, central bank, auction and event calendars on pp. A3-A8.**

Europe will go a long way toward determining the week's global market tone and it starts early with a focus on countries receiving bail-outs. Portugal's cabinet holds an extraordinary cabinet meeting on Sunday as the fifth quarterly review of that country's aid program concludes and following the introduction of fresh austerity measures this past week that were designed to replace cancelled plans to hike the country's social security tax rate. This may help Portugal avert a fresh review, but the country's finances and aid initiatives will be a topic of discussion at the meeting of euro-area finance ministers on Monday and Tuesday. Greece will also be a topic of discussion as it faces heightened risk of falling short of the troika's (ECB-EC-IMF) timetable for fiscal and economic reforms. To that effect, markets are taking as positive a fresh announcement that German Chancellor Angela Merkel will visit Greece on Tuesday for direct talks with Greek Prime Minister Antonis Samaras. Merkel's media spokesman remarked that "We want to help Greece stabilize within the euro zone. We do this by contributing massively to the rescue programs Greece I and Greece II." On the one hand it may just be a polite gesture after Samaras visited Merkel's home turf. On the other hand, when accompanied by further remarks like "We see that under the Samaras government there's a strengthened reform effort and we want to support that", the visit may be more than just symbolic and may hint that Greece's struggles to meet troika timelines could be given a lift by Germany. If so, then Merkel is stepping up to a truer statesman role ahead of her own election next year. Spain's calendar appears light, but with the first of three EU Leaders Summits on tap for October 18-19, the pressure on Spain to request a bail-out will gradually rise as it approaches its own elections. The scene will be set just prior to the politics via fresh forecasts for European economies from the EU that land on Sunday and that are unlikely to be the cheeriest development of the week. Ditto for fresh IMF world forecasts and German forecasts from a leading think-tank over the course of the week. Banking union will also receive intensified focus on two fronts. One is an ECB-Fed conference on bank funding in Germany at the start of the week, and the other will be an EU Parliament panel's debate on banking union proposals on Wednesday. Data risk will be skewed toward Germany in terms of releases that matter the most to world markets. The country's export growth and factory output will provide important updates on the continued health of the economy. Consensus is not upbeat and expects both exports and factory output to fall on the heels of disappointing factory orders data this past week that, if it all comes true, would signal renewed worries over momentum in Germany's economy. Industrial output figures across the euro zone, France, Italy and the UK plus French and UK trade and French CPI round out the data hits. Auction risk should be relatively light and focused on safehaven flows into bunds and gilts.

After a Columbus Day holiday on Monday, political fireworks could get the most **US** headlines next week as Congress reconvenes on Wednesday and the sparring between GOP contender Mitt Romney and President Obama intensifies following what I thought to be a Romney win in the first televised Presidential debate. Their running mates get a go at each other next Thursday when Vice President Joe Biden confronts Congressman Paul Ryan. Biden may have the edge with respect to Washington's ways, but I would think he stands a chance only if he veers away from technical policy matters over which Ryan is likely to hold court. The next Presidential debate is scheduled for October 16th in a town hall format and shifts more of the focus to foreign policy in addition to domestic policy matters that were the exclusive focus of the first debate. Foreign policy will be the exclusive focal point of the final Presidential debate on October 22nd. Data risk will be relatively soft. The move toward greater transparency at the Fed via frequent commentary provided by Fed officials has made the Fed's Beige Book (Wednesday) less material since the regional Fed Presidents are frequently sharing their beliefs based in part upon how their regions fit into the bigger picture. To that effect, it will be a heavy week for Fed speak with Vice Chairman Janet Yellen pulling the communication strings as each of Fisher, Kocherlakota, Plosser, Bullard, and Lacker speak— and who knows who else could appear randomly. The Fed's heavy-hitters also hit the trails next week with each of Vice Chair Yellen, and Governors Tarullo and Raskin scheduled to speak although only Yellen's speech is likely to be market relevant with parallels to Japan's economy a likely topic. The Q3 earnings season also kicks off next week with Alcoa starting it all on Tuesday and the next few weeks will help shape the equity market tone for some time until key global event risk draws nearer into year-end. The US trade balance is expected to widen thanks in no small part to upward

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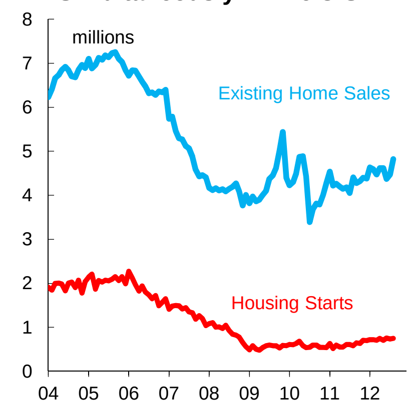
pressure upon oil prices in August. Producer prices won't get much attention behind preferred price measures and they remain relatively tame at 1.8% y/y on headline prices anyway. Of note, however, is that whereas market inflation breakevens and the Fed's preferred market measure (the 5 year forward breakeven) had been trending lower since the FOMC, they went right back upward over the course of the past week and this volatility signals market uncertainty over mixed near-term growth readings and year-end political and fiscal uncertainties with implications for price stability. UofM confidence rounds out the readings and could carry a market-relevant surprise. The Conference Board's consumer confidence index recently shot upward by more than expected, even though it's more weighted toward what turns out to be pretty soft labour markets. The UofM indicator is more focused on markets and household finances that are more resilient. We and consensus could therefore be too cautious toward upsides in this reading. The US auctions 3s, 10s and 30s next week.

Canadian markets start the week on holiday for Thanksgiving, and things don't get much more interesting afterward. The country's markets will follow the broad global tone set by developments elsewhere. Tuesday's housing starts for September might provide a better reading on housing markets than has been available from other housing indicators of late. Whereas national resale figures have dropped by 11% from their peak earlier this year, housing starts have been considerably more resilient. Residential building permits fell slightly in August over July in unit terms (as opposed to value) and this might suggest some moderation in construction levels into September. That said, permit levels remain elevated. Apart from the monthly noise, the bigger macro thematic issue remains whether weakness in resales will be correlated with dropping construction activity as it was in the US where new home construction and resales corrected along similar paths when builders became increasingly reticent to add new supply as inventories backed up in resale and new markets (see chart). This is a key debate in Canada, since resales carry few connotations for GDP by virtue of the fact that they are mostly paper transfers with the only value-added in the transactions provided by facilitating services from agents, banks and lawyers. New home construction, however, is much more significant to GDP through higher value-added content. Canada's trade balance will also be updated next week and this will be significant beside the housing numbers as both housing and trade have deteriorated simultaneously. Consensus is expecting a smaller trade deficit for the month, but the prior month's figures started off Q3 on such a sour note that it would take a large rebound in August and September just to leave trade's contribution to GDP growth flat in Q3. Scotia Economics doesn't foresee this and expects net trade to be a sizeable drag on GDP growth that we think is tracking at about 1.4% at annualized rates in Q3. Canada also auction 3s on Wednesday.

New And Resales Went Down Simultaneously In The U.S.



Source: U.S. Census Bureau, Scotia Economics.

Is **China** stepping on the stimulus pedal? One of the better metrics for estimating the extent to which the Chinese government is encouraging economic growth is data on new yuan loans, which offer an indication of the pace at which China's state-controlled banking sector is flooding liquidity into the system with tacit government approval. Loan growth picked up mid-year to the fastest pace since China's 2008-09 stimulus was implemented (see chart). We suggest watching for the September year-to-date loan growth and comparing it to where loans were last September as a way of looking through the seasonality issues when the data are released next week (the government doesn't provide a specific date). We'll get a better look at the shape of Asian trade in September via Japan's trade balance (Monday), Philippines trade data on Tuesday, and Taiwan's trade balance (Monday). Exports slumped in August and we'll be watching to see if weakness in Europe and China continue to weigh on the rest of the region. India's industrial production (Friday) has been flat or negative in year-on-year terms for four of the past five months and many see it as a sign of the general slump in the BRICS countries. Australian jobs data on Wednesday will be watched for ramifications for the RBA, which

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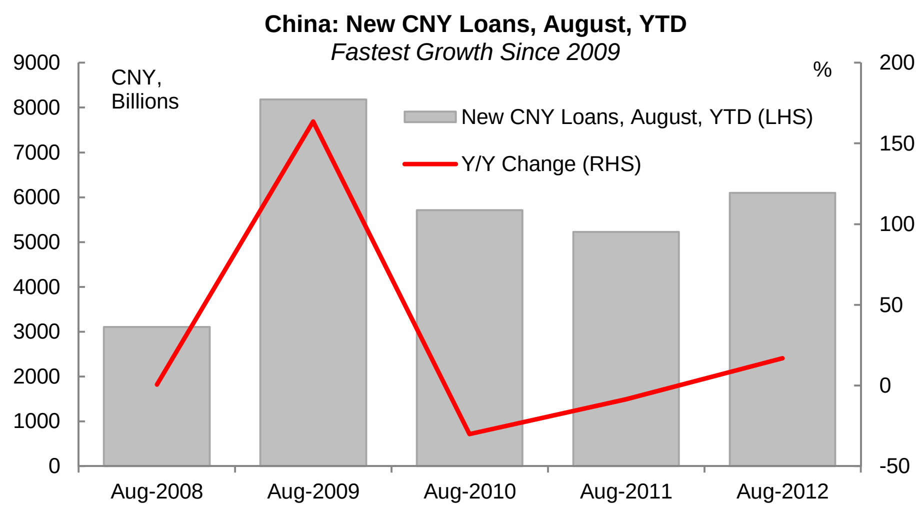
markets still expect to cut rates further as judged by OIS prices. Will Bank Korea cut its reference rate to 2.75% on Thursday after a surprise reduction in June? Every forecaster but one in the Bloomberg consensus thinks so, and a weak print on employment data on Wednesday could buttress the case. Bank Indonesia is expected to stay on hold on Thursday. China's Markit services PMI will be out on Monday while North American accounts are on holiday.

Latam markets will be focused upon Venezuela's Presidential election. Hugo Chavez puts his fourteen controversial years in office amid failing health up against a brave opponent in Henrique Capriles who has the backing of no fewer than thirty opposition parties. Mr. Chavez has unique friends through having supported governments in Cuba, Iran, Syria, and Belarus, while sourcing military items from Russia and securing heavy investments from China, and he'll need his supporters, their political influences, and his domination of state-run media to work in his favour in the face of mixed opinions on the outcome. Brazil's central bank is expected by a slim majority in the Bloomberg consensus to leave its SELIC policy rate on hold at a record low of 7.5% since its introduction in 1999. Mexican CPI, industrial production and trade plus Peru's central bank rate round out other Latam highlights.



Source: Bloomberg, China NBS, Scotia Economics.

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Markets Should Be Looking Through BoC's Loose Rate Guidance

BoC Senior Deputy Governor Tiff Macklem's comments on October 4th motivated a small backing up in 2-year yields and a small appreciation in CAD as markets were somehow surprised that Macklem repeated the BoC's very vague rate guidance. They shouldn't have been surprised, and should be leaning against BoC rhetoric in my opinion.

Macklem Was Bound To Repeat BoC Rate Guidance

First, the BoC is not like the Federal Reserve in that over time each Governor, including Carney, keeps his governing council members on a generally short rope. There are no Richard Fishers or Charles Evans at the BoC to go out and offer sharply divergent opinions in public as they do at the Fed, and the outspoken behaviour of ECB or BoE members is neither encouraged nor tolerated at the BoC. In fact, this is probably a fair comment on Canada in general. Regardless, while the BoC's governing council members, including Macklem, are all very clever and experienced people, the BoC's culture is relatively more opaque than other central banks like the Fed, ECB and BoE. That's not new under Carney either. Thus, governing council members are highly unlikely to signal any bias shift or change in thinking between statements. Hence one of the reasons why Macklem repeated the party line. Carney is more likely to stray, but even there he can be highly reticent to do anything other than wait until the next chance to give full and careful consideration toward any cause for changing one's thinking even if modestly so and after considering input from the BoC's staff. Thus, with the full statement and Monetary Policy Report due just less than three weeks away on October 23 & 24, why not wait? Indeed, the window is closing as the BoC's blackout period on communications approaches (starting on Wednesday October 16th).

That said, I still think the BoC will continue the conditional rate guidance in the upcoming statement and MPR largely because it's so vague as to be of limited use anyway. "To the extent" their forecasts come true, they "may" withdraw "modest" stimulus at some point over the "medium term." You wouldn't want to steer an ocean liner through the Panama canal with that kind of guidance which essentially says they might raise rates by 50-75bps or so at some point over the next couple of years if their base case comes true; hence the wiggle room in the guidance. I would, however, expect the aggressiveness of the communications surrounding the July statement and MPR to be moderated in frequency and tone and that itself could be a subtle hint of a more uncertain/neutral BoC. In this regard, it's important to note that the BoC is undergoing as much experimentation with communication tools as the Fed through a different type of rate pledge and by shifting tone and frequency signals.

Much Has Changed Since The July MPR

More importantly, as we wrote in columns starting in July and August, I think that the October MPR has to revise near-term growth lower, raise spare capacity estimates somewhat higher, and signal more caution. Our bias remains that spare capacity will continue to grow through to 2014 and particularly over the next six months, not shrink and close off by the end of 2013 as the BoC expected as of the July MPR (see chart). I would be amazed, in fact, if the BoC looks entirely through several disturbing recent developments. Look at what has happened since the July MPR that was based mostly upon lagged data up to April through June but for a few very limited readings even at the month of June. Housing is retreating rapidly with national resale volumes going down by double digits and ditto for Toronto's new home sales and this is happening in the wake of the July 9th mortgage rule changes and as the country sits atop all-time record highs for everything in the household sector. That's not true across all markets (three cheers for Calgary!), but Ottawa was particularly concerned about housing excesses in Toronto and Vancouver and wished conditions would cool; this is unfortunately shaping up to be a lesson on being careful over what one wishes for in life and in conducting public policy. Ottawa was also concerned about debt growth, but there is no longer any growth in consumer loans after inflation, and mortgage growth is operating at a fraction of what it was pre-crisis. The risk here is that prices and complementary forms of consumer spending soften in lagged fashion to weakened housing volumes and confidence. Rapidly cooling, not overheating, housing markets should now be the focus of Ottawa's policy concerns. Indeed, this is developing as we argued it would in our piece "Canada Tightens Mortgage Rules - Again," on June 22nd in our *Global Views* weekly (pp.4-6) right after the mortgage rule

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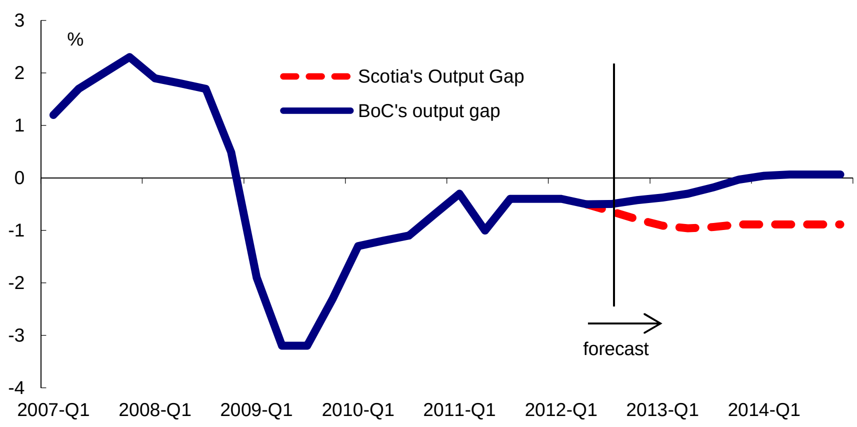
changes were announced. Further, the country is running record trade deficits (indeed, twin fiscal and trade deficits). Not all is peachy in Canada's little corner of the world by any means even as the country touts impressive relative strengths in banking, micro-foundations to mortgage markets that insulate against a US- or European-style housing debacle, natural resources, corporate balance sheets, and fiscal metrics. CAD strength is harming manufacturers and exporters as I believe it has spent the summer going beyond the fundamentals, in part lifted by what I think is prematurely hawkish policy rhetoric. Further, GDP growth is poised to extend 1-handled performance for four consecutive quarters through to year-end with two in the bag and two to go in our forecasts and with Q3 looking like 1-1.5% growth at best. Q3 would therefore risk coming in considerably lower than the BoC's 2% which itself had been revised lower in July from the April estimate for Q3. Growth is therefore significantly under-performing the potential speed limit of the economy.

The BoC Is A Long Way Off From Hiking

In short, this is not a central bank on the verge of hiking by any means. Indeed, I think a policy tightening bias in regulatory and monetary policy terms is contributing toward soft economic growth. Changed mortgage rules, stricter OSFI oversight of the CMHC, private mortgage insurers and lenders, changed accounting rules last Fall that brought securitized assets back on balance sheet, Basel III come January and already essentially being implemented for some time now, and moral suasion applied against households and lenders (and corporations, and exporters...) all amount to net policy tightening that in my opinion is likely cooling housing markets considerably more than originally intended. Further, the BoC is missing its inflation target by a considerable margin. Headline CPI at 1.2% with core (the operational guide) at 1.6% are both overestimated by the BoC's own research to the tune of a half-point measurement error since CPI weights don't adjust dynamically as the Fed's preferred PCE deflator does. For an inflation-targeting central bank with a 2% target that is operating against a weakening backdrop, tightened monetary policy is a long way off. That's without even getting into the plethora of risks facing the global economy into year-end and early next year as per our piece "Risk Off — Due To A Packed Global Calendar" in last week's *Global Views*. In my opinion, bet against the rhetoric and loose guidance — the BoC is on hold for a long time yet with 2014 our call amid two tail risks that in my opinion are fatter toward the later rather than sooner end of the spectrum.

Will Canadian Spare Capacity Narrow Or Widen?



Source: Bank of Canada, Statistics Canada, Scotia Economics

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More Signs Of Softening In Canada's Housing Market

- **Canada's housing slowdown has accelerated heading into the fall.**

Based on reports from major local real estate boards, Canada's housing market slowdown has stretched into the fall. Total home sales across 12 regional boards, representing roughly half of national activity, declined 15% y/y in September. Among major markets, sales were down 11% y/y in August. National resale figures will be released in mid-October.

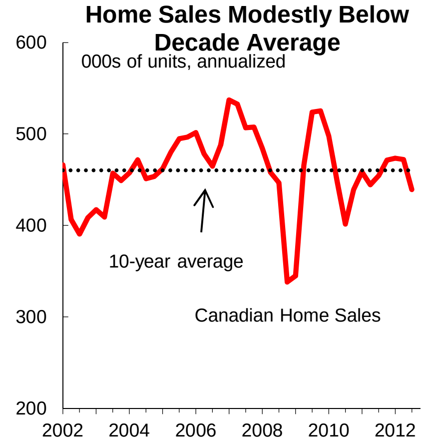
The loss of momentum is pervasive. The sharpest falloff has been in Vancouver, where sales were down over 30% y/y in September and are trending well below historical averages. Toronto's market has also turned, with volumes down roughly 20% y/y, albeit from historically high levels last year. Of the 12 boards reporting for September, only Calgary recorded a y/y increase in sales last month. For the most part, higher-priced homes and housing markets have seen the biggest drop.

Potential buyers are being squeezed by a slower pace of job growth combined with weakening housing affordability, the latter a reflection of high home prices and tougher mortgage insurance rules. The softening in activity was evident before the latest regulatory changes, which lowered the maximum loan amortization period from 30 years to 25 as of early July, though the tighter rules appear to have hastened the adjustment. Anecdotal evidence also suggests lower levels of investor and/or foreign demand.

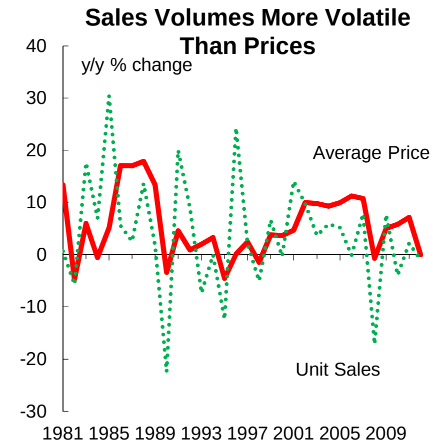
Put in a broader context, current sales levels in most parts of the country are not substantially below the average of the past decade. We have for some time been predicting a softening in activity (both demand and pricing) from unsustainable levels. Nonetheless, the adjustment has been faster than expected.

Average home prices are still holding up well. Conditions in the majority of centres are balanced, measured by the ratio of new listings -to-sales (around 2.0) or months' supply (around 6). However, price trends tend to lag sales volumes, as homeowners are reluctant to cut prices, preferring in many cases to pull off their listing. Swings in volumes are typically greater than in prices, especially in a downmarket. The response of prices to demand shifts is asymmetrical, with demand increases tending to affect prices more than decreases.

Looking ahead, we expect home sales will continue to drift lower into next year, putting moderate downward pressure on prices. Downside risk is higher in markets that have already shifted into buyers' territory (e.g. Vancouver), or in some property segments (e.g. the more heavily supplied Toronto condo market). However, if the Canadian economy continues to post moderate job and income growth, a sharp correction in national average home prices is unlikely. Underlying housing fundamentals are sound, with delinquencies low and inventories contained.



Source: CREA, Scotia Economics



Source: CREA, Scotia Economics

Existing Home Sales

	Sept/11	Sept/12	y/y % chg
Ottawa	1,201	993	-17.3
Toronto	7,422	5,879	-20.8
Hamilton	1,125	884	-21.4
Kitchener	504	442	-12.3
Winnipeg	1,214	1,040	-14.3
Saskatoon	488	448	-8.2
Regina	370	265	-28.4
Edmonton	1,442	1,269	-12.0
Calgary	1,840	2,104	14.3
Fraser Valley	1,165	857	-26.4
Vancouver	2,246	1,516	-32.5
Victoria	436	400	-8.3
TOTAL	**19,453**	**16,097**	**-14.6**

Source: Local real estate associations, Scotia Economics

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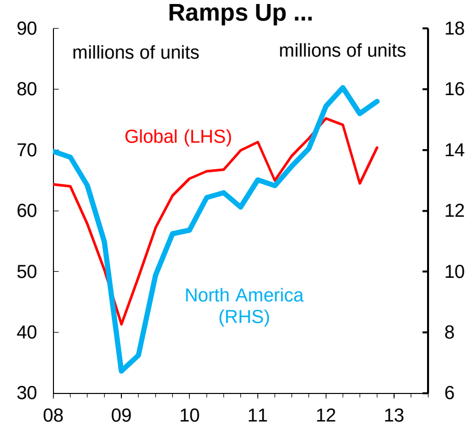
Global Auto Production Revs Up

- **Assemblies are picking up in every region, except Western Europe.**

After a summer lull that added to the manufacturing doldrums of recent months, auto assembly plants have started to ramp up across most of the world and will provide a significant boost to manufacturing and overall economic activity in the final quarter of 2012. Russia and Brazil will lead the way, with assemblies scheduled to post double-digit year-over-year increases. However, every region except Western Europe is expected to post gains in coming months, helping to revive manufacturing activity.

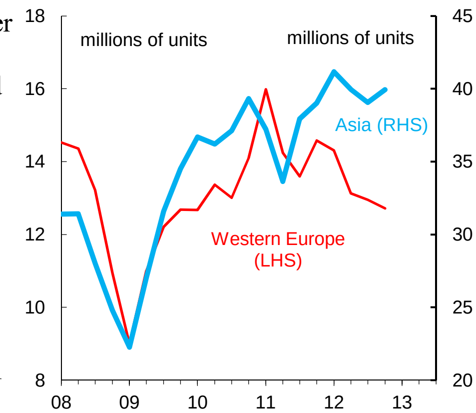
Global Vehicle Production Ramps Up ...



Source: Scotiabank Global Auto Report.

Assemblies in South America are likely to climb more than 15% y/y in the final months of 2012, underpinned by the recent strength in new car demand in Brazil. Car sales in Brazil have soared by more than 20% y/y in recent months and vehicle production set a record high in August. In Russia, vehicle output is on target to reach a record of 2.3 million units this year. Local brands still account for two-thirds of overall vehicle production in Russia, but assemblies by Volkswagen, GM and Ford have surged in excess of 50% this year.

... Except in Western Europe



Source: Scotiabank Global Auto Report.

The improvement in vehicle production across North America will help bolster manufacturing prospects at a time when durable goods orders in other sectors have been weak. The U.S. ISM manufacturing index expanded in September for the first time since May, and will be supported going forward by the ramp-up of North American car and truck output to an annualized 15.6 million units in the final quarter of 2012, from a low of less than 15.0 million units in August. In fact, given stronger-than-expected sales in the United States in recent months, automakers have boosted their production schedule by 85,000 units, roughly 2.5%, over the past month.

Automakers in North America are adding additional shifts or scheduling overtime for the next several months to ensure that the industry has enough supply on hand to meet stronger-than-expected demand. General Motors will lead the gains in North America in the fourth quarter, partly due to the recent re-opening of its Spring Hill, Tennessee plant in September to produce the popular Chevrolet Equinox. Other automakers including Ford, VW, Hyundai and Nissan have also recently added third shifts at several facilities, especially in the U.S. South.

Further production increases are scheduled for the new year, as foreign automakers shift output to North America. For example, Toyota is hiring additional workers for both of its Canadian facilities and will be ramping up output early next year. Capacity at the Cambridge, Ontario facility is being increased by 30,000 units per annum, while the Woodstock facility, which produces the popular RAV4 crossover utility, will expand by 50,000 units in early 2013.

In contrast, conditions in Western Europe continue to deteriorate. Preliminary sales results for September point to at least a 15% slump across the region — double the 7.5% decline through August. Even prior to the double-digit downturn in September, French and Italian automakers had announced work stoppages up to three weeks due to weak demand. Only German automakers, BMW, VW and Audi are likely to raise fourth-quarter assemblies above a year earlier due to strong demand. All three manufacturers are posting solid gains in emerging markets, while VW is also benefitting from a higher market share in Western Europe.

To help reverse the sales fall-out in Spain, the government announced a vehicle scrapping program this week. The program provides a discount of EUR2,000 to new car buyers — half will come from the Spanish government and the other half from automakers. The government has set aside EUR75 million for this initiative.

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Canada's Employment Recovery Bypasses Youth

- **Since the recession, improving youth unemployment has relied upon a declining labour force.**

While Canada is noted for its less severe job losses during the recession and its subsequent payroll resurgence, nationally youth 15-24 have not participated in the employment rebound. The decline in Canada's youth unemployment rate from the 16.4% peak in July 2009 to 15.0% in September 2012 *(chart 1)* reflects almost 68,000 youth leaving the labour force as employment for this age group slid by nearly 17,000. Individuals 15-24, representing roughly 15% of Canada's working-age population, accounted for 52% of the total 431,000 jobs lost during the recent downturn. Though an outsized share of the national loss, during the recessions in the early 1980s and early 1990s, the youth job loss averaged over 70% of the national job decline. During this recovery, the further 0.7% job loss among youth since July 2009 leaves the total correction in youth employment since the pre-recession peak in September 2008 at 10.0% (-267,600 jobs, *chart 2)*. Although the current employment experience for Canada's youth is discouraging, it is less harsh than the 12.0% job loss among U.S. youth since their pre-recession peak, and the decline of almost 18.0% in euro zone youth employment over the five years to Q2 2012.

This time around, the recessionary peak in Canadian youth unemployment is lower than in prior downturns, improving upon the high of 20½% in October 1982 and 18½% in August 1992. Yet the current jobless rate among Canadians 15-24 is still 2½ times the 6.0% unemployment rate for older workers. If the 15-24 labour force had not declined since the recent peak in September 2008, the youth unemployment rate four years later in September 2012 would have been 20.0%.

A key feature distinguishing this cycle is the success of Canadians 55 years and older in gaining, not losing, jobs during the recession and then subsequently capturing nearly 60% of the national employment increase during the recovery. For the comparable periods after the recessions in the early 1980s and early 1990s, this older age group's share of the employment recovery averaged just over 3.0%.

For the industries in chart 3 that account for significant shares of Canadian youth employment, payrolls from January to September of this year have only climbed in health care and social services relative to four years earlier. Over the same period, youth employment in manufacturing, construction and retail and wholesale trade, has fallen by 23.7%, 11.8% and 9.5%, respectively. For the same industries, employment for Canadians 55+ has climbed by 14.5%, 11.8% and 32.8%. Across Canada's other major industries, youth employment was essentially flat in education and only increased in the primary sector.

Canada's Youth:

Chart #1

Unemployment Rate* …

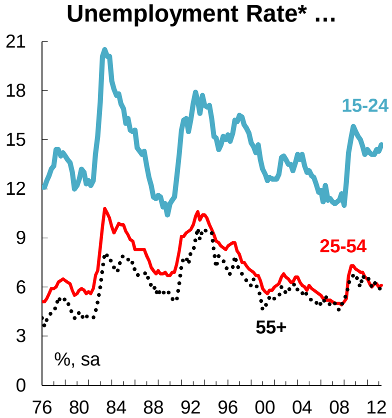


Chart #2

… Employment* …

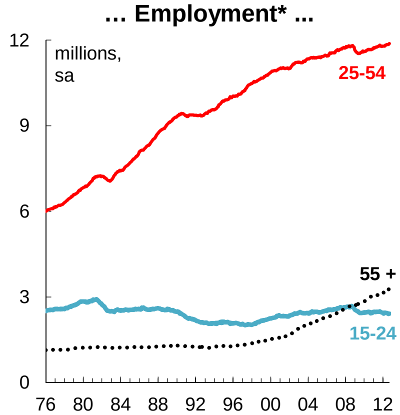
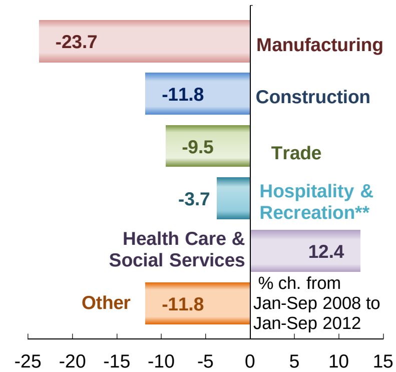


Chart #3

… and Job Creation By Key Industry



* Plotted to September 2012. ** Includes information and culture. Source for all charts in the article: Statistics Canada, Scotia Economics.

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Lumber & OSB Prices Will Recover In 2013

- **As a modest lift in U.S. housing starts hits a wall of limited North American supply; Dramatic gains are likely in 2014-15.**

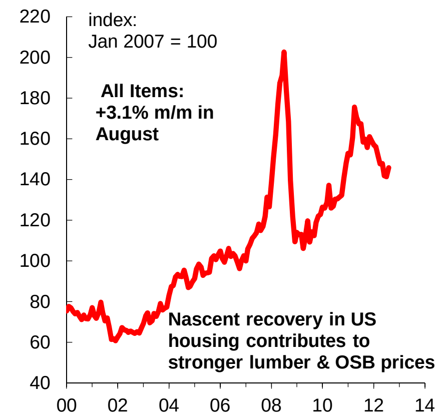
After a challenging environment since 2008 — linked to a prolonged and sharp downturn in U.S. housing — lumber & OSB producers, as well as MDF & particleboard manufacturers, will enjoy a substantial recovery in earnings in 2013. An improvement is already underway. Western Spruce-Pine-Fir 2x4 lumber prices (No.2 & Btr) — relevant for the B.C. Interior/Prairie provinces and the bellwether for North America — will strengthen from an average of US$285 per mfbm in 2012 to a profitable US$315 in 2013 and US$350 in 2014 — well above average mill costs in the B.C. Interior estimated at US$280 (including mill cash costs & overheads plus a probable 5-10% export tax on U.S. shipments next year). Low-quartile producers have significantly lower costs. (The export tax varies inversely with the Random Lengths Framing Lumber Composite Price and will be reduced in 2013, as prices rise.)

While the U.S. housing recovery remains fragile, a pick-up in lumber prices will occur with only a modest further gain in U.S. housing starts to the 850,000 unit mark in 2013 — up from 729,000 units annualized through August this year, but still well below the 2005-06 peak (1.93 million). Substantial sawmill closures in Canada and the United States since 2006 (an 11.5% capacity loss, the equivalent of 140 mills) — combined with fewer logging contractors, trades people and truckers in the building materials industry — will create challenges in meeting higher demand. While lumber mills will be able to increase shifts across North America in 2013, higher prices will be required to incent greater output. Considerable price volatility is expected. As U.S. housing starts approach the one million unit level mid-decade, new sawmill capability will again be required.

Market development for B.C. & Alberta lumber in China has contributed to a tightening of the North American supply & demand balance. Canadian softwood lumber exports to China rose by 4.7% yr/yr in 2012:H1, though deliveries trailed year-earlier levels in May and June, and decelerated from the scorching 63% gain of 2011:H1. Canadian mills appear to have recently re-focused on the U.S. market amid softer economic conditions in China. However, with China's private-sector construction activity expected to rebound in 2013, we expect sales to this market to pick up again. China was the destination for 22.3% of Canadian softwood lumber shipments in 2012:H1, the United States 62.5% and Japan 7.6%. For Western Canada alone, China accounted for 28% of shipments in 2012:H1.

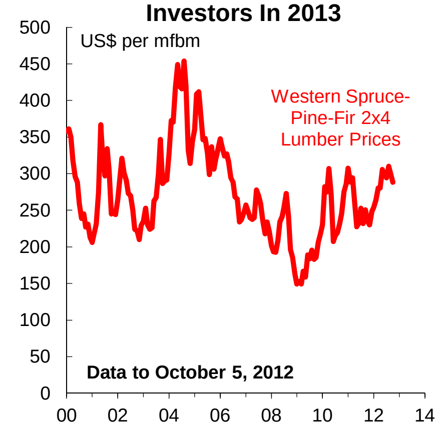
The near-term outlook for OSB — oriented strand board used primarily in flooring & roofing in residential housing, but also in commercial construction — is even more compelling than lumber. Capacity re-starts will be needed in 2013, recently spurring

Scotiabank Commodity Price Index



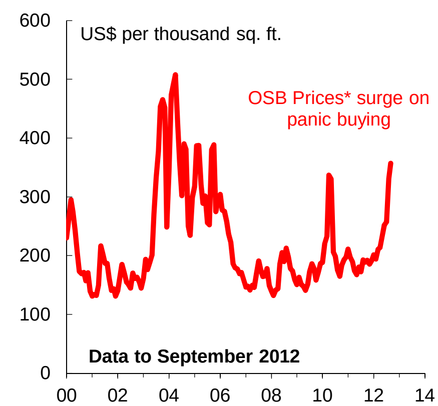
Source: Scotiabank Commodity Price Index.

Lumber & OSB -- 'Top Picks' For Investors In 2013



Source: Scotiabank Commodity Price Index.

OSB Prices Spike



Source: Scotiabank Commodity Price Index.
* U.S. Northcentral region, 7/16" basis.

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announcements by Georgia Pacific and Arbec Forest Products (involving a mill in Miramichi, New Brunswick). Since 2006, 7.2 bn sq. ft. of OSB capacity across the USA & Canada has been idled, of which 4.7 bn is permanently shut, and only 2.5 bn is available for re-start. Panic buying in August reflected lack of supplies for 'sub-flooring' in some areas of the United States (in the Mid-Atlantic and California). OSB prices in mid-September at US$350 per thousand sq. ft. (7/16 inch) yield profit margins of 41%. Plywood prices have also been boosted.

The Fed's QE3 should be a positive for the U.S. housing market, with mortgage rates declining further from already low levels. This should spur private investors to buy more 'distressed' properties for resale or rental. However, in my view, tighter bank lending requirements for borrowers (higher down payments, credit scores & lower appraised property values) and weak employment conditions, rather than mortgage rates, have been bigger restraints on housing activity in recent years.

Recent U.S. housing indicators have turned positive. The median price of an existing home may have bottomed in February 2012 and is now up 9.5% yr/yr. This reflects a declining inventory of existing homes for sale — now at 6.2 months' supply — near the 5.3 months average from 2000-07. However, the number of foreclosed properties — eventually available for resale — remains high. On a more positive note, U.S. household formation was only 800,000 in 2011, well below a normal 1.1 million, pointing to a big pick-up in housing demand down the road. The U.S. stock of economically viable housing may also be much lower than statistics suggest. (MDF prices, a panel board used in kitchen cabinets and furniture, have been at record highs this year.)

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Venezuelan Elections: The Closest Opportunity For A Change

- **Henrique Capriles, a strong competitor for Hugo Chávez.**

After almost 14 years in power, Hugo Chávez faces his closest presidential contest yet in the upcoming election on Sunday, October 7th. For the first time, the opposition elected one single candidate, Henrique Capriles, who has been increasing his already high popularity in recent months. Results from the most reliable polling firms showed that the election will be tight; however, outcomes vary depending on firms and methodologies. Nonetheless, the common theme is that Capriles has been gaining ground against Chávez without achieving a clear advantage.

Amid heightened concerns over Chávez's health, Capriles has presented a strong, pro-institutional, and anti-corruption profile. He has promised that social programs, particularly related to the reduction of hunger and poverty, will be under the supervision, evaluation and administration of the correspondent ministry, not under one party. He has also expressed his willingness to increase investment, simplify tax regimes, stop nationalizations, raise minimum wages and reduce electricity outages and crime. Additionally, in light of the recent explosion in the Amuray oil refinery, the opposition candidate has recognized the need to increase investment in infrastructure as the deterioration in refineries, hospitals and other government institutions has been growing in the last decade. Capriles has been very active, appearing at many campaign events, even outside Venezuela, meeting with the Colombian president, trying to offset Chavez's control over the media.

President Chávez has organized fewer campaign events compared to the opposition; however, he has appeared at several official government affairs. His rhetoric has been in line with the policies he has advocated in the past, focusing on poverty, new housing for the homeless, income redistribution and centralization. He has stated that if he is not re-elected, the country will face civil war.

Both the senior operational commander of the army and the National Electoral Council's (CNE) president have promised free and secure elections; however, many Venezuelan institutions have proven to be pro-Chávez, particularly the military forces. Consequently, we believe that fears of retaliation are still present among the general public, and this could affect the voting process.

The CNE president has announced that results will not be unveiled until they are "viewed as irreversible". This could take time, especially if the results are tight — as the polls have suggested — which may prompt uncertainty. No party is allowed to publish any official polls or results ahead of the CNE.

We anticipate that in the case of a victory by Chávez, economic policies will continue as they have been throughout his term; however, we expect that fiscal imbalances as well as the overvalued currency and a high inflationary environment will not be sustainable for much longer, provoking some adjustments by year-end or next year.

On the other hand, if Capriles wins the elections, we anticipate a period of high uncertainty and even social unrest driven by Chávez supporters in the short term. The role of the armed forces in a post-Chávez era remains a key uncertainty. Additionally, Chavez's party has control over the National Assembly until 2014, which would limit Capriles's agenda in the next two years; however, some minor reforms could be initiated even before he has majority support from Congress offering a more sustainable future for the country.

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Pemex Update: Lots Of News

The following article was published on October 4, 2012.

A steady flow of good news about Pemex has dominated the press in recent months. Just today, Bloomberg reported the discovery of a second deepwater field in the Gulf of Mexico. It was only a couple of months ago that President Calderon had reported the first discovery of deep water crude. Other news has included excitement over the potential for shale gas development, since Mexico has the fourth-largest reserves in the world. The company recently reported record production for the month of September, and has said that it could maintain high levels of production at its top field for more than a decade. All of this positive news would suggest that investors can forget prior concerns around Pemex's production levels, and sovereign analysts can relax about the dependence of Mexican finances on oil.

While we do think that there has been good news about Pemex that should matter to investors, we don't think it is any of the above. Most of the news demonstrates that Pemex still has large amounts of unexplored natural resources, which though undoubtedly good for the company, is nothing new to investors. It is true that September production was the highest in the past 17 months, but it was only a marginal increase of 1% over the average during that prior period, probably aided in part by small declines in production earlier this year due to maintenance delays. We interpret Pemex production data over the last two years as demonstrating stability with no significant trend in the near term; those data continue to represent a significant improvement relative to the rapid declines we saw through 2009.

The concern among investors has always been with regards to Pemex's technical and administrative capability to efficiently extract resources. We think the focus should shift more to administrative abilities than technical assets, since technology can be acquired from foreign companies. For example, the drilling platform making deepwater discoveries for Pemex is leased.

The news that investors should pay attention to instead is the continued talk about reforms. No major reform is imminent, and it is too early to know what type of reform could ultimately win approval. Nevertheless, the fact that Peña Nieto asked Brazil for assistance or that the CEO of Pemex recently outlined a number of radical reforms suggests that pre-election pledges have not been forgotten. Considering the magnitude of the planned changes, it could be years before a reform is adopted. In the meantime, we are tracking progress on incentive contracts. Although they always seem behind schedule, auctions for these contracts continue and foreign service providers are participating in them. Stage 2 of the incentive contracts (for the Chicontepec field) is scheduled for December but we may not see Stage 3 for deepwater fields until 2014. The good news is that these auctions can progress without additional laws or constitutional changes.

Pemex rallied considerably in line with the rally in Mexican sovereign bonds. Nevertheless, the spread over sovereign in the long-end remains mostly stable at around 90bp. We think Pemex should eventually outperform, either because its spread over sovereign becomes increasingly attractive as the sovereign spread declines, or because reforms are eventually implemented. Both of these could take time, however.

For more information on reforms, see our article "Privatizing Pemex" (May 18, 2012).

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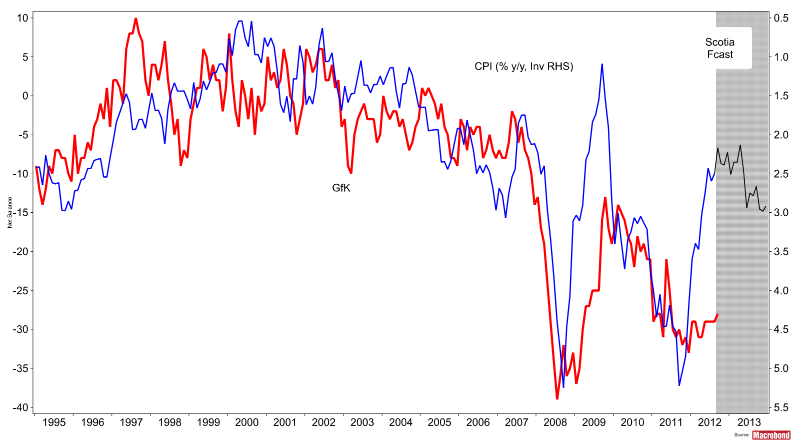
UK Disposable Income Flying (Kind Of)

Real disposable income better than expected, but…

- At the start of the year, one of our key themes for the UK was that inflation was likely to fall sharply — which in turn would provide a significant boost to household real disposable income growth (RPDI). Going a step further that should provide support for consumer spending growth — the biggest share of GDP by expenditure.
- Last week's full breakdown of GDP for Q2 showed that RPDI has indeed recovered. However, the improvement in consumer spending growth has so far been lacklustre. Household consumption growth has been less negative than it was in mid-2011, but has stopped short of turning significantly positive. So what has gone wrong?

Down in the Dumps

Chart 1: UK CPI vs Consumer Confidence



- There are two key things that make consumers happy (or sad). Firstly, having a job. Secondly, low inflation — since this means that wage earners retain more of their disposable income. So far this year, UK consumers have had both. Employment growth has been super-strong and inflation has fallen sharply – down from over 5% y/y to 2.5% y/y. Yet the GfK measure of consumer confidence has barely recovered (Chart 1).
- Chart 1 also shows that if we look back to 2008-09, we had a similarly abrupt slowdown in inflation. Within six months of the peak in inflation there was an impressive rebound in consumer confidence. This was despite the UK economy being in the midst of the deepest recession since the Second World War. So what is different now?

Different kind of inflation:

- The fall in inflation in 2008-09 was somewhat different to what we have experienced so far this year. In particular the **level of petrol prices fell sharply in 2008-09**. Petrol prices fell by 30% in late-2008 as the price of oil plunged. Households that kept their jobs (and that was the vast majority) genuinely had more spare cash in their bank account after filling up at the petrol pump compared with earlier that year.
- By contrast, during 2012 the pace of increase in the price of petrol has slowed. However, the outright level has not really fallen. The price of petrol per litre has gone from around 140p per litre down to 130p per litre and then bounced back again. Consumers have not enjoyed the same sort of windfall as they did 4 years ago so have less reason to be happy.
- The drop in energy costs during 2008-09 was reinforced by a sharp slowdown in **food price** inflation. The fall represented less of a burden on disposable income growth. It was rather less extreme than energy since prices did not fall in outright terms — rather they rose more slowly. The pace of decline in food price inflation during 2008-09 was very similar to what we are currently experiencing, so this probably doesn't help to explain why consumer confidence has behaved differently this time around.

Mortgage rates slashed:

- If ever there was a demonstration of a central bank choosing the nuclear option and it being successful, 2008-09 was it. The Bank of England slashed Bank Rate — down by 150bp per meeting

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at one point. This caused the mortgage interest burden to dive from 8% of disposable income down to just ½%.

- Put differently, the change in the mortgage interest burden provided a seven percentage point boost to disposable income growth. That is massive! In particular, that 7-point fall, when compared to a 2½% drag previously — represented a swing of almost ten percentage points!. To put that into context, the biggest contribution to PDI growth in the latest quarter was just 2.5 percentage points.
- As with the experience of petrol, the drop in mortgage rates left most households with more spare cash in their pockets. That was good for consumer confidence and surely contributed to the recovery in consumer spending.

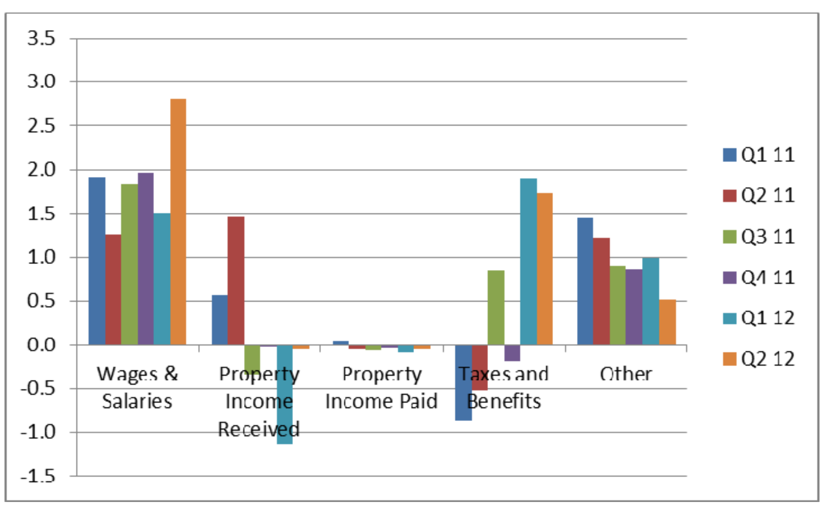
Taxes & benefits:

- This is slightly ambiguous. The 'social benefits' component of the household disposable income calculations showed a significant positive contribution during 2009 – not far off the boost provided by lower mortgage rates described above.
- At face value this might suggest that the government was providing aggressive fiscal ease to support growth. In actual fact, this corresponded with the surge in claimant count unemployment. So while there may have been some discretionary fiscal easing, the bulk of the 'addition' to disposable income was the counterpart to rising job losses. Rather than adding to household income growth, the rise in benefits merely offset the drag from falling wages and salary growth.
- In this regard, the current situation is technically a little more supportive. The taxes on incomes and wealth component of disposable income was a drag on PDI in early-2011. This coincided with the trimming back of the income tax personal allowance for higher income groups as well as the introduction of the 50% income tax band. However, that was a one-off hit to year-over-year disposable income growth. Hence compared with a year earlier, the taxes component is more supportive now because the one-off drag has dropped out of the % y/y calculation.
- Either way, we don't see this aspect as helping to explain why consumer confidence has failed to rebound over the last year. We do see some scope for this component being tweaked to provide a boost to growth going forward, but that is the focus of a future note.

So What?

- We believe that the intimate details of the household disposable income data hold the key to getting growth going. Chart 2 below shows the key contributions to % y/y PDI growth over the last 18 months. The most striking component to us is the property income paid component (which is essentially the mortgage interest burden). This is a significant source of untapped potential.
- It is no great surprise that the contribution from this component has been near-zero,

Chart 2: Key Contributions to Household Disposable Income



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since mortgage rates have hardly moved. However, even though Bank Rate is about as low as it can plausibly go, it is not impossible that mortgage rates could be pushed lower with a little gentle persuasion.

Chart 3: Average Mortgage Interest Rate Paid Minus Bank Rate

- More specifically, the average effective mortgage rate paid is currently around 300bp above Bank Rate (Chart 3). The former takes account of the interest rates attached to the stock of existing mortgages (across the spectrum of fixed, floating and SVRs).
- Immediately prior to the credit crunch, that spread was far too low — close to zero. In more normal times the spread was around 100-150bp. The current spread of 300bp is too high.
- We believe that the main pitfall of the Funding for Lending Scheme (FLS) is that it focuses on boosting new lending. It implicitly assumes that providing new loans will kick-start a chain reaction — with home purchases at the bottom of the ladder helping to get transactions going further up the ladder. This is wishful thinking.
- New lending represents a small fraction of the entire stock of loans. We believe that the Bank should be targeting the **stock** of existing loans. An old-fashioned interest rate cut used to help at least half of existing borrowers. This group would see their monthly mortgage outgoings immediately reduced. This would leave more spare cash in their bank account and they would usually spend that windfall. In the context of the PDI breakdown, this would be seen via a boost in the 'property income paid' component.
- Our view is that the FLS should be tweaked to address this. More specifically, the current FLS rewards mortgage providers with lower funding costs in return for extending new loans. We believe that FLS-mk2 should be hard-coded to offer reduced funding costs to mortgage providers in return for reducing their interest rates on legacy mortgages — particularly by reducing SVRs.

Short term gain…then what?

- The experience of the 2008-09 episode demonstrated that the powerful boost to disposable income growth from reduced mortgage rates was successful in supporting growth. However, the positive news did not last long. Part of that is likely because new shocks came along. The surge in inflation (associated with the VAT hike, higher oil and food price inflation) eroded household real disposable income growth. Similarly, peripheral jitters from the eurozone have also dented business and consumer confidence.
- Clearly the one-off boost to PDI ***growth*** will become exhausted at some point. Nonetheless, if the scheme is successful in supporting overall GDP growth, leading to steady hiring and supporting faster wage inflation, it stands a chance of kick-starting self-fulfilling growth. Put another way, the wages and salaries component of PDI should provide ongoing support to growth. Admittedly, there is an element this being an implicit assumption rather like our criticism of FLS-1. But it's got to be worth a try?

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Fall 2012 Strategy Update: Sticking With A Cyclical Bias For Q4

We increased our cyclical exposure in Q3 and are sticking to a pro-growth bias in Q4. Recovering ISM new orders along with improving earnings revisions underpin our equity-over-bond, cyclicals-over-defensive preference. See Exhibit 1 for asset mix and equity strategy signals. Based on our models, Canada, the Far East (excluding Japan), and LatAm are sporting visible improvements versus the S&P 500. Our short-term bias is the S&P/TSX over the S&P 500 (for the first time since 2010). In terms of TSX sector strategy, we are overweight Energy, Materials, Industrials, and Insurance.

The September manufacturing ISM came in at 51.5, its first "growth" signal since May 2012. More importantly, the New Orders/ Inventories spread now points to positive visibility throughout Q4. Equities and yields are biased higher should the pickup in new orders continue, setting the stage for another +5/+8% equity-to-bond outperformance (see Exhibit 2). The trend in forward earnings is also reversing and supports our pro-growth strategy bias. Revisions ratios (positive to total revisions) bottomed out earlier in July and the 50% sweet spot could be breached shortly.

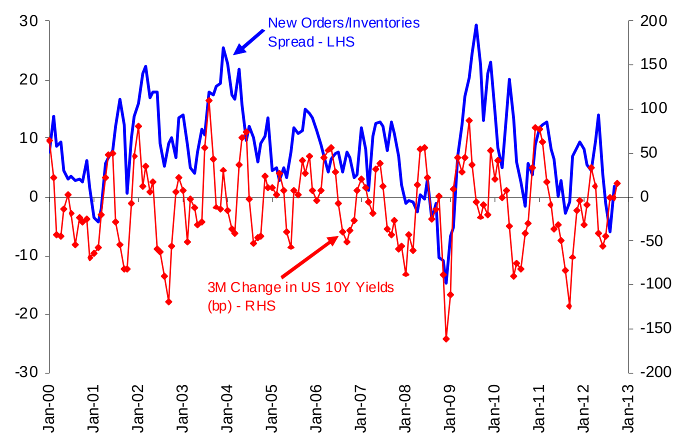
Exhibit 1: Tactical Asset Mix Signals

	Now	Trend	Q3-12	Q2-12	Q1-12	Q4-11
Equity vs. Bonds (U.S.)	+10%	+	+5%	+7%	+7%	+4%
Equity vs. Bonds (Canada)	+9%	+	-5%	-3%	+2%	+3%
Sector Strategy (S&P 500)						
Cyclical vs. Defensive Sectors	+7%	+	+1%	+2%	+5%	+7%
Global Equity						
Canada	OW	+	UW	UW	UW	UW
U.S.	MW	-	OW	OW	OW	OW
Europe (U.K./Germany)	OW	-	OW	OW	OW	OW
Far East	UW	+	UW	UW	MW	UW
LatAm	MW	+	UW	MW	OW	UW

Source: Scotiabank GBM estimates

In addition to recovering new orders and earnings revisions, positive U.S. housing and employment news flow could also support leadership from cyclical assets through Q4 and Q1. To be sure, the pace of U.S. employment gains remains muted, but the trend is picking up compared to the highly disappointing second quarter. The U.S economy added 114k new jobs in September and, more importantly, revisions for August (revised to +142k) and July (revised to +181k) highlight stronger payroll momentum. The unemployment rate dipped under 8% to 7.8%, which will make for soothing headlines and support household confidence. We have not seen any meaningful flows into equity funds in the last year (S&P500 is up 34% YOY), this could spark some asset mix shifts (retail flows).

Exhibit 2: New Orders/Inventories Spread vs. U.S. 10-Year Yield QOQ (2000-2012)



Source: Scotiabank GBM; Bloomberg.

P/Es expand and earnings revisions (finally) bottom

Q3's "risk-on" recovery has been driven mainly by P/E multiple expansion. The MSCI World AC forward P/E has moved up 1.4 points to 12.1x since May, which compares with +1.7 to 13.4x for the S&P/TSX, +1.3 to 13.1x

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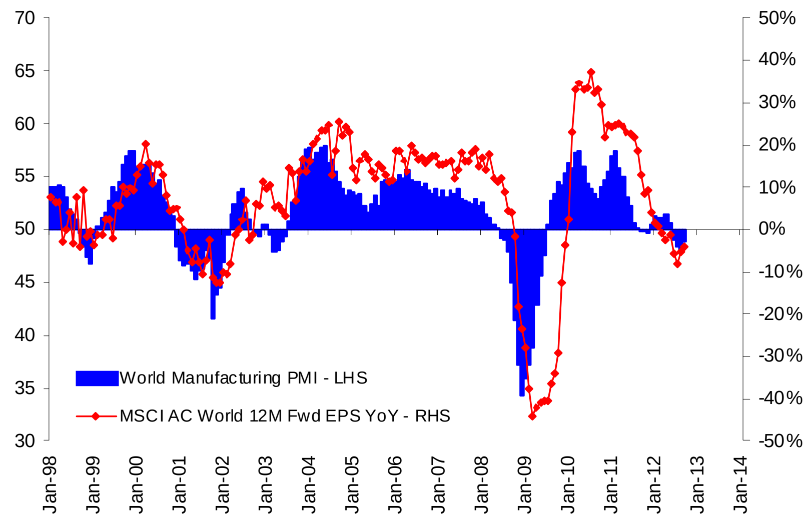
Exhibit 3: World PMI vs. MSCI AC World EPS (1998-2012)



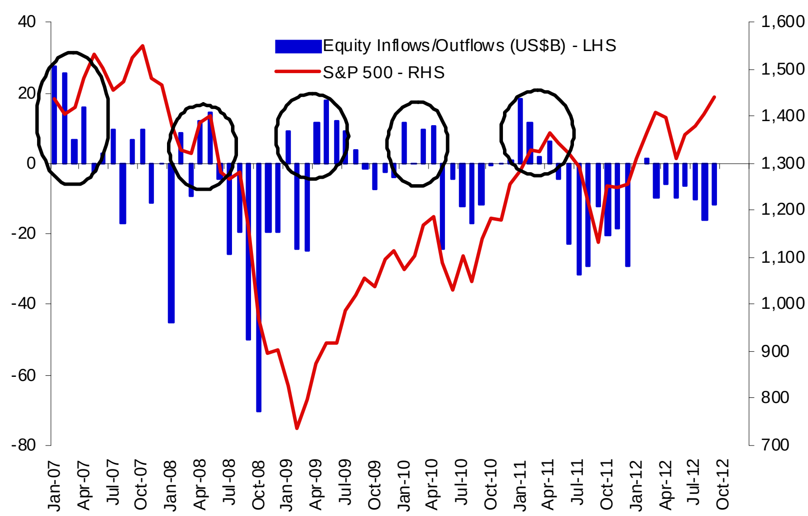
Source: Scotiabank GBM; Bloomberg; Thomson Financial.

for the S&P 500, +1.4 to 16.7x for the Bolsa, and +1.7 to 10.4x for the Bovespa. With the exception of Mexico, major equity benchmarks are still trading at discounts to their historical averages.

Negative earnings revisions plagued equity sentiment from mid-2011 to mid-2012, especially in Europe, LatAm, and Canada. More recently, however, the negative trend in forward earnings appears to have hit bottom. Risk appetite could be supported in the near term as the PMI recovers and earnings revisions turn positive. Rallying on P/E expansion is not sustainable, in our view, and improving forward earnings could extend the rally (see Exhibit 3).

Headline fears post-poning reallocation of flows

Exhibit 4: U.S. Equity Inflows/Outflows vs. S&P 500



Source: Scotiabank GBM, Thomson Financial, ICI.

Although equity markets have recovered since the June lows, sentiment remains shaky and flows are still missing in action. The S&P 500 hit a five-year high (1,466) earlier in September and the index is up over 30% year-over-year. Still, equity appetite is completely absent. According to ICI, U.S. equity mutual fund redemptions have been nearly constant since equities bottomed a year ago with 43 of the last 52 weeks recording equity outflows. Over the last 12 months, investors have pulled out US$136B from equity mutual funds and added US$266B to bond funds.

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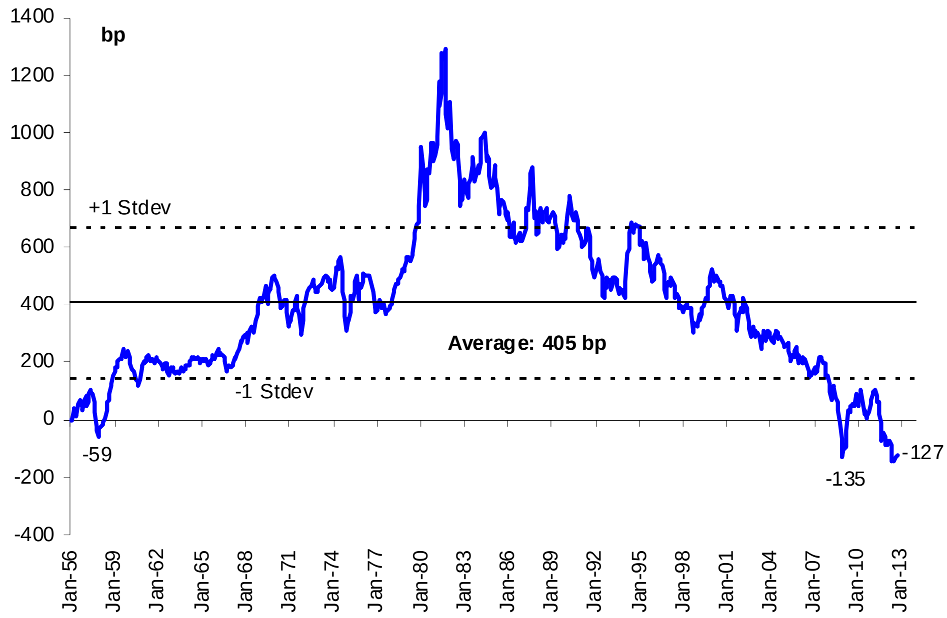
This marks a clear reversal from previous behaviour where flows would follow S&P 500 returns (see exhibit 4). In Canada, equity funds have suffered negative net sales of C$11.7B over the last year, lacking a positive month since March 2011. Headline fears and volatility are keeping many investors away from equities with flows still flocking the comfort of bonds. Longer term, the perceived safety and low volatility of bonds will hurt, in our opinion. In the near tern, the lack of positive equity flows could challenge the ongoing equity rally.

Relative Value: Equities versus bonds

Interest rate forecasts have proven highly frustrating in this post-2008 environment and record low yields have pushed equity relative valuations at the most attractive levels in 60 years. See Exhibit 5. Although a long term reversal should favour equities and dividends over government bonds, we do not expect this shift to occur in the near term. Hence, sporadic equity-to-bond leadership cycles are is likely to continue and tactical strategies should add value.

Exhibit 5: 10-Yr Bond Yields Less TSX Dividend Yield Spread



Avg LT Bond Yield up to 1989, 10-Yr Bond Yield Thereafter
Source: Scotiabank GBM, Thomson Financial, Bloomberg.

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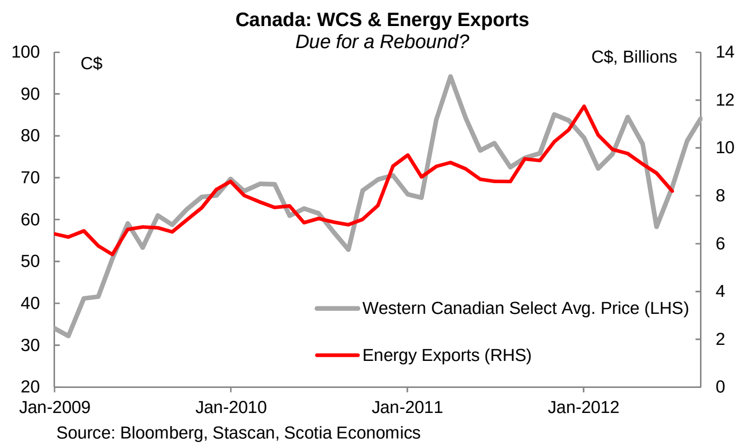
Key Data Preview

CANADA

Housing starts will be released on October 9, and Scotia is anticipating a 205k print. Our call is premised on weaker momentum in building permits, but we would note that the absolute level of permits is still tracking at fairly high levels (225k in May, 241k in June, 229k in July, 223k in August). Indeed, the level of building permits issued in May through July was the highest level issued over a three-month period since prior to the 2008 crisis — and included the highest level of permits for apartments or condos issued since 1981. Is Canada's housing market cooling down from this peak? On the one hand, data on existing home sales for September released last week showed that the rate of turnover in the Canadian housing market has slowed considerably, with Toronto and Vancouver both posting double-digit declines in existing home sales compared to September 2011. On the other hand, developers continue to apply for building permits at an elevated clip. The bottom line is that in all likelihood developers will eventually decide not to act on the permits that they have acquired due to slowing sales, and housing starts will level off in spite of an overwhelming permit backlog (and in defiance of economist models premised on building permits). When that will happen is an open question.

Canada's **international trade** data for August will be released on October 11 and Scotia is anticipating that the trade deficit will improve to -C$1.8bn from an all-time low in July, when it reached -C$2.34bn on a severe decline in exports. (What kind of celebration of 20 years of NAFTA is that?) Exports plummeted in July on weakness in both volumes and prices of crude (volumes -2%, total exports -8.5%) as Canadian distillate prices bottomed — but that wasn't the entire story. Machinery and equipment exports fell by 5.5%, exports of cars and parts fell by 5.3%, exports of aircraft fell by 19.6%... in short, the weakness was quite broad. We're expecting improvement in most of these sectors with US auto sales having been strong in September (implying that exports of parts and finished cars to the US increased in August), fuel prices having rebounded, etc. Moreover, the stronger Canadian dollar should have net positive effects as the trade balance is currently negative (i.e. a lower C$ haul from exports will hurt less than a lower C$ bill for imports helps). It's also worth noting that imports of crude oil fell by a corresponding amount to the decline in exports during July, so there is a possibility that a substitution of cheaper Canadian oil for more expensive foreign distillates is occurring.



UNITED STATES

US **trade balance** data for August will be released on October 11 and Scotia anticipates that the deficit will widen to -US$43.9bn from -US$42bn in July, mostly on higher fuel prices, but also a result of weaker exports of cars and weaker global demand for capital goods exports. The level of the USD on a DXY basis was also lower by 1% on average during August compared to July, so that should result in a weaker trade balance as the US is a net importer. Retail sales were fairly weak, which could imply lower imports of consumer goods. The wild card is the volume of crude imports. Higher crude production in the US has resulted in growing crude inventories and lower prices for some US distillates, but the biggest effects are likely to be felt in terms of US imports of crude as domestic production substitutes for pricier foreign oil that trades at world prices (this speaks more to crude priced using Brent than Western Canadian crude priced using WCS). Crude imports are the biggest drag on the US trade balance, with July's US$17.1bn net oil deficit accounting for 41% of the US trade deficit. That said, another way of thinking about the trade deficit is that the structural import bias still accounts for the other 59% of the trade deficit, so while net energy independence would improve the trade deficit, it wouldn't eliminate it by any stretch.

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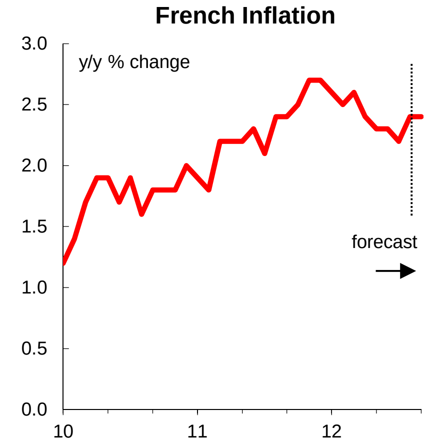
EUROPE

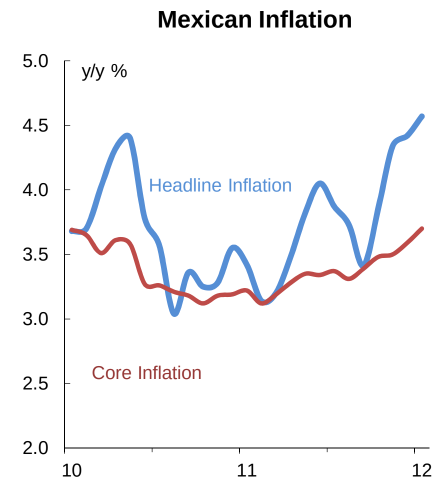
We look for French headline inflation to remain stable in September on a yearly basis at 2.4%, despite the prospect of reaccelerating core price pressures. This would be consistent with a flat reading on a monthly basis. Due to a shift in the summer sale period as compared to last year, the upward impact of the end of the sale period in the textile sector will likely continue to play in the September report, which explains our expectation for an upward movement in core inflation. On the other hand, this move is likely to be offset by the recent drop in energy prices (around -0.8% m/m) thanks to a fall in fuel costs. Indeed, the impact of falling Brent prices since the August peak was, in the case of France, boosted by the 6–euro cent cut in taxes on gasoline. While this factor is not expected to have a huge impact, it could contribute to lower headline inflation by close to 0.1% m/m in September. Finally, we do not discount the risk of seeing further softness in food prices, a spillover from the fall in fresh food prices seen in the August report. Indeed, available September data in Germany in particular pointed to easing year-over-year trend. We look for French food prices to rise only 0.1% m/m with the y/y rate easing to 2.3% from 2.4%.



Source: Bloomberg, Scotia Economics.

LATIN AMERICA

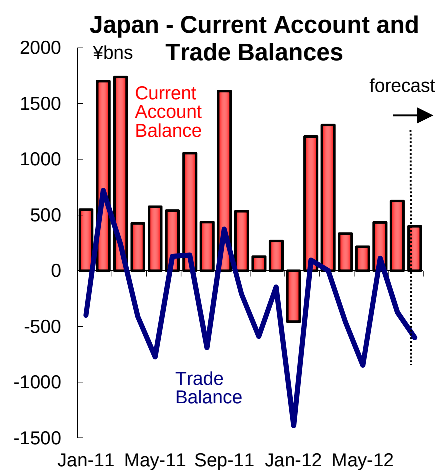
As a result of higher global food prices and a strong local economic performance, inflation in Mexico has been accelerating from 3.8% y/y in May to 4.6% y/y in August. This performance has also been a result of extremely low prices a year before and the likely pass-through effect from Mexican peso depreciation months ago. We anticipate that the September headline inflation figure, to be released on October 9th, will continue to be above the central bank's tolerance range of 3% ± 1%, reaching 4.8% y/y. However, we do not expect any adjustment on the monetary policy stance, as the contributing factors are seen as temporary and recent currency strength should offset price pressures. Core inflation has also increased but at a slower pace, moving from 3.5% y/y in May to 3.7% in August. We expect core inflation to remain below the official range until year-end.



Source: Thomson Reuters.

ASIA

Sluggish global demand for Japanese exports will be reflected in Japan's current account and trade balance data, scheduled for release on October 8th. Japanese exports decreased by 0.7% y/y in the January-August period, while the nation's imports increased by 5.0% in the same period, resulting in a widening trade deficit, estimated at around ¥600 billion in August. Elevated demand for imported goods in Japan reflects continuing post-tsunami/earthquake reconstruction efforts as well as the increased need for energy imports following the closure of most nuclear power plants. The widening of the trade shortfall translates into a smaller current account surplus, estimated at around ¥400 billion in August. Nonetheless, a large surplus on the income account — resulting from earnings from overseas direct and portfolio investments — maintains a positive balance on the current account, equivalent to around 1⅓% of GDP in 2012, compared with 2.1% of GDP in 2011.



Source: Bloomberg, Scotia Economics.

Key Indicators for the week of October 8 - 12

North America

Country	Date	Time	Indicator	Period	BNS	Consensus	Latest
CA	10/09	08:10	Housing Starts (000s a.r.)	Sep	205.0	207.5	223.8
MX	10/09	09:00	Consumer Prices (m/m)	Sep	0.48	0.48	0.30
MX	10/09	09:00	Consumer Prices (y/y)	Sep	4.80	4.81	4.57
MX	10/09	09:00	Consumer Prices Core (m/m)	Sep	0.33	0.24	0.22
US	10/10	07:00	MBA Mortgage Applications (w/w)	OCT 5	--	--	16.6
MX	10/10	09:00	Trade Balance (US$ mn)	Aug F	--	--	-979.2
US	10/10	10:00	Wholesale Inventories (m/m)	Aug	--	0.4	0.7
US	10/11	07:59	Treasury Budget ($ bn)	Sep	--	-2.0	-190.5
CA	10/11	08:30	Merchandise Trade Balance (C$ bn)	Aug	-1.8	-1.9	-2.3
CA	10/11	08:30	New Housing Price Index (m/m)	Aug	--	0.1	0.1
US	10/11	08:30	Initial Jobless Claims (000s)	OCT 6	--	365	367
US	10/11	08:30	Continuing Claims (000s)	SEP 29	--	3279	3281
US	10/11	08:30	Trade Balance ($ bn)	Aug	-43.9	-44.0	-42.0
US	10/12	08:30	PPI (m/m)	Sep	0.6	0.7	1.7
US	10/12	08:30	PPI ex. Food & Energy (m/m)	Sep	0.2	0.2	0.2
MX	10/12	09:00	Industrial Production (m/m)	Aug	--	0.2	0.5
MX	10/12	09:00	Industrial Production (y/y)	Aug	3.6	3.8	4.9
US	10/12	09:55	U. of Michigan Consumer Sentiment	Oct P	78.0	77.9	78.3

Europe

Country	Date	Time	Indicator	Period	BNS	Consensus	Latest
GE	10/08	02:00	Current Account (€ bn)	Aug	--	11.9	12.8
GE	10/08	02:00	Trade Balance (€ bn)	Aug	--	15.2	16.9
GE	10/08	06:00	Industrial Production (m/m)	Aug	-1.1	-0.6	1.3
FR	10/09	02:45	Central Government Balance (€ bn)	Aug	--	--	-85.5
FR	10/09	02:45	Trade Balance (€ mn)	Aug	--	-5000	-4271
UK	10/09	04:30	Industrial Production (m/m)	Aug	-0.7	-0.5	2.9
UK	10/09	04:30	Manufacturing Production (m/m)	Aug	-1.0	-0.7	3.2
UK	10/09	04:30	Visible Trade Balance (£ mn)	Aug	-8000	-8500	-7149
FR	10/10	02:45	Industrial Production (m/m)	Aug	-0.8	-0.3	0.2
FR	10/10	02:45	Manufacturing Production (m/m)	Aug	-0.8	-0.7	0.9
IT	10/10	04:00	Industrial Production (y/y)	Aug	--	-9.7	-7.3
GE	10/11	02:00	CPI (y/y)	Sep F	2.0	2.0	2.0
GE	10/11	02:00	CPI - EU Harmonized (m/m)	Sep F	0.0	0.0	0.0
GE	10/11	02:00	CPI - EU Harmonized (y/y)	Sep F	2.1	2.1	2.1
FR	10/11	02:45	CPI (y/y)	Sep	2.1	2.2	2.1
FR	10/11	02:45	CPI - EU Harmonized (m/m)	Sep	0.0	0.0	0.7
FR	10/11	02:45	CPI - EU Harmonized (y/y)	Sep	2.4	2.4	2.4
SP	10/11	03:00	CPI (y/y)	Sep F	3.5	3.5	3.5
SP	10/11	03:00	CPI - EU Harmonized (m/m)	Sep	2.0	2.0	0.5
SP	10/11	03:00	CPI - EU Harmonized (y/y)	Sep F	3.5	3.5	3.5
FR	10/12	02:45	Current Account (€ bn)	Aug	--	--	-2.5
IT	10/12	04:00	CPI (y/y)	Sep F	3.2	3.2	3.2
IT	10/12	04:00	CPI - EU Harmonized (m/m)	Sep F	2.1	2.1	2.1
IT	10/12	04:00	CPI - EU Harmonized (y/y)	Sep F	3.4	3.4	3.4
EC	10/12	05:00	Industrial Production (m/m)	Aug	--	-0.4	0.5

Forecasts at time of publication.
Source: Bloomberg, Scotia Economics.

Key Indicators for the week of October 8 - 12

Asia Pacific

Country	Date	Time	Indicator	Period	BNS	Consensus	Latest
TA	10/08	04:00	Exports (%)	Sep	--	1.0	-4.2
TA	10/08	04:00	Imports (%)	Sep	--	-3.6	-7.6
TA	10/08	04:00	Trade Balance (US$ bn)	Sep	--	2.5	3.3
JN	10/08	19:50	Current Account (¥ bn)	Aug	400	421.1	625.4
JN	10/08	19:50	Trade Balance - BOP Basis (¥ bn)	Aug	-600	-628.6	-373.6
JN	10/09	01:00	Eco Watchers Survey (current)	Sep	--	--	43.6
JN	10/09	01:00	Eco Watchers Survey (outlook)	Sep	--	--	43.6
PH	10/09	21:00	Exports (y/y)	Aug	--	7.3	6.0
JN	10/10	02:00	Machine Tool Orders (y/y)	Sep P	--	--	-2.7
JN	10/10	19:50	Bank Lending (y/y)	Sep	--	--	0.9
JN	10/10	19:50	Machine Orders (m/m)	Aug	--	-2.3	4.6
SK	10/10	21:00	**BoK Base Rate (%)**	Oct 11	**2.75**	**2.75**	**3.00**
AU	10/10	21:30	Employment (000s)	Sep	--	5.0	-8.8
AU	10/10	21:30	Unemployment Rate (%)	Sep	5.2	5.3	5.1
JN	10/11	01:00	Consumer Confidence	Sep	--	--	40.5
CH	10/11	07:59	Foreign Reserves (US$ bn)	Sep	--	3228	3240
CH	10/11	07:59	New Yuan Loans (bn)	Sep	--	680.0	703.9
ID	10/11	07:59	**BI Reference Interest Rate (%)**	Oct 11	**5.75**	**5.75**	**5.75**
NZ	10/11	07:59	REINZ Housing Price Index (m/m)	Sep	--	--	1.3
JN	10/11	19:50	Tertiary Industry Index (m/m)	Aug	--	0.4	-0.8

Latin America

Country	Date	Time	Indicator	Period	BNS	Consensus	Latest
CL	10/06	07:00	CPI (y/y)	Sep	--	2.7	2.6
CL	10/06	08:00	CPI (m/m)	Sep	--	0.6	0.2
BZ	10/10	07:59	Economic Activity Index SA (m/m)	Aug	--	0.8	0.4
BZ	10/10	07:59	Economic Activity Index NSA (y/y)	Aug	--	2.4	2.3
BZ	10/10	07:59	**SELIC Target Rate (%)**	Oct 10	**7.25**	**7.50**	**7.50**
BZ	10/11	08:00	Retail Sales (m/m)	Aug	--	0.3	1.4
BZ	10/11	08:00	Retail Sales (y/y)	Aug	--	9.1	7.1
PE	10/11	19:00	**Reference Rate (%)**	Oct	**4.25**	**4.25**	**4.25**
PE	10/12	06:59	Trade Balance (PEN mn)	Aug	--	--	-192.1

Forecasts at time of publication.
Source: Bloomberg, Scotia Economics.

Global Auctions for the week of October 8 - 12

North America

Country	Date	Time	Event
CA	10/09	10:30	Canada to Sell CAD7.4 Bln 98-Day Bills
CA	10/09	10:30	Canada to Sell CAD2.8 Bln 168-Day Bills
CA	10/09	10:30	Canada to Sell CAD2.8 Bln 350-Day Bills
US	10/09	11:00	U.S. Fed to Purchase USD1.75-2.25 Bln Notes
US	10/09	11:30	U.S. to Sell USD32 Bln 3-Month Bills
US	10/09	11:30	U.S. to Sell USD28 Bln 6-Month Bills
US	10/09	13:00	U.S. to Sell USD32 Bln 3-Year Notes
US	10/10	11:00	U.S. Fed to Sell USD7.00-8.00 Bln Notes
US	10/10	11:30	U.S. to Sell 4-Week Bills
CA	10/10	12:00	Canada to Sell 3 Year Notes
US	10/10	13:00	U.S. to Sell USD21 Bln 10-Year Notes Reopening
US	10/11	11:00	U.S. Fed to Purchase USD0.75-1.25 Bln Notes
US	10/11	13:00	U.S. to Sell USD13 Bln 30-Year Bonds Reopening
US	10/12	11:00	U.S. Fed to Purchase USD1.75-2.25 Bln Notes

Europe

Country	Date	Time	Event
NO	10/08	05:10	Norway to Sell NOK3 Bln 5% 2015 Bonds
GE	10/08	05:30	Germany to Sell EU4 Bln 6-Mth Bills
FR	10/08	09:00	France to Sell Bills (BTF)
NE	10/09	04:00	Netherlands to Sell Up to EUR2.5 Bln 2018
DE	10/09	04:30	Denmark to Sell Bonds
GR	10/09	05:00	Greece to Sell Bills
SZ	10/09	05:30	Switzerland to Sell 6-Month Bills
UK	10/09	05:30	U.K. to Sell GBP1.75 Bln 4.25% 2032 Bonds
IT	10/10	05:00	Italy to Sell Bills
SW	10/10	05:03	Sweden to Sell Treasury Bills
SZ	10/10	05:30	Switzerland to Sell Bonds
GE	10/10	05:30	Germany to Sell Add'l EU4 Bln 5-Year Notes
IT	10/11	05:00	Italy to Sell Bonds/Floating/Zero Coupon
SW	10/11	05:03	Sweden to Sell Inflation-Linked Bonds
UK	10/11	05:30	U.K. to Sell GBP1.5 Bln 0.125% I/L 2024 Bonds
BE	10/12	06:00	Belgium to Sell Bonds (OLO ORI)

Asia Pacific

Country	Date	Time	Event
CH	10/09	23:00	China to Sell 7-Year Bonds
JN	10/09	23:35	Japan to Sell 2-Month Bills
JN	10/10	23:35	Japan to Sell 3-Month Bills
JN	10/10	23:45	Japan to Sell 30-Year Bonds

Latin America

Country	Date	Time	Event
BZ	10/09	11:00	Brazil to Sell I/L Bonds due 8/15/2016 - NTN-B
BZ	10/09	11:00	Brazil to Sell I/L Bonds due 8/15/2018 - NTN-B
BZ	10/09	11:00	Brazil to Sell I/L Bonds due 8/15/2022 - NTN-B
BZ	10/09	11:00	Brazil to Sell I/L Bonds due 8/15/2030 - NTN-B
BZ	10/09	11:00	Brazil to Sell I/L Bonds due 8/15/2040 - NTN-B
BZ	10/09	11:00	Brazil to Sell I/L Bonds due 8/15/2050 - NTN-B
BZ	10/11	10:00	Brazil to Sell Bills due 10/1/2013 - LTN
BZ	10/11	10:00	Brazil to Sell Bills due 4/1/2015 - LTN
BZ	10/11	10:00	Brazil to Sell Bills due 7/1/2016 - LTN
BZ	10/11	10:00	Brazil to Sell Floating-rate Notes due 3/1/2018 - LFT

Source: Bloomberg, Scotia Economics.

Events for the week of October 8 - 12

North America

Country	Date	Time	Event
US	10/08	20:00	IMF Releases World Economic Outlook
US	10/08	21:30	International Monetary Fund Releases Fiscal Monitor
US	10/09	20:00	IMF Releases Portions of Global Financial Stability Report
US	OCT 9-10		U.S. Treasury Secretary Geithner Visits India
US	10/10	14:00	Fed Releases Beige Book Economic Survey
US	10/10	14:45	Fed's Kocherlakota Speaks to Businesses in Montana
US	10/10	16:45	Dallas Fed's Richard Fisher Speaks at Cato Conference
US	10/11	12:30	Fed's Plosser Speaks on Economy in Pennsylvania
US	10/11	20:00	Fed's Bullard Speaks on U.S. Economy in St. Louis
US	10/12	12:35	Fed's Lacker Speaks on Economy in Charlottesville, VA

Europe

Country	Date	Time	Event
IT	OCT 5-6		Italian Prime Minister Monti Meets Leaders in Malta
FI	10/06	03:05	EU's Rehn Speaks in Interview on Finnish TV1
EC	10/06	08:00	EU's Rehn Speaks to Finnish Womens' Business Group in Helsinki
UK	OCT 7-10		Conservative Party Conference in Birmingham
NO	10/08	04:00	Norway Releases Fiscal Budget for 2013
PO	10/08	06:00	Portugal Releases Industrial Sales, Employment Report
EC	10/08	07:15	EU's Reichenbach Speaks on Greece at Brussels Think Tank
IT	10/08	10:00	Monti Meets Germany's SPD President Gabriel in Rome
EC	10/08	11:00	Euro-Area Finance Ministers Meet in Luxembourg
PO	10/08		Bank of Portugal Releases Data on Banks
GE	OCT 8-9		Joint ECB & Fed Conference on Bank Funding in Germany
EC	OCT 8-9		The Economist EU Presidency Summit Takes Place in Cyprus
EC	10/09	03:00	EU Finance Ministers Meet in Luxembourg
IT	10/09	09:00	Italy's Monti, Enel's Conti Attend Event in Rome
UK	10/09	13:30	King Delivers Stamp Lecture at London School of Economics
EC	10/09	18:00	ECB's Weidmann, Praet Speak at Bundesbank Cash Symposium
FR	10/09		OECD Secretary-General Gurria Speaks at High-Level Seminar
EC	OCT 9-10		NATO Defense Ministers Hold Meeting in Brussels
EC	10/10	03:00	EU Parliament Panel Debates Banking Union Proposals
SP	10/10	03:45	Bank of Spain Chief Economist Malo de Molina Speaks
UK	10/10	06:15	Cameron Speaks at Conservative Party Conference
EC	10/10	07:30	EU Issues Reports on Turkey, Iceland, Serbia, Other Candidates
EC	10/10	09:00	EU's Barnier Speaks at Lisbon Council Conference in Brussels
EC	10/11	03:00	Van Rompuy, Barroso, Monti Speak at Brussels Think Tank
EC	10/11	04:00	ECB Publishes Oct. Monthly Report
GE	10/11	05:00	German Institutes Gives Joint Economic Outlook
EC	10/11	13:00	Italy's Monti at Friends of Europe Dinner in Brussels

Source: Bloomberg, Scotia Economics.

Events for the week of October 8 - 12

Asia Pacific

Country	Date	Time	Event
AU	10/07	19:00	RBA's Stevens, Ex-Deputy Battellino Before Parliamentary Panel
IN	10/08	01:30	Finance Minister Chidambaram at Economic Editors Conference
NZ	10/08	17:00	NZIER Publishes Quarterly Survey of Business Opinion
NZ	10/08	19:00	Quotable Value NZ House Price Inflation Report
AU	10/08	21:00	RBA's Lowe Speaks at Financial Services Luncheon in Tasmania
IN	10/09	00:30	Geithner, Chidambaram at India-U.S. Eco Partnership Meeting
JN	10/09	09:00	IMF Releases Growth Forecasts, Gives Press Conference in Tokyo
JN	10/09	10:30	IMF Releases fiscal monitor report and gives press conference
NZ	10/09	18:30	New Zealand Government Full-Year Financial Statements
US	10/09	20:00	IMF Releases Portions of Global Financial Stability Report
US	OCT 9-10		U.S. Treasury Secretary Geithner Visits India
IN	10/10	07:00	91 Day T-Bill Cutoff Yield
JN	10/10	09:00	IMF Releases Global Financial Stability Report in Tokyo
NZ	10/10	17:30	Business NZ Publishes Performance of Manufacturing Index
NZ	10/10	17:45	Statistics New Zealand on Food Prices
AU	10/10	19:25	RBA's Ellis Speaks at University of Technology in Sydney
NZ	10/10	20:00	ANZ-Roy Morgan Consumer Confidence Survey
SK	10/10	21:00	Bank of Korea Base Rate
ID	OCT 10-11		Bank Indonesia Reference Rate
NZ	10/11	22:00	Foreign Holdings of New Zealand Government Bonds
JN	OCT 11-14		IMF, World Bank Group Annual and Spring Meetings

Latin America

Country	Date	Time	Event
BZ	10/07	07:00	Brazil Municipal Elections
VZ	10/07		Venezuela Holds Presidential Election
CL	10/10	07:30	Central Bank's Traders Survey
CL	10/10	08:30	Central Bank Economist Survey
BZ	10/10		SELIC Target - Central Bank
PE	10/11	19:00	Reference Rate

Source: Bloomberg, Scotia Economics.

Global Central Bank Watch

North America

Rate	Current Rate	Next Meeting	Scotia's Forecasts	Consensus Forecasts
Bank of Canada – Overnight Target Rate	1.00	October 23, 2012	1.00	--
Federal Reserve – Federal Funds Target Rate	0.25	October 24, 2012	0.25	--
Banco de México – Overnight Rate	4.50	October 26, 2012	4.50	--

BoC: a) Weak incoming economic data (including GDP tracking at 1% q/q SAAR in July), b) slowing housing markets signalled by the decreasing pace of resale activity in Toronto & Vancouver, and c) the current easing from the Fed, are cause to expect the BoC to moderate the hawkish bias in its recent communications while maintaining its conditional pledge to increase rates when economic conditions normalize. We see a decent possibility of a relatively dovish MPR on Oct. 24. We don't expect September's volatile increase in jobs to change the outlook and continue to expect the Bank of Canada to hold its overnight rate at 1% through our published forecast horizon. Fed: Minutes from the FOMC's Sept. 13 meeting did not shed light on whether the FOMC will or will not add Treasury purchases to its open-ended asset purchase program. We continue to expect QE3 to run through 2012 and quite likely at least into mid-2013.

Europe

Rate	Current Rate	Next Meeting	Scotia's Forecasts	Consensus Forecasts
European Central Bank – Refinancing Rate	0.75	November 8, 2012	0.75	--
Bank of England – Bank Rate	0.50	November 8, 2012	0.50	0.50
Swiss National Bank – Libor Target Rate	0.00	December 13, 2012	0.00	--
Central Bank of Russia – Refinancing Rate	8.25	November 9, 2012	8.25	--
Hungarian National Bank – Base Rate	6.50	October 30, 2012	6.75	--
Central Bank of the Republic of Turkey – 1 Wk Repo Rate	5.75	October 18, 2012	5.75	--
Sweden Riksbank – Repo Rate	1.25	October 25, 2012	1.50	--
Norges Bank – Deposit Rate	1.50	October 31, 2012	1.50	--

Asia Pacific

Rate	Current Rate	Next Meeting	Scotia's Forecasts	Consensus Forecasts
Bank of Japan – Target Rate	0.10	October 30, 2012	0.10	--
Reserve Bank of Australia – Cash Target Rate	3.25	November 5, 2012	3.25	3.00
Reserve Bank of New Zealand – Cash Rate	2.50	October 24, 2012	2.50	--
People's Bank of China – Lending Rate	6.00	TBA	--	--
Reserve Bank of India – Repo Rate	8.00	October 30, 2012	8.00	--
Bank of Korea – Bank Rate	3.00	October 10, 2012	2.75	2.75
Bank of Thailand – Repo Rate	3.00	October 17, 2012	3.00	--
Bank Indonesia – Reference Interest Rate	5.75	October 11, 2012	5.75	5.75

South Korean monetary authorities will likely ease monetary conditions following the next policy meeting on October 10th, lowering the benchmark interest rate by 25 basis points to 2.75%. Economic momentum in South Korea is weakening as domestic demand and export sector performance continue to deteriorate. Meanwhile, inflationary pressures remain low; the headline consumer price index increased by 2.0% y/y in September, comfortably within the Bank of Korea's 2-4% target range. We expect that Bank Indonesia will maintain its current monetary policy following the next meeting on October 11th.

Latin America

Rate	Current Rate	Next Meeting	Scotia's Forecasts	Consensus Forecasts
Banco Central do Brasil – Selic Rate	7.50	October 10, 2012	7.25	7.50
Banco Central de Chile – Overnight Rate	5.00	October 18, 2012	5.00	--
Banco de la República de Colombia – Lending Rate	4.75	October 26, 2012	4.75	--
Banco Central de Reserva del Perú – Reference Rate	4.25	October 11, 2012	4.25	4.25

We anticipate that the Central Bank of Peru will leave the interest rate unchanged at 4.25% for the 17th consecutive meeting. Inflation remains well above the official tolerance range; after the deceleration observed in July, headline inflation resumed its upward trend, reaching 3.7% y/y in August. We maintain our view that the easing cycle of the central bank of Brazil is coming to an end after more than a year of rate cuts. We anticipate another possible cut of 25 basis points, bringing the reference rate to 7.25% for the remainder of the year. After several months of decelerating inflation, headline inflation has slowly resumed its upward trend, accelerating to 5.3% y/y in September.

Africa

Rate	Current Rate	Next Meeting	Scotia's Forecasts	Consensus Forecasts
South African Reserve Bank – Repo Rate	5.00	November 22, 2012	5.00	--

Forecasts at time of publication.
Source: Bloomberg, Scotia Economics.

Forecasts as at September 27, 2012*	2000-10	2011	2012f	2013f	2000-10	2011	2012f	2013f
Output and Inflation (annual % change)		Real GDP				Consumer Prices[2]		
World[1]	3.7	4.0	3.1	3.3				
Canada	2.2	2.4	1.9	1.8	2.1	2.9	1.7	2.0
United States	1.8	1.8	2.1	1.9	2.5	3.1	2.1	2.2
Mexico	2.1	4.2	3.9	3.6	4.9	3.8	4.2	4.0
United Kingdom	2.0	0.7	-0.3	1.2	2.1	4.2	2.3	3.0
Euro Zone	1.4	1.5	-0.7	0.2	2.1	2.7	2.4	2.0
Japan	0.9	-0.7	2.3	1.5	-0.3	-0.2	0.1	0.1
Australia	3.1	2.1	3.2	3.1	3.1	3.1	2.6	2.8
China	9.4	9.3	7.8	8.2	2.3	4.1	2.7	3.5
India	7.5	10.0	5.7	6.3	6.4	7.7	8.0	7.0
South Korea	4.6	3.6	2.8	3.5	3.1	4.8	2.2	3.0
Thailand	4.4	0.1	5.0	4.0	2.7	3.5	3.3	3.6
Brazil	3.7	2.7	1.7	3.8	6.6	6.5	5.0	5.5
Chile	4.6	6.1	5.2	5.2	3.4	4.4	2.1	2.9
Peru	5.5	7.0	6.3	5.7	2.4	4.7	3.0	3.0

Central Bank Rates (%, end of period)	12Q1	12Q2	12Q3f	12Q4f	13Q1f	13Q2f	13Q3f	13Q4f
Bank of Canada	1.00	1.00	1.00	1.00	1.00	1.00	1.00	1.00
Federal Reserve	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25
European Central Bank	1.00	1.00	0.75	0.75	0.75	0.75	0.75	0.75
Bank of England	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50
Swiss National Bank	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00
Bank of Japan	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10
Reserve Bank of Australia	3.75	3.50	3.50	3.25	3.25	3.25	3.50	3.50
Exchange Rates (end of period)								
Canadian Dollar (USDCAD)	1.00	1.02	0.98	0.96	0.96	0.96	0.97	0.97
Canadian Dollar (CADUSD)	1.00	0.98	1.02	1.04	1.04	1.04	1.03	1.03
Euro (EURUSD)	1.33	1.27	1.29	1.26	1.24	1.23	1.22	1.21
Sterling (GBPUSD)	1.60	1.57	1.62	1.62	1.62	1.63	1.64	1.64
Yen (USDJPY)	83	80	78	80	84	85	86	87
Australian Dollar (AUDUSD)	1.03	1.02	1.04	1.04	1.05	1.05	1.06	1.06
Chinese Yuan (USDCNY)	6.3	6.4	6.3	6.3	6.3	6.2	6.2	6.1
Mexican Peso (USDMXN)	12.8	13.4	12.9	12.8	12.9	12.8	12.9	13.2
Brazilian Real (USDBRL)	1.83	2.01	2.03	1.99	1.98	1.95	1.90	1.86

Commodities (annual average)	2000-10	2011	2012f	2013f
WTI Oil (US$/bbl)	54	95	95	100
Brent Oil (US$/bbl)	52	112	112	112
Nymex Natural Gas (US$/mmbtu)	5.81	4.03	2.75	3.00
Copper (US$/lb)	1.93	4.00	3.65	3.50
Zinc (US$/lb)	0.75	0.99	0.89	1.02
Nickel (US$/lb)	7.36	10.38	7.85	7.80
Gold, London PM Fix (US$/oz)	586	1,569	1,690	1,800
Pulp (US$/tonne)	694	977	880	900
Newsprint (US$/tonne)	575	640	640	660
Lumber (US$/mfbm)	273	255	285	315

[1] World GDP for 2000-10 are IMF PPP estimates; 2011-13f are Scotia Economics' estimates based on a 2010 PPP-weighted sample of 38 countries.

[2] CPI for Canada and the United States are annual averages. For other countries, CPI are year-end rates.

* See Scotia Economics 'Global Forecast Update' (http://www.gbm.scotiabank.com/English/bns_econ/forecast.pdf) for additional forecasts & commentary.

North America

Canada	2011	12Q1	12Q2	Latest	
Real GDP (annual rates)	2.4	1.8	1.8		
Current Acc. Bal. (C$B, ar)	-48.4	-40.6	-64.1		
Merch. Trade Bal. (C$B, ar)	2.3	8.4	-13.9	-28.0	(Jul)
Industrial Production	3.5	0.9	2.6	1.9	(Jul)
Housing Starts (000s)	193	206	230	224	(Aug)
Employment	1.6	0.9	1.2	1.1	(Sep)
Unemployment Rate (%)	7.5	7.4	7.3	7.4	(Sep)
Retail Sales	4.1	4.3	2.6	3.0	(Jul)
Auto Sales (000s)	1589	1703	1670	1615	(Jul)
CPI	2.9	2.3	1.6	1.2	(Aug)
IPPI	4.6	1.8	0.6	0.3	(Aug)
Pre-tax Corp. Profits	15.4	4.2	0.4		

United States	2011	12Q1	12Q2	Latest	
Real GDP (annual rates)	1.8	2.0	1.3		
Current Acc. Bal. (US$B, ar)	-466	-534	-470		
Merch. Trade Bal. (US$B, ar)	-738	-777	-743	-687	(Jul)
Industrial Production	4.1	4.0	4.9	3.1	(Aug)
Housing Starts (millions)	0.61	0.71	0.74	0.75	(Aug)
Employment	1.1	1.6	1.3	1.4	(Sep)
Unemployment Rate (%)	9.0	8.3	8.2	7.8	(Sep)
Retail Sales	8.3	6.4	4.3	4.4	(Aug)
Auto Sales (millions)	12.7	14.1	14.1	14.9	(Sep)
CPI	3.2	2.8	1.9	1.7	(Aug)
PPI	6.0	3.4	1.1	2.0	(Aug)
Pre-tax Corp. Profits	2.1	18.0	14.6		

Mexico	2011	12Q1	12Q2	Latest	
Real GDP	3.9	4.5	4.1		
Current Acc. Bal. (US$B, ar)	-11.1	4.7	1.8		
Merch. Trade Bal. (US$B, ar)	-1.5	7.1	6.1	-11.8	(Aug)
Industrial Production	4.0	4.4	3.7	4.9	(Jul)
CPI	3.4	3.9	3.9	4.6	(Aug)

Europe

Euro Zone	2011	12Q1	12Q2	Latest	
Real GDP	1.5	-0.1	-0.5		
Current Acc. Bal. (US$B, ar)	-3	-32	79	235	(Jul)
Merch. Trade Bal. (US$B, ar)	6.9	28.0	128.6	183.9	(Jul)
Industrial Production	3.5	-1.7	-2.4	-2.7	(Jul)
Unemployment Rate (%)	10.1	10.8	11.2	11.4	(Aug)
CPI	2.7	2.7	2.5	2.6	(Aug)

Germany	2011	12Q1	12Q2	Latest	
Real GDP	3.1	1.2	1.0		
Current Acc. Bal. (US$B, ar)	202.6	215.8	192.1	189.3	(Jul)
Merch. Trade Bal. (US$B, ar)	216.2	223.3	245.2	237.4	(Jul)
Industrial Production	8.0	0.7	-0.3	-1.4	(Jul)
Unemployment Rate (%)	7.1	6.8	6.8	6.8	(Sep)
CPI	2.3	2.2	1.9	2.0	(Sep)

France	2011	12Q1	12Q2	Latest	
Real GDP	1.7	0.4	0.3		
Current Acc. Bal. (US$B, ar)	-54.5	-50.6	-77.0	-6.1	(Jul)
Merch. Trade Bal. (US$B, ar)	-51.9	-54.4	-55.8	-41.7	(Jul)
Industrial Production	1.9	-1.8	-2.1	-3.1	(Jul)
Unemployment Rate (%)	9.7	10.0	10.3	10.6	(Aug)
CPI	2.1	2.3	2.0	2.1	(Aug)

United Kingdom	2011	12Q1	12Q2	Latest	
Real GDP	0.9	-0.1	-0.5		
Current Acc. Bal. (US$B, ar)	-46.4	-100.3	-128.6		
Merch. Trade Bal. (US$B, ar)	-160.3	-159.8	-177.6	-133.7	(Jul)
Industrial Production	-0.7	-2.8	-2.5	-0.8	(Jul)
Unemployment Rate (%)	8.1	8.2	8.1	8.1	(Jun)
CPI	4.5	3.5	2.7	2.5	(Aug)

Italy	2011	12Q1	12Q2	Latest	
Real GDP	0.5	-1.5	-2.6		
Current Acc. Bal. (US$B, ar)	-0.07	-0.07	-0.01	0.02	(Jul)
Merch. Trade Bal. (US$B, ar)	-34.2	-17.5	16.7	66.2	(Jul)
Industrial Production	0.3	-5.4	-7.8	-7.0	(Jul)
CPI	2.8	3.4	3.3	3.2	(Aug)

Russia	2011	12Q1	12Q2	Latest	
Real GDP	4.3	4.9	4.0		
Current Acc. Bal. (US$B, ar)	98.8	40.4	21.2		
Merch. Trade Bal. (US$B, ar)	16.5	19.7	16.7	11.1	(Jul)
Industrial Production	4.8	4.1	2.3	2.1	(Aug)
CPI	8.4	3.9	3.8	6.6	(Sep)

All data expressed as year-over-year % change unless otherwise noted.

Source: Bloomberg, Global Insight, Scotia Economics.

Asia Pacific

Australia	2011	12Q1	12Q2	Latest
Real GDP	2.1	4.4	3.7	
Current Acc. Bal. (US$B, ar)	-33.1	-61.6	-32.9	
Merch. Trade Bal. (US$B, ar)	35.7	1.4	28.0	-5.6 (Aug)
Industrial Production	-1.2	3.9	0.5	
Unemployment Rate (%)	5.1	5.2	5.1	5.1 (Aug)
CPI	3.4	1.6	1.2	

Japan	2011	12Q1	12Q2	Latest
Real GDP	-0.7	2.8	3.3	
Current Acc. Bal. (US$B, ar)	119.2	101.1	49.0	95.0 (Jul)
Merch. Trade Bal. (US$B, ar)	-33.2	-70.2	-73.2	-72.1 (Aug)
Industrial Production	-2.3	2.7	5.1	-4.3 (Aug)
Unemployment Rate (%)	4.6	4.5	4.4	4.2 (Aug)
CPI	-0.3	0.3	0.2	-0.5 (Aug)

South Korea	2011	12Q1	12Q2	Latest
Real GDP	3.6	2.8	2.3	
Current Acc. Bal. (US$B, ar)	26.5	10.2	44.8	28.3 (Aug)
Merch. Trade Bal. (US$B, ar)	30.8	5.5	37.8	37.8 (Sep)
Industrial Production	6.9	2.9	2.4	0.1 (Aug)
CPI	4.0	3.0	2.4	2.0 (Sep)

China	2011	12Q1	12Q2	Latest
Real GDP	10.4	8.1	7.6	
Current Acc. Bal. (US$B, ar)	201.7			
Merch. Trade Bal. (US$B, ar)	155.0	1.4	274.0	319.9 (Aug)
Industrial Production	12.8	11.9	9.5	8.9 (Aug)
CPI	4.1	3.6	2.2	2.0 (Aug)

Thailand	2011	12Q1	12Q2	Latest
Real GDP	0.1	0.4	4.2	
Current Acc. Bal. (US$B, ar)	5.9	1.4	-2.4	
Merch. Trade Bal. (US$B, ar)	1.4	0.4	0.5	1.5 (Aug)
Industrial Production	-9.4	-7.1	-1.5	-11.0 (Aug)
CPI	3.8	3.4	2.5	3.4 (Sep)

India	2011	12Q1	12Q2	Latest
Real GDP	7.5	5.3	5.5	
Current Acc. Bal. (US$B, ar)	-62.8	-21.7	-16.4	
Merch. Trade Bal. (US$B, ar)	-13.5	-15.7	-13.4	-15.6 (Aug)
Industrial Production	4.8	0.6	-0.2	0.1 (Jul)
WPI	9.5	7.3	7.5	7.6 (Aug)

Indonesia	2011	12Q1	12Q2	Latest
Real GDP	6.5	6.3	6.4	
Current Acc. Bal. (US$B, ar)	1.7	-3.2	-6.9	
Merch. Trade Bal. (US$B, ar)	2.2	0.9	-0.8	0.2 (Aug)
Industrial Production	4.1	5.4		3.0 (May)
CPI	5.4	3.7	4.5	4.3 (Sep)

Latin America

Brazil	2011	12Q1	12Q2	Latest
Real GDP	2.5	0.6	0.4	
Current Acc. Bal. (US$B, ar)	-52.5	-48.3	-53.1	
Merch. Trade Bal. (US$B, ar)	29.8	9.7	18.5	30.7 (Sep)
Industrial Production	0.4	-3.5	-4.4	-2.0 (Aug)
CPI	6.6	5.8	5.0	5.3 (Sep)

Chile	2011	12Q1	12Q2	Latest
Real GDP	6.0	5.3	5.5	
Current Acc. Bal. (US$B, ar)	-0.3	-0.5	-9.8	
Merch. Trade Bal. (US$B, ar)	10.0	10.2	5.1	-10.1 (Aug)
Industrial Production	6.9	3.9	2.8	3.6 (Aug)
CPI	3.3	4.1	3.1	2.6 (Aug)

Peru	2011	12Q1	12Q2	Latest
Real GDP	6.9	6.0		
Current Acc. Bal. (US$B, ar)	-3.3	-0.9	-2.2	
Merch. Trade Bal. (US$B, ar)	0.9	0.8	0.2	-0.2 (Jul)
Unemployment Rate (%)	7.7	8.3	7.2	6.7 (Aug)
CPI	3.4	4.2	4.1	3.5 (Aug)

Colombia	2011	12Q1	12Q2	Latest
Real GDP	5.9	4.7	4.9	
Current Acc. Bal. (US$B, ar)	-10.0	-1.6	-3.2	
Merch. Trade Bal. (US$B, ar)	0.4	0.7	0.2	-0.2 (Jul)
Industrial Production	4.8	1.9	-0.1	2.8 (Jun)
CPI	3.4	3.5	3.4	3.1 (Aug)

All data expressed as year-over-year % change unless otherwise noted.

Source: Bloomberg, Global Insight, Scotia Economics.

Interest Rates (%, end of period)

Canada	12Q2	12Q3	Sep/28	Oct/05*	United States	12Q2	12Q3	Sep/28	Oct/05*
BoC Overnight Rate	1.00	1.00	1.00	1.00	Fed Funds Target Rate	0.25	0.25	0.25	0.25
3-mo. T-bill	0.88	0.98	0.98	0.97	3-mo. T-bill	0.08	0.09	0.09	0.10
10-yr Gov't Bond	1.74	1.73	1.73	1.81	10-yr Gov't Bond	1.64	1.63	1.63	1.71
30-yr Gov't Bond	2.33	2.32	2.32	2.40	30-yr Gov't Bond	2.75	2.82	2.82	2.94
Prime	3.00	3.00	3.00	3.00	Prime	3.25	3.25	3.25	3.25
FX Reserves (US$B)	69.2	66.0	67.0	(Aug)	FX Reserves (US$B)	138.0	138.8	140.5	(Aug)
Germany					**France**				
3-mo. Interbank	0.53	0.11	0.11	0.11	3-mo. T-bill	0.04	0.00	0.00	0.00
10-yr Gov't Bond	1.58	1.44	1.44	1.53	10-yr Gov't Bond	2.69	2.18	2.18	2.28
FX Reserves (US$B)	67.9	68.2	68.4	(Aug)	FX Reserves (US$B)	49.2	49.6	51.2	(Aug)
Euro Zone					**United Kingdom**				
Refinancing Rate	1.00	0.75	0.75	0.75	Repo Rate	0.50	0.50	0.50	0.50
Overnight Rate	0.38	0.11	0.11	0.10	3-mo. T-bill	0.37	0.35	0.35	0.35
FX Reserves (US$B)	319.8	328.7	331.3	(Aug)	10-yr Gov't Bond	1.73	1.73	1.73	1.78
					FX Reserves (US$B)	82.4	84.4	86.9	(Aug)
Japan					**Australia**				
Discount Rate	0.30	0.30	0.30	0.30	Cash Rate	3.50	3.50	3.50	3.25
3-mo. Libor	0.13	0.13	0.13	0.13	10-yr Gov't Bond	3.04	2.99	2.99	3.04
10-yr Gov't Bond	0.84	0.78	0.78	0.78	FX Reserves (US$B)	47.7	44.1	41.2	(Aug)
FX Reserves (US$B)	1247.8	1231.2	1232.7	(Aug)					

Exchange Rates (end of period)

USDCAD	1.02	0.98	0.98	0.98	¥/US$	79.79	77.96	77.96	78.71
CADUSD	0.98	1.02	1.02	1.02	US¢/Australian$	1.02	1.04	1.04	1.02
GBPUSD	1.571	1.617	1.617	1.619	Chinese Yuan/US$	6.35	6.28	6.28	6.32
EURUSD	1.267	1.286	1.286	1.305	South Korean Won/US$	1145	1111	1111	1111
JPYEUR	0.99	1.00	1.00	0.97	Mexican Peso/US$	13.361	12.859	12.859	12.696
USDCHF	0.95	0.94	0.94	0.93	Brazilian Real/US$	2.009	2.026	2.026	2.025

Equity Markets (index, end of period)

United States (DJIA)	12880	13437	13437	13636	U.K. (FT100)	5571	5742	5742	5869
United States (S&P500)	1362	1441	1441	1468	Germany (Dax)	6416	7216	7216	7394
Canada (S&P/TSX)	11597	12317	12317	12461	France (CAC40)	3197	3355	3355	3453
Mexico (IPC)	40200	40867	40867	41792	Japan (Nikkei)	9007	8870	8870	8863
Brazil (Bovespa)	54355	59176	59176	59217	Hong Kong (Hang Seng)	19441	20840	20840	21012
Italy (BCI)	761	825	825	837	South Korea (Composite)	1854	1996	1996	1995

Commodity Prices (end of period)

Pulp (US$/tonne)	870	900	850	850	Copper (US$/lb)	3.45	3.75	3.75	3.76
Newsprint (US$/tonne)	640	640	640	640	Zinc (US$/lb)	0.84	0.95	0.95	0.92
Lumber (US$/mfbm)	279	283	285	288	Gold (US$/oz)	1598.50	1776.00	1776.00	1791.75
WTI Oil (US$/bbl)	84.96	92.19	92.19	90.10	Silver (US$/oz)	27.08	34.65	34.65	34.85
Natural Gas (US$/mmbtu)	2.82	3.32	3.32	3.38	CRB (index)	284.19	309.30	309.30	310.45

** Latest observation taken at time of writing.*
Source: Bloomberg, Scotia Economics.

Emerging Markets Strategy

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