Global Views

Weekly commentary on economic and financial market developments

May 25, 2012

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Irish Voters, Marquee U.S. Releases, And Canadian GDP Top The Charts

- **Please see our full indicator, central bank, auction and event calendars on pp. A3-A7.**

Much of the risk tone facing world markets will be set by the **US** economy. For the most part this will only happen toward the end of the week not only because US markets are closed for Memorial Day on Monday but also because a series of key reports will be released on Friday that will help determine what kind of momentum the US economy has into the second quarter. The line-up starts slow with the Conference Board's consumer confidence index on Tuesday and pending home sales on Wednesday, both of which are expected to be flat. Consensus expects Q1 US GDP to be revised from 2.2% to 1.9% Thursday partly due to revised trade effects. On that same day, we'll get a glimpse at the first of the top-tier labour market reports when the ADP private payrolls report arrives. That will be followed by the more complete nonfarm payrolls report and the household survey on Friday. On balance, we're expecting another round of soft sub-200k prints as seasonal distortions continue to come off in a manner that offsets the upsides to job reports over the winter months. Friday actually offers a hat trick of reports that also includes consumer spending during the month of April that is expected to follow a decent nominal gain in retail sales higher, and the ISM manufacturing report. While the prior month's ISM result surpassed expectations and went against the broad tone of regional manufacturing surveys, we're expecting the usual correlations between ISM and gauges such as the recent disappointment in the Philly Fed index to be restored in such a manner as to put downside risk to ISM this time. Fed speak heats up mildly with NY Fed President William Dudley (always voting), Boston Fed President Eric Rosengren (alternate), and Cleveland Fed President Sandra Pianalto (voting) scheduled to speak. Pianalto's speech will likely be the most focused on monetary policy and the economic outlook following Dudley's recent comments that a deterioration in the eurozone and/or the U.S. "fiscal cliff" could motivate additional easing that is unlikely nearer term.

European markets will pose two main forms of risk to global markets next week. One will be an Irish referendum on the European Fiscal Stability Treaty, or the EU fiscal compact on Thursday. Ireland is the only country to hold such a vote within the 25 European nations that signed on to the fiscal pact, as Irish law requires such a referendum to be held on matters affecting sovereignty. The concern overhanging voters is that Ireland may be cut off from international financial aid if it rejects the treaty, and that is why there is a modest balance of opinion in recent polls that is in favour of a yes vote. That said, Ireland has two precedents for rejecting EU treaties (like the Lisbon Treaty in 2008), and another would be a further setback to German-led austerity efforts. A 'no' vote, however, would not derail the fiscal compact because only twelve countries are needed to ratify it. The second main form of European risk comes through key updates on the German economy. Germany's economy averted recession by expanding 0.5% q/q in Q1 following a small 0.2% decline in Q4. Retail sales are expected to come in flat for the April print, the unemployment rate is expected to hold around a post-reunification low of 6.8%, and CPI is expected to be soft enough to justify a further ECB rate cut.

Canadian markets will follow the broad global tone next week with the exception of domestic risk that lands Friday in the form of monthly March and full Q1 GDP figures. We think the economy accelerated in March with the reversal of some temporary factors weighing down growth prospects, but that the quarter as a whole will come in soft at 2% with the notable risk of being significantly weaker. That would disappoint BoC expectations for 2.5% growth, and result in more spare capacity than it judged in the April Monetary Policy Report. Canada auctions 30-year real return bonds on Wednesday.

Asian markets will have little capacity to influence the global tone with the possible exception of China's state version of the purchasing managers' index that is due out on Thursday night. Consensus is expecting a modest drop to a still expansionary reading that lies at odds with the private sector PMI which remains in contraction, and with hard data on industrial production that has slowed markedly into the new year. Indian Q1 GDP is expected to come in at 6% y/y which would remain among the weakest growth rates of the past decade. Japanese household spending, retail trade, industrial production and housing starts are also on next week's schedule. RBA Governor Glenn Stevens delivers a speech into the Monday market open ahead of the June 5th RBA rate decision that consensus expects will yield no change in the cash target rate of 3.75%. The RBA has cut by 100bps since October in two moves.

The **Bank of Brazil** is expected to cut by 50bps on Wednesday which would lower its Selic target rate by a cumulative 400bps since the easing cycle began last August.

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Canada's Household Debt Service Burden Is Higher Than Previously Estimated

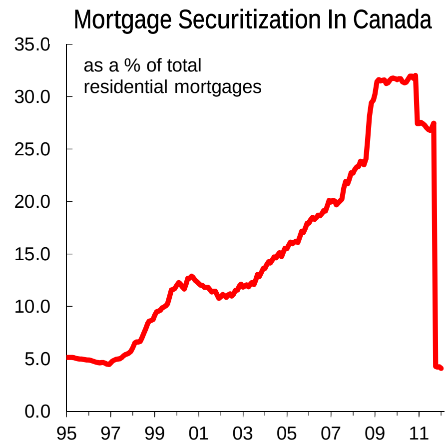
- **An accounting change makes it easier to include estimates of mortgage principal payments at banks.**

Canada's household debt service burden is higher than we previously estimated. What has changed is that our ability to estimate principal payments by mortgage holders to banks has improved thanks to accounting changes affecting banks that became effective November1, 2011. Prior to this accounting change, securitized mortgages and related securities were held off-balance sheet and related principal payments had previously been through off-balance-sheet securitized conduits that were more difficult to track. With the accounting changes, securitized mortgages and related securities must now be held on-balance sheet and that re-captures the data on principal payments back within reports that we use which primarily focus upon on-balance sheet payments.

Chart 1 provides a sense of the magnitude of this change. Prior to November 1st, approximately 27% of total residential mortgages were held off-balance sheet through National Housing Act mortgage-backed securities and special purpose corporations. Following the accounting changes affecting banks such assets were brought back on balance sheet and out of the securitized off-balance sheet categories.

Along with this is that the Bank of Canada's Mortgage Loans Report — through which we estimate principal payments to banks by mortgage holders — also recaptured off-balance sheet receipts of principal payments. The effect is shown in chart 2 in that this report's figures for principal repayment on insured residential mortgages spiked sharply higher in Q4 of last year as off-balance sheet payments were brought back into the data.

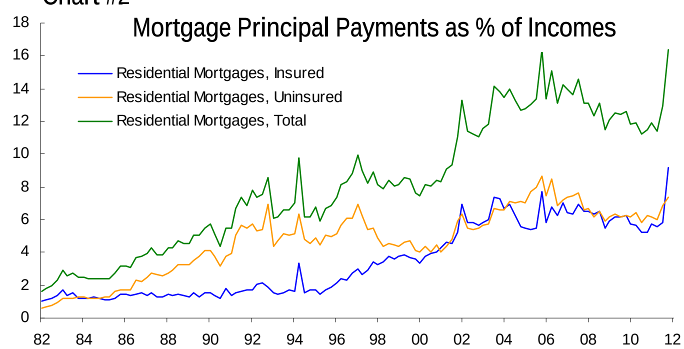
Chart #1



Source: Bank of Canada, Scotia Economics.

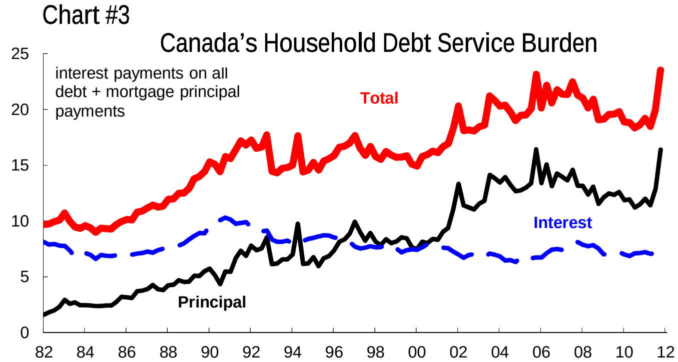
Our household debt service burden is calculated using hard data for interest expense on mortgages and all consumer loan products plus mortgage principal repayment to banks. It is not estimated through rough assumptions as other measures do. With the accounting change, chart 3 shows the flow-through effects that led to a significant upward adjustment in Q4. Figures prior to this were not revised and thus we're left with a break in the comparability of the series over time. One cannot say how the revised figure compares to the past since we still don't have a data series for principal payments through securitized conduits prior to 2011Q4, but one can say that interest and principal payments alone are now absorbing about one quarter of after-tax disposable income.

Chart #2



Note that we are still unable to capture mortgage principal repayments to institutions other than banks. Since banks represent about 75% of the mortgage industry in Canada we're likely missing about 25% of mortgage principal repayments which would add about four percentage points to our debt service measure and thus bring it closer to 30%. We are still unable to capture principal payments on non-mortgage debt products through a consistently defined measure over time such that the true figure is guesstimated to be in the mid-30s given that mortgages are about 70% of total household debt.

Chart #3



Source: Bank of Canada, Statistics Canada, Scotia Economics.

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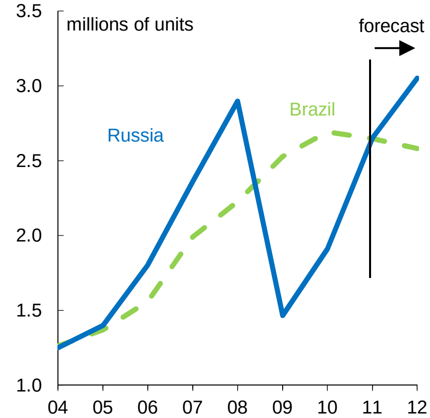
Global Car Sales Continue To Advance, But At A Slower Pace

- **Asia and Eastern Europe lead the way, while a slowdown in Brazil prompts stimulus package.**

Global vehicle sales continue to move higher, but the gain moderated to 3% y/y in April from nearly a 5% advance in the first quarter. Solid gains in Japan, China, Eastern Europe and North America were dampened by ongoing weakness in the euro zone and a recent slowdown in South America — especially in Brazil.

Diverging Trends: Record Sales In Russia, Softness in Brazil



Source: Scotia Economics

Car sales in Japan were nearly double year-earlier levels last month due to the low base effect following last year's earthquake and tsunami. Purchases have advanced at a double-digit year-over-year pace over the past eight months, and through April are running at the highest level since 2006. However, this sharp gain is unlikely to extend beyond 2012, as Japan's vehicle-buying population peaked a decade ago and is currently falling by nearly a percentage point per annum.

Purchases also continued to post double-digit gains in Russia, leaving them on target to exceed 3 million units this year for the first time on record. In fact, Russia is likely to overtake Germany as the largest auto market in Europe before mid-decade. As recently as 2003, car sales in Germany were more than triple the sales level in Russia. Despite its links to the euro zone which has fallen back into recession, car sales across all of Eastern Europe have been advancing year-over-year since early 2010 and show no sign of moderating.

In contrast, car sales in Brazil fell 14% below a year earlier last month, as rising auto-loan defaults prompted some reduction in automotive credit, which normally accounts for 60% of overall vehicle purchases. Data from the Central Bank of Brazil indicate that the number of non-performing auto loans climbed to a record 5.7% in March, up from 3% a year earlier. Given the weakening sales trend, the industry proposed a reduction in the new vehicle sales tax to spur demand.

The government responded this week by unveiling a US$10 billion stimulus package designed to boost the automotive and other industrial sectors. The package provides additional funding for auto loans and includes a temporary cut in the sales tax for some vehicles. Prior to these measures, Daimler had ordered a nine-day furlough for all of it workers at a truck plant in Sao Paulo, while both Ford and Volkswagen had reduced the line speed at their Brazilian assembly plants to prevent a build-up of unsold vehicles. Brazil is the eighth largest vehicle producer in the world, with output of 3.1 million cars and trucks last year. Assemblies have declined by 10% in Brazil this year, contributing significantly to the economic slowdown, and the sector accounts for 20% of the nation's overall industrial activity.

In North America, the auto sector continues to rev up, with second-quarter assemblies scheduled to jump 28% above a year earlier, climbing to the highest level since 2006. In fact, demand is so strong that several automakers have announced plans to forego their normal summer shutdowns. The United States is leading the rebound in North American vehicle production, but Canada and Mexico are not far behind.

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Is A Redemption Fund The Answer To Europe's Troubles?

- **The size of the fund could be enormous, and it could well raise moral hazard, adverse incentives and unintended consequences for all parties.**

Europe is currently debating whether eurobonds or an alternative European Redemption Fund proposal could offer a solution to its sovereign debt and banking crisis. Italian PM Mario Monti recently stated that the majority across the EU support joint eurobond issues and that Germany's opposition could be overcome. That seemed a stretch since it conflicted with the impressions of Luxembourg's Prime Minister Jean-Claude Juncker, and both German Chancellor Angela Merkel and the German political opposition remain united against the Eurobond concept in no small part because the resulting yield convergence would come at the expense of Germany's borrowing costs and with few if any strings attached beyond the European Fiscal Stability Treaty. The notion of a European Redemption Fund contained within a European Redemption Pact that was first proposed last November, however, is being studied as one of the more novel proposals and will be debated by the German Parliament on June 13th. Details on this proposal can be found at: http://www.sachverstaendigenrat-wirtschaft.de/. Our purpose here is to outline its core features, point out the potential size in the relatively near-term, and express our concerns at this stage.

1. Features

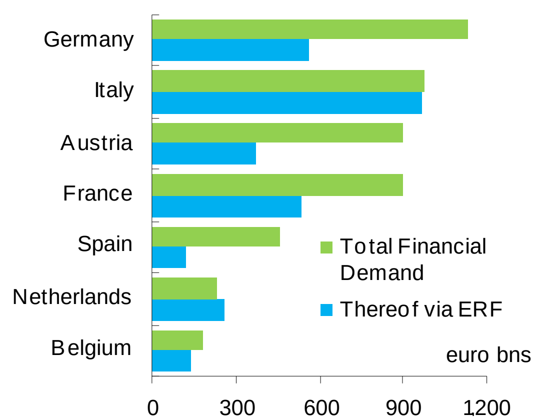
Should the European countries 'socialize' their debts, jointly and severally backing one another's sovereign liabilities so that Germany stands behind the debts of Italy and Spain? Among the many proposals that exist to address the Eurozone's ongoing debt woes, the view that debt socialization would solve Europe's problems by blending the credits of weaker nations with stronger ones seems to be gaining currency. The premise of the pact is that a "joint debt vehicle… should be able to calm markets… by strong countries lending their reputation, i.e. their low risk premia in the bond markets, to member countries facing a liquidity crisis".

The European Redemption Pact would have two core facets:

a) The European Redemption Fund: The Eurozone nations would raise a fund backed jointly and severally by their sovereign credit. The fund's purpose would be to finance the borrowing needs of all Eurozone nations equal to the amount of debt that the countries *currently* have in excess of the 60% debt-to-GDP limit set out in the Maastricht Criteria. The EMU member countries' debt exceeding the 60% ceiling on a certain date will be refinanced via the European Redemption Fund for which the EMU members are jointly and severally liable. The fund's interest expense would be shouldered jointly by the countries that raise it, and the interest costs of the countries that draw on the fund would be payable individually by the fund's borrowers themselves.

b) The Pact's Conditions: Borrowers would have to implement taxes whose revenues would be earmarked to sink their debts payable to the fund. Borrowers would provide a guarantee of the debt equal to 20% of its value by pledging collateral of forex or gold reserves that would be deposited with the new fund and callable should the borrower fail to meet its obligations. Borrowers would implement 'constitutional brakes' analogous to those in Germany and Switzerland to prevent gross debts from rising above current levels, and that would constrain the yearly structural deficit below the level of 0.5% of GDP. Borrowers would also commit to consolidation and structural reforms.

Financing Of General Governments Via ERF Within The Roll-In Phase



Source: German Council of Economic Experts, Scotia Economics.

2. Size

A first concern relates to the potential contingent liabilities that would be taken on by the backer states. Chart 1 provides the estimates of the total financing demand broken down by state,

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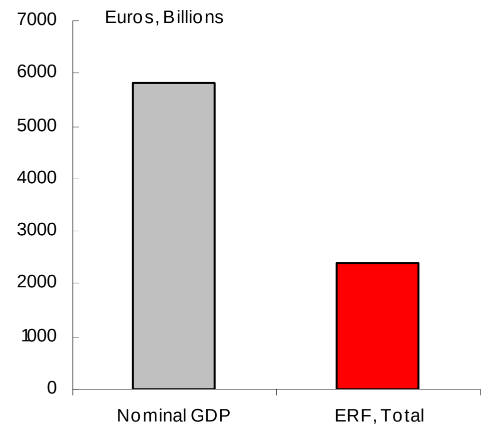
and the amount that would be funded through a European Redemption Fund (ERF) over the four-year roll-in phase for qualifying countries. The ERF would quickly swell to a size of €2.4 trillion of which €1.9 trillion would not be collateralized by gold and FX reserves and would thus be backed by the collection of backer states. The source is the German Council of Economic Experts which crafted the proposal. Chart 2 compares the size of the ERF at the end of the four-year roll-in phase to the current nominal GDP of the likely backer states. Rating agencies could well look unfavourably upon the adoption of such large additional contingent liabilities beyond what has already been embraced as liabilities by the backer states through the EFSF/ESM apparatus.

2014 ERF Size Equal to 40% of Current Nominal GDP of Germany, France, Netherlands, Austria, & Belgium



Source: Scotia Economics, GCEE

3. Concerns

Briefly, there are several main concerns that we have about the viability of the ERF proposal.

1. Clearly the objective here is to lower average debt costs for the more beleaguered states. In so doing, Germany's bond market – and those of other higher-quality credits – would be sacrificed through the adoption of large contingent liabilities and the result over time would be spread convergence by raising German borrowing costs and lowering the borrowing costs of more profligate states. Rating agency implications combined with the leakage of German wealth to fund more such stabilization vehicles would have to be traded off against the uncertain costs and benefits of other proposals. In other words, rather than making Spain and others solvent, this proposal might eventually place funding constraints on the backer nations collectively.

2. It's not clear that those member states that have raised concern about German intrusion into domestic fiscal policy matters would be any more enthused by this option that would entail much stronger intrusion particularly into a potentially divisive round of constitutional debates that would likely be addressed through referendums in at least some countries.

3. Constitutions can, however, be changed and it's not at all clear that member states would faithfully abide by these restrictions on their national fiscal sovereignty. The threat of stopping the funding is held out, but once committed to this path would Europe really be in a position to cease funding activities if doing so risked resurrecting a further fiscal crisis?

4. It is difficult to differentiate a 25 year fund from something that would become more permanent.

5. Related to this last point is concern over whether reduced market pressure upon the more profligate states would turn an ERF into a permanent vehicle subject to moral hazard problems, adverse incentives and unintended consequences. It may well be that the backer states could wind up being committed to a long run ransom path.

6. No one proposal can achieve everything, but nothing within this proposal explains how challenges facing European banks would be addressed and how capital and funding requirements would be met.

7. By pooling credits, the risk that the ECB could turn toward monetizing debt may increase since it would no longer be faced with the politically contentious issue of backing some states over others.

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Business Surveys Put The ECB Further Under Pressure!

Key Points

- **All of the major business surveys (ZEW, PMI, INSEE, Ifo) moved south in May, reinforcing the risk that the eurozone will slip back into recession during Q2.**
- **This dynamic conflicts with the ECB's growth assumption that there will be a gradual recovery in the coming quarters. In combination with the fall in market inflation expectations (gauged by the Euro inflation swap market), this increases the pressure on the ECB to adjust interest rates lower as early as the June meeting with a 25 bps move.**
- **Finally, the need to fill the gap of current political uncertainties forces the ECB to act in order to avoid further fuelling current risk aversion**

All business surveys have moved south

Though we warned ahead of time about the downside risks to May's business surveys the actual outcome was even worse than we feared. Starting with the eurozone PMI data, the composite index fell almost a full point to 45.9 vs. consensus expectations for a stable reading. The drop mainly reflected weaker manufacturing — where the index fell to 45 from 45.9 — its lowest level in 3 years. Furthermore, weaker manufacturing activity was broad based as both French and German indices moved south to 44.4 and 45 from respectively 46.9 and 46.2. It means that the recession risk in this sector is spreading and intensifying across countries. If the core countries such as France and Germany are suffering in this way – you can bet the situation is even worse in the periphery (data to be released in June).

Chart 1: Ifo survey

This worrying signal was reinforced by weaker-than-expected business sentiment throughout the national surveys for May. In France, the INSEE business index dropped to 93 from 95, also lower than expectations for a fall to 94. Perhaps the biggest surprise of all was the plunge in the German Ifo — down three points to 106.9 from 109.9, well below consensus expectations for a mild drop to 109.4. This fall is significant as the Ifo survey had been diverging from all other surveys (having risen for 6 consecutive months). This dive brings the Ifo a little closer into line with the other surveys.

It is true that the Ifo index remains elevated — it was a big fall, but from a high starting point. Nonetheless, the details of the report were not very encouraging. First, the drop in the expectations component to 100.9 from 102.7 is not boding well for upcoming surveys. Indeed, this component typically leads the current conditions component. The latter had been defying gravity, but has now started to follow the expectations series lower — with plenty of potential for further downside.

Second, the survey also showed broad-based weakness by sector (manufacturing, retail, construction, wholesale trade).

All in all, May's surveys sent a compelling signal of weakness across the euro area. This is likely to put pressure on the ECB to loosen policy further at the June meeting.

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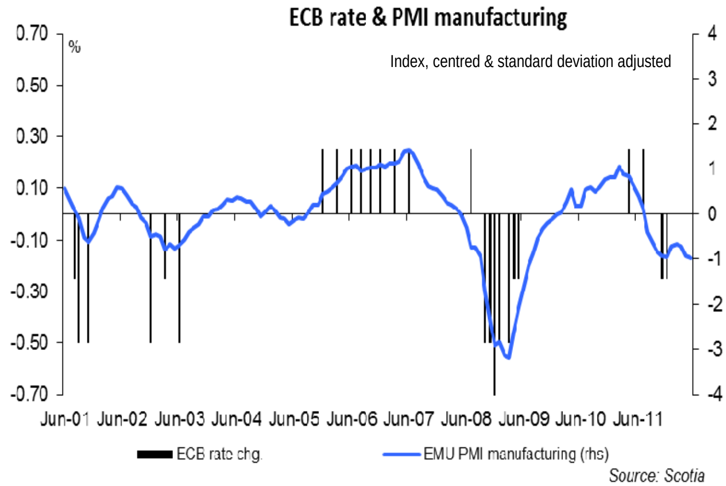
It is worth remembering that at last month's ECB meeting there was an implicit hint that June's meeting will be crucial. Mr. Draghi in particular pointed to the need to observe incoming data over the coming months to make a better assessment. Last week, flat quarterly growth on Q1 EMU GDP seemed to confirm the ECB's assumption that activity stabilised at the beginning of the year. However, these latest surveys are not at all validating the ECB's view that the Euro area will enjoy a slow recovery further ahead. On the contrary, the surveys point to renewed recession. This picture is likely to provoke a downward revision of the ECB's growth outlook with the release next month of new forecast tables.

Chart 2: ECB rate changes & EMU PMI manufacturing



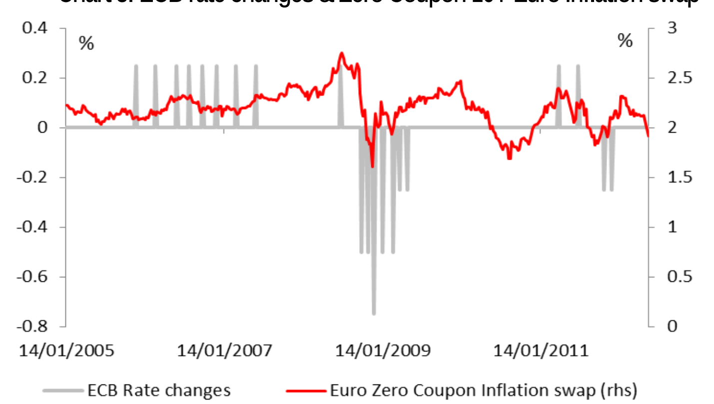
Furthermore, in the context of ECB policy, the relationship between EMU manufacturing and ECB rates indicates an increasing risk of a rate cut in June (Chart 2).

Medium-term inflation expectations: Rising risk of the ECB undershooting its inflation target?

The inflation outlook could also add further justification for the ECB to adjust rates lower. It is true that April's inflation reading was still above the 2% threshold (at 2.6% y/y). However, the sharp fall in oil prices in the past month strengthens confidence that price pressures will ease over the coming months. The May flash estimate will be released next week and we look for the y/y pace to slow down to 2.4% thanks to a sharp drop in energy prices. Preliminary data from May inflation in the Lander of Saxony already hinted in this direction as details showed petrol prices down a sharp 3.2% m/m! This scenario is likely to be replicated in the rest of the German Lander and in the EMU as a whole.

Furthermore, medium-term inflation expectations measured through the Euro inflation market also offers room to manoeuvre for the ECB to adjust rates lower. Indeed, 10Y zero coupon Euro inflation swaps dropped below the 2% threshold — down to around 1.92% (Chart 3). At this level, it suggests that there is growing sentiment in the market that the ECB will undershoot its inflation target. Usually, this factor triggers some dovish reaction from the central bank.

Chart 3: ECB rate changes & Zero Coupon 10Y Euro inflation swap



Filling the gap of political uncertainties

Unfortunately for the central bank, the pressure to act is also coming from the lack of clarity on the political front. While we consider that the agreement on the fiscal pact early this year was a significant step towards easing risk aversion, its ratification is for the moment in a wait-and-see attitude in a number of countries

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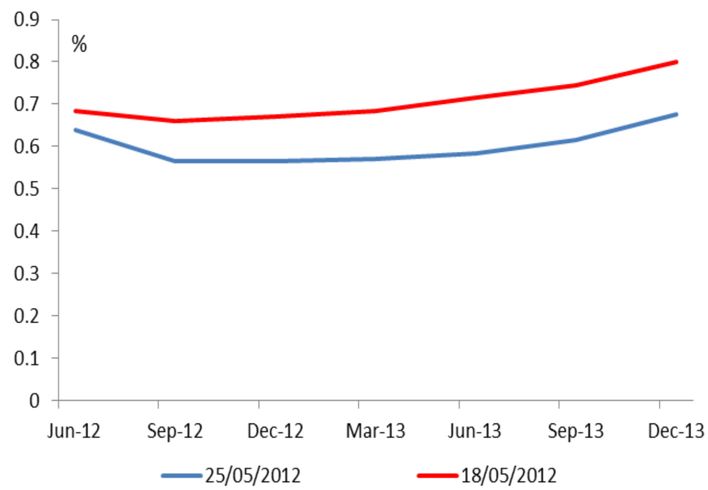
including France and Germany. In the meantime, as seen by the EU summit this Wednesday, there are little hopes to have any strong common commitment from EMU governments before both new Greek and French deputy elections (both on June 17th). Indeed, sticking to a firm stance for Germany is, in the first case, the best way to force Greece to make these coming elections no longer just a vote between "pro" or "anti" austerity plan but rather between "pro" or "anti" euro itself which should, in theory, work more in favour of parties like the PASOK or ND vs. the far left. In the second case, Mrs. Merkel is keen to wait for the results of the French deputy elections in order to see more clearly what is the underlying support for Mr. Hollande before setting any new position.

So, it means still three weeks without any support from politics. It could be argued that the ECB might also prefer to wait for some clarity and keep its "powder dry" for the time being. With interest rates at 1%, there is indeed not too much room to manoeuvre on this front and each bullet should be used carefully. However, at this stage of the crisis, we think it is key that the ECB not also disappoint and it seems that the market is expecting more and more on this front. While the link between Euribor and ECB rates has been looser over the recent period as highly distorted by the ample liquidity offered in the system, front euribor contract nonetheless rallied over the past week, meaning increasing expectations of an ECB rate cut. So, definitely, this June meeting will be a key one!

Chart 4: Euribor contracts



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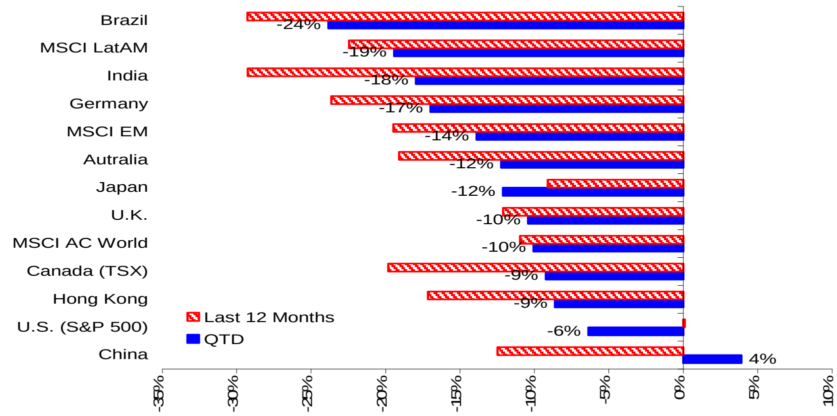
Q2/12 Sell-Off: Assessing The Damage

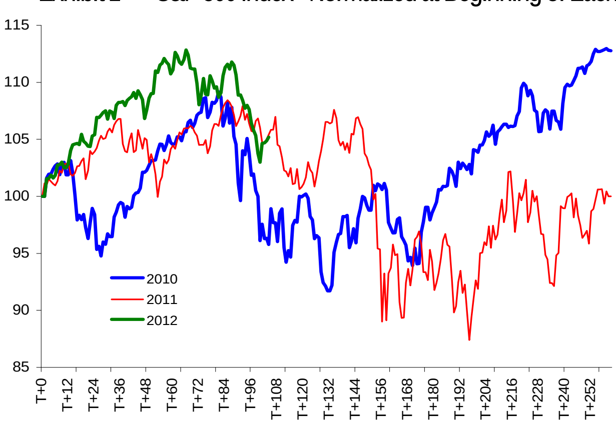
- Global equities have been selling off since late March and the ongoing weakness in cyclical assets bears many similarities with the spring/summer pullbacks of 2010/2011. Since the start of Q2, the MSCI World AC index is down 10%, and the MSCI Emerging Market index has lost 14%. Canada's TSX is off 9%, and the S&P 500 has slipped 6% over that period. All in USD.
- Heightened risk aversion has pushed the USD higher and weakness in emerging market has been compounded by plunging currencies. Brazil (real down 10% in Q2) and India (rupee down 8% in Q2) have suffered the most with equity index losses topping 24% and 18%, respectively. In contrast, China's Shanghai A-Share index is up 4% quarter-to-date. Year-over-year, equity pain is more visible outside the U.S.: the S&P 500 is flat over the last 12 months compared to declines of 17% in Hong Kong, 20% in Canada, and 29% in Brazil. See Exhibit 1 for QTD and YOY performance in USD.
- From its YTD peak, the S&P 500 is now off 8%. The S&P 500 correction hit 16% in 2010 and 19% in 2011. Exhibit 2 highlights the normalized calendar S&P 500 pattern over the last three years.
- Back-to-back disappointing monthly U.S. payrolls report, renewed political uncertainty in the Eurozone, and persistent China growth fears are mostly to blame for the swift blow to risk appetite. We would also add another reason: the "risk-on" window closed down in mid-March when the S&P 500 pushed above 1,400 and U.S. 10-Yr yields hit 2.38%. Through the first three months of 2012, S&P 500 performance had outpaced long-term Treasuries by over 20%, a very extended level. Over the last three months, mean-reversion has acted up, and the S&P 500 is lagging bonds by 8%. As highlighted in Exhibit 3, the ongoing risk-off trade now appears well under way.

Exhibit 1 — Global Equity Returns (in USD) - 2012 QTD & Last 12 Months 23-May-12



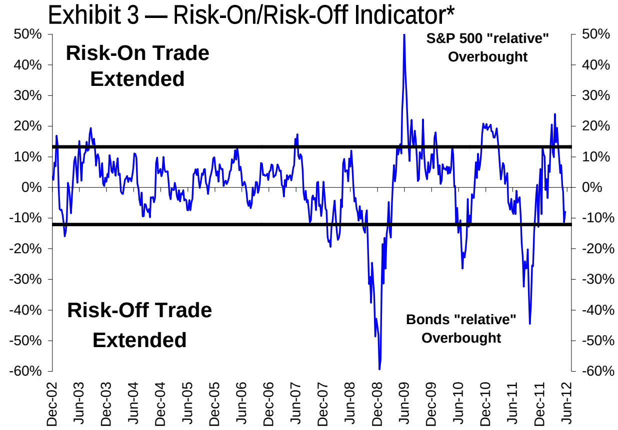
Source: Scotiabank GBM, Bloomberg

Exhibit 2 — S&P 500 Index - Normalized at Beginning of Each Year



Source: Scotiabank GBM, Bloomberg

Exhibit 3 — Risk-On/Risk-Off Indicator*



*S&P 500 minus Long Term Bonds (TLT) - Relative Performance (last 3-months) Source: Scotiabank GBM, Bloomberg

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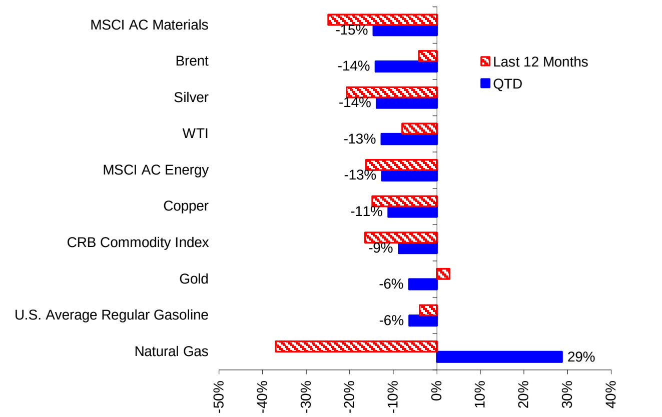
Commodities Suffering

- One of the main casualties of the ongoing sell-off has been commodities, both physical and equities. Since the start of Q2, copper, oil (WTI), and gold have slipped 11%, 13%, and 6%, respectively. Energy (-13% so far in Q2) and Materials (-15%) have been among the worst performing sectors on the MSCI World index. See Exhibit 4.
- China's most recent series of macro data for April contained many disappointing features. Weaker exports (+4.9% YOY in April) and imports (+0.3% YOY: lowest since October 2009) highlighted domestic and foreign strains clamping down growth. We (Portfolio Strategy Team) continue to expect weaker data through Q2, which should trigger broader easing (i.e., lending rate cut). As highlighted in Exhibit 5, TSX and Resource underperformance tends to bottom once lending rate cuts have started.

May PMIs Point to Weak Q2 in Europe, China

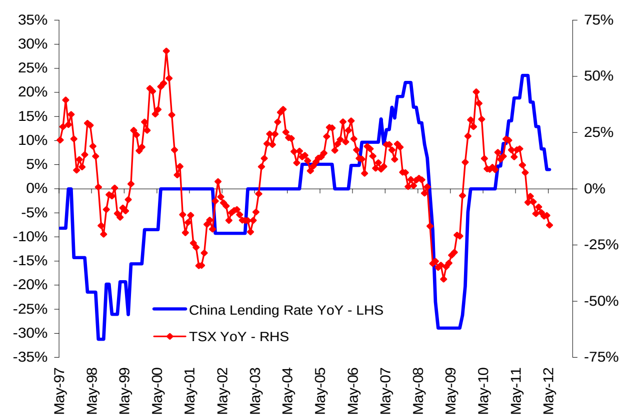
- May PMI manufacturing surveys eased further in Europe with levels of 44 in France and 45 in Germany. China's Flash PMI index slipped to 48.7 in May from 49.3 the prior month. The U.S. ISM index will be released next week and consensus is set at 54.0 (54.8 in April).
- Globally, the pace of economic activity is noticeably slower in Q2. China's Flash PMI has been hovering below the 50 threshold for seven consecutive months and Germany's manufacturing outlook is currently the weakest since July 2009. U.S. indicators are also expected to soften in coming months, although the positive ISM spread over Germany/China PMI is expected to remain well into Q3.
- Policy-wise, a materially weaker outlook for Germany could translate into more flexibility from German politicians and more pro-growth measures (QE, ECB rate cuts, Eurobonds), which should push the euro lower. In China, easing policy could intensify if PMI levels nudge closer to 45 (lending rate cuts). Bottom line: we believe declining PMI/ISM indices should continue to challenge equity sentiment in the near term; however, once these indicators have bottomed, investors will likely want to ride the ISM/PMI recoveries.

Exhibit 4 — Global Commodity Returns - 2012 QTD & Last 12 Months



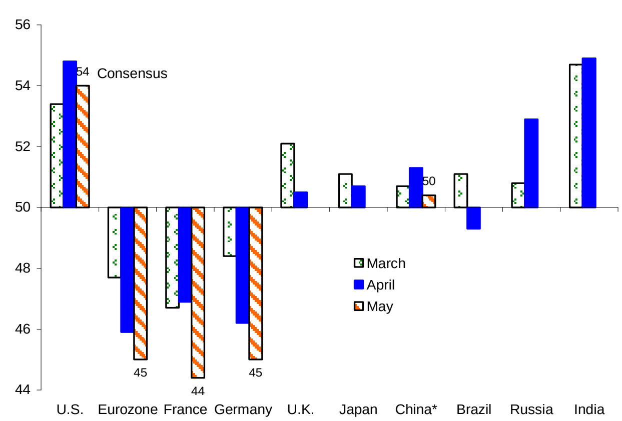
Source: Scotiabank GBM, Bloomberg

Exhibit 5 — China Lending Rate and TSX (1997-2012)



Source: Scotiabank GBM, Bloomberg

Exhibit 6 — Global Manufacturing PMI



*China PMI: Average of Government PMI & Markit/HSBC PMI
Source: Scotiabank GBM, Bloomberg

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Strategy View Unchanged, Looking for Signs to Add Beta

- We stand by our defensive/lower beta strategy stance recommended in our April asset mix and model portfolio update. In our opinion, the ongoing "risk-off" theme may be 2/3 of the way done. We see modest downside from current levels as persistent global macro headwinds and weaker coincident data suppress risk appetite in the near term. (1) Extreme "S&P 500/long bonds" underperformance (risk-on/risk-off indicator), broader China easing (lending rate cuts), and a resolution to the Euro crisis (German flexibility on Eurobonds/ECB) would prompt us to reverse our lower beta stance and raise cyclical exposure. Our 1H/12 game plan was to lower our cyclical exposure; we intend to look for signs to add beta in the second half.

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Key Data Preview

CANADA

Canada Q1 GDP will be released on June 1, and Scotia is anticipating GDP growth of 2% with an increase of 0.4% in the monthly income-approach number. We think that Canadian consumers slowed down their shopping during Q1 2012. Retail sales data indicate that the contribution to growth from retail trade will be just about zero on the quarter — after retail sales grew at an annualized rate of 6.9% from Q3 2011 to Q4 2011. The pace of retail sales is the principal proxy that we use in order to estimate changes in consumption as measured in the 'expenditure-approach' GDP numbers which markets typically focus on. Slower consumption would allay concerns that Canadian consumers are ramping up their shopping, thereby posing a threat to the macro economy and necessitating 'prudential' action to defuse their binging. Rather, Canadian consumers have already binged, with Canada's aggregate consumption having expanded post-2008 even as most of the developed world economies have retrenched. The question now is whether the slow-down will be gradual or abrupt. Aside from watching the consumption numbers, we'll be looking to see the extent to which construction continues to drive growth (we're anticipating a mild contribution). The other major issue is the contribution to growth from oil and gas extraction, which looked fairly weak through the first two months of 2012. We'll be watching to see if that picked up.

UNITED STATES

Nonfarm payrolls and the household employment survey will be released on June 1 and Scotia anticipates that 160k payrolls were added during the month and that the unemployment rate increased to 8.2% from 8.1% in April. Our rationale on non-farm payrolls is that initial claims improved marginally during May (an average of 371k during the first two weeks of May vs. 389k in April) and ought to bring the level of payrolls in-line with the trend 170k/month increase in H2 2011/Q1 2012. The seasonal adjustment math will detract from the headline jobs number this month and, as our studies show that seasonal adjustment added more than is usual during the first months of the year, the seasonally adjusted number that will make headlines could be weaker than the not-seasonally-adjusted data would indicate as the math reverses, leading us to slightly temper our expectations for jobs growth.

US Nonfarm Payrolls
Seasonal Adjustment Factors

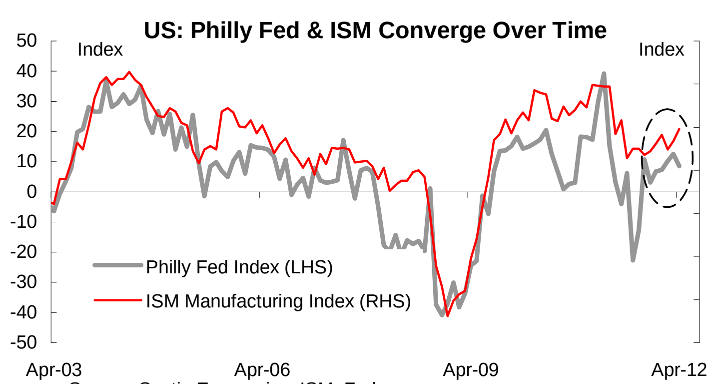
	SA Factor (Past 4 Years)	% Adjustment from SA Factor
January	1.0160	1.60%
February	1.0117	1.17%
March	1.0066	0.66%
April	1.0001	0.00%
May	0.9952	-0.48%
June	0.9927	-0.73%
July	1.0025	0.25%
August	1.0015	0.15%
September	0.9976	-0.24%
October	0.9917	-0.83%
November	0.9907	-0.93%
December	0.9937	-0.63%

Source: Scotia Economics, BLS

Personal Consumption and Income for April are due out on June 1 and Scotia's call is for income to increase by 0.1% m/m and expenditure to have grown by 0.3% m/m. Our call on incomes is driven by muted increases in hours worked (+0.1% m/m) and zero wage gains according to data released by the BLS. Personal spending has outpaced incomes over the past number of months consistent with higher spending on durable goods (mainly autos).

We would draw some attention to the second look at **Q1 GDP** due out May 31: We're anticipating a slight downward revision from the 2.2% to 2% on the basis of weak March trade balance data put out by the Dept. of Commerce subsequent to the release of Q1 GDP. There is wide dispersion among forecasters here, and a real possibility that the negative revisions might pull Q1 GDP below 2% q/q SAAR.

The **May ISM manufacturing index** will be released on June 1, and we'll be looking to see if it tracks the Philly Fed survey lower — or diverges as it did last month. As the chart below indicates, the ISM manufacturing index and the Philly Fed diffusion index typically move in lock step, which leads us to expect the ISM to fall to 53.5 in May from a reading of 54.8 in April.



Source: Scotia Economics, ISM, Fed

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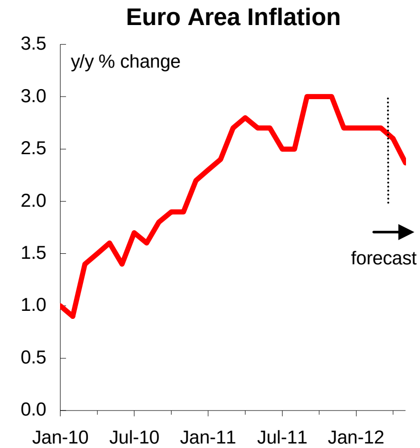
EUROPE

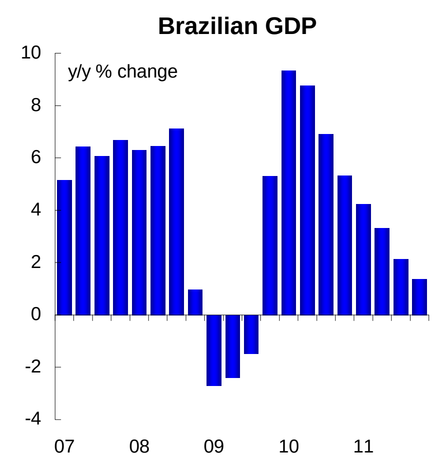
Preliminary estimates for May consumer price inflation will be closely watched next week as a marked softening in inflation could bolster the case for a rate cut by the European Central Bank (ECB) at the next policy-setting meeting on June 6th. Given the approximately 10% drop in Brent crude oil prices over the last month (and 4% drop in the prior month), we expect that softer energy-related costs will pull the headline CPI rate lower in May (housing and electricity and transport costs were the two largest contributors to the 0.5% m/m overall advance in April). We look for annual inflation to slow to 2.4% y/y from 2.6% (a 0.2% m/m fall). Until last month, both food and energy prices had proved quite sticky, and with an earlier stabilization in financial markets, the inflation-fighting ECB appeared content to recede to the sidelines and leave the policy heavy lifting needed to temper the crisis to the national governments of the euro area. Now, with inflation set to move lower, little progress expected in the near term on the political front, and survey indicators pointing to further economic weakness in the coming months (after a somewhat cheerier outcome in the first quarter), the Governing Council members may see things differently. We maintain our view that the ECB will reduce the benchmark refinancing rate by 25 basis points to 0.75% in June.



Source: Bloomberg, Scotia Economics.

LATIN AMERICA

After growing by 2.7% y/y in 2011 and by 1.4% y/y in the fourth quarter of last year, the Brazilian economy has not yet shown any signs of an upturn. The economic activity indicator showed a monthly decline in the first three months of the year, pointing towards continued weakness in GDP growth rate for the first quarter of 2012, to be released on June 1st. Additionally, industrial activity remains sluggish as a result of weaker international demand and the decrease in exports competitiveness caused by the BRL strength at the beginning of the year. Retail sales — a reflection of local demand — points to a slow recovery, which could be accelerated by both fiscal and monetary stimulus already delivered into the economy. The central bank has loosened monetary policy by cutting the reference rate by a total of 350 basis points from 12.50% to 9.0% and we expect this trend to be maintained in the coming months. However, both the fiscal and the monetary stimulus may not have an effect until the second half of the year, leaving the first half relatively weaker. We expect the Brazilian economy to grow by 2.1% y/y in the first quarter and by 3.5% y/y in 2012.



Source: Thomson Reuters

ASIA

Sustained evidence of a slowdown in trade, industrial production and retail sales in China will lead to a downward revision in our GDP growth projection for the next 18 months. The purchasing managers' index to be released in early June will show a weakened manufacturing sector (reading below 50) marking a seventh consecutive monthly decline. China expanded at an 8.1% y/y rate in the first quarter of the year. The government authorities are gearing decisively towards a pro-growth policy mix in the context of relatively well contained price pressures; indeed, consumer price inflation declined to 3.37% y/y in April 2012, down from 6.5% y/y in July 2011. We do anticipate coordinated monetary and fiscal stimuli to be put in place in the coming months. The Chinese central bank will lower reserve requirements to stimulate manageable credit-intensive economic activity during the process of rebalancing from investment to consumption. In the fiscal arena, tax cuts and a boost to basic infrastructure investment projects will become primary growth drivers. Additionally, further credit flows will be allocated to major projects under way.

Key Indicators for the week of May 28 - June 1

North America

Country	Date	Time	Indicator	Period	BNS	Consensus	Latest
US	05/29	09:00	S&P/Case-Shiller Home Price Index (y/y)	MAR	--	-2.7	-3.5
US	05/29	10:00	Consumer Confidence Index	MAY	--	69.5	69.2
US	05/30	07:00	MBA Mortgage Applications (w/w)	MAY 25	--	--	3.8
CA	05/30	08:30	IPPI (m/m)	APR	--	0.1	0.2
CA	05/30	08:30	Raw Materials Price Index (m/m)	APR	--	-2.0	-1.6
CA	05/30	09:00	Teranet HPI (y/y)	MAR	--	--	6.1
US	05/30	10:00	Pending Home Sales (m/m)	APR	--	-0.1	4.1
US	05/31	06:59	ICSC Chain Store Sales - Monthly (y/y)	MAY	--	--	0.6
US	05/31	08:15	ADP Employment Report	MAY	150.0	135.0	119.0
CA	05/31	08:30	Current Account (C$ bn a.r.)	1Q	--	-11.0	-10.3
US	05/31	08:30	Initial Jobless Claims (000s)	MAY 26	370	370	370
US	05/31	08:30	Continuing Claims (000s)	MAY 19	3265	3240	3260
US	05/31	08:30	GDP (q/q a.r.)	1Q S	2.0	1.9	2.2
US	05/31	08:30	GDP Deflator (q/q a.r.)	1Q S	--	1.5	1.5
US	05/31	09:45	Chicago PMI	MAY	--	57.0	56.2
CA	06/01	08:30	Real GDP (m/m)	MAR	0.4	0.3	-0.2
CA	06/01	08:30	Real GDP (q/q a.r.)	1Q	2.0	1.9	1.8
US	06/01	08:30	PCE Deflator (y/y)	APR	--	1.9	2.1
US	06/01	08:30	PCE ex. Food & Energy (y/y)	APR	--	2.0	2.0
US	06/01	08:30	Personal Consumption (m/m)	APR	0.3	0.3	0.3
US	06/01	08:30	Personal Income (m/m)	APR	0.1	0.3	0.4
US	06/01	08:30	Change in Nonfarm Payrolls (000s)	MAY	160.0	150.0	115.0
US	06/01	08:30	Change in Household Employment (000s)	MAY	--	--	-169.0
US	06/01	08:30	Unemployment Rate (%)	MAY	8.2	8.1	8.1
US	06/01	10:00	Construction Spending (m/m)	APR	0.3	0.4	0.1
US	06/01	10:00	ISM Manufacturing Index	MAY	53.5	54.0	54.8
US	06/01	17:00	Domestic Vehicle Sales (mn a.r.)	MAY	11.2	11.2	11.1
US	06/01	17:00	Total Vehicle Sales (mn a.r.)	MAY	14.6	14.4	14.4

Europe

Country	Date	Time	Indicator	Period	BNS	Consensus	Latest
UK	05/28	06:59	Nationwide House Prices (m/m)	MAY	--	0.1	-0.2
SP	05/29	06:59	Budget Balance YTD (€ bn)	APR	--	--	-19.7
TU	05/29	07:00	**Benchmark Repo Rate (%)**	MAY 29	**5.75**	**5.75**	**5.75**
GE	05/29	08:00	CPI (y/y)	MAY P	1.9	2.1	2.1
GE	05/29	08:00	CPI - EU Harmonized (m/m)	MAY P	-0.2	0.0	0.1
GE	05/29	08:00	CPI - EU Harmonized (y/y)	MAY P	2.1	2.2	2.2
HU	05/29	08:00	**Base Rate (%)**	MAY 29	**7.00**	**7.00**	**7.00**
SP	05/30	03:00	CPI (y/y)	MAY P	--	2.1	2.1
SP	05/30	03:00	CPI - EU Harmonized (y/y)	MAY P	2.1	2.0	2.0
EC	05/30	05:00	Business Climate Indicator	MAY	--	-0.7	-0.5
EC	05/30	05:00	Economic Confidence	MAY	--	91.9	92.8
EC	05/30	05:00	Industrial Confidence	MAY	--	-10.2	-9.0
GE	05/30	06:59	Retail Sales (m/m)	APR	0.4	0.2	0.8
UK	05/30	19:01	GfK Consumer Confidence	MAY	--	-32.0	-31.0
FR	05/31	02:45	Producer Prices (m/m)	APR	--	0.2	0.5
GE	05/31	03:55	Unemployment (000s)	MAY	-5.0	-6.5	19.0
GE	05/31	03:55	Unemployment Rate (%)	MAY	6.8	6.8	6.8
EC	05/31	05:00	Euro zone CPI Estimate (y/y)	MAY	2.4	2.5	2.6
IT	05/31	05:00	CPI (y/y)	MAY P	--	3.3	3.3
IT	05/31	05:00	CPI - EU Harmonized (m/m)	MAY P	0.1	0.1	0.9
IT	05/31	05:00	CPI - EU Harmonized (y/y)	MAY P	3.6	3.6	3.7
SP	05/31	06:59	Current Account (€ bn)	MAR	--	--	-5.9

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

Key Indicators for the week of May 28 - June 1

Europe *(continued from previous page)*

Country	Date	Time	Indicator	Period	BNS	Consensus	Latest
IT	06/01	03:45	Manufacturing PMI	MAY	--	43.5	43.8
IT	06/01	04:00	Unemployment Rate (%)	1Q	--	--	8.8
UK	06/01	04:30	Manufacturing PMI	MAY	--	49.7	50.5
EC	06/01	05:00	Unemployment Rate (%)	APR	10.9	11.0	10.9
IT	06/01	13:00	Budget Balance YTD (€ bn)	MAY	--	--	-30.5

Asia Pacific

Country	Date	Time	Indicator	Period	BNS	Consensus	Latest
CH	05/26	21:30	Industrial Profits YTD (y/y)	APR	--	--	-1.3
JN	05/28	19:30	Household Spending (y/y)	APR	--	2.5	3.4
JN	05/28	19:30	Jobless Rate (%)	APR	--	4.5	4.5
JN	05/28	19:50	Large Retailers' Sales (y/y)	APR	--	-0.3	5.1
JN	05/28	19:50	Retail Trade (m/m)	APR	--	0.1	-1.2
JN	05/28	19:50	Retail Trade (y/y)	APR	--	6.0	10.3
AU	05/29	21:30	Retail Sales (m/m)	APR	--	0.2	0.9
JN	05/30	19:50	Industrial Production (m/m)	APR P	--	0.5	1.3
AU	05/30	21:30	Building Approvals (m/m)	APR	--	0.5	7.4
JN	05/31	01:00	Housing Starts (y/y)	APR	--	3.2	5.0
IN	05/31	01:30	GDP (y/y)	1Q	--	6.0	6.1
TH	05/31	03:30	Exports (y/y)	APR	--	--	-6.8
TH	05/31	03:30	Imports (y/y)	APR	--	--	21.5
TH	05/31	03:30	Trade Balance (US$ mn)	APR	--	--	-1401.0
SK	05/31	20:00	Exports (y/y)	MAY	--	-1.0	-4.8
SK	05/31	20:00	Imports (y/y)	MAY	--	-2.4	-0.2
SK	05/31	20:00	Trade Balance (US$ mn)	MAY	--	2500.0	2118.0
CH	05/31	21:00	Manufacturing PMI	MAY	--	52.0	53.3
ID	06/01		Exports (y/y)	APR	--	--	5.5
ID	06/01		Imports (y/y)	APR	--	--	13.4
ID	06/01		Trade Balance (US$ mn)	APR	--	--	840.0
JN	06/01	01:00	Vehicle Sales (y/y)	MAY	--	--	92.0
IN	06/01	01:30	Exports (y/y)	APR	--	--	-5.7
IN	06/01	01:30	Imports (y/y)	APR	--	--	24.3
JN	06/01	07:59	Foreign Reserves (US$ bn)	MAY	--	--	1289.5

Latin America

Country	Date	Time	Indicator	Period	BNS	Consensus	Latest
CO	05/28	07:59	**Overnight Lending Rate (%)**	MAY 25	**5.25**	**5.25**	**5.25**
BZ	05/30	07:59	**SELIC Target Rate (%)**	MAY 30	**8.50**	**8.50**	**9.00**
CL	05/30	09:00	Unemployment Rate (%)	APR	--	6.7	6.6
PE	05/31	06:59	GDP (y/y)	1Q	--	--	6.0
BZ	05/31	08:00	Industrial Production SA (m/m)	APR	--	0.0	-0.5
BZ	05/31	08:00	Industrial Production (y/y)	APR	--	-1.5	-2.1
CL	05/31	09:00	Industrial Production (y/y)	APR	--	2.8	0.2
CL	05/31	09:00	Retail Sales (y/y)	APR	--	8.2	9.2
CO	05/31	12:00	Urban Unemployment Rate (%)	APR	--	10.8	11.0
PE	06/01	07:00	Consumer Price Index (m/m)	MAY	--	--	0.5
PE	06/01	07:00	Consumer Price Index (y/y)	MAY	--	--	4.1
BZ	06/01	08:00	GDP (IBGE) (q/q)	1Q	--	0.5	0.3
BZ	06/01	08:00	GDP (IBGE) (y/y)	1Q	2.1	1.3	1.4
BZ	06/01	09:00	PMI Manufacturing Index	MAY	--	--	49.3
BZ	06/01	14:00	Trade Balance (FOB) - Monthly (US$ mn)	MAY	--	--	881.0

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

Global Auctions for the week of May 28 - June 1

North America

Country	Date	Time	Event
US	05/29	11:00	U.S. Fed to Sell USD8-8.75 Bln Notes
US	05/29	11:30	U.S. to Sell 3-Month Bills
US	05/29	11:30	U.S. to Sell 6-Month Bills
US	05/30	11:00	U.S. Fed to Purchase USD4.5-5.25 Bln Notes
US	05/30	11:30	U.S. to Sell 52-Week Bills
US	05/30	11:30	U.S. to Sell 4-Week Bills
CA	05/30	12:00	Canada to Sell 30-Year Real Return Bonds
US	05/31	11:00	U.S. Fed to Purchase USD1.5-2 Bln Notes

Europe

Country	Date	Time	Event
IT	05/28	05:00	Italy to Sell Bond/Zero Coupon
IT	05/29	05:00	Italy to Sell Bills

Asia Pacific

Country	Date	Time	Event
JN	05/28	23:45	Japan to Sell 2-Year Bonds
CH	05/29	23:00	China to Sell 5-Year Bonds
JN	05/30	23:35	Japan to Sell 3-Month Bills
JN	06/01	04:00	Japan Auction for Enhanced-Liquidity

Latin America

Country	Date	Time	Event
BZ	05/31	11:00	Brazil to Sell Bills due 1/1/2016 - LTN
BZ	05/31	11:00	Brazil to Sell Bills due 7/1/2014 - LTN
BZ	05/31	11:00	Brazil to Sell Bills due 4/1/2013 - LTN

Source: Bloomberg, Scotia Economics.

Events for the week of May 28 - June 1

North America

Country	Date	Time	Event
US	05/30	13:20	Fed's Fisher Speaks on Economy in San Antonio, TX
US	05/30	13:30	Fed's Dudley to Speak on Regional Economy in New York
US	05/30	16:30	Fed's Rosengren Speaks in Worcester, Mass
US	05/31	08:00	Fed's Pianalto Speaks on Monetary Policy in Cleveland
US	05/31	10:30	IMF's Rice Holds Regular Bi-Monthly Briefing in Washington
US	05/31	21:00	Economic Development Summit in Oregon

Europe

Country	Date	Time	Event
EC	05/29	04:00	EU General Affairs Ministers Meet in Brussels
TU	05/29	07:00	Benchmark Repo Rate (%)
HU	05/29	08:00	Base Rate (%)
PO	05/29		Bank of Portugal Releases Financial Stability Report
EC	05/30	06:00	EU Issues Economic-Policy Recommendations to All States
EC	05/30	11:30	ECB's Draghi Speaks at Brussels Think Tank
EC	05/31	04:00	EU Trade Ministers Hold Meeting
EC	05/31	08:00	EU's Van Rompuy Speaks at Chatham House in London
EC	05/31		Rehn, Barroso, Monti Speak at Economic Conference in Brussels
EC	06/01	08:00	EU's Van Rompuy Gives Speech in Leuven

Asia Pacific

Country	Date	Time	Event
AU	05/27	20:00	RBA's Stevens Gives Speech to Payments Conference in Sydney

Latin America

Country	Date	Time	Event
CO	05/28		Overnight Lending Rate
BZ	05/30		SELIC Target - Central Bank

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	June 5, 2012	1.00	--
Federal Reserve – Federal Funds Target Rate	0.25	June 20, 2012	0.25	--
Banco de México – Overnight Rate	4.50	June 8, 2012	4.50	--

Fed: Jobs data due out on June 1 will further clarify the extent to which the 'full employment' aspect of the Fed's dual mandate is being satisfied. The possibility of downward revisions to Q1 GDP implies that the Fed's growth projections for 2012 might prove to be relatively aggressive. We do not anticipate any change to the Fed Funds Rate until 2014H2. BoC: The Bank of Canada revised its guidance for the path of its benchmark interest rate at its April 17 meeting, noting "in light of the reduced slack in the economy and firmer underlying inflation, some modest withdrawal of the present considerable monetary policy stimulus may become appropriate." Despite hawkish BoC rhetoric in April, a weaker global environment, a weaker-than-anticipated US economic situation, and disappointing domestic growth that is creating greater-than-estimated slack reduce the likelihood of BoC tightening in 2012.

Europe

Rate	Current Rate	Next Meeting	Scotia's Forecasts	Consensus Forecasts
European Central Bank – Refinancing Rate	1.00	June 6, 2012	0.75	--
Bank of England – Bank Rate	0.50	June 7, 2012	0.50	0.50
Swiss National Bank – Libor Target Rate	0.00	June 14, 2012	0.00	--
Central Bank of Russia – Refinancing Rate	8.00	June 15, 2012	8.00	--
Hungarian National Bank – Base Rate	7.00	May 29, 2012	7.00	7.00
Central Bank of the Republic of Turkey – 1 Wk Repo Rate	5.75	May 29, 2012	5.75	5.75
Sweden Riksbank – Repo Rate	1.50	July 4, 2012	1.50	--

The Turkish central bank is expected to hold the benchmark policy rate at 5.75% after its meeting next Tuesday. Inflation reached 11.14% y/y in April, its fastest pace since October 2008. However, this acceleration is largely the result of indirect tax / administered price increases as well as earlier currency weakness, and will likely be discounted by the central bank. Meanwhile, the current account deficit continued to moderate in March (on a cumulative 12-month basis). The Hungarian National Bank is also unlikely to adjust rates on Tuesday. Although inflation edged up in April (to 5.7% y/y from 5.5%) and remains well above the central bank's 3% target, the economic picture remains bleak. First-quarter GDP contracted by a disquieting 1.3% q/q and the manufacturing PMI sank in April to its lowest level since August 2009. Renewed currency weakness may preclude any notable moderation in inflation in the coming months; however, the central bank's bias will more likely be tilted to the easing side over the near term.

Asia Pacific

Rate	Current Rate	Next Meeting	Scotia's Forecasts	Consensus Forecasts
Bank of Japan – Target Rate	0.10	June 15, 2012	0.10	--
Reserve Bank of Australia – Cash Target Rate	3.75	June 5, 2012	3.75	3.75
Reserve Bank of New Zealand – Cash Rate	2.50	June 13, 2012	2.50	2.50
People's Bank of China – Lending Rate	6.56	TBA	--	--
Reserve Bank of India – Repo Rate	8.00	June 18, 2012	8.00	--
Bank of Korea – Bank Rate	3.25	June 7, 2012	3.25	--
Bank of Thailand – Repo Rate	3.00	June 13, 2012	3.00	--
Bank Indonesia – Reference Interest Rate	5.75	June 12, 2012	5.75	--

Latin America

Rate	Current Rate	Next Meeting	Scotia's Forecasts	Consensus Forecasts
Banco Central do Brasil – Selic Rate	9.00	May 30, 2012	8.50	8.50
Banco Central de Chile – Overnight Rate	5.00	June 14, 2012	5.00	--
Banco de la República de Colombia – Lending Rate	5.25	May 28, 2012	5.25	5.25
Banco Central de Reserva del Perú – Reference Rate	4.25	June 7, 2012	4.25	4.25

We expect the central bank of Brazil to maintain its expansionary monetary policy stance and cut the reference rate by 50 basis points (bps) to 8.50% at the next meeting. This will be the seventh consecutive cut since last September, a cumulative 400 bps reduction, and will take the rate below 8.75%, the all-time low reached in mid-2009. The authorities are trying to boost the economy by loosening monetary conditions amid a significant economic deceleration. The central bank of Colombia will likely leave its reference rate unchanged at 5.25% at the next monetary meeting. In the last committee minutes, the authorities signaled that more actions could be taken to cool credit growth, leaving the door open for further increases in the reference rate. However, the ministry of finance recently announced an increase in reserve requirements, in an attempt to moderate consumer lending. Amid recent financial market volatility and European debt concerns we expect the central bank to wait for more data before they change the monetary stance.

Africa

Rate	Current Rate	Next Meeting	Scotia's Forecasts	Consensus Forecasts
South African Reserve Bank – Repo Rate	5.50	July 19, 2012	5.50	--

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

Forecasts as at May 4, 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	3.4	3.9				
Canada	2.2	2.5	2.1	2.2	2.1	2.9	2.1	2.1
United States	1.8	1.7	2.3	2.4	2.5	3.1	2.6	2.2
Mexico	2.1	3.9	3.6	3.7	4.9	3.8	3.9	4.0
United Kingdom	2.0	0.7	0.5	1.8	2.1	4.2	2.8	2.7
Euro Zone	1.4	1.5	-0.5	0.9	2.1	2.7	2.2	1.9
Japan	0.9	-0.7	2.0	1.7	-0.3	-0.2	0.1	0.3
Australia	3.1	2.0	3.3	3.4	3.1	3.1	2.5	2.8
China	9.5	9.3	8.4	8.9	2.3	4.1	4.0	4.4
India	7.6	10.0	7.0	7.4	6.4	7.7	6.5	6.8
South Korea	4.6	3.6	3.4	4.2	3.1	4.8	3.3	3.0
Thailand	4.4	5.7	5.0	4.5	2.7	3.5	3.0	2.8
Brazil	3.7	2.7	3.5	4.5	6.6	6.5	5.5	5.0
Chile	4.6	6.1	5.0	5.9	3.4	4.4	3.6	3.2
Peru	5.5	6.8	5.5	5.6	2.4	4.7	3.0	2.5
Central Bank Rates (%, end of period)	12Q1	12Q2f	12Q3f	12Q4f	13Q1f	13Q2f	13Q3f	13Q4f
Bank of Canada	1.00	1.00	1.00	1.00	1.00	1.25	1.50	1.75
Federal Reserve	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25
European Central Bank	1.00	0.75	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	3.75	3.75	3.75	3.75	3.75	4.00	4.00
Exchange Rates (end of period)								
Canadian Dollar (USDCAD)	1.00	1.00	0.99	0.98	0.97	0.97	0.97	0.96
Canadian Dollar (CADUSD)	1.00	1.00	1.01	1.02	1.03	1.03	1.03	1.04
Euro (EURUSD)	1.33	1.29	1.27	1.25	1.25	1.26	1.28	1.29
Sterling (GBPUSD)	1.60	1.60	1.62	1.63	1.65	1.66	1.67	1.68
Yen (USDJPY)	83	82	83	85	86	86	87	87
Australian Dollar (AUDUSD)	1.03	1.07	1.08	1.09	1.10	1.10	1.11	1.11
Chinese Yuan (USDCNY)	6.3	6.3	6.2	6.2	6.2	6.1	6.1	6.1
Mexican Peso (USDMXN)	12.8	12.8	13.0	13.1	13.2	13.1	13.1	13.3
Brazilian Real (USDBRL)	1.83	1.80	1.83	1.85	1.83	1.85	1.86	1.90
Commodities (annual average)	2000-10	2011	2012f	2013f				
WTI Oil (US$/bbl)	54	95	105	105				
Brent Oil (US$/bbl)	52	111	120	120				
Nymex Natural Gas (US$/mmbtu)	5.81	4.03	2.50	2.75				
Copper (US$/lb)	1.93	4.00	3.85	3.70				
Zinc (US$/lb)	0.75	0.99	0.94	1.10				
Nickel (US$/lb)	7.36	10.38	8.50	8.00				
Gold, London PM Fix (US$/oz)	586	1,569	1,650	1,600				
Pulp (US$/tonne)	694	977	875	915				
Newsprint (US$/tonne)	575	640	650	670				
Lumber (US$/mfbm)	273	255	265	310				

[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.

Canada	2011	11Q4	12Q1	Latest	
Real GDP (annual rates)	2.5	1.8			
Current Acc. Bal. (C$B, ar)	-48.3	-41.3			
Merch. Trade Bal. (C$B, ar)	2.3	14.9	10.5	4.2	(Mar)
Industrial Production	3.5	3.0		1.3	(Feb)
Housing Starts (000s)	193	199	207	245	(Apr)
Employment	1.6	1.2	0.9	1.5	(Apr)
Unemployment Rate (%)	7.5	7.5	7.4	7.3	(Apr)
Retail Sales	4.1	4.2	4.3	4.1	(Mar)
Auto Sales (000s)	1588	1603		1707	(Feb)
CPI	2.9	2.7	2.3	2.0	(Apr)
IPPI	4.6	3.9	1.6	-0.9	(Mar)
Pre-tax Corp. Profits	15.0	13.3			

United States	2011	11Q4	12Q1	Latest	
Real GDP (annual rates)	1.7	3.0	2.2		
Current Acc. Bal. (US$B, ar)	-473	-496			
Merch. Trade Bal. (US$B, ar)	-738	-745	-784	-811	(Mar)
Industrial Production	4.1	4.0	3.9	5.1	(Apr)
Housing Starts (millions)	0.61	0.68	0.71	0.72	(Apr)
Employment	1.1	1.3	1.6	1.3	(Apr)
Unemployment Rate (%)	9.0	8.7	8.3	8.1	(Apr)
Retail Sales	8.2	7.5	6.5	6.1	(Apr)
Auto Sales (millions)	12.7	13.4	14.5	14.4	(Apr)
CPI	3.2	3.3	2.8	2.3	(Apr)
PPI	6.0	5.4	3.4	1.9	(Apr)
Pre-tax Corp. Profits	4.2	9.3			

Mexico	2011	11Q4	12Q1	Latest	
Real GDP	3.9	3.9	4.6		
Current Acc. Bal. (US$B, ar)	-9.0	-7.5	-0.2		
Merch. Trade Bal. (US$B, ar)	-1.5	-2.9	7.1	6.7	(Apr)
Industrial Production	4.0	3.5	4.5	3.1	(Mar)
CPI	3.4	3.5	3.9	3.4	(Apr)

Brazil	2011	11Q4	12Q1	Latest	
Real GDP	2.5	1.2			
Current Acc. Bal. (US$B, ar)	-52.5	-63.2	-48.3		
Merch. Trade Bal. (US$B, ar)	29.8	27.0	9.7	10.6	(Apr)
Industrial Production	0.3	-1.9	-3.3	-3.9	(Mar)
CPI	6.8	6.7		6.6	(Jan)

Chile	2011	11Q4	12Q1	Latest	
Real GDP	6.0	4.5	5.6		
Current Acc. Bal. (US$B, ar)	0.0	-5.1	-1.4		
Merch. Trade Bal. (US$B, ar)	10.0	9.4	11.1	12.6	(Apr)
Industrial Production	6.9	2.0	3.5	0.2	(Mar)
CPI	3.3	4.0	4.1	3.5	(Apr)

Italy	2011	11Q4	12Q1	Latest	
Real GDP	0.5	-0.4	-1.3		
Current Acc. Bal. (US$B, ar)	-0.07	-0.03	-0.08	-0.04	(Mar)
Merch. Trade Bal. (US$B, ar)	-34.2	-8.3	-17.5	32.7	(Mar)
Industrial Production	0.2	-3.1	-5.2	-5.5	(Mar)
CPI	2.8	3.3	3.4	3.4	(Apr)

Germany	2011	11Q4	12Q1	Latest	
Real GDP	3.1	2.0	1.2		
Current Acc. Bal. (US$B, ar)	204.1	256.1	215.1	312.9	(Mar)
Merch. Trade Bal. (US$B, ar)	216.1	220.7	223.1	216.5	(Mar)
Industrial Production	8.0	3.5	1.0	1.5	(Mar)
Unemployment Rate (%)	7.0	6.9	6.8	6.8	(Apr)
CPI	2.3	2.3	2.2	2.1	(Apr)

France	2011	11Q4	12Q1	Latest	
Real GDP	1.7	1.2	0.3		
Current Acc. Bal. (US$B, ar)	-60.1	-58.2	-53.2	-54.7	(Mar)
Merch. Trade Bal. (US$B, ar)	-51.0	-45.9	-53.2	-52.0	(Mar)
Industrial Production	2.5	0.5	-1.4	-0.9	(Mar)
Unemployment Rate (%)	9.7	9.8	10.0	10.0	(Mar)
CPI	2.1	2.4	2.3	2.1	(Apr)

Euro Zone	2011	11Q4	12Q1	Latest	
Real GDP	1.5	0.7	0.0		
Current Acc. Bal. (US$B, ar)	-4	183	-43	119	(Mar)
Merch. Trade Bal. (US$B, ar)	6.4	76.9	9.7	138.5	(Mar)
Industrial Production	3.6	-0.1	-1.6	-2.0	(Mar)
Unemployment Rate (%)	10.1	10.5	10.8	10.9	(Mar)
CPI	2.7	2.9	2.7	2.6	(Apr)

United Kingdom	2011	11Q4	12Q1	Latest	
Real GDP	0.7	0.5	-0.1		
Current Acc. Bal. (US$B, ar)	-46.4	-45.4			
Merch. Trade Bal. (US$B, ar)	-159.8	-152.5	-157.4	-162.5	(Mar)
Industrial Production	-1.2	-3.0	-3.0	-2.6	(Mar)
Unemployment Rate (%)	8.1	8.4		8.2	(Feb)
CPI	4.5	4.7	3.5	3.0	(Apr)

Japan	2011	11Q4	12Q1	Latest	
Real GDP	-0.7	-0.5	2.6		
Current Acc. Bal. (US$B, ar)	119.2	48.0	114.5	231.4	(Mar)
Merch. Trade Bal. (US$B, ar)	-33.6	-76.2	-71.2	-70.7	(Apr)
Industrial Production	-2.3	0.0	2.7	15.9	(Mar)
Unemployment Rate (%)	4.6	4.5	4.5	4.5	(Mar)
CPI	-0.3	-0.3	0.3	0.5	(Apr)

Australia	2011	11Q4	12Q1	Latest	
Real GDP	2.0	2.3			
Current Acc. Bal. (US$B, ar)	-33.0	-38.0			
Merch. Trade Bal. (US$B, ar)	35.8	29.3	2.7	2.4	(Mar)
Industrial Production	-0.1	2.1			
Unemployment Rate (%)	5.1	5.2	5.2	4.9	(Apr)
CPI	3.4	3.1	1.6		

China	2011	11Q4	12Q1	Latest	
Real GDP	10.4	8.9			
Current Acc. Bal. (US$B, ar)	201.7				
Merch. Trade Bal. (US$B, ar)	155.0	193.0	3.5	221.1	(Apr)
Industrial Production	12.8	12.8	9.3	9.3	(Apr)
CPI	4.1	4.1	3.6	3.4	(Apr)

South Korea	2011	11Q4	12Q1	Latest	
Real GDP	3.6	3.3	2.8		
Current Acc. Bal. (US$B, ar)	26.5	46.0	10.5	36.5	(Mar)
Merch. Trade Bal. (US$B, ar)	30.8	36.6	6.0	25.4	(Apr)
Industrial Production	6.9	5.2	2.7	0.3	(Mar)
CPI	4.0	4.0	3.0	2.5	(Apr)

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

Source: Bloomberg, Scotia Economics.

Interest Rates (%, end of period)

Canada	11Q4	12Q1	May/18	May/25*	United States	11Q4	12Q1	May/18	May/25*
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	0.80	0.91	1.01	0.96	3-mo. T-bill	0.01	0.07	0.08	0.09
10-yr Gov't Bond	1.94	2.11	1.89	1.82	10-yr Gov't Bond	1.88	2.21	1.72	1.75
30-yr Gov't Bond	2.49	2.66	2.43	2.37	30-yr Gov't Bond	2.89	3.34	2.81	2.84
Prime	3.00	3.00	3.00	3.00	Prime	3.25	3.25	3.25	3.25
FX Reserves (US$B)	65.7	69.2	69.4	(Apr)	FX Reserves (US$B)	136.9	138.0	141.4	(Apr)
Germany					**France**				
3-mo. Interbank	1.35	0.71	0.61	0.60	3-mo. T-bill	-0.06	0.07	0.06	0.07
10-yr Gov't Bond	1.83	1.79	1.43	1.37	10-yr Gov't Bond	3.15	2.89	2.85	2.52
FX Reserves (US$B)	66.9	67.9	68.9	(Apr)	FX Reserves (US$B)	48.6	49.2	50.2	(Apr)
Euro Zone					**United Kingdom**				
Refinancing Rate	1.00	1.00	1.00	1.00	Repo Rate	0.50	0.50	0.50	0.50
Overnight Rate	0.63	0.39	0.34	0.34	3-mo. T-bill	0.37	0.37	0.39	0.37
FX Reserves (US$B)	316.7	319.9	325.5	(Apr)	10-yr Gov't Bond	1.98	2.20	1.83	1.75
					FX Reserves (US$B)	79.3	82.4	84.3	(Apr)
Japan					**Australia**				
Discount Rate	0.30	0.30	0.30	0.30	Cash Rate	4.25	4.25	3.75	3.75
3-mo. Libor	0.13	0.13	0.13	0.13	10-yr Gov't Bond	3.67	3.98	3.08	3.17
10-yr Gov't Bond	0.99	0.99	0.83	0.89	FX Reserves (US$B)	42.8	47.7	45.6	(Apr)
FX Reserves (US$B)	1258.2	1247.8	1248.9	(Apr)					

Exchange Rates (end of period)

USDCAD	1.02	1.00	1.02	1.03	¥/US$	76.91	82.87	79.02	79.64
CADUSD	0.98	1.00	0.98	0.97	US¢/Australian$	1.02	1.03	0.98	0.98
GBPUSD	1.554	1.601	1.582	1.565	Chinese Yuan/US$	6.30	6.30	6.33	6.34
EURUSD	1.296	1.334	1.278	1.252	South Korean Won/US$	1152	1133	1173	1185
JPYEUR	1.00	0.90	0.99	1.00	Mexican Peso/US$	13.936	12.811	13.816	14.020
USDCHF	0.94	0.90	0.94	0.96	Brazilian Real/US$	1.867	1.827	2.024	1.996

Equity Markets (index, end of period)

United States (DJIA)	12218	13212	12369	12503	U.K. (FT100)	5572	5768	5268	5352
United States (S&P500)	1258	1408	1295	1321	Germany (Dax)	5898	6947	6271	6340
Canada (S&P/TSX)	11955	12392	11281	11549	France (CAC40)	3160	3424	3008	3048
Mexico (Bolsa)	37078	39521	36875	37645	Japan (Nikkei)	8455	10084	8611	8580
Brazil (Bovespa)	56754	64511	54513	54823	Hong Kong (Hang Seng)	18434	20556	18952	18713
Italy (BCI)	806	859	725	720	South Korea (Composite)	1826	2014	1782	1824

Commodity Prices (end of period)

Pulp (US$/tonne)	890	870	900	900	Copper (US$/lb)	3.43	3.85	3.54	3.49
Newsprint (US$/tonne)	640	640	640	640	Zinc (US$/lb)	0.83	0.91	0.87	0.86
Lumber (US$/mfbm)	261	266	308	297	Gold (US$/oz)	1531.00	1662.50	1589.50	1569.50
WTI Oil (US$/bbl)	98.83	103.02	91.48	90.99	Silver (US$/oz)	28.18	32.43	28.48	28.24
Natural Gas (US$/mmbtu)	2.99	2.13	2.74	2.57	CRB (index)	305.30	308.46	290.43	281.87

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

Fixed Income Strategy (London)

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Fixed Income Strategy (Paris)

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