Foreign Exchange Outlook

Low inflationary pressures and disappointing growth have laid the foundation for loose monetary policy; however, as we enter the second half of the year the Fed appears poised to begin stepping away from its bond buying program supporting a strong USD and rising yields. Nevertheless, slowing the pace of bond purchases (QE) is not the same as tightening policy, leaving investors still on the hunt for yield, potentially fueling bubbles across a host of emerging markets asset classes as well as in non-US housing and global equities. Meanwhile, substantial JPY weakness juxtaposed against CNY strength highlights a notable FX divergence within the Asian block.

For the USD to continue to broadly strengthen, the Fed will need to step away from QE, implying a strong June employment print. Accordingly in the near-term, we expect broad FX moves to be data dependent. Beyond that, we expect the EUR, JPY and GBP to weaken against the USD into year-end mainly on relative central bank policy and growth outlooks. Several other currencies, including the CAD, MXN, THB and CHF, are expected to be somewhat range-bound, while the AUD, NZD, NOK, PEN and KRW are expected to appreciate.

Forecast Highlights

Americas	USD	USD is poised to strengthen against EUR, GBP, JPY into year-end.
	CAD	Recent weakness is on the back of USD strength. Range-bound from here.
	MXN	Similar to CAD, the risk is near-term weakness followed by a retracement.
Asia / Pacific	CNY	A fresh record high in the currency suggest CNY is approaching fair value.
	JPY	BoJ policy has weakened the yen; more to come closing 2013 at 105.
	THB	A rate cut and broad USD eases THB strength. Expected to be range-bound from here.
Europe	EUR	Recent resiliency is likely to fade; we hold a year-end target of 1.25.
	GBP	A new central bank head is a key risk; we expect GBP weakness.

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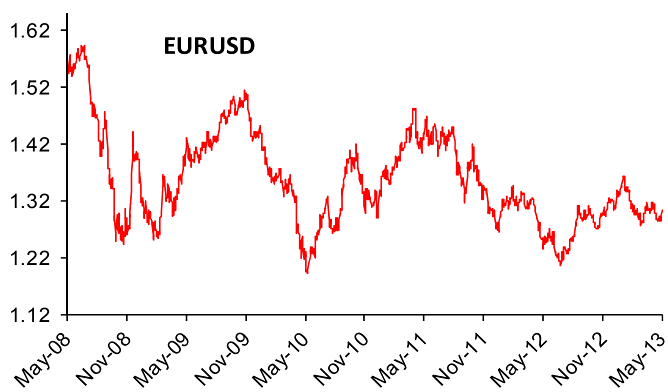
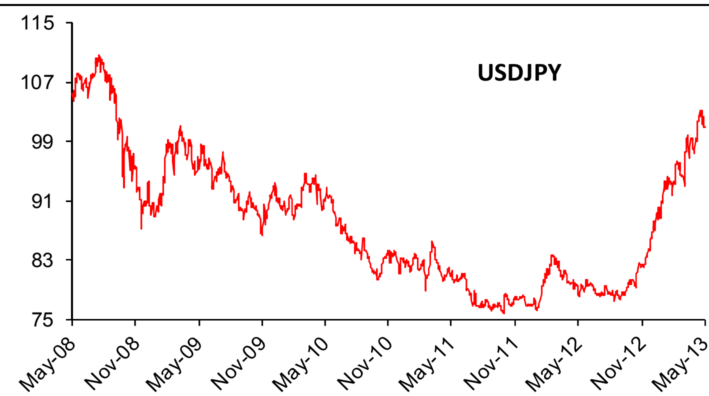
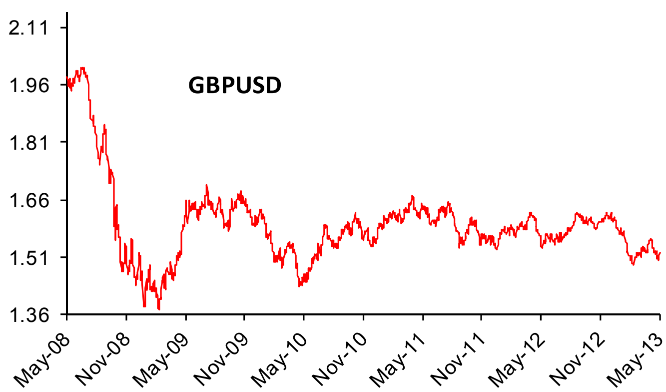
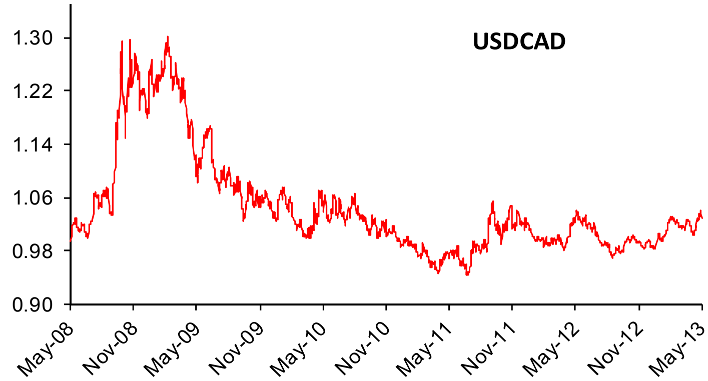
Core Exchange Rates

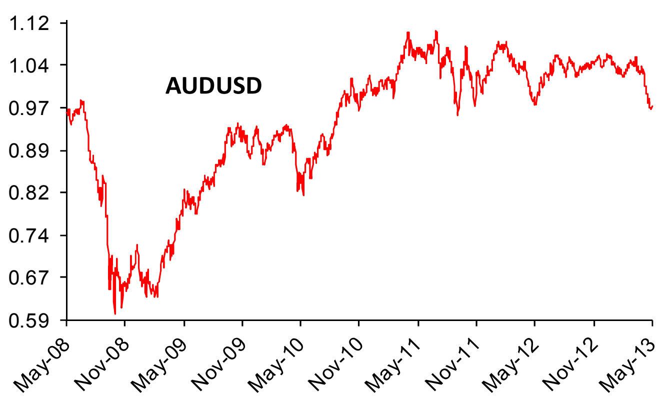
May 30, 2013		Spot	Q1a 13	Q2 13	Q3 13	Q4 13	Q1 14	Q2 14	Q3 14	Q4 14
EURUSD	Scotiabank	1.30	1.28	1.27	1.26	1.25	1.25	1.24	1.24	1.23
	Consensus*			1.30	1.29	1.28	1.28	1.27	1.27	1.27
USDJPY	Scotiabank	100.9	94	102	104	105	106	107	109	110
	Consensus*			100	101	101	102	102	102	102
GBPUSD	Scotiabank	1.52	1.52	1.49	1.47	1.45	1.45	1.45	1.44	1.44
	Consensus*			1.51	1.50	1.49	1.49	1.49	1.49	1.50
USDCAD	Scotiabank	1.03	1.02	1.05	1.03	1.02	1.02	1.01	1.00	1.00
	Consensus*			1.01	1.01	1.01	1.01	1.01	1.02	1.02
AUDUSD	Scotiabank	0.97	1.04	0.96	0.98	1.02	1.04	1.06	1.08	1.08
	Consensus*			1.03	1.02	1.01	1.00	0.99	0.99	0.98
USDMXN	Scotiabank	12.77	12.33	12.08	12.09	12.25	12.33	12.19	12.24	12.38
	Consensus*			12.34	12.10	12.12	12.09	12.11	12.23	12.35

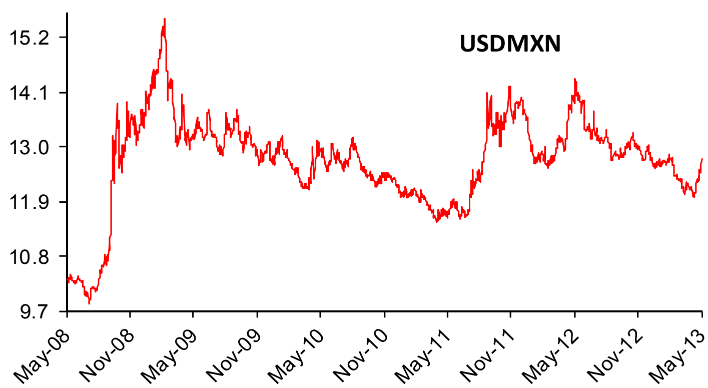












(*) **Source:** Consensus Economics Inc. May 2013

MARKET TONE & FUNDAMENTAL FOCUS

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Expectations for Federal Reserve (Fed) policy underwent an important shift in May. Perceptions that the US economy was firming combined with hawkish comments from several Fed members saw markets quickly price in a shift in stance - one where the Fed would lean towards stepping away from its bond purchase program (QE3). The fallout was a sharp rise in 10-year yields that sent them above 2.0%, a steepening in the yield curve and a stronger US dollar (USD). The stated Fed criteria for a decrease in monthly bond purchases has been a substantial improvement in the labour force; as the Fed tone begins to shift it leaves the June 7th nonfarm payroll release as a crucial data point. A print close to 200k will support a broad based USD rally; however, a disappointment will be faced with important questions about the strength of the labour market and is likely to weigh heavily on the USD – replaying the scenario from the spring of 2012 when a strong USD in May (driven by Europe-related risk aversion) was followed by a weak USD in June as nonfarm disappointed and the Fed was forced to consider more aggressive measures.

The shifting Fed outlook is the most important USD driver; however, for the non-G4 currencies it is this combined with the potential retaliation to loose G4 policy that is driving FX. The term currency war is rearing its head less often, but the underlying theme remains relevant. Every country wants a weaker currency to help stimulate growth, but the math does not work. Loose and aggressive G4 central bank policy has led smaller economies to retaliate by keeping policy more accommodative than they otherwise would have (in May, several countries cut interest rates including: Australia, South Korea, India, Poland, Israel, Turkey, Hungary and Thailand) as well as some moving towards more aggressive measures like capital controls and intervention to help offset currency strength. The country that appears most able to sustain some currency appreciation is the US, with weakness expected to play out in the euro zone, UK and Japan. Many of the smaller open economies are likely to see their currencies hold their own against the USD.

In the NAFTA zone there has been a lot of bad news priced into the Canadian dollar (CAD), including a central bank that will soon be under the leadership of Stephen Poloz, who is widely believed to favour exporters and a weaker CAD; a soft housing markets; and the risks that increasing US energy product pose to Canada's resource exports. However, Canada remains a strong AAA rated sovereign, with an improving growth profile (supported in part by a US recovery) and accordingly even as the CAD has fallen victim to recent weakness, over the medium term it is not expected to shift sustainably away from its current range. A disappointing Mexican growth trajectory and a stronger USD have pressured the Mexican peso (MXN) as of late; however, we expect the MXN to trend back towards 12.25 by year-end as the US recovers and other fears abate. In Latam more generally, we expect the Peruvian sol (PEN) to outperform the Chilean peso (CLP), the Brazilian real (BRL) and the Colombian peso (COP).

In Europe, a broadly stronger USD, an ECB interest rate cut, a building discussion on the potential of negative interest rates but few measures to help reduce fragmentation in credit markets combined with a large euro (EUR) short position (reported by the CFTC as of May 21 as -$13 billion) should all be weighing heavily on the EUR. However, in May the EUR was largely range-bound, failing to break to a fresh year-to-date low. This suggests that there are still large buyers supporting the currency. We expect the EUR to trend lower this year as it falls victim to disappointing structural reforms, a lack of progress on the banking union, ongoing credit fragmentation, negative sentiment and a broadly stronger USD. The British pound (GBP) is also at risk of further downside, weighed down by low growth, elevated inflation, an upcoming change in leadership at the Bank of England and negative sentiment. Swiss National Bank (SNB) President Jordan recently suggested that the level of the EURCHF floor could at some point be adjusted, fueling expectations that the SNB will rise the floor to 1.25. We have maintained a year-end forecast of 1.22; if we are wrong it is likely that the EURCHF will close the year near current levels. The outlook for Swedish krona (SEK) is relatively stable against the USD, but we expect outperformance from the Norwegian krone (NOK).

The Asia/Pacific region faces significant currency pressure. Japanese government and central bank policy has supported a 14% year-to-date (to May 28) drop in the Japanese yen (JPY) against the USD, while the Chinese yuan (CNY) is one of the strongest currencies, having rallied almost 2% against the USD with USDCNY approaching our year-end target of 6.10. The rest of the Asian block lies between these two. It is undeniable that the Asian block of currencies faces a shift in trade patterns and outlooks on the back of a substantially weaker JPY but stronger CNY. In Thailand, the appreciation in the THB was halted with a broad USD rally and the central bank's decision to cut interest rates. We do not expect a further round of material strength to emerge in 2013 and expect instead that the Thai baht (THB) is nearing fair value. For many of the other Asian currencies, including the Malaysian Ringgit (MYR), the Indian Rupee (INR), the Philippine peso (PHP), the Singapore dollar (SGP) and the Korean won (KRW), near-term weakness is likely to continue before reversing later this year. For the AUD, a deceleration in the outlook for Chinese growth, a surprise interest cut by the Reserve Bank of Australia (RBA) and broad USD strength have all weighed heavily on the currency; however, we expect that this shifts as markets gain more comfort with a Chinese GDP close to 8%, the RBA moves away from rate cuts and sentiment shifts to a more neutral stance.

CANADA
Currency Outlook

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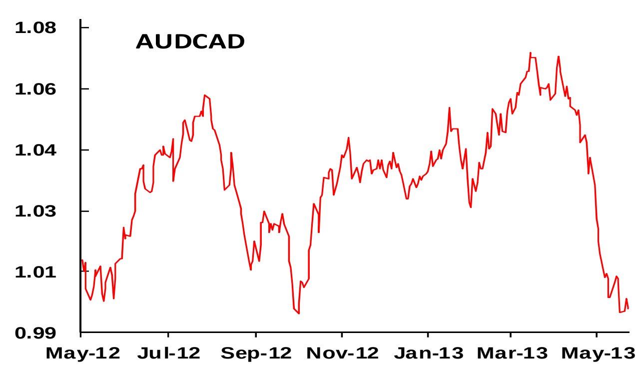
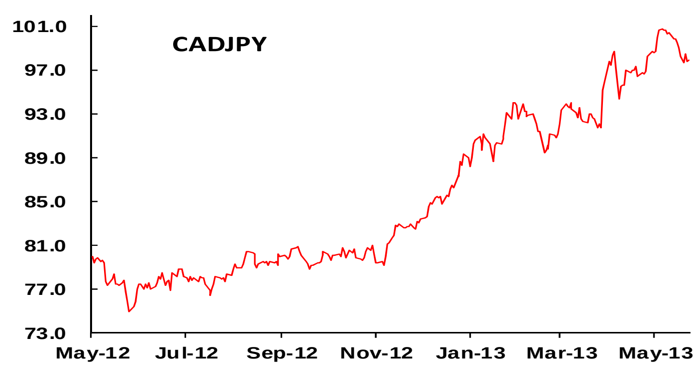
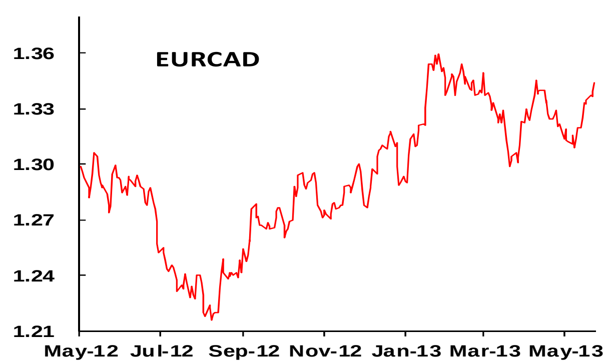
In May the Canadian dollar (CAD) traded to a fresh year-to-date low and flirted with its June 2012 low of 0.9573. There have been four major reasons for CAD weakness in May. The first is a US economic backdrop that is expected to outperform the other G7 economies, including Canada. Accordingly on a relative growth metric, the US is well positioned. In terms of relative central bank policy, a strengthening economic context has allowed the Federal Reserve to move towards a time when the labour force will be showing substantial improvement and accordingly the central bank will be able to begin stepping away from its bond buying program (QE3). This is an important shift and one that has supported a broadly stronger USD against all the major currencies, not just the CAD. On the domestic front, the naming of Stephen Poloz as the next Governor of the Bank of Canada (BoC) has added to CAD weakness. His experience at the Export Development Corporation will be valuable; however, it also lends easily to speculation that he might sympathize with exporters who have faced a strong CAD and that on the back of this, BoC policy might prove far less supportive of the CAD going forward than it has been. The second is the outlook for the Canadian housing market, which some have predicted is positioned for a collapse. We recognize there are risks, but expect a moderation in housing (not a collapse) driven by increased regulation, but see the other housing drivers as proving more supportive (low interest rates until 2015, no significant change to immigration trends, etc.). This could prove a pleasant surprise. Finally, the impact of US domestic oil production on Canadian oil exports is a major concern. To date, as US imports have fallen, Canadian exports have risen (as the US has slowed imports from other regions, namely Mexico, Venezuela, etc.). In addition, forecasts (including those from the International Monetary Fund) suggest that Canadian exports of oil will rise over the next 10 years. Accordingly, there are bad news priced into the CAD, none of which focuses on Canada's strong fiscal and debt positions: its important economic links with the US recovery (namely through forestry and autos); or that on a relative basis Canada is still an attractive destination for official flows. We continue to believe that for every positive driver of CAD there is an offsetting negative factor and vice-versa. This leaves the CAD vulnerable to remaining within a range, slightly weaker than parity, but unable to shift substantially and sustainably away from parity.

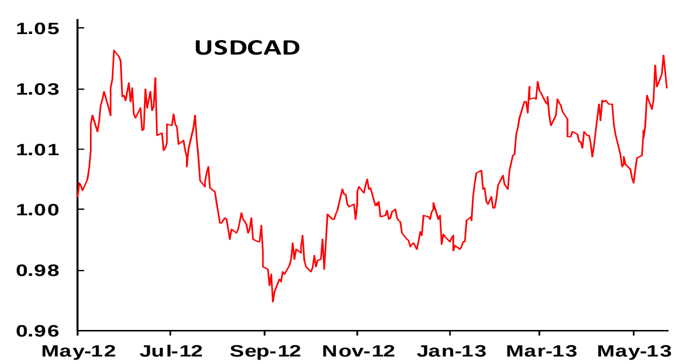
Canadian Dollar Cross-Currency Trends

FX Rate	Spot 30-May	13Q1a	13Q2f	13Q3f	13Q4f	14Q1f	14Q2f	14Q3f	14Q4f
AUDCAD	1.00	1.06	1.01	1.01	1.04	1.06	1.07	1.08	1.08
CADJPY	97.9	92.6	97.1	101.0	102.9	103.9	105.9	109.0	110.0
EURCAD	1.34	1.30	1.33	1.30	1.28	1.28	1.25	1.24	1.23
USDCAD	1.03	1.02	1.05	1.03	1.02	1.02	1.01	1.00	1.00









Canada and United States
Fundamental Commentary

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UNITED STATES - The recent string of weak economic data points to a loss of momentum in the US economy. In April, housing starts unexpectedly declined, headline CPI slid to a 30-month low and despite employment gains, wages and total hours worked deteriorated. Industrial production also started the second quarter on a softer note, dragged down by lower utilities output and reduced durable goods and motor vehicles & parts production. Meanwhile, the ISM manufacturing index declined and the Philadelphia Fed index slipped into contraction territory, highlighting a slowdown in manufacturing activity, although strength in durable goods orders in April point to a rebound. These developments indicate cautious private sector spending growth alongside the drag from fiscal restraint in the second quarter. Nevertheless, improving household finances and gradually strengthening labour markets are expected to support consumer spending. In May, consumer confidence climbed to the highest level since February 2008, bolstered by rising home and equity prices. These factors, combined with lower fuel prices, helped to offset the impact of higher payroll taxes, which bode well for retail sales in April. Going forward, with consumers more optimistic about the future, household spending will likely drive growth in the second half of the year. In turn, and further reinforced by rising hiring intentions by small and medium size businesses, employment growth should gain momentum. Despite the drop in housing starts in April, higher new and existing home sales, rising home prices, and strong permits data suggest the residential construction recovery will continue. Increasing new orders and lean inventories signals a pickup in manufacturing activity in the coming months.

CANADA - Canadian real GDP likely advanced around 2½% q/q SAAR in the first quarter of 2013. The better than expected performance reflects strength in net exports and consumer spending. In March, Canadian merchandise trade eked out a surplus for the first time in over a year, as exports rose sharply and imports held flat. Export volumes growth is now tracking over 2% q/q SAAR in Q1, relative to a mere 0.3% improvement in import volumes. Retail sales volumes also recorded a healthy advance in the first quarter and the Canadian labour market bounced back creating 12.5k jobs in April. Nevertheless, after several months of volatility, the trend pace of employment growth has weakened and consumer spending growth is relatively sluggish. Housing starts also continued to trend lower to roughly 175k in April, while home prices increased at the slowest pace in two years and inflationary pressures moderated further. In addition, manufacturing sales declined in March, largely due to lower petroleum prices. Notwithstanding a strong start to the year, domestic imbalances and the weak global economic backdrop suggest Canada's economic momentum will remain modest through year-end. Forward-looking indicators point to weakness in exports and manufacturing sales in Q2, due to the recent drop in unfilled and new orders. Meanwhile, lackluster employment growth and ongoing household deleveraging continue to subdue consumer spending and new home construction. Meanwhile, fierce retail competition and modest wage growth will keep inflation well anchored. As private-sector demand in the US and global activity picks up in the second half of this year and 2014, growth in the Canadian economy is expected to improve, driven by exports and business investment.

Monetary Policy Commentary

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UNITED STATES - To taper or not to taper asset purchases? That remains the main question for the Fed, and the recent barrage of Fedspeak obscured rather than clarified the time-frame for asset purchase tapering. We lean towards an emphasis on NY Fed President Dudley's argument that data from the sequester period are required before the FOMC can decide one way or the other – pushing the time frame for a decision through to the September meeting (or even beyond), and not the upcoming June meeting as implied by the now-stale minutes from the May 1st FOMC decision. Indeed, we think that a down-turn in the data mid-summer (which we think likely) could push this whole debate into late 2013 or even 2014. Consequently, our view remains that everything's contingent on the economic data, meaning that non-farm Fridays are becoming monetary policy events on par with FOMC Wednesdays.

CANADA - We continue to expect the Bank of Canada (BoC) to hold the overnight rate at 1% through our full forecast horizon pushing through to the end of 2014 with risks of a longer hold contingent on developments in the Canadian macro-economy as well as US monetary policy. Markets are no longer pricing in odds of a BoC cut and in fact are pricing in a modest probability of a BoC rate hike one year out. We think that the shift in forward rates has more to do with developments in US interest rate markets that have seen US 2-year bond yields rise than a fundamental view on the BoC, which we still expect will be constrained by a slowing household sector, a peak in natural resources-related investment, and sluggish US growth throughout our forecast horizon.

EUROPE
Currency Outlook

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EURO ZONE - A broadly stronger USD, an ECB interest rate cut, a building discussion on the potential of negative interest rates and a large EUR short position (reported by the CFTC as of May 21 as -$13 billion) and still the EUR failed to break to a fresh year-to-date low in May. This suggests that there are still significant buyers of the EUR offsetting the large short community and hints that the EUR is likely less vulnerable to downside risk than many believe. Still we expect it to trend lower and hold a year-end EURUSD target of 1.25.

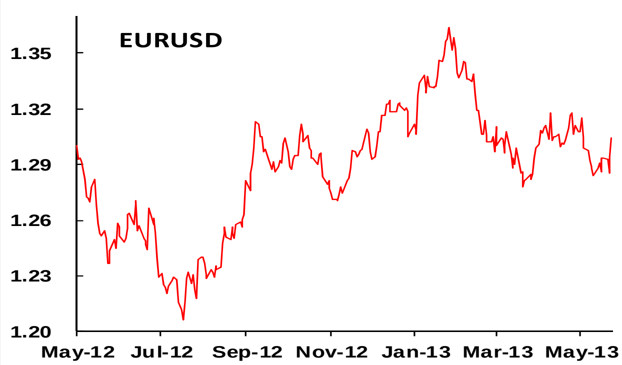
UNITED KINGDOM - A building short GBP position, having increased to -$7.3 billion (CFTC as of May 21), bearish technicals and a broadly stronger USD all contributed to GBP weakness in May. We remain GBP bears viewing the combination of low growth, elevated inflation, an upcoming change in leadership at the BoE and negative sentiment as GBP negatives. We hold a year-end target of 1.45.

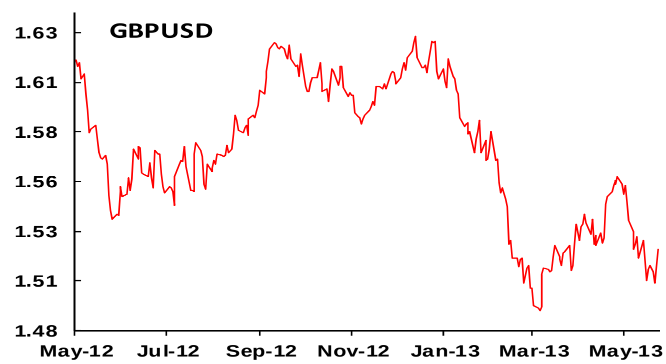
SWITZERLAND - In mid-May, SNB President Jordan suggested that the central bank could shift the level of the EURCHF floor or introduce negative interest rates; on the back of this EURCHF spiked above 1.26 for the first time in almost 2-years and saw increased appetite in CHF short positions (the CFTC reported these at -$2.5 billion as of May 21). We do not expect significant upside pressure from here and hold a year-end EURCHF target of 1.22.

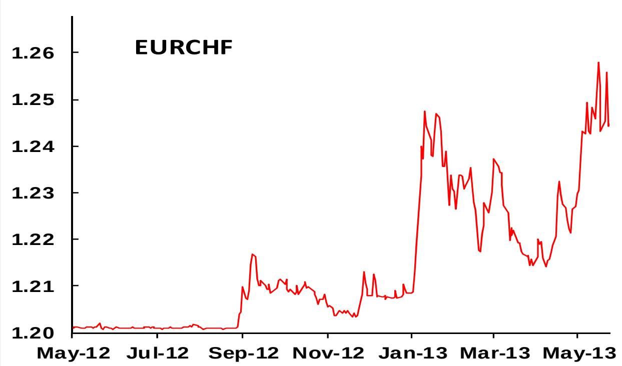
NORWAY - Entering June, the NOK is weak, having lost 5% year-to-date; however, we maintain a relatively strong outlook. The Norges bank is unlikely to cut rates again as it struggles with a financial stability risk of high household debt; on a relative basis, the economy is strong and unemployment is low, investor sentiment appears relatively neutral and the NOK is trading at the mid-point of its 5-year range. We hold a year-end USDNOK target of 5.50.

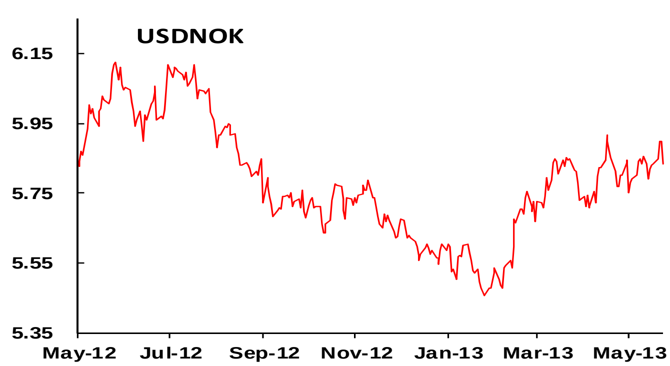
Currency Trends

FX Rate	Spot 30-May	13Q1a	13Q2f	13Q3f	13Q4f	14Q1f	14Q2f	14Q3f	14Q4f
EURUSD	1.30	1.28	1.27	1.26	1.25	1.25	1.24	1.24	1.23
GBPUSD	1.52	1.52	1.49	1.47	1.45	1.45	1.45	1.44	1.44
EURCHF	1.24	1.22	1.24	1.21	1.22	1.23	1.24	1.25	1.25
USDNOK	5.83	5.85	5.75	5.65	5.50	5.45	5.30	5.22	5.20









EUROPE

Fundamental Commentary

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EURO ZONE - First-quarter GDP figures released this month for the euro area highlighted the enduring economic weakness in the region. The results fell short of market expectations, particularly in the case of Germany, where both investment and exports declined sharply during January-March (just offset by an expansion in household spending and larger drop in imports). The ECB's expected 2013 H2 recovery still appears far off, and recessionary conditions could well persist into the second quarter. The fact that several key developed and emerging markets also appear sluggish – prompting a new wave of monetary policy stimulus – suggests that global growth momentum is gathering speed more slowly than earlier anticipated. We have lowered our euro area growth forecasts to -0.7% in 2013 and +0.7% in 2014 (from -0.5% and +0.9%, respectively). Recent weeks have seen increasing acknowledgements by policymakers regarding the absence of a forthcoming recovery and the inability of crisis-ridden states to return to growth amid severe fiscal austerity. Even the German Finance Minister has called for urgent action on youth joblessness, championing proposals for bilateral aid agreements with Germany's troubled euro zone partners. A slight uptick in the PMIs in May was a welcome development, but may prove to be an aberration, in which case the ECB may be compelled to implement another interest rate cut (following the quarter-point reduction to 0.50% in May). Inflation is expected to rebound somewhat after a steep decline in April, though price pressures will remain subdued through 2014.

UNITED KINGDOM - The pound sterling showed renewed weakness in May, with losses amounting to roughly 3% versus the US dollar reflecting weak economic data and the general bias toward USD strength over the month. Despite the rebound in output in the first quarter (the preliminary GDP estimate confirmed growth of 0.3% q/q in January-March, following the prior quarter's 0.3% contraction), there are few indications that the economy is entering a meaningful recovery. The gain was driven almost entirely by a large build-up in inventories, with a small addition from household spending. Meanwhile, private investment and exports continued to detract from growth. Disappointing retail sales data for April suggest that consumer spending is losing steam. The fact that the government's promised 'rebalancing' toward investment and trade has yet to materialize has prompted calls for a tempering of fiscal consolidation plans. According to the IMF's latest Article IV Consultation report on the UK (released May 22nd), of the GBP130 billion in deficit reduction measures slated for FY 2010/11 to FY 2015/16, more than half have already been implemented. The report also supported an expansion of the Bank of England's (BoE) asset purchase program and use of forward guidance by the central bank, and stressed the return of the two state-intervened banks to private ownership in order to strengthen confidence in the financial sector. Inflation dropped sharply in April, from 2.8% y/y to 2.4%. Much of the decline was due to temporary factors, however, and is unlikely to cause any great shift in opinions at the BoE.

SWITZERLAND - As did other major currencies (GBP, EUR), the Swiss franc (CHF) softened considerably in May, reaching its weakest point since May 2011 versus the euro. Losses were driven primarily by bullish speculation regarding US Fed policy, though the CHF was also driven down by comments from Swiss National Bank (SNB) President Jordan. He indicated that the central bank will maintain the minimum exchange rate policy (EURCHF 1.20) for as long as needed, and is – like the ECB's Governing Council – willing to consider a shift in the floor and/or negative interest rates if the inflation outlook does not improve. Consumer prices dropped by 0.6% y/y in April, the same pace as March, while M3 money supply growth accelerated again to 10.2% y/y. On account of the exceptionally accommodative monetary environment, the UBS Real Estate Bubble Index continued its rise in the first quarter, edging closer to 'bubble' territory. The IMF's latest report on the country noted that mortgage debt has surpassed 140% of GDP, and encouraged the government to adopt further measures to contain related financial sector risks. Switzerland registered a 1.1% y/y real GDP expansion in the January-March period (+0.6% q/q), down from 1.4% y/y in the prior quarter. The slowdown mirrors the global trend and, as illustrated by the steep fall in real exports in April (-7.6% m/m, compared with a -0.9% drop in imports), subdued demand from Asia in particular will likely continue to weigh on activity in the second quarter.

NORWAY - The trading pattern of the Norwegian krone (NOK) was largely unchanged over the last month, averaging around the 5.8 per US dollar mark. The first-quarter real GDP results painted a mixed picture; mainland growth rebounded from a seasonally adjusted 0.2% q/q in the fourth quarter to 0.7% in January-March (-0.6% y/y), however, a sharp drop in oil and gas production dragged the headline figure into negative territory (-0.2% q/q, -2.7% y/y). While exporters continue to be hampered by the relatively strong currency and prolonged weakness in the rest of Europe (in addition to lower oil prices in recent months), consumer activity remains supported by real wage growth and low unemployment. Moreover, new fiscal measures – including a small corporate tax cut for non-oil businesses – ahead of the parliamentary election this September should provide a modest boost to mainland growth over the medium term. We expect the economy to grow by around 2⅓% overall in 2013 (2½% mainland). Inflation remains below the central bank's 2.5% target, though it picked up to a 27-month high of 1.9% y/y in April (contrary to many advanced economy peers that have seen large downward inflation surprises recently). The Norges Bank is unlikely to follow the global trend of cutting rates at this time, as the authorities see inflation expectations as anchored in line with price stability over the medium term, providing scope for policy to address concerns related to rising financial imbalances, particularly in the housing market.

Asia / Pacific
Currency Outlook

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JAPAN - In May the Japanese yen (JPY) reached a 4.5 year low having been pressured by aggressive Bank of Japan policy juxtaposed against rising expectations that the Fed would begin stepping away from QE. Entering June, technical studies suggest the uptrend in USDJPY has more to run, while traders continue to build short positions (on May 21st the CFTC reported a net short JPY position of -$12 billion). We hold a Q213 USDJPY forecast of 102 and a year-end target of 105.

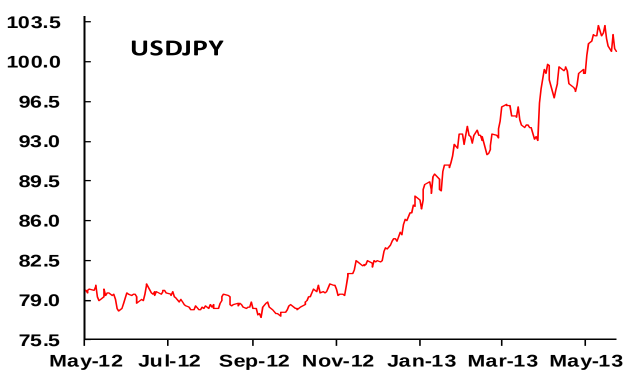
CHINA - As of the end of May, the Chinese yuan (CNY) is the best performing currency year-to-date, having gained 2% against the USD, outperforming all the majors and gaining 17% against JPY, 7% against KRW, 6% against SGD and 5% against TWD – likely putting significant pressure on trade patterns. We are surprisingly close to our year-end target of 6.10; however, we feel that the CNY is increasingly approaching fair value.

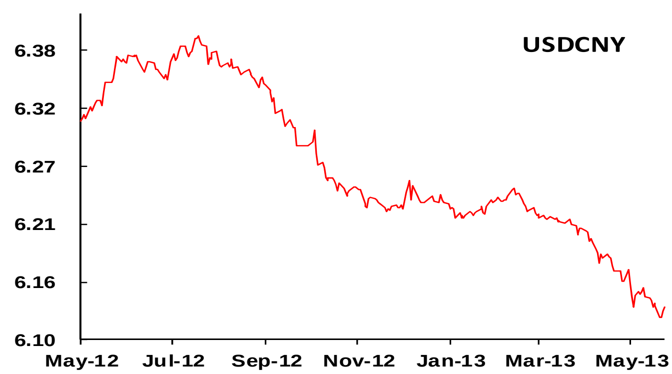
AUSTRALIA - The Australian dollar (AUD) collapsed in May, losing 8% from its April 30th high to its May 23rd low. A surprise RBA interest rate cut to 2.75%, fears over slowing Chinese growth and a strong USD pushed the AUD position from net long $9bn at the end of March to net short $3 billion on May 21st (CFTC). Technically, the downward trend remains in place but the currency is entering oversold. We expect that in the second half of the year the AUD trends back towards parity and hold a year-end target of 1.04.

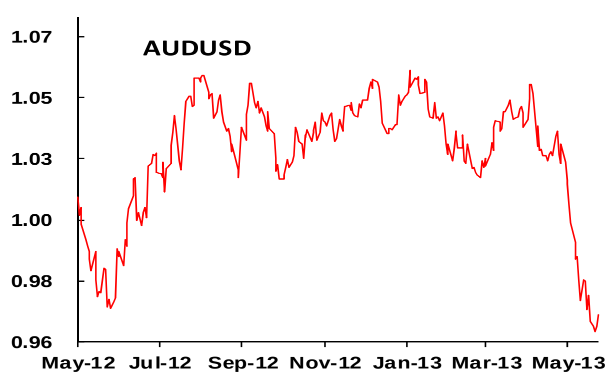
NEW ZEALAND - The New Zealand dollar (NZD) weakened in May as the central bank confirmed it had intervened in FX markets, the outlook for China's growth softened and there was a broad based rally. Traders clung to long positions, with the CFTC reporting that as of May 21st the NZD was one of only two currencies held net long against the USD. At the end of May, the NZD begun to stabilize, but most technical studies still warn of potential near-term downside risk. Into year-end we are more bullish, expecting NZDUSD to close the year at 0.85.

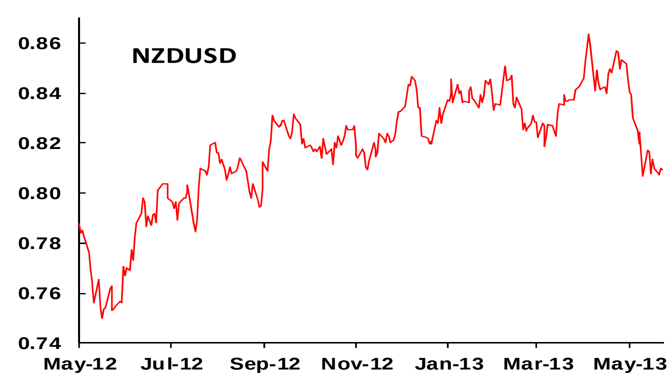
Currency Trends

FX Rate	Spot 30-May	13Q1a	13Q2f	13Q3f	13Q4f	14Q1f	14Q2f	14Q3f	14Q4f
USDJPY	100.9	94.2	102.0	104.0	105.0	106.0	107.0	109.0	110.0
USDCNY	6.13	6.21	6.13	6.12	6.10	6.09	6.07	6.06	6.04
AUDUSD	0.97	1.04	0.96	0.98	1.02	1.04	1.06	1.08	1.08
NZDUSD	0.81	0.84	0.82	0.83	0.85	0.85	0.86	0.86	0.86









Asia / Pacific

Fundamental Commentary

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JAPAN - Market participants' attention is centered on Japan's economic performance in order to assess the effectiveness of the country's recent unprecedented monetary policy actions. Signs are emerging that policymakers' revitalization efforts are starting to bear some fruit: earlier improvements in confidence are translating into a pickup in household spending, while leading indicators point to increasing economic momentum more broadly. In addition, the external sector should receive a boost from the recent substantial depreciation of the Japanese yen. Nevertheless, an extended equity market correction could translate into a deterioration in consumer and business confidence, potentially erasing some of the recent improvements. The country's real GDP increased by 0.9% q/q (non-annualized) in the first quarter of the year following a 0.3% gain in the final three months of 2012. The growth was reasonably broadly-based with the exception of weak investment activity. We have revised our 2013 output growth forecast for Japan, and now expect the economy to expand by 1.4% (1.0% previously), followed by a 1.5% gain in 2014. While the Japanese monetary authorities seem determined to end deflation, inflation remains in negative territory for the time being (consumer prices declined by 0.9% y/y in March). We assess that the period of deflation will come to an end around mid-year, with inflation creeping gradually higher towards 1.2% y/y by the end of 2014. In light of the substantial monetary policy measures announced in April, we do not foresee any material policy changes in the near term.

CHINA - The Chinese economy remains on track for a gradual and modest recovery, though momentum is gathering speed rather slowly. Accordingly, we have revised lower our real GDP growth forecasts for China to 7.9% in 2013 and 8.0% in 2014. The economy is in the midst of a structural change where the economic contribution of household spending—reflecting rising incomes and robust job creation—is increasing while that of investment and exports are diminishing. Despite the fact that purchasing managers' indices show weak growth momentum, various industrial output indicators, such as electricity, cement and steel, together with real estate indicators point to a moderate pickup in activity. The inflation outlook is manageable. The consumer price index recorded a 2.4% y/y gain in April, representing a slight acceleration from the month before. Price pressures will likely build up moderately over the forecast period, reaching 3⅓% y/y by the end of 2013 and around 4% by end-2014, though persistent deflationary pressures further up the distribution chain (producer prices declined by 2.6% y/y in April) should alleviate concerns regarding significant upside pressures on prices. Home price developments and credit growth dynamics—both performing strongly—will be key factors influencing the monetary policy stance in the coming quarters. The People's Bank of China (PBoC) has maintained the benchmark 1-year lending rate at 6.0% since July 2012. We expect the PBoC to begin to raise policy interest rates in the final months of 2013 in order to curb emerging inflationary pressures.

AUSTRALIA - Monetary conditions are easing in Australia; on May 7th, the Reserve Bank of Australia (RBA) lowered the benchmark cash rate by 25 basis points (bps) to 2.75%, taking cumulative reductions to 200 bps since November 2011. Accommodative financial conditions globally combined with below-trend economic growth domestically, a temperate inflation outlook, and a strong AUD triggered the RBA's monetary policy decision. The annual inflation rate, which climbed to 2.5% y/y in the first quarter of the year from 2.2% at the end of 2012, will likely close the year near the current level, thereby remaining consistent with the RBA's 2-3% inflation target. The peak in resource investment will likely occur this year; therefore, measures to support activity in other segments of the economy are warranted. Regardless, Australia will maintain relatively fast rates of economic expansion in comparison to many other advanced economies. Real GDP growth will likely decelerate to 2.6% this year from 3.6% in 2012, before re-accelerating to 3.0% in 2014 on the back of strengthening global demand. The resources sector continues to be the key economic motor in Australia. Household spending growth should gradually pick up as the housing and labour markets continue to improve, and the effect of monetary stimulus measures filter through the economy. Indeed, some signs of a revival are emerging with first quarter retail sales recording the strongest quarterly gain since 2007; meanwhile, however, demand for credit has yet to gather momentum.

NEW ZEALAND - An economic revival is taking place in New Zealand. While investment continues to be underpinned by rebuilding activity in Canterbury, household spending should be supported by improving consumer confidence that reflects developments in the labour and housing markets. The unemployment rate dropped to 6.2% in the first quarter of 2013 from 6.8% in the final three months of 2012, while employment increased by 1.7% q/q following three quarterly contractions. Meanwhile, house price gains accelerated in April (reaching 7.1% y/y compared with an average gain of 6.3% in the first quarter) as house sales increased by over 25% y/y. We expect the country's real GDP expansion to average 2¾% in 2013-14 following a 2½% gain in 2012. New Zealand's monetary authorities have expressed increasing concerns regarding developments in private sector credit and the housing market, prompting the Reserve Bank of New Zealand (RBNZ) to develop new macro-prudential tools (such as higher capital requirements for banks) to promote financial stability. Nevertheless, the benchmark cash rate – currently at 2.5% – remains the central bank's main policy tool. Improving economic conditions have yet to be reflected in inflationary pressures; at 0.9% y/y in the first quarter, consumer price inflation stayed below the lower end of the RBNZ's 1-3% target range. We expect that annual inflation will begin to creep higher in the near term, reaching the 2% mark by the end of 2013.

DEVELOPING ASIA

Currency Outlook

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INDIA - The India rupee (INR) has traded with a weakening bias as less dovish market expectations for Fed policy has boosted the USD and US rates, pressuring India's ability to fund its current account deficit. Though oil and gold prices have eased, the external deficit is unlikely to fall enough to nullify external funding risk for the rupee, particularly if the market's bias for pricing in a less dovish Fed to the USD continues. Capital account inflows following policy rate cuts have thus far failed to support the INR on a sustained basis. We target USDINR at 53.00 in Q4 2013.

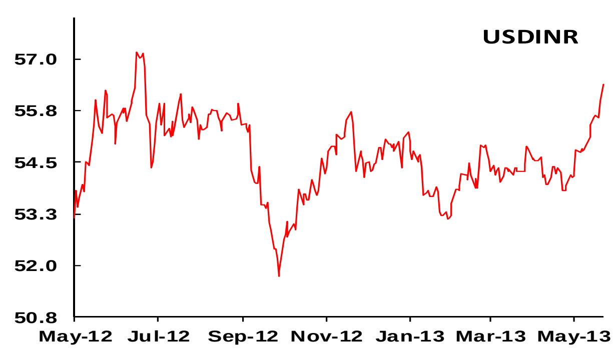
KOREA - The Korean won (KRW) has suffered from broad USD strength in May, despite a rally in the KOSPI. A weakened JPY remains a constraint for the central bank which cited the negative influence of the yen at the May rate cut, constraining KRW's ability to sustain a rally. Weaker imports keep Korean balance of payments, and thus the KRW, fundamentally supported, though with risk from the capital account channel obviously dominating in May. We remain optimistic on the KRW and target 1050 by the end of Q4 2013.

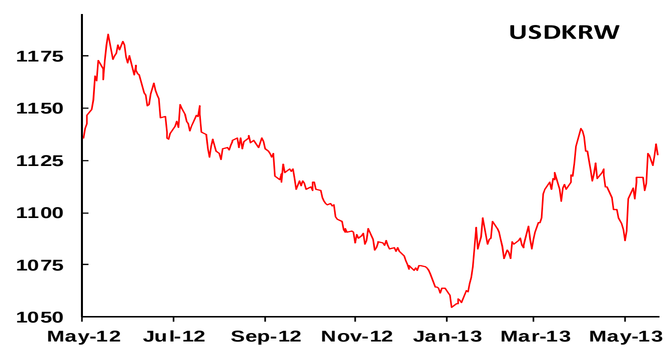
THAILAND - The Thai baht (THB) has weakened significantly since the end of April, experiencing its sharpest and most sustained down-move in over a year. The desire of fiscal authorities to offset foreign portfolio purchases and ease the pressure on exporters will likey lead to additional measures to hinder the pace of inflows. May's policy rate cut will help, as the Bank of Thailand moves in line with the easing bias seen in select other other Asian nations. Our Q4 2013 target of 30.25 for USDTHB is at risk for upwards revision at some point in coming months, dependent on new potential capital flow regulations.

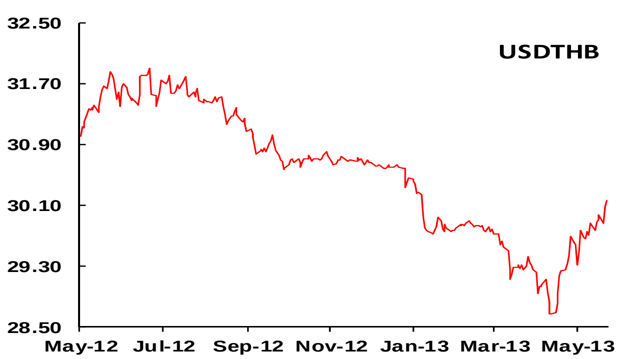
MALAYSIA - The very stong post-election rally in Malaysian bonds and equities saw a degree of profit-taking weigh on MYR during the later stages of May, particulatly in the fixed income space. Malaysia's less dovish policy stance and higher policy rate-implied yield should help keep the MYR a relatively attractive currency. Still reasonably robust domestic growth conditions also support the MYR in the regional context. We target 3.00 by the end of Q4 2013.

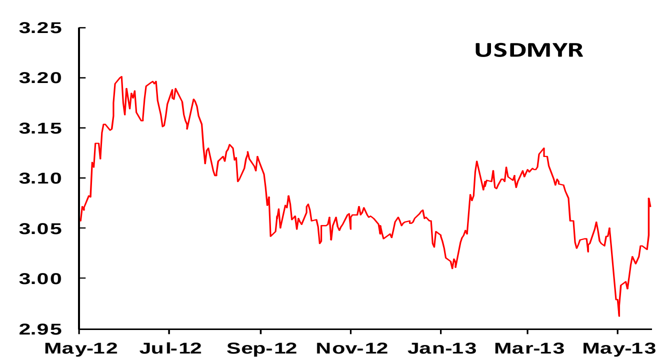
Currency Trends

FX Rate	Spot 30-May	13Q1a	13Q2f	13Q3f	13Q4f	14Q1f	14Q2f	14Q3f	14Q4f
USDINR	56.4	54.3	55.9	54.4	53.0	52.7	52.4	52.1	51.8
USDKRW	1127	1111	1115	1080	1050	1040	1035	1030	1025
USDTHB	30.2	29.3	30.2	30.2	30.3	30.1	30.0	29.9	29.8
USDMYR	3.07	3.09	3.06	3.03	3.00	2.99	2.98	2.96	2.95









DEVELOPING ASIA

Fundamental Commentary

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INDIA - The Reserve Bank of India continues to provide monetary stimulus, although at a cautious pace, in order to stimulate sluggish economic activity; on May 3rd, monetary policymakers lowered the benchmark repo rate by 25 basis points (bps) to 7.25%, taking cumulative reductions to 75 bps since the beginning of the easing cycle in January. The authorities identified two key factors behind the decision: a continuous and steep deceleration in economic growth, and an easing in WPI inflation closer to the central bank's tolerance threshold. While the policymakers pointed out that there is little space for further monetary easing, we assess that the fact that wholesale price inflation weakened substantially to 4.9% y/y in April from 6.0% the month before will allow further modest reductions in the benchmark interest rate. India's economic performance remains subdued, challenged by a high cost of financing, constrained fiscal room and subdued global demand conditions. A gradual improvement is in sight, however, supported by monetary easing and the government's attempt to implement modest economic reforms. We have revised India's real GDP growth forecasts downwards and now expect the economy to expand by 5½% in 2013, followed by a 6% gain in 2014. Shifts in investor sentiment will continue to be reflected in the value of the Indian rupee, as the country suffers from a large current account deficit (equivalent to around 5% of GDP in 2013), a negative sovereign credit rating outlook (affirmed by Standard & Poor's in May), weak government finances, and political instability.

KOREA - The differing views regarding the need for further monetary easing that had emerged among government officials and monetary authorities seem to have waned with South Korean policymakers joining their efforts to stimulate economic activity. The Bank of Korea (BoK) followed several other central banks in monetary easing, reducing the benchmark interest rate by 25 basis points (bps) to 2.5% on May 9th. The rate cut brings cumulative easing to 75 bps since July 2012, and complements the government's supplementary stimulus budget (equivalent to 17.3 trillion won, 1.3% of GDP) unveiled in April and approved by the National Assembly in May. We do not expect any further stimulus in the near term as the authorities will let the recent measures to filter through the economy. Manageable inflation was a key element allowing the BoK to loosen monetary conditions; at 1.2% y/y in April, consumer price inflation remains below the central bank's 2-4% target range. Inflation will likely accelerate gradually in the coming months, reaching 2.2% y/y by the end of 2013, and remaining under the 3% mark through 2014. The South Korean economy is improving, though the country's policymakers estimate that a negative output gap will persist for an extended period of time due to the slow global recovery, adverse impacts stemming from the substantial weakening of the Japanese yen, and geopolitical risks related to North Korea. We expect the economy to expand by 2½% this year, followed by a pickup to 3½% in 2014, on the back of a gradual pickup in private consumption and improving global demand conditions.

THAILAND - Thailand's economy continues to perform relatively robustly, remaining among top performers in the Asia/Pacific region. Nevertheless, the first quarter growth performance disappointed, with real GDP expanding by 5.3% y/y following a 19.1% y/y surge in the final quarter of 2012 that reflected the extensive flooding a year earlier. Economic performance remains broadly-based with household spending being the largest contributor, underpinned by rising incomes. Despite government officials' concerns regarding the impact of the strong Thai baht on the country's exporters, net exports recorded solid gains, increasing by 9.2% y/y in the January-March period. We expect Thailand's output to increase by around 4½% this year as a whole, followed by a 4.2% gain in 2014. Lower-than-expected growth combined with a manageable inflation outlook prompted the Bank of Thailand to lower the benchmark interest rate by 25 basis points to 2.50% on May 29th; the previous rate cut took place in October, 2012. We do not expect any further monetary easing in the coming months, though the central bank continues to be prepared to intervene in the foreign exchange market to limit excessive currency movements. The consumer price index increased by 2.4% y/y in April; we expect the headline inflation rate to close the year near the current level before picking up to slightly above 3% by the end of 2014. Core inflation, at 1.2% y/y in April, remains comfortably within the central bank's 0.5-3.0% target range.

MALAYSIA - Malaysia is experiencing a period of political instability following the May 5th general elections. While losing ground, the 13-party Barisan Nasional coalition remained in power, winning 133 parliamentary seats out of 222. Claiming of electoral irregularities, the opposition Pakatan Rakyat has organized a number of protests across the country. Nevertheless, authorities maintain that the ballot was free and fair. Economic growth in Malaysia slowed in the first quarter of 2013 as real GDP expanded by 4.1% y/y compared with a 6.5% gain in the final quarter of 2012. Output growth continues to be driven by domestic demand, particularly household spending and investment that counterbalance some of the adverse export sector impacts stemming from still-weak growth conditions in advanced economies. Private consumption is underpinned by income growth and favourable labour market conditions, while investment activity is supported by infrastructure projects and capital spending in the domestically oriented manufacturing and consumer-related services sectors. We expect Malaysia's real GDP to grow by 4½% this year and 5.0% in 2014. Inflationary pressures remain muted, with the CPI registering an increase of 1.7% y/y in April. Due to strong domestic demand, monetary policymakers will likely refrain from loosening monetary conditions despite the favourable inflation context. In fact, the monetary policy committee considers the current policy stance (the overnight policy rate is at 3.0%) to be accommodative and supportive of the economy.

DEVELOPING AMERICAS
Currency Outlook

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BRAZIL - There appears to have been another shift in Brazilian authorities' stance towards the currency over the past couple of weeks, with Finance Minister Mantega signaling that the government is not considering intervention to support the real, even after it lost 4% vs. the US dollar over the past month. The most interesting aspect of this is that it was a widely held view that the currency was used as a nominal anchor to avoid an inflationary pressure build-up, while the central bank used the SELIC rate to tighten as little as possible.

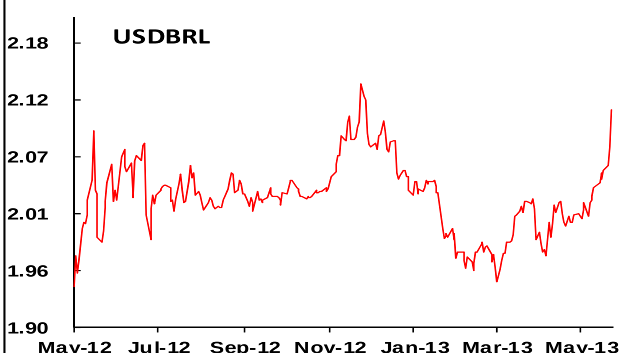
MEXICO - The peso has been ignoring its improving fundamentals over the past couple of weeks, getting fully involved in the "pain trade" as positioning and the broad USD trend have driven the peso to shed almost 4% of its gains relative to the greenback. Interestingly, despite a fairly sharp sell-off on both a cumulative FX move, and on local rates (TIIE 10yrs +70bps, 10yr M-bonos +80bps), the FX market adjustment has remained fairly orderly, to the extent that even if Banco de Mexico had the USD sales mechanism in place it would not have been triggered.

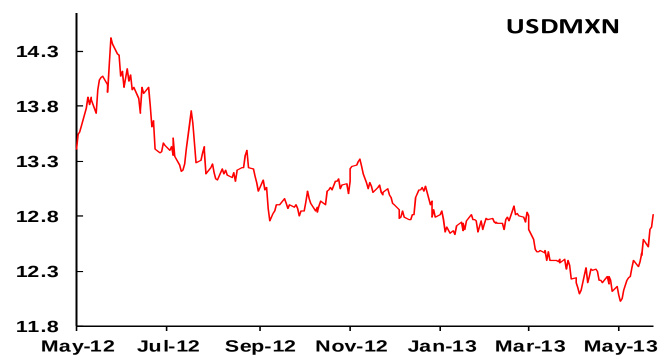
CHILE - The Chilean peso's (CLP) drop over the last leg of the sell-off has been more muted to that seen in more "heavily positioned" LATAM markets, which is consistent with a more modest foreign exposure to local markets. However, on a monthly basis, the CLP's drop has been very similar to those we have seen in other regional currencies such as the COP or MXN, as we believe that the CLP to some degree "front-ran" the sell-off due to its more direct link to China and copper price weakness.

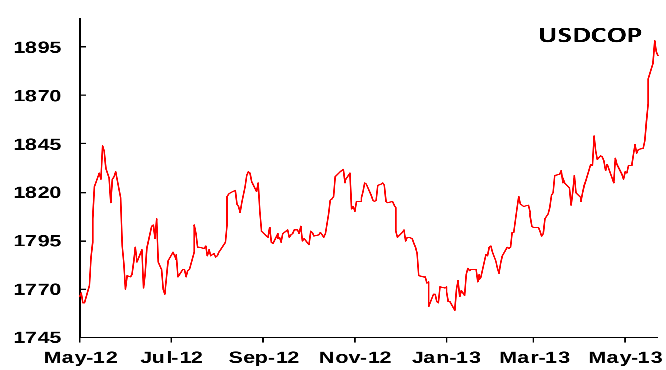
COLOMBIA - The Colombian peso (COP) accelerated its negative trend against the US dollar (USD) in May, reaching its weakest level in 12 months. In line with the rest of its Latin American peers, the COP was affected by the recent USD strength coupled with weak economic activity in Colombia and loose monetary conditions. The central bank will likely extend its USD purchase program on May 31st; however, authorities' observations regarding the USDCOP levels particularly after reaching the 1,900 mark will be relevant for further FX policies.

Currency Trends

FX Rate	Spot 30-May	13Q1a	13Q2f	13Q3f	13Q4f	14Q1f	14Q2f	14Q3f	14Q4f
USDBRL	2.11	2.02	2.01	2.01	2.00	2.01	2.02	2.04	2.05
USDMXN	12.77	12.33	12.08	12.09	12.25	12.33	12.19	12.24	12.38
USDCLP	493	472	478	489	492	493	496	499	500
USDCOP	1891	1825	1850	1880	1900	1910	1900	1900	1890







DEVELOPING AMERICAS
Fundamental Commentary

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BRAZIL - The Brazilian economy remains on a steady – albeit slow– path to recovery. First quarter real GDP growth accelerated from 1.4% y/y in the previous quarter to 1.9% y/y, slightly below our expectation of 2.0%. On a quarterly basis, the country's economy expanded at the same pace than in the previous quarter (0.6% q/q). Industrial activity remained weak, while the agricultural sector accounted for most of the expansion as the services sector decelerated somewhat. The government's stimulus measures implemented since last year coupled with a loose monetary policy have been filtering through the economy, although in a very slow pace. After peaking at 6.6% y/y in March, headline inflation returned to within the central bank's tolerance range, but remained close to the upper level at 6.5% y/y. After raising the reference rate by 25 basis points (bps) in April, the central bank accelerated the pace of monetary tightening, increasing the rate by 50 bps to 8.0% in May. In the statement released after the meeting, authorities referred only to inflation as the main cause for the decision, not mentioning anything about economic activity. We now expect the central bank to raise the reference rate by 50 bps in July and then by 25 bps in August taking it to 8.75%. Nonetheless, our forecast is still subject to the minutes of the recent meeting and inflation behaviour. The Brazilian real recently reached the 2.1 mark against the USD and, although the government has said that they do not have any plans to intervene in the FX market, we expect the currency to return within the 1.95-2.05 range in the coming months.

MEXICO - The Mexican economy has shown signs of moderation, with first-quarter real GDP growth decelerating from 3.2% y/y in the previous quarter to 0.8% y/y. Notwithstanding slower external demand, the change in the government has weighed on economic activity, which we expect to be a transitory effect. In addition, calendar effects (leap year and Easter) had a negative impact on the first quarter data. We anticipate that growth will resume its upward trend in the second quarter of the year; nonetheless, as a result of the weaker-than-anticipated Q1 numbers, we are revising our real GDP growth forecast from 3.4% in 2013 to 3.0%. However, we now expect a stronger pickup next year, with growth accelerating to 4.2% (previously 4.0%). Headline inflation remained above the central bank's target range (2-4%) for the second consecutive month in April. Although price pressures are coming from the volatile components of the consumer price index, we are revising our headline inflation forecast for end-2013 to 4.2% y/y. The central bank has indicated that higher prices are temporary and will not generate second-round effects on inflation. We anticipate that the monetary policy reference rate will remain unchanged at 4.0% for the remainder of the year. Despite the recent depreciation of the Mexican peso (MXN) - 3.1% against the US dollar so far in May - the currency leads the year-to-date charts against its Latin American peers, being close to 2.0% stronger since January. We maintain our view that the USDMXN will close the year at 12.3.

CHILE - The US dollar strength coupled with the less optimistic economic performance in Chile in the first quarter of the year have weighed on the Chilean peso (CLP), which ranks as the worst performer of the five major currencies vis-à-vis the US dollar in Latin America in the last month. Real GDP expanded by 4.1% y/y in the first quarter of the year, significantly below the 5.7% y/y gain registered in the previous quarter. The central bank explained that calendar effects caused by the timing of the Easter holiday (March this year) and the leap year caused a reduction of 0.6% percentage points of growth. Nonetheless, seasonally adjusted data also registered slower growth compared with previous quarters. We anticipate that this moderation will be temporary and activity will resume its upward trend in the second half of the year. We now expect the Chilean economy to expand by close to but slightly below the 5.0% mark in 2013 overall. Inflation continues to decelerate. Headline inflation in April (1.0% y/y) reached its lowest level since 2010, accumulating its fifth straight month below the lower limit of the central bank's tolerance range of 2-4%. As a result, we are revising our 2013 year-end inflation expectation from 2.9% y/y to 2.6% and accordingly, we now anticipate that the monetary policy reference rate will remain unchanged in the coming quarters. Nonetheless, we expect the central bank to move towards a more dovish rhetoric, at least until economic activity recovers and higher inflation gives them reason to maneuver.

COLOMBIA - In line with the rest of the currencies in the region, the Colombian peso (COP) has lost ground against the US dollar over the last month. However, the country's poor economic performance in recent quarters, the loose monetary policy stance undertaken by the central bank since last year, and authorities' efforts to weaken the currency in order to improve exports have caused the COP to underperform the rest of it regional peers, with a loss of 4.4% year-to-date. Economic activity, particularly in the industrial sector remains poor and we anticipate a very weak real GDP growth result for the first quarter of the year (to be released in June). The government already announced an economic program to fuel various sectors of the economy; nonetheless, stimulus measures will probably not start having an effect until the second half of the year or even later. After bottoming out in March at 1.9% y/y, headline inflation returned to within the central bank's tolerance range in April (2.0% y/y). Despite relatively low inflation and weak economic conditions, we do not expect the central bank to resume its monetary easing campaign, and the reference rate will likely be left unchanged at 3.25% for the remainder of the year. Additionally, we expect the authorities to extend the USD daily purchases program which expires by the end of May. Nonetheless, with the COP reaching the 1,900 mark against the USD, the authorities could soften their interventionist rhetoric, particularly if the currency stabilizes around or close to that level.

DEVELOPING EUROPE & AFRICA
Currency Outlook

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RUSSIA - The Russian ruble (RUB) has been depreciating since the beginning of the year. Further weakness lies ahead. The concerted move in favor of the USD has been the primary factor affecting the direction of the RUB in the past few months. On a positive note, the Russian Federation counts on the world's fourth largest foreign exchange reserves, valued at US$513 billion at the end of May (equivalent to 27% of GDP).

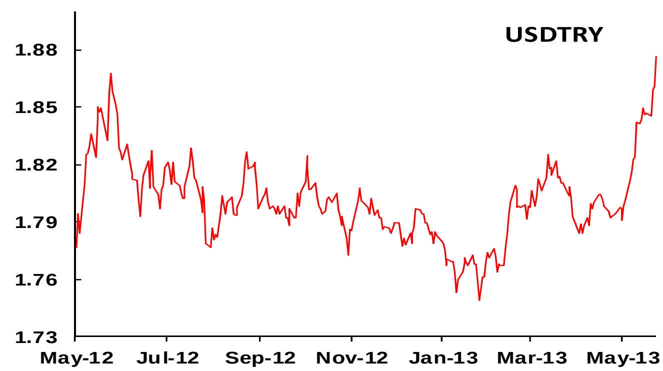
TURKEY - The Turkish lira (TRY) is one of the major casualties of the sell-off momentum affecting emerging-market assets. Non-Deliverable Forward (NDF) markets discount the continuation of a depreciating trend pushing the USDTRY rate near the 1.90 mark by the close of the year. The phasing out of unprecedented massive stimulus injected by the US Federal Reserve intervention in US Treasury bond markets is the primary driver of the TRY selloff.

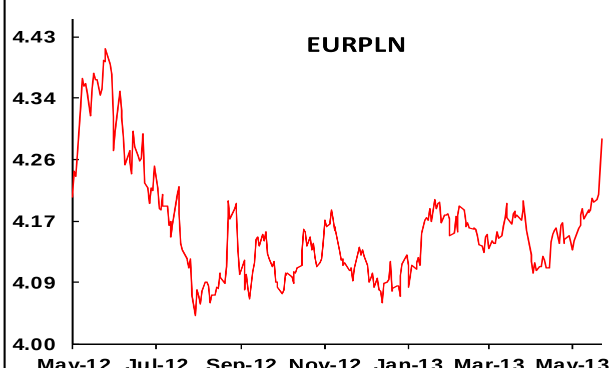
POLAND - The Polish zloty (PLN) has trended weaker since mid-April, and depreciating pressures will continue to weigh on the currency in the months ahead. Though we maintain the view that the PLN will appreciate relative to the euro over the medium term, we have modified our forecasted trajectory in light of further deterioration in the growth and inflation outlooks and the corresponding likelihood for further monetary easing. We have a year-end EURPLN target of 4.10.

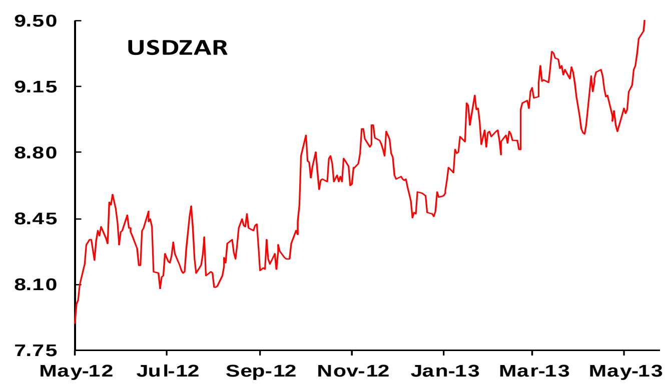
SOUTH AFRICA - The South African rand (ZAR) is under heavy pressure. US-driven capital outflows plus intensified socio-political unrest have been key factors instilling a negative market tone into the South African currency. The gap between forward and consensus forecast rates has widened sharply indicating a deeper bearish investor sentiment for the months to come on the grounds of substantial capital outflows and still wide, yet improving, fiscal and current account deficits.

Currency Trends

FX Rate	Spot 30-May	13Q1a	13Q2f	13Q3f	13Q4f	14Q1f	14Q2f	14Q3f	14Q4f
USDRUB	31.8	31.1	31.7	31.8	32.0	32.4	32.6	32.8	33.0
USDTRY	1.88	1.81	1.84	1.84	1.85	1.86	1.88	1.89	1.90
EURPLN	4.28	4.18	4.15	4.13	4.10	4.07	4.04	4.01	3.98
USDZAR	10.01	9.24	9.60	9.50	9.40	9.45	9.50	9.55	9.60







DEVELOPING EUROPE & AFRICA

Fundamental Commentary

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RUSSIA - Ongoing evidence of improved US economic conditions has triggered a sharp upward adjustment at the long end of the US yield curve enticing repatriation activity towards US$-denominated assets. In the context of decelerating growth in Russia (real GDP to expand by 3.0% in 2013 from 3.4% in 2012), inflation has emerged as an issue of investor concern. Consumer prices posted an increase of 7.2% y/y in April. Monetary easing will help revive growth through the remainder of the year; however, the central bank will remain sensitive to the rise of inflationary expectations. The benchmark repo rate, which has been set at 8.25% since September 2012, will likely decline by 50 basis points (bps) by year-end. The country's terms of trade have not been affected materially despite the bearish tone embedded into the Russian ruble (RUB). Actually, natural gas prices have increased by 42% – whereas crude oil prices have declined only marginally – since the beginning of the year. A speculative move against the RUB can be counteracted by swift official intervention, a common practice applied nowadays by core emerging-market economies. Meanwhile, the government is planning US$7 billion in Eurobond issuance by the end of the second quarter. The energy-rich Russian Federation is the second largest issuer of US$-denominated debt within the universe of emerging market borrowers contained in the EMBIG index. Russian sovereign bonds currently trade at a yield spread of 200 basis points versus equivalent UST debt securities.

TURKEY - The growth and inflation outlook is improving, yet the widening of the current account deficit remains an issue of utmost concern amongst market participants. The economy is positioned to strengthen this year and next averaging a 4.3% growth rate. The central bank stressed that domestic demand is experiencing a healthy recovery and that consumer confidence and industrial production metrics reinforce that view. Headline inflation is receding fuelling expectations that the central bank will inject monetary stimulus by lowering its policy-setting reference rate by at least 50 basis points by the end of the year while adjusting reserve requirements. Consumer price inflation reached 6.1% y/y in April, down from 11% y/y in April 2012. Notwithstanding an improving growth scenario, the Turkish lira (TRY) is extremely sensitive to the erosion in Turkey's external accounts given capital flows volatility. The current account deficit will remain in ascendancy averaging 7% of GDP in 2013-14. Although the country has comfortable access to international bond issuance and foreign direct investment to finance the external gap, high-deficit economies are subject to deeper stress during periods of elevated global financial market volatility. Weak sentiment towards emerging-market assets has also been a major factor weighing on the TRY as the Istanbul Stock Market index suffered from profit-taking forces given that Turkey was the best performing stock market within the core group of emerging-market economies (up 56%) over the past 12 months.

POLAND - Signs of persistent economic fragility, falling inflation and weaker global growth dynamics (which have prompted a new wave of monetary stimulus globally) have allowed the Polish monetary authorities to maintain an easing policy bias. The central bank has reduced the reference rate six times (by a cumulative 150 basis points) since November, pausing only once in April. The pace of real GDP growth slowed to 0.4% y/y in the first quarter from 0.7% in the prior quarter (downwardly revised from 1.1%), matching the low point of the 2009 downturn. Domestic demand remains particularly weak, contracting in yearly terms as households face rising unemployment and slowing wage growth. Lending to both households and businesses remains subdued, although housing credit has shown signs of improvement in recent months. Net trade remains the strongest contributor to growth, as exports benefit from increased cost competitiveness and imports fall with domestic spending. Expansion to non-EU export markets is a key factor driving down the current account deficit (estimated to reach 3% of GDP in 2013). We expect modest real GDP growth of around 1½% this year before the economy regains traction in 2014. The consumer price index recorded its smallest yearly gain since 2006 in April, advancing by just 0.8% y/y. With annual producer prices sliding since November and inflation expectations also at a multi-year low (12 month expected rate of 1.1% y/y in March-April), the headline rate is likely to remain below target well into 2014.

SOUTH AFRICA - The South African economic activity remains in slow and gradual recovery mode, influenced by very high unemployment and the government's drive to inject stimulus through public sector infrastructure spending. The central bank, sensitive to potential pass-through effects from a weaker currency and from above-inflation wage-adjustment settlements, will opt to maintain monetary conditions unchanged through the remainder of the year. The South African central bank has kept it policy-setting repo rate unchanged at 5% since July 2012, providing forward guidance rhetoric that it will remain sensitive to the inflationary impact of a weaker currency. Consumer price inflation recorded a rate of 5.9% y/y in April, near the upper band of the official 3-6% target range. The domestic political unrest and associated strike activity in the mining sector has intensified of late, exacerbating the sell-off tone in currency markets. The rate of unemployment, at 25%, is indicative of the deep social problems facing the current government. The South African rand (ZAR) weakened sharply from 8.90 to 10.10 per USD in May, one of the sharpest declines within the emerging-market world. A substantial contraction in metal prices has also reinforced the rand's depreciation; indeed, gold prices decreased from 1,615 to 1,323 US$ per troy ounce in just three weeks before bouncing back to 1,400. Ironically, despite the currency weakness, the country's main stock market index regained strength recently implying a better outlook for corporate earnings.

GLOBAL CURRENCY FORECAST (end of period)

			2011	2012	2013f	2014f	2013f Q1a	2013f Q2	2013f Q3	2013f Q4	2014f Q1	2014f Q2	2014f Q3	2014f Q4
MAJOR CURRENCIES														
	Japan	USDJPY	77	87	105	110	94	102	104	105	106	107	109	110
	Euro zone	EURUSD	1.30	1.32	1.25	1.23	1.28	1.27	1.26	1.25	1.25	1.24	1.24	1.23
		EURJPY	100	114	131	135	121	130	131	131	133	133	135	135
	UK	GBPUSD	1.55	1.63	1.45	1.44	1.52	1.49	1.47	1.45	1.45	1.45	1.44	1.44
		EURGBP	0.83	0.81	0.86	0.85	0.84	0.85	0.86	0.86	0.86	0.86	0.86	0.85
	Switzerland	USDCHF	0.94	0.92	0.98	1.02	0.95	0.98	0.96	0.98	0.98	1.00	1.01	1.02
		EURCHF	1.22	1.21	1.22	1.25	1.22	1.24	1.21	1.22	1.23	1.24	1.25	1.25
AMERICAS														
North	**Canada**	USDCAD	1.02	0.99	1.02	1.00	1.02	1.05	1.03	1.02	1.02	1.01	1.00	1.00
North		CADUSD	0.98	1.01	0.98	1.00	0.98	0.95	0.97	0.98	0.98	0.99	1.00	1.00
North	**Mexico**	USDMXN	13.94	12.85	12.25	12.38	12.33	12.08	12.09	12.25	12.33	12.19	12.24	12.38
North		CADMXN	13.65	12.96	12.01	12.38	12.10	11.51	11.73	12.01	12.09	12.07	12.24	12.38
South	**Argentina**	USDARS	4.30	4.92	5.80	7.00	5.12	5.21	5.51	5.80	6.10	6.40	6.70	7.00
South	**Brazil**	USDBRL	1.87	2.05	2.00	2.05	2.02	2.01	2.01	2.00	2.01	2.02	2.04	2.05
South	**Chile**	USDCLP	520	479	492	500	472	478	489	492	493	496	499	500
South	**Colombia**	USDCOP	1939	1767	1900	1890	1825	1850	1880	1900	1910	1900	1900	1890
South	**Peru**	USDPEN	2.70	2.55	2.55	2.50	2.59	2.60	2.58	2.55	2.52	2.50	2.50	2.50
South	**Venezuela**	USDVEF	4.29	4.29	6.30	7.90	6.29	6.30	6.30	6.30	7.90	7.90	7.90	7.90
ASIA / PACIFIC														
	Australia	AUDUSD	1.02	1.04	1.02	1.08	1.04	0.96	0.98	1.02	1.04	1.06	1.08	1.08
	China	USDCNY	6.30	6.23	6.10	6.04	6.21	6.13	6.12	6.10	6.09	6.07	6.06	6.04
	Hong Kong	USDHKD	7.77	7.75	7.75	7.75	7.76	7.75	7.75	7.75	7.75	7.75	7.75	7.75
	India	USDINR	53.1	55.0	53.0	51.8	54.3	55.9	54.4	53.0	52.7	52.4	52.1	51.8
	Indonesia	USDIDR	9069	9793	10100	9800	9735	9850	9975	10100	10025	9950	9875	9800
	Malaysia	USDMYR	3.17	3.06	3.00	2.95	3.09	3.06	3.03	3.00	2.99	2.98	2.96	2.95
	New Zealand	NZDUSD	0.78	0.83	0.85	0.86	0.84	0.82	0.83	0.85	0.85	0.86	0.86	0.86
	Philippines	USDPHP	43.8	41.0	40.8	40.5	40.8	42.1	41.4	40.8	40.7	40.6	40.6	40.5
	Singapore	USDSGD	1.30	1.22	1.21	1.19	1.24	1.25	1.23	1.21	1.21	1.20	1.20	1.19
	South Korea	USDKRW	1152	1064	1050	1025	1111	1115	1080	1050	1040	1035	1030	1025
	Thailand	USDTHB	31.6	30.6	30.3	29.8	29.3	30.2	30.2	30.3	30.1	30.0	29.9	29.8
	Taiwan	USDTWD	30.3	29.0	28.8	28.5	29.8	29.8	29.3	28.8	28.7	28.6	28.6	28.5
EUROPE / AFRICA														
	Czech Rep.	EURCZK	25.6	25.1	25.5	24.5	25.7	25.8	25.6	25.5	25.3	25.0	24.8	24.5
	Iceland	USDISK	123	128	122	120	124	121	122	122	122	121	121	120
	Hungary	EURHUF	315	291	300	290	304	294	297	300	298	295	293	290
	Norway	USDNOK	5.98	5.56	5.50	5.20	5.85	5.75	5.65	5.50	5.45	5.30	5.22	5.20
	Poland	EURPLN	4.47	4.08	4.10	3.98	4.18	4.15	4.13	4.10	4.07	4.04	4.01	3.98
	Russia	USDRUB	32.1	30.5	32.0	33.0	31.1	31.7	31.8	32.0	32.4	32.6	32.8	33.0
	South Africa	USDZAR	8.09	8.47	9.40	9.60	9.24	9.60	9.50	9.40	9.45	9.50	9.55	9.60
	Sweden	EURSEK	8.92	8.58	8.20	8.10	8.37	8.50	8.35	8.20	8.20	8.15	8.15	8.10
	Turkey	USDTRY	1.89	1.78	1.85	1.90	1.81	1.84	1.84	1.85	1.86	1.88	1.89	1.90

f: forecast a: actual

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