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Global Views

Weekly commentary on economic and financial market developments

March 9, 2012

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Derek Holt (416) 863-7707
derek.holt@scotiabank.com

Fed, China & ISDA-Aftermath Will Dominate Global Market Attention

- **Please see our full indicator, central bank, auction and event calendars on pp. A3-A9.**

US markets will be at the centre of global attention next week not just because of key domestic developments but also because of a fairly light global calendar. The FOMC decision on Tuesday is far and away the biggest event of the week particularly given that the Fed communicated through the WSJ this past week that it is debating whether or not to sterilize a potential round of additional bond purchases. This would amount to a different way of doing the twist if bonds are purchased in the belly and long ends of the curve while the net cash flow injection is neutralized by withdrawing funds from shorter-term markets. One might expect that after such a leak, this will be a subject of discussion at the FOMC meeting. We're not expecting any explanation in what is likely to be a maintenance statement, however, versus the greater likelihood that the minutes to the meeting will divulge an interesting debate when they are released on April 3rd. Data risk will be elevated throughout the week, starting with expectations for a decent retail sales report with the headline tracking vehicle sales, gasoline prices, and ICSC tallies higher. Key will be when the inflation-adjusted retail sales are released following next Friday's CPI since the price-adjusted volume of retail sales has been climbing at a slow pace in recent months while total inflation-adjusted consumer spending has been flat for three consecutive months. Next week also starts the next monthly cycle of factory data and each of the Empire and Philly Fed surveys will be watched for whether or not they can build upon recent momentum. Industrial production figures are expected to rise, but in our opinion face downside risk owing to the lagged effects of recent weakness in new factory orders and warmer-than-usual weather that could restrain utilities output. CPI inflation could well stabilize at a full point lower than the 3.9% peak last September. The GOP nomination process will return again next week with primaries on Saturday in Kansas and three US territories, but more important primaries in Mississippi and Alabama next Tuesday and then Missouri next Saturday. The last primary will be held in Utah on June 26th in a process that began with the Iowa caucus on January 3rd, and primaries in some key states like Texas and California are not until late May and early June. The US also auctions 10s and 30s in reopenings.

Asian markets will really only have three factors to consider that could influence the global market tone. One is when Chinese export growth figures land into this weekend. Be wary of the headline results that have consensus thinking the y/y growth rate could super-accelerate from -0.5% in January to +31% in February. Year-ago base effects are wreaking havoc with the numbers. For instance, in January 2011, Chinese exports grew by 38% y/y but then the very next month grew by only 2.4%. The bigger issue is that the trend in yearly export growth has been waning throughout much of the past year, but the volatility on monthly readings has been wicked. Regardless, global markets could be easily impressed by this apparent surge in export growth into Monday's market open. The second possible influence on global markets lands when Chinese Premier Wen gives an annual press briefing on Tuesday following the end of the National People's Congress. The scope for market-moving comments is significant on the heels of a policy bias toward lower growth. The third possible influence is the Bank of Japan's regular meeting on Tuesday. Regional market influences will arise through an RBI rate decision on Thursday, India's Federal budget on Friday, and some regional export figures.

Following Greece's successful bond swap, **European** markets will be focused upon the aftermath of an ISDA credit-event ruling. A Euro area finance ministers' meeting is likely to affirm support for the second Greek bail-out. The fundamentals calendar is relatively light and includes an update on eurozone CPI, Spain's budget balance, Germany's ZEW investor confidence survey, and a rate decision by the Norges Bank. UK markets have jobless claims, the unemployment rate and the trade balance to consider. Italy, Spain and France auction bonds.

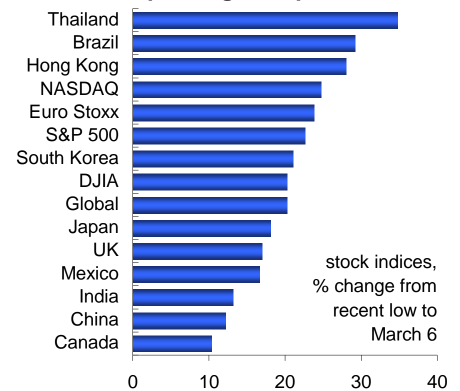
Canadian markets could well continue to decipher the meaning of the recent Bank of Canada statement after Canada 2s sold off and the currency appreciated sharply in the wake of a somewhat more hawkish take on the economy. The only update of relevance next week could be downside risk to manufacturing shipments on Friday in the wake of soft export figures. BoC Senior Deputy Governor Tiff Macklem speaks on "The Role Of Central Banks In A Market System That Supports Growth And Stability" from Brazil.

Latam markets will follow the global market tone with the exception of rate decisions by Mexico and Chile, neither of which are expected to change their key policy rates.

Aron Gampel (416) 866-6259
aron.gampel@scotiabank.com

Spring Thaw, Not Spring Break

Investors have turned optimistic again, reversing much of the pessimism that blanketed the world through much of last year. An aggregate measure of global stock market performance has rebounded a solid 21% since early October, re-establishing the rising trajectory in equity prices from the recession's bottom in the spring of 2009, and signalling a more constructive outlook for economic growth and corporate earnings.



Source: Bloomberg, Scotia Economics.

For the time being, the factors that roiled investors and the global economy have largely been put on the back burner. The list included the euro zone's chronic sovereign debt problems, slower economic growth in both developed and developing economies, recurring geopolitical problems, in addition to repeated natural disasters such as tsunamis, fires, floods, and droughts.

The rebound in equities from their recent lows has been global in scope. Thailand's stock index recorded a 35% jump, followed by a 30% gain in Brazil. A broad measure of European stocks has risen 24%, notwithstanding advancing recessionary conditions throughout the region. In the United States, the 'Apple'-driven Nasdaq has increased a solid 25%, while the benchmark S&P has rallied 23%. Both increases have coincided with evidence that the U.S. economy finally recouped the output lost during the recession. Canada's S&P/TSX has increased a relatively modest 10%, even though trade is rebounding and commodity prices are trending higher again.

The generally upbeat and synchronized stock market performances reflect a number of confidence-enhancing developments. On the European continent, the recession may not be as deep as feared, in part because Germany's core production strengths have enabled it to overcome the sharp reduction in regional trade. Moreover, the second Greek bailout builds upon prior financial and political commitments by the European Union, and reduces the immediate risk of default and a break-up of the single euro currency. The ECB is also now pursuing an increasingly accommodative policy, with successive interest rate cuts and two massive liquidity infusions totalling just over €1 trillion. The U.S. economy has proved to be more resilient as well. Ramped-up motor vehicle assemblies have helped revive industrial activity, while oil & gas production has increased sharply, buoyed by new fracking technology. Consumer spending has benefited from improving employment gains, and cash flows are being bolstered by sharply lower borrowing costs. Ultra-low rates have slashed interest charges on mortgages and consumer credit by about 25% over the past four years, the largest decline on record. This has enabled Americans to pay down debt, increase savings, as well as boost spending.

In addition, there appears to be greater confidence that the developing economies have engineered a soft rather than a hard landing, notwithstanding the comparatively weaker results being posted in a number of countries in the first quarter of this year. Construction and investment activity remains quite firm, helping to keep employment and spending in the relative fast lane of growth.

Despite these improvements, household deleveraging in the more highly indebted developed nations will continue, with most countries embarking upon a multi-year period of fiscal consolidation. In addition, the rise in the price of crude oil poses a growing threat to income-constrained consumers and businesses, and a risk to emerging nations battling domestic inflation. Crude oil prices have escalated to nearly US$110/bbl due to geopolitical tensions in the Middle East and potential supply disruptions surrounding Iran and Syria. A 'rules of thumb' suggests that a sustained 10% rise in the price of crude oil could trim global output growth by around 0.2 percentage points, and lift inflation by around 0.2 percentage points. This year's average to-date price of US$102/bbl represents just over a 7% increase from last year's average of US$95/bbl.

For a broader perspective on foreign exchange trends, please refer to our March 2012 *Foreign Exchange Outlook* at http://www.gbm.scotiabank.com/English/bns_econ/fxout.pdf.

Derek Holt (416) 863-7707
derek.holt@scotiabank.com

Dov Zigler (416) 862-3080
dov.zigler@scotiabank.com

With The Output Gap Closing, What Will The BoC Do?

***** Note: This is an updated version of a note that was first published as a preview in advance of the BoC statement on March 8th and that correctly argued that markets would take the statement as a hawkish signal that would put upward pressure on CAD and lead markets to sell the front end of the Canada curve. Markets would do so, we argued, because the BoC would signal that the economy was closing off spare capacity sooner than anticipated and thus inflation could be a marginally greater risk. *****

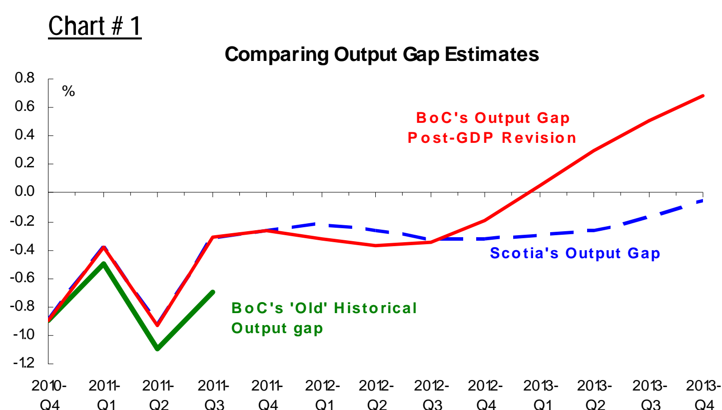
The Bank of Canada's latest interest rate statement flagged that the economy is operating with less slack than it had previously judged. This led the BoC to raise its inflation profile by stating that headline and core inflation would ride around the 2% target throughout the forecast horizon. The BoC also backed down on some of the geopolitical risks it sees by noting somewhat more encouraging developments in Europe. In turning more hawkish, the BoC also repeated the line that "there is considerable monetary policy stimulus in Canada" which has always been a none-too-subtle hint to the rate cut camp to re-think their positioning.

In this article, we explain why the output gap (the sum total of net excess demand or supply in an economy) has suddenly narrowed, where it might go in future, and why the BoC may steadily downplay the implications for some time yet. Overall, our forecast remains for the BoC to commence hiking in 2013Q3 but the two tail risks to this view have been altered by the changed output gap dynamics as we now set out to explain.

Why The Output Gap Has Changed

The BoC is now faced with a materially smaller output gap thanks to the sizeable upward revision to 2011Q3 GDP and sustained, albeit much slower, momentum into 2011Q4. 2011Q3 growth was revised higher from 3.5% to 4.2% and Q4 growth came in only two-tenths lower than the BoC anticipated in the January MPR. The net effect was that the level of output in the economy ended 2011 about a half percentage point higher than what the BoC had previously anticipated. Leaving the BoC's assumption for potential GDP growth unchanged for 2011 means that the output gap therefore narrowed materially. The BoC has yet to publish a Q4 output gap, but its estimate for Q3 was -0.7%, signalling a moderate amount of slack in the economy. We figure that because of the new information, the output gap as at Q3 was actually closer to -0.3% — or nearly a half percentage point lower and that much closer to balance in the Canadian economy. The output gap likely then ended 2011 at the same -0.3% since actual GDP growth of 1.8% in Q4 was very close to the BoC's assumption for potential GDP to have grown by 1.6% in 2011. Given the enormous uncertainty with respect to modelling output gaps and their components, to be speaking toward net slack of only -0.3% in the Canadian economy would be a material change in our judgement — implying the economy is nearer to full capacity, at which point inflation may be a risk.

Chart # 1



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

Where Will The Gap Go In Future?

Where we go with the output gap in 2012 and into 2013 then critically depends upon whether one relies upon the BoC's relatively optimistic growth assumptions for 2013, or Scotia's more conservative forecast which has served us well compared to the consensus bias throughout the crisis period.

Scotia and the BoC have similar growth forecasts for 2012, but they then part company in 2013. In 2013, the BoC expects quarterly growth rates of 3.1%, 3.1%, 3% and 2.8% as published in the January MPR, whereas Scotia expects growth of 2.2%, 2.2%, 2.5% and 2.6%. The impact this has upon output gap dynamics into 2013

Derek Holt (416) 863-7707
derek.holt@scotiabank.com

Dov Zigler (416) 862-3080
dov.zigler@scotiabank.com

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is shown graphically in chart 1 and the effects are significant. Using the BoC's forecast for actual GDP growth, the output gap closes into early next year in contrast to the BoC's January MPR assumption that this would not occur until 2013Q3 (which itself has been a moving target that has floated around the back half of 2013). Indeed, by the end of 2013, the BoC's output gap has shifted into excess demand at 0.7% of GDP which in turn is the largest net excess demand position since 2008Q3 — prior to when Lehman's collapse intensified the global crisis.

Using Scotia's forecast for actual GDP, however, results in the economy not closing off excess supply until the end of 2013 which is in line with the BoC's January MPR view. Thus, whether or not Canada has spare capacity into late 2013 or shuts it much sooner depends upon where one sits on the continuum of forecast opinions for growth in that year. The BoC's response could therefore well be to repeat a move it has made before during the crisis phase by again reducing its 2013 growth assumptions.

Does It Matter?

This naturally begs the question: does it matter? Yes and no. We had said in our Bank of Canada preview published before the statement that markets would react hawkishly by bidding up the value of the Canadian dollar and selling Canada 2s if the BoC came out, as they did, and pointed to "an economy operating around its potential over time" while "the profile for core and total CPI inflation is somewhat firmer than previously anticipated."

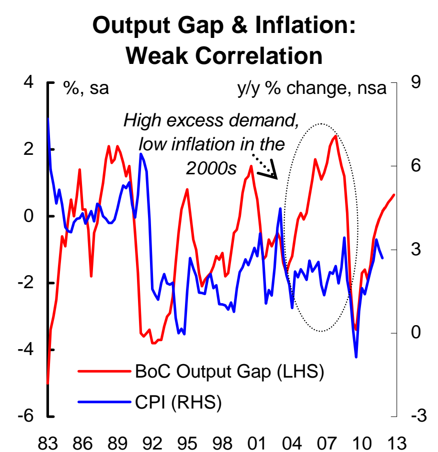
But would it matter in the longer-run debate over when the BoC will ultimately return to tightening monetary policy? Probably not, in our view, and for over a half dozen reasons.

First, Governor Carney has already made it abundantly clear that the BoC will likely lag behind the closure of the output gap in pushing toward a lower neutral rate for this cycle. Carney has noted that the BoC has utilized flexibility in achieving its operational inflation target through monetary cycles in the past. This gives him considerable leeway by which to judge the tenuous connection between output gaps and inflation.

Second, the BoC could well simply tweak its assumptions on a number of variables over 2012-13 and stick avoid stating that the economy will migrate into excess aggregate demand into 2013. The BoC could achieve this by either backing away from 2013 growth assumptions possibly for good reason as some indicators like jobs have lost momentum, or by raising potential GDP assumptions in light of solid business investment albeit the case that this has weakened again of late.

Third, the output gap is not exactly the best predictive tool in forecasting inflation in any event. Thus, even if the output gap closes earlier than anticipated, it does not mean that Carney would automatically interpret that as cause to hike in order to enforce the BoC's inflation target in some rigid formulaic sense. The connection between the output gap and inflation was at its strongest prior to the early 1990s and then became more erratic thereafter (chart 2). Witness, for example, the push toward large net aggregate excess demand in the years before the crisis while inflation remained subdued. That may be because of secular downward influences upon global inflation including but not limited to factors such as China's rise and the impact this had upon bringing cheaper consumer goods to world markets. To be charitable to the BoC, it may also be because domestic monetary policy shifted toward being more pre-emptive in an explicit inflation targeting framework from the early 1990s onward such that inflation expectations built into many contracts became more stable and less connected to output gaps. That may be true, but it bears pointing out that output gaps became weaker predictive

Chart #2



Source: Bank of Canada, Scotia Economics.

Derek Holt (416) 863-7707
derek.holt@scotiabank.com

Dov Zigler (416) 862-3080
dov.zigler@scotiabank.com

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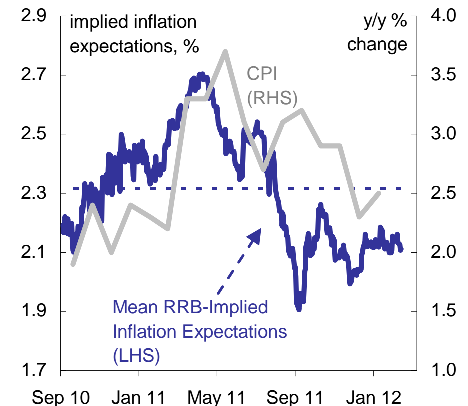
tools for inflation globally over the past two decades, and not just in Canada, as global forces exerted influences upon inflation rates the world over.

Fourth, while Governor Carney signaled a tad more encouragement toward European developments, geopolitical concerns remained as a theme in this past week's statement. The BoC continues to expect global growth to be soft and hence so will be demand for Canadian exports, and that oil prices pose a material downside risk to global growth and a further upside to the Canadian dollar.

Chart #3

Canada: RRB-Implied Average Inflation to 2041 & CPI



Source: Statistics Canada , Bloomberg, Scotia Economics.

Fifth, the domestic economy isn't exactly sparkling. Job market momentum has been lost on a trend basis, and the country's housing and consumer sectors sit at heavily leveraged structural peaks that could well challenge future growth.

Sixth, why tighten monetary policy on output gap reasoning when the Canadian economy is already facing material tightening in other respects? This includes a shift toward fiscal drag at the combined federal, provincial and municipal levels of government. It also includes the impact of a currency that is still operating near parity against the USD; while it is still weaker than the 94 cent peak last July, it has appreciated since last Fall's 1.055 trough against the USD. Further, consider that real wages are going nowhere in Canada as inflation is offsetting nominal wage gains. As gasoline prices surge again, this effect is being further reinforced to the effect of killing off disposable income growth. Finally, the country is soon likely to engage in another round of tightened housing finance policy in pro-cyclical fashion. This would be despite household credit growth having already slowed markedly and despite the fact that the country sits at heavily leveraged all-time peaks for most forms of activity in the household sector that will make future sustained growth in housing demand difficult to come by.

Seventh, as shown in the accompanying third chart, long-run inflation expectations are reasonably well behaved around the BoC's 2% target. Canada's breakevens are not as reliable in the near-term as they are in the US market, but thirty year implied expectations derived from the real return bond market suggest market confidence in the BoC's inflation targeting apparatus that should comfort the BoC.

As a final consideration for now, we also continue not to rule out QE3 being pursued by the US Federal Reserve as we've written about throughout this year, though whether further bond purchases will be sterilized or not is open to debate. If not sterilized, then the potential currency implications could make it difficult for the BoC to front run the Fed through materially early policy tightening. The QE3 story we told in our January 20th piece "Fed's Published Rate Forecasts Could Be A Warm-Up To QE3" has gathered some momentum in our view due to the disappointing readings on US consumer spending and business investment — an issue that we flagged above and that we had argued would occur in that paper.

Derek Holt (416) 863-7707
derek.holt@scotiabank.com

Dov Zigler (416) 862-3080
dov.zigler@scotiabank.com

BoC: Side-By-Side Comparison

Release Date: March 7, 2012

The Bank of Canada today announced that it is maintaining its target for the overnight rate at 1 per cent. The Bank Rate is correspondingly 1 1/4 per cent and the deposit rate is 3/4 per cent.

The heightened uncertainty around the global economic outlook has decreased in the weeks since the Bank released its January Monetary Policy Report (MPR). With tentative signs of stabilisation in European bank funding and sovereign debt markets, conditions in global financial markets have improved and risk aversion has decreased. However, **the global economy is still expected to grow below its trend rate** as the deleveraging process in advanced economies proceeds. The U.S. expansion is proceeding at a modest pace, reinforced by recent improvements in the labour market. Growth in China is moderating to a still-high rate as expected, in response to past policy tightening and weaker external demand. Commodity prices are higher than anticipated, supported by improved global economic conditions and **a** geo-political **risk premium on oil**. **If sustained**, the latter **could ultimately dampen the improvement in global economic momentum**.

Recent developments suggest that the outlook for the Canadian economy is marginally improved from the January MPR. Although **the economy will likely grow faster than forecast in the first quarter due to temporary factors**, underlying economic momentum remains around trend, balancing domestic strength and external weakness. **Private demand is now expected to be slightly stronger than projected**, owing to improved sentiment and highly-supportive financial conditions. Canadian household spending is expected to remain high relative to GDP as households add to their debt burden, which remains the biggest domestic risk. Net exports have been supported by stronger-than-anticipated U.S. activity but are expected to contribute little to growth, reflecting still-moderate foreign demand and ongoing competitiveness challenges, including the persistent strength of the Canadian dollar.

The profile for core and total CPI inflation is somewhat firmer than previously anticipated as a result of reduced economic slack and higher oil prices. After moderating in the second quarter, total inflation is expected, along with core inflation, to be around 2 per cent over the forecast horizon, reflecting the combination of modest growth of labour compensation, an economy operating around its potential over time, and well-anchored inflation expectations.

Reflecting all of these factors, the Bank has decided to maintain the target for the overnight rate at 1 per cent. With the target interest rate near historic lows and the financial system functioning well, there is considerable monetary policy stimulus in Canada. The Bank will continue to monitor carefully economic and financial developments in the Canadian and global economies, together with the evolution of risks, and set monetary policy consistent with achieving the 2 per cent inflation target over the medium term.

Release Date: January 17, 2012

The Bank of Canada today announced that it is maintaining its target for the overnight rate at 1 per cent. The Bank Rate is correspondingly 1 1/4 per cent and the deposit rate is 3/4 per cent.

The outlook for the global economy has deteriorated and uncertainty has increased since the Bank released its October *Monetary Policy Report* (MPR). The sovereign debt crisis in Europe has intensified, conditions in international financial markets have tightened and risk aversion has risen. The recession in Europe is now expected to be deeper and longer than the Bank had anticipated in October. The Bank continues to assume that European authorities will implement sufficient measures to contain the crisis, although this assumption is clearly subject to downside risks. **In the United States, while the rebound in real GDP during the second half of 2011 was stronger than anticipated, the Bank expects the U.S. recovery will proceed at a more modest pace going forward**, owing to ongoing household deleveraging, fiscal consolidation and the spillovers from Europe. Chinese growth is decelerating as expected towards a more sustainable pace. Commodity prices — with the exception of oil — are expected to be below the levels anticipated in the October MPR through 2013.

The Bank's overall outlook for the Canadian economy is little changed from the October MPR. While the economy had more momentum than anticipated in the second half of 2011, the pace of growth going forward is expected to be more modest than previously envisaged, largely due to the external environment. Prolonged uncertainty about the global economic and financial environment is likely to dampen the rate of growth of business investment, albeit to a still-solid pace. Net exports are expected to contribute little to growth, reflecting moderate foreign demand and ongoing competitiveness challenges, including the persistent strength of the Canadian dollar. In contrast, very favourable financing conditions are expected to buttress consumer spending and housing activity. Household expenditures are expected to remain high relative to GDP and the ratio of household debt to income is projected to rise further.

The Bank estimates that the economy grew by 2.4 per cent in 2011 and projects that it will grow by 2.0 per cent in 2012 and 2.8 per cent in 2013. **While the economy appears to be operating with less slack than previously assumed, given the more modest growth profile, the economy is only anticipated to return to full capacity by the third quarter of 2013, one quarter earlier than was expected in October**.

The dynamics for inflation are similar to those anticipated in the October MPR, although **the profile for inflation is marginally firmer**. Both total and core inflation are expected to moderate in 2012 and subsequently rise, reaching 2 per cent by the third quarter of 2013 as excess supply is slowly absorbed, labour compensation grows modestly and inflation expectations remain well-anchored.

Several significant upside and downside risks are present in the inflation outlook for Canada. Overall, the Bank judges that these risks are roughly balanced over the projection horizon.

Reflecting all of these factors, the Bank has decided to maintain the target for the overnight rate at 1 per cent. With the target interest rate near historic lows and the financial system functioning well, **there is considerable monetary policy stimulus in Canada**. The Bank will continue to monitor carefully economic and financial developments in the Canadian and global economies, together with the evolution of risks, and set monetary policy consistent with achieving the 2 per cent inflation target over the medium term.

Oscar Sánchez (416) 862-3174
oscar.sanchez@scotiabank.com

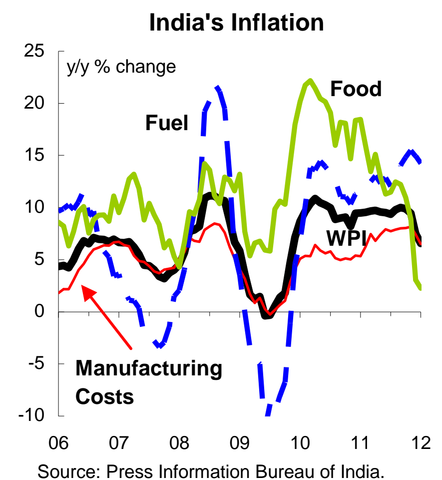
India's Central Bank Cuts Reserve Ratio; Further Reductions Anticipated

- **India's disinflation has exceeded central bank's expectations as favourable weather conditions have aided on the food price front, while fuel costs remain elevated.**

The Reserve Bank of India (RBI) will continue to move towards monetary policy easing as the country finally experiences diminished price pressures on most fronts. Despite the lack of considerable progress in bringing down fuel costs, there is evidence that local gasoline prices have continued to moderate. Therefore, our view of the country's disinflationary process contrasts with consensus in that we expect the yearly gain in wholesale prices (to be published in the coming week) to have continued to come down in February to 6.2% y/y, from 6.55% in January.

The RBI cut the cash reserve rate (CRR) overnight by 75 basis points (bps) to 4.75%. The CRR determines the share of deposits that banks must hold with the central bank, with the new requirement taking effect as of March 10. The reduction in the CRR was not only larger than expected, but also occurred a week before the mid-quarter policy review. Last night's move follows the first cut in the CRR decreed in January, which amounted to 50 bps from the 6% peak.

India has finally joined the set of countries in the Asian region where inflation is on a downward trend. Annual wholesale price gains came down to 6.55% y/y in January, well below the 7.9% average of the past three months. Ebbing food cost gains are now being accompanied by a lower yearly advance in local fuel prices, although the latter still lead as the main source of inflationary pressures (please refer to adjacent chart).



Source: Press Information Bureau of India.

The RBI's estimated rate of disinflation has been met prematurely, with moderating inflationary expectations and some evidence of a fall in core pressures (which are estimated by the RBI by the advance in manufacturing costs, please refer to chart) likely to prompt the RBI to soon complement its switch to a looser monetary stance with interest rate reductions. The benchmark repo cut-off yield stands currently at 8.5% as a result of a two-year monetary tightening campaign that entailed eleven upward revisions. Our recently revised estimate of 5% y/y inflation at end-2012 implies further gains in the disinflationary battle. The extent of the fall in inflation will hinge crucially on the government's commitment to continue to withdraw public gasoline subsidies, and on the future behaviour of global oil prices. Retail gasoline costs in India have been coming down from a US$6 dollar per gallon peak back in August; and stand currently at $5.60. Changes in fuel costs are likely to continue to follow global oil fluctuations more closely as subsidies continue to be curtailed. India stands out in the non-Japan Asian region as a country that continues to register large fiscal deficits despite elevated rates of GDP growth (the country registered a fiscal shortfall of 8.5% of GDP in 2011).

India's economy grew 6.1% y/y in the fourth quarter, the weakest advance in over two years, with monetary tightening, falling export growth and declining government outlays having been a drag on output. Upward cost pressures amid weak household spending have dented the outlook for business investment. With external demand now weakened, the country's economic prospects hinge on a rebound in local demand, with lower cost pressures amid improved household purchasing power setting the tone for upbeat business investment prospects. A switch towards loose monetary policy will further enhance the business outlook. We expect economic activity to regain momentum with the turn of the fiscal year (April/March), as cost containment sows the seeds for a rebound in domestic spending and private investment improves on the back of wider profit margins. An improved outlook for the agricultural sector, as normal rainfall supplants below average monsoons, will also support rural discretionary spending. We expect GDP to gain 7.5 % y/y on average during 2012-13.

Gorica Djeric (416) 866-4214
gorica.djeric@scotiabank.com

Rising Oil Prices & The U.S. Recovery

- **Oil price volatility plays a key role in the economy, but U.S. businesses and consumers are better positioned to absorb oil price shocks than in 2007-2008.**

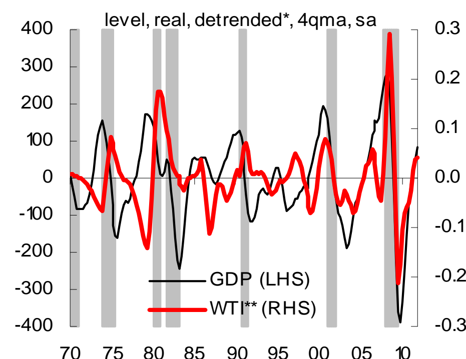
The recent surge in oil prices — prompted by geopolitical risks (Syria and Iran) — has reignited the age-old debate of the impact of energy price shocks on the U.S. economy, the world's biggest importer of crude, but also its third-largest producer, after Saudi Arabia and Russia. While ten of the last eleven U.S. downturns were preceded by sharp spikes in oil prices (chart 1), in the current environment both businesses and consumers have a greater cushion than in the run-up to the most recent recession.

Historically, oil price shocks were largely caused by supply-side factors (e.g, Iranian Revolution, Gulf War). In contrast, the surge that heralded the most recent downturn was produced by strengthening global demand, led by China. Since the mid-1980s, the sensitivity of the economy to oil price changes — including GDP, price indices, and the unemployment rate — the length of the time lags, and the strength of the inverse relationship have all been reduced (charts 1, 2). These adjustments have come as a result of improved monetary policy, more flexible labour markets, and declining energy intensity in production and household consumption (chart 3).

Meanwhile, the price volatility of oil has increased and studies have shown that this expanded volatility has considerably more influence on economic activity than on changes in price levels. The introduction of a market-based oil pricing regime in 1986 may be part of the explanation. In recent times, however, the-above mentioned economic efficiencies and a tighter global supply/demand balance, due to rising demand in developing economies, have played a key role. Consequently, oil consumption has become less elastic, boosting its price volatility and rendering historical comparisons harder.

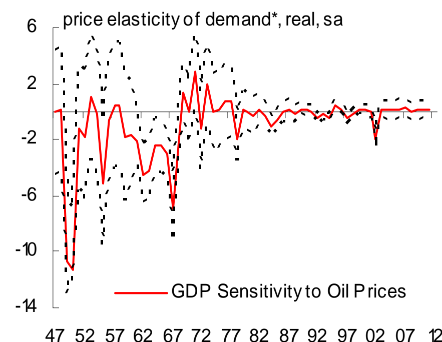
The outlook for oil prices is highly uncertain, hinging on both demand- and supply-side factors. We expect West Texas Intermediate (WTI) to climb an average of US$15 in 2012 to a record annual high US$110/bbl. While this will act as a headwind — on lower-income households in particular — we think that the U.S. economy is better insulated than in 2007-2008. Consumer and, especially, corporate balance sheets are in better shape, and hiring activity is showing signs of picking up. Muted inflation and the Fed's commitment to low interest rates into 2014 are providing further relief. For producers, higher oil prices could help accelerate oil exploration. While high oil prices will increase the U.S. trade deficit, a competitive trade-weighted U.S. dollar and strong agricultural prices — the United States is a major agricultural exporter — will boost exports, providing an offset to the rising cost of oil imports. What's more, domestic oil inventories are better stocked than in 2008, and the International Energy Agency (IEA) may be prepared to release strategic reserves if necessary. Applying OECD and IEA estimates, a 10% increase in oil prices reduces GDP growth by 0.2 and 0.4 percentage points in the first and second year, respectively. However given the current improving macroeconomic environment, we believe the impact will be lower than these estimates.

Oil Price Shocks Tend To Precede Downturns



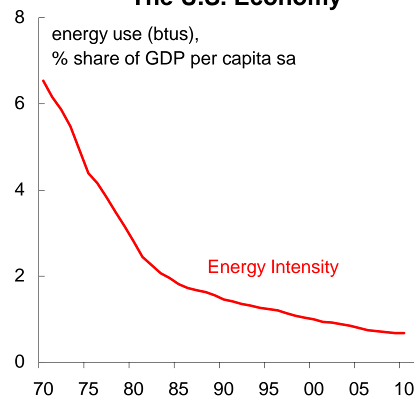
* Detrended using HP filter.
**WTI spot oil price deflated with GDP deflator.
Source: BEA, Nymex, Scotia Economics.

U.S. Economy Less Sensitive To Oil Prices



* Change in GDP to change in oil price.
** Dotted lines are rolling 10-year standard deviations.
Source: BEA, Nymex, Scotia Economics.

Increased Energy Efficiency of The U.S. Economy

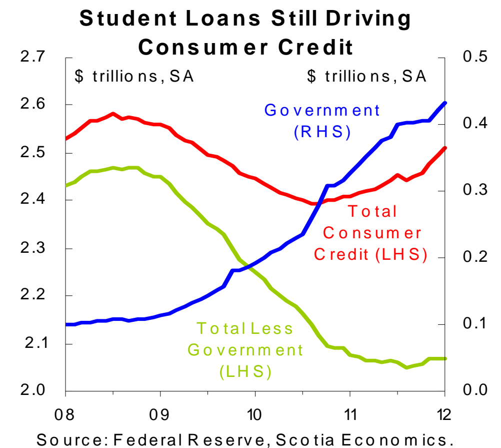


Source: BEA, IEA, Scotia Economics.

Derek Holt (416) 863-7707
derek.holt@scotiabank.com

Dov Zigler (416) 862-3080
dov.zigler@scotiabank.com

Are U.S. Consumers Really Back To Borrowing?



Whether or not US consumer lending is recovering is one of the issues of pertinence to Fed policy going forward. Headlines are enthusiastically pointing to the significant monthly gains in consumer credit that have been occurring for some time. This is taken as a sign of confidence in the economy and as a sign that monetary policy is working. Digging beneath the headlines, however, reveals that what is driving this lending 'recovery' is actually signalling a lack of confidence in the US economy that is more in keeping with weak consumer spending figures.

To get to this observation, we deconstructed the lending categories by class of institutional lender. The accompanying chart does this by plotting the seasonally adjusted institutional break down. The bottom line is that almost all of the growth in consumer credit by category of institution has occurred at government lenders (the blue line). Strip this out, and next to none of it has sustainably occurred at private lenders (the green line). In turn, all of the government category is comprised of student loans that are guaranteed or directly funded by the federal government. Indeed, the Federal Government's loans to students have nearly quadrupled since 2008 to $425 billion today.

About all that one can say that is mildly encouraging is that the total credit less government category of lending has at least stopped bleeding. Balances stabilized over 2011. That said, deleveraging is continuing since there is no growth in private credit whereas there has been mild growth in incomes and population that would ordinarily beget some rise in outstanding credit balances. While some categories like improved auto financing conditions may be healing, this is being offset by weakness in other categories to lead to a flat picture for total consumer borrowing excluding government.

Thus, we're left with a picture whereby the consumer credit 'recovery' isn't really a recovery at all. It reflects a rising tide of people who are exiting the labour force to go back to school which is a sign of a lack of confidence in the job market and the broader economy that is also aided by government policy. This may work for the better in the long run if human capital is built through marketable education, but it signals something very different about the economy from just glancing at the headline credit figures. In other words, the story has not changed one iota from when we began disaggregating the credit components in the earliest stages of this credit "recovery".

Adrienne Warren (416) 866-4315
adrienne.warren@scotiabank.com

Global Housing Markets Remain Under Stress

- **More global property markets have come under increasing stress, consistent with the slowdown in economic growth internationally.**

There is hope that recent signs of improving global economic activity and reduced financial market volatility will help to stabilize global property markets in 2012. The current ultra-low interest rate environment appears set to continue into 2013. For the time being, however, sovereign debt concerns, high unemployment, weak consumer confidence, excess supply and cautious lending continue to restrain activity.

Housing conditions deteriorated across much of Western Europe in the final quarter of 2011, most notably in the struggling peripheral nations. **Ireland's** slump remains the deepest in our survey. Average inflation-adjusted home prices were down 17% y/y in Q4, bringing the cumulative decline from their early-2007 highs to more than 45%.

Price declines also accelerated in **Spain**, showing a drop of 10% y/y over the final months of 2011. After four years of near-uninterrupted retrenchment, average home values have fallen roughly 25% from their peak. In the **U.K.**, house prices continued to fall at a steady pace of 6% y/y. In **Sweden**, one of the region's better performing markets in recent years, average prices were down 5% y/y in Q4.

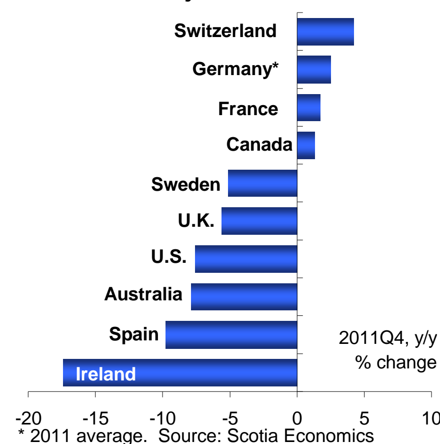
The **French** property market continues to hold up relatively well, reflecting in part tight housing supply. Nonetheless, the pace of price appreciation slowed through the second half of the year, to just under a 2% y/y advance in Q4. Within Europe, **Switzerland** was the only market in our survey to show an acceleration in Q4, albeit slight, with average prices up 4% y/y.

Meanwhile, **Germany's** long housing slump may be coming to an end, with solid domestic growth and low unemployment lifting demand. After a steady decline beginning in the mid-1990s, real home prices edged up for a second consecutive year in 2011 (official data are published only annually). While encouraging, a shrinking population suggests limited potential for significant price appreciation going forward.

Australia's housing boom has come to an abrupt end, as deteriorating affordability and a softening job market sideline potential buyers. Prices have softened steadily over the past year, leaving them down 8% y/y in the final months of 2011. Still, this represents a relatively minor price correction after years of strong appreciation, and overall domestic economic conditions remain reasonably solid.

The **U.S.** housing recovery continues to disappoint. Despite a modest pickup in demand since mid-2011, supported by record housing affordability and an improving job market, distressed property sales continue to depress prices. Average inflation-adjusted existing home prices were down almost 8% y/y in Q4 to new cycle lows. Ongoing price declines have erased a decade of appreciation, and in real terms leave average valuations at mid-1990s levels.

Even in **Canada**, housing has lost its exuberance. Home prices have levelled out over the past six months as market conditions become better balanced and as high prices, tighter mortgage regulations and slowing job growth cool demand. Average inflation-adjusted prices were up just 1% y/y in Q4. We expect sales and prices will be relatively flat in the year ahead, with stronger job and income gains and more positive demographic trends favouring Western Canadian housing markets over those in Central and Eastern Canada.



Nathan Joshua (416) 866-5338
nathan.joshua@scotiabank.com

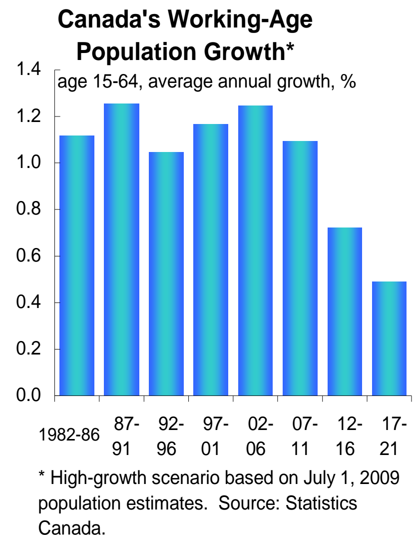
Mary Webb (416) 866-4202
mary.webb@scotiabank.com

Canadian Governments — Adjusting Expenditure Outlooks

- **Program spending restraint, including labour negotiations, mirror future demographic pressures as well as deficit reduction targets.**

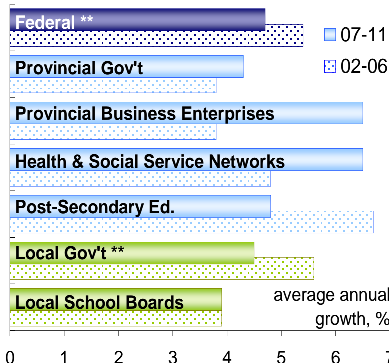
A number of Canadian governments, including Ottawa, are rolling out broad-based program spending changes this spring. In many instances, these measures are intended to shift programs to a more sustainable basis, designed to limit the spending catch-up after consolidations that has frequently occurred in the past. Beyond government spending pressures in health and other areas emanating from an expanding Seniors' cohort, government revenue gains will be dampened by the moderating increases anticipated for Canada's working age population, that will be only partially offset by significant immigration *(top chart).* Thus, Canada's public-sector wage and salary gains over the decade to 2011 *(bottom left chart),* that reflected full- and part-time public-sector employment increases averaging 1.8% annually *(bottom middle chart),* are unlikely to be maintained over the next decade. This constraint is certainly playing into the centre-stage government labour negotiations across Canada this year.

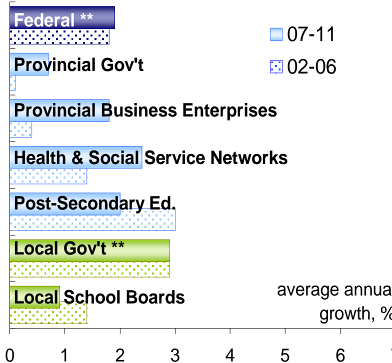
For British Columbia, a critical factor in its strategy to regain black ink by FY14 is securing contracts with a zero net compensation increase that make higher wages conditional on offsetting productivity increases. In Toronto's labour negotiations this year, a key objective for the City is obtaining greater flexibility in managing its workforce as it proceeds with program reforms. Ontario has indicated that its progress in trimming class sizes and shifting to a full-day kindergarten program will be eroded if its teachers refuse a salary and pay-scale freeze to 2014. On the East Coast, Halifax is weathering a transit strike. In addition to wage restraint, governments also are attempting to curtail benefits such as the option to bank sick days that can then be cashed out at retirement.

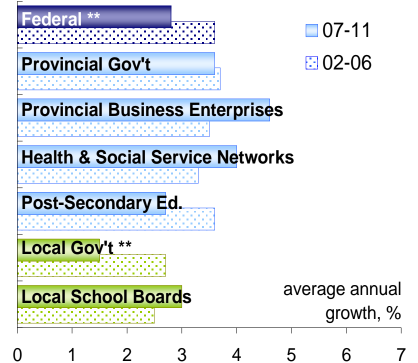


* High-growth scenario based on July 1, 2009 population estimates. Source: Statistics Canada.

For Western Canada, the challenge of managing its wage and benefit expense is increased by the tight labour markets re-emerging after the recession (*bottom right chart*). In Alberta and Saskatchewan, the annual rise in wages and salaries per employee from 2002 to 2011 averaged 4.3% and 3.6%, respectively, compared with a 2.9% increase across the other Provinces.







* Full- and part-time employees (not full-time equivalent) including the military and employees outside of Canada. ** Includes business enterprises. Source: Statistics Canada.

Araceli Espinosa (5255) 9179-5237
araceli.espinosa@scotiabank.com

Joe Kogan (212) 225-6541
joe.kogan@scotiabank.com

Leonor López (5255) 5229-2202
leonor.lopez@scotiabank.com

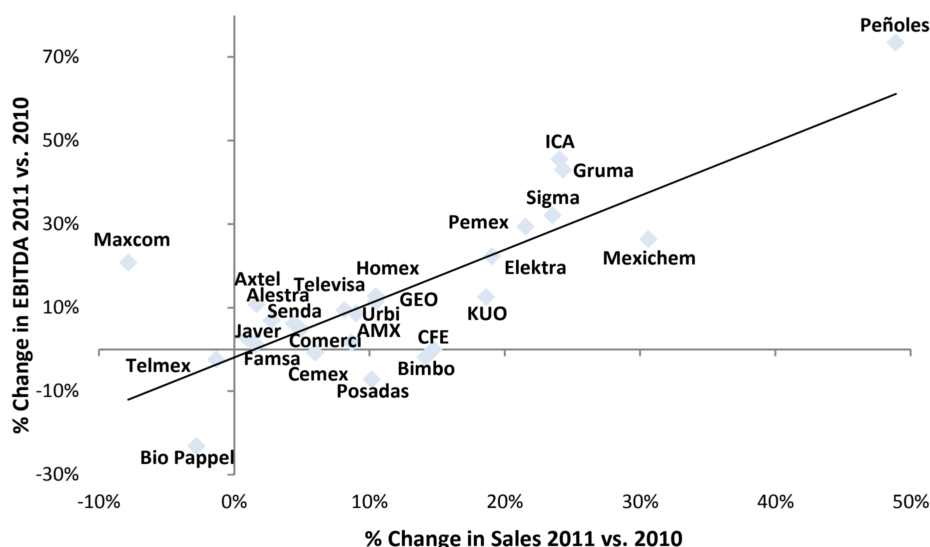
Mexican Corporates 4Q11 Wrapup

While the majority of Mexican corporate spreads have already recovered to levels we saw last summer, spreads on some of the lower rated names remain elevated, not always for good reason in our opinion. We review the evolution of fundamentals and the trends in different sectors.

Overall performance of corporates in 2011

In contrast to the tremendous sell-off in Mexican corporate bonds in the second half of 2011 which averaged 350bp, most corporate fundamentals remained strong. Mexican companies reported improved performance relative to the previous year, with the majority posting growth in sales and in Ebitda due to a variety of factors including currency movements.

Figure 1. Change in Revenues and EBITDA 2011 vs. 2010



Source: Company reports; Scotiabank

Higher oil prices and metals prices helped some firms, while for others, increases in energy and input prices put pressure on margins. In some cases, they were able to take advantage of the situation and pass on those higher costs to consumers.

2011 was a year that offered opportunities for growth through acquisitions, both in Mexico and in other regions of the world, though for some that meant greater indebtedness. The acquisitions were favorable for many corporates; for example, Mexichem, achieved vertical integration, while others were able to diversify income sources. Even with the acquisitions, various companies also achieved outstanding organic growth. Net leverage increased in many cases, as did the share of dollar-denominated debt, but the depreciation of the peso played a significant role in explaining many of these movements. (Appendix 1 shows that 14 out of 25 companies increased their leverage.)

Partial recovery in spreads

Thanks to the market's perception of diminished risks in Europe, the majority of Mexican corporates have recovered to the spreads we saw last summer (firms close to the x-axis in the graph on the next page have fully recovered).

However, many firms with lower credit ratings continue to trade at spreads that are still 100 bp or more above where they were last summer. Some of these companies were significantly affected by the volatility in the exchange rate, increasing the risk of covenant breach. Others had seen a credit-rating downgrade or rating

Araceli Espinosa (5255) 9179-5237
araceli.espinosa@scotiabank.com

Joe Kogan (212) 225-6541
joe.kogan@scotiabank.com

Leonor López (5255) 5229-2202
leonor.lopez@scotiabank.com

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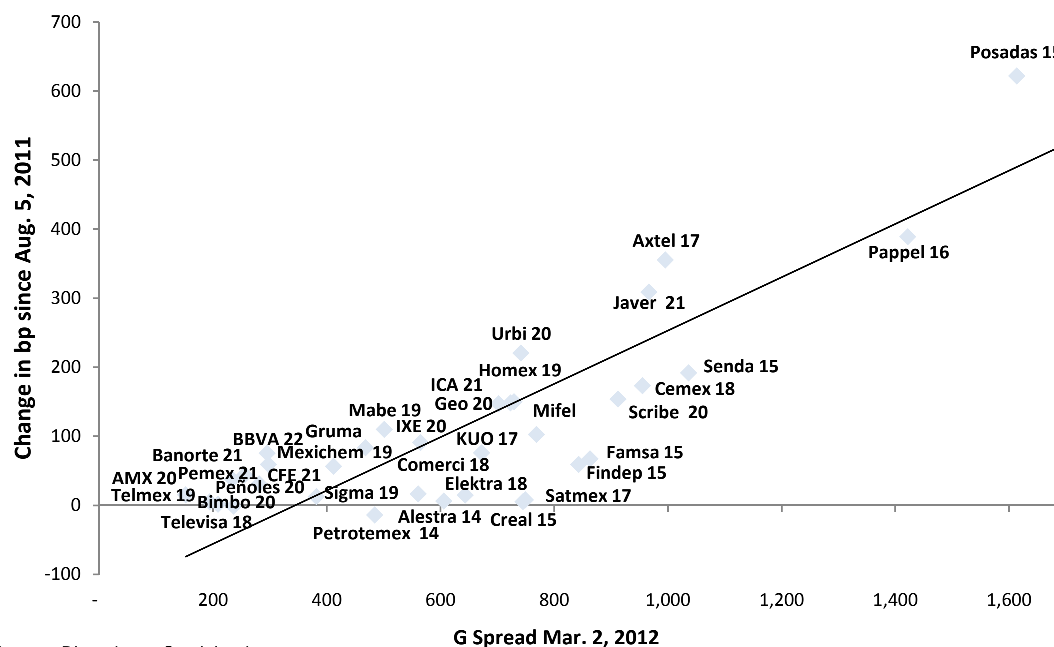
outlook change. Increased competition was particularly harmful to those firms who already had a risky financial profile. In the case of the homebuilders, the lack of cash-flow generation and repeated failures to meet cash flow targets has kept spreads under pressure. (See "Mexican Homebuilder bonds after 4Q11", March 2, 2012). On the other hand, ICA, with favorable earnings results for the year, is still almost 150 bp over its summer level; that is surprising, since while upcoming presidential elections may affect the timing of certain projects, we think the outlook for demand looks good regardless of the election results.

Figure 2. Change in Spreads March 2012 vs. August 2011



Source: Bloomberg; Scotiabank

Results by sector

Among the quasi-sovereigns, Pemex posted good results with regards to the outlook for long-term production, which represents the greatest concern for investors. Pemex still seems attractive to us considering the significant spread differential to the sovereign.

The telecommunications sector is undergoing important regulatory changes. The government is finally trying to reduce the advantage of dominant companies, but those companies continue to do well. The approval of the joint venture between Iusacell and Televisa or an authorization for Telmex to transmit video could provoke significant competition among the largest players. The small companies in the sector seek to survive by offering integrated IT services. The problem is that they must make substantial investments to compete, thereby weakening cash flow. Their position in the industry is less comfortable every day.

The food-product manufacturers experienced volatility in their raw materials prices and negative impacts from currency depreciation. Companies in this sector responded, however, by improving operating efficiency in order to offset this pressure on margins. Gruma and Sigma were even able to achieve greater growth in Ebitda than in sales. In the case of Bimbo though, the company was also affected by the integration of recently-acquired operations with smaller margins, resulting in a contraction in yearly Ebitda.

We continue to believe that the paper sector in Mexico is not in a healthy position to face the pressures on its margins, or to confront the competition from other global paper companies which have better financial profiles and lower costs.

Araceli Espinosa (5255) 9179-5237 araceli.espinosa@scotiabank.com
Joe Kogan (212) 225-6541 joe.kogan@scotiabank.com
Leonor López (5255) 5229-2202 leonor.lopez@scotiabank.com

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In the retail sector, Elektra is performing extremely well compared to competitors and is aggressively widening its base of stores, especially with regards to its store banking operations. Due to limited discolosur, however, it is difficult to evaluate separately the performance of the company's banking and retail businesses. The chemical companies and the conglomerates, which have also experienced volatility in raw materials prices, were able to partially defend themselves by hiking sales prices, and they posted organic growth in sales volumes as well. Furthermore, Mexichem and Kuo took advantage of the situation to acquire companies.

The two micro-financing firms, Crédito Real and Financiera Independencia, capitalized on some competitors' difficulties in gaining access to financing by making acquisitions and achieving substantial loan-portfolio growth. Creal's acquisitions, although more recent, have proven to be more efficient; the company purchased two of its main distributors, thus reducing risks to its capacity for portfolio origination. In addition, Creal not only continues to maintain healthy asset quality (demonstrating that the business of discounting loan payments from the payrolls of unionized government workers has low risk), but it has actually improved delinquency rates even while achieving an outstanding rate of organic growth. The results for Findep, with stagnation in the growth of its organic portfolio and its need to take significant amounts in loan-loss provisions due to the rise in the number of delinquencies, have meant that Creal's spread for several months has hovered below that of Findep.

Please see standalone document for detailed comments on earnings by firm for 18 Mexican corporates.

Alan Clarke (44 207) 826-5986
alan.clarke@scotiabank.com

UK: English Secret Agents

BoE — No Surprises in March

The Bank of England left Bank Rate and the scale of asset purchases unchanged at the March meeting — in line with expectations. Unless the economy had deviated substantially compared with the Bank's assumed path (which it hasn't), it was unlikely that the MPC will be swayed from the current plans. While the March announcement was a formality, the minutes of the meeting is where the focus will be this month. Given the improvement in key survey indicators in the UK and Eurozone, coupled with recent comments from MPC members and a further moderation in fiscal jitters in the periphery of the eurozone, we believe that this latest instalment of QE will be the last. The minutes (released 21 March) will help to give clues on how likely this is.

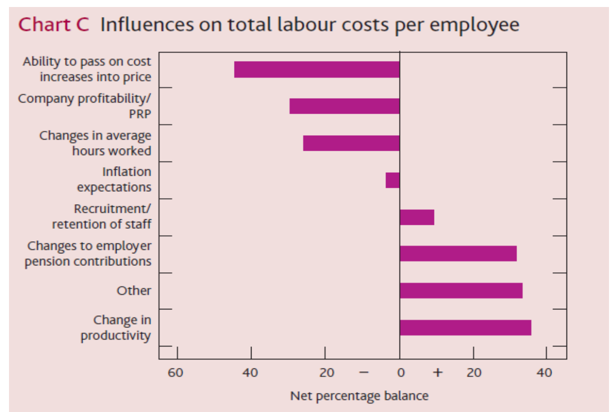
We were as surprised as anyone that the MPC minutes in February showed a split, with the dissenters in favour of even more QE than the majority call for GBP50bn. However, the latest BoE Regional Agents' Report — released in tandem with the minutes tells you all you need to know about why that happened.

Shhh! It's a Secret!

The Bank has around 8000 contacts from the business community nationwide. Each month the Bank conducts a survey of around 700 of these contacts, asking questions about various aspects of their business. The responses are summarised into scores, which gauge aspects of the economy relevant to monetary policy decisions including some influences that ONS data or other indicators do not cover. The analysis by the regional agents has formed an integral part of the Bank's MPC meeting process since 1997 — though the scores were only made public from 2006.

I started the year with a glass half-full — with a growth forecast on the optimistic side of the consensus. A quick read of the latest Agents' report is one of the only things that has made me question that judgment. To summarise: World demand growth had slowed; there was weakening in services sector activity; the degree of spare capacity had widened; credit conditions tightened; and various signs of slowing inflation.

Furthermore, the report typically includes the results of a special or one-off investigation. At this time of the year when pay settlements are being announced, the Bank tends to focus on early clues for wage inflation. Chart C below shows the results of the latest probe. The results were also dove-friendly. In particular, the thing the MPC fears most — a wage — price spiral — registered as the lowest percentage balance.



Meanwhile, the reasons given for higher labour costs were not particularly threatening to the MPC's inflation target.

The text of the report was even more sobering / dove-friendly. Snippets included: little sign of any underlying improvement in consumer confidence; discounts were still considered essential to drive sales; recruitment freezes were becoming more commonplace; while output for the export market was firming, there was particular weakness reported by suppliers of goods to the domestic market and those industries also reported a higher degree of spare capacity; and discounting was essential to induce customers to spend.

In short — it was all very dove friendly and likely to have been a significant contributor to the dissenters' decision to vote for a GBP75bn expansion of QE.

Foresight is better than hindsight

Sadly, although the MPC has the results of the Regional Agents' report at the time of each monetary policy meeting, the rest of us have to wait until two weeks later when the minutes are published. In the interests of transparency, wouldn't it be sporting of the BoE to share this report at the same time so that we can better judge the likely outcome of each meeting?

Alan Clarke (44 207) 826-5986
alan.clarke@scotiabank.com

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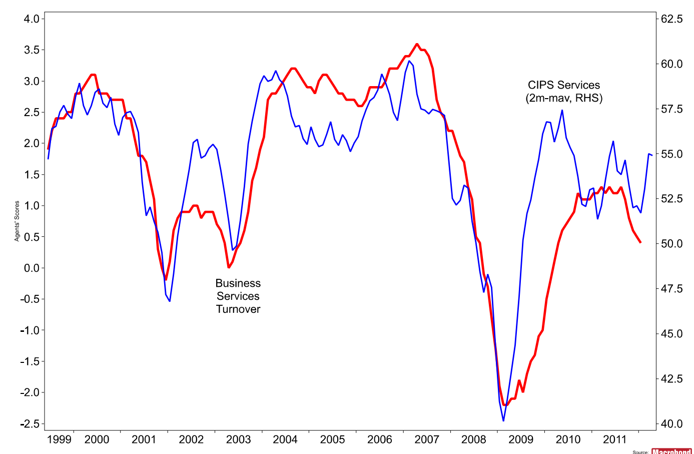
Fortunately for the rest of us, several of the components of the agents' report are lagging. Hence we can have a reasonable idea of where the scores are heading and in turn an early warning of the likely evolution in the committee's stance. In this regard, we believe that there are at least four aspects of the survey that are likely to firm compared with the February assessment:

1. Turnover in business services and 2. manufacturing

The CIPS services survey tends to lead this component of the regional agents' survey by around 4 months with a correlation coefficient of around 80% (Chart 2).

Clearly the CIPS survey is more variable than the BoE agents' equivalent. However, the trend is your friend. The CIPS correctly highlighted the loss of altitude late last year, but has since rebounded. The same has been true of the manufacturing equivalents.

Chart 2: CIPS Services vs Turnover in Business Services



2. Capacity Constraints / Investment Intentions

One aspect of the CBI industrial trends report shows the number of firms working below capacity. Similarly, the European commission industrial sentiment survey provides a gauge of current production capacity. Both suggest that, at worst, the fall in the agents' score for investment intentions or capacity constraints should not be extrapolated. At best, it points to a rebound in the agents' scores.

3. Employment Intentions / recruitment difficulties

The employment intentions component has a reasonable relationship with the equivalent from the CBI industrial trends report and the European Commission survey. There is also a loose relationship between the former and the Manpower Employment Outlook Survey (MEOS). All three have shown a firming in hiring intentions — at least partly reversing the slide into end-2011.

Glimmer of Hope?

The text of the latest agents' report offered one glimmer of hope. With regards to investment intentions, the report noted that *'a few firms reported having restarted postponed investment, even though they remained uncertain about the outlook'*. This chimes with our view that sentiment dived in late-2011 when it seemed likely that the Eurozone would implode, causing shockwaves throughout the global financial system. This provoked investment and hiring plans to be shelved. Now that it is becoming clearer that the world is not coming to an end, we suspect that firms are restarting postponed projects. Unless this was a short-lived phenomenon, we suspect that there will be further upside in the coming reports to hiring and investment intentions.

Conclusion

This month's MPC decision was a formality. The real clues on the next move for the BoE will come from the MPC minutes, and moreover, the thrust of the regional agents' report. The latest BoE regional agents' report might as well have been written by Danny Blanchflower and Adam Posen after a heavy night discussing the great depression and the Japanese deflation — it was very dove-friendly. We believe that the agents' report is rather lagging and the improvement in a number of more forward looking indicators will change the tone of that report starting from this month. We continue to believe that this latest instalment of QE will be the last, but in light of the last set of minutes and agents report, the situation is less clear-cut than we expected it to be.

Guy Haselmann (212) 225-6686
guy.haselmann@scotiabank.com

Should Investors Pay More Attention To The Bundesbank's Concerns?

- **A recent letter to the ECB from Bundesbank President Weidmann publicized concerns about growing imbalances in the Eurozone; specifically, the amount of money Germany is due through the TARGET2 system.**

Few would dispute that the European Union has needed to evolve from its current structure into one of greater integration. Unfortunately, the financial crisis and economic downturn has exposed the flaws and limitations of the current system. Those limitations, combined with policy actions, have caused imbalances to mount and are the basis behind the concerns recently expressed by the Bundesbank. Markets have not yet fully comprehended, for instance, the unintended consequences of the LTRO facility or the growing imbalances of the TARGET2 system. Sentiment and sovereign spreads may have improved recently, but behind the scenes, risks are growing and imbalances might be reaching a breaking point.

The two LTRO offerings combined to lend over $1 trillion to EU banks. The huge quantity was achievable because the ECB lowered (once again) the standards for eligible collateral. The ECB balance sheet has now ballooned to a record $3,960 billion. EU banks have over $600 billion in debt maturing in 2012, and so they were able to borrow cheap money to pre-fund their maturing obligations. In many cases, the banks parked the money in short dated sovereign bonds earning positive carry and zero-risk weighting.

Putting on this trade and earning carry is not risk-free. The banks who borrowed through the LTRO will likely get hit at some point with a variation margin call. This will occur when the collateral falls below a certain threshold. The ECB is required to impose variation margin on its financing operations. A margin call means the bank will either have to post more collateral or sell (non-eligible collateral) bonds to meet the margin call. Some collateral posted with the ECB has dubious valuation, and so the ECB-imposed haircuts offer some, but a limited, cushion of protection. Valuation and quality will probably worsen as the economy deteriorates. Margin calls could hit all borrowers at the same time, and so the selling to meet the margin could easily lead to more selling and so on, sparking a contagion.

The size of the LTRO can be interpreted in two opposing ways. On the one hand, a large LTRO means the banks have more money to put to work in risk assets and "MF Global carry trades". Investors are following the flow of money which is why risk assets have performed so well. On the other hand, a large LTRO is an indication of troubles in the banking system and by buying sovereign debt the banks intertwine their balance sheets more closely with the sovereign debt crisis.

The letter Bundesbank President Weidmann wrote to Mario Draghi publicized concerns about growing imbalances in the Eurozone; specifically, the amount of money Germany is due through the TARGET2 system. TARGET2 is the Eurozone's harmonized payment and settlement processing system for transactions between the members of the European system of central banks. The daily and aggregated transactions are without limit. Simply stated, TARGET2 is an intra-system cross-border accounting tool for claims and liabilities.

When money flows from Spain to Germany for example — say through the purchase of a company or asset — the ECB will assign an "accounts payable" to the Spanish Central Bank and an "accounts receivable" to Germany's Bundesbank. Since southern European countries import more than they export, they have relied on capital inflow from abroad to pay for the goods and services they bought. Conversely, since Germany consistently produces export surpluses, they have to export capital as well. These cash flows have been disrupted since the start of the economic crisis. Money has been withdrawn from troubled Eurozone countries and bank lending has dried-up. Greece, Portugal, Spain among others, no longer had enough money to fund their imports and so they borrowed from their national central banks (NCBs) who created money from nothing. The NCBs then charged it to the entire Eurozone by making a claim at the ECB through the TARGET2 system.

The system was effectively set up in the image of the Federal Reserve System, but unfortunately TARGET2 has no automatic rules for correcting imbalances. There is no annual settlement arrangement among the group of NCBs like at the Federal Reserve. This is the core of the problem. It seems the amount that Germany is due

Guy Haselmann (212) 225-6686
guy.haselmann@scotiabank.com

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continues to accrue and grow perpetually. Some even argue that all capital outflows and current account deficits get funded by Germany through TARGET2. If this is true, then the amount that Germany is due will aggregate to infinity and be owed by the NCBs of the crisis countries, and by those in Eurozone countries to whom Germany exports. Several white papers have been written on this topic.

Having no limits on TARGET2 imbalances is at the heart of what worries the Bundesbank. However, putting limits on the size of TARGET2 liabilities threatens the entire nature of the European monetary union. The mere fact that Germany exposed these worries means that Germany is losing confidence in the ability of the NCBs to honor their commitments. Germany seems concerned that the amount they are owed has become too uncomfortable because it is too great a percentage of its GDP. Ratings agencies may soon start to take notice.

Germany currently has an outstanding balance due to them of €498 billion: an amount equal to 1.5 times Germany's annual federal budget. This amount does not include transfers and guarantees made already and has nothing to do with ESM or EFSF commitments. The total potential costs to Germany may already be €1 trillion, or 30% of its GDP. As long as the Eurozone stays together the risks of Germany assuming these costs are low, but this is also where the problem lies. Hans-Werner Sinn, an economist and President of IFO, said that "these outstanding balances owed by other central banks, open Germany up to blackmail". The bottom line is that potential losses are small if the Eurozone stays together, but can become critical with exponential speed should the makeup of the Eurozone change.

If Greece leaves the monetary union, then all of the other Eurozone central banks would have to bear the Greek central bank's debt. Germany would assume 28% of Greece's €106 billion owed; a manageable cost of around €30 billion. However, the structure is such that as soon as one country leaves the Euro, others have an incentive to leave as well to prevent their NCB losses from increasing. Markets have not yet begun to handicap the possibility that Germany may have the greatest incentive to leave the Eurozone.

Germany has to figure out if the steep costs of leaving the Eurozone remain greater than the potential costs (losses) of remaining in the Eurozone. Currently, the liabilities in TARGET2 amount to 15% of GDP with total commitments arguably pushing that number closer to 30% of GDP. One economist estimated that should Germany leave the Eurozone, its economy would shrink by 15%. If this is true, then Germany could be reaching the tipping point, or point of indifference. Germany knows that these imbalances will only grow over time. Therefore, as soon as Germany loses faith in the ability of another NCB to pay its obligation, more vocal justification to exit the Eurozone may materialize.

Germany's level of trust in the entire process likely decreased recently: the ECB has taken the EU down a road with an inflationary bias, and Spain violated their fiscal targets — breaking the fiscal pact treaty within 24 hours of passage. German parliament and the Bundesbank must be furious that the ECB is relaxing its commitment to price stability. At the same time, sinking growth across the region is sapping revenues further, thus making deficits worse and austerity (to date) counter-productive.

A German exit would immediately shrink the size of the eurozone by 25%, so it is hard to imagine a defection by Germany not resulting in general disintegration. However, one of the biggest sources of imbalances in the Eurozone is that most countries are not competitive with Germany; therefore, removing Germany improves this dynamic. A policy of euro depreciation and moderate inflation would then meet less resistance from the remaining members. On the other hand, doing so could result in credit-rating downgrades, and thus higher sovereign spreads and interest costs.

The situation is quite fluid with too many chefs in the kitchen promoting their own ideas. Market risks and imbalances are increasing with extreme policy. Markets should start to consider a German exit as a distinct possibility. The Greek restructuring shifts the burden of future problems from the private sector to the official sector. Germany has its limit and the letter from the Bundesbank may be signaling that its breaking point is near. Germany recognizes the enormous costs of exiting, but at some point, sunk costs and exit costs outweigh the alternative.

Frédéric Prêtet (00 33) 17037-7705
frederic.pretet@scotiabank.com

ECB — Job Done

- **The ECB kept the refinancing rate unchanged as expected at the March meeting. Once again the governing council revealed that it did not even discuss adjusting rates.**
- **The ECB staff projection for growth this year was revised down but inflation was revised significantly upward. The upward revision for 2013 was minimal.**
- **The ECB expressed even more confidence regarding the success of the LTRO. It continues to monitor credit growth developments.**
- **While the medium term projection left the door open to further policy easing, the tone of the statement suggested that the ECB has for now finished delivering policy support.**

ECB inflation projection revised up and growth down

The upward revision to this year's inflation projection was widely expected given that oil has risen sharply and the EUR exchange rate has weakened compared with three months ago. However, the magnitude of this upward adjustment was far more abrupt than we had expected.

For this year we had expected a mid-point of the projection between 2.2% and 2.3%, from 2% previously. In the event, the ECB revised up even more aggressively to 2.4% y/y (with the forecast range between 2.1% and 2.7%). In other words, even the low-point of the forecast range was above 2% y/y for this year. Mr Draghi was keen to say that the ECB expects Eurozone inflation to revert back to below the 2% mark by early 2013.

Beyond the commodity price shock, higher indirect taxes were also mentioned to justify this increase and this factor could blur the picture a little. It is true that both the Italian and French parliaments approved prospective VAT rate hikes this autumn. For Italy, it would be a rise to 23% from 21% in September and for France from 19.6% to 21.2% in October. However, in the case of Italy, the increase will not take place if budget objectives are met by the end of August. Given slightly better than expected progress in reducing the budget deficit last year (to 3.9% compared to expectations of 4.0%), there is a possibility that it will not apply. Also, for France, the VAT hike is conditional on the re-election of Mr Sarkozy which, according to the recent pools, appears to be unlikely.

The assessment on the risk on inflation is still nonetheless seen as "broadly balanced", likely thanks to the fact that the 2013 inflation forecast has been revised only marginally higher to a mid-point of 1.6% from 1.5%. This figure is indeed still in line with the medium term price stability objective (albeit at the lower extreme). Despite such a low projection, the ECB president revealed that once again the Governing Council did not even discuss the possibility of moving rates.

As expected, the ECB revised down its growth forecast for both this and next year to mid-range targets at -0.1% and 1.1% respectively from 0.3% and 1.3% and risks are still seen on the downside (our own forecasts are still even slightly lower at around -0.5% for this year and 0.9% for 2013).

So assuming that EMU GDP growth will once again contract by around 0.2% to 0.3% in Q1, it suggests that GDP growth will run between 0.2% and 0.3% in each quarter up to the end of 2013. This implies a very slow — below

ECB Macroeconomic Projections

	2012			2013			2012 mid	2013 mid
ECB March forecast								
HICP	2.1	to	2.7	0.9	to	2.3	2.4	1.6
GDP	-0.5	to	0.3	0.0	to	2.2	-0.1	1.1
ECB December forecast (Previous)								
HICP	1.5	to	2.5	0.8	to	2.2	2.0	1.5
GDP	-0.4	to	1	0.3	to	2.3	0.3	1.3

Frédéric Prêtet (00 33) 17037-7705
frederic.pretet@scotiabank.com

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potential — recovery (potential is estimated at around 1.3% by the OECD). The ECB president recognised this fact by saying that the recovery will be "very gradual, if not slow".

More confidence that the job is done, justifying a status quo

Last month, the ECB president's statement already showed some confidence regarding the positive impact of the first long-term refinancing operation (LTRO) in easing financial tensions. This sentiment strengthened further this month, with Mr. Draghi calling it an "unquestionable success" in boosting confidence.

Nonetheless, it is still early days. The ECB president acknowledged that they are still observing the early signs of whether credit growth is being restored. The President referred to an internal ECB lending survey, which highlighted a "modest pickup" from the very negative trend in bank lending seen in the last survey. However, his comments suggested that it is now up to the banks and national governments to take advantage of the return in confidence provided by the ECB. The implication is that the central bank has done its part – "over to you". While the medium term inflation projection left the door ajar to further policy easing, the tone of the statement suggested that the ECB is unlikely to loosen monetary policy any further.

Camilla Sutton (416) 866-5470
camilla.sutton@scotiabank.com

Eric Theoret (416) 863-7030
eric.theoret@scotiabank.com

Copper & Volatility Measures Provide Clues For FX

- **Loose central bank policy and reasonable global growth forecasts have not yet changed and should continue to support CAD, AUD, NOK and SEK, among others.**

The US dollar strengthened broadly during the last six months of 2011, but the first two months of 2012 have been marked by a significant risk rally and a weak USD. The shift can be tied to several themes, explored below. Identifying when and if the risk rally is drawing to end will be an important piece of managing currency risk in 2012. In order to judge a shift in the current trend, volatility measures and copper prices are likely to provide the best clues. Currently, neither suggest that the AUD, CAD, MXN, NOK, SEK rallies are at risk.

Themes in 2012 that have driven a generally weak USD include:

- G4 central bank policy — A commitment from the Fed, BoE, BoJ & ECB to loose, if not loosening and aggressive policy for an extended period of time, has reduced tail risk, increased liquidity and suppressed volatility. This has provided a conducive backdrop for fueling the carry trade and supported the risk rally.
- Global growth outlook — A stabilization, and in some cases improvement, in the global growth outlook has been a welcome change from the summer and fall of 2011. It has supported currencies that are pro-cyclical, including AUD and CAD. The growth outlook remains an important risk going forward, particularly for Europe; however it is hard to ignore that both China's and the US outlook have improved since the fall.
- Europe, Europe and more Europe — The market's tunnel vision on Europe continues. The outlook has improved with some of the near-term banking and financial market risks having subsided; however the medium term outlook is still challenging. Our base case is that for FX traders, the risk of EUR will decouple from the broader USD move, leaving most currencies gaining ground against both the EUR and USD.
- Oil prices — which have been pushed higher by geopolitical risk, supply concerns, central bank policy, a weak USD and a stabilization in the global growth outlook, have helped to support currencies tied to oil exporters, (CAD and NOK). Oil is an important risk for 2012, as the higher it moves the more it threatens global growth.

Spotting a shift in global macros trends will prove an important part of currency management in 2012. Two of the most important themes that have driven the risk rally in 2012 are aggressive G4 central bank policy and an improvement in global growth. The purest way to follow the market's pricing of these two themes is through volatility and copper (with the latter being a good proxy for global growth). Volatility measures (both in equities and FX) remain within their year-to-date range and notably low - see chart 1. A shift above this range would provide the first clue that markets no longer perceive tail risk to have been removed and that the expectation for G4 central bank policy is changing; a precursor to a significant FX correction. The other side is copper, which has fallen from its February high of $398.95, but is still well within a range that suggests a reasonable global growth outlook. Should these metrics break out of their ranges it would suggest that the market environment is changing and that it is time to worry. For the near-term we expect volatility to remain low and copper reasonably strong, thereby suggesting that there is room for further upside for currencies associated with central banks who are not embracing aggressive policy, including CAD, AUD, NOK, SEK and MXN, to name a few.

CHART 1: G7 CURRENCY VOL DEPRESSED

CHART 2: COPPER STILL STRONG

Camilla Sutton (416) 866-5470
camilla.sutton@scotiabank.com

Eric Theoret (416) 863-7030
eric.theoret@scotiabank.com

A Brief Summary Of The Diverging Paths For CAD & EUR

- **CAD is expected to close 2012, having gained 4% year-over-year as the combination of its Triple-A status, strong oil prices, relative monetary policy, low volatility and sentiment are favourable.**

There was a time when the stars had aligned for CAD, and the currency appreciated rapidly. Looking at the Canadian backdrop independently of the global environment presents a more mixed picture for CAD; however we would argue that on a relative basis, the currency is likely to appreciate on a year-over-year basis. Some of the themes that are supporting CAD through parity include:

- Canada's triple A status, which in a shrinking universe of Triple A rated sovereigns, Canada's strong rating and developed bond market make it a natural home for investors searching to move away from Europe. These flows should remain positive for CAD in 2012.
- Commodity prices, including strong oil prices, might weigh on the outlook for growth, but removing the noise they remain a net positive for the Canadian economy and by default CAD. Accordingly oil above $100 bodes well for CAD's outlook.
- Global growth — CAD is known as a pro-cyclical currency, outperforming in periods of strong global growth and vice versa. The US outlook has improved over the last six months; the European outlook has worsened and Asian growth has stabilized. Together this presents a mixed picture for CAD.
- Canadian fundamentals have been stronger than they are today; however on a relative basis we still view these as favourable for CAD.
- Relative monetary policy suggests that the BoC is likely to tighten policy well before the Fed.
- The outlook for CAD is heavily influenced by risk aversion; the current low volatility environment has supported CAD at parity throughout February. We expect there to be spikes in risk aversion throughout the year but these cause only temporary CAD weakness; instead the broader risk environment is CAD positive.

Accordingly, we expect CAD to have a solid year, appreciating 4% from its closing 2011 level.

- **EUR is expected to trend lower in Q212, closing the year at 1.25**

It is hard to find a EUR bull, but the currency rallied 3% in the first two months of 2012. There are four important themes that supported this; but six other themes that should weigh on EUR into year-end. Below is a quick summary of all ten. We start with the four that support EUR:

- Flows, both repatriation and official central bank flows, remain positive for EUR, even as other investors search for alternatives.
- There is a limit to how strong the USD can sustainably be when a the economic backdrop is weak.
- High oil prices and the pressure it puts on inflation limits the ability of the ECB to ease policy from here.
- Germany has value, even in a worse case scenario.

Six themes that weigh on EUR, pushing it to trend lower in 2012:

- The carry trade, with low interest rates and a bearish outlook, EUR is often used as the funding side.
- Growth is likely to be weighed down by austerity, evolving into a vicious circle and threatening investor confidence.
- There is no overnight solution, with the road to recovery a long and painful one. Eventually, we would expect a shift towards closer fiscal ties; however there appears little political will for this in the current environment.
- The ECB's subordination of other Greek investors through its bond swap changes the dynamics of the European bond market and is negative for medium-term investors.
- Investor sentiment is wildly bearish, likely proving too strong a tide to fight over the medium-term.

We do not expect a EUR collapse, but instead look for it to trend lower interrupted by short periods of retracement, closing the year at 1.25.

Derek Holt (416) 863-7707
derek.holt@scotiabank.com

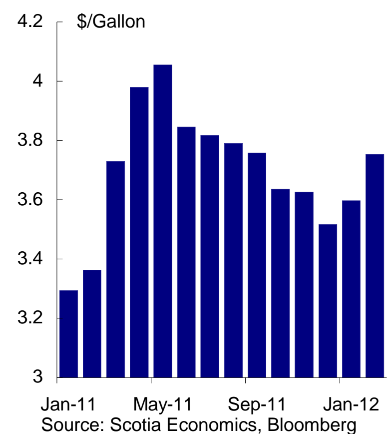
Dov Zigler (416) 862-3080
dov.zigler@scotiabank.com

Key Data Preview

UNITED STATES

It will be a fairly busy week with respect to US data releases. The main event will be the **FOMC meeting** and follow-on Fed Funds Rate announcement. Scotia is not expecting a policy change in light of the Fed's recent commitment to hold the Fed funds rate stable for the next three years. For more on this please see our *Week Ahead* column on page 2.

US February consumer prices will be released on March 16 and we anticipate that they will increase by 0.5% m/m in terms of headline data while core will increase 0.2% m/m. Prices have undoubtedly been in the news — particularly gasoline prices — and for a very good reason: the average price per gallon of gasoline moved from $3.52 in December to $3.59/gallon in January to $3.79/gallon in February (the price as of March 7 is $3.95/gallon). The 5.5% increase in the average gasoline price from January to February will impact headline CPI as gasoline makes up 5.25% of the index directly, forms a component of the 'fuels and utilities' segment, and has an indirect pass-through effect on a host of other consumer prices (although these effects are often lagged). The +0.3% immediate contribution to CPI that we expect from gasoline explains why we see month-on-month CPI momentum, but note that the average gasoline price in February implies an even steeper year-on-year CPI comparison (gas was $3.79/gallon in February 2012, $3.36/gallon in February 2011 — 12% higher). The difference in the year-on-year prices implies an even more significant addition of 0.6% to year-on-year headline CPI. This trend will probably reverse itself mid-year as the average gasoline price in April 2011 ($3.97/gallon) and in May 2011 ($4.06/gallon) were much higher than what we witnessed in February (although those prices are close to the current gasoline price).



US February industrial production data are also due out on March 16, and Scotia is anticipating muted growth of 0.2% (industrial production was flat at 0% in January). That's not to say that we're not enthusiastic about US manufacturing, which has been growing at a decent rate (+0.7% in January) led by autos (+6.8% in January); it's rather that the steady effect of lower natural gas prices combined with warmer weather has been to drag on utilities output (-2.5% in January), pulling down the full industrial production aggregate.

US February retail sales will be released on March 13, and Scotia is anticipating an acceleration to 1% m/m in the headline and 0.7% m/m in core ex-autos after more muted growth of 0.4% m/m headline and 0.7% core in January. The two major trends that we highlighted above — higher gasoline prices and an acceleration in auto demand and production — are likely to be main drivers here as well. With respect to sales momentum in stores, chain store sales as measured by ICSC trended up quite strongly in February, although that's a fairly volatile metric which, even when smoothed, at best offers a signal with respect to direction as opposed to scope. A first look at March manufacturing momentum will come from the release of the **Empire Manufacturing Index** and the **Philadelphia Fed Diffusion Index** on March 15.

CANADA

January manufacturing sales will be released on March 16. Scotia is anticipating a solid gain (+0.8%) in manufacturing sales mainly on the back of an increase in petroleum output as well as solid growth in the autos category. Machinery and equipment is likely to impose a considerable drag. The main story with respect to Canada manufacturing sales is that the absolute level of Canadian manufacturing output only recently returned to pre-crisis levels, implying that even as the consumption side of the Canadian economy recovered fairly briskly, the production side has lagged considerably, and in the process reoriented itself even further towards output of industrial goods and energy products – and away from machinery and equipment. This trend is one of the main explanatory variables in assessing the lagging growth and employment in Ontario and Quebec relative to Alberta, Saskatchewan, and British Columbia. We anticipate that January's manufacturing sales report will highlight this ongoing change.

Daniela Blancas (416) 862-3908
daniela.blancas@scotiabank.com
Sarah Howcroft (416) 863-2859
sarah.howcroft@scotiabank.com
Oscar Sánchez (416) 862-3174
oscar.sanchez@scotiabank.com

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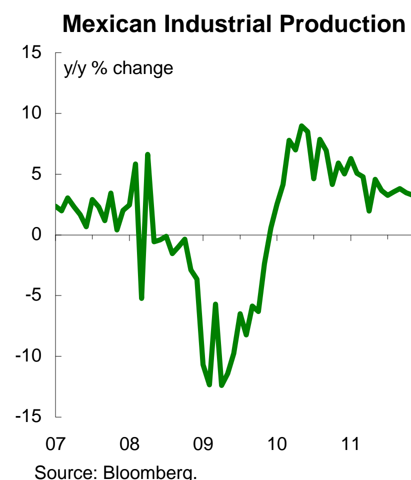
EUROPE

Next Wednesday (March 14th) the Norges Bank, the central bank of Norway, will announce the outcome of the latest meeting of the Executive Board. We expect the bank to maintain the benchmark deposit rate unchanged at 1.75%. The rate was lowered by 50 basis points (bps) following the last meeting on December 14th, surprising market expectations of a smaller cut. Since December, many of the fears of a European meltdown have abated, and signs of stabilization have emerged in both financial markets and economic activity. In Norway, mainland GDP growth for the fourth quarter turned out stronger than expected (0.6% q/q, 1.6% for 2011 as a whole), and the seasonally adjusted unemployment rate edged lower to 3.3% in December. Moreover, on the back of surging oil prices (Brent has gained 17% year-to-date) and record-high house prices, inflation picked up more than expected in February, rising to 1.2% y/y from 0.5% in January (on a monthly basis, the February gain of 1.0% reversed the prior month's 0.2% contraction). On the other hand, the Norwegian krone (NOK) continues to strengthen on the back of its status as a safe alternative to the euro and its link to oil prices. The NOK has gained nearly 5% against the US dollar year-to-date, and reached a record-high of 7.40 versus the euro on March 2nd. We judge that the deflationary pressure from the strong NOK will be offset by higher commodity prices and a decent pace of domestic activity, inducing the central bank to maintain a neutral stance (keeping the deposit rate at 1.75%) through the remainder of the year.

LATIN AMERICA

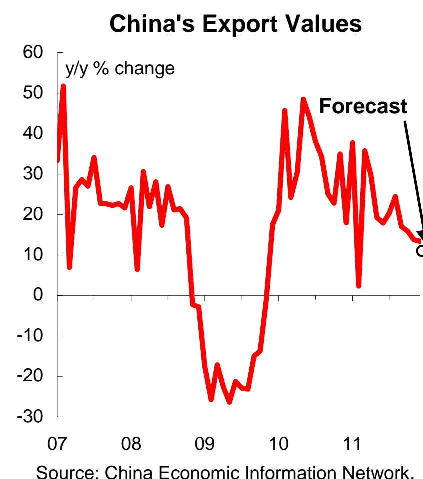
Industrial production (IP) in Mexico is expected to maintain its solid — though moderate — pace of growth in the first months of 2012. We expect IP to expand by 2.9% y/y in January. IP increased by 2.8% y/y in December, slowing from 3.3% in November; however the manufacturing and construction sectors grew by a solid 3.7% and 3.6%, respectively. The automotive sector, which represents close to 12% of total industrial production, continues to outperform as a result of strong demand in the US and Latin America. On a monthly basis, IP registered a modest uptick of 0.85% m/m against December, with electricity, water and gas, manufacturing and construction driving the expansion; however the mining sector — both on an annual and monthly basis — remained subdued, decreasing by 0.26% m/m and by 1.3% y/y.



Source: Bloomberg.

ASIA

China's trade figures for February will be reported next week. While start-of-the-year numbers for China are usually distorted because of Lunar New Year festivities, we expect the January-February combined observations to result in a 12.7% y/y expansion in export values. This implies an expected 33.4% y/y gain in the value of foreign sales in February alone. This result would continue to reflect the pattern registered in the final months of 2011, when Chinese foreign shipments displayed a downtrend due for the most part to slowing exports to Europe. On the imports side, we anticipate a 7.8% y/y gain for the combined January-February figures; which would imply a 39% y/y gain for February.



Source: China Economic Information Network.

Key Indicators for the week of March 12 - 16

North America

Country	Date	Time	Event	Period	BNS	Consensus	Latest
MX	MAR 9-15		ANTAD Same-Store Sales (YoY)	FEB	--	--	3.5
US	03/12	14:00	Monthly Budget Statement (US$ bns)	FEB	--	-229.4	-27.4
US	03/13	07:30	NFIB Small Business Optimism	FEB	--	94.3	93.9
US	03/13	08:30	Advance Retail Sales (MoM)	FEB	1.0	1.0	0.4
US	03/13	08:30	Retail Sales Less Autos (MoM)	FEB	0.7	0.7	0.7
US	03/13	08:30	Retail Sales Ex Auto & Gas (MoM)	FEB	--	0.5	0.6
US	03/13	10:00	JOLTs Job Openings	JAN	--	--	3376
US	03/13	10:00	Business Inventories (MoM)	JAN	--	0.6	0.4
MX	03/13	10:00	Industrial Production (YoY)	JAN	2.9	3.2	2.8
MX	03/13	10:00	Industrial Production (MoM)	JAN	--	--	0.9
MX	03/13	11:00	International Reserves Weekly (US$ mns)	9-Mar	--	--	148848
MX	03/13	11:00	Vehicle Exports (AMIA)	FEB	--	--	158342
MX	03/13	11:00	Vehicle Domestic Sales (AMIA)	FEB	--	--	75297
MX	03/13	11:00	Vehicle Production (AMIA)	FEB	--	--	202701
US	03/13	14:15	**FOMC Rate Decision**	13-Mar	**0.25**	**0.25**	**0.25**
US	03/14	07:00	MBA Mortgage Applications (WoW)	9-Mar	--	--	-1.2
CA	03/14	08:30	Capacity Utilization Rate	4Q	--	81.6	81.3
US	03/14	08:30	Import Price Index (MoM)	FEB	--	0.6	0.3
US	03/14	08:30	Import Price Index (YoY)	FEB	--	5.6	7.1
MX	03/14	10:00	Aggregate Supply & Demand (YoY)	4Q	4.8	--	4.9
US	03/15	08:30	Empire Manufacturing	MAR	--	17.4	19.5
US	03/15	08:30	Producer Price Index (MoM)	FEB	0.5	0.5	0.1
US	03/15	08:30	PPI Ex Food & Energy (MoM)	FEB	0.2	0.2	0.4
US	03/15	08:30	Producer Price Index (YoY)	FEB	--	3.1	4.1
US	03/15	08:30	PPI Ex Food & Energy (YoY)	FEB	--	2.9	3.0
US	03/15	08:30	Initial Jobless Claims (000s)	10-Mar	355	355	362
US	03/15	08:30	Continuing Claims (000s)	3-Mar	3450	--	3416
US	03/15	09:00	Total Net TIC Flows (US$ bns)	JAN	--	--	87.1
US	03/15	09:00	Net Long-term TIC Flows (US$ bns)	JAN	--	--	17.9
US	03/15	10:00	Philadelphia Fed.	MAR	9.5	11.0	10.2
CA	03/16	08:30	Int'l Securities Transactions (C$ bns)	JAN	--	--	7.4
CA	03/16	08:30	Manufacturing Sales (MoM)	JAN	0.8	-0.2	0.6
US	03/16	08:30	Consumer Price Index (MoM)	FEB	0.5	0.4	0.2
US	03/16	08:30	CPI Ex Food & Energy (MoM)	FEB	0.2	0.2	0.2
US	03/16	08:30	Consumer Price Index (YoY)	FEB	3.0	2.9	2.9
US	03/16	08:30	CPI Ex Food & Energy (YoY)	FEB	2.3	2.2	2.3
US	03/16	09:15	Industrial Production (MoM)	FEB	0.2	0.4	0.0
US	03/16	09:15	Capacity Utilization	FEB	78.6	78.8	78.5
US	03/16	09:55	U. of Michigan Confidence	MAR P	75.0	75.6	75.3
MX	03/16	11:00	**Overnight Rate**	16-Mar	**4.50**	**4.50**	**4.50**

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

Key Indicators for the week of March 12 - 16

Europe

Country	Date	Time	Event	Period	BNS	Consensus	Latest
SP	03/12		Spain Budget Balance YTD (€ mns)	JAN	--	--	-52385
SP	03/12	04:00	House transactions (YoY)	JAN	--	--	-25.3
IT	03/12	05:00	GDP sa and wda (QoQ)	4Q F	-0.7	-0.7	-0.7
IT	03/12	05:00	GDP sa and wda (YoY)	4Q F	-0.5	-0.5	-0.5
PO	03/12	06:00	CPI - EU Harmonised (YoY)	FEB	--	--	3.4
PO	03/12	07:00	Trade Balance (€ mns)	JAN	--	--	-1041.0
UK	03/12	20:01	RICS House Price Balance (%)	FEB	--	-14.0	-16.0
GE	03/12	03:00	Wholesale price Index (YoY)	FEB	--	2.6	3.0
FR	03/13	02:30	CPI - EU Harmonised (MoM)	FEB	0.5	0.5	-0.4
FR	03/13	02:30	CPI - EU Harmonised (YoY)	FEB	2.6	2.6	2.6
FR	03/13	02:30	Consumer Price Index (MoM)	FEB	--	0.4	-0.4
FR	03/13	02:30	Consumer Price Index (YoY)	FEB	--	2.4	2.3
FR	03/13	02:30	CPI Ex Tobacco Index	FEB	123.7	123.7	123.1
FR	03/13	03:45	Current Account (€ bns)	JAN	--	--	-3.0
SP	03/13	04:00	CPI (EU Harmonised) (MoM)	FEB	0.0	0.1	-1.7
SP	03/13	04:00	CPI (EU Harmonised) (YoY)	FEB F	1.9	1.9	1.9
SP	03/13	04:00	CPI (Core Index) (YoY)	FEB	--	1.1	1.3
SP	03/13	04:00	Consumer Price Index (YoY)	FEB F	2.0	2.0	2.0
SW	03/13	04:30	CPI - Headline Rate (YoY)	FEB	--	1.8	1.9
IT	03/13	05:00	CPI (NIC incl. tobacco) (YoY)	FEB F	3.3	3.3	3.3
IT	03/13	05:00	CPI - EU Harmonized (YoY)	FEB F	3.4	3.4	3.4
UK	03/13	05:30	Visible Trade Balance GBP/Mn	JAN	--	-7900	-7111
UK	03/13	05:30	Trade Balance Non EU GBP/Mn	JAN	--	-4300	-3748
UK	03/13	05:30	Total Trade Balance (GBP/Mln)	JAN	--	-1900	-1109
GE	03/13	06:00	Zew Survey (Current Situation)	MAR	--	41.5	40.3
EC	03/13	06:00	ZEW Survey (Econ. Sentiment)	MAR	--	--	-8.1
GE	03/13	06:00	ZEW Survey (Econ. Sentiment)	MAR	--	10.0	5.4
IR	03/13	07:00	Industrial Production SA (YoY)	JAN	--	--	-4.7
UK	03/14	05:30	Claimant Count Rate	FEB	--	5.0	5.0
UK	03/14	05:30	Jobless Claims Change (000s)	FEB	--	5.0	6.9
UK	03/14	05:30	Average Weekly Earnings 3M/YoY	JAN	--	1.9	2.0
UK	03/14	05:30	ILO Unemployment Rate (3mths)	JAN	--	8.4	8.4
EC	03/14	06:00	Euro-Zone CPI - Core (YoY)	FEB	--	1.6	1.5
EC	03/14	06:00	Euro-Zone CPI (MoM)	FEB	0.5	0.5	-0.8
EC	03/14	06:00	Euro-Zone CPI (YoY)	FEB	2.7	2.7	2.6
EC	03/14	06:00	Euro-Zone Ind. Prod. wda (YoY)	JAN	-0.9	-0.8	-2.0
EC	03/14	06:00	Euro-Zone Ind. Prod. sa (MoM)	JAN	--	0.5	-1.2
NO	03/14	09:00	**Norwegian Deposit Rates**	14-Mar	**1.75**	**1.75**	**1.75**
SP	03/15	04:00	House Prices ToT Homes (YoY)	4Q	--	--	-7.4
SW	03/15	04:30	Unemployment Rate	FEB	--	8.0	8.0
EC	03/15	05:00	ECB Publishes March Monthly Report				
NO	03/15	05:00	Trade Balance (NOK bns)	FEB	--	42.0	44.1
IT	03/15	05:30	General Government Debt (€ mns)	JAN	--	--	1897946
EC	03/15	06:00	Eurozone Employment (YoY)	4Q	--	--	0.3
EC	03/15	06:00	Euro-Zone Labour Costs (YoY)	4Q	--	2.3	2.7
IR	03/15	07:00	CPI (EU Harmonised) (YoY)	FEB	--	--	1.3
SP	03/16	04:00	Labour Costs (YoY)	4Q	--	--	1.5
IT	03/16	05:00	Trade Balance (Total) (€ mns)	JAN	--	--	1447
IT	03/16	06:00	Current Account (€ mns)	JAN	--	--	402
EC	03/16	06:00	Euro-Zone Trade Balance (€ bns)	JAN	--	-3.0	9.7

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

Key Indicators for the week of March 12 - 16

Asia Pacific

Country	Date	Time	Event	Period	BNS	Consensus	Latest
CH	MAR 9-10		Trade Balance (US$ bns)	FEB	-16	-5.4	27.3
CH	MAR 9-10		Exports (YoY)	FEB	33.0	31.1	-0.5
CH	MAR 9-10		Imports (YoY)	FEB	39.0	31.8	-15.3
JN	03/11	19:50	Machine Orders (MoM)	JAN	--	2.3	-7.1
JN	03/11	19:50	Machine Orders (YoY)	JAN	--	4.4	6.3
JN	03/11	19:50	Domestic CGPI (MoM)	FEB	--	0.2	-0.1
JN	03/11	19:50	Domestic CGPI (YoY)	FEB	--	0.6	0.5
MA	03/12	00:01	Industrial Production (YoY)	JAN	--	0.8	3.0
MA	03/12	00:01	Manufacturing Sales Value (YoY)	JAN	--	--	1.1
JN	03/12	01:00	Consumer Confidence	FEB	--	40.5	40.0
IN	03/12	01:30	Industrial Production (YoY)	JAN	--	2.1	1.8
PH	03/12	21:00	Total Exports (YoY)	JAN	--	-17.7	-18.9
PH	03/12	21:00	Total Monthly Exports (US$ mns)	JAN	--	--	3407
JN	MAR 12-13		**BOJ Target Rate**	13-Mar	**0.10**	**0.10**	**0.10**
HK	03/13	04:30	Industrial Production (YoY)	4Q	--	--	0.2
HK	03/13	04:30	Producer Price (YoY)	4Q	--	--	9.6
SK	03/13	19:00	Unemployment Rate (SA)	FEB	3.2	3.2	3.2
CH	MAR 13-18		Actual FDI (YoY)	FEB	--	14.6	-0.3
TH	MAR 13-16		Current Account Balance (US$ mns)	JAN	--	1500	1940
TH	MAR 13-16		Total Exports (US$ mns)	JAN	--	--	16856
TH	MAR 13-16		Total Exports (YoY)	JAN	--	--	-2.1
TH	MAR 13-16		Total Imports (US$ mns)	JAN	--	--	17094
TH	MAR 13-16		Total Imports (YoY)	JAN	--	--	19.6
TH	MAR 13-16		Total Trade Balance (US$ mns)	JAN	--	--	-238
JN	03/14	00:30	Industrial Production (MoM)	JAN F	--	--	2.0
JN	03/14	00:30	Industrial Production (YoY)	JAN F	--	--	-1.2
IN	03/14	02:30	Monthly Wholesale Prices (YoY)	FEB	6.2	6.7	6.6
IN	03/15	02:30	**India REPO Cutoff Yld**	15-Mar	**8.50**	**8.50**	**8.50**
IN	03/15	02:30	Cash Reserve Ratio	15-Mar	5.00	--	4.75
IN	03/15	02:30	Reverse Repo Rate	15-Mar	7.50	7.50	7.50

Latin America

Country	Date	Time	Event	Period	BNS	Consensus	Latest
BZ	03/12	07:30	Central Bank Weekly Economists Survey				
CL	03/12	08:30	Central Bank Economist Survey				
BZ	03/12	14:00	Trade Balance (FOB) - Weekly (US$ mns)	11-Mar	--	--	268.0
PE	03/12		Trade Balance (US$ mns)	JAN	--	--	1188.2
BZ	MAR 14-21		Economic Activity Indx (MoM) SA	FEB	--	-0.2	0.6
BZ	MAR 14-21		Economic Activity Indx (YoY) NSA	FEB	--	--	1.5
BZ	MAR 14-21		CAGED Formal Job Creation	FEB	--	--	118895
BZ	03/15	07:30	COPOM Monetary Policy Meeting Minutes				
CO	03/15	17:00	Trade Balance (US$ mns)	JAN	--	900	1210
CL	03/15	18:00	**Nominal Overnight Rate Target**	15-Mar	**5.00**	**5.00**	**5.00**
PE	03/15		Economic Activity Indx (YoY) NSA	JAN	--	--	6.0
PE	03/15		Unemployment Rate	FEB	--	--	7.8
PE	MAR 16-23		Central Bank Quarterly Inflation Report				

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

Global Auctions for the week of March 12 - 16

North America

Country	Date	Time	Event
US	03/12	11:00	U.S. Fed to Purchase USD1.75-2.25 Bln Notes
US	03/12	11:30	U.S. to Sell 3-Month Bills
US	03/12	11:30	U.S. to Sell 6-Month Bills
US	03/12	13:00	U.S. to Sell 3-Year Notes
CA	03/13	10:30	Canada to Sell CAD7.7 Bln 98-Day Bills
CA	03/13	10:30	Canada to Sell CAD2.9 Bln 182-Day Bills
CA	03/13	10:30	Canada to Sell CAD2.9 Bln 364-Day Bills
US	03/13	11:30	U.S. to Sell 4-Week Bills
US	03/13	13:00	U.S. to Sell 10-Year Notes Reopening
US	03/14	11:00	U.S. Fed to Purchase USD1.00-1.50 Bln Notes
US	03/14	13:00	U.S. to Sell 30-Year Bonds Reopening
US	03/15	11:00	U.S. Fed to Purchase USD3.50-4.25 Bln Notes
US	03/16	11:00	U.S. Fed to Sell USD8-8.75 Bln Notes

Europe

Country	Date	Time	Event
GE	03/12	06:30	Germany to Sell EU4 Bln 6-Mth Bills
FR	03/12	10:00	France to Sell Bills (BTF)
IT	03/13	06:00	Italy to Sell Bills
NE	03/13	08:00	Netherlands to Sell Up to EUR3.5 Bln 2015 Bonds on March 13
IT	03/14	06:00	Italy to Sell Bonds/Floating Rate Notes (BTP/CCT)
SZ	03/14	06:30	Switzerland to Sell Bonds
SP	03/15	05:30	Spain to Sell Bonds
FR	03/15	06:00	France to Sell Bonds/Notes (OAT/BTAN)
UK	03/15	06:30	U.K. to Sell GBP2 Bln 4.5% 2042 Bonds
UK	03/16	07:10	U.K. to Sell Bills

Asia Pacific

Country	Date	Time	Event
CH	03/11	23:00	Agricul Dev Bank China to Sell CNY15 Bln 7-Year Bonds
CH	03/12	23:00	Agricul Dev Bank China to Sell CNY20 Bln 3-Year Bonds
JN	03/13	23:35	Japan to Sell 3-Month Bills
NZ	03/14	21:30	New Zealand Plans to Sell Government Bonds
JN	03/14	23:35	Japan to Sell 1-Year Bills
JN	03/14	23:45	Japan to Sell 20-Year Bonds

Latin America

Country	Date	Time	Event
BZ	03/13	11:00	Brazil to Sell I/L Bonds due 8/15/2016 - NTN-B
BZ	03/13	11:00	Brazil to Sell I/L Bonds due 8/15/2018 - NTN-B
BZ	03/13	11:00	Brazil to Sell I/L Bonds due 8/15/2022 - NTN-B
BZ	03/13	11:00	Brazil to Sell I/L Bonds due 8/15/2030 - NTN-B
BZ	03/13	11:00	Brazil to Sell I/L Bonds due 8/15/2040 - NTN-B
BZ	03/13	11:00	Brazil to Sell I/L Bonds due 8/15/2050 - NTN-B
BZ	03/15	10:00	Brazil to Sell Bills due 10/1/2012 - LTN
BZ	03/15	10:00	Brazil to Sell Bills due 4/1/2014 - LTN
BZ	03/15	10:00	Brazil to Sell Bills due 1/1/2016 - LTN
BZ	03/15	10:00	Brazil to Sell Floating-rate Notes due 3/1/2018 - LFT

Source: Bloomberg, Scotia Economics.

Events for the week of March 12 - 16

North America

Country	Date	Time	Event
CA	03/12	12:30	Bank of Canada's Macklem Speaks in Sao Paulo
US	03/13	14:15	FOMC Rate Decision
US	03/14	09:00	Fed's Bernanke Speaks to Community Bankers in Nashville, TN
US	03/14	09:00	NYCEDC Executive Committee Meeting
MX	03/16	11:00	Overnight Rate

Europe

Country	Date	Time	Event
EC	MAR 9-10		EU Foreign Ministers Meet in Copenhagen
GE	03/12	05:20	Schaeuble Holds Speech on Tax Policy at ZDH: Berlin
EC	03/12	10:30	ECB Announces Weekly Bond Purchases
EC	03/12	10:30	ECB Calls for Bids in 7-Day Main Refinancing Tender
EC	03/12	10:30	ECB Calls for Bids in 1-Month Refinancing Tender
IT	03/12	11:00	Labor Minister, Social Partners Meet for Labor Reform Talks
EC	03/12	12:00	Euro-Area Finance Ministers Meet in Brussels
EC	03/13	04:00	EU Finance Ministers Meet in Brussels
EC	03/13	04:00	EU's Van Rompuy, Barroso Speak to European Parliament
GE	03/13	06:00	Bundesbank Publishes 2011 Annual Accounts
EC	03/13	06:15	ECB Announces Allotment in 7-Day Main Refinancing Tender
EC	03/13	06:15	ECB Announces Allotment in 1-Month Refinancing Tender
EC	03/13	08:00	ECB Allots 7-Day Term Deposits
GE	03/13	09:00	ECB's Weidmann Speaks After Bundesbank Publishes Annual Report
IT	03/13	12:00	Italian Prime Minister Monti Meets German Chancellor Merkel
EC	03/14	04:15	ECB Calls for Bids in 7-Day Dollar Tender
PO	03/14	05:30	Portuguese Finance Minister Speaks at Parliamentary Commission
EC	03/14	06:00	ECB Announces Allotment in 7-Day US Dollar Tender
UK	03/14	08:00	Prime Minister's Question Time in House of Commons
UK	03/14	10:30	Europe Scrutiny Committee Questions Hoban on Euro-Area Crisis
GE	03/14	13:00	Merkel Holds Town Hall on Germany Economy in Heidelberg
EC	03/15	04:00	Euromoney Conference in Luxembourg
EC	03/15	05:00	ECB Publishes March Monthly Report
FI	03/15	05:00	ECB's Liikanen Speaks in Helsinki
IT	03/15	06:00	Bank of Italy Releases Jan. Public Finance Supplement
AS	03/15	14:30	ECB's Nowotny Speaks in Vienna
UK	03/15	20:00	Bank of England Financial Policy Committee Holds Meeting
GE	03/16	07:30	Merkel Holds News Conference With German Industry Associations
US	03/16	12:00	Portugal's Gaspar Speaks in Washington

Source: Bloomberg, Scotia Economics.

Events for the week of March 12 - 16

Asia Pacific

Country	Date	Time	Event
PH	MAR 11-16		Budget Deficit/Surplus
NZ	03/12	19:00	Quotable Value NZ House Price Inflation Report
JN	MAR 12-13		BOJ Target Rate
CH	03/13	12:00	China NPC: Premier Wen Jiabao Annual Press Briefing
IN	03/14	07:00	182 Day T-Bill Cutoff Yield
IN	03/14	07:00	91 Day T-Bill Cutoff Yield
NZ	03/14	17:00	ANZ Job Advertisements
NZ	03/14	17:30	Business NZ Publishes Performance of Manufacturing Index
NZ	03/14	20:00	ANZ-Roy Morgan Consumer Confidence Survey
AU	03/14	20:30	Reserve Bank Board - Bulletin - March Quarter 2012
AU	03/14	20:30	RBA Foreign Exchange Transactions
IN	03/15	02:30	India REPO Cutoff Yld
IN	03/15	02:30	Cash Reserve Ratio
IN	03/15	02:30	Reverse Repo Rate
IN	03/16	01:30	India Federal Budget

Latin America

Country	Date	Time	Event
CL	03/12	08:30	Central Bank Economist Survey
CL	03/15	18:00	Nominal Overnight Rate Target
CL	MAR 15-16		Argentina's President Fernandez Visits Chile

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	April 17, 2012	1.00	--
Federal Reserve – Federal Funds Target Rate	0.25	March 13, 2012	0.25	0.25
Banco de México – Overnight Rate	4.50	March 16, 2012	4.50	4.50

Events: Scotia expects that the FOMC will maintain the Fed Funds rate at 0.25% and will not signal additional monetary accommodation at its Mar. 13 meeting. Outlook: Scotia sees very strong likelihood that the Fed will hold the Fed Funds rate at 0.25% into 2014. There is risk that the Fed will expand its balance sheet later in 2012. Scotia expects the BoC to hold its overnight rate at 1.00% through mid-2013. Scotia expects that the Fed's projection that the Fed Funds rate will be held constant through 2014 will condition the flexibility of Canadian monetary policy.
Recent inflation numbers in Mexico suggest that the central bank will maintain the overnight interest rate at 4.50% at their next meeting on March 16th. February's yearly headline inflation slowed from 4.05% in January to 3.87%, returning to the central bank's tolerance range, while core-inflation remained stable at 3.37%. Food prices, which tend to have a temporary effect, have been the major contributor to inflation performance. Additionally, economic activity has shown some signs of deceleration, but remains solid, allowing the central bank to maintain a neutral stance.

Europe

Rate	Current Rate	Next Meeting	Scotia's Forecasts	Consensus Forecasts
European Central Bank – Refinancing Rate	1.00	April 4, 2012	1.00	--
Bank of England – Bank Rate	0.50	April 5, 2012	0.50	0.50
Swiss National Bank – Libor Target Rate	0.00	March 15, 2012	0.00	0.00
Central Bank of Russia – Refinancing Rate	8.00	March 11, 2012	8.00	8.00
Hungarian National Bank – Base Rate	7.00	March 27, 2012	7.00	7.00
Central Bank of the Republic of Turkey – 1 Wk Repo Rate	5.75	March 27, 2012	5.75	--

The Swiss National Bank (SNB) will maintain the LIBOR target range of 0-0.25% after the meeting on March 15th, and will likely also leave the currency floor unchanged (currently 1.20 francs per euro). On the back of rising oil prices, February saw the first monthly gain in the consumer price index since September. (Though the year-over-year rate of deflation accelerated to 0.9% from 0.8% in January, the pickup was less than expected). Investor confidence in the SNB's ability to maintain the current floor is strong and the foreign exchange target is regarded as a credible monetary policy instrument, as evidenced by the relative stability of the franc in the 1.205-1.210 per euro range year-to-date. Nevertheless, if the franc continues to weigh on exports in the coming months (exports dropped 3.4% m/m in January) and/or if deflationary pressures intensify, the Swiss monetary authorities will likely opt to adjust the floor upwards.

Asia Pacific

Rate	Current Rate	Next Meeting	Scotia's Forecasts	Consensus Forecasts
Bank of Japan – Target Rate	0.10	March 13, 2012	0.10	0.10
Reserve Bank of Australia – Cash Target Rate	4.25	April 3, 2012	4.25	4.25
Reserve Bank of New Zealand – Cash Rate	2.50	April 25, 2012	2.25	--
People's Bank of China – Lending Rate	6.56	TBA	--	--
Reserve Bank of India – Repo Rate	8.50	March 15, 2012	8.50	8.50
Bank of Korea – Bank Rate	3.25	April 12, 2012	3.00	--
Bank of Thailand – Repo Rate	3.00	March 21, 2012	3.00	--
Bank Indonesia – Reference Interest Rate	5.75	April 12, 2012	5.75	--

The Bank of Japan (BoJ) will likely leave monetary conditions unchanged for now. After orchestrating a weakening of the Japanese yen (JPY) through a significant expansion of its bond-buying program, clear statements of an inflationary goal and unilateral foreign exchange market intervention, we expect the BoJ to remain in wait-and-see mode. Despite the rebound in the JPY, encouraging recent indicators of Japan's economic performance support our view. The Reserve Bank of India (RBI) will likely leave the benchmark repo rate unaltered as well. While we expect further disinflation to have occurred during February, yearly wholesale inflation remains relatively elevated north of 6% y/y (we expect it to have come down to 6.2% in February) as subdued food price pressures continue to be partly offset by double-digit yearly gains in fuel costs. The latter, however, are also trending down albeit at a more measured pace. The RBI decided to lower the cash reserve requirement for banks by 75 basis points (bps) yesterday, to 4.75%; this follows the 50 bps reduction decreed in January.

Latin America

Rate	Current Rate	Next Meeting	Scotia's Forecasts	Consensus Forecasts
Banco Central do Brasil – Selic Rate	9.75	April 18, 2012	9.75	--
Banco Central de Chile – Overnight Rate	5.00	March 15, 2012	5.00	5.00
Banco de la República de Colombia – Lending Rate	5.25	March 23, 2012	5.25	5.25
Banco Central de Reserva del Perú – Reference Rate	4.25	April 12, 2012	4.25	--

After cutting rates in December, the central bank of Chile has maintained the reference rate unchanged at 5.0%. The expansionary monetary policy cycle has been less aggressive than our initial forecast. Inflation rebounded in February to 4.42% y/y after falling to 4.23% in January, reducing expectations for another rate cut at the next meeting. We now expect the central bank to maintain a moderate loosening stance and leave the reference rate at 5.0% at the March meeting, waiting for more signs of the economic performance in the coming months.

Africa

Rate	Current Rate	Next Meeting	Scotia's Forecasts	Consensus Forecasts
South African Reserve Bank – Repo Rate	5.50	March 29, 2012	5.50	--

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

Forecasts as at March 6, 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	3.7	3.4	3.9				
Canada	2.2	2.5	2.0	2.1	2.1	2.9	1.9	2.0
United States	1.8	1.7	2.1	2.2	2.5	3.1	2.4	2.0
Mexico	2.1	3.9	3.1	3.7	4.9	3.6	4.1	4.1
United Kingdom	2.0	0.8	1.0	1.8	2.1	4.2	2.2	2.5
Euro zone	1.4	1.5	-0.5	0.9	2.1	2.7	1.8	1.9
Japan	0.9	-0.9	2.2	1.7	-0.3	-0.1	0.0	0.2
Australia	3.1	2.1	3.8	3.3	3.1	3.1	2.9	2.7
China	9.5	9.2	8.6	8.9	2.3	4.1	4.5	4.3
India	7.6	7.2	7.4	7.6	6.4	7.5	5.5	5.0
Korea	4.6	3.6	3.9	4.2	3.1	3.7	3.3	3.0
Thailand	4.4	0.1	3.8	4.5	2.7	3.5	3.0	2.8
Brazil	3.7	2.7	3.8	4.5	6.6	6.5	5.5	5.0
Chile	3.8	6.2	3.9	5.5	3.3	3.3	2.8	3.5
Peru	5.5	6.8	5.5	5.6	2.4	4.7	3.0	2.5
Central Bank Rates (%, end of period)	**12Q1f**	**12Q2f**	**12Q3f**	**12Q4f**	**13Q1f**	**13Q2f**	**13Q3f**	**13Q4f**
Bank of Canada	1.00	1.00	1.00	1.00	1.00	1.00	1.25	1.50
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	4.25	4.25	4.25	4.25	4.25	4.25	4.50	4.50
Exchange Rates (end of period)								
Canadian Dollar (USDCAD)	1.02	1.01	0.99	0.98	0.98	0.97	0.97	0.96
Canadian Dollar (CADUSD)	0.98	0.99	1.01	1.02	1.02	1.03	1.03	1.04
Euro (EURUSD)	1.32	1.28	1.27	1.25	1.25	1.26	1.28	1.29
Sterling (GBPUSD)	1.58	1.59	1.62	1.63	1.65	1.66	1.67	1.68
Yen (USDJPY)	78	80	80	82	83	83	84	84
Australian Dollar (AUDUSD)	1.06	1.07	1.08	1.09	1.10	1.10	1.11	1.11
Chinese Yuan (USDCNY)	6.3	6.2	6.1	6.1	6.0	6.0	5.9	5.8
Mexican Peso (USDMXN)	12.8	12.9	13.0	13.1	13.2	13.1	13.2	13.4
Brazilian Real (USDBRL)	1.72	1.73	1.74	1.75	1.77	1.80	1.82	1.85
Commodities (annual average)	**2000-10**	**2011**	**2012f**	**2013f**				
WTI Oil (US$/bbl)	54	95	110	115				
Brent Oil (US$/bbl)	52	111	125	125				
Nymex Natural Gas (US$/mmbtu)	5.81	4.03	2.90	3.50				
Copper (US$/lb)	1.93	4.00	3.90	3.80				
Zinc (US$/lb)	0.75	0.99	0.94	1.10				
Nickel (US$/lb)	7.36	10.38	9.00	8.00				
Gold, London PM Fix (US$/oz)	586	1,569	1,750	1,700				
Pulp (US$/tonne)	694	977	900	975				
Newsprint (US$/tonne)	575	640	655	670				
Lumber (US$/mfbm)	273	255	260	300				

[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	11Q3	11Q4	Latest	
Real GDP (annual rates)	2.5	4.2	1.8		
Current Acc. Bal. (C$B, ar)	-48.3	-49.3	-41.3		
Merch. Trade Bal. (C$B, ar)	1.2	0.7	11.6	25.1	(Jan)
Industrial Production	3.5	3.4	2.9	1.7	(Dec)
Housing Starts (000s)	193	205	199	201	(Feb)
Employment	1.6	1.5	1.2	0.7	(Feb)
Unemployment Rate (%)	7.5	7.3	7.5	7.4	(Feb)
Retail Sales	3.6	4.2	3.5	3.4	(Dec)
Auto Sales (000s)	1587	1604	1596	1546	(Dec)
CPI	2.9	3.0	2.7	2.5	(Jan)
IPPI	4.6	5.4	3.9	-2.3	(Jan)
Pre-tax Corp. Profits	15.0	18.0	13.3		

Mexico	2011	11Q3	11Q4	Latest	
Real GDP	3.9	4.5	3.7		
Current Acc. Bal. (US$B, ar)	-8.8	-13.7	-14.0		
Merch. Trade Bal. (US$B, ar)	-1.2	-15.3	-2.8	-3.4	(Jan)
Industrial Production	3.8	3.5	3.2	2.8	(Dec)
CPI	3.4	3.4	3.5	3.9	(Feb)

Chile	2011	11Q3	11Q4	Latest	
Real GDP		4.8			
Current Acc. Bal. (US$B, ar)		-11.6			
Merch. Trade Bal. (US$B, ar)	10.3	3.6	7.6	7.5	(Feb)
Industrial Production	5.4	2.4	0.5	0.4	(Dec)
CPI	3.3	3.1	4.0	4.4	(Feb)

Germany	2011	11Q3	11Q4	Latest	
Real GDP	3.1	2.7	2.0		
Current Acc. Bal. (US$B, ar)	188.1	167.3	235.5	123.9	(Jan)
Merch. Trade Bal. (US$B, ar)	216.2	224.9	222.8	219.1	(Jan)
Industrial Production	8.0	8.1	3.5	2.1	(Jan)
Unemployment Rate (%)	7.1	7.0	6.9	6.8	(Feb)
CPI	2.3	2.5	2.3	2.3	(Feb)

Euro Zone	2011	11Q3	11Q4	Latest	
Real GDP	1.5	1.3	0.7		
Current Acc. Bal. (US$B, ar)	-44	-7	112	258	(Dec)
Merch. Trade Bal. (US$B, ar)	8.3	17.7	101.9	166.0	(Dec)
Industrial Production	3.6	3.9	-0.2	-1.8	(Dec)
Unemployment Rate (%)	10.1	10.1	10.4	10.6	(Jan)
CPI	2.7	2.7	2.9	2.6	(Jan)

Japan	2011	11Q3	11Q4	Latest	
Real GDP	-0.7	-0.5	-0.6		
Current Acc. Bal. (US$B, ar)	120.2	159.5	52.0	-68.2	(Jan)
Merch. Trade Bal. (US$B, ar)	-33.4	-32.4	-83.3	-95.5	(Jan)
Industrial Production	-3.5	-2.0	-2.3	-0.9	(Jan)
Unemployment Rate (%)	4.6	4.4	4.5	4.6	(Jan)
CPI	-0.3	0.1	-0.3	0.1	(Jan)

China	2011	11Q3	11Q4	Latest	
Real GDP	10.4	9.1	8.9		
Current Acc. Bal. (US$B, ar)	290.0				
Merch. Trade Bal. (US$B, ar)	155.3	250.9	192.9	327.3	(Jan)
Industrial Production	12.8	13.8	12.8	12.8	(Dec)
CPI	4.1	6.1	4.1	3.2	(Feb)

United States	2011	11Q3	11Q4	Latest	
Real GDP (annual rates)	1.7	1.8	3.0		
Current Acc. Bal. (US$B, ar)		-441			
Merch. Trade Bal. (US$B, ar)	-738	-723	-745	-810	(Jan)
Industrial Production	4.2	3.7	3.8	2.8	(Jan)
Housing Starts (millions)	0.61	0.62	0.67	0.70	(Jan)
Employment	1.1	1.2	1.3	1.6	(Feb)
Unemployment Rate (%)	9.0	9.1	8.7	8.3	(Feb)
Retail Sales	7.9	8.3	6.8	5.5	(Jan)
Auto Sales (millions)	12.7	12.4	13.4	15.0	(Feb)
CPI	3.2	3.8	3.3	2.9	(Jan)
PPI	6.0	6.9	5.5	4.1	(Jan)
Pre-tax Corp. Profits		3.7			

Brazil	2011	11Q3	11Q4	Latest	
Real GDP	2.5	2.0	1.2		
Current Acc. Bal. (US$B, ar)	-52.6	-42.6	-63.6		
Merch. Trade Bal. (US$B, ar)	29.8	40.3	27.0	20.6	(Feb)
Industrial Production	0.3	0.1	-2.2	-3.2	(Jan)
CPI	6.8	7.1	6.7	6.6	(Jan)

Italy	2011	11Q3	11Q4	Latest	
Real GDP	0.4	0.3	-0.5		
Current Acc. Bal. (US$B, ar)	-0.07	-0.05	-0.03	0.01	(Dec)
Merch. Trade Bal. (US$B, ar)	-33.9	-18.3	-6.7	22.9	(Dec)
Industrial Production	0.2	-0.3	-3.0	-4.1	(Jan)
CPI	2.8	2.9	3.3	3.4	(Jan)

France	2011	11Q3	11Q4	Latest	
Real GDP	1.7	1.5	1.4		
Current Acc. Bal. (US$B, ar)	-62.2	-48.7	-66.5	-9.6	(Dec)
Merch. Trade Bal. (US$B, ar)	-50.6	-49.5	-44.8	-49.5	(Jan)
Industrial Production	2.4	2.7	0.5	-1.5	(Jan)
Unemployment Rate (%)	9.7	9.7	9.8	10.0	(Jan)
CPI	2.1	2.1	2.4	2.3	(Jan)

United Kingdom	2011	11Q3	11Q4	Latest	
Real GDP	0.8	0.4	0.7		
Current Acc. Bal. (US$B, ar)		-113.3			
Merch. Trade Bal. (US$B, ar)	-159.1	-176.8	-151.5	-133.2	(Dec)
Industrial Production	-1.2	-1.6	-3.0	-3.8	(Jan)
Unemployment Rate (%)		8.2		8.4	(Nov)
CPI	4.5	4.7	4.7	3.6	(Jan)

Australia	2011	11Q3	11Q4	Latest	
Real GDP	2.0	2.6	2.3		
Current Acc. Bal. (US$B, ar)	-33.0	-34.0	-38.0		
Merch. Trade Bal. (US$B, ar)	36.4	42.9	31.4	0.3	(Jan)
Industrial Production	-0.1	0.9	2.1		
Unemployment Rate (%)	5.1	5.2	5.2	5.2	(Feb)
CPI	3.4	3.5	3.1		

South Korea	2011	11Q3	11Q4	Latest	
Real GDP	3.6	3.5	3.4		
Current Acc. Bal. (US$B, ar)	26.5	27.6	46.0	-9.3	(Jan)
Merch. Trade Bal. (US$B, ar)	30.8	25.2	36.6	26.4	(Feb)
Industrial Production	6.9	5.3	5.2	2.7	(Jan)
CPI	4.0	4.3	4.0	3.1	(Feb)

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

Source: Bloomberg, Scotia Economics.

Interest Rates (%, end of period)

Canada	11Q3	11Q4	Mar/02	Mar/09*	United States	11Q3	11Q4	Mar/02	Mar/09*
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	0.75	0.87	0.93	0.89	3-mo. T-bill	0.02	0.01	0.06	0.08
10-yr Gov't Bond	2.16	1.94	1.96	2.02	10-yr Gov't Bond	1.92	1.88	1.97	2.04
30-yr Gov't Bond	2.77	2.49	2.58	2.60	30-yr Gov't Bond	2.91	2.89	3.10	3.20
Prime	3.00	3.00	3.00	3.00	Prime	3.25	3.25	3.25	3.25
FX Reserves (US$B)	63.5	65.7	66.2	(Jan)	FX Reserves (US$B)	137.4	136.9	138.2	(Jan)
Germany					**France**				
3-mo. Interbank	1.51	1.35	0.87	0.81	3-mo. T-bill	0.38	-0.06	0.04	0.07
10-yr Gov't Bond	1.89	1.83	1.80	1.79	10-yr Gov't Bond	2.60	3.15	2.79	2.90
FX Reserves (US$B)	66.9	66.9	67.2	(Jan)	FX Reserves (US$B)	51.8	48.6	50.5	(Jan)
Euro-Zone					**United Kingdom**				
Refinancing Rate	1.50	1.00	1.00	1.00	Repo Rate	0.50	0.50	0.50	0.50
Overnight Rate	1.46	0.63	0.37	0.36	3-mo. T-bill	4.85	4.85	4.85	4.85
FX Reserves (US$B)	310.9	316.7	320.5	(Jan)	10-yr Gov't Bond	2.43	1.98	2.14	2.15
					FX Reserves (US$B)	78.9	79.3	81.1	(Jan)
Japan					**Australia**				
Discount Rate	0.30	0.30	0.30	0.30	Cash Rate	4.75	4.25	4.25	4.25
3-mo. Libor	0.13	0.13	0.13	0.13	10-yr Gov't Bond	4.22	3.67	4.12	4.01
10-yr Gov't Bond	1.03	0.99	0.97	0.99	FX Reserves (US$B)	39.7	42.8	45.3	(Jan)
FX Reserves (US$B)	1160.7	1258.2	1291.7	(Jan)					

Exchange Rates (end of period)

	11Q3	11Q4	Mar/02	Mar/09*		11Q3	11Q4	Mar/02	Mar/09*
USDCAD	1.05	1.02	0.99	0.99	¥/US$	77.06	76.91	81.81	82.52
CADUSD	0.95	0.98	1.01	1.01	US¢/Australian$	96.62	102.09	107.33	105.93
GBPUSD	1.558	1.554	1.584	1.567	Chinese Yuan/US$	6.38	6.30	6.30	6.31
EURUSD	1.339	1.296	1.320	1.310	South Korean Won/US$	1178	1152	1116	1118
JPYEUR	0.97	1.00	0.93	0.92	Mexican Peso/US$	13.897	13.936	12.760	12.624
USDCHF	0.91	0.94	0.91	0.92	Brazilian Real/US$	1.879	1.867	1.730	1.787

Equity Markets (index, end of period)

	11Q3	11Q4	Mar/02	Mar/09*		11Q3	11Q4	Mar/02	Mar/09*
United States (DJIA)	10913	12218	12978	12948	U.K. (FT100)	5128	5572	5911	5895
United States (S&P500)	1131	1258	1370	1373	Germany (Dax)	5502	5898	6921	6905
Canada (S&P/TSX)	11624	11955	12644	12503	France (CAC40)	2982	3160	3501	3504
Mexico (Bolsa)	33503	37078	38327	37900	Japan (Nikkei)	8700	8455	9777	9930
Brazil (Bovespa)	52324	56754	67782	67237	Hong Kong (Hang Seng)	17592	18434	21562	21086
Italy (BCI)	796	806	889	885	South Korea (Composite)	1770	1826	2035	2018

Commodity Prices (end of period)

	11Q3	11Q4	Mar/02	Mar/09*		11Q3	11Q4	Mar/02	Mar/09*
Pulp (US$/tonne)	970	890	870	870	Copper (US$/lb)	3.16	3.34	3.89	3.81
Newsprint (US$/tonne)	640	640	640	640	Zinc (US$/lb)	0.85	0.82	0.95	0.92
Lumber (US$/mfbm)	240	261	277	282	Gold (US$/oz)	1620.00	1531.00	1707.00	1687.50
WTI Oil (US$/bbl)	82.14	99.65	106.70	107.99	Silver (US$/oz)	30.45	28.18	35.21	33.87
Natural Gas (US$/mmbtu)	3.75	3.03	2.48	2.27	CRB (index)	298.15	305.30	321.17	318.14

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

Emerging Markets Strategy

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Scotia Plaza 40 King Street West, 63rd Floor
Toronto, Ontario Canada M5H 1H1
Tel: (416) 866-6253 Fax: (416) 866-2829
Email: scotia.economics@scotiabank.com

For general and publication-related inquiries, contact us by telephone, email and/or fax.