AMERICAS

USD reverses some of its early 2018 weakness amid equity market volatility and rising confidence in Fed policy tightening prospects. CAD and MXN under-perform amid worries about rising US protectionism.

EUROPE

EUR supported by firm growth trends while the GBP's recovery is vulnerable to Brexit disappointment as a workable deal with the EU remains elusive. JPY supported by safe haven demand.

ASIA-PACIFIC

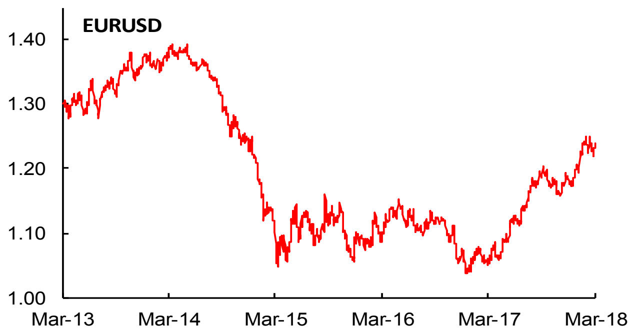
Emerging FX buffeted by market volatility and rising global interest rates as investors redeploy capital. Latam FX remains firm generally but softer commodity prices and local political factors have weighed on near-term performance.

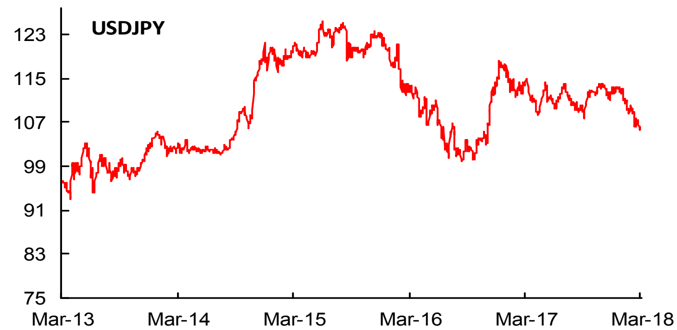
CONTENTS

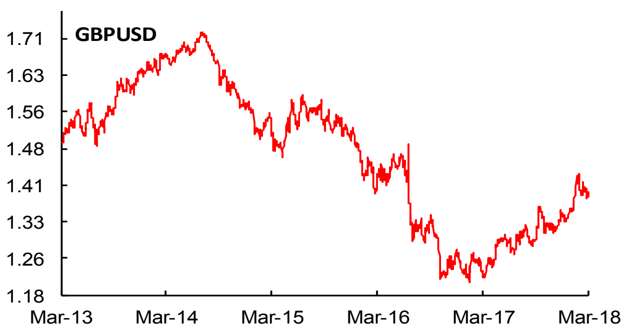
Core Exchange Rates

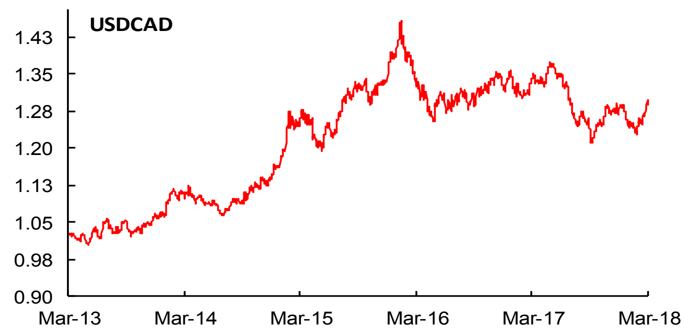
Global Foreign Exchange Outlook

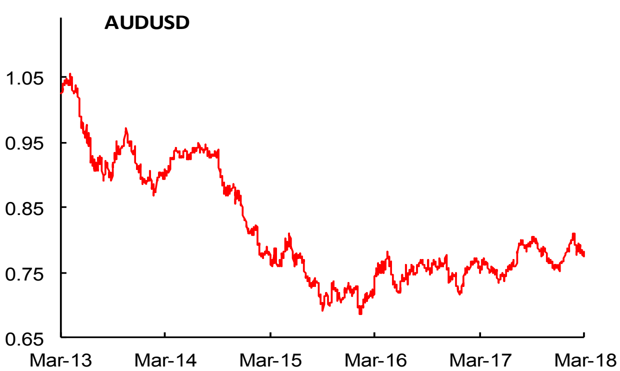
March 6, 2018	Spot	2018f Q1	2018f Q2	2018f Q3	2018f Q4	2019f Q1	2019f Q2	2019f Q3	2019f Q4
EURUSD	1.24	1.18	1.18	1.20	1.20	1.24	1.24	1.28	1.28
USDJPY	106	114	114	115	115	118	118	120	120
GBPUSD	1.39	1.35	1.35	1.37	1.37	1.38	1.38	1.40	1.40
USDCAD	1.29	1.28	1.27	1.26	1.25	1.25	1.22	1.22	1.25
AUDUSD	0.78	0.79	0.79	0.80	0.80	0.81	0.81	0.82	0.82
USDMXN	18.70	18.84	19.11	19.18	19.46	19.56	19.38	19.43	19.71











Market Tone & Fundamental Focus

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The US dollar's (USD) performance in the early part of the year reflected our expectation that it would trade more defensively overall in 2018. More recently, however, USD losses have steadied or reversed, reflecting developments at home as well as abroad that have left the outlook for the next few weeks at least rather unsettled. Over the past week, the White House's decision to implement tariffs on steel and aluminum products has injected further volatility into markets and clouded economic prospects. February had already seen an increase in broader market volatility, triggered by a sharp slide in US equity markets. For now, we think the USD might continue to push higher but we still rather doubt that gains can be sustained in the longer run due to rising fiscal and trade deficits.

We are awaiting full disclosure of President Trump's tariffs before deciding what, if anything, they mean for our economic and currency forecasts. Our basic premise on the FX outlook—that the longer term trend in the USD is poised to weaken—remains intact at this point. But there are divergent opinions on what the imposition of tariffs might mean for the USD. On the one hand, higher prices at home might lead to a more aggressive Fed and a stronger currency. On the other, tariffs may slow growth, prompt job losses and weigh on the USD. The latter case was the experience of the early 2000s when President GW Bush introduced tariffs on steel imports. The USD fell steadily, and quite sharply, overall while they were in place. We doubt a protectionist White House would welcome or want a stronger USD as part of its trade equation.

Beyond these immediate considerations, the USD has been finding support from signs of better than expected growth and perhaps a slightly more hawkish Fed that may be emerging under the new leadership of Chairman Powell. His congressional testimony suggested greater confidence in the economic outlook and pushed markets to start considering the risk of the Fed raising rates more quickly this year.

The Canadian dollar (CAD) and the Mexican peso (MXN) have responded especially poorly to the announcement of the US trade action. The Trump administration's use of tariffs as leverage on Ottawa and Mexico City in NAFTA discussions raises the risk of even more protracted talks on renewing the trade agreement—or worse. Broadly, protectionism is obviously bad news for prospects in both economies—and for both currencies. Just how bad remains to be seen. In Canada, markets had already started to reel back modest expectations for Bank of Canada tightening amid a sharper than expected slowdown in Canadian growth at the end of last year. In Mexico, slower growth, steadier inflation and NAFTA doubts suggest less upward pressure on Banxico policy. For Mexico, investors also have to keep a close eye on the political jockeying for position ahead of the July presidential election.

Among the major currencies, equity market volatility has provided (refuge-related) support for the Japanese yen (JPY) over the past month while stuttering Brexit talks and rising protectionist sentiment in the US are leaving the UK looking somewhat isolated and the pound (GBP) exposed to renewed weakness. The euro (EUR) has been stoic amid the volatility. The Eurozone economy remains resilient but price pressures are soft still, precluding any major adjustment in the European Central Bank's policy settings. The EU has promised swift, targeted retaliatory action in response to US tariffs which has alerted investors to the risk of an escalation of global beggar-thy-neighbour policies. We remain somewhat constructive on the outlook for the EUR at this point, given strong domestic growth trends and we continue to expect the GBP to under-perform, due to Brexit risks. Rising market volatility and heightened global risks suggest there are downside risks to our USDJPY forecast in the next few months.

In the emerging market space, a combination of rising US yields and heightened market volatility has provided significant headwinds for the emerging market FX space broadly. The South African rand has risen modestly over the past month on improving domestic politics while the Korean won has steadied as geo-political tensions eased during the successful winter Olympic Games. Latam currencies are mostly flat over the past few weeks, although many remain relatively firm overall on the year. Moderating commodity prices have dampened the Chilean and Colombian pesos' performances. The Peruvian sol remains choppy, pivoting around its 200-day MA in volatile fashion.

Most other developing market currencies are steady to lower against the USD over the past month. Institute of International Finance data for February reflected the first net, non-resident outflow from emerging market stocks and bonds since November 2016, with outflows concentrated in emerging Asia. This may reflect the equity-centric nature of market volatility and the concentration of foreign investments in local stocks, rather than fixed income. However, rising rates and heightened volatility suggest that investors may become more discerning about investment decisions going forward; highly leveraged and the more highly-indebted countries may have to compete harder for foreign investors' capital.

Canada

Currency Outlook

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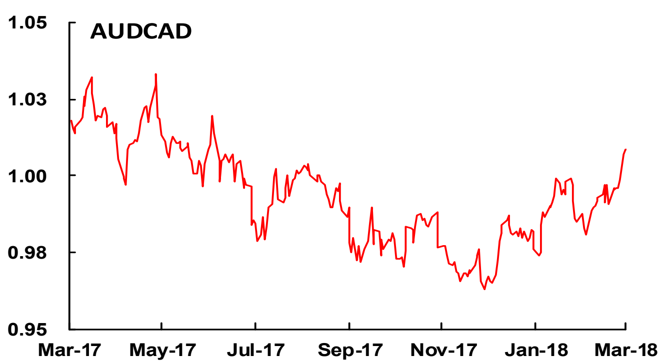
The CAD has traded poorly so far this year, delivering the worst returns of any G-10 currency in year-to-date terms versus the USD. The CAD has sagged amid somewhat softer crude oil prices (and very soft prices for Canadian heavy crude) even as other Canada-relevant commodities (nickel, lumber) have strengthened materially. Higher US interest rates have driven US-Canada short-term spreads to around 50bps, the biggest yield advantage since mid-2017 when USDCAD was trading around 1.35. Most recently, the threat of US trade protectionism has weighed more obviously on CAD sentiment.

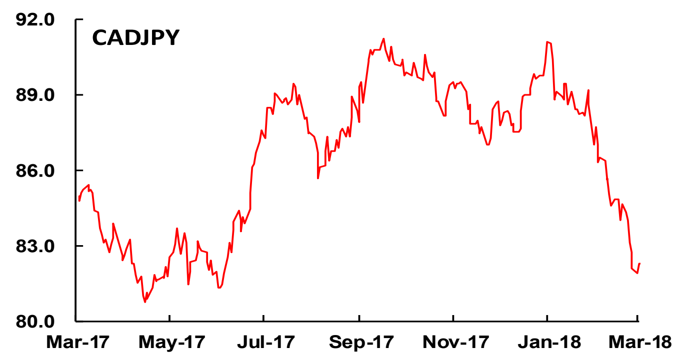
We expect the Bank of Canada to nudge rates gently higher this year and broadly expect strengthening global growth to help underpin commodity prices over the balance of this year. But a modest bump in domestic interest rates (versus a potentially more aggressive Fed) and a somewhat better outlook for raw material prices might not cut it for the CAD in the short-term.

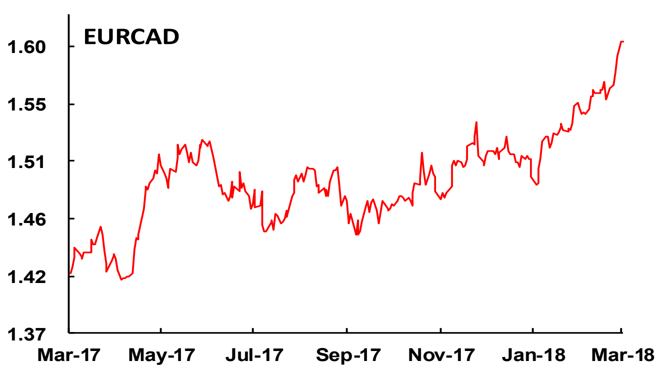
The USD has a window to strengthen a little more in the next few weeks as positioning (speculative investors retain a net long CAD position) and technical signals (USDCAD is trading above its 200-day moving average) combine to put the CAD under pressure. Having moved through the late 2017 high at 1.2915 (where we had expected stronger resistance), the USD may appreciate towards 1.31/1.32 in the next month. We remain bearish on USDCAD in the longer run but we do concede that the bar to the CAD recovering looks somewhat higher now than just a few weeks ago and clear and obvious trade friction may well result in a downgrade of our CAD forecast.

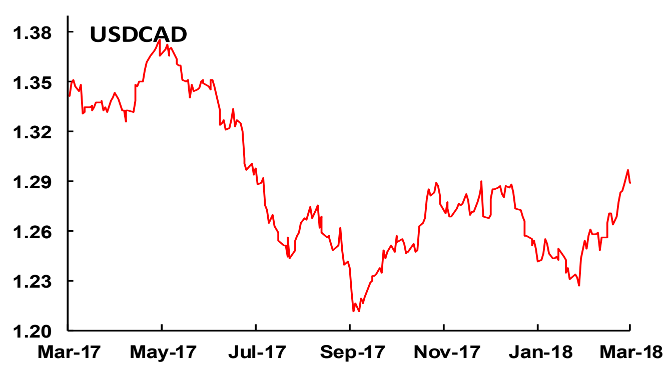
Canadian Dollar Cross-Currency Trends

FX Rate	Spot 6-Mar	18Q1f	18Q2f	18Q3f	18Q4f	19Q1f	19Q2f	19Q3f	19Q4f
AUDCAD	1.01	1.01	1.00	1.01	1.00	1.01	0.99	1.00	1.03
CADJPY	82.3	89.1	89.8	91.3	92.0	94.4	96.7	98.4	96.0
EURCAD	1.60	1.51	1.50	1.51	1.50	1.55	1.51	1.56	1.60
USDCAD	1.29	1.28	1.27	1.26	1.25	1.25	1.22	1.22	1.25









United States and Canada

Fundamental Commentary

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UNITED STATES — The overall pace of US growth slowed in Q4 2017, but the economy remains on track to record a stronger annual expansion in 2018 compared with 2017. Real GDP rose by 2.5% q/q annualized in Q4, down from 3.2% in Q3 as inventory replenishment slowed and stronger growth in household, business, and government spending underpinned a boost in imports and pushed the net trade balance to its lowest level in a decade. Strong labour markets, rising wages, wealth effects from equity markets, and the anticipated USD 300 bn boost in federal spending should together drive a further imbalance between aggregate consumption over saving in the US economy and push the trade deficit wider in coming quarters. Strengthening macro fundamentals across households, industrial sectors, and services point to a further pick-up in residential and business investment during 2018. Stronger capital spending combined with solid global growth and increased domestic fiscal stimulus have led us to mark up again our projections for US GDP growth from 2.5% to 2.7% in 2018 and from 1.8% to 2.2% in 2019. Core PCE inflation is stable at 1.5% y/y, but is expected to accelerate since real GDP growth is set to remain above our 1.8% estimate of potential. A move by the White House to implement possible tariffs on steel and aluminum would add to inflationary pressures. While the possibility of such tariffs has clearly further complicated the ongoing efforts to renegotiate NAFTA, we continue to expect the accord will survive—either in its current form or through a conclusion of the trilateral talks, in 2019 or beyond.

CANADA — The Canadian economy is settling down to a more sustainable path. Following a surge in the first half of 2017, real GDP growth slowed to an average annual rate of 1.6% in the latter half of the year, in line with the economy's potential. Household spending is showing signs of moderating, but is expected to remain relatively healthy, underpinned by low unemployment and strengthening wage gains. New regulatory measures that came into effect January 1st and moderately higher interest rates are expected to cool housing activity. Service-sector activity remains brisk across a range of industries. Strong corporate profit growth and rising operating rates have spurred a revival in business investment. However, investment intentions overall remain mixed, reflecting trade-related uncertainties and weak energy-related spending plans. Exports continue to disappoint, as shipment volumes have struggled to regain any positive momentum over the past year. Strengthening US and global demand should lead to some export improvement this year, though competitiveness pressures and heightened US protectionism remain notable downside risks. We modelled here the possible impact of a US withdrawal from NAFTA and a move to either Most-Favoured Nations (MFN) tariffs or a global trade war. Infrastructure spending is set to ramp up. Inflation has trended higher in recent months. The average of the BoC's preferred measures of core inflation rose to 1.8% y/y in January, up from a low of 1.3% in May. Wage and price increases are expected to continue nudging it higher, as would additional tariffs, if they materialize.

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Monetary Policy Commentary

UNITED STATES — Scotiabank Economics continues to expect another ¼ point hike to the present fed funds target range of 1.25–1.5% at the March 21st FOMC meeting followed by two more hikes this year and two in 2019. Recent growth and inflation signals support staying on track with forecast hikes especially after controlling for possible weather effects on activity readings. The risk of an additional rate hike beyond what we forecast for this year is supported by fiscal policy developments including tax reforms and a large spending increase resulting from the two-year funding and spending agreement. This is occurring while the US economy slips into slight excess demand and may motivate FOMC members to raise their rate forecasts. This rate risk is nevertheless countered by concerns over global protectionism emanating from Washington. This latter set of risks is difficult to judge at this point and our assessment will evolve over the near term. At this time our view does not materially differ from market pricing through fed fund futures after markets have come around to our views on inflation risk that were expressed last Fall. The 2s10s slope of the Treasury curve has been little changed this year and our view remains that the bigger risk is skewed toward curve flattening over the forecast horizon.

CANADA — Scotiabank Economics continues to expect the BoC to hold its policy rate unchanged at 1.25% at the March 2018 meeting. Thereafter we presently forecast two rate hikes over 2018. Many of the fundamentals-based criteria for continued BoC hikes remain intact as spare capacity has been eliminated while the average of the three central tendency core inflation measures approaches the BoC's 2% target. Trade policy uncertainty hangs over the economy. At this point, Canada has yet to experience a negative trade shock while small positive effects of US fiscal stimulus upon export demand are likely. The net effects on GDP growth of what is at risk through the steel and aluminum skirmish are tiny as long as possible retaliatory moves do not extend collateral damage across other industries. We are monitoring this risk and do not wish to over-react. Our base case assumption remains that NAFTA negotiations will extend beyond this year and that being at capacity still means businesses need to invest and hire and monetary policy needs to be conducted appropriately.

G10

Currency Outlook

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EUROZONE — EUR has clearly defined its medium-term range with a pair of outside reversal signals delivered on February 16th (bearish, from multi-year high above 1.2550) and March 1st (bullish, from multi-week low around 1.2150). The near-term outlook appears neutral as market participants defer expectations for ECB policy normalization, however EUR's longer-term prospects remain constructive as market participants look to Fed-ECB convergence and focus on the US's deteriorating fiscal and current account balances ('twin deficits'). We hold a Q4 2018 EUR target of 1.20 and a Q4 2019 forecast of 1.28.

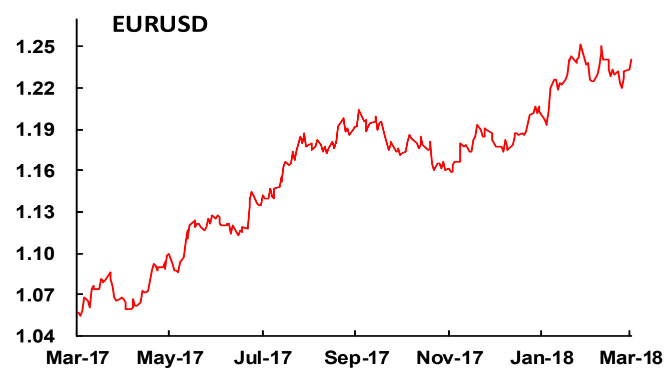
UNITED KINGDOM — GBP remains vulnerable to headline risk surrounding Brexit. PM May's latest speech has offered modest support, allowing for a stabilization vs. both the USD and EUR. Sentiment and speculative positioning remain close to neutral however, as market participants appear unwilling to make any sizeable directional bets. We are longer-term GBP bulls on the basis of both fundamentals and valuation. We hold a Q4 2018 GBP target of 1.37 and a Q4 2019 forecast of 1.40.

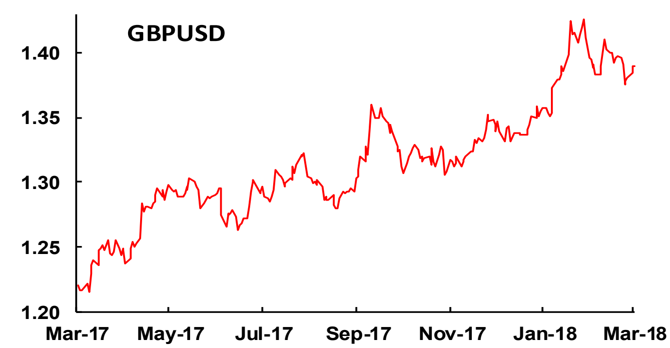
JAPAN — JPY has outperformed on a year-to-date basis, rallying on the back of both fundamentals and sentiment as market participants have reacted to renewed risk aversion and shifted their expectations for BoJ policy. Extended bearish positioning leaves JPY vulnerable to further upside. We acknowledge downside risk to our Q4 2018 USDJPY target of 115.

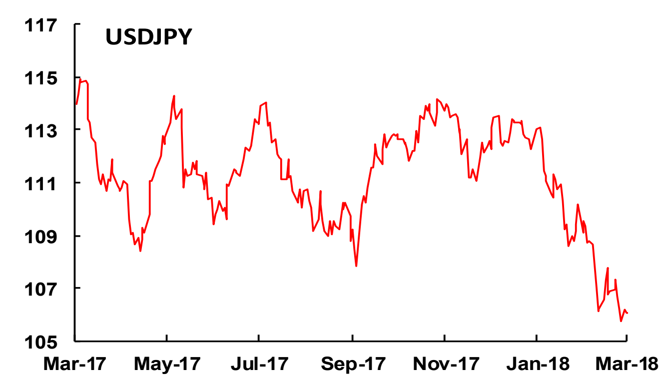
AUSTRALIA — AUD has entered March on the defensive, testing fresh 2018 lows under 0.7800. Supportive terms of trade have provided an important offset to the deterioration in the outlook for relative central bank policy. Speculative positioning is close to neutral following a sizeable liquidation of risk to both sides. We are modestly bullish AUD and hold a Q4 2018 target of 0.80 with a Q4 2019 forecast of 0.82.

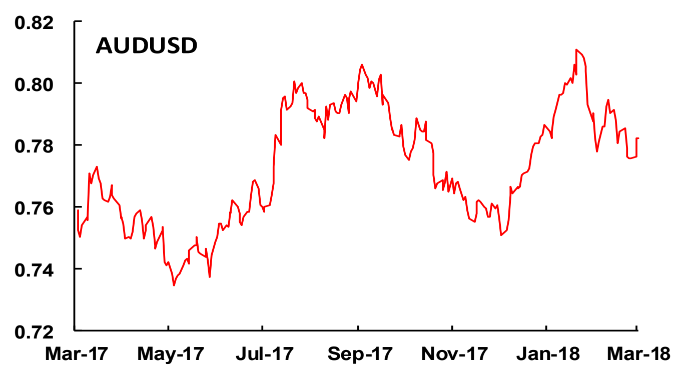
Currency Trends

FX Rate	Spot 6-Mar	18Q1f	18Q2f	18Q3f	18Q4f	19Q1f	19Q2f	19Q3f	19Q4f
EURUSD	1.24	1.18	1.18	1.20	1.20	1.24	1.24	1.28	1.28
GBPUSD	1.39	1.35	1.35	1.37	1.37	1.38	1.38	1.40	1.40
USDJPY	106	114	114	115	115	118	118	120	120
AUDUSD	0.73	0.79	0.79	0.80	0.80	0.81	0.81	0.82	0.82









G10
Fundamental Commentary

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EUROZONE — The outlook for Eurozone GDP growth is still very positive, despite some of the upstream survey indicators coming off the boil. GDP growth approaching 3% y/y around the middle of the year. The buoyancy is likely to be broad-based. Investment spending looks particularly promising. In itself this is encouraging that the expansion should be enduring. Upbeat consumer confidence points to robust household consumption. Overall, we expect GDP to expand by 2¾% this year and a little lower in 2019. Headline inflation is currently slowing towards the psychological 1% y/y threshold, largely due to base effects. Meanwhile, core inflation has been anchored around the 1% mark. Narrowing spare capacity and solid growth should ultimately help underlying inflation to drift higher towards the end of the year, albeit gradually. We expect the ECB to see the current asset purchase programme through to completion in September of this year. At that point, the pace of core inflation will dictate whether the programme terminates there and then, or whether further purchases are made at a reduced rate. Given our inflation outlook, the latter seems slightly more plausible. Thereafter, although speculation is likely to build, we do not expect the ECB to deliver a rate hike at least until late-2019 as underlying inflation remains contained and residual spare capacity is eroded further.

UNITED KINGDOM — The market has fallen into line with the Scotiabank view that the BoE will hike Bank Rate at the May MPC meeting, somewhat sooner than the November 2018 assumption which was the consensus late last year. The BoE's tone has turned more hawkish, particularly in light of signs of accelerating wage inflation, which in turn it is hoped will help to push domestically generated inflation higher. More robust than expected GDP growth at the end of 2017 has also helped, along with the backdrop of strong global growth—particularly in the Eurozone. In light of the strong end to 2017, we now expect GDP growth of 1¾% this year, rising to around 2% in 2019. With the unemployment rate at a 40-year low and growth expanding faster than potential, spare capacity should be eradicated very soon—keeping the MPC on track to hike rates for a second time this year—most likely in November. The main reason to expect above trend GDP growth in 2018 is an improving trajectory for household consumption growth. In turn this should be a reflection of rising real incomes as wage inflation accelerates and CPI inflation falls—essentially the reverse of 2017. We expect inflation to decelerate more abruptly than the market assumes (although the latter has come down a little). In turn, this is likely to be driven by base effects associated with exchange rate sensitive components. As such, the MPC can look through such a move, especially if domestically generated inflation and wages are stable/rising.

JAPAN — The Bank of Japan (BoJ) will likely leave its monetary policy stance unchanged in the foreseeable future, given the central bank's firm commitment to reaching the 2% y/y inflation target. The nation's CPI, excluding fresh food and fuel, rose by only 0.4% y/y in January, highlighting the absence of demand-driven inflation in Japan. At the headline level, prices rose by 1.4% y/y in January. We do not expect the BoJ's 2% y/y inflation target to be met in 2018 unless wage gains—or global energy prices—pick up in a notable fashion. The planned increase in the consumption tax rate (from 8% to 10%) will temporarily take headline inflation above the 2% mark in late 2019. BoJ Governor Haruhiko Kuroda's reappointment for a second five-year term in February implies that the BoJ will continue to implement its ultra-accommodative monetary policy for an extended period of time. Japan's economic growth will remain strong by historical standards despite the fact that preliminary estimates for the fourth quarter momentum were weaker than expected. Real GDP grew by 0.1% q/q (1.5% y/y) in the October-December period. Consumer spending was a key driver of activity. We forecast Japan's real GDP to expand by 1.3% in 2018. In 2019, output growth is set to decelerate to a more sustainable level of 0.9% y/y reflecting cyclical factors and the scheduled consumption tax rate increase in October 2019.

AUSTRALIA — Australia's monetary conditions will remain accommodative over the coming quarters. Following the Reserve Bank of Australia's (RBA) March 6th monetary policy meeting, the Cash Rate Target was left at 1.50%. We maintain our forecast that the RBA will likely begin a cautious monetary normalization phase in the final quarter of 2018 on the back of strengthening wage pressures and demand-driven inflation. Headline inflation picked up to 1.9% y/y in the fourth quarter from 1.8% in the third quarter. We expect a slight acceleration in inflation over the coming quarters, yet the inflation rate will likely hover below the mid-point of the RBA's 2–3% target range through 2018. Price gains will likely intensify in 2019, reaching 2⅔% y/y by the end of the year. Australia's economic outlook for 2018 is favourable. Business and consumer confidence is solid, pointing to continued employment gains, business investment, and consumer spending. Public infrastructure projects and higher export volumes provide additional support to the economy. We estimate that Australia's real GDP will grow by 2.7% in 2018 following a 2⅓% y/y gain in 2017. Australian household spending prospects will be heavily impacted by labour market developments. In 2017, the Australian economy created 34,000 new jobs every month on average, of which 75% were full-time positions. Continued strong employment gains would eventually feed higher wage inflation, yet Australia's persistent underemployment will cushion the pressure on wages somewhat. In the fourth quarter of 2017, wages rose by 2.1% y/y in nominal terms, barely exceeding the nation's inflation rate.

China, India, Brazil

Currency Outlook

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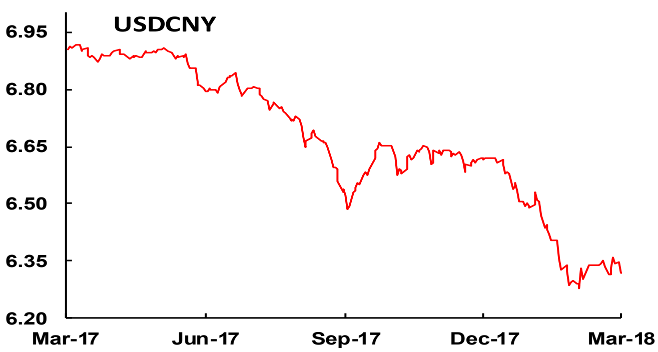
CHINA — China will push forward with economic and financial reforms under the new Politburo and Cabinet. The ruling party has proposed scrapping term limits for the country's president and vice president. We expect China to continue adopting a proactive fiscal policy and a prudent monetary policy to fulfill its economic and social development goals for 2018. We stay cautious on rising inflation pressure in the US and Fed Chairman Powell's hawkish tone. USDCNY is expected to trade in a range of 6.20-6.40 in March.

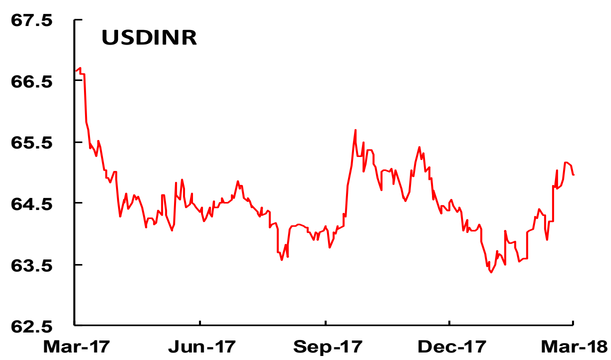
INDIA — India's trade deficit shot up to a 56-month high of USD 16.3bn in January as imports of gold and crude oil surged, which could worsen the nation's current account deficit. We closed our short USDINR position on concern over widening trade deficit and the PNB fraud, but look to sell the pair on rallies amid India's economic recovery. The RBI is expected to review the 5% cap on foreign investment in INR-denominated notes in March or April.

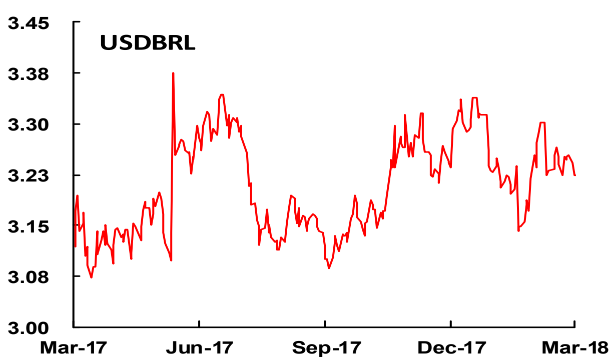
BRAZIL — Outside of a violent 1-day move back in May-2017, USDBRL has traded in a wide 3.06–3.34 range since the end of 2016. For the coming few months, we expect range trading to continue. Fundamentally, we see the BRL as at best fairly valued, but for now, a benign external environment for commodity producers should keep the BRL steady until the positive global growth story turns, or the elections derail sentiment.

Currency Trends

FX Rate	Spot 6-Mar	18Q1f	18Q2f	18Q3f	18Q4f	19Q1f	19Q2f	19Q3f	19Q4f
USDCNY	6.32	6.40	6.40	6.30	6.30	6.20	6.20	6.10	6.10
USDINR	65.0	64.5	64.5	64.0	64.0	63.5	63.5	63.0	63.0
USDBRL	3.22	3.25	3.15	3.25	3.25	3.30	3.30	3.35	3.35







China, India, Brazil

Fundamental Commentary

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CHINA — China's President Xi Jinping will be able to stay in power indefinitely following the country's policymakers' decision to alter the constitution and remove the two-term limits of the president and vice president. The National People's Congress—which runs from March 5th until March 20th—set the 2018 real GDP growth target at 6.5% y/y; while the goal is the same as last year, authorities omitted the 2017 objective of exceeding the target if possible. Chinese policymakers will continue to focus on gradually deleveraging the domestic economy, allowed by a favourable global economic environment that is supporting China's external sector and economic growth. Indeed, the country's credit impulse—the change in new credit issued as % of GDP—has been negative in recent months, implying that the nation's private demand growth (i.e. consumer spending and investment) will slow over the coming quarters. In a similar fashion, year-over-year growth in total aggregate financing has been in negative territory in the past three months. We welcome the government's deleveraging efforts as slower credit expansion will lead to more sustainable and higher-quality economic growth. We expect China's real GDP to advance by 6.5% y/y in 2018 followed by a 6.9% expansion in 2017. China's consumer price inflation slowed to 1.5% y/y in January from 1.8% at end-2017 on the back of lower food prices and a high base in January 2017 that reflects the changing timing of the Chinese New Year. We expect price gains to return towards the 2% mark in the near future. The People's Bank of China (PBoC) will likely leave the official benchmark one-year loan and deposit rates unchanged in 2018 (at 4.35% and 1.50%, respectively), though the central bank is expected to continue to raise the 7-day reverse repo rate—the PBoC's de-facto policy rate—cautiously over the coming months, most likely in March following the expected interest rate hike by the US Federal Reserve.

INDIA — The Indian economy is on the mend following disruptive reform implementations over the past year. Real GDP grew by 7.2% y/y in the fourth quarter of 2017 following a 6.5% increase in the third quarter. Domestic demand was the key driven of activity; a pick-up in fixed investment growth is an encouraging development. We forecast India's real GDP to expand by 7½% y/y over the next two years. The Reserve Bank of India (RBI) held a monetary policy meeting on February 7th and left the benchmark repurchase rate unchanged at 6.0%. One out of the six Monetary Policy Committee members voted for a 25 basis point rate hike, marking a change in the RBI's tone; at the previous meeting in December, one member had voted for a cut while no one had proposed a hike. We expect the RBI's monetary policy stance to remain unchanged until the first quarter of 2019 when a cautious monetary tightening cycle will likely begin. We estimate that India's inflation will pick up slightly over the coming months from the January reading of 5.1% y/y but will remain within the RBI's medium-term target of 4% ±2% y/y. India's Union Budget for Fiscal Year 2018–19 (April-March) was presented by Finance Minister Arun Jaitley on February 1st. According to Jaitley, India's central government deficit will average 3.5% of GDP this fiscal year, thereby missing the Budget 2017 target of 3.2%. The shortfall in FY2018–19 is projected to narrow to 3.3% of GDP vs. an earlier target of 3.0%. The 2018 Budget is a careful balancing act between stimulating domestic demand, particularly the rural economy, and maintaining investor confidence on India's fiscal sustainability. We assess that the government gave priority to the former, which may reflect the fact that this is the last full budget of Prime Minister Narendra Modi's government before the general elections in 2019. Even though the government remains committed to gradual fiscal consolidation, moderate fiscal slippage is evident. Given that deficit targets were relaxed last year as well, India's pledge to reach fiscal sustainability is questionable. Public spending in 2018–19 will be focused on the rural economy, infrastructure, as well as on education, health care, and social protection.

BRAZIL — Over recent days, some concerns over the impact of President Trump's steel & aluminum tariffs on Brazilian exports to the US have added a little to the pressure on the Brazilian real, but only marginally. Our sense is that unless the elections look likely to put a populist back in power, there is no clear catalyst from within that could push USDBRL to weaken materially. However, higher core country interest rates, or weaker commodity prices are longer term risks to bear in mind (we don't see them being relevant factors for the coming few months). On the election front, it's still not even clear who the main contenders for the October Presidential elections will be, but local media is increasingly talking about Sao Paulo's Mayor Alkmin, facing off against Finance Minister Meirelles. It's not yet clear who would represent the PT if Lula cannot run. On the right of the political spectrum, Jair Bolsonaro continues to lead the polls if we exclude Lula, with the latest poll reported by Estado suggesting Bolsonaro leads with 24% (58% rejection rate), followed by Alkmin with 20% (68% rejection rate), while Meirelles only has 5% approval. For now, markets have not reacted to either Brazil's poor fiscal results, or the failed reform push, likely due to a wait and see approach until we see if the elections leave a reformist with a strong mandate in place. If the elections fail to leave a reformist with enough legislative support in power, the BRL's honeymoon could end.

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Pacific Alliance

Currency Outlook

MEXICO — Mexican peso is expected to remain sensitive to the many factors affecting the global environment, such as the normalization process of the monetary policy in the US and other countries, the NAFTA renegotiation process, the possible implications of the US tax reform, some geopolitical tensions and the possible implementation of protectionist policies in the US. In the domestic front, the electoral process is expected to produce only a modest pressure on the MXN.

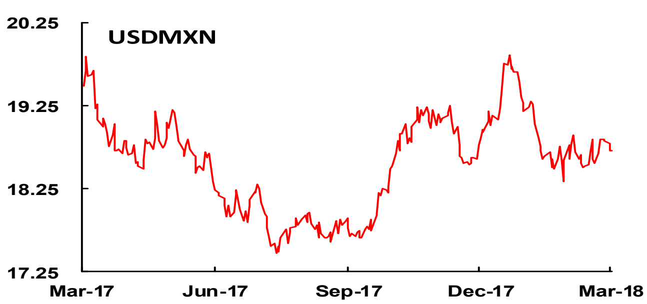
COLOMBIA — January finally saw the benign oil price environment benefiting the Colombia peso (COP), due to a more favorable outlook for external accounts, growth, and fiscal numbers. However, after seeing USDCOP drop to 2760 late in January (from over 3050 back in November), the peso's positive momentum stalled, and it's now back trading sideways. Throughout February, USDCOP lost some ground and mostly traded in a 2800–2900 range, with a couple of spikes nearer to 2950. For now, the risk of more rate cuts by BanRep, alongside the looming elections, should keep USDCOP's downside contained.

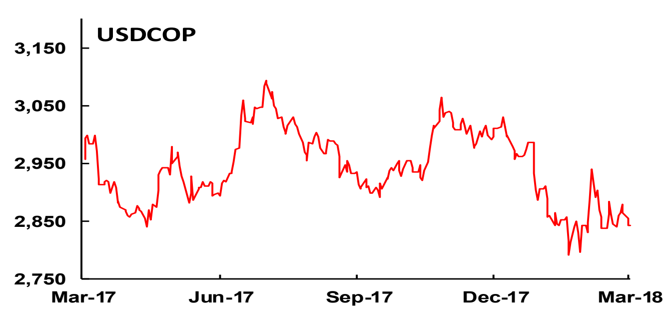
CHILE — The exchange rate in Chile (USDCLP) is being dominated by two kinds of forces. In the very short term, the classical ones: USD international value, copper price, global risk aversion and, to a lesser extent, interest rates expectations. But forces coming from the expectation of foreign currency inflows to finance new investment projects have been increasing, dragging down the exchange rate. Our base case is a year-end price not very different from the spot level (USDCLP 595), with very wide trading range, particularly over the first half of the year, but trend risk is downward biased.

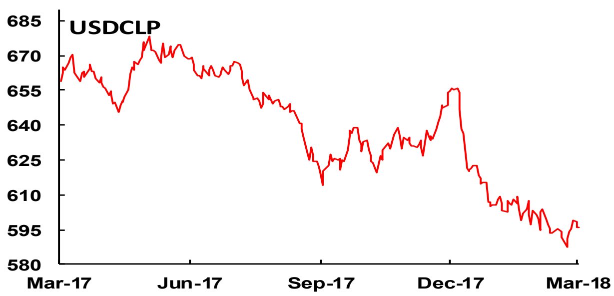
PERU — After fluctuating between 3.20–3.23 through most of January and early February, the PEN has ranged between 3.22–3.27 more recently. The higher range is in line with the mild correction in relevant metal prices, and with regional currencies. The PEN could have weakened even more if not for two factors. The first, and fundamentally most important, was the heavy volume of USD sales by mining companies to pay domestic income taxes. The second was the signal given by the Central Bank in providing USD liquidity at 3.27. Fundamentals continue to favor a mildly stronger PEN going forward, although this will depend also on the evolution of the USD in world and regional markets.

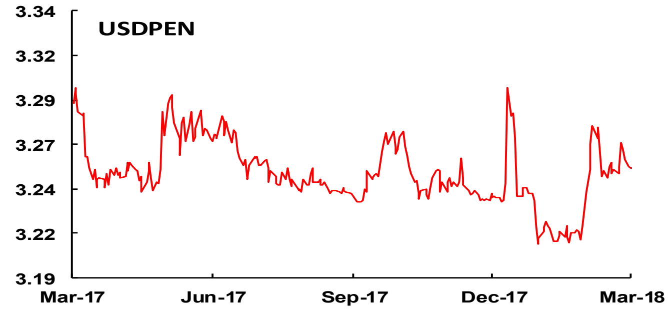
Currency Trends

FX Rate	Spot 6-Mar	18Q1f	18Q2f	18Q3f	18Q4f	19Q1f	19Q2f	19Q3f	19Q4f
USDMXN	18.70	18.84	19.11	19.18	19.46	19.56	19.38	19.43	19.71
USDCOP	2843	2800	2900	2900	2900	2950	2950	3000	3050
USDCLP	596	597	598	597	596	593	591	588	586
USDPEN	3.25	3.22	3.19	3.20	3.18	3.18	3.14	3.15	3.12









Pacific Alliance
Fundamental Commentary

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MEXICO — After a year of sub-par growth in 2017, when a considerable portion of the weakness observed in 2017 could be explained by a dramatic drop in oil extraction due to PEMEX overhaul and a material contraction in civil engineering construction, due to a massive cut in public investment; we are expecting a mild improvement in economic expansion during 2018, although there is a lot of uncertainty around the macroeconomic scenario. Real GDP is expected to grow 2.4% y/y as the exports dynamism gains some traction and the private consumption maintains a healthy pace, driven by positive trends in job creation and transfers from abroad. Total investment is expected to be weak (+1.3% real), affected by the high uncertainty of a less favorable global financial environment and the natural unrest that the coming electoral process is producing. Inflation is expected to keep descending as the shocks of 2017 are absorbed, ending the year close to 4.3%. Banco de Mexico is expected to tighten the monetary stance at least one more time in the reminder of the year, but more interest rate hikes could be necessary if inflation remains stubbornly high or there is a deterioration of global conditions, for instance if the Federal Reserve accelerate the pace of normalization of its monetary policy. These forecasts could change significantly depending on factors such as NAFTA renegotiations, some US policy surprises and the Mexican electoral result.

COLOMBIA — With Presidential elections two months away, the electoral picture is starting to take shape, with the latest poll by Ecoanalitica putting Former President Uribe's candidate Ivan Duque at the front of electoral polls (23.6%), closely followed by Gustavo Petro (left leaning former Mayor of Bogota), while centrists Sergio Fajardo and German Vargas Lleras appear to have fallen behind (8% and 6% support respectively). Given the large share of still un-accounted for votes, the election appears to remain undecided, but it appears that we will end up with a left (Petro ?) vs right (Duque ?) race. At least for now, the two more centrist candidates appear to have fallen behind. On the macro standpoint, as we went to print we still did not know what the CPI number for February said (consensus called for 3.42%), but we do know that members of BanRep's board said that inflation sub 3% would put cuts back on the board's menu. Our sense from recent communication from the Central Bank, is that they see the easing cycle as being on hold, rather than done. We would caution that BanRep has surprised often in the past few months, and it seems that whenever they have seen easing likely justified in the future, they have tended to ease sooner rather than later. With recent data on industrial production (-0.8% in December) and retail sales (-3.8% in December) suggesting weakness, we think near term rate cuts are possible.

CHILE — The current year started with upbeat information for the Chilean economy. Most of the sectorial indices were better than expected in January, while partial foreign trade data for February are also being positive. It means that upward bias for our economic growth forecast for the current year (3.1%) strengthened with the latest dataflow. Putting aside that annual changes in the quarter February-March will be helped by weaker comparison bases (due to a strike in the biggest mining company last year), there are some hints that an intermediate slowing for the rest of the first half of the year might be even milder than originally expected. The President-elect will take office on March 11th, unveiling most of his team; in addition, the guidelines of the economic emphasis will be focused on increasing growth, unleashing private investment forces and improving fiscal finances, which suggests that on the demand side most of news will be expected to be about investment, at least in the first year. Conditions to get it seem supportive: terms of trade moderately improving, calming political environment, soaring business confidence. Many years of low economic growth likely accumulated pent up demand in several areas of the economy. Main risk scenarios are related with politics and terms of trade, but their probability decreased. Accordingly, we expect a moderate normalization of annual inflation (we project 2.8%) and limited (preemptive) actions of the Central Bank till midyear (three hikes, 25bp each, to leave the MPR at 3.25% by December). Though the plunge of the exchange rate may delay both, there is enough historical evidence that the slower but more powerful force of activity will weigh more on monetary decisions, than an exchange rate performance whose pass-through coefficient could be lower this time.

PERU — GDP growth for 4Q17 came in at 2.2% y/y, below expectations of 3.0%. However, the reason was entirely the lack of the seasonal fishing/fishmeal campaign. All components of domestic demand growth were fairly robust, with domestic demand itself coming in at 4.3%. Particularly encouraging was the 3.2% growth in private investment, given the political noise during the quarter. The noise has, if anything, become even more deafening in 2018, with Lava Jato and improper campaign financing affecting nearly all major political leaders, as well as other, separate, corruption charges involving private sector construction companies. There is, actual, not much evidence that this environment is hitting the economy as strongly as one might fear, but it may just be too early for the impact to be fully manifest. Domestic cement consumption, for example, rose 6.6% y/y, in January, which is a positive sign indicative that government investment is performing moderately well. We have yet to modify our 3.7% GDP growth estimate for the year until more conclusive information is available, but the risk is to the downside. Meanwhile, inflation, 1.2% yearly in February, continues to race to the bottom of the Central Bank (CB) target range (1.0%). What's more, given the El Niño linked spike in monthly inflation in March 2017, the yearly figure is likely to drop to close to nil next month. Given this, we see the CB lowering its reference rate (currently at 3.0%) as a distinct possibility. However, it is not a sure thing, as the drop in inflation is temporary, and the CB may have concerns regarding the FX and money market implications of lowering domestic rates when the US Fed is raising rates at a more accelerated pace.

Developing Economies
Currency Outlook

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SOUTH KOREA — The BoK will stay on hold at least until May. Governor Lee Ju-yeol told reporters that the central bank may have to consider a rate hike if the economy grows at around 3% and global yields rise. We stay watching geopolitical situation after the Winter Olympics. The White House said any talks with North Korea must lead to an end to its nuclear program. USDKRW is likely to trade in a range of 1,060-1,100 prior to the March FOMC meeting.

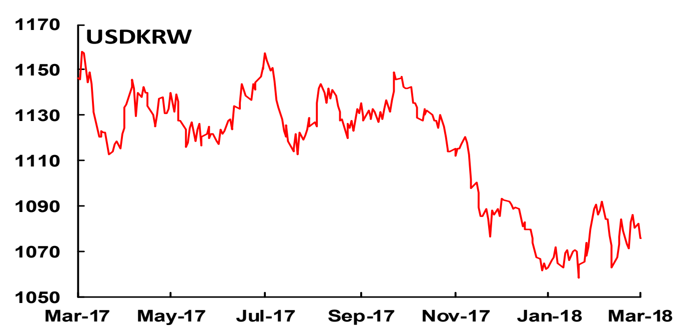
THAILAND — The BoT continues to closely monitor the THB exchange rate and expects the nation's CPI inflation to return to the target of 2.5%±1.5% in Q2. BoT Governor Veerathai has denied an immediate need to follow global policy tightening with a monetary policy depending mainly on local factors. We remain bullish on the THB given the nation's sound fundamentals including large current account surplus. USDTHB is likely to fluctuate in a range of 31.0-32.0 in March.

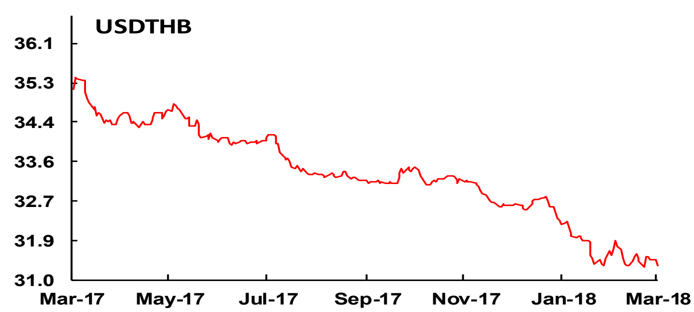
TAIWAN — We expect the CBC to maintain its policy stance under the new CBC Governor Yang Chin-long. Taiwan's economic growth will firm up amid synchronized global growth indicated by rising global manufacturing PMI. The TWD will likely continue to follow the KRW's movements but with a time lag. USDTWD is expected to fluctuate between 29.0 and 29.5 at present. We still hold our short USDTWD position with a target of 28.5.

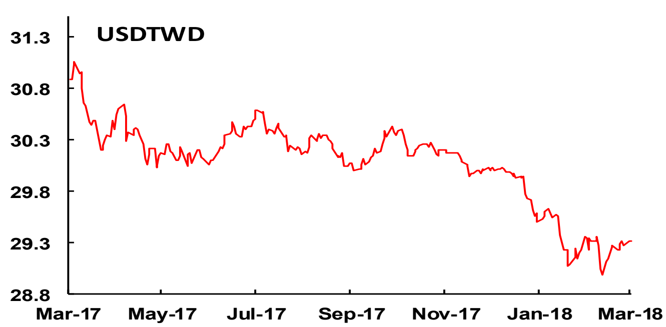
MALAYSIA — Prime Minister Najib Razak has given the strongest hint that the country's 14th General Election will be held before July14th. We believe the MYR is still undervalued in terms of either the NEER or the REER. While Bank Negara Malaysia (BNM) is expected to stand pat on its overnight policy rate (OPR) in March, we note its real policy rate is still in negative territory now. We maintain our existing short USDMYR position targeting 3.80.

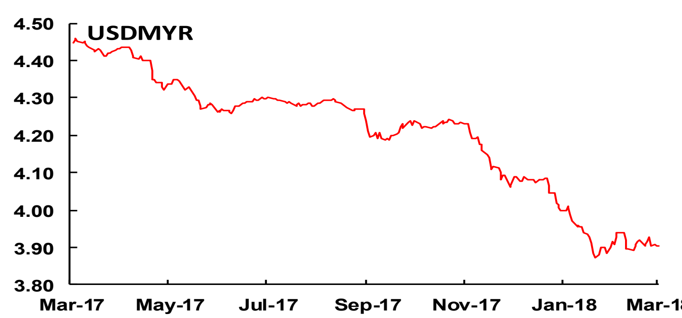
Currency Trends

FX Rate	Spot 6-Mar	18Q1f	18Q2f	18Q3f	18Q4f	19Q1f	19Q2f	19Q3f	19Q4f
USDKRW	1076	1060	1060	1040	1040	1030	1030	1020	1020
USDTHB	31.3	31.8	31.8	31.6	31.6	31.2	31.2	31.0	31.0
USDTWD	29.3	29.4	29.4	29.2	29.2	29.1	29.1	29.0	29.0
USDMYR	3.90	3.85	3.85	3.80	3.80	3.70	3.70	3.60	3.60









Developing Economies

Fundamental Commentary

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SOUTH KOREA — The Bank of Korea (BoK) will likely maintain monetary conditions unchanged in the very near term as external risks—related to geopolitics, trade protectionism, and monetary policy changes in major economies—persist. The 7-Day Repo Rate was raised by 25 basis points (bps) to 1.50% at end-November 2017. South Korea's headline inflation picked up to 1.4% y/y in February from 1.0% a month earlier; the relatively muted inflation in early 2018 reflects base effects related to food prices. We estimate that inflation will accelerate over the coming months on the back of strong domestic demand and will approach the BoK's 2% inflation target in mid-2018. BoK Governor Lee has been reappointed for a second term, implying monetary policy continuity. Once inflation has shown signs of a sustained pick-up, the BoK will likely tighten monetary policy further. We expect the next interest rate hike—of 25 bps to 1.75%—to take place in the second quarter of 2018, most likely at the May policy meeting. South Korean preliminary estimate for fourth quarter real GDP growth was somewhat weaker than expected, yet still a solid 3.0% y/y. All aspects of domestic demand—consumer spending, fixed investment, and public spending—continued to rise, though the external sector was a drag on growth due to strong import demand. The South Korean economy grew by 3.1% in 2017 as a whole; we expect the nation's output to rise by 2½% in 2018.

THAILAND — The Thai economy is performing well. Real GDP expanded by 4.0% y/y in the fourth quarter of 2017, taking output growth to 3.9% for 2017 as a whole, up from the 3.3% gain in 2016. The external sector—particularly merchandise exports and tourism—continues to be the driver of economic activity while domestic demand growth remains somewhat muted. We expect real GDP gains to average 3.5% y/y in 2018–2019. The Bank of Thailand's (BoT) monetary policy stance is set to remain accommodative over the coming months in order to stimulate domestic demand. The most recent policy meeting took place on February 14th; the BoT's Monetary Policy Committee unanimously voted to leave the key interest rate unchanged at 1.50%. We anticipate that a cautious monetary normalization phase will commence in the final months of 2018 after inflation has shown signs of a pick-up. Headline inflation eased to 0.4% y/y in February, remaining below the lower boundary of the BoT's medium-term inflation target of 2.5% y/y ±1.5%. We expect inflation to pick up gradually in the second quarter of 2018.

TAIWAN — Taiwan's economic outlook is favourable. Business confidence in the manufacturing sector is notably strong while export orders, up by 18.6% y/y in December-January, imply continued strong manufacturing activity over the coming months. Taiwan's real GDP expanded by 3.3% y/y in the fourth quarter of 2017, taking annual output growth to 2.8% for 2017 as a whole. Activity was driven by the external sector as well as private consumption, while fixed investment remained weak. We estimate that the economy will advance by 2½% in 2018. The Taiwanese central bank has a new governor, Mr. Yang Chin-long, who will serve a five-year term. We do not expect the leadership change to affect the central bank's policy biases. The next quarterly monetary policy meeting will be held on March 22nd; we expect that the benchmark interest rate will be left unchanged at 1.375%. Following the previous policy meeting in December, the central bank highlighted that Taiwan's output gap remains negative and inflation expectations are anchored. The central bank is forecasted to maintain the status quo until the third quarter of 2018 when we expect the policy rate to be raised by 12.5 basis points to 1.50%. Taiwan's headline inflation eased to 0.9% y/y in January from 1.2% y/y in December, reflecting the timing of the Chinese New Year, which fell in January last year. We expect a modest acceleration in inflation over the coming months on the back of strengthening demand-driven price pressures.

MALAYSIA — The Malaysian central bank, Bank Negara Malaysia (BNM), will tighten monetary policy very cautiously over the coming quarters. Following the January 25th monetary policy meeting, the BNM increased the Overnight Policy Rate by 25 basis points (bps) to 3.25%, marking the first hike since July 2014. Given that the policy rate is already close to its historical ceiling of 3.50%, we foresee only one more interest rate increase (of 25 bps) in 2018, likely to take place toward the end of the year. The BNM's decision to tighten monetary policy reflects Malaysia's ongoing strong economic growth that will likely feed demand-driven inflationary pressures over the coming quarters. The policy action was also justified by the central bank's need to prevent the build-up of financial risks that might arise from overly accommodative monetary conditions. Furthermore, we assess that the timing of the rate hike was optimal given that political uncertainty may rise in the coming months; Malaysia's next general elections are due by August 2018. The Malaysian economy continues to grow strongly; real GDP increased by 5.9% y/y in the fourth quarter of 2017 (vs. 6.2% y/y in Q3). Private sector demand continues to be the main growth driver. Household spending is underpinned by rising incomes and employment, while fixed investment is boosted by infrastructure projects and private sector capital investment in the manufacturing and services sectors. Higher government spending is providing further support to the economy. We forecast that the Malaysian economy will expand by 5½% in 2018 following a 5.9% advance in 2017.

Global Currency Forecast (end of period)

		2018f	2019f	2018f				2019f			
Major Currencies				Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
Japan	USDJPY	115	120	114	114	115	115	118	118	120	120
Euro zone	EURUSD	1.20	1.28	1.18	1.18	1.20	1.20	1.24	1.24	1.28	1.28
	EURJPY	138	154	135	135	138	138	146	146	154	154
UK	GBPUSD	1.37	1.40	1.35	1.35	1.37	1.37	1.38	1.38	1.40	1.40
	EURGBP	0.88	0.91	0.87	0.87	0.88	0.88	0.90	0.90	0.91	0.91
Switzerland	USDCHF	0.95	0.92	0.97	0.97	0.95	0.95	0.94	0.94	0.92	0.92
	EURCHF	1.14	1.18	1.14	1.14	1.14	1.14	1.16	1.16	1.18	1.18
Americas											
Canada	USDCAD	1.25	1.25	1.28	1.27	1.26	1.25	1.25	1.22	1.22	1.25
	CADUSD	0.80	0.80	0.78	0.79	0.79	0.80	0.80	0.82	0.82	0.80
Mexico	USDMXN	19.46	19.71	18.84	19.11	19.18	19.46	19.56	19.38	19.43	19.71
	CADMXN	15.57	15.77	14.72	15.05	15.22	15.57	15.65	15.89	15.93	15.77
Brazil	USDBRL	3.25	3.35	3.25	3.15	3.25	3.25	3.30	3.30	3.35	3.35
Chile	USDCLP	596	586	597	598	597	596	593	591	588	586
Colombia	USDCOP	2900	3050	2800	2900	2900	2900	2950	2950	3000	3050
Peru	USDPEN	3.18	3.12	3.22	3.19	3.20	3.18	3.18	3.14	3.15	3.12
Asia-Pacific											
Australia	AUDUSD	0.80	0.82	0.79	0.79	0.80	0.80	0.81	0.81	0.82	0.82
China	USDCNY	6.30	6.10	6.40	6.40	6.30	6.30	6.20	6.20	6.10	6.10
Hong Kong	USDHKD	7.81	7.78	7.82	7.82	7.81	7.81	7.80	7.80	7.78	7.78
India	USDINR	64.0	63.0	64.5	64.5	64.0	64.0	63.5	63.5	63.0	63.0
Indonesia	USDIDR	13400	13300	13600	13600	13400	13400	13350	13350	13300	13300
Malaysia	USDMYR	3.80	3.60	3.85	3.85	3.80	3.80	3.70	3.70	3.60	3.60
New Zealand	NZDUSD	0.74	0.76	0.73	0.73	0.74	0.74	0.75	0.75	0.76	0.76
Philippines	USDPHP	51.0	49.5	52.0	52.0	51.0	51.0	50.0	50.0	49.5	49.5
Singapore	USDSGD	1.30	1.28	1.32	1.32	1.30	1.30	1.29	1.29	1.28	1.28
South Korea	USDKRW	1040	1020	1060	1060	1040	1040	1030	1030	1020	1020
Taiwan	USDTWD	29.2	29.0	29.4	29.4	29.2	29.2	29.1	29.1	29.0	29.0
Thailand	USDTHB	31.6	31.0	31.8	31.8	31.6	31.6	31.2	31.2	31.0	31.0

f: forecast a: actual

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