December 5, 2017

AMERICAS

USD poised to weaken in 2018 as US growth and yield advantages deteriorate. CAD supported by rising commodity prices. MXN stable amid focus on NAFTA and the domestic political cycle.

EUROPE

EUR will remain supported despite significant yield disadvantage. GBP subject to short-term volatility around Brexit but downside risks are limited.

ASIA-PACIFIC

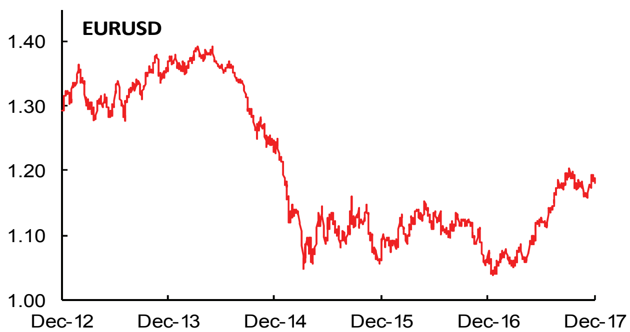
We expect the JPY to under-perform on relative policy risks. The AUD and NZD will rise modestly in the coming year.

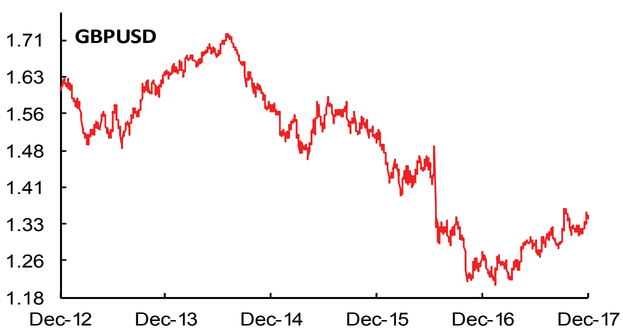
CONTENTS

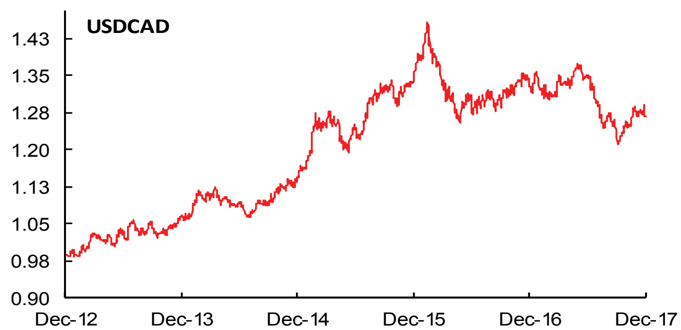
Core Exchange Rates

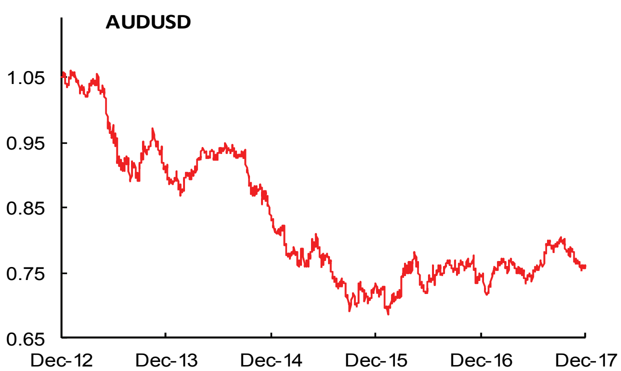
Global Foreign Exchange Outlook

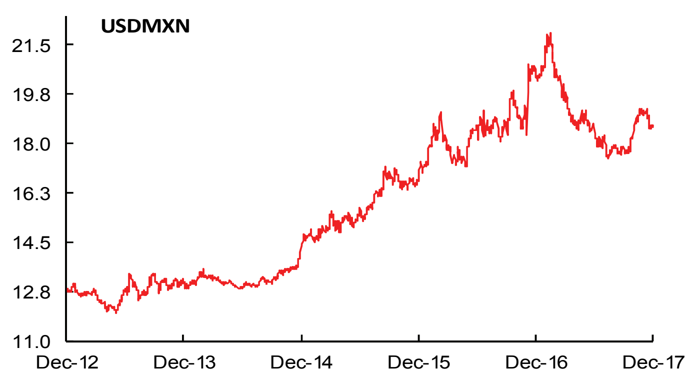
December 5, 2017	Spot	2018f Q1	2018f Q2	2018f Q3	2018f Q4	2019f Q1	2019f Q2	2019f Q3	2019f Q4
EURUSD	1.18	1.18	1.18	1.20	1.20	1.24	1.24	1.28	1.28
USDJPY	113	114	114	115	115	118	118	120	120
GBPUSD	1.34	1.35	1.35	1.37	1.37	1.38	1.38	1.40	1.40
USDCAD	1.27	1.28	1.27	1.26	1.25	1.25	1.22	1.22	1.25
AUDUSD	0.76	0.79	0.79	0.80	0.80	0.81	0.81	0.82	0.82
USDMXN	18.68	19.19	19.04	19.10	19.36	19.46	19.28	19.34	19.61











Market Tone & Fundamental Focus

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The US dollar (USD) is heading into the end of the year somewhat on the defensive. After a temporary reprieve from the broad downdraft that characterized trading between January and September, the USD fell sharply over the past month in a manner that suggests to us that its general retreat may be resuming. We assume a relatively benign global environment persists next year, allowing for strengthening global growth and rising global interest rates to erode the USD's growth and yield advantages that have propped up the currency in recent years. Tail risks around the outlook (political, geo-political and trade-related) are, however, significant and might be growing.

The USD's rally from early September was based on a strengthening in confidence that the Fed would tighten interest rates, a perceived reduction in domestic risks as economic momentum was sustained despite challenging weather conditions and concerns that the euro (EUR) rally had extended too quickly for the European Central Bank's (ECB) comfort. We think a lot of good news is factored in to the USD's current levels, however, with a Fed rate hike this month now a virtual certainty (according to market pricing) and scope for additional economic surprises limited for now. The USD has perked up alongside prospects for tax cuts being implemented soon but it is debatable whether cuts will lift growth materially in the longer run. We are bearish on the overall outlook for the USD moving into 2018 but expect a gradual, rather than sharp, decline in the currency in the next 12 months or so.

The Canadian dollar (CAD) will rise modestly in the next 12 months but the currency has been buffeted by rising US short-term yields, supporting the USD, on the one hand and an improvement in Canada-relevant commodities, delivering a positive terms of trade boost for the CAD, on the other. The Canadian economy is slowing after a strong first half and market expectations for additional Bank of Canada (BoC) rate increases retreated as a consequence. We expect the BoC to tighten rates modestly next year, with excess supply virtually fully eliminated, supporting a slightly firmer CAD. NAFTA risks loom rather significantly on the near horizon for both the CAD and the MXN, however. We anticipate a benign outcome to talks but signs of significant progress are not obvious at this point. We expect the MXN to remain broadly stable in 2018, assuming a positive conclusion to NAFTA talks. Inflation trends (and the impact on monetary policy) as well as the domestic political cycle will influence the exchange rate to a greater or lesser extent as well, however.

We expect the EUR to strengthen modestly in the coming year. Eurozone growth momentum is solid and we think likely to keep pace more or less with expansion in the US (after persistently under-performing in recent years). The EUR has been impervious to extremely onerous (record) short-term rate differentials versus the USD. We think this is at least partly explained by two related issues. Firstly, political risks in the Eurozone have decreased following key elections in France, Holland and Germany. And secondly, perhaps as a consequence, Eurozone-bound investment flows have improved, lifting the currency. Tighter ECB monetary policy remains some distance away but confidence in the economic outlook should bolster expectations that the ECB will move to taper asset purchases fully in the coming year and tighten monetary policy modestly in 2019. The ECB will be embarking on its tightening program as the Fed is nearing the end of its normalization process.

We are constructive on the outlook for the pound (GBP) in the longer run. The Bank of England (BoE) has initiated the start of what we expect to be a slow-burn tightening cycle, whilst maintaining its QE programme, as headline inflation has risen well above target. Tighter policy and progress on Brexit negotiations have added to near-term upward momentum in the GBP. A successful conclusion to the "divorce" proceedings will be a positive for the GBP in the near term but the economic impact of the split from the EU remains uncertain. We are constructive on the longer run outlook for the GBP as we think Brexit negatives have been largely factored in. We also think the GBP is subject to limited downside risk in a broad sense as valuation considerations suggest the GBP is still relatively "cheap" by historic standards.

For the other major currencies, we are bearish on the yen, but alert to any (hawkish) changes in the Bank of Japan's policy outlook that may infer a little more upside risk to the currency than we currently consider realistic. The Australian and New Zealand dollars are expected to appreciate modestly next year, supported by firm commodity prices and tighter monetary policy (late in 2018). Beyond the major currencies, we expect the CNY to hold in a range in the near-term and to edge marginally higher against a generally softer USD through 2018. Highly-leveraged emerging markets are possibly subject to heightened volatility as rising global interest rates suggests heightened competition for international investment flows.

Canada
Currency Outlook

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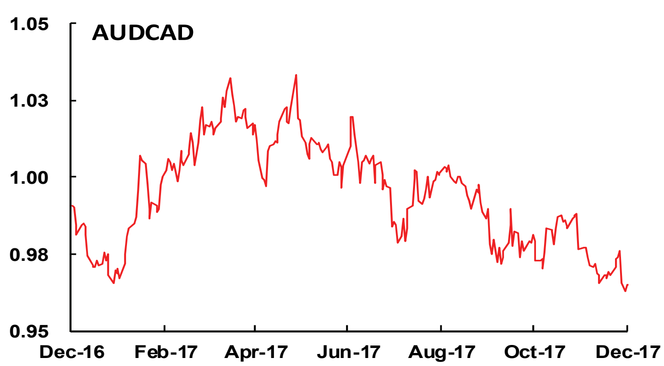
The CAD sell-off that developed from the USD's early September peak has steadied over the past month, with the USD essentially holding in a sideways range trade around 1.28. We expect the CAD to stabilize (at least) versus the USD into year-end but we maintain a modestly bullish outlook for the CAD moving into 2018 and look for the USD to fall to 1.25 over the course of the next 12 months.

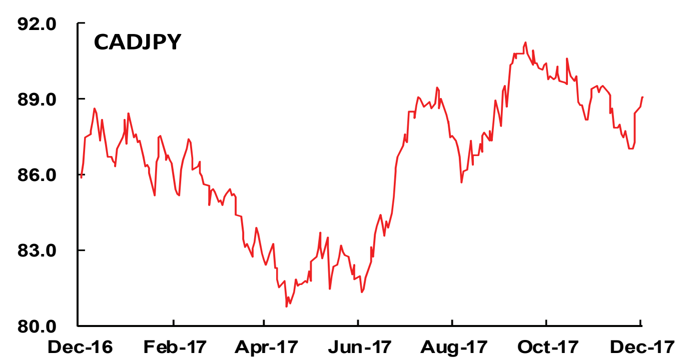
The CAD has become less sensitive to relative interest rates in the past month, ignoring a further 10bps widening in short-term, US-Canada rate spreads that ordinarily – and almost certainly, based on the influence of spreads on spot through the summer – would have suggested more scope for USD strength. Instead, the CAD has shown a tendency to reattach itself to rising crude oil prices, amid signals that OPEC oil producers (and others) will extend production cuts into 2018. The CAD's short-term correlation with yield differentials has softened, in other words, whereas its correlative relationship with crude has strengthened again.

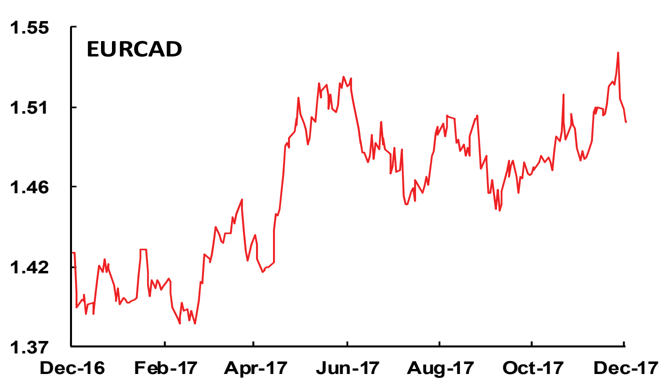
It should be noted that beyond modest gains in crude oil in the past few weeks, Canada-relevant commodity prices have strengthened broadly since early 2016 when commodities broadly reached a nadir. The BoC's commodity index has risen nearly 60% over the period while the broader commodity index (the Thomson-Reuters/CRB) has risen a little more than 10%. The implies a positive terms of trade boost for the Canadian economy and exchange rate that is arguably not yet fully factored into the CAD and might therefore suggest some near-term, upside risk to the CAD outlook even if uncertainties remain in the medium term (NAFTA).

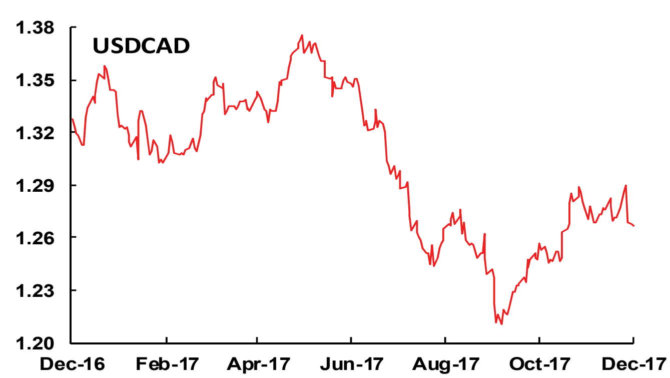
Canadian Dollar Cross-Currency Trends

FX Rate	Spot 5-Dec	17Q4f	18Q1f	18Q2f	18Q3f	18Q4f	19Q1f	19Q2f	19Q3f	19Q4f
AUDCAD	0.96	1.01	1.01	1.00	1.01	1.00	1.01	0.99	1.00	1.03
CADJPY	89.0	87.5	89.1	89.8	91.3	92.0	94.4	96.7	98.4	96.0
EURCAD	1.50	1.51	1.51	1.50	1.51	1.50	1.55	1.51	1.56	1.60
USDCAD	1.27	1.28	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 US economy is gathering strength. Real GDP clocked in at a 3.3% q/q annualized rate in Q3, up from the second-quarter's 3.1% advance; this marks the largest quarterly gain in three years. Recent indicators point to another solid increase in output of close to 3% during Q4. Healthy consumer spending and resurgent business investment support the pickup in activity. A robust job market has propelled the jobless rate to a 17-year low of 4.1% and consumer confidence to a 17-year high. Wages also are beginning to firm alongside the tightening in labour market conditions. Housing activity remains solid, though inventory shortages and worsening affordability are starting to restrain overall sales. Services activity is expanding across a range of industries, led by transportation and warehousing, and professional and business services. Business investment is expanding at its fastest pace in three years. Strengthening industrial activity and rising capital goods orders point to a further pick-up in capital spending into 2018. Non-residential construction is being bolstered by strength in commercial projects. The sweeping tax-reform package unveiled by Republican lawmakers, with its tilt toward tax reductions for business and higher-income households, may, if enacted in 2018, provide marginal additional stimulus, but its growth effects are likely to be limited. NAFTA remains a source of uncertainty. The US Administration's recent update to its NAFTA negotiation objectives makes the prospect of reaching an agreement by the end-March 2018 deadline more difficult, but we continue to expect the pact to survive. Core inflation is edging up, but remains moderate at 1.8% y/y in October.

CANADA — After a blistering start to 2017, the Canadian economy is settling down to a more sustainable pace. Real GDP growth in Q3 slowed to a 1.7% q/q annualized rate, down from a 4% average advance in the first half of the year. Consumer confidence and spending both remain buoyant, underpinned by strong employment growth and rising wages. The fastest pace of job creation in over a decade combined with a steady participation rate has pushed the unemployment rate to a cycle low of 5.9%. Auto sales are still tracking record highs. Even so, consumers are expected to moderate their spending. The income boost from last year's increase in child benefit payments is beginning to fade, though it will get a modest lift from the recent decision to begin indexing these benefits to inflation from mid-2018. Legislated increases in minimum wages in a number of provinces should also provide some support to spending. Regulatory measures have begun to cool home sales, though housing construction remains elevated. The housing sector should face further headwinds in the new year when stricter underwriting guidelines for uninsured mortgages come into effect and higher rates dampen affordability. Service-sector activity remains brisk, with notable gains in wholesale and retail trade, transportation and warehousing, and financial and professional services. Business investment is rebounding. Exports have weakened in recent months, due in part to temporary production shutdowns in a number of sectors, but are expected to rebound later in the year given strengthening global industrial activity. Infrastructure spending is ramping up. Inflation remains low, but has been trending higher in recent months. The average of the Bank of Canada's preferred measures of core inflation was 1.6% y/y in October, up from a low of 1.3% in May. Wage and price increases are expected to continue nudging it higher.

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Monetary Policy Commentary

UNITED STATES — Scotiabank Economics continues to expect another ¼ point fed funds target range hike to 1.25-1.5% at the December 13th FOMC meeting followed by two more next year and one in 2019. This is about 50bps below the FOMC 'dot plot' by the end of 2019 given the uncertainty surrounding matters such as the drivers of low inflation and fiscal policy effects, but we are about 25bps above market pricing over the same time period. We think a transitory inflation soft patch will get a lift from the effects of the USD this year while spare capacity has already shut. Our forecast continues to expect a roughly normalized balance sheet by the end of 2020 under the Fed's present reinvestment schedule. Continued international appetite for Treasuries, continued safe haven appeal due to stock market and geopolitical risks and late cycle dynamics are more likely to result in curve flatteners pending the outlook for fiscal deficits.

CANADA — Scotiabank Economics continues to expect the Bank of Canada (BoC) to hold its policy rate unchanged at 1% until April 2018. We expect two rate hikes in 2018 followed by three more in 2019. Much of the fundamentals-based criteria for continued BoC hikes remain intact including the closure of spare capacity, strong employment gains and firming wage and price dynamics but soft exports and relatively low inflation temper such readings. The Bank of Canada nevertheless places more emphasis upon potential downside risks such as NAFTA negotiations, household debt sensitivities to higher rates, the impact of tightened mortgage rules and external fiscal and geopolitical risks. Evaluating each of these risks involves patience with future forecast revisions to be informed by their progress.

G10

Currency Outlook

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EUROZONE — EUR has entered December around the midpoint of its multi-month range. Seasonals are supportive into year-end and we continue to highlight EUR's resilience in the face of extended (in some cases, record) bearish interest rate differentials. Bullish EUR positioning is extended however, with gross CFTC speculative longs at fresh record highs. We hold a relatively neutral EUR forecast, with a Q1 2018 target of 1.18 and a year-end 2018 forecast of 1.20.

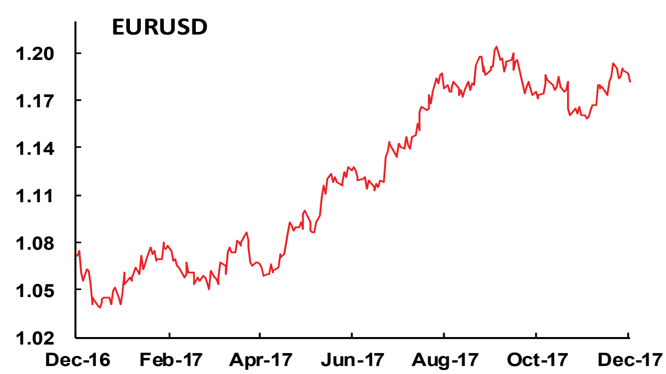
UNITED KINGDOM — GBP remains vulnerable to headline risk in the context of ongoing Brexit negotiations. Talks relating to the 'divorce bill' are nearing completion, paving the way for 2018 discussions on the topic of the U.K.'s post-Brexit trading arrangement with the EU. Speculative CFTC GBP positioning is close to neutral and risk reversals are showing an erosion in the premium for protection against GBP weakness. We are neutral GBP with a Q1 2018 target at 1.35 and a year-end 2018 target at 1.37.

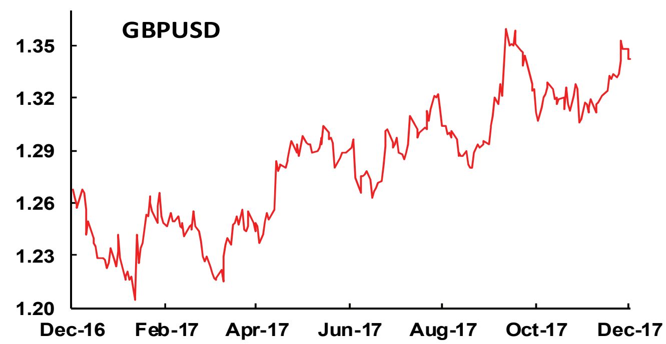
JAPAN — JPY has entered December at the midpoint of its 2017 range. Longer-term yield spreads remain a key driver as geopolitical concerns deliver short-lived knee-jerk rallies. Speculative CFTC JPY positioning is bearish, and extended, leaving it vulnerable to adjustment. We hold a bearish JPY forecast, with a Q1 2018 USDJPY target of 114 and a year-end 2018 forecast of 115.

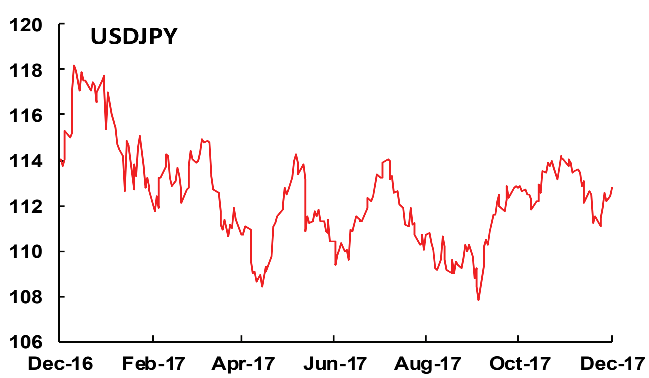
AUSTRALIA — AUD is showing signs of stabilization just above its multi-month low from late November. Interest rate differentials appear to be dominating as we note the absence of any meaningful support resulting from the renewed rally in iron ore. Speculative positioning adjustments (CFTC) are suggestive of a bearish turn in sentiment. We are marginally constructive on the outlook for AUD, with a Q1 2018 target of 0.79 and a year-end 2018 forecast of 0.80.

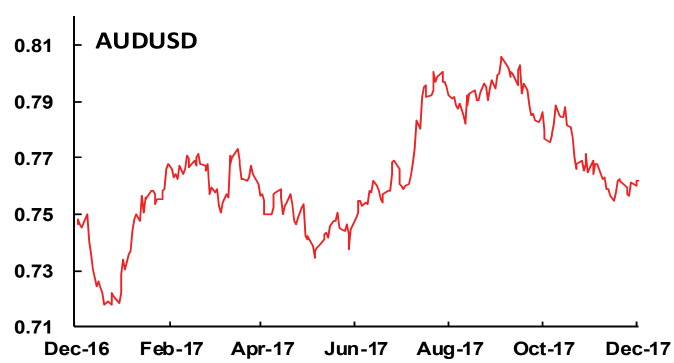
Currency Trends

FX Rate	Spot 5-Dec	17Q4f	18Q1f	18Q2f	18Q3f	18Q4f	19Q1f	19Q2f	19Q3f	19Q4f
EURUSD	1.18	1.18	1.18	1.18	1.20	1.20	1.24	1.24	1.28	1.28
GBPUSD	1.34	1.33	1.35	1.35	1.37	1.37	1.38	1.38	1.40	1.40
USDJPY	113	112	114	114	115	115	118	118	120	120
AUDUSD	0.69	0.79	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 Eurozone survey indicators remain well supported with fresh highs in both the manufacturing and composite PMI's, pointing to robust, above-potential levels of growth. The euro area unemployment rate hints to a continued erosion in labor market slack, falling to fresh, near-decade lows under 9.0%. Inflation remains below target with core consolidating around 1.0% y/y and headline CPI recovering to 1.5% y/y. The ECB's 2018 taper has been announced, with a halving in the pace of asset purchases to 30bn. The programme is expected to run until September 2018. Discussions relating to the normalization of conventional policy are likely to dominate the ECB narrative throughout 2018 as market participants assess the timing of interest rate increases in 2019. Scotiabank anticipates two 25bpt rate increases in 2019, in Q2 and Q4.

UNITED KINGDOM — UK economic prospects have not changed materially over the past month. Retail sales were very soft in October, with ex-fuel sales falling 0.3% year over year. This was the weakest reading since early 2013 and underscores concerns that rising inflation and flat wage growth will crimp consumer demand and restrain growth, with little else to offset this weakness. Surveys suggest the consumer demand rebounded somewhat in November but growth prospects remain challenging. The UK budget came and went with little fanfare and little to alter what remains a relatively weak outlook. Prospects for a quick follow up to the BoE's November rate tightening remain remote. With little change in fundamental prospects, near-term GBP volatility is being driven largely by negotiations surrounding talks which will shape the UK's future relationship with the EU – and the difficulty that UK Prime Minister May is having satisfying diverging interests in her own government. Markets appear to be assuming a benign outcome to discussions which will pave the way for formulating a deal to facilitate UK access to the EU once the Article 50 process is complete, the so-called "soft Brexit". Absent an agreement, "hard Brexit" (i.e. no trade deal with the EU and a return to WTO rule-based trade arrangements) risks will increase, prompting more uncertainty for UK-based businesses and the pound.

JAPAN — Japan's inflationary pressures remain far the Bank of Japan's (BoJ) 2% y/y inflation target. In October, the country's headline inflation eased to 0.2% y/y from 0.7% in September. Meanwhile, core inflation—the CPI excluding fresh food and energy—remained unchanged at 0.2% y/y. Japan's nominal wage inflation accelerated to a still-muted level of 0.9% y/y in September from an average of 0.4% y/y in the first half of 2017. Nevertheless, inflation-adjusted wage increases remain minimal despite Japan's tight labour market. Accordingly, demand-driven inflationary pressures will likely remain absent in Japan over the coming quarters. The BoJ's final monetary policy meeting in 2017 will take place on December 21. The country's monetary policy stance is expected to remain unchanged for an extended period of time as inflation continues to be low. While cautious alterations to the BoJ's asset purchase program are possible before the end of 2019, we do not expect the short-term policy rate (-0.1%) to be increased within our forecast horizon. Japan's current economic activity remains solid with output gains surpassing the country's potential growth rate (of around ½% y/y) by a wide margin. According to preliminary estimates, real GDP grew by 0.3% q/q (non-annualized) in the third quarter of 2017 following a 0.6% gain in the April-June period. In year-over-year terms, output grew by 1.6%, up from the 1.5% pace recorded in the second quarter. We expect Japan's economic growth to average 1.6% y/y in 2017. In 2018–19, real GDP growth will likely be lower—and more sustainable—averaging 1.0% y/y.

AUSTRALIA — Australia's monetary conditions are set to remain unchanged for an extended period of time as accommodative monetary policy is needed to underpin domestic demand. The nation's headline inflation eased to 1.8% y/y in the third quarter of 2017 from 1.9% in the April-June period. While we expect a modest pick-up in inflationary pressures over the coming quarters, the headline inflation rate will likely hover near the low end of the Reserve Bank of Australia's (RBA) 2–3% inflation target range through 2018. Inflationary pressures will likely intensify somewhat over the course of 2019, reaching 2⅔% y/y by end-2019. As a response to gradually rising inflation projections, we expect the RBA's first benchmark interest rate hike to take place in the fourth quarter of 2018. The central bank will likely have a cautious approach to monetary normalization, with additional adjustments anticipated in the second and fourth quarters of 2019 that will take the policy rate to 2.25% by year-end. The Australian labour market is strengthening gradually, yet employment data continue to be volatile. The country's unemployment rate declined to 5.4% in October, the lowest rate in 4½ years. Meanwhile, hourly nominal wages increased by 2.0% y/y in the third quarter, slightly surpassing the inflation rate of 1.8% y/y. A stronger pick-up in real wages would make Australia's economic growth outlook more sustainable given that consumer spending is a key driver of the economy's momentum.

China, India, Brazil

Currency Outlook

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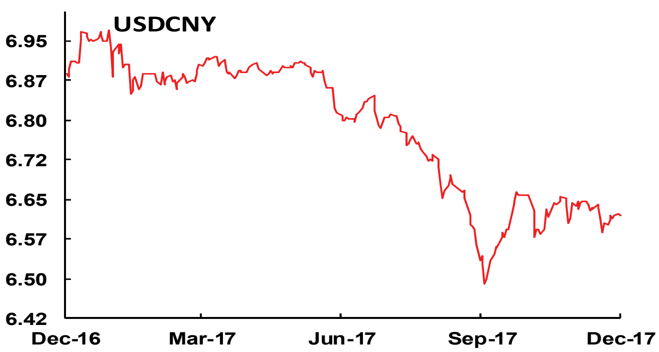
CHINA — The CNY underperformed a basket of currencies in November amid a broadly weakening dollar. However, the CFETS RMB Index could rebound as the dollar is likely to rally modestly on the back of the progress on the GOP tax reform and relatively hawkish remarks from Fed top officials. USDCNY is expected to trade in a range of 6.50-6.70 in December, while remaining susceptible to the EUR that is likely to rebound on hopes for a fresh "grand coalition".

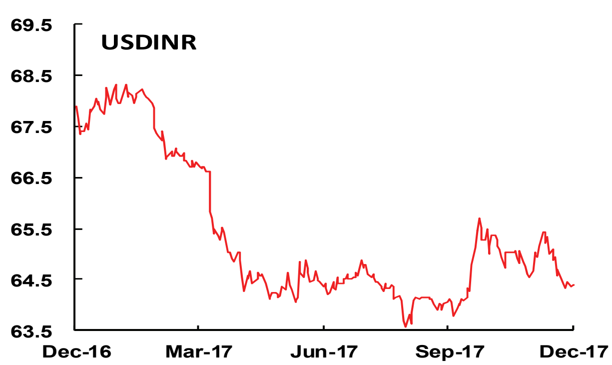
INDIA — India's GDP growth rebounded in the September quarter but cumulative fiscal deficit worsened to 96.1% of the budget estimate for FY2017–18 at the end of October. As a major catalyst for 2019 Lok Sabha elections, the results of the upcoming Gujarat Assembly Elections on December 9–18 will be crucial for both the BJP and the Congress. USDINR is expected to track a broader market tone with an upward bias towards 65 in December.

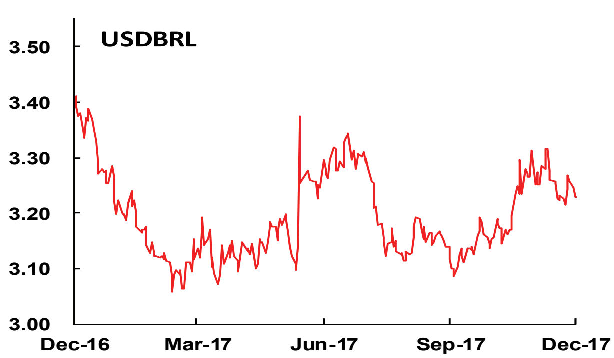
BRAZIL — BRL took a plunge the past two months as the politics around pension reform took a turn for the worse. However, it seems like markets are now taking the no-reforms for now risks as "priced in", leaving USDBRL trading sideways in a 3.20-3.30 range. For now, it seems like markets are comfortable with the Brazilian macro picture as one where the reform outlook is stalled until after the 2018 elections, but in the meantime, the improved growth backdrop is enough good news to stabilize the BRL. The main risks, both negative and positive are related to the 2018 elections, where the outlook remains too fluid to call. A reformist government with a legislative mandate should boost the real, but the weakness risks triggered by a more populist Lula or Bolsonaro government cannot be discarded.

Currency Trends

FX Rate	Spot 5-Dec	17Q4f	18Q1f	18Q2f	18Q3f	18Q4f	19Q1f	19Q2f	19Q3f	19Q4f
USDCNY	6.62	6.60	6.55	6.55	6.50	6.50	6.45	6.45	6.40	6.40
USDINR	64.4	65.0	64.5	64.5	64.0	64.0	63.5	63.5	63.0	63.0
USDBRL	3.23	3.35	3.45	3.50	3.55	3.60	3.55	3.55	3.50	3.50







China, India, Brazil
Fundamental Commentary

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CHINA — Chinese authorities are making progress in tackling the economy's imbalances. On November 17, they unveiled plans for tighter rules on asset management businesses in order to reduce systemic risks related to the shadow banking industry. In our view, this is a significant and needed reform, given that the pricing of risk related to shadow banking products has been inadequate, making the industry one of the weakest links and biggest risk factors in the Chinese economy. The industry has been giving investors implicit guarantees against losses, reflecting the practice that funds from new product issuance have been used to cover investment losses from older ones. The new rules will prohibit such practice and will set harmonized rules across the financial industry to prevent regulatory arbitrage. The implementation period runs until mid-2019; bouts of market turbulence can be expected over the coming quarters as the magnitude of nonperforming debt becomes clearer. Monthly data on China's economic activity in October confirmed that decelerating forces are taking place. The slowdown in industrial activity was unsurprising on the back of sizable factory closures that have been put in place to meet environmental standards. Meanwhile, the slowdown in retail sales growth in October was unexpected, particularly given that year-to-date real disposable income growth was solid at 7.5% y/y in the third quarter, outperforming the nation's real GDP growth. The People's Bank of China (PBoC) released the third quarter Monetary Policy Report in mid-November. The central bank reaffirmed that it will continue to implement "neutral and prudent" monetary policy, as it helps maintain a favourable financial environment for continued supply-side reforms and stable economic growth. We do not expect any changes to the monetary policy stance over the coming months. China's headline inflation rate accelerated to 1.9% y/y in October from 1.6% a month earlier. We expect inflation to remain around the 2% mark over the next few months before reaching 2.5% by the end of 2018.

INDIA — India's economic growth is strengthening; real GDP growth accelerated to 6.3% y/y in the third quarter from 5.7% in the April-June period. Business sentiment has recovered since the low point in July when the nationwide Goods and Services Tax was introduced that caused disruptions to business processes. Following an estimated growth of 6.4% in 2017 as a whole, real GDP gains will likely average 7½% in 2018–19 as the positive impacts from structural reforms improve India's business environment and lead to a sustained pick-up in investment. At end-October, the Indian government approved a sizable two-year recapitalization plan for the country's public sector banks that have been suffering from elevated non-performing assets. More than half of the sum will come from the sale of special recapitalization bonds while the rest will come from banks' share sales and the government's budgetary provisions. The capital injection will help encourage a pick-up in lending in the economy. Against the improving macroeconomic backdrop, Moody's upgraded India's long-term local and foreign currency sovereign ratings by one notch to "Baa2" in mid-November. Both S&P and Fitch rate India one notch lower; given that they both have a stable outlook on India's sovereign credit rating, they are unlikely to follow the Moody's upgrade anytime soon. India's headline inflation picked up to 3.6% y/y in October from 3.3% a month earlier. We estimate that further modest acceleration will take place over the coming months. In addition to the inflation outlook, the Reserve Bank of India (RBI) will pay particular attention to the risk of fiscal slippage by the government as it evaluates the appropriateness of the current monetary policy stance. Accordingly, the RBI will likely leave its benchmark interest rates unchanged through 2018; we assess that the next monetary policy move is a hike, likely to take place in the first quarter of 2019.

BRAZIL — Recent economic indicators continue to suggest growth is very slowly gaining traction, led by an upswing in consumer demand which we believe is supported by relief to the private sector on the back of lower interest rates. Brazil's private sector is more responsive to changes in interest rates than most large LATAM markets due 1) relatively high debt levels, and 2) the relative short maturity of the country's debt, which means debt resets quicker to a changing rate environment (both up or down). On that front, as long as long as the inflation backdrop remains benign, the upswing in consumer spending, and to a lesser degree corporate investment should remain supported by rates. We see the corporate side of the rebound as a little more vulnerable to a stalled reform drive (through confidence), which seems like a rising risk. On the monetary policy front, the BCB is once again expected to deliver a rate cut, in this case a 50bps move, to 7.0%. Brazil's neutral real policy rates have traditionally been around 5%, but following the TJLP reform – which should help de-segment credit markets, its possible neutral rates are now lower. However, we still don't think neutral real rates sit below 4%. At this point, rates are now in lose settings, but not massively so. We think we are getting close to the end of the rate cut cycle, but we don't think we are at it yet. What could derail the easing cycle, and potentially push it into back-pedaling mode? Again, we think politics could be the most likely trigger, with a stalled reserve drive, or a populist candidate victory likely pushing the BRL to weaken, in turn forcing the BCB to backpedal on the rates front. We think that risk is not here yet.

Pacific Alliance
Currency Outlook

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MEXICO — There are several factors that will have an influence on the MXN this year-end. On the external front, the possible implications of a deep fiscal reform in the US and the expected hike in the Fed's interest rate would provide some pressure on the Peso, which will also remain sensitive to concerns being generated by geopolitical tensions. Later on, the next NAFTA renegotiation round is expected to be more of the same: comments about advance but no concrete achievements and the usual pressure from the US trade representative, then bringing some anxiety to the FX market.

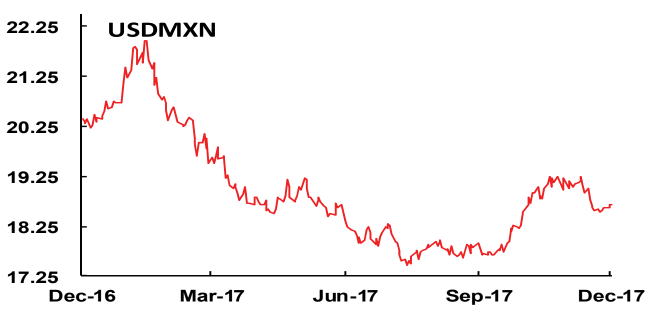
COLOMBIA — The peso is finally benefiting from the rebound in oil prices, after struggling to benefit from stronger crude since September. USD/COP spiked from around 2900 to 3050 from September to early November, before finally regaining its footing and rebounding to just south of 3000. Stronger oil should benefit the peso to the degree it helps rebalance the country's external accounts, but there are also internal risks to consider, with the 2018 presidential elections, and the underwhelming progress on fiscal adjustment taking center stage.

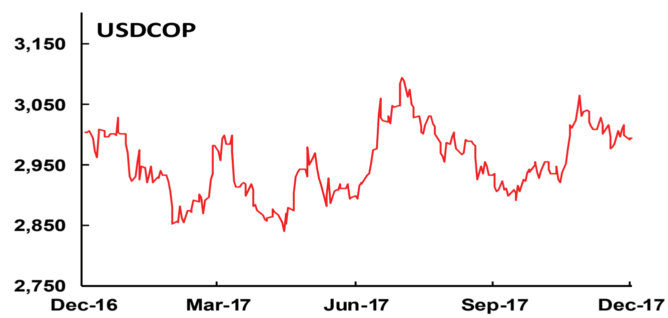
CHILE — In November, the Chilean peso depreciated against the USD a tad less than 2%. The explanation is a result of an increase in domestic political risk due to elections. Probably, volatility of spot price will remain relatively high (as for prices of other Chilean assets, like stocks and bonds), up to the 3rd week of December. Based on historical parameters and the most trustable projections, there are not good reasons to expect a year end level very far from our original forecast (USDCLP641), but even lower, rather around USDCLP636 . Even more, risk for projection is rather downward skewed. For next year our forecast was cut to USDCLP626.

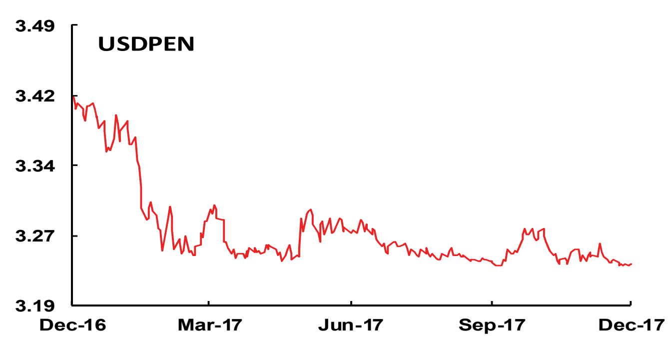
PERU — The Peruvian sol (PEN) continued appreciating, as much as the CB would allow, driven by buoyant metal prices, improving external accounts, and offshore inflows. We maintain our forecasts of 3.22 this year-end, and 3.18 by year-end 2018, but advise that a lot hinges on CB policy.

Currency Trends

FX Rate	Spot 5-Dec	17Q4f	18Q1f	18Q2f	18Q3f	18Q4f	19Q1f	19Q2f	19Q3f	19Q4f
USDMXN	18.68	18.99	19.19	19.04	19.10	19.36	19.46	19.28	19.34	19.61
USDCOP	2993	3005	3100	3100	3050	3000	3000	3050	3100	3100
USDCLP	653	636	633	631	629	626	623	620	617	613
USDPEN	3.23	3.22	3.20	3.19	3.17	3.18	3.19	3.15	3.16	3.13







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MEXICO — Our macroeconomic scenario remains basically the same. After GDP numbers for Q3 were released, and even though it was a bad quarter in terms of growth, our forecast for the whole year remained the same (+2.4% real). Worth noting that the official statistics institute (INEGI) made a change in the base year of the national accounts information, and GDP growth numbers, were revised upwards in previous quarters to 3.2% from 2.8% real y/y in Q1 and 1.9% from 1.8% real y/y in Q2. It should also be noted that Q3 figures were affected by the natural disasters that especially affected oil and gas extraction (-12.2% real y/y) and oil and carbon derivatives (-21.1% real y/y). On the other hand, there is strong growth in many other sectors: machinery and equipment (+18.3% real y/y), electronics fabrication (+6.5% real), transportation equipment (+10.1% real y/y) and financial and insurance services (+8.2% real y/y) among others. However, inflation has remained stubbornly high, reaching 6.59% in the first half of November; while there was a 10.4% increase in minimum wages, effective December 1st; that could have an additional mild impact on inflation. In this environment, we keep expecting Banco de Mexico to increase its reference interest rate in the very near future. Finally, there were significant changes in the Presidential cabinet: José Antonio Meade will become the PRI's presidential candidate and has resigned as the Finance Minister and was replaced by José Antonio González Anaya, former PEMEX General Director. On Banco de Mexico, Alejandro Díaz de León was appointed as the new Governor, substituting Agustín Cárstens. All these changes were well received by the markets.

COLOMBIA — On the macro front, still soft growth data continues to support an easing bias by BanRep, driving another 25bps semi-surprise rate cut (this time, half of economists did anticipate it), that took the policy rate to 4.75%. With inflation sitting at 4.05%, rates settings are now mildly on the lose side, but if we consider 1yr or 2yr ahead expected inflation (arguably the more appropriate way to look at monetary policy), then policy settings look neutral, which is likely what is driving the central bank's continued dovish bias. We don't disagree with the easing, our concern is more on the timing. We think it would be more prudent to wait a couple of months until inflation is more clearly on a downtrend, as it remains just above the CB's target range. On the political front, the elections are starting to come into market focus, but our sense is that the risks from them are only modest. As we anticipated, we are seeing voter expectations consolidate in favor of establishment candidates, while the more radical ones are falling behind. At the moment, pragmatic centrist Sergio Fajardo leads the polls (21%), followed by former VP German Vargas Lleras (12.5%), while former Bogota Mayor and guerrilla militant Gustavo Petro trails at 10.4%, after having led the polls a couple of months ago. As long as this trend holds, the elections should not be a material source of market volatility, although its worth bearing in mind all the surprising results we've had recently, including in Chile a couple of weeks ago.

CHILE — The aggregate data coming from national accounts was mostly aligned with previous information, with the economy growing at 2.2% y/y in Q3, domestic demand at 2.5%, exports at 3% and imports at 4.4%. Current account deficit reached 2.2% of GDP (1.7% in the last 4 quarters). If you add that inflation remains below 2%, unemployment is at 6.7% (not too much above what is estimated the natural rate) and the fiscal deficit estimated for the current year is around 3%, one could conclude the Chilean economy is basically balanced. The problem is the rate of growth for the parameters (supply and demand) remains relatively low compared with the past and even with other countries. GDP is expected to improve in Q4, probably up to 2.4%, but basically shored up by statistical factors. For next year our base case remains at 2.8%. Other factors should also tend to normalcy, like inflation reaching close to 3% and monetary policy rate, though stable up to mid-2018, should start to moderately raise going forward. Moreover, market reaction after the first round of the presidential election was disappointing, which meant that prices of the most important domestic assets plummeted, including stocks, the currency and bonds. Putting aside this can be a temporary reaction, probably it might have some flipside in real investment, which might be partially delayed until we know the result of the run-off, implying a deeper contraction of the item (the worst performer of the national accounts in last 4 years). Accordingly, we also expect prices of mentioned basic assets should return to a normal trend by year-end, once the political dust starts to clear.

PERU — Recently, Peru has seen a mix of good macroeconomic news, and not nearly so good political news. Peru's GDP rose 3.2%, in September, and monthly GDP is coming in closer to 3.0% more consistently. Given recent figures, we see upside to our 2.5% full-year 2017 GDP forecast. Mining and construction stand out as they were up 9.1% and 8.9 respectively, in September. Nearly two-year high cement demand volumes, construction GDP growth could reach 15% in October. The sharp upturn in October financial systems loans, up10% MoM, is another sign of the turnaround in Peruvian growth. Congress approved an expansion 2018 fiscal budget, that includes a 10.3% spending increase, mainly in public sector investment (17.5%). Inflation in November was -0.2% for the month and 1.5% for the year, with a sharply declining trend. We believe that the CB is likely to continue reducing its reference rate, to 3.0% in December, after cutting 25bps in November to 3.25%. A second wave of Lava Jato events have added to political uncertainty even as the economy improves. Statements by Marcelo Odebrecht involve campaign financing for "all major contenders" during the 2006 and 2011 presidential races, and the possibility that Odebrecht may have hired PPK, and/or a firm he may have been linked to, for financial advisory work. Finally, executives from major local construction companies that partnered with Odebrecht were detained by court order pending trial.

Developing Economies

Currency Outlook

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SOUTH KOREA — The BoK will not rush into a second rate hike in the near term. BoK Governor Lee Ju-yeol said on 30 November that the policy direction is reducing accommodation and the negative impact of the KRW's strength on exports has decreased. USDKRW is expected to trade between 1,080 and 1,120 with an upward bias in December. In 2018, a gradual tightening cycle could further prop up the KRW amid continued global synchronized growth.

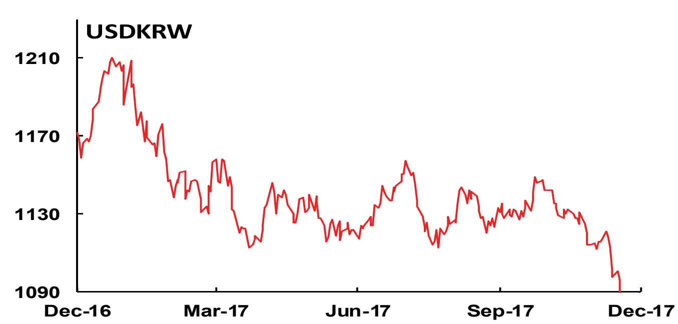
THAILAND — The MPC viewed the degree of monetary policy accommodation should be maintained for some period to support more robust domestic demand, according to the minutes of the BoT's November 8 meeting. Meanwhile, the nation's CPI inflation could return to the target range of 2.5%±1.5% faster than earlier forecast. Thailand's solid fundamentals including large current account surplus will continue to bolster the THB. USDTHB is anticipated to trade between 32.0 and 33.0 in December.

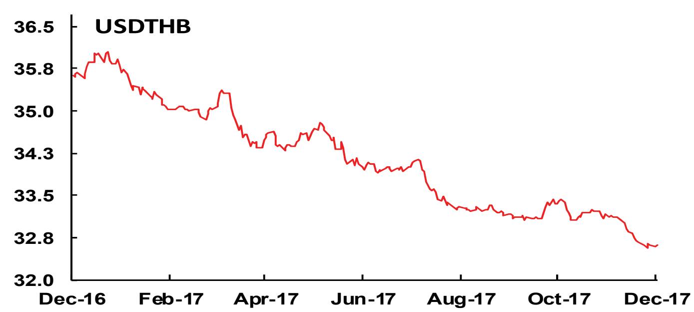
TAIWAN — Taiwan's government raised its 2018 growth estimate to 2.29% from 2.27%, while increasing its CPI inflation forecast for 2018 to 0.96% from 0.87%. The CBC is expected to leave its policy rate unchanged at 1.375% on 21 December, even though the BoK led the way in Asia with a 25 bps rate hike last month. The TWD will likely continue to follow the KRW's movements but with a time lag. USDTWD is expected to fluctuate around the 30.0 level in December.

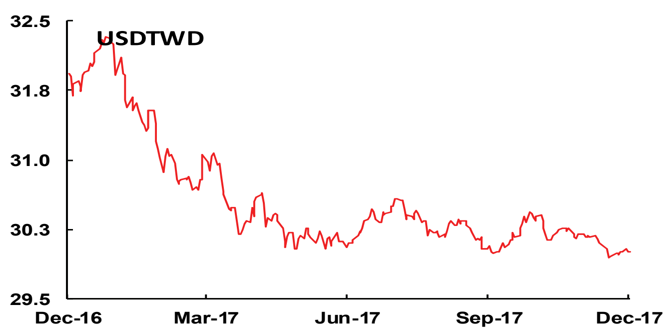
MALAYSIA — The BNM has said that it may consider reviewing the current degree of monetary accommodation and the MYR is "far from reflecting its fair value." Crude oil prices could extend their modest rally into the year of 2018 given the latest nine-month extension to the output cut deal, enhancing Malaysia's external balance and boost the MYR afterwards. We remain bullish on the MYR and expect USDMYR to head for 4.00 in the months ahead.

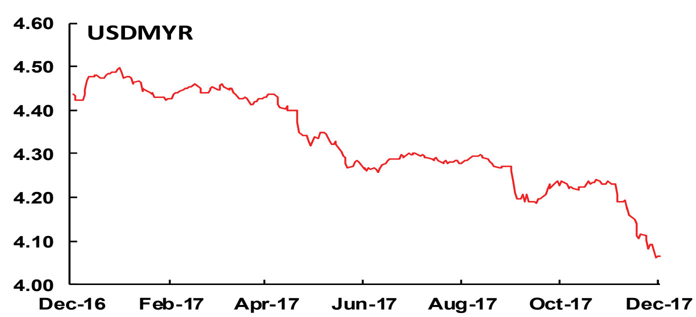
Currency Trends

FX Rate	Spot 5-Dec	17Q4f	18Q1f	18Q2f	18Q3f	18Q4f	19Q1f	19Q2f	19Q3f	19Q4f
USDKRW	1086	1120	1100	1100	1080	1080	1060	1060	1040	1040
USDTHB	32.6	32.5	32.2	32.2	32.0	32.0	31.5	31.5	31.0	31.0
USDTWD	30.0	30.2	30.1	30.1	30.0	30.0	29.9	29.9	29.8	29.8
USDMYR	4.07	4.05	4.00	4.00	3.95	3.95	3.90	3.90	3.85	3.85









Developing Economies

Fundamental Commentary

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SOUTH KOREA — Monetary normalization has commenced in South Korea following the Bank of Korea's (BoK) decision on November 30 to raise the 7-Day Repo Rate by 25 basis points to 1.50%. According to BoK Governor Lee Ju-yeol, the interest rate increase will help prevent future financial imbalances. The BoK will likely adopt a cautious approach to monetary tightening. We forecast two more rate hikes over the course of 2018, likely to take place in the second and fourth quarters. The country's economic growth has proven to be strong with real GDP advancing by 3.8% y/y in the third quarter of 2017. Activity is fairly broadly based with accommodative fiscal and monetary policies supporting domestic demand. Indeed, consumer confidence is strong, implying that household spending will maintain its momentum over the coming quarters. Solid business sentiment and robust external sector activity will underpin facilities investment, while a pick-up in global demand will continue to buttress South Korea's exports. We forecast the country's real GDP growth to reach 3.2% y/y in 2017, up from the 2.8% pace recorded in 2016. We estimate that South Korea's negative output gap has fully closed, which is expected to trigger a gradual pick-up in demand-driven inflationary pressures over the coming quarters. While we estimate that South Korea's headline inflation will remain under the BoK's 2% y/y inflation target in the near term, price pressures are set to intensify gradually from the second quarter of 2018 onwards. Nevertheless, a tighter monetary policy stance will help keep headline inflation below 2.5% y/y through 2019.

THAILAND — The Thai economy is benefiting from the pick-up in global demand. The country's real GDP grew by 4.3% y/y in the third quarter of 2017 following a 3.8% gain in the prior quarter. The external sector—particularly merchandise exports and tourism—continues to be the driver of economic activity while domestic demand growth remains at a more moderate level. Following the strong third quarter data, we have revised our real GDP growth projection for Thailand and now expect the nation's output to grow by 3.8% in 2017 as a whole (vs. the earlier forecast of 3.5%). 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 November 8; 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 by mid-2018. Headline inflation accelerated to 1.0% y/y in November, reaching the lower boundary of the BoT's medium-term inflation target of 2.5% y/y ±1.5%. We expect inflation to remain near the current level in the very near term before starting to pick up gradually in the second quarter of 2018.

TAIWAN — Strengthening trade activity globally is reflected in the Taiwanese economy. Real GDP expanded by 3.1% y/y in the third quarter of 2017 following a 2.3% gain in the April-June period. The external sector is the economy's driving force on the back of strong global demand for electronics, particularly for semiconductors. Meanwhile, domestic demand continues to be relatively weak. We expect Taiwan's real GDP to grow by 2.8% in 2017 and around 2.5% in 2018–19. Price pressures remain low in Taiwan though inflation returned to positive territory in November; prices at the headline level rose 0.3% y/y following a 0.3% decline in October. Meanwhile, prices excluding vegetables, fruit, and energy continued to rise, with core inflation accelerating to 1.3% y/y in November from 1.1% a month before. We expect the headline inflation rate to rise only moderately over the course of 2018 on the back of weak inflation expectations and still-soft domestic demand. Accordingly, we do not expect any changes to the central bank's monetary policy stance over the coming months. The benchmark interest rate was left unchanged at 1.375% at the quarterly monetary policy meeting in September. The next monetary policy meeting is scheduled for December 21.

MALAYSIA — The Malaysian economy continues to grow strongly. Real GDP expanded by 6.2% y/y in the third quarter of 2017 following a 5.8% gain in the April-June period. Growth is broadly based across household consumption, fixed investment, public spending, and net exports. We expect the country's real GDP to advance by 5.8% this year. In 2018–19, the economy will likely expand by around 5⅓% y/y. Malaysia's headline inflation eased to 3.7% y/y from 4.3% a month before; we expect further deceleration in the very near term. Nevertheless, strong domestic demand will generate some inflationary pressures over the coming quarters, prompting the central bank to begin normalizing monetary policy in early 2018. Following the most recent monetary policy meeting on November 9, Bank Negara Malaysia left the Overnight Policy Rate unchanged at 3.0%. Nevertheless, the monetary policy committee noted that it might consider reviewing the need for the current degree of monetary accommodation. The next policy announcement is scheduled for January 25. Malaysia's 2018 Budget targets a fiscal deficit of 2.8% of GDP next year, down from an estimated 3% shortfall in 2017. A modest recovery in global oil prices will support public revenue, allowing for cuts in certain income taxes and an array of benefits for civil servants. The generosity of the budget is not surprising given that general elections are approaching. The elections are due by August 2018, yet they are expected to be called in the near future.

Global Currency Forecast (end of period)

		2017p	2018p	2019p	2017p		2018p				2019p			
Principales Divisas					T3r	T4	T1	T2	T3	T4	T1	T2	T3	T4
Japón	USDJPY	112	115	120	113	112	114	114	115	115	118	118	120	120
Eurozona	EURUSD	1.18	1.20	1.28	1.18	1.18	1.18	1.18	1.20	1.20	1.24	1.24	1.28	1.28
	EURJPY	132	138	154	133	132	135	135	138	138	146	146	154	154
Reino Unido	GBPUSD	1.33	1.37	1.40	1.34	1.33	1.35	1.35	1.37	1.37	1.38	1.38	1.40	1.40
	EURGBP	0.89	0.88	0.91	0.88	0.89	0.87	0.87	0.88	0.88	0.90	0.90	0.91	0.91
Suiza	USDCHF	0.97	0.95	0.92	0.97	0.97	0.97	0.97	0.95	0.95	0.94	0.94	0.92	0.92
	EURCHF	1.14	1.14	1.18	1.14	1.14	1.14	1.14	1.14	1.14	1.16	1.16	1.18	1.18
América														
Canadá	USDCAD	1.28	1.25	1.25	1.25	1.28	1.28	1.27	1.26	1.25	1.25	1.22	1.22	1.25
	CADUSD	0.78	0.80	0.80	0.80	0.78	0.78	0.79	0.79	0.80	0.80	0.82	0.82	0.80
México	USDMXN	18.99	19.36	19.61	18.25	18.99	19.19	19.04	19.10	19.36	19.46	19.28	19.34	19.61
	CADMXN	14.84	15.49	15.69	14.64	14.84	14.99	14.99	15.16	15.49	15.57	15.81	15.85	15.69
Brasil	USDBRL	3.35	3.60	3.50	3.16	3.35	3.45	3.50	3.55	3.60	3.55	3.55	3.50	3.50
Chile	USDCLP	636	626	613	639	636	633	631	629	626	623	620	617	613
Colombia	USDCOP	3005	3000	3100	2938	3005	3100	3100	3050	3000	3000	3050	3100	3100
Perú	USDPEN	3.22	3.18	3.13	3.27	3.22	3.20	3.19	3.17	3.18	3.19	3.15	3.16	3.13
Asia / Pacífico														
Australia	AUDUSD	0.79	0.80	0.82	0.78	0.79	0.79	0.79	0.80	0.80	0.81	0.81	0.82	0.82
China	USDCNY	6.60	6.50	6.40	6.65	6.60	6.55	6.55	6.50	6.50	6.45	6.45	6.40	6.40
Hong Kong	USDHKD	7.82	7.79	7.78	7.81	7.82	7.80	7.80	7.79	7.79	7.78	7.78	7.78	7.78
India	USDINR	65.0	64.0	63.0	65.3	65.0	64.5	64.5	64.0	64.0	63.5	63.5	63.0	63.0
Indonesia	USDIDR	13500	13400	13300	13472	13500	13450	13450	13400	13400	13350	13350	13300	13300
Malasia	USDMYR	4.05	3.95	3.85	4.22	4.05	4.00	4.00	3.95	3.95	3.90	3.90	3.85	3.85
Nueva Zelanda	NZDUSD	0.72	0.74	0.76	0.72	0.72	0.73	0.73	0.74	0.74	0.75	0.75	0.76	0.76
Filipinas	USDPHP	51.0	50.0	49.0	50.9	51.0	50.5	50.5	50.0	50.0	49.5	49.5	49.0	49.0
Singapur	USDSGD	1.36	1.34	1.30	1.36	1.36	1.35	1.35	1.34	1.34	1.32	1.32	1.30	1.30
Corea del Sur	USDKRW	1120	1080	1040	1145	1120	1100	1100	1080	1080	1060	1060	1040	1040
Taiwán	USDTWD	30.2	30.0	29.8	30.3	30.2	30.1	30.1	30.0	30.0	29.9	29.9	29.8	29.8
Tailandia	USDTHB	32.5	32.0	31.0	33.3	32.5	32.2	32.2	32.0	32.0	31.5	31.5	31.0	31.0

r: real; p: previsión

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