FOREIGN EXCHANGE OUTLOOK

August 2003

The USD recovery will be short-lived. Weakening twin deficits and the quest for yield will prevail over growth differentials and UST refunding momentum as key drivers of foreign exchange flows.

Encouraging signs of US recovery reinforce a positive economic outlook for the NAFTA zone. Monetary easing in Canada will temper CAD attractiveness. The "carry trade" momentum and improving inflation outlook may support the MXN .

The EUR's upward trend remains intact despite fragile regional economic activity. Euro zone regulators have adopted a cautious stance towards US government agency debt. GBP stability will not be undermined by recent political events in the UK.

Asian central bank intervention remains an issue to monitor, but USD/JPY trading range is unlikely to be broken. Investors remain vigilant towards potential changes in China's currency regime.

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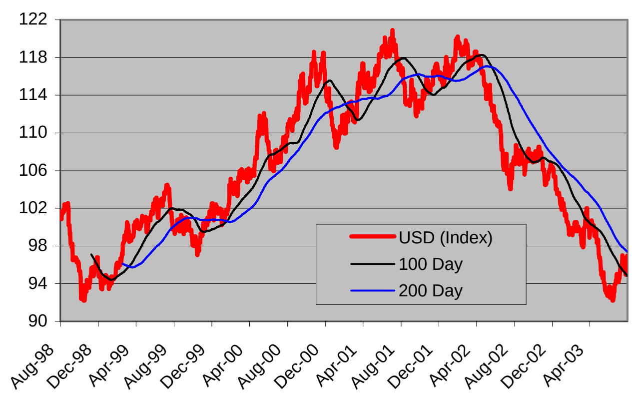
Global Foreign Exchange Outlook

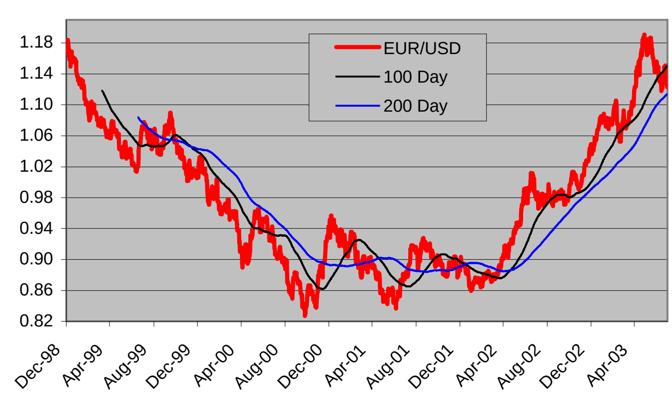
July 31, 2003		Actual	Q1 03	Q2 03	Q3 03	Q4 03	Q1 04	Q2 04	Q3 04	Q4 04
Euro	EUR/USD	1.12	1.09	1.15	1.17	1.20	1.23	1.22	1.20	1.21
	Consensus				1.15	1.16	1.16	1.17	1.16	1.16
Yen	USD/JPY	120.5	118.1	118.1	118.0	118.0	116.0	116.0	118.0	117.0
	Consensus				117.9	117.6	117.1	116.7	116.7	116.8
Sterling	GBP/USD	1.61	1.58	1.67	1.65	1.69	1.74	1.74	1.71	1.72
	Consensus				1.65	1.65	1.65	1.66	1.65	1.65
Canadian Dollar	USD/CAD	1.41	1.47	1.34	1.33	1.29	1.28	1.31	1.32	1.31
	Consensus				1.35	1.35	1.35	1.35	1.35	1.36
Australian Dollar	AUD/USD	0.65	0.60	0.68	0.66	0.68	0.70	0.72	0.70	0.71
	Consensus				0.67	0.68	0.68	0.68	0.68	0.68
Swiss Franc	EUR/CHF	1.54	1.48	1.55	1.54	1.54	1.54	1.53	1.53	1.53
	Consensus				1.55	1.56	1.56	1.56	1.55	1.55

Spot Price vs. 100 Day Moving Average vs. 200 Day Moving Average - (5yr Trend)

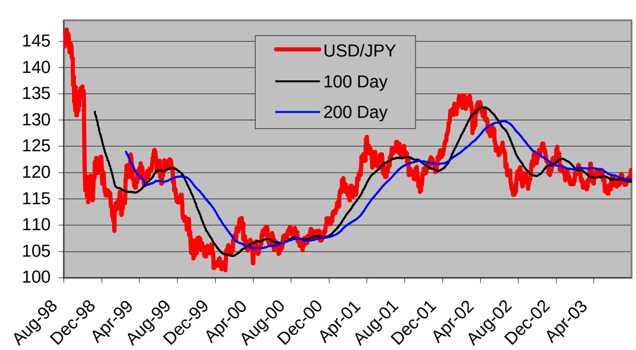
USD (Weighted Index)



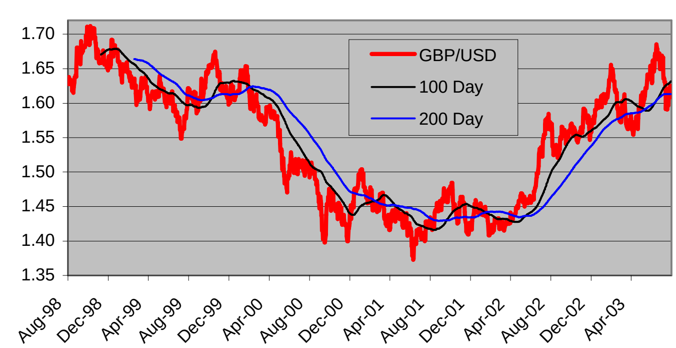
EUR/USD



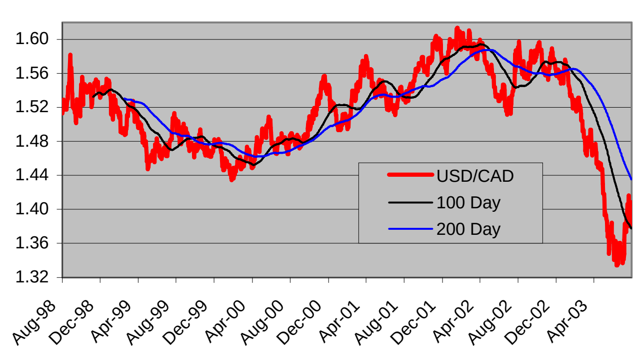
USD/JPY



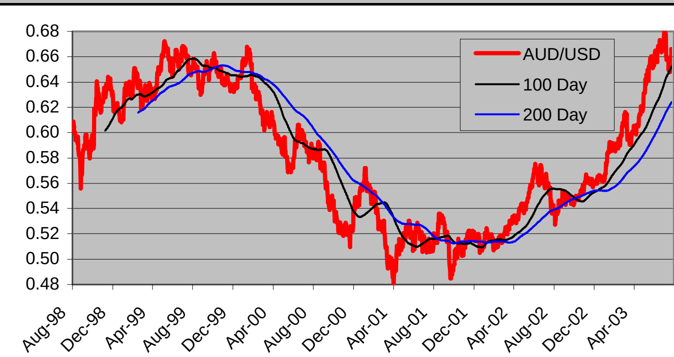
GBP/USD



USD/CAD



AUD/USD



The USD will continue to face significant headwinds in the weeks ahead despite improving economic sentiment amid aggressively pro-growth US policies. Increasing concerns about US macro-imbalances, the build-up in the supply of Treasury debt and the continued willingness of foreign government and private investors to finance the US twin deficits are overshadowing stronger growth prospects. Governance problems are adding to the pressure on the USD; the recent focus on accounting issues at government-sponsored Freddie Mac has prompted real concern (and some evidence) that foreign investors may shun what has become an increasingly favored USD-denominated investment product. With US equity valuations under scrutiny and US Treasury debt markets under pressure, foreign investors will likely adopt a cautious US investment strategy at a time when the US' reliance on foreign capital inflows continues to rise. The USD's broad valuation on foreign exchange markets will be affected adversely as a result. US Fed officials continue to focus on the positive impact of USD weakness (helps fight disinflation), while Treasury Secretary Snow remains indifferent to USD losses; this neglect may put further downside pressure on the currency.

CAD weakness, which followed last month's Bank of Canada (BoC) rate cut has stabilised. The shift to a pro-growth monetary policy amid softening domestic demand, weaker manufacturing and broad USD strength implies additional interest rate reductions from the BoC through the remainder of the year; we look for a further 75 basis points of easing. The short-term interest rate differential over the US will remain at attractive levels and lower domestic interest rates will temper the pace of the CAD rally rather than reverse it. Renewed interest in "carry trades" (long high yielding currencies, short low yielding currencies) has been evident in the past few weeks, underpinning demand for the AUD and NZD along with the CAD. AUD strength is occurring despite steady erosion in the current account. An unprecedented drop in short term interest rates in recent weeks will likely keep the MXN on the defensive in the short run while renewed USD weakness suggests potential for more downside pressure on the MXN in the longer run. Any stabilization in short-term interest rates, prompting renewed speculative MXN purchases against lower yielding currencies could provide moderate underpinning for the peso.

EUR/USD's long term upward trend is intact and a resumption of gains towards the 1.20 area and beyond is likely in the coming months. EUR/USD weakened a little more than we expected last month but there are now strong (technical) signs that the single currency set a significant low against the USD in July above 1.11. US macro-imbalances will prevail over expected growth differentials as key drivers of investment decisions in global foreign exchange markets. The European Central Bank (ECB) advised its members to sell Fannie Mae and Freddie Mac-issued debt in light of the recent accounting issues at Freddie Mac. However, the Bundesbank said it would not comply with the advice and it is unclear whether any sales resulted in repatriation or recycling into other USD-denominated assets. It remains to be seen whether the ECB easing cycle is complete; officials have remarked that interest rates are appropriate, suggesting a base at 2.00% for the key repo rate and the market has discounted the status quo. Sub-target inflation and a stronger EUR could still force the ECB's hand in the coming months.

In the UK, the political fallout from the Iraqi WMD affair continues to taint Prime Minister Blair's image although the long-term damage to his position should remain limited; historically, the Labour party tends to stick with its leaders (when in power) and Mr. Blair remains the party's strongest electoral asset. The government's recent foreign policy troubles do, however, reinforce the view that a concerted push for euro zone membership will have to be shelved for the foreseeable future, especially as popular opposition to the euro remains implacable. That may be a moderate positive for the GBP, because it removes the risk of an "engineered" decline in the currency originally linked to UK participation in the EMU. However, recent comments from Bank of England officials suggest little tolerance for GBP strength at present, so EUR/GBP weakness is likely to remain contained, limiting the scope for GBP/USD movement. In Sweden, opinion polls show strong opposition ahead of September's referendum on joining the euro.

Aggressive Bank of Japan intervention (amounting to USD75bn in the January-July period) has succeeded in stabilizing USD/JPY within its 7-month 115/125 trading range. Foreign net buying of Japanese equities in recent weeks has countered JPY selling to a degree while Japanese exporters continue to recycle receipts on any sign of USD strength. JPY repatriation ahead of the September fiscal half year-end may complicate attempts to curb JPY strength and help keep the USD capped within well-established ranges for the time being.

Developing Asian currencies remain broadly influenced by the limited range of USD/JPY, if only because competitive issues compel other major Asian central banks to mimic the Bank of Japan's currency management policy. Inflexible Asian currency arrangements - especially the CNY peg - are coming under increasing scrutiny from US lawmakers. We anticipate a moderate relaxation in the CNY peg by the end of 2004. Pressure for a revaluation based on high reserves and external surpluses may be reflected broadly across NE Asian currencies. Meanwhile, weak seasonal factors and a failed military mutiny in late July lifted USD/PHP back close to recent range extremes; however, USD/IDR rose on news that Indonesia would leave the IMF loan program, whilst remaining under Fund monitoring. The main developing Latin American currencies remain comfortably within recent ranges, though stable trading conditions may be undermined by a renewed slide in the USD or deteriorating US debt markets.

CANADA
Currency Outlook

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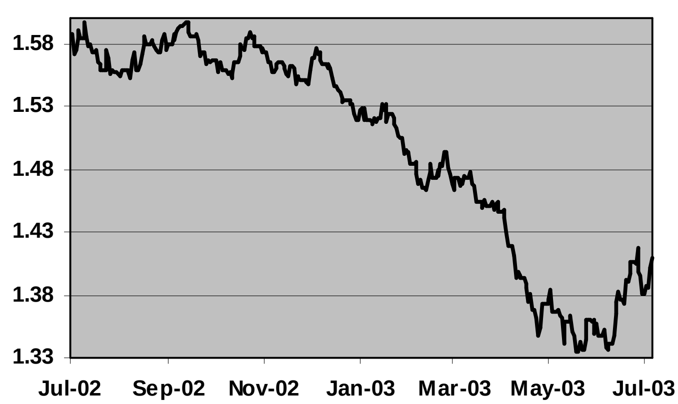
The alarmist positions taken by some market pundits and the media in the wake of the reversal in the CAD during July turned out to be misplaced. After reaching the low 1.33 area, CAD sold off back above 1.40 and reached an intraday high near 1.4190 by the third week. Some of this move was attributed to the abrupt change in policy stance by the Bank of Canada (BoC) and a rate cut that surprised most market participants. Still, the bulk of the correction was really generated by the improved tone of the US dollar. Once the shine came off the greenback towards the end of the month, the CAD started to recover lost ground. In our opinion, the central theme of the foreign exchange market this year has not changed. The cyclical correction of the US dollar will continue until there is a turnaround in the net external payments position of the US or until there is a significantly large growth divergence to cause foreign market participants to begin shifting back into US dollar assets. Until then, the outlook for CAD continues to point to a break below 1.30 before year-end. To the extent that there was a credibility (or lack thereof) element attached to the currency's sell-off after the last Bank of Canada meeting, it now seems that the focus may be swinging away from criticism over the Bank's policy initiatives earlier this year and towards whether it is now actively engaged in restoring growth. If so, that would steer the focus of the CAD market back to developments in the US and the health of US equity markets. Against the crosses, CAD performance has been mixed. We have seen a general improvement against the euro, but the four-month trend of underperformance against the Aussie dollar (AUD) has remained intact. With the BoC poised to offer as much as 75 bps of additional monetary easing relief through the balance of 2003, there is only limited potential for a significant recovery in the CAD-AUD cross.

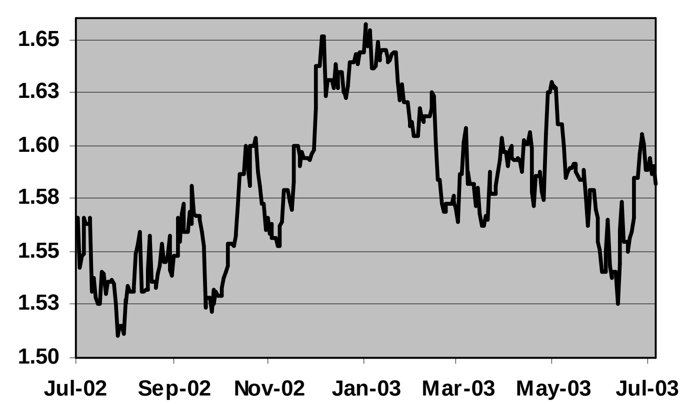
Currency Trends

FX Rate	Going Back			Spot July 31	Outlook			FX Rate
	12 m	6 m	3 m		3 m	6 m	12 m	
USD / CAD	1.584	1.517	1.442	1.409	1.317	1.287	1.313	USD / CAD
EUR / CAD	1.548	1.637	1.598	1.583	1.554	1.557	1.594	EUR / CAD
AUD / CAD	0.859	0.887	0.898	0.911	0.869	0.877	0.948	AUD / CAD
CAD / JPY	75.97	79.28	83.09	85.53	89.62	91.19	88.83	CAD / JPY

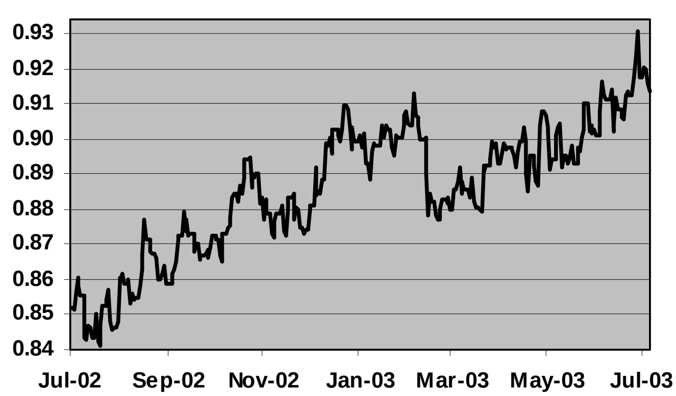
USD / CAD



EUR / CAD



AUD / CAD



CAD / JPY

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UNITED STATES - Evidence continues to point to a pick-up in the United States, with the debate now shifting as to how strong the expansion will prove. Output growth of just 1.4% in Q1 was improved upon quite handily in Q2, as real GDP advanced some 2.4%. More encouraging for the near-term is the composition of growth, with real final sales rising 3.2% and real final sales to domestic purchasers rising 4.6%. Despite a sharp trade drag and shrinking of inventories, the economy has gathered momentum through relatively strong consumption and capital spending. Sentiment is improving as measured by both manufacturing and non-manufacturing surveys; the most recent Beige Book described regional activity as "increasing a notch". Most heartening has been the drop in jobless claims below the 400k threshold for two consecutive weeks, pointing to a possible gain in jobs after five straight months of decline. Layoff statistics have also shown signs of improvement. The uptick is tenuous, and labour market sentiment remains cautious as reflected in the details of the most recent consumer confidence report. Nevertheless, with tax relief now in hand, it appears that retail spending may still be able to bridge the demand gap as capital spending begins to gear up. The Q2 national accounts release showed a robust 7.5% gain in business investment in machinery & software and new orders for core capital goods have risen 5.6% at an annual rate in the most recent three months. Inflation data remain very subdued, with the core PCE deflator advancing just 1.2% in Q2. Nevertheless, the broadest measure of labour costs remains up some 3.2% from a year-ago, suggesting deflation risks are overblown. The recent, sharp increase in bond yields has clearly led to a tightening of overall financial conditions, though not likely to a degree that threatens the recovery. Equity markets have traded sideways during most of the past two months, despite the fact that earnings for Q2 were generally better than market expectations. If evidence builds that above-potential growth is indeed on the doorstep, we would expect to see a bounce in share prices ahead.

CANADA - The most recent monthly indicators suggest the combined impact of a strong Canadian dollar and SARS/BSE will be sufficient to hold output in Q2 roughly unchanged from Q1 levels. Real GDP slipped 0.2% in April and was flat during May. Somewhat surprisingly, the weakness was not concentrated in the service sector - where the SARS effect would be most evident - but rather in the goods producing industries. Manufacturing output is down some 0.5% from a year-ago and 2.7% at an annual rate in the most recent three months. The weakness appears tied to still-soft US demand and the 12% appreciation of the Canadian dollar since the turn of the year. Final domestic demand held up well in the first quarter of the year, though there was a sharp deterioration in net exports that appears to have carried over into Q2, with the May merchandise trade surplus falling below CAD4bn for the first time since last December and only the third time since the beginning of 2000. The impact is being felt in both measured inflation and inflation expectations, with the most recent headline CPI figures for June falling to 2.6% (from a peak of 4.6% in February) and core inflation to 2.1% (from 3.3% in January). Wholesale prices are down 2.7% on a year-ago basis, the weakest in more than a decade. The disinflation has come sooner than expected by the Bank of Canada. In light of these developments and perceived slack in the economy, the Bank chose to revise down its expectations for future inflation - forecasted now to trough at some 1% in 2004 Q1. Prospects for the balance of the year remain clouded, even in the face of expected stronger US activity. Demand for key Canadian exports - notably autos and lumber - could remain soft as spending by US consumers on interest rate-sensitive products remains stretched. Canadian domestic demand may be hampered by modest employment growth - running at just 1.1% through the first six months of 2003, half the pace of the previous five years - and slumping profits tied to a strong Canadian dollar. A clear move to above-trend growth may not be evident until the first half of 2004.

MONETARY POLICY

While criticisms continue to fly over the Bank of Canada's apparent lack of transparency in its shift to an easing stance at its July meeting, there was really no policy option open to the Bank but to lower rates. The decisions to hike rates twice (by 25 bps each) earlier in the year are now viewed by the Bank as being incorrect and with growth in the economy vanishing alongside a precipitous fall in inflation, the guidance forthcoming from the Bank will be towards even lower rates. There are three more meetings left before year-end and we expect the Bank to lower rates 25bps in each of them, with a risk of more aggressive easing nearer term. If the CAD dollar extends this year's rally in the second half, the pressure on the Bank to lower rates even further will increase. The accommodative stance of the Fed is also expected to continue. In the wake of a sluggish equity market (despite decent earnings), a surprise decline in consumer confidence and sharp declines in mortgage refinancings as bond yields climb, the Fed is poised to cut its fed funds target by 25bps at the August 12th FOMC. We then expect no change in rates over the remainder of the year and no tightening for the foreseeable future.

MAJOR CURRENCIES
Currency Outlook

EURO ZONE - Tentative signs of economic recovery have helped stabilize EUR/USD around 1.12. There is still a risk of renewed weakening vis-à-vis the US dollar, although given the interest rate differential and lingering concerns regarding the US economy's external and fiscal imbalances, the bias remains in favour of EUR strength. We anticipate an end-2003 rate near 1.20.

JAPAN - The JPY is still fundamentally biased toward strengthening against the USD. Massive, recurring interventions have so far prevented any significant gains. We expect that this pattern will remain largely intact through the end of next year, although the run-up to the US presidential election in November 2004 may help to temporarily relieve some of the pressure.

SWITZERLAND - The Swiss economic recovery will lag the euro zone's less-than-stellar performance, prompting EUR/CHF to remain in the 1.53 to 1.55 range through the balance of the year. As export prospects improve going into 2004, the franc will regain some ground vis-à-vis the single currency.

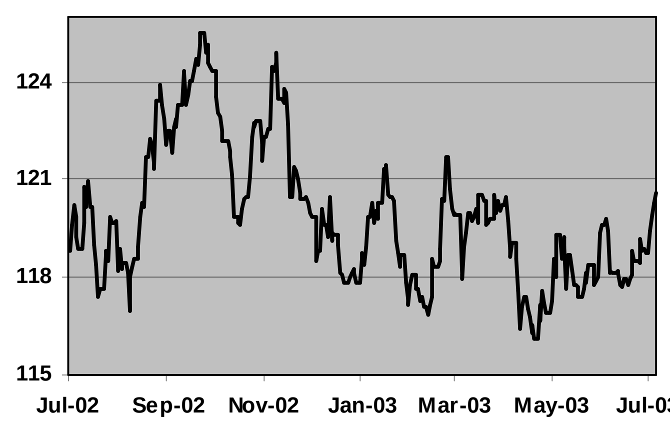
UNITED KINGDOM - The GBP surrendered most of its recent gains against the EUR following the central bank's rate cut in early July. Sterling will remain relatively stable vis-à-vis the single currency in the 0.70-0.72 range through the end of the year as the economic recovery gradually gathers pace.

Currency Trends

FX Rate	Going Back			Spot	Outlook			FX Rate
	12 m	6 m	3 m	July 31	3 m	6 m	12 m	
EUR / USD	0.978	1.080	1.108	1.124	1.180	1.210	1.213	EUR / USD
USD / JPY	119.9	120.3	119.8	120.5	118.0	117.3	116.7	USD / JPY
EUR / CHF	1.452	1.467	1.509	1.540	1.540	1.539	1.534	EUR / CHF
GBP / USD	1.564	1.644	1.595	1.609	1.663	1.707	1.730	GBP / USD

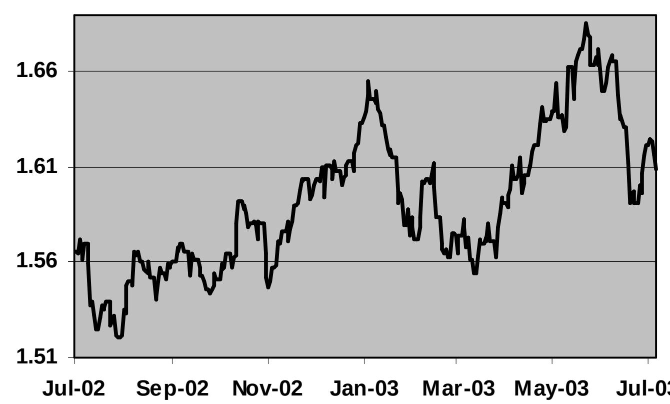
EUR / USD

USD / JPY



EUR / CHF

GBP / USD



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EURO ZONE - As was widely anticipated, the ECB held the refi rate at 2.0% at its late-July meeting; the authorities have made it clear that further easing will not soon be forthcoming. There is substantial liquidity in the system, as evidenced by rapid M3 money supply growth (8.3% in June), and the euro has fallen from its end-May high of 1.19, providing some justification for holding steady and assessing the impact of June's 50 bps cut. July's consumer and business confidence surveys suggest that market actors remain uncertain regarding the pace, strength and timing of the eventual economic recovery. The uptick in real wages derived from slowing inflation, coupled with equity market gains and lower interest rates should give a boost to consumer optimism; however, the national indices have been uninspiring. Companies, meanwhile, are loath to expand production given the dim economic outlook. The closely-followed Ifo index rose to a one-year high in July; however, the fact that the index has gained only five basis points in three consecutive monthly increases hints that the recovery, while under way is fragile. The euro zone industrial sector remains weak - factory output slipped 0.9% m/m in May, while in June the Purchasing Managers' Index fell to its lowest level in 17 months. Moreover, the euro's strength through the first half of the year is hurting the zone's external balances. The May trade surplus narrowed to EUR4.3 billion, versus EUR8.8 billion a year earlier.

JAPAN - Japan's balance of payments data suggest that there is scope for JPY appreciation. The May current account surplus was a record JPY1.56 trillion (USD13.3 billion) as merchandise export receipts jumped 4.2% m/m, while imports were virtually unchanged from the previous month. In addition, net investment income receipts continued to grow - to JPY747 billion in May, pushing the cumulative total through the first five months of the year to JPY3.38 trillion. Core machinery orders rose 6.5% m/m in May, the second increase in the three months. The June Tankan survey had pointed to a recovery in capital expenditures among manufacturers alongside an uptick in profits and the machinery orders data reinforce that view. The pickup in demand for production equipment suggests that manufacturers believe that the 1.2% m/m drop in industrial output in June - the second decline in the past three months - was not indicative of a more protracted slide in demand. Consumer prices have been stable through 2003. Fears of chronic deflation in Japan have been exaggerated; we believe that price trends have, in fact, been beneficial for the hard-pressed consumer, a view that finds some support in the most recent official quarterly survey on consumer sentiment. Respondents indicated a greater willingness to undertake major purchases and were somewhat more upbeat about job prospects than had been the case in the first quarter of 2003.

SWITZERLAND - The government's chief economist has admitted that Swiss output may decline this year, particularly as the prospects for Germany, the country's main trading partner, are dim. Moreover, the KOF leading indicator fell to a fresh 6½-year low in June. The industrial sector remains weak: June's Purchasing Managers' Index contracted for a seventh consecutive month, as output, orders and inventories all fell. The continuing backslide in orders suggests that the economy will stumble along through to at least Q4. Retail sales rose for the first time in six months in April, gaining an inflation-adjusted 0.4% y/y. This is not a sign of a turnaround - it likely has more to do with the Easter holidays (food and drink sales were up 9.1%). The underlying data reveal a sustained retreat in big-ticket purchases such as cars and furniture, as consumers remain hesitant to spend in the face of rising joblessness. The unemployment rate climbed for a third consecutive month in June, reaching 3.8%. Finally, in the same month, the external sector continued to struggle - real imports fell 6.8% y/y, while real exports slipped only 1.5%. Economic weakness is undermining the public balance sheet: income tax revenues fell short of government expectations in the first half of the year, implying a wider than forecast budget deficit. Spending cuts, aimed at fulfilling the balanced budget obligation enshrined in the constitution will likely pare growth rates and lead to higher unemployment.

UNITED KINGDOM - The economy expanded 0.3% q/q in Q2, a slight pickup from the previous quarter's 0.1% rate. The outlook, however, does not suggest a rapid acceleration, making the budget's 2-2½% growth forecast for this year appear increasingly unreachable. Factory orders buckled in July, manufacturing output shrank again in May and foreign demand remains weak. However, rising retail sales (1.9% m/m in June) and strengthening consumer confidence suggest that household spending continues to carry the baton as industry wallows. The Bank of England (BoE) cut the benchmark repo rate 25 bps to 3.5% in July, triggered by weaker than anticipated external demand, below-trend domestic output and the expectation that price pressures will cool. The inflation rate slipped to 2.8% in June, down from 2.9% in May but still a third of a percentage point above the Bank's 2½% target. However, according to EU harmonized standards (which the BoE will adopt next year), June's rate came to 1.1% - one of the lowest in Europe. Stable employment conditions - the jobless rate remains at 3.1% - coupled with half-century low interest rates are fueling a borrowing boom; net consumer credit and mortgage lending both grew by record-setting amounts in June. These two trends - rapid credit growth versus cooling inflationary pressures - combined with the recent precautionary ease imply the Bank will likely hold steady following its August 6-7 meeting, despite relatively weak signals from the real economy.

NON-MAJOR CURRENCIES
Currency Outlook

AUSTRALIA - The AUD will remain biased towards strengthening as substantial, positive interest rate spreads and strong government finances will continue to offset the impact of large current account deficits. The combination of a renewed EUR rally and a recovery in commodity prices will also be AUD-supportive.

NEW ZEALAND - Interest rate reductions in New Zealand should help to limit the risk of excessive NZD appreciation. Nevertheless, spreads remain substantial; as a result, we anticipate additional moderate gains for the NZD through the balance of 2003 alongside a renewed, broadly based sell-off of the USD.

SINGAPORE - The policy stance of the Monetary Authority of Singapore (MAS) of offering economic relief through direct exchange rate management rather than through lower interest rates will limit the likelihood of substantial changes in USD/SGD through the balance of the year. However, since the MAS focuses on the nominal effective exchange rate, some moderate SGD appreciation vis-à-vis the USD is compatible with the current policy stance.

SWEDEN - Opposition to the EUR remains strong in the run-up to the September 14 referendum. As a result, EUR/SEK will continue to trade above 9.1 despite Sweden's current account surplus, more favourable economic performance and positive (albeit narrowing) interest rate differential. A 'no' decision could prompt short-term SEK losses, though the market may already have priced-in such an outcome.

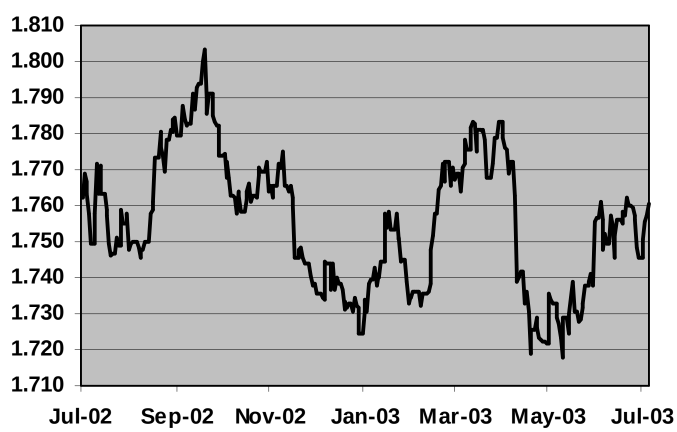
Currency Trends

FX Rate	Going Back			Spot July 31	Outlook			FX Rate
	12 m	6 m	3 m		3 m	6 m	12 m	
AUD / USD	0.54	0.59	0.62	0.65	0.66	0.68	0.72	AUD / USD
NZD / USD	0.47	0.54	0.56	0.58	0.60	0.61	0.60	NZD / USD
USD / SGD	1.76	1.74	1.78	1.76	1.73	1.71	1.72	USD / SGD
EUR / SEK	9.26	9.23	9.12	9.23	9.15	9.09	9.04	EUR / SEK

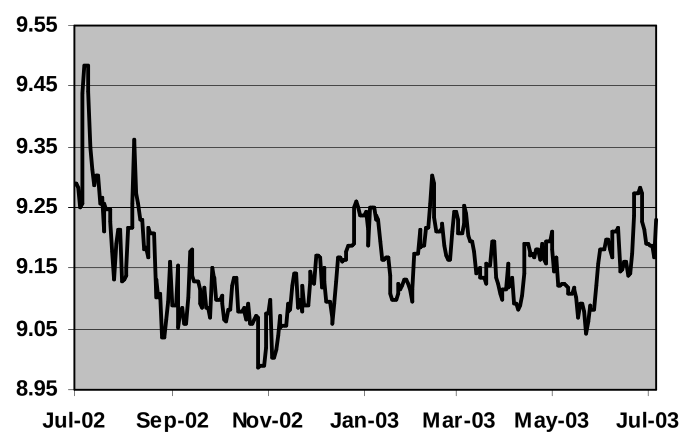
AUD / USD

NZD / USD

USD / SGD



EUR / SEK



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AUSTRALIA - Business and consumer confidence are on the mend. Business sentiment strengthened considerably in June, according to NAB's monthly survey, although respondents reported only a modest improvement in current conditions, with significant variation among sectors. Firms exposed to international competition continue to be squeezed by the impact of Australian dollar appreciation while companies focused on the domestic market (including wholesale and retail trade, recreation and construction) report a favourable environment. In addition, the Westpac/Melbourne Institute index of consumer confidence reached a 9-year high of 115.3 in June. The more upbeat sentiment came despite some deterioration in labour market conditions. Total employment fell by 28,000 in June, with full-time job losses totaling 54,000; the unemployment rate increased a notch to 6.1%. In view of the generally positive forward-looking indicators, we believe that the Reserve Bank will hold its benchmark rate steady at 4.75% following its August 5th meeting despite the fact that price pressures came to an abrupt halt in Q2. The consumer price index was unchanged from the previous quarter, though it was still up 2.7% from a year earlier. A break in the drought nudged food costs lower while the strength of the Australian dollar contributed to a near-10% weakening in gasoline prices and a slight drop in motor vehicle prices. However, a 2% q/q rise in housing prices took some of the gloss off the benign headline CPI.

NEW ZEALAND - The Reserve Bank reduced its official cash rate a further 25 bps to 5.0% in late-July - the third such cut in three months. In announcing the central bank's decision, Governor Bollard noted some "slowing in economic activity [he cited the export sector in particular] and inflation in some parts of the economy". At the same time, "activity in a number of domestic industries, such as housing and construction, remains robust throughout much of the country". Looking ahead, Governor Bollard emphasized that the monetary authorities would be paying particular attention to exports and to housing prices as they consider whether additional interest rate relief is required. Apart from the housing component, inflation measures are generally encouraging: consumer prices were unchanged in Q2 and up only 1.5% from a year earlier - in the lower half of the central bank's 1-3% target range. Figures released after the central bank's decision revealed that export receipts plunged almost 18% (not seasonally adjusted) in June, pushing the trade deficit to a 10-year high of NZD230 million. The most current data suggest that conditions remain mildly positive. Tourism is recovering, as waning SARS fears have triggered a pick-up in air travel throughout the Pacific region. In addition, there are signs that labour demand may be solidifying: June job advertisements rose 5.6% m/m, more than reversing the previous month's 2.8% decline.

SINGAPORE - Preliminary second quarter GDP data revealed a SARS-driven 12% q/q (annualized) contraction in economic activity; output was down 4.3% from Q2 2002. Monthly data indicate a more promising outlook. Retail spending staged an impressive rebound in May, jumping 11.8% m/m after a SARS-related 5.2% decline the previous month. In addition, exports rallied in June, jumping 18.7% y/y, following single-digit increases in the previous two months. The acceleration in foreign shipments will boost industrial activity and, with SARS fears abating, a pickup in tourism should give a further fillip to such labour-intensive sectors as hotels and restaurants as well as to the retail trade. Manufacturing output rose 2.0% m/m in June, the first advance in three months; nevertheless, production languished 7.3% below the year earlier level. Aggressive retail sales promotions in the aftermath of the lifting of SARS warnings by the World Health Organization helped to push the CPI lower. Consumer prices in Singapore were below year-earlier levels for a second consecutive month in June, slipping 0.3% y/y following a 0.1% decline in May. Deflationary impulses are unlikely to become chronic. Domestic demand will gradually recover through the balance of 2003, setting the stage for marginal GDP growth this year, while a pickup in overseas activity in 2004 should help push output up 4% next year - too strong a pace for deflation to persist.

SWEDEN - On the eve of the September 14 referendum on European Monetary Union (EMU), the tide remains against the pro-euro camp. The government is struggling to convince the electorate to abandon the krona; the 'no' camp leads by an average of 13 percentage points according to the three most recent polls. There is a substantial, albeit narrowing number of undecided voters; however, recent events - the single currency's endorsement by labour union LO and the discrediting of a leading 'no' campaigner - have not triggered a significant uptick in support. Sweden's more promising economic outlook and lower unemployment rate are prompting voters to question the benefits of monetary union. The central bank made a precautionary 25 basis point cut in its benchmark rate, reducing borrowing costs to 2.75%. The authorities cited cooling inflationary expectations and lingering excess capacity as reasons for the ease, although the statement also highlighted the lack of "any decisive revision to the risk spectrum" since June, when the monetary authorities cut 50 bps. The central bank expects the inflation rate to fall to 1.1% in a year's time - well below its 2.0% target. Although price trends were the main factor in the decision, weak growth in the euro area and rising joblessness (the rate touched a five-month high of 4.8% in June) also contributed. Manufacturing continues to mirror the wider European trend, slipping 1.8% m/m in May - a 5.0% dip in orders does not bode well for future activity.

CHILE - The Chilean peso (CLP) may be subject to abrupt gyrations on the back of expected BRL depreciation, commodity market adjustments and unattractive interest rates. The US lower house approval of the US-Chile free trade agreement is a supportive long-term factor favouring the South American economy. The 5-month technical correlation with the AUD and the CAD suggest a broad proxy for CLP trends in the near future.

CHINA - Pressures on Beijing to adjust its exchange rate policy are building. We believe that a modest widening of the official trading range will be countenanced in 2004. For the balance of this year, however, the authorities will likely continue their heavy intervention. To dampen the pressures, Beijing has eased restrictions on chinese offshore portfolio investment; measures to stem short-term capital inflows may follow.

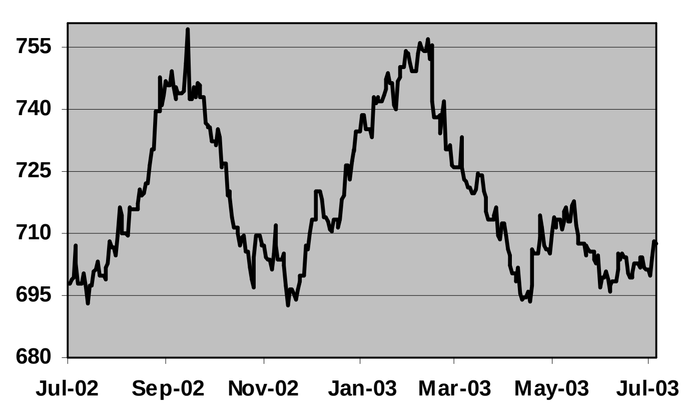
MEXICO - The Mexican peso (MXN) remains well supported by declining inflation and interest rate prospects but is still vulnerable to a sharp weakening of the USD. The July congressional elections reaffirmed the market view that Banco de Mexico's leadership -and its stringent commitment to fight inflation- may not be altered any time soon. Currency stability, foreign ownership of domestic banks and an increasing supply of MXN-denominated securities are also MXN supportive.

SOUTH KOREA - Recurring interventions to stem KRW appreciation vis-à-vis the USD pushed foreign currency reserves to a record USD132 billion at end-June. We expect this pattern to continue as the Korean authorities attempt to ensure that the KRW does not move out of line with other Asian currencies.

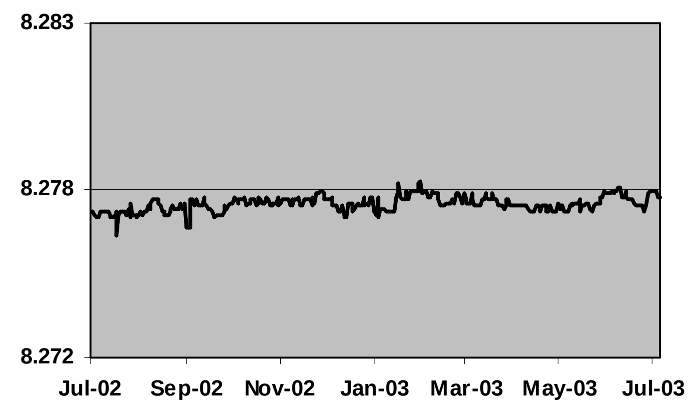
Currency Trends

FX Rate	Going Back			Spot July 31	Outlook			FX Rate
	12 m	6 m	3 m		3 m	6 m	12 m	
USD / CLP	707	734	706	708	709	711	716	USD / CLP
USD / CNY	8.3	8.3	8.3	8.3	8.3	8.3	8.3	USD / CNY
USD / MXN	9.87	10.90	10.29	10.58	10.86	11.08	11.25	USD / MXN
USD / KRW	1,188	1,180	1,218	1,180	1,188	1,203	1,196	USD / KRW

USD / CLP

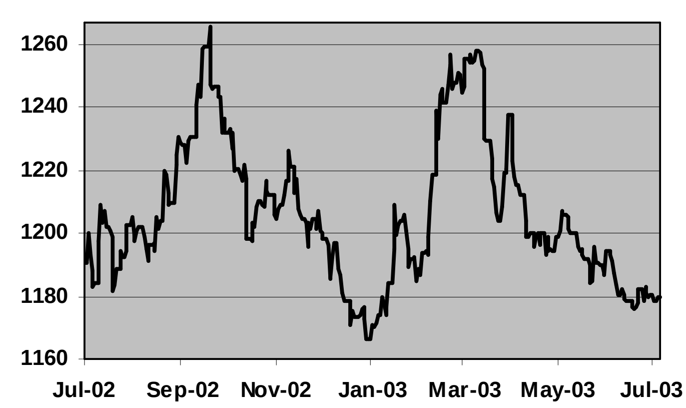


USD / CNY



USD / MXN

USD / KRW



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CHILE - External factors continue to be the major drivers of CLP performance. While the US lower house's approval of the free trade deal is a positive long-term event, the market appears more sensitive to the commodity market cycle and interest rate differentials. After the resurgence of an upward commodity price trend in April-May, copper prices have adjusted to lower levels. It is interesting to note the correlation amongst the commodity-sensitive currencies (AUD, CAD and CLP) over the past five months as a gauge of future CLP moves through the rest of the year. Another factor beyond Chile's control is the direction that the BRL may take in the near future. Interest rate forward markets discount a weakening trend for the Brazilian currency, suggesting a potential negative impact on the CLP. Given that economic growth projections continue to be revised downwards, the savvy leadership at the Chilean central bank may opt to maintain an aggressively stimulative monetary stance, encouraging local investors to look elsewhere in search of higher yields. Since early January, the administered monetary policy interest rate has been kept at 2.75%. Consumer price inflation was 1.6% during the first half of 2003, well in line with the official target. The maintenance of a pro-growth monetary policy will be needed to achieve a below-potential 3-4% rise in GDP in 2003. The government is quite confident that growth will accelerate in 2004.

CHINA - China's export machine is the most dynamic in the world. Foreign sales have been growing at an annual rate of more than 30% over the past year, raising complaints in Japan, Europe and the United States that Beijing is keeping the yuan artificially weak. Other emerging East Asian countries have been more circumspect - in part because the majority are generating trade surpluses vis-à-vis China. In mid-July, Fed Chairman Alan Greenspan added his voice to calls for a policy change. In testimony before the Senate, he warned that Beijing's ongoing, heavy intervention would create unmanageable pressures on China's monetary system. The Chinese authorities quickly responded that the current policy would remain in place, though there were also hints of some willingness to consider greater flexibility. We believe that the authorities will permit some modest de facto appreciation of the currency vis-à-vis the US dollar in 2004. With the United States already running a USD100 billion-plus bilateral trade deficit with China and job losses expected to mount in the US textiles industry following the expiration of quotas on imports from China at end-2004 (just after the US presidential election), the exchange rate policy issue will become increasingly politically charged in the months ahead. Four US Senators recently appealed to Treasury Secretary Snow to determine whether China's exchange rate policy violates WTO or IMF commitments.

MEXICO - The technical decoupling of the MXN from USD has been in place since April, coinciding with the introduction of daily USD auctions by Banco de México. Although market participants do not expect a MXN-USD realignment any time soon, it would be naive to affirm that the MXN will remain indifferent to a sharp deterioration in the USD. Some analysts have interpreted the reduction of daily USD sales from USD32 million to USD14 million as a MXN negative factor. On a very positive note, the steady improvement in inflation expectations has contributed to a reduction in the perceived overvaluation of Mexico's real exchange rate. The money market benchmark 28-day Cete rate reached an all-time low level of 4.18% at the end of July. The fact that the currency remained relatively stable within an established trading range while domestic interest rates continued to decline over the past two months reinforces the notion of MXN decoupling. The PRI-friendly outcome of the July 6th vote also strengthened the likelihood of Guillermo Ortiz' re-appointment as Governor of the Banco de México. Ortiz' decisive drive to bring Mexican inflation to US levels and MXN-sensitive oil export revenue bode well for further monetary easing in the months to come to revive economic activity. The increasing demand for MXN-denominated securities by resident long-term institutional investors also contributes to an overall MXN-positive tone as México benefits from the "carry-trade momentum" in place in North America.

SOUTH KOREA - Korean exports increased a solid 22% y/y in June, in line with the average gains through the first five months of the year. With oil prices stabilizing, imports were up by 13%, double the pace of May, but still far short of the 31% increase in Q1. The Bank of Korea (BoK) lowered its benchmark overnight call rate 25 bps to a record-low 3.75% in July. Governor Park had earlier indicated that he would be prepared to reduce rates should it appear that economic growth in 2003 might fall short of the central bank's 4.1% projection; in July, the BoK reduced its forecast to 3.1%. The revision followed the release of the first official estimate for Q2, which pointed to a 0.7% q/q drop in output, following a 0.4% decline in Q1; the contraction through the first half of the year was largely the result of an officially mandated reversal of the 2002 credit-driven consumer boom. Moreover, the June jobless rate rose 0.2 percentage points to 3.6%, further dampening spending activity. A robust 4.7% m/m surge in industrial output in June together with further easing in the central bank's monetary stance and a recently-implemented array of tax incentives, may offer some much-needed stimulus to both private sector labour demand and to business investment; however, in the very near term, the outlook for domestic spending will depend heavily on government outlays and on exports.

Developing Markets (speculative grade)

Currency Outlook

ARGENTINA - The moderate reduction in the trade surplus in Q3, alongside the very low levels of domestic interest rates, reversed the peso's appreciation trend. News regarding the negotiations with the IMF could precipitate additional movements in the currency, but the most probable scenario, where a "limited" agreement is reached, will trigger a gradual peso decline with sporadic recoveries.

BRAZIL - The Brazilian real (BRL) is poised for steady weakening on the back of profit taking after a sharp rally, accelerating monetary easing, domestic political uncertainties and USD swings. The local market are discounting further short-term interest rate cuts as inflationary pressures continue to recede. The government's intent to ease the banking sector's reserve requirements will be used to spur credit-sensitive economic growth that has entered negative territory.

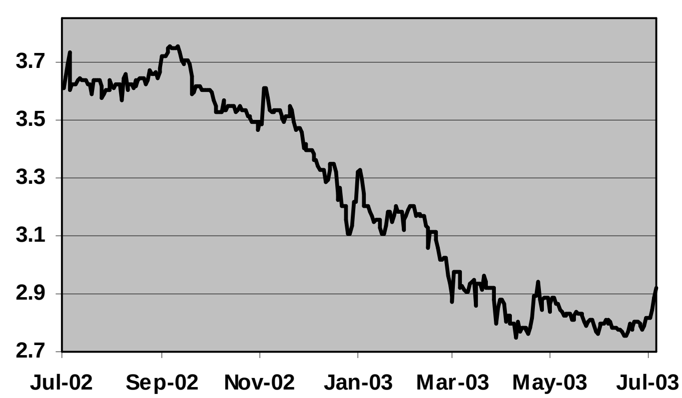
INDIA - The 14-month INR rally has become more volatile. Though the pace of appreciation has quickened since mid-March 2003, there have also been sharper sell-offs. The more upbeat near-term economic prospects may continue to overshadow concerns regarding a worsening public sector balance sheet, pointing to further, temporary INR gains.

VENEZUELA - Oil production is recovering and foreign currency reserves are being replenished; as a result, speculation has arisen regarding the fixed exchange rate system, which was implemented in January, shortly before the harsh and economically damaging (particularly to the export sector) capital controls. It is likely that the government will alter the exchange rate regime, possibly by introducing a dual exchange rate in order to bolster the economic recovery.

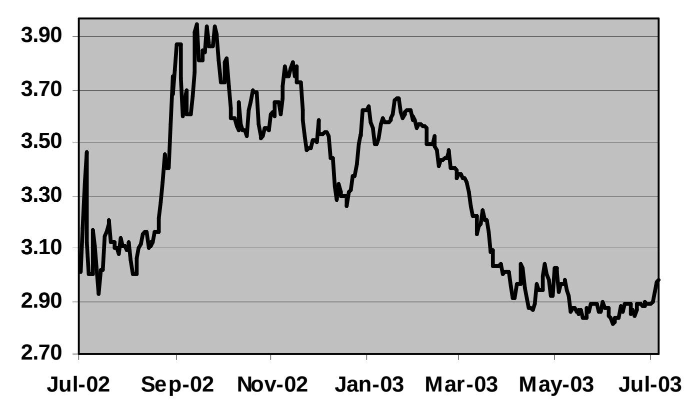
Currency Trends

FX Rate	Going Back			Spot	Outlook			FX Rate
	12 m	6 m	3 m	July 31	3 m	6 m	12 m	
USD / ARS	3.73	3.19	2.81	2.92	3.03	3.11	3.19	USD / ARS
USD / BRL	3.46	3.52	2.91	2.98	3.14	3.27	3.39	USD / BRL
USD / INR	48.7	47.8	47.4	46.1	46.1	46.2	47.2	USD / INR
USD / VEB	1,347	1,922	1,598	1,598	1,936	2,238	2,479	USD / VEB

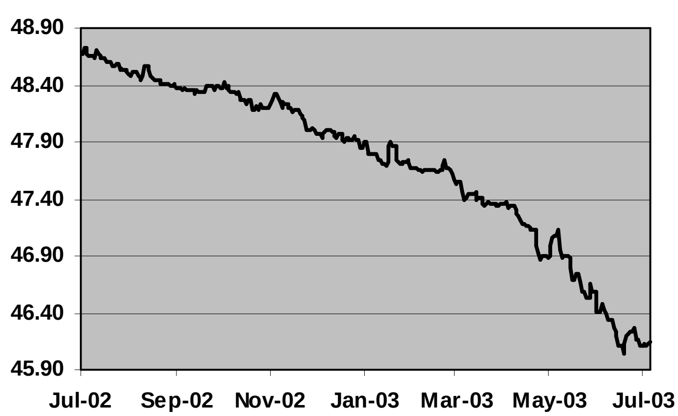
USD / ARS



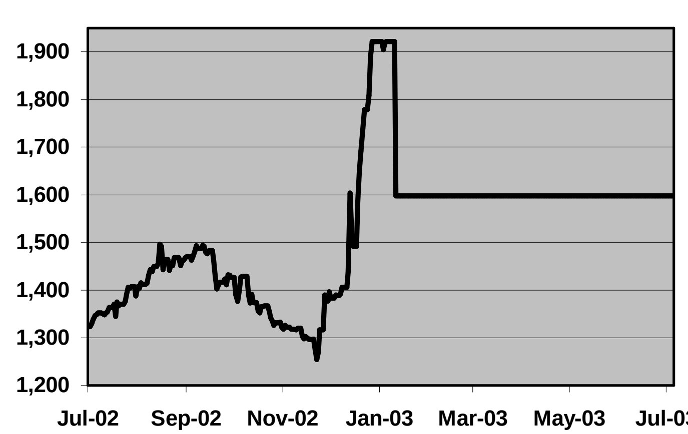
USD / BRL



USD / INR



USD / VEB



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ARGENTINA - As expected, the pace of the strong economic recovery has moderated in the past few weeks; however, growth will likely surpass 5% this year due to the "statistical rebound" effect. This is a clear signal that the government needs to implement the much-needed structural reforms required to place Argentina on a sustainable economic growth path. Following the controversial attitude demonstrated during his recent trip to Europe, President Kirchner adopted a more pragmatic approach during his visit with George Bush, who in turn leant his support to negotiations with the IMF. Though the medium-term accord with the Fund would be mutually beneficial for all parties involved, the negotiations will likely remain contentious, as opposing viewpoints in critical matters remain present. The areas of dissent include changes to the financial system, the inter-provincial revenue-sharing scheme and the size of the primary surplus, along with a variety of other complex structural reforms that must be included in the accord. The IMF has been under pressure to reach a final accord before the September 9th payment deadline, but it is likely that the aggressive nature of Argentina will continue to hinder negotiations. A possible solution would be a middle-of-the-road agreement in which the goal of implementing structural reforms is not entirely achieved, but is sufficient to entice global creditors to adopt a more collaborative approach during the tough negotiations in the months ahead.

BRAZIL - The Brazilian central bank has entered a phase of monetary easing. Following the 150 basis point reduction in the monetary target SELIC rate to 24.5%, local market participants are positioned for further and deeper cuts; the short-term interest rate may end the year as low as 21%. The intensive period of congressional activity associated with the debate on reforms to the social security, tax and bankruptcy legislation has created additional, albeit understandable, tension amongst market participants reflected in lower BRL levels. While the USD has received short-term support on the grounds of massive (refunding) debt issuance, the deterioration of US macroeconomic imbalances may translate into further USD selling through the rest of the year, with negative consequences for the BRL. At the time of writing, one-year non-deliverable forward markets were pricing a USD/BRL rate of 3.54, implying a 16% currency depreciation from current levels. It is worth noting that part of this adjustment could be attributed to profit taking activity after a sharp 30% appreciation between February and July of this year. The exchange rate has been indifferent to the sovereign debt buyback completed at the end of July and is more focused on expectations for inflation and interest rate declines. The inflation front has sharply improved. Single-digit inflation by the end of the year cannot be ruled out, an impressive adjustment from the 15% plus pace through the first half of 2003.

INDIA - The cyclical recovery appears well entrenched and the return of the monsoons - rainfall this summer has been above-average - will help to solidify these gains. GDP rose 4.9% y/y in the first quarter of 2003, a significant improvement over the drought-constrained 2.6% advance the previous quarter. Growth will likely continue to accelerate through the balance of the year; the favourable monsoons have encouraging implications for consumer spending and rural investment. Indian industrial production rose an unexceptional, though still solid 5.7% y/y in May; manufacturing output strengthened 6.1%. The marked increase in rainfall from a year ago will also permit the rebuilding of water supplies held in reservoirs, a development that may slightly reduce power shortages around the country. India's recent trade figures have also been positive. Exports staged an encouraging recovery in May, increasing by 14% y/y to USD4.5 billion, following a 9% rise the previous month. Unfortunately, there has been little progress in addressing the country's underlying structural problems. Finance Minister Singh has conceded that the deficit is a "cause for concern", but there are no credible plans for corrective action. Indeed, fiscal problems may get worse. In mid-July, Prime Minister Vajpayee announced plans to provide a guaranteed 9% rate of return on pension savings; by comparison, the 10-year government bond yield is currently less than 6% and the inflation rate is less than 5%.

VENEZUELA - After an unprecedented 29% y/y decline in GDP in Q1, the economy is rebounding. The government has overcome some of the critical economic challenges that it has faced since the beginning of the year. Oil production is recovering and the government managed to cut costs in order to compensate for the fall in revenues. The financial system has rolled over the maturing internal public debt and a successful external debt swap was executed. Higher oil revenues reduce currency depreciation expectations and foreign exchange controls are allowing a substantial recovery in international reserves, dispelling fears of an imminent default on external debt. This seems to have been recognized by the rating agencies, as Fitch upgraded Venezuela's rating in late June, followed by S&P on July 30. The increase in reserves, however, is mainly derived from the government's refusal to sell foreign currency to importers, leading to a collapse in this sector. This in turn has led to a substantial decline in non-oil activity. The "normalization" of import activity is essential for the economy to grow. Political conditions remain volatile, with recurring demonstrations and clashes between government supporters and opposition sympathizers regarding the unresolved issue of the referendum on President Chávez's tenure. Longer term, the possibility of achieving a higher, sustainable rate of growth in Venezuela is remote without a solution to the deep institutional crisis.

GLOBAL CURRENCY OUTLOOK (end of period)

August 2003

		2001	2002	2003f	2004f	2003f Q1a	2003f Q2a	2003f Q3	2003f Q4	2004f Q1	2004f Q2	2004f Q3	2004f Q4
MAJOR CURRENCIES													
Japan	USD / JPY	131	119	118	117	118	118	118	118	116	116	118	117
Euro zone	EUR / USD	0.89	1.05	1.20	1.21	1.09	1.15	1.17	1.20	1.23	1.22	1.20	1.21
	EUR / JPY	116	125	142	142	129	136	138	142	143	142	142	142
UK	GBP / USD	1.45	1.61	1.69	1.72	1.58	1.67	1.65	1.69	1.74	1.74	1.71	1.72
	EUR / GBP	0.61	0.65	0.71	0.70	0.69	0.69	0.71	0.71	0.71	0.70	0.70	0.70
Switzerland	USD / CHF	1.67	1.38	1.28	1.26	1.35	1.34	1.32	1.28	1.25	1.26	1.28	1.26
	EUR / CHF	1.48	1.45	1.54	1.53	1.48	1.55	1.54	1.54	1.54	1.53	1.53	1.53
CANADA													
	USD / CAD	1.59	1.57	1.29	1.31	1.47	1.34	1.33	1.29	1.28	1.31	1.32	1.31
	CAD / USD	0.629	0.636	0.775	0.763	0.682	0.748	0.752	0.775	0.781	0.763	0.758	0.763
	EUR / CAD	1.41	1.65	1.55	1.59	1.60	1.54	1.56	1.55	1.57	1.60	1.58	1.59
	AUD / CAD	0.81	0.88	0.88	0.93	0.89	0.91	0.88	0.88	0.90	0.94	0.92	0.93
	CAD / JPY	82.4	75.6	91.5	89.3	80.5	88.3	88.7	91.5	90.6	88.5	89.4	89.3
DEVELOPED MARKETS (Non-Major Currencies)													
Australia	AUD / USD	0.51	0.56	0.68	0.71	0.60	0.68	0.66	0.68	0.70	0.72	0.70	0.71
New Zealand	NZD / USD	0.42	0.52	0.61	0.60	0.56	0.60	0.59	0.61	0.61	0.60	0.60	0.60
Singapore	USD / SGD	1.85	1.73	1.73	1.72	1.76	1.75	1.75	1.73	1.73	1.72	1.72	1.72
Sweden	EUR / SEK	9.30	9.12	9.10	9.00	9.22	9.18	9.18	9.10	9.07	9.05	9.02	9.00
Taiwan	USD / TWD	35.1	34.6	34.0	34.5	34.7	34.5	34.2	34.0	34.1	34.2	34.4	34.5
DEVELOPING MARKETS (Investment Grade)													
Chile	USD / CLP	661	720	710	720	733	696	709	710	712	715	717	720
China	USD / CNY	8.28	8.28	8.28	8.25	8.28	8.28	8.28	8.28	8.27	8.26	8.26	8.25
Hong Kong	USD / HKD	7.80	7.80	7.80	7.80	7.80	7.80	7.80	7.80	7.80	7.80	7.80	7.80
Malaysia	USD / MYR	3.80	3.80	3.80	3.75	3.80	3.80	3.80	3.80	3.79	3.77	3.76	3.75
Mexico	USD / MXN	9.18	10.37	11.05	11.39	10.77	10.52	10.76	11.05	11.13	11.22	11.30	11.39
South Africa	USD / ZAR	11.98	8.57	8.70	10.00	7.87	7.46	7.88	8.70	9.01	9.33	9.66	10.00
South Korea	USD / KRW	1,323	1,186	1,210	1,199	1,254	1,187	1,177	1,210	1,189	1,189	1,210	1,199
Thailand	USD / THB	44.2	43.1	42.0	43.0	42.8	41.9	41.8	42.0	42.2	42.5	42.7	43.0
DEVELOPING MARKETS (Speculative Grade)													
Argentina	USD / ARS	1.00	3.36	3.10	3.25	2.97	2.81	2.99	3.10	3.14	3.17	3.21	3.25
Brazil	USD / BRL	2.31	3.54	3.25	3.50	3.35	2.82	3.09	3.25	3.31	3.37	3.44	3.50
India	USD / INR	48.3	48.0	46.0	48.0	47.5	46.4	46.1	46.0	46.5	47.0	47.5	48.0
Indonesia 1/	USD / IDR	10.48	8.95	9.00	10.00	8.90	8.22	8.70	9.00	9.2	9.5	9.7	10.0
Turkey 1/	USD / TRL	1,449	1,655	1,750	2,400	1,714	1,402	1,549	1,750	1,894	2,049	2,218	2,400
Venezuela	USD / VEB	767	1,389	2,200	2,700	1,598	1,598	1,816	2,200	2,316	2,437	2,565	2,700

a: actual; f: forecast; 1/ In thousands

SCOTIA ECONOMICS

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