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Global Economic Outlook: Macro Backdrop Remains Positive with Growth Improving, Interest Rate & Liquidity Tailwinds. Eurozone Periphery Recession Remains a Drag

John Praveen's Global Economic Outlook – May/June 2012 – sees the global macro backdrop remaining favorable for equity markets with GDP growth improving, interest rate and liquidity tails winds and benign inflation. GDP growth continues to improve in the U.S., Japan and core Eurozone, especially Germany. However, Eurozone periphery remains in recession. GDP growth in emerging economies is expected to bottom in Q1 and improve in Q2 in response to interest rate cuts. Stocks continue to be supported by interest rate and liquidity tailwinds. Developed central banks are in pause mode after earlier easing measures, but have left the door open to further liquidity measures and QE expansion. Emerging central banks continue to ease policy/cut rates with India starting rate cuts, while Brazil cut rates for the sixth time. China cut the reserve ratio in May and is on track to ease policy further.

Developed Economies GDP Growth: U.S. Q1 GDP Growth Disappoints, but Economy Remains on Moderate Growth Path. Strong Q1 Rebound in Japan. Germany Lifts Eurozone Q1 GDP. Core Eurozone Stabilizing, Periphery in Recession

- **Global GDP growth is improving modestly in H1 2012 with Japan posting a strong Q1 rebound and likely to post solid growth in Q2. While U.S. Q1 growth disappointed, GDP growth is expected to be solid in Q2 with support from consumption and business investment spending. Eurozone avoided a technical recession with Q1 GDP edging up 0.1% led by an upside surprise in Germany. However, the periphery remains in recession.**
- **The U.S. economy disappointed in Q1 2012 with GDP growth of just 2.2% QoQ annualized, well below expectations of 2.7% and slowing from the 3% pace in Q4 2011.** On an annual basis, GDP rose 2.1% YoY after 1.6% in Q4. Within GDP, there was a solid gain in consumer spending (2.9%), while business investment spending (-2.1%) and government spending (-3%) were weak. U.S. consumer spending added 2% to Q1 GDP growth while government spending subtracted -0.6% and business investment subtracted -0.2% from Q1 growth. Further, weaker inventory accumulation was a drag on growth, with inventories contributing just 0.6% to Q1 growth. Final sales (GDP ex inventories) grew 1.6% QoQ annualized after a weaker 1.1% growth in Q4.
- Despite the sluggish April labor market report, other data, including the solid ISM data confirms the U.S. economy remains on a moderate GDP growth path. Gradually rising household income and declining unemployment are likely to support consumption spending. Further, household deleveraging appears to be largely complete and hence is unlikely to be a drag on consumer spending and GDP growth. Business investment spending is expected to rebound on the back of strong profit and cash levels. **Q1 GDP growth is likely to be revised higher in the next estimate. U.S. Q2 GDP is expected to grow around 2.5%.**
- **Japan's economy posted a stronger-than-expected GDP rebound in Q1 with 4.1% QoQ annualized growth (3% expected).** Further GDP data was revised up for Q4 (+0.1% from -0.7%) and Q3 (7.6% from 7%). The Q1 GDP rebound was led by private consumption (4.4%), government consumption (2.8%), exports (12.3%) and a surge in public investment (23.6%). Private consumption was strong for the fourth successive quarter, rising 4.4% in Q1 after 2.8% in Q4, contributing 2.6% to Q1 GDP growth. Consumption was supported by the revival of Eco Car subsidies under the FY2011 fourth supplemental budget. After weak growth in the previous two quarters, public investment spending surged 23.6% in Q1, contributing 0.9% to GDP. Government consumption was also solid, rising 2.8% in Q4 after 1.6% in Q4. Net exports made a solid contribution to Q1 GDP with exports up 12.3% while imports slowed to 8% as supply chain disruptions eased.
- On the negative side, there were declines in private sector investment with residential investment falling -6.1% after 0.2% in Q4 and 20.5% in Q3. Business investment spending fell a sharp -14.8%, partly as a payback after the 22.3% spike in Q4. Also, there was a 0.4% rise in inventories with rebuilding following the -0.4% decline in Q4 during the Thailand floods. Looking ahead, Japan Q2 GDP growth is likely to remain solid (~2.6%) with continued strength in public reconstruction spending, solid consumption & exports.

- **Eurozone surprised on the upside with Q1 GDP edging up 0.1% QoQ annualized after falling -1.2% in Q4 2011, thereby avoiding a technical recession (two quarters of GDP decline).** On an annual basis, Eurozone GDP growth was flat after rising 0.7% YoY in Q4. Full details of Q1 GDP composition are not yet available, but it appears that strong growth in Germany (27% of Eurozone GDP) offset weakness in Eurozone periphery. **German GDP rebounded a stronger-than-expected 2% QoQ annualized after declining -0.7% in Q4.** According to the FSO, net exports made a strong contribution to Germany Q1 GDP while consumption spending also made a positive contribution, while investment spending declined as the Eurozone crisis apparently took a toll.
- **In contrast, French Q1 GDP was close to flat at 0.16% annualized, while Q4 GDP was revised down to 0.1% from 0.2% earlier reported.** Household spending and government consumption were positive while trade and investment spending were negative. **Italian GDP sunk -3.2% in Q1 after -2.6%, and Spanish GDP declined a more modest -1.2% after a similar -1.2% decline in Q4.** Among other economies, **Portuguese GDP fell -0.1% after -5% decline in Q4, and Czech GDP sunk -4% after -0.4% in Q4. Finnish GDP grew 1.2%, Netherlands GDP declined -0.2%, Austrian GDP grew 0.2% while Belgium GDP rose 0.3%.** Looking ahead, the ECB expects an improvement in global growth and ECB policy to support growth going forward. However, tensions in sovereign debt markets, balance sheet adjustments, and high unemployment are likely to dampen growth.
- **The U.K. economy relapsed into recession with GDP contracting in Q1, for the second successive quarter. U.K. GDP declined -0.8% QoQ annualized in Q1 after -1.2% in Q4.** Full details of Q1 GDP are not yet available. By industry, manufacturing was flat, but construction and mining declined. While there was modest strength in electricity and transportation and communication, it could not offset these declines.

Emerging Economies Growth: China, India Slow in H1. Monetary Easing to Help Boost H2 Growth in Emerging Economies

- **China's April activity data points to slower growth in China in Q2 2012.** Activity data surprised to the downside with a drop in industrial production (IP), fixed asset investment (FAI) and retail sales. IP growth fell to 9.3% YoY in April after rebounding to 11.9% in March. FAI growth declined to 19.2% from 21.1% in March with a sharp slowdown in property investment growth. Retail sales growth fell to 14.1% in April, down from 15.2% in March. Export growth declined to 4.9% YoY from 8.9% in the previous month, while imports declined 0.3% from 5.3% in March. Earlier, China's GDP growth moderated to a weaker than expected 8.1% YoY pace in Q1 2012, the slowest pace since Q4 2008 with slower net exports and residential construction.
- **India's GDP growth is likely to have slowed down to around 6% YoY in Q1 2012 from 6.1% in Q4 2011 and 6.9% in Q3.** Business confidence stabilized in April, inching higher to 54.9 after declining to 54.7 in March from 56.6 and 57.5 in previous months. Industrial Production grew 4.1% YoY in February, while January IP growth was revised down sharply to just 1.1% from the 6.8% reported earlier. Consumption growth remains solid driven by private consumption spending on back of solid income growth. Net exports remain a drag on GDP growth with oil prices remaining elevated and with the rupee depreciating sharply above Rs.54/\$. The trade balance remained wide at – US\$13.9bn in March after –US\$15.2bn in February driven by surging energy bill. GDP growth is likely to get a boost from the RBI rate cuts in April and the government likely to fast-track investment spending.
- **Korea's GDP growth slowed to 2.8% YoY in Q1 2012 following 3.3% growth in Q4, below consensus expectation of 3% growth.** On a QoQ basis growth picked up to 0.9% from 0.3%. Fixed investment surprised to the upside growing 5.1% YoY in Q1 after contracting -1.8% in Q4. Private consumption rose 1.6% in Q1 after 1.1% in Q4, while government consumption rebounded strongly growing 4.4% in Q1 from 1.8% in Q4. Exports rose 5% from 4.4% in Q4, while imports rose 4.6% from 1.6% in Q4.
- **Taiwan's GDP growth slowed sharply to 0.4% YoY in Q1 from 1.9% in Q4.** On a sequential QoQ annualized basis GDP grew 1.1% from -0.6% in Q4 ending Taiwan's technical recession. Private consumption increased 1.5% YoY from 1% in Q4. Fixed capital formation continued to decline, albeit at a slower pace, falling -14.9% in Q1 after -19.4% in Q4. Exports fell -3.3% in Q1 after 0.8% in Q4, while imports declined -7.5% from -7.2% in Q4. Government consumption fell to 2.7% from 3.2% in Q4 2011.
- **Mexico's GDP growth grew 4.6% YoY in Q1 2012 after slowing to 3.9% in Q4 from 4.5% in Q3.** By industry, manufacturing, construction, and agriculture all posted solid growth, the exception was mining, which declined -0.8%. Consumer spending appears to have improved with retail sales accelerating to 7.6% YoY in February from 4.4% in January. Further, while unemployment increased in early Q1, it pulled back to 4.6% in March from 5.3% in February.

However, the outlook for investment spending is mixed. IMEF manufacturing confidence is holding above 50, but the index steadily eased to 52.5 from 52.7 in March. Further, industrial production was mixed in Q1, falling -1.7% MoM in February after 1.3% in January.

- **Brazilian GDP growth is expected to improve to 2.3% in Q1 2012 after slowing to 1.4% in Q4 2011 from 2.1% in Q3.** The outlook for consumer spending is mixed. Retail sales have been strong, rising to 9.6% YoY in February following a strong gain in January. However, unemployment continued to rise to 6.2% in March from 5.7% in February, its lowest level in more than a decade. The outlook for investment spending is mixed. Industrial production was mixed in Q1, falling -0.5% MoM in March after 1.3% in February and -1.6% in January. Further, manufacturing PMI it eased to 49.3 in April. Nevertheless, the central bank (BCB) cutting rates to 9% should provide some support to domestic businesses.

Inflation Outlook: Inflation Easing in Developed Economies. EM Inflation Declining Giving Room to EM Central Banks to Cut Interest Rates

- **Headline inflation continues to ease in the developed economies with lower food and commodity prices, continued slack in the labor market, below-trend growth. While headline inflation in Eurozone and U.K. currently remains above the central bank target (2%), both the ECB and the BoE remain sanguine about the outlook for inflation in the medium-term. The BoJ continues to target inflation around 1% from below 0.5% currently. Inflation in the emerging economies has also been trending lower from the highs of 2011. However, elevated oil prices have slowed the improvement in headline inflation.**
- **U.S. CPI eased to 2.3% YoY in April after 2.7% in March and 2.9% in January and February.** Prices were flat MoM after 0.3% in March. The decline in the annual pace of the headline index was primarily due to a slowdown in energy inflation. Energy inflation eased to 0.9% YoY from 4.6% in March and 7% in February. The recent decline has been mostly due to base effects, but there was still a -1.7% MoM decline in April after 0.9% in March and 3.2% in February. Food inflation also eased to 3% YoY from 3.2%. Core inflation held at 2.3% YoY, but still edged up 0.2% MoM in both March and April.
- **Eurozone headline HICP inflation edged down to 2.6% YoY in April (flash estimate) after holding steady at 2.7% for the fourth straight month in March.** Full details for April are not yet available, but in March prices rose 1.3% MoM after 0.5% in February. Core inflation edged up to 1.6% YoY in March from 1.5% in February. Base effects helped keep prices contained with core prices jumping 1.5% MoM. The bulk of the increase was due to a 16% seasonal surge in clothing prices. German inflation eased to 2.2% YoY in April from 2.3%, Spanish inflation rose to 2% from 1.8%. Italian inflation held at 3.8% in April. French inflation eased to 2.4% YoY in April from 2.6% in March.
- **U.K. inflation edged up to 3.5% YoY in March from 3.4% in February and 3.6% in January.** Prices rose 0.3% MoM after 0.6% with continued gains in core inflation. Core inflation rose to 2.5% YoY from 2.4% with a 0.4% MoM increase. Within core inflation, there were strong gains in clothing prices (2.2% after 2.9%) and household furnishings (1.3% after 1.5%). Outside of core inflation, declines in energy prices were offset by gains in food prices. Food prices also increased to 5.5% YoY from 4.9%, while energy inflation eased further to 8.3% from 9.4%.
- **Japanese headline inflation rose to a higher than expected 0.5% YoY reading in March from 0.3% in February on continued upward pressure from higher fresh food and energy prices.** Core inflation (excluding fresh food) edged up to 0.3% in March from 0.1% in February, driven by higher energy prices and a rise in television prices as a result of the introduction of new products in February. Japanese core-core CPI (excluding energy and food), a better indicator of underlying price trend, remains negative at -0.4% in March after -0.5% in the previous month. Tokyo core inflation, a leading indicator for the national inflation, was down -0.5% after -0.3% in previous two months. There has been a divergence between Tokyo and national prices in the past few months as the post earthquake reconstruction work has resulted in higher price pressures nationwide than in urban areas. This is likely to continue in the coming months, reducing the accuracy of the Tokyo prices as a lead indicator of nationwide prices.
- **China's headline inflation eased to 3.4% YoY in April from 3.6% in March.** On a MoM basis headline inflation fell -0.1% in April after rising 0.2% in March. Food inflation fell to 7% YoY in April from 7% in March. Vegetable prices were the biggest driver of food inflation for the month. As more favorable weather kicks in, vegetable prices are likely to abate in the coming months. Meanwhile, non-food price inflation rose 1.7% in April after 1.8% in March. Non-food price inflation has remained largely stable in the past few months. With the likely decrease in food price inflation, headline inflation is on track to continue its downward trend in the coming months.

- **India's Wholesale Price inflation (WPI) edged up to 7.2% YoY in April reversing the decline to 6.9% in March from 7% in February.** The acceleration in headline inflation was driven by higher food inflation, up 10.5% after 9.9% in March. Fuel price inflation strengthened to 11% from 10.4% in March with coal prices rising 13.9% after 0.4% in previous month. Core inflation (manufactured non-food products) rose to 4.9% in April after easing to 4.6% in March from 5.8% in February. Inflationary pressures are likely to persist with the pass through of tariffs and rupee depreciation increasing the impact of higher oil prices.
- **Korea's headline inflation remains in a downtrend, falling to 2.5% YoY in April after 2.6% in March, taking headline CPI closer to the lower end of the Bank of Korea's (BoK) 2-4% inflation range.** On a MoM basis inflation was flat after declining -0.1% in the previous month. The decline in inflation was mainly due to government measures to lower insurance premiums for medicines, subsidies to childcare programs and free school meals. This was able to offset elevated oil prices to an extent. Core inflation declined 1.8% YoY in April from 1.9% in March. Inflation is expected to remain benign with sub-par growth.
- **Taiwan's April headline inflation rose to 1.4% YoY in April from 1.2% in March.** Headline inflation rose 0.4% MoM after being flat in the previous month. Food inflation slowed to 2.1% YoY in April from 3.1% in March. Core inflation rose 0.9% in April after 0.7% in March and -0.1% in February. Despite low headline inflation in April, inflationary expectations are on the rise as the government contemplates electricity price hikes in June 2012.
- **Mexican inflation eased to 3.4% YoY in April from 3.7% in March and 3.9% in February.** The recent slowdown in prices has primarily been due to reduced supply from November through January in the aftermath of the droughts in Northern Mexico. On a MoM basis, inflation fell -0.3% MoM after rising 0.1% in March. Non-core inflation remains weak, falling -1.8% after -0.6% with another sharp decline in fruits and vegetables (-2.3% after -3.7%) and a reversal in energy (-3.4% after 0.4%). Core inflation edged up to 3.4% YoY after 3.3% in March with the monthly pace holding at 0.2% MoM with core goods inflation rising.
- **Brazilian IPCA inflation remains in a downtrend, easing to 5.1% YoY in April after 5.2% in March and 5.9% in February.** This is the lowest level of IPCA inflation since late 2010 and inflation has been declining each consecutive month since reaching a high of 7.3% in September. Prices rose 0.6% MoM, accelerating from 0.2% in March.

Interest Rates: Fed, ECB & BoE on Hold in Early Q2 with Easing Bias. Door Open for Further QE/LTRO. BoJ Expands QE Again in April. Emerging CBs in Easing Mode

- **Stocks remain supported by liquidity measures and low interest rates and liquidity.** The ECB, the BoE and Fed remained on hold in late April / early May and made no changes to their QE/LTRO programs. However, these central banks have left the door open to further asset purchase / liquidity programs if the Eurozone crisis worsens or economic conditions deteriorate. The BoJ expanded its asset purchase program by ¥5tn at the late April meeting. Emerging central banks continue to ease policy/cut rates with India starting rate cuts, while Brazil cut rates for the sixth time. China cut the reserve ratio in May and is on track to ease policy further.
- **The Fed left policy on hold at their April meeting, as expected.** The Fed continues to commit to leave rates on hold through 2014 due to "the low rates of resource utilization and a subdued outlook for inflation over the medium run." In addition, the Fed will continue the Operation Twist program that is expected to end in June and reinvest principal payments from agency debt and MBS into agency MBS and rolling over maturing Treasury securities. The Fed reiterated its policy of regularly reviewing their holdings and the potential to adjust them as appropriate.
- According to the Fed's statement, the economy is expanding moderately with improving labor market conditions, household spending expanding, and business investment advancing. The Fed noted that there are signs of improvement in the housing sector, but it still remains depressed. Inflation is also rising as a result of higher energy prices, but inflation expectations are contained. **At the April press conference, Chairman Bernanke reaffirmed that Fed remains open to additional QE if growth disappoints.**
- **The European Central Bank (ECB) held rates unchanged at 1% at the May 3rd meeting, unchanged for the sixth consecutive month, as widely expected.** The ECB also did not make any announcements about or changes to non-traditional policies (LTRO, SMP etc). In the introductory statement at the press conference, the ECB indicated that it expects inflation in the medium-term to be in line with price stability, even though inflation is currently elevated and likely to remain above the 2% target through the end of 2012. The ECB also assured that inflation expectations are well anchored, despite the recent use of non-traditional policies (LTRO, bond purchases). The ECB's inflation outlook is broadly balanced. On the economic outlook, the ECB expects an improvement in global growth and ECB

policy to support growth going forward. However, tensions in sovereign debt markets, balance sheet adjustments, and high unemployment are likely to depress the pace of growth. The ECB highlighted the "good progress" that many Eurozone economies have made in terms of fiscal consolidation. However, they continue to highlight the importance of structural reforms and further fiscal consolidation.

- **The Bank of England left rates on hold at 0.5% in May and keep asset purchases steady at £325bn.** Recent U.K. economic data has been weak. GDP has declined for two consecutive quarters and the outlook for future growth remains weak. However, on a more positive note, U.K. inflation has stabilized in early 2012 after being elevated in recent years and is holding between 3.4% and 3.6% the first three months of the year. The decline in inflation and the sluggish prospects for growth can provide the BoE room to expand asset purchases further.
- **The BoJ expanded its asset purchase program by ¥5tn and kept its policy interest rate unchanged at its late April policy meeting.** The BoJ has been under increasing political pressure to undertake further easing measures to support the ongoing GDP recovery. The asset purchase program was expanded to ¥70tn from ¥65tn and the deadline for completion of the purchases was extended to end-June 2013 from end-2012. The bank increased the limit on long-term JGB purchases to ¥29tn from 19tn. The bank increased its allocation to ETFs by ¥200bn and to J-REITs by ¥10bn. It also extended the residual maturity of JGBs to be purchased from 1-2 years to 1-3 years. Due to weak demand for fixed-rate funds, the bank reduced the maximum outstanding amount of fixed-rate funds-supplying operation against pooled collateral with a six-month term by about ¥5trn.
- In its outlook report, the BoJ increased its median GDP growth forecast for FY 2012 to 2.3% from 2% previously. The bank said "the year-on-year rate of change in the CPI is expected to gradually rise to a range of above 0.5 percent and less than 1 percent toward the latter half of the projection period" (FY 2012-13) and thereafter "it will likely be not too long before the rate reaches the Bank's price stability goal." The BoJ increased its median inflation forecast for FY 2012 to 0.3% from 0.1% previously.
- **The People's bank of China (PBC) announced a 50bps cut in the Required Reserve Ratio (RRR) effective May 18th.** This takes the RRR for large banks to 20% and for small and medium banks to 18%. The RRR cut follows a marked slowdown in activity data in April. April money and credit growth was disappointing with M2 growth falling to 12.8% YoY from 13.4% in March, falling short of the PBC's target rate of 14%. Monthly RMB lending fell to 682bn from 1,011bn in the previous month. Despite policy easing through increased fiscal spending, easier liquidity and easier rules on credit to local government platforms, it has not been able to stop the continued downtrend in activity. Monetary policy is likely to be loosened further in the near future with more RRR cuts likely.
- **The Reserve Bank of India (RBI) cut repo and reverse repo rates by a larger than expected 50bps to 8% and 7% respectively and kept the cash reserve ratio (CRR) at 4.75% in April.** The RBI was expected to start easing interest rates with economic activity and confidence indicators continuing to weaken in Q1 while inflation was showing signs of easing. The larger than expected rate cut was in the wake of Industrial Production coming in sharply lower than expected at 4.1% YoY in February and WPI inflation moderating to 6.9% in March. However, the RBI has signaled that further rate cuts are unlikely in the near term "as the deviation of growth from trend is modest, upside risks to inflation persist" and that "the economy is likely to revert close to its post-crisis trend in FY13." The RBI expects GDP growth of 7.3% for fiscal year 2013 and WPI to reach around 6.5% by March 2013.
- **Taiwan's central bank (CBC) is likely to remain on hold at its next quarterly policy meeting in June as key economic activity data remains weak.** The CBC is likely to maintain rates at current level as the further clarity is needed on both the domestic and external front before making further monetary policy changes. Earlier, the CBC remained on hold at its Q1 meeting, highlighting upside risks to inflation and the economy likely to hit bottom in Q1.
- **The Bank of Korea (BoK) left rates on hold at 3.25% for the eleventh consecutive month at its May meeting.** In its statement following the meeting the BoK maintained that "the recovery of economic growth to have faltered, with consumption and investment decreasing while exports maintain generally sound levels". On the external front the bank said that it expects "the global economy to sustain its recovery, albeit at a moderate pace and judges that risk factors still exist". The BoK is likely to be on hold in the near future with inflation moderating and economic activity expected to recover over the year.
- **Mexico's Banco de Mexico (Banxico) left rates unchanged at 4.5% at their late April meeting, as expected.** Banxico kept an easing bias arguing that well-anchored inflation expectations offset upside risks from improving growth prospects. The central bank has benefitted from the recent decline in inflation as the supply shock from earlier floods fades. The real side of the economy benefits from the rise in oil prices and improving U.S. economy.

- **The Banco Central do Brasil (BCB) cut rates by an additional 75bps to 9% at their April 18th meeting.** This was the second consecutive 75bps cut and the sixth consecutive cut since rates reached a high of 12.5% in August 2011. Rates are also near the all-time low of 8.75% that was reached during the financial crisis. The BCB has provided signals that they would consider dropping rates further, potentially below those lows. The recent decline in inflation gives them scope to cut rates further. However, the BCB will likely slow the pace of cuts, to a 25-50bps cut at their next meeting in late May.

Currency Outlook: Dollar Strong against Euro with Fresh Eurozone Risks. Yen Range Bound With Risk Aversion Offset by BoJ Easing. EM Currencies Outlook Remains Solid Though Increased Risk Aversion is a Negative

- **The U.S. Dollar is likely to remain firm against the euro and sterling but weaken against EM currencies.** The euro is likely to weaken in the near term with increased risk of Greece leaving the Eurozone and rising concerns about Spanish banks. The yen is likely to be range bound with strength due increased risk aversion offset by the BoJ's asset purchases. The outlook for EM currencies remains positive, but rising risk aversion could keep them under pressure.
- **The euro is likely to remain weak against the dollar in the near-term with increased risk of Greece leaving the Eurozone** after no party secured a majority in the May elections and Greece set for another election in June. The risk of Greek contagion to the rest of Eurozone and collateral damage to Eurozone banks has increased. In France, uncertainty about French policies with respect to austerity measures, bail-outs and holding the Eurozone together under the new Hollande regime. These risks are likely to keep the Euro under pressure in the near-term.
- **The pound is likely to weaken against the dollar with the economy struggling and continuing asset purchases by the BoE.** The decline in U.K. inflation and the economy less exposed to the Eurozone periphery has caused the pound and euro to diverge recently. Nevertheless, the U.K. economy slipped into recession with two consecutive quarters of GDP declines. This is likely to keep the pound weak.
- **The Japanese yen is likely to be range bound with safe haven gains from increased Eurozone risk aversion offset by additional BoJ asset purchases.** The yen is likely to strengthen on back of increasing safe haven demands due to increased risk of Greek Euro exit. However, the BoJ committing to a 1% inflation target and expanding their asset purchase program will likely put downward pressure on the yen. Further, a relatively positive Japanese GDP growth outlook favors the yen over a longer horizon. Nevertheless, the potential for currency intervention could help keep the yen contained.
- **The outlook for EM currencies remains positive, but rising risk aversion could keep EM currencies volatile.** Concerns over the outlook for Spain and Greece have resulted in fresh strains in Eurozone and could put downward pressure on EM currencies. Nevertheless, EM GDP growth remains relatively healthy. While there are signs of risks that growth in some economies could slow, EM central banks remain active in attempting to halt these slowdowns.

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