Global Economic & Market Monthly Review: Pausing

ECONOMIC ANALYSIS & RESEARCH DIVISION

Executive Summary

July 2013

The US economy is expected to have slowed down during Q2 of 2013, as we estimate that its real GDP grew by 0.9% (Q/Q-AR rate), compared to Q1's 1.8%. For 2013 as a whole, we estimate that it will grow by 1.8%, slower than 2012's 2.2%. In more detail, the growth rate of personal outlays is expected to accelerate (from 1.9% to 2.1%), while fixed investment (from 9% to 7%) and government expenditure (from -1.7% to -2.9%) are expected to decelerate and deteriorate, respectively.

The EZ economy is expected to have posted an improvement during Q2 of 2013, as we estimate that its real GDP shrank marginally by 0.1% compared to Q1's -0.3%. For 2013 as a whole, we estimate that it will shrink by 0.7%, worse than 2012's -0.6%. In more detail, the smaller positive contribution from net exports is expected to offset the improvement (meaning a smaller negative contribution) in domestic demand.

We estimate that Japan's economy will grow at a faster rate (2.2%) during 2013 than in 2012 (1.9%). The main positive factor is the JPY depreciation which supports exports and consequently business investment. The inflation rate will accelerate to 0.7% at the end of 2013 and above 2.0% by the end of 2014. In June, it was at 0.4%, the highest level since the end of 2008. Debt sustainability (public debt to GDP ratio) at 235%, is the most important risk for Japan's economy. Since the outbreak of the crisis in 2008, the primary budget deficit has reached 9% of GDP for every year.

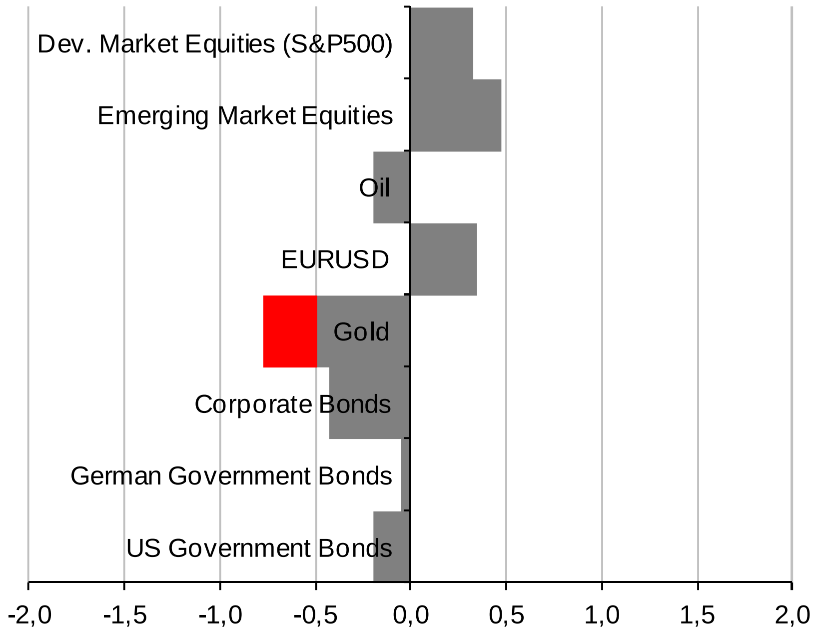
The environment is mainly characterized by low volatility. Apart from our negative view for the gold market, our view for the other markets remains neutral. We set apart the considerable improvement in the emerging equity markets. We also observe that the long term bonds have become cheap relative to the short term bonds and the applied monetary policy. The technical view for the S&P500, EURUSD and oil is positive.

Lekkos Ilias
•) Lekkosi@piraeusbank.gr
Patikis Vasilios
•) PatikisV@piraeusbank.gr
Polychronopoulos Dennis
•) Polychronopoulosd@piraeusbank.gr

Τράπεζα Πειραιώς
Μονάδα Οικονομικής Ανάλυσης και Αγορών
Αμερικής 4, 105 64, Αθήνα
Bloomberg: <PBGR>
Tel: (+30) 210 328 8187, Fax: (+30) 210 328 860

Global Market Risk-Return Scoring

(6-9 month horizon)

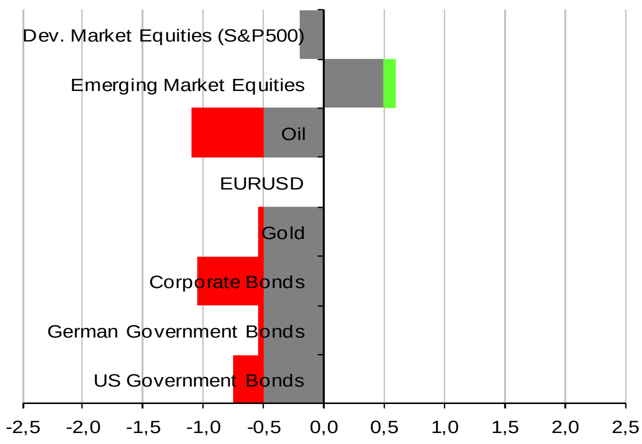


Scoring between -2.5 and 2.5 reflects an average estimate (50%) quantitative fundamental, & (50%) technical factors affecting individual markets.

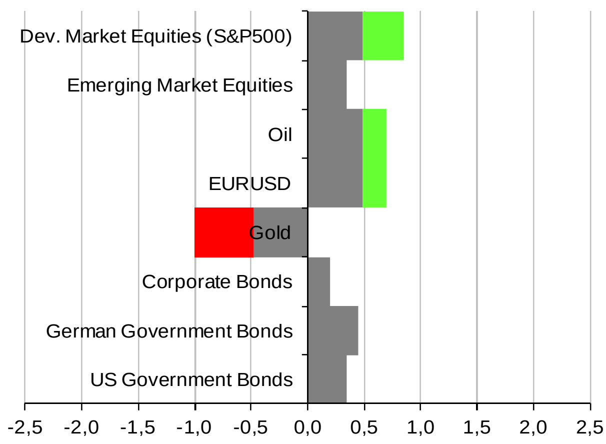
- *-0.49 to 0.49 neutral assessment*
- *0.5 to 1.49 positive assessment (-0.5 to -1.49 negative assessment)*
- *> 1.5 very positive assessment (<-1.5 very negative assessment)*

For long-term estimates (+9 months), more weight should be given to fundamental and quantitative factors, while for the medium term (3-6 months), more weight should be given to technical factors.

Fundamental & Quantitative Estimates



Technical Analysis



Fundamental & Quantitative Estimates: Deviations from long-term average value measures (e.g. P/E for stocks, nominal growth for bonds, ppp for fx) as quantified by estimated "fair values" using for each the appropriate market & economic fundamentals. Technical Picture: Standardized display of figures such as MACD, RSI and other technical analysis measures

Economic Developments

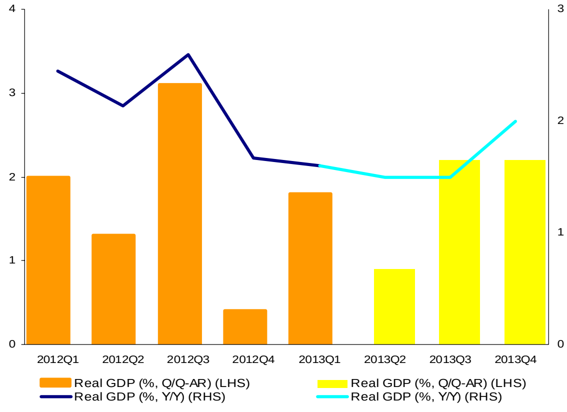
USA: Faster Recovery in 2014

- The US economy is expected to have slowed down during Q2 of 2013, as we estimate that its real GDP grew by 0.9% (Q/Q-AR rate), compared to Q1's 1.8%. For 2013 as a whole, we estimate that it will grow by 1.8%, slower than 2012's 2.2%. In more detail, the growth rate of personal outlays is expected to accelerate (from 1.9% to 2.1%), while fixed investment (from 9% to 7%) and government expenditure (from -1.7% to -2.9%) are expected to decelerate and deteriorate, respectively.

- Constrained international energy prices (and prices of commodities in general) at current (or even lower) levels, coupled with the absence of strong domestic demand, will keep the inflation rate below 2.0% during 2013. Moreover, the negative output gap, which is reflected by the relatively high unemployment rate, will also keep core inflation below 2.0%. At the same time, unemployment will gradually decrease, but will stay above 7.0% until Q1 of 2014.

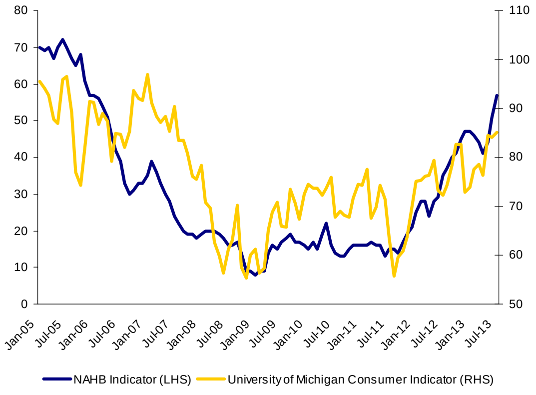
- Therefore, the Federal Reserve will maintain its policy rate at its current very low level (0.25%) and will continue its QE program, but at a slower pace from Q4 of 2013, when the unemployment rate will approach 7.0%. We believe that the QE program will probably stop when the unemployment rate falls below 7.0% for at least two consecutive months. This will not happen before Q2 of 2014.

Real GDP



Source: Bloomberg, Piraeus Bank Research

Leading Indicators Increase



Source: Bloomberg, Piraeus Bank Research

- The austerity measures taken to reduce the fiscal deficit, slower QE pace and uncertainty emanating from the Eurozone crisis are the main factors which could negatively affect the US economy's prospects. On the other hand, higher house prices, better FMIs' balance sheets, sizable household deleverage, high corporate profits and a low inflation rate are some of the factors which could have a positive effect. These factors could cause a positive surprise in the personal outlays growth rate from the end of 2013 onwards. Furthermore, Bernanke has emphasized that the Fed's MPC members will start considering a policy rate increase when the unemployment rate falls below 6.5%.

- The fiscal deficit is expected to shrink dramatically to 6% during 2013, compared to 2009's 13%. Hence, the fiscal consolidation procedure can be more gradual and balanced, which in combination with the debt ceiling increase is more favorable for the US economy's prospects. Likewise, the monetary policy reversal procedure must be gradual and balanced, by taking into consideration international financial stability and domestic labour market improvement.

USA: **M**acroeconomic Projections

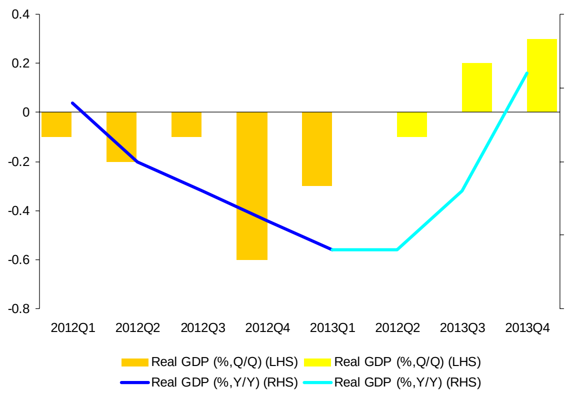
	2012/Q1	2012/Q2	2012/Q3	2012/Q4	2013/Q1	2013/Q2	2013/Q3	2013/Q4	2012	2013
				Q/Q-AR(%)					Y/Y(%)	
Real GDP	2.0	1.3	3.1	0.4	1.8	0.9	2.5	2.5	2.2	1.8
Personal Outlays	2.4	1.5	1.6	1.8	2.6	1.5	2.5	2.5	1.9	2.1
Investment	9.9	4.5	0.9	14.0	3.0	5.0	10.0	10.0	9	7
Public Expenditure	-3	-0.7	3.9	-7	-4.8	-2	-2	-2	-1.7	-2.9
Exports	4.4	5.3	1.9	-2.8	-1.1	5	5	5	3.4	1.4
Imports	3.1	2.8	-0.6	-4.2	-0.4	9	5	5	2.4	1.4
Business Inventories (Contribution)	-0.4	-0.5	0.7	-1.5	0.6	0.3	0.3	0.3		
Inflation Rate	2.8	1.9	1.7	1.9	1.7	1.4	1.7	1.7	2.1	1.7
Core PCE	1.9	1.8	1.6	1.5	1.3	1.1	1.1	1.3	1.7	1.2
Unemployment rate	8.3	8.2	8.1	7.8	7.7	7.6	7.4	7.2	8.1	7.5
Fed - Policy Rate	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25
10Y Treasuty Yield	2.21	1.64	1.63	1.76	1.84	2.48	2.90	2.50	1.76	2.50
EUR/USD	1.33	1.27	1.29	1.32	1.28	1.3	1.30	1.26	1.32	1.26

EZ: Improvement before the German elections

- The EZ economy is expected to have posted an improvement during Q2 of 2013, as we estimate that its real GDP shrank marginally by 0.1% compared to Q1's -0.3%. For 2013 as a whole, we estimate that it will shrink by 0.7%, worse than 2012's -0.6%. In more detail, the smaller positive contribution from net exports is expected to offset the improvement (meaning a smaller negative contribution) in domestic demand. Constrained international energy prices (and prices of commodities in general) at current (or even lower) levels, coupled with the continuous decline in domestic demand, will keep the inflation rate below 2.0% during 2013. At the same time, the unemployment rate (as a lagging variable) will continue to climb to 12.5% at the end of 2013. Therefore, we estimate that the ECB will probably maintain its policy rate at its current level (0.50%) without ruling out an additional decrease of 25bps.

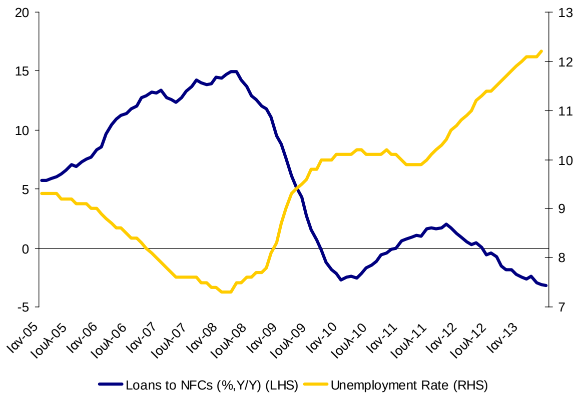
- The improvement in the leading indicators signals the beginning of the recovery (during Q3), after seven consecutive recessionary quarters. The PMI manufacturing leading indicator returned above the 50.0 level after two years. Moreover, Draghi has emphasized that the ECB intends to maintain the current level (or even lower) of the policy rate for an extended period. On the other hand, the disappointing credit expansion data (especially for SMEs) and the decisions in favour of additional austerity measures (from the majority of the EZ member countries) are two discouraging factors for the recovery. Furthermore, the structural unemployment rate has increased alarmingly in the majority of EZ member countries, leaving a large proportion of labour resources unexploited for long time.

Real GDP



Source: Bloomberg, Datastream, Piraeus Bank Research

Unemployment Rate & Loans to NFCs



Source: Bloomberg, Datastream, Piraeus Bank Research

- The main factor determining the prospects of the EZ economy is the need for fast decisions/actions aimed at more complete and viable economic and monetary integration. The OMTs (Outright Monetary Transactions) announcement (from Draghi), the ESM (European Stability Mechanism) operation and the SSM (Single Supervisory Mechanism) agreement are essential measures for the enhancement and viability of economic and monetary integration. Moreover, the SRM (Single Resolution Mechanism) and DGS (Deposit Guarantee Scheme) frameworks are substantial steps for the enhancement and viability of the EZ financial/banking system.

- Without any doubt, strong political will is the main driving force for progress on the aforementioned decisions/actions. The months before the German elections seem to be characterized by a high degree of inactivity, while the governments in the southern peripheral countries are fragile due to the tough austerity measures being implemented and intolerably high unemployment rates. Therefore, fiscal consolidation must be combined with an employment support policy.

EZ: **M**acroeconomic Projections

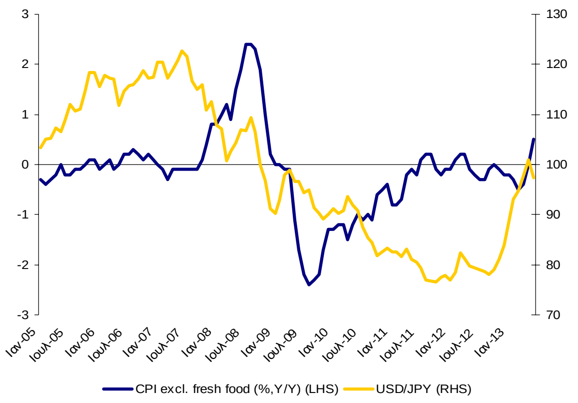
	2012/Q1	2012/Q2	2012/Q3	2012/Q4	2013/Q1	2013/Q2	2013/Q3	2013/Q4	2012	2013
				Q/Q(%)					Y/Y(%)	
Real GDP	-0.1	-0.2	-0.1	-0.6	-0.3	-0.1	0.2	0.3	-0.5	-0.7
Private Consumption	-0.2	-0.5	-0.1	-0.6	0	-0.1	0.1	0.2	-1.3	-0.7
Investment	-1.3	-1.8	-0.8	-1.5	-1.9	-0.5	0.5	0.5	-4.2	-3.5
Public Consumption	-0.1	-0.3	-0.1	0.0	-0.1	-0.1	0.1	0.1	-0.5	-0.3
Exports	0.8	1.5	0.8	-0.9	-0.9	-0.5	0.5	0.9	3	-1
Imports	0.0	0.3	0.3	-1.2	-1.2	-0.9	0.3	0.5	-1	-2
Business Inventories (Contribution)	-0.1	0.0	-0.1	-0.1	0.0	-0.1	0.2	0.2		
Inflation Rate	2.7	2.5	2.5	2.3	1.8	1.4	1.7	1.7	2.5	1.7
Unemployment Rate	10.9	11.3	11.5	11.8	12.1	12.2	12.3	12.4	11.4	12.2
ECB-Policy Rate	1.00	1.00	0.75	0.75	0.75	0.50	0.50	0.50	0.75	0.50
10Y Bund Yield	1.80	1.59	1.44	1.32	1.29	1.73	1.60	1.50	1.32	1.50

China & Japan

- We estimate that Japan's economy will grow at a faster rate (2.2%) during 2013 than in 2012 (1.9%). The main positive factor is the JPY depreciation which supports exports and consequently business investment. The inflation rate will accelerate to 0.7% at the end of 2013 and above 2.0% by the end of 2014. In June, it was at 0.4%, the highest level since the end of 2008. Debt sustainability (public debt to GDP ratio) at 235%, is the most important risk for Japan's economy. Since the outbreak of the crisis in 2008, the primary budget deficit has reached 9% of GDP for every year. In combination with the weak nominal GDP growth rate, the public debt to GDP ratio trajectory has become very alarming. The impending consumption tax increase will be a step towards fiscal consolidation. Moreover, the QE program must be implemented in a way that avoids yield increase and consequently debt service cost.

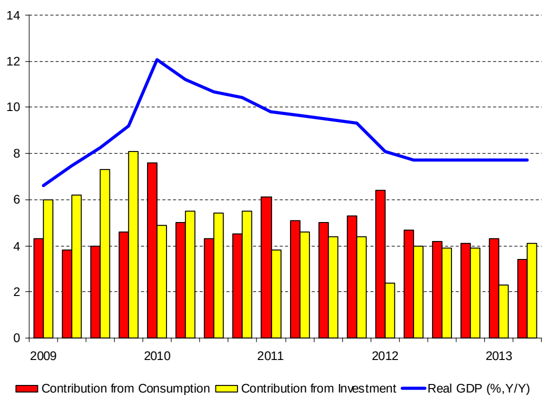
- We estimate that China's economy will grow at a slower rate (7.5%) during 2013 than in 2012 (7.9%). In the coming years, China's economy will grow at 7.0% - 7.5% significantly lower than the growth rate has been. In more detail, the net export contribution is expected to be zero or marginally positive, so the entire GDP growth will come from the domestic demand contribution. In July, the leading PMI manufacturing indicator was at its lowest level in the last eleven months. Moreover, the PMI employment index was at its lowest level in the last 53 months. The sharp increase in the total debt to GDP ratio (from 150% to 210%) after the outbreak of the crisis in 2008 is the most significant risk for China's economy. Due to the fact that the public debt to GDP ratio is at a low level (35%), the majority of the total debt comes from the abundant credit expansion, resulting in the creation of a considerable shadow banking sector. China's government and Central Bank have shown the will to place the shadow banking sector under control, before it has an irrevocably negative impact on the economy.

Japan: Inflation Rate & Exchange Rate



Source: Bloomberg, Piraeus Bank Research

China: Consumption, Investment and GDP



Source: Bloomberg, Piraeus Bank Research

International markets

- International markets continue to present contrasting faces where the investment climate remains positive and the volatility low in the equity markets of developed countries, while volatility and uncertainty both remain high in bond markets (mainly the US), in commodities and in emerging market equities. The asymmetry of returns of equity markets that we saw in the previous quarter continued and by the end of March we observed a significant increase in US and Japanese equities (S&P500 8%, Nikkei 225 20%) while in emerging countries the trend remained negative (MSCI EM -6%, HSCEI China -10%) and European markets were in marginally positive territory (Eurostoxx50 4%, FTSE100 3.5%). The immediate market focus remains monetary policy in the US (and Japan to a lesser extent). So while the previous month's relatively restrictive comments by Bernanke worried markets, more recent milder statements offered relief.

- Along with the monetary policy factor, growth expectations are equally, if not more important for long-term market trends. Thus we observe that the reversal of the Fed's rhetoric led the S&P500 to new highs while, on the other hand, yields on long-term bonds experienced only a marginal drop (bond strengthening), indirectly suggesting expectations of improving prospects of growth and profitability. Indeed, recent earnings announcements surprised positively in the US and a number of indications have increased the likelihood of a positive surprise for growth in 2014 (in line with our expectations). Analysts have adjusted downwards their estimates for growth in 2014 (to 2.7% in February from 2.8%, Bloomberg) increasing the margin for positive surprises.

- Emerging markets, however, remain on a path of continual downward revision of growth expectations for 2014 from 6.53% (BRICs) at the beginning of the year to 5.97%. So in such an environment concerns about US liquidity have a multiplied impact. As we will discuss below, recent pressures on the share prices of these countries have begun to discount this negative dynamic. Nevertheless, the news flow from emerging countries (economic and geopolitical) remains negative.

- In the Eurozone, the combination of (marginally) improved macroeconomic data and the general tranquillity during the build-up to the German elections is contributing to a positive investment climate. As mentioned previously, the substantial decline of peripheral spreads, the rise of the euro and the decline in volatility, have essentially discounted an environment of substantial 'reciprocity' and a less austere fiscal policy in the Eurozone after the German elections, the non-implementation of which would be the cause of an increase in market volatility.

- Overall, after the summer months, the dynamics of the factors that we monitor suggest a more volatile environment. This rise could be sharp on the European crisis front. In the US, a slowdown in the Fed's QE operations, combined with improving economic data will lead to a gradual increase in volatility towards more reasonable levels. We note that the equity (implied) volatility of 12.7% (VIX Index) is very close to the all-time low (9%) and it is very likely that the rise in volatility observed in the US bond market and the gold price, will affect equity markets eventually. If our expectation for a positive surprise in macro data is confirmed, this increase will not adversely affect the upward trend in equity markets.

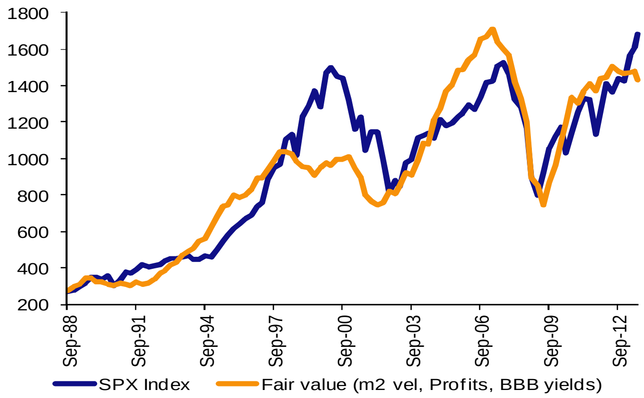
EQUITY MARKETS

- During the first quarter of 2013, the S&P500 index has started to show significant signs of overvaluation. Although the rise in the P / E ratio to 16.3 from 15.3 makes the index fairly valued (the long-term average is 16.3), the 7.5% increase in the price since the end of first quarter is not justified by the statistical model we use, which in addition to profitability, includes the BBB cost of borrowing and the velocity of M2 money (ratio of M2 to nominal GDP). According to this, the estimated rise in corporate profitability of 1.6% had a positive contribution to the fair value of 1.7%, but the rise in the cost of borrowing of 0.50% had a negative contribution of -3.4%, while the estimated drop in money velocity of 0.8% had negative contribution of -0.82%. All these factors would argue for a drop in the S&P500 of -2.6% rendering the index overvalued by 16.7% (from 8.6% in the previous quarter), which now accounts for 80% of a standard deviation of the error of the model. These levels begin to suggest the possible onset of a period of overvaluation. It is also estimated in a different context that current levels of US equity prices diverge significantly from levels consistent with long-term co-movements with other international markets (bond yields, fx, cyclical metals and other commodities).

- During the recent period of financial results announcements, of 260 companies that have announced, 73% surprised positively (by 3.3% compared to expectations), while, according to consensus estimates, profitability is expected to increase by 6% between now and the end of the year (14% for the whole of 2013), while for 2014 an increase of 12% is expected (Bloomberg). These estimates will probably prove relatively optimistic mainly because of the existing relationship between inventory and sales in the US economy. The weight of probability is on a positive surprise, as the growth rate of real consumer spending in the US at 1.8% per year is significantly lower than what would be consistent with the recent acceleration of payrolls and the significant recovery in the property market. This factor mostly counterbalances the signs of overvaluation that we observed.

- These factors argue for a neutral with negative predisposition fundamental picture. The technical picture shows a significant improvement from the previous month, remaining positive. Overall, the assessment of the S&P500 remains neutral (with a positive predisposition). We expect that at this stage the most likely scenario is the continued upward trend for the US stock market as investors continue to focus on potential positive surprises on the macroeconomic front, while, according to the latest Fed announcements, the central bank remains reluctant to significantly reduce the rate of liquidity provision in the economy.

S&P500 & Fair Value



Source: Bloomberg, Piraeus Bank Research

S&P500

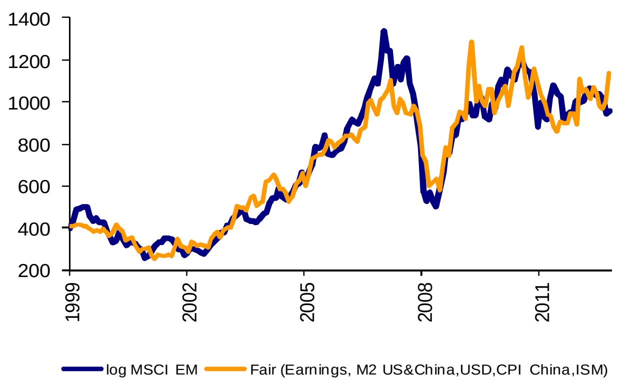
Source: Bloomberg, Piraeus Bank Research

- In emerging markets, uncertainty about the Chinese economy continues with the recent policy moves of the central bank increasing investment risk, with the exception of reducing the minimum allowable interest lending rate which is a positive development. Overall though we observe an upward trend in Chinese interest rates possibly due to both a potential acceleration of growth and inflation, but also possibly because of concerns about the indebtedness of the overall economy. Thus we observe the 7 day repo to be 100bp higher than a quarter ago, the yields on ten-year bonds 20bp higher, but also CDS in Chinese debt higher by 35bp. We note that during the recent episode when the central bank of China was absent from open market operations the 7-day repo rose to 5% (and the corresponding interbank to 28%) while CDS jumped by 147bp. So, in conclusion, part of the rise in interest rates should be attributed to increased risk of bankruptcy (which, however, remains at very low levels overall according to these market metrics).
- When it comes to profitability, although the downward trend remains (-7% yoy for the MSCI Emerging Markets), we have seen some marginal improvements in recent months. During the current period of corporate announcements, although this is still in its early stages, we are seeing a continuation of the recent trend of negative surprises.

- On the positive side we observe that recent price pressures are likely to have largely discounted a series of negative factors. In terms of valuations, the price-earnings ratio decreased to 11.47, a level that is relatively cheap (the average from 1995 is 15). Moreover, as we have mentioned in the past, other factors beyond profitability, such as monetary conditions and inflation in China and the US, show emerging market stocks to be undervalued by 18%, mainly because of the decline of Chinese inflation in the last two years and the recent decline in the rate of monetary growth M2, suggesting future conditions of monetary easing in China. This is a positive for MSCI Emerging Markets, as is the recent acceleration of the M2/M1 ratio in the US. The last factor that could have a positive impact on emerging (and also developed) markets is a potential positive surprise in the growth of consumer spending in the US.

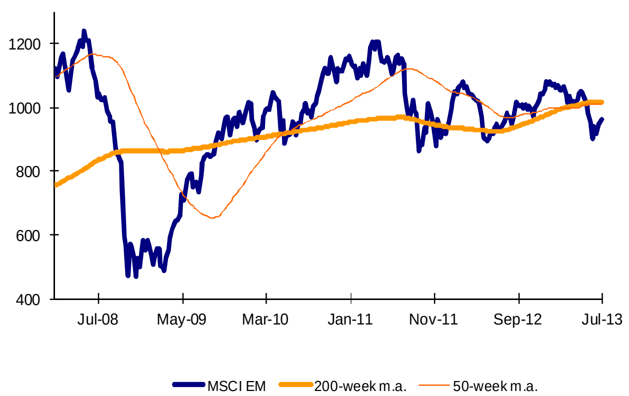
- At this stage, the fundamental picture has improved to positive (from neutral with a positive disposition), while the technical one improved from negative to neutral with a positive predisposition. Overall, the picture has improved to neutral with a positive predisposition.

Emerging Markets MSCI Index & Fair Value



Source: Bloomberg, Piraeus Bank Research

Emerging Markets MSCI Index



Source: Bloomberg, Piraeus Bank Research

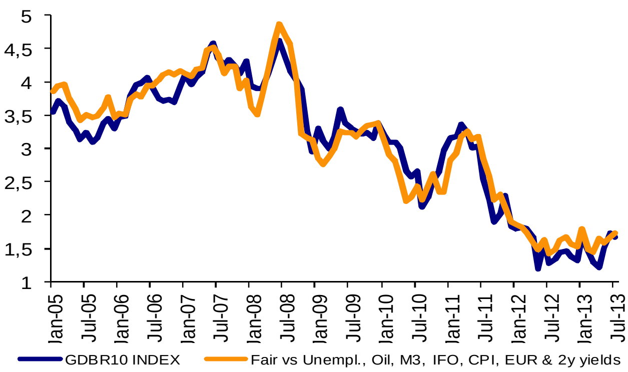
Bond Markets

- Although the majority of economic surprises were negative in both the US and the Eurozone, the Fed's rhetoric over the possibility of reducing the rate of liquidity provision along with a set of marginal positive surprises from June onwards, has led to a substantial rise in government bond yields. In the US we observe a significant increase of the yield curve 10-2 (steepening) as 10-year yields rose by 66bp while two-year ones increased by only 6bp. In Germany, where from June onwards surprises in economic data were more substantial, two-year yields rose by 16bp while ten-year ones went up by 26bp. In the US, the increasing steepness seems excessive since the Fed's intention of holding interest rates at recent lows (as mentioned in the section on the US economic data) renders current 10-year yield levels high relative to the cost of short-term borrowing.

- The decline in core consumer inflation, the decline in the annual rate of money supply rates M2-M1 and the rising price of oil would be consistent with a fall and not a rise in yields. So according to these developments, shorter maturity US bonds are less expensive (remaining very expensive though), while ten-year bonds decrease from borderline expensive and now appear marginally cheap. This improvement, however, is (more than) counterbalanced by our estimate for a major positive surprise in US consumption. At the same time, we note a significant improvement in the technical picture of US bonds, which after being oversold are showing signs of stabilizing. Overall we note a marginal deterioration in the fundamentals-quantitative picture of US bonds (which remains negative) and an improvement in the technical assessment to neutral with a positive predisposition (from neutral with negative predisposition). The overall picture is neutral with a marginally negative predisposition.

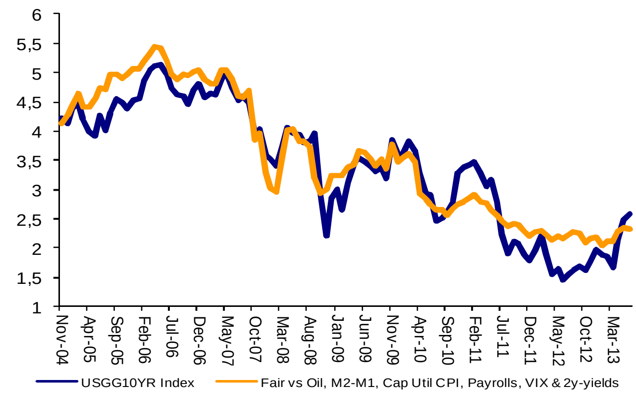
- In Germany, the rise in yields although milder is supported more strongly by the fundamentals. Inflationary concerns caused by the significant rise in oil prices and the calm on the Eurozone crisis front would correspond to upward pressures that outweigh the downside ones due to the decline in the rate of monetary expansion M3, the decline in the IFO and the rise of EURUSD. We also note an improvement in the technical picture to neutral with a positive predisposition (from neutral with negative predisposition). The overall picture is neutral with a marginally negative predisposition.

10 year German Bond Yields



Source: Bloomberg, Piraeus Bank Research

10 year US Bond Yields

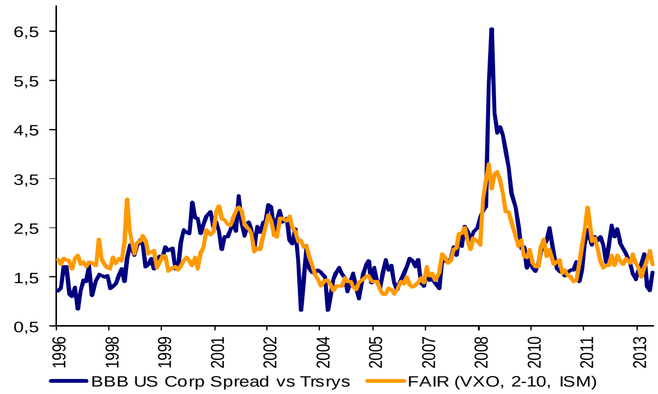


Source: Bloomberg, Piraeus Bank Research

- Corporate spreads remain low ($BBB at 182 bps), below the historical average, but at levels that are also not justified by both corporate profitability, cyclicality of inventory to sales ratios and equity volatility, which remains at very low levels with possible upward trends. The overall picture for corporate bonds remains neutral (with increased negative predisposition) in relation to government ones.

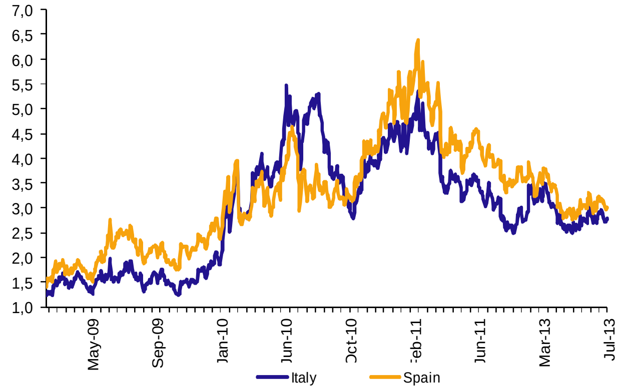
- In the Eurozone, the rise in yields was accompanied by a significant reduction in spreads (65 bps in Italy and Spain, 220 bps in Greece and 22 bps in Portugal). As we mentioned previously, we believe that the Italian and Spanish ten-year spread against Germany of close to 3% does not adequately reflect the risks related to Eurozone cohesion, especially in light of the very slow progress and possibly inadequate banking and fiscal integration. Thid could be a product of the combination of the "imposed" calm due to the German election and the untested Draghi promise to do "everything possible to save the Eurozone" of July 2012.

$BBB Spreads & Fair Value



Source: Bloomberg, Piraeus Bank Research

10-year Spreads vs. Germany



Source: Bloomberg, Piraeus Bank Research

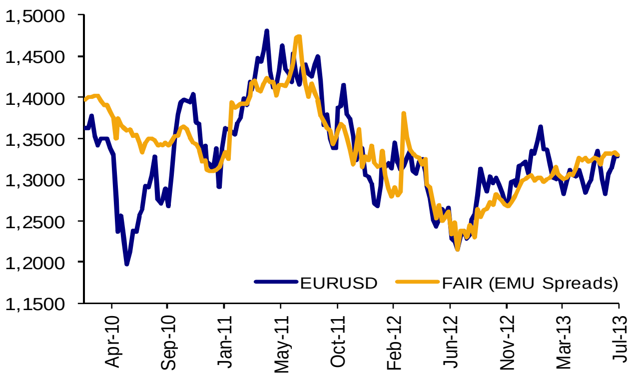
Forex Markets

- The EURUSD exchange rate has strengthened by about 3.1% since the end of the first quarter of 2013. Despite concerns about limiting policies of quantitative easing by the Fed and the substantial rise in long-term US interest rates, the dollar did not strengthen against the euro. Apart from the positive effect of the continuing decline of regional spreads described above, the economic data in the Eurozone, although relatively mild, surprised markets more positively than the US ones (especially from June onwards). The effect of this development was reflected more by the bond yield curve, increasing the two-year spread between Germany and USA. Beyond these developments, in the macroeconomic field, we have started to observe a trend of relative slowdown in M2 monetary growth in the US versus that of the Eurozone which boosts our long-term estimate for the European currency. At the same time, we stress that while the US debate revolves around a slowdown in US quantitative easing, in the Eurozone banks have already started to repay the LTRO's. As a result, we have seen the ECB's balance sheet shrink while in the US we simply have uncertainty about the decrease in the rate of expansion of the Fed's balance sheet, a euro-positive development. The drop in the price of gold (which reflects a return to confidence in the dollar) is a negative for the European currency.

- At this stage the rate appears fairly valued in relation to the Eurozone risks (as depicted in the current periphery spreads), positive in relation to the external trade position with the US (surplus), neutral with respect to the Eurozone-US cyclical economic signs and high with respect to the Germany-US bond yield spreads (of average to high duration). Overall, the fundamental-quantitative picture of the exchange rate remains neutral while the technical picture is improving to positive. The overall picture improves to neutral with a positive predisposition.

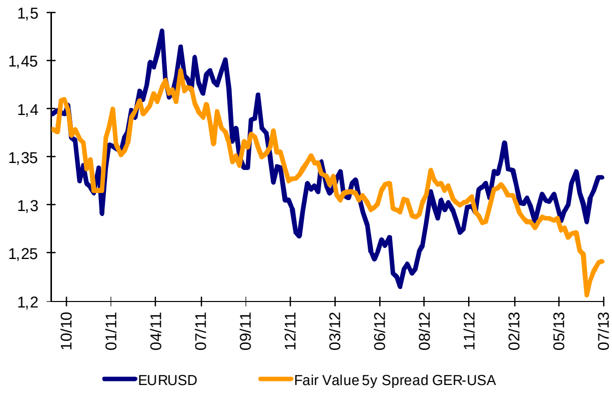
- In terms of a more qualitative approach however, we have often mentioned that pressures on the borrowing costs of countries in the European periphery after the summer of 2012 actually exaggerate the progress of European integration and at these levels a widening of spreads is more likely than a further contraction. We have often referred to the end of the German elections as a catalyst for a rise in volatility. For the next 1-3 months we expect variation within the range from 1.2850 to 1.3400. On a six-month horizon we expect a 1.2300 to 1.3500 range. Our 12-month target remains 1.26, with a heightened possibility of an upward revision.

EURUSD & Eurozone Spreads



Source: Bloomberg, Piraeus Bank Research

EURUSD, GER-US 5 year Spread

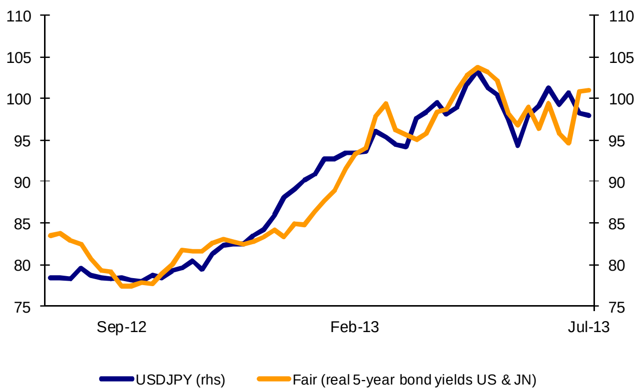


Source: Bloomberg, Piraeus Bank Research

- The USDJPY rate remained under upward pressure (6% since the end of first quarter). According to statements from the Bank of Japan, recent improvements in the economic dynamics of Japan (rising inflation, real growth and the Tankan index) do not point to a further acceleration in the rate bond market purchases (QE), which potentially will tend to halt the rate of Yen weakening. On the other hand, the yen is particularly sensitive to higher long-term US interest rates and the prospect of reducing the rate of quantitative easing in the US causes upward pressure. Since the end of the first quarter real yields on 5-year US bonds have risen by 80bp more than the equivalent Japanese bonds, a movement that supports the rise in USDJPY. However, in accordance with the previous sections, rising US yields are not sufficiently supported by economic data so far and we are likely to enter a period of range trading in yields and the USDJPY. One more reason for such a possibility is the improvement in the trade balance where a deficit of 1617 billion yen has been corrected to 180. In the medium term we expect variation in a broad range of 95-105. Our 12-month target is 95.

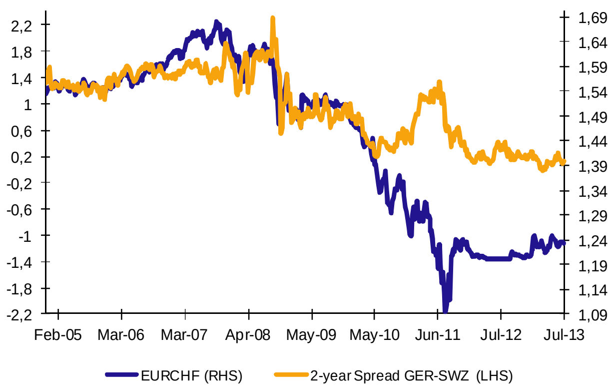
- The EURCHF pair has traded in a band of 1.27-1.21 ytd with upward trends associated with improvements on the Eurozone crisis front. As we have mentioned, these improvements are relatively strong at least as they are measured by the significant contraction in borrowing costs at the periphery. However, the rate of 1.2360 does not adequately reflect this improvement which could reflect scepticism on the part of the market. Another explanation would be that the data in Switzerland have shown significant improvement, compared to the core of the Eurozone, suggesting a re-strengthening of the franc. Some economic data supports such an assumption, for instance, the rise in inflation (from -0.2% to 0.2% per annum), the rise in the trade surplus, and the acceleration of money supply M3 to 12%, while the PMI manufacturing index at 52, is higher than that of Germany (50.3). However, the bond market does not seem to anticipate any significant economic advantage as spreads between Germany and Switzerland have not shown any decline thus still pointing to an undervalued EURCHF (the franc overvalued). According to our overall expectations, as we approach the German elections, the demand for safe havens is likely to increase again and so the rate will not diverge considerably from the "defence" level of 1.20.

USDJPY & 5year US-Japan Real Spread



Source: Bloomberg, Piraeus Bank Research

EURCHF-2 year spread Germany-Switzerland



Source: Bloomberg, Piraeus Bank Research

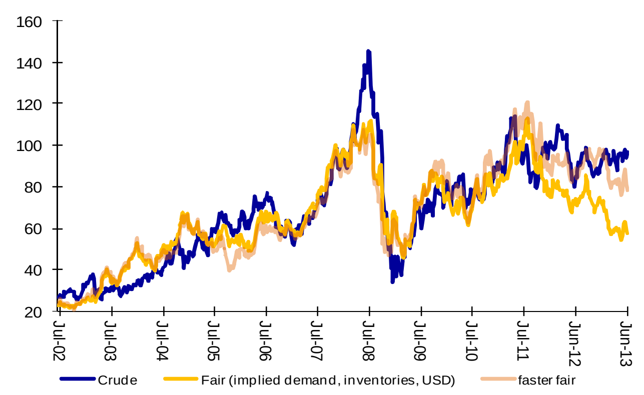
Commodities Markets

- The CCI Index has declined since the end of the first quarter (-7%), with the cyclical metals retracting (London Metal Exchange Index -7%) while precious metals came under significant pressure compared with the end of the first quarter (-16% gold, 28% silver, platinum -8%). Milder pressures were exerted on agricultural commodities (-4%). In the energy market, natural gas suffered heavy losses (-9%) while, conversely, the price of crude oil rose by 9% although Brent fell by 2%. After the losses observed since the beginning of the year the technical picture starts to improve, but remaines negative (in terms of weighted index CCI). In addition to this, commodities (especially cyclical metals) have reached levels where a large amount of concerns about Chinese and US growth is likely discounted. The overall picture remains marginally negative.

- During the last quarter, the fundamentals of the oil market have made improvements which would correspond to a rise of just 7% in our fair value estimations. This is less than the observed rise in crude (11%) probably due to geopolitical concerns resulting from developments in Egypt and Syria. So while the rise of the dollar in trade-weighted terms and the rise of production observed would be consistent with a drop in crude of 8%, the growth in demand would suggest a rise of 15%. The result of these movements is the further widening of the gap to the fair price. The possibility of a positive surprise in US growth (via consumer spending) compensates to a great extent this increased overvaluation, resulting in only a slight deterioration in the quantitative-fundamental picture which, however, remains significantly negative. At the same time we observe an improvement in the technical picture from neutral with positive predisposition to positive. The overall picture is neutral with a negative predisposition.

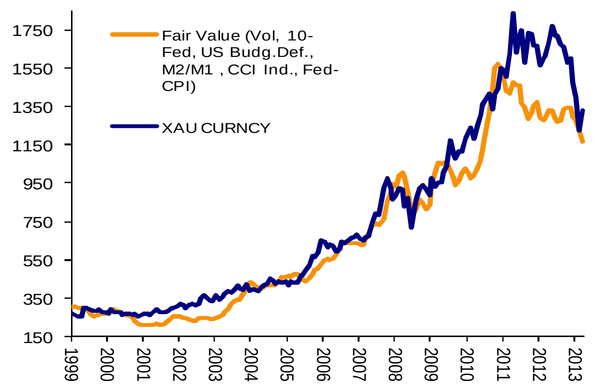
- Although gold has reacted positively by 14% from the lows of June (1200) it remains 16% lower than it was at the end of March. The recent upward reaction in the gold price renders it overvalued again relative to other markets (mainly due to the underperformance of the commodities in relation to the dollar), but also because of fundamental movements that have a negative relationship with the price of gold (the US Federal deficit fell from 6.3% to 5.7% of GDP). Thus we observe a deterioration in the fundamental-quantitative picture to negative (from neutral with a negative predisposition, while the technical picture is again negative (from neutral). The overall picture is negative.

Crude Oil & Fair Value



Source: Bloomberg, Piraeus Bank Research

Gold & Fair Value



Source: Bloomberg, Piraeus Bank Research

Economic Analysis & Markets Division			
Lekkos Ilias	Chief Economist	2103288120	Lekkosi@piraeusbank.gr
Harvey Evangelos	Manager	2103298593	Eharvey@ate.gr
Fakiolas Efstathios	Economic Analyst	2103298777	Sfakiolas@ate.gr
Greek Economy			
Staggel Irini	Economist	2103288192	Staggelir@piraeusbank.gr
Kefalas Konstantinos	Economic Analyst	2103739369	Kefalask@piraeusbank.gr
Developed Economies			
Patikis Vassilis	Head of Developed Markets	2103288855	Patikisv@piraeusbank.gr
Polychronopoulos Dionysis	Economic Analyst	2103288694	Polychronopoulosd@ piraeusbank.gr
Papakostas Valantis	Economic Analyst	2103298778	Cpapakostas@ate.gr
Developing Markets			
Rotsika Dimitria	Economic Analyst	2103288365	Rotsikad@piraeusbank.gr
Margariti Konstantina	Junior Economic Analyst	2103697246	Kmargariti@ate.gr
Sectoral Studies			
Dagalidis Athanasios	Senior Economist	2310293564	Athanasios.Dagalidis@ piraeusbank.gr
Vlachou Paraskevi	Economic Analyst	2103335631	VlachouPar@piraeusbank.gr
Fragoulidou Ifigeneia	Junior Economic Analyst	2310293403	a313@piraeusbank.gr
Secretary			
Papioti Liana	Secretary	2103288187	PapiotiE@piraeusbank.gr