



enjoyed by its neighbors over the past decade, a result of onerous regulation and weak productivity growth. We anticipate that this FDI gap will begin to close as 2013's reforms bear fruit.

Second, growth is set to be sharply stronger. Our economist has noted that the main reason behind the disappointing performance of Mexican manufacturing relative to the US this year was the lack of growth in high-value sectors to which the Mexican economy has become more sensitive. We do not anticipate this dynamic to continue. At the same time, the drag caused by last year's lack of government spending will end, with the IMF showing Mexico to possess one of the most positive fiscal impulses in EM next year. We therefore like to be long MXN against USD, targeting 12.50. Given the positive outlook for oil production and FDI, we also like playing MXN strength against other oil producers, in particular COP and RUB.

In contrast, the Brazilian real will likely face another challenging year. The current account has only improved modestly in spite of significant FX adjustment and the income balance remains a concern as a decade of large scale FDI inflows are 'paid back.' Moreover, while FX reserve coverage remains ample, the BCB has signaled it will adopt a more cautious stance over FX intervention over the course of the coming six months, as the central bank's swap book grows to up to 25% of total reserves. Finally, the upcoming election is unlikely to result an improvement in positive sentiment around the government's fiscal policies. We expect USD/BRL to trade in a high (2.25-2.50) range, ending the year at 2.40.

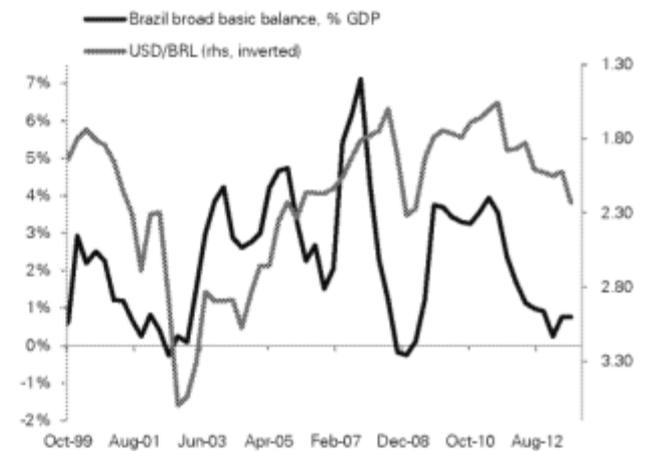
Regarding the Andeans, we foresee a difficult period for COP and a better backdrop for CLP and PEN. With respect to COP, the upcoming election year also represents a concern, with President Santos facing a strong challenge from the populist right. There are also question marks surrounding the outcome of peace negotiations with the FARC. Exports are expected to suffer as Venezuela's economic crises drags on. Combined with a muted outlook for oil prices, this suggests the COP will likely be the best short among Lat Am currencies next year. We like to play this versus a rather depressed CLP, which should benefit from a possible upturn in China and possible lower oil prices. PEN should also be helped by the uptick in growth (especially after last year's slowdown) and spillover effects from the expected increase in copper production.

Altogether we like to be long MXN vs COP and RUB, long CLP vs COP, long PEN and see BRL underperforming the forwards while possibly trading in a 2.25-2.50 range.

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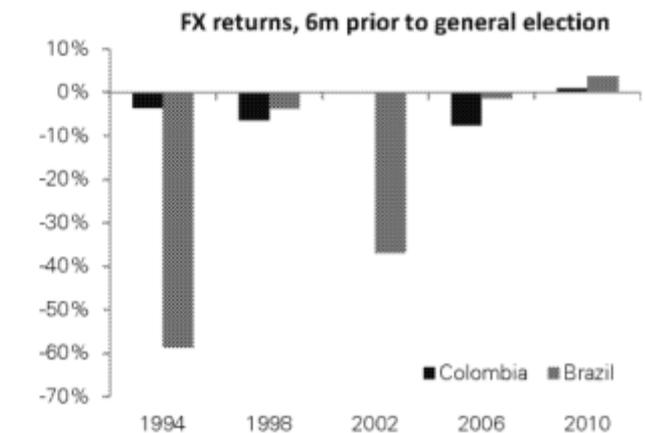
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Basic balance suggests still scope for BRL downside



Source: Deutsche Bank, Bloomberg Finance LP

Elections not good for BRL and COP



Source: Deutsche Bank, Bloomberg Finance LP