MARK CARNEY USHERS IN A LEADERSHIP CHANGE AT THE BANK OF ENGLAND

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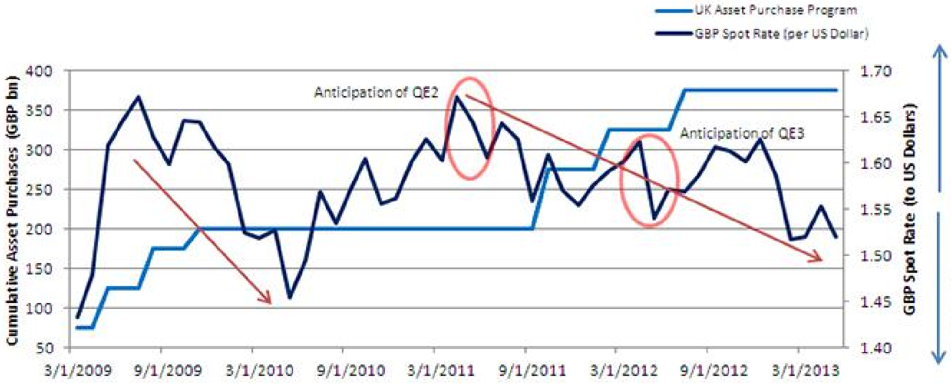
Mark Carney assumes the role of governor of the Bank of England (BOE) today. Carney, the eighth governor of the Bank of Canada (BOC) and the chairman of the G20 Financial Stability Board, has been widely credited for his aggressive and cutting-edge monetary policy stances, which helped Canada avoid the worst of the 2007 financial crisis and subsequently resume growth by mid-2009. Given his bold actions and foresight, his focus on growth-related policies and his desire to achieve a flexible inflation-targeting regime , I view Carney's appointment as a positive development. The highlight of Carney's tenure as BOC governor remains the decision to cut interest rates by 0.5% in March 2008, just one month after his appointment, while the European Central Bank (ECB) delivered a rate increase in July 2008.[1] Carney displayed admirable foresight in anticipating the far-reaching implications of the leveraged-loan crisis . Additionally, when policy in Canada had hit its lower bound , he introduced a nonstandard monetary policy tool called "conditional commitment" in April 2009 that provided forward-looking policy guidance, which served to boost Canadian credit conditions and market confidence. This track record contrasts vastly with that of his predecessor at the BOE, Mervyn King, who has often been criticized for mishandling the pace of rate cuts in 2008 and has been held responsible for the persistently weak UK growth picture. **New Objectives for Bank of England** In March of this year, Chancellor of the Exchequer George Osborne handed the BOE and Governor-elect Carney sweeping new powers to stimulate economic growth and job creation in order to reignite Britain's lackluster economy. Under the new regime, the Treasury outlined joint objectives for the BOE to maintain price stability and support the government's economic policies, including its "objectives for growth and employment."[2] Given the changes to the BOE mandate and its newfound flexibility, we believe that Carney will be able to potentially draw upon a variety of unconventional monetary policy tools and exert his agenda more effectively. In terms of policy potential, the government budget made it clear that Carney will be given significant latitude to embark on expansionary policies. Further, the chancellor rationalized changes in the monetary policy mandate by stating that "low and stable inflation is a necessary but not sufficient condition for prosperity."[3] Given Carney's reputation for swift and deep policy action, he is expected to deliver explicit forward guidance on the future path of overnight interest rates and to extend quantitative easing (QE) in the event that growth continues to lag; both of these policies have the potential to engender further British pound (GBP)[4] weakness against currencies such as the U.S. dollar.

Prevailing Currency Weakness Preceding and During Episodes of Quantitative Easing March 31, 2009 – May 31, 2013



• During the anticipation phase of previous rounds of QE, the GBP weakened ahead of the formal policy announcements. • QE1: QE1 was announced on 03/05/2009[5] and encompassed a value of GBP 200 billion. The policy was initiated in March of 2009 and completed in January of 2010. Although the pound appreciated roughly 11% in that period, markets internalized the impact of balance sheet expansion, and the currency subsequently depreciated by about 16% from August 2009 to May 2010. • QE2: QE2 was announced on 10/06/2011[6] and encompassed a value of GBP 125 billion. From the initiation of the policy in October of 2011 to its completion in May of 2012, the pound depreciated about 4.5%. • QE3: QE3 was announced on 07/05/2012[7] and encompassed a value of GBP 50 billion. From the initiation of the policy in July of 2011 to its completion in November of 2012, the pound depreciated about 4%. Carney has also spoken widely in favor of unconventional and aggressive monetary policy action. He recently described Japan's actions as "a bold policy experiment" from which Europe could draw lessons.[8] Earlier this year at the World Economic Forum in Davos, Switzerland, Carney hinted strongly at a monetary policy overhaul when he said that central bankers should be prepared to take aggressive measures to help economies achieve what he called, "escape velocity."[9] This is especially crucial for the UK, which has been averaging 0.25% year-over-year growth in the past 6 years.[10] We believe that Carney's appointment could spark some much-needed change in the BOE's policies, potentially contributing to GBP currency weakness and stronger economic growth—the pound certainly has recently responded to changes in monetary policy. Carney may be just the right catalyst to get the United Kingdom moving in a more positive direction, as he did for Canada. [1] Source: Heather Stewart, "Mark Carney: Bank governor's journey from wilderness to heart of the City," The Guardian, June 13, 2013. [2] Source: Budget 2013: Chancellor's statement – Oral statement to parliament, https://www.gov.uk/government/speeches/budget-2013-chancellors-statement. [3]Source: Budget 2013: Chancellor's statement – Oral statement to parliament, https://www.gov.uk/government/speeches/budget-2013-chancellors-statement. [4]British pound vs. the U.S. dollar [5] Source: "Bank of England Reduces Bank Rate by 0.5 Percentage Points to 0.5% and Announces £75 Billion Asset Purchase Programme," Bank of England Publications. [6] Source: "Bank of England Maintains Bank Rate at 0.5% and Increases Size of Asset Purchase Programme by £75 billion to £275 billion," Bank of England Publications. [7] Source: "Bank of England maintains Bank Rate at 0.5% and increases size of Asset Purchase Programme by £50 billion to £375 billion," Bank of England Publications. [8]Source: Katie Allen, "Mark Carney warns Europe against lost decade of austerity," The Guardian, May 21, 2013. [9] Simon Kennedy & Jennifer Ryan, "Carney Says Policy Must Achieve 'Escape Velocity,'" Bloomberg, January 28, 2013. [10] Source: World Economic Outlook, International Monetary Fund (IMF), April 2013.

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DEFINITIONS

G20 : Group of 20 of the world's largest economies that meets regularly in order to coordinate global economic policies.

Monetary easing policies : Actions undertaken by a central bank with the ultimate desired effect of lowering interest rates and stimulating the economy.

Lower bound : : Central bank target rates that are at or close to zero, implying limited room for further easing.

Quantitative Easing (QE) : A government monetary policy occasionally used to increase the money supply by buying government securities or other securities from the market. Quantitative easing increases the money supply by flooding financial institutions with capital, in an effort to promote increased lending and liquidity.