CIBC FICC Strategy and Economics

MONTHLY FX OUTLOOK

October 2023

USD – On Fire for Longer

Currency	What's changed
USD	The US economy is less vulnerable to 'higher for longer' rates. We expect investors to add to USD longs as the Fed is likely to be less reactive to weaker data relative to other central banks.
CAD	Shaky real activity is likely to prevent the need for additional tightening from the Bank of Canada this year.
EUR	With policy rates likely at terminal, the discussion now turns towards PEPP and energy supplies ahead of the winter.
GBP	The BoE is likely done raising rates – and the combination of weak activity and a softening labour market will weigh on the GBP in the near-term.
JPY	Intervention risks notwithstanding, JPY bulls will need additional patience in the months ahead.
Commodity FX	We expect the NOK to outperform due to a more constructive terms of trade backdrop alongside idiosyncratic drivers.
LATAM FX	The path of least resistance is for a weaker MXN going forward.
FX Asia	Though Chinese data stabilized in September, the fundamental backdrop still looks soft for the coming months.

Currency outlook

End of period:	Oct 11, 2023	Q4 '23	Q1 '24	Q2 '24	Q3 '24	Q4 '24	Q2 '25	Q4 '25
USD / CAD	1.36	1.39	1.37	1.34	1.33	1.31	1.30	1.29
EUR / USD	1.06	1.03	1.05	1.09	1.12	1.14	1.15	1.16
USD / JPY	149	145	140	135	130	120	120	118
GBP / USD	1.23	1.19	1.21	1.25	1.29	1.31	1.32	1.34
USD / CHF	0.91	0.94	0.93	0.92	0.91	0.89	0.88	0.88
USD / SEK	10.87	11.01	10.30	9.96	9.65	9.47	9.35	9.30
AUD / USD	0.64	0.62	0.63	0.65	0.66	0.68	0.70	0.72
NZD / USD	0.60	0.58	0.59	0.60	0.61	0.63	0.65	0.67
USD / NOK	10.81	10.92	10.25	9.84	9.59	9.39	9.30	9.25
USD / ZAR	19.04	19.15	18.75	18.45	18.15	17.65	17.00	16.90
USD / BRL	5.06	5.20	5.20	5.20	5.40	5.00	5.20	5.40
USD / MXN	17.99	18.00	18.50	19.00	19.20	19.00	18.75	18.50
USD / COP	4231	4300	4300	4400	4500	4300	4100	3900
USD / CLP	930	900	920	880	850	820	840	860
USD / CNY	7.29	7.35	7.38	7.35	7.30	7.25	7.20	7.10

Other crosses

End of period:	Oct 11, 2023	Q4 '23	Q1 '24	Q2 '24	Q3 '24	Q4 '24	Q2 '25	Q4 '25
CAD/JPY	110	104	102	101	98	92	92	91
AUD/CAD	0.87	0.86	0.86	0.87	0.88	0.89	0.91	0.93
GBP/CAD	1.67	1.65	1.66	1.68	1.72	1.72	1.72	1.73
EUR/CAD	1.44	1.43	1.44	1.46	1.49	1.49	1.50	1.50
EUR/JPY	158	149	147	147	146	137	138	137
EUR/GBP	0.86	0.87	0.87	0.87	0.87	0.87	0.87	0.87
EUR/CHF	0.96	0.97	0.98	1.00	1.02	1.01	1.01	1.02
EUR/SEK	11.52	11.34	10.82	10.86	10.81	10.80	10.75	10.79
EUR/NOK	11.45	11.25	10.76	10.73	10.74	10.70	10.70	10.73

Key indicators – Latest data point

End of period:	Quarterly real GDP (y/y %)	CPI (y/y %)	Current acct (% of GDP)	Central bank rate (%)
US	2.40	3.7	-3.20	5.38
Canada	1.10	4.0	-0.99	5.00
Eurozone	0.47	4.3	0.41	4.00
Japan	1.73	3.2	2.22	-0.10
UK	0.56	6.7	-1.79	5.25
Switzerland	0.59	1.7	9.82	1.75
Sweden	-0.80	7.5	5.02	4.00
Australia	2.07	6.0	1.18	4.10
New Zealand	1.81	6.0	-7.50	5.50
Norway	0.70	3.3	17.49	4.25
South Africa	1.68	4.8	-1.43	8.25
Brazil	3.30	4.6	-2.66	12.75
Mexico	3.73	4.5	-1.19	11.25
Colombia	3.00	11.0	-5.08	13.25
Chile	-0.63	5.1	-3.99	9.50
China	6.33	0.1	2.20	

USD

Bipan Rai

Higher for Longer Means the US Dollar Gets Stronger

DXY – Q4 2023: 108.04 | Q1 2024: 105.65

Proxies for FX positions are flagging a significant shift that's underway when it comes to market views on the US dollar. For instance, net USD skews for non-commercial investors (or speculators) have aggressively pivoted from heavy shorts to heavy longs over the past few months. Meanwhile, asset managers are in the midst of pulling the plug on bearish dollar positions accumulated in the early part of this year. The latter is particularly noteworthy given that this investor class tends to be slower moving, and far more 'stickier' when it comes to positioning. Indeed, we think this shift touches on important themes that have been integral to the US dollar's rally over the past few months, and which is likely to extend going forward.

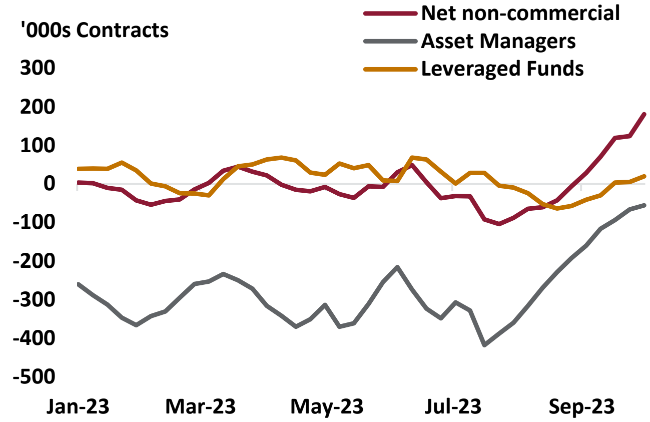
For instance, the most salient takeaway from the recent FOMC, and corresponding Fedspeak, has been that administered rates will remain "higher for longer". That includes the possibility of another rate hike before the year is out – which stands in stark contrast to what the market was pricing in earlier in September. When taken with stronger than expected incoming data, the implied message from the Fed is that it feels that the domestic economy will be a lot more resilient to restrictive policy than it thought earlier in the summer.

And it's the latter point that we think represents a key reason for why investors are keen to pare USD shorts. A more resilient US economy means that the Fed now sees a shallower path for easing in the years ahead, which leads to a repricing in the market and restricts shorts rates from falling too much. The effect of this 'stabilization' means that the market is making the connection to a later start for the easing cycle in the US.

However, this 'stabilization' also matters in the sense that it brings cross-border vulnerabilities into focus. As central banks are mostly all consistent with the "higher for longer" mantra, the reality is that economies with a relatively higher profiles for private sector debt (like Australia and Canada) are particularly exposed the longer rates remain at these levels. That's especially true given the considerable mortgage reset risks over the coming years. The US is less exposed from this lens given the significant deleveraging that we saw post-2008 alongside structural differences in the mortgage market (including fixed rates for longer terms).

Forward OIS still suggests that other central banks are expected to ease rates by less than the Fed by the end of next year. That's something that we expect to see corrected going forward. Indeed, we still see additional scope for investors to add to US dollar longs into the end of this year.

Chart 1: Net USD Longs in 2023 (By Investor Type)



Source: CFTC, CIBC Capital Markets

CAD

Katherine Judge and Avery Shenfeld

More Weakness Before a Revival in 2024

USD/CAD – Q4 2023: 1.39 | Q1 2024: 1.37

Canada's economy has remained on shaky ground in the third quarter, which will likely prevent any further tightening by the Bank of Canada. Although inflation measures remain above target, signs of softening in the labour market, particularly job vacancies, portend to a cooling in inflation ahead. The detail of the September employment report showed a decline in hours worked, while hiring was concentrated in part-time positions, pointing to an extended sluggish trend in GDP. With markets almost fully priced for another quarter point BoC hike this year, and not placing high enough odds on cuts next year, a recalibration will see the loonie end 2023 weaker, with USDCAD likely reaching 1.39 by then.

In contrast, the US data has extended its resilience, with GDP on an accelerating path in the third quarter, which has caused markets to push back rate cut expectations in 2024. There's a material risk of another Fed hike this year, depending on how firm core CPI inflation looks ahead. However, with excess savings fading, we see the potential for a negative GDP print at the turn of the year, which could also cause the Fed to start to cutting interest rates in Q2 2024, albeit a little after the BoC. As the market shifts to account for what we see as a higher likelihood of Fed cuts next year, that will weigh on the broad USD in 2024, supporting the loonie in the process, with USDCAD likely ending 2024 at 1.31.

EUR

Jeremy Stretch

Politics and Weather are the Immediate EUR Headwinds

EUR/USD – Q4 2023: 1.03 **|** Q1 2024: 1.05

After taking the deposit rate to 4.00%, which we consider the terminal threshold, the ECB is now adopting its own "higher-for-longer" narrative. The realization of a rate peak has helped pace EUR depreciation versus the bulk of the majors across Q3. Indeed, a 3% slide versus the USD represents the worst performance in four quarters. Headlined by sliding PMI and Ifo weakness, the Eurozone has witnessed a deterioration in both real economy data and survey sentiment. Moreover, advancing fragmentation concerns (BTP-Bund spreads have widened by around 40bps since the end of August) sit alongside a substantive correction in aggregated positioning - with aggregated EUR longs (real money and leveraged holdings) having fallen by almost three quarters in the last two months. As macro headwinds show no signs of immediate easing, we anticipate scope for additional positioning for EUR downside.

The data, including a faster-than-expected moderation in August flash HICP, supports our notion of conventional policy tightening having run its course. Such a presumption underlines the ECB policy battle switching to discussion of a faster pace of QT. We can expect the ECB to continue to drain liquidity out of the system across 2024, containing EUR downside. However, we can also expect immediate EUR headwinds to persist through early Q4 2023, not least in view of ongoing political risks into upcoming elections and the weather. In terms of the latter, we would note that the Eurozone remains vulnerable to a harsh winter even though its gas tanks are currently 95% full.

JPY

Jeremy Stretch

The Selloff in the Long-End Hits the JPY

USD/JPY – Q4 2023: 145 **|** Q1 2024: 140

USD/JPY remains a function of 10-year UST-JGB spreads. Consequently, as US 10-year yields breached 400bps, we also saw USD/JPY probe above the 150 mark. USD/JPY impetus comes despite persistent intervention warnings from Japanese officials. Despite repeated references regarding watching markets with urgency, allied to standing ready to act against excessive moves, the market has proved to be largely unreactive.

The unexpected uptrend in the key Tankan business survey, the large manufacturers index advanced to +9, supports a graduated recovery narrative. However, the latest BoJ Summary of Opinions (for the September meeting) details that the Bank has split into two camps. Those advocating status quo (including Governor Ueda) detail that it remains appropriate "to continue with easing patiently", and that there is "no need for additional YCC tweak with yields stable." Those advocating an early adjustment referenced "coming closer to achieving the price target", adding that there is a "good chance 2024 wage gains to top this years". The uptick in the headline Tankan and recent retail sales gains appear increasingly consistent with the concept of gradually bringing forward the timing of policy adjustment. However, the 31 October BoJ meeting remains far too soon for a shift. Indeed, we remain mindful of the fact that Ueda stated last month that the "distance to ending negative rates" has not changed much. The economy may be gradually moving towards the achievement of price stability but there is still a distance to travel. Hence, intervention risks notwithstanding, we would reiterate the view that JPY bulls may need to remain patient, likely towards the December BoJ.

GBP

Jeremy Stretch

The BoE is Done, but Will Leave the Door Ajar

GBP/USD – Q4 2023: 1.19 **|** Q1 2024: 1.21

After 14 straight hikes, the BoE opted to hold the bank rate at 5.25% at their September policy meeting. We would note that the decision was a 5:4 split vote, with the Governor utilizing a casting vote. Market confidence regarding the risks of a 15th (and potentially final) rate hike had proved to be compromised by August CPI easing back to 6.7%, equating to the lowest level since February 2022. Having held rates in September, it appears that the BoE is mindful of the lagged impact of the 515bps of accumulated tightening thus far in the cycle. Indeed, we now assume that the BoE has likely concluded its policy tightening.

Ahead of the 2 November MPC, which includes updated macro forecasts, we'd expect the BoE to maintain the presumption that a "further tightening in monetary policy would be required if there were evidence of more persistent inflationary pressures". Key to broad inflation persistence remains both business inflation expectations and second-round wage effects. Signs of a graduated easing in the labour market, as forward-looking PMI survey data remains in negative territory, in particular construction, points towards policy inertia. BoE chief economist Pill recently used a "Table Mountain" metaphor for monetary policy, namely policy remaining restrictive for a protractive period, rather than spiking to beyond 6%. This is the higher for longer mantra UK style. The UK rate spectrum remains a function of inflation expectations and growth assumptions. The paring in terminal rate expectations, allied to ongoing data headwinds point towards ongoing GBP challenges into year-end.

CHF

Jeremy Stretch

With Headline Inflation Below the Target, the SNB is Likely Done With Tightening

EUR/CHF – Q4 2023: 0.97 **|** Q1 2024: 0.98

The SNB held rates at 1.75% at their recent quarterly policy decision, confounding market expectations in the process. While the SNB may continue to suggest that the battle against inflation has yet to be won, it seems likely that they are done and Swiss rates have reached a terminal threshold. Despite a policy of immediate inertia, the SNB's latest policy assessment still detailed that it cannot rule out further tightening to ensure price stability over the medium term. That being said, current headline inflation is running below the 2% target threshold (1.7%), while annual core prices have decelerated for seven straight months, leaving the annual rate at 1.3%. We have not witnessed a lower reading since January 2022. Indeed, as the SNB moderated its inflation profile, we can expect them to continue to hold rates at present levels with the next move likely a cut in Q2 2024.

Beyond conventional policy adjustment, the SNB statement suggested that they would remain active in the FX market. However, moderating inflation pressures, allied to the overvalued CHF, points toward a graduated moderation in the SNB's appetite to sell foreign currency. A reduction in FX activity is set to combine with widening spreads, including in 10 years, to encourage additional USD/CHF upside with moves toward the mid-point of the one-year trading range around 0.9350.

SEK

Jeremy Stretch

The Riksbank Doubles Down on SEK Rhetoric

EUR/SEK – Q4 2023: 11.34 **|** Q1 2024: 10.82

The Riksbank extended policy tightening to a cumulative 400bps post last month's well-discounted 25bps hike. Moreover, despite ongoing real estate concerns the Riksbank moderately revised its policy path and now assume 4.09% at year-end, compared to 4.05% previously. The moderate upgrade leaves open the risks of an additional hike before year-end. However, the Riksbank is now transitioning to a "data-dependent" approach, in line with broad central bank orthodoxy. The policy narrative adjustment underlines an increased focus on incoming data. As the economy surprise index again trends lower, it's unsurprising that the market is currently only pricing in around 9bps for the 23 November meeting.

A switch to "data dependence" may curtail rate hike assumptions at the margin. However, the Riksbank has doubled down on references regarding currency undervaluation. Governor Thedeen referenced a 10-15% undervaluation for SEK in the wake of the recent policy decision. Beyond mere railing against currency weakness, it matters via the impact on imported inflation, with the central bank pledging to support the SEK by spending around a quarter of its FX reserves over the course of the next 4-6 months. The presumption of SEK purchases has helped to encourage EUR/SEK to retreat from recent extremes near 12.00. However, the immediate problem for the Riksbank is that the high-beta status of the SEK, allied to Germany's macro linkages, continues to work against it. Only when macro headwinds moderate and risk sentiment improves should we expect EUR/SEK to move durably below the 200-day moving average.

Commodity FX

NOK

Jeremy Stretch

One Last Hike for the Norges Bank?

EUR/NOK – Q4 2023: 11.25 **|** Q1 2024: 10.76

The Norges Bank was a leader in terms of policy tightening, beginning back in September 2021. However, not only did the recent meeting extend the tightening cycle (the deposit rate is now at 4.25% after a second consecutive 25bps hike), it also underlined an upgraded rate profile which suggests a higher peak than that assumed back in June. Having hiked rates on 13 occasions, the Norges Bank remains biased towards an additional 25bps prior to year-end. Absent a material and unexpected retreat in the data, we would look for rates to reach a terminal at 4.50%, by year-end.

However, not only is the central bank now embracing a higher rate peak, they have also adopted their own "higher for longer" mantra. Hence, rather than rates peaking at the end of 2023, as per the June Monetary Policy Report, the Norges Bank now assumes the rolling over in rate expectations will be delayed until Q4 2024. Moreover, rates are expected to be some 32bps higher at the end of the forecast profile (end 2026) than previously assumed.

Contingent to the more hawkish narrative is a higher oil price profile than previously discounted alongside an improved external environment, albeit the veracity of that latter judgment can perhaps be questioned. That being said, the combination of additional tightening, energy price resilience, supporting an already exaggerated current account surplus, allied to ongoing labour market tightness points towards EUR/NOK trading well below July/August extremes into early 2024.

AUD

Noah Buffam

Languishing AUD

AUD/USD – Q4 2023: 0.62 **|** Q1 2024: 0.63

AUD/USD continued to decline in September, as broad dollar strength and headwinds to global growth caused the high beta currency to decline. We've revised our Q4 2023 forecast for AUD/USD down to 0.62, as we expect dollar strength to persist into year-end. Global growth headwinds are likely to continue to weigh on the AUD, as European growth rolls over and the Chinese economy remains weak. Thus, it is not until Q2 2024 when we expect AUD/USD to begin rally. We expect the pair to eventually reach 0.68 by Q4 2024.

We also expect the RBA to hike rates once more in November. It appears likely that the RBA's Q4 2023 trimmed mean and headline inflation forecasts are too optimistic given the momentum in core CPI and rally in energy prices. The RBA will likely be hesitant to revise higher their inflation profile given that inflation is expected to only return to the target band by Q4 2025. A final hike to 4.35% in November will help the RBA feel more confident that they can reach target inflation by end of 2025. While a hike should lead to some short term gains in AUD, we expect a stronger dollar and declining global growth to dominate AUD/USD movements.

NZD

Noah Buffam

A Confluence of Headwinds

NZD/USD – Q4 2023: 0.58 **|** Q1 2024: 0.59

Even as the USD enjoyed a strong September, NZD/USD managed to eke out a small gain on the month. The outperformance of NZD against the crosses was due to a combination of a rapidly rebounding terms of trade, stronger than expected Q2 GDP, and a still decent environment for FX carry. Moving forward, we expect NZD/USD to weaken to 0.57 through Q4 of this year. Our forecast rests on continued USD strength, weakening global growth, and a mispriced RBNZ.

We expect a slowdown in global growth to weigh on the NZD though year end, given New Zealand's reliance on high value agricultural exports. The RBNZ appears to be cognizant of these risks, as they recently stressed the negative effect that a global growth slowdown will have on the domestic economy. We continue to disagree with the full hike priced for the RBNZ by April 2024, and instead think that the RBNZ will begin cutting rates in Q2 2024 in order to keep real rates from becoming too restrictive. These headwinds support our call for NZD/USD to trade towards 0.57 by year-end.

We expect NZD/USD to rebound towards the 0.63 level by Q4 2024, as the USD comes off overvalued levels and the terms of trade supports the currency. El Nino is likely already impacting New Zealand's terms of trade, and it will continue to boost the NZD as it strengthens into next year.

ZAR

Jeremy Stretch

Fiscal Picture and Stronger USD to Weigh on the ZAR in the Near-term

USD/ZAR – Q4 2023: 19.15 **|** Q1 2024: 18.75

The South African Reserve Bank (SARB) held rates at 8.25% for the second consecutive meeting. Despite this, it remains intent on driving inflationary impulses out of the system. Indeed, the most recent vote on policy was split 3:2 which is somewhat surprising as both the headline and core CPI were comfortably within the 3-6% CPI threshold in August.

Despite elevated real rates, the SARB statement continues to reference additional mechanisms that would help ease CPI back towards the lower end of the inflation target regime. The statement, accompanying the no-change decision, underlined the necessity of "achieving a prudent public debt level, increasing the supply of energy, moderating administered price inflation, and keeping real wage growth in line with productivity gains." Such comments are particularly notable ahead of the government's medium-term fiscal strategy statement (MTFS) on 1 November.

The perpetuation of high real rates provides a degree of support for the currency, in this context, we would note that real money ZAR longs have extended to near one-year highs. However, the ZAR remains susceptible to the MTFS as it's likely to detail the weak state of government finances, allied to a macro backdrop that remains at risk in view of ongoing external headwinds, including utility output. Moreover, should the USD continue to advance on the back of the "higher for longer" Fed narrative, this risks pressuring high beta EM currencies including the ZAR. While the ZAR may continue to struggle in the near term, we expect a graduated recovery narrative through 2024.

LATAM FX

MXN

Luis Hurtado

Banxico's Cautious Stance Continues

USD/MXN – Q4 2023: 18.00 **|** Q1 2024: 18.50

We recognize that Banxico has strongly signalled that the easing cycle will not begin in 2023. Nevertheless, we continue to see current market pricing (70bps in rate cuts for the next twelve months) as too cautious. As we mentioned before, the ex-ante real rate – which is the overnight rate minus 1Y inflation expectations – is already two times above the upper band of Banxico's neutral real rate range and already above 7.0% amid a slow but steady decline in 1Y inflation expectations. Hence, we anticipate continuous 25bps rate cuts starting in March 2024, bringing the overnight rate to 10.00% by the end of Q3 2024 (versus 10.54% currently priced in).

Looking at the currency, with USD/MXN decisively increasing above its 200-day moving average, a break of the 18.40 mark should send the pair towards 18.50, its highest level since March. Going forward, however, we highlight that as the Fed maintains its higher for longer narrative, we expect shifting labour dynamics in the US (through its effect on remittances to Mexico) to remain the largest downside risk for the peso, while a move away from the fiscal conservatism seen so far in the AMLO administration is starting to create some concerns in debt markets. Hence, we maintain our end of year USD/MXN forecast at 18.00 and 18.50 for Q1 2024.

BRL

Luis Hurtado

Carry Out, Fiscal Concerns In

USD/BRL – Q4 2023: 5.20 | Q1 2024: 5.20

Although the government has repeatedly stated it will not change its fiscal target for 2024, it is evident that the current administration will face substantial challenges to achieve 0% of GDP primary fiscal result next year. That said, the administration is already circulating the idea of a “fiscal margin” amounting to BRL71bln. This includes the 0.25% of GDP deficit allowed as the lower band for the fiscal target (BRL29bln), the use of non-executed but approved expenditures (around BRL22bln), and new rules on transfer prices.

Looking at the currency, despite the BRL’s still attractive carry, the latest increase in global yields, and the “higher-for-longer” message among major central banks, are likely to prevent a strong BRL rebound for the remainder of 2023. Moreover, on the local front, we expect the market to focus on when and where debt/GDP will stabilize. The discussion of revenue measures will likely be the next catalyst for BRL movements to either side, while headline risks, as in previous negotiation rounds, should keep USD/BRL vols elevated in the coming weeks. Hence, we maintain our Q4 2023 and Q1 2024 forecasts at 5.20.

CLP

Luis Hurtado

Underperformance Continues

USD/CLP – Q4 2023: 900 | Q1 2024: 920

The CLP has underperformed its LATAM FX peers for most of 2023, dropping 0.1% against the USD so far this year. The Chilean peso performance in 2023 is explained by three main factors. First, the Chilean Central Bank (BCCh) was the first major central bank in the region to signal and implement a rate cut. Second, following the optimism about China’s reopening earlier in 2023, the CLP, given its dependence on copper exports (~40% of total exports), was the first currency in Latin America to be penalized by increasing concerns regarding China’s growth. And third, the BCCh started to build its international reserves in June, announcing a plan to buy USD10bln in 12 months (USD40mln per day).

Nevertheless, USD/CLP has already started to feel toppish. Here, we note that after surprising the market with 100bps rate cut in July, the BCCh cut the overnight rate by 75bps on September 5th and signaled the overnight rate will end the year at 7.75%-8.00%. This has fully reversed the downward move in local rates which, at the end of July, pointed towards an overnight rate close to 7.25% by the end of the year. Moreover, the Ministry of Finance recently announced it would sell USD2bln per month until the end of the year (max USD150mln) more than offsetting the position adopted by the BCCh since June. Finally, we would point out that further and, perhaps, larger growth boosting measures by the Chinese government should bode very well for the CLP from current levels. Our USD/CLP targets for 2023 Q4 and 2024 Q1 remain at 850 and 870, respectively.

COP

Luis Hurtado

Still Sensitive to Global Volatility

USD/COP – Q4 2023: 4300 | Q1 2024: 4300

As we mentioned last month, Banrep signaled that its easing cycle will likely begin in September, in line with our expectations, however the magnitude of the upcoming rate cuts have been left up for debate. Amidst cautious remarks by Banrep board members driven by persistent inflation (expected to end 2023 at around 9%), the passthrough from a weaker COP, and potential upside risks from El Niño, the market is pricing a timid 25bps pace of rate cuts in each of the last three meetings of 2023. Thus, similar to Brazil, we highlight that this situation could quickly change in favour of a more aggressive easing cycle as Colombia’s monetary policy is the second most restrictive in the region.

Moreover, despite the appreciation in the COP and the surge in the COP basis across the curve during the first half of August (1-month COP basis surged above 600bps), funding concerns are dissipating as Banrep stepped in to provide liquidity via repos at extended maturities. In addition, regulators appear to be working towards implementing a rule that would allow local banks to use the deposits of financial institutions (e.g. pensions funds) to comply with regulatory ratio similar to the Net Stable Funding Ratio (NFSR), addressing the underlying issues for COP funding. We also point out that the COP’s liquidity has been impacted by the slow execution of the government’s budget, however, we expect spending to quickly accelerate ahead of the country’s regional election on October 29th. Therefore, we maintain our USD/COP forecasts for 2023 Q4 and 2024 Q1 at 4300 each.

Asia FX

CNY

Noah Buffam

Slow Depreciation Ahead for the CNY

USD/CNY – Q4 2023: 7.35 **|** Q1 2024: 7.38

Expectations for the Chinese economy stabilized somewhat in September, as USD/CNH tracked sideways. While we remain bearish on the outlook for the Chinese economy, we expect further revisions to growth to move at a slower pace. As a result, we have revised our Q4 2023 forecast down to 7.35, implying that peak CNH bearishness occurs in Q1 2024, when we expect the pair to trade to 7.38. The stabilization in Chinese data is apparent in the August industrial production and retail sales beats, alongside the stronger than expected credit growth. While fiscal and monetary stimulus is likely helping to support Chinese data in the short term, we expect a continued deterioration in growth over the next few months. This view is predicated on the fact that previous growth drivers remain overleveraged (real estate and local governments) and targeted stimulus for consumers does not appear to be on the horizon.

Under the surface, the August total social financing (TSF) and new loans releases are less impressive. TSF growth was driven by government borrowing, as local governments were told they have until September to issue any remaining debt for the year. Meanwhile, the increase in new loans was driven by a trend rise in non-financial business loans, but household loan demand remains below June 2023 levels (on a seasonally adjusted basis). Together, this suggests that credit growth is still relatively weak and that household consumption is not yet ready to ramp up.

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