Economics and FICC Strategy

MONTHLY FX OUTLOOK

April 13, 2023

US dollar gives up its throne

Currency	What's changed
USD	The USD decline that started with the spread of banking sector turmoil is set to extend as investor attention turns to other advanced economies that aren't as far along in tightening cycles, with the Fed closer to terminal.
CAD	A broadly weaker USD will benefit the CAD over the rest of the year, with an added tailwind from higher commodity prices in 2024.
EUR	EUR outperformance to continue as the ECB is poised to continue hiking, while the macro backdrop remains resilient.
GBP	Current terminal rate expectations for the BoE look too high; a correction would warrant EUR/GBP upside, capping recent GBP/USD gains in the process.
JPY	Increasing levels of onshore investment, amidst Fed tightening reaching a peak, underlines the prospect of JPY gains ahead.
Commodity FX	Both AUD and NZD should receive a lift from broad USD weakness in 2023, and demand for exports supported by China's re-opening.
LATAM FX	LATAM central banks remain cautious and have avoided signaling the start of easing cycles.
FX Asia	Stronger fundamentals ahead with China's economy now open imply upside for the CNY.

Currency outlook

End of period:	Apr 13, 2023	Q2 '23	Q3 '23	Q4 '23	Q1 '24	Q2 '24	Q3 '24	Q4 '24
USD / CAD	1.34	1.34	1.32	1.31	1.30	1.30	1.29	1.28
EUR / USD	1.11	1.10	1.11	1.13	1.14	1.15	1.15	1.16
USD / JPY	132	125	123	121	120	118	116	115
GBP / USD	1.25	1.24	1.24	1.26	1.27	1.28	1.28	1.30
USD / CHF	0.89	0.89	0.90	0.89	0.89	0.90	0.90	0.91
USD / SEK	10.27	10.14	9.82	9.51	9.34	9.09	9.00	8.84
AUD / USD	0.68	0.69	0.70	0.71	0.72	0.74	0.75	0.76
NZD / USD	0.63	0.62	0.64	0.66	0.67	0.68	0.69	0.70
USD / NOK	10.36	10.18	9.86	9.56	9.39	9.17	9.04	8.88
USD / ZAR	18.10	17.85	17.45	16.90	16.60	16.40	16.25	16.10
USD / BRL	4.92	5.05	5.20	5.40	5.20	5.20	5.40	5.00
USD / MXN	18.10	19.50	20.00	19.80	20.00	20.50	21.00	20.00
USD / COP	4450	4900	4800	4800	4600	4600	4800	4700
USD / CLP	798	850	920	940	920	900	920	880
USD / CNY	6.87	6.85	6.80	6.78	6.75	6.73	6.71	6.69

Other crosses

End of period:	Apr 13, 2023	Q2 '23	Q3 '23	Q4 '23	Q1 '24	Q2 '24	Q3 '24	Q4 '24
CADJPY	98.9	93.3	93.2	92.4	92.3	90.8	89.9	89.8
AUDCAD	0.90	0.92	0.92	0.93	0.94	0.96	0.97	0.97
GBPCAD	1.68	1.66	1.64	1.65	1.65	1.66	1.65	1.66
EURCAD	1.48	1.47	1.47	1.48	1.48	1.50	1.48	1.48
EURJPY	146	138	137	137	137	136	133	133
EURGBP	0.88	0.89	0.90	0.90	0.90	0.90	0.90	0.89
EURCHF	0.98	0.98	1.00	1.01	1.01	1.04	1.04	1.06
EURSEK	11.36	11.15	10.90	10.75	10.65	10.45	10.35	10.25
EURNOK	11.45	11.20	10.94	10.80	10.70	10.55	10.40	10.30

Key indicators – Latest data point

End of period:	Quarterly real GDP (y/y %)	CPI (y/y %)	Current acct (% of GDP)	Central bank rate (%)
US	0.9	5.0	-3.2	4.875
Canada	2.1	5.3	-1.5	4.500
Eurozone	1.8	8.4	-0.7	3.000
Japan	0.4	3.3	2.1	-0.100
UK	0.6	10.4	-3.8	4.250
Switzerland	0.8	2.9	10.1	1.500
Sweden	-0.1	12.0	4.3	3.000
Australia	2.7	6.8	1.2	3.600
New Zealand	2.2	7.2	-8.9	4.750
Norway	1.3	6.5	30.4	3.000
South Africa	1.2	7.0	-0.5	7.750
Brazil	1.9	4.7	-2.9	13.750
Mexico	3.6	6.9	-0.9	11.250
Colombia	2.9	13.3	-6.2	13.000
Chile	-2.3	11.1	-9.0	11.250
China	2.9	0.7	2.4	2.750

CAD

Katherine Judge and Avery Shenfeld

Foundering USD to support CAD

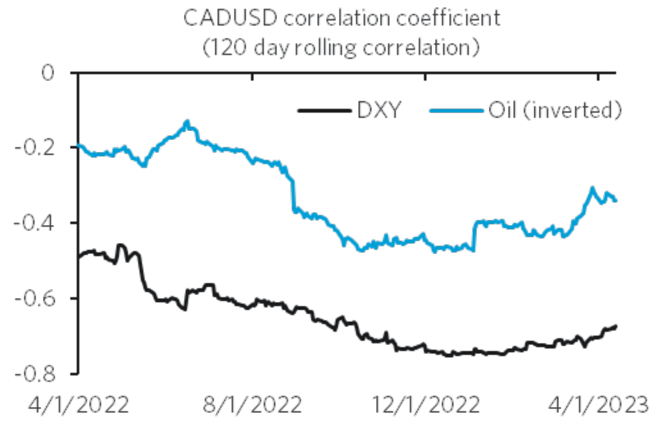
Q2 2023: 1.34 | Q3 2023: 1.32 (USDCAD)

The story for CAD continues to be mostly written elsewhere, as the loonie's cross against the USD has largely moved in sync with other majors, rather than being dictated by oil prices or news from Canada's own economy (Chart 1). The USD lost ground as stress on regional banks dialed down expectations for the extent of further Fed tightening, and we expect to see the greenback slide further when the Fed goes on hold after a final quarter point hike in May, and investor attention turns to other advanced economies overseas that are not as far along in their policy tightening cycles as the Fed, or face higher inflation that could see them lag behind the US in terms of the timing of the first rate cuts in 2024. The debt ceiling deadline could also weigh on the USD temporarily into mid-year, although we ultimately expect a resolution that avoids a government shutdown or default.

Those factors will see the greenback unwind its safe-haven bid to come into better alignment with trade fundamentals, benefitting the loonie in the process. We see USDCAD ending the year at 1.31. The path to that level could come sooner than our base case forecast if fresh banking sector turmoil emerges that stays the Fed's hand from a hike in May, or if a deal on the US debt ceiling proves to be more troublesome this time, especially given the build in net shorts tied to the greenback.

While the market is currently pricing-in what looks like a premature easing in Fed policy this year, it's also understating the Bank of Canada's willingness to let several weak quarters go by before it will be ready to ease, a development we don't expect to see until 2024. At that point, we see both central banks trimming rates, but Canada benefiting a bit from a pick-up in global growth that will be supportive for commodity price expectations. Our target of 1.28 for USDCAD by end-2024 would represent only a middling level for the Canadian dollar relative to its longer-term history, as we don't expect extremes of USD weakness, or the commodities boom and the generous interest differentials that are typically characteristic of periods in which the loonie sustains even firmer levels.

Chart 1: C$ moves driven more by broad USD moves than oil



Source: Bloomberg, CIBC

USD

Bipan Rai

Waking up the USD bears

Q2 2023: 100.7 | Q3 2023: 99.7 (DXY)

March was a tough month for the greenback. Indeed, trade-weighted gauges of the US dollar fell as it became clear that banking system stresses were emerging after the most aggressive tightening cycle in decades. For the Federal Reserve, there were clear implications that ultimately meant two things. First, that the proximity to the terminal rate was closer than thought beforehand. This was communicated at the March meeting – and it supported our existing call for one final hike in May before the Fed stands pat for the rest of the year. Second, that the Fed might have to think long and hard about its hyper-aggressive QT program going forward. The Fed’s response to this episode has led to an expansion of its balance sheet that has effectively offset a significant portion of the QT program to date. What’s more is that QT looks out of place when there’s greater competition among banks for deposits in the US. A slowing, or even a stoppage of QT is not in the price for the USD – which means that risks are still tilted to the downside in the months ahead.

EUR

Jeremy Stretch

Expecting ECB activism

Q2 2023: 1.10 | Q3 2023: 1.11 (EURUSD)

The latest IMF global reserve numbers (for Q4) revealed the proportion of EUR-denominated global reserves breached the 20% threshold for the first time in three quarters. Moreover, we would note an aggressive quarterly increase in the proportion of EUR-denominated holdings (0.81%) exceeded the previous cyclical high witnessed in Q4 2020. The rebuild coincided with the EUR gaining more than 9% versus the USD across Q4. That relative outperformance was largely predicated on an increasingly hawkish ECB allied to the erosion of EU recession concerns.

We expect relative EUR outperformance to extend through the upcoming quarters, in part by virtue of ongoing ECB proactivity. The ECB hiked rates by 50bps in March despite concerns over EU financial system integrity. Post the hike, we noted that ECB President Lagarde underlined that there's no trade-off between price and financial stability. As we do not expect recent banking sector pressures to be systemic, we expect ECB Governing hawks to continue to press for additional tightening. The fact that recent ECB staff macro forecasts still assume that HICP will be above the 2% target threshold in 2025 underlines further scope to tighten. We assume two more 25bps adjustments in May and June, resulting in a 3.50% terminal rate.

While headline CPI benefits from base effects, we can expect an increasing ECB focus on rising core HICP. Within the updated forecasts, staff assumptions for core HICP, excluding energy, food, and indirect taxes, were revised from 4.2% to 4.6%. Governing Council member Schnabel has warned of inflationary pressures proving stubborn, while Knot has highlighted the importance of core prices. We expect the combination of macro resilience and sticky core CPI to warrant ECB activism. That activism contrasts with inertia from many central banks that have entered conditional rate pauses. Consequently, this favours ongoing EUR resilience.

JPY

Jeremy Stretch

Into the Ueda era

Q2 2023: 125 | Q3 2023: 123 (USDJPY)

After an unprecedented 10 years of Kuroda at the helm of the BoJ, the transition to former academic Kazuo Ueda heralds a looming policy transition. The policy of 'Abenomics', was characterized by a cheap JPY and a highly expansionary monetary policy, aimed at pushing Japanese inflation to move towards the 2% target threshold on a sustainable basis. The recent price spike, to more than forty-year highs, was largely a function of higher costs, namely energy. Only when price pressures are deemed to be self-sustaining should we expect a policy reversal.

While headline prices are moderating from recent extremes, the conclusion of the annual wage round points towards conditions increasingly consistent with policy adjustment. The Japanese Trade Union Confederation (Rengu) has detailed that workers have negotiated the biggest pay hikes in 30 years. The average monthly pay hike equates to 3.70%. The uptick in real earnings will support consumption, growth, and policy normalization.

Rising wages suggest that Japan is nearer to sustainably hitting its 2% CPI target. Under such circumstances, we remain mindful of curve normalization under the Yield Curve Control regime. Previously, Governor Ueda has suggested YCC is not appropriate for policy fine-tuning. Consequently, we remain on watch for an early BoJ policy adjustment. We anticipate the bank looking to ease yield curve distortions via the toleration of a wider fluctuation band for 10-year yields. An adjustment is likely to encourage domestic life companies to further materially increase domestic bond holdings, reducing foreign outflows and JPY selling accordingly.

Having unexpectedly adjusted the YCC threshold in December, we would note that new BoJ deputy Governor Uchida underlined that any further YCC adjustments should not be communicated to the market prior to any adjustment. A YCC adjustment, tolerating higher 10-year JGB yields will alleviate a material kink in the Japanese curve, while concurrently making overseas bonds less attractive, even before more expensive hedging costs are included. Increasing levels of onshore investment, allied to the conclusion of Fed tightening in May, underscores the prospect for JPY gains.

GBP

Jeremy Stretch

Time to take stock

Q2 2023: 1.24 | Q3 2023: 1.24 (GBPUSD)

Sterling was the best-performing major versus both the USD and EUR across Q1. Catalysts for outperformance proved to be better than expected data, moderating recession risks, while the fiscal and political credibility deficit, post the Truss political experiment, largely dissipated. We would also note that real money shorts materially corrected from late Q3 2022 extremes.

UK macro sentiment has benefitted from an improving data trend, particularly on the consumer side. Nevertheless, UK inflationary pressures remain elevated, as annual consumer prices rebounded back above the 10% threshold in February. However, fears of an aggressive uptick in electricity prices into the April price reset proved to dissipate. Additionally, fixed-rate mortgage resets have retreated from peaks witnessed in the wake of the Truss fiscal debacle. Annual food price inflation remains at record highs, as prices are 18% above year-ago levels, impacting discretionary spending at the lower end of the income distribution. But positive data surprises, with the economic surprise index testing year-to-date highs on gains in GfK consumer confidence, point towards a more supportive GBP backdrop.

Still, despite the data rebound, we remain mindful of the market proving too aggressive regarding BoE terminal rate assumptions. Upcoming CPI base effects are set provide some powerful inflation relief into early Q2. Moreover, the lagged effects of past BoE tightening have yet to work through the system, and the BoE will have to take stock of those impacts in the wake of 11 straight increases. As a result, the market's current terminal rate assumptions, towards 4.60%, are too high. We expect a correction in expectations to warrant EUR/GBP upside, capping recent GBP/USD gains in the process.

CHF

Jeremy Stretch

Beyond financial sector risks

Q2 2023: 0.98 | Q3 2023: 1.00 (EURCHF)

Despite Swiss CPI unexpectedly easing to 2.9% in March, from 3.4%, annual prices remain above the SNB's 2% ceiling, as they have for the last fourteen months. Irrespective of the March CPI moderation, due largely to lower energy costs and fruit costs, we would not expect this to dissuade the SNB from hiking again at their next quarterly policy decision on 22 June. Having seen the SNB match the ECB last month, they also hiked by 50bps, leaving the policy rate at 1.50%, we would expect the bank to moderate the pace of tightening to 25bps adjustments, this comes as we expect an SNB terminal rate of 2.00% by the end of Q3.

Recent banking sector noise, resulting in the coupling of UBS and Credit Suisse, compromised market pricing into the March SNB decision, indeed in the immediate aftermath of the crisis rate expectations eased below 25bps. However, we continue to expect the SNB to maintain a laser-like focus on their primary policy responsibility, namely monetary policy stability. The latest SNB bulletin maintained a presumption of prices exceeding the 2% target threshold at the end of the forecast horizon, the bank continues to assume prices will be at 2.1%. The overshoot underlines the prospect of additional tightening, not least as the bank remains mindful of ongoing second-round wage effects.

There are some tentative signs of growth and employment prospects moderating. However, as the unemployment rate remains at a 20-year low of 1.9% this underlines scope for additional tightening. We would expect that the SNB will remain comfortable with EUR/CHF remaining around the parity threshold. However, as we expect another 50bps of SNB tightening ahead we would expect USD/CHF downside to persist. We expect USD/CHF to test CHF0.8950 and levels not seen since June 2021.

SEK

Jeremy Stretch

Looking beyond real estate risks

Q2 2023: 11.15 | Q3 2023: 10.90 (EURSEK)

The long-term relationship between Swedish real estate and currency performance suggests that weakness in the former risks ongoing SEK challenges. The release ofQ1 quarterly real estate data risks the annual price correction extending beyond 2012 lows as prices retreat in the face of rising mortgage costs, more than half of households have floating rate mortgages, and increasingly stretched valuations. Yet despite a long-term real estate correction, which has been mirrored by a material reduction in retail spending, retail activity has advanced just once in the last ten months, we remain cautiously optimistic as regards a SEK rebound.

Despite real estate pressures, we expect central bank Governor Thedeen to continue to advocate a tightening bias, defeating inflation remains the primary policy consideration. Although the targeted inflation rate, CPIF, peaked in December at 10.2%, prices remain well above the long-term target threshold. Moreover, in the wake of an unexpected February acceleration to 9.4%, due to record food prices, we would expect Riksbank Governor Thedeen to continue to advocate further tightening.

Beyond a more aggressive policy response, we would underline a key Riksbank structural change, namely moving away from a perceived policy of benign neglect as regards the currency, a stronger SEK will help ease imported price pressures. Nevertheless, we anticipate that the 25 April Riksbank meeting is set to sanction a further 50bps rate hike, taking rates to 3.50%.
Beyond retail headwinds and real estate concerns, it is notable that the economic surprise index has rebounded from early Q1 weakness. Moreover, we would note the strong relationship between risk sentiment and the SEK. Recent banking-related woes, encouraged a spike in equity volatility, compromising SEK valuations,

particularly versus the USD. As we do not regard banking pressures as systemic, the combination of an improved risk tone allied to Riksbank activism, relative to the Fed, points towards a graduated correction in broad SEK undervaluation.

Commodity FX
NOK

Jeremy Stretch

A higher rate path

Q2 2023: 11.20 | Q3 2023: 10.94 (EURNOK)

After pausing in January the Norges returned to policy tightening at their most recent meeting, hiking by a further 25bps, taking rates to 3.00%. The bank has now tightened by a cumulative 300bps, remember the Norges were the first major central bank to hike back in September 2021. Not only did the bank return to policy adjustment they also struck a hawkish tone as the accompanying decision statement underlined that inflation remains above target, albeit annual prices moderated compared to expectations in February. Although the monetary authorities remain wary over the impact of past tightening on a leveraged economy the central bank remains on course to tighten further despite rates reaching 15 year highs. The combination of an elevated inflation profile and improved growth outlook, the recent regional tendency survey suggested that the underlying backdrop had marginally improved, suggests that the Norges bank seems set to take rates to 3.50% by the summer, the bank next meets on 4 May. An upgraded rate path points towards a 40% probability of a terminal rate peak at 3.75%, we would not expect such levels to be considered unless the NOK proves a material underperformer.

The NOK proved the primary Q1 underperformer, it depreciated by more than 6.5% versus the single currency. That weakness is likely at least a partial catalyst for the uptick in Norges hawkishness. Having seen the Riksbank move away from a stance of almost benign SEK neglect, it seems that the Norges Bank now acknowledges that attempting to stimulate currency gains will prove complimentary in the fight against inflation. A hawkish bias, a reduced degree of NOK selling via the “petroleum buffer portfolio” allied to an expected avoidance of a global hard landing suggests the NOK should move off the bottom of the performance league table in Q2.

AUD

Noah Buffam

AUD to gain a tailwind ahead

Q2 2023: 0.69 | Q3 2023: 0.70 (AUDUSD)

We are maintaining our view of a stronger AUD going forward. This is largely predicated on our forecast for a weaker US dollar, alongside the benefits from the ongoing reopening of China’s economy. Earlier this month, the RBA announced that they would hold the policy rate at 3.60%, while softening language around the need for more rate hikes. However, we expect one more 25bps hike for the RBA in early May, given our expectations of a firm upcoming CPI print, and still hawkish rhetoric from Governor Lowe.

Through early March, a sputtering in China’s reopening weighed on the AUD. However, the recent strength in China’s internal demand, as evident in March PMIs, has increased optimism on this front. We anticipate that strong construction demand should keep Australian industrial exports strong, and recovering Chinese incomes will also spill over into tourism. Overall, a broad-based decline in the USD, alongside Chinese demand for Australian exports should continue to lift the AUD over the medium-term.

NZD

Noah Buffam

Upwards for NZD amidst broad USD weakness

Q2 2023: 0.62 | Q3 2023: 0.64 (NZDUSD)

The RBNZ’s surprise 50bps hike stood in stark contrast to other DM central banks that are erring towards conditional pauses for the most part. Having said that, we now think that the RBNZ is likely on hold, as the recent statement began to flag dovish hints. This included the notion that they are expecting to see a moderation in inflation expectations. While the market is currently priced for one more hike, we believe that USD weakness will dominate any NZD rate repricing should our RBNZ call prove prescient.

Elsewhere, the NZD should remain well supported thanks to robust Chinese demand for agriculture exports. Additionally, the weather phenomenon, La Nina, is finally over after 3 years and this will reduce draught in the region to bolster said exports. We expect these factors to reverse some of the large decline in the current account. To summarize, a weakening of the USD, alongside an improving New Zealand current account, will support the NZD over the coming quarters.

ZAR

Jeremy Stretch

Investors exit

Q2 2023: 17.85 | Q3 2023: 17.45 (USDZAR)

The last couple of months has proved challenging for those investing in South Africa. Ongoing domestic macro challenges, associated with ongoing utility load shedding, have combined with international investors becoming record net sellers of domestic bonds on a three-month moving average basis. An additional complication comes via the inverse relationship between the ZAR and risk. The recent episode of bank-related equity woes provided additional justification for investors to abandon high ZAR nominal yields in return for the safety and liquidity of the USD. Additional evidence of recent capital flight comes via the realization that speculative investors have extended ZAR shorts to all-time extremes in the wake of a record weekly ZAR position reduction in the middle of March.

The scale of the speculative investor capitulation allied to the substantive unwinding of bond holdings does suggest that should risk sentiment materially improve, we do not view recent financial sector effects as systemic this could suggest the near 7% year to date ZAR depreciation could materially snap back, prompting USD/ZAR to rebound back towards the 200Day MAV at 17.51.

However, any such bounce remains partly compromised by ongoing domestic weakness. The central bank (SARB) has lowered its 2023 growth assumption to 0.3%, due to substantive load shedding and or ongoing rail freight headwinds. Additionally, inflation remains a SARB concern. Inflation has remained outside of the 3-6% target range since May 2022. Policy tightening now risks extending towards 8.00-8.25%, previously a terminal rate of 7.75% was assumed prior to the unexpected 50bps hike on 30 March. We note that base effects are set to prompt a material CPI correction from Q2 onwards. Provided load shedding issues do not materially extend should global financial sector risks dissipate this points towards the prospect of speculative investors rebuilding positions, boosting medium-run ZAR valuations.

LATAM FX
MXN

Luis Hurtado

Imminent Banxico rate cuts signal peso weakness ahead

Q2 2023: 19.50 | Q3 2023: 20.00 (USDMXN)

Banxico increased the overnight rate by 25bps to 11.25% on March 30. The CB has now moved into a data dependent stance and signaled we are close or already at the end of the tightening cycle. Among the dovish notes in the statement, Banxico mentioned annual headline inflation decreasing more than expected and revised its short-term (the next two quarters) inflation forecast slightly lower. On the other hand, the CB's 2y inflation forecast remains unchanged with both core and headline inflation converging back to target by Q4 2024/early 2025. Looking at economic activity and labour markets, the CB stated that Mexico has "shown resilience and continued increasing during the early part of 2023 at a moderate pace" and that the labor market "remains strong".

Overall, the statement did not bring much of a surprise. Despite the now data dependent stance by Banxico, the CB has not ruled out a final 25bps rate hike in May. Note that sticky and elevated core prices, together with still increasing inflation expectations in the short term were unlikely to allow a more relaxed stance from the CB. We see Banxico's rate announcement as neutral for the MXN and maintain our call for a final 25bps rate hike in May and 75bps in rate cuts during H2, bringing our year-end overnight rate forecast to 10.75%. Looking at the peso, with the market paying increasingly attention to on Mexico's high exposure to US growth, we maintain our USD/MXN upward bias to 18.50 in the short term and prefer to reload USD longs on any USD/MXN dips to 18.00.

BRL

Luis Hurtado

Fiscal framework supports BRL in the short term but revenue measure discussions ahead point to higher volatility

Q2 2023: 5.05 | Q3 2023: 5.20 (USDBRL)

The gradual but feasible fiscal plan unveiled by the Minister of Finance Fernando Haddad at the end of March should limit market concerns about the country's fiscal sustainability. Ensuring that the new fiscal rule does not have many loopholes to increase spending going forward is what ultimately will support ongoing positive momentum. Negotiation in congress will be key.

Planning Minister Simone Tebet stated that the fiscal rule bill draft will be delivered to congress by mid-April. However, she mentioned that complementary measures to increase revenue will not be sent to congress just yet. Note that preliminary information point to revenue measures amounting to BRL110bln-120bln with the inclusion of state tax benefit in the calculation of the federal profit tax representing the bulk of the increase at around BRL90bln. Although we maintain our view of ongoing benefits to Brazilian assets arising from a partial removal of fiscal uncertainties, the current USD/BRL level (near 5.05) makes the pair ripe for tactical moves higher as the fiscal rule discussion in congress begin and headline volatility increases. We would keep our toes out of the water for now.

CLP

Luis Hurtado

BCCh Appears to rule out rate cuts in Q2

Q2 2023: 850 | Q3 2023: 920 (USDCLP)

In a unanimous decision, the Banco Central de Chile (BCCh) maintained the overnight rate at 11.25% in line with market consensus and our forecast. The BCCh highlighted the persistence of elevated core prices over the last several months and stated that the path back to their inflation target would take more than expected in the December Monetary Policy Report. Moreover, the communique maintained the sentence pointing that “it will be necessary to keep the monetary policy rate at 11.25% until macroeconomic conditions indicate that the process of inflation convergence to the 3% target has been consolidated”. This contradicts our expectations of a rate cut signal for the upcoming meetings (either May or June).

Given the strong commitment to consolidate a quick converge back to the 3% target, we no longer expect cuts in Q2. However, as the BCCh keeps the most restrictive monetary policy rate in the region, with its ex-ante real rate (overnight rate – 1Y inflation expectations) hovering 500bps above neutral for the last few months, we maintain our call for 100bps-125bps in rate cuts during the second half of the year. The release of the Monetary Policy Report on Wednesday morning should shed further light on this topic as the BCCh updates its monetary policy rate corridor for the next two years.

Regarding USD/CLP, we are adjusting our Q2 forecast lower to 850 from the previous 900. This reflects our revised expectations of no rate cuts this quarter. However, despite the expected initial knee-jerk reaction in USD/CLP, we maintain a bearish CLP view for the remainder of Q2. This view echoes the increasingly uncertain global growth outlook and considers the risks associated with the discussion of structural reforms in congress as well as the ongoing new constitution process.

COP

Luis Hurtado

Banrep pause is near but inflation continues to surprise to the upside

Q2 2023: 4900 | Q3 2023: 4800 (USDCOP)

In its lates rate announcement, Banrep increased the overnight rate by 25bps, decelerating from the 50bps rate hike in February. Moreover, the CB stated that further decisions will depend on new information available, highlighting the importance of upcoming inflation data prints. On this front, March inflation print came in at 13.34% y/y above the 13.28% y/y expected by consensus and the 13.28% y/y poste in February. Moreover, core process jump to 11.42% y/y, following the 10.86% y/y print in February.

Albeit the recent appreciation of the COP driven by the rebound of oil prices, and the resistance to some radical reform in congress, still high inflation expectations, and the above consensus print in March should continue to penalize the COP. Moreover, note that we maintain our bearish COP view for the remainder of the year and keep our year-end USD/COP at 4800. The lack of a more aggressive monetary policy stance by Banrep against still high inflation and inflation expectations, high current account and fiscal deficits, populist structural reforms, and increasing global growth uncertainties remain the largest headwinds for the Colombian peso.

Asia FX
CNY

Bipan Rai

Stronger fundamentals underpin CNY upside

Q2 2023: 6.85 | Q3 2023: 6.80 (USDCNY)

Despite clear signs of an improving domestic backdrop, USD/CNH has been remarkably stable of late. Business sentiment (as gauged by the CFLP and Caixin PMIs) are still tilted in favour of expansion, while price pressures are ebbing for both households and businesses. The fly in the ointment remains the uncertain backdrop for credit growth – with impulse trackers improving, but still at more moderate levels. That’s an important lead indicator for domestic demand, which is what the governing authorities see as the cornerstone to growth in the coming years.

Our core thesis for this year is that both the CNH and CNY will benefit from sounder fundamental footing going forward. That should lead to an uptick of portfolio inflow, with the risk being that geopolitical tensions counteract.

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