20 June 2019, 15:30 BST

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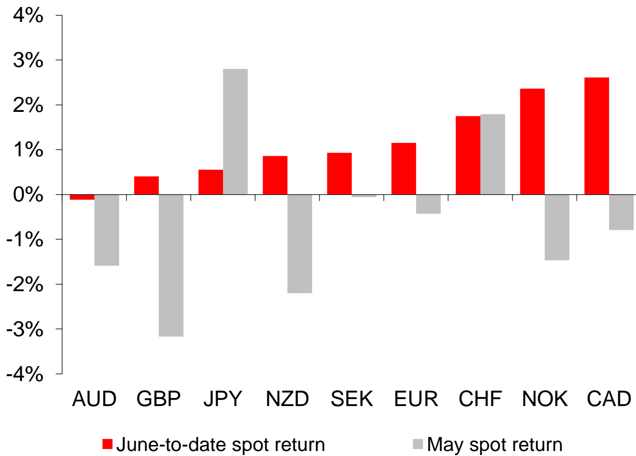
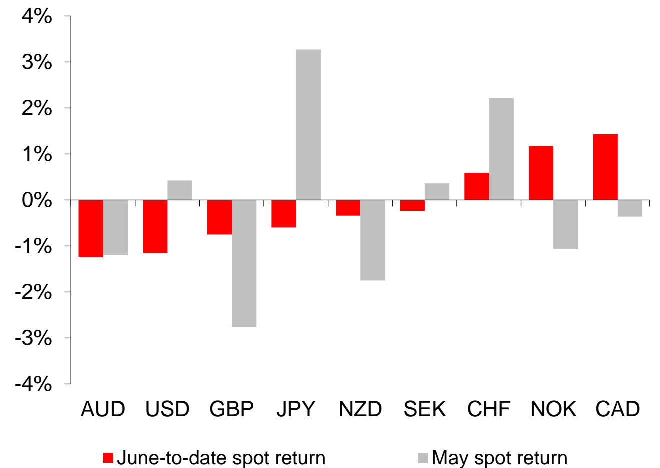
FX Spot Returns

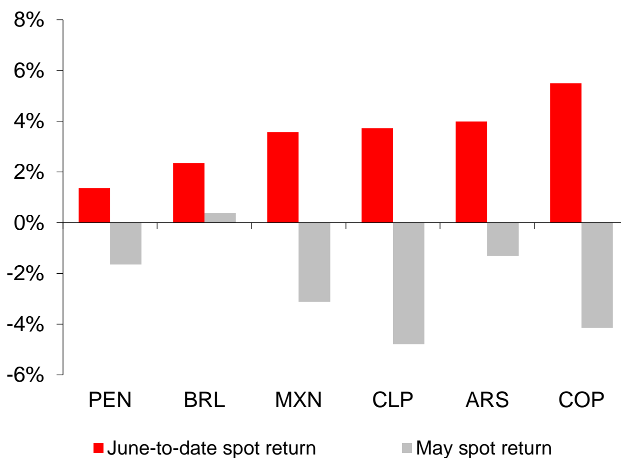
G10 spot returns vs. USD



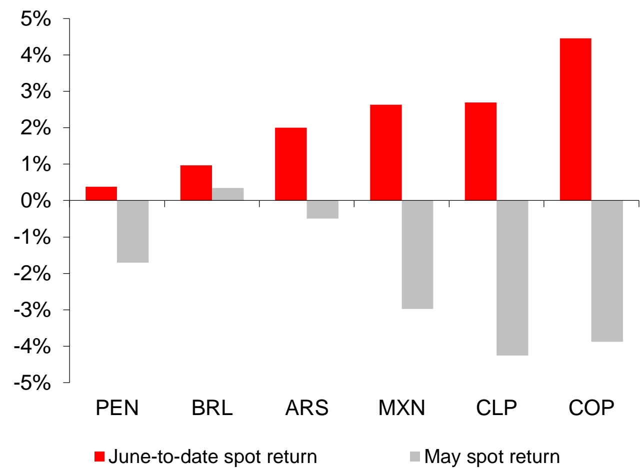
G10 spot returns vs. EUR



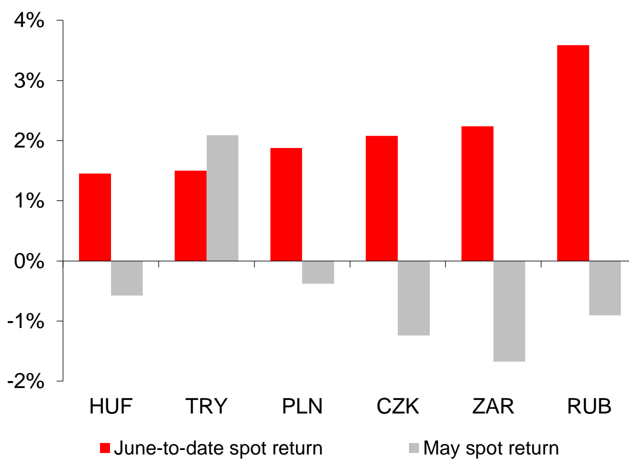
LatAm spot returns vs. USD



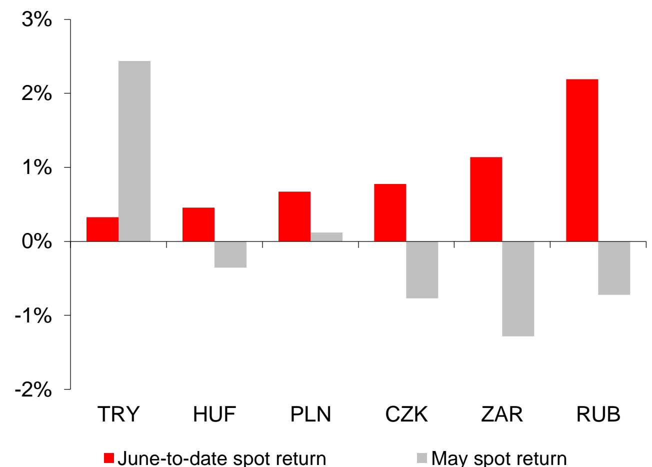
LatAm spot returns vs. EUR



CEEMA vs. USD



CEEMA vs. EUR



Source: Bloomberg, Santander. Note: Data current as at 20 June 2019 at 14:30 BST

FX Forecasts

G10 FX Forecasts						
	Q3-19	Q4-19	Q1-20	Q2-20	Q3-20	Q4-20
EUR-USD	1.14	1.17	1.18	1.20	1.21	1.22
GBP-USD	1.30	1.31	1.33	1.35	1.37	1.38
GBP-EUR	1.14	1.12	1.13	1.13	1.13	1.13
EUR-GBP	0.88	0.89	0.89	0.89	0.88	0.88
USD-JPY	112	115	118	116	115	115
EUR-JPY	128	135	139	139	139	140
USD-CNY	6.70	6.70	6.65	6.50	6.50	6.50
EUR-CHF	1.15	1.18	1.20	1.21	1.23	1.24
USD-CHF	1.01	1.01	1.02	1.01	1.02	1.02
EUR-SEK	10.6	10.4	10.3	10.3	10.2	10.1
EUR-NOK	9.6	9.5	9.4	9.3	9.3	9.2
USD-CAD	1.31	1.29	1.28	1.27	1.25	1.25
AUD-USD	0.68	0.70	0.70	0.71	0.72	0.72
NZD-USD	0.65	0.67	0.68	0.68	0.69	0.69

LatAm FX Forecasts						
	Q3-19	Q4-19	Q1-20	Q2-20	Q3-20	Q4-20
USD-BRL	3.75	3.9	4.0	4.1	4.1	4.1
USD-MXN	19.3	19.8	19.8	20.1	20.3	20.5
USD-CLP	680	685	687	689	691	692
USD-COP	3250	3300	3250	3300	3350	3400
USD-ARS	48.0	52.0	53.9	55.9	57.9	59.3
USD-PEN	3.36	3.37	3.37	3.38	3.37	3.39
EUR-BRL	4.3	4.6	4.7	4.9	5.0	5.0
EUR-MXN	22.0	23.2	23.4	24.1	24.6	25.0
EUR-CLP	775	801	811	827	836	844
EUR-COP	3705	3861	3835	3960	4054	4148
EUR-ARS	55	61	64	67	70	72
EUR-PEN	3.8	3.9	4.0	4.1	4.1	4.1

CEE FX Forecasts						
	Q3-19	Q4-19	Q1-20	Q2-20	Q3-20	Q4-20
EUR-PLN	4.29	4.27	4.28	4.24	4.20	4.25
EUR-CZK	25.8	25.6	25.4	25.2	24.9	25.0
EUR-HUF	325	325	320	322	315	315
USD-RUB	65	67	67	67	64	65
EUR-RUB	74	78	79	80	77	79

Sources: Santander

G10 FX: Main Themes

Currency	3M view	12M view	Main Themes
USD	Neutral	Mildly Bearish	• The USD remains firm, but may now have topped out. The factors that drove the USD higher in 2018 - US growth, high interest rates and risk - are still present, but a dovish Fed should curtail further gains.
EUR	Neutral	Mildly Bullish	• The ECB retains a dovish stance. Growth and inflation forecasts are on the low side, but the negative impact on EUR/USD may be countered by a more dovish US outlook.
GBP	Neutral	Mildly Bullish	• Sterling remains vulnerable, given UK politics and Brexit uncertainty. Economic data have also turned softer, weighing on the pound. However, a dovish Fed and lower USD could provide some support for GBP/USD.
JPY	Mildly Bearish	Bearish	• Low risk appetite boosted demand for the yen, it should weaken if the uncertainties fade. But downside pressure on the currency from a loose BoJ policy is now being countered by dovish policies elsewhere.
CNY	Neutral	Mildly Bearish	• US-China trade tensions remain a risk, with policymakers set to continue with stimulus measures. Much will depend on the June G20 meeting, but further CNY weakness may spark US retaliation and capital outflows.
CHF	Mildly Bearish	Mildly Bearish	• The CHF should gradually weaken: the SNB still views the CHF as 'highly valued' and, despite firm economic data, should maintain a very loose policy into 2020 and remain willing to intervene.
CAD	Neutral	Mildly Bullish	• We see scope for some CAD appreciation. Oil prices have weakened, but are having less effect on the CAD. A dovish Fed should help the CAD, and the BoC could be less dovish if activity picks up in line with their forecast.
AUD	Neutral	Neutral	• Global risk sentiment, with a focus on the US and China, has pulled the AUD lower. Further trade uncertainty, together with speculation of additional RBA rate cuts, should continue to limit the AUD.
NZD	Neutral	Neutral	• The RBNZ cut rates in May, and could do so again as soon as August. Looser monetary policy, and elevated global trade fears, are likely to continue to restrict the NZD over the summer.
SEK	Neutral	Mildly Bullish	• Although CPIF is back above 2%, domestic data have deteriorated this year and the Riksbank is looking unlikely to eke out a rate hike in 2019. With global trade fears elevated, a SEK recovery is unlikely just yet.
NOK	Mildly Bullish	Mildly Bullish	• With the economy performing relatively well, oil prices recovering from their early 2019 lows, and the Norges Bank now in the middle of a hiking cycle, the NOK should strengthen over the coming months.

Bullish · Mildly Bullish · Neutral · Mildly Bearish · Bearish

Source: Santander

G10 FX Overview

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The USD remains firm, in our opinion too firm, but may now have topped out. The factors that drove the USD higher in 2018 - US growth, high interest rates and risk - are still present, but a dovish Fed should curtail further gains.

The EUR has held up well over the last month. This resilience has come despite concerns over EMU activity, a dovish ECB and global trade risks still weighing on sentiment. In absolute terms, the EUR remains vulnerable, but the prospect of looser US monetary policy weighing on the USD suggests that in relative terms it should edge higher over the coming months.

The pound has remained under pressure. The combination of UK political uncertainty, a softening in UK economic data and a still firm US dollar has kept the pound on the back foot against both the USD and EUR.

The yen has remained strong, in our view too strong. A loose BoJ monetary policy, low inflation and sluggish growth have not weakened the yen as we expected. However, ironically the adoption of looser policies by other central banks, weaker CPI and concern over global growth are weighing on other G10 currencies, which, amid still low risk appetite, is helping keep the yen firm.

The renminbi has remained soft, holding on to much of May's decline, with USD/CNY threatening to test, and then break above, the 7 level. The US-China trade tensions continue to have an impact on the economic outlook, so stimulus measures remain. But there may be reluctance to allow the CNY to weaken further amid policymakers' unwillingness to lose control of the currency and spur capital outflows.

We continue to believe that the Swiss franc should be weaker than it is. However, the SNB's very loose monetary policy has not proved sufficient to significantly or sustainably pull the CHF lower, even before other central banks' recent adoption of more cautious/dovish rhetoric.

We retain a cautious stance on the AUD in 2019. Persistent global trade uncertainty, as well as softer domestic data have kept the AUD under pressure over the past quarter. The RBA cut rates in June, but we expect another cut to come in August.

An uncertain global economic backdrop has weighed on the NZD, and this, together with a more expansive monetary policy from the RBNZ, is likely to continue to drag the currency lower during the months ahead.

We remain cautious on the SEK. Domestic data have picked up a little over the past month, but the backdrop of international uncertainty amid the US-China trade dispute continues to weigh on the currency. We expect the Riksbank to struggle to squeeze in a rate hike this year.

We remain positive on the CAD. The currency is still a strong performer against its G10 peers. The Bank of Canada's recent dovish rhetoric did weigh on the currency, but this is now being countered by similar comments from other central banks. The decline in the oil price has also been a drag on the currency, but recent economic data have been good and the BoC still expects recent slower growth to be temporary.

We are positive on the NOK. The economy is performing well, even though CPI has edged lower. The NOK should be supported by a tighter monetary policy, at a time when most developed market central banks are turning significantly more dovish.

USD – Don't look down

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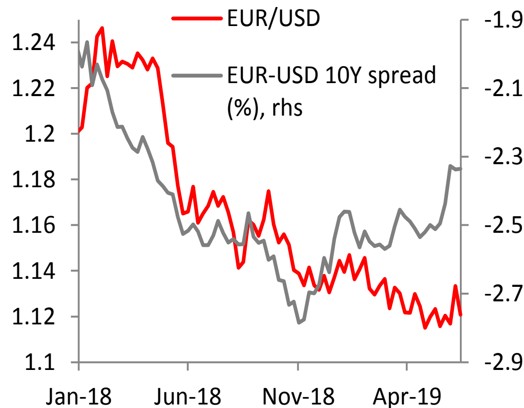
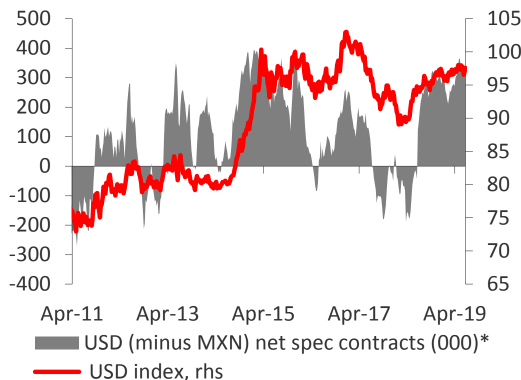
Chart 1: EUR/USD still appears rather cheap, even after the FOMC



Source: Bloomberg, Santander

Chart 2: Being long the USD could appear less attractive in the months ahead



Source: CFTC, Bloomberg, Santander *USD composite index = USD composite index uses AUD, CAD, CHF, EUR, GBP, JPY, NZD IMM positioning to arrive at an aggregate USD position

The USD remains firm, in our opinion too firm, but may now have topped out. The factors that drove the USD higher in 2018 - US growth, high interest rates and risk - are still present, but a dovish Fed should curtail further gains.

The USD should be receiving less support from the 'RAR', i.e. rates, activity and risk. The US rate hike cycle looks to have come to an end. The Fed, as expected, kept US interest rates unchanged at the June FOMC. But it adopted a more dovish stance, expressing concern about the economic outlook, and therefore opening the door to near-term rate cuts. As a result, the US 10Y yield dropped below 2% for the first time since November 2016

We believe that the USD bull-run, which has broadly held since April 2018, was largely motivated by high US rates, which were expected to rise further. The fact that US interest rates remain high, and above its G10 peers, should prevent a big sell-off in the USD, but may no longer be enough to justify further appreciation. Admittedly, with other G10 central banks also adopting more dovish stances, USD pairs could still receive some help from interest rate differentials between the US and its peers.

However, whilst these differentials should remain in the USD's favour, recent movements already indicate that the dollar is on the expensive side, e.g. a lot of the move in EUR/USD in the 12 months from April 2018 can be explained by the move in EU-US 10Y yields. However, since late April 2019, even though the spread has remained negative, it has moved in a more EUR-friendly direction, which has not been reflected in EUR/USD.

Additionally, US activity data appear to remain USD positive. The US economy continues to outperform its peers, but the pace of that outperformance has slowed, but not been reflected in the USD, e.g. the US ISM has dropped to 52.1 from 60.8 in August 2018.

This still implies a more attractive activity backdrop than in many G10 economies, but the positive gap has shrunk. Further, with US GDP expected to slow to 1.9% in 2020, its outperformance versus its peers should narrow further.

The FX market continues to focus on global trade uncertainty, together with low risk appetite. This focus has continued to favour demand for the dollar as a safe-haven asset.

We have long argued that a more 'protectionist' administration would not want to see the USD strengthen and recent comments by President Trump suggest that he is getting irritated by other G10 policymakers taking, or threatening to take, action that weaken their currencies versus the USD. The market, in our opinion, has not placed sufficient weight on these concerns, but going forward it might.

Hence, we see the 'RAR' environment as less USD supportive in relative terms, but as suggested by the absolute level of US rates, activity and risk could still justify the FX market keeping the currency firm. However, commitment of traders' data continue to show that speculators are considerably long the USD. Given this positioning and that the RAR factors, which encouraged USD buying since April 2018, are fading, we expect a repositioning to spur a sensible move lower in the USD.

EUR – No new bad news is good news

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The EUR has held up well over the last month. This resilience has come despite concerns over EMU activity, a dovish ECB and global trade risks still weighing on sentiment. In absolute terms, the EUR remains vulnerable, but the prospect of a looser US monetary policy weighing on the USD suggests that in relative terms it should edge higher over the coming months.

It has been a positive month for the euro. EUR/USD has bounced off of May's low at 1.1107. However, the currency has not thrown off its cloak of vulnerability and in our opinion constantly feels at risk to another wave of selling pressure.

However, its relative resilience over the last month might at least imply that a lot of the known 'bad news', such as slow growth and ECB pessimism, has been priced in. Hence, the direct risk to the currency going forward stems from new factors, e.g. Trump's threat of sanctions on Germany and ire at Draghi inspired EUR weakness..

The pressure of new risks to the EUR is likely to remain, but if these risks do not materialise over the coming months, there are now signs that the market may be re-positioning to price in a less bullish outlook for the US dollar, which by default should provide support for EUR/USD.

Consequently, we retain a positive outlook for EUR/USD and the EUR in general, but the motivation for this has less to do with a genuinely positive EUR view and more to do with the expectation that the USD will falter in H2-19 and into 2020.

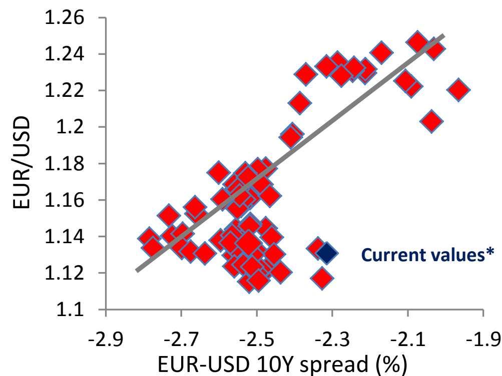
Eurozone economic activity remains subdued, but at least recent revised forecasts do not expect it to deteriorate further. The ECB made only small changes to its economic forecasts. It expects the economy to grow by 1.2% (vs. 1.1% before) this year, 1.4% (1.6%) in 2020 and 1.4% (1.5%) in 2021. Meanwhile, inflation is forecast at 1.3% (1.2%) in 2019, 1.4% (1.5%) in 2020 and 1.6% (1.6%) in 2021.

Admittedly, the currency took a hit in June, after the IMF warned that the Eurozone forecasts looked 'precarious' given trade tensions and Brexit. However, the Fund was also reported, by Reuters, as suggesting that the euro is slightly undervalued. Further, both we and the market expect US growth to slow into 2020, albeit holding above Europe's, and the narrowing of the gap with the US should help the EUR, again in comparison with the USD.

The ECB kept its policy unchanged at the June meeting. President Draghi reiterated the risks to activity, but the fact that he did not add significantly to past dovish/pessimistic comments actually provided some support for the EUR. Draghi did indicate that further stimulus measures, rate cuts and more QE are being discussed. However, as most G10 central banks, with the notable exception of the Norges and Riksbank, are positioning for further easing, the ECB stance is having less of a negative effect on the currency, as the market questions how much scope there is for more ECB easing.

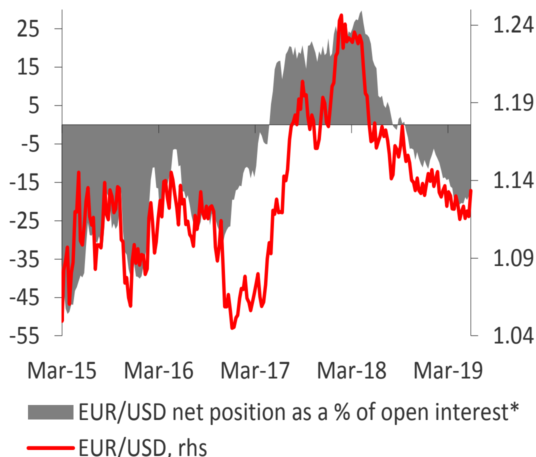
Hence, whilst the market's bias remains euro sceptic, there seem to be fewer new factors to drive the currency even lower. The Fed looks more likely to move before the ECB does. Plus, we still think EU-US yield spreads suggest EUR/USD is undervalued. The GDP story still favours the USD, but slower US growth should weigh on the USD looking ahead, and at least encourage a market that is very long USD and short EUR to reposition in the latter's favour.

Chart 3: EUR/USD still appears on the cheap side given policy and yield spreads



Source: Bloomberg, Santander. Note: EUR/USD and EU-US 10Y spread, weekly data, since the start of 2018
*As at 20 June 2019.

Chart 4: Time to reposition? There is room for speculators and others to sell the EUR further, but will they want to add to an already crowded long USD position?



Source: CFTC, Bloomberg, Santander
*OI=total long and short contracts

GBP – Looking to the USD for support

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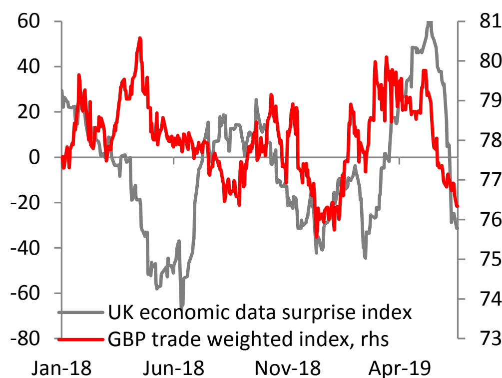
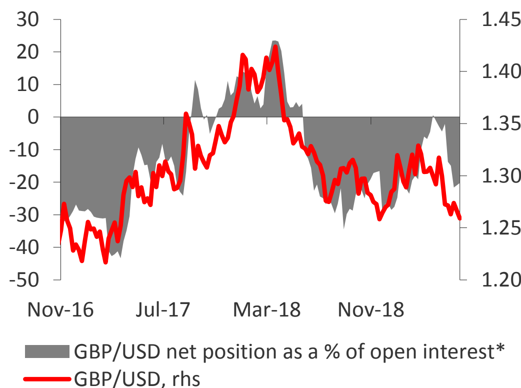
Chart 5: Sterling has been weighed down by political uncertainty, as well as softer economic data



Source: Bloomberg, Santander

Chart 6: Upside data surprises have not helped the pound amid ongoing political uncertainty



Source: CFTC, Bloomberg, Santander
*OI=total long +total short contracts

The pound has remained under pressure. The combination of UK political uncertainty, softer UK economic data and a still firm USD has kept the pound on the back foot against the USD and EUR.

We still feel that sterling is too cheap and since the EU referendum in 2016 has sold off more than fundamentals justify. However, whilst this 'cheapness' might provide some support for the pound over the months ahead, political uncertainty and soft UK data hint at further downside risks.

Consequently, we have revised our sterling forecast profile lower to reflect the lower spot level. The UK political backdrop should continue to be a drag on the GBP. We now expect GBP/USD at 1.30 by year-end, compared to 1.36. However, GBP/USD should find some support if the USD finally weakens amid expectations of US rate cuts, so we still look for GBP/USD gains into 2020, albeit from a lower starting point.

The new UK PM will not be chosen until the week starting 22 July. Further, the next Brexit deadline remains 31 October, implying that politics will remain a key focus for the pound, and on balance, is likely to temper demand for sterling.

Indeed, sterling volatility measures that straddle the October Brexit date seem to be reflecting that uncertainty. One- and three-month GBP/USD vols have declined during June. But six-month vol, the tenor that includes the new Brexit date, remains high.

The downside pressure on the pound has also been reflected in positioning data. The commitment of traders report shows that the speculative part of the market has increased its bets against the pound. This is important for spot sterling because, first, the positioning data, unlike with some G10 currencies, is strongly correlated with GBP/USD. Second, whilst the net short position has increased, there appears ample scope for it to widen further, adding to pressure on the pound.

Aside from UK politics, there are now other factors weighing on sterling, namely softer UK economic data. Between March and early May, UK economic data had tended to surprise to the upside, supporting the pound, pulling GBP/USD to 1.32 and GBP/EUR to around 1.17. However, since early May the data have tended to disappoint and the pound has weakened.

Further, the inventory-led improvement in Q1-19 GDP, +0.5% QoQ, ahead of the first Brexit deadline in March, looks to be reversing. The economy contracted 0.4% MoM in April, increasing the chance of negative GDP growth in Q2-19.

As expected, given the economic and political backdrop, the BoE kept policy unchanged in June. The market has moved away from expecting rate hikes over the next year. In absolute terms, this would be sterling negative, but with other central banks either cutting rates or adopting more dovish rhetoric, in relative terms there is still some grudging support to be found for the pound.

For example, GBP/USD has been dragged lower by a combination of UK uncertainty and USD strength. However, since March the pair appears to have diverged from the UK-US 10Y yield, suggesting that it has been oversold. If, as expected, the Fed cuts rates, the dollar should come under its own downside pressure, which, despite all the UK issues, could prevent GBP/USD from weakening further.

JPY – Caught in a policy squeeze

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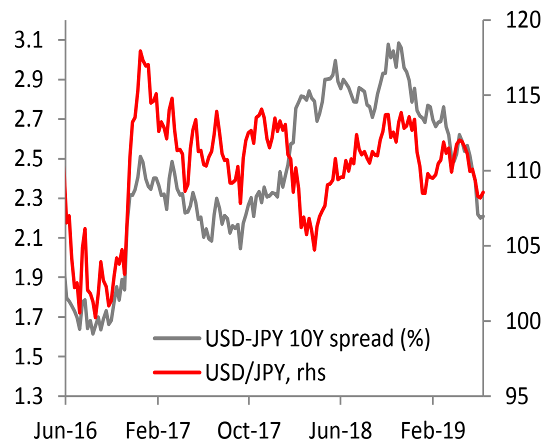
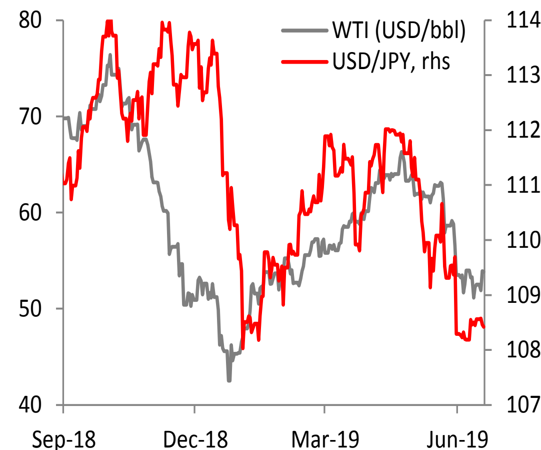
Chart 7: JPY continues to be driven by global risk factors and equities



Source: Bloomberg, Santander

Chart 8: Japanese GDP growth looked good in Q1-19, but the details were less impressive



Source: Bloomberg, Santander

The yen has remained strong, in our opinion too strong. A loose BoJ monetary policy, low inflation and sluggish growth have not weakened the yen as we expected. However, ironically the adoption of looser policies by other central banks, weaker CPI and concern over global growth are weighing on other G10 currencies which, amid still low risk appetite, is helping to keep the yen firm.

The JPY tends to be viewed by the FX market as a safe-haven currency. Hence, demand for the yen has been boosted by concerns over global trade and low risk appetite. This continues to be evidenced by soft equity markets and a lower oil price. The correlation between the Nikkei and USD/JPY has been 0.77 year-to-date, implying that as stocks have been sold off the yen has strengthened.

Hence, whether looking at oil or equities, the short-term message seems clear: the JPY will find it hard to reverse its recent gains as long as markets remain nervous and risk appetite low. Therefore, the focus will be on the G20 meeting on 28 June and whether US-China relations improve.

In addition, the yen is now being kept firm by a squeeze in relative G10 monetary policies. The BoJ kept its ultra-loose monetary policy unchanged in June. The policy has not effectively been altered since September 2016, a stance that we long believed should have been the catalyst for yen weakness.

Unfortunately, the FX market has tended to ignore the past negative effect of the loose BoJ policy on the yen, but is now focussed on the current dovishness of other banks as a reason why the yen should strengthen against their currencies.

BoJ Governor Kuroda did warn that further easing was possible if the Bank lost momentum to achieve its 2% inflation target. Currently, headline CPI is below 1% YoY, and labour cash earnings contracted 0.1% YoY in May, despite unemployment at a record low. In addition, Q2-19 GDP was stronger than expected, growing 0.5% QoQ, albeit after -0.1% QoQ in Q1-19, but export growth in May slumped.

We suspect that without faster wage growth, the Bank will struggle to hit its inflation target. The BoJ forecast CPI at 1.6% in the fiscal year 2021. This indicates that inflation is expected to remain below target through to 2022. Hence, the market is looking for the BoJ to follow other central banks and add to stimulus.

Governor Kuroda had already indicated that options include i) cutting the deposit rate from -0.1%; ii) reducing the target for 10Y yields from the current 0%; iii) expanding the monetary base; and iv) increasing asset purchases. The knee-jerk response to further BoJ stimulus should be yen negative, but would it be sustained amid doubts as to the effectiveness of new measures?

A more negative deposit rate could increase the pressure on the financial sector. Second, lower US 10Y yields and a softer USD risk smothering any positive effect on USD/JPY from a lower JGB target. Third, both the monetary base and asset purchases are already significant, with perhaps limited room for increases. Indeed, the BoJ's balance sheet as a percentage of GDP is 103%.

CNY – The ‘magnificent’ 7

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The renminbi has remained soft, holding on to May’s decline, with USD/CNY threatening to test, and then break above, the 7 level. The US-China trade tensions continue to have an impact on the economic outlook, so stimulus measures remain. But there may be reluctance to allow the CNY to weaken further amid policymakers’ unwillingness to lose control of the currency and spur capital outflows. Things should become clearer at, and after, the G20 meeting on 28-29 June.

Chart 9: Chinese export growth continues to struggle

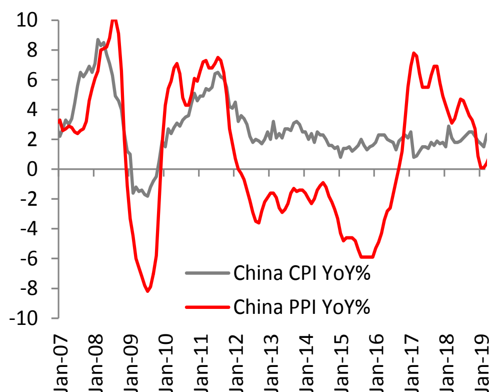
Source: Bloomberg, Santander

Concerns over the global trade outlook have continued to weigh on the Chinese economy. The IMF revised down its estimates for China’s growth to 6.2% this year and 6% in 2020. President Xi did indicate that the economy had improved and was stabilising, but recent data releases still highlight weakness.

Medium-term confidence will depend largely on the outcome of the G20 meeting on 28-29 June. President Trump has warned that he is prepared to block any trade deal that he feels is not good enough. However, the president’s recent backtracking from threatening tariffs on Mexico suggests that if a ‘successful’ agreement is reached, the market will respond positively, probably by buying back into riskier assets.

Recent economic data have confirmed that Chinese activity remains vulnerable. The May PMIs, both Caixin and official, declined. In particular, employment components were weak and export indicators slipped further. Another rise in credit growth for May showed that policymakers continue to ensure that consumers and small businesses have sufficient funds. However, industrial profits were still 3.7% YoY lower in April, albeit after a big gain in March. Further, the jump in CPI to 2.7% YoY in May owed more to higher food prices than spending pushing up prices. Excluding food, CPI was 1.6% YoY, the lowest since September 2016.

Chart 10: Chinese consumer and producer price inflation



Source: Bloomberg, Santander

Hence, policymakers are expected to continue showering the economy with support and further stimulus. Where will this support come from? Well, the consensus continues to see monetary, rather than fiscal, policy doing most of the work. First, the recent rise in credit growth shows that policymakers have backed away somewhat from the need to cut leverage and debt. Second, the PBoC has reiterated its support for SMEs, stating its intention to increase the amount and reduce the cost of loans to small firms. Third, further cuts to banks’ reserve requirement ratios are expected.

Plus, speculation remains as to whether the PBoC will use a weaker CNY as a tool to counter trade tensions. The PBoC Governor hinted that there was no line in the sand for the currency, nor was it wedded to defending the nation’s currency at a particular level.

This was interpreted as a signal that it would allow USD/CNY to break above 7. We still feel that the Bank will be reluctant to do this, amid fear of losing control of the currency and concern that capital outflows will, as in 2015, trigger a deeper depreciation. Such a move would also likely trigger US retaliation, which once again refrained from labelling China as a currency manipulator. However, with CNY volatility increasing, much will depend on the outcome of the G20, although we suspect that allowing the CNY to tumble further may merely offer a potential solution to one problem by creating another.

CHF – A safe franc again?

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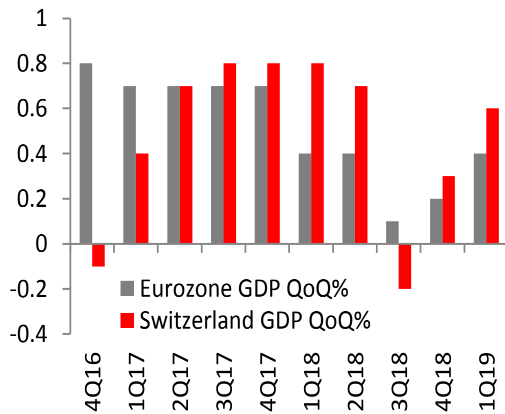
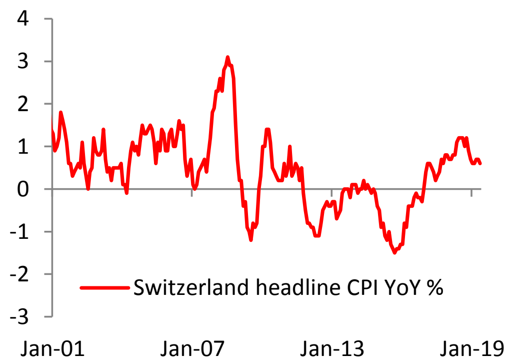
Chart 11: Swiss GDP growth picked up again in Q2-19…



Source: Bloomberg, Santander

Chart 12: …but inflation is expected to remain low



Source: Bloomberg, Santander

We continue to believe that the Swiss franc should be weaker than it is. However, the SNB's very loose monetary policy has not proved sufficient to significantly or sustainably pull the CHF lower, even before other central banks' recent adoption of more cautious/dovish rhetoric. Further, the Swiss economy has held up well, and there are signs that the franc may have been boosted by the recent decline in risk appetite amid global trade tensions.

The SNB kept its monetary policy unchanged at its June meeting. Given the uncertainty surrounding Libor, the Bank announced that it was introducing a new 'policy' rate to replace its previous benchmark Libor rate. However, this new rate implies no substantive changes, with the Bank indicating that sight deposits still face a -0.75% interest rate.

In addition, the SNB continues to warn that the CHF is 'highly valued' and that it reserves the right to intervene in the FX market to weaken it. Given the SNB's low 'policy' rate, large balance sheet and rhetoric, the downside pressure on the CHF should be unbearable, but it is not proving the case.

Over the last three months, the CHF has performed positively against all of its G10 peers, with the exception of the yen. This might suggest that despite its negative rates, the franc is once again being viewed as a safe-haven investment against trade tensions and weak equities, etc.

Previously we had suggested that the CHF had lost its attraction as a safe haven, due to its negative carry. However, over the last three months, as trade tensions have mounted, EUR/CHF has tended to move more in line with USD/JPY, showing a correlation of 0.61, compared to just 0.17 in the prior three months.

Hence, demand for the safety of both the yen and the CHF appears to have increased as risk appetite has declined. Nevertheless, these pressures may be asymmetric for the franc and if trade tensions, etc. ease over the coming months it cannot be guaranteed that the CHF will weaken. We recall that the CHF soared in recent years as Eurozone risks mounted, but did not reverse these gains when those European fears abated.

In addition, the Swiss economy continues to hold up well against the 'strong' currency. The SNB still expects growth this year of around 1.5%, with Q1-19 GDP exceeding expectations, growing by a CHF friendly 0.6% QoQ. But the Bank is warning that downside global growth risks could spill over quickly to Switzerland. Once again, the risk to the CHF is asymmetric, with good Swiss activity supporting the CHF, but soft growth, caused by a global slowdown, also now likely to be CHF positive, if it implies a further decline in risk appetite.

Inflation is still forecast to remain very weak, staying below the 2% target. CPI is forecast at 1.1% in 2021. Hence, the SNB is not expected to change policy any time soon, and certainly not before the ECB. Thus, another downside CHF risk is that with the SNB having little room to run a looser policy, G10/CHF crosses will be pulled lower, as other banks ratchet up the dovish rhetoric and/or ease policy. In such a situation, the SNB may have few options open to it, other than merely accepting a stronger CHF or intervening to weaken it, which traditionally has tended to have mixed results.

CAD – Still a good performer

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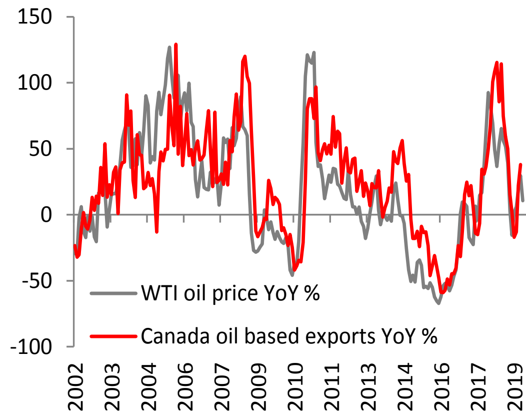
We remain positive on the CAD. The currency is still a strong performer against its G10 peers. The Bank of Canada's recent dovish rhetoric did weigh on the currency, but this is now being countered by similar comments from other central banks. The decline in the oil price has also been a drag on the currency, but recent economic data have been good and the BoC still expects recent slower growth to be temporary.

We reiterate that the CAD has been a strong performer throughout 2019. However, because of the market's main focus on USD/CAD, the currency's gains against other developed market peers sometimes goes unnoticed.

That said, absolute downside pressure on the CAD has mounted over the past few months. First, the oil price has declined. Second, Canadian GDP growth has disappointed. Third, the Bank of Canada adopted a more dovish approach in April, which encouraged the interest rate market to price out the chance of a rate hike in 2019.

In terms of the oil price, the WTI measure has been falling since late April. It dropped from a high at USD66.30/bbl on 23 April, to just above USD50/bbl in mid-June. Given that Canada is an oil-producing economy, the CAD tends to be correlated with changes in the oil price.

Chart 13: Swings in the oil price should impact both the Canadian economy and the CAD



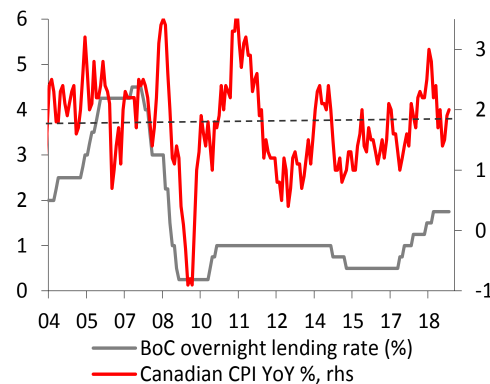
Source: Bloomberg, Santander

However, since late April the CAD has proved resilient, posting gains against all its G10 peers with the exception of the yen and CHF, which suggests that other factors, especially global risk and the Fed outlook, may have outweighed the oil effect.

Indeed, the correlation between USD/CAD and WTI has completely broken down in the short term. Over the last six months the correlation has been almost zero, suggesting that oil has had no impact on the CAD.

However, the longer-term, five-year, correlation is a more intuitively reasonable -0.75, i.e. oil rises, USD/CAD goes down and the CAD strengthens. Our analysis suggests that this long-term link still implies USD/CAD is overvalued given the oil price and should be closer to 1.3000.

Chart 14: The (BoC) expected pick-up in activity and firm inflation could pull the BoC away from its dovish stance



Source: Bloomberg, Santander

GDP data have not been a CAD positive. The economy grew only 0.3% QoQ in annualised terms in Q1-19. In addition, global trade tensions imply more risks. However, the BoC sees the late 2018 and Q1-19 weakness as temporary and expects growth to pick up looking forward.

In April the Bank revised its 2019 GDP forecast down to 1.2% from 1.7%, but 2020 was unchanged at 2.1% and 2021 at 2%. Further, employment data remain very strong, with 5.4% unemployment the lowest on record amid signs of wage growth. Hence, both headline and core CPI are expected to hover around the target 2% level.

Consequently, although the BoC adopted a more dovish stance recently and 2019 rate hikes have been priced out, the economic outlook should still allow for rate hikes in 2019, and crucially provide CAD support by allowing BoC policy to be less dovish than other central banks. Forthcoming data, especially April GDP, released on 28 June, will be key to showing signs of the quick pick-up in activity that the Bank is expecting.

AUD – Wounded by the first rate cut since 2016

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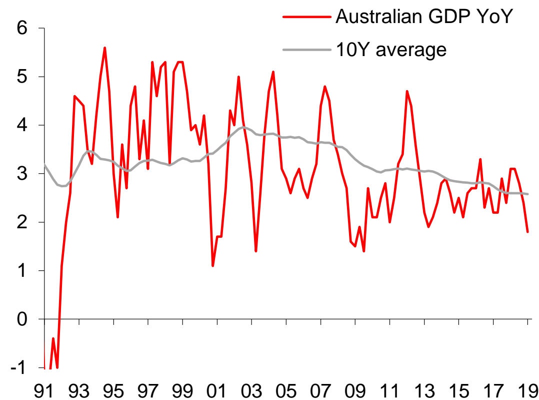
We retain a cautious stance on the AUD in 2019. Persistent global trade uncertainty, as well as softer domestic data have kept the AUD under pressure over the past quarter. The RBA cut rates in June, but we expect another cut to come in August, dragging AUD/USD down to 0.68 in Q3-19. We still see the pair ending the year at close to 0.70.

The Australian economy last experienced a recession in 1991. Back then, George H. W. Bush was still the US president, Amazon Inc., now the world's largest company, had not even been founded, and the first ever mobile text message had not yet been sent. In other words, the Australian economy has seen many years of uninterrupted growth, 27 of them, in fact.

Chart 15: Domestic growth rates have fallen to multi-year lows (%)



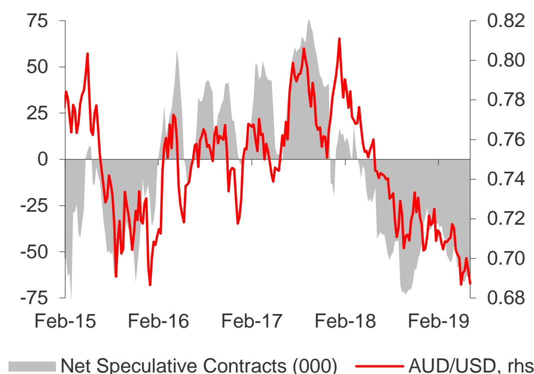
Source: Bloomberg, Santander

But all good things come to an end, and there is growing speculation that Australia's solid run is showing signs of strain. Indeed, growth fell to 1.8% YoY in Q1-19. This is a 10-year low, and well below historical growth levels (Chart 15).

A day before this GDP release, the RBA cut interest rates by 25bp, to 1.25%, a new all-time low. This followed a record 30 meetings with unchanged rates. The dovish shift was expected, so had already been priced into the AUD. However, with the RBA tending to cut rates in twos in the past (see RBA set to cut rates after record 30 meetings unchanged), we expect another 25bp cut to come in August.

A growth rebound would reduce the chances of additional rate cuts thereafter, but while the RBA still forecasts annual growth at 2.75% in both 2019 and 2020, these numbers are starting to look a little optimistic. Indeed, with home loans and building approvals significantly down, and house prices still falling sharply, household spending and confidence are likely to take a hit, as household debt-to-income ratios rise to new highs.

Chart 16: Speculators hold a large net short AUD position, but this is now very close to the May 2015 all-time high, at 76.85k contracts



Source: CFTC, Bloomberg, Santander

Aside from the soft growth data, the unemployment rate has risen in 2019. At 5.2% currently, this is significantly above the RBA's latest "full-employment" estimate, at 4.5%. Recently, RBA assistant governor Ellis signalled that a jobless rate closer to 4% may be needed. Either way, it is clear the Bank wants the unemployment rate to fall further.

As well as missing its "full employment" target, the RBA is struggling to hit its 2-3% inflation target. In Q1-19, headline CPI fell to just 1.3% YoY, a 10-quarter low. Consequently, growth, jobs and inflation data are all currently pointing to looser monetary policy. In fact, the market has even begun to speculate on whether the RBA may eventually need to begin its own QE programme. Even the discussion of this is likely to keep the AUD restrained in the months ahead.

Global trade pressures persist, and these should continue to impact the AUD in the months ahead. After all, China imports about a third of Australian exports, so if the US-China trade conflict hurts the Chinese economy, this is likely to negatively affect the Australian economy. Global trade uncertainty, domestic data and a dovish RBA all point to a soft AUD in the month ahead. However, as the speculative market already has a large net-short AUD position (Chart 16), we only see limited scope for an even softer AUD/USD.

NZD – Soft growth and international uncertainty

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An uncertain global economic backdrop has weighed on the NZD throughout Q2-19, and this, together with a more expansive monetary policy from the RBNZ, is likely to continue to drag the currency lower in the months ahead. As the second weakest developed market currency year-to-date, much of the bad news is probably already priced into the NZD. However, we are cautious on the NZD in the short term and see NZD/USD sitting close to 0.65 in Q3-19.

The RBNZ cut rates in early May, the Bank's first decision under its newly-established seven-person Monetary Policy Committee. It has not decided on monetary policy again since, but does so on Wednesday, 26 June.

Both we, and the market, expect the Bank to leave rates at 1.50% at this meeting. However, the RBNZ's rhetoric will be important, as there is far more uncertainty over what it will do thereafter. The market is pricing in a 94% chance of a further rate cut in 2019, but economists are split as to when the next cut will come, and how many will follow.

Comments by RBNZ assistant governor Hawkesby added to this uncertainty (and boosted the NZD) in early June, as he suggested rates will remain "broadly around the current level". However, we see little point in a one-off 25bp rate cut, some 30 months after its last, especially when most commercial banks only passed on about 15bp of this to consumers. Hence, we expect another cut to come in August. We would not rule out a further cut in November, but this will be data dependent.

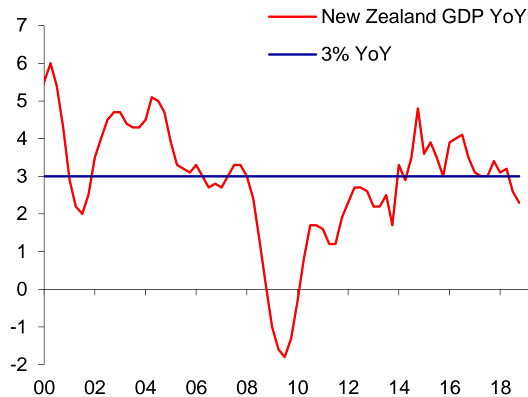
Just 18 months ago, the RBNZ cash rate was higher than any of its developed market peers. However, this yield advantage has gradually eroded since then, with the cash rate overtaken by the US and Canada bank rates. Further RBNZ cuts could see it fall into fourth place by year-end (Chart 18).

After the RBNZ rate cut in May, Deputy Governor Bascand suggested that New Zealand's economy needs to grow at around 3% a year for the central bank to meet its inflation and employment goals. The Q1-19 GDP data showed growth at 2.5% YoY. While unchanged since Q4-18, it is below 3%, and therefore implies that a loose policy is still needed.

At the end of May, New Zealand's Finance Minister unveiled the government's 2019 budget. Net expenditure was lifted to NZD3.8bn per year over the four tax years ending June 2023 (up from NZD2.4bn in the previous budget). Despite the increased spending, the Treasury downgraded its GDP estimates, and now sees growth of just 2.1% for the year ending 30 June 2019 (2.9% predicted in December).

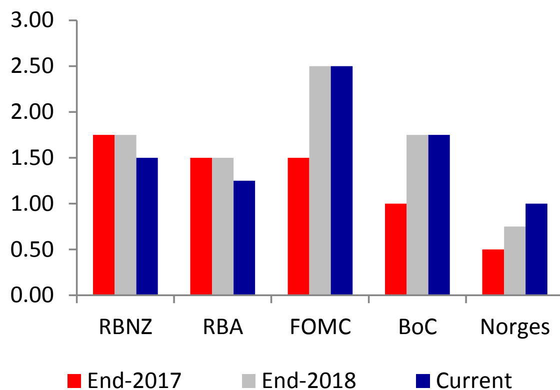
Domestic growth has been hurt not only by softer domestic demand but also by a cooling global economy. In fact, both the Finance Minister and the RBNZ have warned that the economy faces continued risks from the US-China trade dispute. These global risks are likely to continue to limit the currency in the month ahead.

Chart 17: GDP growth is below the 3% YoY rate that Deputy Governor Bascand suggested is needed for the RBNZ to meet its inflation and employment goals



Source: Bloomberg, Santander

Chart 18: The RBNZ base rate has been losing its yield advantage in recent years (%)



Source: Bloomberg, Santander

SEK – Inflation boost

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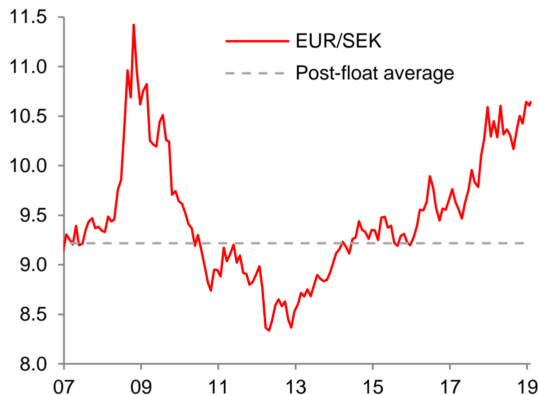
We continue to hold a cautious stance on the SEK. Domestic data have picked up a little over the past month, but the backdrop of international uncertainty amid the US-China trade dispute continues to weigh on the currency.

EUR/SEK touched a 10-year high in mid-May, but the cross has dropped back below 10.7 in June, with the SEK boosted by firmer inflation data. We expect the Riksbank to struggle to squeeze in a rate hike this year, but still see the cross edging towards 10.6 in Q3-19 and to 10.4 by year-end.

Chart 19: EUR/SEK hit a 10-year high on trade tensions in May…



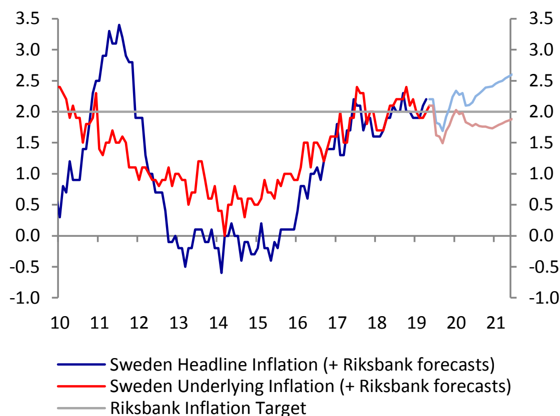
Source: Bloomberg, Santander

The SEK has struggled throughout 2019 and continues to be by far the worst performing G10 currency year-to-date. A more cautious Riksbank at the end of April, as well as escalating US-China trade tensions, prompted a particularly poor start to May for the SEK, with EUR/SEK rising to a 10-year high, at above 10.8.

The SEK has recovered over the past few weeks, with firmer inflation data for both April and May boosting the currency and pulling the cross back below 10.7. CPIF has been comfortably within reach of the Riksbank's 2% inflation target for two years now, but it slipped below this level in Q1-19. As such, the Riksbank will have been relieved to see it creep back to its 2% target in April and to 2.1% in May.

The Riksbank still expects CPIF to drop to 1.5% over the coming months, and if this were the case, it would probably end the Bank's warning of a possible rate hike late this year. The Bank already tweaked its rate hike message in April, from suggesting a H2-19 hike to a late 2019 or early 2020 increase.

Chart 20: …but was supported after CPIF data rose back above 2%



Source: Riksbank, Bloomberg, Santander

The market is pricing in no change in rates from the Riksbank this year, so if it does manage to eke out a hike, it should boost the SEK. However, as the Bank has already suggested that high household debt means any hikes will need to be gradual, the scope for SEK upside is probably limited in this case. Further, although the Norges Bank has lifted rates twice this year, it will be difficult for the Riksbank to hike with the ECB still suggesting additional Eurozone stimulus may be required.

A December hike cannot yet be totally excluded, especially if CPI continues to rise, but the global backdrop of international trade fears and most developed market central banks turning more dovish is likely to restrict the Riksbank's ability to do so.

Recent growth data have been upbeat in Sweden, with the Q1-19 GDP print coming in at a solid 0.6% QoQ, following the very good 1.2% QoQ in Q4-18. Given the soft data last summer, annual growth (currently 2.1%) is likely to rise over the next couple of quarters. However, there are risks to quarterly growth, with the construction boom perceived to now be over.

The international backdrop is likely to continue to be the main driver for the SEK in the month ahead, with the currency vulnerable to changes in risk sentiment. The focus will be on US-China trade talks at 28-29 June G20 meeting, but also on whether global central banks feel forced to ease policy.

NOK – Hiking against the trend

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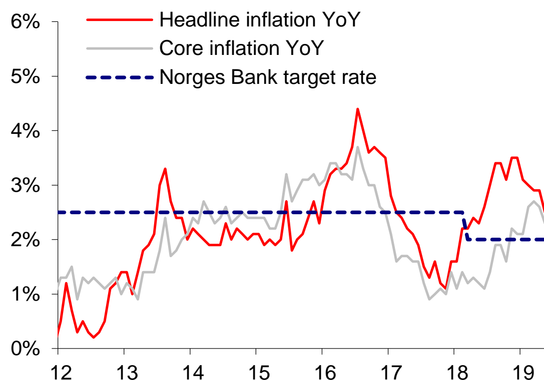
We are still positive on the NOK. Norway's economy is performing well, with most data strengthening in recent weeks, even though CPI has edged lower. The NOK should be supported by monetary policy, as the Norges Bank hiked rates again in June, at a time when most developed market central banks are turning significantly more dovish.

Global growth and the oil price will be key for the NOK in the short term, especially given the current geopolitical tensions in the Persian Gulf and the upcoming OPEC meeting. We still forecast EUR/NOK at 9.5 by Q4-19.

Domestic data have mostly been firm since early May. Trade, employment, confidence, retail sales and industrial production data have all improved over this time. Further, the Bank's regional network report for Q2-19 showed the outlook for producers jumping to its highest level in almost seven years.

The Q1-19 GDP print did disappoint though, with the mainland rate slipping to 0.3% QoQ (below the Bank's 0.64% forecast). Also, although inflation remains comfortably above the Bank's 2% target (Chart 21), it softened in May.

Chart 21: CPI dipped in April, but remains above target



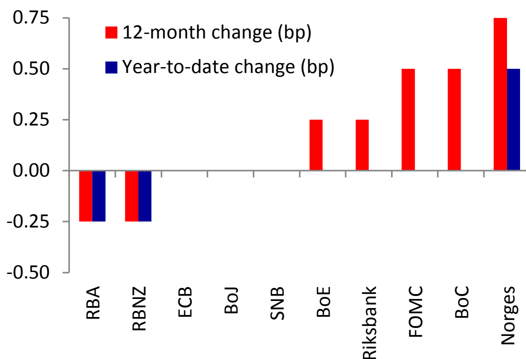
Source: Bloomberg, Santander

Nevertheless, the Norges Bank hiked rates in June by 25bp, taking the deposit rate to 1.25%, its highest level since early 2015. The decision itself was little surprise, as the Bank had suggested a hike was likely. It represents the Bank's third rate hike since last September, more than any other G10 currency central bank (Chart 22).

The Norges Bank expects to hike rates again over the coming six months , and we see a December hike as looking more likely than a September one.

Tighter monetary policy from the Norwegian central bank, at a time when developed market central banks elsewhere are turning more dovish, or even cutting rates, should be positive for the NOK.

Chart 22: The Norges Bank lifted rates again in late June, the Bank's third hike in just nine months, and more than any other G10 currency central bank in the same period



Source: Bloomberg, Santander

However, the yield advantage further hikes would usually imply is difficult to see, given that global trade and growth fears have been pulling most developed market bond yields lower in recent months, including those in Norway.

Further, as the petroleum sector makes up half of Norway's exports, the c.20% drop in the oil price since late April has been key to the NOK's direction, weighing on the currency.

Oil looks set to continue to lead the NOK in the weeks ahead, with the commodity focussed on the upcoming OPEC meeting in Vienna. Despite being initially scheduled for April, and then delayed until June, the OPEC meeting is now set to take place 1-2 July. At this meeting, OPEC is expected to extend production cuts into H2-19.

This could be important for the NOK, as if this and/or geopolitical risks given recent tensions in the Persian Gulf, limit oil supply, then any subsequent boost in the oil price should push up the currency.

LatAm FX: Main Themes

Currency	3M view	12M view	Main Themes
BRL	↗	⇨	• More auspicious prospects for the progress of the pension system reform have favoured the strengthening of the USDBRL cross lately. • Such a trend has been underpinned by the more dovish approach the FOMC has suggested recently. • As inflation dynamics have fared better than broadly expected, the Brazilian central bank may introduce further monetary stimuli going forward.
MXN	↗	↘	• Our call is for Banxico to keep a restrictive tone for the remainder of the year. • The market is pricing a more dovish Fed that could move pre-emptively before long. • The huge monetary policy differential between Banxico and the Fed will be supportive for the MXN, at least in the short term.
CLP	↗	⇨	• The importance of the external scenario will remain a recurring theme for USDCLP, with copper the best reflection of China-US trade tensions. • Risk factors centre on a pronounced global slowdown and copper prices suffering at the margin, both directly impacting local activity. • In the medium term, the convergence of the US economy toward its potential and a pick-up in emerging market growth would constitute an ideal scenario for the CLP, in our view.
COP	⇨	↘	• In June the COP rallied after BanRep decided to end the FX accumulation program that started in September as the currency hit its lowest level since 2016. Current COP levels are more in line with fundamentals. • External factors will continue to be a main driver of the COP's performance, yet we see some pressures coming from domestic factors, as the current account balance widens and fiscal accounts remain a source of concern. • The government's bet on growth as a key factor to meet its fiscal targets remains optimistic, in our view, as leading indicators continue to point to a moderate recovery.
ARS	⬆	⇨	• The peso has appreciated 2.8% in June (to Tuesday 18 June), while the central bank policy rate has dropped 462 basis points. • CPI falling to 3.1% in May, a surprisingly placid mood in the country, and the apparent shift to the centre of the political spectrum by the two most important political contenders are at the root of the encouraging performance. • The factors above, together with the maintenance of a tough macroeconomic policy as agreed with the IMF, enable us to project a stable FX path in the coming two months.
PEN	⇨	↘	• The PEN remains one of the best performers among its LatAm and EM peers, recovering some ground after the sharp depreciation in May. • The external environment will likely be in the driver's seat, with copper prices and the US dollar being the main influences, while the central bank will likely intervene at times of high volatility. • The central bank's board seems comfortable with its holding stance, and with the slow start for the economy in the first quarter, we consider that the board will remain on hold until 4Q19.

Bullish Mildly Bullish ⇨ Neutral Mildly Bearish Bearish

Source: Santander.

BRL – Is that an open window?

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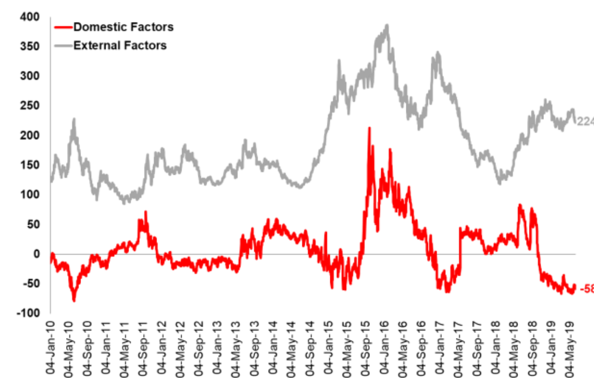
Although by no means a smooth process, the pension system reform bill has worked its way through Congress, increasing the likelihood that a first round vote in the Lower House will take place before the mid-year break in mid-July. If this is indeed the case, we, along with market participants, would be positively surprised, as a vote in 2H19 was our most likely scenario. As a result of this process going forward, after having breached the USD/BRL4.00 threshold, which led the Brazilian Central Bank (BCB) to intervene in the FX market, the improvement on the political front recently pushed the Brazilian exchange rate all the way back to the vicinity of USD/BRL3.85.

Moreover, the proposal outlined by the Lower House's Special Commission has marginally diluted the bill presented by the Federal administration, thereby increasing the likelihood that a robust reform will be implemented and, hence, substantial savings obtained. According to our calculations, the reform should lead to savings of approximately R$750 billion in the next 10 years — an amount close to the volume of savings (R$800 billion) implied in the original proposal sent to Congress by former President Temer. Therefore, in addition to making room for other reforms to be assessed by congressional representatives, we believe that the potential overhaul of the pension system could thwart the deterioration of the fiscal balance and thus enhance market participants' perception of Brazilian financial assets.

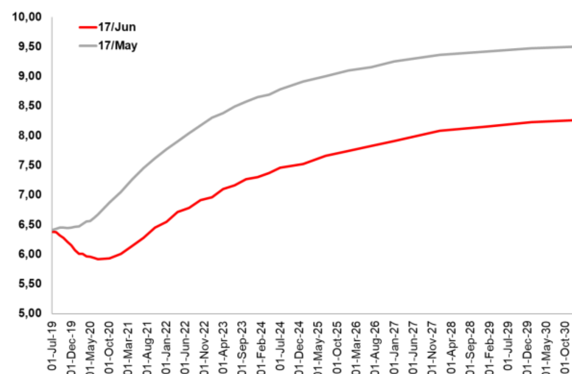
Chart 23: Brazilian 5Y CDS – Breakdown by influence factors (bp)



Source: Santander, Bloomberg

Besides the potentially positive impact on financial asset prices, the potential approval of the pension system reform could eliminate the last source of concern preventing the BCB from implementing further stimuli for the economy. We note that domestic activity indicators continue to suggest a gradual recovery trend; current inflation dynamics remain favourable; market participants' inflation expectations are firmly anchored at targeted levels; and there are mounting signs that monetary policy stances in leading economies are unlikely to change from the accommodative nature by which they are currently characterised. Thus, except for concerns about fiscal dynamics, all the conditions required for a looser monetary policy have seemingly been met. Hence, if the pension system reform is approved, we believe that the monetary authority could embark on a new cycle of interest rate cuts in the country.

Chart 24: Brazilian domestic yield curve (% pa)



Source: Santander, Bloomberg

Consequently, we foresee a strengthening BRL in the aftermath of potential structural changes implied by the pension system reform and believe that the monetary loosening that could follow is likely to limit the room for a perennial strengthening trend. For 2020, we continue to anticipate a weaker BRL compared to our YE19 FX rate of USD/BRL 3.90.

MXN – The risk is for a MXN appreciation in the short term

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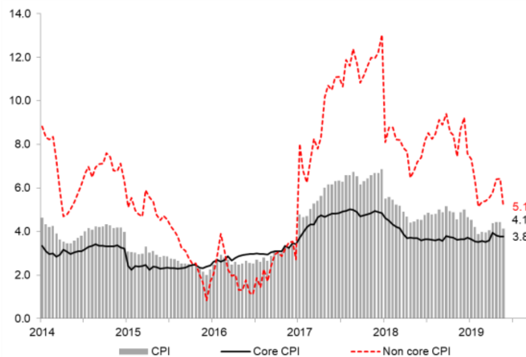
Although the Mexican economy is weakening, our call is for Banxico to keep a restrictive tone for the remainder of the year. Core inflation is not only sticky to the downside but slightly higher. Also, we see a risk of more credit rating downgrades, although we do not expect these to materialise in the short term. On 11 June, we revised our GDP growth estimate downwards. We now see the Mexican economy growing by 1.0% and 1.5% in 2019 and 2020, respectively, down from our previous forecasts of 1.5% and 1.8%. The first quarter of 2019 was affected by one-off factors such as gasoline shortages, and the first half of the year has seen some uncertainty surrounding the beginning of the new administration, which has affected both private investment and consumption. The pledge of fiscal discipline by the administration means that government expenditure is far behind schedule. Meanwhile, private sector investment is still awaiting more clarity on the high real interest rate environment, assessing the new administration's plans, waiting for USMCA to be approved, and becoming more cautious given the perceived risks to global growth.

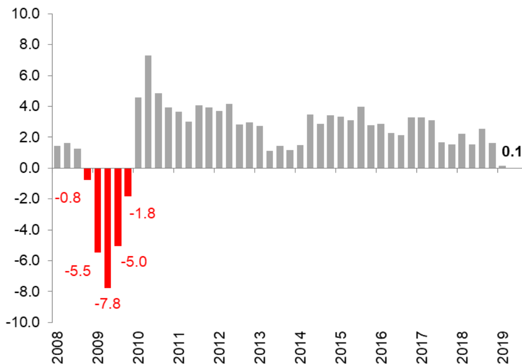
Chart 25: Consumer prices (y/y %)



Source: Santander, INEGI

We believe global growth risk could intensify next year, in line with the market pricing a more dovish Fed that could move pre-emptively before long. On that basis, we also revised downward our Mexican GDP growth forecast for 2020. It is unclear at this juncture whether the global economy was already decelerating, with the trade disputes exacerbating the problem, or if the global economy was progressing reasonably and the trade disputes have begun to threaten a global deceleration. Whichever is the case, global growth is at risk, and we believe the risk could intensify in 2020. A global deceleration in 2020, especially in the US economy, would make any recovery in the Mexican economy a challenge.

Chart 26: Gross domestic product (y/y % s.a.)



Source: Santander, INEGI

The significant monetary policy differential between Banxico and the Fed will be supportive for the MXN, at least in the short term. Banxico may stay on hold for the remainder of the year, while the market is pricing a few cuts by the Fed this year. Nevertheless, with global rates at the long end of the yield curves already collapsing, Mexican rates at the long end have substantial value, as our forecast for the coming years calls for Banxico to catch up with the Fed next year (as economic growth decelerates), and most likely close the spread with the Fed from current levels as core inflation recedes going into 2020. This is also supportive for the MXN.

On this basis, we are revising our year-end USDMXN FX forecasts for 2019 and 2020 to 19.8 and 20.5 from 20.5 and 21.0, respectively. By the same token, we now see the yield for the Mbono 29 finishing 2019 and 2020 at 7.9% and 7.7%, from our previous 8.60% for both years. In addition, the new agreement between US President Donald Trump and the Mexican government that prevented the imposition of tariffs on Mexican exports to the US could pave the way for a prompt resolution of USMCA.

CLP – BCCh to create FX asymmetry, not direction

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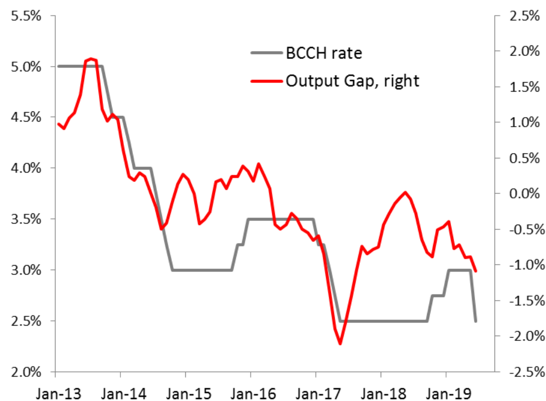
In the last few weeks, the news flow has been predominantly negative for the CLP, with the USD trading strong in global markets, copper prices under pressure, and the BCCh cutting rates unexpectedly by 50bp on 7 June. As a result, the USDCLP rate continues to trade close to the 700 handle as this report goes to press, underperforming broad EM currencies and commodity currencies (approximately 1% in the last four weeks). Offshore positioning indicates that non-residents remain long USD in Chile, although these positions have been stable in the past few weeks.

On the domestic front, the BCCh poured a bucket of cold water on local investors, cutting rates by 50bp to 2.50%, only six months after signalling that its next move would be a hike. The Board stated that the stimulus needed to be "recalibrated", as the neutral interest rate estimate was reduced by 25bp, to 4.00%, and its estimate for potential growth was raised to 3.4%, mainly due to the effects of immigration on the labour supply. This, coupled with the softening of the economy in the last few months and the deterioration of the external outlook, led the Bank to cut rates in a bold move, given its recent history of a limited number of small rate adjustments (the MPR had been adjusted only eight times in the last four years, always by 25bp). Now BCCh guidance suggests that rates should remain stable in upcoming meetings, but the risks seem skewed to the dovish side, as the output gap could continue to widen in a context of low inflation.

Regarding growth, April's IMACEC came in at 2.1% y/y, and pushed the YTD average to 1.7% y/y vs. 3.6% in 4Q18. Some of this weakness is due to the always volatile mining sector, but the underlying trend also points to a slowdown: in the last six months, annualised non-mining growth was 2.3% vs. almost 3.7% y/y in 4Q18. Due to a positive base-year effect, growth figures should begin to improve in July, but in general local growth sentiment remains dovish: 2019 consensus fell to 2.9%, -70bp from February. On the inflation side, May CPI was a relatively high 2.3% y/y, but mostly due to a one-off adjustment in electricity tariffs; the core measure fell to 1.7% y/y, the lowest level in 10 months. Although the CLP is weakening, FX pass-through in the recent past seems to be negligible, so softening output gap conditions should continue to keep inflation at very comfortable levels, not far from 2%.

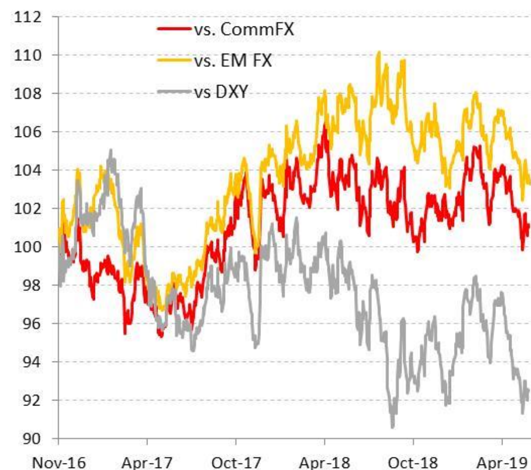
All in all, we continue to see the CLP highly correlated to external forces, i.e. copper and the global USD. The dovish stance of the BCCh will not be trivial, but should not drive the peso weaker per se. We do expect CLP underperformance vs. peers, but if the USD plummets globally after the Fed cuts rates, or as a result of some other factor, we would also expect to see a rally in the peso. As per our metrics, even considering recent rate cuts and weak copper prices, the CLP at 700 looks a little undervalued. We believe that in the coming months a range of 665-695 makes sense for the peso, based on the notion of a range-bound USD globally, where trade frictions set a floor and a dovish Fed sets a ceiling on the greenback.

Chart 27: BCCh policy rate vs. output gap



Source: Santander, Bloomberg

Chart 28: CLP vs non-USD benchmark, Nov'16=100



An increasing value means a stronger CLP and vice versa
Source: Santander, Bloomberg

COP – BanRep provides some relief

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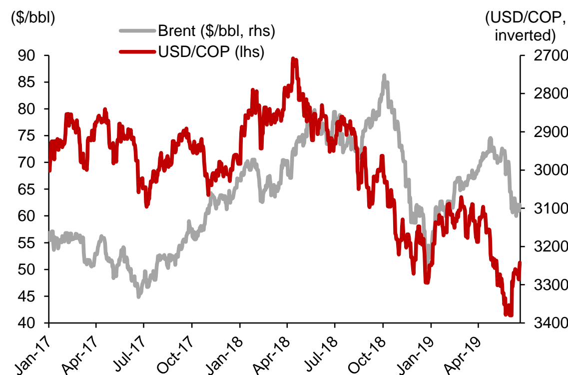
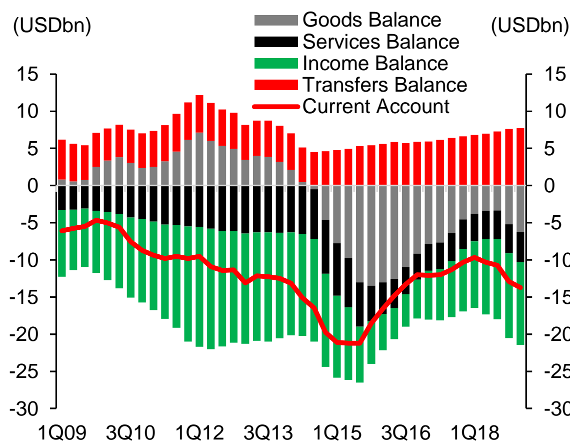
This section of the FX Compass will be on pause over the next few months until further notice

Chart 29:COP strengthens despite lower oil prices



Source: Santander, Bloomberg

Chart 30: Current account widens in 1Q19



Source: Santander, BanRep

Following our last FX Compass (published on 23 May), the COP remained under pressure in the last days of May, staying close to the 3400 level, the weakest since 2016, despite oil prices remaining high with Brent at over USD70/bbl. However, this trend changed in June, as the COP rallied following BanRep's decision to end the international reserve accumulation program that began in September. Indeed, after accumulating $1.8bn over nine months, in addition to the $1bn purchased from the Treasury, the board decided at its monetary policy meeting on 31 May to suspend the program in order to evaluate its impact on the currency. This coupled with a weaker dollar, which depreciated 0.82% in June according the DXY index, led the COP to rally and appreciate 4.08% during the first 20 days of June. The rally came despite the decline in oil prices, which have decreased almost 9% in the past month, with Brent hovering around USD60/bbl. After this rally, we consider that the COP is trading more in line with its fair value, at around 3250 COP/USD.

We consider that the COP may continue to trade close to the current levels in the short term. However, in the second half of the year, we expect the COP to come under renewed pressure and to end 2019 near the 3300 level, as the external environment remains uncertain, with trade tensions persisting amid the potential deceleration of the global economy. Moreover, domestic factors will play a part, as the current account continues to widen and the fiscal front remains a concern.

BanRep reported that the current account deficit widened in 1Q19 to -4.6% of GDP from -3.8% in 4Q18 and -3.5% in 1Q18. BanRep reported that in contrast to 1Q18, the wider deficit reflects mainly an increase in the external balance, in particular in the goods balance, but also FX depreciation accounted for 0.2% ppts of GDP. On the positive side, the deficit was mainly financed by FDI, which surged in 1Q19 and reached US$3.3bn, US$1.4bn higher than a year ago. In general, we consider that the current account deficit will remain above 4.0% of GDP, fostering strong demand for dollars.

In addition, fiscal policy remains a source of concern. The government recently presented the Medium Term Fiscal Plan where it confirmed its goal to decrease the fiscal deficit to -2.4% of GDP in 2019 from -3.1% in 2018, the original target before the Fiscal Rule Committee widened it to allow some room for the additional fiscal cost of Venezuelan migration. While the 2019 target seems achievable, concerns remain for 2020 onwards, as corporate tax revenues are expected to fall, as set out in the 2018 Financing Law, and costs continue to increase. Moreover, the government's bet on growth seems risky, as leading indicators continue to point to a moderate recovery, with growth slightly above 3.0% in 2019 and 2020, below the official forecasts of 3.6% and 4.0%, respectively. On this front, the opinion of the rating agencies remains divided, with Fitch (negative outlook) expressing concern about the government's optimistic view and Moody's more confident in the government's ability to meet its targets (stable outlook).

ARS – A visible horizon until 11 August primary elections

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The peso has appreciated 2.8% this month (to Tuesday 18 June), while the central bank policy rate -the 7-day Leliq- has dropped 462 basis points during the same period. This encouraging performance of the two most sensitive economic indicators reflects CPI falling to a 3.1% monthly rate in May, well below the 4.7% cyclical peak recorded in March, and a surprisingly calm mood in the country, despite still negative economic activity indicators. Last but not least, the encouraging performance of both FX and the CB policy rate also reflects the apparent shift to the centre of the political spectrum by the two most important political coalitions:

I. Centre-left alliance, led by Cristina Fernandez de Kirchner, who surprised Argentines in May by announcing that she would run for vice-president alongside her former cabinet chief, Alberto Fernandez (no relation), who is standing for the presidency.

II. Market enthusiasm for President Macri's choice of vice-presidential running mate. Macri's selection of Miguel Ángel Pichetto, the 68-year-old leader of the Peronist majority in the Senate, is a fresh sign that the 2019 presidential race is apparently increasingly focused on only two contenders.

Strict monetary and fiscal policies, in turn, continue to be enforced by Minister Dujovne and Governor Sandleris. As a result of these measures, the government has achieved the 2019 Treasury primary balance goal so far this year and has been able to freeze the monetary base, which has remained unaltered since September 2018, even as CPI inflation exceeded 50% annually in May.

We anticipate low FX volatility until the beginning of August, given seasonally high demand for M0, resulting from the 50% additional monthly salary locals will collect in July and the coming winter vacation, together with a positive seasonal peak of corn and soybean exports next month, which increases total proceeds from exports. At the beginning of August, public opinion polls should provide a more accurate indication of Argentines' voting intentions in the obligatory 11 August primary elections.

Thus, our base case scenario currently assumes that the government has finally begun to reap the benefits of: (i) its strict fiscal and monetary policy; (ii) the market's positive view of the shift towards the centre of the political spectrum by the two most important coalitions running in the October presidential elections; and (iii) the seasonal peak of exports of corn and soybeans in June and July, together with (iv) the higher seasonal demand for currency and bank reserves usually recorded from mid-June to late July.

Taken together, all of the above enables us to project a stable FX path in the coming 60 days.

Chart 31: ARS/USD and NI zone

Source: Santander, Central Bank, Bloomberg

PEN – Calm after the storm

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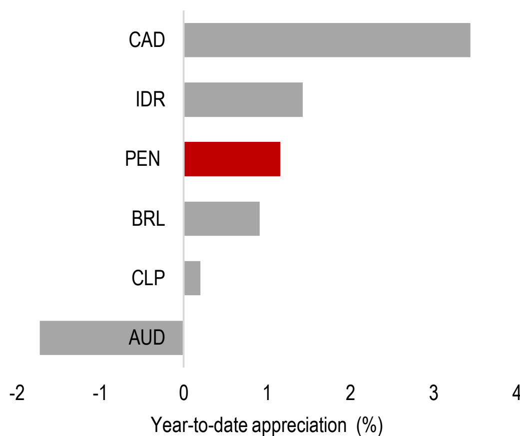
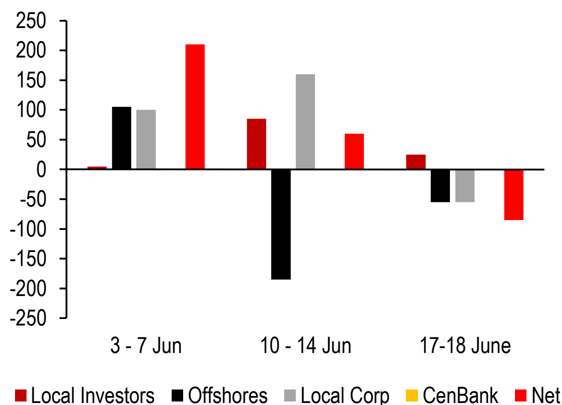
This section of the FX Compass will be on pause over the next few months until further notice

Chart 32: PEN performing well among copper exporters



Source: Santander, Bloomberg

Chart 33:USDPEN FX flows (billion)



Source: Santander, Central Bank

Since our last publication, news on the external environment has improved marginally, giving most EM currencies room to breathe. The PEN was no exception, and the currency appreciated 1.5% in the first three weeks in June, after reaching 3.38 at the end of May, the lowest level since the start of the year. The improvement can be partially explained by the weakening of the US dollar so far this month, as well as the improvement in metal prices, on the back of positive news on the US-China trade dispute, with the copper price increasing 2.1% in June. However, the improvement in the currency was capped by pressures coming from the demand for USD from offshore accounts and local players in the first two weeks of the month. In general, however, PEN continues to be one of the best performers among its LatAm and EM peers, and is still performing relatively well vs. other copper exporter currencies.

Despite the recent improvement, we consider that the risks remain biased to the downside as the external outlook is still uncertain, owing to the ongoing trade conflict between the US and China as well as expectations of a further slowdown in the global economy. While we see the PEN range-bound in the short term, we consider that the currency may come under pressure in 2H19.

On the local front, headline inflation jumped again to 2.73% y/y in May from 2.59% y/y in April, reflecting mainly inflationary pressures from food & beverages, as well as from transportation, due to higher gasoline prices and leisure prices, reflecting mainly higher cable prices. Core inflation (CPI ex-food and energy prices), on the other hand, remained practically stable at 2.56% y/y, but has been above 2.0% for almost a year, suggesting that demand side pressures persist.

In terms of growth, economic activity is showing signs of recovery, as it expanded 3.1% y/y in April, maintaining the pace after the 3.2% y/y growth registered in March, up from the 2.1% y/y and 1.6% y/y reported in February and January, respectively, despite fewer working days due to the Easter week. With this, GDP growth for 2Q19 should be close to 3.5%, improving from the low 2.3% y/y seen in 1Q19. In general, the economy continues to show signs of improvement after a slow start due to low public investment, reflecting the changes in local governments.

Finally, in terms of monetary policy, we consider that the central bank remained tilted toward the hawkish side in its latest communiqué, with the board still differentiating the primary sector from the rest of the activities and acknowledging that the economy ex-primary sector remains dynamic, continuing to believe that the output gap for these activities is narrowing. In general, we consider that the economy will pick up in the coming quarters, as local public investment normalises. However, given the weakness of the first quarter, we believe that the central bank will try to keep the policy rate on hold for longer and we see the first hike by end-2019.

CEE FX: Main Themes

Currency	3M view	12M view	Main Themes
PLN	↘	↗	• We decided to revise our 2H19 EUR/PLN forecasts down, since the starting point is now lower than we were expecting. In the short term, we think the zloty could give up part of its recent gains, but the remainder of the year should in general be positive for the Polish currency. The key assumption underlying this scenario is a gradual recovery of economic growth in Europe and only a mild deceleration in Poland.
CZK	↘	↗	• We think EUR/CZK could rise towards our 2Q target as we do not believe the central bank will deliver a rate hike in June. At the same time, we see a downward risk to our 2Q forecast.
HUF	⇨	↗	• We maintain our forecast that EUR/HUF should stay close to 325 up to the end of this year. We think the forint could depreciate on the back of the dovish tone of the central bank's communications. However, any weakening is unlikely to be significant, owing to the still robust results of the Hungarian industrial sector.
RUB	⇨	⇨	• We decided to revise our short-term forecast for USD/RUB. We believe that at the end of 3Q19 USD/RUB will remain around 65, owing to the rising expectations of lower interest rates in the US, which usually have a positive effect on emerging market currencies. We do not believe that weaker macro data from Russia, expected in the coming months, will push USD/RUB up.

↑ Bullish ↗ Mildly Bullish ⇨ Neutral ↘ Mildly Bearish ↓ Bearish

Source: Santander Bank Polska S.A.

PLN – Stronger starting point for 2H

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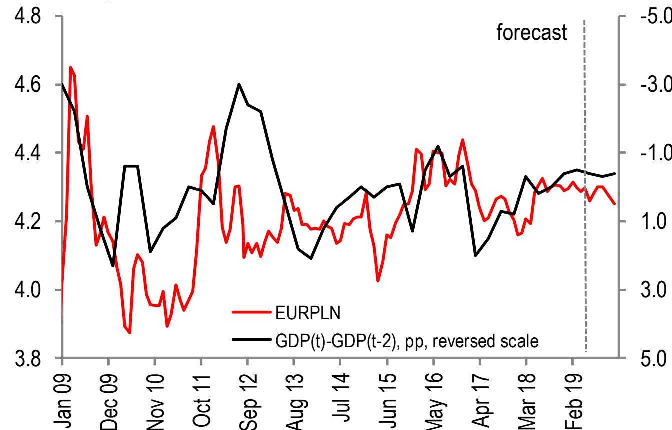
Chart 34: EUR/PLN and change of the Polish y/y GDP pace of growth



Source: GUS, Reuters, Santander

We decided to revise our 2H19 EUR/PLN forecasts down since the starting point is now lower than we were expecting. In the short term, we think the zloty could give up part of its recent gains, but the remainder of the year should in general be positive for the Polish currency. The key assumption underlying this scenario is a gradual recovery of economic growth in Europe and only a mild deceleration in Poland.

Recently, the zloty has tracked global equity trends and the EUR/USD performance. The decline in global stock indexes since early May weighed on the zloty. However, in mid-May the market mood started to improve, coinciding with the release of better-than-expected Polish macro data. The combination of supportive internal and external factors pushed EUR/PLN to 4.26, its lowest since January.

Overall, in 1H19 the zloty performed somewhat better than we had expected with EUR/PLN trading mostly in the lower half of the 4.26-4.34 range in which it has been holding since August 2018. In January, we thought the Polish currency could be under pressure in 1H19 and start to recover later in the year. However, the risk factors for the zloty's performance have had little impact: the economic slowdown in Poland is not that apparent, the Fed stepped back from 2019 rate hikes in early January and Brexit disruption has been limited for now.

The US interest rate market is pricing in a Fed rate cut in 2H19 and the global stock indexes suffered a correction in May after a robust start of the year.

However, equities have already started to recover and we think the market may again start to price in an improvement in the economy, since the general macro data seem not to be deteriorating further. Rising stock indexes – proxy of a robust demand for risky assets – should support demand for the zloty. Furthermore, we expect EUR/USD to rise later in the year.

We see two factors that could curb the zloty's gains – a gradual deceleration in Polish GDP growth and the neutral bias of the Polish MPC. As shown in the graph, it is not only the pace of GDP growth itself that matters for EUR/PLN but also any change in that pace. Since we maintain our view that the Polish economy should level-off after an exceptionally strong performance in 2018, domestic economic trends should be neutral for the zloty. Furthermore, we think the MPC will stay on hold, despite a continued rise in inflation, at least until the end of the year.

We are not assuming that recent changes in Polish politics (new finance minister) or the result of the autumn general elections will have a meaningful or persistent impact on the zloty.

CZK – Boosted by data

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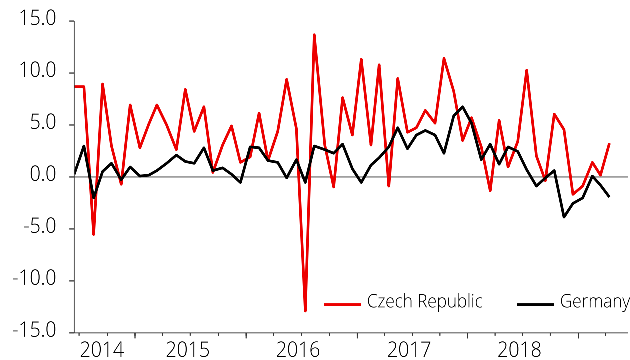
Chart 35: Czech and German industrial output (% y/y)



Source: Thomson Reuters Datastream, Santander Bank Polska

In the last couple of weeks, the Czech koruna benefited from the rise of global stock indexes, robust domestic macro data and hawkish comments by national bank members. We think EUR/CZK could rise towards our 2Q target, as we do not believe the central bank will deliver a rate hike in June. At the same time, we see a downward risk to our 2Q forecast.

In April, retail sales rose 4.8% y/y (the fastest pace since July) and industrial output 3.3% y/y (the highest annual percentage change since November), both exceeding expectations. On top of that, the flash estimate of 1Q19 GDP growth was slightly higher than expected (2.6% vs 2.5%), in line with the 2.6% of 4Q18. There was also an upside surprise from inflation, which neared the top end of the 1%-3% y/y tolerance band when it rose to 2.9% in May.

Robust macro data spurred hawkish comments by Czech central bankers, including the central bank's head, Jiri Rusnok. The governor said that more rate hikes should happen after a pause. Recall that after the last hike in early May, the statement said that rates could change in either direction. It seems stubbornly high inflation and decent macro data might have influenced the central bank's view. We think that interest rates could stay on hold at the June 26 meeting to make the pause announced in May more pronounced. Also, the room for a hike is reduced by the recent significant appreciation in the koruna.

HUF – Dovish central bank likely to weigh on forint

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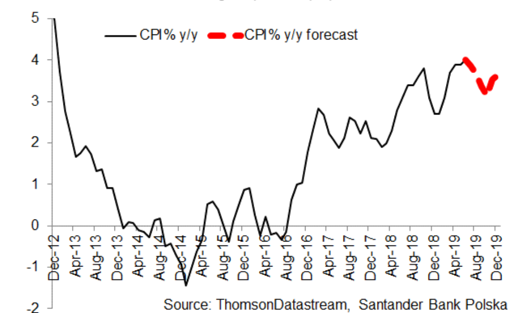
Chart 36: CPI Hungary (% y/y)



Source: ThomsonDatastream, Santander Bank Polska

We maintain our forecast that EUR/HUF should stay close to 325 up to the end of this year. We think that the forint could depreciate on the back of dovish signals from the central bank. However, any weakening will not be significant owing to the still robust results of the Hungarian industrial sector. We estimate June's industrial production rose by 6.7% y/y (vs. 6.0% y/y in April), while the June PMI reading is likely to reach 55.4 vs. 57.9 in May. Also, the inflation reading for June should stay close to 4.0% y/y (vs. 3.9% y/y in May), which would not support expectations of the central bank's rhetoric becoming more hawkish.

Since the end of May, EUR/HUF decreased to 322.20 from 327.30, hitting 320 on the way. HUF strengthening was a result of a fast decline of USD OIS rates (fully pricing in a 25bp cut in US rates on a one month horizon and next 25bp cut on a four month horizon). The marginal forint depreciation noticed in the second ten days of June was a reaction to the release of the Central Bank of Hungary (MNB) minutes for May, in which the MNB suggested that it planned to maintain accommodative monetary policy. The forint appreciation was not prevented by weaker Euro zone data for April and central bank representatives' comments about the possibility of a further deterioration of economic activity in the Euro zone.

In 2020 we expect a gradual HUF appreciation. The stronger forint should be supported by a return of inflationary tension due to the tight labour market. Consequently we forecast EUR/HUF at 315.00 in 2H20E.

RUB – Helped by the Fed

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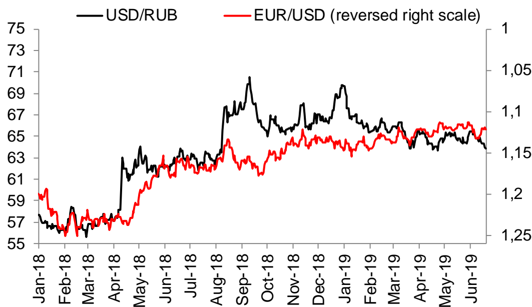
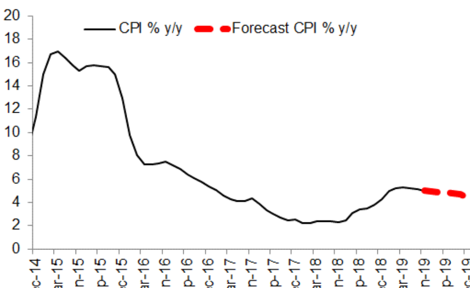
Chart 37: USD/RUB and EUR/USD



Source: ThomsonDatastream, Santander Bank Polska

Chart 38: CPI Russia (% y/y)



Source: ThomsonDatastream, Santander Bank Polska

We decided to revise our short-term forecast for USD/RUB. We now believe that at the end of 3Q19E USD/RUB will remain around 65, owing to rising expectations of lower interest rates in the US, which is usually positive for emerging market currencies. We do not believe that weaker macro data from Russia, expected in the coming months, will push USD/RUB up. We see Russia's June PMI-manufacturing reading at 49.9 (the second month in a row below 50) and we think that industrial production for June rose by 2.1% y/y, better than the poor 0.9% y/y in May but still below the average of the first five months of 2019. We expect June inflation to decrease to 5.0% y/y from 5.1% y/y in May.

Aggressive market pricing of a possible US interest rate cut helped USD/RUB to fall in June, despite the slide in the Brent oil price. As a consequence, USD/RUB is now at 64.20, from 65.40 in late May. The ruble's appreciation was not prevented by the Central Bank of Russia's (CBR) declaration in May that it wants to cut interest rates, which it did in mid-June. The ruble also appreciated despite the May PMI manufacturing reading being weaker than expected (with a drop below 50 for the first time since August 2018) and a negative surprise from the trade balance data.

At the end of 2019E we think the USD/RUB should climb to 67 as a reaction to the poor performance of the Russian economy. In our opinion, Russia will be negatively affected by the deterioration of Asian economies (as a consequence of Sino-US trade and tariff wars) and muted demand for commodities. Moreover the ruble will be hit by CBR's comments about the possibility of interest rate cuts. The argument for further monetary easing is a decrease in the central bank's economic growth forecasts for 2019 from 1.2%-1.7% to 1.0%-1.5%, due to the slowdown in world trade. It is also worth noting that, according to the CBR's head, the inflation generated by the VAT increase at the beginning of this year is slowly fading away and all this should allow rates to return to a neutral level around mid-2020.

G10 FX: IMM Speculative Positioning

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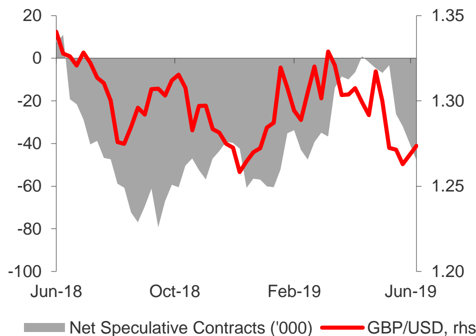
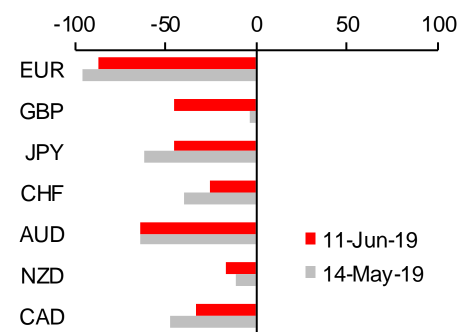
IMM commitment of traders report: GBP/USD position



- **Speculators have turned negative on the GBP in recent weeks.** Indeed, they have gone from holding a relatively neutral GBP position in April and early May, to a net short position of 45k contracts in the week ended 11 June. The resignation of Theresa May as Conservative party leader, which has sparked a leadership contest that may result in a more pro-Brexit prime minister, has weighed on the GBP positioning ahead of the 31 October Brexit deadline, as fears of a no-deal exit have risen.
- **The net long USD composite position is back above 200k,** reaching 212k contracts in early June, with the USD position benefitting directly from the more cautious GBP stance.
- **The net short JPY and CHF positions have declined,** as global trade fears (US, China, Mexico), and Brexit have prompted safe-haven demand for these currencies. The net short JPY and CHF positions have fallen by 16k and 15k contracts over the past four weeks, to around 45k and 25k contracts, respectively.
- **The speculative market is still net short the EUR,** although with EUR/USD unable to break below the 1.11 level in in May, speculators have reduced this position slightly, to c.87k contracts.

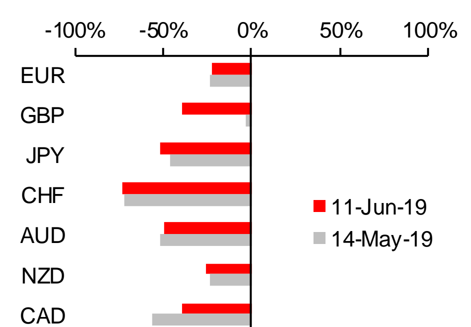
Net Speculative Contracts ('000s)*

	11-Jun-19	14-May-19	4w chg	YtD chg
USD***	212.4	175.1	37.3	209.8
EUR	-86.8	-95.3	8.5	-178.9
GBP	-44.8	-3.3	-41.5	-57.5
JPY	-45.2	-61.6	16.4	70.9
CHF	-24.8	-40.0	15.2	-10.9
AUD	-63.2	-64.0	0.8	-49.6
NZD	-16.1	-11.4	-4.7	1.5
CAD	-32.8	-47.6	14.7	-50.2



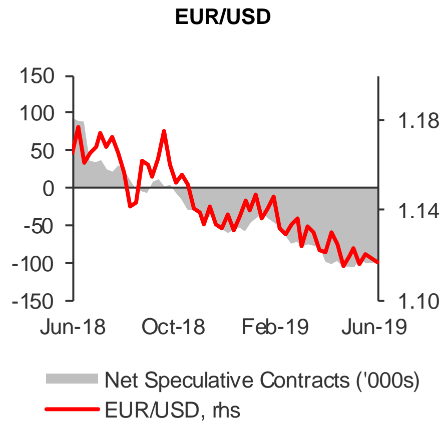
Net Speculative Contracts as % of Open Interest**

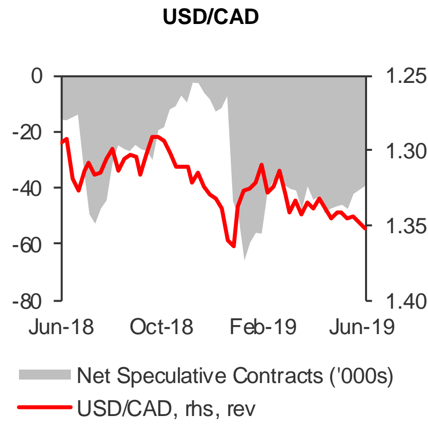
	11-Jun-19	14-May-19	4w chg	YtD chg
USD***	20%	14%	5%	20%
EUR	-22%	-24%	2%	-51%
GBP	-40%	-3%	-37%	-49%
JPY	-52%	-46%	-6%	5%
CHF	-74%	-72%	-1%	-56%
AUD	-49%	-52%	3%	-34%
NZD	-26%	-23%	-3%	7%
CAD	-39%	-56%	17%	-65%

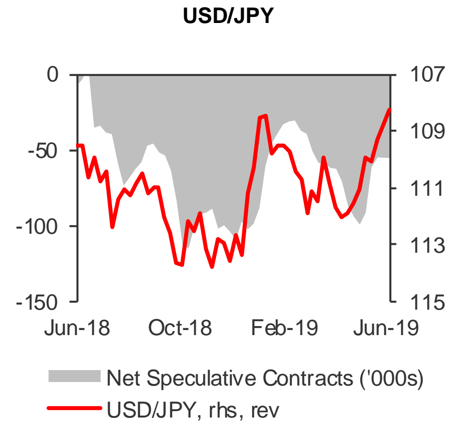


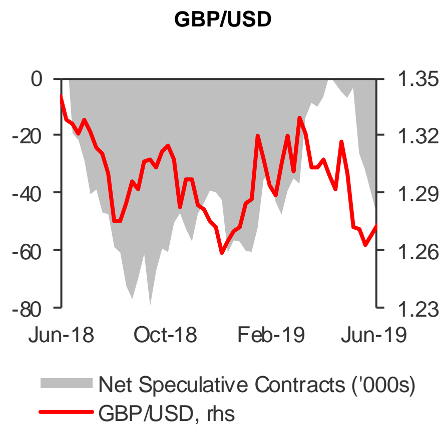
Sources: CFTC, Bloomberg, Santander. Note: *Net Speculative Contracts = Long non-commercial traders contracts minus short non-commercial traders contracts, **Open Interest = The total number of outstanding long and short futures contracts, ***USD composite index = USD composite index uses AUD, CAD, CHF, EUR, GBP, JPY, NZD and MXN IMM positioning to arrive at an aggregate USD position.

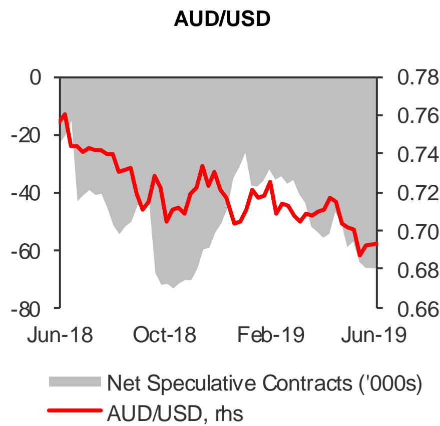
G10 FX: IMM Speculative Positioning

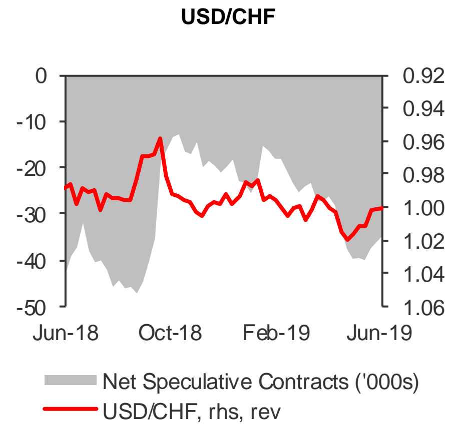


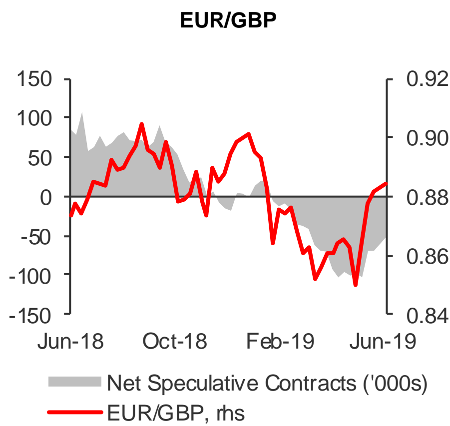


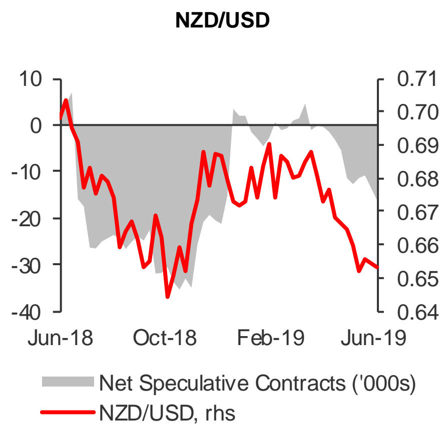


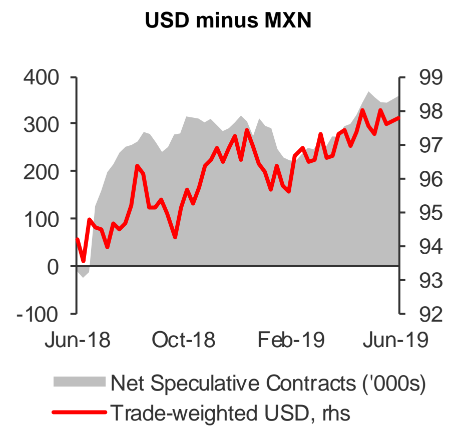












Sources: CFTC, Bloomberg and Santander. Note: IMM commitment of traders report

Latin America FX: Positioning indexes (Z-scores)

USD/BRL

Net Foreign (USD bn) — 12wk MA (%) — BRL (rhs)

40, 30, 20, 10, 0 | 4.5, 4.0, 3.5, 3.0, 2.5

Jun-15, Jun-16, Jun-17, Jun-18, Jun-19

Z-score USD/BRL

Z-score (Offshore USD/BRL longs) — 10-90%

USD longs

2, 1, 0, -1, -2

Jun-15, Jun-16, Jun-17, Jun-18, Jun-19

USD/MXN

Net Spec (% OI) — 12wk MA (%) — MXN (rhs)

80%, 40%, 0%, -40%, -80% | 23, 21, 19, 17, 15

Jun-15, Jun-16, Jun-17, Jun-18, Jun-19

Z-score USD/MXN

Z-score (USD/MXN longs) — 10-90%

USD longs

2, 1, 0, -1, -2, -3

Jun-15, Jun-16, Jun-17, Jun-18, Jun-19

USD/CLP

Foreign NDF (USD bn) — 12wk MA (%) — CLP (rhs)

30, 20, 10, 0 | 750, 700, 650, 600, 550

Jun-15, Jun-16, Jun-17, Jun-18, Jun-19

Z-score USD/CLP

Z-score (Offshore USD/CLP longs) — 10-90%

USD longs

4, 3, 2, 1, 0, -1, -2

Jun-15, Jun-16, Jun-17, Jun-18, Jun-19

USD/PEN

Foreign NDF (USD bn) — 12wk MA (%) — PEN (rhs)

10, 8, 6, 4, 2, 0, -2 | 3.6, 3.5, 3.4, 3.3, 3.2, 3.1

Jun-15, Jun-16, Jun-17, Jun-18, Jun-19

Z-score USD/PEN

Z-score (USD/PEN longs) — 10-90%

USD longs

3, 2, 1, 0, -1, -2

Jun-15, Jun-16, Jun-17, Jun-18, Jun-19

Sources: BM&F, CFTC, BCCh, BCRP, Bloomberg and Santander.

Euro Interest Rate Forecasts

Government Bond yield Forecasts

Germany	Current	3Q19	4Q19	1Q20	2Q20
ECB Depo	-0.40	-0.40	-0.40	-0.40	-0.20
3m	-0.57	-0.57	-0.52	-0.45	-0.39
2y	-0.75	-0.55	-0.45	-0.35	-0.15
5y	-0.66	-0.40	-0.25	-0.10	0.10
10y	-0.31	0.05	0.20	0.35	0.55
30y	0.26	0.60	0.70	0.85	1.00

Swap rate forecasts

Euro	Current	3Q19	4Q19	1Q20	2Q20
ECB Depo	-0.40	-0.40	-0.40	-0.40	-0.20
3m	-0.34	-0.32	-0.32	-0.25	-0.19
2y	-0.37	-0.15	-0.05	0.05	0.25
5y	-0.21	0.10	0.25	0.40	0.60
10y	0.20	0.60	0.75	0.90	1.10
30y	0.74	1.10	1.20	1.35	1.50

US Interest Rate Forecasts

Government Bond yield Forecasts

US	Current	3Q19	4Q19	1Q20	2Q20
FOMC *	2.50	2.50	2.50	2.50	2.50
3m	2.15	2.45	2.45	2.45	2.45
2y	1.72	2.30	2.40	2.50	2.60
5y	1.74	2.35	2.45	2.55	2.65
10y	2.01	2.40	2.50	2.60	2.70
30y	2.53	2.75	2.80	2.85	2.95

Swap rate forecasts

US	Current	3Q19	4Q19	1Q20	2Q20
FOMC *	2.50	2.50	2.50	2.50	2.50
3m	2.34	2.60	2.55	2.55	2.55
2y	1.74	2.35	2.40	2.50	2.60
5y	1.72	2.35	2.40	2.50	2.60
10y	1.95	2.35	2.45	2.55	2.65
30y	2.20	2.45	2.50	2.55	2.65

UK Interest Rate Forecasts

Government Bond yield Forecasts

UK	Current	3Q19	4Q19	1Q20	2Q20
MPC	0.75	0.75	0.75	0.75	0.75
3m	0.77	0.77	0.77	0.79	0.82
2y	0.58	0.75	0.80	0.90	0.90
5y	0.60	0.85	1.00	1.10	1.20
10y	0.81	1.10	1.20	1.25	1.25
30y	1.42	1.75	1.80	1.90	2.00

Swap rate forecasts

UK	Current	3Q19	4Q19	1Q20	2Q20
MPC	0.75	0.75	0.75	0.75	0.75
3m	0.78	0.85	0.85	0.87	0.90
2y	0.82	1.05	1.10	1.20	1.20
5y	0.86	1.20	1.30	1.35	1.40
10y	1.00	1.30	1.35	1.35	1.30
30y	1.18	1.50	1.50	1.55	1.65

G10 Central Bank Calendar

	Current Rate	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec
FOMC (Upper)	2.50	Unch.	-	Unch.	-	Unch.	Unch.	31	-	18	30	-	11
ECB (Depo)	-0.40	Unch.	-	Unch.	Unch.	-	Unch.	25	-	12	24	-	12
BoE	0.75	-	Unch.	Unch.	-	Unch.	Unch.	-	1	19	-	7	19
BoJ	-0.10	Unch.	-	Unch.	Unch.	-	Unch.	30	-	19	31	-	19
SNB	-0.75	-	-	Unch.	-	-	Unch.	-	-	19	-	-	12
BoC	1.75	Unch.	-	Unch.	Unch.	Unch.	-	10	-	4	30	-	4
RBA	1.25	-	Unch.	Unch.	Unch.	Unch.	-25bp	2	6	3	1	5	3
RBNZ	1.50	-	Unch.	Unch.	-	-25bp	26	-	7	25	-	13	-
Norges Bank	1.25	Unch.	-	+25bp	-	Unch.	+25bp	-	15	19	24	-	19
Riksbank	-0.25	-	Unch.	-	Unch.	-	-	3	-	5	24	-	19

Source: Bloomberg, Santander. Note: Current levels as at 20-June-19. For meetings that have already taken place, decision identified as +/- in bp, or "unch" for no change. "-" denotes no meeting taking place that month *FOMC rate refers to upper bound rate. **The FOMC announced in March that is would phase out its Quantitative Tightening between May 2019 and September 2019. US, EZ and UK rates forecasts as correct as at last I&E report (31 May 2019)

Brazil/Mexico Interest Rate forecasts

Brazil	Current	3Q19	4Q19	1Q20	2Q20
SELIC	6.50	5.75	5.50	5.50	5.50
NTNF Jan' 25s	7.31	7.25	7.00	7.00	7.00
NTNF Jan.' 29s	7.83	7.50	7.50	7.50	7.50

Mexico	Current	3Q19	4Q19	1Q20	2Q20
Banxico fondeo	8.25	8.25	8.25	8.00	7.75
Mbono Jun. '21s	7.66	7.75	7.85	7.80	7.75
MBono Jun. '29s	7.50	7.70	7.90	7.80	7.70

Chile/Colombia Interest Rate Forecasts

Chile	Current	3Q19	4Q19	1Q20	2Q20
BCCh TPM	2.50	2.25	2.25	2.00	2.00
BCP 5Y	2.90	2.80	2.80	2.75	2.95
BCP 10Y	3.17	3.40	3.40	3.35	3.45

Colombia	Current	3Q19	4Q19	1Q20	2Q20
Banrep O/N	4.25	4.25	4.50	4.75	4.75
TES Jul '24s	5.33	5.93	5.99	6.05	6.07
TES Apr '28s	6.08	6.43	6.54	6.61	6.64

Argentina/Peru Interest Rate Forecasts

Argentina	Current	3Q19	4Q19	1Q20	2Q20
LELIQ 7-day	65.44	57.90	48.50	43.88	37.00

Peru	Current	3Q19	4Q19	1Q20	2Q20
BRCP Ref. Rate	2.75	2.75	3.00	3.25	3.25

LatAm Central Bank Calendar

	Current Rate	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec
Brazil	6.50	-	Unch.	Unch.	-	Unch.	Unch.	31	-	18	30	-	11
Mexico	8.25	-	Unch.	Unch.	-	Unch.	27	-	15	26	-	14	19
Chile	2.50	+25bp	-	Unch.	-	Unch.	-50bp	18	-	3	23	-	6
Colombia	4.25	Unch.	-	Unch.	Unch.	-	21	26	-	27	31	-	20
Argentina*	65.44	-557bp	-356bp	+1803bp	+578bp	-320bp	~	~	~	~	~	~	~
Peru	2.75	Unch.	Unch.	Unch.	Unch.	Unch.	Unch.	13	10	14	12	8	13

CEE Interest Rate Forecasts

Poland	Current	3Q19	4Q19	1Q20	2Q20
Reference Rate	1.50	1.50	1.50	1.75	1.75
2y	1.59	1.65	1.70	1.85	1.85
10y	2.35	2.40	2.50	2.55	2.45

CEE	Current	3Q19	4Q19	1Q20	2Q20
Hungary	0.90	1.25	1.50	1.50	1.50
Czech Republic	2.00	2.00	2.25	2.50	2.50
Russia	7.50	7.25	7.00	7.00	7.00

CEE Central Bank Calendar

	Current Rate	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec
Poland	1.50	Unch.	Unch.	Unch.	Unch.	Unch.	Unch.	3	-	11	2	6	4
Czech Republic	2.00	-	Unch.	Unch.	-	+25bp	26	-	1	25	-	7	19
Hungary	0.90	Unch.	Unch.	Unch.	Unch.	Unch.	25	23	27	24	22	19	17
Russia	7.50	-	Unch.	Unch.	Unch.	-	-25bp	26	-	6	25	-	13

Source: Bloomberg, Santander. Note: Current levels as at 20-June-19. For meetings that have already taken place, decision identified as +/- in bp, or "unch" for no change. "-" denotes no meeting taking place that month. *On 7 August 2018 = Argentina's monetary policy committee voted unanimously to change the key interest rate to 7-day Leliq rate, which the bank has been changing on a daily basis since the start of October (the decision was made fortnightly previously).

Forecasts and returns vs. forwards and consensus (% non-annualised)

	3M	6M	9M
EUR/USD	**1.14**	**1.17**	**1.18**
vs.forward	0.9	3.5	4.4
vs.consensus forecast	0.9	1.7	0.9
GBP/USD	**1.30**	**1.31**	**1.33**
vs.forward	2.5	3.3	4.9
vs.consensus forecast	2.4	1.6	2.3
EUR/GBP	**0.88**	**0.89**	**0.89**
vs.forward	-1.6	0.2	-0.5
vs.consensus forecast	-1.5	0.4	-0.3
USD/JPY	**112**	**115**	**118**
vs.forward	4.0	6.8	9.5
vs.consensus forecast	3.7	6.5	10.3
EUR/JPY	**128**	**135**	**139**
vs.forward	4.9	10.5	14.4
vs.consensus forecast	4.7	8.5	11.4
EUR/CHF	**1.15**	**1.18**	**1.20**
vs.forward	3.2	5.9	7.7
vs.consensus forecast	2.7	4.4	5.3
USD/CHF	**1.01**	**1.01**	**1.02**
vs.forward	2.3	2.3	3.2
vs.consensus forecast	0.9	1.9	2.7
EUR/SEK	**10.6**	**10.4**	**10.3**
vs.forward	-0.3	-2.2	-3.1
vs.consensus forecast	-0.2	-1.9	-2.4
EUR/NOK	**9.6**	**9.5**	**9.4**
vs.forward	-0.7	-1.7	-2.7
vs.consensus forecast	-0.5	-1.0	-0.9
USD/CAD	**1.31**	**1.29**	**1.28**
vs.forward	-0.5	-2.0	-2.8
vs.consensus forecast	-2.2	-3.0	-2.3
AUD/USD	**0.68**	**0.70**	**0.70**
vs.forward	-1.9	1.0	1.0
vs.consensus forecast	-1.4	0.0	-1.4
NZD/USD	**0.65**	**0.67**	**0.68**
vs.forward	-1.4	1.7	3.2
vs.consensus forecast	0.0	1.5	1.5

	3M	6M	9M
USD/BRL	**3.75**	**3.90**	**4.00**
vs.forward	-2.3	1.6	4.2
vs.consensus forecast	-2.6	2.6	6.7
EUR/BRL	**4.28**	**4.56**	**4.72**
vs.forward	-0.8	5.9	9.5
vs.consensus forecast	-1.7	4.4	7.6
USD/MXN	**19.3**	**19.80**	**19.80**
vs.forward	2.0	4.6	4.6
vs.consensus forecast	-0.8	1.5	2.6
EUR/MXN	**22.0**	**23.2**	**23.4**
vs.forward	2.9	8.3	9.3
vs.consensus forecast	0.1	3.3	3.5
USD/CLP	**680**	**685**	**687**
vs.forward	-0.9	-0.2	0.1
vs.consensus forecast	-2.6	-1.1	-0.4
USD/COP	**3250**	**3300**	**3250**
vs.forward	0.3	1.8	0.3
vs.consensus forecast	1.6	2.3	1.5
USD/ARS	**48.0**	**52.0**	**53.9**
vs.forward	10.6	20.0	24.3
vs.consensus forecast	0.4	5.7	8.9
USD/PEN	**3.36**	**3.37**	**3.37**
vs.forward	0.9	1.2	1.2
vs.consensus forecast	0.9	1.5	1.2
EUR/PLN	**4.29**	**4.27**	**4.28**
vs.forward	0.8	0.4	0.6
vs.consensus forecast	-0.2	-0.5	-0.2
EUR/CZK	**25.8**	**25.6**	**25.4**
vs.forward	0.7	-0.1	-0.8
vs.consensus forecast	0.0	-0.4	-0.4
EUR/HUF	**325**	**325**	**320**
vs.forward	0.4	0.4	-1.1
vs.consensus forecast	0.9	0.9	0.0
EUR/RUB	**74**	**78**	**79**
vs.forward	3.9	9.9	10.8
vs.consensus forecast	0.2	4.0	2.8

Direct returns of long currency positions against the USD (or EUR), in %. Equivalent tenors for forwards. FX forecasts interpolated from end-of-quarter forecasts. Sources: Bloomberg and Santander.

G10 FX: Spot and forward rates

	EUR/USD	GBP/USD	USD/JPY	EUR/JPY	GBP/JPY	USD/CHF	EUR/CHF	GBP/CHF
Spot	1.130	1.268	107.68	121.69	136.58	0.984	1.112	1.248
1M	1.133	1.270	107.41	121.69	136.45	0.981	1.111	1.246
2M	1.136	1.272	107.17	121.72	136.33	0.978	1.111	1.244
3M	1.138	1.273	106.96	121.74	136.21	0.976	1.110	1.242
6M	1.145	1.277	106.34	121.79	135.81	0.969	1.109	1.237
9M	1.153	1.281	105.67	121.81	135.34	0.961	1.108	1.231
12M	1.159	1.283	105.11	121.85	134.91	0.955	1.107	1.226

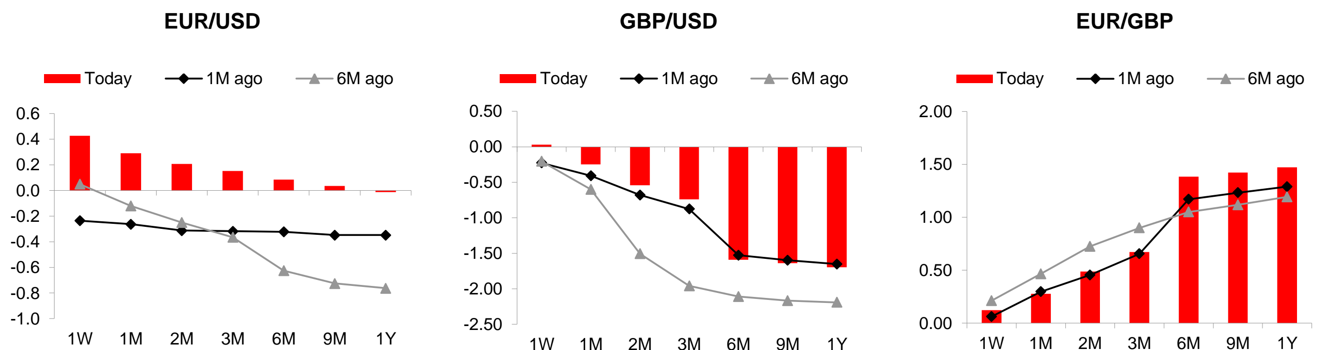
ATMf vol.

	EUR/USD	GBP/USD	USD/JPY	EUR/JPY	GBP/JPY	USD/CHF	EUR/CHF	GBP/CHF
1W	5.3%	5.9%	5.7%	6.0%	7.0%	5.3%	4.1%	5.8%
1M	5.0%	5.9%	6.0%	6.1%	7.4%	5.1%	4.0%	6.0%
2M	5.3%	6.4%	6.3%	6.4%	8.0%	5.3%	4.2%	6.4%
3M	5.4%	6.9%	6.5%	6.6%	8.3%	5.4%	4.3%	6.8%
6M	5.7%	8.8%	6.7%	7.0%	10.3%	5.7%	4.6%	8.5%
9M	5.9%	9.1%	6.9%	7.3%	10.5%	5.9%	4.7%	8.8%
12M	6.1%	9.5%	7.0%	7.5%	10.8%	6.1%	4.9%	9.1%

Implied/realized vol. ratio

	EUR/USD	GBP/USD	USD/JPY	EUR/JPY	GBP/JPY	USD/CHF	EUR/CHF	GBP/CHF
1W	0.92	0.99	0.95	1.00	0.98	0.90	1.03	1.00
1M	0.91	0.94	1.03	1.05	1.04	0.78	0.92	0.90
2M	1.01	1.04	1.13	1.05	1.10	0.93	0.97	1.02
3M	1.06	0.97	1.22	1.05	1.05	1.03	1.04	0.97
6M	1.04	1.07	1.05	0.99	1.02	1.02	1.08	1.06
9M	0.98	1.08	1.12	1.00	1.06	1.03	1.04	1.09
12M	0.98	1.15	1.15	1.00	1.12	1.08	1.05	1.17

25-delta risk reversals



Sources: Bloomberg and Santander. As of 20-June-19

Latin America FX: Spot and forward rates

	USD/ARS	USD/BRL	USD/CLP	USD/COP	USD/MXN	USD/PEN
Spot	43.3	3.84	684	3201	18.9	3.33
1M	45.4	3.85	683	3208	19.0	3.34
2M	47.5	3.86	683	3213	19.1	3.34
3M	49.4	3.87	683	3219	19.2	3.34
6M	55.6	3.90	684	3236	19.5	3.36
9M	61.4	3.93	684	3250	19.8	3.37
12M	66.4	3.95	684	3270	20.1	3.38

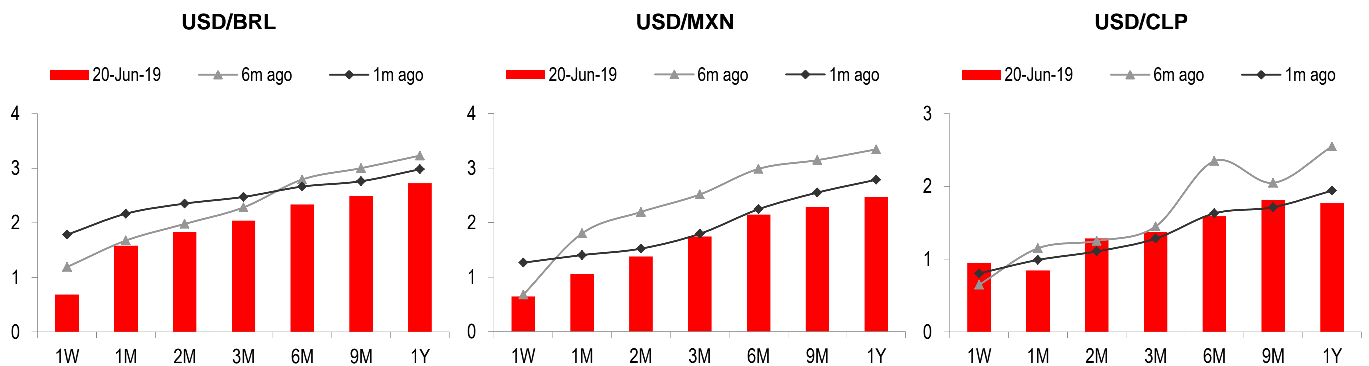
ATMf vol.

	USD/ARS	USD/BRL	USD/CLP	USD/COP	USD/MXN	USD/PEN
1W	8.00	13.61	9.05	10.07	8.46	3.17
1M	12.52	13.39	8.94	9.87	8.73	3.52
2M	15.72	13.54	9.17	10.19	9.44	3.77
3M	17.86	13.58	9.19	10.19	9.79	3.91
6M	25.83	13.62	9.36	10.60	10.53	4.37
9M	27.81	13.60	9.57	10.98	11.04	4.79
12M	28.94	13.63	9.66	11.25	11.45	5.01

Implied/realized vol. ratio

	USD/ARS	USD/BRL	USD/CLP	USD/COP	USD/MXN	USD/PEN
1W	1.15	1.30	1.07	1.80	1.02	1.01
1M	1.38	1.23	1.01	1.19	0.59	0.95
2M	0.81	1.16	1.03	1.05	0.77	0.93
3M	0.97	1.11	1.03	1.04	0.87	1.05
6M	1.49	1.10	1.06	1.16	1.03	1.21
9M	1.50	0.96	1.03	1.17	0.98	1.40
12M	1.21	0.94	0.98	1.18	0.94	1.40

25-delta risk reversals



Sources: Bloomberg and Santander. As of 20-June-19

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EXPLANATION OF THE RECOMMENDATION SYSTEM

RECOMMENDATIONS	
	Definition
Long / Buy	Appreciation of a given currency with an expected return of at least 5% in 3 months.
Short / Sell	Depreciation of a given currency with an expected return of at least 5% in 3 months.

NOTE: Given the recent volatility seen in the financial markets, the recommendation definitions are only indicative until further notice.

DEFINITIONS

***Net Speculative Contracts**	Long non-commercial traders contracts minus short non-commercial traders contracts.
****Open Interest**	The total number of outstanding long and short futures contracts. These data may not be the same as the IMM's total open interest data.
*****USD composite index**	USD composite index uses AUD, CAD, CHF, EUR, GBP, JPY, NZD and MXN IMM positioning to arrive at an aggregate USD position.

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