26 September 2019, 10:30 BST

FX COMPASS

Contents

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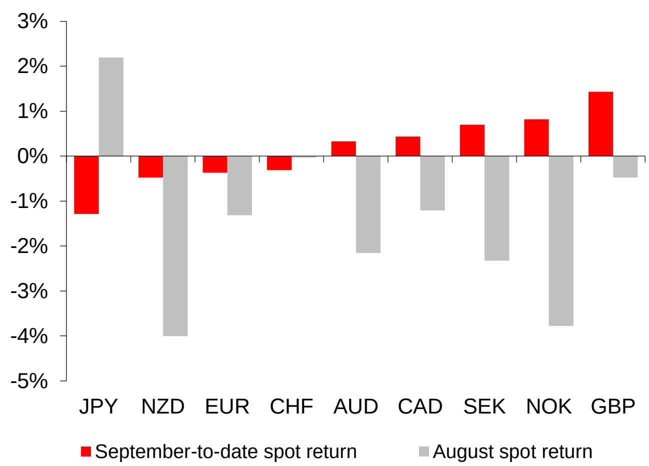
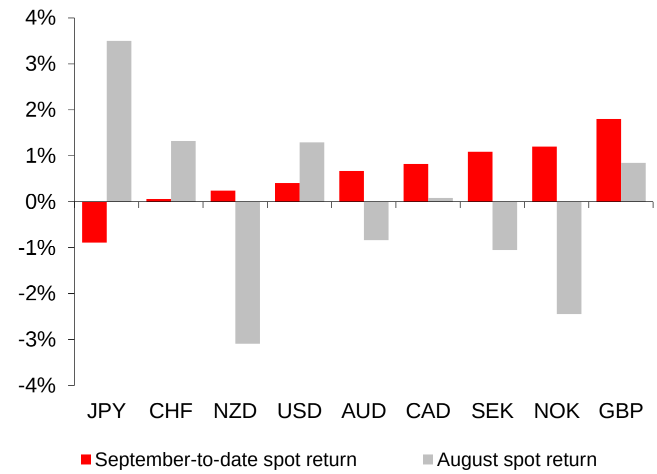
FX Spot Returns

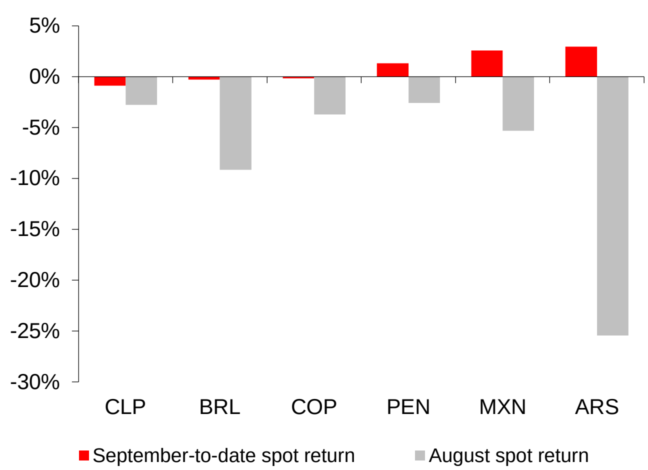
G10 spot returns vs. USD



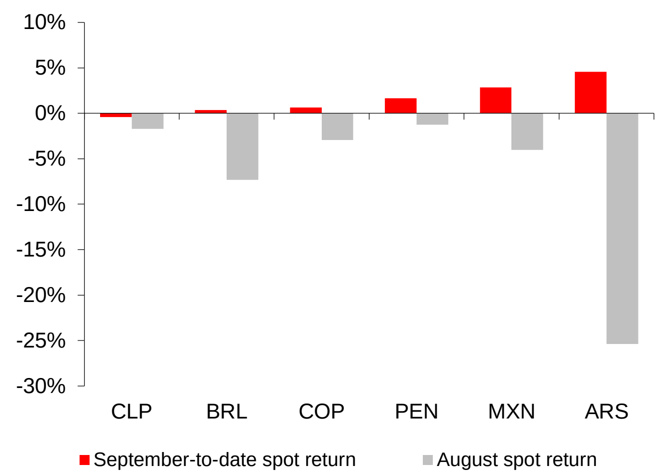
G10 spot returns vs. EUR



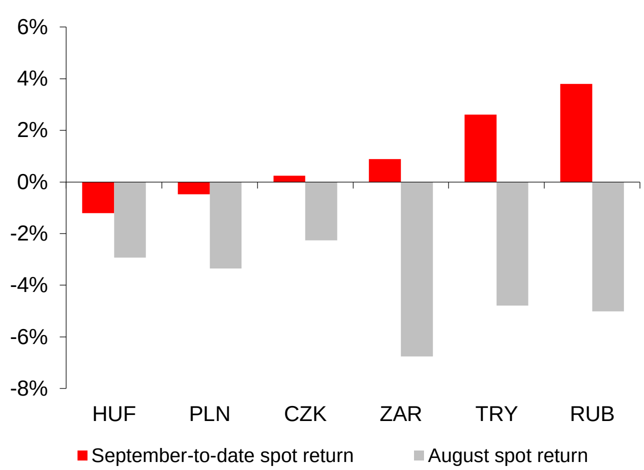
LatAm spot returns vs. USD



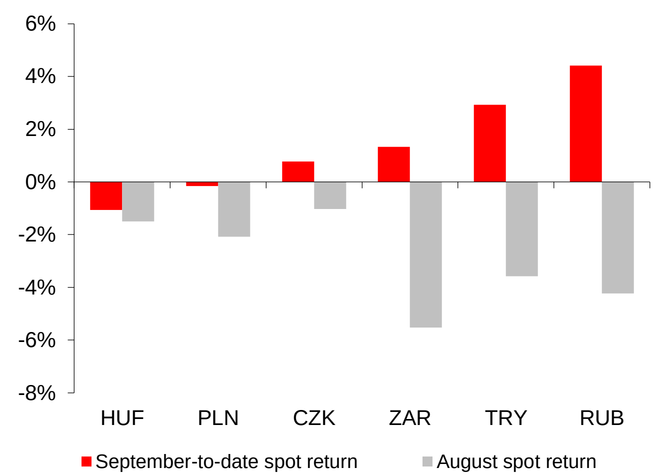
LatAm spot returns vs. EUR



CEEMA vs. USD



CEEMA vs. EUR



Source: Bloomberg, Santander. Note: Data current as at 26-September-19 at 10:00 BST

FX Forecasts

G10 FX Forecasts

	Q4-19	Q1-20	Q2-20	Q3-20	Q4-20	Q1-21
EUR-USD	1.14	1.14	1.15	1.16	1.18	1.18
GBP-USD	1.28	1.26	1.26	1.27	1.28	1.32
GBP-EUR	1.12	1.11	1.10	1.09	1.08	1.12
EUR-GBP	0.89	0.90	0.91	0.91	0.92	0.89
USD-JPY	106	106	103	106	109	112
EUR-JPY	121	121	118	123	129	132
USD-CNY	7.00	6.90	6.80	6.80	6.60	6.60
EUR-CHF	1.11	1.12	1.13	1.13	1.15	1.15
USD-CHF	0.97	0.98	0.98	0.97	0.97	0.97
EUR-SEK	10.6	10.6	10.5	10.4	10.3	10.2
EUR-NOK	9.8	9.7	9.7	9.6	9.6	9.5
USD-CAD	1.29	1.28	1.27	1.25	1.25	1.25
AUD-USD	0.70	0.70	0.71	0.72	0.72	0.73
NZD-USD	0.67	0.68	0.68	0.69	0.69	0.70

LatAm FX Forecasts

	Q4-19	Q1-20	Q2-20	Q3-20	Q4-20	Q1-21
USD-BRL	4.0	3.9	3.9	4.0	4.0	4.0
USD-MXN	19.8	19.8	20.1	20.3	20.5	20.6
USD-CLP	715	705	700	705	715	705
USD-ARS	67	72	76	82	87	91
EUR-BRL	4.6	4.4	4.5	4.6	4.7	4.7
EUR-MXN	22.6	22.6	23.1	23.5	24.2	24.3
EUR-CLP	815	804	805	818	844	832
EUR-ARS	76	82	88	95	103	107

CEE FX Forecasts

	Q4-19	Q1-20	Q2-20	Q3-20	Q4-20	Q1-21
EUR-PLN	4.30	4.30	4.30	4.30	4.30	4.25
EUR-CZK	25.6	25.4	25.2	24.9	25.0	25.0
EUR-HUF	340	340	345	345	350	350
USD-RUB	65	67	70	70	70	70
EUR-RUB	74	76	81	81	83	83

Sources: Santander

G10 FX: Main Themes

Currency	3M view	12M view	Main Themes
USD	⇨	↘	• 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	⇨	↗	• The ECB remains dovish, but we expect no more easing measures. The negative impact on EUR/USD from lower ECB rates may now be countered by more US rate cuts and/or improving risk appetite.
GBP	↗	↗	• Sterling remains vulnerable to political uncertainty. However, we do not expect a no-deal Brexit at the end of October, which should favour a sterling pick-up in Q4-19, but election uncertainty should cap the upside..
JPY	⇨	↘	• Low risk appetite has boosted the yen and downside pressure on the currency from a loose BoJ policy is now being countered by dovish policies elsewhere.
CNY	⇨	↘	• US-China trade tensions have eased slightly. But the CNY remains soft as further domestic stimulus measures should keep the yuan under pressure, despite the US rate cut in September.
CHF	⇨	↘	• Low global risk appetite has boosted the franc. However, the CHF should eventually weaken, while the SNB should maintain a loose policy into 2021 and remain willing to intervene.
CAD	⇨	↗	• We see scope for some CAD appreciation. The BoC is less dovish, oil prices are robust, Canadian economic data are improving and a dovish Fed should help the CAD against the USD.
AUD	⇨	↗	• 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 in 2019.
NZD	⇨	↗	• The RBNZ kept rates on hold in September, but despite cutting by 100bp over the past year, a further cut is likely in November. Together with elevated global trade fears, this is likely to continue to restrict the NZD.
SEK	⇨	↗	• Domestic data have deteriorated and with CPIF back below target, the Riksbank should find it increasingly difficult to justify a 2019 rate hike. With global trade fears elevated, a SEK recovery is unlikely just yet.
NOK	⇨	↗	• An apparent end to the Norges Bank's tightening cycle removes the main argument for a stronger NOK. With the Bank now foreseeably on hold, the NOK is likely to pay more attention to global risk sentiment and oil prices.

⬆ Bullish ↗ Mildly Bullish ⇨ Neutral ↘ Mildly Bearish ⬇ Bearish

Source: Santander

G10 FX Overview

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The USD looks set to remain firm, despite Fed rate cuts and signs of reduced US-China trade tensions. Further, the currency remains stronger than it probably should be as its peers look to be facing strong economic headwinds, with many other central banks also adopting a more cautious line.

The euro is expected to remain vulnerable. The ECB cut rates and its economic forecasts in September, but the negative impact on the euro was less than expected. Much of the soft economic news should already be in the price. Further, we do not expect more easing from the ECB, suggesting that additional US rate cuts in Q4 could allow EUR/USD to return to 1.14 levels by the end of the year.

We suspect that the pound can hold on to its recent gains, but political/Brexit uncertainty still suggests limited appetite to pull the currency significantly higher. However, with speculators still notably net short GBP/USD, there is scope for ‘good’ news to prompt a short squeeze and boost the pound.

The yen has reversed some of its recent gains over the past month. The JPY is perceived as a safe-haven currency and, as such, tends to be in demand at times of low global risk appetite. Hence, US-China trade tensions and concerns about global growth boosted the yen.

The CNY remains soft against the US dollar, but is off of the lows set earlier in the month. An apparent easing of trade tensions between the US and China has helped alleviate some pressure on the renminbi.

We continue to expect the CHF to weaken, but any reversal of its recent gains is likely to be laboured and gradual. The Swiss economy is stuttering and inflation is expected to remain low. Hence, the SNB may have to ease policy further, although as long as risk appetite remains low and other central banks are cutting rates, policymakers may simply have to put up with a strong franc for the foreseeable future.

We retain a positive CAD view. Domestic economic data have outperformed, inflation is back at target, expectations for BoC rate cuts have fallen, whilst further US rate cuts are anticipated, the oil price has firmed and the US-China trade rhetoric has taken on a more friendly/constructive tone.

The AUD and NZD are both still under pressure. Weak domestic data and the likelihood of more rate cuts are still risks for both currencies, as is a further downturn in global risk sentiment. However, the AUD and NZD are much weaker in 2019, and with the net short speculative AUD large, and the NZD position at an all-time high, there should be less scope to sell these currencies further.

We are no longer bullish on the NOK. Domestic data remain solid, but not quite as upbeat as before. The Norges Bank has hiked rates by 100bp over the past year, but no longer expects to raise rates any further in the months ahead. At the same time, risk sentiment has restricted the NOK and unless global confidence picks up, the market is likely to continue to shy away from buying the currency.

We are still neutral the SEK in the short term, but more cautious in the months ahead, as softer domestic data and weaker global risk sentiment are making it more difficult for the Riksbank to maintain its hawkish rhetoric.

USD – Mirror, mirror on the wall…

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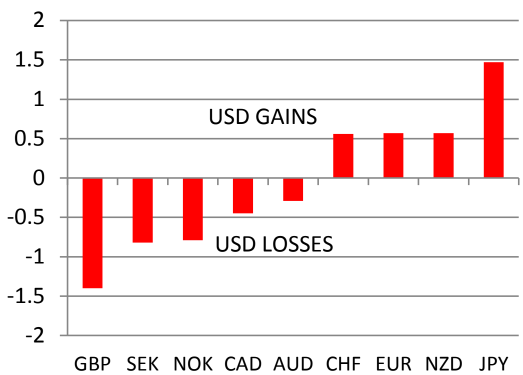
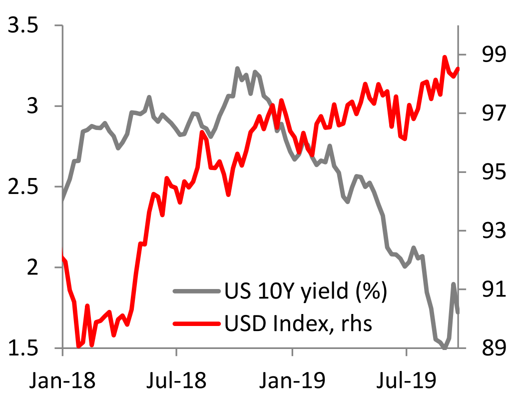
Chart 1: USD carry-adjusted performance against its developed market peers September month to date* – dollar softens a bit…



Source: Bloomberg, Santander *As of 26 September

Chart 2: …but USD still firm as rates are cut, as USD yields still outpace its peers



Source: Bloomberg, Santander

The USD looks set to remain firm, despite Fed rate cuts and signs of reduced US-China trade tensions. Indeed, we argue below that the prospect of a trade deal with China may be ambiguous for the dollar. Further, the currency remains stronger than it probably should be as its peers look to be facing strong economic headwinds, with many other central banks also adopting a more cautious line.

US-China trade tensions have remained a key driver for the dollar and the FX market in general. Relations between the two countries appear to have improved over the last month, with trade talks resuming. The threat of a trade war has undermined risk appetite for much of 2019 and boosted demand for the USD as the market perceives it to be a safe-haven currency. Consequently, if relations between the US and China improve, risk appetite should recover and the dollar should weaken.

However, the impact on the USD from a better trade/growth outlook may be less clear. The FOMC cut US rates in September, partly as a response to concern about global developments. Thus, if the global economy improves there may be less pressure on the Fed to make additional, dollar-negative, rate cuts. Indeed, even though the FOMC was split on whether to cut rates, and by how much, in September, its dot plots and projections now highlight a median scenario with no further cuts, and rates rising in 2021.

Admittedly, the market is not completely convinced and still sees a greater than 50% chance of a rate cut at the FOMC's October meeting. Consequently, the potential for additional rate cuts should still be a dollar negative over the next couple of months.

USD bulls are still able to point to the relative outperformance of the US economy against its peers as a reason to be positive. The consensus expects US growth of 1.8% in 2020, compared to 2.5% in 2019. Although we would emphasise that this implies that the US will outgrow Europe, Japan etc., it does suggest a narrowing of the US's growth premium over its developed market peers.

Further, despite the Fed cutting the Fed Funds target range to 1.75-2.00%, US yields are still more attractive than those offered by its G10 peers. However, again we would highlight that despite this absolute interest rate advantage, the change in yield differentials has not been dollar-positive in 2019.

We still feel that there are sufficient reasons to question whether the dollar will, or should, appreciate more. But the FX market remains reluctant to end its love affair with the greenback, which has now been ongoing since April 2018. However, the currency's recent resilience may have as much to do with the unattractiveness of the alternatives, rather than appetite to boost long USD positions.

Whilst the yen has been supported by low risk appetite, the pound has softened against the dollar owing to Brexit concerns, although September has been a good month for GBP/USD. Moreover, the euro has remained under pressure amid concerns over German economic growth, politics and ECB easing. However, given the comprehensive package of easing announced by the ECB in September, we no longer expect additional rate cuts, which should provide support for euro sentiment and allow the dollar to weaken if, as we and the market expect, the Fed cuts rates again in Q4-19.

EUR – That's all folks

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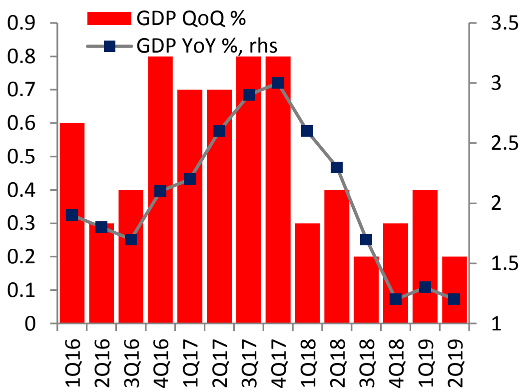
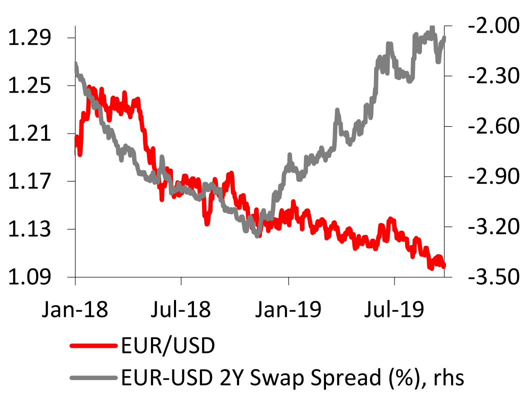
Chart 3: Soft Eurozone fundamentals continue to weigh on the euro…



Source: Bloomberg, Santander

Chart 4: …but EUR/USD still looks on the cheap side given interest rate differentials*



Source: Bloomberg, Santander *As at 24 September 2019

The euro is expected to remain vulnerable. The ECB cut rates and its economic forecasts in September, but the negative impact on the euro was less than expected. Much of the soft economic news should already be in the price. Further, we do not expect more easing from the ECB, suggesting that additional US rate cuts in Q4 could allow EUR/USD to return to 1.14 levels by the end of the year.

The ECB eased monetary policy at its September meeting. The deposit rate was cut 10bp to -0.5% and the asset purchase programme was restarted, with EUR20bn/month. The headline changes were slightly less than the consensus expected, but the detail was dovish: the asset purchase programme is open-ended, continuing for as long as necessary, rather than for a fixed period.

Further, interest rates are now expected to remain at the current level, or lower, until the CPI outlook 'robustly converges' to close to, but below, 2%. Previously, rates were on hold through to the end of H1-20. Despite the policy changes and Draghi's warning that the risks were still tilted to the downside, the euro did not crash. This might suggest that overall the effect of the September move was already priced in. It may also imply that interest rate cuts are having less effect on the currency.

Sentiment was also helped by the announcement of deposit tiering, implying that as much as EUR800bn of banks' reserves would be exempt from the negative deposit rate. This boosted bank shares and general sentiment and also helped the euro.

In addition to the easing, the ECB staff forecasts were revised down. The GDP growth forecast for 2019 and 2020 was cut to 1.1% and 1.2%, from 1.2% and 1.4%, respectively, with 2021 unchanged at 1.4%. The inflation forecasts were also cut, with the 2020 outlook reduced to 1% and 2021 lowered 0.1pp to 1.4%.

The revisions justify the September easing, but with the CPI forecast now very low, there may be less scope for further downward revisions to justify further cuts. Indeed, given the comprehensive package of easing announced by the ECB in September, we no longer expect additional rate cuts, with, as Draghi hinted at, greater focus being put on fiscal policy to support growth. This should be a euro positive, particularly as we still expect the Fed to cut in Q4.

We still suspect that a lot of the bad economic news has already been priced in and there would have to be a greater deterioration in the economic outlook in order for the euro to weaken further. Admittedly, the ongoing threat that the US administration could increase tariffs on Eurozone imports might provide such a shock, but as has been seen with US-China trade tensions, this might also affect the US economy, and force the Fed to cut US rates further.

Nevertheless, market participants generally remain USD-positive and are likely to highlight that in absolute terms USD yields will remain well above Europe's. That said, lower US yields in 2019 have implied that rate differentials are far less USD supportive.

Indeed, looking at EUR/USD versus EU-US 2Y and 10Y spreads, the pair has diverged from the spread. Perhaps this justifies the view that absolute rates are driving the market, but it might also imply that EUR/USD is simply undervalued given rate spreads, and at the very least may have priced in ECB easing, but less so Fed easing.

GBP – Off of the lows

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We suspect that the pound can hold on to its recent gains, but political/Brexit uncertainty still suggests limited appetite to pull the currency significantly higher. However, with speculators still notably net short GBP/USD, there is scope for 'good' news to prompt a short squeeze and boost the pound.

The pound has had a strong September, with sterling rebounding from its recent lows against the euro and US dollar. Month-to-date, the pound has been the best performing developed market currency. However, overall the currency remains weak and its impressive performance in September is partly a response to the big sell-off it suffered between late July and the start of this month.

The catalyst for the GBP's summer drop was the market's concern that the new PM, Johnson, was prepared to sanction a no-deal Brexit. The turnaround came after the UK parliament passed a law forcing the PM to ask for an extension to the Article 50 process if a deal has not been agreed by 19 October. It remains uncertain whether the PM will ask for that extension, but the legislation has seemingly reduced the threat of no deal, at least at end-October.

Sterling was also boosted by the UK Supreme Court's decision on 24 September that PM Johnson's prorogation (suspension) of parliament was not lawful. The FX market seemed to view this as making a no-deal Brexit on 31 October even more unlikely.

UK politics and Brexit are set to remain the key GBP drivers over the coming month. Given that PM Johnson no longer has a parliamentary majority, an early election looks very likely, probably by the end of November. Sterling thus faces a mixture of political scenarios through to the end of October. First, PM Johnson might get a deal agreed by the end of October. There may not be sufficient time for this to be achieved, but we think a deal would be viewed positively by the FX market, at least in the short term, and allow GBP/USD to move back to 1.30 and EUR/GBP to 0.8600.

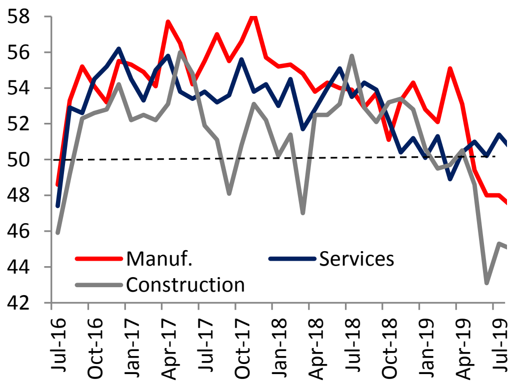
Second, if a deal is not agreed, the PM has to ask for an extension. This would probably be neutral for the pound, at first, and may be what the market has priced in since early September. However, it might then be viewed as harming Johnson and his Conservative party's chances in a forthcoming election, increasing the probability of a change in government and/or a hung parliament, and this would probably be negative for the pound.

UK economic data and BoE rates have been less of a focus for the pound. However, whilst the PMI surveys have remained weak, with the manufacturing and service indices below 50, the August GDP print was better than expected and, at 0.3% MoM, suggests that the economy may have escaped falling into recession.

Further, some of the soft UK data is due to global growth/trade worries, rather than purely UK focussed. Such global concerns are not directly supporting the pound, but indirectly may be providing support for GBP crosses by increasing downside pressure on the euro and to a lesser extent the dollar.

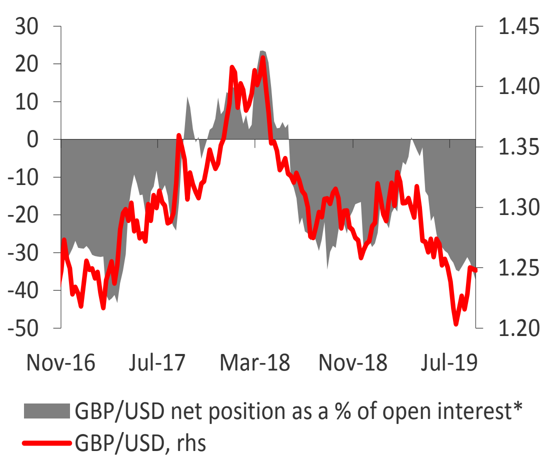
As expected, the BoE kept policy unchanged in September. The Bank continues to see a need for gradual and limited rate hikes, if there is a 'smooth' Brexit. However, it also raised the issue of 'ongoing uncertainty' undermining the outlook, with the risk that it would keep growth below its long-term potential.

Chart 5: UK PMIs remain soft and sterling negative



Source: Bloomberg, Santander

Chart 6: Speculators remain very net short GBP/USD



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

JPY – Holding off

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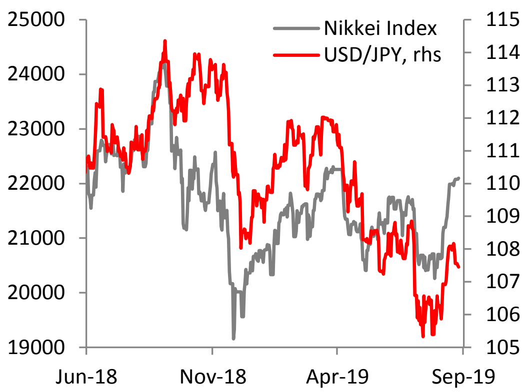
The yen has reversed some of its recent gains over the past month. The JPY is perceived as a safe-haven currency and, as such, tends to be in demand at times of low global risk appetite. Hence, US-China trade tensions and concerns about global growth boosted the yen.

These flows have reversed somewhat in recent weeks. The mood music between the US and Chinese has improved, suggesting that a trade deal by the end of the year may still be possible. Further, the announcement that the US had agreed an initial trade accord with Japan also helped risk appetite. Consequently, Japanese equities, a proxy for risk, have rallied in September. Indeed, the yen may still be slightly on the expensive side given the current level of the Nikkei. In addition, the IMM data on the commitment of traders show that speculators, amid low risk appetite, have gone long the yen since the start of August. If the better risk backdrop/firm equity markets continue, these bets are likely to be unwound, which could further weaken the currency.

Chart 7: A pick up in risk appetite/equities has helped USD/JPY in September

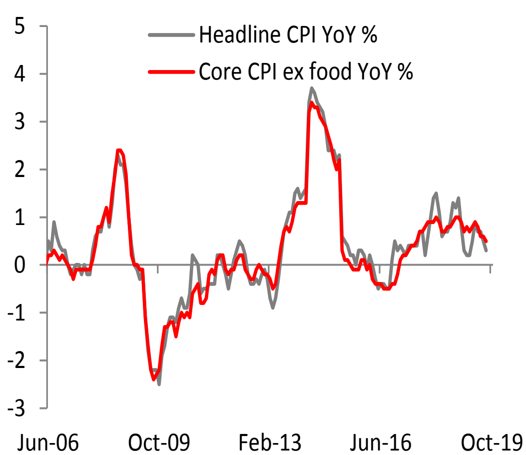


Source: Bloomberg, Santander

However, whilst risk, in our opinion, has been the main driver of the yen recently, a switch in focus toward the BoJ and Japan's economic outlook might prevent it from completely reversing those gains in the months ahead. The BoJ kept its monetary policy unchanged at its meeting in September. The deposit rate was left at -0.1%, the target for JGB yields remains around zero and maximum asset purchases stay at JPY80tn a year. However, Governor Kuroda, who had previously warned that he would not hesitate to ease further if momentum towards 2% inflation was being lost, said that he was now more inclined towards easing than at the previous meeting.

Consequently, the market is pricing in a slightly better chance of a reduction in the depo rate at the 31 October meeting, although it remains broadly 50:50. The October meeting will include revised forecasts for activity and prices, and any downward revision may provide a useful hook on which to hang further easing.

Chart 8: Low inflation should keep the pressure on the BoJ to stay loose



Source: Bloomberg, Santander

However, we continue to highlight that, similar to the SNB, we remain doubtful that another rate cut will significantly weaken the yen and that with the BoJ's balance sheet standing at more than 100% of GDP, it has less room to boost asset purchases. Plus, deeper negative rates could impact the financial sector, general economic confidence and paradoxically inflationary/demand pressures.

Further, note that on 1 October, Japan will hike its sales tax from 8% to 10%. Kuroda stated that he does not see this hike having a 'big impact' on the economy. But previous tax rises have adversely affected the economy. The sales tax will imply a rise in headline CPI, and it is low inflation, as much as growth, that remains a concern for the BoJ. The headline CPI rate in August surprised to the downside, at just 0.3% YoY, and the core rate, excluding fresh food, was just 0.5% YoY, the lowest for two years.

The combination of sluggish wages and a strong yen makes it difficult to sustainably pull CPI higher. The recent pick-up in the yen, and signals from the Fed that further US rate cuts are not guaranteed, has given some wriggle room to the BoJ, by reducing downside pressure on US-Japan 10Y yields and USD/JPY. In our opinion, this highlights that the BoJ has less control over the yen than it would like and yen weakness still depends on better risk appetite and a generally stronger USD and other G10 currencies.

CNY – Prudent easing

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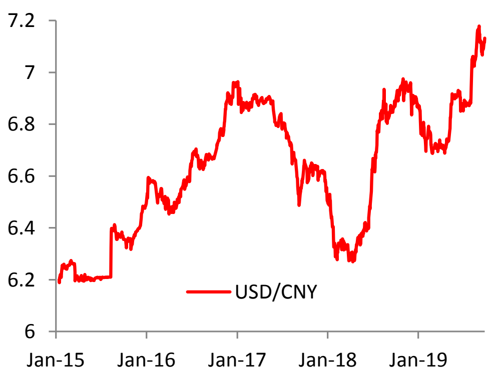
Chart 9: USD/CNY holding above 7



Source: Bloomberg, Santander

Chart 10: Policymakers seem to favour prudent easing in the face of economic headwinds

Source: Bloomberg, Santander

The CNY remains soft against the US dollar, but is off of the lows set earlier in the month. An apparent easing of trade tensions between the US and China has helped alleviate some of the pressure on the renminbi. However, concern about the pace of Chinese economic growth remains, suggesting that policymakers will adopt further easing measures. However, the impact on USD/CNY may be countered by further US rate cuts.

The tensions between the US and China with regard to trade seem to have eased slightly over the last month. China indicated that it is now encouraging firms to buy US agricultural products and gave other waivers to companies to purchase US soybeans without being subject to retaliatory tariffs.

The improved sentiment and risk appetite, at least for now, have reduced demand for the dollar, which is perceived as a safe-haven currency, and allowed USD/CNY to slip off of its September highs. However, the outlook for the Chinese economy remains vulnerable and may keep the CNY under pressure. The consensus, according to Bloomberg, still expects GDP growth in 2020 at 6%, but many analysts now suspect that growth might dip below that key level.

Indeed, recent data have remained on the soft side. Industrial production in August grew by just 4.4% YoY, the slowest rate of growth since 2002. Further, retail sales were softer than expected, growing 7.5% YoY in August. Weaker than expected Chinese trade data reflected still subdued manufacturing confidence. The Chinese trade surplus dropped to USD34.84bn in June, compared to expectations for USD44.30bn and USD44.58bn in July. In US dollar terms, exports contracted 1% YoY, with import growth contracting 5.6% YoY.

Further, whilst Chinese CPI remained relatively high at 2.8% YoY in August, PPI data fell further into deflationary territory. The producer price index tends to be viewed as an indicator for industrial profits and contracted 0.8% YoY in August, compared to -0.3% YoY in July, highlighting the vulnerability of the economic outlook.

Policymakers have responded to these economic risks with further easing, but many market participants feel that more should be done. Hence, China's cautious approach to easing is also providing some support for the CNY.

For example, earlier this month the PBoC again cut banks' reserve requirements. The central bank said that the RRR for all banks will be lowered by 0.5 percentage points. It also cut the reserve ratio by one percentage point for some regional banks, to take effect in two stages, on 15 October and 15 November. The cuts will release 900 billion yuan of liquidity, the central bank said.

But it did not follow the Fed when it cut US rates in September. Indeed, the Loan Prime Rate stood at 4.2% in September, just a little lower than August's 4.25%. Admittedly, policymakers have already put in place other stimulus measures, including tax cuts earlier in the year and boosted infrastructure spending. But the PBoC's governor highlighted that a prudent policy stance is likely to be maintained. We suspect that this will imply gradual and targeted easing measures, which might not please the market but should prevent the CNY from weakening significantly and help relations with the US.

CHF – Low inflation adds to SNB woes

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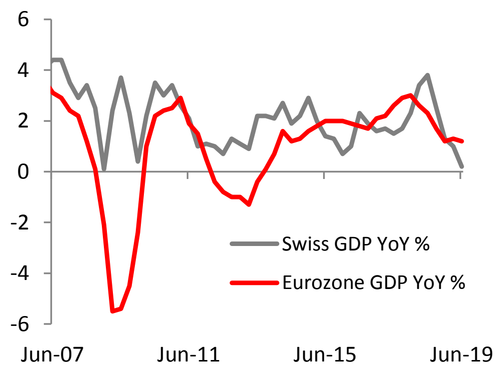
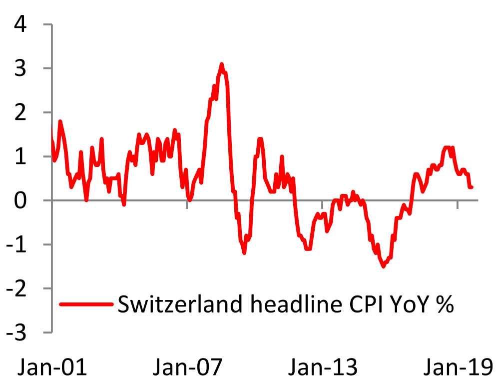
Chart 11: Slower growth to keep pressure on the SNB



Source: Bloomberg, Santander

Chart 12: Swiss inflation expected to stay lower for longer



Source: Bloomberg, Santander

We continue to expect the CHF to weaken, but any reversal of its recent gains is likely to be laboured and gradual. The Swiss economy is stuttering and inflation is expected to remain low. Hence, the SNB may have to ease policy further, although as long as risk appetite remains low and other central banks are cutting rates, policymakers may simply have to put up with a strong franc for the foreseeable future.

Traditionally, the market has perceived the Swiss franc as a 'safe-haven' asset. The introduction of very negative Swiss interest rates did undermine the currency's attractiveness as a haven, but recently we believe it has again benefited from safety flows amid concerns about global growth. Consequently, EUR/CHF hit a low at 1.0812 on 5 September. However, the cross has since bounced off of these lows. The mini-recovery probably owed something to an improved outlook for US-China trade talks; note that the yen also weakened.

But we think that the general pick-up in the euro was key. This suggests that the SNB will remain a price-taker as far as EUR/CHF is concerned, relying on a stronger euro to pull EUR/CHF, but it also suggests that the 1.08 level should offer some support, or it could be a level that the SNB might defend.

Despite the ECB's decision to cut its deposit rate by 10bp to -0.5% on 12 September, the SNB kept monetary policy unchanged in September. Hence, the policy rate remains at -0.75%. The Bank reiterated that it believes that the CHF is 'highly valued' and warned that it remains willing to intervene to weaken it.

We remain doubtful of the scope for further SNB easing and are sceptical about its ability to weaken the CHF. However, the Bank did make some forecast and policy changes that suggest that the door to some form of extra action is still open.

First, the SNB made substantial downward revisions to its growth and inflation forecasts. The economy is expected to grow by just 0.5-1% in 2019, compared to the 1.5% expected in June. Further, CPI forecasts were slashed: 2019's was cut to 0.4% from 0.6%, 2020 to 0.2% from 0.7% and 2021's to 0.6% from 1.1%. For context, CPI is not expected to rise above 1% until Q2-22.

Second, the SNB provided some relief for banks from the impact of negative rates. From November it will adjust the basis for calculating negative rates on sight deposits at the central bank. Reducing the burden of negative interest rates on banks, akin to the ECB's tiering, should help the financial sector, but it also make it easier/less damaging for the SNB to cut its policy rate even further.

However, given that the SNB already has the most negative policy rate among the developed markets, which has failed to prevent the CHF from strengthening, we remain doubtful that simply a more negative rate will weaken the CHF, but it might, at least, prevent the currency from appreciating even further.

An alternative way to make the CHF less attractive, which is attracting more attention, is for Swiss banks to charge clients to hold deposits. Some banks have already been charging for euro accounts, partly to lessen the impact on them of negative Swiss rates. Some institutions have announced plans to impose charges on CHF accounts. To start with, the focus is on wealthy clients.

CAD – Standing out from the crowd

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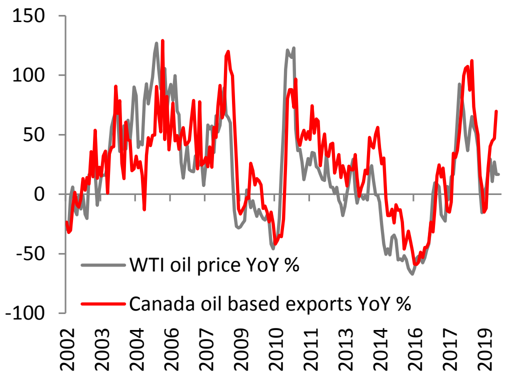
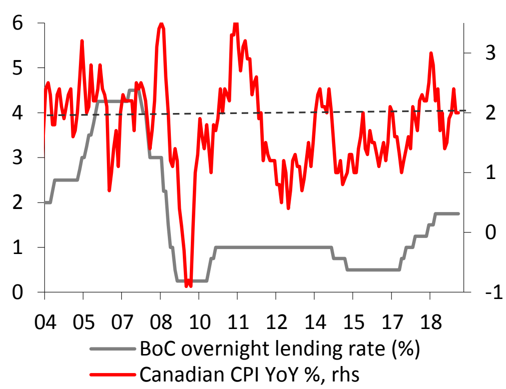
Chart 13: Robust Canadian economic data provides the BoC with room for manoeuvre…



Source: Bloomberg, Santander

Chart 14: …as does solid inflation numbers



Source: Bloomberg, Santander

We retain a positive CAD view. Domestic economic data have outperformed, inflation is back at target, expectations for BoC rate cuts have fallen, whilst further US rate cuts are anticipated, the oil price has firmed and the US-China trade rhetoric has taken on a more friendly/constructive tone. If the FX market maintains its fondness for the US dollar, USD/CAD may decline only slowly, but the CAD should outperform its other developed market peers.

The Bank of Canada kept the overnight rate unchanged at 1.75% in September. Many market participants assumed that, given global trade tensions, the Bank would copy other central banks and, if not cut rates, at least adopt a much more dovish stance. Instead, the BoC took a much more upbeat stance, albeit still conceding that global pressures remained a risk.

Consequently, expectations with regard to interest rate changes have moved in the CAD's favour. Before the September meeting, the market was assuming that a rate cut in H1-20 was all but certain, but following the meeting, this was cut to a less than 50% chance.

The BoC has room for manoeuvre because, despite global risks, the domestic backdrop remains positive. Q2-19 GDP surprised significantly to the upside. The economy grew 3.7% QoQ annualised in Q2, compared to the BoC's forecast for 2.3% and Q1's 0.5%. Activity may slow in H2, but the strong H1 could allow for a small upward revision to 2019 GDP from the current 1.3% forecast.

In addition, inflation remains around the Bank's central target of 2%, and also points to an upward revision to the BoC's 1.6% forecast for Q3-19. Further, unemployment data was better than expected in August, with the unemployment rate staying at 5.7%, close to its all-time low, and wage growth remaining firm.

Consequently, policymakers view the domestic economy as running close to full capacity, implying sustained pressure on inflation. Admittedly, the Bank did flag global trade tensions as a significant risk to Canada. However, the recent improvement, in our opinion, of the rhetoric between the US and China should contain these fears, and help Canada's export outlook and CAD sentiment.

Moreover, with the BoC 'on hold', monetary policy differentials should also support the CAD if, as expected, other central banks remain dovish. The Fed cut US interest rates in September, and we think it will cut again by the end of the year. Traditionally, there has been a strong correlation between BoC rates and the Fed, but this time, it does not look like the BoC will simply copy US cuts.

Indeed, as Deputy Governor Schembri noted, lower global yields have pulled down Canada's borrowing costs/mortgage rates, helping the housing market, despite the less dovish BoC. The BoC can thus piggyback on the US/global decline in yields, taking the benefit, whilst setting the overnight rate to suit the domestic economy.

Aside from the BoC, the firmer oil price, following the disruption to Saudi Arabia's production, should provide some support for the CAD. However, note that federal elections will be held on 21 October. Current opinion polls show the Conservative party neck and neck with PM Trudeau's Liberal party, suggesting that the prospect of a close election and/or change of government may temper CAD bulls.

AUD – A gentle turning point?

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We are relatively neutral the AUD, but there are still risks to the downside. Domestic data are weak, and the RBA is under pressure to continue easing monetary policy. Global risk sentiment continues to weigh on the AUD, although any progress on trade between the US and China in early October has the potential to boost global risk sentiment and the AUD. We continue to see AUD/USD at 0.70 at year-end, although the pair is likely to lag below this level in October.

Australian data remain soft, with GDP falling again in Q2-19. Quarterly growth managed to hold at 0.5%, but the annual rate fell to just 1.4%, its lowest rate in a decade, and just its fourth time below 1.5% since the early 1990s (Chart 16).

RBA Governor Lowe has suggested that Australia's economy has reached a gentle turning point, and he expects to see a modest pick-up in GDP in the coming quarters. Given the particularly weak second half of 2018, base effects alone should ensure annual growth rises in the second half of this year. The next GDP print is not released until December.

As well as the weak GDP numbers, unemployment has ticked up in recent months, rising from 4.9% in February to 5.3% currently, and jeopardising the RBA's "full-employment" target. Similarly, while the annual CPI print rose to 1.6% in Q2-19, this is the fourth consecutive month below the RBA's 2-3% target range.

Given the above, the dovish stance held by the RBA is more than understandable. The Bank has highlighted that an extended period of low rates is likely needed, while accepting that further monetary easing may well be required.

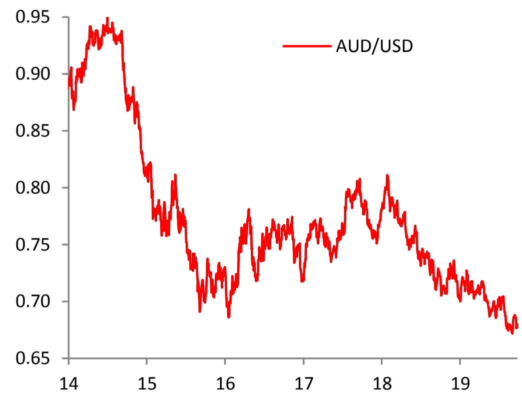
After consecutive 25bp cuts in June and July, the RBA kept rates on hold in August and September. However, the Bank is likely to cut rates again, in our view, and the market is now speculating on a rate cut coming in early October. Indeed, the futures market is pricing in a 75% chance of such a cut.

The Bank may yet opt to wait until November, but we see a rate cut over the next two meetings as very likely, and also expect a further cut by February. Indeed, the past month has seen both the FOMC and ECB cut rates, and the RBA's governor has suggested that if the Bank ignored this shift towards looser policy by developed market central banks, then "our exchange rate would appreciate, which, in the current environment, would be unhelpful in terms of achieving both the inflation target and full employment".

With the cash rate at 1.00% currently, there is not much scope for the Bank to ease further without using extraordinary measures. The RBA has already said that it would consider quantitative easing, but has suggested that it is unlikely.

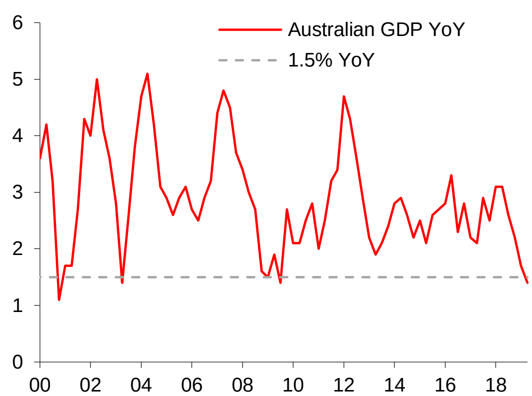
In fact, with Governor Lowe noting that monetary policy has become less effective at the margin, the Bank may decide to take a longer break when normal rate cuts are exhausted, before deciding that there is no other solution than extraordinary easing measure.

Chart 15: The AUD has weakened on a decline in global risk sentiment and a lower RBA cash rate



Source: Bloomberg, Santander

Chart 16: Australian growth is historically weak, coming in below 1.5% YoY in Q2-19 for only the fourth time since the early 1990s



Source: Bloomberg, Santander

NZD – A short break

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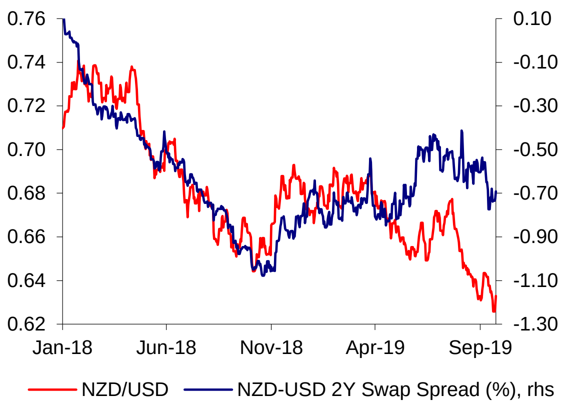
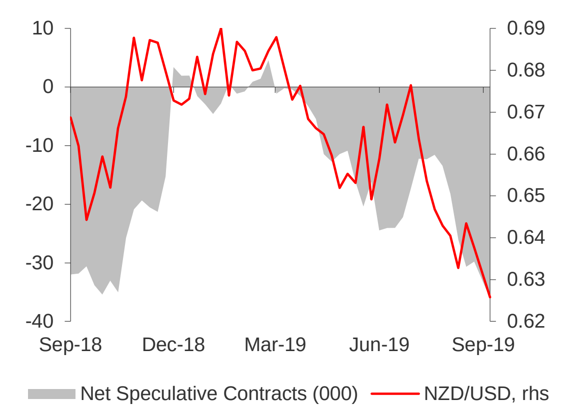
Chart 17: NZD/USD has slipped to a four-year low in late September



Source: Bloomberg, Santander

Chart 18: Speculators now hold their largest net-short NZD position in 16 years of data



Source: CFTC, Bloomberg, Santander

The NZD is still under pressure. Weak domestic data and the likelihood of more rate cuts are still risks for the currency, as is a further downturn in global risk sentiment. However, the NZD has already weakened notably over the past few months, with NZD/USD dropping to a four-year low in late September. In addition, with the net short speculative NZD position at an all-time high, there should be more limited scope to sell the currency further. Hence, we retain our 0.67 year-end forecast.

The NZD is the weakest performing G10 currency in Q3-19, and the second weakest G10 currency, after the SEK, so far in 2019. In addition, in recent weeks, speculators have turned increasingly negative on the NZD, with their net short position now at its highest level in 16 years of data, at 36k contracts. This should imply less scope for further NZD weakness.

However, while the market may be more restrained in its NZD selling in the months ahead, movement in NZD/USD perhaps depends more on the USD. Indeed, the latest triennial FX survey from the Bank of International Settlements, released on 18 September, showed that while the NZD is still the 10th most traded global currency, used in 2.1% of global FX trades, three-quarters of these comprise NZD/USD trades.

Hence, if the FOMC refrains from cutting rates in October and the USD stays strong, NZD/USD is likely to remain subdued, especially if the RBNZ cuts rate further in November, and possibly also in February. The next key support level for NZD/USD is the August 2015 low, of 0.6130.

The RBNZ kept rates on hold at an all-time low of 1.00% on Wednesday, 25 September, but noted that there is scope for more monetary easing if necessary. This unchanged decision was expected, as the RBNZ already surprised the market with a 50bp rate cut at its prior meeting, in August.

The RBNZ has suggested that lower inflation expectations were the main reason for August's rate cut, and that it was better to cut rates too much too soon, rather than too little too late, so as not to be behind the curve. The Bank thinks this "probably lowers the risk of having to resort to unorthodox tools" (something it would rather not do).

Hence, unless domestic data pick up soon, the Bank may not want to wait too long before acting further, if it is to retain its "the earlier the better" mentality.

A strong jobs print in Q2-19 did see the unemployment rate fall to below 4% (an 11-year low, and close to its "maximum sustainable level"). However, while headline inflation sits at 1.7%, this is still below the midpoint of the Bank's 1-3% target.

RBNZ Deputy Governor Bascand says the economy needs to exceed 3% annual GDP to boost inflation. It does not bode well, therefore, that the Q2-19 data showed annual growth falling to 2.1%, its lowest level in five years. The Bank forecasts stronger growth here on in, but if trade fears and geopolitical risks continue to weigh on the global economy, then New Zealand's GDP and CPI may continue to disappoint, which in turn should prompt even lower rates.

SEK – Strong finances but disappointing data

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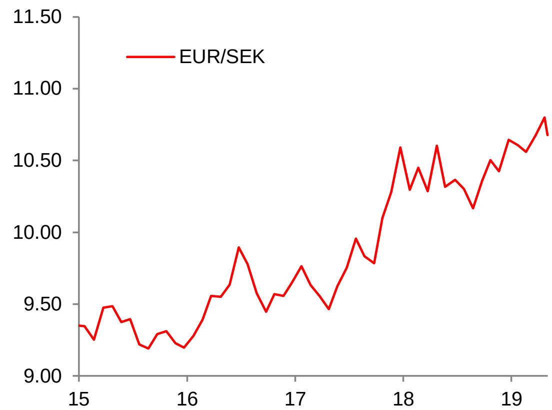
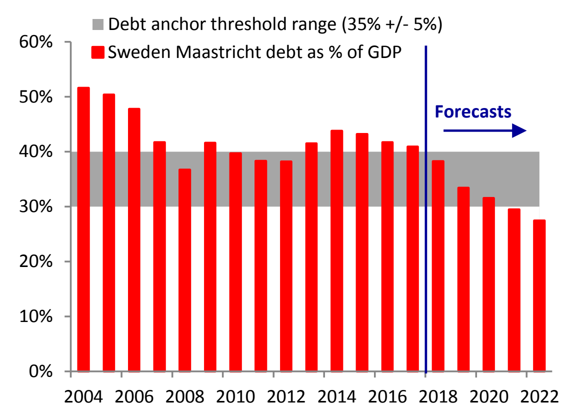
Chart 19: EUR/SEK has been moving on domestic events in September, but still sits close to 10.70



Source: Bloomberg, Santander

Chart 20: Sweden has strong finances, but the government is not yet ready to significantly boost spending until debt levels drop



Source: Bloomberg, Santander

We are still neutral the SEK in the short term, but more cautious in the months ahead, as softer domestic data and weaker global risk sentiment are making it more difficult for the Riksbank to maintain its hawkish rhetoric. We have lifted our EUR/SEK forecasts to 10.6 in Q4-19 (10.4 previously).

It has been a bad year for the SEK. The currency is still by far the worst performing G10 currency, and is still down by 9%, in spot terms, against the USD. EUR/SEK sits at 10.7 currently, and we continue to believe that there should be limited demand to pull the cross above this year's 10.8 highs.

The recent deterioration in economic data has limited the SEK's ability to strengthen. Indeed, in September, softer domestic figures, specifically the CPI and jobs numbers, have had a clear negative impact on the SEK.

The August CPI print certainly weighed on the SEK, as the Riksbank's targeted rate, the CPIF (CPI with a fixed interest rate), fell to just 1.3% (from 1.5%), its lowest level since 2016. Likewise, the August jobs data, released on 17 September, was also a big SEK negative. The unemployment rate was expected to decline, but jumped to 7.4%. This is the highest jobless rate since 2015, and shows a sharp rise over the past few months, from just 6% in April this year.

The latest Riksbank minutes were released at the same time, and showed that the Bank still supports hiking rates towards the end of this year, or at the start of next year. We still cannot see how the Riksbank can justify a 2019 rate hike, though, especially given the latest inflation and employment data.

While the Riksbank maintains a hawkish tone, domestic data have softened, global trade uncertainty has escalated, and other developed market banks have turned far more cautious, with the FOMC, ECB, RBA and RBNZ all cutting rates over the past couple of months.

The Riksbank's hawkish stance did give the SEK a boost on 5 September. However, when the Bank finally accepts that there is very little justification to tighten policy this year, it would be one support less for the SEK, and should keep EUR/SEK high.

There is plenty of international uncertainty, with the US-China trade war and Brexit fears, in particular, hurting trade. As a small open economy, Sweden has suffered from these global risks, and domestic data have clearly deteriorated. Indeed, there was almost no growth in Sweden in H1-19.

Government finances are remarkably good, although still not quite good enough by Swedish standards. The government is meeting its budget surplus target (0.33% of GDP for the 2019 fiscal year). However, while budget surpluses since 2015 have helped Swedish debt levels fall to 39% of GDP in 2018, this is still above the government target ratio of 35%.

In September, the Swedish government presented a mildly expansive budget to the Riksdag, with about SEK13bn in tax cuts. This was already expected, though, with the cuts mostly concessions to the government's coalition partners (Centre Party and the Liberals), formed in January after the inconclusive September 2018 elections.

NOK – Four hikes and they're out

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We are no longer bullish on the NOK. Domestic data remain solid, but not quite as upbeat as before. The Norges Bank has hiked rates by 100bp over the past year, but no longer expects to raise rates any further in the months ahead. At the same time, risk sentiment has restricted the NOK and unless global confidence picks up, the market is likely to continue to shy away from buying the currency. Consequently, we now forecast EUR/NOK at 9.8 by year-end (9.5 previously).

A year ago, the Norges Bank's deposit rate sat at an all-time low (0.50%), where it had been unchanged for the previous two years. Over the past twelve months, the Norges Bank has gradually lifted rates, hiking by 25bp in September 2018, March 2019, June 2019, and again in September 2019.

The Norges Bank is still more upbeat than most of its developed market peers, but its stance is now far more neutral than before. Indeed, while Governor Olsen highlighted in September that there is still a greater probability of rates going up than down, the Bank's forecasts are far more neutral, and see no more than a 40% chance of one further rate hike over its three-year forecast horizon.

Consequently, it looks like the Norges Bank's deposit rate is almost certain to stay at 1.50% for the remainder of 2019. If that is the case, and considering that the Norges Bank is the only G10 currency central bank to hike rates so far in 2019, it seems that there will be no more tightening of monetary policy in the G10 world until at least 2020, as we do not believe the Riksbank will manage to justify a hike in Q4-19.

One reason for a more cautious Norges Bank is the softer inflation data. Indeed, headline CPI fell to 1.6% in August (from 1.9%) while core CPI dropped to 2.1% (from 2.2%). These levels are nothing for the Bank to be concerned about, but inflation in Norway has been heading lower in 2019, thus removing a key support for the Bank's hawkish stance.

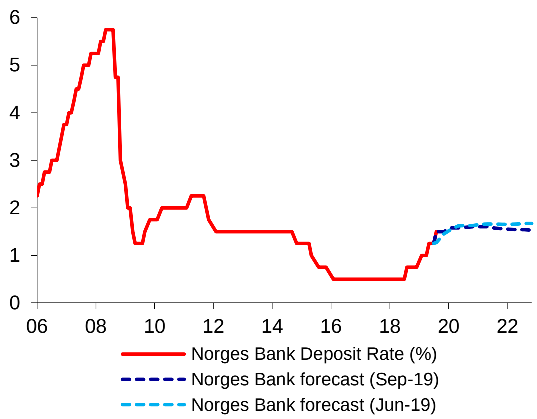
Q3-19 has been a tough quarter for the NOK. The currency has struggled along with those of other small open economies as global risk sentiment dipped, particularly due to US-China trade concerns and the looming Brexit deadline.

Indeed, the UK is Norway's largest trading partner, and so the risks of a no-deal Brexit are potentially an important negative for Norwegian exporters. Likewise, US-China tariffs have had an adverse effect on global trade, hurting other open trade-reliant economies, such as Norway's next largest trading partners, Sweden and Germany.

In addition, in September, geopolitical risks in Saudi Arabia and Iran caught the attention of the NOK. The currency initially strengthened as oil prices rallied after two attacks on Saudi Arabian facilities in mid-September cut output by 5.7mn bbl/day, reducing global supply by over 5%.

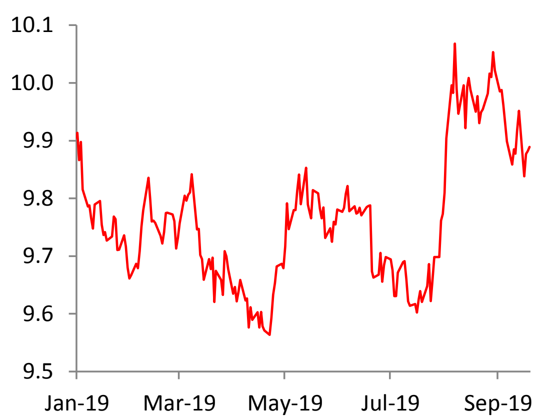
Brent and WTI crude prices rallied by 20%, and 15% respectively, before unwinding over half of this move as reports from Saudi Arabia suggested the lost output would be restored by the end of September.

Chart 21: The Norges Bank has hiked rates by 100bp over the past year, but shifted to a neutral stance in September



Source: Bloomberg, Santander

Chart 22: Despite these rate hikes, the NOK has been under pressure from global risk sentiment



Source: Bloomberg, Santander

LatAm FX: Main Themes

Currency	3M view	12M view	Main Themes
BRL	↗	↗	• Besides leading the base interest rate to a new historical low, the Brazilian monetary authority has signalled it may undertake further cuts. • For now, not even the knotty international scenario seems to be an obstacle for the Brazilian central bank to ease its monetary grip a little more. • Due to the favourable inflation dynamics and the low FX pass-through to domestic prices, we project the Selic target rate to end 2019 at 4.50% pa.
MXN	⇨	↘	• We expect the board of Banxico to cut the policy rate to 7.75% from the current 8.0% and to issue a dovish statement. • Our overall assessment of the 2020 budget is that it is austere and responsible. • In our view, the external scenario is still the number one threat to Mexican markets and to the MXN.
CLP	⇧	⇨	• The importance of the external scenario will remain a recurring theme for the 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 towards potential and a pick-up in emerging markets' growth would constitute the ideal scenario for the CLP.
ARS	⇨	↘	• The spot FX market is gradually consolidating, after the imposition of capital controls by the central bank. • The central bank's daily FX interventions have dropped to US$55 million per day this month. The average daily figure is 62% below the US$146 million recorded in August after the primaries. • We are projecting ARS67/USD by year-end, which reflects some upward adjustments in the current spot rate that are intended to capture the inflation erosion of September-November 2019.

⇧ Bullish ↗ Mildly Bullish ⇨ Neutral ↘ Mildly Bearish ⇩ Bearish

Source: Santander.

BRL – Other *jabuticaba*

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In Brazil there is a popular fruit called *jabuticaba* that grows directly in the trunk of its tree rather than hanging from the branches, as usually happens in nature. Thus, whenever people face a peculiar situation, they usually state they are contemplating another *jabuticaba*. Looking at the behaviour of the expected one-year forward interest rate differential between Brazil and the US and the exchange rate between BRL and USD, it looks as if we are facing such a situation.

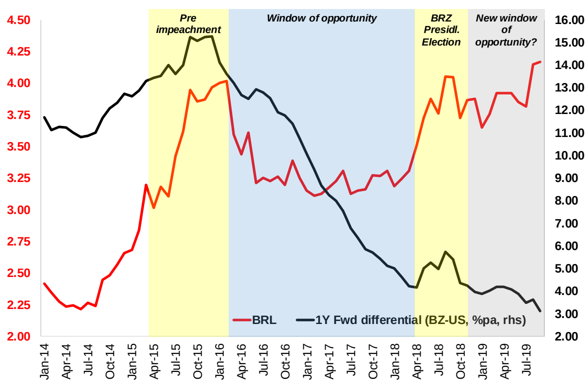
Theoretically, a widening in the interest rate differential between Brazil and the US—due to higher yields in the former or lower ones in the latter—would lead Brazil to attract capital inflows and, hence, the BRL to strengthen compared to the USD. The opposite would happen if the differential narrowed. The trajectories of these variables in recent years have shown a different reality, with BRL weakening taking place in tandem with an increase in the interest rate differential and BRL strengthening following periods when the interest rate differential is narrowing.

Despite the initial oddness of these situations, it seems to us that these moves have to do with the nature of the trajectory of the USD/BRL. In order to check this assumption, we built a model that factors in the influence of international variables—such as commodity prices, the level of the interest rate in the US, the moves of other emerging market currencies against the USD, etc.—on the path of the BRL. After that, we compared the estimates provided by this simulation with the actual level of the FX rate and assumed that the difference between them represents the influence of domestic circumstances on the BRL.

Interestingly, this breakdown helps to explain why we witnessed a widening in the interest rate differential from mid-2015 to early 2016 in tandem with a substantial devaluation of the BRL in the same period. While the model suggests that international circumstances were supposed to lead the Brazilian currency to weaken, we think domestic factors—loss of investment-grade status and the beginning of discussions about the impeachment of Mrs. Rousseff—amplified that move. After Mrs. Rousseff's removal from office, the change in economic directives reduced investors' perception of risk, which allowed the FX rate to strengthen in tandem with a significant narrowing of the interest rate differential.

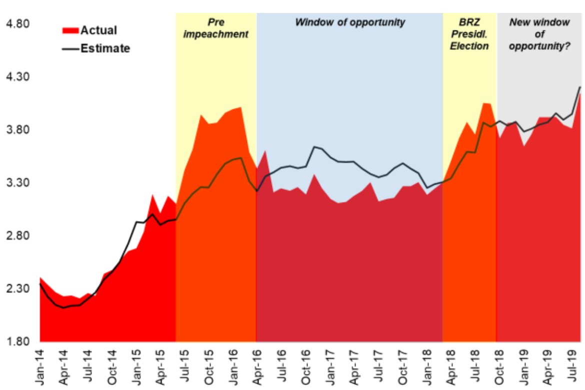
After a slight widening during the recent presidential election campaign, the differential has been at its lowest level lately. However, market participants have taken recent BRL devaluation as a yellow light for the potential continuation of this situation. It is important to bear in mind that, in our view, the move had chiefly to do with external conditions—as signalled by the model—rather than with domestic circumstances. That is the reason why it will be crucial for the incumbent administration to strive for the progress of other structural reforms: it may hinder further weakening of the BRL and create room for the maintenance of a low interest rate differential for a longer period of time.

Chart 23: USD/BRL vs interest rate differential



Source: Santander, Bloomberg

Chart 24: USD/BRL – breakdown by domestic and international influences



Source: Santander, Bloomberg

MXN – Gradual Banxico on external scenario threat to MXN

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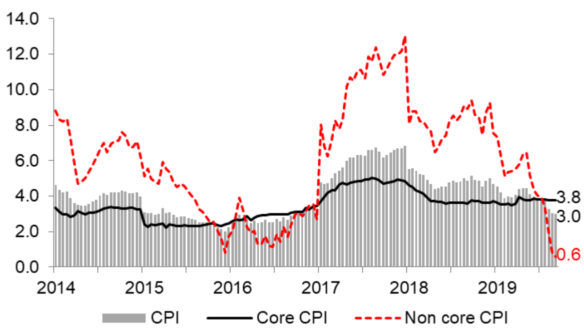
On Thursday, 26 September, we expect the board of Banxico to cut the policy rate to 7.75% from the current 8.0% and to issue a dovish statement. In our view, all the conditions are there for Banxico to start reducing the notably restrictive position it has built up until now. Mexico has among the highest nominal and real rates relative to most emerging markets and the lowest prospects for GDP growth this year, which puts Banxico in an awkward situation that is hard to justify considering the current balance of risks. Headline inflation for the first half of September came in at 2.99% (right in the middle of Banxico's target of 3.0% +/- 1.0%) and core inflation at 3.78%, both YoY. In our view, the current weakness in the economy and the passage of time (allowing previous shocks to core inflation to fade) should allow core inflation to start converging to 3.0% by the beginning of next year. Also, still working towards reducing non-core inflation is the continued downward adjustment of international prices of energy and other commodities.

Chart 25: Consumer prices (annual % var.)



Source: INEGI and Santander.

Our overall assessment of the 2020 budget is that it is austere and responsible. Instead of achieving a primary surplus of 1.0% of GDP, the 2020 budget contemplates a primary surplus of 0.7%, and although this primary surplus is weaker than promised (and with some risk to the downside based on the proposed macro framework), we still call it an austere budget because the expenditure side was already notably austere, with no space for additional cuts. Also, the substantial correction in the current account deficit in the first half of this year (from a deficit of 2.3% of GDP to a deficit of 0.5% this year) shows that monetary policy has no need to be so restrictive when the fiscal side has proven (and continues) to be on the austere side. The external scenario has been relatively stable, making the Mexican peso strong, thus providing a greater cushion for lowering rates.

Chart 26: Public sector expenditure (% GDP)

	Public Sector Programmable Expenditure (GDP%)			
	2017	2018	2019 e/	2020 p/
Programmable Expenditure	**17.6**	**17.3**	**16.8**	**16.6**
Pensions and retairement payments	3.2	3.4	3.6	3.7
Physical investment	2.7	2.7	2.6	2.6

Source: SHCP and Santander.

We now expect Banxico to cut the policy rate by 25bp at each of its next six meetings, regardless of the Fed, reaching 7.25% by year-end 2019 and 6.5% by the third meeting of 2020. We think there is enough visibility now to expect Banxico to continue uninterrupted until they reach 6.5% for the policy rate, which is still attractive in the EM world. Once they reach that level, we would expect to have enough information regarding the state of the global economy (specifically, whether it is entering a recession or decelerating), where the Fed policy rate is going, and where core inflation is heading and how fast (in order to evaluate whether Banxico can keep moving forward to keep closing the spread with the Fed). We think that if conditions play out favourably, the end of this cycle could take the Banxico policy rate to a spread of 400bp versus the Fed policy rate. In our view, the external scenario is still the number one threat to Mexican markets and to the MXN, forcing Banxico to cut in gradual steps of 25bp each rather than 50bp. The approval of the USMCA in the US Congress became more uncertain with the Democrats' decision to launch a formal impeachment inquiry into President Trump, and the threat of a global recession affecting flows to emerging markets remains.

CLP – Blame it on the BCCh

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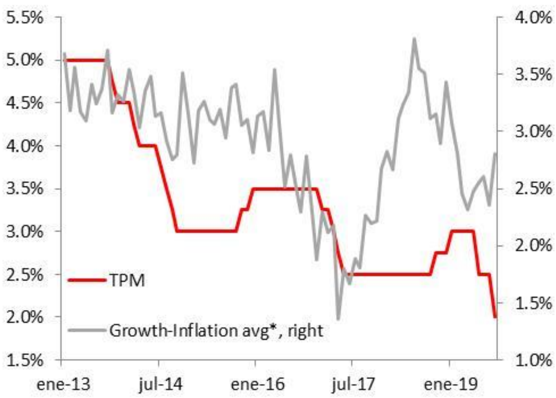
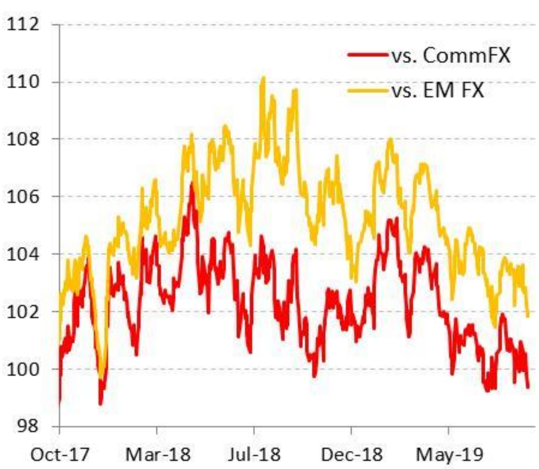
Chart 27: BCCh policy rate (TPM) vs. growth-inflation balance



Growth-inflation avg= average of y/y changes in IMACEC and CPI inflation, last 12M and 12M ahead (as per BCCH survey). Source: BCCH, INE, Santander.

Chart 28: CLP vs. non-USD benchmarks



Base 100=Nov 2016. An increasing value means a stronger CLP vs. peers. Source: Santander

The USDCLP rate has had another month on the roller coaster, fluctuating between 705 and 730 and now quoting close to the upper end of this range. In general, we continue to see the CLP fairly penalised in the EM universe, mainly due to three factors: 1) the US-China trade frictions (China is Chile's main trading partner); 2) very negative NDF points (up to the 5y tenor, where the forward trades 0.5% below the spot; and 3) the super-dovish BCCh. These issues, connected by the low interest rates prevailing in Chile, seem to be gaining importance as of late, with offshore investors being the key driver behind the CLP's soft tone even in a context of copper prices holding on reasonably well in the past few weeks.

The last IPoM report released on 4 September confirmed the clear dovish bias of the BCCh. On top of the 50bp rate cut, to 2%, decided the day before (with minutes later on revealing that even a 75bp adjustment was discussed), the Bank suggested that further easing is likely, mainly based on the negative growth risks stemming from the US-China trade war (and its local repercussions), and the absence of inflationary pressures. The IPoM also cut the GDP projection for 2019 (-65bp to 2.5%), although it was careful to sound dovish but not too bearish. Our sense here is that another 25bp of cuts will come before year-end, and that sub-1% rate levels are likely if the global economy heads toward a recession.

Another important FX announcement was that the BCCh is working to make the CLP a fully deliverable currency in the next two years, in order to make Chile a regional financial centre. Many regulatory steps need to be taken, but the Bank looks fairly committed to fostering CLP usage abroad. Based on the experience of Mexico, we believe that the measure may be positive for the real economy, but at the risk of attracting speculative FX flows to this market, which could exacerbate volatility in a low-yielding, commodity-driven currency such as the CLP.

As regards the growth-inflation balance, trends remain unchanged, still tilting on the dovish side. July's IMACEC came out at a relatively strong 3.2% y/y, but mostly on temporary factors. The 2019 GDP consensus forecast continued to fall, to 2.5%, which means an implicit 3.3% for the Aug-Dec period, vs. the 2.0% average in Jan-Jul. Regarding inflation, August headline as well as core CPI were 2.3% y/y, with most of the components indicating neutral or low underlying pressures. We see inflation staying below target until mid-2020, in line with the BCCh official view (2.8% for end-2020).

In sum, we continue to see markets penalising the CLP in the foreseeable future, due to the China contagion channel, negative carry, and the super-dovish BCCh, on top of the general strength shown by the USD of late. US-China tensions may ease a little, and the Fed might push the USD somewhat lower, but the local rates story would continue dragging the peso. We maintain our short-term range at 695-720, based on a mildly weaker global USD ahead.

ARS – Capital controls have reduced FX volatility

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The spot FX market is gradually consolidating, after the imposition of capital controls by the central bank at the beginning of September. According to the latest foreign exchange flows, Santander traders note that export proceeds are performing quite satisfactorily, when adjusted by the negative agricultural seasonality that is typically observed at this time of year.

The central bank's daily FX interventions have dropped to US$55 million per day this month. The average daily figure is 62% below the US$146 million recorded in August after the primaries.

Dollar deposit leakage, in turn, has stabilised at US$227 million daily in September, or 42% below the US$392 million flight recorded in August. However, albeit occurring at a slower pace, leakage of daily FX sales and dollar deposits has continued since the primary elections.

The dollar quotation in the spot market has significantly reduced its volatility after the peso's free fall. Bear in mind that the local currency dropped more than 20% in the few days after the primary elections, when an unexpected 15% vote differential in favour of the opposition candidate Alberto Fernandez took the market by surprise and left incumbent President Mauricio Macri with a significantly lower likelihood of being re-elected.

Interestingly, some financial inflows can also be detected – mostly through the blue chip arbitrage market – triggered by corporates' decisions to cancel domestic liabilities using hard currency proceeds built up in foreign accounts during the last 18 months. If this incipient process of local debt cancellations continues its current pace, the gap between the dollar spot and the blue chip arbitrage could stabilise after the retracement observed from 23-25 September.

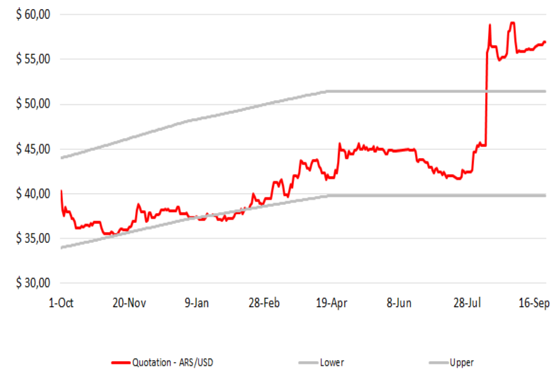
The real effective exchange rate as measured by the central bank – base 15 December 2015=100 – is 27% above its level at the launch of the floating exchange regime at the beginning of the 2015-2019 presidential term, suggesting a quite cheap local currency.

Looking forward, we will remain attentive as to who will be nominated as economic advisor by opposition candidate Alberto Fernandez, should the coalition *Frente de Todos* win the presidency on 27 October 2019.

Although no indications have so far been given by Mr. Fernandez, diverse comments and opinions coming recently from various members of the coalition suggest that the current quotation of around ARS60/USD might be considered satisfactory in real terms by the opposition's technocrats.

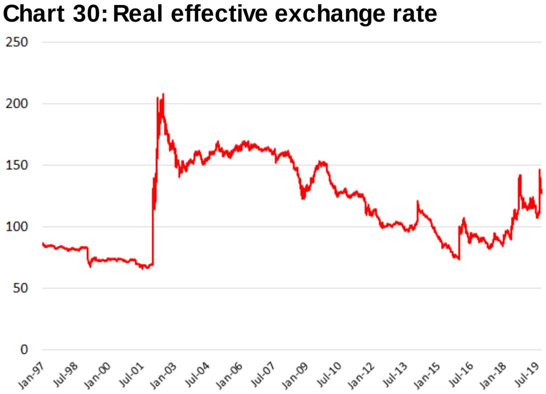
Based on the above, we are projecting ARS67/USD by year-end, which reflects some upward adjustments to the nominal rate that may be intended to capture the inflationary erosion that will take place between September and November 2019.

Chart 29: Nominal exchange rate - ARS/USD



Source: BCRA, Santander, Bloomberg

Chart 30: Real effective exchange rate



Source: BCRA and Santander

CEE FX: Main Themes

Currency	3M view	12M view	Main Themes
PLN	↗	↗	• We decided to further upgrade our year-end EUR/PLN forecast and flattened path for 2020E at 4.30 mainly accounting for the risk related to the European Court of Justice's verdict and the prolonged global growth uncertainty. We believe the EUR/PLN may stay around 4.40 awaiting the ruling but later in the year the pressure might ease.
CZK	↗	↗	• In recent weeks, the Czech Koruna (CZK) has outperformed the PLN and the HUF which might have been due to the solid Czech macro data. EUR/CZK is trading near its 2019 peak and we are leaving our forecasts unchanged.
HUF	↘	↘	• We expect HUF to weaken further in both short term (4QE forecast raised to 340 from 335) and longer term (eg, end of 2020E forecast raised to 350 from 335) as a function of the factors that have been acting on the forint so far (such as a weak external environment).
RUB	⇨	↘	• From now on, we expect USD/RUB to trade within a 62.0–67.0 range in 4Q19E provided that petroleum prices remain high as oil market take longer than initially expected to get supply back to normal.

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

Source: Santander Bank Polska S.A.

PLN – October 3rd: Judgement day

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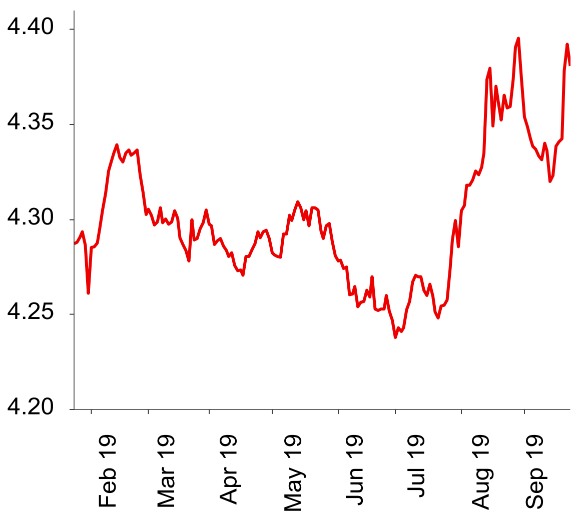
We decided to further upgrade our year-end EUR/PLN forecast and flattened path for 2020E at 4.30 mainly accounting for the risk related to the European Court of Justice's verdict and the prolonged global growth uncertainty. We believe the EUR/PLN may stay around 4.40 awaiting the ruling but later in the year the pressure might ease.

The PLN has been quite volatile in the recent weeks as it first recovered roughly half of losses suffered in mid-July/late-August period but soon returned to c4.40 vs the EUR.

Year-to-date, ten of the main EM currencies lost vs the EUR, out of which five were from the CEE region – the TRY, HUF, PLN, RON and CZK. At the same time, the euro depreciated vs six currencies from the G10 basket.

Chart 31. EUR/PLN



Source: Refinitiv Datastream, Santander Bank Polska

Nearly all EM currencies lost vs the USD but the CEE underperformance suggests there could have been an additional, Europe-related risk factor. In our view, the prolonging Brexit issue could have been the cause.

We also still have a Poland-specific risk factor on the table, namely the European Court of Justice's verdict regarding Polish FX mortgages. The ECJ ruling is expected to be announced on October 3, and we have already seen a sharp PLN depreciation after the date of verdict emerged.

Until now, the issue of the FX mortgages apparently has not been one of the top factors for investors as the exact timing of the verdict was unknown. However, when the information was made public, the market started to price in the scenario where the commercial banks need to buy foreign currencies on the market to cover their FX exposure due to FX mortgages granted. In May, the ECJ's General Ombudsman said that if the methodology used for the calculation of the exchange rate for monthly instalments is ruled illegal, then the mortgage could be converted into a PLN loan at the market FX rate at the time when the initial deal was signed.

It is important to note, however, that there would be no automatic action required on the part of the commercial banks to buy foreign currencies on the market. The ECJ ruling will not be binding for the Polish courts. Furthermore, the pace of any FX purchases would depend on the timing of individual rulings announced by the Polish courts and decisions of the commercial banks. The verdict might mean that banks would now have to include some part of the future losses on their balance sheets but we would probably not know this in early October. There could be some speculative activity on the market against the zloty (with EUR/PLN rising to c4.50) but this should not last long given the likely legal complexity of the verdict and little straightforward evidence of what the ruling actually means for banks.

On October 13, Polish general elections will be held and the recent polls show the ruling Law and Justice (PiS) is well ahead of the opposition parties. It is highly likely that PiS would again win the majority in Parliament and such result should not affect Polish assets meaningfully.

CZK – Data prevented from bigger depreciation

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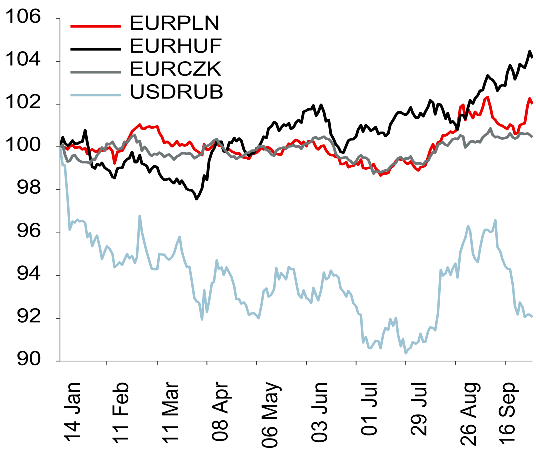
Chart 32. CEE currencies (1 Jan 2019 = 100)



Source: Refinitiv Datastream, Santander Bank Polska

In recent weeks, the Czech Koruna (CZK) has outperformed the PLN and HUF which might have been due to the solid Czech macro data. EUR/CZK is trading near its 2019 peak and we are leaving our forecasts unchanged.

The past few weeks brought a series of positive surprises in the Czech economic activity data after a period of a sluggish releases. August Manufacturing PMI beat expectations after it rose surprisingly for the first time since June 2018. In July, retail sales expanded 6% YoY (the fastest pace since July 2018) while industrial output rebounded to 5.6% (the highest since October 2018) from its multi-month low of -6.4% YoY seen in June. At the same time, inflation held at 2.9% YoY, just below the upper end of the central bank's tolerance range. The central bank expects CPI to stay in the upper half of the 2-3% range for the remainder of the year and then ease towards 2% in 2020. The most recent comments of the Czech central bankers indicate the interest rates are likely to stay on hold in the months to come.

The Czech Republic established a national development fund that is expected to start operating in mid-2020 with cUSD300mn of funding provided by four commercial banks. The fund would engage in infrastructure, education and healthcare projects using leverage to multiply the funding capacity to USD1.5bn. This is the country's response to the likely drop in EU funds in the coming years hence in our view there should not be any meaningful extra effect on economic growth.

HUF – Forint's fall continues

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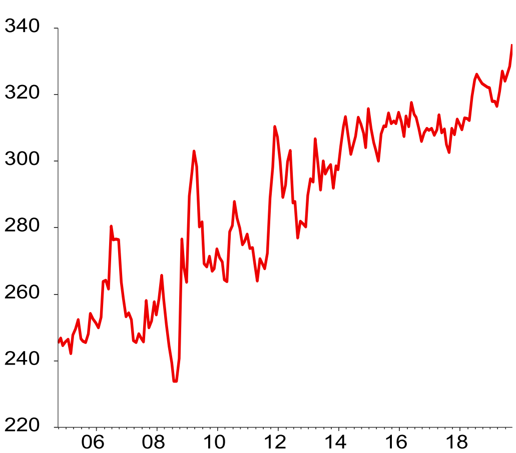
Chart 33. EUR/HUF



Source: Refinitiv Datastream, Santander Bank Polska

EUR/HUF has been the worst performing CEEMEA currency in September and has managed to reach a few new all-time highs, the latest one at 336.1. This weak performance is not surprising given the weak external environment (Eurozone slowing growth) and National Bank of Hungary's (MNB) willingness to accept the currency's weakness.

We expect the HUF to weaken further in both short term (4QE forecast raised to 340 from 335) and longer term (eg, end of 2020 forecast raised to 350 from 335) as a function of the factors that have been acting on the forint so far (like weak external environment). On top of that, we believe that EURHUF might become more volatile in the short run given likely contagion from Poland as the PLN trades increasingly weak ahead of the ECJ's Oct 4 expected ruling regarding CHF mortgages and ahead of the October 13 general elections.

September data has been actually stronger on the margin with Aug industrial production at 8.7% YoY from 4.1% and retail sales at 6.4% from 5.4%.

On Sept 24 the MNB left the base rate unchanged at 0.9% and the deposit rate at -0.1% and underscored that monetary policy orientation remains accommodative. The Central bank noticed a "retreat in CPI rate" (Aug CPI down to 3.1% YoY from 3.3%) and said downward inflation risks have strengthened further due to European slowdown. However, the bank left both the 2020 and 2021 growth (at 3.3%) and inflation (at 3.4% in 2020 and 3.3% in 2021) forecasts unchanged. Median market growth forecast for 2020 and 2021 are at 3.0% and 2.6%, respectively hence so 0.3pp and 0.7pp lower than the central bank's. The MNB also pointed to a much slacker external monetary policy environment given latest Fed and ECB loosening.

RUB – Best CEEMEA performance in September

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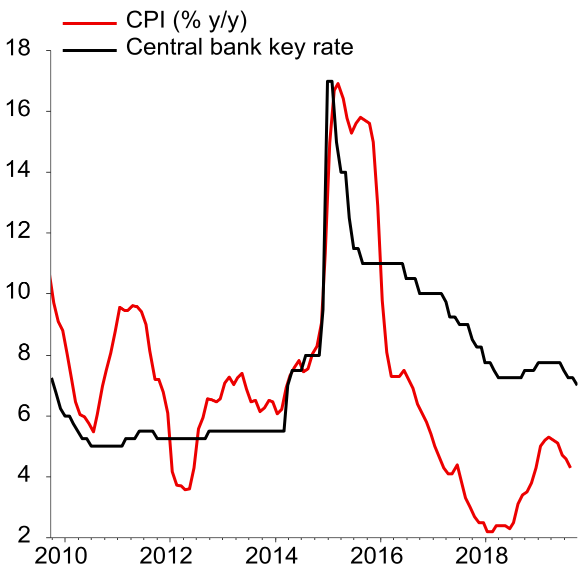
Chart 34. Russia CBR rate and CPI



Source: Refinitiv Datastream, Santander Bank Polska

Oil prices (one of RUB's main performance drivers) are still up c8% MTD, even after significant retracement from their 17% spike due to supply concerns related to attacks on Saudi Arabian oil infrastructure. Not surprisingly, the RUB has been the best performing CEEMEA currency in September (the RUB basket gained c 5%).

From now on, we expect USD/RUB to trade within a 62.0–67.0 range in 4Q19E provided oil prices remain elevated as oil markets take longer to get supply back to normal than initially expected.

Lately, the main theme in Russia has been the Central Bank of the Russian Federation's (CBR) well-communicated rate cutting cycle against a backdrop of slowing growth, inflation and inflation expectations.

As expected, on September 6 the CBR, cut rates to 7.00% from 7.25% as the cutting cycle progresses. Governor Elvira Nabiullina said the CBR will soon consider cutting again but declined to comment whether in Oct or in Dec. The CBR will most likely lower rates to 6.50% by 2H20E (50bp lower from the current rate) which is a mid of the of the 6-7% interest rate range the bank considers neutral for its 4.0% inflation goal. The pace of cuts should not be aggressive – probably one 25bp cut in 2019E still and another 25bp 1H20E.

As for growth, the CBR lowered its 2019 projections to 0.8%-1.3% (1.05% mid) from 1.0%-1.5% (1.25% mid) citing the slowdown in growth of global economy as the main reason. Median growth forecasts of market participants for 2019 declined to 1.1% from 1.2% and for 2020 to 1.6% from 1.7%.

August manufacturing PMI fell to 49.1 from 49.3 while industrial production YoY slightly rose to 2.9% from 2.8% beating expectations at 2.2%.

On the inflation front, August CPI declined to 4.3% YoY from 4.6%, core CPI to 4.3% y/y from 4.5% while PPI YoY fell to 0.3% from 1.1%. The CBR cut it 2019 forecast from 4.2%-4.7% (4.45% mid) to 4.0%-4.5% (4.25% mid). Median inflation forecast by market participants for 2019 declined to 4.7% from 4.8% and for 2020 remained flat at 4.0% (the exact level of CBR's inflation target).

Fixed income market continued its price rally. Yields of OFZ bonds fell MTD by 5-10 bp e.g. JUL'22 to 6.64% from 6.75%, FEB'24 to 6.76% from 6.79% and MAY'29 to 7.01% from 7.09%. RUB cross currency swaps traded lower in yields as well: 2yr fell to 6.25% from 6.60% while 5yr to 5.89% from 6.13%. Moreover, falling FX realized volatility (USDRUB 1mth at 8.1) and better sovereign credit risk (z-spread for 10yr USD bonds narrowed to 177bp from 225bp in June) point to a positive assessment of Russian assets by investors. Notwithstanding this positive sentiment is likely to remain as long as oil keeps trading rich, however the FX and bonds rally might soon be losing its momentum both on fundamental (cutting cycle almost fully priced in) and technical grounds. Hence, prices may stabilize here or even retrace a bit.

G10 FX: IMM Speculative Positioning

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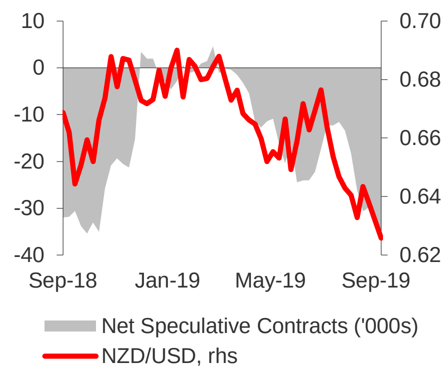
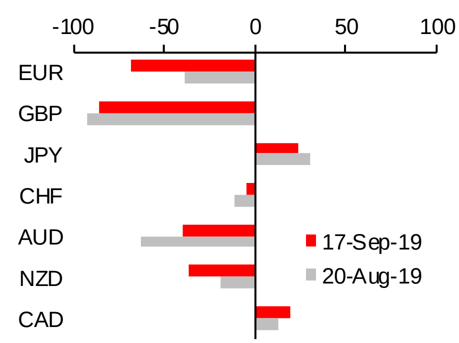
IMM commitment of traders report: NZD/USD position



- **The net short NZD position is now at an all-time high,** rising to 36k contracts in the week ended 17 September 2019, from 29k contracts the prior week, and just 18k contracts four weeks ago. This position has been led by a sharp increase in short contracts following the RBNZ's surprise 50bp rate cut in August.
- **The AUD position has improved in recent weeks,** but remains net short, at 40k contracts (63k contracts four weeks ago). Speculators have held a net short AUD position since April 2018, and the prospect of weak domestic growth, low inflation, and further rate cuts suggests that this position is likely to persist in Q4-19.
- **Speculators turned more negative on the EUR in September,** with the net short position rising to 69k contracts, from just 38k contracts four weeks ago. This decline in EUR long contracts contrasts with the increase in the net USD composite position, which has risen to 110k contracts, the most since June.
- **Speculators retain a large net short GBP positon,** at 86k contracts. With just five weeks until the current Brexit deadline (31-Oct-19), sterling is likely to remain out of favour for now.

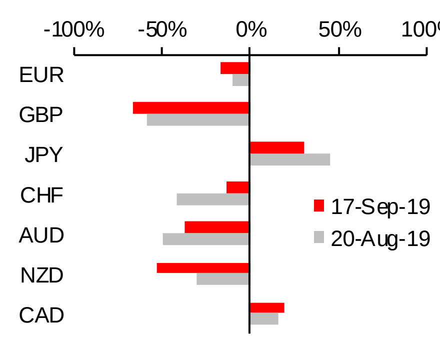
Net Speculative Contracts ('000s)*

	17-Sep-19	20-Aug-19	4w chg	YtD chg
USD***	110.1	68.0	42.1	107.4
EUR	-68.6	-38.0	-30.6	-160.7
GBP	-86.1	-92.4	6.3	-98.8
JPY	23.9	31.2	-7.3	139.9
CHF	-4.6	-11.1	6.6	9.3
AUD	-40.1	-62.8	22.7	-26.4
NZD	-36.0	-18.3	-17.8	-18.5
CAD	19.8	13.0	6.8	2.5



Net Speculative Contracts as % of Open Interest**

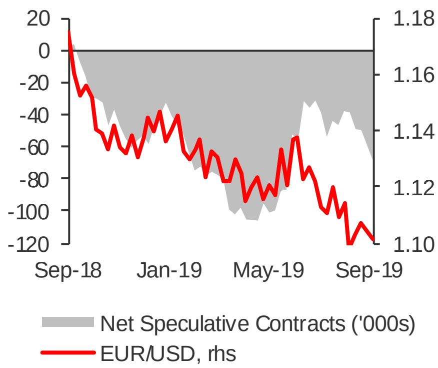
	17-Sep-19	20-Aug-19	4w chg	YtD chg
USD***	10%	6%	4%	10%
EUR	-17%	-10%	-7%	-46%
GBP	-67%	-58%	-9%	-76%
JPY	31%	45%	-15%	87%
CHF	-13%	-41%	28%	5%
AUD	-37%	-49%	13%	-22%
NZD	-53%	-30%	-23%	-21%
CAD	19%	16%	3%	-7%



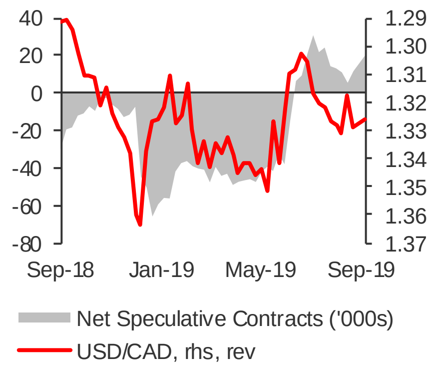
Sources: CFTC, Bloomberg, Santander. Note: *Net Speculative Contracts = Long non-commercial traders contracts minus short non-commercial traders contracts, **Open Interest = The total number of outstanding long and short futures contracts, ***USD composite index = USD composite index uses AUD, CAD, CHF,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

G10 FX: IMM Speculative Positioning

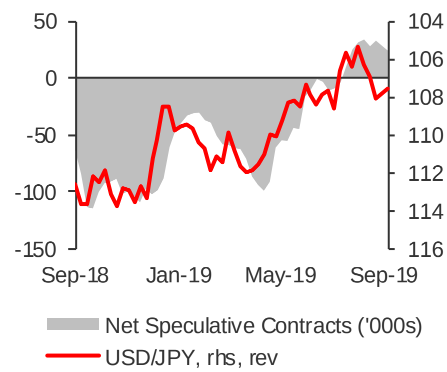
EUR/USD



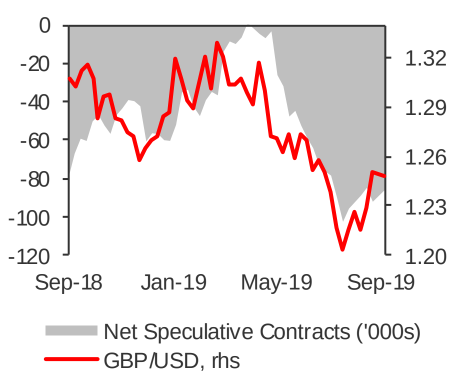
USD/CAD



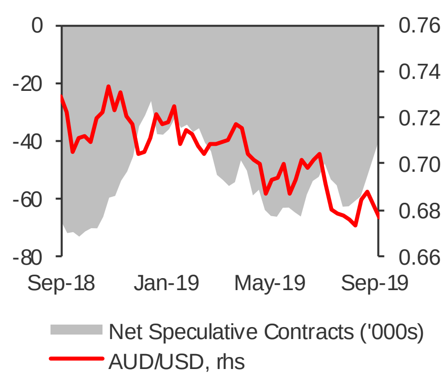
USD/JPY



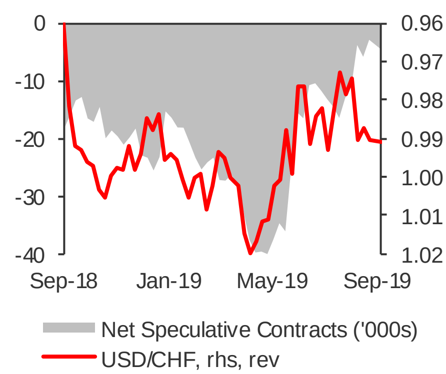
GBP/USD



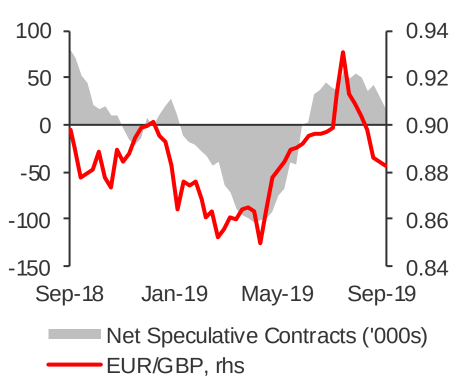
AUD/USD



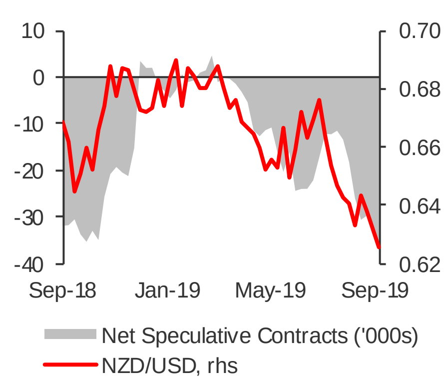
USD/CHF



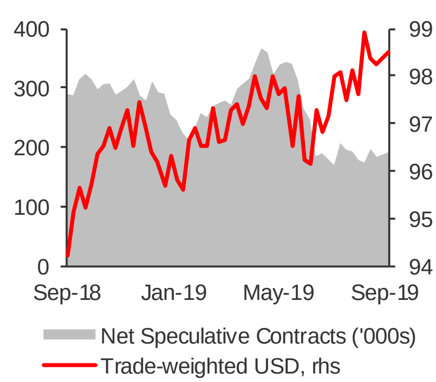
EUR/GBP



NZD/USD



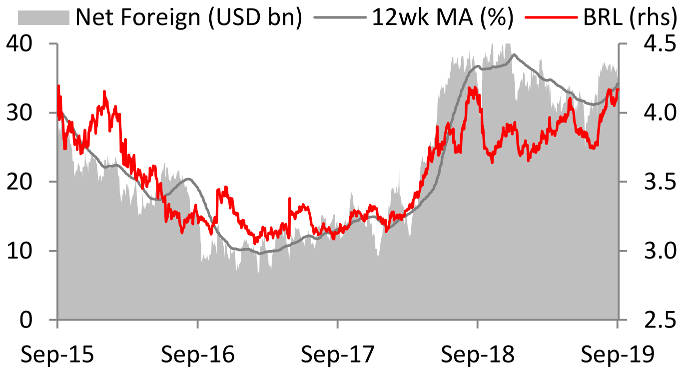
USD minus MXN



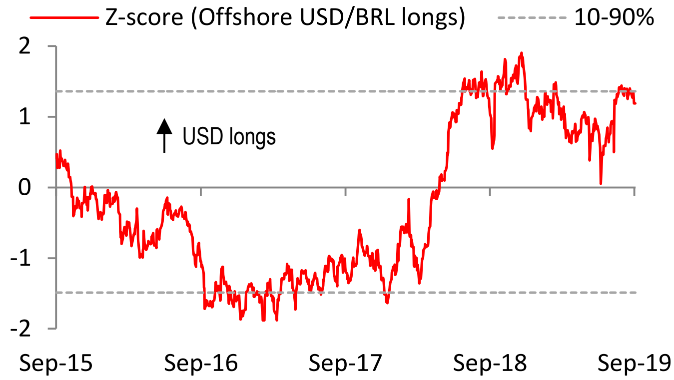
Sources: CFTC, Bloomberg and Santander. Note: IMM commitment of traders report

Latin America FX: Positioning indexes (Z-scores)

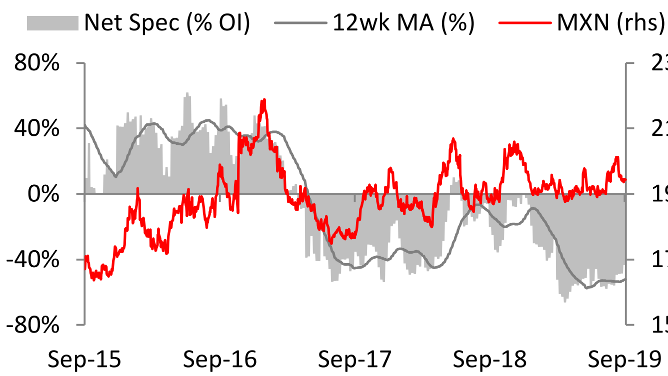
USD/BRL



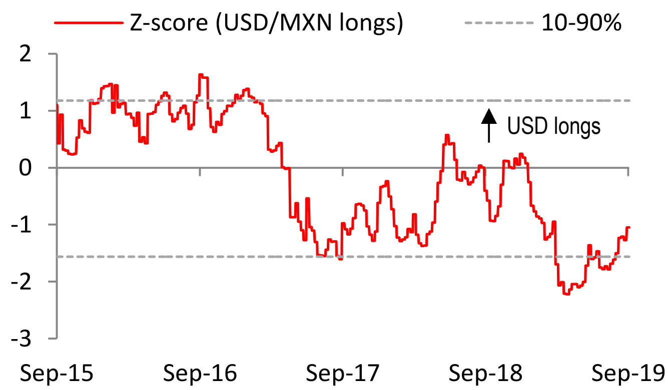
Z-score USD/BRL



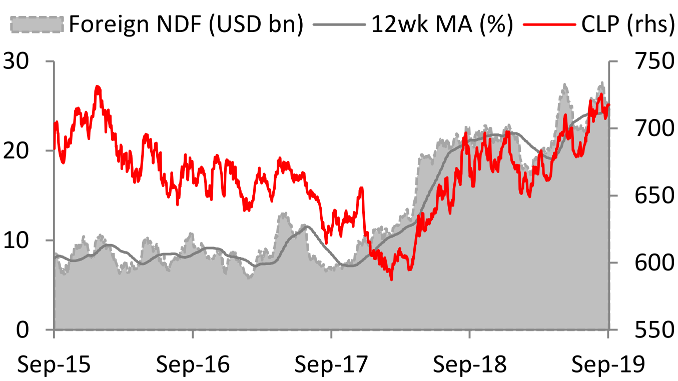
USD/MXN



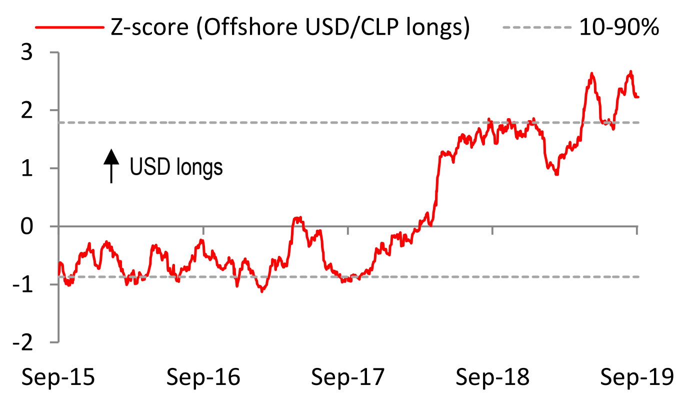
Z-score USD/MXN



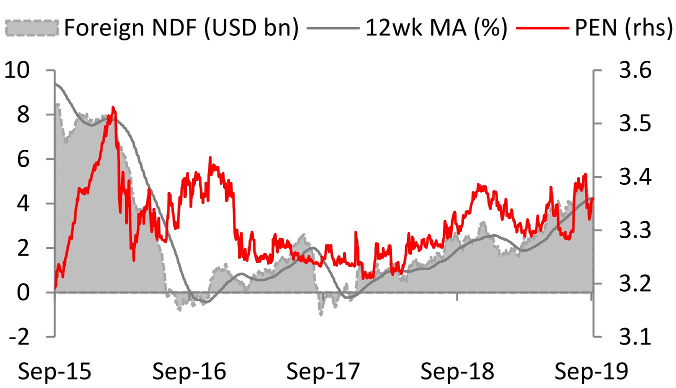
USD/CLP



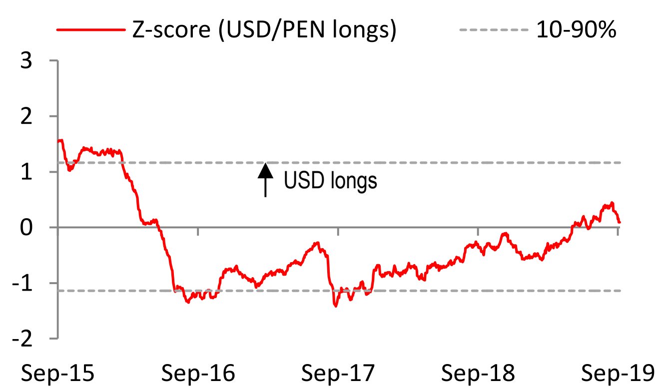
Z-score USD/CLP



USD/PEN



Z-score USD/PEN



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

Euro Interest Rate Forecasts

Government Bond yield Forecasts

Germany	Current	4Q19	1Q20	2Q20	3Q20
ECB Depo	-0.50	-0.50	-0.50	-0.50	-0.50
3m	-0.51	-0.51	-0.46	-0.46	-0.46
2y	-0.74	-0.65	-0.60	-0.55	-0.50
5y	-0.76	-0.60	-0.55	-0.45	-0.40
10y	-0.58	-0.40	-0.35	-0.25	-0.15
30y	-0.10	0.10	0.15	0.25	0.30

Swap rate forecasts

Euro	Current	4Q19	1Q20	2Q20	3Q20
ECB Depo	-0.50	-0.50	-0.50	-0.50	-0.50
3m	-0.41	-0.41	-0.41	-0.41	-0.41
2y	-0.45	-0.35	-0.35	-0.30	-0.30
5y	-0.41	-0.25	-0.20	-0.10	-0.10
10y	-0.17	0.00	0.05	0.15	0.20
30y	0.19	0.40	0.45	0.55	0.60

US Interest Rate Forecasts

Government Bond yield Forecasts

US	Current	4Q19	1Q20	2Q20	3Q20
FOMC *	2.00	1.75	1.75	1.75	1.75
3m	1.85	1.60	1.50	1.55	1.55
2y	1.67	1.40	1.45	1.50	1.60
5y	1.59	1.50	1.50	1.65	1.75
10y	1.71	1.45	1.45	1.60	1.75
30y	2.15	1.95	2.10	2.20	2.30

Swap rate forecasts

US	Current	4Q19	1Q20	2Q20	3Q20
FOMC *	2.00	1.75	1.75	1.75	1.75
3m	2.10	1.75	1.65	1.70	1.65
2y	1.66	1.35	1.40	1.45	1.50
5y	1.52	1.35	1.35	1.55	1.65
10y	1.58	1.35	1.35	1.50	1.65
30y	1.72	1.70	1.80	1.90	2.10

UK Interest Rate Forecasts

Government Bond yield Forecasts

UK	Current	4Q19	1Q20	2Q20	3Q20
MPC	0.75	0.75	0.75	0.75	0.75
3m	0.80	0.80	0.72	0.72	0.75
2y	0.46	0.45	0.50	0.60	0.65
5y	0.38	0.50	0.55	0.70	0.75
10y	0.53	0.75	0.85	0.95	1.00
30y	0.96	1.35	1.50	1.60	1.60

Swap rate forecasts

UK	Current	4Q19	1Q20	2Q20	3Q20
MPC	0.75	0.75	0.75	0.75	0.75
3m	0.76	0.85	0.80	0.80	0.83
2y	0.74	0.75	0.80	0.85	0.90
5y	0.68	0.90	0.85	0.95	1.00
10y	0.68	0.95	0.95	1.05	1.10
30y	0.70	1.10	1.10	1.20	1.20

G10 Central Bank Calendar

	Current Rate	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec
FOMC (Upper)	2.00	Unch.	-	Unch.	-	Unch.	Unch.	-25bp	-	-25bp	30	-	11
ECB (Depo)	-0.50	Unch.	-	Unch.	Unch.	-	Unch.	Unch.	-	-10bp*	24	-	12
BoE	0.75	-	Unch.	Unch.	-	Unch.	Unch.	-	Unch.	Unch.	-	7	19
BoJ	-0.10	Unch.	-	Unch.	Unch.	-	Unch.	Unch.	-	Unch.	31	-	19
SNB	-0.75	-	-	Unch.	-	-	Unch.	-	-	Unch.	-	-	12
BoC	1.75	Unch.	-	Unch.	Unch.	Unch.	-	Unch.	-	Unch.	30	-	4
RBA	1.00	-	Unch.	Unch.	Unch.	Unch.	-25bp	-25bp	Unch.	Unch.	1	5	3
RBNZ	1.00	-	Unch.	Unch.	-	-25bp	Unch.	-	-50bp	Unch.	-	13	-
Norges Bank	1.50	Unch.	-	+25bp	-	Unch.	+25bp	-	Unch.	+25bp	24	-	19
Riksbank	-0.25	-	Unch.	-	Unch.	-	-	Unch.	-	Unch.	24	-	19

Source: Bloomberg, Santander. Note: Current levels as at 26-Sept-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. US and UK rates forecasts correct as at last I&E report (6-Sept-2019). EZ rates forecasts correct as at EUR Rates Strategy Update (18-Sept-2019).

Brazil/Mexico Interest Rate forecasts

Brazil	Current	4Q19	1Q20	2Q20	3Q20
SELIC	5.50	4.50	4.50	4.50	4.50
NTNF Jan' 25s	6.59	6.30	6.00	6.00	6.00
NTNF Jan.' 29s	7.09	7.00	7.00	7.00	7.00

Mexico	Current	4Q19	1Q20	2Q20	3Q20
Banxico fondeo	8.00	7.25	6.75	6.50	6.50
Mbono Jun. '21s	6.73	6.70	6.60	6.60	6.60
MBono Jun. '29s	6.67	6.90	6.80	6.70	6.70

Chile/Argentina Interest Rate Forecasts

Chile	Current	4Q19	1Q20	2Q20	3Q20
BCCh TPM	2.00	1.75	1.75	1.75	1.75
BCP 5Y	2.84	2.15	2.20	2.25	2.30
BCP 10Y	2.73	2.65	2.70	2.75	2.80

Argentina	Current	4Q19	1Q20	2Q20	3Q20
LELIQ 7-day	80.83	72.00	63.50	55.00	46.50

LatAm Central Bank Calendar

	Current Rate	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec
Brazil	5.50	-	Unch.	Unch.	-	Unch.	Unch.	-50bp	-	-50bp	30	-	11
Mexico	8.00	-	Unch.	Unch.	-	Unch.	Unch.	-	-25bp	26	-	14	19
Chile	2.00	+25bp	-	Unch.	-	Unch.	-50bp	Unch.	-	-50bp	23	-	6
Colombia	4.25	Unch.	-	Unch.	Unch.	-	Unch.	Unch.	-	27	31	-	20
Argentina*	80.83	-557bp	-356bp	+1803bp	+578bp	-320bp	-804bp	-229bp	+2287bp	~	~	~	~
Peru	2.50	Unch.	Unch.	Unch.	Unch.	Unch.	Unch.	Unch.	-25bp	Unch.	10	7	12

CEE Interest Rate Forecasts

Poland	Current	4Q19	1Q20	2Q20	3Q20
Reference Rate	1.50	1.50	1.50	1.50	1.50
2y	1.48	1.55	1.55	1.55	1.60
10y	2.03	2.15	2.20	2.20	2.30

CEE	Current	4Q19	1Q20	2Q20	3Q20
Hungary	0.90	0.90	0.90	0.90	0.90
Czech Republic	2.00	2.00	2.00	2.00	2.00
Russia	7.00	7.00	6.75	6.50	6.50

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.	Unch.	-	Unch.	2	6	4
Czech Republic	2.00	-	Unch.	Unch.	-	+25bp	Unch.	-	Unch.	Unch.	-	7	19
Hungary	0.90	Unch.	Unch.	Unch.	Unch.	Unch.	Unch.	Unch.	Unch.	Unch.	22	19	17
Russia	7.00	-	Unch.	Unch.	Unch.	-	-25bp	Unch.	-	-25bp	25	-	13

Source: Bloomberg, Santander. Note: Current levels as at 26-September-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 October 2018 (the decision was made fortnightly previously).

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

	3M	6M	9M
EUR/USD	**1.14**	**1.14**	**1.15**
vs.forward	4.2	4.2	5.1
vs.consensus forecast	3.6	1.8	0.9
GBP/USD	**1.28**	**1.26**	**1.26**
vs.forward	3.8	2.2	2.2
vs.consensus forecast	4.9	1.6	-0.8
EUR/GBP	**0.89**	**0.90**	**0.91**
vs.forward	0.3	1.9	2.8
vs.consensus forecast	-2.1	0.5	1.4
USD/JPY	**106**	**106**	**103**
vs.forward	-1.5	-1.5	-4.3
vs.consensus forecast	1.0	1.0	-1.9
EUR/JPY	**121**	**121**	**118**
vs.forward	2.6	2.6	0.6
vs.consensus forecast	4.2	2.4	-0.5
EUR/CHF	**1.11**	**1.12**	**1.13**
vs.forward	2.1	3.1	4.0
vs.consensus forecast	0.9	1.8	1.8
USD/CHF	**0.97**	**0.98**	**0.98**
vs.forward	-2.0	-1.1	-1.1
vs.consensus forecast	-1.6	-0.8	0.3
EUR/SEK	**10.6**	**10.6**	**10.5**
vs.forward	-0.7	-0.7	-1.6
vs.consensus forecast	-1.1	-0.7	-1.7
EUR/NOK	**9.8**	**9.7**	**9.7**
vs.forward	-1.1	-2.1	-2.1
vs.consensus forecast	-1.0	-1.0	0.0
USD/CAD	**1.29**	**1.28**	**1.27**
vs.forward	-2.7	-3.4	-4.2
vs.consensus forecast	-3.0	-3.0	-2.3
AUD/USD	**0.70**	**0.70**	**0.71**
vs.forward	3.6	3.6	5.1
vs.consensus forecast	2.9	2.9	2.9
NZD/USD	**0.67**	**0.68**	**0.68**
vs.forward	6.4	8.0	8.0
vs.consensus forecast	4.7	6.3	4.6

	3M	6M	9M
USD/BRL	**4.00**	**3.90**	**3.90**
vs.forward	-3.6	-6.0	-6.0
vs.consensus forecast	1.3	-2.5	0.0
EUR/BRL	**4.56**	**4.45**	**4.49**
vs.forward	0.4	-2.1	-1.2
vs.consensus forecast	4.9	-0.8	0.9
USD/MXN	**19.8**	**19.8**	**20.1**
vs.forward	1.2	1.2	2.7
vs.consensus forecast	0.5	0.3	1.1
EUR/MXN	**22.6**	**22.6**	**23.1**
vs.forward	5.4	5.4	7.9
vs.consensus forecast	4.1	2.0	1.9
USD/CLP	**715**	**705**	**700**
vs.forward	-1.7	-3.1	-3.8
vs.consensus forecast	-0.4	-0.1	0.0
EUR/CLP	**815**	**804**	**805**
vs.forward	2.4	0.9	1.1
vs.consensus forecast	3.2	1.6	0.9
USD/ARS	**67**	**72**	**76**
vs.forward	17.4	25.3	33.8
vs.consensus forecast	18.6	10.0	9.1
EUR/ARS	**76**	**82**	**88**
vs.forward	22.2	30.5	40.5
vs.consensus forecast	22.9	12.0	10.0
EUR/PLN	**4.30**	**4.30**	**4.30**
vs.forward	-1.9	-1.9	-1.9
vs.consensus forecast	0.0	-1.1	-1.1
EUR/CZK	**25.6**	**25.4**	**25.2**
vs.forward	-0.7	-1.5	-2.3
vs.consensus forecast	-0.8	-1.6	-2.7
EUR/HUF	**340**	**340**	**345**
vs.forward	1.7	1.7	3.2
vs.consensus forecast	4.6	3.0	4.5
EUR/RUB	**74**	**76**	**81**
vs.forward	5.3	8.5	14.4
vs.consensus forecast	0.9	4.4	9.6

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	1.094	1.235	107.69	117.86	133.03	0.993	1.087	1.227
1M	1.097	1.237	107.45	117.88	132.92	0.990	1.087	1.225
2M	1.099	1.238	107.25	117.90	132.81	0.988	1.086	1.224
3M	1.102	1.240	107.04	117.93	132.69	0.986	1.086	1.222
6M	1.109	1.244	106.32	117.93	132.20	0.978	1.085	1.216
9M	1.116	1.246	105.73	117.97	131.78	0.971	1.084	1.211
12M	1.122	1.249	105.16	118.01	131.34	0.965	1.083	1.205

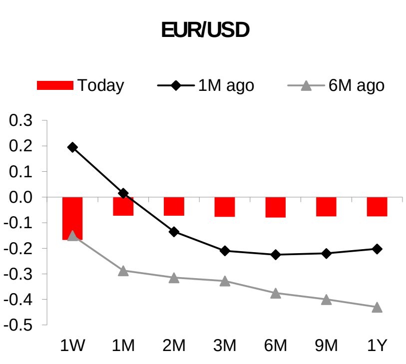
ATMf vol.

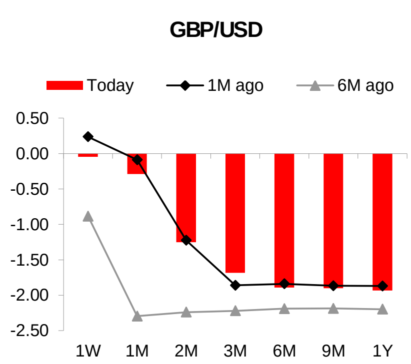
	EUR/USD	GBP/USD	USD/JPY	EUR/JPY	GBP/JPY	USD/CHF	EUR/CHF	GBP/CHF
1W	5.3%	9.1%	6.1%	7.0%	10.4%	5.9%	5.1%	9.7%
1M	5.4%	11.2%	6.2%	7.0%	12.4%	5.6%	5.0%	11.2%
2M	5.5%	11.6%	6.6%	7.1%	13.0%	5.8%	5.1%	11.5%
3M	5.6%	12.0%	6.7%	7.2%	13.4%	5.9%	5.1%	11.8%
6M	5.7%	10.8%	6.7%	7.3%	12.3%	6.1%	5.1%	10.6%
9M	5.9%	10.0%	6.9%	7.4%	11.7%	6.3%	5.2%	9.9%
12M	6.0%	9.6%	6.9%	7.5%	11.3%	6.4%	5.2%	9.5%

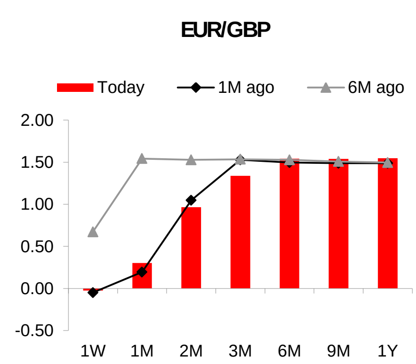
Implied/realized vol. ratio

	EUR/USD	GBP/USD	USD/JPY	EUR/JPY	GBP/JPY	USD/CHF	EUR/CHF	GBP/CHF
1W	1.04	1.19	1.15	1.13	1.16	0.91	0.92	1.13
1M	0.94	1.36	1.11	0.98	1.27	0.91	0.96	1.24
2M	0.99	1.44	0.85	0.94	1.21	0.86	0.97	1.25
3M	1.06	1.62	0.97	1.05	1.42	0.93	1.04	1.42
6M	1.12	1.53	1.10	1.14	1.46	1.03	1.13	1.41
9M	1.09	1.26	1.05	1.06	1.18	1.09	1.15	1.22
12M	1.03	1.17	1.09	1.05	1.16	1.09	1.12	1.17

25-delta risk reversals







Sources: Bloomberg and Santander. As of 26-September-19

Latin America FX: Spot and forward rates

	USD/ARS	USD/BRL	USD/CLP	USD/COP	USD/MXN	USD/PEN
Spot	57.1	4.15	728	3433	19.6	3.35
1M	64.0	4.15	727	3438	19.7	3.36
2M	69.9	4.16	727	3442	19.8	3.36
3M	75.1	4.17	726	3447	19.9	3.36
6M	88.1	4.19	725	3467	20.1	3.38
9M	98.7	4.21	723	3489	20.4	3.39
12M	108.2	4.24	722	3515	20.6	3.40

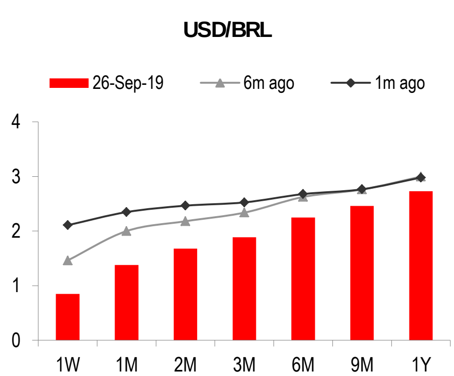
ATMf vol.

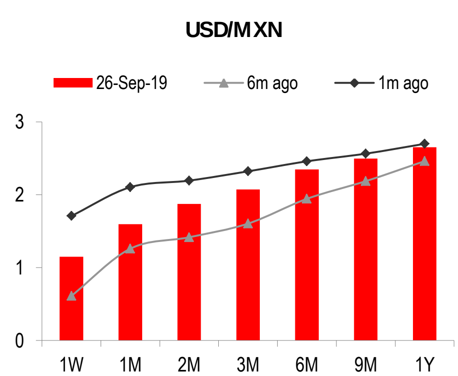
	USD/ARS	USD/BRL	USD/CLP	USD/COP	USD/MXN	USD/PEN
1W	6.65	13.77	9.48	10.25	8.91	3.74
1M	9.53	12.97	9.38	10.58	9.20	4.01
2M	11.58	12.90	9.35	10.67	9.71	4.26
3M	13.30	12.89	9.38	10.81	10.05	4.44
6M	16.75	12.84	9.39	10.87	10.75	4.79
9M	18.68	12.88	9.37	10.95	11.27	5.11
12M	19.95	12.91	9.39	10.96	11.59	5.26

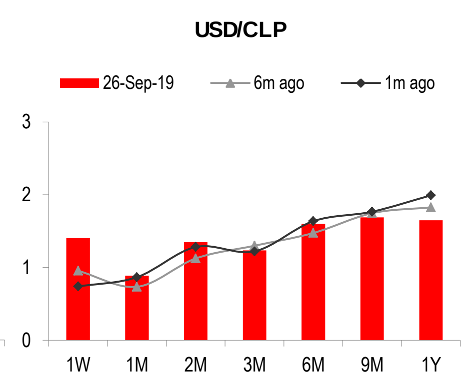
Implied/realized vol. ratio

	USD/ARS	USD/BRL	USD/CLP	USD/COP	USD/MXN	USD/PEN
1W	1.68	1.57	1.54	1.29	1.25	1.03
1M	0.22	1.18	1.23	1.18	1.18	0.84
2M	0.16	0.93	0.96	0.83	0.99	0.83
3M	0.22	1.00	1.06	0.96	1.06	1.00
6M	0.37	1.06	1.06	1.02	1.04	1.12
9M	0.50	1.03	1.05	1.09	1.13	1.26
12M	0.59	0.94	1.01	1.09	1.07	1.38

25-delta risk reversals







Sources: Bloomberg and Santander. As of 26-September-19

IMPORTANT DISCLOSURES

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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.

We generally review our FX recommendations monthly, in our regular FX Compass publication, and when market events/moves so warrant.

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