Currency Report Card – May 2024

10 May 2024

Forecasts

May 2024

Three month forecast returns

Most bullish	Most bearish
COP	CHF
MXN	AUD
BRL	SEK

Source: RBC Capital Markets

12 month forecast returns

Most bullish	Most bearish
BRL	CHF
COP	JPY
NOK	CNY

Source: RBC Capital Markets

Please note that we are introducing SEK and NOK forecasts this month.

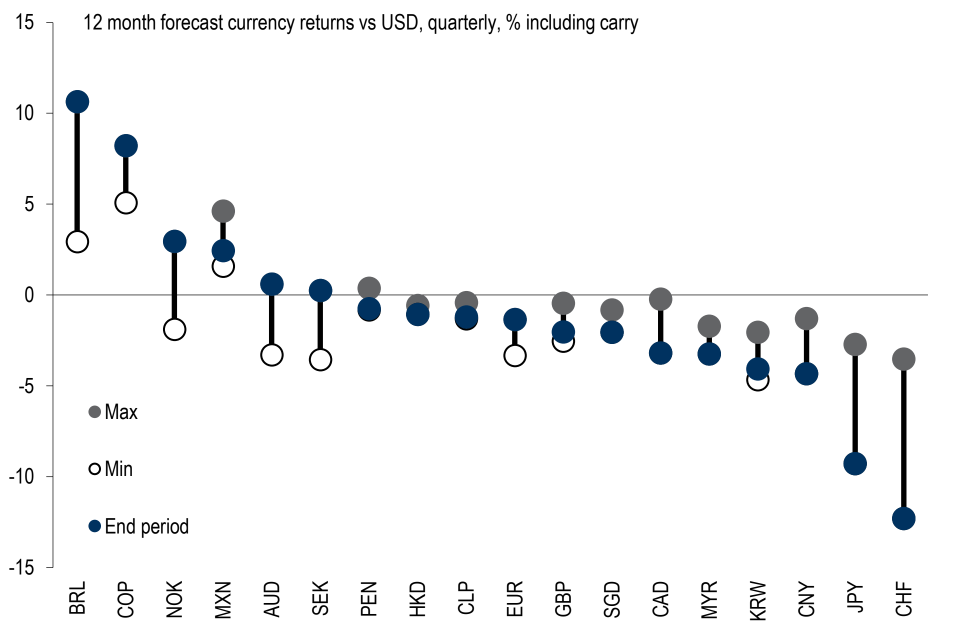
Key forecast revisions:

USD/JPY: Profile revised higher. End-2024 now 162 (prior 154). End-2025 156 (150).

USD/CAD: Longer-run profile revised higher. End-2024 now 1.40 (prior 1.33). End-2025 1.40 (1.33).

AUD/USD: 2024 profile unchanged. Most of the 2025 profile revised lower. End-2025 now 0.68 (prior 0.72).

BRL, COP outperformance; CHF, JPY underperformance



Source: RBC Capital Markets

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US Dollar

Elsa Lignos

1-3 Month Outlook – Incremental gains with risks

USD is up again since our last Currency Report Card, though it is telling that it is not up by more. The March CPI report, published on April 10, caused a sharp rerating of US rate expectations (Figure 1). FOMC officials were forced to acknowledge that the upside surprises in Jan and Feb CPI were more than a "bump in the road". But USD has struggled to hold onto gains and the market reaction to (1) the May FOMC highlighting the high hurdle for hikes, (2) slightly softer April NFP and (3) the outsized reaction to this week's jump in initial jobless claims shows how low the hurdle is for softer data hurting USD and conversely how high the hurdle is for further USD gains. We have left our near-term USD forecasts mostly unchanged despite the change to our Fed call (dropping two cuts from the 2024 forecast, now starting in Dec with -25bps and only two further cuts in 2025). The main exception to that is JPY, which remains the most leveraged currency to front end US rates (see pg 5). If US activity data remain stable, with inflation only gradually declining (our economists' base case), USD continues to benefit from its positive carry and we expect EUR/USD to revisit 1.06/1.05 in Q2/Q3. There are scenarios that could get EUR/USD to parity (significant escalation with Russia or the Middle East, unexpected negative shock in the Euro area, e.g. a European bank failure), but for most people, ourselves included, they are not the base case. On the flipside, with US exceptionalism now completely consensus, USD has asymmetric risk from a slowdown in US data. In the absence of either, we see USD making small incremental gains in a low vol/positive carry trade environment.

6-12 Month Outlook – What can Trump do to USD?

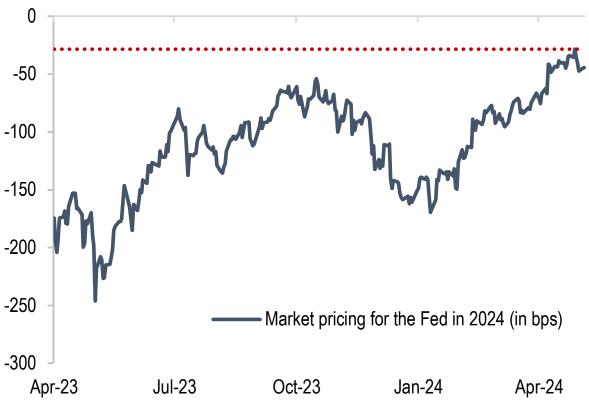
It seems the investor base expecting Trump to be USD-negative is growing – helped by the Politico article last month talking about Trump trade advisers "plotting" a USD devaluation. On a recent NA client trip we found investors 2/3-1/3 split in favour of a Trump victory pushing USD lower. But Trump has limited power to force the Fed's hand if sticky inflation warrants rates on hold. He cannot replace the Chair until Powell's term ends in 2026. Trump could push for a new Plaza Accord but outside Japan, it wouldn't be straightforward to find support. Tariffs on foreign goods are more likely to help than hurt USD. Longer-term, some investors worry that large govt deficits risk pushing USD into long-term decline but as always, we argue that the domestic private sector surplus (Figure 2) prevents that from being an investable idea. Our 2025 USD profile remains pretty flat. The biggest downside risk remains a US recession which is a tail risk rather than base case scenario.

Indicators

	Current (Previous)*
Official cash rate	**5.25-5.50% (5.00-5.25%)**
Trend interest rates (10yr average)	1.4%
Bias in interest rate market	Lower
Core PCE Inflation %Y/Y Jan (Feb)	**2.8% (2.8%)**
Inflation target	2%, on average
Budget balance % GDP 2023 (2022)	**-6.5% (-5.5%)**
Budget balance target % GDP	-
GDP Growth % q/q saar Q4 (Q3)	1.6% (3.4%)
Trend GDP %	2.7%
Purchasing Power Parity Value	**-**
Spot	-
PPP Valuation	-
Current account balance % GDP Q4 (Q3)	**-2.9% (-3.0%)**
Trend current account balance % GDP	-2.5%
Moody's Foreign Currency Rating	**Aaa**
Outlook	Negative

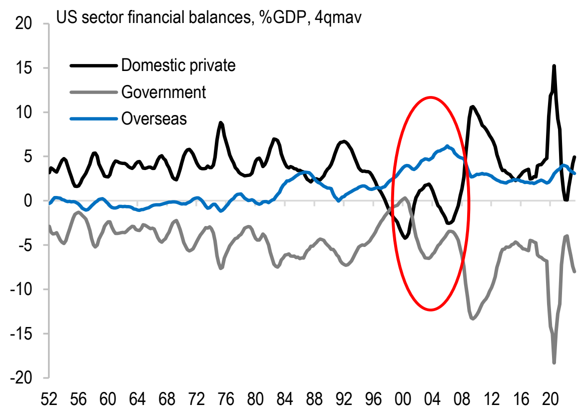
* Current is latest month, quarter or year

1. Markets now priced for less than 2 cuts in 2024 (-45bp)



Source: Bloomberg, RBC Capital Markets

2. Watch out for triple not twin deficits



Source: Federal Reserve, RBC Capital Markets

Forecasts

	2024				2025			
	Q1	Q2f	Q3f	Q4f	Q1f	Q2f	Q3f	Q4f
EUR/USD	1.08	1.06	1.05	1.07	1.08	1.08	1.09	1.08
USD/JPY	151	158	160	162	162	160	158	156
USD/CAD	1.35	1.37	1.39	1.40	1.41	1.42	1.41	1.40

Source: RBC Capital Markets estimates

Euro

Elsa Lignos

1-3 Month Outlook – June cut, and then what?

In the past month, we have found more investors coming around to the idea of the bounce in Euro area activity. To be fair, our EZ economic momentum indicator already shows signs of waning (i.e. data releases are coming in net marginally softer than the previous period's release). But relative to very depressed expectations, data are surprising to the upside. Our EZ ESI remains positive (Figure 1) building incremental gains since the start of the year. What does that mean for EUR? At the moment, not very much. Despite the upside surprises in US data and the sharp revision to Fed expectations, with the ECB still strongly signalling a June start to the easing cycle, EUR/USD is exactly where it was at the start of April. A run down to 1.06 was short-lived and as we go to press, we sit just shy of 1.08 again. Positioning is back to ~25% net short. It hit -45% in mid/late April but has since retraced in line with the bounce in spot. Our outlook is little changed. Whenever EUR/USD gets to a 1.06 handle, we think it will keep running into good buying demand from European corporates and longer-term investors locking in hedges at attractive levels, acting as a brake on EUR downside. On the central bank side, we expect the ECB to follow its June cut with another cut in September and, assuming the Fed starts cutting in December, to match with a December cut of its own. That would add 50bps to the very front end US-EZ yield differential (140 to 190bps). But that is mostly priced by the relative forward curves. We think the damage would be much greater to a currency like CAD, starting from -30bps in front-end yield gap to the US and, on our forecasts, moving to -105bps. We have nudged down our H2 forecasts for EUR/USD but the changes are marginal (1.06/1.08 to 1.05/1.07). Technically and fundamentally, we see any rallies to resistance (1.0848/1.0977) as buying opportunities. Support comes in at 1.0681 then 1.0601.

6-12 Month Outlook – Flat profile in 2025

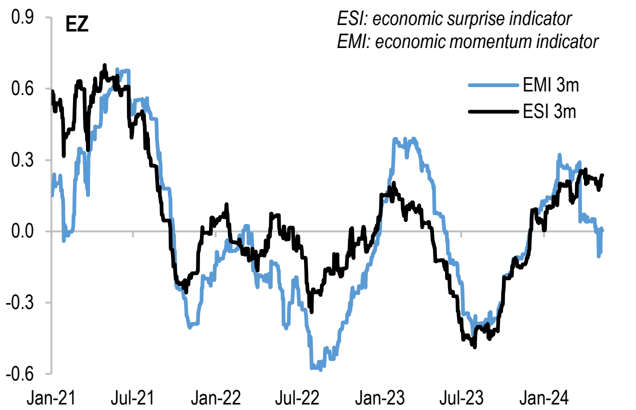
Our long-term outlook is unchanged. Though we see the ECB starting well ahead of the Fed, we do not see them diverging much further than 200bps – not because they cannot but because if the conditions are such that if we see a reacceleration in US inflation, it is likely to spill over to the Euro area too (see our rates team's note on divergence for more). We still think EUR/USD would rally in the event of a US recession, alongside the more traditional havens, JPY and CHF (see more here). In the absence of that, EUR/USD is likely to remain cheap cycling around current levels.

Indicators

	Current (Previous)*
Official cash rate (ECB main refi rate)	**4.50% (4.50%)**
Trend interest rates 10y average	0.8%
Bias in interest rate market	Easing
HICP core Inflation %Y/Y Apr P (Mar)	**2.7% (2.9%)**
Inflation target	2.0% (symmetric)
Budget balance % GDP 2022 (2021)	**-3.6% (-5.2%)**
Budget balance target % GDP	3% of GDP-Unless special circumstances
GDP Growth %Y/Y Q1 A (Q4)	**0.4% (0.1%)**
Trend GDP %y/y	1.5%
Purchasing Power Parity Value Mar	**1.2716**
Spot end-Apr	1.0666
PPP Valuation	EUR/USD is undervalued
Current account % GDP Q4 (Q3)	1.86% (1.23%)
Trend current account balance % GDP	2.2%
Moody's Foreign Currency Rating	**Aaa (Germany)**
Outlook	Stable

* Current is latest month, quarter or year

1. Euro area data beating expectations



Source: RBC Capital Markets, Bloomberg

2. Markets already expecting US outperformance vs EZ

Source: RBC Capital Markets, Bloomberg

Forecasts

	2024				2025			
	Q1	Q2f	Q3f	Q4f	Q1f	Q2f	Q3f	Q4f
EUR/USD	1.08	1.06	1.05	1.07	1.08	1.08	1.09	1.08
EUR/JPY	163	167	168	173	175	173	172	168
EUR/CAD	1.46	1.45	1.45	1.50	1.52	1.53	1.54	1.51

Source: RBC Capital Markets estimates

Japanese Yen

RBC FX Strategy

1-3 Month Outlook – Extremely cheap, but…

There is no doubt that JPY is extremely cheap at current levels. On BIS data, Japan's real effective exchange rate is the weakest it has been since the late 1960s, when Japan's economy was entirely different to what it is today. In nominal terms it is at 34-year lows against USD – though on that kind of horizon, one should really be looking at real rather than nominal measures to understand valuation. But events in the past month have only reinforced the expectation that JPY will stay weak and can weaken further from here. It is now consensus that USD/JPY (and even JPY on the crosses) depends not on the BoJ but on the Fed. On pg 3, we laid out our change of Fed call – we look for the first cut in December, with only two further cuts next year. That feeds through into our USD/JPY forecast. Positioning remains very extended, hovering around 80-90% of the largest net long position of the past 10yrs (Figure 1). But positioning alone cannot reverse USD/JPY. Neither can intervention. On April 29, the BoJ stepped in for the first time since Oct 2022, after USD/JPY briefly traded above 160. The intraday pullback was >3% but it did nothing more than erase JPY losses of the previous trading session. Investors we speak to were hotly anticipating intervention as an opportunity to reload on USD/JPY longs and the heavy flow going through the interbank market on the day (volumes 6x normal) suggests many did just that. Our intervention model finds the best explanation for past behaviour is a combination of the level of USD/JPY and the rate of change. The faster we revisit 160, the more likely it is to prompt intervention. But if USD/JPY grinds higher and US data don't turn lower, we expect USD/JPY will eventually break higher.

6-12 Month Outlook – Highly leveraged to US rates

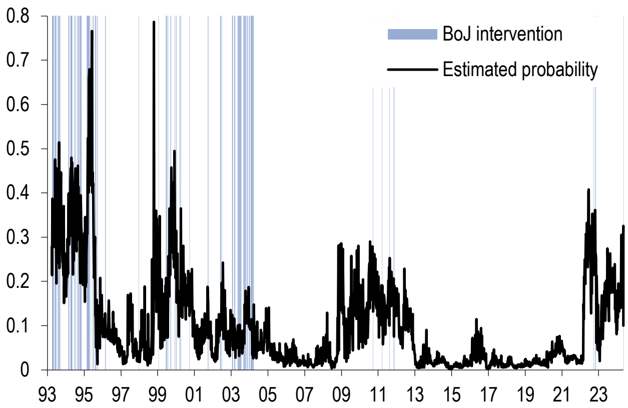
As before, we think the only way for USD/JPY to turn sustainably lower is through exogenous factors – either a sharp slowdown in US data or some other very large (non-inflationary) risk-off shock. Clearly the scale of short JPY positioning puts it at risk for a big short squeeze when that exogenous shock comes along – but that shock has to be large enough to push the Fed to cut rates beyond the -120bps currently priced by end-2025. With -150/-175bps from the Fed, and 30-50bps in hikes from the BoJ, we would be getting to levels where it makes economic sense for Japanese investors to be increasing hedges. Right now our Fed forecast is -75bps by end-2025, which leaves USD/JPY heading higher on our 6-12m forecasts, despite the crowded positioning.

Indicators

	Current (Previous)*
Official cash rate (upper bound)	**0.1%**
Trend interest rates 10y average	-0.1%
Bias in interest rate market	Rising
CPI Inflation %Y/Y Mar (Feb)	**2.7% (2.8%)**
Inflation target	2.0%
Budget balance % GDP 2021 (2020)	**-6.2% (-9.1%)**
Budget balance target % GDP	n/a
GDP Growth %Y/Y Q4 (Q3)	**1.2% (1.6%)**
Trend GDP %Y/Y	0.7%
Purchasing Power Parity Value Mar	**81.38**
Spot end-Apr	157.80
PPP Valuation	USD/JPY is overvalued
Current a/c balance % GDP Q4 (Q3)	3.6% (3.1%)
Trend current account balance % GDP	2.7%
Moody's Foreign Currency Rating	**A1**
Outlook	Stable

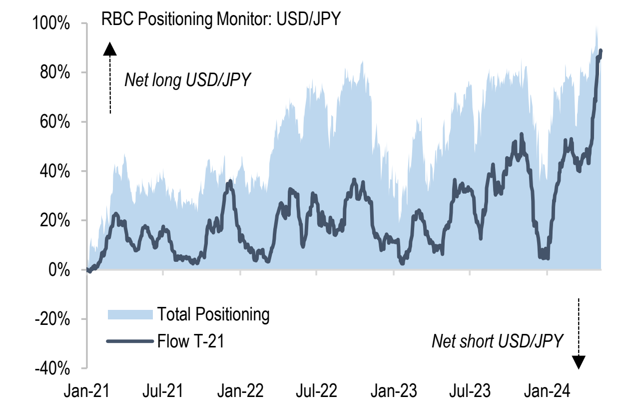
* Current is latest month, quarter or year

1. Tracking JPY intervention risk



Source: RBC Capital Markets, Bloomberg

2. Markets are close to max long USD/JPY



Source: RBC Capital Markets

Forecasts

	2024				2025			
	Q1	Q2f	Q3f	Q4f	Q1f	Q2f	Q3f	Q4f
USD/JPY	151	158	160	162	162	160	158	156
EUR/JPY	163	167	168	173	175	173	172	168
CAD/JPY	112	115	116	116	115	113	112	111

Source: RBC Capital Markets estimates

Sterling

Daria Parkhomenko

1-3 Month Outlook – EUR/GBP profile unchanged

Following its strong performance on the crosses in the first quarter, GBP remained one of the best performers in April, as the relative rate dynamics lent support to the currency (Figure 1). However, as May gets underway, GBP has fallen towards the bottom of the ranks, as UK 2Y yields have seen the largest decline compared to the rest of G10 MTD. Although part of the decline has been in sympathy with the move lower in US yields, the more dovish shift from the BoE at the May MPR meeting also played a role.

On May 9, the BoE signalled that the Bank is getting closer to starting its rate cutting cycle. The voting split showed Deputy Governor Ramsden joining External member Dhingra in voting for a cut, with the other seven members in favor of a hold (prior: 8-1 for a hold). In the press conference, Governor Bailey stated that, "It's likely that we will need to cut bank rate over the coming quarters and make monetary policy somewhat less restrictive over the forecast period, possibly more so than currently priced into market rates". He also indicated that the June meeting was 'live' ("neither ruled out nor a fait accompli"). Although the June meeting is 'live', our economists retain their call for the BoE to start cutting in August and deliver a total of -50bps this year (see here). With markets already pricing a full cut by August and a cumulative -58bps by year-end, we have opted to keep our end-Q2 target for EUR/GBP at 0.85.

6-12 Month Outlook – Limited fiscal headroom

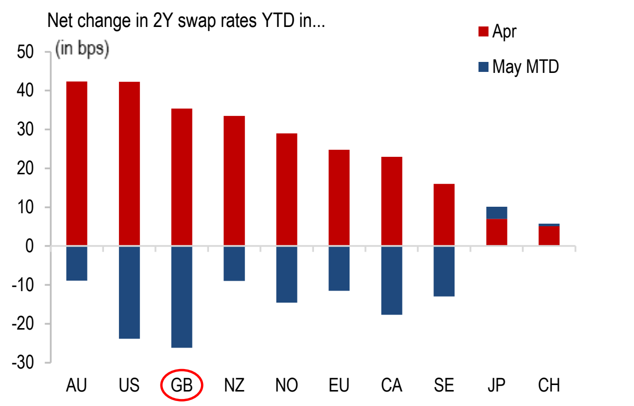
Elections are due by 28 Jan 2025 and it remains widely expected that Labour will be the largest party in Parliament. The factors that would cause material GBP upside, such as single market or customs union membership, do not appear to be in play for the UK on any kind of investable horizon. Fiscally, although concerns have abated since the 2022 Truss/Kwarteng episode, the fiscal backdrop is still constrained, amid a tight spending profile and rising demand for public services, and any deterioration in policy credibility will leave GBP vulnerable. As a result, the incoming government's ability to fight the very negative impulse that the UK faces next year based on current plans will be constrained (Figure 2). We have kept our medium-term EUR/GBP profile unchanged, however, we view the risks skewed to the downside for GBP as long as UK's imbalances continue to require persistent capital inflows and the UK resumes running 'triple' deficits.

Indicators

	Current (Previous)*
Official cash rate	**5.25% (5.25%)**
Trend interest rates 10y average	~1.0%
Bias in interest rate market	Easing
CPI Inflation %Y/Y Mar (Feb)	**3.2% (3.4%)**
Inflation target (HICP)	2.0%
Budget balance % GDP 2022 (2021)	**-4.7% (-7.9%)**
Budget balance target % GDP	Budget surplus as soon as possible
GDP Growth %Y/Y Q1 P (Q4)	**0.2% (-0.2%)**
Trend GDP %Y/Y	1.7%
Purchasing Power Parity Value Mar	**1.3511**
Spot end-Apr	1.2492
PPP Valuation	GBP/USD is undervalued
Current a/c balance sa % GDP Q4 (Q3)	-3.3% (-2.4%)
Trend current account balance % GDP	-3.9%
Moody's Foreign Currency Rating	**Aa3**
Outlook	Stable

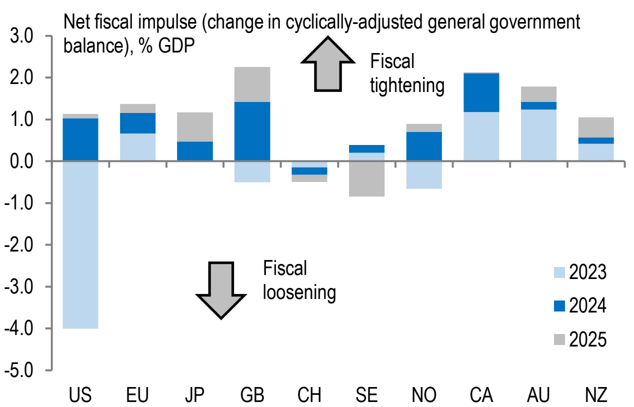
* Current is latest month, quarter or year

1. Relative rate dynamics = key driver of GBP in April-MTD



Source: RBC Capital Markets, Bloomberg

2. UK – expected to be fiscally tightest in 2025



Source: RBC Capital Markets, Bloomberg, national central banks, OECD

Forecasts

	2024				2025			
	Q1	Q2f	Q3f	Q4f	Q1f	Q2f	Q3f	Q4f
GBP/USD	1.26	1.25	1.22	1.23	1.23	1.21	1.21	1.19
EUR/GBP	0.85	0.85	0.86	0.87	0.88	0.89	0.90	0.91
GBP/JPY	191	197	195	199	199	194	191	185
GBP/CAD	1.71	1.71	1.69	1.72	1.73	1.72	1.71	1.66

Source: RBC Capital Markets estimates

Swiss Franc

Elsa Lignos

1-3 Month Outlook – SNB back to intervening

Both USD/CHF and EUR/CHF are exactly where they were a month ago – though both traded higher in the interim and reversed. Technically, the October 2023 high at 0.9244 in USD/CHF serves as important resistance now. Our end-Q2 target is unchanged at 0.92. As noted last month, investors are still likely short CHF against a broad range of high-yielders, though it is not captured by our positioning monitor. But positioning is lighter than it was a few weeks ago – having reached its max ever net long on our AMOS monitor, USD/CHF has retraced to ~75% net long, briefly dipping sub-70% on May 3 (soft US NFP).

Where to from here? The domestic outlook supports CHF lower. While Swiss April CPI surprised to the upside (1.4%y/y, cons 1.1%), the quarter is so far tracking below the SNB's March projection. Inflation is expected to tick a little higher into Q3 2024 (1.5%) but the SNB sees it back at 1.2% through all of 2025 and most of 2026 (Figure 2). It is this sub-target outlook that has prompted the shift to rate cuts and the turnaround in FX policy. Data released for Q1 show all currency holdings bar GBP went up in foreign currency terms (+2.5-14%) so even accounting for some mark-to-market on underlying securities, it is fair to say the SNB was very likely selling CHF and acquiring FX reserves. Outside of Switzerland, the main risk to USD/CHF comes from US data. US CPI on May 15 is the first big test and any signs of US activity data weakening would weigh on USD/CHF and hurt CHF-funded carry trades more generally. We still prefer funding long EM positions in commodity currencies in particular out of high-beta 'medium-yielders' like AUD or CAD. But we think both USD/CHF and EUR/CHF are both likely to head higher in H2, breaking the next resistance levels at 0.9342 and 0.9849 respectively to reach new 12-18m highs. Support in USD/CHF comes in at 0.8995 and 0.8886 while in EUR/CHF it's at 0.9676 and 0.9545.

6-12 Month Outlook – No change in a low vol world

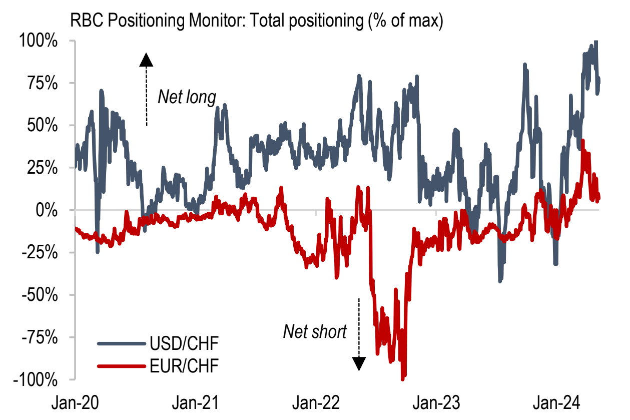
Our medium-term outlook is unchanged. CHF and JPY will likely be the most efficient funding currencies 6m forward based on current curve pricing. The longer that lasts, the more short CHF is at risk of a big squeeze if something happens to kill the carry trade (exogenous risk off shock or sharp global slowdown). But the longer we remain in a low vol environment, the more CHF will keep grinding lower.

Indicators

	Current (Previous)*
Official cash rate	**1.50% (1.75%)**
Trend interest rates average	-0.09%
Bias in interest rate market	Easing
CPI Inflation %Y/Y Apr (Mar)	**1.4% (1.0%)**
Inflation target	less than 2.0%
Budget balance % GDP 2022 (2021)	**1.2% (-0.3%)**
Budget balance target % GDP	Balanced over the business cycle
GDP Growth %Y/Y Q4 (Q3)	**0.6% (0.4%)**
Trend GDP %Y/Y	1.8%
EUR Purchasing Power Parity Value Mar	**1.0650**
EUR/CHF spot end-Apr	0.9807
EUR/CHF PPP Valuation	EUR/CHF is undervalued
Current a/c balance % GDP Q4 (Q3)	7.6% (7.4%)
Trend current account balance % GDP	6.5%
Moody's Foreign Currency Rating	**Aaa**
Outlook	Stable

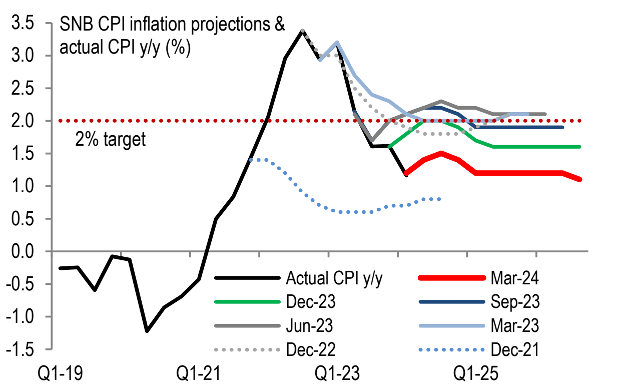
* Current is latest month, quarter or year

1. Some lightening up in long USD/CHF (now ~75% of max)



Source: RBC Capital Markets

2. Inflation seen well below target throughout forecast



Source: Bloomberg, SNB, RBC Capital Markets

Forecasts

	2024				2025			
	Q1	Q2f	Q3f	Q4f	Q1f	Q2f	Q3f	Q4f
USD/CHF	0.90	0.92	0.95	0.95	0.96	0.98	0.99	1.02
EUR/CHF	0.97	0.98	1.00	1.02	1.04	1.06	1.08	1.10
CHF/JPY	168	171	168	170	168	163	159	153
CAD/CHF	0.67	0.67	0.69	0.68	0.68	0.69	0.70	0.73

Source: RBC Capital Markets estimates

Swedish Krona & Norwegian Krone

Gordon Scott

Swedish Krona – The Riksbank's balancing act

The much-anticipated May Riksbank meeting saw the Swedish central bank begin to lower interest rates, delivering a 25bp rate cut. At the March MPR the Riksbank had indicated that a start to the rate cutting cycle was likely either in May or June, and the analyst consensus (which was split 13-7 in favour of rate cut) suggested that this month's meeting was seen as a close decision. The Riksbank's decision to lower interest rates was spurred by a lower than expected March inflation reading with headline CPIF inflation at 2.2% y/y well below the Riksbank's baseline forecast of 2.7% y/y (see Exhibit 1). The downside surprise to inflation, coupled with a repricing of interest rate expectations led SEK to underperform many of its peers over the course of the month with EUR/SEK 1% higher compared to the start of April. The weakness in the Swedish Krona this year has not gone unnoticed by the Riksbank which noted in its decision statement the upside risks this poses to inflation as one of the factors motivating caution in terms of the pace of future rate cuts (mkt pricing: -45bps by year-end). The Riksbank's sensitivity to the exchange rate may serve to limit the weakness in the Krona, although with EUR/SEK below the highs reached last year there remains some scope for a near-term softening in SEK.

Norwegian Krone – A later start to rate cuts

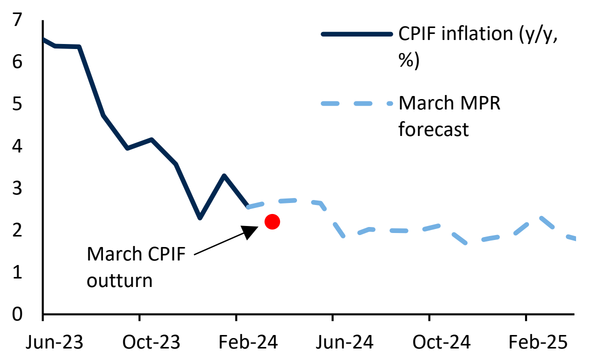
Continuing the trend seen since the start of the year NOK spent much of April on the back foot with EUR/NOK reaching as high as 11.85 by the end of the month. This weakness in NOK reflected a combination of a lower than expected March inflation release, a softer tone for risky assets and lower oil prices, even if NOK's beta to the latter has reduced of late (see Exhibit 2). The start of May, however, has seen a partial reversal of the weakness in NOK with the moves aided by the modestly hawkish tone of the May Norges Bank meeting. At its meeting last week Norges Bank indicated *"The data so far could suggest that a tight monetary policy stance may be needed for somewhat longer than previously envisaged."* Norges Bank had previously suggested policy rates would remain unchanged until the autumn, implying even before last week's meeting a later start to rate cuts than the ECB (which is likely to deliver its first rate cut in June). Looking ahead the divergence between Norges Bank and the ECB may lend a positive bias to NOK, although the currency remains highly levered to developments in oil prices and global risk sentiment.

Indicators - Sweden

	Current (Previous)*
Official cash rate	**3.75% (4.00%)**
Trend interest rates 10y average	0.39%
Bias in interest rate market	Cutting
CPIF Inflation %Y/Y Mar (Feb)	**2.2% (2.5%)**
Inflation target (UND1X)	2.0%
Budget balance % GDP 2023 (2022)	**-0.6% (1.2%)**
Budget balance target % GDP	Cyclical avg. surplus of 0.33%
GDP Growth %Y/Y Q1 (Q4)	**-1.1% (0.0%)**
Trend GDP %Y/Y	2.1%
EUR Purchasing Power Parity Value Mar	**9.4795**
Spot end-Apr	11.7583
PPP Valuation	EUR/SEK is overvalued
Current a/c balance % GDP Q4 (Q3)	7.4% (7.1%)
Trend current account balance % GDP	4.5%
Moody's Foreign Currency Rating	**Aaa**
Outlook	Stable

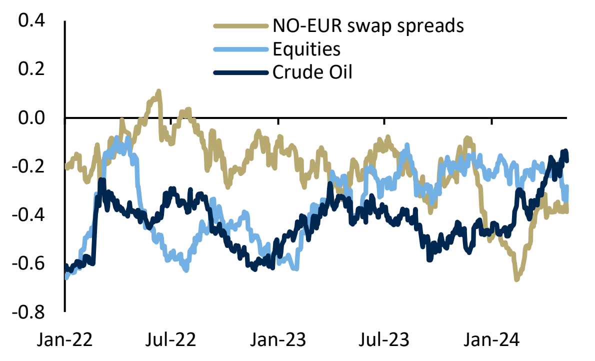
* Current is latest month, quarter or year

1. Swedish inflation – outturn vs March MPR (y/y, %)



Source: RBC Capital Markets, Riksbank, Haver

2. 3m rolling correlations with EUR/NOK



Source: RBC Capital Markets, Bloomberg

Forecasts

	2024				2025			
	Q1	Q2f	Q3f	Q4f	Q1f	Q2f	Q3f	Q4f
EUR/SEK	11.50	11.80	11.70	11.60	11.50	11.40	11.30	11.20
EUR/NOK	11.68	11.70	11.55	11.40	11.30	11.20	11.10	11.00
NOK/SEK	0.98	1.01	1.01	1.02	1.02	1.02	1.02	1.02
CAD/SEK	7.87	8.13	8.05	7.74	7.55	7.43	7.35	7.41

Source: RBC Capital Markets estimates

Canadian Dollar

Daria Parkhomenko

1-3 Month Outlook – BoC to start cutting in June

In April, USD/CAD rallied ~1.8%, amid a higher USD, lower US equities, and the 2Y US-CA rates spread widening against CAD, with this backdrop leaving CAD mixed on the crosses. As we go to press, CAD is one of main underperformers MTD amid USD weakness and Canada seeing one of the larger declines in 2Y yields in G10. In the short-term, the domestic focus will be on April CPI on May 21, which will be the key input into the BoC's June 5 meeting. Our rates team thinks if the CPI-trim & -median measures print below 0.3%m/m on average, then our base case for a June BoC cut is likely to materialize; otherwise, the BoC may wait until the July MPR meeting (mkt: -10bps by June & -25bps by July). There is also Q1 GDP on May 31st, but that is likely to play a secondary role. A BoC June rate cut is not fully priced and that may serve as a small headwind to CAD. However, we think tactically USD/CAD faces asymmetric downside risk if US economic data disappoint or Canadian data surprise to the upside. Hence, our end-Q2 target at 1.37 is unchanged.

6-12 Month Outlook – Raising USD/CAD profile

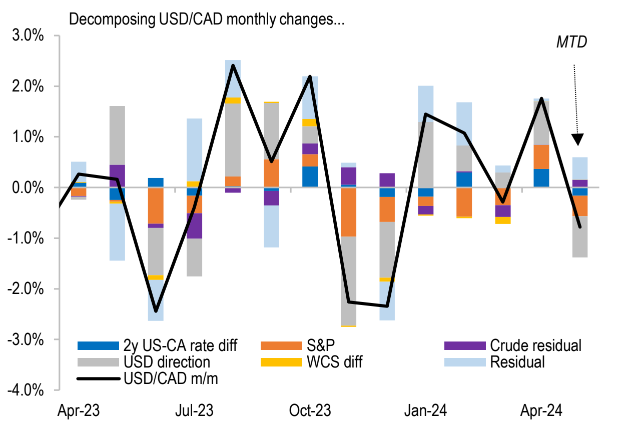
We have raised our longer-term profile for USD/CAD again. Although our broader USD view is unchanged (see pg. 3), our prior forecasts did not sufficiently account for the US-CA policy divergence story. On April 10, our US rates team adjusted their Fed call to one 25bp cut from a total of -75bps this year and kept -50bps for 2025. Meanwhile, our CA economists still see the BoC delivering four consecutive cuts this year and another -100bps next year, with the risk biased to fewer and/or later rate cuts. This would result in the US-CA policy rate gap widening from the current +38bps to +113bps by year-end and +163bps by end-2025. This gap may look wide, but this would not be unprecedented (e.g. -225bps in 2003 & +100bps in 2006/07). More importantly, the Canadian macro story relative to that of the US supports the BoC delivering a more aggressive rate cutting cycle than the Fed. This includes downside surprises in Canada's CPI-trim & -median metrics, the labour market easing, and Q1 GDP tracking the 7th quarterly decline on a per-capita basis. As noted by our CA rates team, the key factors that would prevent the BoC from cutting so much relative to the Fed would be stronger than expected CA data, a meaningful recovery in CA housing activity, Fed hikes, a significant & sustained commodity price shock, and/or pronounced CAD weakness (see here). Incorporating our analysis on US-CA policy divergence, we now see an uptrend in USD/CAD into year-end. A key downside risk would be a material slowdown in the US that results in more significant Fed cuts.

Indicators

	Current (Previous)*
Official cash rate	**5.00% (5.00%)**
Trend interest rates 10y average	1.4%
Bias in interest rate market	Easing
Core CPI Inflation (Trim) %Y/Y Mar (Feb)	**3.1% (3.2%)**
CPI inflation target range %Y/Y	1-3%
Budget balance % GDP 2023 (2022)	**-1.2% (-3.2%)**
Budget balance target % GDP	Declining over the business cycle
GDP growth %Q/Q saar Q4 (Q3)	**1.0% (-0.5%)**
Trend GDP %Q/Q	2.1%
Purchasing Power Parity value Mar	**1.2091**
Spot end-Apr	1.3778
PPP valuation	USD/CAD is overvalued
Current account balance % GDP Q4 (Q3)	**-0.6% (-0.9%)**
Trend current account balance % GDP	-2.0%
Moody's foreign currency rating	**Aaa**
Outlook	Stable

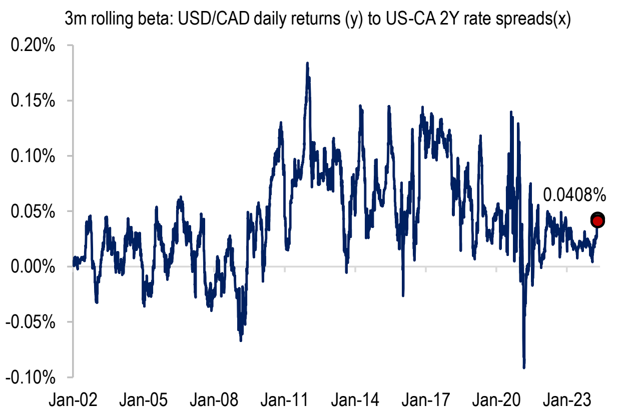
* Current is latest month, quarter or year

1. April rally can be fully explained by underlying variables



Source: Bloomberg, RBC Capital Markets

2. USD/CAD's elasticity to rate spreads has picked up



Source: Bloomberg, RBC Capital Markets

Forecasts

	2024				2025			
	Q1	Q2f	Q3f	Q4f	Q1f	Q2f	Q3f	Q4f
USD/CAD	1.3540	1.3700	1.3850	1.4000	1.4100	1.4200	1.4100	1.4000
EUR/CAD	1.46	1.45	1.45	1.50	1.52	1.53	1.54	1.51
CAD/JPY	112	115	116	116	115	113	112	111

Source: RBC Capital Markets estimates

Australian Dollar

Alvin T. Tan

1-3 Month Outlook – Limited upside potential

Australia's domestic demand has cooled following the RBA's tightening cycle. More importantly, inflation pressures have stayed elevated even if they have peaked. This leads to our baseline expectation of the RBA holding rates steady this year. In this light, the RBA is expected to lag both the Fed and the ECB in the timing of its first rate cut, though the USD will retain a decent carry advantage.

Meanwhile, iron ore prices have rebounded strongly in the past month and are fluctuating in the upper-end of the 5-year range. Australia is the second largest LNG exporter in the world, ahead of Qatar, and the export price of its LNG exports has also been firmer lately. Moreover, Australia's trade relations with China have improved significantly in the past year. With China's economy on a firmer footing this year, the direction of risks from AUD's macro exposure to China is turning more positive.

Over the past few quarters, the AUD/USD spot rate has been driven heavily by the US dollar's broad fluctuations. Given the expectation of a generally resilient US dollar, a patient RBA, and mixed impact from China, AUD/USD is likely to continue fluctuating in sideways fashion with a mild downside bias in coming months.

The Aussie dollar, however, retains a clear negative correlation to the MSCI World Index, indicating that it remains a relatively pro-risk currency. Thus, near-term downside risks for the currency could surge if global risk sentiment stumbles.

6-12 Month Outlook – Potential upside if China's recovery accelerates

Australia's external balance has improved structurally in recent years, turning it into a persistent current account surplus country. It is also no longer an obviously "high carry" currency relative to other G10 currencies. Nonetheless, AUD remains sensitive to global risk sentiment, and it is difficult to see this changing in the coming year.

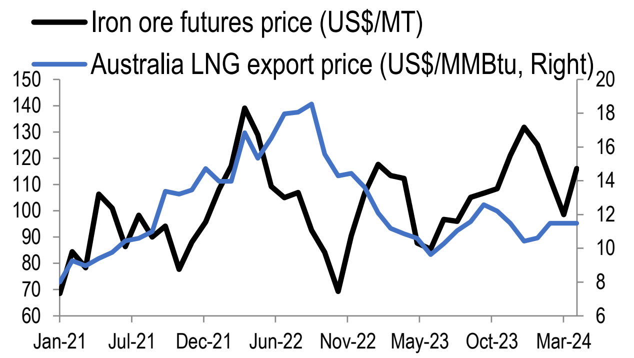
The Aussie will likely outperform the euro, but it is unlikely to demonstrate unilateral strength against the dollar. There is a potential strong upside risk for AUD if China's economy revives strongly, but this is not a baseline scenario.

Indicators

	Current (Previous)*
RBA cash rate	**4.35%**
Trend interest rates (10yr average)	1.60%
Bias in interest rate market	Higher
CPI Inflation %Y/Y last (prev)	**3.6% (4.1%)**
Inflation target	2.0-3.0%
Budget balance % GDP last (prev)	**1.6% (1.4%)**
Budget balance trend % GDP	-1.7%
GDP Growth % y/y last (prev)	1.5% (2.1%)
Trend GDP %y/y	2.4%
Purchasing Power Parity Value Q1	**0.7257**
Spot end-Apr	0.6473
PPP valuation	AUD/USD is undervalued
Current acct balance % GDP last (prev)	**1.2% (1.2%)**
Trend current account balance % GDP	-1.2%
Moody's Foreign Currency Rating	**Aaa**
Outlook	Stable

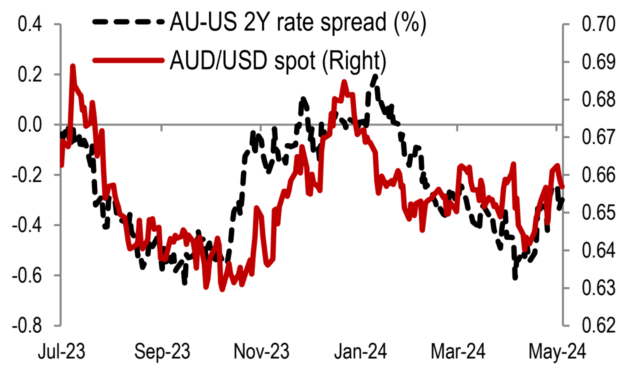
* Current is latest month, quarter or year

1. Firming key commodity export prices lately



Source: RBC Capital Markets; Bloomberg

2. USD's rate advantage will limit AUD/USD gains



Source: RBC Capital Markets; Bloomberg

Forecasts

	2024				2025			
	Q1	Q2f	Q3f	Q4f	Q1f	Q2f	Q3f	Q4f
AUD/USD	0.65	0.64	0.65	0.66	0.67	0.67	0.68	0.68
EUR/AUD	1.65	1.66	1.62	1.62	1.61	1.61	1.60	1.59
AUD/CAD	0.88	0.88	0.90	0.92	0.94	0.95	0.96	0.95

Source: RBC Capital Markets estimates

Chinese Yuan

Alvin T. Tan

1-3 Month Outlook – Economy finding its footing

China's economy appears to be gaining a firmer footing in recent months. The year's GDP growth target of "around 5%" will still require further stimulus measures to achieve. The April politburo statement has ignited speculation that further supportive measures will indeed be forthcoming, particular for the moribund real estate sector.

Falling housing prices nonetheless continue to dampen consumer sentiment and activity, despite a steady drip of targeted support measures through the past year. On the other hand, the exports slump appears to be ending. Foreign investors have also turned more cautiously optimistic, with renewed net capital inflows into local bonds and equities recently.

Additional RRR and interest rate cuts are likely in coming months. The USD should thereby continue to enjoy a significant carry premium over CNY. However, the PBOC has also revealed its determination to cap USD/CNY under ~7.33 through its persistently below-expectations USD/CNY reference rates. It is clear that policymakers are intensely concerned about the bilateral USD/CNY exchange rate.

The PBOC's tight management of the exchange rate has suppressed the renminbi's volatility. The currency has thus become a poor vehicle for expressing a bearish China macro view. It is difficult to see the implicit USD/CNY cap breaking in coming months without a strong across-the-board US dollar upsurge that takes the DXY Index well through 107.

6-12 Month Outlook – Determined cap on USD/CNY

China's multi-year property and construction boom has ended definitively, and policymakers are unwilling to reflate it. The fallout is likely to last for years, and there is no easy alternative driver of the economy at hand. Although Beijing continues to evince an aversion to large-scale fiscal stimulus, targeted support measures are gradually adding up. They should be enough to keep a floor on economic growth.

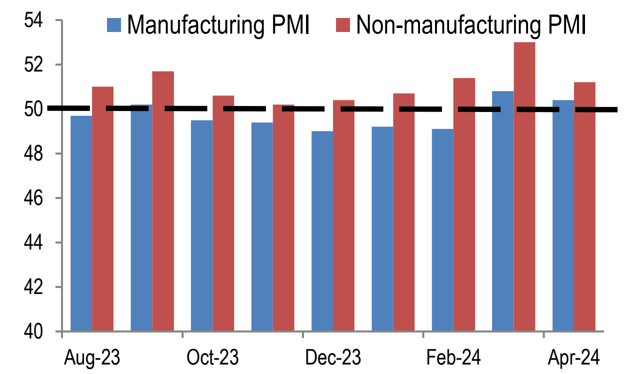
Weak domestic demand and low local interest rates present major headwinds for the yuan. On the flipside is the apparent determination to cap upside risks in the bilateral USD/CNY exchange rate, possibly on the fear that further depreciation could unleash large capital outflows similar to what occurred in 2015-2016.

Indicators

	Current (Previous)*
China 1-year loan prime rate	**3.45%**
Trend interest rates (10yr average)	3.88%
Bias in interest rate market	Lower
CPI Inflation %Y/Y last (prev)	**0.1% (0.7%)**
Inflation target	3.0%
Budget balance % GDP last (prev)	**-4.6% (-4.7%)**
Budget balance trend % GDP	-3.1%
GDP Growth % y/y last (prev)	5.3% (5.2%)
Trend GDP %y/y	5.0%
Purchasing Power Parity Value Mar	**6.7627**
Spot end-Apr	7.2410
PPP valuation	USD/CNY is overvalued
Current acct balance % GDP last (prev)	**1.5% (1.8%)**
Trend current account balance % GDP	1.6%
Moody's Foreign Currency Rating	**A1**
Outlook	Stable

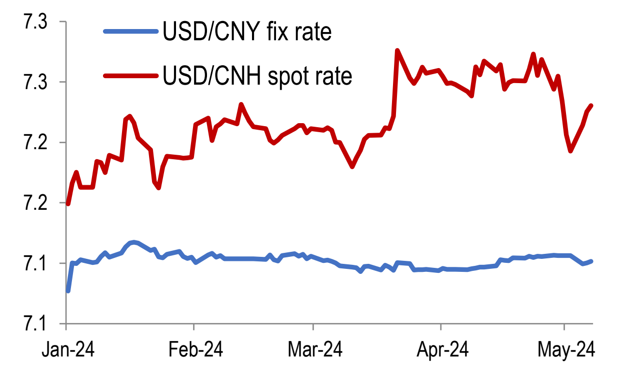
* Current is latest month, quarter or year

1. Economic activity has firmed up in recent months



Source: RBC Capital Markets; Bloomberg

2. PBOC continues to restrain USD/CNY



Source: RBC Capital Markets; Bloomberg

Forecasts

	2024				2025			
	Q1	Q2f	Q3f	Q4f	Q1f	Q2f	Q3f	Q4f
USD/CNY	7.22	7.26	7.32	7.30	7.30	7.28	7.28	7.27
EUR/CNY	7.79	7.70	7.69	7.81	7.88	7.86	7.94	7.85
CNY/JPY	21.0	21.8	21.9	22.2	22.2	22.0	21.7	21.5
CAD/CNY	5.33	5.30	5.29	5.21	5.18	5.13	5.16	5.19

Source: RBC Capital Markets estimates

South Korean Won

Alvin T. Tan

1-3 Month Outlook – Dominated by external factors

The outlook for South Korea's trade-dependent economy has brightened this year. The Bank of Korea is on an extended pause, and the exports cycle appears to have turned for the better. The trade balance has been in a persistent surplus since June 2023, and monthly exports have marked sixth consecutive positive year-on-year growth readings.

Semiconductors are a mainstay of the Korean economy, and the global semiconductor cycle is on an upturn, though still uneven. Local equities have enjoyed sizeable net foreign portfolio inflows in recent months amid the global tech-driven equity rally. The won, however, has not benefitted at all, with the USD/KRW exchange rate continuing to be bedevilled by its high beta to the broad US dollar, plus the uptrend in USD/JPY.

Persistent downside pressures on the neighbouring JPY and, to a lesser extent, CNY are clearly exerting a major drag on the won. South Korea shares significant export complementarities with Japan, and so it's no surprise that the yen's weakness has affected the won.

There are also domestic financial stability concerns in the local credit market caused by a combination of elevated interest rates, high debt levels and weak property sector. Given the various cross-currents, the won is likely to underperform among the Asia FX complex in coming weeks.

6-12 Month Outlook – Cheap amid uncertainties

The won's persistent weakness in 2021 and 2022 has rendered it relatively cheap. Although some the macro headwinds from then have faded, the won remains a hostage to external factors. A more positive cycle for the won will have to await the start of Fed rate cuts.

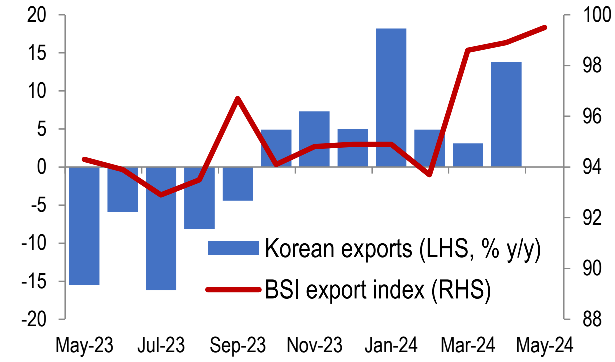
Even then, we need to be mindful of remaining deep macro uncertainties that could hinder any potential KRW uptrend. First are uncertainties about the state of global demand given the Korean economy's heavy export-dependence. Heightened geopolitical concerns in the Korean peninsula is another potential risk factor. Finally, a potential Trump election victory and the related risk of higher US trade tariffs could also weigh on the won.

Indicators

	Current (Previous)*
BOK Base Rate	**3.50%**
Trend interest rates (10yr average)	1.68%
Bias in interest rate market	Lower
CPI Inflation %Y/Y last (prev)	**2.9% (3.1%)**
Inflation target	2.0%
Budget balance % GDP last (prev)	**-1.8% (-0.3%)**
Budget balance trend % GDP	1.3%
GDP Growth % y/y last (prev)	3.4% (2.2%)
Trend GDP %y/y	2.5%
Purchasing Power Parity Value Mar	**1052**
Spot end-Apr	1382
PPP valuation	USD/KRW is overvalued
Current acct balance % GDP last (prev)	**2.1% (1.1%)**
Trend current acct. balance % GDP	5.0%
Moody's Foreign Currency Rating	**Aa2**
Outlook	Stable

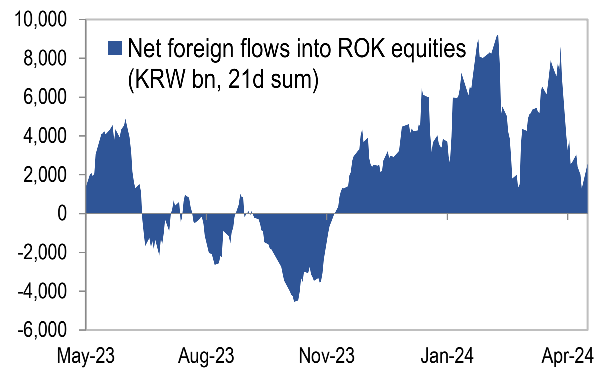
* Current is latest month, quarter or year

1. Cyclical exports upturn



Source: RBC Capital Markets; Bloomberg

2. Strong net equity inflows since late 2023



Source: RBC Capital Markets; Bloomberg

Forecasts

	2024				2025			
	Q1	Q2f	Q3f	Q4f	Q1f	Q2f	Q3f	Q4f
USD/KRW	1347	1390	1420	1400	1400	1390	1370	1350
EUR/KRW	1454	1473	1491	1498	1512	1501	1493	1458
JPY/KRW	8.9	8.8	8.9	8.6	8.6	8.7	8.7	8.7
CAD/KRW	995	1015	1025	1000	993	979	972	964

Source: RBC Capital Markets estimates

Singaporean Dollar

Alvin T. Tan

1-3 Month Outlook – Supported by existing policies

Singapore's inflation readings were choppy in Q1, but continue to slide generally. They are likely to stay volatile in Q2 2024 from the sales tax hike and fluctuating COE prices. The regional exports cycle upturn has also improved the domestic growth outlook, and hence undercut any urgency to ease monetary policy.

Moreover, Singapore is less exposed to China's economy compared to South Korea and Taiwan, so it has been less negatively affected from that angle. The situation should encourage the MAS to maintain the existing currency appreciation settings through the course of 2024.

The trade-weighted SGD's estimated 1.5% annualised appreciation path has and should continue to support further gradual gains in SGD against its main trading partners' currencies. The MAS' trade-weighted SGD index in fact has been trading consistently above the estimated mid-point of the currency band for over two years. SGD's performance since mid-2023 has also consistently placed it among the top half of the Asia FX basket, further underscoring its stable positive performance.

That said, the bilateral USD/SGD exchange rate evinces a consistent high positive correlation to the DXY Index, so it is sensitive to broad US dollar direction. In this light, the range-bound USD/SGD rate is likely to remain so in coming months given the expected resiliency of the US dollar.

6-12 Month Outlook – Valuation getting stretched

The trade-weighted SGD's consistent appreciation in recent years has rendered it relatively expensive among Asian currencies. It would probably require both the start of Fed and MAS policy easing to reverse the currency's valuation. The MAS is unlikely to start easing this year, so the Singapore dollar is likely to remain resilient among Asian currencies.

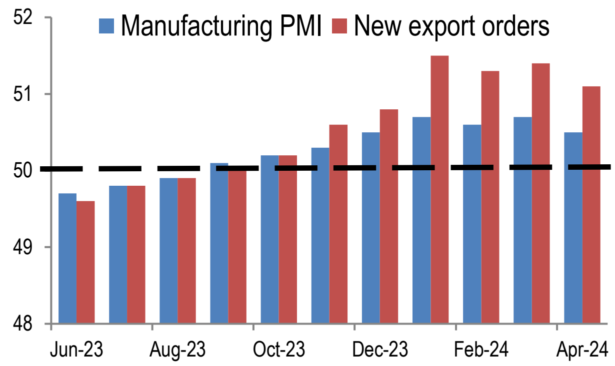
The growing attractiveness of Singapore as an Asian wealth and financial hub also suggests a structural tailwind for SGD. Moreover, the persistently large current account surplus offers robust fundamental support to the currency.

Indicators

	Current (Previous)*
Estimated SGD NEER annual appreciation	**1.5%**
Bias in policy expectations	Flat
CPI Inflation %Y/Y last (prev)	**2.7% (3.4%)**
Inflation target	None
Budget balance % GDP last (prev)	**-0.8% (-1.5%)**
Budget balance trend % GDP	-0.5%
GDP Growth % y/y last (prev)	2.7% (2.2%)
Trend GDP %y/y	3.2%
Purchasing Power Parity Value Mar	**1.3435**
Spot end-Apr	1.3655
PPP valuation	USD/SGD is overvalued
Current account balance % GDP last (prev)	**19.8% (18.5%)**
Trend current account balance % GDP	17.4%
Moody's Foreign Currency Rating	**Aa3**
Outlook	Stable

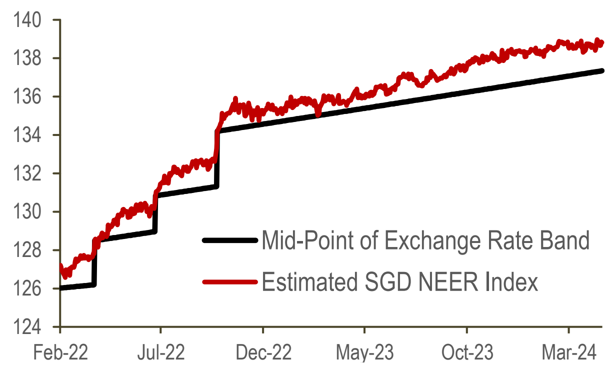
* Current is latest month, quarter or year

1. Growth conditions have improved in recent months



Source: RBC Capital Markets; Bloomberg

2. Trade-weighted SGD continues to be supported by MAS' appreciation settings



Source: RBC Capital Markets

Forecasts

	2024				2025			
	Q1	Q2f	Q3f	Q4f	Q1f	Q2f	Q3f	Q4f
USD/SGD	1.35	1.36	1.37	1.36	1.36	1.35	1.34	1.33
EUR/SGD	1.46	1.44	1.44	1.46	1.47	1.46	1.46	1.44
SGD/JPY	112.2	116.2	116.8	119.1	119.1	118.5	117.9	117.3
CAD/SGD	1.00	0.99	0.99	0.97	0.96	0.95	0.95	0.95

Source: RBC Capital Markets estimates

Malaysian Ringgit

Alvin T. Tan

1-3 Month Outlook – Positive factors in short supply

Malaysia's economy is meandering along, though the weakness in industrial activity is gradually receding. The country's manufacturing PMI nonetheless has been running below the 50 expansion-contraction threshold for twenty consecutive months. Local bond yields are relatively mediocre, and below US yields across the curve.

MYR has also been bedevilled by net foreign equity portfolio outflows for much of the past year, with an especially sizeable outflow in recent months. It is clear that Bank Negara's policy tightening has ended, and it is unwilling to raise rates just to defend the currency. Without an exciting growth story, Malaysia's financial assets will struggle to generate significant interest from global investors.

Moreover, Malaysia's coalition government remains fragile politically, making it challenging to undertake needed but difficult structural reforms to shrink the persistent fiscal deficit and boost the country's growth potential. The government's plan to rationalise subsidies, which are a huge fiscal drain, will likely continue to be slow to be implemented.

On the positive side, the prices of key commodity exports of oil & gas and palm oil have been rising in recent months. The general exports outlook is also brightening. Another is Malaysia's attractiveness for foreign direct investors seeking "supply-side diversification". But in none of these macro themes is the ringgit the top global EM FX trade.

6-12 Month Outlook – Cheap valuation awaiting a catalyst

The main fundamental positive factor for the ringgit is that it is cheap on a number of long-term valuation metrics. The ringgit is among the cheapest Asian currencies according to the famous "Big Mac Index" for example. Malaysia's trade balance is also expected to stay positive this year and next.

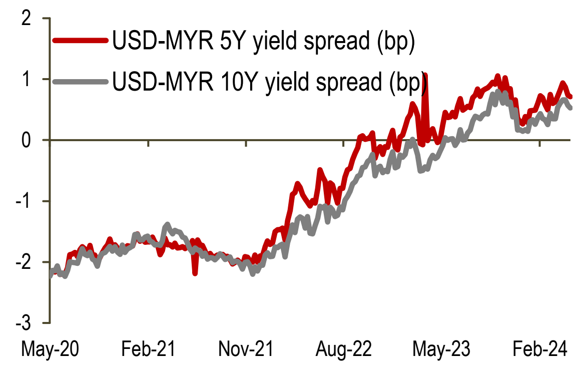
The currency, however, still awaits a catalyst to reverse its cheapness. Malaysia's interest rates continue to lag US ones and those of several of its Asian peers. Plus, there is an abiding question mark about the stability of the current coalition government.

Indicators

	Current (Previous)*
BNM official overnight rate	**3.00%**
Trend interest rates (10yr average)	2.80%
Bias in interest rate market	Lower
CPI Inflation %Y/Y last (prev)	**1.8% (1.8%)**
Inflation target	None
Budget balance % GDP last (prev)	**-5.4% (-5.2%)**
Budget balance trend % GDP	-4.2%
GDP Growth % y/y last (prev)	3.9% (3.0%)
Trend GDP %y/y	4.0%
Purchasing Power Parity Value Mar	**2.9282**
Spot end-Apr	4.7725
PPP valuation	USD/MYR is overvalued
Current acct bal % GDP last (prev)	**1.3% (2.8%)**
Trend current acct balance % GDP	3.7%
Moody's Foreign Currency Rating	**A3**
Outlook	Stable

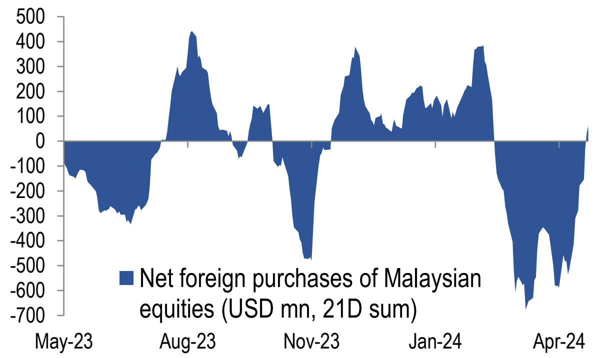
* Current is latest month, quarter or year

1. Fundamental pressure from rate disadvantage



Source: RBC Capital Markets; Bloomberg

2. Large outflows from local equities in March-April



Source: RBC Capital Markets; Bloomberg

Forecasts

	2024				2025			
	Q1	Q2f	Q3f	Q4f	Q1f	Q2f	Q3f	Q4f
USD/MYR	4.73	4.80	4.85	4.83	4.81	4.79	4.77	4.75
EUR/MYR	5.10	5.09	5.09	5.17	5.19	5.17	5.20	5.13
MYR/JPY	32.0	32.9	33.0	33.5	33.7	33.4	33.1	32.8
CAD/MYR	3.49	3.50	3.50	3.45	3.41	3.37	3.38	3.39

Source: RBC Capital Markets estimates

Brazilian Real

Luis Estrada

Global Developments – When it Rains, it Pours.

April witnessed significant global market volatility due to various unexpected geopolitical and economic events:
- US CPI release (April 10): The release of March's CPI data raised concerns about the Federal Reserve's ability to adjust interest rates in June.

- Israeli Airstrikes in Iran (April 17): These geopolitical tensions added to an already volatile environment.
-Japanese Yen Intervention (April 29 and May 3rd): The intervention followed the Yen reaching a high of 160, affecting the forex markets worldwide.

These incidents led to increased market uncertainties, forcing investors to reassess their EM strategies and risk.

1-3 Month outlook – It is a fluid situation

Brazil's economic scenario has been influenced by both external and significant domestic events:

- Before the US CPI data release, BRL was already under pressure, with USD/BRL trading above 5.00 (see Figure 2).

- On April 15th, President Lula's economic team shifted the primary surplus target for 2025 from 0.5% to flat, fueling criticisms of the new fiscal rules.
- In quick response to heightened global and fiscal risks, Brazil Central Bank withdrew its earlier easing guidance.

- Last Sunday, Rio Grande do Sul, was hit by a Major flood.

In the short term, Brazil faces increased fiscal and monetary challenges: This week Finance Minister Haddad announced a relief package estimated ~8.9bn USD after President Lula signed a decree exempting emergency relief from the 2024 fiscal rules. The short-term performance of BRL will depend on how these measures are structured and what monetary policy strategy the BCB takes to defend its inflation target.

6-12 Month Outlook – Adjusting expectations

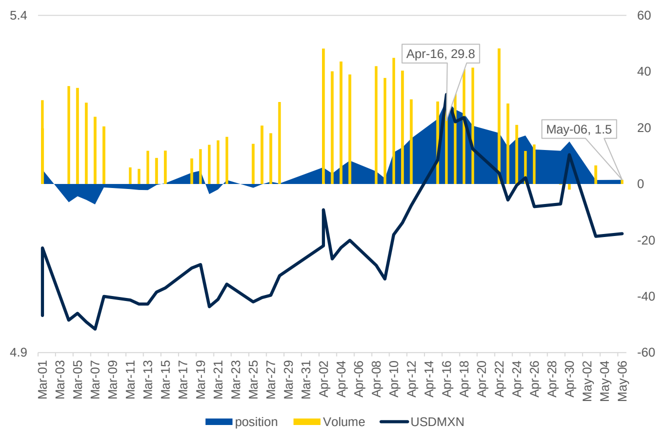
The long-term performance of BRL will hinge on governance. The effectiveness of the BCB's monetary policy and the government's ability to manage fiscal pressures will be crucial. The upcoming appointment of a new Central Bank Governor in 2025 will shape BCB's future credibility. This has forced us to raise our USD/BRL forecasts for the end of 2024, slightly to 4.80 allowing for this story to develop.

Indicators

	Current (Previous)*
Official cash rate	10.50
O/N interest rates (10yr avg)	8.57
Bias in interest rate market	Lower
IPCA Inflation %Y/Y (Previous)	3.69% (4.50%)
Inflation target	3.0% in 2024
Budget balance % GDP (Previous)	-6.8%(-8.4%)
Budget balance target % GDP	-
GDP Growth % y/y (24E) **(Previous)**	1.7% (2.9%)
Trend GDP %y/y(10yr avg)	0.56%
Purchasing Power Parity Value Mar	3.59
Spot end-Apr	5.19
PPP Valuation	USD/BRL is overvalued
Current account balance % GDP('24 ('23))	-0.9%(-0.9%)
Trend current acct balance % GDP(10y avg)	-1.09%
Moody's Foreign Currency Rating	Ba2
Outlook	Positive

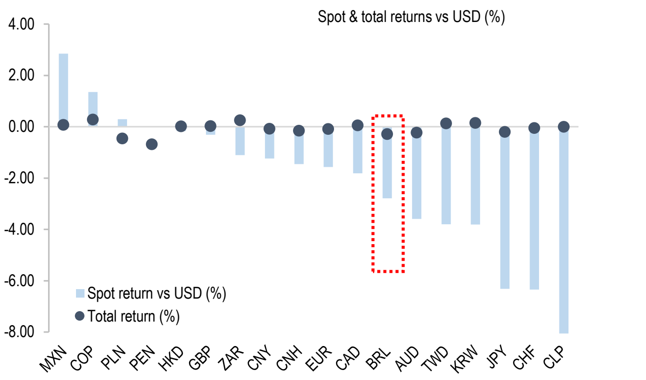
* Current is latest month, quarter, or year

1. RBC Positioning Monitor market closed long USD/BRL



Source: RBC Capital Markets; Note: USDBRL positioning in blue

2. Returns 2024 until April 1st – BRL lagging MXN & COP



Source: Bloomberg, RBC Capital Markets

Forecasts

	2024				2025			
	Q1	Q2f	Q3f	Q4f	Q1f	Q2f	Q3f	Q4f
USD/BRL	5.01	5.05	4.95	4.80	4.80	4.78	4.80	4.85
EUR/BRL	5.41	5.35	5.20	5.14	5.18	5.16	5.23	5.24
BRL/JPY	30.2	31.3	32.3	33.8	33.8	33.5	32.9	32.2
CAD/BRL	3.70	3.69	3.57	3.43	3.40	3.37	3.40	3.46

Source: RBC Capital Markets estimates

Mexican Peso

Luis Estrada

1-3 Month Outlook – April's volatility impact on MXN

The Mexican Peso (MXN) faced significant volatility in April due to the sharp reaction of U.S. Treasury yields to the US CPI release and the equity market's reaction to the Israeli attack on Iran. This dual shock spiked historical volatility to double digits, triggering stop-loss orders in MXN and creating a snowball effect that drove the MXN to 18.20 overnight, clearing the technical positions. According to the RBC Positioning report, there was a significant shift from 51% short USD/MXN to 13% short at the most extreme level (see Figure 1).

Realized volatility in MXN spiked to 14% but has since returned to single digits. Many foreign exchange carry trades were impacted by contamination from duration in the market, although MXN has mostly correlated with "risk-on" and "risk-off" sentiment. Notably, the day Apple reported earnings—which set a floor in the S&P 500 after 2-year U.S. Treasury yields found resistance at a 5% yield and JPY intervention capped the USD/JPY at 160—the price action of MXN changed for the better.

The near-term outlook is influenced by light positioning in MXN and improved entry levels, making MXN an attractive candidate for carry trades going into the summer. The upcoming Presidential Election on June 2nd is anticipated, but it has not been a source of volatility as the outcome seems clear in favor of Morena. We have maintained our Q2 expectations at 16.25 expecting this to be a volatility hiccup in April.

6-12 Month Outlook – Long awaited FDI will come

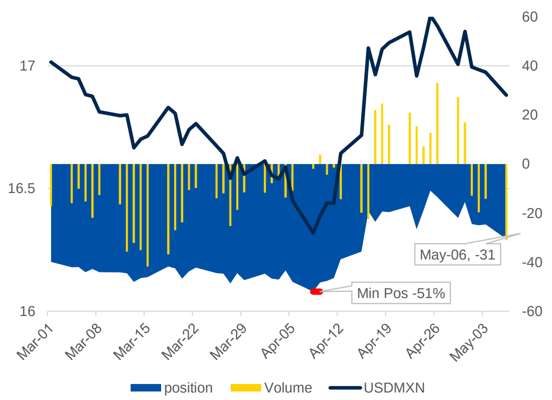
There is a secular trend in MXN driven by the near-shoring trend, supported by announced Foreign Direct Investment (FDI) inflows. In Q1, FDI investments were higher than 70% of the total FDI received in 2023. Additionally, green shoots have fuelled private investment in Mexico, with Banxico noting a surprising 20% growth in private investment in 2023, levels not seen since the 1990s. Portfolio investments have also been aimed at long-term assets like America Movil corporate bonds or Nearshoring REITs. Long-term, MXN is expected to continue outperforming its peers, especially as Banxico has pushed the easing cycle out into 2025

Indicators

	Current (Previous)*
Official cash rate	11.00 (11.25%)
Trend O/N interest rates (10yr avg)	6.33%
Bias in interest rate market	Lower
Headline Inflation %Y/Y (Previous)	4.37% (4.40%)
Inflation target	3%
Budget balance % GDP(Previous)	-3.31% (-4.01%)
Budget balance target % GDP	-
GDP Growth % y/y	2.46 (3.51)
Trend GDP %y/y (10y avg)	1.57%
Purchasing Power Parity Value Mar	16.46
Spot end-Apr	17.14
PPP Valuation	USD/MXN is overvalued
Current account balance % GDP (Previous)	-1.0% (-1.1%)
Trend current acct balance % GDP (10y avg)	-1.0%
Moody's Foreign Currency Rating	Baa2
Outlook	Stable

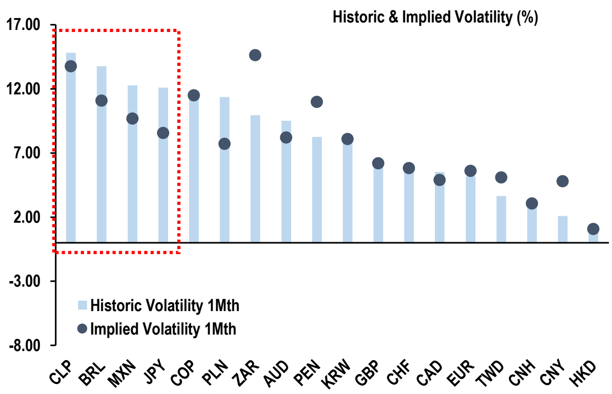
* Current is latest month, quarter, or year

1. RBC Proprietary Positioning now at 31% of historic high



Source: RBC Capital Markets; Note: This shows USD/MXN's positioning in Blue

2. LatAm5 Volatility in April spiked to double digit levels



Source: Bloomberg, RBC Capital Markets

Forecasts

	2024				2025			
	Q1	Q2f	Q3f	Q4f	Q1f	Q2f	Q3f	Q4f
USD/MXN	16.56	16.25	16.80	17.25	17.35	17.40	17.50	17.60
EUR/MXN	17.87	17.23	17.64	18.46	18.74	18.79	19.08	19.01
MXN/JPY	9.14	9.72	9.52	9.39	9.34	9.20	9.03	8.86
CAD/MXN	12.23	11.86	12.13	12.32	12.30	12.25	12.41	12.57

Source: RBC Capital Markets estimates

Chilean Peso

Luis Estrada

1-3 Month Outlook – A proxy for copper again?

Chile emerged as the unexpected outperformer in April, breaking all expectations in the process. Early in April, much like the Colombian peso, the Chilean peso (CLP) strengthened in anticipation of a weak US CPI release. However, when the CPI data surprised on the upside, the CLP lost the 4.5% it had recently gained, returning to the 980s level. Subsequently, USD/CLP staged a downtrend, breaking the key 940 support level and outperforming all its peers. The appreciation has been largely attributed to copper's impressive 17% rally during April. Additionally, there is a significant M&A story developing, as BHP initiated a 39 billion USD bid for Anglo American. Both companies are the largest copper miners in Chile, and the merger could create the largest copper miner in the world.

We expect the CLP to remain strong in the short term as long as the copper rally continues.

6-12 Month Outlook – Waiting for others at 4.0%

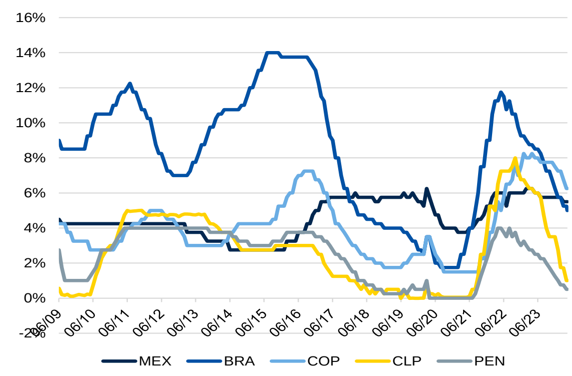
In the medium-term, we are less optimistic about the Chilean peso. The Governor of the Central Bank of Chile, Rossana Costa, was clear during the IMF meetings that BCRC would continue lowering the overnight (O/N) rates to 4%, regardless of the FOMC's easing cycle. Recently, Chilean inflation has shown an upward trend; the latest release for April was at 4%, and in their April Inflation Report, the Central Bank raised its inflation expectations to 3.8% for 2024, up from 3% in February. The next MPC meeting is scheduled for May 23, and the market expects them to maintain current rates. For the end of 2024, expectations are that the O/N rate will be reduced -125bps within the five MPC meetings left in 2024. For this reason, we don't expect USD/CLP to break below 915. We continue to see USD/CLP drifting back higher towards 940, as its overnight rate dips below the Fed Funds.

Indicators

	Current (Previous)*
Official policy rate	6.50% (7.25%)
Trend interest rates (10yr average)	4.0
Bias in interest rate market	Lower
Headline inflation %Y/Y	4.0% (4.5%)
Inflation target	3%
Budget balance % GDP (Previous)	-2.38% (-2.29%)
Budget balance target % GDP	-
GDP Growth % y/y (Previous)	0.41% (0.57%)
Trend GDP %y/y (10y average)	2.1
Purchasing Power Parity Value Mar	688
Spot end-Apr	960
PPP Valuation	USD/CLP is overvalued
Current account balance % GDP (Previous)	-3.78 (-4.10)
Trend current acct balance % GDP (10y avg)	-4.4
Moody's Foreign Currency Rating	A2
Outlook	Stable

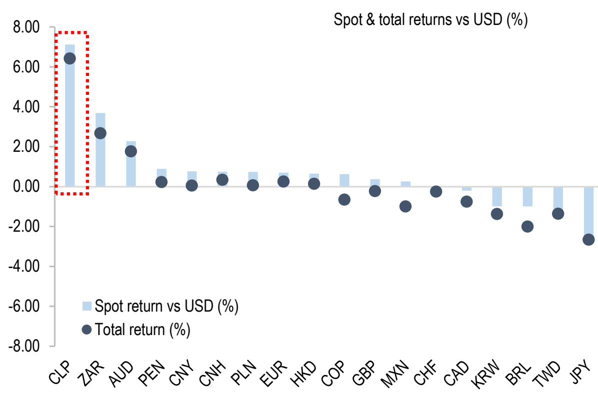
* Current is latest month, quarter, or year

1. LatAm5: O/N Rate vs. Fed Funds Historic Comparison



Source: RBCCM, Bloomberg

2. CLP: The best performer during April's volatility spike



Source: RBC Capital Markets, Bloomberg

Forecasts

	2024				2025			
	Q1	Q2f	Q3f	Q4f	Q1f	Q2f	Q3f	Q4f
USD/CLP	980	930	935	940	940	930	920	920
EUR/CLP	1058	986	982	1006	1015	1004	1003	994
JPY/CLP	30.2	31.3	32.3	33.8	33.8	33.5	32.9	32.2
CAD/CLP	724	679	675	671	667	655	652	657

Source: RBC Capital Markets estimates

Colombian Peso

Luis Estrada

1-3 Month Outlook - Holding its ground

Colombia stands out with the highest overnight interest rate level in the region and a significant gap between inflation (~7%) and overnight rates (11.75%). The Colombian peso (COP) held its ground well during the volatility of April and continues to be the high beta currency for risk-on sentiment in Latin America. The currency started from a very strong position, touching 3770 before the US CPI release, and then corrected back to the 3850-3950 range, where it was trading before the dip below 3800. Despite the ongoing easing cycle, which included a 50 basis points cut on April 30th, we expect the easing to continue with a reduction of 50 basis points at each of the next five MPC meetings, reaching 9.00%. This is not anticipated to affect COP's performance adversely; in fact, we expect the COP to strengthen in Q2, although an update to 3800 is needed after April's reset.

6-12 Month Outlook – Political dark clouds

In the medium-term, the outlook remains positive; however, there are some political concerns on the horizon. The pending Pension Reform, which shifts assets to public managers, is a point of concern. This reform development is linked to a recent scandal involving the CEO of Ecopetrol, the former head of the presidential campaign for President Petro, which has prompted calls for an investigation.

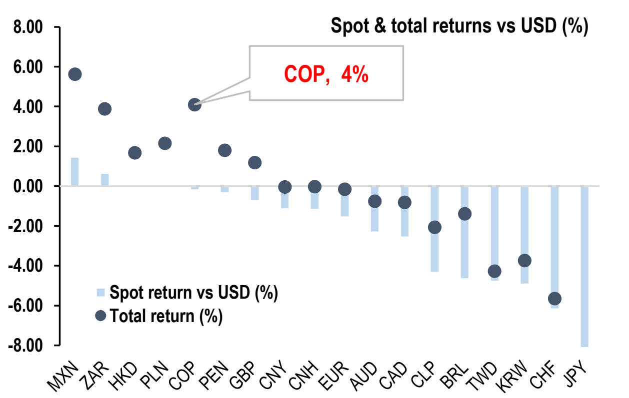
On an examination beyond 2024, markets expect the O/N to keep trending lower into the 6.0% area. This will be a larger challenge as neither Brazil nor Mexico will be at this level in the first half of 2025 and Colombia at such levels will make the COP a target for funding other currencies.

Indicators

	Current (Previous)*
Official cash rate	11.75% (12.25%)
Trend interest rates (10yr average)	5.15
Bias in interest rate market	Lower
Headline Inflation %Y/Y	7.16 (7.36)
Inflation target	3%
Budget balance % GDP (Previous)	0.23 (-1.42)
Budget balance target % GDP	-
GDP Growth % y/y (Previous)	0.3% (-0.6%)
Trend GDP %y/y (10y average)	2 .0
Purchasing Power Parity Value Mar	1399
Spot end-Apr	3919
PPP Valuation	USD/COP is overvalued
Current account balance % GDP (Previous)	-2.66 (-3.52)
Trend current acct balance % GDP (10y avg)	-4.6
Moody's Foreign Currency Rating	Baa2
Outlook	Stable

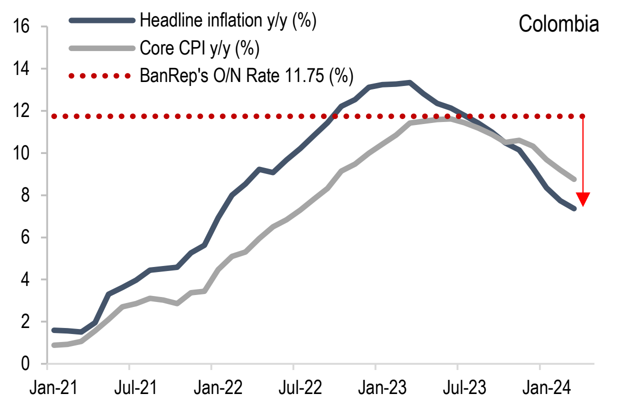
* Current is latest month, quarter, or year

1. YTD Returns – COP holding positive Total Return



Source: RBCCM, Bloomberg

2. O/N Rate still 460bps above ex-post inflation



Source: RBC Capital Markets, Bloomberg

Forecasts

	2024				2025			
	Q1	Q2f	Q3f	Q4f	Q1f	Q2f	Q3f	Q4f
USD/COP	3859	3750	3775	3750	3800	3800	3810	3830
EUR/COP	4164	3975	3964	4013	4104	4104	4153	4136
JPY/COP	25.50	23.73	23.59	23.15	23.46	23.75	24.11	24.55
CAD/COP	2850	2737	2726	2679	2695	2676	2702	2736

Source: RBC Capital Markets estimates

Peruvian Peso

Luis Estrada

1-3 Month Outlook – Range-bound

Peru continues to range trade within a defined band between 3.67-3.87, touching both extremes during April. Initially, USD/PEN dipped to the 3.60s; after the US CPI release, it bounced back to the 3.80s. As of early May, it tested 3.70 again. Adding to the volatility, the Central Bank of Peru surprised markets by pausing rate adjustments at their March MPC meeting and then unexpectedly easing in April with a 25-basis point cut, following the approval of a pension withdrawal. Most recently, they implemented another 25-basis point cut in May, bringing the overnight (O/N) rate to 5.75%, the lowest in the region. For Q2, we maintain our short-term target for USDPEN at 3.70. The immediate effect of the pension withdrawal announcement is usually a stronger currency and weaker bonds. This occurs because pension funds, needing to create liquidity, are more likely to sell USD-denominated bonds and exchange USDPEN to pay savers, rather than selling local bonds where market counterparts can quickly adjust prices, knowing in advance the scale of sales required by the pension funds.

6-12 Month Outlook – Political turmoil with 4% O/N

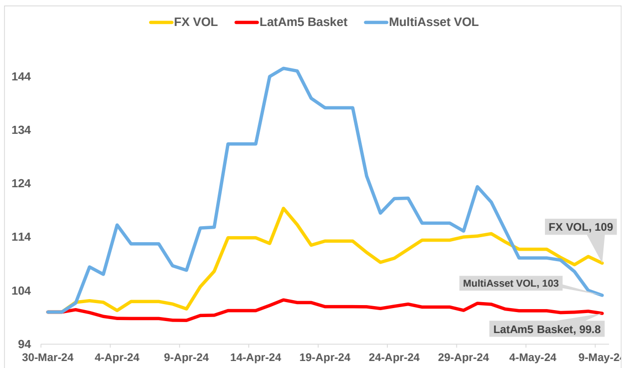
The Central Bank estimates that in five of the next seven MPC meetings, there will be cuts of 25 basis points each, aiming for a year-end rate of 4.40% and a terminal rate of 4.00% by 2025. This approach is considered aggressive, given the 7 billion USD that savers will be able to withdraw before the end of 2024, potentially adding to inflation pressures. Additionally, the seventh withdrawal has drawn attention from Moody's, which downgraded Peru's foreign currency debt rating to BBB-. This rating change reflects concerns about a complex political landscape that could influence the next presidential election. Moreover, Peru's economic growth has been the weakest in the region, strongly influenced by weather-related phenomena.

Indicators

	Current (Previous)*
Official cash rate	5.75 (6.00)
Trend interest rates (10yr average)	5.15
Bias in interest rate market	Lower
Headline Inflation %Y/Y	2.42 (3.02)
Inflation target	3%
Budget balance % GDP	-2.76 (-2.80)
Budget balance target % GDP	-
GDP Growth % y/y (Q2)	0.0%
Trend GDP %y/y (10y average)	2 .0
Purchasing Power Parity Value Mar	1.86
Spot end-Apr	3.77
PPP Valuation	USD/CLP is overvalued
Current account balance % GDP (Previous)	0.63 (-0.45)
Trend current acct balance % GDP (10y avg)	-2.1
Moody's Foreign Currency Rating	Baa1
Outlook	Negative

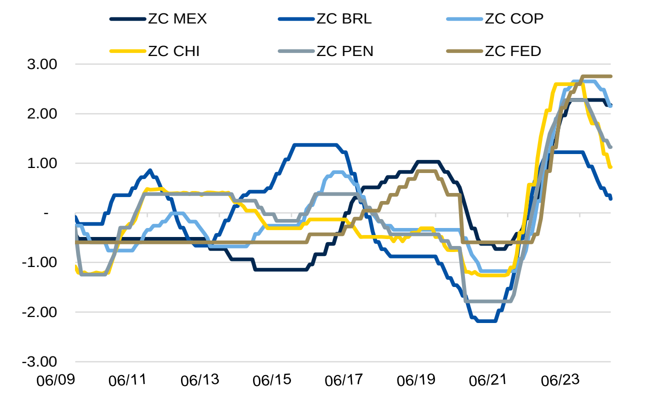
* Current is latest month, quarter, or year

1. FX Vol and Equity/Bonds Vol vs LatAM5 (Normalized)



Source: RBCCM, Bloomberg

2. Z-score of O/N Rates in LatAm5 between 1-2 SD of Mean



Source: RBC Capital Markets, Bloomberg

Forecasts

	2024				2025			
	Q1	Q2f	Q3f	Q4f	Q1f	Q2f	Q3f	Q4f
USD/PEN	3.72	3.70	3.73	3.75	3.75	3.77	3.78	3.80
EUR/PEN	4.02	3.92	3.92	4.01	4.05	4.07	4.12	4.10
PEN/JPY	40.66	42.70	42.90	43.20	43.20	42.44	41.80	41.05
CAD/PEN	2.75	2.70	2.69	2.68	2.66	2.65	2.68	2.71

Source: RBC Capital Markets estimates

Forecasts

Spot forecasts

	2024				2025			
	Q1	Q2f	Q3f	Q4f	Q1f	Q2f	Q3f	Q4f
EUR/USD	1.08	1.06	1.05	1.07	1.08	1.08	1.09	1.08
USD/JPY	151	158	160	162	162	160	158	156
GBP/USD	1.26	1.25	1.22	1.23	1.23	1.21	1.21	1.19
USD/CHF	0.90	0.92	0.95	0.95	0.96	0.98	0.99	1.02
USD/SEK	10.66	11.13	11.14	10.84	10.65	10.56	10.37	10.37
USD/NOK	10.83	11.04	11.00	10.65	10.46	10.37	10.18	10.19
USD/CAD	1.3540	1.3700	1.3850	1.4000	1.4100	1.4200	1.4100	1.4000
AUD/USD	0.65	0.64	0.65	0.66	0.67	0.67	0.68	0.68
USD/CNY	7.22	7.26	7.32	7.30	7.30	7.28	7.28	7.27
USD/KRW	1347	1390	1420	1400	1400	1390	1370	1350
USD/SGD	1.35	1.36	1.37	1.36	1.36	1.35	1.34	1.33
USD/MYR	4.73	4.80	4.85	4.83	4.81	4.79	4.77	4.75
USD/HKD	7.82	7.84	7.84	7.84	7.82	7.82	7.81	7.80
USD/BRL	5.01	5.05	4.95	4.80	4.80	4.78	4.80	4.85
USD/MXN	16.56	16.25	16.80	17.25	17.35	17.40	17.50	17.60
USD/CLP	979	930	935	940	940	930	920	920
USD/PEN	3.72	3.70	3.73	3.75	3.75	3.77	3.78	3.80
USD/COP	3852	3750	3775	3750	3800	3800	3810	3830

Source: RBC Capital Markets estimates

EUR Crosses

	2024				2025			
	Q1	Q2f	Q3f	Q4f	Q1f	Q2f	Q3f	Q4f
EUR/USD	1.08	1.06	1.05	1.07	1.08	1.08	1.09	1.08
EUR/JPY	163	167	168	173	175	173	172	168
EUR/GBP	0.85	0.85	0.86	0.87	0.88	0.89	0.90	0.91
EUR/CHF	0.97	0.98	1.00	1.02	1.04	1.06	1.08	1.10
EUR/SEK	11.50	11.80	11.70	11.60	11.50	11.40	11.30	11.20
EUR/NOK	11.68	11.70	11.55	11.40	11.30	11.20	11.10	11.00
EUR/CAD	1.46	1.45	1.45	1.50	1.52	1.53	1.54	1.51
EUR/AUD	1.65	1.66	1.62	1.62	1.61	1.61	1.60	1.59
EUR/CNY	7.79	7.70	7.69	7.81	7.88	7.86	7.94	7.85
EUR/KRW	1454	1473	1491	1498	1512	1501	1493	1458
EUR/SGD	1.46	1.44	1.44	1.46	1.47	1.46	1.46	1.44
EUR/MYR	5.10	5.09	5.09	5.17	5.19	5.17	5.20	5.13
EUR/HKD	8.44	8.31	8.23	8.39	8.45	8.45	8.51	8.42
EUR/BRL	5.41	5.35	5.20	5.14	5.18	5.16	5.23	5.24
EUR/MXN	17.87	17.23	17.64	18.46	18.74	18.79	19.08	19.01
EUR/CLP	1057	986	982	1006	1015	1004	1003	994
EUR/PEN	4.01	3.92	3.92	4.01	4.05	4.07	4.12	4.10
EUR/COP	4157	3975	3964	4013	4104	4104	4153	4136

Source: RBC Capital Markets estimates

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