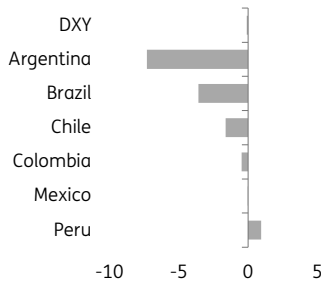


15 March 2019

# LATAM FX Talking

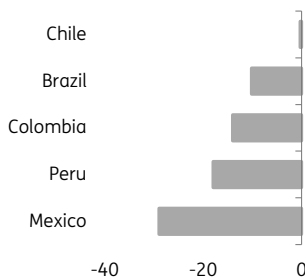
## Monetary policy needle turns more dovish

FX monthly change (%)



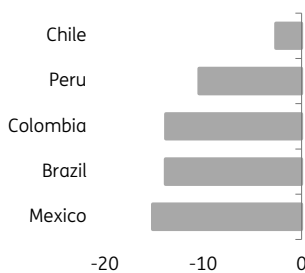
Source: Bloomberg, ING

5yr local rate monthly change (bp)



Source: Bloomberg, ING

5yr CDS monthly change (bp)



Source: Bloomberg, ING

Much like in the US and the EU, monetary policy in LATAM has also incorporated a dovish bias over the past couple of months. Economic activity has disappointed in the largest economies, Brazil and Mexico, while inflation data has surprised consistently to the downside, particularly in Mexico and throughout the Andes, paving the way for a reassessment of the current monetary policy guidance.

For **Chile**, this should translate into a delayed rate-normalization cycle, with BCCh likely losing appetite for a faster rate-hiking cycle, after the two hikes already implemented, amid growing concerns over the strength of the global economy. We also expect the **Colombian** and **Peruvian** central banks to extend the current neutral guidance for longer than initially expected, even though economic activity has shown stronger resilience in both places.

**Mexico** is, however, in our opinion, where the policy guidance has greater room to manoeuvre. With inflation converging convincingly to the targeted range in the coming months, Banxico should overcome its primary barrier for a dovish monetary policy shift. With the policy rate deep inside contractionary territory, and economic activity decelerating, as investment contracts, the case for policy easing should strengthen. Overall, we expect a deeper cycle than currently expected, with a first 25 basis point cut possibly as early as June 27, and no later than 3Q, which should reduce MXN support towards yearend.

In **Brazil**, policymaking is mostly on hold, waiting for Congress to conclude its debate of the all-important social security reform. Even though inflation and economic cycle considerations could in principle accommodate an additional monetary easing, uncertainty vis-à-vis the reform should prevent BACEN from acting until the reform is approved, which we expect to take place sometime in 3Q. A sharp BRL rally following that approval could be an important catalyst for rate cuts.

**Argentina** is, again, a case apart, with monetary tightening being used to stabilize local assets amid heightened volatility driven by external events and the lingering deterioration of local macro fundamentals, with higher than expected inflation and disappoint growth, adding to investor concerns over the outcome of the October Presidential election.

### ING's 12-month currency view vis-à-vis forward/NDF market forecasts

	USD/BRL		USD/MXN		USD/CLP	
1M	3.85	↑	19.20	↓	660.00	↓
3M	4.00	↑	19.00	↓	665.00	↓
6M	3.40	↓	19.10	↓	660.00	↓
12M	3.70	↓	19.50	↓	645.00	↓
	USD/ARS		USD/COP		USD/PEN	
1M	41.80	↓	3100.00	↓	3.29	↓
3M	43.50	↓	3100.00	↓	3.29	↓
6M	46.50	↓	3090.00	↓	3.30	↓
12M	52.80	↓	3020.00	↓	3.27	↓

>/=< indicates our forecast for the currency pair is above/in line with/below the corresponding market forward or NDF outright

Source: Bloomberg, ING

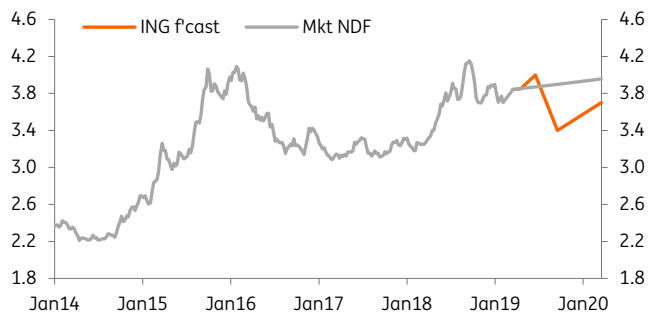
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## USD/BRL

Social security reform debate is initiated in Congress

Current spot: 3.84



Source: Bloomberg, ING

- The social security reform debate is finally under way in Congress. Government leaders remain optimistic about its prospects, but entrenched resistance by powerful special-interest groups suggest a less-than-smooth legislative process.
- The opposition is not large enough to block the reform, but the government does not have the votes yet, to ensure its approval. Lawmakers' support must be negotiated with the government.
- The BRL has underperformed recently and uncertainty about the reform's approval should keep a high-volatility underperforming bias in place. But we still expect the reform to be approved in 3Q, triggering a temporary BRL rally, towards the 3.3-3.4 range.

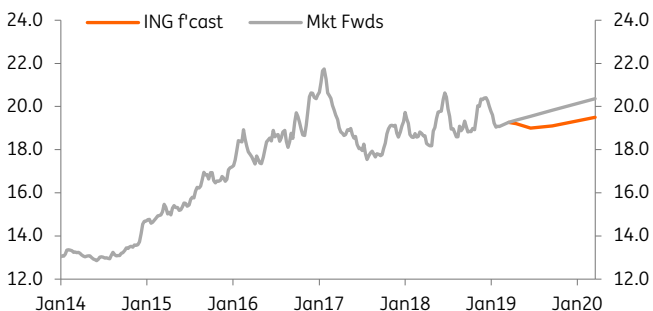
ING forecasts (NDF)	1M 3.85 (3.85)	3M 4.00 (3.87)	6M 3.40 (3.90)	12M 3.70 (3.96)
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## USD/MXN

Still-attractive carry to keep the MXN resilient

Current spot: 19.27



Source: Bloomberg, ING

- Despite lingering policy uncertainties and growing concerns about Mexico's economic growth outlook, we believe that the risk of negative policymaking headlines is smaller in the nearer term.
- In particular, the risk of rupture in market credibility in issues like fiscal prudence, PEMEX and central bank independence should take longer to emerge. We believe that risk should intensify as economic activity disappoints, raising the risk of policy mistakes.
- For now, even though we expect Banxico to shift to a dovish monetary policy stance in the coming months, the mix of attractive interest rates and solid macro fundamentals suggests that the MXN should continue to outperform its regional peers.

ING forecasts (mkt fwd)	1M 19.20 (19.37)	3M 19.00 (19.54)	6M 19.10 (19.83)	12M 19.50 (20.36)
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## USD/CLP

Catch-up to higher copper prices suggests outperformance

Current spot: 671.17



Source: Bloomberg, ING

- The CLP was not immune to the latest USD rally that affected most EM FX but, as copper prices have stayed mildly supportive, there's some room for CLP outperformance in the coming weeks.
- Constructive Chinese data and a favourable resolution to the US-China trade-war impasse would further support the CLP but, at current levels, room for appreciation is relatively limited.
- Near-term CLP prospects are closely linked to external drivers, while local macro trends have become more FX neutral. Inflation has surprised to the downside while economic activity indicators have softened, dragged by mining, which should, in practice, reduce BCCh's rate-hiking appetite.

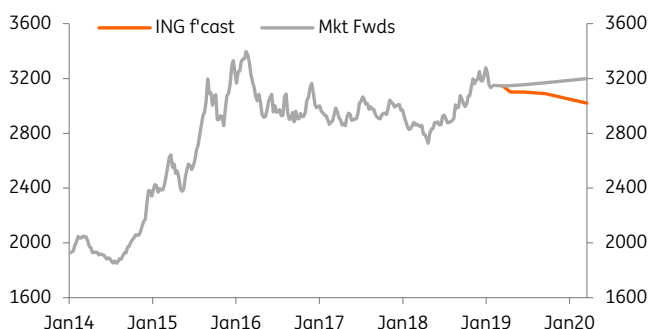
ING forecasts (NDF)	1M 660.00 (671)	3M 665.00 (671)	6M 660.00 (671)	12M 645.00 (672)
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## USD/COP

A supportive COP environment amid higher oil prices

**Current spot: 3144.65**



Source: Bloomberg, ING

- Much like the CLP, the COP was not immune to the USD rally seen in the past month but, as oil prices remain supportive, there's now some scope for a catch-up appreciation in the COP.
- Future FX performance should remain chiefly dependent on external drivers (i.e. oil prices and the USD) with domestic drivers remaining closer to COP-neutral, if a bit more constructive.
- The most notable local macro development has been the surprising resilience of activity data, with GDP growth on track to expand near its potential this year amid solid domestic demand. On-target inflation suggests however that a neutral monetary policy guidance should remain for longer than initially expected.

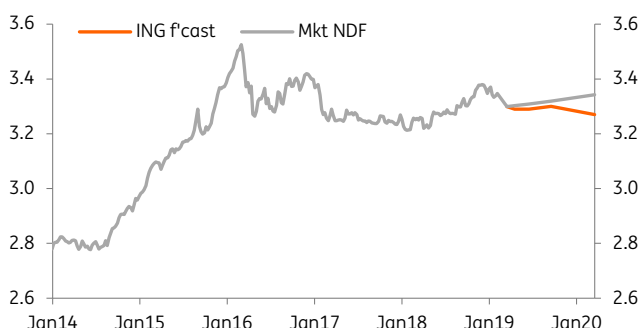
<b>ING forecasts (NDF)</b>	<b>1M 3100.00 (3147)</b>	<b>3M 3100.00 (3155)</b>	<b>6M 3090.00 (3168)</b>	<b>12M 3020.00 (3200)</b>
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## USD/PEN

Solid macro trends help offset trade-war concerns

**Current spot: 3.30**



Source: Bloomberg, ING

- As usual, the PEN traded with the lowest volatility in the region, outperforming sharply amid the widespread sell-off. As a result, the PEN was effectively the least affected by the USD move, following the benign commodity trend more closely than its peers in the region.
- At current levels, further upside seems limited, with BCRP's FX intervention back in the radar, but developments on the US-China front and economic growth would add support to the currency.
- Peru's BCRP should extend the current "neutral" bias for the policy rate (2.75%) longer than we initially thought amid moderate economic activity and on-target inflation.

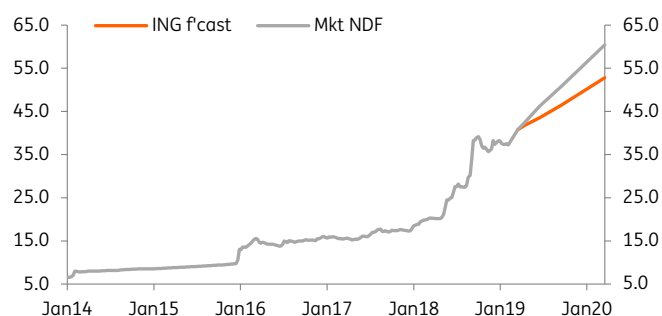
<b>ING forecasts (NDF)</b>	<b>1M 3.29 (3.30)</b>	<b>3M 3.29 (3.31)</b>	<b>6M 3.30 (3.32)</b>	<b>12M 3.27 (3.34)</b>
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## USD/ARS

Evidence of ARS's vulnerability resurfaces

**Current spot: 40.75**



Source: Bloomberg, ING

- The USD rally together with the persistent and higher-than-expected inflation data ended the brief period of calm for ARS assets, pushing the ARS firmly inside the non-intervention zone.
- Local market turbulence led BCRA to raise rates aggressively, and re-establish some level of stability, but the episode confirmed the level of vulnerability that should persist in the local market at least until the October Presidential election is concluded.
- The higher carry and USD-liquidity measures should help stabilise local assets in the nearer term but the combination of high inflation and poor economic activity should complicate the outlook for the presidential election dynamics, keeping alive the risk of a return of Cristina Kirchner to office, if she decides to run.

<b>ING forecasts (NDF)</b>	<b>1M 41.80 (42.58)</b>	<b>3M 43.50 (46.19)</b>	<b>6M 46.50 (50.85)</b>	<b>12M 52.80 (60.42)</b>
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