BofA SECURITIES

LatAm Watch

LatAm Monthly FX Overview

30 March 2023

GEM Economics
LatAm

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Summary of FX views

If the start of 2023 was characterized by optimism about the global outlook, the end of 1Q23 is bringing shock waves from both sides of the Atlantic. What seem to be pockets of vulnerabilities in the financial system has brought strains for the global economy. US rates have repriced substantially, with monetary policy easing now expected around the corner as recession concerns loom. EM FX generally suffered on the heels of risk-off, but the initial market reaction has since faded somewhat. Going forward, we expect continued volatility as global factors have become the key driver of EM FX.

ARS (bearish*): Reserves are precarious amid a record drought, with presidential elections ahead. The parallel gap may widen. We see USD/ARS at 417 by 2023-end.

BRL (bullish*): Fiscal risks remain front and center. In our view, the unveiling of the fiscal framework could provide support. We see USD/BRL at 5.20 by 2023-end.

CLP (bearish*): Moderation in reforms has been supportive, but external imbalances remain amid a more uncertain global outlook. We see USD/CLP at 825 by 2023-end.

COP (neutral*): A weaker dollar has recently supported COP, and we are turning more constructive on the odds of policy moderation. We see USD/COP at 4850 by 2023-end.

MXN (bearish*): Risk-off recently hurt MXN, but a still rich valuation and crowded positioning make risk-reward asymmetric. We see USD/MXN at 20.00 by 2023-end.

PEN (neutral*): A low beta to global factors has recently shielded PEN. The political backdrop will remain a key driver for the Sol. We see USD/PEN at 3.82 by 2023-end.

VES (bearish*): Inflationary pressures are coming back amid government spending increases and lower oil prices. We see VES/USD at 309 by 2023-end.

Table 1: Current FX forecasts
BofA quarter-end FX forecasts

		Forecasts			
Currency	**View/bias**	**2Q '23**	**3Q '23**	**4Q '23**	**1Q '24**
USD/ARS (official)	bearish*	242	280	417	482
USD/ARS (blue chip)	--	508	616	729	772
USD/BRL	bullish*	5.15	5.18	5.20	5.25
USD/CLP	bearish*	810	820	825	830
USD/COP	neutral*	4,750	4,800	4,850	4,885
USD/MXN	bearish*	19.1	19.5	20.0	20.2
USD/PEN	neutral*	3.78	3.80	3.82	3.84
USD/VES	bearish*	58	133	309	533

Source: BofA Global Research *Note: bullish/neutral/bearish labels are relative to year-end 2023 forward contracts.

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Argentina

FX Views and forecasts

View: bearish*

FX reserves are very precarious amid a worse than expected drought, with net reserves around 1.5bn, and rampant inflation. The parallel FX gap is likely to see pressure going forward given this vulnerability, coupled with an electoral year that incentivizes the government to kick the can down the road. We forecast USD/ARS at 417 by 2023-end.

Finance Minister Massa delivered some transitory relief showing some more commitment to the IMF program. But his performance as Finance Minister is becoming lackluster as time passes. Inflation has surpassed 100% per year for the first time since the end of the hyperinflation in the early 1990s, and is now back to a pace close to 7% per month. The decisions to do a peso debt swap to extend maturities, and forcing intra public sector entities to sell dollar bonds in the open market (after the government recently repurchased these same bonds on the basis of being cheap), underscores how fragile the situation is on the FX front. Anything goes to appease the parallel gap.

The official exchange rate remains deeply overvalued and the strategy remains one of patchworks, including severe import restraint. Imports are being curtailed by a combination of red tape and more expensive differentiated exchange rates (e.g. “Coldplay dollar”, “Qatar dollar”, non-necessities), while exporters have been offered a series of FX incentives (“soy dollar”, “soy dollar 2”). These incentives granted some temporary respite to reserves, and the FX gap stabilized in the 90-100% range.

However, FX reserves are once again reaching critically low levels, hovering around 1.5bn. The drought, which was already expected to become a drain in reserves, has been significantly worse than expected. By some accounts, the impact of the drought may be more than 15bn in lower exports relative to last year. To make things worse, political uncertainty around the primaries in August and the general election in October will likely remain elevated, as the deterioration of the outlook favors more extreme candidates from both the ruling party and the opposition.

The political cycle following the record drought is likely to strengthen US dollar demand and generate pressures, especially in 3Q23 and 4Q23. In our view, the direness of the situation will leave the government no choice but to accept a faster depreciation of the official ARS. However, we still expect a widening of the parallel FX gap.

Upcoming risk events

- Impact of drought (1H23); presidential primaries (Aug 13) and elections (Oct 22).

Hedging

We recommend hedging given risk of fast depreciation pace due to overvaluation.

Table 2: USD/ARS forecasts vs fwds
USD/ARS fwd & forecast comparison

	current	chg		
Spot	**208.3**	**+17.73**		
	Forecast		**Forward**	
Period	**current**	**chg**	**current**	**chg**
2Q 2023	241.9	+30.73	260.2	+153.57
3Q 2023	280.0	+40.44	333.1	+207.55
4Q 2023	416.8	+146.50	417.1	+273.87
1Q 2024	482.5	+113.32	489.2	+330.85

Source: BofA Global Research, Bloomberg
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Table 3: USD/ARS (blue chip) forecasts
USD/ARS blue chip forecasts

	current	chg (diff)
Spot	**396.9**	**+24.94**
	Forecast	
Period	**current**	**chg (diff)**
2Q 2023	508.0	+85.66
3Q 2023	616.1	+112.92
4Q 2023	729.4	+134.75
1Q 2024	772.0	+125.94

Source: BofA Global Research, Bloomberg
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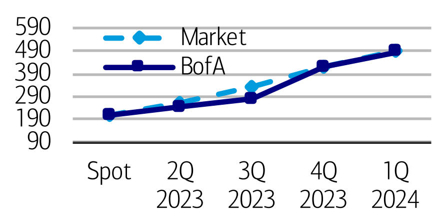
Chart 1: USD/ARS (official) forecasts
USD/ARS fwd & forecast comparison



Source: BofA Global Research, Bloomberg
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*Note: bullish/neutral/bearish labels are relative to year-end 2023 forward contracts.

Brazil

FX Views and forecasts

View: bullish*

Fiscal risks took center stage after the runoff election, following strong outperformance in 2022. We expect the unveiling of a fiscal framework and the record harvest to be supportive for the currency in the near term. We forecast USD/BRL at 5.20 by 2023-end.

After the runoff election, fiscal risks became front and center. Since then, Brazilian assets have been under pressure. Some moderation signals gave some temporary respite, but that did not last. Overall, there could be positive catalysts, but the outlook greatly hinges on the policy actions from and expectations about the administration (see Is the new fiscal anchor enough?). Both monetary policy and developments around the fiscal framework will be key, and both of these are highly intertwined.

The stark tensions between Lula and the BCB make this clear, as the government keeps criticizing the central bank over high interest rates, and the BCB has signaled that fiscal risks are preventing rate cuts from happening. A positive note on the fiscal side is that media reports indicate that the unveiling of a fiscal framework may take place as soon as April. In our view, this could support risk assets, as we believe risks had already been priced to a significant extent. Additionally, the resumption of fuel taxes also helps.

Conditional on the unveiling of the fiscal framework, we recently updated our forecasts and now expect the BCB to cut rates as early as May given the deterioration in local financial conditions (see Five questions on the credit squeeze and one conclusion: rate cuts will come earlier). While we remain of this view, hawkish communication from the BCB following the latest monetary policy decision has tilted the balance of risks.

Despite the rate cuts we forecast, we expect BRL to be somewhat shielded from the lower carry, supported by still high real rates and the positive catalysts from the fiscal side. The record harvest, which could lead to 0.7% of GDP in additional exports, can also provide support amid a relatively cheap BRL real valuation and light positioning.

While a reasonable fiscal framework would bring respite, fiscal risks will remain elevated. However, we are of the view that fiscal risks are priced-in to a significant extent (see Brazil vs. Mexico: Caipirinha, Tequila, or both?). Fiscal concerns will remain a drag, but policy moderation showcasing stronger commitment towards fiscal sustainability, and easing tensions with the BCB, could cement BRL as a major outperformer in 2023.

Upcoming risk events

- Fiscal framework (Apr), BCB Board replacements (Apr), tax reform (1H23)

Hedging

We recommend taking advantage of BRL rallies to hedge policy risks in the short term.

Table 4: USD/BRL forecasts vs forwards
USD/BRL forward and forecast comparison

	current	chg (diff)		
Spot	**5.14**	**-0.08**		
	Forecast		**Forward**	
Period	**current**	**chg (diff)**	**current**	**chg (diff)**
2Q 2023	5.15	-0.04	5.21	-0.34
3Q 2023	5.18	-0.02	5.31	-0.38
4Q 2023	5.20	+0.00	5.38	-0.47
1Q 2024	5.25	+0.05	5.47	-0.55

Source: BofA Global Research, Bloomberg

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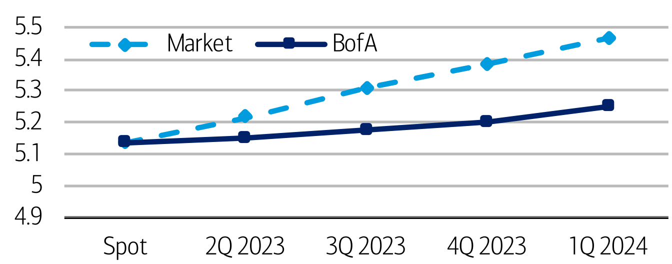
Chart 2: USD/BRL forecasts
USD/BRL forward and forecast comparison



Source: BofA Global Research, Bloomberg

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*Note: bullish/neutral/bearish labels are relative to year-end 2023 forward contracts.

Cross currency basis

Table 5: Cupom cambial contracts
Cupom cambial prices and ranges

Contract	Last	1w chg	3m chg	1y chg	Min	Last vs 1y Avg	Max	1y Avg	1w vol	3m vol	3m z-score	1y z-score
Jan24	6.05	-2	0	300	3.00		6.82	5.19	21	151	-0.5	0.8
Jan25	5.48	-13	-17	221	3.18		6.60	5.00	23	166	-0.7	0.5
Jan26	5.19	-23	-17	185	3.21		6.20	4.84	23	163	-0.7	0.4

Legend: : [redacted]nt value; : 1y average. The z-score measures the distance between the current value and the mean in standard deviation units.
Source: BofA Global Research, Bloomberg

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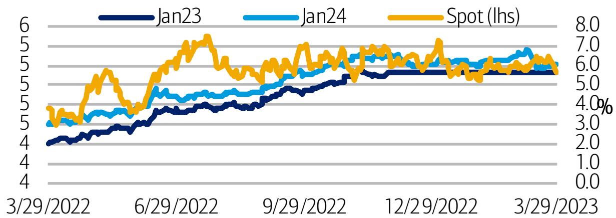
Chart 3: Short-term Cupom Cambial rates vs USD/BRL spot
Short term Cupom Cambial rates and USD/BRL comparison



Source: BofA Global Research, Bloomberg

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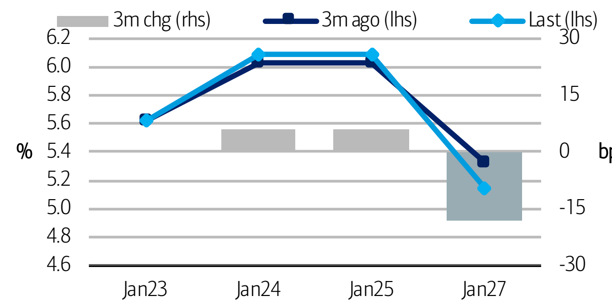
Chart 4: Term structure of Cupom Cambial rates
Cupom Cambial rates 3m evolution



Source: BofA Global Research, Bloomberg

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Volatility surface: USD/BRL

Table 6: Current implied volatilities
USD/BRL options implied volatilities

	10Δ Put	25Δ Put	ATM	25Δ Call	10Δ Call
1m	16.25	16.25	16.95	18.35	20.12
3m	16.32	16.34	17.10	18.64	20.59
6m	16.29	16.29	17.08	18.69	20.78
1y	16.10	16.12	16.94	18.62	20.88

Source: BofA Global Research

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Table 7: 3m z-scores of implied volatilities
USD/BRL 3m z-scores of implied volatilities

	10Δ Put	25Δ Put	ATM	25Δ Call	10Δ Call
1m	- 0.8	- 0.9	- 0.9	- 0.8	- 0.7
3m	- 0.9	- 1.0	- 1.0	- 1.0	- 1.0
6m	- 1.0	- 1.1	- 1.2	- 1.2	- 1.3
1y	- 1.3	- 1.3	- 1.4	- 1.5	- 1.7

Source: BofA Global Research

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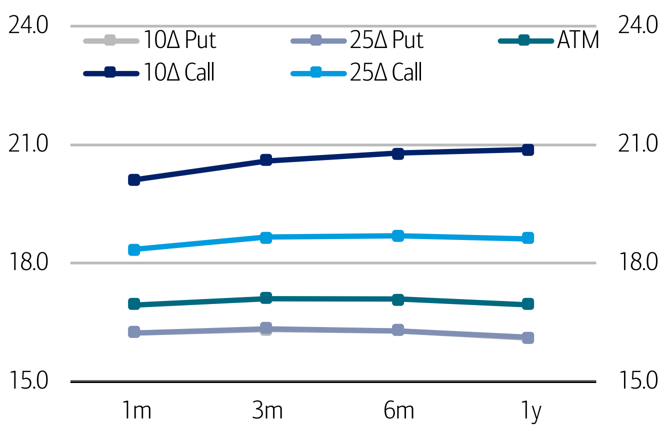
Chart 5: Term structures of implied volatilities
USD/BRL implied volatilities by maturity date



Source: BofA Global Research

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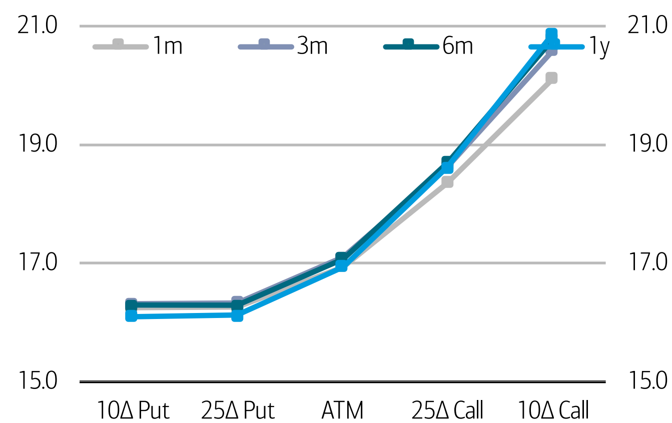
Chart 6: Implied volatility smiles
USD/BRL implied volatility by strike price



Source: BofA Global Research

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Chile

FX Views and forecasts

View: bearish*

Overall, despite some setbacks, the Chilean peso holds its appreciating trend since early in the year. Exposure to China's reopening and higher copper prices are the main driver. But political moderation should not be neglected. Still, a wide current account deficit and low FX reserves are a concern. We see USD/CLP at 825 by 2023-end.

The reopening in China and the subsequent rally in copper prices has been a dealbreaker for CLP. However, a significant compression in local policy risks has likely also played a role. The rejection of the constitutional draft in September was a first sign of relief. Soon, in May, the elections for the body that will draft the new constitutional proposal will take place in a climate of more moderation that is likely to lead to a more balanced writing body. Furthermore, the new rules of the reform process limit tail risks.

Another dimension of moderation can be seen surrounding the tax and pension reforms. For some time, we have been of the view that these reforms would have to be watered down in order to pass Congress. The recent rejection in the Lower House of the government's flagship tax reform is the clearest example of how radical reforms are unlikely to fly. The pension reform is another area where we expect moderation amid a fragmented Congress in order to make any progress. In conclusion, the Chilean peso is subject to much less policy and political risk than a year ago.

On the external front, the global financial stress has worsened the balance of risks around the probability of risk-off scenarios. So far, CLP has been resilient despite having one of the largest exposure to global factors in LatAm. But Chile's external accounts remain a risk. The current account deficit is still wide, and FX reserves are low. In this context, a potential reserve accumulation program cannot be ruled out in the medium term. But the central bank should start by stopping to roll over their NDFs first.

Regarding monetary policy, we remain of the view that markets keep pricing too many cuts too soon. CPI prints early in the year were above expectations, and we now expect BCCh to cut rates starting in June (see Persistent inflation, resilient activity & cautious BCCh. Rate cuts postponed). In this context, carry could provide more support if cuts were to be further postponed. But we also expect some fiscal deterioration with respect to last year. Overall, we keep turning more constructive CLP amid more balanced risks.

Upcoming risk events

- BCCh meeting (April 4); tax, pension, mining (ongoing); constitution (May, December)

Hedging

We recommend hedging given downside global risks.

Table 8: USD/CLP forecasts vs forwards

USD/CLP forward and forecast comparison

	current	chg (diff)		
Spot	**794**	**-4**		

Period	Forecast current	Forecast chg (diff)	Forward current	Forward chg (diff)
2Q 2023	810	-10	801	-23
3Q 2023	820	-10	810	-22
4Q 2023	825	-10	816	-25
1Q 2024	830	-10	821	-31

Source: BofA Global Research, Bloomberg

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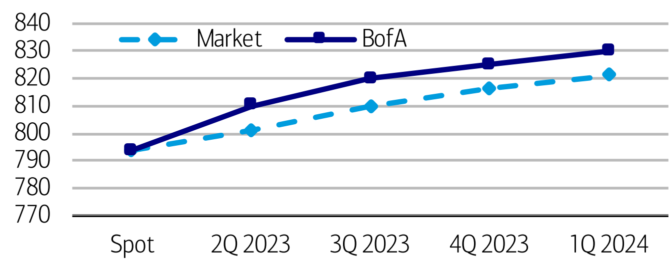
Chart 7: USD/CLP forecasts

USD/CLP forward and forecast comparison



Source: BofA Global Research, Bloomberg

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*Note: bullish/neutral/bearish labels are relative to year-end 2023 forward contracts.

Cross currency basis

Table 9: CAMARA vs 6m LIBOR basis swaps
Camara vs 6m LIBOR basis contract prices and ranges

Maturity	Last	1w chg	3m chg	1y chg	Min	Last vs 1y Avg	Max	1y Avg	1w vol	3m vol	3m z-score	1y z-score
1y	166	9	55	40	59		167	103	25	178	1.8	2.6
2y	130	14	3	42	65		168	115	12	87	1.0	0.6
5y	56	-4	-37	17	23		121	73	12	83	-0.7	-0.8
10y	52	-3	-37	9	20		118	66	11	81	-0.7	-0.6

Legend: [redacted]nt value; : 1y Average. The z-score measures the distance between the current value and the mean in standard deviation units.
Source: BofA Global Research, Bloomberg

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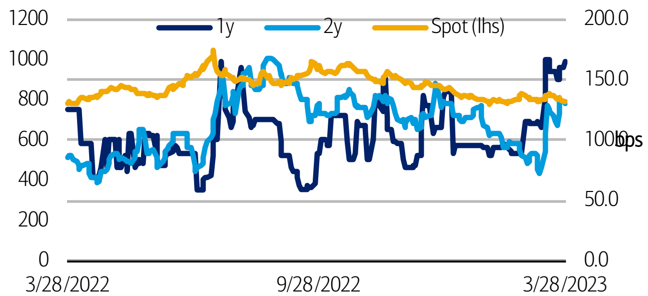
Chart 8: Short-term basis swaps vs USD/CLP spot
Short-term basis swaps and USD/CLP comparison



Source: BofA Global Research, Bloomberg

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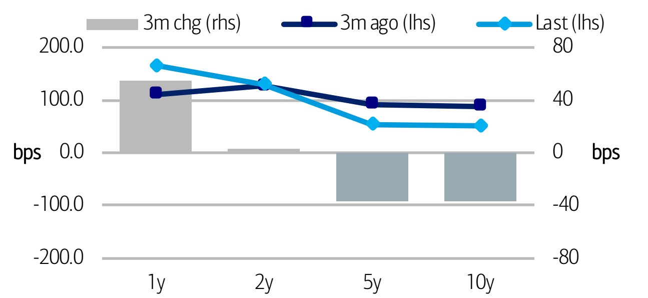
Chart 9: Term structure of basis swaps
Basis swaps 3m evolution



Source: BofA Global Research, Bloomberg

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Volatility surface: USD/CLP

Table 10: Current implied volatilities
USD/CLP current implied volatilities

	10Δ Put	25Δ Put	ATM	25Δ Call	10Δ Call
1m	17.51	17.58	18.46	20.18	22.37
3m	17.32	17.45	18.54	20.60	23.24
6m	17.40	17.48	18.59	20.78	23.66
1y	17.51	17.47	18.57	20.92	24.15

Source: BofA Global Research

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Table 11: 3m z-scores of implied volatilities
USD/CLP 3m z-scores of implied volatilities

	10Δ Put	25Δ Put	ATM	25Δ Call	10Δ Call
1m	- 1.3	- 1.3	- 1.4	- 1.4	- 1.4
3m	- 1.3	- 1.3	- 1.3	- 1.2	- 1.1
6m	- 1.1	- 1.1	- 1.2	- 1.2	- 1.2
1y	- 0.7	- 0.9	- 1.0	- 1.1	- 1.2

Source: BofA Global Research

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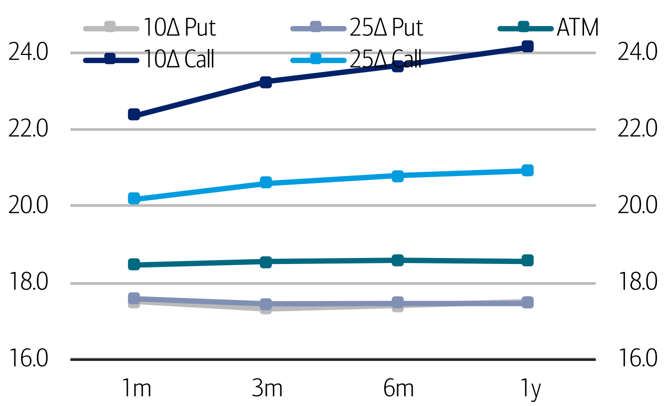
Chart 10: Term structures of implied volatilities
USD/CLP implied volatilities by maturity date



Source: BofA Global Research

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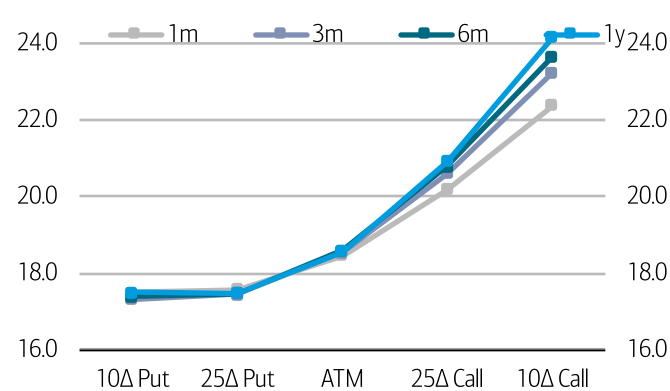
Chart 11: Implied volatility smiles
USD/CLP implied volatility by strike price



Source: BofA Global Research

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Colombia

FX Views and forecasts

View: neutral*

COP has been driven by both global and domestic factors. On the global front, dollar moves explain significant price action. On the domestic side, the policy outlook and monetary policy are the main drivers. Even though we remain cautious about COP exposure on the back of dollar uncertainty, we are gradually turning more constructive that policy moderation could materialize. We expect USD/COP at 4850 by 2023-end.

A few months ago, COP had been a major underperformer in LatAm, as investors added significant risk premium on the back of radical economic policy. Thus, we preferred to be cautious and wait for clear evidence that a significant policy pivot was taking place before adding long exposure in Colombia. Now, while we continue to recommend investors to remain cautious about having directional exposure in Colombia, we believe that the sources of risk have been gradually shifting from domestic to global.

On the domestic front, we are becoming somewhat more confident that policy will not be as radical as initially expected by the market. Health reform and labor reform do not seem to be gaining significant traction among lawmakers and the population, while pension reform, even if damaging, was presented to Congress in a more moderate version than expected. Moreover, our expectation is that Colombia's institutional checks and balances will force economic policy to moderate. We believe that sources of domestic policy risk are lower than they were over recent quarters.

However, the global outlook has turned more challenging. As we have noted previously, the Colombian peso is one of the currencies with the largest beta to global factors in LatAm (see LatAm – FX is mostly global). In particular, COP is highly sensitive to global growth expectations, so we are not surprised that the recent generalized weakening of the US dollar has supported a stronger COP. In fact, the Colombian peso has been LatAm's outperformer since the onset of concerns around financial stability in the US and Europe. The highly uncertain global outlook prompts us to be cautious about COP exposure. In particular, the possibility of a strong dollar should the market fade the cuts priced in US rates or in the event of a strong risk-off shock, could put pressure on COP. This is particularly the case given the dovish bias in BanRep, which could limit support to COP via a potentially lower carry.

Upcoming risk events

- BanRep meeting (Mar 30, Apr 28); reforms debate (1H23); regional elections (Oct).

Hedging

We recommend hedging to protect against global risks or an adverse turn in policy.

Table 12: USD/COP forecasts vs forwards

USD/COP forward and forecast comparison

	current	chg (diff)		
Spot	4614	-186		

	Forecast		Forward	
Period	current	chg (diff)	current	chg (diff)
2Q 2023	4750	-30	4696	+784
3Q 2023	4800	-	4790	+846
4Q 2023	4850	+30	4875	+888
1Q 2024	4885	+35	4955	+921

Source: BofA Global Research, Bloomberg

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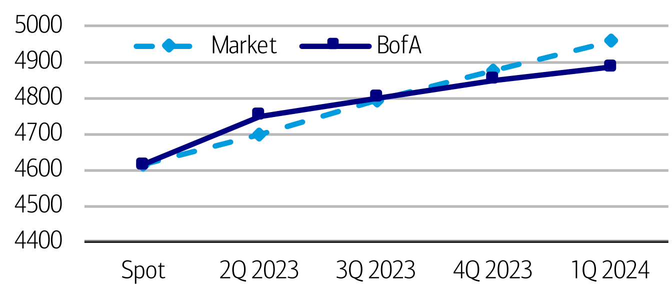
Chart 12: USD/COP forecasts

USD/COP forward and forecast comparison



Source: BofA Global Research, Bloomberg

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*Note: bullish/neutral/bearish labels are relative to year-end 2023 forward contracts.

Cross currency basis

Table 13: IBR vs 3m LIBOR basis swaps
IBR vs 3m LIBOR basis contract prices and ranges

Maturity	Last	1w chg	3m chg	1y chg	Min	Last vs 1y Avg	Max	1y Avg	1w vol	3m vol	3m z-score	1y z-score
1y	-25	-8	37	-66	-74		41	-28	11	80	1.2	0.1
2y	-63	3	37	-119	-109		57	-46	10	74	1.6	-0.4
5y	-105	7	38	-150	-144		45	-67	9	68	3.0	-0.7
10y	-98	3	44	-147	-144		49	-64	9	63	3.0	-0.7

Legend: [redacted]nt value; : 1y average. The z-score measures the distance between the current value and the mean in standard deviation units.
Source: BofA Global Research, Bloomberg

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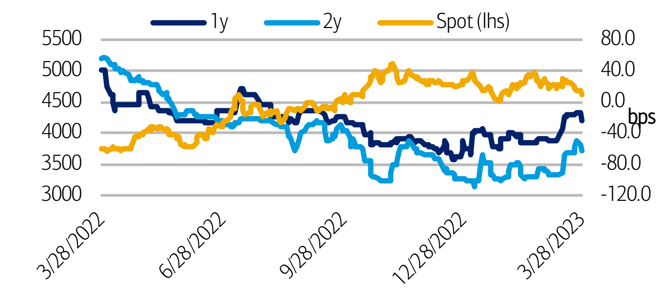
Chart 13: Short-term basis swaps vs USD/COP spot
Short-term basis swaps and USD/COP comparison



Source: BofA Global Research, Bloomberg

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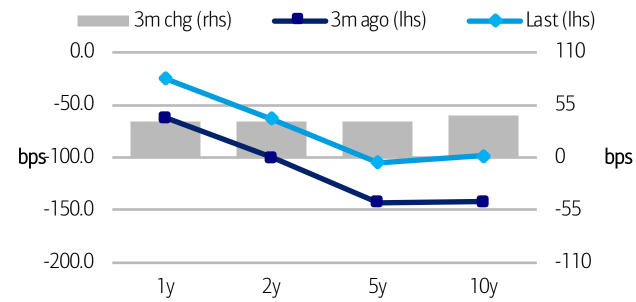
Chart 14: Term structure of basis swaps
Basis swaps 3m evolution



Source: BofA Global Research, Bloomberg

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Volatility surface: USD/COP

Table 14: Current implied volatilities
USD/COP current implied volatilities

	10Δ Put	25Δ Put	ATM	25Δ Call	10Δ Call
1m	17.65	17.74	18.75	20.69	23.15
3m	17.80	17.81	18.78	20.79	23.42
6m	18.09	18.02	18.96	21.01	23.78
1y	18.40	18.18	19.05	21.18	24.21

Source: BofA Global Research

BofA GLOBAL RESEARCH

Table 15: 3m z-scores of implied volatilities
USD/COP 3m z-scores of implied volatilities

	10Δ Put	25Δ Put	ATM	25Δ Call	10Δ Call
1m	- 0.3	- 0.1	+0.1	+0.4	+0.6
3m	- 0.7	- 0.5	- 0.2	- 0.0	+0.1
6m	- 0.3	- 0.1	+0.2	+0.3	+0.2
1y	- 0.1	+0.2	+0.5	+0.5	+0.2

Source: BofA Global Research

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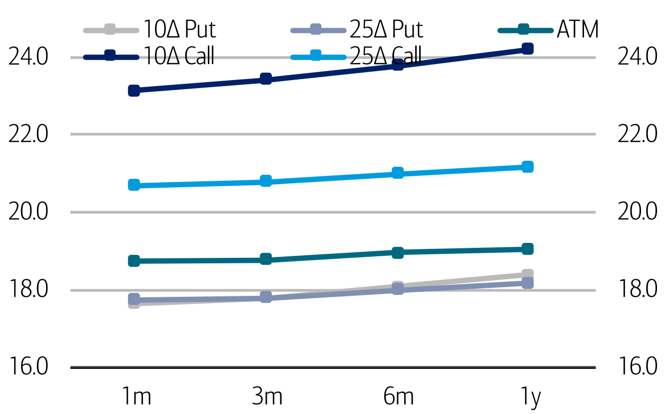
Chart 15: Term structures of implied volatilities
USD/COP Implied volatilities by maturity date



Source: BofA Global Research

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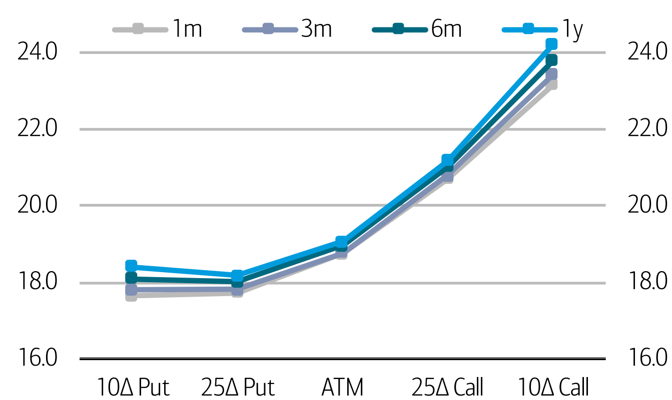
Chart 16: Implied volatility smiles
USD/COP implied volatility by strike price



Source: BofA Global Research

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Mexico

FX Views and forecasts

View: bearish*

The Mexican peso weakened substantially, triggered by a risk-off shock that was amplified by crowded long positioning. Most of the move has been faded, but we remain cautious despite the attractive carry. We deem valuation to be rich in real terms, which coupled with still heavy positioning and an uncertain global outlook, means that MXN continues to have asymmetric risk-reward. We expect USD/MXN at 20.00 by 2023-end.

Early in the year, we decided to turn neutral on MXN (see Mexico - Reducing long exposure to MXN). Our view was that, despite our expectation that the five factors supporting the peso – carry, tight fiscal policy, narrow CA deficit, political stability, and nearshoring – would prevail in the short-term, crowded long positioning represented a significant risk. This could act as an amplifier in the event of a risk-off shock (see The Kryptonites to the Super Peso). Specifically, we were concerned that the market would price a deep US recession, which in our view was a scenario that could hit the peso.

The recent market turmoil driven by concerns about financial stability in the US provided an example of the impact that a risk-off could have on the peso. In just about a week, MXN depreciated north of 5.5%. Most of the selloff has been faded, but we continue to be cautious about long MXN exposure. In our view, the potential for a deep recession in the US has not been fully priced by markets despite signals of banking sector stress. This is evident by the diverging reaction between US rates and equities. While rates are pricing cuts in the short-term amid concerns about a potential slowdown driven by the banking sector downturn, equities have rallied, suggesting a risk-off is not fully priced.

On the domestic front, we still expect Banxico to remain hawkish as it continues to fight a sticky inflation in Mexico. This should continue providing some support on the peso. Yet, we still believe that despite the recent repricing, MXN is not attractive in terms of valuation. This limits upside and therefore negatively impacts risk-reward. Overall, we continue to be neutral MXN and prefer to wait for better entry points to have long MXN exposure. The only exception is our sell CNH/MXN recommendation, which we keep as a structural nearshoring trade (see Nearshoring in Mexico: A lifetime opportunity). One final risk worth noting is the escalation of trade-related tensions with the US amid recent news that the US is preparing an ultimatum in Mexico's energy dispute.

Upcoming risk events

- Banxico meeting (Mar 30); USMCA consultation (1H23)

Hedging

We recommend hedging given still heavy MXN positioning and global risks.

Table 16: USD/MXN forecasts vs forwards

USD/MXN forward and forecast comparison

	current	chg (diff)		
Spot	**18.10**	**-0.57**		

	Forecast		Forward	
Period	**current**	**chg (diff)**	**current**	**chg (diff)**
2Q 2023	19.10	-0.20	18.42	-2.45
3Q 2023	19.50	-0.10	18.76	-2.42
4Q 2023	20.00	+0.10	19.10	-2.41
1Q 2024	20.20	-	19.42	-2.46

Source: BofA Global Research, Bloomberg

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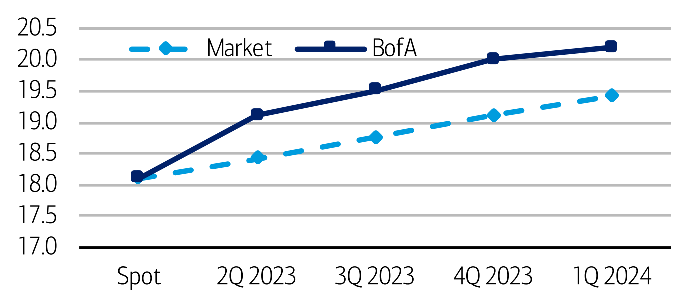
Chart 17: USD/MXN forecasts

USD/MXN forward and forecast comparison



Source: BofA Global Research, Bloomberg

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*Note: bullish/neutral/bearish labels are relative to year-end 2023 forward contracts.

Cross currency basis

Table 17: 28d TIIE vs 1m LIBOR basis swaps
28d TIIE vs 1m LIBOR basis contract prices and ranges

Maturity	Last	1w chg	3m chg	1y chg	Min	Last vs 1y Avg	Max	1y Avg	1w vol	3m vol	3m z-score	1y z-score
1y	-27	-11	19	-9	-70		-12	-36	9	67	0.6	0.7
2y	-9	-12	28	-14	-43		12	-18	7	48	1.3	0.7
5y	31	3	54	-22	-32		55	8	7	53	2.8	1.2
10y	31	5	67	-50	-40		82	14	8	58	3.3	0.6

Legend: : [redacted]nt value; : 1y [redacted]verage. The z-score measures the distance between the current value and the mean in standard deviation units.
Source: BofA Global Research, Bloomberg

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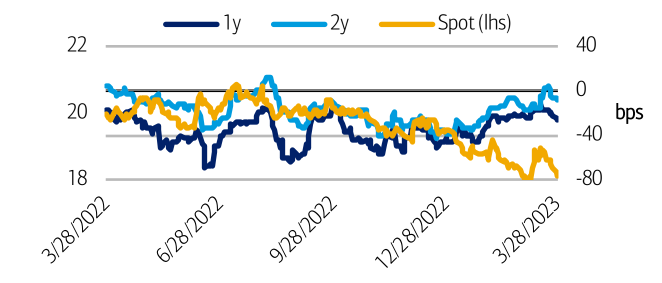
Chart 18: Short-term basis swaps vs USD/MXN spot
Short term basis swaps and USD/MXN comparison



Source: BofA Global Research, Bloomberg

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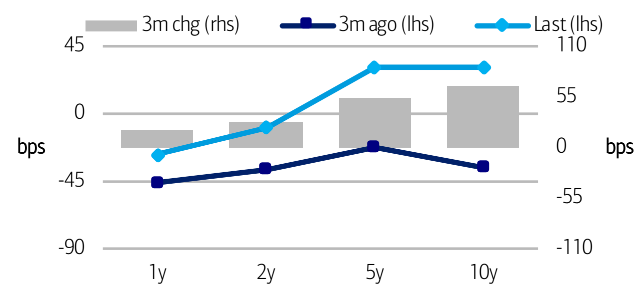
Chart 19: Term structure of basis swaps
Basis swaps 3m evolution



Source: BofA Global Research, Bloomberg

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Volatility surface: USD/MXN

Table 18: Current implied volatilities
USD/MXN current implied volatilities

	10Δ Put	25Δ Put	ATM	25Δ Call	10Δ Call
1m	12.83	13.09	14.28	16.34	18.85
3m	12.24	12.46	13.64	15.76	18.43
6m	11.95	12.16	13.29	15.36	18.04
1y	11.76	11.91	13.01	15.11	17.87

Source: BofA Global Research

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Table 19: 3m z-scores of implied volatilities
USD/MXN 3m z-scores of implied volatilities

	10Δ Put	25Δ Put	ATM	25Δ Call	10Δ Call
1m	+1.4	+1.3	+1.4	+1.4	+1.4
3m	+1.5	+1.5	+1.5	+1.6	+1.6
6m	+1.5	+1.6	+1.6	+1.6	+1.5
1y	+1.3	+1.5	+1.6	+1.5	+1.5

Source: BofA Global Research

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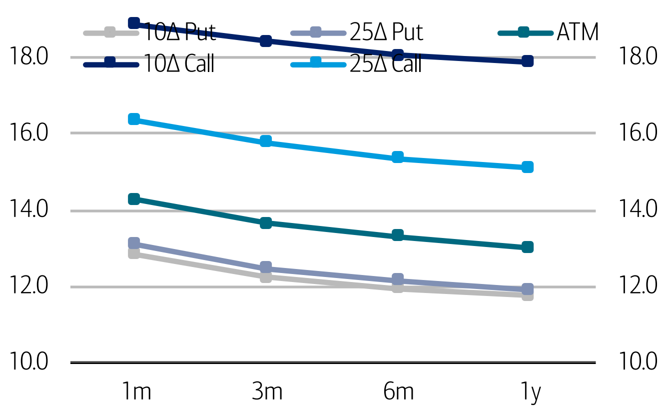
Chart 20: Term structures of implied volatilities
USD/MXN implied volatilities by maturity date



Source: BofA Global Research

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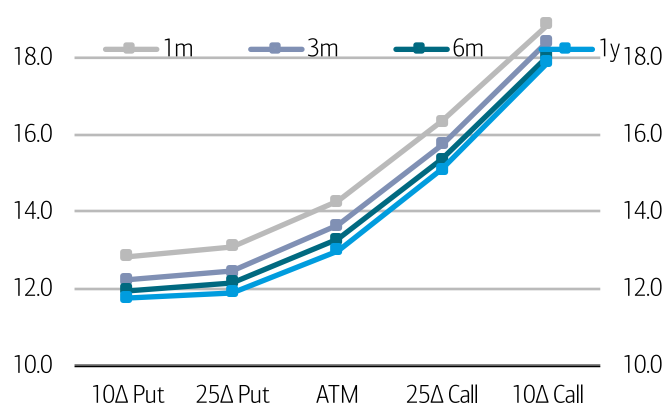
Chart 21: Implied volatility smiles
USD/MXN strike price and implied volatility



Source: BofA Global Research

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Peru

FX Views and forecasts

View: neutral*

PEN has benefitted by its low beta to global factors during the most recent market turmoil. While this should at least partially shield PEN from global swings, we prefer to wait for clear signs of political noise easing to enter long PEN positions. We expect USD/PEN at 3.82 by 2023-end.

In our view, the outlook for the Peruvian sol could be improving. On the global side, it is the currency in LatAm with the lowest beta to global factors, partly due to the central bank's FX intervention policy to curtail FX volatility. This has proved useful at a moment where global uncertainty has substantially increased on the back of concerns about financial stability. As a result, PEN has been the second-best performing currency in the region since the onset of concerns, appreciating about 0.7%.

On the domestic side, locals are becoming increasingly convinced that the recent political noise is stabilizing and could gradually dissipate (see Peru Trip Notes: Dealing with domestic shocks). Aggressive protesting and roadblocks have seemingly eased despite the lack of political support for early elections. However, we prefer to be cautious until we see more concrete and structural evidence of political stabilization. Historically, we tend to see PEN depreciation around elections, so a resumption of protests potentially leading to early elections could put pressure on the currency. Headline risk, such as recent news that some lawmakers were presenting a bill to impeach President Boluarte, will most likely continue.

Meanwhile, the domestic macro story is still supportive. Fiscal concerns are relatively low, while the drag on growth and inflation from recent protests is expected to be transitory. We believe BCRP will most likely keep rates on hold until it sees a downward trend in inflation and inflation expectations, which implies that BCRP will be unable to cut rates this year. This should provide some support to PEN via carry. Granted, the interest rate differential could narrow with the Fed still hiking, but PEN's very low beta to global factors will at least partially shield the Peruvian Sol from global swings. High copper prices will also be supportive for PEN.

Upcoming risk events

- BCRP meeting (Apr 13); early elections (TBD); possibility of El Niño (2Q23); possibility for credit rating action (any moment).

Hedging

We still recommend short-term hedging, given some lingering political noise.

Table 20: USD/PEN forecasts vs forwards
USD/PEN forward and forecast comparison

	current	chg (diff)		
Spot	**3.75**	**-0.09**		
	Forecast		**Forward**	
Period	**current**	**chg (diff)**	**current**	**chg (diff)**
2Q 2023	3.78	-0.09	3.77	-0.24
3Q 2023	3.80	-0.08	3.79	-0.24
4Q 2023	3.82	-0.07	3.81	-0.25
1Q 2024	3.84	-0.06	3.82	-0.27

Source: BofA Global Research, Bloomberg

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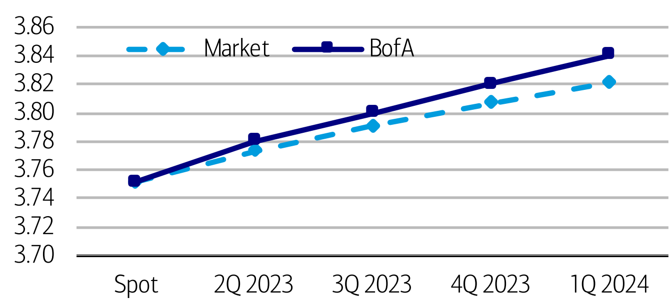
Chart 22: USD/PEN forecasts
USD/PEN forward and forecast comparison



Source: BofA Global Research, Bloomberg

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*Note: bullish/neutral/bearish labels are relative to year-end 2023 forward contracts.

Venezuela

FX Views and forecasts

View: bearish*

Inflationary pressures are spiking amid government spending increases and lower oil prices, with risks of hyperinflation. We see VES/USD at 309 by 2023-end.

Inflation accelerated to peak at 39% in January (20% in February), consistent with hyperinflation, interrupting the disinflation observed in H122 (8% mom average). The acceleration comes amid a faster depreciation of the Bolivar (162% jump last 90days) after the drop in oil prices in H2 and FX reserves, and probably lack of fiscal control. Inflation is at 400% yoy in January, still below 660% in 2021, but could exceed 1000% again in 2023 if the government doesn't take measures.

Oil production bounced back to 670k in January (similar to 2022 average of 675k) after a drop to 550kbpd in August (amid mechanical failures and power outages) and is off the 500k all-time low. Exports had surged after oil shipments to Europe resumed. In May, the US administration allowed European firms to ship Venezuelan oil back to Europe.

The government has showed some signs of pragmatism. It allowed a de-facto dollarization and it opened up to some business with the private sector (and sold some equity in state owned enterprises). But the oil shock and the inflation pick up may slow down GDP again. PDVSA president resigned amid a corruption investigation.

A government negotiator said that progress is being done with the opposition, which could open the door to unfreeze Venezuelan assets abroad for about $3.2bn, following negotiations in Mexico. The war in Ukraine opened opportunities for the oil sector in Venezuela. A meeting took place in Caracas in March between US delegates and Venezuelan authorities. The US has requested free elections and reforms in the oil sector, according to Reuters. License for Chevron to continue operations and export oil to US has been granted.

Recall Venezuelan Juan Guaido's interim government ended in January (had started in January 2019) after the opposition didn't support him. This shows the divisions between Voluntad Popular party and the rest of the opposition Unitary Platform. The 2015 elected National Assembly continues operating (Dinorah Filguera is the new Assembly leader) and a commission would manage assets abroad (though it faces some hurdles).

Table 21: USD/VES forecasts

USD/VES forward and forecast comparison

	current	chg (diff)
VEF	24	+0.38
	DICOM	
Period	**current**	**chg (diff)**
2Q 2023	58	34
3Q 2023	133	102
4Q 2023	309	266
1Q 2024	533	477

Source: BofA Global Research

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*Note: bullish/neutral/bearish labels are relative to year-end 2022 forward contracts.

FX Models

Short-term: Compass 30

Table 22: Compass30 signals for LatAm
Compass30 Signals for LatAm currencies

	Spot	Forecast	Forward	Exp Ret	Std Dev	Signal
BRL	5.23	5.25	5.25	0.1	5.7	Neutral
CLP	807.36	818.62	809.74	-1.1	4.6	Neutral
COP	4679.00	4598	4709	2.4	4.2	Long
MXN	18.36	19	18	-2.8	5.4	Short
PEN	3.77	3.77	3.78	0.3	1.5	Neutral

Source: BofA Global Research. Signals as of 03/27/2023.

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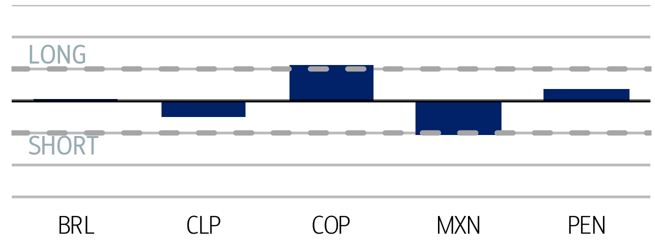
Chart 23: Compass30 signals for LatAm
Compass30 Signals for LatAm currencies



Source: BofA Global Research. Signals as of 03/27/2023.

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Compass30 uses macroeconomic and financial variables to predict currency returns over the following 30 days. For more details about the model, see our Compass 30 Viewpoint.

Medium-term: Compass BEER

Table 23: Compass BEER
Compass BEER Valuations for LatAm currencies

Currency	Spot	Fair value vs USD	Bilateral valuation (%)	Multilateral valuation (%)
ARS	208.3	249.0	18%	28%
BRL	5.2	3.7	-32%	-26%
CLP	793.7	678.8	-16%	-8%
COP	4,614.3	4,067.2	-13%	-3%
MXN	18.1	18.6	3%	5%
PEN	3.8	3.2	-16%	-10%

Source: BofA Global Research. Fair values as of 03/29/2023.

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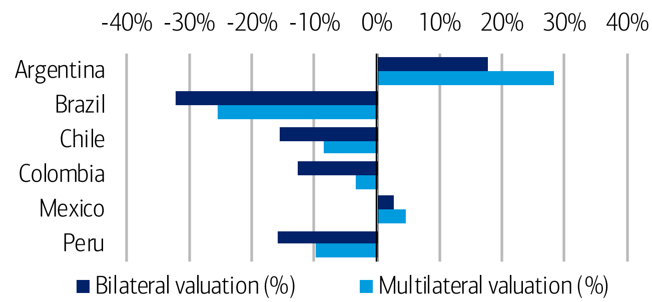
Chart 24: Compass BEER valuations for LatAm
Compass BEER Valuations for LatAm currencies



Source: BofA Global Research. Fair values as of 03/29/2023

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Compass BEER is our medium-term valuation model for EM currencies. It estimates real exchange rate fair values based on macro fundamentals. For more information about the model, see our Compass BEER Viewpoint.

Long-term: Compass FX

Table 24: Compass FX
Compass FX Valuations for LatAm currencies

	Fair Value vs USD	Spot	Bilateral Misalignment vs USD (%)	Trade-weighted Misalignment (%)
Argentina	250.07	208.24	16.72	13.86
Brazil	5.85	5.15	11.94	14.19
Chile	1054.82	789.58	25.15	34.39
Colombia	5250.42	4659.56	11.25	11.79
Mexico	19.96	18.14	9.12	11.16
Peru	4.06	3.76	7.37	5.95

Source: BofA Global Research. Fair values as of 03/27/2023.

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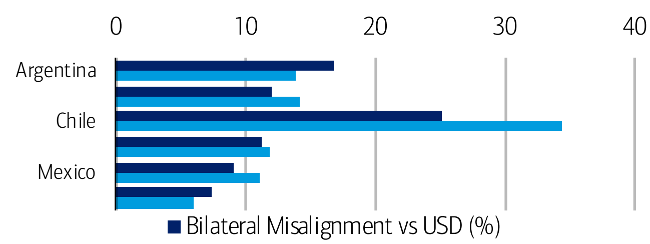
Chart 24: Compass FX
Compass FX Valuations for LatAm currencies



Source: BofA Global Research. Fair values as of 03/27/2023.

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Compass FX provides estimates of long-term equilibrium exchange rates for 22 emerging market currencies, both trade-weighted and bilateral (vs the USD and EUR). For more information about the model, see our Compass FX Viewpoint.

Forecast details

Table 25: LatAm FX Forecasts
BofA quarter-end FX forecasts

Currency	2023 Q2	2023 Q3	2023 Q4	2024 Q1	2024 Q2	2024 Q3	2024 Q4
USD/ARS (official)	242	280	417	482	559	647	748
USD/ARS (blue chip)	508	616	729	772	866	970	1123
USD/BRL	5.15	5.18	5.20	5.25	5.30	5.35	5.40
USD/CLP	810	820	825	830	835	840	845
USD/COP	4,750	4,800	4,850	4,885	4,920	4,960	5,000
USD/MXN	19.1	19.5	20.0	20.2	20.5	20.7	21.0
USD/PEN	3.78	3.80	3.82	3.84	3.86	3.88	3.90
USD/VES	58	133	309	533	922	1592	2752

Source: BofA Global Research.

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Table 26: Comparison against consensus forecasts
BofA and Consensus quarter-end FX forecast comparison

	2023 Q2			2024 Q2		
Currency	**BofA**	**Consensus**	**% Diff**	**BofA**	**Consensus**	**% Diff**
USD/ARS (official)	242	210	15.4%	559	370	51.2%
USD/BRL	5.15	5.18	-0.7%	5.30	5.15	2.9%
USD/CLP	810	818	-1.0%	835	823	1.5%
USD/COP	4,750	4,795	-0.9%	4,920	4,700	4.7%
USD/MXN	19.1	19.02	0.4%	20.5	19.8	3.6%
USD/PEN	3.78	3.85	-1.8%	3.86	3.88	-0.5%

Source: BofA Global Research, Consensus Economics.

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