Global FX weekly

Still in search of a safe landing

09 February 2024

FX Research
Global

The view

G10: Strong economy and falling inflation not sustainable; adjustment unlikely to be smooth for markets. We discuss how to position tactically and structurally.

EM: Carry continues to drive EM FX despite the post US payroll USD rebound. Short EUR is the favored funder, but we flag shifting geopolitical risks to periphery EM.

G10 Themes

Macro: Fed re-pricing; other G10 CBs; global data trends. USD support as long as trends hold, though don't overlook other CB pushback on early cuts.

Flows: USD buying across the board, partial reversal from end-23. Driven by hedge funds, more correlated with Asia flows. Activity in options along similar lines.

CHF: The SNB has been intervening, whilst pulling back from FX sales. Supports structural bearish case for CHF. We are long GBP/CHF and EUR/CHF.

CAD: 1.3% growth for 2024, 2% inflation by 2025. The market may be underpricing BoC rate cuts and pricing a high terminal. We expect USDCAD at 1.30 by year-end.

EM Themes

Long BRL/MXN: We still like buying BRL/MXN. Recent underperformance due to strong US growth, weak euro exchange rate and high carry in MXN.

Short EUR/TRY: We enter this position on TRY stabilization and attractive carry dynamics amid an improving external position.

TWD: We conducted a 3-day marketing tour in Taiwan and met with Taiwanese lifers and corporates to discuss the FX outlook.

SAR: The revised Aramco production capacity target reflects oil market fundamentals, existing spare capacity and fiscal pressures.

VOL

Expect higher vol when the USD eventually enters a new bearish trend with the start of the Fed cutting cycle. As a result, we see 6m USD put skew to richen vs. calls.

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G10 FX Strategy
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Timestamp: 09 February 2024 12:00AM EST

Our medium-term views

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Exhibit 1: Our medium-term views
G10 and EM FX medium-term views

G10	We are bearish USD, looking for EURUSD at 1.15 by end-2024. In our base case, the US economy starts recoupling with the rest of the world, US disinflation continues, and the Fed cuts rates, supporting risk sentiment and pushing the USD lower from an overvalued level. But risks abound: in our main risk scenarios the USD softens less than we expect, or even strengthens. We expect a stronger EUR and GBP this year mostly vs USD—we remain bearish on both Euro area and UK growth, seeing both EURUSD and cable driven by the US recoupling. On JPY, we remain more cautious than consensus, primarily on carry—we expect USDJPY to fall to 142 by end-2024. We expect high-beta G10 FX to perform well but have some reservations on NZD and SEK. We expect EURCHF modestly higher in line with the symmetric SNB stance.
EM	Our client conversations suggest investors are lacking in directional EM FX conviction and leaning more towards relative value trades. In Asia, our preference in relative value FX is for short CNH against long SGD and INR, where positive carry is enhanced, and volatility contained by MAS and RBI intervention. We like long IDR short PHP. In Latam, we favor long BRL against short MXN based on valuations, acknowledging that market positioning is long both currencies against short USD. In EMEA, we close short CZK, long HUF and enter short EUR/TRY on attractive carry dynamics and an improving external position in Turkiye.

Source: BofA Global Research

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Our key forecasts

Exhibit 2: Key BofA G10 and EM FX forecasts
Forecasts as of 8-Feb-2024

(EOP)	YE 2021	YE 2022	YE 2023	1Q24	2Q24	3Q24	YE 2024	YE 2025
EUR/USD	1.14	1.07	1.10	1.07	1.10	1.15	1.15	1.20
USD/JPY	115	131	141	145	143	142	142	136
GBP/USD	1.35	1.21	1.27	1.23	1.26	1.31	1.31	1.40
AUD/USD	0.73	0.68	7.00	0.66	0.68	0.71	0.71	0.71
USD/CNY	6.36	6.90	7.10	7.45	7.40	7.10	6.90	6.70
USD/BRL	5.58	5.29	4.92	4.90	4.88	4.80	4.75	5.00
USD/INR	74.34	82.74	83.21	83.00	82.50	82.00	82.00	81.00
USD/ZAR	15.94	17.04	18.36	18.60	18.50	17.70	17.80	18.40

Source: BofA Global Research. Forecasts as of 8-Feb-2024.

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What we particularly like right now

Exhibit 3: Our latest G10 and EM FX trade recommendations
What we particularly like right now

G10	
Buy GBP/CHF via 3m call spread	A tactical trade given the benign risk backdrop to position for policy divergence/carry
Buy USDSEK	A tactical trade supported by technicals to position for US data resilience and a hawkish Fed and a dovish Riksbank
Buy NOKSEK	NOKSEK can benefit from relative Norges/Riksbank stance, central bank flows, likely lighter positioning, geopolitics
Sell EUR/JPY via 3m put spread	Near-term constructive JPY on the BoJ. Markets could price more ECB cuts in 2H also given the weak European data
Buy 3m EUR/CHF ratio call spread	SNB symmetric reaction function implies intervention to weaken CHF or (more likely) less FX sales to taper balance sheet
Buy EUR/USD	We are bearish USD in 2024 on the start of Fed rate cutting cycle and normalization of the overvalued USD
Buy 4m EUR/GBP vol swap	EURGBP implied is at a historical low and should rise on diverging EZ-UK economic and fiscal outlooks
EM	
Sell EURTRY	We enter this position on TRY stabilization and attractive carry dynamics amid an improving external position
Short PHP/IDR	We enter long IDR vs/ short PHP on better BoP and fiscal performance in Indonesia
Buy BRL/MXN	Investors are over-positioned long in both MXN and BRL, but we believe BRL fundamentals are better and policy better priced

Source: BofA Global Research.

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For complete list of open trades, and those closed over the past 12 months, please see
Trade Recommendations G10 and EM Alpha Trade Recommendations

sections of the report.

G10 Central Bank calls

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Exhibit 4: G10 Central Bank calls

No G10 central bank meetings next week

Country	Next Meeting	BofA	Consensus	Prior	Narrative
US	20-Mar	5.25-5.50%	5.25-5.50%	5.25-5.50%	We now look for the rate cut cycle to begin in June and expect 25bp rate cuts in June, September, and December. This would mean 75bp of rate cuts this year and we retain our view of 100bp of rate cuts in 2025. We also push out the timing of our expected QT slowdown announcement from the March meeting to the May meeting. In addition to altering the timing of tapering, we also adjust the path of QT slowdown. We no longer expect a $15b/m taper in the US Treasury redemption cap at each FOMC meeting. Instead, we now expect a reduction in the redemption cap from $60b/m to $30b/m and for this to remain open-ended. Our view is it can remain at this level until end '24.
Eurozone	7-Mar	4.00%	-	4.00%	We expect quarterly cuts in 2024 from June, one cut per meeting in 2025 until the depo is at 2%, and then more in 2026. We still think the ECB prefers to do too much rather than too little (in contrast to the Fed) which, to us, means the risk of faster cuts in 2H24 is higher than the risk of cuts before June. We still expect the operational framework review to bring an adjustment in the minimum reserve ratio to 2-3% and the ECB to stick to the pre-announced plan to reduce PEPP reinvestments by half in 2H24 and stop fully thereafter.
Japan	19-Mar	-0.10%	-	-0.10%	Following the hawkish January Summary of Opinions, we see a very high likelihood that the central bank will exit negative interest policy (NIRP) and overhaul the current policy framework in its next two MPMs, in March and April. Though the latter remains our base case, we think the March meeting is very much live.
UK	21-Mar	5.25%	5.25%	5.25%	We continue expect the BoE on hold at 5.25% until Aug-24 and a cutting cycle of 25bp per quarter from there. The UK will be the last of the major central banks to start the cutting cycle and is likely to move slower, at least vs the ECB. We see a risk that the BoE cuts rates 25bp per meeting when it starts in August of this year. We think that would have short legs if it were to materialise: faster cuts in 2024 would likely need to be followed by, likely, a long pause down the line or, under some circumstances, even some small reversal of the move.
Canada	6-Mar	5.00%	-	5.00%	We expect five rate cuts in 2024 and another 3 in 2025. We believe the first cut will happen in June as the BoC will likely wait until core inflation and wage growth show a clear downward trend. The main risk to our view is the BoC decides to change language in March and cuts in April, which is more likely if the US Fed were to cut in March
Australia	19-Mar	4.35%	4.35%	4.35%	We expect no rate cuts in 2024 and the cash rate at 3.50% by YE 25 with risks for earlier cuts than we assume.
New Zealand	28-Feb	5.50%	-	5.50%	We expect the RBNZ to downgrade its hawkish stance in Feb but not a full dovish pivot. The RBNZ is now a single inflation mandate Reserve Bank, so sustainable employment will not be in focus going forward. We expect seven rate cuts in 2024 and another 3 in 2025.
Switzerland	21-Mar	1.75%	-	1.75%	We expect the SNB to start cutting later (September 2024) and less (quarterly to 0.5% by September 2025) than the ECB, with the risk of cutting even less. We now expect a more symmetric than before approach toward CHF.
Norway	21-Mar	4.50%	-	4.50%	We continue to look for two rate cuts in 2024, starting in September, and another five in 2025. Symmetric risks.
Sweden	27-Mar	4.00%	4.00%	4.00%	We look for three rate cuts in 2024, starting in June (but May is now live), and another 5 in 2025, similarly to the ECB. Downside risks to this path.

Source: BofA Global Research, Bloomberg consensus forecasts as of 8-Feb-2024.

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The view

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The big picture puzzle and the road ahead

The real economy puzzle

The real economy keeps defying gravity. Not only have G10 economies avoided the recession that consensus had expected when the tightening cycle started, but the unemployment rate remains stuck at an all-time low in most cases. All possible explanations suggesting that this was temporary and that the real economy was about to turn have repeatedly proven wrong. In some cases, concerns for reacceleration have now emerged, particularly in the US. The Eurozone economy has been much weaker than the US, but the region has also avoided a recession and its unemployment rate is also at an all-time low.

We have argued that the real economy's strong performance has to do with drivers that should start to fade this year. Monetary policy tightening has yet to affect the real economy much, as most companies and households remain locked in low interest rate loans. Fiscal policy has been very loose in the US and not necessarily tight in most of the rest of the world. And the massive fiscal stimulus during the pandemic left behind excess savings, particularly in the US. In our view, these three reasons explain both the strong real economy despite the most aggressive monetary policy tightening since Volcker and the US decoupling from the rest of the world. However, approaching loan maturities suggest that tight monetary policy should start affecting the real economy soon, fiscal policy is tightening in most cases this year, and excess savings are running out. Despite taking much longer than expectations, we think the landing is still coming.

The inflation puzzle

Despite the strong economy, inflation has been falling. However, we have been arguing that this is because of supply forces that have very little to do with monetary policy tightening. To a large extent, it has to do with the drop in energy prices since 2022 and the opening of pandemic-related supply bottlenecks. Monetary policy tightening has mostly kept the inflation outlook from getting worse by safeguarding central bank credibility and containing inflation expectations.

We are now concerned that inflation will be stickier, as these "easy wins" are behind and the stretched labor market could keep supporting wages. Some of the labor market data may be backward-looking, but so far not much else in the economy seems to be raising any red flags for a downturn ahead.

The road ahead

In our soft-landing baseline, the above suggests that the economy will slow, with inflation sticky but moving in the right direction this year. This is consistent with a gradual central bank easing cycle—later and slower than market pricing. US recoupling and Fed cuts should help weaken the USD in this case, from a still overvalued level, but later in the year. Even if other central banks cut rates at the same time, we have argued that Fed cuts matter more for markets because they also affect risk sentiment.

We are not there yet. The US economy remains too strong and markets keep getting disappointed about early and fast rate cuts. As a result, the USD remains strong—consistent with our Q1 forecasts. Our view is that the soft-landing scenario and the associated gradual easing cycle will have to wait for this summer.

The path is unlikely to be smooth. Our baseline is an ideal scenario in which growth slows and inflation keeps falling—even if stickier than last year—at about the same time, allowing central banks to start cutting rates in June. However, the timing is unlikely to be so perfect.

One can think of alternative scenarios for the next 1-2 quarters. Growth could remain resilient, while inflation could get stuck on the way, in which case central banks will not cut rates in June. Inflation could even reaccelerate in some cases, with markets pricing out all cuts for this year or even pricing more hikes in some cases. In another scenario, growth could slow but inflation could still be sticky, in which case central banks may have to wait longer before cutting rates. The worst scenario would be if growth slows and inflation gets stuck or even reaccelerates, either because of lagged effects or new shocks, forcing central banks to keep policies tight as they deal with stagflation.

Even if the soft-landing baseline eventually turns out to be right, we believe that we will be trading probabilities of such alternative scenarios in the next one to two quarters, if not for longer. Indeed, we argue that this is what we have been trading since central banks stopped hiking mid-last year. It is also likely that different G10 economies will find themselves in different scenarios, affecting FX markets and beyond, accordingly.

How we position in the meantime

We are short CHF vs. EUR and GBP, to position for CHF weakness from an overvalued level as the SNB stops shrinking its balance sheet, has started to intervene and has expressed concerns about the strong currency. We are **short SEK vs. USD and NOK** on the back of strong US data, NOK undervaluation and a dovish Riksbank vs. the Fed and the Norges Bank. **We are tactically short EURJPY** on BoJ policy normalization and risks of more ECB cuts priced in 2H because of weak data. **We remain long EURUSD for the year**, expecting the USD to weaken as the US economy slows and the Fed starts cutting rates later in the year (year ahead trade). **We also remain long EURGBP short-term vol**, as a year ahead relative value vol trade. (See Exhibit 25 for a list of our G10 open trades and Exhibit 26 for trades closed within the past 12 months).

EM FX View – Carrying the burden of uncertainty.

Taken at first glance, last week's blockbuster US employment report is a USD positive, pushing the DXY index to fresh three-month highs. However, closer inspection of EM FX returns shows that EM carry currencies are making a partial comeback nonetheless. MXN, ZAR, and BRL show modest gains, albeit under 1%.

As we pointed out in last week's issue, the funding base of EM carry trade matters. The underperformance of EUR, CHF and TWD versus long EM carry continues to validate carry trade strategies. However, there are also lessons to be learned in that popular JPY and CNH funding trades have not been as successful over the past week.

Policy expectations

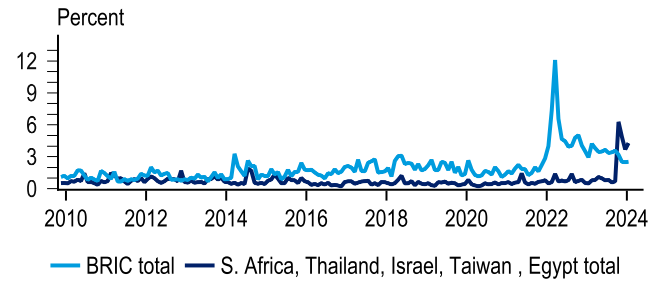
The drivers of EM FX carry trades come down to monetary policy expectations. Ultimately, the market's belief that the Fed will still deliver rate cuts this year is conducive to a risk-on carry environment. The fact that the March Fed rate cut is effectively priced out is taken as "the worst is over" for the time being, inviting more carry trades back in. However, the choice of funding currency is complicated for JPY and CNH due to the respective prospect of a BoJ exit policy from negative interest rates in April and China stimulus by the March National People's Congress. For this reason, the path of least resistance in funding EM FX carry trades appears to be EUR and CHF.

Enemy number of one of carry trades – uncertainty

EM carry trades are notoriously vulnerable to volatility, triggering a rush to safe-haven currencies and a violent carry unwind. Taken at face value overall EM risk appears to be subsiding, especially in geopolitics. However, it is important to recognize the shifting trends. Exhibit 5 shows the aggregation of geopolitical risk among BRIC countries (Brazil, Russia, India and China) as measured by the text-mining of key works in the public media domain. These have significantly declined as a share of geopolitical concerns.

However, there is a significant peak and rise in peripheral EM concerns, which now exceed BRIC and are defined by S. Africa, Thailand, Israel, Taiwan and Egypt. Finally, Exhibit 6 shows that trade policy uncertainty has significantly subsided relative to monetary policy uncertainty. However, with the US election cycle expected to ramp up, trade policy could re-emerge as a key source of uncertainty in the second half of 2024.

Exhibit 5: Peripheral geopolitical risk is > BRIC risk
Geopolitical risk as assessed by public media coverage



Source: BofA Global Research, Macrobond, Matteo Iacoviello indices
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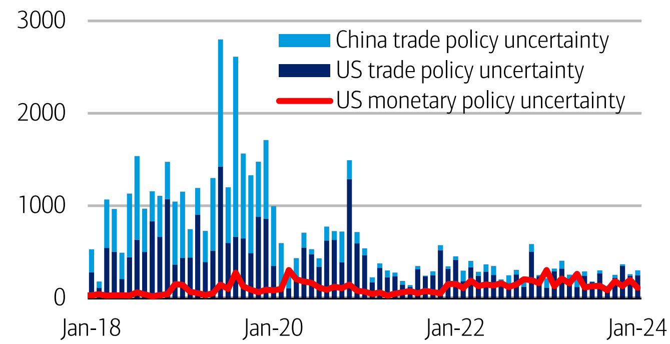
Exhibit 6: Trade policy risks have shrunk relative to Fed policy risk
With the US election cycle approaching – trade policy uncertainty could rise



Source: BofA Global Research, Bloomberg, Baker, Bloom, Davis policy uncertainty indices
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G10 Themes
3 FX questions after a big macro week

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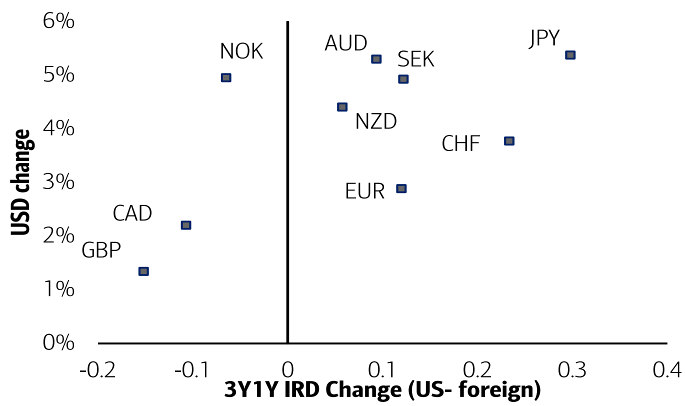
Link to the full report: Liquid Insight: 3 FX questions after a big macro week 07 February 2024

- After a big few weeks of CB meetings and econ data; we reflect on 3 key questions for the FX market. These relate to…
- (1) impact of Fed re-pricing; (2) evolution of other G10 CB outlooks; and (3) how does this fit with recent global data trends
- Upshot is ongoing USD support as long as trends hold, though don't overlook other CB pushback on early cuts

Exhibit 7: YTD change in USD vs. G10 & interest rate differential change (3y1y OIS)
USD has appreciated vs all G10 this year, despite mixed rate differential shifts



Source: Bloomberg; BofA Global Research. +FX% = USD appreciation; +IRD change favors US

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3 Questions in the wake of big few weeks in macro

Financial markets have had a lot to process over the past few weeks, including (but not limited to) 8 of the G10 central banks having meetings, and strong US labor data contributing to further Fed re-pricing. Here we consider 3 key questions for the FX market in the wake of these developments: (1) How has the USD reacted to composition of Fed re-pricing?, (2) How have CB outlooks evolved across the G10?, and (3) Do these CB outlooks fit with recent G10 data trends?

Ultimately, ongoing US data resilience and a more cautious Fed should continue to support the USD in the near-term, until something changes more materially. That said, there's only so much milage the USD can get out of another few months of pushed back cuts, particularly vs. other currencies whose associated central banks are doing the same.

FX flows in ’24 – half a step back

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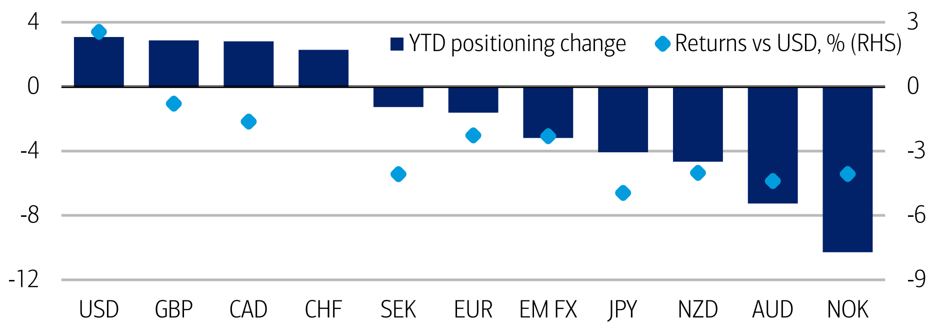
Link to the full report: Liquid Insight: FX flows in ’24 – half a step back 08 February 2024

- Investors took half a step back at the start of '24, buying USD largely across the board, a partial reversal of end-23 action
- The price action seems driven by Hedge Funds, and is more strongly correlated with our Asia investor flows
- In the options space, recent activity has been along similar lines, with the demand for USD calls picking up

Exhibit 8: Change in BofA aggregate FX positioning YTD vs. price action
FX positioning changes have been well in line with the price action



Source: BofA Global Research, Bloomberg. Note: Data are for the period Dec 29-Feb 2. +50 (-50) is max long (short) positioning level vs history. Currencies ranked on their YTD positioning change. We use DXY for USD and the JPMorgan Emerging Market Currency Index for EM FX.

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A partial reversal of the end-‘23 FX flows marked the start of ‘24. Toward the end of ’23, investors sold USD, largely across the board and especially vs. EM FX, amid the improved US inflation outlook and the dovish December FOMC meeting. But the resilient US activity data forced a partial rethink among investors at the start of ‘24, already ahead of the relatively hawkish January FOMC meeting and the solid payrolls report, according to our proprietary FX flows. The recent activity in the FX options space has been along similar lines, with the demand for USD calls picking up.

This year’s FX price action seems to be Hedge Fund-driven, and correlates well with Asia-based investor flows. Near-term USD upside would likely require stronger Real Money participation, but we would watch the Hedge Funds’ space for a USD sell-off. Overall, FX positioning remains light in most cases, and the recent investor positioning changes suggest somewhat reduced positioning risks to most of our trade recommendations.

CHF: SNB has been Intervening

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Link to the full report: FX Watch: CHF: SNB has been Intervening 07 February 2024

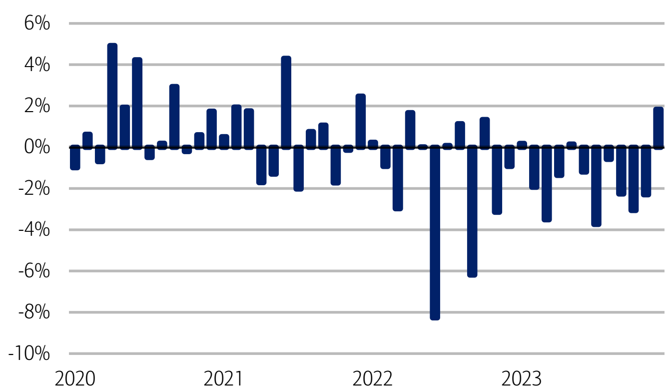
Confirmation of Intervention.

We had placed great store in the release of SNB January FX reserves to gauge the extent (if any) of SNB interventions to weaken CHF as proxied by the weekly sight deposit data. Our priors have been confirmed: The SNB intervened in January as the CHF Real Effective Exchange Rate (REER) hit a new record high. The SNB has placed great store in the value of the REER as it becomes increasingly concerned by the impact on Swiss corporates. We continue to emphasise that the enhanced FX policy introduced at the SNB policy meeting in December is two-pronged: limiting FX sales and selling the CHF. Whilst the SNB has so far stopped short in characterising the CHF as "significantly overvalued", further CHF strength may trigger such a response and we think the March meeting is "live" as the SNB has one eye on developments in ECB policy as well.

Looking at the numbers.

January Swiss FX reserves rose CHF8bn from December. As Exhibit 9 highlights, this is the largest %m/m increase in FX reserves since January 2022. On a y/y basis, FX reserves are still lower but we suspect the pace of declines will slow dramatically against the backdrop of this enhanced FX policy. As ever, valuation adjustments are important with the SNB portfolio composed of both bond and equities. Whilst the MSCI rose 1%, bond returns fell by 1.3% and according to our calculations, SNB reserves were approximately CHF660bn. This suggests some attrition on the headline number but the message is clear. The SNB has been intervening and comparing this to the valuation adjusted December reading, we estimate, that January interventions could be as large as CHF20bn.

Exhibit 9: % M/M Change in Swiss FX Reserves
Build in Swiss FX Reserves largest since January 2022



Source: BofA Global Research, Bloomberg

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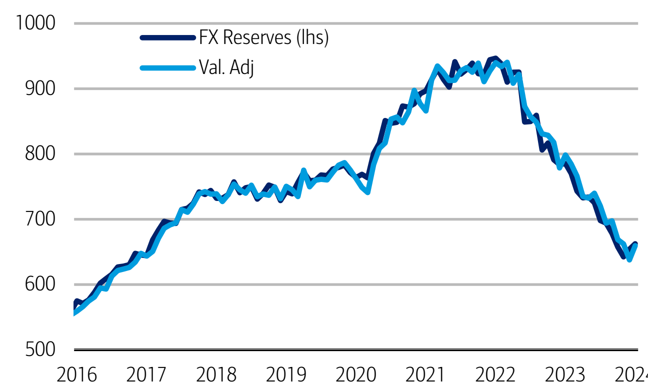
Exhibit 10: Swiss FX Reserves. Nominal vs Val adjusted.
Val adj still suggests that SNB intervened



Source: BofA Global Research, Bloomberg

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We remain short CHF

Today's date reinforces our structurally bearish CHF call. We are positioned long GBP/CHF and long EUR/CHF through call spread structures (see: Global FX Weekly for a full list of open/closed trade). Though the GBP/CHF has a large cyclical element to it, the trade is enhanced by the significant CHF overvaluation. The SNB will not stop here as they guide CHF lower. Swiss CPI data on 13th February will be a key event. Further slippage in headline inflation emboldens the SNB to continue to weaken CHF. There is also the risk to base case scenario that the SNB cuts sooner rather than later. All in all, CHF remains our funding currency of choice in carry trades.

Canada: Top 5 questions for 2024

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Link to the full report: Canada Viewpoint: Canada: Top 5 questions for 2024 07 February 2024

Will the rise in population help the economy in 2024?

We believe so, mainly by continuing to increase potential growth, although in the short term it has mixed effects on inflation. Canada has experienced a dramatic increase in its population since 2022, with non-permanent residents leading the expansion. Net international migration growth dominates the natural increase in population (births less deaths). The increase in population raises the labor force and allows the country to growth with less inflationary pressure. However, the newcomers demand housing which in the short and medium terms exacerbate the shortage of housing, putting upside pressure on inflation through shelter.

Will Canada's activity accelerate or decelerate in 2024?

We expect GDP growth to accelerate from 1.1% in 2023 to 1.3% in 2024 and to 2.4% in 2025 (we expected 0.9% for 2024 and 2.0% for 2025 before). So, we expect the economy to accelerate but to still growth below potential this year (potential growth is about 2.0%). We increase our GDP growth forecast following the strong GDP print in the US at the end of 2023 and the still tight labor market in Canada at the turn of the year. We still expect a relatively weak economy in the first half of 2024, but we expect growth to accelerate to above a 2% rate in the second half of the year, in part supported by looser financial conditions. The risks to our GDP growth forecast are balanced.

When and by how much will the BoC cut in 2024?

We expect the Bank of Canada (BoC) to start its cutting cycle in June 2024 and to cut 25bp at every subsequent meeting to put the policy rate at 3.75% by end-2024 (125bp total cuts this year). We then expect the BoC to continue cutting to put the policy rate at 3.00% by April 2025 (terminal rate). We expect the BoC to have a faster and deeper cutting cycle than the US Fed. We expect the BoC to cut because the economy has been growing below potential for some time and we expect inflation to converge to the 2% target in 2025. The risk to our call is that the BoC starts the cycle later. An earlier start of the cutting cycle is unlikely as the BoC is waiting for core inflation to show a clear downward trend and this will still take a few months. Another risk is that the BoC does a more gradual cycle than what we expect given resilient core inflation.

What matters most for 10y rates in Canada?

Big questions for CAD rates in 2024 include (1) when will BoC start cutting; (2) how fast will they cut; and (3) what will the market price for the "terminal" rate or the trough of the cutting cycle? We think the terminal rate pricing will be the most important rate driver this year. The market may be underpricing BoC rate cuts and pricing a higher terminal. If incoming data comes in as we expect, we believe market pricing will shift and we will likely see CAD rates rally.

Where is USD/CAD headed in 2024?

We like to maintain a bullish bias for the CAD vs USD in 2024 and see the pair falling to 1.30 by year-end. We see limited near-term bearish CAD drivers stemming from Canada. More material USD/CAD downtrend should form once Fed cutting cycle begins.

EM Themes
Sell EUR/TRY on carry dynamics & macro

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Short EURTRY – external position is improving

We short EURTRY using 3m forward at 36.2 (spot: 32.88, target: 34.4, stop: 37.3, carry: c. 3.3% per month). The risk is a more dovish CBT or a much slower improvement in the current account. EURTRY has been stable recently, which makes it a good carry trade if the trend continues. Moreover, a month ago, the 1-month forward was predicting significantly stronger depreciation than the actual outcome (Exhibit 15). The trade balance is also improving fast, which should support the lira (Exhibit 14), together with the reduction in retail demand for FX.

TRY to depreciate only slowly against EUR

Since the beginning of the year, EM FX and EUR have weakened significantly against the USD. However, EM FX performance against the EUR has been much stronger (Exhibit 16). Türkiye's external position is improving further, and we expect EURTRY to go higher only gradually, allowing us to benefit from high carry despite a stronger USD.

Pay 1y OIS (Sep IMM) after the recent rally

We enter a 1y OIS payer in Türkiye with a September IMM start date at 34.6 (target: 38, stop: 32, roll: circa 174bps per month). The key risk is a more dovish-than-expected CBT. The best approach is to execute the trade in small sizes with wide targets and stop. We re-enter the trade after the recent rally of the front-end and the appointment of the new CBT governor, which should benefit our trade (see A change for the better).

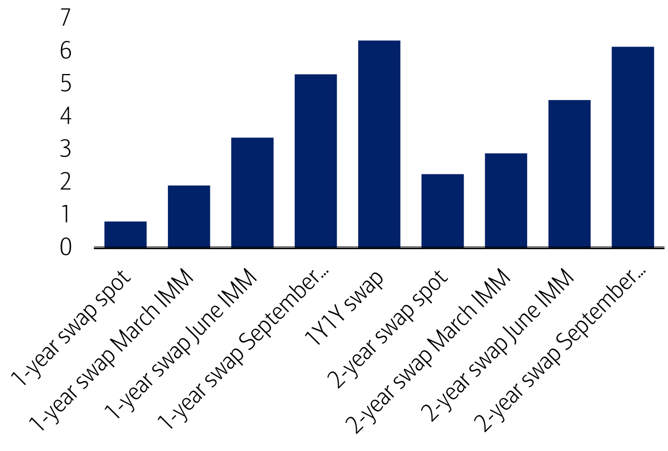
2024 baseline: no cuts; dovish scenario: a November cut

The new CBT governor stated that they will hold rates as long as necessary and that they are ready to act if the inflation expectations deteriorate. Given our 40% 2024YE inflation forecast, we expect the CBT to hold until year-end and cut for the first time in 1Q25. More hikes are also back at the table and the CBT could hike if needed. However, if inflation proves to be lower at c.36% as the CBT's forecasts suggest, we could see a first cut in 4Q24. The central bank could also consider easing some regulations before cutting, if it sees more weakness than expected in economic activity 2H.

Market pricing is more dovish than any of our scenarios

The market is significantly more dovish than our baseline and slightly more so than our alternative scenario (Exhibit 11 and Exhibit 12). The 1y1y and 1y (Sep IMM) swaps look most mispriced. We choose 1y (Sep IMM) because: 1) it offers the best carry and roll (Exhibit 13); 2) the 1y Sep IMM is more mispriced in our alternative scenario; and 3) we have high conviction of no cuts before the November meeting, while the market has the first cut priced from late summer.

Exhibit 11: The market is too dovish relative to our baseline
The chart shows BofA expectations minus market prices for OIS



Source: Bloomberg, BofA Global Research

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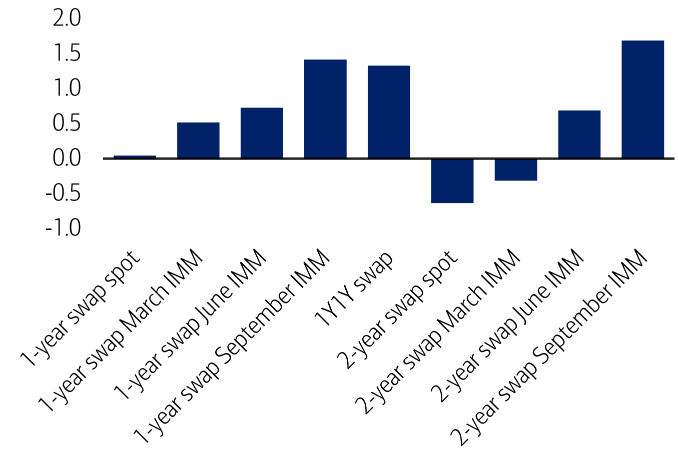
Exhibit 12: 1y (Sep IMM) looks most mispriced in our dovish scenario
The chart shows BofA expectations minus market prices for OIS



Source: Bloomberg, BofA Global Research

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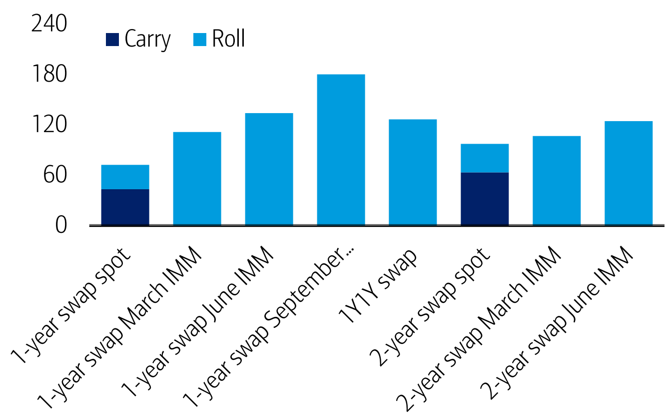
Exhibit 13: 1y (Sep IMM) offers the best carry/roll for paid positions
This is one of the reasons why we select it for paying



Source: Bloomberg, BofA Global Research

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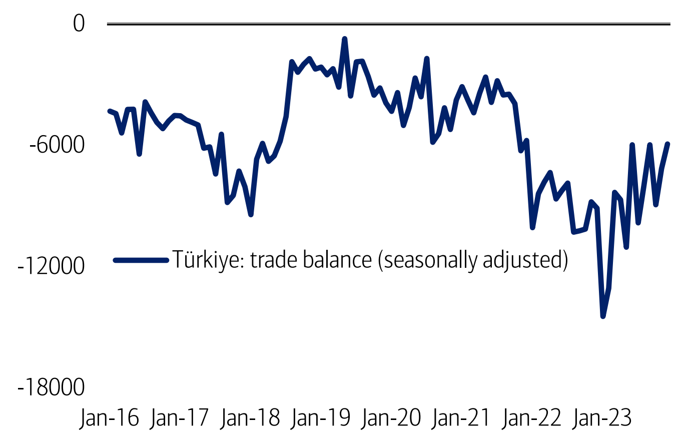
Exhibit 14: Trade balance is improving fast
Rebalancing of the economy should support the lira



Source: Haver, BofA Global Research

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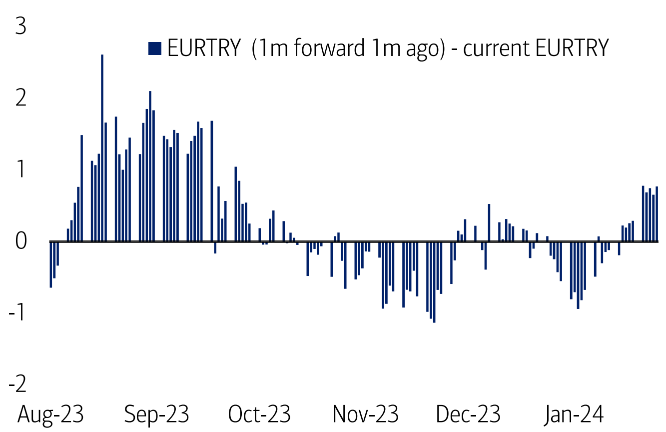
Exhibit 15: Forwards overestimate TRY depreciation recently
We expect this trend to continue



Source: Bloomberg, BofA Global Research

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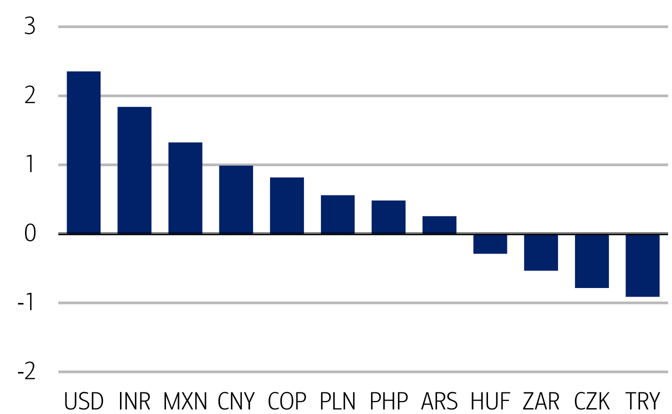
Exhibit 16: Currencies performance against the EUR since 1 Jan 2024
+ means appreciation against the EUR; performance does not include carry



Source: Bloomberg, BofA Global Research

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Why We Still Like Buying BRL/MXN

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Full Report: Emerging Insight: Why We Still Like Buying BRL/MXN 06 February 2024

Why We Still Like Buying BRL/MXN

We remain bullish on BRL/MXN, first opened in late November despite a 2.6% underperformance so far (see Buy BRL/MXN – 2024 Macro Outlook Favors Brazil Over Mexico). US growth outperformance relative to EU has been a headwind. But we expect forthcoming interest rate cuts in Mexico to negatively impact MXN while real rates in Brazil will be the highest across major currencies by the end of the year.

Global factors have not helped much but should going forward.

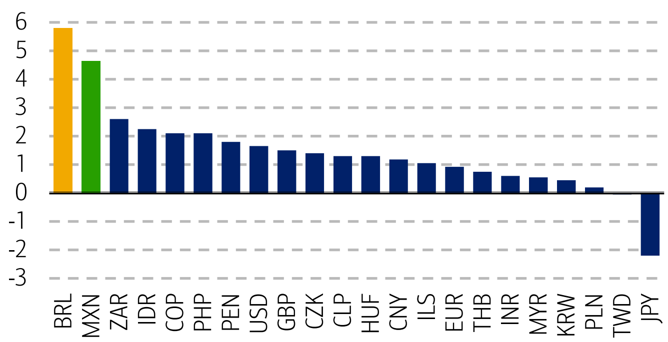
We highlighted the role the euro and US bond yields played in explaining BRL/MXN in the opening trade note. A stronger euro would be positive for BRL/MXN given Brazil's deeper trade links with Europe and Mexico's linkage to the US economy. And lower US bond yields would benefit Brazil more than Mexico given the former's higher debt stock.

The euro weakened 2% against the dollar since we opened the trade. We had estimated a beta coefficient of 1.4 so in a sense this would explain the 2.6% depreciation in BRL/MXN. Bond yields in the US are down by around 20bp since November 28 which should have been positive for BRL/MXN. But the correlation between BRL/MXN and US bond yields is much weaker than that between BRL/MXN and EUR/USD.

Brazil: Why we are still bullish

We believe there are three idiosyncratic factors that are key for the Brazilian real to outperform: disinflation that keeps real interest rates above 5%, real GDP growth above 2% and a primary budget deficit of around 0.5% this year.

Exhibit 17: Major currencies sorted by real rates by end-2024.
Real rates by end-2024 using consensus forecasts for policy rates and inflation. For Brazil and Mexico, we use our own forecasts.



Source: Bloomberg

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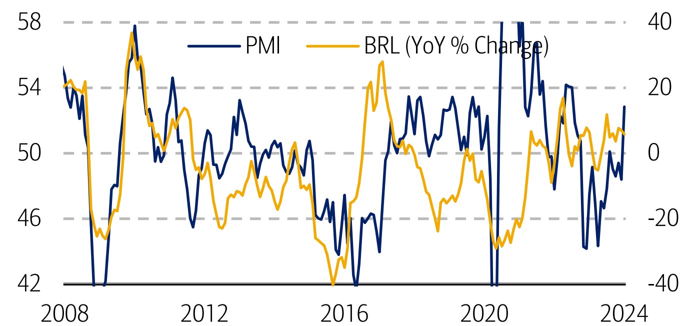
Exhibit 18: Strong growth leads to BRL appreciation.
Brazil's manufacturing PMI and BRL spot returns. Rising PMI tends to lead to BRL spot appreciation.



Source: Haver Analytics

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First, the Brazilian real is the quintessential high carry currency that performs well when it delivers investors a positive real carry in addition to low and stable inflation. Our 2024 forecasts are for 3.7% inflation and a terminal benchmark rate of 9.5%. This implies a real rate of almost 6% which would still put BRL at the very top in the carry rankings of major global currencies (see Exhibit 17).

Second, we forecast Brazil to grow 2.2% this year, well above the 1.5% consensus expectation. Strong growth is key because it attracts foreign capital inflows and helps with debt sustainability. Recent data suggest Brazil's economy is gaining speed, with manufacturing PMI rising to 52.9 in January from 48.8 in 4Q23 (see Exhibit 18). Moreover, the 2017 labor reform, the 2019 pension reform, the 2023 consumption tax reform, several other micro reforms, and the development of pre-salt offshore oil fields are likely to boost potential GDP growth closer to 2.5% than the 2% potential growth estimate held by most analysts (see Brazil Primer: Brasilopedia: The growth awakens).

And third, reducing fiscal deficits are critical for correcting BRL's undervaluation. Brazil needs to eventually run primary budget surpluses of 1-2% of GDP under reasonable assumptions for long-run real interest rates and potential economic growth. We expect the government to reduce the primary deficit to 0.4% this year from 1.3% in 2023. That would be a better outcome than the 0.8% primary deficit predicted by the consensus.

Mexico: Why we are still bearish.

We are bearish Mexico, arguably our most non-consensus view in Latin America. We believe that forthcoming interest rate cuts will negatively impact the Mexican peso. It looks increasingly likely Mexico's central bank may decouple from the Fed, cutting its benchmark rate as soon as March despite the Fed holding its first cut until June. Rate cuts in Mexico would be taking place despite sticky inflation and a tight labor market.

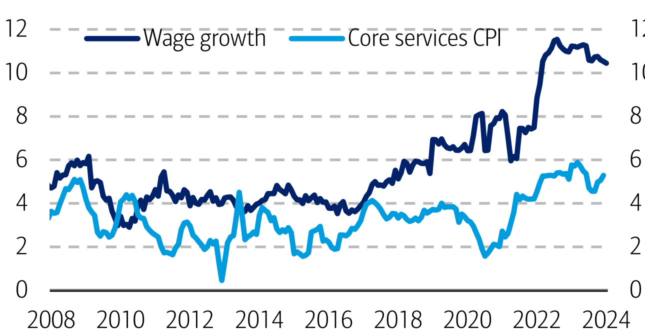
If inflation declines further by February, we believe the central bank is more likely than not to cut rates in March given the weak 4Q23 GDP report. This condition is likely to be met; we expect headline inflation to decline to 4.4% in February from 4.7% in December and core inflation to decline to 4.6% in February from 5.1% in December. Add the sharp slowdown in real GDP growth to 0.3% in Q4 from 4.4% in Q3 and increasing borrowing costs to fund rising budget deficits and the central bank will find it easy to justify a rate cut (see Banxico preview – on hold in February leaving the door open for March).

But on closer inspection the case for lowering rates may be less obvious. First, underlying inflation may be rising, not falling; six-month annualized core inflation rose for three consecutive months to 4.6% in December from 4.1% in September and core services inflation rose to 5.3% in December from 4.6% in September (see Exhibit 19).

Second, the output gap is +4% and the labor market quite tight with unemployment at 2.8%, just 10bp shy of the record low. Wages are growing at more than 10%. This suggests that even if growth decelerates further there will be upward pressures to underlying inflation for quite some time (see Exhibit 20).

Exhibit 19: Inflation is falling in Mexico. Or is it?

Wage growth is YoY % change. Core services CPI is 6m annualized % change



Source: Haver Analytics

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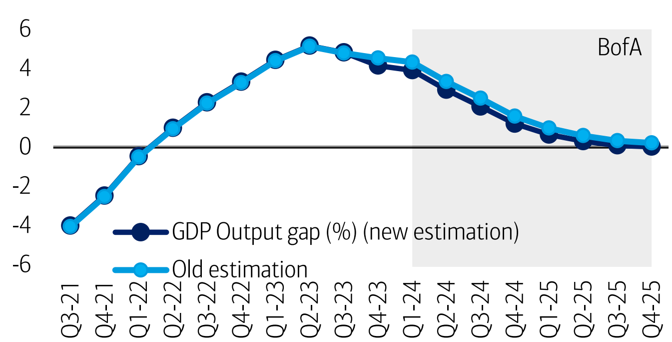
Exhibit 20: Mexico's output gap

We believe that the Mexican economy will remain overheated for some time



Source: BofA Global Research

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And third, the growth slowdown in 4Q23 is likely to reverse in 1Q24. Agriculture contracted by more than 4% in Q4, and a cash-strapped public sector translated into lower public spending. But the government has issued record amounts in capital markets already in January so public spending will likely reaccelerate. We forecast real GDP to grow by 2.3% in 1Q24 (see Mexico's GDP decelerated significantly in 4Q 2023).

Taipei Trip Notes – February 2024

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Full Report: Asia FI & FX Strategy Watch: Taipei Trip Notes – February 2024 06 February 2024

Taiwanese lifers neutral on US$, reduced FX hedging in Jan

We recently went to Taipei and saw a number of real money accounts and large corporates to discuss the FX and rates outlook for 2024. General sentiment from Taiwanese real money accounts (i.e., the life insurance companies) was an aversion to increasing FX hedging as long as the US$ remains in a general trend of stabilization.

The lifers we spoke to confirmed that they had to rapidly increase FX hedging in December 2023 following the dovish communication from the December FOMC meeting and the significant US$ weakness that followed. The December 2023 data shows that lifers rapidly consumed their FX valuation reserves as the USD fell. The decline in FX valuations reserves and the very dovish US$ outlook in December resulted the FX-hedged ratio rising and **monthly FX-hedging cost reaching US$1.2bn for the first time (**see Exhibit 21**)**.

However, as the US$ stabilized in January 2024, lifers subsequently unwound the recent increase in FX hedges, and their latest FX-hedging ratio is likely close to where it was in 3Q23 (which we estimated to be at 61%). One lifer mentioned that the key level of 31.05 could result in that lifer accelerating FX hedging. Others mentioned that they are incrementally increasing FX hedging at 31.3 to take advantage of the better price.

Corporates bullish on export outlook but prefer to hold US$

A few Taiwanese corporates that we met confirmed that they prefer to hold their export earnings in foreign currency, especially in US$, because of the wide yield gap against the Taiwanese Dollar (NT$). Moreover, a few corporates told us that their demand for overseas investment is rising because of the need to invest in manufacturing capacity outside mainland China. The de-risking strategy is more the result of a ‘push’ rather than a ‘pull’ factor due to rising pressure from US- and Europe-based clients asking to source ‘non-China’ content.

On offshoring from China, one technology manufacturer told us that even though labor cost may be more competitive in Vietnam and other ASEAN countries, this manufacturer prefers to keep its core manufacturing capacity in mainland China because of the better infrastructure and the decades of experiences and relationships it has built. Overall, this corporate believes that Vietnam is more than 20 years behind China in manufacturing capacity and efficiency and that it would be hard to replace China as the central node in a global supply chain in the near future.

Lifers rapidly increased FX hedging in December 2023 in response to the dovish FOMC and weak US$ environment. As of the latest quarterly filings for 3Q23, we estimate the weighted-average FX-hedging ratio for Taiwanese lifers to be at 61% (see the report, Asia FI & FX Strategy Watch: Taiwan lifer update – December 2023 05 December 2023). In December 2023, TWD NDF points aggressively widened, falling from a monthly high of -300 pips to -575 pips upon the dovish messaging from the December FOMC. This widening in TWD NDF points was partially caused by a rapid increase in lifers’ FX-hedging ratio. 4Q23 data will not be available until the end of February 2024, when the listed Taiwanese lifers report their quarterly earnings, but we estimate that the FX-hedging ratio may increase closer to 65% around that time.

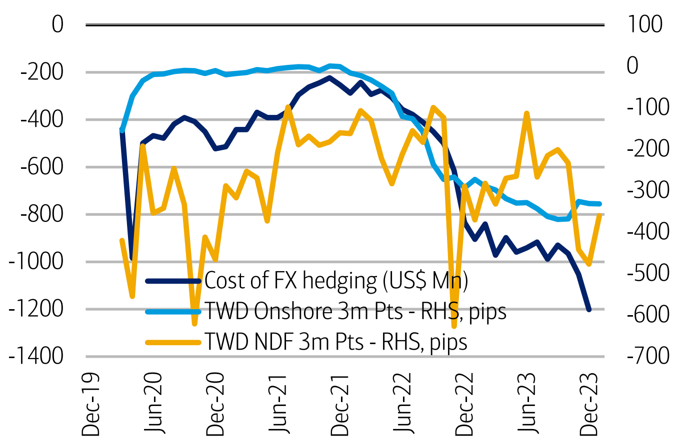
Rapid increase in FX hedging in December 2023 resulted in historic FX-hedging cost. According to the monthly disclosures provided by the FSC, the main regulatory body for the Taiwanese life insurance companies, lifers spent a record US$1.2bn in cost for FX hedging (Exhibit 21) in December 2023. The increase in realized FX-hedging cost corroborates with the increase in the FX-hedging ratio mentioned above. Currently, selling USDTWD 12-months outright has negative carry of 4% on the DF curve and 4.2% on the NDF curve.

Lifers remain active in using proxy FX hedges. Overall, FX hedging through different currencies to 'proxy' the movement in USDTWD remains a small but important part of lifers' total FX-hedging strategy. None of the lifers that we spoke with said that FX hedging through proxies exceeded 10% of their overall FX hedging.

Lifers are increasingly enquiring about South-East Asian currencies to use for proxy hedging. Among this 10%, the most common currencies that lifers would use for proxy hedging would be the CNH, KRW and SGD. However, during this latest trip to Taipei, lifers also increasingly expressed interest in using South-East Asian currencies, especially IDR, INR and PHP given high yields. Market flow commentary also indicated that often, when Taiwanese lifers enter the market to conduct FX hedging, their flow not only pushes TWD NDF points lower but also spills over into the FX points of other Asian currencies given the large size of some individual clips.

Exhibit 21: Cost of FX hedging for lifers (US$ Bn) and DF and NDF points

In December 2023, the life insurance industry in Taiwan spent US$1.2bn per month in FX hedging, a record high since public data was made available starting January 2020



Source: CEIC

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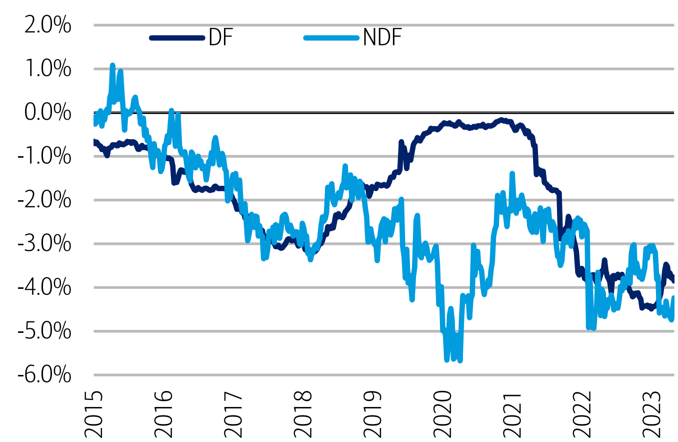
Exhibit 22: FX-hedging cost to sell USDTWD forward (annualized)

FX-hedging cost both onshore and offshore for USDTWD remains deep and expensive



Source: Bloomberg

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Saudi Arabia: energy policy

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Full Report: Emerging Insight: Saudi Arabia: energy policy – 07 February 2024

Saudi energy policy: it's not (only) the economy

The revision to the targeted Aramco Saudi Maximum Sustainable Capacity (MSC) likely reflects a mix of medium-term oil market fundamentals, large existing spare capacity and ongoing fiscal funding needs. We estimate modest fiscal savings from the MSC target revision at 1.5% of GDP (cUS$17.5bn) over four years or 0.4% of GDP per annum, assuming unchanged payout ratio. The additional funds could be put into use into priority domestic diversification projects instead, in our view.

Saudi energy policy makes a U-turn

Main pillars of Saudi energy policy

We believe there are three aspects that are central to energy policy in Saudi Arabia: a) competition for global market share in upstream operations or swing oil producer role (affecting spot prices); b) future investment decisions and maintaining of spare capacity buffer (affecting long-term oil prices); and c) focus on integration and expansion of downstream ventures to create domestic jobs, secure captive demand for crude and make operations less volatile.

Saudi energy policy decisions are likely to finely balance OPEC (Organization of the Petroleum Exporting Countries) members' funding needs, the impact on oil demand, internal group cohesion considerations, reliability as a major oil supplier, and public perceptions (both domestically and internationally).

Strong near-term incentives to support high spot oil prices

The more assertive nationalistic 'Saudi First' policy and the ongoing mega-projects spearheaded by the Public Investment Fund (PIF) suggest large medium-term financing requirements and the need for elevated oil prices.

We think Saudi Arabia's interests remain centered around market stability, rather than spiking or too elevated oil prices that could lead to global oil demand destruction and more rapid decarbonization efforts. Indeed, the Saudi Minister of Energy self-describes energy policy as 'proactive, pre-emptive and precautionary'.

Press reports suggest authorities are considering a further secondary market listing for Saudi Aramco shares this year (current free-float is 1.8%). A potential sale may be aided by a supportive oil price backdrop, in our view.

The sliding fiscal regime allows authorities to capture the upside in oil prices. The royalty rate on crude oil and condensate production, amended effective 1 January 2020, is 15% for Brent prices up to US$70/bbl; rising to 45% for Brent prices between US$70/bbl and US$100/bbl, and to 80% for Brent prices above US$100/bbl).

Underwhelming November OPEC+ meeting does not help

The November 2023 OPEC+ meeting was underwhelming in terms of potential support to oil prices. We suspect it may lead to only resulting in a modest decline in production (possibly closer to a status quo outcome), and exhibiting little cohesion (with Angola subsequently leaving the group). The agreed production cuts are valid only for 1Q24, with some signs that further cuts may be difficult to agree upon, all else being equal.

We see the following key points from the meeting:

1. OPEC+ production is likely slated to decline only modestly in 1Q24, given the low credibility of the pledged cuts. We estimate the cuts announced could result in a decline of only 300k bpd in production for 1Q24 versus October 2023 levels. OPEC+ announced additional voluntary cuts of 2.2mn bpd, but this includes the Saudi 1mn bpd cut rollover and 0.2mn bpd in Russia refined oil product cuts (i.e., 1mn bpd of cuts pledged excluding Saudi Arabia rollover and Russia oil product cuts). Our estimates are smaller because (1) the cuts are voluntary adjustments, and valid only for 1Q24; (2) a number of countries may not fulfil pledges (United Arab Emirates (UAE), Iraq, Russia); and, importantly, (3) the voluntary adjustments are calculated from the 2024 required production level as per the

   35th OPEC Ministerial Meeting held on June 4 2023, in addition to the voluntary cuts previously announced in April 2023 and later extended until the end of 2024, and not from current production reference levels;

2. Note that Iran, Venezuela, Libya still have no quotas. Production may increase from these countries, depending on US sanctions or security conditions;

3. Cohesion of the group may have weakened. Angola rejected its output quota which was based on three external assessments, although its planned production level is not significantly different from the OPEC+ target, and subsequently exited the group. The unilateral Saudi 1mn bpd supply cut may have weakened its hand in negotiations; we had suggested it may distort compliance and future negotiation incentives within OPEC+;

4. Brazil could join OPEC+ from 1 January 2024, but this may be symbolic as it has suggested output cuts would not be binding on it;

5. Further revision of quotas in June 2024 or November 2024 meetings may be complicated. Recall that OPEC+ is planning to start the process of negotiating quotas for 2025 based on independently assessed production capacity, likely helping fulfil a key demand by the UAE to increase its quota over the medium-term. This could minimize frictions between the UAE and Saudi Arabia. OPEC+ had suggested that, by end-June 2024, all OPEC+ countries will undergo an assessment by three independent secondary sources to identify production capacities to be used for 2025 reference production levels. (Nigeria, Angola and Congo external assessments have already been completed); and,

6. A steep decline in oil prices may be needed to force the hand of OPEC+. The next (37th) OPEC and non-OPEC Ministerial Meeting will be held on 1 June 2024, and no official meeting has been announced in the interim period until then for now. The next Joint Ministerial Monitoring Committee (JMMC) is to take place on 3 April 2024.

Spare capacity decisions can affect long-term oil prices

Saudi Aramco future investment decisions and maintaining of spare capacity buffer are a critical policy parameter of Saudi energy policy. In addition to its influence on spot prices through its ability to adjust production, Saudi Arabia can decide on pace of its reserves development which would potentially affect future supply to the market, and hence long-term oil prices. There are distinct trade-offs in this decision. If Saudi Arabia is producing at close to its maximum capacity, it will have little control over sharp upside movements in oil prices. On the other hand, if excess capacity is large, oil prices are likely to be under downward pressure.

VOL

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- Short-dated realized vol rose sharply but with weak implied vol demand.
- Asymmetric vol reaction to USD rally suggests implied vol to rise on weaker USD.

USD realized vol performs on events but lags otherwise

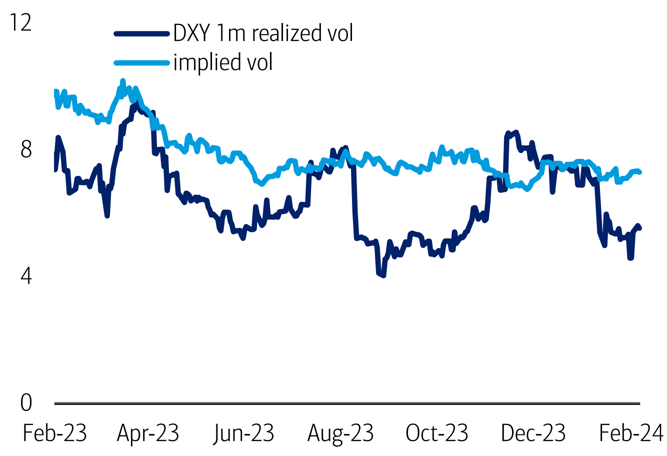
FOMC and NFP (nonfarm payrolls) effects lasted less than a week. At first the Fed hawkish surprise led the DXY rally higher, which was then supported by the NFP surprise. But lack of follow-through is notable, with DXY rally momentum slowing. The 1w and 2w realized vol picked up (Exhibit 24), while corresponding implied vols have not and realized vols over a longer period like 1m remain under water for many major pairs (Exhibit 23).

USD remains stuck in a range, keeping a lid on implied vols for now

DXY had met stiff resistance at 100W and 100d SMAs, falling back into a range. Investors did not look for the USD to rally higher, lacking new catalysts. While the USD had benefitted in the short-term from repricing of fewer Fed cuts, the Fed policy rate direction remains lower. In a rangebound environment, volatility trades lower as investors prefer the style of carry over trend.

In our view, investors are lacking conviction on the timing of directional trend to pay for volatility premia outright at this point. Simply put, the Fed didn't offer guidance for more hikes to validate prior USD uptrend, rather delaying the first cut and staying on hold. To the extent that the Fed is in a wait-and-see stance, so are the investors.

Exhibit 23: Realized vol has bounced off the low but with little follow through for implied vol
DXY 1m realized vol vs implied vol



Source: BofA Global Research, Bloomberg

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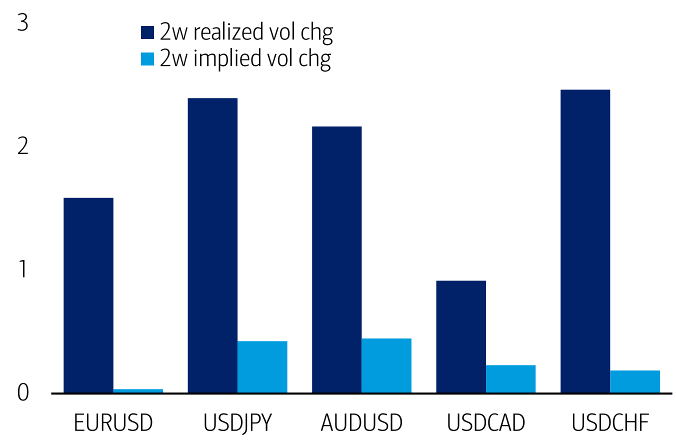
Exhibit 24: Lack of demand for implied vol was across all major G10 currencies
2w implied and realized vol changes Jan 26 to Feb 2



Source: BofA Global Research, Bloomberg

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Lower USD vol on higher spot sees rising vol on the way down

Although vol didn't pickup amid the recent USD rally, we expect higher vol when the USD breaks out of recent range and form an eventual bearish trend with the start of the Fed cutting cycle. As a result, we see 6m USD put skew to richen vs. calls. The risk to our view is higher inflation delaying cuts further.

Trade Recommendations G10

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Exhibit 25: Open trades G10
Current G10 FX trade recommendations. Prices as of 8-Feb-2024.

Trade Description	Open Date	Entry Price	Expiry Date	Current Price	Rationale	Risks
Buy 3m GBP/CHF 1.0950/1.1100 call spread	5-Feb-24	0.47% GBP (spot ref: 1.0947, vol refs: 6.2% & 5.6%)	2-May-24	1.1037	A tactical trade given the benign risk backdrop to position for policy divergence/carry	Heightened geopolitical tensions or a fiscally damaging UK Budget
Buy USDSEK	2-Feb-24	10.49 (target: 10.65/10.90, stop: 10.30)	Spot trade	10.4804	US data resilience/ hawkish Fed, dovish Riksbank, technicals	US data softening more and faster than we expect, leading markets to price a higher chance of Fed rate cuts before June. Upside inflation surprises in Sweden
Buy NOKSEK	1-Feb-24	0.9949 (target: 1.0240, stop/loss: 0.9780)		0.9875	Relative Norges/Riksbank stance, central bank flows, lighter positioning, hedge higher geopolitical risks	Lower oil prices, weaker than expected Norway data, too high EURSEK for Riksbank's comfort
Buy 3m EUR/JPY 158/155 put spread	26-Jan-24	0.6663% EUR (spot ref: 160.41, vol refs: 8.709 & 8.965)	25-Apr-24	160.69	Near-term (tactically) JPY constructive on BoJ normalisation. We see risks of more ECB cuts priced in 2H also given the weak EA data	Markets pricing a more dovish BoJ stance or a more hawkish ECB stance
Buy 3m 1x1.5 0.8320/0.95 EUR/CHF call spread	2-Jan-24	0.53% EUR (spot ref: 0.9320, vol refs: 5.8% and 5.25%)	3-Apr-24	0.94187	SNB symmetric reaction function implies intervention to weaken CHF or (more likely) less FX sales to taper balance sheet	SNB takes a more benign approach to CHF strength should inflation remain elevated
Buy EUR/USD	16-Nov-23	1.0859 (target 1.15, stop/loss: 1.04)	Spot trade	1.0762	The trade expresses our baseline cyclical bearish USD view for 2024 on the start of Fed rate cutting cycle and normalization of the overvalued USD	A later than expected start to the Fed rate cutting cycle
Buy 4m EUR/GBP vol swap	16-Nov-23	5.01 (target: 6.00, stop/loss: 4.50)	20-Mar-24	Current 1m implied vol at 4.20	EURGBP implied is at a historical low and should rise on diverging economic and fiscal outlook between EU and UK. Trade also used to diversification for the core bearish USD view for 2024	Persistent low vol regime in FX market into Q1 2024

Source: BofA Global Research

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Exhibit 26: G10 FX Closed trades
Recently closed trades in G10 FX.

Trade Description	Entry date	Entry Level	Target	Stop	Close date	Level closed
Buy 3m 1x1.5 GBP/SEK call spread	12/01/24	0.66% GBP (spot ref: 13.1008, vol refs: 7.95% and 7.47%)			29/01/24	0.91% GBP (spot ref: 13.3066, vol refs: 7.38% and 6.89%).
Buy 3m 1.90/1.86 GBP/AUD put spread	16/11/23	0.6806% GBP (spot ref: 1.9192, vol refs: 7.207 and 7.007)			3/01/24	1.2315% GBP (spot ref 1.8762, vol refs 7.354 and 6.921)
Sell EUR/NOK via 6m risk reversal (buy 6-month 11.35 put and sell 12.20 call)	16/11/23	Receive 0.7307% EUR (spot ref: 11.8623, vol refs: 8.929 and 9.108)			3/01/24	Trade costs 1.91% EUR (spot ref: 11.3215, vol refs: 9.67%/10.13%)
Sell 1m 143.50/137.00 USD/JPY put spread	8/12/23	Receive 1.0024% USD (spot ref: 144.33, vol refs: 10.738 and 13.634)			19/12/23	Receive 0.72% USD (spot ref: 144.50, vol refs: 9.431 &11.919)
Buy 1y 25-delta AUD/USD risk reversal (call strike 0.7391, put strike 0.6049)	17/11/22	Zero cost (spot ref: 0.6693, vol refs: 12.253 and14.892)			17/11/23	0.65 (options expired worthless)
Buy CAD/MXN	23/10/23	13.3338	14.00	13.00	01/11/23	13.00
Buy EUR/SEK via 3-month collar (buy 3m 11.8380 call, sell 3m 11.3143 put)	13/10/23	Zero cost (spot ref 11.5456, 3m 11.8380 call cost at 0.5676% EUR with vol ref 7.394%, 3m 11.3143 put cost same with vol ref 6.701%)			30/10/23	1.1199% EUR (spot ref: 11.8250, 11.8380 call costs c. 1.21% EUR with vol ref 6.98%, 11.3143 put costs 0.09% EUR with vol ref 6.51%)
Buy 6m GBP/AUD put seagull (long 6m put spread with strikes at 1.94 and 1.90, short 2.05 call)	08/09/23	0.3827% GBP (spot ref 1.9516, put spread vol refs: 8.346/8.099; short call ref: 8.450)			22/09/23	1.2341% GBP (spot ref 1.9006, vol refs 7.981 for 1.94 put, 7.477 for the 1.90 put, and 8.043 for the 2.05 call)
Sell 2m 0.89 USD/CHF put	23/06/23	Receiving 1.0126% USD (spot ref: 0.8967, vol ref: 6.44)			24/08/23	0.8845
Sell 2m 25-delta OTM EUR/GBP put	23/06/23	Receiving 0.31% EUR (strike ref 0.8472, vol ref 5.584, spot ref 0.8592, expiry August 24)			03/08/23	Spot ref 0.86470, vol ref :4.214)
Buy USD/SEK via 3m collar (buy 3m 10.73 call and sell 3m 9.8960 put)	19/07/23	Zero cost (spot ref: 10.2724, vol refs: 12.296% and 10.202%, expiry Oct 19)			01/09/23	1.3316% USD (spot ref: 10.6109, vol refs: 11.777% and 10.377%)
Buy 3m USD/CHF vol swap	14/04/23	8.15%	9.5%,	7.5%	14/07/23	Accumulated 7.6319%
Sell 1y 1.04 EUR/USD put	11/04/23	1.1445% EUR (spot ref: 1.0857, vol ref: 8.517)			23/06/23	0.5238% EUR (spot ref: 1.0960, vol ref: 7.42)
Buy NOK/SEK	28/04/23	0.9638	1.06	0.9280	21/06/23	1.0045
Enter 2m/6m USD/CAD put spread (sell 2m 1.40 put, buy 6m 1.40 put)	13/03/23	0.96% USD (spot ref: 1.3782, vol refs: 8.123/7.877)			07/06/23	1.66% USD (spot ref: 1.3381)
Buy AUD/CAD	14/04/23	0.9028		0.89	25/05/23	0.89
Sell 3m 1.00/1.02905 EUR/CHF call spread	08/03/23	Receive 0.4784% EUR (spot ref: 0.9935, vol refs: 5.651/6.606)			20/04/2023	-0.04% EUR (spot ref 0.98085, vol refs: 5.376/8.971)
Buy 4m USDJPY KI put with American barrier level at 131.50 and strike 128.11	23/01/23	1.8629% USD (spot ref: 130.27, vol ref: 12.312)			24/03/23	1.93% USD (spot ref 130.00,, vol ref: 13.85)
Buy 3m 10.2466/10.70 USD/SEK call spread	20/01/23	1.4689% USD (spot ref: 10.2971, vol refs: 12.752 and13.307)			07/03/23	2.82% USD (spot ref: 10.7008, vol refs: 12.18/11.943)
Buy 1m 1.00075 EURCHF call	30/01/23	0.8031% EUR (spot ref: 1.00192, vol ref: 7.154)			24/02/23	0.99218
Buy 3 GBP/USD collar (sell 1.2850 call and buy 1.2000 put)	24/01/23	0.19% GBP (spot ref: 1.2400, vol refs: 9.4% and 11.0%)			17/02/23	1.6128% GBP (spot ref: 1.1991, vol refs: 9.961 and 10.287)
Sell USD/NOK via 6m collar (buy 6m 9.0227 put and sell 6m 10.10 call)	11/08/22	Zero cost (spot ref: 9.5063, vol refs: 12.481% and 13.890%)			13/02/23	10.0955 (expired worthless)
Sell EUR/CHF via 3m collar (long 0.98 put and short 1.00 call)	01/11/22	0.5619% EUR (spot ref: 0.9879)			01/02/23	Spot ref: 0.99833
Buy 3m6m 25D USD/JPY put calendar spread (short 3m 25D OTM USDJPY put, long 6m USDJPY put; strike 132.70)	17/11/22	1.0185% USD (spot ref: 140.1, vol refs: 12.510 and 11.553)			17/01/23	1.8764% USD (spot ref 128.25, vol refs 15.591 and 13.069)
Buy AUD/NZD via 3m ATMF 1.0608/1.09 call spread	12/12/22	0.9638% AUD (spot ref: 1.0582, vol refs: 6.721% and 6.28%)			13/01/23	1.9730% AUD (spot ref: 1.0917, vol refs 6.929% and 6.504%)

Source: BofA Global Research

EM Alpha Trade Recommendations

David Hauner, CFA >>
MLI (UK)

Claudio Irigoyen
BofAS

Exhibit 27: Open trades
EM Alpha Trade Recommendations

FX	Entry date	Entry level	Current level	Target	Stop	Notional	Rationale/ Time horizon	Risks
Short EURTRY using 3m forward	2/5/2024	36.2	36.37	38	32	10	EURTRY has been stable recently (fwds have overestimated depreciation). Lower retail demand for USD/EUR should be supportive.	The risk is a more dovish CBT or a much slower improvement in the current account
Long IDR vs PHP	1/19/2024	280	279.6	276	282	10	Long IDR vs PHP on favorable risk-reward if political uncertainty eases while BI may cap topside in USDIDR. Fundamental and portfolio flows in Indonesia have been more supportive while PHP's elevated NEER may limit gains.	Risk to the trade from risk-off moves and a drop in energy commodities which may improve PHP's terms of trade over IDR..
Short USDUZS using 3m NDF	1/5/2024	12,674	12,775	12,374	12,902	10	UZS to remain stable in the next 3m after 5% deval in 3Q23. Weak RUB caused August deval, but the RUB is supported now	The risk is an earlier-than-anticipated devaluation of the UZS
Short CNH, long basket	17-Nov-23	100	-	94	102	10	We expect CNH to underperform peers as PBOC will lean-in against appreciation in an effort to keep monetary conditions loose. Basket earns 8bps 3M carry	The risk to the trade is a large fiscal policy stimulus and economic recovery, ending the need for loose monetary policy and CNY appreciates aggressively in 6months.
3m USD call CNH put spread	17-Nov-23	39.8bps	-	7.30/7.55	-	10	Position for our contrarian view Q1 USD/CNY 7.55 forecast. 3.3% maximum payout for 8.5 times leverage	The risk to the trade would be an acceleration in fiscal policy stimulus, offsetting the need for further monetary stimulus and resulting in inflation and higher interest rates
Worst off 6M USD/IDR>5 % OTMS, USDPHP>5% OTMS	17-Nov-23	32bps	-	Both 5%+ above spot	n/a	10	The rationale for the trade is that these are relatively small, open, current-account deficit economies vulnerable to global shocks such as a hard landing and/or geopolitical event	The risk to the trade would be the absence of a global recession and easing of global geopolitical tensions
Long BRL/MXN	11/17/2023	3.52	3.434	4.00	3.25	10	Rate differentials, the euro and US yields will favor BRL. We also find BRL undervalued and MXN overvalued. The macro outlook looks better for Brazil than Mexico.	Main risks against the trade are a larger budget deficit in Brazil given its higher debt levels and strong inflows into Mexico due to nearshoring and/or remittances.
Short USDZAR	11/15/2023	18.15	18.88	17.6	19.5	10	last support for USDZAR at 18.13 now at risk before a retest of YTD lows (17.63-17.42) and/or a lower low; USDZAR is a proxy for EM FX. Light positioning + weakening US data + dovish Fed + soft US CPI = stronger EM FX and ZAR.	The risk is sticky inflation and stronger-than-expected activity in the US.
Long USDHUF	10/12/23	363.56	360.0	382	338	10	Stronger USD + weak BoP fundamentals in Hungary + still long positioning + focus on growth in Hungary = long USDHUF.	Weaker broader dolla.
1yr USD/CNH vol swap at 6.175%	8/2/23	6.175	5.638	-	5.00	10	The rising use of CNY for cross-border trade settlement should help to cut FX risk for local corporates and reduce the inflation pass-through from imported goods.	Weaker USD environment is typically associated with lower FX volatility and a more favorable EM FX environment
Short RONCZK	5/24/2023	4.77	5.01	4.53	4.92	10	RON is overvalued + current account in Romania is not improving (unlike the peers) => weaker RON; hawkish CNB => stronger CZK	The risk is crowded positioning in Czechia and delayed depreciation in Romania
Buy 1y USDHKD 7.7670/7.8500 call spread	3/29/23	Spot 7.8499	7.82	7.7670/7.8500	-	10	Forward points in HKD is very low given the outperformance of HK vs US rates following the increase in US banking sector risk	aggressive rally in US rates that significantly closes the HONIA-SOFR spread.

Source: BofA Global Research. Spot values as of February 8 2024. Bid/offer spreads accounted for in initiation and closing levels. Does not reflect tax withholdings or any investment advisory fees. Past performance is no guarantee of future results. A complete performance record is available on request. Inception date – July 4, 2016 Initiation and closing prices are priced as of trade publication. For additional discussion of baseline views, valuation and risks to open trades, please see links to detailed reports.

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Exhibit 28: Closed trades

EM Alpha Trade Recommendations

Trade description	Entry date	Entry Level	Target	Stop	Notional	Close date	Level closed
Short SGD/KRW	9/20/2023	974	945	990	10	28-Sep-23	969
Short SGD/KRW	9/20/2023	974	945	990	10	28-Sep-23	969
Buy 6m 25-delta call option for USDTWD	8/1/2023	31.6	31.9	29.8	10x10	2/8/2024	-
Short CZKHUF	11/29/2023	15.7	14.9	16.3	10x10	2/6/2024	15.48
Long PLNCZK	11/8/2023	5.51	5.78	5.34	10	1/11/2024	5.67
Long KZT vs USD & EUR	8/2/2023	479	435	530	10	1-Dec-23	481
Long EURZAR	10/2/2023	20.150	21.15	19.6	10	16-Nov-23	19.7
Long INRUSD	1/18/2023	81.65	80	83	10	28-Sep-23	93.26
Short SGD/KRW	9/20/2023	974	945	990	10	28-Sep-23	969
Sell MXN/ZAR	9/25/23	1.09	1.02	1.13	10	28-Sep-23	1.04
Buy USD/PEN	5/4/23	3.72	3.8	3.68	10	28-Sep-23	3.8
Long USDHUF	9/20/2023	358.4	375	347	10	28-Sep-23	47.96
Buy ZAR/CLP	9/7/23	45.08	48.6	44	10	25-Sep-23	4.6851
Long EURPLN	5/17/2023	4.5	4.725	4.365	10	12-Sep-23	4.6851
Short USDZAR through a call spread	8/9/2023	19.06 (for USDZAR)	-	-	10	23-Aug-23	0.57
Short EURHUF	8/4/2023	391.7	372.1	403.5	10	23-Jul-23	383.4
Sell CNH/CLP	6/15/2023	111.7	108	113.6	10	4-Aug-23	118
Short EURZAR	3/1/23	19.35	18.43	22	10	27-Jul-23	19.42
Buy a 3m digital call option on USDZAR	6/20/2023	23	17	18.7	10	5-Jul-23	35.5
Lond USDILS	6/15/2023	3.58	108	113.6	10	5-Jul-23	3.73
Short USDZAR	3/23/2023	18.16	17	18.7	10	15-Jun-23	18.2
Sell MXN/CLP	5/22/23	44.85	42.00	47.00	10	15-Jun-23	46.37
Long USDPLN	3/8/2023	4.43	4.65	4.0	10	15-Jun-23	4.12
Sell USD/BRL	5/31/2023	5.08	4.85	5.2	10	13-Jun-23	4.85
Long KZT vs basket of USD and EUR via 3m NDF	5/25/2023	494.1	470	512	10	1-Jun-23	470
Sell EUR/BRL	23/Feb/23	5.43	5.20	5.80	10	18-May-23	5.34
Short PLNHUF	4/25/2023	82	77.9	84.5	10	15-May-23	81.95
Pay PHP NDF Points	3/8/2023	12	25	5	10	9-May-23	16
Long EUR/CZK	27-May-22	24.7	25.9	22.5	10	4-May-23	23.5
Sell CNH/MXN	26-Oct-22	2.72	2.50	2.90	10	24-Apr-23	2.60
SELL USDZMW VIA 9M NDF	3/6/23	22.05	20	24	10	11-Apr-23	18.53
Sell ILSCZK	3/14/2023	6.12	5.6	6.5	10	11-Apr-23	5.9
Short PLNHUF	3/17/2023	84	79.8	86.5	10	29-Mar-23	81.3
Long USDTWD 12m NDF	11/18/2022	31.17	-	29.45	10	27-Mar-23	29.37
Short USDIDR	2/16/2023	15110	14700	15400	10	8-Mar-23	15400
short ILSZAR	2/2/2023	81.65	4.74	5.14	10	13-Feb-23	4.98
Long USDILS	19-Oct-22	3.54	3.72	3.2	10	13-Feb-23	3.542
Short CZKHUF	1/18/2023	16.53	15.7	17.05	10	13-Feb-23	16.25
Long KZT vs an equal basket of USD and EUR (3m NDF)	1/16/2023	494.9	470.2	509.7	10	15-Feb-23	468
Short EURGEL (using 3m NDF)	20-Oct-22	2.714	2.94	2.53	10	1-Feb-23	2.53
Buy USDZAR	1/19/2023	17.23	17.86	16.85	10	1-Feb-23	14
Short INR vs long IDR	11/18/2022	191.9	183	188	10	18-Jan-23	184.7

Note: Bid/offer spreads accounted for in entry and closing levels. Does not reflect tax, withholdings or any investment advisory fees. Past performance is no guarantee of future results. A complete performance record is available on request. Inception date – July 4, 2016. For additional discussion on baseline views, valuation and risks to closed trades, please see links to the relevant reports. Trade recommendations are highlighted green when the closing value is greater than the entry value and red when the closing value is less than or equal to the entry value. **Source:** BofA Global Research

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World At A Glance Projections

Exhibit 29: G10 FX Forecasts
Forecasts as of 8-Feb-2024

	Spot	Mar-24	Jun-24	Sep-24	YE 2024	Mar-25	Jun-25	Sep-25	YE 2025
G3									
EUR-USD	1.08	1.07	1.10	1.15	1.15	1.16	1.17	1.18	1.20
USD-JPY	149	145	143	142	142	140	138	136.00	136
EUR-JPY	161	155	157	163	163	162	161	160.00	163
Dollar Bloc									
USD-CAD	1.35	1.35	1.34	1.32	1.30	1.30	1.30	1.30	1.30
AUD-USD	0.65	0.66	0.68	0.71	0.71	0.71	0.71	0.71	0.71
NZD-USD	0.61	0.60	0.62	0.63	0.63	0.63	0.63	0.63	0.63
Europe									
EUR-GBP	0.85	0.87	0.87	0.88	0.88	0.87	0.87	0.86	0.86
GBP-USD	1.26	1.23	1.26	1.31	1.31	1.33	1.34	1.37	1.40
EUR-CHF	0.94	0.96	0.96	0.97	0.97	0.98	0.98	0.99	1.00
USD-CHF	0.88	0.90	0.87	0.84	0.84	0.84	0.84	0.84	0.83
EUR-SEK	11.28	11.70	11.40	11.20	11.10	11.10	11.00	10.90	10.80
USD-SEK	10.49	10.93	10.36	9.74	9.65	9.57	9.40	9.24	9.00
EUR-NOK	11.43	11.60	11.30	11.00	10.90	10.90	10.80	10.70	10.60
USD-NOK	10.62	10.84	10.27	9.57	9.48	9.40	9.23	9.07	8.83

Source: BofA Global Research, Bloomberg. Note: Forecasts as of 8-Feb-2024.

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Exhibit 30: EM FX Forecasts
Forecasts as of 8-Feb-2024

	Spot	Mar-24	Jun-24	Sep-24	YE 2024	Mar-25	Jun-25	Sep-25	YE 2025
Latin America									
USD-BRL	4.98	4.90	4.88	4.80	4.75	4.78	4.82	4.90	5.00
USD-MXN	17.09	17.80	17.90	18.30	18.50	18.70	18.90	19.10	19.50
USD-CLP	957	920	910	905	900	905	910	920	925
USD-COP	3,958	4,000	4,050	4,075	4,100	4,125	4,150	4,200	4,250
USD-ARS	831	1,100	1,500	1,670	2,200	2,700	3,200	3,800	4,500
USD-PEN	3.84	3.75	3.76	3.76	3.76	3.77	3.78	3.79	3.80
Emerging Europe									
EUR-PLN	4.32	4.36	4.33	4.29	4.25	4.24	4.23	4.21	4.20
EUR-HUF	387.68	390	395	395	399	387	375	362.00	350
EUR-CZK	25.07	24.90	25.00	24.80	24.60	24.40	24.20	24.00	24.00
USD-RUB	-	76.00	77.00	78.00	80.00				
USD-ZAR	18.96	18.60	18.50	17.70	17.80	17.90	18.00	18.20	18.40
USD-TRY	30.60	32.00	35.00	37.00	40.00	42.00	44.00	45.00	47.00
EUR-RON	4.98	5.01	5.02	5.04	5.05	5.13	5.21	5.28	5.36
USD-ILS	3.69	3.70	3.65	3.60	3.55	3.50	3.50	3.45	3.45
Asian Bloc									
USD-KRW	1,328.25	1,300	1,260	1,250	1,230	1,210	1,190	1,170.00	1,150
USD-TWD	31.36	31.20	31.00	30.70	30.45	30.15	29.90	29.80	29.50
USD-SGD	1.35	1.34	1.33	1.29	1.26	1.25	1.24	1.23	1.22
USD-THB	35.81	35.50	35.50	35.00	34.00	33.50	33.00	32.50	32.00
USD-HKD	7.82	7.83	7.83	7.80	7.78	7.76	7.75	7.75	7.75
USD-CNY	7.20	7.45	7.40	7.10	6.90	6.90	6.80	6.80	6.70
USD-IDR	15,635	15,400	15,400	15,300	15,200	15,200	15,100	15,100	15,000
USD-PHP	55.92	56.50	56.00	55.50	55.00	54.50	54.00	53.50	53.00
USD-MYR	4.77	4.70	4.60	4.60	4.50	4.40	4.30	4.20	4.10
USD-INR	82.96	83.00	82.50	82.00	82.00	81.50	81.00	81.00	81.00

Source: BofA Global Research, Bloomberg. Note: Forecasts as of 8-Feb-2024.

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