WELLS FARGO

International Commentary — June 25, 2024

International Economic Outlook: Mid-Year Outlook 2024

Summary

Forecast Changes

- Despite challenges—mostly geopolitical and monetary policy related—the global economy has been resilient over the first half of 2024. With that said, we have lowered our 2024 global GDP growth forecast marginally, to 2.9% from 3.0% last month. A softer outlook for the U.S. economy accounts for most of the downward revision, although we have also lowered our GDP growth forecasts for Canada, Australia and India relative to last month's publication.
- Given lingering inflation concerns, especially around services inflation, we forecast later or more gradual monetary easing from several central banks, including the European Central Bank, Bank of England, Norges Bank, Reserve Bank of Australia and Reserve Bank of New Zealand. We also forecast a slower pace of rate cuts from central banks in Mexico and Chile, while we expect the Bank of Japan to raise interest rates again in 2024 and also in 2025.
- We have made only modest changes to our outlook for the U.S. dollar. The current phase of elevated U.S. rates means the greenback can strengthen through Q3-2024, though the tendency for more gradual easing from foreign central banks could limit foreign currency declines over the next few months. Longer term, we forecast an extended period of greenback depreciation as U.S. growth slows more noticeably, the Fed lowers interest rates and global financial conditions ease.

Key Themes

- The economic growth divergence between the U.S. and G10 economies that was apparent early this year may be turning to convergence. There are tentative signs of an approaching U.S. economic slowdown, while European economies remain on an overall gradual upswing. We also observe a convergence on the inflation and interest rate front. Encouraging U.S. inflation readings means our view for Fed easing to begin in September is unchanged. Internationally, low productivity combined with labor cost pressures is contributing to lingering inflation risks, which could lead to later or more gradual easing from many foreign central banks.
- Converging growth trends are paired with a global economic outlook that has softened and become modestly more uncertain. Election outcomes across many emerging economies, and approaching elections in France and the U.K., have injected temporary uncertainty; however, we expect a fair degree of policy continuity and only moderate deviations from previous policy paths resulting in little prolonged economic or market impact. Fiscal policy dynamics have become less favorable in select Latin American economies, which has contributed to FX depreciation pressures building on currencies in Brazil and Colombia.
- With the Fed maintaining elevated interest rates for now, we continue to see dollar strength over the next several months, although more gradual easing from international central banks could limit foreign currency declines. Once the Fed begins easing from late this year we believe depreciation pressures can build on the greenback, and a downtrend in the dollar can persist for most of 2025. The yen, Australian dollar and Norwegian krone could perform well versus the U.S. currency during 2025, while we are not phased by recent volatility in Mexico and still see the Mexican peso as a long-term outperformer on lessening domestic political risk and attractive carry.

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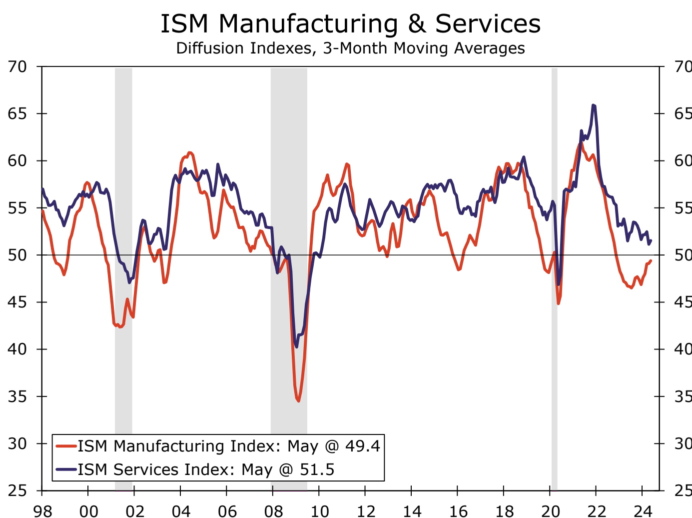
G10 Economic Divergence Turning to Convergence?

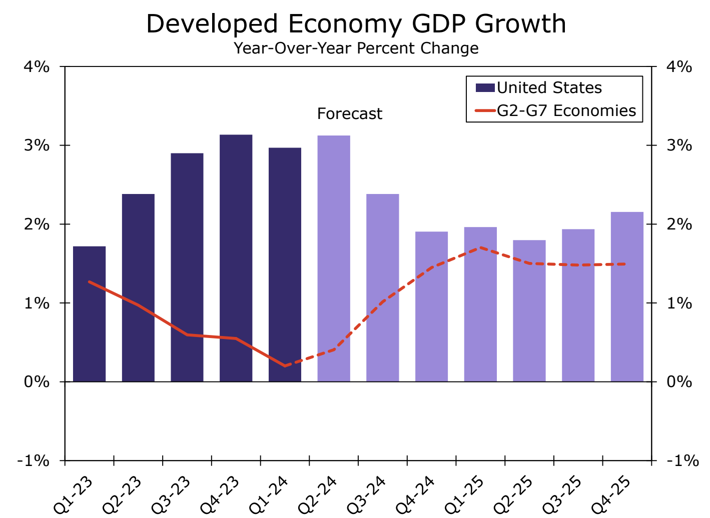
The first half of 2024 saw the global economy evolve in a broadly encouraging direction. U.S. activity demonstrated resilience during the early part of this year, while some foreign economies saw signs of gradual recovery. As a result, our forecast for 2024 global GDP growth has progressively improved over the first half of this year. In December of last year, we forecast the global economy to grow 2.4% this year, and as we reach the midpoint of 2024, we now forecast global growth of 2.9%, down modestly from 3.0% last month. But more recently, two noteworthy themes have emerged. First, we have observed tentative signs that U.S. economic outperformance is starting to wane. The core of the U.S. economy performed steadily during early 2024, but there are some signs of fraying around the edges. During the first quarter, final private domestic demand grew at a 2.8% quarterly annualized pace, although broader GDP growth slowed to just a 1.3% pace. Meanwhile, while sentiment surveys have shown some month-to-month volatility, the U.S. ISM manufacturing index has generally remained in contraction territory (Figure 1). In addition, the ISM services index has clearly softened. Hints of a possible slowdown in the U.S. labor market are also evident. While non-farm payrolls recorded another sturdy 272,000 gain in May, more timely or forward-looking indicators such as initial jobless claims, job openings, and temporary help employment point to a softening jobs trend ahead. And finally, we note that growth in household incomes has fallen below growth in consumer spending and will likely be a headwind to consumer spending moving forward. Together, these factors result in a lower 2024 U.S. GDP growth forecast of 2.3%, compared to 2.6% last month. The downward revision to our U.S. growth forecast accounts for much of our global growth downgrade for 2024.

Figure 1



Source: Datastream and Wells Fargo Economics

Figure 2



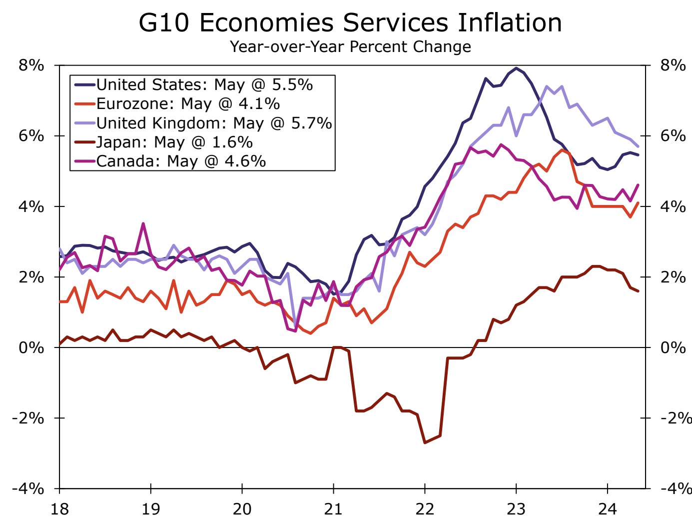
Source: Datastream and Wells Fargo Economics

In contrast to hints of a U.S. slowdown, some key foreign—most notably European—economies have shown a gradual upswing during the early quarters of 2024. Eurozone Q1 GDP rose 0.3% quarter-over-quarter after stagnating during the second half of last year, while U.K. Q1 GDP jumped 0.6% quarter-over-quarter after contracting in the second half of last year. Sweden's first quarter GDP also jumped after several quarters of poor economic performance, and Switzerland's Q1 GDP growth also firmed. Key international economies—particularly the Eurozone, United Kingdom and Canada—are seeing stronger growth in inflation-adjusted household incomes, the opposite of the trend underway in the United States. Moreover, sentiment surveys such as the Eurozone, U.K. and Swedish PMIs, along with the Swiss leading indicators, suggest that the European recovery has continued into the second quarter. There could, however, be a temporary blip in activity for the Eurozone and the United Kingdom, which saw some decline in the June PMI readings—a blip that appears to be related to upcoming elections in France in the United Kingdom. Still, given improving income and growth fundamentals, we doubt those election uncertainties will throw the European recovery off course. Not every G10 economy has benefited from an economic upswing this year, with the Asia-Pacific economies of Japan, Australia and New Zealand continuing to report underwhelming economic growth in early 2024. But from a global perspective, economic trends are relatively encouraging overall. G20 GDP growth held steady in Q1 at 3.3% year-over-year, while the global manufacturing and service

sector PMIs firmed further in April and May. With many foreign economies, in our view, on a gradual upswing, the economic growth divergence theme that was evident across the G10 economies early this year may be starting to turn toward growth convergence. In that sense, the wide growth gap that existed between the U.S. and other major economies in 2023 and early 2024 now appears to be in the process of narrowing (Figure 2). Point being, U.S. exceptionalism may be starting to fade, and a more constructive international environment could be starting to form.

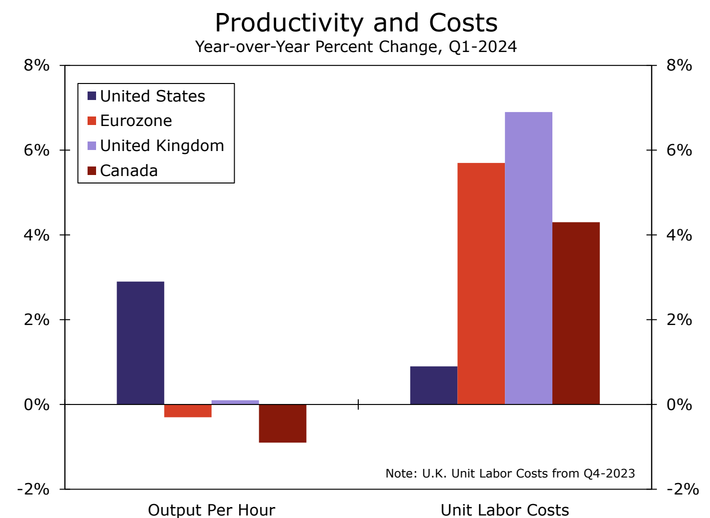
The second noteworthy theme is that economic growth is not the only area where trends are in the process of converging. U.S. inflation, and especially services inflation, was stubbornly persistent during the early months of this year. More recent U.S. inflation readings for April and May have been encouraging, and as a result, U.S. core CPI inflation slowed to 3.4% year-over-year in May. With the U.S. perhaps seeing some ebbing in demand-pull inflation as growth begins to slow, our outlook for Federal Reserve monetary policy is unchanged at this time. We still expect an initial 25 bps Fed rate cut in September and a further 25 bps rate cut in December. We also maintain our view that the Fed will lower its policy rate by a further cumulative 100 bps in 2025. However, certain international countries that had made significant disinflation progress still face lingering concerns surrounding elevated services inflation. In the United Kingdom, services prices rose 5.7% year-over-year in May, while in both the Eurozone and Canada, services inflation is running above 4% (Figure 3). The latest wage readings from the Eurozone, United Kingdom and Canada all show wage growth running above 5%. Given these dynamics, there is a risk that services inflation could recede more gradually across the G10 economies than previously expected and, similarly, central banks might move more cautiously along their monetary easing paths. Uncertainties around disinflation and rate cut cycles are reinforced by a comparison of recent productivity dynamics. While the U.S appears to be enjoying something of a productivity rebound with output-per-hour up 2.9% year-over-year in Q1, growth in productivity in other major economies is barely positive (U.K.) or indeed negative (Eurozone, Canada) (Figure 4). Without a perceptible productivity increase to offset elevated wage growth, unit labor cost pressures are also much more elevated across some key international economies. Higher unit labor costs suggests the risks for key international economies could be tilted toward a slower disinflation process than originally expected. Slower disinflation could also lead to foreign central banks lowering interest rates more gradually than previously expected. Overall, U.S. disinflation trends are turning somewhat more encouraging just as disinflation prospects elsewhere across the G10 are becoming less certain, suggesting some convergence in overall inflation dynamics.

Figure 3



Source: Bloomberg Finance L.P. and Wells Fargo Economics

Figure 4



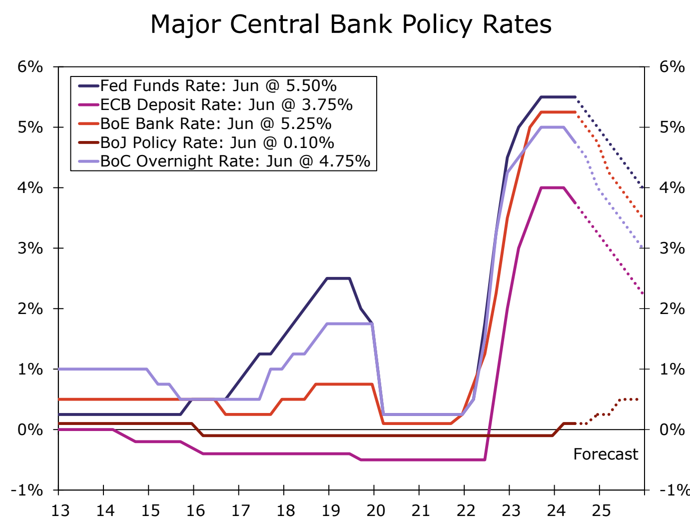
Source: Bloomberg Finance L.P. and Wells Fargo Economics

An Easing in the Pace of Major Central Bank Easing

Sticky inflation, particularly services inflation, was previously a risk to our central bank outlooks; however, this risk is now materializing. As a result, we believe international central banks will be more cautious toward rate cuts in the second half of this year, and we have adjusted our foreign policy rate forecasts accordingly (Figure 5). While the European Central Bank (ECB) delivered a widely expected

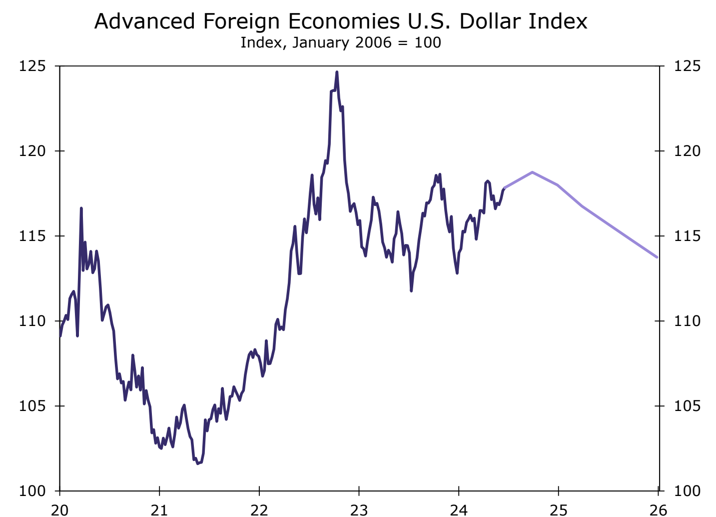
25 bps rate cut in June, we believe persistent wage growth and services inflation will make the ECB wary of proceeding too quickly with additional rate cuts moving forward. As a result, we expect the ECB to hold rates steady in July, and we now see only two more 25 bps rate cuts this year, one to be delivered in September and the other in December. If wage growth and services prices fail to recede, there is also a possibility the next ECB cut gets pushed back to October. In the United Kingdom, Bank of England (BoE) policymakers have to some extent downplayed the persistence of services inflation as due to temporary factors. For now, the BoE still appears on track to deliver an initial rate cut in August. That said, still elevated wage and price growth should keep policymakers cautious regarding the pace of its rate cuts, and we have pared back the amount of BoE easing we expect to be delivered this year. We now believe the Bank of England will cut its policy rate only twice this year, in August and November, which would see the policy rate end 2024 at 4.75%. After an upside inflation surprise in Canada, we now expect the central bank to pause in July before resuming rate cuts in September. Several other institutions are also likely to ease policy more gradually than we previously forecast. Norway's central bank held its policy rate steady at 4.50% this month and, citing elevated wages, provided forward guidance suggesting interest rates could remain steady for the rest of this year. Given that guidance, we pushed back the timing for an initial Norges Bank rate cut to Q4-2024, though we acknowledge Norges Bank easing could be pushed back further to 2025. Australia and New Zealand are both experiencing soft growth but elevated inflation, especially domestically-oriented inflation pressures. With inflation trends seemingly dominating the respective monetary policy outlooks, we now do not expect an initial rate cut from the Reserve Bank of Australia until February 2025, and we have also pushed back the timing of an initial rate cut from the Reserve Bank of New Zealand to November. Japan remains the outlier, and we now expect the Bank of Japan to raise interest rates in October and again in April 2025, and to dial back the pace of its bond purchases over the next several quarters.

Figure 5



Source: Bloomberg Finance L.P. and Wells Fargo Economics

Figure 6



Source: Bloomberg Finance L.P. and Wells Fargo Economics

G10 central banks are not the only institutions where we made changes to our monetary policy outlook. Emerging market central banks are also turning less dovish as inflation risks become more apparent, especially as local currencies are under pressure. Latin American central banks in particular have shifted less dovish, and the majority of our policy rate forecast adjustments come from regional institutions. Last month, we highlighted how Brazil's central bank is likely to keep policy settings steady through the end of 2025 as fiscal risks rise, currency depreciation materializes and services inflation remains elevated. In June, Brazilian Central Bank (BCB) policymakers indeed kept rates on hold and cited all of those risks as justification, while explicitly focusing on risks to inflation stemming from looser fiscal policy. For now, we continue to believe BCB policymakers will be on hold for an extended period of time; however, concerns around fiscal policy have also resulted in financial markets now pricing BCB rate hikes around the end of this year/early 2025. We also believe recent currency weakness in Mexico will keep Banxico policymakers on hold for several months. Lingering inflation concerns had already disrupted Mexico's easing cycle, and with the peso coming under pressure from a perceived rise in political risk, we expect policymakers to remain especially cautious for the time

being and do not expect rate cuts to resume until the fourth quarter of this year. Rounding out Latin America, we also forecast a more gradual pace of monetary easing from Chile's central bank. Chilean Central Bank (BCCh) policymakers slowed the pace of rate cuts in June, and while they communicated additional easing would still be forthcoming, we now believe the terminal rate will be higher than previously expected.

Our outlook for the U.S. dollar has not materially changed this month. For now, we continue to see U.S. dollar strength into Q3-2024 as the Fed delays easing until September, while central banks such as the ECB, Bank of Canada and Bank of England cut interest rates earlier than the FOMC. With that said, with several G10 central banks likely to ease monetary policy at a more gradual pace than previously envisaged, we forecast only limited foreign currency weakness in the interim. However, longer term, we continue to believe the greenback can weaken starting in Q4 of this year, and for dollar depreciation to persist over the course of 2025 (Figure 6). In our view, the combination of the Fed cutting interest rates and slower U.S. economic growth should place depreciation pressures on the U.S. dollar for an extended period of time. As far as growth, as mentioned, activity trends are tentatively starting to swing toward foreign economies. As G10 growth converges toward the U.S., and the U.S. exceptionalism theme fades, we believe sentiment toward foreign currencies can ultimately be supported. In addition, an FOMC that is lowering interest rates should also lead to easier global financial conditions and be supportive of global financial markets. As risk sentiment improves, demand for safe-haven currencies such as the U.S. dollar, in our view, should start to wane. As demand for safe-haven currencies fades, sentiment toward foreign currencies, and the more risk-sensitive currencies, should improve. Sentiment swings can support foreign currencies, both in the G10 and emerging markets.

Of course, foreign currency outperformers and underperformers will take shape. Perhaps one currency that could face further downside and underperform for now is the Canadian dollar. We expect Canadian economic growth to slow from its current pace, and we also see the Bank of Canada as likely to keep lowering policy interest rates at regular intervals, at a pace matching or quicker than many other major central banks this year. In that respect, Fed-BoC interest rate and growth differentials should result in short-term underperformance relative to G10 currency peers. Over the longer term and through much of 2025, we still view the yen as well-placed to benefit from Fed easing and lower U.S. bond yields. Over time, yield differentials can move in a direction that favors Japan's currency, rather than acting as a source of currency depreciation. We also expect the Australian dollar, Norwegian krone and, to a lesser extent, the New Zealand dollar, to strengthen over the medium term. Given elevated wage growth and inflation, we do not expect those central banks to begin easing until after the Federal Reserve—late 2024 in the case of Norway and New Zealand, and not until 2025 in the case of Australia. We also forecast only a gradual pace of rate cuts from those central banks thereafter. Elevated interest rates combined with a gradual pace of easing should be supportive of the respective currencies over time, though in the case of New Zealand, particularly soft economic growth could limit the extent of the currency's gain.

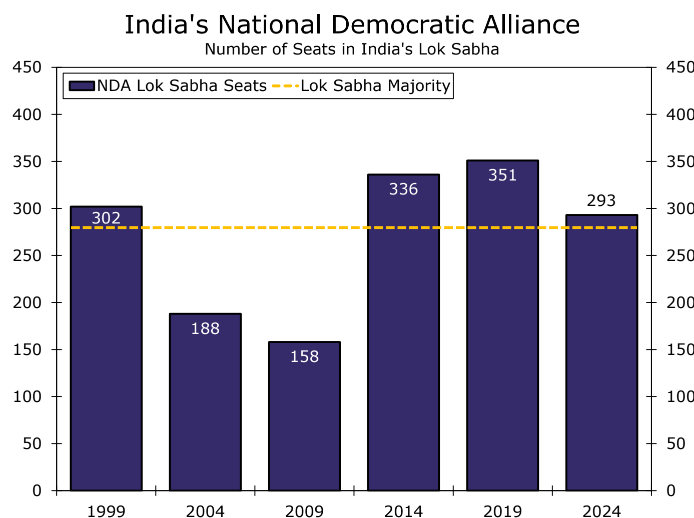
Global Election Reflections Follow Up

The relationship between growth, inflation and central bank monetary policy will likely continue to be the driving force of currency markets over the medium to longer term; however, local political developments have recently dictated the direction of currencies in select emerging market countries. Earlier this month, we shared our views on some of the more important elections that have taken place in the emerging world this year. In our Mid Year 2024 Election Reflections report, we noted that the takeaway from most elections, in our view, was policy continuity. While certain electoral outcomes did result in modest surprises, we believe elections will not fundamentally change the direction of policy in any of the major countries that hosted general elections this year. In certain cases, policy continuity carries a degree of caution. Case in point is Taiwan where the Democratic People's Party (DPP) was elected to a third consecutive term. At the core of the DPP's political platform is advancing the independence from Mainland China movement, which Chinese authorities have openly expressed frustration with. Over the course of the DPP's administration, we would expect independence efforts to persist, which in our view, will keep geopolitical tensions between Chinese authorities and Taiwan elevated. While we do not expect any direct confrontation, Chinese military activity along the border combined with event risks over the next few years (2024-2027) keeps the risk of an accident or strategic miscalculation elevated for the time being. Taiwan's election arguably represents the most concerning policy continuity outcome given the risks of military confrontation; however, unless the

most extreme downside scenario comes to fruition, we believe the path of the Taiwan dollar will not be materially or sustainably disrupted by local politics.

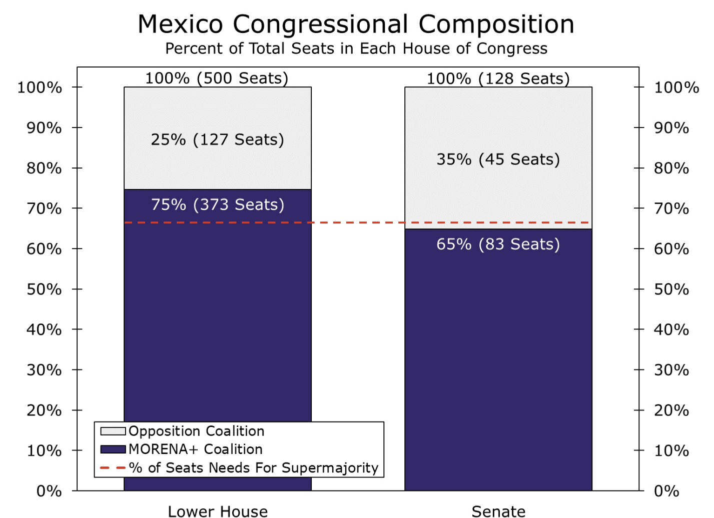
As far as surprises, India's general election was indeed a shock, especially when considering exit poll data. Exit polls suggested Prime Minister Modi's BJP would win a Lok Sabha majority on its own, while Modi's National Democratic Alliance (NDA) would secure a larger representation in India's parliament. Final vote tallies revealed BJP and the broader NDA severely underperformed relative to expectations as well as exit polls, and while Modi was still able to cobble together support to remain prime minister, his leadership is on a less stable foundation and is dependent on a handful of coalition partners with a history of flipping political allegiances (Figure 7). Modi's underperformance generated volatility in Indian financial markets; however, with Modi reappointed as prime minister and the surprise factor wearing off, local markets have calmed. Going forward, in our view, despite Modi's leadership on an unsteady bedrock, we believe India's reform agenda will remain intact and policy continuity will also be the takeaway of India's election. In that sense, efforts to integrate India into the global economy via enhanced manufacturing capabilities, and assimilate local equities and government bonds into global financial markets are likely to continue. We also believe India can receive an upgrade to its sovereign credit rating, and that Prime Minister Modi will continue India's geopolitical stance of maintaining neutrality related to the Russia-Ukraine conflict and the war in the Middle East. In some ways, a reliance on coalition partners could be a positive for India. Prime Minister Modi has orchestrated a hard line religious nationalism stance in an effort to improve his overall popularity. Religious nationalism-types of policies have often raised domestic and international concerns around Modi's social agenda, particularly from the coalition parties Modi now relies on. These same coalition partners may now be able to keep Modi's social agenda in check. While the election result was a surprise, we do not expect local economic or markets trends to be disrupted by local politics. We continue to believe India's economy can be one of the fastest growing economies in the world this year, while the Indian rupee can continue to outperform relative to peer emerging market currencies over the second half of 2024 and into 2025.

Figure 7



Source: India Election Commission and Wells Fargo Economics

Figure 8



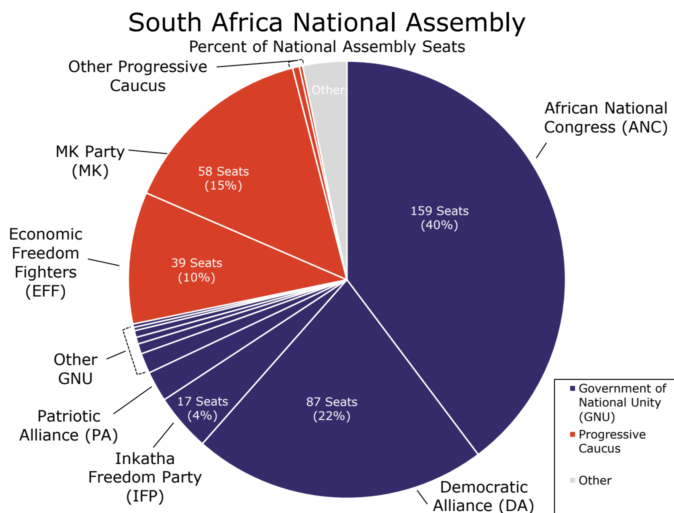
Source: INE and Wells Fargo Economics

Mexico's election also came as a surprise—more so at the congressional level rather than the presidency—and while modest policy changes may be implemented, we ultimately believe a strong sense of policy continuity will prevail in Mexico as well. Leading into the election, Claudia Sheinbaum, AMLO's hand-picked MORENA party successor, was widely expected to win the presidency; however, MORENA and coalition partners surprised by also winning an effective congressional supermajority (Figure 8). A congressional supermajority gives MORENA and its allies the voting power to enact constitutional amendments, many of which were proposed under AMLO and are designed to create a "one party" political dynamic in Mexico. Many of the amendments being considered would be perceived to erode the local democratic process, weaken the nation's key institutions and disrupt the overall governance structure in Mexico. Adding another wrinkle to constitutional reforms, AMLO will overlap with new congress members for about a month, further adding to markets' concerns

that amendments can be implemented with relative ease. Sheinbaum has also expressed a desire to explore and potentially implement select constitutional reforms even after AMLO formally exits office. These concerns drove a sharp selloff in the Mexican peso immediately after the election; however, we are not convinced Mexico is set to experience a fundamental rise in political risk and believe the peso can recover in the weeks, months and quarters ahead. In short, we expect cooler heads to prevail and the full slate of constitutional amendments will not be passed through congress. We struggle to believe policymakers will risk Mexico's position as a top nearshoring destination and broader financial instability for potentially little to no electoral benefit following landslide victories in the past two election cycles. Also, sustained currency depreciation risks renewed inflationary pressures and the central bank restarting its tightening cycle. A combination of high inflation and higher interest rates could push Mexico's economy into recession, a dynamic that could hurt Sheinbaum's credibility. Also, an erosion of governance and a weaker economy puts Mexico's investment grade credit ratings at risk. If Mexico loses investment grade status, capital outflows that place the longer-term health of the economy under pressure could materialize. And finally, AMLO also won a congressional supermajority in 2018; however, his more unorthodox constitutional amendments were never passed. History does not necessarily have to repeat itself, but we take some solace in the fact there is precedent in Mexico for pushing back against more radical policy proposals.

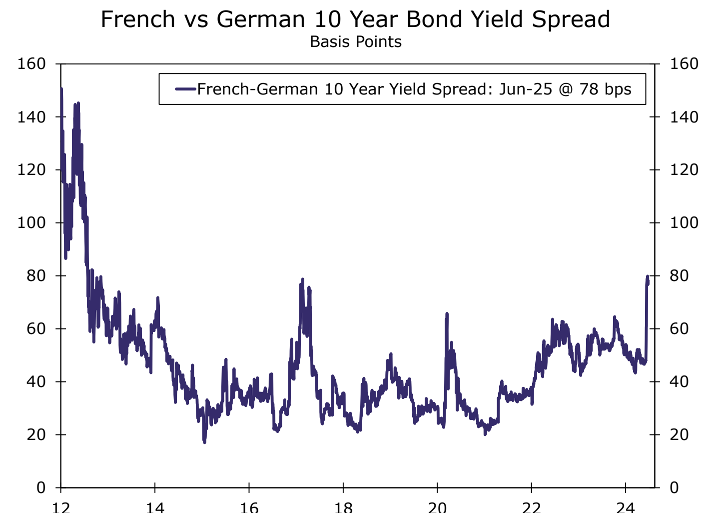
Our earlier election reflections report also highlighted South Africa and how the policy continuity theme may not necessarily play out in Africa's most industrialized nation post general elections. Our view leading into the election was that the incumbent African National Congress (ANC) would lose its governing majority and be forced into a legislative coalition. While the range of potential coalition partners was wide, we believed ANC policymakers would align with the main opposition Democratic Alliance (DA) to form a government and the populist Economic Freedom Fighters and MK Party would be excluded from the political alliance. South Africa's rand came under pressure as the ANC tentatively considered forming a national unity government that included the more radical political parties; however, ultimately our base case scenario materialized and the ANC-DA alliance with Ramaphosa still at the helm has been formed (Figure 9). In our view, the ANC-DA alliance is the best-case scenario for South Africa and the rand. Ramaphosa's reform agenda is still broadly intact, radical proposals are off the table, and DA policymakers may be able to influence fiscal policy in a more responsible direction, which South Africa needs. ANC and DA policymakers are not perfectly aligned on policies and a sense of policymaking paralysis may ensue long term, meaning full continuity is not the takeaway in South Africa, but news of the ANC-DA tie-up has pushed the rand back toward pre-election levels against the U.S. dollar. Going forward, political risks will linger, but we believe the probability of a downside scenario with the rand hitting a new low against the dollar due to local political developments has diminished. Going forward, we believe South Africa's currency will now be influenced more by global and external developments rather than local politics, and broadly follow the path of the U.S. dollar from here.

Figure 9



Source: All Africa, Eyewitness News, The South African and Wells Fargo Economics

Figure 10



Source: Bloomberg Finance L.P. and Wells Fargo Economics

A final and immediate election-related risk is the approaching legislative election in France, scheduled for two rounds on June 30 and July 7. French President Macron called snap legislative elections after his party performed poorly in European Parliament elections, losing heavily to the far-right National Rally. Recent polling, however, suggests Macron's party could suffer equally heavy losses in France's snap legislative elections. A Bloomberg-compiled poll of polls puts support for National Rally at 35%, the left-wing New Popular Front at 28%, and Macron's Ensemble coalition at 21%. Based on current polling, Macron's alliance appears very likely to lose its position as the largest party in the French legislature, a development that would erode the French president's influence and power. Instead, National Rally could secure the most seats, and thus potentially form a minority government or govern in coalition, but fall short of the 289 (out of 577) seats needed to form an outright majority. Importantly, should National Rally fall short of an outright majority, it could limit the extent to which they are able to pursue populist policies such as lower taxes, higher spending and a wider deficit. Far-right politicians no longer seek to remove France from the euro, which should limit the worst case impact on the currency. That said, while French election risks are to some extent already priced into the euro (Figure 10), should National Rally be able for secure some form of government it would likely interrupt France's fiscal consolidation efforts and also make France less inclined to contribute to, and become engaged in, European Union projects. All of these are factors that could, at the margin, slow the pace of the euro's recovery and appreciation prospects over the medium term.

Idiosyncrasies Make Selectivity Important in Emerging Markets

Election developments, along with other idiosyncratic local factors, lead us to believe that more selectivity will be needed when approaching the emerging markets in the second half of 2024, and possibly beyond. Yes, the Fed and the health of the global economy will matter for the direction of emerging market currencies in the second half of this year; however, as we witnessed recently, country-specific idiosyncrasies also matter and can strongly influence the path of local markets. Local politics can be a source of currency performance differentiation as country-specific political risk ebbs and flows. As mentioned, we tend to believe political risk in the above-mentioned countries will lessen in the months ahead, and affected currencies that have not fully rebounded by now could recover as election uncertainties recede. In addition to election risk, the direction of fiscal policy can also create differentiation. Just recently, fiscal policy developments have contributed to significant depreciations in the Colombian peso and Brazilian real. In Colombia, President Petro has encouraged looser fiscal policy in an effort to support economic activity. While the more radical fiscal policy changes have been rejected, Finance Minister Bonilla recently communicated that the debt ceiling had been raised and this year's fiscal deficit target may not be achieved, prompting Moody's to suggest negative ratings actions could be forthcoming should fiscal responsibility slacken. We believe Colombia could receive sovereign credit rating downgrades as a result of less fiscal discipline, and should Colombia lose its final investment grade rating, a crisis of confidence could unfold as select asset managers may be forced to sell sovereign exposures. Market participants will be paying close to Colombia's fiscal evolution from here, and with Colombia's central bank still likely to ease monetary policy going forward, a combination of a large fiscal deficit and reduced carry appeal could result in peso underperformance.

A lack of fiscal responsibility is also a theme impacting Brazil's currency. Recently, Finance Minister Haddad communicated that fiscal surplus targets, already previously relaxed, would not be met and the government would be targeting a primary fiscal balance rather than a surplus. Adding fuel to the fire were President Lula's comments that primary fiscal balance would be met through higher revenues rather than spending limitations. Brazil's debt burden is already high and unsustainable, and rhetoric suggesting a worsening fiscal position exacerbated concerns that Brazil's debt will continue to rise. Fiscal rhetoric has triggered a selloff in the Brazilian real, taking the currency from one of the top performing emerging currencies to a notable underperformer relative to the entire EM FX spectrum and peer Latin American currencies. Concerns around the direction of fiscal policy reached Brazil's central bank as policymakers, at a minimum, paused the monetary easing cycle in June citing the potential inflationary impact of more expansive fiscal spending. In our view, fiscal worries have intensified and are unlikely to dissipate in the near future. Against this fiscal backdrop, we reiterate our view that Brazilian Central Bank policymakers have ended their easing cycle. There is a risk rate cuts could resume in 2025 as Lula is set to appoint the new central bank governor and two additional monetary policy committee (COPOM) members, tilting the balance of COPOM in favor of Lula appointees. With Lula likely to still press for easier monetary policy next year, COPOM may feel compelled to cut rates in a show of allegiance toward the president. Cutting rates may not necessarily contribute to a weaker currency; however, should markets question the independence of Brazil's central bank, currency depreciation could persist over the medium to longer term. Fiscal slippage

and central bank independence concerns could also act as a source of Brazilian real performance underperformance over time.

Given new fiscal concerns we have turned less constructive on both the Brazilian real and Colombian peso, two examples of where selectivity in emerging markets has resulted in less optimism. On the other hand, other idiosyncratic events in select countries have either not disrupted our optimistic currency outlook or shifted us in a more positive direction. As far as countries with recent election surprises, we maintain our constructive outlook on the Indian rupee. In addition to our view for policy continuity and stable political risk, we believe the Reserve Bank of India (RBI) will keep policy rates steady until Q4-2024. While the rupee does not offer a significant amount of carry, RBI policymakers maintaining interest rates at current levels for the next few quarters preserves any carry appeal associated with the rupee and offers a sliver of insulation should the Federal Reserve not cut interest rates when, or as aggressively, as we expect. Despite new political uncertainties, we also reiterate our optimistic outlook for the Mexican peso. In addition to our rationale above, technocratic cabinet members have already been appointed by Sheinbaum, helping ease political risk. We also believe the Central Bank of Mexico (Banxico) will keep policy rates steady for most of 2024 as FX depreciation is likely to push inflation higher in the short term. Also, with policy uncertainty tied to the U.S. election likely to materialize in the coming months, we doubt Banxico policymakers will lower policy rates and potentially risk another bout of currency volatility leading into an uncertain U.S.-Mexico relationship and policy mix. In that sense, we believe Banxico will not restart its easing cycle until December with a 25 bps rate cut, and will also continue to communicate patience and caution when considering additional easing. As political risk improves and market participants refocus on underlying dynamics that made the peso a top performing currency for years, we believe the USD/MXN exchange rate can trend below MXN18.00 in the second half of this year and push toward MXN17.00 by the middle of 2025. We have also adopted a more constructive outlook on the Chilean peso. Chilean Central Bank (BCCh) policymakers have slowed the pace of easing, and we believe policymakers may be close to ending their easing cycle. In fact, policymakers may be ending the easing cycle just as the Fed begins lowering policy rates, which can place rate differentials on a more supportive path for the Chilean peso longer term.

Wells Fargo International Economic Forecast

	GDP				CPI			
	2022	2023	2024	2025	2022	2023	2024	2025
Global (PPP Weights)	3.5%	3.2%	2.9%	2.8%	8.7%	6.8%	3.6%	3.5%
Advanced Economies[1]	2.6%	1.6%	1.7%	2.0%	7.3%	4.6%	2.9%	2.5%
United States	1.9%	2.5%	2.3%	1.9%	8.0%	4.1%	3.1%	2.6%
Eurozone	3.4%	0.6%	0.8%	1.6%	8.4%	5.4%	2.3%	2.1%
United Kingdom	4.3%	0.1%	0.8%	1.5%	9.1%	7.3%	2.7%	2.3%
Japan	1.0%	1.8%	0.1%	1.4%	2.5%	3.3%	2.5%	2.0%
Canada	3.8%	1.2%	0.8%	1.8%	6.8%	3.9%	2.5%	2.1%
Switzerland	2.7%	0.7%	1.3%	1.5%	2.8%	2.1%	1.4%	1.2%
Australia	3.8%	2.0%	1.2%	2.1%	6.6%	5.6%	3.4%	2.7%
New Zealand	2.4%	0.6%	0.7%	2.3%	7.2%	5.7%	3.3%	2.2%
Sweden	2.7%	0.1%	1.1%	1.7%	8.1%	5.9%	2.9%	1.9%
Norway	3.0%	1.1%	0.7%	1.5%	5.8%	5.5%	3.4%	2.5%
Developing Economies[1]	4.1%	4.3%	3.9%	3.3%	9.8%	8.3%	4.1%	4.2%
China	3.0%	5.2%	5.1%	4.3%	2.0%	0.2%	0.8%	1.6%
India	6.5%	7.7%	7.0%	6.6%	6.7%	5.4%	4.8%	4.5%
Mexico	3.9%	3.2%	1.8%	2.1%	7.9%	5.5%	4.6%	4.1%
Brazil	3.0%	2.9%	1.8%	2.0%	9.3%	4.6%	4.0%	3.6%

Forecast as of: June 25, 2024

[1]Aggregated Using PPP Weights

Source: International Monetary Fund and Wells Fargo Economics

Wells Fargo International Interest Rate Forecast

(End of Quarter Rates)

Central Bank Key Policy Rate	2024			2025			
	Current	Q3	Q4	Q1	Q2	Q3	Q4
United States	5.50%	5.25%	5.00%	4.75%	4.50%	4.25%	4.00%
Eurozone[1]	3.75%	3.50%	3.25%	3.00%	2.75%	2.50%	2.25%
United Kingdom	5.25%	5.00%	4.75%	4.25%	4.00%	3.75%	3.50%
Japan	0.10%	0.10%	0.25%	0.25%	0.50%	0.50%	0.50%
Canada	4.75%	4.50%	4.00%	3.75%	3.50%	3.25%	3.00%
Switzerland	1.25%	1.00%	1.00%	1.00%	1.00%	1.00%	1.00%
Australia	4.35%	4.35%	4.35%	4.10%	3.85%	3.60%	3.35%
New Zealand	5.50%	5.50%	5.25%	5.00%	4.75%	4.50%	4.25%
Sweden	3.75%	3.50%	3.00%	2.75%	2.50%	2.25%	2.25%
Norway	4.50%	4.50%	4.25%	4.00%	3.75%	3.50%	3.25%
China[3]	10.00%	9.50%	9.50%	9.00%	9.00%	8.50%	8.50%
India	6.50%	6.50%	6.00%	5.75%	5.75%	5.75%	5.75%
Mexico	11.00%	11.00%	10.75%	10.25%	9.75%	9.25%	8.75%
Brazil	10.50%	10.50%	10.50%	10.50%	10.50%	10.50%	10.50%
Chile	5.75%	5.25%	5.00%	5.00%	5.00%	5.00%	5.00%
Colombia	11.75%	10.25%	9.25%	8.75%	8.25%	8.00%	8.00%

2-Year Note	2024			2025			
	Current	Q3	Q4	Q1	Q2	Q3	Q4
United States	4.74%	4.35%	4.05%	3.85%	3.70%	3.55%	3.45%
Eurozone[2]	2.79%	2.80%	2.70%	2.60%	2.50%	2.40%	2.30%
United Kingdom	4.20%	4.10%	3.95%	3.80%	3.65%	3.50%	3.40%
Japan	0.31%	0.35%	0.40%	0.45%	0.50%	0.55%	0.55%
Canada	3.98%	3.90%	3.65%	3.50%	3.35%	3.20%	3.10%

10-Year Note	2024			2025			
	Current	Q3	Q4	Q1	Q2	Q3	Q4
United States	4.24%	4.15%	4.00%	3.90%	3.85%	3.80%	3.75%
Eurozone[2]	2.40%	2.40%	2.40%	2.35%	2.35%	2.30%	2.30%
United Kingdom	4.07%	4.00%	3.90%	3.80%	3.70%	3.60%	3.50%
Japan	1.00%	1.05%	1.10%	1.15%	1.20%	1.20%	1.15%
Canada	3.38%	3.35%	3.25%	3.20%	3.15%	3.10%	3.10%

Forecast as of: June 25, 2024

[1] ECB Deposit Rate [2] German Government Bond Yield [3] Reserve Requirement Ratio Major Banks

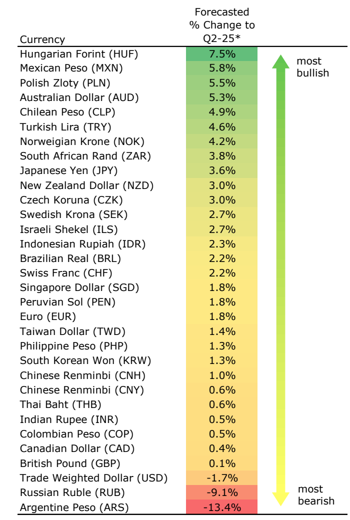
Source: Bloomberg Finance L.P. and Wells Fargo Economics

Wells Fargo International FX Forecast

Currency Pair*	Current Rate	Q3-2024	Q4-2024	Q1-2025	Q2-2025	Q3-2025	Q4-2025
G10							
EUR/USD	1.0707	1.0600	1.0700	1.0800	1.0900	1.1000	1.1100
USD/JPY	159.62	160.00	157.00	155.00	154.00	153.00	152.00
GBP/USD	1.2684	1.2600	1.2500	1.2600	1.2700	1.2900	1.3100
USD/CHF	0.8940	0.9100	0.9025	0.8900	0.8750	0.8625	0.8550
USD/CAD	1.3651	1.3800	1.3800	1.3700	1.3600	1.3500	1.3400
AUD/USD	0.6646	0.6600	0.6800	0.6900	0.7000	0.7100	0.7200
NZD/USD	0.6115	0.6000	0.6100	0.6200	0.6300	0.6400	0.6500
USD/NOK	10.6064	10.6125	10.4675	10.3250	10.1825	10.0450	9.9100
USD/SEK	10.5068	10.6125	10.5150	10.3700	10.2300	10.0900	9.9550
Asia							
USD/CNY	7.2631	7.2900	7.2600	7.2400	7.2200	7.2000	7.1800
USD/CNH	7.2892	7.3000	7.2600	7.2400	7.2200	7.2000	7.1800
USD/IDR	16375	16500	16400	16200	16000	15800	15600
USD/INR	83.43	83.75	83.50	83.25	83.00	82.75	82.50
USD/KRW	1387.41	1400.00	1390.00	1380.00	1370.00	1360.00	1350.00
USD/PHP	58.77	59.50	59.00	58.50	58.00	57.50	57.00
USD/SGD	1.3543	1.3600	1.3500	1.3400	1.3300	1.3200	1.3100
USD/TWD	32.45	32.75	32.50	32.25	32.00	31.75	31.50
USD/THB	36.71	37.25	37.00	36.75	36.50	36.25	36.00
Latin America							
USD/BRL	5.4176	5.5000	5.5000	5.4000	5.3000	5.2000	5.1000
USD/CLP	944.34	930.00	920.00	910.00	900.00	880.00	860.00
USD/MXN	17.9945	17.7500	17.5000	17.2500	17.0000	17.0000	16.7500
USD/COP	4070.61	4150.00	4150.00	4100.00	4050.00	4000.00	3950.00
USD/ARS	909.50	940.00	970.00	1000.00	1050.00	1100.00	1150.00
USD/PEN	3.8080	3.8000	3.7800	3.7600	3.7400	3.7200	3.7000
Eastern Europe/Middle East/Africa							
USD/CZK	23.17	23.50	23.25	23.00	22.50	22.00	21.50
USD/HUF	369.94	372.75	359.75	351.75	344.00	336.25	328.75
USD/PLN	4.0169	4.0575	3.9725	3.8900	3.8075	3.7275	3.6475
USD/RUB	85.42	90.00	90.00	92.00	94.00	96.00	98.00
USD/ILS	3.7367	3.7000	3.6800	3.6600	3.6400	3.6200	3.6000
USD/ZAR	18.1592	18.2500	18.0000	17.7500	17.5000	17.2500	17.0000
USD/TRY	32.9437	33.0000	32.5000	32.0000	31.5000	31.0000	30.5000
Euro Crosses							
EUR/JPY	170.90	169.50	168.00	167.50	167.75	168.25	168.75
EUR/GBP	0.8441	0.8425	0.8550	0.8575	0.8575	0.8525	0.8475
EUR/CHF	0.9572	0.9650	0.9650	0.9600	0.9550	0.9500	0.9500
EUR/NOK	11.3561	11.2500	11.2000	11.1500	11.1000	11.0500	11.0000
EUR/SEK	11.2495	11.2500	11.2500	11.2000	11.1500	11.1000	11.0500
EUR/CZK	24.81	25.00	25.00	24.75	24.50	24.25	24.00
EUR/HUF	396.08	395.00	385.00	380.00	375.00	370.00	365.00
EUR/PLN	4.3008	4.3000	4.2500	4.2000	4.1500	4.1000	4.0500

Forecast as of: June 25, 2024

Source: Bloomberg Finance L.P. and Wells Fargo Economics



Currency	Forecasted % Change to Q2-25*
Hungarian Forint (HUF)	7.5%
Mexican Peso (MXN)	5.8%
Polish Zloty (PLN)	5.5%
Australian Dollar (AUD)	5.3%
Chilean Peso (CLP)	4.9%
Turkish Lira (TRY)	4.6%
Norweigian Krone (NOK)	4.2%
South African Rand (ZAR)	3.8%
Japanese Yen (JPY)	3.6%
New Zealand Dollar (NZD)	3.0%
Czech Koruna (CZK)	3.0%
Swedish Krona (SEK)	2.7%
Israeli Shekel (ILS)	2.7%
Indonesian Rupiah (IDR)	2.3%
Brazilian Real (BRL)	2.2%
Swiss Franc (CHF)	2.2%
Singapore Dollar (SGD)	1.8%
Peruvian Sol (PEN)	1.8%
Euro (EUR)	1.8%
Taiwan Dollar (TWD)	1.4%
Philippine Peso (PHP)	1.3%
South Korean Won (KRW)	1.3%
Chinese Renminbi (CNH)	1.0%
Chinese Renminbi (CNY)	0.6%
Thai Baht (THB)	0.6%
Indian Rupee (INR)	0.5%
Colombian Peso (COP)	0.5%
Canadian Dollar (CAD)	0.4%
British Pound (GBP)	0.1%
Trade Weighted Dollar (USD)	-1.7%
Russian Ruble (RUB)	-9.1%
Argentine Peso (ARS)	-13.4%

Forecast as of: June 25, 2024
*Percentage Change Against USD, Q2-25 Vs. Current Spot Rate

Source: Bloomberg Finance L.P. and Wells Fargo Economics

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