WELLS FARGO

International Commentary — October 26, 2021

International Economic Outlook: October 2021

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Summary

Forecast Changes

- As the outlook for the global economy continues to soften, we have again revised our 2021 global GDP forecast lower. We now expect the global economy to grow 5.8% this year as the recovery stalls amid ongoing COVID-related disruptions as well as a sharp economic deceleration in China.
- But despite a worsening growth outlook, we have brought forward the timing of interest rate hikes for a few notable central banks. Given rising inflationary pressures and hawkish policymaker commentary, we now believe the Bank of England will begin its rate hike cycle at its November meeting. In addition, local fiscal and political worries as well as elevated inflation lead us to believe the Brazilian Central Bank will take an even more hawkish stance on monetary policy.
- With global growth still trending softer and the Fed likely to taper asset purchases in the near future, we continue to believe the U.S. dollar can broadly strengthen through the end of this year. In addition, we believe dollar strength could persist into early 2022 as the Fed continues to trim asset purchases and financial markets may be priced for too much monetary tightening at select foreign central banks.

Key Themes

- The global economy continues to face a flurry of issues. COVID-related growth disruptions have been persistent, while regulatory changes and property sector challenges have weighed on China's economy. As the Northern Hemisphere heads into the winter and holiday months, another wave of COVID infections seems quite likely, while issues in China will likely linger for the time being. Against this backdrop, the outlook for the global economy has softened, and we think risks around our global growth forecast remain tilted to the downside.
- Even though growth prospects have slowed, inflation expectations continue to rise. We can point to supply chain disruptions and higher commodity prices as drivers of price pressures, and expect these rising inflation pressures to result in further monetary tightening from central banks around the world. However, while we agree on the direction of monetary policy, we believe financial markets may be expecting foreign central banks to normalize monetary policy at too quick of a pace, especially the Bank of England.
- Our forecast for a stronger U.S. dollar through the end of this year remains intact; however, we believe there is increasing scope for a resilient greenback into 2022 as country-specific factors and fundamentals evolve in a way that could be conducive to foreign currency weakness. As financial markets reprice monetary policy expectations abroad and the Fed tapers asset purchases in 2022, foreign currencies could weaken. In addition, local political developments across the emerging markets could result in idiosyncratic events weighing on emerging market currencies throughout next year and also contribute to broad U.S. dollar strength.

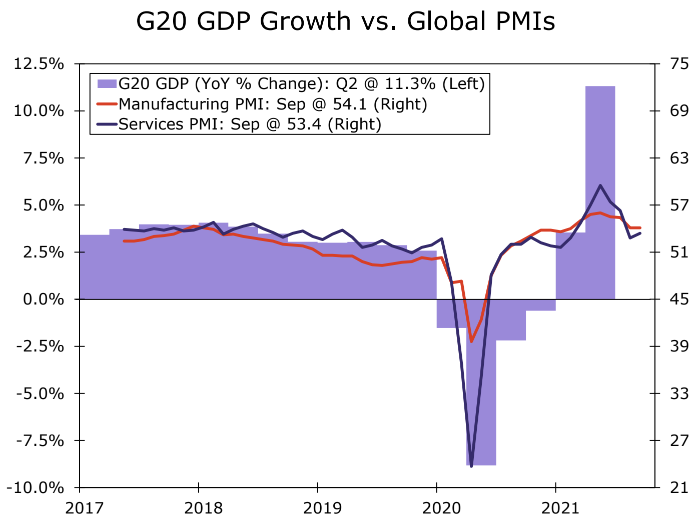
Global Growth Slowdown to Continue

The global economy has contended with a myriad of issues in recent months. Starting in the summer, the Delta variant emerged and proved to be more contagious than prior strains of the virus. Outbreaks across the major developed and emerging economies saw a partial reimposition of government-enforced restrictions around the world. In addition, out of an abundance of caution on the health front, consumers voluntarily restricted their activities, delaying their return to normal life and regular spending patterns. These restrictions, both voluntary and involuntary, have had negative implications for global economic growth, and are still issues the global economy is working through. In addition to COVID-related disruptions, growth prospects in China have dwindled over the past few months amid President Xi Jinping's goal for common prosperity. A harsh regulatory crackdown on multiple sectors has resulted in a sell-off in local Chinese equity markets and waning confidence toward China as an investment destination. On top of the regulatory crackdown, but not completely distinct, have been concerns regarding the sustainability of China's real estate sector as well as the financial problems at Evergrande. China's real estate industry has experienced a notable slowdown recently, and with the industry and related activities accounting for close to 30% of China's economy, a lack of confidence in the property sector has contributed to a marked deceleration in the Chinese economy.

While we recognized and appreciated the headwinds facing the global economy, we thought these issues would be temporary and have only a modest impact on global output. Over the past few months, the economic effects of the Delta variant and China's softening growth outlook have proved to be more severe than initially expected. To that point, high frequency measures of global economic activity softened over the course of Q3. The global manufacturing PMI moved lower over the course of the quarter, while the services PMI trended downward in Q3 as a result of COVID-related restrictions (Figure 1). In our view, COVID issues and China's recent struggles will not be going away just yet. As we head into the winter and holiday months in the Northern Hemisphere, another wave of virus infections seems more than likely. Reports from sector analysts also indicate there is potential for a significant energy shortage and an energy crisis could be looming. Should these concerns materialize, global manufacturing, and particularly Chinese manufacturing, could experience another setback, while domestic and international travel would likely be disrupted yet again.

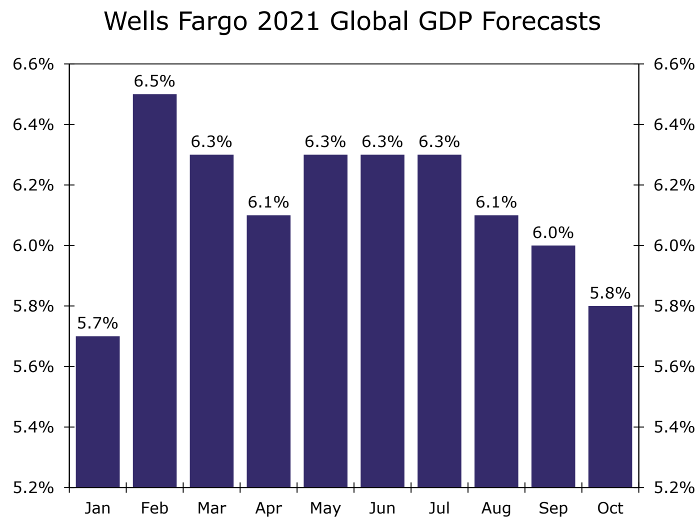
As we think about these issues and update our global economic outlook, we again recognize that global economic growth is on a downward trajectory. **As a result, we revised our global GDP forecast lower and now forecast the global economy to grow 5.8% this year**. This month's forecast update marks the third downward revision in as many months to our global GDP forecast and a sharp downward adjustment from the 6.5% global economic expansion we forecast back in February (Figure 2). We also believe the risks to our current forecast remain tilted to the downside. Should the energy shortage intensify and another COVID wave materialize, at least one more downward revision to the global growth outlook could be appropriate. The economic impact, should these risks manifest and persist for a period of time, could also spillover into 2022 and complicate the global growth picture next year. For now, we forecast global growth in excess of 4% next year, which represents above-trend growth for the global economy. Should COVID continue to be an issue and China's economy decelerate even further, we could eventually revise our 2022 outlook to show just pre-COVID, trend-style growth prospects for the global economy.

Figure 1



Source: Datastream and Wells Fargo Securities

Figure 2



Source: Wells Fargo Securities

Slower Growth Hasn't Stopped Central Bank Tightening

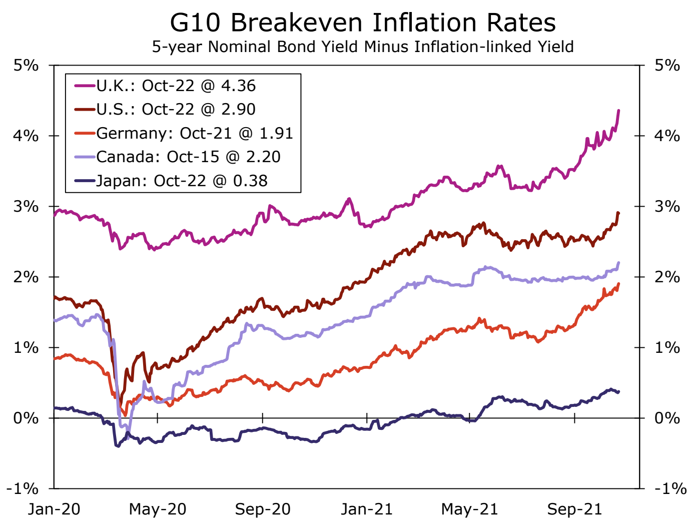
Despite less optimistic growth prospects, central banks around the world continue to tighten monetary policy, or have at least started the process of preparing financial markets for an imminent tightening. Just recently, the Reserve Bank of New Zealand (RBNZ) lifted its Cash Rate 25 bps to 0.50%, the first rate hike in New Zealand since 2014. In Norway, the Norges Bank raised its Deposit Rate 25 bps, taking the main policy rate to 0.25%, while also providing forward guidance for additional rate hikes before the end of this year. In addition, Bank of Canada (BoC) policymakers continue to signal a further tapering of asset purchases is likely. But perhaps the most significant monetary policy developments have come from the Bank of England (BoE). In recent weeks, BoE policymakers have started to signal interest rate hikes could be forthcoming in the very near future, probably as early as November. Hawkish rhetoric from Governor Andrew Bailey saw financial market participants dramatically bring forward expectations for interest rate hikes in the United Kingdom. We have also adjusted our view for BoE monetary policy as well. Given hawkish commentary from Bailey and other BoE members, we now expect the Bank of England to raise interest rates 15 bps to 0.25% at the November meeting, a much earlier forecast than we previously expected.

In just about all cases of central bank monetary policy tightening, we can point to rising inflation and inflation expectations as the justification. Across the G10, inflation has risen significantly over the past 12 months, especially in economies where COVID-related restrictions have been eased and vaccination rates are relatively high. Inflation in the United States, United Kingdom, Canada and New Zealand is currently above target, while policymakers at those central banks seem to be more concerned that price growth may not be as transitory as initially thought. As far as inflation expectations, breakeven inflation rates have jumped in many of the major developed economies over the past few months. To that point, five-year breakeven rates, a benchmark gauge for future inflation, in the U.S., U.K., Eurozone and Canada have trended higher as supply chain disruptions persist and as commodity prices are likely to stay elevated for the time being (Figure 3). Even in Japan, where inflation has failed to reach the Bank of Japan's inflation target for years, price expectations have risen and the five-year breakeven rate remains in positive territory. However, it is our sense that financial markets may be priced too aggressively for tightening from select central banks. Granted, we agree on the direction of monetary policy, and we believe policy rates will generally move higher; however, we disagree with the timing and, in some cases, the magnitude of these rate hikes.

Starting with the U.K., we believe financial markets have turned too hawkish on the Bank of England. Again, we agree interest rates will be lifted in the U.K. come November and will be raised further in 2022; however, financial markets expect the Bank of England to raise interest rates to 0.75% over the next six months (Figure 4). In our view, the Bank of England will take a more measured approach to lifting interest rates as the economy has recently demonstrated uneven growth amid rising COVID cases and energy shortages. In the next six months, we forecast the BoE policy rate to rise to 0.25%

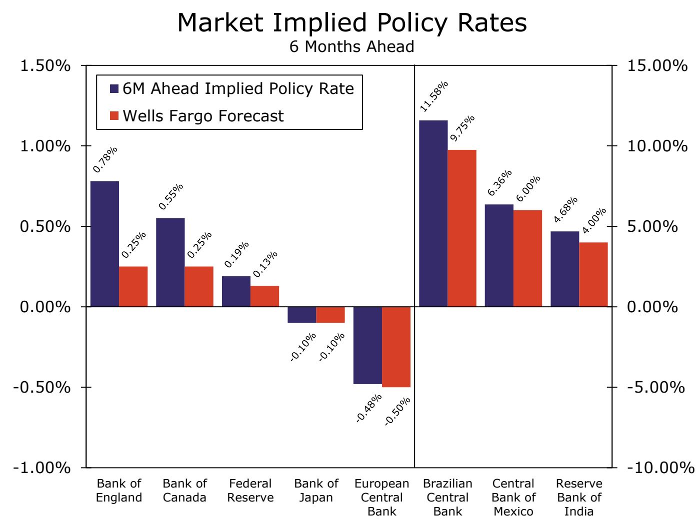
and for financial markets to eventually scale back expectations for rate hikes in the United Kingdom. The same can be said in Canada where markets are priced for at least one 25-bp rate hike at the Bank of Canada's April meeting. In our view, the Canadian economy is strong enough to justify a reduction in asset purchases this year, although we believe the initial BoC rate hike will not come until the second half of 2022. Similar to the Bank of England, we believe financial markets will adjust to our view on Canadian monetary policy in the not too distant future. And in the emerging markets, we believe markets are still priced for too much tightening at some of the major developing economy central banks, in particular the Brazilian Central Bank (BCB) and Reserve Bank of India (RBI). Elevated inflation and currency weakness are valid concerns in Brazil; however, we believe the BCB will not look to disrupt the economic recovery too severely with overly aggressive monetary tightening. Indeed, we expect BCB policymakers to turn more hawkish through the end of this year, although markets may be priced for too aggressive tightening in 2022. In India, the economy is surely recovering from the devastating second wave of COVID infections earlier in the year. But, with inflation prospects somewhat subdued and the recovery still fragile, we expect the RBI to keep monetary policy ultra-accommodative for the foreseeable future.

Figure 3



Source: Bloomberg LP and Wells Fargo Securities

Figure 4



Source: Bloomberg LP and Wells Fargo Securities

U.S. Dollar Strength Could Persist into 2022

The external environment we highlighted above should, in our view, be conducive to U.S. dollar strength through at least the end of this year. We believe a decelerating global economy that is still facing serious and potentially longer-term risks, should attract safe-haven capital flows toward the U.S. dollar. As safe-haven flows hit the U.S. dollar, we expect most G10 currencies to weaken, with some of the more risk-sensitive currencies, such as the Australian dollar, to underperform. In addition, G10 currencies that are associated with dovish central banks should also experience weakness. In that sense, we expect the Japanese yen and Swedish krone to come under pressure through the end of Q4-2021. And finally, the euro should continue to weaken amid a persistently dovish European Central Bank, that in our view, is nowhere near normalizing monetary policy. We also expect the euro to continue its status as one of the most popular funding currencies for investors looking at carry trade opportunities, which should keep downward pressure on the common currency for the time being.

Also supporting our view for short-term dollar strength is an elevated likelihood the Fed officially announces a decision to taper asset purchases in the near future. Given recent commentary from Fed Chair Powell and other FOMC members, we believe a taper announcement could take place as early as November and for the actual reduction in asset purchases to begin in December. We believe the Fed's inflation goals have largely been met, and while the September non-farm payrolls report was underwhelming, we think the U.S. labor market has progressed sufficiently to warrant scaling back quantitative easing. In our view, a Fed taper decision should also attract market participants toward the U.S. dollar. We also believe uncertainty around the health of the global economy has made market participants more sensitive to monetary policy decisions. While the Fed has been relatively clear in its forward guidance, lingering concerns around the health of the global economy could result in more pronounced dollar strength in the immediate aftermath of the Fed's November monetary policy assessment.

Emerging market currencies could also experience challenging times over the next few months. Slowing global growth and tighter Fed monetary policy should result in broadly weaker currencies across the emerging markets spectrum through the end of this year. Currencies associated with weak underlying economic fundamentals, unattractive real interest rate differentials with the U.S. dollar, and where the economy relies on foreign investor participation in local markets to fund current account deficits should come under the most pressure. In addition, currencies associated with elevated political risks could also be more vulnerable to sizable deprecations. In this sense, we believe the South African rand and Indonesian rupiah could be at risk, while the Mexican and Colombian pesos could come under pressure. Aside from external developments, country-specific and idiosyncratic events are also beginning to have a larger influence over the path of certain emerging market currencies, and these developments are likely to continue for the time being. Fiscal and political risks have weighed on the Brazilian real, and as the 2022 presidential election gets closer, we expect fiscal and political dynamics to result in a weaker currency over the course of our forecast horizon. And finally, the Turkish lira has experienced yet another significant depreciation. President Erdogan exerted his influence over the central bank and forced a large interest rate reduction, while he also purged members of the central bank not aligned with his views on monetary policy. In addition, geopolitical tensions could be rising amid pressure from major foreign countries for Erdogan to release a prisoner perceived to be a critic of the Turkish governor. In our view, a lack on independence at the Turkish central bank and geopolitical risks associated with the Erdogan administration could place pressure on the lira for the foreseeable future.

This broad strength in the U.S. dollar against G10 and emerging market currencies could persist into 2022, especially as financial markets adjust to the timing and magnitude of tighter monetary policy abroad and as the Fed tapers asset purchases over the course of next year. Should markets scale back expectations for tighter monetary policy in countries such as the United Kingdom and Canada as well as select emerging market countries, the U.S. dollar could trend higher for longer than we currently expect. We also expect the Fed's plans to taper asset purchases to be uninterrupted and for quantitative easing in the United States to end midway through 2022. Tighter Fed monetary policy in 2022 and slower policy tightening from foreign central banks could result in a stronger greenback into early next year as well. For now, we believe the U.S. dollar will revert to a weaker trend over the longer term; however, given recent developments, that longer-term outlook is also evolving and the greenback's performance could be more mixed. We still expect U.S. dollar softness against many foreign currencies, but also see increasing potential for U.S. dollar resilience against several foreign currencies based on country-specific fundamentals.

Global Economic Forecasts

Wells Fargo International Economic Forecast

	GDP				CPI			
	2020	2021	2022	2023	2020	2021	2022	2023
Global (PPP Weights)	-3.1%	5.8%	4.2%	3.2%	3.2%	4.1%	3.9%	3.3%
Advanced Economies[1]	-4.5%	5.3%	4.1%	2.8%	0.7%	3.2%	2.9%	1.7%
United States	-3.4%	5.6%	4.0%	3.2%	1.2%	4.5%	4.2%	1.8%
Eurozone	-6.3%	5.0%	4.2%	2.2%	0.3%	2.3%	1.7%	1.5%
United Kingdom	-9.8%	7.0%	4.4%	2.2%	0.9%	2.2%	2.7%	2.1%
Japan	-4.6%	2.3%	2.8%	1.7%	0.0%	-0.2%	0.6%	0.6%
Canada	-5.3%	5.4%	4.1%	2.3%	0.7%	3.2%	2.5%	2.1%
Switzerland	-2.5%	3.3%	3.0%	2.0%	-0.7%	0.5%	0.6%	0.7%
Australia	-2.4%	3.7%	3.4%	3.1%	0.9%	2.4%	1.9%	2.1%
New Zealand	-2.1%	4.9%	3.8%	2.8%	1.7%	2.8%	2.3%	2.2%
Sweden	-2.8%	4.3%	3.4%	2.2%	0.7%	1.8%	1.6%	1.5%
Norway	-0.8%	3.5%	3.9%	2.1%	1.3%	2.9%	2.1%	1.9%
Developing Economies[1]	-2.1%	6.2%	4.3%	3.6%	5.1%	4.8%	4.7%	4.6%
China	2.3%	8.0%	5.5%	5.4%	2.4%	1.1%	2.1%	2.2%
India	-7.3%	8.2%	8.1%	5.0%	6.2%	5.0%	4.6%	4.8%
Mexico	-8.3%	6.2%	3.1%	2.4%	3.4%	5.5%	4.5%	3.8%
Brazil	-4.1%	5.2%	1.8%	2.3%	3.2%	8.5%	5.0%	3.5%

Forecast as of: October 26, 2021

[1]Aggregated Using PPP Weights

Source: International Monetary Fund and Wells Fargo Securities

Interest Rate Forecasts

Wells Fargo International Interest Rate Forecast

(End of Quarter Rates)

	Central Bank Key Policy Rate					
	2021	2022				2023
	Q4	Q1	Q2	Q3	Q4	Q1
United States	0.25%	0.25%	0.25%	0.25%	0.25%	0.25%
Eurozone[1]	-0.50%	-0.50%	-0.50%	-0.50%	-0.50%	-0.50%
United Kingdom	0.25%	0.25%	0.50%	0.50%	0.75%	0.75%
Japan	-0.10%	-0.10%	-0.10%	-0.10%	-0.10%	-0.10%
Canada	0.25%	0.25%	0.25%	0.50%	0.75%	1.00%

	2-Year Note					
	2021	2022				2023
	Q4	Q1	Q2	Q3	Q4	Q1
United States	0.35%	0.45%	0.65%	0.85%	1.05%	1.25%
Eurozone[2]	-0.65%	-0.65%	-0.60%	-0.60%	-0.55%	-0.55%
United Kingdom	0.60%	0.75%	0.90%	1.05%	1.20%	1.30%
Japan	-0.10%	-0.10%	-0.10%	-0.10%	-0.05%	-0.05%
Canada	0.75%	0.90%	1.05%	1.20%	1.35%	1.45%

	10-Year Note					
	2021	2022				2023
	Q4	Q1	Q2	Q3	Q4	Q1
United States	1.70%	1.90%	2.00%	2.10%	2.15%	2.20%
Eurozone[2]	-0.20%	-0.15%	-0.10%	0.00%	0.15%	0.30%
United Kingdom	1.10%	1.25%	1.40%	1.50%	1.60%	1.65%
Japan	0.10%	0.10%	0.15%	0.15%	0.20%	0.20%
Canada	1.60%	1.85%	1.95%	2.10%	2.20%	2.30%

Forecast as of: October 26, 2021

[1] ECB Deposit Rate [2] German Government Bond Yield

Source: Bloomberg LP and Wells Fargo Securities

Currency Forecasts

Currency Pair*	Current rate	Q4-2021	Q1-2022	Q2-2022	Q3-2022	Q4-2022	Q1-2023
G10							
EUR/USD	1.1587	1.1500	1.1400	1.1400	1.1500	1.1600	1.1700
USD/JPY	114.23	115.00	116.00	117.00	118.00	119.00	120.00
GBP/USD	1.3773	1.3600	1.3400	1.3400	1.3500	1.3600	1.3700
USD/CHF	0.9206	0.9250	0.9350	0.9375	0.9350	0.9300	0.9275
USD/CAD	1.2386	1.2500	1.2500	1.2300	1.2100	1.1900	1.1800
AUD/USD	0.7503	0.7300	0.7100	0.7200	0.7300	0.7400	0.7500
NZD/USD	0.7157	0.7000	0.6900	0.7000	0.7100	0.7200	0.7300
USD/NOK	8.3627	8.5225	8.5975	8.5100	8.3475	8.2325	8.1200
USD/SEK	8.6241	8.7825	8.8600	8.8150	8.6950	8.5775	8.4625
Asia							
USD/CNY	6.3833	6.4000	6.4000	6.3800	6.3600	6.3400	6.3200
USD/CNH	6.3811	6.4000	6.4000	6.3800	6.3600	6.3400	6.3200
USD/IDR	14153	14300	14400	14300	14200	14100	14000
USD/INR	74.96	75.50	75.75	75.75	76.00	76.00	76.25
USD/KRW	1167.40	1180.00	1180.00	1175.00	1170.00	1165.00	1160.00
USD/PHP	50.77	51.25	51.25	51.00	50.75	50.50	50.25
USD/SGD	1.3480	1.3500	1.3600	1.3600	1.3500	1.3400	1.3300
USD/TWD	27.84	28.00	28.00	27.75	27.50	27.25	27.00
USD/THB	33.12	33.50	33.50	33.25	33.25	33.00	33.00
Latin America							
USD/BRL	5.5759	5.7000	5.8000	5.9000	6.0000	6.1000	6.2000
USD/CLP	806.75	820.00	830.00	840.00	850.00	860.00	870.00
USD/MXN	20.1884	20.5000	20.5000	20.2500	20.0000	19.7500	19.5000
USD/COP	3777	3900	3900	3850	3800	3750	3700
USD/ARS	99.5145	102.0000	105.0000	108.0000	111.0000	114.0000	117.0000
USD/PEN	3.9893	4.0200	4.0400	4.0600	4.0800	4.0600	4.0400
Eastern Europe/Middle East/Africa							
USD/CZK	22.18	22.50	22.75	22.50	22.25	21.75	21.25
USD/HUF	314.91	317.50	324.50	320.25	313.00	306.00	299.25
USD/PLN	3.9734	4.0000	4.0300	3.9900	3.9125	3.8350	3.7600
USD/RUB	69.61	70.00	70.00	69.00	68.00	67.00	66.00
USD/ILS	3.1991	3.2000	3.2000	3.1900	3.1800	3.1700	3.1600
USD/ZAR	14.8284	15.0000	15.2500	15.5000	15.7500	16.0000	16.2500
USD/TRY	9.5451	10.0000	10.2500	10.5000	10.7500	11.0000	11.2500
Euro Crosses							
EUR/JPY	132.36	132.25	132.25	133.50	135.75	138.00	140.50
EUR/GBP	0.8413	0.8450	0.8500	0.8500	0.8525	0.8525	0.8550
EUR/CHF	1.0667	1.0650	1.0650	1.0700	1.0750	1.0800	1.0850
EUR/NOK	9.6900	9.8000	9.8000	9.7000	9.6000	9.5500	9.5000
EUR/SEK	9.9928	10.1000	10.1000	10.0500	10.0000	9.9500	9.9000
EUR/CZK	25.70	26.00	26.00	25.75	25.50	25.25	25.00
EUR/HUF	364.88	365.00	370.00	365.00	360.00	355.00	350.00
EUR/PLN	4.6040	4.6000	4.6000	4.5500	4.5000	4.4500	4.4000

Forecast as of: October 26, 2021

Source: Bloomberg LP and Wells Fargo Securities

United States/USD

Outlook

We expect a period of U.S. dollar strength to persist through the end of this year, followed by a more mixed performance by the greenback as 2022 progresses. For the immediate period ahead, positive factors for the U.S. dollar include the likelihood of a tapering in the Fed's bond purchases as soon as next month, and slowing global growth, which could offer some safe-haven support. If international central banks fail to fully deliver on near-term rate hike expectations, that could also provide support to the U.S. dollar. That said, with Fed rate hikes still some ways off, the U.S. dollar could eventually slip against some currencies where central banks are likely to be more active, though the greenback could remain reasonably resilient against currencies where growth and monetary policy prospects are more uncertain.

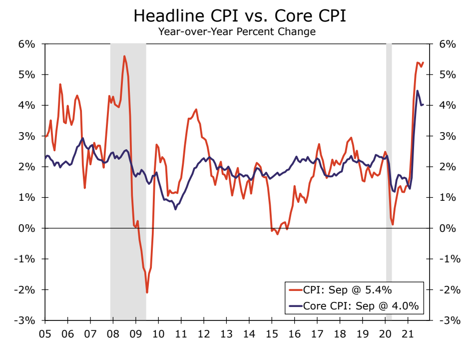
Fundamental Focus: Economics, Policy & FX

U.S. Economy Trends Are Steady, Not Spectacular

- Recent U.S. data suggest the economy continues to advance at a respectable pace, although an ongoing slowdown in growth since earlier this year remains evident.
- Perhaps most notably, the September employment report disappointed, as nonfarm payrolls rose just 194,000, although that was partly offset by upward revisions to prior months. The jobless rate fell to 4.8%. Despite the underwhelming nature of the report, it was probably strong enough for the Fed to begin adjusting its monetary policy stance in November.
- Other September activity data were mixed. Retail sales unexpectedly rose 0.7% month over month; however, industrial output fell 1.3%.
- Perhaps the most positive recent news has been reflected in business confidence surveys, as the September ISM manufacturing index rose to 61.1 and the ISM services index edged higher to 61.9.
- Given the mixed and underwhelming news on economic activity, we have lowered our forecast for 2021 U.S. GDP growth to 5.6%, from 5.9% previously. For 2022, we expect GDP growth to slow further to 4.0%.
- Meanwhile, inflation remains persistently elevated. For September, the CPI edged higher to 5.4% year over year, while the core CPI was steady at 4.0% year over year.

Fed Set to Make Formal Taper Announcement in November

- The latest jobs report was probably "good enough" for the Fed to announce a long-awaited adjustment to its monetary policy stance. We believe the Fed is more likely to announce a tapering of its bond purchases at its Nov. 3 meeting, rather than at the Dec. 15 meeting.
- With respect to the pace of tapering, we expect policymakers to set the pace such that purchases cease by mid-2022.
- While monetary policy is the immediate focus, fiscal and budget policy may come back into focus in December. U.S. lawmakers passed a short-term increase to the debt ceiling in the past month; however, the increase was modest and the issue will come back into focus again in December. Democratic lawmakers are also continuing discussions to pass the bipartisan infrastructure bill, as well as a broader spending bill.



Source: U.S. Department of Labor and Wells Fargo Securities

Economic & FX Risks

Upside FX Scenario

- Our base case is for U.S. dollar strength to persist through the end of 2021, with a more mixed performance by the greenback as next year progresses. However, there is also a risk scenario in which an extended period of U.S. dollar strength could materialize.
- U.S. inflation has remained stubbornly elevated. Should those inflation pressures persist, the Fed could taper its bond purchases even faster than expected and bring forward the expected timing of interest rate increases. Both would likely boost U.S. yields and support the U.S. dollar.
- On the flip side, market participants have recently priced in reasonably aggressive rate hike expectations over the next several quarters. Should international central banks fail to fully deliver on those expectations, foreign currencies could also come under pressure versus the U.S. dollar.
- U.S. financial market sentiment appears relatively calm for now. However, COVID developments and Chinese developments still have some potential to surprise in the months ahead, prompting unsettled markets and likely U.S. dollar strength.
- Should these scenarios play out, U.S. dollar strength should be more persistent and could last through most and perhaps even all of 2022.

Central Bank Outlook

Fed Funds Rate Forecast			
Current: 0.125%	**3M**	**6M**	**12M**
Wells Fargo	0-0.25%	0-0.25%	0-0.25%
Market Implied	0.13%	0.19%	0.46%

Source: Bloomberg LP and Wells Fargo Securities

- We expect the Fed to shortly begin to slow its bond purchases from the current purchase pace of $80 billion worth of Treasury securities and $40 billion worth of mortgage-backed securities every month. Specifically, we view a formal tapering announcement as most likely at the Nov. 3 policy meeting, and that policymakers will set the pace of tapering such that net purchases come to an end around mid-2022.
- In our view, policy interest rate increases are still a ways away. We expect the Fed to maintain its current target range for the fed funds rate of between 0% and 0.25% for an extended period, but eventually see rate hikes by late 2023, with a cumulative 75 bps of rate hikes forecast over the second half of that year.

Eurozone/EUR

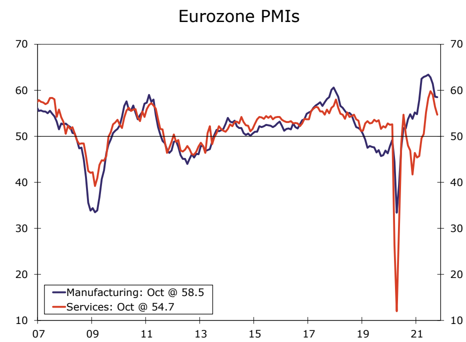
Outlook

We expect euro weakness into the early part of 2022 and only a limited recovery in the currency thereafter. While fundamentals still appear supportive of medium-term expansions, economic growth appears to be losing significant momentum in late 2021. And while inflation pressures have firmed, the uptick in underlying inflation seems less marked for now, with ECB policymakers viewing the inflation spike as temporary. Against the backdrop of slower growth and a cautious central bank that will likely taper its bond purchases only gradually, we see further weakness in the euro for now. Moreover, with ECB rate hikes a distant prospect, the euro should remain a popular funding currency, and any medium-term rebound in the euro should be modest at best.

Fundamental Focus: Economics, Policy & FX

Growth Slows a Little...

- While growth likely continued at a respectable clip during the third quarter, there were some signs of a moderation in the pace of expansion as the quarter continued.
- Activity data have been mixed. August retail sales rose 0.3% month over month, less than expected and following a large 2.6% fall in July. Meanwhile, August industrial output fell 1.6%.
- The Eurozone PMIs have also softened in recent months, a trend that continued in October. The services PMI fell to 54.7, while the manufacturing PMI was broadly steady at 58.5. Eurozone September economic confidence was little changed at 117.8.
- Despite somewhat mixed trends in recent months, we believe the prospects for continued Eurozone expansion are quite good. To date, there has not been a significant, renewed uptick in COVID cases across the region. Consumer finances are also still in good shape—for the second quarter, Eurozone household disposable income rose 4.9% year over year, while the household saving rate of 19.0% is still at a historically elevated level.
- We forecast Eurozone GDP growth of 5.0% in 2021, slowing to 4.2% in 2022.



Source: Datastream and Wells Fargo Securities

Inflation Quickens a Little...

- Eurozone CPI inflation has started to move higher, though the increase has so far been led by energy prices. The September CPI quickened to 3.4% year over year, with energy prices rising 17.6%.
- That is not to say there hasn't been some increase in underlying price pressures. First, upstream price pressures are evident in the price components of the Eurozone PMIs, while producer prices have also quickened markedly. And at the consumer price level, there has also been some modest acceleration of underlying inflation trends. For instance, September saw the core CPI rise 1.9% year over year and the services CPI rise 1.7%.
- Still, after a near-term spike, we expect the Eurozone to moderate back below 2% over the medium term. In a similar vein, ECB policymakers do not yet appear convinced we are seeing a sustained pickup of inflation, with ECB President Lagarde describing the current spike as "largely transitory."
- As a result, we expect the ECB to announce at its December monetary policy that it intends to taper its overall bond purchases at only a very gradual pace during 2022.

Downside FX Scenario

- We see the euro as vulnerable for now, and see only moderate gains in the euro over the medium term. That said, the risks to our base case scenario for EUR/USD are likely still tilted to the downside.
- Activity growth has been uneven recently. We expect solid consumer fundamentals will see a resumption of more steady economic growth over time; however, should that take longer than expected, the euro could come under pressure.

- So far, energy prices have driven inflation higher, with underlying inflation pressures showing only a moderate increase. If the Eurozone inflation uptick proves briefer than we anticipate, the ECB could maintain accommodative monetary policy for an extended period and taper its bond purchases even more gradually than forecast. In an environment where many global central banks are tightening policy, that would likely weigh on the euro.
- In this downside scenario, the EUR/USD exchange rate could fall into a $1.1000-$1.1200, or possibly below.

Central Bank Outlook

ECB Deposit Rate Forecast			
Current: -0.50%	**3M**	**6M**	**12M**
Wells Fargo	-0.50%	-0.50%	-0.50%
Market Implied	-0.51%	-0.49%	-0.43%

Source: Bloomberg LP and Wells Fargo Securities

- The ECB's December monetary policy meeting now looms as the next key event. At that meeting, we expect the ECB to announce it will fully complete its €1,850B PEPP program broadly as expected, and no later than Q2-2022. Upon completion of the PEPP program, we expect the ECB to increase the pace of its regular asset purchase program to €50B per month, from €20B per month currently.
- We expect interest rates to remain unchanged for an extended period. We forecast the ECB's Deposit Rate will remain at -0.50% through all of 2021, 2022 and 2023.

Japan/JPY

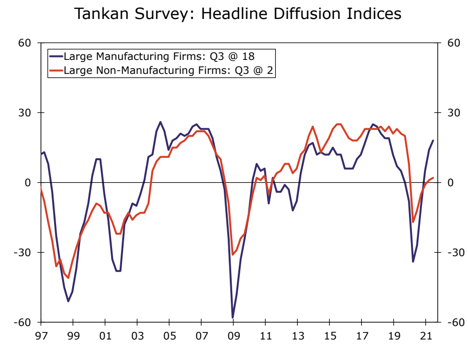
Outlook

The yen has softened markedly versus the greenback in recent weeks, a trend we believe is likely to continue over the medium term. A state of emergency that had affected large parts of the country was lifted in late September, improving growth prospects for Q4-2021 and 2022. However, inflation pressures are still absent, meaning the Bank of Japan's especially accommodative monetary policy should persist. As international bond yields move higher, that should continue to pressure the yen lower, particularly if other risk factors such as COVID concerns or Chinese economic concerns also eventually ease. We expect the yen to soften versus the greenback as well as most other G10 currencies over the medium term.

Fundamental Focus: Economics, Policy & FX

Japanese Growth: Darkest Before the Dawn?

- The third quarter was challenging for Japan's economy, as a state of emergency remained in place for Tokyo and surrounding regions, with restrictions not lifted until the end of September.
- As a result, recent activity data have been uniformly weak. August retail sales slumped 4.1% month over month, while the tertiary industry index (a broader measure of service sector activity) fell 1.7%. August industrial output also fell 3.6%.
- However, with an end to restrictions and the potential for some fiscal support in the months or quarters ahead, the growth outlook for Q4 and 2022 is more encouraging. So far, this is primarily reflected in confidence surveys. For Q3, the closely followed Tankan survey showed an increase in the large manufacturers' index to +18 and an increase in the large non-manufacturers' index to +2. For September, the economy watchers survey rose to 42.1, while the October manufacturing PMI rose to 53.0 and the services PMI rose to 50.7.
- We have revised our 2022 GDP growth forecast for Japan higher, though at 2.8% it will still hardly be a banner year as far as Japanese economic recovery is concerned.
- While growth prospects have improved a bit, inflation prospects remain subdued. To be sure, the September CPI rose 0.2% year over year and the CPI excluding fresh food rose 0.1%. However, much of that was energy driven, and excluding energy, inflation remains in negative territory.



Source: Datastream and Wells Fargo Securities

Keeping Up with Politics and Policy

- Japan's Fumio Kishida of the Liberal Democratic Party was appointed by parliament as the country's new prime minister in early October, and immediately called for a general election on Oct. 31. He also said he would set up a "new capitalism" seeking to spread the fruits of economic growth.
- Kishida also called for the compilation of an extra budget after the general election to add to the economic stimulus, seeking to have it approved by parliament by the end of the year. The size and scope of any extra budget is unclear at this point, though some media reports have hinted at an economic package of as much as ¥20 trillion-¥30 trillion.

Economic & FX Risks

Downside FX Scenario

- We expect the yen to weaken versus the greenback over the medium term. However, there is a scenario that could see the yen soften more than we currently forecast.
- Inflation pressures remain absent in Japan. Globally however, should price pressures prove more persistent than expected and the Federal Reserve in particular moves to less accommodative monetary policy, global bond yields should rise further, which should weigh on the yen.

- We expect Japanese growth to improve in the coming quarters, though if the pickup is more gradual than forecast, the yen may experience additional weakness.
- In this downside scenario for the Japanese currency, the USD/JPY exchange rate could reach JPY125.00 or beyond.

Upside FX Scenario

- We also see a potential upside scenario for Japan's currency. The economy could rebound more quickly than expected, especially in the context of additional fiscal stimulus. While that may not elicit a monetary policy response, stronger growth could nonetheless improve yen sentiment.
- Internationally, central banks may not raise rates as quickly as currently anticipated, while COVID developments or Chinese developments could still present lingering concerns. These scenarios could dampen global bond yields, which should be yen positive.
- In this upside scenario for the Japanese currency, the USD/JPY exchange rate may not move much beyond JPY115.00, which is close to current levels.

Central Bank Outlook

BoJ Policy Rate Forecast			
Current: -0.10%	**3M**	**6M**	**12M**
Wells Fargo	-0.10%	-0.10%	-0.10%
Market Implied	-0.03%	-0.02%	-0.02%

Source: Bloomberg LP and Wells Fargo Securities

- Our outlook is for the Bank of Japan to hold its policy rate steady at -0.10% through all of 2021, 2022 and 2023, and to make no major changes to its quantitative easing program. Despite the underwhelming performance of Japan's economy, we see only limited risk of a further reduction in the Bank of Japan's already negative policy interest rate.

United Kingdom/GBP

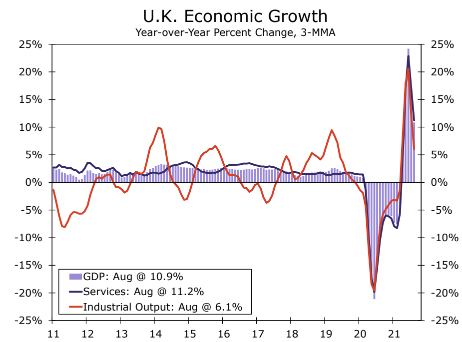
Outlook

We expect weakness in the pound for the immediate period ahead, though we see some potential for a moderate recovery over time. Activity growth has been uneven and COVID concerns have resurfaced, while inflation has jumped higher. Against this backdrop, we expect the Bank of England to start raising interest rates very soon, though perhaps at a more gradual pace than generally anticipated. Subdued growth and only moderate tightening could weigh on the pound for now. However, over time, as markets policy expectations are recalibrated and the U.K. enjoys steadier growth, we see potential for gains in the U.K. currency, especially with a cautious U.K. central bank likely raising interest rates before the Fed begins its own rate hike cycle.

Fundamental Focus: Economics, Policy & FX

An Uneven Advance for the U.K. Economy

- The U.K. recovery has been uneven in recent months, with both good and bad news on the economy. In terms of the broadest measure of economic activity, August GDP rose 0.4% month over month, slightly less than expected, while July GDP was revised to show a small fall compared to the previously reported small rise. In terms of the details, August services activity rose 0.3%, only half as much as forecast, while industrial output rose.
- September retail sales were similarly downbeat, as sales dipped 0.2% month over month, the fifth monthly decline in sales in a row.
- Confidence surveys showed mixed momentum for the U.K. economy in the third quarter as well as into the fourth quarter. For October, the PMI surveys were an upside surprise, as the manufacturing PMI rose to 57.7 and the services PMI rose to 58.0, though there is perhaps some skepticism as to how long that uptick in confidence will last.
- Another favorable economic print came from labor market data for the three months to August, which showed a large rise in employment, while there were also signs of some firming in underlying wage growth.
- Given the mixed news, the near-term outlook for the economy remains moderate and somewhat uncertain, especially as recent weeks have seen a rebound in new COVID cases, which has some potential to crimp activity. We expect the U.K. economic expansion to continue; however, we also anticipate an ongoing slowing in the pace of growth over time.



Source: Datastream and Wells Fargo Securities

Bank of England Ready for Interest Rate Lift-Off

- While activity growth has been uneven, CPI inflation has for the most part been trending higher. The September CPI was the exception to that rule, as headline inflation eased to 3.1% year over year and core inflation eased to 2.9%. That will likely be a temporary lull, however, as higher energy prices and signs of firmer wage growth are likely to boost inflation again in the coming months.
- Moreover, the latest CPI reading comes against a backdrop of increasingly hawkish comments from central bank policymakers. Recently, Bank of England Governor Bailey said rising energy prices mean inflation “will last longer and it will of course get into the annual numbers for longer as a consequence,” while also adding that it "raises for central banks the fear and concern of embedded expectations. That’s why we, at the Bank of England have signaled, and this is another signal, that we will have to act."
- In this context, we think the September CPI print was hot enough for the Bank of England to kick off its rate hike cycle. We expect the central bank to raise its policy rate by 15 bps to 0.25% at its November meeting. We forecast gradual tightening next year and anticipate 25 bps of rate increases at the May 2022 and November 2022 meetings.

Economic & FX Risks

Downside FX Scenario

- We expect the pound to appreciate modestly against the U.S. dollar over the medium term. However, the pound could face potential downside in the near term, as well as a slower rate of appreciation over the medium term than we currently forecast.
- Market participants have priced in aggressive rate hike expectations for the upcoming months. Should the Bank of England fail to deliver on those expectations, that could weigh the pound.
- Recent U.K. activity data has been uneven and uncertain. If U.K. growth slows more sharply than expected that would likely be negative for the pound, while a recent rebound in COVID cases could also weigh on U.K. currency sentiment.
- Global bond yields have risen in recent weeks as monetary tightening expectations have firmed internationally. Should the trend of higher yields intensify, that would likely restrain the U.K. currency.
- In this more cautious scenario, we would expect the pound to underperform, with the GBP/USD perhaps falling as low as a $1.2800-$1.3000 range, and rebounding only modestly over the medium-term.

Central Bank Outlook

BoE Bank Rate Forecast			
Current: 0.10%	**3M**	**6M**	**12M**
Wells Fargo	0.25%	0.25%	0.50%
Market Implied	0.47%	0.75%	1.07%

Source: Bloomberg LP and Wells Fargo Securities

- Given recent hawkish comments from U.K. central bankers, we expect the Bank of England to raise its policy rate 15 bps to 0.25% at its November meeting. In 2022, however, we see only a gradual pace of monetary tightening, and forecast 25 bps rate hikes at the May 2022 and November 2022 announcements. Market expectations for BoE tightening are more aggressive, anticipating around 100 bps of cumulative tightening over the next 12 months. Finally, we expect Bank of England tightening will continue in 2023, with further rate increases slated for that year.

Switzerland/CHF

Outlook

Despite recent franc gains, we see increasing potential for a softening in the Swiss franc over the medium term. Confidence surveys have been softer on balance, pointing to slower growth ahead. Thus, even with a modest pickup in inflation recently, the Swiss National Bank seems likely to continue with its accommodative monetary policy stance for an extended period. In addition, the central bank also appears to have been somewhat more active intervening in FX markets in recent months. In an environment of global monetary tightening and rising global bond yields, the Swiss franc should underperform, the risk to that view being unexpected market stress that could contribute to unexpected franc resilience.

Fundamental Focus: Economics, Policy & FX

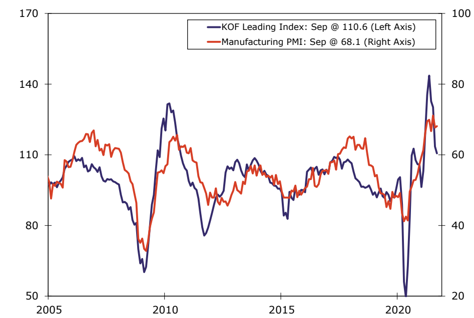
More of the Same from Switzerland

- Mixed economic news from Switzerland in recent weeks suggests the country continues to experience a steady, rather than strong, recovery.
- The closely followed KOF leading indicator fell further in September to 110.1, an indicator of potentially slower growth ahead. On a more positive note, the September manufacturing PMI edged higher to 68.1.
- August real retail sales also rose 1.1% month over month, which was the first monthly increase since March. September external trade figures were yet another mixed data point, as real exports rose 0.4% month over month but real imports fell 0.8%.
- Inflation has moved higher, but not by anywhere near enough for the Swiss National Bank to even contemplate any shift in monetary policy. The September CPI rose 0.9% year over year, while the August trimmed mean CPI rose 0.6%.
- Given the lack of strong themes for directional trends from within Switzerland, the franc will likely stay beholden to global developments in the months ahead.

Hints of Rising Foreign Exchange Intervention

- Among the elements of the Swiss National Bank's monetary policy that does not appear to have changed is it willingness to intervene in foreign exchange markets. The central bank's FX intervention totaled 5.44B francs in Q2, up from just 0.30B francs during Q1. September foreign exchange reserves rose 10.4B francs to 940B francs.
- The Swiss National Bank's recent uptick in intervention activity could well be a restraining factor for the franc moving forward.

Swiss Leading Indicators



Source: Bloomberg LP and Wells Fargo Securities

Economic & FX Risks

Downside FX Scenario

- Our outlook is for gradual weakness in the franc versus the euro and U.S. dollar over the medium term; however, there is some risk of an even faster decline.
- Swiss National Bank monetary policy will likely remain on hold for an extended period, meaning that in a world of rising global bond yields, Swiss yields are unlikely to follow international yields meaningfully higher. That widening (negative) yield gap could weigh on the franc more than we expect.
- The central bank has become more active intervening in FX markets in recent months. Should that activity persist, or should global jitters eventually ease over time, the franc would likely face additional downside.
- In this less favorable scenario, the EUR/CHF exchange rate could rise as high as a CHF1.1200-1.1400 range over time.

Central Bank Outlook

SNB Policy Rate Forecast			
Current: -0.75%	**3M**	**6M**	**12M**
Wells Fargo	-0.75%	-0.75%	-0.75%
Market Implied	-0.74%	-0.66%	-0.56%

Source: Bloomberg LP and Wells Fargo Securities

- We expect the Swiss National Bank's policy interest rate to remain steady at -0.75% for all of 2021, 2022 and 2023.

Canada/CAD

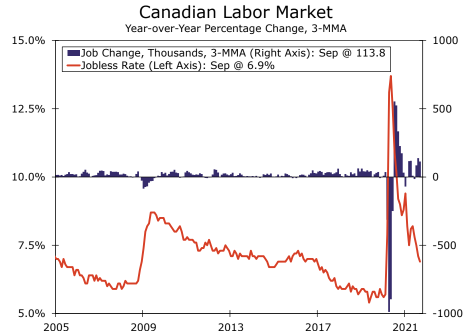
Outlook

The Canadian dollar may be somewhat restrained in the near term, but we believe the currency's prospects remain quite favorable over the medium term. The prospect of imminent Fed tapering and an ongoing global growth slowdown are factors that could weigh on the Canadian dollar for now. However, most local fundamentals remain favorable, including firming growth, elevated commodity prices, and a steady Bank of Canada shift toward less accommodative monetary policy. Over time, those factors should all be supportive of the Canadian dollar.

Fundamental Focus: Economics, Policy & FX

Canada's Economic Upswing Gathering Momentum

- After facing COVID-related challenges that held back the economy earlier this year, Canada's economic recovery is now gaining some perceptible momentum.
- July GDP dipped 0.1% month over month, a bit less than expected, as services activity rose 0.4% but industrial output fell 1.1%. More encouraging, Statistics Canada's early estimate is that August GDP rose 0.7% month over month.
- Recent activity data have generally been upbeat. In particular, September employment rose 157,100 and the jobless rate fell to 6.9%. The details were even more impressive, as full-time employment rose by 193,600. Elsewhere, August retail sales rose 2.0% month over month and manufacturing sales rose 0.5%. The September manufacturing PMI was upbeat, rising to 70.4.
- Alongside firming growth has been rising inflation. For September, the headline CPI rose 4.4% year over year, while the average of the core CPI measures quickened further to 2.7%. Growth and inflation trends should keep the Bank of Canada moving steadily along the path toward less accommodative monetary policy.



Source: Datastream and Wells Fargo Securities

Politics and Policy Relatively Benign

- The Bank of Canada makes its next monetary policy announcement later this week. We expect the central bank to hold its policy rate steady at 0.25%, but also slow the pace of its government bond purchases further to just C$1 billion per week. Alongside the announcement, the Bank of Canada will also release updated economic projections.
- Following the Liberal Party's general election victory, Prime Minister Trudeau kept Chrystia Freeland on as finance minister and deputy prime minister. Barring no major surprises with other cabinet appointments, that suggests a fair degree of policy continuity from the Canadian government.

Upside FX Scenario

- Our base case is for the Canadian dollar to gain over the medium term, though we also see a potential upside scenario where the Canadian dollar's gains are even larger than we anticipate.
- The economy appears to be returning to a stronger growth path. If that uptick is even more robust than expected and is accompanied by continued elevated commodity prices, that should offer direct support to the Canadian dollar.
- Inflation has for the most part surprised to the upside in recent months. Should that continue, it could hasten further Bank of Canada monetary tightening and boost the currency.
- Separately, a benign election outcome has removed a potential currency negative.
- In this more favorable scenario, the Canadian dollar could strengthen more than expected, with the USD/CAD exchange rate potentially moving to CAD1.1500 or below.

Central Bank Outlook

BoC Overnight Rate Forecast			
Current: 0.25%	**3M**	**6M**	**12M**
Wells Fargo	0.25%	0.25%	0.75%
Market Implied	0.31%	0.52%	1.12%

Source: Bloomberg LP and Wells Fargo Securities

- Quickening inflation means the Bank of Canada's shift to less accommodative monetary policy remains on track. We expect a further slowing in the weekly pace of bond purchases to just C$1 billion per week to be announced at the October monetary policy meeting and for the quantitative easing program to come to a close at the January announcement. We expect the Bank of Canada to deliver an initial rate hike in Q3-2022 and another rate increase in Q4-2022, followed by a further cumulative 75 bps of rate hikes in 2023. That said, we also see the risks tilted toward earlier rather than later for interest rate increases.

Australia/AUD

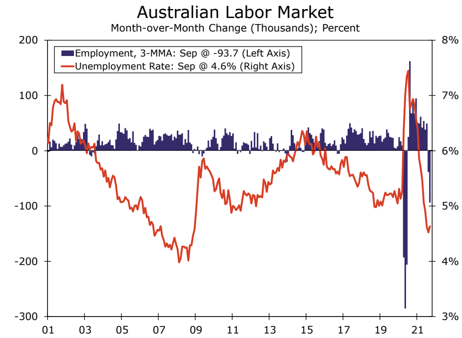
Outlook

We expect the Australian dollar to weaken over the next several months, and see only limited prospects for a recovery in the currency over the medium term. GDP likely contracted sharply in Q3, though as vaccination rates rise and the economy reopens, growth prospects for Q4 and for 2022 look better. Still, with inflation pressures muted, the Reserve Bank of Australia should hold policy rates steady for an extended period. A more uncertain outlook for China's economy is another potential negative for the Australian currency. Against this backdrop, we expect the Australian dollar to soften well into 2022, before stabilizing as the year progresses.

Fundamental Focus: Economics, Policy & FX

Australian Economy Passing the Worst

- The evidence of a sharp decline in activity for Australia during the third quarter continues to mount. September saw another large decline in employment, although the details of the report were not as discouraging as the headline figures. Employment fell 138,000, more than expected, while the jobless rate ticked up to 4.6%. That said, the employment decline was fully accounted for by a drop in part-time jobs, as full-time employment actually rose by 26,700.
- The ongoing slowdown is China's economy is also a potential negative for Australia's economy and currency, while we also note a decline in Australia's commodity prices in recent months, when measured in U.S. dollar terms.
- The more encouraging news regarding the outlook is that the economy is getting closer to a reopening phase. Sydney and Melbourne both exited strict lockdowns during October as vaccination rates increased, and the prime minister has signaled plans to accelerate opening international travel. Nationwide, 85% of the eligible population has had at least one dose, and 69% are fully vaccinated.
- As a result, a return to growth in Q4 and throughout 2022 is looking increasingly likely. This is starting to be reflected in confidence surveys. For September, business conditions fell to +5 but the forward-looking confidence measure rose to +13. For October, the manufacturing PMI rose to 57.3 and the services PMI rose to 52.0.
- Still, a return to growth would be in line with the Reserve Bank of Australia's outlook and is unlikely to prompt monetary policy action for some time. In early October, the central bank held monetary policy steady. While the central bank is likely to taper its assets purchases further during the early part of 2022, it repeated that its base case does not anticipate an increase in policy interest rates until 2024.



Source: Datastream and Wells Fargo Securities

Economic & FX Risks

Downside FX Scenario

- Our base case is for an underwhelming performance by the Australian dollar over the medium term. That said, we suspect the risks are still likely tilted toward a larger initial decline and perhaps a minimal medium-term rebound.
- The Australian economy is starting to reopen as vaccination rates increase. However, if the rebound in activity is slower than expected or there is an unexpected COVID setback, the Australian dollar could be subject to additional downside.
- Internationally, bond yields are rising as many central banks signal their intention to raise interest rates or otherwise move to less accommodative monetary policy. Given Australia's central bank is unlikely to raise rates for some time, that places some additional downside on the Australian currency.
- Should China's currency slow more sharply than we currently expect and this prompts commodity prices to weaken further, those factors would also likely be negative for the Australian dollar.

- In this less favorable scenario, the AUD/USD exchange rate could fall to $0.6800 or below, and may struggle to get back much above $0.7000 over the medium term.

Central Bank Outlook

RBA Cash Rate Forecast			
Current: 0.10%	**3M**	**6M**	**12M**
Wells Fargo	0.10%	0.10%	0.10%
Market Implied	0.11%	0.18%	0.53%

Source: Bloomberg LP and Wells Fargo Securities

- We expect the RBA to hold its Cash Rate steady at 0.10% over our entire forecast horizon—that is, the rest of 2021, and through all of 2022 and 2023.
- We expect Australia's economy to have returned to a steadier growth path by early 2022. As a result, we expect the next tapering of the RBA's bond purchases to occur in February, at which time we expect the weekly pace of bond purchases to slow to A$3B from the current A$4B. We expect that reduced pace of bond purchases to continue until at least May 2022, at which time the RBA would conduct a further review.

New Zealand/NZD

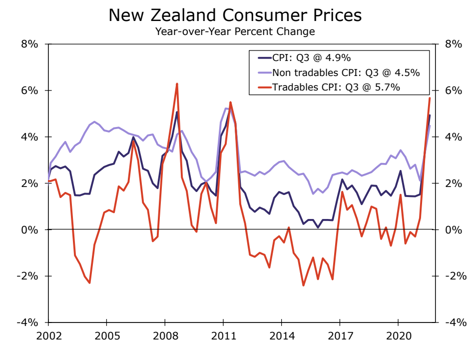
Outlook

We expect some further downside in the New Zealand dollar and see a modest recover in the currency over time. The economy likely shrank very sharply in Q3 amid a renewed COVID outbreak, and despite rising vaccination rates, there remains some uncertainty as to how quickly and how broadly the economy will reopen. As a result, the rebound in activity could be relatively gradual. For the time being at least, that could also mean a restrained NZ dollar, even as inflation increases and the Reserve Bank of New Zealand hikes rates. Once restrictions are eased, growth firms and rate hikes continue, we see potential for stronger NZ dollar gains.

Fundamental Focus: Economics, Policy & FX

Some Economic Light, but Still a Long Tunnel

- After a sharp downturn in activity as COVID restrictions went into place, there are now hints of stabilization in the economy, though it remains uncertain how rapid or strong any recovery will be.
- Retail card spending slumped 19.7% month over month in August, but edged up 0.9% in September. However, credit card spending fell 3.3% in September, following a 15.8% slump in August.
- Quarterly business confidence showed net 8% pessimism in Q3, compared to net 9% optimism in Q2. More recent confidence survey have shown signs of improvement however. October business confidence did fall to -8.6; however, firms' assessment of their own activity outlook improve to +26.2. Meanwhile, the September manufacturing PMI rose to 51.4 and the services PMI rose to 46.9.
- The key uncertainty remains how quickly restrictions will be lifted, particularly for Auckland, the country's largest city. Eighty-five percent of the eligible population have had at least one vaccine dose, while 67% are fully vaccinated. Still, the government has not yet outlined a precise path or timing on when restrictions could be eased further, which could limit the pace of economic rebound.
- Even with mixed activity trends, CPI inflation jumped sharply higher during Q3. Headline inflation quickened more than expected to 4.9% year over year, as the tradeables CPI rose 5.7% and the non-tradeables CPI rose 4.5%. Elevated inflation suggests further rate hikes will be forthcoming, even given lingering uncertainties.



Source: Datastream and Wells Fargo Securities

Reserve Bank of New Zealand Begins Rate Hike Cycle

- In early October, the Reserve Bank of New Zealand (RBNZ) became the second developed economy central bank to hike interest rates during the current cycle, raising its policy rate by 25 bps to 0.50%.
- The RBNZ said that COVID-19-related restrictions have not materially changed the medium-term inflation and employment outlook, and that capacity pressures remain evident in the economy. In addition, while the economy contracted sharply during the nationwide lockdown, the central bank said it expected activity to recover quickly as restrictions ease, and that recent economic indictors supported this picture.
- The RBNZ was somewhat balanced regarding the pace of future tightening, saying that "further removal of monetary policy stimulus is expected over time, with future moves contingent on the medium-term outlook for inflation and employment." That said, the central bank's assessment of the economic outlook was relatively constructive overall, and particularly in the context of the upside Q3 CPI surprise, we expect another 25-bp rate increase at the November monetary policy announcement.

Economic & FX Risks

Downside FX Scenario

- We expect a moderate gain in the NZ dollar over the medium term, though the risks are potentially tilted toward a slower pace of NZ dollar appreciation, or even renewed downside in the immediate period ahead.
- Given lingering uncertainties about the pace of reopening, a slower-than-expected rebound in the economy could place downward pressure on the NZ dollar.
- Market participants have priced in relatively aggressive rate hike expectations over the near term. To the extent the central bank fails to fully deliver on expectations, that could be a potential negative for the NZ dollar.
- Globally, bond yields have started to rise as many central banks contemplate monetary tightening. This rising yield environment could weigh on the NZ currency.
- In this less favorable scenario, the NZ dollar could fall towards $0.6500 in the coming weeks and months, and could struggle to gain much beyond current levels over the medium term.

Central Bank Outlook

RBNZ Official Cash Rate Forecast

Current: 0.50%	3M	6M	12M
Wells Fargo	0.75%	1.00%	1.50%
Market Implied	0.78%	1.28%	2.03%

Source: Bloomberg LP and Wells Fargo Securities

- Following an initial rate hike in October, we anticipate another 25-bp rate increase from the RBNZ in November.
- We expect a steady once-per-quarter pace of rate hikes during 2022, which would see the Official Cash Rate finish next year at 1.75%. That said, our projected pace of monetary tightening is somewhat slower than what is currently priced into interest rate markets.

Sweden/SEK

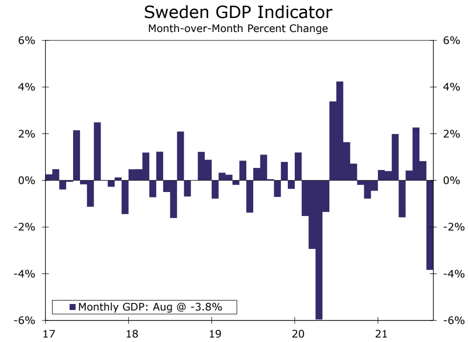
Outlook

We expect only modest gains in the Swedish krona versus the euro over the medium term. Sweden's economy experienced a pause during August, and while that slowdown will likely prove to be brief, it will likely reinforce the central bank's comfort with maintaining its accommodative monetary policy stance for an extended period. Given this backdrop, we expect the Swedish krona to be an underperformer among the G10. The krona could hold broadly steady or enjoy slight gains against a similarly subdued euro, but is likely to lag behind many other G10 currencies.

Fundamental Focus: Economics, Policy & FX

Swedish Recovery Hits an Economic Pothole

- Sweden's economy appeared to hit an air-pocket in August, with weakness across a wide variety of activity indicators.
- The August GDP indicator slumped 3.8% month over month, the largest monthly decline since April 2020 at the onset of the pandemic, with soft exports in particular contributing to the decline. The August GDP indicator was up a modest 2.4% compared to one year ago. Other indicators to display softness for August include household consumption (-1.1% month over month) and private sector production (-4.7% month over month).
- There was no obvious reason behind the August softness nor has there been any significant rebound in COVID cases. At this stage, we expect the weakness to be temporary. The September PMI surveys appear consistent with that narrative, as the manufacturing PMI rose to 64.6 and the services PMI rose to 69.6.
- Meanwhile, inflation trends remain reasonably contained. September CPIF inflation quickened to 2.8% year over year, while CPIF ex-energy inflation firmed slightly to just 1.5% year over year.
- Central bank policymakers clearly remain of the view that the current uptick of inflation will likely be temporary. Deputy Governor Floden said contagion effects on inflation from higher energy prices are not that likely. He described the market pricing of rate hikes as an overreaction, although separately, Deputy Governor Jansson said the market pricing in rate hikes was not a major problem.



Source: Statistics Sweden and Wells Fargo Securities

Central Bank Outlook

Riksbank Interest Rate Forecast			
Current: 0.00%	**3M**	**6M**	**12M**
Wells Fargo	0.00%	0.00%	0.00%
Market Implied	0.05%	0.17%	0.27%

Source: Bloomberg LP and Wells Fargo Securities

- Our outlook for Swedish monetary policy remains unchanged. We expect the Riksbank to hold its policy rate steady for an extended period and see the repo rate remaining steady at 0.00% through the rest of 2021, and for all of 2022 and 2023.

Norway/NOK

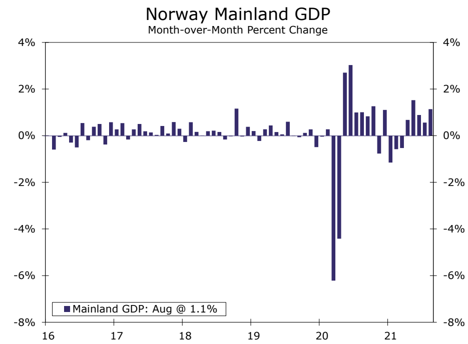
Outlook

We are constructive on the Norwegian krone's prospects over the medium term. Norway's economy continues to enjoy a solid economic rebound, while oil prices also remain elevated. As a result and even with underlying inflation trends subdued for now, we expect the Norges Bank to follow up its initial policy rate increase with another hike in December. A soft euro could be a restraining factor for Norway's currency in the near term; however over time, we expect Norway's growth and monetary policy trends to contribute to krone gains versus both the euro and U.S. dollar.

Fundamental Focus: Economics, Policy & FX

More of the Same from Norway's Economy

- The past month of data continues to suggest steady expansion for Norway's economy.
- August mainland GDP rose 1.1% month over month, more than expected and the fifth increase in a row. Mainland GDP was 5.0% higher compared to August last year. August industrial output also rose by 2.7% month over month.
- The September manufacturing PMI fell to 59.2, still a level consistent with a sturdy pace of growth going forward.
- There was a stark divergence within the details of the September CPI report. Headline inflation quickened more than expected to 4.1% year over year. Underlying inflation also quickened, but remains much more contained for now at just 1.2% year over year.
- That divergence was noted by Central Bank Governor Olsen, who said the current high level of inflation is most likely transitory, perhaps a somewhat "dovish' monetary policy comment. However, on the "hawkish" side, referring to the krone and even after sizable gains recently, Olsen said the krone is not at a very strong level just now.
- Overall, considering economic trends and recent central bank commentary, we believe the Norges Bank is clearly on track to raise its policy interest rate a further 25 bps to 0.50% at its December monetary policy announcement.



Source: Bloomberg LP and Wells Fargo Securities

Central Bank Outlook

Norges Bank Deposit Rate Forecast			
Current: 0.25%	**3M**	**6M**	**12M**
Wells Fargo	0.50%	0.75%	1.25%
Market Implied	0.53%	0.72%	1.14%

Source: Bloomberg LP and Wells Fargo Securities

- We expect the Norges Bank raise its policy rate by 25 bps to 0.50% in December, following the initial rate hike it delivered in September. We also expect a further cumulative 100 bps of rate increases during 2022.

Mexico/MXN

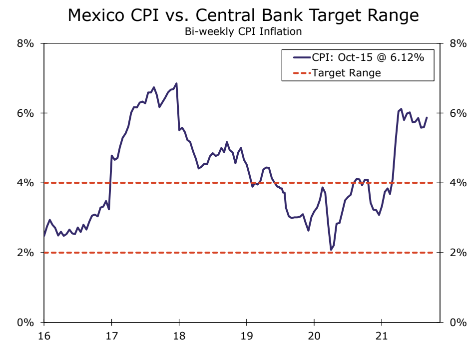
Outlook

The peso has rallied over the past few weeks; however, we believe the short-term outlook for the currency will be challenging and forecast a weaker peso through the end of this year. A more pronounced global economic deceleration and a Fed taper should result in broad U.S. dollar strength over the next few months. Despite our view for more aggressive Banxico tightening, we believe these external dynamics could have more influence over the path of the peso and place depreciation pressure on the currency through Q4-2021. Over the longer term, a broadly weaker U.S. dollar and attractive carry associated with the peso should result in a stronger Mexican peso over 2022.

Fundamental Focus: Economics, Policy & FX

External Factors Still Peso Negative

- Our view is that the global economy is still softening and will continue to exhibit signs of deceleration. In our view, a slowdown in global economic growth should place depreciation pressure on foreign currencies, especially emerging market currencies including the Mexican peso.
- In addition to global growth concerns, we believe the Fed is getting closer to officially announcing a decision to taper asset purchases. With global growth and the U.S. economy slowing, we believe markets will be sensitive to tighter Fed monetary policy. In that context, should the Fed move forward with a taper before the end of this year, the Mexican peso should come under pressure.
- Against this backdrop, the peso should reverse course and begin to weaken again against the U.S. dollar. By the end of Q4-2021, we forecast the USD/MXN exchange rate to trend higher toward MXN20.50.



Source: Bloomberg LP and Wells Fargo Securities

Rate Hikes Help, but Not Enough to Stem Depreciation

- In our view, the Central Bank of Mexico is likely to tighten monetary policy more aggressively as inflation concerns continue to rise. We now expect Banxico to lift interest rates 50 bps at its meeting in November and raise the Overnight Rate another 25 bps in December. Our new central bank forecast suggests policy rates in Mexico will reach 5.50% by the end of this year.
- As far as inflation, the biweekly CPI recently climbed more than expected to 6.12% year over year in mid-October. Inflation is currently well above the central bank's target range and is proving to be stickier than policymakers originally thought. To that point, inflation concerns have been at the core of Banxico's decision to lift interest rates multiple times over the past few months.
- Banxico took a more hawkish stance on monetary policy at its latest meeting, which also supports our view for a 50-bp rate hike in November. In September, policymakers voted 4-1 to raise the Overnight Rate. Previously, the rate setting committee voted 3-2 in favor of tighter monetary policy.
- Despite our view for faster rate hikes in Mexico, we think financial markets are priced too aggressively. Right now, Markets are priced for 100 bps of tightening over the next three months. As financial markets adjust to our view of just 75 bps of tightening in the next three months, the peso should also experience downside.

Economic & FX Risks

Downside FX Scenario

- Risks around our peso forecasts are tilted to the downside, as emerging market currencies could come under more pressure than we expect over the next few months. Should the Fed pursue a more aggressive taper schedule and reduce asset purchases at a quicker pace than we currently expect, emerging market currencies could come under significant pressure. Our analysis suggests the Mexican peso could be particularly vulnerable in this scenario.

- Financial markets are also priced for aggressive monetary tightening from Banxico, which could lead to a more pronounced peso sell-off. Should policymakers not match markets expectations and not turn as hawkish as we expect, the peso could come under pressure.
- In a "taper tantrum" and less hawkish Banxico scenario, USD/MXN could test all-time highs of MXN25.78.

Upside FX Scenario

- An upside scenario is also centered on Fed monetary policy. We forecast peso strength over the medium to longer term; however, the peso could reach our targets quicker if the Fed takes a more measured approach to monetary policy. Should the Fed's taper be slower than markets expect, the peso could rally sharply.
- A less hawkish Fed could result in the peso reaching MXN19.00 by the second half of 2022.

Central Bank Outlook

Banxico Overnight Rate Forecast			
Current: 4.75%	**3M**	**6M**	**12M**
Wells Fargo	5.50%	6.00%	6.50%
Market Implied	5.77%	6.36%	7.19%

Source: Bloomberg LP and Wells Fargo Securities

China/CNY & CNH

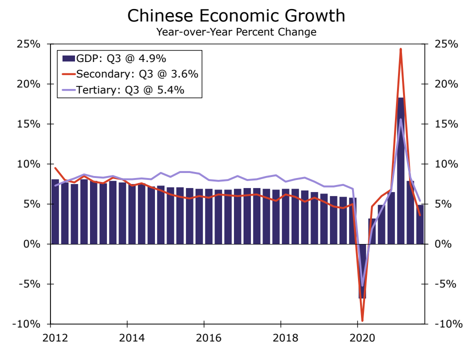
Outlook

Q3 GDP data indicated the Chinese economy decelerated sharply to start the second half of the year. Including Q3 data, as well as our view for that slowdown to persist into Q4-2021, we have revised our annual GDP forecast lower again. Given the slowdown in the economy, we expect the central bank to accommodate a weaker currency over the next few months. Longer term, we expect China's financial markets to open to foreign investors and become more accessible. As local markets open up, capital should flow toward renminbi denominated assets and support the currency.

Fundamental Focus: Economics, Policy & FX

Economic Disruption Finally Revealed

- The past few months have been difficult for the Chinese economy. COVID restrictions, property sector concerns and regulatory changes have all contributed to a slowdown in China's economy. Just recently, the full extent of the deceleration was revealed, as China's economy grew just 0.2% quarter over quarter and less than 5% on a year-over-year basis. To put these data into perspective, China's economy grew 1.2% quarter over quarter in Q2, and pre-COVID, was growing around 1.5% on a sequential basis.
- Relative to our forecasts, China's economy decelerated more than we expected. Given the underwhelming GDP data, we have once again revised our GDP forecast lower and now expect the Chinese economy to grow 8% in 2021. Given the myriad of risks facing the economy, we continue to believe risks around our revised GDP forecast are tilted toward even slower growth.
- China's energy rationing remains a key downside risk to our GDP forecast. Given a global energy shortage, China has opted to conserve energy and limit manufacturing output. Recent data also revealed the impact of energy rationing, as industrial production softened to 3.1% year over year in September. As of now, energy shortages do not seem to be going away, and softer manufacturing output could lead to a further slowdown in the broader economy.



Source: Bloomberg LP and Wells Fargo Securities

Evergrande Backs Away from the Cliff...for Now

- China's real estate and property sector has also come under pressure amid President Xi's push for common prosperity. Evergrande, in particular, has come under enormous pressure; however, the immediate default risk has subsided as the company recently made a grace period payment on dollar-denominated bonds.
- While the immediate default risk has been lifted, the longer-term probability of an Evergrande default remains elevated. The company still has large debt payments to make in 2021 and close to $7 billion of bond payments to make next year. In our view, unless Evergrande is able to divest assets or some type of bailout from the Chinese government is negotiated, default risks associated with Evergrande will remain a concern.
- As of now, we are not making any explicit assumptions regarding Evergrande; however, we do not expect a collapse of China's real estate sector or broader corporate sector turmoil. We also do not believe any corporate debt sector blowup would lead to China having its own "Lehman Moment."
- We do, however, expect Chinese authorities to accommodate a weaker currency to offset some of the economic slowdown. PBoC daily fixing has been slightly weaker than consensus expectations, and in our view, these actions are likely to continue over the course of the next few months and lead to a weaker renminbi through the rest of 2021.

Economic & FX Risks

Downside FX Scenario

- Risks around our renminbi forecasts are tilted toward a weaker currency than we forecast. It is possible that, in the short term, the PBoC seeks to intervene and artificially weaken the currency rather significantly should the economy come under pressure amid the slowdown in the real estate sector and energy rationing. FX intervention would see the currency weaken, although we do not expect a full-blown devaluation.

- While not our base case scenario, an Evergrande default or bankruptcy could result in widespread contagion across China's economy. A sustained and prolonged China deceleration could see market participants pull capital out of China and renminbi denominated assets.
- In the event this combination materializes, the PBoC could allow the renminbi to depreciate significantly and capital flows could exit China. This combination could result in significant renminbi weakness, in which USD/CNY and USD/CNH could test CNY/CNH7.00.

Upside FX Scenario

- Our upside scenario is centered around Evergrande. Should the Chinese government bail out the company or the company avoids a disorderly default, sentiment toward China could turn quite positive. Concerns regarding contagion would be alleviated, and we would expect local and global financial markets to rally.
- Also, should the economy experience a sharp rebound in Q4 and the PBoC allows the currency to more freely float in order to attract more foreign capital into the country, the renminbi could also strengthen considerably.
- In this scenario, USD/CNY and USD/CNH could reach CNY/CNH6.20, a level not seen since 2018.

Brazil/BRL

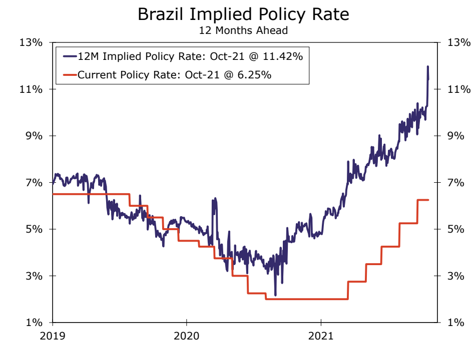
Outlook

Our prior concerns regarding the Brazilian real are beginning to materialize, and the impact on the currency has been more significant than we expected to this point. President Bolsonaro has stepped up efforts to increase social spending ahead of the election, and the currency has come under significant pressure. In our view, Auxilio Brasil is likely to be approved, which could put Brazil's spending cap in jeopardy. Going forward, we continue to expect election-related risks as well as fiscal slippage concerns to weigh on the currency and forecast a weaker Brazilian real over the entire forecast horizon.

Fundamental Focus: Economics, Policy & FX

Fiscal Risks Are REAL

- The Brazilian real has come under pressure over the past few weeks as President Bolsonaro negotiates his new social spending plan, Auxilio Brasil. As of now, Bolsonaro is seeking to extend fiscal support to households via an extra 400 to 500 reais per month (~US$75). Concerns are building around the proposal, as Brazil's fiscal balance would be pushed more into deficit and Brazil's constitutional spending cap may also in jeopardy.
- Bolsonaro's cabinet members have pushed back against extending social aid. Four members of the economic advisory team recently resigned amid opposition to additional social spending; however, Paulo Guedes, a key figure of economic policy, has reiterated his commitment to the current administration despite his view for fiscal responsibility. While Guedes has suggested he will not resign, we expect tensions between Guedes and Bolsonaro to persist and be a source of stress on the currency going forward.
- Brazil's fiscal and debt trajectory appear unsustainable, and should Bolsonaro's proposal be approved, the government's public finances would be in more precarious shape. In our view, Auxilio Brasil is likely to be approved in the near future and push the fiscal balance further into deficit and increase the debt burden, which should contribute to a weaker currency. Should the spending cap be breached, which as of now is unclear while the proposal is still being debated, we would expect the currency to come under even more pressure.



Source: Bloomberg LP and Wells Fargo Securities

Rate Hikes Not Supporting the Currency

- Renewed fiscal concerns have also contributed to financial markets pricing more aggressive tightening from the Brazilian Central Bank purely in an effort to defend the value of the currency. Just over the past few weeks, markets have repriced sharply for more pronounced tightening at the BCB's October meeting as well as at later meetings.
- Given the volatility within local Brazilian financial markets recently, we have adjusted our policy rate forecast and now expect the BCB to raise the Selic Rate 150 bps to 7.75% at the October meeting. Forward guidance at the BCB's September meeting suggested only 100 bps of tightening in October; however, we believe policymakers will feel the need to protect the currency as well as contain inflation. In December, we expect the BCB to lift interest rates another 100 bps and take the Selic rate to 8.50% by the end of 2021.
- We expect policy rates to move higher in 2022 as well; however, given the political and fiscal risks permeating across the country that are unlikely to recede anytime soon, we doubt rate hikes will be sufficient to support the currency. Only if dynamics around the election and fiscal spending dramatically change in the coming quarters do we believe rate hikes could be a source of support for the currency.

Economic & FX Risks

Downside FX Scenario

- Risks around our Brazilian real forecast are toward more depreciation than we currently expect. Monetary policy dynamics are somewhat encouraging; however, as mentioned we doubt tighter monetary policy will be enough to offset political and fiscal risks. Should Brazil's spending cap indeed be breached, the currency would likely face significant depreciation pressure, and our targets for the USD/BRL exchange rate would be reached earlier than we anticipate.

- Brazil's economy is also sensitive to a material economic slowdown in China. Should China's economy decelerate significantly or if a corporate debt crisis emerges, Brazil's financial markets could come under pressure.
- In a scenario where Brazil's spending cap is breached, the USD/BRL exchange rate would likely reach record levels, with the real possibly weakening to BRL7.00 per dollar.

Upside FX Scenario

- A scenario for a stronger Brazilian real includes a solid commitment to the constitutional spending cap, fiscal responsibility and to the longer-term reform agenda. Despite falling approval ratings, Bolsonaro would need to push back against additional fiscal stimulus for the currency to rally materially.
- Spending restraints could lead to both capital flows returning to Brazil and a faster economic rebound. The BCB could tighten monetary policy perhaps even faster than markets expect and create positive real interest rate dynamics again in Brazil.
- Bolsonaro retaining office could also result in a longer-term relief rally for the currency, especially if markets do not question the spending cap or Brazil's fiscal and debt positions.
- In this scenario, USD/BRL could move below BRL5.00 and would likely sustain those gains.

Central Bank Outlook

BCB Selic Rate Forecast			
Current: 6.25%	**3M**	**6M**	**12M**
Wells Fargo	8.75%	9.75%	10.75%
Market Implied	10.25%	11.58%	11.97%

Source: Bloomberg LP and Wells Fargo Securities

- Our view on Brazilian policy rates has been adjusted given local financial market volatility. We now expect a 150-bp rate hike in October and another 100-bp rate increase in December. By the end of this year, we expect the Selic rate to be raised to 8.75%. Over the course of 2022, we expect the BCB to maintain its hawkish policy stance as the currency weakens and as inflation remains above the central bank's target.
- In our view, financial markets are still priced for too much tightening in Brazil. Directionally, we agree on the path ahead for the Selic rate; however, we expect less tightening than financial markets are implying.

Asia

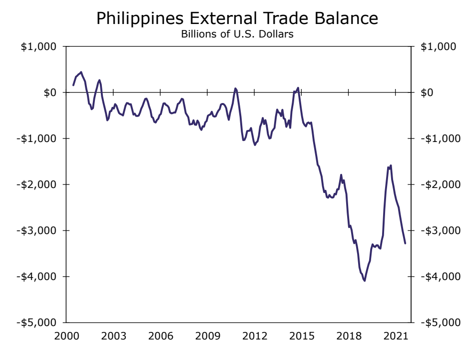
Indonesia/IDR

Outlook: In our view, Indonesia is one of the more vulnerable emerging market economies to rising U.S. yields and tighter Fed monetary policy, and given our view for an imminent Fed taper, we believe the rupiah can come under short-term pressure. The government is heavily reliant on foreign investors purchasing local debt, which is a vulnerability, in our view. Should the Fed indeed taper asset purchases before the end of this year, we expect foreign investors to move capital toward U.S. assets and away from many emerging markets. This shift in asset allocation could place particular pressure on the rupiah over the next few months. In addition, our concerns regarding the health of the global economy could result in safe-haven flows toward the U.S. dollar and also contribute to a weaker rupiah through the end of this year. As far as the local economy, COVID cases have come down significantly and local authorities have reopened international travel. Tourism is a key source of revenue and reopening borders should improve the overall health of the economy. Tourism revenues may take time to accumulate, so we would expect the benefits of increased travel to be more of a medium-term development. Bank Indonesia also seems content with keeping interest rates on hold for the time being; however, as the economy improves, we would expect inflation pressures to build and for the central bank to tighten monetary policy. These dynamics can support the rupiah over the course of 2022, while broad dollar weakness can help the currency strengthen over the longer term.

Source: IIF and Wells Fargo Securities

Philippines/PHP

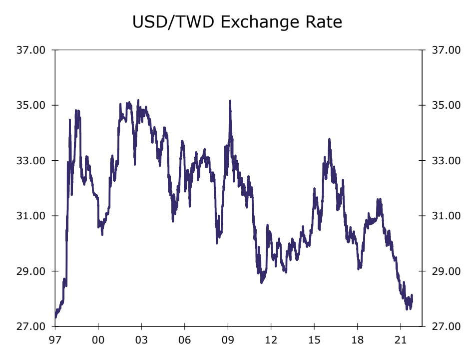
Outlook: Our forecast profile for the Philippine peso is unchanged as we continue to forecast modest short-term weakness in the currency and gradual strength over the longer term. Our short-term forecast is based around our core view of broad U.S. dollar strength against G10 as well as emerging market currencies for the time being. Safe-haven capital flows to the U.S. dollar as well as an imminent Fed tapering should put modest depreciation pressure on the Philippine peso. We also note the Philippine economy has been slow to recover amid the spread of the Delta variant as well as higher oil prices. Elevated oil prices pushed the Philippine trade balance further into deficit in August and a weaker current account position has weighed on the peso recently. For the time being, we expect current account dynamics to contribute to a weaker peso at least through the end of this year. Over the medium to longer term, we expect the global economy to stabilize and for sentiment toward emerging market currencies to improve. In addition, we expect foreign central banks to tighten monetary policy at a quicker pace than the Fed, which should also lead to a broadly weaker U.S. dollar. Against this backdrop, the Philippine peso should strengthen; however, we believe that strength will be gradual. Next year, the Philippines will host presidential elections as well. As of now, we do not expect a build up of political risk tied to the election; however, we will be monitoring closely for candidates with potentially unorthodox policy agendas.



Source: Bloomberg LP and Wells Fargo Securities

Taiwan/TWD

Outlook: We maintain our view that the Taiwan dollar will remain steady in the short term and continue to forecast gradual strength in the currency over the medium to longer term. Taiwan maintains some of the strongest underlying economic fundamentals not only in emerging Asia but across the entire emerging markets complex. The country has a current account surplus, solid growth and inflation dynamics as well as low levels of debt. In this context, the Taiwan dollar has become one of the main "safe-haven" currencies within the emerging markets and has attracted capital flows over the course of the pandemic. Geopolitical risks continue to build with China; however, for the time being, we do not expect a material or significant escalation to the point where the local currency comes under pressure. Should geopolitical tensions escalate more than we expect, the currency could experience downside risks, and we would make adjustments to our USD/TWD exchange rate forecast. Aside from geopolitical risks, the central bank could opt to intervene in FX markets in favor of a weaker currency. In our view, FX intervention is more of a tail risk, as the U.S. Treasury recently named Taiwan a potential currency manipulator. In an effort to protect against being labeled a currency manipulator, we believe authorities will allow the currency to more freely float, which should result in upside for the currency.

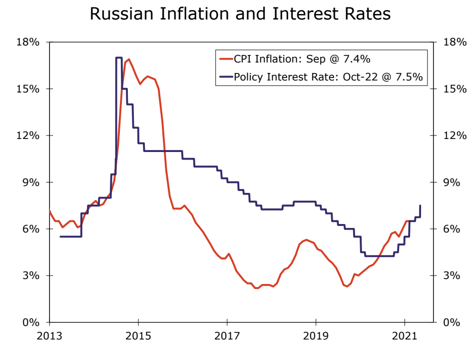


Source: Bloomberg LP and Wells Fargo Securities

Emerging Europe, Middle East & Africa

Russia/RUB

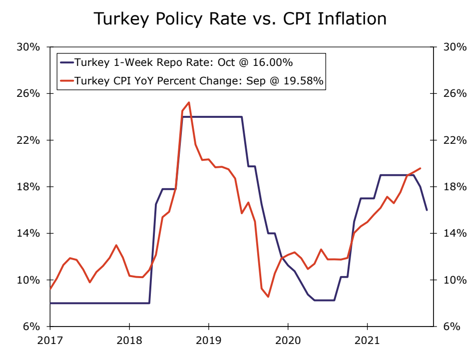
Outlook: The ruble has experienced a sizable rally over the past month as oil prices push higher and as the Central Bank of Russia surprised markets with more hawkish monetary policy action. Given the more hawkish stance on monetary policy and elevated energy prices, we have made modest adjustments to our short-term outlook for the ruble and expect the currency to hover around current levels through the end of this year. As far as monetary policy, the central bank recently raised interest rates more than markets expected, hiking its Key Rate 75 bps to 7.50%. Financial markets were priced for a 50-bp rate hike and also expected forward guidance to suggest the tightening cycle would end in October. However, Governor Nabiullina suggested another interest rate hike would be likely at its next monetary policy meeting in an effort to contain inflation. As of September, Russian inflation hit 7.4% year over year, well above the central bank's target range, and has also proven to be less transient than initially expected. In our view, inflation is likely to trend higher in the short term, which could mean a 50-bp rate hike from the central bank in the near future. In the short term, positive real interest rates should be a key source of stability. Over the longer term, we maintain our view for a stronger ruble. For the time being, geopolitical tensions with the United States have calmed significantly and the risk of meaningful sanctions against Russia is currently low. In addition, Russian economic fundamentals are relatively strong and should contribute to a stronger currency over time, especially as the global economy stabilizes over the course of 2022.



Source: Bloomberg LP and Wells Fargo Securities

Turkey/TRY

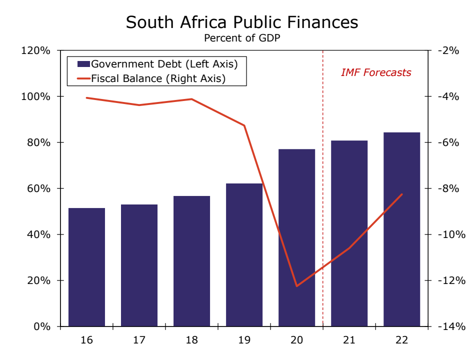
Outlook: Over the past few months, we highlighted the possibility of another large Turkish lira depreciation. We felt President Erdogan's intervention in monetary policy would eventually lead to another purge of central bank policymakers as well as a large reduction in Turkey's one-week repurchase rate. Just recently, Erdogan did indeed replace central bankers not aligned with his view for easier monetary policy and used his influence over policymakers to force another interest rate cut. To that point, policy rates in Turkey were reduced 200 bps to 16%, a more aggressive cut than markets were expecting. As a result, the lira sold off sharply and hit a new record low against the U.S. dollar. In our view, Erdogan's influence over monetary policy is unlikely to abate for the time being, and we continue to forecast the currency to depreciate against the greenback over the entire course of our forecast horizon. Aside from local factors, we continue to believe the short-term outlook for most emerging market currencies could be challenging amid persistent dollar strength. Turkey's underlying economic fundamentals remain especially weak, which in our view, leaves the lira particularly vulnerable to more pronounced weakness. The combination of a lack of central bank independence and fragile fundamentals should result in a lira that depreciates to record lows over the course of 2022.



Source: Bloomberg LP and Wells Fargo Securities

South Africa/ZAR

Outlook: Our outlook for the South African rand is little changed, and we continue to forecast a weaker currency over the entire course of our forecast horizon. The rand's resiliency continues to surprise, especially given the myriad of risks building within the global economy as well as the fragile state of the South African economy. South Africa's economy is still struggling to gather momentum and economic fundamentals remain relatively weak. In our view, a struggling economy and modest local inflation pressure should keep the South African Reserve Bank (SARB) on hold for the time being and keep interest rates steady through at least the end of this year. As of now, financial markets are priced for almost 50 bps of interest rate hikes over the next three months, which we believe is too aggressive. A repricing of interest rate expectations should contribute to a weaker currency in the short term. Over the longer term, we believe the government's lack of a concise plan to stabilize public finances should also contribute to a weaker currency. According to the IMF, South Africa's debt burden should continue to rise through 2022, and over time, we believe financial market participants will eventually place more focus on deteriorating public finances. As markets focus on a rising debt burden and the still-significant fiscal deficit, we believe the rand could face more serious depreciation pressure.

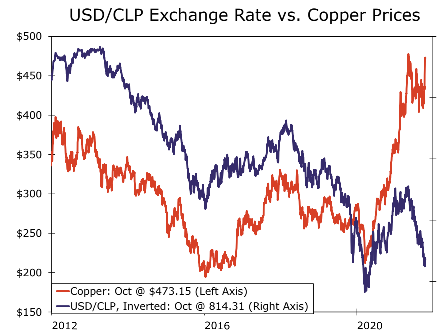


Source: IMF and Wells Fargo Securities

Latin America

Chile/CLP

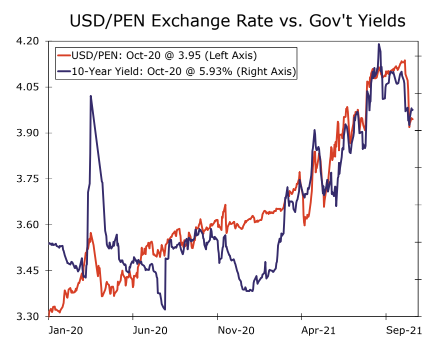
Outlook: Chile is one of the top performing emerging market economies this year; however, we remain concerned regarding the direction of local politics and continue to forecast a weaker currency over the course of our forecast horizon. The Chilean economy has recovered from the COVID-induced slowdown extremely well, as aggressive fiscal stimulus, early access to pension funds and one of the highest vaccination rates in the world has sparked record levels of economic activity. Strong economic activity, along with elevated commodity prices, has pushed inflation well above the central bank's target and has prompted aggressive monetary tightening over the past two months. Despite sharp interest rate hikes, we believe the combination of the upcoming presidential election and constitutional rewrite process will place depreciation pressure on the Chilean peso through the end of 2022. To that point, Chile will host its presidential election on Nov. 21, and as of now, the left-leaning Gabriel Boric is leading opinion polls. Latest polling suggests Boric could win around 30% of votes in the first round of the election, well short of the required threshold to outright win the presidency. However, should Boric receive a significant amount of votes and advance to the runoff round, we believe local financial markets could come under pressure, given Boric's proposed policies designed to upend Chile's economic model. The likelihood of Boric advancing to the second round of the election underpins our view for a weaker Chilean peso through the end of this year. Longer term, we remain concerned the constitutional rewriting process will turn contentious and will also result in drastic changes to Chile's economy. A left-leaning constitutional convention could draft proposals around more fiscal spending and allow for an elevated debt burden as well as make Chile a less desirable investment destination. In our view, risks around Chile's new constitution should keep downward pressure on the Chilean peso for the foreseeable future. Elevated political risk should continue to disrupt the historically tight correlation between copper prices and the currency.



Source: Bloomberg LP and Wells Fargo Securities

Peru/PEN

Outlook: Local politics continue to be the driving force of the Peruvian currency, and despite recent positive news on the political front, we are hesitant to make significant adjustments to our sol forecasts. President Castillo continues to keep local Peruvian financial markets on edge as his platform calling for marked changes to Peru's economy has injected volatility into Peruvian asset prices. However, just recently, Castillo's Prime Minister Guido Bellido, largely viewed as an unorthodox and radical policymaker, resigned from office. Bellido's resignation was received well by financial markets as the risk of dramatic changes to Peruvian policy is now somewhat reduced. Castillo also replaced Bellido with a more conservative and respected prime minister in Mirtha Vasquez, who has a track record of proposing and voting for policies to maintain Peru's current economic model. As a result, the currency and bond yields have rallied. Sovereign yields have come down almost 100 bps, while the sol has strengthened over 4.5% in just a few weeks' time. These recent developments are all positive; however, we remain cautious on the outlook for the Peruvian currency. We are not yet convinced that Castillo will take a turn toward more orthodox policymaking and completely abandon his platform for transforming Peru's economy. In our view, Castillo is likely to continue with rhetoric and political posturing aimed at fulfilling his political ideologies, even if the likelihood of his agenda being implemented is low. This rhetoric should place the currency back on a weakening trend and eventually result in the USD/PEN exchange rate climbing back above the key PEN4.00 level. In addition, Peru's sovereign credit rating has been downgraded multiple times, and political risk continues to build as the government's public finance position steadily deteriorates. Additional rating downgrades are possible in the near future, which could also contribute to a weaker sol over the medium term.



Source: Bloomberg LP and Wells Fargo Securities

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