Maybank

Macro | FX Research & Strategy

Global

FX Monthly

2022, Issue 3: Pricing in Risk Premium

What Has Changed This Month?

- We revised EUR, GBP, NZD, JPY, KRW, CNY, TWD, MYR, INR, IDR, THB as ongoing war in Ukraine persists for longer and to account for Fed's recent hawkish shift.

Our Strategies

- The emergence of new risk drivers expose USD risks to the upside in coming months. Some of these risk drivers include (1) increasing downside risks to growth, especially with the war in Ukraine persisting; (2) continuing supply chain pressures; (3) elevated energy prices, inflationary pressures globally; (4) Importantly, Fed turning more hawkish in recent weeks is a significant risk to consider. **But our over-arching view continues to call for USD nearing its peak, underpinned by: (a) hawkish Fed expectations somewhat in the price and that USD's sensitivity to yield moves tend to weaken during current episode of yield curve flattening; (b) Fed is not the only one tightening; (c) global economic backdrop to remain somewhat supportive (no recession or stagflation) to support synchronous policy normalisation; (d) ongoing talks between Russia-Ukraine in hope of reaching a comprehensive deal (that may take weeks to month to forge). Any worsening to (c) and (d) will extend the USD support.**

- RBA and BoC will have their policy meetings in Apr. Given the war-triggered rally in the commodity complex that has underpinned the AUD surge thus far, we see room for retracement especially if RBA Lowe continues to disappoint on the extent of his hawkish pivot. On the other hand, Canada's tight labour market and rising inflation could spur BoC to normalize monetary policy more aggressively. Divergence of policy stance between the two central banks should bring the AUDCAD lower. We prefer to tactically short this cross on rallies.

- Asian March PMI Mfg largely remained in expansionary territory—Indonesia at 51.3 (vs. 51.2 prior), Thailand at 51.8 (vs. 52.5 prior), Philippines at 53.2 (vs. 52.8 prior), South Korea at 51.2 (vs. 53.8)—with the exception of Malaysia (49.6 vs. 50.9 prior), which is mildly in contractionary territory. Broadly, readings continue to suggest some resilience in regional economic activity to ongoing war and supply disruptions, secondary demand drags. Despite the aggressive hawkish shift in Fed signalling via dots plot and Fedspeaks, and concomitant surge in UST yields, AxJ FX have weathered the Fed normalization messaging relatively well and most AxJ FX have not seen significant drags post-FoMC. Expectations of further MAS tightening in Apr could be supportive of SGD, especially if a re-centering (upwards) in policy band materializes.

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Top 3 Currency Plays for Apr

Sell DXY on Rallies
Tactical Sell AUDCAD
Long SGD NEER

Key Events for the Month Ahead

Date	Event
1 Apr	EU-China Summit
7 Apr	Canada Federal Budget
10 Apr	French Presidential Elections
24 Apr	French Presiidential Elections - Run-off

G7 Global Overview

USD: Dollar Still Supported For Now

Forecast	2Q 2022	3Q 2022	4Q 2022	1Q 2023
USD Index	**97.56** (95.12)	**97.09** (93.93)	**95.46** (92.71)	**95.11** (--)

Previous Forecasts in Parentheses

- **Motivation:** USD is likely to remain supported on the back of the current geopolitical situation and with the expectations of tighter Fed policy move. Fears of a much faster Fed, strong US data and geopolitical concerns could see USD supported but we are of the view that USD may see some risk of peaking as (1) most of the hawkish expectations are in the price; (2) on a relative basis with other central banks, albeit with a lags, the Fed is not the only one tightening; but despite synchronous policy normalisation in the face of inflationary pressures, there could still be the risk of a risk based cautious view on the global economic backdrop. An improvement in the geopolitical space coupled with reopening globally allows for some space for cyclical FX to intermittently strengthen.

- With the emergence of new risk drivers, USD risks could be skewed to the upside in coming months. Some of these risk drivers include (1) increasing downside risks to growth, especially with the war in Ukraine persisting; (2) continuing supply chain pressures; (3) elevated energy prices, inflationary pressures globally; (4) Fed turning more hawkish. Though hawkish Fed expectations may already be in the price, we are cautious of Fed turning even more restrictive.

- As of 31 Mar, 30d Fed fund futures are pricing in about 8 hikes for 2022 (vs. 7 hikes in 2022 as per Fed's dots plot in Mar-2021). But while higher US rate expectations typically add to USD upward pressure, we think it may be useful to consider how USD sensitivity to rate moves can vary in different yield curve regimes (i.e., steepen vs flattening period).

- If we look at past 32 years of daily data since 1990 on DXY sensitivity (90d rolling basis) to 2y and 10y UST yields against different regimes of 2y10y yield curve episodes. Historically, USD sensitivity to yields picks up when 2y10y yield curvesteepens – a proxy for brighter economic prospects. However, the relationship starts to weaken in episodes of yield curve flattening. This may suggest that markets are cautious that aggressive Fed tightening may hurt US economic growth and thus dent its appeal of its rate advantage. The current yield curve regime is one where 2y10y is flattening (last at+20bps vs +89bps peak of the year in early-Jan 2022). So technically, USD's sensitivity to yield uptick should be weaker as compared to periods when the yield curve is steepening.

- USD strength will however be uneven. Amongst the DM majors, negative/low yielders such as EUR and JPY are vulnerable to the downside but commodity-linked FX such as AUD, CAD and NZD could still gain the upper hand vs USD due to soaring commodity prices and respective central bank biases.
- Amongst ASEAN FX, Fed's hawkish monetary policy divergence may marginalize some ASEAN FX, including MYR whose monetary policy maybe perceived to be relatively accommodative. On the other hand, SGD could find solace from a hawkish MAS.
- To sum up, near-term (coming 2-3months) risks could be skewed to the upside for broad US, and our forecasts for currencies like EUR, JPY, INR and MYR and others are revised lower.
- But to some extent, our over-arching view for now continues to call for USD nearing its peak, barring no further escalation in geo-political tension and no further surprises in Fed tightening already made so far, underpinned by: (1) hawkish Fed expectations somewhat in the price and that USD's sensitivity to yield moves tend to weaken during current episode of yield curve flattening; (2) Fed is not the only one tightening; (3) global economic backdrop to remain somewhat supportive (no recession or stagflation) to support synchronous policy normalisation; (4) ongoing talks between Russia-Ukraine in hope of reaching a comprehensive deal (that may take weeks to month to forge).
- The 100-handle could remain a strong resistance for the DXY. Despite the aggressive hawkish shift in Fed signalling via dots plot and Fedspeaks, and concomitant surge in UST yields, AxJ FX have weathered the Fed normalization messaging relatively well and most AxJ FX have not seen significant drags post-FoMC.
- **Growth and Inflation Outlook:** Real GDP growth was revised down to 6.9% in the third estimate of Q4 (from 7%) on the back of softness to consumption growth but partially offset by a faster pace of inventory investment. YoY core PCE inflation was revised up to 4.59%. ADP Private sector employment increased by 455k in March, in line with consensus expectations for a 450k gain.
- Feb core CPI rose 0.51% (m/m sa), in line with consensus of 0.5%. The YoY rate rose to 6.4% (from 6.0%), the fastest pace since 1982, on the back of further acceleration in shelter, travel categories and Covid wave subsided but was mitigated by sequentially slower gains in labor-sensitive services. Headline CPI rose to 0.8% from 0.6% consensus, led by higher energy prices.
- NFP rose 678k in Feb and was revised 92k higher in prior months — well above consensus expectations, indicating a strong pace of job growth in part driven by the return of Omicron-related absences. The unemployment rate fell to 3.8% from 4.0%, as strong household employment growth was partially offset by a one-tenth rise in labor force participation.
- **Monetary Policy Forecast:** At the last FoMC (16-17Mar), FoMC voted 8-1 to raise rate to 0.25% - 0.5%. Bullard was the only dissenter as he called for 50bps hike. Dots plot signalled another 6 more hikes this year

(vs. their Dec-2021 FoMC projection for 3 hikes). For 2023, Fed is now looking for about 3 – 4 more hikes and none for 2024.

- 15-16 Mar 2022 FOMC meet saw the target fed funds rate (FFR) raised by +25bps to 0.25%-0.50%. FOMC Statement and “dot plot” signal FFR hikes in all the remaining six FOMC meetings for this year i.e. seven hikes in total amounting to +175bps in 2022 plus another 3-4 hikes in 2023. Balance sheet reduction (quantitative tightening) is also guided to commence soon after the start of the FFR hikes cycle.

- Latest FOMC statement and dot plot shows Fed is focusing on its price stability mandate given the consumer price index (CPI) trends. This is as Fed raised its 2022 inflation rate forecasts to 4.3% vs 2.6% in Dec 2021. Fed also revised upwards the inflation rate forecasts to 2023 and 2024 to 2.7% and 2.3% respectively from the Dec 2021’s projections of 2.3% and 2.1% respectively. Core inflation is also expected to be higher now i.e. 4.1% vs 2.7% previously in 2022; 2.6% vs 2.3% previously in 2022; 2.3% vs 2.1% previously in 2022.

- Updated dot plot indicates a total of seven rate hikes this year totalling +175bps and another 3-4 hikes in 2023 to result in the median FFR reaching 2.75% by end-2024 (Fig 4) and a longer-term rate of 2.375%. Back in Dec 2021, the forecasts were 3 hikes totaling +75bps per year in 2022-2023 followed by another 2 hikes amounting to +0.50bps in 2024 with a longer-term rate of 2.50%.

- Fed’s unemployment rate forecasts for 2022-2023 remain at 3.5% with a slightly higher 3.6% in 2024 vs 3.5% previously, while 2022 real GDP growth forecast is trimmed to 2.8% from 4.0% previously while the projection for 2023 and 2024 are maintained at 2.2% and 2.0% respectively.

- Fed also alluded to balance sheet reduction or “quantitative tightening” to commence soon after the start of FFR hike cycle as per the FOMC statement i.e. “The Committee expects to begin reducing its holdings of Treasury securities and agency debt and agency mortgage-back securities at a coming meeting”. QT may begin as soon as the next FOMC meeting on 3-4 May 2022 but we think no later than the 26-27 July 2022 FOMC meeting. To note, QE Taper that started Nov 2021 ended this month.

- Fed Chair Powell then told reporters that inflation is too high, labor market is over-heated and price stability is a “pre-condition” for Fed. While he noted that Ukraine war had highly uncertain implications for US economy that create near term upward pressure on inflation while weighing on economic activity, he played down the risk of recession and emphasized that US economy is “very strong” and can handle tighter policy. Powell also signalled that balance sheet announcement could come as soon as May and the rolldown framework to move faster than last time.

- Comments made by Fed officials are starting to shift significantly, looking for much faster pace of policy normalisation, in terms of magnitude of rate hikes and trajectory. We believe this is due to inflation showing no signs of abating and may even be at risk of going higher for longer amid Ukraine situation exacerbating supply chain disruptions. So far, markets have taken Fed's hawkish shift in its stride (i.e., no major sell-off in equities or FX) and we opined that this is because the Fed is playing catch-up with markets (i.e., dots plot have been lagging markets' pricing). But if the tide shifts and markets end up playing catch-up with the Fed instead, then we would be more cautious as surprise shocks can undermine sentiment and add to USD support. And the risk is that markets may not have priced in rates above 3% or 4% into 2023. This is also 1 risk to be mindful of and how that can intermittently add to USD support.

- Mester is not ruling out 50bps hike and backs front-loading rate hikes in 1H this year, given the underlying strength of the economy and the Fed fund rate is at low levels. She also wants to get policy rate up to 2.5% this year and follow up with more increases next year to rein in 40y high inflation.

- Daly also share similar view in **getting rates up to neutral** (Fed estimates neutral at ~2.4%) and that **Fed could consider tightening to restrictive policy** to ensure that inflation comes back down. She is also looking at +50bps hike and decision to shrink balance sheet at May FoMC (if economics data in coming weeks support).

- Bullard reiterate his stance that the Fed needs to move aggressively to keep inflation under control. He is also looking for rates to get to neutral at least so as not to put upward pressure on inflation. Bullard's estimate neutral at 2% while the median of FoMC officials is at 2.4%. He also cited the 1994 tightening cycle as an analogy on how fast Fed should move. That cycle was indeed one of the fastest but most compressed cycle since 1980s, where then-Fed Chair Greenspan tightened by 300bps over a 1y period in 1994-95, which included two 50bps hike and one 75bps hike. "Soft-landing" was achieved, recession and inversion of 2y10y yield curve was also averted.

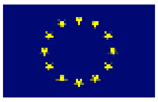
- During a NABE seminar (21 Mar), Powell had also sounded more hawkish in saying, *"We will take the necessary steps to ensure a return to price stability. In particular, if we conclude that it is appropriate to move more aggressively by raising the federal funds rate by more than 25 basis points at a meeting or meetings, we will do so. And if we determine that* ***we need to tighten beyond common measures of neutral and into a more restrictive stance, we will do that as well****.*

- The 30d Fed fund futures are now (as of 31 Mar) pricing in rate to go up to 2.25% by end-year (vs. 1.95% a week ago vs. 1.06% as of late-Jan 2022). The fed fund futures are also implying >50% probability of 50bps at the next 2 FoMCs on 4th May and 15th Jun.

- **Latest Fiscal and External Balance Outlook:** The trade deficit increased to $89.7bn in Jan from an upwardly revised $82.0bn in Dec. Total volume of trade was largely unchanged, with a decrease in exports (-$3.9bn) offset by an increase in imports (+$3.8bn).

- **Key domestic events and issues to watch in Apr**: ISM Manuf (1 Apr); Feb Factory orders, durable goods orders (4 & 26 Apr), NFP (1 Apr); Trade balance (5 Apr); CPI (12 Apr); retail sales (14 Apr); PCE deflator (28 Apr); 1Q GDP (28 Apr).

- **Technical Outlook:** DXY consolidated near recent highs. Last seen at 98.46 levels. Bearish momentum on daily chart intact though RSI rose. On weekly chart, bearish momentum appears to be emerging on the MACD with RSI showing signs of falling from near overbought conditions. Risks are to the downside. Bias to sell rallies. Resistance at 98.55 (21 DMA), 99.45 (triple top), 99.73 (76.4% fibo retracement of 2020 high to 2021 double-bottom low). Support at 97.72 (61.8% fibo) and 96 levels (50% fibo).



EUR: War Undermines but NIRP Regime Change Supports

Forecast	2Q 2022	3Q 2022	4Q 2022	1Q 2023
EURUSD	**1.1200** (1.1400)	**1.1250** (1.1600)	**1.1500** (1.1800)	**1.1500** (--)

Previous Forecasts in Parenthesis

- **Motivation for the FX View:** We calibrate our EUR forecast softer amid war in Ukraine persisting for longer, stagflation fears, French election uncertainty risks and ECB-Fed policy divergence. 2y EU-UST yield differentials have continued to widen to more than 3y low of -246bps (vs. -194bps at start Mar). Prolonged military conflict in Ukraine (entering into its 2nd month) is a risk and could further worsen supply chain disruption, aggravate energy crisis and weigh on economic activities while rising prices will hit household budget. But we expect EUR to consolidate and recover in coming weeks as (1) Europe's recovery from pandemic remains intact as recent Mar prelim PMIs suggest little evidence of major slowdown and ECB does not anticipate stagflation; (2) ECB may need to catch-up on policy normalization as inflation continues to rear its head. A potential end to ECB's negative interest rate policy (NIRP) era may have profound and positive impact on EUR; (3) USD tends to peak post-first Fed hike while EUR historically bottoms and appreciate; (4) tentative signs of progress in Russian-Ukraine negotiations though a comprehensive deal for ceasefire, withdrawal of troops, neutralisation and demilitarization could take up to weeks to come to an agreement. To conclude, we expect EUR to be in a bottoming process with base around 1.09 – 1.12 this quarter. Risks to this view are: (1) Fed's policy normalization (with risks of stepping up its pace); (2) French election risks (Apr-2022) but we do not expect political driven weakness to persist; (3) protracted military conflict in Ukraine. Eventually into later part of 2H 2022, we expect EUR to trade higher (towards 1.15-1.16 levels) as USD strength gives way. Global growth recovery is expected to broaden amid reopenings/ relaxation of border restrictions while persistent price pressures in Europe (and/or over US) puts pressure on ECB normalise policy earlier.

- **ECB Policy Normalisation/ NIRP regime change can add to EUR strength.** ECB's Visco reiterates ECB's stance that supply shock cannot be countered simply by monetary policy while Villeroy said that green transition may cause some inflationary pressure and ECB must not over-react to energy price volatility. But there are also <u>ECB speaks, action that showed **increasing willingness to normalise policies**</u>. For instance, ECB's Knot said he does not rule out 2 interest rate hikes this year should forecasts for already soaring consumer prices shift higher still. He added that prices are "the dominating worry" right now with the dangers to the outlook tilted to the upside… the war risks stoking energy costs, with a longer bout of elevated inflation increasing the chance that price expectations of household and companies move higher. ECB's Lane, Vasle and Muller have also recently backed support for hike this year while Kazimir wants ECB to end negative rates in next 12 months. ECB's decision to accelerate the wind down of QE was perceived as preparing the ground for lift-off when necessary conditions are satisfied. Lagarde also highlighted that inflation dynamics over medium term will not return to the pattern seen in pre-pandemic. An eventual scenario of **ECB catching up on policy normalisation or ending NIRP (negative interest rate regime) may catch markets by surprise and that can aid EUR's recovery.** As of 30 Mar, markets are pricing in over 60bps hike this year and over 100bps hike cumulatively in a year's time.

- **French election a source of volatility but likely to fade.** First round of Presidential election takes place on 10th Apr and if no candidate takes a majority in the first round, a run-off will then be held on 24th Apr for the top 2 candidates. 12 candidates including President Macron, his main rivals, Marine Le pen, Jean-Luc Melenchon and Eric Zemmour are challenging for French presidency. As of 28 Mar, Politico's poll of poll voting intentions showed Macron in the lead (28%) while Le pen and Melenchon are runner-ups at 19% and 14%, respectively. That said, Macron's lead has been falling slightly while support for Le Pen picked up. Macron has been criticised for his absence at campaigns as he gets very involved with Russia-Ukraine crisis. Nonetheless incumbent Macron is still expected to win a second term however in the unfortunate scenario that Macron loses, EUR could face further downside.

- **Stagflation a concern but ECB dismissed possibility.** Russia invasion of Ukraine has now entered into its second month. Prolonged military conflict risks worsening global supply chain disruptions and in turn exacerbating inflation woes. The risk of a prolonged rise in energy and food prices could mean even higher price pressures adding constraints to growth, triggering stagflation concerns. Some European companies in industries like fertiliser, steel mill, especially those energy-intensive ones have reportedly cut production due to high input cost. EUR is at risk of being dragged lower given its trade, energy and investment ties with Russia. In 2020, Russia was 5th largest partner for EU exports and imports while EU relies heavily on Russia for energy consumption (41% gas comes from Russia). At one point, Russia even threatened to cut natural gas supplies to Europe (via Nord Stream 1 pipeline) as part of its counter-response to sanctions imposed (though it has not yet made that decision). That said, ECB officials have played down fears of stagflation in EU. Lagarde said that "even in the bleakest scenario with second round effects with a boycott of gas and petrol and worsening of war that goes on for a long time, the Euro-area will still manage a 2.3% growth". This is assuming a severe scenario of stricter sanctions on Russia that leads to disruptions in global value chains, higher energy prices due to reduction in supply, a stronger repricing in financing markets and larger second round effects. ECB's base case scenario with CPI at 5.1% could still see GDP growth at 3.7% for 2022. Under a less extreme adverse scenario, the hit to growth and jump in inflation is not as pronounced.

- **Growth and Inflation Outlook: Markets are keeping a close scrutiny on how growth in the EU-area will be affected by Ukraine crisis.** At first glance, Euro-area prelim PMIs came in firmer for both manufacturing (57 vs. 56 est.) and services (54.8 vs. 54.3) in March. Germany and France's PMIs also surprised to the upside. There maybe little evidence at this point to say that EU growth momentum has been derailed, though we note that some sentiment surveys such as EU consumer confidence (-18.7 vs. -12.9 expected), German IFO expectations (85.1 vs. 92 exp) and France consumer confidence (91 vs. 94 exp) fell for the month of March. We keep a close watch on development. Taking stock, Euro-area final GDP rose 0.3% q/q in 4Q, in line with softer expectations as omicron wave, supply chain disruptions weighed on activity. Breakdown by country showed that German economy shrunk in 4Q w0hile Spainish and French economies expanded. In annual terms, 4Q GDP for Euro-area was 4.6%. For whole of 2021, growth for the region came in at a respectable +5.2%. Euro-area economy is now at pre-pandemic lavel.

- **Headline CPI surged to fresh record high of 5.9% y/y in Feb,** up from 5.1% in Jan. The rise was fuelled by sharp increases in the price of energy (+32% y/y) and food (+4.2% y/y) as well as cost of services and manufactured goods. Core inflation surged to another record high of 2.7% y/y, up from 2.3% in Jan. ECB warned that inflation could hit 7.1% this year under a "severe" scenario (assuming more sanctions, higher energy costs). We retain our view that inflation could still head higher amid supply chain disruptions, higher energy prices amid ongoing war in Ukraine. (in part driven by omicron variant) while energy prices remain supported amid geopolitical tensions between US-Russia over Ukraine. Softer EUR may also have resulted in some imported inflation while the pursuit of climate change goals could also further keep commodity price pressures broadly supported. Overall, we still expect that ECB could be forced to play catch-up in normalizing policies especially if inflation proves to stay elevated for longer. This can be a positive for EUR.

- **Monetary Policy Forecast:** We expect ECB to keep policy status quo (deposit rate maintained at -0.5%) at the upcoming meeting on 14 Apr. We believe there will be no further steps taken to accelerate policy normalization at this stage, given a divided ECB over when rates should be tightened. For now, markets are pricing 2 hikes (of 25bps each) by end-2022 with the first hike potentially coming at 8th Sep GC. A total of 4 ECB hikes is now priced in a year's time. We also expect ECB to follow its earlier-said sequence of ending bond purchases before raising rates. We continue to monitor ECB speaks to get a sense of any hawkish shifts.

- Outcome of last ECB meeting (10 Mar) came as a surprise to most analysts as ECB accelerated its wind-down of monetary stimulus. ECB signalled that it is more concerned of inflation than weaker economic growth. Bond purchases will slow from May (to EUR30bn then to EUR20bn in Jun) and that APP could end as soon as 3Q. These were largely in line with our expectations - *pace of APP be reduced (from planned EUR40bn/month starting Apr) or be made flexible while an earlier end (vs. previously guided timeline of Oct-2022) is not ruled out. We believe policy normalisation plan should not be derailed and that policymakers can use forward guidance to anchor stability in financial conditions and the EUR*. The ECB also managed to paint some guidance and score some flexibility on policy rate trajectory. In particular ECB said that any hikes will be "gradual" and take place "some time after" bond purchases end, instead of "shortly after". This is a notable shift from its previous statement where it said that GC no longer suggests interest rates could go lower than at present. Lagarde elaborated that "some time after" is encompassing as it can be the week after but it can also be months later. She stressed that time horizon is not what's going to matter most but the incoming data. On net the overall meeting was regarded as a hawkish tilt.

- **Latest Fiscal and External Balance Outlook**: Euro-area current account surplus held steady at EUR23bn in Jan. Surpluses were recorded for services (EUR16bn), goods (EUR14bn) and primary income (EUR6bn) but partially offset by a deficit for secondary income (-EUR13 billion). For 12 months to Jan-2022, EU area current account surplus stood at 2.4% of GDP (vs. 2.2% of GDP in 2020).

- **Key domestic events and issues to watch:** Mar mfg PMI, CPI estimate (1 Apr); Apr sentix investor confidence (4 Apr); Mar services PMI (5 Apr); Feb PPI (6 Apr); Feb retail sales (7 Apr); ZEW survey expectations (12 Apr); Feb IP (13 Apr); ECB meeting (14 Apr); Feb trade (20 Apr); Feb construction output, Mar CPI, Apr consumer confidence (21 Apr); Feb current account (22 Apr); Apr prelim PMIs (22 Apr); Apr consumer confidence (28 Apr); Apr CPI estimate, 1Q GDP (29 Apr).

- **Technical Outlook:** EUR traded a touch firmer after hitting multi-month low in early Mar. Pair was last at 1.1055 levels. Mild bullish momentum on daily chart intact but rise in RSI moderated. On the weekly chart, bullish divergence is emerging on the MACD. We still see technical supporting bottoming out play. Bias to buy dips. Support here at 1.1050, 1.1010 (21 DMA) and 1.0860 (76.4% fibo retracement of 2016 low to 2018 high). Resistance at 1.1140, 1.1190/1.12 (61.8% fibo, 50DMA) and 1.1245 (100 DMA).

GBP: Hurt by Surging Inflation and BoE's Slight Dovish Tilt

Forecast	2Q 2022	3Q 2022	4Q 2022	1Q 2023
GBPUSD	1.3200 (1.3600)	1.3250 (1.3600)	1.3400 (1.3800)	1.3500 (--)

Previous Forecasts in Parenthesis

- **Motivation for the FX View: We revised GBP forecast lower in light of recent shifts:** (1) BoE seems to show signs of softening its stance; (2) softer GBP adds to inflation, further hurting household budget. (3) Yet Chanellor Sunak did not address near term economic headwinds when presented with opportunity at spring budget; (4) War in Ukraine persisting for longer should also hurt broad sentiments while swath of sanctions on Russian oligarchs may potentially hurt UK's financial hub status as money flows could be curtailed. BoE Governor Bailey's emphasis that BoE had softened its guidance on future rate increases to reflect the high level of economic uncertainty brings a potential risk that BoE may not be as hawkish even as inflation rips through. This can further hurt household budget and weigh on consumption and growth outlook. Ongoing supply chain disruption may worsen due to war in Ukraine persisting. Concerns of elevated energy prices feeding into runaway inflation and potentially a weaker GBP (due to less hawkish BoE), could further bring about imported inflation, fuelling a vicious cycle and hurting consumers and businesses. The risk of much faster pace of Fed normalization (such as double tightening of rates and QT) could drive BoE-Fed policy divergence and this pose further downward risks to GBP in the near term.

- **Signs that BoE Turning Slightly Less Hawkish.** We noted some slight shifts in tone and language since the last MPC on 17th Mar. In particular, BoE Governor said that that further tightening of policy "might be" appropriate in coming months. The phrase "might be" was used instead of "likely" as seen from previous statement.Subsequently, at a speech in Brussels (28 Mar), he said that "we are facing a very big shock by any historical standard and there is a very high level of uncertainty.. the task we have is clear but its's hard". This was a follow-up emphasis from his earlier remarks that BoE had softened its guidance on future rate increases to reflect the high level of economic uncertainty. Seperately in a speech in London (30 Mar), Deputy Governor Broadbent said that "even when central banks attempt to engage in more standard, conditional statements about future policy, they can be sometimes mistaken for firmer commitments than they really are. We caution that in light of Ukraine situation persisting, there is a risk of officials turning less hawkish as they may prioritise supporting growth over fighting inflation. Any of such shift would result in paring back of rate expectations and that will weigh on GBP. To some extent, a hawkish Fed may even ampflfy GBP's weakness especially if markets price in BoE-Fed policy divergence. For now (31 Mar), markets are still pricing in over 130bps hike up to Dec-2022.

- **Sunak's Support May Not Have Done Enough.** At the spring statement, Chancellor Sunak attempted to address rising costs Some highlights include: (1) cutting fuel levy by 5p per litre until Mar 2023 – worth about GBP2.4bn; (2) increased threashold at which Britons start paying payrolls tax (a national insurance) by GBP3k instead of the panned GBP300 - this move will help 30mio people; (3) cut basic rate of income tax to 19% in 2024 (down from 20%) – measure worth GBP5bn/ year; (4) double grant to GBP1bn for stuggling Britons amongst others. While it does seem generous, skeptics have it that the support may not be sufficient to help those with lowest incomes while Office for Budget Responsibility said that net tax cuts offset only 1/6 of the tax rises introduced since Sunak becomes Chancellor in 2020.

- **Growth and Inflation Outlook: UK has recently cut 2022 GDP forecast to 3.8%,** from 6% citing impact of Ukraine war, high global inflation and continuing supply chain pressures. Forward looking surveys and activity indicators are looking mixed. On the positive, labor market remains tight with unemployment rate dipping to 3.9%, downside from 4.1%. while prelim services PMI rose further to 61 for Mar (vs. 60.5 in Feb). On the negative, manufacturing PMI eased to 55.5, from 58 in Feb (though still in expansionary territory), consumer confidence plunged to -31 for Mar, from -26 in Feb and retail sales fell to 4.6% y/y in Feb, down from 7.2% in Jan. We also point out that Chancellor Sunak's spring statement (on 23 Mar) did not address near term economic headwinds though fuel duty of 5pence will be suspended till Mar-2023. We continue to monitor if growth momentum slows further amid supply chain disruptions. Taking stock, UK economy expanded 1.3% q/q (final print) in 4Q, (up from 1% in preliminary print). Services sector and exports led the expansion. Looking back, UK experienced one of its fastest pace of economic growth (+7.4% in 2021) since 1941.

- **Headline CPI rose to fresh multi-decade high of 6.2% y/y in Feb,** up from 5.5% in Jan. Main drivers of higher prices are energy, fuel and food.BoE now expects CPI to peak at 8% in 2Q. We see risks of inflation staying elevated as Russian invasion of Ukraine continued to result in cost-push inflation, affecting prices of food and energy. These will further add to upward pressure in coming months. Meanwhile core inflation rose to all-time high of 5.2% y/y (vs. 4.4% in Jan).

- **Monetary Policy Forecast: There is no MPC in Apr. We expect BoE to continue with its back-to- back hike of +25bps rate hike at the next MPC on 5th May.** Taking inflation down to its medium term target of 2% is still BoE's priority but at the same time, BoE Governor seemed to have hint at softening guidance on future rate increases to reflect high level of economic uncertainty. We also noted that some BoE officials also seem to favor raising rate in a "measured" way – (earlier) BoE Chief Economist said that BoE will seek to bring inflation down in a way "that doesn't disturb the rest of the economy", BoE Governor Bailey gave a heads-up that inflation could again overshoot BoE's forecasts but warned that markets should not get carried away about the likely magnitude of hike. For now (as of 31 Mar), markets are still pricing in over 130bps hike up to Dec-2022.

- At the last BoE meeting (17 Mar), the MPC voted 8-1 to raise policy rate by 25bps to 0.75%, as widely expected. BoE cautioned that inflation looks set to climb to around 8% in 2Q, up from its previous projection of a peak of 7.25%. BoE explained that the spike in inflation means the squeeze on households incomes in the U.K. will be “materially larger” than implied in February. It also warned that the war in Ukraine will exacerbate global supply chain disruptions. The squeeze on incomes will lead to a weaker outlook for growth and raise unemployment. On forward guidance, we noted the slight dovish shift in tone as Governor Bailey said that further tightening of policy “might be” appropriate in coming months. This constitutes to a shift in tone and language from “likely”.

- **Fiscal and External Balance Update: 4Q current account deficit narrowd sharply to GBP7.3bn, from GBP24.4bn.** Trade deficit shrank as exported rebound sharply. Investment income also rose to GBP4.7bn surplus, for the first time since 2011. As % of GDP, current account deficit was at 1.2% of GDP vs. 3Q of 4.2% of GDP.

- Public sector net borrowing (PSNB ex) for month of Feb alone was GBP13.1bn, higher than GBP8.1bn expected. For the 1st 11 months was GBP138.4bn, 52% below the record GBP290.9bn borrowed between Apr 2020 to Feb 2021. Office for Budget Responsibility projected that borrowing for next fiscal year is now forecast to be GBP99bn, GBP16bn higher than previously projected. Public sector net debt, excluding state-owned banks, totalled GBP2.327tn or 94.7% of GDP.

- **Key domestic events and issues to watch:** Mar PMI Mfg (1 Apr); services PMI (5 Apr); Mar construction PMI (6 Apr); Feb industrial production; monthly GDP, construction output, trade, (11 Apr); Mar labor market report (12 Apr); Mar CPI, PPI (13 Apr); Mar retail sales, Apr prelim PMIs (22 Apr) Mar public finances (26 Apr).

- **Technical Outlook:** GBP traded in consolidative pattern after the decline since start of 2022. Last seen at 1.3125 levels. Bearish momentum on weekly chart remains intact while on the daily chart, there is a lack of conviction on momentum at this point. Price action could remain consolidative in 1.3050 – 1.3250 range until clearer signs emerge. Wider range seen at 1.30 – 1.34.

AUD: Retracement Risks

Forecast	2Q 2022	3Q 2022	4Q 2022	1Q 2023
AUDUSD	0.7400 (--)	0.7500 (--)	0.7500 (--)	0.7600 (--)

No Change to Previous Forecasts

- **Motivation for the FX View:** AUD surged throughout most of Mar and arrived at the 0.75-figure (beyond our 1Q forecast which is already among the bullish of the lot) by the end of the month, underpinned by the surge in commodity prices (energy, metal, agriculture). AUDUSD has also benefitted from recently widened AU-US yield differential (Russian attack-triggered risk aversion), rise in commodity prices (iron ore, copper prices, energy). The broader risk-off did not seem to affect AUD as much. Australia is seen as a possible alternative LNG provider to Europe if current conflict with Russia tarry longer. We remain constructive on the AUD even as RBA Governor Lowe seems determined keep cash target rate lower for longer. Slower moving global thematics - climate change needs (infrastructure, clean energy) should provide some longer-term TOT underpinnings.

- Another contributing external factor that supports AUD is China's recent endeavours to stabilize property market. Local governments announced various respective market measures – accelerated mortgage approvals seen in Beijing and Shanghai, lower down payment ratios in reported in the Heze city. More recently, Harbin has plans to remove the ban on new homebuyers from selling their properties within three years of purchase. A strong revival of the property sector in China is unlikely but steady iron ore gains could continue to cushion the AUD and supports our sanguine view of the currency for 2022.

- For the month of Apr however, AUD could run into some bearish retracement risks given the fact the strong rally in Mar. Any sign of de-escalation for the war in Ukraine via a compromise to ceasefire could spur some profit-taking for the AUD.

- **Growth and Inflation Outlook:** AUD has thus far been supported by reasonably rebound in household spending and better business conditions reported for Feb. House price index ffor 4Q was solid with a 23.7%y/y recorded. The Feb labour report was also robust encompassing a +77.4K net addition of jobs recorded for the month, slightly higher participation rate of 66.4% and a lower jobless rate of 4.0% vs. previous 4.2%. The CBA household spending also rebounded 1.8%m/m from previous -10.0% as the Omicron wave faded.

- **Subsequently leading indicators are a tad more mixed.** Key data includes consumer inflation expecations that accelerated to 4.9%y/y for Mar from previous 4.6% - the highest since 2012. ANZ consumer confidence sank to the lowest since Sep 2020 for the week ending 27 Mar, printing 91.2 vs. previous 95.8. According to the report by the report, household confidence is hurt by the rising petrol prices. That could suggest some adverse impact on private consumption for Mar. NAB business confidence surveyed in 1Q edged lower to 14 from a score of 19 in the quarter prior. Respondents also reported some deterioration in the business conditions in the last three months and business conditions are expected to worsen over the next three months. Some deceleration in Australia's domestic demand may be a greater justification for RBA to take its time to normalize monetary policy.

- **Monetary Policy Forecast:** The central bank is expected to keep status quo at its next policy meeting on 5 Apr in the absence of strong wage growth and a lack of "evidence" for pervasive price pressure, according to Govenor Lowe in his speech on 22 Mar. **We look for RBA to reduce its balance sheet in May and raise cash target rate as soon as Jun.** Thus far, RBA is focused on wage growth as a key impetus for its policy rate normalization and continues to expect wage growth to be gradual. This was validated by the modest 4Q wage price index print of 2.3%. In addition, the recent rise in household debt to income ratio may also be a hurdle for aggressive tightening in the absence of strong wage growth. That said, we see the risk of RBA potentially sounding a tad more hawkish as recent surveys suggest that consumer confidence is hurt by the rising price pressure. As of now, cash rate futures imply more than seven hikes this year. We see potential for cash rate forwards to have aggressively run ahead of the RBA and AUD could be subjected to retracement risks should hawkish tilt remain less aggressive than market expectations.

- The last meeting took place on 1 Mar after Russia attacked Ukraine. RBA chose to reiterate its message of patience as wage growth is still expected to be gradual and referred to the Ukraine war as a new source of uncertainty to inflation due to its impact on energy prices and disruptions to supply chains. Overall, the policy statement was taken to be dovish with gradual steps on normalization still preferred. While price pressure is expected to rise on the back of the recent surge in petrol prices, the central bank stated it is still premature to conclude that the CPI will sustain within the 1-3% target band. Thereafter in a separate speech on 22 Mar, RBA Lowe acknowledged that risks to inflation are skewed to the upside but retained dovish bias. He said RBA needs evidence of pervasiveness of rising inflation expectations before the central bank responds. He noted that households have an accumulated savings of A$250bn over the past two years and median mortage borrower also has a loan repayment buffer of two years which could aid households through a period of high inflation as long as inflation comes back down again.

- Monetary policy normalization could continue to underpin the AUDUSD notwithstanding some interim retracements.

- **Latest External Balance Outlook:** As of last available data, current account surplus was recorded at 3.93% of GDP for 3Q 2021. Current account is seen at A$23.9bn for 3Q2021 vs. $22.9bn in 2Q. The quarter saw wider goods surplus at A$37.4bn vs. previous A$28.2bn.

- **Fiscal Outlook: T**he 2022-23 federal budget was presented with a focus on helping Australians with the rising cost of living. Key highlights of the budget include a 50% reduction to fuel excise for the next six months, one-off $250 “cost of living payment” for six million Australians, separate one-off $420 tax offset for low- and middle income earners from 1 Jul as well as tax-deductions for SMEs for employee training and digital technology expenses. Fiscal deficits narrowed to A$78bn for FY2023 or 3.4% of GDP from expected A$79.8bn for FY2022. Real GDP is forecast to soften from 4.25% for FY2022 to 3.5% for FY2023 and then to 2.5% in each of the following three years. Unemployment rate to fall to 3.75% in the 3Q of 2023 and should remain thereabouts to FY2025. Key commodity prices to fall from current elevated levels by the end of 3Q. CPI is expected to rise 4.25% for FY2022 before easing to 3% FY2023. Wage price index to rise 2.75% in Fy2022 and then to 3.25% for FY2023-2024..

- **Key domestic events and issues to watch:** Mfg PMI (Mar), CoreLogic House Price (Mar), home loans (Feb), commodity index (Mar) on 1 Apr; M-I inflation (Mar), ANZ Job advertisments (Mar) on 4 Apr; Composite PMI (Mar) and RBA policy decision on 5 Apr; Trade (feb) on 7 Apr; Foreign Reserves (Mar) on 10 Apr; CBA household spending and NAB business surveys (Mar) on 12 Apr; Westpac consumer (Apr) on 13 Apr; consumer inflation expectation (Apr) and labour report (Mar) on 14 Apr; Westpac leading index (Mar) on 20 Apr; prelim. PMI for mfg, services, comp. (Apr) on 22 Apr; CPI (1Q) on 27 Apr, import price, export price (1Q) on 28 Apr; PPI (1Q).

- **Technical Analysis:** We still stick to a tactical bearish view on the AUD given that AUDUSD has made many attempts and failed to break above the upper bound of the rising channel, marked at around 0.7480-0.7520. Stochastics flag overbought conditions and MACD forecast suggest bearish divergence. Pair may retrace towards then 0.7395 (21-dma) which happens to be the middle of the rising trend channel. Resistsance at 0.7556.

NZD: Preparing for Borders to Re-open

Forecast	2Q 2022	3Q 2022	4Q 2022	1Q 2023
NZDUSD	**0.7000** (0.7200)	**0.7100** (0.7300)	**0.7100** (0.7300)	**0.7100** (--)

Previous Forecasts in Parenthesis

- **Motivation for the FX View: We retain our constructive bias on NZD** amid continued rise in commodity prices (in particular soft/agri commod such as food, dairy) and hawkish RBNZ. At point of writing (31 Mar), our bullish 1Q forecast of 0.69 (vs. consensus of 0.68) has been \ met. We expect NZD to trade 0.6850 – 0.7050 range in coming weeks to months, drawing support from higher commodity prices, economy reopening (international borders to be eased from May, in turn boosting tourism) and the potential for faster RBNZ hikes. We still opined that with global inflation elevated, policymakers may even quietly favor a stronger currency to curb imported inflation. But with Ukraine situation persisting for longer, we acknowledge that downside risks to global growth has indeed risen. That may affect Kiwi's trajectory. As such we calibrate our FX forecast levels lower but maintain trajection path.

- **Continued Rise in Dairy Prices Supportive of NZ Exports, NZD.** The weighted average winning price for all milk products hit an all time high of $5065 at the fortnightly Global Dairy Trade auction in early Mar. The global dairy trade price index also hit 1593, breaking the last record high of 1573 in Apr-2013. Prices for other dairy-related products such as butter, cheddar cheese, wholemilk powder were all up as well. The rise in dairy prices was fuelled by steady demand while global milk supply faltered below average as production in EU and US continued to be impacted by higher cost of feed while environmental challenges in NZ also impacted supply. In late-Feb, Fonterra lifted its forecast farmgate mild price for current season to a record high mid-point of $9.60/kg of milk solid. Dairy prices are likely to stay elevated in the near term, alongside food prices amid food security concerns, supply chain disruptions due to war in Ukraine. NZD and dairy prices are positively correlation (coefficient of 0.56) and elevated dairy prices is another factor that is supportive of NZD gains in the near term.

RBNZ May Not Lose Out to Hawkish Fed. OIS-implied show markets are pricing in about 200bps hike for Fed this year. On the kiwi front, markets are also pricing in about 200bps rate increases for RBNZ this year. With 6 more MPCs to go, it is highly likely we see at least one if not two 50bps hike. About 50% probability is priced in for 50bps hike in Apr. We do not rule that out as RBNZ had indicated its openness to do 50bps if need rises. What is holding us back from calling for 50bps is that NZ economy still faces near term downside risks owing to omicron spread (though it has peaked, daily cases are still high at ~15k cases per day) and global supply chain disruption impacting activities. Hence we have our call for 50bps hike in May 25th MPC instead when omicron spread further stabilizes, borders restrictions ease (from May onwards) and better clarity on Ukraine situation. So to some extent, hawkish Fed may not cause much policy divergence impact.

- **Hawkish RBNZ May See 50bps Hike in May as Inflation Runs Amok.** Price pressures continue to run red hot on multiple fronts from wages to food, dairy and petrol prices. RBNZ is also projecting headline CPI to rise to 6.6% in early 2022. This justified RBNZ guiding for a faster pace of monetary policy normalization: (1) Quantitative tightening will commence in Jul with a sell-down in QE holdings at pace of NZ$5bn per year and RBNZ will not reinvest proceeds of expired debt; (2) OCR projections have been raised to 3.25% by end-2023 (up from 2.6% previously). This implies another +225bps hike projected over the next 2 years; (3) MPC is open and willing to hike OCR by 50bps if needed. In comparison to other major DM central banks, RBNZ is now perceived to be one of the more hawkish one, apart from Fed. On policy divergence play, NZD may gain the upper hand over its DM peers.

- **Tourism another Boost to NZ Growth.** NZ is preparing to ease border measures much earlier than expected as Omicron situation shows signs of improvement. Phased reopening has been brought forward from Oct-2022 with Australians allowed to enter the country without needing to quarantine or isolate from 13 Apr and to open fully to visa-waiver countries from 1 May, including US, UK, Japan, Singapore, Taiwan and others. While economic momentum may be temporaily affected in 1Q, we expect a a decent rebound in 2Q. But looking out, we acknowledge there are increasing downside risks to growth, especially with the war in Ukraine persisting. That can pose downward pressure on NZD at some point when more data comes on stream.

- **Downside Risks to NZD Outlook.** (1) War in Ukraine futher escalates into biochemical/ broaden to involve more countries or last longer may hamper global economic momentum and that will have negative spillover effects on NZ. Also furuther slowdown in China growth, or sudden weakening in CNH can also weigh on NZD, given its high sensitivity to global growth and China. (2) RBNZ fails to live up to hawkish guidance will be a drag on NZD (unwinding risk); (3) Much faster shifts in Fed's pace of policy tightening will weigh on sentiment and narrow NZD's yield advantage.

- **Growth and Inflation Outlook: NZ economy expanded +3% q/q in 4Q, up from -3.6% in 3Q.** Rebound was led by services and goods producing industries, including manufacturing output (+6.5%), construction gain (+8.7%) while primary sector output fell. **Looking on, 1Q economic**

activity could slow futher amid widespread Omicron variant and subsequent tightening of measures. Consumer confidence fell to 81.7 in Feb (vs. 97.7 in Jan) while card spending slumped to -7.6% m/m (vs. 2.1% in Jan). But we expect any slowdown to be temporary and economy should rebound in 2Q 2022 when infections fade, restrictions eased and borders reopen. Manufacturing PMI rose to 53.6 vs. 52.1 in Jan while services PMI remains in contractionary territory (48.6 vs. 45.9 in Jan). On employment conditions, labor market continue to exhibit signs of tightening. Unemployment rate fell further to all time low of 3.2% in 4Q (vs. 3.4% in 3Q), while hourly earnings continued to accelerate to +1.4% q/q in 4Q (vs. 1.2% q/q in 3Q).

- **1Q CPI will be released on 21 Apr.** Price pressures continue to rise overall with NZ food prices surging +6.8% y/y in Feb, an 11-year high while dairy prices also rose to 9-year high. **RBNZ now sees headline CPI rising to 6.6% in early 2022.** 4Q headline CPI surged to more than 30-year high of 5.9% y/y, up from 4.9% in 3Q. This is the third quarter in a row that headline CPI breached above RBNZ's 1% - 3 target band. Price increase was broad-based across 10 out of the 11 main groups in NZ CPI basket. In particular the main drivers contributing to upward price pressure include construction and rental for housing as well as petrol prices. We expect price pressure to stay supported given supply chain disruption and spread of omicron variant in NZ.

- **Monetary Policy Forecast:** We expect RBNZ to raise rate by 25bps again for the 4th consecutive time at the next MPC on 13 Apr. A series of gradual rate hikes is still highly probably instead of 50bps hike as omicron spread in NZ poses near term downside risks to economic activity but at the same time RBNZ needs to bring inflation under control. Possibly a 50bps hike at 25 May MPC is likely as covid situation should further stabilize by then following a peak in mid-Mar. This is also in line with Governor Orr's comments that "we're looking at some economic disruptions in the near term but can see on the horizon a return to something approaching normal activity" For now, markets are pricing in about 200bps rate increases for this year. With 6 more MPCs to go, it is highly likely we see at least one if not two 50bps hike. About 50% probability is priced in for 50bps hike in Apr. We do not rule that out as RBNZ had indicated its openness to do 50bps if need rises. What is holding us back from calling for 50bps is that the economy still faces near term downside risks owing to omicron spread (though it has peaked, daily cases are still high at ~15k cases per day) and global supply chain disruption impacting activities. Hence we have our call for 50bps hike in May 25th MPC instead when omicron spread further stabilizes, borders restrictions ease (from May onwards) and better clarity on Ukraine situation.

- The last MPC (23 Feb) saw RBNZ took another hawkish step forward. OCR was raised for 3rd time in a row by 25bps to 1% while quantitative tightening will commence in Jul with a sell-down in QE holdings at pace of NZ$5bn per year and will not reinvest proceeds of expired debt. Recall that RBNZ bought a total of NZ$55bn of government bonds under its QE program over 2020-21 due to pandemic. Accompanying MPS also indicated that more monetary tightening was needed than signalled in Nov MPS. While RBNZ considers the spike in global inflation to be temporary, it also said that long term inflation expectations have risen.

Inflation is now seen to accelerate to 6.6% in 1Q 2022 and it does not expect inflation to return to 1% - 3% range until 2025. OCR projections have been raised to 3.25% by end-2023 (up from 2.6% previously). This implies another +225bps hike projected over the next 2 years. RBNZ also projected OCR to be at 2.2% at end of 2022 and indicated that the MPC is open to hike rates by 50bps if need arises.

- **External Balance and Fiscal Outlook: NZ posted record annual current account deficit of $20bn.** Imports more than overwhelmed exports in 4Q. YTD current account deficit stood at -5.8% of GDP. Quarterly current account deficit surged to $6.5b in 4Q, up from $4.7b the previous quarter.

- **NZ government expects budget deficit to return to surplus by the fiscal year ending June 2024 (FY24),** according to its Half Year Economic and Fiscal Update. This is 2 years ahead of previous forecasts due to significantly stronger tax revenue than forecast in its mid-2021 budget. Net debt will be higher at 37.6% of GDP in 2021/22 compared to 34.0% forecasted in May. The net debt peaks at 40.1% by 2022/23 before falling to 30.2% by the end of the forecast period.

- **Key domestic events and issues to watch:** Mar consumer confidence (1 Apr); Mar commodity price (6 Apr); RBNZ MPC, Mar food prices (13 Apr); MarMfg PMI (14 Apr); Mar services PMI (19 Apr); 1Q CPI (21 Apr); Mar trade, Apr activity outlook (28 Apr).

- **Technical Outlook:** NZD extended its move higher for the month of Mar. Pair was last seen at 0.6935 levels. Mild bullish momentum on daily chart is fading while RSI fell. Bearish divergence on MACD and RSI appear to be playing out. We reiterate caution for retracement move lower. Support at 0.6915 (200 DMA), 0.6870 (50% fibo) and 0.6790 (38.2% fibo retracement of Oct high to Jan low). Resistance at 0.6960 (61.8% fibo), 0.70, 0.7060 (76.4% fibo).

CAD: Prepare for A Very Hawkish BoC

Forecast	2Q 2022	3Q 2022	4Q 2022	1Q 2023
USDCAD	1.2400 (--)	1.2300 (--)	1.2300 (--)	1.2200 (--)

No Change to Previous Forecasts

- **Motivation for the FX View:** USDCAD touched a low of 1.2430 (close to our longheld 1Q forecast at 1.24) against the USD on 30 Mar before making a marginal rebound. We remain modestly bullish on the CAD to strengthen as BoC shifts hawkish on inflation. Deputy Govenor Sharon Kozicki said that the central bank is prepared to “act forcefully” to return inflation to the 2% target after noting strong demand, tight labour market and high inflation. The prospect of a peace deal did not tank the crude oil prices given US’ skepticism of Russia’s commitment.

A lack of momentum for US and Iran to reach a deal for sanctions to be lifted also underpin crude oil prices. In addition, OPEC+ suppliers seem more determined to maintain relations with Russia and wish to be "politically detached" in their production decisions. We stay constructive on the currency for a move towards the 1.22-figure on a 12-month view.

- **Longer term, expect broadening growth, climate change transformation to also be structural factors for oil prices to stay supported in the medium term.** As broadening growth recovery underpin flight and freight demands, fuel consumption could also rise and keep crude oil prices and concomitantly, the CAD supported. Even as more nations pledge net zero carbon emission, infrastructure needs for energy transformation would also require fossil fuel in the interim. CAD is thus likely to benefit from structural shifts and oil prices should remain broadly benign for the currency.
- **Growth and Inflation Outlook:** CPI accelerated to 5.7% for Feb from previous 5.1%, well above the 1-3% inflation target of the BoC. Core inflation also picked up pace to 3.5%y/y from previous 3.4%, underscoring the risks of inflation expectations drifting higher. Breakdown show that the rise is broadbased with food, shelter, household operations and transportations as well as health, personal care accelerating y-o-y compared to Jan. More recently, industrial product price also overshot expectations with a print of 3.1%m/m vs. previous 3.0% while raw materials price index up 6.0%m/m. Higher input prices could continue to be passed on to consumers given current strength in demand condtions.
- Retail sales for Jan rebounded more than expected to 3.2%m/m from previous -2.0%, underscoring the resilience in spending that should gain momentum as the Omicron wave fades. However, more recent consumer confidence survey conducted by the Nanos research revealed a decline in consumer confidence (weekly polling) to 56.3 (lowest since Jan 2021). The Nanos research, albeit based on a small sample of 250 Canadians, revealed that respondents were concerned with the war in Ukraine as well as inflation.
- With regards to the labour market, Canada added a net 336.6K of jobs in Feb and jobless rate fell to 5.5% from 6.5%. Hourly wage rate has risen 3.3%y/y from previous 2.4%. We may continue to see strong hiring intentions based Mfg PMI for Feb suggest that manufacturing output is still expanding.
- **Monetary Policy Forecast:** BoC raised its policy interest rate by 25 bps on 3 Mar, noting strong economic conditions at full capacity and inflation too high at around 5% (three year high). Like many other central banks, BoC was concerned that the war in Ukraine is raising prices of energy and food, posing a new major source of uncertainty for inflation. Along with the first rate hike, the central bank flags quantitative tightening will be the next step by allowing government bonds to mature.
- More recently, Deputy Governor Sharon Kozicki said that the central bank is prepared to "act forcefully" to return inflation to the 2% target after noting strong demand, tight labour market and high inflation. She was concerned that higher price pressures are "especially painful" for

low income individuals. We thus see a strong likelihood for BoC to commence quantitative tightening at the next meeting on 13 Apr to accompany a 50bps hike to bring policy rate to 1.00% in an attempt to tamper rising inflation. Robust labour market conditions and capex sentiment could mean that domestic conditions are strong enough for BoC to become more aggressive on rate hikes.

- **Latest External Balance Outlook:** As of last available data, Canada's current account balance was at a surplus of C$1.2 for 4Q, an improvement from the previous -U$1.6bn deficit. Firm commodity prices continue to bode well for Canada's external balances.
- The next federal budget will be released on 7 Apr. Finance Minister and Deputy Prime Minister Chrystia Freeland pledged to improve affordability and to continue building an inclusive Canada with the budget. Sources have cited that t the budget will be a "back to basics" after two years of outsized expenditure. Of relevance would also be the boost to defence allocation given NATO's urge for members to spend at least 2% of GDP on defence. On the other hand, some have voiced concerns about fiscal consolidation. We recall that 2021 Budget had been expansionary with $101.4bn in new spending over three years expected to spur recovery and to support the transition to a green economy.
- **Key domestic events and issues to watch:** Building permits (Feb), 1Q BoC overall business outlook on 4 Apr; Feb trade on 5 Apr; Mar labour report on 8 Apr; BoC rate decision on 14 Apr; Feb manufacturing sales on 14; housing starts on 18 Apr; Mar CPI on 20 Apr; Mar industrial product price and Feb retail sales on 22 Apr;CFIB business barometer for Apr on 28 Apr and Feb GDP on 29 Apr.
- **Technical Analaysis:** USDCAD seems unable to break below the 1.2450 and has been swiveling around the 1.25-figure. Daily chart suggests some retracement. We think there could be some shor-term consolidation before USDCAD bears take the pair lower towards 1.24-figure.Weekly chart is bearish bias.

JPY: USDJPY Could Remain in Elevated Ranges in Interim

Forecast	2Q 2022	3Q 2022	4Q 2022	1Q 2023
USDJPY	120 (114)	120 (113)	118 (112)	117 (--)

Previous Forecasts in Parentheses

- **Motivation for the FX View:** USDJPY saw an exponential surge in March. The pair rose from around 115 in end-Feb to a high of 125, before u-turning lower. Interestingly, JPY's haven characteristic seems pale relative to USD in this episode of Russia-Ukraine conflict. When the conflict escalated in the first few weeks of March, markets saw a rush to dollars, and concerns on potential supply disruptions in oil markets from the crisis led to elevated energy prices, which in turn fed into incrementally hawkish Fed stances and higher UST yields, boosting the USDJPY pair. Other factors such as stubbornly dovish BoJ signalling, higher energy import burden, bullish Nikkei (negatively correlated with JPY), and bouts of short-covering in USDJPY etc., possibly contributed to USDJPY's recent surge too. Towards end-Mar though, signs of progress in Russia-Ukraine talks and concomitant moderation in oil prices seems to have blunted USDJPY's upward momentum. 125 is also known as the Kuroda line—Kuroda made comments in 2015 interpreted as defending the yen around the 125 mark—and could be a key resistance to watch. On net, we look for some relative stabilization in UST-JGB differentials in 2Q versus earlier rapid widening, and for broad dollar strength to see some near-term resilience, which could lead USDJPY to remain in elevated ranges (but less chance of spiking much higher past 125) in the interim. Global price pressures could still moderate later in 2H as energy inventories rebuild and supply chain disruptions ease. Alongside moderating dollar strength, USDJPY could see a gradual retracement lower later in the year.

- **Haven demand for JPY on Ukraine crisis was much more limited than expected, relative to dollar**. Russia-Ukraine tensions had escalated quickly in Feb-Mar, with Putin recognizing two self-proclaimed separatist regions in eastern Ukraine, and subsequently sending military forces into Ukraine. US and Europe had countered with various stricter-than-expected sanctions or restrictions on Russia in retaliation, including on Russian FIs, elites, Nord Stream 2, access to western financing, trade in high-tech exports etc. **In current episode of market turmoil, USD seems to be the preferred haven of choice given concerns over financial market contagion**. I.e., sanctions on Russian central bank, exclusion of some Russian lenders from SWIFT, and reallocation of assets out of Russia, have led to broad international demand for USD. This preference for USD versus JPY might have anchored part of USDJPY's surge in March. We note though, that the FRA-OIS spread has begun heading lower from 10 Mar (albeit still elevated versus Jan-Feb), indicating receding stresses in dollar money markets. **There are also tentative signs of progress in peace talks towards late March, and this could on net imply lower haven demand for USD going forward too, if subsequent geopolitical developments lean positive**.

- **Apart from the Ukraine crisis, Fed stance and UST-JGB yield differentials are likely to remain as key drivers of the USDJPY pair too**. In Mar, FoMC voted 8-1 to raise rate to 0.25% - 0.5%. Dot plot signalled another 6 more hikes this year (vs. their previous projection for 3 hikes). For 2023, Fed is now looking for about 3 – 4 more hikes and none for 2024. Powell told reporters that inflation is too high, labor market is over-heated and price stability is a "pre-condition" for Fed. While he noted that Ukraine war had highly uncertain implications for US economy that create near term upward pressure on inflation while weighing on economic activity, he played down the risk of recession and emphasized that US economy is "very strong". The FoMC was followed by a series of hawkish Fedspeaks from officials in recent weeks as well. For instance, Powell said that the Fed may need to raise rates more quickly than needed. It will take all “necessary steps” to contain inflation, even if that implies hiking in increments of >25bps. At last check, markets are now looking for around +200bps of rate increases from Fed by Dec, which implies at least 2 +50bps hikes at some point. This is in sharp contrast to BoJ’s dovish stance. As a result, 2Y UST-JGB yield differentials are last seen at around +240bps, versus +146bps in end-Feb. Nonetheless, the widening in yield differentials show signs of peaking, especially with Fed’s current expected terminal rate at below 2.5%.

- More broadly, the prospect of US interest rates rising for the next few years, while the BoJ remains committed to an easing stance, could help sustain relative demand for overseas investments (such as US treasuries). Demand from pension funds such as GPIF as well as private sector entities could be in play. **Such outflows could temper the extent of support that the JPY receives from an expected current account surplus**—consensus estimates see current account coming in at 2.1% of GDP in 2022 (versus 2.8% in 2021). Meanwhile, there are signs that the longer-term negative correlation between Nikkei and JPY remains somewhat intact. Any significant episodes of volatility in Japanese risk assets could still lend some support to the JPY.

- Admittedly, over the course of Feb-Mar, Japan’s energy importer status also likely meant drags on JPY on higher import costs amid elevated commodity prices. On energy outlook, even as interim supply disruption fears are keeping brent prices above the US$100-handle in late Mar, extent of oil price gains could be constrained going forward given (i) signs of positive developments in Russia-Ukraine peace talks, (ii) signs of interest in Russian oil from parts of Asia, including China, India and Indonesia (suggesting less disruption in global supplies), (iii) planned ramp-ups in OPEC+ supplies over time, and (iv) reports of US planning to release as much as 180mn barrels in reserves over the next several months (much higher than earlier release of 50mn barrels in Nov, 30mn in Mar). **This could translate to some moderation in global price pressures, conditional on pandemic-induced supply-side constraints starting to ease as well.** In such a scenario, UST yield and USDJPY upside risks could moderate somewhat.

- **Growth and Inflation Outlook:** 4Q (P) GDP came in at 5.4% q/q SAAR, seeing a turnaround from -2.7% prior but still mildly lower versus expected 6.0%. Private consumption growth came in at 2.7%q/q, slightly better than expected 2.3%. Business spending expanded at 0.4%q/q, on par with expected 0.5%.

- Latest macro indicators point to more mixed domestic growth momentum in 1Q 2022. PMI Mfg for March came in at 53.2 versus 52.7 prior. But services activity remains in contractionary territory at 48.7, despite improving from 44.2 prior. Feb retail sales came in at -0.8%y/y, versus expected -0.3%. Still, earlier BoJ projections seem to imply that the Omicron drag will be transient. In BoJ’s Jan projections release, **while FY2021 (runs till Mar 2022) growth was lowered to 2.8% from 3.4% (Oct projection), FY2022 growth was actually bumped up to 3.8% from 2.9% (Oct projection).**

- Headline inflation for Feb registered at 0.9%y/y versus 0.5% in Jan. The indicator excluding fresh food is still tame at 0.6%y/y while that excluding both fresh food and energy is still negative at -1.0%. Base effects and ongoing supply disruptions may still skew these readings to the upside in the coming months, possibly to around 2% from Apr onwards. In Jan, t**he BoJ raised slightly CPI (all items less fresh food) forecasts in FY2022-2023 (FY2022: 0.9% -> 1.1%; FY2023: 1.0% -> 1.1%).**

- **Monetary Policy Forecast:** BoJ left interest rates and asset purchases unchanged in its 18 Mar meeting, as expected, but revised down its economic assessment just two months after the prior upgrade. Covid and Russian invasion were cited as concerns for growth and prices. Authorities signalled that inflation could accelerate to around 2% from Apr onwards, but said that there's "absolutely no need" for the central bank to raise rates to react to cost-push inflation. **The bank's stance that a weaker yen was net positive for the overall economy also remained unchanged**.

- BoJ's Jan meeting minutes saw members emphasizing the importance of communication to explain that dovish policy was meant to achieve economic growth with steady wage increases, in addition to restoring stable inflation, and that the end of some pandemic measures should not be mixed up with reduction in monetary easing extent.

- It is more likely that fiscal measures will be deployed to assuage impact of rising costs (from weaker JPY, elevated energy prices) on households and importers, rather than utilizing monetary policy. BoJ is unlikely to veer from its earlier policy stance near-term. For instance, its announcements of unlimited bond buying of 10Y notes on Mar 29, 30 and 31, to cap 10Y yields at 0.25%, signaled its commitment to its ultra-dovish policy and led USDJPY to surge towards the 125-handle at one point (first time in 7 years). Notably though, the 125-handle resisted the upswing quite decisively, and the USDJPY pair is significantly lower at last seen. 125 is also known as the Kuroda line—Kuroda made comments in 2015 interpreted as defending the yen around the 125 mark.

- **While significant shifts in BoJ's dovish stance is unlikely, we do not rule out verbal intervention of minor YCC tweaks**. Japan's energy importers are warning that recent fall in JPY is exacerbating a surge in fuel costs, and may weigh on their margins while raising prices for consumers. If the perceived harm to the economy from falling JPY becomes larger, BoJ may be forced to "talk" up the value of the yen to slow the currency's slide, and wider two-way swings might be seen in the pair, as opposed to the one-way surge higher earlier.

- **Latest Fiscal & External Balance Outlook:** In Feb 2022, **a parliamentary committee approved a record JPY107.6trn (US$936bn) spending plan for FY2022 (starting Apr)**. Kishida has vowed seamless spending for 16 months (beginning with supplementary budget mentioned above) to provide sufficient support to lift the economy from Covid-induced doldrums. Consensus forecasts see the fiscal deficit coming in at around -6.5% of GDP in 2022, on par with the

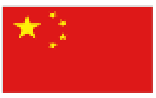
-6.4% seen in 2021, and still wider than the -3.2% average seen in 2015-2019 (pre-Covid).

- To counter the impact of rising energy costs on the domestic economy, PM Kishida has rolled out JPY360bn in measures in March. The government currently pays oil refiners a subsidy of JPY18.6 per liter of gasoline, up from an earlier JPY5 subsidy offered since Jan. At last check, the subsidy program will be extended to end of April. Additional measures might be forthcoming, including subsidies or handouts for households to help pay for higher food bills.

- Current account for Jan came in at a deficit of -JPY1189bn, widening from -JPY371bn prior. Feb exports grew by 19.1%y/y (versus expected 20.6%), while imports growth surprised to the upside at 34.0% (versus expected 26.4%). As a result, trade deficit came in at -JPY668bn, wider versus expected -JPY150bn, but narrowing from -JPY2199bn prior. We note that the trade balance has seen deficit readings from Aug 2021 to Feb 2022, versus average surplus outturns in the first 7 months of 2021. **Such developments could weigh on the current account in the interim.**

- **Key domestic events and issues to watch:** 1Q Tankan Surveys (1 Apr); Mar Vehicle sales (1 Apr); Feb Labor cash earnings (5 Apr); Feb (P) Leading Index CI (7 Apr); Feb Current Account (8 Apr); Mar (P) Machine tool orders (11 Apr); Feb Core machine orders (13 Apr); Mar Trade (20 Apr); Mar CPI (22 Apr); Apr (P) Jibun Bank PMIs (22 Apr); Mar Jobless rate (26 Apr); Mar (P) Industrial production (28 Apr); Mar Retail sales (28 Apr); BoJ Policy decision and revised outlook (28 Apr).

- **Technical Outlook:** USDJPY pair was last seen around mid-122. RSI remains near overbought territory, while bullish momentum in pair shows signs of moderating. Key resistance remains at 125, which rejected an earlier spike in March. Support at 120.65 (38.2% fibo retracement from Jan low to Mar high), 119.30 (50.0% fibo), 117.90 (61.8% fibo). Volatile, wide swings could still be possible between 120 and 125 in the interim, but we prefer to sell rallies towards 125.



RMB: More Two-way Risks Now

Forecast	2Q 2022	3Q 2022	4Q 2022	1Q 2023
USDCNY	**6.35** (6.33)	**6.33** (6.32)	**6.32** (6.30)	**6.30** **(--)**
USDCNH	**6.35** (-6.33)	**6.33** (6.32)	**6.32** (6.30)	**6.30** **(--)**

Previous Forecasts in Parentheses

- **Motivation for the FX View:** USDCNY ended Mar at 6.34 (close to our 1Q forecast of 6.35) after a rather volatile month. China manages an increasingly challenging juggle of dynamic zero-covid strategy, monetary policy prudence and keeping the economy afloat. Granted, there had been plenty of supportive property measures implemented by respective local governments but those have not translated to improvement in data. Signs of capital outflows in Feb unnerved investors and the perception of the CNY is no longer that of a impervious one (as flagged in our FX Annual Outlook 2022). Moves of the USDCNY as well as the CNY TWI suggest that the best of CNY days might have passed and we are looking at a more volatile currency now with carry advantage rapidly eroded by narrowing yield differentials. That said, there are still structural underpinnings including (1) strong current account surplus, (2) bond-related passive inflows due to WGBI inclusion. We still hold a bearish view on the USDCNY towards 6.30 (12-month view) but appreciation rate will be slow with the pair now facing more two-way risks. The recent spike above 6.3861 (USDCNY) coincided with the sell-off in equities that also prompted top officials to pledge more growth support as well as to instill confidence in China's capital markets. **That gives credence to our long held view that USDCNY could remain within the 6.30-6.40 range as this is the zone that the authorities feel comfortable for the USDCNY to trade in for much of this year, barring drastic moves in the greenback.**
- While the COVID-19 omicron variant is cast into the rearview mirror for most of the world, China is still struggling to straddle between dynamic zero-covid strategy and growth by the use of "bubbles" to ensure production of key manufacturing companies could continue. Our expectations for demand recovery to broaden in the rest of the world especially within Asia where vaccination rates have caught up have played out to some extent, notwithstanding impact of rising energy prices. **In a growth environment, even as we remain constructive on the CNY against the countercyclical USD, we are more negative on the CNY on a trade weighted basis as we expect China assets to become less attractive relative to regional peers and that has played out to some extent.**
- Recall that our risks to our view include a lack of recovery in the housing market that can precipitate into an economic hard landing or a credit crisis - With the Chinese authorities so unwilling to let go of dynamic zero-Covid policy and the three red lines for property developers, there is a chance that growth recovery could be slower than desired and PBoC is forced to ease monetary policy more aggressively. An absence of inflation at home and a runaway inflation in the US could even force Fed to be more aggressive in tightening. That could drastically narrow (or even invert) the US-CH yield differentials and at that point, fears of hard landing could dampen CNY sentiments further and spur the currency into a more dramatic tailspin. To some extent, these risks seem to have increased, skewing risks to the upside to our forecasts.
- **Growth and Inflation Outlook: GDP target for 2022 is set around 5.5%, a tad firmer than most estimates (IMF at 4.8%, median estimate of private analysts polled by BBG at 5.2%). Since the two sessions, there have been plenty of pledges to support growth. Premier Li Keqiang also acknowledged some challenge in meeting the 5.5% growth target. This suggests a fair amount of policy supports is needed to achieve this level of output and activity.**

- Vice Premier Liu He made a somewhat overdue appearance at the special meeting of the Financial Stability and Development Committee (FSDC) on 16 Mar. There were a few key points made at the meeting including:

    • more “policies that benefit markets”,

    • to support overseas share listings,

    • to have a good discussion with the US authorities on ADRs,

    • to “complete rectification work on large platform companies via standardized, transparent and predictable supervision”.

    • there was also mention of having “proactive monetary policy” to support the economy in 1Q.

- Contraction in Mar PMI numbers and persistent decline in housing prices suggest further deterioration in demand conditions. China’s lockdown measures especially in Shanghai that started in the last week of Mar could see further extensions as infections continue to rise relentlessly. Growth is likely to be compromised further as a result with consumption taking the brunt. TSMC Head noted that the demand for consumer electronics including smartphones, PCs and TVs have been adversely affected since the lockdowns. Based on the latest survey by the central bank, business confidence has fallen with export orders down to just 40.9 for 1Q vs. 48.7 in quarter prior. Domestic orders have also fallen to 41.4 from 51.2. Profitability declined to 49.3 from 57.4. Households are also turning cautious. In a separate survey, 37% of respondents had a negative view of the hiring sentiment and more than of them prefer to save money.

- **Monetary Policy Forecast**: Loan prime rates were left unchanged - 1Y at 3.70% and 5Y at 4.60%. This follows the 1Y MLF rate which was also kept steady at 2.85% last week, contrary to market’s expectations for a MLF cut on 15 Mar including our own. We expect 1Y MLF to be lowered 10bps and RRR to be lowered 50bps within 1H 2022.

- As we near the end of 1Q, rate adjustments have taken a pause for two months. In so far, we have more sporadic and targeted supportive property measures implemented at the local government/city levels rather than broad measures for the country. There seems to be more reliance on government bond issuance for infrastructure endeavours in line with cross-cycle policy design. We think a policy rate action (MLF and RRR) should be provided within the 1H of 2022.

- **PBoC released its quarterly monetary policy statement for 1Q on 30 Mar, vowing to step up magnitude of monetary policy and ensure that policies are forward-looking, targeted and autonomous. The central bank also wants to “further unclog policy transmission”, acknowledging that credit support has not been uneven and adequate and growth has faced “supply shock, slower demand and weakening expectations”, a repeated reference to the “triple pressure”. There was also an announcement to expand relending to support small and agricultural businesses and ensure the proper use of the financial support for small-and micro-sized firms.**

- **Latest Fiscal and External Balance Outlook:** Fiscal deficit target for 2022 is lowered to 2.8% of GDP, down from 3.2%, underscoring a stance of fiscal consolidation. The key word for 2022 seems to be frontloading and overall fiscal stance could remain neutral. Current account surplus for 4Q 2021 came in at $118.4bn vs. previous at $82.6bn.

- **Key domestic events and issues to watch:** Caixin Composite and Services PMI for Mar are due on 6 Apr; foreign reserves for Mar on Jul, credit data including aggregate financing, new yuan loans and money supply du e 9-15 Apr; PPI and CPI for Mar on 11 Apr; Mar trade on 13 Apr; MLF on 13-16 Apr; new home prices on 15 apr; Mar IP, retail sales, ex-rural FAI and 1Q GDP on 18 Apr; LPRs on 20 Apr; SWIFT Global Payment for Mar on 21 Apr; FX Net settlement on behalf of clients on 22 Apr, Mar industrial profits on 27 Apr, caixin Mfg PMI for Apr on 29 Apr, NBS Composite, Mfg, Non-Mfg PMI on 30 Apr.
- **Technical Analysis (USDCNH):** Despite the volatility seen in Mar, this pair seems to remain constrained within the 6.30-6.40 range. A falling wedge has formed but it is still far from the apex which could come in 2023. In the meantime, support at 6.35 (50-dma) before the next at 6.3309 (76.4% fibo retracement fo the Feb-Mar rally). Resistance at 6.3710.

KRW: Room for Recovery

Forecast	2Q 2022	3Q 2022	4Q 2022	1Q 2023
USDKRW	**1190** (1180)	**1180** (1160)	**1160** (1140)	**1150** (--)

Previous Forecasts in Parenthesis

- **Motivations for the FX View:** The weakening in KRW to 1244 (vs. USD) earlier this month was well within our expectations as we cautioned that the risk of long drawn military conflict between Russia and Ukraine could zap risk appetite, lead to higher oil prices (hurt oil importer such as KRW) and exacerbate inflation concerns. We also highlighted that the risk of faster Fed could add to USD strength (which turned out that the Fed did make another hawkish shift at the FoMC) while Korean Presidential election uncertainty may pose some downside risks to KRW (especially if Yoon is chosen due to foreign policy bias). All of these risks highlighted materialized and marginally overshoot our USDKRW resistance at 1240. Since peaking at 1244, KRW has recovered by 2.7% to 1210 levels (spot close 30 Mar). **We see room for KRW to extend its recovery from here (spt ref 1215) towards 1180/90 levels in coming weeks** on the back of: (1) tentative signs of progress on peace talks may suggest that war fears may have peaked for now; (2) and oil prices easing off from highs to provide breather for net oil importer FX; (3) hawkish Fed somewhat in the price while hawkish BoK may mitigate; (4) relative stabilization in Chinese equities after China pledged to keep its capital markets stable; (5) drawing experience from past military conflicts that weakness in high-beta KRW typically do not last and tends to reverse after a few weeks. **That said, we do not expect one way move given KRW being highly sensitive to market developments especially when war in Ukraine is still raging on. Tentative progress in peace talks does not mean that war is over and** some scepticism remains over Russia's offer to de-escalate. Geopolitical situation will remain fluid and risks are 2-way for markets. increasing downside risks to global growth, especially with the war in Ukraine persisting may hamper sentiment and get in the way of KRW's recovery. In addition, the case of Fed increasingly becoming more hawkish is one risk that may continue to provide that intermittent support for USD. We are however cautious on 2 potential domestic development: (1) Yoon coming in as the next President in May as his foreign policy leaning could reignite geopolitical tensions with China; (2) new BoK Governor Rhee (yet to be confirmed) that may turn out to be less hawkish. These new developments are worth monitoring and may pose fresh downside risks to KRW.

- We calibrate USDKRW forecast levels slightly higher to account for potential geopolitical risks (Korea peninsula as well as China-Korea relations) and potential global growth risks due to war in Ukraine persisting. That said we hold to our downward trajectory for USDKRW underpinned by (1) metaverse thematic lending a boost to memory chip cycle. This should support capex, exports and see foreign equity inflows return; (2) sound macro fundamentals at home; (3) BoK tightening cycle; (4) proxy play to ride the global reopening story; (5) potential inclusion to MSCI pending announcement in Jun - to attract re-rating foreign flows.

- **Potential MSCI Inclusion, Clean Energy and Metaverse thematics are Positives for KRW.** Memory chips are a key component in the metaverse world, in which users interact with each other in digital worlds. And Korea accounts for >70% of global DRAM memory market share. The **current downcycle in memory chip market could reverse when the world races to adopt metaverse technology**. Samsung has indicated that the widely expected downturn in memory market is unlikely to be as severe as precious episodes while SK Hynix said that supply flexibility has changed from the past as chip suppliers are managing capacity with demand. Potential bottoming in the sector and pick-up thereafter could see foreign inflow of funds again and this should bode well for KRW. Elsewhere as the world embark on their transition to clean energy. Korea also has a part to play in global supply chain via battery (LG Energy) and electric vehicles (Hyundai Motor). Potential MSCI inclusion of Korean equities (May/jun review) may also bring about foreign inflows as global fund managers rebalance their portfolios. This can be a potential positive for KRW.

    - **Efforts Taken to Increase Foreign Accessibility to Onshore Markets.** The government is currently considering whether to allow greater foreign participation in KRW onshore forwards and swap markets. Earlier the government also announced extension of trading hours for onshore spot and eased restrictions against overseas investors to encourage foreign participation. These efforts (current still under consideration) could help with satisfying some of MSCI inclusion criteria.

- **Geopolitical tensions between China and Korea may be brewing.** South Korea helds its Presidential election 9th Mar and the outcome saw Opposition Yoon emerging as a President. He is a political novice but is widely known for his previous role as a prosecutor-general in investigating corruption scandals, scandals including the case with former President Park Guen-hye. We reiterate that his victory may undermine KRW due to foreign policy bias that leans towards resetting China ties. He had indicated plans to buy an additional Terminal High Altitude Area Defense (THAAD) anti-missile system. This may be a concern for KRW and markets as this risks retaliation from China. Recall that China-Korea relations deteriorated in 3Q 2016 over US-Korea alliance decision to deploy a US THAAD to defend against North Korea missile threat. In response, Beijing then used economic coercion, among other levers, to try to force Seoul to abandon the THAAD deployment (but failed).

- **New BoK Governor Likely to Continue with Rate Hike Cycle but May Be Less Hawkish.** IMF Director Rhee Changyong has been nominated as the next BoK Governor pending parliamentary hearing, confirmation. It is not clear at this point if he will make it in time for 14th Apr MPC. Elsewhere new President Yoon takes office in May and he is perceived to favor policies aimed at boosting corporate activity and free market. This may present some risks that new BoK Governor may be less hawkish if both Governor and President were to work hand in hand in coordinating policies. Rhee's last comments to reporters - *that external risks, such as the U.S. credit tightening and Russia-Ukraine war pose risks to the Korean economy, adding that he will seek to conduct monetary policy in a balanced manner by taking into consideration growth, inflation and financial stability.* - may suggest that his policy stance may be more balanced. Nevertheless, with inflation still running red hot in Korea, a move to tighten possibly in May could still be on the cards.

- **Risks to outlook include** (1) a much faster pace of Fed tightening; (2) variant evolution proving more fatal than past strains resulting in fresh lockdowns, delayed reopenings; (3) another round of sharp increases in oil prices as KRW is highly sensitive to market moves and is a net oil importer. Highly sensitive KRW could succumb to sell-off in the above risk-off scenarios.

- **Growth and Inflation Outlook:** The recently concluded IMF Article IV projected Korea's growth to come in at 3%. It also noted that *comprehensive policy response, which, along with strong economic fundamentals, has underpinned a remarkable post-pandemic recovery and limited long-term scarring. However, uncertainty surrounding the outlook is high, linked to global and COVID-related risks.* At home, the MoF sees the economy expanding 3.1% in 2022, following a 4% growth in 2021. Forward looking surveys suggest that underlying growth, activity momentum should still remain intact. For instance, manufacturing PMI inched higher to 53.8 in Feb, up from 52.8 in Jan. Peak in omicron wave and subsequent relaxation of restrictive measures may support confidence and activity.

- Taking stock, **4Q GDP saw a sequential pick up to 1.2% q/q,** up from 0.3% in 3Q. On y/y terms, preliminary 4Q GDP was revised higher to

4.2% y/y (vs. 4.1% per advanced estimates) Improvement was broad-based but most notably, private consumption rebounded sharply. Investments also jumped, thanks to expansion in construction investment while government expenditure also rose on increased spending on goods and healthcare benefits.

- **Korea CPI continued to rise further to 3.7% y/y for Feb,** up from 3.6% y/y in Jan. Higher cost of petroleum, outdoor dining and housing rentals were the main drivers of inflation. Headline CPI would be even higher if not for the fuel tax cut last year and extension of 20% tax cut in oil products by another 3 months to minimise impact of surging energy prics. This is also the 11th consecutive month of CPI staying above BoK's 2% target and was at around 10-year high. Core CPI accelerated to 3.2% y/y, up from 3% prior. BoK revised inflation outlook to decade high of 3.1% for 2022, up from its earlier projection of 2%. BoK expects headline CPI to stay high in mid-to-upper 3% range due to ongoing surge in oil prices, rise in prices of personal services and industrial products.

- **Monetary Policy Forecast**: We expect BoK to pause policy tightening cycle at the next MPC on 14 Apr as policymakers assess impact of its prior 75bps rate hike (in 3 MPCs since Aug-2021) and macro development such as war in Ukraine, global inflation, growth, etc. BoK previously said that it will monitor effects of rate hikes, covid-19 situation, GDP, inflation, financial imbalances and changes in other nations' monetary policies while deciding on timing of future rate hikes. The cumulative 75bps hike earlier can afford some time for policymakers as BoK is ahead of its peers in unwinding pandemic monetary stimulus. This window will also allow for new Governor (IMF Director Rhee Changyong has been nominated pending parliamentary hearing, confirmation and is not clear if he will make it in time for Apr MPC) to come onboard and assess the situation. We opined that the subsequent MPC on 26th May could see BoK resuming its rate hike cycle in attempt to arrest red hot inflation.

- There was no MPC in Mar. At the last MPC (24 Feb), BoK kept policy rate on hold at 1.25%, as widely expected. BoK now sees inflation hitting 3.1% this year (vs. 2% earlier projection). BOK also held to its view that economy would continue sound growth helped by recovery in private consumption and robust exports. The higher inflation for longer view and optimistic assessment of growth outlook reinforces our case for BoK to resume policy tightening in 2Q.

- **External Balance and Fiscal Outlook:** Current account surplus further narrowed to $1.81b in Jan, down from $6.06bn in Dec. The surplus in goods account declined sharply as imports of energy, including oil more than overwhelmed the strong exports. Nonetheless, this is the 21st consecutive month of current account surplus.

- Under the 2023 budget guidelines, the government plans to normalize COVID-19 related emergency spending to pre-pandemic levels and make efforts to secure fiscal space to support new policy goals by the incoming government. Spending plans should be drafted by end-may for the 2023 national budget. Taking stock, the Korean government had drawn up 7 rounds of supplementary budgets with record high national budget of KRW607.7tn (or US$496 billion) for 2022. In February, it created this year's first extra budget of KRW16.9tn to support merchants hit by the pandemic. As a result, Korea's national debt rose at a rapid pace and fiscal deficit widened. The national debt is forecast to reach KRW1,075.7tn this year, marking the first time that the debt would exceed the 1,000 trillion-won mark. Debt-to-GDP ratio is also expected to rise to a record high of 50.1 percent this year and the fiscal deficit is likely to reach 70.8 trillion won, equivalent to 3.3 percent of the GDP.

- **Key domestic data to watch:** S. Korea releases Mar trade, mfg PMI (1 Apr); Mar CPI (5 Apr); Feb current account (8 Apr); Feb unemployment rate (13 Apr); BOK MPC (14 Apr); 1st 20 days of exports, Mar PPI (21 Apr); 1Q GDP (26 Apr); Apr consumer confidence (27 Apr); May Business survey – mfg and services (28 Apr); Mar IP (29 Apr).

- **Technical Outlook:** USDKRW saw a sharp run-up in early part of Mar before partially retracing the move lower into end-Mar. Last seen at 1215 levels. Bearish momentum on daily chart intact though RSI shows signs of rising (but on a low conviction basis). Bullish trend channel formed aince Dec-2021 remains intact. We look for the pair to trade with in. Support at 1208 (50 DMA), 1198 (100 DMA, lower bound of trend channel) before 1187 (50% fibo retracement of 2020 high to low). Resistance at 1223 (21 DMA), 1232 before 1244 levels. Bias to lean against strength.

TWD: Tide Turning

Forecast	2Q 2022	3Q 2022	4Q 2022	1Q 2023
USDTWD	**28.40** (27.50)	**28.20** (27.80)	**28.00** (--)	**28.00** (--)

Previous Forecasts in Parenthesis

- **Motivations for the FX View: We revised TWD forecast lower for 2Q and 3Q but kept TWD projection firmer than current spot to reflect somewhat constructive bias.** While global demand for tech needs could still underpin TWD strength, we hold to our bias that unlike in 2021, TWD is not likely to outpeform peers this year. Some negatives that could weigh on TWD include (1) Its zero covid strategy - a laggard in reopening/ hindrance to full economic recovery; (2) tentative signs of slowing export orders a drag on twd and (3) though CBC tightened 25bps, it still lags on policy tightening (vs. hawkish Fed and peers in the region). Fed-CBC policy divergence could further undermine TWD; (4) elevated energy prices can undermine energy importers like TW while rising prices hurt household wallet; (5) potential supply chain disruptions (raw materials like neon gas for chip making) that may weigh on economic activities, exports.

- **Ukraine crisis can disrupt semiconductor production.** Ukraine produces about 50% of the world's supply of semiconductor-grade neon, a key component for lasers in chipmaking. Based on research from Techcet, The gas, a biproduct of Russian steel manufacturing, is purified in Ukraine. Russia is also the source of 35% of the palladium used in the United States. The metal is used in sensors and memory, among other applications. Companies that supply chipmakers with materials for semiconductor fabrication buy gases, including neon, palladium and C4F6, from Russia and Ukraine. Now with US sanctions on Russia and Russian-related firms as well as military conflict in Ukraine (affecting production), there could be shortage in supply and this could affect the semiconductor industry in general. We do note that based on various reports, semiconductor firms are saying that it has diversified sourcing for its supplies and stockpiles hence disruption may be kept at a minimal. We continue to watch this space as protracted war could affect supply chain and production.

- **Fed-CBC monetary policy divergence marginalizes TWD.** Recent comments made by Fed officials are starting to shift significantly, looking for much faster pace of policy normalisation, in terms of magnitude of rate hikes and trajectory. For instance, a handful of Fed officials including Bullard, Williams, Mester, Daly expressed support for 50bps hike while policy turning restrictive was also discussed. As of 30 Mar, markets are pricing in ~77% probability of 50bps Fed hike at the next meeting on May 4th and for fed fund rate to go to 2.4% by end-2022. this translates to >200bps hike this year alone. Though hawkish Fed expectations may already be in the price, we are cautious of Fed turning even more restrictive. This is one risk that is not fully priced and may well provide that intermittent upward pressure to UST yield and USD. On the other hand, CBC may not be as hawkish as the Fed. Fed-CBC policy divergence here could drive USDTWD higher for now.

- **Tech supercycle to keep TWD supported but linkage may ease.** While the ongoing shortage in the semiconductor world may gradually ease into later part of 2022 and as more production capacity comes onstream in 2023, the emergence of metaverse thematic in the medium term could potentially further drive tech demand for chips and this can pose upward pressure on prices of chips while at the same time inflow of foreign funds into metaverse thematic could accelerate, providing support for the likes of tech-proxy FX, including TWD. For Taiwan, apart from TSMC being the world's largest suppliers of semiconductor chips, there are also other electronic devices ODMs such as Quanta, Inventec that have the capability to ride the metaverse trend, in terms of layering the infrastructure and technology that enable devices to connect to the faster network (moving beyond 5G to 6G) to access the content. Looking forward, semiconductor supply-demand rebalancing with China and US ramping up production, adding to supply chain may help to address the demand-supply imbalances. Hence our view that markets could move to price a peak in demand-supply imbalance in 2022 and that the tech proxy linkages with TWD may ease, as such.

- **Growth and Inflation Outlook: Taiwan's official statistics bureau DGBAS cautioned that 2022 growth forecast may be lowered from its current projection of 4.42%. The agency cited the ongoing war (if it persists) in Ukraine as the main reason for possible adjustment.**

But the agency shows confidence that 2022 growth would remain above 4%. We see some signs of moderation in growth momentum, confidence. For instance, mfg PMI slipped to 54.3 (vs. 55.1) though it remains expansionary while monitoring indicator (similar to leading indicator) continued to decline since mid-2021. Consumer confidence also fell to 9-month low of 72.24 in Mar. Taking stock, Taiwan's economy grew at its fastest pace of 4.88% y/y in 4Q for the first time in over a decade. For in Mar 2021, GDP grew 6.3% y/y. Tech exports was the main driver of growth.

- Headline CPI rose 2.36% y/y in Feb, slower than the 2.84% y/y in Jan. This is the 7th consecutive month that CPI comes in above 2%-target. Food and transportation were the main drivers of higher inflation. Core inflation also rose at a slower pace of 1.65% y/y, down from 13y high of 2.42% in Jan. That said, ongoing military conflict in Ukraine could continue to keep commodity prices supported and that would feed through to higher CPI in coming months.

- **Monetary Policy Forecast: We expect CBC to raise rate again at the upcoming MPC on 16 Jun,** following its surprise early move to tighten at Mar meeting (by 25bps). Focus has shifted to curbing inflationary pressures, from supporting growth. Magnitude of rate hike may revert to its typical 12.5bps increase, instead of the 25bps seen at Mar meeting as some sectors of the economy (i.e. tourism, self-employed, etc.) still need support. We also opined that prospects of a faster Fed is one reason for CBC to tighten and It is likely that we could see Fed embark on 50bps hike as soon as at the May FoMC.

- At the last MPC (17 Mar), CBC surprised with a 25bps hike (vs. no hike expectations) to take policy rate to 1.375%. Decision was unanimous. CBC sees private consumption warming up. Raw material prices will affect inflation this year and that rate hike is helpful to contain inflation. Inflation forecast was raised to 2.37%, from 1.59%. Depuity Governor, Tzung-ta told lawmakers that interest rate hike was helpful to tame housing market. The aggressive move also saw TWD gained the most (in a day) since May 2021.

- **External and Fiscal Outlook: Current account surplus widened to US$32.19bn in 4Q,** from US$26.1bn in 3Q. Both goods and services surplus expanded. Trade was driven by demand for electronics used in digital transformation and emerging technology applications while services was due to rising freight rates mid container shortages and port congestion. For 2022, Taiwan's current account surplus climbed to a historic high of US$116.12bn. As of 4Q, Current account surplus stood at 14.95% of GDP. Taiwan's debt as % of GDP last stood at 35.2 while fiscal surplus was at 0.37% of GDP. Taiwan has a self-mandated cap of 40% of debt to GDP

- **Key domestic events and issues to watch:** Mar mfg PMI (1 Apr); Mar FX reserves (7 Apr); Mar CPI, trade (8 Apr); export orders (20 Apr); Mar industrial production (25 Apr); 1Q GDP (28 Apr).

- **Technical Outlook:** USDTWD had another round of sharp run-up in Mar. Last seen at 28.675 levels. Bullish momentum on daily chart is now fading while RSI easing from overbought conditions. Bearish divergence is also showing up on MACD and RSI. Correction lower ahead. Support at 28.50 (21 DMA), 28.35 (38.2% fibo retracement of 2022 low to high) and 28 levels (61.8% fibo). Resistance at 28.75, 28.86 levels.

SGD: MAS Apr Tightening Bias Lends Support

Forecast	2Q 2022	3Q 2022	4Q 2022	1Q 2023
USDSGD	1.3200 (--)	1.3100 (--)	1.3000 (--)	1.2900 (--)

No Change to Previous Forecasts

- **Motivation for the FX View:** The extent of sanctions on Russia and the degree of hawkish tilt by the Fed (on inflation risks) were more severe or aggressive than expected, and this likely provided some support to DXY (and USDSGD pair) from late Feb to mid-March. But to some extent, AxJ FX have been relatively resilient to this bout of US yield upswing, and late March saw some signs of positive progress in peace talks. Historically, if military conflict is short-lived, drags on AxJ FX tend to be reversed (on average) over several weeks or months. With regards to the macro impact of the Russia-Ukraine war, while cognizant of secondary growth drags on Asia via economic linkages with EU, this could remain manageable on net, particularly as China switches to a pro-growth stance to mitigate renewed Covid risks. Despite lingering uncertainties on the war, the SGD NEER has risen back to test the upper bound of the policy band again in late March. Domestically, further easing in Covid curbs, and expectations for another tightening move from MAS in mid-Apr (house view looks for re-centering to prevailing level), are providing support to the SGD as well. Comparing historical episodes of re-centering higher in policy mid-point, we think that USDSGD may move lower by up to 1% or more if a re-centering decision does materialize. We look for a move lower in USDSGD in 2Q, and subsequent gradual dips over time, particularly if pandemic drags remain contained. Historically, USD strength also tends to fade post the first Fed rate hike in each cycle.

- USDSGD pair surged from 1.3460 pre-Russian attack on 23 Feb towards interim peak of 1.3670 by mid-March, but further upswings were visibly more hesitant by then. **As Russia-Ukraine induced volatility settles, broad shifts in USD will likely remain as a key driver of near-term moves in FX markets.** By our estimates, the SGD NEER basket has been trading near the upper bound of the policy band by late March. In this case, idiosyncractic SGD strength may be constrained prior to the next MAS policy move, and any down-move in USDSGD will require broader dollar softness to set in.
    - For the dollar, some intermittent near-term support could come from potential downside risks to growth—severe sanctions by

West on Russia could still lead to drags on European growth, even if some ceasefire comes to pass in the coming days or weeks. Fed turning more hawkish in recent days is also a significant risk to consider. FoMC voted 8-1 to raise rate to 0.25% - 0.5% in March. Dots plot signalled another 6 more hikes this year (vs. their previous projection for 3 hikes). For 2023, Fed is now looking for about 3 – 4 more hikes and none for 2024. The hawkish-tilt March FoMC was followed by a series of hawkish Fedspeaks from officials in recent weeks as well. At last check, markets are now looking for around +200bps of rate increases from Fed by Dec, which implies at least 2 +50bps hikes at some point.

— But to some extent, our over-arching view for now continues to call for USD nearing its peak, barring any further escalation in geo-political tension or any further surprises in Fed tightening bias. The 100-handle could remain a strong resistance for the DXY. **Despite the aggressive hawkish shift in Fed signalling via dots plot and Fedspeaks, and concomitant surge in UST yields, AxJ FX have weathered the Fed normalization messaging relatively well** and most AxJ FX have not seen significant drags post-FoMC.

- Towards late March, negotiators from Russia and Ukraine had their first in-person meeting in Istanbul. We saw Russia offering to scale down its military operations in northern Ukraine. Ukraine offered to turn neutral (not forming military alliance with other countries and give up its NATO ambition) in exchange for legally binding security guarantees from Western countries. Though broad headlines on the conflict remain two-way, there are still hopes that a diplomatic compromise might be forged in the coming weeks or months. **Recent market behavior suggests that any further positive developments in the conflict could lead AxJ FX, including SGD, to tilt towards cautious optimism on net.** Risk is if further rounds of sanctions/counter-sanctions structurally worsens West-Russian relations, and risking larger drags on European growth, which could then spillover to Asia to some extent. The EU accounts for a substantial 9% of ASEAN exports, and more than 11% for Vietnam and the Philippines. FDI from the EU makes up 11% of ASEAN FDI inflows.

- **Domestically, latest round of policy announcements reflect a commitment to Covid-endemic stance from authorities**. 7-day average in Covid cases has fallen from around 18k at the start of March to around 6-7k as of late-March. Weekly infection rate already showed signs of dipping below 1 at the start of March and was last seen at around 0.66, suggesting that the latest Covid wave can be contained. More importantly, PM Lee's announcement in late March also saw many Covid-related restrictions being eased, with group sizes doubled to 10, masks made optional outdoors and most restrictions lifted for fully vaccinated visitors. Easing in Covid restrictions could continue to support SGD sentiments.

- **Negative contagion from China growth moderation concerns to SGD remains mild at this point**. Rather, some relative stability in the yuan could actually impart relative resilience to regional FX such as SGD. On a basket basis, the yuan continues to be supported by strong current account surplus. While ongoing Covid wave in China and concomitant partial lockdowns need to be monitored, President Xi had said that China will "strive to achieve the greatest prevention and control effect with the smallest cost", and this seems to be bringing to fruition our separate call that China could be more adaptive in their Covid control measures as consumption is sluggish. In a bid to support markets after deep sell-offs, authorities also released a key statement pledging to introduce more "policies that benefit markets", to support overseas share listings, to have a good discussion with the US authorities on ADRs, to "complete rectification work on large platform companies via standardized, transparent and predictable supervision", and to utilize "proactive monetary policy" to support the economy. Rising Fed-PBoC policy divergence is a risk to watch for, but large spillovers to AxJ FX are unlikely at this point.

- **Growth and Inflation Outlook:** Final 4Q 2021 GDP growth (+6.1%) came in higher than advance estimate (+5.9%) but below our economist team's expectations (+6.5%) due to the downgrade in services growth.

- Our economist team expects 1Q flash GDP (out mid-April) to come in at around +4.5% (vs. +6.1% in 4Q21), with manufacturing leading growth, albeit at a slower pace compared to the past 6 quarters. Supply chain disruptions from China's flash lockdowns and slowing external demand amid the Russia-Ukraine war will likely have a more visible impact on Singapore's manufacturing and exports in March and the coming quarters.

- **Our economist team also sees 2022 GDP growth forecast at 2.8%** (versus prior projection of 3.8%, and below MTI's GDP forecast range of 3% to 5%) for 2022 on the back of lower global and EU growth, higher energy prices, manufacturing supply chain disruptions and a more aggressive Fed tightening policy. The reopening and relaxation of borders will help cushion the negative impact from weaker external demand, elevated oil prices and rising interest rates. Services and construction will be the main growth drivers this year, as manufacturing slows.

- Core CPI eased to +2.2%y/y in Feb (vs. 2.4% prior) on the back of softer food and services costs, while headline CPI (+4.3% versus 4.0% prior) was driven by surging COE prices and rising rental costs. **Our economist team maintains 2022 forecasts for headline CPI (+3.6%) and core CPI (+2.7%).** The Ukraine-Russia conflict drove both food and energy prices higher in March. Domestically, rising wage costs in a tighter labour market and stricter foreign worker measures will filter through to higher services prices.

- **Monetary Policy Forecast**: In mid-Oct, MAS kept the width of the policy band and the level at which it is centred unchanged, but raised slightly the slope of the SGD NEER policy band (est. 0.5%), from 0%. Subsequently on 25 Jan, in an off-cycle move, MAS raised "slightly" the slope of the SGD NEER band, while leaving the width and level at which it is centred unchanged. We estimate that the slope is now at 1.0% p.a.. The off-cycle decision was premised largely on rising inflation risks, with MAS citing "rapidly accumulating external and domestic cost pressures", amid "confluence of recovering global demand and persistent supply-side frictions".

- We think that the policy move should be largely seen as a reinforcement of the strategy that MAS has embarked on since last Oct, i.e., pre-emptively adjusting policy parameters in calibrated steps as assessment of inflation risks swing to the upside. We assessed in our earlier reports that SGD NEER could trade in the +1.5% to +2.0% above par range in the lead-up to the Apr policy decision, and this is coming to fruition now. By our estimates, SGD NEER has risen above the +1.5% level since 10 March, and has been testing the upper bound of the policy band in late March.

- **Our economist team expects the MAS to tighten again via a re-centering of the S$NEER band at the April meeting,** which will provide more room near term for the SGD NEER to appreciate and contain imported inflation. There may also be some chance for slope-steepening (current slope est. at 1.0% p.a.) although this is not our baseline. Comparing historical episodes of re-centering higher in policy mid-point, we think that USDSGD may move lower by up to 1% or more if a re-centering decision does materialize. Of course, the risk is if MAS pauses in tightening given earlier frontloading in slope-steepening (Oct, Jan), preferring to wait-and-see on global oil developments.

- As of writing, USDSGD is around 1.3560, and trades around +2.2% from the implied mid-point of 1.3873, with the top estimated at 1.3596 and the floor at 1.4151. Output gap is now expected to close in 2022, while core inflation is expected to creep higher still. Given these macro conditions, our Taylor rule estimates suggest that SGD NEER is likely to see a modest upward bias over the next few quarters.

- Domestic interest rates continued rising in March. The 3-month SOR (3MSOR) and 3-month SIBOR (3MSIBOR) are at 0.953% and 0.789% at the time of writing, higher than the 0.542% and 0.591% seen in end-Feb. While risks might be skewed modestly to the upside for rate moves, financial stability risks among households and corporates are likely to remain manageable. We expect the 3M SIBOR to rise to around 1.80% at end-4Q 2022.

- **Latest Fiscal and External Balance Outlook:** Finance Minister Lawrence Wong delivered the Budget on 18 Feb. Our economist team assesses that Budget FY2022 shores up finances to meet priorities for a post-pandemic future, including growing healthcare spending; expanding the social safety net; and transitioning to a green economy.

- Budget 2022 stays expansionary with a small deficit of $3bn (0.5% of GDP). There will be increases to the GST rate (7% to 9%), property taxes, personal income tax (for top earners), and carbon tax. Foreign worker policy will be tightened with the hike in minimum qualifying salaries for EP and S Pass holders. Notably, the GST rate increase from 7% to 9% will be conducted in two stages—one percentage point each time on 1 Jan 2023 and 1 Jan 2024. A $6.6bn Assurance Package will cushion the impact of the GST hike. The GST offset package includes cash payouts, GST vouchers, U-Save rebates, MediSave top-ups and CDC vouchers. The package will cover at least 5 years of additional GST expenses for a majority of Singaporean households, and 10 years for lower income households.

- Given the above, our economist team raises forecasts for average headline inflation to 1.8% (from 1.2%) in 2023 and core inflation to 2.1% (from 1.5%) in 2023 from the 1% GST hike. A 2% GST hike is expected to increase consumer prices by about 1.3% points over the relevant period. For 2022, forecasts for average headline inflation at 3.6% and core inflation at 2.7% are maintained. On net, forward-looking nature of policy-making could still nudge MAS to remain on a policy-tightening path, supportive of the SGD.

- The current account surplus improved to 18.1% of GDP in 4Q 2021, from 17.0% prior. A broad recovery trend has been observed since the trough in 4Q 2019. On higher-frequency indicators, we note that Feb NODX growth eased to +9.5% (vs. +17.6% in Jan), with both electronics (+11.6% vs. +14% in Jan) and non-electronics (+8.8% vs. +18.6% in Jan) cooling. Higher prices rather than volumes are supporting nominal export values. Real NODX (2018 prices) fell by -2.9% (vs. +2.9% in Jan), the first contraction since August 2021, reflecting manufacturing capacity limits and possibly supply disruptions. Our economist team maintains 2022 NODX growth forecast at 4%-6%, despite headwinds from the Russia-Ukraine war and China's flash lockdowns. **Resilient trade surpluses could help anchor SGD sentiments overall**.

- **Key domestic events and issues to watch**: Mar PMI (4 Apr); Feb Retail sales (5 Apr); 1Q (A) GDP (7-14 Apr); MAS Policy decision (11-15 Apr); Mar NoDX (18 Apr); Mar CPI (25 Apr); Mar Industrial production (26 Apr); 1Q Unemployment rate (28-29 Apr).

- **Technical Outlook**: USDSGD pair last seen at 1.3560, on par with levels seen end-Feb despite sentiment swings in March. On USDSGD daily chart, momentum is modestly bearish while RSI is not showing a clear bias. Risks for pair could be skewed modestly to the downside in the interim. Resistance at 1.3620 (23.6% fibo retracement from Feb low to Mar high), 1.3690 (Feb high). Support at 1.3520 (61.8% fibo), 1.3470 (76.4% fibo), 1.3410 (2022 low).

MYR: Mitigated by Oil and Economic Re-Opening

Forecast	2Q 2022	3Q 2022	4Q 2022	1Q2023
USDMYR	4.20 (4.15)	4.18 (4.12)	4.15 (4.10)	4.15 (--)

Previous Forecasts in Parentheses

- **Motivation for the FX View:** In the past month, the pair reached a peak of 4.2380 and a low of 4.1700 and despite the news of a more hawkish Fed and still ongoing Russia-Ukraine conflict, drags on MYR have been relatively contained, with buoyant oil prices providing offsetting support. The pair seems to have settled around the 4.20-4.22 range. Given our view of an extended USD support for the next few months we are revising our MYR forecasts slightly weaker in 2022 to reflect that. However, there could be possible upside risk to the MYR if the geo-political situation improves leading to an eventual softer USD environment, oil price and RMB stability, and on the domestic front, the move to an endemic scenario as current wave of Omicron cases likely eases will support domestic consumption driven growth. Continued Fed normalization could be a drag on, but likely not derail MYR recovery if a scenario of Fed miscommunication is avoided. We hence look for USD/MYR to trade largely ranged in the 4.20-4.25 over the remainder of 1H 2022 and in part 3Q 2022, before potentially dipping lower on net in 2H.

- **The relatively modest drags on MYR thus far from Russia-Ukraine developments could be due in part to the impact on oil markets from the conflict**. To some extent, concerns over potential supply disruptions have led Brent to swing higher. Given MYR's positive correlation with oil moves, this likely provided some offsets to sentiment drags.

- Given environment of Fed normalization, broader USD swings could account for a significant portion of USD-AxJ volatility in 2022. **There is a likely limit to the extent of dollar support from hawkish Fed**. Historically as seen in past 7 Fed rate hike cycles over the last 50 years, while 3-mth run-up to Fed's first rate hike is typically supportive of DXY strength, the DXY generally sees declines post-first Fed hike, i.e., -2% to 4% on average in a T + 90 trading days window as USD long positions unwind post-event risk. Another constraining factor is that the terminal rate of Fed policy could be lower this time round, possibly at 2.5% or lower, which could lead Asian risk assets to remain relatively in appeal over time. (A risk factor to this medium-term USD-negative view could be surprises in Fed quantitative tightening plans, if significantly more aggressive in pace than expected).

- In the near-term, the epidemiological trajectory still matters and the risk of emerging variants or rebound in cases can impinge on MYR recovery. Macro activity could recover more sustainably as curbs ease further over time. **Importantly, the government has vowed not to reimpose lockdowns amid a ramped-up COVID-19 inoculation programme**.

- On domestic politics, 3 governments in 3 years underscore political instability after the 14th General Election (GE) in May 2018. Current government holds a slim majority via a fragile coalition. Memorandum of Understanding (MOU) on Transformation and Political Stability signed on 13 Sep 2021 ("effective" until July 2022) with Pakatan Harapan bloc of the oppositions supposedly provides a temporary respite from politicking to focus on policies for economic recovery. But the fractious and fluid dynamics of domestic politics does raise the possibility of general elections in 2H 2022.

- **Elections and associated near-term uncertainties could induce higher vols for the USDMYR pair, but a sustained period of volatility and extended MYR losses is not our base case**. While the USDMYR pair did rise by >8% from 2Q to 4Q 2018 (last elections in May 2018), the bulk of this upswing can be attributed to broad dollar strength (DXY >+6%) and oil softness (oil > -20%) over the same period. Accounting for these two factors, the actual elections-induced impact on MYR is likely modest—the BIS-estimated MYR REER (real effective exchange rate basket) notably fell by a modest 1.5% over this period. To a large extent though, a scenario of contained MYR vols/losses on election uncertainty is conditional on there being clear signs of ability of (potential) next ruling party/coalition to maintain policy continuity and economic traction post Covid-recovery.

- **Growth and Inflation Outlook:** GDP rebounded +3.6%y/y in 4Q 2021 (3Q 2021: -4.5%) and +3.1% in 2021 (2020: -5.6%). But last year's real GDP was -2.7% below 2019 level. Sectors, consumer spending and investments remained sub-2019, except manufacturing and external trade thanks to global economic rebound as well as public consumption reflecting fiscal stimulus.

- **Our economist team maintains forecast of broad-based +6.0% growth in 2022**, underpinned by sustained economic opening as the Government proceeds with "Living with COVID-19" strategy and transitioning from the pandemic phase to the endemic stage of COVID-19. This is enabled by high primary vaccinations, rollouts of booster shots and inoculations of adolescent and children, which also prevented the healthcare system from being overwhelmed and suggest stronger immunity given the de-coupling between the Omicron-driven surge in COVID-19 cases and statistics on deaths as well as patients on ICU and ventilations. Progress in economic opening is further enhanced by the Government's plan to fully open the country's international borders on 1 Apr 2022. Where the Government is "tightening" as far as COVID-19 policy is concerned is on mandating booster shots to maintain full-vaccination status.

- CPI eased to +2.2% YoY in Feb 2022 (Jan 2022: +2.3% YoY) as diminishing base effect of transport cost offset higher food & non-alcoholic beverages (FNAB) cost. Core inflation inched up to +1.8% YoY (Jan 2022: +1.6% YoY; 2021: +0.7%) amid pent up discretionary spending and services demand following economic opening. The economics team maintain their 2022 inflation rate forecast at +2.7% (2021: +2.5%) but see upside risk from global energy commodity prices – especially crude oil - as well as elevated food-related commodity prices, including crude palm oil (CPO) price, and global supply chain disruptions in the wake of Russian invasion of Ukraine.

- Mitigations include the continued "blanket" fuel price subsidies so far; implementation of price administration and supply-side measures (e.g. freeze on base electricity tariffs for all electricity users in Peninsular Malaysia from 1 Feb 2022 until end-2024; introduction of subsidy to poultry farmers for chicken (MYR0.60/kg) and egg (MYR0.05/kg) production; allowing short term (Dec 2021-Feb 2022) importation of frozen whole chicken); as well as remaining slacks in the economy to contain demand-pull and wage-driven inflation.

- **Monetary Policy Forecast:** OPR kept at record-low 1.75% at the 2-3 March 2022 BNM's Monetary Policy Committee (MPC) meeting i.e. for the tenth consecutive MPC meeting and since July 2020. Monetary Policy Statement (MPS) acknowledged downsides from Ukraine-Russia military conflict. Maintain our call of unchanged OPR for much of 2022 before a +25bps rise in 4Q 2022 i.e. 2-3 Nov 2022 MPC meeting.

- BNM Annual Report 2021 was out on 30 Mar 2022, which comes with reviews of official 2022 macro forecasts.

- Overall, the key takeaway is that of continued outlook of firmer economic expansion this year given the marginal downward revision in real GDP growth forecast despite downside risks to growth as well as theexternal uncertainty caused by the Russia-Ukraine War. At the same time, the outlook of faster core inflation rate signals broader inflationary pressures amid pent-up domestic demand/spending from economic and international border openings as well as the pass-through effect of higher input costs following Russia-Ukraine War's risk premiums on commodity supplies and prices. Nevertheless, BNM still sees sizeable negative output gap remaining in 2022 at between -3.0%to -4.0% (2021: -6.0%; 2020: -6.8%) which BNM views as the key and lingering "slack" or "spare capacity" factor to contain the upside to core inflation rate.

- BNM also stated that monetary policy in 2022, first and foremost, will continue to support a sustainable economic recovery, while preserving price stability. BNM states that interest rate is not the best tool to deal with cost-push inflation e.g. surge in commodity prices due to geopolitical factors and prolonged supply-related disruptions, which is better addressed with price administration and supply-side measures. Current monetary policy stance is therefore appropriately accommodative. Still, BNM acknowledges the need to strike a balance between the need for continued monetary policy support to sustain the economic recovery momentum, and the risk of keeping low interest rate for too long that could lead to the emergence of financial imbalances. Going forward, BNM will ensure the degree of monetary policy accommodation is consistent with the expected firming of real GDP growth and moderate rise in inflation rate. Overall, this confirm the monetary policy normalization/tightening intention on BNM part. But BNM makes it clear that adjustments in monetary policy stance will be gradual and measured, indicating no US Fed-like aggressive interest rate hikes.

- Our economics team tweaked their view on the Overnight Policy Rate (OPR). For this year, we still expect a single +25bps hike to 2.00% p.a. on 2-3 Nov 2022 MPC. However, for 2023, we are now penciling in a total of +100bps hikes to 3.00% p.a. vs +50bps hikes to 2.50% previously. The change in our OPR view - especially for 2023 – reflect "catch up" on monetary policy normalisation as we factor the outlook of aggressive interest rate hikes by US Federal Reserve.

- **Fiscal and External Balance Outlook: Budget 2022 will likely see a third consecutive year of >6% budget deficit to GDP at 6.0% (2021E: 6.5%).** Meanwhile, Fiscal Outlook 2022 report indicates budget deficit to GDP ratio will go sub-5% from 2023 onwards (2023E: 4.8%; 2024: 4.3%) en-route to the 12th Malaysia Plan target of 3.0%-3.5% in 2025. **Trajectory of narrowing fiscal deficits, if maintained, should be net positive for medium-term MYR sentiments**.

- **Key domestic events and issues to watch:** Feb PMI Mfg (1 Apr); BNM Monetary policy decision (10/11 May); Foreign Reserves (7 & 25 Apr); Feb Industrial Production (11 Apr); Feb Trade (18 Apr); Mar CPI (22 Apr).
- **Technical Outlook:** USDMYR rose in early-Mar but gains were partially pared into end-month. Last seen at 4.21 levels. Daily momentum is flat though RSI rose. Risks slightly skewed to the upside. Resistance at 4.22, 4.2280, 4.2480 levels. Support at 4.2000, 4.19 (23.6% fibo retracement of 2022 low to high, 50 DMA), 4.1840 levels (200 DMA).

IDR: Resilience to War and Hawkish Fed

Forecast	2Q 2022	3Q 2022	4Q 2022	1Q 2023
USDIDR	**14,250** (14,100)	**14,200** (14,100)	**14,100** (14,000)	**14,100** (--)

Previous Forecasts in Parentheses

- **Motivation for the FX View:** Despite some intermittent support to the dollar from Russia-Ukraine uncertainties (including more severe than expected bout of sanctions by the West on Russia), as well as recent surge in UST yields triggered by incrementally hawkish Fed, USDIDR has not reacted excessively. Pair has been relatively stable, trading in between 14,260 to 14,410 over the last two months. To some extent, benign commodity prices as well as receding Covid-19 wave domestically could be helping to anchor IDR resilience. We adjust our USDIDR forecasts marginally higher, to take into account the aforementioned risk factors, but continue to look for a net gradual IDR recovery in the subsequent quarters, alongside phasing out of Omicron drags, easing of export restrictions, potentially positive developments in Russia-Ukraine conflict etc. We acknowledge that risks to our IDR forecasts could be to the downside (i.e., weaker IDR than we expect) if portfolio flow trends do not see a positive recovery or commodity prices see a more discernible downturn in the coming quarters.
- **Bout of market volatility triggered by Russian attack on Ukraine modestly dampened but did not derail IDR sentiments, with positive shock to commodity prices likely providing some offset**. Indonesia's top exports include palm oil, coal, copper and nickel. Despite signs of earlier price rallies moderating, most of these commodities continue to see elevated price ranges versus pre-Russian invasion. Benign commodity prices will likely sustain the trade surplus, which is net positive for IDR. Risk is if progress in peace talks and eventual easing in global supply disruptions lead to a more discernible downturn in commodity prices, but such dynamics are likely to take time, and will be mitigated to some extent by resilient demand from continued global reopening trends.

- **Recent adjustments to coal and palm oil export policy remain a concern near-term, but could ease over time**. To recap, an export ban on coal was implemented in Jan, to boost inventories at power plants and ensure energy sufficiency at home. Subsequently, coal miners compliant with new regulations on domestic market sales were cleared to restart shipments. Baseline assumption is for ban-induced drag on exports to ease over time as more firms comply with the regulations. With Russia and Ukraine accounting for about 80% of global sunflower oil exports, palm oil has risen in costs as buyers raced to find substitutes for sunflower oil. In a bid to cool domestic cooking oil prices, authorities first introduced domestic market obligation rules for crude palm oil (which required companies to direct 30% of exports to local markets), then replaced it with higher export duties (around US$675 a ton based on current prices, up from US$375) instead. Higher export duties tend to make it more profitable (on relative basis) to sell domestically rather than abroad. This is a modest near-term negative for trade surpluses, but likely manageable alongside elevated export prices still.

- **Recent rout in US treasuries triggered by hawkish Fed signalling via dots plot, Fedspeaks) likely impeded IDR recovery, but did not lead to large IDR losses as in earlier Fed tapering episodes.** IGB-UST 10Y yield differential narrowed from around interim high of 500bps in early Mar to interim low of around 420bps on 20 Mar, as UST yields spiked. But subsequently towards end-March, the treasury rout shows signs of easing and the differential has widened towards 440bps at last seen again. **On net, carry appeal of IGB assets might have moderated a tad and dampened IDR sentiments accordingly, but yield differentials likely remain sufficiently wide to avoid triggering a larger exodus of foreign funds**. On bond flows, we note that net outflows in March (-US$2376mn MTD as of 29 Mar) was modestly worse compared to outflows in Nov, Dec 2021, but with signs of treasury rout easing emerging towards late March, flows in the weeks ahead may reveal more reliable hints for trends in the months ahead. Outflows from bonds are also mitigated to some extent by inflows into IDR equities (US$530mn MTD as of 30 March).

- **In any case, extent of broad volatility spillovers from external risk events to IDR assets should be contained, given lower foreign holdings in Indo sovereign bonds, healthier current account balance, larger FX reserves, and lower inflation vs. earlier Fed tapering episodes**. House view looks for current account to come in at a modest deficit of 1.4% of GDP in 2022 compared to pre-pandemic period (deficit of above 2.5% of GDP). Foreign reserves came in at US$141.4bn in Feb, versus US$141.3bn prior, remaining near historical highs.

- On Covid, 7-day average in Covid-19 cases were seen at around 4k in end-March, versus interim highs near 56k on 20 Feb. On net, **authorities are largely sticking to a Covid-endemic and reopening policy stance.** Bali welcomed first foreign visitors under relaxed Covid rules in early March, with visitors no longer required to quarantine. The relaxation was subsequently extended to Bintan and Batam, and then to the whole of Indonesia on 21 March. Indonesia will also lift a ban on domestic travel during the Muslim holiday season of Eid al-Fitr in early May, after the annual tradition was banned for two years.

- **Growth and Inflation Outlook:** GDP growth firmed to +5% in 4Q as the easing of mobility restrictions drove a recovery in domestic demand and the global commodity boom kept the export engine roaring. For 2021 overall, GDP rose by +3.7%, reversing the -2.1% decline in 2020.
- On higher-frequency indicators, S&P Global PMI Mfg for Mar came in at 51.3 in March, on par with 51.2 in Feb. Feb retail sales growth eased to +14.5% (from 15.2% prior) as the Omicron wave saw cases jumping to record highs then, but we note that drags could ease with cases reverting to a downtrend since late Feb.
- **Our economist team trims 2022 GDP forecast slightly to +5.1% (from +5.4%)**, mainly on the back of a small downgrade in private consumption due to the Omicron wave in the first quarter. Our revised GDP growth forecast is at the mid-point of both the Finance Ministry (4.8% to 5.5%) and BI (4.7% to 5.5%) forecast ranges. Finance Minister Sri Mulyani commented that while the Russia-Ukraine conflict poses a threat to the recovery, Indonesia will be able to withstand the situation relatively well given its high trade surplus and foreign reserves, thanks to its position as a major commodity exporter.
- Headline CPI (+2.6%) rose to a near 2-year high in March, mainly driven by food prices as the government scrapped caps on cooking oil prices. Pertamina finally raised the price of Pertamax (13% of total gasoline consumption) by around +38% to IDR12,500 from 1 April. Our economist team estimates that the fuel price hike will add around +0.3%pt to headline CPI, and **raise average headline CPI forecast to +3.7% (from +3.2%) in 202**2, to account for the increase in unsubsidized fuel prices and higher food prices.
- **Monetary Policy Forecast:** In its policy decision on 17 March, BI kept its policy rate unchanged as widely expected, to maintain IDR stability and control inflation, while supporting the economic recovery, which is facing risks from the Russia-Ukraine war. The reserve requirement ratio for banks had already been raised on 1 March from 3.5% to 5%, and is set to rise again to 6% in June and to 6.5% in September. With the Fed turning more hawkish, Governor Perry Warjiyo acknowledged that the Fed could deliver 6 more rate hikes this year after the +25bps hike overnight. He reiterated that BI will maintain its policy rate at 3.5% unless there are clear signs of inflation picking up significantly.
- **Our economist team maintains the view that the BI will raise its policy rate by +75bps this year, despite a more hawkish Fed**. BI can afford to be patient given that inflation remains soft and within its target range on the back of fuel subsidies, while IDR is supported by healthy external balance with rising commodity prices. Expect the first rate hike to be delivered in May or June.
- For the whole of 2021, BI purchased IDR358trn (2.1% of GDP) worth of government bonds to fund the budget deficit (which came in at 4.65% of GDP). Under the extended burden sharing agreement, BI will purchase IDR224trn (1.3% of GDP) in 2022.
- **Latest Fiscal and External Balance Outlook:** In Sep 2021, parliament proceeded to approve Jokowi's 2022 budget with a total spending of IDR2,714.2trn (US$190bn), a slight decrease from IDR2,750trn budget

for 2021. Government revenue is expected to rise discernibly, as both income tax and value-added tax (VAT) are projected to grow by more than +10% with the expansion of VAT collection and the normalization of growth. Fiscal deficit was estimated at 4.85% of GDP.

- In early Jan, it was estimated that Indonesia recorded a budget deficit of 4.65% of GDP for 2021, "far smaller" than initial estimates, according to FM Sri Mulyani. The government collected IDR2,003trn (US$140 billion) in revenues, while spending reached IDR2,787trn. Tax revenues were 19% higher than in 2020 and about 104% of the target. F**ollowing better than-expected revenue collections in 2021**, t**he 2022 fiscal deficit estimate was lowered to 4.3% of GDP.**

- Tax reforms in 2022, including a VAT hike and a tax amnesty program, could generate additional revenue of around 0.7% to 1.5% of GDP, helping the government meet its lower fiscal deficit target. **Signs of fiscal discipline can help mitigate drags on IDR from a return of current account surplus into modest deficit territory**. FM Sri Mulyani said in March that the VAT hike slated for Apr would still be implemented, despite rising consumer goods prices. She assured that the government would shield low-income groups from the impact of the hike via social aid programs.

- Exports picked up +35.2% in Feb as the coal export ban was relaxed, while imports eased to +25.4%, resulting in the trade surplus widening to US$3.8bn. Our economist team assesses that high commodity prices will likely sustain the trade surplus, as Indonesia's top exports include palm oil, coal, copper and nickel, and these commodities' prices remain in elevated trading ranges. **Our economist team estimates the current account deficit at -1.4% of GDP in 2022 (versus mild surplus of 0.3% of GDP in 2021),** as recovery in domestic consumption may lead to robust import demand.

- **Key domestic events and issues to watch**: Mar PMI Mfg (1 Apr); Mar CPI (1 Apr); Mar Foreign reserves (7 Apr); Mar Local auto sales (15-21 Apr); Mar Trade (18 Apr); BI Monetary policy decision (19 Apr).

- **Technical Outlook:** USDIDR last seen at 14,370. The pair largely saw ranged trading between 14,200 and 14,450 over the last few months. Momentum and RSI on daily chart are mildly bullish, but extent of upswings could be constrained near-term, with interim key resistance at Dec high of 14,450. Next resistance at 14,570 (2021 Jul high), before 14,640 (2021 Apr high). Support at 14,290 (38.2% fibo retracement from early Dec high to late Dec low), 14,190 (late-Dec low).

PHP: Moderation in Oil Needed for Sustained Recovery

Forecast	2Q 2022	3Q 2022	4Q 2022	1Q 2023
USDPHP	51.00 (--)	50.50 (--)	50.00 (--)	49.50 (--)

No Change to Previous Forecasts

- **Motivation for the FX View:** Despite heightened volatility in USDPHP in March, some triggers for the earlier upswing has unwound a tad and drivers underpinning PHP levels have not seen a fundamental shift. We keep our forecasts unchanged for now and monitor risk drivers. To recap, a more severe-than-expected bout of Western sanctions on Russia (global growth drags, money market stresses) and increasingly hawkish Fed buttressed broad dollar strength for most of the month. Meanwhile, expectations for disruptions to global energy markets pushed up oil prices and led to higher energy import bill for Philippines. Our original end-1Q forecast of 51.0 thus saw discernible upside risks, with the USDPHP pair seeing an interim peak of around 52.5 at one point. But towards end-March, markets seem to be pricing in some cautious optimism in the Russia-Ukraine conflict, after tentative signs of progress in peace talks. Dollar softened on net in the last week of March, oil prices are moderating (aided by news of another US crude reserves release) and USDPHP has slipped below the 52-handle decisively. Notably, domestic Covid risks are also easing, with 7-day average in new cases now numbering in the hundreds versus high of 35k in mid-Jan. Conditional on oil gains potentially seeing some moderation—on possible progress in diplomatic resolution to Russia-Ukraine war and OPEC+ supply hikes—PHP sentiments could see modest support over time. To some extent, despite intermittent aid for the dollar from ongoing drivers (war, Fed), our over-arching view for now continues to call for USD strength being somewhat limited in the interim. AxJ FX have weathered the latest bout of hawkish Fed messaging and accompanying spike in UST yields relatively well. This supports our base case for a modest dip in USDPHP in subsequent quarters.

- Brent surged from around mid-US$90s/bbl pre-Ukraine war to peak of near-US$140 on fears of disruption in Russian supplies in March. US and partial UK bans on Russian oil, "self-sanctioning" by oil traders etc., had likely exacerbating concerns over global oil shortages then. But there are opposing factors to consider. Key European countries such as Germany, Netherlands, Austria are against imposition of European bans on Russian oil imports (i..e, less chance of exacerbating energy crisis). Towards late March, US is also planning to release as much as 180 million barrels in crude reserves over the next six months. This is notably much larger than earlier planned releases (50mn barrels in Nov, 30mn in Mar). As a result, Brent has softened below US$110 as of writing. **The latest period of moderation in oil prices coincides with a recovery in PHP, with USDPHP falling below the 52-handle, which implies that the PHP-oil correlation might remain intact near-term.**

In this case, conditional on oil gains potentially see some moderation—on possible progress in diplomatic resolution to Russia-Ukraine war and OPEC+ supply hikes—PHP sentiments could see modest support over time.

- On Covid curbs, it was announced in late Feb that Metro Menila and 38 other areas will be downgraded to Alert level 1, starting 1 March. Under Alert Level 1, intrazonal and interzonal travel will be allowed. All establishments, persons, or activities are permitted to operate, work, or be done at full on-site capacity, provided that health standards are observed. Philippines also began reopening in Feb to foreign visitors who have been vaccinated and test negative for the virus. Tourists from about 150 nations were allowed to visit for the first time in nearly two years. Starting 1 Apr, submission of a negative lab-based ART test taken <24 hours pre-departure will also be accepted in place of the initial requirement of an RT-PCR test taken 48-hours prior to departure. With Covid risks largely contained, Health Secretary Duque said in mid-March that Philippines will likely remain under Alert level 1 until the end of President Duterte's term, or until end-June. **Easing Covid drags on the domestic economic should lend support to PHP on net**.

- Impact on PHP from remittances flows remains a factor to watch for, even as impact from this driver has been overshadowed by influence of oil and dollar moves recently. Overseas Filipino Workers Remittances (OFWR) grew by a slower +2.5%y/y in Jan 2022 (Dec 2021: +3.3%). Our economist team noted that OFWR's monthly y/y growth has been moving within +2.5% to +5.2% range since July 2021. For 2022, house view expects OFWR to register +4.2% growth to US$32.75b (BSP expects +4% growth). Caveat to OFWR outlook now is the impact of Russia-Ukraine war, especially if the conflict drags on Europe which accounts for 12% of 2021 OFWR versus a miniscule 0.008% share for Russia and Ukraine. Meanwhile, foreign reserves came in at US$108.0bn for Feb, versus $107.7bn prior, remaining near historical highs. **Resilient remittances and adequate reserves can still be supportive of PHP at the margin**.

- **May 2022 elections could be a volatility event**. Some level of policy uncertainty given the change in political regime could induce some caution in PHP in the lead-up to and during elections. Candidate Marcos currently hold an wide lead in polls (some estimates seeing him taking more than half of the votes), but details regarding his stances on various policy prongs are still lacking for now.

- **House view is for the series of legislative reforms introduced by the Duterte government to boost Philippines' long term economic competitiveness**. Beginning with the Tax Reform for Acceleration and Inclusion Act (TRAIN) in 2018 (implemented in stages), recent reforms in place included Corporate Recovery and Tax Incentives for Enterprises (CREATE), Financial Institutions Strategic Transfer (FIST) and Retail Trade Liberalisation Act (RTL). Latest amendments to the Public Service Act (PSA) will lift foreign ownership restrictions on all public services that are not public utilities, and possibly accelerate capital formation. Sectors impacted include air transport, telecoms, toll roads, and rail and shipping. These reforms are expected to act as catalysts to boost private investment including FDI and thus economic growth.

- **Growth and Inflation Outlook:** Philippines' real GDP growth picked up to +7.7%y/y in 4Q (3Q 2021: +6.9%), resulting in full year 2021 growth of +5.6%, in line with our economist team's +5.5% estimate. Except for agriculture, which posted marginal decline, all sectors of the economy recovered from the contraction in 2020. The decision to allow economic activities to operate with strict standard health protocols and procedures have mitigated the downsides to growth in 2Q-4Q 2021.

- On higher frequency indicators, PMI Mfg for Mar came in at 53.2 versus 52.8 prior, remaining relatively robust. Unemployment rate for Jan slipped to 6.4%, slightly lower than prior 6.6%.

- **House view for 2022 real GDP growth remains at +7.0%**. Domestic demand will continue to drive the recovery, as the economy progressively re-opens. At the current recovery momentum, the economy's quarterly real GDP value could return to pre-pandemic levels by the 3Q/4Q of this year.

- Headline monthly inflation rate was stable at +3.0%y/y in Feb (on par with 3.0% prior), which is at the center of BSP's target range of 2%-4%. Easing FNAB inflation on dissipating base effect was offset by the pick up in transport costs amid upward pressures on global crude oil prices. Our economist team maintains 2022 headline inflation rate forecast at +3.4% (2021: +3.9%).

- **Monetary Policy Forecast:** BSP kept policy interest rate at 2.00% at the second meeting of 2022 which has been unchanged since -25bps cut on 19 Nov 2020. It now expects inflation to breach the 2%-4% target in 2022 but to return within range in 2023. Monetary policy statement tilted to "hawkish" tone. I.e., Given the potential broadening of price pressures over the near term, BSP said it now stands ready to respond to the buildup in inflation pressures that can dis-anchor inflation expectations. Previously, BSP said it was prudent to maintain accommodative policy stance given a manageable inflation environment. **House view now looks for two +25bps hikes at end-3Q 2022 and end-4Q 2022 from one +25bps hike in 4Q 2022 previously**.

- Governor Diokno commented that raising the policy rate to between 2.5% to 2.75% as part of an exit from Covid stimulus would be "reasonable and consistent" with Philippines' macroeconomic targets. Normalization would likely start in 2H, but would be data dependent. A 2.75% key policy rate "might be reached by next year."

- **Latest Fiscal and External Balance Outlook:** The expansionary Budget 2022 of PHP5.024trn (signed by President Duterte in Dec 2021), which is +11.5% higher than Budget 2021, should help to maintain underlying economic recovery momentum.

- **There are early signs of increasing fiscal stresses.** Average monthly budget deficit from Jan 2021 to Feb 2022 is around PHP129bn, vs. the pre-pandemic monthly average of PHP55bn in 2019, reflective of the fiscal challenges associated with the pandemic. Last Jul, Fitch Ratings' maintained Philippines' credit rating at investment grade "BBB", but downgraded its outlook to "negative" from "stable", citing the impact of the prolonged pandemic. Comments also mentioned "downside risks to medium-term growth" as a result of potential scarring effects, and potential challenges from unwinding stimulus and "restoring sound public finances".

- Exports growth picked up to +8.9%y/y in Jan (Dec 2021: +7.3%), double-digit imports growth eased to +27.5%y/y (Dec 2021: +39.1%) and trade deficit narrowed to -US$4.7bn (Dec 2021: -US$5.3bn). On a related note, BSP raised its current account deficit forecast for 2022, from US$9.9bn to US$16.3bn, on import demand recovery and higher oil prices. **House view sees current account at deficit of 1.8% of GDP in 2022 versus 0.1% deficit pre-Covid average over 2015-19**.

- **Key domestic events and issues to watch:** Mar PMI Mfg (1 Apr); Mar CPI (5 Apr); Feb Unemployment rate (7 Apr); Mar Foreign reserves (7-15 Apr); Feb trade (8 Apr); Feb Overseas Remittances (14-17 Apr); Mar BoP Overall (18-23 Apr); Mar Budget balance (26 Apr).

- **Technical Outlook:** USDPHP last seen at 51.67, coming off rapidly from interim peak near 52.5 in mid-March. Momentum and RSI on daily chart are both bearish, suggesting that risks for pair could be skewed mildly to downside for now. Support at 51.50 (38.2% fibo retracement from Dec low to Mar high), 51.15 (50.0% fibo), 50.85 (61.8% fibo). Resistances at 51.85 (23.6% fibo), 52.50 (Mar high).

THB: Interim Drags from Elevated Oil, Hawkish Fed

Forecast	2Q 2022	3Q 2022	4Q 2022	1Q 2023
USDTHB	33.00 (32.00)	32.50 (32.00)	32.50 (31.70)	32.00 (--)

Previous Forecasts in Parentheses

- **Motivation for the FX View:** USDTHB pair remains elevated (versus Feb average) amid myriad concerns, including Russia-Ukraine war, China partial lockdowns, hawkish Fed signalling. Recent surge in UST yields has likely contributed towards foreign outflows from TH bonds in March, which has led to recent drags on the THB, but the pace of outflows shows signs of easing over the past two weeks. Equity inflows have also blunted the extent of drags from net bond outflows. More importantly, markets saw signs of moderation in oil prices towards end-March, on US release of strategic crude reserves and signs of progress in Russia-Ukraine talks, which is positive for THB via lower energy import bills. Developments have led USDTHB to retrace lower from interim highs near 33.8. Chance for sharp spikes in the pair (i.e., significant softening in THB) could be reduced, conditional on (i) no further hawkish surprises from Fed and (ii) no exacerbating in oil supply crunch. Current conditions could continue to see THB trading a tad on the backfoot, but conditional on an eventual diplomatic solution being found, we could see USDTHB revert to a slow dip in latter quarters.

- In early March, US banned Russian oil imports, matched in part by UK. We also note broad signs of "self-sanctioning", with reputational, financing, policy risks raising reluctance among traders in purchasing Russian crude. These developments likely exacerbated concerns over global oil shortages, and contributed to brent's surge towards a high of US$138/bbl at one point. **Period of up-moves in oil prices coincided with upswings in USDTHB, suggesting that concerns over Thailand's elevated energy import bills likely weighed heavily on THB sentiments.** A key concern by market watchers was whether EU would impose bans on energy imports from Russia too. According to reports, Baltic countries including Lithuania pushed for an embargo, while Germany, Austria and Netherlands look to be opposed to such moves for now. Latest reports suggest that while the EU would likely still avoid embargos at this point. Instead, it will be working with US to cut Europe's dependence on Russian energy over time.

- Towards end-March, we saw some reports of tentative positive developments in Russia-Ukraine conflict. More specifically, Russia said that it will reduce military operations near Kyiv and Chernihiv. While US expressed scepticism and others cautioned that Russia's move may just be a tactical repositioning of forces, there are hopes that strong Ukraine resistance and a weakening domestic economy would still lead to increased chances for Russia to agree to a ceasefire in the coming weeks. **Besides tentative hopes for progress in diplomatic resolution, end-Mar THB sentiments could also be aided by signs of renewed downturn in oil prices, following confirmation that US is planning to release as much as 180 million barrels in reserves over the next six months**. This is notably much larger than earlier planned releases (50mn barrels in Nov, 30mn in Mar).

- Domestic Covid cases have been on an upswing for most of Feb, but **there are tentative signs that Feb spike in Covid cases is taking a pause in March**. 7-day average in new daily cases is around 30k, only modestly higher versus March average. Initial Feb surge prompted authorities to raise Covid-19 alert to Level 4, with containment measures stepped up in high-risk areas. Still, extent of interim drags on sentiments could be contained given that no lockdowns are planned for now. >70% of the ~70mn population received at least 2 shots. Authorities released a roadmap for transitioning from pandemic status to endemic, potentially by July.

- Thailand's urgency in reopening stems from its reliance on tourism, which contributed about one-fifth of economic output before the pandemic. After an earlier suspension on Omicron concerns, the Thai government lifted the suspension of "Test and Go" from 1 Feb 2022, which means re-implementation of quarantine-free travel for foreign visitors. In early March, THB saw a boost from a DJ report regarding a potential shift in China's zero-Covid strategy—including the use of travel bubbles, exploration of new antiviral drugs. But details were lacking and calibration of Covid strategy does not imply a near-term return of Chinese tourists to Thailand. Latest projections from the Tourism Council of Thailand see around 5.6mn tourist arrivals in 2022 (does not include return of Chinese tourists), still a far cry from the 40mn arrivals in 2019. **But while reopening plans may not lead to a sharp recovery in tourist numbers initially, it could also help anchor**

some confidence in THB assets. Despite recent geopolitical concerns, we note net inflows into TH equities around +US$1006mn in Mar (MTD as of 31 Mar).

- **Another key market mover in March was an increasingly hawkish Fed**. FoMC voted 8-1 to raise rate to 0.25% - 0.5% in March. Dots plot signalled another 6 more hikes this year (vs. their previous projection for 3 hikes). For 2023, Fed is now looking for about 3 – 4 more hikes and none for 2024. The hawkish-tilt March FoMC was followed by a series of hawkish Fedspeaks from officials in recent weeks as well. At last check, markets are now looking for around +200bps of rate increases from Fed by Dec, which implies at least 2 +50bps hikes at some point. But to some extent, our over-arching view for now continues to call for USD nearing its peak, barring any further escalation in geo-political tension or any further surprises in Fed tightening bias. The 100-handle could remain a strong resistance for the DXY. Despite surge in treasury yields from hawkish Fed signalling, **dollar strength is only more discernible towards yield-sensitive JPY and most USD-AxJ pairs are seeing two-way swings instead**. This suggests that AxJ FX could be more resilient to this round of Fed policy normalization. For THB, trends in bond flows might be an indicator to watch. While net outflows was seen for the month (US$2023mn MTD as of 31 Mar), we note that outflows had visibly slowed in the second half of the month.

- **Risks of early elections needs to be monitored**. With PM Prayut's popularity rating in decline and growing rifts in his Palang Pracharath Party (PPRP), there is growing speculation that an election (required to be held by 1Q 2023) may be brought forward to 2022. House view is for the PPRP to renominate Prayut, allowing him to stay in power until 2025. But in the case of an early election, we could see risks of delay in passage of Budget FY2023. If results are contentious, ensuing social unrest could dampen THB sentiments as well. During the 2013/14 political crisis, THB had experienced losses of more than 6% against USD at one point.

- **Growth and Inflation Outlook**: 4Q GDP rebounded by +1.9% as domestic demand recovered with the relaxation of Covid measures, while exports benefited from improving external demand and reopening of borders. For 2021 overall, real GDP rose by +1.6% (vs. -6.2% in 2020).

- Domestically, PMI Mfg came in at 51.8 for Mar, deteriorating slightly from 52.5 prior but still in expansionary territory. But alongside potential drags on global and EU growth from the Russia-Ukraine war, **our economist team has cut 2022 GDP forecast to +3.2% (from 4%)**. Drags could materialize via Thailand's manufacturing and exports. Tourism drags may also be a concern, as Russia accounts for 5.4% of tourism receipts (in 2019) – the third largest source after China and Malaysia, while the rest of Europe accounts for around 18%. Higher energy and food prices will likely increase inflation and weigh on consumer confidence.

- Headline CPI soared to +5.3% in Feb, the fastest pace since Sep 2008, on surging energy and food prices. This was partly due to a low base in utilities, as the government reduced electricity and water bills in Feb/Mar 2021 as part of Covid relief measures. **Our economist team raises 2022 average headline inflation forecast to +4.8% (from +2.9%)**

and core inflation to +2% (from +1.6%), due to higher than expected cost pass-through from producers to consumers. Both energy (12%) and raw food (21%) account for a significant share of the CPI basket. Retail diesel prices, which will be capped at THB30 (US$0.9) per liter until end April, are set to rise as the government will only subsidize 50% of any increase in prices from May.

- **Monetary Policy Forecast:** BoT kept its policy rate at 0.5% with a unanimous vote on 30 March, in line with expectations. The central bank cut its 2022 GDP growth forecast to +3.2% (from +3.4%), but expects the economic recovery to remain intact in 2022 and 2023 despite the impact from the Russia-Ukraine war, which has led to higher commodity prices and slower external demand. It hiked its headline inflation forecast to +4.9% (from +1.7%), mainly to account for rising energy and food prices, assessing that recent increases in inflation were primarily driven by cost-push factors, while demand-pull inflation pressures remained tame.

- **Our economist team maintains the view that BoT will deliver its first +25bps rate hike only in 4Q**, as it focuses on supporting the economic recovery. Raising the policy rate at this juncture will not tame inflation as costs are mainly driven by energy prices rather than core components. **The relative policy divergence between Fed and BoT could continue to weigh on THB sentiments to some extent**, and other factors, such broadly easing USD, or a more sustainable downward trajectory in oil prices, might be needed for any USDTHB down-moves to gain traction.

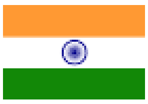
- **Latest Fiscal and External Balance Outlook**: Parliament earlier approved the budget for FY2022 (starting 1 Oct), which sees reduced spending on defence and education, and increased outlays on combating Covid fallout. The THB3.1trn (US$93bn) plan is 5.8% less than FY2021's, and estimates the budget deficit at THB700bn. In Oct, the cabinet approved a further THB92bn in relief measures, with about THB42bn going towards cash transfers under an existing co-payment scheme to support consumption, while around THB37.5bn will go towards smaller firms to help retain jobs. The Cabinet has also approved measures amounting to THB131.6bn to support rice farmers' incomes during production year 2021/22.

- **In March, r**elief measures worth THB70bn (US$2.1bn) to counter rising energy prices were approved. Retail diesel prices will be capped at THB30 (US$0.9) per liter until end April, after which the government will only subsidize 50% of any increase in prices. The Oil Fuel Fund Office has already spent THB61.6bn to subsidise diesel and LPG prices since last year. From May to July, cash assistance for cooking gas purchase will be raised to THB100/month (from THB45) for 3.6mn welfare card holders. Other measures include a THB250/month oil subsidy for motorcycle taxis, lower electricity charges for eligible consumers, and lower contribution under the social security system (from 5% to 1%) for both employers and workers.

- In Sep 2021, a government panel approved raising public debt-to-GDP ratio to 70% from 60% in order to raise state borrowing to finance its stimulus and to ensure debt repayment ability. Authorities planned to significantly increase the share of longer-dated sovereign bonds (vs.

short-term securities) for its financing needs, with the former expected to make up around 48%-56% of the government's THB2.3trn (US$68.4bn) borrowing in the new FY compared with 31% in the prior year. **House view is for fiscal deficit to narrow towards 4.3% of GDP in 2022 from 4.8% prior.**

- **We note that authorities are considering various taxes to shore up fiscal revenue** as public debt climbed to 59.6% of GDP in 2021 and fiscal deficit stayed wide. Plans include a 0.1% stock transaction tax, normalization of the land & buildings tax and a THB300 fee on foreign tourists from Apr 2022, but gains will likely be small at less than 0.5% of GDP. Other ways to raise tax revenue will be improving personal income tax collection, raising VAT from the current 7%, and imposing a carbon tax.
- On trade data, customs exports accelerated by +16.2%y/y in Feb on the back of strong global demand for both commodities and manufactured products, prior to the intensification of the Russia-Ukraine war. Imports growth eased to a 11-month low of +16.8%, resulting in a small trade surplus of US$123mn (versus prior deficit of -US$2526mn). **But given potential spillovers to Thailand exports and tourism from ongoing Russia-Ukraine war, current account could still come in at a deficit reading in 2022 (house projection at 1.0% of GDP)**.
- **Key domestic events and issues to watch:** Mar PMI Mfg (1 Apr), Mar Business sentiment (1 Apr); Mar CPI (5 Apr); Mar Consumer confidence (8 Apr); Mar Customs trade (22 Apr); Mar Manufacturing Production (26-29 Apr); Mar BoP Current account (29 Apr).
- **Technical Outlook**: USDTHB last seen near 33.45. Momentum on the USDTHB daily chart has turned mildly bearish (from mostly bullish in March), while RSI is not showing a clear bias. Overall developments suggest that key resistance for USDTHB at 34.00 (Sep, Dec double-top) could still hold in the interim. Support at 33.15 (100-dma), 32.85 (38.2% fibo retracement from Jun 2011 low to Sep, Dec double-top), 32.50 (50.0% fibo).



INR: Cheaper Oil Aids RBI To Stay Focus on Growth Support

Forecast	2Q 2022	3Q 2022	4Q 2022	1Q 2023
USDINR	**75.50 (74.50)**	**75.00 (74.20)**	**74.50 (74.00)**	**74.50 (--)**

Previous Forecasts in Parentheses

- **Motivation for the FX View:** In Feb, we raised the 1Q USDINR forecast in light of the military conflict in Ukraine that fanned crude oil prices higher. We had expected INR to be weakened by the war-triggered oil swings but we also looked for retracement thereafter as historical episodes of military conflicts demonstrated that these impacts tend to dissipate. Price actions played out as expected but the magnitude of the oil swings, the protractedness of the war (more than a month now) were underestimated. As such, we downgraded the INR further to reflect these developments.

- Perhaps the most contentious event to eye at this point is India's oil deal with Russia. India is said to purchase 15mn barrels of oil from Russia on a CIF basis where Russia bears cost, insurance and freight. More recently, there were sources cited saying that Russia had offered India very steep discount (as much as $35/bbl on the price pre-war) on its oil. In exchange, India hopes to promote exports of its medicines, engineering goods and chemicals to Russia. Russia has offered to use Russia's messaging system of SPFS as an alternative to SWIFT in the rupee-ruble denominated payments. Russia's Foreign Minister Sergei Lavrov made a two-day trip(31 Mar- 1Apr) to Delhi for talks. The on-going India-Russia oil deals are drawing rebukes from officials from US and Australia and may have some impact on the Australia-India FTA that is close to completion. However, purchase of Russian oil should dampen fuel-inflation at home and allows for RBI to keep monetary policy stance accommodative to support growth.

- **To some extent, our over-arching view for now continues to call for USD nearing its peak, barring no further escalation in geo-political tension and no further surprises in Fed tightening already made so far. The 100-handle could remain a strong resistance for the DXY. Despite the aggressive hawkish shift in Fed signaling via dots plot and Fedspeaks, and concomitant surge in UST yields, AxJ FX (including INR) have weathered the Fed normalization messaging relatively well.**

- **Growth and Inflation Outlook:** Industrial production rose to 1.3%y/y from previous 0.7% (also revised higher). The headline was supported by infrastructure/construction output which rose 5.4%y/y in Jan vs. previous 2.1%. Consumer durables made a steeper fall of -3.3%y/y vs. previous -2.6% while non-durables rebounded 2.1%y/y from previous -0.1%. Breakdown by industry showed a rebound in mining and manufacturing output while electricity growth slowed to 0.9%y/y from previous 2.8%.

- The slight improvement in PMI Services (51.8 for Feb vs. 51.5) bode well for the sector, possibly also boosted even more recently as some Indian states lifted all restrictions. The Retailers Association of india noted that retail business rose 10%y/y in Feb, extending a trend of recovery and normalization from pandemic days. That said, the RAI cautioned that values are not adjusted for inflation and quantitative growth is still lacking for some categories. Taken together, the manufacturing and services are still at the early stage of recovery and rather uneven, rendering the RBI between a rock and a hard place.

- Inflation surprised to the upside at 6.1%y/y for Feb (again), accelerating from previous 6.0%. Headline was driven by food (5.9%y/y vs. prev. 5.4%) and clothing & footwear (8.8%y/y vs. prev. 8.8%), housing prices (3.6%y/y vs. 3.5%). Fuel inflation softened a tad to 8.7%y/y from previous 9.3%. Should India successfully purchase oil from Russia, inflation could be kept under control to some extent. Right now, retail fuel prices have been raised incrementally but could be adjusted lower given US' massive release of its strategic oil reserve that has brought international crude oil back towards the U$100-handle (brent at U$107/bbl as of 1 Apr).

- Trade deficit for Feb widened to $20.9bn vs. previous $17.4bn. Exports steadied with a growth of 25%y/y but imports picked up pace to 36.1%y/y from previous 23.5%. Oil imports rose from $11.96bn in Jan to $15.28bn for Feb, contributing to the widened trade deficit. Should domestic demand continue to recovery and external demand hurt by elevated crude oil prices and geopolitical tensions, we can expect India's trade deficit and concomitantly, current account deficit to deteriorate. One silver lining is India's ability to step up wheat export as world's breadbasket region (Russia and Ukraine) is affected by the war. Indian farmers just had a record harvest that could contribute to a record wheat export for this year. ITC, India's biggest wheat exporter, expects its exports to grow 3x for FY2023.

- **Monetary Policy Forecast:** On the monetary policy front, RBI's stance is increasingly clear with a preference to support growth rather than to focus on inflation. Earlier this month, RBI Das had pledged to provide ample liquidity (current state is already in surplus state and in the process of normalization) to support the functioning fo the credit system whilst acknowledging the uncertainties that shroud the inflation outlook. He was also quite confident that retail inflation should ease from current elevated levels and cheap oil deals with Russia could aid in that aspect. Taken together, we look for the growth-focused, inflation-nonchalent RBI to retain its accommodative monetary policy stance at the Apr meeting and to keep all policy rates unchanged. Main repo rate at 4.00% and reverse repo rate at 3.35%. Cash reserve ratio at 4.00%.

- **Latest Fiscal and External Balance Outlook:** Budget 2022-23 is an expansionary one. **Fiscal deficit is projected to come in a tad higher than previous estimate at 6.9% of GDP for FY2021-2022 but should ease further to 6.4% for FY2022-23.** Finance Minister Nirmala Sitharaman had proposed increasing capital spending by 35% to INR7.5trn for 2022- 2023. In addition, there is a push for infrastructure-led growth with spending focused on roads, rail, logistics and energy, bringing to fruition the National Master Plan for economic transformation, multimodal connectivity and logistics efficiency that was approved by the Union Cabinet last Oct. Effective capital expenditure is estimated to be at 4.1% of GDP.

- **Key domestic events and issues to watch:** Markit Mfg, services, composite PMI (Mar) on 4 Apr; RBI policy decision (no change) on 8 Apr; industrial production for Feb and Mar CPI on 12 Apr; Mar WPI on 14 Apr; Mar trade on 14-15 Apr.

- **Technical Analysis:** USDINR finds tentative support at the 50-dma at 75.50 but bearish momentunm suggests there is a possibility of a bearish extension towards 75.14 before the next at 74.70. Resistance at 76.26.

VND: Stabilizing but still a tad Vulnerable

Forecast	2Q 2022	3Q 2022	4Q 2022	1Q 2023
USDVND	22900 (--)	22800 (--)	22800 (--)	22700 (--)

No Change to Previous Forecasts

- **Motivation for the FX View:** We maintain our forecast trajectory, expecting two-way actions of the USDVND with small risks to the upside. Recent Russia-Ukraine conflict that triggered market volatility could still be a risk to VND. Our economist has downgraded 2022 GDP from 6.7% to 5.8% because of the geopolitical conflict as well as China's intermittent lockdowns. That said, growth could still be underpinned by the recent reopening of Vietnam's border. VND could be supported by inflow of tourist receipts, FDI.
- Cautious sentiment, rising energy prices and buoyant USD had underpinned the USDVND. Vietnam saw equity-related outflow of around $156.2mn for Mar but more recent daily net flows had turned positive, suggesting some signs of stabilization in sentiment.
- Inflation risks are being carefully managed by the government with a slash on environmental tax on petrol being approved recently to ease fuel costs. The industry and trade ministry ordered importers to double Mar imports to 1m cbm in order to make up for the shortage at the local Nghi Son oil refinery. Meanwhile, the authorities also urged Vietnam Oil and Gas Group for greater oil exploitation output, exploration of new oil fields and to construct the Vung Tau refinery project.
- USDVND has recently stabilized within the 22800-22900 range. Room for USD upside could be limited at this point (given an incredible 10 Fed hikes priced over the next 1 year). The 100-handle could remain a strong resistance for the DXY. Despite the aggressive hawkish shift in Fed signaling via dots plot and Fedspeaks, and concomitant surge in UST yields, AxJ FX (including VND) have weathered the Fed normalization messaging relatively well.
- **Growth and Inflation Outlook:** Inflation has become a growing concern as Vietnam is a net energy importer. **Our economic team raised 2022** headline inflation foreast to 4% from previous 3.8%, expecting food and fuel prices to lift CPI above SBV's 4% target cap from 2Q notwithstanding government measures expected to mitigate some of the price pressure.
- Mar data was mixed with output of some industries dampened by rising prices including the petroleum as well as the agriculture, forestry and fishery sector. Industrial production rose 8.5%y/y in Mar, steady from Feb. Headline is buoyed by manufacturing (+9.6%) and water supply & waste management output at 8.5%. Electricity and gas output softened to 4.8% in Mar from 8.0% previously. Agriculture, forestry and fishery sector slowed from 3.2% to 2.5% due to the rise in the prices of animal feed. Meanwhile, services sector gained 4.6%y/y, buoyed by financial, banking & insurance, transporation & storage and wholesale, retail sales & motor

vehicles. Expect the reopening of borders and tourist inflows to support accommodation & food services that have been on a persistent decline. Retail sale picked up pace to 9.4%y/y from previous 4.1%. Adjusted for inflation, our economist noted that retail sales actually grew at a more muted 1.6%. Forecast for 2022 real GDP growth is cut to 5.8%, below the target range of 6-6.5% set by the government.

- Trade balance swing back into a surplus of $1.39bn. Exports picked up pace from pervious 13.2%y/y to 14.8% for Feb. Imports on the other hand, slowed to 14.6%y/y from previous 21.95. VND has also been cushioned by FDIs with pledged inflow recorded at $243.8mn. Its balance of payment could be supported by the inflows of tourist receipts as Vietnam has opened its borders from mid-Mar.

- Key risks to the economy from the Russo-Ukraine war at this point arise from rising commodity prices(that could have pass-through effects on household consumption), trade (impact on vietnam's exports to Russia and to countries that supply to Russia, impact on external demand), tourism arrivals. In addition, China's intermittent lockdowns have proven to affect freight costs and Vietnam's supply chains.

- **Monetary Policy Forecast:** Our economist looks for a hike of 50bps to lift policy rate (refinancing rate) to 4.5% from the current 4% but only towards the end of the year. SBV is likely to keep monetary policy accommodative for as long as possible to support growth recovery and will only start to hike policy rate when domestic demand show signs of affecting inflation expectations. SBV expects credit growth to be at 14.1% for 2022.

- **Latest Fiscal and External Balance Outlook: Right at the start of the year, the National Assembly has approved a $15bn economic recovery package for 2022-**2023. This package includes upgrading healthcare capacity and pandemic resilience (VND60 trn), ensuring social welfare and employment (VND53.15trn), businesses and cooperatives aid (VND 110trn), infrastructure development (VND113.85trn) alongside other reforms. VAT for certain goods and services will also be lowed by 2% to 8%. The budget defict is expected to be raised nu am average of 1-1.2% of the GDP. by about VND240trn. Our economist expects fiscal deficit to be 4% of GDP. Public debt ratio remains modest at around 43-44% of GDP in 2022 (vs. 43.7% of GDP in 2021), well below the debt ceiling of 60% of GDP.

- **Key Domestic Events and Issues to Watch:** Domestic vehicle sales (Mar) due on 6-13 Apr; Apr CPI, trade, retail sales, industrial production due on 25-30 Apr.

FX Forecasts

	End Q2-22	End Q3-22	End Q4-22	End Q1-23
USD/JPY	120.00	120.00	118.00	117.00
EUR/USD	1.1200	1.1250	1.1500	1.1500
GBP/USD	1.3200	1.3250	1.3400	1.3500
AUD/USD	0.7400	0.7500	0.7500	0.7600
NZD/USD	0.7000	0.7100	0.7100	0.7100
USD/CAD	1.2400	1.2300	1.2300	1.2200
USD/SGD	1.3200	1.3100	1.3000	1.2900
USD/MYR	4.2000	4.1800	4.1500	4.1500
USD/IDR	14250	14200	14100	14100
USD/THB	33.00	32.50	32.50	32.00
USD/PHP	51.00	50.50	50.00	49.50
USD/CNY	6.35	6.33	6.32	6.30
USD/HKD	7.80	7.80	7.80	7.80
USD/TWD	28.40	28.20	28.00	28.00
USD/KRW	1190	1180	1160	1150
USD/INR	75.50	75.00	74.50	74.50
USD/VND	22900	22800	22800	22700
DXY Index	97.56	97.09	95.46	95.11
SGD Crosses	End Q2-22	End Q3-22	End Q4-22	End Q1-23
SGD/MYR	3.18	3.19	3.19	3.22
JPY/SGD	1.10	1.09	1.10	1.10
EUR/SGD	1.48	1.47	1.50	1.48
GBP/SGD	1.74	1.74	1.74	1.74
AUD/SGD	0.98	0.98	0.98	0.98
NZD/SGD	0.92	0.93	0.92	0.92
CAD/SGD	1.06	1.07	1.06	1.06
SGD/IDR	10795	10840	10846	10930
SGD/THB	25.00	24.81	25.00	24.81
SGD/PHP	38.64	38.55	38.46	38.37
SGD/CNY	4.81	4.83	4.86	4.88
SGD/HKD	5.91	5.95	6.00	6.05
SGD/TWD	21.52	21.53	21.54	21.71
SGD/KRW	902	901	892	891
SGD/INR	57.20	57.25	57.31	57.75
SGD/VND	17348	17405	17538	17597
MYR Crosses	End Q2-22	End Q3-22	End Q4-22	End Q1-23
JPY/MYR	3.50	3.48	3.52	3.55
EUR/MYR	4.70	4.70	4.77	4.77
GBP/MYR	5.54	5.54	5.56	5.60
AUD/MYR	3.11	3.14	3.11	3.15
NZD/MYR	2.94	2.97	2.95	2.95
CAD/MYR	3.39	3.40	3.37	3.40
MYR/IDR	3393	3397	3398	3398
MYR/THB	7.86	7.78	7.83	7.71
MYR/PHP	12.14	12.08	12.05	11.93
MYR/CNY	1.51	1.51	1.52	1.52
MYR/HKD	1.86	1.87	1.88	1.88
MYR/TWD	6.76	6.75	6.75	6.75
MYR/KRW	283	282	280	277
MYR/INR	17.98	17.94	17.95	17.95
MYR/VND	5452	5455	5494	5470

Source: Maybank FX Research and Strategy as of 1 Apr 2022.
*These forecasts are meant to be indicative of FX trends and not meant to be point forecasts.

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