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FX Monthly

2017, Issue 4: Will Growth Enthusiasm and Political Risks Ease in May?

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What Has Changed This Month?

- Much has changed in the G7 space in the past month and we have made modest upgrades in the GBP and the EUR projections according to recent political developments. The DXY forecast is also calibrated lower accordingly.
- INR was also received a mild upgrade against the USD given the surprising move by RBI and a hawkish tone in its statement but we like to maintain this upside trajectory of the USDINR as we anticipate bonds inflow to slow and seasonality shifts against the rupee.
- USDVND forecast was recalibrated lower to take into account the lack of USD strength but we still see vulnerability in the VND to two Fed hikes this year.
- MYR forecast was revised firmer (vs. the USD) to reflect the positive outlook given the recent initiatives from BNM to broaden and deepen the onshore financial markets.

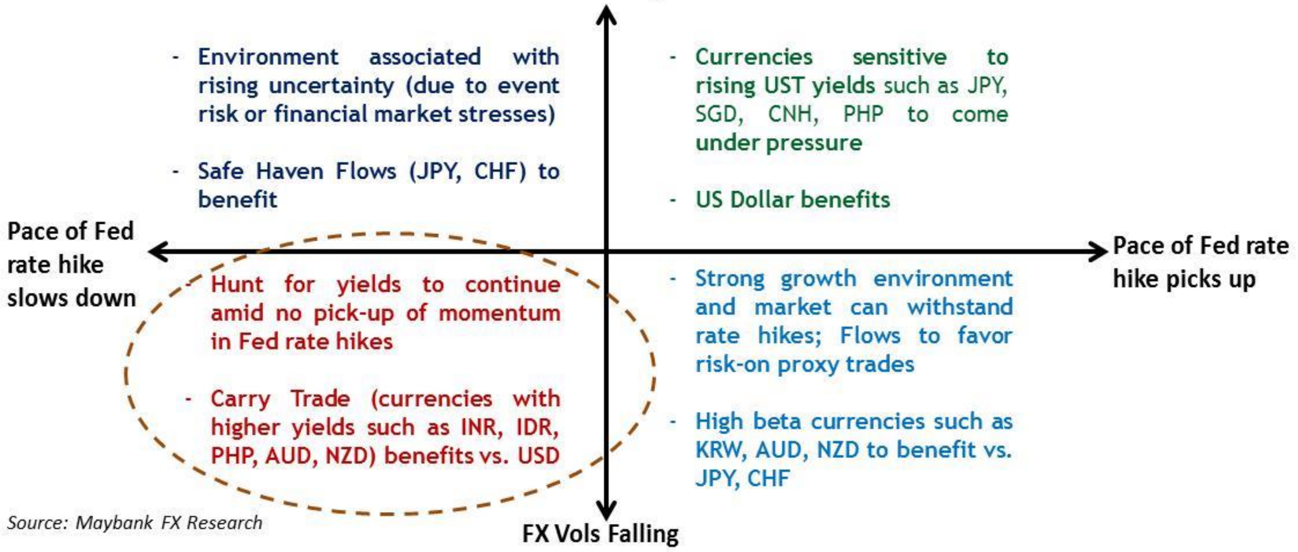
Our Strategies

- With political risks receding in Europe, we expect markets to price out political risk premium and this should keep the EUR supported (but not elevated). We are not of the view that ECB will change its stance on accommodative monetary policy soon given benign inflation outlook but relative to BoJ (the other central bank on easing bias), we see scope for ECB to move earlier than BoJ in terms of taper/signal change in monetary policy stance. We favor **long EURJPY, as one of our strategic trade** for 2017.
- We like to **maintain our short term bearish AUD call, against the USD (towards 0.73/0.72) and the MYR(3.24)** given stretched long positioning, extension in commodity correction, a potential credit rating downgrade event post the Federal Budget delivery and a possible USD resurgence in a seasonally bullish month for the greenback.
- We are biased to **lean against GBP strength** as matters of politics are fluid and *Brexit* negotiation with EU has yet to begin. Downside surprise to economic data should also weigh. **Beyond the 2-3y horizon, we do however see GBP trading higher than current levels, possibly towards 1.35 - 1.40** as GBP is perceived to be undervalued from both historical and fundamentals perspective (our BEER model puts GBP at 1.40).
- Amongst AXJs, we are **positive on the MYR** given the recent initiatives from BNM. We expect foreign investors' confidence to gradually return. We see scope for Ringgit to play catch up with regional peers and **extend its gains towards 4.34, 4.30 levels** (vs the USD) for the month of May. Prefer to long the MYR against the SGD, THB, IDR, PHP and JPY.

SEE PAGE 53 FOR IMPORTANT DISCLOSURES.

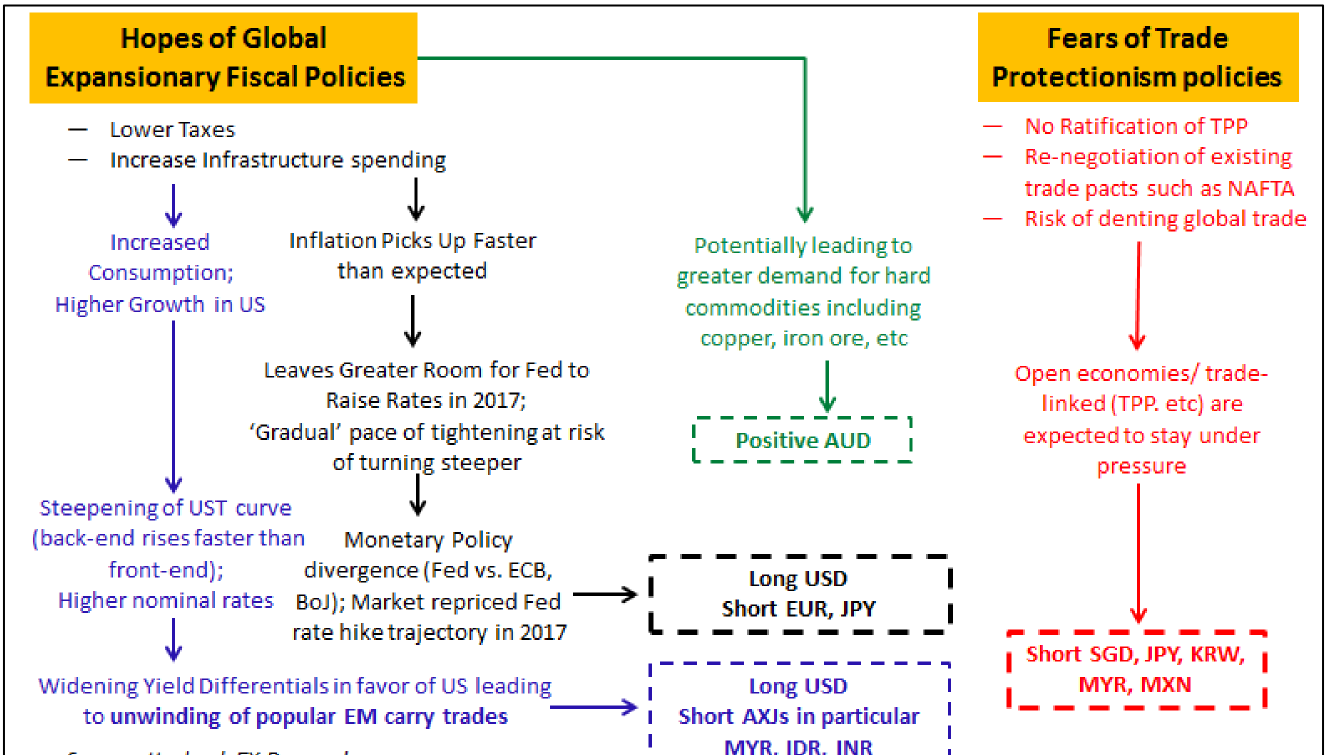
So What?

In the short to medium term, FX Vols and Pace of Fed Rate Hikes are Determinants to FX Bias, Current Environment Favours: INR, IDR, AUD, NZD



Source: Maybank FX Research

Hopes of Expansionary Fiscal Policies vs. Fears of Trade Protectionism



Source: Maybank FX Research

G7 Global Overview

USD: Looking out for Fiscal Policy Deliberations and Labour Market Signals

Forecast	2Q 2017	3Q 2017	4Q 2017	1Q 2018
USD Index	99.22 (102.22)	100.16 (102.50)	99.83 (101.36)	97.98 (99.46)

Previous Forecast in Parenthesis

- **Motivation for the FX View:** We expect at least two rate hikes in 2017, more likely in June onwards. We do caution that additional repricing of a surprise Fed hike over the course of the year (due to market complacency over Fed rate hike trajectory) could continue to see UST yields higher in particular Treasuries 2y and below, and see **USD strength (buy the rumor) in the lead-up to FOMC** meetings. Since the US Presidential elections, the focus has shifted back to a stronger USD due to a US cyclical upturn (from positive slew of US data) and the potential for a pickup in inflation. We continue to expect domestic factors and a repricing of the future stance of monetary policy to support the USD. Even though the market's expectations on the Fed tightening cycle have moved, we think market pricing for the federal funds rate may be dovish at times and we still expect the Dollar to appreciate in the short term. During this phase and around FOMC announcements, we believe the **USD could still be mildly supported**. In addition, we may need clarity on both fiscal and trade policies from the Trump administration to support a US reflation view. If one of these falters, we could see softness in the USD and further sharp ups and downs in the dollar in 2017. The Trump administration success in its efforts to introduce tax reform remains unclear at this juncture. Continued absence of an agreement on revenue raising measures, President Trump's tax plan will likely have to be scaled back and unclear signals on the tax reforms could soften the USD over the next month or so. At the May FOMC meeting, we expect the Fed to reiterate continued strengthening in the labor market, but still not strongly signal a June hike.

- Nonetheless, as long as there are less economic growth downgrades by supranationals and the market, some signs of global inflation emerging, rising expectation of faster pace of Fed rate hike and if oil remains somewhat stabilized around $50-60/bbl, then we will expect USD strength to be sustained in 2017 and UST yield steepening to appear more entrenched. Oil having dropped to belo $50 have continued to weight on the USD.

- **Growth and Inflation Outlook:** The advance release end of April is likely to show that GDP growth slowed significantly to 1.0% q/q saar in Q1 17. Potentially due to private consumption growing by a tepid 1.0% q/q saar in Q1, even if residential investment rose strongly. Regarding other components of business fixed investment, structures investment looks set to make solid gains while intellectual property and equipment investment will likely grow more modestly. Data on inventory accumulation point to a large negative contribution at -0.7pp. Elsewhere, recent data on trade point to a small positive contribution.

- Data in April seems to have indicated some slowing down in March. Nonfarm payrolls expanded 98k in March, with the private sector adding 89k and the government sector increasing 9k. The headline number was considerably weaker than consensus expectations of 180k and shows substantial weakening consistent with the deterioration in initial claims over March. We continue to see divergence between soft and hard data. We look for labour markets to accelerate in the near term and when judging the economic outlook, we take considerable signal from employment growth. In our view, payroll increases in the 200k range are consistent with continued economic expansion, and as long as labor markets improve at or around this pace, we view risks surrounding the recovery as broadly balanced.

- March US CPI inflation was much weaker than expected. Headline CPI inflation fell 0.3% m/m, while core inflation declined 0.1%. Energy prices declined, while food prices rose modestly. At the core level, the softness reflects modestly weaker shelter inflation compounded by large declines in a few specialized categories. Core services inflation declined for the first time since 2010. Core CPI will gradually firm over time, supported by domestic price pressures and our view that the economy is at full employment. Nevertheless, goods inflation has taken longer to turn around than we anticipated, despite the improving trend in import and producer price pressures.

- **Monetary Policy Forecast:** We expect the FOMC to remain on hold in May. The softness in incoming data should not delay Feds plans for normalization. We expect two further hikes this year – in June and Q3-Q4 (Sep or Dec) followed by a balance sheet normalization in Dec. This is evident in the Mar FOMC minutes. Continued weak data could derail a June hike, but the bar to disrupting the Fed's plans is higher now than it was in previous years.

- But any substantive deceleration in data this year, and we could see Fed step back toward their more dovish bias. The fiscal stimulus this year if it materializes is the main factor likely to support growth but with the NFP showing deceleration rather than acceleration and if the weakness continue, if Congress disappoints by failing to implement the fiscal stimulus, monetary policy could be more dovish and weigh the USD lower.

- Balance sheet reduction later this year is now part of the Fed's plan. The minutes to the March meeting contained detailed discussion on balance sheet policies with staff weighing in with various alternative scenarios during the March meeting. This early signaling and communications is potentially done to avoid adverse market reactions.

- The meeting participants reaffirmed the approach to balance sheet normalization articulated in the Committee's Policy Normalization Principles and Plans announced in September 2014 and agreed that any reduction in securities holdings should be "gradual and predictable" and accomplished primarily by phasing out reinvestments of principal received from those holdings.

- **Latest Fiscal and External Balance Outlook:** Fiscal policy should be expansionary over the next few years as the tax reforms take shape and some investment in infrastructure becomes apparent under the Trump administration. The deficit has fallen sharply from its peak. Fiscal sustainability risk continues to weigh on the outlook and may emerge sooner than later. In the long term, an improved US economy and manufacturing sector, US shale oil and gas production may improve the US current account leading to dollar support but this is likely to be long drawn and may probably begin only in 2018. The US other deficits - current account and BOP deficits have moved slightly wider and is expected to continue. The latest Jan 2017 US nominal trade deficit was in line with consensus but rose from a month earlier, to $48.5bn from -$44.3bn. The U.S. chalked up its largest trade deficit since March 2012 as a jump in merchandise imports in January exceeded a smaller gain in shipments overseas.

- **Key domestic events and issues to watch in May 2017:** Key US events: PCE Deflator (1 May and 30 May); ISM Manufacturing (1 May) (expected: 56.5); Factory Orders (4 May); Durable Goods (4 May, 26 May); Trade Balance (4 May); NFP (5 May); CPI (12 May); GDP 1Q (26 May), FOMC (4 May); FOMC minutes (25 May)

- **Technical Outlook:** DXY traded a high of 101.34 in mid-Apr before drifting lower into end-month. Last seen at 98.90 levels. Bearish momentum on daily and weekly charts remains intact while stochastics is heading into oversold conditions. Support remains at 98.80 (61.8% fibo retracement of Nov low to 2017 high). Downside may persist for longer if key support at 98.60 (upward sloping trend-line support from the lows in 2014, 2016 and 2017) breaks down. Otherwise we believe the downside should be limited towards 98.60 levels and could soon rebound. Resistance at 99.80, 100.80 levels.

EUR: Pricing Out Political Risks

Forecast	2Q 2017	3Q 2017	4Q 2017	1Q 2018
EURUSD	**1.0800** (1.0450)	**1.0700** (1.035)	**1.0800** (1.0600)	**1.0800** (--)

Previous Forecast in Parenthesis

- **Motivation for the FX View:** A Macron-Le Pen second round run-off (with markets/polls expecting a Macron Presidency) is broadly positive for the EUR. Recent polls including Harris Survey and Ipsos/Sopra Steria suggest the same with Macron winning the second round by 64% to 36%. Even defeated contenders including 3rd placed Fillon (Right-wing) and 5th placed Hamon (socialist) have also urged voters to support leading candidate Macron (centrist) against Le Pen (Far Right) for the second round. We do not expect much surprise in the second round run-off on 7 May. This scenario should calm any market anxiety, support investor sentiment and keep EUR supported. But we are slightly cautious how much the EUR can rally (off the back of French elections), given that a Macron victory has now been priced in to some extent while ECB remains on monetary easing bias. We expect EUR's profile to shift slightly higher but remain confined to 1.0680 – 1.10 range for the month of May.

- Given current market development, we revised upwards our EUR forecast across the forecast horizon - pricing in some degree of EUR weakness for 3Q due to potential political risks from German elections and potential pick up in USD strength; revised upward 4Q 2017 and 1Q 2018 forecast higher, reflecting potential ECB tapering/rate hike speculation (potential monetary policy convergence with Fed).

- Apart from receding French election risks, we believe that a higher EUR (1.08-handle from previous 1.06-handle in late-Mar) was also in part due to markets somewhat expecting an earlier than expected ECB rate increase or tapering ahead of schedule due to recent upticks in inflation data. But we are not in the same camp. **We think market speculation for ECB rate increases or further taper may have come too soon and eventual disappointment could limit gains.** The ECB had placed strong emphasis on core inflation and increasingly (at the last ECB press conference in Mar) stressed that wage growth is a key indicator of domestic underlying inflation. He said that policy rates would remain at "present or lower levels" even if headline inflation is at 2%. Furthermore, core inflation was largely unchanged at 0.9% y/y in Feb (unchanged from previous 3 months). And the increase in headline was due to base effects and energy prices (i.e. imported inflation). Imported inflation reduces real wages (since wage growth is subdued) and could weigh on household consumption. There is little justification for ECB to call off monetary easing from mere upticks in headline inflation.

- German Federal elections (24-Sep) 3Q 2017 should also warrant some caution. Much remains unknown at this stage and some clarity on German opinion polls should come after Jun-Jul 2017. Like France and Netherlands (which both held their elections in Apr and Mar, respectively), German opposition (AfD) party is banging on anti-immigration and is perceived to be a hard critic of the Euro and Islam. But given a poor showing of the parties favouring anti-establishment, anti-Euro and far-right ideologies at the Netherlands and French Presidential elections, it seems that the rise in populism in Europe may face a backlash (recall how rise in populism resulted in markets pricing in political risk/undermining the stability of the Euro club and a weaker EUR, the reverse is also true).

- But beyond the German elections, we expect ECB's plan to end QE in Dec-2017 to come into play and possibly signal raising rates. Divergence of ECB's monetary policy with the Fed could narrow and possibly play catch up. This should lend support to the Euro towards our current medium term fair value of around 1.15 over time. We note the possibility of Italy elections in mid-2018 (which could put some downside pressure on the EUR). We believe Euro-area needs deeper structural reforms in debt and labor market to lift long term growth potential and push EUR meaningfully higher above 1.20 but pushing through policies within the Euro-area are often complicated and challenging.

- **Growth and Inflation Outlook:** Euro-area recovery broadens. PMI releases since Aug 2016 continued to show acceleration in growth momentum. Flash PMI - both manufacturing and services rose further to 72-month high in Apr and the increases continue to surpass expectations. Breakdown by country also showed strong contribution from both Germany and France, with the latter outperforming Germany.

- In the last quarterly assessment report (9 Mar), ECB modestly revised 2017 and 2018 growth to 1.8% and 1.7% (from 1.7% and 1.6%), respectively. ECB's Draghi acknowledged that the survey results suggested that economic expansion will continue to firm and broaden. Domestic demand including recovery in investment is expected to benefit from favorable financing conditions.

- **Euro-area inflation decelerated in Mar, with headline falling to 1.5% y/y** (vs. 2% in Feb). Decline was due to food & non-alcoholic beverages, transportation and recreation & culture prices. Core inflation (which is ECB Draghi's main focus) slipped to 0.7% y/y for Mar (vs. 0.9% for the past 4 months). ECB's Draghi said there is no convincing upward trend in underlying inflation (21 Apr). In the last quarterly assessment report (9 Mar), ECB revised 2017 inflation to 1.7%, from 1.3%. The ECB expects headline inflation to remain at 2% in coming months due to energy prices. Measures of underlying inflation remained low and are expected to rise only gradually over the medium term

- **Monetary Policy Forecast:** There is no monetary policy meeting next month. The next one is scheduled for 8 Jun. We still expect ECB to keep monetary policy status quo at the next meeting, after its decision (back in Dec 2016) to extend QE till end 2017. **We reiterate that it remains too early to call for further tapering, given that core inflation has yet to see a meaningful recovery.**

- At the last ECB meeting (27 Apr), Draghi reiterated that inflation remains subdued and has yet to show a convincing upward trend, in particular core inflation. He added that the ECB is not confident that inflation will rise and stay at the bank's goal of just below 2%. He reiterated that the ECB could increase the size or lengthen the duration of its asset purchase program if inflation looks set to fall far back below ECB's target.

- ECB's Chief mandate in getting Inflation higher. Without upward and sustainable prices pressures, there is no strong basis for ECB to move into neutral or tightening stance. Previously, **ECB Draghi had said that higher inflation will not automatically result in QE tapering**. For inflation to be considered as 'sustained adjustment', there are four elements that need to be fulfilled: Inflation (1) is affecting the medium term, (2) is durable, (3) is self-sustained and (4) is region wide. So far it remains too soon to tell if the four elements above are met as core inflation continued to hold (slipped slightly in the past month) and is not showing any signs of uptick. The **ECB had placed**

strong emphasis on core inflation and increasingly (at the last ECB press conference in Mar) stressed that wage growth is a key indicator of domestic underlying inflation. He said that policy rates would remain at "present or lower levels" even if headline inflation is at 2%. Recent ECB speaks (6 Apr) have also struck a dovish rhetoric - ECB President Draghi said ECB's policy stance is still appropriate… there is 'no need to deviate from policy path'… and is too soon to reduce stimulus. He added that ECB will not raise interest rate before end of bond purchase. Praet said that rates to stay at present or lower level well past QE. He elaborated that rate hike expectations would make QE less effective. In other ECB speaks, Constancio said it is too soon to declare success on inflation, as recent increases were due to food and energy components. He added that the most recent decrease in CPI was disappointing. Vasiliauskas echoed Draghi's earlier comments that ECB's future policy path should be predictable – ECB will end asset purchase phase first and then discuss other possible actions. He reiterated that the ECB members have not discussed anything about interest rates and it would be premature to discuss changing the guidance on lower rates. He also made reference to how other central banks such as BoE as good examples of how ECB should follow.

- To recap, QE was extended beyond Mar 2017 for another 9 months to end-2017, at a reduced pace of €60bn per month. There were also a handful of technical tweaks to the APP to ensure smooth implementation of the program. Our take is ECB's monthly purchase after Apr 2017 may seem like a tapering at first glance but in actual fact, the option chosen between the 2 (either €80bn per month for 6 months or €60bn per month for 9 months) implies a larger QE amount (€540 bn). This implies ECB is still far from tapering and is expected to remain on easing bias.

- **Latest Fiscal and External Balance Outlook:** Euro area's current account surplus ballooned to record high in Feb to EUR37.9bn (vs. 26.1bn in Jan). This is the highest surplus since the formation of the EURO and was due to increase in both goods and services surplus.

- The government deficit ratio is projected to decline to 1.5% in 2017, from 2.1% of GDP in 2015. Projected government debt ratio is projected to decline gradually to 88.4% in 2017, from 91.5% of GDP in 2015.

- **Key domestic events and issues to watch:** Mar PPI (3 May); 1Q Advanced GDP (3 May); Mar Retail sales (4 May); Mar IP (12 May); ZEW survey, 1Q prelim GDP (16 May); Apr core CPI (17 May); Mar current account (19 May); May flash PMIs (24 May); May CPI estimate (31 May).

- **Technical Outlook:** EUR traded higher; last seen at 1.080 levels (25 Apr). Bullish momentum on daily, weekly and monthly chart remains intact while stochastics is still rising. Resistance at 1.0940 (near 24 Apr high); sustained close above could see further upside towards 1.12 levels. Interim support is at 1.0840 (200 DMA) before 1.08 levels. A close below 1.08-handle may see further downside pressure towards 1.0720 handle. Technical bias to buy on dips.

GBP: A Calculated Move or a Risky Gamble?

Forecast	2Q 2017	3Q 2017	4Q 2017	1Q 2018
GBPUSD	1.3000 (1.2000)	1.2600 (1.2300)	1.2800 (1.2400)	1.3000 (1.2600)

Previous Forecast in Parenthesis

- **Motivation for the FX View**: We believe the current level of GBP is a reflection of market expectations for a Conservative victory at the upcoming General election (8 Jun). **Rising hopes and expectation for the Conservatives' lead to widen over Labour party should continue to lend support to the GBP,** especially given stretched GBP shorts positioning. **But hopes and expectations have to be validated by future opinion polls and local election results (4 May).** While a Conservative victory is priced in to some extent, the potential downside scenarios including other parties getting their act together and play catch up with Conservative, the risk of Scottish referendum, etc. are not priced in. And we think it remains too soon to conclude election results from opinion polls. N**arrowing of the lead should dampen market complacency and weigh on the GBP.** Moreover, we have flagged out that **potential downside surprise to economic data in coming weeks to months should also weigh on GBP.**

- **While we do expect upside risks for the GBP, possibly towards 1.30-1.3050 levels, we are biased to lean against strength.** We also think the current GBP vol environment maybe "relatively cheap", we suggest using **option strategies to play event risk.** For an optimistic take on election results (or favor GBP upside), one may consider buying seagull structure (with Knock-Out option) or One Touch Option. For a pessimistic take on election results (or favor GBP downside), one may consider buying GBP put spread or low delta put option. (For further details, please see below).

- **Opinion Polls vs. Betting Odd.** We believe **PM May's move to call for snap election is a calculated move** but matters of politics are fluid and fickle. **Miscalculation will almost certainly jeopardize PM May's political career** and unleash a new realm of uncertainty especially in the unfortunate event of a change in country leadership (GBP can re-test below 1.20). Going by opinion polls (conducted on 12-13 Apr before the announcement of the election), early poll results showed a strong lead (of 22 points) for the Conservative party over Labour party. This is the widest lead Conservative party ever has over Labour party since 2010. Those results also represent the lowest voting intention share for Labour party since Jun 2009 (when leader Gordon Brown was then-PM). 50% of the electorate also think that PM Theresa May would make the best PM, compared to Labour's Jeremy Corbyn (14%) while 36% said they don't know. **Current polls results suggest that the wide lead could translate into a comfortable win for the Conservative party.** Based on opinion polls from 10 – 27 Mar, sampling from 10,972 respondents, the **Electoral calculus predicted that**

Conservative party could win by 112-seats majority. Even **bookmaker William Hill says the Conservatives have an 84% chance of winning with an overall majority.**

- **Watch Local Election Results:** As of now, we prefer not to over-interpret opinion polls and prediction, especially when there are still 7 weeks to go and the most recent poll was conducted before the 8-Jun election date was announced. We still think opinion polls are at best a rough guide and not the Holy Grail, given how opinion polls got it so wrong in 2015 – recall that almost all opinion polls pointed to a hung parliament for UK while the actual elections outcome was a victory for the Conservatives. While the focus has mainly been placed on the Conservative and Labour Parties, much remains unknown how the Liberal Democrats and Scottish National Party may fare. Although Liberal Democrats lost badly in the 2015 general elections from 57 seats to just 8 seats in Parliament, they may pose some risks for PM Theresa May and her party in the upcoming elections. Recent polls have shown slow but increasing support and there is a chance the Liberal Democrats (the only party committed to *Bremain*) can garner support in the South-West region and those supporting *Bremain*. Instead we look to local election results (4 May) for a closer indication of how various parties may fare in the upcoming General election. **Local elections are scheduled for 4th May where 4,581 council seats are up for grabs in England, Scotland and Wales. Voting for 6 new metro mayors will also take place.**

- Given recent market development and a sharp rally in the GBP above key resistance 1.2620 (200 DMA), we **revise our GBP forecast higher across the forecast horizon**. We expect **GBP to trade in higher range** of 1.26 – 1.30 for the month of May (from 1.20 – 1.27). **Though elections are typically perceived as uncertainty and should weigh on GBP, the move higher in the GBP despite snap elections being called is due to the large lead Conservative has over Labour party.** Hence we **caution that if this lead narrows beyond the comfort of the markets, GBP will face renewed downside risks**. For now, the enthusiasm is still on given the wide lead (widest lead since 2010) and resilient economic data. We **believe downside surprise to economic data should weigh on GBP** as well. We had also shared (in our last monthly outlook) that the strong 4Q 2016 GDP (+0.7% vs. +0.6%) was due to the jump in net exports while fixed investments declined and household consumption fell. Rising inflation (+2.3% y/y in Mar), possibly faster than wage growth will depress real wages and eat into household budget (consumer squeeze).

- We also wish to add that ***Brexit* negotiation with the EU has yet to commence.** The **election is a short term distraction from the real underlying issue**. Negotiating trade deals can be a long-drawn process (especially with the EU) and much remains unknown over London's status as a financial hub; if it can continue to attract foreign inflow of funds and investments, if MNCs will relocate their HQs and result in job losses (Goldman Sachs is reported to consider 50% cut to London staff, with transfers to NY and Frankfurt offices while UBS and HSBC are considering moving their staff out of London).. We see these uncertainties returning and re-exert downside pressure on the GBP, beyond the elections.

- **Beyond the 2-3y horizon,** we do however **see GBP trading higher than current levels, possibly towards 1.35 - 1.40 as GBP is perceived to be undervalued from both historical and fundamentals perspective** (our BEER model puts GBP at 1.40). The 20% or so depreciation since referendum results (Jun 2016) should help the UK economy to rebalance and grow sustainably over time - current account deficit should narrow, exports should become more competitive and tourism and education receipts should pick up further. We believe UK should be able to manage the exit, transform itself into a global marketplace and continue to attract capital (longer-term). We priced in a slightly higher GBP towards 1Q 2017 due to our expectations that trade negotiations may gain momentum towards year-end following German Federal elections (Sep 2017), shifts in BoE MPC (more dissenters due to rising inflation) and potentially better clarity (in terms of trade relations, MNC commitment to FDIs, ongoing job creation, if investment will start to pick up) on UK's exit. Past experience of UK leaving the ERM back in 1992 saw a period of consolidation (for a few years) at historical lows for GBP, before the eventual move higher in the following years. GBP TWI traded above 100-levels in 1998 (from the lows of 80 in 1993-1996) due to buoyant demand fueled by rapid growth of wealth, credit and money.

- **Option Strategy Ideas: For clients who are more optimistic** and **believe GBP can rise further** amid stretched GBP short positioning, we suggest the following FX option plays:

  (1) Buy 3-month GBPUSD One Touch (OT), with strike at 1.3750. Premium at GBP16.5%.

    - An attractive risk-reward profile of 6x if GBP spot hits 1.3750 within the next 3 months. Client also benefit when vols start to rise as this option play (via OT) is an expression of long vols
    - Recall that option vols typically run higher in the lead up to election and referendum day. And vols during those period punched above 10-levels
    - Assume if GBP spot rises towards 1.3240 levels over the next 1-month, the OT is estimated to be worth 33%. This is double the cost of 16.5%, with 2 more months remaining (assuming vols stay unchanged). Should vols climb higher, the value of the OT will be worth higher.

  (2) Buy 3-month seagull (modified with KO), with maximum payout of 3.7% if GBP spot rises to 1.3450 within the 3-month period. Zero cost premium. All 3 legs are in equal notional.

    - Client buys GBP Call Strike 1.2950, Client sells GBP Call Strike 1.3450, and Client sells GBP Put Strike 1.2600 that early terminates (KO) if 1.3250 is triggered. All 3 legs are in equal notional.
    - Unlike a normal Seagull, in this structure, if spot were to trade to at or above 1.3250 anytime before the expiry date, the liability leg on the downside will early terminate. Hence thereafter, client will not be disadvantage should there be a turnaround in spot.

- Risk to this structure is GBP did not trade higher towards 1.3250. Instead GBP traded lower and beyond 1.26. This means client will need to buy GBP higher than prevailing spot.

- **Option Strategy Ideas: For clients who are less optimistic and wishes to position for GBP downside** perhaps due to belief that opinion polls' indication remains too early to foretell outcome; that Labour and/or Liberal Democrats may narrow the gap with Conservative or a case of PM May's miscalculation which may result in the change of country leadership (black swan event), we suggest the following strategies:

  (1) Buy 3-month GBP put spread, with maximum payout of 500 pips at premium of USD130pips.

  - Client buys GBP Put Strike 1.27 and Client sells Put Strike 1.22. Both legs in equal notional
  - Attractive risk-reward profile of 4x.

  (2) Buy 3-month GBP Put Strike 1.20, with premium at USD38pips

  - A low cost plain vanilla option to position for black swan event. Breakeven at 1.1962.

  The above is priced off GBP spot ref of 1.2775 (on 20 Apr).

  For further details on pricing, please contact our Structuring desk in Global Markets, Singapore.

- **Growth and Inflation Outlook:** PMIs remain in expansionary territories (above 50). While services PMI rose in Mar (55 vs. 53.3), both manufacturing PMI (54.2 vs. 54.6) and construction PMI (52.2 vs. 52.5) continue to print softer. IP also slipped in Feb (-0.7% m/m vs. -0.4% in Jan). Retail sales also fell in Mar (-1.5% m/m vs. +1.3% prior) – this is the fastest pace of decline in 7 years. These data are in line with our expectation that data are showing signs of falling momentum and **we continue to caution for downside surprise to economic data, and this could weigh on GBP.** BoE also cautioned that it expects business investment to fall and consumer spending to slow as inflation eats into household budgets.

- **Though UK inflation held steady in Mar (+2.3% y/y),** it remains near 3-year highs. Rising inflation was due to rising food and clothing prices while air fares offset some of the upside impact. Core inflation slipped to 1.8% (from 2% in prior month). With wages rising just 2.3% (average weekly earnings, y/y %) for the 3-months ending Feb, **the strong surge in inflation is depressing real wages and eating into household budget.** Continued deceleration in wage growth and/or rising inflation could weigh on real wages and crimp household spending. With prices of essentials (such as food, transport) rising and wages not rising faster, households will be left with little left for discretionary spending.

- **Monetary Policy Forecast:** We expect BoE MPC to remain on hold at 0.25% at the next meeting on 11 May. Though inflation is ticking higher, we think a **premature tightening to arrest inflation may upset growth momentum especially in an environment of slowing growth (due to potential consumer squeeze and falling business investment) and *Brexit* and election uncertainty.** We do however acknowledge that the MPC stance may shift (more dissenters but not enough to form a majority to vote for rate increase) at some stage and such shift could support GBP (as market speculates for tightening). BoE MPC member Vlieghe commented (23 Mar) that inflation doesn't mean rate increase. He elaborated that he needs to see evidence of strong wage growth before considering voting for a rate rise. He added that much of inflationary pressure (headline) was due to GBP's sharp depreciation and the consequential price action via the import price channel on fuel and food. This echoed BoE deputy Governor Broadbent's comments (23 Mar) that there is no material evidence of domestic inflation pressures. He also added that there is no need for interest rate increase soon (5 Apr).

- At the last MPC meeting (16 Mar), though policy rate was kept unchanged at 0.25%, the vote was not unanimous (8-1 voted to hold). Kristin Forbes voted for 25bps hike, she believes that MPC should be nimble to and willing to quickly adjust the appropriate path for monetary policy in either direction as needed. She believes a rate hike now to reduce upside inflation pressures and deliver fresh stimulus if it turned out that BoE had moved too early. The other surprise was that more than 1 other member believes it take little additional upside news to justify tightening. The recent meeting suggests that the BoE stance could be shifting and is preparing markets for a rate hike, possibly sooner than expected (we had initially expected to BoE to remain on hold as recent data suggests slowing momentum while real wages may fall and affect household spending).

- **Latest Fiscal and External Balance Outlook:** UK Chancellor Hammond met budget deficit target for 2016/17. Budget deficit stood at 2.6% of GDP and is smaller than what Office of Budget Responsibility (OBR) expected. This is also the small deficit since GFC. Debt to GDP ratio is now projected to decline from 88.8% in 2017/18 to 88.5% in 2018/19 and 79.8% in 2021/22. The budget took into account fresh updates to 2017 growth forecast (2%, from 1.4% previously).

- UK's current account deficit to GDP narrowed from about -5% of GDP in 3Q 2016 to -2.4% of GDP for 4Q 2016. Massive improvement was due to trade deficit narrowing (thanks to increase in exports amid softer GBP)

- **Key domestic events and issues to watch:** Apr Mfg PMI (2 May); Apr Construction PMI (3 May); Apr services PMI (4 May); Mar IP, trade, BoE meeting (11 May); Apr CPI, PPI, RPI (16 May); Mar jobs report (17 May); Mar retail sales (18 May); public finances (23 May); 1Q GDP (25 May).

- **Technical Outlook:** GBP broke above key resistance (200DMA at 1.2620) on 18 Apr. Last seen at 1.2920 levels. Weekly, daily momentum indicators are bullish bias. Next area of resistance at 1.30 - 1.3055 (38.2% fibo retracement of Jun high to Oct low). Decisive move beyond that area of resistance could potentially see room for further upside towards 1.3430 (50% fibo). Stochastics suggests GBP is approaching overbought conditions. Support at 1.2620 (200 DMA).

AUD: Downside Risks

Forecast	2Q 2017	3Q 2017	4Q 2017	1Q 2018
AUDUSD	0.7300 (--)	0.7500 (--)	0.7800 (--)	0.7800 (--)

No Change to Previous Forecasts

- **Motivation for the FX View:** AUD corrected towards the 0.75-figure, along with the iron ore price correction, in line with our anticipation. Long AUD positioning is still stretched and recent price moves suggest that AUD bears are awaiting the next trigger. Technical cues suggest little directional bias at this point. We still see risks to the downside given positioning, strong bearish seasonality in May and the upcoming event that could be potentially negative for the AUD - the Federal Budget on 9 May. Failing to impress could result in the loss of its highly prized AAA-rated. Pressure might build in the AUD in the lead-up to the event. That could bring the pair towards 0.72. Beyond the near-term, we still look for AUD to head higher towards 0.78 (vs. the USD) by the end of the year, as we expect the demand for commodities to be sustained somewhat on the back of global infrastructure demands.

- Australia may lose its AAA rating this year. Most of the impact on the AUD is likely to be a kneejerk and we even see risks of a near-term pressure in the lead-up amid all the uncertainties. It could be a mild knock on business confidence and a political blow. However, the economic consequence is more nuanced. Australia government debt is fully denominated in Australian dollars so the government is fully able to pay by its debt even if borrowing cost rise. The impact could however be on the banks' credit rating as a downgrade from their current AA- could raise their funding cost. Growth outlook this year seems a tad supported by the improvement in terms of trade though RBA has noted that most of the income could be paid out to foreign owners as dividends. That said, we remain cautiously more optimistic of the growth outlook compared to the past. The recovery in external demand may allow more breathing room for services sector in Australia to fill the void left behind by the mining investment. The improvement in its external balance may boost the government's ability to finance its budget shortfall and avert the loss of its AAA rating within the year.

- **Growth and Inflation Outlook:** The widening trade surplus provides some support for the AUD amid improving terms of trade. That could continue to keep AUD supported on dips. Retail sales dipped -0.1%m/m in Feb, well under the expected 0.3% growth. The month saw a 0.4%m/m fall in purchase of household goods as well as a -2.5% decline in sales of apparel. We continue to watch this print for any further deterioration in the contribution that the household consumption towards national income. The Mar labour report was a solid one with seasonally adjusted employment growth posting a rebound from recent prints. This could be the first sign of bottoming in the labour market but let's not get too carried away by one data point. Afterall, the trend in hiring has been down. The trend in unemployment growth (s. adj) is still up, accelerating from 3.8%y/y to 5.1% in Mar. We flagged this in the last monthly and it was one of the focal points at the RBA meeting. Last available data revealed that ratio of household debt to disposable income is still on the rise while wage growth is still weak. That could weigh on consumption. Spare capacity in the labour market has risen in recent months, capping wage growth, increasing the downside risks to household consumption and growth prospects. Capacity utilization rates in the manufacturing firmed in Mar while that of the services sector softened under the 5-year average.

- For the second time (in a row), Australia's inflation missed expectations. The headline CPI came in at 0.5%q/q, steady from the previous quarter, driven mostly by fuel, housing, health, transport and education. Year-on-year, CPI narrowly missed the median forecast of 2.2% with a print of 2.1%, albeit still an acceleration from the previous 1.5%. Nonetheless, inflation is finally back within RBA's target range of 2-3%. Underlying inflation rose to 1.80%y/y from the previous 1.55%.

- **Monetary Policy Forecast:** We expect RBA to hold rates at 1.5% for the rest of this year. With unemployment still rising, private consumption still soft and housing prices in Melbourne and Sydney still looking frothy, RBA is caught between a rock and a hard place. Even with the recent macro-prudential measures to limit interest-only lending to 30% of new residential mortgage lending along with other strict internal limits imposed, household debt to income ratio is high and unlikely to reverse in the near-term. Hence, we see a high hurdle for RBA to lower cash target rate any lower from the current 1.50%. CPI is headed back towards the RBA target band of 2-3% but food and housing were the main drivers. With underlying inflation still subdued amid slow wage growth, the current inflation trajectory should not be an impetus for a rate action in the near-term.

- Australian bonds are still in demand as investors continue to favour higher yielding, better quality bonds. The Australian sovereign curve saw downward shift in yields across the curve in the past month, last checked on 24 Apr. 10-year was last seen around 2.59%, around 15bps lower from a month ago. With inflation still subdued and mixed outlook on its economic growth trajectory, Australian bonds are less at risk of a rate hike in the medium term relative to other developed nations. That could continue to support the domestic bond demand. With central banks around the world (with the exception of the US) reluctant to allow rates to run much higher, wholesale funding cost for Australian banks are also likely to be capped for now, also lowering the risks for a rate cut. Thus, barring any data surprises, AUD is more likely to be driven by other factors like commodity prices, terms of trade rather than policy rate expectations.

- **Latest Fiscal and External Balance Outlook:** When it comes to the budget, the incumbent government is always wary about losing its AAA sovereign rating. The Mid-Year Economic and Fiscal Outlook

(MYEFO) released in Dec 2016 saw its budget deficit rise by more than A$10bn. Australia kept its top-grade rating at all three agencies but S&P expressed pessimism about the government's ability to return the budget to surplus by end FY2021. There is a real risk that S&P could downgrade Australia at May. However, the rating agency had assured that a one-step rating downgrade on Australia would only affect those states and territories that have AAA ratings (namely New South Wales, Victoria and Australian Capital Territory). Policy-wise, Treasurer Morrison said that the budget will focus on improving housing affordability – package to include a mutual-obligation superannuation plan for first-home buyers, tax breaks for downsizing the family home in retirement, and a social housing plan to ease rental stress (Australian).

- The macro economic assumptions for the budget are crucial. Real GDP growth forecast for 2016-17 is revised lower to 2¾% from previous 3%. Nominal GDP growth is also revised lower to 4½%, taking into account weaker commodity prices and moderate outlook for inflation. The government tries to reduce the share of fiscal spending of GDP From 25.9% in 2015-16 to 25.3% in 2018-19. The economy is very much predicated on how key commodities will perform. With iron ore prices giving up most of its gains since the mid-year budget update last Dec, the gains to the budget is also being eroded. Into the rest of the year, a sustained supportive tone in commodity prices could mean more material income gains for the economy. We even see upside risks to growth that could stem from stronger external demand this year, allowing room for economic rebalancing and domestic services to strengthen.

- **Key domestic events and issues to watch:** Apr M-I Inflation on 1st, RBA meeting on 2nd, Trade on 4th, RBA SoMP on 5th, building approvals and NAB survey on the 8th, followed by retail sales on the 9th as well as the Federal Budget, home loans on 15th, RBA Minutes on the 16th, labour report on the 18th, building approvals on 30th.

- **Technical Outlook:** The short AUD call that we made last month came to fruit and we continue to remain bearish on the currency heading into seasonally bearish May. Weekly, momentum indicators are bearish. This pair needs to head below 0.74570 (50% Fibonacci retracement of the Dec-Mar rally) before the next support around 0.7390, before 0.73 and then perhaps even 0.72.

NZD: Risks Skewed to the Downside

Forecast	2Q 2017	3Q 2017	4Q 2017	1Q 2018
NZDUSD	0.7100 (--)	0.7300 (--)	0.7500 (--)	0.7700 (--)

No Change to Previous Forecast

- **Motivation for the FX View:** We expect **NZD to face downside pressure heading into the month of May** on concerns that US may target the dairy sector (if tariffs are imposed on dairy imports into US, then NZ dairy exports could potentially suffer) while seasonality trends typically indicate that month of May is a negative month for NZD (falling for 7 out of the past 10 Mays since 2007). We **expect NZD to trade in lower range of 0.68 - 0.7050 (as compared to prior month of 0.69 - 0.71).** We caution that a decisive move below 0.68 may open way for further downside towards 0.6650 levels. Resistance remains at 0.7050.

- Despite our expectation for NZD downside risks in May, we are not turning negative on the currency as factors supporting the NZD remain intact: **neutral RBNZ** (no longer on easing stance but yet to hike anytime soon though we are of the view that RBNZ may hike “earlier than sooner”); **better inflation outlook** with 1Q jumping into the 1 - 3% RBNZ target range while longer turn inflation expectation remains anchored at 2% and **optimistic growth outlook** (supported by job growth and tourism spending). In the event US did not impose any tariffs on dairy, the NZD may even rally off the back of diminished concern. We maintain our NZD forecast across the forecast horizon, expecting Kiwi to gradually rise into 1Q 2018, due to RBNZ rate hike expectations and domestic resilience.. Our fair value (fast tracking model based on real yield differentials, current account differentials and reflation proxy) puts Kiwi at 0.76.

- **Growth and Inflation Outlook:** The **outlook on NZ’s economy remains optimistic** (RBNZ expects 2017 GDP to be 3.7%), supported by strong labor market (4Q unemployment rate at recent lows of 5.2% while job creation outpaced population growth), pipeline of construction activity (expect an acceleration of activity on Kaikoura rebuilding efforts post-Earthquake), tourism spending (direct contribution to GDP at 5.6%; a further 4.3% is indirectly contributed; while tourism spending accounted for 20.7% of NZ total export earnings) amid accommodative monetary policy (OCR at record low of 1.75%). We still expect the NZ economy to outperform most of G7 economies this year.

- Growth is expected to return in 1Q 2017 as wet weather factors (which resulted in the dip in 4Q GDP) are deemed to be temporary. There are also signs that activity picked up - Manufacturing and services PMI expanded at faster pace in Mar. 4Q GDP surprised to the downside (+0.4% q/q vs. +0.7% Consensus), due to the drag on manufacturing and agricultural production (amid wet weather conditions) as well as mining sector (owing to closure of the Maari oilfield). 2016 annual growth eased to 2.7% y/y.

- **1Q CPI surprised to the upside,** rising 2.2% y/y (vs. 2% Consensus vs. +1.4% in 4Q) and 1% q/q (vs. 0.8% Consensus). The move higher was driven by fruits/vegetables and cigarettes/tobacco components. This is the first time since 3Q 2011 that CPI has risen above the mid-point of RBNZ's 1-3% target band. We expect firmer CPI to result in shifts in market expectation for a "sooner rather than later" RBNZ rate hike.
- **Monetary Policy Forecast:** We expect RBNZ to maintain an accommodative monetary policy, with OCR on hold at record low of 1.75% at the upcoming meeting on 11 May. Accompanying monetary policy statement is likely to remain "neutral" and re-emphasize the need for weaker exchange rate to achieve more balanced growth. New forecasts for growth, inflation and rates will be released in this upcoming meeting – watch out for bullish assessment to growth and inflation. We expect the rate profile to be revised, pricing in higher rates than previously anticipated.
- We continue to expect RBNZ to raise rates earlier than their own forecast – Mar 2020. We believe the RBNZ should be one of the next major central banks to raise rates as inflation is already showing further signs of uptick owing to higher commodity prices, construction-related cost pressures and strength of the domestic economy. NZ OIS shows markets are expecting a hike as early as Feb 2018.
- At the last RBNZ meeting (24 Mar), MPC kept rate on hold at 1.75%, as widely expected at the last meeting on 24 Mar. Accompanying statement is "neutral", in line with Wheeler's speech (2 Mar) – confirming the shift to a neutral policy stance and describing the balance of risks to inflation as even (skewed to the upside for domestic growth and downside for global growth). He acknowledged the 4% depreciation in the NZD TWI since Feb and partly attributed the decline to weaker dairy prices and interest rate differentials. He stressed again that further depreciation is needed to achieve more balanced growth. On inflation expectations, RBNZ believes longer term expectations remain well anchored at around 2%.
- **Latest Fiscal and External Balance Outlook:** Government finances continue to perform well above expectations with OBEGAL showing a surplus of $1.41bn (vs. forecast surplus of $498mil) for the 8-months to Feb 2017. This was due to higher than forecasted tax revenue (from corporate taxes) while expenses were lower than expected (in relation to Kaikoura earthquakes where expenses have yet to be quantified).
- 4Q current account deficit narrowed to $2.3bn (vs. revised $5bn in 3Q). The improvement was due to services balances (thanks to tourism). For 2016 NZ current account improved to -2.7% of GDP (vs. -3.4% of GDP in 2015). Net external debt position excluding financial derivatives and equity was $143.5 bn (or 55% of GDP at end-2016), down from $149.1 bn (or 58.2% of GDP) as of 3Q 2016. The narrowing of external debt position was due to faster increase in external

lending (increased by \$6.3bn) over external borrowing (Increased by \$649m).

- **Key domestic events and issues to watch:** 1Q Labor market report (3 May); RBNZ meeting, Apr food prices (11 May); 2Y inflation expectations (12 May); 1Q retail sales (15 May); Apr trade (24 May). GDT auctions on 2 and 16 May.

- **Technical Outlook:** NZD fell on concerns that Trump could next target dairy after targeting Canadian softwood lumber. Pair was last seen at 0.6910 levels. Weekly, daily momentum indicators are bearish bias. Next area of support at 0.6880 - 0.69 before 0.6810 (50% fibo retracement of Sep 2015 low to 2016 high). We caution that a break below 0.6810 support may open room for further downside towards 0.6650. Resistance at 0.71 (23.6% fibo). Play the range, but with bias to the downside.

JPY: No Let Up In Asset Purchases

Forecast	2Q 2017	3Q 2017	4Q 2017	1Q 2018
USDJPY	108 (--)	110 (--)	113 (--)	113 (--)

No Change To Previous Forecasts

- **Motivation for the FX View:** Our bearish view on the JPY has not changed. This is even though the JPY has been the best performing currency in the Asian space so far this year, rising 7.1% against the USD. We continue to look for the JPY to remain on the depreciation trend ahead as we still expect the divergence in monetary policy between the US and Japan to remain intact. This should widen the yield differentials between the UST and JGB, albeit more gradually, and lift the USDJPY higher in the next three-six months.

- The gains in the JPY so far can be attributed to doubts about global reflation trades, leading to ongoing re-positioning of long-USD bets, and some safe-haven flows. This was reflected in the inflow of foreign funds to Japanese assets amounting to JPY1.76tn in the first two weeks of Apr (latest data available). Meanwhile, local investors sold off JPY3.12tn in foreign assets during the same period and probably repatriated the funds back into Japan. Taken together, these have led to some unwinding of short-JPY bets as well, putting upside pressure on the pair. Nevertheless, we expect this unwinding to be short-lived and for short-JPY to pick-up once geopolitical tensions and risks subside. Latest CFTC data shows short-JPY bets intact though waning, suggesting bets are still for further JPY deprecation ahead.

- Despite market rumblings about the need for the BOJ to articulate an exit strategy, we doubt that the central bank is anywhere close to ending its ultra-loose monetary policy. This view is shared by BOJ governor Kuroda who recently commented that the BOJ's "very accommodative monetary policy" will continue and the current pace of asset purchase to be maintained for some time. This suggests, as we had previously written that the BOJ is in no hurry to provide an exit strategy. The governor further reiterated that monetary policy is not constrained by "the fact that (the BOJ has) acquired 40 percent of JGBs already or that (its) balance sheet is about 80 percent of GDP". Thus, the policy bias remains for the continuation of existing monetary easing and low domestic interest rates for as long as the 2% inflation target is not achieved. This then should continue to put downward pressure on the JPY.

- Given the BOJ still on easing mode and the Fed on a tightening bias, further monetary policy divergence between the two is to be expected. We expect the BOJ to maintain its current policy stance for the foreseeable future, while the Fed is expected to hike rate again at its Jun meeting. Even if the Fed does not tightened even more than expected, this divergence in policy should see yield differentials between the UST and JGB continue to widen, putting downside pressure on the JPY and boosting the USDJPY. In addition, global reflation trades could re-emerge should Trump manage to push through his tax reforms and infrastructure spending program. This could result in yield differentials between the UST and JGB widening even further and be supportive of a higher USDJPY.

- Further BOJ easing measures in 2017 appears unlikely for now but cannot be ruled out completely. We nevertheless expect the BOJ to stay on hold for now. But should inflation fail to gain traction going into 2018, we cannot discount the BOJ unleashing even more easing measures to lift inflation towards the BOJ's 2% target. The easing measures could include cutting interest rate further to -0.3% (from -0.1% currently) and increasing asset purchases of ETFs and J-REITs and other instruments to JPY10tn and JPY6tn.

- Despite widening yield differentials, we do not expect the UDJPY to climb unconstrained in 2017. We expect the pair's upside to be capped by several factors. These factors include persistent current account surpluses, safe-haven plays and continuing speculation of a BOJ tapering. The current account has been in persistent surplus and the first two months of 2017 was no different, registering a surplus of JPY2.88bn. In addition, geopolitical tensions in Syria and on the Korean peninsula, concerns over rising protectionist sentiments, and political uncertainties in the EU could spur safe haven plays. Though this is unlikely and not our base case, there is speculation that the BOJ will have to embark on tapering this year as it runs-up against operational limits where there could be greater demand for JGB than supply. These should work together to cap USDJPY upward trajectory.

- **Growth and Inflation Outlook:** The economic recovery remains underway but at an uneven pace. Industrial production accelerated by 4.7% y/y in Feb (Jan: 3.2%) – a pace not seen since Mar 2014. Core machinery orders though slipped by 0.9% y/y in Feb after rising by 8.6% in Jan. The global cyclical recovery continued to lift exports to its strongest pace since Jan 2015, up 12% y/y in Mar from 11.3% in Feb. Imports also accelerated by 15.8% y/y in Mar from Feb's 1.2% - the third straight month of increase, signaling a pick-up in domestic demand. As we had previously written, we expect the economy to grind along for the rest of the year so long as private consumption continues to lag. The economy is also unlikely to find much support from the record FY2017 budget of JPY97.45tn as most of the budget has been allocated for military expenditure, debt-servicing expenses and social services cost. Just JPY5.98tn has been set aside for public and other works. Thus, the economic recovery is likely to limp along for the rest of the year. In its outlook report, the BOJ expects GDP to come in at 1.6% and 1.3% in FY2017 and 2019 respectively.

- Already in the third month of 2017, there does not appear to be any signs of inflation gaining traction. Headline inflation rose by 0.2% y/y in Mar, the same pace as in Feb, helped by higher oil prices. This drove transport cost up by 3.0% y/y in Mar and moderated the decline in utility costs (Mar: -0.7% y/y vs. Feb: -2.1%). However, moderating food prices (Mar: 0.6% y/y vs. Feb: 0.8%) mitigated these increases. Core inflation (headline inflation excluding fresh food) accelerated by 0.3% y/y in Mar from 0.2% in Feb, the third consecutive month of increase that was last seen in 2015. Nevertheless, these price increases are still far away from its 2% inflation target. With private consumption still sluggish and wage growth constrained, inflationary pressure remains limited. In addition, the favored gauge of the BOJ – 'core-core' inflation (headline inflation less fresh food and energy prices) reversed gear, falling by 0.1% y/y in Mar after rising by 0.1% in Feb. With the BOJ's 2% inflation target still a distant away, the easing bias in policy should continue. Given lack of significant traction in inflation, the BOJ revised down its FY2017 core CPI forecast to 1.4% from 1.5% previously and expects FY2018 and FY2019 core CPI to come in at 1.7% and 1.9% respectively. The BOJ still expects CPI will reach 2% only around FY2018 (i.e. Apr 2018-Mar 2019).

- **Monetary Policy Forecast:** Recent remarks by BOJ governor Kuroda that the central bank's "very accommodative monetary policy" will continue and the current pace of asset purchase to be maintained for some time suggests in no hurry to publicly articulate an exit strategy. These comments were reinforced by Deputy Governor Iwata's testimony to the Diet on 25 Apr that revealed the BOJ's internal debates on an exit strategy but which it felt was too premature to be public articulated. Thus while the ultra-loose monetary policy is likely to remain intact, the central bank is also thinking of the day it would end this policy and is working towards an orderly exit. At his press conference after the BOJ policy decision on 27 Apr, he not only reiterated that the BOJ will keep taking necessary policy steps to hit the inflation target, but that it was "too soon to discuss BOJ exit".

- The governor further reiterated that monetary policy is not constrained by "the fact that (the BOJ has) acquired 40 percent of JGBs already or that (its) balance sheet is about 80 percent of GDP". Moreover, the recent nomination of two "reflationists" – namely banker Hitoshi Suzuki and economist Goshi Kataoka - to the BOJ board to replace two outgoing dissenters of the current policy suggests that PM Abe preference for the continuation of aggressive monetary stimulus. Thus, the policy bias remains for the continuation of existing monetary easing and low domestic interest rates for as long as the 2% inflation target is not achieved. Thus, the policy bias remains for the BOJ to its current policy framework of QQE with Yield Curve Control that it implemented in Sep 2016. This framework has short-term interest at -0.1% and the yield of the 10Y JGB targeted at about 0%.

- We expect the BOJ to refrain from adding to its policy measure for now as it focuses on achieving a “normal” yield curve through control of both the short- and longer-terms interest rates. We also expect the BOJ to maintain the pace of JGB purchases at around JPY80tn. While the BOJ could ease policy further, we believe such a move would come only to ensure that inflation gains traction to meet its 2% inflation target. Otherwise, such moves are not imminent. The additional measure that the BOJ could unleash includes cutting interest rate further to -0.3% (from -0.1% currently) and increasing asset purchases of ETFs and J-REITs and other instruments to JPY10tn and JPY6tn.

- **Latest Fiscal and External Balance Outlook:** The FY2017 budget of JPY97.45tn cleared its final hurdle when it was passed by the Upper House of parliament on 27 Mar. The Lower House had already given its approval in Feb. As note previously, the budget was a 0.8% increase from FY2016 with the bulk of it allocated for military expenditure, debt-servicing expenses and social services cost. Together, they account for slightly over 60% of the total budget. Of the total, only JPY5.98tn is set aside for public and other works that would directly impact the economy. The FY2017 takes effect on 1 Apr 2017.

- After a slow start to the year, the current account (CA) surplus widened in Feb to JPY2.81tn in Feb from JPY0.07tn in Jan. This was due to the larger surpluses in the goods and services account (Feb: JPY1.01tn vs. Jan: -JPY1.09tn) and the primary account (Feb: JPY1.98tn vs. Jan: JPY1.27tn). The financial account surplus rebounded to JPY1.78tn after sliding into a deficit of JPY1.54tn in Jan. The rebound could be attributed to the stronger FDI inflow of JPY2.14tn (Jan: JPY1.11tn), smaller portfolio outflow of JPY2.86tn (Jan: -JPY4.71tn) and jump in the ‘other investment account’ of JPY1.68tn (Jan: JPY0.38tn). Consequently, the overall balance of payments (BoP) recorded a surplus of JPY3.55tn in Feb vs. the deficit of JPY3.07tn in Jan.

- **Key domestic events and issues to watch:** Preliminary GDP print for 1Q 2017 will be released on 18 May. While there is no BOJ meeting in May, we still have the minutes of the 15-16 Mar meeting on tap 2 May as well as the summary of opinions of the 26-27 Apr meeting on 10 May. BOJ governor Kuroda speaks at the Global Think Tank summit in Yokohama on 2 May, while BOJ board member Harada speaks as a panelist in Tokyo on 12 May. JGB auctions in May: 10-year (9 May), 30-year (11 May), 5-year (16 May), 1-year (17 May) and 20-year (18 May).

- **Technical Outlook:** USDJPY broke out (high) of the falling wedge formation, at time of writing. Last seen at 111.30 levels. Daily momentum and stochastics continue to indicate a bullish bias. USDJPY needs to trade decisively past 111.80 (50 DMA, 50% fibo retracement of Mar high to Apr low) for further upside to regain momentum towards 112.70 (61.8% fibo). Failing which, USDJPY may slip back towards 109.90 levels (23.6%), 109 (200 DMA).

CNY: Sell in May?

Forecast	2Q 2017	3Q 2017	4Q 2017	1Q 2018
USDCNY	6.95 (6.96)	7.01 (7.02)	7.04 (7.05)	7.04 (7.05)
USDCNH	6.95 (6.96)	7.02 (7.03)	7.05 (7.06)	7.04 (7.05)

Previous Forecast in Parenthesis

- **Motivation for the FX View:** USDCNY is getting little direction cues from the USD recently, trapped between the range trades of the USD and the strength of the JPY that weighs on the pair. In the absence of USD strength, the CFETS RMB index has been on a moderate decline towards the 93-figure. While the rise in FX reserves suggest that capital outflow has slowed somewhat in Mar, the recent underperformance of the stock market and the sell-off in bond markets in anticipation of tightening/deleveraging measures suggest that risks to the yuan remain to the downside. PBOC had eased capital controls a little at mid-Apr. While the slight tweak underscores their eagerness to proceed further on capital account liberalization, the small move also suggests that the authorities prefer to maintain some sort of caution over markets' expectations for further yuan depreciation. With the USD tempered by Trump's random comments and a lack of progress in infrastructure projects and tax reforms by the White House, China may have a window of opportunity to ease capital controls in the 3Q or earlier part of 4Q to boost the allure of its onshore financial markets to foreign institutional investors, in the hope of drawing more capital inflows.

- The 12month USDCNH forward points continue to drift lower to 1670 as we write. This underscores 1) the lack of USD cues; 2) market players' confidence in the central bank to keep the RMB stable. This can continue as long as the USD and US rates do not see a sudden surge. In the midst of the current calm, China has been encouraging foreign inflows. Capital outflow is a concern in the backdrop as more Chinese nationals seek returns overseas and gain the USD exposure, in addition to the requirements of the One Belt One Road initiative. Bear in mind that MSCI has proposed a new consultation to include China's A-shares in its EM index. Their new proposal would reduce the number of companies to 169 from the previous 448 under the proposal last year by including only large cap companies. CNH is to be used for index calculation instead of the originally proposed CNY in order to "minimize currency drag and potential tracking error due to divergence of CNY and CNH". The weight of the A-shares will also be reduced to 0.5% from the previous 1.0%. This could raise the chances of China's A Shares inclusion into the MSCI EM index and boost foreign inflows into China's domestic equity market. Further capital account liberalization may be required for investors to say yes to the MSCI proposal.

- **Our monthly Maybank vulnerability score** (using 9 economic and market variables: GDP, Yield, Politics, Current Account, Inflation, Fiscal, Equity Valuation, Population, Reserves) showed the score for China deteriorated to 5.0 (with 1 being the best and 9 being the worst) from previous 4.9 as the score for fiscal partially negates the deterioration in inflation and fiscal in the past month.

- **Growth and inflation outlook:** China has had a pretty good quarter, posting a firmer than expected growth number of 6.9%y/y, stronger industrial production, retail sales and even urban fixed assets investment for Mar. Our economist took the opportunity to upgrade the growth forecast for the year, expecting China to see a growth of 6.7% from the original projection of 6.5%. While the contribution of final consumption expenditure consumption has been unexpectedly strong, we also expect investment to remain supportive of the growth momentum.

- PPI softened to 7.6%y/y in Mar from previous 7.8%, in tandem with the softer base metal prices. On the other hand, CPI edged higher to 0.9%y/y from previous 0.8%y/y. Decline in food costs dragged on the consumer prices headline. ***With food and fuel inflation rather anchored, it is possible for CPI to continue to lag that of PPI for now. In addition, the recent iron ore and oil price moves suggest softer PPI prints for the next few months.***

- **Monetary Policy Forecast:** For so far this year, PBoC has raised 1-day SLF rates by 55bps, 7-day and 1 month by 20bp, MLF rates by 10bps and 7-day reverse repo by 20bps. More is expected, especially after China posted a rather strong set of data prints for Mar. This is likely meant to reinforce the message that the government desires less debt taking, risk taking and more deleveraging. The amount of rate increase suggests that the debt-laden economy is not able to withstand too much tightening and with Mar economic data having a seasonal boosts, the release of Apr numbers are required for PBOC to unleash the next round of tightening. Recall that PBoC had stated in the (Central Economic Work Conference, 4Q Monetary Report) that monetary policy will be "prudent and neutral" and the central bank is certainly sticking to this theme in its recent action.

- **Latest Fiscal and External Balance Outlook:** From the NPC, Finance Minister Xiao Jie announced that budget deficit for the year is retained at -3% of GDP for 2017 though the absolute deficit amount is raised CNY200bn to RMB2.38trn this year. Government debt is low at 36.7% of GDP, local government debt ceiling is to be raised by 10%. China aims to reduce the VAT brackets from four to three. China to target lowering CNY1trn in corporate tax and expenses including the broadband fees, electricity tariffs and logistics. At a state council in Apr, Premier Li Keqiang unveiled more details on tax cuts by lowering VAT rates for natural gas and agricultural items to 11% from previous 13%, lending a boost to demand. The insurance sector also received a boost as individuals who have purchased commercial health insurance could be allowed an exemption of up to CNY2400 from personal income tax every year. Tax break measures were also passed for small companies with annual taxable revenue of CNY500K and below.

- China is still at a nascent stage of looking into public-private-partnership (PPP). Implementation is to speed up with the third batch of MoF PPP taking 11 months to start compared to 15 months for the first batch. This could boost private investment with less fiscal commitment from the government.

- Current account surplus narrowed tremendously to U$11.8bn in 4Q from previous U$37.6bn as imports jumped. BOP has been recording outflow via loan, trade credit and currency deposit in the month that amounted to U$116bn. Expect this outflow to narrow into 1Q given that China imposed more capital account restrictions for individuals and corporates to remit or invest overseas since the start of the year. FX reserves have risen in Mar and PBoC was even comfortable enough to ease some capital restrictions. SCMP reported that PBoC has now allowed banks to process outbound yuan payment and remittance requests for their corporate and individual clients. The central bank had required the procedures to meet certain requirements like a show of outbound yuan that match inbound to gain approvals.

- **Key domestic events and issues to watch:** NBS Mfg PMI due on 30st Apr, Caixin PMI on 2nd May, foreign reserves on 7th, trade on the 8th, CPI, PPI on 10th, monetary data on 10-15th. Apr retail sales, FAI, industrial production on 15th. Property prices on 18th. Industrial profits on 27th.

- **Technical Outlook:** USDCNH has been hovering within a tight range of 6.86-6.92 for the past month and more recent sessions see a gradual drift higher, last seen around 6.90. The 50-DMA has been guiding the pair higher. Risks have turned higher as we move into May, a seasonally bullish month for USD. We hold our view that USDCNH could move higher. Resistance at 6.90 again before 6.92 and then 6.96. Support at 50-DMA at 6.88 before 6.86.

KRW: Election & its Implication on Foreign Policy

Forecast	2Q 2017	3Q 2017	4Q 2017	1Q 2018
USDKRW	1140 (--)	1150 (--)	1160 (--)	1170 (--)

No Change to Previous Forecast

- **Motivation for the FX View:** USDKRW is expected to be caught between politics (Presidential elections on 9 May and its impact on foreign policies – US-Korea alliance, North Korea aggression and China's travel ban on THAAD installation) and fund inflows off the back of exports recovery amid rising current account surplus. Political risk is multi-fold and challenging and could dampen investor sentiment (to some extent) and limit gains in KRW. Seasonality trends for May also tend to favor a weaker KRW (currency typically fall in 7 out of the past 10 Mays since 2007). On the other hand, Korea's exports recovery (Korea's exports is about 50% of GDP), continued foreign fund inflows into KOSPI and hopes of Trump's spending and tax reforms (support for appetite for risk) amid well contained Fed rate hike expectation for 2017 may have created a sweet spot for KRW to stay supported. We see 2 way risks between 1100 – 1150 range for the month of May.

- South Korea's Presidential Election is scheduled for 9th May. Opinion polls (since Mar) are showing that votes are swinging between Moon Jae-In (from Democratic or Minjoo party) and Ahn Cheol-soo (People's Party). Most recently (as of 26 Apr), Moon's lead over Ahn appear to have widened (Hankook Research poll shows Moon at 40.4% while Ahn was at 26.4% while Metrix Survey showed Moon at 40.3% vs. Ahn at 29.6%). Moon's lead was attributed to its focus from competition to state planning while Ahn's decline was due to his performance in the series of Presidential debates which some claimed were unprofessional and negative allegations involving his campaign team and his wife.

    - Moon, the front-runner from the beginning, is a disciple of "sunshine policy" – and believes in advocating a softer line on North Korea, backing investment aid and diplomacy. He was initially against THAAD installation but back-tracked after being criticized by the Conservative candidates during a televised debate (20 Apr). He also attempted to guard against criticisms that he has anti-American leanings to avoid damaging the US-South Korean alliance, in saying "need to closely talk and coordinate with our ally the United States".

    - Ahn positions himself as a centrist and is trying to strike a balance to appeal to the young and progressive voters with his stance on corruption and economy while reassuring the Conservative voters that S. Korea is safe under his government (while he favors reaching out to North Korea, he is also in favor of THAAD installation and accuses China of not doing enough to stop N.Korea's nuclear program).

    - The other lower placed candidates (as indicated by polls) are Conservative: Hong Joo-Ryo from Liberty Korea party (formerly known as Saneuri party but rebranded to distance the party from now-defunct former President Park), which is placed in a distant third position and Yoo Seong-min, from the Bareun party (is a branch split off the Saneuri party), whom has yet to break above 5%.

- Though Korea elections typically may not result in a big impact for markets (as compared to elections in the western world UK, France, US), we think this election may be slightly different. Previous Presidents in the past 10 years were from the Conservative camp - favors strong US-South Korea alliance and typically favors a tough approach to North Korea. But the upcoming election sees 2 candidates to the left of the Conservative party. In particular front-runner Moon is a disciple of "Sunshine policy" and may be seen as advocating a softer stance on North Korea. This may anger the Americans and subject the US-South Korean alliance to risks. His caution against the installation of THAAD may also anger US but could appease China – which could mean the removal of travel ban to South Korea (a plus for tourism revenue and supports growth). Geopolitical tensions may ease and could be supportive of further gains in KOSPI and KRW, in this scenario. (Though we understood some may argue that US could withdraw from defending in the region and this could worsen the security/ geopolitical tension but we argue that back in 2000s when US-South Korean alliance was less strong, North Korea presented less dramatic threats and today, China is also playing a greater role in regional security).

- We **maintain our USDKRW forecast over the forecast horizon and keep the upward trajectory in USDKRW** into 4Q 2017 as we expect markets to reprice Fed rate hike expectation when Trump's plan on tax reforms and fiscal spending take shape towards end-2017.

- **Our monthly Maybank Vulnerability score** (using 9 economic and market variables: GDP, Yield, Politics, Current Account, Inflation, Fiscal, Equity Valuation, Population, Reserves) for S.Korea deteriorated to 7.1 (vs. 6.2), due to politics and fiscal.

- **Growth and Inflation Outlook:** 1Q 2017 prelim GDP came in stronger than expected (+0.9% q/q vs. 0.8% expected vs. 0.5% in 4Q), owing to strong pick-up in exports and capital investment. This is the fastest quarterly growth since 2Q 2016. Per day exports for the first 20 days of Apr continued to jump higher (+19.2% y/y) - its highest level since Aug 2011, driven by ship exports. By destination, exports to Europe and US rebounded sharply while exports to China moderated. BoK official said consumption hurt by drop in Chinese tourists (due to China's travel ban). Finance Minister said that economy is not out of the woods, in response to better than expected 1Q GDP, saying that trade protectionism led by US, rising geopolitical tension are key economic uncertainties while corporate restructuring is still ongoing (we believe this refers to Daewoo shipbuilding).

- The BoK expects S.Korea's economy to grow at 2.5% (vs. 2.7% previously forecasted) in 2017. Slowing consumption is the primary factor amid political uncertainty (leading to the decline in consumer confidence). Ongoing corporate restructuring on troubled industries such as shipping and ship-building and the potential risks of protectionist-related measures (from US) may continue to weigh on growth.

- **Headline inflation for Mar** rose to 2.2% (vs. 2.1% Consensus vs. 1.9% in Feb). This is the highest level since Jun 2012 due to base effects. Finance Ministry said that further rise is unlikely considering the recent moves to control oil prices and stabilise prices of agricultural goods. We continue to expect inflation to stay firm but moderate from recent highs as base effects from oil prices are likely to ease going forward. Core inflation slipped to 1.4% y/y (vs. 1.5% y/y prior).

- **Monetary Policy Forecast**: We expect BoK to keep monetary policy accommodative, with policy rate on hold at record low of 1.25%, at its upcoming meeting on 25 May. There is no strong case for BoK to raise rates as recent rising pressures (headline CPI) were due to base effects from oil prices and is likely to ease going forward and the domestic economy remain sluggish amid slowing private consumption and ongoing corporate restructuring. There is also little incentive to stimulate the economy via lower rates as household debt remains high and BoK does not want to fuel higher debt. BoK report on financial stability showed debt owed by so-called high risk households stands at 7% of total debt in 2016 (up from 5.7% in 2015). This group of people refers to those holding more debt than the value of assets and has a debt service ratio above 40%.

- **Latest Fiscal and External Balance Outlook:** Current account surplus widened to 8.4bn in Feb (vs. 5.28 bn in Jan) due to goods trade surplus widening. This is the 60th consecutive month of surplus.

- Korea's sovereign debt is expected to increase to KRW682.4tn by end-2017, from KRW641tn. Government debt now stands at 44.8% of GDP. The rising debt has to do with tax cuts and increasing welfare spending made during former President Lee's era. The National Assembly Budget Office estimates government debt will rise to KRW800tn in 3 years' time.

- **Key domestic events and issues to watch:** S. Korea releases Apr trade data (1 May); CPI, PMI (2 May); first-20 days of exports data (21 May); BoK meeting (25 May); and Apr Industrial Production (31 May).

- **Technical Outlook:** It was a month of 2 halves for USDKRW - traded near 1150 before turning lower. Last seen at 1125 levels. Bearish momentum on weekly and daily chart remains intact. Next support at 1110 (2017 low) before 1098 levels (61.8% fibo retracement of 2014 low to 2016 high). Resistance remains at 1142 (200 DMA) before 1154 (38.2% fibo).

SGD: Pullback

Forecast	2Q 2017	3Q 2017	4Q 2017	1Q 2018
USDSGD	1.4100 (--)	1.4200 (--)	1.3950 (--)	1.3950 (--)

No Change to Previous Forecasts

- **Motivation for the FX View:** The SGD is on track to end Mar on a positive note amid fading global reflation trades, the ongoing synchronized recovery in exports in the region and possible monetary policy convergence with the US. The SG has gained 0.2% against the USD so far in Apr. Gains though have been stronger since the start of the year. Year-to-date, the SGD has risen by an even stronger 3.8% against the USD.

- Going into May though the outlook for the SGD is cloudier. An examination of price action in May for the past 10 years suggests downside pressure on the SGD. This move could coincide with the expected resurgence in USD underpinned by steady US economic growth, the ongoing normalization of US rates with a hike possibly in Jun and then another in 2H, expectation of Fed's unwinding of its QE, and possible EUR pullback amid disappointment with ECB policy. We also cannot discount the possibility that the global reflation trade could re-emerge, narrowing yield differentials between the UST and SGS, which could spur fund outflows from Singapore back to the US, boosting USDSGD.

- We do not expect though that this sell-off will be overly aggressive. The improvement in the macroeconomic fundamentals of the economy led by the synchronized recovery in exports in the region that is boosting investment sentiments and also the SGD. Support for the SGD should also come from the government's mildly expansionary fiscal policy, still accommodative monetary policy, its triple-A status and persistent balance of payments surpluses. In the midst of mild USD strength, all of these should temper any sharp climb in the USDSGD.

- In addition, the ongoing unwinding of stale long-USDSGD positions amid doubts about global reflation trades should be supportive of the SGD. This should continue to allow the SGD to depreciate at a more gradual pace. It is also looking unlikely that the Fed would be aggressive in hiking rates in 2017 and this should continue to lend support to Singapore bonds and equities that in turn provides some support for the SGD. Though data on foreign ownership of Singapore equities and government debt is lacking, inference from the gains in the STI as well as lower bond yields (with the exception of the shorter end) suggests there were foreign inflows. Year-to-date, the STI is up nearly 10% while yields for government bonds are lower by 2.6-43.6bp.

- Though the MAS statement for its Apr meeting did not remove the phrase "for an extended period" to signal a hawkish tilt, our house view remains for a possible adjustment in Oct. Our view is premise on signs that inflation, especially core, is re-accelerating and economic momentum is picking up. Consequently, we may see a policy shift to a "mild appreciation bias" as inflation, including core, and growth gain traction. This policy shift towards a tightening would be supportive of the SGD.

- We maintain our bearish view of the SGD. We continue to expect the pair to grind mildly higher to 1.41 and 1.42 by end-2Q and -3Q and then holding steady at 1.3950 for both end-4Q 2017 and 1Q 2018.

- **Singapore's monthly Maybank Vulnerability score** (using 9 economic and market variables: GDP, Yield, Politics, Current Account, Inflation, Fiscal, Equity Valuation, Population, Reserves) held steady at 4.1. This should be supportive of the intrinsic value of the SGD. Our model shows that the SGD NEER was last seen 0.11% below the mid-point implied at 1.3950. Upper bound is implied at 1.3671 while lower bound is now at 1.4230.

- **Growth and Inflation Outlook:** Preliminary GDP (based on first two months' data) for 1Q 2017 showed the economy expanding by 2.5% y/y, a moderation from 4Q 2016's 2.9%. On a q/q seasonally adjusted annualized basis, GDP contracted 1.9% from 4Q 2016, reversing the 12.3% surge in 4Q 2016. Growth in 1Q was driven mainly by manufacturing (+6.6% y/y), especially electronics and precision engineering, as well as a pick-up in services, which rose by 1.5% y/y (4Q: 1.0%). Dragging growth lower though was construction, which fell 1.1% y/y. The surge in industrial production to 10.2% y/y in Mar (Feb: revised down to 10.2%) brought 1Q 2017 manufacturing growth to 8.0%, higher than the advanced GDP estimates of 6.6%. Our economic team expects manufacturing alone to increase overall GDP growth by around 0.3 percentage point assuming all other things held unchanged. This then suggest that 1Q 2017 GDP could be upgrade to 3.0% (from the preliminary estimates of 2.5%) as services could also be revised upwards due to healthy print in Mar. There are emerging signs that services growth has broadened to financial, business and wholesale services from just largely the trade-related services segments in 4Q 2016, namely strong bank lending activities, property transactions and no-oil re-exports. This improvement in services should lend support to stronger growth in 2017. Our economic team is holding their full-year GDP forecast at 2.5% for now, but is looking to upgrade their forecast when final 1Q 2017 GDP is released on 17 May.

- Headline and core inflation took a breather in Mar, holding steady from Feb. Headline inflation rose by 0.7% y/y in Mar on the back of higher private road transport costs (+6.9%). Meanwhile core inflation (which excludes accommodation and private transport) climbed 1.2% y/y as services inflation rose slightly (+1.6%). The Mar prints brought 1Q 2017 headline and core inflation to 0.6% and 1.3% y/y respectively vs. 4Q 2016's 0% and 1.2%. Inflationary pressures are expected to accelerate for the remainder of the year, underpinned by higher commodity prices and a cyclical recovery, as well as the planned administrative price increase (such as the hike in service & conservancy charges and water prices). Our economic team is maintaining their average headline inflation forecast at 1.2% (MAS forecast 0.5%-1.5%) and core inflation forecast at 1.6% (MAS forecast 1%-2%) in 2017, at the upper half of MAS forecast range.

- **Monetary Policy Forecast:** The MAS maintain its 'neutral policy' stance at its recent Apr meeting as expected by market and ourselves. The slope of the SGD NEER policy was kept at zero percent, with no change to the width of the policy band or the level at which it is centered. The forward guidance that the neutral policy stance is appropriated for "an extended period" was maintained, against expectations of some participants in the market that this phrase would be removed to signal a tightening bias. According to the Mas Macroeconomic Review released on 27 Apr, growth remained volatile and uneven with domestic-oriented sectors largely subdued. This together with the soft labor market is likely to curb Inflationary pressures. The inability of firms to pass on higher business cost to consumers also suggests limited consumer price upside.

- Despite the dovish statement, our house view remains for a possible adjustment in the MAS policy stance at the Oct meeting, where we expect a shift to a "mild appreciation bias". This view is premised on our economic team's expectations that inflation could surprise on the upside this year due to the uptick in administrative prices (water, service and conservancy charges) and higher commodity prices (including both oil and food). At the same time, our economic team is also expecting 2017 growth to strengthen, allowing greater flexibility for the MAS to adjust policy.

- Our Taylor Rule estimates appear to suggest that a shift to a "mild appreciation bias" would be appropriate. Our estimates show that the SGD NEER is expected to strengthen ahead. Based on our analysis, the current policy parameters could be adjusted at the next policy meeting in Oct. This should temper inflationary pressures that could arise in the next six-to-nine months amid a synchronize recovery in exports in the region and possibility of stronger global growth led by the US.

- The USDSGD slipped to a new low for 2017 at 1.3907 (on 25 Apr) – a level not seen since Nov 2016 – amid a moderation in the USD. Pair has since rebounded but remains below the 1.40-levels at the point of writing. This oscillation in the USDSGD so far this year has seen the 3-month SOR (3MSOR) coming off from 1.0152% on 4 Jan to hit a low of 0.7370% on 23 Jan before climbing higher to reach 0.8397% as of 26 Apr. Similarly, the slide in the 3-month SIBOR (3MSIBOR) has been more gradual with the rate falling from 0.9689% at the start of the year to hit a low of 0.9391% on 24 Feb before climbing gradually to hit a new high for 2017 of 1.0015% on 13 Apr. The 3MSIBOR has since eased off to hover just a tad off the 1.0% level at 0.9988% as of 26 Apr. The more modest rise in rates suggests that the rise in mortgage rates is unlikely to be significant for now. Deposit rates (for 12-month fixed) have not risen since end-Jan but has slipped lower to 0.33%. This continues to suggest that risks related to interest rate increases affecting financial and economic stability, particularly in interest rate- and property-related sectors, seems limited for now.

- Upward pressure on domestic rates remains given our expectations of two more Fed rate hikes for the remainder of 2017. US 3MLIBOR continues to edge higher and is currently hovering around 1.17% at the point of writing, a new high for 2017. Ample liquidity has so far kept domestic rates from tracking the US 3MLIBOR higher though. With US rate hike trajectory still on a gradual path, domestic rates should continue its slow grind higher. We expect the 3MSIBOR and 3MSOR to end 2Q 2017 at 1.37% and 1.15% respectively. For the full-year, we expect the rates to end 2017 at 1.62% and 1.40% respectively.

- **Latest Fiscal and External Balance Outlook:** Tax revenues in the first two months of the year have so far exceeded those in the same period in 2016. A total of SGD9.80bn of tax revenue was collected in Jan and Feb combined, more than the SGD8.2bn collected in the same period in 2016. Stronger collection of revenues from the goods and services tax accounted for these gains so far. At this pace, the government's tax revenue collect could well exceed the SGD57.8bn collected for the whole of 2016.

- The current account surplus narrowed to SGD18.13bn in 4Q from SGD22.77bn in 3Q 2016. The smaller surplus was due to the narrower goods and services surplus (of SGD25.69bn vs. 3Q: SGD27.90bn) and the deterioration in both the deficits in the primary and secondary income deficits (to -SGD3.74bn and -SGD3.81bn respectively from -SGD2.54bn and SGD3.77bn in 3Q respectively). The financial and capital deficit ballooned in 4Q to SGD22.73bn (3Q: -SGD18.18bn) on the back of larger financial derivative and 'other investment' outflows (of SGD3.37bn and SGD24.25bn) and more moderate portfolio investment outflow of SGD13.96bn that more than offset the larger direct investment inflows of SGD18.86bn. As a result of the larger deficit in the financial and capital account, the overall balance of payments (BoP) slipped into a deficit of SGD3.93bn in 4Q from a surplus of SGD5.43bn in 3Q. For the full-year, the current account surplus of SGD78.06bn was more than offset by the deficit in the capital account of SGD81.90bn leading to a BoP deficit of SGD2.46bn in 2016 - the first deficit since 2001.

- **Key domestic events and issues to watch:** Final GDP for 1Q 2017 will be released on 17 May.

- **Technical Outlook:** USDSGD consolidated in 1.39 – 1.4070 range for the month of Apr. Last seen at 1.3970 levels. Bearish momentum on weekly chart remains intact but we observed that stochastics on daily and weekly are near oversold conditions. Key support at 1.3920 levels. Break below opens way for further downside towards 1.38. Resistance at 1.4060. A close above 1.41 levels is required for further upside momentum to gain traction.

MYR: A Positive Twist

Forecast	2Q 2017	3Q 2017	4Q 2017	1Q 2018
USDMYR	4.3000 (4.4000)	4.2500 (4.3500)	4.3000 (4.4000)	4.3500 (--)

Previous Forecast in Parenthesis

- **Motivation for the FX View:** We are positive on the Ringgit outlook given the recent initiatives from BNM to broaden and deepen the onshore financial markets. We interpret these steps as positive development and expect foreign investors' confidence to gradually return. Foreign buying on Bursa Malaysia is now into its 11th consecutive week, the longest since May 2013. Cumulative net purchase amounted to MYR6.91bn – the highest amongst regional peers in Indonesia, Philippines and Thailand. Our Fixed Income analysts also expect foreign interest on MGS to return gradually. Given improved investors' sentiment, well-managed expectation for Fed rate hike and MYR being fundamentally and historically undervalued, we see scope for Ringgit to play catch up with regional peers and extend its gains towards 4.34, 4.30 levels (vs the USD) for the month of May. We are also revising our USDMYR forecast lower across the forecast horizon.

- We reiterate our **long-standing bias that the Ringgit remains fundamentally undervalued.** Our fair value estimate (which takes into account interest rate differential, inflation differential, current account differential and reflation variables) puts USDMYR at 3.65 levels. We had previously said that Ringgit weakness was temporary and was not a reflection of underlying fundamentals (which remain intact). We believe stability is gradually returning to Ringgit as political/ contingent liability risk subsides, fiscal consolidation gains traction, oil prices continue to stabilize and uncertainty subsides. Solid underlying fundamentals and policies, backed by domestic demand, re-calibrated supportive budget (on a lower oil price assumption suggests flexibility in the fiscal space), relative stability in oil prices though some downside pressure exists, relative attractive yields in the MGS, stabilizing FX reserves to retained imports & short-term debt, accommodative monetary conditions (to support businesses) remain intact and should provide an anchor for MYR stability once short-term noises subside. We believe USDMYR range of 4.20-4.40 is likely to remain relatively sustained for 2017.

- **Positive Development to Deepen Onshore Financial Markets**. According to BNM press release (13 Apr), the Financial Markets Committee (FMC) announced a number of initiatives targeted to promote (1) a fair and effective market, (2) improve bond market liquidity; (3) ease hedging activities and; (4) enhance transparency and market information. All the initiatives under (1) to (3) will take effect on 2 May 2017 (Tue) while enhancement to financial market infrastructure will be implemented on a gradual basis and is expected to be completed over a 12 – 18 month period. In particular on points 2 and 3, the regulated short-selling of securities in wholesale money market will be liberalized to allow all residents to participate in short selling activities. This is to facilitate a more effective avenue for the hedging of interest rate risk exposure as well as to generate more trading activities and liquidity in the secondary government bond market. Eligible securities for short-selling transactions will also be expanded to include Malaysian Government Investment Issue (MGII) with an outstanding nominal amount of at least MYR2bn, on top of Malaysian Government Securities (MGS). The aim is to elevate liquidity in the MGII issue and narrow the pricing gap between MGS and MGII. A consultation paper will be issued for market feedback (by 28 Apr) on this proposed inclusion of MGII for short-selling activities. Registered non-bank entities (including institutional investors, companies) will be allowed to hedge up to 100% of their underlying assets and to manage an additional 25% of FX exposures. This allows registered investors to fully hedge and actively manage their FX exposures including unwinding of hedging positions.

- **Foreign purchase of Bursa equities** is now into its 11th consecutive week, the longest since the 24 consecutive weeks of buying which ended in May 2013. Cumulative net purchase amounted to MYR6.91bn – the highest amongst regional peers in Indonesia, Philippines and Thailand. KLCI has also reached a near-2year high.

- On fixed income, our analysts noted that some of the outflows in March was due to the selloffs in MGS 9/17 and MGS 10/17 which essentially brought forward the risks that could have otherwise come in September (MYR14b maturity) and October (MYR13.5b maturity). Given very low foreign positioning in MGS, they believe the outflows in March were driven by offshore banks and total return funds and this implies that the foreign holdings that remain should be stickier than before. They expect 2Q17 to fare better than 1Q17 and the worst may be over after the huge MYR26.2b outflows in March; foreign net selling of Malaysian bonds to recede sharply and may even reverse in the next 3 -4 months given there is no maturities of government bonds in Apr-May 2017 while the next two maturities are Government Investment Issue (GIIs) on 15 Jun and 30 Aug and the foreign holdings for those GIIS are much lower than MGS. They think there is chance of 10y MGS returning to sub-4.00% by end-2Q17. Decline in Malaysia's weight in GBI-EM GD index may be near its bottom after dropping to 7.5% from ~9.5% since Nov 2016, if onshore liquidity improves and the reopening of 7y MGS & GII and 10y MGS & GII between May and July could see more bonds becoming eligible to be added to the index constituents.

- **External** reserves have stabilized and risen since end-Jan 2017. Our Economists noted that it could be due to several factors including (1) rising repatriation of net export earnings - According to BNM, a total of USD2b were repatriated in Dec 2016 – Feb 2017, with rising monthly trend i.e. USD0.4b in Dec 2016, USD0.7b in Jan 2017, and USD0.9b in Feb 2017; (2) net FDI inflows - Petronas-Saudi Aramco deal for the latter to buy 50% stake worth USD7b in Petronas' RAPID project; Alibaba's investment in e-commerce hub in Malaysia encompassing logistics, cloud-computing and e-financial service to boost trade and e-commerce in the region, which will also be part of the collaboration between Alibaba and the Malaysian government to develop a Digital Free Trade Zone (DFTZ) in Malaysia; (3) Improvements in the overall current account balance via narrower deficits in the services trade and income account, complementing the sustained trade surplus. Improvement in the services trade deficit is possible amid the recovery in inbound tourist arrivals last year, which is expected to be not only sustained but gain momentum this year. This, among others, is due to the 72% surge in bookings from Chinese tourists to come to Malaysia for the period 16 Mar –31 Aug 2017 following China's imposition of travel ban to South Korea mid the geopolitical tension in the Korean peninsula. Meanwhile, the income account may register higher repatriation of income, profits and dividends from overseas direct and portfolio investments by Malaysia's corporates and investment funds, especially the Government-linked entities, including Petronas.

- **Growth and Inflation Outlook:** Our Economists maintain our 2017 real GDP forecast of +4.4% (2016: +4.2%), underpinned by faster growth in domestic demand (2017E: +4.9%; 2016: +4.4%) reflecting sustained consumer spending growth (2017E: +5.9%; 2016: +6.1%), stronger investment growth (2017E: +3.9%; 2016: +2.7%) on progress of existing - and the rollout of - new major infrastructure and investment projects, and pick up in government consumption expenditure (2017E: +2.9%; 2016: +1.0%).

- The wild card is external trade in view of the uncertainties over the US trade policy under President Trump, especially the risk to US-China trade relation. However, under the current expectation of a moderate pick up in global economic growth (2017E: +3.1%; 2016: +2.9%) and firmer commodity prices, we are looking at relative better trade growth in 2017 i.e. higher growth in exports and imports of goods and services of +1.3% and +1.5% respectively (2016: +0.1% and +0.4% respectively).

- We continue to keep a close tab on key high frequency domestic data, namely the monthly economic indicators such as the indices on industrial production and distributive trade, external trade, money and banking statistics, as well as major commodity output and prices. In addition, our focus is also on the economic trends as well as policy and political developments in the major economies i.e. US, Europe (including UK), China, Japan.

- Continued robust export and import growth in Feb 2017 of +26.5% YoY (Jan 2017: +13.6% YoY) and +27.7% YoY (Jan 2017: +16.1% YoY) respectively contributing to +MYR8.7b trade surplus (Jan 2017: +MYR4.7b). Low bases in early-2016, pick up in global economic activities and firmer commodity prices are boosting trade growth in early-2017 amid risks from US trade policy and commodity price outlook. YTD, exports surged +19.8% (Jan-Feb 2016: +2.7%), imports jumped +21.5% (Jan-Feb 2016: +2.5%) with trade surplus of +MYR13.4b (Jan-Feb 2016: +MYR12.7b). Adjust our full-year growth forecasts for exports and imports to +8.5% and +9.8% respectively from +2.0% and +2.5% previously, but keep trade surplus projection of +MYR85.5b given that the first two months' trade surplus is around 16% of our forecast. Similarly, 2018 export and import growth forecast tweaked to +4.0% and +7.4% from +4.1% and +4.9% previously while maintaining the +MYR83b trade surplus. With no change in trade balance, our forecasts remain for current account balance (2017E: +MYR24.7b or +1.9% of GDP; 2018E: +MYR23.9b or +1.8% of GDP) and real GDP growth (2017E: +4.4%; 2018E: +4.5%) forecasts (to note, for GDP growth, what matters is net trade, not trade growth).

- **Headline inflation rate in Mar 2017 jumped further** to +5.1% YoY (Feb 2017: +4.5% YoY) owing to transport while core inflation was steady at +2.5% YoY (Feb 2017: +2.5% YoY). In 1Q 2017, headline inflation rate accelerated to +4.3% YoY (4Q 2016: +1.7% YoY; 1Q 2016: +3.4% YoY) but core inflation rate was contained at +2.4% YoY (4Q 2016: +2.1% YoY; 1Q 2016: +3.6% YoY).

- Our Economists **revised upward their 2017's headline inflation rate forecast to 3.5%-4.0% from 3.0%-3.5% previously** (official 2017: 3.0%-4.0%; 2016: +2.1%). Accordingly, we also tweak our 2018 inflation rate forecast lower to 2.0-2.5% from +3.0% previously to reflect the higher base in 2017, on top of other key assumptions such as stable average crude oil price of USD55/bbl for 2017-2018 and firmer average MYR exchange rate vs USD (2017E: 4.41; 2018E: 4.35). The upward revision to this year's inflation rate reflects the factoring in of the +4.3% inflation rate in 1Q 2017. In addition, there is the complexity of forecasting inflation rate amid the volatile global commodity prices, especially crude oil and raw materials, and the impact on domestic fuel and food prices, hence the range forecast. The newly introduced mechanism of weekly price setting for domestic fuel prices further complicate forecasting as prices turned up to be more volatile, and the pass through impact to other goods and services are not easy to ascertain at this point. Nonetheless, we maintain our view that the current “cost-push” headline inflation would taper amid the absence of “demand-pull” and “wage-driven” inflationary pressure as suggested by the stable core inflation rate, and amid the sticky unemployment rate of round 3.4%-3.5% since Dec 2015.

- **Monetary Policy Forecast:** We maintain our call that despite the higher inflation rate expected this year, the core inflation remains stable and the **Overnight Policy Rate (OPR) will be kept steady at 3.00% p.a. as the focus of BNM’s monetary policy is to support growth** given the continued uncertainties over key factors that could affect the global economy, trade and financial markets, namely US trade policy stance; the delivery of President Trump’s fiscal stimulus; the pace of Fed’s interest rate hikes; political risks in Europe relating the Brexit and key elections; and the rising geo-political tensions

- In the last BNM meeting on 2 Mar, BNM kept the Overnight Policy Rate (OPR) at 3.00%. The Statutory Reserve Requirement (SRR) was also maintained at 3.50%. The Monetary Policy Statement (MPS) issued after the MPC sounded “neutral” to us. Growth momentum is expected to be sustained in 2017 after the 4.2% expansion in 2016, mainly on steady domestic demand. Any upside to growth this year is contingent upon a more positive contribution from the external sector. Inflation will average higher this year reflecting primarily the pass-through of higher global crude oil prices on domestic retail fuel prices. However, BNM sees the relatively high headline inflation in 1H 2017 to moderate thereafter, while core inflation will rise only modestly as the cost-driven inflation is not expected to have a significant impact on the broader price trends given the stable domestic demand conditions.

- **Latest Fiscal and External Balance Outlook:** Themed “Accelerating Growth, Ensuring Fiscal Prudence, Enhancing Wellbeing of People”, Budget 2017 maintains commitment to fiscal discipline and consolidation; supports domestic demand via corporate income tax rate cut, incentives for tourism, SMEs, exports and digital economy, and infrastructure investment; and focuses on the wellbeing of the low-and middle-income groups by addressing the issues of inclusivity, equality, cost of living and affordable housing.

- Budget deficit target for 2017 is set at -3.0% of GDP, sustaining the policy of fiscal consolidation since 2010. This year’s aim of -3.1% of GDP is maintained and achievable. Based on monthly data, we estimated budget deficit in Jan-Aug 2016 was -3.9% of GDP as the deficit of -5.6% of GDP in 1H 2016 turned into an estimated surplus of +1.2% of GDP in July-Aug 2016.

- We expect the fiscal deficit to remain flat at 3.1% of GDP, as government spending is likely to pick up (as we enter the election campaign).

- **Key domestic events and issues to watch:** Trade data (5 May); FX reserves (5 and 22 May); BNM meeting (11 May); Industrial Production (11 May); CPI Inflation (17 May); GDP (19 May).

- **Technical Outlook:** Ringgit continues to outperform and hold on to gains despite USD strength seen elsewhere. The move lower for USDMYR remains in line with our call. Pair was last seen at 4.3500 levels. Daily momentum continues to indicate a mild bearish bias while stochastics is falling into near oversold conditions. We noted previously that 21, 50DMAs cut 100DMA to the downside - these signals suggest some downside risks in the interim. Next support seen at 4.3400 (50% fibo retracement of Nov-2016 low to 2017 high) before 4.30 (61.8% fibo). Resistance at 4.40 levels..

IDR: Political Risks Possibly In The Horizon

Forecast	2Q 2017	3Q 2017	4Q 2017	1Q 2018
USDIDR	13300 (--)	13400 (--)	13450 (--)	13500 (--)

No Change to Previous Forecasts

- **Motivation for the FX View:** The IDR has been stuck within the 13200-13450 range since the beginning of the year even as the USD retreated. The IDR has not been able to break out on either side of this range. Even the prospects of an S&P credit rating upgrade could not lift the IDR out of its current trading range. Nevertheless on a year-to-date basis, the IDR made gains of 1.4% against the USD.

- So far, it has not only been the unwinding of some long USD positions, the relative peaceful conclusion of domestic regional elections, the cyclical recovery in exports in the region and firmer commodity prices has been supportive of the IDR, but the inflows of foreign funds in Apr as well. Consequently, the IDR has gained 0.3% against the USD in Apr to date.

- Doubts about global reflation trades as well as speculation of an imminent credit rating upgrade from S&P (either at the end of May or in Jun) that should be positive for the IDR has reignited carry trades and encouraged foreign inflows into Indonesian assets. In Apr so far, foreign investors have nearly USD1bn in equities (USD0.98mn), exceeding their purchase of USD759mn in for the whole of Mar. Year-to-date, the foreign inflows into equities has hit USD1.61bn, more than the USD1.26mn purchased for the whole of 2016. Meanwhile, foreign funds have added IDR12.96tn to their outstanding holdings of government debt month-to-date in Apr, a moderation from the IDR31.33tn added in the whole of Mar. Unlike equities, foreign investors added only IDR70.37tn to their outstanding holding of government debt so far this year, and could be on track to exceed the IDR107.39tn added for the whole of 2016.

- However, seasonality suggests that we could see weakness in the IDR in May. This suggests that USD strength could re-emerge and lift the USDIDR higher in May. This could mean either fading carry trades fade or diminishing expectations of a credit rating upgrade, though we are of the view that the former would be the more likely cause. The two Fed rate hikes expected in Jun and in 4Q should narrow the yield differentials in favour of the US. This could spur some reversal in flows from Indonesian assets back into the US and reduce carry, weighing on the IDR. In addition, the political uncertainty in Europe and threat of protectionist measures from the US could spur safe-haven plays and an aversion for riskier assets and weigh on the IDR as well. We could thus see increase volatility in the IDR with the USDIDR bouncing higher as a result.

- Political stability, which has been positive for the IDR so far, could become unsettled ahead. The loss of Jokowi-ally Ahok in the Jakarta gubernatorial elections could possibly increase the risk of policy uncertainty. The opposition victory in Jakarta could embolden and galvanize the opposition against the President and delay the pace of reforms. Should this happen, we could investment sentiments turn and investment decisions delayed until political certainty and policy clarity are in sight. Moreover, we have the verdict of Ahok's blasphemy trial coming up on 9 May that could see increased political tensions. All of these are likely to be IDR-negative. We will continue to watch the political arena closely and update our outlook for the USDIDR should the political situation change.

- Nevertheless, we do not expect the USDIDR to climb too aggressively with the pair still likely to end 2Q at 13300. We continue to expect the positive sentiment stemming from expectations of a credit rating upgrade by S&P to cap upside to the pair. This is because underscoring this possible credit rating upgrade is the ongoing reform process, which so far has seen 14 stimulus packages introduced with a 15th (relating to logistics) underway. These reform packages have helped to cut red tape and liberalize rules that have been a drag on investment and growth, and also supportive of specific growth industries. In addition, government's efforts to rein in the budget deficit by cutting unnecessary expenditure last year and the successful implementation of the recently ended tax amnesty program that have increased government revenue have provided more fiscal space to the government in 2017. As well, the government's USD400bn infrastructure spending spree should lift potential growth and hence the IDR.

- **Maybank vulnerability score** (using 9 economic and market variables: GDP, Yield, Politics, Current Account, Inflation, Fiscal, Equity Valuation, Population, Reserves) for Indonesia has improved to 5.1 from 5.4. This was largely due to the improvement in inflation and fiscal risks and should be supportive of the intrinsic value of the IDR.

- **Growth and Inflation Outlook:** Growth is unlikely to outperform 4Q 2016's 4.94% given that government spending has yet to regain momentum after being subjected to fiscal consolidation in 2016. The planned expenditure of USD400bn on infrastructure will likely be manifested in GDP from 2H onwards. Still, the cyclical recovery in the region should continue to lift exports and support growth ahead. This could be seen in the strong export growth in 1Q 2017 of 20.8%, an acceleration from 4Q 2016's 14.0%. In addition to the cyclical uptick, the still accommodative monetary policy is also supportive of growth. However, growth remains uneven with consumer spending slipping. This was reflected in the dip in motorcycle sales in 1Q 2017, falling 6.8% y/y from 4Q 2016's -4.8%. Motor vehicle sales though remained healthy, rising 5.8% y/y in 1Q 2017, though this was a moderation from 4Q 2016's +12.6%. Nevertheless, the growth of around 5% for 1Q is unlikely to distract from the improving economy. Our economic team continues to expect full-year real GDP to expand by 5.1% for 2017, better than the 5.0% in 2016.

- Inflation did not accelerate as expected in Mar. Instead, headline inflation rose by a slower 3.61% y/y in Mar from Feb's 3.83%. appears headed back towards the 4.0% level after headline inflation re-accelerated to 3.83% y/y in Feb. The moderation in headline inflation could be attributed to lower food prices (up just 2.99% y/y compared to 4.39% in Feb) that offset the higher cost of housing and transport (Mar: 4.09% and 3.16% vs. Feb: 3.71% and 3.07%). Core inflation also moderated, rising by just 3.30% y/y in Mar from 3.41% in Feb. This moderation in consumer prices is unlikely to be a game changer but could signal a bottom. We continue to expect inflationary pressures to rise on the back of a rise in administered electricity tariff and volatile food prices. These, together with the weaker domestic currency, should work in tandem to lift imported prices. Consequently, our economic team continues to project headline inflation to average 4.26 in 2017, in line with the central bank's forecast for inflation to accelerate above 4.0% in 2017.

- **Monetary Policy Forecast:** Since cutting its benchmark policy rate by 25bp in Oct 2016, the BI has kept its policy intact to anchor inflationary expectations and maintain IDR stability. The 7-day reverse repo rate remained at 4.75%, while both the lending facility and deposit facility rates were held steady at 5.5% and 4.00% respectively. This kept the interest rate corridor steady at 75bp on either side of the policy rate. The front-loading of rate cuts (amounting to 150bp) in 2016 has given some breathing space to BI to hold its policy rate steady amid US Fed rate hikes this year and threats of protectionism. The thinking at the central bank appears to be shifting. According to BI deputy governor Perry Warjiyo, the central bank has room to ease policy from the domestic perspective but have keep policy on hold to take into account global events such as US Fed fund rate hikes. Nevertheless, market appears to discount this as the macroeconomic environment continues to suggest a rate hike rather than a cut. Rising global oil prices and domestic factors such as electricity tariff rates that could see headline inflation accelerate back above 4% in 2017 amid steady economic growth. Our economic team believes that the BI will use other monetary tools such as macroprudential policies to boost growth rather than the policy rate. Consequently, they expect the central bank to keep the policy rate on hold for the rest of the year.

- **Latest Fiscal and External Balance Outlook:** With the tax amnesty programme winding down at end-Mar, the final tally might not be known for a while. Still, data released by the Finance Ministry suggested that the government has earned IDR110tn in penalty rates so far. This was on the back of IDR4668.77tn of assets held abroad declared by Indonesian. Of these, the bulk of the assets were in Singapore with IDR751.19tn, followed by the British Virgin Islands with IDR76.92tn and then by Hong Kong with IDR56.27tn. However, the assets repatriated were small compared to the total assets declared – just 3.13% or IDR145.95tn. This was probably due to the lack of avenues for investment under the programme. An expansion of investment opportunities could spur more of these funds onshore. Nevertheless, the tax amnesty programme can be considered a success for the revenues it raised for the government as well as the number of participants, which totalled 832,631.

- The current account deficit (CAD) improved significantly in the last quarter of 2016, coming in at -USD1.81bn in 4Q or just 0.8% of GDP, compared to 3Q's -USD4.68bn (1.9% of GDP). This improvement can be attributed to the larger goods and services surplus of USD3.5bn (vs. 3Q: USD2.31bn) and the moderation in the primary income deficit to USD6.27bn from -USD8.01bn in 3Q. The overall balance of payments surplus narrowed to USD4.51bn in 4Q from USD5.71bn in 3Q, underpinned by the narrower CAD and smaller surplus in the financial account of USD6.76bn in 4Q vs. 3Q's USD10.55bn. For the full-year, the CAD improved to 1.75% of GDP in 2016 from 2.03% in 2015. For 2017, our economic team expects the CAD deteriorate to 1.95% of GDP due to greater import of capital goods to support the government's infrastructure programme. This is more sanguine that the BI's CAD projection of 2.11% for 2017.

- **Key domestic events and issues to watch**: 1Q 2017 GDP will be released sometime on 2-8 May. BI will also decide on monetary policy on 18 May. On 9 May, outgoing Jakarta governor Ahok will know his fate when the court hands down its ruling on his blasphemy case. S&P could also be announcing its sovereign credit ratings for Indonesia either at end-May or in Jun.

- **Technical Outlook:** USDIDR traded a wider than usual range of 13250 – 13370 amid Jakarta elections. Pair was last seen at 13310 levels. Daily momentum and stochastics indicators are not providing a clear bias. Continue to favor 13260 – 13330 range. We caution that a break above 13330 (50 DMA) could see the pair trade higher towards 13370.

PHP: Risks To The Downside

Forecast	2Q 2017	3Q 2017	4Q 2017	1Q 2018
USDPHP	50.30 (--)	50.50 (--)	50.70 (--)	50.70 (--)

No Change to Previous Forecasts

- **Motivation for the FX View:** The PHP has gone from being an underperformer in the region at the beginning of Apr to now among the outperformers so far this month. The PHP has gained nearly 1.1% against the USD so far in Apr. This makes the PHP the second best performer in the region after the MYR. In contrast, the PHP was the laggard among the ASEAN currencies in Mar, gaining just 0.16% against the USD. This outperformance so far can be attributed to a change in sentiments that began at the end of Mar when Fitch affirmed the Philippines' BBB- sovereign credit rating with a positive outlook that has spurred inflows into Philippines assets. Month-to-date in Apr, foreign investors have purchased USD44.71mn in equities compared to the sell-off of USD23.74mn in Mar.

- Despite this outperformance, we remain bearish on the PHP, especially in the month ahead. Looking at historical price action for the past 10 years for May, it would appear that the risk appears to be tilted to the upside for the USDPHP. Aside from this seasonal pressure, the potential USD move higher on the back of steady US economic growth, the ongoing normalization of US rates (one hike in Jun and another sometime in 2H), expectation of Fed's unwinding of its QE, and possible EUR pullback amid disappointment with ECB policy. There is also the possibility that the global reflation trade could re-emerge that could see an outflow from riskier assets back to the USD.

- Domestically, the PHP continues weighed by the Duterte risk premium, i.e. investor concerns over the overly aggressive anti-legal drug campaign and the president's intemperate temperament. This has led to a reversal in foreign portfolio investment. Though Apr has been favourable to Philippine equities as discussed above, foreign investors have sold USD147.75mn of equities so far this year, in contrast to the USD83.39mn that were purchased for the whole of last year. Foreign bond purchases data is not available but an examination of the Philippine sovereign bond yield movement suggests that there has been a sell-off in government debt so far this year and this could well include foreign investors. Year-to-date, sovereign bond yields have been broadly higher by 0.4-73.1bp in across all tenors.

- As we had caution previously, we need to see the dissipation of this risk premium before an improvement in the PHP can be realized. While indiscriminate killings are still being reported, there are signs that the campaign against illegal drugs is slowing. This should allay foreign investor concerns and could eventually lead to the return of foreign investors into the Philippine assets and lift the PHP higher.

- In the longer term, we could see more inflows into the Philippines equity market. This is because valuations in the Philippines have fallen after the sell-off in the equity market over the past few months. According to our estimates using the Cyclical Adjusted P/E (CAPE) ratio, equities are now relatively cheaper (as reflected by estimated P/E ratios minus their 5-year average P/E ratios) compared to its peers and this could eventually attract foreign inflows as a result.

- In the next three-to-six months, pressure on the PHP is still to the downside. The expected resurgence in the USD due to the two Fed rate hikes pencilled in for the remainder of this year, together with the potential re-emergence of global reflation trades, spur outflows from Philippine assets and weigh on the PHP. In addition, protectionist measures that could disrupt global trade by the Trump administration cannot be discounted and this could also add to downside pressure on the PHP.

- Strong growth momentum, lifted by expansionary fiscal policy, continues to be supportive of the PHP. However, increasingly, the focus has shifted to the deteriorating current account. The current account has registered a deficit of 1.2% of GDP in 4Q – the first deficit since 1Q 2012. As we had previously caution, a 25bp rate hike (as expected by our economic team in either 2Q or 3Q of this year) to keep the economy from overheating and for inflation to stay within the BSP comfort zone of 2-4% is unlikely to be a panacea for its currency woes. We continue to expect the PHP to remain under pressure for the remainder of the year underpinned by USD strength and the Duterte risk premium that should keep the pair supported above the 50-figure in 2017.

- Our monthly **Maybank vulnerability score** (using 9 economic and market variables: GDP, Yield, Politics, Current Account, Inflation, Fiscal, Equity Valuation, was unchanged at 5.3. The deterioration in fiscal risk was completely offset by the improvement in population risk. This should be supportive of the intrinsic value of the PHP.

- **Growth and Inflation Outlook:** The government continues to target growth of 6.5-7.5% for 2017 on expectations that its expansionary spending program (where the ceiling for deficit spending was raised to 3% of GDP from 2017 to 2019) would provide the leg up for the economy. Aside from government spending, the cyclical recovery in exports led by the US and China has also lifted exports (up 24% and 11% y/y in Jan and Feb respectively) should also be supportive of the government's outlook. However, private consumption spending could slow given that remittances are not showing signs of outperformance. Instead, remittances have slowed in Feb to 3.4% from Jan's 8.6% and this could be a drag on growth. Consumption spending should also slow on the back of faster inflation amid weaker PHP and expected implementation of the first phase of the tax system reforms towards consumption taxes. In addition, the expected 25bp policy rate hike in mid-2017 should slow consumption. Due these reasons, our economic team is projecting growth to come in just a tad below the government's growth projection at around 6.4% in 2017.

- Inflation pressures continue to mount as growth accelerates with headline rising by 3.4% y/y in Mar, up from Feb's 3.3%. Elevated food prices (Mar: 4.0% y/y vs. Feb: 4.1%) and higher housing and utility costs (Mar: 4.0% y/y vs. Feb: 2.9%) lifted inflation higher in Mar. Core inflation continue to climb higher as well, up 2.9% y/y compared to 2.7% in Feb. Continued weakness in the PHP against the USD, impact of phase 1 of the proposed tax reform package and higher commodity prices (especially crude oil and food commodities) are likely to put upside pressure on inflation. Our economic team maintains their full-year headline inflation at 3.5% in 2017, which is at the upper half of the government's 2-4% inflation target for 2017 and in line with the BSP's expectations of 2.9%.

- **Monetary Policy Forecast:** Since 16 May 2016, the BSP has maintained its benchmark policy rate at 3.0%. Aside from the overnight borrowing rate, the overnight lending rate and overnight deposit rate were also left unchanged at 3.5% and 2.5% respectively. The 50bp symmetrical corridor on either side of the policy rate was kept in place. However, it is likely that the current policy stance might not last. This is because, unlike most of it regional peers in the region, the BSP is expected to be the first central bank in the region to hike rates in 2017 given that the economy expanding at a healthy pace above 6% and inflation accelerating close to the upper bound of the government's comfort zone for inflation. The BSP could also be mindful of the gap between UST and Philippines treasury yields could narrow when US Fed rate hikes in the remainder of 2017 that could spur capital outflow. To counter these challenges, our economic team expects the central bank to hike the policy rate by 25bp rate hike once in 2Q 2017. This modest rate adjustment should ensure that real interest rate remain positive, though we doubt that this would be sufficient to ease downside pressure on the PHP.

- **Latest Fiscal and External Balance Outlook:** After a positive start to the year with a fiscal surplus, the fiscal position has since slipped back into deficit in Feb and Mar of PHP23.72bn and PHP61.47bn respectively. is back in deficit of PHP32.97bn in Mar. These deficits were on the back of increased in government spending in these two months that more than offset revenues. For 1Q 2017, the fiscal deficit was at PHP82.97, narrower than the deficit of PHP112.49bn in 1Q 2016. The government expects the deficit ceiling will be kept at 3% of GDP through 2022.

- The balance of payments (BoP) deficit widened to USD549.5mn in Mar from the deficit of USD436.1mn in Feb. While a detailed breakdown of the components of the BoP is unavailable for now, we surmise that the widening deficit could possibly be due again to the widening merchandised trade gap and portfolio outflows. The trade deficit in the first two months of the year amounted to USD4.2bn while outflows from equities were at USD348.89mn. The BSP continues to maintain their expectations that the overall BoP would remain in a surplus of USD1bn for 2017. However, this projection is expected to be revised sometime in May to reflect recent market development.

- **Key domestic events and issues to watch:** The BSP meets on 11 May to decide on monetary policy and the government will release 4Q 2017 GDP on 18 May.

- **Technical Outlook:** USDPHP slipped in early-Apr to a low of 49.27 (13 Apr) but retraced losses into month-end (as we write). Pair was last seen at 50.10 levels. Daily momentum and stochastics indicators are bullish bias. We believe a test above previous all-time high at 50.42 is possible. Support at 49.40. Biased to buy on dips.

THB: Downside Risks

Forecast	2Q 2017	3Q 2017	4Q 2017	1Q 2018
USDTHB	34.80 (--)	35.30 (--)	36.00 (--)	36.20 (--)

No Change to Previous Forecasts

- **Motivation for the FX View:** The THB has so far undoubtedly been the best performing currency in ASEAN. Year-to-date, the THB has gained 4.1% against the USD. The faster gains in the THB in 2017 coincided with increasing market doubts over global reflation trade prospects, leading to the unwinding of stale long USD bets, providing support for the THB's move higher.

- The unwinding of long-USD positions amid concerns about Trump's ability to deliver on his economic promises is insufficient to explain this outperformance in the THB so far this year. Our VAR decomposition analysis (which shows the percentage of the forecast variance due to each endogenous variable) suggests that the factor most important to changes in the USDTHB is the political environment. Thus, while the political calm in the kingdom is providing the impetus for an economic growth recovery and a stable investment environment for foreign funds, any shifts in political sentiments could impact the USDTHB.

- Other factors that could move the USDTHB include real yields, foreign purchases of government debt and current account balances. Rice prices (a proxy for the important agricultural sector) and FDI and foreign purchases of equities play a lesser role in determining the movement of the USDTHB. The widening of real yield differentials between the 10Y UST and Thai government bond should encourage capital inflows in search of higher returns, lifting the THB higher. Also, relative low foreign ownership in Thailand at 15% (compared to Indonesia at 38% as of end-Mar 2017) suggests that there is upside to foreign ownership of Thai assets. This makes Thailand more attractive as an investment destination than Indonesia, supportive of the THB.

- Aside from rising real yield differentials, the ballooning current account surplus is also supportive of the THB. With the exception of Singapore, which historically has persistent and high current account surpluses, Thailand has seen its current account surplus balloon to more than 10% of GDP since 2014. In contrast, the current account surpluses of both Malaysia and Philippines are tapering, while Indonesia continues to see persistent current account deficits.

- This combination of a persistent current account surplus and widening yield differentials has improved the investment sentiments for foreign investors. This is reflected in the strong inflow into Thailand recently. So far in 2017, foreign funds have purchased THB105.92bn of government debt. If such purchases by foreign investors continue in the months ahead, this could be supportive of the THB

- However, the gains in the THB may not be sustainable. Seasonally, May could see downside pressure on the THB, possibly because May is when local firms pay out dividends to foreign investors. This could see an outflow of funds from Thailand resulting in a softening THB. This in turn could spur speculative sell-off in Thai assets by foreign funds in anticipation of these outflows. Already in the last week of Apr, foreign funds have sold THB1.54bn and THB7.78bn of equities and government debt. Further flow reversals could put the recent gains in the THB at risk. As well, the BoT has announced that it intended to curb short-term supply in May to prevent hot money flows into Thailand and could limit support for the THB in the month.

- Further upside risks to the USDTHB could also come from the market underpricing US Fed fund rate hikes that could not only see a sharper upward move in UST yields but also in the USD. This could spark a sell-off in EM assets, including those from Thailand. In addition, the recent US Treasury Department foreign-currency report may have not accused Thailand of being a currency manipulator but there is a risk that some remedial action could be taken by the US to re-align its trade surplus with Thailand. The report by the Commerce Department in Jun could propose such remedial action that could include protectionist measures. This could potentially disrupt trade and weigh on the THB ahead.

- Additionally, we believe that downside pressure to the pair could come when political tension rises towards the latter part of the year. For now, the funeral of the late King HM Bhumibol, which is expected sometime in Nov and the coronation of HM King Maha Vajiralongkorn, which should follow soon after, should ensure political calm and stability. But once these events are over and the election schedule is announced, likely in the early- to mid-part of 2018, simmering political tensions are likely to break open to the surface.

- Key to this political tension is the continued domination of the military (and the elites) in the political arena to the exclusion of nearly everyone else. The military has been given the power to appoint the 250 members of the new Senate in the first five years after the first parliament convenes under the new constitution and more importantly, the new constitution allows for the appointment of a non-elected PM to head the government. This suggests that the military and its allies will continue to dominate politics long after the coup. This could re-ignite political temperature ahead of the general elections, and this could keep foreign investors on the sidelines until the political climate clears up, weighing on the THB sentiments and possibly keep the USDTHB supportive around the 36-handle by the end of the year.

- **Our Maybank vulnerability score** (using 9 economic and market variables: GDP, Yield, Politics, Current Account, Inflation, Fiscal, Equity Valuation, Population, Reserves) for Thailand was steady at 4.3. The improvement in inflation risk was completely offset by the rise in population risk. This should be supportive of the intrinsic value of the THB.

- **Growth and Inflation Outlook:** The economic recovery that we have seen so far appeared to have slowed in Mar, but has not stopped in its track. Manufacturing output fell by 0.5% y/y in Mar, the second month of decline, dragged lower by the 11% y/y drop in car output. The bright spot remain exports, which rose 9.2% y/y in Mar, a rebound from the 2.8% drop in Feb. This suggests that the cyclical recovery in exports in the region is still intact. The strong double-digit import growth in Feb and Mar of 20.4% and 19.3% point to a pick-up in domestic demand that probably included private consumption. In addition, the government infrastructure spending programme is also helping to drive growth ahead. With the growth recovery on track, the Finance Ministry is keeping its GDP growth projection of 3.6% for 2017 intact, more sanguine that the BoT forecast of 3.4%. Our economic team remains optimistic about growth prospects, projecting the economy to grow by an above-consensus 4.5% in 2017. Market expectation is for growth of 3.3%.

- The above-1.0% headline inflation printed since Dec 2016 stalled in Mar. Headline inflation rose by just 0.76% y/y in Mar, down from +1.44% in in Feb. This sharper moderation comes on the back of continued moderation in food prices (Mar: +0.68% y/y vs. Feb:+ 1.0%), steeper decline in housing cost (to -1.19% y/y in Mar from -1.17% in Feb) and more moderate increase in transport cost of 3.3% (vs. +5.58% in Feb). Core inflation though accelerated in Mar, rising by 0.62% y/y from Feb's 0.59%. Given the expected sharper economic recovery, rising commodity prices and still weak THB, our economic team expects headline inflation to accelerate to 2.5% in 2017, higher than the 2.2% the BoT is looking for.

- **Monetary Policy Forecast:** Like its peers in the region, the BoT has left its benchmark interest rate unchanged so far this year. The overnight bond repurchase rate was kept close to historic lows at 1.25%. The last time the policy rate was even lower at 1.25% was during the Great Financial Crisis in 2009-10. The still-low GDP growth by historical standards suggests further policy accommodation should be forthcoming but we think that any rate cut is unlikely at this juncture. This is because monetary policy is already accommodative and near historic low, and the central bank views expansionary fiscal policy to be more appropriate to drive economic growth. Monetary policy should instead play a supportive and complementary role to fiscal policy. Our economic team believes that the central bank is more likely than not to hike its benchmark policy rate to anchor inflationary expectations and to prevent the economy from overheating. At the same time, a rate hike would also lift domestic yields, keeping the current spread between the UST and Thai bonds or widen it, helping to reduce any outflow from Thai assets. Thus our economic team is now looking for a two 25bp rate hikes in the benchmark policy rate this year, one in Sep and the other in Dec.

- **Latest Fiscal and External Balance Outlook:** The budget for FY2018 (Oct 2017 – Sep 2018) has been approved by the cabinet and now awaits legislative acquiescence for the budget to take effect. The FY2018 budget has penciled in a larger deficit of THB450bn (2.9% of GDP) for FY2018 compared to the expected deficit of THB390bn (2.6%) in FY2017. Expenditure for the new fiscal year is set at THB2.9tn, up 6% from FY2017, with 23% of total expenditure earmarked for investment. With the government still running a budget deficit, public debt is recorded at 42.2%of GDP as of end Dec, under the 60% threshold.

- The current account surplus narrowed in Mar to USD2.58bn (from USD5.74bn in Feb) in contrast to expectations for an USD4.1bn surplus. Details remain sparse but the BoT suggested that this surplus were supported by export and tourism receipts.

- **Key domestic events and issues to watch:** 1Q 2017 GDP will be released on 15 May. BoT meets on 24 May to decide on monetary policy.

- **Technical Outlook:** USDTHB rebounded, in line with our tech call (in our last Monthly Outlook). We said w*hile bearish momentum and the bearish trend channel (formed since Oct 2015) stay intact, we caution that the pair could face rebound risks towards 34.87, 35 levels*. Pair was last seen at 34.60 levels. Bullish momentum on daily chart remains intact. We continue to hold on our rebound risks call. Support at 34.30 levels.

INR: Risks To The Upside

Forecast	2Q 2017	3Q 2017	4Q 2017	1Q 2018
USDINR	65.00 (65.50)	65.70 (66.50)	66.20 (67.00)	66.00 (--)

Previous Forecast in Parenthesis

- **Motivation for the FX View:** Focus is on what RBI has in store after the surprise reverse repo rate increase to 6.0%, narrowing the liquidity adjustment facility corridor to 25bps. The goal was to soak up the excess liquidity and a narrower corridor can align the operating target with the policy rate. Even as inflation trajectory remains benign (with CPI only mildly firmer in Mar), core inflation is seen sticky to the downside. RBI is still wary of upside risks in view of possible El Nino, one-off effect of GST and HRA implementation of the 7th Pay Commission. The surprise move by the central bank to raise the reverse repo rate also triggered sales of Indian bonds. It was the front end that was sold off more aggressively with the 6M 35bps higher as investors start to reprice a policy rate move in the nearer future. The longer end was capped with the 10y yields around 9bps higher since a month ago, at last check (25 Apr). Flows data suggest that Indian bonds are still very much favoured by foreign investors with an inflow of U$2.67bn seen between 1-21 Apr, lured by the appeal of higher yields, attractive growth story amid the remonetization process and strong mandate held by Modi that can facilitate growth. In addition, corporate tax cuts and support for agriculture and infrastructure spending from the budget should also be growth boosting.

- RBI has been intervening in the forex markets, buying USD to "smooth volatility". Daily technical indicators suggest bearish momentum but weekly momentum show oversold conditions. In addition, May is a seasonally bearish month for rupee. As of 24 Apr, 77% of central government securities have been utilized and we expect the bond-related inflows to slow in the next two months. USDINR forecast for 2Q is slightly lowered towards 65. Trajectory towards the end of the year is still likely to be to the upside, led by mild USD strength but we expect rupee to withstand US tightening better than its peers.

- Our **Maybank vulnerability score** (using 9 economic and market variables: GDP, Yield, Politics, Current Account, Inflation, Fiscal, Equity Valuation, Population, Reserves) for India was unchanged at 4.6 (with 1 being the best score and 9 being the worst) as the improvement in politics negate the deterioration in the inflation score.

- **Growth and Inflation Outlook:** 4Q GDP for 2016 (Oct-Dec) came in stronger than expected at 7.0%y/y, albeit slowing from the previous 7.4%, underpinned by resilient manufacturing, strong agricultural output and faster growth in the services sector. Industrial production slipped -1.2%y/y in Feb from the previous 3.3%, weighed by the -1.6%y/y decline in the manufacturing sector. Trade-wise, while there was a strong rebound in exports, the surge in import far surpassed that of exports with a print of 45.3%y/y, leaving a wider trade deficit of U$10.4bn. CPI firmed to 3.81%y/y from previous 3.65%, on the back of higher food and beverages, clothing and footwear, housing and mostly fuel. On the other hand, Mar WPI softened to 5.70%y/y from previous 6.55%. Slower price increase was noted across the board including primary articles, fuel, power, light and manufactured products. The latest industrial outlook survey reveals an improvement in sentiments on demand conditions including production, order book and capacity utilization this quarter. Respondents are optimistic about transferring the rising cost of materials to selling price which should leave the profit margin unaffected in 1Q 2017-2018 (Mar-Jun). While the survey suggests potential improvements in the outlook of the industrial sector, the stagnant profit margin (albeit an improvement from the contraction seen in the previous quarter) does not bode well for private investment.

- **Monetary Policy Forecast:** Most of the RBI MPC committee members were concerned about the inflation risks that emanate from the potential El Nino that could affect monsoon rain, the implementation of the HRA allowances and the one-off GST kick-off. The hawkish RBI, along with the hike in the reverse repo rate to 6.00%, has triggered a sell-off in the bond markets but strong foreign interest capped the longer term yields. A key issue is that private investment remains weak and RBI Patel even mentioned in the Minutes of the Apr RBI meeting there is still room for banks to cut lending rates. However, with growth prospects looking firm, the urgency to lower rates is hardly compelling. We look for RBI to keep policy rate unchanged at the next policy meeting on 7 Jun.

- **Latest Fiscal and External Balance Outlook:** Finance Minister Jaitley pledges support to the farmers, infrastructure spending and personal income tax cuts and corporate tax cuts for small and medium businesses to boost consumption and investment. The current account deficit remained steady widened to $3bn in the quarter ending Sep. Trade deficit was lower at U$25.6bn vs. previous U$23.8bn. Capital account recorded an outflow of U$17.5bn. Portfolio investment recorded a net inflow of U$6bn due to strong equity demand in the quarter. With Modi already grasping a firm mandate, investors will closely watch for the smooth implementation of the GST, scheduled on 1 Jul.
- **Key domestic events and issues to watch:** PMI is due on the 2nd, trade on 10-15th, CPI and industrial production on the 12th, WPI on 15th.
- **Technical Outlook:** 1M NDF remains heavy within the downward sloping trend channel. While momentum is still bearish, stochs are oversold, price seems to be testing the 200-WMA a round 64.30 and we fear a mild reversal. Retracements could bring the pair towards the 65-figure, closely watched for any breakout of the trend channel. If bears press on, next support is seen around 63.96 before 63.57, 62.60.

VND: Wary of USD Bulls

Forecast	2Q 2017	3Q 2017	4Q 2017	1Q 2018
USDVND	22900 (23300)	23100 (23400)	23300 (23500)	23400 (23600)

Previous Forecast in Parenthesis

- **Motivation for the FX View:** Our view remains the same for the dong as USDVND bounced from Apr low to levels around 22740 (27 Apr). The dong seems to be increasingly markets guided with the 50-DMA capping bids at this point. In the absence of Apr data at the point of writing, we view the lift in regional trade performance as a positive sign for Vietnam's exports outlook with major exports of computer and electrical components and phones & spare parts likely to see a stronger growth for Apr, as hinted by the first 20-days trade numbers of South Korea. With retail sales not showing much of an uptrend, the trade balance may have a chance of improvement given the resilience of external demand. Still, FDI inflows have been weak, registering -4.0%y/y declines in the first four months of the year. USDVND remains vulnerable to the USD trajectory. Despite the USD retracement, we are still wary of its potential resurgence in view of two more likely hikes by the Fed. Portfolio inflows have been positive, keeping a lid on the USDVND. Expect pressure on the USDVND to be mostly on the upside as we anticipate further rate hikes by the Fed to lift the currency pair into 3Q and 4Q this year, looking for the pair to reach 23400 by year end, taking into account the recent USD retreats.

- **Growth and Inflation Outlook:** As of last available information (27th Apr), we recall that the 1Q GDP came in lower than expected at 5.10%y/y, slowing from the previous 6.21%. The head of GDP department in the General Statistics Office noted that the 38% fall in Samsung's output in the quarter has shrunk electronics production in Vietnam by 1%. That said, Samsung has announced to make smart TVs at its latest U$3bn Vietnam facility, improving the prospect of manufacturing-related export. Mar PMI-mfg came in at stronger 54.6 (vs. previous 54.2) with sharper growth of output recorded along with strong growth in new orders. That could possibly mean an improvement in industrial production from the deceleration of 5.5%y/y in Mar from previous 15.2% in Feb. Slowdown was seen in manufacturing and electricity with mining and quarrying still clocking deep declines. Exports in Jan-Mar also slowed to 12.8%y/y from Jan-Feb 15.4% while imports quickened pace from 19.6%y/y to 22.4%. The acceleration was broad-based with both domestic and foreign-invested sector seeing around 20% growth each. Domestic consumption seems to be improving with retail sales for the first quarter seeing 9.2%y/y, quickening from Jan-Feb 8.7%.

- Inflation for Mar came in at 4.65%y/y, slowing from previous 4.74%, weighed by lower food inflation. Head of GSO Price Statistics Department urged Ministries to keep an eye on prices of essential goods in particular rice, gasoline, steel and fertilizer in order to keep CPI below 4%. Food inflation may be low now but any rise in fuel prices, coupled with the weak dong could threaten the headline CPI to the upside. The Ministry of Planning and Investment's National Centre for Socio-Economic Information and Forecast expects inflation to average around 4.7% in 2Q with potential weakness in dong likely to keep price pressure.

- **Monetary Policy Forecast:** According to a statement by the central bank on 10 Apr, they continue to ensure stable interest rate and stands ready to respond to any extraordinary movement. The SBV would strictly monitor to promptly intervene when need be through open market operations, refinancing to manage money supply. The central bank is working to resolve and restructure NPLs so as to improve the monetary transmission system. We expect little action from SBV in terms of rates.

- Elevated price pressure has effectively has reduced the real borrowing rates. Expectations for a strong USD, higher US rates could continue to keep the dong on the backfoot. SBV is likely to keep policy rates (currently base rate at 9.0%, refinancing rate at 6.5% and discount rate at 4.5%). USDVND could continue to keep a mild uptrend into 2Q and 3Q. A resurgence in USD strength would still leave USDVND vulnerable to the upside. In addition, exports growth is still weak whilst imports growth has been robust, leaving the trade balance in wider deficits. Lean FX reserves-import ratio of barely above 2 would mean that any external shocks in the FX space could force SBV to devalue the dong. Should USD remain on the upmove, expect USDVND reference rate to be fixed higher and that should guide the USDVND towards our 23400 forecast by 4Q.

- **Latest Fiscal and External Balance Outlook:** In April, Vietnam set a lower budget deficit of 3.38% of GDP for 2017 from previously 3.50%. 2016-18 public debt (including government debt, debt guaranteed by government, municipal debt) is capped at 65% of GDP. 2016-18 government debt is set at no more than 54% of GDP while foreign debt is set at no more than 50% of GDP. The Treasury Is to offer VND5.5trn of bonds on 3 May, at least VND66trn of government bonds in 2Q. As of last available data, the government has gotten VND14.3trn from 1Q sale of state stakes. This is part of an ongoing effort by the government to divest VND67trn from SOE in the years leading to 2020. Key use of the capital is to develop important infrastructure projects like the Long Thanh International airport, along with the recent plans to build the Chrey Thom Bridge that will connect the southern province of An Giang in Vietnam to Cambodia's Kandal province. This is mean to promote bilateral trade and bring about more economic benefits for those communities along the border areas. That said, there was no timeframe for the construction.

- Current account recorded a surplus of U$155mn in 4Q (latest data available), narrowing drastically from the U$3.5bn seen in 3Q on the back of narrower net trade surplus of goods. Expect 1Q 2017 print to possibly dip into deficit but we remain cautiously optimistic on Vietnam's external position, expecting the improvement in regional demand to boost Vietnam's trade in 2Q .

- **Key Domestic Events and Issues to Watch:** PMI-mfg is due on the 3rd. CPI is due on the 24th. Trade balance, retail sales, industrial production within 25-31st.

- **Technical Outlook:** USDVND hovered within 22700-22770 for the past few sessions, capped by the 50-DMA. Daily momentum is mild bullish though stochs approaches overbought conditions. Weekly momentum also turning lower. We see some risks to the downside towards the 22700 as price action suggests a mini double top around 22760. A break of the 22700 support opens the way to Apr low of 22650.

FX Forecasts

	End Q2-17	End Q3-17	End Q4-17	End Q1-18
USD/JPY	108	110	113	113
EUR/USD	1.0800	1.0700	1.0800	1.1000
GBP/USD	1.3000	1.2600	1.2800	1.3000
AUD/USD	0.7300	0.7500	0.7800	0.7800
NZD/USD	0.7100	0.7300	0.7500	0.7700
USD/SGD	1.4100	1.4200	1.3950	1.3950
USD/MYR	4.3000	4.2500	4.3000	4.3500
USD/IDR	13300	13400	13450	13500
USD/THB	34.80	35.30	36.00	36.20
USD/PHP	50.30	50.50	50.70	50.70
USD/CNY	6.95	7.01	7.04	7.04
USD/HKD	7.80	7.80	7.80	7.80
USD/TWD	30.80	31.50	32.00	32.00
USD/KRW	1140	1150	1160	1170
USD/INR	65.00	65.70	66.20	66.00
USD/VND	22900	23100	23300	23400
DXY Index	99.22	100.16	99.83	97.98
SGD Crosses	**End Q2-17**	**End Q3-17**	**End Q4-17**	**End Q1-18**
100 JPY/SGD	1.3056	1.2909	1.2345	1.2345
EUR/SGD	1.5228	1.5194	1.5066	1.5345
GBP/SGD	1.8330	1.7892	1.7856	1.8135
AUD/SGD	1.0293	1.0650	1.0881	1.0881
NZD/SGD	1.0011	1.0366	1.0463	1.0742
SGD/MYR	3.0496	2.9930	3.0824	3.1183
SGD/IDR	9433	9437	9642	9677
SGD/THB	24.68	24.86	25.81	25.95
SGD/PHP	35.67	35.56	36.34	36.34
SGD/CNY	4.94	4.94	5.05	5.05
SGD/HKD	5.53	5.49	5.59	5.59
SGD/TWD	21.84	22.18	22.94	22.94
SGD/KRW	809	810	832	839
SGD/INR	46.10	46.27	47.46	47.31
MYR Crosses	**End Q2-17**	**End Q3-17**	**End Q4-17**	**End Q1-18**
EUR/MYR	4.64	4.55	4.64	4.79
JPY/MYR	3.98	3.86	3.81	3.85
MYR/HKD	1.81	1.84	1.81	1.79
MYR/CNY	1.62	1.65	1.64	1.62
GBP/MYR	5.59	5.36	5.50	5.66
AUD/MYR	3.14	3.19	3.35	3.39
NZD/MYR	3.05	3.10	3.23	3.35
MYR/IDR	3093.02	3152.94	3127.91	3103.45
MYR/INR	15.12	15.46	15.40	15.17
MYR/KRW	265.12	270.59	269.77	268.97
MYR/PHP	11.70	11.88	11.79	11.66
CNY/MYR	0.6178	0.6054	0.6099	0.6170

Source: Maybank FX Research as of 28 April 2017

*These forecasts are meant to be indicative of FX trends and not meant to be point forecasts.

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