Maybank

Macro | FX Research & Strategy

Global

FX Monthly

2022, Issue 7: Facing Recession with No Fear…?

What Has Changed This Month?

- We left most currency forecasts unchanged and made modest adjustments to CAD, KRW, THB, JPY. Rising recession risks weighed on pro-cyclical CAD, KRW, THB, but triggered an unwinding in JPY shorts, as markets pared back bets on pace of Fed hikes.

Our Strategies

- Markets are focusing on how Fed is getting closer to tapering off the magnitude of rate hike after Fed Chair Powell said that it will be appropriate to slow hikes 'at some point'. We think a corrective unwinding in USD longs is justified after the build-up but it may be too early to concur at this stage as the risk of another 75bps hike at Sep FoMC is still possible given elevated inflation. Also Fed Chair Powell did comment that "another unusually large increase could be appropriate at our next meeting" and that is dependent on data. Softer inflation prints ahead could lead to expectations of step-down in pace of tightening and that could drag on UST yields and USD.
- Regional USD-AxJ pairs continue to retrace lower from recent highs, aided by broader bout of dollar softening. Drags on policy-tightening laggards IDR, THB show tentative signs of easing, given recent decline in UST yields. For PHP, sentiments likely received a modest boost from greater policy clarity. President Marcos had introduced a 19-point legislative agenda to spur growth and attract new investment flows. Meanwhile, in line with our expectations post MAS off-cycle, SGD NEER has risen to near the middle of our +0.5% to +1.5% above par projection range, and pace of gains could slow a tad going forward. Among AxJ FX, MYR could be more sensitive to external risk triggers, given exposures via significant China trade linkages and oil outlook. Sentiment recovery could take time.

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Top 3 Currency Plays for Aug

Sell USDJPY Rallies
Long SGDCNH on Dips
Long AUDCAD

Key Events for the Month Ahead

Date	Event
Aug	US House Speaker Nancy Pelosi's Asia Visit

G7 Global Overview

USD: Managing Growth Concerns

Forecast	3Q 2022	4Q 2022	1Q 2023	2Q 2023
USD Index	105.17 (104.36)	103.72 (101.71)	102.42 (100.87)	100.76 (99.30)

Previous Forecasts in Parentheses

- **Motivation:** US 2Q GDP contracted 0.9% q/q annualised (vs. 0.4% expected). The second consecutive quarterly contraction puts US economy in a technical recession. And this leads markets to further unwind Fed rate hike expectations. Fed fund futures now show 50bps hike expectation for Sep FoMC vs. 50% probability of 75bps hike a week ago. This is likely to be followed by 25bps each in Nov and Dec.

- The USD DXY rose around 4% in July before retracing back 3% by end of the month, continuing its ups and downs, to end at around 105.91 slightly higher than the 104.91 (as at 30 June). The euro, GBP and JPY strengthened vs USD in the second half of July despite Fed tightening with 75bps moves, as ECB and BOE raised their policy rates and US growth concerns rise and markets price in a potential peak in Fed hawkishness. The markets retracement is expected but may have been slightly overdone.

- We are likely to see USD swings continue over the next few months as the USD is likely to remain supported on the back of the protracted Russia-Ukraine geopolitical situation, even as the expectations of tighter Fed policy move eases subject to the volatility of data releases. The global growth concerns intensifying and continued frictions in the inflation dynamics working its way through the global economy suggest that markets may be mired in a risk-based cautious view based on the global economic backdrop. These factors are likely to lead to USD support and delay any further sharp USD retracement towards end of the year. Nonetheless, signs of slowdown in the US economy and concerns of an eventual easing by the Fed, an improvement in the geopolitical space and positive developments out of China, coupled with reopening globally can quickly allow for some space for cyclical FX to intermittently strengthen relative to USD.

- Amongst ASEAN FX, Fed's current hawkish monetary policy divergence may marginalize some ASEAN FX, including MYR whose monetary policy may be perceived to still be relatively accommodative. On the other hand, SGD could find solace from a hawkish MAS.

- To sum up, near-term (coming 3-6 months) risks remain skewed to the upside for broad USD. We revise our forecasts for JPY slightly stronger, and some regional currencies to reflect the recent domestic and market developments.

- Global growth could see downside risks in 2H & global inflation momentum could start to peak, even as any easing in headline readings should be a slow grind. Meanwhile, chatters of US recession risks could lead policymakers to be more careful in calibrating rate hike pace, in attempt to engineer soft growth landing. UST yields have begun moderating on above-mentioned factors. Current DXY strength could be more tied to haven demand, and extent of rally could be constrained, even as DXY looks to remain in elevated ranges near-term. We remain long USD in the short term but factor in a moderation in USD as we approach year end as inflation momentum eases in end 2H with oil prices easing and potentially some US tariffs on Chinese imports are removed concomitantly a Fed hawkish signalling to ease after Jul FOMC (milder rate hike trajectory).

- **Growth and Inflation Outlook:** 2Q adv reading for real GDP declined 0.9% (consensus: 0.4%), largely due to inventories led by a $45bn annualized drop in farm inventories. Consumption growth slowed to 1.0%, its slowest pace of the expansion compared to 2.6% average pace in 2017-2019. Government expenditure also contracted but net trade contributed 1.4pp to GDP growth on the back a rapid rise in exports and some normalization in imports (3.1% after 18.9% in 1Q).

- Non-farm payrolls rose 372k for June (consensus: 265k) albeit with a third month of downward revisions and of underperformance in household employment. Unemployment rate was unchanged at 3.6%, but the underemployment rate fell sharply on fewer part-time workers. Average hourly earnings rose 0.3% m/m and 5.1% y/y.

- **Monetary Policy Forecast:** The FOMC raised the fed funds rate target range by 75bps to 2.25%-2.5%, in line with consensus expectations. The FOMC statement's policy outlook was unchanged from the June statement. No voters dissented in the July decision compared to the June session. The statement's characterization of economic growth was downgraded slightly, acknowledging that "recent indicators of spending and production have softened." However, the rest of the economy was unchanged, with job gains "have been robust in recent months" and that inflation "remains elevated."

- The press conference with Powell, seems quite dovish as Powell reiterated the June dot plot and highlighted that the 75bp hikes thus far are "unusually large" and that it will likely become appropriate to slow the pace as policy tightens. Powell also shared that the full impact of rate hikes has not been fully transmitted into the economy yet. Most importantly, he also highlighted that the FOMC would react to upcoming data on growth, labor market, and inflation compared to the focus on inflation previously.

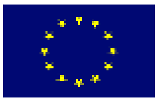
- The June FOMC median dot in the Summary of Economic Projections (SEP) shows a funds rate midpoint of 3.375% at end-2022, up from the 1.875% rate projected at the Mar meeting - which correspond to a 75bp hike at the July meeting, 50bp at Sep, 25bp at Nov, and 25bp at Dec meetings. Sixteen out of eighteen participants projected a funds rate above the median longer-run dot in 2024, with the longer-run median edging back up to 2.5% (vs. 2.375% in March).

- Fed's latest "dot plot" signals another +100bps FFR hikes in the remaining three FOMC meetings this year to 3.375% in 2022 vs 1.625% mid-point of current target FFR range, with current hikes cycle ending in early-2023 at 3.75%. Fed's policymakers expect FFR to be at 3.375% in 2024.

- Fed raised its 2022 inflation rate forecasts to 5.2% vs 4.3% in Mar 2022 but trimmed inflation rate forecasts for 2023 and 2024 to 2.6% and 2.2% respectively from the Mar 2022s's projections of 2.7% and 2.3%. Fed bumped up its unemployment rate forecasts to 3.7%, 3.9% and 4.1% for 2022, 20223 and 2024 respectively from 3.5%-3.6% range previously. Fed's 2022-2024 real GDP growth forecasts are trimmed to sub-2% i.e. 1.7% in 2022-2023 and 1.9% in 2024 vs 2.8% in 2022, 2.2% in 2023 and 2.0% in 2024 previously.

- **Key domestic events and issues to watch in Aug:** ISM Manuf (1 Aug); Factory orders, durable goods orders (3 & 24 Aug); Trade Balance (4 Aug); NFP (5 Aug); CPI (10 Aug); FOMC Minutes (18 Aug); FOMC Meeting Minutes (7 Jul); PCE deflator (26 Aug); 2Q GDP (25 Aug).

- **Technical Outlook:** DXY took a turn lower after hitting a multi-year high of 109.29 (mid Jul). Last at 106 levels. Bearish momentum on daily chart intact while RSI fell. Still bias for downside play. Key support at 105.90 (23.6% fibo retracement of 2022 low to high). A decisive break there will see further losses accelerate towards 104.75 levels (50 DMA), 103.80 (38.2% fibo). Resistance at 106.95 (21 DMA), 107.50 and 108.20.



EUR: Italy Politics a Curve Ball to Recovery

Forecast	3Q 2022	4Q 2022	1Q 2023	2Q 2023
EURUSD	**1.0350** (1.0500)	**1.0500** (1.0800)	**1.0600** (1.0800)	**1.0800** (1.1000)

Previous Forecasts in Parentheses

- **Motivation for the FX View: We look for EUR recovery to continue amid hawkish ECB** while USD strength and hawkish Fed may have found an interim peak. But the recovery is not one-way as emergence of Italian political uncertainty can heighten volatility in the lead-up to snap elections in Sep. Elsewhere some of the negatives – energy woes, EU recession risks could continue to pose lingering drags on EUR. That said, the ECB has shown determination to tighten with a larger than expected 50bps hike and could continue to do so amid high inflation in the Euro-area. Some member EU countries such as Estonia, Lithuania and Latvia are already hitting between 16% and 20% for headline CPI.

In addition, the introduction of anti-fragmentation tool - TPI to compress yield spreads should further complement ECB's policy normalisation process. We look for EUR to trade in 1.00 – 1.04 range in coming weeks.

- **Italy Snap Election on 25 Sep.** It was Five Star Movement (5SM) whose earlier action triggered the political mess in Italy – as it refused to vote on the EUR26bn package to help Italians tackle inflation and energy costs. Meanwhile Forza Italia and the The League called for a new Draghi-led government without 5SM as its coalition partner. Premier Draghi later resigned for the second time (21 Jul) despite winning the confidence vote (95-38) in the senate (315 members) as he lacks the backing of all three of his key coalition allies – Five Star Movement (5SM), Northern League and Forza Italia who boycotted the confidence vote. Nonetheless, Draghi enjoyed broad support at home and abroad. President Materella subsequently dissolved parliament and a snap election awaits on 25 Sep. Based on current polls, the favourite is the coalition led by far right Brothers of Italy (Giorgia Meloni is the leader), including Northern League (Salvini the leader) and Forza Italia (Berlusconi the leader). Brothers of Italy polls ahead with 24% while Democratic party (PD) takes second place with 22%. PD (Enrico Letta the leader) may need to form an alliance with 5SM (Conte the leader) to mount a serious challenge on the Far Right. Polling results remain too early to call and political developments can be fluid. We keep in view upcoming polls for support shifts.

- **Energy Woes, Geopolitics Still 2-Way Risks for EUR.** As of writing (26 Jul), gas flows from Russia to Germany are planned to be cut to 20%, from about 40% of capacity (effective 27 Jul) and current flows remain insufficient to fill storage facilities prior to the peak winter heating season. Following the release of turbine from Canada, it's currently stuck in transit in Germany with no Russia permit. Markets are concerned that flows could retreat if part of a key turbine is not returned and Putin had warned that volumes could be cut to 20% of capacity by the end of this month, when another part is due for maintenance.

- Elsewhere, ongoing military conflict in Ukraine shows no signs of abating despite Moscow and Kyiv reaching a deal to allow shipment of grains to ease global food crisis. Russian missiles hit the Black Sea port of Odessa a day after the grain agreement. Nonetheless geopolitics risk remains fluid and should continue to pose 2-way risks to EUR. An end to conflict may be too soon to call but the scenario should never be ruled out. We note that Russia is rushing to hold referendums in Ukrainian territories occupied by its troops to "merge" them into Russia by early September. Some of these Russian-occupied Ukrainian territories are Donetsk, Luhansk, Kherson and Zaporizhzhia. Some political experts believe that these territories may represent Putin's basic goals and with these, he could possibly declare victory.

- **ECB Likely to Hike Another 50bps at Sep Meeting.** With inflation still showing no signs of abating and the availability of new tool – Transmission Protection Instrument, we opined another back to back 50bps hike to bring MRO and deposit rate to 1% and 0.5%, respectively is highly likely. ECB speaks so far had hinted at another hike of similar magnitude. For example, Lagarde said that ECB will hike rates as much as needed to tame prices. Nagel said that it is better to start with bigger rate increase and that the TPI will be used in exceptional circumstances. Holzmann said that ECB may have a to accept a moderate recession to stem price pressures if it sees signals that inflation expectations are rising. Kazaks said that this was “not the only front-loading” and he would say that “rate increase in Sep also needs to be quite significant”. He also said he has “no major objections” to recent market expectations for 150bps of tightening by Jun-2023.

- **Further Upside Risks to EUR if** (1) war in Ukraine shows signs of abating; (2) ECB catches up on policy normalisation (i.e. +75bps hike); (3) EU growth momentum though may be impacted but not derailed.

- **Growth and Inflation Outlook: ECB lowered growth projection for 2022 to 2.1%, down from 2.8% previously while maintaining earlier projection of 2.1% growth for 2023.** Lagarde indicated that a “prolongation of the war in Ukraine remains a source of significant downside risk to growth, especially if energy supplies from Russia were to be disrupted to such an extent that it led to rationing for firms and households. 2Q GDP will be released on 29 July – when the report would not be in time to capture. But consensus suggests growth deceleration for 2Q. Looking at prelim PMI for Jul, manufacturing unexpectedly slipped into contractionary territory of 49.6 (down from 52.1) while services slowed to 50.6 from 53. ZEW survey also plunged to -51.1, from -28 while consumer confidence slumped to -27 in Jul, down from -23.6 in Jun. Taking stock, final 1Q growth saw upward revision to 0.6% q/q vs. 0.3% in initial estimate. Higher revision was due to trade even though household consumption fell. On annual basis, Euro-area growth came in at 5.4% y/y vs. 5.1%.

- **Headline CPI rose to record high of 8.6% y/y in Jun, up from 8.1% in May.** Nearly half of the record high inflation resulted from energy prices while food and services are the other major factors driving prices higher. Across Euro-area nations, Estonia has the highest CPI at 22% while Lithuania, Latvia and Slovakia saw CPI at 20.5%, 19.2% and 12.6%, respectively. Lowest CPI was recorded in Malta (6.1%) and France at 6.5%. Germany and Finland are close to Euro-area headline print/ Core CPI was at 3.7% in Jun, a touch softer than 3.8% printed in May. We retain our view that inflation could still remain elevated amid worsening supply chain disruptions, higher energy prices amid ongoing war in Ukraine. Pursuit of climate change goals could also further keep commodity price pressures broadly supported. Weaker EUR (more than 12% peak to trough YTD) may also have resulted in some imported inflation. Overall, we still expect ECB to play catch-up in normalizing policies especially if inflation proves to stay elevated for longer. This can be a positive for EUR. ECB projected inflation at 6.8% and 3.5% in 2022 and 2023, respectively with assumption of average oil price of $105.8/bbl and $93.4/bbl for 2022 and 2023, respectively.

- **Monetary Policy Forecast:** There is no meeting scheduled in Aug. **The next one is on 8 Sep. We opined that another 50bps rate hike is plausible to combat price pressures.** As of 22 Jul, markets are pricing in slightly more than 50bps rate increase at Sep meeting and for cumulative 100bps hike for remaining 3 meetings in Sep, Oct and Dec.

Going forward, t**here will be no forward guidance as indicated by ECB and that future rate decision is data-dependent.**

- At the last Governing Council meeting (21 Jul), ECB raised rates by 50bps for deposit rate, Main Refinancing Operation (MRO) and marginal lending facility. So these rate now stand at 0%, 0.5% and 0.75%, respectively. This is the first interest rate increase in 11 years for the ECB and the magnitude of hike was larger than earlier flagged by ECB (+25bps) though we noted that markets were split between 25bps and 50bps hike. At the press conference, Lagarde said that that an updated assessment of inflation risks and ECB's approval of the new anti-fragmentation policy tool (Transmission Protection instrument or TPI) had led to the decision to double the pace of hike. She also painted a gloomy outlook owing to growth slowing, war in Ukraine being a drag on growth, higher cost of living as a result of high inflation while business face supply chain disruptions and higher costs. But ECB's mandate is about price stability, so raising rates to combat inflation takes priority especially when "price pressure is spreading across more and more sectors". Inflation is still expected to remain "undesirably high for some time", due to higher food, energy prices as well as wage increases. Looking on, ECB did not provide forward guidance on future rate increases, saying only that further increases will be as appropriate and decisions will be made meeting-by-meeting. On the new tool – TPI, it will allow ECB to counter disorderly moves in government bond markets (in the 1y to 10y space) if it believes the bonds of these Euro-area nations are experiencing unwarranted disorderly market dynamics that pose a risk to ECB effectively delivering on its price stability mandate. ECB also indicated that purchases of private sector securities could be considered if appropriate. Activating this instrument will be entirely at the discretion of ECB. Purchases would be terminated upon durable improvement in transmission or based on assessment that persistent tensions are due to country fundamentals.

- **Latest Fiscal and External Balance Outlook**: Euro-area current account posted a deficit of EUR4bn in May, similar to Apr's deficit. Deficits were mainly for secondary income and goods balance. In the 12 months to May 2022, the current account recorded a surplus of EUR138 billion (1.1% of euro area GDP), compared with a surplus of EUR352 billion (3.0% of euro area GDP) in the 12 months to May 2021.

- **Key domestic events and issues to watch:** Jul mfg PMI, unemployment rate (1 Aug); Jul services PMI, Jun PPI, retail sales (3 Aug); Sentix investor confidence (8 Aug); Jun IP (12 Aug); Aug ZEW survey, trade (16 Aug); 2Q employment, GDP (17 Aug); Jun construction output (18 Aug); Jul CPI (18 Aug); current account (19 Aug); Aug prelim PMIs, consumer confidence (23 Aug); Aug CPI estimate (31 Aug).

- **Technical Outlook:** EUR's partial recovery post early-Jul's decline is underway. Pair traded below parity briefly in Jul; last at 1.0220 levels. Daily momentum is mild bullish while RSI is flat. Consolidative trades likely with risks skewed to the upside. Resistance at 1.0270 (38.2% fibo retracement of May high to Jul low), 1.0370 (50% fibo) and 1.0420 (50 DMA. Support at 1.02 (21 DMA), 1.0150 (23.6% fibo) and 0.9950 levels

GBP: BoE to Shift to 50bps Hike

Forecast	3Q 2022	4Q 2022	1Q 2023	2Q 2023
GBPUSD	1.2200 (--)	1.2300 (1.2500)	1.2400 (1.2800)	1.2600 (1.2800)

Previous Forecasts in Parenthesis

- **Motivation for the FX View**: We expect GBP short squeeze to play out in coming week or two, as markets shake out stale shorts ahead of BoE MPC (4 Aug). We expect BoE to increase its pace of tightening to 50bps combat inflation before expectations get entrenched. But sell-on-rally trade for GBP could soon come into play after position shake-out as UK still face stagflation risks while domestic political uncertainty should drag on GBP in the lead-up to 5 Sep, when the new PM is unveiled. Furthermore, political pressures, including risk of EU-UK trade war due to parts of NI protocol being scraped, Scottish referendum should continue to weigh on GBP. We look for 1.18 – 1.23 range in coming weeks. But we expect some of the drags – energy woes, supply chain disruptions to fade towards year-end. Potential improvement in the geopolitical space and positive developments out of China, coupled with reopening globally (drivers of growth) should allow for GBP to intermittently strengthen relative to USD.

- **Truss as PM Implies Heightened Volatility for GBP.** Its down to former Chancellor Rishi Sunak or Foreign secretary Liz Truss as next UK PM after more than 150,000 Conservative party members vote. Result should be announced by 5 Sep. Sunak is perceived as a “policy continuity” candidate while Truss is seen to embrace Brexit, from her recent hard stance against EU (took the lead to scrap parts of Brexit deal arrangement with Northern Ireland). Her manifesto also highlighted a series of tax cuts, including the increase in national insurance, abandon planned corporate tax increase and even strike off “environmental levies” off energy bills. She believes that tax cuts increase the supply side of the economy. Potentially, this could boost near term growth outlook, inflation and could potentially trigger faster BoE. A Sunak government would likely mean slow growth while corporates will be subjected to the corporate tax hike (25% in 2023, up from 19%) he imposed when he was Chancellor. He stood by his decision not to cut taxs until inflation was curbed. As such we envisage higher volatility (more 2-way trades) for GBP in the event Truss is elected PM. Her manifesto may provide some near term boosts for GBP but her hard stance on EU risks triggering EU-UK trade war (a negative for GBP). In the first head-to-head debate (25 Jul), Sunak warned that Truss’s planned tax cuts would push up inflation and interest rates, add thousands of pounds of mortgage payment and top people into misery while Truss fought back and said Sunak’s plan would drive the economy into recession. Yougov polls has shown than Truss is poised to beat Sunak by 24 points in a run-off.

- **Plenty of Political Uncertainties a Drag on GBP**. EU launched 4 new legal procedures against UK (22 Jul) after UK lower house cleared a bill to unilaterally scrap parts of brexit deal arrangement with Northern Ireland. Cumulatively, the number of infringement procedures now stand at 7 and is possible more procedures are launched to protect EU single market from British violations of the NI protocol. Britain as 2 months to respond. The ECJ could impose fines but this is not likely to happen for at least a year. We had earlier said that Britain's action constituted to a breach of international treaty and risks of EU-UK trade war should not be ruled out. Elsewhere First Minister Nicola Sturgeon told members of the Scottish Parliament (MSPs) that her government want to stage a second Scottish independence referendum on 19 Oct 2023. She has asked the supreme court to rule on the legality of holding a new referendum without Westminster's permission. It is believed that the court will rule it unlawful without Westminster giving it the powers to do so under section 50 of the Scotland Act. Play-up of multiple political risks can undermine GBP.

- **GBP Short a Stagflation Proxy Trade**. BoE's dire economic projection that UK growth will stagnate into 2024, alongside double-digit inflation makes a strong case for stagflation in UK and underscores our bias for short GBP as a stagflation proxy trade. BoE was not alone with its bearish assessment. Earlier, the IMF also assessed UK's economic growth to be more gloomy as it projected UK to "slump to the bottom of the league table of comparable economies in G7" and "it will also face the highest inflation". The protracted war in Ukraine and extended covid lockdowns in China further worsened global supply chain disruption, driving up food and energy prices, in turn adding to inflationary pressures and dragging on household disposable income and overall growth. Moreover the 4-5% depreciation in GBP on trade-weighted basis YTD will further pushed up imported inflation.

- **Growth and Inflation Outlook: UK growth surprised to the upside in May (+0.5% m/m vs. -0.3% in Apr).** Growth was broad-based across sectors, including health though there was some weakness in consumer-facing acitivies. 2Q GDP may contain some upside surprises as IP, construction output, retail sales came in better than expected while consumer confidence is no longer falling (held ground at -41). IMF projected UK growth to slow to 1.2% in 2023, from 3.7% growth projection in 2022 (already a cut from earlier forecast of 4.7%). The sharp downward revision was due to projection for consumption to be weaker than expected as inflation erodes real disposable income, while tighter financial conditions are expected to cool investment. Elsewhere, BoE warned of UK recession as it cited concerns on the impact of extended covid lock down in China (hitting supply chain and price pressures). That said 2022 growth forecast was maintained at 3.75% but a 0.25% contraction was pencilled in for 2023 growth (vs. earlies projection of 1.25%).

- **Headline CPI surged to fresh 40-year high of 9.4% y/y in Jun,** up from 9.1% in May. Food and fuel remain the main drivers of higher prices. Recall that the energy price cap increase by 54% wef 1 Apr partly contributed to the record high 9% headline CPI. We see risks of inflation staying elevated as protracted war in Ukraine continued to result in cost-push inflation, affecting prices of food, energy, fertiliser and industrial metals. These will further add to upward pressure in coming months. Meanwhile core inflation continue to ease from all-time high of 6.2% y/y to 5.8% in Jun. BoE projected inflation to hit above 11% in Nov, due to another round of increase (40%) in UK energy price cap. Households are also projected to face a 1.75% drop in real disposable income this year, the second biggest decline since 1964.

- **Monetary Policy Forecast: We expect BoE to increase its pace of hike to +50bps at the next MPC on 4th Aug.** This will be the 7th increase to bring policy rate to 1.75%. Bringing inflation down to its medium term target of 2% remains BoE's priority. The last MPC also saw a hawkish shift in tone - policymakers signaled they are prepared to "act forcefully" to tame inflation if needed. BoE Governor Bailey also said that the central bank will bring inflation back to 2% target "no ifs, no buts" and officials prepared to move borrowing costs higher in bigger steps if needed to curb prices. Markets are now pricing in ~45bps hike each at Aug and Sep MPCs.

- At the last BoE meeting (16 Jun), the MPC voted 6-3 to raise rates by 25bps. 3 members voted for 50bps increase while 6 voted for 25bps. BoE also projected inflation to jump above 11% in Oct, due to another round of increase (40%) in UK energy price cap. In a speech in Germany (24 Jun), BoE Chief Economist Huw Pill said that "given the tightness of the labor market and perceived strength of pricing power in large parts of the corporate sector, the threat exists that higher headline CPI leads to second round effects in prices, wages and costs that exacerbate the magnitude and crucially, the persistence of the target overshoot". He also supports BoE to act "more aggressively" if needed. In an MNI event (20 Jun), BoE's Mann said that BoE needs to raise rates more aggressively to stave off a drop in GBP that would drive up inflation. She added that domestic price pressures are likely to prove firmer because of government stimuli, strong employment, big bonus payments to workers, strength of housing market and build-up of savings by consumers. She also made reference to faster pace of tightening from Fed and ECB, and that BoE should move more quickly. She was one of the MPC dissenter whom voted for 50bps hike at previous BoE MPCs.

- **Fiscal and External Balance Update:** Public sector net borrowing was GBP22.9bn in Jun. This was GBP4.1bn more than in Jun-2021. Public sector net debt, excluding public sector banks, totalled GBP2.07tn or 83.2% of GDP. 1Q current account deficit widened sharply to GBP51.7bn, from deficit of GBP7.3bn in 4Q. This represents a deficit of 8.3% of GDP, the largest shortfall since 1955. Goods deficit widened sharply while primary income turned into deficit. ONS did caution that there is more uncertainty than usual due to impact post-Brexit in how data for goods imported and FDI are being collected.

- On 26th May, **former** Chancellor Sunak unveiled the latest set of support measures as part of a GBP15bn package targeted at alleviating rising costs. Millions of households will receive GBP400 discount on their energy bills, a one-off GBP650 payment for 8mio of the worst-off households, a one-off GBP300 payment to 8mio pensioner households and GBP150 each to 6mio disabled people. A 25% windfall tax was imposed on profits of oil and gas (O&G) companies, but with a 90% tax relief for firms that invest in O&G extraction in the UK. The 25% windfall tax will raise around GBP5bn revenue to finance the latest set of measures. Sunak said that the latest measures will have minimal impact on inflation as measures are targeted and partially funded by raising new money.

- **Key domestic events and issues to watch:** Jul PMI Mfg (1 Aug); services PMI (3 AUg); construction PMI, BoE MPC (4 Aug); 2Q GDP, Jun industrial production; monthly GDP, construction output, trade (12 Aug); Jun labor market report (16 Aug); Jul CPI, PPI (17 Aug); Jul retail sales, Jul public finances (19 Aug); Aug prelim PMIs (23 Aug).

- **Technical Outlook:** GBP saw partial retracement of its losses in Jul. Last at 1.22 levels. Mild bullish momentum on daily chart intact while RSI shows tentative signs of turning lower. We still caution for 2-way risks amid fluidity of domestic politics. Support at 1.20 (21 DMA), 1.1950 levels. Resistance at 1.2240 (50 DMA), 1.2350 (23.6% fibo retracement of 2021 high to 2022 low) and 1.2520 (100 DMA).

AUD: Not Immune to Swings but Likely Cushioned by Demand for its Commodities in a Resource-Scarce World

Forecast	3Q 2022	4Q 2022	1Q 2023	2Q 2023
AUDUSD	0.7000 (--)	0.7000 (--)	0.7100 (--)	0.7200 (--)

No Change to Previous Forecasts

- **Motivation for the FX View:** We retain a cautiously optimistic view on the antipode. To some extent, China's property malaise have driven a price correction for base metals such as iron ore. There could be further declines in base metal prices but the strong infrastructure thrust by the Chinese government may provide some cushion on the margins. In addition, export volume of coal and natural gases have been on the rise (to help plug the gap for Europe's energy shortage) and could contribute to Australia's trade surpluses, a cushion for the AUD to counter risk-off swings amid recession fears.

- Meanwhile, cash futures imply a longer runway for RBA to hike rates compared to its developed peers (Fed, RBNZ, amongst others) possibly due to difference in inflation trajectory. RBA is expected to hike its cash target rate by around 200bps by the end of 2022. That could certainly bring its policy rate closer towards the Fed fund target rate. Property prices have started to soften but more recently, RBA has highlighted higher household savings (relative to pre-pandemic level), stringent lending standards, strong household balance sheet and the fact that only 1/3 of households have housing debt as strong reasons for Australia's financial system to withstand further rate increases. Credibility of the central bank to raise rates is especially important in an inflationary environment and we reckon, can provide support to the AUD.

- **Growth and Inflation Outlook:** Australia's preliminary Jun services PMI slipped to 50.4 vs. previous 52.6, a a sharp contrast to the Mfg PMI holding up at 55.7 (albeit still softer vs. previous 56.2). The services PMI underscores the demand destruction of rising inflation as well as mortgage rates that likely affected consumption. Most of the leading indicators paint the same picture including the deterioration of business confidence for 2Q (5 vs. previous 15) as well as the fall in Westpac consumer confidence for Jul to 83.8 vs. previous 86.4.

- CoreLogic have logged back to back declines in median city values for May (-0.3%m/m) and Jun (-0.8%m/m). More recent reports citing CoreLogic suggest that the price declines have accelerated for a few key cities (Sydney, Brisbane, Melbourne) over the past few weeks of Jul because of the rise in the cost of living as well as interest rate burdens.

- The silver lining at this point is still Australia's strong labour market. Labour market conditions remain tight with a net 88.4K jobs added in Jun (+52.9K full-time and +35.5K part-time). Participation rate rose to 66.8% from previous 66.7% and the jobless rate dropped to 3.5% from preivous 3.9%. Tight labour market conditions could give RBA confidence to tighten further.

- Consumer inflation expectation eased a tad to 6.3%y/y in 2Q from previous 6.7%. Australia's CPI came in a tad softer than expected at 6.1%y/y, albeit still a significant pick-up from previous 5.1%. The pick-up was broad-based with food, clothing and footwear, housing, household furnishings, and recreation registering stronger price increase for 2Q on a year-on-year basis. Trimmed mean actually came in above expected at 4.9%y/y vs. previous 3.7%. inflation pressure could continue to rise given the hefty 5.1% hike on minimum wage that took effect on 1 Jul. With measures of underlying inflation well above the 2-3% inflation target of the central bank and the latest CPI report is likely to nudge RBA to raise cash target rate by another 50bps. Cash rate futures still imply a 50bps hike next week and RBA speakers have made a strong case that the financial stability would not be strained by further rate hikes to counter inflation.

- **Monetary Policy Forecast:** RBA raised cash target rate by 50bps to 0.85% and another 50bps is expected on 2 Aug as the central bank vows to counter inflation. The most recently released M-I inflation expectations for Jul eased only a tad to 6.3%y/y from previous 6.7%. 2Q CPI was not too far at around 6.1%y/y and could gather pace on floods at home, elevated energy prices while a tight labour market thus far (unemployment at 3.5%) suggest that the economy can withstand further rate increases. Recently, RBA board member Ian Harper had noted that broadening price pressures should spur RBA to act. In July, the central bank had acknowledged concerns on household spending but highlighted that household saving ratio remains higher than pre-pandemic levels and can support debt repayments as mortgage rates rise. This underscores a strong case for RBA to continue to raise cash target rate by clips of 50bps until inflation trends back towards the 2-3% target range.

- **Latest External Balance Outlook:** As of last available data, current account surplus was recorded at 2.9% of GDP for 1Q 2022, narrowing from the previous 3.53%. Current account balance fell to A$7.5bn from A$4635b on narrower goods and services surplus (from previous $A29.1bn to $28.2bn) and wider primary income deficits.

- **Fiscal Outlook:** Treasurer Jim Chalmers delivered a ministerial statement on budget this morning, downgrading the economic growth forecast for FY2022 (ending Jun) to 3.75% from previous estimate of 4.25% (made by the former government). A slight deceleration is expected to 3% for FY2023 and then to 2% for FY2024. Inflation is expected to peak at 7.75% by Dec before moderating to 5.5% by Jun 2023. The downgrades in forecast are made due to inflation and rising interest rates that could weigh on the property market and household spending. A full set of fiscal forecasts would be presented in Oct.

- **Key domestic events and issues to watch:** Jul Mfg PMI, M-I inflation, ANZ job advertisements (1 Aug), Jul CoreLogic House Price, Jun home loan, Jun building approvals, RBA policy decision (2 Aug), Services PMI for Jul (3 Aug); Jun trade (4 Aug); SoMP (5 Aug); foreign reserves (8 Aug); Jul NAB business conditions, confidence (9 Aug); Aug Westpac consumer confidence (10 Aug); Minutes of the RBA Policy meeting (16 Aug); 2Q wage price index (17 Aug); Jul labour report (18 Aug); Flash Aug Mfg, Services PMI (23 Aug); Jul retail sales (29 Aug); Jul building approvals (30 Aug), Jul private sector credit (31 Aug).

- **Technical Analysis:** AUDUSD rebounded above the 0.70-figure by end Jul, buoyed by the broader USD strength. Bullish momentum remains intact on the daily and weekly chart. Stochastics on the weekly chart show signs of turning higher from oversold condition. We look for further bullish move notwithstanding retracements. The next resistance is seen around 0.7060 (38.2% Fibonacci retracement of the Apr-Jul sell-off) before 0.7175 (200-dma). Support is seen around 0.6970 (50-dma).

NZD: Unwinding Some of Global Growth Scares

Forecast	3Q 2022	4Q 2022	1Q 2023	2Q 2023
NZDUSD	0.6400 (--)	0.6500 (--)	0.6600 (--)	0.6600 (--)

No Change to Previous Forecasts

- **Motivation for the FX View: Our call in the last FX Monthly that *NZD sell-off might have been overdone and we expect the pace of NZD's decline to moderate and possibly partially reverse some of its weakness* panned out well for the month of Jul.** Broad improvement in covid situation in China, alongside borders relaxation/economy reopenings in Asia, including NZ should help mitigate growth downturn to some extent. Relative stability in global equities (NZX50 up 3% while

US equities up nearly 5% MTD basis) – risk sentiment channel - and potential peak in Fed hawkishness/USD strength may continue to serve as mitigating factors for Kiwi to find some support. Looking on, markets will also focus on US review on China tariffs. Potential partial removal of US tariffs on Chinese imports can be modestly be supportive of risk sentiment. In addition, a hawkish RBNZ walking its talk should also be supportive of NZD. We still maintain a mild upward trajectory profile for NZD into 2023. The case for a more durable Kiwi rebound would however require global growth to pick up momentum, China to stand-down on their zero covid policy and see a reopening of their borders and economy.

- **Hawkish RBNZ Can Shore Up Support for NZD.** RBNZ is expected to continue raising rates in clips of 50bps for 2 more meetings this year at the Aug and Oct meetings. As the last MPC (13 Jul) was a review meeting hence a shorter MPS. The focus is on Aug MPC for new projections for cash rate and economic indicators. In particular if RBNZ revises upwards its projection for OCR to beyond current of 4%. Governor Orr is concerned of inflationary expectations becoming unanchored and more persistent and hence wants to avoid doing 'too little too late'. While it is likely RBNZ may pause or even slow its pace of tightening at the last meeting this year (Nov MPC), we opined that current pace of **tightening and guidance - allowing for rates to go much higher than its peers - can help mitigate against hawkish Fed and provide some support for Kiwi**. A stronger Kiwi can also help to mitigate against imported inflation.

- **Downside Risks to NZD Outlook**: (1) War in Ukraine futher escalates into biochemical/ broaden to involve more countries or last longer may hamper global economic momentum and that will have negative spillover effects on NZ. (2) further slowdown in China growth (hard landing risks), or further weakening in CNH can also weigh on NZD, given its high sensitivity to global growth and China. (3) RBNZ fails to live up to hawkish guidance will be a drag on NZD (unwinding risk); (4) Much faster shifts in Fed's pace of policy tightening will weigh on sentiment and narrow NZD's yield advantage. On net, global growth concerns, inflation worries and fears of tighter monetary conditions may keep risk appetite on a leash.

- **Growth and Inflation Outlook: Recession risks in NZ have risen though we do not expect a technical recession in 2Q as economy gradually normalises** post-omicron wave and the reopening of borders in Apr, May should boost tourism and partially help support growth. That said, Mfg PMI contracted (49.7 vs. 52.6 prior) for the first time in Jun since nationwide lockdown in Aug 2021. All 5 sub-categories fell while new orders slipped below 50-mark. Meanwhile services PMI held up in expansionary territory (55.4 vs. 55.2 prior). Ongoing supply chain disruptions and labor constraints are likely to hold back growth momentum. Taking stock, NZ economy surprisingly contracted 0.2% q/q in 1Q (vs. 0.6% expected vs. 3% in 4Q). Primary industries, including mining, fishing and forestry as well as manufacturing output in F&B, tobacco and machinery led declines. Retail and restaurant spending also fell. The surge in omicron infection back in 1Q dampened economic momentum as multiple sectors including tourism were affected amid border closure and tighter restrictions. In annual terms, 1Q GDP grew 1.2% y/y, down from 3.1% y/y in 4Q.

- **Headline CPI surged to fresh 32-year high of 7.3% in 2Q**, up from 6.9% in 1Q. The main contributor was housing, including the rising prices for construction and rentals while transport was the next biggest contributor to CPI (owing to prices of fuel). This is the 5th quarter in a row that headline CPI breached above RBNZ's 1% - 3 target band. Potentially, we opined that inflation may have peaked but price pressures can continue to stay elevated amid supply chain disruption and tight labor market. RBNZ expects inflation to fall to 4.4% in 2023, 2.5% in 2024 and 2% in 2025.

- **Monetary Policy Forecast:** We expect RBNZ to maintain its pace of raising rate by 50bps to bring OCR to 3% at the next MPC on 17 Aug. Key focus of RBNZ is to ensure that current high CPI (2Q at record 32y high of 7.3%) does not become embedded into longer-term inflation expectations. Markets' implied still see another 2* 50bps hike fully priced for upcoming MPCs for remainder of the year in Aug and Oct (as of 26 Jul). All in, markets are looking for another 138bps hike to bring OCR to ~3.8% by end-year. Peak rate as priced by markets is at 4% in Apr-2023.

- At the last MPC (13 Jul), RBNZ raised OCR 50bps to 2.5%, as widely expected. This is the 3rd back to back 50bps hike and MPC is comfortable with tightening policy "at pace" (i.e. 50bps) until inflation is contained. In terms of projection, RBNZ stuck to its peak cash rate projection of 3.95%. RBNZ highlighted that there is still near term upside risk to CPI and emerging medium term downside risks to economy activity. RBNZ will release new projections for cash rate and economic indicators at its next MPS (17 Aug).

- **External Balance and Fiscal Outlook: NZ current account deficit widened to NZ$8.5bn in 1Q, from NZ$6.6bn in 4Q 2021.** This was due to higher imports, driven by demand for vaccines, antigen test kits and consumption goods while exports was smaller. For the year ended 1Q 2022, current account deficit widened to 6.5% of GDP, from -5.8% of GDP in 4Q.

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

- In the annual budget (19 May), the government **unveiled a package of measures worth NZ$1bn targeted to help low and middle household cope with rising inflation**. 2.1mio people (those earning led than $70k per year) will receive a weekly payout of NZ$27/week for 3 months from 1 Aug while reduction in fuel duties (25c/litre) to offset rising petrol prices will be extended by 2 months, alongside hald-price public transport. Budget deficit is projected to widen to NZ$6.63bn for coming year (vs. NZ$831mio projected in Dec) and is not expected to return to surplus until sometime in 2025. The stimulus measures are targeted instead of broad-based and is temporary, hence is not likely to add to inflation pressures but to help targeted group of people cope with the surge in living costs

- **Key domestic events and issues to watch:** Jun building permits (1 Aug); 2Q labor market report (3 Aug); Jul card spending (9 Aug); Jul mfg PMI, food prices (12 Aug); Jul services PMI (15 Aug); 2Q PPI, RBNZ meeting (17 Aug); Jul trade (19 Aug); 2Q retail sales (25 Aug); Aug consumer confidence (26 Aug); Aug activity outlook, business confidence (31 Aug).
- **Technical Outlook:** Kiwi rose for the month of Jul. Pair was last at 0.6310 levels. Mild bullish momentum on daily chart intact while RSI rose. Risks skewed to the upside for now. Resistance at 0.6320 (50 DMA), 0.6380 and 0.6450 levels. Support at 0.6260, 0.62 (21 DMA) and 0.6180 levels.

CAD: Time to Ride on USD Correction

Forecast	3Q 2022	4Q 2022	1Q 2023	2Q 2023
USDCAD	1.2700 (1.2500)	1.2600 (1.2400)	1.2500 (1.2400)	1.2500 (1.2300)

Previous Forecasts in Parenthesis

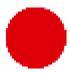
- **Motivation for the FX View:** We tweaked our forecast for CAD a tad lower as the decline in international crude oil prices amid recession fears weakened the currency more than expected. Nonetheless, CAD has remained one of the most resilient currencies in the face of USD strength. Even after a 100bps hike, BoC remained hawkish but we see limited room for the central bank to hike aggressively given that the overnight rate is already within the estimated neutral range. A slowdown in the pace of tightening could mean less support for the CAD going forward. In addition, global growth slowdown could reduce its exports receipts and narrow its trade surplus. The silver lining is that we could be in for a short period of corrective decline for the USD. We are thus still likely to see a similar move lower in the USDCAD towards the 1.27-figure by the end of 3Q.
- **Growth and Inflation Outlook:** Canada continues to experience **tight labour market conditions**. Jobless rate fell to 4.9% from previous 5.1% even as the nation recorded a net drop of 43.2K of employment for Jun. Hourly wage rate picked up pace more than expected to 5.6%y/y from previous 4.5%, underscoring signs of an overheating economy.
- Retail sales for May picked up pace to 2.2%m/m from 0.7% previously and strong growth was seen in motor vehicles & parts dealers at 3.8%m/m. Ex-auto, retail sales quickened to 1.9%m/m from previous 1.1%. Furniture & home furnishings declined at a slower pace by -0.4%m/m vs. previous -0.9%. Food & Beverage picked up pace to +1.9%m/m vs. previous -0.5%. While household spending seems to be

strong in May, the Bloomberg Nanos consumer confidence index suggest spending might have deteriorated significantly into 2H due to the negative wealth effect from the correction in property prices and inflation eating into disposable income.

- CPI accelerated to 8.1%y/y in Jun from previous 7.7%. Month-on-month, CPI softened to 0.7%m/m from previous 1.4%. Food inflation softened to 0.1%m/m from previous 0.8% while shelter has also slowed to 0.4%m/m from previous 0.7%. Transportation eased to 2.3%m/m from previous 3.5%. Month-on-month breakdowns suggest that price pressure might have eased somewhat in Jun after BoC raised the overnight lending rate by 125bps (before the big Jul hike). More importantly, raw material price index seem to have fallen as well. The industrial product price fell -1.1%m/m in Jun with the breakdown showing price declines for most subcomponents with the exception of crude energy (+.5%m/m). On the whole, this could mean potential for easing price pressure for businesses and concomitantly, consumers.
- **Monetary Policy Forecast:** BoC took overnight rate by a stunning 100bps to 2.50% on 13 Jul, doubling its tightening pace from its 50bps hike on 1Jun. The central bank wanted to frontload the tightening process so as to achieve a soft landing and was concerned that inflation at around 8% risk unanchoring inflation expectations. In addition, the economy is in extreme tight capacity with notable shortages of workers, goods and services. And so, the BoC wants to assure a route of short-term pain (higher cost of living + greater interest rate burden from rate hikes) in exchange for a longer term gain of sustainable price stability.
- BoC noted that the policy rate is now at 2.5%, within the long-run neutral range estimated to be between 2-3%. The aggressive rate hike in Jul to neutral could mean that the pace of tightening at the next meeting should slow and become more data-dependent with the next CPI, wage data releases continue to be scrutinized. The policy trade-offs between inflation and growth would need to be managed more carefully as the central bank moves into a restrictive monetary policy stance. 2Q business outlook based on the survey by BoC eased to 4.9 in the quarter vs. 5.0 in the quarter prior. In addition, the balance of opinion on futures sales optimism also deteriorated further to -26.0 in 2Q from -11.0 –a positive reading of future sales optimism indicates an expected rise in rate of future sales growth. Outlook has soured but the silver lining is that inflation show signs of easing a tad. **Given softening business, consumer sentiment and housing activity, BoC is likely to shift from frontloading-mode to a more calibrated approach with a hike of 50bps in Sep.**
- **Latest External Balance Outlook:** As of last available data, Canada's current account balance was at a surplus of C$4.6 for 1Q22, widening from the previous U$0.8bn surplus. Firm commodity prices continue to bode well for the external balance of net-energy exporters such as Canada.
- In terms of the fiscal, recall that deficit for FY2021/22 came in at C$114bn , better than projected C$145bn seen in Dec. Finance Minister Chrystia Freeland's budget delivered on 8 Apr was mostly focused on fiscal consolidation and prudence. She gave a projection of $31mn in net new spending over the next five years that pales in comparison to allocations in previous budgets. The budget was focused on innovation

and productivity Canada Growth Fund which is a $15bn investment vehicle to incentivize businesses to embrace change and adapt to changing usiness landscape. Looking into the medium term, fiscal deficit is projected to narrow to C$8.4bn by 2026. Debt to GDP ratio to fall to 41.5% by 2026 from 46.5% this year.

- **Key domestic events and issues to watch:** Jul Mfg PMI (4 Aug); Jul labour report (5 Aug); Jun Mfg Sales (15 Aug); Jul housing starts, Jul CPI (16 Aug); raw materials price index (18 Aug); Jun retail sales (19 Aug); Aug CFIB business barometer (25 Aug); 2Q current account (30 Aug); Jun GDP (31 Aug).
- **Technical Analysis:** USDCAD slipped to levels around 1.2790, finding some support thereabouts (61.8% Fibonacci retracement of the Jun-Jul rally). Bearish momentum is still in place with support seen around 1.2720. Resistance at 1.2930 (21-dma).



JPY: More Manageable UST Yields Could Cap USDJPY

Forecast	3Q 2022	4Q 2022	1Q 2023	2Q 2023
USDJPY	**135** (137)	**132** (--)	**128** (--)	**125** (--)

Previous Forecasts in Parentheses

- **Motivation for the FX View:** USDJPY saw more two-way swings in Jul after Mar-Jun rally, given some retracement in dollar strength and net decline in treasury yields, as US recession risks came to the fore. While lack of hawkish tilt from BoJ and still-wide Fed-BoJ policy divergence could still lead USDJPY to trade in elevated ranges near-term, earlier upswing in the USDJPY pair has notably stalled. We note that part of the reason for JPY's earlier underperformance was due to diminishing haven asset appeal, given hit to current account balances, on slow tourism recovery and elevated energy import burden. Recent softening in oil prices on global growth fears could help ease drags on this front. On net, we maintain that **clearer signs of potential Fed dovish pivot (into 2023) could lead USDJPY to continue its retracement lower**, especially if a broadening of price pressures in Japan over the next few quarters also leads BoJ to reconsider its ultra-accommodative stance. But the ongoing late-Jul downswing in the pair (from peak of 139.39 to below 133 last seen) had occurred at a significantly faster pace than we expected. USDJPY shorts were likely exacerbated by Powell comments, weaker-than-expected US GDP, as well as momentum-based selling. It is unclear at this stage if markets are too optimistic on the extent of expected Fed dovish tilt. Combating inflation should still take priority in the interim. **We adjust our 3Q forecast modestly lower and acknowledge downside risks near-term for the pair.**
- **Fed stance and UST-JGB yield differentials are likely to remain as key drivers of the USDJPY pair.** 2Y UST-JGB yield differentials remain

wide at around +295bps at last seen, albeit having moderated from high near +348bps in mid-Jun. Going forward, front-loading of Fed rate hikes could keep UST yields (and USDJPY) supported on dips, even as chances of yields retesting interim highs in mid-Jun could be relatively low for now, with some corners of the markets betting that Fed might have to tilt dovish next year as growth risks escalate. In particular, markets likely gave some weight to Powell's comments on potentially slowing pace of Fed hikes "at some point" at the Jul FoMC. Recent US activity and jobs data are already showing tentative signs of softening. OIS-implied currently looks for Fed policy rate to peak at around 3.3% in Dec 2022 (versus market expectations of a higher peak near 3.9% just 6 weeks ago). On net, **calmer UST yields could dampen upward pressures on USDJPY pair.**

- Still, ongoing normalization in US interest rates, while the BoJ remains committed to an easing stance, could help sustain relative demand for overseas investments (e.g., US treasuries). Demand from pension funds such as GPIF as well as private sector entities could be in play. **Such outflows could offset the support that JPY conventionally receives from an expected current account surplus**—consensus estimates see current account coming in at 1.7% of GDP in 2022 (versus 2.8% in 2021). **This could mean that USDJPY could remain in elevated ranges for some time versus pre-Covid range of 105 to 115, even as risk could be skewed to the downside for the pair (versus current spot levels) into 2023.**

- Admittedly, over the course of the last few months, Japan's energy importer status also likely meant drags on JPY on hit to current account balances amid elevated commodity prices. But there are tentative signs that this burden could be easing, albeit modestly. Brent has declined from US$124/bbl in early Jun to US$107 at last seen, a ~14% drop. While some support (on dips) could emerge on supply-side concerns, upside risks should be more manageable on (i) mounting concerns over softening global aggregate demand as financial conditions tighten, (ii) signs of interest in Russian oil from parts of Asia, including China, India, (iii) planned ramp-ups in OPEC+ supplies over time. Admittedly, inpact of (iii) could be more modest near-term. Market chatters are that UAE and Saudi Arabia are already pumping almost as much oil as they can. Latest data also show OPEC+ members producing 2.8mn b/d below their collective target. On net, o**il price shifts could act as an amplifier for USDJPY moves—elevated oil import burdens could be supportive of USDJPY near-term, while easing in oil import burden into 2023 could help nudge USDJPY lower then.**

- On politics, we note that in the Jul upper house elections, LDP and its junior coalition partner Komeito won 76 seats, above the 56 needed to retain majority and the 69 needed to increase their size in the body. **Markets could have taken the results to reflect resilient public support for recent government policies, including ultra-accommodative central bank stances**. This could help moderate the extent of domestic pressures on BoJ to tilt hawkish, and any such move will likely be data-dependent; i.e., requiring more sustained demand-side price pressures, improving growth momentum.

- **Growth and Inflation Outlook:** 1Q (F) GDP came in at -0.5%q/q SAAR, contracting on a sequential basis versus +4.0% prior, but still slightly better versus expected -1.1%. Private consumption growth was largely flat (+0.1%) on a sequential basis, while business spending contracted by -0.7%q/q, worse than expected +0.3%.

- Tankan surveys for 2Q suggest some improvement in outlook among manufacturers and non-manufacturers, albeit more modest than expected. Labor cash earnings for May grew by 1.0%y/y, versus expectations for 1.5%. Softer-than-expected labor cash earnings for May highlights challenges in inducing sustainable wage gains domestically in Japan.

- Japan CPI for Jun came in at 2.4%y/y, on par with expectations and slightly lower versus 2.5% prior. The reading ex fresh food came in at 2.2%y/y, also as expected. Base effects, a weaker JPY and ongoing supply disruptions may still mean an elevated headline CPI higher in the coming months (2% or higher), but BoJ views these developments as transitory. BoJ thinks that the current cost-push inflation cannot be sustained as the impact of energy prices could eventually ease, while wages have yet to rise sustainably.

- **Monetary Policy Forecast:** BoJ stood pat on policy settings (policy rate at -0.1%) on 21 Jul. The YCC will be maintained at current settings (0% target yield for 10Y with 25bps cap). There was arguably less of an impetus for an immediate move given that domestic prices have yet to see runaway momentum. New macro forecasts from BoJ in Jul indicate some caution in growth (FY2022 growth projection at 2.4% vs. 2.9% prior), but a tad more near-term inflation risks (CPI all items less fresh food for FY2022 forecast at 2.3% vs. 1.9% prior). Notably though, core inflation is expected to come in at around 1.4% in FY2023, still modestly lower versus the 2% target; i.e., price pressures are still not entrenched yet. **While BoJ noted risks from rapid JPY depreciation, Kuroda's comments in the QA session remained largely dovish**. There also appears to be no plans to review the YCC framework for now.

- **Meanwhile, even as Kuroda quashed hopes for near-term policy changes, chatters of potential tweaks will likely continue into 2H and 2023, especially if inflation pressures broaden more sustainably**. There are very tentative signs that this could be occurring. Looking at Jun price data, the trimmed mean (a measure of price growth that factors out biggest gains and falls), rose 1.6%y/y, fastest since 2001. The weighted mean (gives more importance to key items), also reached new records. Meanwhile, the share of components in the consumer price basket seeing price increases also rose to 71.3%, the highest proportion on record. A pick-up in the intensity and pace of such developments could gradually lead BoJ to reconsider their policy stance.

- On possibility of FX intervention, we note that officials from the BoJ, the Ministry of Finance and the Financial Services Agency met in mid-Jun after the JPY saw a bout of softening, and in a joint statement, expressed their concern about the sudden weakening of the JPY, saying they will take action if necessary. **Risks on direct intervention by authorities might be higher now, and could help keep USDJPY resist**

upswings towards the psychological threshold of 140, even as the threshold for intervention might be high.

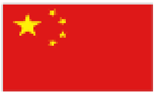
- **Latest Fiscal & External Balance Outlook:** In Feb 2022, **a parliamentary committee approved a record JPY107.6trn (US$936bn) spending plan for FY2022 (starting Apr).** Kishida has vowed seamless spending for 16 months (beginning with supplementary budget mentioned above) to provide sufficient support to lift the economy from Covid-induced doldrums. Consensus forecasts see the fiscal deficit coming in at around -6.7% of GDP in 2022, slightly wider versus the -6.4% seen in 2021, and significantly wider than the -3.2% average seen in 2015-2019 (pre-Covid).

- **To counter the impact of rising energy costs on the domestic economy, PM Kishida is rolling out a combined JPY6.2trn emergency economic package.** The key features of the package include cash handouts of JPY50k per child for low-income households, more subsidies for oil wholesalers to reduce retail gasoline costs, and support for SMEs and livestock farmers. The package aims to prevent rising raw material costs from adding to supply-chain bottlenecks as the domestic economy attempt to recover from Covid drags. To finance the new spending, the government will tap JPY1.5trn from reserve funds allocated for emergency spending in the current FY beginning Apr, around JPY2trn secured in the FY2022 budget and other sources, as well as JPY2.7trn from an extra budget to be compiled later.

- Current account surplus for May narrowed significantly to JPY128bn versus JPY501bn prior, adding to dampened sentiments for JPY. Pre-Covid average in 2019 was JPY1600bn. On a more positive note, trade deficit for Jun narrowed to -JPY1384bn, versus -JPY2386bn prior, as lockdown conditions in China eased. Still, the trade balance has seen deficit readings from Aug 2021 to Jun 2022, versus average surplus outturns in the first 7 months of 2021. **Such developments could remain as interim drags on JPY.**

- **Key domestic events and issues to watch:** Jul Vehicle sales (1 Aug); Jun Labor cash earnings (5 Aug); Jun (P) Leading Index CI (5 Aug); Jun Current account (8 Aug); Jul (P) Machine tool orders (9 Aug); Jul PPI (10 Aug); 2Q (P) GDP (15 Aug); Jun Tertiary industry index (16 Aug); Jul Core machine orders (17 Aug); Jul Trade (17 Aug); Jul CPI (19 Aug); Aug (P) Jibun Bank PMIs (23 Aug); Jul Jobless rate (30 Aug); Jul Retail sales (31 Aug); Jul (P) Industrial production (31 Aug).

- **Technical Outlook:** USDJPY pair was last seen near the 133-handle. On weekly chart, RSI is exiting from overbought territory, while bullish momentum in pair has largely moderated. Meanwhile on daily chart, momentum and RSI are modestly bearish. Risks of large upward retracements could be reduced. Pair is unlikely to test peak of 139.40. Resistance at 134.50 (38.2% fibo retracement of May low to Jul high), 136.35 (23.6% fibo), before 139.40 (Jul high). Support at 131.45 (61.8% fibo), 133.00 (38.2% fibo), 129.50 (76.4% fibo).



RMB: Benign USD Environment Masks Underlying Drags

Forecast	3Q 2022	4Q 2022	1Q 2023	2Q 2023
USDCNY	6.75 (--)	6.70 (--)	6.68 (--)	6.65 (--)
USDCNH	6.75 (--)	6.70 (--)	6.68 (--)	6.65 (--)

No Change to Previous Forecasts.

- **Motivation for the FX View:** USDCNH remained within the 6.60-6.80 range that we have pencilled in many weeks ago. Market indicators (forward points, narrow USDCNH-USDCNY premium) also show signs of stability for the USDCNH and USDCNY. However, we reckon this has to do more with the broader USD direction and the pullback in UST yields rather than macro improvements at home.

- While we can continue to look for further consolidation within the established range against the USD, we see too many risk factors for us to turn aggressively bullish on the yuan at this point including Covid uncertainties (Shanghai's mass testing in 9 out of 16 districts for the next few days), a lack of decisive changes in zero-Covid strategy that could weigh on recovery prospects as well as the potential for an escalation of geopolitical tensions with the US should US House Speaker Nancy Pelosi make a trip to Taiwan in August. China has reportedly warned of a "military response". **We thus remain cautious on the yuan, looking for 6.60-6.80 range to hold but further underperformance vs. regional peers such as the SGD.**

- **Growth and Inflation Outlook:** Just base on PMI numbers alone, China seems to be outperforming, bucking the trend of growth deterioration that is seen for both services and manufacturing sector across the world. However, beyond the initial optimism owed to the resumption of supply-chain and order fulfillment after pandemic-related restrictions were lifted, such improvement in production and business conditions may remain threatened by the risk of either future lockdowns or weakening external demand. In addition, cautious hiring sentiment underscores a lack of confidence in the business climate and conditions.

- **Key to China's outlook is how the officials stem a potential downward spiral of its property sector.** Early in Jun, news of mortgage owners' refusing to make mortgage payments for projects that face prolonged construction delays broke and raise concerns of a systemic banking risks. The government has since mentioned the potential for grace periods for mortgage owners to halt payments for projects that face delays without incurring penalties, thus allowing some breather for banks' NPL and the concomitant potential need for provisions that could lead to further systemic strains to the financial system. That said, the protest had only amplified the vulnerability of the property market and there were even news of some suppliers to developers (such as Evergrande) refusing to make bank loan repayments as the developers have not paid up on their bills owed to them, a sign of widening boycott.

China State Council is reported to have setup a fund (CNY50bn from China Construction Bank) and a CNY30bn relending facility from PBoC to support 12 developers + newer distressed real estate firms, a likely attempt by the government boost confidence.

- Jun activity suggests that China has bottomed out from the impact of its Shanghai-lockdown with industrial production up 3.9%y/y vs. previous 0.7%. Breakdown of the industrial production report suggests that output has accelerated across the sectors including mining (+8.7%y/y vs. previous +7.0%), manufacturing (+3.4%y/y vs. previous +0.1%) and electricity, gas and water supply (+3.3%y/y vs. previous 0.2%). More recently, there are reports of a halt in the increase of subway usage and oil refinery volumes which could mean some moderation in production and retail sales momentum for Jul.
- The directive from the top seems to be aimed at infrastructure spending for the second half of the year and potential tweaks to the covid management policies. China Development Bank has set up a fund to invest CNY1.3bn in the construction of a highway in Shanxi and an airport in Henan province. Separately, the Agricultural Development Bank of China also set up a fund to invest CNY500mn in the construction of a hydro-power station in Chongqing. In total, infrastructure spending (raised from financial bonds issuance, local government special bonds, land sales and other sources) of around CNY7.2trn would be the main thrust for the economy in the face of the property malaise and Covid uncertainties.
- We still see a need for a more decisive shift in the dynamic zero-Covid strategy in order for businesses and consumers to sustainably regain confidence. That would in turn provide boost to most sectors of the economy, including the property sales.
- **Monetary Policy Forecast**: We look for 5Y LPRs to be adjusted by another 10bps lower by Chinese banks. The RRR to be lowered another 50bps within the next two quarters. **Given that demand has started to pick up and US treasury yields seem to be nearing a peak by recession fears, PBoC might feel more comfortable with easing monetary policy further at this point.** We anticipate RRR cuts and MLF cut in 2H to potentially weigh on the yuan but its combination with fiscal sepnding could mean that the current easing cycle is likely to be shallow and thus, depreciation pressure on the yuan should be easily offset by growth optimism. PBoC Yi Gang pledged to keep monetary policy accommodative whilst noting that the "current level of real interest rates are quite low already".
- **Latest Fiscal and External Balance Outlook:** Fiscal target for 2022 was projected to be 2.8% of GDP, down from 3.2%, underscoring a stance of fiscal consolidation but that is increasingly unlikely as we look for further fiscal spending to support the economy. Recently, China Center for international Economic Exchanges Vice Chair Wang Yiming said that the fiscal deficit-to-GDP ratio could be raised to support domestic demand.
- **Key domestic events and issues to watch:** Jul Caixin Mfg PMI (1 Aug), Jul Caixin composite and services PMI (3 Aug); 2Q current account balance (2Q P); Jul trade data (7 Aug); Aggregate financing (9-15 Aug); Jul CPI and PPI (10 Aug); 1Y MLF (13-16 Aug); New home prices,

industrial production, retail sales, FAI ex rural and property investment (15 Aug); FX Net settlement (19 Aug); 1Y, 5Y LPR (27 Aug); Aug Official Mfg, non-mfg, composite PMI.

- **Technical Analysis:** USDCNH hovered around 6.75 on the last working day of Jul. We are wary of the bullish pennant formed after considerable consolidation within the 6.60-6.80 range. Momentum indicators do not show much directional bias at this point but a bullish pennant could augur a move above the 7.00-figure

KRW: Looking for a Technical Turn

Forecast	3Q 2022	4Q 2022	1Q 2023	2Q 2023
USDKRW	**1280** (1260)	**1260** (1240)	**1240** (1220)	**1230** (1210)

Previous Forecasts in Parentheses

- **Motivations for the FX View:** We expect KRW to remain under pressure amid global growth concerns, tighter financial conditions and recent surge in covid infection in Korea that may pose risks to activity momentum. But we continue to flag out the potential for KRW losses to moderate or partially recover especially from stretched levels. Easing UST yields, softer oil prices, BoK still embaring on rate hike cycle, rebound in tech shares (+3.5% QTD), return of foreign inflow (1st QTD positive net foreign inflow this year), Asia reopening story, potential peak in Fed hawkishness and USD strength are some factors that could support the intermittent bounces in KRW. Elsewhere we also keep a look out on US review of China tariffs. Potential removal of US tariffs on Chinese imports can be perceived as modestly positive for broad risk sentiment and is supportive of KRW. Nonetheless, a more meaningful recovery in KRW will however require a better assessment of global growth, sharper pullback in UST yields and China's zero-covid policy to end (can boost tourism, sentiment and help with growth stabilisation in China - spillover effect to broader Asia).

- **Technically a Potential Turn in USDKRW Should Not be Ruled Out.** We note that past periods of sharp USDKRW run-up in 2014-16, 2018-20 saw KRW depreciate by around 22% vs. USD on average. The current run-up since late-2020 is similarly seeing ~22% depreciation in KRW (vs. USD). We opined that the current sell-off in KRW could potentially be near a turning point. Taking other technical signals in consideration, the bearish divergence in MACD and RSI may add to further signals that pace of decline in KRW may moderate and a USDKRW interim top may be near.

- **Global Growth Downgrades a Drag on High-Beta/Pro-Cyclical KRW.** World Bank earlier projected global growth to slump to 2.9% in 2022, from 5.7% in 2021. This is also significantly lower than its Jan's projection for growth at 4.1%. The downward revision was due to war in Ukraine disrupting activity, investment and trade while pent-up demand fades and fiscal, monetary accomdation is withdrawn. World Bank warned that even if a global recession is averted, the pain of stagflation could persist for several years. The OECD also projected global growth to decelerate sharply to around 3% for 2022 and 2.8% in 2023. OECD cited Russian war, covid pandemic – more aggressive or contagious variants may emerge as well as China's zero covid policy disrupting supply chain. At the same time, OECD doubled its inflation outlook to nearly 9% for its 38 member states.

- **Risks to outlook include** (1) a much faster pace of Fed tightening beyond Sep meeting; (2) covid deterioration leading to fresh lockdowns, delayed reopenings; (3) another round of sharp increases in oil prices as KRW is highly sensitive to market moves and is a net oil importer; (4) potential deterioration in China-Korea relations. We reiterate that Yoon as a President may undermine KRW due to his foreign policy bias that leans towards resetting China ties. He had indicated plans to buy an additional Terminal High Altitude Area Defense (THAAD) anti-missile system. This may be a concern for KRW and markets as this risks retaliation from China. Recall that China-Korea relations deteriorated in 3Q 2016 over US-Korea alliance decision to deploy a US THAAD to defend against North Korea missile threat. In response, Beijing then used economic coercion, among other levers, to try to force Seoul to abandon the THAAD deployment.

- **Growth and Inflation Outlook: Economic growth unexpectedly accelerates to 0.7% q/q in 2Q (vs. 0.6% in 1Q).** Strong private consumption (+3%) as well as a bump up in government spending offset dismay exports (-3.1%) and ongoing decline (4th consecutive quarters) in corporate spending (-1%). These can be attributed to slowing Chinese economy (affecting external demand), supply chain disruption owing to war in Ukraine and tighter financial conditions globally. In annual terms, 2Q GDP was at 2.9% y/y vs. 2.6% expected. South Korea government lowered its 2022 growth projection to 2.6%, from 3.1% previously. This is lower than BoK's projection for growth in 2022 and 2023 to come in at 2.7% and 2.4%, respectively. BoK expects investments and export growth to slow while private consumption should pick up amid relaxation in covid restrictions. Looking on, the forward looking surveys and activity indicators suggest that underlying growth, activity momentum is somewhat mixed. Mfg PMI slipped to 51.3 in Jun vs. 51.8 in May while 1st 20days of exports posted a sharp rebound of 14.5% vs. -3.4% prior.

- **Korea CPI surged to 24-year high of 6% y/y in Jun,** up from 5.4% y/y in May. Prices at hotels and restaurants jumped the most while F&B, household goods & services as well as utility costs also saw large price increases. This is also the 15th consecutive month of CPI staying above BoK's 2% target and the fastest pace since 1998. Core CPI accelerated to 4.4% y/y in Jun, up from 4.1% y/y in May. BoK now expects headline CPI to stay at 6% for some time. Finance Ministry looks for inflation to rise to 4.7% in 2022. Looking forward, ITS Minimum Wage Commission had agreed to raise minimum hourly wage by 5% in 2023. This may further add to inflationary expectations and support the case for more aggressive monetary policy.

- **Monetary Policy Forecast**: We expect BoK to keep pace with another 50bps hike to bring policy rate to 2.75% at the upcoming MPC on 25 Aug. BoK Governor Rhee indicated that the BoK is prioritizing the combat against inflation before it gets worse while the recent upside surprise to 2Q GDP supports the case for further tightening. Governor Rhee had earlier indicated that the pace of hike may still vary and gradual 25bps hike remains "desirable" going forward and is reasonable for markets to see rates at 2.75% - 3% by year end. He also shared that policy rate is likely at lower end of neutral rate and that another 1 or 2 hikes wouldn't be tightening. We also opined the large magnitude of hike is to keep pace with Fed such that yield spread is maintained to mitigate against capital outflows.

- At the last BoK meeting (13 Jul), the MPC raised rate by an unprecedented pace of 50bps to bring policy rate to 2.25%. The decision was unanimous. BoK said it needs to continue rate hike trend as inflation will be above target for considerable time. The MPS also said that pace and size of rate hike is dependent on inflation, growth, financial imbalance, major countries' policy changes and geopolitical risks. BOK expects CPI to stay above 6% for some time while growth to be slightly below projection in May. But stagflation is not on Governor Rhee's minds. On net, fighting inflation (so long it remains above 6%) still takes priority at BoK.

- **External Balance and Fiscal Outlook:** Current account turned surplus in May with +$3.86bn, following a deficit of $80mio in Apr. But May surplus fell from year ago as imports rose more than exports. Higher import bill was due to higher raw material prices.

- Korea's national debt rose at a rapid pace and fiscal deficit widened. The national debt is forecast to reach KRW1,075.7tn this year, marking the first time that the debt would exceed the 1,000 trillion-won mark. Debt-to-GDP ratio is also expected to rise to a record high of 50.1 percent this year and the fiscal deficit is likely to reach 70.8 trillion won, equivalent to 3.3 percent of the GDP.

- On 29 May, South Korea approved a record extra budget worth KRW62tn (or US$49.5bn), in attempt to offset the impacts of Covid-19 and rising cost of living. Budget measures include some subsidies for people vulnerable to faster gains in prices. Targeted groups are mainly owners of small and medium size businesses (estimate to be around 5.5mio owners). Budget will not be funded by any bond issuance but tax revenues from existing spending plans.

- **Key domestic data to watch:** S. Korea releases Jul trade, mfg PMI (1 Aug), Jul CPI (2 Aug); FX reserves (3 Aug); Jun current account (5 Aug); Jul unemployment rate (10 Aug); 1st 20 days of exports (22 Aug); Aug consumer confidence (23 Aug); Aug Business survey – mfg and services (24 Aug); Jul PPI, BoK MPC (25 Aug); Jul IP (31 Aug).

- **Technical Outlook:** USDKRW was broadly firmer for the month of Jul though there are signs of the pair coming off. Last at 1301 levels. Daily momentum is mild bearish while RSI is falling. Risks to the downside.

Support at 1292 and 1285 levels (50 DMA). Resistance at 1306 (21 DMA), and 1320 levels.

TWD: Weakness Lingers but A Reversal Is Likely

Forecast	3Q 2022	4Q 2022	1Q 2023	2Q 2023
USDTWD	**30.00** (--)	**29.80** (--)	**29.60** (--)	**29.50** (--)

No Change to Previous Forecasts

- **Motivations for the FX View: Our long-standing contrarian call (first shared in Annual outlook) for TWD to underperform in 2022 has so far panned out.** Looking on, we still expect TWD softness to linger in the face of (1) slowing global growth with recession risks on the rise; (2) ongoing Fed-CBC policy divergence can undermine TWD in the interim; (3) still-elevated energy prices undermine energy importers like TW while rising prices hurt household consumption pattern; (4) risk of worsening China-Taiwan relations that may affect investment inflows, in particular the potential repercussion in the event Pelosi decides to pay a visit to Taiwan; (5) housing market and equity market softness. But we believe the >9% sell-off in TWD (peak-to-trough) YTD may start to moderate. The 25% sell-off in TWSE (peak-to-trough) could also potentially present attractive re-entry points for investors, from a valuation standpoint. Potential foreign inflows can support TWD. The global demand for technology is also intact and Taiwan has its competitive advantage to benefit from the trend. Tentative signs of green shoots was also observed in the sustained uptick in export orders. We look for USDTWD to peak in 3Q before easing slightly into year-end. A potential peak in Fed hawkishness, USD strength and UST yields coming off, alongside faster Asia reopening should also lend support to the view.

- **Geopolitical Risks Undermine Sentiments.** In response to a rumored visit to Taiwan by US house speaker Nancy Pelosi, China has warned of "serious consequences" if Pelosi proceeds with her visit. Chinese Defence Ministry said that PLA will not turn a blind eye to her visit, which it perceives as a move to support Taiwan independence. China went to threaten about deploying diplomatic, economic and even military means to stop her landing on Taiwan. We had cautioned as early as last year that in a US-China virtual summit in Nov-2021, *China President Xi told Biden that any support for Taiwanese independence would be "like playing with fire" and "those who play with fire will get burnt". While tensions were typically more bark than bite, we are slightly cautious this time round as tensions were* intensifying and can affect businesses, investments. Via the sentiment channel, worsening tensions is a source of volatility for TWD.

- **CBC May Still Go Slow With Policy Normalisation.** Four rounds of selective credit controls measures imposed by CBC since Dec-2020 as well as policy rate hikes this year have undermined housing transaction and home mortgage growth. Taiwan's housing market can be sensitive to interest rates and we believe CBC does not want to cause a housing market meltdown with its aggressive rate hike cycle even though it wants to combat inflation. Apart from credit control measures previously imposed to target house prices, CBC's cumulative hikes of 37.5bps in 1H may already have dampened housing market sentiments, alongside covid-19 spread. To some extent, we expect CBC to continue monitoring housing market while still keeping its rate hike cycle alive with a step-down in pace of hike.
  - Housing transactions in Taiwan are already showing signs of moderation. 6 largest cities, including Taipei, New Taipei, Taoyuan, Taichung, Kaohsiung and Tainan reported 7.7% y/y drop in transaction volume in May. In the 5 months to May-2022, housing transactions in the 6 cities only rose 0.7% from a year earlier.

- **Potentially Looking Attractive.** Taiwan stock benchmark index (TWSE) posted a 7% rebound in Jul (trough-to-peak) after seeing its worst performance (down by nearly 25%) in the half-year to date (30 Jun) in the last 20 years. This was mainly due to external risks including global recession concerns, inflation worries and tighter monetary policies. To some extent, we believe that our long-standing caution (first shared in 2022 annual outlook) for the worsening of China-TW relations may also have played a part in affecting investment inflows. YTD, foreigners net sold >$35bn of local equities amid unwinding of tech holdings. The massive sell-off this year saw PE ratio for TWSE crumbling to about 10x (as of late Jul-2022). On an average basis over 22years, TWSE PE is about 23x while the 5y average stands at 16.8x. From a valuation standpoint, re-entry levels for TWSE may seem attractive for investors, especially when tech fundamentals remain intact.
  - Tech Fundamentals Intact and Taiwan Has Competitive Advantage. IDC projected worldwide semiconductor revenue to rise by 13.7% y/y to reach $661bn in 2022, after a bumper record in 2021. Resilience is seen in cloud, network infrastructure and automotive markets. There were challenges for most of this year amid supply-demand disruptions caused by unexpected war in Ukraine and covid shutdowns in China. But some of these disruptions may start to fade especially with the reopening of more economies including China from covid lockdowns. Global semiconductor demand will also increasingly shift towards high performance ones. TSMC has confirmed in its Technology Symposium (Jun-2022) that 3nm (N3) chips will be introduced in 2H this year while 2nm (N2) will come sometime in 2025. New technologies will be used to make advanced CPUs, GPUs and SoCs. Apple, Intel are some of the companies that demand N3 chips. TSMC, amongst other Taiwanese foundries have the competitive edge and should continue to build on increasing its global market share. TrendForce forecast Taiwanese foundries will increase in size by 19.8% in 2022. The data company also project Taiwanese share of global market to

increase to 66% in 2022, up from 64% in 2021. As global demand dynamics continue and supply constraints start to ease, we should expect renewed interest in Taiwanese assets.

- **Growth and Inflation Outlook: Activity momentum continues to show signs of slowdown** in recent months amid covid spread in Taiwan. Mfg PMI slipped into contractionary territory of 49.8 in May, from 50 in Apr while industrial production rose at a slower pace of 0.73% y/y in Jun, down from 4.48% y/y in May. That said, export orders continued to surprise to the upside +9.5% y/y in Jun, up from 6% y/y in May. The rebound was led by telecommunication products and electronics. **2Q GDP out on 29 Jul.** Taking stock, 1Q GDP was revised slightly higher to 3.14% y/y (vs. prelim print of 3.06% earlier). But this is still a slowdown from its fastest pace (in over a decade) of 4.88% in 4Q. The slowdown was due to domestic demand and government spending. Covid outbreak in TW, resulting in extended lockdowns as well as multiple occasions of blackout and water shortages proved challenging for growth momentum. That said, headline growth still surpassed expectations, owing to robust exports. DGBAS said that demand for new technology applications and cargo shipping services remained vibrant amid easing supply chain bottlenecks. DGBAS had earlier lowered 2022 growth forecast to 3.91%, from 4.42% previously. The agency cited global inflation and covid dampening domestic and external demand as main factors for the bearish adjustment even as export growth forecast was revised higher to 14.62% this year, from 9.69% prior.

- **Headline CPI rose to 14y high of 3.59% y/y in Jun**, up from 3.39% y/y in May. This is the 11th consecutive month that CPI comes in above 2%-target. Food (led by eggs, fruits, vegetables), restaurant, rental, electricity and fuel remain the main drivers of higher inflation. Core inflation also rose 2.7% y/y in Jun, up from 2.6% y/y in May. Ongoing military conflict in Ukraine continues to complicate supply chain disruptions, keep commodity prices supported and that is expected to feed through to higher CPI in coming months. DGBAS revised 2022 CPI forecast higher to 2.67%, driven by rising import costs. Agency expects CPI to moderate from middle of this year though it also cautioned that uncertainty remain in place.

- **Monetary Policy Forecast: We expect CBC to continue with its rate hike cycle to raise rates by 12.5bps again at the upcoming MPC on 22 Sep.** We opined that CBC policymakers may opt to preserve monetary ammunition (i.e. not raising rate by larger magnitude of 25bps) as some sectors of the economy (i.e. tourism, self-employed, real estate etc.) still require support as covid/ border restrictions remain - a constraint on domestic demand, tourism sectors. Taiwan's housing market can be sensitive to interest rates and we believe CBC does not want to cause a housing market meltdown with its aggressive rate hike cycle even though it wants to combat inflation. So far this year, CBC's cumulative hikes of 37.5bps may already have dampened housing market sentiments, alongside covid spread. To some extent, we expect CBC to continue monitoring housing market while still keeping its rate hike cycle alive with a step-down pace of hike.

- At the last MPC (15 Jun), CBC raised rate for a second consecutive time this year but pace of hike reverted to +12.5bps, as we expected.

Benchmark interest rate was raised to 1.50%. CBC also raised RRR on NT$ demand deposits and time deposits by 0.25ppts each, effective 1 Jul. The interest on refinancing of secured loans and temporary accommodation are also raised to 1.875% and 3.75%, respectively. The Board judged that raising both the policy rates and RRR would send a clear message that CBC continues to adopt a monetary policy stance of tightening. Governor Yang estimated that 25bps hike in RRR translate to withdrawing NT$120bn from the system.

- **External and Fiscal Outlook: Current account surplus widened to $30.68bn in 1Q 2022,** from $25.83bn in 1Q 2021. Both goods and services surplus expanded. Trade was driven by demand for electronics used in digital transformation and emerging technology applications while services was due to rise in income by cargo shipping providers amid tight supply of containers. Current account surplus expanded to 15.2% of GDP in 1Q (vs. 14.95% of GDP in 4Q). Taiwan's debt as % of GDP last stood at 35.2 while fiscal surplus was at 0.37% of GDP. Taiwan has a self-mandated cap of 40% of debt to GDP.

- Earlier, S&P upgraded Taiwan's credit rating to AA+, up from AA. S&P attributed the upgrade to TW's fiscal management – flexible and well-executed and that its strong economic performance alleviated the need for large-scale financial support measures. Budget deficit is expected to have peaked at 3.6% of GDP in 2021 and fall to 1.5% of GDP in 2022, with gradual decline thereafter. It also pointed out that the economy has benefited from strong global demand for semiconductor chips. It also mentioned that tension across Taiwan Strait should not affect TW's manufacturing sector. Seperately TW's MOF said it will actively reduce the tax burden on commodity and implement relief and revitalisation measures to facilitate TW's economic stability and resiliency.

- **Key domestic events and issues to watch:** Jul mfg PMI (1 Aug); Jul CPI, FX reserves (5 Aug); Jul trade (8 Aug); 2Q current account (19 Aug); Jul export orders (22 Aug); Jul unemployment (22 Aug); Jul industrial production (23 Aug); 2Q prelim GDP (31 Aug).

- **Technical Outlook:** USDTWD drifted a touch higher in Jul. Pair was last at 29.95 levels. Bullish momentum on daily monthly chart intact though RSI shows signs of turning from near overbought conditions. Bias to lean against strength. Resistance at 30, 30.1 levels. Support at 29.85 (21 DMA), 29.70 (50 DMA) and 29.40 levels (100 DMA).

SGD: Off-Cycle Boosts SGD NEER; Relative Appeal Versus Peers Intact

Forecast	3Q 2022	4Q 2022	1Q 2023	1Q 2023
USDSGD	1.3700 (--)	1.3600 (--)	1.3500 (--)	1.3400 (--)

No Change to Previous Forecasts

- **Motivation for the FX View:** SG is seeing a new wave of Covid cases, with 7-day average >8k at late Jul versus interim trough near 2k in end-Apr, but impact on sentiments remains modest. Market focus remains largely on external risks (i.e., Fed, China growth, supply chain disruptions) for now. Developments imply continued mirroring of broader dollar biases near-term for the USDSGD pair. We note some softening in broad dollar lately, as markets price in a potential dovish tilt by Fed into 2023, on incremental growth risks. Concomitant backing off in UST yields from recent highs could help constrain the extent of interim USDSGD upside risks. Meanwhile, elevated global growth uncertainties could lead to some support for SGD, given its relative "safe haven" characteristics, aided by front-loading of monetary policy tightening (another off-cycle move in Jul) and favorable macro fundamentals such as ample fiscal space, resilient trade outturns and current account surpluses. SGD NEER has reached +1.1% above par as we write, around the middle of our +0.5% to +1.5% projection range and we remain buyers of SGD NEER on dips. After recent declines, we prefer to sell USDSGD on rallies at this point.

- Jul saw another +75bps hike from Fed, along with cues that that a similar-sized move was still possible in Sep. Still, markets focused on Powell's comments on potentially slowing pace of Fed hikes "at some point", and pared bets on pace/peak in Fed hikes. OIS-implied currently looks for Fed policy rate to peak at around 3.3% in Dec 2022 (versus market expectations of a higher peak near 3.9% just 6 weeks ago). On net, **calmer UST yields could help reduced interim upside risks for the USDSGD pair**.

- **Domestically, lower likelihood of return to strict Covid curbs could help anchor sentiments**. On 22 Apr, the DORSCON level was adjusted from Orange to Yellow, with group sizes being removed for mask-off activities and household visitors. More importantly, all workers could return to the workplace (up from 75% prior) and safe distancing will no longer be required between individuals or between groups. Capacity limits for larger settings/events (75% prior) have also been removed. On border entry, fully vaccinated and well travellers will not require any tests to enter Singapore. As of 14 June, capacity limits and requirements for negative ART tests were also removed for nightlife establishments. Continued recovery in domestic consumption could put a floor on GDP growth, despite concerns over softer interim external demand. Nonetheless, some caution could be warranted given signs of a broad recent uptrend in recent cases from Jun-Jul, but given sufficient healthcare capacity, high vaccination rates, well-communicated policy measures and significantly-reduced chance of wider lockdowns, domestic sentiments are unlikely to sour excessively.

- **Negative contagion from China growth moderation or yuan depreciation concerns to SGD could be easing.** Recent activity indicators point to some tentative bottoming in China's economic activity, at a time when PMI readings in DM economies are softening discernibly. While some caution is warranted on account of risks from Covid-zero policies and property sector vulnerabilities, a repeat of the yuan rout in Apr-May looks unlikely at this point. Spillover drags on SGD sentiments should moderate as well.

- **Growth and Inflation Outlook:** 2Q GDP came in at +4.8%y/y, versus expectations for +5.4%, largely due to better than expected performance in manufacturing (+8%) and services (+4.7%). Construction (+3.8% vs. +1.8% in 1Q) picked up but remains 23.7% below pre-pandemic levels (2Q19), as the sector continues to face labour shortages despite the relaxation of borders. On a quarter-on-quarter seasonally adjusted basis, GDP was flat (vs. +0.9% in 1Q), the weakest print since 2Q21.

- On higher-frequency indicators, retail sales for May came in at 17.8%y/y, accentuated by low base effects from last May, but still above expected 13.4%. IP growth lost steam in June (+2.2%) as semiconductor production (-2.6%) fell sharply from the record high level in May. Slowing consumer demand for PCs and smartphones may be weighing on chips. **Our economist team maintains 2022 GDP growth forecast at +2.8%**. Slowing global growth will weigh on manufacturing and trade-related services.

- Core CPI at +4.4% and headline CPI at +6.7% indicated stronger price increases across most categories in June. While global food and oil prices are easing, a tight labour market and rising wages will continue to drive services inflation in the second half. **Our economist team expects average core CPI at +3.5% and headline CPI at +5.5% in 2022. The team also raises 2023 forecasts for core CPI to +2.8% (from +2.1% prior) and headline CPI to +3.5% (from +1.8% prior)**.

- **Monetary Policy Forecast**: Reacting to concerns that core inflation is expected to rise above 4% near-term, while the economy remains on track to expand at a creditable pace, MAS implemented another off-cycle tightening move on 14 Jul to "lean against price pressures becoming more persistent"; i.e., to prevent inflation expectations from becoming entrenched, via re-centring the mid-point of the SGD NEER band up to its prevailing level. There is no change to the slope or width of the policy band. Given that SGD NEER was estimated at +1.6% above par in the last session close, the mid-point/band is estimated to have shifted higher by this extent.

- **Our economist team looks for MAS to maintain the current tighter stance at the October meeting**, unless inflation surprises on the upside yet again, warranting another material change to the MAS' inflation forecast. The S$NEER is currently trading at about +1.0% above the implied mid-point of the band, so there is still room for the SGD to appreciate. A slowing global economy and rising interest rates are deflationary forces that could cool price pressures in the second half. **Should broadening price pressures lead to another tightening move, a slight slope steepening (e.g., from current estimated +1.5% p.a. slope to +2.0%) should be more likely versus another re-centring move. The bulk of MAS normalization moves should be behind us by now.**

- As of writing, USDSGD is around 1.3800, and trades around +1.1% from the new implied mid-point of 1.3950, with the top estimated at 1.3675 and the floor at 1.4230. Output gap is now expected to close and see a slight positive reading in 2022, while core inflation could see a broad-based step up in 2022 and risks remaining elevated for some time.

Given these macro conditions, our Taylor rule estimates suggest that SGD NEER is likely to see a modest upward bias near-term. **We had proposed on 14 Jul that SGD NEER could trade within a +0.5% to +1.5% range above the new implied mid-point**, given some "haven" characteristics versus peers in this period of elevated external uncertainties, with preference to buy SGD NEER on dips. SGD NEER has crept higher from estimated trough of +0.2% mid-month to around +1.1% as of writing.

- Domestic interest rates continued rising in Jul. The 3M SORA and 3M SIBOR are at 1.2295% and 2.5321% at the time of writing, higher than the 0.7720% and 1.9125% seen in end-May. While risks might continue to be skewed to the upside for rate moves, MAS' stress test (published Dec 2021) shows that the household mortgage servicing ratios (MSRs) remain manageable under a conservative scenario of shocks to income and interest rates arising from a virulent virus outbreak. Specifically, the observed median MSR remains below the maximum threshold of 60% for the Total Debt Servicing Ratio (TDSR) guideline, even if income falls by 10% from the lows seen during the COVID-19 pandemic and interest rate increases by 250bps. As the bulk of the household liabilities are housing loans, the results suggest that the median household would still be able to service its debt. **House view for 3M SIBOR forecast is at 3% in 2022 and 3.2% in 2023. 3M SORA forecast is at 2.75% in 2022 and 2.95% in 2023**.

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

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

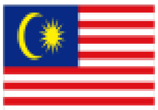
- In Jun, a S$1.5bn package was announced to help combat domestic inflation, including cash handouts (GST vouchers), utilities credits and one-off relief for taxi and private-hire car drivers. Given the overall limited scope of the new measures, spillover impact to SGD should be relatively limited.

- More recently, in light of supply-side shocks to energy markets globally, MTI Minister Gan Kim Yong said that the government does not intend to cap energy consumption by energy-intensive industries, and instead has other measures to help businesses improve their energy efficiency and tide over this period of elevated prices.

- The current account surplus improved to 19.75% of GDP in 1Q 2022, from 18.12% prior. A broad recovery trend has been observed since the trough in 4Q 2019. On higher-frequency indicators, NODX growth eased to +9% in June as electronics (+4.1%) softened to the slowest pace in 19 months due to the plunge in PCs, reflecting sluggish demand in the consumer electronics market. Our economist team narrows 2022 NODX growth forecast to 5%-6% (from 4%-6%), given the better than expected performance in 1H (+10.2%), but expect growth to ease to low-single digit growth in 2H. The global trade outlook is dampened by the China slowdown, Russia-Ukraine war, and global monetary tightening. **Further boosts to current account from trade outturns could be somewhat limited, even as some resilience is likely**.

- **Key domestic events and issues to watch**: Jul PMI (2 Aug); Jun Retail sales (5 Aug); Jul Foreign reserves (8 Aug); Jul NoDX (17 Aug); 2Q (F) GDP (22-25 Aug); Jul CPI (23 Aug); Jul Industrial production (26 Aug).

- **Technical Outlook**: USDSGD pair last seen modestly below 1.38, swinging discernibly lower in recent days, on dollar softening. For USDSGD pair, momentum on daily chart has turned modestly bearish while RSI is also on a gentle decline. Risks could be skewed to the downside in the interim, but prefer to sell USDSGD on rallies at this point. Resistance at 1.3880 (50.0% fibo retracement from May low to Jul high), 1.40 (23.6% fibo). Support nearby at 1.3770 (76.4% fibo), before 1.3670 (May low).



MYR: Global Growth Concerns and Policy Catch Up Factors

Forecast	3Q 2022	4Q 2022	1Q 2023	2Q2023
USDMYR	**4.40** (4.35)	**4.40** (4.30)	**4.35** (4.30)	**4.30** (4.25)

Previous Forecasts in Parentheses

- **Motivation for the FX View:** Once again, USD/MYR reached a new peak of 4.4751 on 14 Jul (similar patter seen in June as it peaked on 14 June) as dollar strength continued in the run up to the Jul FOMC meeting before falling on dollar moderation. Since then the pair has remained around the 4.42-4.47 range. We expect MYR to remain under pressure amid global growth concerns, tighter financial conditions and with BNM still catching up on the rate hike cycle. Nonetheless, the potential peak in Fed hawkishness, easing UST yields and USD moderation are some factors that could see the intermittent bounces in MYR. We think the USD retracement following the Jul 2022 FOMC is as expected but may have seen a bit of overshooting. On that basis, we should still expect USD support to pick up again in the run up to Aug and next FOMC on 20 Sep. More recently softer oil prices and expectations of upcoming domestic elections coming closer are expected to add further pressure on the MYR. On the back of these new developments we are revising the MYR slightly upwards to reflect some of the uncertainties building up over the next 6-12 months.

- Malaysia's external trade outlook is still a "battle" between the ongoing commodity price support and the downside of global economic outlook amid Russia-Ukraine war, US monetary tightening and China growth developments. Risks of fallouts from Russia-Ukraine war (especially on Europe), US-led global monetary policy tightening and China's lockdowns are clouding global economic – hence trade - outlook. Thus far, Malaysia is benefitting from commodity and tech exports. Palm oil, LNG and crude oil contributed to 23% of 5M 2022's +23.5% exports growth, with E&Eaccounted for another 48%.

- In summary, MYR weakness was largely driven by exogenous factors, including the earlier rise in UST yields, USD strength, sharp and continued decline in CNH (of which MYR has a strong correlation to), IMF's downgrade of global growth, risks of China slowdown amid extended lockdowns and ongoing war in Ukraine (sentiment, china proxy play). Some of these drivers have eased but lingering concerns about global growth and risk aversion will continue to support USD and raise cautious view of risky assets for the next few months or so, which may keep MYR ranged bound around 4.40-4.45.

- On the domestic front, the fractious and fluid dynamics of domestic politics does raise the possibility of general elections in 2H 2022. Elections and associated near-term uncertainties could induce higher vols for the USDMYR pair, but a sustained period of volatility and extended MYR losses is not our base case. While the USDMYR pair did rise by >8% from 2Q to 4Q 2018 (last elections in May 2018), the bulk of this upswing can be attributed to broad dollar strength (DXY >+6%) and oil softness (oil > -20%) over the same period. Accounting for these two factors, the actual elections-induced impact on MYR is likely modest—the BIS-estimated MYR REER (real effective exchange rate basket) notably fell by a modest 1.5% over this period. To a large extent though, a scenario of contained MYR vols/losses on election uncertainty is conditional on there being clear signs of ability of (potential) next ruling party/coalition to maintain policy continuity and economic traction post Covid-recovery.

- **Growth and Inflation Outlook**: Our economist team maintains forecast of broad-based +6.0% growth in 2022, in view of the potential 2Q 2022 and 2H 2022 GDP growth dynamics, but tweaked the supply-side and demand-side forecasts to factor in 1Q 2022 performance, and trimmed 2023 growth forecast to +4.7% from +5.0%. Real GDP growth likely strengthened further in June 2022, taking cue from the surge in Manufacturing PMI's % YoY growth signaling stronger manufacturing output growth. Further, real GDP shrank in June-Sep 2021, pointing to the prospect of low-base effect boost to monthly real GDP growth in June-Sep 2022 (and 3Q 2022).

- Headline inflation went up to +3.4% YoY in Jun 2022 (May 2022: +2.8% YoY; 1H2022: +2.5% YoY) mainly on rising food & non-alcoholic beverages (FNAB) cost (Jun 2022: +6.1% YoY; May 2022: +5.2% YoY). Core inflation also up to +3.0% YoY (May 2022: +2.4% YoY). Our economics team maintain our 2022 and 2023 inflation forecasts at +3.4% and +4.1%

respectively, primarily on the impact of announced and impending rationalization in price subsidies for essential food, fuel and energy

- **Monetary Policy Forecast:** BNM raised OPR by 25bps to 2.25% at the 5-6 July 2022 Monetary Policy Committee (MPC) meeting. This followed the 25bps hike to 2.00% at the 10-11 May 2022 meet. BNM's Monetary Policy Statement (MPS) maintains the messaging that BNM's unwinding of accommodative monetary policy – hence OPR hikes - will be "measured and gradual". No change in our view of total +75bps hikes this year to 2.50% and another +50bps hikes next year to 3.00%.

- We noted BNM's Monetary Policy Statement (MPS) assessment of slowing global economic growth on one hand amid the downside risks from rising inflationary pressures, conflict in Ukraine, global supply chain conditions and financial market volatility, and strengthening domestic economic activities and demand - including retail spending - as well as improving labour market conditions on the other hand, reflecting the impact of full economic opening – including international borders that facilitates the recovery in tourism-related sectors. BNM's real GDP growth forecast for Malaysia is currently a range of +5.3% and +6.3% (1Q 2022: +5.0% YoY; 2021: +3.1%). BNM also keeps its view that this growth outlook comes with downside risks stemming from external factors i.e. weaker-than-expected global growth; further escalation of geopolitical conflicts; worsening supply chain disruption.

- BNM maintains its 2022 forecast for headline inflation rate of +2.2% to +3.2% (5M 2022: +2.4% YoY; 2021: +2.5%; 2020: -1.2%) and for core inflation rate of +2.0% to +3.0% (5M 2022: +2.0% YoY; 2021: +0.7%; 2020: +1.1%). BNM foresees higher inflation rate in coming months (May 2022: +2.8% YoY; Apr 2022: +2.3% YoY) but the upward pressures on monthly inflation will be contained primarily by price controls and subsidies.

- MPS concluded that with positive domestic economic growth outlook for this year, the conditions and time is right to further adjust the degree of monetary policy accommodation via the announcement of another 25bps hike in OPR. MPS also reiterated that the process of unwinding monetary policy stimulus will be "measured and gradual".

- We interpret "measured and gradual" to mean further/future OPR hikes will be by 25bps quantum, notwithstanding the ratcheting up of US Fed's interest rate hikes from 25bps in Mar 2022 to 50bps in May 2022 and 75bps in June 2022.

- Inflation rate, while rising, is slower relative to regional peers and major economies and is predominantly cost-push and supply-driven so far this year as Russia-Ukraine war led to surges in commodity prices, and food, energy and fuel costs. Historically, BNM has tolerated periods of negative real OPR and negative differentials between OPR and US fed funds rate.

- Our OPR outlook is total of +75bps hikes to 2.50% in 2022 and another +50bps hikes to 3.00% in 1H 2023. Interest rate swap (IRS) curve is currently pricing in OPR hikes of +50bps next 6 months and +100bps increases over next 12 months.

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

- **Key domestic events and issues to watch:** Jul PMI Mfg (1 Aug); BNM Monetary policy decision (8 Sep); Foreign Reserves (5 & 22 Aug); Industrial Production (9 Aug); BoP Current Account balance (12 Aug); GDP (12 Aug); Trade data (19 Aug); Jun CPI (26 Aug).

- **Technical Outlook:** USDMYR is finally showing signs of easing near recent highs amid USD pullback, firmer oil prices and supported risk sentiment. Pair was last at 4.4490 levels. Mild bullish momentum on daily chart is waning while RSI fell from overbought conditions. Bias for corrective move lower. Support at 4.44 (21 DMA), 4.4130 (50 DMA). Resistance at 4.50 (2017 high).

IDR: Expected Resilience from Trade Balances

Forecast	3Q 2022	4Q 2022	1Q 2023	2Q 2023
USDIDR	**14,700** (--)	**14,500** (--)	**14,400** (--)	**14,300** (--)

No Change to Previous Forecasts

- **Motivation for the FX View:** USDIDR was in a consolidative phase for most of the first four months of the year and only broke out higher towards May-Jul, alongside China partial Covid lockdowns, Fed normalization concerns (i.e., portfolio outflows), uncertainty relating to export policy, and more recently, global growth risks (likely weighing on commodity demand outlook). Still the magnitude of USDIDR upswing has been somewhat contained versus historical episodes of IDR depreciation, and we note signs of cautious optimism emerging. The palm oil export ban was relatively short-lived and is gradually unwinding; CPO exports are expected to recover significantly in the coming months, supporting trade balances despite recent moderation in prices. Latest data out of China also shows some signs of bottoming out in economic activity. Reaction to latest Jul FoMC also saw markets paring back expectations in peak Fed rate, given rising growth risks. Lower UST yields on net could help ease drags on IDR from portfolio flows. BI also notably committed to remain in markets to ensure IDR stability.

- **CPO export volume recovery could help anchor trade surpluses despite moderation in prices**. Indonesia's top exports include palm oil, coal, copper and nickel. It ships about a third of the world's edible oil supplies, consuming just over a third of production domestically. Our regional plantations analyst views CPO inventories in Indonesia as bloated, with exports likely to pick up in coming months (as permit bottlenecks ease) and providing further support to trade balance, despite softer CPO prices. In Jul, the Indonesian government announced a USD200/t palm oil export levy waiver (in effect till end-Aug) in its bid to stimulate exports. It may still take at least 2 months for inventories to normalize as ID is now entering its seasonal peak production cycle in 2H, but concomitant boost to export volumes could still help aid IDR sentiments in the interim. On net, comments from Sahat Sinaga, acting chairman of the Indonesia Palm Oil Board, suggests that Indonesia could ship up to 17.3 million tons of palm oil overseas in 2H, versus just 10.7 million tons in 1H due to export ban imposed in late April and other curbs. Meanwhile, Jokowi's visit to China reportedly produced pledges from China to prioritize imports of Indonesian agricultural products, including a commitment to increase imports of CPO by 1mn tons.

- April-June rout in US treasuries triggered by earlier hawkish shifts in Fed signalling dampened IDR sentiments, with the June bout of UST yield climb above 3% having a more discernible drag. IGB-UST 10Y yield differential narrowed from around interim high of 500bps in early Mar to interim low of around 384bps in early May as UST yields spiked, but has on net headed higher since; last seen at around 448bps. **On net, yield differentials likely remain sufficiently wide to avoid triggering a larger exodus of foreign funds**, even as near-term drags on IDR from portfolio flows appear intact, with Jul MTD net outflows in equities and bonds reaching -US$192mn and -US$2046mn, respectively. But on bond outflows in particular, we note that magnitude is more modest versus Covid onset in Mar 2020 (-US$7538mn). **Post the Jul FoMC, markets likely took comfort from Powell's comments on potentially slowing pace of Fed hikes "at some point".** Treasury yields declined in reaction, with the front-end seeing larger dips versus long-end. Any additional support for the "peak hawkish Fed" narrative could help cap interim UST yield upswings and help moderate the extent of sentiment drags on IDR.

- **In any case, extent of broad volatility spillovers from external risk events to IDR assets should be contained, given lower foreign holdings in Indo sovereign bonds, still resilient current account balance, larger FX reserves vs. earlier Fed tapering episodes**. House view looks for current account to come in at a modest deficit of 0.5% of GDP in 2022 compared to pre-pandemic deficit of above 2.5% of GDP. Foreign reserves rose slightly to a 3-month high of $136.4bn as of end June (from $135.6bn in May), as the government issued global bonds (Samurai bond sale) that raised US$624mn.

- On Covid, 7-day average in Covid-19 cases was seen at around 5k in late Jul. While there are signs of a gradual uptick in recent weeks, case counts remain low versus interim highs near 56k on 20 Feb. Covid-related risks have fallen significantly. On net, **authorities are largely sticking to a Covid-endemic and reopening policy stance.**

- **Growth and Inflation Outlook:** GDP growth was steady in 1Q as the relaxation of pandemic curbs drove a pickup in household consumption.

GDP expanded by +5%y/y, the same pace as 4Q. 1Q real GDP came in +7.4% higher than pre-pandemic (1Q19) levels.

- On higher-frequency indicators, Mfg PMI for Jun came in at 50.2, deteriorating slightly from 50.8 prior. But on net, our economist team noted that domestic demand is extending its robust recovery, with consumer confidence soaring to a new record high in May and June. Car sales and property transactions have benefited from the government's Covid stimulus measures, but may ease in the second half when the incentives expire. Visitors arriving via flights climbed to 184k in May, rising to 26% of pre-pandemic levels with the relaxation of borders and events such as the Pertamina Grand Prix and G20 meeting. Both domestic (+25% in 1Q) and foreign investment (+34%) realization are surging, with FDI especially strong in basic metal (downstreaming industries) and electric vehicles. **Full year 2022, 2023 GDP growth forecasts are maintained at +5.1%, 5.2%, respectively**.

- Headline CPI (+4.3%) breached BI's target range in June, driven by the jump in food prices. But core inflation (+2.6%) rose at the same pace for the third month. Our economist team expects headline CPI to accelerate to +4.7% in the second half of the year (vs. +3% in 1H22), and **have recently raised full year inflation forecast to +3.9% in 2022**.

- **Monetary Policy Forecast:** BI stood pat on 21 Jul, keeping the policy rate at record low 3.5%. Authorities expressed slight caution on the domestic growth outlook, i.e., growth could come in below 4.9%, i.e., mid-point of BI's 4.5% to 5.3% target. While headline CPI reading is expected to breach the 2-4% target, core reading should remain within the range, i.e., manageable underlying price pressures. Rather than the policy rate, other tools such as bond sales will be used to reduce market liquidity. BI also committed to remain in markets to ensure IDR stability.

- On current account, BI raised its forecast to between -0.5% to +0.3% of GDP (from previous estimate of a 0.5%-1.3% of GDP deficit), given the resilient trade surplus which climbed to a record high of US$15.6bn in 2Q (vs. $9.3bn in 1Q). While portfolio investment has seen a net outflow of around US$2.2bn month-to-date (as of 27 July), reversing the $0.2bn net inflow in 2Q, foreign direct investment is expected to be firm. FDI realization in 2Q jumped by +42.2% in 2Q from a year ago (vs. +34.1% in 1Q), mainly driven by the secondary sector (+60.8%). More resilient current account dynamics could help mitigate sentiment drags. On net, **our economist team maintains view for a +75bps hike from BI in 2022 to end the year at 4.25%, with the first rate hike at the next meeting in August followed by two rate hikes in 4Q**.

- Meanwhile, with regards to concerns on unwinding of QE-era bond purchases, BI Governor Perry Warjiyo said that sales would be conducted carefully. The aim is to soak up excess market liquidity, while also pushing bond yields up to make Indonesian assets more attractive amid global monetary tightening. BI had sold around IDR1.1trn of bonds in the first half of Jul and aimed to sell about IDR70trn of bonds with maturities of 5 years and below over time.

- One risk to look out for could be some tentative concerns over BI autonomy, given recent discussions over a new draft legislation requiring BI to take into account the government's broad economic strategy when making monetary policy decisions. The bill could also provide a legal basis for BI to buy sovereign bonds in the primary market when needed during a financial crisis.

- **Latest Fiscal and External Balance Outlook:** In Sep 2021, parliament proceeded to approve Jokowi's 2022 budget with a total spending of IDR2,714.2trn (US$190bn), a slight decrease from IDR2,750trn budget for 2021. Government revenue is expected to rise discernibly, as both income tax and value-added tax (VAT) are projected to grow by more than +10% with the expansion of VAT collection and the normalization of growth.

- In early Jan 2022, it was estimated that Indonesia recorded a budget deficit of 4.65% of GDP for 2021, "far smaller" than initial estimates, according to FM Sri Mulyani. The government collected IDR2,003trn (US$140 billion) in revenues for 2021, while spending reached IDR2,787trn. Tax revenues were 19% higher than in 2020 and about 104% of the target. **Following better than-expected revenue collections in 2021, the 2022 fiscal deficit estimate was lowered to 4.3% of GDP. This was subsequently lowered to 3.9% of GDP.** Fiscal conditions also seem to be improving YTD, with realization of state revenues reaching IDR1317trn as of Jun, representing 58% of the targeted revenues for 2022, and a 48.5% increase from a year ago.

- In an Apr public address, **President Jokowi called on public agencies to prepare a "detailed, correct and precise" spending plan to return the state budget to below 3% of the GDP in 2023**, in accordance with Law no. 2 of 2020 on State Financial Policy and Deficit Financial System Stability, after allowing the deficit to exceed 3% in FY2020-FY2022 to meet pandemic financing needs. **Signs of fiscal discipline can help mitigate drags on IDR from a return of current account surplus into modest deficit territory**.

- Exports in June accelerated by +40.7% (vs. +27% in May), following the lifting of the palm oil export ban. For 1H, exports were driven and flattered by high prices rather than volumes, especially for shipments of coal, palm oil, iron & steel, nickel and copper. Trade surplus widened to US$24.9bn in the first half of 2022, more than double the $11.8bn recorded in the same period in 2021. Drags from earlier CPO export ban should continue to ease over the next few months. On net, house view looks for current account to come in at a modest deficit of -0.5% of GDP, versus mild surplus of +0.3% of GDP in 2021. **Outlook remains resilient for the year, which could help mitigate recent IDR drags.**

- **Key domestic events and issues to watch**: Jul PMI Mfg (1 Aug); Jul CPI (1 Aug); Jul Foreign reserves (5 Aug); 2Q GDP (5 Aug); Jul Trade (15 Aug); Jul Local auto sales (15-21 Aug); 2Q BoP Current Account (19 Aug); BI Monetary policy decision (23 Aug).

- **Technical Outlook:** USDIDR last seen at 14,835, mildly lower versus levels seen in end-Jun. Momentum on daily chart has turned mildly bearish while RSI is also on the dip. Risks skewed mildly to downside. Pair could test key resistance at 15,000 intermittently, even as sustained breakout higher for longer looks less likely at this point.

Earlier bearish divergence could still be in play. Besides 15,000, next resistance at 15,200. Support at 14,800 (50-DMA), 14,600 (100-DMA).

PHP: Tentative Bottoming in Sentiments

Forecast	3Q 2022	4Q 2022	1Q 2023	2Q 2023
USDPHP	54.50 (--)	54.00 (--)	53.50 (--)	53.00 (--)

No Change to Previous Forecasts

- **Motivation for the FX View:** USDPHP hit a high near 56.4 around mid-Jul, on confluence of drags from trade balance weakening, Fed tightening as well as domestic policy uncertainty. Since then though, oil prices have softened, helping to ease drags from energy import burdens. Rising US recession risks have led to an increase in bets for Fed to pare pace of rate hikes, bringing dollar and UST yields lower. In a recent State of Nation Address, President Marcos also introduced a 19-point legislative agenda to spur growth and attract new investment flows, providing some clarity on policy trajectory. In a way, the latest confluence of developments could imply that earlier negative sentiments on PHP could be easing. We maintain a gradual downward-sloping trajectory in our USDPHP forecasts in the coming quarters.
- **While oil is not the dominant factor for PHP in this complex risk environment, rise or decline in energy import bills could continue to influence PHP**. Brent has fallen from around US$124/bbl in early Jun to US$107/bbl at last seen. Extent of oil price upsides could also be constrained going forward given (i) mounting concerns over softening global aggregate demand as financial conditions tighten, (ii) signs of interest in Russian oil from parts of Asia, including China, India, (iii) planned ramp-ups in OPEC+ supplies over time. Admittedly, inpact of (iii) could be more modest near-term. Market chatters are that UAE and Saudi Arabia are already pumping almost as much oil as they can. Latest data also show OPEC+ members producing 2.84mn b/d below their collective target. In this case, **conditional on oil gains potentially seeing some moderation in 2H, PHP sentiments could see modest support over time**.
- On Covid, we note that while 7-day average in cases has risen to around +3k in late Jul, versus lows near 200 in May, President Ferdinand Marcos has pledged that the country will no longer implement COVID-19 lockdowns, adding that it cannot afford to put one in place. Instead, efforts will be made to ensure that the healthcare system does not get overwhelmed. **Sustained easing in Covid drags on the domestic economy should lend support to PHP on net.**

- OFWR growth slowed in May 2022 to +1.8%y/y (Apr 2022: +3.9%), partly on base effect given last year's fastest growth of +13.1% in May 2021. OFWR outlook faces the global economic downsides due to Russia-Ukraine war drags on Europe and US-led global interest rate hikes, but our economist team maintains 2022 OFWR growth forecast at +4.2% (5M 2022: +2.5%; 2021: +5.1%). Meanwhile, foreign reserves for Jun came in at US$102bn, seeing a mild decline versus US$103.7bn prior, but remaining high versus historical averages (2012-19 average around US$81bn). **On net, resilient remittances flows and adequate reserves could still help mitigate PHP drags over the year**.

- **Some spillovers from soft yuan and China Covid/growth risks was likely in play for the AxJ FX complex over the last few months, but concerns could have eased a tad.** We note more signs of stabilization in activity in China, despite the official Covid-zero stance. China PMIs, both manufacturing and non-manufacturing, also returned to expansionary territory in Jun, giving cause for cautious optimism. **PHP could also see relative resilience on this front given the more domestic-oriented nature of the Philippines economy**. As of 2020, share of exports to GDP is relatively low for Philippines at 25%, versus 61% for Malaysia, 176% for Singapore, 52% for Thailand. While Indonesia has a lower share at 17%, it is more sensitive to global commodity trends given its pre-dominantly commodity-linked exports.

- **Growth and Inflation Outlook:** Philippines' real GDP growth in 1Q 2022 accelerated +8.3%y/y (versus +7.8% prior), underpinned by stronger domestic demand—especially private consumption—amid easing of movement restrictions and improved labour market conditions. But alongside heightened external risks and BSP interest rate hikes cycle kicking off, **our economist team maintains GDP growth for 2022 at 6.5%.**

- On higher frequency indicators, PMI Mfg for Jun came in at 53.8, following outturns of 54.1 prior, reflecting some traction in the domestic economic recovery. But a BSP survey shows businesses putting on hold expansion plans amid rising inflationary pressures. Labour market performance remains broadly mixed. While employment rebounded +1.0%m/m (Apr 2022: +2.9%), unemployment rate rose to 6.0% in May 2022 (5M2022: 6.1%) after registering the pandemic-era low of 5.7% in Apr 2022. Underemployment rate also picked up to 14.5% (Apr 2022: 14.0%). Our economist team maintains 2022 and 2023 unemployment rate forecasts at 5.5% and 5.0% respectively (2021: 7.8%).

- Headline inflation rate accelerated further to +6.1%y/y in Jun 2022 (May 2022: +5.4%), well above the upper end of BSP's target range of 2%-4%, on higher FNAB, HWEGOF and transport costs. **With the latest inflation print, our economist team revises upwards 2022 and 2023 headline inflation rate forecasts to +5.3% (from +4.6%) and +3.9% (from +3.3%), respectively (2021: +3.9%).** Addressing the impending food crisis, new President Marcos said his administration would rather boost local production than rely on imports, vowing to significantly increase the output of rice and corn. If successful, this could help improve the current account, and lend the PHP some support. But progress would take time.

- **Monetary Policy Forecast:** BSP implemented a surprise +75bps hike on 14 Jul. Surprise policy announcement might be to address concerns that the central bank was behind the curve in addressing inflation concerns, especially with rising bets for outsized Fed hikes near-term. **On net, house view looks for BSP to frontload and brought forward policy interest rate to this year by another +75bps to 4.00% as BSP expects inflation rate of +5.0% in 2022 and +4.2% in 2023**. Progress in rate hikes could help blunt recent upside pressures on USDPHP. Meanwhile, latest comments from BSP Governor Medalla has narrowed magnitude of potential hike on 18 Aug to 25-50bps. The Governor also maintained that BSP is prepared to use all its tools to preserve financial stability.

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

- **There are early signs of increasing fiscal stresses.** Public debt climbed to 63.5% of GDP as of end-Mar, 3.1%-pts higher on year-ago basis. Average monthly budget deficit from Jan to Jun 2022 is around -PHP112bn, vs. the pre-pandemic monthly average of -PHP55bn in 2019, reflective of the fiscal challenges associated with the pandemic.

- But in his state of the nation address in late Jul, **President Marcos vowed to overhaul the tax system, introducing a 19-point legislative agenda to spur growth and attract new investment flows**. A proposed VA tax on digital services is estimated to generate PHP11.7bn in revenues if implemented in 2023. The administration targets 6.5-7.5% growth this year and 6.5-8% GDP expansion through 2028. **He also pledged to bring down the fiscal deficit to GDP ratio to 3% by 2028 (consensus estimate of -7.7% this year), while lowering debt-to-GDP ratio to less than 60% by 2025**.

- May 2022 saw third month of single-digit exports at +6.2%y/y (Apr 2022: +6.2%) amid tepid manufacturing exports & commodity-based exports surge vs continued double-digit imports growth of +31.4%y/y (Apr 2022: +29.4%) reflecting impact of high global commodity & input prices plus softer PHP amid slower consumption goods imports. Trade deficit widened to –US$5.7b (Mar 2022: -US$5.3b). Shipments to China & US in recent months show impact of external headwinds. But as mentioned, **Jun-Jul decline in commodity and energy prices could bring some relief on the import burden front. House view looks for current account deficit this year to come in at 2.5% of GDP, versus 1.7% prior.**

- **Key domestic events and issues to watch:** Jul PMI Mfg (1 Aug); Jul CPI (5 Aug); Jul Foreign reserves (8-15 Aug); Jun Unemployment rate (9 Aug); Jun trade (9 Aug); 2Q GDP (9 Aug); Jun Overseas Remittances (14-17 Aug); BSP Policy decision (18 Aug); Jul BoP Overall (18-23 Aug); Jul Budget balance (22 Aug).

- **Technical Outlook:** USDPHP last seen at 55.15, swinging higher in the first half of Jul and retracing lower after. Momentum on daily chart is modestly bearish while RSI also on the dip, suggesting that upside risks could be somewhat contained in the interim. Resistance at 55.90 (21-DMA), 56.45 (Jul high). If up-moves remain resisted by key resistances, we could see pair paring gains towards support at 54.45 (50-DMA), 54.20 (50% fibo retracement from Apr low to Jul high).

THB: Tourism Uptick To Ease Drags, But Recovery Likely Slow

Forecast	3Q 2022	4Q 2022	1Q 2023	2Q 2023
USDTHB	**35.50** (34.80)	**35.10** (34.40)	**34.80** (34.00)	**34.50** (33.60)

Previous Forecasts in Parentheses

- **Motivation for the FX View:** USDTHB touched high (since 2006) near 37-handle this month, before paring gains into end-Jul on broader dollar softening. Caution for THB remains intact, given firm Covid-zero Covid stance in China (complicates timeline for return of Chinese tourists), and perceptions of lagging policy normalization versus peers and major central banks. Recent weakening in current account dynamics explain in part our modest adjustments higher for USDTHB forecasts. But drags from Fed-BoT policy divergence could have eased a tad. Recent comments from BoT Governor suggest rate hikes are coming soon, albeit likely gradual in pace. Meanwhile, Powell comments post Jul FoMC and another contractionary GDP reading in US had led markets to pare back expectations on pace of Fed hikes. On net, USDTHB pair could remain in buoyant trading ranges for a while yet but with various drag factors already baked somewhat into THB sentiments, USDTHB could have tentatively peaked in Jul. As tourism revenue receipts provide incremental support over time, THB drags could ease into 2023.

- A key market mover in March-Jun was an increasingly hawkish Fed, as persistently high inflation readings eventually forced Fed to hike by +75bps in June and Jul. But in recent weeks, markets appeared to have pared back hawkish expectations on Fed. The rising US recession risks could lead Fed to be more careful in calibrating rate hike pace later in the year. Reflecting these sentiment shifts, OIS-implied market expectations for peak Fed policy rate going forward has moderated to around 3.3% at last seen, from high of around 3.9% in mid-June. As such, **likelihood of another bout of strong dollar rally could be reduced, which could help cap extent of interim USDTHB strength.**

- For THB, trends in portfolio flows might be a key indicator to watch. Pace of bond outflows was mild in Jul (-US$96mn as of 27 Jul) versus Jun (-US$440mn), while equities actually saw modest net inflows (+US$128mn MTD as of 27 Jul), reversing the performance in Jun (-US$841mn). **Some cautious optimism could be emerging on the portfolio flow front for now.**

- THB continues to be impacted by oil price swings, given its role as an net oil importer. While global growth concerns in Jun-Jul has led to some paring of earlier gains, brent is last seen still >US$100/bbl. But extent of oil price upsides could be constrained going forward given (i) mounting concerns over softening global aggregate demand as financial conditions tighten, (ii) signs of interest in Russian oil from parts of Asia, including China, India, (iii) planned ramp-ups in OPEC+ supplies over time. Admittedly, inpact of (iii) could be more modest near-term. Market chatters are that UAE and Saudi Arabia are already pumping almost as much oil as they can. Latest data also show OPEC+ members producing 2.84mn b/d below their collective target. On net though, **conditional on oil gains potentially seeing some moderation in 2H, THB sentiments could see modest support over time**.

- Domestic Covid cases have been on an upswing for most of Feb-Mar, but **has largely reverted to a downtrend from Apr**. 7-day average in new daily cases is around 2-3k in late-Jul, versus peak of near-30k in end March. Earlier, authorities released a roadmap for transitioning from pandemic status to endemic.

- **Tourism flows are improving at a healthy pace (from low base), even as absence of Chinese tourists will continue to weigh on the outlook.** Post recent scrapping of various Covid curbs, tourism recovery is ongoing, with authorities expecting about ~1.5mn tourists a month in 2H versus <300k in Apr. But it will take significantly more time for a more discernible recovery in tourism activity, given that Chinese tourists (28% of total visitor arrivals in 2019) will unlikely return this year, with China maintaining its Covid-zero policy. Pre-Covid tourist levels were closer to 40mn, with tourism sector accounting for about 12% of GDP, while authorities only expect 8mn visitors in 2022. In the interim, THB could still see sentiment shocks on shifts in Covid risks/headlines coming out of China.

- **Growth and Inflation Outlook**: 1Q GDP growth picked up slightly due to the recovery in private consumption with the reopening and return of tourists. GDP rose by +2.2% from a year ago (vs. +1.8% in 4Q), above consensus (+1.7%) but slightly below our economist team's estimate (+2.4%). On a q/q SA basis, GDP expanded by +1.1% (vs. +1.8% in 4Q). For now, Thailand remains the laggard among ASEAN-6 countries with the softest GDP recovery in 1Q, as compared to +5% in Indonesia, Malaysia, and Vietnam, and +8.3% in the Philippines. 1Q GDP remained around 2.4% below pre-pandemic (1Q19) levels, as services exports (tourism) are around 64% below pre-pandemic levels.

- On higher-frequency indicators, PMI Mfg came in at 50.7 for June, moderating from 51.9 prior but remaining in expansionary territory. Domestic demand picked up in May as both private consumption and investment improved with the reopening tailwind. Exports were resilient while tourist arrivals climbed with the easing of travel restrictions. **Our economist team maintains 2022 GDP growth forecast at +3.2%.** While tourism will support growth, we remain cautious on the outlook for private consumption, which may be dampened by surging living costs and high household debt.

- Headline CPI climbed to a 14-year high of +7.7% in June, driven by food and energy costs, and a weak THB. With the higher than expected price pressures to date (1H22: +5.6%), **our economist team raises headline CPI forecast by another leg to +6.3% (from +6%), slightly higher than BoT's estimate (+6.2%)**.

- **Monetary Policy Forecast:** On 8 June, the MPC voted 4-3 to keep its policy rate at 0.5%. BoT cited that given the upside risks for economic recovery and inflation, there would be less need for the current accommodative monetary policy going forward. It raised its headline CPI forecast to +6.2% (from +4.9% in March) in 2022 and +2.5% (from +1.7%) in 2023.

- BoT Governor Sethaput recently said that Thailand's interest rate normalization should come "sooner rather than later" to anchor inflation expectations but pace could be gradual. He noted that BoT needed to balance between growth and inflation risks even as emphasis could be shifting to the latter with growth becoming firmer. **Our economist team now expects the BoT to hike 3 times in 2022 to tackle inflation, with a +25bps hike in each of the remaining meetings in Aug, Sep, and Nov. This will lift the policy rate from the current of 0.5% to 1.25%.**

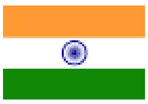
- **Latest Fiscal and External Balance Outlook**: In recent months, fiscal efforts largely revolve around managing cost-of-living pressures, involving cash assistance, discounts or excise-tax cuts for products such as retail diesel, cooking gas purchases, electricity. Contributions under the social security system were also lowered (from 5% to 1%) for both employers and workers.

- Parliament passed the first reading of a THB3.185trn draft budget bill for FY2023 (starting 1 Oct), with 278 votes in favour, 194 against and 2 abstentions. The budget sees spending growth of 2.74% in spending and projects deficit at around 3.9% of GDP. The bill still has to pass second and third readings in Aug before being sent for senate and royal approval. Signs of progress in the budget process could be net positive for THB, even as broader external cloudy outlook could mitigate extent of positive spillovers.

- In late Jul, the cabinet approved additional economic assistance worth THB27.4bn (US$785mn) from 1 Sep to support lower-income households amid soaring inflation. This includes extension of the co-payment scheme (THB800 per person per month) for the fifth time, and THB200 cash handouts to vulnerable groups (elderly, disabled, and state welfare card holders). The schemes will be funded from borrowings under the second emergency loan decree, and the drawdown is expected to leave around THB50bn of remaining borrowings from the overall THB500bn.

- Recent comments from Finance Minister Arkhom suggests that authorities will focus on maintaining fiscal discipline after the large bout of borrowing earlier. House view is for fiscal deficit to narrow towards 4.3% of GDP in 2022 from 4.8% prior. **While efforts to maintain fiscal discipline are largely positive for THB sentiments over the long-run, there could be near-term concerns on potentially more constrained support to growth from fiscal policy**.

- We also note some tentative concerns surrounding the State Oil Fund, which is more than THB100bn in debt. The energy ministry is currently considering ways to boost the fund, including asking oil refineries to channel parts of their profits and requiring gas separation plants to send income from price differences.
- The current account deficit narrowed to US$1.9bn in Jun (vs. $3.7bn in May), as the net service, income, and transfers balance displayed a smaller shortfall. Trade and service sectors reportedly recovered on account of improving foreign tourist figures, following relaxation of Covid curbs and travel restrictions. The -US$3.7bn deficit (widest in 9 years) in May appeared to be due in part to repatriation of dividends and profits by foreign companies, which was likely a transitory drag.
- Meanwhile, export growth (+11.8%) picked up to a 3-month high in June, boosted by resilient global demand especially for agricultural products, as well as a weak THB. But imports (+24.5%) continued to outpace exports due to higher bills for fuel imports, keeping the trade balance in a deficit for the third straight month, at US$1.5bn (vs. $1.9bn in May). On net, elevated energy bill continues to pose drags to current account balance, but drags could be tempered in part by improving tourism receipts over time, conditional on further oil gains being capped. **Our economist team maintains current account deficit forecast at 1% of GDP in 2022.**
- **Key domestic events and issues to watch:** Jul PMI Mfg (1 Aug), Jul Business sentiment (1 Aug); Jul CPI (5 Aug); Jul Consumer confidence (9-10 Aug); BoT Policy decision (10 Aug); 2Q GDP (15 Aug); Jul Customs trade (24 Aug); Jul Manufacturing Production (26-30 Aug); Jul BoP Current account (31 Aug).
- **Technical Outlook**: USDTHB last seen near 36.15, swinging higher in the first part of Jul before paring gains. Bullish momentum on daily chart has largely moderated, while RSI remains in overbought conditions. Risks skewed mildly to the downside. Key resistance at 37.0. Support at 36.2 (21-DMA), 35.3 (50-DMA).



INR: Widening Trade Deficit Still A Threat

Forecast	3Q 2022	4Q 2022	1Q 2023	2Q 2023
USDINR	79.00 (--)	79.50 (--)	79.50 (--)	80.00 (--)

No Change to Previous Forecasts

- **Motivation for the FX View:** Widening trade deficits and elevated crude oil prices (Brent still around the $100/bbl) could continue to keep the pressure on the INR, especially if domestic recovery is maintained. That said, much has been done administratively to curb inflation, limit the current account deficit as well as to prop up the INR. The most sweeping change enacted by RBI is to allow for trade settlement with Russia and Sri Lanka to be in rupee. Exchange rates are to be market determined according to RBI.

- This month, the government has curbed the export of wheat flour and other associated products with effect from 12 Jul. This is done to curb food inflation at home especially ahead of festive season. Tax and shipping restrictions on fuel exports also took effect in Jul in order to ensure adequate supply for domestic use. These came on top of restrictions on sugar exports and an outright ban of wheat export in May. The protectionistic policies have limited exports receipts for India. On the other hand, India has also raised its import duty on gold to 12.5% from 7.5% in order to reduce gold imports and slow the widening of the trade deficits as well as the depreciation pressure on the INR.

- With regards to the INR itself, there has been traces of FX intervention to prop up the currency. The level of foreign exchange reserves had actually fallen $30bn since the end of May to around $573bn at last check. While this could be partially due to valuation effects, RBI Das more recently used the analogy of using the umbrella when it rains to point out the purpose of accumulating reserves. With RBI likely to continue to support the rupee with outright USD sales in the spot market, we anticipate slower depreciation. At the same time, some expectations for slower pace of Fed tightening might translate to more benign USD and US yield environment. USDINR may thus have a chance of remaining within 79-80.

- **Growth and Inflation Outlook:** Industrial production picked up pace to 19.6%y/y from previous 6.7%, flattered by the base effects as India experienced the delta Covid-19 wave last year. Production actually rose 2.3%m/m in May. There was growth across all sectors including mining(+3.4%m/m), manufacturing (+2.0%m/m) and electricity (+2.8%m/m). Looking forward, Jun PMI eased to 53.9 from previous 54.6 while services PMI rose to 59.2 from previous 58.9. PMI numbers suggest that activity numbers remain in expansion for now. That said, the IMF had cut growth forecast to 7.4% from previous 8.2% for FY2023. RBI has also recently reduced its growth forecast to 7.2% from previous 7.8%.

- CPI steadied around 7.0%y/y for Jun as softer food inflation at 7.75%y/y (vs. previous 7.97%) offset stronger price pressure for clothing & footwear (9.5% vs. prev. 8.85%), housing (3.9%y/y vs. 3.7%) and fuel and light (10.4%y/y vs. prev. 9.5%). Month-on-month, price pressure actually eased for most subcomponents including food at 1.00%m/m from previous 1.6%, clothing & foorwear at 0.80%m/m vs. previous 1.04%, housing at -0.48% vs. prevous 0.36%. Fuel and light inflation also slowed to 1.03% from previous 1.28%. To quite a fair extent, inflation is being contained by various administrative measures even if it is at the expense of some deterioration in trade balance.

- **Monetary Policy Forecast:** RBI is likely to take the repo rate by another 50bps to 5.40% at the Aug meeting. Recent decline in CPI was modest and Jun's print of 7.01% y/y could still be uncomfortable for the MPC and the central bank may continue to tighten monetary policy further to temper inflation. A hawkish RBI could continue to spook investors and spur equity outflows. Apart from the next rate hike in Aug, we look for the central bank to ease pressure on the INR by means of intervention so as to keep depreciation at a measured pace.

- Recall that Finance Minister Nirmala Sitharaman assured that economic growth will remain supported by fiscal spending whilst RBI pivots towards countering inflation. She highlighted that supply-side spending generates enough multiplier effect to spur the economic rebound from the pandemic which will act as the offset for RBI's plan to remove monetary policy accommodation. More recently, FinMin has also mentioned about monitoring the current account deficits.

- **Latest Fiscal and External Balance Outlook:** Budget 2022-23 was an expansionary one. **Fiscal deficit was projected to ease to 6.4% of GDP for FY2022-23 from 6.9% in the year prior but this could be increasingly challenging given the amount of fiscal spending the government has planned to help in the coping of inflation pressures.** Finance Minister Nirmala Sitharaman had proposed increasing capital spending by 35% to INR7.5trn for 2022- 2023. In addition, there is a push for infrastructure-led growth with spending focused on roads, rail, logistics and energy, bringing to fruition the National Master Plan for economic transformation, multimodal connectivity and logistics efficiency that was approved by the Union Cabinet last Oct. Effective capital expenditure is estimated to be at 4.1% of GDP.

- Trade deficit widened to $26.2bn in Jun vs. previous $24.3bn. Exports growth quickened a tad to 23.6%y/y vs. 20.6% while imports remained strong at around 57.6%. The deficit is likely to widen as more exports restrictions were imposed in Jul even as the gold import duties take effect. Elevated oil prices around $100/bbl will not help. Oil import burden has been on a steady increase.

- **Key domestic events and issues to watch: Jul** Mfg (1 Aug), Services PMI (3 Aug); RBI policy decision (5 Aug); Jun industrial production (12 Aug); Jul CPI, trade (12 Aug); Jul WPI (16 Aug); Jul fiscal deficit (30 Aug),

- **Technical Analysis:** 1M USDINR NDF retains a bullish bias and was last at 79.30. This pair retains a bid tone with MACD bullish and stochastics still rising. The NDF seems to have formed a rising wedge. While risks are still to the upside for this pair, there is reversal risks. Support at 78.40 (21-dma) before the next at 77.90 (50-dma).

VND: SBV Moves to Counter Inflation

Forecast	3Q 2022	4Q 2022	1Q 2023	2Q 2023
USDVND	23000 (--)	22900 (--)	22900 (--)	22700 (--)

No Change to Previous Forecasts

- **Motivation for the FX View:** VND had been under pressure from its fluctuating trade balance (an accumulated U$828.3m of deficit for Jan-Jun) as well as unfavourable yield differential vis-à-vis the USD, especially in Jun. However, the latter factor seems to have shifted more recently. USDVND fell in reaction to the surge in its interbank rates after SBV started issuing T-bills in vigor since Jun to curb inflation. Overnight lending rate spiked above the 4% towards the end of Jul as 7-day T-bills issuance picked up pace. The recent withdrawal of liquidity stabilized the interest rate differential between USD and VND in the interbank market and restored strength to the VND vs. the greenback. The surge was a significant driver of recent VND appreciation as the VND overnight interbank rate was still around 0.75%, below the USD overnight interbank rate of 1.6% in the week of 27Jun to 1 Jul. The VND has been supported by other ways earlier this month including FX intervention. SBV is said to have sold USD12-13bn to stabilize the forex market. Taken together with the recent correction in the USD, USDVND has a chance of reverting towards 23000 by the end of the quarter.

- The drop in liquidity forced banks to lift the deposit rate for dong. 12M deposit has recently been raised to as high as 4.7% before easing back to levels around 3.90%. Most Vietnam banks have utilized their credit quota for the year (albeit there are talks of abandoning credit quota) and the recent hike in deposit rates could translate to higher lending rates as well (even with the interest rate subsidy scheme). That could in turn pressure Vietnam's growth into the second half.

- **Growth and Inflation Outlook:** Vietnam continues to benefit from open borders, fading omicron wave and FDI flows. However, slowing exports growth could pressure the VND as the global demand weakens. Vietnam just released its Jul data today and exports growth slowed to 8.9%y/y from previous 20.0%. Imports on the other hand, decelerated even more than expected to 3.4%y/y from previous 16.3%. Trade surplus narrowed to $21mn from $276mn in Jun. Thus far this year, Vietnam's trade balance has been meandering in and out of deficit, providing little cushion to the VND that came under pressure due to unfavourable interest rate differential. Recent signs of equity-inflows might help. Industrial production for Jul slowed a tad to 11.2%y/y from previous 11.5% but retail sales picked up pace to 42.6%y/y from previous 27.3%, boosted by the surge of tourist spending and flattered by base effects.

- CPI, on the other hand, eased to 3.14%y/y vs. previous 3.37% owed to fuel tax cuts. Transport prices eased to 15.22%y/y in Jul vs. previous 21.4%. Housing/construction materials also eased a tad to 1.1%y/y vs.

previous 1.5%. These serve as offsets to stronger price pressure in food (3.0%y/y vs. prev. 2.3%). That said, core CPI picked up pace to 2.6%y/y from previous 2.0%, likely spurring SBV's recent T-bill auction in order to curb inflation.

- Our house forecast 2022 GDP to be at +6.9%, cautioning that the risk of moderation in global growth in 2H could weigh on Vietnam's economic momentum (notwithstanding flattering base effects for 3Q) while rising price pressure crimp on consumption recovery.
- **Monetary Policy Forecast:** Even as our economist maintains view for a hike of 50bps for the refinancing rate (to 4.5%) and the discount rate (3%) in the 4Q as inflation pressure broadens, there appears to be move to withdraw liquidity in vigor most recently to counter inflation and that in turns, strengthen the VND.
- **Latest Fiscal and External Balance Outlook: Right at the start of the year, the National Assembly has approved a $15bn economic recovery package for 2022-**2023. This package includes upgrading healthcare capacity and pandemic resilience (VND60 trn), ensuring social welfare and employment (VND53.15trn), businesses and cooperatives aid (VND 110trn), infrastructure development (VND113.85trn) alongside other reforms. VAT for certain goods and services will also be lowered by 2% to 8%. Our economist expects fiscal deficit to be 4% of GDP. Public debt ratio remains modest at around 43-44% of GDP in 2022 (vs. 43.7% of GDP in 2021), well below the debt ceiling of 60% of GDP.
- **Key domestic events and issues to watch:** Aug Mfg PMI (1 Aug), Aug CPI, industrial production, trade, retail sales on 25-31 Aug

FX Forecasts

	End Q3-22	End Q4-22	End Q1-23	End Q2-23
USD/JPY	135.00	132.00	128.00	125.00
EUR/USD	1.0350	1.0500	1.0600	1.0800
GBP/USD	1.2200	1.2300	1.2400	1.2600
AUD/USD	0.7000	0.7000	0.7100	0.7200
NZD/USD	0.6400	0.6500	0.6600	0.6600
USD/CAD	1.2700	1.2600	1.2500	1.2500
USD/SGD	1.3700	1.3600	1.3500	1.3400
USD/MYR	4.4000	4.4000	4.3500	4.3000
USD/IDR	14700	14500	14400	14300
USD/THB	35.50	35.10	34.80	34.50
USD/PHP	54.50	54.00	53.50	53.00
USD/CNY	6.75	6.70	6.68	6.65
USD/CNH	6.75	6.70	6.68	6.65
USD/HKD	7.80	7.80	7.80	7.80
USD/TWD	30.00	29.80	29.60	29.50
USD/KRW	1280	1260	1240	1230
USD/INR	79.00	79.50	79.50	80.00
USD/VND	23000	22900	22900	22700
DXY Index	105.17	103.72	102.42	100.76
SGD Crosses	End Q3-22	End Q4-22	End Q1-23	End Q2-23
SGD/MYR	3.21	3.24	3.22	3.21
JPY/SGD	1.01	1.03	1.05	1.07
EUR/SGD	1.42	1.43	1.43	1.45
GBP/SGD	1.67	1.67	1.67	1.69
AUD/SGD	0.96	0.95	0.96	0.96
NZD/SGD	0.88	0.88	0.89	0.88
CAD/SGD	1.08	1.08	1.08	1.07
SGD/IDR	10730	10662	10667	10672
SGD/THB	25.91	25.81	25.78	25.75
SGD/PHP	39.78	39.71	39.63	39.55
SGD/CNY	4.93	4.93	4.95	4.96
SGD/HKD	5.69	5.74	5.78	5.82
SGD/TWD	21.90	21.91	21.93	22.01
SGD/KRW	934	926	919	918
SGD/INR	57.66	58.46	58.89	59.70
SGD/VND	16788	16838	16963	16940
	End Q3-22	End Q4-22	End Q1-23	End Q2-23
JPY/MYR	3.26	3.33	3.40	3.44
EUR/MYR	4.55	4.62	4.61	4.64
GBP/MYR	5.37	5.41	5.39	5.42
AUD/MYR	3.08	3.08	3.09	3.10
NZD/MYR	2.82	2.86	2.87	2.84
CAD/MYR	3.46	3.49	3.48	3.44
MYR/IDR	3341	3295	3310	3326
MYR/THB	8.07	7.98	8.00	8.02
MYR/PHP	12.39	12.27	12.30	12.33
MYR/CNY	1.53	1.52	1.54	1.55
MYR/HKD	1.77	1.77	1.79	1.81
MYR/TWD	6.82	6.77	6.80	6.86
MYR/KRW	291	286	285	286
MYR/INR	17.95	18.07	18.28	18.60
MYR/VND	5227	5205	5264	5279

Source: Maybank FX Research and Strategy as of 29 Jul 2022.
*These forecasts are meant to be indicative of FX trends and not meant to be point forecasts.

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