Maybank

Macro | FX Research & Strategy

Global

FX Monthly

2018, Issue 8: Taking The Lead From RMB

What Has Changed This Month?

- We revised AUD forecasts lower for 2019 on declining chance of a rate hike in 2019 as financial conditions continue to tighten and a housing market that is unlikely to bottom soon.
- We lowered NZD forecasts to account for a dovish RBNZ and softer dairy outlook.
- GBP forecasts were lowered to partially account for the risk of no deal brexit. Play up of brexit fear and PM May's leadership being challenged are potent sources of volatility for GBP. We maintain our cautious optimism on the outlook of GBP (upward trajectory) on the basis that UK will manage an orderly brexit.
- For EUR, we are cautious in the near term (4 - 6 weeks) on Italy budget concerns and potential political risks in the lead up to German Bavarian State election (14 Oct) amid negative carry environment and still-cautious market sentiment. Our forecast levels were revised slightly lower but maintain the bullish bias trajectory.
- The IDR forecast was lowered in 2H 2018 to reflect market concerns over its twin deficits amid escalating emerging market risks. The THB outlook in 3Q and 4Q 2018 was lifted due to the return of foreign interest in Thai debt and increasing expectations of BoT policy normalisation.

Our Strategies

- Trade war still dominates and Trump's eagerness to clinch a NAFTA deal is in contrast to his aggressive threat to slap more tariffs on China and his rejection of a European Union offer to remove tariff on automobiles. This has given rise to further CAD strength vs. CNH, AUD, NZD and most of AxJ complex that is RMB-linked. That said, we caution that there is more fear than optimism in the price with regards to the current US-China trade war. Any positive development on that front could trigger sharp rebounds in relevant currencies. **The reintroduction of counter cyclical adjustment factor in the RMB daily fixing protects the downside for RMB as well as AXJ but trade war still dictates the direction. The magnitude of the RMB swings could affect sentiment and the USD.**
- Policy divergence amid upward price pressures and robust economic growth generally support the USD but watch out for guidance from the Sep FOMC for any hint of moderation in the pace of tightening. We continue to favour positioning ahead for ECB-Fed policy convergence, given that Fed tightening may already be priced in while markets may potentially run the risk of "under-expecting" ECB's future policy normalisation trajectory. Bias to accumulate EUR on dips.
- Geopolitical tensions, EM vulnerabilities (Argentina, Turkey) remain in the background and should not be written off. Some AXJs (IDR, INR and PHP) may be more affected than others. Amongst AXJs, we favour THB, SGD, KRW given their current account surpluses, sound fundamentals and concomitant room for monetary policy manoeuvres.

Analysts

Saktiandi Supaat
(65) 6320 1379
saktiandi@maybank.com.sg

Christopher Wong
(65) 6320 1347
wongkl@maybank.com.sg

Fiona Lim
(65) 6320 1374
fionalim@maybank.com.sg

Leslie Tang
(65) 6320 1378
leslietang@maybank.com.sg

FX Forecast Revision for next 2 quarters

	Upward	Downward
3Q	KRW, THB, CAD, JPY	IDR
4Q	THB	EUR, GBP, NZD, MYR, IDR

Top 3 Currency Plays for September

Bias to Buy EUR on dips towards 1.14-1.15 levels for move towards 1.20

Accumulate USD, EUR against AXJ FX

Short IDR, INR, PHP vs. THB, SGD and KRW

Key Events for the Month Ahead

Date	Event
Early Sep	Details on Italy's economic and financial details to be released
6-7 Sep	US may impose next tranche of tariffs on China after deadline for comments is passed.
20 Sep	LDP Presidency Election
21 Sep	The start of Indonesia's presidential campaign
27 Sep	FOMC's Guidance on Rate Trajectory
End Sep	Italy's draft budget plan to be presented

G7 Global Overview

USD: Trade Tensions Still Centre Stage

Forecast	3Q 2018	4Q 2018	1Q 2019	2Q 2019
USD Index	94.83 (95.21)	93.50 (92.77)	92.87 (91.77)	91.69 (91.06)

Previous Forecast in Parenthesis

- **Motivation for the FX View:** The USD index fell slightly in our month ahead forecast horizon due to downward revisions as we recalibrate JPY to reflect some of the safe haven plays from the recent Turkish crisis concerns. The end year USD index rose because of revisions lower to euro (due to risk of German state elections in Oct and Turkish risk) and lower GBP (due to risk of no deal has escalated).

- USD likely to remain mixed for the remainder of 2018. Against the majors we expect to see a milder downtrend likely to remain in place for second half of 2018 but we do not rule out bouts of USD strength like what we had witnessed in the past few months. Against the emerging market and regional currencies we expect the dollar to remain strong as concerns that the ongoing trade tensions are starting to affect growth in China. If oil prices continue to rise and if there is a significant escalation of US-China trade tensions – we could see higher financial volatility and eventually some effects on global growth with impact on the USD upside being constrained and bond yields falling. In addition, any further escalation our of EM with Turkey and Brazil Oct presidential elections, some risk to EM Asia.

- However, if activity slows or labor market conditions weaken, we believe the Fed would be more likely to delay its normalization plans even if higher import prices boost short-term inflation outcomes. A more serious escalation that threatens the US recovery could lead to a pause in balance sheet normalization, though it is far too early to draw any such conclusion. For now, the committee sees fiscal stimulus as providing solid momentum in domestic activity, as well as a significant buffer against external shocks; we retain our view that the Fed will hike its policy rate one to two more times this year and three times next year. Although, for this year we now have built in a higher probability of just one more hike by the Fed.

- We do remain wary of more bouts of USD strength (as previously cautioned) that could emanate from a few scenarios - 1) trade war escalation which we think is more pronounced and sustained and will likely linger and get priced in particularly against emerging market currencies; 2) inflation pick up – price pressure is still subdued but sustained global recovery could stoke demand-pull inflation and a global bond rout; 3) markets to re-price a more aggressive tightening trajectory as the Fed becomes more hawkish under the new Chair Powell; 4) US fiscal and debt issues could lead to more issuance; 5) Italian political uncertainty from government financing issues (end-

Aug/early Sept when Italy's economic and financial plans will be presented; new public finance targets to be set by 30 Sep; draft Italy budget to be submitted to the EU for review by 15 Oct) affecting risk aversion or flight to quality flows into US and global AAA assets with better credit rating, supporting USD among others. These could in turn trigger another sell-off in global bonds and correction in riskier assets.

- However, despite the rise in US libor, widening of libor-OIS spread (partially attributable to surge in funding needs for US Treasury owing to Trump's fiscal measures) could potentially moderate when 1) US funding requirements slows and US Treasury receives tax receipts. This could lead to a less tight global funding market and typically weigh on the dollar; 2) the peak in earnings growth.

- That said we believe broader term shifts were already underway to support the case for broad USD downtrend, including (1) US tax reforms and its wider implication on deficit, debt and the USD; (2) reserve diversification away from the USD; (3) USD countercyclical play; (4) USD downtrend cycle.

- Synchronous global economic recovery, led by US, EU remains intact and it may be too soon to judge if recent inflation upticks could gather pace sustainably to warrant a shift for faster pace of rate hikes. As such we maintain our bias for broad USD downtrend and look for opportunities on USD upticks to fade into. We believe that a slightly faster pace of tightening amid healthy economic growth outlook and optimistic corporate earnings outlook should not derail the growth momentum or USD down-trend. That said the interim risk-off sentiment could remain as markets adjust from a period of policy certainty under Yellen's era to a period of policy uncertainty under a new leadership (Powell) and under the Trump administration. In particular we wish to point out that recent US data has already shown signs of deceleration in momentum – Industrial production, Philly Fed, housing starts, uni. Of Michigan sentiment, existing home sales and preliminary PMIs.

- To add further on the USD inverse relationship with global trade and economic growth is that a large share of international trade is transacted in USD even when the US itself is not the party to the transaction. This suggests that world trade volumes are driven in large part by USD. Appreciation in the USD crimps demand for US exports but also for all USD-denominated exports.
- Developments in US trade relations with China, Europe and NAFTA in coming months will be crucial. But it will be hard to forecast its schedule with certainty and its impact as the scenarios are multiple fold. In the meantime, markets are likely to price the trade war risk premium with greater certainty at the moment since June.
- **Growth and Inflation Outlook:** The second print of 2Q GDP was revised higher to 4.2%q/q growth from 4.1%. Consumer spending was revised lower to 3.8% from 4.0% though intellectual property investment was revised higher to 11% from 8.2%, lifting the headline.

- Headline CPI rose sharply in July, eating into wage gains that have barely budged in the past four months and strengthening the case for the Fed to keep raising interest rates gradually. Core CPI, which excludes food and fuel, rose 2.4% from a year earlier, the biggest advance since Sep 2008. Month on month, both the main CPI index and core rate rose 0.2% in line with expectations.

- While shelter costs gave a big boost to the results, steady consumer demand is underpinning inflation just as a trade war threatens to lift costs on a range of goods. Inflation-adjusted wages were unchanged in July from the previous month and dropped 0.2% from a year earlier. The overall CPI rose 2.9% yoy, in line with expectations while Core CPI was projected to advance 2.3 % yoy after rising 1.7 percent in June. A 0.3% jump in shelter costs accounted for about 60% of the increase in the overall CPI last month. Some items that posted big declines in June reversed course in July. Among them were hotel and motel rates, which rose 0.4% after a record decline of 4.1% in June. Airfares jumped 2.7 percent, the most since July 2013, following a 0.9 percent drop in June.

- **Monetary Policy Forecast: We maintain our outlook that further progress toward the Fed's mandate will keep the FOMC on a path of gradual policy normalization. We expect the next 25bp increase in the target funds rate to occur as early as Sep with a total of 3-4 hikes this year.** Fed funds rate (FFR) was raised by +25bps to 1.50%-1.75% at the first FOMC meeting chaired by Jerome Powell in March 2018.

- The Fed left policy unchanged on 2 Aug and stuck with a plan to gradually lift borrowing costs amid "strong" growth that suggests for a hike in September. Economic activity has been "rising at a strong rate," and unemployment "has stayed low," the Federal Open Market Committee said in the statement. While leaving rates on hold as expected, the committee repeated guidance for "further gradual increases" in its policy benchmark, lining up September's FOMC meeting for the third hike of the year. Nonetheless, President Donald Trump voiced out his unhappiness saying he wasn't "thrilled" it was raising rates. The committee described risks to the outlook as "roughly balanced," and restated that "monetary policy remains accommodative" while leaving the target range for its benchmark policy rate at 1.75 percent to 2 percent. Most Fed officials in June had projected three or four rate hikes for 2018, implying one or two more moves this year.
- There's a lot of concern that the trade negotiations and the heightened rhetoric surrounding trade negotiations might lead to slower economic activity later in the year, But while it looks likely for another rate hike in Sep, and another one in Dec, the text hasn't been written just yet on that.
- The committee noted in the statement that both headline and core inflation "remain near 2 percent." Unemployment was 4 percent in June, below the Fed's 4.5 percent estimate of the level that reflects full employment. The gradual pace of rate increases shows that officials want to see if tight labor markets can continue to draw more people into the workforce and produce higher wages, without sparking unwanted inflation.
- The minutes of the July 31-Aug FOMC meeting reaffirmed policy makers' intent to take a gradualist approach to interest-rate increases, but also

signaled a willingness to deviate from the current policy path. The Fed expressed the view that growth may slow in the second half of the year following a stellar second quarter. Policy makers cited risks to the economic outlook, including trade tensions and a slowdown in the housing market. The flat yield curve has raised concerns about a possible inversion. Still, policy makers are divided about the implications, and the recent flatness will continue to be discussed at the upcoming FOMC meeting in September.

- **More recently,** USD turned lower post-Powell's speech at Jackson Hole last Fri. He said there is no clear sign of inflation accelerating above 2%. …gradual hikes likely appropriate if growth stays strong… there doesn't seem to be elevated risks of overheating. His comments reassured markets that gradual pace of tightening remains the appropriate policy stance for now and there was no mention of a step up in the pace of normalisation.

- **Latest Fiscal and External Balance Outlook:** The "Tax Cuts and Jobs Act" (TCJA) was signed into law on Dec 22, 2017. Although the tax policy left out many controversial overhauls that have been put forth, the final reconciled bill between the House and the Senate still saw major reforms including corporate tax cuts to 21% from 35% and one-time tax repatriate of earnings and profits at 15.5% and 8% for reinvestments (further details are outlined in Appendix 1 at the end of this report). These tax reforms will have implications on broader economy, politics and the US Dollar.

- Briefly on the economic front, the TCJA is expected to increase US GDP by 0.8% in 2018, reduce marginal tax rates and increase personal consumption. Output and aggregate demand will be lifted, hence boosting government revenue, according to Tax Policy Center's (TPC) analysis on macroeconomic effects of tax reforms.

- On the tax reforms' implications on FX, it is not as clear cut. The one-time repatriation could lead to demand for USD. In the current episode that is unfolding, tax reforms is expected to widen US budget deficit to -5.4% of GDP (vs. -3.4% currently) while debt to GDP will rise to 97.5% of GDP (vs. 75% of GDP currently), according to Congressional Budget Office (CBO) estimates.

- And if history is of any guide, the current period of tax reforms (widening budget deficit and rising debt to GDP) is akin to expansionary fiscal policies and like previous periods, the USD should weaken.

- **Key domestic events and issues to watch in Sep 2018:** ISM Mfg (4 Sep); FOMC (27 Sep); Factory orders and Durable Goods Orders (6, 27 Sep), NFP (7 Sep); Trade balance (6 Jul); CPI (13 Sep); Retail Sales (14 Sep); Housing Starts (19 Sep); GDP 2QS (27 Sep); Core PCE (28 Sep); PCE Deflator (28 Sep).

- **Technical Outlook:** Our call (in last month's FX Outlook) for downside play in the DXY appears to be playing out. DXY was last seen at 94.70 levels. Bullish momentum on weekly chart is waning while stochastics is falling from overbought conditions. Price pattern on weekly charts showed an evening star (bearish reversal setup) in play. On the month chart, the candlestick for month of Aug is shaping up to be a gravestone doji. This is typically associated with a bearish reversal. We maintain our bias to lean against strength. Intra-week rebound especially around FoMC meeting is possible. An interim top is likely to have been formed at 97 levels. Key support levels at 94.60 (61.8% fibo retracement of Jun low to Aug high) and 94 levels (76.4% fibo). An extended move lower towards 93.2 (Jun low), 94.5 (200 DMA) should not be ruled out over an extended period.

EUR: Cautious Near Term but Constructive Medium Term

Forecast	3Q 2018	4Q 2018	1Q 2019	2Q 2019
EURUSD	**1.1700** (--)	**1.1900** (1.2000)	**1.2000** (1.2200)	**1.2200** (1.2300)

Previous Forecast in Parenthesis

- **Motivation for the FX View:** We are slightly **cautious in the near term** (4 – 6 weeks) on Italy budget concerns and potential political risks in the lead up to German Bavarian State election (14 Oct) amid negative carry environment and still-cautious market sentiment as trade war (EU to retaliate if US impose auto tariffs) and geopolitical concerns (in Turkey) remain. Dips towards 1.14 – 1.15 should not be ruled out especially in the event Italy and EU clash over 2019 budget plans **but that does not alter our view or signal a change in our bias to accumulate on dips.** We calibrate our forecast levels modestly lower to reflect above-mentioned risks but maintain the bullish bias trajectory across the forecast horizon.

- We continue to **retain a constructive bias in the medium term** on a combination of factors that should take time to develop: (1) monetary policy convergence at some stage possibly towards the turn of the year (ECB-Fed policy divergence likely to slow as Fed normalisation likely to have been priced in while ECB normalisation remains underpriced by markets); (2) inflation already overshooting ECB's sub-2% target; sustained price pressures above target may result in ECB needing to normalize policies ahead of schedule; (3) improved economic backdrop on sustained signs of activity momentum in Europe, looking past transitory factors in 1Q though trade war tensions still warrant caution; (4) political concerns in Germany play out after Bavaria State election (14 Oct).

- **Italy Budget Warrants Caution in the Near Term.** Local media reported that government may set 2019 deficit to GDP at -1.7 to -1.8%, much higher than the target of -0.9% set by previous administration. Given that the coalition government may push on with planned reforms that could cost more than EUR100bn (Five Star Movement is pushing for citizen income while League is proposing flat tax and to impose immigration limits) and boost spending (demand for funds), coinciding with September which is typically the busiest month for new bond sales in Europe, Italian bond yields could remain supported or even rise further. EUR's negative correlation with Italian yields has strengthened since Mar this year. **Further rise in Italian bond yields may add to further downward pressure on EUR**. Some dates to keep in mind include **end-Aug/early Sept when Italy's economic and financial plans will be presented; new public finance targets to be set by 30 Sep; draft Italy budget to be submitted to the EU for review by 15 Oct. The final budget has to be ratified by Italian parliament by end-2018. EUR may see some volatility around those dates mentioned above.**

- **Concerns with Turkey Have Implications for EU Banks.** The rapid decline in the Turkish Lira (-40% at one point between end-Jul and 13 Aug 2018 vs. USD), triggered by Trump's tweets (11 Aug) to double import tariffs on Turkish steel and aluminum to 50% and 20%, respectively, following US sanctions against 2 Turkish Ministers (10 Aug) over Turkey's detention of an American pastor Andrew Brunson (due to espionage and terrorism allegations) may have stabilized for now. But the **rapid decline in TRY has led to concerns over EU banks' exposure to Turkey.** According to BIS report (end-Jun 2018), Spanish banks have the highest exposure to Turkish borrowers at US$83bn, French banks are owed US$38bn, UK banks are owed US$19bn, Italy and German banks are each owed US$17bn. Concerns remain over Turkish borrowers' ability to meet debt obligation or if European banks stop rolling over the loans resulting in defaults and this could eventually impact European banks' stability. **Turkey President Erdogan is scheduled to visit Berlin on 28 Sep. Talks of financial aid on the agenda list.**

- **Turkey's problem transcends into political ones for Europe**. It is important to note that Europe relies on Turkey to contain the flow of migrants trying to reach Europe. If Turkey economy heads for a hard landing, the EU could face the risk of migrants resurging again as Turks may prioritize other economic issues. Already the number of migrants trying to reach Europe from Turkey has risen to 14,000 YTD Jul 2017, up from 9,152 in the same period last year. This could complicate the political situation in Europe as the rise in populist parties (far right) have been using the migration issue (amongst others) to win votes in recent elections. Recall how Germany's Alternative for Germany (AfD) party won 12.6% of the votes in German Federal election and entered the Bundestag with 94 seats and most recently in Mar 2018, anti-immigrant League and anti-establishment 5 Star Movement (5SM) formed the coalition government in Italy. Oct 14 brings German Bavarian State election, German Chancellor Merkel is at risk of losing powers if Christian Social Union (or CSU, the sister party to Merkel's CDU party and coalition partner) loses the election to right wing AfD. **Rise in populism undermines the Euro-club; heightens political uncertainty and this may pose downside pressure on the EUR**.

- **Growth and Inflation Outlook: Euro-area economy showed signs of stabilisation with 2Q GDP being revised higher** to +0.4% q/q (vs. +0.3% as reported in advanced estimates). This follows a weak 1Q GDP (+0.3% q/q) amid temporary factors due to cold weather conditions, influenza outbreak in Germany, Easter holidays and industrial strikes.

The moderation was also due to capacity constraints. ECB had highlighted that capacity utilisation and backlogs/supply delivery times in the capital goods sector stand at all-time highs while in the construction sector, an increasing number of firms are indicating that a shortage of labour is limiting their production. Unemployment rate has also been falling; last at 8.3% in Jun (lowest level since Dec-2008). Euro-area recovery enters into 21 consecutive quarters of growth.

- The last ECB macroeconomic projection in Jun 2018 report shows that projections for 2018 growth has been revised lower to 2.1% (vs. 2.4% in Mar-2018 projection) while projections for 2019 and 2020 stay unchanged at 1.9% and 1.7%, respectively (as of last). Downward adjustments were made to private consumption and investments. Nonetheless ECB still expects growth to remain solid over the next few quarters, in line with elevated levels of business and consumer sentiment though real GDP is projected to trend gradually lower towards 1.7% in 2020 as tailwind gradually fades.

- **Euro-area inflation continues to inch higher to 2.1% y/y in Jul (vs. 2% in Jun).** This was largely due to higher energy prices, services and food, alcohol & tobacco. The **increase validated our call for inflation to rise towards ECB's sub-2% target** on ECB's monetary policy measures, higher energy prices and rising wage growth (labor cost rose to 2% y/y in 1Q 2018, highest level since 2013 and is expected to rise further amid tightening of labor market). The rise in headline CPI above 2% in Jul was also the first time since 2012. Core CPI held steady at 1.1% y/y for Jul. Last ECB macroeconomic projection (Jun 2018) shows inflation is projected to inch higher to 1.7% for 2018 and 2019 from 1.4% (Mar projection). ECB's trajectory for inflation is expected to remain flat at 1.7% for forecast horizon from 2018 – 2020 as declining profile of energy inflation offsets a gradual strengthening in non-energy and food inflation.

- **Monetary Policy Forecast: We expect ECB to keep monetary policy stance status quo** at the upcoming ECB GC meeting (13th Sep) following their move in Jun on timeline of APP reduction and forward guidance on rates. **ECB is expected to keep rates unchanged till Autumn 2019 (around Oct-Nov) but we see risk that the ECB may need to move earlier than expected** (relative to ECB's timeline) should (1) inflation data, in particular core CPI continues to surprise to the upside while (2) growth and activity data continues to hold up. With global oil production still constrained despite planned OPEC production increases, oil prices could still stay supported and that has already tipped Euro-area inflation to overshoot ECB's inflation target of under-2%. Headline CPI was last at 2.1% y/y (Jul). A weaker currency (YTD decline of 10% at one point vs. USD) could result in higher prices via the **import price channel**. This should add on to further upside pressure for Euro-area CPI. **We do not rule out the possibility that ECB could proceed with baby steps to normalize deposit rate first** (currently at -0.4%) at some stage.

- At the last ECB meeting (26 Jul), ECB's Draghi offered no new insights to forward guidance. He reiterated that "key ECB interest rates to remain at their present levels at least through the summer of 2019, and in any case for as long as necessary to ensure the continued sustained convergence of inflation to levels that are below, but close to, 2% over the medium term". He seemed to exhibit more confidence in the growth assessment and prospect for sustainable convergence of inflation to ECB's target. On inflation, Draghi said that "domestic cost pressures are strengthening and broadening amid high levels of capacity utilization and tightening labor markets". Although he did repeat his warning that increased protectionism around the world could hurt euro-area exports and undermine growth recovery in euro-zone, he seemed less concerned as he played up recent Trump-Juncker efforts to ease trade tensions. He added that the ECB has not done further analysis and had not updated its estimate of the impact of protectionism on Euro-area growth… direct impact of the tariffs implemented are limited but full trade war would create an entirely different climate.

- Taking stock of ECB action in Jun, ECB announced that APP at monthly pace of €30 billion will continue till Sep 2018 and will be **reduced to €15 billion per month between Oct and Dec 2018 and then APP will end thereafter.** Policy rates (Main Refinancing operations, deposit facility and marginal lending facility were kept on hold at 0%, -0.4% and 0.25%, respectively). ECB added that rates will be kept at current levels at least through the summer of 2019 (Jun – Sep) depending on incoming data.

- **Latest Fiscal and External Balance Outlook:** Euro area's current account surplus rose modestly to EUR24bn in Jun (up from EUR22bn in May). This was due to the rise in goods surplus while services surplus was largely unchanged. Current account surplus to GDP was last seen at 3.6%, for the 12-months to Jun.

- The EA19 government deficit narrowed to -0.9% of GDP in end-2017 (vs. -1% of GDP in 3Q). This is the narrowest level since 2008. Breakdown showed German government recorded +1.3% surplus of GDP while deficits were seen for France, Italy and Spain at -2.6%, -2.3% and -3.1 of GDP, respectively.

- **Key domestic events and issues to watch:** Aug Mfg PMI (3 Sep); Jul PPI (4 Sep); Aug services PMI, Jul retail sales (5 Sep); 2Q final GDP (7 Sep); Sep ZEW survey (11 Sep); Jul IP (12 Sep); ECB GC meeting (13 Sep); Jul trade, 2Q labor cost (14 Sep); Aug CPI (17 Sep); Jul current account, Sep construction output (19 Sep); Sep prelim PMIs (21 Sep); Sep consumer confidence (27 Sep); Sep CPI estimate; Turkey President Erdogan to visit Berlin with financial aid item likely to be on the agenda (28 Sep).

- **Technical Outlook:** EUR traded a month of 2 distinct halves – softer in early part amid geopolitical tensions between US-Turkey before the recovery into month-end. Last seen at 1.17 levels. Bearish momentum on weekly chart is waning while stochastics is showing signs of turning higher from oversold conditions. Bullish divergence on weekly chart also appears to be in the making. Bias for further upside but gains only likely to accelerate on clean break above 1.1710 (38.2% fibo retracement of 2017 low to 2018 high), 1.1760 (100 DMA). Extension of the rally towards 1.1860 levels should not be ruled out. Failure to push through key resistance decisively could reignite retracement pressures again. Support at 1.1620 (50 DMA), 1.1540 (21 DMA). Accumulate on dips preferred.

GBP: Cautious Optimism

Forecast	3Q 2018	4Q 2018	1Q 2019	2Q 2019
GBPUSD	1.3200 (--)	1.3400 (1.3700)	1.3200 (1.3400)	1.3500 (1.3700)

Previous Forecast in Parenthesis

- **Motivation for the FX View**: We **maintain our cautious optimism on the outlook of GBP** on the basis that UK will manage an orderly brexit (i.e. to strike a deal with EU while PM May remains in power, cabinet divide narrows). While **brexit and PM May's leadership are undoubtedly the key sources of volatility** (uncertainty) for GBP, we believe **pessimism on no-deal may have been front-loaded onto GBP** (which explains the >3% depreciation at one point to sub-1.27 before the recovery). This can also be seen from CFTC leveraged GBP-short positions at 15-month high. We argue that any positive progress towards an agreement on Brexit could build on recent momentum and result in further GBP shorts rushing for the exit. This could force an abrupt move higher in GBP and the market bias may even be shifted to rebuild GBP long, from sell GBP-on-rallies. The **recovery may even be amplified in the environment of renewed USD weakness**. However we acknowledge the risks of no-deal brexit as details on EU's offer for customized union remain scanty at this stage. Play-up of brexit fear (no deal or PM May's leadership being challenged) especially when deadline is approaching is a potent source of volatility for GBP. As such we calibrate our forecast lower to partially take into consideration those risk factors but maintain the forecast trajectory. The slight kink lower in 1Q forecast is to take into account uncertainty associated with the formal exit of UK (29 Mar 2019, 11pm GMT). Our base case remains for an eleventh-hour deal with EU and a no-deal brexit will be averted.

- **Development on Brexit negotiations remain fluid (often more negative than positive) but the recent one (29 Aug) was a surprising positive twist.** EU Chief Negotiator Barnier said ***"we are prepared to offer a partnership with Britain such as has never been with any other third country"***. This caught market by surprise and record GBP-shorts were inevitably caught off guard. GBP-shorts squeeze saw an abrupt move higher in the GBP (+1.2% overnight vs. USD). Though it may be premature to jump the gun on smooth brexit as details remain far and few in between, recent comments from Barnier suggest that a deadlock on negotiations might be broken and this somewhat reconciles with UK Brexit secretary Raab's earlier comments that the *UK and EU have reached agreement on about 80% of issues relating to Brexit. And some of the issues unresolved are Irish border issue. He insisted that he was "still confident" of reaching an issue with the EU ahead of brexit departure on 29th Mar*

2019 and said that the failure of talks was unlikely. EU's Barnier further noted (30 Aug) that a solution to Ireland/Northern Ireland border problem in brexit negotiations is possible. Taken together these developments are positive and should further help to unwind excessive pessimism on brexit outlook for the time being.

- There are some key dates over the next 2 months to keep in view: (1) Conservative Party Conference (30 Sep – 3 Oct 2018) – watch out for risk of PM May's leadership being challenged and/or release of Brexit blue print; (2) EU Summit (18 – 19 Oct) was a deadline at first for getting brexit issues ironed out but timeline for full Brexit Summit is believed to be shifted out to November. Nonetheless discussion on Brexit will still go on in Oct, with French President Macron aiming to push for a "new alliance" between EU and Britain. It was reported that a new Continental structure could see 'concentric circles' with the EU and Euro at its core and the UK in a second ring. Shift in deadline is welcomed as this leaves room for more details to be ironed out.

- **Downside Risks to Our Outlook: (1) no-deal brexit** (akin to hard brexit scenario) concerns if re-emerged will dampen confidence on GBP bulls. Recall that comments from UK International Trade Secretary Liam Fox (5 Aug) that there is a 60% chance that of no-deal brexit and BoE Carney's comments (3 Aug) that Britain leaving the European Union without a deal is "uncomfortably high" at the moment weighed on GBP; (2) Delay in finalising a deal heightens uncertainty (raises fears of disorderly brexit), dampen investor/business confidence and expose GBP to further vulnerabilities; (3) growing divide within PM May's cabinet leading to PM May's leadership being challenged is also another source of volatility for GBP. Recall that brexiters are working on the blue print which will allow for possible Canadian-style free trade agreement but only if EU backs down on demands over Irish Border. The paper is expected to be published in Sep and is expected to have support of 60 to 80 Conservative MPs – could amplify the growing divide and derail EU-UK negotiation efforts (GBP-negative); (4) slowing economic momentum including deceleration in wage growth, PMIs, IP will weigh on GBP

- Into the medium term, we maintain our bias that GBP could trade higher. GBP is perceived to be undervalued from both historical and fundamentals perspective (our BEER model puts GBP at 1.40 – 1.45). The 20% or so depreciation in the Brexit-aftermath (from Jun to Oct 2016) should help the UK economy to rebalance and grow sustainably over time - current account deficit should narrow, exports should become more competitive and tourism and education receipts should pick up further. We hold to our belief that UK should be able to manage the exit, transform itself into a global marketplace and continue to attract capital (longer-term).
    - Past experience of UK leaving the ERM back in 1992 saw a period of consolidation (for a few years) at historical lows for GBP, before the eventual move higher in the following years, where GBP TWI traded above 100-levels in 1998 (from the lows of 80 in 1993-1996) due to buoyant demand fueled by rapid

growth of wealth, credit and money. If history is a guide (assuming UK manages the transition well and takes the opportunity to correct its imbalances), its currency may start climbing higher.

- **Growth and Inflation Outlook:** 2Q GDP rebounded to +0.4% q/q (vs. +0.2% in 1Q). The rebound was attributed to the construction and services sectors (strongest quarterly expansion since end-2016 and accounts for nearly 80% of UK economy) thanks to hot weather following the cold snap in 1Q (which weighed on growth and activity). Manufacturing sector, on the other hand, continue to contract. Activity data such as retail sales grew faster in Jul (+0.7% m/m vs. +0.2% expected vs. -0.5% in Jun), helped by hot weather and World Cup (boost to food sales). Actual 2Q growth and activity data validated our earlier call that there are signs that momentum could pick up again.

- As of the last Quarterly Inflation report (2 Aug), BoE MPC expects GDP to grow by around 1.75% per year on average over the forecast period. Net trade and business investment could continue to support UK activity while consumption grows in line with the subdued pace of real incomes. The MPC continues to judge that the UK economy currently has a very limited degree of slack. Unemployment is low (5.2%) and is projected to fall a little further. In the MPC's central projection, therefore, a small margin of excess demand emerges by late 2019 and this could feed through into higher growth in domestic costs than has been seen over recent years.

- **UK headline inflation rose to 2.5% y/y in Jul** (vs. 2.4% in Jun). This was the first increase since Nov 2017 and the level remains well above BoE's 2% target. Transport tickets, fuel and computer games (highly volatile) led price gains while decline in prices of clothing, footwear and financial services offset some of the upside price pressures. Core inflation was steady at 1.9% (unchanged from prior month). Modest rise in CPI and steady wage growth suggest household income growth is at risk of being subdued and that may impact consumption going forward. That said wage growth could re-accelerate as public sector salary cap may be lifted. Times reported that PM May is planning to announce that state-employed staff including teachers, doctors and police officers could get a pay rise this year as government's pay cap (at 1%) could be lifted.

- **Monetary Policy Forecast: We expect BoE to keep policy rate unchanged at 0.75% at its upcoming MPC meeting on 13th Sep.** Monetary policy stance is likely to remain status quo for as long as over the next 9 - 12 months before the next rate hike as uncertainty over Brexit takes precedence. OIS implied suggests the next rate hike could take place in May-2019 at the earliest (50.7% probability). BoE's forward guidance shows another 2 hikes expected to end-2020. We remain watchful of inflationary pressures as tight labor market could generate domestic price pressures. Sustained rebound in CPI towards 3% again could change our view on BoE policy status quo (to front-load rate hikes). The size of BoE balance sheet (GBP435bn) is also expected to stay unchanged until policy rate reached 1.5% (this was discussed and agreed at the Jun BoE MPC meeting).

- At the last BoE meeting on 2 Aug, MPC raised policy rate by 25bps to 0.75%, as expected. The unanimous decision was unexpected. BoE's Carney said that a modest tightening of monetary policy is appropriate with domestically generated inflation pressures building and the prospect of excess demand emerging. He added that if macroeconomic forecasts proved right, the BoE would have to increase rates further albeit gradually. On Brexit, he shared that some brexit outcomes would warrant a cut in key rate.

- **Latest Fiscal and External Balance Outlook:** UK's current account deficit narrowed further to -3.4% of GDP for 1Q 2018 (from -3.8% of GDP in 4Q 2017). This represents the 4th consecutive quarters of improvement and is the narrowest level since 2011, helped by narrowing of trade (in particular goods exports was strong) and primary income deficits. The Office of Budget Responsibility has projected current account deficit to be about -4.4% of GDP in 2021, rather than -2% of GDP initially forecasted in Mar 2017. Foreign inflow of capital is needed to fund the deficit. But if Brexit uncertainty takes a turn for the worse or persists for longer, investor/business sentiment can be adversely impacted. Slowdown in foreign inflows could worsen the situation and the GBP could come under pressure as a result.

- UK recorded the biggest Jul budget surplus in 18 years, with surplus at GBP2bn, much higher than GBP1.1bn expected. Improvement was due to larger tax receipts. According to Office of National Statistics, the 2018-19 deficit is running more than one-third below the year earlier levels as government's budget benefit from record employment and reasonable consumer spending. Progress suggests the Chancellor Hammond is on course to undershoot the forecast deficit of 1.8% of GDP. Though Chancellor Hammond intends to run a budget surplus by mid-2020s, he did suggest he could announce more spending in his Budget speech in Nov.

- **Key domestic events and issues to watch:** Aug Mfg PMI (3 Sep); Aug Construction PMI (4 Sep); Aug services PMI (5 Sep); Jul trade, IP, construction output, Jul GDP (10 Sep); Jul labor report (11 Sep); BoE MPC meeting (13 Sep); Aug CPI, PPI (19 Sep); Aug retail sales (20 Sep); Aug public finances (21 Sep); 2Q GDP (28 Sep).

- **Technical Outlook:** GBP traded a month of two halves: fell to a low of 1.2662 (15 Aug) amid fear of no-deal brexit before the recovery into end-Aug on hopes of a customized deal (offered by EU). Pair was last seen at 1.3010 levels. Bearish momentum on weekly chart is waning while stochastics shows signs of rising from oversold conditions. Price pattern shows a *falling wedge pattern forming – this is typically associated with bullish reversal. Rebound need to clear above the area* of resistance at 1.3040 (50 DMA) - 1.3070 (23.6% fibo retracement of Apr high to Aug low) for further gains to accelerate. Extension of the rally towards 1.3290 (100 DMA), 1.3310 (38.2% fibo) should not be ruled out. Failure to push above could nullify the rebound momentum and the pair could ease off to trade a lower range of 1.26 – 1.30. Support seen at 1.2860 (21 DMA).

AUD: Stretched

Forecast	3Q 2018	4Q 2018	1Q 2019	2Q 2019
AUDUSD	0.74 (--)	0.75 (--)	0.73 (0.78)	0.72 (0.80)

No Change to Previous Forecast

- **Motivation for the FX View:** Australia just had a change of Prime Minister in a span of a month from Malcolm Turnbull to Scott Morrison. The proposal of the energy bill that was initially meant to include the legislation of the carbon emission target in the National Energy Guarantee was deemed to have broad support in the coalition. However, the drop in carbon emission targets to appease the conservative group in his coalition exposed the weakness in Turnbull's leadership. On 21st Aug, Home Affairs Minister (and hardline conservative) Peter Dutton challenged Turnbull's leadership and failed by an uncomfortable slim margin. Then came a string of resignations in the cabinet including the Trade Minister and Finance Minister and then a letter of petition, with 43 signatories for Turnbull to call for another leadership vote which he did not stand as a candidate. It was down to Julie Bishop, Scott Morrison and Peter Dutton. AUDUSD spiraled below the 0.73-figure before some recovery on the win by Scott Morrison.

- We had indicated in our recent note that domestic politics could present opportunities to buy the AUD as trade war risks remain mostly frontloaded and there is still much more fear than optimism in the price. The trade war presents a more fundamental threat to the Australian economy rather than politics and thus a stronger and more lasting driver of AUD. Should trade tension ease in the next few weeks, AUDUSD could head higher and break out of the downward sloping trend channel that started early this year. Insofar, China has matched the past two tranches of tariffs, dollar for dollar. The US has to decide on the tariff by the end of Aug and the tariff could be imposed as early as Sep. The value of Chinese imports targeted this time is four times as much as what has been slapped on so far (U$50bn) and could have more significant impact on inflation and growth. That translates to further downside risks to the AUD. However, should there be any signs of delay or postponement on the decision; we anticipate a short squeeze to the AUD.

- We are less sanguine on the prospect of a rate hike now given the impact of the drought in the Eastern part of Australia. To put things into perspective, the value of the agricultural output is around the same as the value of iron ore and a quarter of it comes from the New South Wales that is now entirely in drought as confirmed by the officials. Rural goods make up around 15% of total exports of goods for Australia. The deterioration in current account is unlikely to show up in 2Q though as net exports of goods for Apr-Jun have been positive and they are likely to be a contributor to the headline GDP as well. Expect the fall in metal prices, impact of trade war and this drought to show up in 3Q numbers.

- We anticipate that the yield differential between the 10y AU bonds and US treasuries are likely to be more negative as the US continue to keep the rate hike trajectory on track. We see upside risks to the Fed rate hike trajectory in next year and greater risk of RBA not doing much in the same time horizon. That compels us to soften our AUDUSD forecast trajectory though we maintain a bullish medium term (3 month view) of the pair based on some optimism on the US-China trade front that could see tensions ease, potential for China's growth to stabilize as well as stretched positioning that leaves the AUD bears vulnerable to short squeezes.

- **Growth and Inflation Outlook:**

  - **As of last release, CPI** quickened to 2.1%y/y from previous 1.9%. The average of the trimmed mean and median was at 1.9%. Seasonally adjusted, the headline actually firmed to 2.2%y/y from previous 2.0%. Food inflation softened in the quarter but this was outweighed by the acceleration in transportation, recreation and education. Looking at the breakdown for goods and services, the CPI for goods seem to be on the uptick, possibly buoyed by the rise in energy prices as well as the cheaper AUD. With the drought affecting the agriculture output of the country, there could also be some upside risks to food inflation.

  - **Growth** prospect is rather decent for 2Q, notwithstanding the external headwinds posed by the trade war and the drought in parts of Eastern Australia. In fact, the growth of exports and imports of goods have accelerated into double digit in May and Jun. Growth of exports receipts were underpinned by stronger overseas sales of metal ores and minerals. Retail sales, a proxy of household consumption, surprised to the upside in Jun as well, up 1.2%q/q in 2Q from previous 0.2%. A stronger GDP print is likely for 2Q but that would not be enough for RBA to raise rates. Notwithstanding the political upheaval at home, growth could continue at a decent pace but acceleration is unlikely. NAB survey reveals that business conditions have been on the decline from its peaks in earlier part of this year. Unemployment growth actually contracted while full time hiring growth (seasonally adjusted) bounced from recent lows, improving the prospect of higher wages but only in time.

  - Even as RBA did not raise cash target rate, financial conditions have been tightening for Australian residents and corporates with requirements for more collateral and APRA restrictions. Residential property price increase has been softening since the mid of last year with prices of houses in Sydney in contractions. Property price in Perth and Darwin also remained in contraction but the former seems have bottomed and could see modest gains in the next few months. 3M BBSW has stabilized at a rather elevated level around 1.95% after rising above 2.1% at one point in Jun. Because of the declines in home prices for quite a number of cities, housing affordability has improved for the third consecutive quarter. The housing affordability index rose to 71.3 in 2Q from 70.6 in the prior quarter. Historical data showed that the last time the average weighted residential property price bottomed was in 3Q 2016 when the housing affordability index hit a high of 74.5. That also coincided with the plunge in short term rates. In that year, 3M BBSW fell to a low of 1.7150%. With policy normalization still ongoing in the US, expect interbank interest rates to remain elevated and that could continue to crimp on the real estate market along with the stricter APRA supervision. Smaller lenders have raised rates for home loan borrowers and that could increase the interest payment to disposable income which has been rising from lows of 2015. Westpac, one of the bigger Australia banks, joined the gang in lifting mortgage rates by 14bps, citing higher funding costs. That could further exacerbate home loan growth. Dwelling finance commitment for housing has been in contraction for the past 7 consecutive months and the -6.7%y/y fall in Jun (latest data) is the steepest yet. That could, in turn, keep interest payments high for households and dampen consumption.

- **Monetary Policy Forecast:** We continue to expect RBA to keep cash target rates unchanged and we see an increasing possibility of the central bank standing pat in 2019. With the CPI still close to the lower bound of the 2-3% inflation target and plenty of uncertainty in the horizon amid the current trade war, there is very little motivation for the central bank to move rates at this point. AUD has been under pressure against the USD, trapped in a downward sloping trend channel. We note that RBA seems to be comfortable with the AUD at this point and even stated its expectations for terms of trade to "stay at a relatively high level". That said, RBA Lowe had said that the next move is still likely a hike rather than a cut, acknowledging the strong hiring momentum and potential for wage growth and inflation to head higher in the coming months as the output gap turns positive.

- However, that rate hike might not come at all as wage growth remains subdued and as Westpac announced an out-of-cycle hike for its mortgage rates by 14bps. There are speculations that other big lenders might hop on the band wagon even though some have lowered their mortgage rates earlier this month. Regardless, this underscores the fact that tighter financial condition could leave less room for RBA to lift rates at all.

- **Latest Fiscal and External Balance Outlook:** Budget deficit is forecast to be A$14.5bn for 2018-19. The government projects a surplus of A$2.2bn in 2019-20, in line with market expectation. The outstanding Australian government debt is projected to be at A$533bn by the end of June this year and at A$561bn at the end of Jun next year. Thus net debt is forecast to peak at 18.6% of GDP in 2017-18. In response, S&P held on to their negative watch on Australia, citing global trade tensions among risks for Australia.

- Following the recent by-elections in which the Coalition lost all three seats it contested to the Australian Federal Labor party, Australia had a change of Prime Minister from Malcolm Turnbull to Scott Morrison.

Eyes are on whether he is able to unify the coalition better than his predecessor in order for the government to function better. The next half-Senate election must be held between August 4, 2018 and May 18, 2019. The House of Representatives election date, on the other hand, can be set any time up until November 2, 2019. Labor has been able to garner significant support but both governments are rather conscious of the impact that their policies have on cost of living and cost of doing business with the coalition proposals a tad more corporate-friendly with a proposal for corporate tax cuts. However, markets are unlikely to react unfavorably to a change in government. Hence, impact on AUD from a Labour win or Coalition or Liberal win is likely to be rather neutral. A hung parliament occurs when none of the political party could get an outright majority and that requires securing 76 seats in the 150 members of the House of Representative. That could see a greater chance of some volatility at that point but hung parliaments do not last long and that suggests that pressure on AUD will also be temporary.

- **Key domestic events and issues to watch:** Retail sales on 3rd Sep; BoP Current account balance for 2Q, net exports of GDP for 2Q and RBA meeting on 4th; 2Q GDP on 5th; Trade on 6th; home loans on 7th; NAB business survey on 11th; labour report on 13th; Minutes of the meeting on 18th.

- **Technical Outlook:** AUDUSD last printed 0.7280. The number of net non-commercial futures positions for the AUD is still near its lowest seen since 2015. We do not see this as sustainable but recovery is not expected to be sharp as well given trade war risks. Eye the 0.7370-level, the 50-dma as well as the upper bound of the trend channel that this pair has to break. Daily chart shows a bullish divergence between the price action and MACD forest. Key support at 0.7140. AUDUSD tends to move sharply higher when it reaches that level.

NZD: Still Lack Catalysts to Take Flight

Forecast	3Q 2018	4Q 2018	1Q 2019	2Q 2019
NZDUSD	0.6700 (--)	0.6800 (0.7000)	0.7000 (0.7100)	0.7200 (--)

Previous Forecast in Parenthesis

- **Motivation for the FX View:** We still hold to our view that **NZD lacks fundamental catalysts to drive it meaningfully higher** as monetary policy divergence between Fed and RBNZ persists, dairy prices remain soft (Fonterra cuts milk payout by 0.25 to $6.75/kg amid rising production in North America, Europe while demand in Asia and Middle-East slows) while external environment remains unfavorable (trade war tensions between US-China remain and NZD is highly sensitivity to movements in CNH and risk sentiment). That said we believe the downside for the NZD may be limited towards 0.66, as implied by our fair value model projection and CFTC short positioning at historical levels. We do not rule out NZD forming at interim bottom around 0.6600 levels and we look for opportunity to buy on dips, looking for short term rebound towards 0.6850 levels (next 2 – 4 weeks). Current spot at 0.6660.

- Our fair value model shows that NZD spot is close to testing our model's lower bound of 0.66 levels (1 standard deviation of fair value estimate of 0.73 levels). Historically NZD spot has hardly trade outside of our model's lower bound and this implies that downside could be limited, barring external shocks (i.e. full-blown trade war, re-escalation of geopolitical tensions, etc.). In addition NZD net short position is near historical records. This adds to our bias that NZD downside may be limited from current levels.

- But at the same time, **limited room for downside and a potential mild rebound do not imply that the NZD is ready to take flight**. This is so because NZD lacks fundamental drivers from within to rise meaningfully: NZ 2Q growth is expected to slow (data to be released on 20th Sep); falling dairy prices have yet to turn around and the RBNZ is dovish and not turning neutral or hawkish anytime soon. In particular, RBNZ even suggested that chances of rate cut have increased amid weaker growth… RBNZ in no hurry to raise rates… and the decline in the NZD is welcomed. To add to the list of domestic drivers, the external environment (of trade war between US and China as well as geopolitical tensions in US) is not helping with sentiment. In light of the above development, we calibrate our FX forecast for 4Q and 1Q modestly lower but continue to maintain the upward sloping trajectory in our forecast.

- **Growth and Inflation Outlook:** The last MPS (9th Aug) noted that recent weakness in GDP growth is expected to persist in the near term, with 2Q GDP likely to dip further to 2.3% (**data to be released on 20 Sep**) before recovering to 2.5% in 3Q (where data would be released on 20 Dec). Growth over the medium term is expected to recover in 2019 (towards 3.5% RBNZ projection), supported by fiscal stimulus (government's Families Package), export growth and monetary stimulus. On inflation outlook, **MPC projected a delayed return in inflation to RBNZ's target range mid-point to 1Q 2021** (from late 2020 as projected in May MPS). RBNZ expects CPI to increase in 2019, supported by non-tradables inflation while tradables inflation is expected to increase (amid fuel excise duties) but remain below its historical average.

- Growth momentum in NZ moderated for 1Q (0.5% q/q vs 0.6% prior). This was due to pullback in infrastructure construction as reconstruction efforts in the aftermath of Kaikoura earthquake eases while most other sectors of the economy held up well. Manufacturing PMI moderated further to 51.2 in Jul (vs. 52.7 in prior month) while services PMI rose to 55.1 in Jul from its 5.5 year low of 52.7 in Jun. Given that services sector account for 2/3 of NZ GDP, the rebound helps to ease some worries for 2Q GDP.

- **PPI rose further in 2Q** (input up 1% vs. 0.6%; output up 0.9% vs. 0.2% q/q). This is the 9th consecutive quarters of gain amid rise in fuel prices. Headline CPI rose to 1.5% y/y in for 2Q, up from 18-month low of 1.1% in 1Q. The rise was due to higher prices for household energy (subcomponents including electricity, gas and solid fuels), transport (higher petrol prices), food, actual rentals and dwelling insurance. Both tradable and non-tradable inflation rose in 2Q. Headline CPI now comes close to the middle of RBNZ's inflation target range of 1 - 3%. Our internal projection also shows inflation possibly rising towards RBNZ's median target of 2% in early 2019. RBNZ quarterly survey of inflation expectation for 3Q also showed a modest rise to 2.04% y/y. Inflation expectations tend to have implication on inflation, OCR and the NZD.

- **Monetary Policy Forecast:** We still expect RBNZ to maintain OCR on hold at 1.75% at its next meeting (27th Sept) and for the rest of the year amid cautious inflation outlook, signs of moderation in global activity, ongoing trade war concerns between US and China as well as RBNZ's explicit guidance to pursue policy status quo. Though RBNZ did caution that the next move could be a cut instead of a hike, we do not subscribe to the "cut" bias as growth, activity and inflation outlook remain strong and do not warrant a rate cut. In fact we expect inflation to pick up, owing to fiscal impulse, higher prices via import price channel given the depreciation in NZD, higher oil prices and minimum wage increases. Our expectations is still for a rate hike in 2H 2019, much earlier than RBNZ's projection of end-2020.

- At the last MPC meeting (9 Aug), RBNZ MPC kept OCR unchanged at 1.75% as widely expected but RBNZ surprisingly **turned more dovish than expected with Governor Orr saying that OCR is expected to remain at record low till 4Q 2020 on weaker growth and risk that a slump in business confidence could hamper investment** (note that this is a shift to a later date from early 2020 as earlier projected in May MPS). Accompanying MPS also projected a delayed return in inflation to RBNZ's target range mid-point to 1Q 2021 (from late 2020 as projected in May MPS). **RBNZ Asst. Governor and Chief Economist McDermott said that chances of rate cut have increased amid weaker growth…** and he expects growth to re-accelerate in 3Q.. if not "that means we've got something wrong and we are going to have to reconsider where we're at. RBNZ expects 2Q GDP to dip further to 2.3% (data to be released on 20 Sep) before recovering to 2.5% in 3Q (where data would be released on 20 Dec). **He emphasized that markets need to understand that a rate increase was "off the table for the foreseeable future".** In RBNZ's press conference (9 Aug), **Governor Orr said that he was very pleased with the movement in the exchange rate** over the recent quarters saying that the **NZD was very close to fair value.**

- In an interview with Bloomberg at Jackson Hole (22 Aug), **RBNZ's ORR reiterated that the central bank has not ruled out cutting interest rates if needed to achieve inflation target** but he also added that output needs to fall in order to take such a step in the near term. He said that **RBNZ is in no hurry to raise rates…** and that puts RBNZ out of sync with the rest of the world and "that's fine… that will feed through the exchange rate and will support the NZ economy". He also **re-emphasized that he welcomed the decline in the NZD, saying that it supports NZ's export-oriented economy.** He further added that he is **"very pleased with the fact that the exchange rate reflected nothing other than inflation differentials between us (NZ) and our trading partners".**

- **Latest Fiscal and External Balance Outlook:** NZ government surplus is projected to be $3.1bn this year rising to $7.3bn by 2020/21. Finance Minister Grant Robertson also shared that net debt at $62.5bn is relatively low compared to international trends and at 22.1% of GDP. It is projected to fall to 20.8% of GDP for the full year and 20% of GDP over the next 5 years.

- NZ unadjusted current account turned to surplus in 1Q ($182m vs. deficit of -27.5bn in 4Q), helped by services balance as tourism receipts remain robust. In seasonally adjusted terms, annual deficit widened to -2.8% of GDP, driven by goods balance on higher import demand and higher oil prices while exports was lower amid softer dairy prices. 2Q data is scheduled for released on 19 Sep.

- **Key domestic events and issues to watch:** 2Q ToT (3 Sep); 2Q Mfg activity (10 Sep); Aug food prices (13 Sep); Aug Mfg PMI (14 Sep); Aug services PMI (17 Sep); 2Q current account (19 Sep); 2Q GDP (20 Sep); Aug trade, activity outlook, business confidence (26 Sep); RBNZ MPC meeting (27 Sep); Sep consumer confidence, Aug building permits (28 Sep). GDT trade auctions take place on 4 and 18 Sep.

- **Technical Outlook:** Our call in last month's FX outlook to rebound was overly optimistic. NZD's losses accelerated on the break of support at 0.67 levels. Pair traded a low of 0.6545 (15 Aug) amid dovish RBNZ and tensions in geopolitics and US-China trade disputes. Last seen at 0.6650 levels. Mild bullish momentum on daily chart is showing signs of waning while stochastics shows signs of turning lower from overbought conditions. Further downside pressure possible intra-day. Support at 0.6620, 0.6540 levels. Resistance at 0.6660 (21 DMA), 0.6710 (76.4% fibo retracement of Aug high to low), 0.68 levels.

JPY: Bears' Influence Is Waning

Forecast	3Q 2018	4Q 2018	1Q 2019	2Q 2019
USDJPY	113.00 (115.00)	112.00 (--)	111.00 (--)	111.00 (--)

Previous Forecasts in Parenthesis

- **Motivation for the FX View:** JPY is among the best performing currencies within the G10. So far in Aug, the JPY has gained nearly 0.7% against the USD. JPY strength in Aug though was not what we had expected. The JPY had failed to weaken due to (1) a USD pullback on optimism of easing global trade tensions, and (2) demand for safe-haven proxy plays including the demand for JPY due to spill-over effects from the Turkish crisis. The JPY had appreciated to 109.78 against USD, though it has since come off to trade closer to the 112-levels at the point of writing as concerns over Turkey and Sino-US trade war eased. Meanwhile, widening yield differentials between 10Y UST and JGB amid ongoing BOJ ultra-loose monetary policy (including holding the 10Y JGB yield around the 0% levels) should continue to put downside pressure on the JPY. Consequently, we have tweaked our forecast for the USDJPY lower in 3Q to reflect recent market developments but maintain the pair's downward trajectory for our forecast horizon.

- Since BOJ governor Kuroda's comments on "reversal rate" theory in Nov 2017, i.e., that the BOJ's policy of keeping interest rates low were harming the profitability of commercial banks and harming their ability to lend. This has been interpreted by market as a signal of a tighter policy. However, the BOJ governor walked back on those comments, suggesting that the reversal rate was unnecessary in the Japanese context as the BOJ had already made changes to its monetary framework. At the same time, market also looked at the BOJ's purchases of bonds and ETFs with every reduction seen as a sign of asset tapering. These reductions were taken as signals of "stealth tapering" by the central bank. We do not agree with this interpretation as we view such moves by the BOJ as technical adjustments, purchasing JGBs and ETFs as and when necessary to achieve its policy goals. Thus we expect the USDJPY to remain supported ahead as we do not foresee the BOJ removing its ultra-loose monetary policy anytime soon.

- Putting downside pressure on the JPY is the commitment of the BOJ to maintain its ultra-loose monetary policy until inflation is stable around the 2%-levels. Reinforcing this commitment was the BOJ's introduction of a forward guidance in the same vein as the US Fed with expectations of keeping low rates "for extended period of time". This forward guidance signals that policy normalisation is unlikely within our forecast horizon and should continue to flush out hold-outs of short-USDJPY positions. This should keep the USDJPY supported.

- Despite the move by the BOJ to allow the 10Y JGB yield to fluctuate in a wider range around the zero percent level, we do not expect the yield to climb significantly higher in the near term. This is because of the BOJ's preference for a measured and orderly climb in 10Y JGB yield. To guard against speculative activities, the central bank has shown its willingness to offer to buy unlimited amount of bond to temper rapid increases in the yield. This should cap 10Y JGB yield moves higher. As for 10Y UST yield, it is still expected to climb higher, despite its recent pullback, on Fed rate hike expectations. This should widen the gap between 10Y UST and JGB and weigh on the JPY in the month ahead.

- Recent data suggests that foreign inflows into equities and debt have reversed in Aug and further outflows could be supportive of the JPY. Previously, foreign inflows into Japanese assets had led to a concomitant dip in the JPY due to hedging activities. As we had previously noted, foreign investors hedge their Japanese asset purchases against further JPY depreciation by short-selling the JPY, thus putting downside pressure on the JPY. When foreign investors sell Japanese assets though, they unwind their short-JPY positions, putting upside pressure on the JPY. With sentiments possibly souring due to the stronger JPY that could crimp corporate earnings and concerns over Sino-US trade tensions could spur further sell-offs in

Japanese assets in Sep and keep the JPY supported. This should cap upmoves in the USDJPY in the month ahead and keep the pair hovering around the 113-levels by end-3Q.

- Though we are penciling some weakness in the JPY in Sep, we cannot rule out further downside risk to our USDJPY forecast should Sino-US trade tensions re-escalate as Trump plays to his political base ahead of the mid-term elections in Nov. The re-emergence of trade tension between China and US is likely to weigh on the JPY. This is because the currency is not viewed as a safe-haven proxy play in this situation as Japan itself is vulnerable to any fall-out from the trade disruption between the two world's largest economies. At the same time, Japan is also a target of US protectionist measures with Japanese steel and aluminum and motor vehicle exports under threat of US tariffs, and rising US protectionist tendencies are likely to weigh on the JPY.

- On the flip-side, the Turkish situation could blow up again should the US continue its economic pressure on the economy. The re-emergence of Turkish crisis could lift the JPY higher on demand for safe-haven assets and put downside risks to our USDJPY forecast. Similarly, should signs emerge that support for PM Abe in the LDP presidential election on 20 Sep is wavering, domestic political risks could emerge and spur demand for the safe-haven assets and weigh on the USDJPY.

- We continue to expect a moderation in USD strength against the majors, including the JPY, going into 2019. A milder downtrend for the USD is expected towards the end of the year though we cannot rule out bouts of USD strength. We maintain our view that the USD is bound for a broad pullback due to (1) rising US deficit and debt from US tax reforms; (2) reserve diversification away from USD; (3) USD countercyclical play; and (4) broad USD downtrend cycle. Thus we expect some strengthening of the JPY towards the end of the year.

- Recent CFTC data suggests that market is positioning for reduced USD strength. While market continues to be net short-JPY, i.e., expecting weakness in the JPY since May, these bets have been coming off. Investors have reduced their short-JPY bets to 101,522 contracts as of the week of 21 Aug, while increasing their long-JPY bets to 54,116 contracts. Given expectations for reduced USD strength ahead, we could see further reduction in net short-JPY positioning that could limit downside pressure on the JPY.

- Downside pressure on the JPY is also likely to come from importer demand for foreign currency (usually USD). Healthy economic growth and improvement in wages have seen healthy import demand (up 7.7% y/y in 1H 2018). With economic growth expected to remain healthy (BOJ expects real GDP to expand by 1.5% in FY2018), import demand should remain healthy, and increased import demand should weigh on the JPY. On the other hand, anecdotal evidence suggests exporters could park their export earnings abroad on expectations of further JPY weakness and repatriate earnings only during quarter-end for book-keeping purposes.

- At the same time, 4Q tends to be a seasonally strong month for the JPY vs. the USD, and there is the potential for the JPY to rebound in the last three months of the year. This is likely to mitigate the downside pressure on the JPY and lift the JPY higher by end-4Q.

- In addition, the current level of the JPY is fundamentally undervalued by about 1.8% and this suggests some room for the JPY to depreciate mildly towards our fair value estimate. Our BEER fair value model which takes into account differentials in REER, terms of trade, GDP per capita and interest rate; net foreign assets (as % of GDP); ratio of total trade to GDP; productivity; and government consumption, estimates USDJPY at 109.

- Against the backdrop of safe-haven demand due to the Turkish crisis and softer USD due to easing Sino-US trade tensions, we have revised lower our forecasts for the USDJPY in 3Q. We now expect the USDJPY end 3Q around 113 instead of the 115 we had previously expected. We however maintain our forecast and trajectory for the USDJPY, penciling in some pullback in USD strength to allow the USDJPY to ease and end the year around 112. In 1H 2019, we look for the pair to hover around the 111.

- **Growth and Inflation Outlook:** The economy rebounded in 2Q, bouncing back by +0.5% q/q sa from -0.2% in 1Q. The rebound was attributable to the stronger personal consumption (2Q: +0.7% vs. Disappointing though was net exports, which was a drag on GDP in 2Q, subtracting 0.1%-pt from growth. This rebound gives us confidence that growth should remain supported for the rest of 2018. The government's FY2017 supplementary spending package of around JPY2tn as well as preparations in the run-up to the 2020 Olympics in Tokyo should bolster economic growth for the whole of 2018. The BOJ expects full-year growth to come in around 1.5% (previously 1.6%) for FY2018 and kept its FY2019 forecast unchanged at 0.8%.

- Hopes for a stronger uptick in inflation was dashed in Jul. Headline inflation did accelerate by 0.9% y/y in Jul vs. Jun's +0.7%, lifted by firmer food prices (Jul: +1.3% vs. Jun: +0.4%) and transport costs (Jul: +1.5% vs. Jun: +1.3%). Core (headline less, while core-core (headline less fresh food and energy) inflation was unchanged at +0.8% as higher energy costs failed to deliver the expected boost to consumer prices. With inflation only grinding higher slowly, any talk of normalisation remains premature. We expect the BOJ to continue its pursuit of its ultra-loose monetary policy until its 2% inflation target is achieved. The BOJ expects core inflation to come in at 1.1% in 2018, and then to accelerate to 1.5% and 1.6% (excluding the effects of the consumption tax hike) in FY2019 and FY2020 respectively.

- **Monetary Policy Forecast:** There was no policy meeting in Aug but focus remains on the tweaks made at its 31 Jul meeting. The policy balance rate was maintained at -0.1% and the 10-year JGB yield target at around zero percent. Yield of 10Y JGB spiked as market tested the upper limits of the range that the 10-year bond yield was allowed to fluctuate. BOJ operations though capped the yield's climb to maintain an orderly pace of advance in the 10Y yield. Since then, the 10Y JGB yield has hovered around the 0.10%-levels.

- Other minor tweaks to its policy included shifting purchases of exchange-traded funds (ETFs) towards assets linked to the Topix from the Nikkei and allowing greater flexibility in bond operations and asset purchases to ensure sustainability of the current framework. Forward guidance for policy rates was also introduced with extremely low levels of short- and long-term interest rates to remain for an extended period of time. At the same time, the central bank also allowed the 10-year JGB yield some leeway to move up and down depending on developments in economic activity and prices. Meanwhile, the BOJ reduced the amount to which negative interest rate applies from JPY10tn in an acknowledgement to the profitability of commercial banks.

- According to BOJ Governor Kuroda, these minor changes to the policy framework were to improve the sustainability of exiting policy over the long haul. He also warned that the central bank would add further easing measures if required in response to critics who claimed that the tweaks were stealth tapering. We doubt that the policy tweaks will end speculation on BOJ exit plans, though it should halt JPY-bulls' attempts to push the JPY higher for now.

- **Latest Fiscal and External Balance Outlook:** For the financial year ended on 31 Mar, the total tax revenue collected amounted to JPY58.8tn, up JPY3.3tn from a year ago. This reflected the strong economic activity amid a weak JPY. A breakdown showed that individual income, corporate income and consumption taxes collected were JPY18.9tn (up JPY1.3tn), JPY23tn (up JY1.7tn) and JPY17.5tn (up JPY0.3tn) respectively. Accordingly, the amounted collected was higher than the initial fiscal budget for 2017 by JPY1.1tn.

- The current account (CA) surplus narrowed mildly to JPY1.18tn in Jun from JPY1.94tn in May, weighed by the smaller surplus in the primary income of JPY0.59tn vs. May's JPY2.40tn even as the balance in the goods and services rebounded to a surplus of JPY0.65tn in Jun from May's deficit of JPY0.26tn. The financial account surplus also narrowed to JPY0.62tn in Jun from JPY3.32tn in May due to the decline in both portfolio investment of JPY1.73tn (May: +JPY1.95tn) and "Other investment" segment (Jun: -0.05tn vs. May's: +0.21tn). Consequently, the overall balance of payments (BoP) surplus narrowed to JPY1.24tn in Jun from JPY6.64tn in May.

- **Key domestic events and issues to watch:** Eyed closely in Sep will be the final estimates for 2Q18 GDP and Aug CPI on 10 and 21 Sep respectively followed by BOJ policy meeting on 18-19 Sep. At the same time, BOJ will release minutes of its Jul policy meeting and summary of opinions for the Sep meeting on 25 and 28 Sep respectively. We also have BOJ Board Member Kataoka speaking in Yokohama on 6 Sep and BOJ Governor Kuroda in Osaka on 25 Sep. On the political front, the ruling LDP will hold elections for its presidency on 20 Sep, where the winner will automatically become prime minister. JGB auctions in Sep: 10-year (5 Sep), 30-year (11 Sep), 5-year (13 Sep), 1-year (18 Sep) and 20-year (20 Sep).

- **Technical Outlook:** USDJPY drifted lower for the month of Aug. Last seen at 111 levels. Momentum and oscillator indicators are not providing a clear bias. But price pattern shows a potential cup and handle pattern appears to be in the making. This is typically associated a bullish continuation pattern. Immediate resistance at

111.60 (50% fibo retracement of 2017 high to 2018 low) before 113.20 (61.8%). A break above these levels could point to further upside towards 115.30 levels. Support at 110 levels.

RMB: PBoC Supports But Trade War Still Matters

Forecast	3Q 2018	4Q 2018	1Q 2019	2Q 2019
USDCNY	6.75 (--)	6.72 (--)	6.65 (--)	6.62 (--)
USDCNH	6.75 (6.77)	6.72 (--)	6.65 (--)	6.62 (--)

No Change from Previous Forecasts

- **Motivation for the FX View:** The announcement by PBoC to reintroduce the counter cyclical factor coincided with the announcement by Powell that the Fed is unlikely to raise the rate hike trajectory as there is not much evidence that the US economy is overheating. That triggered broad USD offers since (24 Aug) and we anticipate a period of USD weakness as market players take the opportunity to flush out stretched positioning, especially against the USD. As USD continues to depreciate broadly, the uncertainty between the US-China trade standoff still keeps the USDCNH supported on dips. The development on that front still dictates where the USDCNH swings next although we view more fear than optimism in the price of the pair. In addition, the reinstatement of the CCAF suggests that the authorities remain concern about the yuan amid EM contagion risks, potential EUR weakness and any RRR cut that could be required in reaction to sluggish activity. Hence, expect moves lower in USDCNH to also be limited.

- **Developments of The War At Hand :**

  – At the end of the last mid-level trade talk between US Treasury Under Secretary David Malpass and Chinese Commerce Vice Minister Wang Shouwen, there was little breakthrough and the tariff on U$16bn of imports kicked into effect on both sides. While both parties have committed to keep communication open, they also raised the possibility that further negotiations could be postponed until after the mid-term elections. Eyes are on whether the US will impose up to 25% tariff on U$200bn of Chinese imports that would ratchet up the trade war in Sep. A decision is supposed to be made by around the time this report is published (31 Aug). While the lack of progress at the US-China trade talks has dampened hopes of tensions easing between the two nations and some form of a trade deal forged with Mexico could be perceived as US strengthening its position against China, we see a risk of a delay in the next tranche of tariffs given the sheer impact and ramification that it has on the global economy and inflation including that of the US. The National Retail Federation urged the USTR to reject the tariffs on U$200bn of Chinese goods with a study that found tariffs on China-origin furniture and travel goods would cost American consumers nearly U$6bn a year. This could also affect the fiscal deficit for the US - Trump had to spend U$4.7bn in the first round of aid to compensate for market losses caused by Chinese tariffs in a trade war. Earlier, the Trump administration promise up to U$12bn in support to the farmers. The US had been rather quick to impose the first U$50bn in order to make its threat on the next U$200bn look more credible. However, **the lengthening of the tariff hearing on this upcoming round of tariffs suggest more caution and there was also an overwhelming demand from companies to testify. We anticipate more caution on the next move. Any signs of delay could be taken as a positive signal and push the USDCNH towards our 3Q forecast of 6.75.**

- <u>Addressing Domestic Challenges:</u>
  - Industrial production slowed significantly in the past few months. With China facing headwinds on the trade front, a series of fiscal measures were unleashed to cushion growth amid the uncertainty. That includes a plan to spend CNY1.35tn (U$199bn) for local government to spend on infrastructure with focus on transport, gas and telecommunications as well as plans to cut taxes, provide VAT rebates to encourage research and manufacturing in “advanced” and “modern service providers”. This came after the State Council’s assurance that China’s proactive fiscal policy to be “more proactive”. There were also news that the State Planners have said that large-scale unemployment is “not allowed” amid the trade friction. While these have certainly allowed some improvement in the RMB depreciation expectations, another RRR cut may still be necessary and that is negative for the RMB. We expect these growth boosting measures to feed into the economy and data to show some improvement at the turn of the quarter. At that point, RMB should also strengthen in line with the fundamentals.

- **With the trade war led by a rather trigger-friendly Commander-in-Chief, we acknowledge that RMB is still rather vulnerable to the downside. Should Trump and his troop of China hawks impose tariff on another U$200bn of Chinese imports, it is highly likely for USDCNH to test higher along USDCNY. USDCNH could head towards its recent high of 6.9586 towards the key psychological 7**. However, we maintain our view that more fear than optimism is in the price. Lows against the USD are likely to have been established for the year. Further yuan weakness could trigger risk dampening the stock market further and that seems to a risk that China officials take seriously. A long-drawn war could affect the base voters of Trump and that is also why the CCAF has been reinstated to support the RMB in the short-term and it should work to limit downsides. With USD positioning still rather stretched, we anticipate that there could be more room for USDCNH and USDCNY to head lower and hold our view for USDCNY to arrive around 6.75 by end-Sep.

- **Growth and inflation outlook**: Industrial production surprised to the downside again for Jul, staying at 6.0%y/y. FAI (urban) dropped to just 5.5%y/y from previous 6.0% while retail sales also softened to 8.8%y/y from previous 9.0%. Activity data slumped in a month when the trade war with the US officially started with the first tranche of tariffs imposed. New yuan loans came off to CNY1.45trn, albeit still above the expected CNY1.275trn. The more recently released industrial profits slowed to 16.2%y/y from previous 20.0%. Much of the growth is contributed by SOEs. Private companies posted negative profits for the 9th consecutive months, and the fall in Jul is the steepest for the year. The trend in the PMI-mfg numbers for large companies as well as SMEs continues to extend lower in Jul. The start of the trade war likely had dampened the sentiments of purchasing managers then.

- To have a cue on whether policy measures work on supporting the real economy, we eye the next slew of data for a better idea. Trade surplus narrowed in the month as the import bill swelled to 20.9%y/y from previous 6.0%. Significant increase was seen in technological products and costs of machinery that were targeted by the first tranche of tariffs that came into effect on 6 Jul. Trade surplus narrowed to CNY176.96bn from previous CNY260.89bn. Inflation also ticked higher to 2.1%y/y from previous 1.9%, firmer than expectations. While food inflation remained rather subdued at around 0.5%y/y, price pressure increase in the transport & telecom subcomponent and residence.

- Easing measures so far have been rather targeted on infrastructure projects, improving credit accessibility for small and medium businesses, agriculture and exporters. Eyes on the next set of credit data for a sense of whether banks have been lending to boost the economy.

- Money supply M2 accelerated to 8.5%y/y from 8.0%. Breakdown of the Jul aggregate financing data revealed that shadow financing continues to be on the decline including entrusted loan, trust loan and banker's acceptance bill. Traditional lending bounced to 12.9%y/y in Jul from previous 12.7%. This comes after a number of regulatory tightening on wealth management products this year. RRR cuts insofar have been targeted and are deemed to be supportive of traditional bank lendings as the authorities attempt to shift financing back to the traditional route.

- **Monetary Policy Forecast:** Even with the series of fiscal measures, we still do not rule out another RRR cut. However, a broad-based one is less likely than a targeted one like the ones we have seen in Apr and Jul this year. Policy mix has shifted towards more growth cushioning though credit growth via shadow financing is unlikely to revisit their heydays again.

- The average OMO rates weighted by outstanding of securities came off as well as 3M shibor, underscoring the flush liquidity conditions onshore. That has also depressed the onshore forward curve for the

USDCNY as opposed to the 12M USDCNH forward points which have rebounded. The restriction put in place by the authorities to bar offshore interbank lending and deposits via the free trade zone restricts the flow of yuan offshore, basically tightening capital outflow channel. Another RRR cut could come in Oct should activity continue to be lackluster.

- **Latest Fiscal and External Balance Outlook:** China had set out a target earlier this year, to reduce its budget deficit target from 3% of GDP to 2.6%, lower than speculated 2.9%. However, with the plentitude of fiscal measures undertaken recently, the budget deficit to GDP ratio could rise as China cushions growth in the face of a trade war. This is especially in light of only modest growth expected for this year.

- **Key domestic events and issues to watch:** NBS PMI numbers for Jul due on 31st Aug, Caixin PMI on 3^{rdt}; FX Reserves on the 7th; trade data on the 8th; inflation on the 10th; Money supply, new yuan loans, aggregate financing on 10-15th; surveyed jobless rate, activity data on the 14th; new home prices on the 15th; FX net settlement (clients) on the 20^{h}; industrial profits on the 27th.

- **Technical Outlook:** Downsides are compelling for the USDCNH on the weekly chart as momentum indicators turns lower. Last seen around 6.8460. We cannot rule out upticks but bears are getting fatigue from its recent run-up. Our bias is to the downside with support at 6.7890-level before the next at 6.6830.

KRW: Cautious Recovery

Forecast	3Q 2018	4Q 2018	1Q 2019	2Q 2019
USDKRW	**1120** (1130)	**1110** (--)	**1100** (--)	**1090** (--)

Previous Forecasts in Parenthesis

- **Motivation for the FX View:** Our call in the last FX Monthly for signs of stabilisation in Aug (after the 7% sell-off vs. USD in Jun - Jul), with room for gains in the KRW towards 1,100 levels within a trading range of 1100 – 1145 was close to being met. The pair traded a high of 1137 (16 Aug) before easing off to 1107 (29 Aug). For the month ahead, we see a lower range of 1090 – 1135, with bias to lean against USDKRW strength. Newly announced fiscal stimulus (yet to be approved) to support the creation of jobs, minimum wage and nurture innovative growth, rising bets for BoK to tighten in 4Q, eligibility for "targeted relief" from steel quotas imposed by US, relative stability in RMB, Powell's recent speech at Jackson Hole (suggesting that Fed maintain its gradual pace of monetary tightening) as well as more favourable geopolitical outlook on the Korean peninsula (Moon-Kim Summit expected in Sep) should support the case for KRW stability or even modest strength. We calibrate the 3Q forecast lower to reflect the above optimism. Forecast trajectory and levels for the horizon remains intact.

- Government has proposed to spend a record KRW471tn ($420bn) for 2018. This is the largest budget increase in 10 years and is aimed at aimed at creating jobs, raising minimum wage and boosting economic recovery momentum. Budget will be submitted to the National Assembly by early Sep but may face challenge getting approved as President Moon's party only hold 129 out of the 299 seats in parliament.

- That said caution remains warranted on 2 fronts: lingering trade war concerns between US and China as well as geopolitical tensions between US and Turkey. Any re-escalation could negate the appetite for CNH and risk sentiment, respectively and reignite weakness in the KRW. The sensitivity of KRW to changes in CNH and changes in stock market (proxied by MSCI World Index) remains high at 0.98 and 0.40x, with a positive correlation of 0.52 and 0.70, respectively. This suggests that a sell-off in both equities and CNH would see KRW much worse off. Nonetheless, the reverse is also true - recovery in CNH and firmer equities should support gains in KRW.

- **Growth and Inflation Outlook: South Korea's economic growth momentum moderated in 2Q (+0.7% q/q vs. +1% in 1Q), owing to slower pace of expansion in private consumption and investments** (in particular facilities and construction investments). On y/y basis, 2Q GDP was up 2.9%, from 2.8% in 1Q. Exports of goods and services rose by +0.8% q/q (vs. +4.4% in 1Q) led by increase in exports of semiconductor and petroleum & coal products. Breakdown of the exports component however saw a divergence in performance with services export rising due to rebound in Chinese tourist arrivals (after ban was lifted) while goods exports slowed. On the production side, manufacturing, utilities and services rose while construction declined.

- **BoK has recently revised lower (by 0.1ppts) its FY GDP forecast for 2018 and 2019** to 2.9% and 2.8%, from 3% and 2.9%, respectively). And the decision was to reflect latest economic trend - sluggish job creation, slower exports amid escalating trade war tensions between US and China.

- **Inflation held steady at +1.5% y/y in Jul (unchanged since May)** as higher prices from food, beverages & tobacco, clothing/footwear, transport were offset by health and communication. Prices of agricultural products including vegetables rose amid higher temperature (due to summer heat wave). Core CPI eased modestly to 1.1% y/y in Jul, from 1.2% in Jun. In a separate research report by BoK, Korea's true inflation is said to rise 2.2% in 2Q, up from 1.6% in 1Q. True inflation is defined as excluding the so-called "administered prices", which is controlled by the government for policy purposes and it applies to 30 service items including utilities and government subsidized welfare sectors (such as medicine, education, etc.). The report said "administered prices kept a slower pace of rise compared to consumer prices, bringing down the rise of CPI. As such there is a divergence in the true CPI and the commonly referred to headline CPI (which includes those goods and services controlled by the government). To put things in perspective, true CPI rose by about 1.9%

since 2016, nearing the BoK's 2% inflation target. Point to note was there was also 1 rate hike last year. And 2Q 2018 true CPI does suggest that target has been breached.

- **Monetary Policy Forecast**: There is no MPC meeting scheduled in Sep. We still see risk of a 25bps rate hike in 4Q 2018, possibly as early as at the next meeting on 18th Oct if demand-induced price pressures picks up pace. Minimum wage could increase by 16% this year, its largest magnitude of increase since 2001. Wage pass-through is expected to have positive impact on consumption spending, growth and lead to inflationary pressures. To add, the **presence of a dissenter is significant for BoK policy decision.** At the 12 Jul BoK MPC meeting, Lee Il-houng, a distinguished Economist was the lone dissenter in the 7-member board. Recall back in 2017, he was also the lone dissenter at the Oct 2017 meeting which subsequently paved the way for the first rate hike in 6 years the following month in Nov 2017. Moreover BoK still see the economy growing at its potential rate… the growth and inflation trajectories aren't all that different from paths seen in April. In addition at the 27th Jul parliamentary session, BoK Governor Lee said that it will be necessary to adjust the level of accommodative monetary stance in an attempt to secure more policy leeway to deal with future business cycles if the economy stays on a good cycle. We believe these comments are strong hints that the BoK is preparing markets for rate hike soon.

- At the last MPC meeting on 31st Aug, BoK kept policy rate unchanged at 1.5%, as widely expected. Like in the last MPC meeting on 12 Jul, there was one dissenter - Lee Il-houng, a distinguished Economist remains the lone dissenter in the 7-member board. Accompanying statement noted that economic growth is expected to be generally consistent with the path projected in Jul. BoK noted that employment conditions in Korea have become more sluggish; inflation will pick up and gradually approach the target level of 2% but may be lower than previous forecasts; uncertainties are rising in global markets more than expected due to protectionist policies.

- **Latest Fiscal and External Balance Outlook:** Current account surplus widened to $7.38bn in Jun, up from the same period last year (+$6.94bn). The rebound was mainly due to increased goods surplus and lower deficit in services account. This marks the 76th consecutive month of current account surplus which started in Mar-2012.

- Korea's national debt is projected to reach KRW700tn this year (38.6% of GDP) and to rise to KRW740tn next year. The level remains relatively low vs. other major developed economies.

- The government has proposed to spend a record KRW471tn ($420bn) for 2018. This is the largest budget increase in 10 years and is aimed at aimed at creating jobs, raising minimum wage and boosting economic recovery momentum. The government also plans to issue up to KRW97.8bn of bonds in 2019; of the total 57.1tn will be used for redemption payments and the remainder will be net issuance. The 2019 budget will be submitted to the National Assembly by early Sep but may face challenge getting approved as President Moon's party only hold 129 out of the 299 seats in parliament. Moreover President Moon's expansionary fiscal policy is under pressure as unemployment had worsened and income inequality has widened. Government data showed that the number of jobs increased by only 5,000 from a year earlier in July, compared with 106,000 new jobs added to the local market in the previous month. It marked the slowest job growth since January 2010. Unemployment rate also rose to 3.8% in Jul (vs. 3.6% in 1Q 2018).

- **Key domestic events and issues to watch:** S. Korea releases Aug exports, CPI, (1 Sep); Aug PMI Mfg (3 Sep); 2Q final GDP, Aug CPI (4 Sep); Aug FX reserves (5 Sep); Jul current account (6 Sep); Aug unemployment rate (12 Sep); Aug PPI and first 20 days of trade data (21 Sep); Sep consumer confidence (28 Sep).

- **Technical Outlook:** USDKRW traded lower into the end of month. Last seen at 1113 levels. Near term pressure may be skewed to the upside. Resistance at 1122 (21, 50 DMAs), 1140 (Jul-Aug high). But signs are building up for a drift lower. Bullish momentum on weekly chart is waning while stochastics is falling from near-overbought conditions. We are biased to lean against strength looking for further downside play. Support at 1102 (50% fibo retracement of Jun low to Jul high), 1094 (61.8% fibo).

SGD: Casting A Weary Eye On Trade Disruptions

Forecast	3Q 2018	4Q 2018	1Q 2019	2Q 2019
USDSGD	1.3750 (--)	1.3650 (--)	1.3650 (1.3600)	1.3600 (1.3550)

Previous Forecasts in Parenthesis

- **Motivation for the FX View:** Our outlook for the SGD till the end of the year has not changed. We continue to expect upside risks to lift the USDSGD higher to 1.3750 by end-3Q before easing off towards 1.3650 by end-2018 as trade tensions is expected to ease by then once the US mid-term elections are over in Nov.

- For now, the threat of trade disruption from tit-for-tat tariffs imposed by US and China on each other should continue to weigh on the SGD. This is unsurprisingly given that Singapore is acutely reliant on trade. Already there are signs that the synchronised export-led recovery is waning. At the same time, the electronic cycle is losing steam and is nearing its end. Thus, trade disruption from protectionist measures is likely to exacerbate this slowdown in the global supply-chain and weigh on the Singapore economy. This in turn should drag the SGD lower. Should the trade disputes escalate into a trade war, there could be further downside risks to our SGD outlook.

- While there could be some tapering in USD strength ahead, there is unlikely to be any sharp reversal as healthy US growth and expectations of firmer inflation increases the probability of a further

Fed rate hike in 4Q. This is likely to lead to broad gains in the USD against the AXJs as higher yields and still strong corporate earnings still favour US assets vs. emerging Asian assets. Firmer USD is likely to remain a drag on the SGD and keep the USDSGD elevated.

- Aug-Sep tends to be seasonally weak months for the SGD vs. the USD, and this could suggest there could be more downside to the SGD in the month. In six out of the past 10 years, the SGD has shown weakness against the USD in Sep. We could thus see the USDSGD climb higher from current levels towards the 1.3750-levels by end-3Q.

- We do not expect the SGD to weaken significantly from current levels. The SGD could possibly find support from the CNY and EUR, both of which are expected to firm going into 2019. Dissipating Sino-US trade tensions as well as measures to support domestic growth should keep the CNY buoyant ahead. As for the EUR, the convergence of monetary policy between the EU and the US should be supportive of the EUR. Given the increasing sensitivity of CNY and EUR moves on the SGD, a softer USDCNY and a firmer EURUSD should be put upside pressure on the SGD and cap upside to the USDSGD.

- Underscoring the SGD is its still healthy domestic fundamentals. The healthy budget surpluses of the past few years provide fiscal space for the government to accelerate its infrastructure programme, including development of Changi Airport Terminal 5 and the redevelopment and rejuvenation of the Jurong Lake District, should it become necessary. Aside from the country's ample fiscal space, its triple-A status and persistent high balance of payments surpluses are also supportive of the SGD. These should provide incentive for investors to remain vested in Singapore assets, including the SGD. Taken together, the healthy macroeconomic fundamentals should keep the SGD supported and keep the USDSGD on its gradual downward trajectory going into 2019.

- We have however made tweaks to our 2019 forecast to reflect expectations for a more moderate reduction in USD strength next year after the exceptional year for the USD in 2018. We now expect the USDSGD to end 1Q 2019 at around 1.3650 (from 1.3600 previously) and then ease to around 1.3600-levels by end-2Q 2019 (from 1.3550 previously).

- **Growth and Inflation Outlook:** Final print for 2Q GDP saw growth come in weaker-than-expected on the back of slower services growth. This is even though manufacturing growth was upgraded from the preliminary print. GDP rose by 3.9% y/y in 2Q18 vs. advance estimates of +3.8%, and easing from +4.5% in 1Q. Services growth underperformed expectations, rising by just +2.8% y/y in 2Q vs. advance estimates of +3.4% - the slowest pace in four quarters. Manufacturing on the other hand accelerated by +10.2% y/y (adv. est.: +8.6%), bolstered by electronics, biomedical manufacturing and transport engineering. Construction remained a drag on growth, contracting by -4.6% compared to advance estimates of -4.4% and vs. 1Q's -5.2% due to dip in public sector activities.

- Manufacturing is expected to slow in 2H as prospects of a Sino-US trade war weigh on trade and investment. In addition, the electronic cycle is also on the wane. At the same time, recent harsh property measures could hurt property-related business services and construction outlook. Consequently, our economic team maintains its real GDP forecast at +3.5% for 2018 because of concerns over escalating trade tensions. It also kept its 2019 growth forecast unchanged at +2.7%. MTI also maintains it GDP forecast at 2.5-3.5% for 2018. The MTI also highlighted two main downside risks to growth ahead: (1) escalating trade tensions between US and China/EU, and (2) faster-than-expected normalisation of monetary policy in the US if inflation surprises on the upside.

- Headline inflation rose 0.6% y/y in Jul – the same pace as in Jun – weighed by the slide in car prices and COE premiums (-36%). At the same time, accommodation cost slipped lower (-3%), while services inflation eased to +1.5% in Jul vs. +1.7% in Jun. Core inflation (excludes private road transport and accommodation costs) accelerated to a new four-year high in Jul, rising to +1.9% y/y vs. +1.7%. This was due to the steep increase in electricity and gas prices (+12.7% y/y in Jul vs. +3.7% in Jun).

- Looking ahead, core inflation should taper off in 4Q as electricity tariffs ease somewhat in 4Q after they are expected to remain elevated until Sep. Oil prices should also come off slightly as reflected in the slide in Brent oil prices since Jun. Headline inflation is expected to remain subdued going forward as COE premiums should remain soft. Note also that a trade war is deflationary and will contain inflationary pressures for the rest of 2018. Consequently, our economic team maintains its headline and core inflation forecast at +0.7% and +1.7% respectively for 2018. MAS continues to look for core inflation to rise gradually for the rest of 2018, averaging at the upper half of its 1-2% forecast range for 2018. Similarly, it expects headline inflation to come in at the upper half of its 0-1% forecast range for 2018.

- **Monetary Policy Forecast**: After pursuing an accommodative policy the past two-and-a-half years, the MAS began the process of policy normalisation at its semi-annual policy meeting on 13 Apr. At that meeting, the MAS shifted to a ‘slight appreciation bias’ for the SGD NEER by increasing slightly the slope of the policy band. The level at which the band is centred and the width of the policy band was left unchanged though. This move by MAS was underpinned by the monetary authority’s expectations that core inflation will rise gradually on the back of improving labour market and on moderate rise in oil and food commodity prices amid the steady expansion path of the economy. As estimates for key parameters are not revealed by MAS, we have assumed that the slope of the SGD NEER policy band to be at the stronger end of the 0-1% range at 0.75% p.a. This should allow for a stronger SGD on a trade-weighted basis to mitigate the expected climb in core inflation in both 2018 and 2019.

- As discussed above, core inflation is accelerating and this has lifted market expectations that this could lead to another round of tightening by the MAS in Oct. Nevertheless, further tightening by the MAS is not our base assumption. We continue to expect the MAS to maintain its current ‘slight appreciation bias’ at its next policy meeting in Oct. This is because inflation should remain within the upper half of the MAS' 1-2% inflation forecast for this year and no overshoot of the MAS inflation goals is expected.

- The USDSGD had climbed to a new 2018 high at 1.3819 on 15 Aug amid USD strength on rising Sino-US trade tensions. With the easing of trade tensions, the pair has eased off to hover around the 1.3650-levels at the point of writing. As for domestic interest rates, the 3-month SOR has roller-coasted in Aug before hovering around the 1.63-levels at the point of writing. This though is off the 2018 high of 1.73% on 10 May (a level not seen since 13 Jan 2016). Meanwhile, 3-month SIBOR climbed to a new 10-year high of 1.6369% on 7 Aug but has edged lower to hover around 1.6362% currently. Both the 3-month SOR and 3-month SIBOR remain elevated as the withdrawal of monetary stimulus in the other advanced economies continues. We are now gradually seeing mortgage rates respond to the climb in domestic rates. Deposit rates (for 12-month fixed) also continues to edge higher, climbing 1bp to 0.38%-levels at the beginning of Aug. This continues to suggest that risks related to interest rate increases affecting financial and economic stability, particularly in interest rate- and property-related sectors, remain on the gradual uptick.

- USD 3MLIBOR has come off slightly after climbing to a new 2018 high not seen since 2008 at 2.37% on 4 May. Fed balance sheet reduction is playing a part in draining liquidity from the system and this has resulted in the recent moves higher in domestic rates vis-à-vis the USD 3MLIBOR. We continue to expect the 3MSIBOR and 3MSOR to edge higher to 1.89% and 1.77% respectively by end 3Q 2018. For end-2016% respectively.

- **Latest Fiscal and External Balance Outlook:** The government collected just SGD5.5bn in tax revenues in Jun, a slowdown from the SGD8.5bn collected in May. This dip in tax revenue collected can be attributed to the lower corporate income tax collected of SGD1.8bn in Jun compared to May's SGD2.9bn, and to the lower GST collected of SGD0.2bn in Jun vs. SGD2.6bn in May.

- The current account (CA) surplus widened to SGD22.83bn in 2Q 2018 compared to SGD20.5bn in 1Q. As a percentage of GDP, the CA surplus rose to 20% in 2Q vs. 18.4% in 1Q. The wider CA surplus was largely attributable to the increase in the goods and services surplus of SGD29.38bn in 2Q vs. 1Q's SGD27.66bn. The financial and capital deficit narrowed to SGD14.10bn in 2Q from SGD15.32bn in 1Q due to the larger direct investment inflows of SGD13.70bn (1Q: +SGD8.5bn) and smaller outflows of SGD18.41bn (1Q: -SGD26.62bn) from the "other investment" segment. Consequently, the overall balance of payments (BoP) surplus widened to SGD7.8bn in 2Q vs. SGD6.8bn in 1Q.

- **Key domestic events and issues to watch:** Key data releases that will be closely eyed will be CPI prints for Aug on 24 Sep ahead of the MAS meeting in Oct. Before that, Aug NODX on 17 Sep will also be in focus for signs of any fall-out from the Sino-US trade war.

- **Technical Outlook:** USDSGD traded a month of 2 halves in Aug – rising at first before retracing those gains into end-month. Last seen at

1.3680 levels. Mild bullish momentum on weekly chart shows tentative signs of waning while stochastics shows early signs of turning from overbought conditions. Price pattern on weekly chart does suggest slowing gains and possibly a bearish reversal setup. Resistance at 1.3780 (50% fibo), 1.3820 (2018 high). Failure to push above these levels should attract selling interest. Support at 1.36 (38.2% fibo retracement of 2017 high to 2018 low), 1.3510 levels (100 DMA).

MYR: Awaiting clarity on key policy measures

Forecast	3Q 2018	4Q 2018	1Q 2018	2Q 2019
USDMYR	4.0800 (--)	4.0700 (4.0300)	4.0500 (3.9800)	4.0500 (3.9800)

Previous Forecast in Parenthesis

- **Motivation for the FX View:** In line with most other regional currencies, the MYR weakened against the USD by around 1% in the month of Aug albeit not as bad as other regional currencies such as the IDR. It reached a high of 4.1105 on 24 Aug, in the run up to the release of the Fed minutes and Jackson Hole. The drop in reserves level for the past 4 months may indicate BNM using reserves to contain further weakness in MYR.

- Latest developments in the RMB which had played an anchor of stability for Asian FX also led to some impact on MYR. In particular, the RMB losing its safe-haven status as USD strengthened, partly driven by a few factors such as seasonal dividend payments by Mainland companies, unwinding of short positions by offshore real money and a general shift in sentiment caused by fears of repercussions from the economic conflict with the US.

- The risk of a possible global trade war becoming more sustained, coupled with continuing Fed policy normalisation and repatriation of corporate earnings, may further add to USD tightness. In that base scenario, riskier and commodity currencies are likely to remain vulnerable. Further out, we continue to anticipate more USD underperformance on the back of a further flattening of the UST yield curve and concerns about the deteriorating US twin deficits.

- In addition, our economics team sees rising likelihood that the BNM could keep rates on hold until 2019 to support domestic demand especially consumer spending. Taking all these into consideration, we revise our G7 forecasts leading to adjustments to our dollar levels and as a result, we revise higher again our USDMYR forecasts for this year.

- Nonetheless, MYR fundamentals remain well anchored by sustained current account surplus, rising FX reserves to retained imports & short-term debt, sustained growth pick-up backed by consumption, investment and exports as well as higher oil prices. We maintain our lower USDMYR forecast trajectory beyond 2018 on efforts taken by the new government to improve governance, transparency and accountability. However, we acknowledge there could still be some uncertainty over the next few years as the new government navigates the new political environment and foreign investors still remain somewhat cautious for now. Domestically some concerns about a pullout in some of the investment projects from the previous administration may have inadvertently affected sentiment in the short term, although our medium term view remains supportive of the currency.

- As such taking into consideration both domestic and external factors, we now have a slower pace of MYR appreciation vis-à-vis the dollar, consistent with our USD weakness view in the medium term. On the domestic front in the short term, a weak MYR bias coupled with USD strength will likely persist, before some element of certainty comes from the Budget 2019 in Oct. Overall in the short term, domestic policy uncertainty risk may still somewhat weigh on the MYR despite solid fundamentals.

- We believe the 100-day promises made by PH in its manifesto will be a "scorecard" for investors to check if PH and its team of Eminent Persons fulfilled their objectives, in terms of execution and implementation. Swift execution of its objectives and clear communication to address government finances will demonstrate the new government's capability; dispel uncertainty associated with government policies and restore investors' confidence within the next 100 days. This could manifest into further gains for the Ringgit. Meantime we do not rule out bouts of volatility as investors await results. While sentiment may have stabilised for now and we continue to maintain a bullish bias on the Ringgit, FX is never one way and is also driven by externalities including global monetary policies, financing conditions, USD direction, pace of UST yield upmove, geopolitical events (such as tensions in middle east that may affect oil prices, US mid-term elections), ongoing trade tensions, etc..

- We reiterate our long-standing bias that the Ringgit remains fundamentally undervalued (by about 5%). Our fair value model which takes into account the relative differentials in interest rates, inflation, current account and a reflation proxy variable (defined as the change in the ratio of MSCI World index to JPM Global Aggregate Bond Index) estimates USDMYR at 3.70 levels. Based on BIS data, MYR REER is about 5-6% undervalued relative to its 10-year average. We had previously said that Ringgit weakness was temporary and was not a reflection of underlying fundamentals. We believe stability is gradually returning to Ringgit as political/ contingent liability risk subsides, fiscal consolidation gains traction (budget deficit expected to be cut further to -2.8% of GDP vs. 3% of GDP in 2017), oil prices continue to stabilize and uncertainty subsides.

- The key risks to our outlook are (1) sharp rise in UST yields due to more aggressive than expected Fed policy normalisation could lead to foreign outflows and weigh on Ringgit and (2) risk-off plays/ rise in vols (uncertainty) arising out of synchronous recovery stalling, swings in crude oil and/or palm oil prices to the downside may weigh on

Ringgit; (3) **As a trade dependent country, risks of trade war could weigh on the MYR as well as other currencies in ASEAN,** (4) higher risk from EM volatility and eurozone risk escalation.

- External reserves fell for the fourth consecutive month (i.e. since midApr 2018) by -USD0.3b to USD104.2b at mid-Aug 2018 vs –USD0.1b to USD104.5b at end-Jul 2018 mainly amid indications of net portfolio capital outflows. The latest external reserves figure is equivalent to 7.6 months of retained imports and 0.9 times of short-term external debt. Foreign investors remained cumulative net sellers of Malaysian equities in 1-21 Aug 2018, but the pace slowed to –MYR0.1b vs –MYR1.7b in Jul 2018 and –MYR4.9b in Jun 2018. Aug 2018 started with +MYR0.5b net foreign buying in the first trading week of the month (1-9 Aug 2018), riding on positive sentiment from the gains S&P500 as most US corporations reported strong earnings. But foreign investors turned net sellers of –MYR0.7b on 10-21 Aug 2018 in response to the financial and geopolitical crisis in Turkey.

- Meanwhile, data on net foreign flows in Malaysian bonds for this month is only available at the end of the first week of Sep 2018. To recap, foreigners turned +MYR4.0b net buyers of Malaysian bonds in Jul 2018 (Jun 2018: -MYR6.7b) after three consecutive months of net selling.

- The Institute of International Finance's (IIF) daily EM portfolio capital flows data showed volatile net flows this month. The month started positively with net inflows of +USD4.5b on 1-9 Aug 2018 (+USD2.7b in equities; +USD1.7b in bonds), but reversed to –USD3.0b net outflows (- USD1.9b in equities; -USD1.1b in bonds) on 10-19 Aug 2018, and switched back to +USD2.4b net inflows (+USD1.8b in equities; +USD0.5b in bonds) on 21-22 Aug 2018. Most negatively affected by the volatile EM portfolio capital flows so far this month in terms of total equity and bond net outflows are Turkey and South Africa, while Indonesia, India, Taiwan, Thailand, Vietnam and Philippines are most affected in terms of net portfolio capital outflows from their equity markets.

- Amid the volatile portfolio capital flows so far this year, Malaysia's external reserves will be supported by the repatriation of export proceeds given the positive trade flows thus far. Trade surplus jumped +41.0% to +MYR60.6b in 1H 2018 vs +MYR42.9b in 1H 2017, consistent with our forecasts of larger trade surplus of +MYR127.7b this year (2017: +MYR97.2b) and +MYR140.9b next year. Reflecting confidence in the sustainability of Malaysia's trade - hence current - account surplus, BNM on 17 Aug 2018 announced flexibility to the requirement for repatriation of export earnings. Exporters can now automatically place their export proceeds into their foreign currency accounts with onshore banks for the purpose of meeting their six months forward foreign currency obligations (e.g. payments for imports and borrowings) upon establishing such obligations with their onshore banks. Previously, exporters have to convert their 75% of repatriated earnings from foreign currencies into MYR and then reconvert back to foreign currencies to meet their 6 months forward obligations that entailed increased documentations and paper works.

- **Growth and Inflation Outlook: Our economists trimmed their 2018 and 2019 real GDP growth forecasts, both to +4.8% vs +5.1% and +4.9% previously as 1H 2018 growth slipped to +4.9% (2017: +5.9%) and taking into account of the year-to-date economic data.** Change in government after the general election on 9 May 2018 results in policy shifts and uncertainties with mixed impact on domestic demand. Consumption tax holiday period from 0% GST in June-Aug 2018 and fuel price subsidy until end-2018 will have positive but transitory effect on consumer spending growth (2018E: +7.6% vs +7.3% previously; 2019E: +6.3% vs +6.7% previously). Public spending (2018E: -1.2% vs +0.8% previously; 2019E: maintained at +1.0%) mainly due to impact on Government development expenditure from the reviews in major infrastructure projects that involve cost reductions, postponements and cancellations, as well as pending clarity on Government policy on Government-linked companies (GLCs) amid changes in managements and boards. Private investment growth forecasts of +3.3% in 2018 (+2.0% previously) and +3.8% in 2019 (unchanged) trail last year's robust growth of +9.3% as businesses and industries wait for clarity on key policy measures and events such as the outcome of the reviews of major infrastructure projects, announcement on minimum wage hike, and the tabling of Budget 2019 on 2 Nov 2018. Maintained our view of slower 2018-2019 growth in exports (2017: +9.4%; 2018E: +3.8% vs +4.5% previously; 2019E: +3.5% vs +4.3% previously) and imports (2017: +10.9%; 2018E: +2.0% vs +1.8% previously; 2019E: +2.5% vs +3.3% previously) of goods and services after the surge in 2017 and amid signs of moderating global economic growth in 2H 2018 and 2019.

- Inflation rate remained sub-1% at +0.9% YoY in Jul 2018 (Jun 2018: +0.8% YoY) as the 0% GST period of Jun-Aug 2018 results in slower increases or declines in most of the prices of goods and services in the CPI basket. Expects full-year inflation rate to be at the upper end of our 0.5%-1.0% forecast range (Jan-Jul 2018: +1.4% YoY; 2017: +3.7%) on continued sub1% inflation rate until year-end. Inflation is expected to pick up moderately to 1.5%-2.0% next year.

- Headline inflation stayed south of 1.0% YoY in Jul 2018 on slower increases or declines in the prices of most goods and services in the CPI basket - except the "transport", "housing, water, electricity, gas and other fuels", and "education" sub-groups - reflecting the impact of "consumption tax holiday" following the zero rating of GST during the Jun- Aug 2018 period. Meanwhile, core CPI dropped -0.2% YoY in July 2018 after decelerating to +0.1% YoY in June from +1.5% YoY in May 2018.

- Both headline and core inflation rates in Jan-Jul 2018 were low at +1.4% YoY and +1.2% YoY respectively. Given the soft headline inflation rate during Jun-Jul 2018 period and the likelihood of continued sub-1% inflation rate for the rest of this year, we maintain our 2018 and 2019 headline inflation rate forecasts at 0.5%-1.0% and 1.5%-2.0% respectively.

- The slowdown in 2Q 2018 real GDP growth to +4.5% YoY (1Q 2018: +5.4% YoY) led us to cut our full-year 2018 and 2019 growth forecasts, both to +4.8% (vs +5.1% and +4.9% previously). At the same time, **BNM**

now expects this year's real GDP growth forecast to come in at around +5.0% vs the official forecast of +5.5% to +6.0% range made in Mar 2018.

- **The downgrades in 2018 and 2019 growth outlook further support the view of relatively subdued inflation this year and next year compared with the +3.7% inflation rate in 2017 when economic growth was firmer at +5.9%.**

- **Monetary Policy Forecast:** BNM kept the OPR unchanged for the third consecutive Monetary Policy Committee (MPC) meeting on 10-11 Jul 2018. The accompanying Monetary Policy Statement (MPS) was "dovish" on inflation with expectation of negative headline inflation rate for some months and low inflation rate in 1H 2019 on the effect of the 0% GST rate in June-Aug 2018 and the fuel price stabilization until end-2018 before the impact of these factors dissipates. Consequently, BNM expect headline inflation for 2018 to be lower than the current official forecast of 2.0%-3.0%. The economic growth and inflation outlook supports our view of no change in BNM's current Overnight Policy Rate (OPR) level of 3.25% until end-2019 after the +25bps hike at the Monetary Policy Committee (MPC) meeting on 25 Jan 2018. Furthermore, post-GFC, BNM's monetary policy objective also includes financial stability. Under current environment of US-led rising global interest rates and volatility in Emerging Market's capital and FX markets, interest rate policy plays a role in managing capital flows and currencies, further underlining our view of no change in OPR.

- Furthermore, unless the US Fed turns very aggressive on its interest rate hikes vs the current guidance, there is currently "positive carry" in terms of the differences between Malaysia and US interest rates and between domestic interest rate and inflation rate which should not necessitate further interest rate hike this year. Malaysia is also ahead of the curve marginally in normalizing its interest rate i.e. since 2011, as the current OPR is just 25bps short of the pre-GFC peak of 3.50%.

- **Latest Fiscal and External Balance Outlook:** While the planned removal of GST, reinstatement of fuel price subsidy and raising minimum wage were meant to alleviate living costs for the nation, the measures are expected to have repercussions on government finances. Most importantly, will these measures result in increased burden for the government in terms of borrowings and will the fiscal discipline or sovereign credit rating be compromised?

- Our Economists estimated that GST removal entails a revenue loss of MYR44bn (based on Budget 2018 projection). **Replacing GST with the previous Sales and Services Tax (SST) which last earned a full-year revenue of MYR17b in 2014, there is a prospective net tax revenue loss of MYR27b.** Malaysia's budget deficit to GDP ratio will arithmetically increase by as much as 1.9 percentage points, just on this basis alone, assuming no offsetting reduction in expenditures or revenues from oil or more efficient collection of taxes. However this is only a simplistic assumption for preliminary illustration. **Former BNM Governor Zeti (currently a member of the Eminent Persons) recently said that Malaysia can meet its revenue requirements**

after shelving the GST by prioritising its projects, increasing the efficiency of the public sector, avoiding wastages and exploring new sources of revenue.

- Our Economists also noted that PH's Alternative Budget 2018 argues there is scope for operation expenditure rationalisation such as lowering the Prime Minister's Department budget to MYR8.4bn from MYR20.8bn.

- On oil prices, our Economists shared that every US$10/bbl increase in annual average crude oil prices will boost government revenues by MYR7-8bn via oil related revenues. Last year's average crude oil price averaged US$54/bbl, up from US$44/bbl in 2016. And YTD 2018, crude oil price averaged about US$69. Theoretically the US$15 increase in crude prices from 2017 works out to a potential increase in government revenues by MYR10.5bn – 12bn.

- **Smallest current account surplus since 2Q 2016**. Current account surplus shrank in 2Q 2018 to +MYR3.9b or +1.1% of GDP (1Q 2018: +MYR15.0b or +4.4% of GDP) on smaller goods trade surplus (2Q 2018: +MYR26.1b; 1Q 2018: +MYR35.7b) as pick up in exports was offset by rebound in imports; bigger deficit in income account (2Q 2018: -MYR16.0b; 1Q 2018: -MYR14.9b) on repatriation of dividends from foreign investment in Malaysia; and wider services trade deficit (2Q 2018: -MYR6.2b; 1Q 2018: -MYR5.8b) on higher imports of constructionand transport-related services as well as lower surplus of travel.

- Financial account posted smaller surplus of +MYR9.2b in 2Q 2018 (1Q 2017: +MYR15.2b) as the higher net inflows of other investments (2Q 2018: +MYR48.4b; 1Q 2018: +MYR6.4b) was offset by bigger net outflows in portfolio investments (2Q 2018: -MYR38.3b; 1Q 2018: -MYR2.6b) amid foreign net sell of Malaysian equities and bonds last quarter, and turnaround in direct investment to net outflows (2Q 2018: -MYR0.7b; 1Q 2018: +MYR10.7b) as direct investment abroad (DIA) exceeded foreign direct investment (FDI).

- Current account surplus was +MYR18.9b or +2.7% of GDP in 1H 2018. We trimmed our 2018 and 2019 current account surplus forecasts to +MYR46.4b or +3.2% of GDP (+MYR54.2b or +3.7% of GDP previously) and to +MYR51.1b or +3.4% of GDP (+MYR59.7b or +3.8% of GDP previously) respectively (2017: +MYR40.3b or +3.0% of GDP).

- Domestic policy and global trade are the key influences on the trend in and size of current account surplus. Imports of goods and services are getting a short-term boost from the 0% GST period i.e. June-Aug 2018 as businesses take advantage of this to do their purchases, which are expected to dissipate post-consumption tax holiday period. Pakatan Harapan (PH) Government's policy of reviewing major infrastructure projects to lower costs, postpone or cancel projects will impact investment growth, with spillovers on imports of construction-related materials, equipment and services.

- Despite the risk to global economic and trade growth amid the on-going and escalating US-China trade war, any downside to exports will be mitigated by lower imports - especially that of intermediate goods with knock on impact on imports of capital and consumption goods – to keep trade and current accounts in surplus. There are also potential trade substitution and diversion effects as well as investment relocations to either boost exports directly or via imports for re-exports, where Malaysia could be a beneficiary.

- **Key domestic events and issues to watch:** Trade data (5 Sep); FX reserves (6 & 21 Sep); Industrial Production (7 Sep); CPI (19 Sep), BNM Policy Meeting (5 Sep).
- **Technical Outlook:** USDMYR continued to trade higher. Last seen at 4.1080 levels. Bullish momentum on weekly chart remains intact while stochastics is in overbought conditions. Uptrend still intact but gains could slow given stretched technical conditions. Resistance at 4.15, 4.1780 (50% fibo retracement of 2017 high to 2018 double-bottom low).Support at 4.1020 (38.2% fibo), 4.08 levels.

IDR: Bears Still Have The Upper Hand

Forecast	3Q 2018	4Q 2018	1Q 2019	2Q 2019
USDIDR	14750 (14450)	14600 (14250)	14500 (14100)	14300 (13900)

Previous Forecasts in Parenthesis

- **Motivation for the FX View:** The USDIDR continues to be the worst performer among its ASEAN peers in Aug. Already, the USDIDR has climbed to a three-year high of 14715 on 31 Aug amid escalating emerging market risks emanating from Argentina and Turkey. We have revised our outlook for the USDIDR for the rest of the year and into 2019 but maintain the downward trajectory of the USDIDR. Underpinning our forecast are upside pressure on the pair from the spill-over effects from emerging market risks, expectations of Fed rates, simmering Sino-US trade war concerns, further deterioration in the twin deficits amid higher oil prices, and high foreign ownership of domestic debt. Still, it is not all bad news as optimism over government spending ahead of the presidential and general elections in 2019 as well as preparation for major event onshore, namely the World Bank-IMF Annual Meetings in Bali on 12-14 Oct should mitigate some of these upside risk to our USDIDR forecast.
- The USDIDR remains under upside pressure despite the benchmark policy rate having been raised by 125bp to maintain macroeconomic and financial stability. Even the BI's dual intervention in the FX and bond markets, amounting to nearly USD14bn of its foreign reserves since Feb, has not had the desired effects on the IDR. It did manage though to prevent the IDR from rising too aggressively. Driving the sell-off in the IDR can be attributable to Indonesia's persistent current account deficit. The current account deficit has widened in 2Q due to

seasonal factors to 3.0% of GDP. Supportive of the deficit as well is elevated oil prices, which is edging gradually towards the USD80/bbl levels.

- We expect downside pressure on the IDR to continue for a little while longer. This is because like in Aug, Sep tends to be a seasonally weak month for the IDR vs. the USD. In seven of the past 10 years, the IDR has weakened against the USD in Sep. Thus, there is a potential for the IDR to head lower in the month. The USDIDR could bounce higher as a result with the possibility of a USDIDR overshoot back towards the 14800-levels before easing to end 3Q around the 14700 levels.

- The sell-off in equities and debt that had weighed on the IDR appears to have been stemmed. With UST yields coming off from the 3.0%-levels, this has spurred renewed interest in higher yielding assets in emerging markets, including in Indonesia. Renewed foreign interest in Indonesian debt especially has seen foreign investors purchased USD 557.7mn in debt in Aug, continuing their purchases from Jul. On the other hand, foreign investors have been selling their holdings of equities in Aug with USD76.45mn sold. This is in contrast to the USD54.04mn purchased for the whole of Jul. This has allowed the USDIDR to retrace from some of its losses from earlier in the month as it did in Jul. This should keep cap upside in the USDIDR in 3Q.

- Risk to further foreign portfolio inflows is that sentiments can just as easily change and lead to a sell-off in Indonesian assets and keep the USDIDR supported, especially should trade tensions re-escalate. Just as important, foreign holdings of Indonesian sovereign debt are among the highest in the region, making the IDR vulnerable to any sell-off triggered by market stresses.

- Going into 2019, we can expect some volatility in the markets as the 17 Apr Presidential and general elections draw closer. For now, the opinion polls point to strong support for Jokowi but things can change from now till Apr next year. Signs of waning support for Jokowi could shake market confidence and sent the USDIDR even higher. Our house view is for a Jokowi to win at this juncture, which should put downside pressure on the USDIDR going into the elections.

- In light of recent market developments, we revised our USDIDR forecast higher over our forecast horizon. We now expect the USDIDR to come in around 14750 by end-3Q 2018 (from 14450 previously) before easing to around 14600-levels by end-2018 helped by the government measures to curb the current account deficit and shore up foreign reserves. In 1H 2019, we look for the pair to edge slightly lower to 14500 and then to 14300 by end-1Q and -2Q 2019 (from 14100 and 13900 previously).

- **Growth and Inflation Outlook:** After disappointing in 1Q, the economy surprised with a better-than-expected print in 2Q. 2Q 2018 GDP expanded by 5.27% y/y vs. market estimates of 5.1% and 1Q's 5.06%. Growth was lifted by stronger household consumption (above 5% to 5.14% for the first time since 3Q 2016), aided by stronger household spending during the Eid holidays. Also supportive of 2Q GDP was robust government expenditure (of 5.26% y/y vs. 1Q's 2.74%). Our economic team remains upbeat about growth prospects for the rest of 2018. Government spending remains supportive growth even as the government mulls plans to delay certain infrastructure projects to rein in the current account deficit. Spending ahead of the presidential and general elections in Apr 2019 also buoy the economy. In addition, major events like the Asian games (18 Aug-2 Sep) and the World Bank-IMF Annual Meetings in Bali (12-14 Oct) should also provide private consumption with a lift. While higher interest rates are likely to dampen private spending to some extent, macroprudential measures, especially for home buyers, could mitigate some of this risk. Our economic team expects the economy to expand by 5.21% in 2018 before accelerating further to 5.31% in 2019. BI expects the economy to expand by 5.0-5.4% and 5.1-5.5% in 2018 and 2019 respectively.

- After decelerating in the past two months, headline inflation picked up by 3.18% y/y in Jul from 3.12% in Jun. Lifting consumer prices higher in Jul was once again food prices, which rose 5.35% y/y vs. 4.67% in Jun, as well as the pick-up in housing cost (Jul: 1.97% y/y vs. Jun: 1.87%). Transport cost though slipped lower by 1.34% y/y in Jul (Jun: +1.93%) on after accelerating in the previous two months as higher crude oil prices did not translate into higher prices. Core inflation accelerated in Jul, rising 2.87% y/y from Jun's 2.72%. The government's move to address imported inflation should help temper inflationary pressures ahead. The government is looking to impose a tariff of 7.5% on around 900 consumer goods to reduce consumption. Nevertheless, IDR weakness should remain a source of inflationary pressure, driving up imported good prices, including oil. Our economic team expects headline and core inflation to come in at 3.40% and 2.76% respectively for 2018. The BI continues to target inflation to range 2.5 and 4.5% in 2018.

- **Monetary Policy Forecast:** After a pause in Jul, the BI hiked its 7-day reverse repurchase rate again by 25bp to 5.50% at its 15 Aug meeting amid global uncertainty triggered by the Turkish crisis. This marks the fourth rate hike by the central bank this year and brings the cumulative rate hike to 125bps for 2018. The deposit and lending facility rates were lifted by 25bp as well to 4.75% and 6.25% respectively, keeping the interest rate corridor at 75bp on either side of the policy rate. This move by the BI is consistent with the governor's strategy of keeping policy "pre-emptive, front loading, and ahead of the curve" in order to maintain macroeconomic and financial system stability. In short, the BI hopes to improve the attractiveness of the local financial market and maintain the current account deficit at a safe level with its rate hike.

- In this current environment, we cannot rule out the possibility that the BI will continue with its policy tightening cycle. BI Governor Perry Warjiyo has reiterated that the central bank's top priority is to stabilize the economy and the IDR. Thus, continued downside pressure on the IDR should keep the BI policy stance on a hawkish bias. This leaves the Sep meeting open for another move by BI. Our economic team though is penciling another 25bp rate hike to 5.75% to come only in 4Q 2018.

- **Latest Fiscal and External Balance Outlook:** President Joko Jokowi's draft state budget for 2019 included increases in subsidies as well as civil servants' pay, and a doubling of benefits to poor households, a nod to upcoming presidential election in Apr 2019. The government intends to narrow the 2019 budget deficit to 1.84% of GDP from 2.12% targeted this year as the government stepped up efforts to boost confidence as the currency and asset markets fell. The key budget assumptions for 2019 include GDP growth of 5.3%, inflation of 2.5-4.5%, crude oil price at USD70/bbl and average USDIDR at 14,400.

- As expected, the current account deficit (CAD) widened to USD8.03bn in 2Q 2018 (equivalent to 3.04% of GDP) after narrowing mildly to USD5.54bn (2.21% of GDP) in 1Q. The wider CAD was largely attributable to the deficit of USD1.5bn in the goods and services account (1Q: +USD0.75bn). The surplus in the financial account though widened in 2Q to USD4.00bn vs. 1Q's +USD2.39bn, supported by a rebound in portfolio investment of USD0.05bn (from 1Q's -USD1.15bn) and larger surplus in the "other investment" segment of USD1.46bn vs. USD0.55bn in 1Q. Still, the overall balance of payment deficit widened to USD4.31bn in 2Q vs. -USD3.85bn in 1Q. Nevertheless, BI expects to keep the current account deficit below 3% of GDP by end-2018. Given the recent deterioration in the current account deficit, our economic team is now projecting the current account deficit to come in around 2.50% of GDP in 2018 vs. 2.2% of GDP previously forecasted.

- The government announced measures on 14 Aug to shore up its foreign exchange reserves as well as to control the CAD. These measures included plans to curb capital and consumer goods imports by imposing a tax of 7.5% on select products, moves to accelerate the use of biodiesel fuel to cut the import of oil, the push for import substitution whenever possible, and to promote tourism. Success in this area would be positive for the IDR.

- **Key domestic events and issues to watch**: Keenly watched in Sep is the BI's policy meeting on 27 Sep for possible policy moves. The political season will begin on 21 Sep with the kick-off with the start of campaigning for the presidency. Also watched will be foreign reserves for Aug on 7 Sep.

- **Technical Outlook:** USDIDR continued to trade higher for the month; last seen at 14,710 levels. Bullish momentum on weekly chart remains intact. Next resistance at 14,830 (previous high in 2015 and record high). Beyond that would be uncharted territory for USDIDR. Next psychological resistance at 15,000. Support at 14600 (21 DMA), 14440 (50 DMA).

PHP: Headwinds Persist

Forecast	3Q 2018	4Q 2018	1Q 2019	2Q 2019
USDPHP	54.00 (--)	53.50 (--)	54.00 (--)	53.90 (53.80)

Previous Forecasts in Parenthesis

- **Motivation for the FX View:** We maintain our outlook for the USDPHP in the next three- to nine-months. Upside pressure on the USDPHP is likely to be partially mitigated by expectations of further rate hike by the BSP and intervention by the central bank in the FX markets to stem PHP volatility. This has capped the pair around the 53.640-levels for the time being. We however continue to look for the USDPHP to climb higher in the month ahead underpinned by potential external risks, including Turkish crisis and other emerging market risks, expectations of Fed rates and simmering Sino-US trade war concerns. In addition, weak underlying fundamentals, including further deterioration in the twin deficits amid higher oil prices, are likely to keep the USDPHP supported towards the end of 3Q. We should see the pair continue its climb higher towards the 54-levels by end-3Q.

- The two 50bp rate hike in Aug is unlikely to signal an end to the current BSP tightening cycle. We believe that consensus is looking for another 25bp hike by the BSP, mostly likely to take place at the upcoming policy meeting on 27 Sep. This follows from the BSP governor's comments that the central bank has "not closed the door" on further action with the decision still data-driven. There could lead to some unwinding of long-USDPHP positions into the BSP meeting and providing some relief to the USDPHP.

- Still, downside moves in the USDPHP is likely to be limited given the economic fundamentals appear to have weakened. The trade balance remains in a deficit, still hovering around the USD3bn mark. At the same time, overseas remittances is weakening, declining by -4.5% in Jun from +6.9% in May. In addition, the current account deficit should have widened even more on elevated oil prices (in value terms) given that Philippines is an oil-importing economy. The government's ambitious infrastructure building programme is likely to keep the current account in deficit in 2018 and possibly into 2019 as well. These suggest that the current account deficit is unlikely to see any significant improvement ahead. Importantly, the current account deficit has been on the broad downtrend since 2015. Further deterioration should be supportive of the PHP.

- The fiscal position also shows no signs of improvement. The tax reforms implemented to date have yet to show any significant results in terms of revenue collection. Instead, the fiscal deficit continues to balloon with the deficit in the first seven months of the year at PHP279.4bn. For now, there is little sign that the tax reforms will reverse the fiscal deficit that has plague governments for the longest time anytime soon. In fact, the fiscal deficit is likely to worsen further given the ambitious infrastructure building programme of the government. An added concern is that the government could spend more of its revenue collected to service interest payments rather

- USDPHP should continue to come under upside pressure from the ongoing sell-off in Philippine equities by foreign investors. In Aug so far, foreign investors have divested a total of USD88.65mn of equities from their holdings amid concerns over BSP rate hikes and trade war concerns. In 2018 so far, foreign investors have sold off USD1.36bn in equities. Our analysis using the Cyclical Adjusted P/E (CAPE) ratio model though continues to suggest that domestic equities appears relatively cheap (as reflected by the estimated P/E ratios minus their 10-year average P/E ratios) compared to its regional peers. This is particularly given the expected strong economic performance this year. Greater inflows towards the end of the year once the current risk aversion episode fades could weigh on the USDPHP and allow the pair to ease from the 54-levels in 3Q to around the 53.50-levels by end-2018.

- We maintain our USDPHP unchanged for 3Q and 4Q 2018 with the risk still to the upside in 3Q on global risk aversion. Thereafter, the USDPHP should ease to 53.50 by year-end as trade tensions fade and USD strength softens. Rising political risk as elections for the House of Representative and half of the Senate (due 13 May 2019) approach should lift the USDPHP higher back towards 54.00 by end-1Q 2019. We tweak our end-2Q 2019 USDPHP forecast to reflect the more moderate reduction in USD strength with the pair expected to ease to 53.90 (from 53.80 previously).

- **Growth and Inflation Outlook:** Economic growth slowed to 6.0% y/y in 2Q from a downwardly revised 6.6% in 1Q (previously 6.8%). The moderation in growth was due to the worsening net external demand though domestic demand growth momentum was sustained. Except for construction, the slowdown in the economy was relatively broad-based. Growth in the manufacturing and services sectors eased to 5.6% and 6.6% respectively in 2Q from 7.6% and 6.8% in 1Q. The mining sector shrank while the agriculture sector stagnated. Bucking the trend was construction that expanded 13.5% y/y in 2Q on the back of a pick-up in private construction which accounted for almost 60% of total construction, as well as sustained momentum in public construction. With 1H growth coming in at 6.3% y/y, the economy is expanding at a pace below the 6.5% average for the past five-years. In view of the 1H 2018 performance and the BSP's 100bp rate hikes YTD, our economic team has revised lower its 2018 and 2019 growth forecasts to 6.3% and 6.5% respectively (previously 6.8% for both years).

- Headline inflation rate (base year = 2012) surged in Jul, accelerating by 5.7% y/y from 5.2% in Jun on the back the impact of the Tax Reform for Acceleration and Inclusion (TRAIN) Act measures; weaker PHP; and higher costs of food & non-alcoholic beverages (FNAB), utility and transport. Core inflation (CPI excluding selected food items as well as energy prices) also rose by 4.5% y/y in Jul from 4.3% in Jun.

Our economics team maintains its 2018 and 2019 inflation forecasts at +4.6% and +3.7% respectively as it expects inflation to peak in the Jun-Aug period before easing gradually towards the end of the year. The BSP inflation target remains at 2-4% for 2018-2020 and its inflation forecast is at 4.5% (from 4.6% previously) for 2018 and 3.3% for 2019 (from 3.4% previously).

- **Monetary Policy Forecast:** After tightening policy by 25bp each in May and Jun, the BSP raised its overnight borrowing rate by 50bp to 4.00% on 9 Aug. This move had been broadly anticipated after Indonesia's central bank had taken the lead with a similar quantum at its Jun policy meeting. The BSP left the interest rate corridor intact with the overnight lending rate and overnight deposit rate both raised by 50bp accordingly to 4.50% and 3.50% respectively. The interest rate corridor remained symmetrical on either side of the policy rate by 50bp.

- The 50bp rate hike though does not necessarily signal the end of the tightening cycle. According to the BSP governor, "we have not closed the door" on further action even as the central bank expects inflation to potentially peak, "perhaps by next month" with the decision still data-driven. In addition, the BSP statement following the policy decision had stated that the economy can accommodate further tightening, suggesting that there is further room to accommodate another move in this current cycle. Consequently, our economic team is penciling in one more 25bp rate hike this year. We think that this hike could come as early as at its 27 Sep policy meeting.

- **Latest Fiscal and External Balance Outlook:** The fiscal deficit widened to PHP86.4bn in Jul (Jun: -PHP53.3bn) as government spending outstripped the increase in revenues collected. Treasury Bureau data showed that government spending climbed to PHP328.13bn in Jul from PHP278.49bn in Jun. Revenue collected in Jul rose to PHP241.74bn from PHP224.20bn in Jun. YTD, government revenues stood at PHP1.65tn, while government expenditure came in at PHP1.93bn. This brought the fiscal deficit to PHP279.4bn in the first seven months of the year.

- The balance of payments (BoP) deficit narrowed in Jul to USD0.46bn from –USD1.18bn in Jun, attributed to the outflows from the government's payment of maturing foreign currency loans as well as BSP FX operations. For the first seven months of the year, the BOP deficit climbed higher to USD3.71bn due to expanding trade gap in 1H 2018 on sustained rise in imports of raw materials and capital goods to support domestic economic expansion. The current account data has yet to be released but the BSP continues to expect a deficit of USD3.1bn (-0.9% of GDP) for 2018. The central bank continues to project a BoP deficit of USD1.5bn (-0.4% of GDP) for the whole of 2018 even though this level has already been breached since Jun.

- **Key domestic events and issues to watch:** Ahead of the BSP policy meeting on 27 Sep, market will be eyeing CPI print for Aug on 5 Sep for hints of whether inflation has peaked. Also closely watched will be foreign reserves for Aug on 7 Sep.

- **Technical Outlook:** USDPHP was last seen near record highs of 53.50 levels. Up-trend remains intact. Resistance at 53.63 (previous high). Beyond that would be uncharted territory for USDPHP. Psychological resistance at 55 levels. Support at 52.90, 52.700 levels.

THB: Near-Term Outlook Still Bearish

Forecast	3Q 2018	4Q 2018	1Q 2019	2Q 2019
USDTHB	33.00 (33.50)	33.50 (33.80)	33.80 (--)	33.60 (33.30)

Previous Forecasts in Parenthesis

- **Motivation for the FX View:** The USDTHB has been the best performing currency within the ASEAN space in Aug. A combination of a return of foreign interest in Thai debt and increasing expectations of policy normalisation by the BoT is weighing on the pair. We have revised our USDTHB outlook over the forecast horizon to reflect the current slippage in the USDTHB.

- Easing emerging market risk and Sino-US trade tensions earlier in Aug together with signs of robust domestic economic recovery spurred renewed foreign interest in Thai debt in Aug. After selling off USD12.7mn in debt in Jul, foreign investors have purchased USD2.15bn in debt so far in Aug. Foreign demand for Thai equities though remained in the doldrums with USD0.30bn sold off in Aug month-to-date. Net foreign portfolio inflows in Aug weighs on the USDTHB and allowed the pair to come off from its 2018 high of 33.526 on 20 Jul to hover around 32.684 at the point of writing.

- However, profit-taking activities in the equity markets since 2017 after strong foreign inflows of USD2.24bn for the whole of 2016 are likely to persist. These profit-taking activities reflect investors' belief that the economy is facing domestic structural headwinds, including hollowing out of industries, ageing demographics and rising leverage. We do not think that these structural issues can be resolved overnight and these concerns will thus continue to weigh on Thai equities. In addition, market concerns over escalating trade war between China and US given its relatively export-dependent economy as well as spill-overs from emerging market risks, also weigh on Thai assets. At the same time, there could be some re-allocation of assets away from Thailand as political uncertainty re-emerges in the run-up to the general elections expected early 2019. We could thus see further weakness in the THB in 3Q.

- Yield differentials between 2Y UST and Thai bond, which has narrowed recently, may not persist in the near term. While market expects the Fed to lift its rates further underpinned by strong US data, there is no imminent expectation of a BoT policy normalisation. These expectations should keep both short-end UST supported and Thai bond yields steady. This in turn should led to a re-widening of the gap between the 2Y UST and Thai bond yields, spurring a further re-allocation of assets to higher yielding US assets and buoying the USDTHB in 3Q. A 25bp rate hike is expected sometime in 4Q to begin the monetary policy normalisation process but we doubt that this move would be sufficient to mitigate the risks from politics that could lift the USDTHB higher in 4Q.

- Still, we do not expect further aggressive moves in the USDTHB beyond 3Q. This is because while 3Q tends to be a seasonally strong quarter for the THB vs. the USD as corporates repatriate funds for the fiscal year-end, 4Q is typically a weak quarter for the THB. At the same time, the re-emergence of political risk as the general elections approaches should put upside pressure on the USDTHB in 4Q.

- At the same time, healthy macro-economic fundamentals should continue to underpin the USDTHB and keep the pair from climbing back towards the 34-handle from current levels. In addition, persistent current account surpluses (around 10% of GDP) should be supportive of the THB. At the same time, we are looking for a pick-up in private investment to drive the next phase of growth and the THB higher. Our optimism arises from the high correlation between private investment and trade for Thailand. Thus, this current economic cycle should keep the economy and hence the THB supported. The government's push to accelerate infrastructure projects, especially the USD47bn Eastern Economic Corridor project ahead of general elections, could deliver upside surprises to domestic demand, growth and weigh on the USDTHB.

- However, political risk ahead is likely to weigh on the THB. PM Prayuth has recently indicated that the return to civilian rule could take place on 24 Feb 2019, lifting hopes that the ban on political activities will be removed soon. We believe that the actual date of the elections will take place after the coronation of HM King Vajiralongkorn, the date of which has yet to be confirmed, and the enabling election bills are published in the Royal Gazette, expected sometime in 3Q. Moving forward on the election will be positive for sentiments in the near term, though it could eventually lift political temperature as election fever catches on in early 2019. This should keep investors on the sidelines until political uncertainty dissipates. Such political concerns are likely to put upside pressure on the USDTHB in the next six months.

- Our base scenario is for the general elections to proceed as planned in Feb 2019. We believe that a majority government by a single party is unlikely given the new Constitution. A fractious parliament made up of smaller parties is likely with the Senate dominated by 250 members appointed by the military junta. This should allow the military to retain influence in the government as no single party will be able to command a majority. More likely than not, PM Prayuth should remain as PM as a result. We do not expect any change in economic policy direction and for the BoT to begin policy normalisation in 4Q 2018. Some initial volatility is expected in the aftermath of the election but we expect the THB to stabilise and continue on its appreciation path thereafter.

- Given the return of foreign investors into Thai debt, which weighed on the USDTHB, we have revised our USDTHB forecast to reflect these recent developments. We now expect the USDTHB to end 3Q 2018 at 33-handle (previously 33.50) before climbing higher towards 33.50 (33.80 previously) and 33.80 at end-2018 and 1Q 2019 on elections risk. Thereafter we expect the USDTHB to ease to around the 33.60 (from 33.30 previously) by end-2Q 2019.

- **Growth and Inflation Outlook:** The economy continued to recovery robustly. The economy expanded by 4.6% y/y in 2Q, just off the 1Q pace of +4.9%. Underpinning growth in the quarter was solid private investment, which rose 4.5% (1Q: +3.7%), and pick-up in private investment (2Q: +3.6% y/y vs. 1Q: 3.4%). We expect the recovery to persist for the rest of the year. Government spending, especially ahead of the general elections expected early next year, together with planned infrastructure building projects including transport networks and the Eastern Economic Corridor should continue to bolster growth. We continue to expect the export-led recovery to spark a revival in private investment that should sustain growth in 2018, given the high correlation between export recoveries and machinery & equipment investments for Thailand. Our economic team is penciling full-year growth of 4.5% for 2018.

- Headline inflation picked-up in Jul, rising 1.46% y/y after easing to 1.38% in Jun. Driving consumer prices higher was the rebound in food prices (Jul: +0.02% y/y vs. Jun: -0.03%) and energy cost as reflected in higher transport cost (Jul: +4.4% y/y vs. Jun: 4.14%). Core inflation (headline inflation excl. raw food and energy) though moderated to +0.79% y/y in Jul from +0.83% in Jun. The Commerce Ministry maintained its 2018 headline inflation forecast at 0.8-1.6% with the mid-point at 1.2%. At the same time, it expects 3Q and 4Q inflation to average 1.4% and 1.5% respectively. The BoT inflation forecast remains at 1.1% for 2018 - at the bottom of its 1-4% inflation target range for 2018. Our economic team maintains its 2018 inflation at 1.3%.

- **Monetary Policy Forecast:** The BoT has left its policy rate unchanged at 1.50% since Jun 2015. The last time the policy rate was even lower was during the Great Financial Crisis in 2009 at 1.25%. Despite the policy being on hold for so long, there does not seem to be any sense of urgency in the BoT to normalise policy. This is in contrast to its ASEAN peers who have already begun the process of policy normalisation.

- This accommodative bias of the central bank appears to have coming to an end after robust 2Q GDP print. The BoT Governor Veerathai Santiprabhob was quoted as saying on 20 Aug that “there was less need for an extremely accommodative stance since the recovery in the economy is clearer”. His comments reinforced minutes of the last policy meeting where members of the policy board discussed conditions and appropriate timing to begin normalizing monetary policy”. He however has since walked back on those hawkish comments following the spike in the THB. It was reported that he said that the central bank will consider the THB strength at its next policy meeting and that a rate hike was not imminent. The less hawkish tone sent the USDTHB higher as a result.

- This back-peddling by the governor though only suggests that a rate hike is not imminent. This means that a policy adjustment at its 19 Sep is unlikely. We reiterate that we do not think that there is a need for the central bank to normalise rate currently given benign inflationary pressures. However as growth accelerates back towards potential, a pick-up in inflationary pressures is likely. Accordingly, our economic team continues to look for the BoT to normalise this year and a rate adjustment is expected to take place in 4Q 2018.

- **Latest Fiscal and External Balance Outlook:** After approving a THB63bn spending budget to aid the agriculture sector, the government has approved in principle a THB200bn Southern Infrastructure Plan. Among the projects that were given in-principle approved was a THB34bn dual track railway in Surat Thani province. Still, each project under the Plan will need to submit a proposal to the cabinet for approval. Details regarding the Plan, including how all the projects will be funded, remain scarce.

- The current account surplus ballooned in Jun after narrowing in the previous month, reversing the moderation that started in Mar. The current account surplus rose to USD4.08bn in Jun from USD0.96bn in May. Aside from the larger trade surplus (of USD2.88bn in Jun vs. USD2.69bbn in May), the surplus in the primary and secondary income segments was the primary driver of the larger current account surplus (Jun: +USD1.21bn vs. May: -USD1.74bn). The overall balance of payments recorded a deficit of USD5.29bn in Jun after a surplus of USD0.05bn in. Details for the financial account are unavailable at the moment but larger portfolio outflows are likely to be the main culprit for the deteriorating in the overall BoP in Jun.

- **Key domestic events and issues to watch:** CPI print for Aug on 3 Sep will be watched for further signs of inflationary pressures. At the same time, we have BoT meeting to decide on policy on 19 Sep.

- **Technical Outlook:** Our call (in last month's FX Outlook) for USDTHB to retrace lower towards 32.80 was more than met. Pair traded a low of 32.50 (28 Aug) before the bounce into month-end. Last seen at 32.70 levels. Technical charts suggest rebound risks in the near term possibly towards 33 levels. But underlying bearish momentum remains intact. Bias remains to lean against strength. Support at 32.55 (100 DMA), 32.30.

INR: Rising Brent Brings INR into Unchartered Waters

Forecast	3Q 2018	4Q 2018	1Q 2019	2Q 2019
USDINR	70.00 (--)	69.00 (--)	68.50 (--)	68.20 (--)

No Change to Previous Forecast

- **Motivation for the FX View:** USDINR remains in a tight range recently and the recovery in the brent crude oil continues to buoy the pair. While most of other Asian FX benefitted from the 10-figure plunge in the USDCNH and USDCNY on 24th Aug, USDINR remained stubbornly elevated. This pair had been buoyed by the rising brent, as market players bid the crude on NAFTA optimism as well as expectations of Iranian supply disruption risk due to US sanctions. In Aug, rupee was also hurt by Jul trade deficit which widened more than expected to U$17.9bn from previous U$17.5bn since May 2013. This brings to mind the time when rupee was hammered by Bernanke-triggered "taper tantrums" and the currency was considered as one of the "Fragile Five" – a group of nations penalized because of their twin deficits. INR remains increasingly vulnerable with higher brent threatening the current account deficit. Elevated oil prices, gold prices and a weaker currency feeds into a vicious circle and impact on purchasing power, wages and household consumption limits RBI's room to hike.

- For a central bank that has been rather hawkish on inflation for a long time, RBI seems unwilling to hike much more. While the lower prospect of a rate hike should encourage investors to hold on to their rupee bonds, weaker fundamentals continue to dampen the appetite for it. The last hike of 25 bps on 1st Aug was meant to stem the INR from further depreciation. However, barring further escalation in the US-China trade war, the peaks of the USD are likely to have been established. While we do not want to rule out further ventures into unchartered waters at 72-figure and 73-figure, our bias for USD is to the downside and we could see USDINR end the quarter near to our forecast at 70.00.

- **Growth and Inflation Outlook:** Industrial production quickened to 7.0%y/y for Jun from previous 3.2%, well above expectations. However, the bounce in the output growth was also due to a low base in Jun 2017 and could taper off as the base effects fade into the next month. According to the RBI forecast based on the industrial outlook survey, order books continue to trend lower for the quarter ending Sep. Household consumption could be hurt by lower rupee, rising energy prices and concomitant increasing price pressures.

- Food inflation softened in Jul, bringing the headline CPI down to 4.17%y/y from previous 4.92%. However, apart from the flooding situation in Kerala, monsoon rain levels have been in deficit for the rest of India and that could have some impact on agriculture output and also caps household consumption. In addition, the flooding is projected to affect the harvest of rubber.

- Trade deficit has increased rather persistently from Apr to Jun and net-exports could be a drag on growth headline. With the US still waging a trade war with China that started in Jul, net exports could become a bigger drag on the headline for 3Q growth.
- **Monetary Policy Forecast:** Our view for a rate hike on 1st Aug came to fruit but we think this could be the start of an extended pause. There is an increasing disparity in opinions on growth conditions amongst the MPC members stated in the Minutes of the Aug meeting. Dholakia takes the decline in capacity utilization as a sign of widening output gap while some others expect closing of the output gap to increase inflationary pressure. We do not think the next hike would come as easy as the ones so far. Our view is that RBI is unlikely to raise cost of financing for the sake of defending the rupee as that could risk dampening consumption and investment. Current data suggests manufacturing growth and industrial activity are already subdued.
- In fact, comments by the government and the central bank suggest that they do not seem very concerned with the currency weakness though the central bank assured today (29 Aug) that it will continue FX operations and intervention to curb undue swings. That increases the likelihood that RBI would not resort to rate hikes to support the rupee.
- Managing inflation is still the mandate of the RBI and recent inflation prints have softened. That should take the pressure off the central bank to raise rates. However, the small deficit of 6% in the rainfall level still warrants a watch on food inflation which has brought down the consumer price index.
- **Latest Fiscal and External Balance Outlook:** With the price of brent crude still rather elevated, current account is still at risk of further deterioration. Finance Minister announced that the fiscal deficit for FY17 is poised to come in at 3.5%, well above the 3.2% projected as tax collections following the implementation of GST was lower than expected. The RBI also released a report on the states budget, reporting that the consolidated gross fiscal deficit overshot the budget estimates in 2017-18 due to shortfalls in own tax revenues and higher revenue expenditure. For the coming year, the government estimates fiscal deficit to improve to 3.3%.
- **Key domestic events and issues to watch:** 2Q GDP on 31st Aug; PMI-mfg on 3rd Sep; current account balance for 2Q between 5-28th Sep; Aug CPI and Jul IP on 12th; trade on 12-15th; WPI on 14th.
- **Technical outlook:** 1M NDF remains rather biased to the upside, last seen around 71.20. Momentum is increasingly bullish for this pair. A break of the 2015 high of 69.43 could see a potential test of 71.30. This pair is heading into unchartered waters. Next key level is 72 and then perhaps 73. Support at 69.50.

VND: Still Vulnerable

Forecast	3Q 2018	4Q 2018	1Q 2019	2Q 2019
USDVND	23100 (--)	23000 (--)	22900 (--)	22800 (--)

No Change to Previous Forecasts

- **Motivation for the FX View:** We remain optimistic that the dong could strengthen towards 23100 from the current levels at around 23300 vs. the USD. We see some likelihood that the USD has peaked for the quarter and further unwinding of long USD positions could press the USDVND lower in tandem with the rest of USDAxJ.

- We are long-term positive on the VND and that also explains our bias for VND to strengthen should anything positive come out of the US-China trade war. Moody's upgraded Vietnam's long term credit rating by 1 notch from B1 to Ba3, citing strong growth potential supported by increasingly efficient use of labour and capital in the economy. The rating agency also noted the improvements in the health of the banking sector that Moody's expects to be maintained, albeit from relatively weak levels". The upgrade brings its rating to par with the BB- rating given by S&P, but still a notch lower compared to Fitch's BB. Following Moody's upgrade, Deputy Head of National Financial Supervisory Commission said that Vietnamese lenders need to improve credit access for businesses as up to 60% of SMEs borrow from unofficial lenders at very high interest rates. Invigorated by the Moody's rating upgrade, the Deputy PM Vuong Dinh Hue (on 29 Aug) urged the SBV to resolve NPLs owned by credit institutions and the Viet Nam Asset Management Company to below 3% by 2020. Earlier this month, Deputy PM Vuong Dinh Hue also pledged that the government will sell more long-term bonds in domestic market and cut foreign borrowing to lower forex risks. Barring further escalation in the trade war, foreign investors could be attracted to the strong growth potential of Vietnam and possibly stronger institutions that the government is trying to establish. This is a long-term positive for the VND.

- Another reason to be long-term positive on the VND, albeit not new, SBV was cited by a local press saying that the foreign currency deposit ratio is to be reduced to below 7.5% of money supply by 2020 from 8.21% end of last year and then to 5% b 2030. Foreign-currency lending should stop by 2030 as well. This is meant to stamp out dollarization and could support the dong in the long term.

- Foreign companies continue to show interest to invest in Vietnam with an approval just granted to Janakuasa Pte and 2 other unnamed investors to develop a 78MW wind power farm in Mekong Delta province of Tra Vin - an investment of nearly U$150mn. Construction to start in 1H 2019 with electricity generation likely in early 2020. FDI slowed in Aug however and that could be a sign of concern on the trade war front. That explains the weakness in the VND for the month.

- For a country that is so reliant on trade and exposed to China and the US, the ongoing trade war between the US and China remains a downside risk for the VND. That explains the outflow seen in the equity markets. We look for the USDVND to remain a tad biased to the upside but could find some relief thereafter should trade tensions subside along with the US mid-term elections and we look for a mild retracement towards 23000 towards the end of the year.
- **Growth and Inflation Outlook:** Markit reported a strong print for the manufacturing sector at 54.9 for Jul albeit softer than the previous 55.7. According to the details of the report, output remains on the expansion though momentum eased from those seen in the previous month. Industrial production for Aug came in at a rather decent 13.4%y/y, slowing a tad from the previous 14.3%. Breakdown reveals that the heavily weighted manufacturing sector maintained a steady growth of 15.4%y/y while electricity and gas output slipped from 18.0%y/y to 13.5%. FDI inflow slowed in Aug though the consistent increase in FDI could continue to support the VND. While visitor arrivals actually slowed significantly in the month, retail sales accelerated slightly, underscoring the strong household consumption. The wage growth averages around 7%y/y since 2015 and that could continue to support private consumption.
- Vietnam also plans to expand offerings in its derivative markets to include underlying assets such as oil and agricultural products to attract more foreign investors although Chairman Nguyen Thanh Long did not indicate a time frame.
- The CPI in Aug slipped less than the expected 3.90%y/y to 3.98% from the previous 4.46%. Food inflation slowed along with the transportation, housing and construction materials and health and personal care subcomponents. With inflation easing, we see less need for a rate hike. The government could continue to use policies and administration to keep prices in check. The legislature targets a cap of 4% for CPI.
- **Monetary Policy Forecast:** As other central banks in the region hiked rates to buffer against further currency weakness that threatens their inflation outlook, there seem to be some speculation that SBV could do the same. However, the recent inflation data for Vietnam suggest that price pressures are still in control and are unlikely to dampen consumption. As such, SBV should be less motivated to hike rates. Furthermore, FDI has slowed in Aug with U$276.15mn recorded for the month vs U$1406mn in the month prior. With a trade war still on between the US and China, we do not think it is a favourable environment to raise cost of financing for businesses. As such, we hold our view that policy rates are unlikely to change for the rest of the year.
- In terms of NEER, VND has depreciated a tad from where it was in Jul. This was probably due to strong recovery in the heavily weighted RMB that was not matched by the VND. In terms of NEER, VND has gained significant competitiveness compared to its trading partners and that could buffer Vietnam's exports in a trade war environment.

- **Latest Fiscal and External Balance Outlook:** Vietnam's fiscal position is likely to remain in consolidation mode as fiscal deficit remains wide. The National Assembly stated that the average state budget deficit planned is estimated to be 3.7% of GDP for 2018 and NFSC commented earlier this month that the budget is on track to meet that target set. The government needs to fund state budget deficit of VND 206.15trn and pay principal loans of CNY157.13trn this year. The government aims to reduce budget deficit to 3.5% of GDP by 2020.

- Current account recorded an increase to USD4.3bn in 2Q from the previous U$3.9bn. Net trade surplus of goods rose to U$5.2bn from previous U$4.9bn. The competitive dong could keep the current account in surplus. Financial account surplus narrowed to U$3bn. Overall balance of payments records a surplus and could support the VND.

- **Key Domestic Events and Issues to Watch:** PMI Mfg on the 3rd; domestic vehicle sales in 6th-13th; CPI, trade numbers, retail sales, IP and 3Q GDP are due 25th-30th Sep.

FX Forecasts

	End Q3-18	End Q4-18	End Q1-19	End Q2-19
USD/JPY	113	112	111	111
EUR/USD	1.1700	1.1900	1.2000	1.2200
GBP/USD	1.3200	1.3400	1.3200	1.3500
AUD/USD	0.7400	0.7500	0.7600	0.7800
NZD/USD	0.6700	0.6800	0.7000	0.7200
USD/SGD	1.3750	1.3650	1.3650	1.3600
USD/MYR	4.08	4.07	4.05	4.05
USD/IDR	14750	14600	14500	14300
USD/THB	33.00	33.50	33.80	33.60
USD/PHP	54.00	53.50	54.00	53.90
USD/CNY	6.75	6.72	6.65	6.62
USD/HKD	7.85	7.85	7.80	7.80
USD/TWD	30.80	30.60	30.50	30.40
USD/KRW	1120	1110	1100	1090
USD/INR	70.00	69.00	68.50	68.20
USD/VND	23100	23000	22900	22800
DXY Index	94.83	93.50	92.87	91.69
SGD Crosses	End Q3-18	End Q4-18	End Q1-19	End Q2-19
SGD/MYR	2.9673	2.9817	2.9670	2.9779
SGD/IDR	10727	10696	10623	10515
SGD/THB	24.00	24.54	24.76	24.71
SGD/PHP	39.27	39.19	39.56	39.63
SGD/CNY	4.91	4.92	4.87	4.87
SGD/HKD	5.71	5.75	5.71	5.74
SGD/TWD	22.40	22.42	22.34	22.35
SGD/KRW	815	813	806	801
SGD/INR	50.91	50.55	50.18	50.15
MYR Crosses	End Q3-18	End Q4-18	End Q1-19	End Q2-19
EUR/MYR	4.77	4.84	4.86	4.94
JPY/MYR	3.61	3.63	3.65	3.65
MYR/HKD	1.92	1.93	1.93	1.93
MYR/CNY	1.65	1.65	1.64	1.63
GBP/MYR	5.39	5.45	5.35	5.47
AUD/MYR	3.02	3.05	3.08	3.16
NZD/MYR	2.73	2.77	2.84	2.92
MYR/IDR	3615	3587	3580	3531
MYR/INR	17.16	16.95	16.91	16.84
MYR/KRW	274.51	272.73	271.60	269.14
MYR/PHP	13.24	13.14	13.33	13.31
CNY/MYR	0.6044	0.6057	0.6090	0.6118

Source: Maybank FX Research as of 31 August 2018

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

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Published by:

Malayan Banking Berhad
(Incorporated in Malaysia)

Saktiandi Supaat
Head, FX Research
saktiandi@maybank.com.sg
(+65) 63201379

Christopher Wong
Senior FX Strategist
wongkl@maybank.com.sg
(+65) 63201347

Fiona Lim
Senior FX Strategist
Fionalim@maybank.com.sg
(+65) 63201374

Leslie Tang
Senior FX Strategist
leslietang@maybank.com.sg
(+65) 63201378