FX Thoughts -
End In Sight for Monetary Stimulus?

FX Research & Strategy| Global Markets
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Overview

1. End in Sight for Monetary Stimulus?
   — *Policy Divergence-Convergence Play*
   — *A Deterioration in Risk Sentiment?*
   — *Fed Still the only Central Bank in the Midst of Monetary Policy Normalisation*

2. Our House View on FX
   - USD – Modest Strength; Markets Still Underpricing Fed's Normalization plans
   - EUR – Unwinding of Monetary Policy Divergence Trade
   - GBP – Politics Take a Back Seat as Focus Switches Back to BoE Tightening
   - JPY – Funding Currency of Choice as BoJ shows No Intent to Adjust Monetary Policy Bias
   - AUD – Modest Up-move Towards 0.80; Iron Ore Prices to Support AUD
   - CNY – Expect Further Weakness
   - MYR – Positive Outlook thanks to Improving Domestic Drivers, Oil Prices
   - SGD – Expect Modest Depreciation Pressure Ahead

3. Strategic/ Tactical Plays

4. Concluding Remarks

End In Sight for Monetary Stimulus?

Central Bankers' Hawkish Remarks - A Wake Up Call?

ECB Forum (26 - 28 Jun 2017)

ECB Draghi:
"Deflationary forces is gone and reflationary forces are at play"

"Our analysis suggests that the drivers of low oil prices at present are mainly supply factors, which a central bank can typically look through"
~ 27 June 2017

BoE Carney… *would vote to tighten monetary policy if business investments begin to rise and offset weaker consumption*

BOE Haldane

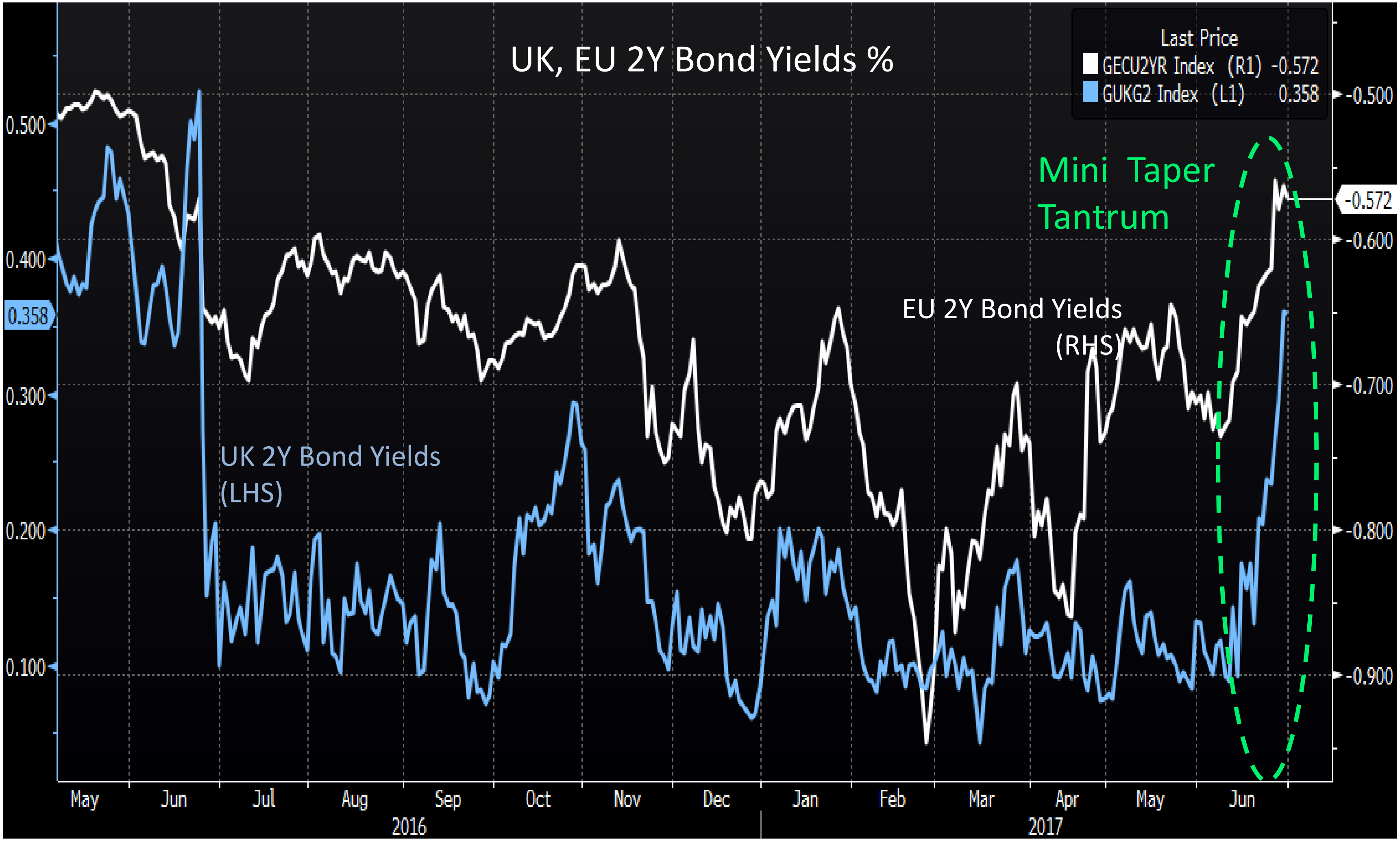
"BOE needs to look seriously at raising rates" ~ 29 June 2017

BoC Poloz:
"It does look as though those cuts have done their job. We're just approaching a new interest rate decision, so I don't want to prejudge that, capacity – excess capacity – is being used up steadily."
~ 27 June 2017

Source: Bloomberg, Maybank FX Research

End in Sight for Monetary Stimulus

EU, UK Bond Yields Jumped to One-Year High in Response



Source: Bloomberg, Maybank FX Research

Mixed Response on FX Markets…

Hawkish assessment of economic outlook and expression of interests to remove some degree of monetary stimulus have resulted in majors' bond yields and currencies surging at the expense of the USD.

There are 3 immediate repercussions:

1. ECB, BoE, BoC's monetary policy divergence with the Fed will slow and perhaps even converge at some point later. This **initial shift is expected to weigh on the USD** and **support the EUR, GBP, CAD** for now;

2. Withdrawal of monetary stimulus should **tighten monetary conditions and weigh on risk sentiment**, exerting **downside pressure on Asian currencies** (i.e. KRW, TWD, PHP, THB,) that are typically sensitive to risk sentiment;

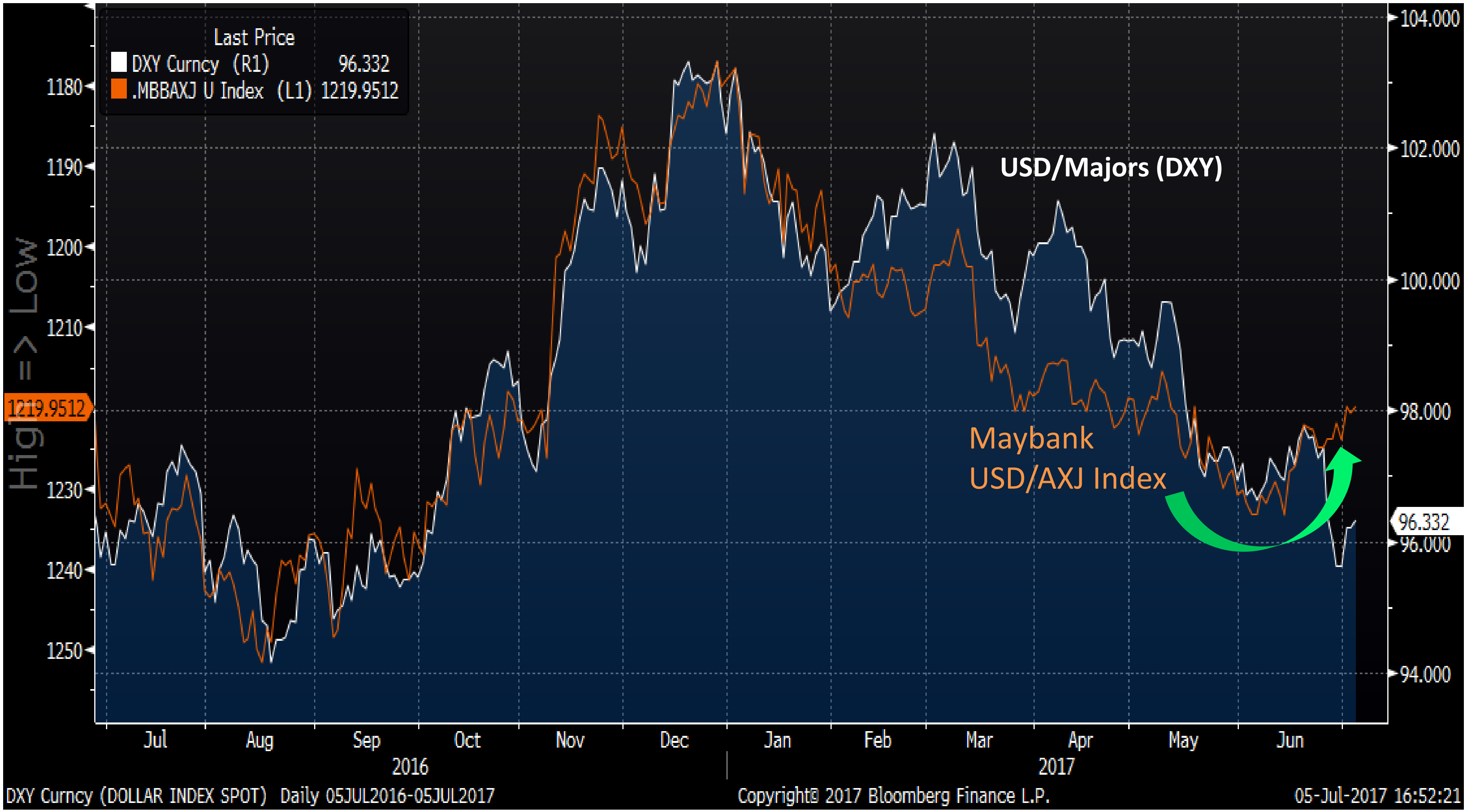
3. **Ongoing monetary policy divergence between BoJ and Fed** should add to **upward pressure for USDJPY**

USD Temporary Weakness vs Majors but Strength vs. Asian Currencies

Note: Spot Returns in % Change from start of ECB forum 26 Jun 2017 to 3 Jul 2017
Source: Bloomberg, Maybank FX Research

End in Sight for Monetary Stimulus

USD Performance Differs Across Regions

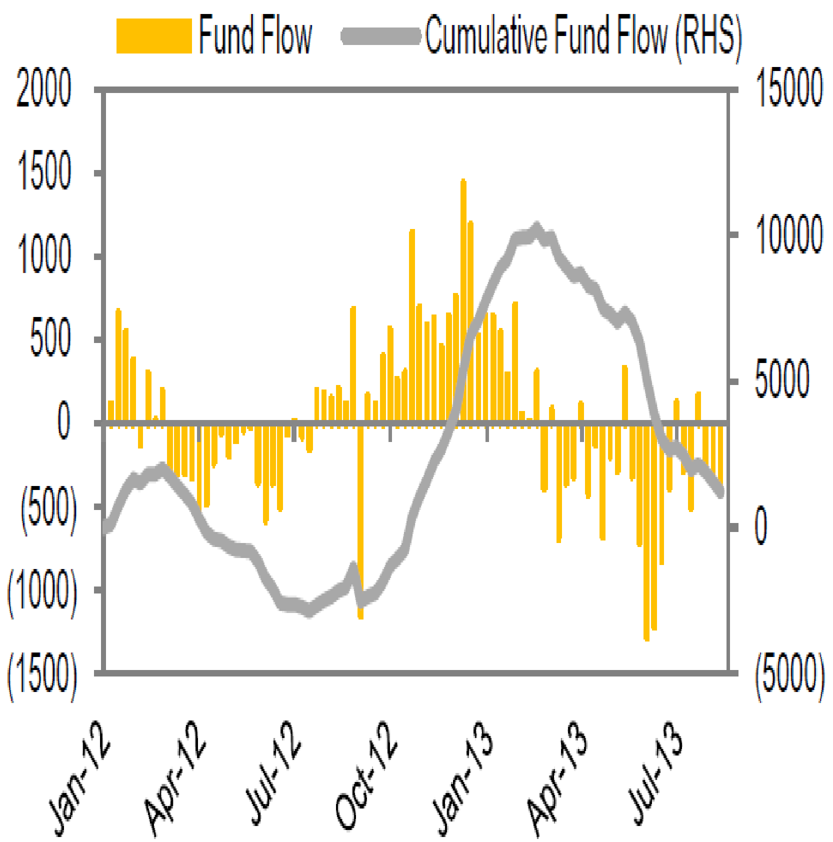


Note: Maybank USDAXJ index comprises of USD vs. CNH, IDR, INR, KRW, MYR, PHP, SGD, THB, TWD, equally weighted
Source: Bloomberg, Maybank FX Research

Taper Tantrum in 2013 Showed EM Outflow and Currency Weakness

Inflows to EM Assets Slumped

AXJ Weekly Fund Flow (USD mil)



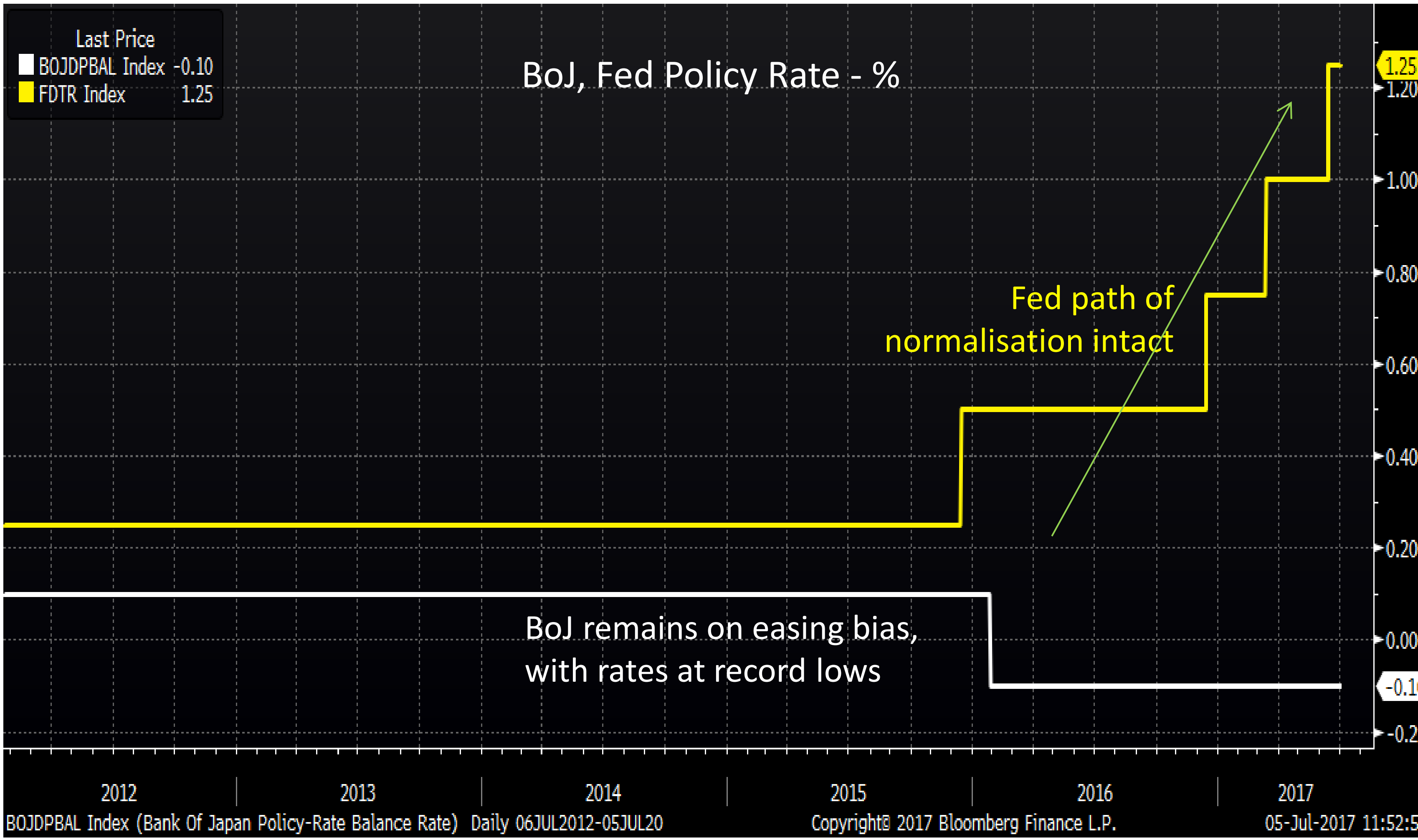
IDR, THB, PHP, MYR Depreciated Sharply

Currency Changes vs USD
(Indexed to 100: May 2013)

Source: EPFR, Bloomberg, Maybank FX Research, Maybank KE

End in Sight for Monetary Stimulus

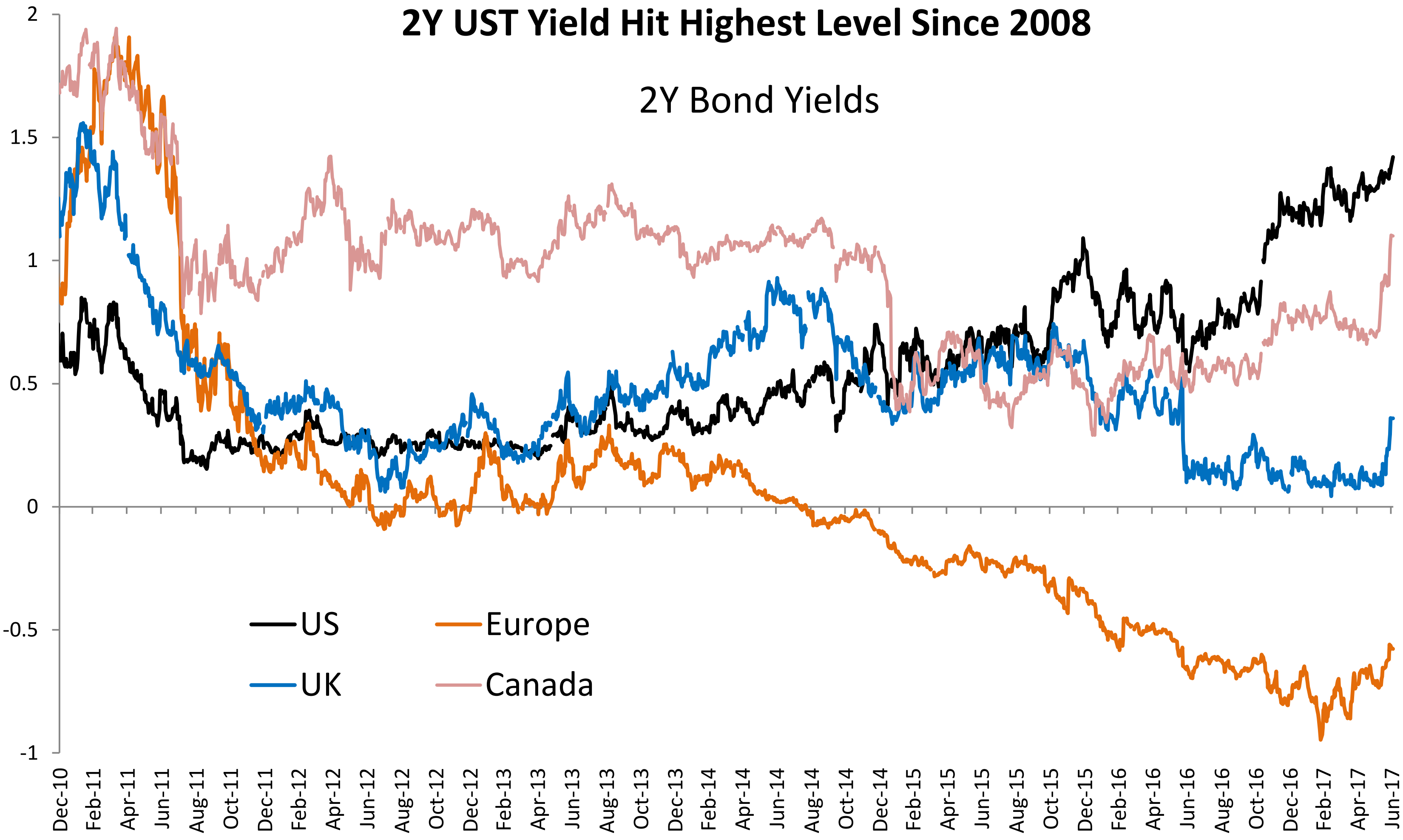
Growing Divergence of Policy between Fed and BoJ Keeps USDJPY Supported



Source: Bloomberg, Maybank FX Research

End in Sight for Monetary Stimulus

But Fed Still the Only Major Central Bank Normalizing Monetary Policies



Source: Bloomberg, Maybank FX Research

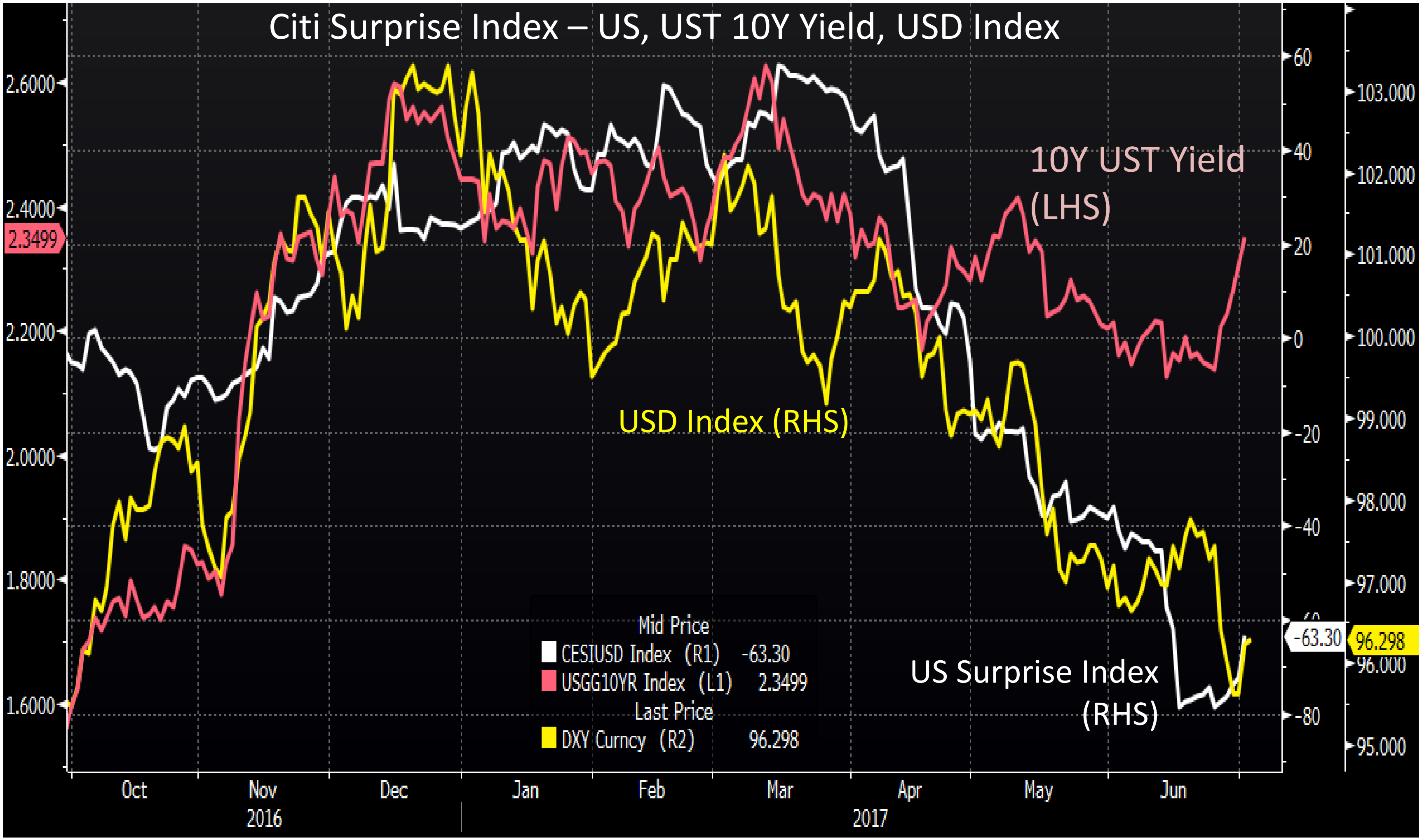
Our House View on FX

USD: Policy Normalisation and Strong Growth to Support USD

- We caution that **markets may be running the risk of underestimating the Fed's willingness** to withdraw monetary stimulus from the system.
  - Market expectation for Fed rate hike trajectory beyond 2017 is clearly out of step with Fed's forward guidance (Markets are pricing in about 1 hike each for 2018 and 2019 while Fed is expecting about 3 hikes each for 2018 and 2019.
  - Fed Chair Yellen dismissed the moderation in price pressures as transitionary and tightness in Labour market should translate into higher wage cost going forward
  - Economic recovery remains intact
  - Loose Financial conditions and supported asset prices should encourage the Fed to tighten
- **Price and consumer spending-related data** will be the key signposts to watch – Upside surprise should lead markets to re-think positioning for USTs and USD
- **Balance sheet unwinding should also have some tightening effect on financial conditions** index (another key signpost to watch)
- Maintain Modest USD Strength Ahead

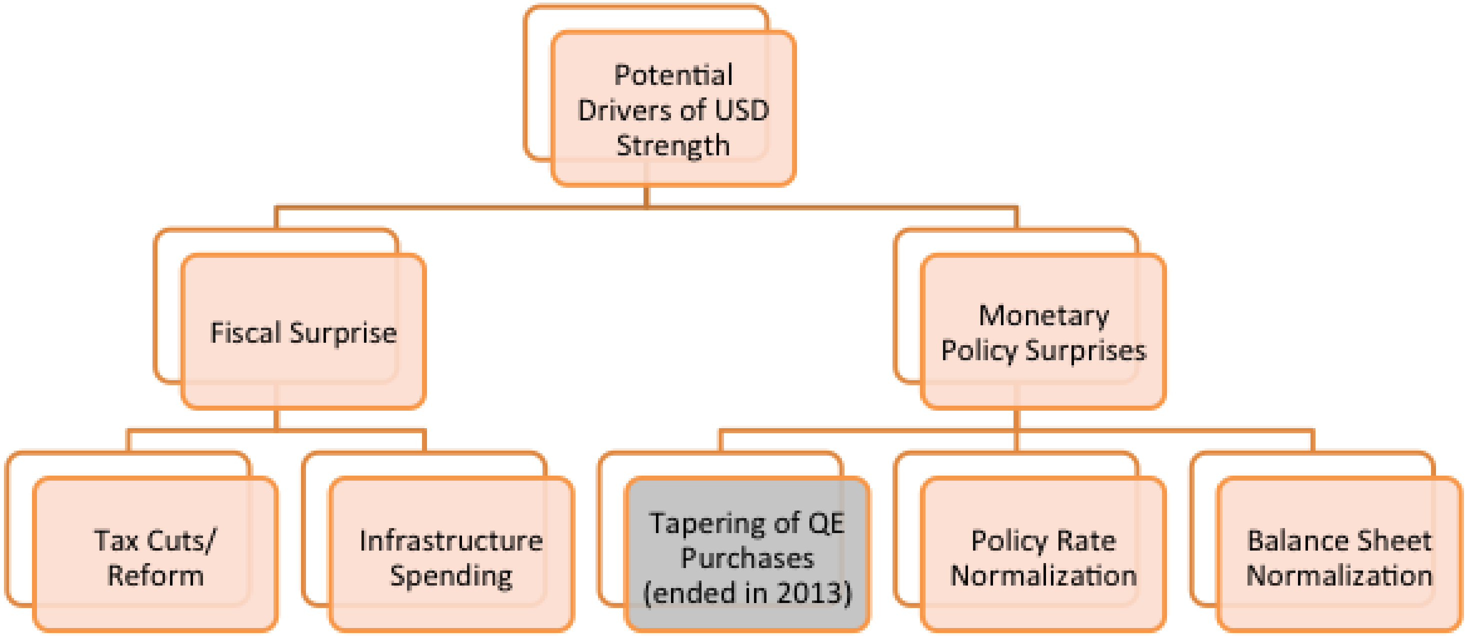
House View on the USD

Upside Surprise to US Economic Data to Support UST Yields and USD Strength



Source: Bloomberg, Maybank FX Research

Where Can USD Strength Come From?



Increase Consumption, Investment, Higher Growth, Higher Inflation,

↓

Tighten Monetary Policy

↓

Higher UST yields, UST curve to steepen

Source: Maybank FX Research

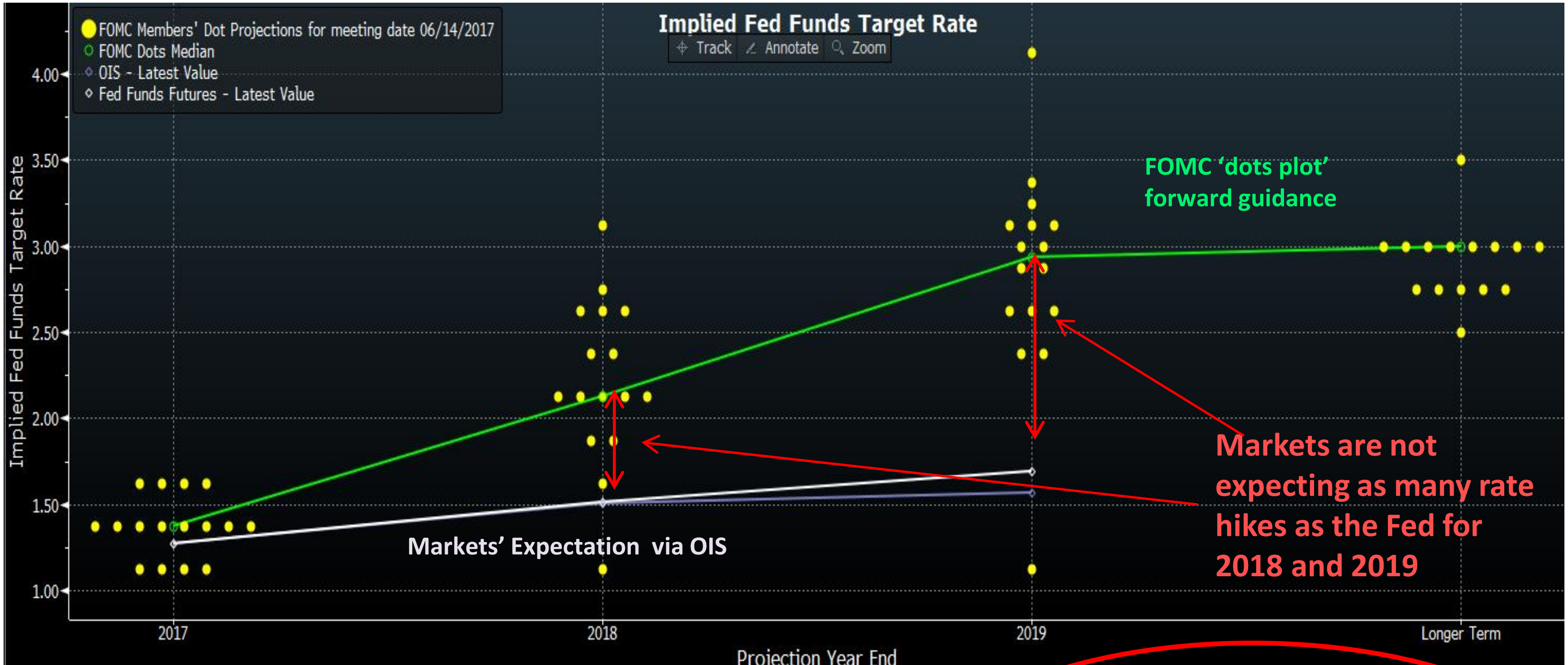
- From 1 hike/ year in 2015, 2016 to potentially 1 hike/ quarter in 2017
- For 2018 & 2019, markets are far underpricing Fed's rate projections, pricing in 30bps increase vs. Fed's 75 bps.

=> Eventual re-pricing of Fed Rate hike Could lead to Additional USD Gains

- Details are sketchy at this stage. Fed may announce b/s reduction end 2017.
- An increase in B/S (via QE) pushed yields to record lows.
- A reversal of that could lead to further tightening in financial conditions resulting in **higher bond yields, stronger USD.**

Markets Yet to Buy Fed's Schedule of Policy Normalization

Eventual Shift in Market Expectation to Support UST Yields and USD Strength

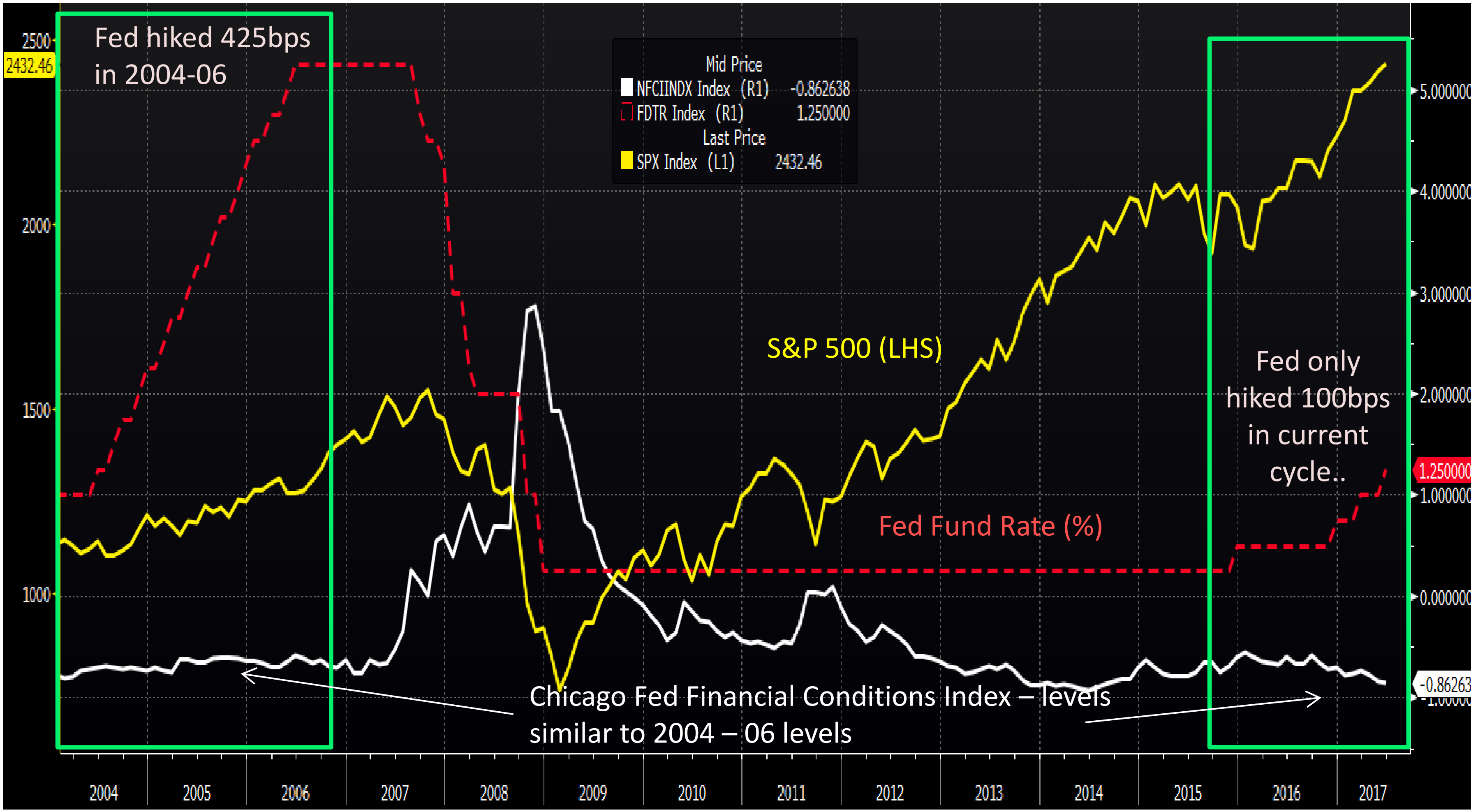


	End 2018	End 2019
FOMC (Dots Plot)	+75bps	+81bps
Markets (implied from OIS)	+24bps	+6bps
Markets Under-pricing Fed's Forward Guidance	51bps	78bps

Source: Bloomberg, Maybank FX Research

Market Conditions Remain Favorable for Fed to Tighten Monetary Policy

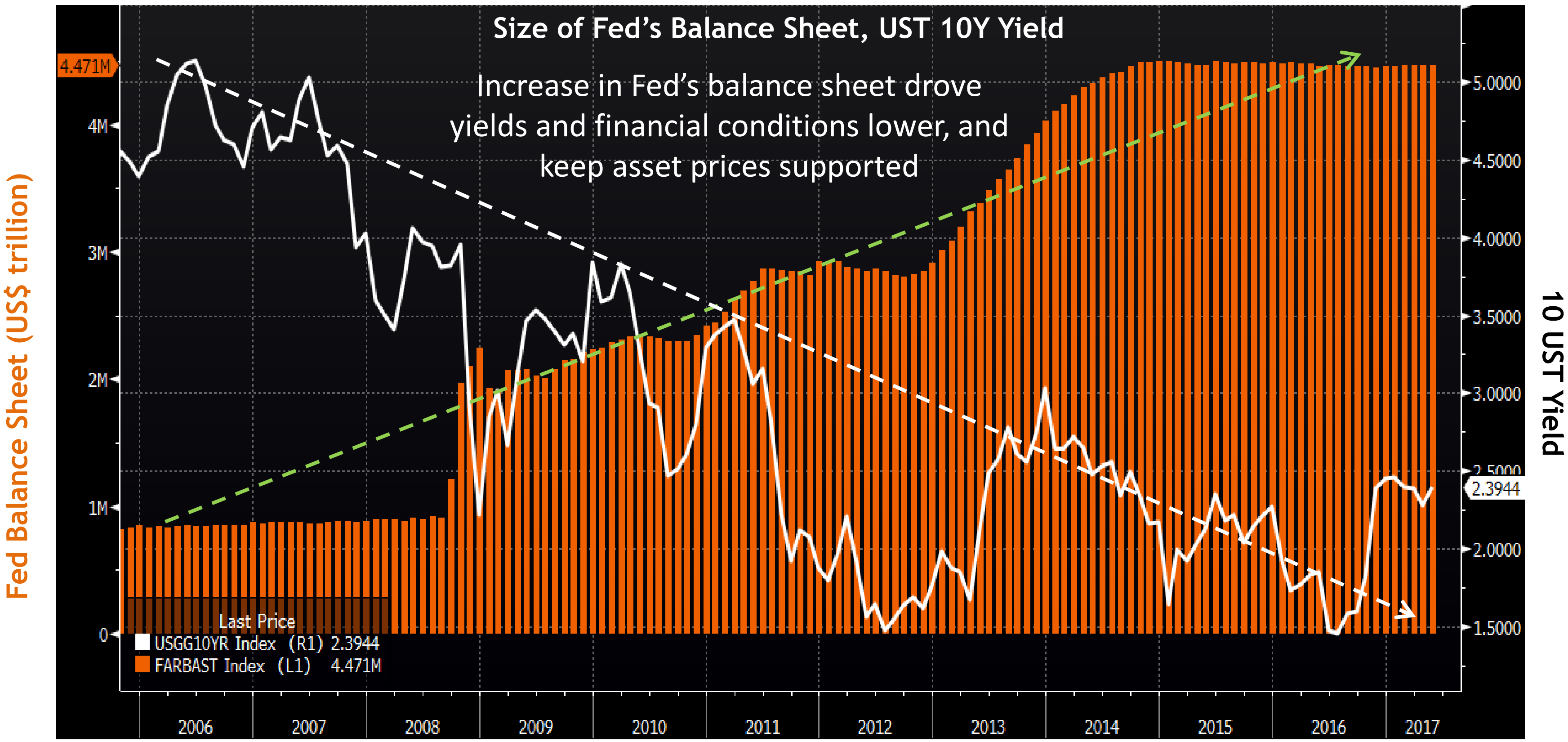
Financial Conditions at record lows and equity markets continue to make new highs



Source: Bloomberg, Maybank FX Research

Balance Sheet Reduction -> Tightening of FCI -> Higher Rates

Rates Driven Lower as Fed's Balance Sheet Increased; Reduction in B/S to drive Rates Higher



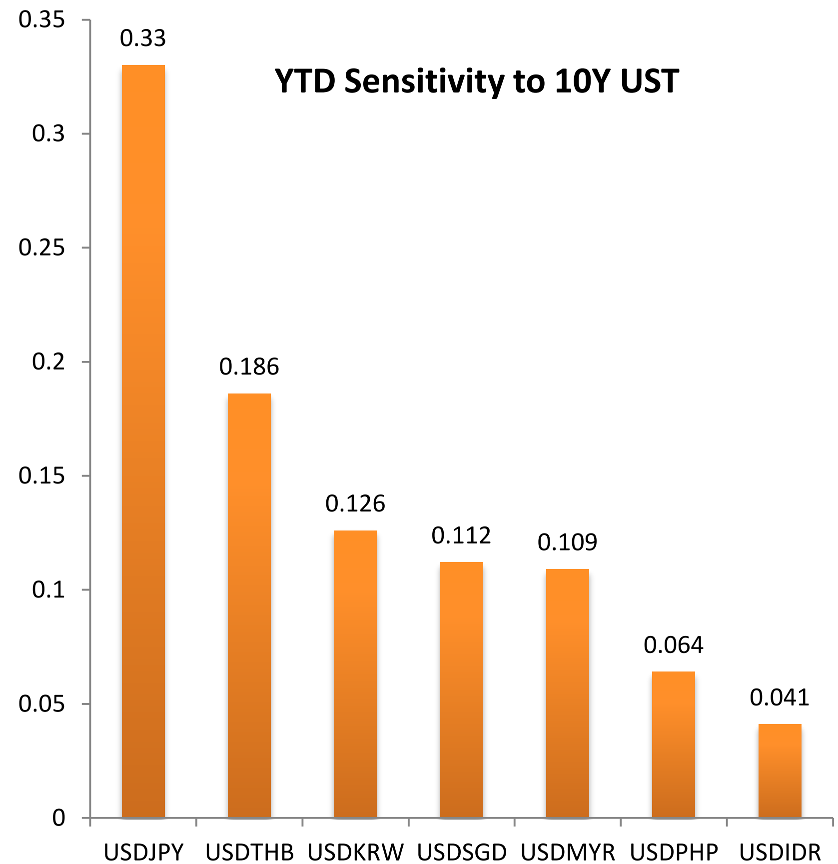
$675 billion reduction in the Fed's balance sheet over a two-year horizon is about **equivalent to a 25 basis point hike** in the funds rate [Kansas Fed, 10 May 2017]

Source: Bloomberg, Federal Reserve Bank of Kansas City, Maybank FX Research

Higher UST Yields Could Lead to Higher USD/AXJs

UST Yield and DXY Remain Positively Correlated; Higher UST Yield could lead to strong USD

USDJPY, USDTHB, USDKRW and USDSGD Most Sensitive to Increases in UST Yields



Source: Bloomberg, Maybank FX Research

EUR: Supported on Dips

1. **Negativity Surrounding EUR Dissipating**
   - Political risks in Euro-area receding
   - Sustained signs of economic recovery broadening
   - Rising Expectation that ECB may signal some removal of monetary stimulus

2. **Downside Factors that Could Limit EUR Gains**
   - Subdued core inflation persisting
   - ECB's hawkish talk does not translate into tapering/tightening action
   - Upcoming German Elections (Sep) and risk of Italy calling for early elections

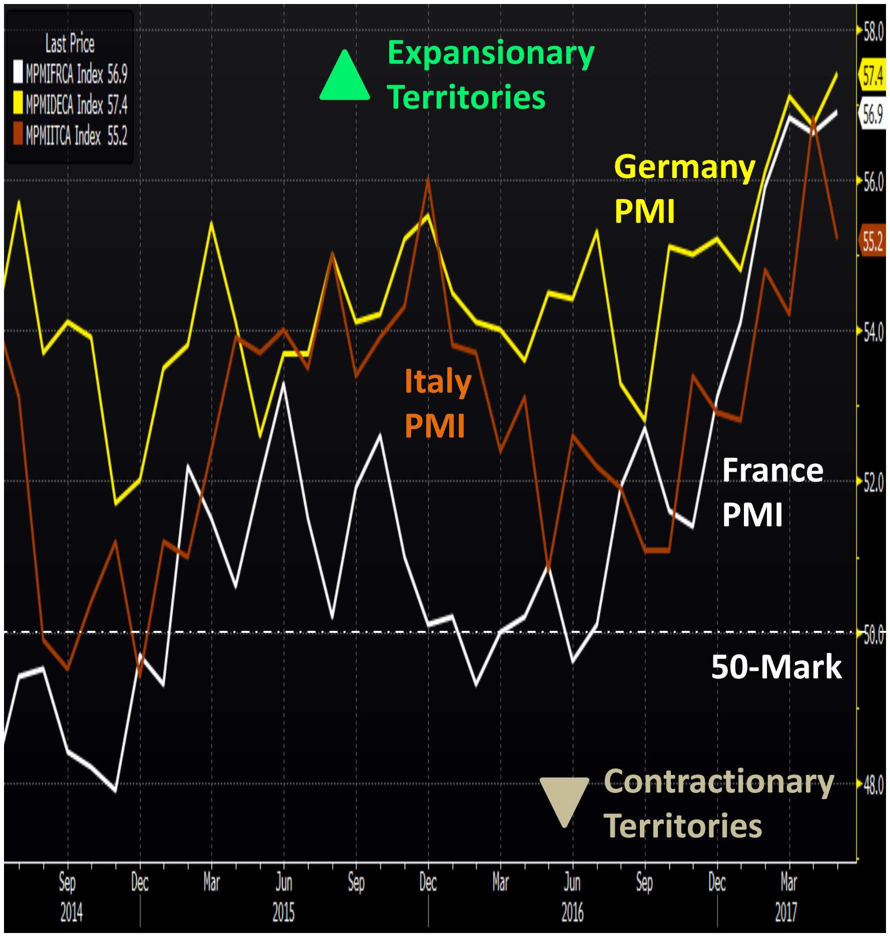
3. **Strategy**
   - Maintain Long EURJPY as core strategic trade for 2017 on monetary policy divergence between ECB and BoJ

Forecast	3Q 2017	4Q 2017	1Q 2018	2Q 2018	End 2018
EUR/USD	1.1250	1.1400	1.1500	1.1300	1.1200

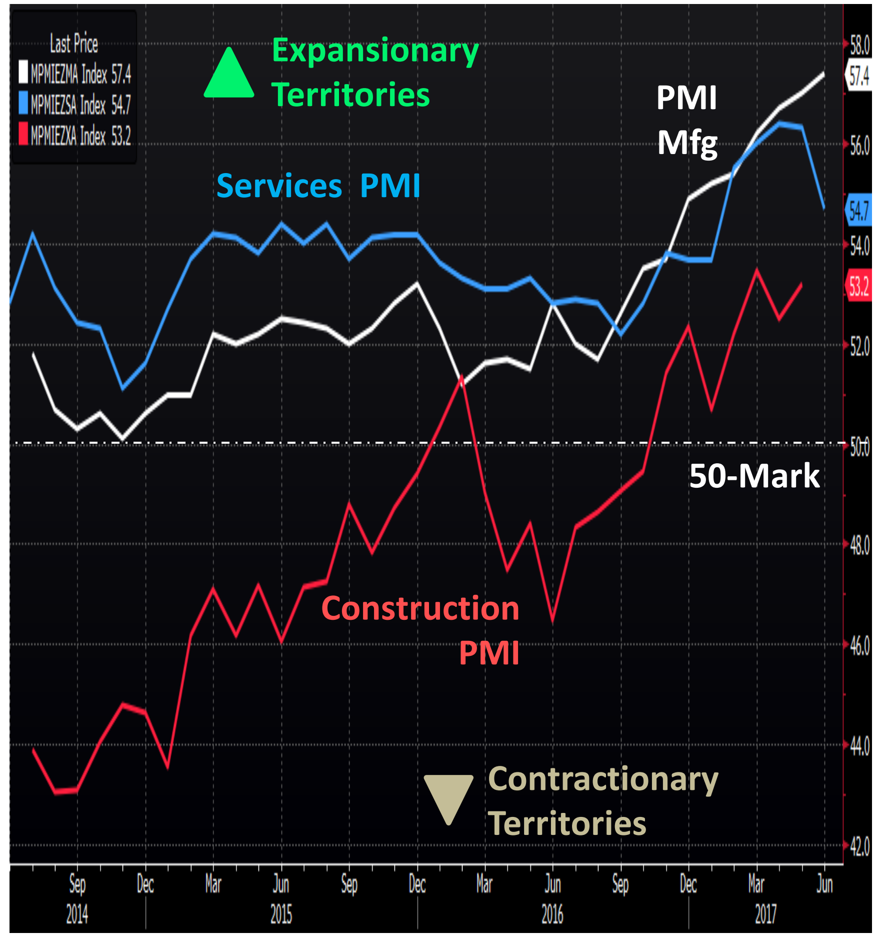
House View on the EUR

Euro-Area Recovery Broadening…

… Across Geographies



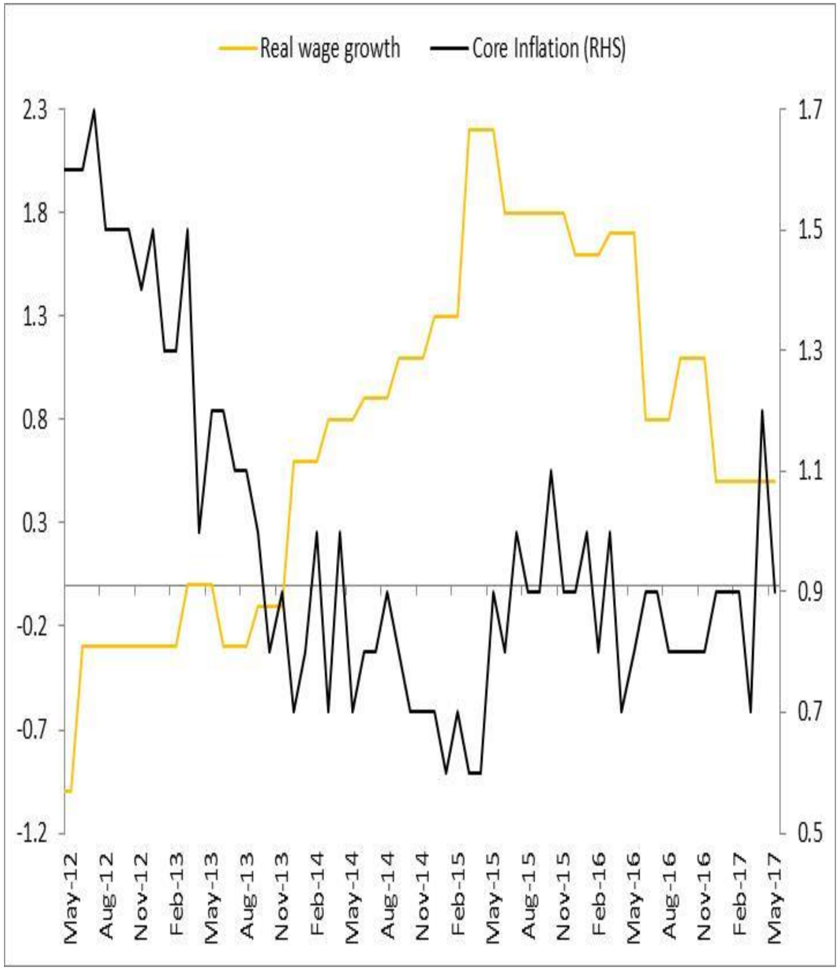
…and Across Sectors



Source: Bloomberg, Maybank FX Research

But Inflationary Pressures and Wage Growth Remain Subdued

Core Inflation and Real Wage Growth Still Subdued, owing to labor market slack and labor market reforms

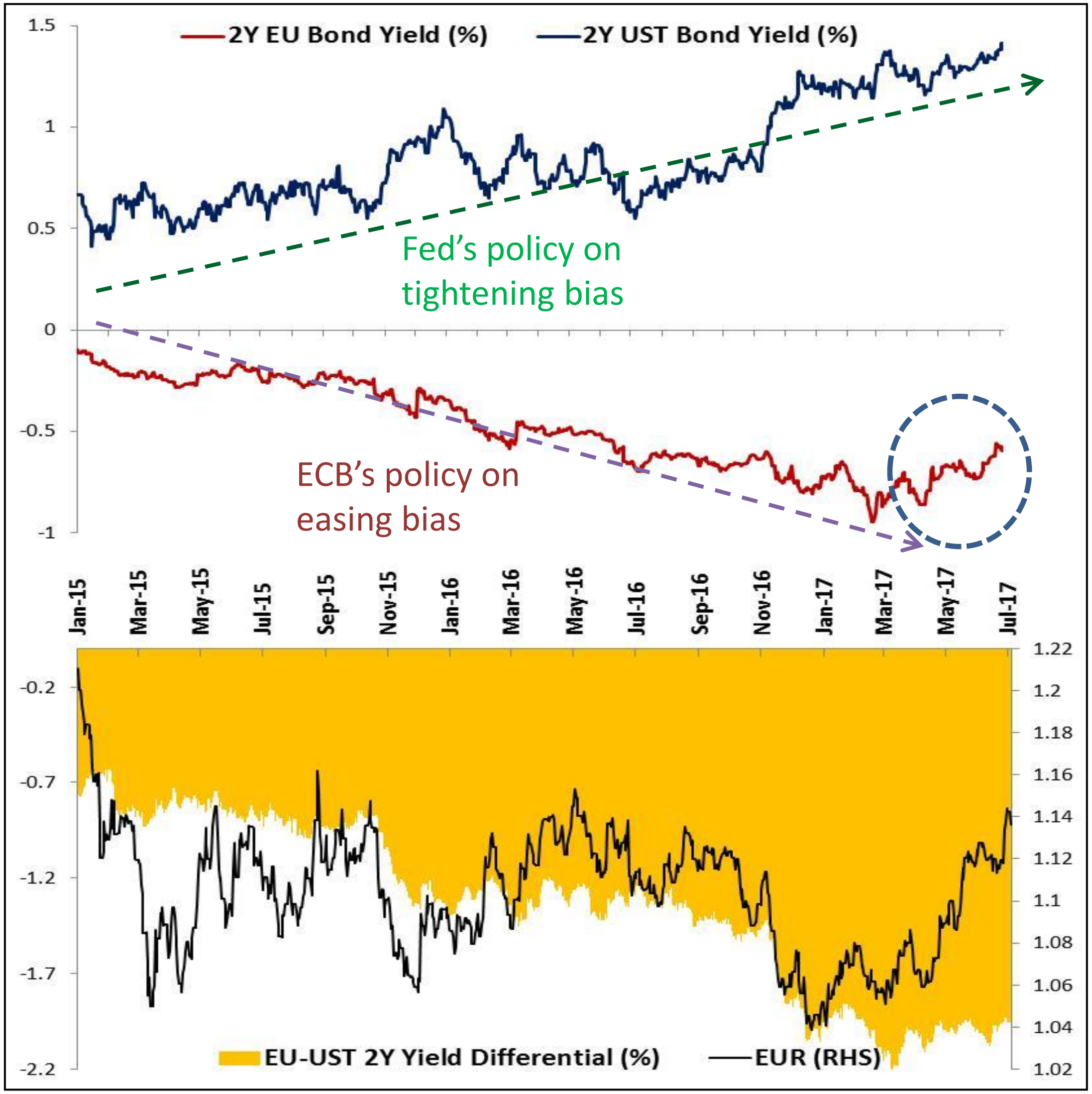


Built-up of Pipeline Pressures but market-based measure of longer-term inflation declined

Source: Bloomberg, Maybank FX Research

House View on the EUR

Slowing Policy Divergence Negates EUR Downside Pressure



Source: Bloomberg, Maybank FX Research

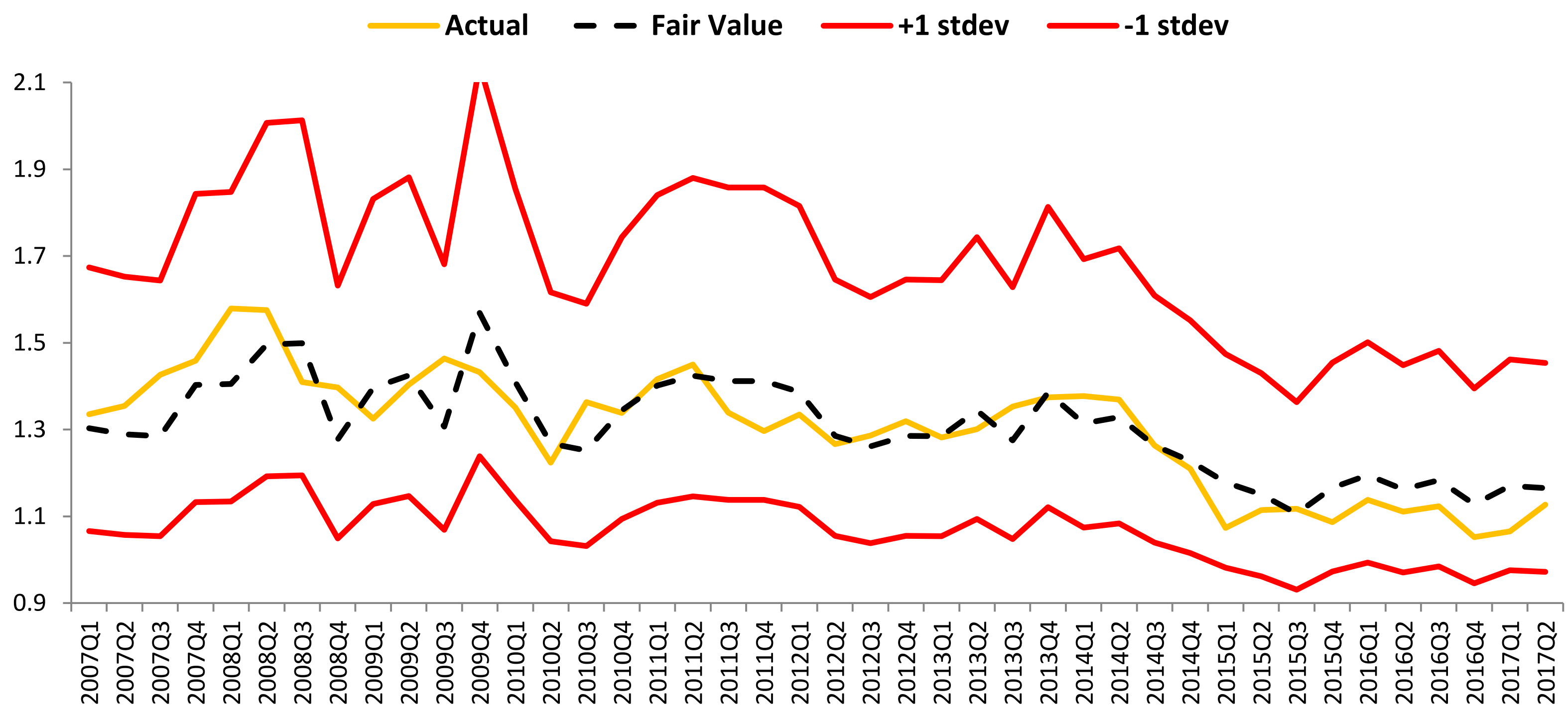
- Monetary policy divergence between the Fed remains
  - Fed on path towards normalization
  - ECB still doing QE
- But ECB's recent stance on inflation suggests an inclination towards withdrawal of monetary stimulus

=> Slowing policy divergence negates EUR negativity

- But we caution that markets may have ran ahead of fundamentals as ECB still urges persistency in accommodative monetary policies and inflation remains subdued
- Markets disappointment with ECB should limit EUR gains -> EUR correction could re-visit 1.12 levels

House View on the EUR

EUR Fair Value around 1.1650



EUR fair value = *f* (Interest rate differential , inflation differential, Current account differential, reflation variable)

- EUR could trade higher towards our medium term fair value of around 1.1650 over time if **ECB's monetary policy divergence with the Fed slows rapidly** or **even converge with the Fed over time**.
- Euro-area needs deeper structural reforms in government debt and labor market in order to lift long term growth potential and push EUR meaningfully higher above 1.20 but pushing through policies within the Euro-area are often complicated and challenging.

Source: Eviews, Bloomberg, Maybank FX Research

GBP: Temporary Stability but Macro Pressures to Weigh

1. **Turning Less Bearish on GBP**
   - Domestic political risk temporary recedes
   - Focus on BoE tightening to keep GBP and UK yields temporarily supported

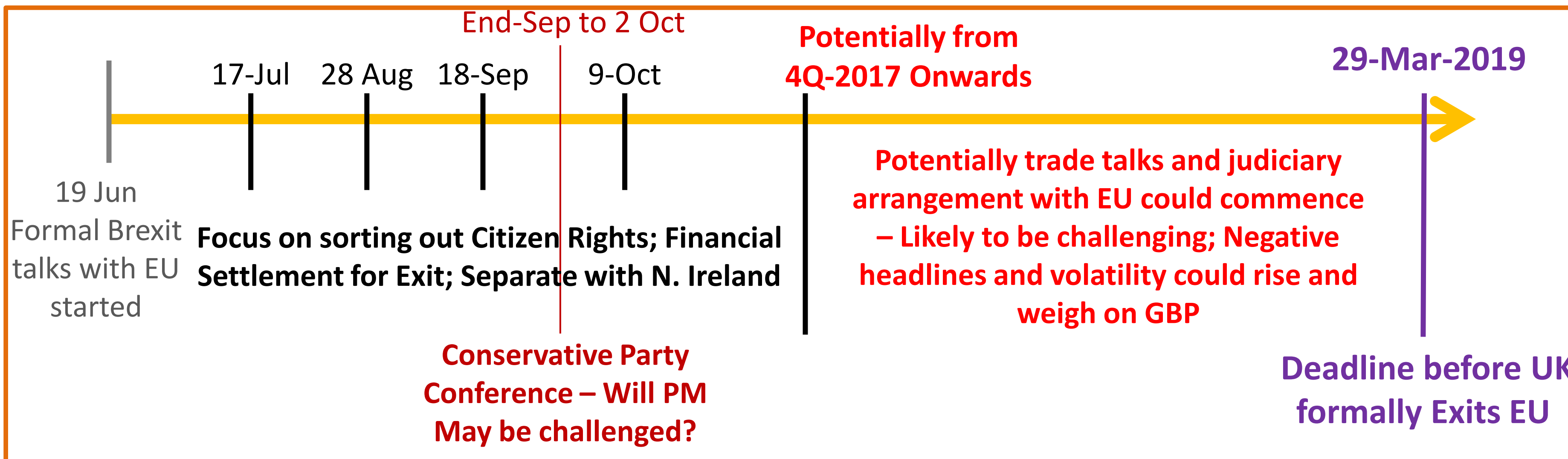
2. **But Retain a Cautious Outlook**
   - Brexit uncertainties remain and negotiations on trade and judicial arrangement (likely to begin in later part of the year) are likely to be long-drawn process
   - Deceleration in macro-fundamentals (i.e. growth momentum, consumer spending, business investments) should limit GBP gains
   - Though BoE may raise rates, we are not of the view they could tighten much as BoE does not want to derail recovery process

3. **Strategy**
   - Buy GBPSGD on dips towards 1.76 levels for a move towards 1.80, 1.84
   - Buy GBP on dips towards 1.25-1.26 levels for an eventual move towards 1.35-1.40

Forecast	3Q 2017	4Q 2017	1Q 2018	2Q 2018	End 2018
GBP/USD	1.3200	1.3000	1.2900	1.3200	1.3500

Brexit Uncertainties Remain; Key Focus from 4Q 2017

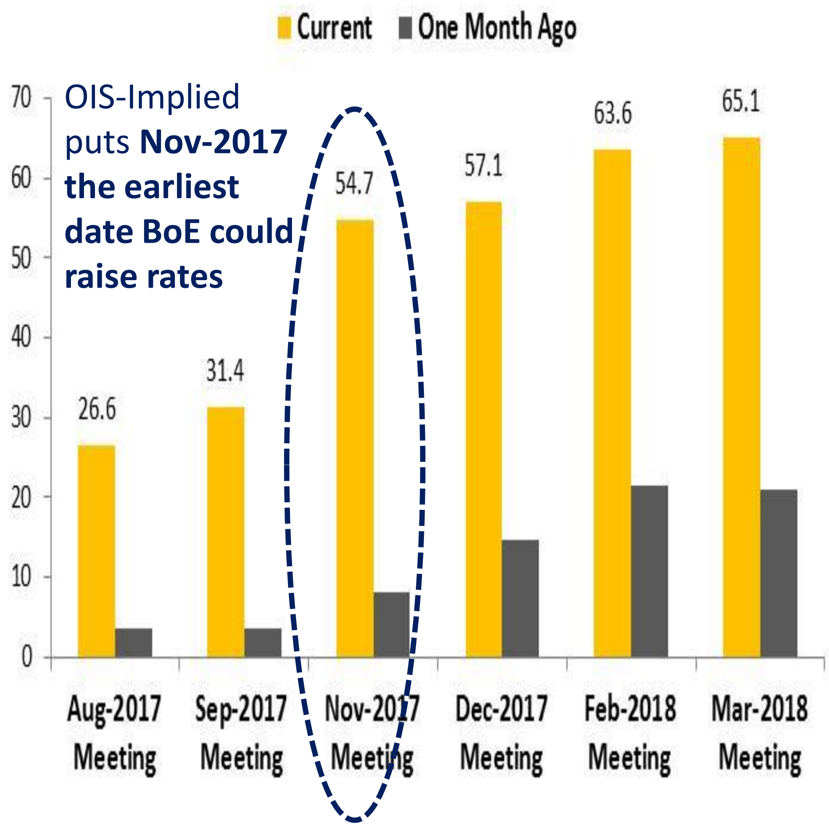
- **Brexit uncertainties have not gone away** but … UK's softer stance on Brexit may help
- **Negotiations have started** with initial timeline and immediate priorities being laid out for next 3 months – **helps to restore some stability to GBP**
- Too soon to pass judgement as the **heavyweights – judicial and trade formal negotiations are only scheduled to commence later** (we think probably some time in 4Q-2017). **Negotiations are expected to be challenging**; should see a return of **negative headlines and heightened volatilities**
- Other risks to watch include: **Conservative Party Conference if PM May's leadership is challenged** and if **Conservative-DUP partnership can hold through** for the next 5 years



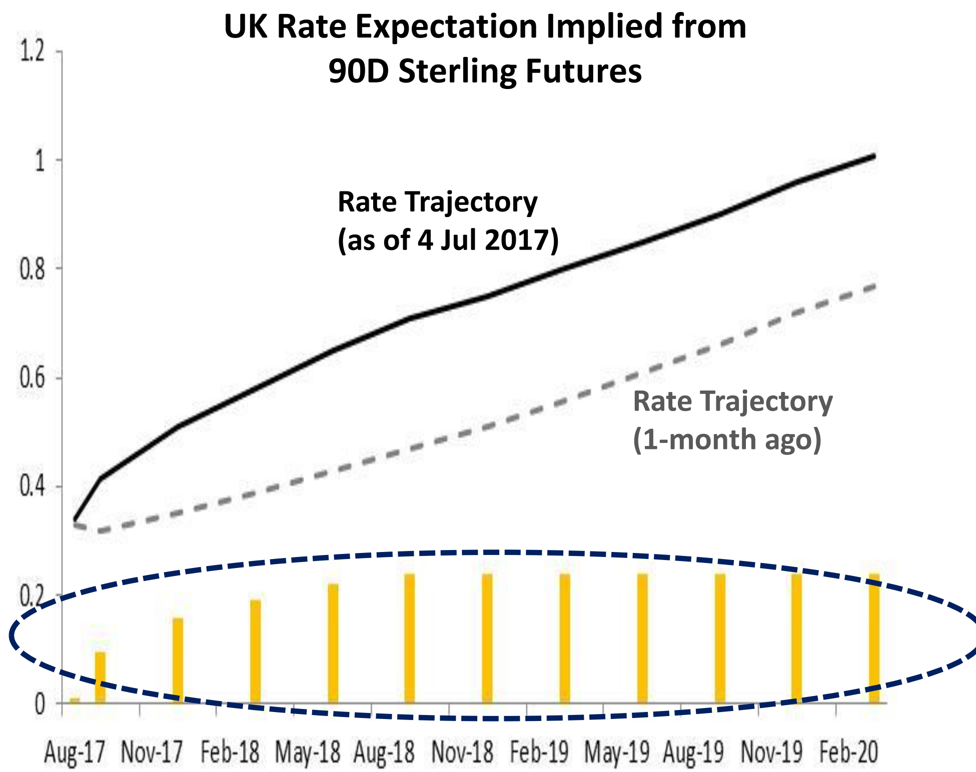
Source: Maybank FX Research

BoE Tightening Should Temporarily Support Yields and GBP

BoE Rate Hike Probability on the Rise; Supportive of UK Yields and GBP Temporarily…



…But Rate Hike Trajectory Remains Mild (+25bps/year; GBP Not Unlikely to Draw Sustained Support from Yield Plays Unless Trajectory Picks Up



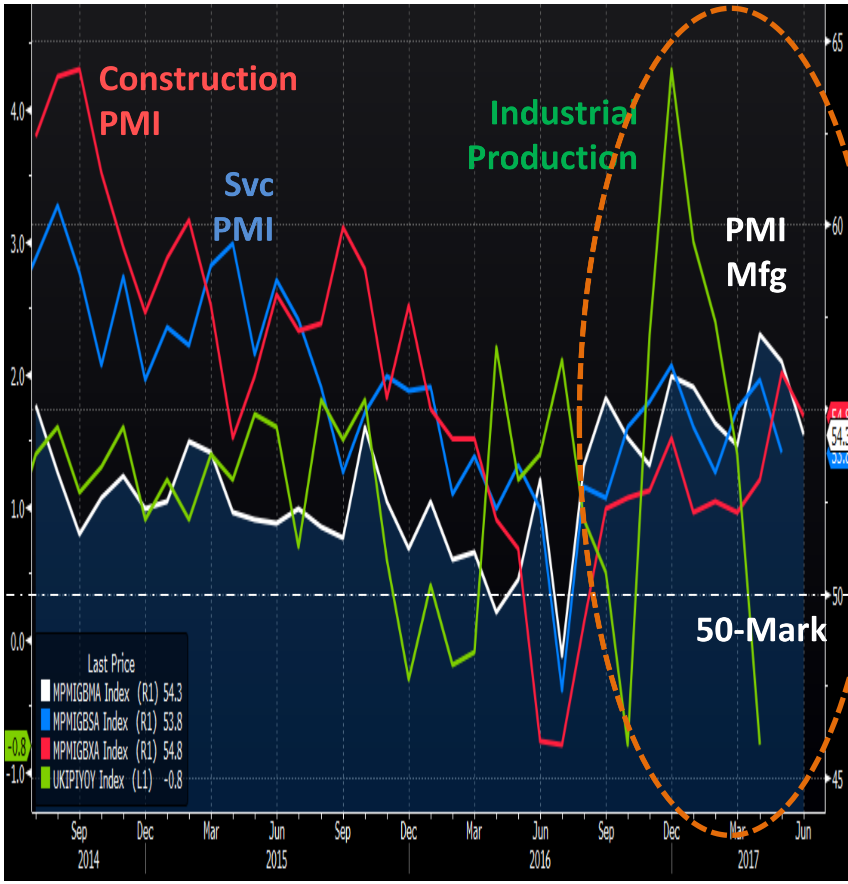
Rate Trajectory from 90D Sterling Futures does not imply a steepening in UK rates

Source: Bloomberg, Maybank FX Research

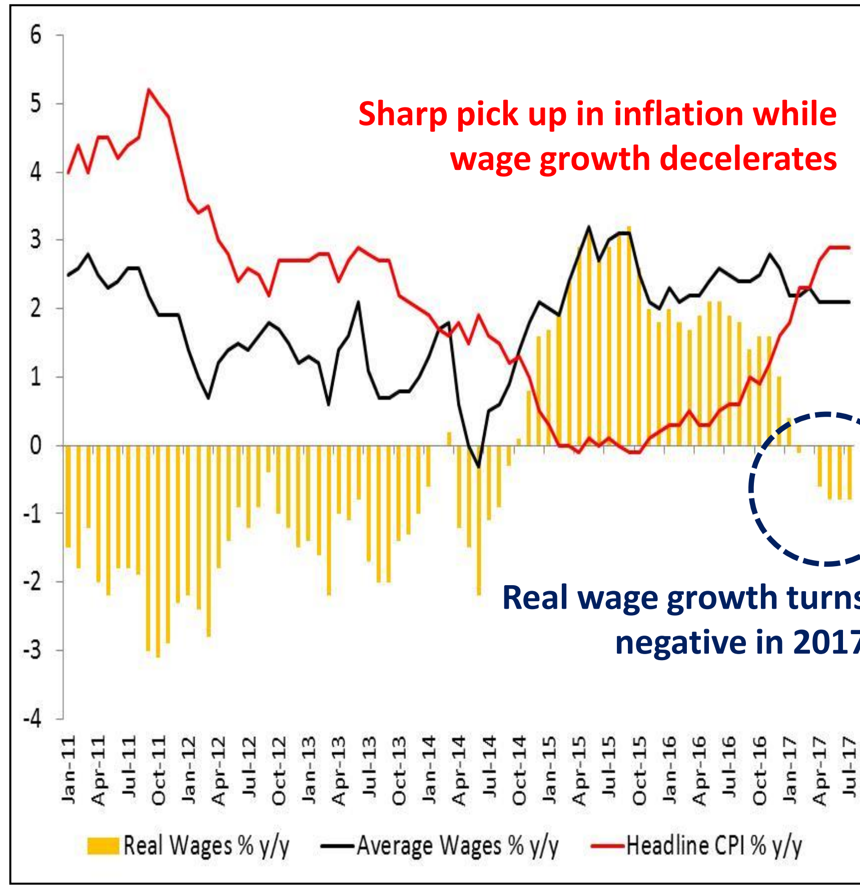
House View on the GBP

Economic Data Downside Surprises to Limit GBP Gains

Growth Momentum Decelerating - PMI Mfg, Services, Construction & IP



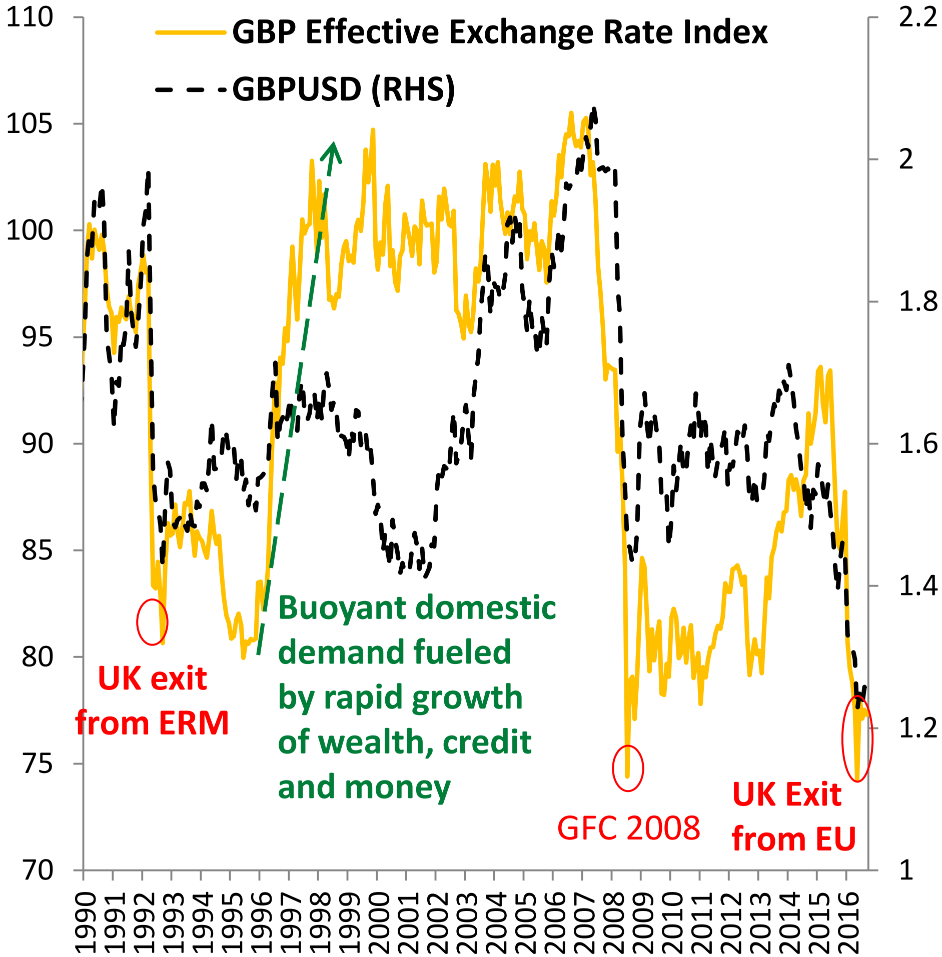
Rising Inflation and decelerating wage growth squeezing household consumption



Source: Bloomberg, Maybank FX Research

GBP May Trade Higher Over Time as Economy Rebalances

An Eventual Bounce after a period of Rebalancing and Recovery in Investor Sentiment



Source: Eviews, Bloomberg, Maybank FX Research

- The **20% or so depreciation since referendum results (Jun 2016) should help the UK economy to rebalance and grow sustainably over time** - current account deficit should narrow, exports should become more competitive and tourism and education receipts should pick up further.

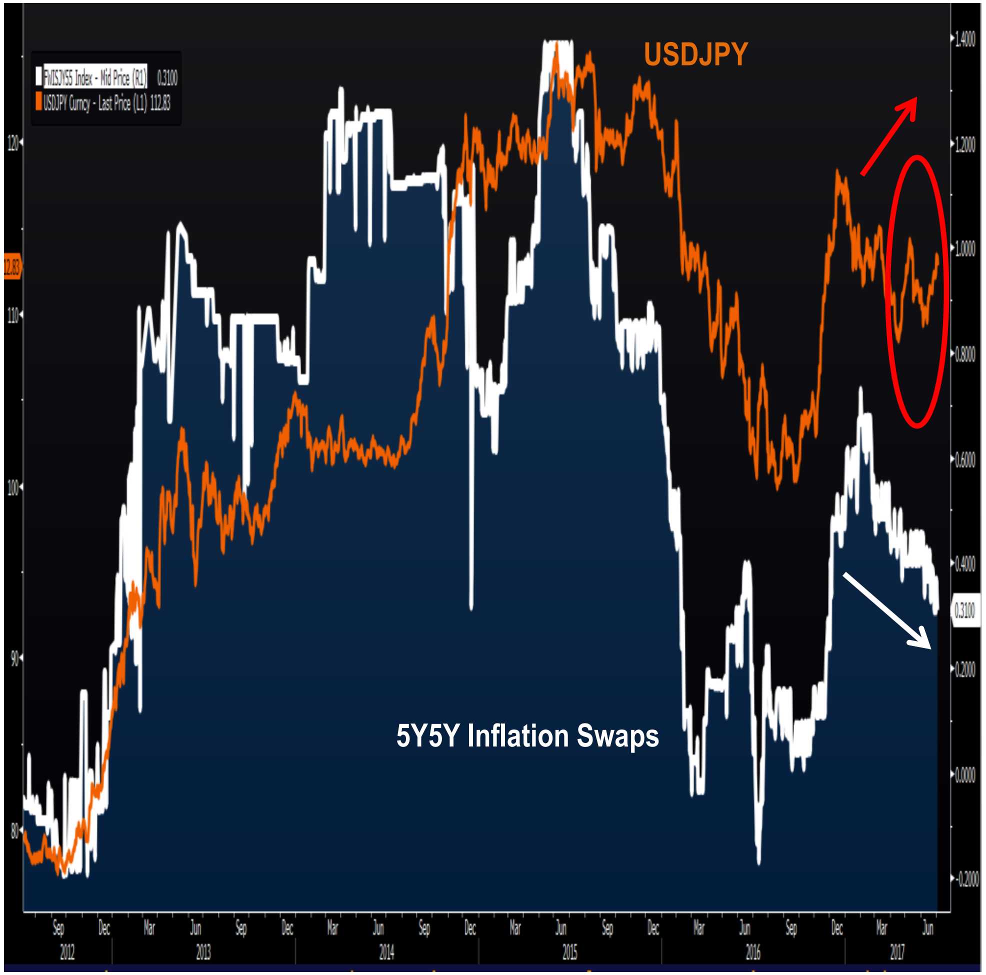
- **Past experience of UK leaving the ERM back in 1992 saw a period of consolidation (for a few years) at historical lows** for GBP, before the **eventual move higher in the following years, where GBP TWI traded above 100-levels in 1998** (from the lows of 80 in 1993-1996) due to buoyant demand fueled 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.

- **Our In house Fair Value puts GBP at around 1.40 – 1.50 range**

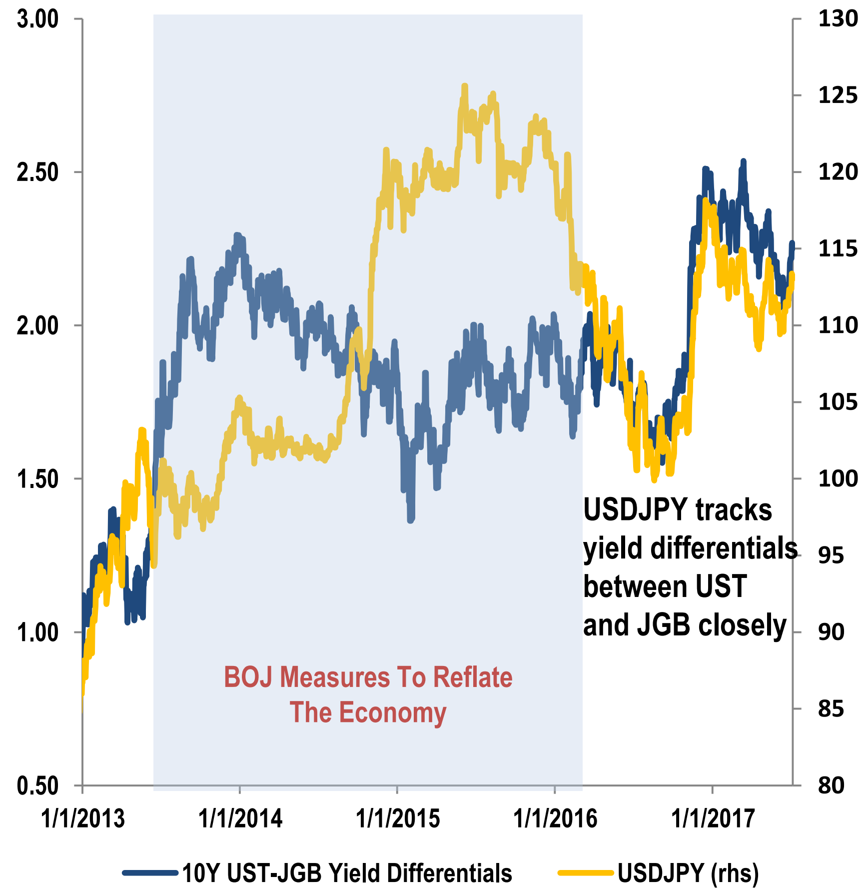
Expectations Of Widening Yield Differentials Lifts USDJPY Higher Even As Inflationary Expectation Falls

USDJPY Climbing Higher Even As Longer Term Inflation Indicator Falls …



Source: Bloomberg, Maybank FX Research

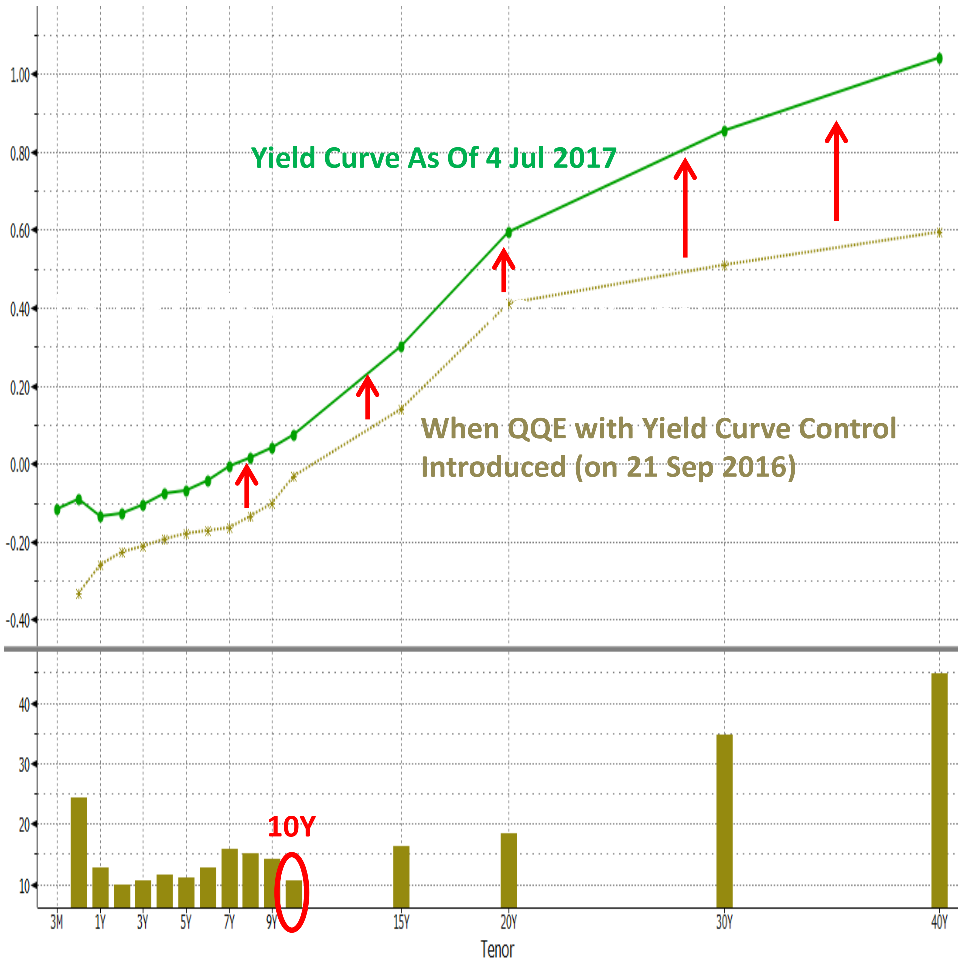
… As Widening UST-JGB Differentials Expected To Lift USDJPY Higher



Forecast	3Q 2017	4Q 2017	1Q 2018	2Q 2018
USD/JPY	115 (118)	117 (120)	117 (120)	119 (--)

BOJ's Ultra-Loose Monetary Policy Continues To Back-Stop The USDJPY

Underscoring The USDJPY Rise Is BOJ's QQE With Yield Curve Control



Source: Bloomberg, Maybank FX Research

- BOJ surprised markets last year when it introduced a new policy framework – **Quantitative and Qualitative Monetary Easing (QQE) With Policy Curve Control**.

  - kept negative interest rate at -0.1% for the portion of reserves that banks park with the BOJ
  - it also aimed to keep the benchmark 10Y bond yield around zero percent

- It continued to expand the monetary base at an annual rate of JPY80tn (though this could vary according to market conditions)

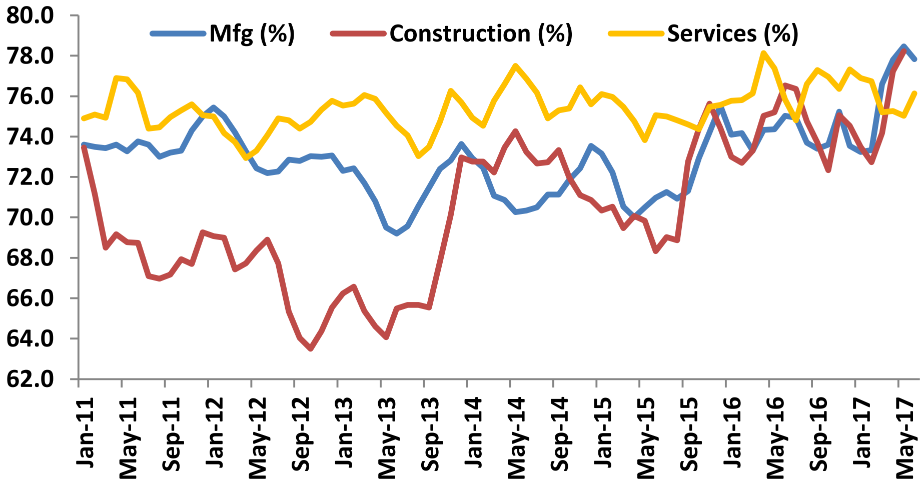
- Aside from allowing the BOJ to control the short-term and long-term interest rates, the new framework also allows for the lowering of borrowing cost, while lifting inflation expectations and supporting the profit margins of banks/funds vested in JGBs

- **A year since the introduction, the yield curve has risen pivoting around the 10Y which remains around 0%.**

Economic Backdrop Is Improving, Supportive of AUD

Slack Is Tightening

Capacity Utilization Rate



Employment Growth Has Seen Consistent Pick Up

Australia Has Seen Signs of Improvements

- Capacity utilization rate is rising which indicates that ***slack is reducing*** in the economy.
- In addition, ***employment growth has also seen a consistent recovery*** and hiring is done in the services sector.

That may translate into some wage growth but we do not expect a strong improvement in that area.

As RBA Governor Lowe has pointed out

"Productivity growth has slowed."

"Workers face more competition (form foreigners and robots)"

"People value employment security in an uncertain world and feel they can increase it by not asking for a bigger wage rise."

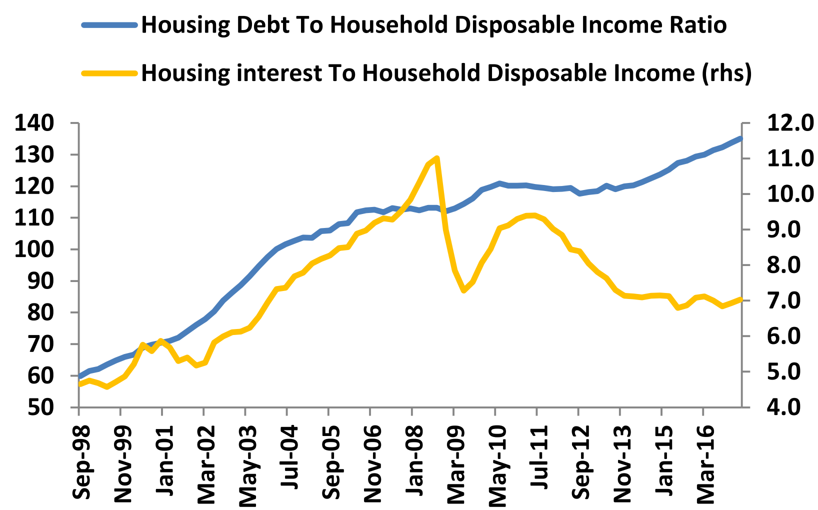
=> "We'll have to get used to it"

~ June 06 RBA Lowe Speech

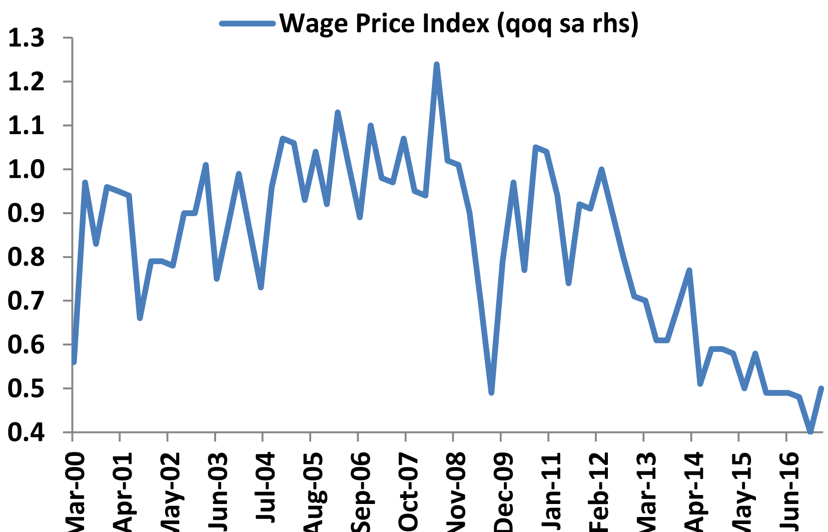
Source: ABS, RBA CEIC, Bloomberg, Maybank FX Research & Strategy

RBA Unlikely To Move This Year, Dampening Aggressive AUD Bulls

Household Debt Has Been Rising



But, Wage Growth Has Been Anemic



Two Key Things In the Latest RBA Statement:

- **Low Growth of Real Wages**
- **Rising Household Debt**

"Consumption growth remains subdued, reflecting slow growth in real wages and high levels of household debt"

~4 July 2017 RBA Statement

RBA is not in any position to hike rates in the near future. They cannot afford to join the rest of other G7 central bankers that have turned hawkish.

Plus, a stronger AUD could undermine the services economy.

"The outlook continues to be supported by the low level of interest rates. The depreciation of the exchange rate since 2013 has also assisted the economy in its transition following the mining investment boom. ***An appreciating exchange rate would complicate this adjustment."***

~4 July 2017 RBA Statement

Source: ABS, RBA CEIC, Bloomberg, Maybank FX Research & Strategy

House View on the AUD

A Base in Iron Ore Prices Is Supportive of AUD

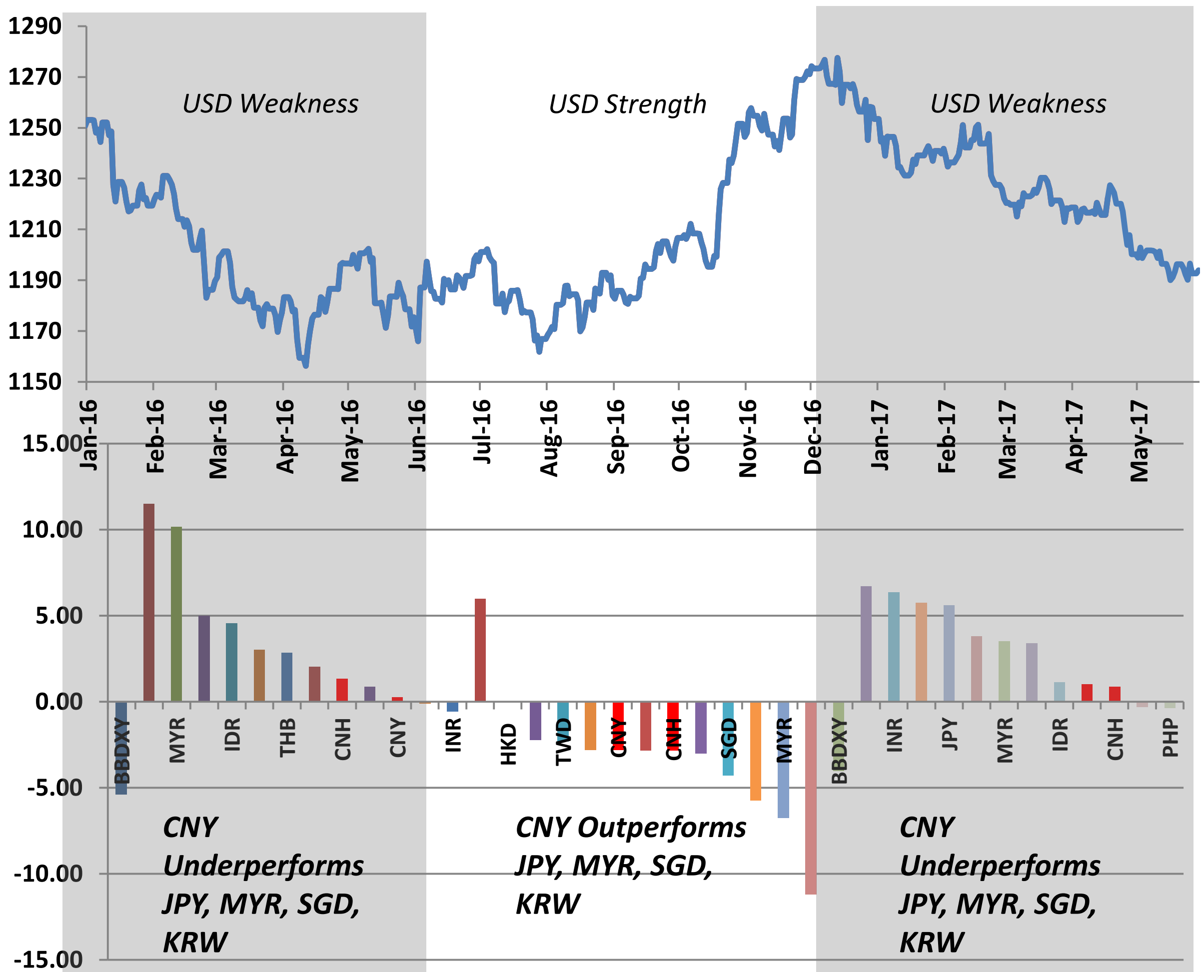
With RBA unlikely to give clear cues for the AUD, the currency is all the more dictated by commodity swings. The bottom in the AUDUSD came a little earlier than we expected, at around 0.73-0.74. Last seen above 0.76, USD strength could still bring this pair lower and **we look for modest upmove towards 0.80 by the end of the year.**

Forecast	3Q 2017	4Q 2017	1Q 2018	2Q 2018
AUD/USD	0.76	0.80	0.78	0.76

Source: Bloomberg, Maybank FX Research & Strategy

RMB - Taking Cues From The USD With A Little Extra Added

"Counter-Cyclical Adjustment Factor" To Soften Impact Of Sharp Market Swings



Source: Bloomberg, Maybank FX Research & Strategy

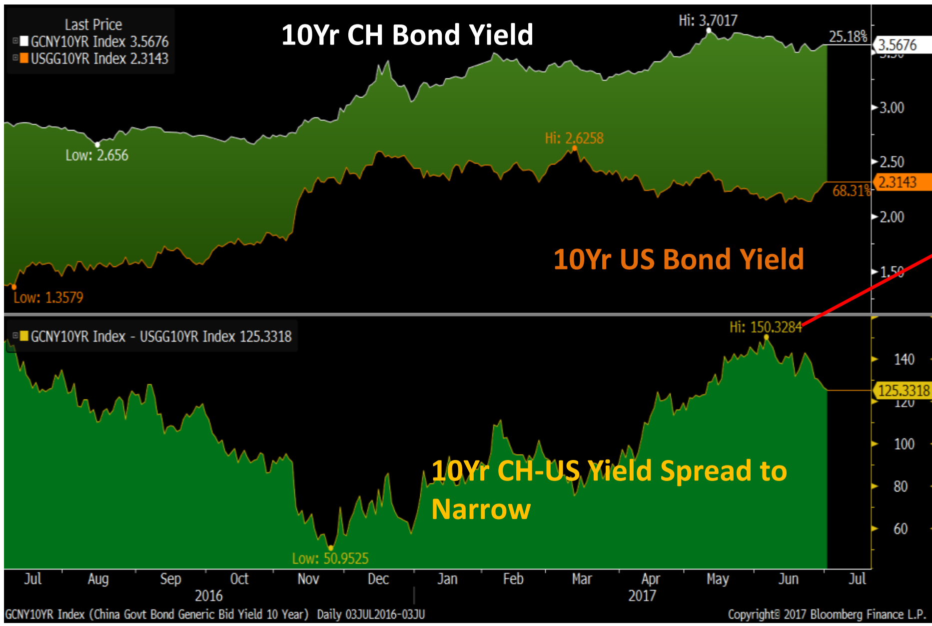
- RMB has been taking the cue from the USD. The absence of USD strength allows RMB to stabilize thus far this year, in addition to less capital outflows.
- The introduction of the "**Counter-Cyclical Adjustment Factor**" suggests that PBOC wants more RMB stability (or rather less RMB depreciation) in an environment of rising UST yields and possibly USD strength, especially as we near the 19th National Congress of the Communist Party of China that takes place in Nov.
- **As such, we have recently calibrated our year-end USDCNY forecast towards 6.87.**

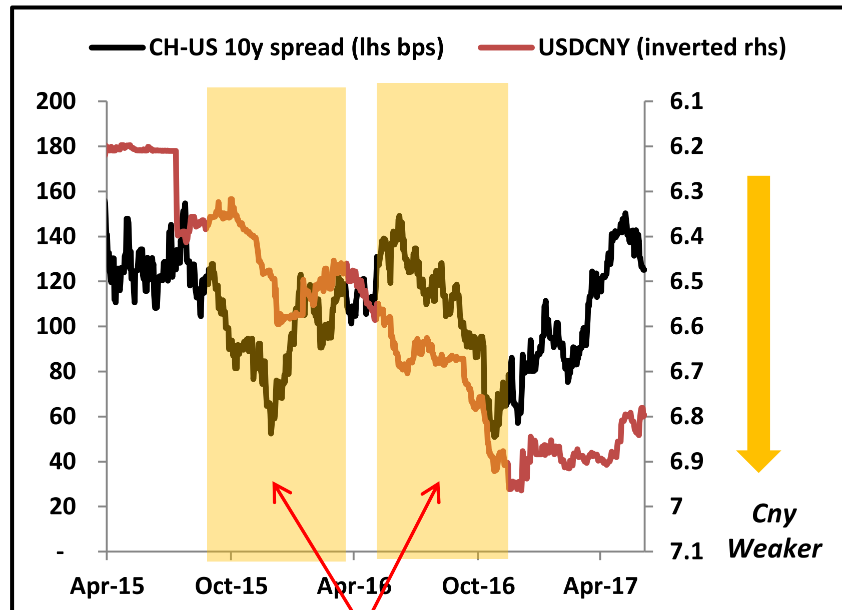
Forecast	3Q 2017	4Q 2017	1Q 2018	2Q 2018
USD/CNY	6.80	6.87	6.85	6.90

RMB - Further Weakness As CH-US Yield Spread To Narrow…

With PBOC unlikely to move OMO and MLF rates for the rest of the year and still upside risks to UST yields, **we expect the yield differential between China and US bonds to narrow, bringing USDCNY higher towards 6.87 (year end forecast).**

CH-US 10y yield has narrowed from its peak of 150bps on 6 Jun to 125bps. We see further extension of this trend.



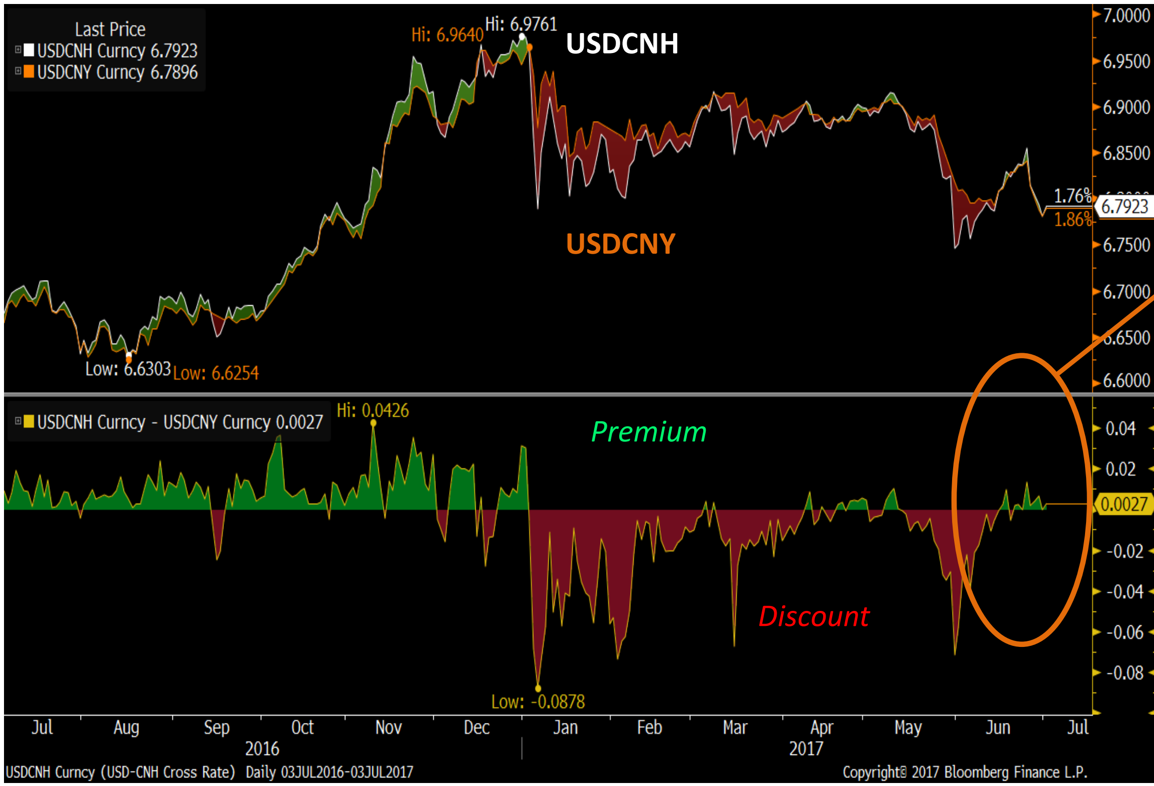


Source: Bloomberg, Maybank FX Research
Chart above is taken as of 3 Jul 2017.

CNY Tends To Weaken when yield spread Narrows

RMB - Markets Seem To Agree

USDCNH has been trading at a persistent premium to USDCNY **– a signal of bearish CNY views surfacing because of the yield compression with those of the USTs.** This is in spite of multiple episodes of suspected intervention in the past two months and the new fixing model to stabilize the Renminbi.



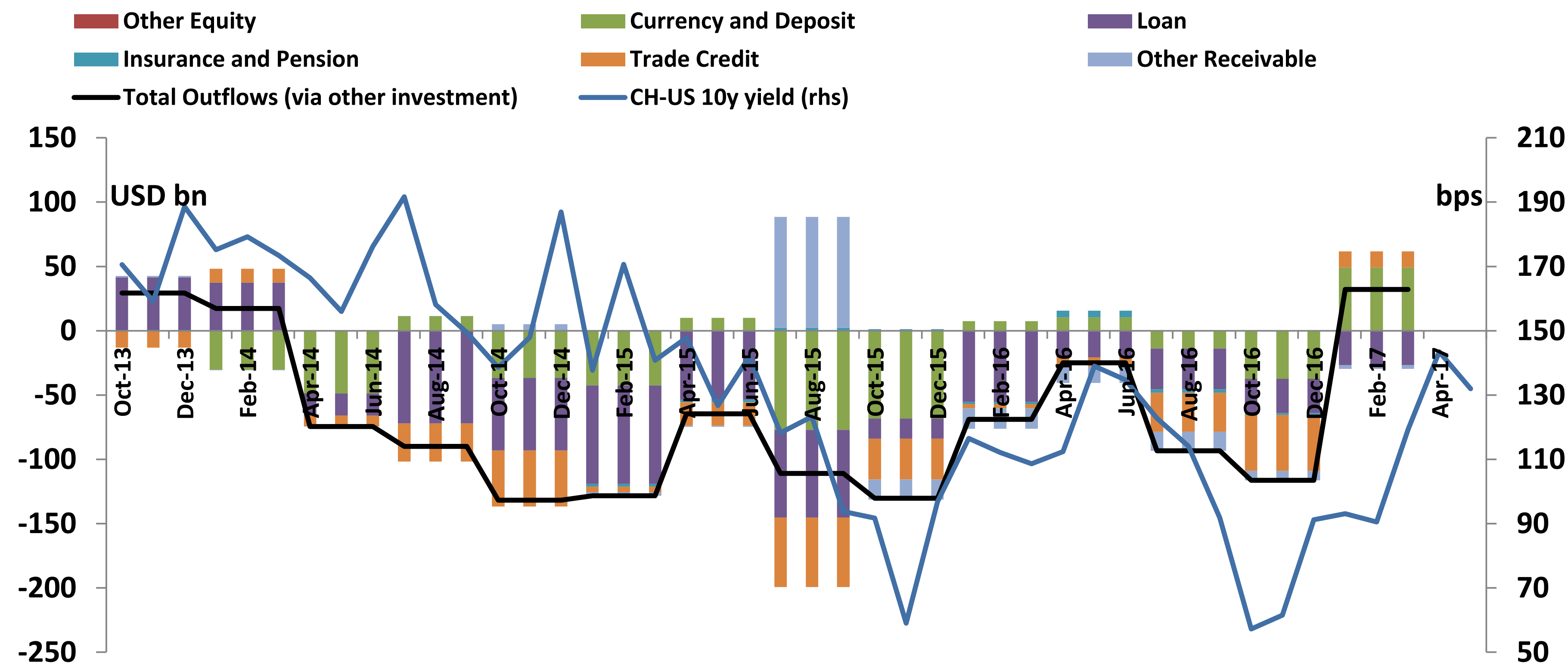
USDCNH-USDCNY premium has been mitigated by suspected PBOC intervention and stronger CNY fixing. However, it is still persistent.

Source: Bloomberg, Maybank FX Research & Strategy
Chart above is taken as of 3 Jul 2017.

Forecast	3Q 2017	4Q 2017	1Q 2018	1Q 2018
USD/CNY	6.83	6.90	6.85	6.90

RMB - Outflows Could Worsen

With CH-US yield spread likely reached a peak, we expect USDCNY to head higher and capital outflows to worsen in the next half of the year. However, the countercyclical adjustment factor could help limit the yuan depreciation for now. Beyond the 19th Party Congress, RMB may be allowed to react more to market forces into 2018.



Source: CEIC, Bloomberg, Maybank FX Research & Strategy

Forecast	3Q 2017	4Q 2017	1Q 2018	1Q 2018
USD/CNY	6.83	6.90	6.85	6.90

RMB – Nov, Dec are Seasonally Bullish Months for USDCNH

Bear in mind that beyond the 19th Party Congress, Nov and Dec are **seasonally bullish months** for USDCNH (rising 4 out of 5 Dec). **The Run up could even sharper, beyond our year-end forecast of 6.87.**

Source: CEIC, Bloomberg, Maybank FX Research & Strategy

Forecast	3Q 2017	4Q 2017	1Q 2018	1Q 2018
USD/CNY	6.80	6.87	6.85	6.90

House View on the MYR

Positive on Ringgit Outlook

- **External Factors are Supportive**
  - Rebalancing of global oil supply-demand is bringing about relative stability in oil prices
  - Global risk sentiment constructive, with VIX at record lows

- **Domestic Factors Are Improving**
  - Recent BNM initiatives to deepen and broaden domestic financial markets are positive steps to restore **foreign investors' confidence** (foreign fund inflow to equity and debt already happening)
  - Mandatory conversion of export proceeds also lead to demand for Ringgit
  - **Potential election sometime this year should lead to demand for MYR assets**
  - Solid underlying fundamentals (2017 growth expected to be 4.4%), backed by **domestic demand** (consumer spending and investment growth) as well as **exports recovery** (+20.6% y/y in Apr) amid accommodative monetary policy (OPR at 3%)
  - Sustained current account surplus (+1.8 expected for 2017) and higher oil prices to support plans to keep budget deficit under control (-3% of GDP)
  - **Stabilizing FX reserves** to retained imports & short-term debt should also provide an anchor for the MYR

- **Challenges**
  - Aggressive Fed policy normalization – rate hikes and balance sheet reduction could result in USD strength
  - Co-ordinated efforts from other major central banks to withdraw monetary stimulus could tighten monetary conditions and weigh on risk sentiment and weigh on MYR

- **Strategy**
  - **Bias to stay long MYR vs. short SGD, KRW, JPY, THB, PHP**

Forecast	3Q 2017	4Q 2017	1Q 2018	2Q 2018	End 2018
USD/MYR	4.2500	4.3000	4.3000	4.2500	4.2000

BNM Recent Initiatives – A Boost to Investors' Confidence

- **Promote A Fair and Effective Market**
  - Introduction of the Principles for a Fair and Effective Financial Market
  - A new code of conduct for Malaysian Wholesale Financial Markets

- **Improve Bond Market Liquidity**
  - the regulated short-selling of securities in wholesale money market will be liberalized to **allow all residents to participate in short selling activities.** This is to facilitate a more effective avenue for the hedging of interest rate risk exposure as well as to generate more trading activities and liquidity in the secondary government bond market

  - **Eligible securities for short-selling transactions will also be expanded to include Malaysian Government Investment Issue (MGII)** with an outstanding nominal amount of at least MYR2bn, on top of Malaysian Government Securities (MGS). The aim is to elevate liquidity in the MGII issue and narrow the pricing gap between MGS and MGII.

- **Additional Hedging Flexibility**
  - Registered non-bank entities (including institutional investors, companies) will be allowed to **hedge up to 100% of their underlying assets and to manage an additional 25% of FX exposures.** This allows registered investors to fully hedge and actively manage their FX exposures including unwinding of hedging positions. Previously the flexibility to hedge without documentation is only applicable to 25% of its MYR assets (for non-resident investors) or foreign currency assets (for resident investors)

- **Strengthen Financial Market Infrastructure**
  - Information reporting and settlement infrastructure will be enhanced for greater transparency and to facilitate surveillance on the onshore financial market (over 12 – 18 month period)

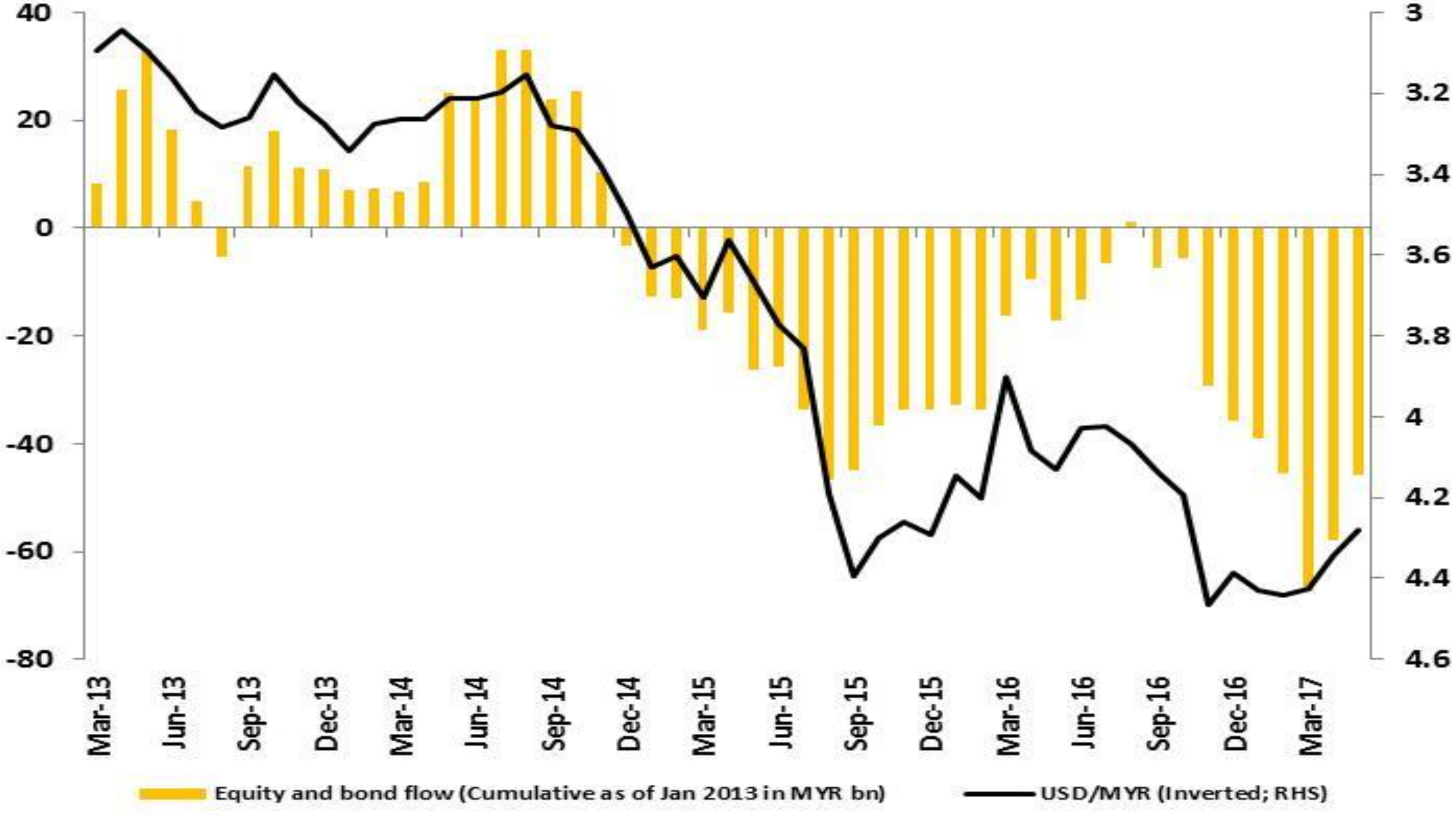
We view these initiatives as positive developments. These are **steps towards broadening and deepening the onshore financial markets**, allowing investors to better manage rates and FX exposures. **We believe investors' confidence should gradually return**

Note: BNM Initiatives announced 13 Apr, effective 2 May 2017 for points 1 - 3

Stability Gradually Returning to the MYR

MYR Rebounding on Foreign Inflows into Malaysia

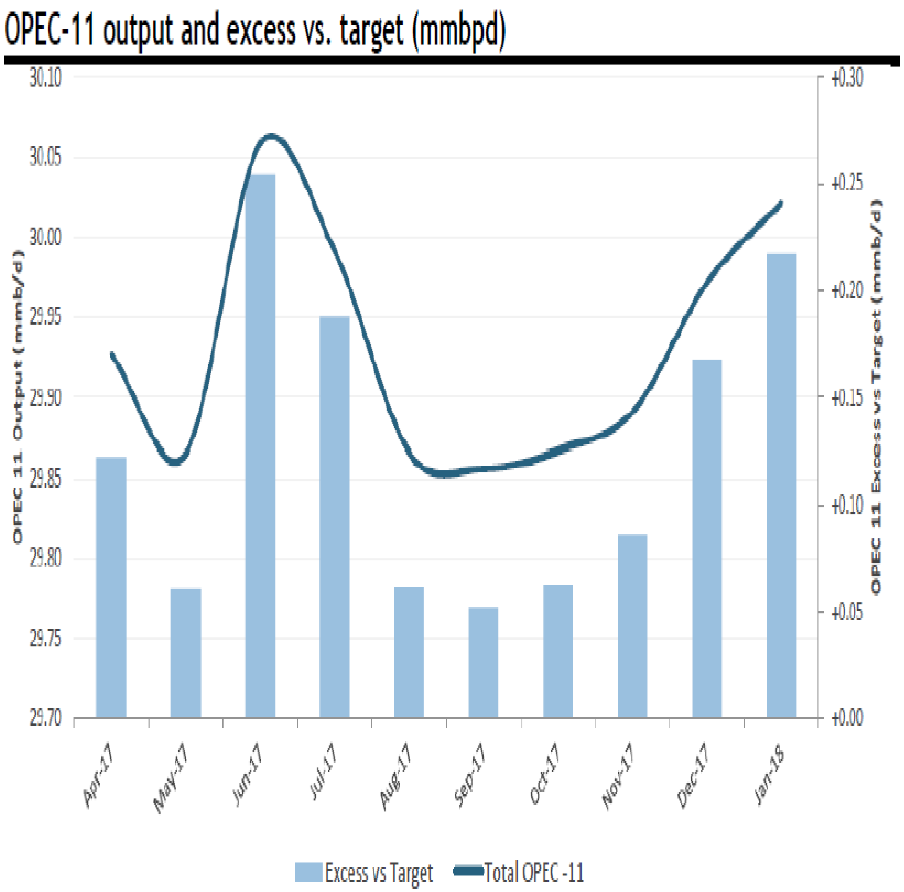
USDMYR (RHS, Inverted),
Net Equity and Bond Inflow from Foreign Insti (Cumulative as of Jan 2013 in MYR mil)

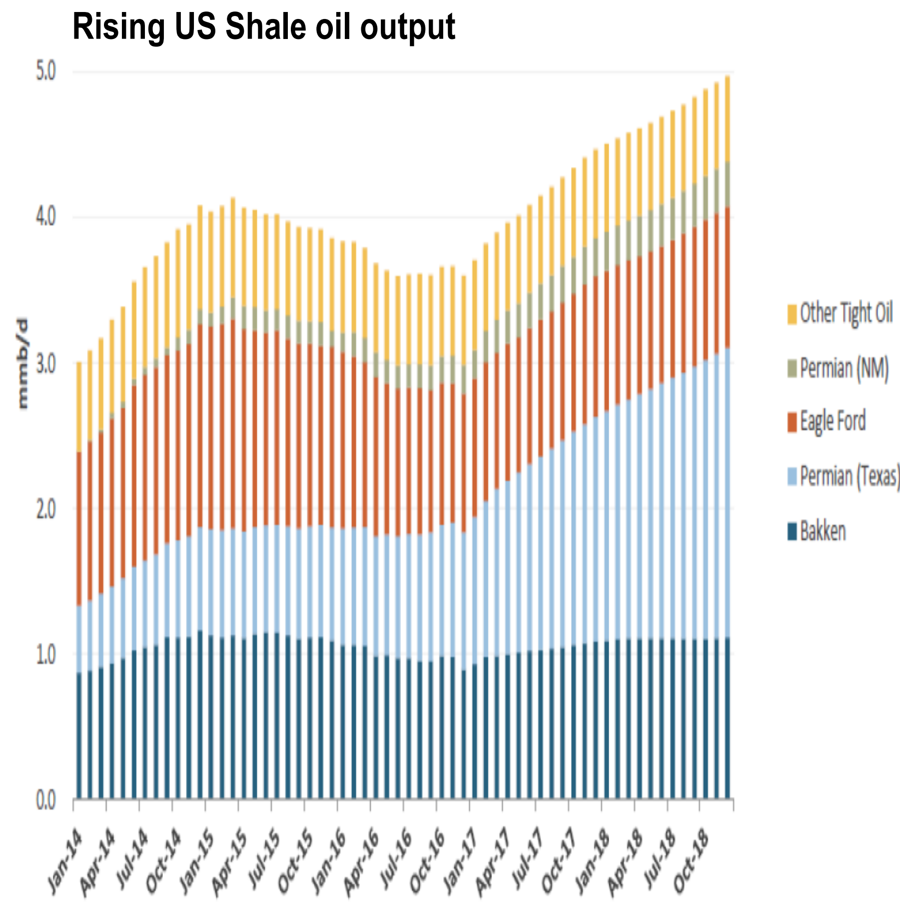


Source: Bloomberg, Maybank FX Research

House View on the MYR

Oil Prices – Largely a Supply Issue

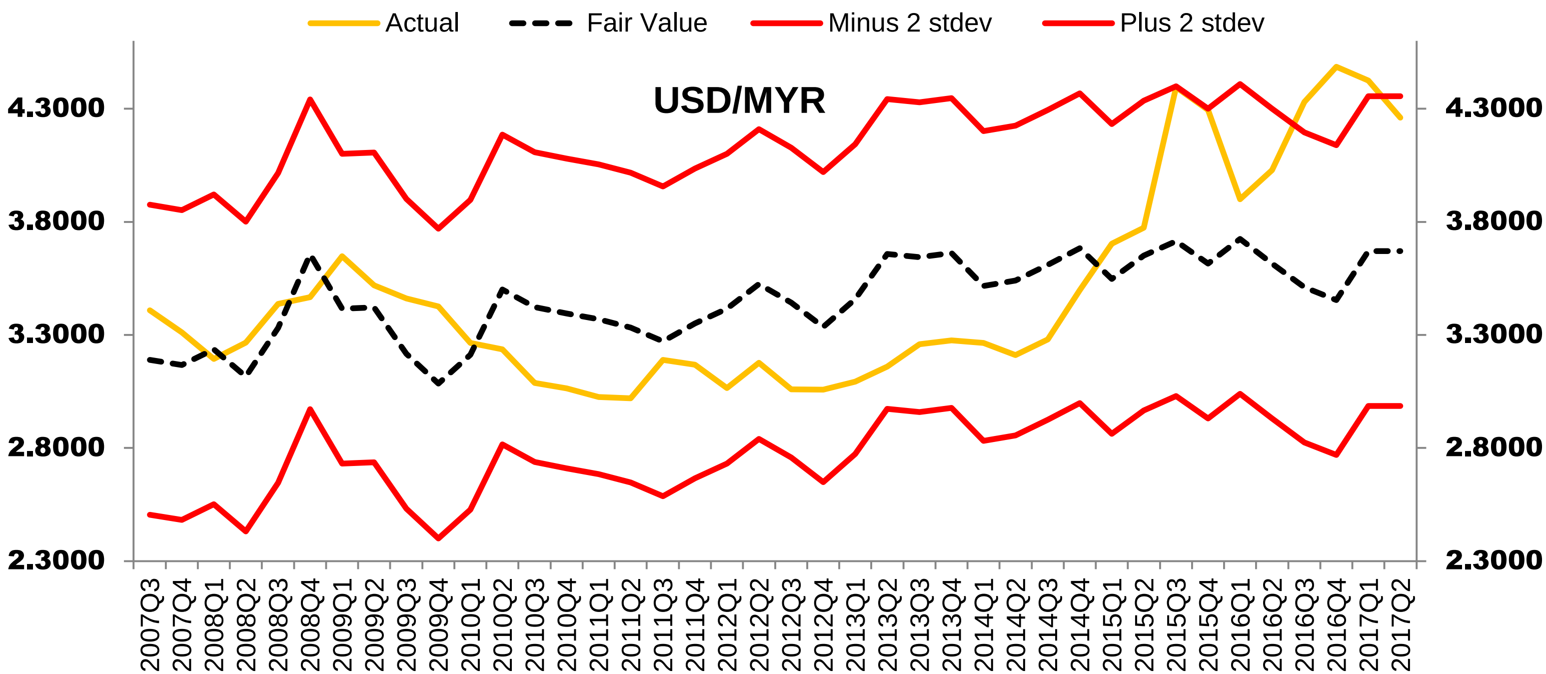




Source: FGE, Maybank IB-Research, Maybank FX Research

House View on the MYR

Current Level of Spot MYR is Sold Beyond Fundamentals



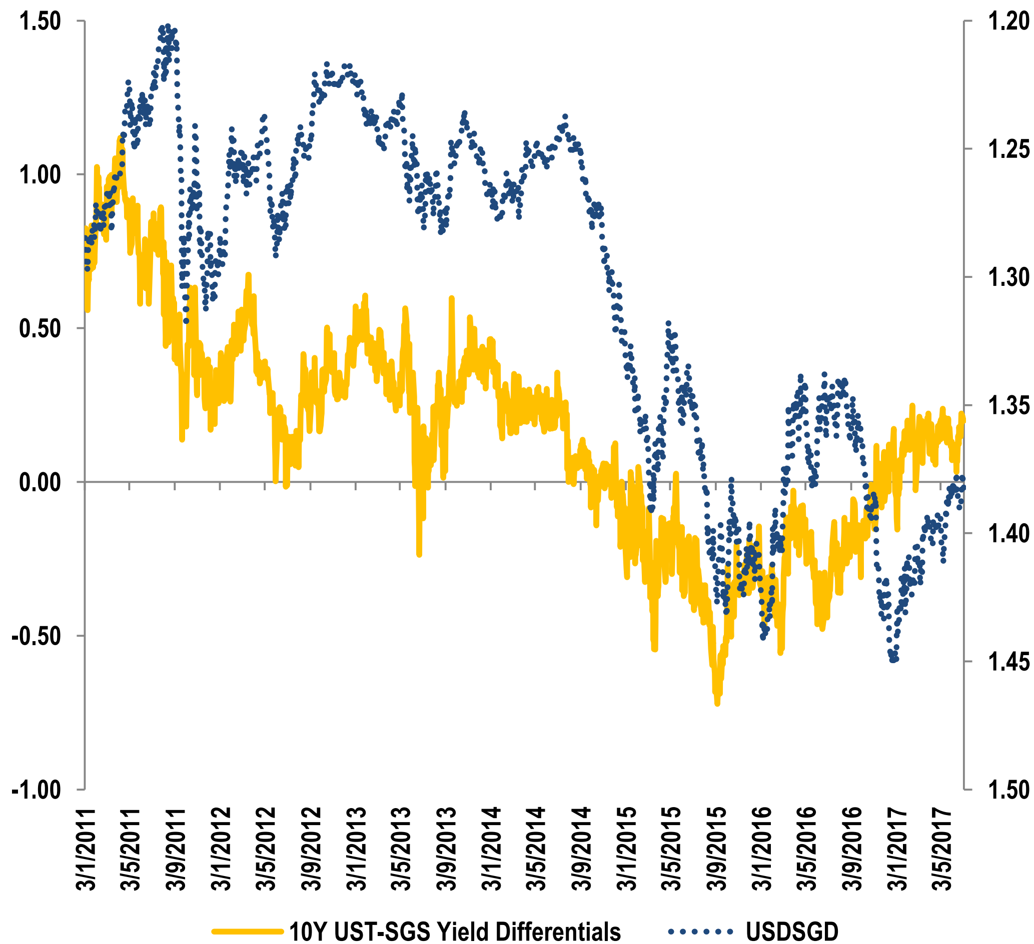
MYR fair value = *f* (Interest rate differential , inflation differential, Current account differential, reflation variable)

- Ringgit weakness **not** a reflection of fundamentals but market sentiment
- Our fair value suggests MYR is about 14% undervalued relative to medium term fair value of 3.70
- Economy still on track to expand at around 5% y/y for 2017, underpinned by domestic demand resilience, stronger investment growth and pick-up in government expenditure, amid accommodative monetary policy

Source: Eviews, Bloomberg, Maybank FX Research

Widening Yield Differentials Supportive Of The USDSGD

USDSG Has Been Broadly Tracking 10Y Yield Differentials Between UST & SGS



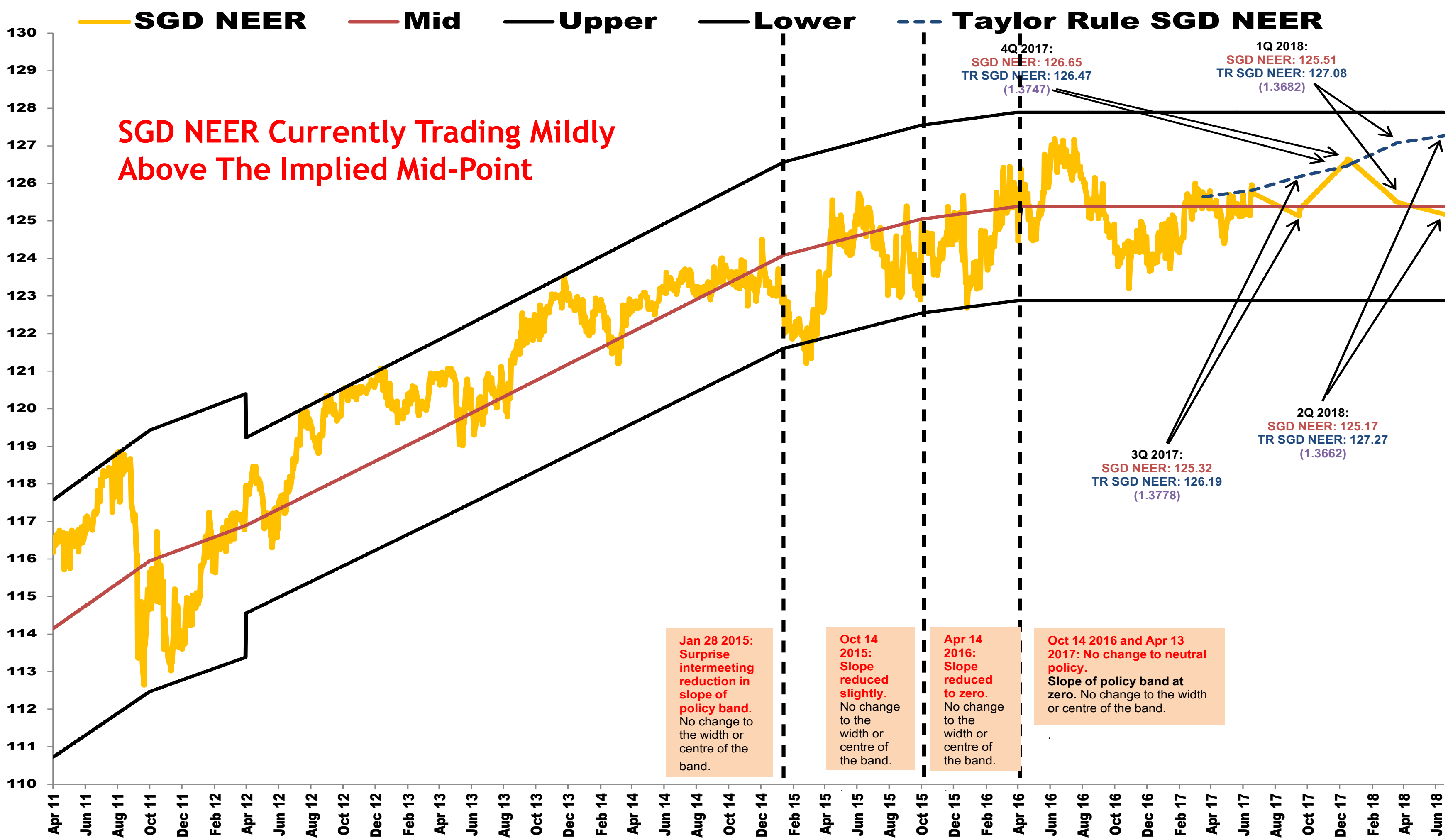
Source: Bloomberg, Maybank FX Research

- Rise in UST yields to be underpinned by steady US economic growth, the ongoing normalization of US rates (next hike likely in Sep 2017) and expectations of Fed's unwinding of its balance sheet.
- The rise in UST yields will have a significant impact on the USDSGD given the sensitivity of the USDSGD to moves in 10Y UST yield.
- Rise in UST yields should narrow yield differentials between the UST and SGS (as shown in the chart on the left) , leading to fund outflows and lift the USDSGD higher.

Forecast	3Q 2017	4Q 2017	1Q 2018	3Q 2018
USD/SGD	1.3900 (1.4200)	1.3800 (1.3950)	1.3950 (--)	1.4050 (--)

Risk Of Shift To "Mild Appreciation" From Neutral Policy In Oct

Our Taylor Rule Estimates Suggest A Shift In Policy Would Be Appropriate



Source: Bloomberg, Maybank FX Research

Strategic/ Tactical Trade Ideas

Tactical Trade Ideas

- **Tactical Long USDJPY, USDKRW, USDTWD, target 115, 1160, 30.90, respectively on widening yield differential plays - CB divergence**

- **Tactical Short EUR, looking for a move towards 1.12 levels as markets over-priced ECB's tapering/tightening plans**

- **Tactical Short NZD as RBNZ is not in hurry to raise rates and risk of potential inclusion of debt-to-income ratio to macro-prudential toolkit, target 0.7070 levels**

- **Bias to Buy AUDSGD on dips, targeting a move towards 1.0590. Dips towards 1.0420, 1.0380 remain a buy**

Strategic Trade Ideas

- **Buy EURJPY targeting 130 objective**
  - **on receding political risks and to position for eventual monetary divergence**

- **Buy AUDJPY targeting 88 objective**
  - **on the view that global rates are likely to remain suppressed given the rising level of global savings rate and that China could emerge as a large net creditor and lender to the world. That could keep global liquidity flush, volatility low, equities on the upmove and risk appetite supported.**

- **Positive on MYR**
  - Amongst AXJs, we are positive on the MYR given the recent initiatives from BNM. We expect foreign investors' confidence to gradually return
  - We see scope for Ringgit to play catch up with regional peers and potentially extend its gains further towards 4.25, 4.20 levels (vs the USD)

- **Buy USDSGD targeting 1.40-objective on USD recovery.**

- **Buy GBP on dips towards 1.25-1.26 targeting 1.35-1.40 Objective**

  - **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.**

Concluding Remarks

Concluding Remarks

- Focus is likely to shift back to central bank policies and inflation, for coming months
- Signs are rising for potential withdrawal of monetary stimulus, in particular the BoE, ECB and BoC amongst the G7s
  - But Fed remains the only major central bank in the midst of normalising monetary policy and
  - BoJ remains the only central bank that has yet to talk about policy shifts
  - Potential tightening of financial conditions should also weigh on sentiment
- Maintain view for modest USD strength
- Expect more USD upside vs. Asian currencies
- EUR and GBP remain better buy on dips

2017/2018 Forecast

	End 3Q-17	End 4Q-17	End 1Q -18	End Q2-18	End 4Q-18
USD/JPY	115	117	117	119	118
EUR/USD	1.13	1.14	1.15	1.13	1.12
GBP/USD	1.32	1.30	1.29	1.32	1.35
AUD/USD	0.76	0.80	0.78	0.76	0.75
NZD/USD	0.73	0.75	0.77	0.76	0.75
USD/SGD	1.3900	1.3800	1.3950	1.4050	1.4200
USD/MYR	4.25	4.30	4.30	4.25	4.10
USD/IDR	13400	13450	13500	13500	13400
USD/THB	34.50	35.00	35.30	35.80	36.00
USD/PHP	50.50	50.70	50.70	50.30	49.80
USD/CNY	6.80	6.87	6.85	6.90	6.80
USD/HKD	7.80	7.80	7.80	7.80	7.80
USD/TWD	31.00	31.00	31.50	32.00	31.50
USD/KRW	1150	1160	1170	1180	1140
USD/INR	65.70	66.20	66.50	66.70	66.40
USDVND	22850	22950	23100	23300	23400
USD DXY Index	98.09	97.70	97.05	97.97	98.03
SGD Crosses	**End 3Q-17**	**End 4Q-17**	**End 1Q -18**	**End Q2-18**	**End 4Q-18**
100 JPY/SGD	1.209	1.179	1.192	1.181	1.203
EUR/SGD	1.564	1.573	1.604	1.588	1.590
GBP/SGD	1.835	1.794	1.800	1.855	1.917
AUD/SGD	1.056	1.104	1.088	1.068	1.065
NZD/SGD	1.015	1.035	1.074	1.068	1.065
SGD/MYR	3.058	3.116	3.082	3.025	2.887

APPENDIX I:
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