Maybank

FX Outlook

Prices, Policies, Politics and Multi-Dimensional Asia

FX Research & Strategy| Global Markets
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Overview

1. Key Macro Questions for 2017

2. Our House View
   - **3*P***s + **1M** - Price pressures, Policy Normalization, Political Risks Receding + Multi-Dimensional Asia FX
   - Strategic Plays

3. Concluding Remarks

Key Macro Questions for 2017

Key Macro Questions for 2017

Fed's Policy Normalization?

Political Risks Receding?

The Multi-Dimensional Asia FX?

Commodities – Will The Tumble Continue?

Key Macro Questions for 2017

Fed's Policy Normalization?

Fed's Policy Normalization?

USD Has Almost Corrected Post-US Election Exuberance…

DXY Daily Chart

Source: Bloomberg, Maybank FX Research

Where can USD Strength Come From?

Fed's Policy Normalization?

Where Can USD Strength Come From?

- Potential Drivers of USD Strength
  - Fiscal Surprise
    - Tax Cuts/Reform
    - Infrastructure Spending
  - Monetary Policy Surprises
    - Tapering of QE Purchases (ended in 2013)
    - Policy Rate Normalization
    - Balance Sheet Normalization

Increase Consumption, Investment, Higher Growth, Higher Inflation,

↓

Tighten Monetary Policy

↓

Higher UST yields, UST curve to steepen

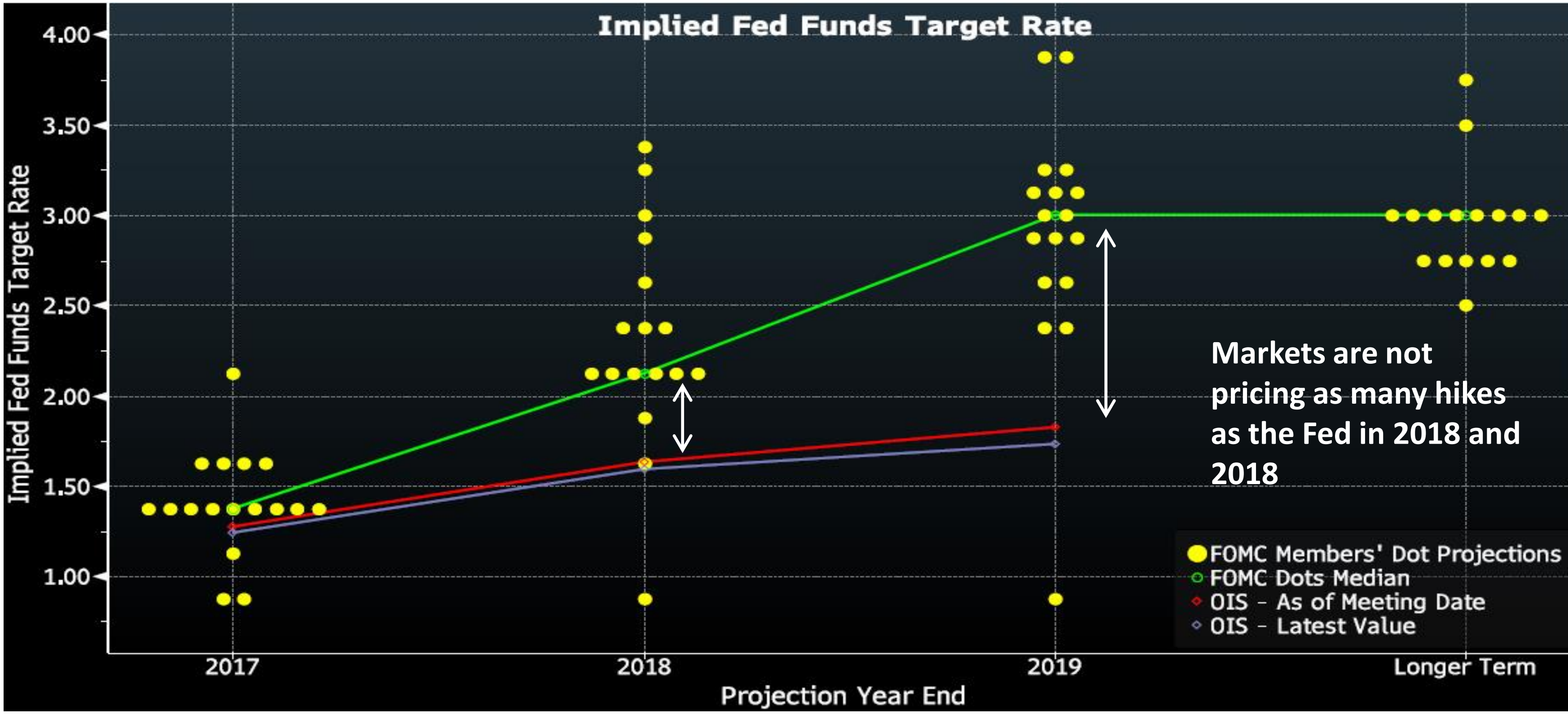
Source: Maybank FX Research

- 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.**

USD to rise once Markets Price In Fed's Rates Projs in 2018, 2019

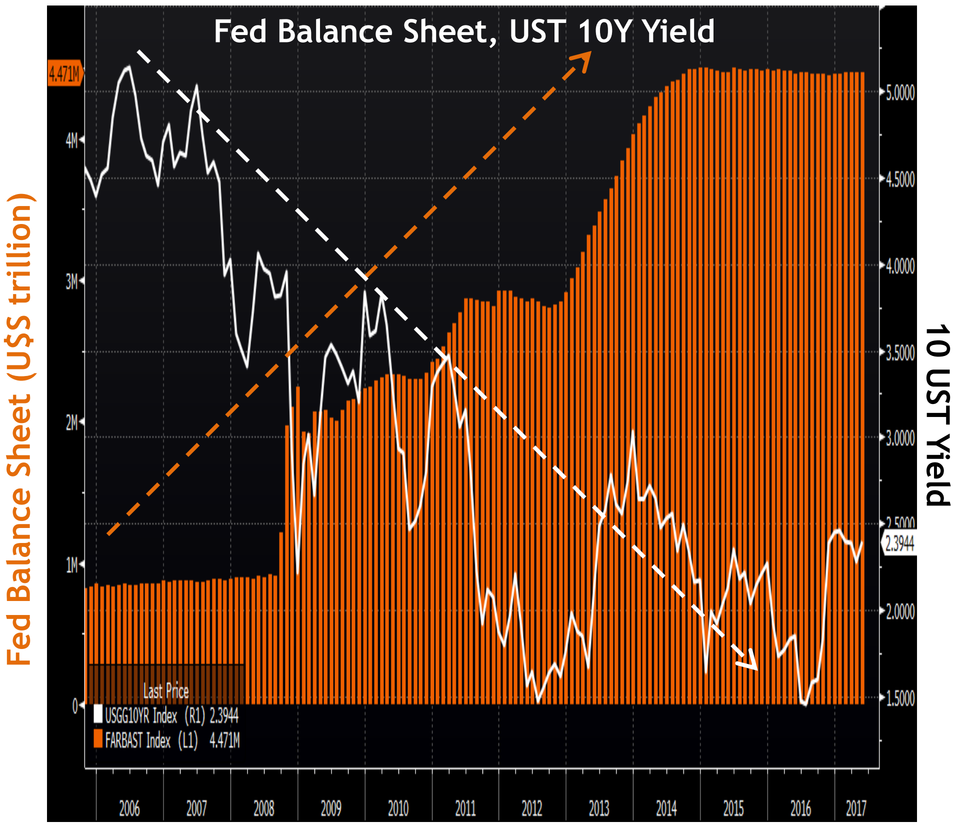


	End 2017	End 2018	End 2019
Fed (Dots Plot)	+50bps	+75	+87bps
Markets (implied from OIS)	+40bps	+30	+17bps
Markets Underpriced Fed by	10bps	45bps	70bps

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



Fed's balance sheet went from less than $900bn before the GFC to about $4.5tn today. In terms of GDP, Fed's balance sheet grew from 6% to over 23% of GDP.

Increase in balance sheet (via Quantitative easing) is normally thought to affect market prices and yields through a portfolio rebalancing effect: the central bank reduces the supply of relatively risky assets from markets, resulting in an increase in market prices, and decline in yields.

So a **balance sheet reduction** is expected to reverse these effects (i.e. lower market prices and potentially **higher yields**).

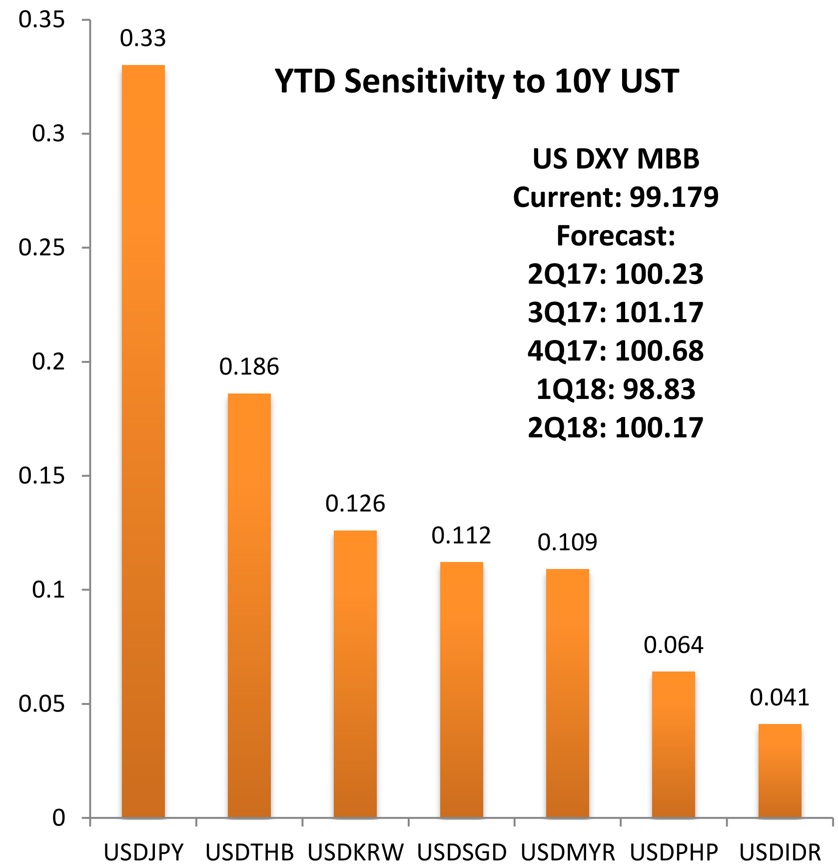
$675 billion reduction in the Fed's balance sheet over a two-year horizon is about **equivalent to a 25 basis point hike** in the funds rate [Kansas Fed, 10 May 2017]

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



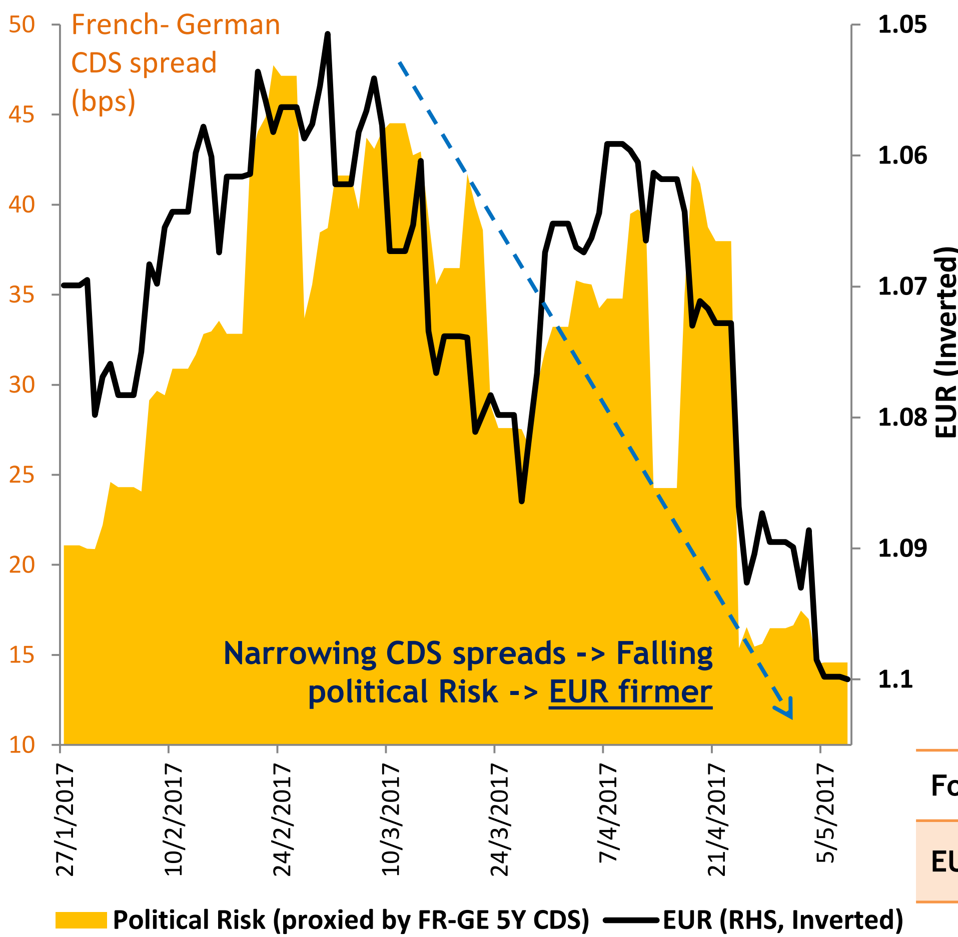
Source: Bloomberg, Maybank FX Research

Key Macro Questions for 2017

Political Risks Receding?

Unwinding of Political Concerns Reduces Negativity on the EUR

Falling Political Risk (Proxied by French-German CDS spread) sees EUR firmer



Source: Bloomberg, Maybank FX Research

- Political concerns in Europe are gradually receding after Netherlands and France Presidential elections got by with no major downside surprise
- Populism policies (anti-EU, anti-Immigration) suffered setbacks as Euro-club stability stays intact
- **Receding political risks and no impetus for ECB to add to QE should keep EUR supported (EUR, a strategic buy on dips)**

Forecast	2Q 2017	3Q 2017	4Q 2017	1Q 2018	End 2018
EUR/USD	1.0800	1.0700	1.0800	1.1000	1.1200

But Some Worries Still Remain – French Legislative/ Italy?

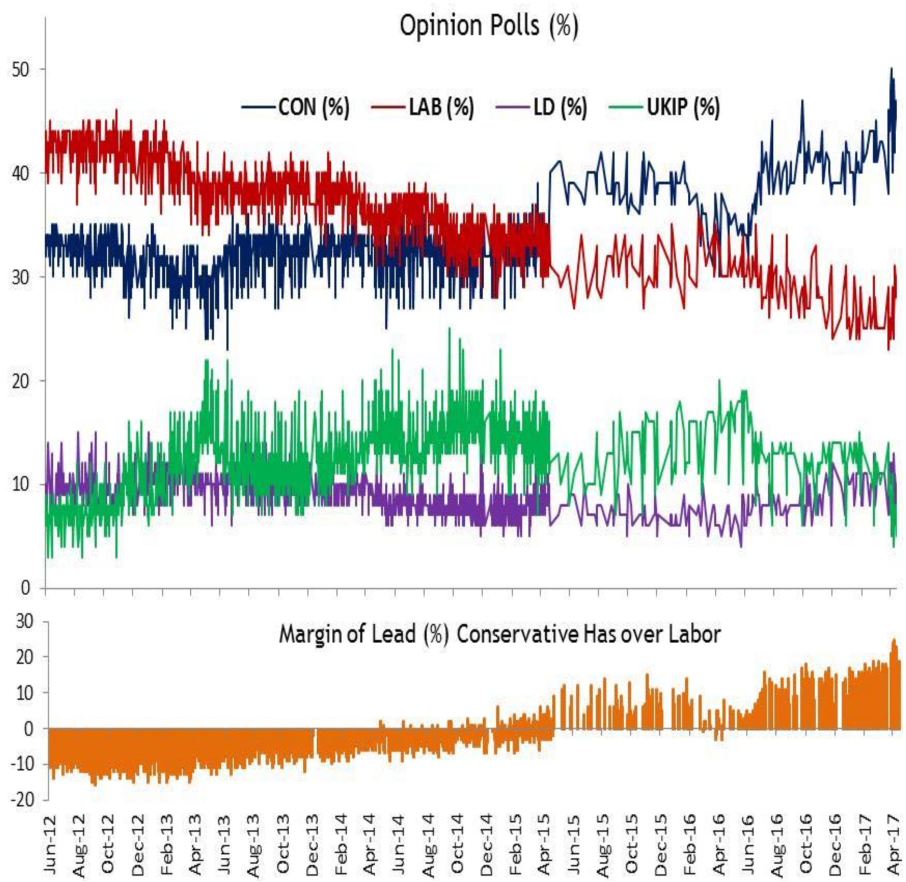
- **Upcoming Legislative Elections in France (11 and 18 Jun)**
  - Unclear if President Macron can secure parliamentary majority of 289 seats (out of 577 seats)
  - To secure a majority is crucial in order for Macron to push through reforms, or risk being a ‘lame duck’ President

- **Italy General Election – the next scare?**
  - No date firmed; rumored date: as early as in Jun 2017
  - Next GE to be held no later than 20 May 2018
  - Could re-ignite political concerns as recent polls suggest Five Star Movement (anti-establishment) is in the lead (if election is held now)

- **German Federal election (Sep-2017)**
  - Early polls suggest no downside surprise for now

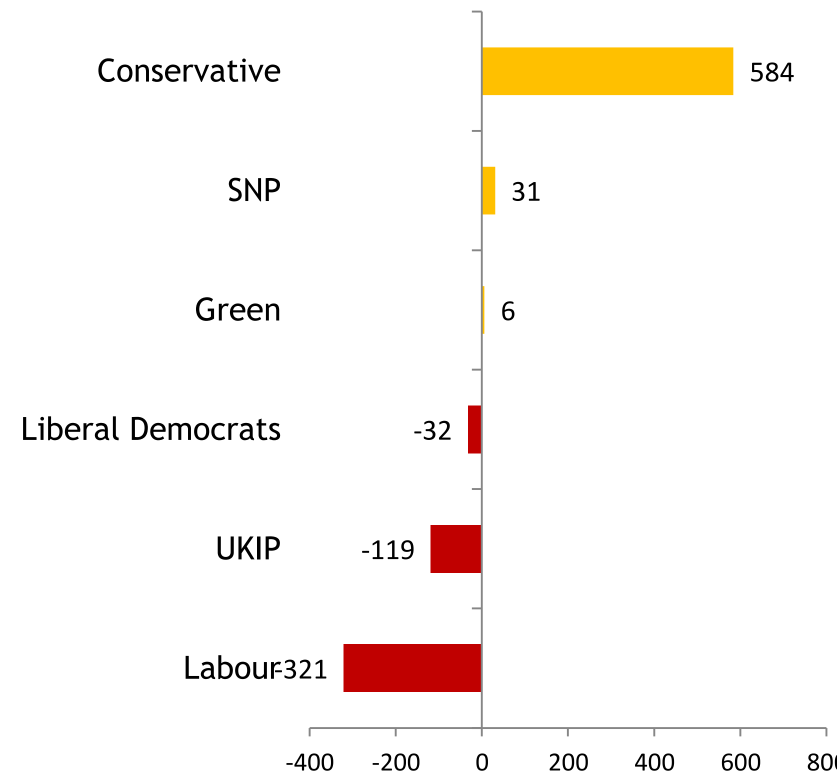
Upcoming UK General Elections – Polls Pricing in No Surprise

Early opinion polls continue to show a widening margin of lead the Conservative has over Labor -> Indication of Landslide victory for Theresa May



Source: UK Polling Report, FT, Maybank FX Research

Local Election Results (4 May 2017) showed that PM May's Conservative party made huge gains while Labour and UKIP have lost badly

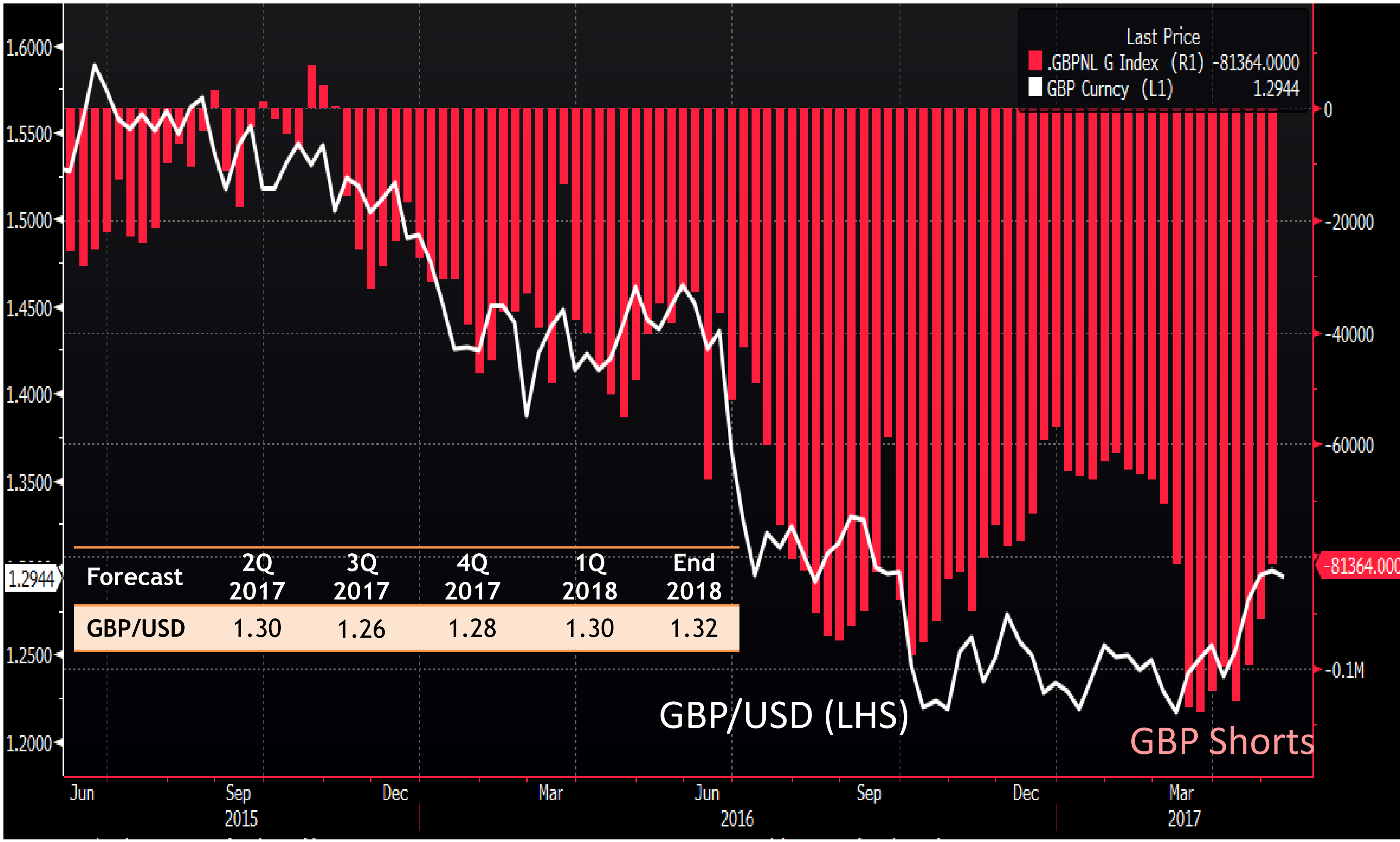


Note: A total of 4,581 council seats were up for grabs in England, Scotland and Wales. Local election held on 4th May 2017

Political Risks Receding

Leading to Unwinding of GBP Shorts Positioning

GBP/USD, GBP CFTC Positioning

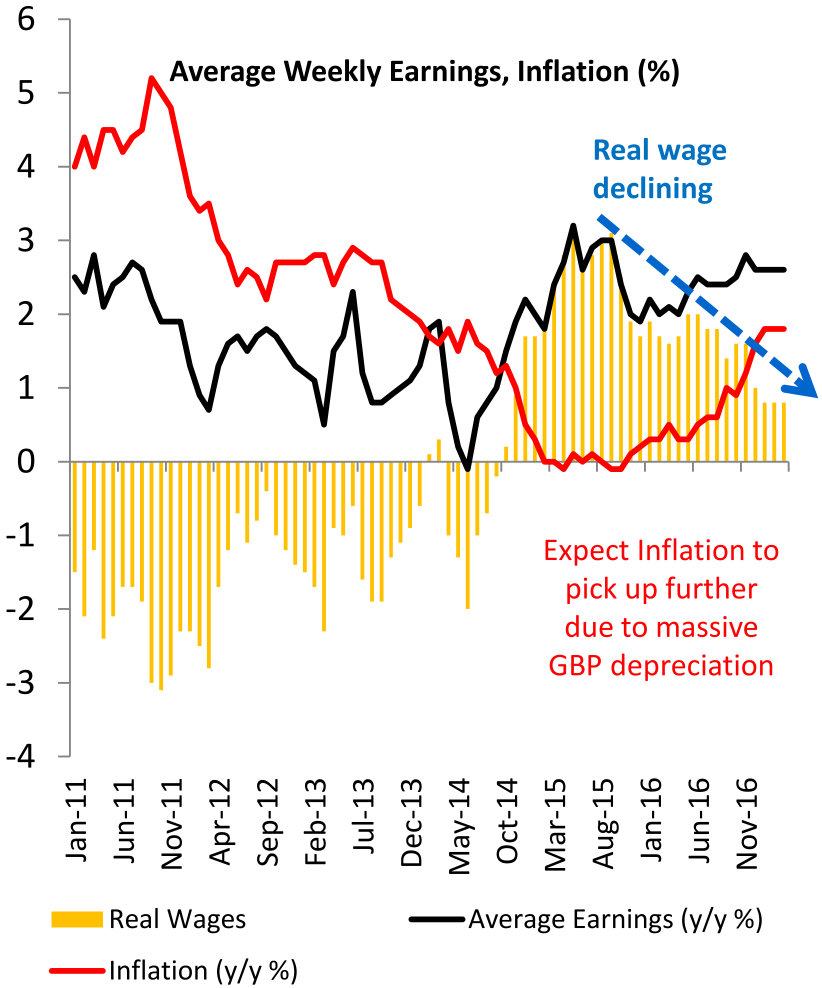


Forecast	2Q 2017	3Q 2017	4Q 2017	1Q 2018	End 2018
GBP/USD	1.30	1.26	1.28	1.30	1.32

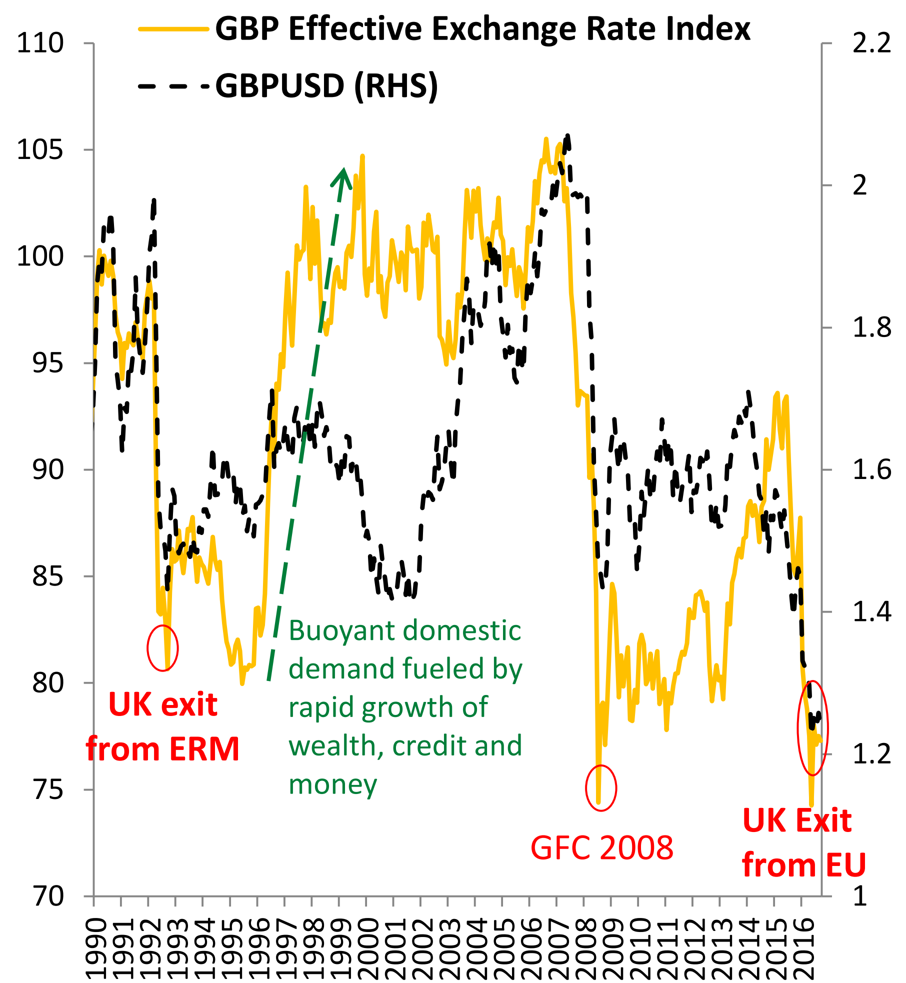
Source: Bloomberg, Maybank FX Research

GBP Upside in Medium Term but Choppy in the Short Term

Rising Inflation and Decelerating Wage Growth Crimps Household Budget

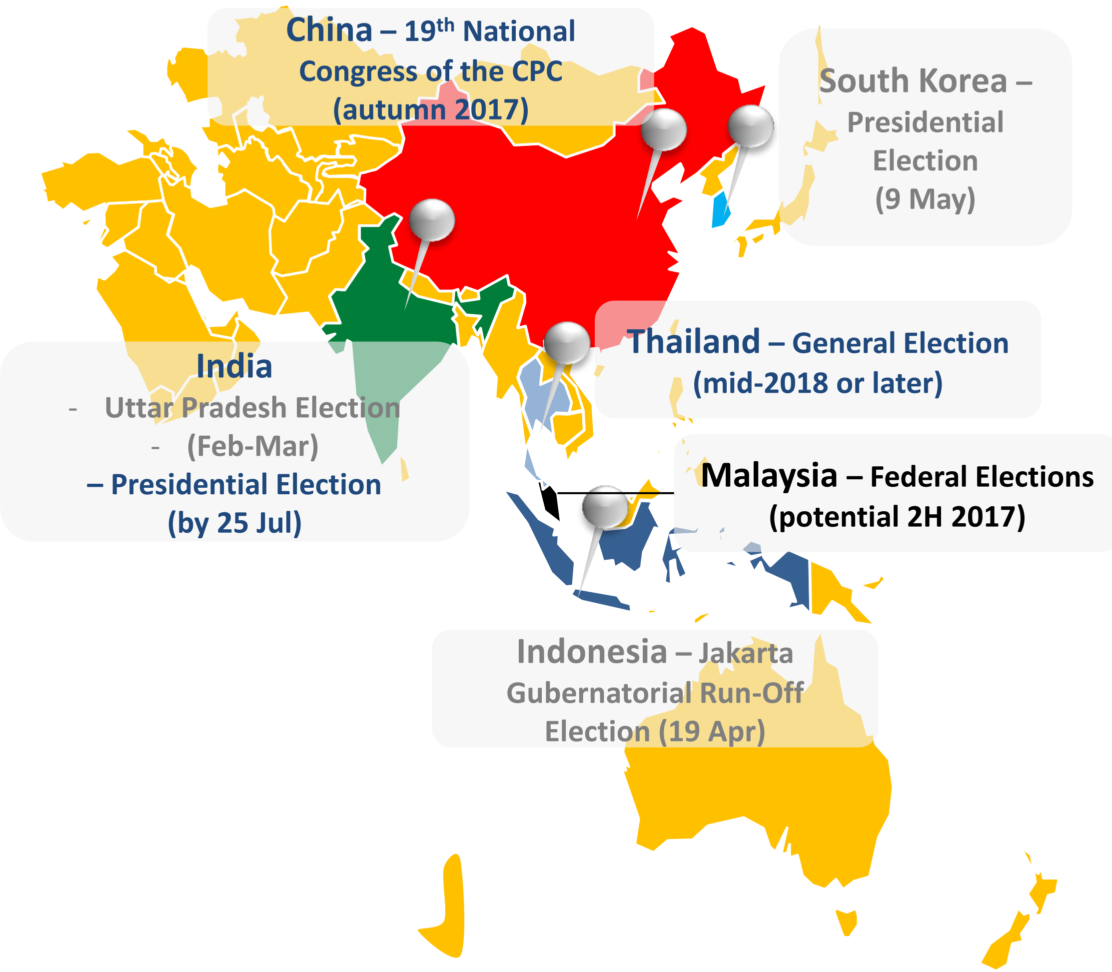


An Eventual Bounce after a period of Rebalancing and Recovery in Investor Sentiment



Source: Bloomberg, Maybank FX Research

Regional Political Risks Are Also Receding, Except for Thailand



Key Political Events in Asia

Thailand
- ➢ General Election *(mid-2018 or later)*

India
- ~~➢ Uttar Pradesh State Election *(Feb – Mar)*~~
- ➢ Presidential Election (*must be held before 25 Jul*)

Indonesia
- ~~➢ Jakarta Gubernatorial Run-Off Election (19 Apr)~~

China
- ➢ The 19th National Congress of the CPC (*2017 autumn*) *PBoC may want to keep yuan stable nearing the event.

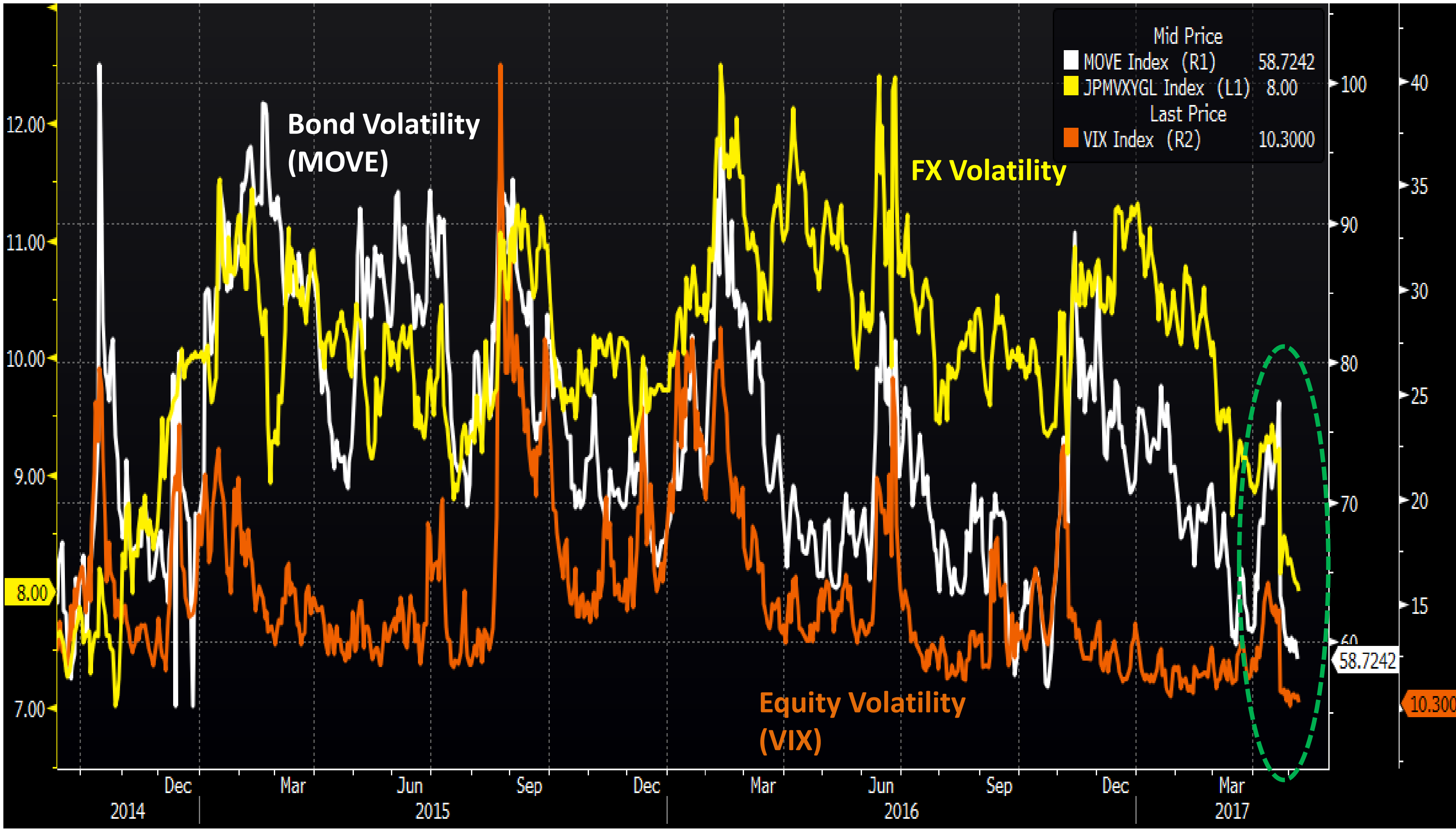
S. Korea
- ~~➢ Presidential Election (9 May)~~

Malaysia
- ➢ Potential Federal Elections – a positive for MYR and MY assets

Note: All dates of key political events are accurate as of 8 May 2017.
Source: Maybank FX Research

Political Risks Receding

Implied Volatilities Have Also Fallen to Multi-Period Lows



Source: Bloomberg, Maybank FX Research

Key Macro Questions for 2017

The Multi-Dimensional Asia FX?

JPY – Bearish Outlook; Weighed By Policy, Yields & Equities

CNY - Still Taking the Cue from USD

MYR – Positive Outlook; Playing Catch Up

SGD - Neutral Outlook; MAS Could Move In Oct

IDR - Neutral Outlook; Anticipating S&P Sovereign Credit Rating Upgrade

THB - Bearish Outlook; Political Risks To Re-Emerge

PHP - Bearish Outlook; Deteriorating Current Account Balances Weighs

INR - Resilience; Careful of Short Term Downside

Bearish On JPY

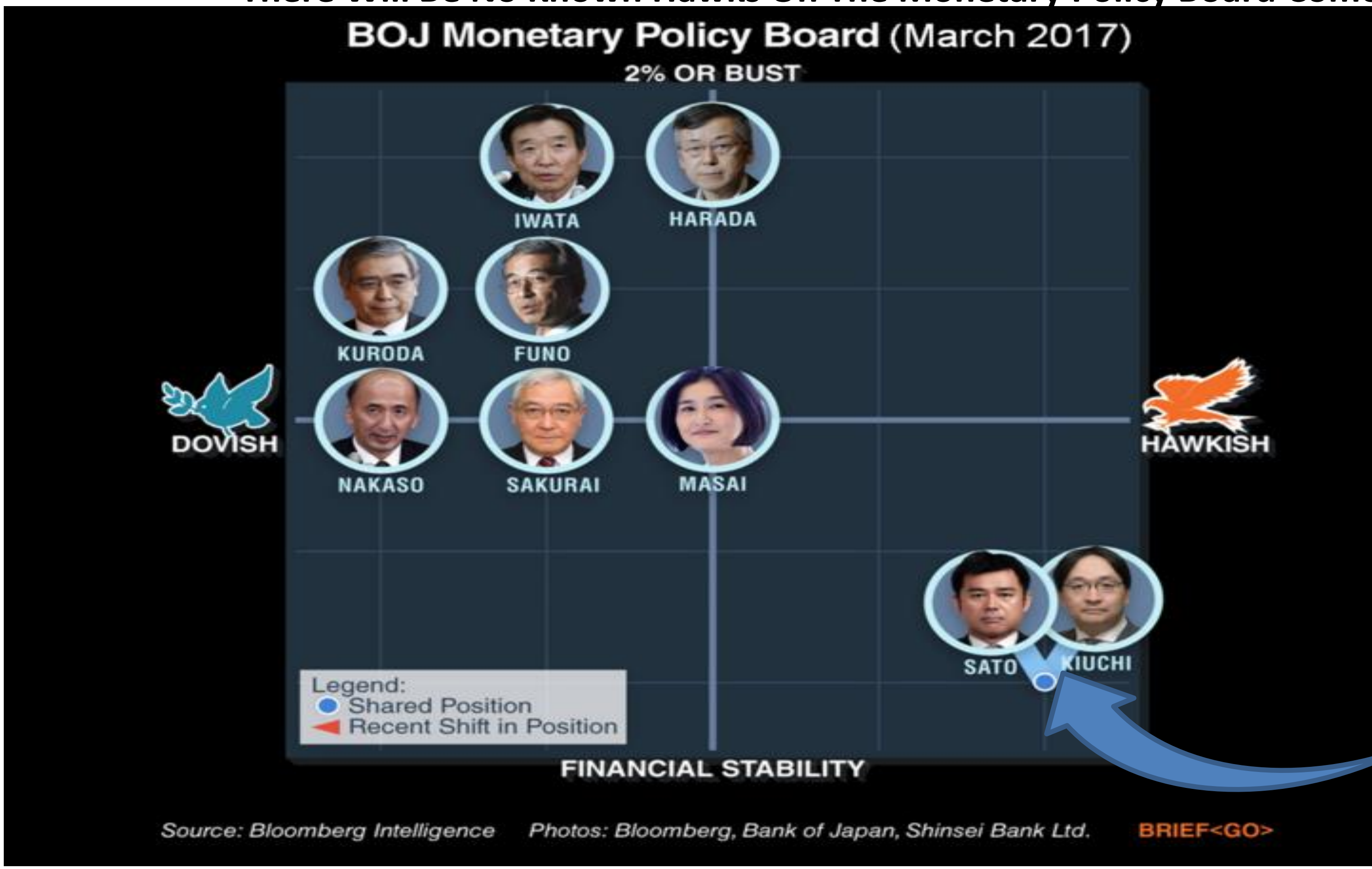
1. Key JPY Drivers
    a. Ultra-loose monetary policy to remain in place until 2% inflation target is achieved
    b. Widening yield differentials between UST-JGB
    c. Positive sentiments encouraging foreign investment in equities

2. Challenges/Risks Ahead
    a. Signaling end/tapering of current monetary policy
    b. Re-emergence of geopolitical risks to spur safe-haven flows

3. Strategy
    a. Bias to long USDJPY on sensitivity to rising UST yields

No End To Ultra-Loose Monetary Policy In Sight Yet

The Doves Are Set To Increase Their Domination Of The BOJ -
There Will Be No Known Hawks On The Monetary Policy Board Come Jul

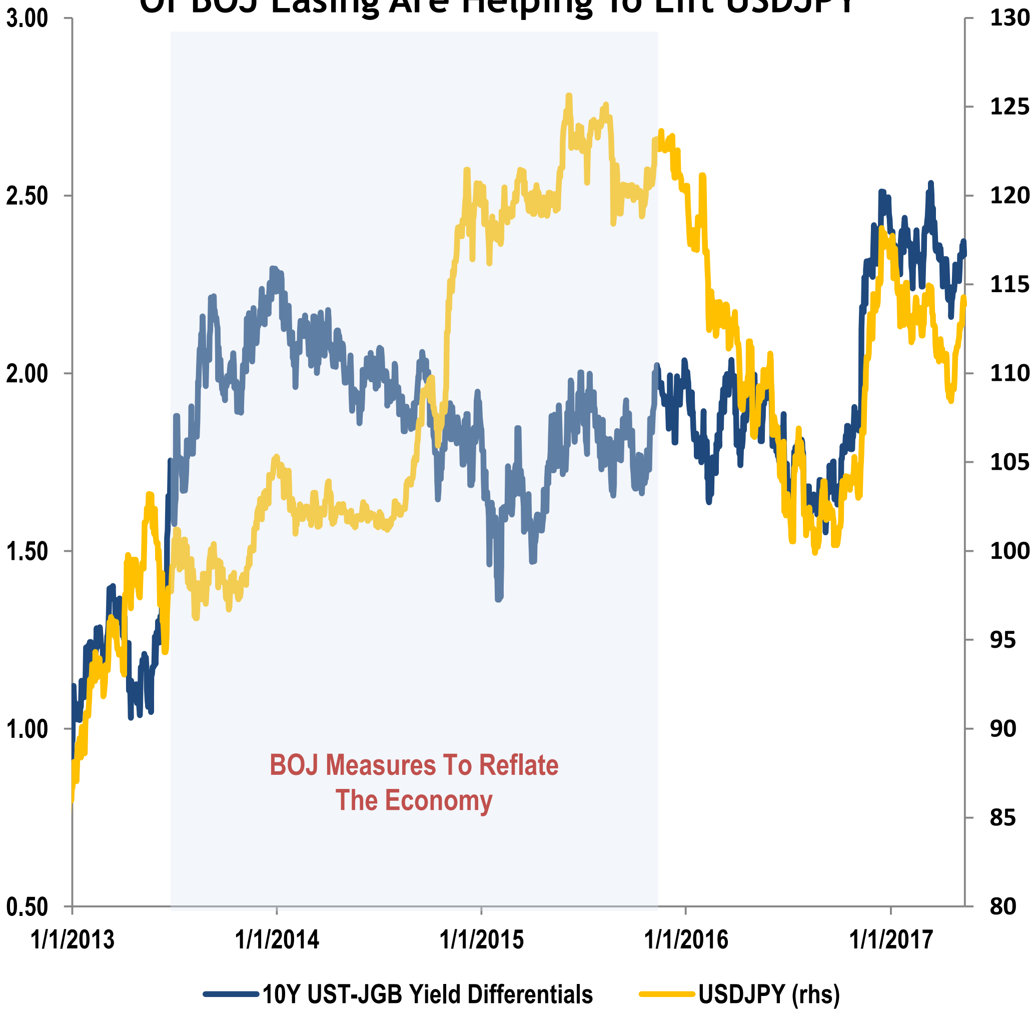


Hitoshi Suzuki - a banker with commercial banking and financial markets in Japan and abroad - and Goshi Kataoka - an economist viewed as a reflationist – are set to replace Takahide Kiuchi and Takehiro Sato (term ends 23 Jul) on the Monetary Policy Board

Source: Bloomberg, Maybank FX Research

Widening Yield Differentials Lifts USDJPY Higher

Widening UST-JGB Differentials Against A Backdrop Of BOJ Easing Are Helping To Lift USDJPY

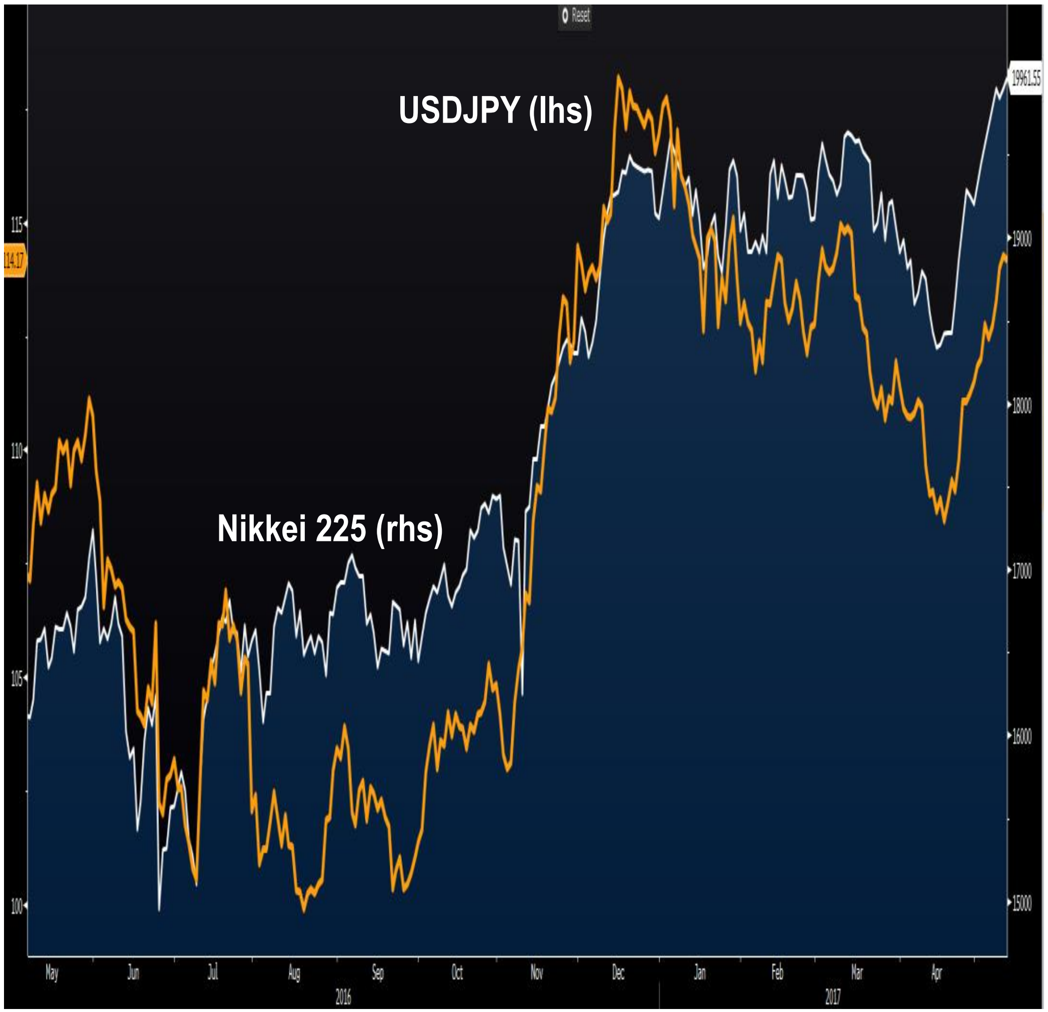


Source: Bloomberg, Maybank FX Research

- JPY subjected to depreciation pressures due to:
  - On-going ultra-loose monetary policy as inflation has yet to gain traction;
  - USD strength on Fed rate hike expectations (monetary policy divergence)
- Expect USDJPY to trade higher on widening UST-JGB yield differentials
- Moves higher though could be tempered by global risk aversion

Receding Global Risk Sentiments Supportive Of USDJPY

Foreign Inflows Into The Nikkei Should Lift The USDJPY Higher



Source: Bloomberg, Maybank FX Research

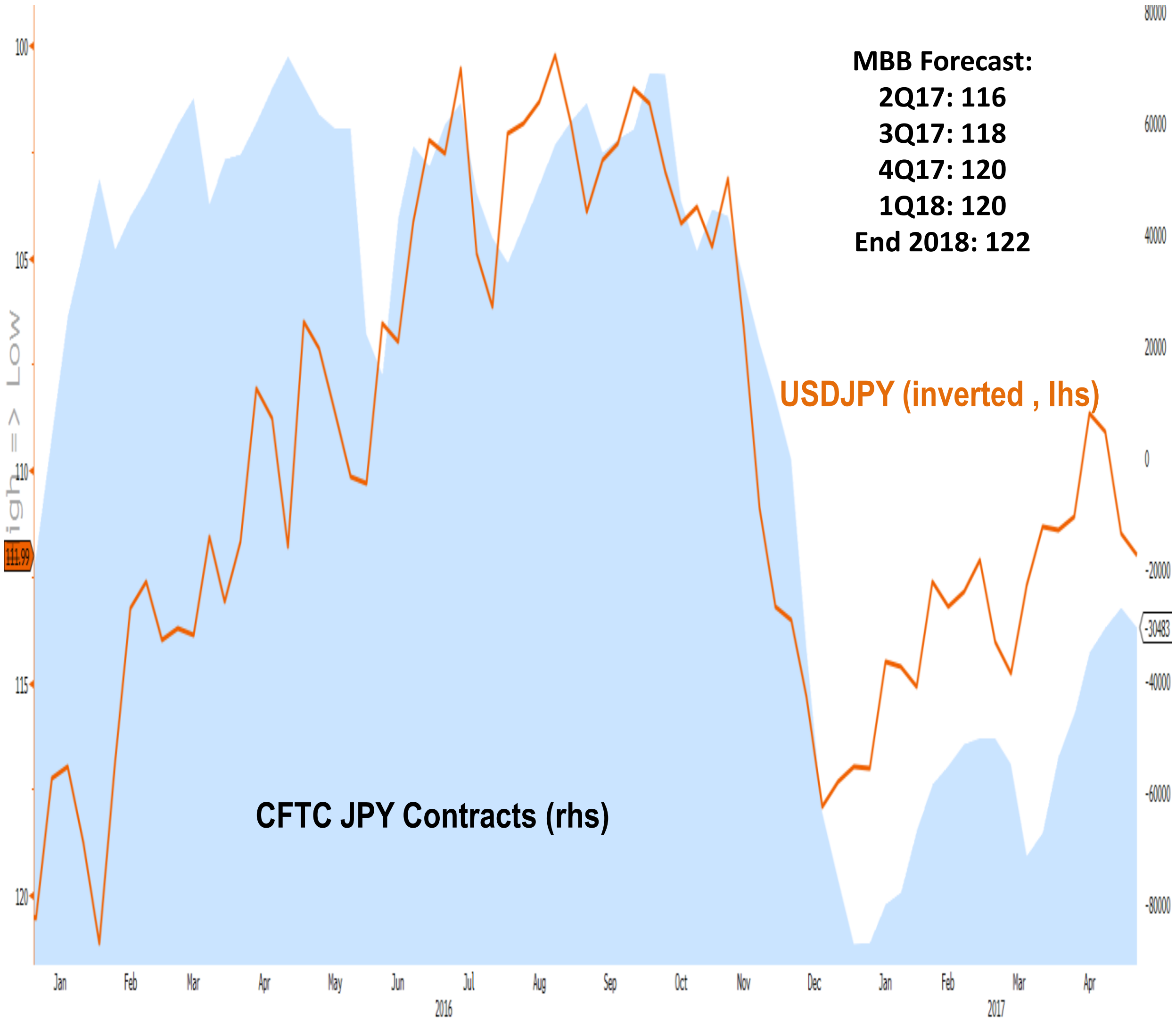
- The receding concerns about geopolitical risks, namely political uncertainty in France and on the Korean Peninsula, has shifted focus back to earnings and equities particularly in Japan

- The inflows of foreign funds into Japanese equities have help to lift the Nikkei within striking distance of the high seen in Jun 2015 (20868; currently at 19962).

- These inflows are supportive of the USDJPY as seen in the high correlation between the USDJPY and the Nikkei. <u>This is because foreign investors usually hedge their equity purchases against further JPY depreciation by short-selling the JPY</u>.

- Further inflows into the Nikkei should be supportive of the USDJPY at 120 by end-2017.

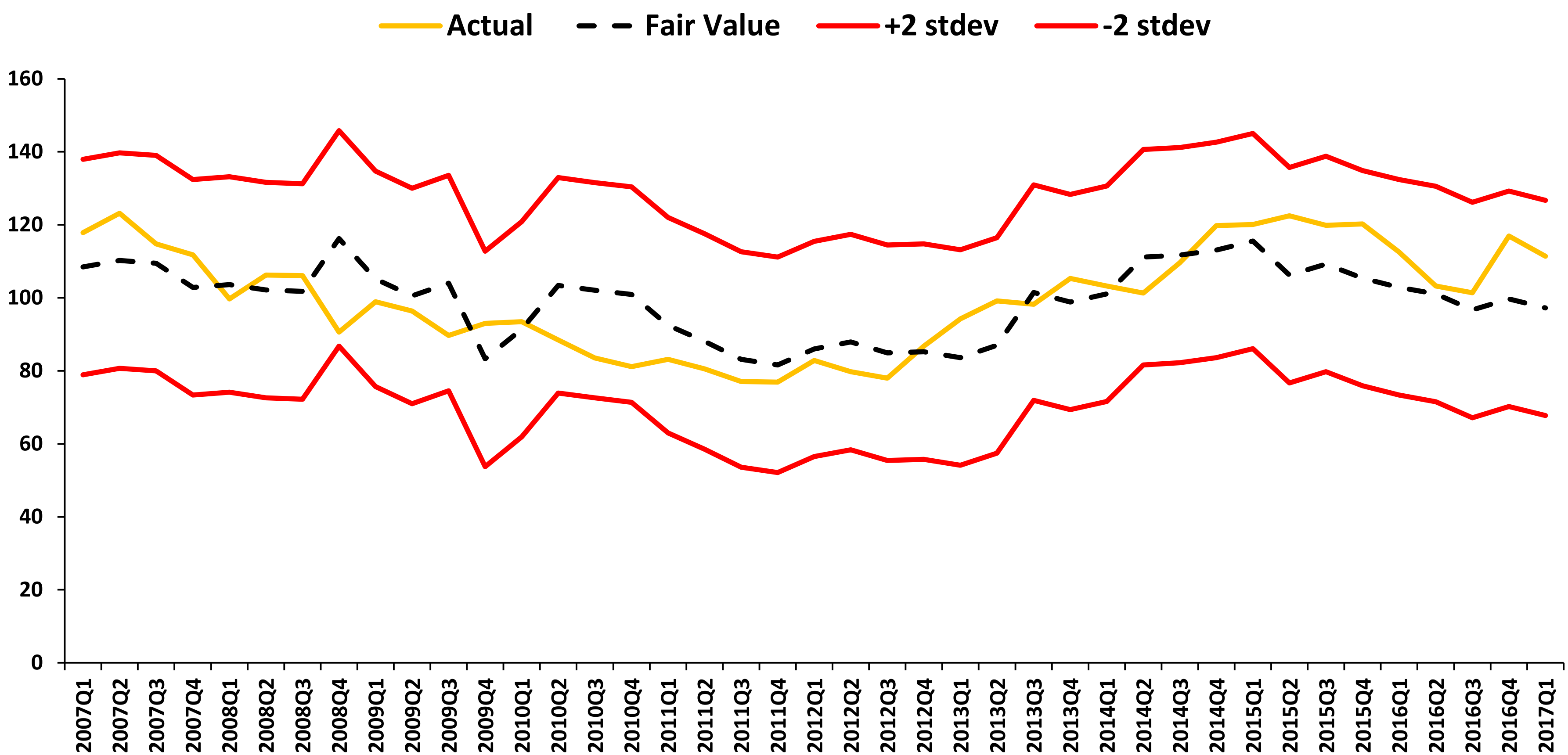
Bets On JPY Weakness Have Rebounded



Source: Bloomberg, Maybank FX Research

- Recent CFTC data showed that speculators are still positioned for JPY weakness.
- But such bets are still way off those seen in Dec 2016. This suggests that there could be further room for net short-JPY bets ahead
- We watch for a re-pricing of Fed rate hike expectations. <u>A continuous climb in UST yields with the JGB holding steady around current levels could lead to further increases in net short-JPY bets</u>
- Which should lift USDJPY towards our forecast of 120 by year-end.

JPY Fair Value Estimates at 100 Levels



FX Tracking shorter-to-medium term model: To estimate the **medium term fair value range of USDJPY** based on 3 cyclical factors – the differential between Japan and US current account to GDP ratios; 10Y bond yield differentials between Japan and US adjusted for inflation and a reflation proxy defined as the ratio of World Equities to World Government bonds

Source: Eviews, CEIC, Bloomberg, Maybank FX Research

RMB - How Will RMB Be Managed In 2017?

"***the RMB exchange rate will be further liberalized, and the currency's <u>stable position</u> in the global monetary system will be maintained***".

~ Premier Li Keqiang NPC 2017

"improvements will be made to the market-based mechanism for setting the RMB exchange rate to ensure it remains generally stable at an appropriate and balanced level".

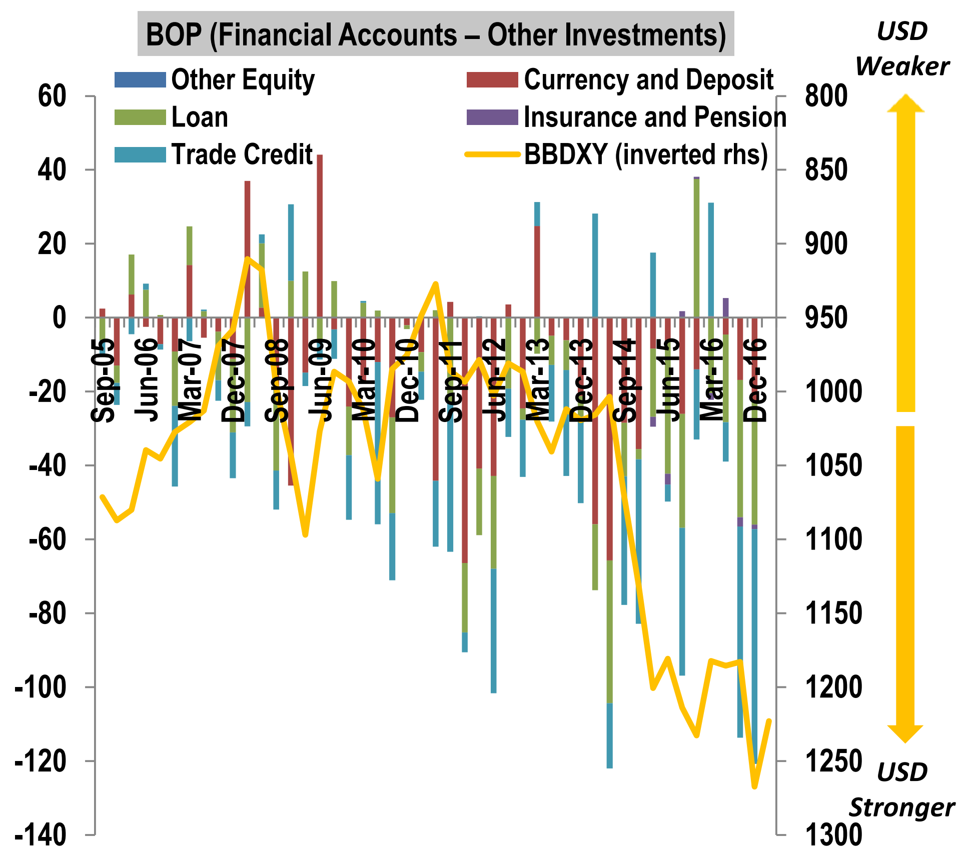
~ Premier Li Keqiang NPC 2016

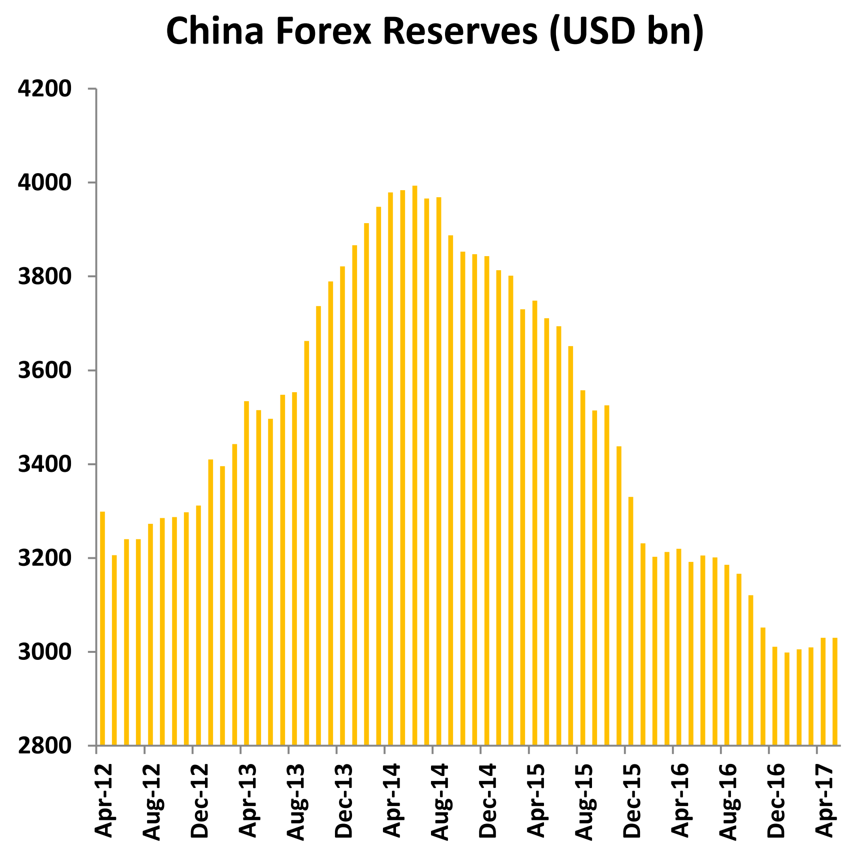
Our View

- RMB is **Unlikely to Make Waves** This Year, **More Likely to Take the Direction From The USD** as Fed prepares to raise rates more than once (unlike 2015, 2016).
- **No Major Reforms** That Would Generate a Spike In Volatility
- China is serious about wooing foreign institutional investors to their bond and equity markets. **Allowing market forces** to guide yuan more would prevent a build-up in pent-up depreciation pressure, bring about more credibility in the spot pricing of the yuan, lessen the need for FX policy guidance/changes and even capital controls.
- "Stable position" will be "maintained" against the CFETS, BIS and SDR basket by using FX reserves.

RMB - Capital Outflows Is Still A Concern

Capital Outflow Is At The Back of Policy Makers' Minds But USD Weakness Provides Relief….



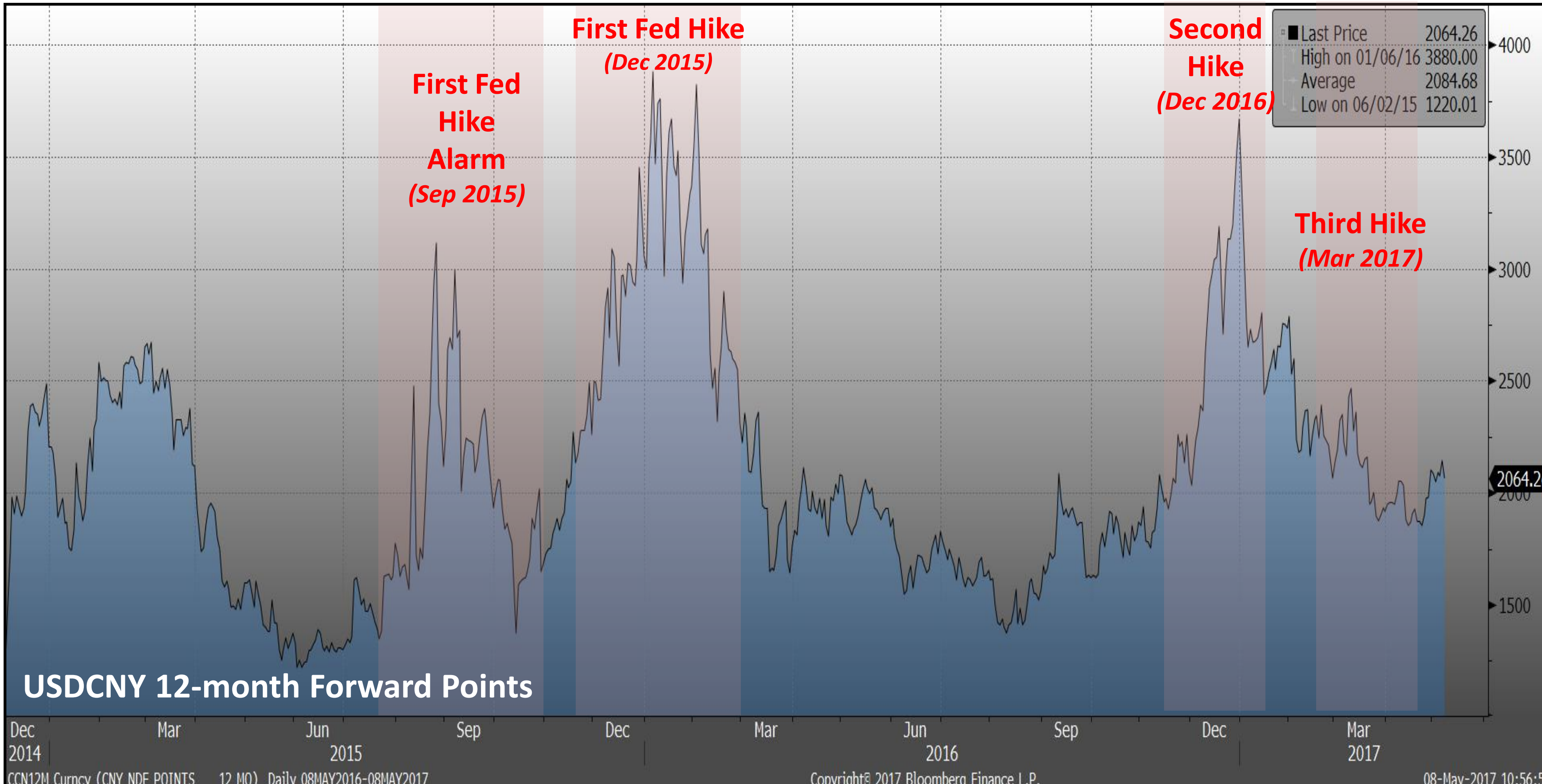


Since 2014 (when China started capital account liberalization in earnest), outflows have persisted in the form of trade credit, loans and to a lesser extent currency and deposit. This is exacerbated by the strong USD environment

The Forex Reserves have recorded three consecutive months of mild increase owed not just to capital controls but also, USD weakness….

RMB - Markets Are Pricing In Less Depreciation Pressure

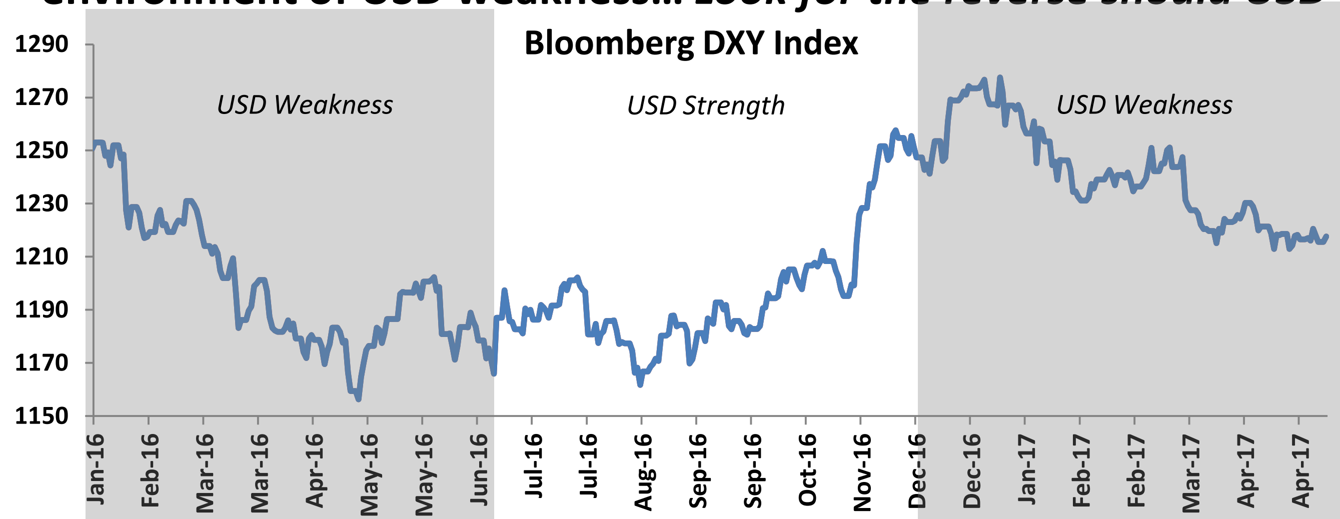
RMB Depreciation Expectation Tends To Heighten Along With Fed Rate Hike Expectations

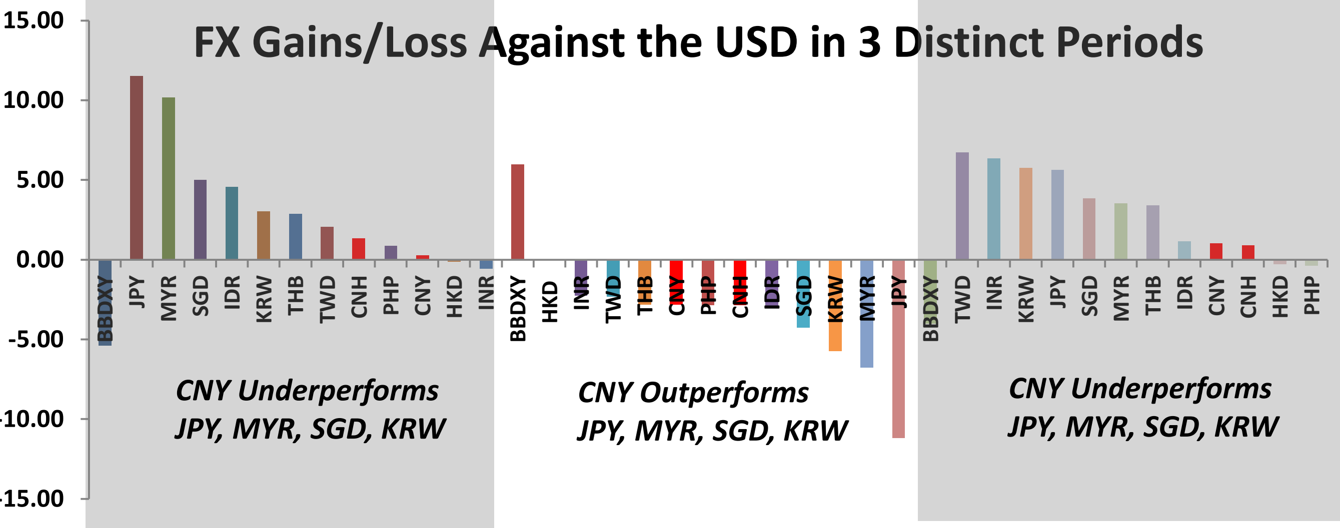


However, along with the muted USD moves,
RMB depreciation pressure *has lessened* with each recent hike…

RMB - Still Taking The Cue From The USD

How To Play? RMB seems to consistently underperform against export oriented FX in an environment of USD weakness… *Look for the reverse should USD recover…*





In an environment of USD strength,

Recent episodes have shown that CNY could outperform export-oriented FX (JPY, MYR, SGD, KRW).

Against the USD, CNY should weaken and we look for this pair to head towards 7.04 by the end of this year.

MBB Forecast:
2Q17: 6.95
3Q17: 7.01
4Q17: 7.04
1Q18: 7.04
End 2018: 6.90

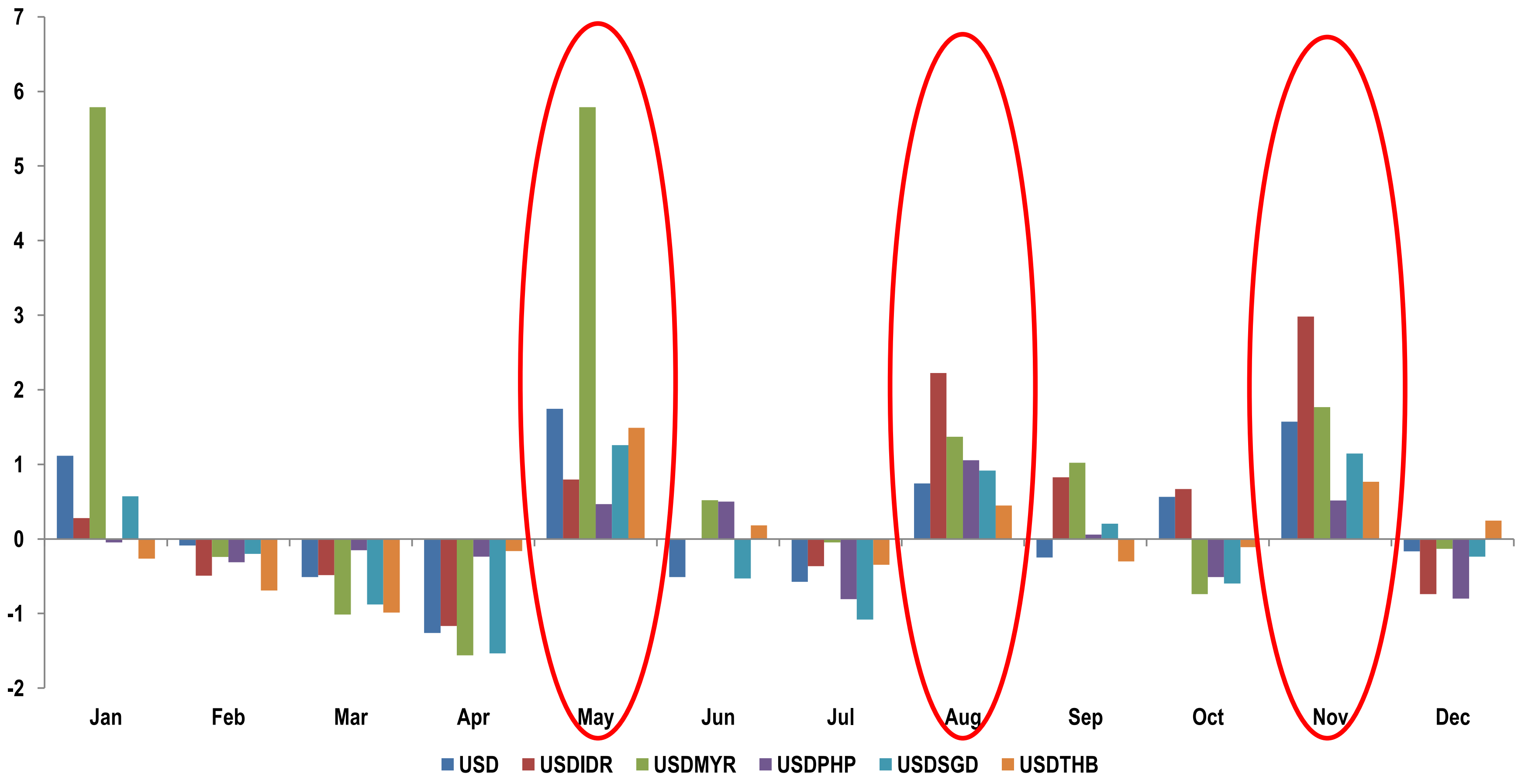
ASEAN FXs Have Picked Up Since Nov But Is This Sustainable?

Note: Maybank ASEAN-5 FX is comprised of SGD, MYR, IDR, THB, PHP, equally-weighted vs the USD

Source: Bloomberg, Maybank FX Research

Seasonality Suggests Risks To USD/ASEAN FX Are To The Upside

May, Aug and Nov Are Not Good Months For USD/ASEAN FX

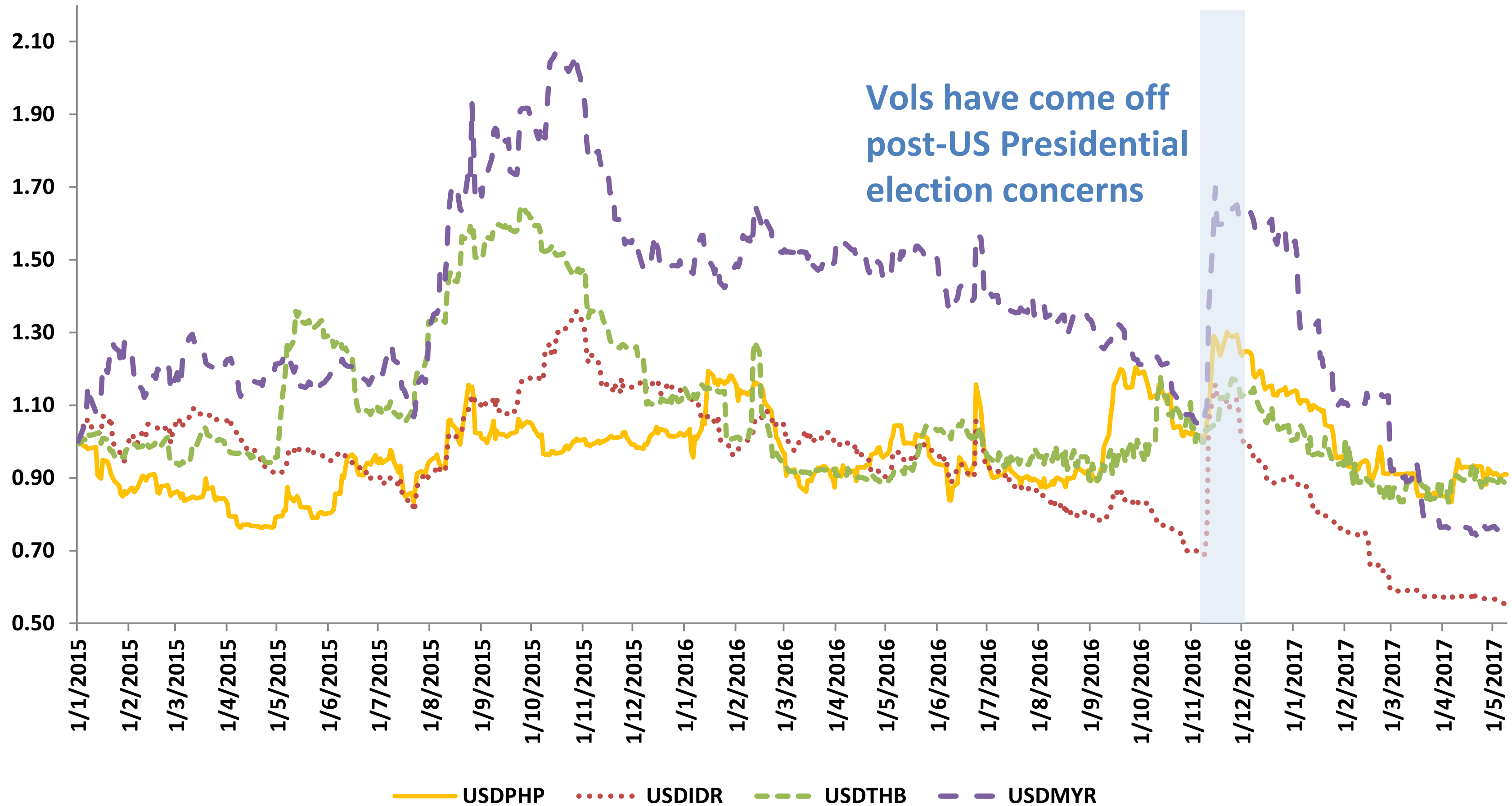


Note: Based on 10-year averages of monthly currency movements (2007-2006)

Source: Bloomberg, Maybank FX Research

FX Volatility Has Been On The Slide Since The US Presidential Election

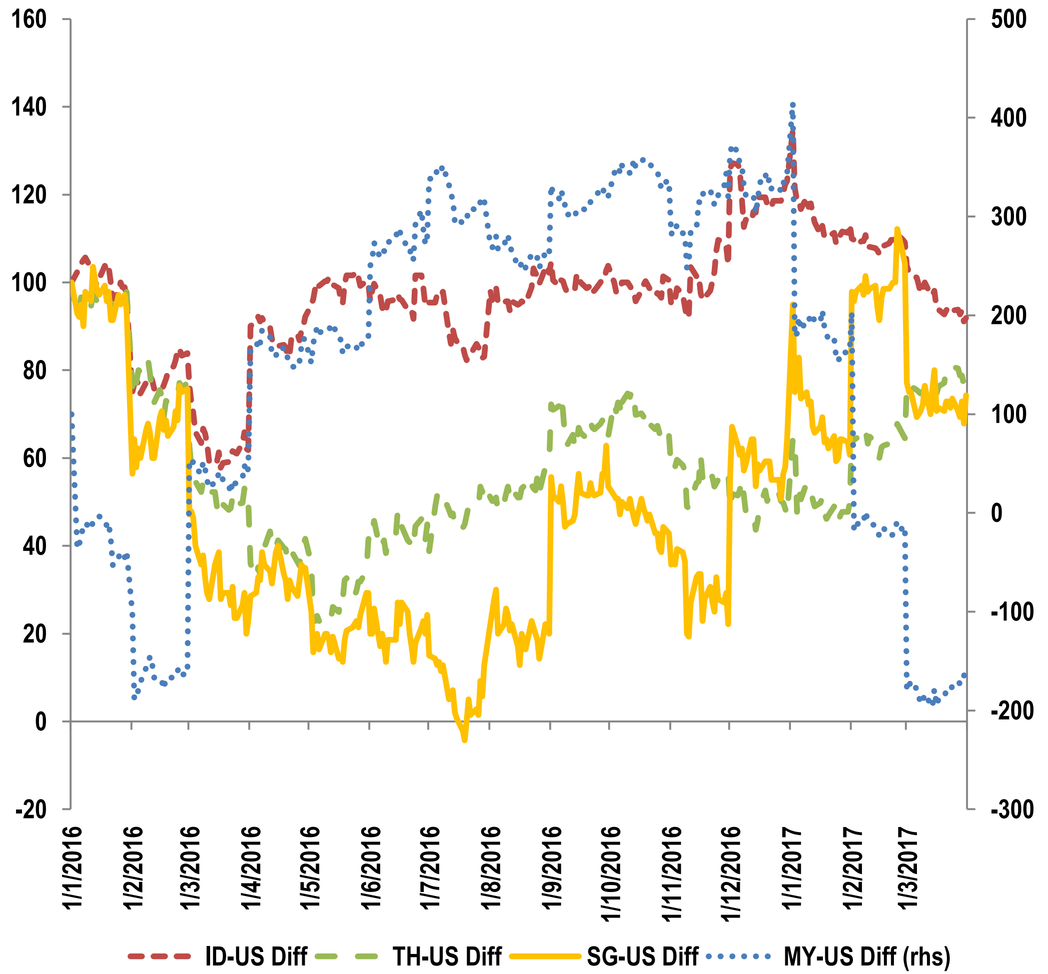
PHP, THB Vols Have Remained Elevated Compared To Its Peers; Likely Due To Domestic Politics



Note: Volatility based on 3-month ATM

Source: Bloomberg, Maybank FX Research

Real Yield Differentials Suggests Differing Pace Of Inflows, Impact On FX



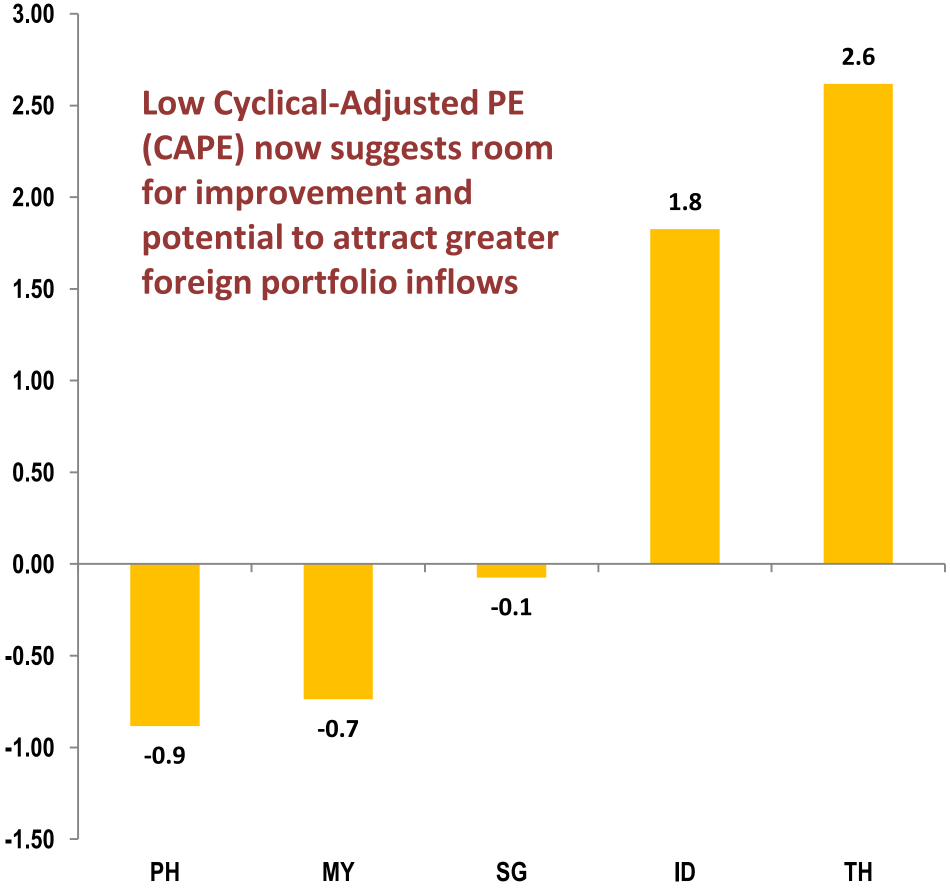
Note: Yield differentials between domestic 10Y yields and 10Y UST yields

Source: Bloomberg, Maybank FX Research

- Real yield differentials for ID has been narrowing after reaching a peak in Feb this year but are still elevated vs. its peers
- But this elevated positive yield differentials between the UST and Indonesian government debt could make Indonesia debt attractive to foreign investors, a positive for IDR
- Yield differentials between US and Singapore and with Thailand are on the rise, indicating potential inflows to TH and SG government debt
- This suggests possible upside to THB and SGD
- Malaysia real yield differentials remain in negative territory and may not see inflows to government debt

CAPE Valuation Suggests PHP & MYR Attractiveness In Longer Term

Potential Upside To PHP & MYR In The Longer Term From Inflows Into Undervalued Equities



Note: Cyclical adjusted P/E ratio (CAPE) is defined as price divided by the average of 10 year earnings (both adjusted for inflation)

Source: Bloomberg, CEIC, Maybank FX Research

- From a CAPE perspective, continued inflow into ASEAN equities could be supportive of ASEAN FX in the longer term
- Philippines is attractive in the longer term but faces near-term stresses from the president's overly aggressive anti-drug policy and his temperament that could hold portfolio inflows
- Malaysia is also attractive in the longer term given as current under-valuations could prompt a re-evaluation
- Indonesia position is ambiguous but high real yields (highest in the region) and rising commodity prices makes its bonds and equities attractive in the near term
- Singapore and Thailand are less attractive destination for equity inflows in the longer term.
- Malaysia real yield differentials remain in negative territory and may not see inflows to government debt
- In the near term (3-6 months), foreign investment flows could still favor Indonesia than Philippines or Thailand.

Positive on Ringgit Outlook

- **External Factors are Supportive**
  - Global Oil supply-demand is rebalancing 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 (+26.5% y/y in Feb) amid accommodative monetary policy (OPR at 3%)
  - Re-calibrated supportive budget, on a lower oil price assumption suggests flexibility in the fiscal space
  - 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

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

Forecast	2Q 2017	3Q 2017	4Q 2017	1Q 2018	End 2018
USD/MYR	4.3000	4.2500	4.3000	4.3500	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)

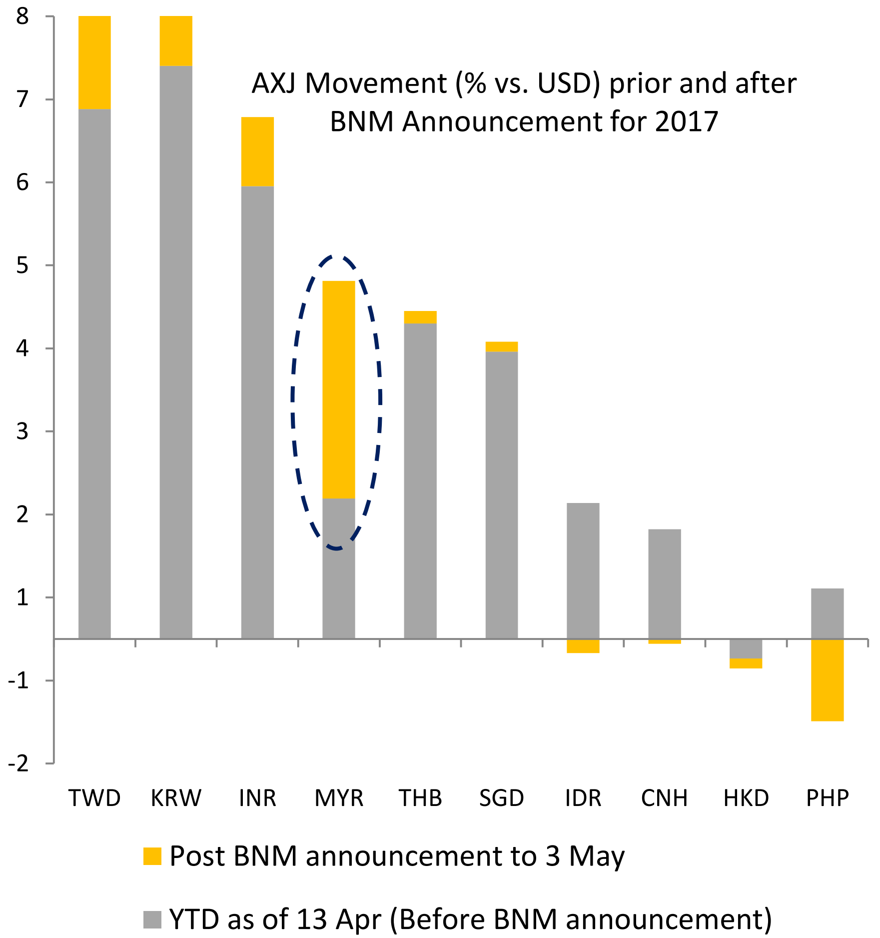
- **Strengthen Financial Market Infrastructure**
  - Information reporting and settlement infrastructure will be enhanced for greater transparency and to facilitate surveillance on the onshore financial market (over 12 – 18 month period)

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**

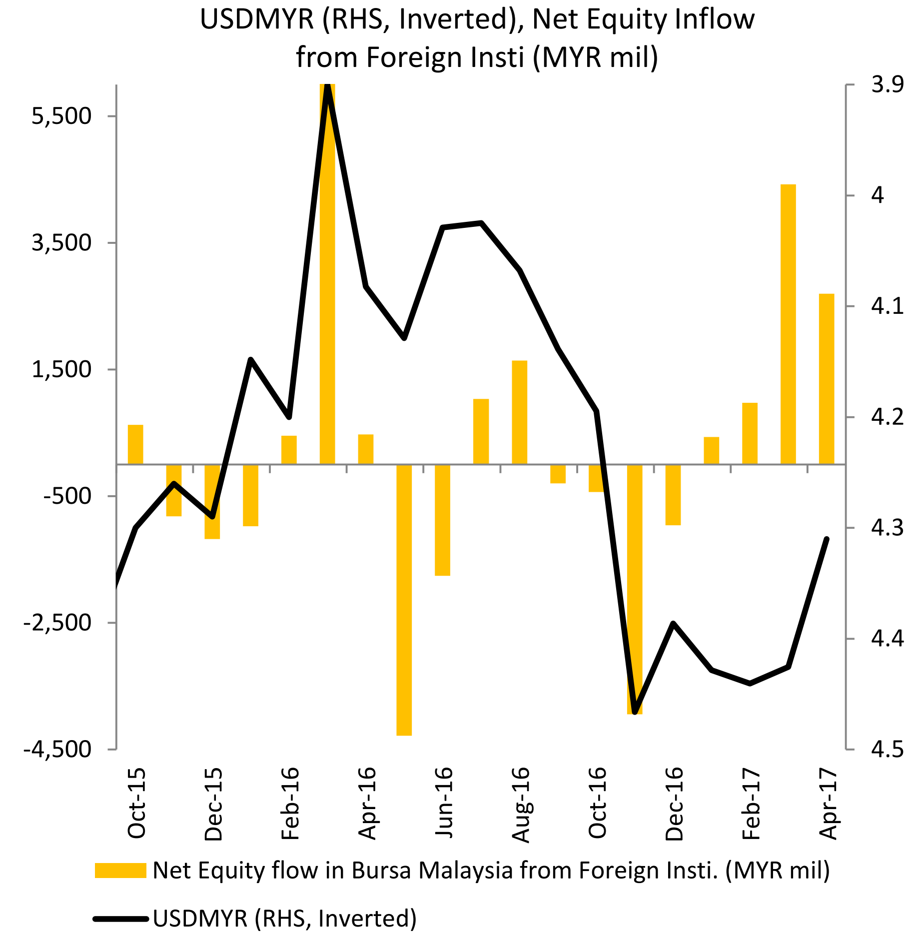
Note: BNM Initiatives announced 13 Apr, effective 2 May 2017 for points 1 - 3

Stability Gradually Returning to the MYR

MYR playing catch up with other AXJs post-BNM announcement; YTD gains now surpassed other ASEAN FX

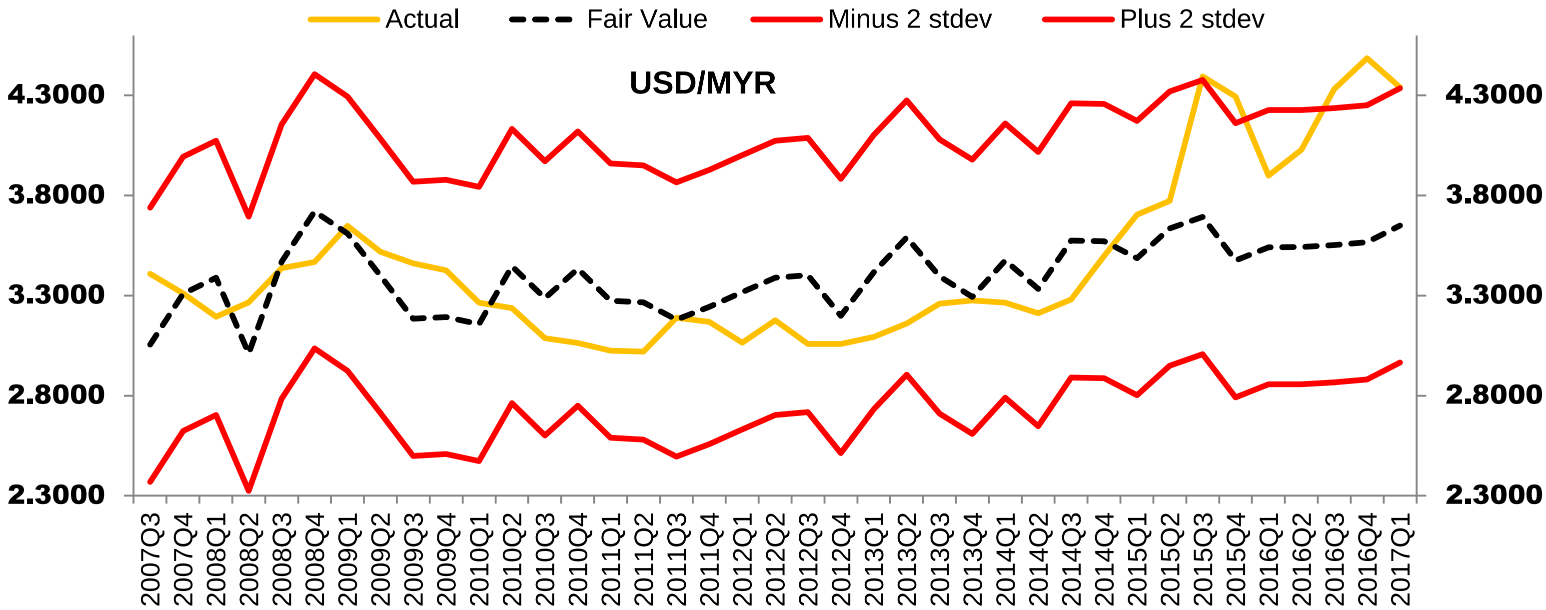


MYR Rebounding on Foreign Inflows in Bursa Malaysia



Source: Bloomberg, Maybank FX Research

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 <u>**not**</u> a reflection of fundamentals but market sentiment
- Our fair value suggests MYR is about 16% undervalued relative to medium term fair value
- Economy still on track to expand at 4-5% 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

Neutral on SGD Outlook

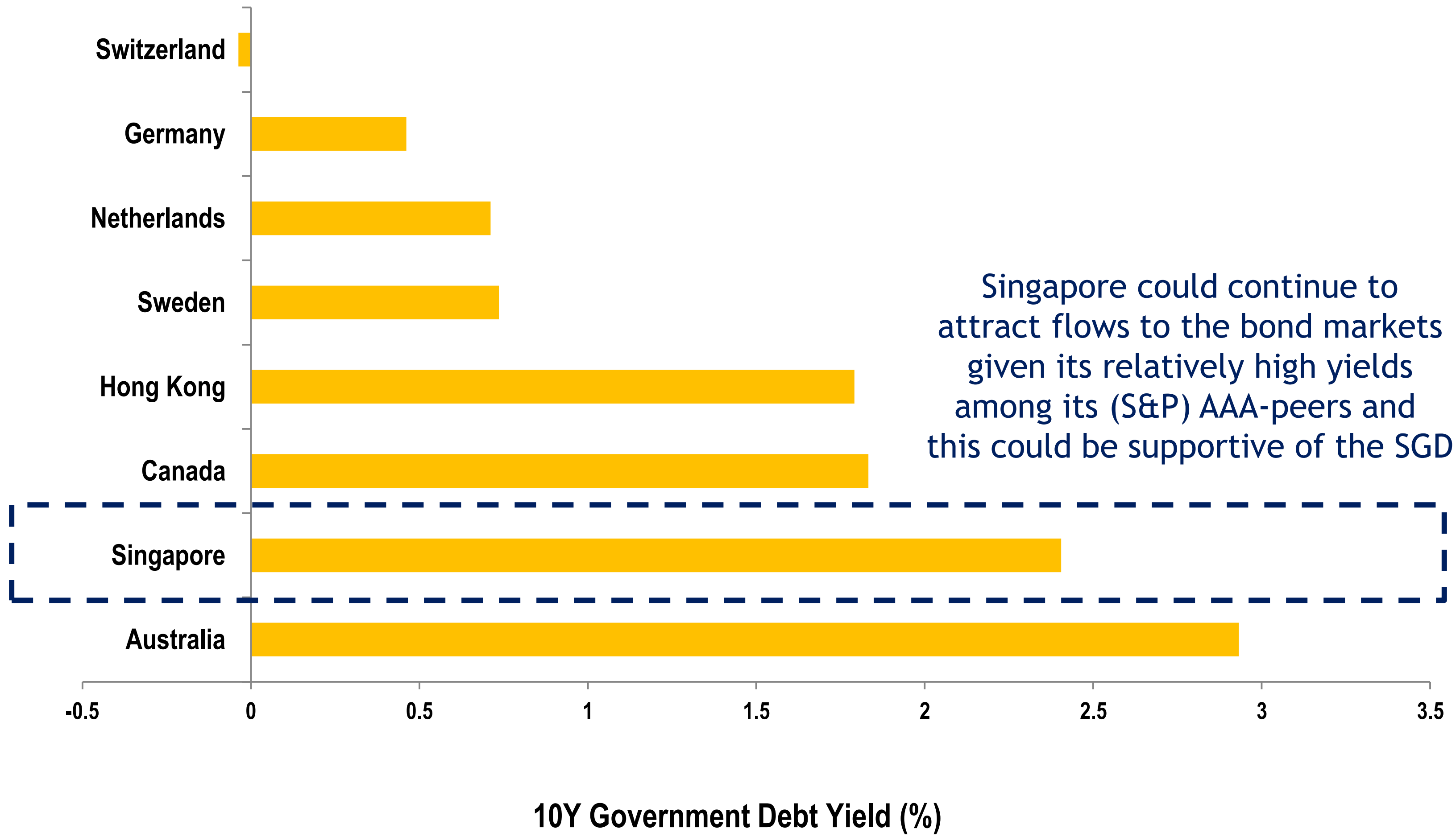
1. Key SGD Drivers
   a. Expansionary fiscal policy together with accommodate monetary policy should put a floor on the SGD
   b. Persistent current account surpluses and quasi-safe haven inflows as a consequence of being the only Triple-A rated economy in Asia.
   c. Potential shift in monetary policy to a 'mild appreciation' stance in 4Q should be supportive

2. Challenges/Risks Ahead
   a. Failure of domestic growth and/or core inflation to gain traction could see accommodative monetary policy extended for longer
   b. External headwinds (lower global growth in the region, China and G3) weighs on the economy
   c. Aggressive Fed rate hikes and balance sheet reduction could strengthen the USD even more

3. Strategy
   a. Move to tighter monetary policy should be supportive of the SGD and the USDSGD should end the year around 1.3950.

Singapore Has One Of The Highest 10-Year Bond Yields Among Its Triple-A Peers

Singapore Is The Only Triple-A Rated Country In Asia

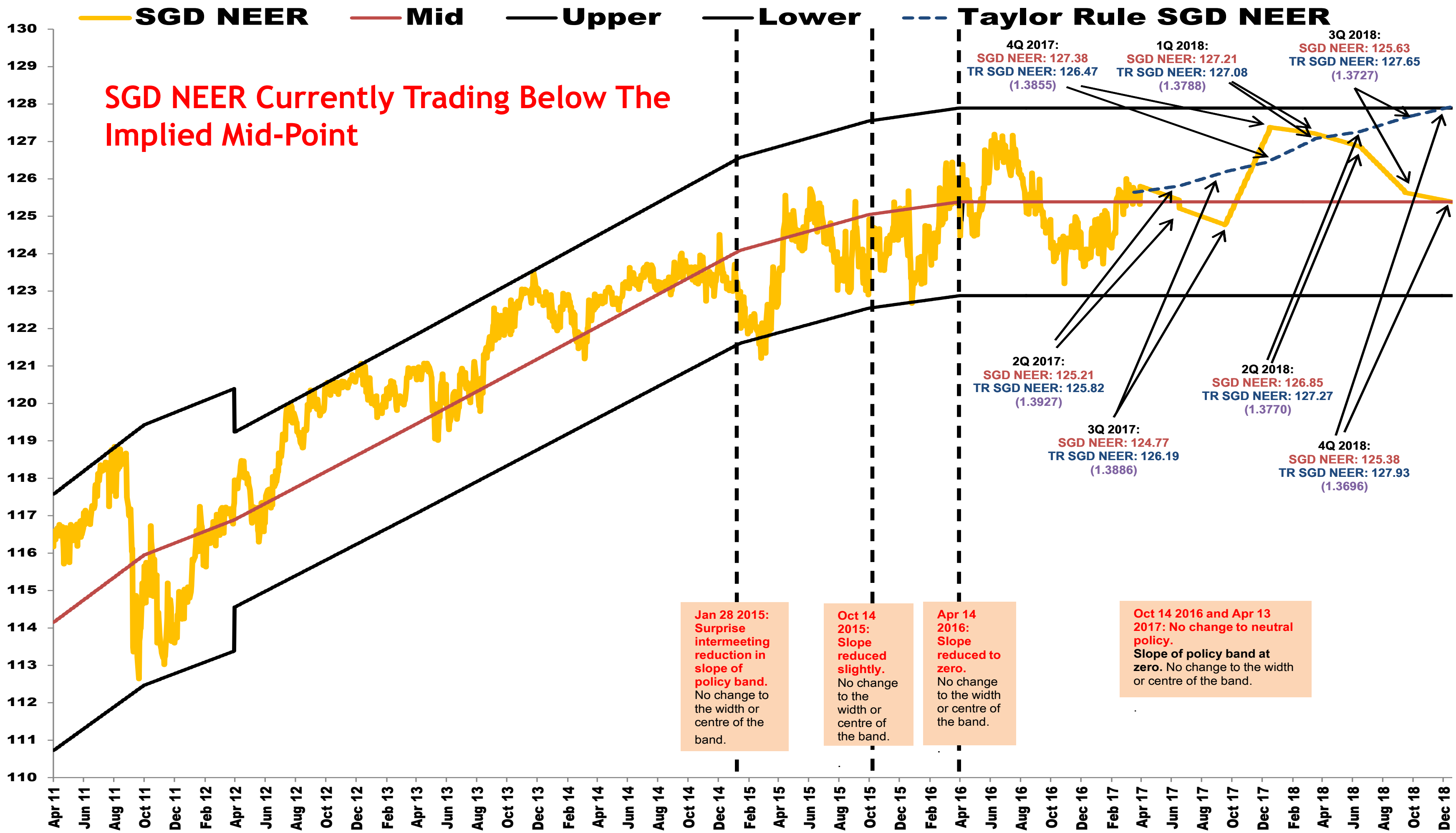


Singapore could continue to attract flows to the bond markets given its relatively high yields among its (S&P) AAA-peers and this could be supportive of the SGD

Source: Bloomberg, Maybank FX Research

Neutral Policy Could Give Way To "A Mild Appreciation" Stance In Oct

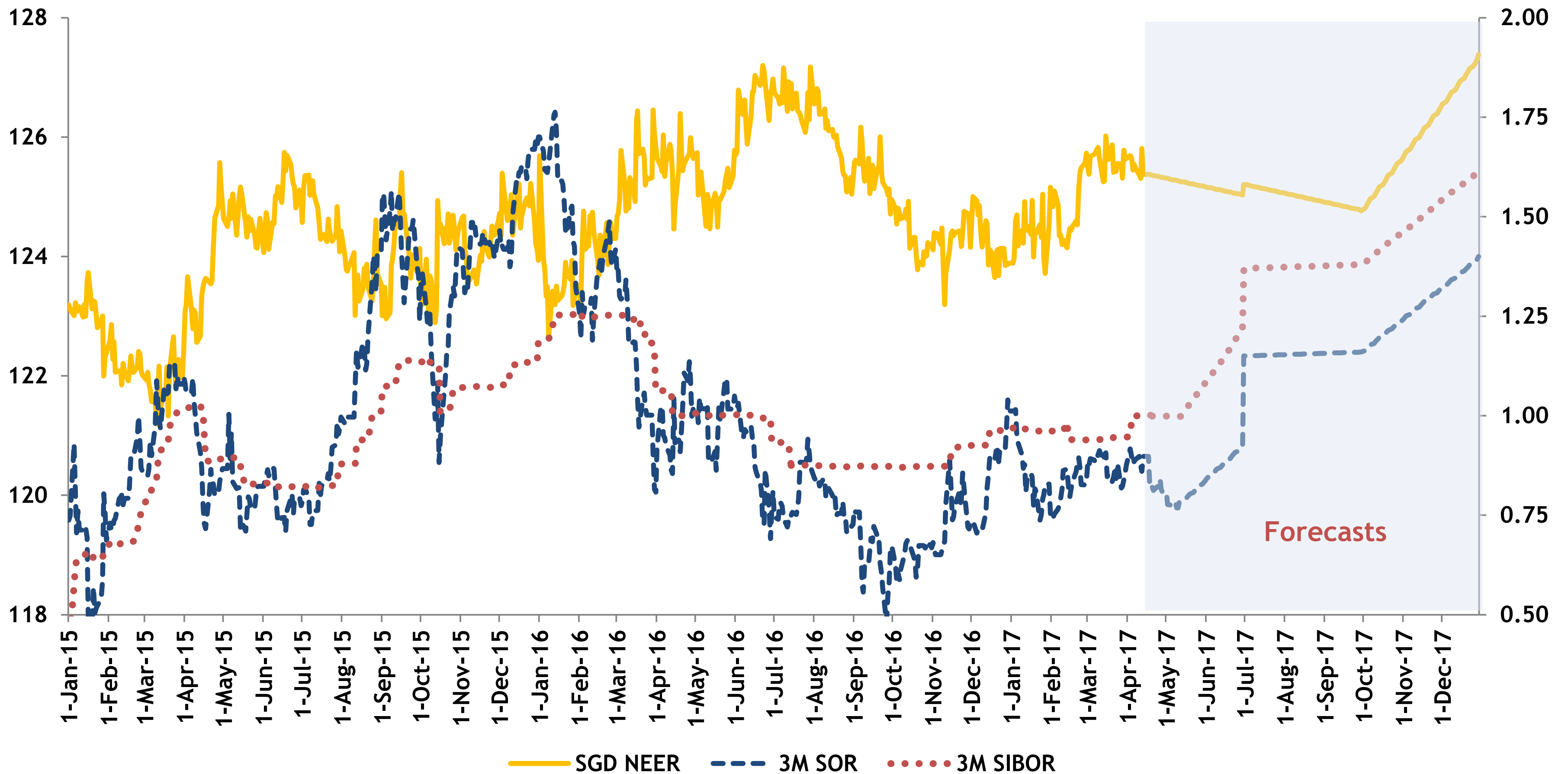
Our Taylor Rule Estimates Suggest A Shift In Policy Would Be Appropriate



Source: Bloomberg, Maybank FX Research

Expectations of SGD NEER Strength To Moderate Domestic Rates Climb

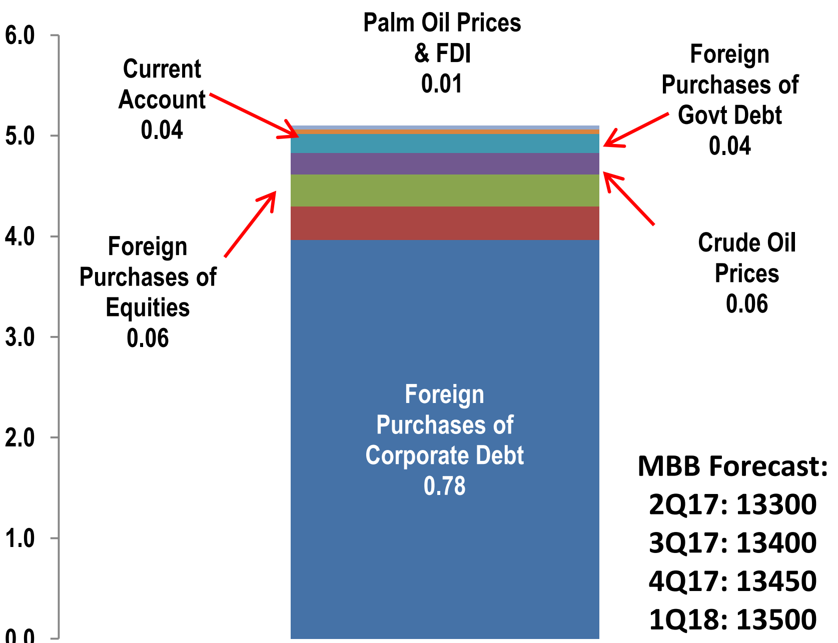
Upward Pressure On Domestic Rates Remain Given Expectation Of At Least Two More Fed Rate Hikes In 2017



Source: Bloomberg, Maybank FX Research

IDR Driven By Foreign Purchases Of Corporate Debt

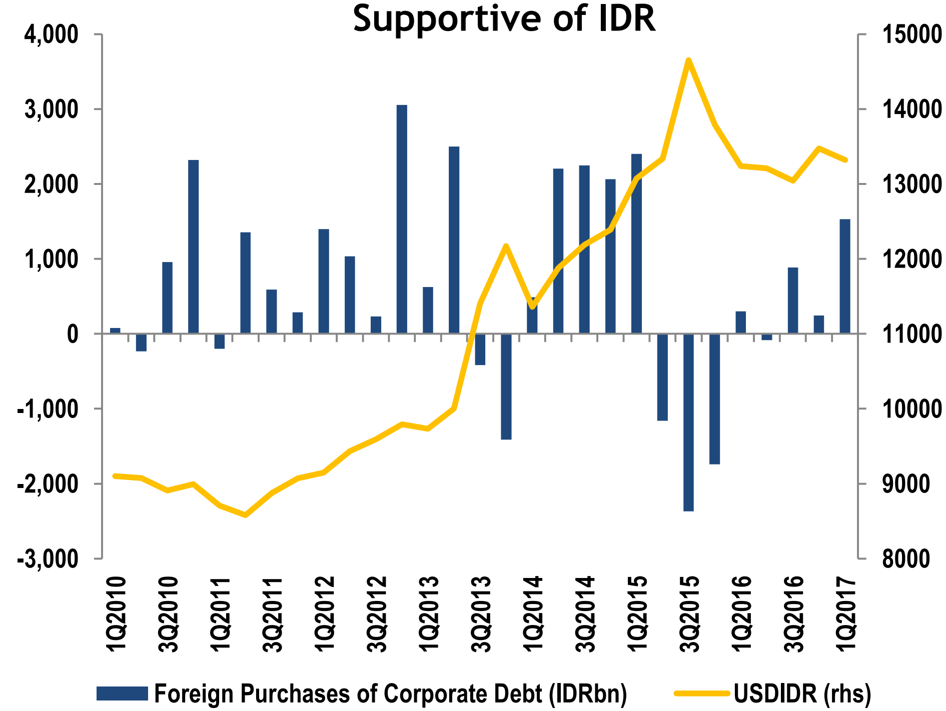
VAR Decomposition Of USDIDR Moves



MBB Forecast:
2Q17: 13300
3Q17: 13400
4Q17: 13450
1Q18: 13500
End 2018: 12000

Note: Data is from 1Q 2010 to 1Q 2017

Further Purchases By Foreign Investors Should Be Supportive of IDR

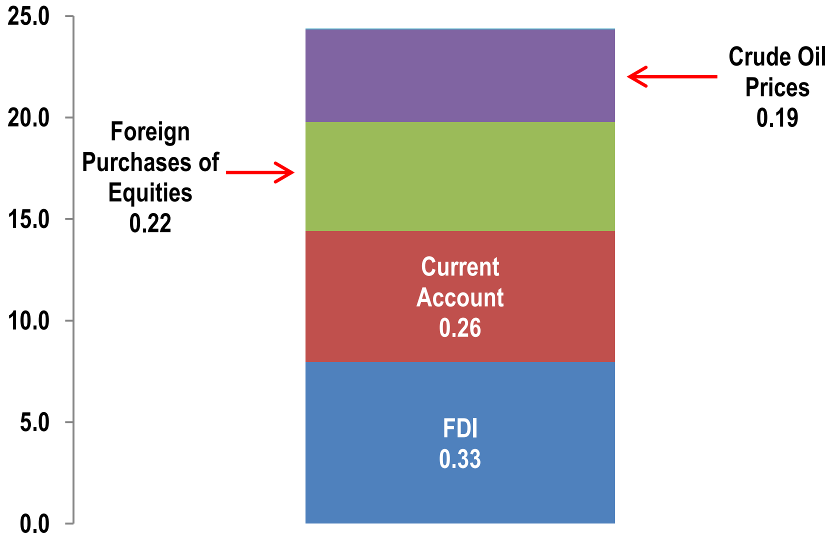


- IDR remain supported recently due to strong fund inflows, particularly to corporate debt
- Expectations of a S&P sovereign credit rating sometime in the early part of 2H 2017 is supportive of the foreign inflows into Indonesia assets
- BI has policy room to raise rates this year, which could cap IDR upside

Source: Bloomberg, CEIC, Maybank FX Research

Deterioration In Current Account To Weigh On PHP

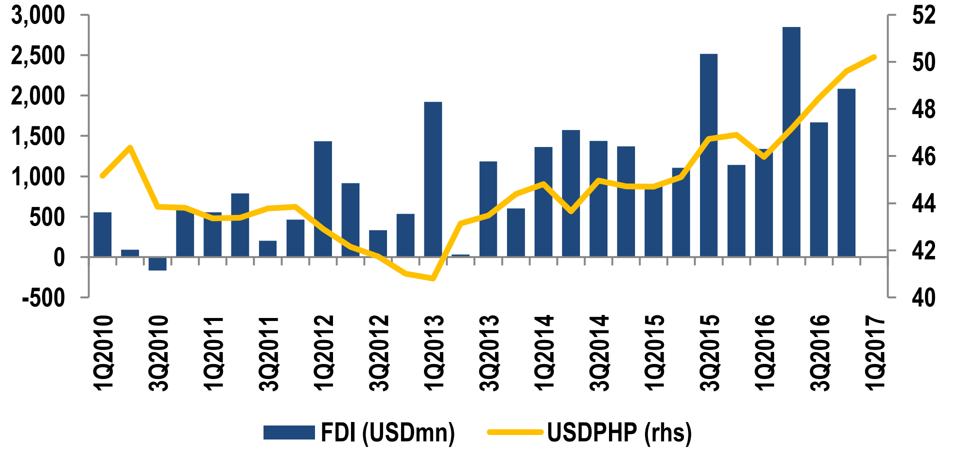
VAR Decomposition Of USDPHP Moves

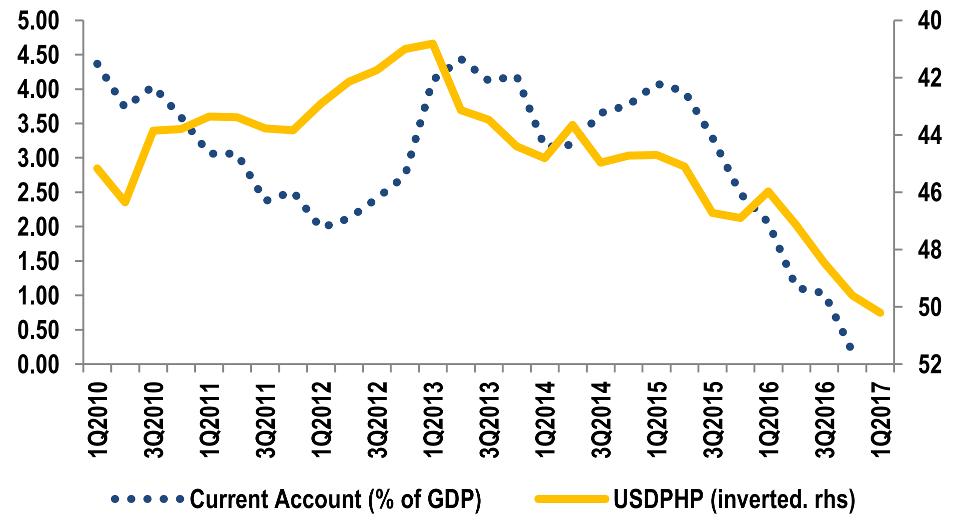


Note: Data is from 1Q 2010 to 1Q 2017

- PHP faces downside pressure from deteriorating current account surpluses
- Foreign concerns over President's overly-aggressive drug-policy and his temperament could weigh as well
- But downside to the PHP could be limited by FDI inflows, which should also be helped by ongoing planned tax reforms

Deteriorating Current Account Surplus Weighing On PHP But FDI Should Limit Downside

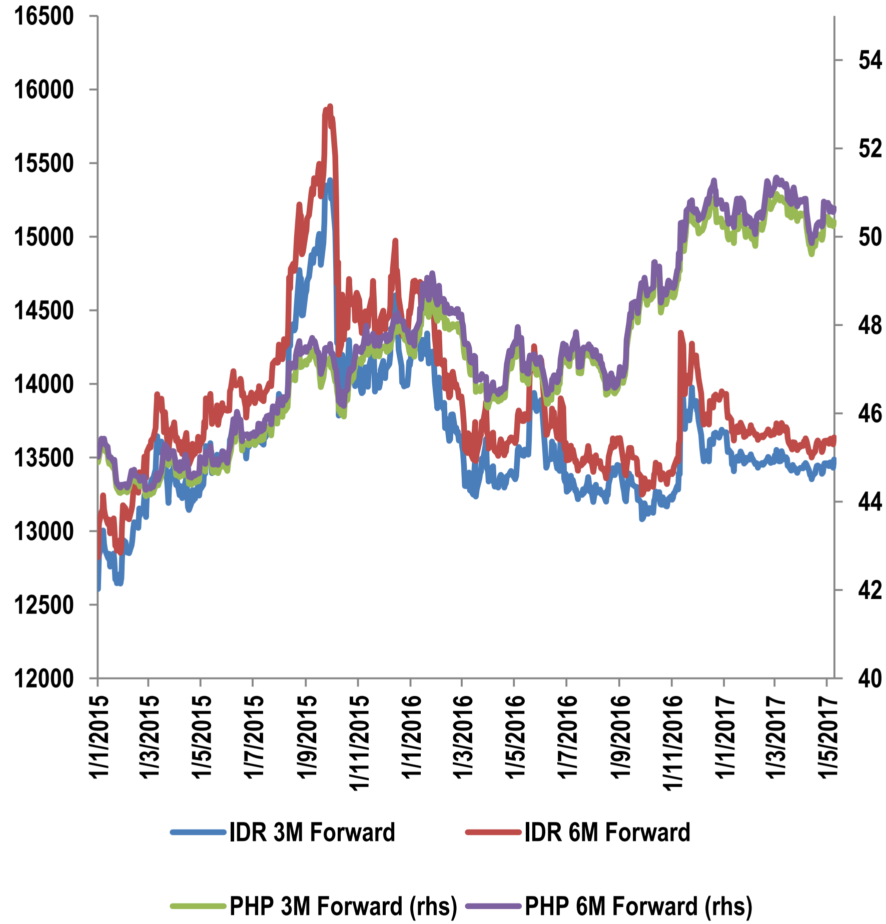




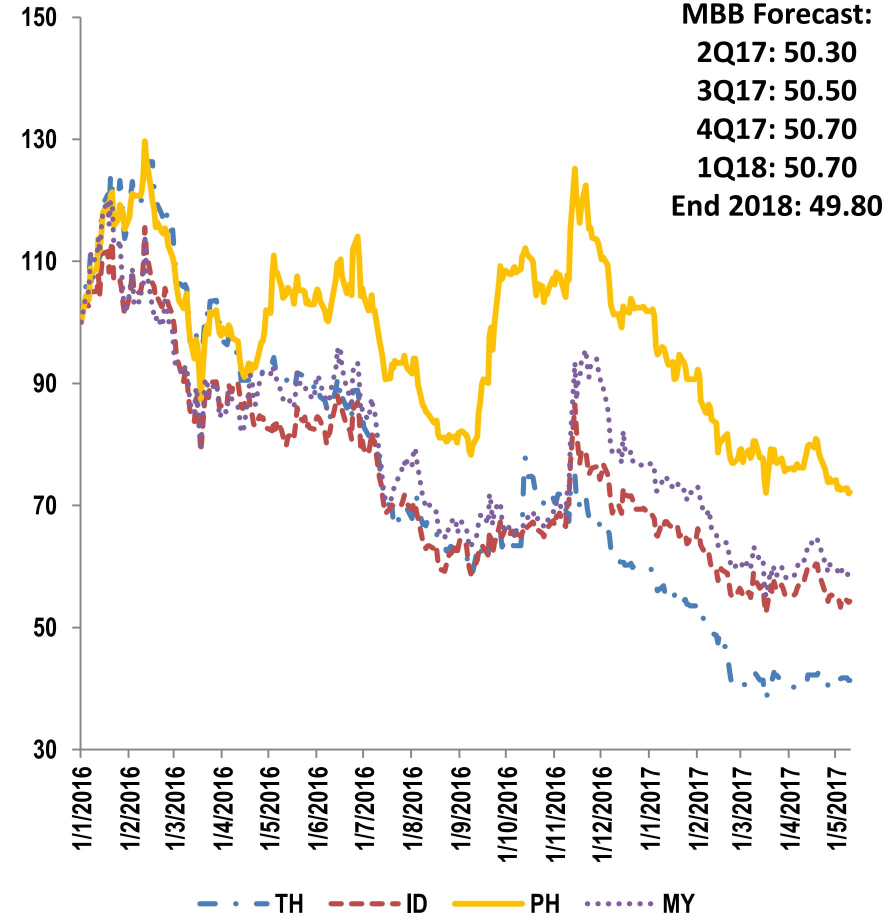
Source: Bloomberg, CEIC, Maybank FX Research

More Upside To The USDPHP Compared To Its Regional Peers

Forwards Suggest More Upside To USDPHP And Stable USDIDR



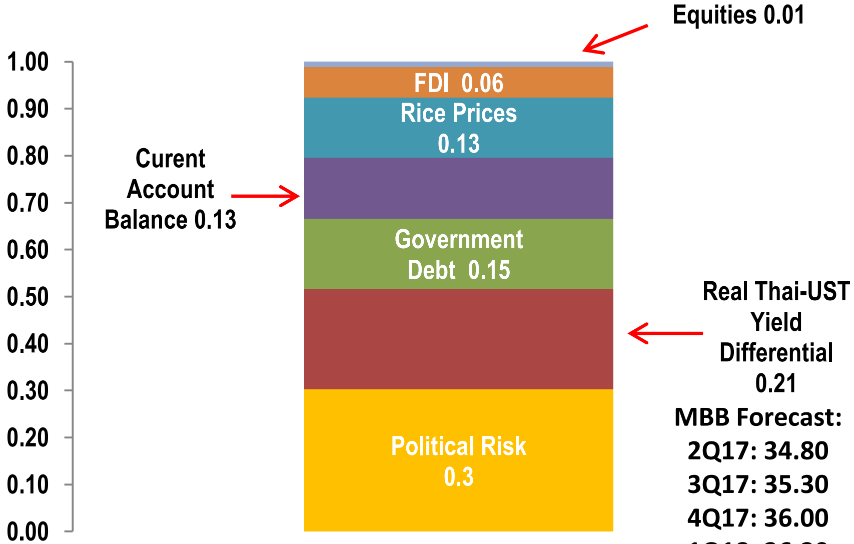
Falling But Elevated 5-Year CDS Suggests Political And Policy Uncertainty In Philippines



Source: Bloomberg, Maybank FX Research

Rise In Political Risks Could Be Supportive Of USDTHB

VAR Decomposition Of USDTHB Moves

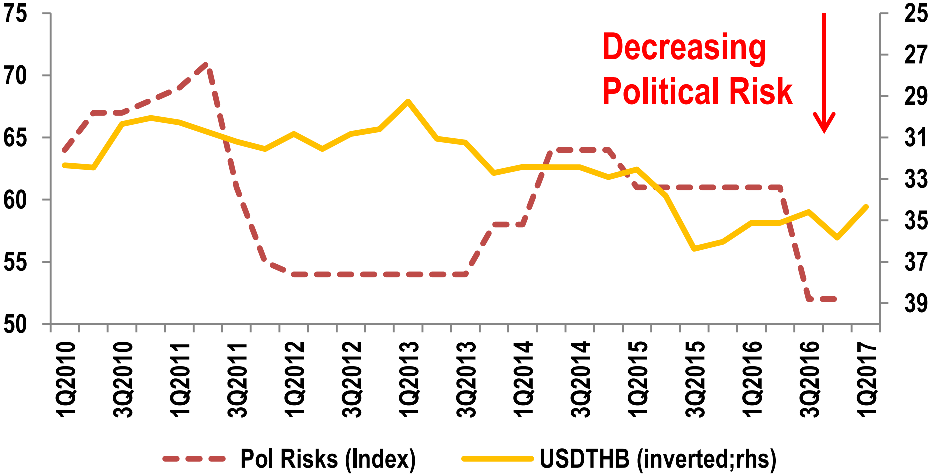


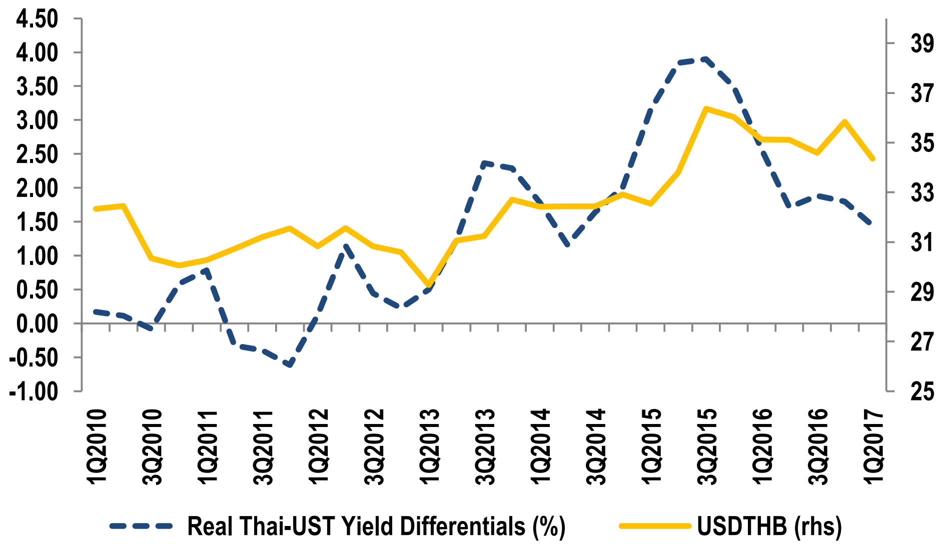
Note: Data is from 1Q 2010 to 1Q 2017

MBB Forecast:
2Q17: 34.80
3Q17: 35.30
4Q17: 36.00
1Q18: 36.20
End 2018: 36.30

- The USDTHB recent moves could be attributed to the calm in the domestic political environment as reflected in the EIU's recent low political risk score.
- Also helping is the narrowing yield differentials between Thai govt. debt and UST that should support inflows into Thai govt. debt and hence weigh on the USDTHB
- In the medium term, we expect this political calm to be disrupted in the lead-up to the general elections expected sometime in 2Q, 3Q 2018 – supportive of USDTHB move higher

Improving Political Environment And Narrowing Yield Differentials With UST Conducive For THB

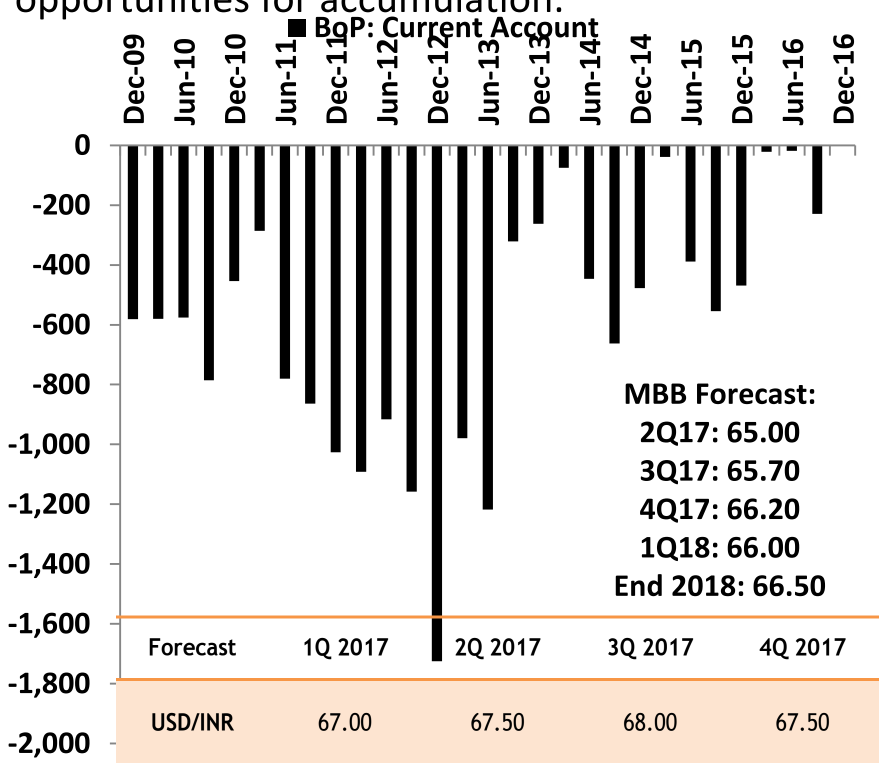




Source: EIU Political Risk Score, Bloomberg, CEIC, Maybank FX Research

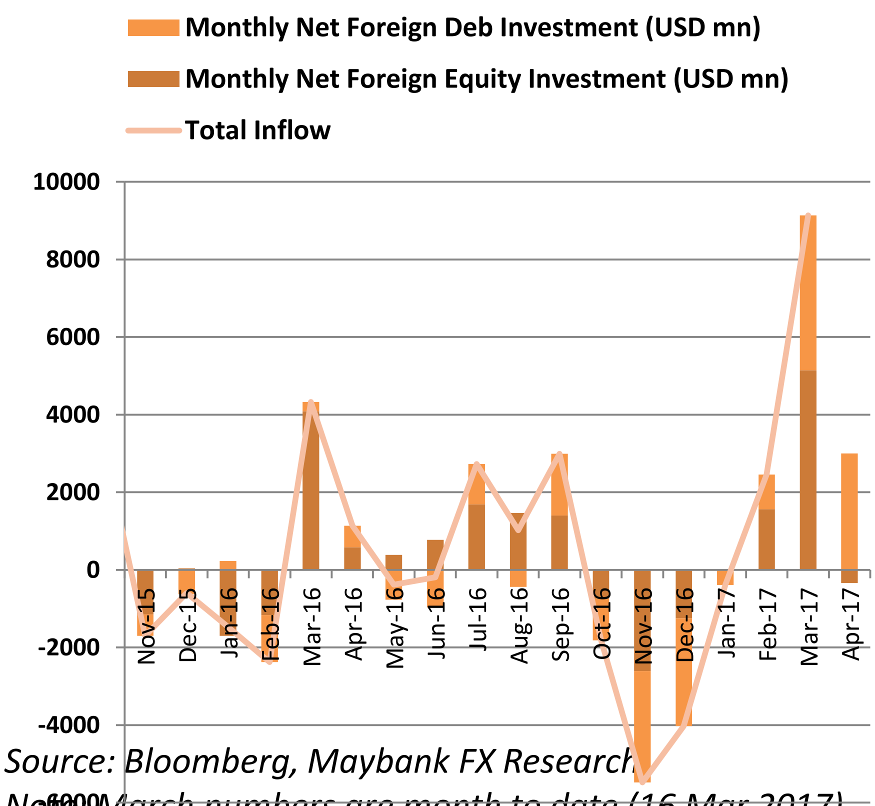
INR – Resilience, Careful Of Short-term Downsides

INR Has been Lifted By A Series of Fortunate Events including a budget that has managed to boost growth boosting measures and stick to fiscal consolidation. **Current account balance looks to be sustained.** Uttar Pradesh victory paves the way for reforms. Soft USD also provide conducive environment for carry which should favour higher-yielding INR. That said, equity has started to correct. 80% of Government Debt Limit is utilized for this quarter so bond inflows could slow and seasonality has turned against the INR for May. So short-term downside in INR could provide opportunities for accumulation.



Forecast	1Q 2017	2Q 2017	3Q 2017	4Q 2017
USD/INR	67.00	67.50	68.00	67.50

Source: CEIC, Maybank FX Research



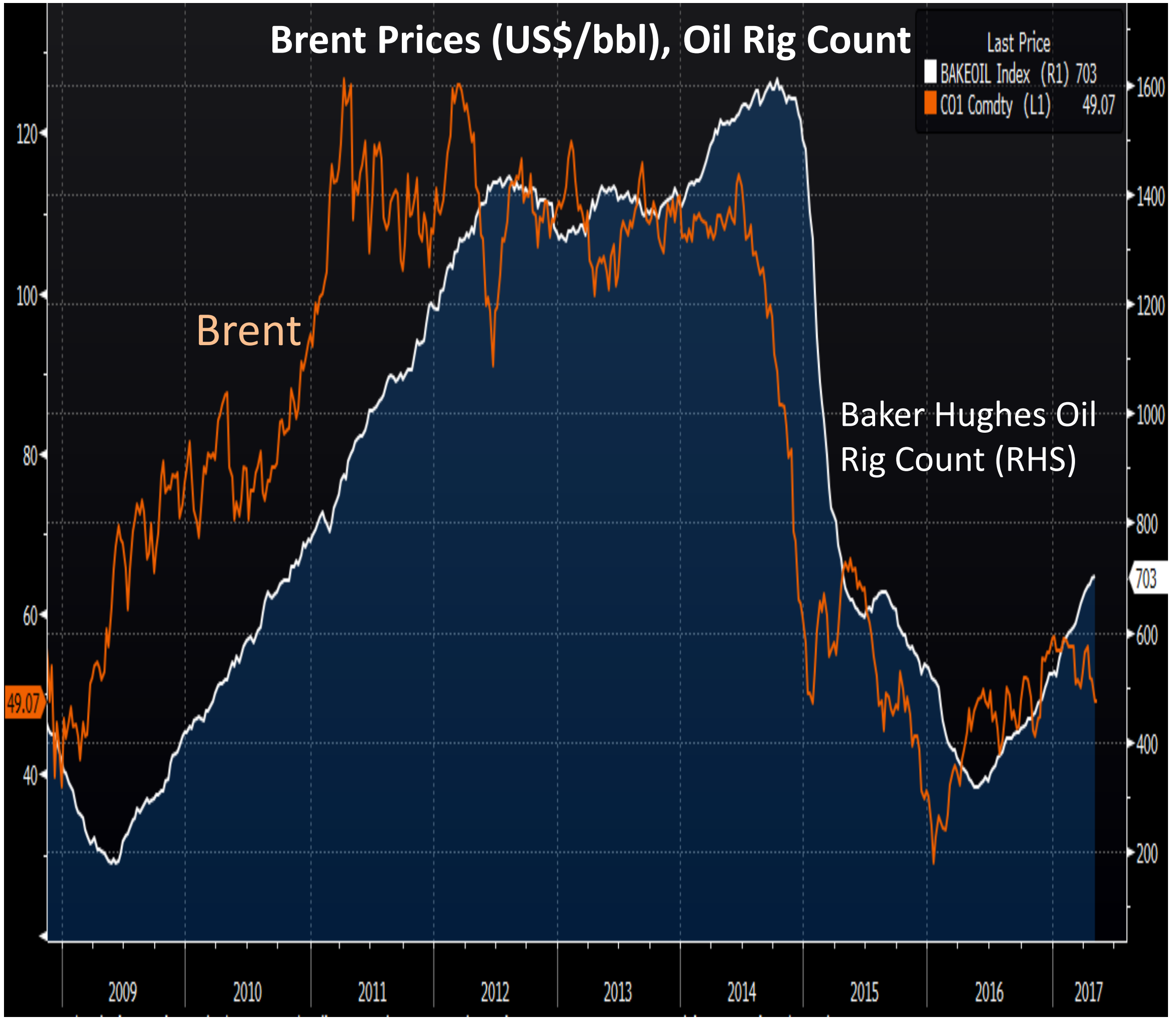
Source: Bloomberg, Maybank FX Research

Note: March numbers are month to date (16 Mar 2017)

Key Macro Questions for 2017

Commodities – Will The Tumble Continue?

Relative Oil Price Stability as Oil Demand-Supply Undergoes Rebalancing



Source: Bloomberg, Maybank FX Research

Oil Minister Khalid Al-Falih said [8 May 2017] that the group will likely maintain cuts this year and possibly into 2018.

This was backed up Russia, with its Oil Ministry saying it was ready to support extend the oil deal beyond 2017.

Bloomberg also reported that OPEC countries have also discussed the possibility of deepening their output cuts, although no consensus has been reached yet.

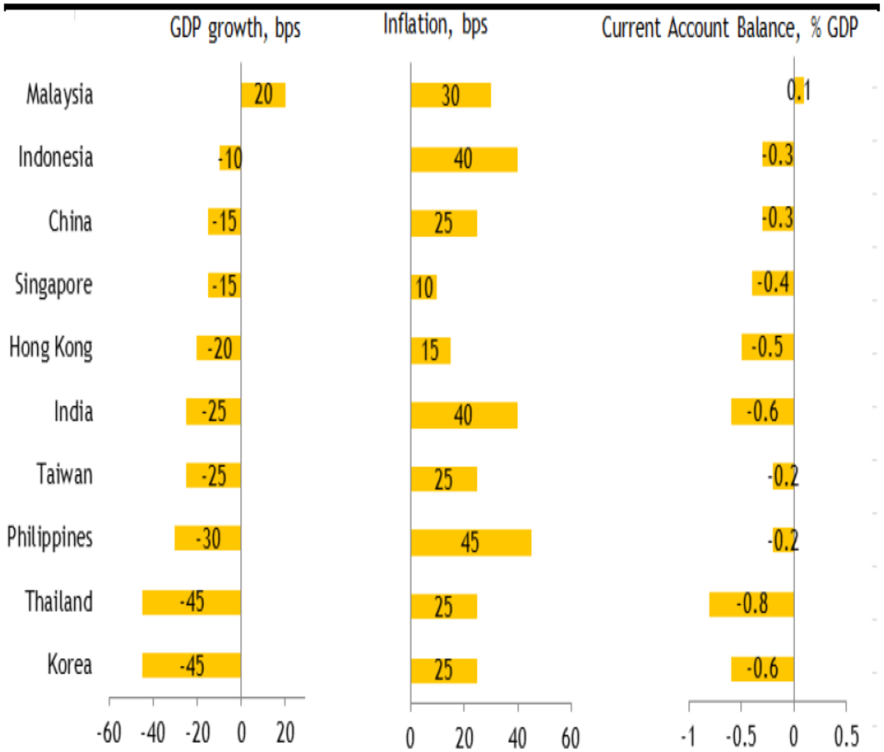
The data was also positive, with China Customs reporting April imports of crude oil were up 5.6% y/y to 32.6mt.

OPEC meeting on 25 May - Watch for oil cut extension announcement -> Support for Oil Prices

Oil Price has Varying Impact on Asian Currencies, Albeit All Positive

Apart from its obvious impact on economic fundamentals…

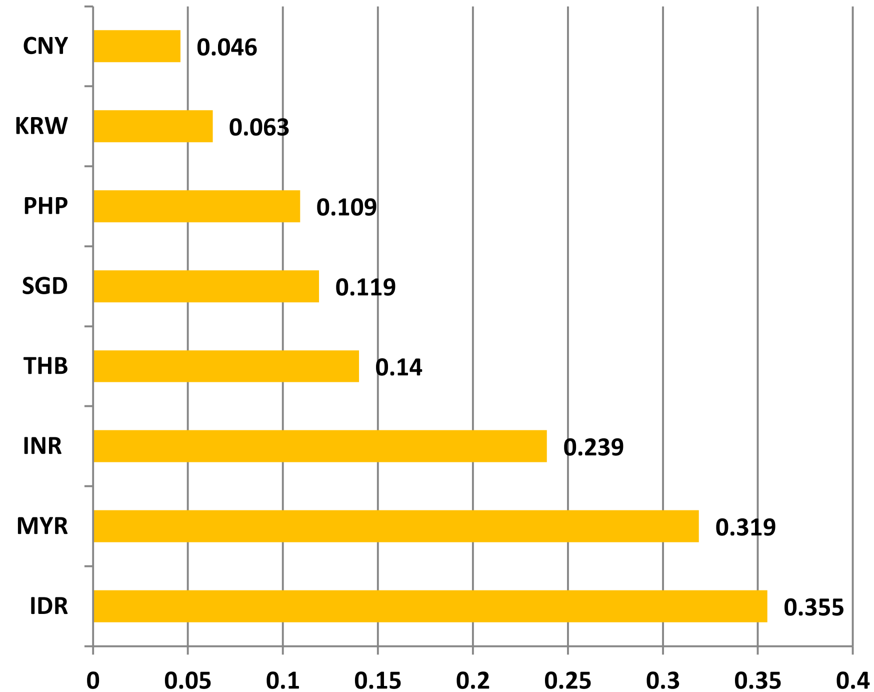
Impact of 10% Rise in Oil Prices on GDP, Inflation & Current Account



Source: Maybank Kim Eng estimates

We also have to keep in mind the oil prices were a proxy of risk sentiments. Impact on FX differs slightly.

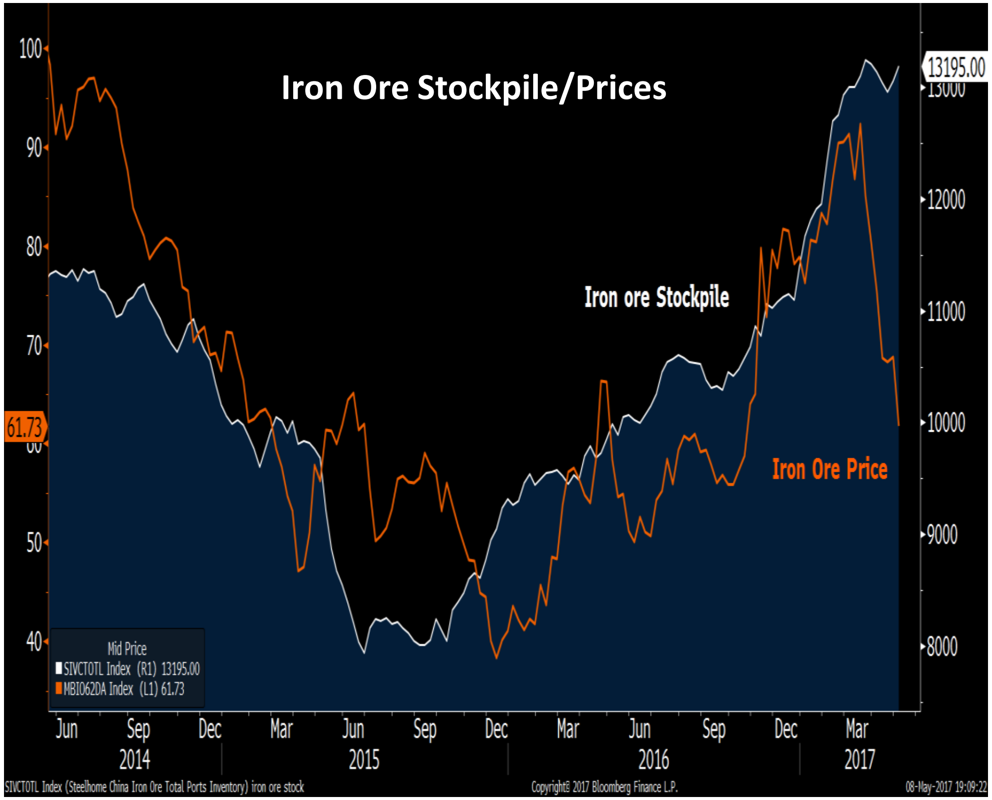
% Change in Currency Against the USD with 1% increase in Brent



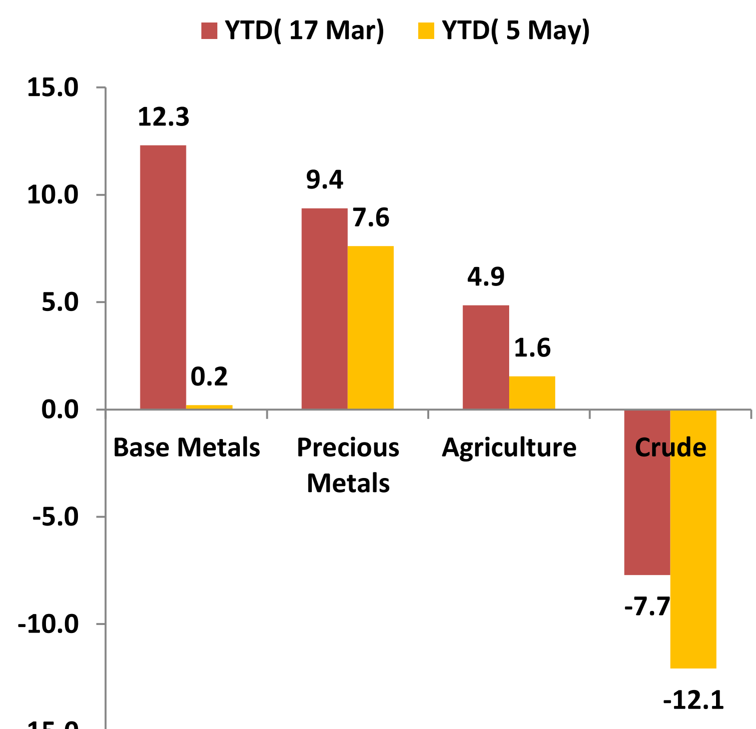
Source: Bloomberg, Maybank FX Research
Note: Sample period is 2010-2017.

Iron Ore Prices Corrected, But We Are Not Looking For A Collapse…

As iron ore stockpiles plateau, iron ore prices also saw sharp correction since Mar, dragging the AUD lower…



Base Metals Have Given Up All Gains Since Mar. Crude Prices Have Fallen Lower.



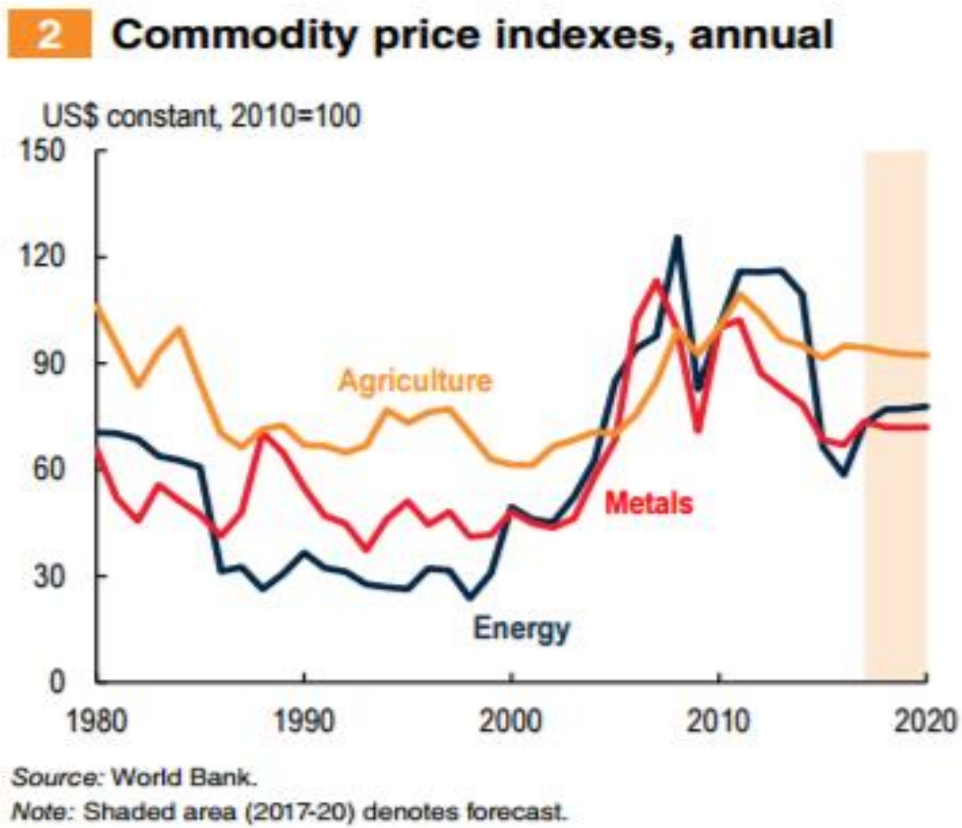
Source: Bloomberg, Maybank FX Research

"Overall, the reflationary conditions that dominated global commodity markets in 2016 **may be reaching their limits,** though positive sentiment and further steel and coal capacity cuts in China may provide further support."

Rio Tinto 2016 Strategic Report

But Prices Tend to Overshoot, Should Stabilize in Time…

According to the quarterly report by World Bank (dated Apr 2017), metal prices are forecast to *rise 16%* in 2017 on strong demand and tightening markets.



Hence, even as metal prices have corrected sharply recently, we do not expect prices to continue to tumble.

Take note that prices tend to overshoot and with prices already corrected sharply, we might not see a lot more declines.

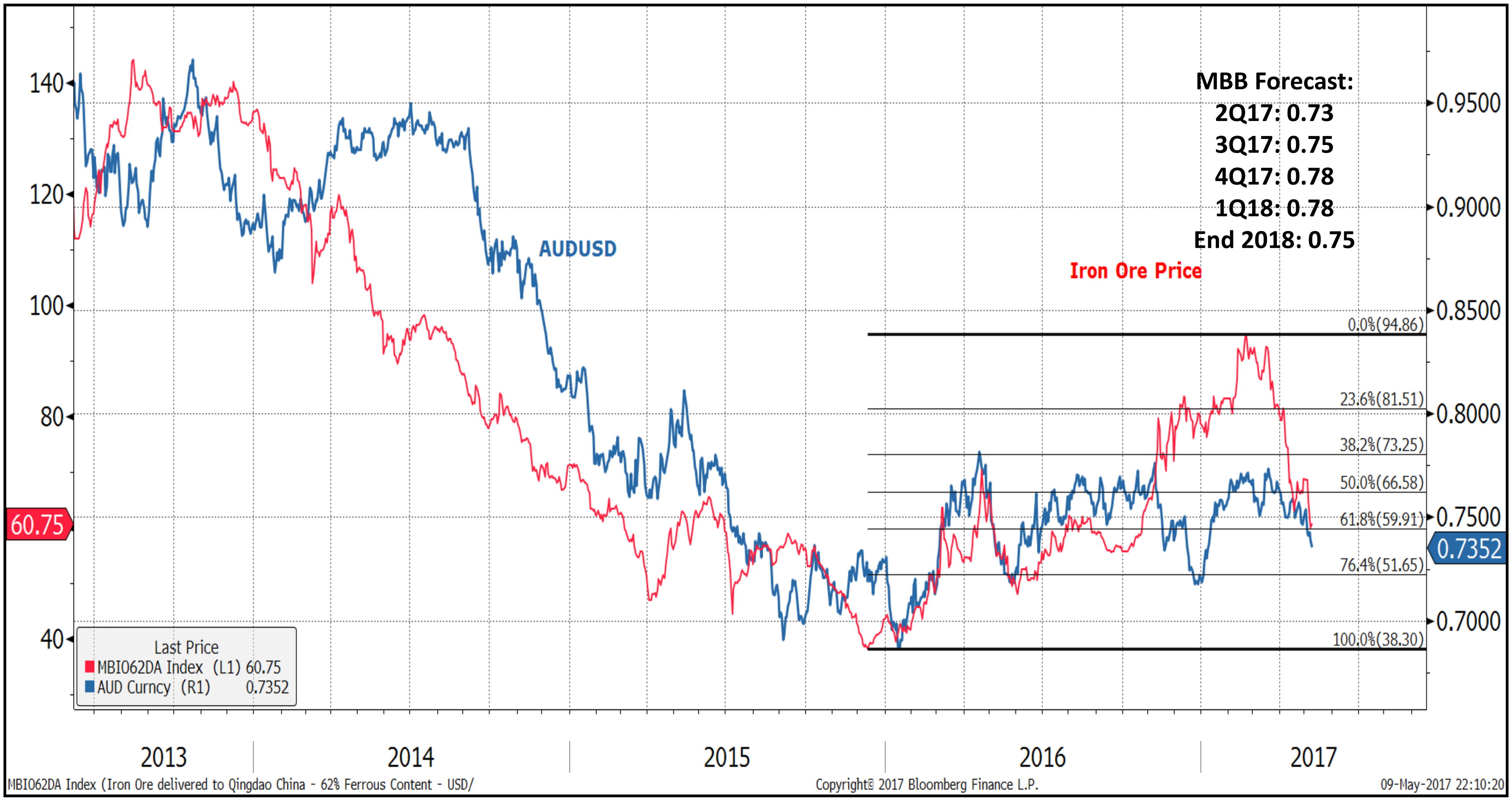
The World Bank continues to see <u>**upside risks**</u> from stronger global demand, slower ramp-up of new capacity, tighter environmental constraints and policy action that limits exports.

<u>**Downside risks**</u> include slower demand from China, and higher than expected production.

Source: Commodity Markets Outlook by World Bank (April 2017)

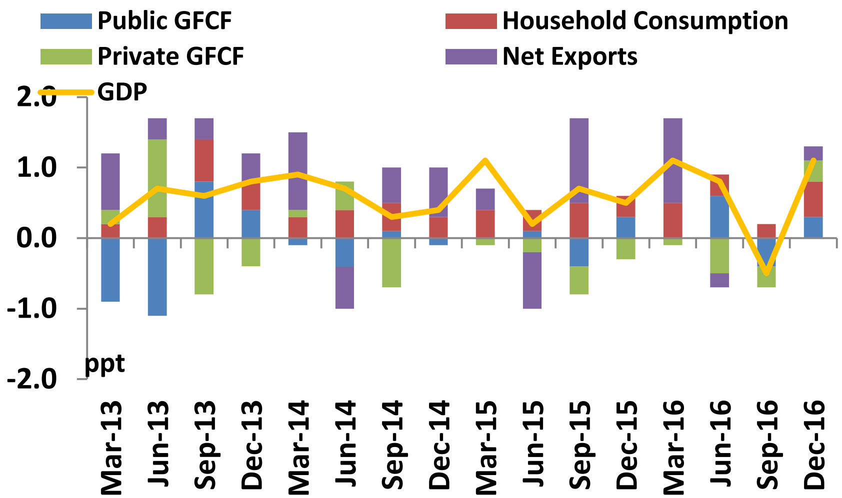
AUD - Eventual Stabilization in Metal Prices To Form Base for AUD

With RBA and other data points unlikely to give clear cues for the AUD, the currency is all the more dictated by commodity swings. We see a potential bottom around 0.73/0.72 (against the USD) before range bound trades within the 0.72-0.78.

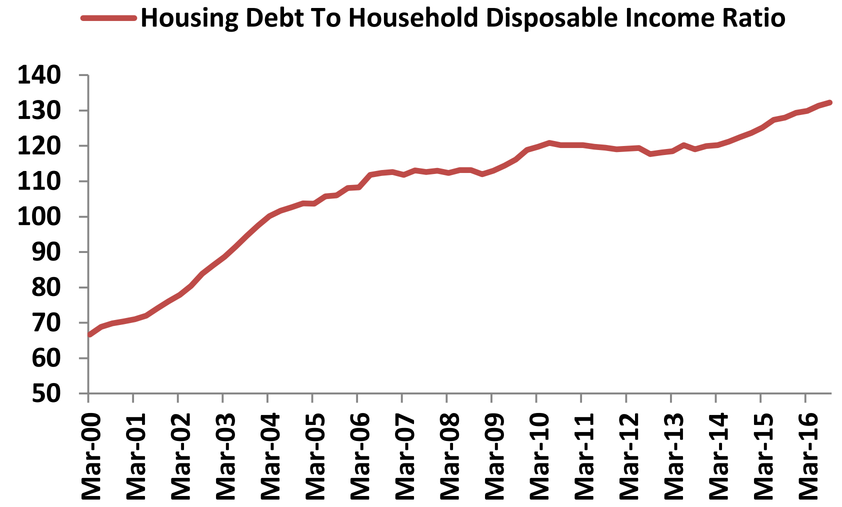


AUD - RBA Unlikely To Move This Year, Leaving AUD more susceptible to Metal Swings

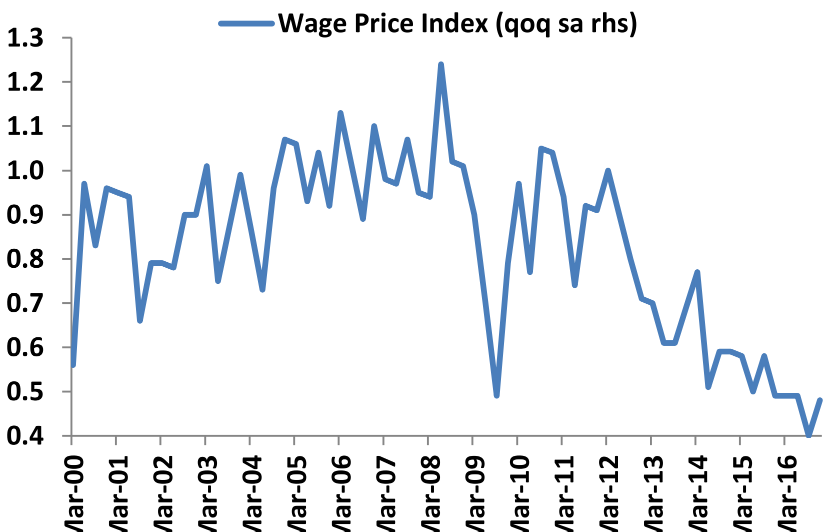
Household consumption Has Been A Key Driver of Growth



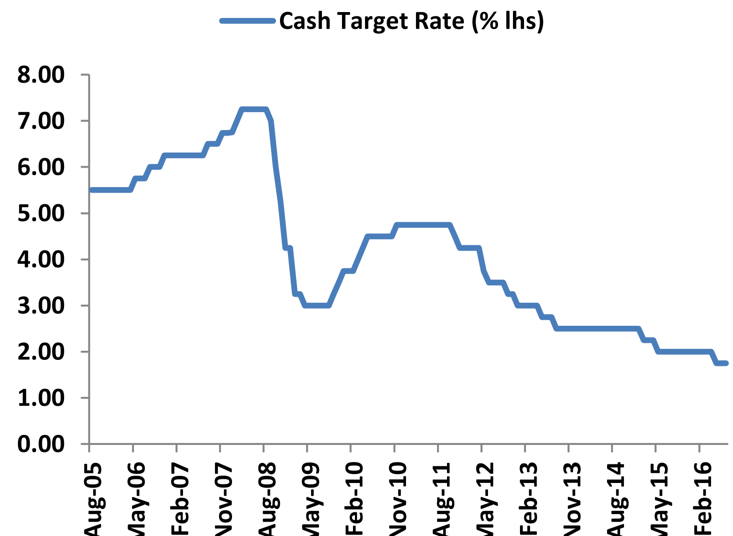
Household Debt Has Been Rising



However, Wage Growth Has Been Anemic



RBA Is Likely To Leave Rates At 1.50%



Our House View on FX Outlook

3*P*s and 1M

Big picture:

*P*rice Pressure, *P*olicy Normalization, Receding *P*olitical Risks
Plus The *M*ulti-Dimensional ASIA

- We continue to see rising ***Price pressure*** once the reflation theme resumes. Potential recovery of base metal prices and crude could nudge price pressures around the world higher.

- ***Policy Normalization*** Has Gained Momentum in the US as the Fed started hiking earlier this year (as opposed to Dec in 2015,2016) and there are already talks of balance sheet reduction.

- We started the year with ***Political risks*** aplenty but the French elections have turned out favorably for the EU, polls for German elections seem to approve Merkel. While there is still the legislative election for France in June and other key political events such as Thailand's General Election in mid-2018, China's National Congress, Malaysia's General Election to look forward to, political risks have somewhat receded to some extent and that has brought down volatility (VIX) to year lows, equities to record highs.

- Asian currencies are likely to move at different speed with idiosyncratic drivers likely to create a ***Multi-Dimensional Asia***: In Japan, the ultra-loose monetary policy will keep the USDJPY elevated beyond current levels, while in ASEAN, political risks in Thailand; deteriorating current account surplus in Philippines; expectations of a S&P sovereign credit rating upgrade in Indonesia; and stable oil prices and recent moves by the BNM in Malaysia.

Strategic Trade Ideas

- Buy EURJPY on receding political risks and to position for eventual monetary policy divergence

- Buy USDSGD, USDJPY on sensitivity to UST yields rising
  - Buy on dips towards 1.39, targeting a move towards 1.4200
  - Buy on dips towards 111, targeting a move towards 116 and then 118

- Favor long INR and THB against short JPY (Asian Central Bank RV Plays)

- Short PHPINR on diverging current account balances

- Long MYR (against SGD, JPY, THB, PHP) as MYR plays catch up relative to peers, fundamental valuation

The House View – G7 + China

- **USD** – Remains Supported on Dips; Expect fiscal (tax reforms, infra spending) and monetary policy normalization (rates and balance sheet) to lead to further USD upside

- **GBP -** A Buy-on-Dips in Medium Term towards 1.35-1.40; But Upside on GE already priced in while *Brexit* uncertainty remains -> Bias to Sell on Rally towards 1.3050 for 1.28, 1.2650 objective

- **EUR -** Receding political concerns (Netherlands, French elections over) and ECB not adding to QE to keep EUR supported on dips; Play 1.05 – 1.12 Range. French Legislative elections (11 & 18 Jun) still a downside risk for EUR

- **AUD** – Short-term Correction In Play. Bottom Seen Around 0.72/0.73. Bias to Buy on Dips towards 0.73 for first target of 0.76.

- **NZD** – Weighed by dairy prices but yield differentials to mitigate weakness; 0.68 – 0.72 range

- **JPY** – To Weaken Towards 120 (vs. USD) on continue policy easing and sensitivity to rising UST yields. Bias to buy on dips.

- **CNH** – Weaker vs. USD (7.05). Stronger Against Regional Peers and Non-USD Majors

The House View – ASEAN FX

- **SGD -** Downside Risks vs. the USD (1.4200), vs. MYR (2.99-3.12). USDSGD support at 1.3950.
- **MYR** – Positive Outlook on recent BNM initiatives; potential election end-2017 may lead to further demand for MYR assets. Expect 4.30 – 4.40 to hold for 2017
- **IDR -** Short term vulnerability towards 13450 but strong fundamentals to provide support on dips, especially a potential upgrade to investment grade by S&P.
- **PHP -** Near-term pressure to the downside due to Duterte Risk premium and deteriorating current account balances sours prospects for PHP assets in the near term. Could see PHP heading towards 50.70 (vs. the USD) towards the end of the year.
- **THB -** In the backdrop of more Fed rate hike this year, should see gradual weakening towards the end of the year to 36.00 (against USD) as tension rises in the run up to the general election in 2018.

The House View – SGD Crosses

- **EURSGD** – Bias to Buy on Dips below 1.50. Resistance at 1.52-1.54 levels
- **GBPSGD** – Expected to trade wide range of 1.78 – 1.84; Bias to Buy on Dips
- **AUDSGD** – Correction has Played Out. Support is seen around 1.0293 and we see rebound risks towards 1.0881.
- **JPYSGD -** Downside Risk towards 1.22
- **SGDCNY** – Peaked around 5.05 from around the 4.94 levels

The House View – MYR Crosses

- **SGDMYR - Maintain Bearish Bias; Potential To Test 3-Levels in 3Q 2017**
- **EURMYR – To Hold Steady in 4.55 – 4.79 Range**
- **GBPMYR - Supported on Dips towards 5.36; But Upside Likely to Stay Cap around 5.70**
- **AUDMYR - Having reversed sharply, we caution rebound risks in this pair towards 3.20 at first and then perhaps 3.39**
- **JPYMYR - Bearish Bias; Expect Further Downside towards 3.70 Levels.**
- **MYRCNY – This cross might head higher to peak around 1.65 before the next support around 1.62.**

2017/2018 Forecast

	End Q2-17	End 3Q-17	End 4Q-17	End 1Q -18	End 4Q-18
USD/JPY	116	118	120	120	122
EUR/USD	1.08	1.07	1.08	1.10	1.12
GBP/USD	1.30	1.26	1.28	1.30	1.32
AUD/USD	0.73	0.75	0.78	0.78	0.75
NZD/USD	0.71	0.73	0.75	0.77	0.75
USD/SGD	1.4100	1.4200	1.3950	1.3950	1.3950
USD/MYR	4.30	4.25	4.30	4.35	4.20
USD/IDR	13300	13400	13450	13500	12000
USD/THB	34.80	35.30	36.00	36.20	36.30
USD/PHP	50.30	50.50	50.70	50.70	49.80
USD/CNY	6.95	7.01	7.04	7.04	6.90
USD/HKD	7.80	7.80	7.80	7.80	7.80
USD/TWD	30.80	31.50	32.00	32.00	32.00
USD/KRW	1140	1150	1160	1170	1140
USD/INR	65.00	65.70	66.20	66.00	66.50
USDVND	22900	23100	23300	23400	23000
USD DXY Index	100	101	101	99	98
SGD Crosses	**End Q2-17**	**End 3Q-17**	**End 4Q-17**	**End 1Q -18**	**End 4Q-18**
100 JPY/SGD	1.216	1.203	1.163	1.163	1.143
EUR/SGD	1.523	1.519	1.507	1.535	1.562
GBP/SGD	1.833	1.789	1.786	1.814	1.841
AUD/SGD	1.029	1.065	1.088	1.088	1.046
NZD/SGD	1.001	1.037	1.046	1.074	1.046
SGD/MYR	3.050	2.993	3.082	3.118	3.011
SGD/IDR	9433	9437	9642	9677	8602
SGD/THB	24.68	24.86	25.81	25.95	26.02
SGD/PHP	35.67	35.56	36.34	36.34	35.70
SGD/CNY	4.929	4.937	5.047	5.047	4.946
SGD/HKD	5.532	5.493	5.591	5.591	5.591
SGD/TWD	21.84	22.18	22.94	22.94	22.94
SGD/KRW	808.51	809.86	831.54	838.71	817.20
SGD/INR	46.10	46.27	47.46	47.31	47.67

2017/2018 Forecast

	End 2Q -17	End 3Q -17	End 4Q -17	End 1Q-18	End 4Q -18
USD/JPY	116	118	120	120	120
EUR/USD	1.08	1.07	1.08	1.10	1.08
GBP/USD	1.30	1.26	1.28	1.30	1.30
AUD/USD	0.73	0.75	0.78	0.78	0.76
NZD/USD	0.71	0.73	0.75	0.77	0.76
USD/SGD	1.41	1.42	1.40	1.40	1.40
USD/MYR	4.30	4.25	4.30	4.35	4.35
USD/IDR	13300	13400	13450	13500	13350
USD/THB	34.80	35.30	36.00	36.20	36.50
USD/PHP	50.30	50.50	50.70	50.70	50.30
USD/CNY	6.95	7.01	7.04	7.04	7.00
USD/HKD	7.80	7.80	7.80	7.80	7.80
USD/TWD	30.80	31.50	32.00	32.00	32.00
USD/KRW	1140	1150	1160	1170	1180
USD/INR	65.00	65.70	66.20	66.00	66.00
USDVND	22900	23100	23300	23400	23400
MYR Crosses	End 2Q -17	End 3Q -17	End 4Q -17	End 1Q-18	End 4Q -18
EUR/MYR	4.644	4.548	4.644	4.785	4.698
JPY/MYR	3.707	3.602	3.583	3.625	3.625
MYR/HKD	1.814	1.835	1.814	1.793	1.793
MYR/CNY	1.616	1.649	1.637	1.618	1.609
GBP/MYR	5.590	5.355	5.504	5.655	5.655
AUD/MYR	3.139	3.188	3.354	3.393	3.306
NZD/MYR	3.053	3.103	3.225	3.350	3.306
MYR/IDR	3093	3153	3128	3103	3069
MYR/INR	15.12	15.46	15.40	15.17	15.17
MYR/KRW	265.12	270.59	269.77	268.97	271.26
MYR/PHP	11.70	11.88	11.79	11.66	11.56
SGD/MYR	3.05	2.99	3.08	3.12	3.11

APPENDIX I:
TERMS FOR PROVISION OF REPORT, DISCLAIMERS AND DISCLOSURES

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