Maybank

Macro | FX Research & Strategy

Global

FX Monthly

2023, Issue 8: Still Facing China and US Headwinds

What Has Changed This Month?

- We adjusted our forecast for the USD higher against most G10 and Asian currencies as the surprising resilience of the US economy boosted the USD and UST yields.

Our Strategies and Views

- The Jackson Hole Economic Symposium came and went without significant policy guidance from the central bankers present at the event (ECB/Fed/BoE/BoJ). Fed Powell's emphasis on "uncertainty and risk management" in his keynote speech suggests that the hurdle to hike further may be higher now and that could be the case for most central banks (apart from BoJ/PBoC/SBV). More caution is warranted as major central banks are confronted with increasing risks to growth and sticky core inflation. The recent downside surprise in US data had dampened the high-for-longer trades but the US economy's comparative resilience vs. the Eurozone, UK, China could still keep the USD supported on dips.

- China announced a number of growth and market supports towards the end of Aug from halving levies for equity trading to allowing local governments to ease criterion for more to become first-time home buyers. Major banks were reportedly ordered by the authorities to cut interest rates for existing mortgages as well as deposit rates. Local governments are also ramping up special bond issuance/utilization to invest in infrastructure. Given the consumer/business confidence deficit in the country, hope for recovery in 4Q could be premature but any signs of stabilization in consumption/credit growth could provide better anchor for the RMB and the rest of AxJ.

- We like to flag the risks of AUD and NZD coming under pressure in the remaining months of 2023 should RBA and RBNZ turn out to be the first few central banks to kick off their easing cycle ahead of the Fed. That is a scenario that is not priced yet for the next six months and we prefer to short the antipodes on rally.

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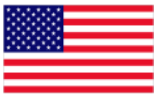
Top 3 Currency Plays for Sep

Sell AUD, NZD on Rally
Buy EURCNH
Sell the USDJPY, SGDJPY

Key Events for the Month Ahead

Date	Event
1 Sep	Singapore Presidential Election
Sep 2023	Finalization of Thailand Budget

G7 Global Overview



USD: Still in "Data Dependent" Phase

Forecast	3Q 2023	4Q 2023	1Q 2024	2Q 2024
USD Index	103.63 (102.65)	102.89 (101.94)	102.14 (100.30)	100.50 (98.61)

Previous Forecasts in Parentheses

- **Motivation for the FX View:** The DXY index saw another swing back up again in Aug on the back of resilient US data. The USD DXY rose around 1% in Aug largely due to stronger US data in Aug which mitigated expectations just a month ago that the Fed will see a pause following a PCE coming in lower than expected and a softer NFP. UST 10 year yields also rose to around 4.13% by end Aug from around 3.92% on 1 Aug. Any indication from data releases of a likely slower quarterly growth pace, would also significantly raise the likelihood that a 4Q move would be much harder. There is some likelihood that there could be some further signs of cooling in inflation by then, reducing the probability the Fed would undertake a second hike. Our economists are still expecting no more hikes. But we do note that the view could change as the current turning point risk environment would highly depend on inflation (and growth) outcomes. The "high" or "higher for longer" driver for US policy rates remains a significant driver of UST yields and US dollar in Aug and into most of Sep in our view unless US data sees dramatic moves downwards.

- In late Aug, the U.S. job openings and labor turnover survey (JOLTS), fell to the lowest level since early 2021, suggesting a cooling in labor demand, while the U.S. Conference Board's measure of consumer confidence points to an easing in consumer spending. The JOLTS data "cast further doubt on the idea that the Fed will need to keep rates high for longer. Nonetheless, the question of what the Fed will do next will continue to hang over the market in Sep after Fed Chair Powell said at Jackson Hole that inflation remains too high and that officials are open to raising rates further if needed.

- Our DXY forecasts moved higher because of our downward revisions to the euro and JPY given the pricing-in of the unlikely policy tightening shift out of BOJ in end 2023 and early 2024. We also expect USD to remain supported in 3Q as its carry vis-a-vis other currencies still remains with some softness in the tail end of 4Q as the markets price in some indications of growth easing and cooling of inflation then.

- **Growth and Inflation Outlook:** 2Q (S) US real GDP was actually softer at 2.1% QoQ (prior. 2.4% QoQ). Services still grew at a reasonable pace of 2.4% QoQ although goods expanded at a tepid pace of 0.7% QoQ. With excess savings dwindling and student debt repayments resuming in October, we expect consumer spending to cool even further in the months ahead. Non-residential fixed investment grew a robust 7.7%, driven by strong growth in structures and equipment, contributing 1.0 ppt to GDP. Fiscal support for initiatives to increase US semiconductor manufacturing capacity is likely supporting investment growth in these categories.

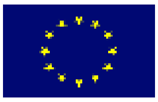
- The US labour market still looks resilient but the latest labour data prints seem supportive of a slowdown in the actual labour market conditions which could be less optimistic than the initial headline data suggests.
- **Monetary Policy Forecast:** FOMC meeting on 25-26 July 2023 saw Fed raised the target fed funds rate (FFR) range by +25bps to a 22-year high of 5.25%-5.50% as widely expected.
- Aside from the FFR decision, and the tweak in the description on the pace of economic expansion to “moderate” from “modest”, the latest FOMC statement did not change from the previous statement released after 13- 14 June 2023 FOMC meeting.
- In particular, FOMC statement implies Fed keeps the door open for further rate hike, given that its current “dot plot” signals additional +50bps hikes in 2H 2023. With the +25bps hike done at the 25-26 June 2023 FOMC meeting, the “dot plot” implies another +25bps increase at one of the remaining three FOMC meetings of this year i.e. 19-20 Sep; 31 Oct - 1 Nov; and 12-13 Dec.
- The recent Powell’s Jackson hole keynote speech started on a hawkish tone – that is, focused on getting inflation down to the 2% goal and it remains too high. He also assured that the Fed is prepared to hike more until “we are confident that inflation is moving sustainably down toward our objective”. Powell spent considerable effort on breaking down the inflation dynamics -> delving into supply and demand factors that included the availability of semi-conductor chips and concomitant effects on core goods inflation as well as housing services and non-housing services inflation. There is notable uncertainty on whether the recent downtrend in inflation metrics could extend. The US labour market is still observed to be resilient. Taken together, the concluding part of his speech was more on “risk management along the path forward” – while real rates are now positive, the neutral rate of interest is uncertain. As such, it is back to watching the data and acting with caution. The lack of mention on rate cuts pared rate cut expectations a tad more with only 86bps implied cut from current levels by end of 2024 priced in the Fed Fund Futures. Powell’s concluding points reflect that there is considerable uncertainty with the inflation trajectory as well as the policy path.
- As of 30 Aug 2023, futures market is pricing in 86%-14% split between pause and another +25bps hike at the 19-20 Sep 2023 FOMC. For the 31 Oct – 1 Nov 2023 FOMC meeting, the odds are 63.5% for pause and 36.5% for +25bps hike to 5.50%-5.75%. The probability of pause remains the highest for the final FOMC meeting of this year on 12-13 Dec. Overall, market is still pricing in a slight increase in probability for another rate hike in Sep.

- Between now and the next FOMC meeting (19-20 Sep 2023), and in relation to Fed's policy mandates on inflation and employment, there will be inflation and job market data releases respectively. To note, latest inflation number showed US inflation rate eased to +3.0% YoY in June 2023 – the lowest since Mar 2021. But that did not stop Fed from rehiking FFR at the 25-26 July 2023 FOMC meet after the pause at 13-14 June 2023 FOMC meet amid the still tight job market conditions.

- Maintain our call of no more FFR hike for the rest of the year… but it will be a "fluid" forecast. We maintained our view of FFR staying at the current 5.25%-5.50% level for the rest of the year, to be followed by a total of -200bps cuts in 2024. Admittedly, this is a "fluid" forecast, subject to how inflation and job market data pan out - as well as on the narratives by Fed's senior officials - between now and the remaining FOMC meetings for this year.

- **Key domestic events and issues to watch in Sep:** NFP (1 Sep), S&P Global US Manuf PMI, ISM Manuf (1 Sep), Factory Orders, Durable Goods Orders (5 & 27 Sep), FOMC (21 Sep), ADP (4 Sep), Trade Balance (6 Sep), NFP (1 Sep), Jul CPI (13 Sep), Empire Manuf (15 Sep), Retail Sales (14 Sep), Initial jobless claims (28 Sep), GDP (28 Sep), Core PCE (28 Sep), PCE deflator (29 Sep).

- **Technical Outlook:** DXY index was last seen at around 103.49. Momentum indicators suggest the DXY is still more vulnerable to the downside. Support is at 102.51 and 102.35. Resistance at 103.60 and 104.00.



EUR: Gentler Appreciation Expected

Forecast	3Q 2023	4Q 2023	1Q 2024	2Q 2024
EURUSD	**1.0800** (--)	**1.0900** (1.0900)	**1.1000** (1.1100)	**1.1200** (1.1300)

Previous Forecasts in Parentheses

- **Motivation for the FX View: We lower our EURUSD forecasts starting with 4Q2023 and the quarters ahead while maintaining the upward trajectory. This is to account for a potentially gentler appreciation of the EURUSD, as the USD remains better supported ahead by a resilient US economy and higher for longer US yields.** Economic data from the Eurozone showed that growth has returned to the Eurozone and that headline inflation has moderated. At the same time, core inflation remains sticky at elevated levels and as such the future of ECB hikes remains in the balance. We think that the EUR will continue on our expected trajectory against the USD, given that the Fed is likely closer to the end of its tightening cycle and pressures on the EUR from

EU-US yield differentials could abate, albeit at a slower pace than previously expected.

- **Risk(s) to our View:** The war in Ukraine is still ongoing and an end is nowhere in sight. Any further escalations of this war, although unlikely, present a key risk to our view for a stronger EUR. We expect peace to continue to be hard to achieve as Ukraine has retained its hard stance against Russia. We also expect most sanctions to remain, and this could continue to weigh on the Eurozone trade balance. This could then in turn weigh on the EUR.

- Also on the Ukrainian war-front, Russia has backed out of the Black Sea Grain initiative that allowed Ukraine to export grain via its ports in the south of the country. Russia looks unlikely to reverse its decision after turning its back on the deal on 17 Jul and could result in a price in global wheat prices which could in turn affect inflation in the Eurozone. In addition, this development represents a potential escalation in the conflict, and while there has been no immediate impact on the EUR, we keenly observe further developments on this front.

- Energy risks while lowered, still linger and a resumption of an energy crisis theme could weigh heavily on the EUR. Asian demand for LNG has remained muted thus far, and if this demand should pick up, then Europe will be competing for a limited supply of flexible LNG cargos. Europe is currently projected to attract almost 75% of global flexible LNG supply. This is the key assumption that drives analysts' estimates that Europe will survive the next winter. Should this situation change, then the EUR could once again face some challenging headwinds.

- The EUR also faces risks of ECB overtightening, which could lead to a destabilization of financial markets and a potential slowdown in the Eurozone economy. While the ECB has shown a hawkish tilt in recent months and signaled a willingness to raise interest rates to combat rising inflation, the potential for renewed financial instability remains a concern. While concerns over the viability of European banks have alleviated, continued tightening of monetary policy could once again call the viability of banks into question. However we recognize that the ECB has thus far handled the issues of combating inflation and maintaining banking and financial sector stability fairly well. As such, we think that this risk remains under control for now.

- The fall of Silicon Valley Bank, Signature Bank and the subsequent acquisition of Credit Suisse by UBS have called financial sector stability to question. The viability of European banks, such as Deutsche Bank, have also been similarly called to question and tested by markets. The EUR had weakened in the episodes of fear caused by Credit Suisse and Deutsche. While the fears seem to have eased and remain controlled now, the return of Europe-specific financial sector stability concerns are likely to weigh on the EUR once again.

- Eurozone growth prospects could drastically worsen if China's recovery does not materialize. This narrative is looking increasingly likely and if Eurozone economic data continues to deteriorate, then the ECB could be less convinced about tightening, especially if there is an accompanying pullback in price levels. Overall, this would be negative for the EUR from both a poorer growth standpoint and from the lack of support from the central bank.

- **Growth and Inflation Outlook:** Eurozone growth prospects have been lifted by the fall in natural gas prices that could potentially lower inflation and lift GDP. In addition, Europe also stands to benefit from China's reopening and recovery, although a sharper uptick in global demand recovery could have implications on commodity prices that may affect Europe's gas outlook. However, the ECB has also recognized that downside risks to growth exist given existing narratives about the slower than expected.

- Prelim 2Q23 Eurozone GDP growth printed at +0.3% SA QoQ (exp: 0.3%; prev: 0.3%) and +0.6% SA YoY (exp: 0.6%; prev: 0.6%), in line with advance estimates.The Eurozone has exited recessionary territory and once again headed into a growth environment as Ireland in particular experienced bumper growth in the second quarter of the year. Growth in Germany was flat QoQ, while Frace experienced a +0.5% QoQ expansion. While this should not be taken too positively, the Eurozone has by advance estimates emerged from a recession, which should be positive for the EUR at the margin.

- Jul Core CPI inflation printed at 5.5% YoY (exp: 5.5%; prev: 5.5%), while headline inflation moderated to 5.3% YoY (exp: 5.3%; prev: 5.3%), in line with preliminary estimates. We suspect that sticky core inflation could be the main consideration for the ECB moving forward as they advocate greater data dependence. We do however recognize that there are a few more data releases ahead of their next decision in Sep.

- **Monetary Policy Forecast:** On 27 Jul, the ECB raised rates by 25bps to take the deposit facility rate to 3.75%, marginal lending facility to 4.50% and main refinancing rate to 4.25%. There was a marked departure from the ECB and Lagarde's unequivocally hawkish position on inflation and an absence of previous language such as "inflation remained far too high for too long" and that the ECB was not pausing as it had yet to reach the terminal rate. Instead, there was a new emphasis on data dependence, although Lagarde did add that the ECB was still focused on combating inflation. Lagarde also suggested that the ECB could hold on raising rates at the upcoming Sep meeting and hike at a later date and said that the GDP growth figures for the Eurozone were encouraging. The approach of holding on rates for one meeting and hiking later is similar to the Fed's approach, and it remains entirely possible that the ECB takes this approach given their public acknowledgement of monetary policy transmission lags.

- For the rest of 2023, current OIS implied pricing is for a terminal deposit facility rate of 3.80%, with the market implying that the ECB could be done with one more hike. A pause would not necessarily be negative for the EUR as long as growth does not deteriorate significantly and inflation is en-route towards the 2% target. Given that the ECB's core inflation projection is 4.6% for 2023, and core inflation still remains sticky with the latest print at 5.5%, there is still a disparity between what the market is pricing in and what the ECB is expecting. Should the ECB actually deliver on expected rate hikes, we should see further gains for the EUR.

- **Key domestic events and issues to watch in Sep:** EC Aug Final Mfg PMI (1 Sep), EC Sentix Investor Confidence (4 Sep), ECB 1Y/3Y CPI Expectations, EC Aug Final Services/Composite PMI, EC Jul PPI (5 Sep), EC Jul Retail Sales (6 Sep), EC 2Q Final GDP (7 Sep), EC ZEW Survey Expectations (12 Sep), EC Jul Industrial Production (13 Sep), **ECB Policy Decision (14 Sep),** EC Jul Trade Balance, EC 2Q Labour Costs (15 Sep), ECB Jul Current Account, EC Aug Final CPI (19 Sep), Jul Construction Output (20 Sep), Sep Prelim Consumer Confidence, (21 Sep), Sep Prelim Mfg/Services/Composite PMI (22 Sep), Aug M3 Money Supply (27 Sep), ECB Economic Bulletin, Confidence Indices (28 Sep), EC Sep Prelim CPI (29 Sep).

- **Technical Outlook:** Pair was last seen at around 1.0870. Resistance is at 1.0971 and 1.1065. Support is at 1.0814 and 1.0680.

GBP: Near-term Support, Medium-term Challenges

Forecast	3Q 2023	4Q 2023	1Q 2024	2Q 2024
GBPUSD	1.2700 (--)	1.2500 (1.2400)	1.2400 (--)	1.2300 (--)

Previous Forecasts in Parenthesis

- **Motivation for the FX View: We maintain our forecasts for GBPUSD on the four quarters ahead. Given the prevailing sense that rate cuts could be some way off, we think that the GBP will retain support in the near-term and gradually fall off further in the future given the medium-term challenges facing the UK.** The UK's medium-term prospects still look grim, given the existence of price pressures, labour market shortages and an ailing economy, all structural problems inherited from Brexit. In addition, we think it is unlikely the BOE deviates from the Fed for an extended period. Governor Bailey has supported this view with his comment that the BOE were in a similar place to the ECB and Fed. We still believe that the cable is fundamentally overvalued at levels above 1.24. Based on this, we see the opportunity to fade rallies in the cable, although this could take a longer time to play out given that BOE hikes will be supportive.

- **Risk(s) to our View:** While we remain bearish on the GBP at current levels, we are also cognizant of two-way risks for the outlook. UK data has largely come in more positive than expected, although we feel that tailwinds from previous positive data prints and the Northern Ireland protocol are largely over and done with. Moreover, the Sunak administration's credibility that they have attained thus far could provide some support to the economy and help offset the negative effects of Brexit-related structural problems. Overall, while the downside risks are significant, it is important to keep in mind that there are still potential upside factors that could impact the cable.

- Governor Bailey has also acknowledged that the UK is in a wage-price spiral is also rather worrying. Core inflation had also re-accelerated earlier and this could potentially portend stagflation. While the BOE hikes should support the GBP at the margin, bad inflation or out of control inflation should be seen as a factor that is overall negative for the GBP. On balance, the risk is tilted towards GBP weakness, since stagflation fears could potentially weigh heavily on the GBP.

- The UK is in a tough position in no small part due to Brexit and the resulting protracted negotiations that have yet to be resolved. A positive resolution to any of these unresolved issues is likely to provide some support for the GBP. These issues are of paramount economic importance to the UK, but are ultimately politically daunting for the Sunak administration to deal with. The NI deal has passed the UK parliament and this has provided some tailwinds for the GBP. However, ultimately, the UK faces structural issues such as a labour shortage and poorer economic prospects from losing the common Euro market arising from Brexit. While no resolution for these issues remain in sight, Sunak's administration continues to gain more credibility for itself as it works on these issues. Should some further concessions be obtained from the EU, we do see the risk for a stronger GBP than we had previously projected.

- The fall of Silicon Valley Bank, Signature Bank and the subsequent acquisition of Credit Suisse by UBS have called financial sector stability to question. The viability of European banks, such as Deutsche Bank, have also been similarly called to question and tested by markets. Given the geographical proximity and the close ties of the UK banking system to the Euro banking system, the GBP weakened in the episodes of fear caused by Credit Suisse and Deutsche. While the fears seem to have eased and remain controlled at this point in time, the return of Europe-specific financial sector stability concerns are likely to weigh on the GBP once again.

- Although the BOE's tightening thus far has been seen as an appropriate response to inflationary pressures that remain elevated and stubborn, there also exists a risk that the BOE overtightens. This could worsen the UK's already difficult economic situation, given that Brexit-related structural problems such as a shortage of skilled labour and disrupted supply chains have contributed to the UK's weak economic performance in recent years. When overlaid with potential credit tightening issues that could arise in times of financial sector turmoil e.g. if banks were to refuse to lend to one another, an overtightening while appropriate in terms of dealing with inflation, could potentially drive the UK into a recession, which would eventually weigh on the GBP. The BOE therefore has to strike a tricky balance between raising rates to combat inflation and providing economic support e.g. through liquidity provided via their various facilities. In addition, Governor Bailey has already publicly admitted that the UK is in a wage-price spiral, and should this eventually lead to stagflation, there could be further problems for the UK and for the GBP down the line.

- **Growth and Inflation Outlook:** Quarterly GDP growth in the 2Q preliminary print looked indicated a modest expansion at +0.4% YoY (exp: 0.2%; prev: 0.2%) and +0.2% MoM (exp: 0%; prev: 0.1%). There was an upside surprise to the monthly GDP growth in Jun at 0.5% MoM (exp: 0.2%; prev: 0.1%). This was the first of many data prints that suggested that rates could stay higher for longer as the economy in the UK is not doing as badly as previously thought – given earlier expectations of a recession. Current consensus forecast suggests GDP growth to come in at +0.3% YoY (prev: +0.2% YoY) for the UK in 2023. In addition, there are still significant downside risks for the UK economy – it may struggle to recover from current challenges such as the lingering impact of COVID-19, supply chain disruptions, and slowing global demand in addition to facing the structural issues such as labour market shortages and loss of the common market that have come with Brexit. The balance of probability is still tilted in favour of a UK recession, with the implied likelihood of a UK recession over the next 12 months is at 60% (prev: 54.5%). The BOE earlier upgraded growth forecasts for the UK to 0.25% in 2023 and 0.75% in 2024 and 2025. This is in stark contrast to their previously anticipated recession forecasts of about -1.50% in 2023 and -1.00% in 2024. That said, the BOE also recognizes two-way risks for growth amid the current uncertainty in the global economy.

- Jul CPI inflation fell to 6.8% (exp: 6.7%; prev: 7.9%). Core CPI inflation remained sticky at 6.9% (exp: 6.8%; prev: 6.9%), with the services sector accounting for an estimated +0.8% SA MoM increase in prices. This supports the case for further rate hikes, given that persistence in price pressures, especially from the services component that the BOE is most focused on, could result in significant upside risks to inflation in the future. Recall that the previous re-acceleration in core inflation in Apr was also attributable to firmer services inflation. Inflation overall is on the right trajectory as the bank has said, although concerns of upside risks and sticky core inflation should also weigh heavily on policymakers' minds. Inflation has been kept sticky also in part due to a labour shortage in the UK that has been exacerbating strong wage cost pressures. Consensus estimates for CPI inflation in the UK are at 7.5% in 2023 and 3.0% in 2024, higher than the BOE expects.

- **Monetary Policy Forecast:** On 3 Aug 2023, the Bank of England's Monetary Policy Committee (MPC) responsible for setting monetary policy to achieve the 2% inflation target and support growth and employment, voted 6-3 to increase the Bank Rate by 25bps to 5.25%. Two members (Haskel and Mann) preferred a 50bps increase, while one member (Dhingra) preferred to maintain the bank rate.

- The MPC noted that their remit on price stability and specifically to return CPI inflation to the 2% target sustainably in the medium term formed the primary objective of the decision. As such, the BOE pledged to be data-dependent on decisions moving forward. Data of particular interest would include inflation, GDP, unemployment and wage growth. The BOE noted that the current stance was restrictive and they would ensure that the rate would be sufficiently restrictive for sufficiently long to return inflation to the 2% target sustainably in the medium term.

- Should inflation indeed fall off in the second half of the year as the BOE suggests, the terminal rate could turn out to be lower than the market is pricing at the moment. We think that the BOE is in a difficult spot and has declined to provide forward guidance to provide itself with some flexibility. Unresolved problems from Brexit could pose more troubles for the BOE in the future. The BOE is also cognizant of the risk of overtightening at this point of time, given the prevailing concerns of an overtightening in the Eurozone area.

- **Key domestic events and issues to watch in Sep:** S&P Aug Final Mfg PMI (1 Sep), Official Reserves Change, S&P Aug Final Services/Composite PMIs (5 Sep), S&P Aug Final Construction PMI (6 Sep), CPI/Output Price Expectations (7 Sep), Aug ILO Unemployment, Jul Avg Weekly Earnings, Other Employment (12 Sep), Jul Monthly GDP , Jul Industrial/Manufacturing Production, Jul Visible Trade Balance (13 Sep), RICS House Price Balance (14 Sep), BOE Inflation next 12 Months (15 Sep), Rightmove House Prices (18 Sep), Aug CPI/RPI/PPI (20 Sep) , Aug Public Sector Finances, **BOE Policy Decision** (21 Sep), Consumer Confidence, Aug Retail Sales, Sep Prelim Mfg/Svc/Composite PMIs (22 Sep), Nationwide House Price Indices (28 Sep to 3 Oct), 2Q Final GDP, Current Account, Aug Money Supply, Aug Mortgage Approvals (29 Sep).

- **Technical Outlook:** Pair was last seen at around 1.2675. Resistance is at 1.2780 and 1.2850. Support is at 1.2540 and 1.2400.

AUD: Pressure Unlikely to Lift Much

Forecast	3Q 2023	4Q 2023	1Q 2024	2Q 2024
AUDUSD	**0.65** (0.65)	**0.66** (0.68)	**0.66** (0.70)	**0.68** (0.70)

Previous Forecasts in Parenthesis

- **Motivation for the FX View:** We downgraded the AUDUSD forecasts from 4Q 2023 onwards. We look for the bearish seasonality to potentially extend into Sep, especially if Australia's labour market and retail sales continue to soften. At this point, cash rate futures still imply a 50% probability of a rate hike by Mar 2024. We hold our view that even as RBA remains vigilant on inflation, weakening household consumption should mean that 4.10% is the peak of this tightening cycle for the RBA. We also see risks that RBA could be one of the first few G7 central banks to kick off its easing cycle, especially ahead of the Fed (as the average mortgage costs rise at home) and that could weigh on the AUD into 2024.

- **Growth and Inflation Outlook:** Recall that the inflation for the year through Jun 2023 came in at 6.0%y/y, just a tad under RBA's inflation forecast of 6¼% as indicated in the SoMP that was released in May. While the headline inflation as well as underlying inflation had eased more than expected due to lower automotive fuel prices, slower increase in prices of food, furniture, appliances and clothes, most worrying was the strong services inflation that rose to more than two-decade high of 6.3% and these include rents, restaurant meals, holiday travel and insurance. **A more forward looking indicator** would be the Melbourne Institute consumer survey that indicates consumer's expectations of price pressure over the next 12 months. **The Aug survey indicates that consumers expect <u>inflation to ease further</u> to**

4.9% over the next 1 year vs. 5.2% seen in Jul. Consumers expect inflation to be around 5.9% (Which is pretty close to current headline). Easing inflation expectations could reduce the need for RBA to tighten monetary policy further.

- **Most recently released retail sales surprised to the upside at +0.5%m/m vs. previous -0.8%. The** headline was boosted by the stronger spending on catering and takeaway food outlets linked to the 2023 FIFA Women's World Cup and school holidays. Breakdown reveals +1.3% growth in spending on cafes, restaurants and takeaway food services, +3.6% rise in department stores. Household goods retailing fell -0.2%. Separately, CBA household spending was flat 0.0%m/m for Jul compared to 0.5% in the month prior. Given that the strong ABS retail sales for Jul is event-linked, we do not expect spending to be as resilient for Aug. Afterall, the household saving ratio plunged to just 3.7% for 2Q from 4.4%. This compares to the 23.6% household saving ratio seen in Jun 2020. At 3.7%, it is lower than pre-pandemic 2019 levels. Lower saving ratios could reduce Australian's ability to consume.

- Unemployment rate rose to 3.7% for Jul. Australia lost a net -14.6K jobs in Jul, a -21.2K loss of full-time employment was offset by a 9.6K gain in part-time. Participation rate fell a tad to 66.7% from previous 66.8%. In the latest Statement of Monetary Policy (Aug), RBA had maintained its projection for unemployment rate to rise to 4.0%. We anticipate further softening of the employment market as household consumption continues to weaken. Prelim. Mfg and services PMI have deteriorated further in contractionary region for Aug at 49.4 and 46.7 (vs. prev. 49.6 amnd 47.9 respectively).

- Home loans fell -1.0%m/m in Jun, after a strong growth for May. The strong The recovery in the home prices was also alluded to the anticipation for RBA to end its tightening cycle. An imbalance of supply and demand is also a key reason for home prices to rise. It is unclear if the rise in home prices could sustain as mortgage rates remain very high and more supply of homes have come on stream due to the recent rebound in prices.

- **Monetary Policy Forecast:** We look for RBA to keep cash target rate unchanged at 4.10% and we see risk that the central bank could be one of the first to cut into 2024. RBA held cash target rate unchanged at 4.10% on 1 Aug, in line with our expectations which was against the consensus. Our view for RBA to keep policy settings unchanged was based on the fact that household spending had softened recently in the backdrop of low household saving ratio (at 3.7% for 2Q 2023). This compares to the 23.6% household saving ratio seen in Jun 2020. At 3.7%, it is lower than pre-pandemic 2019 levels. Australian households have run down their excess savings and are now saving much less than before due to higher interest rates and elevated inflation. Prelim. Services PMI for Aug also fell further into contractionary terrain to 46.7 from 47.9, underscoring weakening demand conditions that **just might not have shown up on the quarterly inflation metrics** yet. In our view, even though Aug was a hawkish pause, this is likely the last live decision as we look for household spending to weaken further. **We look for the RBA to keep cash target rate unchanged at 4.10% for the rest of the year and to cut cash target rate by 25bps in Feb 2024.**

- **Latest External Balance Outlook:** As of last available data, current account surplus was recorded at +1.4% of GDP for 1Q 2023, widening a tad from the previous 1.13%. Over the same period, Australia recorded a AUD12.3bn of current account surplus vs. previous A$11.7bn in 4Q 2022, buoyed by the stronger surplus in goods and services trade balances. Trade surplus widened a tad to AUD11.3bn in Jun from previous AUD10.5bn as imports (-4%) fell more on the month vs. exports (-2%). Weakening demand in China could continue to weigh on export receipts for Australia.

- **Fiscal Outlook:** Australia is projected to achieve a fiscal surplus of 0.2% of GDP for FY2022-2023 but this would be a fleeting one. This would be the first surplus in 15 years but Treasurer Jim Chalmers also flagged that a deficit of $13.9bn is expected for FY23-24.

- **Key domestic events and issues to watch:** PMI Mfg (Aug F), Jul jome loans [1 Sep]; Aug M-I inflation [4 Sep]; Final Services PMI, RBA policy decision [5 Sep]; 2Q GDP [6 Sep]; Jul trade [7 Sep]; Sep Westpac consumer conf, Aug NAB business confidence/conditions survey [12Sep]; Aug CBA household spending, Aug labour report, Sep consumer inflation expectation [14 Sep]; Minutes of RBA meeting [19 Sep]; Westpac leading index for Aug [20 Sep]; prelim. Sep Mfg PMI, Services PMI [22 Sep]; Aug CPI [27 Sep]; Aug retail sales [28 Sep].

- **Technical Outlook:** AUDUSD seemed to have bottomed around the 0.64-figure and has risen to levels around 0.6490 in light of lower UST yields, support measures in China. These confluence of factors also improved risk sentiment and bolstered the USD. The bearish trend channel seems to have violated and a bottom seem to have formed tentatively around the 0.64-figure. Momentum seems to suggest further room for bullish extension towards 0.6610 (50-dma). We see that as a cap for the AUD. Interim resistance is seen around 0.6550.

NZD: Volatile Trades Ahead

Forecast	3Q 2023	4Q 2023	1Q 2024	2Q 2024
NZDUSD	**0.60**	**0.60**	**0.61**	**0.62**
	(0.63)	(0.65)	(0.67)	(0.67)

Previous Forecasts in Parenthesis

- **Motivation for the FX View:** We downgraded the NZDUSD forecast a tad as the resilience in the US economy had lasted longer than expected and that has kept the NZDUSD under pressure. The small forecast downgrade also takes into account the sharp decline in milk prices in Aug that is due to the current surplus of fresh milk in China. **Barring a technical rebound in the near-term, we look for the NZD to remain under pressure for much of 4Q 2023** as weak domestic demand at home could eventually force RBNZ to embark on an easing cycle ahead of other G7 economies within the next six months – a scenario that is underpriced by markets based on OIS. That said, the 12-month NZDUSD trajectory is still a modestly bullish one as we look for US growth to slow further while China's economy could find its foothold into 2024.

- CFTC data suggests that long NZD positions have been unwound almost completely from its high of 45010 in Jun 2022 and net long contracts are at a tenth of that now. While that could mean that the decline in the NZDUSD could slow and there could even be some upside risks in the near-term, fundamental drivers such as potential for further RBNZ-Fed policy divergence should weigh on the NZDUSD eventually.

- **Growth and Inflation Outlook**: BusinessNZ Mfg PMI fell to 46.3 for Jul from prev 47.4 while performance services index also fell to 47.8 from previous 49.6. Activity is slowing for both services and manufacturing. Meanwhile, the soft patch persists for retail card spending as well, slowing to a flat growth for Jul vs. +0.9%m/m in Jun, a sign that retail spending into 3Q is likely to remain weak.

- Of note, retail sales (ex inflation) falling by a steeper than expected -1.0%q/q. Breakdown suggests almost all subcomponents were under pressure with the eception of motor vehicles/parts (+3.7% vs. prev. -2.1%), department stores (+0.4% vs. prev. +0.5%), pharmaceutical (+1.4% vs. prev. -3.2%) and accommodation (+0.2%m/m vs. -2.6%). The rest of subcomponents saw quarter-on-quarter decline in 2Q and these include supermarket/groceries, furniture, hardware/building supplies, clothing/footwear, food&beverage and electrical goods. The decline was observied in spite of strong population growth that was expected to boost domestic demand.

- Recall that 2Q CPI eased to 6.0%y/y from 6.7% in 1Q. The quarterly pace also slowed less than expected to 1.1% from previous 1.2%. Tradeable inflation quickened to +0.8%q/q from previous 0.7% while non tradeable eased to 1.3%q/q from previous 1.7%. The pullback in non-tradeable inflation also underscores weaker domestic demand. While the prints were firmer than median estimates, the disinflation progress is largely intact. Into 3Q, food prices fell -0.5%m/m in Jul vs. prev. +1.6 but 2Y inflation expectations edged higher to 2.89% from 2.79%. Disinflation process seems to have stalled for now. We do not think that will move the needle for RBNZ policy decision next month.

- REINZ house sales for Jul also slowed to +1.6%y/y from previous +14.6%. Despite slower house sales, trend-wise, there are signs of a recovery in the real estate. Meanwhile, nuilding approvals fell -5.2%m/m in Jul vs. previous growth of +3.4%. CoreLogic House prices also clocked another steep decine of -10.1%y/y for Jul vs. previous -10.6%. Construction activity still seems pretty weak at this point and would probably require more time to recover. Taken together, sluggish activity could eventually have a spillover effect on the labour market.

- In fact, unemployment rate rose more than expected to 3.6% form previous 3.4%. While that is still below the pre-pandemic levels, weak domestic demand, not helped the least by rising average mortgage costs could continue to dampen hiring intentions.

- **Monetary Policy Forecast:** RBNZ is likely to keep OCR at 5.50% for the rest of 2023 and the central bank could start cutting rates in 1Q 2024.

We bear in mind that RBNZ expects inflation to come within the 1-3% target by 3Q 2024 and the latest inflation prints, whilst a tad firmer than expectations, continue to suggest that price pressure continues to ease. On the other hand, monetary policy settings are restrictive enough such that these factors do not fan inflation pressures higher. The central bank notes that the mortgage rates on outstanding loans have increased by around 200bps from early 2022 and average mortgage rates are expected to reach around 6% in early 2024. The central bank also noted that there are pockets ofstress emerging but early indicators suggest that the increase in stressed lending in the coming months should be modest. Manufacturing and services have already started to slow and further deterioration could soften hiring conditions more considerably and spur RBNZ to cut in 1Q 2024.

- **External Balance and Fiscal Outlook:** NZ current account could remain in deficit. Current account deficit narrowed to -NZD5.22bn in 1Q vs. NZD10.1bn in the quarter prior. Services balance have started to swing into surplus and could rise further into 2Q amid the influx of migrants and tourist arrivals. However, goods trade could remain in deficit due to weak external demand. Trade deficit widened in Jul due to a fall in exports from NZ6.18bn to NZ5.45bn while imports rose to NZ6.546bn from prev. 6.29bn.

- **The Treasury projected a return to fiscal surplus in 2025/2026, delayed by one year.** New Zealand now expects the economy to avoid recession, looks for a budget deficit of NZ7.6bn in 2023-2024. GDP growth is expected to be around 1% for this FY23/24 and 3.2% in FY22/23. Net debt to peak at 22% of GDP in 2023-2024. The budget includes an extension pf 20 hours Early Childhood Education to include 2y olds, abolition of $5 prescription co-payment, subsidies for children to take public transport and $71bn of infrastructure spending. The budget was seen more expansionary than expected, funded by more borrowing. This could boost discretionary spending slightly.

- That said, the Geneal Election is scheduled to be held on 14 Oct and parties are proposing changes to the tax system. Labour pleged to remove the 15% GST from fruit and vegetable and to increase benefits for low-income households if it retains power. Main opposition National Party proposed to increase tax credits for families and lift tax thresholds to compensate for inflation that could ultimately benefit middle-income voters.

- **Key domestic events and issues to watch:** ANZ Aug Consumer confidence [1 Sep]; 2Q Terms of Trade [4 Sep]; ANZ Aug Commodity Price [5 Sep]; Mfg Activity for 2Q [7 Sep]; Aug REINZ House sales [10-14 Sep]; Card spending for Aug, Net Migration for Jul [12 Sep]; Aug Food prices [13 Sep]; Aug BusinessNZ mfg PMI [15 Sep]; Performance services index [18 Sep], Aug Non resident bond holdings [18 Sep]; BoP current account bal for 2Q [20 Sep]; 2Q GDP [21 Sep]; Aug trade [22 Sep]; ANZ Sep activity outlook, business confidence [28 Sep];ANZ Sep consumer confidence [29 Sep].

- **Technical Outlook:** NZDUSD rose to levels around 0.60. Recent price action suggests that there could be a bottom forming around 0.59. Momenutm is turning higher based on MACD forest as well as stochastics.

Resistance at 0.6025 before the next at 0.6060 and then at 0.6110 (50-dma). Support at 0.5900 before 0.5840.

CAD: Range Intact

Forecast	3Q 2023	4Q 2023	1Q 2024	2Q 2024
USDCAD	**1.33** (--)	**1.32** (1.31)	**1.31** (1.30)	**1.31** (1.30)

Previous Forecasts in Parenthesis

- **Motivation for the FX View:** We maintain our forecast trajectory for USDCAD for the next 12 months as we look for USD to weaken more discernibly alongside an economic slowdown. Upside surprises in Canada's data could keep the BoC hawkish but another rate hike is highly unlikely as unemployment continues to rise. That could mean that risks to the USDCAD could be skewed to the downside. Medium-term, the end of the hiking cycles around the world without a severe economic recession could actually be modestly benign for risk-sensitive CAD. Potential for China to stabilize and recover could also bolster pro-cyclical CAD to some extent.

- The high-for-longer narrative has been played in the favour of UST yields as well as the USD for so long that a string of weak data could knock the USDCAD off its current lofty heights. Even as the high-for-longer market narrative could be exhausted for now, that does not mean that it cannot return or linger to some extent given that this is conditional on data. In addition, this divergence of the US vs. RoW can persist for a while and keep the USDCAD supported on dips. As such, we calibrated the USDCAD forecasts a tad higher.

- **Growth and Inflation Outlook:** Inflation outlook remains uncertain especially with the unexpected pick-up in CPI for Jul to 0.6%m/m from previous 0.1% (estimated 0.3%)/ Year-on-year, CPI accelerated to 3.3%y/y from previous 2.8%. The uptick in the headline driven by the rise in food inflation (+0.4%y/y vs. prev. 0.1%), recreation and education (+2.1%m/m vs. prev. -0.8%), alcohol and tobacco (+0.4% vs. prev. +0.1%). Energy prices accelerated to +1.7%m/m from previous +1.4%. Goods inflation was relatively stable at +0.2%m/m. Core inflation eased with trim CPI softening to 3.6%y/y from previous 3.7%.

- Spending has slowed with retail sales ex auto for Jun down a steeper -0.8%m/m compared to an estimated growth of +0.3%. The may retail sales ex auto was also revised lower to -0.3%. With interest rates raised further in Jul, we expect spending to slow more discernibly into 3Q.

- Based on the 2Q business survey conducted by BoC, that was already the outlook projected by businesses. The high interest rate environment affects firms that are linked to housing and consumer discretionary spending but firms also noted that there are signs of resilience due to fewer concerns on recession, improved supply chains, path of interest rates. Private investment is expected to be modest due to the weakened demand outlooks but investment intentions remain strong for firms linked to natural resources. Pressures in the labour market is eaing and growth in wages is expected to “moderate from high levels”. More firms are expecting inflation to take five years or more to get to 2% as inflation is perceived to be spurred by government spending and strong demand. The Business Outlook suvey indicator suggests less inflationary pressure as demand outlook is weaker.

- When asked about price-setting, firms look for price increases to slow but businesses have not reverted to pre-pandemic price-setting behaviour. They are still adjusting prices at a higher frequency and with a larger magnitude than usual.

- The labour market did show signs of softening with unemployment rate on the rise, last at 5.5% for Jul vs. 5.4%. Canada lost a net -6.4k jobs in Jul, a stark contrast to the 59.9K added in the month before. Net job losses were part-time at -8.1K and that offset the full-time employment gain of +1.7K for Jul. Participation rate fell to 65.6% from previous 65.7%. The rise in unemployment, the net job losses suggest that BoC may find it harder to hike rates.

- **Monetary Policy Forecast:** BoC is unlikely to hike further. We look for the overnight lending rate to remain unchanged at 5.00% for the rest of the year. Headline inflation might have surprised to the upside, above the central bank’s 1-3% target inflation mandate, but core inflation continued to ease and that should be reason for the central bank to act with caution. Retail sales have started to slow as well and that was before the rate hike in Jul. BoC business survey suggests that while there are still pockets of resilience in the economy, prospects are being dampened by the high interest rate environment. Weakening demand prospects (of consumption and investment) as indicated by the BoS (Business Outlook Survey) should deter the BoC from tightening further as the accumulated 475bps rate hike continue to work its way through the economy.

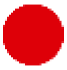
- **Latest External Balance Outlook:** As of last available data, Canada’s current account balance was at a deficit of -U$14.2bn for 1Q23, wider than the -U$6.6bn deficit for 3Q. Trade balance has collapsed back into deficit with the latest recorded at CAD3.73bn for Jun. This was due to the fall in exports in the month that exceeded the decline in imports.

- The new Federal budget presented on 28 Mar showed an increase of C$43bn of new net costs over six years with a focus on improving health-care and fund clean-technology subsidies. Canada records C$6.44 deficit in the first ten months of FY2022-2023. However, the budget 2023 no longer shows a projection towards a balanced budget by 2028. Fiscal is still pretty much expansionary with overall balance at -1.5% of GDP for FY2022-2023, albeit still narrower than the -3.24% of GDP for the prior fiscal year.

- **Key domestic events and issues to watch:** Jun, 2Q GDP, Mfg PMI for Aug [1 Sep]; Jul Trade, BoC Rate Decision [6 Sep]; Jul Building permits [7 Sep]; Aug labour report [8 Sep]; Wholesale sales for Jul [14 Sep]; Jul manfuacturing sales, Aug existing home sales [15 Sep], Aug housing starts [18 sep]; Aug CPI [19 Sep]; BoC Summary of deliberations [21 Sep];

Jul retail sales [22 Sep]; CFIB business barometer for Sep [28 Sep]; Jul GDP [29 Sep].

- **Technical Outlook:** USDCAD could be vulnerable to more downside and we see move towards 1.3460 from current 1.3530. Momentum indicators are turning lower. Resistance at 1.3680. Next support at 1.3390 before 1.3330.



JPY: "Weak For Longer"

Forecast	3Q 2023	4Q 2023	1Q 2024	2Q 2024
USDJPY	**145** (138)	**142** (136)	**140** (132)	**134** (125)

Previous Forecasts in Parentheses

- **Motivation for the FX View:** We are revising our USDJPY forecast upwards to reflect a weaker profile for the JPY over a longer period. This "weak for longer" narrative for the JPY is firstly a reflection of the factor that that BOJ is likely to maintain a dovish tilt for the rest of 2023 and almost entirely in 2024. Although we believe the YCC is likely to be abolished in 2Q 2024, this would do little in supporting the JPY given that JGB yields could still be not much higher from current levels. An exit from NIRP is likely to only occur in 1H 2025, when the BOJ should be more convinced by then that a 2.00% inflation level can be sustainably held. Meanwhile, UST yields are likely to stay elevated and only come off gradually as the Fed keeps rates high with a hawkish tilt until US inflation looks comfortably at around the 2.00% mark. A cut from the Fed may only come in 2Q 2024. Consequently, we see the USDJPY to stay elevated (albeit coming off slightly over time) at 145, 142 and 140 in 3Q 2023, 4Q 2023 and 1Q 2024 before a sharper move downwards in 2Q 2024 to 134.00. At the same time, we think it less likely that the USDJPY would move up much higher than our forecasts from 3Q 2023 – 1Q 2024 given the possibility of intervention by the BOJ/MOF at 150.00. We would like to note that the risk to our view is that US inflation reaccelerate causing the Fed to hike aggressively again although we think this is unlikely to materialize.

- **Growth and Inflation Outlook:** 2Q GDP (P) numbers accelerated and surprised strongly on the upside at 6.0% QoQ (est. 2.9% and 1Q. 3.7% QoQ). However, the big driver of growth was external demand, which was reflection of both the reopening boost to tourism and the weaker JPY giving support to goods demand (and tourism for that matter too). Domestic demand itself was actually weak as private goods consumption slumped although services consumption continued to rise. Capex was also lackluster. The numbers as a whole in our view continues to reflect the fragility of the Japanese economy given that the reopening boost would gradually wane whilst the global economy is looking to soften amid the high rates. Whilst 2023 growth can still perform reasonably well at 2.0% YoY, there is a chance that 2024 could see it come out much slower at 1.0% YoY.

- Headline inflation for July was steady at 3.3% YoY whilst the core number was at 3.1% YoY and the core-core at 4.3% YoY. All numbers were in line with expectations and still showed price pressures holding up. However, there is clearly deviation emerging between services and goods inflation. Price pressures for services rose amid the expiration of travel subsidies and a jump in mobile phone charges. Price revisions to transportation should see services inflation firm from 4Q 2023. An easing of cost pressures could have contributed to a moderation in goods inflation. Food inflation looks to have stabilized though. As it stands, going into 2H 2023, a moderation in core inflation is likely to be limited amid this continued services price pressure.

- Meanwhile, it is not fully clear in our view if wages are trending upwards as June labor cash earnings slowed to 2.3% YoY (May. 2.9% YoY) whilst the real number contracted even more at -1.6% YoY (May. -0.9% YoY). Labor market at the same time still look tight especially compared to pre-pandemic with the Jul job-to-applicant ratio at 1.29 although we do note the jobless rate ticked up to 2.7% (Jun. 2.5%). However, there is no reason to believe that this increase in the latter is a reflection of worsening labor market conditions as the jobless rate increase looks to be a reflection of more people seeking jobs or leaving roles to look for higher pay. Structurally, the labor market appears tighter, providing an opportunity for workers to push higher pay. This combined with the minimum wage increase and the spring wage negotiable outcome looks to point towards more pick up in wages. We do believe in the possibility that this could be the case going forward although we stay wary of the risks amid a fragile economic setting both domestically and globally.

- Aug (P) PMI data again showed a further pick-up in services to 54.3 (Jul. 53.8) whilst manufacturing remained in contraction territory at 49.7 (Jul. 49.6). The former is a continued reflection of how the reopened economy is boosting services demand. However, this should gradually wane in time, eliminating this form of support for the economy. The manufacturing PMI has now been in contraction for 9 of the last 10 months. This was in line with the softening in the global goods trade. Underlying, the numbers were mixed and did not point any necessary signs of improvement. New export orders and overall new orders saw increases but stayed below the 50.0 mark whilst the future manufacturing output index fell substantially by 2.4 points. The PMI numbers overall still reflects the fragility of the economy.

- July retail sales accelerated above expectations to 6.8% YoY (est. 5.5% YoY and Jun. 5.6% YoY) whilst on a monthly basis it turned around to a positive number at 2.1% MoM (est. 0.8% MoM and Jun. -0.6% MoM). As a whole retail sale still remains on an upward trend albeit some blips as it benefits from the economic reopening with the inflow of foreign tourists. Some recent higher wage growth numbers could be supportive of consumption. Aug consumer confidence at the same time was slightly lower at 36.2 (Jul. 37.1) although this is just a one month fall and does not necessarily imply that the upward trend has turned around just yet. We stay confident that consumption momentum can maintain for the rest of 2H 2023, giving support to the economy. However, the risk that the reopening boost can wane overtime, especially into 2024 highlights the fragility of the economy.

- **Monetary Policy Forecast:** We see that the BOJ is likely to abolish the YCC in 2Q 2024 whilst they would exit the NIRP in 1H 2025. We see the former happening around that time once the broad perspective review is completed and a sufficient time has passed to allow for price discovery in the JGB 10y yield market (given that it is uncertain where yields should stand at after years of YCC though we think it would likely remain below 1.00%). We strongly believe that the BOJ is unwilling to continue with the YCC given the issues it poses to market functionality. The last MPM had shown that 11 out of 15 members were in favor of increasing the flexibility of the YCC. Almost all opinions at the same time did point that they thought the YCC adjustment was a measure to continue the current framework of monetary easing. This points to the BOJ still at least expressing a dovish tone in the medium term even if they make the YCC adjustment.

- However, our rationale behind the much later date for the NIRP exit revolves around how economic conditions are looking to evolve after this year. Whilst inflation looks to be able to still hold up albeit moderating in 2H 2023, it remains uncertain how the state of the economy would be after this year. The BOJ's own core inflation forecast at this point though is actually expecting a slow down over the coming years and to below the target at 2.00% – FY2023: 2.5%, FY2024: 1.9% and FY2025: 1.6%. However, with a structurally tighter labor market in Japan, there is a possibility that wages can pick-up in the medium term, supporting higher inflation. We are also keeping a close eye to how wage negotiations fare next year although we would not rule out the possibility that it can still come out solid. We therefore see a likelihood that inflation can come be more soundly at 2.00% by 1H 2025 and by the point, the BOJ should be more convinced to exit NIRP.

- Overall, we believe the BOJ is still going to keep a dovish tilt for the rest of 2023 and 2024, which in turn would be a negative for the JPY. Hence, we expect to BOJ policy decision on 22 September to show no changes.

- Meanwhile, on the point of intervention, we see it likely that the BOJ/MOF may only come in at 150.00 given that they would want to avoid creating a new high. If they do not come in around that level, there is a risk that momentum can keep pushing up the USDJPY especially in light unfavorable near term fundamentals that include continued easy BOJ monetary policy and a "high for longer" Fed that would keep UST – JGB differentials wide. The possibility of intervention means that there would limited upside for the USDJPY from current levels.

- **Latest External Balance Outlook:** June CA balance stayed in surplus at 1.5tn yen (May. 1.8tn yen). However, we would also note that the Jul trade balance actually turned to a deficit again at 78.7bn yen (Jun. 43.0bn yen) due to imports falling less than expected at -13.5% YoY. On real terms, imports had actually jumped by 2.9% MoM. Meanwhile, exports had declined on nominal terms by -0.3% YoY but on real terms it rose 1.3% MoM as automobile exports remained strong with an easing in supply chains. We continue to keep a close eye on how the trade and CA balance especially in light of the weaker JPY and the risk of higher commodity prices. For now, the external position still looks manageable given the CA is in surplus since February. Tourism numbers should still stay strong for the rest of this year with the reopening boost still in effect.

- **Key domestic events and issues to watch:** 2Q capital spending (1 Sept), 2Q company profits/sales (1 Sept), Jul household spending (5 Sept), Jul (P) leading/coincident index, Jul cash earnings (8 Sept), 2Q (F) GDP (8 Sept), Jul BOP CA (8 Sept), Aug bank lending (8 Sept), Aug money stock (11 Sept), 3Q BSI large all industry/large manufacturing (13 Sept), Aug PPI (13 Sept), Jul core machine orders (14 Sept), Nationwide/Tokyo dept sales (15 – 22 Sept), Aug trade data (20 Sept), Aug CPI (22 Sept), Sept (P) Jibun Bank PMIs (22 Sept), BOJ policy decision (22 Sept), Aug PPI services (26 Sept), Tokyo CPI (29 Sept), Aug jobless rate/job-to-applicant ratio (29 Sept), Aug retail sales (29 Sept), Aug (P) IP (29 Sept), Aug consumer confidence index (29 Sept) and Aug housing starts (29 Sept).

- **Technical Outlook:** Pair was last seen around 145.90. Resistance is at 148.00 and 151.95 (2022 high). Support is at 145.06 (21-dma) and 138.00. Momentum indicators point to the downside.

RMB: Aiming for Stabilization

Forecast	3Q 2023	4Q 2023	1Q 2024	2Q 2024
USDCNY	**7.30** (7.15)	**7.25** (7.10)	**7.20** (6.95)	**7.15** (7.00)
USDCNH	**7.30** (7.15)	**7.25** (7.10)	**7.20** (6.95)	**7.15** (7.00)

Previous Forecasts in Parenthesis

- **Motivation for the FX View:** We turn more cautious on the yuan but our forecast trajectory is still a bearish one for USDCNY and USDCNH over the next 12 months. We assume (1) that the Fed is at the end of its tightening cycle (or at most one hike away from it), (2) global growth will slowdown gradually (with minimal growth differential between the rest of the world with the US), (3) China's "proactive" fiscal policy could take effect soon - with local government debts resolved to some extent to improve their capacity to invest in strategic infrastructure projects. (4) easing of macro-prudential policies (easing of existing mortgage rates/ cutting of downpayments) for properties to potentially increase disposable income for households to consume and to potentially support the property sector. We see a chance for credit growth to improve in Aug and domestic demand to stabilize in Aug and that could provide modest support for the RMB. Regardless, any hope for growth rebound in 4Q could still be pre-mature. We downgraded USDCNY and USDCNH forecast to take into account the recent market developments as well as the fact that economic recovery is not likely to be as soon or as strong as we had originally expected.
- **What has happened in Aug:**

  — **Measures provided:**

  - Market-related - reduction of stamp duties for equity trading (0.1% to 0.05% as of 28 Aug). The last time this was done was in 2008.
  - Slow the pace of IPOs.
  - Restrictions on the frequency and the amount of refinancing will only be set for companies that continuously report financial losses and whose stock prices have fallen below IPO levels or net asset levels.
  - Property-related - *Local government can remove a rule that disqualifies people who've ever had a mortgage from being considered a first-time home buyer in major cities.* This basically allows more people to qualify as first-time home buyers.
  - Extend personal income tax rebates for people who buy new homes within one year after selling old homes till end of 2025.
  - **Downpayment ratio was cut** by varying extent in different top tier cities - Beijings (up to 80% previously to current 35-40%),

Shanghai (up to 70% previously to current 35%), Guangzhou (up to 70% previously to current 30%) and Shenzhen (up to 80% previously to current 30%).

- A directive was said to be given to major SOE banks to cut interest rates on the majority of the nation's CNY38.6trn of existing mortgages. The reductions will only affect loans on first homes. In order to ease the pressure on the NIMs, *interest rates for yuan deposits could be cut between 5-20bps across tenors and could be announced as soon as 1 Sep*. Apart from allowing existing mortgage owners to benefit from rate cuts, this would also reduce the mortgage repayment pressure and Chinese banks would also be more keen to lower the 5Y LPR to be reduced in Sep.
- **Local government debt -** On 28 Aug, the MOF pledged to prevent and resolve the local government debt risks and strengthen its fiscal discipline. The Finance Ministry will ramp up and implement active fiscal policies and hasten the transfer of payments to localities. In a separate report to the NPC Standing Committee that day, the NDRC urged local government to accelerate issuance and the use of special bonds.
- Bloomberg calculation suggests that provincial governments had sold the most amount of special bonds in more than a year in Aug. This is after the central government set a Sep deadline for regionals to issue their remaining allocation for the year (a total of CNY3.8trn quota for 2023). Thereafter, there could be also be a boost in debt supply from Oct. Bond issuance are estimated to be around CNY520bn for Aug and are mainly used to finance infrastructure projects.

- Yuan has been supported by the PBoC via the daily USDCNY reference rate fixes (persistently 900pips lower than market estimates), cross-border financing parameter adjustments, a fair extent of jawboning as well as tighter CNH liquidity. **The recent recovery of the yuan was both a reflection of peak pessimism and the efforts from the authorities to defend the RMB.** 1W CNH forward implied yield remains somewhat elevated around 3.18% (as of 31 Aug), off its high of 7.48% seen on 21 Aug. Looking back in history, 1W CNH forward implied yield rose to a high of almost 17% and hit 51.7% in Sep 2016. Into Sep, liquidity demand could increase for tax repayments and that could mean this tight liquidity condition is more likely to sustain for a while.
- Ratio of FX settlement by bank customers to foreign-related FX Receipts was 63.7% in Jul, a drop of around 6ppt from levels recorded in the month prior. Ratio of FX Sales to foreign-related FX payments was also 2ppt lower in Jul at 67.0% compared to a month ago. This underscores the unwillingness of exporters to convert their forex receipts in Jul. Corporates have also reduced the amount of forex sales as holding yuan becomes less appealing.
- **Growth and Inflation Outlook:**
  - Our economist downgraded GDP forecast to 4.6% for 2023 from 5% seen previously. That would be well below the growth target set at the Two Sessions by the NPC. Three key risks were pencilled in by our economist and that is the property spiral which is the

negative feedback loop between property sector, financial system and real economy. The second key risk is further deterioration in private investment. The third is the problem with labour market weakness – the youth (age 16-24) refusing to seek employment and the enforcement of salary limitations that could weigh on private consumption.

- China's July activity data confirms that the economy is weakening on all fronts. Industrial production slowed to 3.7%y/y for Jul vs. previous 4.4%. Retail sales decelerated to just 2.5%y/y from previous 3.1%.FAI ex rural for Jan-Jul slowed to 3.4%y/y vs. 3.8%y/y seen for Jan-Jun. Residential property sales for the first seven months slowed to a growth 0.7%y/y from 3.7% seen in 1H 2023. Property investment Ytd also declined by a sharper -8.5%y/y from previous -7.9%.
- There could be modest signs of economic stabilization into 4Q as the cut for interest rates of existing mortgage should raise disposable income slightly and reduce mortgage repayment pressure. Easing of criteria to become a first-time home buyer could also support the property sector but the extent of support is uncertain due to the broader lack of confidence in the economy.

- **Monetary Policy Forecast:**
- PBoC cut 1Y MLF ny 15bps from 2.65% to 2.50% on 15 Aug and provided CNY401bn yuan via the facility. It also cut 7-day reverse repo rate by 10bps to 1.80% the same day from 1.90% previously, providing CNY204bn of funds via the reverse repo. The last time PBoC cut both rates was in Jun and that had failed to support credit growth.
- The 5Y loan prime rate was kept unchanged at 4.20% on 20 Aug but 1Y was cut to 3.45% from previous 3.45%. The lack of transmission to the 5Y LPR was surprising but we reckon that a cut could be a matter of time. Towards the end of Aug, a directive was said to be given to SOE banks to cut interest rates on the majority of the nation's CNY38.6trn of existing mortgages. The reductions will only affect loans on first homes. In order to ease the pressure on the NIMs, *interest rates for yuan deposits could be cut between 5-20bps across tenors and could be announced as soon as 1 Sep.* Apart from allowing existing mortgage owners to benefit from rate cuts, this would also reduce the mortgage repayment pressure and Chinese banks would also be more keen to lower the 5Y LPR to be reduced in Sep.
- **Latest Fiscal and External Balance Outlook:** The MOF pledged to prevent and resolve the local government debt risks and strengthen its fiscal discipline. The Finance Ministry will ramp up and implement active fiscal policies and hasten the transfer of payments to localities. In a separate report to the NPC Standing Committee that day, the NDRC urged local government to accelerate issuance and utilization of special bonds. External balance could remain in surplus given weak domestic demand. Imports remained in decline, alongside contractions in exports.
- **Key domestic events and issues to watch:** Aug Caixin PMI [1 Sep]; Aug Caixin Services PMI [5 Sep]; Aug foreign reserves, trade [7 Sep]; Aug CPI, PPI [9 Sep]; Aug credit data [9-15 Sep]; 1Y MLF [15 Sep]; Aug IP, retail sales, FAI [15 Sep]; 1Y,5Y LPR [20 Sep]; Aug industrial profits [27

Sep], Caixing Mfg, Services PMI [29 Sep]; Sep NBS Mfg, Non-Mfg PMI [30 Sep].

- **Technical Analysis:** USDCNH is last seen within the 7.27-7.35 range. Momentum bias is increasingly bearish. Break of the 7.2730-support to open the way towards 7.2330. Resistance at 7.3750.

SGD: Challenging Headwinds Ahead

Forecast	3Q 2023	4Q 2023	1Q 2024	2Q 2024
USDSGD	**1.3500** (1.3350)	**1.3400** (1.3250)	**1.3250** (--)	**1.3150** (--)

Previous Forecasts in Parentheses

- **Motivation for the FX View: We raise our USDSGD forecasts for 3Q23 and 4Q23 to factor in potential upward pressure on the pair as US yields remain higher for longer and as the USDCNY moves higher and drags Asian currencies along.** The SGDNEER has remained firm above the mid-point of the policy band although it has come off from earlier highs seen around the 1.90% to 2.00% levels. The SGD should be somewhat better sheltered than other Asian currencies in an environment of high US yields, given the correlation of SG rates to US rates due to the lack of an interest rate policy. Our assessment is that MAS is likely to stand pat in October, and the continued appreciating stance (assumed to be +1.5% p.a.) in the SGDNEER should provide plenty of support for the SGD and result over time in a lower USDSGD.

- On 14 April, MAS stood pat and left policy settings (slope, centre and width) unchanged. This is the first stand pat after a series of five tightening moves that began in October 2021. This decision goes against our expectations for a tightening via a re-centre upwards, given that core inflation remained well above MAS' comfort levels. In our view, this was largely due to MAS' inflation outlook being more sanguine and expectations for growth being more pessimistic than we had expected.

- The trajectory for a lower USDSGD remains intact although it could take a longer time to come to fruition. While MAS stood pat, the current policy stance still implies a +1.5% appreciation in the SGDNEER against its trade-weighted constituents, which will also provide support for the SGD against the USD. Given that Singapore's robust macroeconomic fundamentals such as a persistent current account surplus, strong governing institutions and pro-growth policies remain intact and are fundamentally unchanged, we remain convicted on our positive medium-term view on the SGD.

- The fundamentals for the SGD have not materially changed – robust macro fundamentals in Singapore such as ample fiscal space, current account surpluses, healthy labour market and political stability etc. will continue to impart SGD some "safe-haven" appeal, which is likely to be reflected in SGD resilience in the future. Indeed since 14 Apr, the SGD continues to display signs of resilience against most other currencies on both a bilateral and trade-weighted basis.

- **Risks to our View:** There is a chance that global growth prospects could deteriorate further and that China's anticipated reopening effects do not live up to expectations. In such a scenario, it would be difficult for Singapore as a small country that is highly dependent on trade to escape a recession. We would therefore expect that in such a scenario, the SGD could underperform, and any SGD weakness could be further exacerbated should MAS decide to support growth by easing the current appreciating policy stance via moving to a zero appreciation path. For now this is not our baseline scenario and we do not expect MAS to ease to move to a zero appreciation path in a sudden move and expect easing, if any, to be gradual and measured.

- **Growth and Inflation Outlook:** On growth, 2Q2023 final GDP showed that the Singapore economy grew by +0.1% SA QoQ (exp: 0.4%; prev: -0.3%) and by +0.5% YoY (exp: 0.8%; prev: 0.7%), narrowly avoiding a technical recession, but missing the earlier advance estimates. MTI has lowered the growth forecast to 0.5% to 1.5% (prev: 0.5% to 2.5%) in 2023, showing that challenging headwinds lie ahead for Singapore, especially as China languishes. Our economists maintain their full-year GDP growth forecast at +0.8% YoY, which is at the lower end of MTI's forecast range. Manufacturing is expected to remain tepid in 2H2023 due to weak external demand and services may remain supported by consumer-facing segments with the tourism recovery.

- On inflation, MAS lowered its forecasts for both core CPI (2.5% to 3.0% YoY; prev: 2.5% to 3.5%) and headline CPI (4.5% to 5.5% YoY; prev: 5.5% to 6.5% YoY). MAS recognized both upside and downside risks exist to inflation and central bank chief Ravi Menon has said that the central bank will not pivot to a growth supportive stance as it remains vigilant of the risks that upside shocks to inflation could cause price pressures to be more persistent than expected, even as the forecasts for inflation are lowered.

- July headline CPI came out at 4.1% YoY (est. 4.2% YoY and Jun. 4.5% YoY) whilst the core number was at 3.8% YoY (est. 3.8% YoY and Jun. 4.2% YoY).

- **Monetary Policy Forecast:** The poorer than expected growth outlook and the balance of risks skewed to easing of inflationary pressures likely influenced MAS' decision to stand pat rather than to tighten further. We note that MAS used "sufficiently tight" to describe the current policy stance in addition to their usual use of the word "appropriate". We think this could be a possible hint to their policy leaning in October. **Given the current outlook for growth and inflation, we think it is likely that MAS will be biased towards a stand pat in Oct as long as MAS' core inflation is on their projected trajectory.** However, we would not rule out a tightening in Oct should MAS' core inflation projections change materially if upside imported inflation risks materialize. The base case for MAS to stand pat however, remains intact.

- This latest decision was in line with the narrative that the Fed and other central banks around the world are coming to an end of the tightening cycle. Should global inflation trends indeed show a significant deceleration in core inflation prices, we then think that the case for MAS standing pat in Oct should further strengthen. However, we also note that MAS highlighted upside risks to inflation and specifically cited commodity price shocks. Thus far the earlier OPEC surprise production cut has resulted in a somewhat sustained increase in oil prices. We need to monitor this space as any easing in energy prices could provide some support for the MAS narrative that inflation will come off later into the year. We would like to highlight that core inflation prints in many advanced economies in the world remain elevated and persistent despite a moderation in headline inflation and our economists are not as certain that MAS' core inflation, which is slightly different in that it excludes accommodation and private transport and as such includes energy, will come off later in 2023.

- **Latest Fiscal Outlook:** Budget 2023 came out in Feb and mainly provided more social support amid rising costs of living and the hike in GST. A deficit is still expected albeit at a relatively low level of 0.1% of GDP or SGD0.4bn.

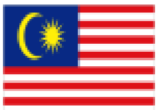
- A large SGD3bn top-up was done for the GST Assurance Package (AP) to SGD9.6bn. This is in light of the likelihood that a 2% GST hike would raise about SGD3.5bn annually. Cash payouts of various sorts were adjusted or introduced including an increase in the cash component of the AP by between SGD300 and SGD650, CVC vouchers to be raised SGD100 to SGD300 in 2024, etc. The permanent GST voucher (GSTV) scheme for eligible Singaporeans was also raised, which brings total spending for this to SGD1.7bn from 2024 onwards. In addition to all this, the Enterprise Financing Scheme, which include the 70% government risk-share for trade loans and support for domestic construction projects via project loans, will be extended for another year until end March 2024.

- On the revenue side, Singapore is looking to implement the Pillar 2-global minimum tax from 2025, via introduction of a Domestic Top-Up Tax, which will top up the MNE groups' effective tax rate in Singapore to 15%. This part of a broader international movement by other countries including the EU, UK and Switzerland to implement Pillar 2 in phrases starting from 2024.

- The FY2022 deficit meanwhile was smaller than projected at 0.3% of GDP or SGD2bn (vs initial projections of 0.5% of GDP or SGD3bn). Draw on reserves was also lower than initial estimations at SGD3.1bn (vs expectations of SGD6bn). The overall drawdown from past reserves from FY2020 to FY2022 totaled SGD40bn, much less than the initial SGD52bn sought by the government for the President's agreement. As a whole, there was little to note for the SGD from the FY2023 budget, given that Singapore's overall fiscal health remains sound and it does not need to borrow to spend.

- **External Balance Outlook:** NODX fell at a steeper pace in Jul in its 10th straight month of decline as contraction of exports to China and the EU overshadowed a rebound in US-bound exports. NODX fell -20.2% YoY (exp: 14.3%; prev: 15.6%). Electronics exports fell -26.0% (prev: -16.0%). Trade releases remain reflective of the moderation in global demand and the challenging headwinds ahead for Singapore. Our economists revised their 2023 NODX forecast to -12% to -9% (prev: -9% to -6%; Jan to Jul: -15.6%). Earlier hopes for a China reopening boost is giving way to the risk of a China deflationary shock. Singapore's Current Account balance for 2Q2023 is at 18.11% of GDP (1Q2023: 18.49%). Singapore's current account has remained in a structural surplus and short term (quarterly) fluctuations are not expected to have a material impact on the SGD.

- **Key domestic events and issues to watch in Sep:** Aug PMI/ESI (2 Sep), Aug S&P PMI, Jul Retail Sales (5 Sep), COE Bidding (6 Sep), Foreign Reserves (7 Sep), Aug NODX/Electronics Exports (18 Sep), COE Bidding (20 Sep), Aug CPI (25 Sep), Aug Industrial Production (26 Sep), Aug Money Supply (29 Sep).
- **Technical Outlook:** Pair was last seen at around 1.3512. Resistance is at 1.3600 and 1.3762. Support is at 1.3401 and 1.3300.



MYR: Facing Fed policy and China growth headwinds

Forecast	3Q 2023	4Q 2023	1Q 2024	2Q 2024
USDMYR	**4.60** (--)	**4.55** (4.50)	**4.45** (4.35)	**4.35** (4.20)

Previous Forecasts in Parentheses

- **Motivation for the FX View:** We keep our MYR forecasts largely unchanged except for a slight revision to the forecasts from 4Q 2023 onwards to reflect recent market developments as well as a slight delay in the China recovery and factoring in "high or higher" for longer US policy rates which had kept the USD more elevated for longer into end 2023. The recent CNY support on the back of China market interventions and targeted stimulus related factors has helped support regional currencies including the MYR in July but China growth concerns has weighed down regional currencies including MYR in Aug.
- Nonetheless, recent China efforts to support the economy and lift animal spirits have helped keep CNY and regional currencies supported. CNH 1W forward implied yield has risen and sustained a tight liquidity condition to discourage USD-CNH carry trades. Other measures out of China to support animal spirits include banks limiting investment outflows via Bond Connect (Reuters) and the expectations that banks may reduce rates on existing mortgages and deposits. These measures and possibly other stimulus measures to support the property sector may emerge towards end 2023. These may have some positive impact on CNY and potentially regional currencies including the MYR as the

impact is felt via an eventual turnaround in the Chinese economy and financial sector.

- Recent upward momentum in global commodity prices (i.e. crude oil & palm oil) continues due to signs the market is tightening, with estimates that crude demand is running at a record clip just as OPEC+ cuts back production. West Texas Intermediate has held above $80 a barrel by late Aug.

- The results of the state elections in mid Aug was in line with our economists baseline scenario or assumption is that the outcome of these state elections will broadly mirror the results of the Parliament seats contested in these states at the 15th General Election back in Nov 2022 i.e. PH/BN will keep the multiracial states Selangor, Penang and Negri Sembilan while PN/PAS will retain the Malay heartland/belt states of Kedah, Kelantan and Terengganu. What is more – and most - important is that after the conclusion of the state elections, the PM, his Cabinet and the Federal Government is able to focus on policy making and implementation of economic and institutional reforms given that there is over four years to go before the next general election.

- 2Q 2023 current account (CA) surplus rose to +MYR9.1b or +2.1% of GDP (1Q 2023: +MYR4.3b or +1.0% of GDP), supported by continued surplus in the goods trade account and smaller deficits in services, primary and secondary income accounts. Our full year 2023 CA surplus outlook as % of GDP stays at 2.4% but the value is cut to +MYR43b from +MYR47b (1H 2023: +MYR13.4b or +1.5% of GDP; 2022: +MYR55.1b or +3.1% of GDP) following our revision in 2023 real GDP growth forecast to +4.0% from +4.5%.

- Financial account posted bigger net outflows (2Q 2023: -MYR11.6b; 1Q 2023: -MYR2.4b), mainly on net outflows in other investments (2Q 2023: - MYR15.1b; 1Q 2023: +MYR20.9b) and smaller net inflows in direct investment (2Q 2023: +MYR4.9b; 1Q 2023: +MYR10.9b) despite the portfolio investment net inflows (2Q 2023: +MYR8.1b; 1Q 2023: -MYR33.3b). The net outflows in other investment was driven mainly by repayment of residents' interbank borrowing while the net inflows in portfolio investment was attributed to non-residents' acquisition of domestic debt securities.

- The global situation which looks unfavourable over the past 1H 2023 are not expected to keep persisting until year end as had panned out recently. The Fed could also eventually soften its stance closer towards year-end as inflation gradually falls. China we believe would show more discernible level of recovery over the tail end of 2023 and we factor in some significant level of targeted stimulus to help the economy and that should give a boost to commodities' prices eventually. Domestically, the conclusion of the state elections and status quo results - lend credence to somewhat extended stability of the current government. This could potentially see positive effects on both cold (FDI) and hot (equity+ bond) portfolio flows and coupled with the scenario of an eventual Fed pause and softer USD expectatons may lead exporters to further sell their USD holdings from export proceeds. All these are possible scenarios which may materialize in the latter part of 2H 2023 and we are already factoring it into our MYR forecasts.

- We are also mindful of risks that could result in our expectations not panning out. This include US data staying strong for too long with inflationary pressure concerns emerging again and China's consumption failing to pick-up. These risks will need to be priced in a bit into our forecasts, however, but for now, we remain confident that these risks would not materialize at a significant level.

- Growth and Inflation Outlook: Factoring 1H 2023 GDP growth of +4.2%, another round of high base effect on 3Q 2023 GDP (i.e. +14.4% YoY in 3Q 2022 vs +8.8% YoY in 3Q 2022), and the impact of slower global economic growth (2023E: +2.7%; 2022: +3.5%) on external trade, our 2023 real GDP growth forecast is revised back to our original +4.0% from +4.5%, which was raised in May 2023 after 1Q 2023 GDP release amid China re-opening "euphoria" that has now "soured". Signaling prospect of subdued % YoY GDP growth in 3Q 2023, July data showed declines in manufacturing purchasing managers index, signaling lacklustre manufacturing output, plus weakness in exports (July 2023: -13.1% YoY; June 2023: -14.1% YoY; 2Q 2023: -11.1% YoY) and imports (July 2023: -15.9% YoY; June 2023: -18.7% YoY; 2Q 2023: -11.5% YoY). Meanwhile, CPO output - agriculture GDP proxy - rebounded (July 2023: +2.3% YoY; June 2023: -6.3% YoY; 2Q 2023: -3.1% YoY).

- Limiting the downside to 2H 2023 - and thus full-year - GDP growth include the on-going tourism recovery and the positive investment growth momentum as the surge in approved private sector investment since 2021 is translating into rising actual/realised private investment plus progress in the on-going major infrastructure projects. There will also be larger Government deficit spending in 2H 2023 after it shank to MYR39.7b in 1H 2022 vs MYR45b in 1H 2022, given 2023 budget deficit of MYR93.9b.

- July 2023 saw further declines in exports to -13.1% (June 2023: -14.1% YoY) and imports to -15.9% (June 2023: -18.7% YoY) resulting in lower trade surplus (July 2023: +RM17.1b; June 2023: +RM25.5b). Currently, we expect full-year exports and imports to decline by -2.0% (7M2023: -5.9% YoY; 2022: +24.9%) and -0.5% (7M2023: -6.5% YoY; 2022: +31.0%) respectively with trade surplus of +MYR231b (7M2023: +MYR135.4b; 2022: +MYR256.2b).

- Headline inflation rate eased further to +2.0% YoY in Jul 2023 (Jun 2023: +2.4% YoY; MIBG estimate: +2.2% YoY; 7M2023: +3.0% YoY; 2022: +3.3%). Core inflation also eased to +2.8% YoY (Jun 2023: +3.1% YoY; 7M2023: +3.5% YoY; 2022: +3.0%). Keep our 2023 inflation rate forecast of +3.0% for now, as monthly inflation stays sub-3% for the rest of this year, mainly on base effect, while mindful of upside surprises from food prices due to the El Nino weather phenomenon.

- Inflation risk remains biased to the upside amid the fluid policy on price subsidies and controls. The Government has started to implement targeted subsidies, beginning with electricity at the start of this year whereby subsidy is given only to domestic (household) and lowvoltage users vs non-domestic (industrial, commercial) and medium/high voltage users. This was followed by the exclusion of very high-income households from electricity subsidies at the start of 2H2023 i.e. those with monthly electricity consumption excess of 1,500kWh. Next is the implementation of targeted fuel subsidy, potentially next year that will also end the "benefits" to the high-income households. At the same time, we are mindful of El-Nino-related food inflation risks. This is as rice prices is on upward trend, rising +2.4% YoY in July 2023 (Jun 2023: +1.4% YoY) and +0.9% MoM (Jun 2023: +0.3% MoM). This is attributed to global shortage in rice supply following adverse weather conditions, panic buying due to El-Nino and India's decision to ban rice exports.

- **Monetary Policy Forecast:** Following the decision by the BNM's Monetary Policy Committee (MPC) meeting on 5-6 July 2023 to keep the Overnight Policy Rate (OPR) at 3.00%, we expect OPR to stay at this "slightly accommodative" level - as per BNM's description – for the rest of the year, with expectations of continued moderation in inflation. BNM also removed the assessment that "inflation risk is tilted to the upside", as well as its full-year inflation rate forecast range of 2.8%-3.8% that suggest forecast review is underway with the likelihood of the number now coming in at the lower end/half of that forecast range. This is based on four takeaways from BNM's latest Monetary Policy Statement (MPS) issued after the above-mentioned MPC i.e.

- Cautious global economic outlook as BNM changed its view on China, acknowledging "slowing recovery post-economic re-opening in recent months" vs "stronger-than-expected rebound" in the previous MPS in May 2023, while the MPS line on the downside risks to global economic outlook now adds "slower major economies".

- Constructive domestic economic outlook. Domestic economic growth slowed in recent months as exports are dragged by slower external demand. But for the remainder of this year, the economy will be driven by resilient domestic demand, as favourable labour market conditions – especially in the domesticoriented sectors – underpinned consumer spending, plus rebounds in tourist arrivals, thus tourism-related activities, on top of progress in multi-year infrastructure projects supporting investment activity.

- Expectations of continued moderation in inflation in 2H 2023 after the downtrend so far this year. In particular, BNM removed the assessment that "inflation risk is tilted to the upside", as well as its full-year inflation rate forecast range of 2.8%-3.8% that suggest forecast review is underway with the likelihood of the number now coming in at the lower end/half of that forecast range.

- MPS also added that BNM's MPC sees limited risk of future financial imbalances, compared with previous statement about the need to ensure monetary policy stance is appropriate to prevent the risk of future financial imbalances. Assuming the "financial imbalances risk" refers to the Ringgit situation and amid the outlook of further US Fed's interest rate hikes, we view that BNM feels its recent statement (by the Financial Market Committee or FMC on 27 June 2023) on Ringgit and FX market intervention is sufficient and effective in stabilising Ringgit i.e. not reaching and breaching 4.70 vs USD.

- **Fiscal Outlook:** To recap, MADANI Economy targets budget deficit to GDP ratio of 3% or less over the next 10 years. MoF SecGen reiterated this year's budget deficit forecast of 5% of GDP and the targets of 4.1% in 2024 and 3.2% in 2025 based on the Medium-Term Fiscal Framework as per the retabled Budget 2023 (27 Feb 2023) i.e. no slowing in fiscal consolidation next few years. The "3% or less over the next 10 year" target reflects a desired level for sustainable budget deficit, thus government debt and debt servicing, plus the government still need to spend and invest, especially in relation to "raising the floor" for the people e.g. universal access to public infrastructure and services (transport, education, healthcare); social protections. Meanwhile, "goodies" announced during the launch of MADANI Economy (e.g. MYR300 to 1.3m civil servants and MYR200 to 1m pensioners; MYR100 e-wallet credit to 10m people in the B40-M40 category) are funded mainly by savings from cancelling and/or tendering projects previously awarded under direct negotiations. MoF SecGen also touched on Fiscal Responsibility Act (FRA) to be tabled by year-end. Among others - and in line with other countries' FRAs - there will be fiscal charter that set goals on fiscal deficit, debt level and servicing, as well as government guarantees and committed liabilities, and MoF is answerable to the Parliament for deviations from the goals.

- **External Balance Outlook:** July 2023 saw further declines in exports to -13.1% (June 2023: -14.1% YoY) and imports to -15.9% (June 2023: -18.7% YoY) resulting in lower trade surplus (July 2023: +RM17.1b; June 2023: +RM25.5b). Currently, we expect full-year exports and imports to decline by -2.0% (7M2023: -5.9% YoY; 2022: +24.9%) and -0.5% (7M2023: -6.5% YoY; 2022: +31.0%) respectively with trade surplus of +MYR231b (7M2023: +MYR135.4b; 2022: +MYR256.2b).

- **Key domestic events and issues to watch:** S&P Global PMI MFG (1 Sep), Aug Foreign reserves (7 and 22 Sep), Jul Manufacturing sales, Jul IP (11 Sep), June Trade data (19 Sep) and Aug CPI (22 Sep).

- **Technical Outlook:** Pair was last seen at around 4.6385. Resistance is at 4.6600 and 4.6980. Support is at 4.6109 and 4.5612.

IDR: Expect Longer Period of Weakness

Forecast	3Q 2023	4Q 2023	1Q 2024	2Q 2024
USDIDR	**15,200** (15,000)	**15,000** (14,900)	**15,000** (14,700)	**14,700** (14,600)

Previous Forecasts in Parentheses

- **Motivation for the FX View:** We have revised our USDIDR forecast slightly higher as we now see the pair is likely to remain at relatively high levels in the next 9 months with only a discernible downward move to come in 2Q 2024. Two factors are likely to lead to result in such a condition for the next 9 months which are 1) Fed rates staying high and 2) political uncertainty arising from the upcoming Feb 2024 presidential elections. The possibility that the Fed could pause and keep a hawkish tilt for the rest of 2023 may keep foreign investors generally at bay still, which limits the inflows into Indo GBs and result in only small downward moves in the USDIDR till end 2023. There could be some expectations of a Fed softening emerging in markets during 1Q 2024 but the IDR is unlikely to get much relief as the presidential elections around that time may lead investors to adopt a "wait and see" approach and again limit inflows into Indo GBs. Only once the dust has settled politically in 2Q 2024 and the Fed then starts to cut, we would likely see stronger inflows into Indo GBs, leading the pair much lower.

- **Growth and Inflation Outlook:** 2Q GDP accelerated to the fatest pace in three quarters at 5.17% YoY (est. 5.00% YoY and 1Q. 5.03% YoY) on the back of stronger domestic consumption and investment, which in turn offset lower net exports. The latter was due mainly to lower prices for many of Indonesia's key commodity exports that include palm oil and coal. There was also notably broad-based improvement across most of the sectors. Going forward, our economists continue to maintain that growth should come out at 5% for 2023 as steady domestic demand cushions the softer demand from China and other external markets. Regardless, even so domestic demand would also ebb, which could be reflected in the already slowing credit growth.

- July headline inflation continued the downward trend as it surprised below expectations at 3.08% YoY (est. 3.10% YoY and Jun. 3.52% YoY) and moving closer to the middle of BI's range at 1.5% - 3.5%. This came on top of a deceleration in food costs (due to the high base last year), transportation costs and housing and utilities. Core inflation also eased further to 2.43% YoY (est. 2.52% YoY and Jun. 2.58% YoY). Our in-house economists expect that inflation could soften further in the final months as they see it averaging 2.7% for Aug – Dec. This would be a result of transport cost and housing and utilities continuing to ease. The former would be due to the effect of the +30% hike in subsidized fuel price fading whilst the latter would be driven by favorable base effects. At the same time, food inflation may start to climb due to the effect of El Nino and a wearing off of the base effects.

- Retail sales in July hit a five month low. Consumer confidence meanwhile was the lowest since March at 123.5 (Jun. 127.1). BI had attributed the declining demand to the end of June school holidays and Ramadhan-Idul Fitri holiday season. Regardless, the numbers are still robust reflecting that consumption can hold up and support the economy.

- **Monetary Policy Forecast:** BI again held rates at 5.75% as expected at their August meeting as they continued to try to ensure IDR stability. The move comes even as Governor Perry Warjiyo actually expects the Fed to hike another 25bps in September. The economic case for the central bank at this point to hike again though is weakening as inflation is now within their target range and continues to ease. This therefore can explain the central bank looking unwilling to move rates any higher to support the IDR even as they believe the Fed is keep going move again.

- Instead, Governor Perry Warjiyo has mentioned that BI can alternatively keep supporting the IDR through "Operation Twist" and bond market interventions. The central bank is also introducing a new short term instrument called the SRBI which uses SBN/government securities as the underlying and targeted at attracting 1) foreign portfolio inflows and 2) help banks manage their liquidity. The first goal looks clearly aimed at providing support to the currency if it is successful at achieving this. However, it is also interesting to note that there is a possibility this instrument could be aimed at also complementing or replacing operation twist given that BI could be facing limitations on the volume of short-term bonds they have available for sale.

- SRBI itself would be a short term discount instrument with tenor from 1 week to 12 months and replace reverse repo (RR). On the primary market, it can be purchased by banks but foreign investors can purchase it on the secondary market. The first auction would be done on 15 September with 6m, 9m and 12m on offer. Whether SBRI can be successful in attracting sufficient foreign inflows is difficult to gauge at this point. Foreign ownership in Indo GBs are still now high whilst there have been outflows from Indo bonds in August given the "higher for longer" concerns. Hence, we remain cautious in viewing whether this tool can be a success in supporting the currency.

- **Latest Fiscal Outlook:** The budget 2024 deficit target has been set at 2.3% of GDP on the assumption of 5.2% GDP growth and inflation forecasted at 2.8% in 2024. The government will be raising expenditure by 6%. They highlighted importance on food and energy security as they earmarked Rp108.8tn to maintain stable prices, increase farm output and develop the government's ongoing food estate program. This comes in the face of adverse weather conditions such as El Nino and rising global food protectionism that could lead to upside risks to inflation. They have also set aside 12.8% of the budget for infrastructure. Rp52tn would also allocated to increases civil services salaries and raise government pensions which could be seen as a measure to boost domestic consumption and support the economy. The overall deficit target itself is not dissimilar to the 2.28% set in 2023 and it is near the pre-pandemic levels. The IDR has been favored among the high yielders given the government's disciplined fiscal approach and the trade surplus. However, the shrinking trade surplus and the current account turning into deficit (talked about in the next section) could risk unravelling this favorability.

- **Latest External Balance Outlook:** The country resiliently maintained a trade surplus in Jul although it substantially narrowed to $1.3bn (est. $2.6bn and Jun. $3.5bn). This was a result of exports tanking by -18.03% YoY (est. 19.20% YoY and Jun. 21.20% YoY) and imports contracted much smaller than expected at -8.32% YoY (est. -15.29% YoY and Jun. -18.35% YoY). The former was due to the lower commodity prices compared to last year. However, interestingly, there is a possibility export volumes could have been quite resilient given that June volumes only saw a small decline. The ban on bauxite shipments also contributed to the fall in ore exports but it only made up a small part of overall exports. The government is reportedly also looking to ban quartz sand exports, which could have some impact. Meanwhile, on imports, the contraction was smaller than the prior month due to a rebound in consumer goods imports and a strengthening in capital goods imports. Despite the numbers in July, the country could continue to maintain a trade surplus for the rest of the year. However, we note the risk of a shrinking trade surplus would weigh on the currency.

- The country's current account (CA) in 2Q 2023 turned into a deficit at -0.5% of GDP for the first time since 2021. This came on top of weaker commodity pieces compared to last year and a softer global trade environment. For now, the country is only expected to report a narrow CA deficit of -0.2% of GDP in 2023 but we note of the risk of this being wider especially going into next year, which could be a negative for the currency.

- Foreign reserves remained steady at $137.70bn (Jun. $137.5bn) in July. The IDR had actually strengthened in July and that had probably allowed for less of the reserves to be utilized. However, with the IDR weakening in August, there is a possibility that the level of reserves could have declined. Therefore, the downtrend is unlikely to have turned in July and looks still intact.

- Indonesia experienced net outflows month to date as of 23 Aug 2023 of -$0.49bn, which is a turnaround of inflows from the last two months of inflows. It was also the highest level of outflow since Feb 2023. The outflow looks to have been driven by the "higher for longer" concerns of Fed rates. Additionally, the quick softening in inflation to within BI's target range, closer to the midpoint and the weakening in credit growth could be creating anxiety that BI looks under greater pressure to cut sooner than the Fed can pivot. Whilst we do not think that scenario would play out, fears related to it could be weighing on appetite for Indo GBs. We expect the rest of this year to see months of either outflows or close to little net change given that it is difficult to see how foreign investors would want to position strongly into Indo GBs before end 2023 if the Fed keeps a hawkish tilt and expresses an intend to hold for quite a while. High funding costs with uncertainty on when the pivot would come would also be a disincentive for foreign investors to buy into Indo GBs. Overall, the unfavorable bond flows situation would a major factor that would keep the currency at weak levels until year end.

- Meanwhile, there was a large equity outflow month to date as of 29 August 2023 at -$1.2bn. This was the highest amount seen since December 2022 and it was a reflection of the fall we have been seeing in equity markets globally. The weakness we have seen in global equity markets looked to have also been driven by the "higher for longer" concerns of Fed Rates. As a note, August is the summer month too where trading volumes in major equity markets such as the US can be lighter and hence, prices weaker. Therefore, it is also difficult to read too much into price action in global equity markets for this period and there could potentially be a turnaround in the coming months.

- FDI for 2Q 2023 was at $4.9bn (1Q 2023. $5.1bn) and was roughly at similar levels as the same time last year, being only -1.1% less. We stay wary that FDI could slow in the coming months building up to the general elections in Feb 2024 and investors adopt a wait-and-see approach. The risk of lower inflows from this angle also supports our thesis that the IDR could remain at weak levels for the 6-9 month horizon.

- **Key domestic events and issues to watch**: Aug S&P Global PMI mfg (1 Sept), Aug CPI (1 Sept), Aug foreign reserves (1 Sept), Aug consumer confidence (8 Sept), Aug trade data (15 Sept), Aug local auto sales (15 - 21 Sept) and BI policy decision (21 Sept).

- **Technical Outlook:** Pair was last seen at around 15230. Momentum indicators are pointing to downside. Resistance is at 15542. Support is at 15156 and 15014.

PHP: Strength Limited Amid Twin Deficit

Forecast	3Q 2023	4Q 2023	1Q 2024	2Q 2024
USDPHP	**56.00** (55.50)	**56.00** (55.00)	**55.50** (54.50)	**54.00** (53.00)

Previous Forecasts in Parentheses

- **Motivation for the FX View:** We revise our forecasts for the USDPHP higher over the next 12 months on the basis that elevated levels of UST yields may only gradually come off more substantially in 1H 2024. The pair is likely to maintain a flat profile for the rest of this year as the Fed likely stays on hold and keeps a hawkish tilt with US inflation only on a gradual downward path. There could be a slight downward move in USDPHP in 1Q 2024 as markets begin to anticipate more of the possibility of a Fed pivot but with cuts likely in 1H 2024, leading to stronger downward moves in the USDPHP then. Meanwhile, on the domestic front, although growth has been falling off, inflation at the same time still remains high which is likely to keep the BSP holding for the rest of 2023 and possibly in 1H 2024. This should at least give support to the PHP limiting any upside gains for the USDPHP from current levels.

- **Growth and Inflation Outlook:** 2Q GDP growth fell off substantially and well below expectations at 4.3% YoY (est. 6.0% YoY and 1Q. 6.4% YoY), which was due to easing domestic demand growth. It appears that the elevated levels of interest rates is started to weigh on the domestic demand, which had been a scenario that we feared playing out. A business outlook survey by the BSP itself showed that a higher number of respondents now cite that business is constrained by higher rates. The high interest rates could keep weighing on domestic demand going into the second half of 2023. Net external demand meanwhile did improve on top of a pick up in exports whilst imports stagnated. However, the global economic environment could see more slowdown amid higher Fed rates, which could hurt the external sector and weigh on growth. Our in-house economists are consequently revising the entire year forecast down to 5.2% from 5.5% in 2023.

- High frequency indicators such as the S&P Global Mfg PMI released in July was higher at 51.9 (June. 50.9). However, it is difficult to say that this represents any turnaround as it could just be one off and that the downward trend could keep persisting. With a weakening in the global goods trade environment, we are inclined to believe that the downward trend continues and that this would keep weighing on the economy.

- Headline inflation is also continuing to ease quite substantially with the Jul number coming in below expectations at 4.7% YoY (est. 4.9% YoY and Jun. 5.4% YoY). There was a broad based easing. Base effects supported slowdown for areas such as transport. Core inflation also eased quite a bit to 6.7% YoY (Jun. 7.4% YoY) although still quite elevated. Our in-house economists foresee that the headline number is likely on track to hit BSP's target range of 2.0% - 4.0% by 4Q 2023. Core inflation should also similarly keep cooling. They are maintaining their inflation forecast at 5.5% for 2023 although they also note upside risks that include the onset of El Nino affecting agricultural production and the PHP150 increase in nationwide daily minimum wage, raising demand.

- **Monetary Policy Forecast:** BSP held rates at 6.25% in their August meeting but at the same time they continue to retain quite a hawkish tilt as they stayed wary of upside inflation risks. Even though they expect headline inflation to hit its target range 2.00 – 4.00% by 4Q 2023, they still adjusted their inflation forecasts due to the impact of higher international oil prices. They now see 2023 inflation at 5.6% (prior. 5.4%) and 2024 at 3.3% (prior. 2.9%). They also stay wary of price pressure risks related to El Nino and the higher minimum wage adjustments. However, they stay cognizant of the weakening growth situation and the impact that the high interest rates are having on domestic demand. This looks to be limiting the space they have to raise rates further despite the still high inflation. For now, Governor Eli Remolona is ruling out any easing although Finance Secretary Diokno is confident they can cut rates in 1Q 2024. It is unlikely they would hike further the growth situation but a cut could still be much further down the road until both headline and core inflation has really cooled to the target range. Our in-house economists expect rates to stay unchanged for the rest of 2023.

- **Latest Fiscal Outlook:** June budget balance swung further into deficit at -PHP225.4bn (Apr. PHP122.2bn) as revenue shrank by -7.91% YoY whilst spending only was a bit lower compared to year back at -2.59% YoY. From Jan – June, the budget was in deficit was at PHP551.7bn, which is lower compared to the same period last year at PHP674.2bn (though that was a period when the economy was just barely emerging out of the pandemic). Fiscal pressures are likely to keep persisting amid an high budget spending, which in turn would be a factor that weighs on the PHP and limits its strengthening going forward.

- **External Balance Outlook:** June trade balance stayed in deficit albeit narrower at -$3.9bn (May. -$4.4bn). This came on top of the plunge in imports by -15.2% YoY amid lower commodity price compared to last year. Imports of consumer goods and capital goods were also flattish. Exports though grew but slower at 0.8% YoY (May. 1.9% YoY). Agriculture exports rebounded whilst electronic shipments continued to increase although exports of mineral products was in decline. Our in-house economists exports and imports to shrink in 2023 amid a subdued external trade environment. They see the full year 2023 trade deficit should come out at -$54.0bn.

- OFWR growth in June eased on a yearly basis to 2.1% YoY (May. 2.8% YoY) but it did rise 12.9% MoM and hit a year high of $2.81bn. The Department of Migrant Workers expects that 2023 OFW deployment should surpass pre-pandemic levels whilst at the same time, our in-house economists see that OFWR should grow by 3.0% YoY in 2023 to hit $33.5bn. Despite the risk of a slowdown in the global economy, our in-house economists continue to believe that repatriation should hold up as OFWR has proven to be resilience in the last two global downturns as OFW sustained their remittance to support their families during tough economic periods.

- Bonds saw foreign net outflow of -$0.65bn in the three months ended 30 June. This was a contrast to the net inflow of $0.45bn for the three months ended 31 May. Concerns about DM central banks not quite being done with hikes in June looked to have led to large outflows in June. We expect that outflows could have slowed in July or there could have been a slight net inflows following the big outflow in the prior month. However, we see that the outflow could have picked up in August again amid the “higher for longer” concerns of US rates. We expect the rest of this year to see months of either outflows or close to little net change given that it is difficult to see how foreign investors would want to position strongly into Philippines bonds before end 2023 if the Fed keeps a hawkish tilt and expresses an intend to hold for quite a while.

- Meanwhile, equities saw a net outflow of -$0.09bn as of 29 August 2023, which was a reflection of the weakness in the global equity markets. Going forward, although there would be volatility in the global equity markets given the continued uncertainty and the risks of corrections, we still expect equities around the world to trend up amid the increasing likelihood of an economic soft landing and an eventual end to the Fed rate tightening cycle. Hence, equity inflows whilst it may be choppy in coming months could still likely to overall be positive in 2H 2023 and give support to the PHP.

- FX defensive buffers was slightly better in July as foreign reserves marginally rose to $99.7bn (Jun. $99.4bn). The improvement came as the PHP saw quite some strengthening that month with the DXY pulling back. However, we expect that foreign reserves likely have fallen in August as the PHP came under negative pressure from higher UST yields and DXY strength. As a whole, we believe that foreign reserves should stay quite stable for the remainder of 2023 as the PHP should be flattish in both 3Q and 4Q 2023.

- **Key domestic events and issues to watch**: Aug S&P PMI mfg (1 Sept), Aug CPI (5 Sept), Aug foreign reserves (5 Sept), Jul unemployment data (8 Sept), Jul trade data (8 Sept), Jul OFWR (15 Sept), Aug BoP (19 Sept), BSP policy decision (21 Sept), Aug budget balance (26 Sept), Aug money supply (28- 30 Sept and Aug bank lending (29 Sept).

- **Technical Outlook**: Pair was last seen around 56.60. Resistance is at 57.21 and 58.07. Support is at 56.48 and 55.41.

THB: Bumpy Road

Forecast	3Q 2023	4Q 2023	1Q 2024	2Q 2024
USDTHB	**35.00** (33.75)	**34.75** (33.00)	**34.50** (32.50)	**33.50** (32.00)

Previous Forecasts in Parentheses

- **Motivation for the FX View:** We revise our USDTHB forecast upwards on the basis on the basis that elevated levels of UST yields may only gradually come off more substantially in 2Q 2024. The pair is likely to maintain a flat profile for the rest of this year as the Fed likely stays on hold and keeps a hawkish tilt with US inflation only on a gradual downward path. There could be a slight downward move in USDTHB in 1Q 2024 as markets begin to anticipate more of the possibility of a Fed pivot but with cuts likely in 2Q 2024, leading to stronger downward moves in the USDTHB then. Despite the pair eventually coming off under this scenario, the USDTHB is still going to be rather elevated due to some domestic risk. This includes the possibility of higher populist related spending by the new government that could lead to more bond supply and hurt appetite, weighing on the THB. However, we do note also that the more business friendly Pheu Thai led government could attract both more equity inflows and FDI flows that can help offset some of this negative effect.

- **Growth and Inflation Outlook:** 2Q GDP growth disappointed at 1.8% YoY (est. 3.0% YoY and 1Q 2.6% YoY) on top of a slump in public consumption and subdued exports growth due to weaknesses in China's economy. Investment also slowed amid the political uncertainty. Despite this, our in-house economists are optimistic that growth can pick up from here. With the appointment of the new PM Srettha Thavisin and the soon to be formed cabinet, political uncertainty should dissipate, and government spending and private investment should be pick up. Private consumption should also strengthen as the new government rolls out supportive measures that include cash handouts to the youth, raising the minimum wage and a household income guarantee of 20,000 baht. Regardless, our in-house economists have revised down the 2023 to 3.2% from 3.8% due to the more subdued first half expansion.

- July headline inflation picked up slightly to 0.38% YoY amid (June. 0.23% YoY) on a rebound in fuel prices although food price inflation continue to moderate. The core number also soften to 0.86% YoY (June. 1.32% YoY). This marked the third month in a row that inflation has fallen below the BOT's target range of 1-3%. Regardless, BOT's retains a hawkish rhetoric with upside risks of inflation in 2H 2023 especially with the continued return of tourists. Lower inflation is certainly helping real rates to be higher but on the other hand.

- **Monetary Policy Forecast:** The BOT raised rates at the August meeting by 25bps again to 2.25%. The decision to raise the rate was unanimous among the committee. The BOT noted a few reasons in their decision to undertake this hike which include narrowing slack in the economy, expected resurgence in inflation and the need to preserve policy space. They continue to see upside risks to inflation arising from El Nino and the possibility of the return of more tourists. However, our in-house economists do not expect the BOT to hike any further given the low inflation numbers and as other central banks pause and potentially ease next year. We expect that BoT will keep rates steady in 2024.

- Foreign reserves as of 18 Aug was at $214.5bn as it continued to fall with the THB coming under pressure from higher yields and the political uncertainty in addition to weaknesses in China's economy. We expect the foreign reserves to at least stabilize from here as UST yields retreat from stretch positions and the political situation stabilizes.

- **Latest Fiscal Outlook:** There appears to be some resolution to the political situation as a new Pheu Thai Prime Minister (PM) Srettha Thavisin has been appointed. He leads a coalition together with other conservative parties. A new cabinet is likely to be formed soon and Srettha may also become the finance minister. However, all eyes would be on the finalization of the state budget for the fiscal year starting 1st October. The country's fiscal is likely to come under pressure as the new government may adopt a number of populist measures that include providing a 10,000 baht to Thais aged 16 and over, ensuring household income guarantee of 20,000 baht per month in addition to subsidy measures. This looks set to put pressure on the bond market, risking outflows and weighing on the THB. The incoming government could also front-load a lot of its proposed policies and spending, which in turn would raise the amount of short-term cash requirements. On the flipside, the Pheu Thai led government is also perceived to be more business friendly and this could encourage more foreign investment and inflows into the equity markets, which would be a positive for the currency.

- **Latest External Balance Outlook:** July trade balance saw a narrower surplus at $0.3bn (Jun. $2.0bn) as both exports and imports contracted. The BOP CA balance though swung back into deficit at -$0.45bn (Jun. $1.4bn). The narrowing in the surplus of the goods trade may have led the CA balance into deficit but the underlying numbers also do highlight weakness in the global goods trade given the contraction in overall trade value. Services trade though is likely to pick up further with the return of tourists and give a bigger boost to Thailand's external position going forward. Resultantly, this would provide support for the THB.

- From a portfolio perspective, bonds saw a net outflow month to date as of 30 August 2023 at -$1.1bn, which was a reflection of both the political uncertainty can concerns regarding the "higher for longer" narrative of Fed rates. The net outflow was the first in six months. Despite some resolution to the political situation, we see a risk of net outflows persisting in the coming months given that the new government could pursue populist measures that could reduce foreign appetite for Thai bonds. Meanwhile, on equities, there continue to be net outflows month to data up to 30 August 2023 at -$0.3bn. This could be a reflection of the anxiety regarding the political situation and some weakness in global equity markets for the month. However, equity inflows should pick-up with the formation of a more business friendly led Pheu Thai government.

- **FDI performance would continue to be watch closely in 2023.** FDI for 1Q 2023 was at $2.0bn (4Q 2022. $1.5bn). It is challenging to see if FDI can pick up more strongly this year given Thailand has been facing increasing competition for neighboring peers for FDI with the country manufacturing wages being the second highest in ASEAN after Malaysia. However, we do not rule out FDI picking up into the future given the formation of a more business friendly Pheu Thai led government.
- **Key domestic events and issues to watch**: Aug S&P Global PMI mfg (1 Sept), Aug business sentiment index (1 Sept), Aug CPI (5 Sept), Aug consumer confidence (7 – 13 Sept), Aug car sales (18 – 24 Sept), Aug customs trade data (23 – 28 Sept), Aug ISIC mfg production index (26 – 29 Sept), Aug ISIC capacity utilization (26 – 30 Sept), BOT policy decision (27 Sept), Aug trade data (29 Sept) and Aug BoP overall/CA balance (29 Sept).
- **Technical Outlook:** Pair was last seen around 35.00. Support is at 34.56 (200-dma), 33.59 and 33.00. Resistance is at 35.71 (2023 high) AND 36.21.

VND: Pressured by US rates

Forecast	3Q 2023	4Q 2023	1Q 2024	2Q 2024
USDVND	23,800	23,800	23,500	23,500
	(23,500)	(23,400)	(23,300)	(23,200)

Previous Forecasts in Parenthesis

- Motivation for the FX View: We keep the USDVND forecasts trajectory unchanged but adjusted the level as the unexpected resilience of the US economy fanned the UST and USD a tad higher. The persistent rise of the UST yields and USD strength have spurred the USDVND higher. At home, equity markets corrected this month but HCM Index had started to recover into the end of Aug. Portfolio flows were rather volatile with USD110mn outflow recorded between 1-25 Aug.
- On the other hand, FDI inflows remains healthy with average pace of around $1.6bn realized FDIs seen for the first eight months this year, cushioning the VND. While USDVND might seem pretty elevated now and there could even be more risks of upside should US economic resilience continue to surprise us, our base case scenario is still for an eventual slowdown for the US and for most central banks (including the Fed) to end their respective tightening cycles. Potential for a gradual China recovery, release of key electronic products may even generate an export recovery for Vietnam into the 4Q of the year and that is positive for VND.

- **Growth and Inflation Outlook:** Our economist looks for 3Q forecast to pick up to around 4.5-5% from 4.1% recorded in 2Q on better industrial production, resilient retail sales and upbeat public investment. Mfg PMI improved to 48.7 for Jul from previous 46.2. Our economist is also optimistic on export recovery as global electronic demand stabilize as well as the low base. Taken together, there is upside risks to the 2023 GDP forecast of 4%.

- Inflation rose to 3% in Aug from 2.1% in Jul, recording a 09%m/m vs. a month ago. Stronger headline was mainly driven by slower transport deflation (-0.3%), firmer transport costs (+3.9%) on higher fuel prices. Our inflation forecast remains at 2.8% in 2023 and +3.5% in 2024.

- **Monetary Policy Forecast:** There have been calls from PM Pham Minh Chinh for the SBV to lower average rates and direct credit to production and other growth sectors, pointing out that the credit growth in 1H was low and commercial lending interest rates are high and businesses encountered challenges in credit access. In response to that, SBV Deputy Governor Dao Minh Tu told the press that the central bank may lower interest rates with commercial banks in order to ease credit conditions for businesses if conditions allow. **Base case remains for deposit rate to be cut by another 25bps before year end which would take the total reduction to 150bps.** That said, our economist sees an increasing risk that the weakening VND could deter the SBV from easing monetary policy further.

- **Latest Fiscal and External Balance Outlook:** Current account flipped into surplus of around $6.5mn for 1Q 2023 vs. the deficit of $-1.0n in 4Q 2022. Trade surplus has been widening with the latest recorded at USD3.82bn vs. previous USD2.15bn. The -7.6%y/y decline in exports for Aug was outpaced by the -8.3%y/y decline in imports. Our economist looks for a potential recovery in exports in 4Q.

- As for fiscal, based on the MOF report, the state budget revenue is expected to be around VND1.62 quadrillion ($68.5bn), up 0.4% from 2022 and state budget expenditure at VND2.07 quadrillion, a 16.3% increase from 2022. State budget deficit to come in around VND455.5trn which would be 4.42% of GDP. Central budget deficit will amount to VND430.5trn (4.18% of GDP), local budget deicit at VND25trn (0.24% of GDP).

- **Key domestic events and issues to watch:** Sep CPI, Industrial production, Trade and 3Q GDP are due 25-31 Aug.

FX Forecasts

	End Q3-23	End Q4-23	End Q1-24	End Q2-24
USD/JPY	145.00	142.00	140.00	134.00
EUR/USD	1.0800	1.0900	1.1000	1.1200
GBP/USD	1.2700	1.2500	1.2400	1.2300
AUD/USD	0.6500	0.6600	0.6700	0.6800
NZD/USD	0.6000	0.6000	0.6100	0.6200
USD/CAD	1.3300	1.3200	1.3100	1.3100
USD/SGD	1.3500	1.3400	1.3250	1.3150
USD/MYR	4.6000	4.5500	4.4500	4.3500
USD/IDR	15200	15000	15000	14700
USD/THB	35.00	34.75	34.50	33.50
USD/PHP	56.00	56.00	55.50	54.00
USD/CNY	7.30	7.25	7.20	7.15
USD/CNH	7.30	7.25	7.20	7.15
USD/HKD	7.82	7.80	7.79	7.78
USD/TWD	31.25	30.50	30.25	30.00
USD/KRW	1300	1280	1270	1250
USD/INR	82.50	82.50	81.00	81.00
USD/VND	23800	23800	23500	23500
DXY Index	103.63	102.89	102.14	100.50
	End Q3-23	End Q4-23	End Q1-24	End Q2-24
SGD/MYR	3.41	3.40	3.36	3.31
JPY/SGD	0.93	0.94	0.95	0.98
EUR/SGD	1.46	1.46	1.46	1.47
GBP/SGD	1.71	1.68	1.64	1.62
AUD/SGD	0.88	0.88	0.89	0.89
NZD/SGD	0.81	0.80	0.81	0.82
CAD/SGD	1.02	1.02	1.01	1.00
SGD/IDR	11259	11194	11321	11179
SGD/THB	25.93	25.93	26.04	25.48
SGD/PHP	41.48	41.79	41.89	41.06
SGD/CNY	5.41	5.41	5.43	5.44
SGD/HKD	5.79	5.82	5.88	5.92
SGD/TWD	23.15	22.76	22.83	22.81
SGD/KRW	963	955	958	951
SGD/INR	61.11	61.57	61.13	61.60
SGD/VND	17630	17761	17736	17871
	End Q3-23	End Q4-23	End Q1-24	End Q2-24
JPY/MYR	3.17	3.20	3.18	3.25
EUR/MYR	4.97	4.96	4.90	4.87
GBP/MYR	5.84	5.69	5.52	5.35
AUD/MYR	2.99	3.00	2.98	2.96
NZD/MYR	2.76	2.73	2.71	2.70
CAD/MYR	3.46	3.45	3.40	3.32
MYR/IDR	3304	3297	3371	3379
MYR/THB	7.61	7.64	7.75	7.70
MYR/PHP	12.17	12.31	12.47	12.41
MYR/CNY	1.59	1.59	1.62	1.64
MYR/HKD	1.70	1.71	1.75	1.79
MYR/TWD	6.79	6.70	6.80	6.90
MYR/KRW	283	281	285	287
MYR/INR	17.93	18.13	18.20	18.62
MYR/VND	5174	5231	5281	5402

Source: Maybank FX Research and Strategy as of 31 August 2023.
*These forecasts are meant to be indicative of FX trends and not meant to be point forecasts.

DISCLAIMER

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