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Maybank

FX Monthly

2023, Issue 5: Fed Pause Possibly in Sight

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What Has Changed This Month?

- We have adjusted our forecasts for a number of pairs due to better support for the USD and a disappointing China recovery. We now see that the Fed may engage in a "hawkish pause" for a while before softening their stance towards the year end as price pressures may only gradually decline as the labour market remains resilient. Consequently, this has led us to revise our DXY forecast upwards as we now expect it to stay a firmer than we had initially expected. This also contributed to our decision to move the EURUSD forecast lower and USDJPY forecast upwards. Meanwhile, the disappointing and lackluster China economic recovery has resulted in us raising our USDCNH forecast. The AUDUSD, USDCAD, USDSGD, USDMYR, USDIDR, USDTHB, USDPHP and USDVND forecasts were all concurrently raised on the basis of the firmer USD and disappointing China economic recovery.

Our Strategies and Views

- Market expectations of the Fed rate hike path in the near future have flipped quite aggressively and quickly between hike, cuts or pause amid the varying comments from Fed officials and US data. Going into June, we are faced with an FOMC meeting where our expectations are for them to likely to stand pat albeit they may engage in a "hawkish pause" as they now monitor the effects of their cumulative rate hikes to date. With that in mind and given how far the DXY has climbed on rate hike expectations in May, the index could come off a little into the month albeit still staying firm. Under this scenario, we believe that therefore USD strength would encounter a limit in the coming month.

- China's economic recovery is looking to be rather lackluster with indicators in the last month such as CPI, industrial production, PMI and retail sales pointing towards both consumption and manufacturing activities looking to be weaker than expected. Concurrently, US – China relations continue to be tense with China recently banning the use of Micron chips in key infrastructure projects and rejecting a US proposal for a defense chief meeting. At this point, the market looks to be pricing in a high level of pessimism regarding these issues. We therefore see that further downside for the CNH, AxJ, AUD could be more limited.

- UK April core CPI continued to stay elevated as it accelerated to 6.8% YoY (Mar. 6.2% YoY). This is the first advanced economy in this high inflation cycle to have observed this particular phenomenon of a reacceleration in core price pressures. This is exacerbated against a backdrop of a BOE acknowledged wage-price spiral and expectations for flat growth, creating fears of stagflation. We stay wary of the risk that other advanced economies could face similar issues.

Top 3 Currency Plays for Jun

Sell DXY on Rally
Accumulate AUDUSD on dips
Sell USDSGD, USDIDR, USDJPY on Rally

Key Events for the Month Ahead

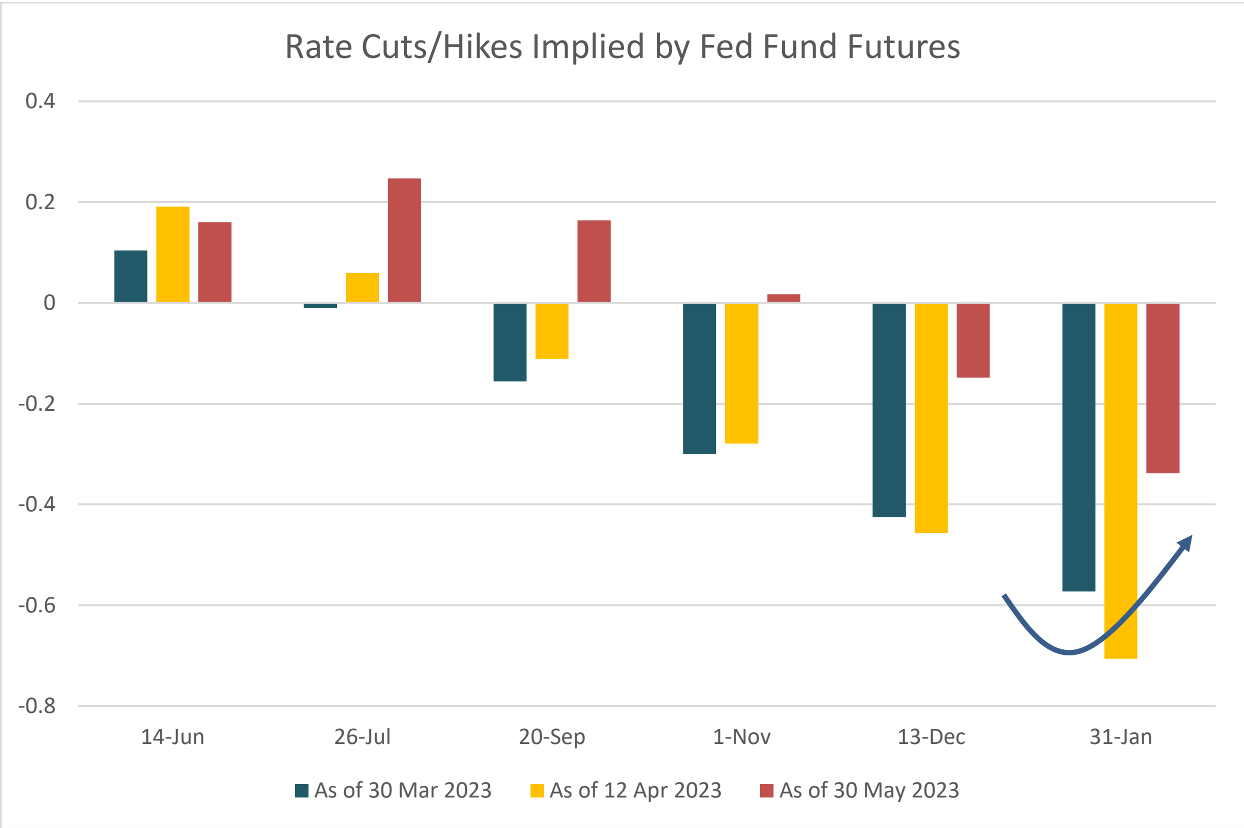
Date	Event
3-4 Jun	OEPC + Meeting

Central Bank Meetings for the Month Ahead

Date	Event
6 June	RBA Policy Decision
7 June	BoC Policy Decision
14 June	Fed Policy Decision
15 June	ECB Policy Decisioin
16 June	BoJ Policy Decision
22 June	BOE Policy Decision
22 June	BI Policy Decision
22 June	BSP Policy Decision

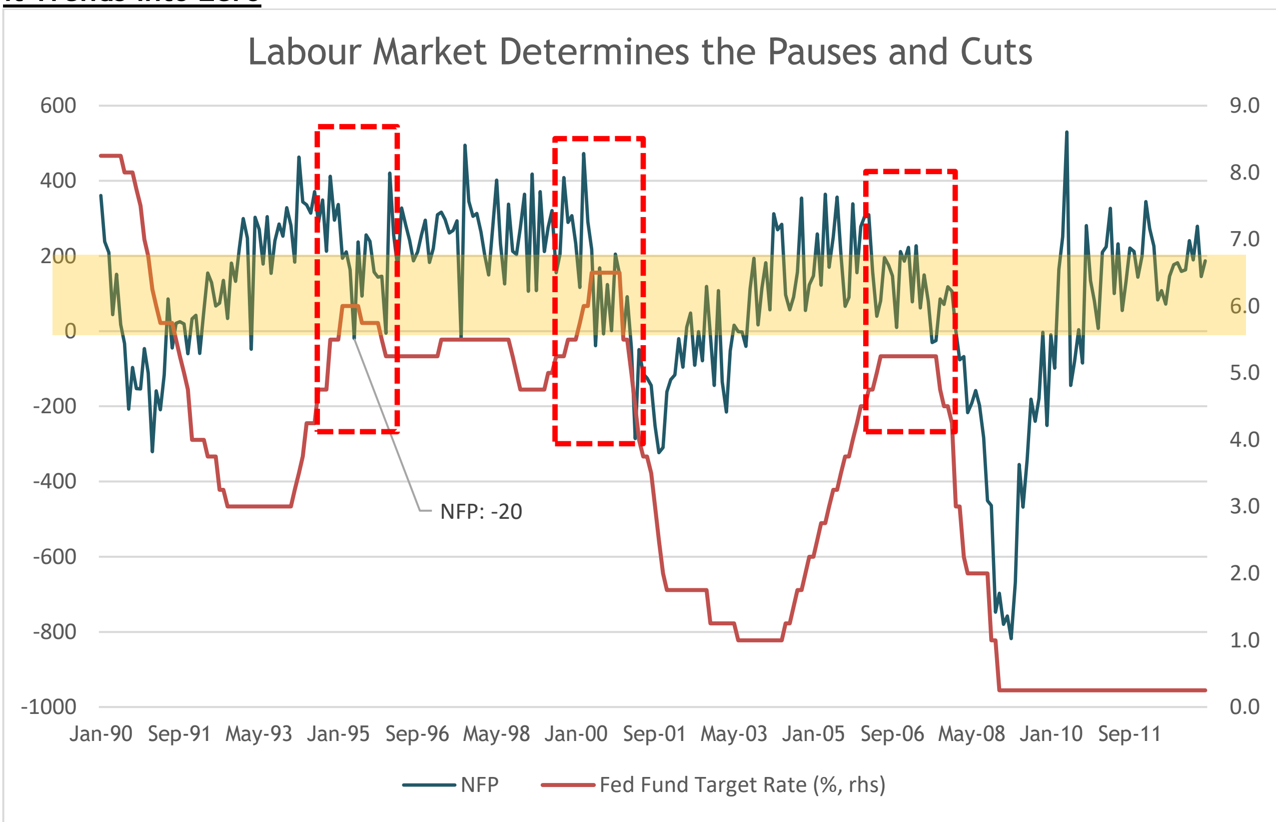
SEE PAGE 53 FOR IMPORTANT DISCLOSURES AND ANALYST CERTIFICATIONS

Markets Looked for One More Hike in 2023 in May



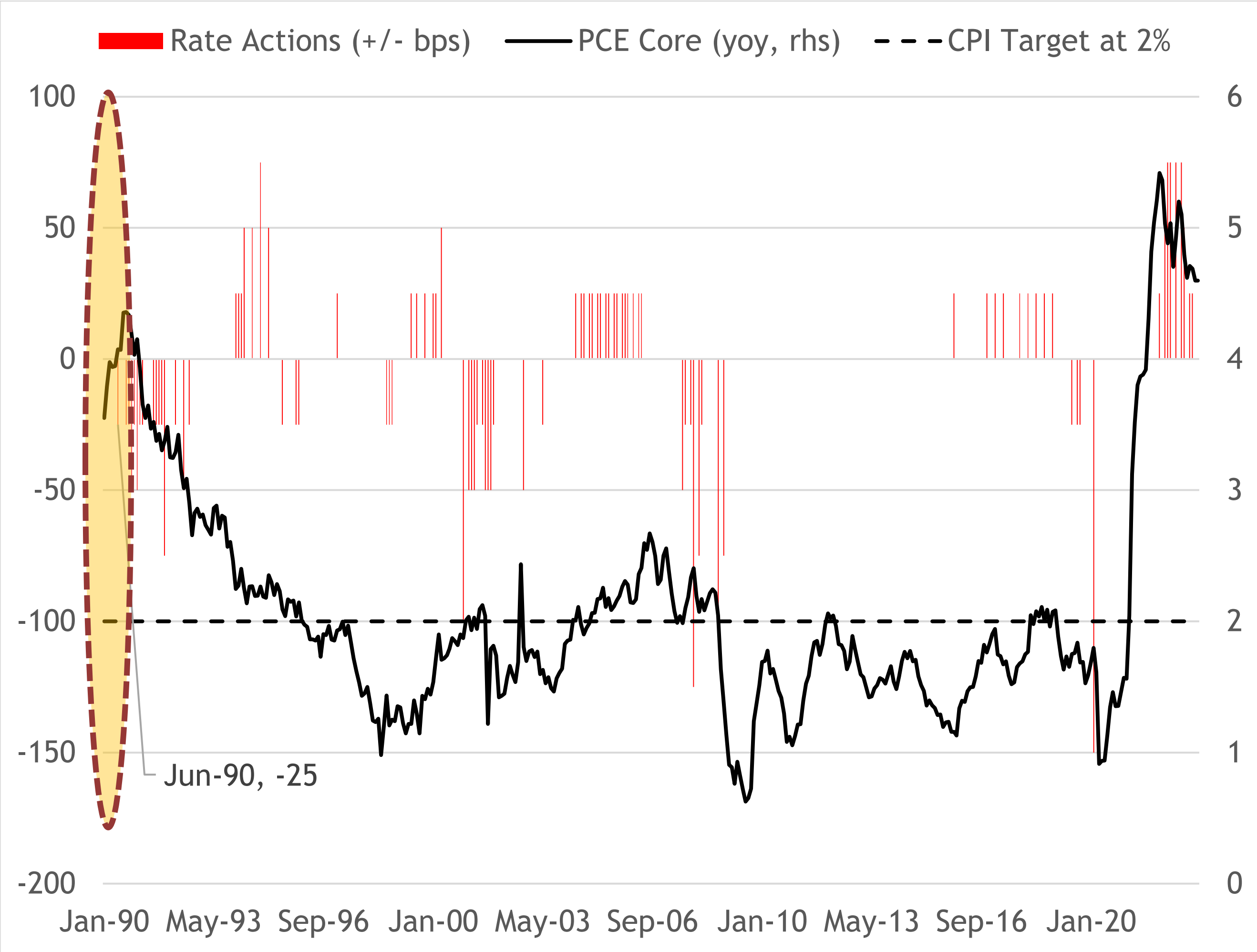
Sources: Bloomberg, Maybank FX Research & Strategy

Fed Tends to Pause When NFP Drops Beyond 200K, Cuts When it Trends into Zero



Sources: Bloomberg, Maybank FX Research & Strategy

It Would Not Be The First Time for Fed to Cut Rates before Inflation Eases back to 2% Target



Sources: Bloomberg, Maybank FX Research & Strategy

G7 Global Overview

USD: Stretched Positioning, Potential to Sell USD on Rally

Forecast	2Q 2023	3Q 2023	4Q 2023	1Q 2024
USD Index	104.13 (101.63)	103.43 (100.59)	102.91 (99.56)	100.55 (99.07)

Previous Forecasts in Parentheses

- **Motivation for the FX View:** The DXY index traded within a 101.027 (4 May) to 104.699 (31 May) range in May and trended upwards through most of the month on a combination of hawkish Fed re-pricing and debt ceiling woes, both of which caused UST yields to trend higher. The FOMC raised rates by 25bps in the 4 May meeting to bring the Fed Funds Rate to 5.00% to 5.25%. Since then, market views on future Fed moves have vacillated between a 20% chance of a 25bps hike on 14 Jun to a 70% probability and back to a 30% probability at the time of writing.

- We adjust our DXY forecasts higher on the back of these developments as the USD seems to have moved higher and does not seem to be paring gains even as market expectations for FOMC vacillate. Notably, the EUR and the JPY remain at relatively weak levels against the USD and this has led to a broadly higher DXY, despite some moderation from GBP outperformance.

- Earlier concerns over the debt ceiling and banking stability are likely to dissipate. At time of writing, the Democrats and Republicans have reached a non-partisan compromise on the debt ceiling and banking stability concerns have taken a backseat. There is a small risk that the debt deal is shot down by Congress, but we view this as very unlikely.

- US-China tensions have also escalated in recent times and this is on net positive for the USD, as evidenced by the broadly higher USDCNY. While the CNY might not be part of the DXY, we see heightened geopolitical tensions as a driver for a broadly stronger USD and on net a broadly stronger DXY - the JPY and CHF (combined weight of about 17.2%) are the components that could benefit from heightened tensions and even then, it is unclear that they will outperform the USD. The remaining components, the EUR, GBP, CAD and SEK are likely to weaken in times of heightened geopolitical tensions.

- We think that recent USD strength could be a bit stretched and there could be room for the USD to come off from current levels into Jun, although we are pricing in a more gradual depreciation for the USD further into the year. Key data to look out for include NFP (2 Jun) which could provide hints for the 14 Jun FOMC decision. In the absence of further drivers, we see the potential to sell the USD on further rallies.

- **Growth and Inflation Outlook:** 1Q2023 real GDP rose +1.3% YoY in the second reading (exp: 1.1%; prev: 1.1%), improving upon the first reading. Personal consumption was supportive at +3.8% YoY (exp: 3.7%; prev: 3.7%). Household spending on services was firmer than initially estimated, while purchases of merchandise were slightly weaker. The housing sector posted its eight-straight quarterly decline while business investment in equipment shrank for a second-quarter. While GDP grew, gross domestic income contracted -2.3% YoY (prev: -3.3%), the worst back to back decline since the start of the Covid-19 pandemic. This suggests that economic expansion could be losing steam under the weight of high inflation and tighter credit conditions.

- Apr Core CPI rose 0.4% MoM (exp: 0.4%; prev: 0.4%) and 5.0% YoY (exp: 5.5%; prev: 5.5%). Meanwhile, headline CPI inflation in Apr clocked in at 0.4% MoM (exp: 0.4%; prev: 0.1%) an 4.9% YoY (exp: 5.0%; prev: 5.0%). Powell's preferred inflation gauge, the PCE Core Deflator was firm in Apr at 0.4% Mom (exp: 0.3%; prev: 0.3%). Overall, price pressures remain firm and at a level that exceeds the Fed's comfort zone.

- Apr non-farm payrolls rose 253k (exp: 185k; prev: 165k), while the unemployment rate in Apr remained firnm at 3.4% (exp: 3.6%; prev: 3.5%). The US labour market looks resilient and labour data prints are more supportive of further Fed rate hikes although we note that substantial downward revisions have been applied to NFP in previous months and that actual labour market conditions could be less optimistic than the initial headline data suggests.

- **Monetary Policy Forecast:** May Fed Minutes depicted uncertainty surrounding future rate hikes. The FOMC raised rates by 25bps and reiterated that curtailing inflation remains the principle objective of the Fed. FOMC noted that banking sector stress could induce banks to tighten lending standards more than they would have in response to higher interest rates, however the economic impact of this remains uncertain. Several FOMC members noted that if the economy progressed in line with their current projections, future rate hikes may not be warranted. The implication of the minutes confirmed that additional rate hikes will be data dependent.

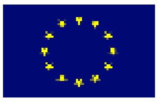
- **FOMC Outlook -** The FOMC meeting on 4 May raised the Fed Funds Rate by 25bps to 5.00% to 5.25%. There was no dot plot released for the May meeting so there were no clues beyond the minutes as to the Fed's leaning for future meetings. The Fed remained strongly committed to returning inflation to the 2% target and recent Fedspeak has been mixed, with hawkish Fedspeak driving the odds of a Jun hike to a peak of 70% (from a low of 20%), which has since moderated on more measured Fedspeak that suggest the Fed could adopt a wait and see approach and pause in June, resulting in a 30% chance of a Jun Fed hike at the time of writing.

- The March FOMC's FFR median forecast or the "dot plot" signals FFR target range peaking at 5.00%-5.25% and staying at the terminal rate this year i.e. unchanged from the position in Dec 2022. For now we expect no rate cuts this year and are less certain about the terminal rate of 5.25% lasting through 2023. If labour market data continues to point to a resilient labour market implying strong underlying wage pressures, the Fed could be forced to raise its rates as inflation has remained sticky and elevated.

- Our base case remains for the Fed to eventually come to an end of its tightening cycle, although we recognize that there is some uncertainty when and how this will come to fruition. The overall picture looks to be finely balanced - inflation looks to be firm and the labour market is healthy, but economic growth prospects look to remain somewhat muted. We think that the Fed is more likely inclined to pivot to a pause on labour market weakness and the room for further hikes could also be limited given the underlying economic tensions.

- **Key domestic events and issues to watch in Jun:** Fed Beige Book, May ADP Employment, Initial Jobless Claims, Continuing Claims, S&P Global US Manufacturing PMI, ISM Manufacturing (1 Jun), May NFP, May Unemployment Rate, Labour Force Participation, Average Hourly Earnings (2 Jun), S&P Global Services/Composite PMIs, Factory Orders, Durable Goods Orders, ISM Services (5 Jun), MBA Mortgage Applications, Trade Balance (7 Jun), May CPI (13 Jun), May PPI (14 Jun) **FOMC Rate Decision (15 Jun SG/KL Time)**, May Retail Sales, Industrial Production, Empire Manufacturing (15 Jun), Uni Mich Sentimen (16 Jun), May Housing Starts (20 Jun), May Existing Home Sales, May Leading Index (22 Jun), Jun Prelim S&P PMIs (23 Jun), May P Durable/Cap Goods Orders, May New Home Sales, Conf Board Consumer Confidence (27 Jun), 1Q2023 GDP (29 Jun), Personal Income, MNI Chicago PMI, U Mich Sentiment, PCE Core Deflator (30 Jun)

- **Technical Outlook:** The double bottom that formed in April has played out and the DXY index was last seen at 104.377 levels. Stochastics and RSI are flagging overbought levels, although momentum is still bullish. We see resistance for DXY at 105.65 (200-dma) and supports at 103.00 (psychological, 100-dma) and 102.4 (50-dma).



EUR: Short-term Bearish, Medium-term Bullish

Forecast	2Q 2023	3Q 2023	4Q 2023	1Q 2024
EURUSD	1.0700 (1.1000)	1.0800 (1.1100)	1.0900 (1.1200)	1.1100 (1.1300)

Previous Forecasts in Parentheses

- **Motivation for the FX View: We revise our EURUSD forecasts lower for the next four quarters to account for a potentially more hawkish than anticipated Federal Reserve and to account for recent lacklustreeconomic data releases that have contributed to some EUR weakness.** Notably, Germany is now in a technical recession (defined as 2 consecutive quarters of QoQ contraction). The confluence of a more hawkish Fed and weaker Eurozone data has contributed to bearishness in the EUR that we see as likely short-term in nature. Nevertheless, we still acknowledge that the European Central Bank (ECB) is potentially the central bank that is the furthest from the end of the tightening cycle, which we think will have a positive impact for EUR sentiment. Additionally, we expect the EU's economic growth, as well as the rest of the world, to slow down but not deteriorate significantly, potentially bolstered by China's recovery. In the event of an eventual pause in rate hikes by the ECB later in the year, it could be viewed positively for EUR sentiment, as long as the decision is motivated by disinflation and growth does not deteriorate significantly. It is worth noting that while this is not our base case, such a pause could be viewed to be bullish for EUR sentiment, as it would signal the ECB's willingness to maintain a balance between inflation control and economic growth. This scenario could be possible if other central banks, such as the Fed, also reach the end of their rate hike cycles, and the energy situation remains comfortable for Europe, while the labour market displays resilience. Overall, we remain optimistic about the EUR's medium-term prospects and this is reflected in our overall trajectory for an overall higher EURUSD.

- EURUSD trended lower in May on the back of a widening in the US-EU 10Y yield differential (123bps May avg vs 109bps Apr avg). This widening comes in stark contrast to the compression in yield differentials that we had observed from Oct-22 to Apr-23. Broadly, debt ceiling related fears and the hawkish Fed re-pricing had driven UST yields higher and contributed to this widening. However, we continue to believe that the Fed is will eventually come to the end of its tightening cycle, while the ECB is more likely to continue on its own tightening cycle, on a path that is divergent from the Fed. While the recent hawkish re-pricing of Fed expectations is in direct conflict with this, we reckon that the market could have run a bit ahead of itself and a paring back on these hawkish expectations could be possible. Inflation in the Eurozone remains relatively high with core inflation sticky at elevated levels and the ECB has taken an unequivocally hawkish stance on battling inflation, even when faced with financial stability woes. This should, at the very least, support the EUR if not provide impetus for it to strengthen.

- The economic landscape for the Eurozone continues to be mixed, as services activity remains robust, while manufacturing sector continues to contract. We think that while there could be potential tailwinds from China's recovery, this could possibly take a longer time to play out. We do see possible upsides for the EU as easing energy prices and supply issues from 2022 should provide support for the economy, however the rollback of state-backed support initiatives could offset the boost that these developments could provide for economic growth. The EU's largest economy, Germany, is currently in a technical recession and we recognize that this could heighten fears for a EU recession.

- The ECB raised its policy rate (deposit rate) by 25bps to 3.25% (prev: 3.00%) at the latest 4 May meeting, referring to inflation being "too high for too long". There was a continued emphasis on data dependence and Lagarde reiterated that the ECB was not pausing and that the terminal rate had not been reached. While the 25bps hike did disappoint some who subscribed to a more hawkish view of the ECB, we think that the ECB is still maintains a hawkish tilt, as evidenced by the recent release of the March ECB minutes. While there was a growing divide among council members over the magnitude of policy tightening and the transmission mechanism of monetary policy, the overall sentiment remained relatively hawkish. The hawkish tilt in the minutes was established largely on the fact that inflation remains stubbornly persistent, despite the diverging views on the appropriate monetary policy decision among the governing council. However, despite the ECB's core inflation projections of 4.60% in 2023, markets are currently pricing in an OIS-implied 3.60% terminal rate – slightly lower than last month's OIS-implied 3.75% terminal rate. This suggests that while the ECB may remain hawkish on inflation, market sentiment is not as certain about future rate hikes given the evolving economic landscape. This could lead to future bouts of EUR strength should the ECB become more hawkish than what is currently priced in.

- A warmer winter, slower drawdown in gas inventory have made all the difference for the European economy, limiting the decline of the EUR. Germany plans to reach 70.7mn tonnes per year of LNG import capacity by 2030 which would lift the country to the world's fourth largest LNG import capacity. This comes after Russia completely halted gas supply to Germany after the Nordstream pipeline was sabotaged. Germany then rushed to install floating storage and regasification units in order to import gas. According to energy analysts, Europe is on track to completely fill its gas storage toward the end of Oct 2023. Asian demand for LNG has remained muted and as such Europe is expected to be the final destination for the majority of flexible LNG cargos. Looking forward, analysts predict that Europe's gas inventories will end Mar 2024 around half full, which would be enough for Europe to endure the coldest of the last 30 winters. Stronger energy resilience could mean that the European stronghold would be less vulnerable to energy supply shocks and that bodes well for the EUR.

- **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, which has currently accumulated a healthy surplus. This could then in turn weigh on the EUR.

- 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 in the face of banking turmoil, 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. In particular, the viability of certain European banks, including Deutsche Bank, remains uncertain, and any abrupt shifts in monetary policy could further exacerbate these issues. 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.

- The Federal Reserve has become more hawkish than previously expected by markets and this has led to a substantial re-pricing in rate hike expectations moving forward. Notably, the implied probability of a 25bps at the next FOMC (13 to 14 Jun) had risen from 18% to almost 70% at its peak. As at time of writing, the market sees a 64.1% chance that the FOMC hikes by 25bps in Jun. There is a risk that the Fed remains more hawkish than expected and our base case for monetary policy divergence between the ECB and Fed does not materialize. This could result in more pronounced and sustained weakness in the EUR.

- **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, albeit 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.

- 1Q23 estimates of Eurozone growth came in at +1.3% YoY (exp: 1.4%; prev: 1.8%) and 0.1% QoQ (exp: 0.2%; prev: 0.0%). These readings showed that the eurozone dodged a winter recession, despite inflation remaining a menace in the first quarter. Although GDP missed estimates, the economy has showed surprising resilience in the face of energy price shocks and this was largely due to support from governments for consumers and businesses. Notably, Germany stagnated in terms of growth, with consumption spending dragged down by the squeeze on real income caused by high inflation. France, Spain and Italy however, managed to post modest growth figures a small positive. A further drag on the overall GDP figure also came from Ireland contracting -2.7% in 1Q23, however Ireland's growth is regularly volatile and that explains the miss from the consensus figure. We remain wary that the final 1Q23 GDP numbers could print to the downside, especially as Germany's GDP growth figures disappointed at -0.3% SA QoQ (exp: 0%; prev: 0%), placing it in a technical recession.

As earlier suggested, consumption was indeed dragged down by the squeeze on real income caused by high inflation as private consumption fell -1.2% QoQ (exp: -90.7%; prev: -1.7%).

- Most advanced economies, including the Eurozone, are seeing contractions in manufacturing activity implied by PMIs, although services PMI remain firmly in expansionary territory. This trend looked to continue in April as Final Eurozone PMIs came in at 45.8 for manufacturing (exp: 45.5; prev: 45.8) and 56.2 for services (exp: 56.6; prev: 56.2). Preliminary May PMIs look to continue this trend, with Manufacturing printing at 44.6 (exp: 46.0; prev: 45.8) and Services at 55.9 (exp: 55.5; prev: 56.2).

- Meanwhile, Eurozone continues to see a rather stable unemployment rate of 6.5% in Mar (exp: 6.6%; prev: 6.6%). Tight labour market conditions seem to be supportive of household spending and the services sector. Apr Core CPI inflation printed at 5.6% YoY (exp: 5.6%; prev: 5.6%), while headline inflation remained firm at 7.0% YoY (exp: 7.0%; prev: 7.0%. Price pressures remain sticky and are in line with the ECB view that inflation has remained “far too high for too long”. Mar PPI inflation was at +5.9% YoY (exp: 5.8%; prev: 13.3%).

- **Monetary Policy Forecast:** On 4 May, the ECB raised rates by 25bps to take the deposit facility rate to 3.25%, marginal lending facility to 4.00% and main refinancing rate to 3.75%. The ECB remained consistent in citing that inflation remained “far too high for too long” and Lagarde clarified that the ECB was not pausing and that it had yet to reach the terminal rate. This is largely consistent with her earlier view that price stability concerns remain an issue for the Eurozone.

- The Mar ECB meeting minutes showed that the governing council was becoming increasingly divided about the magnitude of rate hikes and the transmission of monetary policy tightening thus far. However, the minutes still very much retained a hawkish tilt, and recognized the risks of persistently high and stubborn core inflation.

- For the rest of 2023, current OIS implied pricing is for a terminal deposit facility rate of 3.60%, with the market implying a total of roughly 60bps of hikes for the ECB. 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, there is still a significant 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.

- **Latest Fiscal and External Balance Outlook:** The Eurozone current account was in a €31.2b surplus in March (prev: €24.5b).. In the 12 months to March 2023, the current account recorded a deficit of -€76b, compared to a surplus of €189b (1.5% of Euro area GDP) one year earlier. This was driven mainly by a switch from a surplus (€181b) to a deficit (-€4b) for goods, a switch from a surplus (€49 billion) to a deficit (€19 billion) for primary income, and, to a lesser extent, by a larger deficit for secondary income (up from €156 billion to €164 billion) and a reduction in the surplus for services (down from

€115 billion to €111 billion). The 2022 Eurozone current account was in deficit of -€97.1b.

- **Key domestic events and issues to watch in Jun:** EC May Final Mfg PMI, EC Apr Unemployment Rate, EC May Prelim CPI (1 Jun), EC May Final Services and Composite PMI, EC Apr PPI (5 Jun), EC Apr Retail Sales (6 Jun), OECD EC Economic Outlook (7 Jun), EC 1Q2023 Final GDP (8 Jun), Jun ZEW Survey Expectations (13 Jun), EC Apr Industrial Production (14 Jun), EC Apr Trade Balance, **ECB Policy Decision (15 Jun),** EC May Final CPI (16 Jun), Apr ECB Current Account (20 Jun), EC Jun Prelim Consumer Confidence (22 Jun), EC Jun Prelim PMIs (23 Jun), EC M3 Money Supply (28 Jun), ECB Economic Bulletin, EC Jun Consumer Confidence, Economic Confidence, Industrial Confidence and Services Confidence (29 Jun), EC May Unemployment Rate, EC Jun Prelim CPI (30 Jun).

- **Technical Outlook:** EURUSD traded at around 1.0680 levels at time of writing, having broken past the 1.07 support level. EURUSD has trended lower in May and momentum indicators are bearish, although this looks to be waning. Stochastics is flagging oversold conditions, while RSI is approaching oversold conditions. Next support is at 1.06 figure, and we see a likely trading range of 1.05 to 1.10 for EURUSD.

GBP: Wage-Price Spiral Portends Potential Stagflation Woes

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

No Change to Previous Forecasts

- **Motivation for the FX View: We maintain our GBPUSD forecasts to account for the fact that even in light of the recent Fed hawkish re-pricing the BOE has similarly become more likely to continue on its tightening cycle. Core CPI inflation has re-accelerated in the UK, with BOE Governor Bailey admitting that the UK was in a wage-price spiral.** However, we also recognize that the BOE had been one of the more dovish of the major central banks, with BOE Governor Bailey not being as firm on inflation as Fed's Powell or ECB's Lagarde. In addition, the UK's medium-term prospects still look grim, given the existence of price pressures, labour market shortages and an ailing economy, structural problems inherited from Brexit. Should inflation continue to remain sticky, the policy space for the BOE to hike rates will be narrower in the face of a recession. We had earlier advocated a tactical short of the GBPUSD on the belief that the UK's poor economic fundamentals should weigh heavily on the cable. This has played out and we now suggest caution ahead of risk events such as NFP and the upcoming FOMC (13 to 14 Jun) and BOE (22 Jun) policy decisions. We still believe that the cable is fundamentally overvalued at levels above 1.24, but recognize that the risk-reward is not as attractive as it was before, given that the cable is now trading much closer to 1.24 levels than it was before. Based on this, we remain medium-term neutral on the GBP at current levels of around 1.23 to 1.24.

- **Risk(s) to our View:** While we remain neutral 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.

- There is a risk that the Fed becomes more hawkish than expected and does not pause. However, this is also mitigated by the current market positioning for the BOE. At time of writing, the market is pricing in up to 100bps of rate hikes for the BOE in 2023, with the upcoming 22-Jun meeting implying a 119.9% probability of a 25bps hike i.e. fully pricing in a 25bps hike and a 19.9% chance of a larger 50bps move. This was largely based on the fact that the latest UK CPI release (24 May) showed that core inflation accelerated in April and is a potential worry for the BOE. The fact that Governor Bailey has also acknowledged that the UK is in a wage-price spiral is also rather worrying. We think that 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 overlayed 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:** UK Prelim 1Q2023 GDP growth came in at +0.2% YoY (exp: 0.2%; prev: 0.6%) while March monthly GDP was at -0.3% MoM (exp: 0%; prev: 0%). Growth prospects appear to be improving slightly for the UK economy, however this is coming off a base of an expected recession to a level of growth that is expected to be roughly flat. Current consensus forecast suggests GDP growth to come in at +0.2% YoY (prev: -0.4% 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 at 57.5%. The BOE has also 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.

- On the inflation front, core CPI inflation accelerated in April and was hotter than expected at +6.8% YoY (exp: +6.2%; prev: +6.2%), while headline CPI inflation moderated, but remained above consensus, at +8.7% YoY (exp: +8.2%; prev: +10.1%). Price pressures remain persistent at elevated levels and the re-acceleration in core inflation is worrying. This is the first advanced economy that the phenomenon has been observed in, and against a backdrop of a wage-price spiral that the BOE has acknowledged and expectations for growth to be basically flat, this could create a much larger problem of stagflation for the UK. Consensus forecasts for the UK's CPI have increased to +6.9% YoY (prev: 6.5%) in 2023. Latest BOE inflation forecasts imply that CPI inflation will fall quickly to around 5% by the end of 2023. This is predicated on a fall in energy prices, as the BOE recognizes that food prices should continue to rise. Inflation is expected to return to the BOE's preferred target of 2% only in 4Q2024. Inflation has been kept sticky also in part due to a labour shortage in the UK that is keeping wage cost pressures strong.

- **Monetary Policy Forecast:** In line with expectations, the BOE delivered a 25bps rate hike (vote split: 7 hike, 2 maintain) in the last meeting on 11 May, bringing the policy rate to 4.50%. Our view is forthe BOE to continue to raise its policy rate by 25bps at the Jun meeting, to strike a balance between combating inflation and being supportive of economic growth. The market is currently pricing in a 119.9% chance of a 25bps hike on 22-Jun and a total of about 100bps of hikes in 2023. Existing inflationary pressures remain strong, with the recent re-acceleration in core inflation and as headline inflation moderated but remains at relatively high levels. The market is currently pricing in about a 5.50% terminal rate for the BOE and we think that this could be overstated. There unresolved problems from Brexit could pose more troubles for the BOE in the future. In addition, should inflation play out according to what the BOE has suggested, 5.50% could represent an overtightening of rates. A risk which we think the BOE are cognizant of at this point of time, given the prevailing concerns of an overtightening in the Eurozone area.

- **Latest Fiscal and External Balance Outlook:** PM Rishi Sunak has signaled his intentions to reduce the UK's national debt and cut inflation as priorities for 2023. He also added that he wishes he could implement tax cuts, but understands that it is practically impossible with the current level and persistency of inflation. Chancellor Jeremy Hunt is already under pressure from UK conservative MPs to show a path to lower taxes, which many believe is the easiest way to stave off a recession. However, inflation is not the only thing preventing tax cuts. If taxes are cut and government spending is to remain the same, then the government must finance the spending. The most expedient way to do this would be to increase government debt. However, this goes directly against the PM's intentions to reduce the UK's national debt. It remains to be seen how Chancellor Hunt plans to deal with this problem, with independent fiscal watchdog the Office for Budget Responsibility noting that there would be less headroom for the March budget, given weak productivity and labour market issues that have damaged the UK's economic prospects. The UK's budget deficit in 2022 stood at £125 billion, roughly 5.4% of GDP. Meanwhile, the current account deficit stood at -4.24% of GDP or about £100 billion. Chancellor Hunt's 15 March budget was spun as one that was pro-growth and pro-families by offering giveaways to both corporates (investment subsidies) and families (childcare and energy). However, there was a glaring absence of tax cuts, given the current inflationary environment that the UK is in. This was one of the thinnest margins for a UK budget after having relaxed fiscal rules in November, leaving himself with £6.5b to spare in contrast to the average cushion of £25.6b over the last 13 years. This leaves the UK with a small buffer against a crisis against the current backdrop of fear over financial stability, and puts the UK in a precarious position should a serious shock to the economy occur.

- UK Mar Trade Balance stood at a deficit of -£2.8b (exp: -£5.0b; prev: -£3.4b), while the Feb Goods Trade balance came in at a deficit of -£16.4b (exp: -£17.5b ; prev: -£16.6b). The trade balance improved largely due to an improvement in the services balance, however the goods balance continued to show a weakness in exports which fell -

3.3% MoM as imports fell -2.8% MoM. Nevertheless, the trade deficit reinforces the difficulty that the UK is facing and underscores the importance of access to the EU common market.

- **Key domestic events and issues to watch in Jun:** May Nationwide House Price Indices, Apr Consumer Credit, Apr Mortgage Approvals, Apr Money Supply, May Final S&P Manufacturing PMI (1 Jun), Reserves Changes, S&P Final May Services/Composites PMI (5 Jun), S&P Final May Construction PMI, BRC Sales (6 Jun), May RICS Houseprice Balance (8 Jun), May Jobless Claims, Apr Unemployment (13 Jun), Apr GDP, Apr Industrial/Manufacturing Production, Index of Services, Construction Output, Apr Trade Balance (14 Jun), BOE/Ipsos Inflation Next 12 Months (16 Jun), Rightmove House Prices (19 Jun), May CPI/RPI/PPI, May Public Finances/Public Sector Net Borrowing, Apr House Price Index (21 Jun), **BOE Policy Decision (22 Jun)**, Jun GfK Consumer Confidence, May Retail Sales, Jun Prelim S&P PMIs (23 Jun), Jun BRC Shop Price Index (27 Jun), Jun Nationwide House Price Indices (28 Jun to 3 Jul), May Consumer Credit, May Mortgage Approvals, May Money Supply (29 Jun), Llyods Business Barometer, 1Q Final GDP, 1Q Current Account and Trade (30 Jun).

- **Technical Outlook:** GBPUSD last traded round 1.2430 levels, with the GBP retracing earlier strength seen in May. We see support levels at 1.24 and 1.23 figure with resistances to the upside at 1.25 and 1.27 the next key level. Momentum is currently bearish, and stochastics is flagging oversold conditions. RSI is neutral and looks to be rising. We think that GBPUSD should be bound between a 1.23 to 1.27 range and recognize two-way risks for the pair.

AUD: Slow Gains, Seaonality Risks Ahead

Forecast	2Q 2023	3Q 2023	4Q 2023	1Q 2024
AUDUSD	**0.67**	**0.67**	**0.70**	**0.71**
	(0.70)	(0.72)	(0.73)	(0.73)

Previous Forecasts in Parenthesis

- **Motivation for the FX View:** AUD ended May with a bearish break-out of the range that has held for several weeks. Investors were spooked by weaker-than-expected data from China and fears that China's recovery is fizzling out resulted in a precipitous decline of the AUDUSD. In addition, stronger US data, hawkish Fed speaks and the minutes of the May FOMC meeting which suggests a more data-dependent Fed spurred markets to price in a hike this year and for the Fed Fund Target Rate to be at where it is by the end of this year. This is a contrast to 4 rate cuts seen at the start of the month and the USD strengthened broadly, dragging the AUDUSD to test the 0.65-figure. We revised the AUD lower given the absence of animal spirits in China's economy at this point, bringing to fruition the risks of weaker-than-expected China recovery that threaten our forecast. Our modestly bullish trajectory of the AUD reflects our view that China's recovery could take longer than expected and the end of the hiking cycle could potentially bring some relief to the AUD. In the near-term, we eye a potential hike from the RBA after the stronger-than-expected Apr CPI release on 31 May. A hawkish stance could potentially support the AUDUSD into Jun.

- **Key risks to our view:** China's growth continues to deteriorate, dragged by waning growth momentum seen in rest of the world. A US recovery ahead of the rest of the world could also strengthen the USD against pro-cyclical AUD.

- Australia is projected to turn in a silver of a surplus of $4.2bn for Budget FY2022-2023 (that ends Jun 2023). 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.

- Broadly, the budget includes $14.6bn set aside as cost-of-living relief – ($3bn of direct energy bill relief to low income households and small businesses; $1bn for homes and businesses to become more energy efficient; $300mn to help lower energy bills for tenants in social housing properties;

  - **For individuals:** Low income households receive a deduction of up to $500 from their power bills from 1 July. Eligible small businesses will receive a deduction of up to $650.

  - **For families:** Eligible single parents with one child will be able to earn an extra $569.10 every two weeks (additional $24.60 per additional child) on top of the current base rate of $922.10. Payment will stop only when youngest child turns 14 instead of 8 years old at the moment. Separately, the family income threshold to qualify for Parental Leave pay and Dad and Partner Pay is raised to $350K per annum (3000 more parents become eligible).

  - **For small businesses:** a bonus 20% deduction (up to a cap of $20K per annum) for small businesses for expenditure that supports electrification and more efficient use of energy.

  - **For employees:** The government requires superannuation to be paid on payday rather than "at least quarterly" with effect from 1 Jul 2026. Very high annuation balances will attract a higher rate of tax from 1 Jul 2025.

  While Treasurer Chalmers said that the budget is not inflationary, the opposition clearly begs to differ. That said, we look at recent data and see that risks to inflation at this point could be balanced. We

- **Growth and Inflation Outlook:** The M-I inflation gauge for Apr quickened 6.1%y/y vs. previous 5.7%. This comes after wage price index for 1Q steadied at +0.8%q/q, steady from previous. Year-on-year, wage growth quickened to 3.7%y/y from previous 3.4%. we continue to see two-way risks for CPI. We see two-way risks to price pressure. Retail sales strengthened more than expected by 0.4%m/m in Mar vs. previous 0.2%. This strength is unlikely to sustain, judging by the fall in the Westpac consumer confidence to 79.0 from previous 85.0. However, Australia's domestic demand is also boosted by net arrivals in Australia that has started to lift the housing market at home. The NAB business confidence for Apr improved a tad to 0 from -1 in the month prior while business conditions deteriorated a tad to 14 from 16.

- Unemployment rate rose to 3.7% from 3.5% and Australia lost a net -4.3k jobs in Apr (-27.1K of full-time hires, +22.8k of part-time). This could be the start of some deterioration in the labour market. On the real estate, auction clearance rate was strong at 75.3% as of 21 May and inching higher. Median house price rose 0.70%m/m in Apr slowing just a tad from previous 0.8%. Regardless, the rise in the median housing price underscores strong housing demand, a sign that Australia's housing market could be benefitting from China's re-opening and rising net-overseas migration.

- **Monetary Policy Forecast:** RBA surprised on 2 May by raising cash target rate by 25bps to at 3.85%. In Apr, the central bank was focused on the fact that "policy operates with a lag" and more time is needed to assess the impact of past rate hikes. Well, RBA decided that data releases since then was sufficient enough to spring a 25bps hike on markets, noting that inflation at 7% is still too high. The central scenario projects inflation to take "a couple of years before inflation returns to the top of the target range", highlighting that services price inflation is still rather high and broad-based. Another factor that gave the RBA some confidence to hike rates was the tight labour market.

- Apr CPI surprised majorly to the upside with a print of 6.8%y/y vs. previous 6.3%. That could potentially mean that RBA is now forced to fall back its caveat of "further tightening of monetary policy" and raise cash target rate by another 25bps to 4.10% in order to get inflation back to target of 2%. The language could remain hawkish. We remain constructive on AUD as the drags from RBA-Fed divergence to dissipate once Fed becomes more growth-focused.

- **Latest External Balance Outlook:** As of last available data, current account surplus was recorded at +1.2% of GDP for 4Q 2022, widening a tad from the previous 0.95%. Australia recorded a AUD14.1bn of current account surplus vs. previous A$753mn, buoyed by the stronger surplus in goods and services trade balances. For Mar, trade improved with exports rebounding to 4%m/m growth vs. previous -3%. Imports rose 2%m/m vs. previous -9%. Trade surplus widened unexpectedly to A$1.53bn vs. previous A$1.4bn (revised higher).

- **Fiscal Outlook:** Australia is projected to turn in a silver of a surplus of $4.2bn for Budget FY2022-2023 (that ends Jun 2023). 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:** May Mfg PMI [1 Jun]; Private CAPEX [1Q]; Apr investor loan, home loans [2 Jun]; May Judo Australia Comp PMI, Services PMI, May M-I inflation [5 Jun]; BoP current account balance for 1Q, **RBA policy decision** [6 Jun]; 1Q GDP, May foreign reserves [7 Jun]; Apr trade [8 Jun]; May CBA household spending, Westpac consumer confidence, NAB May business confidence, conditions [13 Jun]; Jun consumer inflation expectation, May labour report [15 Jun]; Minutes of the RBA Jun meeting; May Westpac leading index [21 Jun]; Judo Bank June Composite, Mfg, Services PMI [23 Jun]; May CPI [28 Jun], May job vacancies, retail sales [29 Jun], May private sector credit [30 Jun].

- **Technical Outlook:** AUDUSD waffled around 0.67 as we write. This pair is bearish on the weekly chart right now but is fast entering oversold conditions. Given the absence of any trend at this point, we reckon there is a possibility of a rebound from support around 0.6590 notwithstanding some volatility that the coming month may bring. Resistance at 0.6780 (50-wma). On the monthly chart, momentum indicators are rising. We remain constructive on this pair.

NZD: RBNZ's Done, Now Watch the Fed for the Next Cue

Forecast	2Q 2023	3Q 2023	4Q 2023	1Q 2024
NZDUSD	**0.63**	**0.65**	**0.67**	**0.67**
	(--)	(--)	(--)	(--)

No Change to Previous Forecasts

- **Motivation for the FX View:** Our move to turn cautious on NZD proved to be correct. RBNZ raised OCR by 25bps to 5.50% in line with expectations. The new OCR level is projected to be the peak in this cycle and RBNZ expects inflation to come within the 1-3% target by 3Q 2024. Within the statement that accompanies the decision, the central bank noted that while measures of core inflation remain elevated, most near-term inflation expectation measures have declined. Correspondingly, the OCR could be lowered from 3Q 2024. There are also signs of labour shortages easing and job vacancies have fallen. The clear signal from the central bank that it had reached terminal rate spurred NZDUSD to fall towards the 0.60-figure, not helped the least by the hawkish Fed speaks that amplified the monetary policy divergence.

- At this point, we may need to look at how US data evolves. Based on trend, the US NFP has been on a decline. The latest upside surprises in NFP does not take away from that. With one hike already priced for the Fed, risks are skewed to the downside for the USD against the NZD from this point. Barring an upside surprise for NFP and inflation numbers, we expect NZDUSD to head higher in the short term as well as the medium term.

- **Growth and Inflation Outlook**: Multiple Inflation metrics suggest that price pressure have slowed for New Zealand – food prices for Apr slowed to 0.5%m/m vs. prev. 0.8%. House prices remained in steep decline of -10.3%y/y vs. -10.5%. The 2Y inflation expectation for 2Q also slowed to 2.79% compared with 3.30% in 1Q.

- Consumer confidence fell to 79.2 vs. previous 79.3. Such deterioration might be offset by the strong recovery in net migration at +112.K for Mar. Strong arrivals may continue to support domestic demand for New Zealand but at the same time, ease the tightness in the labour market. Home sales have been on the decline with a fall of -15.3%y/y vs. previous -15.0%. The budget includes an extension pf 20 hours Early Childhood Eductation 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.

- Mfg PMI improved to 49.1 for Apr vs previous 48.1, albeit still in contractionary. Performance services index for Apr on the other hand, fell to 49.8 vs. previous 53.8. Breakdown of the PSI reveal that purchasing managers are less positive on employment, activity/sales and new orders. These goes in line with the drop in consumer confidence.

- **Monetary Policy Forecast:** RBNZ raised OCR by 25bps to 5.50% in line with expectations. The new OCR level is projected to be the peak in this cycle and RBNZ expects inflation to come within the 1-3% target by 3Q 2024. Within the statement that accompanies the decision, the central bank noted that while measures of core inflation remain elevated, most near-term inflation expectation measures have declined. Correspondingly, the OCR could be lowered from 3Q 2024. There are also signs of labour shortages easing and job vacancies have fallen. RBNZ Orr expressed confidence that the current rate setting is restrictive and will constrain spending and investment but he still retains optionality to change that view upon the new information suggests different.

- **External Balance and Fiscal Outlook:** NZ current account could remain in deficit given a consistent deficit in its goods trade. 4Q current account deficit narrowed to NZD9.46bn (at -8.9% of GDP) vs. NZD11.4bn (-8.5% of GDP) in the quarter prior. New Zealand's trade balance swung into surplus of NZD427mn in Apr from -NZD1.5bn in the month prior. That could bode well for the current account in 2Q.While a surplus could be hard to sustain, current account as a whole could still be propped up better by tourist inflows and fall in freight costs while weakening consumption that reduces the import bill.

- **The Treasury projects 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 Eductation 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.

- **Key domestic events and issues to watch:** 1Q Terms of Trade [2 Jun]. ANZ May Commodity price [6 Jun]; 1Q Mfg Activity [8 Jun]; May REINZ House sales [10-14 Jun]; Card spending retail [12 Jun]; Net Migration [Apr]; May food prices [14 Jun]; 1Q current account GDP ratio, GDP [15 Jun]; May BusinessNZ Mfg PMI [16 Jun]; May Performance Services Index, 2Q Westpac consumer confidence [19 Jun]; May trade [22 Jun]; ANZ Jun activity outlook, business confidence [29 Jun]; ANZ Jun consumer confidence [Jul].

- **Technical Outlook:** NZDUSD softened recently and pressed against support around 0.6090. This marks the key support and a failure to break this level could mean an arguable inverted head and shoulders in the making and that could propel the NZDUSD higher. Potential neckline at 0.6530 and a bullish extension there is the next and more important confirmation of the price pattern. Otherwise, consolidation within the 0.60-0.65 could continue.

CAD: BoC to Hike

Forecast	2Q 2023	3Q 2023	4Q 2023	1Q 2024
USDCAD	1.33	1.33	1.31	1.30
	(1.32)	(1.30)	(1.28)	(1.28)

Previous Forecasts in Parentheses

- **Motivation for the FX View:** We downgraded the CAD from 1.28 to 1.30 by the end of the year as we expect global slowdown to drag on the CAD more than what was originally expected. With the US looking rather resilient and the rest of the world potentially slowing more discernibly, USD could remains supported in the near-term. However, rate cuts from the Fed are still possible in the second half of the year as US NFP continues to trend lower. We prefer to maintain a bearish profile of the USDCAD towards the 1.30-figure by the end of the year.

- Intermittent support for the CAD could come from a potential rate hike in the next month. Apr CPI surprised to the upside with the headline CPI accelerating to 4.4%y/y from previous 4.3%. Core CPI (trimmed) on the other hand, slowed less than expected to 4.1%y/y from 4.4% (vs. expected 4.1%). Labour market conditions continue to be really tight with unemployment rate steady at 5.0% and hourly wage rate for permanent employees steady at 5.2%y/y vs the expected slowdown to 4.8%. Such upside surprises may nudge BoC to raise policy rate by another 25bps. At the momentum OIS implied only 28% chance of a rate hike on 7 Jun. In addition, we have the OPEC meeting coming up on 3-4 Jun and any surprise cut in production could also bring the USDCAD lower.

- Risks to our view is that the Fed decides to tighten a lot more than expected and that could bring the USDCAD substantially higher. A more severe slowdown in growth alongside an absence of demand recovery in China could also strengthen the USD against most other currencies in the world, including the pro-cyclical CAD.

- **Growth and Inflation Outlook:** Mfg PMI improved to 50.2 from previous 48 – an outlier given the fact that manufacturing in the rest of the world remains mostly in contraction. CFIB small business optimism rose to 56.4 from previous 55.7. Details in the survey report suggest that there is shortage of skilled labour that could be a limitation on production. Fewer reported insufficient dometic demand (30.8 vs. previous 33.2) while reports of insufficient foreign demand rose slightly to 9.0 from

7.5. The survey report also suggest that the cost of wages are concerning to more busienssses (69.7 vs. previous 69.2). This undescores tighte labour market conditions and upside pressure on wages that could spur another rate hike.

- Building permits for me surprised to the upside at 11.3%y/y vs. previous 5.5%. Housing starts were also more than expected at 261.6K vs prev. 213.8K. Existing home sales accelerated to 11.3%m/m vs. previouos 1.4%. Meanwhile, retail sales fell -1.4m/m in Mar . vs. previous -0.2%. Ex auto, the fall was gentler at -0.3% vs. previous -0.3%. There are increasing signs that activity is not slowing as much and another hike from the BoC is not out of question.

- Labour market remains tight with unemployment rate steady at 5.0%y/y in Apr. Canada added a net 41.4k jobs in Apr vs. +34.7K previously. Hourly wages steadied at 5.2%y/y, more than the expected 4.8%. Participation rate was unchanged at 65.6%.

- Apr CPI surprised to the upside with the headline CPI accelerating to 4.4%y/y from previous 4.3%. Core CPI (trimmed) on the other hand, slowed less than expected to 4.1%y/y from 4.4% (vs. expected 4.1%). BoC has its inflation target at 2% and the central bank projects inflation to fall to 3% by mid 2023 and to 2% in 2024. The recent upside surprises could mean some upside risks to the central bank's forecasts for inflation.

- **Monetary Policy Forecast:** BoC is expected to keep rates unchanged at 4.50% on 7 Jun but we see a risk of a hike. The decision reflects evidence of softening economic conditions (demand and inflation). The summary of deliberations released on 27 Apr revealed that the BoC actually considered hiking rates in Apr but decided to stand pat on monetary policy settings instead. Minutes also emphasized that policy rates are likely to remain steady for the rest of 2023 and more rate hikes are not off the table. This tilts the risks to rates to the upside rather than downside. In addition, CFIB business survey indicate that cost of wages remains a concern for more businesses vs. other factors. Inflation and wages have surprised to the upside as well.

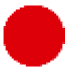
- **Latest External Balance Outlook:** As of last available data, Canada's current account balance was at a deficit of U$7.8bn for 4Q22, wider than the -U$0.2bn deficit for 3Q. Trade balance may remain under pressure as energy prices continue to remain lacklustre and that could reduce amount of oil export receipts.

- 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. Within the plan however, the tax rules are tweaked for dividends banks and insurance firms receive from firms for holding their shares. The government will treat these dividends as business income starting in 2024 and this is expected to increase the tax revenue by C$3.2bn over five years from next year according to the Federal Budget.

- **Key domestic events and issues to watch:**

- S&P Mfg PMI for May [1 Jun], Apr Buiding permits [6 Jun]; Int'l trade for Apr, BOC Policy Decision [7 Jun], May labour report [9 Jun]; Manufacturing sales for Apr, May housing starts [15 Jun]; Apr wholesale trade sales [16 Jun]; May industrial product price [19 Jun]; Apr retail sales [21 Jun]; May CPI [27 Jun]; CFIB Business Barometer for Jun [29 Jun]; Apr GDP, BoC Business outlook survey for 2Q [30 Jun].

- **Technical Outlook:** USDCAD softened recently and pressed against support around 0.6090. This marks the key support and a failure to break this level could mean an arguable inverted head and shoulders in the making and that could propel the NZDUSD higher. Potential neckline at 0.6530 and a bullish extension there is the next and more important confirmation of the price pattern. Otherwise, consolidation within the 0.60-0.65 could continue.



JPY: Near Term Weakness As BoJ Dovish, Fed Hike Bets

Forecast	2Q 2023	3Q 2023	4Q 2023	1Q 2024
USDJPY	**138** (134)	**137** (132)	**133** (130)	**131** (128)

Previous Forecasts in Parentheses

- **Motivation for the FX View:** The USDJPY has seen a substantial move up this month given the climb in UST yields amid a ramp up in June Fed rate hike bets and the US debt ceiling impasse. As it stands, there is some sense of short-term capitulation on the part of JPY bulls given that we have hit the middle of the year and yet both the domestic and global factors are scarcely working out in favour for the JPY. The BOJ has continued to stay dovish and given almost no hints of any tightening adjustment whilst a number of Fed officials still sound hawkish. Net short CFTC positions in the JPY have risen by quite a fair amount in the month of May too and stand at the highest level since early November 2022, when the USDJPY was close to its high of that year. However, JPY weakness temporarily looks to have been tempered amid jaw boning from the Japanese Ministry of Finance as a top currency official warned of government actions regarding the JPY. There remains a risk of further upside in the near-term especially if US data continues to stay strong. However, the potential of actual Japanese government intervention can create a short-term cap on the pair. Despite, the near term uncertainty, we continue to believe that the pair would still head downwards going into year end as the Fed eventually softens its stance with inflation gradually falling and the US economy weakens. Also, we believe that the BoJ would widen the YCC band by +/- 25bps from as early as October which can go some way to re-energize JPY bulls. However, we are still revising our forecast upwards as we now expect the USD to stay firmer than we had originally expected going into 2Q and 3Q before coming off more discernably into year end.

- **Growth and Inflation Outlook:** The 1Q GDP preliminary surprised on the upside coming out at 0.4% QoQ on a real basis (est. 0.2% QoQ) and 1.6% QoQ on an annualized basis (est. 0.8% QoQ). The real number had actually followed on from two quarters of decline. The recovery in the 1Q 2023 looks to have been driven by domestic demand even as external demand decline. The latter was particularly a result of a sharp fall in goods exports at 6.5% QoQ which could be a reflection of increasing weakness in global trade as goods demand falls post pandemic. Good imports had also similarly declined in line. Both export and import services had risen over the quarter which a result of the reopening of the global economy as more people began to travel. Domestic demand this quarter was also similarly stronger due to the economic reopening. The Japanese economy we believe could still be able to edge out a reasonable rate of recovery for 2023, possibly above 1.0% and into 2024. Consumer spending may increasingly be a bigger contributor of GDP growth with time given that wages are to see are a large increase from the recent negotiations and that household spending should decline with the end of the pandemic and return to normalcy.

- Headline inflation for April picked up in line with expectations to 3.5% YoY (est. 3.5% YoY and Mar. 3.2% YoY). The core number also accelerated in line with estimates at 3.4% YoY (est. 3.4% YoY and Mar. 3.1% YoY) whilst the core-core number was slightly below expectations but still a pick-up at 4.1% YoY (est. 4.2% YoY and Mar. 3.8% YoY). Core food inflation saw a big pick-up for the month contributing to higher numbers across all the inflation counts due to increased wheat and feedstuff prices and the spread of avian flu. Energy inflation in contrast saw a larger fall given the application of energy bill subsidies by the government. The factors affecting core food inflation may still take a while to dissipate which could mean that this category could accelerate into summer 2023. The energy category should continue to see a decline although this is likely to narrow after hikes in electricity charges for households are implemente don 1 June. Overall, price pressures should gradually reduce going into the end of this year and into next year although there is risk it could fall below 2.0% deeper into 2024 and into 2025. There is no certainty at this point that wages can continue to keep rising sustainably over the coming years which would make it challenging to see if inflation can hold up above 2.0%. This would make the economic case difficult for the BoJ to consider embarking on a tightening cycle. However, we do not rule out the possibility that high inflation numbers near term can energize JPY bulls in the interim.

- High frequency indicators such as May (P) Jibun Bank mfg PMI showed some slightly pick up to 50.8 (Apr. 49.5) as it crossed into expansion territory. The new orders index showed an increase by 2.0pt to 50.5 from the prior month whilst the output index rose by 4.1pt to 51.9 and the stocks of items purchased index was up 0.7pt to 52.0. Combined, these categories helped push up to overall index. Falls in the employment index and the supplier delivery time index weighed on the headline index. The output forecast index also saw a decline by 1.5pt to 59.9 which may highlight concerns of a stagnating global economy. We may be wary if the mfg PMI can continue to rise given concerns about the global and China economic weakness. Meanwhile, services PMI was up for the sixth month at 56.3 (Apr. 55.4) which reflecting the ongoing effects from the economic reopening. The backlog index, the new business index, the new export orders index and the employment index under the services PMI rose but the business expectations index fell, which could be some indication of concerns on whether the services sectors can keep up its strong performance. We believe that there is a risk that services PMI may eventually stagnate and even fall as the effects of the economic reopening wanes.

- **Monetary Policy Forecast:** For now, there still appears to be near to no hints of any BoJ policy adjustment. If anything, Ueda has continued to sound dovish as he recently even mentioned that the central bank should patiently maintain easy monetary policy. His comments regarding the latest inflation data looks to be stemming out expectations of any near term policy adjustment despite the pick-up in price pressures. He had said specifically, "The cost of impeding the nascent developments toward achieveing the 2% price stability target, which are finally in sight, by making hasty policy changes would likely be extremely high." At the same time, he is also not ruling out any options that the central bank can undertake whether it be lifting the YCC, widening the band or changing the part of the curve to be targeted. Given his persistent dovishness, there is some sense of short-term capitulation on the part of JPY bulls.

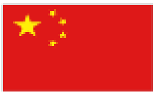
- We still expect a widening in the YCC band by 25bps to +/- 0.75% as part of a first step for the BoJ to gradually lift the YCC policy given concerns about market functionality issues and an already bloated balance sheet. However, we think such a move is likely to only happen from as early as October 2023. The YCC policy itself we believe will likely still be maintained until at least 2024.

- A top currency official at the Japanese Ministry of Finance Masato Kanda has warned recently on government actions regarding the JPY. This came after meeting among the Ministry of Finance, the BoJ and the Financial Services Agency. Kanda specifically said, "It's important that currency markets reflect fundamentals and move in a stable manner. Excessive moves aren't desirable". He further added, "The government will continue to closely monitor market moves, and will take appropriate responses if necessary". Whilst his words may not necessarily mean immediate intervention in the currency, it does highlight some level of seriousness on the government's part to try to limit the JPY weakness. Last year, the government had reportedly first intervened on 22 Sept when the USDJPY was around the 145 level. Taking that history into account, we do not rule out the possibility that the government may choose to come in around that level again. We believe as a whole that intervention into the currency can at least in interim possibly slow the pace of depreciation. It would not necessarily stop JPY depreciation if both global and domestic factors keep working against the currency.

- **Latest External Balance Outlook:** The country's trade deficit for April again furthere narrowed to -432.4bn Yen (Mar. -754.5bn Yen) as imports fell by -2.3% YoY whilst exports grew up 2.6% YoY. The growth in exports was driven by increase in transportation equipment exports, which possibly reflects improvement in the semiconductor supply. It remains uncertain going forward if exports can hold up given the lackluster China economic recovery and the risk of further weakness in the US economy. It is also uncertain on how imports would fare going forward given concerns about global economic weakness. It therefore remains unclear if Japan can turn around a trade surplus this year. The failure to do so is set to make a factor that would continue to weigh on the JPY.

- **Key domestic events and issues to watch:** 1Q Capital spending (1 June), 1Q Company profits/sales (1 June), Apr Cash earnings (6 June), Apr Household spending (6 June), Apr (P) Leading index CI/Coincident index (7 June), 1Q (F) GDP (8 June), Apr BoP CA balance (8 June), May Bank lending (8 June), May Tokyo average office vacancies (8 June), May PPI (12 June), May (P) Machine tool orders (12 June), May Trade data (15 June), Apr Core machine orders (15 June), BoJ Policy decision (16 June), Nationwide/Tokyo Dept sales (16 – 22 June), Apr Capacity utilization (20 June), May CPI (23 June), June (P) Jibun Bank Mfg/composite/services PMI (23 June), May PPI services (26 June), May Retail sales (29 June), May Dept store, supermarket sales (29 June), June Consumer confidence index (29 June), May Jobless rate (30 June), May Job-to-applicant ratio (30 June), June Tokyo CPI (30 June), May (P) IP (30 June) and May Housing starts (30 June).

- **Technical Outlook:** USDJPY has recently been testing the 140.00 resistance level. Upside risks still remain amid the release of US NFP data tomorrow. If the pair decisively breaks that level, the next level of resistance would be at 142.51 and 144.00. Support is at 137.28 and 135.00.



RMB: Growth Fears Weigh

Forecast	2Q 2023	3Q 2023	4Q 2023	1Q 2024
USDCNY	**7.05** (6.75)	**7.05** (6.70)	**6.95** (6.65)	**6.95** (6.60)
USDCNH	**7.08** (6.75)	**7.08** (6.70)	**6.95** (6.65)	**6.95** (6.60)

Previous Forecasts in Parenthesis

- **Motivation for the FX View:** We downgraded our forecasts for the RMB and look for USDCNY to remain supported on dips around 7.10 for the next several weeks. Market action suggests that bearish pressure is building on the yuan with the onshore and offshore discount vs. the USD (conversely also seen as USDCNH-USDCNY premium) widening. IIF data also suggests that China experienced equity and bonds outflows in Apr.

- We are not turning entirely negative on China's growth amd still look for consumption recovery. However, a onsumption-led recovery in the next half of the year (that could boost imports of goods and services) could weaken its external balance and that is net negative for the yuan. Meanwhile, we look for USD yields to come off into the second half of the year. That could be provide some mitigating effect on the rise of the USDCNY and USDCNH. Pair may remain elevated within 6.90-7.20 range between 2Q-3Q 2023. Our forecasts are pencilled in to be around 7.05 for USDCNY.

- There are signs that outflows are happening gradually towards the levels seen in pre-Covid, with net travel outflows recorded at -USD43bn compard with USD27.9bn. The current drags on yuan also includes the negative carry vs the USD, increasing market uneasiness over how the US is acting more aggressively to contain China's technology advancements, lingering risks of geopolitical conflict over Taiwan as well as scars from Xi Jinping's draconian policies imposed over recent years (the shutdown of private education enterprise, the technology crackdown, Covid-zero).
- **Growth and Inflation Outlook:**
- The break of the 7-figure came one day after the release of weaker activity data and in the absence of a recovery in the property sector. New home prices slowed to just 0.32%m/m in Apr vs. previous 0.44%. China's activity data for Apr released on Tue (16 Jul) underscores what the credit /inflation/trade data had suggested – that domestic demand is still rather weak. Almost all measures of activity undershot consensus. Industrial production quickened to 5.6%y/y from previous 3.9%, well under the expected 10.9%. Retail sales also accelerated to 18.4%y/y from previous 10.6% (vs. expected 21.9%). Fixed assets ex rural weakened to 4.7%y/y vs. previous 5.1%. Property investment clocked a steeper decline of -6.2%y/y for Jan-Apr vs. -5.8% in 1Q (expected -5.7%).
- Underwhelming data releases revived speculations of rate cuts after the 1Y medium-term lending rate and other OMO rates (key 7-day reverse repo) were kept unchanged by PBoC on Mon. This was in contrast to the hawkish Fed comments by various Fed officials this week that drove the UST yields higher. Dismal growth prospect of China at this point could render USDCNY more sensitive to swings in the UST yields.
- We bear in mind that activity data released was already propped up by the low base effects from Apr last year during the Shanghai lockdown. As such, growth momentum is even more sluggish when we look at the month-on-month figures. While retail sales clocked a growth of 18.4%y/y, retail spending actually slipped -7.5% on the month, well under the average 2.0%m/m growth seen for 2022.
- There was a divergence between spending on services and goods as in line with the Services PMI numbers. Spending on catering/restaurants rose around 1.08%m/m in Apr but that of physical goods fell 8.76%. The overall headline was dragged lower as catering/restaurants only account for around 10% of the headline. As much as spending on the services sector could continue to hold up, a lack of recovery in the broader economy and income could eventually weigh on the services sector.
- According to the NDRC report on 17 May, CNY378.4bn of fixed asset investments were approved between Jan-Apr and they were mainly in the high-tech, energy and water conservancy industries. Within Apr

alone, 14 FAI projects were approved, worth CNY98bn. NBS released a statemen, reiterating that the government is pledged to "create a new pattern of development and comprehensively deepen reform and opening up". **This could mean that future government investment could remain very sector-specific and targeted.** The breakdown of the FAI released yesterday suggests that private firms have great hesitance in making fixed assets investment while non-private firms still maintained a growth of around 1.9%y/y. Lower business confidence would mean hesitant hirers. Companies now remain cost conscious based on earnings report by tech conglomerates.

- The silver lining is that the services sector is a major employer. **We are cautiously optimistic that the government would act in time to prevent growth momentum from deteriorating further.** Looking at the personal deposit levels, there are no signs that Chinese households have started to dip into their savings and that could still mean plenty of spending power should confidence return. We do not rule out the possibility that Chinese households may take longer than the rest of the world to regain the confidence to spend after re-opening.
- **Monetary Policy Forecast:** PBoC kept its policy rates unchanged for Apr and could continue to do so for the rest of the quarter. However, there are whispers of banks being asked to reduce deposit interst rates in order to encourage the flow into investments. PBoC also conducted a survey and found that the overall loan demand index in 1Q 2023 had risen to 78.4%, a 18.9% increase from the quarter prior. Breakdown revealed that new loans were provided for manufacturing, infrastructure construction, services industries and real estate. These are nascent signs of activity recovery.
- 1Y MLF is expected to remain at 2.75% in May and that should keep 1Y loan prime rate at 3.65% and 5Y at 4.30%. It is likely that the government may want to assess the strength of the recovery after the re-opening before providing further stimulus in the second half of the year. We anticipate a rate cut of 10bps to 1Y MLF and 7day reverse repo as early as Jun that could open the way for LPRs to be adjusted lower by the Chinese banks by the same magnitude.
- **Latest Fiscal and External Balance Outlook:** Fiscal deficit (general public deficit) is seen at 3.0% of GDP for 2023. MOF has plans to issue CNY3.16trn in general sovereign bonds in 2023, CNY510bn more than 2022. However, the quota for general bonds to be sold by local government was kept unchanged at CNY720bn. Total income from taxes and fees are projected to be 6.7% more at CNY21.7trn this year vs. 2022 but expenditure on public services (healthcare, eduation, defense and internal security) is also expected to be raised 5.6%. Consolidated General Public Budget is expected to be a 4.47% deficit of GDP. Total budget deficit is around 7.4% of GDP.
- **Key domestic events and issues to watch:** Caixin May Services PMI [5 Jun], Foreign Reserves, May trade [7 Jun], May aggregate financing, money supply, new yuan loans [9-15 Jun], May CPI, PPI [9 Jun]; May FDI [11-18 Jun]; 1Y MLF [15 Jun]; May retail sales, FAI ex rural, industrial production, FX Net settlement on behalf of clients [15 Jun]; 1Y, 5Y LPR [20 Jun]; May industrial profits [28 Jun]; Jun Mfg, Non-Mfg PMI [31 May].

- **Technical Analysis:** This pair has risen higher within the 6.83-7.00 range, not establishing any trend line at this point. Weekly chart suggests some bullish bias for this pair with resistance seen around 6.98 and then at 7.0250. Support at 6.8302 before 6.7550. 21-wma has made a death cross with the 50-wma and could be en-route towards the 200-wma. Technical indicators are still rather mixed and we look for more two-way moves for this pairing.

KRW: Possible Recovery of Exports Led by Tech

Forecast	2Q 2023	3Q 2023	4Q 2023	1Q 2024
USDKRW	1300 (--)	1280 (--)	1270 (--)	1260 (--)

No Change to Previous Forecasts

- **Motivations for the FX View: While we have revised our forecasts for CNY and other Asian currencies weaker, we maintain our forecasts for the KRW on the belief that exports have bottomed and that chip demand will recover and that the KRW will be one of the main beneficiaries of this development.** We are seeing nascent signs of an improvement in export numbers for Korea and the latest market optimism and hype over Artificial Intelligence (AI) should bode well for future demand for chips. Graphic processing units (GPUs) that are used heavily for the purposes of AI specifically require memory chips that Korean companies such as Samsung and SK Hynix specialize in producing.
- We have seen better support for the KRW through the month of May and apart from technology narrative, we saw that foreign inflows into Korean equities reached record levels in May. As previously stated, we saw KRW pare back on losses sustained in Apr to trade stronger in May. South Korea has also been earmarked on the watchlist for inclusion in the FTSE Russell World Government Bond Index, which should be further supportive of the KRW. The Korean government is also making a strong push for this to happen and market watchers think there is a 50% chance that this could happen by September 2023. We watch developments on this front closely.
- The Fed's hawkish repricing in May affected many other currencies, but the KRW remained relatively unscathed and was one of the outperformers against the USD. We still see the possibility that the Fed pauses as it approaches the end of the tightening cycle, despite the vacillations of the market and we think that this should be positive for the KRW. The BOK has paused on its tightening and has provided hawkish forward guidance for its future actions, should data warrant a rate hike.

- While our revision of our forecasts for China were driven by lacklustre economic data, we still maintain our view on China's reopening to materialize later in the year, although we realize that it could be at a slower than expected pace. Given China's close trade linkages and geographical proximity to Korea, we expect the KRW to be one of the largest beneficiaries of China's anticipated recovery.
- **Risks to our View**: KRW's traditionally high-beta to global chip demand and global equity performance means that it is inclined to see amplified swings from geopolitical developments. While this is positive in the context of China's reopening, developing tensions between US and China could leave Korea stuck between a rock and a hard place. Korea is a US ally, but it has shown in refusing to join the US-led protectionist chip-bloc against China that it does not want to offend China. Indeed, it could well be the case that Korea cannot afford to offend China. We see a potential drag on the KRW if tensions continue to escalate and Korea is forced to pick a side.
- We also note potential tensions with China, North Korea as risk triggers. Recall that China-Korea relations deteriorated in 3Q 2016 over US-Korea alliance decision to deploy US Terminal High Altitude Area Defense (THAAD) anti-missile system to defend against North Korea missile threat. President Yoon had earlier indicated plans to buy an additional THAAD system. This may be a concern for KRW if it induces risks of retaliation from China. But we also note some recent efforts from Yoon to avoid antagonizing China. Meanwhile, inter-Korean tensions are also in play as North Korea ramps up missile tests in recent weeks. South Korean president Yoon has warned of "overwhelming" response if North Korea attempts any nuclear action. Meanwhile, KRW also continues to be exposed to swings in broader geopolitical risks. E.g., Biden's warning of China potentially making a move on Taiwan on a "much faster timeline" than previously thought, continued aggressive Russian strikes in Ukraine etc., could continue to cap sentiment recovery.
- Global growth concerns remain a persistent drag on high-beta/pro-cyclical KRW. Global growth slowed in 2022 to 3.2% and is expected to remain at below-trend rates in 2023 and 2024. The OECD believes the Ukraine war to be the main cause for the moderation in growth recovery post-Covid and cost of living issues continue to persist globally. Global growth is projected to come in at 2.6% in 2023 and 2.9% in 2024. Further downside risks about the global growth and inflation outlook could weigh heavily on high-beta/pro-cyclical currencies like the KRW. Issues that potentially could lead to such a situation are the recent surprise OPEC+ production cuts, an escalation of tensions between Russia and the West, or the return of banking turmoil on a wider scale.
- Korea's energy importer status also means that there is a serious risk to inflation running rampant following the most recent OPEC+ surprise production cuts. Analysts suspect that oil may once again rise to >$100/bbl and this could weigh heavily on global recovery as the costs of doing business rise. In such an environment, there would be a two-fold drag on the KRW via high inflation rates and poorer growth prospects. This risk has recently been reduced as energy prices have moderated of late, although an uptick in prices could happen fairly quickly, especially if OPEC makes a surprise move.

- **Growth and Inflation Outlook:** South Korea's real GDP grew at+2.6% YoY in 2022. Latest consensus forecasts see growth in 2023 at 1.4% and 2024 at 2.3%. The main reason for below-trend growth continues to be a drag in exports which is expected to contract -0.8% YoY in real terms. 1Q23 advance GDP figures showed that the Korean economy likely grew by +0.8% YoY (exp: 0.9%; prev: 1.3%) and +0.3% SA QoQ (exp: 0.2%; prev: -0.4%).

- In May, the BOK revised its real GDP growth projections downwards to 1.% in 2023 (prev: 1.6%) and 2.3% in 2024 (prev: 2.4%). BOK is expecting challenging headwinds from global economic sluggishness and interest rate hikes, but expect the economy to pick up in 2H2023 as external conditions improve, in particular as China's anticipated reopening comes into play. Officials recognize that uncertainty remains high.

- South Korea 's May exports contracted by less than expected at -15.2% YoY (exp: -16.3%; prev: - 14.3%), while imports contracted by -14.0% (exp: -14.4%; prev: - 13.3%). The May trade deficit stood at US$2. 1 0 b (exp: -US$2. 5 3b; prev: -US$2.65b). This development is in line with our view of a possible bottoming of trade flows in line with the expected chip and semi -conductor cycle and as the latest hype on artificial intelligence could also possibly spur demand.

- South Korea's unemployment rate in Apr came in at 2.6% (exp: 2.9%; prev: 2.7%), indicating that the labour market continues to be resilient and remains healthy. Meanwhile, Apr Industrial production came in at -8.9% YoY (exp: -7.8%; prev: -7.6%), showing a decline in manufacturing activity that was in line with the BOK's downward growth revisions.

- On inflation, BOK expects CPI inflation to rise by 3.5% in 2023 (prev: 3.5%) and 2.5% in 2024 (prev: 2.6%). Core inflation is expected to be above the previous forecast at 3.3% (prev: 3.0%). The expected moderation in headline price pressures is due to easing pressures from both an increased supply and reduced demand. However, this forecast was predicated on lower crude oil prices, which has thus far played out to expectations. Core inflation is expected to decrease at a slower than previously anticipated pace due to an increase in services demand, a tight labour market, and the lagged pass-through of accumulated cost pressures. In terms of actual outturns, Apr headline CPI inflation cooled to +3.7% YoY (exp: %; prev: 4.2%), while core CPI inflation moderated very slightly and showed signs of stickiness at +4.6% YoY (prev: 4.8%).

- **Monetary Policy Forecast**: The Bank of Korea (BOK) maintained its policy rate at 3.50% on 25 May in line with market consensus. This follows similar pauses in Apr and Feb, on the back of two 25bps rate increases in Nov and Jan. In Feb, markets viewed the hold on its policy rate as hawkish as the BOK's language indicated it saw a restrictive stance as appropriate for a longer period of time. This had provided some support for the KRW. The latest language that accompanied the May decision reiterated the BOK's resolve to combat inflation, although it also recognized downside risks to growth. Core and headline inflation have both showed signs of moderating and this provides an argument for the BOK to listen to, a growing camp in favour earlier rate cuts amid weak exports and a worsening property market in Korea. Given that the BOK remained cognizant of the upside risk to price pressures, we think that the BOK should on balance stand pat at 3.50% at the upcoming July meeting. This view could possibly change based on Jun economic data releases.

- **Latest Fiscal & External Balance Outlook: Fitch maintained Korea's rating at AA- (outlook stable) in Sep, citing robust external finances and resilient macroeconomic performance** versus geopolitical risks related to North Korea and structural challenges from an ageing population. The new administration has proposed a fiscal rule of 3% of GDP managed deficit (consolidated balance minus social security surplus) and 60% of GDP debt limit, which implies incremental fiscal discipline, though its passage is uncertain. Fitch forecasts a deficit decline to 1.2% of GDP in 2023 alongside lower expenditure. Debt-to-GDP ratio could rise marginally from an estimated 49.5% in 2022 to 51.5% by 2025. **Actual fiscal outturns for 2022 showed a surplus of 0.2% of GDP (versus an expected deficit of -2.7%). While this remains a positive for the KRW at the margin, consensus estimates are expecting a fiscal deficit of -1.2% in 2023 and -0.7% in 2024.**

- South Korea's trade balance in Apr came in at a -US$2.6b deficit, improving on the near -US$4.6b deficit in Mar. While Apr exports continued to fall at -14.2% YoY (exp: -12.2%; prev: -13.8%), we have seen a possible bottoming in May export numbers which contracted by less than expected at -15.2% YoY (exp: -16.3%; prev: - 14.3%), while imports contracted by -14.0% (exp: -14.4%; prev: - 13.3%). The May trade deficit stood at US$2.1b (exp: -US$2.5b; prev: -US$2.6b). Should chip demand eventually pick up, the trade balance should improve and this should provide a significant tailwind for the KRW.

- **Key domestic data and events to watch in Jun:** May Trade, May S&P Global Manufacturing PMI (1 Jun), 1QP GDP, May CPI (2 Jun), May Foreign Reserves (5 Jun), BoP Goods and Current Account Balance (Apr), Bank Lending to Household May (9 Jun to 16 Jun), Import/Export Price Indices May, May Unemployment, Apr Money Supply (14 Jun), May PPI , 20-day Imports/Exports (21 Jun), Retail Sales (26 Jun to 30 Jun), Jun Consumer Confidence (28 Jun), Jun Business Survey (29 Jun), May Industrial Production, Cyclical Leading Index (30 Jun).

- **Technical Outlook:** USDKRW last traded at 1321.60 levels between a 1308 to 1343 range in May (1295 to 1345 range in April). Momentum, stochastics and RSI are all neutral. We see key upside resistance at 1350 and support at 1300 levels. Breakouts to the bottom are to be supported by 1200 and resisted at the top by 1400 psychological levels.

SGD: MAS' Appreciating Stance to Provide Support

Forecast	2Q 2023	3Q 2023	4Q 2023	1Q 2024
USDSGD	1.3300 (1.3150)	1.3150 (1.3000)	1.3050 (1.2950)	1.3050 (1.2950)

Previous Forecasts in Parentheses

- **Motivation for the FX View:** 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.
- **We earlier revised our USDSGD forecasts slightly higher to reflect the policy staying unchanged but still expect the SGD to appreciate against the USD. We make a further downward revision to USDSGD to account for a weaker and slower than anticipated effect from China's reopening. The trajectory for a lower USDSGD remains intact and** this is in line with our bearish USD-Asia core view for the year ahead. In addition, should the narrative that the Fed is coming to an end of its tightening cycle come to fruition, the SGD should also find some support despite a lack of MAS tightening. 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. We remain convicted on our positive medium-term view on the SGD.
- We also think that there is a chance the Fed is more hawkish than expected and does not pause. This has also been accounted for in our forecast for USDSGD. We think that the SGD NEER will continue to remain resilient and indeed in the recent bout of USD strength, we saw the SGD NEER actually trade firmer as it traded firmer around 1.10% to 1.20% above the mid-point, largely due to weakness in the MYR and CNY.
- 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. However, we also see the Fed coming to an end of the tightening cycle and are looking for the USD to weaken gradually through the year as the market pares back on USD assets. In addition, we expect China's reopening effects to be beneficial for Asian currencies and specifically for the SGD, with its close trade linkages to China. This is in line with our economists

views that a China recovery later in the year could potentially decouple Singapore's growth prospects from a possible recession in the US.

- **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 that does not factor into our baseline scenario.

- **Growth and Inflation Outlook:** On growth, 1Q2023 final figures showed that the Singapore economy contracted by -0.4% QoQ SA in 1Q2023 (exp: -0.6%; prev: -0.7%) and grew by +0.4% YoY (exp: 0.2%; prev: 0.1%). MTI has forecast growth at 0.5% to 2.5% in 2023, with expectations for growth to be around the mid-point of the range, on the back of a stronger economic recovery in China. Our economists are less optimistic and see the economy stagnating rather than rebounding in the coming quarters. They maintain their 2023 GDP forecast at +0.8% YoY for 2023 and now see an increased risk of a technical recession, should the expected boost from China's reopening fail to materialize in 2Q2023. Developments in economic growth have largely turned out in line with MAS' view at the last monetary policy statement.

- Apr Industrial Production came in at -1.9% SA MoM (exp: 0.1%; prev: 9.7%), underscoring continued weakness in factory activated. Apr NODX also disappointed at -9.8% YoY (exp: -9.7%; prev: -8.3%) and +2.7% SA MoM (exp: -3.1%; prev: 18.4%), while electronic exports were at -23.3% YoY (prev: -22.3%) showing that exports still remain weak.

- On inflation, MAS kept its forecasts unchanged for both core CPI (3.5% to 4.5% YoY) and headline CPI (5.5% to 6.5% YoY). MAS expects core inflation (+5.5% in Jan-Feb) to stay elevated in the next few months as accumulated business costs are passed through to consumer prices, before slowing discernibly in the second half of the year to around +2.5% YoY by end 2023. MAS also noted upside risks (commodity price shock) and downside risks (growth slowdown) to inflation. Our economists are less certain about the sharp decline in core inflation given the persistent wage pressures from a tight labour market and the expansion of the Progressive Wage Model to larger sectors. In summary, MAS' inflation outlook was more sanguine than we had expected.

- The latest Apr inflation prints showed that core inflation remains sticky at levels well above MAS' comfort zone at 5.0% YoY (exp: 4.7%; prev: 5.0%) while headline CPI inflation accelerated to 5.7% YoY (exp: 5.5%; prev: 5.5%). Cost of services accelerated, which offset softer prices in utilities, food and retail. Meanwhile, accommodation edged up and private transport costs accelerated. Our economists' maintain their projections for core CPI at +4.5% YoY and headline CPI at +5.6% YoY in 2023. Core inflation is expected to remain sticky and fall slowly due to domestic price pressures that arise from a tight labour market, the 1% hike in GST and the expansion of the Progressive Wage Model to larger sectors.

- **Monetary Policy Forecast:** The combination of a poorer than expected growth outlook and a more optimistic than expected inflation outlook 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 October as long as MAS' core inflation is on their projected trajectory.** However, we would not rule out a tightening in October or at an off-cycle meeting (likely July) should MAS' core inflation projections change materially in the event that upside imported inflation risks materialize.

- This latest decision is 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 think that the case for MAS standing pat in October should further strengthen. However, we also note that MAS highlighted upside risks to inflation and specifically cited commodity price shocks. However, the earlier OPEC surprise production cut has not resulted in a sustained increase in oil prices and this could provide some support for the MAS narrative that inflation will come off later into the year, should the trend continue. 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 February and mainly revolved in providing more social support amid rising the rising costs of living and the hike in GST. A deficit is still expected albeit at a 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.

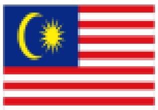
- On the revenue side, Singapore is looking to implement the Pillar 2-global minimum tax from 2025, via introduction of a Domestic Top-Up Tax, which will top up the MNE groups' effective tax rate in Singapore to 15%. This part of a broader international movement by other countries including the EU, UK 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:** Trade data in Apr continued to be weak as NODX came in at -9.8% YoY (exp: -9.7%; prev: 9.8%) although it also rose +2.7% SA MoM (exp: -3.1%; prev: 18.4%). Electronics exports remained weak at -23.3% (prev: -22.3%). These conditions remain reflective of the moderation in global demand and the overall tapering of economic growth prospects in Singapore and abroad. Singapore's Current Account balance for 1Q2023 is expected to come in at 17.0% of GDP (4Q2022: 19.3%). Singapore's current account has remained in a structural surplus and a weakening of the current account balance is not expected to have a material impact on the SGD.

- **Key domestic events and issues to watch in Jun:** May PMI/ESI (3 Jun), Apr Retail Sales (5 Jun), May S&P Global PMI (6 Jun), COE bidding (7 Jun), May Foreign Reserves (7 Jun), May NODX and Electronic Exports (16 Jun), COE bidding (21 Jun), May CPI Inflation (23 Jun), May Industrial Production (26 Jun), May Money Supply (30 Jun)

- **Technical Outlook:** USDSGD last traded at 1.3540 levels at the top end of our expected 1.32 to 1.3550 range. We see supports for USDSGD at the 1.3450 and 1.3350 levels, while resistances are at the 1.3550 level and the 1.36 figure. Momentum for the pair remains bullish, while stochastics flags overbought levels and RSI remains neutral, although at close to overbought levels. We see two-way interest in USDSGD and think it could trade within a 1.33 to 1.36 range moving forward.



MYR: Sentiment Hit By Global Factors But Weakness Temporary

Forecast	2Q 2023	3Q 2023	4Q 2023	1Q2024
USDMYR	4.45 (4.30)	4.40 (4.20)	4.25 (4.10)	4.20 (4.10)

Previous Forecasts in Parentheses

- **Motivation for the FX View:** USDMYR has edged higher this month as sentiment to the currency (and for that matter other EM FX) took a hit due to a number of negative external developments. These included the US debt ceiling impasse, ramp up in rate hike bets (amid Fed hawkish speak and strong US data), weakness in global commodity prices (crude oil, palm oil) and disappointment in China recovery.

However, whilst the global situation looks unfavourable at this point, we do not expect these developments to keep persisting until year end. The debt ceiling impasse looks like it would get resolved before a default occurs whilst there is a possibility of a Fed pause in June (albeit maintaining a hawkish tone). The latter could also eventually soften its stance closer towards year-end as inflation gradually falls. China we believe would show more discernible level of recovery also at that time and that should give a boost to commodities' prices. Hence, we believe that current weaknesses in the MYR should be temporary and the USDMYR should still follow a downwards path over the next year. As a whole, we are still revising our forecast upwards to factoring the USD staying firmer longer than we initially expected.

- BNM has also noted that the ongoing developments in the global financial markets have weighed down on market sentiment. These include the US debt ceiling impasse and episodes of stress in the US and European banking sector, which has led to demand for safe haven assets and outflows from EM economies. They have made particular mention that external developments are having a more dominant impact on the MYR performance. Additionally, they have also said that the recent depreciation in the MYR is not limited to Malaysia alone and that the movement of the MYR against other major trading partners, as measured by the NEER, has been relatively more muted. BNM has emphasized that the movements in the MYR would be market determined and that they will continue managed the risks arising from heightened financial market volatility, which to this end, they said their market operations would ensure sufficient liquidity and orderly functioning of financial markets. Overall, the central bank believes the MYR performance should improve as uncertainties from global markets developments subside and this in turn will better reflect Malaysia's sound economic fundamentals.

- Despite our positive view still of the MYR and other regional EM FXs, we are also mindful of risks that could result in our expectations not panning out. This include US data staying strong for too long and China's consumption failing to pick-up. For now, we remain confident that these risks would not materialize at a serious level.

- Putting into context, our FX-tracking model finds that the USDMYR in the short run would not hit the highs of 2022 and would in a worse case scenario likely top out at 4.6900. But our model is only indicative taking into consideration the variables in the model. At the same time, when looking at the MYR REER, we see a negative z-score and implies the MYR as third most undervalued currency in the region. This points to the MYR to possibly seeing a substantially lift once the global situation shifts and improve.

- **Growth and Inflation Outlook:** 1Q 2023 GDP growth saw a moderation to 5.6% YoY (4Q 2022. 7.0% YoY) with a contraction on a non-seasonally adjusted quarterly basis of -4.3% QoQ although on a seasonally adjusted basis, there was an expansion of 0.9% QoQ. There was a deceleration across all the major sectors whilst domestic demand eased. Both exports and imports fell amid weakness in global trade although net external demand technically surged by 54.4% YoY (4Q 2022. 23.0% YoY) by virtue of there being a larger fall in imports compared to exports.

Given the outcome of the 1Q 2023 GDP, our economists have bumped up their 2023 real GDP growth forecast to 4.5% YoY (prior. 4.0% YoY) as the previous figure was too pessimistic. However, factors that we had stated would weigh on this year's outlook still hold. This includes the negative impact that high interest rates and inflation would have on domestic demand and weakness in the global economy that could hurt commodity prices, manufacturing and consequently trade. Base effects are also an additional factor that feeds into the forecast. We do note that excess household savings, a rebound in tourism and stronger China recovery later in the year could help limit the negative effects of these factors. Overall, the 2023 forecast represents a moderation from last year that was boosted by a reopening of the economy.

- High frequency indicators do not look so positive with the S&P Global mfg PMI remaining in contraction territory at 48.8 (Mar. 48.8). This is also a reflection of a weakening in the global economy and the Malaysia PMI numbers have been similarly observed in other countries. Therefore, risk is skewed for economic growth to keep moderating going forward.

- For 2023, BNM expect moderate real GDP growth of +4.0% to +5.0% range (2023F previous: +4.5%; 2022: +8.7%) underpinned by slower global growth and elevated inflation and input costs. By sectors, services moderates to +5.0% (2023F previous: +5.3%; 2022: +10.9%), manufacturing growth eases to +4.0% (2023F previous: +3.9%; 2022: +8.1%) and slower growth in mining (2023F: +0.7%; 2023F previous: +1.2%; 2022: +3.4%); but expect bigger expansion in agriculture (2023F: +2.0%; 2023F previous: +1.1%; 2022: +0.1%) and construction (2023F: +6.3%; 2023F previous: +6.1%; 2022: +5.0%).

- Headline inflation rate moderated to +3.3% YoY in Mar 2023 (Mar 2023: +3.3% YoY). Core inflation eased marginally to +3.6% YoY (Mar 2023: +3.8% YoY). Maintain our 2023 inflation rate forecast at +3.0%, mainly on base effect and as fuel subsidy stays for the time being as per the re-tabled Budget 2023, although inflation risk remains biased to the upside amid fluid price subsidy/control policy.

- **Monetary Policy Forecast:** BNM against market expectation raised the OPR by another 25bps in the May meeting from 2.75% to 3.00%. However, this was in line with what our in-house economists had called far who had seen that a hike was possibly in May, Jul or Sept. The Monetary Policy Committee (MPC) had seen that it was timely to further normalise the degree of monetary accommodation and to ensure that the stance of monetary policy is appropriate to prevent the risk of future financial imbalances. Our in-house economists now expect BNM to stay on hold at 3.00% for the rest of 2023. The monetary policy stance at the current level for now still looks slightly accommodative and remains supportive of the economy at a time when dark clouds could be emerging in the global economic environment.

- The MPC also overall sees that risks to the domestic growth outlook to be relatively balanced. They noted that domestic demand will drive the Malaysian economy, as household spending remains resilient, underpinned by better labour market conditions with unemployment continuing to decline to pre-pandemic levels. A pick-up in tourist arrivals and further progress of multi-year infrastructure projects they believe should also support investment activity. Domestic financial conditions they mention should also remain conducive to financial intermediation, with no signs of excessive tightening affecting consumption and investment activities.

- BNM has also noted that the ongoing developments in the global financial markets have weighed down on market sentiment. These include the US debt ceiling impasse and episodes of stress in the US and European banking sector, which has led to demand for safe haven assets and outflows from EM economies. They have made particular mention that external developments are having a more dominant impact on the MYR performance and that the recent depreciation in the MYR is not limited to Malaysia alone. BNM has emphasized that the movements in the MYR would be market determined and that they will continue managed the risks arising from heightened financial market volatility. Overall, the central bank believes the MYR performance should improve as uncertainties from global markets developments subside and this in turn will better reflect Malaysia's sound economic fundamentals.

- **Fiscal Outlook:** The much anticipated re-tabled Federal Budget was released on the 24 Feb 2023 with the budget deficit seen to be at a narrower -5.0% of GDP (versus -5.5% of GDP in the original proposal) although it is still higher than -3.0 - -4.0% of GDP seen pre-pandemic. There still appeared a commitment to fiscal consolidation as the target to reduce the fiscal deficit to -3.2% of GDP by 2025 was set. The budget focused on introducing more "progressive and redistributive" tax measures through taxing higher income groups more and cutting the rate for the middle income. At the same time, there are attempts to strengthen governance in public spending through a tabling of the Government Procurement Act (GPA). However, our in-house economists noted the lack of details of sustainable revenue enhancing measures with the reintroduction of GST not appearing high on the government agenda. Fuel subsidy is also to stay in place with no specific mention of a targeted scheme being implemented in the coming year.

- Regarding corporations, the government is looking to adopt the Global Minimum Effective Tax rate of 15% in 2023 via the implementation of the Qualified Domestic Minimum Top Up Tax. This would put the country in line with its participation in the GLOBE Model rules (Pillar 2) initiative and inclusive framework on BEPS. There would also be lower Micro, Small and Medium Enterprises' (MSME) income tax rate of 15% for the first RM150,000 of taxable compared to RM100,000 proposed in the previous 2023 budget.

- On account of lower oil prices, the overall petroleum revenue is projected to drop by -20.9% to RM65.2bn and account for 22.4% of total revenue compared to 28.0% of total revenue in the prior year. Petronas would be contributing a lower level of dividends at RM40bn compared to RM50bn in the prior year.

- Fuel subsidies are to stay in place with no specific mention of any targeted scheme being implemented in the coming year. Our in-house economists have noted that past episodes of adjustment in fuel subsidies during periods of high crude oil prices did happen after key elections are out of the way. The country would be seeing six state elections later in the year.

- Government domestic debt is projected to stay just below 60% of GDP by end 2023, which compared to 57.7% as of end-2022. This still keeps it below the debt ceiling of 65% of GDP. Total government debt meanwhile is projected to rise to 62% of GDP by end 2023 from 60.4% of GDP as of end 2022. If the MTFF assumptions for 2023 – 2025 are realized, our in-house economists forecast that the government total debt should be at 62.8% of GDP in 2025 whilst the domestic debt level would be just over 60% of GDP in 2024 – 2025. As a note, government domestic debt as a percentage of GDP has been trending upwards since 2018 – 2019. However, we also do note the occurrence of the pandemic in the last couple of years which generally hurt the financial position of governments globally. Government debt service charge to revenue ratio has also been on upward trend for the last 10 years or so and will be at 15.9% in 2023, which is above the 15% international best practice threshold.

- **External Balance Outlook:** Apr 2023 exports and imports declined to -17.4% YoY (Mar 2023: 1.8% YoY; Feb 2023: +9.8% YoY) and -11.1% YoY (Mar 2023; -1.8% YoY; Feb 2023: +11.1% YoY) while trade surplus narrowed to +RM12.8b (Mar 2023: +RM26.7b Feb 2023: +RM19.6b). The decline in exports had been driven by a fall in manufacturing, agriculture and mining exports. Imports was dragged down by a fall in imports of intermediate goods and consumption goods. The numbers are overall reflecting weakness in both global trade and economy. The Malaysia trade numbers have also been similarly observed in other peer countries such as Thailand and Indonesia. The weak trade numbers only add the plethora of weaker indicators that point towards moderation in growth in the coming future.

- This year, amid softer global economic growth, our economists expect export and import growth to slow to +4.0% (4M2023: -2.6%; 2022: +25.0%) and +6.0% (4M2023: -0.3%; 2022: +31.3%) with trade surplus of +MYR240b (4M2023: +MYR77.2b; 2022: +MYR255.5b). The forecast also reflects our projection of slower global real GDP growth forecast (2023E: +2.0%; 2022: +3.4%). Four months into the year, the external trade performance reflected the headwinds from the economic downturns in US and Europe given the slowdown in exports to US (4M2023: -0.4% YoY; 2022: +17.5% YoY) and drop in shipments to EU (4M2023: -10.2% YoY; 2022: +21.8% YoY), but we expect tailwinds to external trade via exports to China (4M2023: -11.1% YoY; 2022: +9.4% YoY) from firmer growth in China on its full economic re-opening to kick in later in the year.

- Key domestic events and issues to watch: 31 May Foreign reserves (8 June), Apr Manufacturing sales (9 June), Apr IP (9 June), May Trade data (29 June), 15 June Foreign reserves (22 June) and May CPI (23 June).

- **Technical Outlook:** USDMYR is holding around the 4.61 level recently. We stay wary of further upside with the release of US economic data in the near term. Resistance is at 4.6257 and 4.7495. Support is at 4.6000, 4.5500 and 4.5500.

IDR: Resilient Amid Global Uncertainty

Forecast	2Q 2023	3Q 2023	4Q 2023	1Q 2024
USDIDR	14,800	14,700	14,500	14,400
	(14,700)	(14,400)	(14,200)	(14,000)

Previous Forecasts in Parentheses

- **Motivation for the FX View:** Despite seeing some decline over the last month amid, the IDR has held up quite resiliently compared to its other ASEAN peers. The IDR may be getting support from the stronger appeal of IGBs. Easing inflation has meant that the high yielding IGBs is proving attractive from a real perspective. Additionally, the falling price pressures also implies a higher possibility for BI to cut especially once the Fed pivots, providing an opportunity for the IGBs to rally. For investors betting on a Fed pivot eventually, IGBs may appear ideal for them to position into, which could explain the inflows we have seen this year. Despite our optimism for the currency, we are revising our USDIDR forecast slightly upwards due to our expectations that the USD may still firmer and more supported than we had initially foreseen for the rest of 2Q and 3Q, given that the Fed may engage in a hawkish pause until towards year end. Our forecasts though are still pointing towards a downward trend for the pair over the next year.

- **Growth and Inflation Outlook:** GDP growth held up and beat expectations for 1Q 2023 at 5.03% YoY (est. 4.97% YoY) riding on strong domestic consumption. Household consumption extended its firm momentum as it rose by a similar amount as the prior quarter at 4.5% YoY (4Q. 4.5% YoY). Government consumption also rose for the first time since 4Q 2021 at 4.00% (4Q 2023. -4.8% YoY). Investment however softened to the slowest pace in 2 years at 2.1% YoY (4Q 2023. 3.3% YoY). Net exports of goods and services stayed robust too for 1Q 2023. The economy as a whole still seems to be on steady footing as domestic consumption, which is the main driver of Indonesia economy is holding up well. Election related spending in 2H 2023 is also likely to boost domestic consumption too. Our in-house economists therefore continue to hold their 2023 GDP growth forecast at 5.00%.

- Headline inflation in April fell faster than expected at 4.33% YoY (est. 4.39% YoY and Mar. 4.97% YoY) as food prices eased significantly due government food security measures that included distribution of chilli seeds and funding of rice drying machines. Specifically, the food, beverage and tobacco category price growth hit a 13-month low of 4.6% YoY whilst the volatile food category price growth slowed substantially to 3.7% YoY (Apr. 5.8% YoY). The headline number is now heading to the upper end of BI's 2-4% target range. The core number at the same time eased to the softest pace in 10 months at 2.8% YoY (Mar. 2.9% YoY). Given inflation is easing faster than initial expectations, our in-house economists have therefore downgraded the 2023 headline inflation forecast to 3.7% YoY (prior. 4.2% YoY). They expect the headline to hit the upper end of BI's range as early as May or June. With falling inflation pressures, expectations may grow for a BI cut but so far the central bank has given no hint. Regardless, speculation of a BI cut this year is likely to stay in place. Overall, this puts IGBs in favour given better real yields and the potential from a rally should a cut happen. For that matter, IGBs have already been quite in favour, which is providing support to the IDR.

- The retail sales index in April rose to the highest level since May 2019 as consumer confidence continued to keep rising to 126.1 (Mar. 123.3) on the back of Ramadan and Idul Fitri. However, the year-on-year growth in the index softened to 1.1% YoY (Mar. 4.9% YoY) as the reopening tailwind faded (with the easing of Covid19 restrictions in early 2022). The retail sales number as a whole implies that the consumption is still robust and that the economy remains on sound footing.

- **Monetary Policy Forecast:** BI unsurprisingly again held rates at 5.75% at its latest policy meeting, in line with expectations. However, the central bank to have given no hint of a rate cut either with Governor Perry Warjiyo instead emphasizing that they will continue to assess the economic data each month. BI maintained their GDP growth forecast at 4.5% - 5.3% and stayed optimistic on the external balance, where both trade and the CA has been in surplus. BI also believes that inflation would return to its target range in 3Q 2023. Overall, our in-house economists are expecting that BI would keep policy rate unchanged for the rest of 2023 with a cut only to start in 2024. However, they also point that an earlier than expected Fed pivot (by the end of this year) may allow BI to start easing earlier too. The possibility of a rate cut can help keep interest strong in the IGBs and hence, give support to the IDR.

- **Latest Fiscal Outlook:** The country reported a fiscal surplus for the entire 1Q 2023 at 0.6% of GDP or $8.7bn. Revenues jumped by 29% YoY as collection from certain sectors such as manufacturing, financial services, transportation and corporate services improved. This offset the fall in customs and excise revenues (-8.9% YoY) and export duties (-7.1% YoY). The latter was a result of moderating crude palm oil prices and falling commodities exports. The fiscal policy agency also noted that the appreciation in the IDR against the USD had been a positive for the country's fiscal position. This included reducing interest payments on debt and spending on fuel subsidies in addition to raising revenues from royalties on natural resources. The government is targeting a fiscal deficit of 2.84% of GDP for 2023, which keeps it below their legal limit of 3.00% of GDP. Indonesia's better fiscal position is helping to make the IDR and IGB more attractive among its high yielding peers and encouraging more foreign inflows.

- **Latest External Balance Outlook:** The country continued to resilient maintain a trade surplus (albeit even wider) in April at $3.94bn (Mar. $2.91bn) although there was a huge plunge it exports at -29.4% YoY (Mar. -11.6% YoY), which was more than offset by also a big fall in imports by -22.3% YoY (Mar. -4.9% YoY). Export decline was driven by the fall in commodities' exports. Coal (-24.1% YoY) and palm oil (-41.4% YoY) fell heavily given that their prices stand at much lower levels compared to last year. Ores, slag & ash (-31.5% YoY) and tin & articles (-51.7% YoY) fell sharply too. Apr also marked the first month since Jan 2022 that export value dipped below $20bn. The decline in imports meanwhile was across the board. Our in-house economists expect to see that both exports and imports should continue to fall due to lower prices (compared to last year) of both export (coal and palm oil) and import commodities (crude oil). However, they also believe that the country should still be able to maintain a trade surplus going forward. Therefore, the country's trade position should continue to be supportive of the IDR.

- Apr foreign reserves was little changed at $144.20bn (Mar. $145.19bn) given the USD was quite ranged over the month. We would not be surprise if the reserves declined further in May as rate hike bets came back into play amid strong US data and concerns emerged about the weak pace of China's economic recovery. For the rest of this year, we believe that foreign reserves may likely see a gradual recovery amid the economic uncertainty and choppy markets that likely would still end the year with EM currencies being stronger.

- There was a continued net foreign inflow into Indonesia Government Securities (IGBs) which was at $0.07bn up month to date until 26 May 2023 as there remained a reasonable level of interest although the inflow was lower than the same period prior month. Generally, IGBs can be seen as more attractive than other high yielding peers given the stronger fundamental position of Indonesia as the government continues to exercise strong fiscal discipline (with the fiscal deficit having stayed below the fiscal legal limit of 3.0% of GDP in 2022) and the country resiliently continuing to maintain a trade surplus so far this year. Despite the recent set back, we believe that interest towards IGBs is likely to continue strengthening going forward especially towards the year end when the Fed is likely to more discernibly soften its stance. Near term, interest may still be decent although a ramp up in rate hike bets could limit the level of it.

- FDI for 1Q 2022 flatlined at $5.1bn (4Q 2023. $5.1bn) although it did represent a 20.2% YoY increase. The Investment Minister had noted that the manufacturing sector especially to the metal industry was the top ranked area to attract FDI. This may be a reflection of the result of the government's effort to strongly develop more-value added natural resources activities such as downstream processing of the raw materials. For now, we are still expecting that the level of FDI should at least remain stable in 2023 as the government continues to keep pushing ahead with attracting FDI into the downstream commodities area.

- **Key domestic events and issues to watch**: May S&P Global Mfg PMI (5 June), May CPI (5 June), May Foreign reserves (9 June), May Consumer confidence index (12 June), May Trade data (15 June), May Local auto sales (15 – 21 June) and Bank Indonesia Policy decision (22 June).

- **Technical Outlook:** Pair has been hovering around the range of 14700 – 15000 and we see that it could likely still do so although it interimly break above the top of the range. Resistance is at 15046 and 15100. Support at 14900 and 14800.

PHP: Cautious Amid Weak Fundamentals

Forecast	2Q 2023	3Q 2023	4Q 2023	1Q 2024
USDPHP	**55.50** (54.25)	**55.50** (54.00)	**55.00** (53.75)	**54.50** (53.50)

Previous Forecasts in Parentheses

- **Motivation for the FX View:** In line with its others regional peers, the PHP has also seen a weaker month amid broad USD strengthening as Fed rate hike bets again ramp up. However, we believe that further weakness in the currency should be more limited going forward given that the Fed tightening cycle is likely around its final stages already. It also appears that the BSP may keep rates on hold for the rest of this year in their fight to bring down inflation. This should help maintain a reasonable rate differential between the Philippines and the US and support the PHP. We continue to expect the USDPHP to head downwards towards the end of this year as US inflation comes off. However, we have made an upward revision to our forecast as we now see the USD may hold up more firmly than we initially expected as the Fed may engage in a hawkish pause in 2Q and 3Q before softening their tone towards year end.

- **Growth and Inflation Outlook:** 1Q 2023 GDP growth eased although it stayed above expectations at 6.4% YoY (4Q 2022. 7.1% YoY and est. 6.1% YoY) as external demand slumped. A slower global economy and world trade resulted in exports and imports of goods slowing whilst exports and imports of services stalled. However, domestic demand did pick up to 7.2% YoY (4Q 2022. 5.5% YoY) which help keep the overall growth number high. This came on top of stronger gross fixed capital formation and government consumption even as private consumption moderated. All economic sectors also saw expansion this quarter with the exception of mining which declined due to a fall in coal mining. Our in-house economists are overall maintaining their 2023 growth forecast at 5.5% as they expect further slowdown ahead domestic demand is weighed down by elevated inflation, interest rates and a slowing global economy resulting in sluggish external demand.

- High frequency indicators such as the S&P Global Mfg PMI released in Apr showed a decline for a third month in a row to 51.4 (Mar. 52.5). The number has remained in expansion territory but its continued decline does raise concerns about economic weakness going forward.

- Headline inflation in April eased further to 6.6% YoY (Mar. 7.6% YoY) on moderation of key items such as food & non-alcoholic beverages and housing & utilities. However the inflation numbers for these categories still remained high at 9.3% YoY (Mar. 10.8% YoY) and 7.6% YoY (Mar. 8.6% YoY) respectively. Transport inflation also eased further to 5.3% YoY (Mar. 9.0% YoY) given that Brent prices are a lot lower than it was at the same time last year. Core inflation though was roughly unchanged at 7.9% YoY (Mar. 8.0% YoY) showing that price pressures are broadening out. Our in-house economist have cut their headline inflation forecast to 5.5% YoY (prior. 5.9% YoY) given the faster than expected decline in price pressures. Regardless, the forecast is also still elevated and hence, it may not be supportive of the BSP to cut within 2023.

- **Monetary Policy Forecast:** BSP held rates at 6.25% at their latest meeting after nine consecutive rate hikes as inflation has recently eased. The central bank has also revised its inflation forecasts downwards with 2023 at 5.5% (prior. 6.0%) and 2024 at 2.8% (prior. 3.1%) given the slower than expected inflation in Mar and April although the new forecast numbers are still elevated. The BSP also expects that monthly inflation is likely to revert to its target range 2-4% by 4Q 2023 as both domestic, global growth slows and the impact of the previous rate hikes weigh in. However, the central bank is still staying mindful of upside inflation risks especially the effect that El Nino can have on food prices and utility rate as well as the potential hikes in transportation fares and wages. Going forward, our in-house economists expect that the BSP would stand pat for the rest of 2023 especially as the monetary policy statement had make mention of the need of the central bank to "keep its interest rate at its current level over the near term". Governor Medalla himself has also indicated that they would likely stay pat in the next 2-3 meetings and that interest rate cuts is not the next imminent course of action. The BSP holding the rates should help maintain reasonable rate differential between the Philippines and the US, supporting the PHP. Attention in the future is also looking to shift to the RRR, which taking cue from the Governor's comment, could see a cut from 12% to 10% in 2H 2023.

- **Latest Fiscal Outlook:** Apr budget balance turned a surplus at PHP66.8bn (Mar. –PHP210.3bn) as revenue increase at 26.7% YoY exceeding spending growth at 9% YoY. As a whole, fiscal pressures are likely to keep persisting amid an expansionary budget, which can weigh on the PHP.

- **External Balance Outlook:** Mar trade deficit widened further to -$4.9bn (est. -$4.4bn and Mar. -$3.9bn) as exports fell even more at -9.1% YoY (Feb. 18..1% YoY) than imports did at -2.7% YoY (Feb. -11.8% YoY). The fall in exports was driven by a contraction in manufacturing exports, which could reflect weakening global trade. Agriculture-led exports also showed a fall. The imports decline meanwhile was mainly a result of a fall in commodities imports that was due to prices standing at a lower level compared to last year (when the Ukraine conflict had caused a surge). Our in-house economists are consequently trimming their 2023 export and import forecasts to 3.0% YoY (prior. 5.0% YoY) and 2.3% YoY (prior. 3.5% YoY) respectively with expectations that the global economic and trade environment could be quite subdued. They main their full year estimate for trade deficit at -$59bn.

- OFWR growth picked up again in Mar but it still fell below expectations at 3.0% YoY (est. 3.3% YoY and Feb. 2.4% YoY). The stronger OFWR was supported by higher repatriations from major source countries and regions such as the US, Singapore, Korea, Europe ex-UK, UK, Japan and the Middle East. However, there could be downside risks with OFWR growth given global economic risks as manufacturing PMIs are showing weakening around the world from the US, Europe to China. Regardless, our in-house economists are still expecting OFWR to be at 3.0% YoY this year given that history has shown in the past two downturns, the number would stay resilient as overseas workers would send money home to support their families during challenging times.

- Bonds saw foreign net outflow of -$0.3bn as of 31 Mar 2023. Appetite for Philippines bonds have been weak amid concerns about the country's fundamentals - deep twin deficit position. The government's push for more infrastructure development and the possibility of higher oil prices can also risk worsening their position. We are not expecting appetite for bonds to substantially improve near term given the country's structural concerns.

- Meanwhile, equities saw a marginal net foreign outflow of -$0.07bn as of 30 May 2023. Sentiment towards equities have likely been subdued given the global macro uncertainty related to the US debt ceiling impasse and direction of the Fed rate path (with still fairly strong US data). The sentiment could continue to stay edgy as this uncertainty is likely to remain for a while.

- FX defensive buffers was steady in April as foreign reserves held at $101.5bn (Mar. $101.5bn) as the USDPHP swung quite heavily during the month. For this year, it would be challenging to strong sustainable rises in the in the foreign reserves given the uncertain global environment.

- **Key domestic events and issues to watch**: May S&P Global Mfg PMI (1 June), May Foreign reserves (5 – 10 June), May CPI (6 June), Apr Unemployment rate (9 June), Apr Trade data (9 June), Apr OFWR (14 – 18 June), May BoP overall (18 – 22 June), BSP Policy decision (22 June), May Budget balance (27 June) and May Bank lending (28 – 30 June).

- **Technical Outlook:** Pair continues to hold around our expected range of 55.00 – 57.00 and we expect to continue to do so. Resistance is at 57.00 and 57.72. Support is at 55.00 and 54.50.

THB: Bumpy Road But Stay Optimistic On Tourists Return

Forecast	2Q 2023	3Q 2023	4Q 2023	1Q 2024
USDTHB	34.00	33.25	32.50	32.00
	(33.50)	(33.00)	(32.25)	(31.50)

Previous Forecasts in Parentheses

- **Motivation for the FX View:** The USDTHB has been seeing quite a climb in the last month due to broad USD strengthening, uncertainty regarding the election outcome and concerns regarding the pace of China's recovery. Regardless, the pair still holding within the range it has traded in for most of this year around 34.00 - 35.00. In the interim, the USDTHB may continue to trade at the higher end of that range given the headwinds we have mentioned. However, we still stay positive on the THB in the medium term given that we still expect tourist arrivals from China to increase throughout the rest of the year especially in the second half and therefore, improve Thailand's external position. Furthermore, the election uncertainty, whilst it may weigh on the currency in the interim, has historically shown not to impact it in the medium term. The USD strength should also gradually come off closer towards year end. However, the USD strength may not dissipate as much as we had initially called for and it may still fairly supported in 2Q and 3Q. Resultantly, whilst we still see the USDTHB maintaining a downward path, we have raised our forecast to show that it may be more gradual.

- **Growth and Inflation Outlook:** 1Q GDP growth both picked up and came out stronger than expected at 2.7% YoY (est. 2.3% YoY and 4Q 2022. 1.4% YoY). This stronger number was a reflection of the tourism recovery gathering pace, stronger agricultural performance (better yields for certain crops) and domestic demand staying firm with the labour market conditions improving. Goods exports in contrast declined and public consumption fell for a third straight quarter due to lower social transfers. Private investment also eased although public investment gained momentum given more road and bridge construction projects and purchase of equipment by state enterprises. Our in-house economists as a whole are choosing to maintain their 2023 forecast at 4% as tourism continues to pick up and government support measures help boost consumption (regardless of which coalition or party forms the government, the expectation is that expenditure supporting measures such as cash handouts, debt forgiveness and minimum wage hikes are likely to still be implemented).

- Foreign tourist arrivals look to be recovering nicely, which could give a boost to both economy and the THB. The country reported that visitor arrivals from China had hit 36.5% of 2019 levels in April (Mar. 27.4%). This saw total arrivals hit 68.3% of 2019 levels in April (Mar. 63.9%). The numbers should keep improving especially into 2H 2023 when Chinese tourists get more comfortable with travelling overseas. The Tourism Authority of Thailand had recently said that tourist arrivals from China are likely to hit 1 million a month each from October. Chuwit Sirivejkul, regional director for East Asia at Tourism Authority of Thailand, said that advanced hotel bookings and requests for chartered flights pointed to a surge in arrivals.

- April headline inflation fell further again to 2.7% YoY (Mar. 2.8% YoY) as lower raw food prices more than offset higher energy price increases. Core inflation was flat at 1.7% YoY (Mar. 1.7% YoY), which continued to reflect the limited demand pressures. Demand side pull on inflation may not possibly materialize given that there are signs that labour market conditions are not necessarily tight in Thailand, which in turn could risk resulting in easing wage growth. Concurrently at the same time, cost pressures appear to also be easing with the April PPI falling at a faster pace of -3.4% YoY (Mar. -1.7% YoY). BOT's inflation forecast is at 2.9% YoY.

- **Monetary Policy Forecast:** BoT hiked by another 25bps in the May meeting to bring the benchmark rate to 2.00% in line with expectations. However, they still sounded somewhat hawkish as noted that risk for inflation is on the upside. That said they still cut their 2023 inflation forecasts for headline to 2.5% YoY (prior. 2.9% YoY) and core to 2.00% (prior. 2.4% YoY). GDP growth forecast was maintained at 3.6% YoY for 2023 and 3.8% for 2024. They did raise their CA balance to $6bn (prior. $4bn) to account for higher tourist arrivals. Our in-house economists believe that the BoT is done with hikes for now as inflation is easing already. There us also a risk that there could still be substantial political uncertainty building into the next meeting with the joint sitting of parliament to elect the new PM to be held in the first week of August. Given the expectations of a hold, the THB is set to receive less support from a domestic rates angle.

- Foreign reserves as of 19 May was at $222.6bn as it fell throughout May amid broad USD strengthening and concerns regarding the pace of China's recovery. There could be a contained decline or possibly stabilization in the level of foreign reserves in the coming weeks as further upside in the USD should be more limited. We also do not rule out the possibility of a correction in the greenback. We do expect that foreign reserves should still hold up or rise gradually throughout the rest of 2023 as the Fed pauses and eventually pivots.

- **Latest Fiscal Outlook:** The election outcome saw opposition parties achieve a generally resounding victory over the military linked parties. Move Forward won 151 seats whilst Pheu Thai finished second with 141. However, no one party was able to achieve anything close to a simple majority of the combined National Assembly at 376. This has resulted in a high level of uncertainty on how the formation of the new government would pan out like. Move Forward together with Pheu Thai and five other parties have signed an MOU where they aim to drive 23 agendas. This include legalizing same sex marriage, placing cannabis back on the banned narcotics list and replacing compulsory enlistment with voluntary recruitment. Notably, the 23 agendas did not include the Move Forward campaign pledge to reform the lese majeste law. This may have been done to avoid it becoming a sticking point for the coalition to win more support (especially among the senators) to form the new government. Combined, this coalition has 313 seats, which still leaves them quite short of the majority and the possible need to get the support of senators. The coalition has also formed a transition team with the leaders meeting every week until it can formally take power. The coalition will also form seven working panels of which the first of 23 sub-committees plan to fine-tune agendas agreed by member parties. There are a number of issues that have emerged within the coalition which includes that both Move Forward and Pheu Thai squabbling over the house speaker position. However, both have continued to reiterate their commitment to work together to form the next government. Whether Pita Limjaroenrat would become the next Prime Minister is still a major uncertainty. Given that the voting for the Prime Minister may not occur until end July, there is risk that the political noise can drag on for an extended period of time. Regardless, whilst the political outcome can cause some interim knee-jerk reaction, we do not believe that it would have a significant impact on the THB in the medium term. That is however, unless there is sustained political stability and a more unified direction on economic policy would the THB benefit see stronger performance in the medium to long term.

- **Latest External Balance Outlook:** Apr trade balance swung back into deficit at -$1.5bn (Mar. $2.7bn) as exports slumped in April by 7.6% YoY due to sharper contraction in industrial products amid weakness in global trade. Destination wise, exports to China saw a jump as result of greater demand for durians. However, it worsened for other places such as the US, ASEAN-5 and Japan. Imports also saw a steep decline at -7.3% YoY. The CA balance meanwhile also recorded a small deficit of $0.5bn (Mar. $4.8bn) due to a lower goods trade surplus and a deficit in net services, income and transfers. We however believe that Thailand's external position should improve going forward as more China tourists gradually return to the country. This would provide a boost for the THB.

- From a portfolio perspective, equity saw an outflow month to date up to 30 May of -$0.9bn. This could be a reflection of the anxiety regarding the election outcome. Additionally, the weaker global risk sentiment resulting from the uncertainty in relation to the US debt ceiling impasse could have both also weighed on equities in recent sessions. However, equity inflows should gradually once the US debt ceiling is raised and the domestic political situation stabilizes. Bonds meanwhile saw a net inflow of $0.6bn month to date until 30 May. However, there has been outflows since the election possibly due to concerns about the political uncertainty and the net inflow number had actually been much higher earlier in the month.

- **FDI performance would continue to be watch closely in 2023.** FDI for the final quarter fell to $1.5bn (3Q 2022. $2.0bn). Overall, for 2022, total FDI was at $9.4bn, which was around a 31% decline from the prior year. Thailand has been facing increasing competition for neighbouring peers for FDI with the country manufacturing wages being the second highest in ASEAN after Malaysia.

- **Key domestic events and issues to watch**: May S&P Global Mfg PMI (1 June), May Business sentiment index (1 June), May CPI (6 June), May Consumer confidence (7 – 13 June), May Car sales (18 – 24 June), May Customs trade data (23 – 28 June), May ISIC Mfg production index (26 – 30 June), ISIC Capacity utilization (26 – 30 June), May BoP CA and overall balance (30 June) and May Trade data (30 June).

- **Technical Outlook:** Pair has been hovering around the 34.00 level. Pair we believe is likely to stay around that mark near term. Resistance is at 35.00 and 35.52. Support is at 34.00 and 33.50.

VND: Downside Risks to Growth

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

Previous Forecasts in Parenthesis

- **Motivation for the FX View:** We adjusted the USDVND forecasts higher to reflect downside risks to Vietnam's economy. Moves of the pair had been muted for much of the past month. Equity markets rose a tad with the HCM Index up 2.8% (1-30 May, possibly buoyed by recent growth boosting measures that the government provided including the reduction of VAT tax as well as successive policy rate cuts. Even so, Vietnam continues to experience equity outflows for much of last month with $208.3mn of net equity outflows clocked between 1-30 May.

- In spite of softer growth outlook, risks posed by the real estate liquidity, some anxiety on power crunch as well as rising UST yields, USDVND remained very resilient. VND was supported by the FDI inflows beween Jan-May 2023 with total actual inflows of investment amounting to around $7.65bn in the first five months of the year. Registered FDI amounts to around $10.86bn over the same period. While this is a tad softer (0.8% lower in actual flows) vs. the same period in 2022 the inflows still managed to provide some support for the VND. In addition, weak import demand kept the trade balance in surplus ($2.24bn in May) and provided an incidental support for the currency as well.

- Lookng forward, we eye the growth of Vietnam cautiously. External demand continue to languish and resulted in a 5.9%y/y contraction for exports receipts for May. Our economist noted weakening domestic demand (retail sales slowing from May) as well as external demand (flailing exports). Growth forecast is cut to 4% for 2023. 2Q 2023GDP is expected to slow to 3% vs. 3.3%. As such, we continue to look for USDVND to trend gradually towards 23200 over the next 12 months.

- **Key risks to this view** is for a reacceleration of inflation in the US that could inject more uncertainties on Fed's policy trajectory or contagion from corporate defaults that could weigh on domestics assets and concomitantly, the VND.

- **Growth and Inflation Outlook:** Our economist has cut 2023 GDP forecast to 4% from 5.5% on the basis of sluggish growth outlook of the US and EU and less demand from China's services led recovery. Weakening growth outlook could weigh on private consumption in Vietnam as well while tourist spending is unlikely to cushion growth. 2Q2023 growth is expcted to be around 3% vs. previous 3.3% in 1Q2023.

- **Focus in the near-**term is on the power crunch at home and Vietnam has started to restart the solar power projects that were idled for years in order to improve supply conditions. Factories were limiting energy consumption and the government. So to some extent, the energy crunch is affecting the Vietnam's produxtion.

- **PM Pham had urged commercial banks to ease lending rates for busiensses.** He also wants more measures to support corporate bonds and property markets. Meanwhile, SBV had also allowed companies to extend their loan repayment deadlines through Jun in 2024. This 1Y debt suspension was informed via circulars to commercial banks "in the hope of facilitating the continuation of capital turnover and access to new loans for production and businesses".

- Earlier last month, recall that the Ministry of Planning and Investment has urged the government to stick to its 6.5% GDP growth target for 2023 in spite of growing pressure. They put out two scenarios - the first is for Vietnam to growth 6% for FY2023 (6.7% for 2Q, 6.5% for 3Q and 7.1% for 4Q). The first scenario of allowing the economy to grow 0.5% below the target would require even stronger growth in 2024 and 2025 to achieve the five year target of 6.5%. He thus urged for new support policies (tax and fees reduction, lower lending interest rates) to support growth.

- Inflation forecasts are mained at 3.4% for 2023 as weak domestic could probably tame price pressure.

- **Monetary Policy Forecast:** In Mar, SBV became the first central bank in the region to embark on an easing cycle, cutting the discount rate 100bps on 15 Mar at first and then followed by lowering its refinancing rate and deposit rate cap (for terms between 1-6M) to 5.5% from 6% with effect from 3 Apr. The cap on lending interest rates for short-term loans in some sector was also reduced to 4.50% from 5.00%.

- SBV cut policy rates for the third time this year, taking the 5% from 5.5% with effect from 25 May. in order to boost economic recovery. Overnight lending rate in the interbank market will also be lowered by the same magnitude to 5.5% from 6%. Discount rate remains at 3.5%. Pressure on the banks have been in focus of late and the refinancing rate cut could aid to lower the deposit rates. In addition, there is hope that this will help boost private consumption, ease credit conditions for businesses and support economic growth.

- **Along with the downgrade in GDP, our economist looks for SBV to cut refinancing rate, discount rate and short-term deposit rate caps by another 50-100bps within the next three months.**

- Thus far, VND has reacted calmly as Fed's dovish pivots allowed a more benign US interest rate environment for SBV to ease without jeopardizing the stability fo the VND too much. That said, we cannot rule out a tail risk of a reacceleration of inflation in the US that could generate a tad more volatility.

- **Latest Fiscal and External Balance Outlook:** Current account deficit steadied around -$1.0mn for 4Q 2022 vs. $-0.9n in 3Q. With external demand poise to weaken in 2023 and potential for China's recovery to boost energy prices, current account deficit could be at risk of widening again this year, thus potentially adding pressure on the VND. Some of the weakness in goods exports could be offset by services as tourist arrivals continue to recover. This is particularly for Chinese tourists given that China resumed group tours to Vietnam from 15 Mar.

- As for fiscal, 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:** Jun CPI, Industrial production, Trade are due 25-30 Jun.

FX Forecasts

	End Q2-23	End Q3-23	End Q4-23	End Q1-24
USD/JPY	138.00	137.00	133.00	131.00
EUR/USD	1.0700	1.0800	1.0900	1.1100
GBP/USD	1.2300	1.2300	1.2400	1.2400
AUD/USD	0.6700	0.6700	0.7000	0.7100
NZD/USD	0.6300	0.6500	0.6700	0.6700
USD/CAD	1.3300	1.3300	1.3100	1.3000
USD/SGD	1.3300	1.3150	1.3050	1.3050
USD/MYR	4.4500	4.4000	4.2500	4.2000
USD/IDR	14800	14500	14300	14100
USD/THB	34.00	33.25	32.50	32.00
USD/PHP	55.50	55.50	55.00	54.50
USD/CNY	7.05	7.05	6.95	6.95
USD/CNH	7.08	7.08	6.95	6.95
USD/HKD	7.80	7.80	7.80	7.80
USD/TWD	30.45	30.00	29.30	29.30
USD/KRW	1300	1280	1270	1260
USD/INR	80.00	80.00	79.00	78.50
USD/VND	23500	23500	23400	23300
DXY Index	104.13	103.43	102.19	100.55
	End Q2-23	End Q3-23	End Q4-23	End Q1-24
SGD/MYR	3.35	3.35	3.26	3.22
JPY/SGD	0.96	0.96	0.98	1.00
EUR/SGD	1.42	1.42	1.42	1.45
GBP/SGD	1.64	1.62	1.62	1.62
AUD/SGD	0.89	0.88	0.91	0.93
NZD/SGD	0.84	0.85	0.87	0.87
CAD/SGD	1.00	0.99	1.00	1.00
SGD/IDR	11128	11027	10958	10805
SGD/THB	25.56	25.29	24.90	24.52
SGD/PHP	41.73	42.21	42.15	41.76
SGD/CNY	5.30	5.36	5.33	5.33
SGD/HKD	5.86	5.93	5.98	5.98
SGD/TWD	22.89	22.81	22.45	22.45
SGD/KRW	977	973	973	966
SGD/INR	60.15	60.84	60.54	60.15
SGD/VND	17669	17871	17931	17854
	End Q2-23	End Q3-23	End Q4-23	End Q1-24
JPY/MYR	3.22	3.21	3.20	3.21
EUR/MYR	4.76	4.75	4.63	4.66
GBP/MYR	5.47	5.41	5.27	5.21
AUD/MYR	2.98	2.95	2.98	2.98
NZD/MYR	2.80	2.86	2.85	2.81
CAD/MYR	3.35	3.31	3.24	3.23
MYR/IDR	3326	3295	3365	3357
MYR/THB	7.64	7.56	7.65	7.62
MYR/PHP	12.47	12.61	12.94	12.98
MYR/CNY	1.58	1.60	1.64	1.65
MYR/HKD	1.75	1.77	1.84	1.86
MYR/TWD	6.84	6.82	6.89	6.98
MYR/KRW	292	291	299	300
MYR/INR	17.98	18.18	18.59	18.69
MYR/VND	5281	5341	5506	5548

Source: Maybank FX Research and Strategy as of 1 June 2023.
*These forecasts are meant to be indicative of FX trends and not meant to be point forecasts.

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Malaysia

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