Maybank

Macro | FX Research & Strategy

Global

FX Monthly

2023, Issue 6: Awaiting China Stimulus

What Has Changed This Month?

- We have adjusted our forecasts for most currencies to reflect our belief that the USD will be better supported on slowing global growth, in part due to China's recovery being delayed and inflation potentially extending expectations for DM central bank rate hikes. Inflation remains a problem in most advanced economies, with the Fed, BOE and ECB all looking to address this issue adequately. Notably, the Fed has continued with hawkish rhetoric after it was the only one of the three that paused. USD broadly weakened early in the month but strengthened in the second half to remain relatively unchanged as stronger US data supported hawkish Fed rhetoric.

Our Strategies and Views

- We are now exactly halfway through 2023 and we still have not seen a definite end to the hiking cycle from key central banks. RBA and BoC did a surprise hike in Jun after pausing and it seems like Fed is going the same way too - with Powell's threat of back-to-back hikes. ECB hiked 25bps and already committed to another hike in Jul with some officials calling for more beyond summer. BoE hiked 50bps, bigger than expected. SNB, Norges Bank and Turkish central bank also made their move. While upside surprises in inflation prints force many central banks to remain on their tightening path, we are confronted with the possibility that growth could be increasingly at risk at this point, pushing the 2y10y UST yield into deeper inversion. Services sector which had remained buoyant, holding up global growth on revenge travels, tight labour markets conditions, have started to show signs of weakness based on prelim. Services PMI. This could suggest that the weakness in manufacturing have started to broaden into those sectors. Pro-cyclical currencies such as most Asian currencies +AUD, NZD could remain under pressure in the near-term vs. the USD.
- SGD has been trading on the strong side of the SGDNEER band but persistent weakness in the manufacturing sector as well as the recent softening of core inflation saw the SGDNEER drifting a tad lower. Our economist sees a technical recession looming and small probability of easing. That could translate to room for SGDMYR to pull back.
- We still look for China to unleash its stimulus package soon with potentially business-friendly policies to boost confidence (consumers'/businesses'/investors'). Eyes are on the politburo meeting at the end of Jul but we reckon anytime before that is possible. Yuan bears should tread carefully for a potential turn in sentiment.

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Top 3 Currency Plays for Jul

Sell SGDMYR on Rally Above 3.45
Buy USDCAD on Dips
Sell USDIDR and USDPHP On rally

Key Events for the Month Ahead

Date	Event
End Jul	China Politburo Meeting

Central Bank Meetings for the Month Ahead

Date	Event
4 Jul	RBA Policy Decision
6 Jul	BNM Policy Decision
12 Jul	RBNZ Policy Decion
12 Jul	BoC Policy Decision
13 Jul	BOK Policy Decision
25 Jul	BI Policy Decision
27 Jul	FOMC Policy Decision
27 Jul	ECB Policy Decision
28 Jul	BOJ Policy Decision

G7 Global Overview

USD: In the FOMC's "Slower Quarterly Pace" Phase

Forecast	3Q 2023	4Q 2023	1Q 2023	2Q 2024
USD Index	103.51 (103.43)	102.71 (102.91)	101.27 (100.55)	99.32 (99.07)

Previous Forecasts in Parentheses

- **Motivation for the FX View:** The DXY index trended lower for the most part of June on the back of expectations that the Fed will see a step-down in the pace of hiking following Fed Chair Powell's post meeting press conference. This despite the July FOMC delivering a hawkish surprise with a dot plot that showed a median projection of two additional hikes in 2023 with limited impact on market pricing. With the slower quarterly pace, a Jul hike would significantly raise the likelihood of a 4Q move much harder as there is some likelihood that there could be some cooling of inflation by then, reducing the probability the Fed would undertake a second hike. Our economists are expecting only one more Fed hike as early as July. But we do note that the view could change as the current turning point risk environment would highly depend on inflation (and growth) outcomes.

- Our DXY forecasts remain largely unchanged on the back of these developments albeit the USD seems to have eased slightly in June. We still expect USD to remain supported in 3Q with some softness in 4Q as the markets price in some cooling of inflation in the end of 2023. Notably, we have adjusted the JPY weaker to reflect that BOJ stays stubbornly dovish and developed markets (DM) central banks continue hiking rates as inflation persistently remains too high. We see though that such factors that hurt the JPY are likely to keep persisting into year-end 2023 and only start to slightly recede in 2024. Meanwhile, the domestic economic situation is unlikely to push the BOJ to move in 2023. Japanese bond market functionality issues at the same time have also heavily eased. We also revised GBP/USD higher to reflect market developments and expectations of further rate increases as early as in Aug.

- 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.

- Last month we highlighted that USD strength could be a bit stretched and there could be room for the USD to come off from current levels into Jun. That had panned out although we are pricing in a slightly more gradual depreciation for the USD further into the year, largely in the tail end of 2023.

- **Growth and Inflation Outlook:** 1Q 2023 US GDP was revised up to 2% in the third reading reflecting upward revisions to exports and consumer spending. Household spending rose at 4.2% as services outlays were adjusted higher. Key inflation indicators such as personal consumption expenditures price index excluding food and energy rose at a 4.9% pace in the first quarter.

- May core CPI rose 0.44% m/m sa, 4bp above consensus and 2bp above the prior three-month average. A breakdown of the details in the report does show falling used car auction prices and sustained declines in shelter categories in May from Mar/Apr. Travel categories were mixed (airfares -3.0%, lodging +1.8%), but car insurance rates rose even more than expected (+2.0%). Headline CPI rose 0.12%, as energy prices fell 3.6% but food prices rose 0.2%.

- NFP rose 339k in May, exceeding consensus expectations for the fourteenth straight month and revisions were positive too with the 3-month average pace at +283k, up from +222k previously. The household survey also showed a large increase in employees, but the net number of unemployed people led to a rise in the unemployment rate by three tenths to 3.7%.

- 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:** FOMC meeting on 13-14 June 2023 saw Fed maintained target fed funds rate (FFR) at 5.00%-5.25% as widely expected. With the exception of FFR decision, the latest FOMC statement was virtually a carbon copy of the statement released after 2-3 May 2023 FOMC meeting. The real surprise was Fed's latest "dot plot" which now signals additional +50bps hikes this year vs guidance back in Mar 2023 of FFR peaking and staying at 5.00%- 5.25%.

- The updated FOMC's FFR median forecast or the "dot plot" signals FFR reaching 5.625% by end of this year i.e. implying additional +50bps hikes in FFR target range to 5.50%-5.75%, versus the position in Mar 2023 when FFR was seen as peaking at 5.125% (i.e. as per current 5.00%-5.25% target range). This suggests two more rounds of +25bps hike in FFR. There are four FOMC meetings left this year i.e. 25-26 July; 19-20 Sep; 31 Oct - 1 Nov; and 12-13 Dec.

- The more hawkish FFR outlook by Fed for the rest of this year probably relates to the changes in its macro forecasts, especially the upward revisions in 2023 real GDP growth (i.e. implying growth "soft-landing") and core inflation (private consumption expenditure, PCE) rate forecasts to +1.0% and +3.9% respectively from +0.4% and +3.6% previously, as well as the cut in unemployment rate forecast to 4.1%

from 4.5% back in Mar. Fed expects this year's headline inflation rate to be at 3.2%, slightly below the previous forecast of 3.3%.

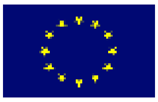
- In addition, Fed's "dot plot" maintain the guidance of "modest" - 100bps cuts in FFR next year, although – and obviously - the end-2024 FFR level is now higher at 4.625% (i.e. 4.50%-4.75%) vs 4.125% (i.e. 4.00%-4.25% target range) previously following the upward revision to end-2023 level as mentioned above. This is as Fed foresees a resilient US real GDP growth (2024E: +1.1% vs +1.2% previously) as well as still above-2% headline inflation (2024E: +2.5%) and core inflation (2024E: +2.6%) rates next year, while unemployment rate is expected to be at 4.5% next year (trimmed slightly from 4.6% previously).

- We think one more +25bps hike is a possibility now, but anything beyond is somewhat excessive. Consequently, we revised our view of FFR peaking at 5.25%-5.50% this year, to be followed by a total of -200bps cuts in 2024, which is our prevailing view on FFR for next year

- 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 July:** S&P Global US Manuf PMI, ISM Manuf (3 Jul), Factory Orders, Durable Goods Orders (5 & 27 Jul), FOMC Minutes, ADP, Trade Balance (6 July), NFP (7 Jul), Consumer Credit (11 Jul), June CPI (12 Jul), Empire Manuf (17 Jul), Retail Sales (18 Jul), Initial jobless claims (20 Jul), FOMC, GDP, Core PCE (27 Jul), PCE deflator (28 Jul).

- **Technical Outlook:** DXY Index was last seen at 103.493 levels. Supports are at 102.80 (50 dma) and further to the downside at 102.00, while resistance is at 105.00 (200 dma). Stochastics are flagging oversold conditions as RSI remains at neutral levels. All momentum indicators are rising and turning bullish.



EUR: Countervailing Factors at Play

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

Previous Forecasts in Parentheses

- **Motivation for the FX View: We maintain our EURUSD forecasts for the next four quarters given the countervailing factors of the ECB committing to another hike in July (positive for EUR) and poorer Eurozone economic data (negative for EUR). We think that the EUR will continue on the expected trajectory against the USD, although we recognize that the USD could be better supported on a slowdown in global growth concerns and persistent inflation which could result in continued central bank tightening.**

- Germany is currently experiencing a technical recession, which means it has seen two consecutive quarters of quarter-on-quarter contraction. The combination of a more hawkish Federal Reserve and weaker economic data in the Eurozone has contributed to a negative bias for the EUR. However, we believe that the European Central Bank (ECB) is the central bank that is least likely to finish tightening its monetary policy, and this could have a positive impact on the sentiment towards the EUR. The ECB has committed to another hike in July and is arguably the most hawkish among global central banks, which should bode well for the EUR.

- Furthermore, we anticipate that economic growth in the European Union (EU) and globally will slow down without significant deterioration, potentially supported by China's recovery. If the ECB eventually decides to pause its interest rate hikes later this year, it could be seen as a positive development for the EUR sentiment, as long as the decision is motivated by a desire to control inflation and doesn't lead to a significant decline in growth. It's important to note that this is not our main expectation, but if such a pause occurs, it could be seen as bullish for the EUR, indicating the ECB's commitment to maintaining a balance between inflation control and economic growth.

- This scenario becomes more plausible if other central banks, like the Federal Reserve, also reach the end of their tightening cycles and if Europe's energy situation remains stable while the labor market remains resilient. Overall, we maintain an optimistic view of the EUR's prospects in the medium term, and this is reflected in our expectation for a higher EURUSD exchange rate.

- EURUSD trended higher in Jun on the back of a narrowing in the US-EU 10Y yield differential early in the month on the back of a ECB rate hike (15 Jun) and a Fed pause (14 Jun). The Fed however remained hawkish, and this provided ample support for the USD. We think that the ECB is still the furthest away from pausing and look for this to provide an impetus for a stronger EURUSD, although this could now take a longer time to play out given that divergence with the Fed could now be delayed. 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 an EU recession, or at the very least bode poorer growth prospects for the EU.

- 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.

- In addition, Russian state-linked private military company the Wagner Group had earlier left Ukraine and reportedly marched onto Moscow in a reported mutiny. This was later suspiciously resolved with an agreement between Putin and Belarus leader Lukashenko to allow the Wagner Group into Belarus to avoid all charges. Some political analysts suggest that this could be a ruse to allow the Wagner Group to potentially re-group and march on to Kyiv. This represents a potential escalation in the conflict, and we watch developments on this closely.

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

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

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

- The Federal Reserve has become more hawkish than previously expected by markets and the probability of Fed rate cuts has drastically fallen. 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 or take longer to play out. This would weigh on the EUR and could affect the expected trajectory shown in our forecasts.

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

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

- Final 1Q23 Eurozone GDP growth came in at +1.0% YoY (exp: 1.2%; prev: 1.3%) and -0.1% QoQ (exp: 0.0%; prev: 0.1%). The Eurozone has slipped into a technical recession, and this was largely due to inflation weighing heavily on consumption. Previous estimates had shown that the Eurozone had narrowly avoided a recession with QoQ growth seen as being flat. However, perhaps this view was always naïve, with Germany and several other Eurozone economies now in a technical recession. France recorded close to zero growth, with a flatline growth in 4Q22 and a modest increase of +0.2% QoQ in 1Q23. However, not all is doom and gloom as GDP volumes in the Eurozone are more than 2% higher than the level recorded pre-pandemic in 4Q19. By the same measure, the UK economy is about 0.5% smaller than pre-pandemic levels.

- 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 continued through May as final PMI numbers showed that services remained in expansion at 55.1 (exp: 55.9; prev: 55.1), while manufacturing stayed in contractionary territory at 44.8 (exp: 44.6; prev: 44.8). June Prelim PMIs show that this trend continues, with manufacturing PMI at 43.6 (exp: 44.8; prev: 44.8), while services PMI was at 52.4 (exp: 54.5; prev: 55.1). We note however, that the PMIs are now deteriorating and services could perhaps dip into contractionary territory as well, which could foreshadow slower Eurozone growth prospects in the future as activity declines.

- Meanwhile, Eurozone continues to see a rather stable unemployment rate of 6.5% in Apr (exp: 6.5%; prev: 6.6%). Tight labour market conditions seem to be supportive of household spending and the services sector. May Core CPI inflation printed at 5.3% YoY (exp: 5.3%; prev: 5.3%), while headline inflation was at 6.1% YoY (exp: 6.1%; prev: 6.1%. Price pressures remain sticky and are in line with the ECB view that inflation has remained "far too high for too long". Preliminarily, prices looked to have re-accelerated in Germany with Jun prelim numbers for CPI inflation coming in at 6.8% YoY (exp: 6.8%; prev: 6.3%).

- **Monetary Policy Forecast:** On 15 Jun the ECB raised rates by 25bps to take the deposit facility rate to 3.50%, marginal lending facility to 4.25% and main refinancing rate to 4.00%. 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 position that price pressures remain a concern for the Eurozone.

- The May ECB meeting minutes showed that the governing council recognized that while headline inflation had eased considerably in recent months, upside risks to inflation existed and underlying price pressures remained strong. This formed the basis for their 25bps rate hike at the May meeting in order to ensure that interest rates were at levels that were sufficient to ensure inflation returned to a 2% target in a timely manner. The governing council also recognized the reinforcing effect of a wage-profit-price spiral and that signs of this were emerging in the Eurozone.

- For the rest of 2023, current OIS implied pricing is for a terminal deposit facility rate of 3.90%, with the market implying a total of roughly 40bps more 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 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 narrowed to a €3.6b surplus in Apr (prev: €31.2b). Current account deficit amounted to 0.4% of Euro area GDP or €55b in 12 months to Apr 2023, compared with a surplus of €139b (1.1% of euro area GDP) one year earlier.

- **Key domestic events and issues to watch in Jul:** EC Jun Final Mfg PMI, (3 Jul), EC May Final Services and Composite PMI, EC Apr PPI (5 Jul), EC Apr Retail Sales (6 Jul), Jul Sentix Investor Confidence (10 Jul), Jul ZEW Survey Expectations (11 Jul), EC Apr Industrial Production (13 Jul), EC May Trade Balance (14 Jul), EC Jun Final CPI (19 Jul), May ECB Current Account, EC Jul Prelim Consumer Confidence (20 Jul), EC Jul Prelim PMIs (24 Jul), EC M3 Money Supply (26 Jul), ECB Policy Decision (27 Jul), Economic, Consumer, Industrial and Services Confidence, ECB Survey of Professional Forecasters (28 Jul), EC 2Q Advance GDP, EC Jul Prelim CPI (31 Jul).

- **Technical Outlook:** EURUSD traded at around 1.0869 levels at time of writing. EURUSD has trended higher in Jun, with stochastics flagging overbought conditions but falling, while RSI is neutral. Support is at 1.0820 (100 dma) and key resistance is at 1.10. We see a likely trading range of 1.05 to 1.10 to hold.

GBP: BOE Surprise to be Supportive

Forecast	3Q 2023	4Q 2023	1Q 2024	2Q 2024
GBPUSD	1.2700 (1.2300)	1.2400 (--)	1.2400 (--)	1.2600 (--)

Previous Forecasts in Parentheses

- **Motivation for the FX View: We revise our GBPUSD forecasts higher for one quarter to account for the additional support for the GBP that arises from heightened expectations for the BOE to raise rates. The re-acceleration in core CPI has been worrying, with Governor Bailey also admitting that the UK is in a wage-price spiral**. We expect that the BOE could raise rates by up to 100bps further, and this should provide additional support for the GBP in 3Q2023. However, we also note that the BOE's approach is to demur on providing forward guidance in the fashion that the ECB and Fed have opted to and this is widely seen as dovish. 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 still believe that the cable is fundamentally overvalued at levels above 1.24. Based on this, we see the opportunity to fade rallies in the cable, although this could take a longer time to play out given that BOE hikes will be supportive.

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

- There is a risk that the Fed becomes more hawkish than expected and does not pause. Recent hawkish comments from Fed Chair Powell have underscored this risk. However, expectations for the BOE to tighten remain high and this should moderate the risk of this weighing too much on the cable. There is also the possibility that the Fed is posturing in order to prevent the market from running too far ahead of itself.

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

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

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

- Although the BOE's tightening thus far has been seen as an appropriate response to inflationary pressures that remain elevated and stubborn, there also exists a risk that the BOE overtightens. This could worsen the UK's already difficult economic situation, given that Brexit-related structural problems such as a shortage of skilled labour and disrupted supply chains have contributed to the UK's weak economic performance in recent years. When 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:** Final 1Q20232 GDP growth came in at +0.2% YoY (exp: 0.2%; prev: 0.2%) and +0.1% QoQ (exp: 0.1%; prev: 0.1%). Growth appears to have improved 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 is at 52.5% (prev: 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 May and was hotter than expected at +7.1% YoY (exp: +6.8%; prev: +6.8%), while headline CPI inflation was hotter than consensus at +8.7% YoY (exp: +8.4%; prev: +8.7%%). Price pressures remain persistent at elevated levels and the continued 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 +7.15% YoY (prev: 6.9%) 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:** The BOE surprised and delivered a 50bps rate hike (vote split: 7 hike, 2 maintain) in the last meeting on 22 Jun, bringing the policy rate to 5.00%. Moving forward, we see a total of 100bps of rate hikes for the BOE, and a likely terminal rate of 6.00%. At this point, the market is currently pricing in a 176.6% probability of a 25bps hike at the next 3 August meeting, which implies 76.6% chance of a 50bps hike. Existing inflationary pressures remain strong, with the recent re-acceleration in core inflation and as headline inflation moderated but remains at relatively high levels. We think that the BOE is in a difficult spot and has declined to provide forward guidance to provide itself with some flexibility. Unresolved problems from Brexit could pose more troubles for the BOE in the future. Thee BOE is also cognizant of the risk of overtightening at this point of time, given the prevailing concerns of an overtightening in the Eurozone area.

- **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 Apr Trade Balance stood at a deficit of -£1.5b (exp: -£3.7b; prev: -£2.8b). The trade balance improved as the goods deficit narrowed and the services balance remained in surplus. The trade deficit reinforces the difficulty that the UK is facing in terms of slowing global demand and underscores the importance of access to the EU common market.

- **Key domestic events and issues to watch in Jul:** S&P Jun Manufacturing PMI (3 Jul), S&P Jun Services and Composite PMI (5 Jul), S&P Jun Construction PMI (6 Jul), Jun Jobless Claims, Jun Claimant count, May Avg Weekly Earnings, May ILO Unemployment rate (11 Jul), RICS House Price balance, May Industrial and Manufacturing production, May Trade Balance (13 Jul), Rightmove House Prices (17 Jul), Jun CPI, RPI, PPI (19 Jul), Jul Consumer Confidence, Jun Retail sales, Jun Public Sector Net Borrowing (21 Jul), Jul Prelim S&P PMIs (24 Jul), Jul Nationwide House Price Indices (28 Jul to 3 Aug), Lloyds Business Barometer, Jun Mortgage Approvals, Jun Money Supply (31 Jul).

- Technical Outlook: GBPUSD last trades at around 1.2620 levels at time of writing, having come off earlier lows and trended higher in the lead up to the surprise BOE decision where it hit highs of above 1.28 figure but quickly came off. Support is at 1.25 figure while resistance is the earlier high of 1.2820. Stochastics flags overbought conditions, while RSI is neutral and overall momentum looks to be bearish for the pair.

AUD: Better Levels To Buy Awaits

Forecast	3Q 2023	4Q 2023	1Q 2024	2Q 2024
AUDUSD	0.65 (0.67)	0.68 (0.70)	0.70 (0.71)	0.70 (--)

Previous Forecasts in Parenthesis

- **Motivation for the FX View:** The revision of 2Q 2023 from 0.70 to 0.67 seems to be the correct decision given where AUDUSD is landing at this point. We continue to maintain a mildly bullish profile for the AUDUSD over the next four quarters to head above the 0.70-figure. AUDUSD had risen pretty substantially since the start of Jun, clocking +6.8% gains from its Jun lows to peak. Our call for RBA to hike turned out to be right last month and that set the AUDUSD on the bullish rebound, amplified all the more by Fed's decision to pause its tightening cycle. We do not look for a rate hike in July however, as the central bank had sounded more concerned about household consumption. Instead, the next rate hike could be in Aug and that could be the last in this cycle. Services inflation had been a key concern and RBA may want to raise the cash target rate one more time before Australia enters into peak tourist season towards the end of the year.

- We caution that there is room for bearish retracements in the near-term. RBA is not likely to hike in Jul in our view, as mentioned. In addition, an absence of strong stimulus roll-out from China may mean metals could remain sluggish. That said, we continue to maintain the view that AUD is a buy on dips as we look for China's recovery to be a matter of when and with 11.6mn of Chinese graduates set to hit the labour market from Jun, it is possible, a stimulus package is to be rolled out soon.

- **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 AUD. An unexpected slowdown in Australia's economy or deterioration in its labour market conditions could see RBA lean dovish sooner than expected and spur more AUD depreciation.

- **Growth and Inflation Outlook:** Private capex for 1Q already set a rather bullish tone for the AUD at the start of the month with the survey indicating that companies may be spending a record amount for the FY2023-2024. However, it was the significant upside surprise in the Apr CPI release in late May that spurred RBA to hike rates decisively in early Jun.

- For the rest of the month however, data is mixed with property-loans falling unexpectedly by -2.9%m/m in Apr vs. previous +5.3%, a sign that the rising interest rate environment has started to dampen housing demand. However, CBA household spending jumped +3.1%m/m vs. previous -4.2%, recording a 4.7%y/y growth vs. previous +3.8%. Private consumption could still continue to hold up given that Westapac consumer confidence for Jun rose marginally to 79.2 vs. previous 79.0. This is especially given still-tight labour market conditions with unemployment rate falling to 3.6% in May from previous 3.7% and 75.9k net employment change recorded for May.

- Prelim. PMI for Jun suggests manufacturing remains in contraction at 48.6 vs. previous 48.4. Services fell pretty sharply to 50.7 in Jun from 52.1, albeit still in expansionary territory. RBA may choose to pause at its next policy meeting in Jul to await the next set of data. Any further signs of economic or rather spending resilience would probably nudge the the central bank to hike one last time in Aug.

- **Monetary Policy Forecast:** Our call for RBA to hike turned out to be right last month and that set the AUDUSD on the bullish rebound, amplified all the more by Fed's decision to pause its tightening cycle. Even as RBA had signaled a pause earlier this year and expressed concerns for household consumption, the recent hikes proved that the central bank will still prioritize inflation fighting, especially with the labour market still maintaining its resilience.

- Looking forward, we look for RBA to pause in July, noting RBA's concerns with household spending which had shown mild signs of a slowdown. The next and potentially last hike of the cycle could happen in Aug when the SoMP will also be scheduled for release and we see that as potentially necessary to ensure RBA achieves its inflation mandate of getting inflation back to the mid-point of 2-3% ahead of the peak tourism season during summer.

- Our call for a stand pat on 4 Jul will thus mean that AUD will not be able to get that support from monetary policy decision in the coming weeks. We continue to look for AUD to remain under pressure in the interim but a hawkish pause in rate action could also mean that further declines could be shallow.

- **Latest External Balance Outlook:** As of last available data, current account surplus was recorded at +1.4% of GDP for 1Q 2023, widening a tad from the previous 1.13%. Over the same period, Australia recorded a AUD12.3bn of current account surplus vs. previous A$11.7bn in 4Q

2022, buoyed by the stronger surplus in goods and services trade balances. For Apr, trade surplus narrowed to AUD11.2bn from previous AUD14.8bn - exports fell to AUD56.2bn vs. previous AUD59.1bn. Imports of goods fell to AUD30.8bn from AUD34.8bn.

- **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:**

- Jun Mfg PMI [1 Jul]; Jun M-I inflation, Jun investor loan, home loans , May Building approvals, private sector houses [3 Jul], RBA policy decision [4 Jul]; May trade [6 Jul]; Jun foreign reserves [7 Jun]; Jun CBA household spending, Jun NAB business confidence, conditions, Jul Westpac consumer confidence [11 Jul]; Jul consumer inflation expectation [13 Jul]; Minutes of the RBA Jul meeting [18 Jul]; Jun Westpac leading index [19 Jul]; Jun labour report [20 Jul]; prelim. Judo Bank Composite, Mfg, Services PMI for Jul [24 Jul]; Jun, 2Q CPI [26 Jul], Jun retail sales [28 Jul].

- **Technical Outlook:** AUDUSD could remain under pressure in the near-term. Last at 0.6620. Resitance at 0.6670. Momentum is increasingly bearish based on MAD as well as stochastics. Risks skewed to the near term with support around 0.6560. Resistance at 0.6670.

NZD: Looking for A Recovery, Sans Inflation

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:** We maintain our NZDUSD trajectory towards 0.67 over the next nine months. New Zealand is officially in a technical recession now, defined by two consecutive quarters of economic contraction. GDP fell -0.1%q/q in 1Q after a -0.7% contraction in 4Q of 2022. While we are cognizant that weaker external demand could likely adding pressure on NZ goods trade, it is more likely that we could see some sequential growth for 2Q amid the reconstruction after the cyclones and floods as well as the rise in tourist and migrant rise. Jun business confidence rose to -18 from -31.1 in May, logging another sharp month-on-month improvement based on the survey of business opinion by ANZ. Activity outlook turned positive for the first time since Apr 2022. Business confidence actually hit a low of -70.2 last Dec and remained on a slow creep higher. Based on the survey, there is a sense of cautious optimism, especially after RBNZ signalled the end of its tightening cycle. All these are still conditional on New Zealand's inflation trajectory and 2Q CPI release on the 19th July could be one of the key indicators to watch.

- On the side, a fresh remit was provided to the RBNZ policy committee that includes an expanded "context" section which directs the RBNZ to consider factors including government objectives when it makes interest rate decisions. RBNZ had warned that this could undermine its independence. In addition, both the central bank and the Treasury recommended that the dual objective of maintaining price stability and to support maximum sustainable employment be changed to clarify that price stability should be the committee's primary focus but this recommendation was ignored. The main opposition National Party had vowed to get the central bank to get the central bank back to single mandate (of price stability) if it wins the **general election in Oct.**

- **Growth and Inflation Outlook**: New Zealand is officially in a technical recession now, defined by two consecutive quarters of economic contraction. GDP fell -0.1%q/q in 1Q after a -0.7% contraction in 4Q of 2022. We expect sequential growth for 2Q amid the reconstruction after the cyclones and floods as well as the rise in tourist and migrant rise. Jun business confidence rose to -18 from -31.1 in May, logging another sharp month-on-month improvement based on the survey of business opinion by ANZ. Activity outlook turned positive for the first time since Apr 2022. Business confidence actually hit a low of -70.2 last Dec and remained on a slow creep higher. Based on the survey, there is a sense of cautious optimism, especially after RBNZ signalled the end of its tightening cycle. All these are still conditional on New Zealand's inflation trajectory and 2Q CPI release on the 19th July could be one of the key indicators to watch.

- Another indicator that we watch is household spending and the Westpac consumer confidence actually provided a hopeful picture of 2Q with an improvement to 83.1 from previous 77.7. This improvement in consumer confidence is in line with the rise in business confidence but the level underscores that confidence is still tepid.

- 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:** Since RBNZ raised OCR by 25bps to 5.50% in May and projected this to be the peak in this cycle, there has been neither expectations for a rate hike nor expectations for a rate cut within this year even though New Zealand has entered into a technical recession. We bear in mind that RBNZ expects inflation to come within the 1-3% target by 3Q 2024 and eyes are on 2Q CPI due on 19th Jul for further gauge on the disinflation progress. Outlook is a tad uncertain though amid optimism that reconstruction and tourist arrivals/migrant may keep the labour market from significant deterioration along with the halt in the rate hikes. On the other hand, monetary policy settings are restrictive enough such that these factors do not fan inflation pressures higher.

- *Recall that within the May policy 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:** Meanwhile, NZ current account could remain in deficit given a consistent deficit in its goods trade. Current account deficit narrowed to -NZD5.22bn in 1Q vs. NZD10.1bn in the quarter prior. Services balance have started to swing into surplus and could rise further into 2Q amid the influx of migrants and tourist arrivals. However, goods trade could remain in deficit due to weak external demand. It is unlikely for NZ current account to turn into surplus in the near-term.

- **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:** May Building Premits [3 Jul]; Jun REINZ House Sales [10-14 Jul]; RBNZ Policy Decision [12 Jul]; BusinessNZ Jun Mfg PMI, Jun Food prices [13 Ju]; 2Q CPI [19 Jul]; Jun trade [24 Jul], ANZ Ju; Consumer Confidence [28 Jul]. ANZ Activity Outlook, Business Confidence, CoreLogic House Prices for Jul [31 Jul].

- **Technical Outlook:** NZDUSD crept higher and was last seen around 0.6080. Risks in the near-term is still skewed to the downside based on momentum indicators. Next support is seena round 0.5990. Resistnace at around 0.6170. Longer-term, monthly shows bearish momentum is mild and stochastics are rising from oversold conditions.

CAD: Downside Pressure for Now

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

No Change to Previous Forecasts

- **Motivation for the FX View:** We continue to maintain our forecast levels and trajectory for the CAD as we look for USDCAD to remain mostly within the range of 1.30-1.35 for the next few weeks with risks skewed to the upside in the near-term as inflation had slipped close to the top end of BoC's 1-3% target inflation range, last printed 3.4%, rendering more rate hikes less likely. At the same time, Fed Powell's mention of back-to-back hikes had generated some hawkish re-pricing that add support for the USDCAD. Into the next four quarters, we still look for the pair to drift towards the bottom of the range, around the 1.30-figure as we look for easing inflation in the US to eventually mellow the hawkish Fed.

- 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:**

- CFIB business barometer for Canada turned out to be lower at 54.1 vs. previous 56.4 – a sign that small businesses are less optimistic when they were surveyed in Jun. Breakdown suggests that average price plans and wage plans are expected to ease while hiring intentions have also decreased. More of the businesses see insufficient demand as a limitation on sales and fewer see shortage of skilled labour as limitations.

- Labour market conditions showed some signs of softening with a fall of 32.7K ful time employment on net for May while part-time employment rose 15.5K. Participation rate eased only a tad to 65.5% from 65.6%. Unemployment rose to 5.2% from previous 5.0% while wage growth eased to 5.1%y/y from 5.2%. The CFIB survey suggests that hiring conditions could start to weaken a tad more.

- Housing starts also fell to 202.5k for May vs. previous 261.4K, a 23% drop, underscoring weakening construction sector amid high interest rates and concomitantly decline in demand. May CPI eased to 3.4%y/y from previous 4.4%, within expectations. Much of the deceleration was due to the softening pace of price increase for energy prices. However, groceries, food and mortgage interest rate cost actually remained elevated. It was core inflation (average of trim and median core) that spurred a rally in the USDCAD with a deceleration to 3.85% from previous 4.25%. This was lower than median estimate of 3.95%. Even as inflation remains above the 1-3% inflation target, BoC may still want to take into account recent surveys and pause on 12 Jul to better assess the economic conditions before making its next move.

- **Monetary Policy Forecast:** BoC is expected to keep rates unchanged at 4.75% on 12 Jul and we too see a point in pausing to allow more information and data to come through before BoC makes its next move. While the inflation target is not yet achieved, there is certainly progress. Consumption may look strong based on the recent retail sales print at 1.1%m/m but that was for Apr. The CFIB business survey seems to suggest that demand conditions might have softened already. We are thus of the view that BoC may not even need to hike any more this year.

- **Latest External Balance Outlook:** As of last available data, Canada's current account balance was at a deficit of -U$14.2bn for 1Q23, wider than the -U$6.6bn deficit for 3Q. Trade balance 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 Jun [4 Jul], Int'l trade for May [6 Jul]; Jun labour market [7 Jul]; BOC Policy Decision [12 Jul], Jun housing starts [18 Jul]; Jun CPI [18 Jul]; May retail sales [21 Jul]; CFIB Business Barometer for Jul [27 Jul]; May GDP [28 Jul].
- **Technical Outlook:** USDCAD is resisted by the 21-dma at 1.3278 and we cannot rule out further move higher towards 1.3420 (51-dma). Stochastics are rising from oversold conditions. MACD is still turning more bullish. Support around 1.3160 before the 1.30-figure. 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	3Q 2023	4Q 2023	1Q 2024	2Q 2024
USDJPY	145 (137)	**142** (133)	**140** (131)	**133** (-)

Previous Forecasts in Parentheses

- **Motivation for the FX View:** The USDJPY climbed higher this month as DM central banks looked to be extending their hiking cycle for longer in their battle against inflation. At the same time, the BOJ remains stubbornly dovish as they do not appear to be sufficiently convinced that inflation can rise sustainably in Japan given wages are not showing signs of pick-up. Additionally, market functionality has substantially improved reducing the urgency for the BOJ to adjust YCC. The current situation as we see it though is unlikely to shift too quickly and this could result in the JPY facing an extended period of weakness in the coming months. Consequently, we have raised our USDJPY forecasts upwards. We do note that there is a strong possibility that the Japanese government via the BOJ could intervene in the market soon but we believe that an intervention by them would likely keep the USDJPY between a range of 140 – 150 in the interim.

- **Growth and Inflation Outlook:** The 1Q GDP second reading saw quite an upward revision to 2.7% QoQ from an initial 1.6% QoQ. The revised reading was much higher than the market estimate at 1.9% QoQ. The main driver behind the higher reading was the much larger contributions from private inventory investment. However, scrutinizing the details, we see that inventory of work in progress grew sharply in the second reading. The inventory of work in progress in the initial GDP reading was actually estimated through ARIMA modeling whilst in the second reading, calculation was done on the basis of using financial statements statistics of corporations by industry. As this kind of represented a calculation methodology difference, we do not see this contributing component as to shifting our judgement on the economic situation. Meanwhile, private capex also played some part (though to a lesser extent) in the revision. This does strengthen our view that capex could play a substantial part in driving growth forward. Capital spending itself rose by an astounding at 11.0% YoY (est. 6.0% YoY and 4Q 2022. 7.7% YoY). Overall, we continue to see strong economic recovering throughout the rest of this year.

- Headline inflation for May slowed but fell in line with expectations to 3.2% YoY (est. 3.2% YoY and Apr. 3.5% YoY). The core number similarly decelerated but was below estimates at 3.2% YoY (est. 3.1% YoY and Apr. 3.4% YoY). The core core number in contrast both picked up further and beat the consensus forecast at 4.3% YoY (est. 4.2% YoY and Apr. 4.1% YoY). The main driver behind the numbers again was a strong core food inflation reading at 9.2% YoY that itself was likely a result of the rise in feedstuff prices and the spread of the avian flu. Other categories that contributed to the readings included non-durable goods. Energy was a negative feeder again for the month as electricity and city gas saw downward contributions. Going forward, it looks like core food could continue to remain a positive contributor given other indicators are still showing foodstuff prices on the rise. Energy could start to be an upward contributor too as seven main electric companies are expected to raise their electricity charges. However, we are not getting the impression inflation as a whole at this point appears to be demand driven. Instead, it continues to appear that supply side issues are a major contributing factor. For that matter, data in April is not showing any discernible pick-up in wages as labour cash earnings only rose by 1.0% YoY (est. 1.8% YoY and Apr. 1.3% YoY) whilst real earnings was negative at -3.0% YoY (est. -2.0% YoY and Apr. -2.3% YoY). Given the emphasis the BOJ places on the need for wage pick-up and demand driven inflation, it is challenging to see the economic situation providing much of a case for any form of tightening adjustment. Meanwhile, June Tokyo CPI which provide a more updated reading of price conditions all fell below expectations. Such circumstances are likely to keep weighing on the JPY.

- High frequency indicators such as June (P) Jibun Bank Mfg PMI fell into contraction territory at 49.8 (May. 50.6), which was the first drop in four months. The output index, new orders index, the suppliers' delivery times index and the stock of purchases index all weighed on the headline number. The next export orders index also fell. The readings overall could be some reflection of a weakening in the global goods trade and a downturn in the China economy. The services PMI meanwhile also declined slightly to 54.2 (May. 55.9). Given that it still remains in expansion territory, we are not too concerned about the reading and that there continues to be strong activity in that sector with the reopening of the economy since the end of the pandemic. Gradually though, the services PMI may eventually stagnate and even fall as the effects of the economic reopening wanes. Overall, the indicators in our view highlight the fragility of the economy and this can only work against any hopes for a BOJ tightening from an economic perspective.

- Retails sales in May turned around from a decline to come out at 1.3% MoM (est. 0.8% MoM and Apr. -1.2% MoM). The positive figure was driven by pharmaceuticals and cosmetics, household appliances, fuel and food & beverages. General merchandise, autos and fabrics, apparel & accessories weighed down on the reading though. As the economy continues to benefit from the reopening this year, retail sales are likely to keep holding up, feeding into economic growth. However, inflation meanwhile is still appearing to more driven by supply side issues than it is regarding by this stronger demand as exemplified by robust retail sales growth.

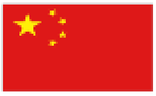
- **Monetary Policy Forecast:** On this front, BOJ Governor Kazuo Ueda seems to continue to express a stubbornly dovish tone. BOJ is showing limited signs of even considering any shift near term. He has said that the central bank would be patiently maintaining easing. Recently, he has mentioned that it would be possible for a normalization in monetary policy if the BOJ becomes confident that inflation can pick up next year. However, he does not appear confident that price pressures can pick up as he mentioned that they are "forecasting some increase in the rate of inflation into '24" but "they are less confident about the second part". For now, he also said that whilst inflation has risen more than 3%, "which is well above the 2% inflation target", they also "think underlying inflation is still a bit lower than 2%". Regarding the YCC, he has commented that the "side-effects have been lessening somewhat". Compounding this dovish tone, the actual underlying economic and market case do not support a BOJ adjustment any time soon. Market functionality issues have significantly eased and inflation and wage data are not justifying any move. A YCC adjustment we now think may instead come in 2024. Overall, this continued easy monetary stance is going to keep weighing on the JPY especially at a time when other global DM central banks are looking to extend their hiking cycle.

- Meanwhile, intervention now looks more likely to happen soon especially and would come at probably around the 145.00 – 150.00 level for the USDJPY. Language from government officials now look much stronger too with both the Finance Minister Shunichi Suzuki and Vice Finance Minister Masato Kanda claiming they are watching the market with "urgency" and that they see recent moves as "rapid and one-sided". Intervention however we see would likely keep the USDJPY fluctuating around a range of 140.00 to 150.00. However, the BOJ will also have to limit the amount of intervention it does. Japan is still considered a free-floating country by an IMF report and the US Treasury has not labeled the country as a currency manipulator. The IMF criteria states that "intervention has been limited to at most three instances in the previous six months, each lasting no more than three business days" whilst the US treasury "assess net purchases of foreign currency, conducted repeatedly, in at least 8 out of 12 months, totaling at least 2% of an economy's GDP". Given these conditions, if macro conditions move much more against expectations in a negative way towards the JPY (e.g. the Fed hikes two times more instead of just one more time), then the BOJ may have to allow the USDJPY to move above 150.00 as they refrain in engaging in excessive intervention by this point.

- **Latest External Balance Outlook:** The country's trade deficit for May widened to 1.37 trillion Yen (Apr. -436.4bn Yen) as imports decline less than expected at -9.9% YoY. Exports did grow above estimates at 0.6% YoY (est. -1.2% YoY) but this was insufficient to offset the imports. Going forward, there are little expectations for exports to perform better given the lackluster China economic recovery and weakness in manufacturing in Europe and the US. Imports on the other hand could also fare worse going forward given concerns about global economic weakness but it may not do enough to offset underperformance in exports. The risk that Japan fails to turn around a trade deficit this year is high and this could keep weighing on the JPY.

- **Key domestic events and issues to watch:** 2Q Tankan large and small indexes (3 July), May Labour cash earnings (7 July), May household spending (7 July), May (P) Leading/Coincident index (7 July), May BoP CA balance (10 July), June Bank lending (10 July), June (P) Machine tool orders (11 July), June PPI (12 July), May Core machine orders (12 July), May Capacity utilization (14 July), June Nationwide dept sales (14 – 21 July), June Tokyo dept store sales (14 – 24 July), May Tertiary industry index (18 July), June Trade data (20 July), June CPI (21 July), Jul (P) Jibun Bank PMI indexes (24 July), June PPI services (26 July), Jul Tokyo CPI (28 July), BOJ Policy decision (28 July), June Annualized housing starts (29 July), June Retail sales (31 July), June Dept store, supermarket sales (31 July), June (P) IP (31 July), Jul Consumer confidence index (31 July) and June Housing starts (31 July).

- **Technical Outlook:** The pair is hovering just below the 145.00 level, which marks the start of a range between 145.00 – 150.00 where BOJ intervention is very likely to happen. Consequently, 145.00 marks the key resistance level with the next after that at 150.00 and 151.95 (2022 high). Support is at 140.00, 138.81 (50-dma) and 135.00 (psychological level). Bullish trend channel is intact. Momentum indicators are looking stretched on the upside which implies some near term reversal. USDJPY could climb a bit more before coming back down again amid an intervention. It would eventually fluctuate between the 140.00 -150.00 range near term.



RMB: Yuan Bears May Need to Tread Carefully

Forecast	3Q 2023	4Q 2023	1Q 2024	2Q 2024
USDCNY	**7.15** (7.05)	**7.10** (6.95)	**6.95** (6.95)	**7.00** (--)
USDCNH	**7.15** (7.08)	**7.10** (6.95)	**6.95** (6.95)	**7.00** (--)

Previous Forecasts in Parenthesis

- **Motivation for the FX View:** USDCNY and USDCNH now print around 7.24 towards the end of Jun, a reflection of growth concerns and disappointment on a lack of clarity on stimulus plans from the government. We raise our forecast once again to 7.15 for both onshore and offshore pairings to take into account this delay but maintain our moderately bullish trajectory for the yuan against the USD in 4Q 2023. **We caution against turning too bearish on yuan at this point as we believe that a stimulus package is in the making and could be communicated soon.**
- We anticpate business-friendly policies to be in the plan, spending on infrastructure projects, further measures to support property demand such as lower mortage rates or downpayments in second/third tier cities. Tax relief, better social security coverage (healthcare/education) would be positive for migrant workers. Late last year, Zhengzhou was already removing barriers to hu kou registration in the city and more of such hu-kou related reforms could support consumption, investment as well as boost efficiency, productivity as China's population ages. We still look for a consumption-led recovery, notwithstanding an absence of a growth plan in the near-term. However, a possibility of some level of consumption-led recovery in the latter half of 2H (that could boost imports of goods and services) could weaken its external balance. On net, we look for appreciation against the USD then but some pressure on the trade-weighted perspective. Meanwhile, we look for USD yields to come off into the tail end of this year. That could be another reason for the USDCNY and USDCNH to drift lower in the tail end of 2H.
- **Growth and Inflation Outlook:** We still look for a consumption-led recovery over the next 6-12 months, notwithstanding a lack of clarity on that front in the near-term. Holiday spending over the Dragon Boat weekend was reported to be under pre-pandemic levels, a deterioration from spendings over Labour Day holidays which were marginally above 2019's. This could suggest that retail sales could continue to weaken for Jun from 12.7%y/y recorded for May. There are a few reasons for weak sepnding – sluggish property sector, gloomy economic outlook that crimps on hiring and threaten job security. Even as the Chinese government aims to refrain from stimulating the economy via the property sector, a further deterioration would have a negative wealth effect on household spending. At this point, supply and demand conditions are both weakening – declines in floor sales sold

observed in Jun, smaller rise in new home prices. fall in land bids and construction by developers and rise in USD debt defaults by developers.

- One of the most concerning issue is youth unemployment which reached a record high in May. To address that, the Ministry of Human Resources and Social Security is said to launch a six-month campaign from Jul to boost youth employment. The authorities will provide career guidance, skills training, job referrals and internship opportunities during the campaign. Focus will be employment in advanced manufacturing, modern services and other fields. This is likely to address the record high youth unemployment seen in May in light of another 11.58mn of graduates hitting the job market from Jun.
- 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. Chinese households may take longer than the rest of the world to regain the confidence to spend after re-opening but enough stimulus is also required.
- **Monetary Policy Forecast:** PBoC cut key policy rates by 10bps in Jun including 7-day reverse repo, 1Y MLF. 1Y and 5Y LPRs are also adjusted lower accordingly, a sign of good transmission. Our economist believes another rate cut could be in the offing but likely to be towards the end of the year. Regardless, monetary policy easing may not boost credit demand as long as consumer and investors remain fearful of a deeper economic downturn. Earlier, there are whispers of banks being asked to reduce deposit interst rates in order to encourage the flow into investments. Expectations for further monetary policy easing without a fiscal stimulus could only add pressure on the yuan amid divergence from other key central banks.
- **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.
- Total fiscal spending on services and infrastructure seem to have hardly grown this year (around only 1%y/y) as the government becomes more careful about the fiscal budget this year. That is probably why the GDP growth is only set at around 5% for 2023. However, the officials have been mentioning “forceful stimulus”, “effective” measures and greater spending on infrastructure would be one of the most direct and effective way to stimulate demand. The 3% budget deficit target might still be breached this year.
- Exports actually contracted in May by -0.8%y/y while imports fell -4.5%. Trade surplus narrowed to $65.81bn from $90.2bn previously. Narrowing goods trade surplus could add pressure on the yuan

especially in light of the persistent debt outflow seen (based on IIF data).

- **Key domestic events and issues to watch:** Caixin Jun 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: Risk of Lagging on China Lingers

Forecast	3Q 2023	4Q 2023	1Q 2024	2Q 2024
USDKRW	1300 (1280)	1280 (1270)	1270 (1260)	1250 (1260)

Previous Forecasts in Parentheses

- **Motivations for the FX View: We revise our forecasts for USDKRW higher for the next four quarters, although we remain positive on the trajectory for the KRW. This is in line with our view that the USD could remain better supported for longer on a more hawkish Fed as well as a China recovery that has hitherto flattered to deceive.** We think that this means China's reopening and the expected benefit to the KRW could take longer to play out, while the more hawkish Fed should weigh on the KRW. Our upward revision of forecasts reflects this. However, we also note that there are nascent signs of an improvement in export numbers for Korea and the latest 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-related computations require memory chips that Korean companies such as Samsung and SK Hynix specialize in producing. We therefore maintain the expected downward trajectory of the KRW against the USD.

- Jun has been a tale of two halves for the KRW. USDKRW trended lower into the first half of the month and touched a low of 1268.90 on 16 Jun in the lead up to the FOMC decision. However, it trended higher and hit a high of around 1325 levels as better US data supported hawkish

Fedspeak as Fed Chair Powell claimed that two consecutive hikes were still possible even though the Fed had paused. We think that there is a reasonable chance that this narrative continues for a while and have made upward revisions to our forecasts to account for the potentially firmer USD moving forward.

- 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 as the expected inflows from benchmark investors should drive the KRW stronger.

- Meanwhile, while the Fed has paused on raising rates, Fed Chair Powell has been exceptionally hawkish and this has finally resulted in market pricing in fewer cuts and an increase probability of Fed rate hikes moving forward. We believe that future US inflation prints, most importantly the Fed's preferred core PCE indicator will be key. The BOK had earlier paused on its tightening and has provided hawkish forward guidance for its future actions, should data warrant a rate hike. On the whole, should price pressures moderate from current levels, growth slow down but not tank and central banks end their tightening cycles, the global macro environment would be positive for the KRW moving forward.

- While our revision of our forecasts for China were driven by lacklustre economic data, we think it is possible that China's reopening sets in albeit at a slower than previously anticipated 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 reopening when it happens.

- **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 should oil prices spike once again. OPEC once again cut production early in Jun, with total cuts of 3.6m barrels per day (bpd) or 3.6% of global demand on the cards. Saudi Arabia has telegraphed production uts to 9m bpd in Jul from around 10m bpd in May. 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 quickly, especially if OPEC continues to cut production.

- **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 preliminary GDP figures showed that the Korean economy likely grew by +0.9% YoY (exp: 0.8%; prev: 0.8%) and +0.3% SA QoQ (exp: 0.3%; prev: 0.3%).

- 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. The South Korean government (Finance Ministry) has been mulling cutting their GDP forecasts, but for now this remains at 1.6% for 2023. This move has been mentioned by both Finance Minister Choo as well as other unnamed Finance Ministry officials.

- 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.

- The latest 20-day trade figures further support the narrative that exports could have found a bottom as exports in 20-days leading to 21 Jun rose +5.3% (prev: -16.1%) while imports fell -11.2% (prev: 15.3%). We watch the next trade data print on 1 Jul for further clues on how the export situation will evolve for South Korea.

- South Korea's unemployment rate in May came in at 2.5% (exp: 2.7%; prev: 2.6%), indicating that the labour market continues to be resilient and remains healthy. Meanwhile, May Industrial Production came in at -7.3% YoY (exp: -8.6%; prev: -9.0%), showing a decline in manufacturing activity that was in line with the BOK's downward growth revisions. On an SA MoM basis however, May Industrial Production improved +3.2% (exp: -0.9%; prev: -0.6%), which should be taken as a positive.

- 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, May headline CPI inflation cooled to +3.3% YoY (exp: 3.4%; prev: 3.7%), while core CPI inflation moderated very slightly and showed signs of stickiness at +3.9% YoY (prev: 4.0%).

- **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. They may mention upside risks to inflation and the persistence of inflation above their target, but could opt to delay the hike to a further date.

- 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 May came in at a -US$2.1b deficit, improving on the -US$2.6b deficit in Apr. Should chip demand eventually pick up, the trade balance should improve and this should provide a significant tailwind for the KRW. However, there are signs that China's reopening effects could be delayed and this could weigh on the trade outlook for South Korea. In addition, the US has continued to be hawkish on China in terms of rolling out chip measures, which could also dampen the outlook for chips and exports for South Korea, which would be negative for the KRW.

- **Key domestic data and events to watch in Jul:** Jun Trade (1 Jul), Jun S&P Mfg PMI (3 Jul), Jun CPI (4 Jul), Jun FX Reserves (5 Jul), May BoP Goods/Current Account Balance (7 Jul), Jun Unemployment Rate SA (12 Jul), BOK Policy Decision, Jun Import/Export Price Indices (13 Jul), May Money Supply (14 Jul), Jun PPI, Jul 20-Days Exports/Imports (21 Jul), 2Q Advance GDP (25 Jul), Consumer Confidence, Retail Sales (26 Jul to 31 Jul), Jun Industrial Production (28 Jul).

- **Technical Outlook:** USDKRW last traded at 1318.25 levels. Momentum, stochastics and RSI are all at neutral levels but rising. 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: Heightened Probability of Technical Recession

Forecast	3Q 2023	4Q 2023	1Q 2024	2Q 2024
USDSGD	**1.3350** (1.3150)	**1.3250** (1.3050)	**1.3250** (1.3050)	**1.3150** (1.2950)

Previous Forecasts in Parentheses

- **Motivation for the FX View: We revise our USDSGD forecasts slightly higher to account for the heightened probability of a technical recession in Singapore. Our economists see the base case for MAS to continue to stand pat at the Oct meeting amid persistent price pressures but see a small probability that MAS could ease given that a technical recession is now likely.** In addition, we see that China's reopening effects could take longer than expected to come into play, although we maintain our view on the trajectory for USDSGD to move lower.

- On 14 April, MAS stood pat and left policy settings (slope, centre and width) unchanged. This is the first stand pat after a series of five tightening moves that began in October 2021. This decision goes against our expectations for a tightening via a re-centre upwards, given that core inflation remained well above MAS' comfort levels. In our view, this was largely due to MAS' inflation outlook being more sanguine and expectations for growth being more pessimistic than we had expected.
- The trajectory for a lower USDSGD remains intact in line with our view that China's reopening should eventually come in, albeit at a delayed basis. 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 earlier thought that there was a risk that the Fed remains hawkish after a pause and this has materialized. The risk now is that global growth slows down and price pressures remain strong, which should be overall favourable for the USD in the long term. We think that the SGD NEER will continue to remain resilient we saw SGD NEER actually trade firmer in Jun at around 1.15% to 1.65% above the mid-point. The SGD NEER had earlier remained resilient in times of USD strength and in this month of some USD weakness, the SGD NEER has actually firmed and traded higher.
- 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. In particular, they see a heightened risk of a technical recession in 2Q23 and expect flash 2Q GDP to print at -0.8% YoY implying a technical recession.

- The manufacturing contraction continues as May Industrial Production came in at -10.8% Yoy (prev: 6.5%), the worst level since Nov 2019. In SA MoM terms, Industrial Production fell -3.9% (exp: 2.6%; prev: -1.6%), deeper than April's contraction. All clusters recorded YoY output declines, with the exception of transport engineering and the biomedical manufacturing sector.

- 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.

- May CPI inflation prints showed that core inflation moderated, but remains sticky at levels well above MAS' comfort zone at 4.7% YoY (exp: 4.7%; prev: 5.0%) while headline CPI inflation moderated to 5.1% YoY (exp: 5.4%; prev: 5.7%). Moderating services and food inflation offset firmer utilities costs, while private transport and accommodation costs both eased. 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 if upside imported inflation risks materialize. Our economists see a small probability that MAS could ease to support the economy in Oct, especially given the likely technical recession that Singapore is in. The base case for MAS to stand pat however, remains intact.

- This latest decision was in line with the narrative that the Fed and other central banks around the world are coming to an end of the tightening cycle. Should global inflation trends indeed show a significant deceleration in core inflation prices, we 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.

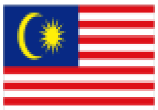
- The FY2022 deficit meanwhile was smaller than projected at 0.3% of GDP or SGD2bn (vs initial projections of 0.5% of GDP or SGD3bn). Draw on reserves was also lower than initial estimations at SGD3.1bn (vs expectations of SGD6bn). The overall drawdown from past reserves from FY2020 to FY2022 totaled 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 May continued to be weak as NODX came in at -14.7% YoY (exp: -7.7%; prev: 9.8%) and by -14.6% SA MoM (exp: -1.9%; prev: 2.6%). Electronics exports remained weak at -

27.2% (prev: -23.3%). 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 at 18.52% of GDP (4Q2022: 19.3%). Singapore's current account has remained in a structural surplus and short term (quarterly) fluctuations are not expected to have a material impact on the SGD.

- **Key domestic events and issues to watch in Jul:** 2Q23 Prelim URA Private Home Prices, Jun Purchasing Managers Index, Jun Electronics Sector Index (3 Jul), Jun S&P Singapore PMI, May retail Sales, COE Bidding (5 Jul), Jun FX Reserves (7 Jul), 2Q Advance GDP (10 Jul to 14 Jul), Jun NODX and Electronics Exports (17 Jul), COE Bidding (19 Jul), Jun CPI (24 Jul), Jun Industrial Production (26 Jul), Jun Unemployment Rate (27 to 28 Jul), 2Q Final URA Private Home Prices (28 Jul), Jun Money Supply (31 Jul).

- **Technical Outlook:** USDSGD last traded at 1.3560 levels. We see supports for USDSGD at the 1.35 levels, while resistances are at the 1.36 figure. RSI and stochastics are rising and nearing overbought levels. Momentum remains bullish and we see two-way risks for the pair moving forward. USDSGD likely to keep within a 1.32 to 1.38 range.



MYR: Domestic and External Alignment for a Turnaround

Forecast	3Q 2023	4Q 2023	1Q 2023	2Q 2024
USDMYR	4.60 (4.40)	4.50 (4.25)	4.35 (4.20)	4.20 (--)

Previous Forecasts in Parentheses

- **Motivation for the FX View:** The MYR trade weighted BIS Index has fallen around 4% ytd, the weakest in the region. USDMYR has risen around 6.2% ytd and reached a high of around 4.6950 on 26 June 2023 vs low of 4.2200 on 27 Jan. It edged higher in June as sentiment to the currency (and for that matter other EM FX) took a hit due to a number of negative external developments, in particular continued CNY weakness amid expectations of a 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. Domestically, part of the lackluster demand for MYR assets could be in part due to cautious market participants who may also be waiting for the completion of the upcoming state elections as early as Aug this year before committing to investment commitments.

- Overall, balance of payments data highlights concerns about net FDI being significantly lower than historical standards. Net portfolio flows have remained positive with some renewed interest into Malaysia's bond market but that has been offset by net foreign equity outflows this year whilst others in the region including Indonesia, India for example saw inflows. Amidst all these, the current account balance (trade drivers) remains a pillar of support.

- However, whilst the global situation looks unfavourable at this point, we do not expect these developments to keep persisting until year end. The Fed could also eventually soften its stance closer towards year-end as inflation gradually falls. China we believe would show more discernible level of recovery over the tail end of 2023 and we factor in some significant level of targeted stimulus to help the economy and that should give a boost to commodities' prices eventually. Domestically, the state elections may conclude by 3Q 2023 and thereafter if the results lend credence to extended stability of the current government could see positive effects on both cold (FDI) and hot (equity+ bond) portfolio flows and coupled with eventual Fed pause and softer USD expectatons may lead exporters starting to sell their USD holdings from export proceeds, which may have grown. All these are possible scenarios which may materialize in the latter part of 2H 2023 and we are factoring it into our MYR forecasts.

- **For the remainder of the year, we are revising our forecast upwards to factor the USD staying firmer longer than we initially expected and to factor in part the delay in the China stimulus.**

- Last month we had highlighted that BNM has also noted that the ongoing developments in the global financial markets have weighed down on market sentiment. BNM has emphasized that the movements in the MYR would be market determined and that they will continue managing 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. We are mindful though that based on BIS NEER MYR levels, has weakened most in the region and if current trend persists would suggest and extended undervaluation of the MYR NEER.

- Overall, BNM 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. More recently, BNM signaled after markets closed on Wed 28 June that it will intervene in the foreign exchange market to stem movements that are deemed excessive. We see this as efforts to stem excessive volatility in the currency and from the trade weighted index perspective to come in if the NEER levels are not in line with fundamentals. In addition, our economics team are also expecting another OPR hike of 25bps either in July or Sep MPC which may help support MYR. From a macro policy mix perspective, any clear future long term structural policy and fiscal rebalancing strategies could also help encourage future FDI and portfolio investment interests and support the currency.

- If the MYR weakness intensifies it may also affect the inflation objectives of the current monetary policy stance and so inflation-output tradeoffs thresholds may lead to eventual leaning against the wind activity. Thus far a flexible MYR exchange rate system has helped Malaysia as a shock absorber without seeing price levels seeing the need to adjust sharply. However, the extent of currency undervaluation and moves too much away from its economic fundamentals may need to be addressed before it affects the real economy significantly.

- 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.

- **Growth and Inflation Outlook:** 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.

- Five months into the year, exports and imports dropped by -2.3% YoY (2022: +25.0%) and -1.0% YoY (2022: +31.3%) respectively, pointing to headwinds from the economic downturns in US and Europe given the slowdown in exports to US (5M2023: +2.5% YoY; 2022: +17.8% YoY) and drop in shipments to EU (5M2023: -9.4% YoY; 2022: +21.8% YoY), while the expected positive impact from China's zero COVID-19 policy exit and full economic opening has yet to materialise amid slump in exports to China (5M2023: -8.9% YoY; 2022: +9.5% YoY). In addition, commodity export prices have softened year-to-date, amplifying the kicking in of base effect, after last year's surge in commodity prices in the wake of Russia-Ukraine war. Currently, our economics team expect full-year exports and imports to decline by -2.0% (5M2023: -2.3% YoY; 2022: +25.0%) and -0.5% (5M2023: -1.0% YoY; 2022: +31.3%) respectively and trade surplus of +MYR231b (5M2023: +MYR92.4b; 2022: +MYR255.5b).

- Headline inflation rate eased further to +2.8% YoY in May 2023 (Apr 2023: +3.3% YoY; MIBG estimate: +2.8% YoY; 5M2023: +3.4% YoY; 2022: +3.3%). But core inflation down only slightly to +3.5% YoY (Apr 2023: +3.6% YoY; 5M2023: +3.8% YoY; 2022: +3.0%). Our 2023 inflation rate forecast of +3.0% assumes monthly inflation stays sub-3% for rest of the year, mainly on base effect, although inflation risk is biased to the upside especially amid fluid subsidy policy and weak Ringgit.

- Maintain our 2023 inflation forecasts at +3.0% as we expect monthly inflation rate to stay sub-3% YoY for the rest of the year, mainly on base effect. However, inflation risk remains biased to the upside amid the fluid policy on price subsidies and controls, as per the implementation of targeted electricity subsidy starting this year that exclude non-domestic, non-MSME as well as medium and high voltage electricity users, with plans to exclude high-income group from electricity and fuel subsidies next year.

- **Monetary Policy Forecast:** Despite the easing headline inflation, core inflation – which BNM describes as the "proxy" of demand-pull inflation

– remains sticky. Thus, we are not ruling out another +25bps hike in BNM's OPR to 3.25% - potentially at the next MPC meeting on 5-6 Jul 2023 - from current 3.00% (which was raised by +25bps at 2-3 May 2023 MPC meeting). Current 3.00% OPR is described by BNM as "slightly accommodative" and the latest Monetary Policy Statement (MPS) mentioned about the need to ensure monetary policy stance is appropriate to prevent the risk of future "financial imbalances". BNM did not specify what are the "financial imbalances" risks, but current state of MYR and interest rate differentials vs major currencies and benchmark interest rates - especially given Fed's hawkish pause with guidance of additional +50bps hikes - may well be the relevant factors.

- **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:** Exports and imports registered softer declines in May 2023 i.e. -0.7% YoY (Apr 2023: -17.6% YoY) and -3.3% YoY (Apr 2023: -11.1% YoY). Trade surplus rose to +RM15.4b (Apr 2023: +RM12.6b). Currently, we expect full-year exports and imports to decline by -2.0% (5M2023: -2.3% YoY; 2022: +25.0%) and -0.5% (5M2023: -1.0% YoY; 2022: +31.3%) respectively and trade surplus of +MYR231b (5M2023: +MYR92.4b; 2022: +MYR255.5b).

- **Key domestic events and issues to watch:** S&P Global PMI MFG (3 July), BNM Policy Meeting (6 July), June Foreign reserves (7 and 24 Jul), May Manufacturing sales, May IP (12 July), June Trade data (20 July) and June CPI (24 July).

- **Technical Outlook:** USDMYR last traded at 4.6610 levels with stochastics flagging overbought conditions. Support is at 4.6250 while resistance is at 4.70 and 4.75 (Oct-22 high) further to the upside. Momentum indicators are neutral as bullish momentum has some what waned.

IDR: Resilient Amid Global Uncertainty

Forecast	3Q 2023	4Q 2023	1Q 2024	2Q 2024
USDIDR	15,000 (14,700)	14,900 (14,500)	14,700 (14,400)	14,600 (--)

Previous Forecasts in Parentheses

- **Motivation for the FX View:** The IDR has seen some weakness recently as the pair crossed above 15,000 mark after having spent quite a period below it. Initially, investors had found IGBs appealing given the country's robust fundamentals (resilient trade surplus and disciplined fiscal management) in addition to easing inflation boosting real yields and raising speculation that BI would be the first to cut. However, with the Fed forecasting two more hikes whilst other DM central banks including the RBA, BOE, BOC and ECB looking to a few more more hikes (amid stubbornly high inflation), investors may have taken some chips off the table, exited IGBs. This henceforth weighed on the IDR recently. The anxiety surrounding the extent of which central banks would keep hiking before hitting terminal is likely to weigh on sentiment for some time into the third quarter. Consequently, we therefore think that the path downwards for the USDIDR may be slower than we had initially expected, which has necessitated upward revisions to our forecasts.

- **Growth and Inflation Outlook:** Our in-house economists continue to maintain their GDP forecasts at 5.00% YoY for 2023 as they expect domestic demand to remain steady in addition to seeing some boost from election-related spending in 2H 2023. Additionally, President Jokowi has declared 28 – 30 June as collective Eid leave to create a 5-day weekend which could encourage travel and consumption and provide support to the economy. Meanwhile, exports could see some slump in the coming months given lower commodity prices compared to the prior year. However, the trade balance should still be in surplus due to lower global oil prices, which should at least prevent it from weighing negatively on the GDP growth.

- Headline inflation in May surprised on the downside at 4.00% YoY (est. 4.21% YoY) and hit the top end of the target range (2 – 4%) earlier than Bank Indonesia's (BI) expectations. BI had initially expected inflation to only reach the target range by the third quarter. The easing in inflation in May had been heavily driven by the deceleration in both the volatile food and energy categories. This was a result of the high base last year where both food and energy prices had climbed amid the Ukraine conflict. Price of Pertamina Dex alone was reduced by -5.2% from the prior month, in line with easing global oil prices. The government has also been taking active measures to stabilize food price and ensure food security. These include distributing subsidies to poultry farmers, funding rice drying machines and importing 2mn tonnes of rice in 2023. The volatile food category continued to decline to 3.3% YoY (Apr. 3.7% YoY). Core inflation meanwhile further moderated to 2.7% YoY (Apr. 2.8% YoY). Transportation inflation also concurrently eased to a 9 month low although it was still elevated at 10.6% YoY whilst housing, water, electricity and other fuel category on the other hand was unchanged from the prior month at 2.5% YoY. Going forward, our in-house economists forecast headline inflation to be at 3.7% YoY in 2023 as both food and transport costs would likely keep decelerating. Despite this positive development related to easing inflation, we think that BI is unlikely to cut rates so soon given they would want to avoid hurting the IDR as other global central banks are still tightening.

- Change in the retail sales index in May was flattish due to the Ramadan falling earlier this year compared to last year. Ramadan this year fell on 19 – 25 April compared to 29 April – 6 May last year, which resulted in a higher base for the retail sales index in May. Nevertheless, the consumer confidence index in May continued to inch up higher to 128.3 (Apr. 126.1), which was a one year high as economic conditions continued to improve. These reasonably decent economic numbers are giving more assurance consumption can remain supported this year, implying that the economy would be on sound footing.

- **Monetary Policy Forecast:** BI unsurprisingly held rates at 5.75% at their latest June policy meeting as they look to provide support to the IDR, which had seen some weakness recently amid concerns that DM central banks may extend their tightening cycle. BI is now also expecting that the Fed would hike rates to 5.50% in July, compared to their previous estimate of 5.25%. They also maintained their GDP growth forecast at 4.5% - 5.3%, seeing it likely to come out at around 5.00%. This is even as they sounded less optimistic on China's growth prospects. They did though remain confident that the current account can stay in surplus in 2Q. Going forward, we expect BI to keep rates on hold for the rest of 2023 given the pressure the IDR may face from the prospects of further tightening by other DM central banks.

- **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 resiliently maintain a trade surplus in May although it narrowed substantially to $0.44bn (Apr. $3.94bn). Even though exports did rebound in May to 0.96% YoY (Apr. -29.40% YoY), imports also saw a big turnaround to 14.35% YoY (Apr. -22.32% YoY). Exports had received support from a surge in palm oil exports (126% YoY) due to last year's low base when shipments of crude palm oil and some its derivative products were banned for 3 weeks to ensure domestic supply given the Russia – Ukraine war. The imports jump on the other hand was broad-based and particularly lead by capital goods, which hit a historical monthly high. For the entire 2023, our in-house economists believe that Indonesia should still maintain a trade surplus due to lower oil prices, which should help narrow the oil & gas trade deficit. The maintenance of this surplus should continue to give support to the IDR in the face of other external pressures in the coming months.

- Meanwhile, Indonesia would allow the exports of five raw minerals (namely copper, iron ore, lead, zinc, and anode mud from copper concentrates) until May 2024. This walks back on their initial plans to ban exports of all metal ore from June 2023 onwards. The decision to delay the banning of exports should provide more time for the construction of smelters. However, bauxite shipments were already banned effective from 10 June as the government had assessed that four existing smelters can absorb ores intended for export. The impact from the ban is likely to only have a limited impact on Indonesia's external position given that bauxite only accounts for 0.2% of total exports.

- May foreign reserves fell substantially from last month's level to $139.30bn (Apr. $144.20bn) as the DXY saw a rebound in strength for that month as Fed rate hike bets came back into play. This was in line with our expectations that we had previously stated. We would not be surprise if foreign reserves sees further decline amid continued pressure on EM currencies from the possibility of further DM central bank hikes.

- There was strong net inflow into Indonesia Government Securities (IGBs) which was at $0.81bn month to date until 21 June 2023. The flow though over the month so far has not been consistent and reflects some shifting in sentiment. There were strong inflow earlier in the month into the IGBs as Indonesia CPI eased to the target range leading to investors possibly choosing to position into these bonds amid the likelihood of peaking rate. Restricted supply may also have helped support appeal for IGBs. However, following the FOMC meeting where the Fed forecasted two more hikes (compared to general expectations of one more hike), there was substantial outflow from IGBs as investors took chips off the tables and sold off from the EM bonds. For now, the outflows from the IGBs could slow given the possibility that the Fed rates may peak with one more hike and hence,

- 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**: June S&P Global PMI mfg (3 July), June CPI (3 July), June Foreign reserves (7 July), June Consumer confidence index (10 July), June Local auto sales (15 – 21 June), June Trade data (17 July) and Bank Indonesia Policy decision (25 July).

- **Technical Outlook:** USDIDR was last seen around 14993. Momentum indicators gradually looking to turn more stretched which imply upside could gradually become more limited. Resistance is at 15173 and 15217 (200-dma). Support is at 14857 (50-dma) and 14800. Pair likely to remain within a range of 14700 – 15100 near term. USDIDR is a sell on rallies when it hits around the top end of that range.

PHP: Cautious Amid Weak Fundamentals

Forecast	3Q 2023	4Q 2023	1Q 2024	2Q 2024
USDPHP	55.50 (-)	55.00 (-)	54.50 (-)	53.00 (-)

- **Motivation for the FX View:** Over the last month, the USDPHP has gradually edged lower although as a whole, it has continued to remain around a tight range 55.00 – 56.00. High rates together with broad dollar strength coming off have continued to provide support to the PHP even as the country's fundamentals remain weak – twin fiscal and trade deficit position. As the BSP are unlikely to move rates for the rest of 2023, this should allow the PHP to maintain a reasonable level of rate differential in the face of additional hikes by other DM central banks. We therefore expect that the USDPHP should still be able to roughly hold at around current levels and continue to maintain our forecasts, which show only very marginal moves in the pair.

- **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 May showed a showed a turnaround from months of decline as it came out at 52.2 (Apr. 51.4). Despite the pick-up in May, we stay wary of the downward trend overall staying intact as the global goods trade risks declining in the coming months. It should be noted that mfg PMI has been weakening elsewhere around the world.

- Headline inflation in May continued to ease for a fourth month in a row to 6.1% YoY (Apr. 6.6% YoY) as both food & non-alcoholic beverages (FNAB) and transport costs declined. The deceleration in the two categories was a result of the high base last year when crude oil and food prices spiked amid the Ukraine conflict. On a monthly basis though, headline inflation was unchanged. Core inflation also eased to 7.7% YoY (Apr. 7.9% YoY) after it had been unchanged in the prior month, which gives some hope that the core categories is at least seeing some deceleration. Our in-house economists are expecting that headline inflation would slowdown for 2023 to 5.5% YoY (2022. 5.8% YoY). Throughout the rest of this year, they see that monthly inflation should keep decelerating due to base effects and return to BSP's 2.0 – 4.0% range by 4Q 2023. The continued easing of elevated levels of inflation should relieve the pressure on the BSP and allow them to avoid further rate hikes from this perspective.

- **Monetary Policy Forecast:** BSP held rates at 6.25% at their latest meeting again as elevated inflation continues to ease. They also did slightly adjust their inflation forecast and see a gradual return to the 2-4% target by 4Q 2023. They see 2023 inflation now at 5.4% YoY (prior. 5.5% YoY) although they raised the 2024 estimate just slightly to 2.9%

YoY (prior. 2.8% YoY). Governor Felipe Medalla also indicated that they are unlikely to move in the next 2-3 meetings and prefer to see headline inflation stay below 4.00% for at least two consecutive month before considering monetary easing. Our in-house economists are expecting them to stay on hold for the rest of 2023 as they continue their battle to bring down inflation. They are also unlikely to cut given that there appears to be a “zero output gap”, firm domestic demand and upward risks to the still current elevated inflation. With rates being maintained at such levels, the PHP can still maintain a reasonable level of rate differential in the face of potentially additional hikes from other DM central banks. Meanwhile, importantly the BSP on 8 June cut the RRR by 250bps, which be effective from 30 June 2023. This may have been part of the BSP’s longer term plan. The government has also appointed Eli Remolona as the new BSP Governor to replace Medalla, whose term would end on 2 July. Remolona had previously been with the BIS and New York Fed. At this point, it does not immediately appear clear that policy would be substantially different.

- **Latest Fiscal Outlook:** May budget balance swung into deficit at -PHP122.2bn (Apr. PHP66.8bn) even as revenue grew at 9.35% given that spending held up. From Jan – May, the budget was in deficit at PHP326.3bn. As a whole, fiscal pressures are likely to keep persisting amid an expansionary budget, which would weigh on the PHP.

- **External Balance Outlook:** Apr trade deficit continued to be deep in deficit at -$4.5bn (Mar. -$5.1bn) as exports fell heavily by -20.2% YoY (est. -9.0% YoY). Imports also fell by -17.7% YoY (est.-8.2% YoY) but it was not enough to offset the export decline. The fall in trade as a whole can be reflective of the risks of a slowing global economy. Our in-house economists had set their 2023 export and import forecasts at 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. Their full year estimate for trade deficit is at -$59bn. The trade deficit is going to keep weighing on the PHP.

- OFWR growth picked up again in Apr to 3.7% YoY (Mar. 3.0% YoY) supported by higher repatriations from the US, Hong Kong, Taiwan and UK. Despite risks to global growth, 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. This should provide some support to the PHP.

- Bonds saw foreign net inflow of $0.9bn for quarter to date up until 31 May. The inflow could have been driven by expectations (especially earlier in the quarter) then of DM central banks coming to an end with their tightening cycle and hence, pushing investors to position into high yielders. However, this data is dated and it is likely that there could have been some outflows since amid concerns that DM central banks may not actually be quite done with rate hikes. Outflows can risk occurring for a while longer as DM central banks continue to express a hawkish tone and therefore, bond flows can risk weighing on the PHP going forward.

- Meanwhile, equities saw a net foreign inflow of $0.09bn as of 29 June 2023. Given that this inflow was marginal, not too much can be read into it just yet. Throughout the month so far, the PSEi has actually been quite choppy. In our own view, we expect that sentiments towards equities could be edgy amid continued global rate hikes and risk of economic downturns.

- FX defensive buffers was slightly weaker in May as foreign reserves fell to $101.3bn (Apr. $101.5bn) amid some weakness in the PHP on top of broad dollar strength. 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**: June S&P Global Mfg PMI (3 July), June CPI (5 July), June Foreign reserves (5 – 10 July), May Unemployment rate (7 July), May Trade data (11 July), May OFWR (14 – 18 July), June BoP Overall (18 – 22 July), June Budget balance (26 July), June M3 Money supply (28 – 31 July) and June Bank lending (28 – 31 July)

- **Technical Outlook** USDPHP was last seen at 55.22 as it tests the 100-dma at 55.31. We watch if it can decisively break that support with the next level after that at 54.42 (FI retracement of 50.0% from Dec 2021 low to Sept 2022 high). Resistance is at 55.81 (50-dma) and 56.11 (200-dma). USDPHP likely to remain around a range of 55.00 – 56.50 near term. USDPHP is sell on rallies as it hits around the top end of that range.

THB: Bumpy Road But Stay Optimistic On Tourists Return

Forecast	3Q 2023	4Q 2023	1Q 2024	2Q 2024
USDTHB	35.70 (33.25)	**35.25** (32.50)	**34.80** (32.00)	**34.50** (-)

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:** USDTHB was last seen around 35.48. Support is at 35.12 (200-dma), 34.55 (50-dma) and 34.41 (100-dma). Resistance is at 35.52 (FI retracement of 50.0% from Jan low to Oct high) and 36.21 (FI retracement of 61.8% from Jan low to Oct high). Momentum indicators show bullishness looking stretched. We do not rule out the possibility for some downwards reversal from here.

INR: Resilient in Sweet Spot

Forecast	3Q 2022	4Q 2022	1Q 2023	2Q 2023
USDINR	82.00 (80.00)	81.50 (80.00)	81.00 (79.00)	81.00 (78.50)

Previous Forecasts in Parentheses

- **Motivation for the FX View: We revise our USDINR forecasts higher across all four quarters in line with our revisions of other USD-Asia pairs higher. We expect that the hawkish Fed will likely provide better support for the USD moving forward, however we maintain the trajectory of our forecasts to account for the USD coming off, albeit more slowly than expected as factors such as China's reopening come into play.**

- On FX intervention, we think that it is likely RBI sticks to its approach of "leaning against the wind" to restore orderly conditions in the FX market. India relies heavily on capital flows to funds its current account deficit and this opens the Indian FX market to large and lumpy flows which then generate bouts of volatility. The RBI steps in to then cushion this volatility and broadly means that they accumulate reserves in times of USD weakness and expend reserves in times of USD strength. As expected, this has played out with India's foreign reserves falling in May amid USD strength but rose in early to mid-Jun amid USD weakness.

- India's external position has also improved as its current account deficit has narrowed to around 2.0% of GDP in 1Q23, from 2.2% of GDP in 4Q22, and compared to 3.7% of GDP in 3Q22. This is due to a combination of commodity prices coming off and a resurgent post-pandemic export of Indian services. Net services exports in FY23 were close to US$150b versus FY22's US$110b. All in all, this has provided the INR with some support as it remains resilient.

- We think the INR should trend lower over the next four quarters as economic fundamentals look strong. GDP growth has been healthy, inflation has meaningfully abated and the current account deficit has improved. That said, RBI's approach of leaning against the wind should keep USDINR within a controlled range and we should see an increase in India's FX reserves over this period.

- **Growth and Inflation Outlook:** India's 1Q23 GDP re-accelerated to 6.1% YoY (exp: 5.0%; prev: 4.5%) surging ahead of expectations. Annual Estimate for 2023 GDP is at +7.2% YoY (exp: 7.0%) and the re-acceleration in GDP implies that the undershoot of the level of GDP from pre-pandemic potential trend has narrowed to about 5%. The positive surprise was largely due to stronger Indian exports and a continued emphasis on public investment by the government.

- CPI inflation has largely abated in India as food prices meaningfully undershoot expectations and core inflation has moderated despite remaining sticky in 2022. The latest May CPI inflation print has headline at 4.25% (exp: 4.31%; prev: 4.7%) amid a meaningful pullback in food prices. Meanwhile, Core inflation has come off to 5.11% in May (prev: 5.30%). The inflation situation in India thus looks to be under control, as opposed to the situation that several other countries are facing.

- **Monetary Policy Forecast:** All things considered, the RBI is in a sweet spot given that growth is healthy and inflation looks to be under control. Broad consensus expects that the RBI will be on a prolonged pause and the bigger question is if there will be a change in its stance of "withdrawal of accommodation" to "neutral". We feel that given that upside risks to inflation still exist e.g. oil/commodity price shocks and El Nino affecting food prices, the RBI may decline to be too optimistic in its outlook. We look for RBI to maintain their policy rate at the upcoming August meeting, and perhaps for it to refer to the positives while retaining some flexibility to react to any changes to the growth/inflation outlook. They may soften their stance, but not as materially as some might expect. Moreover, while US yields have risen over the past couple of months, Indian yields have fallen about 30bps over the same period which implies that real monetary conditions are normalizing more slowly and are more accommodative than pre-pandemic levels.

- **Latest Fiscal and External Balance Outlook:** India's FY23 budget remains an expansionary one with expenditures estimated to be at US$560b and revenues at US$530b. The fiscal deficit however is expected to fall to 5.9% of GDP (prev: 6.4%). The budget looks to lend economic support through favourable income tax structures , an increase in government capital spending and a push toward job growth and support for agricultural and adjacent sectors.

- India's trade balance stood in a deficit of -US$267.7b on an NSA basis in May. However, as earlier mentioned the current account deficit narrowed meaningfully in 1Q23 to around 2% of GDP (-US$67b). India's external position looks to have improved and as we have earlier asserted this should continue to provide support for the INR.

- **Key domestic events and issues to watch in Jul:** Jun S&P Mfg/Services/Composite PMI (5 Jul), May Industrial Production, Jun CPI (12 Jul), Jun Wholesale Prices, Jun Exports/Imports, Jun Trade Balance (14 Jul), Jun Fiscal Deficit, Jun Eight Infrastructure Industries (31 Jul).

- **Technical Analysis:** 1M USDINR NDF was last seen at 82.14. Stochastics flags oversold levels, while RSI remains neutral. Momentum looks to be turning bullish. Support is at 81.50 (Fibo), while resistance is at 82.30 (200 dma).

VND: Downside Risks to Growth

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

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 Q3-23	End Q4-23	End Q1-24	End Q2-24
USD/JPY	145.00	142.00	140.00	133.00
EUR/USD	1.0800	1.0900	1.1100	1.1300
GBP/USD	1.2700	1.2400	1.2400	1.2600
AUD/USD	0.6500	0.6800	0.7000	0.7000
NZD/USD	0.6300	0.6500	0.6700	0.6700
USD/CAD	1.3300	1.3100	1.3000	1.3000
USD/SGD	1.3350	1.3250	1.3250	1.3150
USD/MYR	4.6000	4.5000	4.3500	4.2000
USD/IDR	15000	14900	14700	14600
USD/THB	35.70	35.25	34.80	34.50
USD/PHP	55.50	55.00	54.50	53.00
USD/CNY	7.15	7.10	6.95	7.00
USD/CNH	7.15	7.10	6.95	7.00
USD/HKD	7.80	7.80	7.80	7.80
USD/TWD	31.03	30.50	30.25	30.00
USD/KRW	1300	1280	1270	1250
USD/INR	82.00	81.50	81.00	81.00
USD/VND	23500	23400	23300	23200
DXY Index	103.51	102.71	101.27	99.32
	End Q3-23	End Q4-23	End Q1-24	End Q2-24
SGD/MYR	3.45	3.40	3.28	3.19
JPY/SGD	0.92	0.93	0.95	0.99
EUR/SGD	1.44	1.44	1.47	1.49
GBP/SGD	1.70	1.64	1.64	1.66
AUD/SGD	0.87	0.90	0.93	0.92
NZD/SGD	0.84	0.86	0.89	0.88
CAD/SGD	1.00	1.01	1.02	1.01
SGD/IDR	11236	11245	11094	11103
SGD/THB	26.74	26.60	26.26	26.24
SGD/PHP	41.57	41.51	41.13	40.30
SGD/CNY	5.36	5.36	5.25	5.32
SGD/HKD	5.84	5.89	5.89	5.93
SGD/TWD	23.24	23.02	22.83	22.81
SGD/KRW	974	966	958	951
SGD/INR	61.42	61.51	61.13	61.60
SGD/VND	17603	17660	17585	17643
	End Q3-23	End Q4-23	End Q1-24	End Q2-24
JPY/MYR	3.17	3.17	3.11	3.16
EUR/MYR	4.97	4.91	4.83	4.75
GBP/MYR	5.84	5.58	5.39	5.29
AUD/MYR	2.99	3.06	3.05	2.94
NZD/MYR	2.90	2.93	2.91	2.81
CAD/MYR	3.46	3.44	3.35	3.23
MYR/IDR	3261	3311	3379	3476
MYR/THB	7.76	7.83	8.00	8.21
MYR/PHP	12.07	12.22	12.53	12.62
MYR/CNY	1.55	1.58	1.60	1.67
MYR/HKD	1.70	1.73	1.79	1.86
MYR/TWD	6.74	6.78	6.95	7.14
MYR/KRW	283	284	292	298
MYR/INR	17.83	18.11	18.62	19.29
MYR/VND	5109	5200	5356	5524

Source: Maybank FX Research and Strategy as of 30 June 2023.
*These forecasts are meant to be indicative of FX trends and not meant to be point forecasts.

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