Macro | FX Research & Strategy

Global

2 May 2023

FX Monthly

2023, Issue 4: Awaiting Fresh Stresses

What Has Changed This Month?

- We adjusted our forecasts for GBPUSD, USDJPY and USDSGD higher. We expect divergence between the BOE and the Fed to provide some support for the GBP. We also revised our USDSGD forecasts upwards to take into account MAS standing pat and signaling a likely pause on tightening in April. We softened the bullish profile for AUD, NZD on risks of slower than expected recovery in China, US-China tensions. USDJPY forecasts were shifted higher to account for unwinding of long JPY positions after BOJ decision to stand pat. Our core view for a weaker USD remains intact on China's anticipated reopening and the Fed coming to an end of its tightening cycle.

Our Strategies

- May has been widely known to be the seasonally bullish month for the the greenback, clocking gains for eight out of the past 12 Mays. However, that seasonality factor has been increasingly challenged as the DXY index was down for the past three Mays since 2020. For May 2023, we focus on the Fed, widely expected to raise policy target rate by a final 25bps to 5.00-5.25% on the 3rd and potentially signalling a pause. Markets still look for around 75bps cut by Jan 2024 but the Fed is likely to stand firm with the view that rate cuts are unlikely within the year. Such gaps provide opportunities to sell the USD on rallies. Regardless, a signal to pause by the Fed could mean that currencies with more tightening runway (EUR, GBP) are still likely to outperform vs those that have halted (AUD, CAD, RMB and to some extent NZD) in the next few weeks.

- The ECB and BOE are likely to diverge from the Fed in terms of monetary policy tightening moving forward. We have more conviction that the Fed will be done after one more hike, in contrast to the BOE, which should hike at least once more after yet another surprise inflation print and the ECB, where the hike has been fully priced in and the question is more on the magnitude of the hike (either 25bps or 50bps). Despite central bank divergence, we see stretched valuations and overbought conditions in the cable, as such we recommend a tactical short of GBPUSD at levels above the 1.24 figure.

- China's GDP surprised to the upside, spurring upside revisions to growth forecast for this year. That said, China equities and RMB itself remain lackluster as investors are sceptical on whether the recovery can sustain, uneasy over US' measures to restrict China's technology advancement, lingering tensions over Taiwan as well as the RMB's negative carry vs. the USD. The Politburo pledged to support economic recovery and should that gain traction, we see better support for regional AxJ + AUD, NZD.

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Top 3 Currency Plays for May

Sell USDIDR, USDJPY on Rally
Tactical Short GBPUSD
Accumulate AUD on Dips

Key Events for the Month Ahead

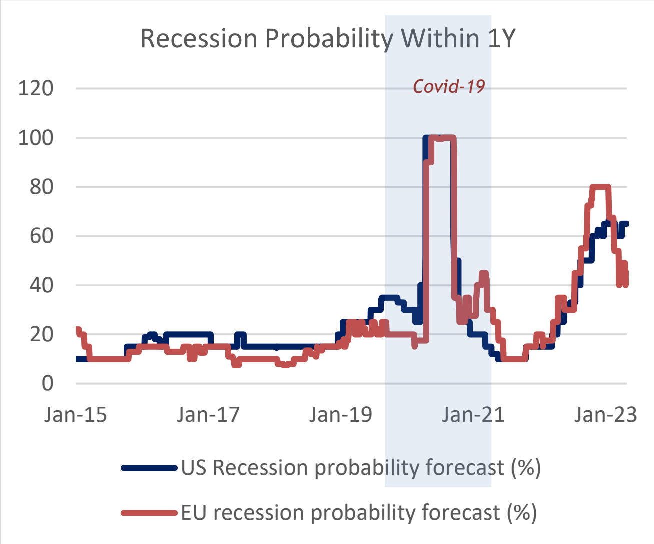
Date	Event
9 May	Australia Federal Budget
14 May	Thailand General Election

Central Bank Meetings for the Month Ahead

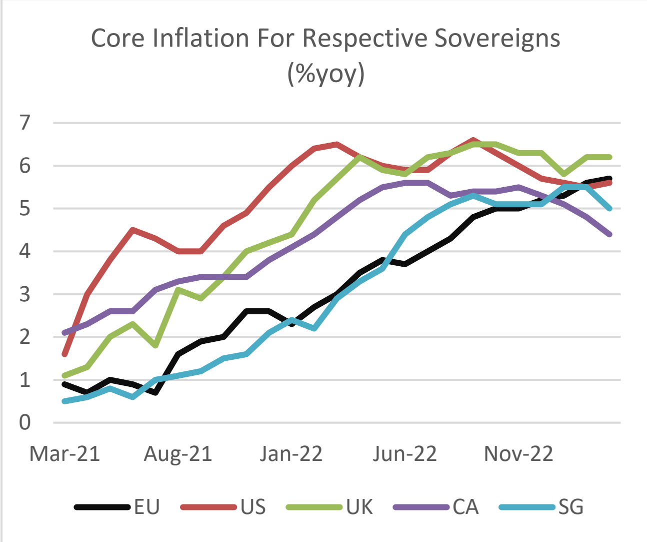
Date	Event
3 May	FOMC Policy Decision
3 May	BNM Policy Decision
4 May	ECB Policy Decision
11 May	BoE Policy Decision
18 May	BSP Policy Decision
25 May	BoK Policy Decision
25 May	BI Policy Decision
25 May	RBNZ Policy Decision

Recession Probabilities Remain Elevated

Recession is Seen More likely in the US vs. EU in 1Y



Core Inflation Seems to Be Easing for Most, Albeit Still Elevated

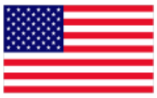


Source: Bloomberg, Maybank FX Research & Strategy

US Debt Ceiling Crisis - Timeline of key Dates

No.	Scenario	Implication on the FX	Probability
1	US begins to defaults on some debt obligations	• There would be a knee jerk downward decline in the DXY although it should eventually retrace some of its losses • Given the USD's outsized position as a global reserve currency and the high foreign holdings of US treasuries, the DXY would only gradually decline in the long term as countries, corporations and individuals offload their USD denominated assets overtime	5% likelihood We see it as extremely unlikely that the US would default on any of its debt obligations given the economic and political (e.g. weakening of their international standing) implications it would have on themselves
2	Credit rating downgrade but debt ceiling is raised	• Just as it has happened in history, the DXY would be more subdued during the period of the downgrade but then it should eventually move in line with other macro developments again	25% likelihood This looks unlikely to happen given that the rating agencies for now are expecting the US to raise its debt ceiling and avoid a default of any sort whilst still having a capacity to repay
3	Debt Ceiling is raised (even if it occurs close to the "X-date") and any sort of default is avoided (Our base case scenario)	• Little impact in the medium to long term on the DXY given that it would just be business as usual • However, we do note that in the interim, there could be DXY volatility arising from a worsening of the political stalemate together with credit rating downgrades fear and hence, we are pricing in some weakness into the DXY within the coming months	70% likelihood This looks likely to happen given that history has shown the US government eventually successfully raises the debt ceiling even if it happens at the 11^{th} hour

G7 Global Overview



USD: Growth Concerns Emerging

Forecast	2Q 2023	3Q 2023	4Q 2023	1Q 2024
USD Index	101.63 (101.39)	100.59 (100.18)	99.56 (98.98)	99.07 (98.47)

Previous Forecasts in Parentheses

- **Motivation for the FX View:** The DXY index kept generally in a tight range around 101-103 in April. It reached a high of 103 on 3 Apr and a low of 100.79 on 14 Apr after the surprise dip in Mar inflation gave a boost to expectations that a Fed pause in their aggressive rate hike cycle may be on the horizon. With the March FOMC 25 bps hike, our in-house economists forecast one more 25bp in 1H 2023. The March FOMC statement and Powell noted that recent financial sector developments are likely to result in tighter credit conditions, which will likely weigh on economic activity. In fact, the FOMC's forecast implies that the economy will be quite weak in the rest of the year. Without fresh stresses emerging, the mark-to-market impact of banking stress and associated credit tightening appears meaningful in places such as commercial real estate and small business lending, but appears small generally in other parts of the economy, i.e. consumer spending & services, holding up well thus far. We will need to monitor new data that emerges.

- In light of these developments, we are factoring that some support remains for USD but with US growth softening and enhanced with latest developments and growth outside US especially China and emerging markets likely to pick up in 2H 2023, we maintain our current USD trajectory of some decline in 2H 2023 including risk of some US debt ceiling concerns emerging in the end of 2Q 2023 onwards. The DXY levels are also revised higher to reflect slight adjustments to the JPY in 2023 on the back of the recent BOJ announcements & developments.

- We are also pricing in some risk of debt ceiling impasse volatility emerging in the run-up to June 2023. The debt ceiling will likely need to be raised or suspended after a $2.5 tn debt limit increase enacted in Dec 2021 is exhausted and extraordinary measures are no longer sufficient to avoid default. The government officially reached the statutory limit on Jan 19, according to a letter from Treasury Secretary Janet Yellen, although extraordinary measures will allow Treasury to continue to pay obligations until at least early June. As such, there could be further risk of USD volatility and some softness in end 2Q and 3Q.

- **Growth and Inflation Outlook:** Real GDP rose 1.1% annualized in the 1Q, below consensus expectations of 1.9% largely dragged by weaker inventory growth. The weak inventory growth was offset by domestic final sales which rose 3.2%, partly reflecting a reacceleration in consumption growth to +3.7% annualized. While business fixed investment slowed to 0.7%. Inventory growth was particularly weak for manufacturing transportation ex-autos and wholesale machinery, while retail inventories increased slightly and farm inventories declined by less than in 4Q.

- March core CPI rose 0.38%, but below consensus of 0.4% and is at a 4-month low. What is significant to highlight is that the monthly shelter inflation fell sharply and likely to trend lower. Core services prices excluding rent and OER rose strongly to 0.40% on the back of categories with pent-up price pressures like car insurance and daycare.

- March non-farm payrolls rose 236k, exceeding the 230k consensus expectations on continued strength across the leisure, healthcare, and business services sectors. The unemployment rate declined by a tenth to 3.5%, amid a 577k increase in household employment. Average hourly earnings increased by 0.27% m/m in March which was slightly below expectations and the Feb pace was revised down 0.03pp to +0.21%.

- **Monetary Policy Forecast:** The Mar FOMC minutes showed that the FOMC members scaled back their rate hike expectations this year due to the financial sector turmoil concerns and they continue to monitor for signs of a credit tightening/crunch. FOMC raised their benchmark lending rate by 25-bps to a range of 4.75% to 5.00% in Mar, as they tried to balance the risk of a credit crunch with incoming data showing price pressures remained elevated despite concerns of a “mild recession” later this year.

- **FOMC Outlook -** FOMC meeting on 21-22 Mar 2023 - in the wake of US banking turmoil - saw target fed funds rate (FFR) raised by +25bps to 4.75%-5.00%. Fed’s latest “dot plot” signals no change in FFR peaking and staying at 5.00%-5.25% this year, suggesting one more +25bps hike at 2-3 May 2023 FOMC meet. From the latest FOMC Statement, the decision to further hike FFR by +25bps - after the +25bps increase on 1 Feb 2023 which further slowed the pace of FFR hikes from +50bps in Dec 2022 following four +75bps hikes between June and Nov last year – reflects Fed’s commitment to tame inflation. FOMC statement pointed out that job gains picked up in recent months, inflation remains elevated and reiterated that the Fed is strongly committed to returning inflation to the 2% target. Our house view is for a peak at around 5-5.25% in spring (May FOMC).

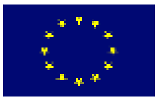
- The updated FOMC’s FFR median forecast or the “dot plot” signals FFR target range peaking at 5.00%-5.25% and staying at the terminal rate this year i.e. unchanged from the position in Dec 2022. This suggests one more round of +25bps hike in FFR at the 2-3 May 2023 FOMC meets. For now expect no rate cuts this year and this terminal rate of 5.25% to last through 2023. The risk of a further June hike is lower now in part because credit seems somewhat tight in the aftermath of the banking turmoil, and some hesitancy in the minutes about even a May hike, suggests that the bar for the FOMC to agree at its May and future meetings to both hike and signal additional tightening is not currently implied by the median dot.

- Further underscoring this, FOMC statement on FFR path ahead changed to “some additional policy firming may be appropriate” from “ongoing increases in the target range will be appropriate” in order to attain a stance of monetary policy that is sufficiently restrictive to return inflation to 2% over time. Fed expects inflation rate – based on its preferred measure i.e. private consumption expenditure (PCE) inflation - to be at +3.3% in 4Q 2023 (+3.1% previously) and moderate to +2.5 by 4Q 2024 and +2.1% by 4Q 2025 (both unchanged from Dec 2022 forecasts). Core PCE inflation is expected to be at +3.6% in 4Q 2023 (+3.5% previously) and moderate to +2.6% by 4Q 2024 (+2.5% previously) and +2.1% by 4Q 2025 (unchanged). No change in our view of FFR peaking at 5.00%-5.25% in May 2023 and stay there for the rest of 2023, to be followed by a total of -200bps cuts in 2024. Market is currently evenly split between no change and +25bps hike at 2-3 May 2023 FOMC and seeing FFR cuts starting 2H 2023 by pricing in 4.20% at end-2023 and 2.85% at end-2024.

- In the wake of several bank runs and collapse over the past couple of weeks, the FOMC statement added that the US banking system is sound and resilient. Fed cautioned that there will be tighter household and businesses credit conditions that will weigh on the economy, job market and inflation, although the impact is uncertain. Consequently, Fed trimmed its 4Q 2023 and 4Q 2024 real GDP growth forecasts to +0.4% and +1.2% vs +0.5% YoY and +1.6% previously, with 4Q 2025 growth of +1.9% vs +1.8% previously. Projections for unemployment rate in 4Q 2023, 4Q 2024 and 4Q 2025 are little changed at 4.5% (4.6% previously, 4.6% (unchanged) and 4.6% (4.5% previously). US authorities announced full guarantee of deposits at Silicon Valley Bank (SBV) and Signature Bank, while Fed unveiled a new lender of last resort facility - Bank Term Funding Program (BTFP) – where banks can exchange their US Treasuries, agency debts and mortgage-backed securities at par for one year funding at Overnight Index Swap (OIS) +10bps. In response to Credit Suisse trouble, Fed together with the central banks in Eurozone, Japan, England, Switzerland and Canada enhanced their USD swap line arrangements.

- **Key domestic events and issues to watch in May:** ISM Manuf (1 May); FOMC (4 May); NFP (5 May); Factory Orders, Durable Goods Orders (2 & 26 May); ADP (3 May); Trade Balance (4 May); CPI (10 May); Retail Sales (16 May); Initial Jobless Claims (18 May); FOMC Minutes (25 May); FOMC (23 Mar); GDP (25 May); PCE Deflator (26 May).

- **Technical Outlook:** DXY index hovered around 101.10 as we write, having broken above the 21-dma. Key support is seen at 100.80 which remains intact. Double bottom has formed with the low for Apr matching the low in Feb. This could mean some retracements towards the 103-figure (50,100-dma). Momentum is increasingly bullish as well. On the weekly chart, 21-ma is en-route to cross the 100-ma and that is bearish. Moves higher could thus be capped at 103 before the DXY index extends lower.



EUR: Divergent Central Banks Implying Stronger EUR

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

No Change to Previous Forecasts

- **Motivation for the FX View: We maintain our base scenario for EURUSD forecasts over the next four quarters, which suggest that the EURUSD will remain at 1.10 levels by the end of the quarter.** We acknowledge that the European Central Bank (ECB) is potentially the central bank that is the furthest from the end of the tightening cycle, which may have a positive impact on the EUR sentiment. Additionally, we expect the EU's economic growth, as well as the rest of the world, to slow down but not deteriorate significantly, potentially bolstered by China's recovery. In the event of an eventual pause in rate hikes by the ECB later in the year, it could be viewed positively for the EUR sentiment, as long as the decision is motivated by disinflation and growth does not deteriorate significantly. It is worth noting that while this is not our base case, such a pause could be viewed positively for the EUR sentiment, as it would signal the ECB's willingness to maintain a balance between inflation control and economic growth. This scenario could be possible if other central banks, such as the Fed, also reach the end of their rate hike cycles, and the energy situation remains comfortable for Europe, while the labor market displays resilience. Overall, we remain optimistic about the EUR's prospects in the current market conditions.

- EURUSD trended higher in Apr on the back of a continued narrowing US-EU 10Y yield differential (109bps Apr avg vs 127bps Mar avg). This compression in yield differentials has been driven by the continued narrative that the Fed is coming to the end of its tightening cycle, while the ECB is more likely to continue on its own tightening cycle, on a path that is divergent from the Fed. In addition, banking concerns have taken a backseat, which has also driven the EUR higher. Although there were initial fears over European banking stability, the ECB's decision to stay the course and hold firm on its well-telegraphed hike has reinforced their credibility and lent support to the EUR. Inflation in the Eurozone remains relatively high with core inflation sticky at elevated levels. Meanwhile, economic activity continues to show a mixed picture, with the services sector expanding and the manufacturing sector contracting. However, there is still a possibility that economic growth and prospects could be better than previously anticipated, given potential tailwinds from China's recovery, stronger EU-UK trade relations after the Northern Ireland protocol agreement, and easing energy prices and supply issues from 2022 that bode well for the EUR. Overall, the outlook for the EUR remains positive despite some uncertainties in the economic landscape.

- Despite financial stability fears, the ECB followed through earlier in March on its anticipated 50bps rate hike, bringing the policy rate to 3.00% (previously 2.50%). During the announcement, Lagarde cited the Separation Principle, which aims to reduce conflicts of interest between the ECB's price stability mandate and its financial stability mandate. Notably, the ECB removed its hawkish forward guidance and instead referred to future hikes being determined on a meeting-by-meeting basis and data dependent. While some ECB officials have become more dovish in their rhetoric, an overall hawkish tilt persists, as evidenced by the recent release of the March ECB minutes, there was a growing divide among council members over the magnitude of policy tightening and the transmission mechanism of monetary policy, the overall sentiment remained relatively hawkish. The hawkish tilt in the minutes was established largely on the fact that inflation remains stubbornly persistent, despite the diverging views on the appropriate monetary policy decision among the governing council. However, despite the ECB's core inflation projections of 4.60% in 2023, markets are currently pricing in an OIS-implied 3.75% terminal rate – slightly higher than last month's OIS-implied 3.50% terminal rate. This suggests that while the ECB may remain hawkish on inflation, market sentiment is not as certain about future rate hikes given the evolving economic landscape.

- 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 imply the Eurozone's trade balance remains in deficit.

- 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 flexble LNG cargos. Europe is currently projected to attract almost 75% of global flexible LNG supply. This is the key assumption that drives analysts estimates that Europe will survive the next winter. Should this situation change, then the EUR could once again face some challenging headwinds.

- The EUR also faces risks of ECB overtightening in the face of banking turmoil, which could lead to a destabilization of financial markets and a potential slowdown in the Eurozone economy. While the ECB has shown a hawkish tilt in recent months and signaled a willingness to raise interest rates to combat rising inflation, the potential for renewed financial instability remains a concern. In particular, the viability of certain European banks, including Deutsche Bank, remains uncertain, and any abrupt shifts in monetary policy could further exacerbate these issues. However we recognize that the ECB has thus far handled the issues of combating inflation and maintaining banking and financial sector stability fairly well. As such, we think that this risk remains under control for now.

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

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

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

- Most advanced economies, including the Eurozone, are seeing contractions in manufacturing activity implied by PMIs, although services PMI remain firmly in expansionary territory. This trend looked to continue in April as Preliminary Eurozone PMIs came in at 45.5 for manufacturing (exp: 48.0; prev: 47.3) and 56.6 for services (exp: 54.5; prev: 55.0).

- Meanwhile, Eurozone continues to see rather stable unemployment rate at around 6.7%. Tight labour market conditions seem to be supportive of household spending and the services sector. Mar Core CPI inflation remained sticky in line with expectations at +5.7% YoY (exp: 5.7%; prev 5.7%) underscoring persistent underlying core price pressures. However, Mar headline CPI inflation moderated to +6.9% YoY (exp: 6.9%; prev: 8.5%) largely in line with expectations. Feb PPI inflation was at +13.2% YoY (exp: 13.3%; prev: 15.1%).

- **Monetary Policy Forecast:** In March, ECB delivered another 50bps hike to take the deposit facility rate to 3.00%, marginal lending facility to 3.75% and main refinancing rate to 3.50%. In Feb, Lagarde was earlier explicit in the central bank's intention to hike another 50bps in Mar, and said that the "intend" was not "irrevocable", acknowledging that risks to growth outlook have become more balanced, and as a result, retained optionality and flexibility. However, she was clear that the rate decision in the face of banking crisis was targeted at price stability, citing the Separation Principle which aims to reduce the conflict of interest between the ECB's mandates of price stability and financial stability. The statement that accompanied the decision said that the ECB would remain "data dependent" and would decide "meeting-to-meeting" on rate hikes.

- The Mar ECB meeting minutes showed that the governing council was becoming increasingly divided about the magnitude of rate hikes and the transmission of monetary policy tightening thus far. However, the minutes still very much retained a hawkish tilt, and recognized the risks of persistently high and stubborn core inflation. This also implies that a 50bps hike is still within the realms of possibility at the upcoming May meeting and would not be too much of a hawkish surprise to us, even though OIS-implied probability of a 50bps hike at the upcoming meeting is only 22% at the moment. This should also provide ample room for further EUR upside should the ECB indeed choose to hike 50bps. Nevertheless, our base case remains for a 25bps increase, in line with both market pricing and the predominant market view.

- For the rest of 2023, current OIS implied pricing is for a terminal deposit facility rate of 3.75%, with the market implying a total of roughly 75b of hikes for the ECB. Any signal to persist with the current pace of 50bps per hike could actually provide further intermittent boost to the EUR. A pause would not necessarily be negative for the EUR as long as growth does not deteriorate significantly and inflation is en-route towards the 2% target. Given that the ECB's core inflation projection is 4.6% for 2023, there is still a significant disparity between what the market is pricing in and what the ECB is expecting. Should the ECB actually deliver on expected rate hikes, we should see further gains for the EUR.

- **Latest Fiscal and External Balance Outlook:** The Eurozone current account was in a EUR 21.3b surplus in February compared to a EUR -0.7b deficit in January. Year-to-date the Eurozone has accumulated a current account surplus of EUR 20.6b. The 2022 Eurozone current account was in deficit of EUR -97.1b.

- **Key domestic events and issues to watch in May:** EC Apr Final Mfg PMI, EC Mar M3 Money Supply, EC Apr Prelim CPI Inflation (2 May), EC Unemployment (3 May), EC Mar PPI, EC Apr Final Services and Composite PMI, **ECB Policy Decision (4 May)**, ECB Survey of Professional Forecasters, EC Mar Retail Sales (5 May), EU Commission Economic Forecasts (8 May to 15 May), EC Mar Industrial Production (15 May), May

ZEW Survey Expectations, EC Mar Trade Balance, EC 1Q Prelim GDP (16 May), EC Apr Final CPI Inflation (17 May), ECB Economic Bulletin (18 May), EC May Consumer Confidence (22 May), EC May Flash PMIs, EC Mar Current Account (23 May), EC Apr M3 Money Supply, Confidence Indices (30 May)

- **Technical Outlook:** EURUSD hovered around 1.10 levels a current key support/resistance level, having convincingly broken past the previous 1.09 level resistance. RSI is neutral, while stochastics are flagging overbought conditions. Momentum for EURUSD is bullish, however this is waning. EURUSD has consolidated for much of Apr and traded within a 1.0788 to 1.1095 range. We see some potential for EUR to move higher based on technicals, although we remain cautious of possible near-term pullbacks with bouts of USD strength. Looming central bank decisions could also provide for some volatility in price action. Next resistance is at 1.11 level, while support is seen at 1.09 (former resistance turned support).

GBP: Mean Reversion on the Cards Given Poor Fundamentals

Forecast	2Q 2023	3Q 2023	4Q 2023	1Q 2024
GBPUSD	1.2300 (1.2100)	1.2300 (1.2200)	1.2400 (--)	1.2400 (--)

Previous Forecasts in Parentheses

- **Motivation for the FX View: We revise our GBPUSD forecast for 2Q 2023 upwards to account for the fact that the BOE is more likely to continue on its tightening cycle. Recent UK inflation prints have been surprisingly hot, and when combined with a tight labour market, should force the BOE to hike rates at the upcoming May meeting. In contrast, the Fed is expected to approach the end of its tightening cycle.** However, we also recognize that the BOE has been one of the more dovish of the major central banks, with BOE Governor Bailey not being as firm on inflation as Fed's Powell or ECB's Lagarde. In addition, the UK's medium-term prospects still look grim, given the existence of price pressures, labour market shortages and an ailing economy, structural problems inherited from Brexit. Should inflation continue to remain sticky, the policy space for the BOE to hike rates will be narrower in the face of a recession and this underpins our bearish GBP outlook, we still expect some correction to the GBP as it currently trades at levels that appear to be very stretched in terms of valuations and as technical indicators are flagging overbought conditions. **Based on our analysis, we advocate a tactical short position on the GBPUSD currency pair, as we anticipate a downward**

trajectory towards our projected levels. Our assessment of the prevailing conditions underscores the unfavorable fundamentals for the UK economy, thus bolstering our conviction in this recommendation.

- **Risk(s) to our View:** While the prevailing conditions do seem to paint a bleak outlook for the GBPUSD currency pair, there are still potential upside factors that cannot be entirely discounted. 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.

- 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.

- **Growth and Inflation Outlook:** The UK's final 4Q2022 GDP came in slightly better than expectations at +0.6% YoY (exp: +0.4%; prev: +0.4%) and +0.1% QoQ (exp: 0%; prev: 0%). Feb GDP showed that growth stagnated at 0% MoM (exp: 0.1%; prev: 0.4%). While growth appears to be picking up, prospects for the UK economy are still anticipated to be negative, indicating a contraction rather than an expansion. Current consensus forecast suggests GDP growth to come in at -0.4% YoY (prev: -1.0% YoY) for the UK in 2023. The UK economy 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. Economists still expect a UK recession, with a survey of 51 economists in January seeing a 90% chance of a recession happening in the UK over the next 12 months, painting a bleak picture for the UK's growth prospects in 2023. The BOE's forecasts for growth are also dismal, expecting real GDP to contract by -1.50% YoY in 2023 and -1.00% YoY in 2024.

- On the inflation front, Mar Core CPI was hotter than expected at +6.2% YoY (exp: +6.0%; prev: +6.2%), while Mar headline CPI moderated, but remained above consensus, at +10.1% YoY (exp: +9.8%; prev: +10.4%). Price pressures remain persistent at elevated levels. Consensus forecasts for the UK's CPI stands at +6.5% YoY in 2023. Meanwhile, the BOE's forecasts for inflation stand at +10.75% YoY for headline and +5.25% YoY for core in 2023. These levels remain above the BOE's preferred target of 2%. Inflation has been kept sticky also in part due to a labour shortage in the UK that is keeping wage cost pressures strong.

- **Monetary Policy Forecast:** In line with expectations, the BOE delivered a 25bps rate hike (vote split: 7 hike, 2 maintain) in the last meeting on 23 March, bringing the policy rate to 4.25%. Our view is for one more 25bps hike at the May meeting as inflation remains elevated (Mar Core CPI remained sticky +6.2% YoY although Mar headline CPI moderated to +10.1%) and the labour market remains tight (wage growth was firm at +5.9% YoY in Feb). The market is currently pricing in a 102.1% chance that the BOE will hike by 25bps at the May meeting, which implies a miniscule 2.1% chance of a hawkish 50bps surprise. The BOE's hand should be forced once again at the upcoming meeting in May as it was at the previous meeting in March, given existing persistent and stubborn inflationary pressures and strong wage pressures. However, the BOE has remained relatively dovish compared to its counterparts and has demurred on its forward guidance. We think that there remains a risk of overtightening that the BOE is cognizant of, and although inflation remains sticky at elevated levels it is expected to fall sharply later in 2023 and this could feed into the narrative that the BOE could have already reached its terminal rate, which means any further hikes could be perceived as overtightening. The market is currently pricing a 4.9% terminal rate for the BOE.

- **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 Feb Trade Balance stood at -£4.8b (exp: -£4.9b; prev: -£3.5b), while the Feb Goods Trade balance came in at -£17.5b (exp: -£17.0b ; prev: -£16.1b). The wideaning the trade balance was mainly due to a -6.3% MoM fall in exports, while imports fell -1.4% MoM. The drag on exports reinforces the difficulty that the UK is facing and underscores the importance of access to the EU common market.

- **Key domestic events and issues to watch in May:** Apr Nationwide House Price Indices, Apr Final Manufacturing PMI (2 May), Mar Mortgage Approvals, Mar Money Supply, Apr Final Services & Composite PMIs (4 May), RICS House Price Balance, Mar Monthly GDP, Mar Industrial Production, Mar Manufacturing Production, Mar Trade Balance, 1Q23 Prelim GDP, **BOE Policy Decision (11 May),** Jobless Claims, Mar Average Earnings, Mar Unemployment (16 May), May Rightmove House Prices (22 May), Apr Public Sector Finances, May Preliminary PMIs (23 May), Apr CPI Inflation, RPI and PPI (24 May), Apr Retail Sales (26 May), Apr Mortgage Approvals, Apr Money Supply (31 May)

- **Technical Outlook:** GBPUSD last traded at 1.2560 levels, having surged past the 1.25 resistance on the last trading day of April. We see the next key resistance at the 1.26 level, with 1.27 the next key level seen on the upside. Meanwhile, support is at 1.25 (previous resistance turned support) and 1.24 further to the downside. Stochastics are flagging overbought conditions for the GBP, while RSI is neutral but rising towards overbought levels. A potential bullish crossover in MACD is forming. However, we look for a retracement in the GBP and recognize that looming central bank decisions could provide some volatility in the near term for currencies.

AUD: Slow Gains, Seaonality Risks Ahead

Forecast	2Q 2023	3Q 2023	4Q 2023	1Q 2024
AUDUSD	**0.70**	**0.72**	**0.73**	**0.73**
	(--)	(--)	(0.74)	(0.75)

Previous Forecasts in Parenthesis

- **Motivation for the FX View:** We still look for AUDUSD to head higher towards 0.95 as we still retain our expectations for China to recover into the second half of the year. However, we are slightly less bullish on the AUD than before, taking into consideration recent developments – as the US continues to restrict China's technology advancement and fan geopolitical tensions along the Taiwanese Strait, Australia is also wedged in a difficult position between its traditional military allies as well as its biggest trading partner. China's recovery is also uneven thus far, with the real estate sector still under pressure. This could mean that China's recovery could take more time to gain traction. On net, we remain constructive on AUD over the next twelve months but due to the aforementioned factors (of geopolitical tension, potential for China's recovery to be more gradual than expected), we look for a more moderate bullish profile for the AUD. May is a seasonally bearish month for the AUD and could present buying opportunities.

- AUD remained an underperformer for much of Apr as markets remain skeptical on whether China's recovery can be sustained, Fed-RBA divergence as well as cautious sentiment as manufacturing activity continues to slow for most parts of the world. RBA's decision to halt its rate hikes have crimped on the AUD vs. more hawkish peers including NZD, EUR, GBP, USD. We do not expect the underperformance of the AUD to sustain for long as most central banks come close to the end of their respective tightening cycles and RBA's decision to spring a rate hike today (2 May) also helps to provide some support for the currency. In addition, recovery in China has not taken off yet. Global growth slowdown on the other hand, weighs on metal prices (iron ore, copper) and concomitantly, Australia's term of trade and the AUD. This is not helped by the fact that property investment in China is still weak. We remain optimistic on recovery there that could these factors into bullish AUD drivers. A weaker-than-expected recovery in China and a more severe slowdown for the global economies are still the most significant risks to our bullish AUD outlook.

- **Growth and Inflation Outlook:** Recent data indicates uneven growth pace in the economy. Manufacturing PMI for Apr deteriorated to 48.1 from previous 49.1. Services on the other hand, rebounded back to expansion at 52.6 for Apr.

- Mar labour report was a solid one with 53K of employment added on net. That consists of 72.2K full time employment and -19.2K of part-time hires shed last month. Unemployment rate steadied at 3.5% with participation rate also stable at 66.7%. Tight labour conditions could continue to underpin household spending, which was strong at 8.0%m/m vs. -0.1% in Feb. This could continue given how Westpac consumer confidence jumped 9.4% in Apr to 85.8. All these indicators seem to suggest that private consumption remains rather resilient and the services sector could still hold up.

- Meanwhile, on the inflation front, we are seeing signs of easing even before Australia releases its usual quarterly numbers for 1Q as well as the Mar CPI print. Consumer inflation expectation eased to 4.6%y/y for Apr vs. previosu 5.0%. The Melbourne Institute inflation gauge for Mar decelerated to 5.7%y/y from pervious 6.3%. Such indications of disinflation justify RBA's decision to halt its tightening cycle in Apr.

- On the real estate front, there are some signs of bottoming with home loans value clocking a milder decline of -0.9%m/m in Feb vs. previous -2.4% (revised sharply higher from -5.3%). The decline in investor loan value slowed to -1.2%m/m vs. previous -21%. Building approvals for Feb rose 4.0%m/m vs. previous -27.1%. Approvals for private sector housesalso rebounded +11.3% on the month for Feb vs. previous -13.5%.

- As RBA turned less hawkish and halted rate hikes, NAB business confidence improved to -1 from -4 while business conditions only eased slightly to 16 in Mar from 17.

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

- That said, we do not think there could be more opportunities for RBA to pull off another surprise rate hike. If anything the tight labour market (based on Mar labour report) probably gave the RBA room to do so now. PMI data for Apr, alongside trade data actually suggest that demand conditions could be softening and the window for further tightening could be closing soon.

- As such, hawkish as the RBA may want to sound with the mention of "further tightening of monetary policy" that may be required to get inflation back to target, we do not think that another hike will come easy. The language of the RBA statement as well as the surprise action probably alleviated some pressure on the AUDUSD from the Fed-RBA policy divergence but we can easily expect the Fed to caution on potential for more rate hikes at the meeting ths month in order to curb inflation there too. Beyond the near-term, we remain constructive on AUD as the drags from RBA-Fed divergence to dissipate once Fed becomes more growth-focused.

- Another key event that happened in Apr was the outcome of the first RBA review done in decades. The 51 recommendations from the RBA review were put forth on 20 Apr, all accepted by the government in principle. Key recommendations include reducing the RBA meetings to just eight a year vs. once every month. RBA to maintain the inflation target of 2-3% and aim for the mid-point. This is slightly different from the old inflation target mandate that seeks to achieve inflation to be around 2-3%, on average, over time. This could mean a tad more urgency to get inflation back towards 2.5%. Post-meeting statement will also include unattributed votes. RBA to establish governance board to oversee bank management, separated from the monetary policy settings. The legislated changes will start from 1 Jul 2024 and thus are unlikely to present fresh impetus for AUDUSD in the near term.

- **Latest External Balance Outlook:** As of last available data, current account surplus was recorded at +1.2% of GDP for 4Q 2022, widening a tad from the previous 0.95%. Australia recorded a AUD14.1bn of current account surplus vs. previous A$753mn, buoyed by the stronger surplus in goods and services trade balances. For Feb, trade has been underperforming with exports contracting -3%m/m vs. +1% prev. while imports are down -9% vs. +5% in Jan. Trade surplus widened unexpectedly to A$1.39bn vs. previous A$1.13bn.

- **Fiscal Outlook:** Eyes on the May budget to be handed down on 9 May 2023. Treasurer Chalmers said that the budget will need to strike a balance between inflation and growth risks, near-term and longer-term priorities. Some of which could could include energy transition, digitisation and defence – there was a military review done recently. The Defence Strategic Review recommends the government to reprioritize spending toward purchasing long-range missiles and military drones while boosting domestic defence manufacturing, noting that the US is no longer "the unipolar leader of the Indo-Pacific" and also in the face of a military build-up by China (Bloomberg).

- The labour government produced its first budget on 25 Oct 2022, projecting deficit to narrow to A$36.9bn in 2022-2023 (1.5% of GDP) from A$134.2bn (6.5% of GDP) in 2020-2021. Deficit was expected to widen to A$44.0bn in 2023-2024 (1.8% of GDP) and A$51.3bn in 2024-25 (2.0% of GDP). Deficit projections for over the four years to 2025-26 is also expected to be A$42.9bn less than Mar budget. **The above are based on GDP growth projection of 3.**25% for 2022-2023 (vs. 3.5% projected previously), 1.5% for 2023-2024. The labour market is forecast to soften with unemployment rate seen at 4.5% in 2Q 2024.

- **Key domestic events and issues to watch:** Services PMI, Composit PMI for Apr [3 May]; Mar trade [4 May]; **SoMP [5 May];** Mar home loans (investor loan, owner occupier) for Mar [5 May]; NAB business confidence, conditions, Mar building approvals [8 May]; CBA household spending for Apr, Westpac consumer confidence for May, retail sales ex inflation for 1Q [9 May]; May consumer inflation expectations [11 May]; **Minutes of May RBA policy meeting, [16 May];** Westpac leading index for Apr, **1Q wage price index** [17 May]; **Apr labour report [18 May];** Judo Bank Australia prelim. Mfg., services, composite index for May [23 May], Apr retail sales [26 May]; Apr building approvals [30 May].

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

NZD: Caution into May

Forecast	2Q 2023	3Q 2023	4Q 2023	1Q 2024
NZDUSD	**0.63**	**0.65**	**0.67**	**0.67**
	(0.65)	(0.67)	(0.68)	(0.68)

Previous Forecasts in Parenthesis

- **Motivation for the FX View:** We turn a tad cautious on NZD in the near-term after RBNZ decided to frontload the rate hikes with a 50bps move at the last meeting and signalled a downshift with a mention that the deliberations were between a 25bps hike and 50bps. RBNZ had even noted in the statement that the government "was comfortable that current lending rates faced by businesses and households will help ensure core inflation and inflation expectations" and the 50bps hike was a way to offset the downside pressure that the decline in wholesale interest rates have on the lending rates for businesses and households, whilst boosting retail deposit rates. There is thus a real chance that RBNZ would pause on 24 May or choose to signal pause then which would probably give NZD another nudge lower. RBNZ has been one of the most aggressive and decisive hawks since 2021. This shift could continue to crimp on the NZD vs. peers that are still on the tightening path (EUR, GBP).

- Apart from a less hawkish RBNZ and an upcoming divergence between the Fed and RBNZ, NZD drags also include a lack of strong recovery from China as well as increasing jitters in financial markets that typically hurt risk-sensitive NZD. Potential for further current account deterioration as manufacturing contracts could also weigh on the NZD. We thus revised the NZD lower but kept the trajectory in a bullish trend to reflect our view for NZD to gain against the USD as well as our optimistic outlook on China's recovery as well as expectation for the Fed to pause after the final hike in May.

- **Growth and Inflation Outlook**: Inflation slowed more than expected to 1.2%q/q vs. previous 1.4%. with tradable slowing to half its pace at +0.7%q/q vs. prev. 1.4%. Non-tradeable on the other hand, quickened to 1.7%q/q vs. previous 1.5%. Headline inflation eased towards 6.7%y/y from previous 7.2%. The inflation report for 1Q reflects how services sector continues to thrive, much like most parts of the world at this point as the re-opening theme and arrival of tourists continue to buoy demand for services more than goods. Food prices for Mar also slowed to 0.8%m/m vs. previous 1.5%, adding to the softer CPI headine. This was rather surprising given some expectations for food inflation to head higher in light of the damages fo Cyclone Gabrielle.

- Performance Services index (PSI) slipped only a tad to 54.4 from 55.8, a print that is still well in expansionary zone. This gauge is even above the long term average of 53.6 with all five sub-indexes in expansion. PSI activity/sales rose to 56.7 for Mar from 53.9 previously. Employment also firmed a tad to 51.3 from previous 51.1. New orders/businesses on the other hand, slipped to 53.1 from previous 56.3, albeit still an expansionary figure. Stocks/inventories slipped to 57.3 from previous 58.5. Notwithstanding slight deterioration, the PSI report was an overall strong one and paints a picture of buoyant activity in services. **In contrast, the BusinessNZ manufacturing PMI for Mar dropped to 48.1 vs. previous 51.7 (also revised lower). This would be in line with the world manufacturing scene and could potentially bode ill for its current account.a**

- **Monetary Policy Forecast:** RBNZ decided to frontload the rate hikes with a 50bps move at the last meeting and signalled a downshift with a mention that the deliberations were between a 25bps hike and 50bps. RBNZ had even noted in the statement that the government "was comfortable that current lending rates faced by businesses and households will help ensure core inflation and inflation expectations" and the 50bps hike was a way to offset the downside pressure that the decline in wholesale interest rates have on the lending rates for busienss es and households, whilst boosting retail deposit rates.

- There is thus a real chance that **RBNZ would pause on 24 May** or choose to signal pause then which would probably give NZD another nudge lower. Our bets lean towards an outright pause at the next meeting based on the decisive style of this central bank. The front-loading for the sake of Cyclone Gabrielle has been done at the last meeting and there are signs of weakness emerging, not just in home prices nit a;sp the manufacturing sector which has started to contract based on PMI for Mar. RBNZ has been one of the most aggressive and decisive hawks since 2021. This shift could continue to crimp on the NZD vs. peers that are still on the tightening path (EUR, GBP).

- **External Balance and Fiscal Outlook:** NZ current account could remain in deficit given a consistent deficit in its goods trade. 4Q current account deficit narrowed to NZD9.46bn (at -8.9% of GDP) vs. NZD11.4bn (-8.5% of GDP) in the quarter prior.

- At the Half-Year Economic and Fiscal update for 2022 in Dec, the Treasury Department looked for three quarters of negative GDP growth from 2Q of 2023 with the economy expected to contract 0.8% for full calendar year 2023. Budget deficit for 2022-2023 was projected to be NZ3.6bn and to return to surplus of NZ1.7bn in 2024-2025. Net debt seen to peak at 21.4% of GDP in 2023-2024 vs. 17.2% as of Jun 2022.

- **Key domestic events and issues to watch:** CoreLogic House prices for Apr [1 May], 1Q labour report, average hourly earnings for 1Q [3 May]; Mar builing permits [4 May]; ANZ Community Price for Apr [4 May]; Apr REINZ house sales [10-14 May]; Apr food prices [11 May]; BusinessNZ Mfg PMI for Apr [12 May]; 2Yr inflation expectation for 2Q [12 May];

Performacne Services Index for Apr [15 May]; Apr trade [19 May]; 1Q retail sales ex inflation [23 May]; RBNZ policy decision [24 May]; May ANZ consumer confidence [26 May]; building permits for Apr [30 May]; May ANZ Activity outlook, business confidenc [31 May].

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

CAD: Drags from Policy Divergence Amplified For Now

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

Previous Forecasts in Parentheses

- **Motivation for the FX View:** We maintain a constructive view on the CAD notwithstanding some pressure in the near-term as BoC is almost certain to keep policy rates unchanged for the rest of the year while Fed makes its (likely) final hike in May. Once the signal for a pause is provided, USD and UST yields should also start to ease.

- USDCAD has rebounded rather substantially on the back of oil decline, growth slowdown and BoC-Fed monetary policy divergence. Softening inflation pressure, private consumption and manufacturing activity could keep the BoC on hold. As a result, CAD continues to underperform more hawkish G7 peers (EUR, GBP). USDCAD could see a more discernible decline once the Fed signals a pause in May. Beyond the near-term, we also look for some support from recovery in crude oil prices (not ruling out further OPEC+ cut, China's recovery boost). A move below the 1.30-figure is still expected by the end of the year.

- **Growth and Inflation Outlook:** Canada's Mar Mfg PMI firmed only a tad to 48.7 from previous 48.8. The CFIB business barometer index improved for Mar, with firm's expectations for businesss performance for the next 12 months rising to 55.3 while the short-term optimism index rose to 52.2. Wage growth as well as plans to raise future prices have slowed. That suggest that the central bank may continue to take a wait and see approach to see whether the deceleration in demand as well as price pressure could pan out.

- Building permits for Feb surprised to the upside at 8.6%y/y vs. previous -3.7%. This may not last as existing home sales slowed to 0.4%m/m in Mar from previous 2.3%. Housing Starts also softened to 213.9K for Mar vs. previous 240.9K. Meanwhile, retail sales fell -0.2%m/m in Feb. vs. previous +1.6%. Ex auto, the fall was steeper at -0.7% vs. previous 0.9%.

These indicate some softening in spending as concerns over a downturn start to weigh.

- Labour market remains tight with unemployment rate steady at 5.0%y/y in Mar. Canada added a net 34.7k jobs with 75.5K added in service-producing, partially offset by the 40.9K job losses in goods-producing sectors, 6.1K of which is in manufacturing. Hourly wages softened to 5.2%y/y from previous 5.4%, albeit still elevated. Participation rate fell to 65.6% from previous 65.7%.

- CPI slowed quite considerably to 4.3%y/y for Mar from previous 5.2%. Core inflation (trim) also eased to 4.4%y/y vs. previous 4.8%, now higher than headline. Tight labour market conditions may continue to be supportive of spending and keep inflation from returning to target sooner. Wage growth has to ease more to rein in private consumption. 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.

- **Monetary Policy Forecast:** BoC is expected to keep rates unchanged at 4.50% on 7 Jun. 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. The decision reflects evidence of softening economic conditions (demand and inflation). 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 contrast to the OIS implied 35bps cut by Dec.

- Recall that in a speech before, Governor Macklem laid out the conditions that they are monitoring. The central bank wants price pressure for services to ease, wage growth and inflation expectations to moderate and the businsses need to normalize their price-setting behaviours in order to stave off any further rate hikes. **These seem to be progressing in a way that do not require BOC to consider further rate hikes. However, BoC is unlikely to provide any dovish signal anytime soon given that labour market is still tight with hiring momentum still ongoing and wage growth still healthy. It is more likely for the central bank to remain err on the side of caution until inflation is closer to the target of 1-3%. Strong services sector (as indicated in the breakdown of the labour report) could continue to keep core inflation from faling more rapidly.**

- **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 Apr, Int'l trade for Mar[1 May], Apr labour report [5 May]; Mar Buiding permits [10 May]; Manufacturing sales for Mar, Apr CPI [16 May]; Mar retail sales [19 May]; Industrial Product price for Apr [23 May]; CFIB Business Barometer for May [25 May]; 1Q current account bal [30 May], Mar GDP [31 May].

- **Technical Outlook:** USDCAD is also in range and was last seen around 1.369-figure. Pair remains within this range of 1.32-1.39. Daily chart indicates bullish momentum for the pair and could nudge this pair towards next resistance at 1.3720 before the next at 1.3860. Support at 1.3530 and then at 1.3430. Looking at the monthly chart however, bulish momentum is waning and the medium-term trend could be skewed to the downside.

JPY: Macro Conditions to Work in Favour

Forecast	2Q 2023	3Q 2023	4Q 2023	1Q 2024
USDJPY	**134** (128)	**132** (125)	**130** (122)	**128** (120)

No Change to Previous Forecasts

- **Motivation for the FX View: We revise our forecasts for USDJPY upwards to account for JPY weakness after the BOJ stood pat on policy and avoided any monetary adjustments in near term. Notably, the BOJ removed earlier dovish guidance and Governor Ueda kickstarted a policy review that could "last 12 to 18 months".** At this point, we recognize that it is expensive to hold a short USDJPY view (long JPY) and the upward momentum on USDJPY could be due to the unwinding of some bets for a more hawkish Ueda. At the same time, while the Fed is expected to raise rates by 25bps at the upcoming meeting, making it even more expensive to long the JPY, we do believe that they are coming to the end of their tightening cycle. As such, our downward trajectory for USDJPY remains intact as we continue to see JPY weakness as temporary and still believe the factors that can drive a stronger JPY would fully materialize throughout this year. These factors include 1) Softening Fed stance guiding UST yields lower, 2) Possibility of some minor monetary adjustment by the BOJ and 3) The return of the JPY's safe haven allure. Underpinning factor 1) is weakening US economic data that increases the chances of cooling inflation and raises the risk of an economic recession. As for factor 2), whilst Ueda did not move just yet after taking office, we think that a widening in the YCC band by 25bps to +/- 0.75% is on the cards from as early as June given that the market functionality issues is a matter that the central bank would want to resolve. For factor 3), falling UST yields would be supportive of the JPY's position as a safe haven in addition to the Japanese banks being in a relatively better position than the US or Swiss banks. Overall, we continue to hold to our short USDJPY trade.

- The looming US debt ceiling also looks to remain supportive of the JPY as FX volatility could be expected if the political stalemate persists. Our base case is that the debt ceiling will be raised and any sort of a US default would be avoided. However, there could be interim volatility in currencies and weakness in the DXY the longer the political stalemate persists. Upside risks for the JPY also exist in the unlikely event of a US credit rating downgrade or an even unlikelier US default. Although UST yields are likely to rise in such scenarios, we expect fundamentals will be against the USD and for the JPY, given that investors will likely lose confidence in the former and look to safe-havens such as gold, CHF and the JPY in such a situation. That said, we do believe that the debt ceiling discussions are political posturing by the Republicans at this point of time and our base case is for the debt ceiling to be lifted once they have extracted sufficient concessions. We note however, that our core view for a stronger JPY remains intact regardless of the outcome.

- **Growth and Inflation Outlook:** Inflation for March appeared to show that underlying price pressures are holding up as core inflation (ex fresh food) stayed at 3.1% YoY (Feb. 3.1% YoY) and core core inflation (ex fresh food and energy) accelerated to 3.8% YoY (Feb. 3.5% YoY). Headline inflation meanwhile slightly slowed down to 3.2% YoY (Feb. 3.3% YoY). Even though government energy subsidies have kicked in, there seems to be signs of strong underlying price momentum. Services inflation in particular continued to rise with the economy now reopened as people more easily can go out whilst more visitors are now returning back to Japan. Food inflation was also still strong at the same time. Overall, about 4/10 of the categories are standing above the BOJ's implied target inflation number of 2.0%. Going forward, we believe that core inflation can keep holding up given the stronger wage momentum following the large increases agreed at the Spring Wage negotiations. Headline in contrast could moderate in the coming months given the government energy subsidies. However, we are not expecting that the inflation numbers to date would be enough to shift the BOJ's thinking or stance just yet. The BOJ may not be immediately be convinced that underlying price pressures can sustainably hold up as it is still not clear just yet that wages would see strong increases year to year (especially if the reasoning of the recent large wage increase from the Spring negotiations was due to inflation rather than underlying labour tightness). Regardless, a continued strong underlying core CPI numbers can still help energize JPY bulls, who would continue to speculate on a BOJ shift and consequently give the currency support.

- High frequency indicators such as Apr (P) Jibun Bank mfg PMI showed some slightly pick up to 49.5 (Mar. 49.2) although it remained in contraction territory. The new orders index in particular showed an increase by 2.4pt to 49.3 from the prior month. The output index (-0.8pt), supplier delivery times index (+0.8pt – increase is actually a negative) and the stock of items index (-1.0pt) weighed on the overall number. In line with the fall in these two numbers was also a decline in the output forecast index (-2.8pt). Combined, the fall in the output index and the output forecast index could be some reflection of both weakening global economic conditions currently and going forward. Firms therefore may now be choosing to run down inventories instead. Meanwhile, the Apr (P) Jibun Services PMI was about static at 54.9 (Mar. 55.0) as underlying service PMI indices rose across the board. The near orders index increased by 3.0pt amid the recovery in foreign tourists coming into Japan. Business expectations index also increased by 3.0pt the new business index was up 1.0pt. Therefore, it looks like the service industry is actually generally on quite strong footing as it is. Overall, the PMI numbers shows an economy that is in some sense still quite fragile as industrial activity risk facing a tougher period even as services is stronger.

- Tourism expenditure is picking up strongly with spending by overseas visitors increasing to 1,014.6bn Yen in 1Q 2023 from 594.9bn Yen in 4Q 2022 according to Japan Tourism Agency data. This spending is now at 88% of 1Q 2019 even as inbound visitors so far in 2023 at only at 59% of 1Q 2019 levels. Average spending per visitor was at 212,000 Yen in 1Q 2023, which is about 44% higher than in 1Q 2019. Despite such positive numbers, we stay cautious about whether this is a structural shift of higher spending by tourists or it could just simply be temporary due to pent-up post Covid-19 travel demand and a weaker JPY. In any circumstance, the high spending by tourists is likely to give a boost to both 1Q 2023 GDP and the Mar Retail sales numbers.

- **Monetary Policy Forecast:** The Bank of Japan stood pat and did not change any of their policy parameters at the 28 April announcement. This was largely in line with our expectations as we earlier expected Governor Ueda to not rock the boat in his first meeting in charge. Notably however, the BOJ removed their dovish forward guidance regarding the policy rate being the same or going lower and they announced a policy review that could take 12 to 18 months to complete. The market sold JPY on the announcement in spite of the removal of dovish forward guidance, likely as bets on a more hawkish than expected Ueda were unwound.

- The uncertain parameters (broad-based) and length (12 to 18 months) of the policy review seem like the BOJ is kicking the can too far down the road. We think that this should introduce volatility into FX, especially as Ueda clarified that policy normalization was still possible even as the review on policy was in progress. There exists a tremendous divergence in terms of central bank policy rates between Japan and the rest of the world. Should this result in a growing US-Japan yield differential, we expect more pressure on the JPY in the near term. On the other hand, should the BOJ surprise the market with a tightening or other monetary adjustments, we should also see an outsized strengthening of the JPY as existing carry positions unwind.

- Our base case remains that a widening in the YCC band by 25bps to +/-0.75% is on the cards from as early as June given that market functionality issues are matters that the BOJ would want to resolve. Apart from market functionality issues, an easing of YCC parameters should allow the BOJ so unwind some of its already bloated balance sheet. This should also restore some credibility to the BOJ in terms of moving towards policy normalization in the face of inflation. Although the BOJ had explicitly referred to achieving its price stability target of 2% inflation in a sustainable and stable manner, accompanied by wage increases. While recent inflation prints have shown some signs of price increases, the BOJ perhaps wants to make clear that it wants to see a healthy sustainable increase in inflation, not purely from external price shocks, but driven sustainably alongside wage growth.

- **Latest External Balance Outlook:** The country's trade deficit for Mar further narrowed to -754.5bn Yen (Feb. -898.1bn Yen) as the pace of imports growth slowed down to 7.3% YoY (Feb. 8.3% YoY). Imports was mainly held down by a fall in mineral fuels and chemicals imports even as machinery and food imports increased. In fact, the machinery imports rose for the first time in five months. Machine imports is likely to keep recovering throughout this year with the Mar Tankan survey showing stronger capex plan figures for FY23. Exports meanwhile still saw an increase at 4.3% YoY (6.5% YoY). The transportation equipment and general machinery categories helped support export growth whilst electricidal equipment and chemical products were a drag. Transportation equipment exports have been on the rise as the semiconductor shortage issue alleviates. The trade deficit as a whole has been contracting since the peak since autumn 2022 with imports falling and hence, improving the JPY's position.

- **Key domestic events and issues to watch:** Apr (F) Jibun Bank mfg PMI (1 May), Apr (F) Jibun Bank services PMI (8 May), Apr (F) Jibun Bank composite PMI (8 May), Mar Labour cash earnings (9 May), Mar Household spending (9 May), Mar (P) Leading and coincident index (10 May), Mar BOP CA balance (11 May), Mar Trade balance BOP basis (11 May), Apr Bank lending (11 May), Apr PPI (15 May), Apr (P) Machine tool orders (15 May), Apr Nationwide dept sales (16 – 22 May), Apr Tokyo dept store sales (16 – 22 May), 1Q (P) GDP (17 May), Mar (F) IP (17 May), Mar Capacity utilization (17 May), Apr Trade data (18 May), Apr CPI (19 May), Mar Core machine orders (22 May), May (P) Jibun Bank mfg PMI (23 May), May (P) Jibun Bank services PMI (23 May), May (P) Jibun Bank composite PMI (23 May), Apr (F) Machine tool orders (24 May), May Tokyo CPI (26 May), Mar (F) Coincident and leading index (29 May), Apr Jobless rate (30 May), Apr Job-to-applicant ratio (30 May), Apr Retail sales (31 May), Apr Dept store, supermarket sales (31 May), Apr (P) IP (31 May), Apr Annualized housing starts (31 May) and May Consumer confidence index (31 May).

- **Technical Outlook:** USDJPY was last seen around 137.50 levels, with stochastics and RSI both flagging overbought conditions. MACD suggests momentum remains bullish, with resistances at 138.00 and 140.00 levels. Supports are seen at 137.00 and 135.00 (previous resistances turned supports).

RMB: Recovery Eclipsed by Geopolitical Fears and Policy Scars

Forecast	2Q 2023	3Q 2023	4Q 2023	1Q 2024
USDCNY	6.75 (--)	6.70 (--)	6.65 (--)	6.60 (--)
USDCNH	6.75 (--)	6.70 (--)	6.65 (--)	6.60 (--)

No Change to Previous Forecasts

- **Motivation for the FX View:** We are still constructive of the yuan and we expect mild appreciation against the USD this year but underperformance on a trade weighted basis could persist towards the 98-figure, last seen around 100.50 based on the official CFETS data.
- The tourism outflow has not happened to a large extent yet with the outbound travel for 2Q still expected to be around 64% lower than the same period in 2019. The current drags on yuan comes from a myriad of factors including the negative carry vs the USD, increasing market uneasiness over how the US is acting more aggressively to contain China's technology advancements, lingering risks of geopolitical conflict over Taiwan as well as scars from Xi Jinping's draconian policies imposed over recent years (the shutdown of private education enterprise, the technology crackdown, Covid-zero). Anecdotal newsflow highlighted falling foreign investments - new investments from Taiwanese firms falling 10.4%y/y in 1Q, Softbank cut majority its stake in Alibaba.
- Early this year, Premier Li Qiang has emphasized on how the state would continue to provide support to the private sector and "optimize the business environment" for local and foreign companies to thrive. Headlines might have been rather negative on the yuan and China but based on IIF data, equity flow and debt flow have been positive in Mar. We still see potential for stronger China recovery into the second half of this year to bring the USDCNY towards the 6.60-figure. At that point, positioning for the Fed to cut once US CPI eases closer towards inflation target would also undermine the greenback and bring the pair closer to our12-month forecast.

Growth and Inflation Outlook:

- 1Q GDP surprised to the upside with a print of 4.5%y/y vs. previous 2.9% (expected at 4.0%). Quarter-on-quarter, there was a stronger acceleration in growth to 2.2% vs. a flat growth in the quarter prior. Most noteworthy was retail sales' upside surprise a 5.8%y/y growth for mar vs. prev. 3.5%. Residential property sales rebounded pretty strongly at 7.1%y/y from previous 3.5%. However, it was clear that the recovery was not on strong footing yet with property investment clocking steeper than expected decline of -5.8%y/y vs. previous -5.7%. FAI was down to 5.1%y/y vs. previous 5.5% while industrial production only ticked higher to 3.0%y/y vs. previous 2.4%.

- Risks are to the upside for yuan based on recovery potential – a scenario that seem to be underpriced for now. We watch the housing market carefully for further recovery in order to sustain household spending. Average home prices seem to have risen by 0.44%m/m in Mar, a pick up from the 0.30% growth seen in the month prior. Broadly thus far for 2023, overall land purchases by developers remain subdued amid pressure to finish uncompleted projects or repay/restructure debts. However, there are signs of progress with Country Garden Holdings Co. purchased residential land in a local government auction for the first time since Dec 2021 (WSJ). Sunac announced a plan to restructure its debt worth U$9.1bn. China Evergrande said an agreement is reached with some creditors to settle $1915bn in foreign borrowings. Sales of residential buildingsrose 8.8% in Mar.
- Inflation has eased to 0.7%y/y in Mar from previous 1.0%. Month-on-month, CPI fell -0.3%m/m vs. previous -0.5%. Consumer goods eased ot 0.5%y/y from previous 1.2% while services inflation firmed to 0.8%y/y from previous 0.6%. Ex. Food and energy, CPI actually rose a tad to 0.7% vs. previous 0.6%. Demand remains rather subdued overall.
- This comes after several measures launched to support the housing market over the past few months - mortgage rates have been lowered, debt extensions were provided, the “three red lines” borrowing restrictions were reportedly eased for 30 unnamed property firms as a pilot program amongst others, allowing private equity investors to invest in developers and shifting towards completed home sales model as opposed to the build-to-order model. More recently, Xiamen has adjusted its purchase restriction policy and allow singles to buy a second home.
- In order to support consumption recovery, there were also measures to improve supply of rental apartments. Firms in the business of home rentals/leasing would be able to issue bonds to fund the construction, purchase and operation of their business. This is done in the hope that an increase in the supply for home rentals may improve the affordability of rentals.
- According to a PBoC survey, expectations for property prices have improved. A more material recovery in the real estate could potentially sustain a consumption-led recovery that the government looks for.
- **Monetary Policy Forecast:** PBoC kept its policy rates unchanged for Apr and could continue to do so for the rest of the quarter. However, there are whispers of banks being asked to reduce deposit interst rates in order to encourage the flow into investments. PBoC also conducted a survey and found that the overall loan demand index in 1Q 2023 had risen to 78.4%, a 18.9% increase from the quarter prior. Breakdown revealed that new loans were provided for manufacturing, infrastructure construction, services industries and real estate. These are nascent signs of activity recovery.
- 1Y MLF is expected to remain at 2.75% in May and that should keep 1Y loan prime rate at 3.65% and 5Y at 4.30%. It is likely that the government may want to assess the strength of the recovery after the re-opening before providing further stimulus in the second half of the year.

- **Latest Fiscal and External Balance Outlook:** Fiscal 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%.

- **Key domestic events and issues to watch:** China Apr NBS Mfg, Non-Mfg PMI [30 Apr]; Caixin Apr Mfg PMI [4 May], Caixin Apr Composite, Services PMI [5 May], Foreign Reserves (7 May), Apr trade [9 May]; Apr aggregate financing, money supply, new yuan loans [9-15 May], Apr CPI, PPI [11 May]; Apr FDI [11-18 May]; Current Account 1Q [12 May]; 1Y MLF [15 May], FX Net settlement on behalf of clients [15 May]; Apr retail sales, FAI ex rural, industrial production [16 May], 1Y, 5Y LPR [22 May]; Apr industrial profits [27 May], May 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: Potential Beneficiary of China's Reopening

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

No Change to Previous Forecasts

- **Motivations for the FX View**: Despite underperformance in the KRW in April, we maintain our KRW forecasts to account for China's anticipated re-opening effects coming in stronger later in 2023. The KRW has a high correlation to the CNY and China's reopening should boost Korea's economic growth prospects given the linkages between the two economies and geographical proximity. While we expect China's reopening to boost all Asian currencies, we think the KRW could be one of the largest (and most likely of) beneficiaries. We expect this reopening effect to outweigh the drag from a slowdown in global growth and the tech sector.

- April is a seasonally bearish month for the KRW, given that it is dividend payout season for Korean equities and these inevitably leads to foreign outflows from Korea as investors repatriate their investments. This causes strong headwinds for the KRW and has been observed throughout the month of April by underperformance in the KRW. However, we would expect pressures from these outflows to somewhat alleviate in May and think that there could be room for the KRW to pare back on April losses.

- Despite Samsung recently posting a record US$3.4b loss on its memory chip division, confirming the global chip downturn, the company joined other chipmakers in predicting some relief from the broad tech recession that has hurt some of the world's biggest tech companies such as Apple and Intel. In a view widely held by both industry players and observers, tech demand is expected to pick up later in 2023 on China's anticipated reopening and accelerating developments in the artificial intelligence space. This widely held narrative should provide some tailwinds for the KRW, should it turn out as expected.

- We also believe that the Fed is approaching the end of its tightening cycle and the market is also pricing in a Fed cut of 25bps as early as September (55.5%), with implied probabilities for cuts in November (80.2%) and December (87.8%) coming in at an even higher likelihood. We therefore believe the Fed to be truly coming to the end of the hiking cycle and this should be positive for the KRW, given that the BOK has already paused on its tightening and has provided hawkish forward guidance for its future actions.

- In addition, 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.

- **Risks to our View**: KRW's traditionally high-beta to global chip demand and global equity performance means that it is inclined to see amplified swings from geopolitical developments. While this is positive in the context of China's reopening, developing tensions between US and China could leave Korea stuck between a rock and a hard place. Korea is a US ally, but it has shown in refusing to join the US-led protectionist chip-bloc against China that it does not want to offend China. Indeed it could well be the case that Korea cannot afford to offend China. We see a potential drag on the KRW if tensions continue to escalate and Korea is forced to pick a side.

- We also note potential tensions with China, North Korea as risk triggers. Recall that China-Korea relations deteriorated in 3Q 2016 over US-Korea alliance decision to deploy US Terminal High Altitude Area Defense (THAAD) anti-missile system to defend against North Korea missile threat. President Yoon had earlier indicated plans to buy an additional THAAD system. This may be a concern for KRW if it induces risks of retaliation from China. But we also note some recent efforts from Yoon to avoid antagonizing China. Meanwhile, inter-Korean tensions are also in play as North Korea ramps up missile tests in recent weeks. South Korean president Yoon has warned of "overwhelming" response if North Korea attempts any nuclear action. Meanwhile, KRW also continues to be exposed to swings in broader geopolitical risks. E.g., Biden's warning of China potentially making a move on Taiwan on a “much faster timeline” than previously thought, continued aggressive Russian strikes in Ukraine etc., could continue to cap sentiment recovery.

- **Global growth concerns remain a persistent drag on high-beta/pro-cyclical KRW.** Global growth slowed in 2022 to 3.2% and is expected to remain at below-trend rates in 2023 and 2024. The OECD believes the Ukraine war to be the main cause for the moderation in growth recovery post-Covid and cost of living issues continue to persist globally. Global growth is projected to come in at 2.6% in 2023 and 2.9% in 2024. Further downside risks about the global growth and inflation outlook could weigh heavily on high-beta/pro-cyclical currencies like the KRW. Issues that potentially could lead to such a situation are the recent surprise OPEC+ production cuts, an escalation of tensions between Russia and the West, or the return of banking turmoil on a wider scale.

- Korea’s energy importer status also means that there is a serious risk to inflation running rampant following the most recent OPEC+ surprise production cuts. Analysts suspect that oil may once again rise to >$100/bbl and this could weigh heavily on global recovery as the costs of doing business rise. In such an environment, there would be a two-fold drag on the KRW via high inflation rates and poorer growth prospects. This risk has recently been reduced as oil prices moderated towards the end of April.

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

- In Feb, the BOK revised its real GDP growth projections to 1.6% in 2023 (prev: 1.7%) and 2.4% in 2024 (prev: 2.6%). BOK is expecting challenging headwinds from global economic sluggishness and interest rate hikes, but expect the economy to pick up in 2H2023 as external conditions improve, in particular as China’s anticipated reopening comes into play. Officials recognize that uncertainty remains high.

- South Korea’s unemployment rate in Mar came in at 2.7% (exp: 2.8%; prev: 2.6%), indicating that the labour market continues to be resilient and remains healthy. Meanwhile, Mar Industrial production came in at -7.6% YoY (exp: -10.2%; prev: -8.0%), showing that the anticipated slowdown in activity was better than expected and could potentially herald some recovery for the South Korean economy.

- South Korea’s Mar trade deficit was also narrower than expected at -US$4.6b (exp: -US$6.0b; prev: -US$5.3b). This was largely due to a smaller than anticipated fall in exports at -13.6% (exp: -16.0%; prev: -7.6%) and a corresponding -6.4% YoY fall in imports (exp: -6.5%; prev: 3.5%). 20-day export/import data also showed a drag as exports fell -11.0% YoY (pre: -17.4%) while imports fell -11.8% YoY (prev: -5.7%). Trade data prints are largely in line with the narrative that the external environment remains challenging and the drag from lower global demand will weigh on the Korean economy in 2023.

- On inflation, BOK expects CPI inflation to rise by 3.5% in 2023 and 2.6% in 2024. The expected deceleration is due to easing pressures from both an increased supply and reduced demand. However, this forecast was predicated on lower crude oil prices, a narrative which is at risk due to the surprise OPEC+ production cuts. In terms of actual outturns, Mar headline CPI inflation cooled to +4.2% YoY (exp: 4.3%; prev: 4.8%), but core CPI inflation remained sticky at +4.8% YoY (prev: 4.8%).

- **Monetary Policy Forecast**: The Bank of Korea (BOK) maintained its policy rate at 3.50% in April. This follows a similar pause in 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 April decision reiterated the BOK's resolve to combat inflation, although it also recognized downside risks to growth. However, this did not stop the underperformance in the KRW. While the latest headline CPI inflation print showed signs of easing, core inflation remains sticky at elevated levels. Market consensus is for BOK to hold at its upcoming May meeting. However, a growing camp is supporting earlier rate cuts amid plunging exports and a worsening property market in Korea. We remain cognizant of upside risks to inflation arising from OPEC+ production cuts and think that the BOK should on balance stand pat at 3.50% at the upcoming meeting.

- **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 current account for Mar came in at a -US$4.62b deficit, improving on the near -US$13b deficit in Jan. However, exports continued to fall, albeit by less than expected at -13.6% YoY (exp: -16.0%; prev: -7.5%). The persistent export drag and current account deficit (albeit small) could weigh on the KRW at the margin.

- **Key domestic data and events to watch in May:** Apr Trade (1 May), Apr CPI Inflation, Apr Manufacturing PMI (2 May), Apr Foreign Reserves (4 May), Bank Lending to Households (9 May to 16 May), Mar Money Supply (12 May), Apr Import/Export Price Indices (16 May), May 20-Day Imports/Exports (22 May), May Consumer Confidence, 1Q Household Credit (24 May), PPI Inflation, **Bank of Korea Policy Decision (25 May),** Retail Sales (27 May to 31 May), Apr Industrial Production (31 May)

- **Technical Outlook:** USDKRW last traded at 1338.50 levels and traded between a 1295 to 1345 range in April (1260 to 1330 range in March). Stochastics are overbought and RSI is neutral. Pair has broken out of the earlier well defined range bound by the 50dma and 200dma since February. Key upside resistance is at the 1350 level. We would suggest to watch for USDKRW to trade between a 1275 to 1375 range in May. Breakouts to the bottom to be supported by 1200 and to the top resisted by 1400 psychological levels.

SGD: Remain Constructive Despite MAS Stand Pat

Forecast	2Q 2023	3Q 2023	4Q 2023	1Q 2024
USDSGD	1.3150 (1.3000)	1.3000 (1.2900)	1.2950 (1.2850)	1.2950 (1.2850)

Previous Forecasts in Parentheses

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

- **As such, we revise our USDSGD forecasts slightly higher to reflect the policy staying unchanged but still expect the SGD to appreciate against the USD.** This is in line with our bearish USD-Asia core view for the year ahead. In addition, should the prevailing 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, given our house view that China's reopening will likely gain steam later in the year and this will drive the SGD stronger.

- 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, advance estimates showed that the Singapore economy contracted by -0.7% QoQ SA in 1Q2023 (exp: -0.1%; prev: 0.1%) and grew by +0.1% YoY (exp: 0.6%; prev: 2.1%). YoY growth was below our economists' expectations (+1.1%) on weaker than expected services growth (+1.8%). Our economists have lowered their 2023 GDP forecast to +0.8% (from +1.7%) in 2023, due to weaker than expected 1Q performance and downside risks to growth. MAS noted that growth prospects have dimmed in 2023, driven by further contractions in trade and subdued activity in the services sector. MAS sees downside risks to global growth and specifically to Singapore and are projecting a step down in GDP growth to 0.5% to 2.5% YoY in 2023 (2022: +3.6% YoY). On a whole, advance estimates show that growth in 1Q 20232 and MAS' growth projections paint a more pessimistic picture than we had expected.

- Mar Industrial Production came in at -4.2% YoY (exp: -6.1%; prev: -9.7%) and on a SA MoM basis grew by 9.3% MoM (exp: +1.1%; prev: -0.4%). Mar NODX fell by -8.3% YoY (exp: -19.4%; prev: -15.8%) and rose by +18.4% SA MoM (exp: 3.6%; prev: -8.2%). Feb retail sales rose 12.7% YoY (exp: +2.0%; prev: -0.8%). SG data was mixed and while there were some positives to be gleaned, there remains much room for improvement. Earlier dismal data prints contributed to the poorer than expected 1Q2023 advance estimates of GDP and were reflective of slowing growth prospects for Singapore's economy. That said, our economists see China's reopening later in the year having a bigger impact on economic growth and that should reflect in future economic data prints.

- 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 remain skeptical on 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. Our economists' maintain their projections for core CPI at 4.5% YoY and headline CPI at 6.0% YoY in 2023. In summary, MAS' inflation outlook was more sanguine than we had expected.

- Data releases saw Sep-Feb Core CPI Inflation remain persistent at elevated levels. In the light of the recent surprise OPEC production cuts, MAS could become more inclined to tighten given the potential inflationary effects of the rise in oil prices on Singapore. The implication of this is that inflation could be even sticker than initially thought. Our economists now forecast average core inflation at 4.5% in 2023 (up from 4% previously) and headline inflation at 6.0% (unchanged). MAS will likely raise its 2023 core inflation forecast to 4% to 5% (from 3.5% to 4.5%) and maintain headline inflation forecast at 5.5% to 6.5%. Core inflation remains sticky at levels well above MAS' comfort zone, with the latest Feb core CPI print coming at +5.5% YoY, with broad price increases across food, retail and services following a 1% hike in GST in Jan 2023 and a persistently tight labour market. Our economists also expect a chance that the expansion of the Progressive Wage Model to food services could fan food price pressures.

- **Monetary Policy Forecast:** The combination of a poorer than expected growth outlook and a more optimistic than expected inflation outlook likely influenced MAS' decision to stand pat rather than to tighten further. We note that MAS used "sufficiently tight" to describe the current policy stance in addition to their usual use of the word "appropriate". We think this could be a possible hint to their policy leaning in October. **Given the current outlook for growth and inflation, we think it is likely that MAS will be biased towards a stand pat in October as long as MAS' core inflation is on their projected trajectory.** However, we would not rule out a tightening in October or at an off-cycle meeting (likely July) should MAS' core inflation projections change materially in the event that upside imported inflation risks materialize.

- This latest decision is in line with the current market 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. We earlier highlighted that the recent OPEC surprise production cut could result in higher than expected oil prices and as such we would not rule out a tightening should such a situation be realized. 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.

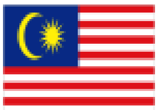
- The FY2022 deficit meanwhile was smaller than projected at 0.3% of GDP or SGD2bn (vs initial projections of 0.5% of GDP or SGD3bn). Draw on reserves was also lower than initial estimations at SGD3.1bn (vs expectations of SGD6bn). The overall drawdown from past reserves from FY2020 to FY2022 totaled 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 remained poor in Mar as Electronics Exports printed at -22.3% YoY (prev: -26.5%), NODX at -8.3% YoY (exp: -19.4%; prev: -15.8%), although NODX rose +18.4% on an SA MoM basis (exp: 3.6%; prev: -8.2%). These conditions remain reflective of the moderation in global demand and the overall tapering of economic growth prospects in Singapore and abroad. Singapore's Current Account balance for 1Q2023 is expected to come in at 17.0% of GDP (4Q2022: 19.3%). Singapore's current account has enjoyed a structural surplus and a weakening of the current account balance is not expected to have a material impact on the SGD.

- **Key domestic events and issues to watch in May:** Apr PMI/ESI (3 May), S&P Global PMI Apr, COE bidding (4 May), Foreign Reserves (4 May to 8 May), Mar Retail Sales (5 May), Apr NODX and Electronic Exports, COE bidding (17 May), 1Q Final GDP (22 May to 26 May), Apr CPI Inflation (23 May), Apr Industrial Production (26 May), Apr Money Supply (31 May)

- **Technical Outlook:** USDSGD was last seen at 1.3340 levels. Stochastics are at overbought levels, while RSI is neutral. USDSGD has mainly range-traded through Apr, largely keeping within our earlier expected of 1.32 to 1.3550 (specifically 1.3204 to 1.3392). We see similar two-way interest going forward for USDSGD, with the 1.32 to 1.3550 barring any surprise from the Fed (3 May). Shooting star candlesticks have also formed in the daily USDSGD charts on the last two trading days of Apr, and this could portend some SGD strength heading into the Fed meeting.

Looking further ahead, we expect USDSGD to test the 1.3150 level sometime this quarter. This could happen sooner than expected should the Fed itself signal that it is coming to the end of its tightening cycle at the upcoming FOMC decision.



MYR: Waiting for the Turnaround

Forecast	2Q 2023	3Q 2023	4Q 2023	1Q2024
USDMYR	**4.30** (--)	**4.20** (--)	**4.10** (--)	**4.10** (--)

No Change to Previous Forecasts

- **Motivation for the FX View:** USDMYR largely hovered around 4.40 levels in Apr before rising the last few weeks to a high of 4.47 on the back of concerns about the slower than expected recovery in China, lingering fears on banking sectors around the world, recent softer than expected export and commodity market developments and lingering domestic related concerns which in part led to some selling in equities. Our trajectory remains unchanged for the USDMYR, reflecting our continued mildly bearish view of the USD in 2H 2023 and some eventual resiliency in the MYR on the back of some pickup in China and regional recovery. In addition, we also note the possibility of a 25bp hike to 3.00% by BNM this year as expected by our economists amid sticky core inflation as a result of demand and cost push inflationary pressures. This is relative to an eventual dovish Fed as a mild recession in the US leads to a shift in Fed policy in 2H 2023 onwards. These should provide some mild support to the MYR.
- As such, we continue to maintain a cautiously positive outlook for the MYR even amid the sharp climb in the USDMYR pair since mid Jan. A few factors recently have been weighing on the MYR which include a rebound in the USD (driven by anxiety about the pace of US inflation earlier and more recently USD support amid global financial stability concerns) and fading optimism from China's initial reopening. However, our view on US inflation stays intact of which we expect it to keep moving in a bumpy downward trajectory and we think the financial concerns may linger but contained in its global contagion effects. Consequently, we have been careful not to overstretch recent Fed hawkishness and our in-house views sees that the US rate would likely hit 5.00-5.25% in 2023. Further data releases from China would give more clarity on the country's pace of recovery. Therefore, we see that the MYR should receive more positive support going forward.
- Regardless, we stay mindful of the various risks related to the MYR. These include the inherent possibility that the Fed has to hike more aggressively than expected as shifts in data shows US inflation stays at

an elevated level. Additionally, we are wary of sentiment taking a hit from political uncertainty especially in light of upcoming state elections. There is also the possibility of oil prices being hurt by the pressure that high Fed rates could cause on the economy.

- Putting into context, our model estimates suggest that MYR performance going forward would depend to a large extent on the following key factors, i.e., resilience/recovery in oil prices, continued stabilization in the political environment and fiscal dynamics, and sustained positive RMB narrative amid China re-opening. At the same time, the MYR is also the most undervalued among the Asian currencies based on our Maybank BEER model. An improvement in sentiment towards the currency could therefore substantially lift the currency.

- **Growth and Inflation Outlook:** Feb 2023 saw firmer growth in Industrial Production Index (IPI) (Feb 2023: +3.6% YoY; Jan 2023: +1.8% YoY), Distributive Trade Index (DTI) (Feb 2023: +10.6% YoY; Jan 2023: +8.5% YoY) and Crude Palm Oi (CPO) output (Feb 2023: +10.2% YoY; Jan 2023: +10.1% YoY). Inputting these indicators into Maybank's monthly GDP tracker, our economists estimated monthly GDP grew +6.2% YoY in Feb 2023 (Jan 2023: +4.3% YoY; 2M 2023: +5.3% YoY; 4Q 2022: +7.0% YoY).

- Consequently, going forward, our in-house economists **expect growth for 2023 to normalize to a fair 4.0% YoY (2022:+8.7%).** The number itself is also some reflection of the effects of high inflation – interest rate environment on the global economy. Offsetting those headwinds include a drawdown of household/individual "excess savings", FDI growth momentum and faster growth from China as it emerges from its Covid19 – zero policy.

- Mar 2023 exports and imports declined to -1.4% YoY (Feb 2023: +9.8% YoY; Jan 2023: +1.4% YoY) and -1.8% YoY (Feb 2023: +11.1% YoY: Jan 2023: +2.2% YoY) while trade surplus widened to +RM26.7b (Feb 2023: +RM19.6b; 1Q2023: RM64.4b). This year, ***amid softer global economic growth, our economists expect export and import growth to slow to +4.0%*** (3M2023: 2.8%; 2022: +25.0%) and +6.0% (3M2023: +3.7%; 2022: +31.3%) with trade surplus of +MYR240b (3M2023: +MYR64.4b; 2022: +MYR255.5b

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

- Headline inflation rate moderated to +3.4% YoY in Mar 2023 (Feb 2023: +3.7% YoY; 1Q 2023: +3.6% YoY). Core inflation eased marginally to +3.8% YoY (Feb 2023: +3.9% YoY; 1Q 2023: +3.9% YoY). ***Maintain our 2023 inflation rate forecast at +3.0%, mainly on base effect and as fuel subsidy stays for the time being as per the re-tabled Budget 2023, although inflation risk remains biased to the upside amid fluid price subsidy/control policy.***

- **Monetary Policy Forecast:** Amid headline inflation "stickily" easing from the peak in Aug 2022 and as core inflation being higher than headline since Oct 2022, BNM again kept OPR unchanged at 2.75% at Mar 2023 MPC after the pause in Jan 2023 MPC. But the latest Monetary Policy Statement (MPS) retains the words "further normalization", implying current pause does not mean the end of OPR hike cycle. MPS also added that it is keeping an eye on cost factors – including those arising from financial market development, which we think is largely about Ringgit – that could affect inflation outlook. **We expect another +25bps hike this year to bring OPR back to pre-COVID 19 level of 3.00%.** The next MPC is on 2-3 May 2023.

- Overall, BNM sees the current monetary policy stance to remain supportive of economic growth and will continue to balance the risks to domestic inflation and economic growth. More importantly, BNM continues to monitor the impact of past Overnight Policy Rate (OPR) adjustments on the economy and so far, the impact of the adjustments on financial conditions has been orderly, no signs of excessive tightening in consumption and investment and at the same time moderates the strength of inflationary pressure amid normalisation of inflation expectations. BNM also iterates that further normalisation to the degree of monetary policy accommodation evolves both global and domestic conditions and their implications on the overall outlook of domestic inflation and economic growth. These include various cost factors, including those arising from financial market developments that could affect the inflation outlook and more than expected persistent price pressures.

- BNM has kept the OPR unchanged at 2.75% for the second consecutive Monetary Policy Committee (MPC) meeting on 5-6 Mar 2023. BNM said the decision was to allow it to continue assessing the impact of last year's four OPR hikes totalling +100bps (between May and Nov) on growth and inflation. Despite the pause so far this year, we do not see this as the end of OPR upcycle, and ***still see the scope for another +25bps increase in OPR to 3.00%, especially given the upside risk to inflation from the "fiscal policy overhang" with regards to fuel subsidy.*** To also note, the pause in BNM's OPR hike cycle has happened before i.e. the post-GFC interest rate hike cycle where OPR was raised from the then record low of 2.00% to 2.75% between Feb 2010 and July 2010, then paused before it was raised again to 3.00% in May 2011 and stayed there for the next three years.

- **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**: Our forecasts of slower 2023 exports and imports growth of +4.0% (2022: +25.0%) and +6.0% (3M2023: +3.7%; 2022: +31.3%) reflects our projection of slower global real GDP growth forecast (2023E: +2.0%; 2022: +3.4%). ***We expect narrower trade surplus of +MYR240b this year (2022: +MYR255.5b).*** Three months into the year, the external trade performance reflected the headwinds from the economic downturns in US and Europe given the slowdown in exports to US (3M2023: +8.0% YoY; 2022: +17.5% YoY) and drop in shipments to EU (3M2023: -2.3% YoY; 2022: +21.8% YoY), but we expect tailwinds to external trade via exports to China (3M2023: -8.1% YoY; 2022: +9.4% YoY) from firmer growth in China on its full economic re-opening to kick in subsequent months. Meanwhile, the sharply slower 1Q 2023 growth in exports (+2.8% YoY vs 4Q 2022: +11.8% YoY) and imports (+3.7% YoY vs 4Q 2022: +18.5% YoY) as well as decline in trade surplus (-1.0% YoY to +MYR64.4b) point to external demand being a drag on 1Q 2023 real GDP growth for Malaysia last quarter

- **Key domestic events and issues to watch:** PMI Mfg (2 May), BNM Policy Decision (3 May), Mar IP (9 May), Mar Trade data (19 May), Foreign reserves (9 May, 22 May), GDP (12 May), Apr CPI (26 May).

- **Technical Outlook:** USDMYR was last seen around 4.4615.Stochastics are rising into overbought condition. Key resistance is marked by the 200-dma at 4.4833 before 4.5270. Support at 4.4250 (100-dma). We see consolidative trades to continue within the 4.38-4.50 range.

IDR: Staying Positive Given Favourable Fundamentals

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

No Change to Previous Forecasts

- **Motivation for the FX View:** The IDR had a reasonably strong month as it continued to appreciate with the USDIDR now sitting quite below the 15,000 mark. The high yielding appeal of the IDR together with its favourable fundamentals (trade surplus in 1Q 2023 and strong fiscal discipline) has likely been attracting a lot of interest especially as expectations increase of an end to the Fed tightening cycle. This interest has also been reflected by a positive net inflow into Indonesia Government Bonds (IGBs) over the last month. We believe that foreign inflows into the IGBs would keep strengthening going forward and continue supporting the IDR. Hence, we hold on to our forecast of the USDIDR trending downwards over the next year.

- **Growth and Inflation Outlook:** After the lower than expected Mar inflation with headline at 4.97% YoY (est. 5.12% YoY) and core at 2.94% YoY (est. 3.03% YoY), BI also made the decision to soften its inflation outlook. The central bank now sees that headline inflation would return to its target range of 2 – 4% by August (earlier than previously projected at September). They also expected core to remain within the target range for the rest of 2023. Our in-house economists have also concurrently lowered their 2023 headline inflation forecast to 3.7% YoY (from 4.2% YoY) and expect core at 2.6% YoY given this faster than expected softening in inflation and the limited second-round effects from higher fuel prices following the Sept 2022 +30% hike. Falling food inflation due to last year's high base and the El Nino conditions (leading to more food production at major producers such as Brazil and the USA) should also contribute to the lower CPI. Overall, the falling inflation is strengthening BI's case for a pause, which in turn would reduce the domestic rate support for the IDR. However, the IDR would still get a boost from a widening IGB-UST spreads amid the possibility of an end to the Fed tightening cycle. Meanwhile, we do take note of the risks related to OPEC's decision to cut output by 1.15m bpd that can lead to higher oil prices and inflation. However, the government on the other hand may avoid hiking fuel prices (as the 2024 election approaches) this year given the 30% hike in Sept 2022 last year (instead possibly putting pressure on the fiscal position).

- Retail sales strengthened in March as consumer confidence hit a 7-month high at 123.3. BI itself had noted that consumption had received a boost from Ramadan, discount programs and smooth distribution of goods. Retail sales had seen quite a turn-around in the last two months from the negative number see in January, which implies the economy is now on a more sound footing.

- **Monetary Policy Forecast:** BI unsurprisingly again held rates at 5.75% at its latest policy meeting, in line with expectations. The central bank's tightening cycle looks to have come to an end especially with inflation pressures having eased. The IDR is also among the best performing currencies regionally against the USD in the month of April so far. As mentioned earlier, the central bank has softened its inflation outlook as they now see headline returning within the target range of 2 – 4% by August (compared to previous expectations of September). BI also expects that both current account and capital & financial account to record a surplus in 1Q 2023, which would give strong support to the IDR. They also at the same time maintained their GDP growth forecast at the upper end of the 4.5 – 5.3% range with the governor believing that softening inflation would support private consumption whilst investment and exports will remain solid.

- Regarding the FX proceeds matter, there has been some improvement in the appetite for the USD term deposits. There is now interest in the longer tenors compared to previously when all placement had just been in the 1-month tenor. Exporters had placed $26.5m in the 3-month tenor for the 4 April auction whilst the 11 April auction saw $6.8m placed in the six-month deposits. As it stands, the developments look encouraging.

- **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:** March trade balance was still in surplus although it narrowed quite significantly at $2.9bn (Feb. $5.5bn). This was due to a plunge in exports by -11.3% YoY (Feb. 4.4% YoY) that was driven by a fall in coal exports (-1.8% YoY) and palm oil (-28.2% YoY). The former coal exports had seen prices plunge given weaker gas prices, resulting from warmer than expected weather conditions in Europe. Palm oil's decline was a result of the high base in the prior year that in turn had been driven by the Russia-Ukraine war. By country, non-oil & gas shipments were no longer held up by China whilst exports to other countries such as the US, Malaysia, South Korea and India fell substantially, which maybe reflective of weakening global economic conditions. Imports meanwhile saw a bigger fall of -6.3% YoY (Feb. -4.3% YoY) due to a fall in raw materials and consumer goods imports, which offset increases in capital goods imports. Our in-house economists as a whole though still expect the country to maintain a trade surplus going forward (albeit narrower) due to the lower oil prices compared to last year. Therefore, the country's trade position should continue to be supportive of the IDR.

- Mar foreign reserves rose to $145.20bn (Feb. $140.31bn) as USD broad strength came off amid the banking crisis and speculation that the Fed tightening cycle could be coming to an end. The increasing possibility of the latter happening soon we believe is likely to give a boost to EM FX and hence, we therefore see that foreign reserves should continue to climb this year.

- There was a net foreign inflow of $0.3bn into Indonesia Government Securities (IGBs) up until 14 Apr 2023 as appetite continued to improve amid speculation of the Fed tightening cycle ending soon. IGBs can be seen as more attractive than other high yielding peers given the stronger fundamental position of Indonesia as the government continues to exercise strong fiscal discipline (with the fiscal deficit having stayed below the fiscal legal limit of 3.0% of GDP in 2022) and the country resiliently continuing to maintain a trade surplus so far this year. We believe that appetite towards IGBs is likely to keep strengthen this year as the Fed gradually soften its stance.

- FDI for 4Q 2022 stood at $5.3bn which brings the entire 2022 total at about $20.8bn. This marked an increase of about 5.8%, which is a reflection of the emergence of the economy out of the pandemic. For now, we are expecting that the level of FDI should at least remain stable in 2023. Indonesia as a whole is likely to still mainly see FDI inflows into the primary and secondary sectors. This is due to both the drive to boost downstream activities and grow the EV related industries.

- **Key domestic events and issues to watch**: Apr S&P Global mfg PMI (2 May), Apr CPI (2 May), 1Q GDP (5 May), Apr Foreign reserves (8 May), Apr Consumer confidence index (9 May), Apr Trade data (15 May), Apr Local auto sales (15 – 21 May), 1Q BOP CA balance (23 May) and BI Policy decision (25 May)

- **Technical Outlook:** We see the pair at 14700 levels, with RSI and stochastics flagging oversold conditions, although both are rising. MACD indicates momentum remains bearish. We see supports at 14500 and 14400, with resistances at 14700 and 14800. We expect the pair to likely trade within the 14700 to 15000 range in the near-term given the uncertain global environment, but remain medium-term bullish on IDR.

PHP: Cautious Amid Weak Fundamentals

Forecast	2Q 2023	3Q 2023	4Q 2023	1Q 2024
USDPHP	54.25 (-)	54.00 (-)	53.75 (-)	53.50 (-)

No Change to Previous Forecasts

- **Motivation for the FX View:** The PHP has been facing a challenging April as it saw quite substantial declines. The currency had been hurt by the BSP Governor hinting at a rate pause (amid slowing inflation), corporate USD demand in addition to some first half month strength in the broad USD and oil prices. Strength in both the USD and oil prices did come off later in the month but that does not appear to have been enough for the PHP to pare back all its losses just yet. Even so, we think any remaining recent weakness should eventually dissipate as corporate USD demand wanes and the Fed tightening cycle comes closer to an end, leading to the PHP paring back more of its losses. However, PHP gains beyond the paring back of these losses would be limited by the currency's weaker fundamentals of a deep twin deficit. Therefore, we believe that the USDPHP should tend to our cautious forecasts.

- **Growth and Inflation Outlook:** Our economists for now continue to hold their growth forecast for 2023 at 5.5% YoY, which marks a slowdown from the 2023 level at 7.6% YoY. The 2023 forecasted level stands lower than pre-pandemic growth rates of around 6.0-7.0%. The deceleration of growth comes on top of fading pent up demand as the economy emerges out of the pandemic. Also, high inflation is likely to hurt household consumption. External demand too is expected to weaken amid a slowing global economy although China's recovery should provide some spillover benefits to Asian economies. Infrastructure spending may help support the economy but implementation can also take time. Overall, the economy still appears rather fragile and hence, concerns of the impact that higher BSP rates can have on it.

- High frequency indicators such as the S&P Global Mfg PMI released in Apr still seemed to show that industrial activity is holding up. The number for Mar continued to decline for a second month in a row to 52.57 (Jan. 52.7) but it still remained in expansion territory as it has so for the last year.

- Headline inflation in Mar slowdown below expectations to 7.6% YoY (Feb. 8.6% and est. 8.0% YoY) as base effects began to kick in. Transports costs, food & non-alcoholic beverages (FNAB) and housing & utilities

(HWEGOF) all saw deceleration. The easing in transport inflation was driven by brent oil prices being at a much lower level compared to last year. Lower electricity and gas costs helped offset high rental and water supply costs that led to HWEGOF decelerating overall. FNAB saw general easing as a whole. Core inflation meanwhile still rose substantially at 8.0% YoY (Feb. 7.8% YoY), which implies strong underlying price pressures in the economy. Going forward, we expect inflation to keep easing as base effects continue to weigh in. Food prices should also soften although it may stay elevated amid weather disturbances and high costs of fertilizer and feed meal costs. The cumulative BSP rate hikes should also have a significant effect on slowing down inflation. Our in-house economists are expecting that headline inflation would come out at 5.9% YoY in 2023 (which is still slightly higher than the 2022 level at 5.8% YoY).

- **Monetary Policy Forecast:** Governor Felipe Medalla this month hinted at the possibility that the central bank could pause rate hikes. The Governor himself said, "We're probably pausing in the next meeting because the inflation prints are very good. If April turns out to be a very low inflation month, so that's three good points in a row, we are in the position to pause." His words appeared to weigh on the PHP in April as it reduced support for the currency from a domestic rates angle. Our in-house economists still expect that the central bank would raise rates by an additional 25bps to 6.50% before end 1H 2023 given that core inflation continues to raise whilst the output gap at the same is still at "zero" compared to being "negative" last year. They then expect the BSP to stay on hold at that level for 2H 2023. With one last hike potentially to be the case, support for the currency from a domestic rates angle would reduce from there.

- **Latest Fiscal Outlook:** Feb budget balance fell into deficit at PHP106.4bn (Jan PHP45.7bn) as revenue declined by -0.25% YoY whilst spending marginally rose by 0.01% YoY. As a whole, fiscal pressures are likely to keep persisting amid an expansionary budget, which would weigh on the PHP. The 2023 NEP is guided by the Medium-Term Fiscal Framework (MTFF) and the proposed 2023 budget is therefore expected to come out 4.9%, higher than in 2022. Expenditure on infrastructure is likely to be sustained at around 5.0% of GDP in 2023 (2022: 5.8% of GDP) with the focus being on the development of rail transport. The fiscal deficit for 2023 is also estimated to come out at a wide level of -6.1% of GDP (2022f: -7.6% of GDP). The MTFF though is aiming to improve revenue via the imposition of value-added tax on digital goods and excise tax on single-use plastics.

- **External Balance Outlook:** Feb trade balance continued to see a deficit although it narrowed to -$3.9bn (est. -$5.0bn and Jan. -$5.7bn). This came on top of a plunge in exports by -18.1% YoY (Jan. -13.5% YoY). The export group that saw the largest fall was the electronic products commodity group. Imports meanwhile also fell heavily by -12.1% YoY (Jan. 3.9% YoY) with the biggest declines being in electronic products, transport equipment, cereals and cereal preparations, iron and steel ad chemical materials and products. Amid a fragile global economy, trade can risk continuing to weaken. Our in-house economists expect an overall 2023 trade deficit at -$59bn (2022. -$58bn) as exports growth slow amid a more depressed global economy. Imports growth is also expected to weaken although it won't offset exports. The country's trade deficit position would continue to weigh on the PHP.

- OFWR growth for Feb 2023 eased to 2.4% YoY (Jan. 3.5% YoY), which was at a 9 month low. There was softer repatriation from major source countries such as the US and UK, which offset sustained growth from South Korea and Europe ex-UK as well as pick up in Canada, Singapore, Japan, Hong Kong, Taiwan and Middle East. In PHP terms, OFWR growth was at 10.3% YoY in 2M 2023 compared to 3.0% YoY in USD. This was not only a reflection of the currency translation gains but also that overseas workers had to repatriate less back to their families. Regardless of a softer month for OFWR growth, our in-house economists expect it to still stay resilient for 2023 and project it to come out at 3.0% YoY despite economic challenges such as the risk of more banking stress and the economy directly being hit by high rates. The past two downturns have shown that repatriation still sustains during difficult periods instead of slumping as overseas workers do more to support families back home. For now though, the global economy is still appearing to hold up as the global composite PMI for Mar was at 53.4. Regarding the PHP, OFWR may be of some support but it wouldn't be enough to offset the negative effects arising from the twin deficit position and a worsening of risk appetite during periods of downturn.

- Bonds saw foreign net outflow of -$0.3bn as of 31 Mar 2023. Appetite for Philippines bonds have been weak amid concerns about the country's fundamentals – deep twin deficit position. The government's push for more infrastructure development and the possibility of higher oil prices can also risk worsening their position. From a domestic rates angle, Medalla's comments recently about a potential BSP pause in rate hikes also likely has hurt appetite for Philippines bonds. We are not expecting appetite for bonds to substantially improve near term given the country's structural concerns.

- Meanwhile, equities saw a net foreign inflow of $0.018bn as of 20 April 2023. Inflows into equities have been rather tepid amid fragile global market sentiment as investors continue to digest mix macro data and assess Fed speakers' comments on the likelihood of the Fed ending its tightening cycle. Sentiment towards equities are likely to remain shaky in the near term amid this uncertainty.

- FX defensive buffers saw some improvement in Mar as foreign reserves rose marginally to $100.2bn (Feb. $98.2bn) amid broad USD weakening that month. However, reserves would likely fall in April as the PHP has come under more selling pressure. For this year, it would be challenging to see foreign reserves rise sustainably this year given the less favrouable twin deficit position of the PHP.

- **Key domestic events and issues to watch**: Apr S&P Global mfg PMI (2 May), Apr CPI (5 May), Apr Foreign reserves (5 – 10 May), Mar Unemployment rate (8 May), Mar Trade data (9 May), 1Q Agriculture output (10 May), 1Q GDP (11 May), Mar OFWR (14 – 18 May), BSP Policy decision (18 May), Apr BOP overall (18 – 22 May), Apr Budget balance (25 May) and Apr Bank lending (28 – 31 May)

- **Technical Outlook:** USDPHP trades at 55.30 levels with stochastics flagging overbought conditions while RSI is neutral. MACD is indicating bullish momentum, although a bearish crossover looks to have just formed and could indicate a change in trend. We see supports at 55.00 and 54.20. Resistances are at 56.30 and 57.20.

THB: Stay Optimistic Amid China's Recovery

Forecast	2Q 2023	3Q 2023	4Q 2023	1Q 2024
USDTHB	33.50 (-)	33.00 (-)	32.25 (-)	31.50 (-)

No Change to Previous Forecasts

- **Motivation for the FX View:** The USDTHB has been ranged traded around 34.00 – 34.50 for much of April as investors remained on the edge awaiting more signs on the pace of China's recovery. As a whole though, we still stay positive regarding the THB as we believe that China's economic recovery would start to pick up pace more strongly as the year goes by, leading to a greater number of tourist inflows into Thailand (in particular, there should be a larger increase in 2H2023). A rescinding broad USD strength amid a possible Fed tightening cycle end and somewhat robust appetite for gold, given concerns regarding the global economy, should also provide further support for the THB. Meanwhile, Thai general elections would be occurring on the 14th May but we expect any resultant THB weakness (especially via the effects it could have on hurting bond inflows) would be temporary and that it should eventually dissipate together as the election outcome becomes clearer. Overall, we therefore continue to hold our forecasts for the USDTHB.

- **Growth and Inflation Outlook:** Mar headline inflation decelerated back to the BoT's target range and to a 15 month low at 2.8% YoY (Feb. 3.8% YoY) as food prices softened from last year's high base whilst transport costs also declined amid more moderate oil prices. Core inflation meanwhile slightly fell to 1.7% YoY (Feb. 1.9% YoY) and was unchanged from the prior month. A number of the core categories remained generally stable. With a stronger than expected downtrend in inflation, the Commerce Ministry has lowered its headline inflation forecast down to 1.7 – 2.7% (from 2 – 3% previously). Similarly, our in-house economists also lowered their inflation forecast to 2.7% YoY (from 3.3% YoY previously).

- Growth wise, our in-house economists continue to maintain their forecast at 4% YoY as they see that the tourism led recovery is still intact and that there will be minimal disruption from the upcoming elections. Their base-case for growth had also already factored in potential delay in budget approvals and government spending resulting from a political transition.

- **Monetary Policy Forecast:** The BoT reiterated that it will keep focusing on policy normalization, which implies the central bank is sticking to gradual tightening until inflation is clearly in retreat. BoT Governor Sethaput Suthiwartnarueput has said that "inflation has returned to target earlier than expected, but we have to see whether the trend is intact" and additionally noted that "core inflation in services sector may be sticky given rising tourist arrivals". He also noted that "the most important thing now is stability both for fiscal and monetary" policies and "not boosting the economy". Our in-house economist are expecting that the BoT would raise rates by another 25bps to 2.00% at the next May meeting although they see this would likely be the terminal rate. The support for the currency from a domestic rates angle should therefore be limited going forward.

- Foreign reserves as of Apr 14 was at $224.3bn as there hasn't been much change in the level for the last couple of weeks. The USDTHB as a whole has also been ranged traded during that time period too. We see that reserves can continue to raise generally throughout 2023 amid receding greenback strength.

- **Latest Fiscal Outlook:** Election has been set for the 14th May following the dissolution of parliament on the 20th March. As it stands, a NIDA poll that surveyed 2,000 people from 3rd April to 7th April is showing that the Pheu Thai Party, which is associated with Paetongtarn Shinawatra (the 36-year old daughter of ex-Prime Minister Thaksin Shinawatra) is still leading with 47.2% in favour of the party. The Move Forward Party is at a distant second with 21.2% in favour of them whilst Prayuth Chan-o-cha has a 10.8% approval rating. The same NIDA poll also showed that Paetongtarn Shinawatra was the most popular choice for Prime Minister (PM) with 35.7% in favour of her. Pita Limjaroenrat of the Move Forward Party is at second place with 20.25% in favour whilst Prayuth Chan-o-cha remained third with 13.6% in favour.

- However, the selection of the new PM is not simply a straightforward process of who gets the most vote in this election. The appointment of the PM would require the support of the majority of members in the House of Representatives and Senate combined. There are 500 seats in the House of Representatives (400 are constituency MPs whilst 100 are party lists MPs) and 250 seats in the senate. The 250 seats in the senate were appointed by the military regime that came to power after the May 2014 coup. For an opposition MP to become the PM, his/her party would need to capture essentially 376 out of the 500 seats (about 75% of all seats) in the House of Representatives. As a note, parties controlled by the Shinawatra clan has actually won every election since 2001 and even twice with a landside but three of its governments had been removed in military coups or court rulings. A candidate backed by the Junta would in essence only need the support of 126 seats of the House of Representatives to be appointed PM (and as a formality, a royal endorsement from the King).

- The Pheu Thai Party is chasing for a landslide victory but if they fail to do so, the party is also open to forming a government with like-minded groups.

- Voter turnout is expected to be strong given active campaigning by political parties. Turnout has exceeded 70% since the 2007 with the exception of the 2014 election, which the opposition had boycotted. This time around, there would also be 3m new voters, making up 5% of all eligible votes, who came of age during the youth protest in 2020 that had demanded Prayuth's resignation. In total, 14.7% of all voters consist of youth aged between 16 and 26.

- All major parties not surprisingly have put out populist policies with pledges from the top 9 parties requiring Bt3.1tn per year after excluding their overlapping policies (according to analysis by Thai Development Research Institute) even despite a rule that prevent parties from attracting votes with non-economically viable pledges (by requiring them to specify the cost of policies and the sources of funding). Among the more prominent pledges include the Pheu Thai Party promising to triple farmers' income and putting in place a 3 year debt moratorium. They also vowed to nearly double minimum wages to Bt600, whilst worker's with a bachelor's degree would draw a minimum monthly salary of Bt25,000. The party has also mentioned that it will seek to collect Bt300bn from businesses currently outside of the tax system to plug the budget deficit. Prayuth's United Thai Nation party is pledging to increase benefits for welfare cardholders from Bt200 – 300 to Bt1,000 a month and create a fund to boost crop prices in the northeast. The current ruling Palang Pracharath (PPRP) party is promising to raise the state welfare scheme benefits to Bt700 per for month for those earning less than BT100,000 a year.

- Such promises of wage increases are coming at a time when FDI in Thailand has already been on a losing momentum amid rising labour costs, ageing population and more competition from other regional peers. In fact, Thailand's manufacturing wages are the second highest in the ASEAN region after Malaysia. The minimum wage itself had been raised by 5% to Bt328 – 354 just recently on 1 Oct 2022. Beyond wages, the Eastern Economic Corridor (EEC) may risk facing project delays given that a proposal to adjust a construction contract for the HSR linking the three airports was not approved by a board meeting in early March. This can dampen foreign investment at a time when it has just picked up after the pandemic.

- An implications of this election is that the passing of budget FY2024 could risk being delayed. This would imply that disbursements may be disrupted. More concerning, capex disbursement has consistently been falling below target over the years and this budget delay only serves to worsen the problem.

- Deputy PM Supattanapong Punmeechaow though has said that his government would not let the political vacuum affect the economy and insists that they will accelerate budget disbursement.

- As mentioned earlier, our in-house economists continue to keep their growth forecast intact at 4% YoY for 2023 despite the election as they believe that there would be minimal disruption to the tourism led-recovery. Their base-case has already factored a political transition that may result in delays for budget approvals and government spending.

- The behavior of the currency during past elections has been mixed. In the 2014 election, the USDTHB rose building up towards the elections but it would later retrace its gains. As for the 2019 election, the USDTHB was generally tracing the movements in the DXY. However, we believe any resultant THB weakness from the upcoming election should be temporary and would dissipate as the election outcome becomes clearer.

- **Latest External Balance Outlook:** Mar trade balance swung into a surplus for the first time in a year at $2.7bn However, the underlying were not too positive. Exports tumbled by -4.2% YoY (Feb. -4.7% YoY) as exports of industrial products stayed weak at -5.9% YoY (Feb. -6.2% YoY). Agricultural exports on the other hand though rose for the second straight month at 4.2% YoY (Feb. 3.6% YoY). Thailand has raised its rice export target as prices have risen amid a shortage due to the ongoing war in Ukraine. Country wise, export to China continued to fall at -3.8% YoY although this should improve as the country's recovery continues to progress. Exports to Japan and the US were the largest for the month. Our in-house economists are still maintaining their export forecast at -3% to +1% for this year. Meanwhile, imports saw a big fall at -7.1% YoY, which helped allow for the balance to be in surplus. The decline was mainly due to the high base for oil imports last year with oil prices now having moderated this year. Overall, Thailand's external position is likely to be more supported this year by tourism inflows (than the goods trade), especially from China, which provide support for the THB.

- From a portfolio perspective, equity and bonds saw an outflow of -$0.1bn and -$0.9bn respectively. The outflow in equities could be due to the election uncertainty and fragile global market sentiment as investors continue to speculate on the end of the Fed tightening cycle. As for bonds, the outflow could be due to concerns about the results of the upcoming elections and the uncertainty on how political parties eventually plan to fulfil their pledge should they win. However, we believe that inflows are likely to come back after the elections are over and the dust settles. History has shown this to be the case with foreign outflows prior to both the 2014 and 2019 election and a surge inflows in the months after the elections are over. Also, appetite towards Thai bonds should receive a boost once the BoT signals that it is done with hiking rates (Our in-house economists believe that there would only be one more hike of 25bps by the BoT).

- **FDI performance would continue to be watch closely in 2023.** FDI for the final quarter fell to $1.3bn (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**: Apr S&P Global mfg PMI (2 May), Apr CPI (3 May), Apr Consumer confidence (5 May), 1Q GDP (15 May), Apr Car sales (18 – 24 May), Apr Customs trade data (23 – 28 May), Apr ISIC capacity utilization (26 – 30 May), Apr ISIC mfg production index (26 – 30 May), Apr BOP CA balance (31 May), Apr BOP overall balance (31 May), Apr Trade data (31 May) and BoT policy decision (31 May).

- **Technical Outlook:** USDTHB was last seen at 34.20 levels, with stochastics falling just shy of overbought levels and RSI neutral. MACD shows that momentum is neutral, although it could possibly turn bearish soon. We see resistances at 34.50 (50ma) and 35.40 (200ma) levels, with supports at 34.00 and 33.40 levels.

VND: Growth Challenges Could Weigh

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

No Change to Previous Forecasts

- **Motivation for the FX View:** We maintain the trajectory of the USDVND forecasts as well as the level. Moves of the pair had been muted for much of the past month. Equity markets were lackluster with HCM Index down 2% (1-27 Apr). Vietnam continues to experience equity outflows for Apr with $115.2mn of net equity outflows clocked between 1-27 Apr.
- In spite of softer growth outlook and risks posed by the real estate liquidity crunch, USDVND could still trend lower as the end of the Fed tightening cycle draws close and US yields start to extend their decline, providing SBV a more benign environment to cut policy rate to support growth without severely undermining the VND.
- Vietnam clocked USD8.2bn of FDI beween Jan-Apr 2023 with investment flows from Singapore leading with around $2.2bn. The Foreign Investment Agency reported that $4.1bn of new projects were granted with investment licences during the four months. Processing and manufacturing attracted the lion share of capital flow of around $5.1bn.
- The flow of investment could have provided the buffer for VND given the persistent portfolio outflow that Vietnam has witnessed in the past four months. Somehow, investment confidence might have been slightly affected by the recent liquidity challenges faced by property developers and possible contagion effects on the financial system as well as weaker global growth outlook.
- The government has acted to support growth by reducing the VAT rate to 8% from 10% as well as provided CIT deductions for busineses. The VAT reduction will last from Feb to Dec this year. CIT deductions could be claimed for any donations or sponsorship expenses related to pandemic in the country for FY2022 (Vietnam Briefing). Earlier, there were measures to cut corporate income tax rate for SMEs to support the smaller businesses and such fiscal measures should be supportive

of the VND. 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 to 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:** Based on available data, credit growth for Vietnam remains weak at just 2.57% since the start of the year, as of 20 Apr. Lending was around 6.46% over the same period in 2022. This underscores weak demand at home and well under the 15% credit growth target. Deputy Governor Dao Minh Tu was cited noting that headwinds in real estate and capital markets have hurt credit expansion.

- **PM Pham had urged commercial banks to ease lending rates for busiensses.** He also wants more measures to support corporate bonds and property markets. We can expect another round of weak activity data for Apr that could beckon another interest rate cut from SBV.

- 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.

- This comes after 1Q GDP surprised to the downside at +3.3%y/y for 1Q vs. previous +5.9% in 4Q 2022. Growth was slowest since 3Q 2021, weighed by manufacturing sector led by the -13% plunge in computer, electronics & optical products on the back of communication equipment and consumer electronics.

- Industrial production for Apr picked up pace to 0.5%y/y from previous -1.6%. Exports fell -17.1%y/y from previous -14.8%. Imports fell more than expected by -20.5%y/y vs. previous -11.1%. Trade suplus widened to $1.51bn. Retail sales slowed to a growth of 11.5%y/y from previous 13.4%. Month-on-month, retail sales rose 3.7%, buoyed by tourism revenue and accommodation & food services. Rising tourist arrivals have been supporting retail sales but expect retail sales growth to weaken in the face of high base according to our economist. Consumers may also be less willing to spend as hiring slows.

- Inflation eased unexpectedly to 2.81%y/y from 3.35%. Food inflation slowed to 3.62%y/y vs. prev. 3.97%. Housing/construction materials alo slowed to 5.20%y/y from previous 6.68%. Transport prices fell -3.94%y/y vs. prev. 4.91%. Education slowed sharply to 5.98%y/y vs. previosu 8.41%. Core inflation rose 4.56%y/y vs. previous 4.88%. Our economist cut headline CPI foreast to 3.4% from 4.3% as the economic slowdown cools inflation by more than previously expected.

- **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%.
- Head of Monetary Policies at SBV Pham Chi Quang said that SBV has room to consider more policy rate cuts as inflation slows and credit growth remains low. He expects inflation to meet target at around 4.5% and the central bank has been urging commercial lenders to lower lending rates to support businesses.
- **Along with the downgrade in GDP, our economist looks for SBV to cut refinancing rate and short-term deposit rate caps by another 50bps in 2Q , albeit with no further change to the discount rate.**
- 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. However, the extent of uncertainty is likely to be limited relative to what was seen in 2022 and that should also limit the USD bullish momentum and threats to the VND.
- **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:** May CPI, Industrial production, Trade are due 25-30 May.

FX Forecasts

	End Q2-23	End Q3-23	End Q4-23	End Q1-24
USD/JPY	134.00	132.00	130.00	128.00
EUR/USD	1.1000	1.1100	1.1200	1.1300
GBP/USD	1.2300	1.2300	1.2400	1.2400
AUD/USD	0.7000	0.7200	0.7300	0.7300
NZD/USD	0.6300	0.6500	0.6700	0.6700
USD/CAD	1.3200	1.3000	1.2800	1.2800
USD/SGD	1.3150	1.3000	1.2950	1.2950
USD/MYR	4.3000	4.2000	4.1000	4.1000
USD/IDR	14700	14400	14200	14000
USD/THB	33.50	33.00	32.25	31.50
USD/PHP	54.25	54.00	53.75	53.50
USD/CNY	6.75	6.70	6.65	6.60
USD/CNH	6.75	6.70	6.65	6.60
USD/HKD	7.80	7.80	7.80	7.80
USD/TWD	30.00	29.30	29.00	29.00
USD/KRW	1300	1280	1270	1260
USD/INR	80.00	80.00	79.00	78.50
USD/VND	23400	23300	23300	23200
DXY Index	101.63	100.59	99.56	99.07
	End Q2-23	End Q3-23	End Q4-23	End Q1-24
SGD/MYR	3.27	3.23	3.17	3.17
JPY/SGD	0.98	0.98	1.00	1.01
EUR/SGD	1.45	1.44	1.45	1.46
GBP/SGD	1.62	1.60	1.61	1.61
AUD/SGD	0.92	0.94	0.95	0.95
NZD/SGD	0.83	0.85	0.87	0.87
CAD/SGD	1.00	1.00	1.01	1.01
SGD/IDR	11179	11077	10965	10811
SGD/THB	25.48	25.38	24.90	24.32
SGD/PHP	41.25	41.54	41.51	41.31
SGD/CNY	5.13	5.15	5.14	5.10
SGD/HKD	5.93	6.00	6.02	6.02
SGD/TWD	22.81	22.54	22.39	22.39
SGD/KRW	989	985	981	973
SGD/INR	60.84	61.54	61.00	60.62
SGD/VND	17795	17923	17992	17915
	End Q2-23	End Q3-23	End Q4-23	End Q1-24
JPY/MYR	3.21	3.18	3.15	3.20
EUR/MYR	4.73	4.66	4.59	4.63
GBP/MYR	5.29	5.17	5.08	5.08
AUD/MYR	3.01	3.02	2.99	2.99
NZD/MYR	2.71	2.73	2.75	2.75
CAD/MYR	3.26	3.23	3.20	3.20
MYR/IDR	3419	3429	3463	3415
MYR/THB	7.79	7.86	7.87	7.68
MYR/PHP	12.62	12.86	13.11	13.05
MYR/CNY	1.57	1.60	1.62	1.61
MYR/HKD	1.81	1.86	1.90	1.90
MYR/TWD	6.98	6.98	7.07	7.07
MYR/KRW	302	305	310	307
MYR/INR	18.60	19.05	19.27	19.15
MYR/VND	5442	5548	5683	5659

Source: Maybank FX Research and Strategy as of 2 May 2023.
*These forecasts are meant to be indicative of FX trends and not meant to be point forecasts.

DISCLAIMER

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