

FX Insight

Fed's Bazooka and Its Implication on FX

Cumulative 150 Bps Rate Cut and \$700bn "QE" Unleashed

Fed cut rate by 100bps to 0 - 0.25% target range and relaunch bond buying program by at least \$700bn. The latest set of easing measures was targeted at supporting the flow of credit to households and businesses as well as to serve as a coordinated policy response to Federal government's measures to counter COVID-19 impact. The textbook reaction to a large Fed cut should have been some relative strengthening for EM Asia FX as interest rate differentials move in Asian economies' favor. But this may not play out much in current context as strong Fed reaction could induce worries of a protracted negative shock to global growth and demand from COVID-19 outbreak. That and likely further easing from Asian central banks dampened Asian FX sentiments.

G7 Plays: Favor EUR, JPY vs. Short CAD, AUD, NZD and USD

We do not prefer FX that are highly sensitive to market development and those where their respective central banks have room to ease or are contemplating unconventional monetary policies. Some of these FX include CAD, AUD and NZD. RBNZ had most recently (16 Mar) cut rate by 75bps to record low of 0.25% and is working on asset purchase program. For AUD, RBA could potentially announce QE plan as early as this Thu. We also do not favor the USD as Fed's balance sheet has room to play catch up with ECB and BoJ. The size of Fed's current balance sheet (at \$4.24tn) is still below its peak (of \$4.5tn) in 2014 and still pales in comparison to BoJ and ECB, which have overtaken Fed in 2017. There is still room for Fed to potentially expand its balance sheet. We continue to favor typical safe haven FX, including EUR and JPY whereby their rates are already in negative territories and are perceived to have limited room for monetary stimulus.

Asian RV Plays: Long THB, PHP, CNH, TWD and SGD vs. Short KRW, MYR, IDR

We remain positive on the THB, PHP, CNH, TWD and SGD given their relative resilience to market volatility. We note that MAS easing is already priced in somewhat for SGD, with SGD NEER at -1.3% below implied policy mid as of writing. TWD and SGD also have the capacity to benefit from renewed regional demand growth, particularly in electronics, as Covid concerns eases sequentially in 2H. A return of tourism flows, albeit from a low base, and an overall positive current account surplus could support the THB. Meanwhile, recent PHP weakness is likely exacerbated by worries over the central Manila lockdown.

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Two Emergency FoMC Intra-Meetings - 150bps Cut and \$700bn “QE”

In a surprise emergency meeting (15 Mar), the Fed cut rate by **100bps** to **0 - 0.25% target range** and **relaunch bond buying program by at least \$700bn**, of which \$500bn will be on buying Treasury securities and \$200bn in MBS securities beginning today and over coming months. Other measures include **sharply lowering the rate charged to banks for short term emergency loans from its discount window to 25bps** from 1.75%, **allowing banks to borrow from the discount window for as long as 90 days**, re-adjusted **USD swap lines with 5 central banks** including ECB, BoJ at near-zero interest rates for up to 84 days, etc..

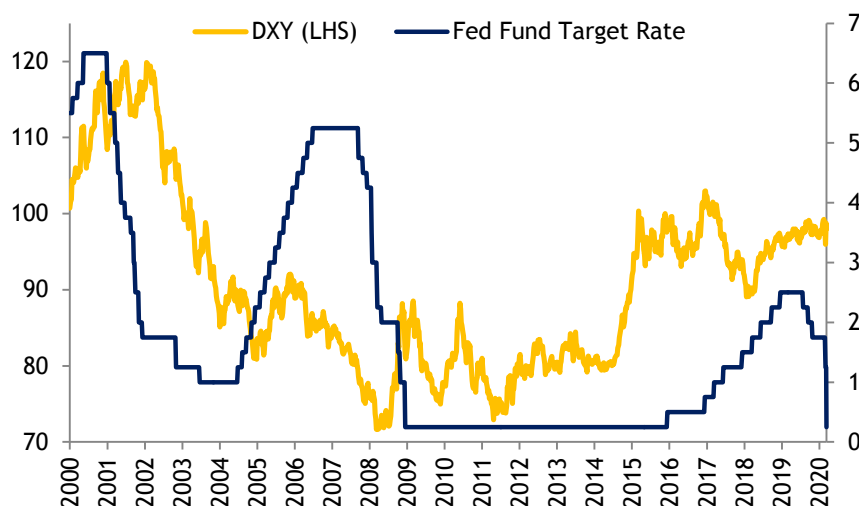
The Fed also provided forward guidance, indicating that it expects to “maintain this target range until it is confidence that the economy has weathered recent events and is on track to achieve its maximum employment and price stability goals”. There will be no scheduled FoMC meeting this week, and no summary of economic projections or dots plot for rates forecast.

The latest set of **easing measures was targeted at supporting the flow of credit to households and businesses as well as to serve as a coordinated policy response to federal government’s measures** (which included access to free testing, provide \$1bn in food aid and extend sick leave to vulnerable Americans) to counter COVID-19 impact.

This comes after the first emergency Fed meeting on 3 Mar, when Fed delivered 50bps cut to bring Fed fund target range to 1% - 1.25%. At the press conference then, Fed Chair Powell said he “recognised that a rate cut will not reduce the rate of infection, it won’t fix a broken supply chain but we do believe that our action will provide a meaningful boost to the economy”. He added that “the spread of the coronavirus has brought new challenges and risks... virus and measures being taken to contain it will weigh on economic activity here and abroad for some time”.

So all in, the Fed has dramatically cut rate by 150bps and re-launch bond purchase program of \$700bn, in a space of 2 weeks.

Fed Cut Rates to Lower Bound



Source: Bloomberg, Maybank Research & Strategy

March 16, 2020

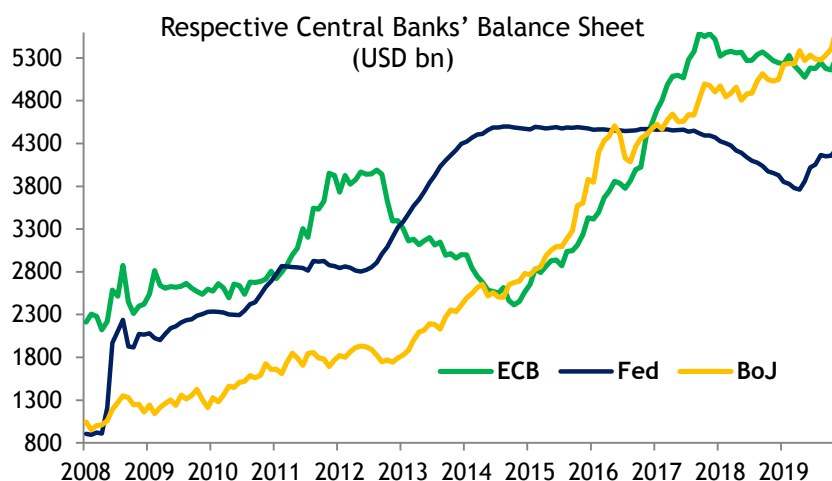
Fed QE - A Quick Overview

In the wake of the Global Financial Crisis (GFC) 2007-08, which found its roots in the US housing market had rapidly spread to the US financial sector, with the collapse of the Lehman Brothers and then to the global financial sector, the Fed had used unconventional monetary policy tools - quantitative easing (or QE) - in an attempt to ease financial conditions, increase market liquidity and support smooth functioning of markets.

- QE 1 - Initiated in November 2008. The Fed proposed to buy \$100bn of agency debt and \$500bn of mortgage-backed securities (MBS);
- QE 1 was extended in March 2009. The Fed proposed to buy another \$850bn in MBS and debt;
- QE2 - Started in November 2010. The Fed proposed to buy \$600bn worth of longer-dated treasuries by mid-2011;
- Operation Twist - Initiated in September 2011 as a maturity extension program aimed at increasing the average maturity of the bank's treasury portfolio, resulting in the Fed buying \$400bn worth of Treasuries with maturities between 72 and 360 months and sold off an equal amount in 3 - 36 month tenor;
- QE3 - Initiated in September 2012. The Fed proposed to buy \$40bn worth of MBS per month with an open-ended time frame;
- QE3 (infinity) - Extended on December 2012, an increase in the amount of open-ended purchases from \$40bn to \$85bn per month.

In June 2013, the Fed Chair Bernanke announced a potential scale-back of its asset purchases (or what is known as tapering). He held back making the decision and only announced in December 2013 that the Fed would begin tapering its purchases in January 2014. That concluded Fed's QE experiment which started in 2008, where its **balance sheet ballooned from under \$1tn to a peak of nearly \$4.5tn in 2014**. That said size of Fed's current balance sheet (at \$4.24tn) is still below its peak in 2014 and still pales in comparison to BoJ and ECB, which have overtaken Fed in 2017.

Still Room for Fed to Expand Its Balance Sheet



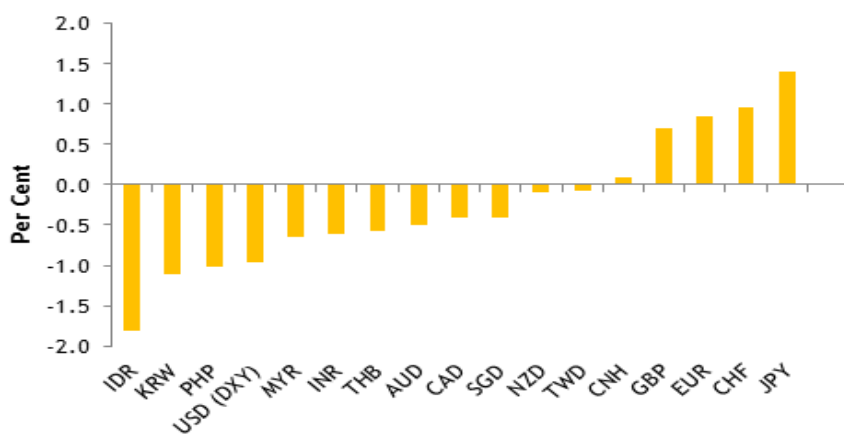
Source: Bloomberg, Maybank FX Research & Strategy

Market Reaction to Recent Fed Moves - Different in Each Episode

In the 3 Mar Fed's 50bps rate cut, USD fell decisively lower across the board, with AXJs including KRW, MYR and THB appreciating.

But the same cannot be said in the 15 Mar episode when Fed cut rate by 100bps and relaunch QE. The market's reaction was largely negative, with 10y UST yield gapped more than 30bps lower while S&P500 futures went limit down as Fed's surprise and somewhat drastic response (3 days before scheduled FoMC) implied an enormous sense of urgency (and potentially desperation) that the COVID-19 outbreak may be worse than expected. USD was mixed with USD falling against the negative yielding, safe-haven FX proxies including JPY, EUR and CHF but the USD rose against most AXJs, including IDR, PHP.

AXJs Broadly Softer vs USD while Negative Yielders Outperformed



Note: Outcomes are vs. USD except for DXY

Source: Bloomberg, Maybank FX Research & Strategy

The textbook reaction to a large Fed cut should have been some relative strengthening for EM Asia FX as interest rate differentials move in Asian economies' favor. But this may not play out much in current context as strong Fed reaction could induce worries of a protracted negative shock to global growth and demand from Covid. That and likely further easing from Asian central banks likely dampened Asian FX sentiments. In particular, risk-proxy KRW and portfolio flow-sensitive IDR saw the most weakness. Even PHP which has been relatively resilient prior is not spared, as the central Manila lockdown weighed on sentiments over domestic economic activity.

USD Moves - Choppy and Differentiated

We take stock of choppy USD price action since 21 Feb when the **USD started to decline as its carry appeal and risk on proxy status crumbled** in the face of sharp sell-off in US equities, plunge in UST yields. Drivers for these include poor US data (slump in services PMI, softer CFNAI, etc.), Fed's emergency 50bps cut, leading markets to price in further rate cut at the upcoming FoMC as well as COVID-19 outbreak in US.

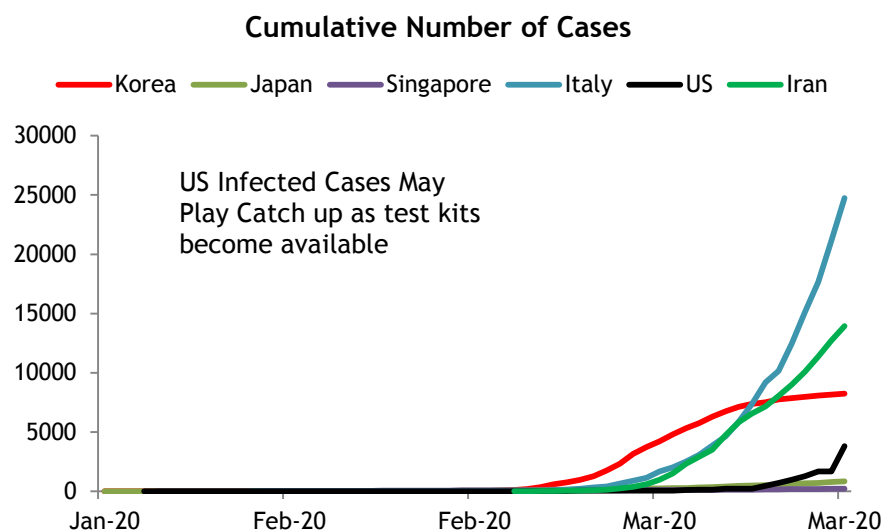
But the past few sessions saw a turn-around as DXY retraced more than 50% of the >5% decline since 21 Feb. We attributed the recent DXY rebound to dollar regaining its safe haven status amid market flight to

quality, in light of the massive sell-off in all asset classes from equities to oil to gold - somewhat a resemblance of a typical market meltdown (for reference, most equity markets including US, EU, Japan, Australia are down between 20 and 30% YTD while Dow Jones was down around 50% during GFC 2008-09 but over a longer time horizon of about a year).

In this episode, apart from COVID-19 pandemic, the plunge in oil prices (50% YTD) due to Russia-Saudi stand-off on oil production added to the general risk off sentiment (USD +ve). This is also in line with our earlier caution that USD decline will slow at some stage when UST yields have fallen low enough for USD to regain its safe-haven status.

So if we can keep it simple as a general rule of thumb, **when the risk-off is US-centric, USD is a sell; but when the risk-off becomes global, with concerns over USD-shortage and liquidity issues, the USD is a buy.**

Spike in COVID-19 Cases in US Can Weigh on USD



Source: WHO, Worldometer, Maybank FX Research & Strategy

Into the next two weeks, eyes are particularly on the number of infections in the US which is expected to surge exponentially and we take guidance from the epidemic curves of Italy and Iran that have not plateaued despite lockdown measures imposed by Italy. The Director of the US National Institute of Allergy and Infectious Disease, Dr. Anthony Fauci spoke on Sunday and expects test access to be “infinitely better” than few weeks ago. US Vice President Mike Pence has also assured that the “US is moving to widespread testing”. So as the US ramps up on diagnostic capacity, we can expect the COVID-19 cases reported by the US to swell.

In fact, confirmed cases of COVID-19 as reported by Worldometer at last check for today (16 Mar) has more than doubled to 3802 vs. the number of cases reported to WHO for 15th Mar at 1678. So far, Trump's declaration of state of emergency has allowed the Federal Government to distribute up to \$50bn in aid to states, cities and territories but there is no lockdown of any region in the US. Should the pace liken that of Italy and Spain, restrictions on interstate travels and even a 14-day national shutdown as suggested by Dr. Fauci may not be out of question. Equity markets could take a further hit at that point. USD liquidity could be affected again by brutal rounds of equity sell-off. That has been

somewhat USD positive insofar. However, in an environment where COVID-19 becomes a more US-centric issue, USD may ultimately be hurt. Beyond the near-term, the sharp and intense correction in equity bourses may eventually attract bargain hunters and investors would be watching for any signs of deceleration in the new cases reported by the US.

Long EUR, JPY vs. Short CAD, AUD, NZD, USD

We reiterate that in the G7 world, we **do not prefer FX that are highly sensitive as well as those where their respective central banks have room to ease or are contemplating unconventional monetary policies.** Some of these FX include CAD, AUD and NZD. RBNZ had most recently (16 Mar) cut rate by 75bps to record low of 0.25% and is working on asset purchase program. For AUD, RBA could potentially announce QE plan as early as this Thu. We also do not favor the USD as Fed's balance sheet has room to play catch up with ECB and BoJ.

We continue to favor typical safe haven FX, including EUR and JPY whereby their rates are already in negative territories and are perceived to have limited room for monetary stimulus.

Long THB, PHP, CNH, TWD, SGD vs. Short IDR, MYR, KRW

A part of current USD strength is arguably exacerbated by liquidity issues. As the Fed continues to inject liquidity into global markets—via bond purchases, allowing banks to borrow from the discount window for as long as 90 days and reducing reserve requirement ratios to zero percent, lowering the rate on standing U.S. dollar liquidity swap arrangements by 25 bps—and pertinent on banks working to pass the liquidity on, could lead to some easing of USD credit concerns. If this plays out, other factors such as interest rate differentials could regain their influence on USD-AxJ pairs and AxJ FX may see some subsequent recovery vs. USD once market volatility eases a tad.

High-beta FX, Risky assets Can Still Underperform when US Rates are Cut to Lower Bound as seen from 2008 GFC when Fed Unleashed QE1; Recovery Only Sets in Few Months Later in Mar 2009



Source: Bloomberg, Maybank FX Research & Strategy

Further out, we also remain positive on the THB, PHP, CNH, TWD and SGD given their relative resilience to market volatility. We note that MAS easing is already priced in somewhat for SGD, with SGD NEER at -1.3% below implied policy mid as of writing. TWD and SGD also have the

capacity to benefit from renewed regional demand growth, particularly in electronics, as COVID-19 concerns eases sequentially in 2H. A return of tourism flows, albeit from a low base, and an overall positive current account surplus could support the THB. Meanwhile, recent PHP weakness is likely exacerbated by worries over the central Manila lockdown. But we note that on net, drags on growth are likely manageable relative to peers, given the more closed nature of its economy. As long as COVID-19 cases do not escalate drastically, sentiments should be supported overall. For CNH, the successful containment measures at home have somewhat paid off and as production level continues to recovery, investors are determined to look past the ugly data for Jan-Feb in favour of CNH. Anticipation of more rate cuts also increases the allure of the RMB bonds, also boosted by expectations for FTSE Russell to include China in its Government Bond index.

What's Next in Terms of Fed Policies?

We do not expect Fed to go beyond its lower bound rate to the negative realm as Fed Chair Powell had re-emphasized that negative interest rate is not an appropriate policy response. We do not rule out the chance of another increase in asset purchase program by a larger amount (as seen from prior QE1 extension) if markets do not stabilise and if COVID-19 outbreak goes out of hand especially with the potential spikes in infected cases in US as test kits become available.

DXY - Consolidate; Risks Skewed to the Downside



In the last FX Insight, [The Domino Impact of an Oil Shock, 10 Mar 2020](#), we shared our caution for DXY to rebound in the near term. That has played out as DXY rebounded has high as 98.81 (13 Mar). DXY was last seen at 97.57 levels. Mild bullish momentum on daily chart remains intact but RSI suggests waning traction. We do not rule out consolidative price action from here with risks skewed to the downside. Support at 97.26 (50% fibo retracement of 2020 high to low), 96.64 (38.2% fibo) and 95.90 (23.6% fibo). Resistance at 98.70 (76.4% fibo).

Measures Announced Thus Far

	<u>Fiscal Measures</u>	<u>Monetary Measures</u>
US	<p>(13 Mar 20) Trump announced a state of emergency, allowing Federal Government to distribute up to \$50bn in aid to states, cities and territories.</p> <p>(11 Mar 2020) House approved the aid bill to provide enhanced unemployment benefits, free virus testing and additional funds for food assistance. Senator has to vote for it this week.</p>	<p>(3 Mar 20) Unscheduled 50bps cut to the FFTR.</p> <p>(12 Mar 20) Fed massively expanded reverse repo operations, injecting \$1.5tn of liquidity to the banking system.</p> <p>(15 Mar 20) Fed cut interest rate by 100bps down to 0.00-0.25%. Fed also restarted QE with the purchase of \$500bn in USTs and \$200bn in MBS. In addition, Fed also allows banks to borrow from discount window for as long as 90 days and it units with five other CBs to ensure dollar availability via swap lines.</p>
Italy	(11 Mar 20) A \$28bn plan to be split into two spending packages and include injecting money to a fund guaranteeing loans to SMEs, companies affected by virus and support for the retrenched.	ECB delivered a calibrated and targeted package of stimulus, including QE purchases of EUR120bn through to end-2020. On top of its existing commitment to buy EUR20bn per month, more favourable terms on TLTRO, additional long-term loans for banks to provide immediate liquidity and easing of capital buffer rules for banks to keep lending going while stress test on banks have been postponed to 2021 (from 2020).
Germany	(13 Mar 20) Germany pledged to spend "whatever necessary" to protect its economy. Authorized state bank (run by government), KfW, to lend out as much as EUR550 (\$610bn) to companies	
Switzerland	(13 Mar 20) Switzerland prepared to release up to CHF 10bn to help companies and employees. CHF8bn of the amount to cover costs related to partial unemployment (including helping sporting organisations to cover lost income from cancelled and postponed events with up to CHF50mn)	SNB meets on 19 Mar.
Canada	<p>Budget to be released on 30 Mar. PM Trudeau promised a \$1bn package to combat COVID. Finance Minister announced a new facility to support funding markets for SMEs "at a time when they may have increased funding needs and credit conditions are tightening".</p> <p>Jeremy Rudin, Banking Regulator Chief, lowered domestic stability buffer by 1.25ppt of risk-weighted assets, effective immediately.</p>	<p>BoC lowered policy rate by 50bps to 0.75% on 13th Mar on top of the 50bps cut on 4th Mar.</p> <p>BoC will start a \$500 switch operation in the 30y sector on 16 Mar (Mon). New bi-weekly term repo operations (6M (C\$4bn) and 12M(\$C3bn)) will start on Mar 17. The central bank will continue to carry out operations for regular 1M and 3M term repo.</p>
UK	(11 Mar 20) Finance Minister Rishi Sunak announced fiscal package of GBP30bn (\$37bn) that includes a tax cut for retailers, cash grants to small businesses.	<p>(11 Mar 20) BoE lowered interest rates by 0.5ppt</p> <p>Lowered capital requirements for UK banks. Banks can now utilize a part of their reserves known as the "counter-cyclical capital buffer" to increase their resistance to global financial shocks.</p>
Australia	(12 Mar 20) Australia announced A\$17.6bn (\$11.4bn) stimulus package that includes payments to small businesses for hiring and \$750 cash payout for welfare recipients along with support for tourism business.	<p>(3 Mar 2020) RBA cut cash target rate by 25bps.</p> <p>(16 Mar 2020) RBA to announce more policy measures on 19 Mar, stands by to purchase government bonds. Likely to cut by 25bps.</p>
New Zealand	PM Ardern promised a "more significant" stimulus package to fight coronavirus vs. previous \$12bn committed to infrastructure.	(16 Mar 2020) RBNZ cuts OCR by 75bps in an emergency announcement, large scale asset purchase program if more support needed

	<u>Fiscal Measures</u>	<u>Monetary Measures</u>
Japan	<p>(Feb 20) JPY500bn in low-cost loans to affected companies.</p> <p>(10 Mar 20) Japan's Prime Minister Shinzo Abe on Tuesday (March 10) approved a second 430 billion yen (US\$4.1bil) package that includes support for SMEs hit.</p> <p>Fiscal measures: JPY48.6bn to stop further spread of virus and support medical services, JPY246.3bn to support fallout from school closures, JPY119.2bn to support shrinking business activities and maintain employments, JPY16.8bn emergency measures in case of sudden shift in situation.</p> <p>Financing measures: JPY606bn safety net lending; JPY543bn special loans; JPY204bn as financing support for large and medium firms; JPY 250bn to finance support for supply chains.</p>	<p>(16 Mar 20) BoJ said it would buy more assets including ETFs and corporate bonds and offer a new zero-interest rate loan program for corporates. The central bank will be able to buy at an annual pace of JPY12trn, double the annual target of JPY6trn.</p>
China	<p>Local governments are allowed to frontload another CNY848mn of bond sales (that was originally part of the quota for the new year ahead set in Mar) for utilization before Mar. CNY290bn worth of this quota is meant for special bonds (for infrastructure construction) (4th Feb)</p> <p>Corporate taxes will reduce and government expenses to be cut. (16th Feb).</p> <p>State Council temporarily waive social insurance premiums (state pension, unemployment and accident insurance) for SMEs waived (Feb to Jun), halved for large firms (until Apr). Those in Hubei will be exempted regardless of size. (19th Feb)</p>	<p>In Feb, PBoC lowered MLF, 7D, 14D reverse repo by 10bps by aggressive 10bps. 1Y LPR was guided down by 10bps to 4.05% and 5Y LPR was 5bps lower at 4.75% for Feb.</p> <p>(13 Mar 20) PBoC announces targeted RRR cuts for certain banks. The central bank cut by 0.5 to 1ppt under inclusive finance scheme, an additional 1ppt for joint stock banks. This RRR aims to unleash CNY550bn to banking system and will take effect 16 Mar 2020.</p>
South Korea	<p>(3 Mar 20) South Korea announced a \$9.8bn stimulus package including SME subsidies to help companies pay workers, childcare subsidies and jobs retraining for people who lost jobs</p>	<p>(16 Mar 20) BoK Cut key interest rates by 50bps to 0.75%.</p>
Singapore	<p>(18 Feb 20) Singapore will spend S\$4bn on a slew of new measures and enhancements to existing schemes to stabilise its economy.</p> <p>(11 Mar 20) DPM Heng said a second stimulus package is being crafted. PM Lee said its meant to help companies with costs and cash-flow, for workers to keep their jobs and retrain during their downtime.</p>	<p>(4 Feb 2020) MAS flags room for SGDNEER to weaken within the policy band to accommodate any economic hit.</p>
Malaysia	<p>(27 Feb 20) Malaysia to introduce MYR20bn stimulus to ease cash flow of affected businesses, to assist affected individuals, to stimulate demand for travel and tourism.</p>	<p>(3 Mar 20) BNM Cut OPR to 2.50% to provide a more accommodative monetary environment to support the projected improvement in Malaysia's economic growth amid COVID-19 outbreak.</p>

	<u>Fiscal Measures</u>	<u>Monetary Measures</u>
Thailand	<p>(10 Mar 20) Thailand's government approved a package of stimulus measures that it said will inject about 400 billion baht (\$12.7 billion) into the economy to counter the economic blow from the coronavirus outbreak.</p> <p>Steps such as (60bn THB) tax cuts and 180 billion baht of concessionary loans for some businesses will combine to deliver the boost, Lavaron Sangsnit, the director-general of the Fiscal Policy Office, said in a briefing Tuesday.</p>	BoT meets on 25 Mar.
Indonesia	<p>(25 Feb 20) \$718mn stimulus to counter virus impact that includes taxes of hotels and restaurants in 10 tourist destinations for 3 months, subsidy for housing loan interest for low-income people.</p> <p>(13 Mar 20) Indonesia introduced a second \$1.55bn of emergency fiscal stimulus plan including waiver of import tax for 6 months for some goods, corporate tax rate to reduce by 30% and income tax waived for manufacturing workers wef 1Apr.</p>	BI has been actively supporting the rupiah in the FX market. BI announced a 400bps cut in its RRR to 4% with effect from 16 Mar. Cut RRR by 50bps for banks' financing trade for a period of 9 months from 1 Apr. BI meets on 19 Mar.
Philippines	(Week of 16 Mar 20) A house bill filed last week will be seeking to set aside PHP108bn for an emergency stimulus package, with slightly less than half likely going to the tourism sector	(16 Mar 20) BSP considers to cut 50bps on 19 th Mar.

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Published by:



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