UOB HOUSE VIEW

3Q2018

GLOBAL MACRO

Our positive macro-economic outlook remains intact, and we still see global growth of just below 4% this year. While prices are generally higher, inflation is not running away in 2018. Geopolitics continues to create a lot of uncertainty and the warnings are getting louder after G7 Leaders' summit in Canada & another round of US-China tit-for-tat in June. US leads the way in normalizing monetary policy but geopolitics & rising trade tensions could still spoil the party.

ASSET ALLOCATION

There are many issues weighing on investments so far in 2018, but we argue that in the end, healthy global growth and healthy earnings growth is going to be supportive of growth assets like equities. Meanwhile, a period of normalizing interest rates is inherently a headwind for fixed income markets For 3Q 2018, we continue to overweight equities, underweight fixed income, stay neutral on commodities, and underweight cash.

EQUITIES

Multiple geopolitical and macroeconomic issues have come to dominate the headlines in recent months. With each issue pulling in a different direction, equities have often been caught in the cross-currents. We are positive on Japanese equities, neutral on US and European equities for now, but the view on emerging market equities is more differentiated.

FIXED INCOME

We continue to expect the US Fed to hike rates in 2H 2018 and the rate hike path will likely remain gradual into 2019 and 2020. Fixed income continues to face "headwinds" to returns due to rising rates, but yields are now higher and given how much bond yields have already moved we think fixed income has a good chance of providing positive returns from these levels.

COMMODITIES

Commodities Strategy: Supply disruptions drive clear price trends. At the half year mark of 2018, clear price trends have emerged for key commodities complexes. Gold and precious metals are mostly weaker. While supply disruptions triggered wild price swings in palladium and aluminum and have spilled over to copper. Saudi Arabia's hint of dialing back on supply cuts has capped Brent crude oil at USD 80 / bbl.

FX & INTEREST RATES

Further rise in USD yield off the back of more Federal Reserve rate hikes, a moderation of strong Asian export growth momentum and on-going tense US-China trade relations are all key drivers that will drive USD stronger and Asian currencies weaker in 2H 2018. Despite the thrills & spills in 1H there is little reason to suspect that monetary policy tightening might be derailed at least in rest of 2018. The second half of 2018 will see monetary conditions become incrementally less accommodative but the path to higher yields will not be a walkover.

UOB

GLOBAL MACRO

Dribbling Past Geopolitics

"Things are neither clear nor clean in the world of football right now and many people recognise this reality." - Diego Maradona

While this is probably not a very famous quote, as we enter into the World Cup 2018 and we replace "football" with geopolitics, this quote resonates quite well with the global environment we are in today.

Our positive macro-economic outlook remains intact, and we still see global growth of just below 4% this year. And while prices are generally higher, inflation is not running away in 2018. And even though there had been quite a number of risk events during the first half of 2018, it probably also did not hurt as much as we initially feared.

That said, geopolitics continues to create a lot of uncertainty in the outlook and the warnings are getting louder after the G7 Leaders' summit in Canada even though the economic fundamentals remain healthy. The US Federal Reserve continues to lead the way in normalizing monetary policy but geopolitics & rising trade tensions could still spoil the party.

In our previous quarterly report (2Q 2018 dated 23 Mar 2018), we highlighted "*on balance, we believe we have more to be hopeful for than to be fearful, but admittedly the number/degree of "fears" is increasing*." Indeed, there remains various risk events over the next 6-12 months with many of them emanating from the geopolitical space:

a. **Trade policy developments: US-China trade tensions and US trade tensions with its major allies and rest of the world.** This is the biggest risk on the table and our base case is still a gradual de-escalation through negotiations (i.e. not trade war). Importantly, the negotiations may be long drawn and we note that geopolitical events along the way may provide speed bumps or unexpected developments to take place.

b. **Higher US interest rates.** US rates are expected to head higher but this is in line with the backdrop of an improving US economy and US employment. Our base case has been revised to a total of four hikes in 2018 (from three previously), but even if the Fed hikes four times this year – which represents the fastest annual pace of normalisation since the Fed started hiking rates in 2015 – we do not see it as excessive US monetary tightening.

c. **Emerging market risks**. There are some troubled spots in EM spaces, but in EM Asia, the risks remain well contained amidst better macro-economic fundamentals now versus during 1997 and pro-active actions taken to address the issues. That said, risk of capital outflows and weaker currencies for the Asian region remain while tighter liquidity in Asia may also lead to more bond defaults and increased defaults in SME sector.

d. **China's slowdown**. We expect an orderly dial down of growth, likely at 6.7% in 2018, from 6.9% in 2017. But this assumes there will not be an all-out trade war and we expect China and the US to move towards an agreement eventually.

e. **Crude oil prices.** Crude oil looks to have topped US$80/bbl and expected to be around US$70-80/bbl. The key oil-related event to watch is the 174th (ordinary) OPEC meeting on 22 June)

f. **Eurozone geopolitical developments.** Recent geopolitical developments in Italy and Spain were certainly a surprise but our base case is still for the Eurozone to remain intact.

g. **Brexit negotiations**. There is still no clarity on the terms between UK and EU despite many quarters of negotiations. Not a problem today but the Brexit deadline of March 2019 is getting closer.

And of course, there are other developments that will generate headlines in 3Q such as the on-going US Special Counsel Robert Mueller's investigation into Russian meddling with the 2016 US presidential elections, the Mexican presidential elections on 1 July (which may have implications to the NAFTA negotiations), and US domestic political developments leading up to the November mid-term elections.

Fortunately, once every 4 years, a global sporting event takes over the attention of the World: the 2018 FIFA World Cup tournament (14 June to 15 July 2018) may be a welcome distraction from geopolitics for the next few weeks. But there may not be much to cheer for the US this time as it failing to qualify for the first time since 1986, so we probably can still expect politically-charged tweets coming from the White House. We have a consensus call that geopolitics will not derail growth or monetary policy and a non-consensus call for World Cup host country Russia to lift the FIFA World Cup Trophy. In the meantime, stay calm and watch football.

ASSET ALLOCATION

Healthy market fundamentals

There are many issues weighing on investments so far in 2018, but we argue that in the end, healthy global growth and healthy earnings growth are going to be supportive of growth assets like equities. We continue to overweight equities and underweight fixed income markets. Earlier in the year, the bullish case was more of a consensus view of markets. After the equity market correction in February, the most common view was that it was a "healthy" correction. But by June, the continued "noise" of market risks and the continued lackluster market performance have appeared to dampen the confidence of global investors in recent months.

The bullish case for equities is fairly straightforward. We argue that in the last 40 years, there were really only 2 years when global GDP growth was above trend and earnings were growing at a double digit rate and equities did not have above average returns. Those years were 1994 and 1987, and we argue that while both of those periods coincided with late cycle uncertainties, we find the differences between then and now far outweigh the similarities. Unless, something unusual happens in 2018, we would expect the positive fundamentals to be supportive of equities through the end of the year.

Overall, our equity scorecards that monitor typical drivers of equity performance continue to look healthy. Leading indicators, absolute GDP growth, earnings growth, fund flows and fiscal policy all remain positive supporters of the scorecard. Valuations had previously been a negative but we have shifted valuations to neutral. The US price earnings multiple had been high earlier in the year but after earnings growth and a sideways market, valuations have returned back close to average levels. We currently have the US market at 16.4X 1 year forward earnings vs a long term average of 15.5X. Other markets like Asia are back in line with long term average valuations. The obvious negative in the scorecard comes from monetary policy which is tightening in the US and thus tightening monetary conditions globally. This headwind is largely offset by the positive fiscal policy boost in the US which is unusually expansionary at a late cycle stage. Thus, the backdrop for equities is quite strong and it would take the rise of some new risk to undercut the outlook (see below for our comments on the greatest threats to markets).

A period of normalizing interest rates is inherently a headwind for fixed income markets. US Treasury yields have climbed form 2.4% at the start of the year to 2.95% in June. The start of a cycle of rising yields triggers investor anxiety over what levels could they rise to. But we argue the path of future rates has a pretty clear structure. While it seems like there is a lot of debate between 3 hikes or 4 hikes in 2018, the reality is that there is broad consensus that the peak fed funds rate is somewhere between 3% and 3.5%. If we know the Fed Funds path, then we can calculate the 2 year path as effectively as the makeup of the 8 quarters of Fed Funds outlook. If we can calculate the 2 year then we have a pretty clear idea for the 5 year and even the 10 year. The range of possibilities is not really as uncertain and as wide as market may fear at the initial stages of the rate hike process. Ultimately if the Fed Funds is peaking in the 3% to 3.5% range in the next couple of years then we should expect the 10 year to flatten and even invert at some point in the next couple of years, and thus the 10 year expected range does not have to be so unpredictable as many fear. It also means that the 10 year yield has likely already made its largest moves and given the better carry in credit, we would expect fixed income funds to be positive through the rest of the year after being down in the first half of the year.

While we have constructive views on equities and fixed income, it is fair to say there are a significant number of risk issues that could undermine our expectations. The most material issue so far in the first half of 2018 has been the concerns about potential trade wars. The US policies have been erratic and economically harmful. Global markets fear that the trade rhetoric could escalate. But in the end the economic impact of the trade tariffs announced are small and ultimately we continue to accept that most of the trade rhetoric is geared to negotiations and not with a goal of outright trade reductions. European politics has become a key risk in the wake of Italy's new government although the new Economic minister said it has no plans to leave the Eurozone and will focus on reducing debt level. That said, if the anti-Euro sentiment is rekindled, then we would expect markets to turn more volatile. Rising inflation remains as a key risk as well. With unemployment rates falling, wages could start to pick up and drive up inflation more than expected. If so, the Fed Funds rate hike path as outlined above could be at risk.

For 3Q 2018, we continue to overweight equities, underweight fixed income, neutral on commodities, and underweight cash.

Asset Class	Policy	UOB House View Weight (%)	Benchmark Weight (%)
Equities	Overweight	60.0	55.0
Bonds	Underweight	32.0	38.0
Commodities	Neutral	5.0	5.0
Cash	Underweight	1.0	2.0

EQUITIES

Multiple geopolitical and macroeconomic issues have come to dominate the headlines in recent months. With each issue pulling in a different direction, equities have often been caught in the cross-currents. Sharp intra-day turnarounds have become more common, and many global equity indices have traded sideways with higher volatility. Investors who bemoaned the absence of volatility in 2017 may have gotten more than they wished for this year!

We maintain a neutral stance on US equities. In our view, tariffs are not likely to derail the economy's growth trajectory for now, as trade does not constitute a large share of the US economy. Overall, the US economy remains on a positive footing, and may even grow faster than expected owing to the tax cuts passed in late 2017. While US equities can be expected to deliver positive returns against this backdrop, we do not expect these returns to be large as both corporate profit margins and valuations are already high relative to history.

We downgrade our view on European equities from positive to neutral. Activity indicators suggest deceleration in the pace of European growth. While we continue to expect positive growth, it is likely to proceed at a slower pace, which will be reflected in a similarly slower pace of earnings growth. Furthermore, we expect political headlines to produce bouts of volatility in the coming months, particularly in Italy. As such, while European equities should deliver positive returns, the risk/reward balance has shifted in favour of a neutral allocation.

We maintain a positive view on Japanese equities. Economic growth is likely to remain supported by external demand and Olympics-related capex. Going forward, a stronger USD and the market perception that the Bank of Japan will maintain ultra-accommodative monetary policy for an extended period will be a tailwind for Japanese equities. In addition, there are hints that Japan may be making headway in defeating inflation, as wages are on the rise. Should investors become convinced that Japan is on track to escape nearly three decades of deflation/disinflation, Japanese equities can be expected to enjoy a substantial re-rating.

The view on emerging market equities is more differentiated. Looking ahead, emerging markets are likely to face a cocktail of positive but less synchronized global growth, rising US interest rates, a stronger USD, stable/higher oil prices and wider credit spreads. We therefore favour markets that are likely to respond positively to this combination of global drivers or that have their own positive domestic drivers. We maintain our positive views on equities in China (earnings recovery) and Korea (pick-up in global growth). We take a neutral view of India, Brazil and Mexico, as the balance of global and domestic drivers for these markets points to a more subdued performance.

COMMODITIES

Overview - Commodities Strategy: Supply disruptions drive clear price trends

At the half year mark of 2018, clear price trends have emerged for key commodities complexes. Gold and precious metals are mostly weaker. Meanwhile, supply disruptions triggered wild price swings in palladium and aluminum and have spilled over to copper. Saudi Arabia's hint of dialing back on supply cuts has capped Brent crude oil at USD 80 / bbl.

Gold: Rebound in USD off the back of rising rates trigger further weakness in gold price

In the precious metals space, a resurgent USD coupled with ever rising US rates both in the front and back end triggered further long liquidation across gold, silver and platinum. As such, gold was sold-off back below USD 1,300 / oz, silver was depressed at USD 16.50 / oz, while platinum encountered heavy selling from USD 950 to 900 / oz. The exception was palladium which bucked the trend as it was well supported just under USD 1,000 / oz. This was mainly due to concerns over supply disruption from US sanctions on Russia.

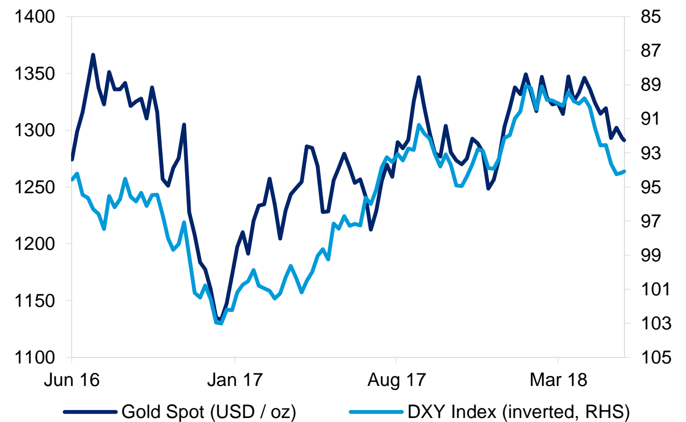
Copper: Benefiting from increasing supply disruption in the base metals complex

In the base metals space, supply disruption played an even more critical role in keeping prices well supported. US sanctions on Russia has removed a key global supply for aluminum and this is further exacerbated by new tariffs by US against their import of aluminum and related products. As such, aluminum staged a strong rally from USD 2,000 to 2,600 / MT across April. Copper was lifted above USD 7,000 / MT on spillover investor proxy hedge for increasingly volatile aluminum prices as well as renewed concerns over supply disruption from Chile's massive Escondida copper mine.

Brent Crude: Capped under USD 80 / bbl as Saudi Arabia hints of easing supply cuts

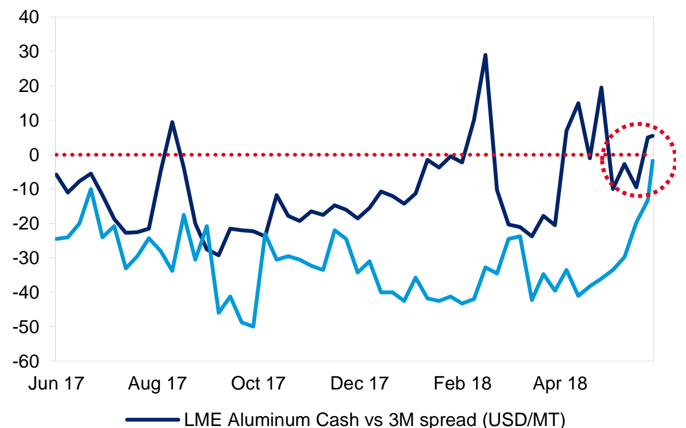
In the energy space, crude oil's strong rally since last year was capped by renewed hints from Saudi Arabia and Russia to dial back some of their very successful supply cuts. This has pushed Brent crude oil price back below USD 80 / bbl. As for WTI crude oil, ever rising US production has translated into a wider discount to Brent crude oil, of as much as USD 10 / bbl.

Gold Price Continues To Exhibit Strong Inverse Correlation To The DXY



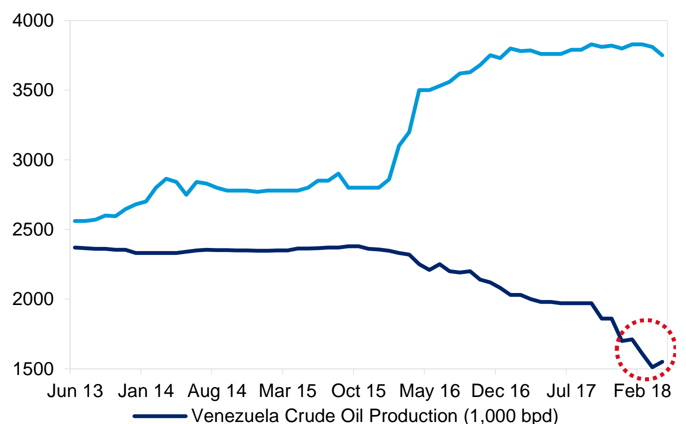
Source: Bloomberg, UOB Global Economics & Markets Research

Both LME Copper And Aluminum Witnessed Rising Cash vs 3M Spread



Source: Bloomberg, UOB Global Economics & Markets Research

Venezuela's Crude Oil Production Has Collapsed; While US Sanctions Threaten Iran's Production Recovery



Source: Bloomberg, UOB Global Economics & Markets Research

FIXED INCOME

Challenging Times In 2018

Our message in 2018 has been to warn that fixed income markets will face headwinds in from rising rates, but we have also advocated that investors don't need to panic. We have expected fixed income returns to underperform equity returns in 2018 but that we expect fixed income returns to be positive for the year. As of May, most fixed income markets have been modestly negative. While US rate hikes have continued at a slow pace, benchmark yields of US Government Bonds rose rapidly at the beginning of the year. The average yield or "carry" of most bond funds are higher now and it is now common to see average yields of 4% or more. At this level of "carry" we continue to expect that fixed income should deliver positive returns despite the fact that rate hikes will persist.

In the first 5 months of the year, government bond yields shifted sharply higher with the US 10-year yield rising from 2.4% at the start of the year to 2.86% by the end of May. Singapore's 10-year yields have largely followed, rising from 2% to 2.57% over the same period. Rising benchmark yields have put pressure on bond funds. The global benchmark of the Barclays Global Aggregate Index total return, year-to-date as of the end of May was -1.0% measured in USD. The Asian benchmark of the JPM Asia Credit Core Index total return year-to-date as of the end of May was -2.7% in USD terms.

While rising rates in 2018 has been widely expected by global investors, fixed income markets have also had to adjust to widening credit spreads. Generally, broad benchmarks such as the Barclays Global Corporate Aggregate or the JPM Asia Credit Index have seen average investment grade corporate spreads widen by 20bp. It is common for healthy global growth to lead to monetary tightening policies such as rate hikes among the global central banks. But usually healthy growth is positive for credit conditions, and thus it is modestly surprising to see pressures on credit as well. Corporate profitability around the world remains healthy, and thus wider spreads appear to be the result of fixed income volatility affecting sentiment, valuations concerns and fund flows. While some investors note that credit spreads had gotten "expensive", and were tighter than earlier in the cycle, we would also note that in the final years of previous cycles credit spreads were even tighter than they have been in this cycle. Overall, we would expect fixed income volatility to translate into some degree of wider spreads but that corporate health is strong enough that we don't think further spread widening is justified. Thus, **we continue to overweight credits over government bonds**.

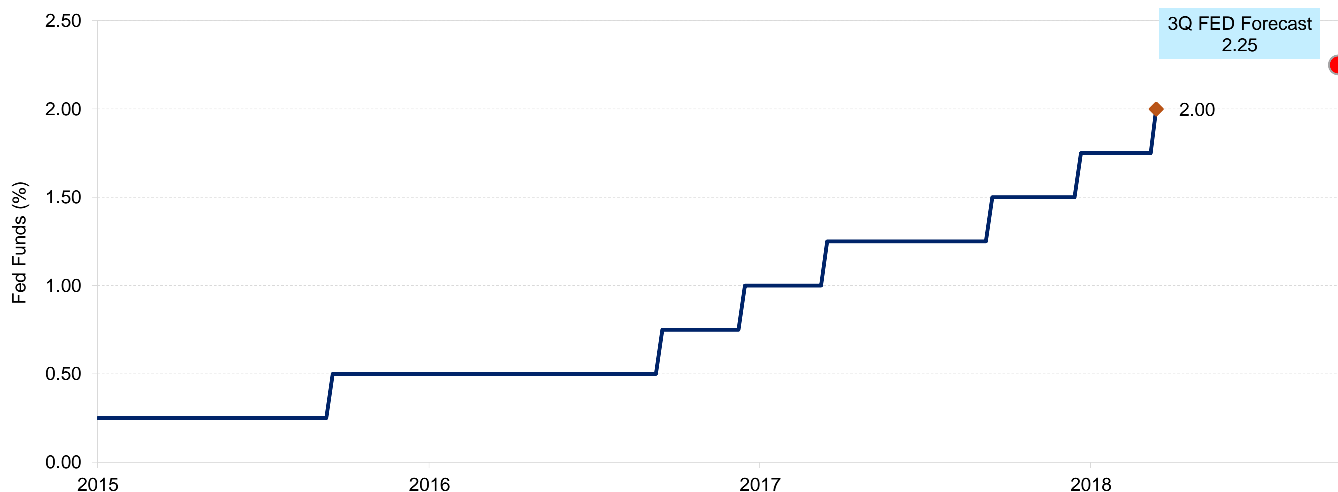
Strong US growth and broad based global growth are usually very supportive of emerging market growth. But rising US rates have contributed to a firmer USD trend that has become a headwind for some emerging markets with weaker balance of payments such as Argentina and Turkey. **We would be neutral emerging markets for the coming quarter due to USD risks, but within emerging markets we continue to overweight Asian credits**.

While 2018 has been a challenging year for fixed income investors so far, we continue to advocate patience. Fixed income markets remain less volatile than equity markets and thus continue to hold an important role for many lower risk investors. Even in a terrible year like 2018 in the face of rising rates, the Global Bond indices are only down -1% -- equities had suffered far more in their bad years. Plus fixed income has the benefit that higher yields imply better returns in the coming years. At some point, this global expansion that has continued for 9 years will eventually turn down and at that stage fixed income will be a preferred asset class again.

FX & INTEREST RATES

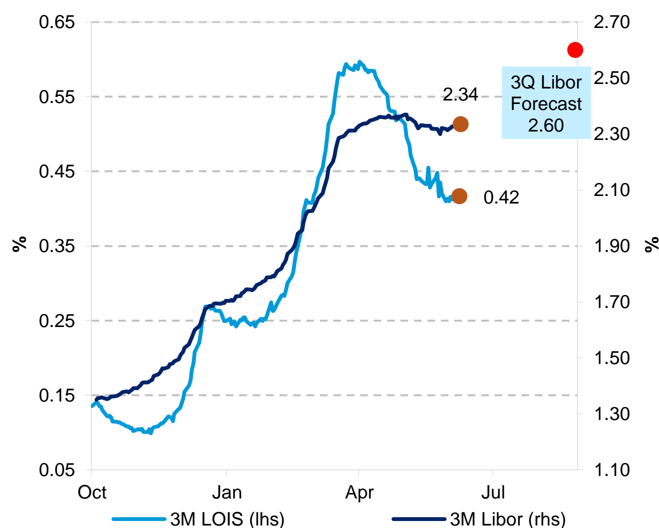
UNITED STATES

FED Funds Rate



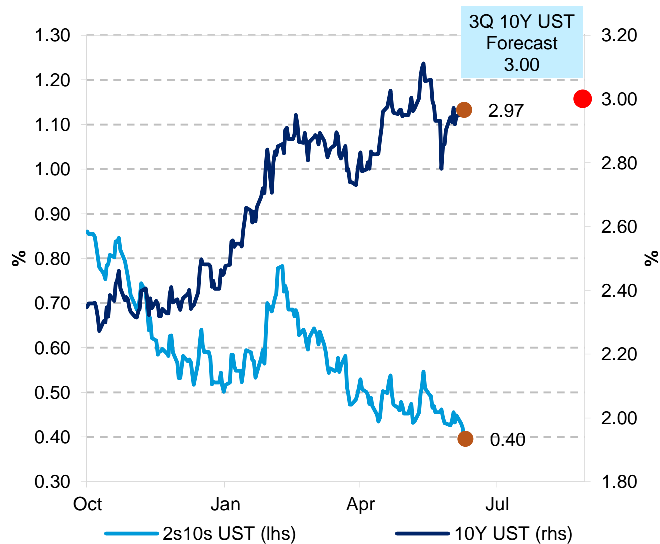
The moderately hawkish June FOMC provided the affirmation for a steeper Fed rate trajectory in 2018 and we now expect two more hikes in Sep and Dec FOMC (after June's rate hike to 1.75%-2.00%), bringing the FFTR range to 2.25%-2.50% by end-2018 (from previous forecast of 2.0%-2.25%). That said, even if the Fed hikes four times this year – which represents the fastest annual pace of normalisation since the Fed started hiking rates in 2015 – we do not see it as excessive US monetary tightening. We maintain our 2019 rate hike expectation at three 25bps hikes which now implies that we expect the Fed to exceed their long run FFTR at 3.0% by mid-2019. The Fed's balance sheet reduction (BSR) program is expected to continue as scheduled and since trimming the balance sheet is somewhat a 'substitute' for rate hikes, so we believe the continuation of BSR is a key factor the FOMC will take into consideration and not add more rate hikes (beyond what is implied in the dot-plot chart) unless we get a sharp inflation surprise.

3M US Libors



- We expect to see 3M Libor at around 2.60% at the end of 3Q2018.
- Since recording a peak in April, LOIS spread has narrowed due to OIS playing catchup ahead of the June FOMC rate hike.
- LOIS is expected to remain sticky in 3Q to reflect tighter funding conditions as Balance Sheet Reduction (BSR) continues to build towards USD 50bio per month in October.

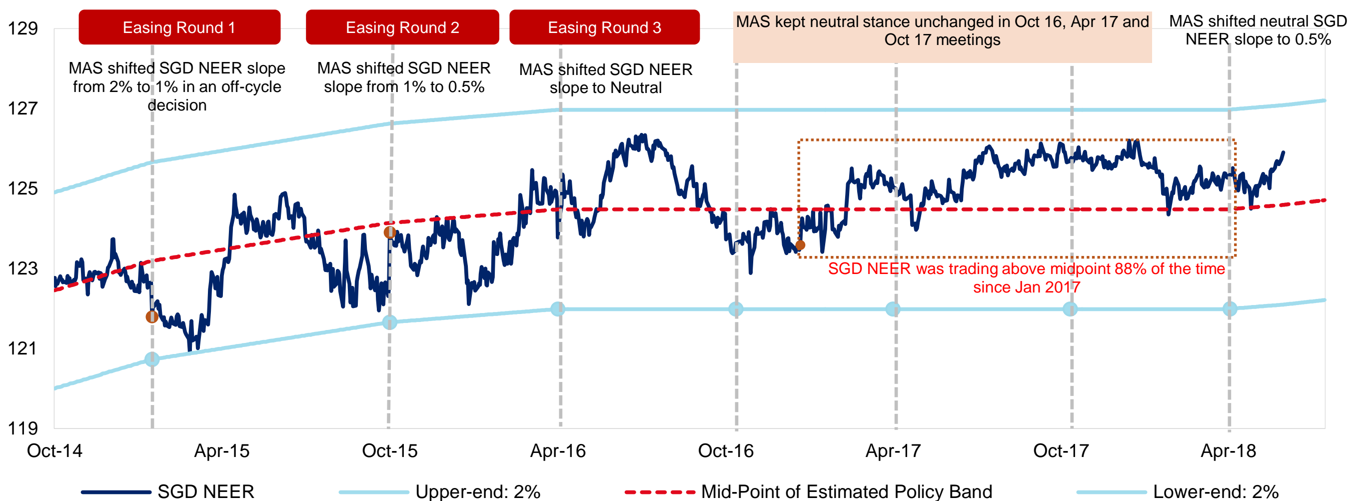
10Y US Treasuries



- We expect to see 10Y UST at 3.00% by the end of 3Q2018.
- 2s10s UST curvature will continue in a downward trend and could encounter sharper repricing lower now that every FOMC is a "live" event from 2019.
- 10Y UST term premium have not richen significantly despite a backdrop that includes BSR and larger budget deficits. We see upside risk to term premiums.

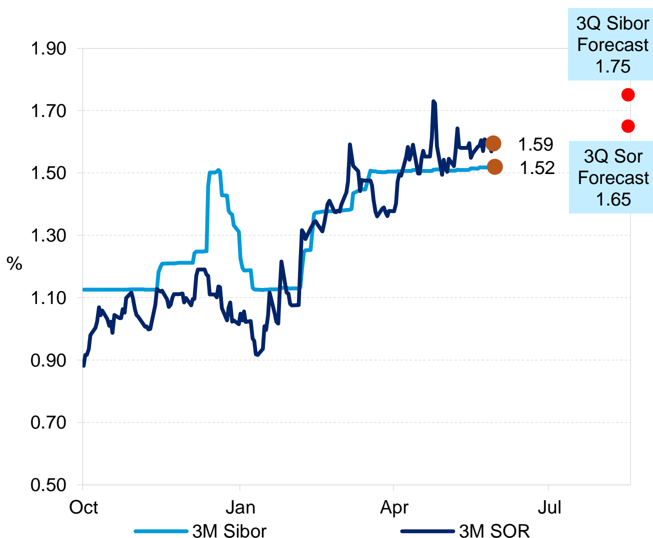
SINGAPORE

SGD NEER



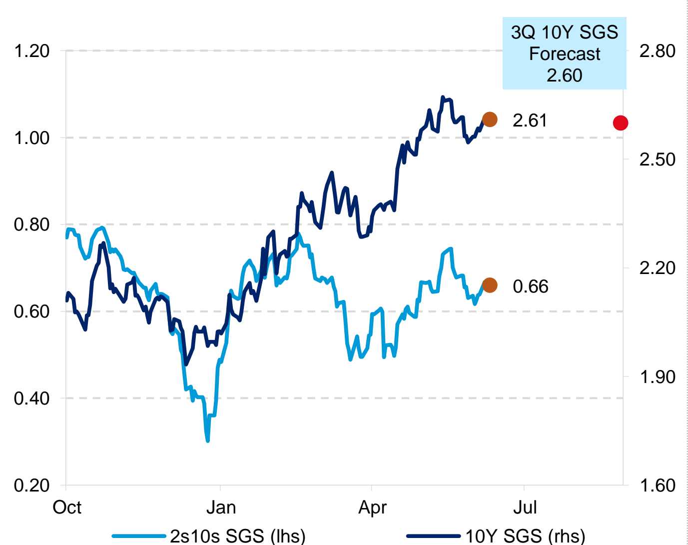
As we had expected, the Monetary Authority of Singapore (MAS) on 13 April embarked on the path of monetary policy normalisation by increasing slightly the slope of the SGD NEER policy band, deviating from the neutral slope stance over the last four policy meetings (since April 2016). We estimate this slope to be 0.5% pa. Although the economy has regained its footing, compared to the low growth period of 2015-2016, and thus justifying policy normalisation, the tone of the central bank statement was cautious. In their statement, the MAS cautioned against the possibility of the escalation of the US-China trade dispute. Moreover, the MAS said that although "global final demand is projected to stay firm in 2018, the pace of expansion could slow slightly as the cyclical upturn matures." Because of the cautious statement, we are of the view that the MAS will maintain the current slight appreciation stance (estimate: 0.5% pa) in the next October 2018 policy meeting. Concurrently, the US Federal Reserve is expected to continue its gradual hiking process. As such, we see further mild SGD weakness ahead. It is worth noting that given the mild appreciation trend of the S$NEER policy band, any SGD weakness will be less pronounced compared to the rest of the Asian currency block. Overall, we see a slow climb in USD/SGD towards 1.36. We forecast USD/SGD at 1.34 in 3Q18, 1.35 in 4Q18 and 1Q19 and 1.36 in 2Q18.

3M SOR and Sibor



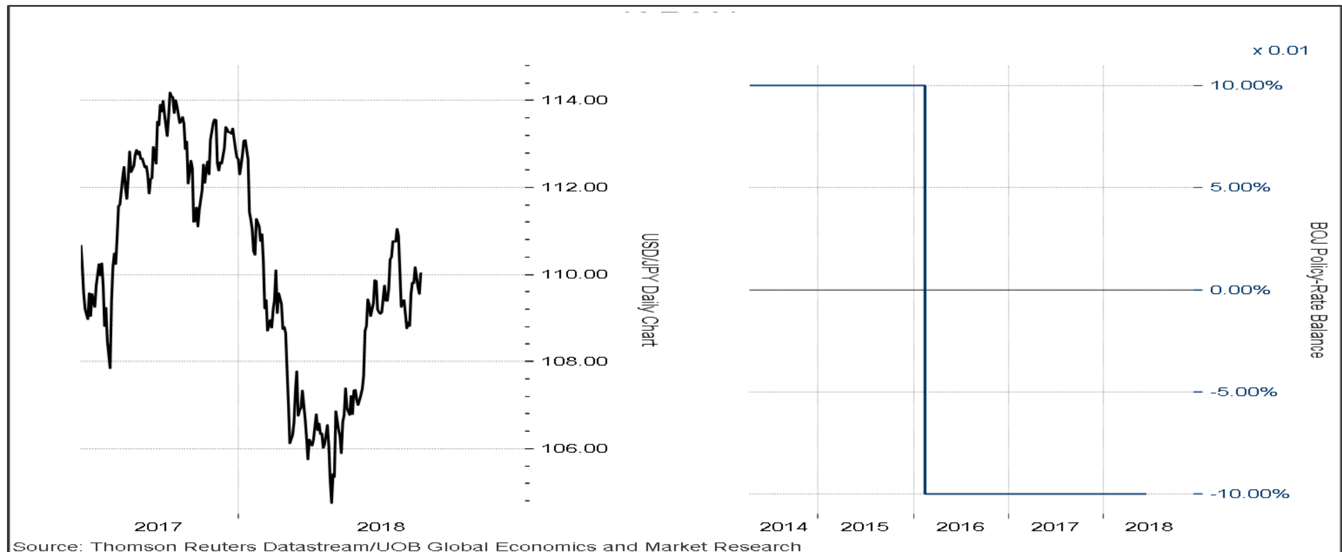
- We expect to see 3M SOR and SIBOR at 1.65% and 1.75% by the end of 3Q2018 respectively.
- Tighter 3M Sor vs. Sibor spread has been resilient in a backdrop of appreciating SGD NEER and could persist in the absence of a USD funding crunch.
- Positive EM sentiments have been tested with higher US rates and currency. Risk premium re-pricing has been modest thus far, but negative catalysts remains for 3Q.

10Y SG Bonds



- We expect to see 10Y SGS at 2.60% by the end of 3Q2018.
- After June's 20Y auction, the next meaningful duration supply will only come in September's 15Y auction. Absent supply overhang, 10Y SGS has potential to outperform against UST as well as on the 2s10s curve.
- Longer maturity SGS may also see better demand now that the High Speed Rail project has been postponed.

JAPAN

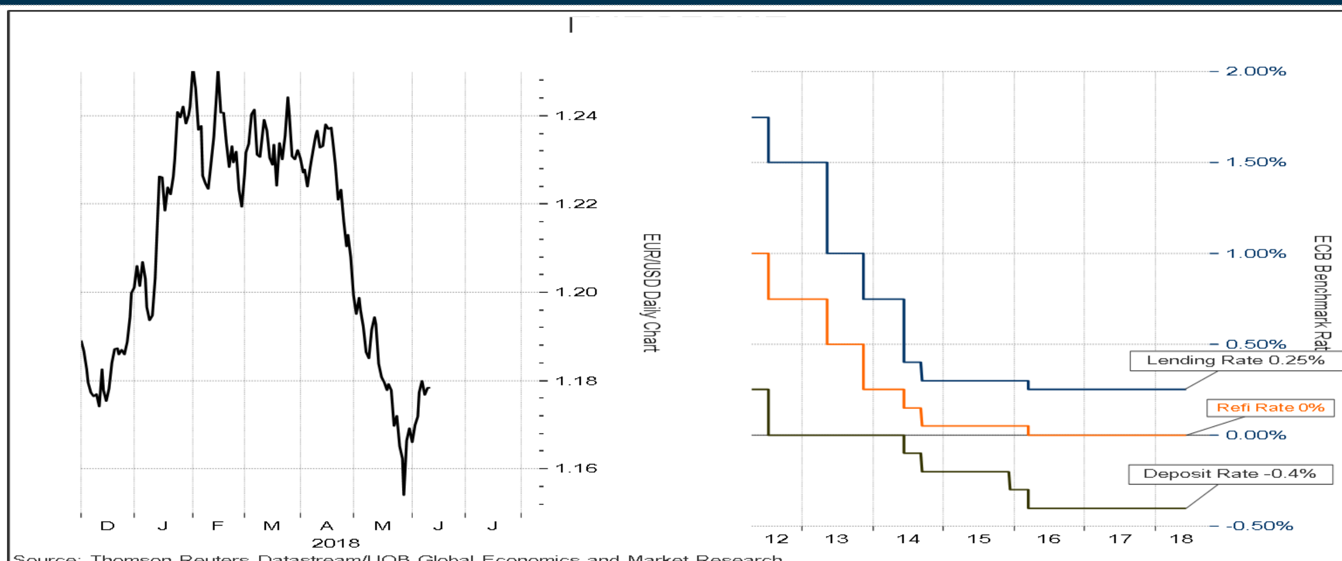


Source: Thomson Reuters Datastream/UOB Global Economics and Market Research

Despite another status quo decision on 18 Jun, the specter of "BOJ normalization" is not dispelled by the removal of the BOJ timeframe to achieve the 2% price target (in Apr) and cutting the view of CPI from around 1% to 0.5%-1.0% range (in Jun). BOJ's cause was also not helped by the fact that the projected annual pace of JGB buying remains well off the official target of JPY80trn per annum. From JPY58trn (end-2017), the pace of purchase eased further to a low of JPY44trn (as of 20 Mar). Since April, the pace has stabilized and hovered just below JPY 50trn (as of 8 Jun), still well off target.

While we maintain our long-held view that it remains premature to expect the BOJ to talk about tapering its quantitative easing program anytime soon, because Japan is still far away from its 2% inflation target, the markets may still reignite speculation about "BOJ tapering" unless the BOJ finds a way to reassert its "easy monetary policy" credentials. Meanwhile, escalating concerns over global trade war with its negative impact on Japanese exports now keep the JPY biased on a weak note. In addition, the contraction in quarterly 1Q GDP growth and softer inflation are on balance negative for the JPY as well.

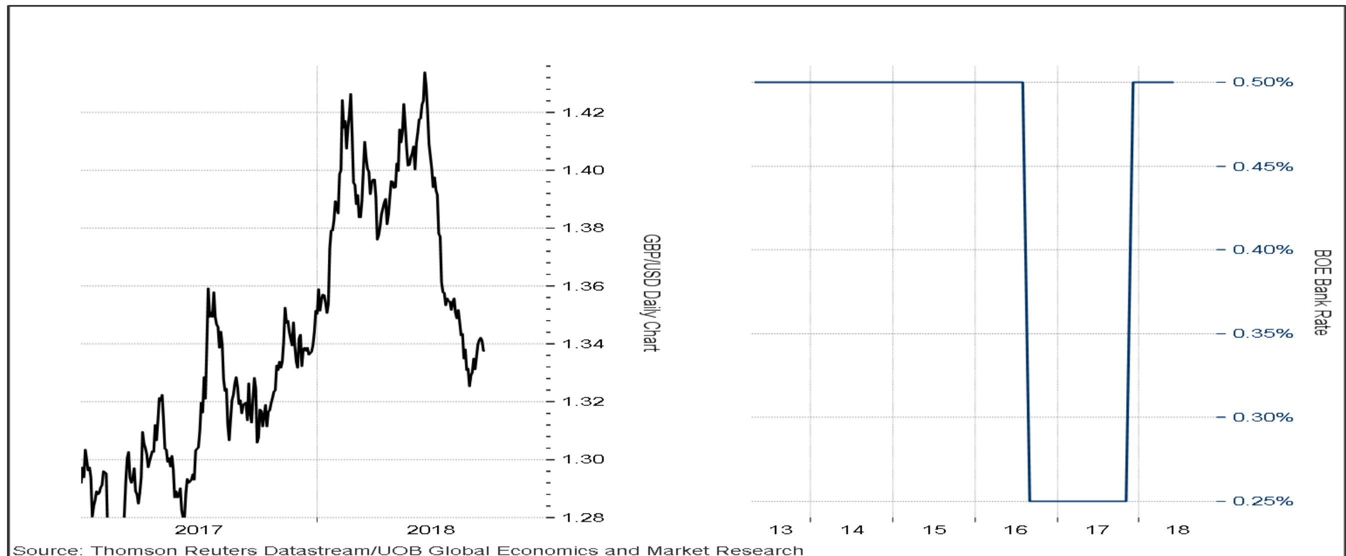
EUROZONE



Source: Thomson Reuters Datastream/UOB Global Economics and Market Research

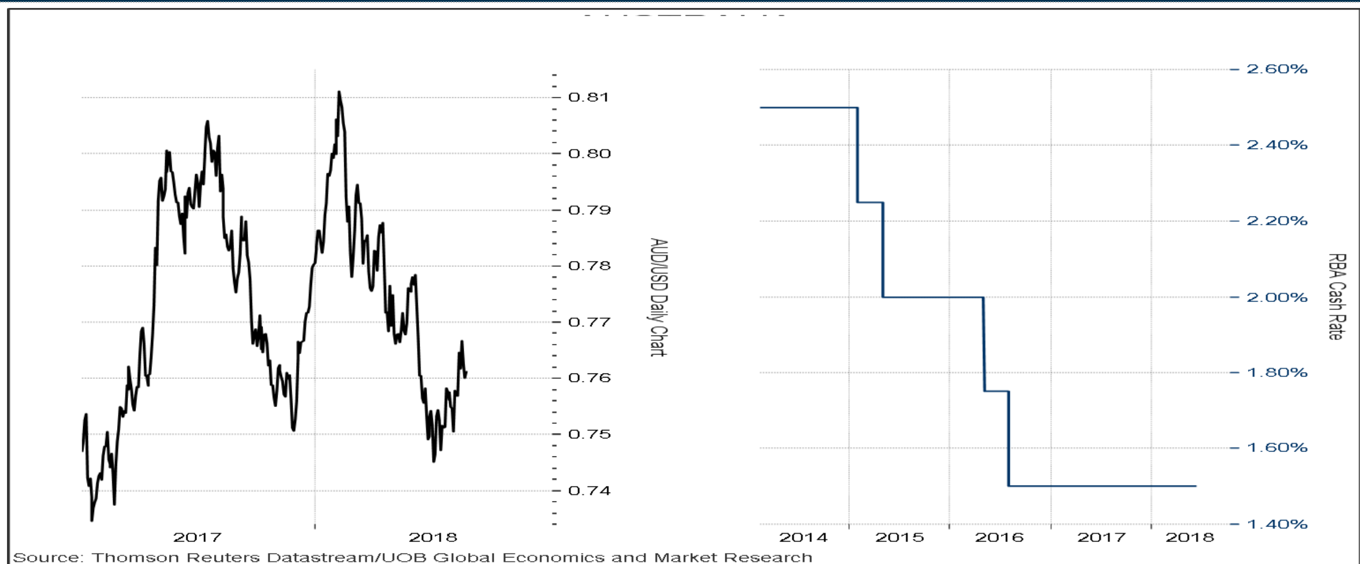
The past quarter has been decidedly volatile for the EUR. At the start of the quarter, the escalation of the political crisis in Italy triggered heavy selling in the EUR/USD and forced it back down from its high of 1.24 in April to as low as 1.1550 in late May. After several rounds of intense negotiations, Italy finally managed to form a government and the new Economy Minister Giovanni Tria reiterated that the new coalition government has no plans to leave the Eurozone and will focus on reducing debt level. In addition, while ECB acknowledged in its 17 June meeting the plan to end QE soon, they disappointed by pushing out further subsequent plans to raise rates As a result, EUR/USD stayed soft near 1.16. Overall, we maintain our positive outlook for EUR/USD as ECB is still on the path of policy normalization despite a longer timeline. We forecast EUR/USD at 1.20 in 3Q18, 1.21 in 4Q18, 1.22 in 1Q19 and 1.23 in 2Q19. Prevailing spot reference rate is 1.16.

UNITED KINGDOM



Yet another quarter has passed and there is still no clarity on Brexit terms between Britain and the EU. In the meantime, the latest about face by the BoE at its May meeting dealt a heavy blow to GBP bulls. As mentioned above, while we maintain the view of a delayed rate hike in August by the BoE, that is contingent on growth bouncing back and Brexit negotiations staying positive. Furthermore, faced with various uncertainties, GBP is unlikely to benefit much from this sole rate hike. In terms of price action, disappointment over the lack of progress in Brexit discussion, coupled with the "surprise" decision by BoE not to hike in May, have pushed GBP/USD firmly back below the 1.40 handle to current level of 1.34. We maintain our negative outlook for GBP/USD and see the pair drifting lower towards 1.30. Overall, we forecast GBP/USD at 1.33 in 3Q18, 1.32 in 4Q18, 1.31 in 1Q19 and 1.30 in 2Q19. Prevailing spot reference is 1.32.

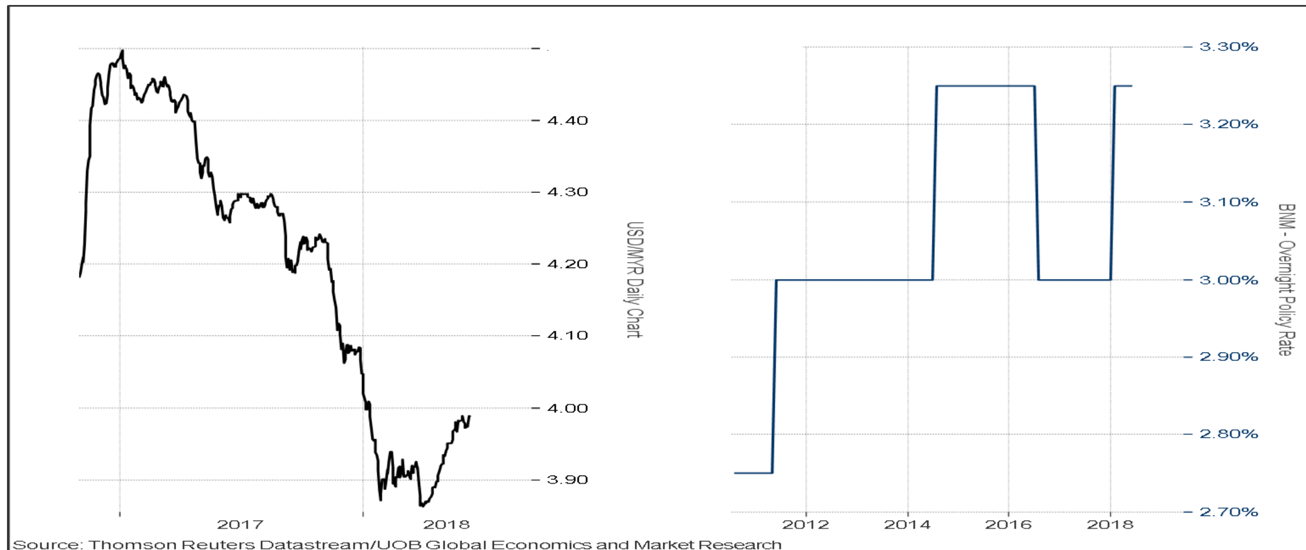
AUSTRALIA



Due to Australia's subdued wage growth as well as soft inflation trajectory, there is no pressing need for the RBA to hike. We believe that the first hike from the RBA will only occur in 1Q19.

On the other hand, prices of key commodities remain constructive. Industrial prices have traded noticeably higher across 2Q, led by LME copper which rallied back above USD 7,000 / MT to USD 7,300 / MT. After selling off in March, benchmark price for iron ore also consolidated above the key USD 60 /MT level. Consequently, Australia's terms of trade has improved moderately following a brief dip towards the end of last year. We believe the AUD will continue to draw support from positive commodities prices as it waits out the RBA. However, it is also important to acknowledge that that strong AUD upside above 0.80 is capped by on-going US Federal Reserve rate hikes. After all, since the previous FED rate hike, at 1.75%-2.00% Federal Funds Rate is now higher than the RBA's OCR at 1.50%. Until the RBA decides to hike, this policy rate differential will only widen further, to the detriment of the AUD. Overall, we see modest AUD strength ahead, to 0.77 in 3Q18, 0.78 in 4Q18, 0.79 in 1Q19 and 0.80 in 2Q19.

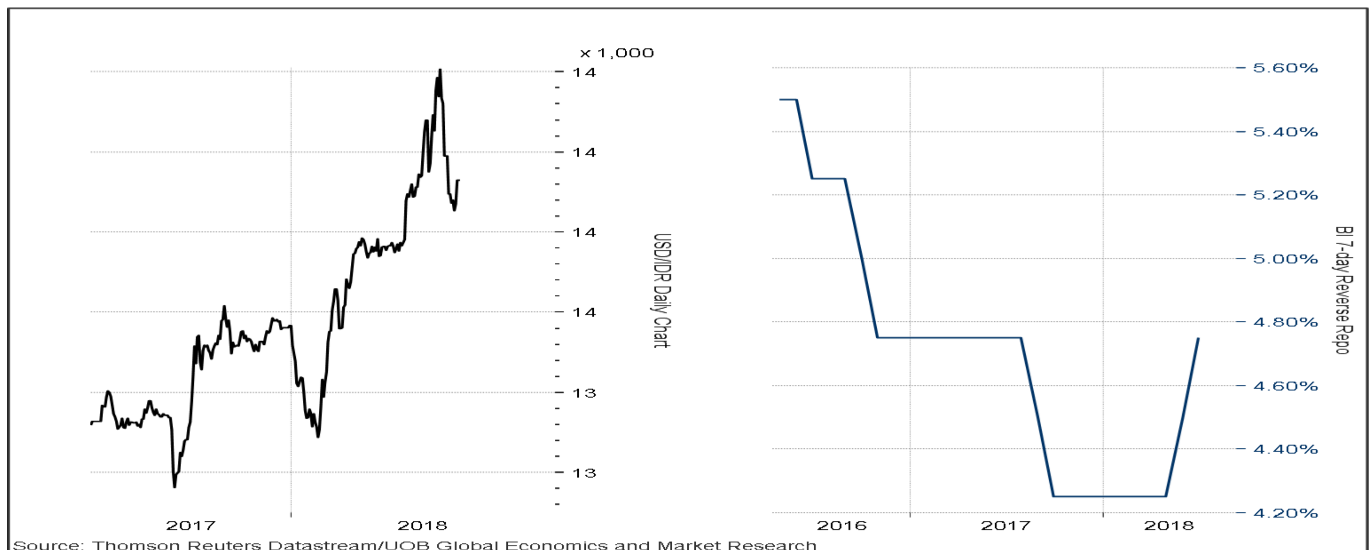
MALAYSIA



Bank Negara Malaysia (BNM) is likely to maintain a neutral monetary policy stance and keep the Overnight Policy Rate (OPR) unchanged at 3.25% for the rest of the year. A moderating inflation trend and positive real interest rates provide flexibility for monetary adjustment should economic activity slow more than expected.

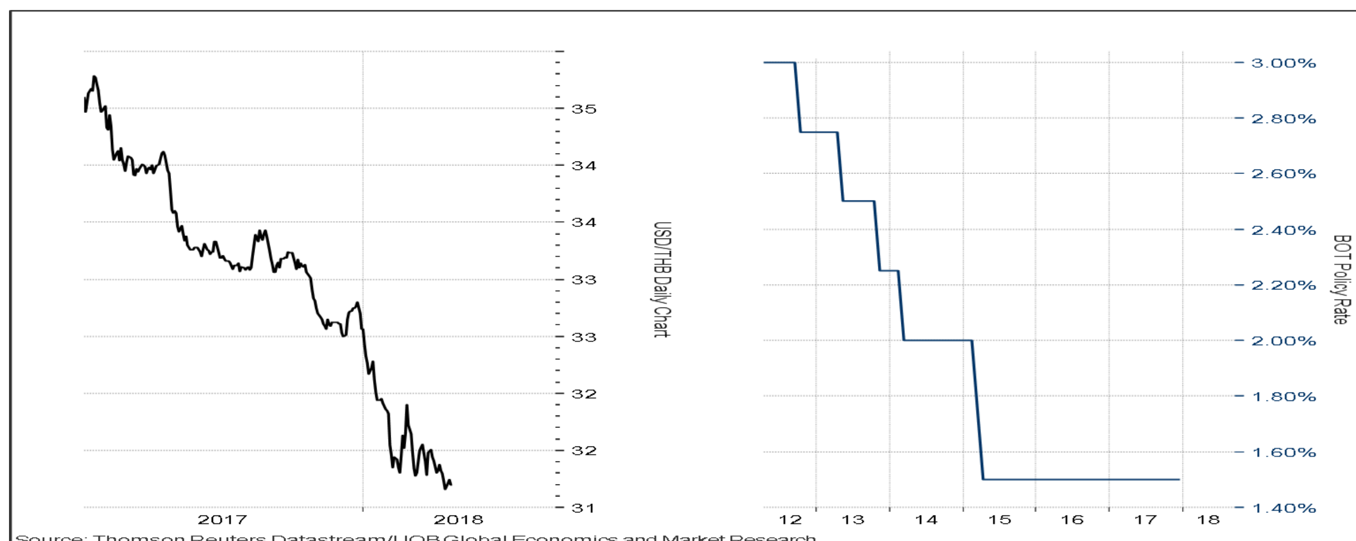
Going forward, after its strong run up over the past year, we forecast that Brent crude oil will start to consolidate around prevailing level of USD 70 to 80 / bbl. This is together with potential fiscal reforms by the new government are expected to be supportive of the MYR. As such, we adopt a neutral outlook for USD/MYR and see consolidation around 3.95 going forward from 3Q18 to 2Q19. Prevailing spot reference rate is 3.99. One of the risks to our neutral USD/MYR forecast is that of more aggressive tightening path by the US Federal Reserve. That could potentially result in further USD strength against Asian FX and the MYR as well.

INDONESIA



Bank Indonesia (BI) decided to raise the BI 7-day Reverse Repo Rate by 50bps to 4.75% at two meetings in May 2018. The rate hikes are part of BI's policy mix to maintain economic stability amidst rising global financial market uncertainty and tightening global liquidity. BI also pledged to continue its efforts to stabilize the rupiah in accordance with the fundamentals while ensuring that market mechanisms remain key in determining the rupiah exchange rate. We have revised our benchmark rate forecast to include another 25bps hike in Q3 to bring BI rate to 5.00% and then followed by another 25bps in Q4 to end the year at 5.25%. The series of rate hikes by BI may help keep the IDR stable below the psychological 14,000 level. Overall, we forecast USD/IDR at 13,950 in 3Q18 and 14,000 across 4Q18, 1Q19 and 2Q19.

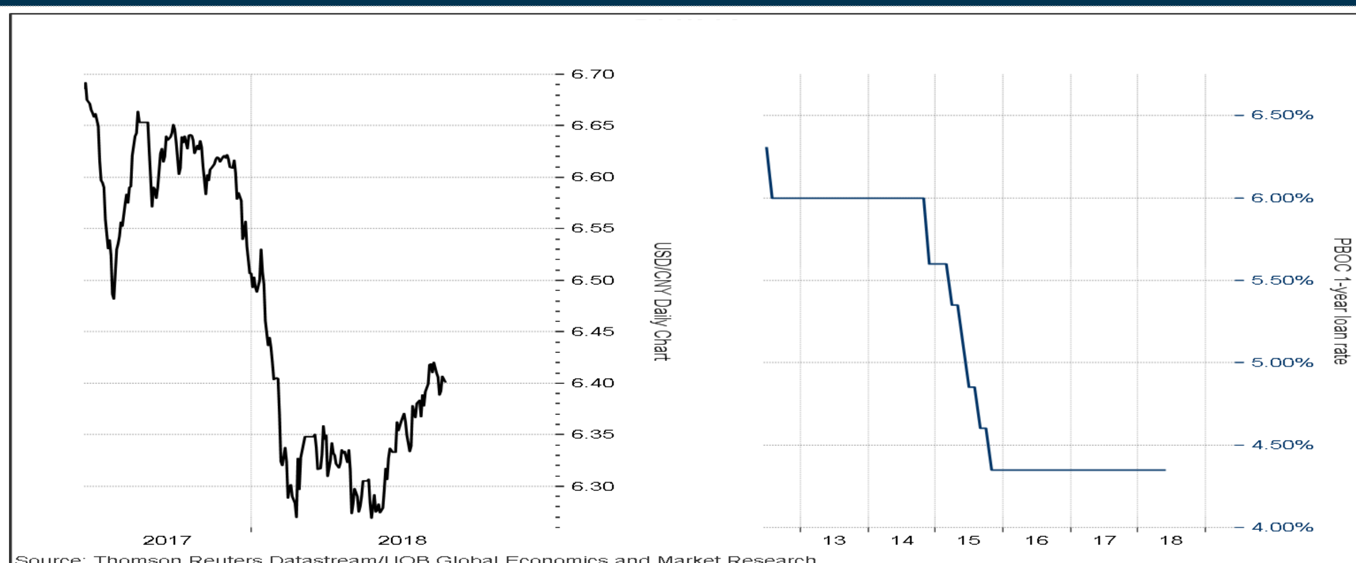
THAILAND



The BoT kept the policy rate unchanged at 1.5% on 16 May 2018. Looking forward, the BoT will likely raise the policy rate to 1.75% in 4Q18 as the economy would continue to expand steadily at around its potential rate, thus lessening the need for an exceptionally accommodative monetary policy.

In the face of further rise in US rates and on-going US monetary policy tightening, we believe that the THB alongside other Asian currencies will now weaken modestly against the USD going forward. This mild THB weakness, together with the above mentioned anticipated BoT rate hike in 4Q18 will help ensure that the Thai economy stays within its sweet spot near potential GDP growth. Overall, we forecast USD/THB at 32.2 in 3Q18, 32.4 in 4Q18, 32.6 in 1Q19 and 32.8 in 2Q19.

CHINA



The PBoC has been guiding the interbank rates higher via small increases to the open market operation (OMO) rates, three times in 2017 and again in March 2018. Recent moves were in lock-step with US rate hikes. These minor adjustments are in line with the central bank's prudent and neutral policy stance and its deleveraging policy as well as prevention of systemic risks. This is likely to be the PBoC's preferred channel. We also reiterate our call that there is still likelihood for PBoC to raise its policy rates (1Y lending and 1Y deposit rates) by 25bps in 2H18 as the US Fed continues with its rate hike trajectory. Following the unusually large 100bps cut to banks' reserve requirement ratio (RRR) in April (first cut since February 2016) which was targeted for repayments of banks' MLF borrowings and support for small and micro enterprises, we anticipate another similar RRR move in 2H18 to encourage lending to SME sector.

USD/CNY seemed to have registered a key medium term low in 2Q and will likely trend gradually higher from here. On-going trade tension between the US and China, coupled with upcoming rate hikes from the US Federal Reserve will weigh on the CNY. However, any weakness in the CNY will be modest as China will still register a reasonably strong growth rate of about 6.7% for this year. In additional, local interest rates are biased higher. Overall, we maintain our view for mild weakness in the CNY going forward. Our forecast for USD/CNY is 6.42 for 3Q18, 6.45 for 4Q18, 6.50 for 1Q19 and 6.55 for 2Q19.

FX, INTEREST RATE & COMMODITIES FORECASTS

FX	14 Jun 18	3Q18F	4Q18F	1Q19F	2Q19F
USD/JPY	110	110	111	112	113
EUR/USD	1.18	1.20	1.21	1.22	1.23
GBP/USD	1.34	1.33	1.32	1.31	1.30
AUD/USD	0.76	0.77	0.78	0.79	0.80
NZD/USD	0.70	0.71	0.71	0.72	0.73
USD/CNY	6.40	6.42	6.45	6.50	6.55
USD/HKD	7.85	7.84	7.83	7.82	7.80
USD/TWD	29.91	30.00	30.20	30.40	30.50
USD/KRW	1,082	1,085	1,090	1,095	1,100
USD/PHP	53.34	53.30	53.50	54.00	54.30
USD/MYR	3.99	3.95	3.95	3.95	3.95
USD/IDR	13,930	13,950	14,000	14,000	14,000
USD/THB	32.15	32.20	32.40	32.60	32.80
USD/MMK	1,349	1,350	1,360	1,370	1,380
USD/VND	22,759	22,900	23,000	23,100	23,200
USD/INR	67.61	67.80	68.00	68.50	69.00
USD/SGD	1.34	1.34	1.35	1.35	1.36
EUR/SGD	1.58	1.61	1.63	1.65	1.67
GBP/SGD	1.79	1.78	1.78	1.77	1.77
AUD/SGD	1.01	1.03	1.05	1.07	1.09
SGD/MYR	2.98	2.95	2.93	2.93	2.90
SGD/CNY	4.79	4.79	4.78	4.81	4.82
JPY/SGDx100	1.21	1.22	1.22	1.21	1.20

RATES	14 Jun 18	3Q18F	4Q18F	1Q19F	2Q19F
US Fed Funds Rate	2.00	2.25	2.50	2.75	3.00
USD 3M LIBOR	2.34	2.60	2.80	2.95	3.20
US 10Y Treasuries Yield	2.94	3.00	3.20	3.25	3.35
JPY Policy Rate	-0.10	-0.10	-0.10	-0.10	-0.10
EUR Refinancing Rate	0.00	0.00	0.00	0.00	0.00
GBP Repo Rate	0.50	0.75	0.75	0.75	1.00
AUD Official Cash Rate	1.50	1.50	1.50	1.75	1.75
NZD Official Cash Rate	1.75	1.75	1.75	1.75	1.75
CNY 1Y Benchmark Lending	4.35	4.60	4.60	4.60	4.60
HKD Base Rate	2.25	2.50	2.75	3.00	3.25
TWD Official Discount Rate	1.38	1.38	1.38	1.50	1.50
KRW Base Rate	1.50	1.50	1.75	1.75	2.00
PHP O/N Reverse Repo	3.25	3.25	3.25	3.50	3.50
SGD 3M SIBOR	1.52	1.75	1.95	2.15	2.40
SGD 3M SOR	1.57	1.65	1.85	2.05	2.30
SGD 10Y SGS	2.59	2.65	2.75	2.85	2.95
MYR O/N Policy Rate	3.25	3.25	3.25	3.25	3.25
IDR 7D Reverse Repo	4.75	5.00	5.25	5.50	5.50
THB 1D Repo	1.50	1.50	1.75	1.75	1.75
VND Refinancing Rate	6.25	6.25	6.25	6.25	6.25
INR Repo Rate	6.25	6.25	6.25	6.25	6.25

COMMODITIES	14 Jun 18	3Q18F	4Q18F	1Q19F	2Q19F
Gold (USD/oz)	1,300	1,280	1,250	1,220	1,200
Brent Crude Oil (USD/bbl)	77	70-80	70-80	70-80	70-80
LME Copper (USD/mt)	7,257	7,300	7,500	7,700	7,900

THE TEAM

Global Economics & Markets Research
Asset Management
Private Bank

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