AXJ Outlook – 2024 Year-End Edition

Economics & Strategy | Asia ex-Japan

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MIZUHO

Asia ex-Japan FX & Rates Outlook

Year-End 2024: **Trump-flation, Tyranny & Turbulence**

Trading Trump 2.0 Uncertainties: Policy and (Geo-) Political Upheaval from Trump 2.0 will inevitably rock global markets, policies and politics. The tensions between the reflationary aspects of **Trump-flation** and demand-dampening **tariffs** is hard to model. Consequently, there appears to be greater certainty about **turbulence** (from uncertainty) than there is clarity on trend.

Fed Trumped by Trump-flation?: The unexpected hawkish flex by the Fed to halve rate cuts for 2025 (to jut 50bp to leave rates at 3.75-4.00%) speaks to reflationary concerns from "Trump-flation". In other words, Trump 2.0 appears to have "trumped" a stronger desire to assure a soft-landing. That Trump-flation is hard to model, abrupt policy shifts is a clear risk, with attendant volatility in yields and the USD.

FX Hijacked by USD Tyranny: A dominant, if not **tyrannical "Trump USD" has hijacked the FX dynamics** as Trump 2.0 bets conspire with the Fed's partial (tilted to reflation outcome) Trump-flation considerations. Trouble is, given the inherent uncertainties/disruptions involved in Trump 2.0, the tyranny of the "Trump USD" intensifies volatility from abrupt, broad-based USD convulsions.

Rates Rocked by Trump-flation Turbulence: Turbulence in the rates space due to accentuated tensions between fiscal-reflationary outcomes as opposed to adverse global demand/trade shocks and potential for fiscal spending restraints suggest elevated volatility in rates. Possibly amplified at the long-end. As the dust settles though more pronounced term and risk premia appear to be par for the course and complementary to lower risk-free rates.

Trump-flation, Tyranny & Turbulence

- **Asia FX:** Trump 2.0 trade uncertainties conspiring with Fed cuts interrupted (possibly suspended in early-2025) and resultant USD dominance (amid elevated UST rates) sets the stage for USD-driven volatility biased to the downside until H2 2025. High-yielders prone to fiscal slippage-inflation risks may under-perform amid a steeper UST yield curve while Trump 2.0 tariff impact will be fluid whilst sensitivities to CNY/China risks wil be highly differentiated. Scope for pronounced late-2025 recovery is based on depth of adverse Trump impact since late-2024. On the whole recovery will probably be partial and volatility sticky (from elevated/unabated uncertainty).

- **CNY**: The trade war 2.0 is set to keep the CNY under pressure but PBoC's FX stabilizing measures and the major shift in fiscal and monetary policy mix will support domestic growth and counter external shocks. We expect the CNY to stabilize in H2-2025 as the tariffs delivery undershoots.

- **HKD:** Although the HK stock market retracement and a hawkish Fed put a pause on HKD appreciation, the HKD spot is expected to stay in the strong half of its trading band amid the Fed's easing cycle

- **INR**: As economic prospects dim and inflation pick-up more distinctly, the RBI's low-volatility FX reserve-currency volatility management strategy is feeling the strains. Drawdown on reserve into a strong USD and Trump 2.0 risks could result in more pronounced rupee weakness requiring opportunistic recovery latre-2025.

- **KRW**: Geo-political risk premium will linger and weigh on recovery prospects amid the BoK's tendencies to support softer growth in 2025 as Trump 2.0 threats lump.

- **TWD**: TWD is vulnerable to various threats under Trump 2.0 and turns in the semi-conductor cycle. Any escalation in trade tensions with China or US could dent Taiwan exports growth and set CBC on calibrated easing.

- **SGD**: While the moderation in the S$NEER within the policy bands has already gotten underway, there remains scope for further softening within the bands. MAS easing alongside CNY downside risks could accentuate downside risk in SGD through mid-2024 although s a lower beta currency before late-2025 recovery.

- **IDR**: Fiscal undercurrents remain as announced reforms do not give sufficient credence to new administration, while wider current account deficit on little upside to commodity prices likely to cast an overhang over IDR.

- **MYR**: Volatile swings on higher correlation to UST yields; but fundamentals should still see MYR in a good standing. BNM's prolonged hold ought to provide further support even if the currency is subject to volatility on CNH risks.

- **PHP**: Political woes, faster pace of cuts by BSP relative to regional peers, alongside slow-to-consolidate fiscal deficit compounding "twin deficit vulnerabilities" should mean regional underperformance.

- **THB**: Debt woes will weigh on recovery and more notability volatile nature of large swing and gains to persist in 2025. BoT to turn increasingly cautious and the central bank independence subject to political threats.

- **VND**: Diminished FX reserves will weigh on FX reserve accumulation under Trump 2.0 and current account surplus imply that there is significant risk of being target under the new administration.

- **AUD:** RBA looking to the possibility of easing in 2025 will perversely imply upside volatility as inflation remains bumpy and labour market gains remain robust. Nonetheless, China's fit and starts recovery may constrain in H1.

Currency Forecast

FX Forecasts	Q4 24	Q1 25	Q2 25	Q3 25	Q4 25
USD/CNY	7.04-7.38	7.10-7.55	7.15-7.60	7.05-7.45	6.98-7.37
	7.28	7.32	7.38	7.23	7.12
USD/HKD	7.76-7.80	7.75-7.79	7.75-7.79	7.75-7.79	7.76-7.80
	7.77	7.76	7.76	7.75	7.76
USD/INR	83.8 – 86.3	83.9 - 87.8	83.5 - 87.8	83.0 - 86.5	82.6 – 86.1
	85.2	85.8	86.0	84.8	84.3
USD/KRW	1317-1490	1320-1500	1370-1540	1330-1480	1290-1400
	1455	1438	1442	1385	1345
USD/SGD	1.283-1.368	1.327-1.376	1.330-1.388	1.315-1.375	1.292-1.344
	1.359	1.363	1.371	1.335	1.318
USD/TWD	31.6-33.1	31.8-34.5	32.1-34.5	31.5-33.9	31.2-33.5
	32.4	32.8	33.1	32.5	32.2
USD/IDR	15170 - 16350	15690 - 16380	15900 - 16480	15100 - 16380	14710 - 15810
	16150	16250	16300	15650	15200
USD/MYR	4.12 - 4.58	4.29 - 4.65	4.27 - 4.67	4.13 - 4.55	3.99 - 4.36
	4.51	4.53	4.53	4.30	4.12
USD/PHP	56.0 - 59.6	56.6 – 60.2	57.1 – 60.5	55.9 – 59.8	54.7 - 58.2
	58.9	59.5	59.6	57.2	56.5
USD/THB	32.3 - 35.3	32.9 - 35.9	33.8 - 36.2	33.4 - 35.7	32.7 - 34.9
	34.5	34.8	35.2	34.3	33.6
USD/VND	24560-25900	25300-26100	25200-26200	24600-25800	24500-25600
	25500	25850	25750	25100	24700
AUD/USD	0.616-0.694	0.610-0.660	0.608-0.668	0.610-0.673	0.645-0.700
	0.624	0.615	0.613	0.655	0.680

Note: For FX forecasts, level in parentheses pertains to period end forecasts; and the period's range precedes this.

Asia Ex-Japan (AXJ) FX: Trump Turbulence

Fig 1a. Trump USD Dominates

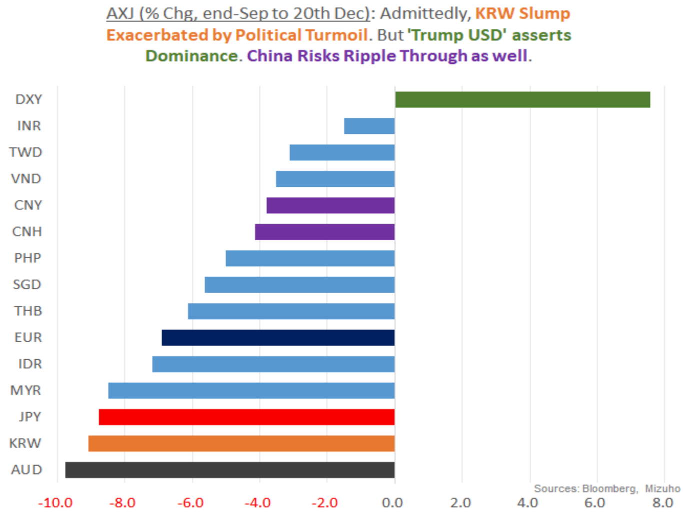


Fig 1b. Despite Fed Cuts, Real Yields Buoy USD

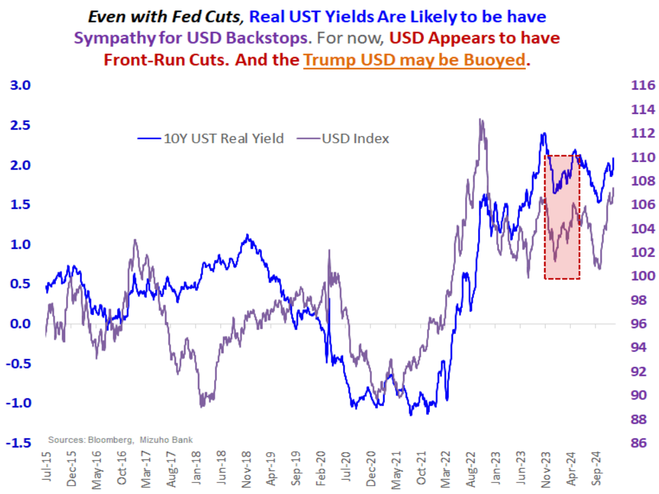


Fig 1c. AXJ Sensitivities to CNY Vary

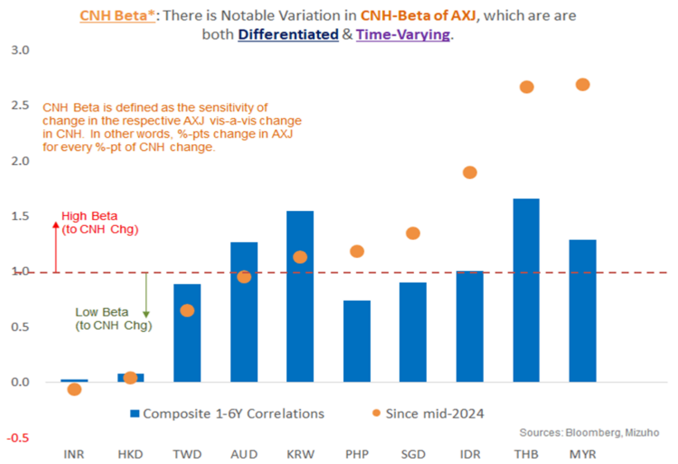
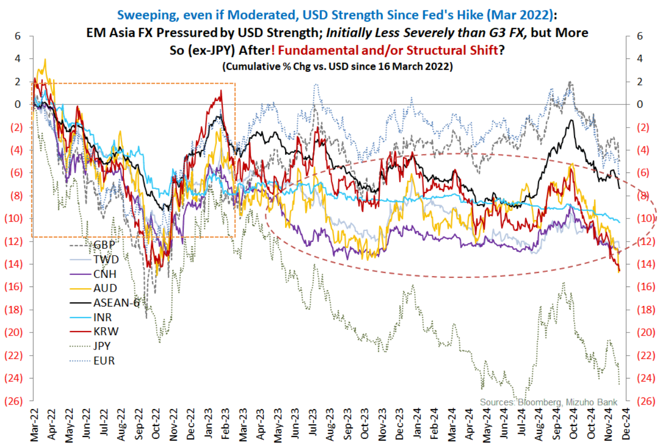


Fig 1d. Relative AXJ Under-performance



FX

- Defiant & Dominant "Trump Effect": *Despite 100bp of Fed rate cuts*, AXJ **are** *down* nearly 6%* since end-September. Such **defiant** and emphatic **USD strength**, *unencumbered by Fed cuts*, may be **attributed to** a **dominant "Trump effect"** – assumed to be *reflationary for the US* and *repressive for the rest* (allies, and adversaries alike) – **more than washing emphatic Fed cuts**. To be sure, the Fed dialing back easing bias (at the Dec FOMC) may accentuate, but not solely drive, USD buoyancy. Trump 2.0 is in the driver's seat. Nonetheless, **Trumpflation-driven USD surge at the expense of AXJ** is **neither linear nor unremitting.**

- Headlines (Risks)…: But ***initially***, **AXJ may be hijacked by, and sensitive to, headline risks**; and ***not necessarily from Trump 2.0 exclusively***. So, **regardless of underlying fundamental allure**, Trump 2.0 risks (led by announcement effects) could trigger sharp bouts of AXJ volatility.

- …& Headlights Especially as **AXJ are prone to "deer in the headlights" type** of **acute volatility** form being wrong-footed. After all, **unpredictability is a feature**, not a bug, (for Trump 2.0), and *volatility its companion.*

- Tariff Threats & Transmission: To be sure, **China has inherent** (albeit under-appreciated) **buffer from US trade antagonism** given unmatched industrial heft and unassailable cost/-efficiency advantages. Nevertheless, the **announcement effects of outsized/aggressive tariffs will inevitably trigger bearish CNH reflex**. Consequently, **most other AXJ will invariably suffer collateral damage –** as supply-chain and financial links overwhelm scope for near-term substitution gains.

- Ubiquitous, Uneven & Upsized: **Wider spill-over AXJ pain** from **tariff risks as** may be **ubiquitous** given the sweeping and inextricable linkages with China. Crucially, the **"beta"** (sensitivity to CNY depreciation drag) will be **uneven**, differentiated for trade/investment and geo-political exposure, across AXJ. *In many cases,* **AXJ losses may be upsized**, *exceeding the relative magnitude of CNY depreciation.*

- Differentiated & Dynamic: Specifically, **AXJ "beta"** vis-à-vis CNY pressures/China risks are not just **differentiated**, but also **dynamic**, (see Box 1) varying with the *details of tariff threats/execution, risk of retaliatory miscalculations and willingness/incentive to de-escalate/compromise.* Notably, **commodity FX** (AUD, IDR.) may **far more sensitive to onshore China stimulus triggers**. And even the **trade sensitivities in other supply-chain reliant AXJ** may be further differentiated. ***Upstream trade assaults*** restricting China's technology access impact KRW, TWD and JPY most vs. downstream impact ASEAN FX.

- Not Just Collateral (Damage): What's more, **AXJ pain may not be exclusively transmitted indirectly from CNY** as ***China may not be the only one in the crosshairs*** of Trump 2.0 US trade antagonism. *Vietnam, Taiwan* and *Korea* are at risk of direct trade pressures (and attendant FX wobbles) if Trump's bilateral, bottom-line, zero-sum game instincts are not tamed.

- Fed Detour: A **bumpy path of Fed cuts**, interrupted by sticky inflation and *US exceptionalism,* contrasting against Asia's growth pressures amid **trade risks** are **set to pressure AXJ**. But by the same token, *the Fed relenting to cut more* (later in 2025) could provide **some relief (and partial recovery) for AXJ**.

- Bark Worse than Bite Relief: Sustained AXJ relief though will be **highly contingent** on the ***trade tariff bark being worse than the actual trade disruption bite***. In other words, the worst of **tariff-driven uncertainty risk premium needs to abate for AXJ to find durable traction**.

- Tentative Two Halves with Back-End Relief: **AXJ are likely to be on the back foot into mid-2025** compromised by Trump 2.0 trade turbulence and a relatively less dovish Fed. But policy and geo-economic factors compromising AXJ (underpinning USD) may relent later. So, **AXJ pain may not be unremitting as relief/** ***partial restoration*** **tentatively emerges** later in **H2 2025**. All said though, the **vagaries of unpredictable Trump 2.0.** will remain hard to call. **Non-linearity** and **bumpiness will feature**.

Rates

- Trump Twist: To be sure, the **Trump 2.0 squeeze** (higher) **in yields** (that have rebounded from Fed cut pullback earlier) **hobbles an uninterrupted path down in rates**, which might ***otherwise*** have been ***expected from a global easing cycle***. This inevitably has **scope to spill-over into AXJ yields as buoyancy**. In some cases, partially offsetting, and in others, overwhelming, policy easing in Asia.

- Divergence& Differentiated Premiums: Notably, Trump 2.0 impact, accompanied by relative policy shifts, have resulted in signs of divergence between high-yield and low-yield dynamics in Asia. In the higher-yield space, long-end yields have climbed (as UST yields have risen) in contrast to the decline in the low-yielder space. This may partly be attributed to **more differentiated risk premium**. But not just that. This could partly be due to the *dimming (albeit not demise) allure of "all-in" returns in favour of risk re-pricing* at the margin.

Fig 1e. Risk-repricing Hits High-Yielders

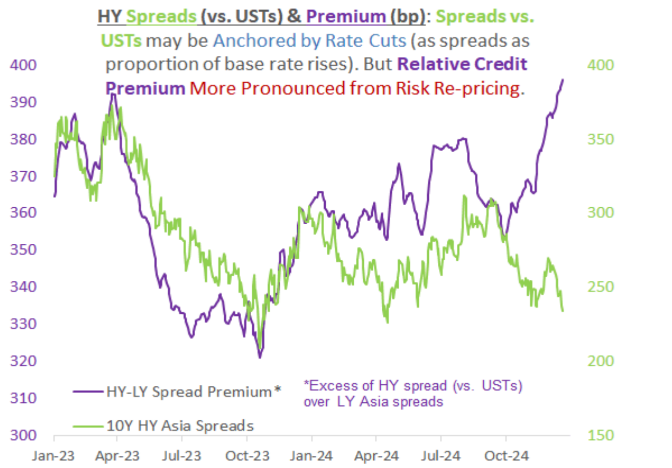
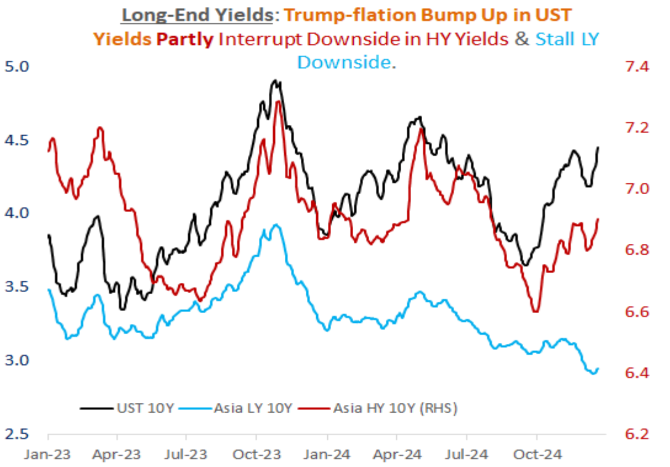


Figure 1f. Trump-flation Gets in the Way of Lower Yields



Box 1: Trump 2.0 Tariffs: Collateral & Bilateral Pains

In a Nutshell

- Expectations of **Trump 2.0 tariffs trained on China don't adequately appreciate far more profound and pervasive global trade risks elsewhere** from ***bi-lateral shocks*** and ***collateral damage***.
- *In fact, trade anguish could be relatively greater elsewhere as the* ***incremental trade shocks*** *are* ***disproportionately larger for other trade partners*** *than it is for* given **Beijing's advantages** of, **and consequent buffer** from, China's *sheer economic-manufacturing heft*.
- Accordingly, while it is **intuitive to express first-order Trump 2.0 tariff blows as CNH sell-off**, *harsher currency depreciation pressures in MXN, MYR, THB, AUD, KRW and TWD* may better capture the **confluence of trade shocks** from ***collateral damage*** and ***bi-lateral trade risks***.
- A **risk-differentiated, intra-AXJ view** (that is agnostic to broader USD dynamics) favours being *long SGD and INR* against a *short basket of VND-AUD-KRW-TWD*.

1. Trump 2.0 Tariff & China Pain

- Understandably, **Trump's "tougher on China" posturing**, (*replete with the threat of 60% tariff across all Chinese goods), **invoke fears of heightened trade antagonism** **with, and resultant** **economic pain for, China**.
- More so, if strident trade hawks dominating the White House dramatically dial- **US-China trade antagonism** and increased propensity for a volley of retaliatory responses aggravate **attendant economic pain**.
- FX Implication 1: And so, assumptions of **US-China trade antagonism resulting in USD strength *at the expense of CNH*** mis certainly legitimate.

2. But China Antagonism, Anguish Elsewhere

- *But* expectations of **Trump 2.0 tariffs trained on China don't adequately appreciate far more profound and pervasive global trade risks elsewhere** from ***bi-lateral shocks*** and ***collateral damage***.
- ***Acutely so for exporters in Asia*** *(and* ***Mexico****) that are both dependent on US and inextricably intertwined with the Chinese supply-chain.*
- *In fact, trade anguish could be relatively greater elsewhere* China's *sheer economic-manufacturing dominance* that inadvertently render ***incremental trade shocks disproportionately larger for other trade partners***.
- FX Implication 2: And so, ***CNH sell-off*** might be the lower-beta version ***compared to the broader depreciation jolts elsewhere in the AXJ space*** (as well as compared to MXN and possibly even CAD).

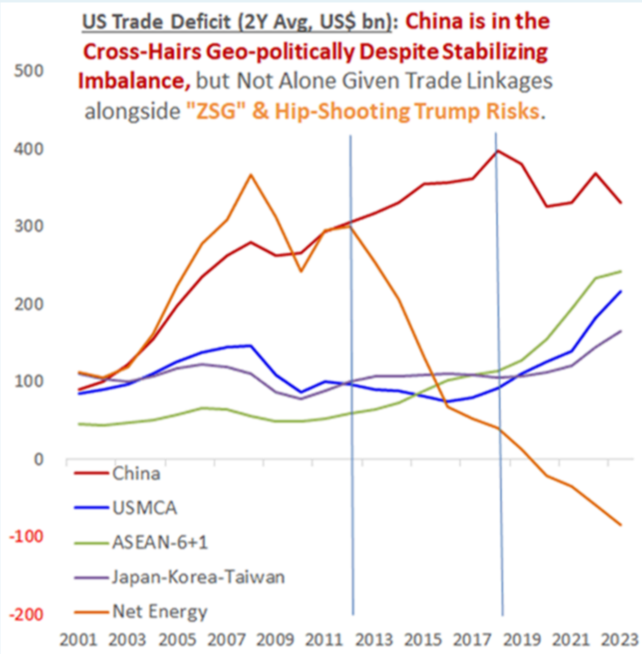
3. Collateral & Bilateral Shock Transmissions …

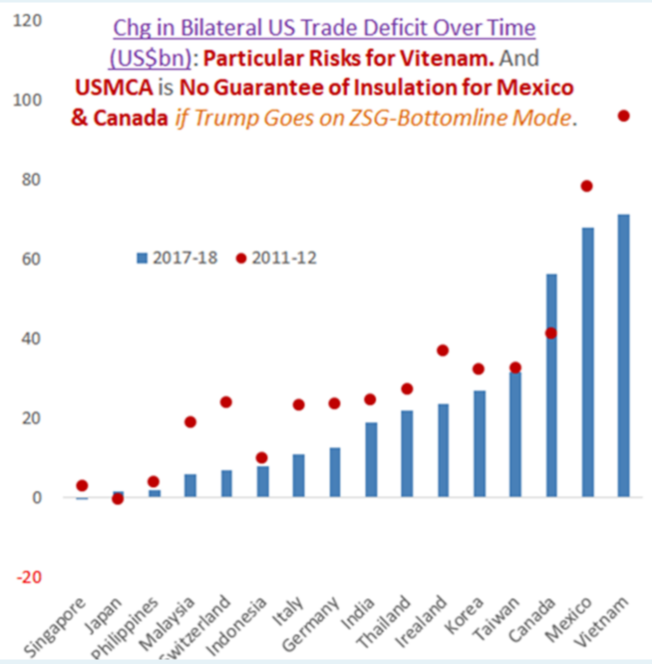
- Point being, **China's unmatched manufacturing advantages** *of scale, capabilities, supply chain dominance* and other *production synergies*, **which cannot be easily or quickly replicated**, translates to **relative superior resilience** (once adjusted for global demand cycle) **to global trade shocks**.
- Whereas **collateral damage elsewhere along the supply-chains** from, adverse US-China trade conflict fallout is bound to be significant, possibly worse (than the direct impact on China) for many other exporters.

- Especially once, *supply-chain reliance*, underlying *resource demand*, *second-order economic spillovers* and *financial channels* are accounted for.
- What's more, **trading partners other than China** are also at **high risk of direct, bilateral Trump 2.0 trade blows** from more *mercurial, bottom-line focused US trade policy* that is *rooted in zero-sum game view of globalization.*
- FX Implication 3: Notably, the alignment of risks warn of **sharper sell-off in MYR, AUD, THB, KRW and TWD** given *heightened sensitivities from trade dependence* (via supply-chain, and upstream commodities impact) *accentuated by wider investment and financial flows.*

4. … Differentiated Across AXJ

- To be sure, **wider AXJ risks derived from Trump 2.0 tariff threats** are ***differentiated*** and ***dynamic***, contingent **on the details and execution** of tariffs, **retaliatory responses** and **propensity to walk back after negotiations**.
- But **at first blush**, pre-existing vulnerabilities to collateral damage from supply-chain/investment linkages and bilateral trade antagonism suggest greater sensitivities for *MXN, MYR, THB, AUD, KRW and TWD*.
- **Collateral damage from supply-chain risks impact most of Asia**, with *upstream tech exports from Taiwan, Korea and Japan* at conspicuous risk. And *Australia is vulnerable to outsized ripples via commodity channels.* **India** is **notably least exposed to trade/financial linkages with China**.
- **Bilateral trade pain** may arguably be *most acute for Vietnam* (outside of Mexico), with Taiwan and Korea also not off the hook. Remarkably, **Singapore's trade deficit with US limit risks if bilateral US trade antagonism**.
- FX Implication 4: Accordingly, a **risk-differentiated, intra-AXJ view** (that is agnostic to broader USD dynamics) favours being *long SGD and INR* against a *short basket of VND-AUD-KRW-TWD.*





CNY: Depreciation pressure returns

	Q3 2024	Q4 2024	Q1 2025	Q2 2025	Q3 2025	Q4 2025
Policy Rate (%)	1.5	1.5	1.3	1.1	0.9	0.9
USD/CNY	7.00 - 7.28	7.04-7.38	7.10-7.55	7.15-7.60	7.05-7.45	6.98-7.37
	7.02	7.28	7.32	7.38	7.23	7.12
GDP (% YoY)	4.6	5.0	4.4	5.0	4.9	4.8
CPI (% YoY)	0.5	0.3	0.5	0.1	0.2	1.2

Note: Values in black are historical whereas those in blue represent forecasts. * Point forecast is for end-period. Ranges are only indicative.

Fig 2a. CNY weakened amid tariff concerns

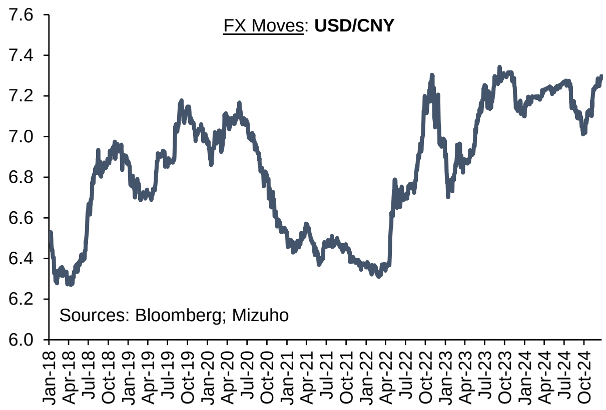


Fig 2b. Continued deflationary pressure onshore

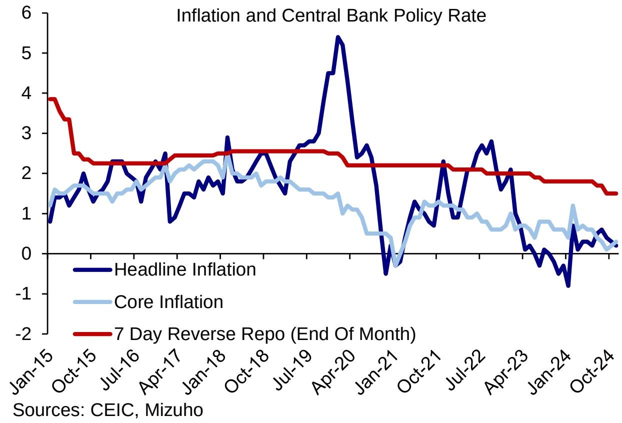


Fig 2c. Exports held up after Trump tariffs 1.0

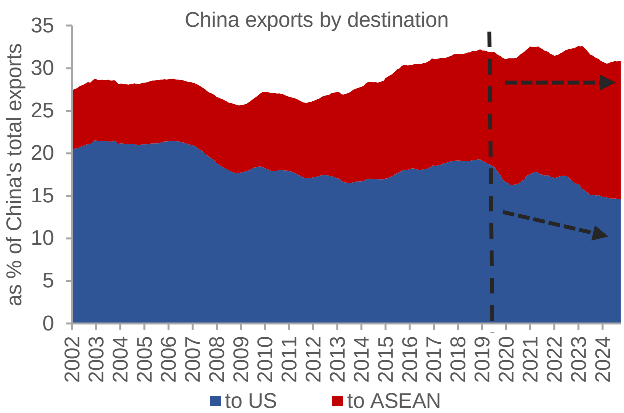
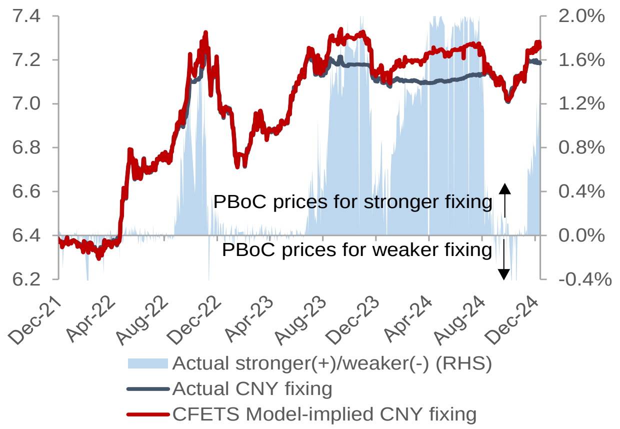


Fig 2d. PBoC priced for a stronger fixing in the past



FX

- Looming US tariff threats: Concerns over a potential trade war 2.0 after Trump's victory and the USD strength sank the CNH to a 13-month low of 7.3269 Through his social media post, US president-elect Trump vowed to impose an additional 10% tariff hike on all Chinese goods. If implemented, the average US tariffs on Chinese goods would climb to around 40%, which is lower than Trump's earlier proposal of 60% tariffs this year. Market participants will monitor the actual implementation of US tariff hikes on Chinese goods given the constraints of US reflation risks.

- Lower tolerance for RMB depreciation: Unlike the trade war 1.0, the PBoC is unlikely to engineer RMB depreciation to counter impact from tariffs hikes. The PBoC repeats to prevent the formation of one-way FX market movements and their self-fulfilment, while Chinese leaders reiterate the goal of keeping the RMB stable at a reasonable equilibrium. A sharp RMB depreciation to counter tariff impacts could hinder RMB internationalization and exacerbate capital outflow, posing a direct challenge to President Xi's goal of building a powerful currency. Furthermore, the regulator will face a tough task in managing RMB depreciation expectations, and a policy misstep could risk an FX depreciation-driven financial market crisis.

- New policy mix to counter tariff shocks: Chinese leaders have made a significant policy shift to support domestic growth and counter tariff shocks. The Chinese Politburo meeting pledged to implement more proactive fiscal policies and moderately loose monetary easing next year. The Central Economic Work Conference previews more proactive macro policies, including raising budget deficits, delivering cuts in the Required Reserve Ratio (RRR) and policy rates at appropriate times, and prioritizing consumption growth.

- US-China interest rate spread still weighs: Considering the shrinking room for Fed easing and the PBoC's shift to a moderately loose monetary policy, continuous US-China rate differentials are set to pressure the CNY exchange rate in H1 2025. If FX stability is warranted, the PBoC will likely ease further to support growth and combat deflation risks. Amid prevailing USD exceptionalism, the USD yield advantage will continue to encourage onshore corporates and individuals to hoard USD.

- Manageable RMB depreciation risks: Despite escalating pressure on the RMB, we do not hold a particularly bearish view on its outlook. The marginal impact of additional tariff hikes in Trade War 2.0 is expected to be less severe, following supply chain redirection due to the first trade war and the COVID period. The actual impact of tariffs on the Chinese economy will vary depending on their levels. We believe that US tariff implementation could be lower, with maximum tariffs of 50-60% potentially serving as a negotiation tool. Potential US tariff relief could trigger a CNY rebound in Q4 2025. Despite further rate cuts, the PBoC is expected to actively use the CNY fixing tool to defend the currency.

Rates

- More rate cuts amid reflationary policies: China's average interest rates for general loans have surpassed its nominal GDP growth rates for five consecutive quarters, indicating to a tight liquidity environment. We expect more cuts to bank lending rates to revive business sentiment, as the PBoC prioritizes efforts to guide a moderate increase in prices. We consider an appropriate 1Y LPR to be around 2.5% for 2025, 60bp lower than the current rate. Additionally, we foresee paced rate cuts in 2025, with a 20bp reduction each quarter, allowing banks time to adjust their deposit rates accordingly and protect their net interest margins.

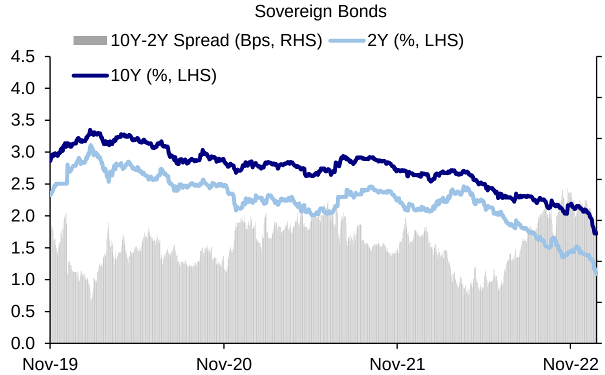
- Unusually ample liquidity at year-end: Although seasonal factors usually drive rates higher in late December, expectations for a loosening monetary policy following the annual Central Economic Work Conference push rates lower across the curve. In late December, the 1Y CGB yield fell below 0.9%, and the 10Y CGB yield reached a record low of 1.71%, against the backdrop of RMB 2 trillion refinancing bonds being issued by local governments. However, we still believe that the PBOC will honour its forward guidance and conduct a RRR cut by the year-end.

- Market in a wait-and-see stance: While Trump's China policy will be crucial to monitor in the coming months, we believe his tariff threats are more likely to serve as leverage in negotiations, which would lead to significantly reduced tariff rates ultimately. However, this ongoing trade uncertainty is expected to heighten market volatility and adversely affect business sentiment in the near future.

- Yields: Overall, yields may drift lower in the short term as market expectations for easier monetary conditions rise. We foresee subdued front-end CGB yields over the next few months as the PBoC aims for lower bank deposit rates in view of the squeezed net interest margins of major banks.

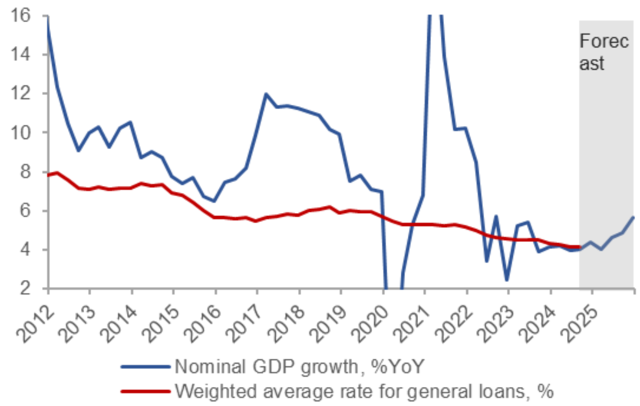
- Curve: Given the likelihood of increased market volatility, term spreads are likely to move sideways in the near term. However, we expect the term spread to widen later next year, with the 10Y CGB yields being propped up back to ~2.0% by reflationary policies.

Fig 2e. PBoC averts unwanted flattening



Sources: Bloomberg, Mizuho

Figure 2f. A tight liqudity situation for several quarters



Box 2: Why Beijing Will Not Deploy an Aggressive CNY Devaluation

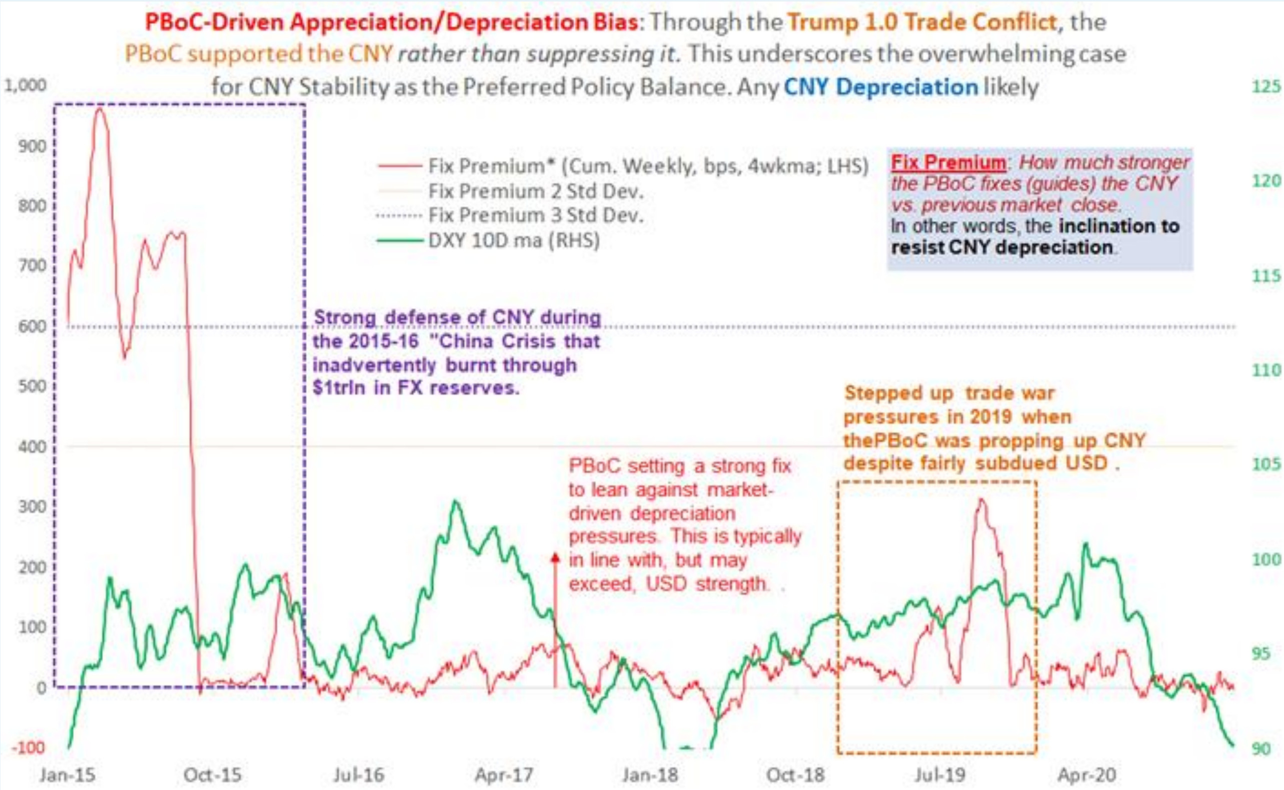
In a Nutshell

- Fervent bets that that Beijing will actively **weaken CNY in response to Trump tariffs** sorely *lacks nuance, misplaces context,* and *ignores lived experience.*
- Fact is, **Trump 1.0 tariffs required Beijing to support, not suppress, the CNY**. And **little has changed on that front**.
- Above all, **CNY depreciation pressures** (from tariffs) **accentuating wider China macro woes** amid intensifying geo-political stress (including trade antagonism) is a **greater threat than any imagined relief sought from a weaker CNY**.
- To be sure, **CNY depreciation risks** are heightened. But this is **from market pressures amid geo-economic stress** and ***not a policy response to tariff threats***.

- Lopsided, if not Misguided: Reports that Beijing could resort to CNY depreciation in response to, or to mitigate tariffs is a lopsided argument given ***benefits don't outweigh the associated costs***. At best, it **overstates the case and latitude for CNY depreciation**. *At worst,* **it is grossly misguided**.
- Balance of Risks Favours CNY Stability: In the grander scheme of things, the **desirability of a broadly stable and supported CNY* overwhelms** *narrow and potentially high-cost CNY depreciation.*
- Destabilizing Capital Outflows a Prominent Threat: Specifically, the **threat of an adverse**, self-reinforcing **loop of depreciation and potentially destabilizing capital outflows**. This remains **a prominent threat** as Beijing struggles to simultaneously reinstate onshore confidence and confronts geo-political threats.
- Trade Benefit of Weaker CNY Limited: What's more, the **trade advantages from a cheap(er) renminbi** as China scales the value chain are **far less compelling**.
- Tariff Cushion: **Admittedly**, a **cheaper CNY** that (all else equal) allows for lower USD pricing of exports could **initially cushion against the adverse demand impact of tariffs**.
- Involves Greater Macro Risks: But it inevitably entails **greater macro risks**. For one, it is **ultimately repressive for Chinese industries** (and inevitably, the economy). More dangerously, such **overt (FX) mercantilism will court**, ***and ironically justify***, **further US trade backlash**.
- Neither Convincing …: Point being, **CNY depreciation is simply not convincing** as a credible mitigation for trade conflict threats risks insofar that it **risks further inflaming trade animosity** and **impedes China's more strategic pursuit of technological leadership**.
- … Nor Controlled: Moreover, **acute geo-political stress** that threaten to **intensify capital/financial outflow risks** that simultaneously feed into, and off, **CNY pressures** suggest that **CNY depreciation** *as a tool* **lacks requisite** (but critical) **control to avert the dangers of spiralling macro instability**.
- Trump 1.0 Tariffs Required CNY Support: In fact, **CNY depreciation during Trump 1.0 tariffs was in spite**, ***not because,*** **of Beijing's emphatic attempts to shore up the CNY**. So, cheapening the CNY in response to tariffs **is not the lived experience**. Nor is it likely to be a new reality.
- As Macro Stability Trumps Tariff: Fact is, **sharp CNY depreciation threatens to impose far more debilitating macro pain** from destabilizing outflows. Whereas *China's unmatched industrial scale, expertise and ecosystem allows it to weather tariffs without unduly exposing itself to destabilizing FX risks.*

- Admittedly, Path of Least Resistance (& Optimal Stability): **To be sure, CNY depreciation is likely to be a glaring outcome** of trade/geo-political stress. But not by Beijing's design (or even desire). Instead, the PBoC will merely be judicious in the sharp trade off between CNY defense and FX reserve depletion so that it does **not engage in futile, and wasteful resistance**. Counterintuitively, **accommodating some CNY depreciation** is healthy pressure relief that **helps deflect adverse spiral of depreciation and capital outflows**. So, CNY depreciation may be conceded, not encouraged; with a view of **optimal stability between CNY backstop and wealth (FX reserve) preservation**. More so, **as Beijing commits looser monetary policy stance**.
- CNY Relief Overstated, If Not Illusory: But all said, any **imagined benefit of cheap CNY to counteract Trump 2.0 tariffs** is not just **overstated**, but **arguably illusory**. And ultimately, it may prove to be **strategically self-defeating**. Especially given the geo-economic cross-roads, where China will need to be more acquisitive (be it talent, technology, know-how or resources) to ensure industry leadership.
- Beijing Can't Afford Cheap (CNY): All said, **a cheap CNY** to counteract tariffs will **inadvertently and ironically prove too costly** for overall macro-stability. Critically, *Beijing especially can't afford a cheap CNY* that not only threatens to potentially destabilize macro/financial conditions amid current uncertainty/doubts, but over time, impedes Beijing's broader technological ambitions.

* More so in trade-weighted terms, but not at the exclusion of relative USD/CNY stability (once the broader and sweeping USD trend is accounted for).

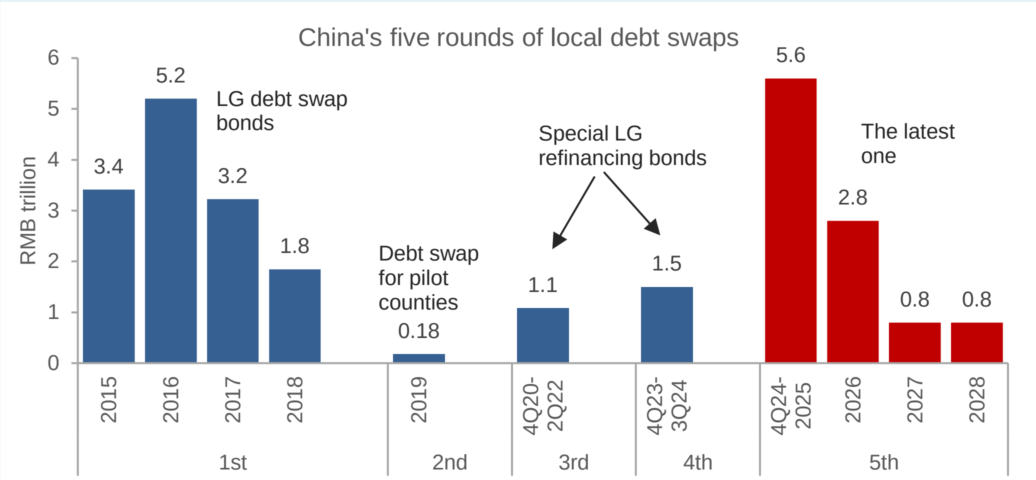


Box 3: How to interpretate China's RMB10trn debt swap plan

In a Nutshell

- While market reactions to China's latest debt swap plan have been tepid, we believe the impact of this five-year plan will be front-loaded and thus more positive than market expectations.
- This plan is expected to significantly enhance local fiscal conditions, providing local governments with more resources to support domestic demand.
- China also plans to expand the types of projects eligible for funding through special local government bonds, which should help address the sluggish public investment observed year to date.

- 5Y debt swap plan: China has introduced a RMB 10 trillion relief plan to mitigate the problem of hidden local government debt, which includes an annual increase of RMB 2 trillion in the debt ceiling for special local government bonds for three years and RMB 0.8 trillion in new issuances over the next five years, starting in 2024.
- Front-loaded impact: While market reactions to China's latest debt swap plan have been tepid, we believe the impact of this five-year plan will be front-loaded and thus more positive than market expectations. With less than one month remaining in 2024, more than half of the debt swap plan (RMB 5.6 trillion) will be implemented in the next 13 months, exceeding 4% of China's annual GDP. This represents the largest annual amount since China launched its first round of local debt swap programs in 2015.



- Less interest payments: According to Finance Minister Lan Fo'an, the entire debt swap program is projected to save local governments RMB 600 billion in interest over the next five years, which amounts to more than half of the government's interest payments made in 2023.
- Mitigated debt burden: Furthermore, this program is anticipated to alleviate the burden on local governments in repaying hidden debt using government revenue against the backdrop of sluggish land sales. Such enhanced fiscal conditions would allow local government to allocate more resources to support domestic demand.
- The part of debt left unattended: Meanwhile, the current size of the debt swap is not enough to completely tackle China's hidden debt challenges. We estimate that the interest-bearing liabilities of local government financing vehicles (LGFVs), the primary form of hidden local debt, reached nearly

RMB 50 trillion in June 2024. More than half of these LGFVs do not have adequate cash flow or earnings to service their debt. As a result, LGFVs with long project return periods are likely to face significant pressure in repaying their debts, which will continue to affect local fiscal conditions. It is essential for local governments to support the restructuring of LGFV debt that is not part of the debt swap through mergers, acquisitions, or liquidations.

- Fiscal deficit up to 4% of GDP: Looking forward, we anticipate further fiscal measures aimed at boosting domestic consumption in the coming months. Minister Lan has suggested that there is substantial room to increase China's central fiscal deficit. We predict that Chinese officials will raise the official fiscal deficit to between RMB 5.2 and 5.5 trillion, which would represent 3.8% to 4% of GDP in 2025. Furthermore, the central government is expected to shoulder a larger share of spending obligations next year compared to 2024.
- A wider range of projects funded via government bonds: Moreover, several additional measures are expected, including the issuance of special sovereign bonds to replenish national bank capital and the financing of a wider array of projects through special local government bonds. It is important to note that authorities have recently released guidelines for acquiring undeveloped or idle land from developers using these bonds.

HKD: Stays clam before Trump's storm

	Q3 2024	Q4 2024	Q1 2025	Q2 2025	Q3 2025	Q4 2025
USD/HKD	7.76-7.82	7.75-7.79	7.75-7.79	7.75-7.79	7.75-7.79	7.76-7.80
	7.773	7.76	7.76	7.75	7.75	7.76
GDP (% YoY)	2.9	2.4	1.9	2.0	2.7	3.0
CPI (% YoY)	2.5	2.1	2.3	2.9	2.5	2.3

Note: Values in black are historical whereas those in blue represent forecasts. * Point forecast is for end-period. Ranges are only indicative.

Fig 3a. HKD strengthened as Fed cut rates

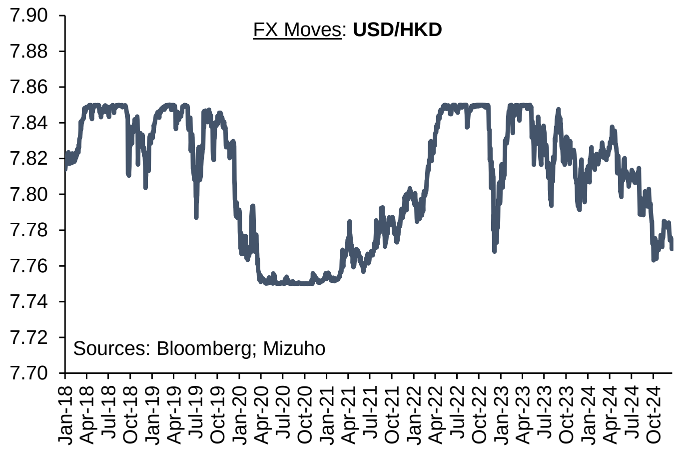


Fig 3b. Subdued underlying inflation

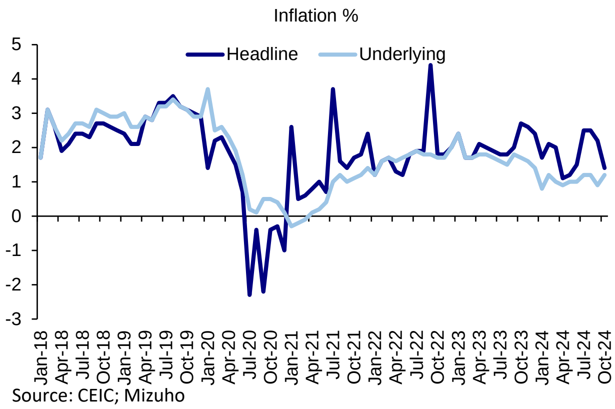
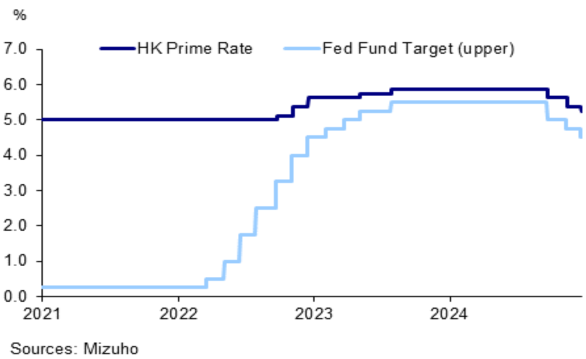


Fig 3c. HSI consolidated amid China stimulus rally

Fig 3d. HK banks followed foot-steps of Fed's cuts



FX

- Stays calm before Trump's storm: HKD sentiment soured after Trump's victory. The return of RMB depreciation pressure and the repricing of higher USD rates pushed HKD spot back to near 7.78 level. In December, renewed China stimulus hopes boosted the Hang Seng Index and encouraged equities inflows, pushing HKD spot back to near 7.77 level. Onshore China investors remained keen to add more exposure to HK shares, with southbound Stock Connect flow increasing further to near HKD 730bn.

- Pick-ups in IPO market: IPO market sentiment continued to improve, with more companies launching their listing projects since October. With the recovery in HK equities, Hong Kong IPOs have raised more than USD 10.5bn so far this year, significantly exceeding the amount of USD 5.9bn in the year of 2023. Several IPOs received heavy oversubscriptions, leading to HKD liquidity squeeze. In light of IPO regulation tightening in A-shares markets, Chinese companies emerged as active players in HK IPO market, with a leading Chinese express delivery company raising USD 749mn via the IPO listing.

- USD-HKD peg to stay intact: Trump's return to office could ramp up discussions on the USD-HKD peg stability, alongside worsening HK government budget deficits. Despite the revocation of HK's special status and the passage of the Hong Kong Autonomy Act during Trump's first presidency, we expect the USD-HKD peg to remain intact. Restricting USD exchange into HKD would be a costly option for the US financial sector and could damage the USD's status in the currency market and as a reserve asset. In early December, President-elect Trump warned BRICS of 100% tariffs if they attempt to move away from the USD. This suggests that the Trump administration would avoid making moves that jeopardize the USD's status as a dominating global currency. The HK government is highly unlikely to change the peg, as there is no better alternative for such a small and open economy.

- Strong-half of trading band: Although the HK stock market retracement and a hawkish Fed put a pause on HKD appreciation, the HKD spot is expected to stay in the strong half of its trading band amid the Fed's easing cycle. However, the sooner Fed's rate cut cycle could slow HKD upward momentum. Additionally, the Hang Seng Index could regain momentum if the Chinese government commits to ramping up stimulus to counter external shocks. Improving HK business sentiment and stabilizing property markets should support corporate and mortgage loan demand, thereby narrowing the USD-HKD rate spread in the medium term.

Rates

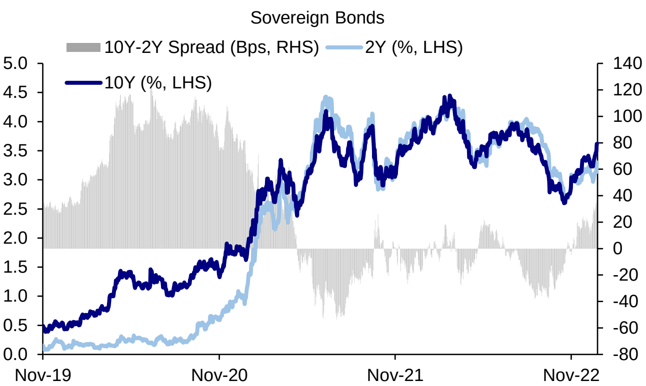
- HK interbank rates rebounded: HK interbank rates rebounded on the IPO subscription demand and year-end liquidity tightening, following the consolidations in October and November. The renewed China stimulus hopes also bolstered HK stock market sentiment and supported HKD rates. The tick-up in the Hang Seng Index transaction volume brought settlement demand for HKD but its impact on HKD rates was relatively modest. As a result, HK banks scaled down liquidity withdrawal via discount window operations so far in December. HK aggregate balance remained unchanged at near HKD 45bn.

- Undersubscriptions for HK government bonds: The HK government launched a retail infrastructure bond with a target size of HKD 20bn at a minimum coupon of 3.5% or linked to inflation. However, the bonds received undersubscriptions, and the final issuance size will likely be adjusted lower to HKD 17.8bn. The comparatively low yield of 3.5% versus the Silver Bond yield of 4% and a reviving IPO market might have contributed to the lackluster demand for bond subscriptions. Additionally, the expansion of HK bond issuance flagged worries about HK government budget deficits in the medium term.

- Follow-up cuts in HK prime rate: HK banks followed suit to cut the prime rate by 25bps after the Fed's 25bps rate cut in November but slowed to a 12.5bps cut another Fed's 25bps cut in December. This follow-up rate cuts after three straight FOMC meetings were slightly surprising, given the record of HK's slow prime rate hike cycle since mid-2022. This rate decision suggested that HK banks are motivated to stabilize the property market and lend out excessive liquidity given the subdued loan-to-deposit ratio. By supporting the local property market, HK banks could mitigate credit-impaired losses in their commercial real estate (CRE) loans to HK clients. Despite the narrowing spread between the prime rate and HIBOR funding costs, a stabilizing property market could benefit banks' credit portfolios.

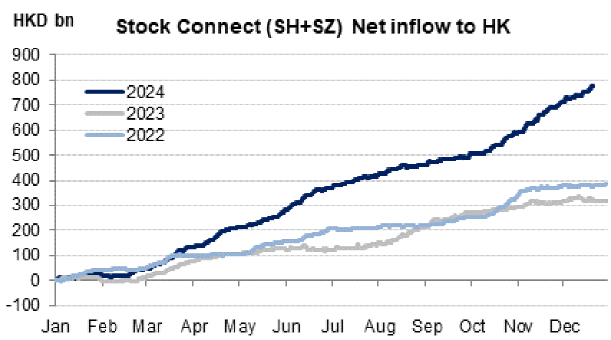
- Year-end liquidity squeeze: HK rates are subject to upside at year-end, considering the year-end seasonality and the Fed's slowing rate cut pace. The pick-up in IPO projects and the rebound in HK equities fuelled upward pressure on HKD rates. If the HK banks' total 62.5bps prime rate cut materializes to stabilize the property market, the return of mortgage loan demand should help reduce the USD-HKD rate divergence. However, the slowing momentum in HK equities is set to delay the timing of HKD hitting 7.75, and the absence of HKD liquidity injection will keep the aggregate balance low for a while.

Fig 3e. HKGB term premium tracked on UST



Sources: Bloomberg, Mizuho

Figure 3f. Strong Stock Connect inflow



INR: Risk Beta Bumped Up

	Q3 2024	Q4 2024	Q1 2025	Q2 2025	Q3 2025	Q4 2025
Policy Rate (%)	6.50	6.50	6.00	5.50	5.25	5.25
USD/INR	83.3-84.0	83.8-86.3	83.9-87.8	83.5-87.8	83.0-86.5	82.6-86.1
	83.8	85.2	85.8	86.0	84.8	84.3
GDP (% YoY)	5.4	6.2	5.9	6.5	6.3	5.4
CPI (% YoY)	4.2	5.6	5.3	5.8	4.2	4.5

Note: Values in black are historical whereas those in blue represent forecasts. * Point forecast is for end-period. Ranges are only indicative.

Fig 4a. Increasing Pressures on the Rupee

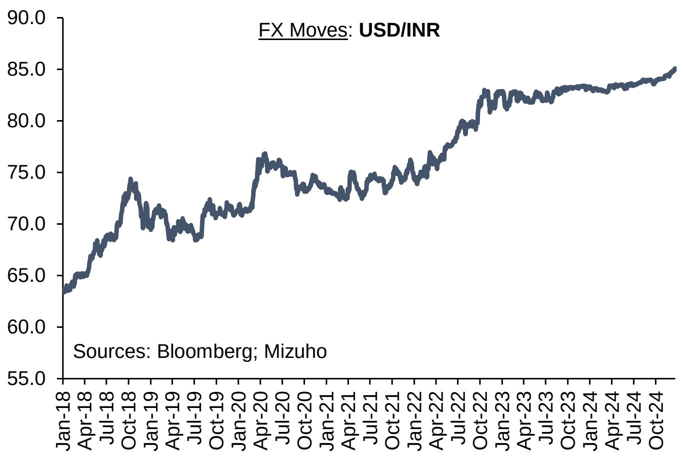


Fig 4b. India Inflation Rebound is Inconvenient

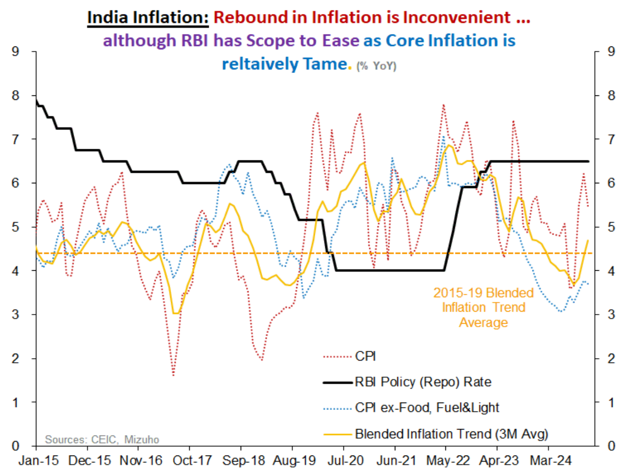


Fig 4c. Eroded Real Rate Compromises INR

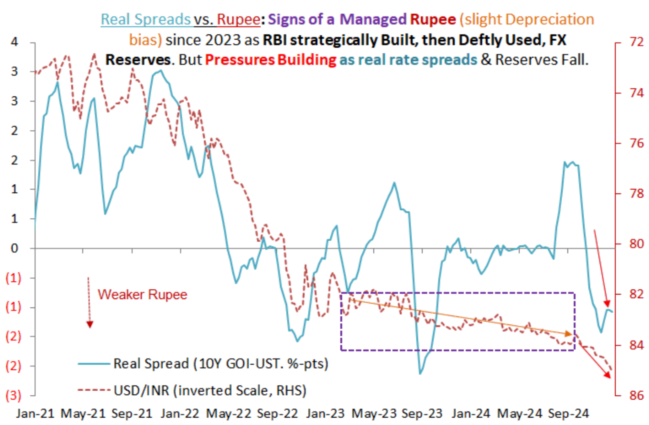
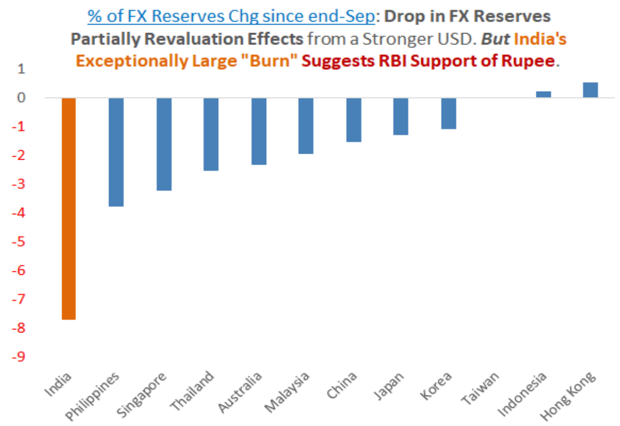


Fig 4d. FX Reserves Burnt to Temper Rupee Slide



FX

- Woes beyond Trump Dollar: The **Indian rupee** has come under **considerable pressures** in recent weeks as the *Trump 2.0 USD rebound* has collided with, and inevitably *exacerbated by, dimming onshore macro factors.* And the conspiracy of headwinds has arguably **bumped up rupee's "risk beta"** from earlier.

- Inflation & Real Pressures: For one, there has been a **resurgence of inflation** above that has **rapidly dented real rate support for the rupee**. Admittedly, this is disproportionately driven by food, as is telling from core inflation is better contained. Nonetheless, threats to inflation expectations may **extract greater risk premium**.

- Exacerbated by Growth Headwinds: More so, amid **unexpectedly sharp deceleration in growth** (with Q3/FYQ2 GDP stumbling to 5.4% from 6.7%). Worrying signs of consumption pressured by stretched households and private sector capex rebound stifled by caution **take some shine off India's stand-out growth narrative/allure**. And this is a **double whammy for INR** amid inflation rebound.

- RBI Bind: In which case, the **RBI's conspicuous abstinence from a cutting cycle** in contrast to most of its regional peers has been **deprived of the benefit of relative (policy) rate support advantage**. Instead, it appears to be **cast in the shadow of a policy bind impeding the rupee**. At least while inflation exceeds the RBI's 4%+/- 2%-pts bounds, highlighting the RBI's policy dilemma, and potentially sharper trade-offs.

- "Twin Deficit" Overhang: *Moreover,* the **"twin deficit" handicap** for the rupee is now harder to brush off on account of growth out-performance and/or inflation discipline. And **despite softer oil prices** that alleviate the Current Account pressures, the **rupee valuations may be compromised,** *all else equal.*

- Reserves Building Turns to Burn: Notably, assurances of **India's earlier FX reserve building**, (that hit a record of over $616bn in Sep) has now turned to **nascent anxiety about FX reserve burn**, amid a loss of >$47bn (to $569bn). Valuations effect from a stronger USD may only be blamed for less thana quarter of these losses. Worse, deeper losses are probably tucked off balance sheet. So *rupee is stifled for now.*

- Mitigated by CNY Hedge Advantage: Nonetheless, **rupee position as preferred anti-CNY hedge** a **fairly unique source of resilience** (especially amid Trump 2.0 tariffs threat for China). In fact, apart from **inherently low correlation with CNY**, b *India's strategic geo-political positioning against China may enhance rupee's relative allure* amid trade conflict turbulence.

- INR Outlook: Inevitably, the risks are tilted to more pronounced USD/INR upside, with 88 not an outlandish test, even without extreme outcomes. The silver lining is that trade war headwinds may affect rupee less. Perhaps even boost relative allure. And a coincidence f dis-inflation, RBI easing backed by deeper Fed cuts could restore partial traction to `$82.5-8335 levels into late-2025 (as the USD mellows broadly).

Rates

- Central Bank: With a **new central bank chief Malhotra** now in place, a **remarkably patient RBI that has abstained from easing** is **expected to judiciously lower rates**, starting in February 2025. To be sure, Malhotra is **not an unmitigated dove**. But equally, he is ***not inclined to be unduly hawkish*** given the burden of ensuring growth does not falter.

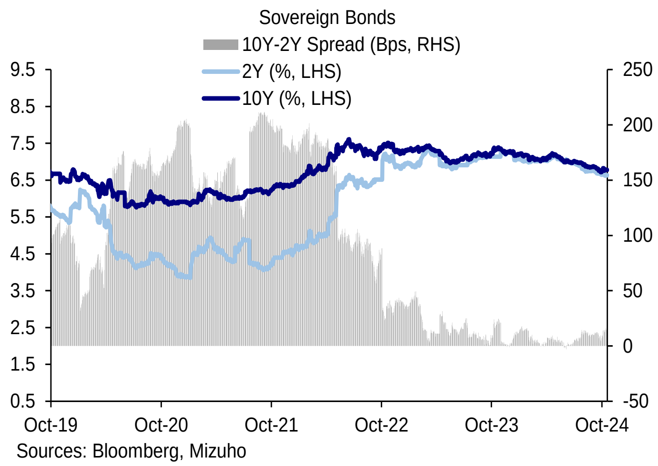
- Policy Rate: In which case, 100-125bp of cuts, premised on dis-inflation being restored after the outburst of food-led inflation, is not unreasonable. Exceptionally elevated real rates in the context of sharp slowdown in growth justify (if not warrant). *Rupee stability* though *will feature prominently as a trade-off in policy calculus.*

- Yields: Whilst expectations of, RBI cuts have been bumped up significantly, this may **not immediately and unequivocally spell softer GOI yields** as *higher UST yields from "Trumpflation" dampen downside in yields.*

- Curve: More so, at the long-end as UST yield curve steepening, while not as yet pronounced, is likely to come through more emphatically into the Fed cut cycle and amid Trumpflation-induced uncertainty.

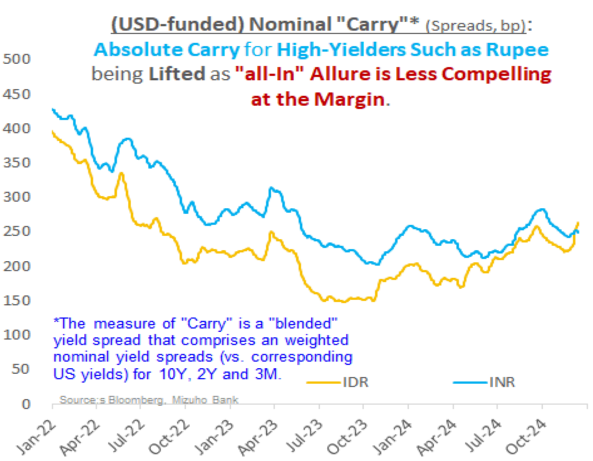
- Wider spreads: What's more, ***even when UST yields decline*** with Fed cuts, (re-)**widening GOI-UST spreads**; may temper GOI yield softening. Especially as a steeper UST yield curve catalyzes a **shift from** *"all-in" returns to risk-adjusted re-pricing.*

Fig 4e. Some Downside in Yields Expected



Sources: Bloomberg, Mizuho

Figure 4f. "Carry" Needs Restoring amid Risk re-pricing



KRW: Politics and Policy Woes

	Q3 2024	Q4 2024	Q1 2025	Q2 2025	Q3 2025	Q4 2025
Policy Rate (%)	3.50%	3.00%	2.75%	2.50%	2.25%	2.25%
USD/KRW	1303-1391	1317-1490	1320-1500	1370-1540	1330-1480	1290-1400
	1314	1455	1438	1442	1385	1345
GDP (% YoY)	1.5	2.0	1.0	1.7	2.2	2.2
CPI (% YoY)	2.1	1.6	1.9	2.2	2.3	2.0

Note: Values in black are historical whereas those in blue represent forecasts. * Point forecast is for end-period. Ranges are only indicative.

Fig 5a. KRW underperformed on political woes

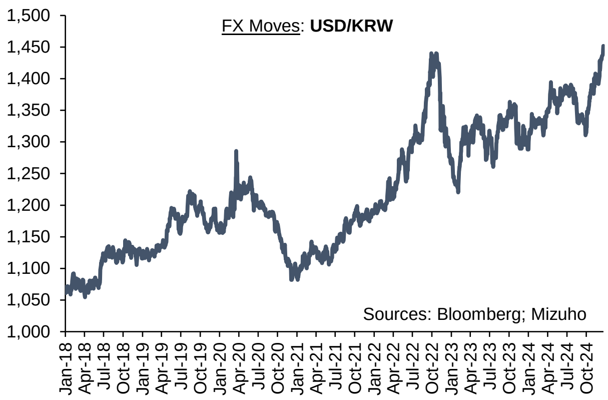
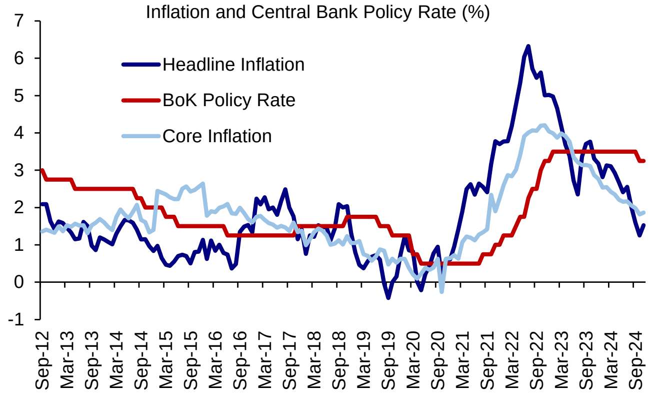
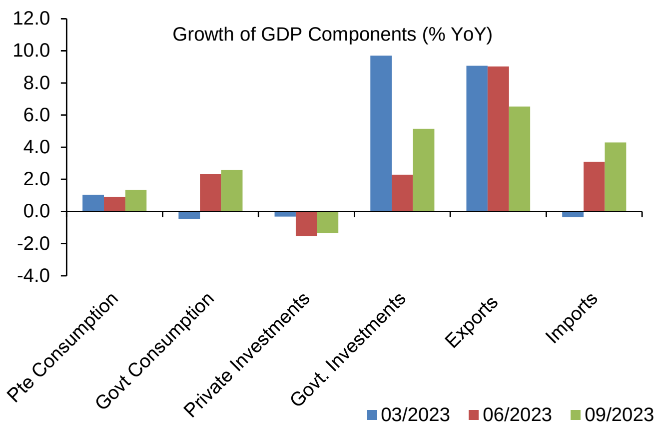


Fig 5b. Headline inflation decline aid BoK easing



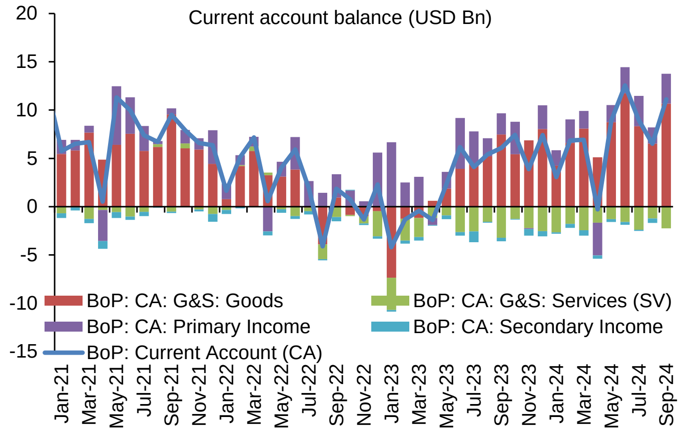
Source: CEIC; Mizuho

Fig 5c. Weaker exports growth engine worries



Sources: CEIC, Mizuho

Fig 5d. September surplus spike due to primary income



Source: CEIC, Mizuho

FX

- KRW faces painful cuts: As expected, amid the higher UST yields which buoyed the Greenback, the KRW continued depreciating with their middle of the pack performance for November as the BoK went ahead with a surprise rate cut. That said, the political risk from President Yoon's martial law led to subsequent KRW underperformance. Furthermore, softer export growth will also worry KRW bulls especially as we head into Trump 2.0. Domestic growth worries also imply that rates may also be less supportive of the KRW into 2025.

- Current Account Spike, Little Joy: Given that the current account spike in September was largely due to an increase in primary income inflows, the durability is in doubt. Furthermore, services deficit widened as charges on intellectual property rights rose alongside imports of other business services. That said, the goods balance improved in September from US$6.5b to US$10.7b to indicate healthy demand levels.

- Softer Growth, Fading Tailwinds: Nonetheless, the sight of moderating exports growth will worry KRW bulls who kept hanging onto hopes of current account surplus translating to durable KRW boost. Specifically, customs data indicate that nominal semiconductor exports growth may have peaked as it moderates from the 52% YoY seen in Q2 to 42% YoY growth in Q3. Admittedly, these are high levels of revenue even if it plateaus but worries of an eroding of comparative advantage from traditional corporate strongholds unlikely to abate.

- Faltering Domestic Conditions: Demand domestically remains weak as private consumption growth averaging 1.1% in the first three quarters of 2024 is far below the 2.8% average seen from 2016-19. Contracting private investment also reflect the downbeat business sentiments. The weaker demand conditions also provided impetuous for BoK easing.

- Political and Policy Risk Premium: President Yoon's martial law episode is imparting a political risk premium as the ruling party plans for his exit and to contain the fallout. Critically, this also implies possible fiscal policy delay as the trimmed budget which was a catalyst behind the debacle will be up for further debate.

- Trump 2.0: US-China tensions will impact Korea's export demand given that China remains their largest market. Furthermore, large current account surplus and the need to keep KRW stable imply that a direct mention of tariffs on Korea remains on the card.

- Balanced flows: Risk off episode continued to worsen foreign outflows from equities though inflows into bonds was a welcomed offset. This dynamic is likely to persist for the months ahead and the risk remain to the downside should the current volatility and liquidity issues threaten their announced inclusion into the WGBI.

- Outlook: Into the year end, KRW is unlikely to shake off its underperformance to recover below 1400 among regional peers as political, policy and growth woes mount. A return to sub-1400 in Q1 is premised on a return to political normalcy with the fiscal budget approved. Nonetheless, with the BoK increasingly concerned on growth, the extent of recovery is restrained. Furthermore, Trump 2.0 risks represent sharp KRW depreciation risks as executive orders signed in Q1 imply that Korea is unlikely to escape being embroil in trade tensions.

Rates

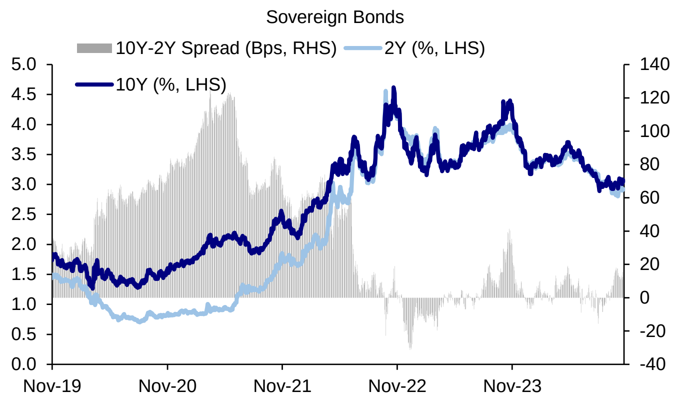
- Central Bank: Our expected easing in Q1 was brought forward by the BoK who were concerned about slowing growth and no longer deterred by the housing prices in Seoul which showed a slowing momentum in recent weeks. We continue to see prospects of another cut in Q1 as growth is likely to remain weak and the need to lean against trade headwinds grow. Rate cut pace is expected to remain steady in 2025 as authorities remain watchful of KRW pressures and a resurgence in property prices.

- Risks: Despite political woes, the risk may be externally driven as a direct hit from Trump 2.0 may see the BoK front load rate cuts in Q1.

- Yields: Even as front-end yields fall, 10-2Y spreads have been compressed to less than 10bps in December driven by UST yield movement. Front end yields continue to face downside risks from BoK easing, the political episode has diminished the allure of KRW assets and lifts yields across the curve by widening the risk premium. Any further threat to their WGBI inclusion may cause yields to rise more.

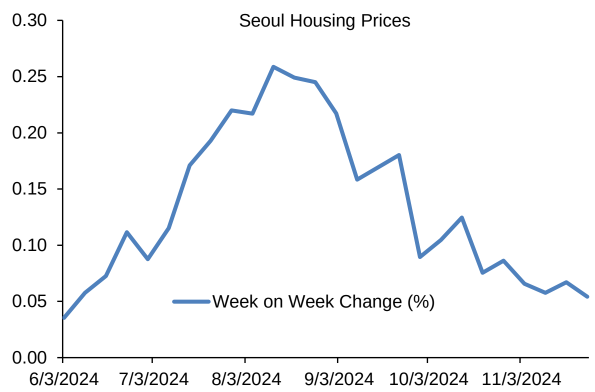
- Curve: Steepening prospects may elude in the very near term into the year end on UST movements though it remains the structurally attractive proposition considering the fiscal and demographic issues which would widen the term premium.

Fig 5e. Term premium compresson worsen



Sources: Bloomberg, Mizuho

Figure 5f. Softer housing price momentum allow easing



Sources: CEIC, Mizuho

TWD: Defensive

	Q3 2024	Q4 2024	Q1 2025	Q2 2025	Q3 2025	Q4 2025
Policy Rate (%)	2.000	2.000	2.000	1.875	1.750	1.750
USD/TWD	31.5-32.9	31.6-33.1	31.8-34.5	32.1-34.5	31.5-33.9	31.2-33.5
	31.7	32.4	32.8	33.1	32.5	32.2
GDP (% YoY)	4.2	3.2	2.7	3.2	3.2	3.0
CPI (% YoY)	2.2	2.3	2.0	1.9	2.0	1.8

Note: Values in black are historical whereas those in blue represent forecasts. * Point forecast is for end-period. Ranges are only indicative.

Fig 6a. TWD remains in a defensive mode

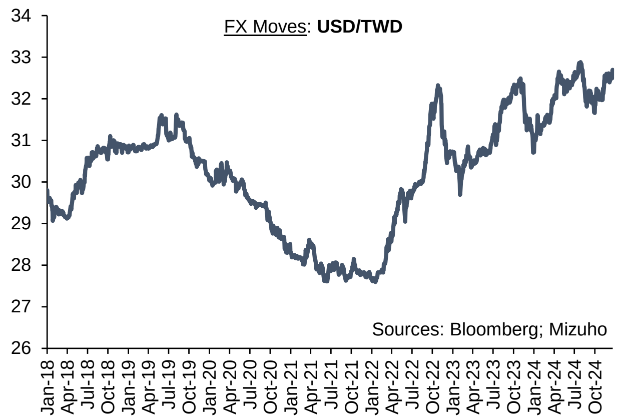
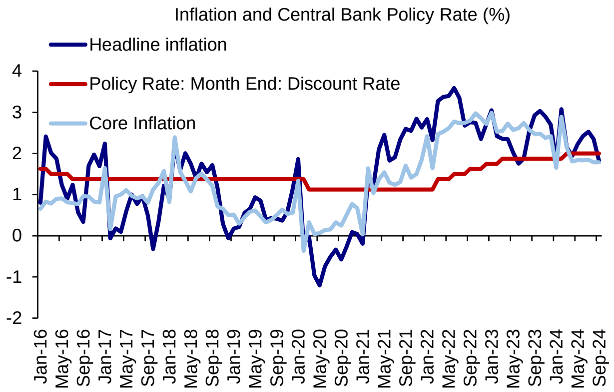
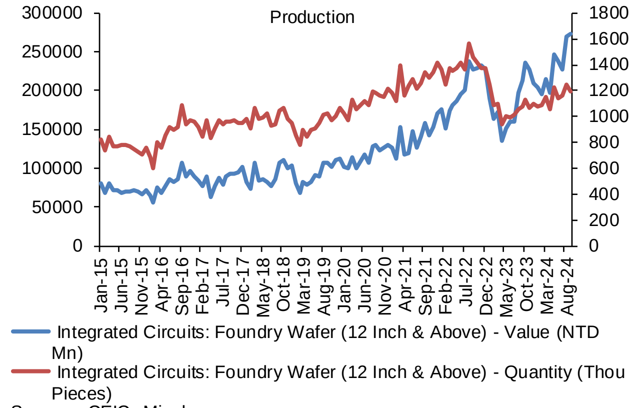


Fig 6b. Core inflation sticky, weather hit headline



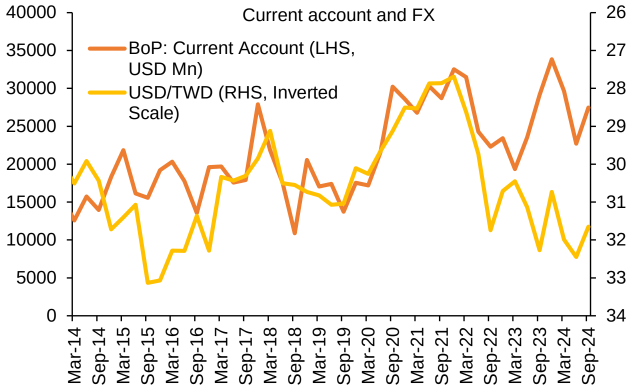
Sources:CEIC, Mizuho

Fig 6c. Semiconductor demand remains strong



Sources: CEIC, Mizuho

Fig 6d. Current account surplus not a firm backstop



Source: CEIC; Mizuho

FX

- Moderate performance: Since the US election day, TWD has depreciated from 31.9 to around 32.7 level. The TWD depreciation coincided with intensifying Taiwan equities outflows and declines in Taiwan stock markets. That said, the milder net effect relative to peers is likely a reflect of CBC's defensive intervention efforts, rate stance and still resilient economic outlook. So far, investors have adopted a wait-and-see mode on the development of geopolitical tensions, given a possible shift of US stance on Taiwan under Trump's presidency.

- Currency manipulation concerns: The new Trump 2.0 administration implies higher risk of US Treasury labelling Taiwan as a currency manipulator. Since June 2022, Taiwan has been on the FX monitoring list due to its current account surplus (14.7% of GDP) and huge trade surplus with the US (USD 57bn, 4 quarter moving average). The Trump administration may also leverage the currency manipulator issue as a negotiation tool to address US-Taiwan trade imbalances and the relocation of chips production.

- Engulfed in trade conflicts: Considering Taiwan heavily reliance on exports to the China/HK region (~ 30%) and US (~20%), any escalation in trade tensions with these key partners could dent Taiwan exports growth.

- Alongside Cross-straits concerns being 'live': On that note, with previous episodes of President Trump citing the need for Taiwan to make defence payments, it is not unforeseeable that in the US-China negotiation front, defence and sovereignty acknowledgments are on the table. Consequently, this puts the TWD on a defensive mode subject to abrupt depreciation risks.

- Allure of semiconductor retained: TWD remains backstopped by semiconductor demand as production levels remain elevated with potential to rise further. The widening gap between quantity and value of production indicate that prices remain high in a reflection of the robust demand.

- Buoyed Current Account remains a backstop: The Q3 current account surplus uptick reflect strong exports revenue. While this underpins the TWD fundamentally, it does not present itself as a cause for TWD rallies.

- Especially as financial flows weigh: While electronic demand remain solid, valuation concerns surround equities and AI related sectors have not abated. In turn, outflows from Taiwan equities intensified in November amounting to US$8.7 billion and the durability to reversal to inflow in early December remain in doubt.

- Inflation a setback for TWD bears: Sticky core inflation and bumpy headline inflation delay any near term policy normalisation hopes which sets back outright bearish bets on the TWD.

- TWD outlook: Into early 2025, TWD is vulnerable to various trade related under Trump 2.0 may spark sharp depreciation episodes to above 34 levels though we expect such episodes to be brief as the CBC to act and contain such knee jerk reactions. That said, **any defence related changes from Trump 2.0 have the potential to turn existential and may have a more durable hit on the TWD**. Meanwhile, risk off episodes surrounding the AI boom and semi-conductor cycle could increase foreign equity outflow pressure. While the new FX volatility reserve mechanism could reduce FX-hedging support among lifers, the FX reserve-rich central bank could smooth out TWD volatilities. We expect the TWD to weaken further, possibly surpassing the 33 level before recovering in H2-2025.

Rates

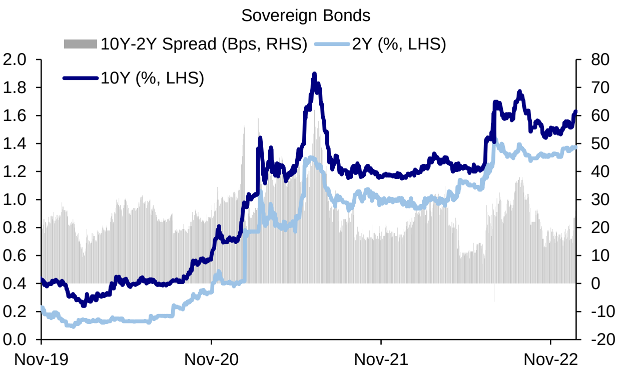
- Central Bank: Even as housing prices show signs of stabilising, it is still premature for the CBC to begin policy normalisation especially as inflation remains elevated even though most of the headline inflation increase was due to the Typhoon in October and December. The CBC will also want to avert the situation of re-igniting the housing market. We hold onto our view of a calibrated rate cut in Q2 as the external demand support on growth may begin to level off.

- Risks: Possibility of a further hike has been diminished and the risks are now skewed towards an earlier than expected rate cut should Trump 2.0 dampened global trade flows.

- Yields: As expected, the decline in yields has been relatively milder compared to regional peers as backed by expectations that the CBC will embark on a prolonged hold.

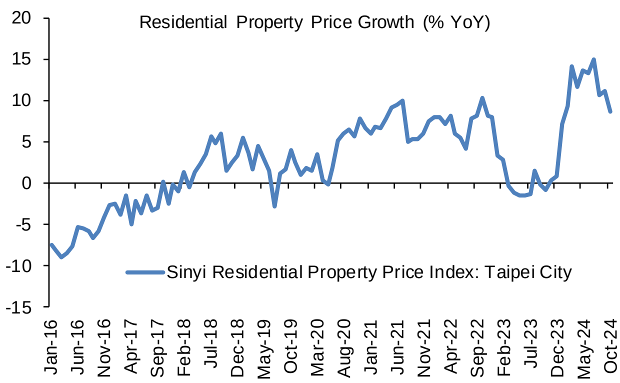
- Curve: Reflecting the narrow room for a smaller term premium, the 10-2Y spread is essentially similar to that compared to late October. Movements will defer to wider UST trends with steepening on the cards but the follow through will be a milder one in Taiwan as rate cut continue to elude.

Fig 6e. Decline in yields are relatively milder



Sources: Bloomberg, Mizuho

Figure 6f. Slower price momentum a marginal relief



Sources:CEIC, Mizuho

SGD: Tariff Shelter?

	Q3 2024	Q4 2024	Q1 2025	Q2 2025	Q3 2025	Q4 2025
S$NEER Slope	2.0%	2.0%	2.0%	2.0%	1.5%	1.5%
S$NEER Mid-pt	Hold	Hold	Hold	Hold	-65bp	Hold
USD/SGD	1.278-1.359	1.283-1.368	1.327-1.376	1.330-1.388	1.315-1.375	1.292-1.344
	1.285	1.359	1.363	1.371	1.335	1.318
GDP (% YoY)	5.4	2.3	2.3	2.4	2.3	2.1
CPI (% YoY)	2.2	1.8	2.1	2.0	2.1	2.2

Note: Values in black are historical whereas those in blue represent forecasts. * Point forecast is for end-period. Ranges are only indicative.

Fig 7a. SGD has been an outperformer

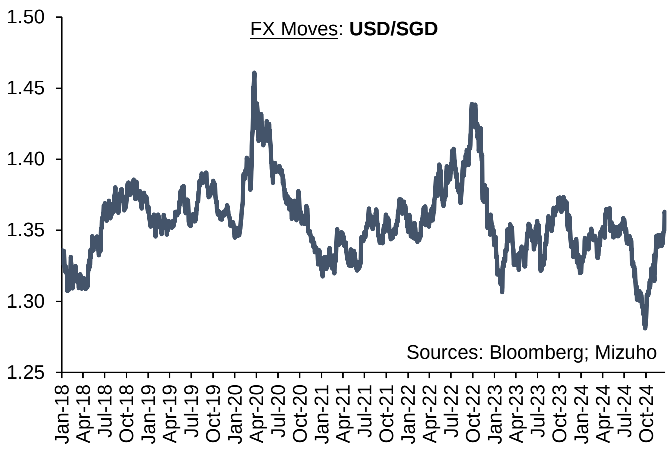


Fig 7b. Declining Core Inflation

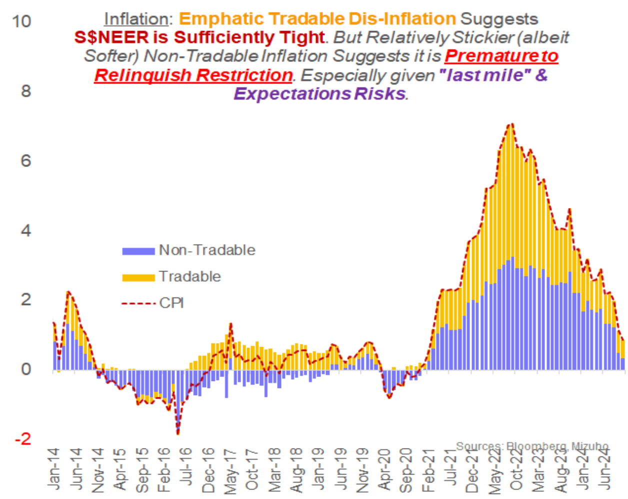


Fig 7c. Exceptional S$NEER Surge

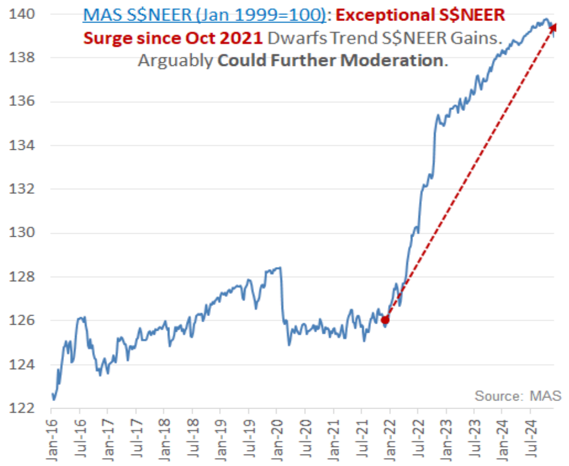
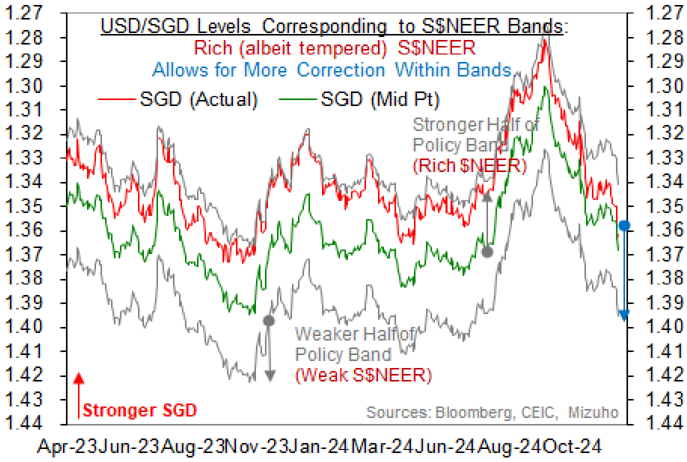


Fig 7d. Scope to Correct Further Within the Band



FX

- Stretched Outperformance: Remarkable Tariff Shelter: The SGD is endowed with unique trade attributes that renders it a relative (USD-neutral) refuge from US tariff disruptions. Notably, its bilateral trade deficit with the US despite its overall trade and current account surplus.

- Bilateral Buffer: This goods deficit against the US is an uncharacteristic feature in the AXJ space that buffers SGD from direct US trade antagonism. Coupled with a broader, significant external surplus, the SGD derives quasi-haven allure.

- Relative Stability: In turn, the relative SGD stability amidst potential turbulence on escalating tariff antagonism, or even just uncertainty, is notable.

- Outperformance Still Constrained: But this is more a predisposition for opportunistic edge than it is preordained outperformance of the SGD. In fact, our view of fading SGD outperformance (from the last edition) is predominantly unchanged.

- Collateral Damage Risk: For one, and most glaring, broader negative global trade impact is bound to inevitably hurt an economy as open (and as trade-reliant) as Singapore's via supply-chain and financial channels. In other words, mitigated bilateral trade conflict risks do not adequately negate collateral trade risks. Notably, significant CNY weight in the S$NEER also compromises SGD buffer via S$NEER policy parameters.

- MAS Easing Bias: Speaking of policy, the runway of exceptional and unprecedented S$NEER strength from record MAS tightening is now exhausted. On the contrary, the case for S$NEER easing so as to soften levels suggests SGD depreciation risks in the offing of the MAS loosens policy.

- Rich S$NEER: Moreover, the S$NEER remains rich. Despite easing back from the top side of the policy bands, it is still in the top half. And so this gives scope for the S$NEER to soften within existing policy bands even in the absence of any overt policy shifts.

Rates

- Central Bank: Whilst the MAS has held steady (in Oct) citing appropriate stance given the balance of risks, the **shifts in risk dynamics are increasingly tilted to the downside**. And *impending Trump 2.0 tariffs* with *only accentuate uncertainty*. Moreover, **inflation is still set to recede** durably, ***even if bumpily***. Hence, the **incentive to ease policy restrictions** is markedly increased. What's more, with inherited policy exceptionally tight, **easing to appropriately temper S$NEER restriction may be just a matter of time**.

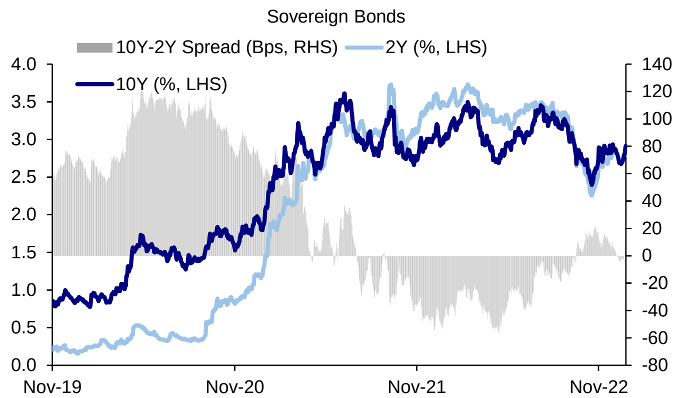
- Price-Taker with "Premium Nudge": In theory, given the choice of FX-based (S$NEER) policy, the **MAS tools do not set out to directly influence rates**. Instead, the **MAS**, is by and large a **price taker of global (mostly US) rates**. That said, the *MAS may indirectly influence SGD rate premium vis-à-vis US rates*.

- Reining in "SGD Premium": To that end, impending easing may **rein in the "SGD premium"**. Specifically, partially reversing lower SGD rates vis-à-vis corresponding US rates. In other words, undershoot SGS yields rates vis-à-vis UST yields may prove excessive once relative policy shifts and wider global risk premium are incorporated. This is over and above reversion of UST-SGS spreads.

- Yields (following USTs Lower): Nonetheless, regardless of scope for relative SGS yields catch-up (with UST yields), the **broader direction of travel in SGS yields** will be dictated by **UST yields**. As such, it will be **prone to greater volatility** amid tensions between Trump-flation driven upside later supplanted Fed cut drag.

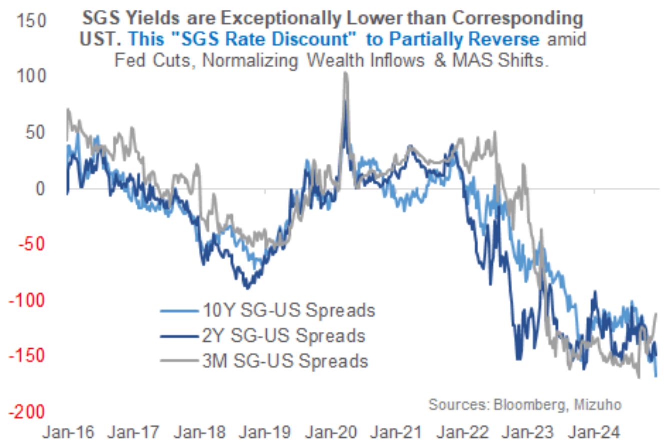
- Curve: Moreover, **SGS yield curve is also set to steepen** in tandem with a steeper UST yield curve.

Fig 7e. Price-Taker of UST Shifts



Sources: Bloomberg, Mizuho

Figure 7d. Discount Appears Excessive amid Risks



IDR: Rupiah Woes Persist

	Q3 2024	Q4 2024	Q1 2025	Q2 2025	Q3 2025	Q4 2025
Policy Rate (%)	6.00%	6.00%	6.00%	5.75%	5.50%	5.25%
USD/IDR	15070-16400	15170-16350	15690-16380	15900-16480	15100-16380	14710-15810
	15140	16150	16250	16300	15650	15200
GDP (% YoY)	4.9%	5.1%	5.0%	4.9%	5.2%	5.4%
CPI (% YoY)	2.0%	1.7%	2.0%	2.1%	2.9%	2.9%

Note: Values in black are historical whereas those in blue represent forecasts. * Point forecast is for end-period. Ranges are only indicative.

Fig 8a. Fed-induced IDR volatility

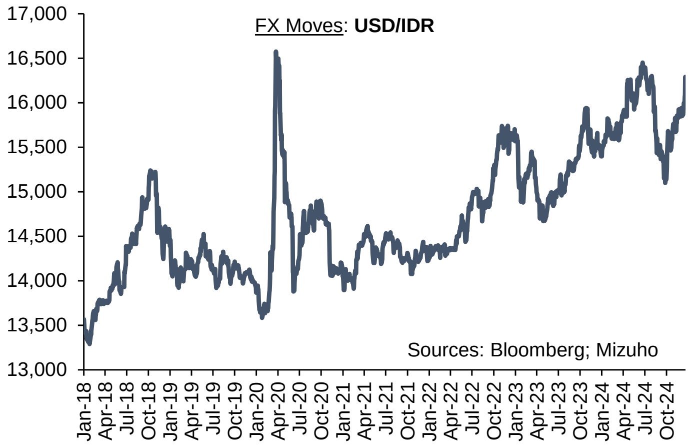
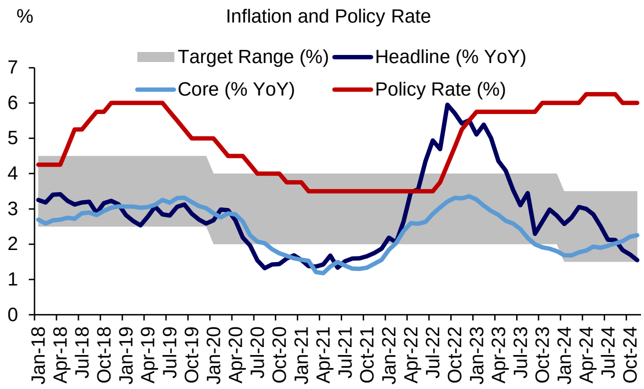
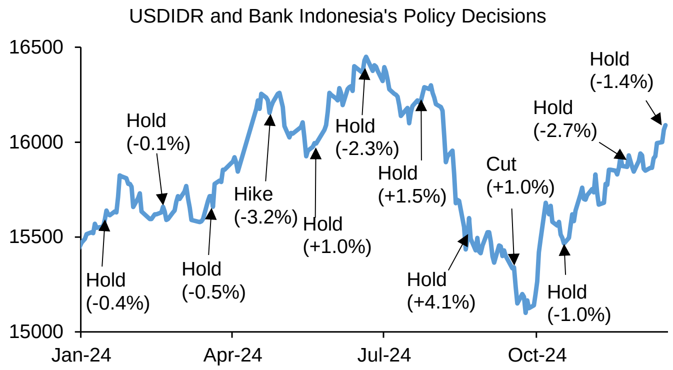


Fig 8b. Inflation remains stable



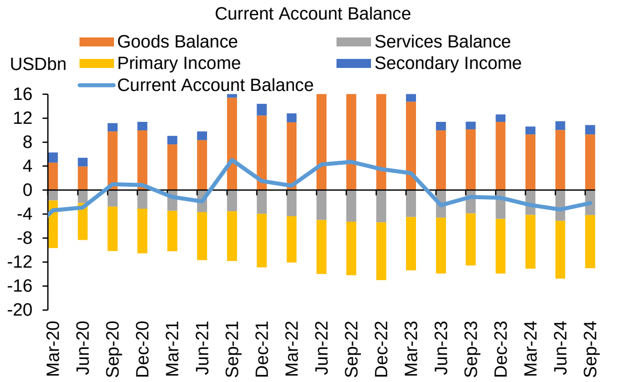
Sources: CEIC; Mizuho

Figure 8c. BI's concerned over rupiah stability



Note: Parantheses indicate IDR appreciation(+)/depreciation(-) against USD since previous meeting.
Sources: Bloomberg; Mizuho

Fig 8d. Current account deficit narrowed slightly in Q3



Source: CEIC; Mizuho Bank

FX

- Fed-induced FX volatility: Amid US-elections induced volatility and adjustment to Fed rate cut expectations, USD/IDR moved above mid-15,000 and remains languishing at levels slightly below 16,000 in October through mid-November. Notably, the surge in USD strength in the lead-up to FOMC saw Bank Indonesia intervening into FX markets, and even characterised its interventions as "quite bold". Following FOMC, BI emphasised that it would guard the IDR "strongly" as USD/IDR breached 16,200 levels.

- Reforms may relief short-term woes; but long-term fiscal woes remain: Developments on fiscal reforms have not provided much support to the IDR, and there is basis for such circumspection. On 15 Nov, the Energy Minister said that the government is finalising a policy review that includes an option to replace its current subsidies for gasoline, diesel and other transportation fuels with cash-handouts for poor citizens. Nonetheless, there have been no further updates till-date. For reference, Indonesia's subsidy reform has a checkered history. Successful attempts feature social assistance to the poor, strong political leadership and communication campaigns, but efficiency of reforms could be mitigated by volatility in the oil and currency markets.

- Meanwhile, Prabowo's cabinet added a Tax Amnesty law revision to its list of priority bills for 2025, which could potentially boost coffers and expand the tax base. But even if the Tax Amnesty program helps to achieve the 2025 fiscal deficit target, questions for future years remain given massive spending plans. All in, fiscal woes will continue to cast an overhang on IDR as risks to fiscal outlook remain tilted to the downside.

- Political risk premium: Prabowo's bloated cabinet raises risk of inefficacious policymaking and policy implementation. But some political uncertainty should have subsided with the conclusion of local elections. Notably, opposition candidate, former cabinet secretary Pramono Anung, was elected as the Jakarta governor role, even as Prabowo's party Gerindra made significant gains in gubernatorial races.

- Modest Growth Support: Growth moderated slightly to 4.9% in Q3 (Q2: 5.0%) on a weaker external sector. Domestic consumption warrants closer monitoring as it registered a QoQ contraction.

- Stable Inflation: Headline inflation remains stable (Oct: 1.7%; Nov: 1.6%), remaining within the bottom-half of BI's 2.5±1% target range. Nonetheless, core inflation edged higher (Oct: 2.2%; Nov: 2.3%) from 2.1% in September. Inflation looks to remain stable for the rest of the year. While upside risks are present in 2025 on VAT hike and amid developments of subsidy reform and possible demand-led inflation on greater infrastructure spending, overall inflation should remain within BI's inflation target range.

- Financial Flows: Indonesia saw net equity and bond outflows in month of November.

- IDR Outlook: BI's interventions likely to backstop weakness at ~16,000 levels. A bloated administration which has much to prove on its fiscal prudence, some signs of slowing domestic consumption would continue to cast an overhang on IDR.

Rates

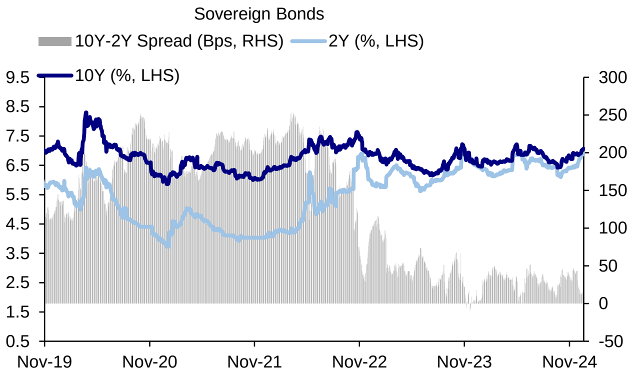
- Staggered Easing: Bank Indonesia stood pat for the two meetings after its first cut in September, as expected, citing concerns over IDR stability. Notably, BI's outlook on FFR trajectory was more uncertain. BI also expressed that even as there was still room for easing, the room was more limited. We are expecting another hold at the December meeting, given that nothing material has changed since the last meeting and IDR remains languishing near 16,000 levels.

- Risks to Slower Easing: Risks remain tilted towards Bank Indonesia easing slower than expected as USD takes time to stabilise as Trump's policies and Fed policy trajectory becomes clearer with December Dot Plot.

- Yields: Yields have broadly climbed higher. 2Y yields in November are on average 13.6bps higher compared to October average, while 10Y yields in November are on average 14.4bps higher compared to October average.

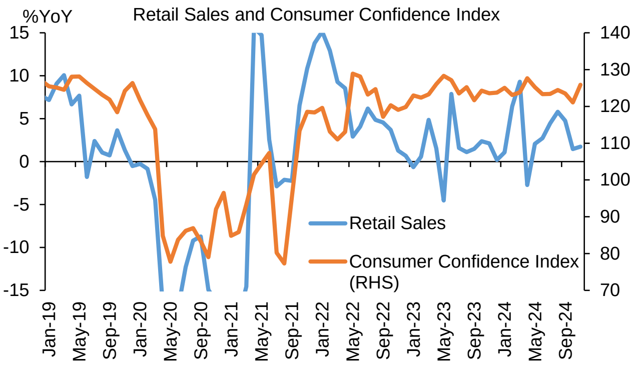
- Curve: Steepening bias to curve amid supply dynamics and fiscal outlook. In addition, a slower pace of easing which could support front-end yields more.

Fig 8e. Term Spread low by historical standards



Sources: Bloomberg, Mizuho

Fig 8f. Oscillations in retail sales



Source: CEIC; Mizuho

MYR: External Risks Dominate

	Q3 2024	Q4 2024	Q1 2025	Q2 2025	Q3 2025	Q4 2025
Policy Rate (%)	3.00%	3.00%	3.00%	3.00%	3.00%	3.00%
USD/MYR	4.09 – 4.72	4.12 – 4.58	4.29 – 4.65	4.27 – 4.67	4.13 – 4.55	3.99 – 4.36
	4.12	4.51	4.53	4.53	4.30	4.12
GDP (% YoY)	5.3%	4.4%	5.6%	4.3%	4.5%	5.4%
CPI (% YoY)	2.0%	2.0%	2.1%	2.2%	2.3%	2.3%

Note: Values in black are historical whereas those in blue represent forecasts. * Point forecast is for end-period. Ranges are only indicative.

Fig 9a. MYR's still a regional outperformer

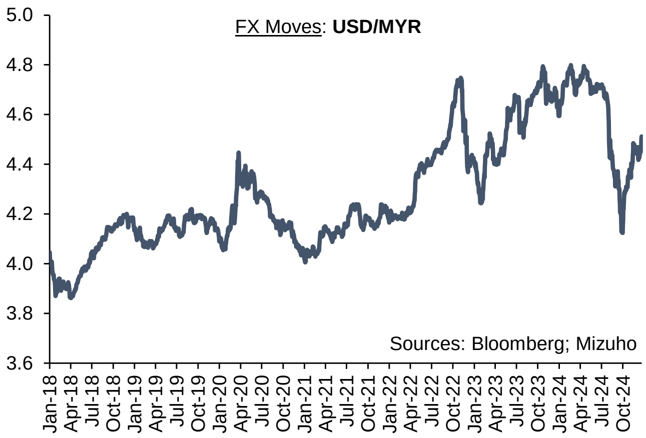
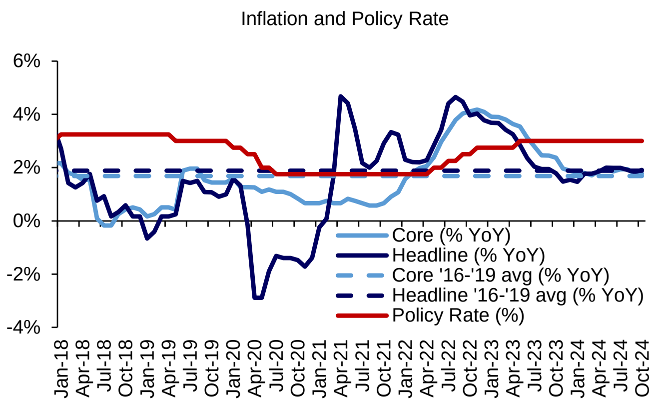
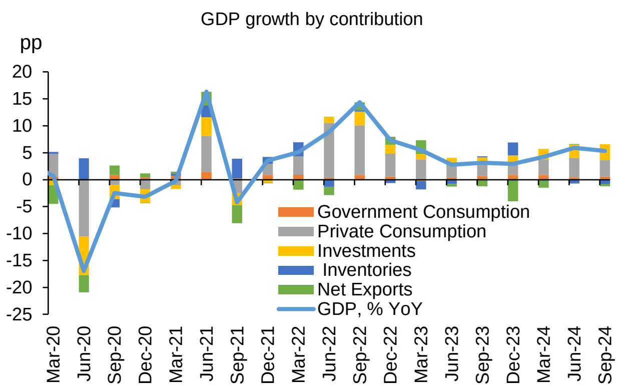


Fig 9b. Inflation remains stable



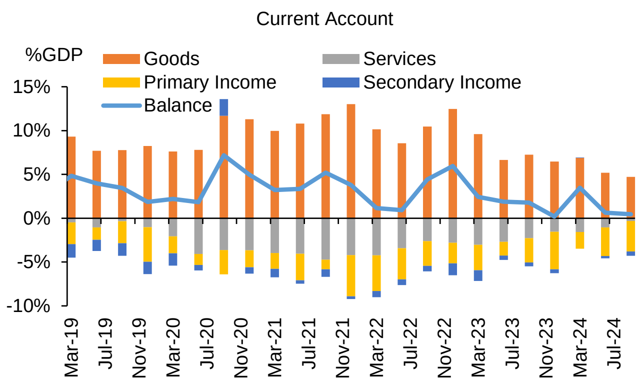
Source: CEIC; Mizuho

Fig 9c. Growth remains resilient



Source: CEIC; Mizuho

Fig 9d. Current Account surplus narrowed slightly in Q3



Source: CEIC; Mizuho Bank

FX

- FX Outperformer: Despite MYR's underperformance in recent weeks, it remains the only currency regionally that has gained against the greenback on a YTD basis. The present underperformance could be due to higher sensitivities of the currency to UST yields, given that BNM's prolonged hold leaves external forces a more dominant driver of MYR moves, in addition to suffering from collateral damage from adverse US-China trade conflict fallout, given Malaysia's position along the supply chains.

- Resilient Growth: Growth should remain constructive for the MYR. There were no revisions to Q3's 5.3% YoY growth. From a demand perspective, growth was supported by an acceleration in government spending and investments. Household spending moderated YoY but was still an expansion on a NSA QoQ basis. Growth in goods exports was offset by a higher acceleration in goods imports. From a production perspective, manufacturing activity growth accelerated less compared to advance estimate, which was offset by agriculture and construction activity performing better-than-expected. Services activity was in-line with expectations. Looking ahead however, there are some downside risks to Q4 growth on bad weather and impact of floods.

- Semiconductor Tailwinds: Malaysia should continue enjoying semiconductor tailwinds going into 2025, although growth could see a sharp moderation in part due to high base effects.

- Collateral Damage from Trump 2.0 Tariffs: MYR may see higher delta to escalation in US-China tensions as it is at higher risk to suffer damage from Trump 2.0 tariffs given heightened sensitivities from trade dependence (via supply-chain, and upstream commodities impact) accentuated by wider investment and financial flows.

- Stable Inflation: Inflation edged up slightly in October, with headline printing at 1.9% (Sep: 1.8%), on the back of faster price increases on food away from home. Nonetheless, inflation in November and December could edge up amid disruption caused by the floods, but not expected to be outsized.

- Current Account: Q3 current account surplus printed at 0.4% of GDP, a further narrowing from Q2: 0.6% (Q1: 3.5%) as primary income outflows widened while goods surplus narrowed. In Q4, current account balance may remain lacklustre as higher palm oil prices are in part due to poorer Malaysia harvests amid adverse weather conditions.

- Financial Flows: There were net equity outflows in November, and likely to have seen net bond outflows as well as MGS has been selling off.

- MYR Outlook: MYR looks to continue to see heightened volatility in coming weeks on external developments and should retain buoyancy above 4.40 levels.

Rates

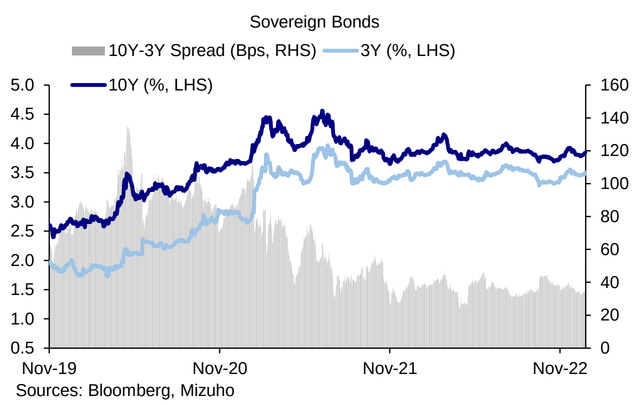
- BNM's Steady Hands: BNM stood pat at the 6 November meeting. The meeting was a non-event given expectations of a prolonged hold by BNM amid supportive growth and managed inflation. The statement retained the wording that monetary policy stance remains "supportive" of the economy and is consistent with the current assessment of inflation and growth prospects. We retain our view of a prolonged hold by BNM.

- Risks: Risks are tilted to a 25bps cut in late 2025 or even 2026 should domestic consumption shows signs of cracks and electronics cycle tailwinds fade. Notably, resilient domestic consumption is in part due to massive EPF withdrawals; and may not be that sustainable in the long-term.

- Higher Yields: Amid volatility in US yields, government bonds have sold-off. 3Y yields are on average 7.9bps higher in November compared to October, while 10Y yields are on average 7.1bps higher. Accordingly, term spreads have narrowed slightly.

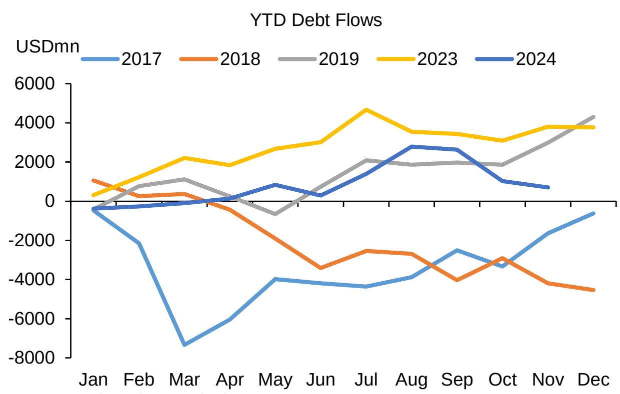
- Curve: BNM anchor should see term spreads stabilising.

Fig 9e. Yields stable amid BNM's continued hold



Sources: Bloomberg, Mizuho

Figure 9f. Nov saw net debt outflows



Sources: Bloomberg; Mizuho

PHP: Mounting Growth Risks

	Q3 2024	Q4 2024	Q1 2025	Q2 2025	Q3 2025	Q4 2025
Policy Rate (%)	6.25%	5.75%	5.50%	4.75%	4.50%	4.25%
USD/PHP	55.4 - 58.9	56.0 - 59.6	56.6 - 60.2	57.1 – 60.5	55.9 - 59.8	54.7 – 58.2
	56.0	58.9	59.5	59.6	57.2	56.5
GDP (% YoY)	5.2%	5.8%	5.7%	6.8%	5.6%	5.4%
CPI (% YoY)	3.2%	2.6%	2.9%	3.3%	3.2%	3.3%

Note: Values in black are historical whereas those in blue represent forecasts. * Point forecast is for end-period. Ranges are only indicative.

Fig 10a. PHP has been flirting with 59 handle

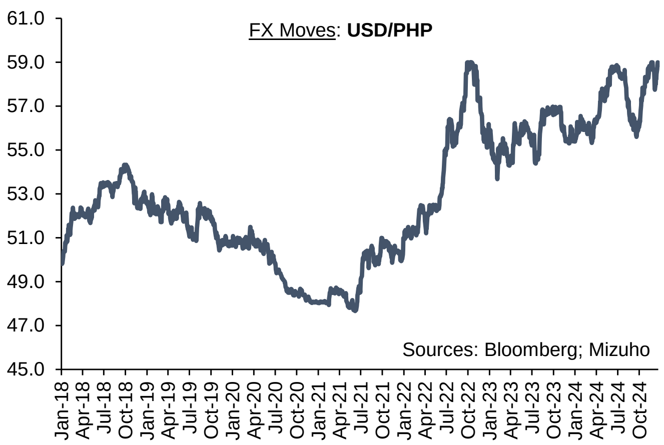
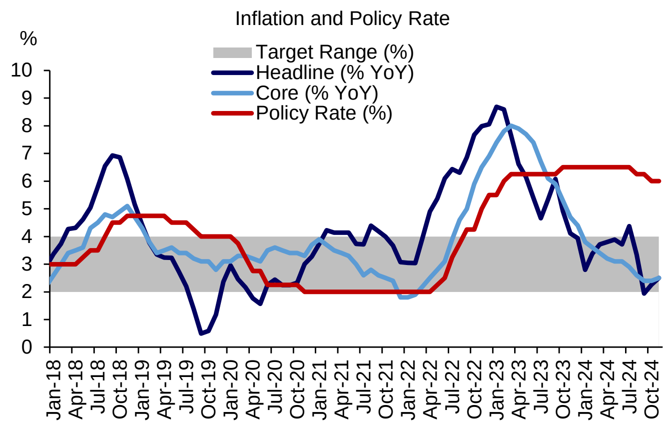
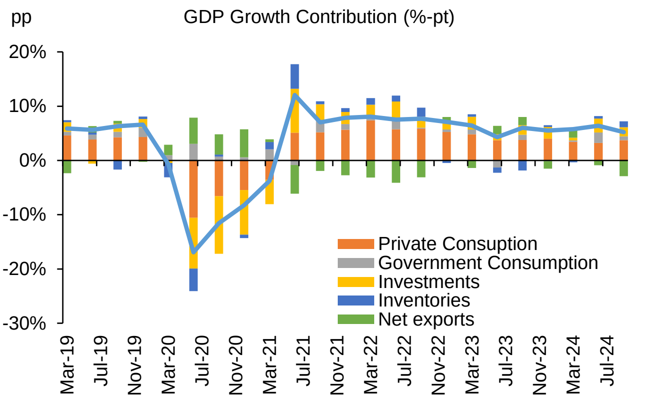


Fig 10b. Inflation remains within target band



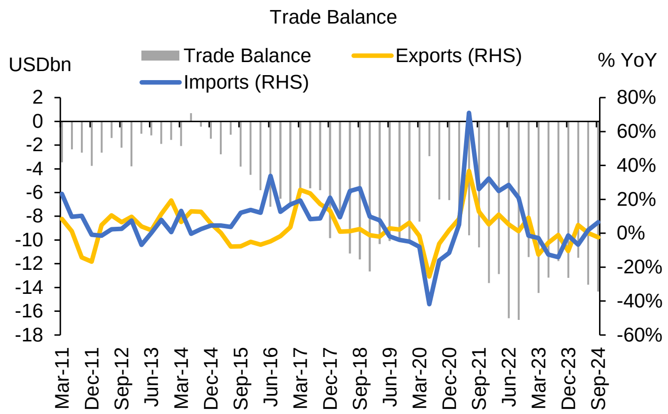
Source: CEIC; Mizuho

Fig 10c. Growth moderated in Q3



Source: CEIC; Mizuho

Fig 10d. Trade balance deteriorated in Q3



Sources: CEIC; Mizuho

FX

- Backstopped by Interventions: USD/PHP has been flirting with the 59 levels in recent weeks. BSP has confirmed that it is intervening in the FX market, albeit in "small amounts". Nonetheless, BSP Governor Remolona had remarked in late November that USD/PHP could move to 60 levels, which may suggest that authorities are backstopping PHP weakness at a higher level.

- Fiscal Risks Abound: Budget 2025 spending of PHP6.352tn was approved by the Senate on 26 November. Our view remains that fiscal slippages risk are present and would weigh on Philippines "twin deficit vulnerabilities".

- Mounting Growth Risks: Philippines' growth for 2024 looks likely to miss the 6% target. Q3's growth printed at 5.2% YoY, a sharp moderation from Q2 (6.4%) on the back of moderating government consumption and deteriorating external sector. With continued bad weather in the Philippines, outlook for Q4 is tilted to the downside. In addition, despite household consumption expanding by 3.2% on a QoQ basis in Q3 after two consecutive QoQ contraction, we remain downbeat on the outlook of household spending given contracting e-commerce sales in 2025 (Q4 could still some reprieve on spending for the Christmas holidays). The factors above would weigh on growth even as investments could continue to be supported (average YoY growth in past 4 quarters: 7.4% YoY) amid incentives to attract FDI.

- Inflation-in-check: Inflation edged higher to 2.3% in October (Sep: 1.9%) on a re-acceleration in food prices amid bad weather conditions in that month. Upside risks persist for November given continued bad weather, but should remain within the lower-half of BSP's 2-4% inflation target.

- Current Account: Q3 current account deficit could narrow slightly from Q2 (-4.6% of GDP) on slightly better trade balances while remittances remained stable. Sharp moderation of remittances in October, coupled with bad weather which could necessitate more imports, would likely see a widening of current account in Q4.

- Political Tensions: Political tensions rising to a boiling point with Vice President Sara Duterte threatening to assassinate President Marcos Jr. in the event she was killed, and a subsequent impeachment case filed against Duterte. Rising political tensions will add an overhang to PHP in the lead-up to the mid-term elections in May 2025, which increasingly looks to be a proxy battle between the Marcos' and Duterte's dynasties.

- PHP Outlook: Amid BSP's interventions, PHP unlikely to see durable traction above 60 levels. Nonetheless, any PHP rally likely to be shortlived amid political woes, growth concerns and twin deficit vulnerabilities.

Rates

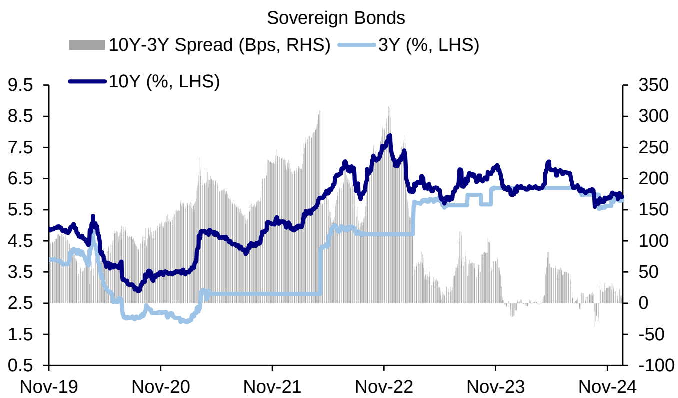
- Central Bank: The decision on 19 December appears open for now as BSP awaits more data. Governor Remolona had said on 20 November that weak economic growth may cause BSP to cut key rates, but BSP may also pause if there's an indication of inflationary pressures. At this juncture, given our view of mounting growth risks and that November inflation (published early-December) should remain in the lower-half of BSP's 2-4% target range, we expect BSP to proceed with another 25bps cut.

- Risks: Risks tilted towards a cut amid mounting growth risks. PHP weakness may not feature as strongly insofar as the passthrough to inflation remains limited.

- Yields: Yields have broadly sold-off as UST yields climbed; but BSP's continued easing has seen the yield curve steepening. 3Y yields are on average 3.5bps higher in November compared to October, while 10Y yields are 14.9bps higher on average in November compared to October. Relatedly, S&P upgraded Philippines outlook to Positive (from stable) on 26 November, although the rating remained at 'BBB+', a notch a Fitch's rating of 'BBB' and Moody's rating of 'Baa2'. While the upgrade is encouraging, we do not expect any imminent ratings upgrade by S&P as we expect continued slow pace of fiscal consolidation, while risks are towards current account narrowing less-than-expected.

- Curve: Yield curve looks to continue steepening as BSP continues easing, in addition to supply dynamics pushing long-end yields higher.

Fig 10e. The term premium is compressed



Sources: Bloomberg, Mizuho

Figure 10f. Credit Rating of Philippines vs Peers

	S&P	Fitch	Moody's	
AAA	SG, AU	SG, AU	SG, AU	Aaa
AA+	TW			Aa1
AA	KR	TW	KR	Aa2
AA-		KR	TW	Aa3
A+	CH	CH	CH	A1
A				A2
A-	MY		MY	A3
BBB+	TH, PH	TH, MY	TH	Baa1
BBB	ID	PH, ID	PH, ID	Baa2
BBB-	IN	IN	IN	Baa3
BB+	VN	VN		Ba1
BB			VN	Ba2

(blue)	Investment Grade
(grey)	Non-investment Grade ("Junk")

THB: Independence Woes

	Q3 2024	Q4 2024	Q1 2025	Q2 2025	Q3 2025	Q4 2025
Policy Rate (%)	2.50%	2.25%	2.00%	1.75%	1.75%	1.75%
USD/THB	33.2 - 35.9	32.3 - 35.3	32.9 - 35.9	33.8 - 36.2	33.4 - 35.7	32.7 - 34.9
	34.2	34.5	34.8	35.2	34.3	33.6
GDP (% YoY)	3.0%	4.0%	3.2%	2.8%	2.9%	2.0%
CPI (% YoY)	0.6%	1.0%	1.4%	1.6%	1.7%	1.5%

Note: Values in black are historical whereas those in blue represent forecasts. * Point forecast is for end-period. Ranges are only indicative.

Fig 11a. THB gave up some gains in November

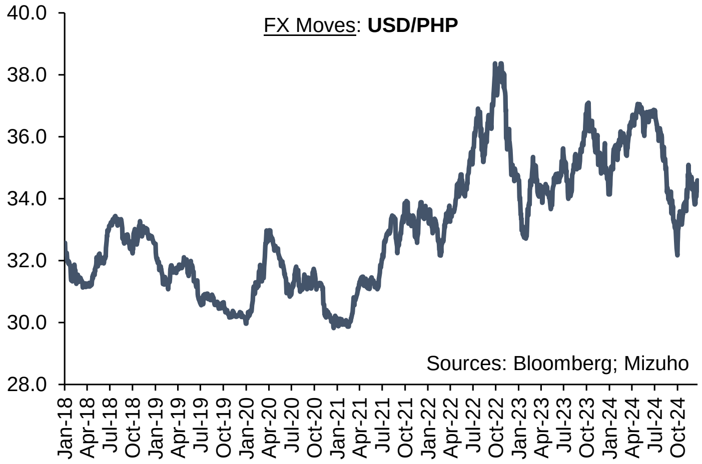


Fig 11b. BoT wary of credit conditions

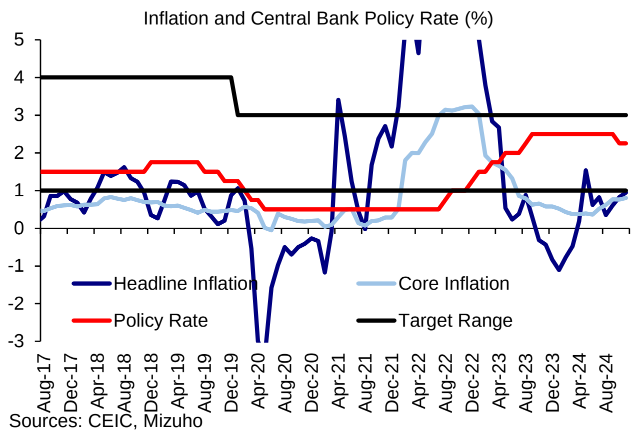
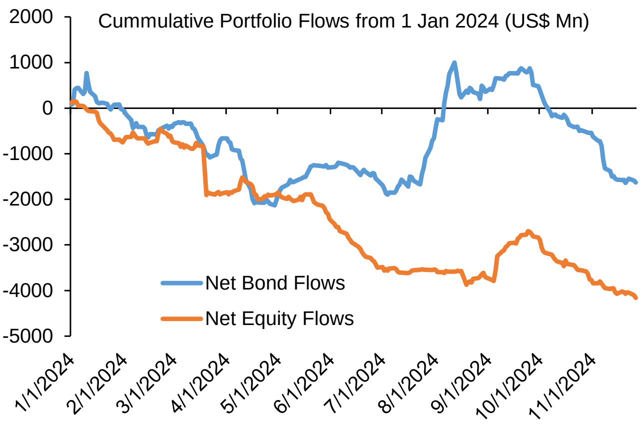
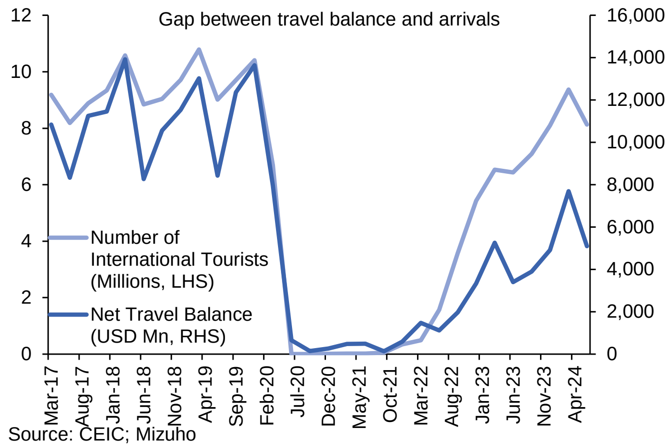


Fig 11c. Foregin outflows continued



Source: Bloomberg; Mizuho

Fig 11d. Travel balance gap restrains THB



FX

- Internal conflict amid external volatility: The significant reversal on the part of the UST yields which has surged in November has expectedly led to the high beta THB leading losses for the month as tailwinds turn headwinds. Furthermore, the THB was further weighed down by perceptions of a loss of central bank independence over the nomination of the incoming BoT Chairman which has been perceived as a loss of central bank independence. We expect some THB recovery on hopes of fiscal stimulus though heightened volatility continue into the year end.

- Central bank woes: The importance of central bank independence cannot be any clearer for the THB as the BoT is perceived to anchor macroeconomic stability especially in terms of the balance between debt stability and fiscal-monetary sustainability. Admittedly, the direct powers of new Chairman Kittiratt Na-Ranong who is also an ex-member of the ruling party does not extend to appointment of the BoT governor or the allocation of FX reserves as government spending. In turn, this ought to assuage investors (as well as THB bulls) who remain on the edge about the pressure on the BoT for further cuts.

- Fiscal Risk Mellow For Now: After the initial digital wallet debacle, it appears that details of new stimulus programs thus far appear more target to those who are in need and tend to be in the form of cash. While spending on fiscal transfer remain concerning, the targeted nature implies better multipliers even though it does not raise longer term potential growth.

- Trump Risks Reassessed: Even as worries about trade tariffs mount, the greater threat to the THB continues to be the direct impact from rising UST yields rather than trade tensions. Specifically, Thailand's risks second order given that they are not in the direct crosshair compared to Vietnam and Korea which run large current account surpluses with the US. Furthermore, they are also not prime targets of re-shoring initiatives given relative supply chain positioning.

- Portfolio outflows continued: In November, foreign outflows from both equities and bonds persisted amid worries of Trump 2.0 and pressures from higher UST yields.

- Though China and CNH Woes Weigh: That said, China's economy remain critical to THB recovery with the expenditures of Chinese tourist closely watched in 2025. The lack of a more complete services account recovery to a durable surplus point to the lacklustre travel balance. The flip side though is that investment from China into Thailand may end up as a positive for the THB as we enter Trump 2.0.

- Outlook: Even as seasonal USD softness may aid THB heading into end-2024, we continue to expect overall buoyancy above the mid-33 level. Even as the self-inflicted wounds has led to THB underperformance in November, we continue to expect **THB's relative near-term allure** to be retained on comparatively more prolonged hold relative to ASEAN peers such as PHP and IDR though its marginal attraction is diminished by its heightened volatility especially for those seeking stability.

Rates

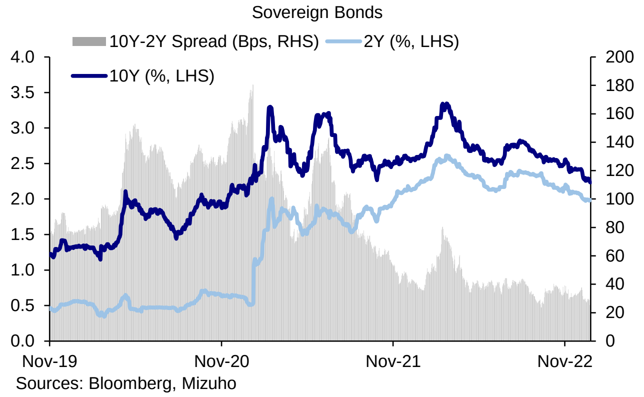
- Central Bank: We expect that the BoT will act **for a further rate cut** in Q1 to support growth amid worsening credit condition and to complement recent debt restructuring measures. Amid these worries, we expect rates to decline to 2.00% in Q1 which is likely in their neutral range considering risk of THB depreciate and the tendency for the BoT to worry about longer term debt sustainability. Late Q3 2025 is towards the end of Governor Sethaput's term and prospects of easing may rise materially.

- Risks: While the near-term risk continues to be that of an earlier expected easing, the bigger worry might be that it is perceived as an erosion of central bank independence which leads to a bigger than expected decline in yield on the front end while longer end may rise as a greater risk premium is demanded.

- Yields: A mild reflection of these concerns, yields have edged slightly lower on the front end leading to a mildly steeper curve compared to the end of October. Nonetheless, we expect that elevated UST yields to continue to be a key driver and keep 2Y yields elevated above 1.9% till end December.

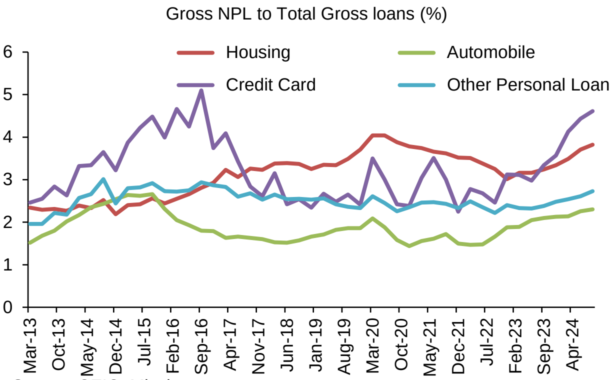
- Curve: Even after the mild steepening, the curve remains very flat with the 10Y-2Y spread at less than 30bps. Even as cash handouts boost near term growth prospects, a slight reckoning from bond markets ought to be watched for especially if fiscal deficits are revised upwards and borrowing plans are enlarged. Given that the risk leans towards BoT easing, this will also aid steepeners.

Fig 11e. Narrower Spreads driven by USTs



Sources: Bloomberg, Mizuho

Figure 11f. Rising NPLs are worrying



Source: CEIC; Mizuho

VND: Crosshairs

	Q3 2024	Q4 2024	Q1 2025	Q2 2025	Q3 2025	Q4 2025
Policy Rate (%)	4.50%	4.50%	4.50%	4.50%	4.50%	4.50%
USD/VND	24540-25457	24560-25900	25300-26100	25200-26200	24600-25800	24500-25600
	24568	25500	25850	25750	25100	24700
GDP (% YoY)	7.4	7.6	5.7	6.0	6.1	6.3
CPI (% YoY)	3.5	2.9	2.8	3.3	3.5	3.6

Note: Values in black are historical whereas those in blue represent forecasts. * Point forecast is for end-period. Ranges are only indicative.

Fig 12a. VND depreciation a worry

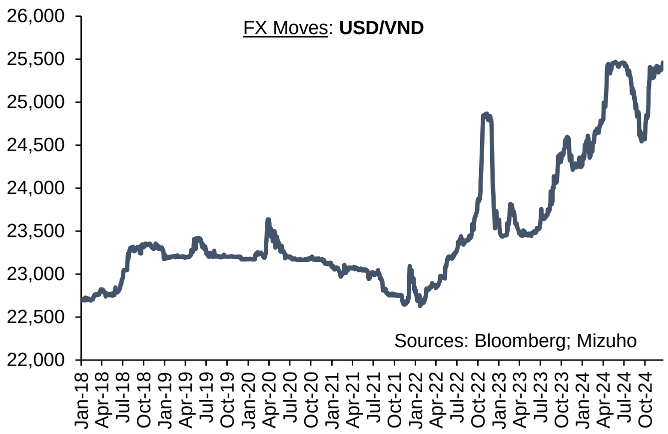
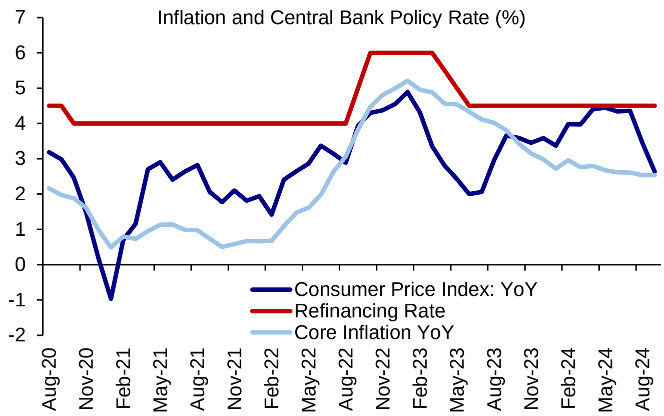
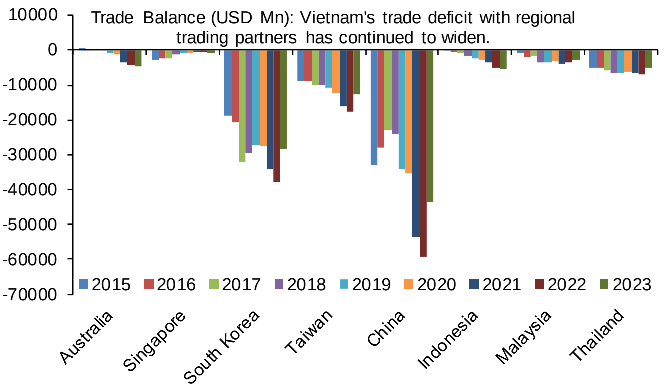


Fig 12b. SBV to continue to hold rates



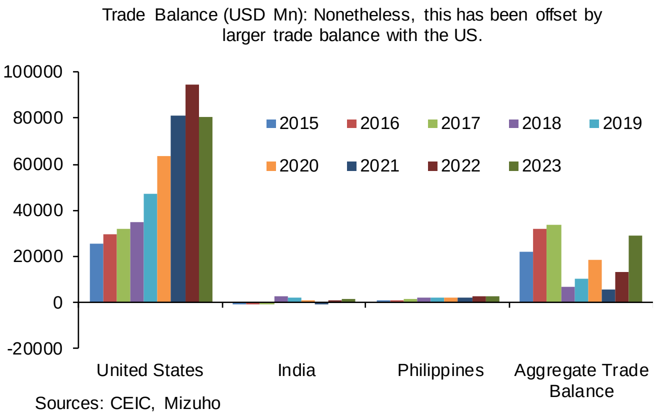
Source: CEIC; Mizuho

Fig 12c. China + 1 evident in trade deficit



Sources: CEIC, Mizuho

Fig 12d. Trade surplus with US has grown



Sources: CEIC, Mizuho

FX

- Woes Growth Even Amid Relative Outperformance: For the month of November, the VND may have managed to sustain only a mild depreciation of 0.5%. Though this is really of little cheer given the FX reserves were likely expended as USD/VND approached the upper limit of the SBV's trading band. Considering Vietnam's 2.5 months of FX-Import coverage ratio, there is a need to be ever more vigilant for depreciation episodes especially as Trump 2.0 may bring the trade war narrative to Vietnam even as re-configuration of supply chain enhances macro prospects.

- Political Risks Remain In the Backdrop: Recent issuance of disciplinary warning to ex-parliament Chairman Hue for violating anti-corruption continues to indicate underlying tensions in the crackdown on graft.

- Eroding FX Buffers in Focus: FX reserves have declined to US$82bn as of August 2024 which is 9% lower than end-2023 and more worryingly the import coverage ratio has declined to 2.5 months which is below the 3-month norm of international benchmarks. These implies that the authorities may be less able to defend the VND in times of USD strength.

- Embroiled In Trump 2.0: Furthermore, the stark increasing in trade surplus with the US may put the VND in the crosshairs once again. Specifically, even under the latest US Treasury report from the Biden Administration, Vietnam's continues to be on the monitoring list due to the large current account surplus and bilateral trade surplus. **Prominent members of the incoming Trump administration** were part of the Senate who opposed Vietnam's application to be classified as a market economy back in Q3.

- Unfortunate Trajectory: The problem in the path ahead is that **attempts by the SBV to rebuild their FX reserves through net purchases can be viewed by the next US administration as attempts to manipulate the currency** and fulfilled all criteria of being listed as trying to gain an unfair competitive advantage which gives the US President powers to enact trade restrictions. Consequently, this diminishes prospects of VND appreciation.

- Unresponsive to Growth Slowdown and Pick-Up: Admittedly, industrial production and retail sales point to a mild moderation in economic activity. That said, a late Q4-2024/Q1-Q025 pick up on front loading of export demand to the US will not be surprising. Nonetheless, the macroeconomic improvement is unlikely to translate into clear VND gains given the pipeline risks of US-China trade war and unresolved domestic woes. For the latter, SBV press conference cites an elevated NPL of 4.5% highlight the underlying stresses in the banking sector and broader macrofinancial stability concerns.

- Financial flows: Reflecting the Trump 2.0 woes, foreign outflow from equities outflow persisted and intensified in November. Without positive development in the Chinese economy, optimism in Vietnam continue to elude.

- Outlook: We remain concerned about possibility of VND depreciation risk in the months ahead as FX buffers remain low. Buoyancy above 25000 retained even as USD make see some seasonal softening into late December. The path for appreciation may also be rather confined to a middle of the pack performance in defiance of their more optimistic growth outturns compared to regional peers. We see potential risks of further VND depreciation in Q1 2025 should President Donald Trump mention Vietnam as a possible target for tariffs.

Rates

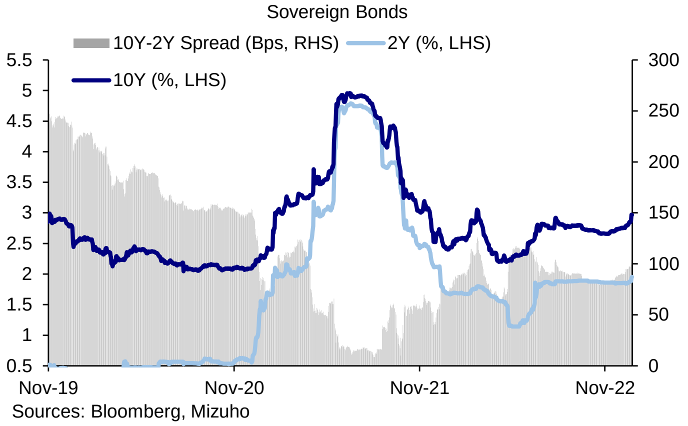
- Central Bank: Given the reportedly high NPL ratios and considerations to bolster the VND, the default stance will continue to be a policy rate hold for the next 6 months as the USD/VND remain elevated in the top half of the trading band. Specifically, the USD/VND is 0.4% from the SBV's upper limit, though it is slightly wider than the 0.2% gap seen in late October.

- Risks: Rather than continue steepening, there is also risk for gradual lifting of the entire curve as very short end rates may rise via open market operations to assist in defending the VND while longer term economy risk from Trump 2.0 see investors continue to demand higher term premium

- Yields: Consequently, yields will remain buoyant as the base case with markets adjusting to higher UST yields.

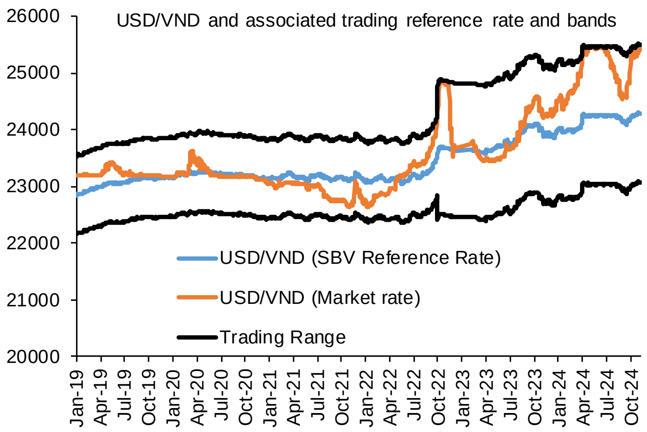
- Curve: A recent steepening of the yield curve reflects markets demand for higher premium at the long end as unsuccessful auctions at the 15, 30 years tenor indicate the gap in government and market expectations. Further mild steepening to be on the cards as investors become worried about Vietnam's China+1 prospects.

Fig 12e. Long end yields rose



Sources: Bloomberg, Mizuho

Figure12f. VND stayed near to top of band in Nov



Source: Bloomberg; Mizuho

AUD: Where's the Confidence?

	Q3 2024	Q4 2024	Q1 2025	Q2 2025	Q3 2025	Q4 2025
Policy Rate (%)	4.35%	4.35%	4.35%	4.10%	3.85%	3.60%
USD/AUD	0.635-0.694	0.616-0.694	0.610-0.660	0.608-0.668	0.610-0.673	0.645-0.700
	0.691	0.624	0.615	0.613	0.655	0.680
GDP (% YoY)	0.9	0.9	1.0	0.9	1.3	1.3
CPI (% YoY)	2.8	3.0	2.8	2.4	3.0	2.7

Note: Values in black are historical whereas those in blue represent forecasts. * Point forecast is for end-period. Ranges are only indicative.

Fig 13a. AUD rally faded

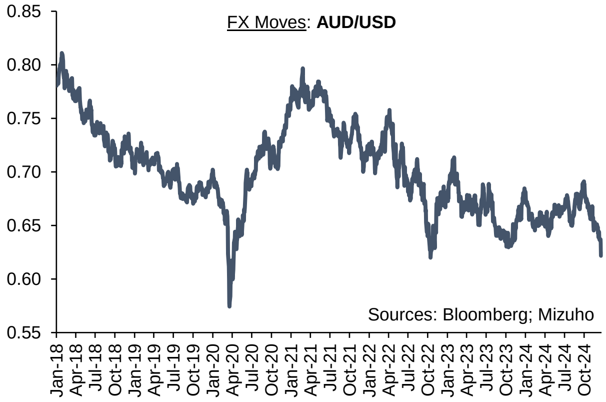


Fig 13b. Headline inflation decline of little consolation

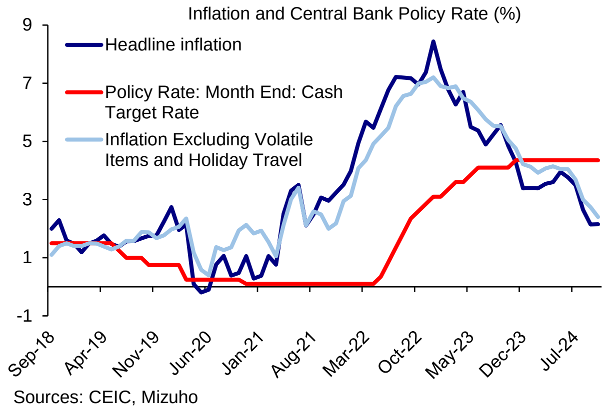


Fig 13c. Services inflation rose

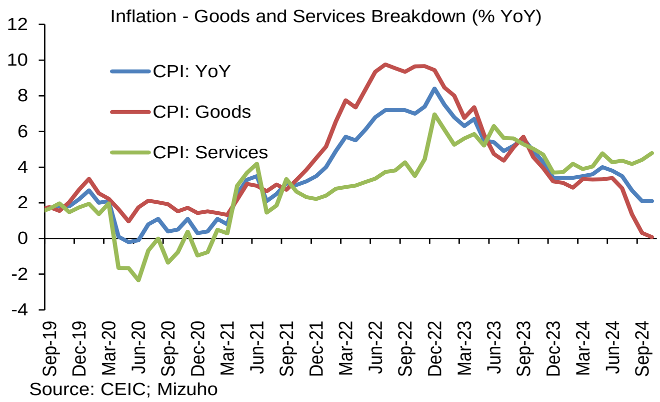
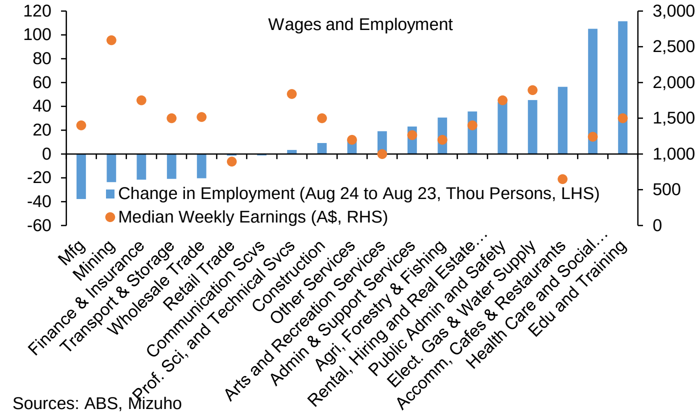


Fig 13d. Wage differentials dull employment gains



FX

- Flimsy Backstop and Absence in Catalyst for Rallies: AUD turned in a **middle of the pack performance** for November amid a widely expected RBA rate hold. In December, AUD **caved in to an underperformance as Q3 GDP reveal continued growth weakness**. Correspondingly, the RBA appears to be hopeful for the potential to embark on cut in 2025 even amid an increasingly bumpy dis-inflation path. This policy stance is also no catalyst for AUD rallies, though it may perversely become a risky backstop facing AUD bears. Swings will come from expectations of a pick-up in China economic activity.

- Trump 2.0 Collateral Damage from China: Like many countries, China is Australia's largest trading partner. While their commodity exporting angle does not put Australia in direct sight of tariff tensions, the fear is that escalating tariffs on China's goods will restrain economic recovery and demand for Australia's exports, diminishing AUD recovery prospects.

- Yet rallies remain China dependent: That said, a more durable recovery in China's fixed asset investment and industrial activity remains essential for AUD rallies. Consequently, given policy lags, the **looser monetary policy stance in China ought to underpin H2 growth in Australia.**

- RBA's dovishness invite volatility: While it may be tempting to see the RBA's inclination to cut as a bearish signal for the AUD, it may end up trigger more **near term upside AUD volatility** as the trimmed mean inflation remains bumpy and services inflation remain sticky. To be clear, even as the RBA's espouse some confidence on inflation, it is hard to see the sudden uptick in confidence given that trimmed mean inflation was higher in between their November and December meetings and the wage growth of 3.5% in Q3 stepping down from 4.1% should also be viewed from the angle that momentum remain at 0.8% QoQ.

- It's the economy: Clearly, the concerns are on growth as the diminished household savings ratio and weak household consumption grow increasingly worrying and will drag on AUD performance. Robust labour market performance should also be viewed from a sectoral perspective as job gains mainly stemmed from less well-paying sectors. As such, the tepid consumption should not be too surprising.

- Reframing Inflation: Amid these concerns, we think that the RBA may soon abandon the view that the underlying headline inflation remains high and the current low inflation readings are mainly the result of government relief measures such as rebates. The reconciliation should come from the fact that the some of these subsidies may be permanently in the baseline. The elevated underlying real rates also diminishes AUD allure.

- Outlook: Into 2025, amid rate cut expectations, AUD weakness to weigh on attempt to retake 66 cents in H1 may persist as Trump 2.0 will likely see a ramp up of tariff threat and China's recovery continue to be subject to fits and starts. A durable recovery in H2 on revelation that tariffs threats being negotiable and headwinds from initial cuts fade as the RBA faces a shallow easing cycle (75bps) as inflation bumps calls for calibration in rate cuts. Viewed against regional peers, long AUD/SGD may retain attraction as the MAS has showed clearer inclinations for easing with lesser FX depreciation concerns of regional peers such as the IDR and PHP who need clearer opportunities to ease. Furthermore, AUD tend to exhibit displays a higher beta to China even relative to the SGD.

Rates

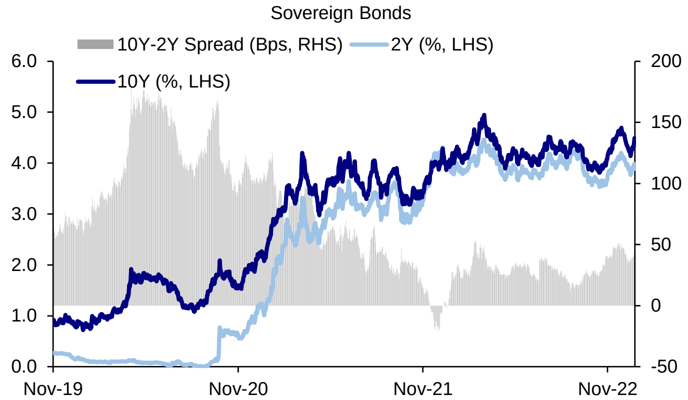
- Central Bank: As the February 2025 meeting turns in a live one, front end yield volatility become increasingly accentuated with hypersensitivity to upcoming data prints expected. Trump 2.0 may end up being a restrain on rate should it drive up resource demand front loading and associated price pressures and bump up growth. For now, we lean towards the first cut in Q2 though we envisage that there is a high 40% chance of a cut in Q1. Q2 may well be the quarter when prolonged subdued growth become intolerable for the RBA.

- Risks: The risk is for the RBA to front loaded cut of 35bps at the initial stage should employment show signs of buckling fast given that the rise in unemployment rate tend to be sharp rather than gradual.

- Yields: Yields declined alongside global developments with long end yields falling more. With RBA's change in policy response function, front end yields look set to come under more pressure but given that the depth of rate rates may fall short of peers such as the Fed and the ECB, the decline in font end yields may lag.

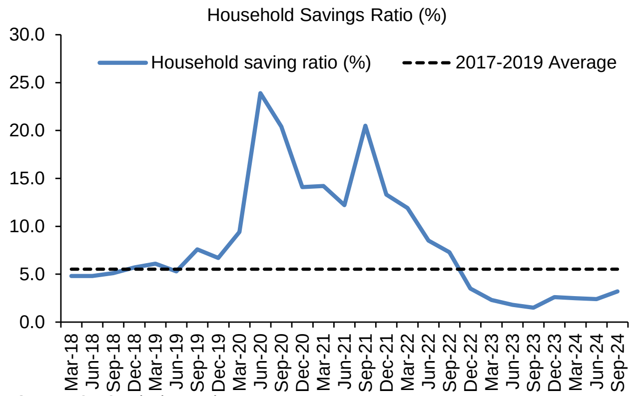
- Curve: With the RBA's shift in tone, **steepening will be increasingly watched** for especially as domestic fiscal woes will also not go unnoticed even amid bond rallies on rate cuts.

Fig 13e. Yields decline in November



Sources: Bloomberg, Mizuho

Figure 13f. Household savings ratio eludes



Source: CEIC; Mizuho Bank

Global FX Assumptions: Trump USD Front-Loaded, Not Unfettered

	Q4 2024	Q1 2025	Q2 2025	Q3 2025	Q4 2025	Q1 2026
DXY	106.5	105.6	102.2	103.4	99.5	100.2
	100.5-108.5	102.5-109.8	99.0-107.5	98.8-104.7	97.5-104.3	96.0-102.5
Brent Crude (US$/brrl)	72.0	68.5	64.5	61.5	65.5	63.8
	68.5-82.5	63.5-78.8	60.5-72.5	57.5-69.6	58.5-72.5	58.5-70.5
Fed	4.25-4.50%	4.00-4.25%	3.25-3.50%	2.50-2.75%	2.50-2.75%	2.50-2.75%
ECB	3.00%	2.50%	2.00%	2.00%	2.00%	2.00%
BoJ	0.25%	0.35%	0.35%	0.35%	0.50%	0.50%

The USD Backdrop

1) The Trump USD: **Trump 2.0 provides a significant level boost to USD dynamics** that is expected to be pronounced through most of H1 2025 at least, **but perhaps not unremittingly so**. Fact is, **Trump's** (loudly) **articulated posture** (be it policy and diplomatic), and associated bombast are mostly **inclined to boost the USD through** one of **two channels**. The first is *via 'USD exceptionalism"* and **corresponding USD boost**. The other is from mechanisms of ***US antagonism**,* which in turn, **undermines the currencies at the receiving end**. In any case, and more comprehensively, ***geo-politics***, ***energy policies*** and ***relative monetary policy shifts*** are all **also positioned to align with a stronger USD**.

2) But Not Spared Some Doubt/Decay: Nonetheless, ***even for the "Trump USD"**,* unchallenged one-way ascendancy ***without any signs of decay*** is highly unlikely. Broadly speaking, **some shine could "USD Trump"** on account of disappointment on the economic front. Especially multiple dimensions of a strong USD (on US exceptionalism and antagonism priced in). This means susceptibility to "disappointments may be under-accounted for. What's more, USD may not be unscathed by retaliation on the trade front. Finally, the Fed easing cycle is not necessarily blown off by, and certainly not mutually exclusive to, by Trump 2.0.

3) Meaningful Back-end Moderation: In fact, all said, under a confluence of conditions, **USD could mellow meaningfully at the backend of 2025**; as the ***worst of risk scenarios are alleviated*** (diminished have demand) and at the same time ***US exceptionalism is appropriately tempered, such that Fed policy restraint is dialed back****.* In other words, a **conspiracy of "fear" and Fed (restraint) firing up the Greenback could unwind**; thereby **moderating the intensity of USD bulls**. Especially if three conditions are fulfilled. Specifically these are:

a. Condition 1 – Fed Cuts Significantly (More than Expected): Despite the downgrade to the number of cuts (to 2 from 4) into 2025, the **Fed could deliver more cuts**. Especially as *US economic exceptionalism may turn out to be be overstated*. Moreover, the *US may not be entirely unscathed by the trade conflict* that is intended as a core part of Trump 2.0 policies. Finally, the *Trump 2.0 reflationary expectations* (so-called Trump-flation) prove to be a *lesser risk in terms of constraining Fed easing.*

b. Condition 2 – Trade War Bark is Worse than the Bite: Furthermore, the **most extreme demand destruction risks associated with Trump 2.0 trade tariffs prove to be overblown** as the Trump administration dials back trade antagonism (and tariff rates) as negotiations progress. This *unwinds some of the more acute currency damage* to trading partners (e.g. MXN, CNY, CAD, EUR, etc.). And as a corollary, **exaggerated** (and perverse) **USD bullishness** *deriving from adverse trade risks* **subside**.

c. Condition 3 – China Stimulus/Support Sufficient to Avert CNH Sell-Off: Finally, sharp CNY pressures are alleviated by more encouraging China stimulus put in place to backstop the economy and insure against more destabilizing CNY outflows. In turn, this lends some support, if not scope for (partial) recovery for AXJ more widely. This is a precondition for AXJ to be better positioned to exploit measured (albeit not a full) USD pullback. Although non-reversion to pre-Fed hike levels will likely still apply, as USD retains some of the structural/geo-political advantages.

4) But Controlled Landing, Not Crash: But even with these conditions, **USD is likely to have a controlled landing**, ***not an unmitigated crash**.* Not by a long shot. First off, the early **path to a softer USD** may be **exceptionally bumpy** *with **bullish detours likely into early-2025**.* What's more, given that **softening of US data is unlikely to take a linear path**, *corresponding* (initial) *stickiness of Fed rates could impede a softer USD.* Furthermore even if US suffered headwinds, sufficiently **acute US recessions may** (initially) **trigger USD strength** *v(from haven demand)* before USD softens on rate cuts and bottoming. All said, the stage may be set for ***a cushioned decline not an uncontrolled downward spiral*** (in coming months) tied purely to Fed rate cuts/expectations.

5) Non-Reversion "USD Smile" Slope: Crucially, the **depth of decline is likely to be far more limited**, **stopping well** ***short of a "full reversion"*** *to pre-Fed normalization (to ~90 DXY index levels).* Instead, the **Fed's direction of policy travel** (down in rates) alongside more elevated uncertainty **corresponds to a gently softer USD tracing the slope down the "USD Smile"**.

6) Less Compelling Fiat Alternatives: More so, as the most liquid **fiat alternatives to the Greenback** *(such as the EUR, JPY and GBP)* **are structurally less compelling** *compared to previous cycles.* This partly explains exceptional support in Gold (that has defied elevated real rates), cryptocurrencies and other real assets. The upshot though is that in relative fiat terms, the **Greenback could appear stronger relative to the past through Fed cuts**. More so, as geo-politics tilts the scale to the advantage of the Greenback.

7) No Real Divergence: What's more, ***in real rate terms*****, enduring and profound policy divergence**, *corresponding with a sharp and sustained USD drop,* is unlikely. Point being, the US is unlikely to go it alone with large and fast rate cuts, checking nominal divergence. And US dis-inflation is not particularly vulnerable to falling significantly short. Especially **given superior domestic buffer to energy shocks** (from geo-politics) in Europe and Japan. Again, this **checks the extent of USD pullback**.

G3 Central Banks: Hawkish Flex/Restraint Bumpy Path

Fed: **Despite a significantly hawkish upgrade to the December 'Dot Plot'** that now only factors in two (50bp) of rate cuts for 2025, we expect the **Fed may lower rates significantly more** – close to, or lower than, 3.00%. This is premised *still restrictive settings* being caught *wrong-footed by strained consumer cash-flows.* Moreover, *reflationary effects of Trump 2.0 may be exaggerated* whereas the *demand softening impact* from trade tariffs (and plans to cut fiscal spending) may be *under-accounted* for (see Box 4). The upshot is that **premature hawkish restraint**s on understandable sticky inflation/reflation risks, may eventually prove to be **misguided**.

ECB: With a **higher degree of economic uncertainty** and **geo-political exposures**, the ECB **needs to be more watchful of fragile confidence**. As such we expect that the ECB will have to engage in deeper cuts heading into 2025 as economic weakness and vulnerabilities are exacerbated by the threat of trade conflicts. **Inadvertent** (but inevitable) **EUR volatility** through pockets of perceived policy divergence and trade/diplomatic abrasion will render policy more complex (and trade-offs sharper). But this is a necessary cost of policy relief.

BoJ: The BoJ is probably **committed to setting course for rates to go towards (but possibly shy of) 1.00%**. ***But*** **over a much longer horizon** and **highly conditional on economic strengths materializing**. This includes sustained wage gains. But if the Fed re-calibrates to a faster pace of cuts (as we predict) and at odds with a slower pace of cuts it has indicated, the BoJ may be caught off-guard with **much sharper JPY appreciation**. Which in turn may **entail dire threats of adverse income/balance sheet impact**. Given Japan's deep exports dependency that ties back to wages and (already fragile) household confidence, this **is a policy mis-step that the BoJ cannot afford**. Gradualism erring on the side of accommodation.

Box 4: Fed: The Problem with Partial Assumptions

- **Insofar** that the Fed's **hawkish pivot** *accompanying (and essentially overwhelming!) the 25bp cut* **only partially incorporates Trump 2.0 risks**, it **may be problematic**.
- Point being, *halving of 2025 'Dot Plot' rate reduction to 50bp* was presumably premised on **hawkish economic upgrades**; comprising *inflation projections bumped up* and *unemployment nudged lower.*
  - Inflation (PCE): **Bumped up 2025 projection by 40bp to 2.5%**. Full reversion to 2% inflation target pushed out to 2027 (from 2026), although 2026 is a mere 0.1%-pt higher (at 2.1%).
  - Core Inflation (core PCE): **Lifted 2025 projection by 30bp to 2.5% inflation/core inflation.** Full reversion to 2% core inflation also deferred to 2027 (from 2026), although 2026 overshoot is just 0.2%-pt (at 2.2%).
  - Unemployment: **unemployment is now nudged lower (by 10bp)** to 4.3% in 2025 (from 4.4%
  - Growth: Growth is hardly changed over 2022-2027, only fractionally tweaked (up 10bp for 2025 to 2.1%), with that 0.1%-pt coming out of 2027 (at 1.9% from 2.0%).
- At face value, the proportionate 50bp inflation-jobs (PCE up 40bp and unemployment down 10bp) hawkish upgrade appears to square with the hawkish 50bp 'Dot Plot' shift.
- But the trouble is, the **assumptions of "Trump-flation" risk** are **at best incomplete**. *At worst, outright biased.*
- To be sure, it is revealed that **uncertainty around inflation forecasts** have **increased materially**.
- Nonetheless, despite the uncertainty, the emphasis appears to be on the **upside bias in Trump 2.0 inflation**.
- Specifically, **less uncertain** (and coincidentally ***reflationary***) **outcomes** such as *tax cuts* and *deregulation* are ostensibly being **incorporated by some**.
- *In contrast,* **more uncertain** outcomes related to trade tariffs (and consequent retaliation), with ***distinctly adverse economic effects****,* are **omitted from economic forecasts**.
- It is understandable to preclude the complexities of uncertainty.
- But it is **mistake to confuse the uncertain for the improbable***.
- The **precise outcomes from trade antagonism may be highly uncertain**.
- ***But*** there are **significant probabilities of global trade friction, to the detriment of US (onshore) demand** (after higher import prices are borne**).
- Moreover, **dis-inflation from money-multiplier suppression** resulting from *Bessent's fiscal deficit reduction plans* alongside *cost slashing ambitions of minted DOGE^* also appear to be out of the Fed's calculus.
- So, what's **potentially problematic** is that **Trump 2.0** appears to be *framed with the bias reflation* whilst *under-accounting for adverse demand risks* as well as *unfamiliar dis-inflation dynamics.*
- In turn, this suggests that the Fed's dovish flex may be inadvertently overdone.
- The **resultant curve ball** for markets from this may be UST yields unexpectedly turning sharply lower heading into 2025.

* "Knightian uncertainty" (derived from Frank Knight's characterization of uncertainty) refers to the inability to predict (ascribe probabilities to outcomes), hence quantify due to unknowns that cannot be modelled. But these are not necessarily proportionately improbable.

** The US does not have the luxury of benefitting from import substitution for a large swathe of goods.

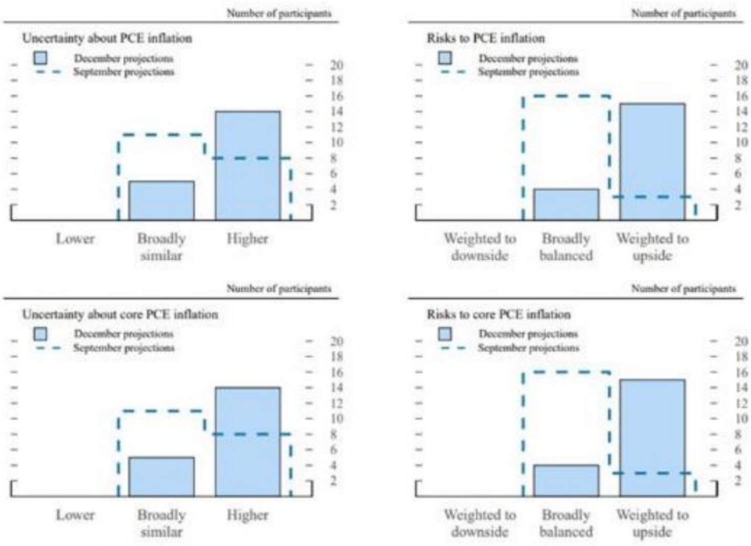
^ DOGE refers to the newly formed Department of Government Efficiency led by Elon Musk and Republican Vivek Ramaswamy to slash government spending.

Table 1. Economic projections of Federal Reserve Board members and Federal Reserve Bank presidents, under their individual assumptions of projected appropriate monetary policy, December 2024

Percent

Variable	Median[1]					Central Tendency[2]					Range[3]				
	2024	2025	2026	2027	Longer run	2024	2025	2026	2027	Longer run	2024	2025	2026	2027	Longer run
Change in real GDP	2.5	2.1	2.0	1.9	1.8	2.4–2.5	1.8–2.2	1.9–2.1	1.8–2.0	1.7–2.0	2.3–2.7	1.6–2.5	1.4–2.5	1.5–2.5	1.7–2.5
September projection	2.0	2.0	2.0	2.0	1.8	1.9–2.1	1.8–2.2	1.9–2.3	1.8–2.1	1.7–2.0	1.8–2.6	1.3–2.5	1.7–2.5	1.7–2.5	1.7–2.5
Unemployment rate	4.2	4.3	4.3	4.3	4.2	4.2	4.2–4.5	4.1–4.4	4.0–4.4	3.9–4.3	4.2	4.2–4.5	3.9–4.6	3.8–4.5	3.5–4.5
September projection	4.4	4.4	4.3	4.2	4.2	4.3–4.4	4.2–4.5	4.0–4.4	4.0–4.4	3.9–4.3	4.2–4.5	4.2–4.7	3.9–4.5	3.8–4.5	3.5–4.5
PCE inflation	2.4	2.5	2.1	2.0	2.0	2.4–2.5	2.3–2.6	2.0–2.2	2.0	2.0	2.4–2.7	2.1–2.9	2.0–2.6	2.0–2.4	2.0
September projection	2.3	2.1	2.0	2.0	2.0	2.2–2.4	2.1–2.2	2.0	2.0	2.0	2.1–2.7	2.1–2.4	2.0–2.2	2.0–2.1	2.0
Core PCE inflation[4]	2.8	2.5	2.2	2.0		2.8–2.9	2.5–2.7	2.0–2.3	2.0		2.8–2.9	2.1–3.2	2.0–2.7	2.0–2.6	
September projection	2.6	2.2	2.0	2.0		2.6–2.7	2.1–2.3	2.0	2.0		2.4–2.9	2.1–2.5	2.0–2.2	2.0–2.2	
Memo: Projected appropriate policy path															
Federal funds rate	4.4	3.9	3.4	3.1	3.0	4.4–4.6	3.6–4.1	3.1–3.6	2.9–3.6	2.8–3.6	4.4–4.6	3.1–4.4	2.4–3.9	2.4–3.9	2.4–3.9
September projection	4.4	3.4	2.9	2.9	2.9	4.4–4.6	3.1–3.6	2.6–3.6	2.6–3.6	2.5–3.5	4.1–4.9	2.9–4.1	2.4–3.9	2.4–3.9	2.4–3.8

FOMC participants' assessments of uncertainty and risks around their economic projections



Source: Charts and Table from the Fed's Summary of Economic Projections released with the FOMC.

Rates: Volatile, but Toppish (despite Trump-flation)

Generally Softer Rates: The **big picture view is for dovish policy to continue** coming through **feeds into the narrative for global rates to soften** further *even if this transpires amid elevated global rates volatility in the interim.* To be sure, current dial-back of dovish inclinations in the context of Trump 2.0 (and attendant Trump-flation) and generally elevated geo-political uncertainty and tension will prove to be overwhelmed by lagged policy tightening and persistent demand restraints working though with a lag.

Global Rate Cuts to Gather Pace: For one, fragile underlying demand conditions alongside lingering geo-political risks make the case for more emphatic rate cuts. The US Fed will, despite current reservations, probably set the stage for global rates to decline. This **sets front-end yields up for more pronounced pullback**.

Maybe Because, and Not Just Despite, of Trump 2.0: And to be sure, Trump 2.0 and Trump-flation expectations could actually reinforce the case for softer rates. Not only because of negative demand impact that has not been fully accounted for. Notably, Trump 1.0 tariffs were not particularly inflationary, and in fact led to a slowdown in demand. Finally, the fiscal cost cutting commitment of "Team Trump" may be under-appreciated. And this means that the current elevation priced into the UST yield curve may be excessive.

Steeper Curve: **Lower rates** will also be **accompanied by a steeper yield curve**. With yield curve inversion shrugged off in Q3, the 10-2Y spread for the *UST curve may be set to widen to 30-80bp* into 2025 on a confluence of factors. Not only from the mechanics of rate cuts, but also from uncertainty further out.

Wider (Risk) Premium: ***Associated with a steeper UST yield curve*** and Fed rate cuts is a **wider risk premium**. This, as the allure of "all-in" returns is challenged by risk-adjusted re-pricing. Pressures from fiscal deficits and trade disruptions only exacerbate these dynamics.

Oil: Softer amid Uncertainty

Softer: Oil prices could soften further in 2025 on a conspiracy of demand dampeners and supply-push despite lingering volatility (and latent upside risks) from unabating Geo-political risks. The upshot is that the overwhelming conspiracy of demand (depressing) factors alongside impending supply boost are likely to keep prices suppressed, and more likely than not, a tad softer amid Trump 2.0 uncertainties.

Demand Dampeners: Signs of softening demand as global fiscal push becomes more constrained and post-pandemic consumption bump-up fizzles point towards softening demand growth outside of specific pockets of optimism (in AI, tech, etc.)

China Shortfall: What's more, despite the assurances of more emphatic stimulus, downside risks to China's growth persist. And given the stockpiling of Oil by China, the potential for a large bump-up in oil demand from China is somewhat less promising than is the risk of slippage in demand.

Exacerbated by Trump 2.0 Trade Conflict: What's more, the potential for negative demand shocks from Trump2.0 trade tariffs and threats of a retaliatory spiral, *even if only due to uncertainty,* is more likely than not to suppress demand and consequently keep prices soft.

In Spite of US Exceptionalism: Admittedly, **optimism about US exceptionalism** that lends itself to elevated US demand is a justifiable counter-point to the narrative of softer oil. But this is a partial view. Even without debating the validity of enduring US demand resilience amid trade antagonism, materially higher oil/energy output under Trump 2.0 (generic support for O&G seen in Trump 1.0 souped up by considered 3MBpD output increase ambitions associated with Scott Bessent's wider "Three 3s" plan) could easily offset exceptional. Possibly more than offset as supply bump-up. So oil may be set to soften. Not just in spite, but partly as a by-product, of US exceptionalism.

OPEC Delaying the Inevitable: Finally, the biggest supply hold-back factor, the OPEC's deliberate and deliberated production curbs could also start to be loosened. Whilst the output restoration has been delayed for now, the revenue pain points from prolonged, self-imposed curbs now confronting serious loss of market share to US and non-OPEC producers could force OPEC's hand to restore supply soon (enough). And while the gambit that potential sanctions on Iran crimping global oil supply is not misplaced, this will be overshadowed by capacity elsewhere; limiting any sustained upside to oil prices.

Conflict –Latent, Not Unleashed, Volatility: Admittedly, **tail risks of oil prices surging on conflict r**isks spinning out of control cannot be dismissed. In which case, the potential for prices to spiral past $100/bbl cannot be dismissed. ***But* desensitization to war** means that *unless there is imminent and inevitable disruption to production and/or passage of crude,* prices and volatility are more likely to be contained.

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