# Asia ex-Japan FX & Rates Outlook

## Jan-Feb 2025*: Head(line Volatility) & Tail (Risks)

Trump 2.0 Tariff Threats: Trump's **zero-sum game view** of, and "winner takes all" approach to, global trade inevitably dials up headline risks from tariff threats. And a desire **for "heads I win, tails you lose" type of deal** derives US advantage at the expense of trading partners. This accentuates relative US exceptionalism, underpins interim (hawkish) **Fed divergence** and lends to **strength of "Trump USD"**. Notwithstanding which, lurching from one headline to another sets the stage for significantly more pronounced two-way volatility.

(Heads-or-Tails Type) Policy Uncertainty: Global central banks, the Fed not excepted, are **hobbled by macroeconomic-policy uncertainty** and the consequent **policy quagmire**. Specifically, forced to grapple with *opposing threats from inflationary tariff triggers* on one hand, and *adverse demand shocks* resulting from tariffs on the other. Notably, the contrast between the Fed's preoccupation with inflationary risks whilst other global central banks (including in Asia) worry about negative growth shocks underscore relative hawkish Fed divergence. In turn, underscoring **risk-repricing from relatively more elevated US rates**.

FX Overrun by Volatile USD Bulls: **Heightened two-way risks** will dominate as *chaotic, shoot-from-the-hip style of* **Trump 2.0 tariffs hit markets volatile USD bulls**. To be sure, the "Trump flex" will probably underscore bigger picture of USD buoyancy. That said, *Trump's preferred tactic of front-loading threat bombast as a basis for leverage during subsequent negotiations underscore non-linear FX moves. Especially as* **FX markets are rendered hyper-sensitive to (US) tariff headlines**. Back-end scope for moderated USD strength (pressures on AXJ) is subject to tariff threat de-escalation and coinciding CNH traction.

(Initial) Headwinds to Lower Rates: A turbulent path to lower rates in Asia derives from Fed-driven headwinds from elevated UST yields initially. After which, risk re-pricing could get in the way even as US rates eventually come lower (on assumed back-end Fed cuts). Meanwhile, US fiscal-tariff tensions could induce a **good deal of two-way volatility**. More pronounced term and risk premia however look to be the endgame.

*The publication of this January edition was purposefully delayed a week to better capture the initial round of tariff risks and repercussions.

# Head(line Volatility) & Tail (Risks)

- **Asia FX**: Hyper-sensitivity to tariff headlines (be it pressures on elevated threats or relief from worst-case averted) amid heightened US policy uncertainty compounded by hawkish Fed divergence (vis-à-vis Asian central banks) sets the stage for accentuated two-way volatility. Albeit with a distinct bearish bias for AXJ (or at least an absence of scope for sustained rebound) initially in 2025 as US exceptionalism and antagonism conspire. Scope for negotiated compromises later in 2025 (or early-2026) could however set the stage for a cautious and measured recovery as AXJ risks are moderated accordingly. Softer US rates though may not fully filter though as risk premium in Asia is expected to adjust higher from exceptionally suppressed levels.

- **CNY:** Trump's campaign % threat of 60% tariffs watered down to 10% tariff opening salvo, complemented by PBoC backstop, has helped help with RMB traction. But a silver lining on negotiation is not a silver bullet for the risks of further trade conflict escalation. Latent CNH fragility and downside risks remain intact for now.

- **HKD:** The return of carry trade flow following the HKD year-end seasonal liquidity squeeze contributed to the HKD weakness, but we expect the HKD to stay in the strong half of trading band amid Fed's easing cycle.

- **INR**: Cyclical headwinds and structural impediments could conspire to impose sharper trade-off on policy easing by the RBI (justified as it is). Especially as improved fiscal consolidation targets appear stretched on the optimistic side. What's more, India's loss of advantage from Russian oil also dims rupee at the margin. Some degree of hysteresis entailing lower rupee equilibrium limits rupee rebound, denying full reversion.

- **KRW**: Interim relief from domestic political woes may be renewed should elections be called. Nonetheless, National Pension Service hedging will temper excessive weakness.

- **TWD**: TWD remains vulnerable to risk off episodes alongside allusion to defence arrangements under Trump 2.0. Easing by the CBC will remain cautious and calibrated in the months ahead.

- **SGD**: Slight reduction in slope of the S$NEER by the MAS not an outright bearish call as the modest and gradual appreciation stance intact. Nonetheless, deference on USD swings will drive volatility for the small open economy especially in H2 2025 as indirect tariff impact and direct loophole allegations remain key risks.

- **IDR**: Underperformance looks to persist amid a confluence of fiscal woes and global growth headwinds seeping through. Tensions between BI's desire to ease and rupiah stability will persist. Further pressures could see tests to record low levels re-emerging should USD volatility continue, even as BI attempts to temper weakness.

- **MYR**: Two-way volatility on swings in UST yields and US-China trade tensions; but solid fundamentals should more generally position MYR in a good standing for further outperformance against regional peers.

- **PHP**: Growth headwinds both domestically and externally pressure PHP, But BSP interventions by BSP merely temper excessive volatility, not determine levels. Crucially, there can be no lines in the sand as dynamic FX stability-easing trade-off analysis in the context broader relative AXJ valuations determine BSP backstop.

- **THB**: Volatility to persist and imply time sensitive vulnerability even as a firmer current account surplus aids prospect of recovery further out. Fiscal debt reckoning a risk to be watch even as ruling party solidifies position.

- **VND**: Diminished FX reserves will continue to weigh on VND prospect under Trump 2.0 and current account surplus imply that there is significant risk of being targeted.

- **AUD**: RBA looking to the possibility of easing in 2025 will restrain AUD climb but two-way volatility accentuates as labour markets cloud easing pathway. Furthermore, China's fit and starts recovery will constrain.

# Currency Forecast

| FX Forecasts | Q4 24 | Q1 25 | Q2 25 | Q3 25 | Q4 25 | Q1 26 |
|---|---|---|---|---|---|---|
| USD/CNY | 7.04-7.38 | 7.10-7.55 | 7.15-7.60 | 7.05-7.45 | 6.98-7.37 | 6.97-7.26 |
| | 7.28 | 7.32 | 7.38 | 7.23 | 7.12 | 7.12 |
| USD/HKD | 7.76-7.80 | 7.75-7.79 | 7.75-7.79 | 7.75-7.79 | 7.76-7.80 | 7.76-7.80 |
| | 7.77 | 7.76 | 7.76 | 7.75 | 7.76 | 7.77 |
| USD/INR | 84.1-85.8 | 85.4-88.5 | 86.2-88.9 | 85.5-88.9 | 85.2-88.2 | 84.8-87.8 |
| | 85.6 | 87.1 | 87.8 | 86.5 | 86.0 | 86.0 |
| USD/KRW | 1360-1500 | 1370-1540 | 1330-1480 | 1290-1400 | 1280-1380 | 1360-1500 |
| | 1438 | 1442 | 1385 | 1345 | 1340 | 1438 |
| USD/SGD | 1.283-1.368 | 1.327-1.376 | 1.330-1.388 | 1.315-1.375 | 1.292-1.344 | 1.292-1.337 |
| | 1.367 | 1.363 | 1.371 | 1.335 | 1.318 | 1.321 |
| USD/TWD | 31.6-32.8 | 32.2-34.5 | 32.1-34.5 | 31.5-33.9 | 31.2-33.5 | 31.0-33.5 |
| | 32.8 | 33.3 | 33.5 | 32.5 | 32.2 | 32.2 |
| USD/IDR | 15170-16305 | 15850-16560 | 15900-16620 | 15300-16490 | 15000-16100 | 15100-15750 |
| | 16102 | 16350 | 16450 | 15800 | 15400 | 15230 |
| USD/MYR | 4.12 – 4.51 | 4.29 – 4.58 | 4.27 – 4.67 | 4.13 – 4.55 | 3.99 – 4.36 | 3.99 – 4.24 |
| | 4.47 | 4.47 | 4.53 | 4.30 | 4.12 | 4.14 |
| USD/PHP | 56.0 - 59.0 | 57.2 - 60.2 | 57.1 – 60.5 | 55.9 - 59.8 | 54.7 – 58.2 | 54.8 – 57.5 |
| | 57.8 | 58.8 | 59.6 | 57.2 | 56.5 | 56.3 |
| USD/THB | 32.3-35.2 | 32.9 - 35.9 | 33.8 - 36.2 | 33.4 - 35.7 | 32.7 - 34.9 | 32.6-34.6 |
| | 34.1 | 34.8 | 35.2 | 34.3 | 33.6 | 33.3 |
| USD/VND | 24560-25512 | 24900-26100 | 25200-26200 | 24600-25800 | 24500-25600 | 24500-25600 |
| | 25485 | 25550 | 25750 | 25100 | 24700 | 24680 |
| AUD/USD | 0.617-0.694 | 0.610-0.653 | 0.608-0.668 | 0.610-0.673 | 0.645-0.700 | 0.655-0.700 |
| | 0.618 | 0.615 | 0.613 | 0.655 | 0.680 | 0.678 |

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

## Asia Ex-Japan (AXJ) FX: Tariff Head(line) & Tail Risks!

Fig 1a. Trump Tariffs Fire Up Volatility

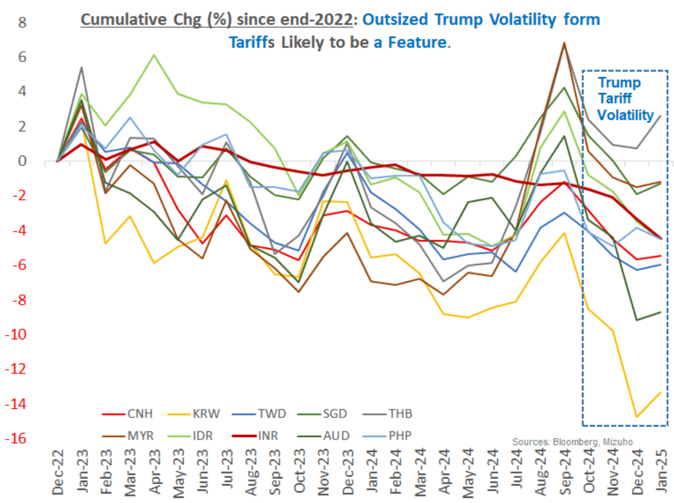



Fig 1b. Fed Restraint to Underscore Divergence

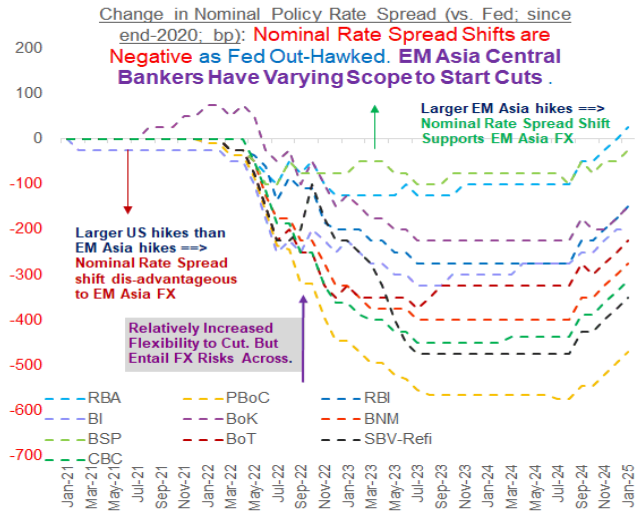



Fig 1c. JPY-related Risks Amplify Vulnerabilities

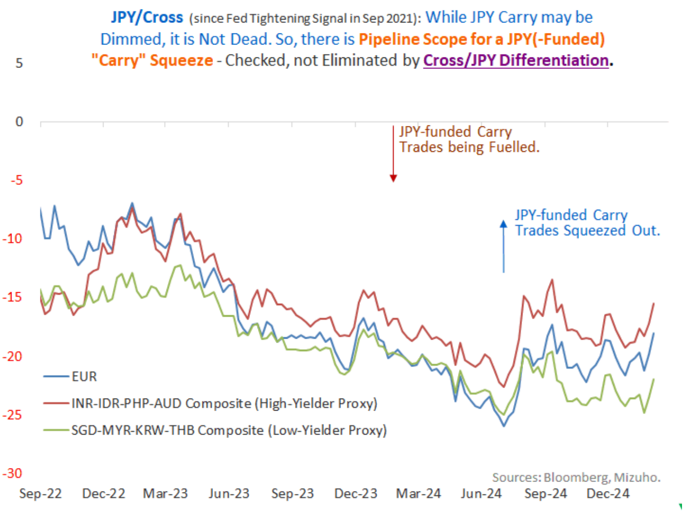
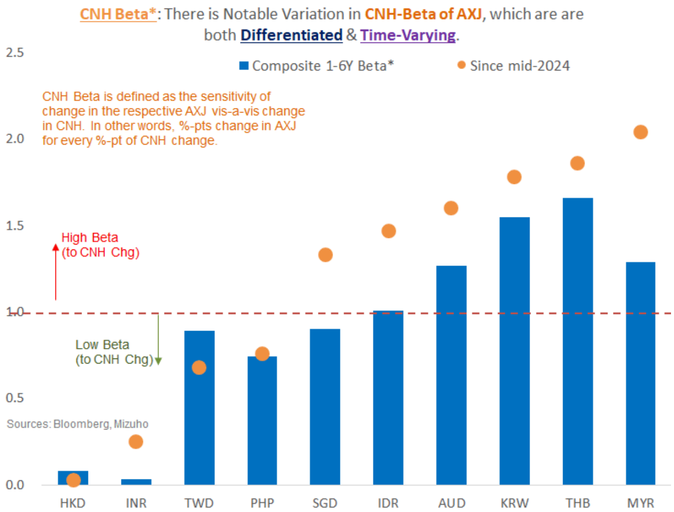



Fig 1d. CNY Beta Uneven & Upsized




**FX**

- Tariff Head(line) & Tail Risks: **AXJ continue to be prone to wild swings from tariff headline risks**. Especially as **"heads or tail" type of binary outcomes** are **repeatedly played out**. From *acute sell-off on* instances of Trump's callous *tariff threats to relief rallies when* the tariff *threats are rescinded or suspended.* With "only the first salvo" in Chinese tariffs, Europe in the line of fire, **headline tariff triggers**, and *attendant volatility* abound. And the ***tail risk of bilateral trade antagonism*** in the rest of Asia and/or ***escalatory tit-for-tat trade wars***.

- Trumped Up (Tariff) Threats & De-sensitization: Admittedly, markets may **increasingly be inclined to assume that tariff threats are trumped up**. Specifically, only **to be exploited as leverage for future negotiations**. *Consequently,* it is **tempting to suggest** markets may be emboldened to **start downgrading tariff-induced threats**. Which ***incrementally de-sensitize AXJ to tariffs headlines.***

- Bluster Not Always a Bluff: But the **luxury of linear de-sensitization to tariff risks is a tall order**. After all, **unpredictability is a feature**, not a bug, **of Trump 2.0, tariffs and all**. And more likely than not, President *Trump will be inclined to keep his audience on their toes*. He does know a thing or two about getting (TV) ratings up and truly believes in zero-sum games. So **not every bluster will turn out to be a bluff**.

- Proliferation of AXJ Pain: Instead, what's likely is a **proliferation of AXJ pain** from **tariff threats**. **Direct impact from bilateral US confrontation** is **a notable, understated** (given current US-China focus) **threat**. But *Vietnam*, *Taiwan* and *Korea* are imaginably at risk of direct trade pressures (and attendant FX wobbles) *if Trump's bilateral, bottom-line, zero-sum game instincts are not tamed.* And **JPY could cut both ways**, **dragging AXJ** *on the way down* given trade links and *equally via "carry squeeze" on the way up.*

- Triggers & Transmission: But **averting direct confrontation is no real comfort**, given various transmission channels of shocks from global trade upheaval. Most conspicuous are **CNY ripples** owed to *sweeping and inextricable linkages with China*. **Spill-over EUR drag**, should Trump make good EZ tariff threats, is another channel. And transmissions from **indirect commodity shocks** could also show up.

- With "Beta" Discrimination: And this so-called **"beta"** (sensitivity to) **will vary across AXJ**. **Commodity beta** *variations even more stark across producers and importers* Notably **"CNY beta",** will be *differentiated for trade/investment/ geo-political exposure.* In fact, some **AXJ may exceed corresponding CNY losses**.

- Devil in the Dynamic Details: Notably, **commodity FX** (AUD, IDR.) may **far more sensitive to onshore China stimulus triggers**. And the **trade sensitivities in other supply-chain reliant AXJ** may be further differentiated. ***Upstream trade assaults***, which restrict China's technology access are likely to adversely impact KRW, TWD and JPY most. Whereas downstream impact flows more to ASEAN FX (e.g. THB, MYR).

- (Initial?) Fed Exceptionalism: Moreover, **a tariff-enhanced version of Fed exceptionalism** on **perceptions of accentuated (hawkish) Fed divergence,** is **primed to accentuate AXJ pain**. Specifically, as the *Fed's inclinations to guard against inflationary tariffs effects contrasts with Asian central banks (ACBs) instinct to (pre-emptively) insure against gathering trade headwinds. So,* until the Fed resumes easing ***sharper* policy trade-offs** (rate cuts vs. FX backstop) **for ACBs amplify downside AXJ sensitivities from tariff risks**.

- But Two Halves with Back-End Relief: ***But*** *that said,* **AXJ pain from Trump 2.0 tariff turbulence** coupled with Fed-ACBs divergence **may not be unremitting.** Instead, **partial *relief, albeit fragile, may be set to* emerge** in **H2 2025/late-2025** (into 2026). Especially if the trade conflict settled into negotiated compromises rather than an escalatory spiral. For all his **unpredictability Trump** is likely to angle for a deal. Caveat being, non-**linearity** and **bumpiness will feature for now**.

- 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**.

**Rates**

- "Trumpflation Buoyancy" in Yields: **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.

- Restoring Risk Premiums: ***Despite tariff risks*** landing square **on EM Asia, risk premium expressed in yield spreads** (vs. USTs) are *unusually* and e*xceptionally suppressed.* Interrupted term premium restoration in the UST yield curve is only a partial, but insufficient buffer. We **expect risk re-pricing to widen Asia HY-UST spreads as the allure of "all in" returns from HY diminishes** *with increasing uncertainties,* largely offsetting rate cuts. Even low yield spreads appear to be too compressed in relative terms.

Fig 1e. Risk-repricing Hits High-Yielders

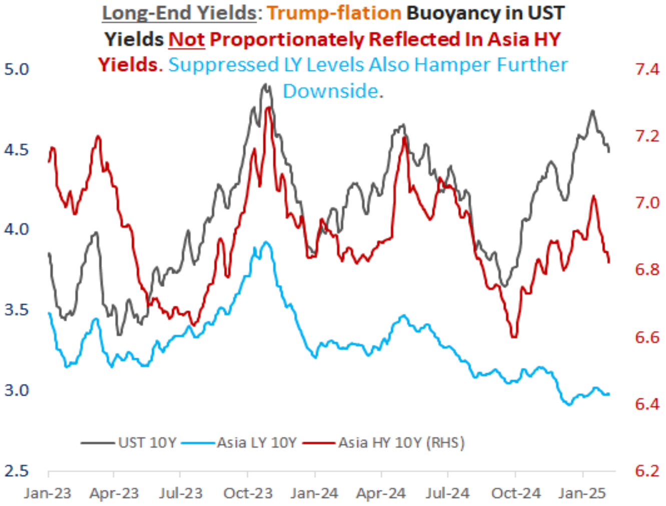
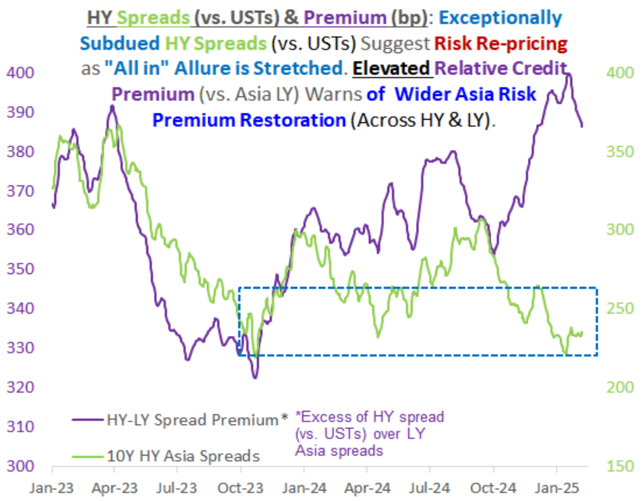



Figure 1f. Trump-flation Hampers Lower Yields

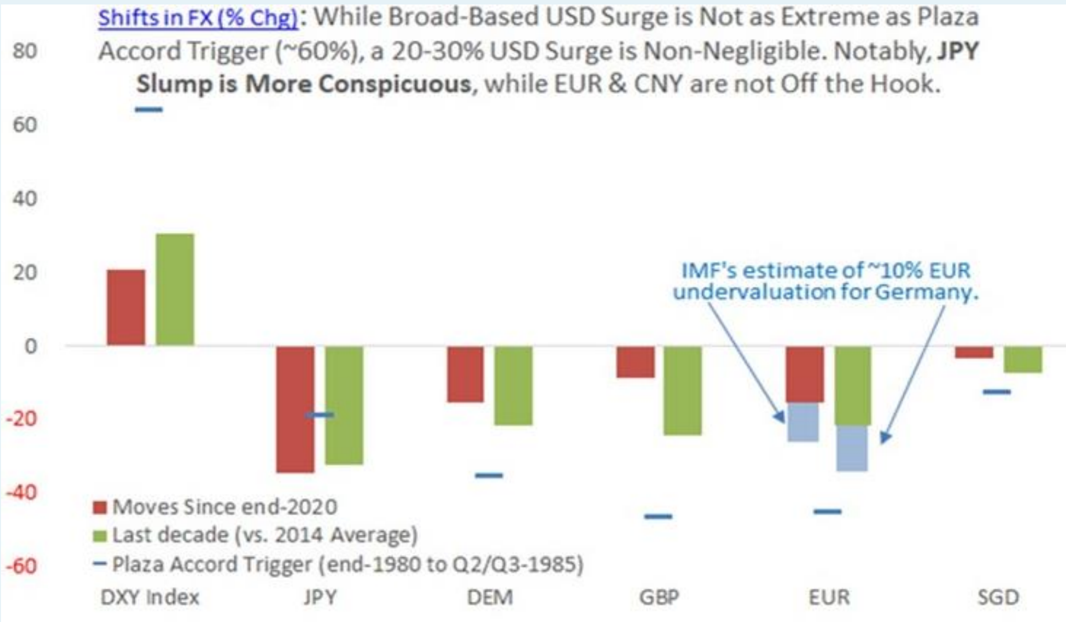


**Box 1: Macro Tail Risks: The "Trump" Plaza**

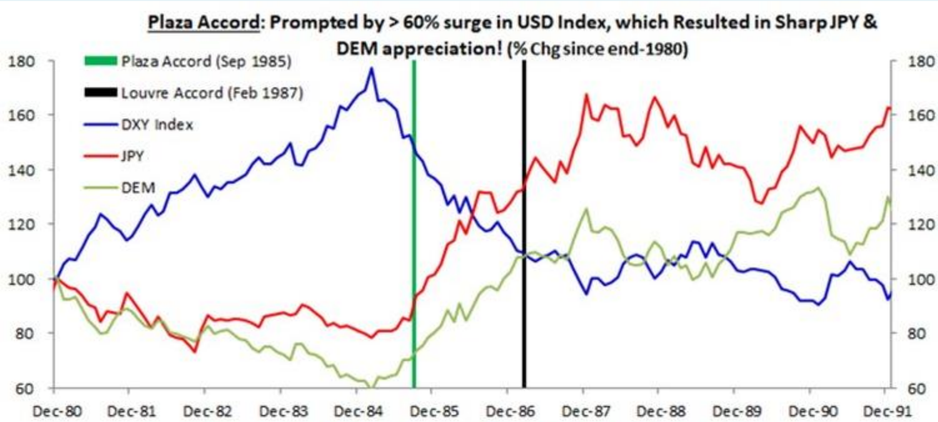
*"Never tell me the odds" – Han Solo, Star Wars (The Empire Strikes Back)*

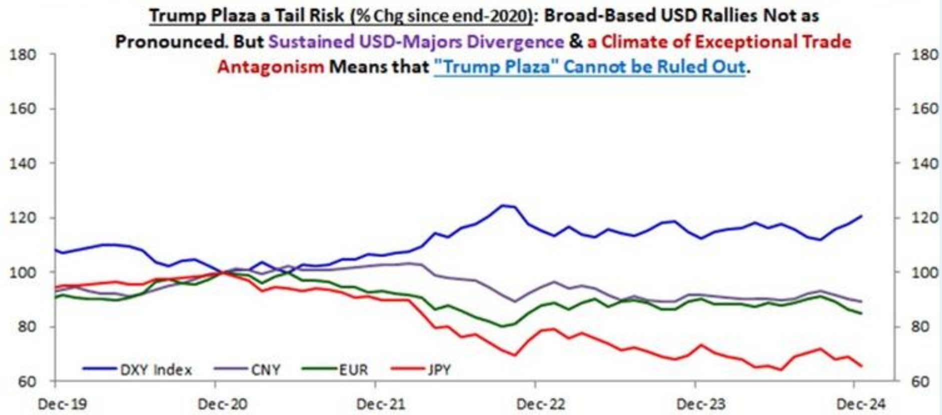
In a Nutshell:

- A **Plaza Accord-type reflex** from the Trump Administration is *admittedly* **a "tail risk"** (*of* *extreme consequence but very low probability*).
- Especially given **broad-based currency valuations** (vis-à-vis the USD) ***have not diverged as violently as compared to the 1980-1985 Plaza Accord run-up***. **Nonetheless**, coordinated policy action to revalue major currencies (JPY, EUR) higher (and soften the USD) **cannot be dismissed summarily**.
- Not *when global trade antagonism is exceptionally elevated* amid US tariff threats. **Perversely**, *currency pressures* on US partners *from* **tariffs threats** may **increase the odds of a "Trump Plaza" outcome**.
- Upshot: With **JPY exceptionally undervalued**, *USD significantly stronger* (on broader measures) and the *US intent on forcefully correcting trade imbalances*, **nothing is off limits**.
- Especially **insofar as a carefully managed calibration of currencies** (vs. USD) **helps to achieve the USD's dual objective** of an *uncontested reserve currency* yet *sufficiently competitive.*
- ***While certainly not the first resort***, there is **an identifiable path to Trump Plaza** (Plaza Accord 2) **amid heightened geo-economic tensions**.
- If this comes to bear, the ***sharpest appreciation shocks may come through the JPY*** with **significant collateral damage** *to Nikkei and risk sentiments amid "carry unwind".*
- ***AXJ assets could inevitably be swept up in volatility*** *and* ***pressured****. Although opposing FX (appreciation) forces via JPY and CNY cues will obfuscate the "end game".*




- The Trump Plaza (Accord 2.0) Tail Risk: The **"Trump Plaza"** reference is less to real estate and ***tail risks*** (*of* *extreme consequence but very low probability*) ***of the 1985 Plaza Accord-types of event trigger**** from this Trump (2.0) Administration.
- Exceptional USD Strength - Subduing Excessive & Unabating: Specifically, flagging the risk of **exceptional USD strength, if unabated, triggering** the possibility of **a coordinated G10/Major central banks/Finance Ministries plan** *to guide check extended, excessive and unabating USD strength.*
- Orderly Markets & by Order of US Manufacturing Ambitions: The stated aim of this Plaza Accord-type course will be **to restore orderly FX markets to remove trade distortions**. Notably, **US ambitions to revive strategic manufacturing advantage** also features.
- Critics of Scale & "Success" Not Wrong: Critics of the idea have good reasons to reject the idea of a Plaza Accord reboot 40-years on. For one, the experience of *materially higher FX imbalance thresholds* and *lessons of mixed success*




- JPY is the Sore Thumb: Notably, JPY is more than 33% weaker (vs. the USD) since end-2020, ***reminiscent of Plaza Accord-type perceived currency imbalance***.
- EUR Masks Trade Imbalance: Sure, EUR is "only" 15% softer (vs. USD) from end-2020. *But IMF estimates of EUR being ~10% undervalued for Germany* is smoking gun for a US Treasury inclined to re-balance currency shifts based on effective German-led trade imbalances with the Euro-zone.
- CNY a Chronic Undervaluation: And while CNY slippage is deemed even less extreme, it is less the recent depreciation than it is notions of chronic undervaluation.

- The Balanced USD "Bessent Agenda": Crucially, **Treasury Secretary Bessent's desire for** a **USD uncontested** in its position **as the global reserve currency *but not untenable*** (from excessive strength) ***as a globally competitive manufacturer***, arguably **can square with coordinated calibration of USD strength.**
- Albeit Requiring Steady Hands: The caveat is that this attempt at surgical precision in recalibrating a "Goldilocks USD" requires exceptionally steady hands, given two-way risks associated with reflexivity.
- Mitigating Uncontrolled USD Tailspin: **Bessent's time in stress-testing FX markets** and **structurally far less desirable fiat alternatives** (in other Majors) may **mitigate risks of setting off a disorderly plunge in the USD**.
- The "Louvre" Fear Lingers: Nonetheless, **memories of** the ***"Louvre Accord"*** *subsequently required to arrest excessive USD weakness* **warns of inadvertent oversteer** if "reflexivity" risks take hold.
- Underpins "Tail" & Tool: Accordingly, this, **puts the "tail" in Plaza Accord reboot risks**. *But while* a **"Trump Plaza"**, so to speak, is clearly **not the first port of call**, it would be a *mistake not to recognize it as* ***a potential tool in the box for strident trade hawks***.
- JPY the Most Pronounced Risk?: ***If "Trump Plaza"/Plaza Accord 2.0* tail *risk materialize*, sharp revaluation shocks may be most pronounced in the JPY**. Not only *given the depth of JPY fall,* but perhaps from *memories of* the *original Plaza Accord.*
- Adverse Nikkei & "Risk Off" Spill-over: In which case, the collateral damage from a **coincidence of *adverse Nikkei spill-over*** and "***carry unwind" accentuating "risk off"*** may be considerable.
- CNY Cues & AXJ Stress: Consequently, **AXJ assets could also come under pressure**, although the *opposing FX (appreciation) forces from JPY* and (imaginably) *CNY cues* will **create tensions** and **set off attendant volatility**.

** To realign Major currencies higher (vis-à-vis the USD) to address entrenched trade imbalances*

*** Extrapolated from the 7.5% from the IMF Article IV, (conservatively) adjusted for a drop in EUR since.*

## CNY: A Brief Relief

| | Q4 2024 | Q1 2025 | Q2 2025 | Q3 2025 | Q4 2025 | Q1 2026 |
|---|---|---|---|---|---|---|
| **Policy Rate (%)** | 1.5 | 1.3 | 1.1 | 0.9 | 0.9 | 0.9 |
| **USD/CNY** | 7.04-7.38 | 7.10-7.55 | 7.15-7.60 | 7.05-7.45 | 6.98-7.37 | 6.97-7.26 |
| | 7.28 | 7.32 | 7.38 | 7.23 | 7.12 | 7.12 |
| **GDP (% YoY)** | 5.4 | 5.0 | 4.9 | 4.8 | 4.7 | 4.5 |
| **CPI (% YoY)** | 0.2 | 0.4 | 0.1 | 0.1 | 1.0 | 0.5 |

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

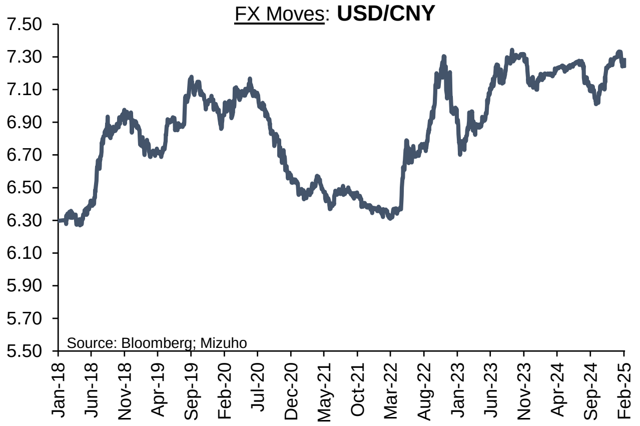



Fig 2b. Continued deflationary pressure onshore

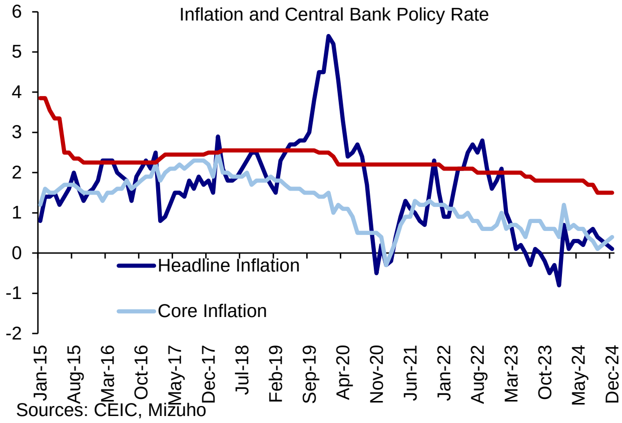



Fig 2c. PBoC scaled up CNH bill issuance

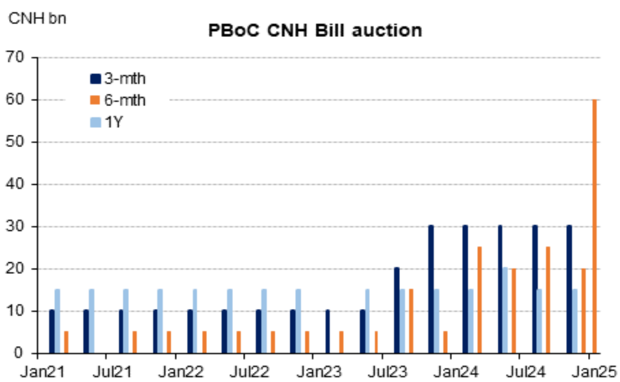



Fig 2d. CNH-CNY gap narrowed after the holiday


**FX**

- 10% tariff implementation: Following a flurry of tariff comments, US President Trump delivered the broad 10% tariffs plan on USD 520bn Chinese goods. In response, China imposed a 10-15% levy on around USD 14bn of US energy/oil and agricultural equipment imports out of the total USD 164bn imports from the US. Overall, market participants perceived this development as mildly positive, as Trump moved away from the extreme 60% tariff hike plan and China's retaliation were proved to be mild. In addition to the tariff arrangement, the surprising Trump-Xi call before Trump's inauguration and Trump's reprieve on the prohibition of the Chinese video-sharing platform fuelled optimism about the China-US relationship in its early stages. With the worst-case scenario avoided, the RMB experienced a brief relief in the week of Trump's inauguration.

- RMB Respite: The CNH spot strengthened to below the 7.3 level for the first time in 2025 after Trump's inauguration. The RMB market showed signs of stabilization, with a narrowing CNH-CNY spot gap. The USD/CNY spot also moved away from the top of its 2% daily trading band based on the CNY fixing. After the Spring Festival, the PBoC capped the CNY fixing below the 7.2 handle, signalling the status quo to preserve FX stability amid heightening trade tensions

- New RMB liquidity facility: PBoC Governor Pan revealed that the HKMA would establish a RMB 100bn liquidity facility for trade finance. We believe that the new CNH liquidity facility for trade finance aims to mitigate the adverse impact of the recent CNH liquidity squeeze on trading or other financing activities, following the expansion of PBoC's CNH bill issuances amid mounting RMB depreciation pressure. With the new longer-term trade financing funding facility mitigating the side effects on CNH liquidity squeeze, it will pave the way for more active CNH liquidity management as a tool to defend the currency, with more often and expansion of CNH bill issuances.

- US tariff uncertainties drag on: Despite a less negative start to the China-US relationship, US tariff uncertainties are set to keep the RMB under pressure. Considering Trump's unpredictability in negotiations, RMB sentiment is likely to remain fragile, coupled with amplifying market volatilities. Following a relief rally, the RMB could come under pressure again due to tariff uncertainties. The wide US-China interest rate gap, with the 10Y UST – CGB yield gap at a record large 3%, also poses a major headwind for the RMB exchange rate.

**Rates**

- Persistent deflation pressure: Despite a 5.4% YoY increase in 4Q, China's GDP deflator declined at a faster pace of 0.7% YoY, down from the 0.5% decrease in Q3, highlighting persistent deflation pressures. Amid expectations of upcoming monetary easing, onshore rates rallied broadly last December, with 1Y and 10Y central government bond (CGB) yields hitting historical lows of 0.881% and 1.597%, respectively. Additionally, China's 30Y CGB yields have remained below their Japanese counterparts for the third consecutive month, with spreads widening further in January.

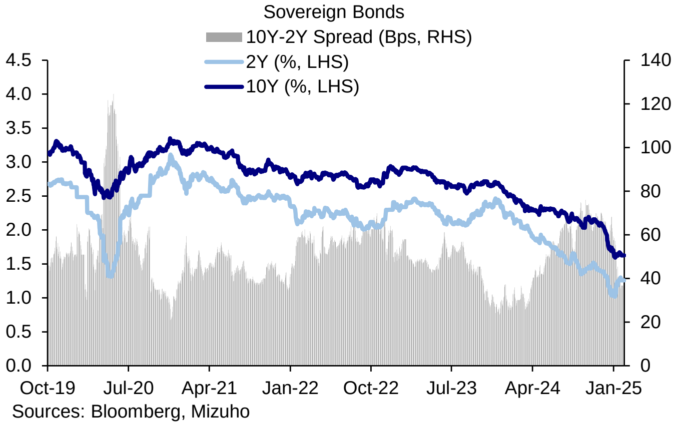
- Rally cooled, for now: In response, the PBoC implemented several measures to curb excessive market speculation. These included skipping the promised RRR cut at the year-end, suspending repurchases of CGBs from the secondary market, and withdrawing interbank liquidity through open market operations for three weeks in a row. These actions proved effective, with 7D repo rates rising notably above the upper band of 2% and term spreads significantly flattening.

- The patient PBoC: However, we anticipate that the PBoC will soon refocus on guiding lower bank deposit rates by allowing gradually declining CGB yields at the front end. Despite the skipped RRR cut in December, senior PBoC officials have promised further interest rate and RRR cuts at a more appropriate time to support economic growth. We believe this RRR cut is delayed rather than canceled, especially with increased market turbulence as Trump unveils his full China policy in the coming months.

- Yields: Overall, yields may remain range-bound in the short term as the Lunar New Year holiday (28 January – 4 February) adds to seasonal volatility. We expect front-end CGB yields to moderate after the 8-day holiday and remain relatively subdued over the next few months as the PBoC rolls out more easing measures.

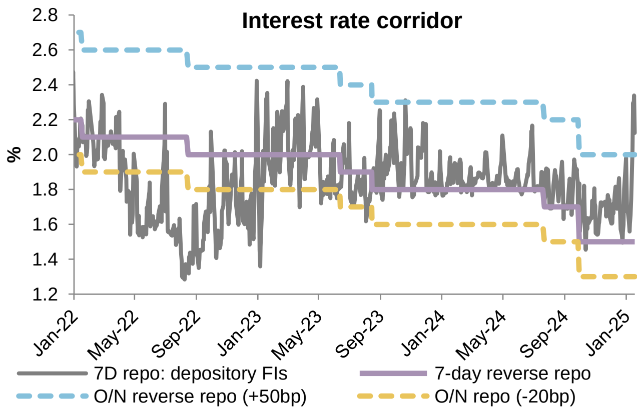
- Curve: Given the likelihood of increased market volatility, term spreads are likely to move sideways in the near term. However, we expect the term spread to widen over the longer term, with 10Y CGB yields being propped up back to around 2.0% by reflationary policies.

Fig 2e. PBoC averts unwanted flattening




Sources: Bloomberg, Mizuho

Figure 2f. 7D repo rates rose notably in January



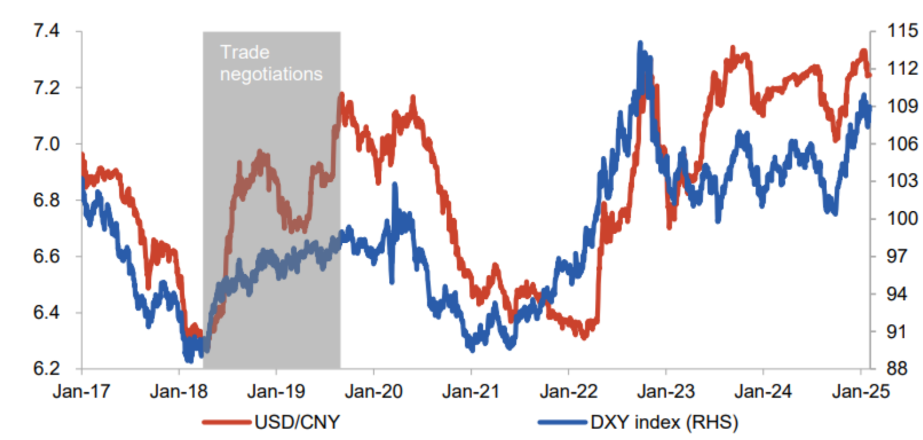
### Box 2: Tariffs 2.0: No man ever steps in the same river twice

**The Trump administration has imposed an additional 10% tariff on imports from China, effective February 4. In retaliation, China has announced tariffs of up to 15% on a range of US goods. Despite these measures, the market reacted with cautious optimism as China's response was relatively restrained and avoided tariffs on US agricultural products. Consequently, the Hang Seng China Enterprise Index rose by 3.51% on the same day.**

**While the future of China-U.S. trade disputes remains uncertain, we believe it is unlikely to mirror the trade war of 2018-19, given the significantly altered circumstances.**

**RMB depreciation?** It would be a knee-jerk reaction for the market to assume that China would allow significant depreciation of the RMB to offset the impact of the additional tariff. When China-US trade tensions escalated rapidly in 2018, the CNY spot rate was at its strongest level since China reformed its FX rate pricing mechanism in August 2015. Even after the weakening during 2018-19, the CNY spot barely surpassed its weakest level seen in 2016 and remained within the key level of 7.0 against the dollar (Fig 1).

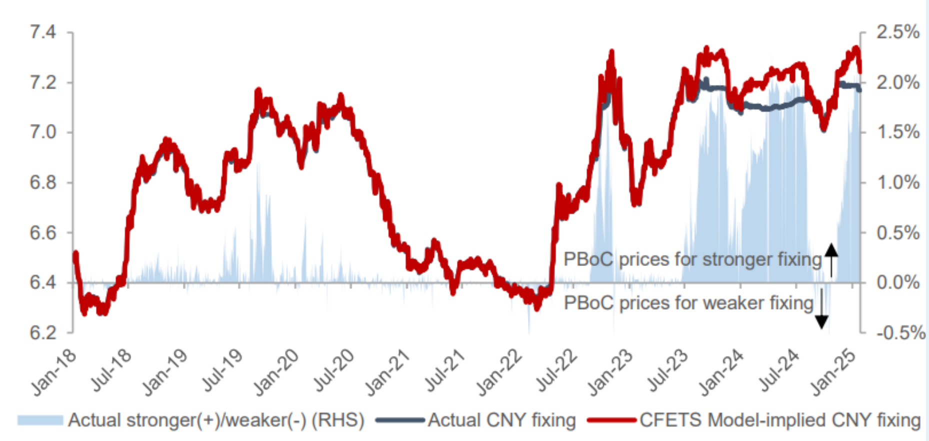
**Fig 1** The RMB is now in a much weaker position compared to early 2018




Source: Bloomberg, Mizuho

However, the situation has changed significantly. Prior to Trump's inauguration in January, the CNY spot traded close to 7.35, its weakest level since 2007. Any sharp depreciation beyond this level or signs that the PBoC is loosening its grip on the RMB fixing rate (Fig 2) could trigger massive selling pressure on the RMB and unleash market expectations for further depreciation. We believe the last thing Chinese policymakers want to see is soaring volatility in the FX and financial markets as they are working hard to revive economic sentiment onshore.

**Fig 2** The PBoC has significantly ramped up its support for the RMB fixing rate




Source: Bloomberg, Mizuho

**Tariff Retaliation?** Although China has responded with a 15% tariff on US coal and LNG and a 10% tariff on crude oil, agricultural machinery, and large displacement vehicles, this response is considered relatively restrained. In fact, there is very limited room for China to adopt tariff retaliation without significantly disrupting the daily operations of its domestic enterprises, not mentioning that China's imports from the US totaled USD164b in 2024, only one-third of its exports to the US.

Instead, it would be in China's interest to uphold its role as a defender of the world's multilateral trading system, resolving trade disputes through the World Trade Organization and bilateral dialogue. Last December, former PBoC governor Yi Gang publicly stated that the best economic response to US tariffs is to stick to free-trade practices. China is reportedly also considering other options, such as promising more purchases of US agricultural and energy products, increasing FDI in US manufacturing, and offering more leeway in a potential TikTok acquisition during negotiations with the US. While imposing widespread retaliatory tariffs may not be the best option for China, it always remains an option during trade negotiations with the US.

**Muted Growth Impacts?** Despite the imposition of additional tariffs since 2018, current levels of Chinese exports directly shipped to the US remain higher than those seen before the trade war (Fig 3). Additionally, China's share of exports to ASEAN has steadily increased, as some exports are routed through ASEAN countries for final assembly and packaging to circumvent the 25% tariff (Fig 4).

**Fig 3** China's trade with the US remains resilient

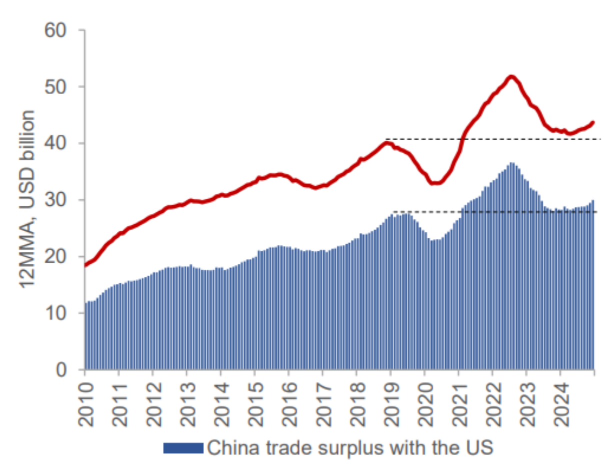
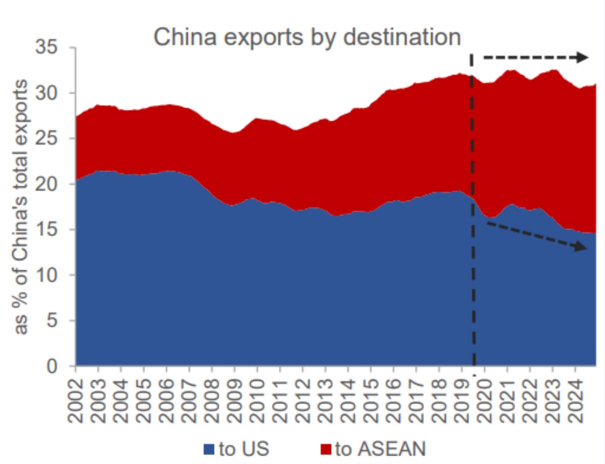



**Fig 4** A rising share in China's exports to ASEAN




Source: CEIC, Mizuho

For exports shipped directly to the US, studies[1] show that US importers absorbed approximately 94% of the higher costs immediately after additional tariffs were imposed (Fig 5). As the tariff rate reached 25%, more importers began passing these increased costs onto final consumers (Fig 6).

**Fig 5** Us import prices indices (incl. tariffs) jumped after tariffs

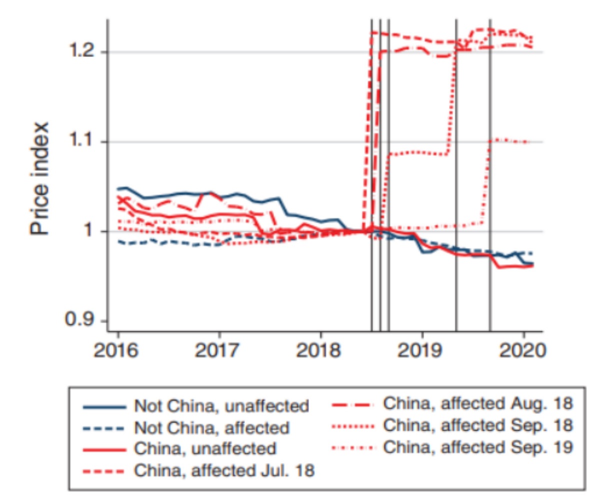
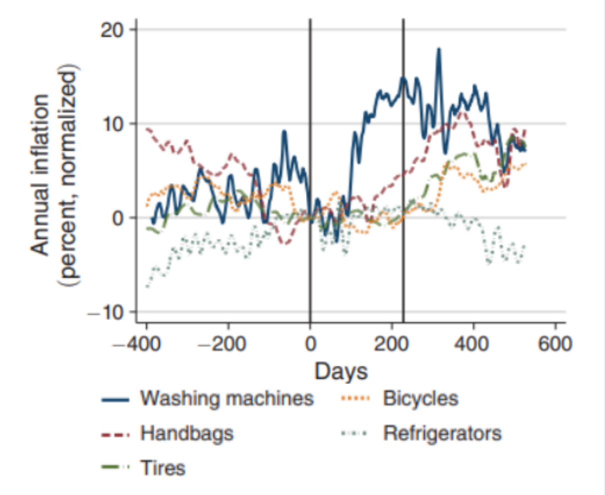



**Fig 6** US importers passed increased cost to consumers within a year




Source: Cavallo, Alberto, Gita Gopinath, Brent Neiman, and Jenny Tang.

Additionally, the US has become more vulnerable to imported inflation compared to pre-COVID days. With US inflation rates running notably above the Fed's 2% target, additional tariffs on imports from China (15% of total imports), Canada (13%), Mexico (15%), and potentially the EU (16%) together may significantly derail the FOMC's current balance in achieving its dual targets of maximum employment and moderate inflation.

[1]Cavallo, Alberto, Gita Gopinath, Brent Neiman, and Jenny Tang. 2021. "Tariff Pass-Through at the Border and at the Store: Evidence from US Trade Policy." American Economic Review: Insights, 3 (1): 19–34.

## HKD: Range trading

| | Q4 2024 | Q1 2025 | Q2 2025 | Q3 2025 | Q4 2025 | Q1 2026 |
|---|---|---|---|---|---|---|
| USD/HKD | 7.76-7.80 | 7.75-7.79 | 7.75-7.79 | 7.75-7.79 | 7.76-7.80 | 7.76-7.80 |
| | 7.77 | 7.76 | 7.76 | 7.75 | 7.76 | 7.77 |
| GDP (% YoY) | 2.4 | 1.0 | 1.1 | 2.5 | 2.9 | 3.3 |
| CPI (% YoY) | 1.4 | 2.3 | 2.9 | 2.5 | 2.3 | 2.1 |

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

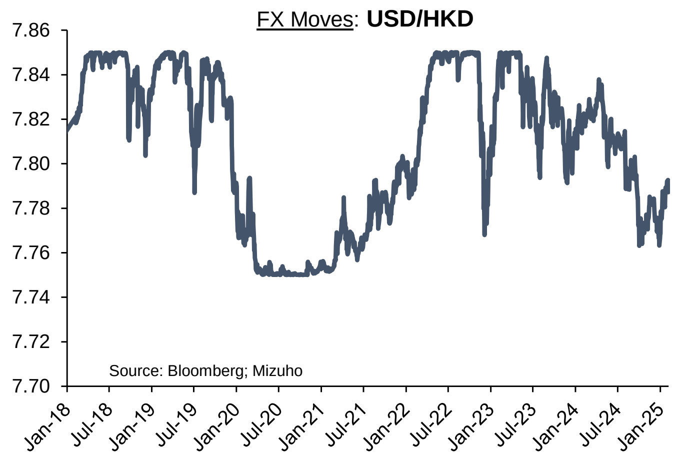



Fig 3b. Subdued underlying inflation

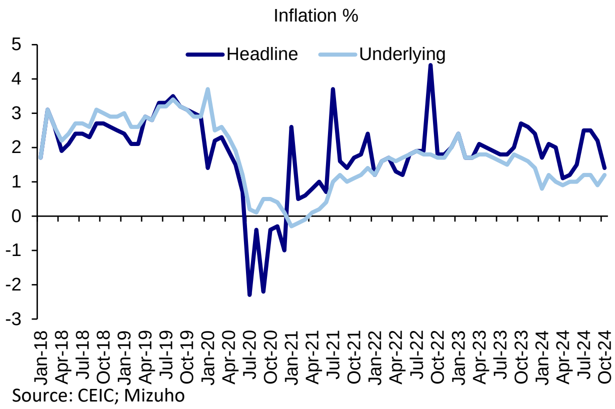



Fig 3c. HK equities settlement demand steady

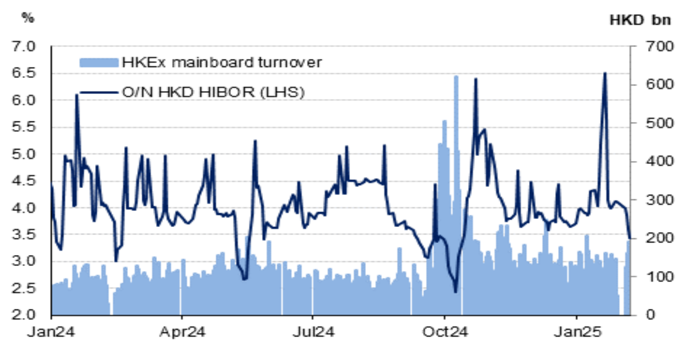
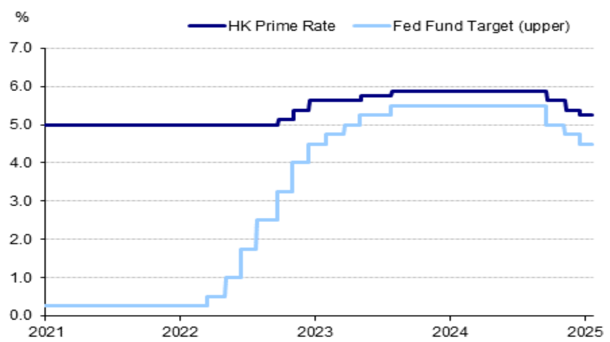



Fig 3d. Limited room for further prime rate cut




**FX**

- Range-trading: The HKD spot weakened from 7.76 to near 7.79 level as the HKD-USD interest rate spread turned back negative at the beginning of 2025. The easing of the HKD year-end seasonal liquidity squeeze and waning Fed rate cut expectations contributed to the HKD weakness. Under the guidance to enhance investor returns, some large Chinese enterprises started to pay half-yearly dividends, but the overall size of the flow was relatively small to drive the HKD exchange rate. Due to flush HKD liquidity conditions, the carry trade flow of long USD/HKD spot returned to play, driving the HKD lower. Equity inflow was broadly positive for the HKD. The strong Southbound Stock Connect inflow exceeding HKD 100bn so far in 2025 provided support for HKD purchase demand.

- The new IPO platform: The IPO frenzy did not translate into an HKD rally. Despite the busy IPO listing schedule and oversubscriptions for numerous IPOs, the total amount of funding raised was rather small in the absence of mega corporate listings. In addition, the new IPO platform of Fast Interface for New Issuance (FINI) allows a shorter time gap between IPO pricing and trading and a smaller size of capital for settlement in IPO margin financing activities. As a result, the smaller size and shortened duration of lock-up capital for IPO settlement mitigated their impact on overall HKD liquidity conditions.

- More China FX reserves allocation in HK: At the Asia Financial Forum, PBoC Governor Pan revealed that China would increase the FX reserves allocation ratio on HK assets. The guidance indicates more capital inflow to HK amid USD diversification and provides support to HKD financial asset prices, coupled with higher connectivity between onshore China and HK financial markets. However, the officials refrained from unveiling details on the reserves allocation plan, and HK financial markets were largely muted to the headline.

- Fluctuating in the strong half of the band:. We expect the HKD to fluctuate below 7.8 most of the time as the Fed will likely extend its rate cut cycle for a while. In the absence of Trump's broad and universal tariff plan, the impact on US inflation from Trump's policies should remain limited at this moment. In the meantime, Southbound capital inflow from onshore China is set to continue as Chinese investors seek higher yields via outbound investment channels following a shift to a moderately loose monetary policy. The familiarity and low valuations of H-shares will provide an incentive to onshore investors for HK investments. With the steady HKD spot and forward curve, market participants are not looking for a change in the USD-HKD peg amid Trump's second term.

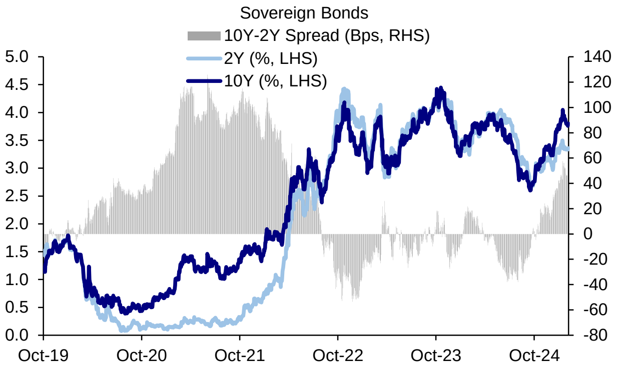
**Rates**

- Flush HKD liquidity conditions: The year-end liquidity squeeze dissipated at the beginning of 2025. Structurally, the subdued HKD loan demand amid macro and property market downturn justified the negative HKD-USD interest rate gap. Indeed, the 1-month and 3-month HKD HIBOR - USD SOFR interest rate gap turned negative on the second day of 2025. The HKMA aggregate balance remained unchanged near HKD 45bn as the HKD spot did not touch the 7.75 or 7.85 level.

- Stock market impact took the backseat: Despite a rebound in the Hang Seng Index, the turnover of HK equities remained relatively subdued compared to the period in October 2024, and the steady HKMA aggregate balance is enough to cover HKD settlement demand. As mentioned, the new IPO platform of FINI shortened the duration of the IPO capital lock-up period as well as the capital size. The impact from equity flow and IPO activities on the HKD interest rate side proved to be limited.

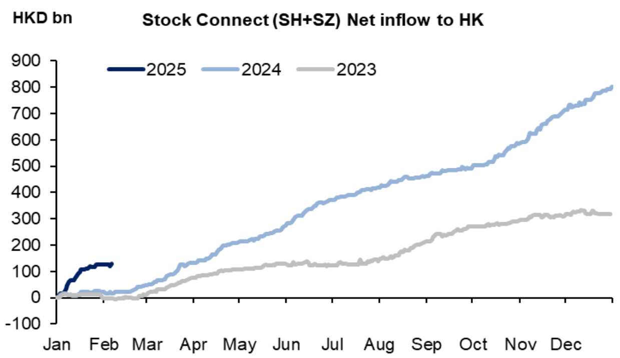
- Track on USD rates: With the USD-HKD peg expected to hold in the foreseeable future, the HKD IRS tracked USD IRS. The 3Y HKD IRS was hovering near 3.7% vs. 4.1% for USD IRS. As the Fed likely frontloaded rate cuts in Q4-2024 and reserves less room for further rate cuts, the carry of entering HKD IRS (customer pays fixed 3Y HKD IRS, receives floating 3-month HKD HIBOR) narrowed significantly to near 20bps.

Fig 3e. HKGB term premium tracked on UST




Sources: Bloomberg, Mizuho

Figure 3f. Stock Connect inflow continued in 2025




Sources: Mizuho

# INR: (Bearish) Hysteresis

| | Q4 2024 | Q1 2025 | Q2 2025 | Q3 2025 | Q4 2025 | Q1 2026 |
|---|---|---|---|---|---|---|
| **Policy Rate (%)** | 6.50 | 6.00 | 5.75 | 5.50 | 5.25 | 5.25 |
| **USD/INR** | 84.1-85.8 | 85.4-88.5 | 86.2-88.9 | 85.5-88.9 | 85.2-88.2 | 84.8-87.8 |
| | 85.6 | 87.1 | 87.8 | 86.5 | 86.0 | 86.0 |
| **GDP (% YoY)** | 6.2 | 5.9 | 6.5 | 6.3 | 5.4 | 5.3 |
| **CPI (% YoY)** | 5.4 | 5.0 | 4.9 | 4.2 | 5.6 | 5.4 |

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

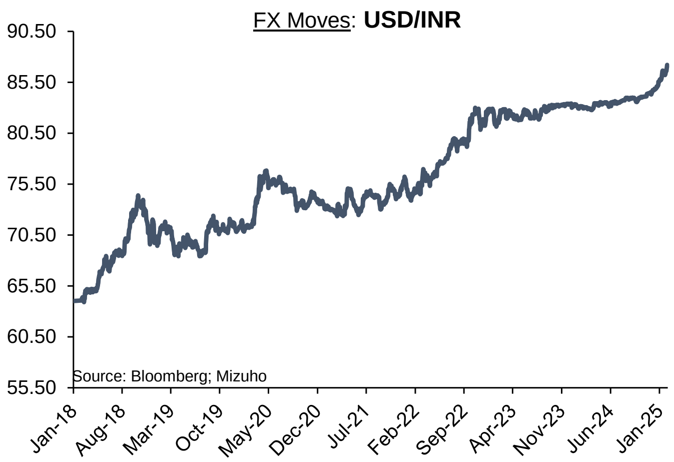



Fig 4b. Rupee Catches Down with AXJ Peers

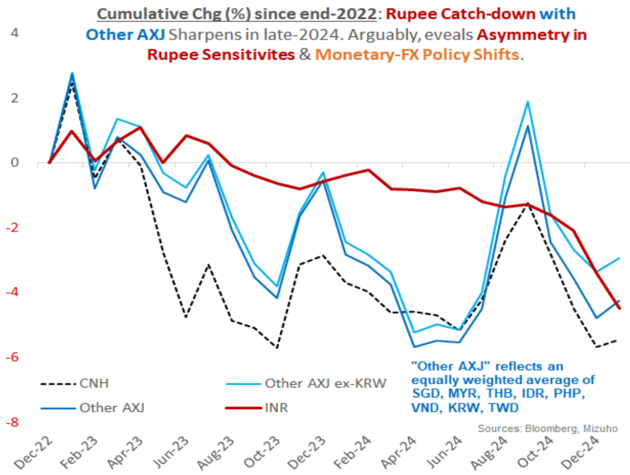



Fig 4c. Struggles to Track Broader AXJ Bounce

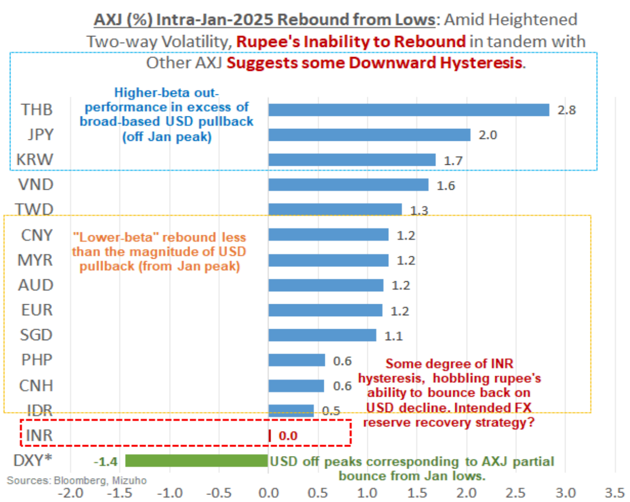
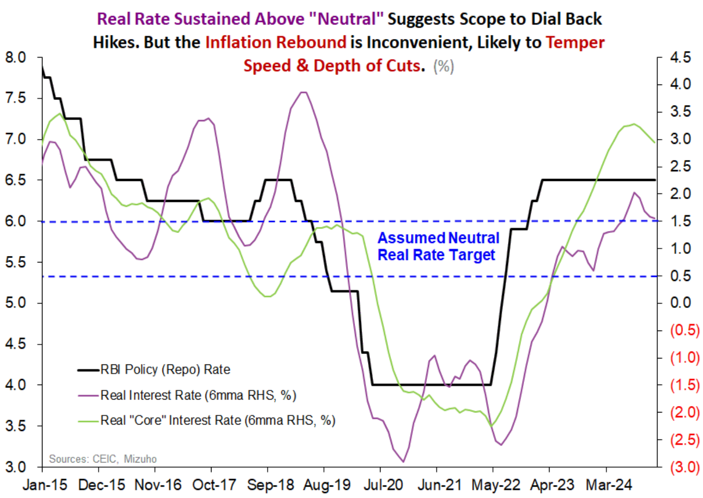



Fig 4d. FX Reserves




## FX

- Marked Under-performance: **In sharp contrast to lower-beta, steady rupee dynamics** evident from H22023 through October 2024, **rupee** appears subject to **marked under-performance** since late-2024. **Partly**, this may **be "catch-down" with other AXJ**. But equally, *hints of bearish dynamics cannot be ignored.*

- Asymmetric Sensitivities: Notably, the **inability of the rupee to rebound** *in tandem with other AXJ in* January, speaks to **asymmetric rupee sensitivities**. Specifically, a rupee that is *more sensitive to depreciation pressures than it is sympathetic to broad-based AXJ rebound.*

- (Bearish) Hysteresis: Crucially, rupee's asymmetric sensitivities (inclined to relatively greater weakness than gains) may not be a blip. Instead, it **could underpin some degree of bearish hysteresis**, *which accommodates more structural and sustained rupee* weakness. Conveniently, a **relatively weaker rupee outcome squares with "Make in India" ambitions** underlining the major economic policies of Modi 3.0.

- Dovish RBI Compromises Traction: What's more, a **distinctly dovish RBI**, *set to initiate a meaningful cutting cycle,* **compromises rupee traction**. To be sure, despite mild reversal of dis-inflation, **exceptionally elevated real (core) rates mean that scope for RBI cuts is merely moderated**, not overturned.

- Adverse Growth Shock: What's more, the **adverse growth shock**, entailing an **unexpectedly sharp deceleration in GDP** (Q3/FYQ2 GDP stumbling to 5.4% from 6.7%) **further dims rupee**. Especially given a **double whammy** of; i) ***lost halo effect*** from stand-out growth narrative/allure, and; ii) **real returns compressed** by simultaneously softer growth and higher inflation.

- Fiscal Edge Blunted by "Twin Deficits": *Moreover,* any hypothetical **rupee edge from incremental (0.1%-pt) fiscal consolidation** to 4.8% (FY25) and 4.4% (FY26) is **blunted by the "twin deficit" handicap**. Especially without the cover of compelling growth out-performance (and/or inflation discipline).

- Oil & Troubled Waters: Similarly, rupee buoyancy from subdued oil prices is hobbled as **India's ability to benefit from Russian oil is surrendered** to US dominance in troubled geo-political waters.

- INR Outlook: Inevitably, risks are tilted to **pronounced USD/INR upside that proves stickier**. Especially given the **propensity to rebuild FX reserves**, *after $78.3bn was burnt* since Sep 2024 peak of $616.2bn. Near-term ascendancy to 88 is outlandish, even without the most acute of risk retrenchment. Notwithstanding outlook for USD to mellow into late-2025/early-2026 sub-86 will be a stretch to sustain (and extend).

## Rates

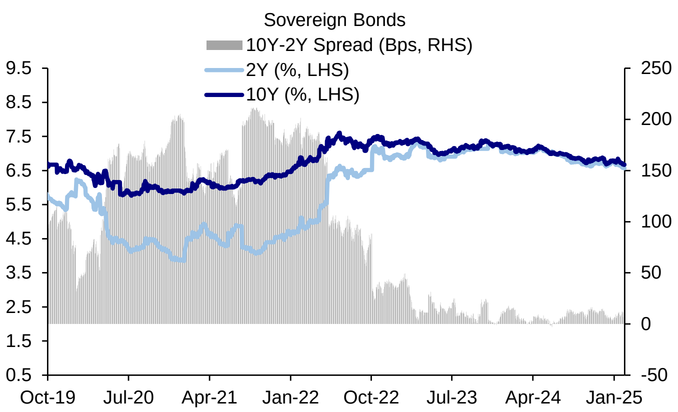
- Central Bank: The RBI's **new central bank Governor Malhotra is likely to preside over a dovish shift,** *swapping exceptional abstinence from easing for judicious activism to pre-empt a hard-landing*. To be sure, Malhotra is **not an unmitigated dove**. So, a bumpy rate cut path contingent on dis-inflation restored is par for the course. But equally, he is ***not inclined to be unduly hawkish*** so the bar to cut is lower.

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

- Yield Pressure Resisted by Spreads: Despite bumped up expectations of RBI the **path to unequivocally softer GOI yields** is **neither clear nor unfettered**. For one, spill-over from *higher UST yields amid "Trumpflation" gets in the way.* Crucially, a **re-widening GOI-UST spreads**; amid rising uncertainty may demand *risk-adjusted re-pricing*. Especially if accentuated by steeper UST yield curve.

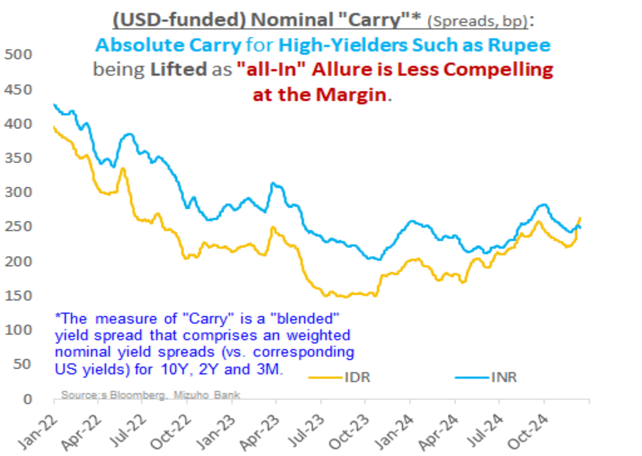
- Steeper Curve on Fiscal Uncertainty: Whilst fiscal consolidation ought to dampen yields, hints of debt-based fiscal targets further out suggest a steeper GOI curve as fiscal uncertainty is priced into the long-end.

Fig 4e. Bumpy and Muted Softening in Yields Expected




Sources: Bloomberg, Mizuho

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



## KRW: Interim Relief?

| | Q4 2024 | Q1 2025 | Q2 2025 | Q3 2025 | Q4 2025 | Q1 2026 |
|---|---|---|---|---|---|---|
| **Policy Rate (%)** | 3.00% | 2.75% | 2.50% | 2.25% | 2.00% | 2.00% |
| **USD/KRW** | 1317-1487 | 1360-1500 | 1370-1540 | 1330-1480 | 1290-1400 | 1280-1380 |
| | 1471 | 1438 | 1442 | 1385 | 1345 | 1340 |
| **GDP (% YoY)** | 1.4 | 1.0 | 1.7 | 2.2 | 2.2 | 2.0 |
| **CPI (% YoY)** | 1.6 | 1.9 | 2.2 | 2.3 | 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 5a. KRW gains on interim political relief

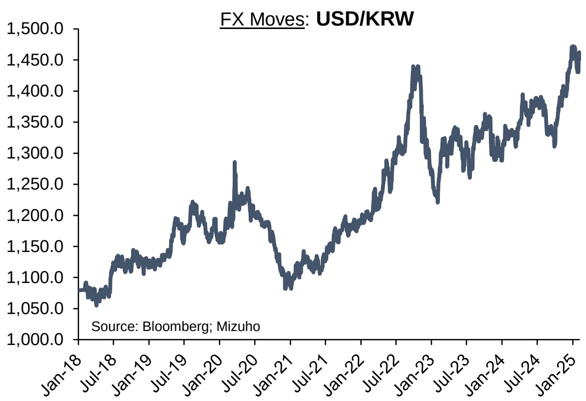
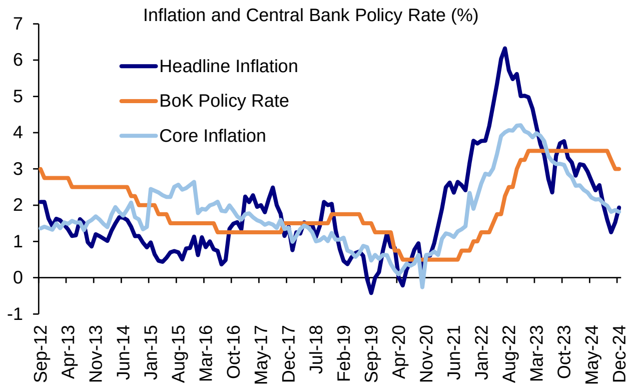
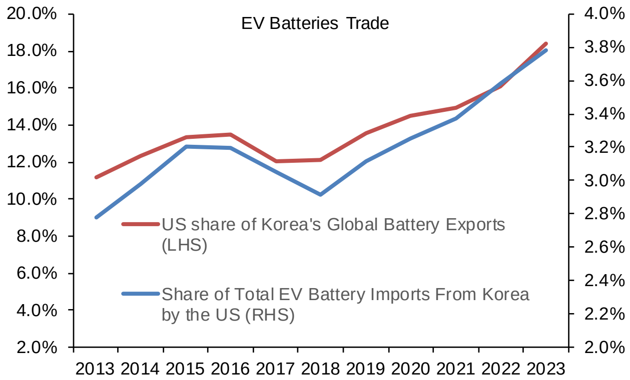



Fig 5b. Inflation remains condusive for easing



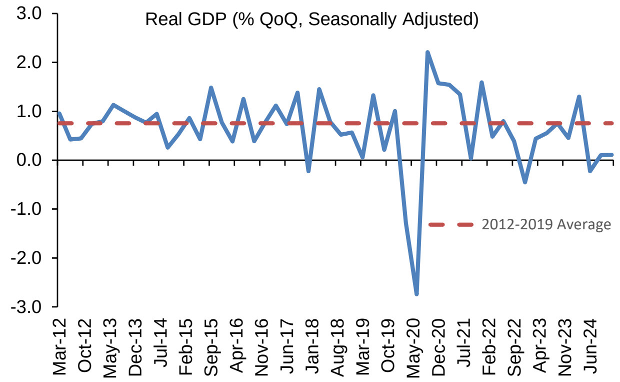

Source: CEIC; Mizuho

Fig 5c. Assymetric spillovers to batteries trade




Sources: UNComTrade, Mizuho

Fig 5d. Growth has been dismal in 2024




Sources:CEIC Mizuho

**FX**

- Interim relief: The KRW has outperformed regional peers with Minister of Finance Choi Sang-mok assuming the role of Acting President has appeared to calm markets amid efforts to ensure ample liquidity and support. That said, the **timeline of next election** remains up in the air as **it is dependent on the resignation or removal** (by the Constitutional Court) **of President Yoon**.

- Contingent on elections: Consequently, elections in 2025 may seek further KRW volatility. Furthermore, markets will continue to assess the impact of Trump's executive orders such as EV credits and plausible tariffs on China. The BoK's rate cut cycle also imply that KRW recovery continues to be subject to fit and starts and may relegate the current outperformance to a middle of the pack one in the months ahead.

- Un-electrified: Trump's removal of incentive for Electric Vehicles will be a setback for automobile and battery sectors with the latter taking a bigger brunt of the hit given their reliance on supplying American companies. While Korea has seen their small share of batteries imported by the US steadily increase over the year, the export demand is at risk of a sharp plunge in 2025 with EV batteries exports to the US taking up almost a fifth of total EV battery exports. These external headwinds will drag on the industrial sector which is already at risk of stagnating. Competition from Chinese automobile companies is also likely to add further strains.

- Election Volatility: Should President Yoon be removed from office or resign, snap elections will be held within 60days. Nonetheless, the twist and turns in the investigation alongside domestic protests from both ends imply that there is **considerable uncertainty over the timeline of the next elections though political pressures may push towards an election in H2 2025**.

- Downbeat Forecast: With overall 2024 growth at just 2% after two quarters of 0.1% QoQ expansion in the second half, the BoK is likely faced with a negative output gap which underpins their overall tendency for an easing cycle as well as our case for a downbeat bumpy KRW recovery.

- Fiscal Boost and Associated KRW Risks: Amid the weak growth, the need for frontloading the 2025 Budget as well as an supplementary Budget has been well acknowledged by the authorities and this may come through in late Q1. That said, fiscal slippage risks may be rising as collections remain weak.

- Balanced flows: As we had expected, foreign inflows into bonds persisted in January to lean against the continued outflows from equities. The WGBI inclusion and worries around corporate profitability and competitive would underpin the persistence of such flow dynamics in the months ahead.

- Multi-Prolong support highlight intensity of headwinds: With KRW's gains partially aided by the National Pension Service's strategic hedging, its outperformance in January should not viewed as a base for outsized rallies. Furthermore, the need for Finance Ministry to issue their forex stabilisation bond (due in 1 year) after 21 years reflects the headwinds facing the KRW.

- Outlook: Buoyancy above 1400 for H1 2025 will be sustained as tariffs threats get re-iterated and negotiations provide two-way volatility and domestic politics weigh. Excessive weakness though will be tempered by National Pension Service hedging. Sub-1400 recovery is premised on more cautious tone of rate cuts in H2 as they signal an approach towards neutral territory even though they are likely to proceed at a steady pace of 25bp per quarter.

**Rates**

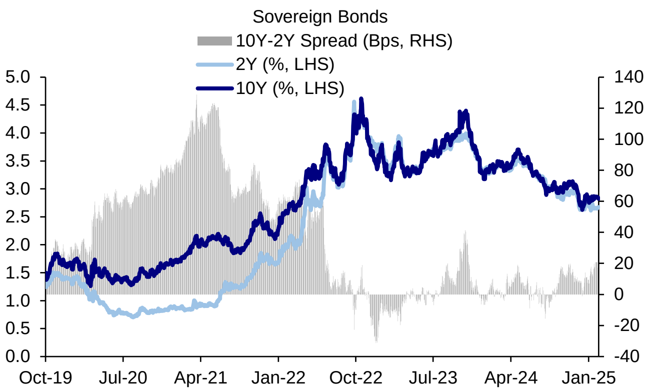
- Central Bank: The BoK's decision to hold in January should not distract from the fact that they **are in a rate cut cycle and given the weak growth outturns**, they are on track for **another cut in Q1**. We expect the BoK cut by **25bp in Q2** and signal a steady pace of cuts to provide support to growth. At this juncture, the BoK is likely to affirm the certainty of easing but proceeded steadily in each quarter. Simply put, this will allow yields to reflect their intent to ease and enable the associated economic passthrough in a bid to provide some overall FX stability and prevent undue panic around financial stability and unforced policy errors.

- Risks: The risk around the baseline leans towards more front-loaded cuts (50bps in Q1 instead of 25) to support the economy and align with fiscal policy support in Q1.

- Yields: Short end yields decline to reflect an increasing bias for the BoK to continue easing while long end yields rose in deference to UST yields.

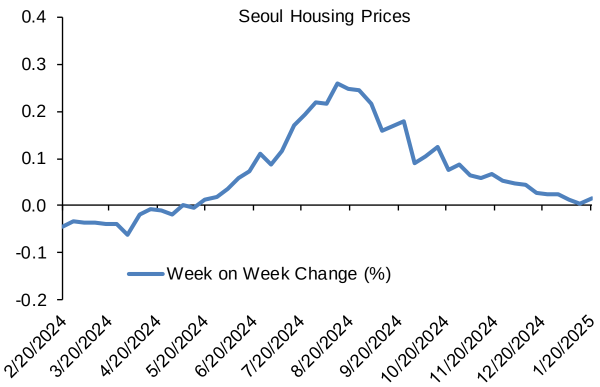
- Curve: The term premium remains extremely compress and ought to widen through the year as the BoK continues their rate cuts which aids curve steepening. The need for continued fiscal support will also keep longer end yields elevated, as such the decline in 10Y yields will lag that of the 2Y.

Fig 5e. Steepening on the cards




Sources: Bloomberg, Mizuho

Figure 5f. Housing price growth continued to slow




Sources: CEIC, Mizuho

# TWD: Deep Thoughts?

| | Q4 2024 | Q1 2025 | Q2 2025 | Q3 2025 | Q4 2025 | Q1 2026 |
|---|---|---|---|---|---|---|
| **Policy Rate (%)** | 2.000 | 2.000 | 1.875 | 1.750 | 1.750 | 1.750 |
| **USD/TWD** | 31.6-32.8 | 32.2-34.5 | 32.1-34.5 | 31.5-33.9 | 31.2-33.5 | 31.0-33.5 |
| | 32.8 | 33.3 | 33.5 | 32.5 | 32.2 | 32.2 |
| **GDP (% YoY)** | 3.2 | 2.7 | 3.2 | 3.2 | 3.0 | 3.0 |
| **CPI (% YoY)** | 2.3 | 2.0 | 1.9 | 2.0 | 1.8 | 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

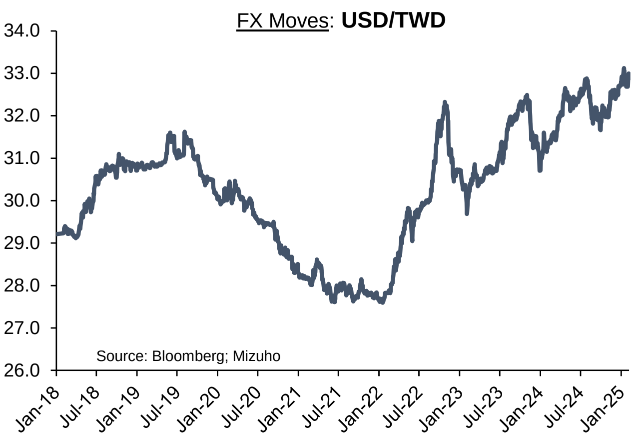



Fig 6b. Core inflation sticky, weather hit headline

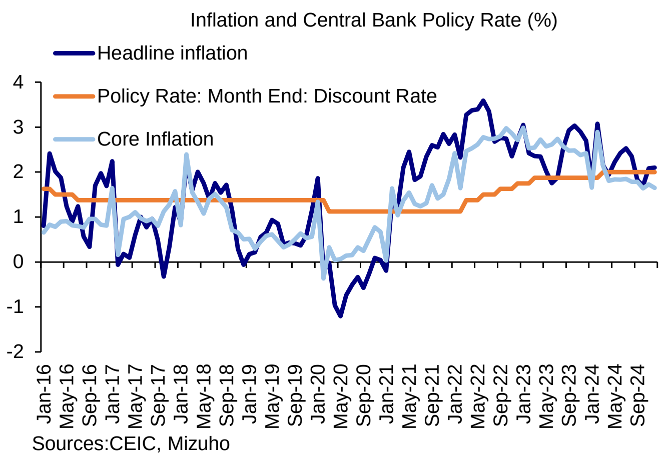



Fig 6c. Semiconductor reliance turns risky

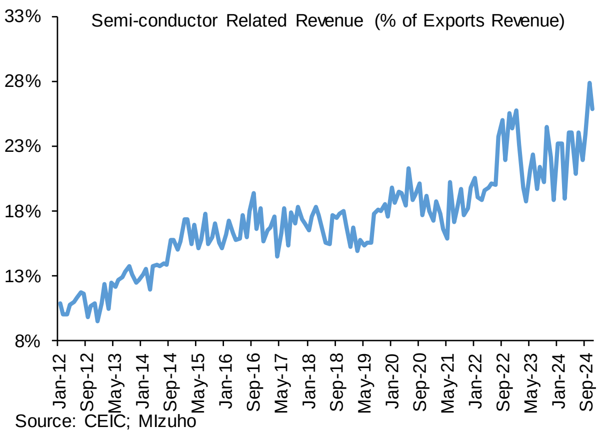
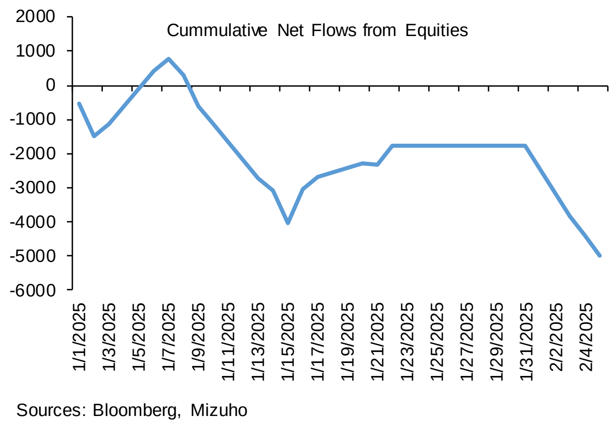



Fig 6d. Equities outflows continued amid tech woes




**FX**

- Rebounded from a 9-year low: The TWD spot slid to its 9-year low of 33.15 level amid the US tariffs threats and broad USD strength. Initial relief from Trump's less aggressive tariff plan and a warm start of China-US relationship in Trump's second term also faded as Trump imposed tariffs on Mexico, Canada and China. In addition, Trump's promotion on the AI development should continue to support AI chips demand from Taiwan manufacturers, fuelling capital inflow into Taiwan stock markets lately. Firmer Taiwan export orders for December also eased concerns over slowing exports growth. Nonetheless, concerns stemming from China's AI Startup DeepSeek which reportedly runs on less powerful chips.

- Currency manipulation under Review: Despite no immediate tariff implementation on Day one of Trump's second term, Trump reportedly ordered his administration to address currency manipulation by other countries. With Taiwan being on the FX monitoring last since June 2022, the TWD is subjected to the risk of being labelled a currency manipulator.

- Defence Still A Key Risk: China has continued to emphasize to Trump's administration that the Taiwan question is most likely to have a disruptive impact on China-US relations. Understandably, differences between the US and China continue to persist on the issue given that the US continues to highlight concerns over the coercive actions of China against Taiwan in the South China Sea. The challenge for Taiwan is not merely about payments given staunch Chinese objection on US sales of weapons to Taiwan.

- Exports Reliance Exposed?: With semiconductor getting an increasingly larger share of exports revenue, recent revelation from DeepSeek showing highly capable AI models built at a fraction of the cost compared to Silicon Valley rivals. Consequently, TWD may come under pressure from downside risk of actual semiconductor demand alongside lofty valuations of its leading semiconductor manufacturers.

- Correction, Not Collapse: That said, even as valuation corrections are probable, the industrial needs ranging from automobiles to military systems alongside the dimension of sovereign needs imply that a sharp collapse in semiconductor demand is unlikely. A renewed global focus on defence implies that underlying demand for chips should remain firm even as tech firm face a reckoning over their capex plans.

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

- TWD outlook: Given these risks, TWD is vulnerable to various trade related under Trump 2.0 may spark sharp depreciation episodes to test 34 levels though we expect such episodes to be brief as the CBC to act and contain such knee jerk reactions. That said**,** defence related threats from President Trump have the potential to turn existential and may have a more durable hit on the TWD alongside sharp correction on semiconductor related equities. 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 again before recovering in H2-2025.

**Rates**

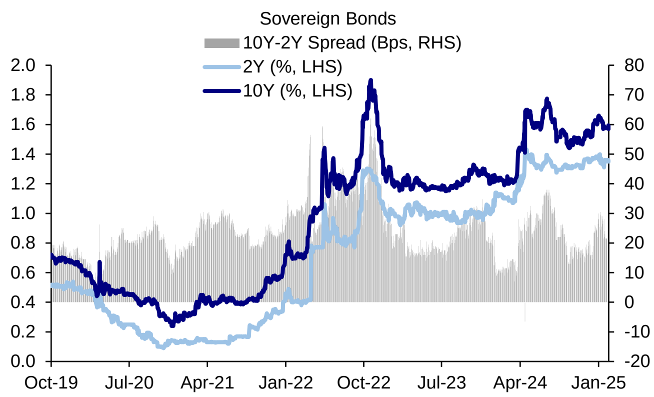
- Central Bank: With **Q4 growth momentum remaining strong at 0.5% QoQ on a seasonally adjusted basis**, it is still premature for the CBC to begin policy normalisation especially as inflation remains elevated even though most of the headline inflation increase was due to the Typhoon in October and December. The CBC will also want to avert the situation of re-igniting the housing market after recent measures show signs of paying off. That said, **December's property price uptick** will keep policy makers on their toes on easing too early and the initial support may come through fiscal and trade initiatives rather than monetary policy accommodation. We retain our view of a **calibrated rate cut in Q2 as external demand support may begin to level off.**

- Risks: Perversely, **remote tail** risks from equity market fallout may spark sharp property market corrections which nudges the CBC to tweak property sector measures and bring forth their rate cut plans.

- Yields: Going against global developments, yields edged lower across the curve.

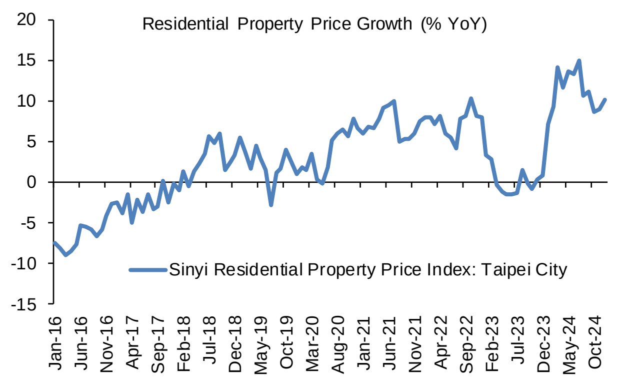
- Curve: Reflecting the narrow room for a smaller term premium, the 10-2Y spread is essentially similar to that compared to late October. Movements will defer to wider UST trends with steepening on the cards but the follow through will be a milder one in Taiwan as rate cuts continue to elude.

Fig 6e. Decline in yields are relatively milder




Sources: Bloomberg, Mizuho

Figure 6f. December property price uptick may worry




Sources:CEIC, Mizuho

## SGD: MAS' Resilient Insurance

| | Q4 2024 | Q1 2025 | Q2 2025 | Q3 2025 | Q4 2025 | Q1 2026 |
|---|---|---|---|---|---|---|
| **S$NEER Slope** | 2.0% | 1.5% | 1.5% | 1.5% | 1.5% | 1.5% |
| **S$NEER Mid-pt** | Hold | Hold | Hold | Hold | Hold | Hold |
| **USD/SGD** | 1.283-1.368 | 1.327-1.376 | 1.330-1.388 | 1.315-1.375 | 1.292-1.344 | 1.292-1.337 |
| | 1.367 | 1.363 | 1.371 | 1.335 | 1.318 | 1.321 |
| **GDP (% YoY)** | 2.3 | 2.3 | 2.4 | 2.3 | 2.1 | 1.9 |
| **CPI (% YoY)** | 1.8 | 2.1 | 2.0 | 2.1 | 2.2 | 2.1 |

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

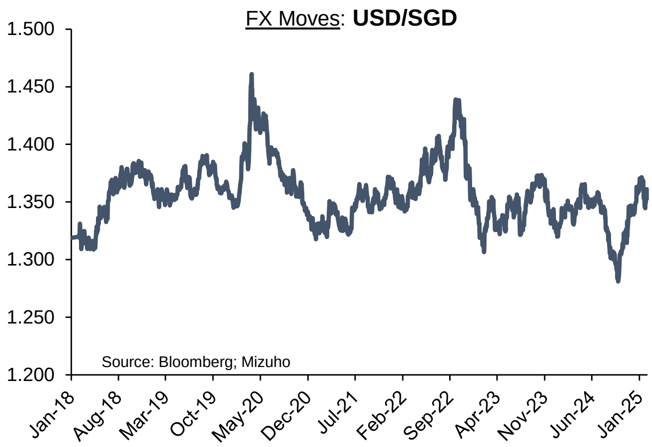



Fig 7b. Declining Core Inflation

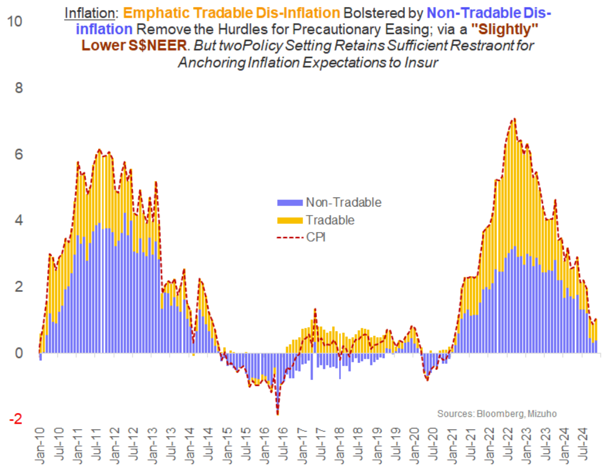



Fig 7c. Exceptional S$NEER Surge

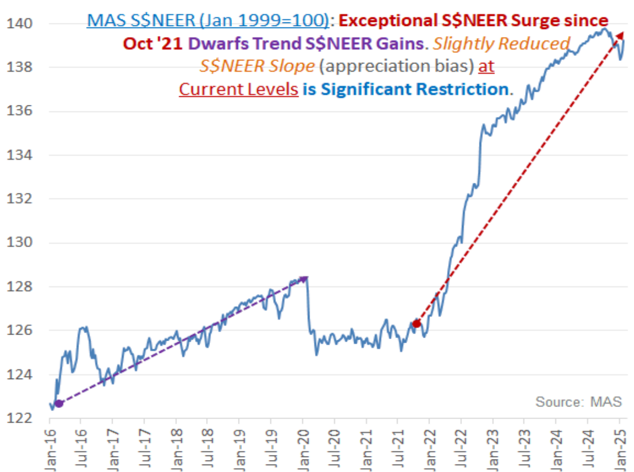
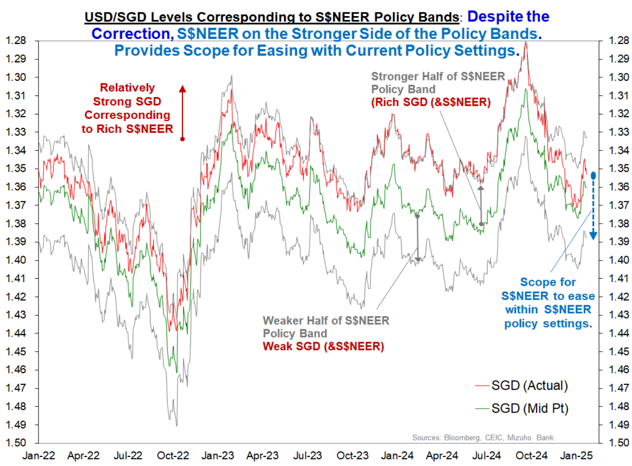



Fig 7d. Scope to Correct Further Within the Band




**FX**

- Hawkish Easing: Arguably, the **MAS' calibrated S$NEER appreciation bias inadvertently amounted to hawkish easing**. The **defining feature** being MAS' assessment that ***policy is now effectively set for resilience amid heightened Trump 2.0 (trade) uncertainties*** – *against opposing demand and inflation shocks* – thereby **suggesting no further easing**.

- Bullish SGD Reflex Overstates MAS Impact: Nonetheless, the initial bullish **SGD response was more coincidence** (of broad-based) USD pullback **than** it was **causation** (from hawkish interpretations owed exclusively to MAS' hawkish caveat embedded in the easing for Jan).

- S$NEER Restraint – "Slightly" Lower Slope For the record, the **MAS only *"slightly" reduced the S$NEER slope* despite the context of *lofty S$NEER elevation*.** This entails **two dimensions of lingering hawkish restraint**. First, the **pace of S$NEER merely tempered** (and not terminated), means that the **anchor for inflation expectations is meaningfully intact**.

- S$NEER Restraint – At Lofty Elevation: Second, **exceptionally rich S$NEER** that has been from *inherited, record, front-loaded, tightening* previously (three rounds re-centring S$NEER higher in 2021-22) translates to **significant restraint**. Despite modest S$NEER pullback (within prevailing S$NEER bands) the **relatively elevated S$NEER subdues inflation risks *and then some***, packing in **additional price shock buffer**.

- Resilient Insurance Cover, Not Urgent Relief: To be sure though, ***rather than urgent relief***, the **MAS move** (calibrated S$NEER slope reduction) is **aimed at S$NEER policy resilience** *to withstand adverse demand impact* (from heightened trade uncertainties) as well as *inflation shocks* (from tariffs/geopolitics). Specifically, as it retains S$NEER slope ($NEER appreciation bias) to anchor inflation expectations whilst insuring against demand shocks by tempering S$NEER headroom (and attendant scope for SGD outperformance).

- Intra-band Demand Shock Absorption: Crucially, the **rich S$NEER *which ordinarily enhances dis-inflation dynamics*** simultaneously also has **embedded insurance against adverse demand shocks** *by way of allowance for S$NEER to fall within the bands*.

- SGD Outlook: But despite resilient insurance engineered in S$NEER policy, **USD gyrations will the main driver of SGD volatility** amid heightened headline risks. **Sharp SGD downside risks** (testing 1.38) **into mid-2025** marked by acute volatility amid **US trade antagonism/headlines**. **Late-2025 SGD rebound** (1.31-41.32) *premised on a mellower USD* coinciding with tariff relief, *China (CNY) backstop* and *MAS on hold.*

**Rates**

- Central Bank: The **MAS has signalled** that **policy** is **set for resilience** *to weather either demand dent and/or inflationary shocks* from tariffs. This calculated, pre-emptive calibration suggests no further pipeline easing. Hence, this *pause amid a gentler S$NEER slope* is seen as **hawkish easing**. ***Although,* adverse demand shocks identified as the greater threat** means that **policy surprises will be dovish** in nature.

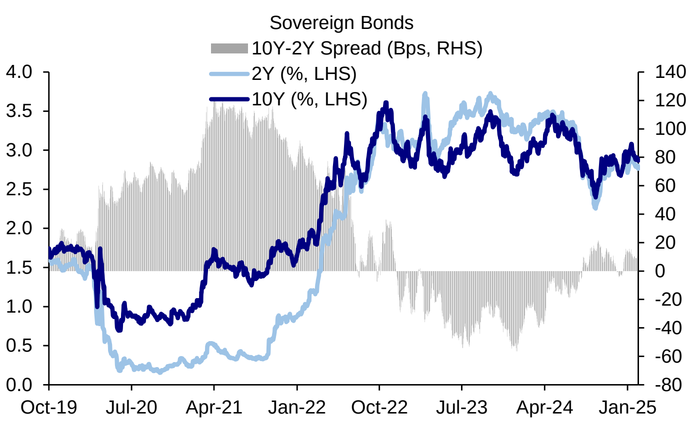
- Negative USD/SGD Forward Points Persist: In which case, the **usual (MAS easing) triggers for a more emphatic shift to less negative USD/SGD forwards are impaired**.

- SGD Rates Discount Intact": Hence, with **still deeply, albeit somewhat tempered, negative USD/SGD forward points** (consistent with SGD appreciation expectations), **covered interest parity suggests** *SGD rates at a discount (even if diminished at the margin) to the corresponding US rates*.

- Yields (following USTs Lower): This **"SGS discount"** is *not only applicable at the front-end,* but also **persists out the SGS curve**. The exceptionally pronounced discount in SGD rates (vis-à-vis US rates) notwithstanding, **overall directional cues for SGS yields are likely to still be driven by USTs**.

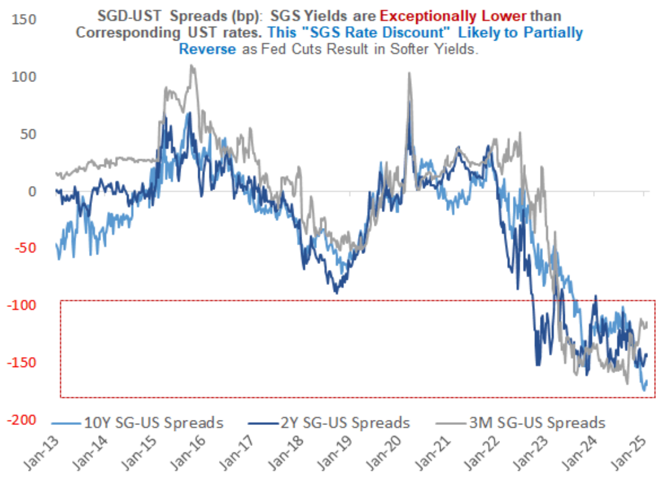
- Softer, Steeper & Narrower: All things considered, **softer SGS rates are likely**, *in sympathy with UST yields set to decline from elevation later in 2025, and arguably steepen as well.* Although at a lower beta that narrows the SGS discount (UST-SGS negative spread).

Fig 7e. Price-Taker of UST Shifts




Sources: Bloomberg, Mizuho

Figure 7d. Exceptional Discount Set to Erode



## IDR: Hands Tied

| | Q4 2024 | Q1 2025 | Q2 2025 | Q3 2025 | Q4 2025 | Q1 2026 |
|---|---|---|---|---|---|---|
| **Policy Rate (%)** | 6.00% | 5.75% | 5.50% | 5.25% | 5.00% | 4.75% |
| **USD/IDR** | 15170-16305 | 15850-16560 | 15900-16620 | 15300-16490 | 15000-16100 | 15100-15750 |
| | 16102 | 16350 | 16450 | 15800 | 15400 | 15230 |
| **GDP (% YoY)** | 4.8% | 5.0% | 4.9% | 5.1% | 5.0% | 5.0% |
| **CPI (% YoY)** | 1.6% | 2.0% | 2.1% | 2.9% | 2.9% | 2.8% |

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

Fig 8a. USD/IDR little durability below 16,100

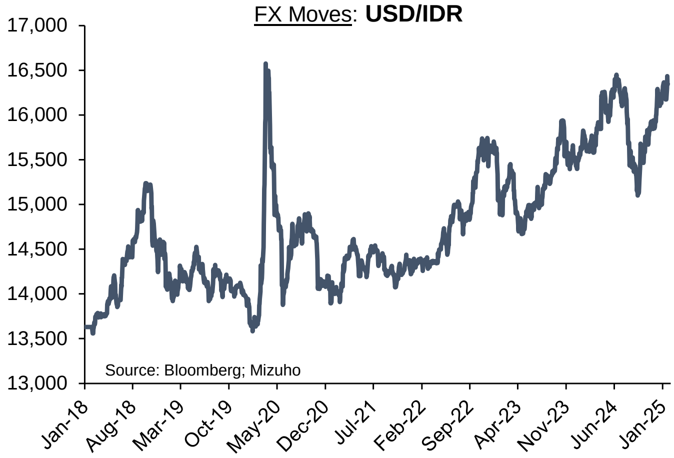
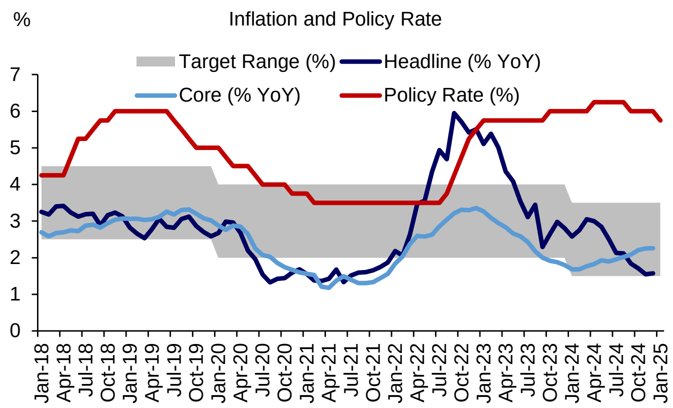
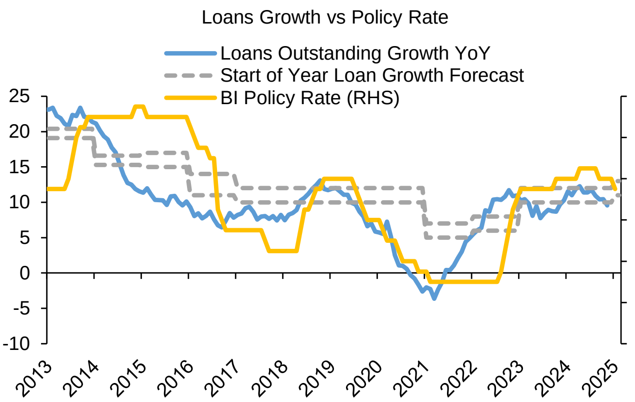



Fig 8b. Inflation remains stable



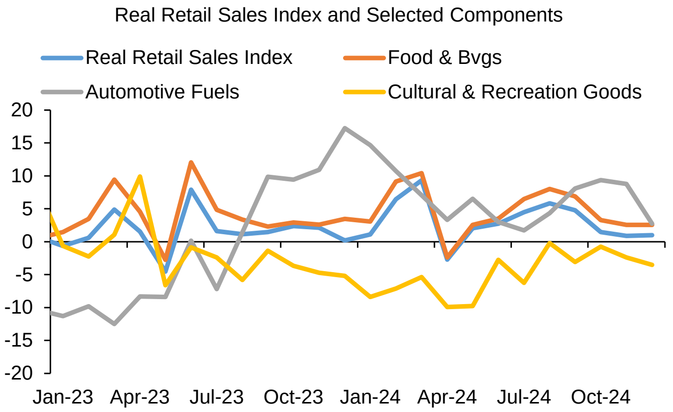

Sources: CEIC; Mizuho

Figure 8c. Loan Growth below forecasts tend to imply impending easing




Source: CEIC; Mizuho

Fig 8d. Consumers More Discerning in Spending




Sources: CEIC; Mizuho

**FX**

- A Bad Start to the New Year: IDR kicked-off the year on the wrong foot as fiscal woes came into spotlight with the watered-down VAT increase announced on 31 December and official launch of the free lunch programme. In addition, January's surprise cut also gave pressure to the IDR. The fiscal bugbear and BI's cut have led IDR-underperformance against regional peers on a YTD basis. Since the start of the year, authorities have also intervened into the FX markets (and have thus far managed to cap weakness under 16,400) and reiterated their commitment towards ensuring rupiah-stability.

- Tighter Controls: In an attempt to bolster Indonesia's FX reserves and support the IDR, Indonesia announced that it planned to force commodity firms to keep export earnings onshore for a year starting March 1. The policy tightens an existing requirement that resource firms keep 30% of earnings onshore for at least three months. The measure applies to all of Indonesia's major commodities.

- Growth Risks Abound: That the watered-down VAT increase comes on the back of concerns of cost-of-living pressures also suggests that consumers may be stretched. Real retail sales growth have been soft in recent months, with households scaling back on recreation & culture goods (which are more discretionary) since

May 2023. Instructively, Bank Indonesia had also lowered its 2025 GDP forecast from 4.8%-5.6% to 4.7%-5.5%.

- Stable Inflation Outlook: Headline inflation remains stable (Oct: 1.7%; Nov: 1.6%) and should remain stable. Watered-down VAT increase narrowly scoped to luxury goods and services only should see marginal pass-through to overall CPI number.

- Current Account: 2024 current account deficit is expected to be near the wider-end of BI's 0.1-0.9% of GDP range. Current account deficit is likely to widen further in 2025 on smaller goods balance surplus amid commodity headwinds and uncertainty over global demand. Notably, Indonesia was reported to be weighing cuts to nickel mining quotas in order to support prices.

- Financial Flows: Outflows from debt continued since BI's cut in January.

- IDR Outlook: IDR underperformance looks primed to persist amid fiscal woes and BI's growth concerns. Any downside surprise to Q4 GDP growth could serve to exacerbate uncertainty over BI's easing bias, and add pressure to the IDR. A breach of 16,600 is foreseeable should USD volatility continue, even as BI attempts to temper weakness.

**Rates**

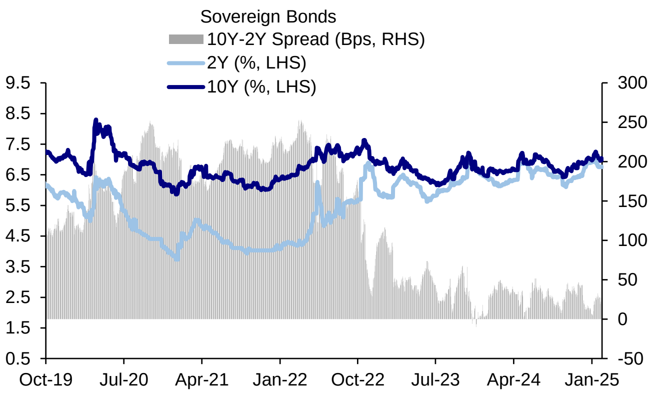
- Caught by Surprise: Bank Indonesia delivered its second cut at the January meeting, the second surprise following the first surprise cut in August. The January cut was arguably a pre-emptive on growth concerns, but it should not be misconstrued as the start of an unfettered easing cycle, as further cuts will still be conditional on relative rupiah stability. We retain our view that BI's easing cycle will still be staggered. That is to say, shifting back to a pause before cutting again. As things stand (assuming no sudden sharp and sustained USD depreciation), we do not expect another cut in Q1 (i.e. in February and March) as BI monitors the pass-through effects of its rate cut and spillovers to the IDR, barring any material downside surprise to growth.

- Increasing Uncertainty: Arguably, the January cut have added uncertainty to rate trajectory as rupiah stability may no longer be front and center of Bank Indonesia's policy calculus. This is especially so given that the weeks leading up to BI's decision was characterised by broad USD strength and Trump-induced FX volatility. The slight tilt towards growth raises questions on the extent of the tilt.

- Yields: Despite the surprise cut, 2Y and 10Y yields in January are on average 6bps and 13bps higher compared to December 2024 respectively. The curve also steepened, with 10Y-2Y spreads averaging 20bps in January, compared to 14bps in December. While the curve steepening is in-line with an easing cycle, higher yields are likely due to spillovers from the ascendancy of UST yields.

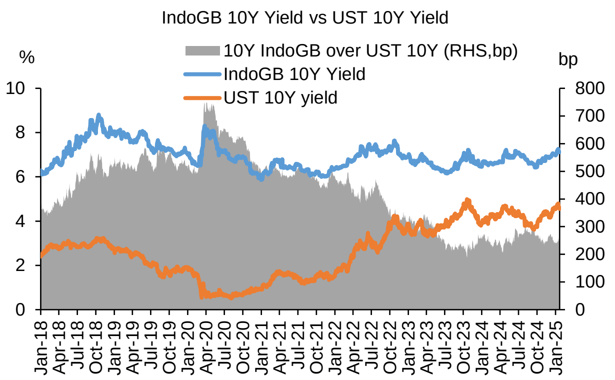
- Curve: Easing bias ought to see curve steepen, in addition to auctions although 10Y-2Y spreads may remain compressed as BI takes a staggered (and gradual) approach on easing.

Fig 8e. Curve Steepend slightly following BI's cut




Sources: Bloomberg, Mizuho

Fig 8f. IndoGB-UST 10Y spreads Narrower




Sources: Bloomberg; Mizuho

## MYR: Anchor of Stability

| | Q4 2024 | Q1 2025 | Q2 2025 | Q3 2025 | Q4 2025 | Q1 2026 |
|---|---|---|---|---|---|---|
| **Policy Rate (%)** | 3.00% | 3.00% | 3.00% | 3.00% | 3.00% | 3.00% |
| **USD/MYR** | 4.12 – 4.51 | 4.29 – 4.58 | 4.27 – 4.67 | 4.13 – 4.55 | 3.99 – 4.36 | 3.99 – 4.24 |
| | 4.47 | 4.47 | 4.53 | 4.30 | 4.12 | 4.14 |
| **GDP (% YoY)** | 4.8% | 5.5% | 4.6% | 4.1% | 5.1% | 4.6% |
| **CPI (% YoY)** | 1.8% | 1.9% | 2.0% | 2.2% | 2.1% | 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 9a. MYR gained given BNM hold

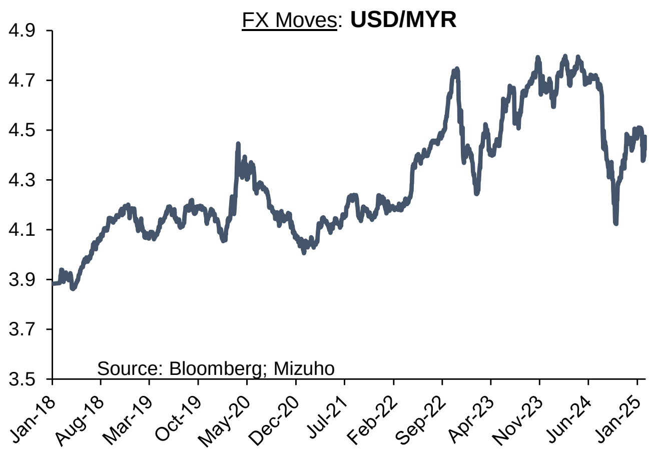
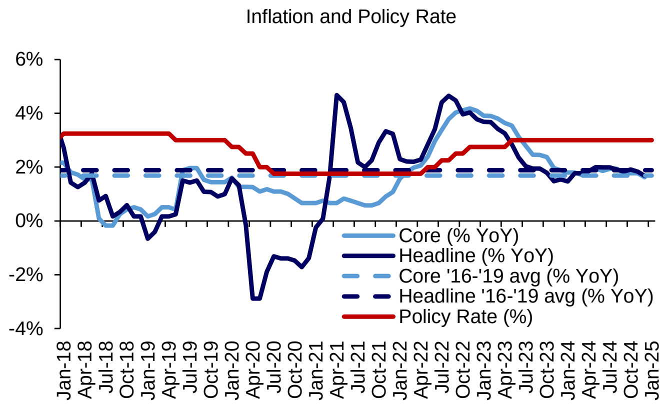
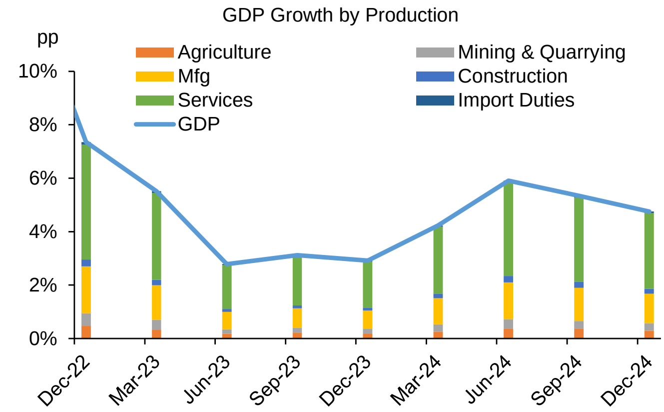



Fig 9b. Inflation remains stable



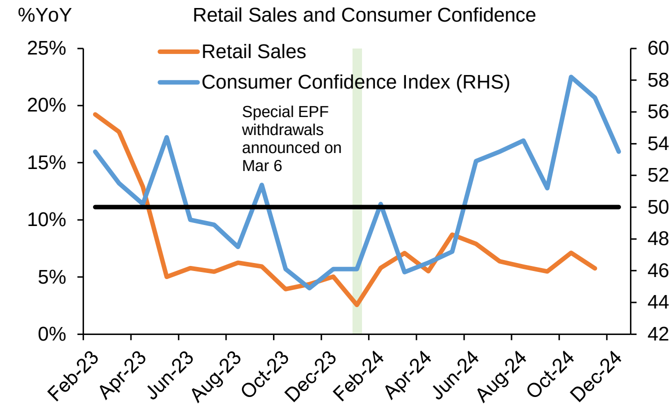

Source: CEIC; Mizuho

Fig 9c. Growth supported by Manufacturing and Services




Sources: CEIC: Mizuho

Fig 9d. Supported Retail Sales and Buoyant Consumer Confidence




Source: CEIC; Mizuho Bank

### FX

- Volatility Abound: Despite things relatively stable in Malaysia, USD/MYR was still volatile driven by external drivers, in particular lower UST and headlines on US-China trade tensions. Malaysia has outperformed several regional currencies, gaining by 0.8% since the turn of the year amid partial trade antagonism relief.

- Economy in "Sweet Spot": "Sweet spot" was how BNM Governor characterised the Malaysia economy, and was corroborated by data. Advance estimates indicated that growth held up even bad weather damaged crops, supported by services and manufacturing sectors. Looking ahead, these two sectors are expected to remain buoyant. In particular, services growth ought to be resilient amid supportive wage growth.

- Stable Inflation, Upside Risks in 2025 Contained: Inflation in 2025 remained stable at around 2.0%. In the coming year, upside risks are present form a) the expansion in Sales & Services Tax in May 2025 (details of affected goods/services await), b) RON95 subsidy rationalisation (expected to be implemented in mid-2025) and c) increases to minimum wages and rollout of progressive wage system. However, given the momentum of price increases this year considering similar developments in 2024[1]*, upside risks are likely moderate.

- Current Account: We expect a narrower current account surplus in 2024 compared to 2023 (1.5% of GDP) on a smaller goods balance and higher primary income outflows. In particular, Q4 goods balance should see some deterioration on poorer palm oil harvest on adverse weather conditions. Into 2025, we expect current account surplus to improve from 2024 but still fall short of 2016-2019 average of 2.7% of GDP. This takes into account continued electronics tailwinds. Nonetheless, the slew of high-profile investments announced in 2024 by MNCs while should mean more financial inflows, could also see rising imports of technology, capital goods and raw materials, which can deteriorate the current account balance.

- Fiscal Consolidation on Track: Fiscal consolidation looks to be able to meet 2024 target of 4.3% of GDP.

- Political Undercurrents Pose Tailrisks: Signs of internal rifts within PM Anwar's cabinet have surfaced recently on Trade Minister Zafrul Aziz's potential switch from United Malays National Organisation (UMNO) to the PM's own party, the People's Justice Party. The two parties had set aside years of rivalry to form the government in 2022 after a hung parliament. Nonetheless, this should be tailrisk as political premium should be managed given the King Sultan Ibrahim's pro-business stance.

- MYR Outlook: With BNM's stable hold providing an anchor for rates, FX volatility would be externally driven. Oscillating developments and policies under Trump 2.0 as well as the ringgit's higher beta to CNH (and thus sensitivity to China stimulus) impart two-way volatility.

**Rates**

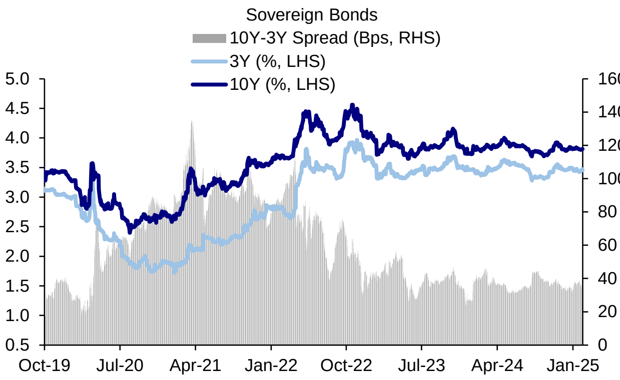
- BNM's Steady Hands: As expected, BNM stood pat at the January meeting. A prolonged hold remains the base case as BNM characterised the current policy stance as "supportive" of the economy and is "consistent" with the current assessment of inflation and growth prospects.

- Domestic Consumption Present Tailrisks: Buoyant domestic consumption on the back of EPF savings withdrawals present risks of struggling consumers once the "sudden windfall" is depleted. On the external front, while electronics cycle tailwinds could fade moderation in manufacturing growth should not be too alarming especially in view of high base effects.

- Stable Yields: Yields have remained stable, with 3Y and 10Y yields broadly unchanged in January compared to December 2024 levels as BNM's prolonged hold anchors rates. The curve steepened very mildly by 3bps.

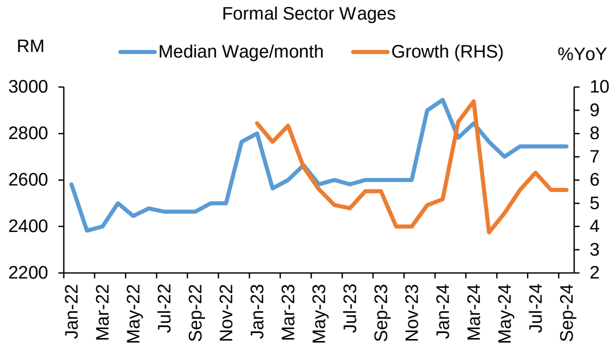
- Curve: Curve could steepen as upcoming auctions in February into March are all >5Y tenor.

Fig 9e. Spreads stable with BNM anchoring rates




Sources: Bloomberg, Mizuho

Figure 9f. Wage Growth Supportive




Note: Time series limited by data availability.
Sources: Department of Statistics Malaysia; Mizuho

[1] Budget 2024 expanded the scope of SST and diesel subsidy rationalization was rolled out in May 2024. While Budget 2024 only featured a pilot progressive wage system, inflation remained moderate despite robust wage growth (as proxied by increases in formal sector wages) in 2024.

## PHP: Headwinds Abound

| | Q4 2024 | Q1 2025 | Q2 2025 | Q3 2025 | Q4 2025 | Q1 2026 |
|---|---|---|---|---|---|---|
| **Policy Rate (%)** | 5.75% | 5.50% | 4.75% | 4.50% | 4.25% | 4.25% |
| **USD/PHP** | 56.0 - 59.0 | 57.2 - 60.2 | 57.1 – 60.5 | 55.9 - 59.8 | 54.7 – 58.2 | 54.8 – 57.5 |
| | 57.8 | 58.8 | 59.6 | 57.2 | 56.5 | 56.3 |
| **GDP (% YoY)** | 5.8% | 5.7% | 6.2% | 5.4% | 5.4% | 5.1% |
| **CPI (% YoY)** | 2.6% | 2.9% | 3.1% | 3.2% | 2.9% | 2.1% |

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 remains near 59 handle

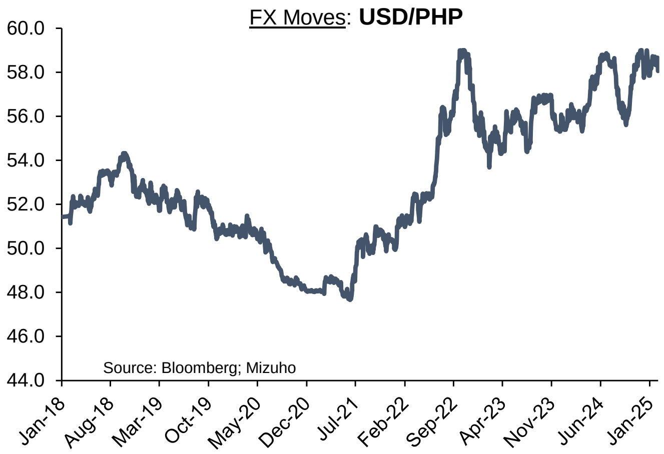
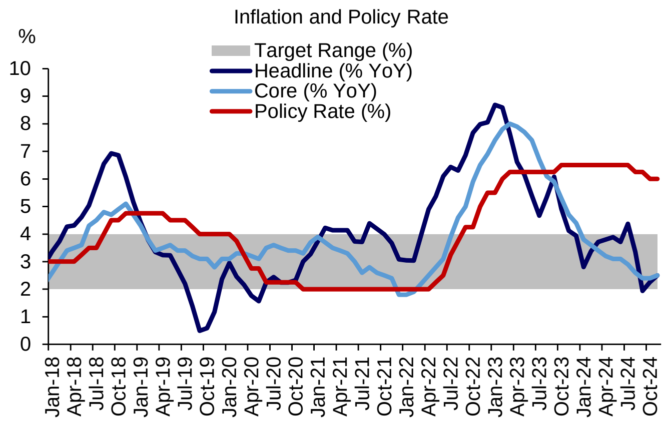
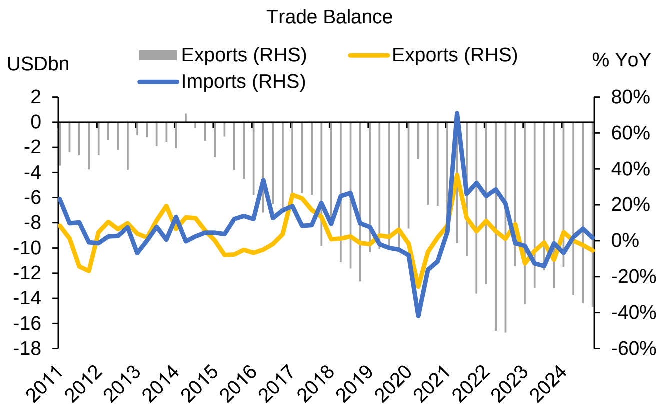



Fig 10b. Inflation remains within target despite uptick



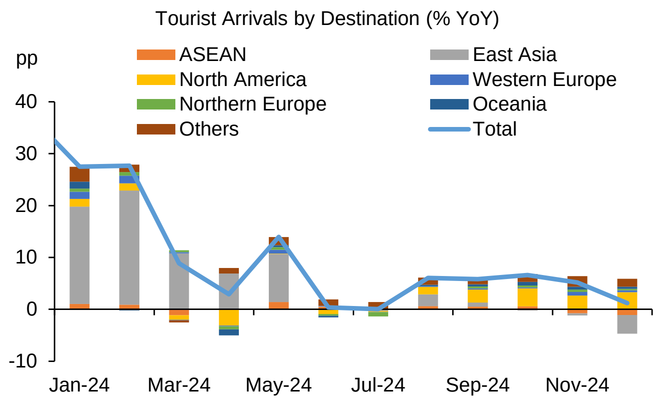

Source: CEIC; Mizuho

Fig 10c. Trade Balance Little Changed from Q3




Sources: CEIC; Mizuho

Fig 10d. Tourism growth moderating, but still supportive




Sources: CEIC: Mizuho

**FX**

- Backstopped by Interventions: USD/PHP remains languishing around 58-59 levels as it underperformed regional peers as the BSP looks likely to continue their easing bias.

- Poor Domestic Sentiment: Downside risks for domestic consumption are increasingly worrying. Despite the holiday season, a survey conducted by Social Weather Stations (SWS) in December revealed that 63% of Filipinos saw themselves as poor, the highest self-rated poverty level in 21 years. A separate survey by the same organisation indicated that the number of Filipino households experiencing involuntary hunger has jumped to 25.9%, the highest since the pandemic.

- Inflation-in-check: Inflation edged higher to 2.9% in December (Nov: 2.5%), with core inflation ticking up to 2.7% (Nov: 2.5%). The increase was driven by food inflation, education services and restaurant & accommodation services. Rice inflation should be managed given that on 16 January 2025, the National Price Coordinating Council (NPCC) has approved a resolution urging the Department of Agriculture to declare a "food security emergency for rice" as prices remain high despite declining global rice costs and tariffs reductions ordered by President Ferdinand Marcos Jr. The declaration would allow authorities to release buffer stock rice to stabilise local prices.

- Current Account: Current account deficit for 2024 is likely to widen further to around 2.9% of GDP (2023: 2.7% of GDP). This is despite likely supportive services inflows from tourism receipts. Nonetheless, the deficit could potentially see some narrowing in 2024 on better harvests, and thus reduced need for rice imports. The country's palay production had faced challenges in 2024 as a dry spell brought on by the El Nino phenomenon early in 2024 and crop damage caused by flooding during La Nina in the latter part of the year had resulted in a decline in rice production. Nonetheless, external trade presents headwinds.

- Political Tensions: Political tensions have subsided since the feud between Vice President Sara Duterte and President Marcos Jr. reached a boiling point. But does not detract from mid-elections in May looking to be a tough battle, and the attendant political uncertainty may weigh on the PHP.

- Geo-political tensions a Tail Risk: News headlines suggest higher Philippines-China tensions. Apart from a long-standing maritime dispute in parts of South China Sea, Philippine authorities in January arrested a Chinese national and two Filipino cohorts for alleged espionage in in relation to disputed waters while it was reported that Chinese state-sponsored hackers penetrated the executive branch of the Philippines government and stole sensitive data in early January. Thus far, spillovers to FX have thus far remain modest, but escalation of such conflicts to potential armed conflict presents a tail risk to watch out for.

- PHP Outlook: Growth headwinds both domestically and externally would pressure the PHP, but interventions by BSP ought to temper excessive weakness. Authorities have appeared to be able to defend the 59 handle; but should 59 handle be breached, the next key level would be 60.

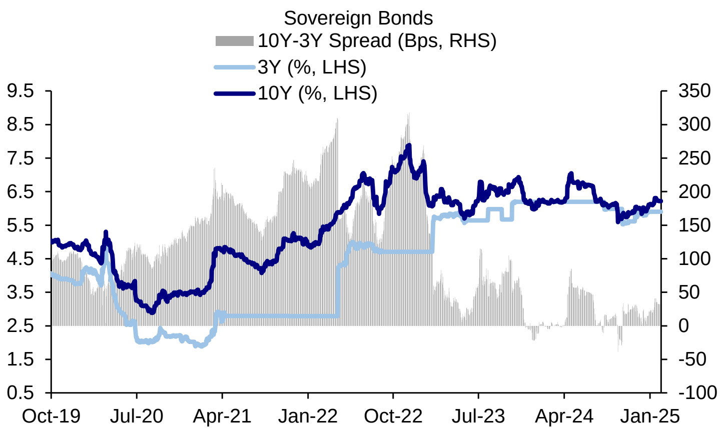
**Rates**

- Central Bank: Despite the tick-up in inflation, BSP should not be deterred from another 25bps cut at the February meeting amid growth risks and inflation still remain comfortably within the target band. Furthermore, the February meeting is the only meeting in this quarter, and we do not expect any off-cycle moves at this juncture. Moving February's meeting one week *earlier* instead of *later* due to scheduling conflicts may also allude to some urgency in acting without calling for an off-cycle move.

- Yields: Compared to December, the yield curve bear-steepened in January. 3Y yields edged up by ~5bps while longer-end 10Y yields climbed up 20bps.

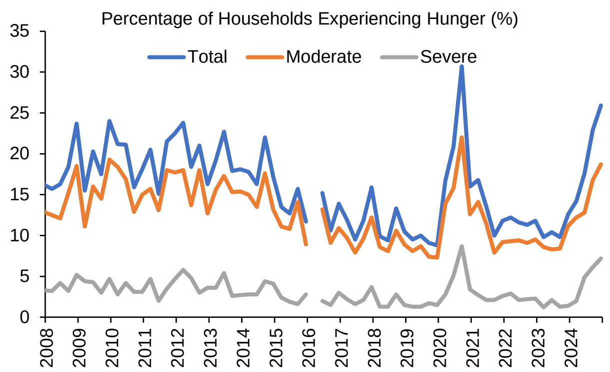
- Curve: 10Y-3Y spreads increased from an average of 13bps in December to 28bps in January. Further steepening expected as BSP continues easing, while Q1 indicative supply schedule suggests more supply at the longer-end.

Fig 10e. Short-term elevated despite BSP's cuts




Sources: Bloomberg, Mizuho

Figure 10f. Households Appear Stretched




Sources: Social Weather Stations; Mizuho

Note: Missing data due to data availability.

## THB: Missing Anchors

| | Q4 2024 | Q1 2025 | Q2 2025 | Q3 2025 | Q4 2025 | Q1 2026 |
|---|---|---|---|---|---|---|
| **Policy Rate (%)** | 2.25% | 2.00% | 1.75% | 1.75% | 1.50% | 1.50% |
| **USD/THB** | 32.3-35.2 | 32.9 - 35.9 | 33.8 - 36.2 | 33.4 - 35.7 | 32.7 - 34.9 | 32.6-34.6 |
| | 34.1 | 34.8 | 35.2 | 34.3 | 33.6 | 33.3 |
| **GDP (% YoY)** | 4.0% | 3.2% | 2.8% | 2.9% | 2.0% | 2.2% |
| **CPI (% YoY)** | 1.0% | 1.4% | 1.6% | 1.7% | 1.5% | 1.4% |

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 volatilty to persist in 2025

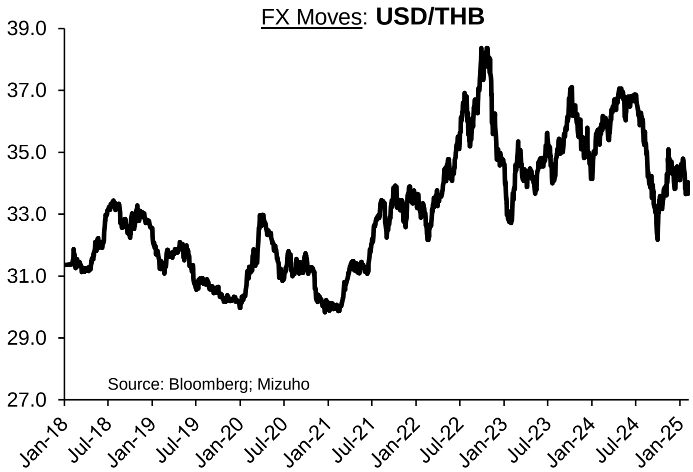
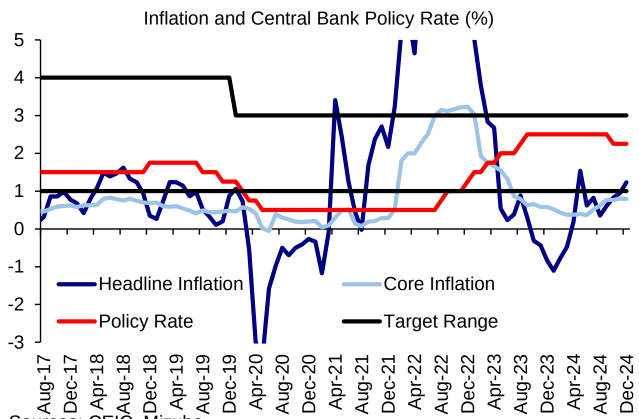
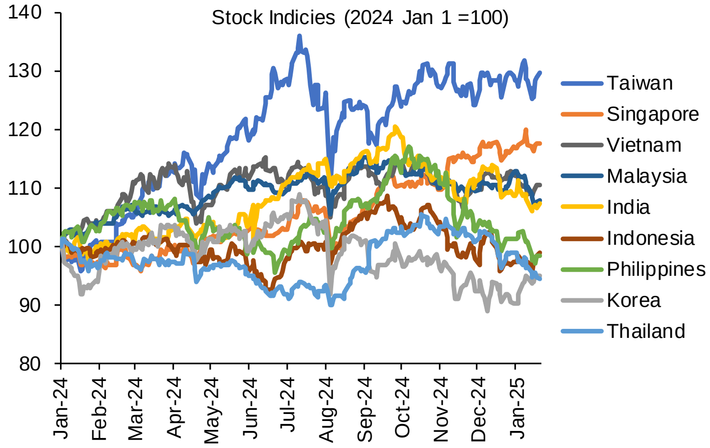



Fig 11b. BoT will face pressures to ease in 2025



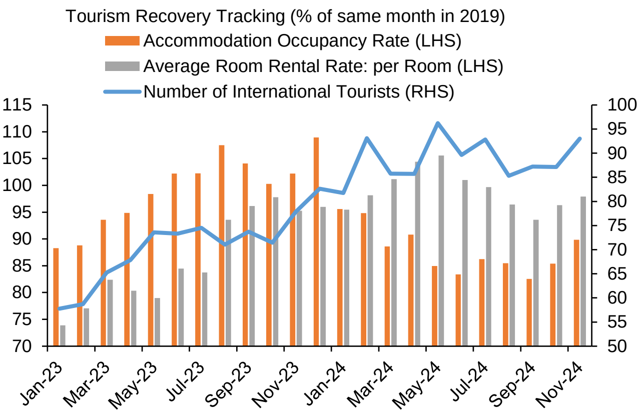

Sources: CEIC, Mizuho

Fig 11c. Lacklustre equities weigh on the THB




Sources: Bloomberg, Mizuho

Fig 11d. 2025's firmer tourism recovery face blips




Source: CEIC; Mizuho

**FX**

- Still A Wild Ride: The THB continued on its wild ride at the turn of 2025 catching onto tailwinds from the JPY and partial relief from delayed tariffs. The **THB's volatile situation is unlikely to abate in the near term** as it is subjected to **domestic uncertainties and external spillovers** from the JPY and USD. The former continues to swing around BoJ's hiking path with a deference to UST yields while the latter confronts the impact of Trump's executive orders and consequent implications on the Fed. **Domestically**, investors had to brace for potential bumps in tourism recovery as well as examining the potential of their entertainment complex plan to **anchor longer term growth.**

- Leadership Independence: The rejection of potential BoT Chairman Kittiratt Na-Ranong who was seen as a political appointee was admittedly perceived as a positive sign of BoT independence and backstop THB gains towards end of 2024. Partial relief over lawsuits over Thaksin may also have aided the semblance of political stability. Nonetheless, the **search** for the **next BoT Governor** by the Ministry of Finance (MoF) in 2025 which entails the next candidate having "modern ideas" and being "able to work closely together with the MoF" **will have far bigger implications for central bank independence compared to the appointment of the Chairman given the wide-ranging autonomy of the Governor.**

- Delayed Fiscal Risks More Worrying For Long Term Bulls: Near term fiscal risk may appear diminished with the latest estimates for FY 2025 (released in December 2024) for public debt ratio reduced from 67.9% to 65.6% of GDP. Nonetheless, these public debt risks are merely delayed and not resolved with the FY2028 estimate revised upwards to 69.2% from 68.6% and the new 5-year trajectory show no signs of an inflection compared to the previous path which peaked in FY2027.

- Economic and FX Divergence: While our assessment is that Thailand's supply chain position imply that they might be less threaten by direct tariffs relative to regional peers such as Vietnam, their external economic interlinkages via Chinese tourist and export demand appears to have an outsized impact on the THB.

- Firmer Current Account Amid Volatile Recovery: That said, we expect that the current account surplus to be firmer in 2025 to underpin the THB recovery but remain insufficient to withstand the onslaught of volatility. Simply put, the underlying economic potential to recovery remains at significant risk of external developments.

- Unrelenting outflows: Equities and bond outflows persist in 2025 as UST yields surged in January.

- Of Gains and Vulnerabilities: THB's potential for recovery among peers is diminished by its heightened volatility emanating from the risk backdrop. Notably, while tourism may not offset growth headwinds, it is an important FX driver as a return to a firmer current account surplus sets it apart from deficit peers such as the PHP and IDR. Compared to these peers, the relative lack of rate cuts also enhances THB's attractiveness. However, its volatility means that gains may fade abruptly leaving time sensitive investors vulnerable.

- Outlook: We expect USD/THB buoyancy to be retained above mid-33 while sporadic fears of tariffs and domestic governance conflicts may trigger tests of 35. All in, the THB remains vulnerable especially in the early stages of Trump 2.0 amid fears of widespread tariffs.

**Rates**

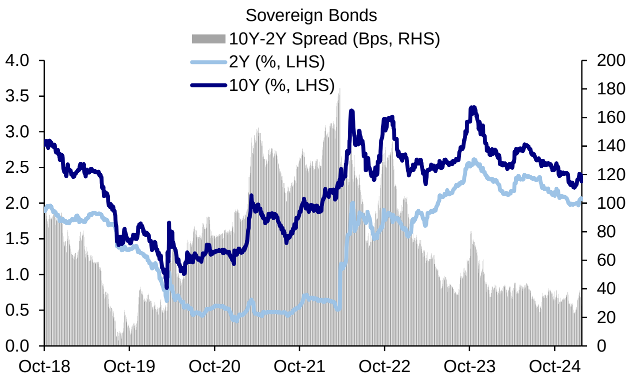
- Central Bank: We continue to expect that the BoT will act **for a further rate cut** in Q1 to support growth amid worsening credit condition and to complement recent debt restructuring measures. Amid these worries, we expect rates to decline to 2.00% in Q1 which is likely in their neutral range considering risk of THB depreciation 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: The main worry is around an erosion of central bank independence which leads to a bigger than expected decline in yields on the front end while longer end may rise as a greater risk premium is demanded with the fiscal trajectory heading toward the legal limit in the medium term.

- Yields: In line with USTs movement, yields in Thailand rose across the curve amid some steepening as the BoT portrayed an image of holding rates. Nonetheless, further steepening remains on the cards.

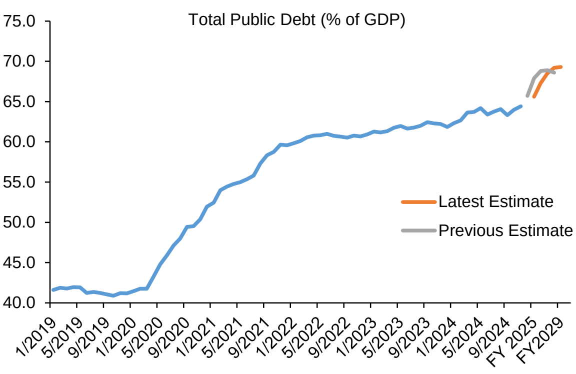
- Curve: Even after the mild steepening, the curve remains very flat with the 10Y-2Y spread at around 30-35bps. While cash handouts boost near term growth prospects, a slight reckoning from bond markets ought to be watched should the handouts be broadened to the wider public trigger fears of larger debt issuance. Given that the risk leans towards BoT easing, this will also aid steepeners.

Fig 11e. Slight Steepening in January




Sources: Bloomberg, Mizuho

Figure 11f. Rising Public Debt a Key Worry




Source: CEIC; Mizuho

## VND: Knowns and Unknowns

| | Q4 2024 | Q1 2025 | Q2 2025 | Q3 2025 | Q4 2025 | Q1 2026 |
|---|---|---|---|---|---|---|
| **Policy Rate (%)** | 4.50% | 4.50% | 4.50% | 4.50% | 4.50% | 4.50% |
| **USD/VND** | 24560-25512 | 24900-26100 | 25200-26200 | 24600-25800 | 24500-25600 | 24500-25600 |
| | 25485 | 25550 | 25750 | 25100 | 24700 | 24680 |
| **GDP (% YoY)** | 7.6 | 5.7 | 6.0 | 6.1 | 6.3 | 6.3 |
| **CPI (% YoY)** | 2.9 | 2.8 | 3.3 | 3.5 | 3.6 | 3.2 |

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 seasonal gains may wobble

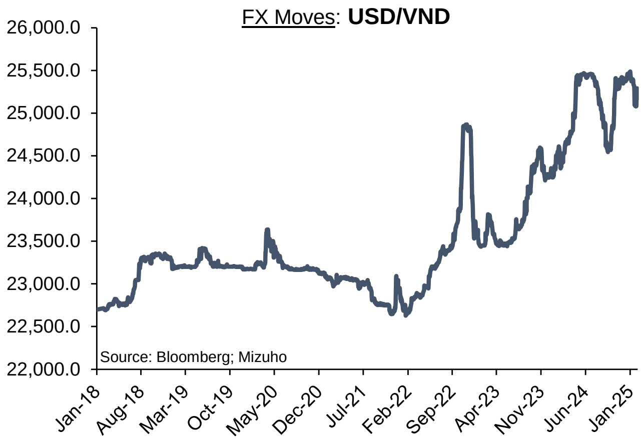



Fig 12b. SBV to continue to hold rates

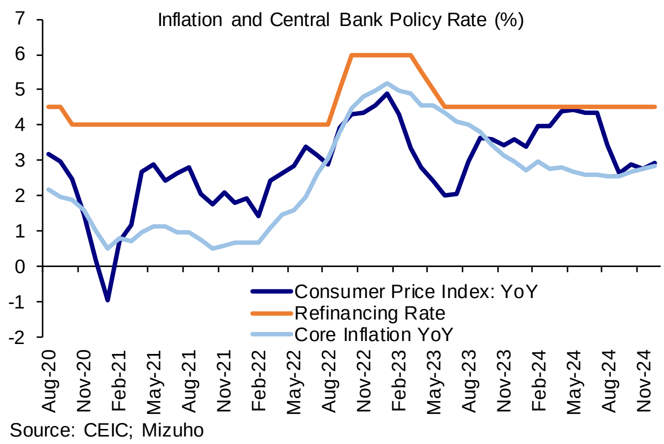



Fig 12c. External demand is key cyclical driver

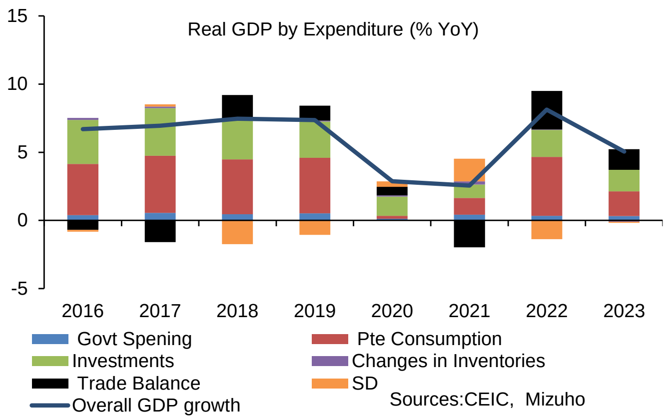
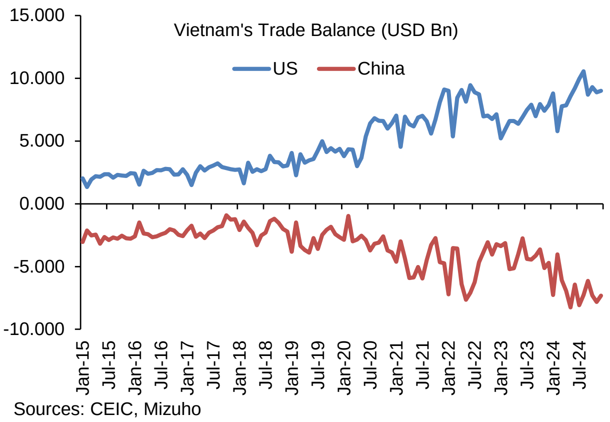



Fig 12d. Trade surplus with US has grown




**FX**

- Macro Outperformance, Reserves Unknown Discomfort: For 2025, the VND has outperformed regional peers and that came on the back of GDP growth ending the year on a higher note exceeding official target for 2024 and likely **seasonal demand into the TeT holidays**. Nonetheless, we continue to see that the lack of FX reserves data as a discomfort given its potential for abrupt shocks as we enter Trump 2.0. In short, sustaining current VND levels would already be a remarkable achieve for the months ahead.

- Growth hardly a catalyst for the VND: Despite growth outperformance, the VND depreciated more than 4% against the Greenback despite the SBV's rate hold. The **VND also underperformed peers such as the IDR, PHP and THB. These peers eased policy rates and their economies grew at a slower pace**. Furthermore, double digit growth targeted by the PM in 2025 remains a high bar given the higher base from exports demand in 2024. Trade is usually the cyclical factor driving growth and for it to accelerate further will be a stretch.

- Reserves remain our key reservation: Simply put, revelation of FX reserves in September 2024 retaining at US$92billion is little comfort considering the strength of the Greenback in Q4 2024. The extent of intervention depleting towards 2 months of import cover is very well possible. These figures if released officially may spark an initial knee jerk reaction and as such, the data prints may be delayed as was the case in most of 2024.

- Plus One: Given the precedence under Trump 1.0, it is certainly tempting to suggest that the Vietnam is set to gain on grounds that there may be an acceleration of the China+1 strategy as the US intensifies its trade war with China. **These gains are likely to be more modest and unlikely to be unfettered** as the Trump administration may apply selected tariffs on Vietnam to protect their industries given that much of the supply chain would have already diversified. More importantly, **VND underperformed during Trump's first term despite the economic progress.**

- Minus One: The tariff threat is not a theoretical one given that **prominent members of the incoming Trump administration such as Vice President Vance** were part of the Senate who opposed Vietnam's classification as market economy which leaves them subjected to more prohibitive trade barriers.

- Perception Risks: Into **mid-2025**, the release of the next edition of the US Treasury report on FX policies of their trading partners will be closely watched. Given that Vietnam will remain on the watchlist, it warrants close monitoring to see if they will be "upgraded" to **currency manipulator status** should the SBV be seen as manipulating currency when they attempt rebuild their FX reserves through net purchases. Consequently, we expect the SBV to act cautiously during periods of a softer USD.

- Financial flows: Outflows from equities persisted into December 2025 and intensified in January ahead of Trump's inauguration.

- Outlook: As gains from seasonal festivities fade, we expected continued buoyancy above 25000 and remain concerned about possibility of VND depreciation risk in the months ahead as FX buffers remain low. 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 late Q1 2025 should President Donald Trump mention Vietnam as a possible target for tariffs.

**Rates**

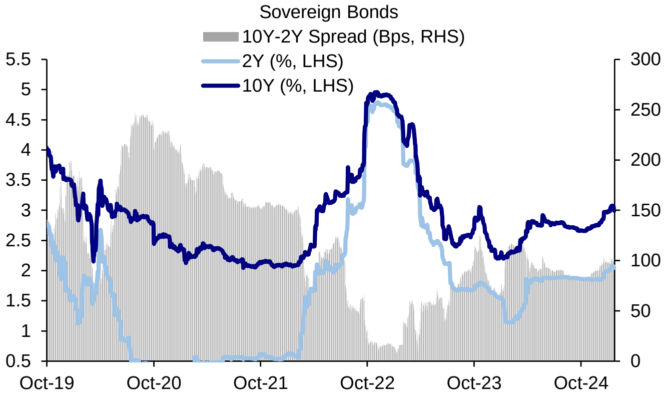
- Central Bank: Even as there is some relief on the VND amid a larger gap with the upper bound, we retain our base case that the SBV will keep rates on hold as the VND will remain the over-riding concern. In fact, the continued sight of restructuring needs of corporate bonds flows will also mean that the authorities may find it difficult to tighten policy to defend the VND.

- Risks: Given the rather strong case for a rate hold, the risks stem from remote tail risks events on both ends. Specifically, policy mistake of rate cuts to bolster growth which would risks VND stability even if it is likely conducted under a softer USD backdrop. On the other end, VND instability may imply that push the SBV towards a rate hike as a lesser evil to a rundown in reserves.

- Yields: Yields were lifted across the curve over the past month amid domestic preference to hold cash ahead of the festive season along with the external driver of higher UST yields.

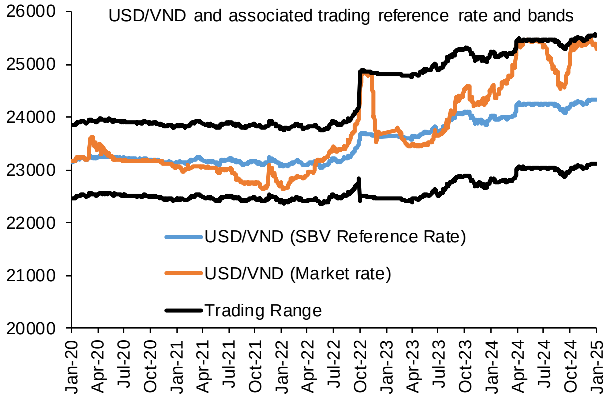
- Curve: There is room for further steepening of the yield curve towards 120bps-140bps range from the current 100bps spread but this will be driven by elevated UST yields and higher term premium in the US.

Fig 12e. Yields rose across the curve



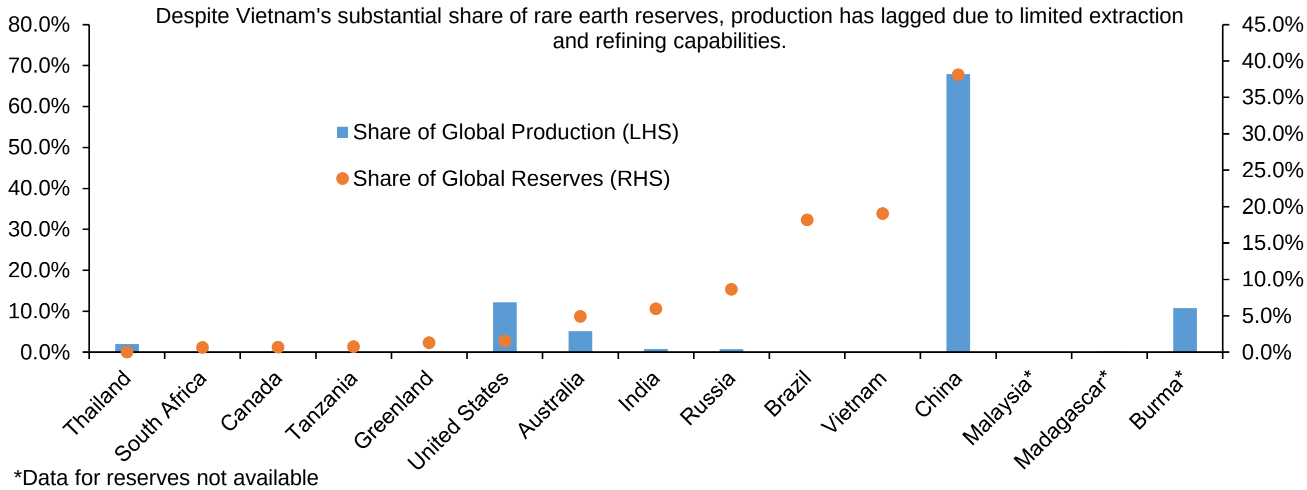

Sources: Bloomberg, Mizuho

Figure12f. VND saw marginal relief ahead of Tet




Source: Bloomberg; Mizuho

## Box 3: Vietnam: Realising Potential




*Data for reserves not available
Sources: USGS, Mizuho

- It has been well noted that Vietnam has the world's second largest reserves of rare earths after China.
- However, this potential remains largely untapped as there is little processing ability domestically.
- In 2022, Vietnam accounted for 1.4% of global rare earth production and 19% of global rare earth reserves. Most of the raw output was imported by China^ which remains the **leader in both mining and refining capabilities.**
- While it is clear that foreign direct investments remain critical for Vietnam to realizes its rare earth potential to support related industries ranging from semiconductors, electric vehicles to military applications, **external support may also be unfortunately limited even though forthcoming**.
- Point being, China's stranglehold on processing capabilities (>80% of global capacity) imply that the US has also been sending rare earth ores to China for processing.
- As such, even as Vietnam has established strategic partnerships with the likes of Australia recently, the mining process and associated processing technology transfer will involve a much longer timeline.
- Looking ahead, as we enter into Trump 2.0, the urgency of establishing supply chain resilience may accelerate such developments in Vietnam to develop an eco-system for rare earths and downstream industries especially as China has began to ban exports of some rare minerals in late 2024.
- That said, given the comparative advantage of Chinese producers, China may also seek to partner Vietnam firms in a bid to retain their refining edge over the US.
- Domestically, environmental concerns and governance issues over lucrative mining concessions will need to be ironed out to allow the underlying potential of rare earths to be realized.

^US geological survey 2022 Minerals Yearbook

## AUD: Proxy Relief and Fears

| | Q4 2024 | Q1 2025 | Q2 2025 | Q3 2025 | Q4 2025 | Q1 2026 |
|---|---|---|---|---|---|---|
| Policy Rate (%) | 4.35% | 4.10% | 3.85% | 3.60% | 3.60% | 3.60% |
| USD/AUD | 0.617-0.694 | 0.610-0.653 | 0.608-0.668 | 0.610-0.673 | 0.645-0.700 | 0.655-0.700 |
| | 0.618 | 0.615 | 0.613 | 0.655 | 0.680 | 0.678 |
| GDP (% YoY) | 0.9 | 1.0 | 0.9 | 1.3 | 1.3 | 1.2 |
| CPI (% YoY) | 2.4 | 2.5 | 2.4 | 2.6 | 2.7 | 2.6 |

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 whipsawed on tariff flip-flop

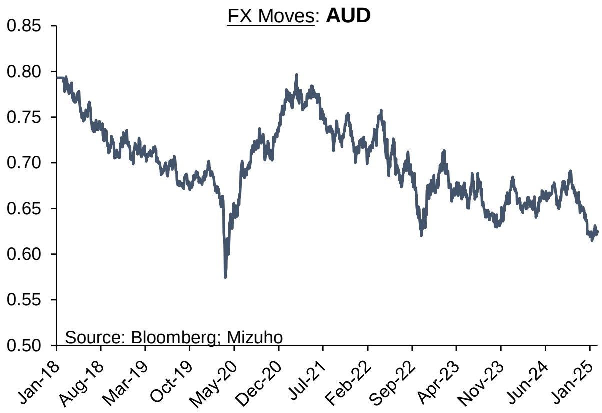
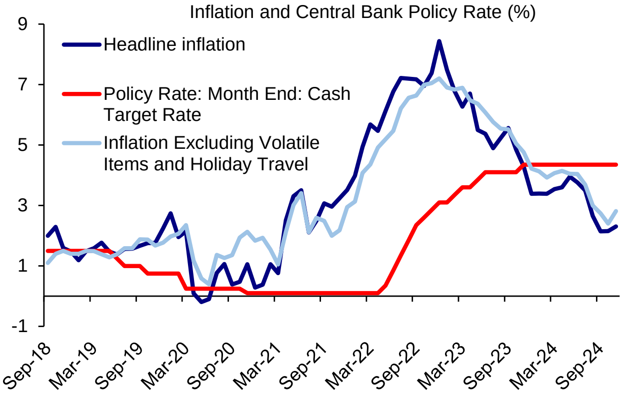
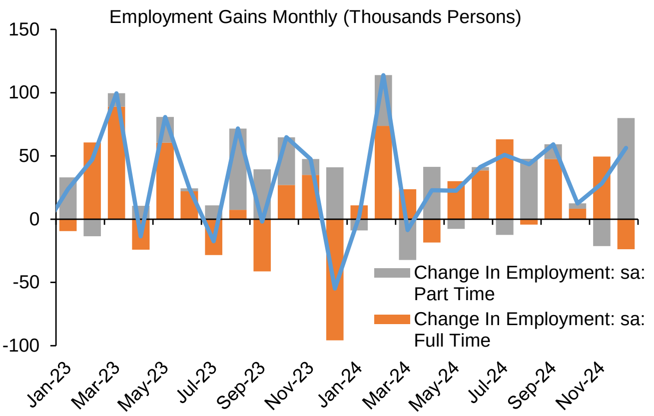



Fig 13b. Inflation less of an impediment to easing



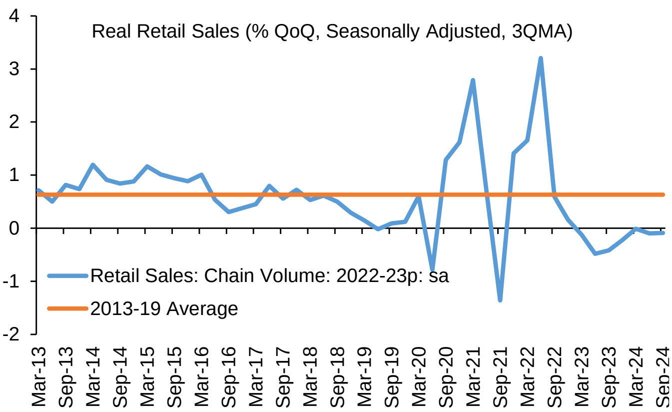

Sources: CEIC, Mizuho

Fig 13c. Employment gains stayed robust…




Source: CEIC; Mizuho

Fig 13d...but real retail sales stayed weak




Sources: CEIC, Mizuho

**FX**

- China's Partial Relief and Risks: AUD has outperformed on expectations of likely negotiations between US and China amid a backdrop of temporal relief for Canada and Mexico. Consequently, the AUD was afforded substantial tailwinds. The road ahead though remains bumpy with Chinese compliance on previous trade agreements being studied, further escalation of trade tensions between US and China very much on the table.

- Stimulus 2.0: While China stimulus has their potential to buoy the AUD, the consumption focused nature of these plans should remind us that the current brand of stimulus should have smaller correlations compared to previous pump priming stimulus via infrastructure projects. Domestically, the RBA's inclination to ease continues to hinge on labour market conditions.

- Employment stayed robust keeping AUD bulls and RBA on the edge: Employment gains were robust in December and the skew towards part time employment is merely reflective of seasonal effects rather than signalling outright weakness. Nonetheless, we continue to reflect that the **distribution of jobs towards lower paying ones imply that these outsized gains translate to a slightly more diminished impact in term of purchasing power.**

- But Real Retail Sales remain Weak: While nominal retail sales prints have brought about some cheer despite some evidence of consumers being price sensitive, the **persistent contraction of real retail sales for the majority of 2024** reflect the inflationary impact on household budgets.

- Validating Dovish Tendencies: Given the RBA's earlier reframing of inflation, softer employment is the next piece of evidence which backs up the RBA's case for easing in Q1. The **problem for the RBA is that the next employment print is only schedule to be release on 20 February which is after their 18 February meeting**. In turn, AUD bulls remain on tenterhooks about the prospects of easing with markets already pricing in three quarters chance of a 25bp cut.

- Insurance Needed?: Consequently, from our earlier call for near term upside volatility, this has evolved into accentuated two way volatility. First, there is strong tendency for the RBA to proceed with an insurance cut. Whether an insurance cut will lead to a bearish AUD is highly dependent on Governor Bullock's signal on the path ahead. Without employment data, she may continue to point to the need for calibration and data dependence in allusion to their milder rate hike cycle. While a cut at their next meeting may not see any immediate collapse of AUD back towards 61 cents, should the easing conspire with employment figures weakening, we would not be surprised to see the AUD retest 61 cents. That said, opportunistic bulls would likely step in at that juncture.

- Weak Hold: Considering the inclination to ease, a hold in February is also unlikely catalyse a rally though it may imply resilience for a few weeks. That said, mixed Chinese data post Lunar New Year implying soft consumer sentiments will also mean that the RBA hold may not end up as a durable backstop.

- Outlook: AUD weakness will continue to linger against the Greenback given expectations for the RBA to ease and still wobbly economic recovery in China. Nonetheless, given a shallower cutting cycle, we hold onto the case for AUD's relative allure against the IDR and PHP which looks more vulnerable and with greater tendencies for deeper cuts. Even against the SGD, there is some relative allure given the MAS's penchant for anchoring growth especially amid plausible trade headwinds and the AUD's slightly higher beta to the CNH should a firmer China growth take hold.

**Rates**

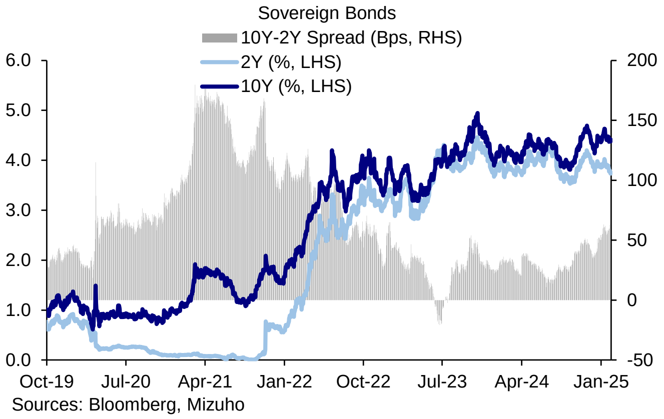
- Central Bank: We have shifted our call for the RBA to ease in February rather than April. Admittedly, this will be a close call. Nonetheless, this is premised around the framing of a pre-emptive cut and any thoughts of an easing cycle will be framed around data dependence.

- Risks: The tail risk is for the RBA to take a small cut of 15bp In February to signal the pre-emptive nature of their cut and in turn markets may be slightly disappointed such a move. The difficulty in communication may imply that front end volatility is par for the course.

- Yields: 10Y yields rose about 10bps while front end 2Y yields hovered around 3.9%. On the front end, ACGB yields skew towards downside given the prospects of easing. Deference to broad UST movements to hold.

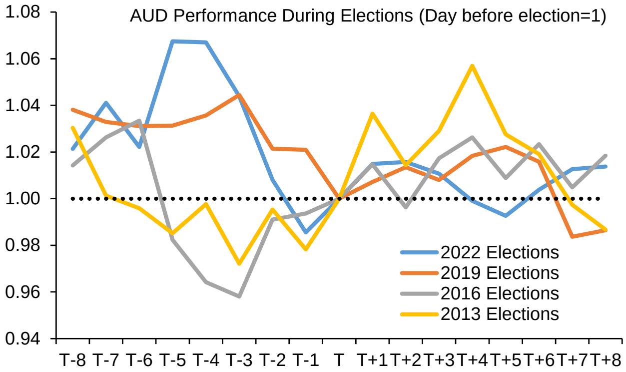
- Curve: Admittedly, after the recent steepening, the 10Y-2Y spread is within historical territory. That said, while there is no immediate concern of fiscal slippages, upcoming elections due by May inevitably brings back forecast on fiscal spending of the next government and avails room for more steepening in the months ahead.

Fig 13e. Long end yields rose and curve steeepened




Sources: Bloomberg, Mizuho

Figure 13f. AUD election performance




Sources: Bloomberg, Mizuho. T denotes day before elections.
T-1 denotes a week before elections

## Global FX Assumptions: USD Bulls – Trade & Trading Volatility

| | Q4 2024 | Q1 2025 | Q2 2025 | Q3 2025 | Q4 2025 | Q1 2026 |
|---|---|---|---|---|---|---|
| **DXY** | 108.5 | 106.2 | 104.3 | 102.8 | 99.5 | 100.6 |
| | 100.7-108.5 | 102.5-110. | 99.0-108.8 | 98.8-105.8 | 97.5-104.3 | 96.0-103.8 |
| **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% | 4.25-4.50% | 3.75-4.00% | 3.25-3.50% | 3.00-3.25% | 3.00-3.25% |
| ECB | 3.00% | 2.50% | 2.00% | 2.00% | 2.00% | 2.00% |
| BoJ | 0.25% | 0.50% | 0.75% | 0.75% | 0.75% | 0.75% |

**The USD Backdrop**

*1)* Volatile USD Bulls amid Tariff Hyper-Sensitivity: The *chaotic, shoot-from-the-hip style of* **Trump 2.0 tariffs make for volatile USD bulls**. Point being, the wider backdrop of tariffs threat generally underpins the Greenback. But *Trump's preferred tactic of front-loading threat bombast as a basis for leverage during subsequent negotiations* **render FX markets hyper-sensitive to (US) tariff headlines**. Typically resulting in FX markets **lurching from exaggerated trade conflict fears to sheer relief of worst-cases averted**.

*2)* Trump, Not Trumped, USD: **But while USD may be prone to pullback from peak tariff surge** amid two-way tariff volatility, the *Greenback* ***will retain relative buoyancy of "USD Trump"***, **not be trumped into a sustained retreat**. Fact is, **Trump's** (loudly) **articulated postures**, and associated bombast will still **buoy the USD through** one of **two channels**. First is *via '****USD exceptionalism****"* and **corresponding USD boost**. The other, from mechanisms of ***US antagonism****,* which in turn, **undermines the currencies at the receiving end**. And with Trump's penchant for trafficking in **uncertainty**, there is **cache to the allure of USD refuge**.

*3)* Albeit with Some Decay: Nonetheless, ***even for the "Trump USD"****,* unchallenged one-way ascendancy ***without any signs of decay*** is highly unlikely. Apart from volatility around tariffs, **some shine could "USD Trump"** on account of disappointment on the economic front. Especially as US exceptionalism is priced to perfection. 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.

*4)* Meaningful Back-end Moderation: In fact, all said, under a confluence of conditions, **USD could mellow meaningfully at the backend of 2025 into H1-2026**; 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.

5) 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, **US economic softening is unlikely to take a linear path.** *Corresponding* (initial) *stickiness of Fed rates could impede a softer USD.* Furthermore, even if US suffered headwinds, **acute US recessions may** (initially) **trigger USD strength** *(from haven demand)* before USD softens on rate cuts. 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.

*6)* Especially with the "Bessent Backstop": Even **more so given that Bessent** (the Treasury Secretary) **has emphasized** how imperative it is for the US that the ***Greenback is unchallenged in its dominance as the world's reserve currency***. This implies a "Bessent backstop that mitigates against **sharp USD declines**.

7) Non-Reversion "USD Smile" Slope: This squares with any moderation in the USD **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) **corresponds to a gently softer USD tracing the slope down the "USD Smile"**.

8) 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 structurally stronger relative to the past through Fed cuts**. More so, **as geo-politics tilts the scale to the advantage of the Greenback.**

9) 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 only factors in two (50bp) rate cuts for 2025, we expect the **Fed may lower rates significantly more** – to about 3.00%. Admittedly, the ***tariff uncertainties might incline the Fed to hold on off cuts initially*** (to mid-2025). But larger catch-down cuts after are 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. The upshot is that **premature hawkish restraint**s on understandable sticky inflation/reflation risks, may prove **misguided, demanding compensatory cuts**.

**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 may be preferred into mid-2025.

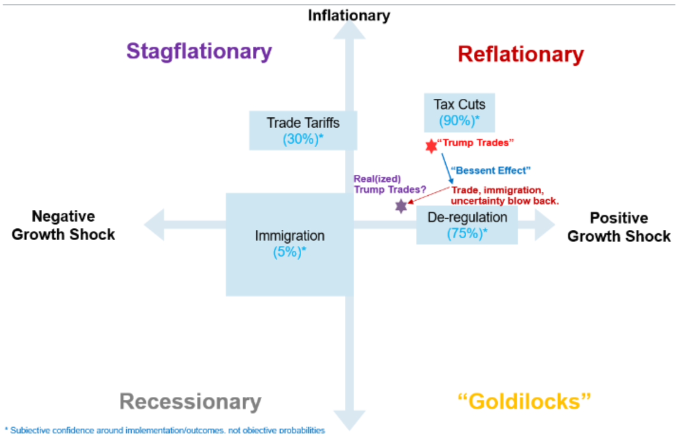
**Box 4: The Trump (Wild) Card (I): Will the Real Trump Trades Please Stand Up?**

"There is nothing more deceptive than an obvious fact." **– Sherlock Holmes**

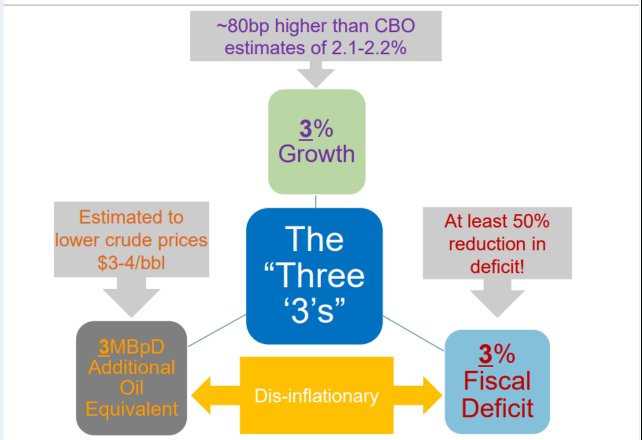
- Trump(-flation) Trades**: Assumptions of Trump-flation**, *conflated with* (growth- and inflation-boosting) *reflation* premised on a confluence of tax cuts, de-regulation, tariffs and immigration, **has driven the so-called "Trump trades"** expressed as;
    i. **brutal bear steepening** (higher yields led by the long-end) of the UST yield curve;
    ii. **unfettered USD bullishness** and**;**
    iii. **ebullient equities.**
- Priced to Perfection: And **Trump trades** appear to be **priced to perfection**, ***if not over-baked*** on account of the implied legislative firepower from the "red-wave" and efficiency/efficacy advantages from of inherited "inside knowledge" on Washington's machinery from the first term.
- But Clarity on Outcomes Low: Trouble is, appearances of **high conviction Trump 2.0 trades are deceptive**. Especially when **clarity on precise Trump 2.0 outcomes** from Trump 2.0 is ***problematically low***.
- Execution Uncertain: Moreover, Trump trades are invariably **subject to the uncertainty of execution** (both in terms of form and timing) of key Trump 2.0 policies, and consequent impact on Trumpflation (reflation).
- Chasing Exuberance: What's more, **this version of Trump trades risks chasing exuberance** *to the point of exhaustion.* Especially given already **richly-valued equities defying surging yields alongside an expensive USD**.
- Testing (US) Exceptionalism: Point being not only are "Trump trades" *over-saturated*, but arguably *inebriated on overly-optimistic narratives that push the envelope on US exceptionalism*.
- Realities of Risk-Rewards: Whereas the **"real(ised)"**,and certainly more realistic, version of **Trump trades must acknowledge less compelling risk-rewards from stretched valuations/positions** (across yields, the Greenback and equities); thereby *limiting unfettered one-way bets.*
- The "Bessent Effect": Crucially, the **"Three 3s" proposed by in-coming Treasury Secretary Scott Bessent warn of doubled down bullish USD-bearish UST bets** (from "Trump trades") **being wrong-footed**; as given the suggestion of a ***dis-inflationary, lower yield path to higher growth aspirations***.
- Taming (USD) & Tempering (UST) Bulls: Hence, there is a **case for softer UST yields** (from current elevation/ascendancy) ***even if/as term premium is decompressed****.* In other words, a **bull** (not bear) **steepening**, with softer yields overall helping to **dampen excessive USD strength**.
- Fed & Trumped-up Reflation: **Especially as early Trumpflation (reflation) expectations prove to be trumped up, which sees the Fed relents on rate restraint amid mellowing reflation risks**.
- Consequently, the **real (and realized) Trump trades** may **temper**, and ***in some cases overturn****,* the **current iteration of Trump trades**., resulting in;
    i. lower, not higher yields as inflationary shocks and fiscal deterioration are overblown;
    ii. a bull (rather than bear) steepener as a Fed that consequently relents on policy restraint (more rate cuts)
    iii. a mellower , not unremittingly stronger, USD from elevated levels (albeit significantly more buoyant compared to pre-Fed tightening levels from late-2021/early-2022, and;
    iv. more differentiated, perhaps *even divergent,* performance in equities as the broad boost to equities from tax cut (extension) are dampened with regards to already richly valued equities, and perhaps further tempered, if not overturned by, regulatory re-allocations and outright tariff dent.

- The upshot is that **tempered USD strength**, **bull steepening** of (a rather elevated) **UST curve** and **stark divergence in equities may be the real(ised) Trump trades** that take into account the execution gaps involved in campaign-to-Oval Office transition.

**Trumpflation May Not be as Reflationary as Currently Assumed**




**The "Bessent Effect": A Dis-inflationary, Lower Yield Path to Higher Growth?**




**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 tariff risks arguably reinforce the case for softer rates***. Not only because of *adverse demand impact* that has not been fully accounted for. But also because, 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 but Deferred: **Lower rates** will also be **accompanied by a steeper yield curve**. With yield curve inversion shrugged off in Q3 2024, the 10-2Y spread for the *UST curve may be set to widen to 30-80bp* into 2025 on a confluence of rate cut mechanics as well as uncertainty further out. *Although deferred into late-2025* **as the Fed suspends easing while it assesses Trump-flation risks amid tariff threats in H1**. But interim Fed restraint on Trump-flation risks means more distinct steepening may be deferred further out as well.

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** (O&G deregulation/incentivization souped up by 3MBpD output increase ambitions associated with Bessent's "Three 3s" plan) could easily offset US exceptionalism demand. So, **oil may soften**. Not just in spite, but partly as a by-product, of US exceptionalism.

OPEC & Russia: Finally, the biggest supply hold-back factor, the **OPEC's deliberate and deliberated production curbs could also start to be loosened**, softening oil. This, partly in response to Russia sanctions that are unlikely to be bullish for oil prices in any case (See Box 5). 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). Also 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.

**Box 5: Oil: Russia Sanctions a Sizable Twitch, Not an Unremitting Trend**

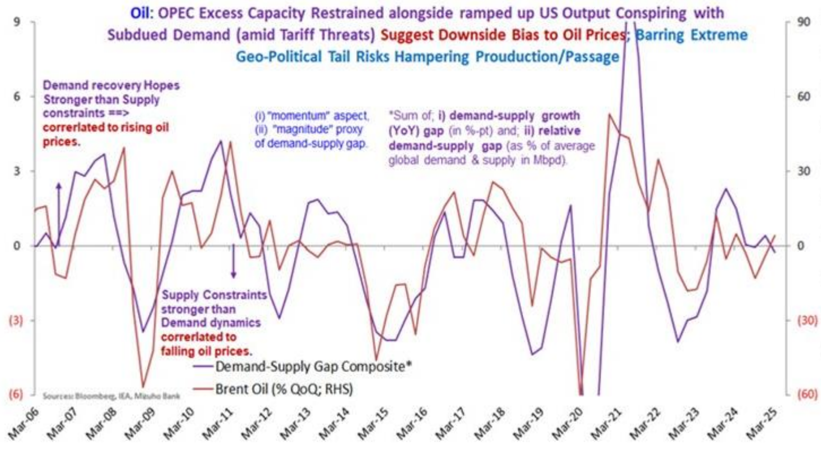
In a Nutshell: The **knee-jerk higher in oil prices form a wider net of (US) sanctions** aimed at impeding the global flow of Russian oil is understandable, but likely overblown. Fact is, the **bigger picture** of **global demand-supply dynamics/risks suggest oil** being **relatively subdued**. So, this twitch is not necessarily a trend. Especially as non-OPEC supply led by US appears to be flush, while "leaky" Russia oil sanctions lead to an even deeper Russia discount. What's more, China may dampen, not inflame, Oil's bullish price dynamic.

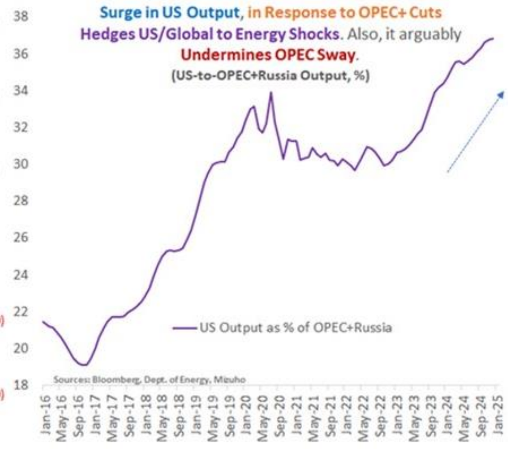
Attendant **inflation fears** and **associated surge in yields** are ***almost certainly overblown*** and ***very likely unsustainable*****,** **although near-term price dynamic may provoke bond bears**. **USD though may find structural lift** (as a more significant net energy exporter) through higher oil, contrary to received wisdom about negative USD-Oil correlations.

**AXJ pain from oil** flares to hit PHP, INR, KRW and THB **based on historical sensitivities, but subject to evolving nuances**. Although ***rupee may get better buffer from Russian oil access*** and ***KRW may be more insulated if shipping costs rise***.

- Wider Russian Sanctions: Brent crude has jumped over $80/bbl in response to **significantly widened net of sanctions on Russia's oil** exports – hitting ***shipping*** , ***trading*** and ***insurance***.

- Supply Crimp Fears: The **bullish (**crude) **price reflex**, presumably ***driven by fears supply being materially crimped*** (to the order of 500K-800KBpd) for is **wholly justified**. And *may be more upside shocks left.*
- But Not a Game-Changer: *But* the **grander demand-supply dynamics** are still shaping up for **relatively stable**, ***not soaring,* oil prices.**
- Five Key Mitigating Factors: To be sure, geo-political shifts continue to pose a serious upside risk to oil. But there are five mitigating factors to quell fears of unremitting bullish trend in oil.




i. Global Demand-Supply to Buffer: For one, the **bigger picture is for aggregate global supply dynamic** to at least **keep apace, if not comfortably outstrip, demand shifts**.
ii. Non-OPEC led Supply Offset: Second, the **of Russia's crude disruption** is likely to be offset elsewhere. OPEC has compelling spare capacity poised for (delayed) output bump-up. Crucially, non-OPEC production outside of Russia has grown significantly, and is set to be flush.
iii. "Leaky" Russian Oil Sanctions: Notably, the **sanctions could still prove "leaky"**. **Russia's oil leaching into global supplies** is **highly likely outcome** (and the lived experience). And with Russian oil **at an even deeper discount**, perversely ***blunting price upside*** from sanctions
iv. US Energy Ascendancy: What' more, **US ambitions to materially lift energy output**, inevitably deepening and solidifying its position as a **net energy exporter** is yet another **critical dynamic to check unmitigated upside* in prices**.
v. Beijing Buffer: On the demand-end, **China's inclination to stockpile during periods of softer prices**, provides the **strategic inventory buffer** to **dampen bullish oil impulses**. Especially as onshore demand recovery remains subpar.

* Admittedly, US producers will welcome price buoyancy, but the supply will subdue the extent of upside in prices, all else equal.

- Bullish Trigger, Not Trend: And so, it may well be that **widening US sanctions** on Russia **prove to be a trigger for some** (and most likely blunted) **bullish adjustment in "equilibrium" price levels**, and ***not an unremitting bullish trend***.
- Inflation Threat Overblown: It follows then that **inflation fears from Russian sanctions** (and resultant rise in oil prices) may be **overblown**. ***Even at $100 barrel***, Brent crude will ***not be nearly as inflationary as*** it was ***in late-2021/2022***.

- Nonetheless, May Fuel Bond Bears: But that said, **Russia sanction/wider geo-political risks** to **Oil** (supply) **could inadvertently fuel already agitated bond bears**; *exaggerating perceptions of* (marginal) *hawkish Fed pivot amid "sticky" inflation* concerns.
- Crude Yield Dynamics: Which suggests that the already **stretched surge in long-end yields may be fueled further in the near-term**. But ***such reflexive crude lift to already elevated yields is unlikely to be sustained*** into late-2025/early-2026.
- USD Gain: *Contrary to received wisdom about negative USD-Oil correlations,* a **structurally stronger USD may square with higher crude prices**. Especially given US ambitions to ramp-up oil/energy output (from record levels), at the expense of geo-political adversaries such as Russia and Iran.
- AXJ Pain: This **could exacerbate AXJ pain that accompanies upside oil** (and attendant inflation) risks. More so given strains from higher UST yields amid (perceptions of) a relatively more hawkish Fed.
- But with Nuanced Differentiation: **But** the exposure of "usual suspects"** such as INR, PHP, KRW, and THB may be **even more nuanced**.
- Notably, *PHP may be relatively harder hit relative to INR* given India's access to (cheaper) Russian oil offset that the Philippines doesn't benefit from.
- And *if shipping costs rise with Oil, KRW is better positioned to enjoy a better offset than THB.*

** Despite the similarity of high (negative) sensitivity to oil prices, PHP and INR are relatively more exposed to high-import reliance (relative to consumption) whereas KRW and THB typically have better industrial offset.

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