Emerging Asia Economics Monthly – March 2009

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Our Vision:

For Economics & Markets Research to be the most respected, sought-after and commercially valued source of economics and markets research and information on Australia, New Zealand, the Pacific and Asia.

Highlights

- Evidence so far suggests that the acute weakness of Q4 2008 has carried over into 2009 largely intact. Trade volumes and investment continue to decline sharply across the region.
- Some positive signs have appeared in PMIs and confidence data. This is particularly true in China, where the massive stimulus effort is starting to gain traction. However, these data signal an inflection point—it is too early to declare a recovery.
- We retain our 2009 call as the "Year of the Bootstrap." Any growth will be domestic-led this year, and the ASEAN group will continue to outperform the more export-dependent NIEs.
- USD-AXJ is expected to remain in an uptrend, but the momentum should eventually slow. SGD and TWD are still seen as under-performers, while CNY continues to tread water.
- Cross-winds in emerging Asian rates are problematic for a directional view, but the signal for the curve is clear—further steepening ahead.

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Emerging Asia's Improving PMIs - Recovery or Inflection Point?

This article examines whether a recovery in parts of emerging Asia is underway. Purchasing Managers Indices (PMIs) in China, India, Hong Kong and Singapore all improved in January, providing a first glimpse of hope since markets took a steep dive in late 2008. We analyse the available PMI sub-indices to try to tease out what is driving the recent improvement. We conclude that PMI improvements, while genuine, are consistent with a moderation in the rate of manufacturing decline (i.e., an inflection point) rather than a recovery. The recent improvement in PMIs to date is based heavily on domestic factors, consistent with our "2009: Year of the Bootstrap" theme.

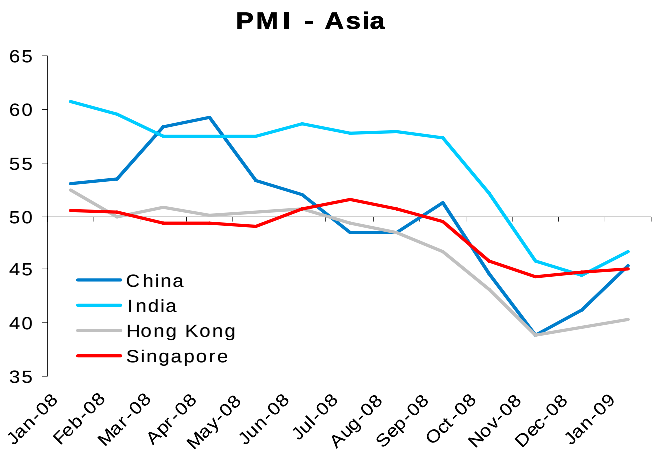
Interpreting Purchasing Managers Indices

A Purchasing Managers Index (PMI) is a manufacturing survey typically based on five major indicators: new orders, inventory levels, production, supplier deliveries and employment levels. Each economy has a customized index, which can include items such as input/output prices to provide an early warning on inflation, or export orders which shed light on the health of the external environment going forward. These are timely indicators of business conditions, released just a single day after the month they reference.

It is important to note that the baseline for a PMI is 50. This level indicates no change in business conditions from the previous period. A reading above 50 indicates that business conditions are improving and vice-versa. However, as survey responses are limited to "improving," "no change" and "declining," the PMI is only useful in estimating the direction of the recovery or decline, and cannot measure the magnitude. Lastly, PMI data are only available for China, India, Singapore and Hong Kong. This sample of economies provides an incomplete, although fairly comprehensive, view of the manufacturing activity in the region.

Distinguishing between an Inflection Point and a Recovery

In the final quarter of 2008, emerging Asia (and almost everywhere else) saw sharp, widespread declines in exports, industrial activity and, to a lesser extent, consumption. These were sparked by a severe drop in growth reflecting balance sheet preservation on the part of banks, a collapse of global trade volumes with knock-on effects for manufacturing, deteriorating household balance sheets due to declining asset values, and a generalized de-leveraging of consumers and firms. The rate of decline across a swath of indicators was the steepest in recent memory as Q4 GDP fell precipitously in many economies, and the sharp downward momentum looked set to continue into early 2009.



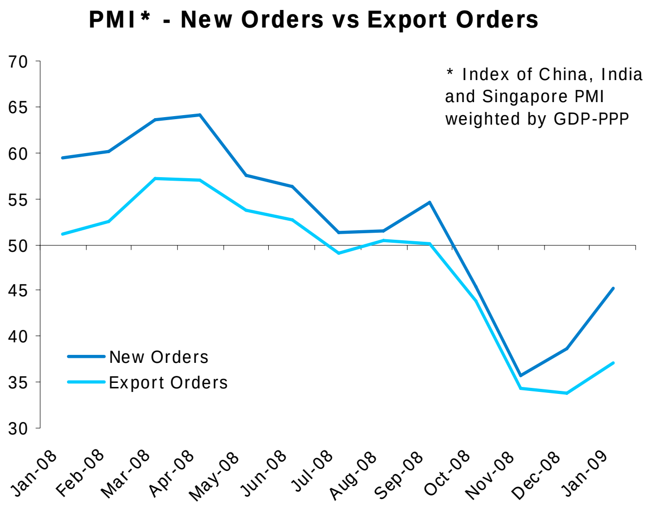
For the first three quarters of 2008, PMI readings across emerging Asia signalled stable or improving conditions. While there was a downward trend in the PMIs for China and India, levels remained at or above the threshold level of 50 for the most part. However, PMI readings fell sharply across all economies in our sample beginning in October with the intensification of the global downturn. This mapped closely into the sharp decline in trade (both exports and imports) as well as investment in the Asia region.

Surprisingly (and encouragingly) PMIs appear to have bottomed in early 2009. The extent of the rebound varies across economies, with China climbing the most while the upturn in the more trade-exposed Hong Kong and Singapore economies has been more modest. Following the release of these data, some commentators have pronounced that a recovery is under way. In our view, a closer look at PMIs is needed in order to arrive at an assessment.

What is Driving the Recent Improvement in PMIs?

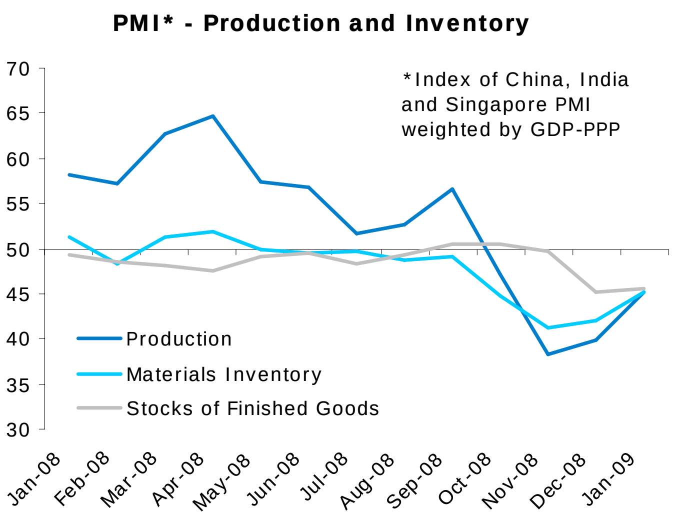
To determine what is behind the recent improvement in PMIs, we "drilled down" into the key sub-indices. In this section we analyze three important slices of Asian composite PMI—orders data, inventory data, and Chinese sectoral data.

Orders – Domestic versus Export-related



In our sample, new orders for China, India and Singapore are now slowing at a less rapid pace than in late 2008. Much of this improvement appears to be coming from domestic orders. In fact, reported export orders (on a PMI, not numerical, basis) are still weaker than in October. The implication is that parts of domestic demand must be firm or improving, and taking a larger share of total production. With the collapse of trade volumes across the region, this would make sense, although for most Asian economies—with the important exception of China—consumption has been flat or contracting, while manufacturing (and industrial production more generally) has slowed sharply.

Inventories



PMI data also suggest a turn in the inventory cycle. With exports and activity declining at a rapid clip in October, Asian manufacturers quickly cut back production and material purchases, as indicated by the steep drops in the relevant PMIs. By December, however, stocks of finished goods had fallen sufficiently to prompt some production restarts and materials purchases, which at least partially explain the bottoming of the PMI. The consumption data (declining real retail sales numbers across the board, although still growing at a healthy pace in China) do not indicate a rebound in consumer spending, eliminating this source as a possible driver of production.

Fiscal Stimulus – The Case of China

The final—and perhaps most compelling—possible explanation for the recent upturn in PMI levels relates to fiscal stimulus-related spending by governments. To explore this case, we look at the Chinese sector level PMI order data to see how different industries (across the traded goods and domestic-oriented sectors) are performing vis-à-vis one another.

- The traded goods sector is still at distressed PMI levels and declining. Textile production continues to fall reflecting extremely weak global demand and trade flows.

- The primary consumption PMI indicator is performing relatively well. The retail trade PMI rose in December and is currently in expansionary territory as consumption in China has been largely unaffected by the global downturn. For now, with exports and investment contracting, consumption is the sole (expenditure) pillar of GDP growth.

- On the investment front, the picture is negative in terms of levels and mixed in terms of momentum. Construction PMI fell steadily during 2008 as the authorities tried to cool growth (an effort which began in early 2007), and is now just below the neutral level, and stable. The metal products industry was hit hard by the global manufacturing slowdown, which came on top of the domestic, policy-induced real estate slowdown. Its PMI has turned up of late, although the level is currently only one-half of early 2008 levels.

Conclusion

PMI readings increased in parts of emerging Asia in early 2009, suggesting signs of a recovery after a dismal final quarter of 2008. This article has taken a closer look at the recent behaviour of PMIs and, based on our analysis, we have the following observations:

- Recent PMI readings are almost uniformly still below the "no change" level of 50. This indicates that manufacturing conditions are still deteriorating and have yet to bottom. However, rising PMI levels indicate that conditions now appear to be deteriorating at a slower pace.

- It is still early days as the improvement in PMIs involves only a few data points. We would prefer to see a more sustained turnaround (with readings consistently above 50) before concluding that a clear recovery trend has been established.

- In our view, therefore, the recent increase in PMIs is consistent with an inflection point or slowing of the rate of deterioration of Asian economies, not a recovery.[1]

Looking ahead, PMIs will be a key indicator to watch in gauging the growth prospects for emerging Asian economies. With asset prices continuing to decline globally and the advanced countries' banking crisis still unresolved, a revival of foreign demand for Asian products still seems a way off. In the meantime, fiscal stimulus programs will seek to support domestic demand in the region and it is here where we would expect to see further improvements in PMIs in the months ahead. While China is likely to have some success in lifting its growth in 2009 (albeit from an estimated quarter-on-quarter growth rate of zero in Q4 2008), for most of the rest of the region a full-fledged recovery will not come about in the absence of a recovery in the US and Europe. And that is something Asia can do precious little about.

Chang Wei Liang

Paul Gruenwald

[1] More formally, the second derivative (or the rate of change of the rate of change) has turned from negative to positive, although the first derivative remains negative.

FX and Rates Strategy Overview:
No Light at the End of the Tunnel

Market Outlook

Q4 2008 and Q1 2009 were already going to be a write-off, but across the globe data reports for the period have fallen far short of expectations—expectations which were pretty gloomy in the first place. Forward looking indicators for Q2 are not very encouraging. Meanwhile, high profile casualties from the front lines of the global financial crisis remain in intensive care, diverting attention away from the passage of a $787bn fiscal stimulus package in the US.

All together, this has pushed US equities through key levels of support—taking off the table whatever risk trades investors had been able to muster and setting up another adverse feedback loop within a vicious circle of plunging asset prices, spiking risk aversion and knock-on effects for the real economy. A clear break in the circle is unlikely until aggressive fiscal and monetary policy responses from around the globe start to bear fruit. Ahead of this, markets must feel confident that the financial crisis is over—something we won't have a handle on for quite some time. Until then, the overall uptrend in USD-AXJ should remain intact.

FX Strategy

The renewed spike in risk aversion has pushed USD-AXJ higher, with USD-KRW still leading the way as the more liquid vehicle for expressing discontent. USD-AXJ has advanced nearly 9% year-to-date, compared with a 25% advance in USD-KRW. Although risk aversion and March debt redemptions remain an immediate hurdle for the KRW, ultimately we expect USD-KRW to lead USD-AXJ lower later this year. As such, we would view the current rally in USD-KRW as an opportunity to lock in attractive levels for the ride down.

Turning to the SGD, the MAS's semi-annual policy meeting is fast approaching in early April, when we expect to have a re-centring and widening in the S$NEER policy band. This would pave the way for further gains in USD-SGD, helping to close the distance with our target for the peak in USD-SGD around the 1.66 area.

Finally, the pace of gains in USD-TWD has started to increase—tracking a staggering drop in exports, a record contraction in GDP, and a still bleak outlook. The Taiwanese authorities have openly sanctioned the move, so further gains in USD-TWD seem assured. The only question is speed.

- ***Corporates***: Hedge SGD and TWD export exposures and balance sheet risk, if USD-based.
- ***Real money funds*** with AXJ allocations: Under-weight SGD and TWD; prepare to over-weight KRW.
- ***Leveraged funds***: Take advantage of dips to buy USD-SGD and USD-TWD forward outright. Take advantage of rallies to sell USD-KRW forward outright.

Rates Strategy

Rates markets in emerging Asia are being buffeted by cross-winds. On the one hand, central banks in the region still have the ability and willingness to cut interest rates further. On the other hand, markets are concerned about a supply overhang as governments begin to finance fiscal stimulus programs. Spikes in risk aversion are also problematic for most of the rates markets in emerging Asia. Although the combination is problematic for a directional view, in terms of the curve the signal is clear—further steepening ahead.

- ***Real money funds*** with emerging Asia in their benchmark should selectively favour bonds with shorter tenors. Allocations should be currency-hedged.
- ***Leveraged funds*** can side-step the problem of negative carry in steepeners by taking on basis risk. For example, a front-end receiver position in Chinese IRS could be paired with a long-end payer position in Korean IRS.

Tamara Henderson

Foreign Exchange and Policy Rate Forecasts

		Current	Mar 09	Jun 09	Sep 09	Dec 09	Mar 10	Jun 10
China	USD/CNY, eop	6.835	6.84	6.84	6.84	6.84	6.84	6.82
	AUD/CNY, eop	4.440	4.30	4.00	3.80	3.70	3.70	3.80
	PBoC base lending rate	5.31	5.04	4.77	4.50	4.50	4.50	4.50
Hong Kong	USD/HKD, eop	7.753	7.76	7.76	7.76	7.76	7.78	7.80
	AUD/HKD, eop	4.989	4.90	4.50	4.30	4.20	4.20	4.40
	HKMA discount rate	0.50	0.25	0.25	0.25	0.25	0.50	1.00
India	USD/INR, eop	51.81	52.0	52.0	51.0	51.0	50.0	50.0
	AUD/INR, eop	32.92	32.8	30.2	28.6	27.5	27.0	28.0
	RBI repo rate	5.50	5.00	4.50	4.00	4.00	4.00	4.50
Indonesia	USD/IDR, eop	12,000	12,000	12,000	11,900	11,600	11,600	11,300
	AUD/IDR, eop	7,829	7,600	7,000	6,700	6,300	6,300	6,300
	BI rate	8.25	7.75	6.75	6.00	6.00	6.00	6.00
Malaysia	USD/MYR, eop	3.67	3.64	3.74	3.80	3.80	3.80	3.75
	AUD/MYR, eop	2.39	2.29	2.17	2.13	2.05	2.05	2.10
	BNM overnight rate	2.00	2.00	1.50	1.50	1.50	1.50	1.50
Philippines	USD/PHP, eop	48.21	48.5	49.5	50.0	49.5	48.8	48.5
	AUD/PHP, eop	31.15	30.6	28.7	28.0	26.7	26.4	27.2
	BSP reverse repo rate	5.00	4.50	3.50	3.50	3.50	3.50	3.50
Singapore	USD/SGD, eop	1.53	1.54	1.58	1.62	1.66	1.66	1.63
	AUD/SGD, eop	0.99	0.97	0.92	0.91	0.90	0.90	0.91
	3M SGD SIBOR	0.70	0.65	0.55	0.55	0.65	0.75	0.95
S Korea	USD/KRW, eop	1,534	1,500	1,400	1,400	1,375	1,350	1,300
	AUD/KRW, eop	982	950	810	780	740	730	730
	BoK overnight call rate	2.00	1.50	1.00	1.00	1.00	1.50	2.00
Taiwan	USD/TWD, eop	34.85	35.2	36.0	36.0	35.5	35.5	35.0
	AUD/TWD, eop	22.45	22.2	20.9	20.2	19.2	19.2	19.6
	CBC discount rate	1.25	1.25	1.00	0.50	0.50	1.00	1.25
Thailand	USD/THB, eop	36.06	36.2	37.6	39.4	39.4	38.8	38.8
	AUD/THB, eop	23.29	22.8	21.8	22.1	21.3	21.0	21.7
	BoT repo rate	1.50	1.00	0.50	0.50	0.50	0.50	0.50
Vietnam	USD/VND, eop	17,480	17,500	17,800	18,100	18,500	18,500	18,000
	AUD/VND, eop	11,267	11,000	10,300	10,100	10,000	10,000	10,100
	SBV base lending rate	7.00	6.00	5.00	5.00	5.00	5.00	5.00

Foreign Exchange Cross-Rate Forecasts

	Current Spot	ANZ Forecast					Current 12M Fwd or NDF	Implied 12M % Change	
		Mar-09	Jun-09	Sep-09	Dec-09	Mar-10		ANZ	Forwards
CNY-HKD	1.14	1.13	1.14	1.14	1.14	1.14	1.12	0%	-1%
CNY-INR	7.31	7.60	7.60	7.46	7.46	7.31	7.54	0%	3%
CNY-IDR	1,770	1,830	1,900	1,830	1,700	1,700	2,140	-4%	21%
CNY-MYR	0.528	0.532	0.547	0.556	0.556	0.556	0.529	5%	0%
CNY-PHP	7.06	7.09	7.24	7.31	7.24	7.13	7.13	1%	1%
CNY-SGD	0.221	0.225	0.231	0.237	0.243	0.243	0.218	10%	-1%
CNY-KRW	220	219	205	205	201	197	209	-10%	-5%
CNY-TWD	5.10	5.15	5.26	5.26	5.19	5.19	4.86	2%	-5%
CNY-THB	5.23	5.29	5.50	5.76	5.76	5.67	5.17	8%	-1%
HKD-INR	6.43	6.71	6.71	6.58	6.57	6.43	6.77	0%	5%
HKD-IDR	1,560	1,610	1,670	1,600	1,490	1,490	1,910	-4%	22%
HKD-MYR	0.465	0.469	0.481	0.487	0.488	0.488	0.471	5%	1%
HKD-PHP	6.22	6.25	6.37	6.41	6.35	6.26	6.36	1%	2%
HKD-SGD	0.194	0.199	0.203	0.208	0.213	0.213	0.194	9%	0%
HKD-KRW	194	193	180	179	176	173	186	-11%	-4%
HKD-TWD	4.49	4.54	4.63	4.62	4.55	4.55	4.34	1%	-3%
HKD-THB	4.61	4.67	4.84	5.05	5.05	4.97	4.62	8%	0%
INR-IDR	242	231	231	233	227	232	274	-4%	14%
INR-MYR	0.072	0.070	0.072	0.075	0.075	0.076	0.071	3%	-4%
INR-PHP	0.97	0.93	0.95	0.98	0.97	0.98	0.98	1%	1%
INR-SGD	0.030	0.030	0.030	0.032	0.033	0.033	0.029	8%	-5%
INR-KRW	30.1	28.8	26.9	27.5	27.0	27.0	29.5	-14%	-6%
INR-TWD	0.697	0.677	0.692	0.706	0.696	0.710	0.661	2%	-5%
INR-THB	0.716	0.696	0.723	0.773	0.773	0.776	0.711	7%	-21%
IDR-MYR	0.00030	0.00029	0.00029	0.00030	0.00033	0.00033	0.00025	10%	-17%
IDR-PHP	0.00398	0.00388	0.00381	0.00400	0.00427	0.00421	0.00333	6%	-16%
IDR-SGD	0.00012	0.00012	0.00012	0.00013	0.00014	0.00014	0.00010	15%	-18%
IDR-KRW	0.124	0.120	0.108	0.112	0.119	0.116	0.097	-6%	-22%
IDR-TWD	0.00288	0.00282	0.00277	0.00288	0.00306	0.00306	0.00227	6%	-21%
IDR-THB	0.00295	0.00290	0.00289	0.00315	0.00340	0.00334	0.00242	13%	-18%
MYR-PHP	13.4	13.3	13.2	13.2	13.0	12.8	13.5	-4%	1%
MYR-SGD	0.418	0.423	0.422	0.426	0.436	0.436	0.412	4%	-1%
MYR-KRW	417	412	374	368	361	355	395	-15%	-5%
MYR-TWD	9.65	9.67	9.63	9.47	9.33	9.33	9.20	-3%	-5%
MYR-THB	9.90	9.95	10.05	10.37	10.36	10.20	9.79	3%	-1%
PHP-SGD	0.031	0.032	0.032	0.032	0.034	0.034	0.031	9%	-2%
PHP-KRW	31.2	30.9	28.3	28.0	27.8	27.7	29.3	-11%	-6%
PHP-TWD	0.722	0.726	0.727	0.720	0.717	0.727	0.682	1%	-6%
PHP-THB	0.741	0.746	0.760	0.788	0.796	0.795	0.726	7%	-2%
SGD-KRW	997	974	886	864	828	813	958	-18%	-4%
SGD-TWD	23.1	22.9	22.8	22.2	21.4	21.4	22.3	-7%	-3%
SGD-THB	23.7	23.5	23.8	24.3	23.7	23.4	23.8	-1%	0%
KRW-TWD	0.023	0.023	0.026	0.026	0.026	0.026	0.023	14%	1%
KRW-THB	0.024	0.024	0.027	0.028	0.029	0.029	0.025	21%	4%
TWD-THB	1.03	1.03	1.04	1.09	1.11	1.09	1.06	6%	4%

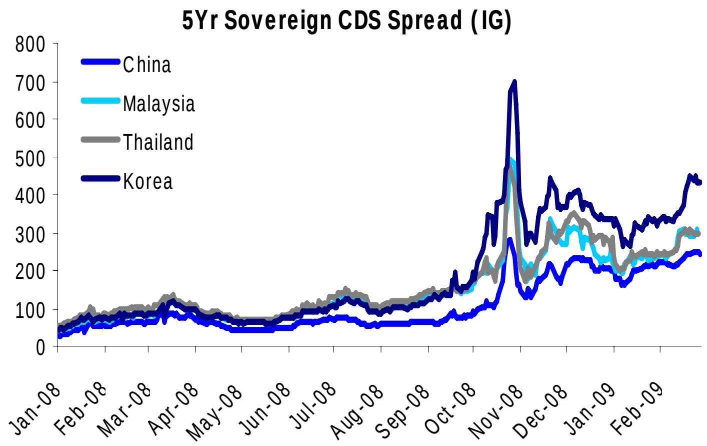
Long-Term Foreign Currency Government Bond Ratings

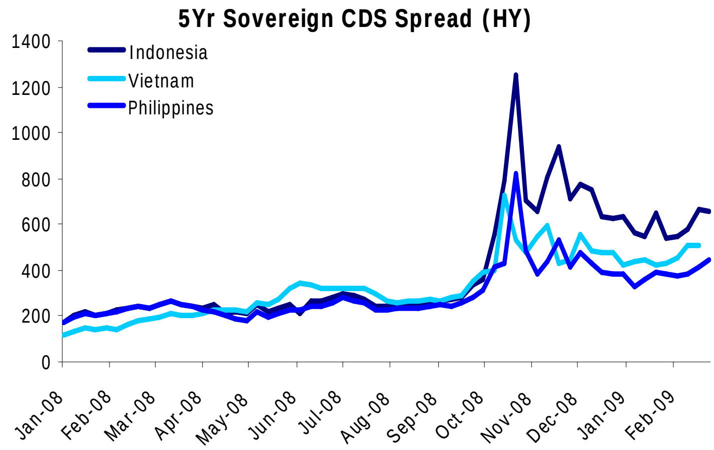
	Moody's	S&P	Fitch
Investment Grade			
China	A1	A+	A+
Hong Kong	Aa2	AA+	AA
India	Baa2	BBB-	BBB-
Korea	A2	A	A+
Malaysia	A3	A-	A-
Singapore	Aaa	AAA	AAA
Taiwan	Aa3	AA-	A+
Thailand	Baa1	BBB+	BBB+
Sub-Investment Grade			
Cambodia	B1	B+	NR
Indonesia	Ba3	BB-	BB
Philippines	B1	BB-	BB
Vietnam	Ba3	BB	BB-

*denotes an upgrade; # denotes a downgrade over previous month

Source: Bloomberg

Sovereign CDS Spreads

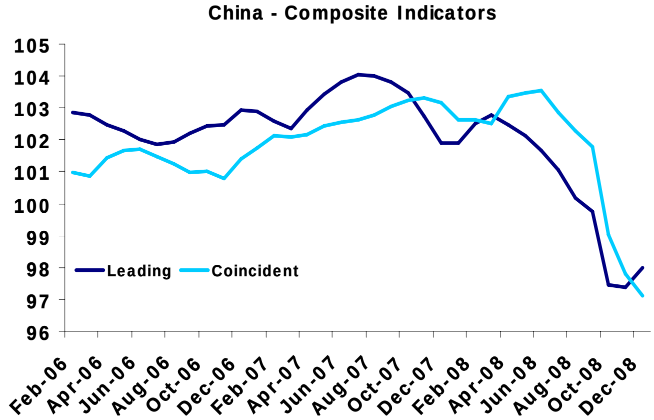


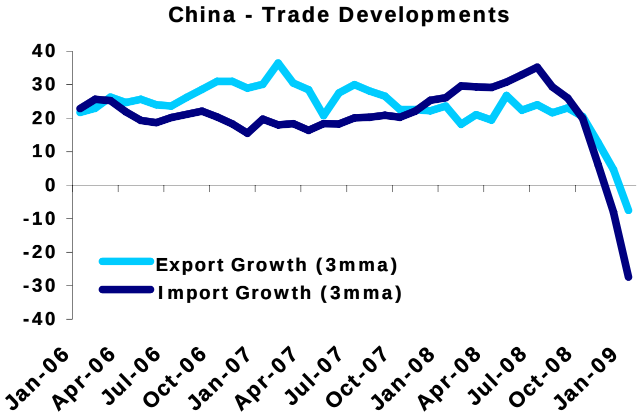


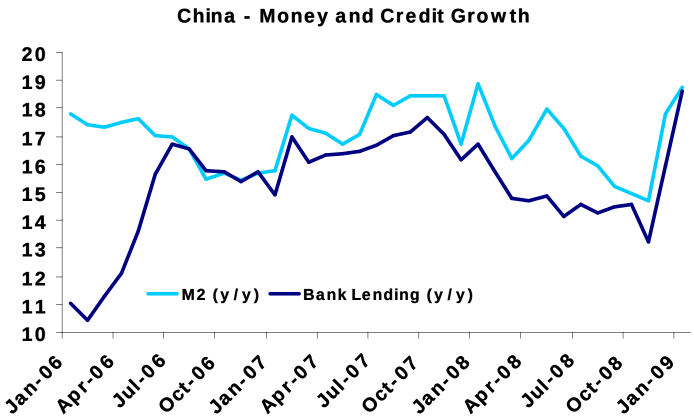
Source: Bloomberg

Source: Bloomberg

Country Update: China







Some consumer and production data suggest the beginning of a turnaround, but trade numbers remain dismal. The stimulus plan appears to be gaining traction but it is too early to declare a recovery. The timing of the Lunar New Year complicates our assessment.

- Retail sales during the Lunar New Year holiday (25-31 Jan) rose 14% (y/y) led by electronic appliances. Vehicle sales continued to slide in Jan, falling by 14.4% (y/y). The pace of decline, particularly for passenger cars, seems to be stabilizing.
- PMI numbers improved in January. Both the official and CLSA series rose, but with readings below 50 continuing to signal a contraction in activity. Orders and purchasing sub-indices out-performed. The composite leading indicator turned up modestly in Dec, but remains well below 2008 levels. The coincident indicator continues to decline.
- Trade collapsed in Jan. Exports contracted by 17.5% (y/y), the worst outturn in 13 years, while imports fell by a staggering 43.1%, a record decline. The trade surplus remained around $40bn.
- The CPI fell to 1% (y/y) in Jan, the lowest in two years. Services and non-food prices are now declining. Producer prices fell by 3.3%. Housing prices are also declining, with the 70-city index falling by 0.9% in Jan.
- Banks lent a record RMB1.62 trillion in Jan in a push to stimulate the economy. About 40% of the recent sharp increase was the purchase of discounted bills, while around one-third was long-term corporate loans. The PBOC is reportedly monitoring credit quality closely.
- While some recent data are encouraging, we are cautious about declaring a recovery. That being said, China may have reached an inflection point where the decline in growth is now levelling off. We continue to expect growth to be below the 8% comfort level for most of this year.

Paul Gruenwald

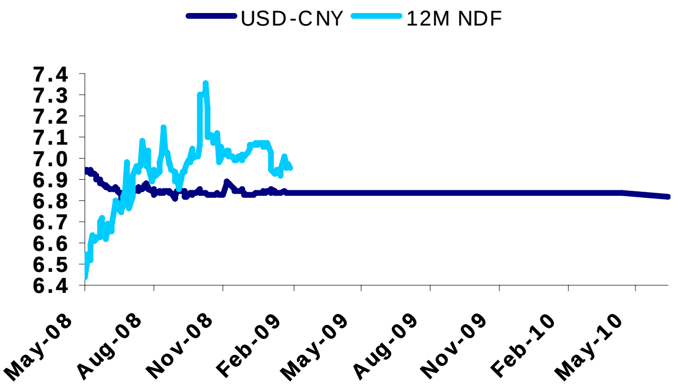
Economic Data - China

Monthly data	Jun-08	Jul-08	Aug-08	Sep-08	Oct-08	Nov-08	Dec-08	Jan-09
Industrial Production, % y/y	16.0	14.7	12.8	11.4	8.2	5.4	5.7	N/A
Retail Sales, % y/y	23.0	23.3	23.2	23.2	22.0	20.8	19.0	14.0
Consumer Price Index, % y/y	7.1	6.3	4.9	4.6	4.0	2.4	1.2	1.0
Exports, % y/y	17.7	26.9	21.1	21.3	19.1	-2.2	-2.8	-17.5
Imports, % y/y	31.2	33.6	22.9	20.9	15.4	-18.0	-21.3	-43.1
Trade Balance, US$ bn	21.4	25.3	28.7	29.4	35.2	40.1	39.0	39.1
Foreign Exchange Reserves, US$ bn	1,808.8	1,845.2	1,884.2	1,905.6	1,879.7	1,884.7	1,946.0	N/A
Quarterly data	**Mar-07**	**Jun-07**	**Sep-07**	**Dec-07**	**Mar-08**	**Jun-08**	**Sep-08**	**Dec-08**
Real GDP, % y/y	13.0	14.0	13.0	12.0	10.6	10.1	9.0	6.8
-Primary Sector ytd	4.4	4.0	4.3	3.7	2.8	3.5	4.5	5.5
-Secondary sector ytd	14.6	15.0	14.8	14.7	11.5	11.3	10.6	9.3
-Tertiary sector ytd	12.7	13.5	14.0	13.8	10.9	10.7	10.5	9.5
Nominal GDP, RMB tn	5.3	11.2	17.4	25.7	6.3	13.5	20.8	30.1
Current Account, US$ bn (semi-	N/A	162.9	N/A	371.8	N/A	191.7	N/A	N/A
Capital Account, US$ bn (semi-annual)	N/A	1.5	N/A	3.1	N/A	1.7	N/A	N/A

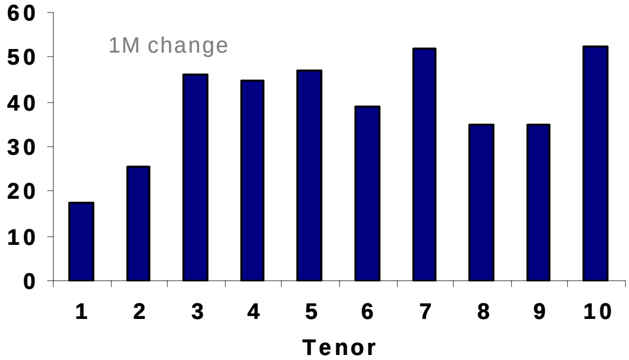
Source:CEIC

China: FX and Rates Strategy

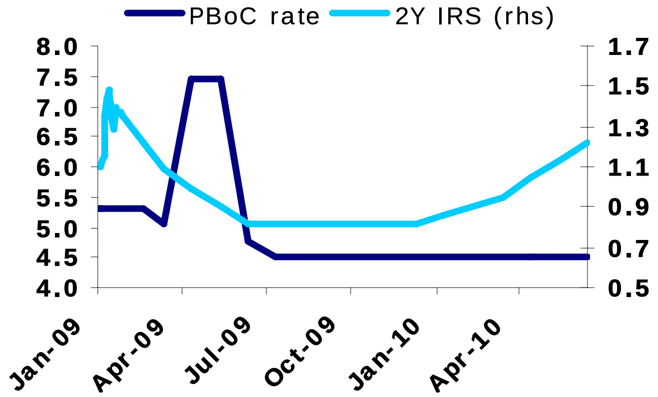
NDFs have pared devaluation expectations



IRS Curve: More bear steepening in February



Rates nearing trough



USD-CNY remains in a holding pattern, while speculation surrounding a possible CNY devaluation has ebbed—although NDFs are still pricing in risk of a move toward the 7.0 level. Both data and the PBOC have tempered rate cut hopes.

FX

USD-CNY continues to tread water—around 6.84 since July 2008. Meanwhile, market speculation about a possible devaluation has ebbed in the wake of official commentary by the Premier, SAFE and the PBOC—all suggesting that the CNY will be kept stable. Also, recent data suggest that China's fiscal stimulus is starting to gain some traction, reducing the need for a devaluation in the first place.

We continue to believe that the authorities will opt for USD-CNY stability during the current slowdown, as any economic gains from a devaluation would be short-lived at best. Indeed, during the Asian crisis in 1997/98, the authorities kept the CNY steady amid sharply weaker currencies in the rest of the region.

As such, USD-CNY is expected to remain in a holding pattern until the authorities are confident that sufficient growth momentum has been restored. At such time (unlikely in 2009), a resumption in gradual CNY appreciation against the USD is anticipated. Adding to the cause for a weaker USD over the longer-term, PBOC Governor Zhou has called for raising the status of the IMF's SDR currency basket as a means to avoid an excess concentration of FX reserves in a single currency.

Rates

A surge in bank lending along with PBOC commentary have prompted markets to scale back rate cut hopes. PBOC Governor Zhou alluded to the use of "different tools" for monetary policy, while Deputy Governor Yi said that the current policy rate is at the proper level and that there was limited room to cut further.

Although the pace of deterioration appears to be slowing, a recovery is not yet at hand. As such, we expect another 81bps of cuts from the PBOC; this should bring a bout of bull-steepening back to the CNY rates market.

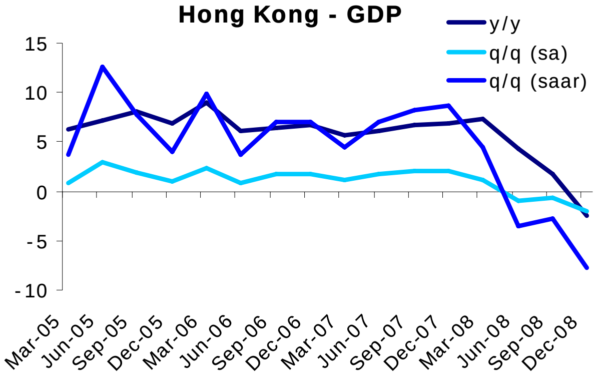
Tamara Henderson

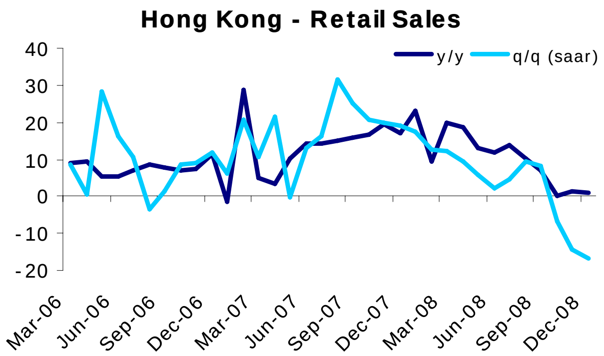
Market Forecasts - China

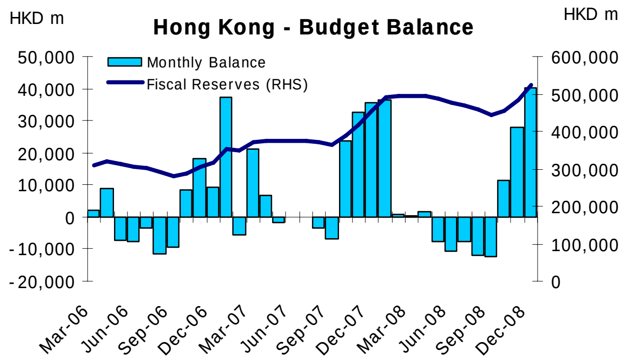
FX	Current	Ytd	Mar-09	Jun-09	Sep-09	Dec-09	Mar-10	Jun-10
USD-CNY	6.835	0.1%	6.84	6.84	6.84	6.84	6.84	6.82
AUD-CNY	4.440	-7.4%	4.30	4.00	3.80	3.70	3.70	3.80
NZD-CNY	3.510	-11.1%	3.40	3.10	2.90	2.80	2.90	2.90
JPY-CNY	0.074	-2.2%	0.070	0.068	0.068	0.067	0.065	0.063
EUR-CNY	8.834	-7.4%	8.55	8.21	7.66	7.39	7.39	7.50
Rates	**Current**	**Ytd**	**Mar-09**	**Jun-09**	**Sep-09**	**Dec-09**	**Mar-10**	**Jun-10**
PBOC's 1-year base lending rate	5.31	0	5.04	4.77	4.50	4.50	4.50	4.50
3-month SHIBOR	1.28	-50	1.1	1.0	0.8	0.8	0.9	1.1
2-year IRS (onshore vs 7-day repo fix)	1.36	28	1.1	0.8	0.8	0.8	1.0	1.2
10-year IRS	2.80	101	2.7	2.6	2.6	2.6	2.7	2.8

Sources: ANZ and Bloomberg

Country Update: Hong Kong







Hong Kong suffered its first quarterly contraction since Q2 2003 as exports plunged at a faster rate. Retail sales growth held steady, while inflation unexpectedly rose. The government unveiled another stimulus package to tackle rising unemployment. 2009 will remain a difficult year.

- Hong Kong's Q4 GDP contracted by 2.5% after growing 1.7% in Q3. On a q/q basis, the economy shrank 2% (sa). For the whole of 2008, the economy expanded 2.5%.
- Retail sales held up, growing 0.9% (y/y) in Dec after 1.2% in Nov. In terms of volume, a decline of 0.7% in Dec was an improvement over the 2.7% contraction in Nov. Unemployment continued to deteriorate, climbing ½ ppt to 4.6% in Jan.
- Following a drop of 11% (y/y) in Dec, exports declined 22% in Jan as global demand receded. Imports contracted at a faster pace of 27% (versus -16% in Dec), and the trade balance posted a HK$7bn surplus, the first since Jan 2006.
- Inflation was higher than expected at 2.7% (y/y) in Jan, up from 2.1% in Dec, as an increase in food prices more than offset a large decline in energy prices. Nevertheless, inflation is expected to ease as the downturn weighs further on demand.
- The government unveiled another stimulus package worth HK$1.6bn to tackle unemployment and create 62,000 jobs. Other measures included a 50% cut in the personal income tax and a 20% reduction in the rental on government properties. The island expects to incur a fiscal deficit of HK$40bn for 2009-10, but ample fiscal reserves imply that public finances remain healthy.
- Conditions in 2009 will remain challenging as both external and domestic demand remains subdued. However, closer economic cooperation with China in terms of tourism development and cross-border infrastructure projects will help mitigate the impact from the global recession.

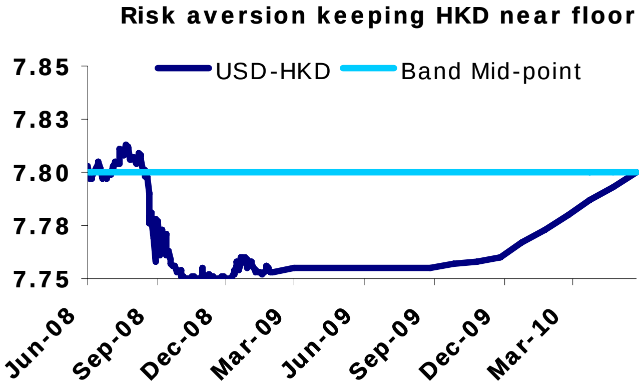
Chong, Jun-Jie

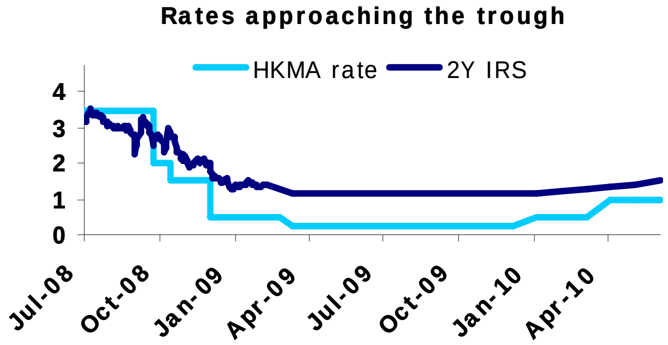
Economic Data - Hong Kong

Monthly data	**Jun-08**	**Jul-08**	**Aug-08**	**Sep-08**	**Oct-08**	**Nov-08**	**Dec-08**	**Jan-09**
Retail Sales, % y/y	11.7	13.7	10.2	7.0	0.3	1.2	0.9	N/A
Composite Consumer Price Index sa, % y/y	6.1	6.3	4.5	3.1	1.7	3.1	2.1	2.7
Exports, % y/y	-0.6	11.1	1.9	3.6	9.4	-5.3	-11.4	-21.8
Imports, % y/y	1.3	15.4	1.5	3.9	11.3	-7.9	-16.2	-27.1
Trade Balance, US$ bn	-3.1	-2.5	-1.6	-2.1	-1.8	-1.1	-1.5	N/A
Foreign Exchange Reserves, US$ bn	152.1	153.3	153.2	153.7	149.3	160.5	178.1	N/A
Quarterly data	**Mar-07**	**Jun-07**	**Sep-07**	**Dec-07**	**Mar-08**	**Jun-08**	**Sep-08**	**Dec-08**
Industrial Production, % y/y	-1.6	-2.3	-2.0	-0.3	-4.4	-4.2	-6.7	N/A
Real GDP, % y/y	5.6	6.1	6.7	6.9	7.3	4.3	1.7	-2.5
-Private consumption	5.3	7.6	11.3	9.7	7.6	3.5	0.0	-3.2
-Government consumption	2.5	3.8	2.4	3.3	0.6	3.2	2.0	2.6
-Gross fixed capital formation	0.3	6.5	-1.1	8.0	10.1	4.9	3.2	-17.3
Nominal GDP, HKD bn	373.6	378.1	415.4	447.9	410.6	401.6	429.9	436.4
Current Account, US$ bn	8.4	3.2	7.8	6.1	6.6	4.0	9.7	N/A
Capital & Financial Account, US$ bn	-10.2	-5.1	-9.6	-8.3	-4.3	-2.6	-11.9	N/A

Sources: Bloomberg, CEIC

Hong Kong: FX and Rates Strategy





USD-HKD remains near the floor of the trading band as risk aversion remains acute amid ongoing casualties from the front lines of the global financial crisis. We expect the HKMA to narrow the gap with the Fed funds target, bringing the policy rate to 0.25% before the end of March.

FX

It is essentially the same story for USD-HKD, with acute risk aversion keeping the pair near the floor of the 7.75-7.85 trading range. In the wake of the Lehman Brothers bankruptcy in September, USD-HKD was pinned down by a mass unwinding of carry trades. Now, we are seeing hot money inflows from mainland China.

Meanwhile, a $787bn fiscal stimulus package was approved by the US Congress in late February, but this has failed to stem renewed haemorrhaging in global equity markets, especially in the financial sector. US banks, automakers and the mammoth insurer AIG are still struggling, while the Dow has breached a key technical precipice of support.

As such, we now expect USD-HKD to remain near the floor of the trading band for most of 2009. The climb-out of this mess—to which the Hong Kong economy is highly exposed via trade as well as financial links—is going to be painstaking. In the current environment there is negligible risk that the peg will be dismantled.

Rates

In order to maintain the viability of the USD-HKD currency peg, HKMA monetary policy must mirror that of the US Federal Reserve. Like the Fed, the HKMA has cut policy rates sharply. Unlike the Fed, the HKMA has a bit more ammunition left. Meanwhile, HKMA chief Yam said the "second wave [of the financial crisis] is upon us…and may well carry greater risks to emerging markets." We expect the HKMA to narrow the gap with the Fed Funds target before the end of March, bringing the HKMA's base rate to 0.25% from 0.50% currently.

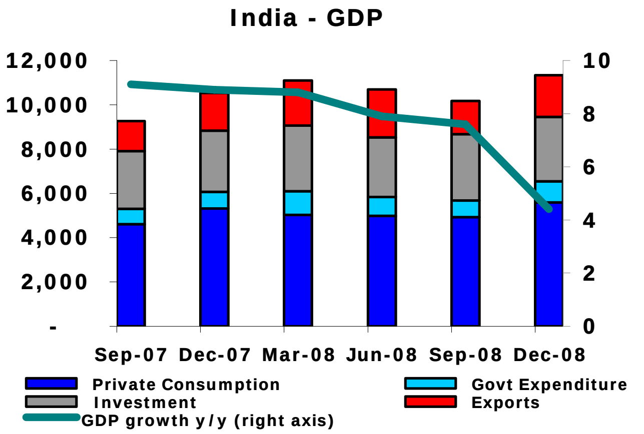
Tamara Henderson

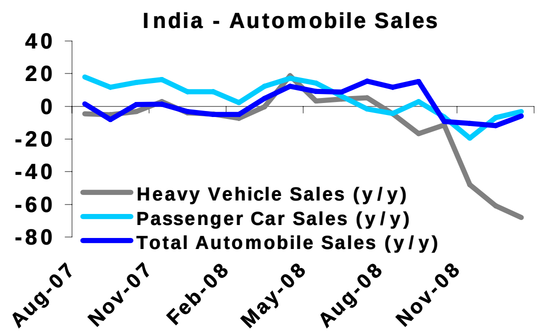
Market Forecasts - Hong Kong

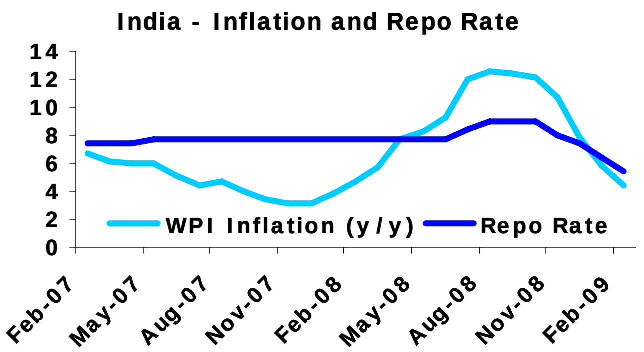
FX	Current	Ytd (%)	Mar-09	Jun-09	Sep-09	Dec-09	Mar-10	Jun-10
USD-HKD	7.753	0.0%	7.755	7.755	7.755	7.760	7.780	7.800
AUD-HKD	4.989	-8.4%	4.9	4.5	4.3	4.2	4.2	4.4
NZD-HKD	3.943	-12.2%	3.9	3.5	3.3	3.2	3.3	3.4
JPY-HKD	0.082	-4.2%	0.079	0.078	0.077	0.076	0.074	0.072
EUR-HKD	9.859	-9.0%	9.7	9.3	8.7	8.5	8.4	8.6
Rates	**Current**	**Ytd (bps)**	**Mar-09**	**Jun-09**	**Sep-09**	**Dec-09**	**Mar-10**	**Jun-10**
HKMA's discount rate	0.50	0	0.25	0.25	0.25	0.25	0.50	1.00
3-month HIBOR	0.78	-17	0.5	0.5	0.5	0.5	0.7	0.9
2-year IRS (onshore vs 3M HIBOR)	1.38	-11	1.1	1.1	1.1	1.1	1.3	1.5
10-year IRS	2.32	39	2.2	2.2	2.2	2.2	2.3	2.4

Sources: ANZ, Bloomberg

Country Update: India







A sharp drop in industrial production and no sign of recovery in automobile sales suggests further deterioration in the economy. Limited fiscal space and looming elections place the burden of sustaining the pace of activity squarely on the RBI. In the wake of weak Q4 GDP, a further reduction in the repo rate is on the horizon.

- GDP growth slowed to 5.3% (y/y) in Q4, following 7.6% in Q3. Private consumption remained relatively robust, while government spending surged. A lack of foreign demand and weak investment place domestic consumption as the sole (expenditure) pillar of growth.
- Registering the worst performance since 1993, industrial production posted a 2.0% (y/y) decline in Dec following modest growth of 2.4% in Nov. Automobile sales dropped by 6.0% in Jan with heavy vehicle sales contracting by 68% and passenger car sales falling by 3.2%.
- WPI inflation fell to 3.4% (y/y) in the week ending February 14, well within the RBI's comfort level of 5% and providing scope for further rate cuts.
- The excise duty on imports and the service tax were lowered by 2% to 8% in the recent fiscal announcements made by the government, implying a revenue loss of $6bn. The deteriorating fiscal position has led S&P to downgrade India's sovereign outlook to negative.
- With the model code of conduct in force before elections and limited capacity for fiscal expansion, the onus of sustaining growth rests on monetary policy. Still, the new government may feel compelled to announce new fiscal measures after elections in May.

Vimal Balasubramaniam

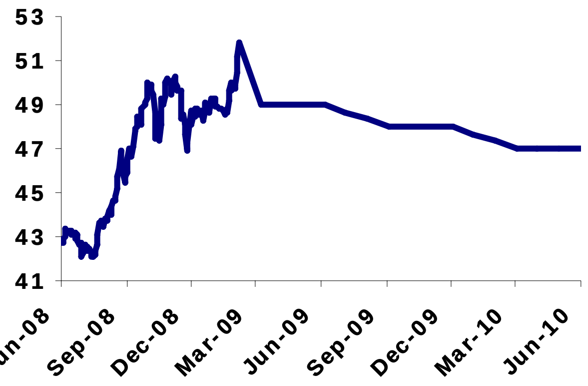
Economic Data - India

Monthly data	Jun-08	Jul-08	Aug-08	Sep-08	Oct-08	Nov-08	Dec-08	Jan-09
Industrial Production, % y/y	5.4	6.4	1.7	6.0	-0.3	1.7	-2.0	N/A
Automobile Sales, % y/y	8.7	15.3	11.7	15.2	-9.3	-10.4	-11.8	-6.0
Wholesale Price Index, % y/y	12.0	12.5	12.9	12.1	10.7	8.2	5.9	5.0
Exports, % y/y	39.2	37.1	27.8	10.4	-12.1	-9.9	-1.1	N/A
Imports, % y/y	32.5	57.2	46.6	43.3	10.6	6.1	8.8	N/A
Trade Balance, US$ bn	-9.2	-11.7	-12.9	-10.6	-10.5	-10.1	-7.6	N/A
Foreign Exchange Reserves, US$ bn	302.3	295.9	286.1	277.3	244.0	239.0	246.6	N/A
Quarterly data	**Mar-07**	**Jun-07**	**Sep-07**	**Dec-07**	**Mar-08**	**Jun-08**	**Sep-08**	**Dec-08**
Real GDP, % y/y	9.8	9.1	9.1	8.9	8.9	7.9	7.6	5.3
-Agriculture	5.3	4.4	4.4	6.9	3.1	3.0	2.7	-2.2
-Industry	12.4	9.9	10.0	8.7	7.0	7.5	6.5	2.0
-Services	10.5	10.8	10.3	10.2	11.9	10.0	9.6	9.9
Nominal GDP, INR tn	10.4	9.9	9.8	11.4	11.9	11.5	11.7	1
Current Account, US$ bn	4.2	-6.7	-4.3	-4.5	-1.5	-9.8	-12.5	N/A
Capital Account, US$ bn	15.8	17.8	33.2	31.0	26.0	11.8	8.2	N/A

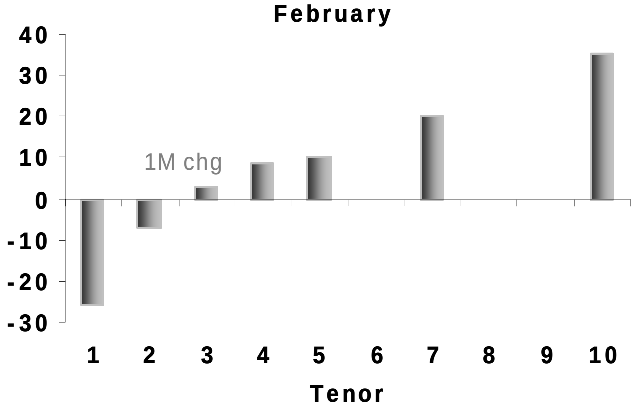
Sources: Bloomberg, CEIC

India: FX and Rates Strategy

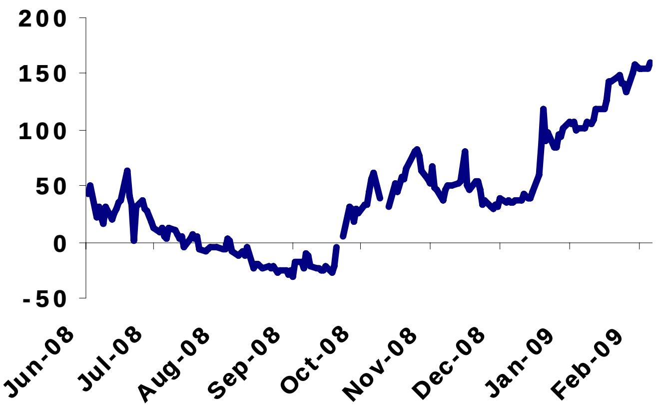
USD-INR buffeted by crosswinds



IRS curve bear-steepened in February



2s-10s IRS to steepen further



Portfolio outflows have slowed and India's trade deficit continues to improve, reducing pressure on the INR. However, India's investment grade status is in jeopardy as a result of its deteriorating fiscal position, and global risk aversion has spiked once again. On balance, such cross-winds should keep USD-INR range-bound until a new government takes the helm after elections in May.

FX

USD-INR faces cross-winds which should keep the pair range-bound above the 50-threshold over the near-term. On the one hand, India's sovereign rating is under pressure due to a deteriorating fiscal position (see below). In addition, there has been a renewed spike in global risk aversion.

Supportive of the INR, however, are improved portfolio flows and a significant narrowing of the trade deficit. Foreign equity outflows were a key driver of rupee weakness in 2008, but outflows have been progressively slowing. Year-to-date, these flows have actually improved by 56%. Also, India's trade deficit has nearly halved, falling to $7.6bn in December compared with $13.9bn in August 2008.

Rates

INR rates markets have come under increased pressure amid news that: 1/ the government will borrow an *additional* INR 450bn this fiscal year, bringing the total to INR 3.6 trln (7% of GDP), 2/ the RBI is using open market auctions to buy government bonds, raising concerns that the next step is full monetization of the government's ballooning debt, and 3/ India's BBB- sovereign rating is vulnerable after a Moody's analyst hinted at such, while S&P officially shifted its outlook from stable to "negative."

Meanwhile, RBI Governor Subbarao has fuelled rate cut hopes, saying there is "certainly room" to cut. Also, WPI inflation has fallen below 4%, well within the RBI's comfort zone of 5%. Ultimately, we expect the RBI cut its policy rate by another 150bps this year. This should bring the bulls back to the Indian rates market, but in the current environment enthusiasm will likely be contained to the front-end of the curve. As such, steepeners would still seem to be the better bet.

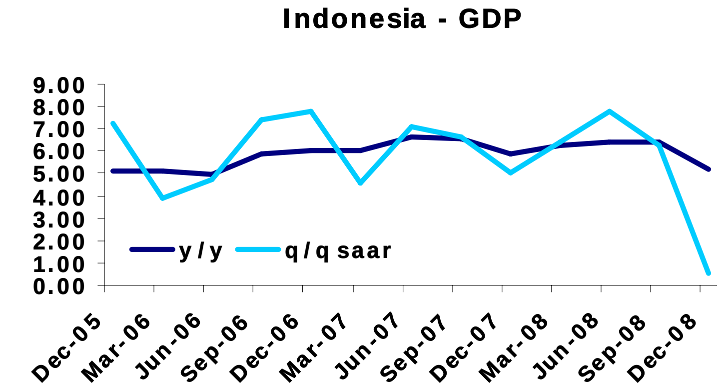
Tamara Henderson

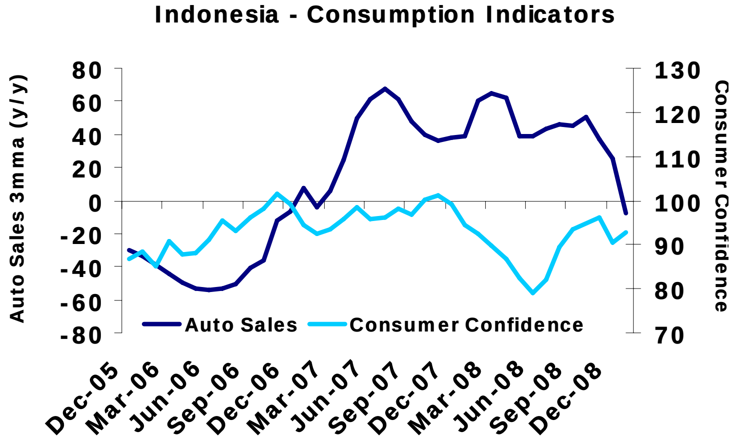
Market Forecasts - India

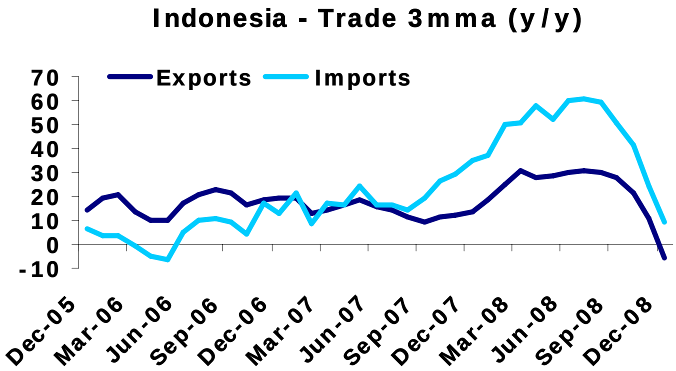
FX	Current	Ytd (%)	Mar-09	Jun-09	Sep-09	Dec-09	Mar-10	Jun-10
USD-INR	51.81	6.2%	52.0	52.0	51.0	51.0	50.0	50.0
AUD-INR	32.92	-3.7%	33	30	29	28	27	28
NZD-INR	25.65	-9.0%	26	23	22	21	21	22
JPY-INR	0.53	-0.6%	0.53	0.52	0.50	0.50	0.48	0.46
EUR-INR	65.28	-4.0%	65	62	57	56	54	55
Rates	**Current**	**Ytd (bps)**	**Mar-09**	**Jun-09**	**Sep-09**	**Dec-09**	**Mar-10**	**Jun-10**
RBI's repo rate	5.50	-100	5.00	4.50	4.00	4.00	4.00	4.50
3-month MIBOR	7.64	-125	7.3	6.8	6.6	6.6	6.7	6.9
2-year IRS (vs NSE MIBOR)	4.11	-34	3.5	3.0	2.8	2.8	3.0	3.1
10-year IRS	5.71	89	5.7	5.8	5.9	6.0	6.1	6.2

Sources: ANZ and Bloomberg

Country Update: Indonesia







Growth stalled in Q4. While Indonesia is one of the least trade-exposed countries in the region and has strong consumption momentum to boot, it too has been caught in the global slowdown and faces tough challenges ahead.

- GDP growth slowed to 5.2% (y/y) in Q4 from 6.4% in Q3. However, the q/q seasonally adjusted annual rate dropped to 0.5% from 6.2% previously. The implication is that Indonesia is not too far from facing a technical recession.
- Private consumption growth eased to 4.8% (y/y) in Q4, compared with 5.3% in Q3. Investment spending slowed to 9.1% (y/y) from 12.2% previously as risk aversion rose with the spreading of the global financial crisis.
- Export growth slipped to 1.8% in Q4 from 10.6% in Q3. However, imports fell by an even larger amount, declining 3.5% in Q4 following growth of 11.0% previously.
- The prognosis for domestic demand remains negative. While the consumer confidence index rose to 92.8 in Jan, it remains in pessimistic territory. Auto sales showed a steep decline of 23.5% (y/y) in Jan, compared with growth of 1.2% in Dec.
- Inflation fell to 9.2% (y/y) in Jan from 11.1% in Dec. This was due to a decline in transportation prices as the government enacted another fuel price cut as world oil prices spiralled lower.
- Bank Indonesia lowered its benchmark interest rate by 50bps to 8.25% in Feb, for a cumulative 125bps of cuts since Dec. With inflation pressures falling rapidly and global growth prospects further deteriorating, BI has scope to reduce rates further.
- As Indonesia prepares to enter an election cycle, government expenditure will likely pick up strongly, supportive of domestic demand. Downside political risk should to be limited.

Chang Wei Liang

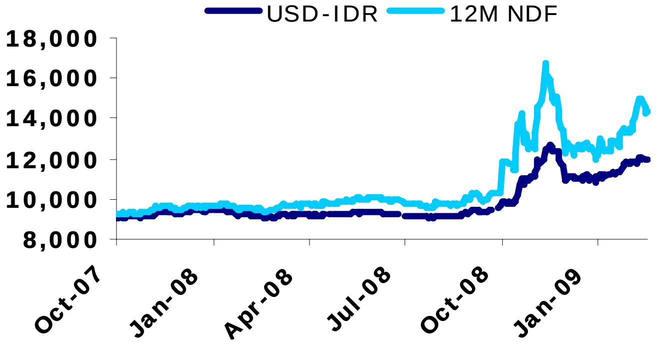
Economic Data - Indonesia

Monthly data	Jun-08	Jul-08	Aug-08	Sep-08	Oct-08	Nov-08	Dec-08	Jan-09
Industrial Production, % y/y	2.4	2.8	2.9	-0.8	6.2	1.0	-2.8	N/A
Retail Sales Index, % y/y	7.4	6.5	13.7	3.2	-15.5	-26.3	-5.4	N/A
Consumer Price Index, % y/y	11.0	11.9	11.8	11.9	11.6	11.5	11.1	9.2
Exports, % y/y	34.1	24.8	29.9	29.0	4.7	-1.8	-20.6	N/A
Imports, % y/y	63.4	68.8	45.4	38.5	40.3	-5.6	-8.0	N/A
Trade Balance, US$ bn	3.0	1.8	2.4	2.9	2.0	2.5	2.4	N/A
Foreign Exchange Reserves, US$ bn	56.8	58.0	55.9	54.6	48.4	47.8	49.2	48.3
Quarterly data	**Mar-07**	**Jun-07**	**Sep-07**	**Dec-07**	**Mar-08**	**Jun-08**	**Sep-08**	**Dec-08**
Real GDP, % y/y	6.0	6.6	6.6	5.8	6.2	6.4	6.4	5.2
-Private consumption	4.7	4.7	5.1	5.5	5.7	5.5	5.3	4.8
-Government consumption	3.7	3.8	6.5	2.0	3.6	5.3	14.1	16.4
-Gross fixed capital expenditure	7.6	7.6	9.7	12.4	13.7	12.0	12.2	9.1
Nominal GDP, IDR tn	918.9	964.8	1,030.8	1,034.9	1,117.6	1,229.6	1,332.5	1,274.3
Current Account, US$ bn	2.6	2.2	2.1	3.4	2.6	-1.2	-0.6	N/A
Capital & Financial Account, US$ bn	1.8	2.0	-1.0	0.7	-1.6	2.6	0.5	N/A

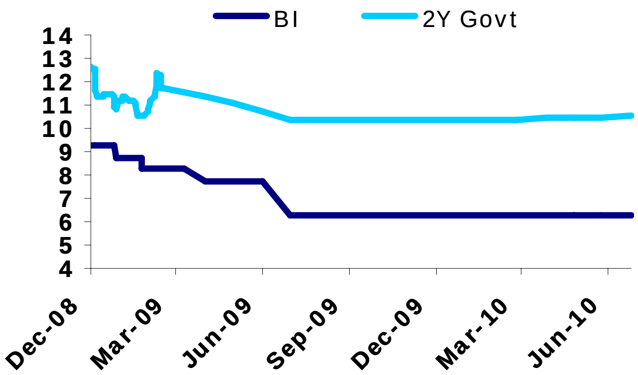
Sources: Bloomberg, CEIC

Indonesia: FX and Rates Strategy

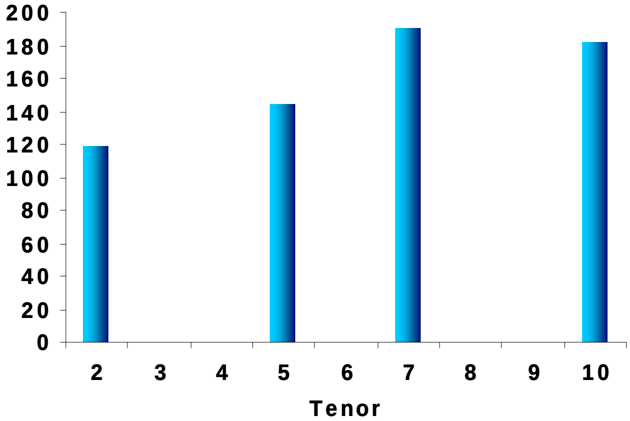
Foreigners remain pessimistic



BI has more rate cuts in the pipeline



Bonds Spooked by Supply Worries & Risk Aversion in February (bps)



Foreigners remain pessimistic about the IDR, even though the authorities have said that all means will be used to ensure currency stability. Upgraded swap arrangements and the approach of elections will provide added ability and willingness for authorities to cap more aggressively any further outsized advances in USD-IDR.

FX

USD-IDR is back up in the 12,000 area, boosted in part by general risk aversion associated with worries about a more prolonged global slump. Meanwhile, the 12-month NDF is trading above 14,000, implying a further 20% depreciation in the rupiah—which seems a bit dire.

Indonesia's FX reserves have fallen by 16% during the July-January period to $50.9bn. This is still a healthy 8 months of import cover (not to mention that the trade balance is also in surplus), but markets are more concerned about the trend than the level. Probably by no coincidence BI Governor Boediono has said subsequently that the bank would intervene to "reduce volatility" but not "go against the flow." Still, volatility in the current environment has tended to flow in one direction, which keeps BI on the other side, providing USD liquidity to the market.

At the same time, BI has said it will resort to additional ammunition to stem currency volatility if necessary. In this vein, Indonesia has proposed a currency swap arrangement with the US to help support the IDR, and is in talks to expand an existing $6bn currency swap arrangement with Japan. Indonesia already has similar arrangements with China and Korea for $3bn each.

In addition, Spring elections are approaching, and inflation at 9.2% (although falling) still remains high enough for the BI to continue to flag it as a concern. All together, the authorities have increased ability and willingness to keep a tight reign on the IDR.

Rates

Although spooked by supply worries and risk aversion (vis a vis EM debt) in February, we remain bullish on IDR rates in 2009. BI has more rate cuts in the pipeline, the government is in a better financing position, and IDR bonds offer good value and attractive yields.

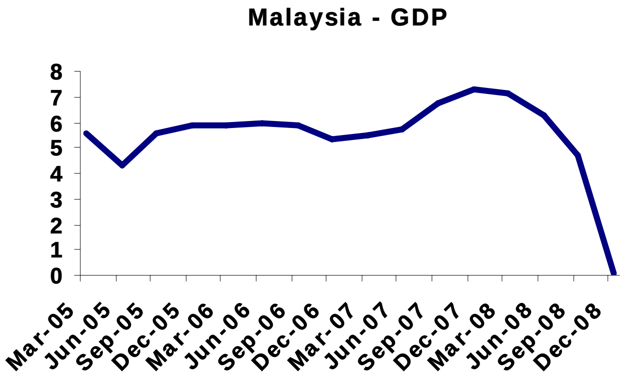
Tamara Henderson

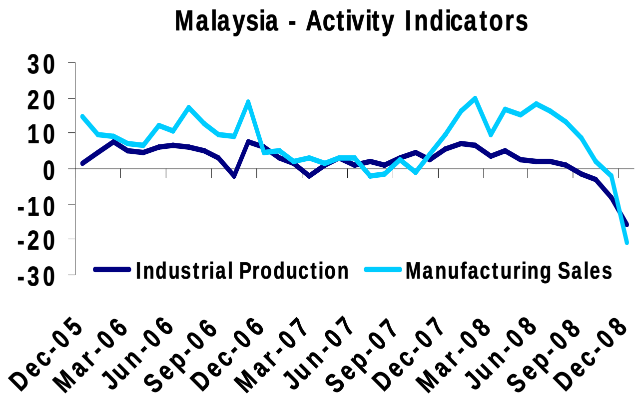
Market Forecasts - Indonesia

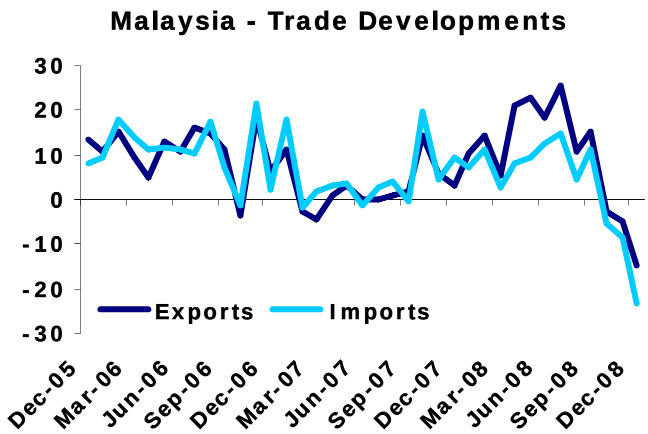
FX	Current	Ytd (%)	Mar-09	Jun-09	Sep-09	Dec-09	Mar-10	Jun-10
USD-IDR	12,000	7.9%	12,000	12,000	11,900	11,600	11,600	11,300
AUD-IDR	7,829	-1.6%	7,600	7,000	6,700	6,300	6,300	6,300
NZD-IDR	6,193	-5.6%	6,000	5,400	5,100	4,800	4,900	4,900
JPY-IDR	124	-0.9%	120	120	120	110	110	100
EUR-IDR	15,415	-2.6%	15,000	14,400	13,300	12,800	12,500	12,400
Rates	**Current**	**Ytd (bps)**	**Mar-09**	**Jun-09**	**Sep-09**	**Dec-09**	**Mar-10**	**Jun-10**
BI's bank rate	8.25	-100	7.75	6.75	6.00	6.00	6.00	6.00
3-month JIBOR	9.89	-225	9.7	8.7	8.0	8.0	8.0	8.1
2-year IRS (versus IDR fix)	16.75	275	16.5	15.8	15.4	15.4	15.5	15.6
10-year IRS	11.50	200	11.4	11.2	11.0	11.0	11.1	11.1

Sources: ANZ and Bloomberg

Country Update: Malaysia







The Malaysian economy expanded at the slowest pace in seven years in Q4. With leading indicators looking weak, Bank Negara cut its overnight rate. Aside from economic woes, there are concerns about political stability.

- GDP growth came in well below expectations as the economy grew by a mere 0.1% (y/y) in Q4, down from 4.7% in Q3.
- Consumption plunged with vehicle sales contracting further to 17.5% (y/y) in Jan from 5.7% in Dec. Manufacturing sales also fell by 20.8% in Dec after contracting 1.9% in Nov due to dismal performance in refined petroleum products and semi-conductors.
- Industrial production fell 15.5% (y/y) in Dec, continuing the downward trend from 8.2% in Nov. This reflected decreases in manufacturing, electrical and mining activity.
- Exports continued their downward spiral, contracting by 14.9% (y/y) in Dec from a fall of 4.9% in Nov. Shipments of mineral fuel, crude, electrical and chemical exports decreased the most. Imports also fell in Dec, declining 23.1%.
- CPI inflation slowed to 3.9% (y/y) in Jan from 4.4% in Dec. Cheaper fuel pushed transportation costs down.
- BNM reneged on its earlier comments in Feb by cutting interest rates. The overnight rate was lowered by 50bps to 2.00%, underlining concerns about economic growth.
- The political outlook seems somewhat less stable with scandals, party defections and stand-offs in several states ahead of an impending political handover of the Prime Minster's post to Datuk Najib, who faces party elections.
- We expect the effects of an anticipated "bigger and more comprehensive" second stimulus package to be modest as exports continue to tumble and commodity prices remain weak.

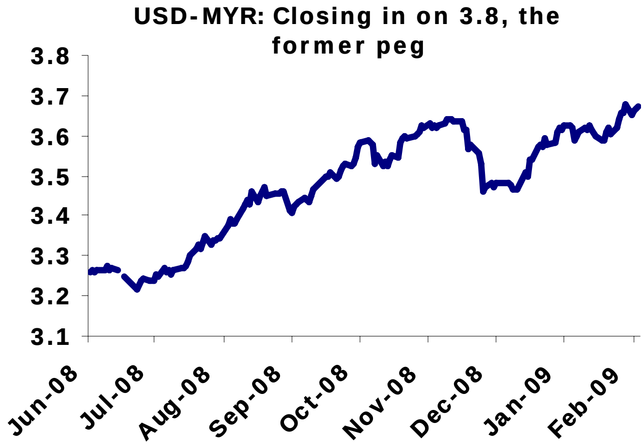
Naresh Navaratnarajah

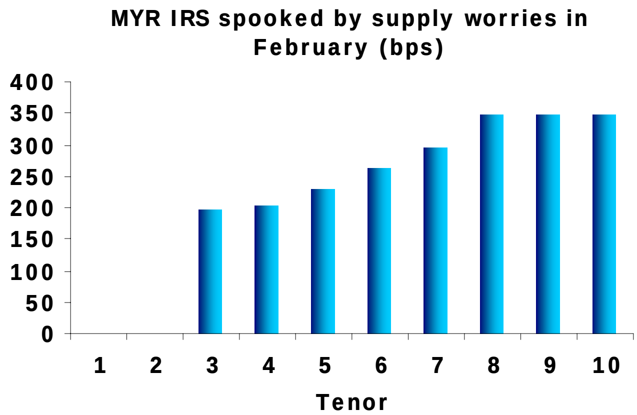
Economic Data - Malaysia

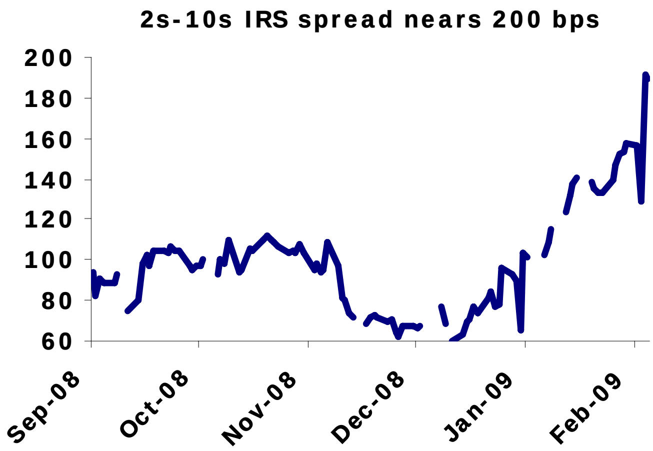
Monthly data	Jun-08	Jul-08	Aug-08	Sep-08	Oct-08	Nov-08	Dec-08	Jan-09
Industrial Production, % y/y	2.3	2.4	1.2	-1.7	-2.8	-8.2	-15.5	N/A
Manufacturing Sales, % y/y	18.1	16.2	13.4	8.6	2.1	-1.9	-20.8	N/A
Consumer Price Index, % y/y	7.7	8.5	8.5	8.2	7.6	5.7	4.4	3.9
Exports, % y/y	18.6	25.3	10.7	15.0	-2.6	-4.9	-14.9	N/A
Imports, % y/y	12.5	15.0	4.4	11.4	-5.3	-8.6	-23.1	N/A
Trade Balance, USD bn	3.9	4.4	3.7	4.3	2.7	3.2	3.4	N/A
Foreign Exchange Reserves, US$ bn	120.0	119.3	116.9	104.5	94.9	92.1	85.7	85.9
Quarterly data	**Mar-07**	**Jun-07**	**Sep-07**	**Dec-07**	**Mar-08**	**Jun-08**	**Sep-08**	**Dec-08**
Retail Sales, % y/y	25.3	33.0	39.7	35.7	19.8	23.8	25.4	16.5
Real GDP, % y/y	5.5	5.7	6.7	7.3	7.4	6.7	4.7	0.1
-Private consumption	7.6	12.3	13.0	10.2	11.7	9.0	8.1	5.3
-Government consumption	7.3	10.4	6.0	4.2	14.7	10.9	6.9	13.8
-Gross fixed capital formation	9.5	6.0	12.8	10.2	6.0	5.6	3.1	-10.2
Nominal GDP, MYR bn	144.6	154.3	166.3	176.7	175.4	189.4	198.7	177.3
Current Account, US$ bn	5.7	7.3	8.6	8.0	7.5	11.3	11.2	N/A
Capital & Financial Account, US$ bn	0.8	2.2	-9.0	-5.2	8.3	-3.8	-17.8	N/A

Sources: Bloomberg, CEIC

Malaysia: FX and Rates Strategy







USD-MYR is quickly closing the gap with the 3.80 level—the former level of the peg and also our targeted peak in 2009. Exports fell nearly 15% (y/y) in December, and indications from data in the rest of the region suggest much worse in Q1. Meanwhile, risk aversion picked up in February as markets fretted about a more prolonged slump in the global economy.

FX

The MYR was an out-performer in 2008, shedding just 4.7% against the USD compared with an average loss of 10.5% within AXJ. This has changed in 2009, with the MYR now among the under-performers—having lost 6% already. As exports have started to plummet in the region in a staggering fashion, FX markets have started to focus more on the currencies of countries with large export exposures.

Over 100% of Malaysia's GDP is exposed to exports and, as has occurred across AXJ, exports have started to contract at an accelerating pace (-14.9% in December compared with -4.9% in November). The figures for January should be much worse, judging by performance elsewhere in the region. Although imports are dropping even faster and Malaysia's trade surplus is rising, the knock-on effects from the slump in global demand are starting to filter through the local economy.

The authorities are responding with fiscal stimulus, cuts in interest rates and the reserve requirement, and a tolerance for larger advances in USD-MYR in order to support economic growth and to maintain competitiveness within the region. We continue to target a peak of 3.80—the former level of the peg.

Rates

Bank Negara has cut the OPR by an uncharacteristically aggressive cumulative 125bps to 2.0% this year, including an unexpected 50bps cut in February. However, the rates market failed to rally as supply worries predominated. Details of a "mini" budget are due on March 10, keeping supply in focus near-term.

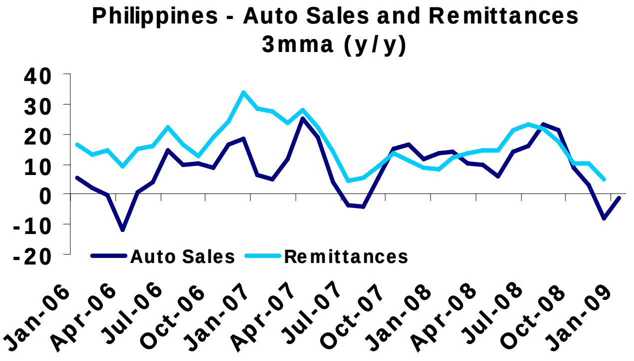
Tamara Henderson

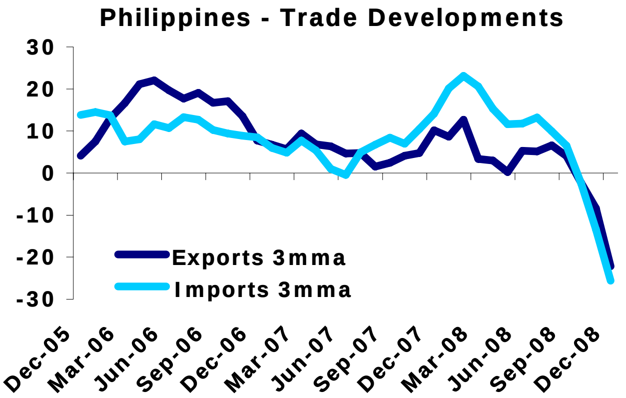
Market Forecasts - Malaysia

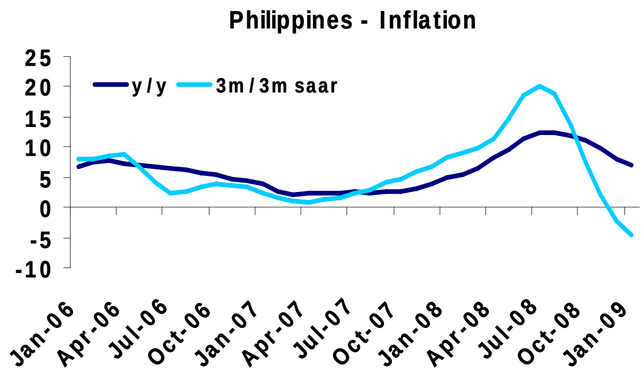
FX	Current	Ytd (%)	Mar-09	Jun-09	Sep-09	Dec-09	Mar-10	Jun-10
USD-MYR	3.67	6.0%	3.64	3.74	3.80	3.80	3.80	3.75
AUD-MYR	2.39	-1.6%	2.3	2.2	2.1	2.1	2.1	2.1
NZD-MYR	1.88	-6.2%	1.8	1.7	1.6	1.6	1.6	1.6
JPY-MYR	3.88	-7.3%	3.7	3.7	3.8	3.7	3.6	3.5
EUR-MYR	4.68	-3.0%	4.6	4.5	4.3	4.2	4.1	4.1
Rates	**Current**	**Ytd (bps)**	**Mar-09**	**Jun-09**	**Sep-09**	**Dec-09**	**Mar-10**	**Jun-10**
BNM's overnight policy rate	2.00	-125	2.00	1.50	1.50	1.50	1.50	1.50
3-month KLIBOR	2.13	-124	1.9	1.6	1.6	1.6	1.8	1.9
2-year IRS (vs 3M KLIBOR)	2.04	-78	1.8	1.5	1.5	1.5	1.7	1.8
10-year IRS	3.93	43	3.8	3.8	3.8	3.8	3.8	3.9

Sources: ANZ and Bloomberg

Country Update: Philippines







The Philippine economy is one of few in Asia that has not seen a marked deterioration. Growth should remain well-supported with robust domestic demand and muted declines in net exports. The key concern is whether remittances will fall given difficulties in key host countries.

- Domestic demand is holding up well, with passenger car sales rebounding to 14.2% (y/y) growth in Jan from a 19.5% decline in the previous month.
- Exports fell 40.3% (y/y) in Dec as shipments of electronics and manufacturing fell by 35% and 27%, respectively on a m/m basis. Imports have also deteriorated sharply, falling by 34.2% in Dec. Nevertheless, the trade balance still posted a deficit of $620mn for the month.
- Overseas remittances slowed to a trickle at 0.8% (y/y) in Dec, down from 10.5% in Nov. Demand for labour in key overseas markets such as the US and Middle East is slowing and the Philippine labour department estimated that over 5,400 overseas Filipino workers have been displaced due to the global economic crisis. Going forward, it is likely that remittances may contract as a result of increased job losses.
- The quarterly business confidence index rose to -6.80 in Q4 from -12.90 in Q3. However, a negative reading still reflects a pessimistic mood among businesses.
- Inflationary pressures have receded, with the Jan reading dropping to 7.1% (y/y) from 8.0% previously. On the month, inflation was essentially flat at 0.3%. Core inflation is also abating, falling to 6.9% in Jan from 7.3% in Dec.
- In light of the need to increase fiscal spending to support growth, the government approved a larger budget deficit target for 2009, allowing the shortfall to widen to as much as 2% of GDP.
- The Philippines could well out-perform the region in terms of economic growth if the momentum in domestic consumption can be maintained.

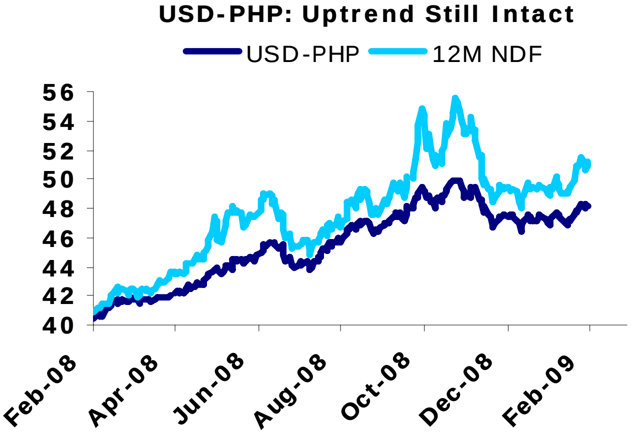
Chang Wei Liang

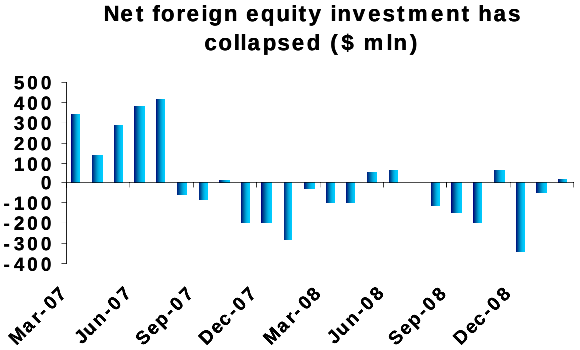
Economic Data - Philippines

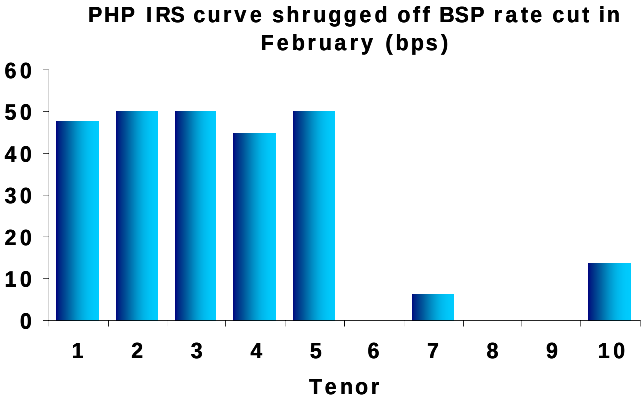
Monthly data	Jun-08	Jul-08	Aug-08	Sep-08	Oct-08	Nov-08	Dec-08	Jan-09
Manufacturing Production Value-add, % y/y	7.5	10.4	6.3	13.0	8.7	0.1	-9.7	N/A
Passenger Car Sales, % y/y	17.4	31.0	20.6	12.3	-5.9	2.0	-19.5	14.2
Consumer Price Index, % y/y	11.4	12.3	12.4	11.8	11.2	9.9	8.0	7.1
Exports, % y/y	8.8	4.4	6.6	1.1	-14.8	-11.4	-40.3	N/A
Imports, % y/y	12.7	16.0	1.1	2.5	-11.1	-31.5	-34.2	N/A
Trade Balance, US$ bn	-0.8	-1.4	-0.6	-0.4	-0.6	0.0	-0.6	N/A
Foreign Exchange Reserves, US$ bn	32.1	32.4	32.5	32.3	31.8	32.4	32.6	34.1
Quarterly data	**Mar-07**	**Jun-07**	**Sep-07**	**Dec-07**	**Mar-08**	**Jun-08**	**Sep-08**	**Dec-08**
Real GDP, % y/y	7.0	8.3	7.1	6.4	4.7	4.4	5.0	4.5
-Private consumption	5.9	5.6	5.7	6.2	5.2	4.1	4.4	4.5
-Government consumption	9.5	11.9	6.4	4.6	1.9	-1.5	13.4	4.7
-Gross fixed capital formation	10.3	20.9	8.8	6.7	2.9	3.0	7.0	1.9
Nominal GDP, peso bn	1,524.1	1,618.6	1,613.8	1,891.8	1,668.0	1,837.9	1,864.9	2,126.8
Current Account, US$ bn	1.9	1.7	1.0	1.7	0.9	0.8	-0.5	N/A
Capital & Financial Account, US$ bn	0.5	-0.4	3.3	-0.5	0.7	0.5	0.5	N/A

Sources: Bloomberg, CEIC

Philippines: FX and Rates Strategy







Beneficial effects from remittances and seasonal portfolio flows are expected to give way to the realities of global recession and continued risk aversion in the months ahead—pushing USD-PHP back toward the 50.0 level.

FX

The Philippine peso has been an out-performer within AXJ this year—thus far defying gravitational pulls from elevated risk aversion, plunging exports and limited fiscal ammunition to maintain momentum in domestic demand.

Net foreign equity outflows have slowed and remittances from overseas workers have held up—providing the peso with a toehold of support. The peso has also benefited from a relatively impressive outturn for Q4 GDP, which slowed a mere ½ ppt to 4.5% (y/y).

Ultimately, we expect enthusiasm for the peso to fade in the coming months, with these sources of temporary support giving way to the realities of the global recession and continued risk aversion.

Rates

Inflation remains in a downtrend, providing further scope for the BSP to cut interest rates, but worries about supply and elevated risk aversion (vis a vis EM debt) have pushed PHP IRS rates up as much as 50bps in February.

The government expects its budget deficit to more than double to PHP 177bn (2.2% of GDP) compared with a shortfall of PHP 68bn in 2008—as it spends more to insulate the domestic economy from the global recession.

There is not much duration in the PHP curve, so issuance at the longer tenors would be welcome—ultimately supportive of trading in the secondary markets. Near-term, however, supply pressures are likely to continue to dominate any beneficial effects from BSP rate cuts.

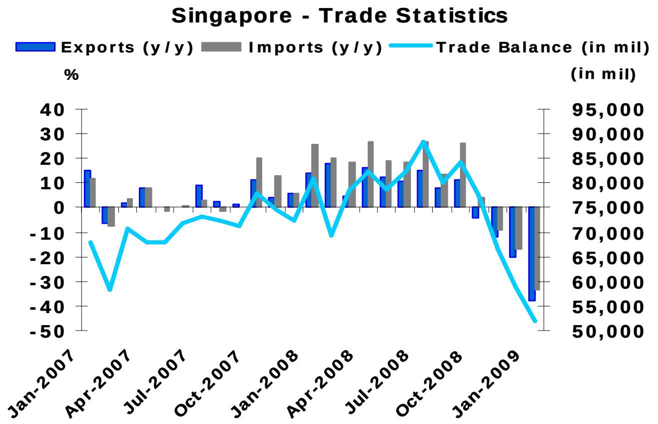
Tamara Henderson

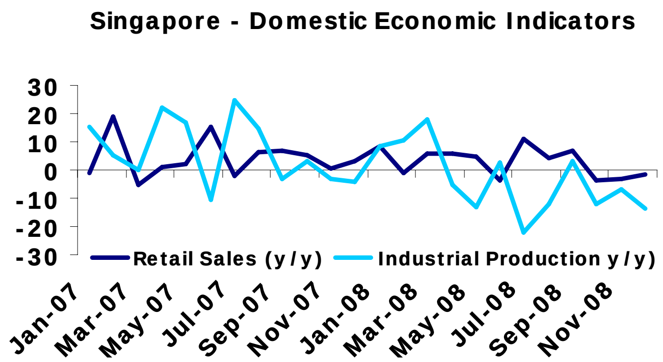
Market Forecasts - Philippines

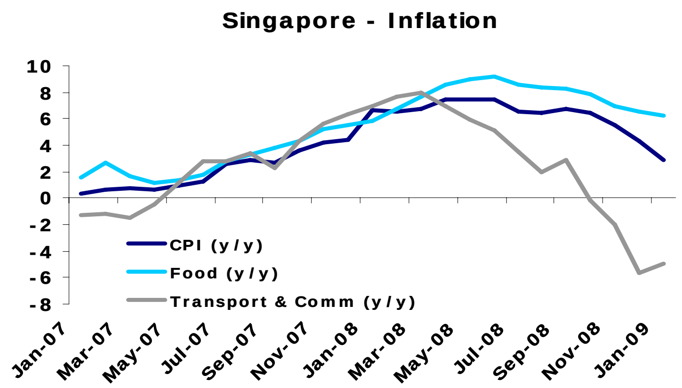
FX	Current	Ytd (%)	Mar-09	Jun-09	Sep-09	Dec-09	Mar-10	Jun-10
USD-PHP	48.21	1.4%	48.5	49.5	50.0	49.5	48.8	48.5
AUD-PHP	31.15	-6.5%	30.6	28.7	28.0	26.7	26.4	27.2
NZD-PHP	24.52	-10.7%	24.3	22.3	21.5	20.3	20.5	20.9
JPY-PHP	0.49	-5.7%	0.495	0.495	0.495	0.485	0.465	0.449
EUR-PHP	61.19	-7.6%	60.6	59.4	56.0	54.5	52.7	53.4
Rates	**Current**	**Ytd (bps)**	**Mar-09**	**Jun-09**	**Sep-09**	**Dec-09**	**Mar-10**	**Jun-10**
BSP's overnight reverse repo rate	5.00	-50	4.75	4.00	4.00	4.00	4.00	4.00
3-month PHIBOR	5.31	6	5.1	4.3	4.2	4.2	4.2	4.3
2-year IRS (versus 3M IB ref rate)	4.33	25	4.1	3.3	3.2	3.2	3.2	3.3
10-year IRS	5.96	-14	5.9	5.6	5.6	5.6	5.6	5.6

Sources: ANZ and Bloomberg

Country Update: Singapore







With the economy in deep recession, the government announced several stimulatory measures (including a reduction in corporate taxes). Exports declined sharply as deteriorating global economic conditions pared demand for electronics and other goods. Inflation continued to ease as oil prices fell and demand for goods and services remained weak.

- Non-oil domestic exports dropped 34.8% (y/y) in Jan after contracting 20.8% in Dec as the deepening global recession pared demand for electronics and other goods. Shipments for electronics plunged 38.4%, while non-electronic goods, including petrochemicals and pharmaceuticals, fell 32.4%.
- The government announced that the economy may shrink by as much as 5% in 2009, revising the lower bound of its growth forecast range from -2%. Amid the deepening slump, the government is cutting corporate taxes and increasing spending.
- Inflation continued to ease, falling to 2.9% (y/y) in Jan from 4.3% in Dec. Oil prices fell and a deepening economic slump hurt demand for goods and services. Food prices rose by 6.2% (y/y) while transport & communication costs fell by 5% as gasoline and automobile prices declined. The government expects consumer prices to hold steady or fall marginally in 2009.
- Tourist arrivals fell 1.6% to 10.1 million in 2008. The Singapore Tourism Board expects tourist arrivals in 2009 to decline sharply by 11% and plans to spend S$90 mn in promotional campaigns to attract more visitors.
- The stock market remained volatile, with the STI index falling by 6% in Feb 2009. Both consumer and business sentiment will remain weak in 2009 amid rising unemployment and deteriorating asset prices.
- Conditions in 2009 will be poor for Singapore's open economy. With both foreign and domestic demand weak, we expect GDP to fall by around 3%.

Ivy Tan

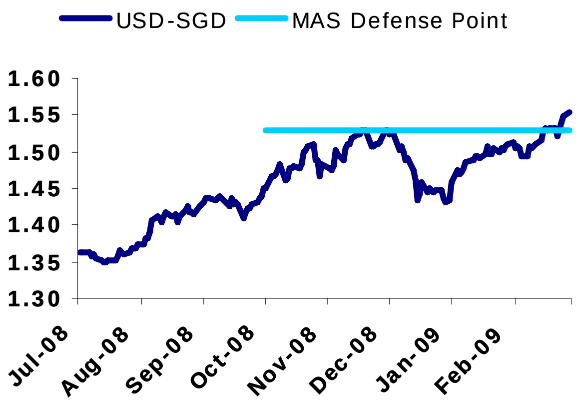
Economic Data - Singapore

Monthly data	Jun-08	Jul-08	Aug-08	Sep-08	Oct-08	Nov-08	Dec-08	Jan-09
Industrial Production, % y/y	2.3	-22.0	-11.9	3.1	-12.2	-6.6	-12.8	-29.1
Retail Sales, % y/y	-3.6	11.3	4.0	7.0	-3.5	-3.3	-1.6	N/A
Consumer Price Index, % y/y	7.5	6.5	6.4	6.7	6.4	5.5	4.3	2.9
Domestic Exports (Non-oil), % y/y	-10.6	-5.8	-13.9	-5.7	-15.5	-17.5	-20.8	-34.8
Imports (Non-oil), % y/y	3.1	4.3	0.1	12.6	-2.2	-12.4	-14.0	-29.0
Trade Balance, US$ bn	1.4	1.5	2.6	1.5	0.4	1.0	0.7	0.5
Foreign Exchange Reserves, US$ bn	175.3	175.6	171.5	169.1	162.5	165.8	168.9	169.2
Quarterly data	**Mar-07**	**Jun-07**	**Sep-07**	**Dec-07**	**Mar-08**	**Jun-08**	**Sep-08**	**Dec-08**
Real GDP, % y/y	7.6	8.6	9.5	5.5	6.7	2.5	0.0	-4.2
-Private consumption	2.7	5.8	6.3	5.8	4.1	4.4	2.7	-1.2
-Government consumption	-1.6	3.4	-0.6	9.5	10.4	9.0	9.9	2.7
-Gross fixed capital formation	19.7	25.7	15.4	17.0	30.5	25.0	14.9	-9.9
Nominal GDP sa, SGD bn	59.2	61.8	64.2	66.5	66.0	64.3	64.5	62.8
Current Account, US$ bn	11.5	9.8	11.5	6.3	8.1	6.7	7.7	4.5
Capital & Financial Account, US$ bn	-11.9	-3.1	-8.0	0.7	2.0	-3.8	-8.6	-1.1

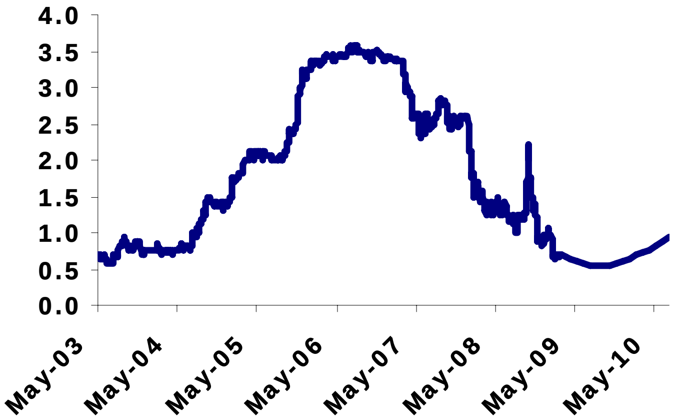
Sources: Bloomberg, CEIC

Singapore: FX and Rates Strategy

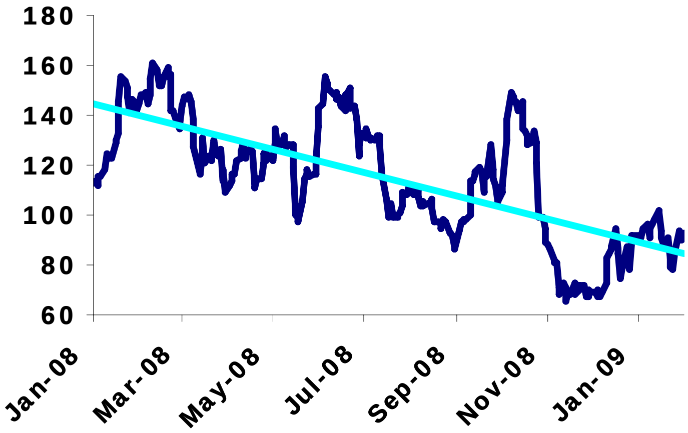
USD-SGD closing the gap with 1.6



3M SIBOR to trough near 0.55%



2s-10s IRS spread yet to break trend



The MAS is expected to re-centre and widen its S$NEER policy band at its next regular meeting in April, paving the way for further gains in USD-SGD. Our target for the peak in USD-SGD in 2009 continues to be in the 1.66 area.

FX

The MAS indicated in January that there would be no inter-meeting discussion of its S$NEER policy, leaving any adjustments to the April meeting. Meanwhile, the 1.53 level in USD-SGD—a former intervention point for the MAS—has been broken in the wake of alarming GDP results and heightened volatility in equity markets.

Singapore's GDP contracted by 4.2% (y/y) in Q4, the worst performance in at least 33 years, and non-oil domestic exports fell by 34.8% in January, the biggest drop on record. Government authorities expect continued weak performance in 2009 (somewhere between -2% and -5% versus growth of 1.1% in 2008). With the effects of the global recession now hitting the local economy with full force, we expect the authorities to allow USD-SGD to play a bit of catch-up with the currencies within AXJ.

As such, in early April we expect the MAS to announce a re-centring and widening of its S$NEER policy band, paving the way for USD-SGD to progress significantly higher. No change in the slope of the band (currently zero percent) is anticipated unless the downward momentum in the global economy fails to ebb—something we will not have a handle on until the middle of this year. Notably, the MAS maintained a zero percent appreciation path in its policy band during the downturn in 2001, when GDP contracted by 2.2%.

As of writing, the entire forward curve (both onshore and offshore) appears to be priced for unchanged MAS policy all year. This presents a significant opportunity for those not already in long USD-SGD positions.

Rates

We continue to target 0.56% in 3-month SGD SIBOR, which was the low during the 2001/03 downturn. Singapore's fiscal stimulus plans have had limited impact on 2s-10s (GOV and IRS), as the country's ample reserves will be tapped to finance much of the spending increase.

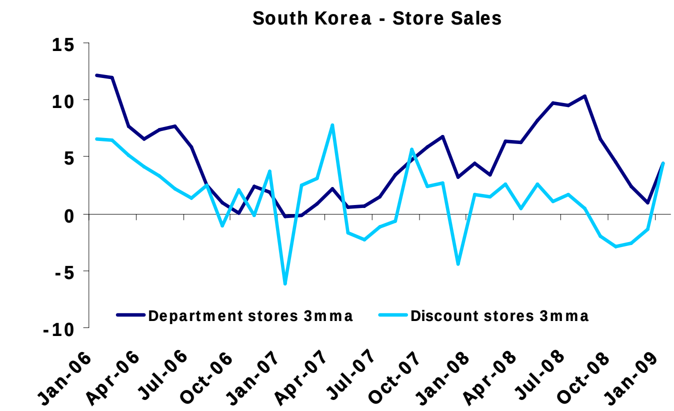
Tamara Henderson

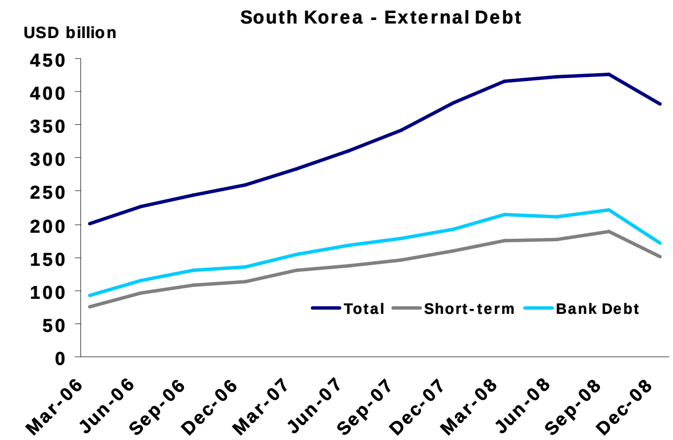
Market Forecasts - Singapore

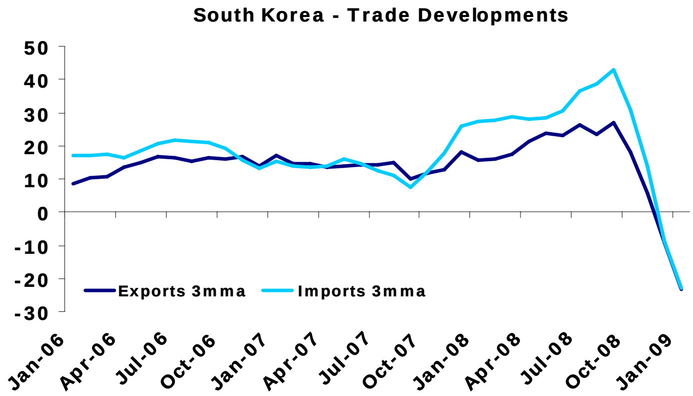
FX	Current	Ytd (%)	Mar-09	Jun-09	Sep-09	Dec-09	Mar-10	Jun-10
USD-SGD	1.535	7.3%	1.54	1.58	1.62	1.66	1.66	1.63
AUD-SGD	0.993	-1.2%	0.97	0.92	0.91	0.90	0.90	0.91
NZD-SGD	0.782	-5.7%	0.77	0.71	0.70	0.68	0.70	0.70
JPY-SGD	1.568	-0.5%	1.57	1.58	1.60	1.63	1.58	1.51
EUR-SGD	1.951	-2.4%	1.93	1.90	1.81	1.83	1.79	1.79
Rates	**Current**	**Ytd (bps)**	**Mar-09**	**Jun-09**	**Sep-09**	**Dec-09**	**Mar-10**	**Jun-10**
3-month SIBOR	0.70	-26	0.65	0.55	0.55	0.65	0.75	0.95
2-year IRS (onshore vs 6M SOR)	1.64	7	1.6	1.5	1.4	1.4	1.5	1.7
10-year IRS	2.57	30	2.6	2.5	2.4	2.4	2.5	2.5

Sources: ANZ and Bloomberg

Country Update: South Korea







Momentum still looks weak although Lunar New Year spending surprised on the upside. Export and import growth have collapsed. Banks are aggressively paying down external debt (which remains high) and fears of a "March crisis" are overblown.

- Domestic demand indicators are mixed. Consumption indicators unexpectedly improved in Jan as spending picked up over the Lunar New Year holiday. However, industrial production fell by 18.6% (y/y) in Dec and by 9.7% in the following month.
- Exports and imports both fell by over 30% (y/y) in Jan, but the trade balance deteriorated sharply to a deficit of almost $3bn. Shipments to Europe fell by 45%, twice the rate of the decline to the US. Automobile exports fell by a staggering 64%.
- CPI inflation slowed to 3.7% (y/y) in Jan, a 11-month low. Food prices continued to rise while transportation costs fell. Producer price inflation declined 1ppt to 4.7%.
- External debt fell by 10% in Q4 to $380.5bn. The bulk of the decline was short-term bank debt, reflecting aggressive use of the BOK's USD liquidity facility.
- For the second straight month, the BOK cut its policy rate by 50bps. The base rate stands at 2.00%, down from 5.25% in October. Both the government and rating agencies say that the planned stimulus will not damage the country's fiscal position, among the strongest in Asia.
- The government's leading indicator continues to deteriorate, suggesting a weakening of conditions going forward. The coincident indicator continues to fall rapidly as well.
- We continue to forecast a decline in GDP of around 3% this year, although by the final quarter growth may turn positive. Despite some improvement in the consumption indicators, it is too early to declare a rebound. Fears of a "March crisis" related to bank debt owed to Japanese creditors are misplaced.

Paul Gruenwald

Economic Data - South Korea

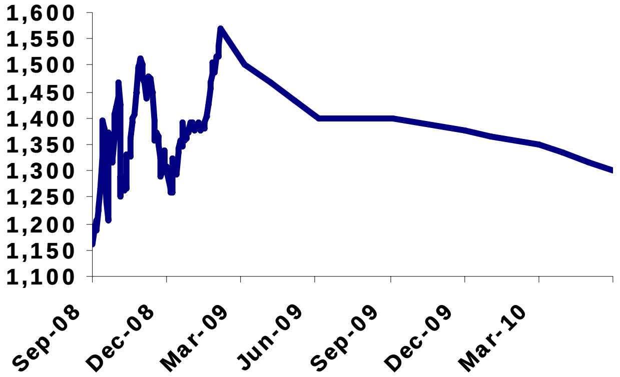
Monthly data	Jun-08	Jul-08	Aug-08	Sep-08	Oct-08	Nov-08	Dec-08	Jan-09
Industrial Production, % y/y	6.6	8.7	1.9	6.1	-2.3	-14.0	-18.6	-9.7
Retail Sales, % y/y	6.8	12.3	10.4	4.7	1.5	-1.0	-1.2	N/A
Consumer Price Index, % y/y	5.5	5.9	5.6	5.1	4.8	4.5	4.1	3.7
Exports, % y/y	16.4	35.6	18.1	27.6	7.8	-19.5	-17.9	-33.8
Imports, % y/y	32.7	47.0	36.4	45.4	10.3	-15.0	-21.6	-31.9
Trade Balance, USD bn	-0.6	-2.0	-3.8	-2.1	1.0	0.0	0.5	-3.4
Foreign Exchange Reserves, US$ bn	258.5	247.9	243.4	240.4	212.8	201.0	201.0	201.6

Quarterly data	Mar-07	Jun-07	Sep-07	Dec-07	Mar-08	Jun-08	Sep-08	Dec-08
Real GDP, % y/y	4.0	4.9	5.1	5.7	5.8	4.8	3.8	-3.4
-Private consumption	4.1	4.4	4.8	4.6	3.4	2.3	1.1	-4.4
-Government consumption	6.3	6.9	4.5	5.6	3.9	4.0	4.4	4.9
-Gross fixed capital formation	7.2	5.5	1.3	2.9	0.5	0.1	1.4	-8.4
Nominal GDP, KRW tn	204.8	221.6	226.9	247.9	218.7	241.1	242.6	N/A
Current Account, US$ bn	-1.9	1.1	2.0	-0.8	-0.1	1.8	-1.3	0.9
Capital & Financial Account, US$ bn	4.7	-0.3	-3.9	0.3	0.4	-3.6	-4.4	-4.8

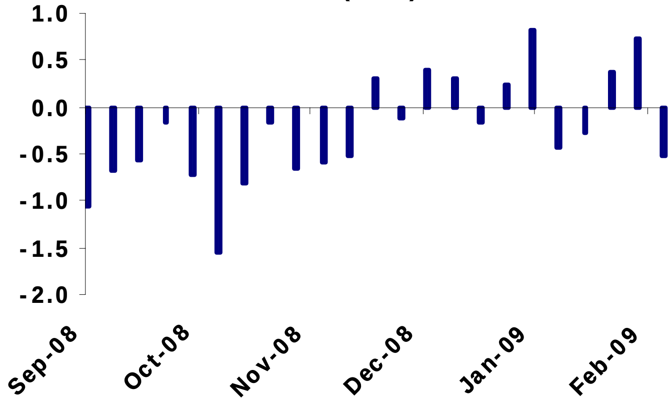
Source: Bloomberg, CEIC

South Korea: FX and Rates Strategy

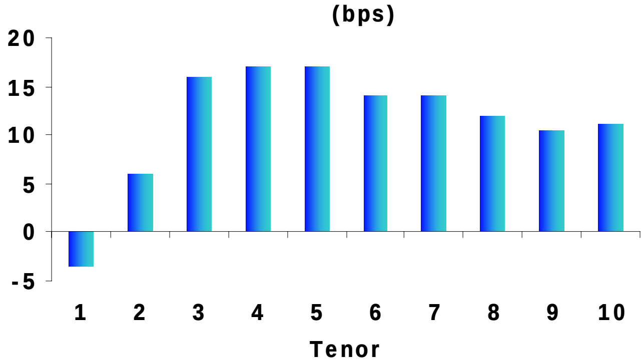
1,600 is opportunity to ride USD-KRW lower



Net Foreign Equity Flows Improving ($ bn)



KRW IRS shrug off BoK cut in February (bps)



USD-KRW continues to lead USD-AXJ higher amid another acute bout of global risk aversion. Although timing is tricky, ultimately we expect USD-KRW to lead USD-AXJ lower later this year. As such, the current rally in USD-KRW should be viewed as offering attractive levels for the ride down, particularly after March.

FX

US equities have broken below key support relatively easily and in tandem USD-AXJ has pushed ever higher, paced by USD-KRW which is preparing an assault on the 1,600 level. Risk aversion and March debt redemptions remain a hurdle over the near-term, but ultimately we expect USD-KRW to lead USD-AXJ lower later in the year—just as the pair has led the way higher. As such, we view the current foray toward 1,600 as an opportunity to position for the ride down.

"March crisis" fears are considered to be overdone, and there are a number of factors which will provide traction for the KRW once external debt repayments are out of the way this month. Notably, Korea's external debt burden is shrinking quickly. Also, the current account should swing back into surplus in February—not only are imports contracting more than exports, but also in m/m terms February exports managed to rise, while imports continued to fall.

Meanwhile, foreign investment interest is returning. FDI rose 2% (y/y) in Q4, following a decline of 2% in Q3. Unlike the rest of AXJ, Korea also attracted healthy net foreign equity inflows in December and January ($0.6bn and $0.5bn, respectively). As of end-February, these flows were up nearly 100% (ytd) from a year ago.

Rates

We anticipate another 100bps of cuts before a trough of 1.0% is reached in the BOK's policy rate, offering support for the front-end of the curve. Meanwhile, risk aversion and worries about supply are weighing on the long-end. As such, we continue to favour steepeners—looking for the 2s-10s KRW IRS spread to widen above 100bps.

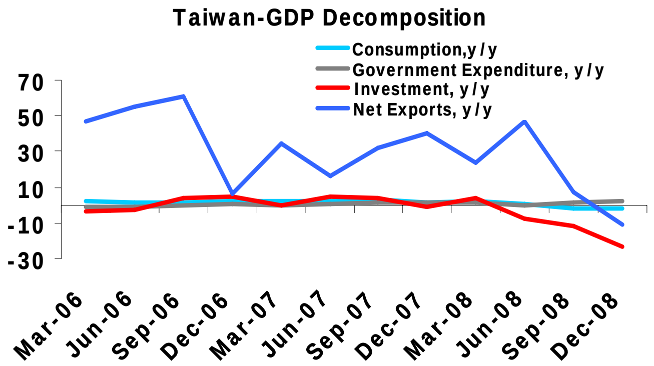
Tamara Henderson

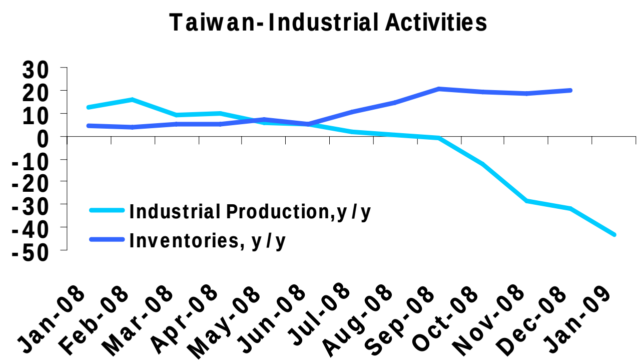
Market Forecasts - South Korea

FX	Current	Ytd (%)	Mar-09	Jun-09	Sep-09	Dec-09	Mar-	Jun-10
USD-KRW	1534	21.8%	1500	1400	1400	1375	1350	1300
AUD-KRW	982	11.0%	950	810	780	740	730	730
NZD-KRW	772	5.9%	750	630	600	560	570	560
JPY-KRW	15.68	13.0%	15.3	14.0	13.9	13.5	12.9	12.0
EUR-KRW	1938	10.1%	1880	1680	1570	1510	1460	1430
Rates	**Current**	**Ytd (bps)**	**Mar-09**	**Jun-09**	**Sep-09**	**Dec-09**	**Mar-**	**Jun-10**
BOK's overnight call rate	2.00	-100	1.50	1.00	1.00	1.00	1.50	2.00
3-month KORIBOR	2.51	-144	2.5	2.0	1.6	1.6	1.9	2.4
2-year IRS (vs 91D KRW CD)	2.98	-31	2.5	2.0	2.0	2.0	2.1	2.2
10-year IRS	3.68	11	3.5	3.3	3.3	3.3	3.4	3.4

Sources: ANZ and Bloomberg

Country Update: Taiwan





Taiwan suffered a record year-on-year fall in GDP in Q4 2008. Domestic demand remains weak and the decline of export orders accelerated in January, suggesting a vulnerable start to 2009.

- GDP shrank by 8.4% (y/y) in Q4, after dropping 1.0% in Q3. Manufacturing and services contributed the most to the decline. Net exports fell sharply (-11.3%), and facilities investment, which is highly correlated with exports, collapsed by 23.2%.
- Domestic demand remains weak, as commercial sales dropped by 18.8% (y/y) in Jan. However, retail sales only fell 1.9% compared with a drop of 11.3% in Dec, supported by the “shopping voucher” scheme.
- Industrial production contracted by 43.1% in Jan, in line with the deterioration in the external sector. Producer inventories have been building up quickly in the last few months. Industrial production cannot recover until the necessary adjustment in inventories has been completed.
- Exports declined by a record 44.1% (y/y) in Jan, while imports fell even more sharply, by 56.5%. Exports to China shrank more than 50%, mirroring the slowdown in assembly activities on the Mainland.
- Inflation concerns have faded, with CPI rising by 1.6% (y/y) in Jan, 0.4ppt above the rate in Dec.
- The CBC cut its policy rate by 25bps to a historical low of 1.25% on Feb, 18. Further rate cuts are expected and the loosening of monetary conditions should continue.
- Export orders, which are seen as an important leading indicator, dropped by 41.7% (y/y) in Jan.
- Government expenditure will likely be the only growth engine for most of 2009. The Ministry of Finance has planned a NT$170bln bond issuance in Q1. Given that the current public debt-to-GDP ratio is around 30%, there is ample room to ramp up spending to combat the effects of the global slowdown.

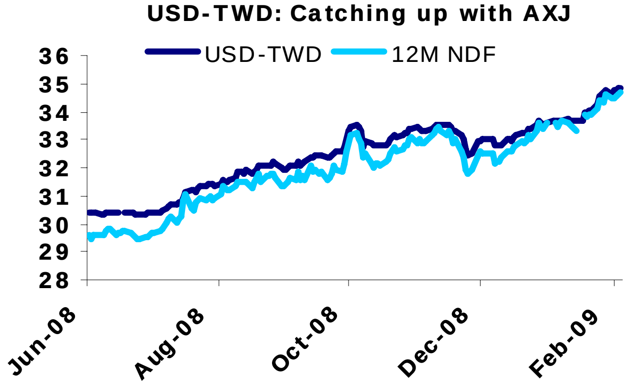
Zhou Hao

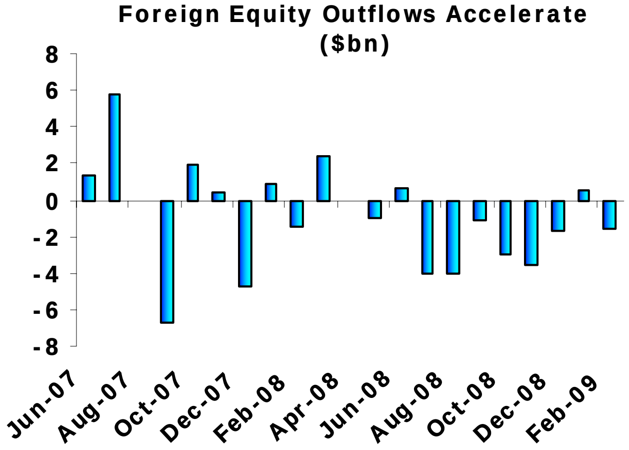
Economic Data - Taiwan

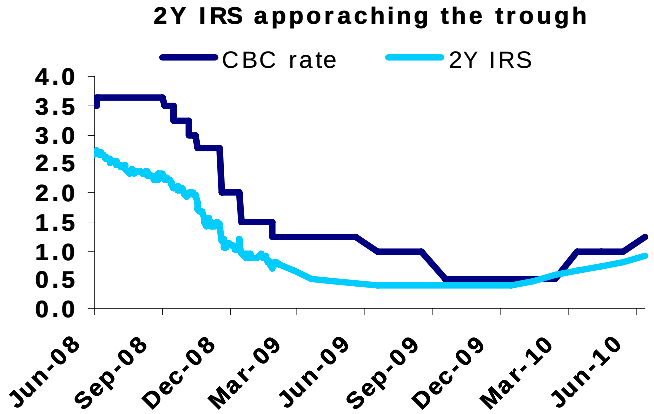
Monthly data	Jun-08	Jul-08	Aug-08	Sep-08	Oct-08	Nov-08	Dec-08	Jan-09
Industrial Production, % y/y	5.2	1.9	0.7	-1.2	-12.5	-28.3	-32.0	-43.1
Retail Trade Index, % y/y	-5.1	-10.0	-7.3	-7.8	-6.1	-9.0	-11.3	-1.9
Consumer Price Index, % y/y	5.0	5.8	4.7	3.1	2.4	1.9	1.3	1.6
Exports, % y/y	21.2	7.9	18.2	-1.6	-8.3	-23.3	-41.9	-44.1
Imports, % y/y	22.4	11.8	39.8	10.3	-7.2	-13.2	-44.6	-56.5
Trade Balance, US$ bn	1.4	-0.4	-0.1	0.8	2.9	1.5	1.8	3.3
Foreign Exchange Reserves, US$	291.4	290.9	282.1	281.1	278.2	280.7	291.7	292.7
Quarterly data	**Mar-07**	**Jun-07**	**Sep-07**	**Dec-07**	**Mar-08**	**Jun-08**	**Sep-08**	**Dec-08**
Real GDP, % y/y	3.8	5.5	7.0	6.4	6.2	4.6	-1.0	-8.4
-Private consumption	2.3	2.2	3.1	1.6	2.1	0.5	-2.1	-1.7
-Government consumption	0.0	0.7	1.7	1.1	1.3	-0.2	1.2	2.2
-Gross fixed capital formation	-0.3	4.7	3.8	-0.8	3.7	-8.0	-11.8	-23.2
Real GNP, % y/y	4.1	6.2	6.4	6.1	6.8	3.1	-0.5	-8.4
Nominal GDP, TWD tn	2.6	2.5	2.8	2.9	2.7	2.6	2.7	2.6
Current Account, US$ mn	9,410.0	5,905.0	6,477.0	11,183.0	8,494.0	6,744.0	1,867.0	7,919.0
Capital Account, US$ mn	-26.0	-19.0	-33.0	-18.0	-271.0	-20.0	-32.0	-11.0

Source: Bloomberg, CEIC

Taiwan: FX and Rates Strategy







The pace of gains in USD-TWD has started to increase—tracking a staggering drop in exports and a record contraction in GDP. Authorities appear to have sanctioned the move, and further gains in USD-TWD seem assured. The only question is speed.

FX

The 8.4% (y/y) contraction in Taiwan's Q4 GDP was unprecedented. Unfortunately, the outlook remains bleak. After a staggering 42% (y/y) contraction in December exports, the result for January managed to be even worse (-44%). January export orders suggest further deterioration in the months ahead, contracting nearly 42% compared with a drop of 33% in the previous month. In addition, global risk appetite has faltered in tandem with US equities, which have now broken below key levels of support.

The authorities have responded with more rate cuts and have given the green light for USD-TWD to move higher, reportedly selling TWD in the first part of February to cap gains. In addition, CBC Vice Governor Chou has openly encouraged Taiwanese importers to hedge foreign currency exposure. As such, we expect USD-TWD to remain in an uptrend in the months ahead. The only uncertainty would seem to be the pace of gains—CBC was reportedly selling USD (Feb 28) to prevent a push through the 35.0 level.

Note that Taiwan's external position remains solid, as the drop in exports has been out-paced by imports. As such, the current account surplus quadrupled in Q4 to $8bn, and FX reserves rose to the highest in at least six years to $293bn in January.

Rates

The CBC cut rates to a record low in February. We expect still more to come, favouring receiver positions.

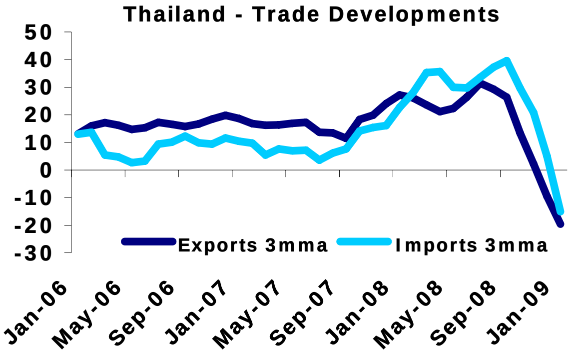
Tamara Henderson

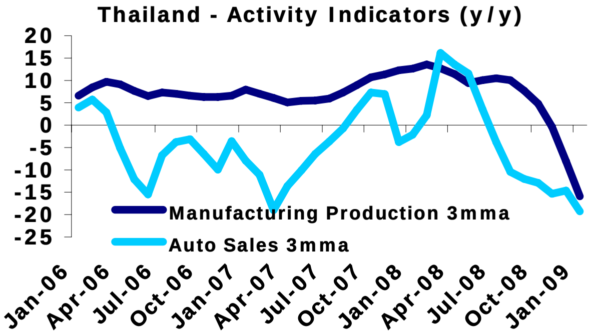
Market Forecasts - Taiwan

FX	Current	Ytd (%)	Mar-09	Jun-09	Sep-09	Dec-09	Mar-10	Jun-10
USD-TWD	34.85	6.3%	35.2	36.0	36.0	35.5	35.5	35.0
AUD-TWD	22.45	-2.6%	22.2	20.9	20.2	19.2	19.2	19.6
NZD-TWD	17.64	-7.2%	17.6	16.2	15.5	14.6	14.9	15.1
JPY-TWD	0.356	-1.5%	0.359	0.360	0.356	0.348	0.338	0.324
EUR-TWD	44.27	-3.5%	44.0	43.2	40.3	39.1	38.3	38.5
Rates	**Current**	**Ytd (bps)**	**Mar-09**	**Jun-09**	**Sep-09**	**Dec-09**	**Mar-10**	**Jun-10**
CBC's discount rate	1.25	-75	1.25	1.00	0.50	0.50	1.00	1.25
3-month CP	0.57	-51	0.5	0.4	0.4	0.4	0.6	0.9
2-year IRS (versus 3M CP)	0.78	-28	0.6	0.5	0.5	0.5	0.8	1.0
10-year IRS	1.45	1	1.4	1.3	1.3	1.3	1.4	1.5

Sources: ANZ and Bloomberg

Country Update: Thailand





Thailand continues to face severe challenges, with investment, tourism and exports suffering from the global downturn. The good news is that PM Abhisit's coalition has brought a much-needed reduction in political uncertainty.

- Thailand's GDP contracted by 4.3% (y/y) in Q4, down from growth of 3.9% in Q3. This was due to a decline in exports and investment, which fell 8.6% and 3.3%, respectively. Private consumption growth slowed to 2.2% from 2.7%.
- Domestic demand momentum appears to be fading. Automobile sales plummeted 29.4% (y/y) in Jan, down from -8.3% in Dec. The consumer confidence index rose slightly to 75.2 in Jan from 74.8 in the previous month, but still signals that consumers believe the economy will continue to weaken, albeit at a slower pace.
- Manufacturing production fell for the third straight month, contracting 21.3% in Jan, led by a fall in the production of construction materials and electronics.
- Exports contracted by 25.3% (y/y) in Jan compared with a 12.5% decline in Dec. However, imports fell even faster, down 36.5% in Jan from a decline of 6.5% in Dec. The trade surplus rose to $1.7bn, the largest in two decades.
- Tourist arrivals remained dismal, falling by 10.5% (y/y) in Dec. The continued perception of political instability, along with a weaker external environment, means that tourism receipts will likely remain subdued in coming months.
- Inflation continued to decline, with prices falling 0.4% (y/y) in Jan following an increase of 0.4% in Dec, largely due to a drop in energy prices.
- The Bank of Thailand cut its benchmark interest rate by 50bps to 1.50% amid weaker growth prospects and abating inflation.
- PM Abhisit plans to spend THB 117bn in 2009 on measures to support growth, including cash handouts, free school supplies and tax waivers. Growth should fall to the 1-2% range this year.

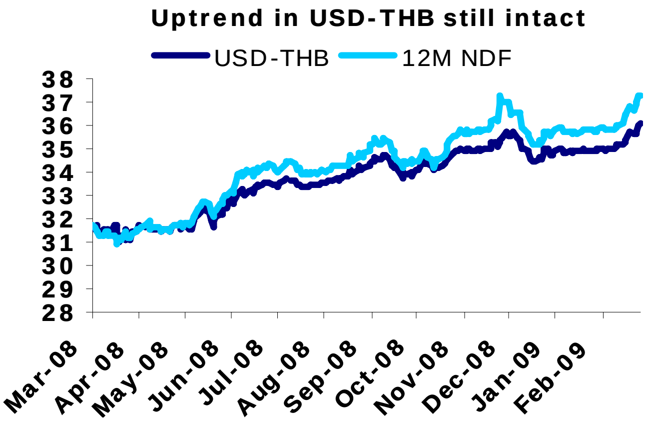
Chang Wei Liang

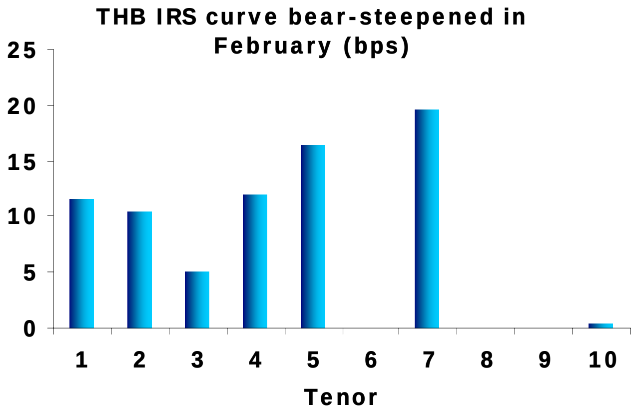
Economic Data - Thailand

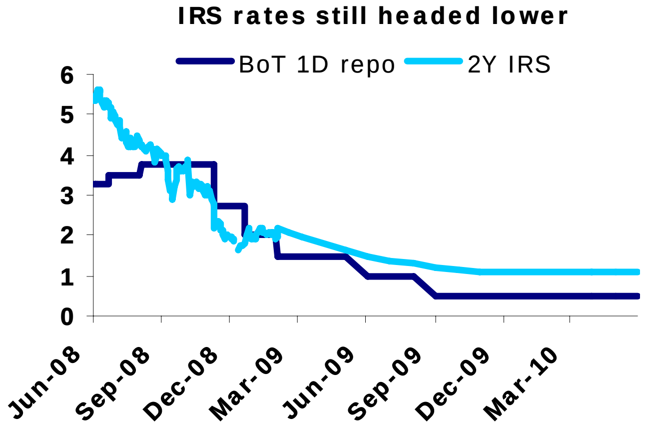
Monthly data	Jun-08	Jul-08	Aug-08	Sep-08	Oct-08	Nov-08	Dec-08	Jan-09
Industrial Production, % y/y	11.3	11.1	7.8	4.3	2.4	-7.7	-18.5	-21.3
Retail Sales, % y/y	7.0	5.9	4.8	-0.5	-3.2	-13.7	-2.5	N/A
Consumer Price Index, % y/y	8.9	9.2	6.4	6.0	3.9	2.2	0.4	-0.4
Exports, % y/y	30.4	47.4	17.7	22.6	5.2	-18.6	-12.5	25.3
Imports, % y/y	30.7	55.1	26.9	39.3	21.7	2.0	-6.5	36.5
Trade Balance, US$ bn	0.8	-0.8	-0.6	0.4	-0.7	-1.3	0.2	0.0
Foreign Exchange Reserves,	103.0	102.1	98.9	99.9	101.0	103.8	108.3	107.9
Quarterly data	**Mar-07**	**Jun-07**	**Sep-07**	**Dec-07**	**Mar-08**	**Jun-08**	**Sep-08**	**Dec-08**
Real GDP, % y/y	4.4	4.4	5.1	5.7	6.0	5.3	3.9	-4.3
-Private consumption	1.4	1.2	1.9	1.9	2.7	2.5	2.7	2.2
-Government consumption	8.4	10.5	8.9	9.0	-0.4	-3.7	-2.9	10.4
-Gross fixed capital formation	-1.4	0.1	2.5	3.8	5.4	1.9	0.6	-3.3
Nominal GDP, THB bn	2,096.5	2,047.3	2,093.7	2,255.7	2,297.1	2,283.1	2,321.4	2,201.1
Current Account, US$ bn	1.8	1.1	1.7	2.2	1.0	0.7	-0.3	0.1
Capital Account, US$ bn	-0.1	0.6	2.3	1.0	6.8	-4.0	2.6	-0.7

Source:Bloomberg, CEIC

Thailand: FX and Rates Strategy







Thai authorities are using all available tools to cushion the impact of the global recession—rate cuts, fiscal stimulus, lowering investment hurdles, and sanctioning a weaker currency to help exporters. More rate cuts and further gains in USD-THB are anticipated in the months to come.

FX

In sharp contrast with last year, the baht is among the currencies that have out-performed within AXJ thus far in 2009—having shed "just" 4.2% against the USD compared with 5.7% for AXJ. We expect such out-performance to be temporary, and look for an assault on the 40.0 level before year-end.

Indeed, the baht's performance within AXJ slipped in February—down 3.7% against the USD compared with 3.4% for AXJ. Notably, the authorities were reportedly in the market on numerous occasions in February selling THB in order to help Thai exporters remain competitive against regional counterparts. In addition, BoT Governor Tarisa Watanagase said the bank would "make sure the baht moves in line with regional currencies" (Feb 19).

Rates

The BOT has slashed interest rates by a cumulative 225bps, cutting the one-day repo rate in progressively smaller increments—100bps in December, 75bps in January and 50bps in February to 1.50%. Although we see scope for another 100bps of rate cuts before the trough is reached, markets recognize that monetary policy ammunition is getting low. At the same time, the government is ramping up spending to cushion the blow from the global slump—fuelling concerns about bond supply. Such cross-winds continue to favour curve steepening positions over the near-term.

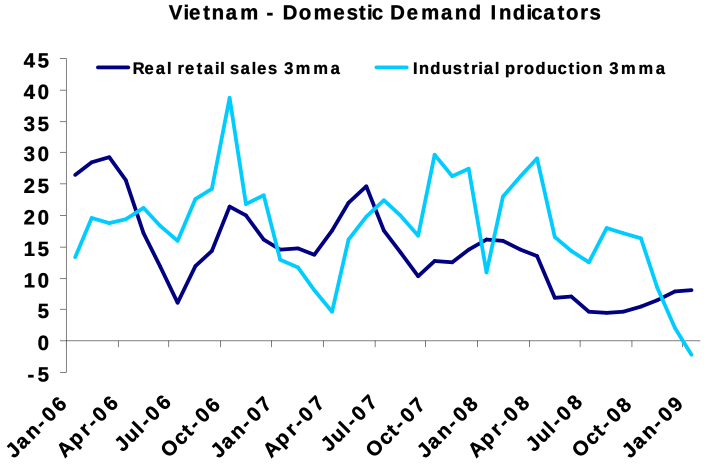
Tamara Henderson

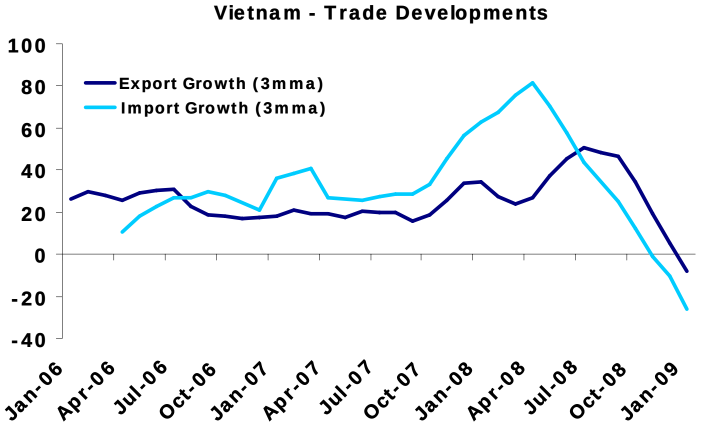
Market Forecasts - Thailand

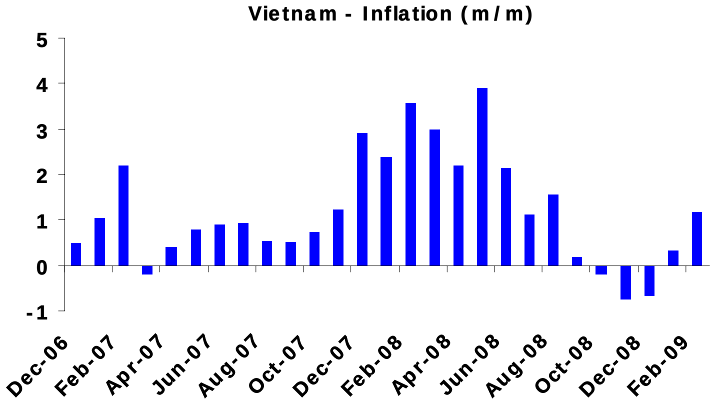
FX	Current	Ytd (%)	Mar-09	Jun-09	Sep-09	Dec-09	Mar-10	Jun-10
USD-THB	36.06	3.8%	36.2	37.6	39.4	39.4	38.8	38.8
AUD-THB	23.29	-4.6%	22.8	21.8	22.1	21.3	21.0	21.7
NZD-THB	18.24	-9.4%	18.1	16.9	16.9	16.2	16.3	16.7
JPY-THB	18.28	0.0%	0.369	0.376	0.390	0.386	0.370	0.359
EUR-THB	18.22	2.5%	45.3	45.1	44.1	43.3	41.9	42.7
Rates	**Current**	**Ytd (bps)**	**Mar-09**	**Jun-09**	**Sep-09**	**Dec-09**	**Mar-10**	**Jun-10**
BOT's 1-day repo rate	1.50	-125	1.00	0.50	0.50	0.50	0.50	0.50
3-month BIBOR	1.80	-115	1.7	1.2	0.8	0.6	0.6	0.6
2-year IRS (vs 6M THB fix)	2.20	35	1.7	1.2	1.1	1.1	1.1	1.1
10-year IRS	3.63	126	3.5	3.3	3.3	3.3	3.3	3.3

Sources: ANZ and Bloomberg

Country Update: Vietnam







The pace of activity continues to soften although the declines in investment and exports may be stabilising. Inflation is now half the mid-2008 "crisis" level, although the latest monthly rate jumped substantially. The SBV is moving to further ease monetary conditions. Growth looks to be on a 5% track this year.

- Our analysis is complicated by the timing of the Lunar New Year. Where appropriate, we averaged the Jan and Feb growth rates.
- Domestic demand appears to be weakening. Real retail sales growth is trending near 5% while industrial production growth is falling by 3%, although the trend has stabilized.
- Exports fell by 3.7% (y/y) in the first two months of the year. Rice shipments doubled while oil shipments fell by over 40%. Imports fell by 42.3% during the period; the decline was broad-based. The trade balance was in surplus through Feb.
- Inflation fell sharply to 14.8% (y/y) in Feb, barely half the level of mid-2008. Food prices are still rising by 22%. Somewhat worryingly, monthly inflation was 1.2% in Feb, easily the highest print since last March.
- Monetary conditions continue to be eased. The State Bank of Vietnam announced it will lower the mandatory reserve ratio from 5% to 3% in March. Also, the government will provide a 4ppt interest rate subsidy (via the banks) to virtually all sectors of the economy to spur credit growth.
- The Ho Chi Minh index fell by nearly 20% in February as risk appetite waned. Foreigners were net sellers in every week of the month.
- Vietnam will fare better than most emerging Asian economies in 2009 given its weak links to the global financial system and its domestically-led growth. The overall pace of activity should decline to 5 to 5½%, but the risks are on the downside.

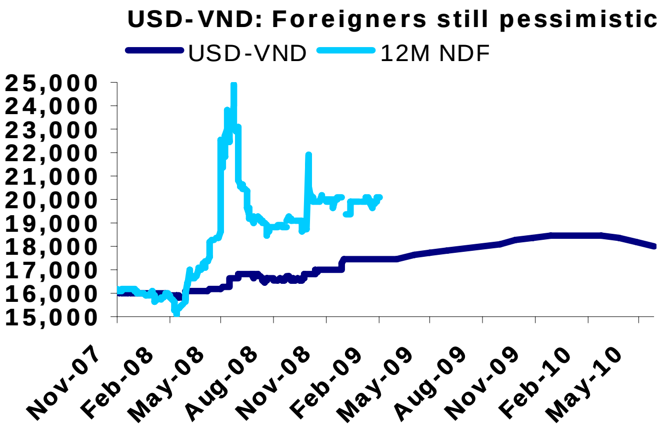
Paul Gruenwald

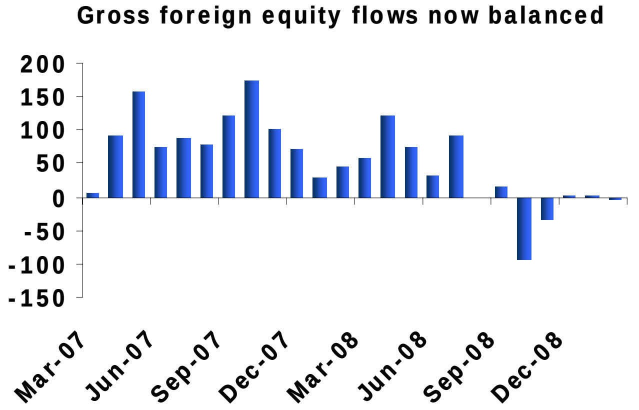
Economic Data - Vietnam

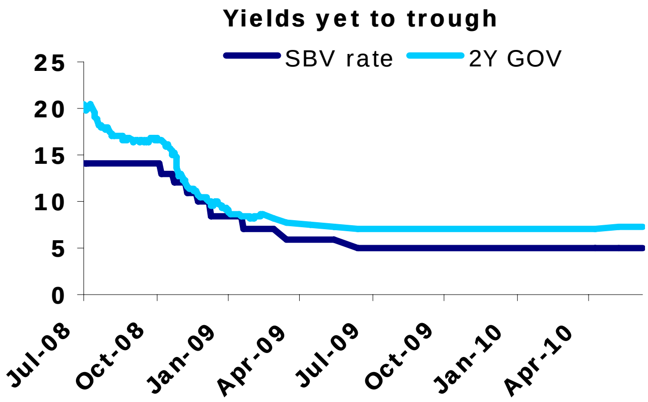
Monthly data	Jul-08	Aug-08	Sep-08	Oct-08	Nov-08	Dec-08	Jan-09	Feb-09
Industrial Production, % y/y	11.4	29.3	9.1	9.2	-0.3	0.5	-4.2	19.4
Retail Sales, % y/y	36.1	27.5	37.7	38.9	26.9	34.1	29.7	5.8
Consumer Price Index, % y/y	27.0	28.3	27.9	26.7	24.2	19.9	17.5	14.8
Exports ytd, % y/y	37.1	36.7	39.1	36.7	34.3	30.0	-25.8	-3.7
Imports ytd, % y/y	60.3	53.9	51.1	44.2	38.9	32.2	-55.2	-42.3
Trade Balance, USD bn	-1.0	-0.4	-0.5	-0.2	-0.9	-0.4	0.4	-0.1
Quarterly data	**Mar-07**	**Jun-07**	**Sep-07**	**Dec-07**	**Mar-08**	**Jun-08**	**Sep-08**	**Dec-08**
Real GDP, % y/y	7.7	7.8	8.2	8.5	7.5	6.5	6.5	6.2
-Agricultural, forestry, fishery	2.3	2.8	3.1	3.7	3.2	3.3	3.8	3.8
-Industry and construction	9.2	9.7	10.1	10.6	8.0	7.0	7.0	6.3
-Services	7.8	8.5	8.6	8.7	8.3	7.6	7.2	7.2
Nominal GDP, VND tn	210.9	282.6	293.8	356.8	254.1	371.7	390.8	462.2
Foreign Exchange Reserves, USD	18.3	20.8	22.6	23.5	26.4	22.3	23.8	0.0

Sources: Bloomberg, CEIC, General Statistics Office of Vietnam

Vietnam: FX and Rates Strategy







The authorities are trying to dampen speculation about a further devaluation in the dong in order to shore up investor confidence. Ultimately, we expect officials to sanction further gains in USD-VND as the external environment remains challenging in the months ahead.

FX

Having devalued the dong in October, November and late December, the authorities are now trying to quell speculation about further slippage against the USD in order to build market confidence. In recent months, the devaluations of the currency had been justified by officials as a means to stabilize the economy and support exports, which fell nearly 30% in 2008. In contrast, the central bank said in February that it will clamp down on currency speculation, and that speculation about a devaluation of the dong was "inaccurate."

Meanwhile, registered FDI plunged to a record low in January ($185mln or 10.8% of the level in January 2008). Disbursed FDI is down 21% from a year ago. Net foreign portfolio equity flows have turned negative, down 107% (ytd) as of end-February. In addition, aggressive rate cuts have significantly compressed what had been an attractive yield differential. Whether the authorities can appeal to foreign investors by offering (and delivering) a stable currency remains to be seen. We believe the external environment will remain too challenging for the authorities to hold the line at 17,500 in USD-VND. NDFs are priced for a level approaching 20,000 in twelve month's time, while we are more inclined to view 18,500 as the peak this year.

Rates

Having already slashed the policy rate by a cumulative 700bps, the government has now turned to interest rate subsidies as a means of further supporting domestic demand without discouraging foreign investment. As such, we shift to a neutral view on the VND curve.

Tamara Henderson

Market Forecasts - Vietnam

FX	Current	Ytd (%)	Mar-09	Jun-09	Sep-09	Dec-09	Mar-10	Jun-10
USD-VND	17,480	0.0%	17,500	17,800	18,100	18,500	18,500	18,000
AUD-VND	11,267	-8.3%	11,000	10,300	10,100	10,000	10,000	10,100
NZD-VND	8,838	-12.7%	8,800	8,000	7,800	7,600	7,800	7,700
JPY-VND	179	-7.3%	179	178	179	181	176	167
EUR-VND	22,221	-9.0%	21,900	21,400	20,300	20,400	20,000	19,800
Rates	**Current**	**Ytd**	**Mar-09**	**Jun-09**	**Sep-09**	**Dec-09**	**Mar-10**	**Jun-10**
SBV's base lending rate	7.00	-150	6.00	5.00	5.00	5.00	5.00	5.00
Overnight VNIBOR	6.54	N/A	5.8	5.0	5.0	5.0	5.1	5.2
2-year IRS (versus 3M VNIBOR)	8.47	-201	7.7	7.0	7.0	7.0	7.0	7.2
10-year IRS	9.15	-56	8.9	8.7	8.7	8.7	8.7	8.7

Sources: ANZ and Bloomberg

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