OCBC Global Outlook 2H25

A tale of tariff risks and market reckoning

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As dawn broke on 2025, the global economy found itself at a critical juncture. The world was still shaking off the lingering effects of the pandemic, while new challenges - geopolitical strife, tariffs, and technological disruption - had emerged to reshape the economic landscape. The first half of the year unfolded like a high-stakes chess match between central banks, financial markets, and political leaders. The global economy, much like a ship navigating stormy seas, had shown remarkable resilience - but the waters ahead remained treacherous, with undercurrents of risk that could capsize even the most stable of vessels.

The tariff shockwave in 1H25

The United States: no longer the resilient juggernaut?

The United States entered 2025 as the relative bright spot in the global economy. Nonetheless, GDP growth in the first quarter contracted 0.2% QoQ, which is a slight improvement from the initial estimate of a 0.3% decline, but still marked the first drop in three years. The key contributing factor was the frontloading of imports amid heightened tariff anxiety, spurred by consumers' panic buying coupled with businesses stockpiling ahead of the potential tariffs. Since the inauguration of US president Trump on 20 January, the flurry of executive orders and tariff announcements have steamrolled financial markets. Still, US recessionary fears have faded after the initial roller-coaster ride for financial markets in April after the 'Liberation Day' tariff announcements on 2 April. The labor market, though cooling from its post-pandemic highs, remained robust, with nonfarm payrolls printing at 139k for unemployment relatively stable at 4.2% for May.

Yet beneath the surface, cracks were forming. The Federal Reserve remains in a delicate balancing act, under pressure from US president Trump to slash interest rates, but cautiously awaiting the inflation and growth implications from tariffs, albeit delayed. Meanwhile, May consumer price index (CPI) ticked up to 2.4% YoY (0.1% MoM), but the core CPI was static at 2.8% YoY (0.1% MoM), which is still above the Fed's 2% target. With the FOMC currently in wait-and-see mode, any expected rate cuts have been delayed into late 2025, with market players eyeing the next move earliest only at the September FOMC.

Given that reciprocal tariffs are currently in the 90-day suspension period till early July, there is still little clarity about who else will be able to negotiate a trade deal with the US administration, apart from the UK and maybe China. The US Court of International Trade has ruled the use of emergency powers to justify the sweeping reciprocal tariffs as unlawful, but the Federal Circuit Court of Appeals allowed the tariffs to stay in place amid the legal battles. That said, the US administration may still pivot to other measures such as Section 232 (national security), Section 301, Section 122 etc to sustain tariff manoeuvres.

Meanwhile, the "one big, beautiful bill" is currently making its way through Congress. Comprising of tax cut extensions from the 2017 Tax Cuts and Jobs Act, repeals of certain Biden administration tax credits, provisions for border security, defence and energy production, raising the debt ceiling etc., this bill is estimated to increase long-run GDP by 0.8% but also raise the 10-year budget deficit by USD2.6trn from 2025-2034 on a conventional basis before added interest costs,

according to the Tax Foundation. In turn, this has fuelled market speculation of de-dollarization and a shift to diversify away from USD-denominated assets. Moody's also recently did a one-notch downgrade of the US' credit rating to strip it of its Aaa rating to Aa1, saying that successive US administrations and Congress had failed to agree on measures to reverse the trend of large annual fiscal deficits and growing interest costs. Given the state of flux and many moving parts, it will likely still be an exciting and bumpy ride ahead for the US economy. This is notwithstanding President Trump's famous words that "Trade wars are good, and easy to win."

Europe: to the rescue?

Across the Atlantic, the Eurozone's GDP growth was revised up to 0.6% QoQ in 1Q25, double the pace of 0.3% published a month ago. This economic performance was inspired by Germany, the industrial powerhouse, which recorded 0.4% growth (after a more modest 0.2% in 4Q24) and also a strong showing by Ireland (9.7%). Nonetheless, unpredictable US tariff policies still threaten to cast a long shadow over the region which could face 50% tariffs on steel and aluminium and 25% tariffs on auto import.

In the Spring 2025 Economic Forecast, the prognosis is for moderate growth (1.1% for the EU and 0.9% for the euro area) amid the global economic uncertainty. This represents a significant downgrade to the Autumn 2024 Forecast, largely due to the impact of increased tariffs and unpredictability of the tariffs' final configuration. EU exports could stumble in line with lower global goods demand, while weaker domestic demand would similarly weigh on import growth.

The European Central Bank (ECB) had cut interest rates for the eighth time to 2% recently, but the latest cut was tipped more as a strategic move to ensure inflation remains on track towards the 2% target over the medium term. This would help to underpin inflation expectations and avoid an unwarranted tightening in financial conditions, according to Lane. Importantly, ECB chief Lagarde has hinted that the central bank is now "in a good position" as inflation is now just below 2%. Market interpretation is a pause is imminent, but we have not ruled out one more cut later this year. As disinflationary pressures strengthen, there is probably policy space for the policy rate to reach the lower end of the neutral 1.75%-2.25% range.

Should the US-EU trade tensions subside, there could be potential upside momentum for Eurozone growth. External headwinds that prompt greater EU structural reforms, similarly, such as in the areas of infrastructure and defence spending, could be constructive for growth potential in the medium-term as well.

Japan: Virtuous cycle interrupted?

The Japanese economy presented a paradox in 2025. 1Q25 growth contracted at an annualised pace of 0.2%, weighed down by weak net exports, albeit this was less severe than the initial estimate of a 0.7% decline. This weak performance was even before the announcement of US reciprocal tariffs in April, suggesting that the economy was already sluggish and did not really benefit from any frontloading effects pre-tariff. In fact, Japan's exports shrank in the first 20 days of May and trade negotiations with the US have not yielded concrete results. A technical recession in 2Q25 cannot be ruled out as the combination of weak domestic demand, sustained inflation and a lack of progress in trade negotiations. Japanese chief negotiator

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Akazawa is meeting US counterparts for a third round of talks, but an agreement is still elusive at this juncture.

Core inflation (excluding fresh food) accelerated to 3.5% YoY in April, the fastest in more than two years, driven by soaring rice (+98.4%) and energy (9.3% post-phasing out of government subsidies for gas and electricity) prices. While this should bolster the case for further monetary policy normalization, BOJ officials remain cautious about further rate hikes. BOJ kept its policy rate unchanged at 0.5% earlier this month and BOJ governor Ueda has warned of "extremely high" uncertainties ahead of the 16-17 June meeting.

The economic fragility comes ahead of the key upper house election in July. PM Ishiba's approval ratings have fallen to their lowest since he took office amid rising costs of living concerns. Unsurprisingly, PM Ishiba's administration is already drafting an economic stimulus plan to ease the costs for households, but consumption-tax cuts may not yet be forthcoming due to fiscal concerns.

China: The Great Slowdown

Once the unstoppable engine of global growth, the world's second-largest economy is now grappling with a confluence of structural challenges. 1Q25 GDP growth came in at 5.4% YoY, unchanged to that in 4Q24, after policy efforts to strengthen the domestic economy to offset the impact of the trade war. There are green shoots that recent talks in London have yielded to a principle to a framework on rare earths and sales of strategic technologies. However, China will still face an additional 30% tariffs on exports to the US. Meanwhile, disinflation continues to plague the Chinese economy, even as several initiatives to boost domestic consumption, including a trade-in subsidy program for consumer goods, are already in place. The question remains if China can continue to engineer a soft landing as the pace of its slowdown has significant implications for the rest of the region.

ASEAN: Under pressure amid global uncertainties

Southeast Asian economies have shown relative resilience in 1Q25 despite the global uncertainties, especially the external headwinds like tariffs. Some of the contributing factors were the stable domestic demand, a rebound in tourism as well as frontloading effects ahead of the expected US tariffs, particularly during the 90-day suspension period. But even ASEAN was not immune to global headwinds. Weaker demand from China and the threats of reciprocal and sectoral tariffs took a toll on business and consumer confidence. Given the disparate and elevated reciprocal tariffs that smaller ASEAN economies like Laos, Cambodia and Vietnam may eventually face when the 90-day suspension period expires, the outlook remains cloudy.

Inflationary pressures have abated across most ASEAN nations, allowing their central banks to adopt a more accommodative stance. ASEAN's trade policy has focused on deepening regional integration while navigating shifting global trade dynamics. The recent ASEAN Summit noted that the ASEAN Trade in Goods Agreement (ATIGA), which helped to reduce tariffs, will be upgraded. However, non-tariff barriers such as divergent product standards and customs inefficiencies, are beyond the low-hanging fruits. Individual members are also pursuing bilateral trade negotiations with the US administration while looking to bilateral deals with

economic partners outside of the US. Looking ahead, ASEAN needs to continue to accelerate digital trade frameworks, harmonise regulations, collaborate and cooperate to mitigate any polarization in the global economic landscape.

The second half of 2025 presents both opportunities and risks for ASEAN. To sustain growth, ASEAN must enhance supply chain resilience, expedite regional payment connectivity, position the bloc as a global economic hub in an increasingly fragmented global economy. To avoid falling prey to a "divide and conquer" strategy under an aggressive US tariff regime, ASEAN must leverage its centrality in regional trade frameworks like RCEP for instance to maintain open supply chains, stay united, diversify partnerships and reinforce economic resilience in order to secure its own economic future.

The dance of risk and reward in financial markets

Equities: The AI Frenzy and the return of trade wars

Financial markets navigated a turbulent period in the first half of 2025, marked by shifting US Federal Reserve rate cut expectations, US recession fears, geopolitical turmoil and surprising macroeconomic twists and turns. In the US, the S&P 500 story was one of mega-cap tech stocks, comprising AI, cloud computing amongst others. A roller-coaster April post-Liberation Day reciprocal tariff announcements sent shockwaves through financial markets. Since then, however, any green shoots of a trade deal such as the UK-US and more recently hints of an agreement for China's rare earth exports (which are critical input for high-tech manufacturing) in exchange for semiconductors have boosted market sentiments as investors look for reasons to dip their toes back in.

Bonds: the great pivot

The US Treasury bond market saw wild swings, with the 10-year yield hitting a high of 4.79% on 14 January before slumping to a year-to-date low of 3.99% on 4 April and is currently trading in the middle of the wide range around 4.38% as of 12 June. Financial markets had started 2025 anticipating 6 Fed rate cuts, but ended 1H25 with expectations for just one to two cuts. Interestingly, market interpretation is that the bond vigilantes are the ones calling the shots rather than the equity market when it comes to the "TACO" meme.

Meanwhile, gold prices hit fresh highs whereas oil prices slid from USD78 per barrel to a year-to-date low of USD56 per barrel before recovering to again the mid-range of US66 per barrel. In Asia, the picture was mixed – concerns about punitive reciprocal and sectoral tariffs continue to weigh, which meant that rallies were fleeting to a certain extent.

Currencies: The Dollar's Slow Retreat

The U.S. dollar, after a multi-year reign of prominence, showed tentative signs of weakness in 2025. The DXY index, which tracks the greenback against a basket of major currencies, slid in the first half of the year as the Fed's tightening cycle peaked. Market chatter about de-dollarisation and diversification away from USD-denominated assets meant the USD had to take a backseat, but also meant that some central banks could ease monetary policy to support growth, especially with subsiding inflation.

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With the softer USD, emerging market currencies were more stable as investors turn their eye back to macro-economic fundamentals, benefiting those with higher yields such as the Indonesian rupiah and Thai baht.

Commodities: Oil's precarious balance

Oil prices oscillated in the first half of 2025, caught between supply risk, the unwinding of OPEC+ supply cuts, concerns over global trade friction and uncertainty, as well as weak demand from China. Specifically, OPEC+ has brought forward its plans of phasing out 2.2mbpd in voluntary cuts, with four consecutive months of production hikes between April and July. Nevertheless, escalating geopolitical tensions pose an upside risk to oil prices.

On 13 June, the Israeli military launched multiple airstrikes on targets across Iran in an effort to dismantle Iran's nuclear enrichment programme. In response, Iran has vowed to retaliate heavily against these military strikes. This incident resulted in a spike in crude oil prices to a near five-month high. Should the situation escalate into a broader regional conflict, Brent oil prices could exceed USD100/bbl, potentially reaching USD120/bbl, reflecting fragile risk sentiment and market unease over any incident that could trigger a wider escalation. Under these circumstances, further sanctions on Iran and trade routes blockages in the Strait of Hormuz (SOH) cannot be ruled out, as this is a critical transit route for oil from the Middle East to the rest of the global oil market.

On the other hand, gold has outperformed to date, reaching fresh highs on multiple occasions. Year-to-Date as of 13 Jun 2025, gold rallied ~30%. Geopolitical risks, tariff threats, concerns of US debt sustainability, questions around USD's status as safe haven and primary reserve currency were some of the reasons that boosted the appeal of gold as a hedge against heightened uncertainty.

Over in the edible oil front, crude palm oil (CPO) has lost its rare premium over soybean oil since April, aligning with our expectations, and has traded below MYR4,000/mt since May, compared to an average of MYR4,673 in 1Q25. We forecast CPO to average MYR4,300 in 2025, up from MYR4,218 in 2024, reflecting a more balanced CPO dynamic. While output is set to rise seasonally in 2H25, demand from major importers like India and China is also expected to strengthen. Domestic demand in Indonesia remains firm. While consumption for industrial and edible purposes continues to be robust, the key driver of growth in 2025 will be the biodiesel sector, following the implementation of the B40 mandate in February 2025.

Will the roller-coaster continue in 2H25?

As a quote goes, "We're decoupling, but slowly, messily, and expensively,". Indeed, this trade war 2.0 will continue to reshape global supply chains. Shellshocked companies are delaying capex and investments and also hiring intentions, while workers are tightening their belts in anticipation of the cooling labour market conditions. Apart from the kneejerk reactions in financial markets with important wealth effects, this would likely translate into real economic impact down the road. It is unsurprising then that 2025 GDP growth forecasts have been marked down across the board, whether by the IMF, World Bank, OECD, AMRO or OCBC Research for that matter.

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While there are glimmers that US trade deals are being struck, the clock continues to tick and confidence may be elusive the more prolonged the uncertainties. While 1H25 was a story of resilience and recovery, the drama may not be over yet. The 2H25 narrative will be written by growth, inflation, policy shifts and fickle risk appetite. We see a soft but tepid landing for the global economy, with clear geographical divergences – for instance, a slowdown for the US is long overdue and is likely to play out from 2H25 but an outright recession is not our base case.

Central banks are likely to continue to walk a fine line in 2H25. Most central banks are inclined to ease monetary policy further, with the exception of the BOJ, but a data-dependent approach means the decision would swing on the upcoming inflation prints as market players are carefully watching for the tariff pass-through. There is little consensus on how much and when the Fed will cut rates again. In turn, the questions if current market rallies, banking more on hope than anything else, will run out of fuel. With the core unpredictability of US president Trump's flip-flop tariff policy, the wildcard is double-edged – should we get an upside surprise of tariff reduction and/or trade deals galore on the July 9 deadline, this could also imply upside risk to the current market swoon.

As the curtain rose on the second half of 2025, the global economy stood at a crossroads. The path ahead would be shaped by central bank decisions, geopolitical developments, and the unpredictable whims of markets. Between hope and fear, we probably have to be content with that this will be a marathon race rather than a 100-meter sprint. As the old Wall Street adage goes, in the end, you're measured not by how much you make, but by how much you keep. For investors, the playbook theme remains clear: stay nimble, diversify, and prepare for volatility. When the sky is cloudy, preserving capital might prove just as important as chasing returns.

GDP Growth Rates

% Change YoY	2024	2025F	2026F	2027F
US	2.8	1.3	1.5	1.5
Eurozone	0.9	0.9	1.1	1.1
Japan	0.2	0.6	1.0	1.0
United Kingdom	1.1	1.0	1.2	1.5
New Zealand	-0.5	1.4	2.7	2.7
Australia	1.0	1.8	2.3	2.5
China	5.0	4.6	4.4	4.5
Hong Kong	2.5	2.2	2.3	2.0
Taiwan	4.3	3.3	2.4	2.3
India	6.5	6.0	6.0	6.2
Indonesia	5.0	4.7	4.8	5.0
Malaysia	5.1	4.3	4.3	4.5
Philippines	5.7	5.5	5.9	6.0
Singapore	4.4	1.6	2.5	2.5
South Korea	2.0	1.0	1.4	2.1
Thailand	2.5	2.0	2.0	3.0
Vietnam	7.1	5.5	5.5	6.0

Note: India forecasts are based on the fiscal year. FY25 is April 2024 until March 2025.
Source: Bloomberg, IMF, OCBC.

Inflation Rates

% Change YoY	2024	2025F	2026F	2027F
US	3.0	2.4	2.2	2.2
Eurozone	2.4	2.0	2.0	2.0
Japan	2.7	2.2	2.0	2.0
United Kingdom	2.5	2.7	2.3	2.1
New Zealand	2.9	2.0	2.0	2.0
Australia	3.2	2.5	2.7	2.6
China	0.2	0.5	2.2	2.4
Hong Kong	1.7	1.7	2.1	2.3
Taiwan	2.2	2.2	1.8	1.7
India	4.6	3.8	4.2	4.0
Indonesia	2.3	2.0	2.7	2.5
Malaysia	1.8	3.0	2.1	2.0
Philippines	3.2	2.5	2.5	3.0
Singapore	2.4	0.9	1.5	1.8
South Korea	2.3	1.9	1.8	1.9
Thailand	0.4	0.9	2.0	2.0
Vietnam	3.6	3.7	4.0	4.0

Note: India forecasts are based on the fiscal year. FY25 is April 2024 until March 2025.
Source: Bloomberg, IMF, OCBC.

Central Bank Policy Rates

Benchmark Rate %	Current	End-2025F	End-2026F
US Fed Funds Rate	4.25-4.50	3.50-3.75	3.25-3.50
ECB Deposit Facility Rate	2.00	1.75	1.75
BoJ Target Rate	0.50	0.75	1.00
BoE Base Rate	4.25	3.75	3.50
RBNZ Cash Rate	3.25	3.00	3.00
RBA Cash Target Rate	3.85	3.35	3.35
China Loan Prime Rate (1-year)	3.00	2.80	2.80
CBRC Discount Rate	2.000	1.875	1.875
Hong Kong Base Rate	4.75	4.00	3.75
BI Rate	5.50	5.25	5.25
BNM Overnight Rate	3.00	2.50	2.50
BSP Overnight Reverse Repo	5.50	5.00	5.00
RBI Repurchase Rate	5.50	5.00	5.00
Singapore SORA*	1.89	2.20	2.20
BOK Target Overnight Call	2.50	2.00	2.00
BOT Repurchase Rate	1.75	1.50	1.50
SBV Refinancing Rate	4.50	4.00	4.00

*Benchmark risk free rate
Note: India forecasts are based on the fiscal year. FY25 is April 2024 until March 2025.
Source: Bloomberg, IMF, OCBC.

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Australia

Australia: Room for RBA to Ease

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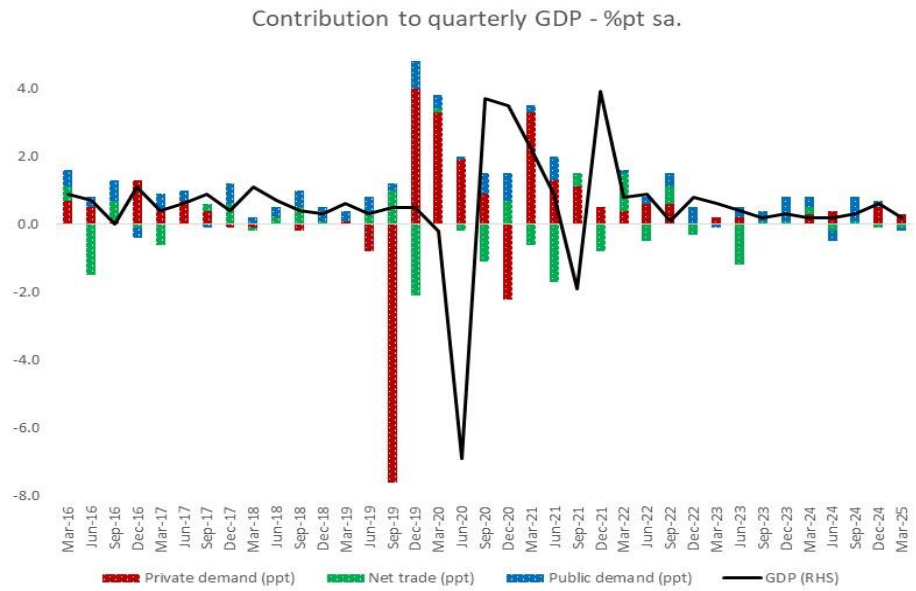
- Economic growth outlook should continue to recover slightly for rest of 2025, driven by a rebound in household consumption, continued strength in public demand, and accommodative monetary policy. That said, the pace of recovery may be more gradual due to weaker global demand, trade-related uncertainties and softer domestic consumption momentum.
- The disinflation journey has progressed steadily over the past year, with both headline and underlying inflation easing into the RBA's 2–3% target range. Headline CPI is projected to rise temporarily above 3% in 2H25 as more subsidies expire but should converge to settle around the midpoint of the target range into 2026.
- Our view is that RBA is not in a hurry to ease policies, given still tight labour market while inflation is just returning to RBA's target range, with the risk of a slight rebound in 2H25. Our base-case looks for one 25bp cut each in 3Q25 and 4Q25.

Economy may continue to recover, albeit gradually

The Australian economy expanded 0.2% QoQ in 1Q25, compared to 0.6% QoQ in 4Q24. Annually, GDP rose 1.3%. Public sector spending contracted, with large declines in public investment and no growth in government spending. Energy, telecommunications, rail and road project completions and delays drove the decline in public investments.



Source: Australian Bureau of Statistics, OCBC Research

State and local government spending declined by 0.3%, primarily due to decreased electricity rebate payments to households in most areas. Meanwhile, national government spending continued to moderate as spending on social benefit programs including the Medicare Benefits Scheme (MBS) and the National Disability Insurance Scheme (NDIS) fell.

Australia

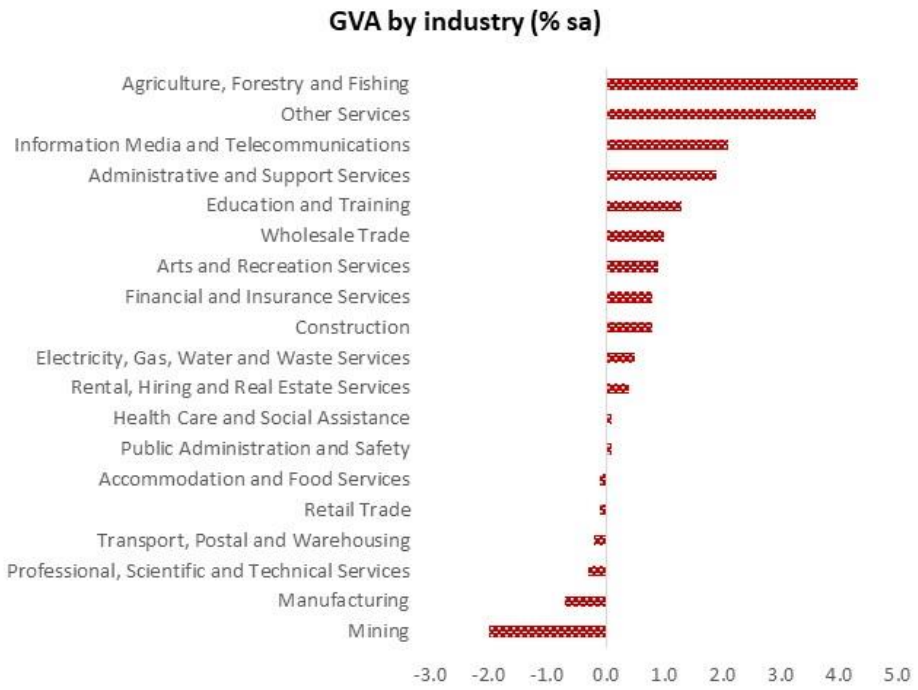
Private demand, comprising household consumption, dwelling investment, and business investment, was a key driver of growth although momentum slowed, and the recovery was uneven across components.

Household consumption increased 0.4%, with essential spending significantly driven by a substantial 10.2% increase in spending on electricity, gas, and other fuels. This surge was attributed to higher electricity usage due to warmer summer conditions and the reduction of electricity bill relief payments to households. Food spending also saw an increase of 0.8%, as supermarket disruptions from the previous quarter normalised and Queensland households prepared for Ex-Tropical Cyclone Alfred by stockpiling essentials. Discretionary spending grew at a slower pace of 0.3%, following a strong retail performance in 4Q24, although there were notable increases in vehicle purchases and a 1.0% rise in spending on recreation and culture, aided by high attendance at major sporting and music events, such as F1 Grand Prix, Australian Open, AFL opening round and Adelaide Fringe Festival.

Private investment rose by 0.7%, contributing 0.1 ppt to GDP growth. Dwelling investment saw a significant increase of 2.6%, reflecting heightened activity in house constructions and renovations in line with a rise in approvals. Non-dwelling construction also increased by 1.3%, driven by investments in mining and electricity projects, while machinery and equipment investment fell by 1.7% with the decline in IT equipment spending.

In terms of gross value added (GVA) by industry, the 'Agriculture, Forestry and Fishing' sector led the gains, rising by 4.3% QoQ. This was driven by strong livestock output to meet sustained export demand, particularly from the United States. However, grain production was limited due to wet weather affecting summer crop planting in Queensland. Other key contributors to GVA growth included the Services industries, with Construction increasing by 0.8% in line with heightened private investment in both residential and non-residential projects, Information Media and Telecommunications rising by 2.1% due to strong performance in broadcasting and digital services, and Administrative and Support Services growing by 1.9% as activity in tourism, travel, and recruitment agencies picked up. In contrast, the mining sector experienced a decline of 2.0%, with decreases in all major commodities like coal, iron ore, and oil and gas, largely due to adverse weather conditions from cyclones in Queensland and Western Australia.

Australia



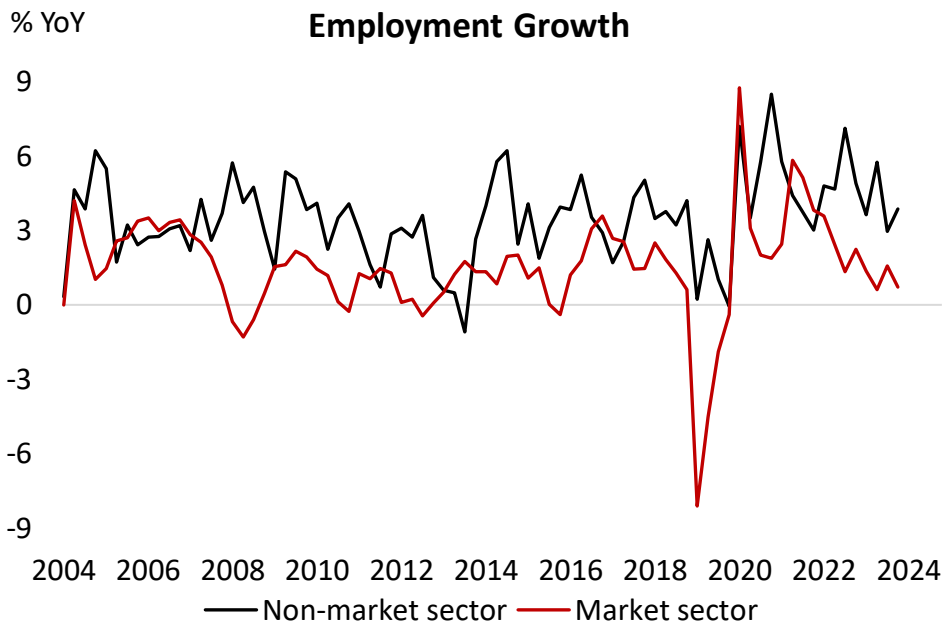
Source: Australian Bureau of Statistics, OCBC Research

Looking ahead, economic growth outlook should continue to recover slightly for rest of 2025, driven by rebound in household consumption, continued strength in public demand, and accommodative monetary policy. That said, the pace of recovery maybe more gradual due to weaker global demand, trade-related uncertainty and softer domestic consumption momentum. We project 2025 growth to come in at 1.8%, a step down from earlier projection of 2.3% (per our 1H25 outlook).

Still tight labour market; modest softening ahead

Labour market conditions have remained steady in recent months. The unemployment rate has hovered around 4.1% since mid-2024, and employment growth has been solid. The steady unemployment rate could be explained by the improvement in market sector jobs growth over 2024, with the accommodation and food services industry recording the largest rise in employment in the past year. The non-market sector, which includes the health care and education industries, continued to support employment growth through to late 2024. Participation and employment-to-population ratios remain near historical highs, reflecting a resilient labour force.

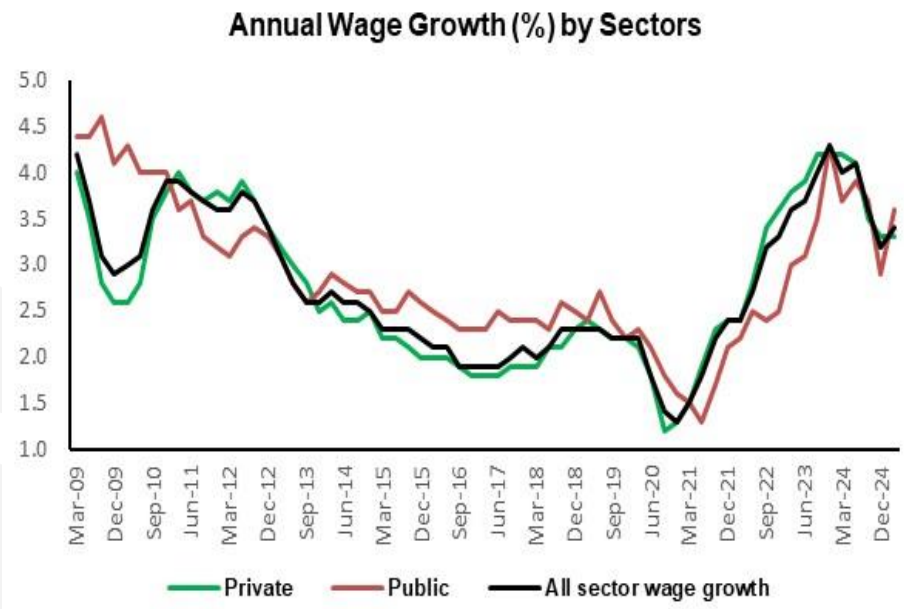
Australia



Source: Australian Bureau of Statistics, OCBC Research

Wage growth on a year-ended basis has moderated over the past year. 1Q25 wage growth however ticked up modestly to 3.4%. Public sector wages were the main driver, due to one-off public sector awards for people working in childcare and aged care. Private sector wage growth held steady at 3.3%.

Looking ahead, wage growth is expected to ease gradually over the next year. RBA expects wage growth to stabilise around 3.0–3.1% by 2026. Public sector wages are likely to remain elevated in the near term due to ongoing agreement renewals, but overall, the outlook suggests a more balanced labour market with wage pressures continuing to moderate.



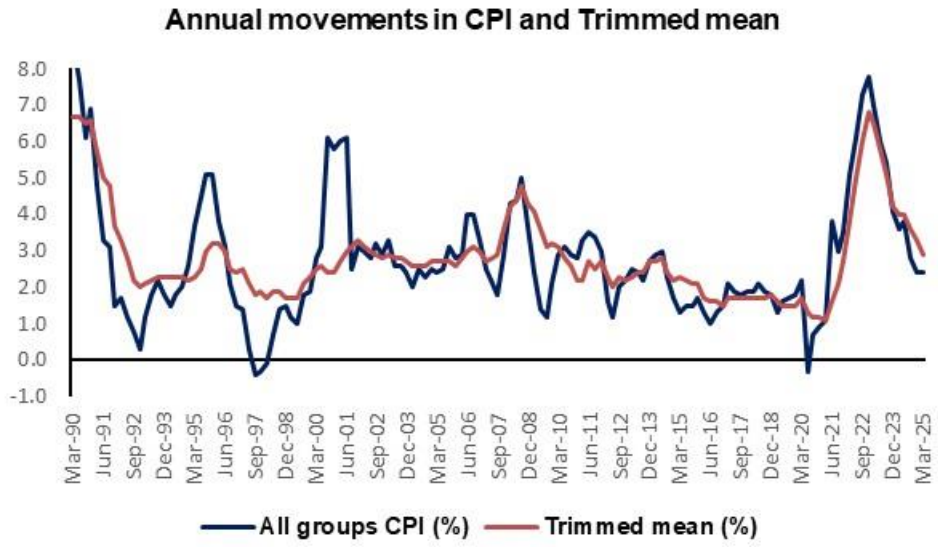
Source: Australian Bureau of Statistics, OCBC Research

Australia

Inflation has returned to RBA's target range

The disinflation journey has progressed steadily over the past year, with both headline and underlying inflation easing back within the Reserve Bank of Australia's (RBA) 2–3% target range. As of 1Q25, trimmed mean inflation – the RBA's preferred measure of underlying inflation – stood at 2.9% year-ended, while headline inflation was slightly lower at 2.4%. This marks the first time since late 2021 that underlying inflation has returned to the target, reflecting a broad-based moderation in price pressures.

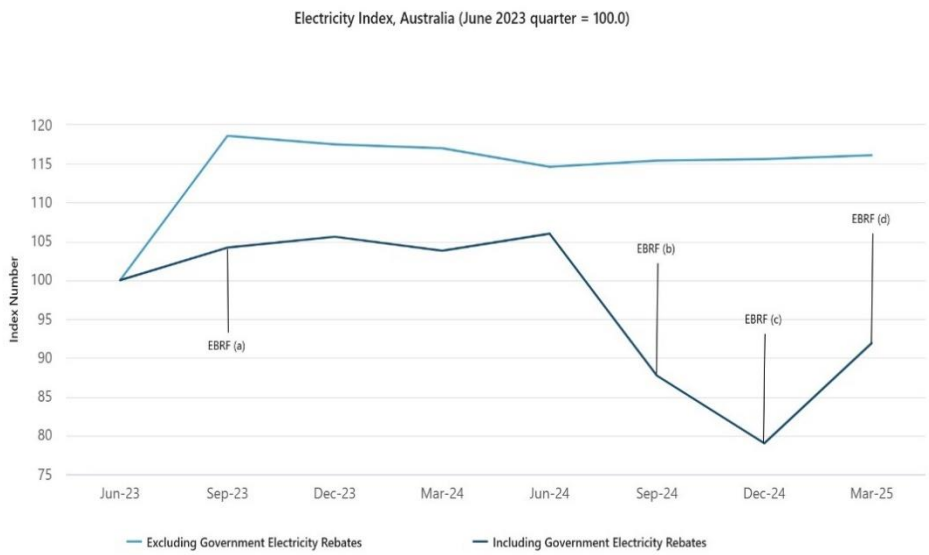
Several factors have contributed to disinflation including housing-related inflation. New dwelling construction costs declined and rent inflation stabilised, in line with earlier slowing in advertised rents. In addition, market services inflation, such as insurance and education, moderated and is now close to historical averages. Retail goods inflation has also slowed, although the full impact of recent global trade developments on import prices is yet to be seen. Finally, temporary government subsidies, particularly electricity rebates, have played a role in dampening headline inflation. However, some of these subsidies were unwound in 1Q25.



Source: Australian Bureau of Statistics, OCBC Research

Looking ahead, underlying inflation is expected to remain within RBA's 2–3% range, settling around the midpoint over the forecast horizon. Headline inflation is projected to rise temporarily above 3% in 2H25 as more subsidies expire, before converging back towards the midpoint. Financial market measures of inflation compensation remain close to survey measures of medium and long-term expectations. Unions' long-term inflation expectations have also fallen closer to the midpoint of the target range. Overall, long-term inflation expectations remain anchored at the target and inflation outlook has been revised a touch softer, reflecting softer domestic demand, easing labour cost pressures, and a modest decline in import prices.

Australia



a. Introduction of the 2023-24 Energy Bill Relief Fund (EBRF) for concession households in NSW, VIC, SA, TAS, NT and ACT, and all households in QLD and WA, from July 2023
b. Introduction of the first instalment of 2024-25 Commonwealth EBRF rebates for all households, and State government rebates in QLD, WA and TAS, from July 2024
c. Introduction of the second instalment of 2024-25 Commonwealth EBRF rebates for all households, and the second instalment of the WA State government rebate
d. Introduction of the third instalment of the 2024-25 Commonwealth EBRF rebates for all households in NSW, VIC, QLD, SA, TAS, NT and ACT

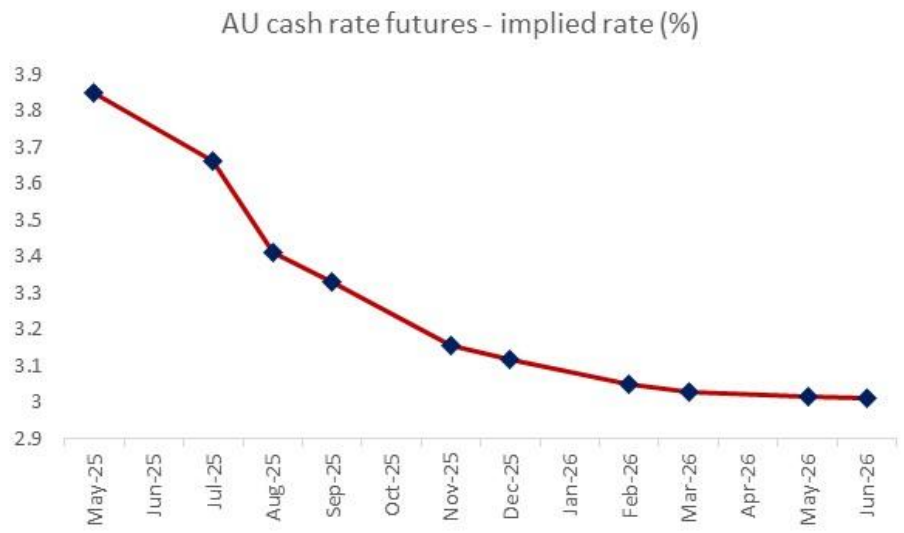
Source: Australian Bureau of Statistics, OCBC Research

RBA's easing cycle has room for another two cuts this year

RBA lowered cash rate two times in 2025, with the most recent 25bp cut at the 20 May MPC. The cash rate now stands at 3.85%. RBA's rhetoric was more dovish than expected and the cash rate futures added to rate cut expectations, an additional 72bps for the rest of the year.

Some highlights of the accompanying statement alluding to RBA's dovishness were seen in Governor Bullock revealing that a 50bp cut was discussed, although the strength of argument for a 25bp cut was much bigger, and there was also discussion between a hold and a cut. The statement opined that "inflation is in the target band and upside risks appear to have diminished" – while understandably the commentaries have to support the rate cut decision and hence would be more dovish than the previous statement, such an opinion was still picked up as dovish. The Board has a scenario analysis – considering a severe downside scenario and noted that "monetary policy is well placed to respond decisively"; while this is a scenario analysis, it nevertheless reflects the asymmetric risk that the Board sees.

Australia



Source: Bloomberg, OCBC Research

Our view is that RBA is not in a hurry to ease policy, given the still tight labour market condition while inflation is just returning back to RBA's target range, with risk of slight rebound in 2H25. Growth risks are somewhat skewed to the downside, owing to tariff implications. A lower cash rate path is expected to provide support to activity amid global economic headwinds. Our base line looks for a 25bp cut each in 3Q and 4Q 2025, following the 25bp cut to 3.85% at the 20 May meeting.

Euro Area

Euro Area: External headwinds

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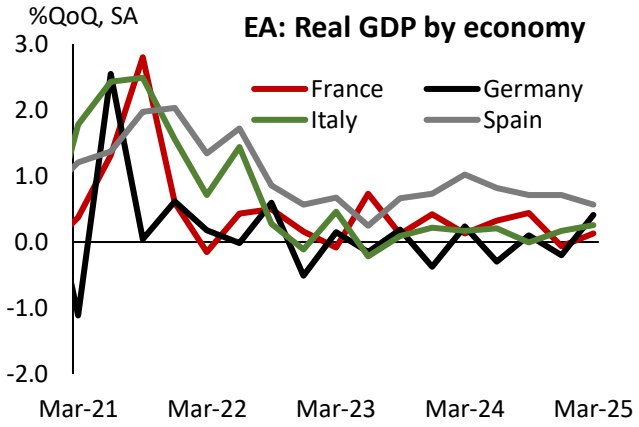
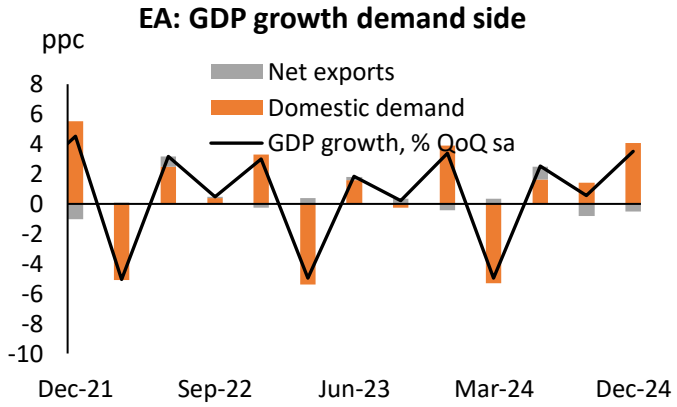
- We expect Euro area growth to be 0.9% YoY in 2025, with the balance of risks skewed to the downside. The outcome of trade negotiation with the US remains a key source of uncertainty in 2H25.
- Recent fiscal changes in Germany and the fading of US exceptionalism are some tailwinds to keep sentiments supported.
- In terms of monetary policy, we forecast another 25bp rate cut from the European Central Bank (ECB) following the 25bp cut on 5 June.

Trade uncertainties obfuscate the growth outlook

The Euro area grew at a strong pace of 0.9% YoY in 2024 from 0.4% in 2023 supported by higher government and private consumption expenditures. Investment spending, however, remained subdued as most key drivers fared poorly in 2024. Housing investment growth contracted through 2024, and twenty member states reported a decline[1] while investment spending in other key categories such as equipment, vehicles and intellectual property also contributed negatively to GDP growth. By member state, growth was strong in Spain (3.2%), Malta (6%), and France (1.2%) while it was stable in Greece (2.3%) and Italy (0.7). Germany's economy contracted by 0.2% YoY in 2024 from flat growth in 2023.



Source: CEIC; OCBC



Source: CEIC; OCBC.

Economic growth was 0.3% QoQ seasonally adjusted in 1Q25 from 0.1% in 4Q24, supported by the bigger economies including France, Germany, Italy and Spain. For 2Q25, the growth momentum is likely to see continued front-loading of exports to the US, which had earlier surged to 71.4% YoY in March from 59.5% February. US President Trump had extended the deadline for the imposition of additional tariffs to 9 July. The tariffs currently in place for EU products entering the US are 10% reciprocal tariffs, 25% tariffs on steel and aluminium and 25% levy on automobiles. On the other hand, PMI readings and a broad range of economic indicators suggest that the ongoing trade war has resulted in heightened uncertainty and reduce the

[1] European Commission Spring 2025 forecasts.

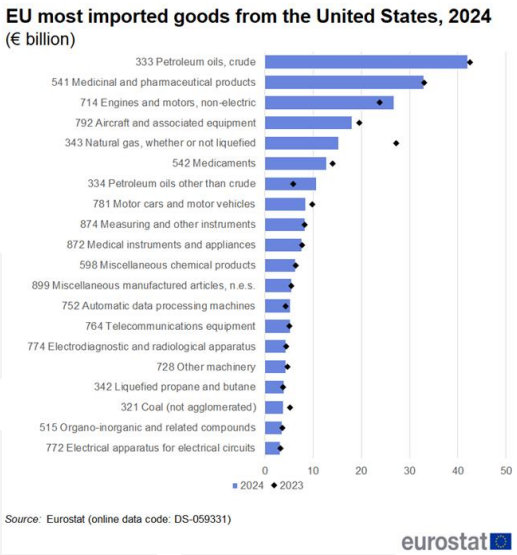
Euro Area

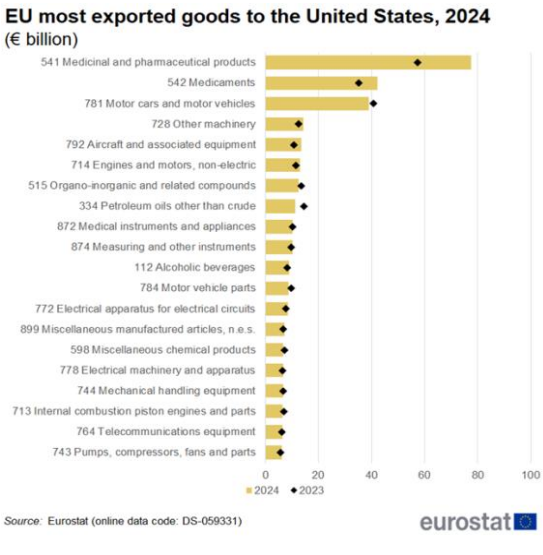
ability of businesses and households to make informed decisions, leaving most in a 'wait-and-see' limbo.

As such, we expect Euro area growth to be 0.9% in 2025, with the balance of risks skewed to the downside. The growth outlook will be heavily dependent on the outcome of tariff negotiations. The negotiations between the US and EU are reported to cover tariff and non-tariff barriers, raise economic security, mutual investments, strategic partnerships. Specific sectors that have been under the spotlight include agriculture and automotives.

More broadly, about 90% of EU exports to the US were manufactured products in 2024 and within this machinery & transport equipment and chemicals account for ~71%. The most exported good to the US in 2024 were medicinal and pharmaceuticals products, medicaments and motor cars and vehicles. In 2024, the US was the largest partner for EU exports of goods (20.6%) and the second largest partner for EU imports of goods (13.7%). The EU has a goods trade surplus of EUR197.4bn in 2024 with the US while it had a services deficit of EUR108.6bn in 2023.

Source: European Commission, CEIC, OCBC.





Euro Area

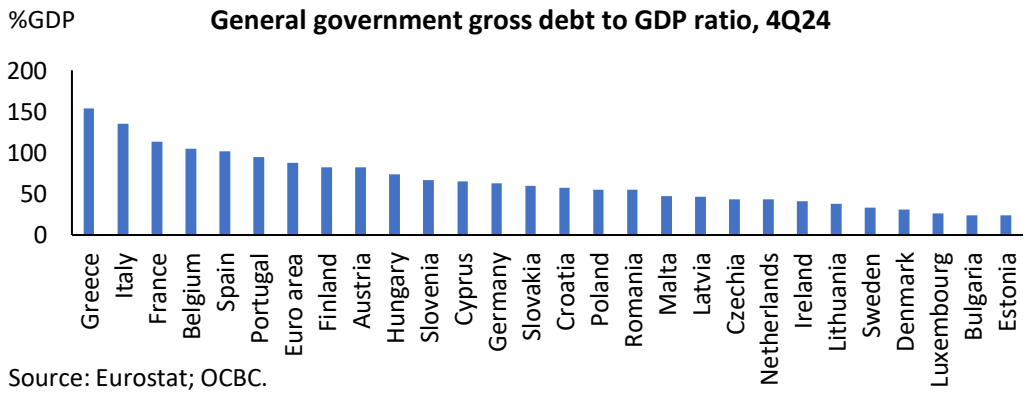
Within the EU, the US traded the most with Germany followed by Ireland, Italy, France and the Netherlands.

Developments in 1H25 suggest that the EU is poised for stronger medium-term growth. The changes in the Germany's fiscal framework in March 2025 could prove to be a strong catalyst for medium-term growth for Germany, and by extension the Eurozone. Specifically, Germany introduced crucial constitutional reform of its national fiscal framework.

First, it set up a new infrastructure fund worth EUR500bn (11.6% of 2024 GDP) outside the scope of the 'debt brake'. The fund is aimed at financing new projects in areas such as transportation, healthcare, energy, education, research and digitalisation within twelve years. Second, defence spending above 1% of GDP is excluded from the calculation of the 'debt brake' and third, the states are allowed to take on more debt up to 0.35% of GDP annually from previously required to run balanced budgets. The European Commission estimates that Germany's GDP could be 1.25% higher by the end of 2029 and 2.75% higher by 2035. It expects this to have positive spillovers onto the EU member states, lifting EU GDP by 0.75% by 2035.

Indeed, fiscal consolidation continued in the Euro area last year. The euro area government deficit to GDP ratio narrowed to 3.1% from 3.5% in 2023. The consolidation was led by Greece (+1.3% of GDP from -1.4% in 2023), Italy (-3.4% of GDP from -7.2 in 2023) and Cyprus (+4.3% of GDP from 1.7% of GDP) even as the France (-5.8% from -5.4%) and Germany (-2.8% from -2.5%) registered higher deficits.

The euro area general government gross debt to GDP ratio was relatively stable at 87.4% in 4Q24 from 87.3% in 4Q23. There is significant disparity in the debt ratio amongst the various euro area members, with Germany's debt to GDP ratio at 62.5% while Greece's ratio at 153.6% of GDP.

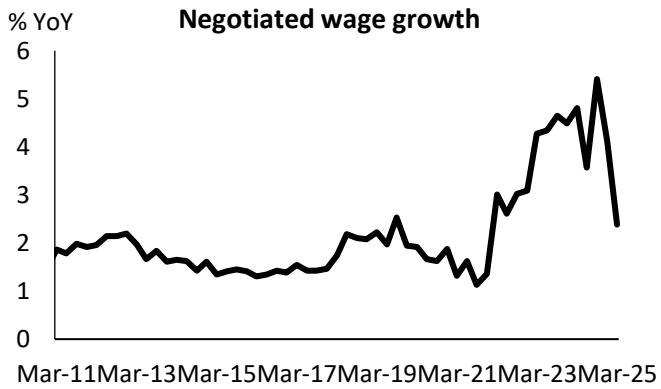


Source: Eurostat; OCBC.

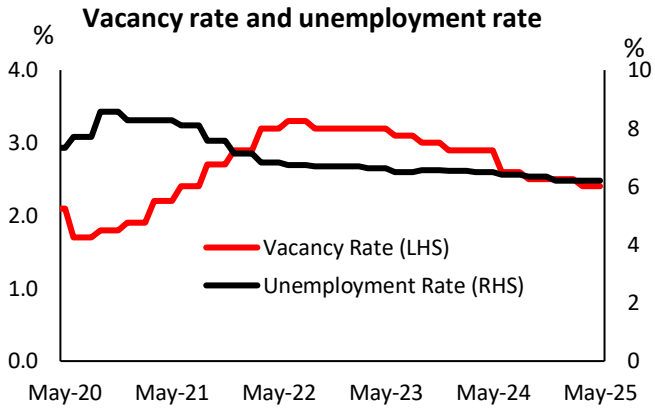
Meanwhile, labour market conditions have remained relatively resilient to start 2025. Euro area 1Q25 employment growth was 0.8% YoY, similar to 2024, while the unemployment rate remained unchanged at 6.2% in March. The labour productivity gains at 0.4% YoY were similar to 4Q24.

Euro Area

There are signs that the labour market may be slowing, consistent with the ECB's assessment. Negotiated wage growth for the Euro area slowed to 2.4% YoY in 1Q25 from 4.1% in 4Q24. Ahead of this, compensation per worker also slowed to 4.1% YoY in 4Q24 from 4.5% in 3Q24. The job vacancy rate stood at 2.4% in May 2025, versus 2.5% in December 2024.



Source: European Commission, Bloomberg, OCBC



Source: European Commission, Bloomberg, OCBC

Soft wage growth, subdued commodity prices and a weaker economic growth are likely to keep inflationary pressures in check in the Euro area. Headline inflation, as measured by the Harmonised Index of Consumer Prices (HICP), was stable at 2.2% YoY in April versus March. Higher food inflation of 3.0% in April from 2.9% in March was offset by lower energy inflation of -3.6% YoY versus -1.0% in March. Services inflation was higher at 4.0% YoY from 3.5% in March. Core inflation picked up to 2.7% YoY from 2.4% in March. We expect headline inflation to average 2.0% in 2025 from 2.4% in 2024.

Although the growth and labour market dynamics remain supported of continued disinflation, ECB President Lagarde was calibrated in her assessment of the impact of tariffs on inflation. She noted that "the question of the impact of tariffs on inflation is very delicate.[2]" She added that "there are lots of elements that are moving at the moment that we'll be able to estimate the impact of as the negotiations advance and as this new context develops."

Our house view is that there is one more 25bp cut to go for the remainder of 2025, taking the deposit rate to 1.75% by end-2025. ECB has significantly reduced its deposit rate by 200bps from May 2024 until 5 June 2025. This is significantly lower the US Federal Reserve's 100bp in rate cuts during the same period. The question is how much, if at all, lower the ECB will go, bringing into focus the terminal rate. The deposit rate at 2.00%, following the 25bp cut on 5 June, is broadly considered to be at neutral levels. ECB President Lagarde mentioned that the ECB is in a "good position". However, she did note that ECB will continue to "decide meeting-by-meeting on the basis of data…".

[2] Lagarde Says International Trade Will Never Be the Same, Bloomberg, 23 May 2025. Last accessed 12 June 2025.

Japan

Japan: Subdued growth

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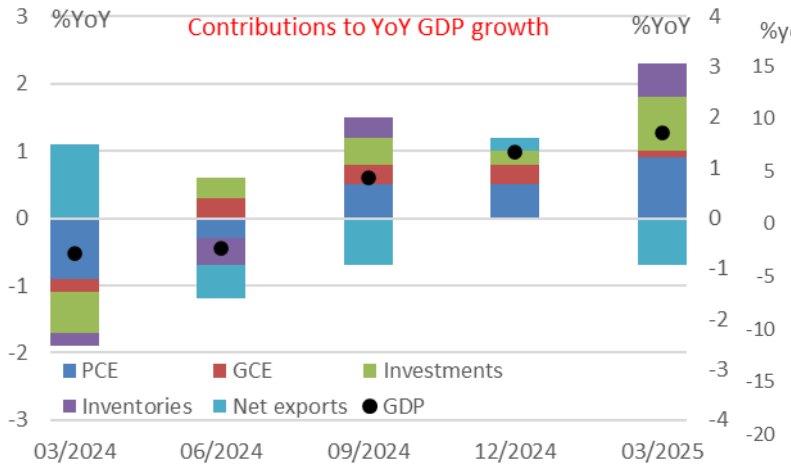
- Economic growth is likely to moderate in the quarters ahead, as business fixed investment plans have turned more cautious, and net exports may be a drag. Private consumption is likely to contribute positively to growth. We lower our 2025 GDP growth forecast to 0.6% YoY from 1.0% previously.
- A tight labour market and firms' price-setting behaviour suggest that the prospect remains for inflation to stay sustainably above the 2% target as wage growth is passed onto prices, albeit with downside risk should the tariff impact on growth turn out to be bigger than expected.
- The baseline inflation outlook allows the Bank of Japan (BoJ) to continue with monetary policy normalisation, but the subdued growth outlook means BoJ is in no rush to hike rates. We expect additional 50bps of rate hikes between now and 1Q26 which will bring the BoJ Target Rate to 1.00%.

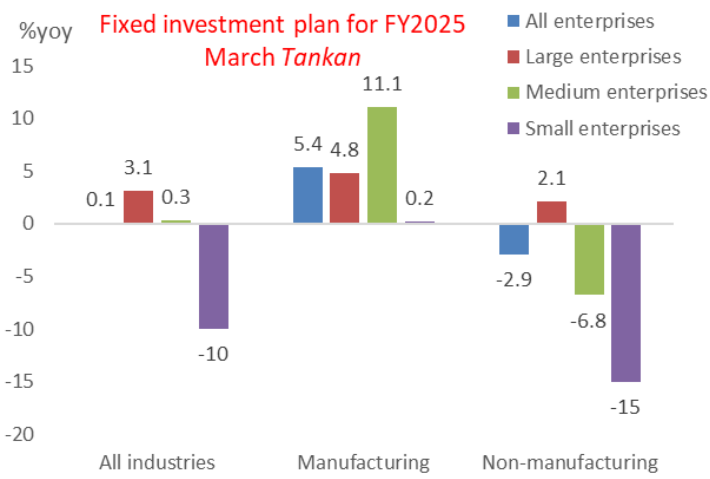
Subdued growth ahead

The economy shrank marginally by -0.04% QoQ seasonally adjusted in 1Q25, after three quarters of QoQ expansion. Net exports were the main drag, while private consumption grew by 0.1% QoQ, private investment grew healthily at 1.1% QoQ (residential investment) and 1.4% QoQ (non-residential investment). Our base-case outlook assumes some negative impact of tariffs on exports, and indirect impact on domestic demand in particular fixed investment as corporates hold back on investment plans in view of the uncertainty. We lower our 2025 GDP growth forecast to 0.6% YoY from 1.0% previously. Granted, tariff and other trade policy development remains fluid and there is a higher-than-usual uncertainty surrounding our baseline forecasts.

Private consumption is expected to increase moderately. While being virtually flat QoQ in 1Q25, private consumption nevertheless added 0.9 percentage points to YoY GDP growth in that quarter. Consumer sentiment has recently weakened partly due to the increases in the prices of food. But data including retail sales and household spending suggest that private consumption is still likely to contribute positively to annual growth. Moreover, another year of robust wage growth – as suggested by the *Shunto* results – is likely to keep private consumption resilient, as income catches up with price increases. That said, the risk is for smaller bonuses upon potentially narrower profits especially at manufacturing enterprises being affected by overseas demand amid tariffs.

Japan





Source: Bank of Japan, Cabinet Office, Bloomberg, OCBC Research.

Private non-residential investment expanded QoQ for a fourth quarter in 1Q25, consistent with the buoyant investment plans as reflected by the previous *Tankan* surveys. Business fixed investment plans for FY2025 have however turned more cautious as per the latest *Tankan* survey in March, especially for the non-manufacturing sector and small enterprises. Overall growth (all enterprises, all industries) projected for FY2025 is virtually zero (0.1%). Most optimistic is the 11.1% YoY growth projected at medium-size manufacturing enterprises, while most pessimistic is the 15.0% YoY fall in fixed investment at small non-manufacturing enterprises. The relatively optimistic plan at manufacturing enterprises suggest that the potential impact of tariffs might not have been fully reflected, as the survey was done before the announcement of reciprocal tariffs.

The US was the biggest merchandise exports market for Japan in 2024 and has continued to rank first in the first four months of this year. The impact of tariffs might have already started to show up, with Japan's exports to the US falling by 1.8% YoY in April, differing from the 2.0% YoY increase in total exports and the 6.0% YoY increase in exports to Asia. Japan's exports to the US amounted to 3.5% of Japan nominal GDP in 2024. In particular, automobile-related exports to the US amounted to 1.3% of nominal GDP growth – majority were high value-added motor vehicles on which an additional 25% tariff has been imposed. Export of vehicles (to all markets) had recovered from last year's certification issues, and increased steadily in 1Q25, only to reverse to a 5.8% YoY drop in April. At this juncture, we assume a negative 0.35 percentage point impact of tariff on GDP via the exports channel but note there is high uncertainty on the elasticity of demand and how trade relations evolve.

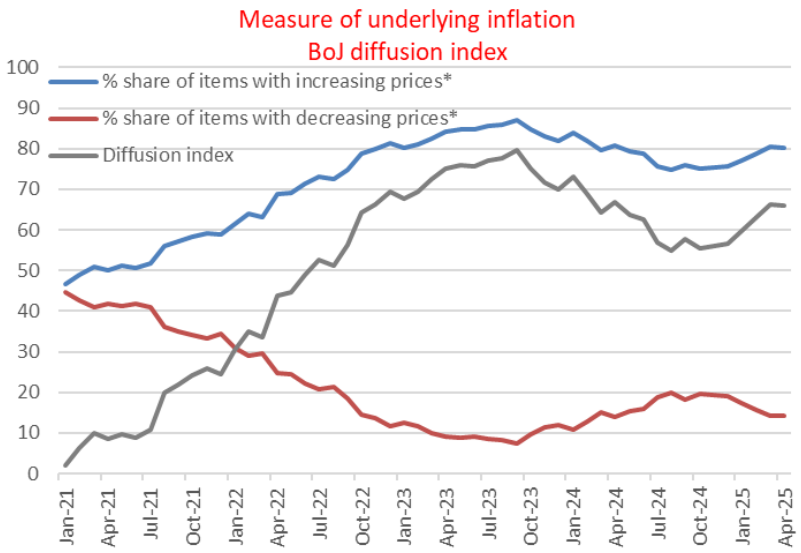
Prospect for sustained wage growth, and pass-through onto prices

A tight labour market and firms' price-setting behaviour suggest that the prospect remains for inflation to stay sustainably above the 2% target, albeit with downside risk should the tariff impact on growth turn out to be bigger than expected. While BoJ sounded somewhat dovish in the inflation outlook, opining "underlying CPI inflation is likely to be sluggish, mainly due to the deceleration in the economy", it nevertheless puts FY2025 core CPI inflation forecast at 2.0-2.5%. According to BoJ,

Japan

the output gap has followed an improving trend and is likely to remain around the current level before improving again towards the end of their projection period.

Core CPI (CPI less fresh food) and core core CPI (CPI less fresh food and energy) inflation have been picking up in year-on-year terms over recent months. Core CPI inflation hit 3.5% YoY in April, the fastest since January 2023. Core core CPI inflation printed 3.0% YoY, the highest since February 2024. The May Tokyo CPI inflation was also hotter than expected, with Tokyo core CPI inflation at 3.6% YoY and Tokyo core core CPI inflation at 3.3% YoY. According to BoJ's measure of underlying inflation, the share of items in the core CPI basket which saw YoY increases in prices has rebounded and last stood at 80.3%.



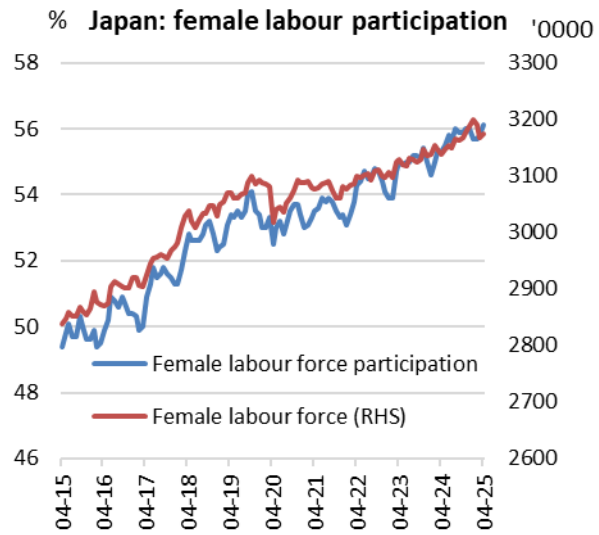
**items under core CPI basket (CPI less fresh food) whose price indices increased/decreased from a year ago.*
Source: Bank of Japan, OCBC Research.

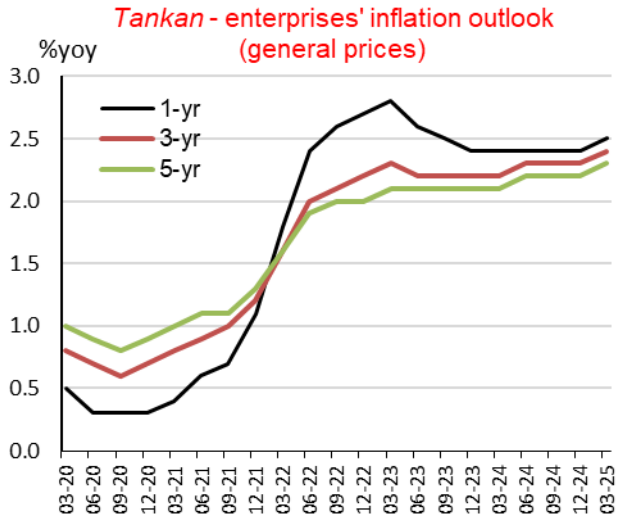
Firms' price-setting behaviour is a factor that impacts the price transmission mechanism. There have been signs that firms are prepared to pass or have passed on higher labour costs to selling prices and hence are relatively receptive to wage hike requests. The 2025 *Shunto* – spring wage negotiation led by Rengo (Japanese Trade Union Confederation) – has achieved an average wage growth of 5.32%. Meanwhile, according to *Tankan* surveys, enterprises' short-term (1-year), medium-term (3-year) and long-term (5-year) inflation expectations have stayed sustainably above the 2% level, and all edged higher by 0.1 percentage point in the latest survey.

Corporates have continued to see a shortage of labour supply. The diffusion index for employment conditions (excessive employment – insufficient employment) has mostly stayed as negative or turned a tad more negative under the latest March *Tankan* survey, compared to the December survey. Labour shortage has been reported as more severe in the non-manufacturing sector than the manufacturing sector.

Japan

The outlook for labour force participation has not changed much from our last assessment; further increases in the labour force participation of women and seniors – having advanced to a high degree thus far – are likely to be small. The female labour participation appears to be plateauing, which was last at 56.1% in April 2025, compared to the previous high of 56.0% in December 2024. BoJ opined that "upward pressure on wages and prices is likely to be stronger than suggested by the output gap", amid labour supply constraints





Source: Bloomberg, OCBC Research

Monetary policy normalisation to continue, slowly

Prospect for a virtuous cycle between wage growth and inflation continuing to play out, and hence for inflation to stay sustainably around the 2% target, will likely allow the Bank of Japan to continue with monetary policy normalisation, including the ongoing slow-paced QT and additional policy rate hikes. We expect the BoJ to stick with its plan to reduce JGB purchases, and our base-case is for one additional 25bp hike in 4Q25 and another 25bp hike in 1Q26 that will bring the BoJ Target Rate to 1.00%.

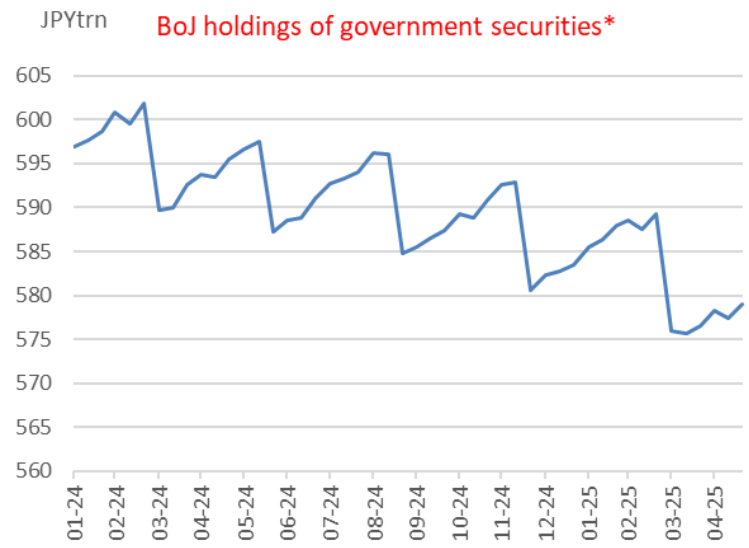
Interest rates forecasts	Q225	Q325	Q425	Q126
BoJ Target rate	0.50	0.50	0.75	1.00
JPY TONAR	0.48	0.48	0.73	0.98
1M JPY TIBOR	0.60	0.65	0.85	1.10
3M JPY TIBOR	0.77	0.70	0.95	1.20

BoJ kept its policy rate unchanged at 0.50% at the 30 Apr/1 May meeting as widely expected. The Summary of Opinions (the meeting minutes) highlighted "negative demand shocks are expected", and these include impact on business investment, household consumption, exports to the US and export profitability. Still, if the BoJ's outlook for economic activity and prices is realised, the BoJ "will continue to raise the policy interest rate and adjust the degree of monetary accommodation". The

Japan

BoJ's stance to continue to hike rates has been kept unchanged. We agree with this direction of monetary policy, for the reasons laid out above, and as real interest rates remain negative. That said, with high uncertainty around baseline outlook, the BoJ is unlikely to rush to hike rates. BoJ sees risk to the downside for both of their growth and inflation outlook, and it opined that "the likelihood of realising the outlook is not as high as before".

Another aspect of monetary normalisation is the reduction in the BoJ's balance sheet via lowering the holdings of government securities. QT has been ongoing for almost a year, at a slow pace. According to the plan set out in July 2024, BoJ's monthly JGB purchase is on a step-down schedule by the quarter – Apr-Jun monthly purchases are set at JPY4.1trn (April actual was JPY3.95trn), to be reduced to 3.7trn/3.3trn/ 2.9trn over the next three quarters. Our base-case is for BoJ to stick with this plan. Should the upward moves in long-end yields become more rapid, some shifts in allocation of reductions by remaining maturity cannot be ruled out.



**On BoJ balance sheet*
Source: Bloomberg, OCBC Research.

United Kingdom

United Kingdom: Moderating growth; gradual approach in BoE rate cuts

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Assisted by Miki Tan Wei Xi

- Economic growth is likely to moderate in the quarters ahead, as trade flows may slow after previous front-loading, and business investment plans may turn more cautious. Household consumption is likely to hold up. On balance, 2025 GDP growth is forecast at 1.0%.
- In consideration of the factors of energy price cap, potential tariff impact, and wage growth and potential pass-through, we expect YoY CPI inflation to ease from July onwards, and forecast 2025 CPI inflation at 2.7%.
- The inflation backdrop supports Bank of England's (BoE) gradual and careful approach in delivering additional rate cuts; the subdued growth outlook also justifies interest rates at less restrictive levels. Our base-case is for one 25bp cut in each of the remaining quarters of the year, which will then bring the Base Rate to 3.75%.

Growth to slow

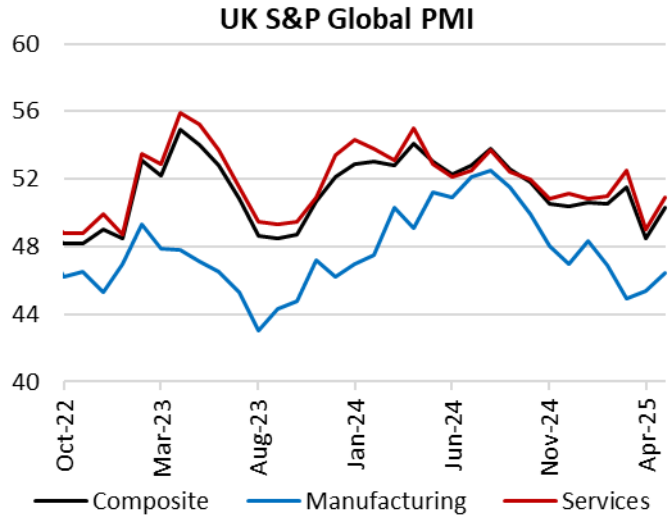
The UK economy grew by 0.7% QoQ sa in 1Q25, a significant improvement compared to the modest 0.1% QoQ sa in 4Q24 and virtually flat growth in 3Q24. In output terms, 1Q25 growth was driven by a 0.7% QoQ expansion in the services sector. Within the services sector, major contributors to growth were administrative & support services activities, and wholesale retail trade. Meanwhile, production also grew by 1.1% QoQ. In expenditure terms, 1Q25 growth was driven by gross fixed capital formation (GFCF), net trade and household consumption, in that order.

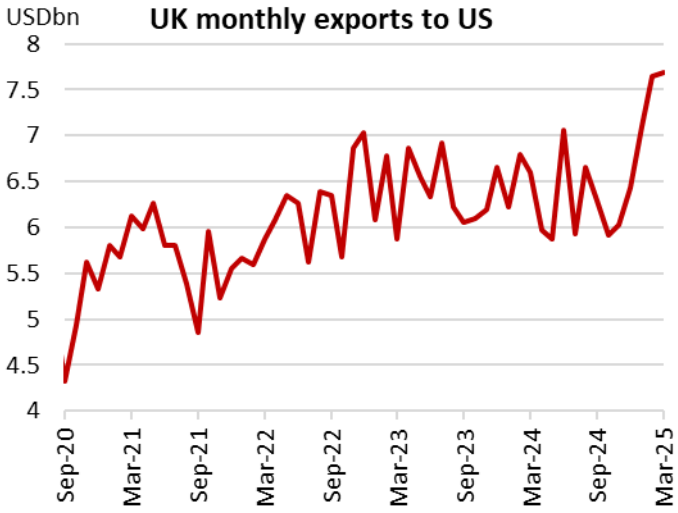
Growth is likely to moderate in the quarters ahead, as trade flows may slow after previous front-loading and the strong GFCF may not be repeated, while household consumption is likely to hold up providing some support to growth. Composite PMI dipped into contractionary territory in April and May, after staying in the expansionary zone for 17 consecutive months, which also reflect a dimmer outlook for economic activities. On balance, 2025 GDP growth is forecast at 1.0%.

External trade has probably benefited from front-loading flows ahead of anticipated tariffs. US was UK's largest export market for goods, accounting for 16.2% of total UK goods exports in 2024, with nearly half being machinery and transport equipment. Goods exports to the US were robust in 1Q25, growing by 16.4% YoY. This strong demand may however fade, as reflected by recent manufacturing PMIs – below the 50-mark for the eighth consecutive month in May, as firms scaled back production probably as client orders fell and in anticipation of weaker demand ahead; new orders stayed in the contractionary zone in May. Tariff uncertainty, government policy and global market turbulence were listed as factors underlying a further decrease in new export orders for May.

United Kingdom

The robust growth in GFCF in 1Q25 was partly supported by some big-ticket items in the transport sector (because of increased aircraft imports). There is uncertainty as to whether such growth will repeat. Business confidence has already weakened in 1Q25 as per surveys including PMIs, with the increases in NICs (National Insurance contributions) and uncertainty about its impact on the economy among respondents' primary concerns. Adding in the uncertainty on the external trade front, business investment may turn more cautious. For one, US is by far UK's biggest overseas market for cars; in 2024, UK exported GBP9bn worth of cars to the US, accounting for 27.4% of total UK car exports. On a more positive note, under the recent US-UK trade deal (US-UK Economic Prosperity Deal), for the first 100,000 vehicles imported to the US from UK car manufacturers each year, the tariff rate will be cut from 25% to 10%; the US also "intends to provide certain key UK imports with modified reciprocal tariff treatment", based on the balanced trading relationship between the two countries, and on national security priorities. These provide some support to industries including motor vehicle manufacturing.

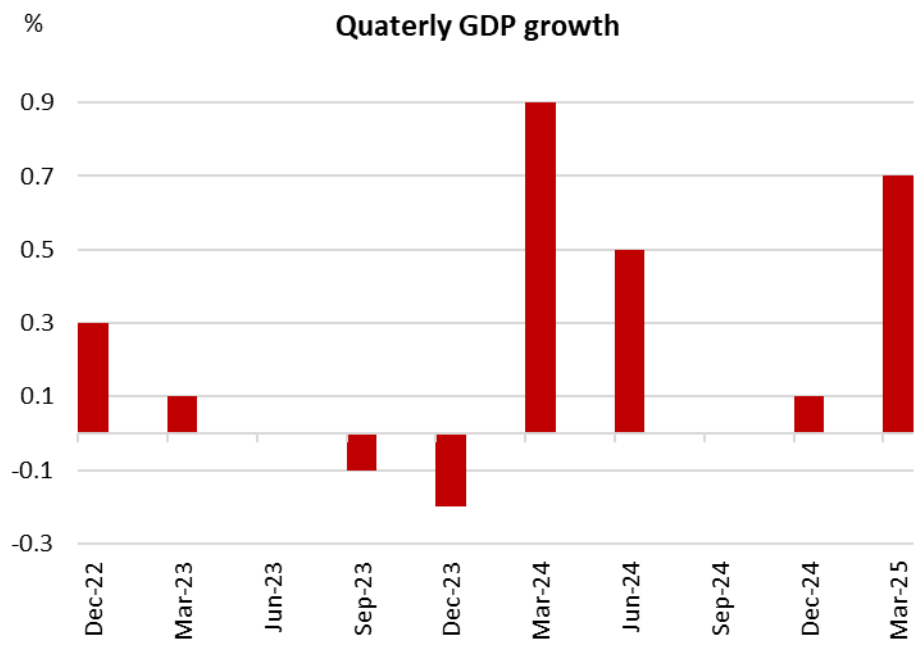




Source: Bloomberg, CEIC, OCBC Research

Household consumption is expected to hold up well, notwithstanding a loosening labour market, as wage growth is still likely to match (if not higher than) inflation while there is purchasing power to be released. Household consumption growth has lagged the increase in real household disposable income over the past quarters (since 2022), resulting in a higher household saving ratio, at 11.6% in 4Q24. We believe one of the main reasons for households to accumulate savings was the high interest rates, as the BoE embarked on the rate hiking cycle back in 2022 with cumulative 515bps of rate hikes. Now, after a total of 100bps of rate cuts by the BoE, interest rates are at a less restrictive level and prospects remain for additional rate cuts. Meanwhile, energy regulator Ofgem (Office of Gas and Electricity Markets) has announced reductions in the energy price cap by 7% for the July-September period compared to the April-June period. Counteracting these are higher taxes. On balance, some household spending power is likely to be released. April retail sales growth accelerated to 5.3% YoY versus 2.6% in March, sending a promising signal.

United Kingdom



Source: ONS, OCBC Research

Inflation

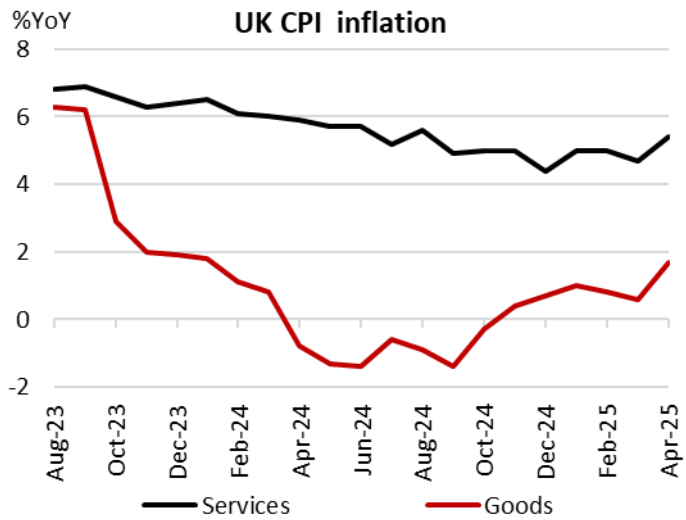
CPI inflation accelerated to 3.5% YoY in April, versus 2.6% YoY in March. Inflation had been expected to pick up materially mainly due to the higher energy price cap in 2Q25 compared to both 1Q25 and 2Q24, but the April outcome was still a tad higher than expected with some pick-up in contributions to inflation from transport, and recreation and culture categories. CPI including owner occupiers' housing (CPIH) rose by 4.1% YoY in April versus 3.4% YoY in March. In consideration of the factors of energy price cap, potential tariff impact, and wage growth and potential pass-through, we expect YoY CPI inflation to ease from July onwards and forecast 2025 CPI inflation at 2.7%.

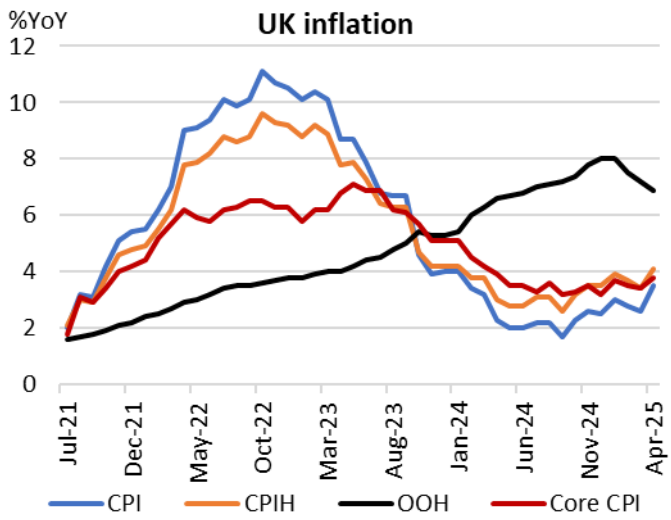
Energy price cap. Ofgem set energy price cap at GBP1849 for 2Q25, which was 6.4% higher than the GBP1738 set for 1Q25, and 9.4% higher than the GBP1690 set for 2Q24. The May and June readings of CPI inflation are likely to stay high reflecting the higher energy price cap. Beyond this, Ofgem has set the energy price cap lower at GBP1720 for 3Q25, mainly as wholesale price for energy have gone down, while lower supplier business costs have also helped. Changes in the energy price cap has been feeding through onto the price index for "housing, water, electricity, gas and other fuels" categories and affecting the consumer price index. Granted, the price cap is set every quarter; but the subdued global growth outlook renders a strong rebound in energy prices less likely for the forecast horizon of the remainder of this year.

Tariff impact. Net impact of tariff on inflation is somewhat ambiguous. On balance, BoE has judged that "higher tariffs will weigh slightly on UK inflation". BoE opined that the recent appreciation in the sterling effective exchange rate, weaker world activity and reduced US demand for imports are expected to weigh on CPI inflation.

United Kingdom

Wage growth. Upside to inflation may come from wage growth and potential pass-through onto consumer prices. The 6.7% increase in the NLW (National Living Wage) which started in April and higher NICs for employers may lead companies to pass on higher labour costs for consumers. But a likely small margin of excess supply may limit such pass-through.



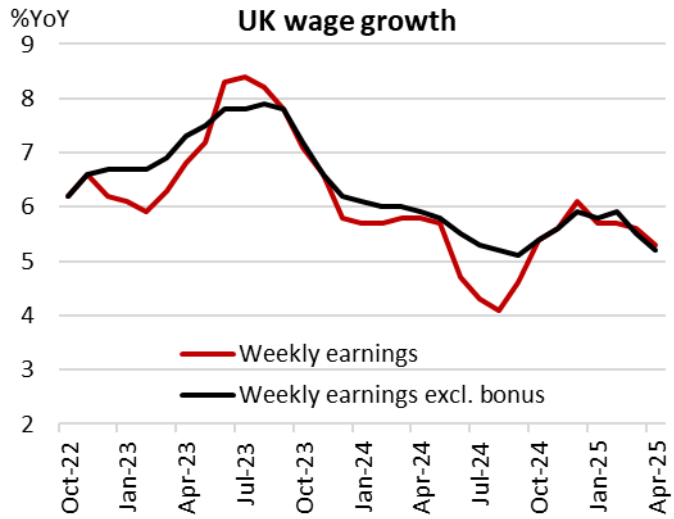


Source: Bloomberg, OCBC Research

A loosening labour market

The labour market has continued to loosen, with estimates for payrolled employees having decreased by 0.2% MoM and 0.4% YoY in April. Job vacancies have been falling since May 2022, and the ratio of job vacancies to unemployed fell further to 0.46 in April. BoE's model suggests that "underlying three-month on three-month employment growth softened to around 0% at the start of 2025", which was below estimated population growth. In addition to the subdued economic growth outlook, the recent increase in NLW and employer NICs may render firms yet more cautious in their employment plans. Wage growth has also slowed, with growth in employee's average regular earnings excluding bonuses having eased to 5.2% YoY and total earnings including bonuses to 5.3% YoY in the February-April period - still elevated but showing a downward trend. While the 6.7% rise in the NLW *per se* is expected to push up annual wage growth somewhat, the increase in employer NICs may lead firms to contain pay increase to partly offset the impact on their costs. Overall, wage growth is likely to remain decent but is projected to slow.

United Kingdom

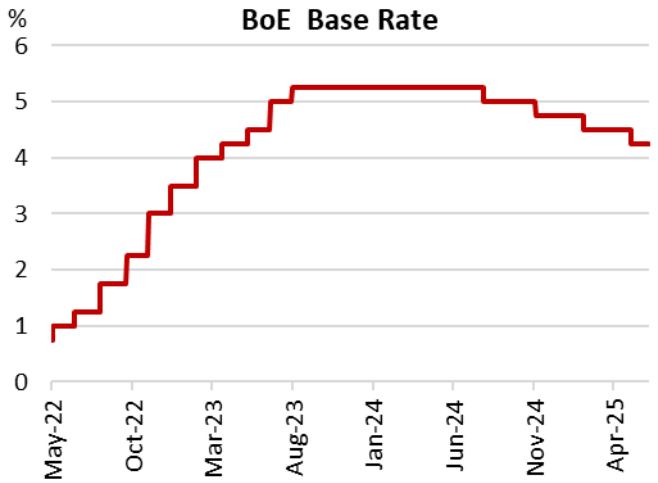


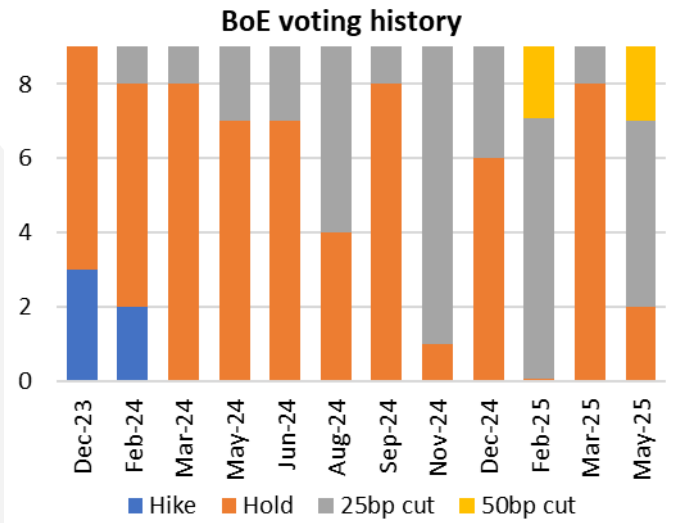
Source: ONS, Bloomberg, OCBC Research

A gradual and careful approach to interest rate cuts

BoE cut its policy Base Rate by 25bps to 4.25% at its 7 May meeting, by three-way split votes – with 5 members voting for the 25bp cut, two members for a 50bp cut and two members for a hold. BoE judged that underlying GDP growth have slowed since mid-2024 and the labour market has continued to loosen. Progress on disinflation in domestic price and wage pressure is generally continuing. The central bank reiterated that monetary policy is not on a pre-set path and risks to inflation are in both directions.

The inflation backdrop supports BoE's gradual and careful approach in delivering additional rate cuts, in our view. The subdued growth outlook also justifies interest rates at less restrictive levels. Market has recently added to rate cut expectation pricing additional 51bps by year-end, in line with our base-case remains for one 25bp cut in each of the remaining quarter of the year, i.e. 50bps of additional rate cuts for the rest of the year which will then bring the Base Rate to 3.75%.





Source: Bank of England, Bloomberg, OCBC Research

United States

United States: Short Term Gain, Long Term Pain

Tommy Xie
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- Corporates' reluctance to invest amid heightened uncertainty may weigh on growth. However, unlike the 2008 crisis, the U.S. household sector is not facing structural imbalances. The job market is still holding up well for now. There is little evidence so far of a sustained shift in inflation expectations.
- On fiscal side, the "One, Big, Beautiful Bill" if passed by the Senate may support near-term growth, they are also expected to widen deficits and add to long-term debt pressures, potentially raising the terminal rate of interest over time.
- Recession risk is not part of our baseline scenario, although elevated vigilance is warranted amid a volatile policy environment.

The economy contracted by 0.2% QoQ seasonally adjusted in 1Q25, a sharp reversal from the 2.4% expansion in 4Q24. The contraction was primarily driven by a surge in imports, which spiked 41.3% QoQ (vs. -1.9% in 4Q24), reflecting frontloading activity by businesses and consumers ahead of anticipated tariff hikes. Government spending also declined by 0.7% QoQ, mainly due to a 7.1% drop in defense expenditures.

The main driver of growth in 1Q25 was private investment, which surged 24.4% QoQ, recovering from a 5.6% contraction in the previous quarter. This strength was largely due to frontloaded equipment purchases (+24.8% QoQ), as firms rushed to beat tariff implementation timelines. Private consumption rose by 1.2% QoQ, easing from 4.0% in 4Q24.

The early suspension of the reciprocal tariff by the Trump Administration came as a positive surprise, helping to reduce near-term recession risk. However, the Administration's decision to retain a 10% universal tariff keeps the effective U.S. tariff rate at its highest level since the 1930s. Ongoing trade uncertainty will likely continue to weigh on growth, even as recent easing in financial conditions has lifted market sentiment.

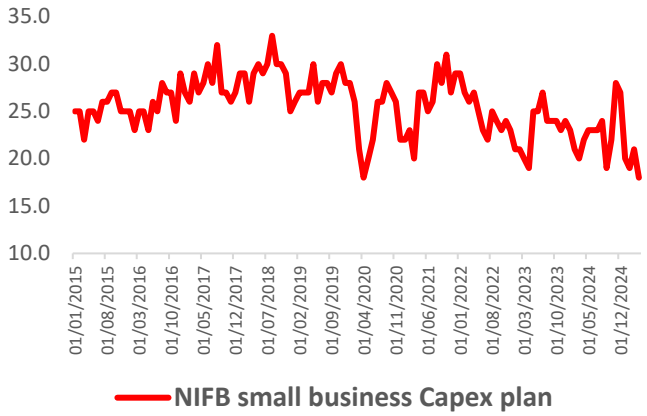
Capital expenditure was one of the few bright spots in 1Q25, but forward-looking indicators suggest caution ahead. Both the NFIB Small Business Capex Plans Index and the Empire State Manufacturing Survey's six-month-ahead capex intentions fell to levels last seen during the onset of the COVID-19 pandemic, reflecting a growing reluctance to invest amid heightened uncertainty.

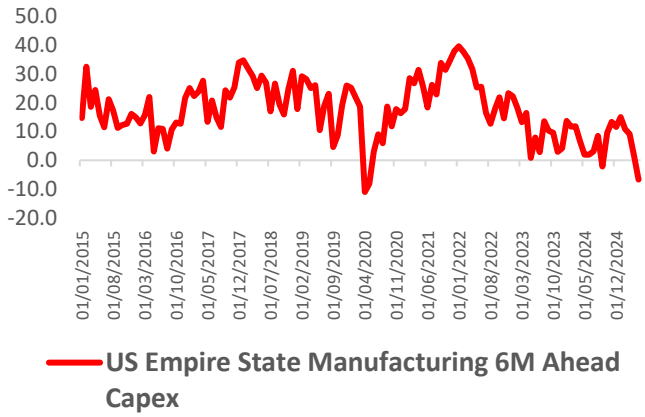
Despite mounting concerns about a potential recession, we maintain that the risk of a downturn over the next two years remains low. Unlike the 2008 crisis, the U.S. household sector is not facing structural imbalances. Following significant deleveraging since the Global Financial Crisis, household balance sheets remain relatively healthy. Therefore, a recession is not part of our base case.

Chart 1: Small business turned more cautious on capex plan

Chart 2: Capex plan under the US Empire State Manufacturing also fell

United States

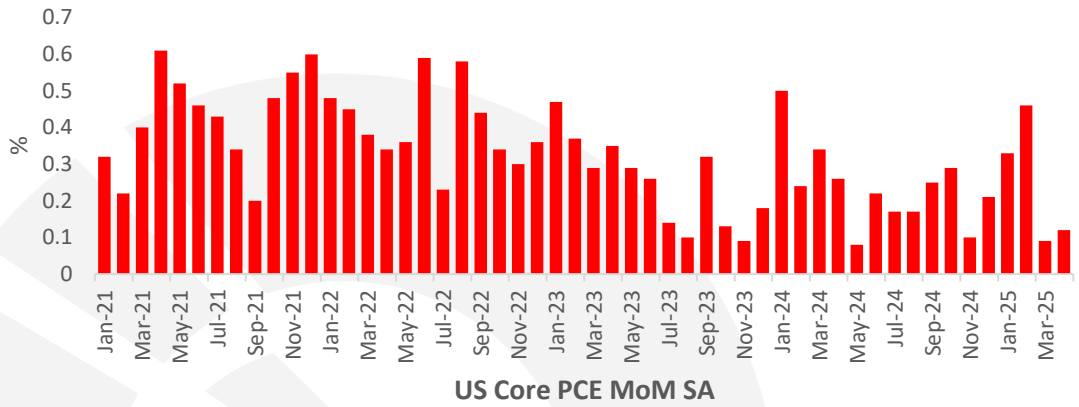




On the labor market front, conditions remain resilient for now. Nonfarm payrolls rose by 139,000 in May, exceeding consensus expectations of 126,000. Job gains were led by leisure and hospitality (+38k) and financial services (+20k), despite the Fed's Beige Book noting weakness in these sectors. The unemployment rate edged up to 4.24% from 4.19% in April, marking the fourth consecutive monthly increase and the highest level since October 2021. This gradual upward trend has also been reflected in rising continuing jobless claims.

Inflationary pressures continue to ease. Headline CPI rose 2.3% YoY in April, down from 2.4% in March. On a monthly basis, CPI rebounded by 0.2% after a 0.1% decline in March. Core inflation also remained subdued. The Personal Consumption Expenditures (PCE) Price Index rose by 0.1% MoM in April, led by modest increases in both goods and services prices. On a YoY basis, PCE inflation eased to 2.1% from 2.3%, supporting the ongoing disinflation narrative.

Chart 3: The sequential growth of core PCE has softened, creating room for policy normalization.



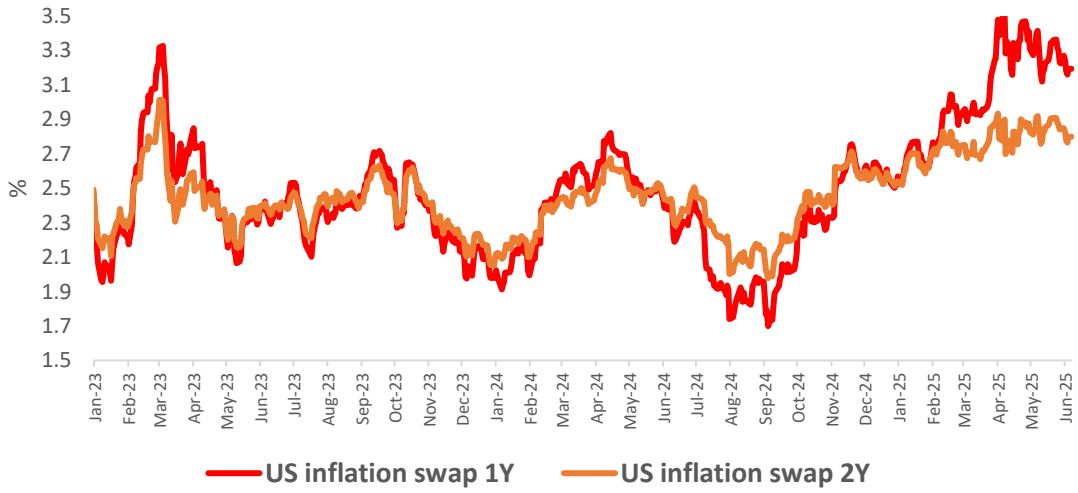
Given the weakening growth momentum and benign inflation backdrop, our rates strategist continues to expect three Fed rate cuts in 2025 to facilitate further policy normalization. The key risk to this outlook remains the potential inflationary shock from new tariff measures. However, there is little evidence so far of a sustained shift in inflation expectations. While the University of Michigan survey showed a spike in 5-year inflation expectations to 4.6% in May—the highest since 1991—we

United States

caution against overinterpreting such survey data, which may be distorted by political polarization and/or fickle headline-driven sentiments.

Instead, we place greater emphasis on market-based indicators. The 1-year CPI swap currently prices in inflation at 3.2%, suggesting a near-term bump. However, the 2-year CPI swap has eased to 2.8%, indicating limited passthrough into medium-term expectations. Notably, the divergence between the two measures only emerged after the announcement of the "Liberation Day" tariffs in early April, suggesting markets still view the inflation shock as temporary.

Chart 4: The gap between 1Y CPI Swap and 2Y CPI Swap has widened since early April.



On the fiscal front, efforts by Elon Musk's Department of Government Efficiency (DOGE) to cut federal spending by USD1trn have fallen well short, contributing to renewed volatility in the U.S. Treasury market. This was exacerbated by Moody's downgrade of U.S. sovereign ratings, highlighting concerns that a ~6% federal budget deficit may become a structural feature of the U.S. fiscal landscape.

Further complicating the outlook is the narrow House passage (215–214) of the "One, Big, Beautiful Bill" on May 22. The bill—now headed to the Senate—proposes to make the 2017 Trump tax cuts permanent, introduce new tax relief on tips and overtime, increase defense and border security spending, and raise the debt ceiling. While these measures may support near-term growth, they are also expected to widen deficits and add to long-term debt pressures, potentially raising the terminal rate of interest over time. **Please refer to our thematic report for detailed analysis of the bill.**

In summary, the U.S. economy remains on a fragile recovery path, supported by easing financial conditions, a resilient household sector, and short-term fiscal stimulus. Despite ongoing trade-related uncertainty and political risks, we maintain our full-year GDP growth forecast at 1.3%. Recession risk is not part of our baseline scenario, although elevated vigilance is warranted amid a volatile policy environment.

China

China: Bottleneck to Reflate the Economy

Tommy Xie
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- The recent 90-day trade truce is expected to mitigate downside risks to the near-term growth outlook. We now forecast 2Q25 GDP to remain above 5% YoY.
- In response to rising global uncertainties, fiscal policy has taken a more prominent role. However, monetary policy hit its bottleneck in an effort to reflate the economy. The property market is set to play a central role in China's efforts to boost domestic demand in 2025.
- Given the still-uncertain trade outlook and the sluggish recovery in the property sector, we maintain our full-year GDP forecast at 4.6% YoY, with fiscal and monetary easing measures likely to cap further downside risks.

Key economic indicators for March and 1Q25 exceeded market expectations, signalling a stronger-than-anticipated start to the year. The economy expanded by 5.4% YoY in 1Q25, holding steady from 4Q24. The stronger-than-expected performance in 1Q25 can be attributed to four main drivers including support from the front-loading activities, high-tech manufacturing, policy support from the consumer trade in program and accelerating infrastructure investment.

Chart 1: Net export remained the key driver to China's growth in the first quarter

Despite the strong 1Q25 data, headwinds are gathering. The intensification of U.S.-China trade tensions, particularly the reciprocal tariff hikes taking effect in April, is expected to weigh on China's exports and overall sentiment. The unexpected pause in reciprocal tariffs in early May and the rollback of earlier tit-for-tat measures shows China's "escalate to deescalate" strategy pays off.

That said, this de-escalation does not equate to a full return to normalcy. President Trump had a 90-minute phone call with President Xi in early June regarding the trade talk. The call helped pull back the fragile trade truce between the U.S. and China from the brink of collapse, with both leaders agreeing to restart trade negotiations that had stalled amid accusations of non-compliance with prior commitments.

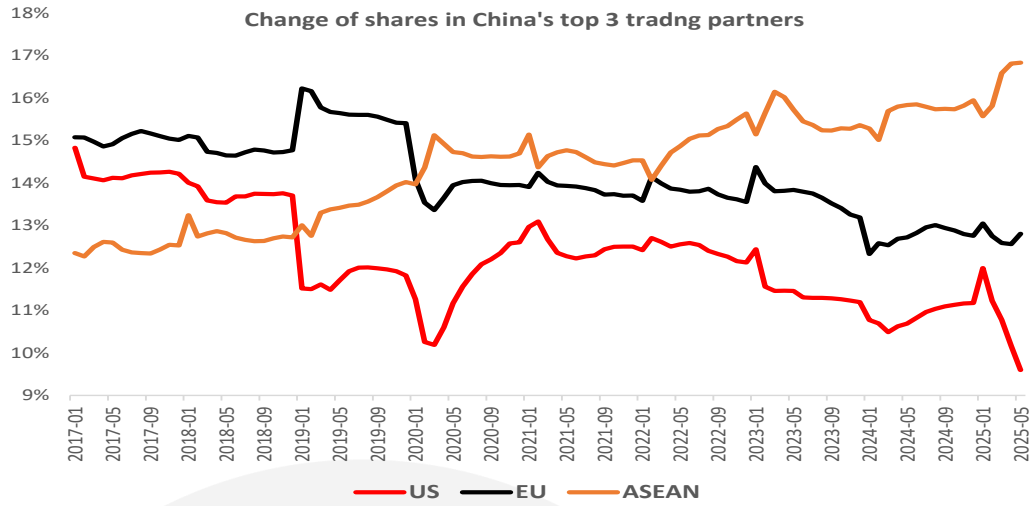
China

Over next one to two months, the trajectory of trade relations will largely depend on two factors: (1) the progress of direct U.S.-China negotiations. The US signalled a willingness to remove restrictions on some tech exports in exchange for assurances that China is easing limits on rare earth shipments. (2) how both sides engage third-party countries and trade blocs through broader consultations and coalition-building.

From China's perspective, the strategic response will likely include continued efforts to reduce reliance on the U.S. export market—via both supply chain restructuring and third-country transshipment routes in the short to medium term. Moreover, the temporary truce is unlikely to deter China's longer-term export market diversification strategy.

China's exports showed surprising resilience in April, with total outbound shipments rising by 8.1% YoY, despite a sharp escalation in trade tensions with the United States. Nevertheless, China's export growth slowed to 4.8% YoY in May. The sharpest drag came from exports to the United States, which contracted by 34.5% YoY, from -21.0% in April.

Chart 2: The share of China's exports to US in total export has fallen below 10%.



While there were signs of frontloading activity in the first half of May following the temporary trade truce, momentum faded by late May, indicating that the boost from early shipments has largely been exhausted. Recent shipping data suggests that export activity stabilized in early June, with a modest rebound recorded in the first week. Looking ahead, we believe the tariff-related shock is largely priced in, and the trajectory of China's exports will increasingly hinge on underlying demand fundamentals rather than temporary policy noise.

Regarding US-China trade talk, as of 12 June, what has been confirmed by both sides is that a framework agreement to ease export controls has been reached, marking a modest but notable step toward de-escalation. As U.S. Commerce Secretary Lutnick put it, the deal "puts meat on the bones" of the consensus reached last month in Geneva. But the key question remains: what kind of "meat" is on the table? While details remain limited, it appears both sides are preparing for

China

partial compromises, with the U.S. expected to relax certain technology export controls in exchange for China's conditional easing of rare earth export restrictions.

Nevertheless, it seems that China's push for the removal of the 20% fentanyl-related tariff remains unsuccessful. The next thing to watch is whether this agreement leads to an extension of the current 90-day trade truce, providing a more stable window for further negotiations.

While the negotiations have not resolved the underlying trade frictions, the framework agreement acts as a "pressure release valve" in U.S.-China economic relations. It lowers the immediate risk of further escalation and creates space for broader discussions on more contentious issues, including tariffs and strategic decoupling.

In response to rising global uncertainties, fiscal policy has taken a more prominent role, with the fiscal deficit target this year raised to 4% of GDP from the usual 3%. The budgeted fiscal deficit will increase by CNY1.6trn to CNY5.66trn, primarily due to a CNY1.2trn increase in fiscal expenditures, which are set to reach CNY29.7trn.

To further stimulate growth, the quota for ultra-long-term special treasury bonds has been increased by CNY300bn to CNY1.3tn, while a CNY500bn special bond issuance is planned to recapitalize major state banks. Additionally, local government special bond issuance will rise by CNY500bn to CNY4.4trn. In total, central and local governments will issue CNY11.86trn in debt in 2025, a YoY increase of CNY2.9trn—underscoring a more proactive fiscal stance to offset external headwinds.

In addition to proactive fiscal policy, China unveiled a comprehensive package of policy supports in early May covering a wide range of areas including monetary, housing, capital market support as well as fresh initiatives targeting technology, consumption, and trade. This reinforces that China's top policymakers are placing greater emphasis on sentiment management, recognizing its role in fostering market confidence and policy effectiveness. The 2025 Government Work Report explicitly highlights the importance of incorporating market feedback into policy implementation and aligning expectations to cultivate positive social sentiment.

Since September 2024, the narrative surrounding China's equity market has shifted from "uninvestable" to "tradeable", and now in 2025, to "investable"—thanks to the DeepSeek moment and the private sector symposium between President Xi and China's top private entrepreneurs.

On monetary policy, given CPI remained low in the negative territory, monetary easing remains necessary. However, monetary policy also hit its bottleneck. In its 1Q25 Monetary Policy Report, the PBoC offered valuable insight into the structural nature of China's low inflation. It noted that the effectiveness of monetary policy in influencing prices depends on the balance between supply and demand. In the context of an investment-led growth model focused on supply-side security, monetary easing may increase production capacity without boosting demand,

China

thereby exacerbating supply-demand imbalances and making inflation harder to revive.

The report emphasizes that the key to restoring price momentum lies in expanding effective demand, resolving bottlenecks in the real economy, and improving the supply-demand circulation. This requires deepened structural reforms supported by coordinated fiscal, monetary, industrial, employment, and social security policies. Now, we expect PBoC to lower its benchmark interest rate by another 20bps this year although the room for more aggressive rate cuts may be limited given the bottleneck faced by the economy.

The property market is set to play a central role in efforts to boost domestic demand in 2025. While debates continue over the root cause of the economic downturn, there is growing consensus that the deep adjustment in the property sector is the root cause. The 2025 Government Work Report explicitly states that sustained efforts are needed to stabilize the real estate market and prevent further declines.

As China transitions toward a new real estate development model, policymakers prioritize measures to prevent developer debt defaults, ensuring financial stability within the sector. In February, Guangdong Province announced a RMB30.7bn special bond issuance for land acquisition and storage—the first large-scale initiative of its kind. This approach is expected to be replicated nationwide, signalling stronger fiscal support for the sector.

Given these policy shifts, stabilizing the property market will be a major focus in 2025, serving as a critical lever to support domestic demand and restore confidence in the broader economy.

Beyond conventional fiscal and monetary support, we believe China retains ample policy tools to stabilize growth. Among them, new-type urbanization is likely to emerge as a key strategic focus in the coming year. This initiative seeks to address hukou-related barriers faced by migrant workers, enabling them to purchase homes and access public services in urban centers. If effectively implemented, these reforms could generate a "threefold benefit": enhancing social equity, unlocking housing demand by absorbing excess inventory, and stimulating consumption as migrant workers integrate more fully into urban life.

Meanwhile, the recent 90-day trade truce is expected to mitigate downside risks to China's near-term growth outlook. We now forecast 2Q25 GDP to remain above 5% YoY, supported by external stability and policy tailwinds. That said, given the still-uncertain trade outlook and the sluggish recovery in the property sector, we maintain our full-year GDP forecast at 4.6% YoY, with fiscal and monetary easing measures likely to cap further downside risks.

Hong Kong

Hong Kong: Cautious optimism

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- Our full-year GDP growth forecast for 2025 is revised up back to 2.2% YoY, albeit still erring on the low side of the government forecast range at 2%-3%. The labour market is expected to soften further, while the inflation outlook hinges on the strength of domestic demand and external prices pressures. We tip the 2025 unemployment rate and inflation forecast at 3.4% and 1.7% YoY respectively.
- HKD rates stayed low now amid the flush liquidity but should the weak-side convertibility undertaking be triggered, any reversal in HKD rates move can be rapid and forceful. We expect the 3-month HIBOR can potentially normalise back to the 2.5-3.0% area, but the timing is highly uncertain. Separately, we expect the local banks to slash the prime rate further by 25bps in the 3Q25, following the expected Fed's decision to resume rate cuts.
- We expect the residential property price index to stay largely flat in 2025, on the back of narrowing buy-rent gap, further cut in prime rate, together with increases in non-local and end-user demand. In view of the negative carry, we still hold on to a bearish view on the commercial real estate market. The property prices of retail spaces and office are expected to fall further by around 5%-10% this year.

Drag is not as significant as initially feared

The heightened growth and policy uncertainties, together with the unclear trajectory of US inflation and Federal Reserve policy rate cuts, are expected to hinder the recovery of consumer spending, business capital expenditure and loan demand in early 2025. However, while we do see some soft patches in data, the drags were not as significant as initially feared. External demand continued to hold up, while positive wealth effects stemming from asset market rallies contributed to stabilizing market sentiment. Additionally, green shoots are emerging from multiple fronts. Earlier-than-expected US-China trade truce, robust performance in the asset market, and the implementation of accommodative fiscal and monetary policies in Mainland China have all served as tailwinds for HK's economic momentum. Meanwhile, we saw some fund repatriation/inflows on the back of the de-dollarisation and asset diversification trends. The situation warrants cautious optimism regarding the outlook for the remainder of the year, despite ongoing challenges.

Chart 1: Solid start to the year on export boom

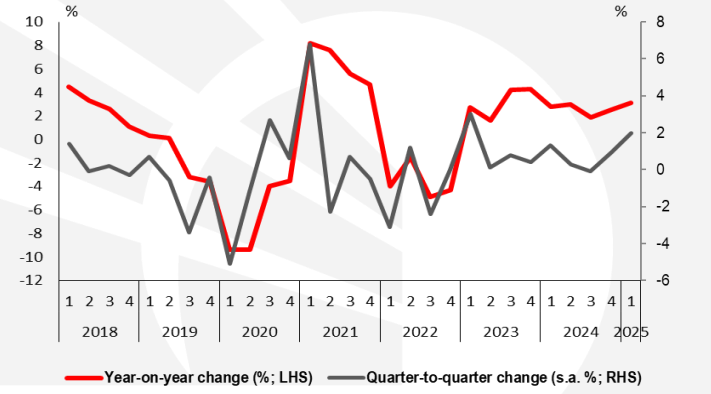
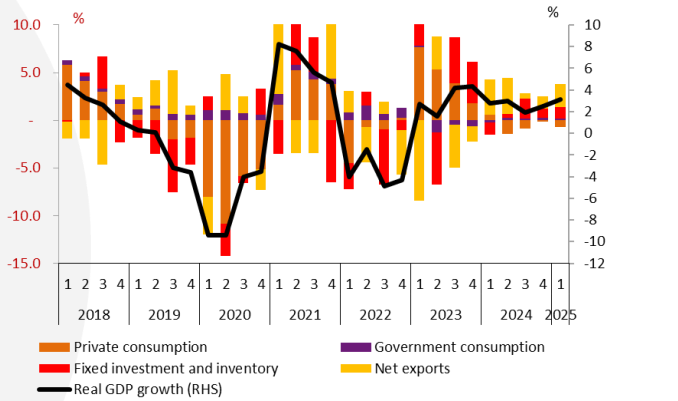


Chart 2: Private consumption contracted further



Hong Kong

Solid start to the year on export boom

The economy demonstrated remarkable resilience in the midst of tariff uncertainties and slowdown in global growth, with real GDP growth accelerating to 3.1% YoY in the first quarter of 2025 **(Chart 1)**, from an upwardly revised 2.5% YoY in 4Q24, on the back of goods and service export boom. On a seasonally adjusted basis, the economy grew by 2.0% QoQ (4Q24: 0.9% QoQ). During 1Q25, private consumption expenditure contracted by a faster pace of 1.2% YoY (4Q24: -0.2%) **(Chart 2)**, yet it was offset by brisk pace of expansion in other components of GDP. Growth in goods and service exports paced up to 8.7% YoY and 6.6% YoY respectively (4Q24: 1.3% YoY and 6.5% YoY), with the former due to front-loading of exports ahead of US' tariff implementation. Meanwhile, gross domestic fixed capital formation reverted to growth, increasing by 2.8% YoY (4Q24: -0.7% YoY). Growth in government consumption however slowed to 1.2% YoY (4Q24: 2.1% YoY).

Near-term outlook is still challenging

Despite the resilient performance in 1Q25, the near-term challenges are not to be overlooked. HK's trade performance is expected to weaken in periods ahead, due to the high base effect and fading export front-loading. The unemployment rate ticked up again, posing further drag on domestic demand. We expect to see soft patches in economic data in coming quarters, but a recession is not our baseline scenario. Our full-year GDP growth forecast for 2025 is revised up back to 2.2% YoY, albeit still erring on the low side of the government forecast range at 2%-3%. HK's labour market is expected to soften further, as the tariff war and changing consumption patterns will have negative bearings on selected sectors. The inflation outlook hinges on the strength of domestic demand and external prices pressure. We tip the 2025 unemployment rate and inflation forecast at 3.4% and 1.7% YoY respectively.

Casualty of tariff war and other weak spots

Thanks to the export front-loading demand, HK's merchandise exports still grew by 11.9% YoY in the first four months this year **(Chart 3)**. However, the casualty of trade war is starting to show lately. In April, as US and China engaged in tit-for-tat tariff battle, exports to US rose at a much slower pace of 1.0% YoY. Based on a set of assumptions and rough calculation, the direct total value added affected by US' tariff (i.e. domestic exports to US) is around HK$510 million, which translates to only around 0.02% of HK's GDP. Nonetheless, as a trading and transhipment centre, HK's re-exports will also be adversely affected by tariff-related trade disruptions in the region. Exporters and companies highly reliant on re-export trades will be directly impacted. Reduction of trade volumes will also negatively affect the trade financing business.

In parallel, the economy continues to suffer from the slow burn of weak consumption sentiment. HK's retail sales fell further by 5.6% YoY in value terms in the first four months this year **(Chart 4)**, albeit moderating from the decline of 6.7% YoY in 4Q24. If positive wealth effects stemming from asset market rallies are sustained, retail sales are expected to stabilize somewhat in the next couple of months. Otherwise, we expect retail sales to stay fairly weak and record a mid-single-digit decline for the full year.

Hong Kong

While we did not see signs of recovery in loan demand so far this year, its year-on-year decline nonetheless moderated on a lower basis of comparison **(Chart 5)**. Looking ahead, the drop in HIBOR and looser monetary conditions should render some support to loan demand this year. Total loans and advances are expected to see positive growth YoY? by mid- to late 2025.

Chart 3: Merchandise exports held up in 1Q

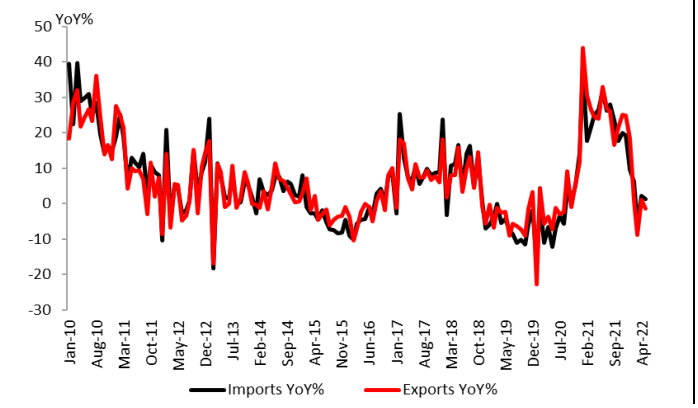
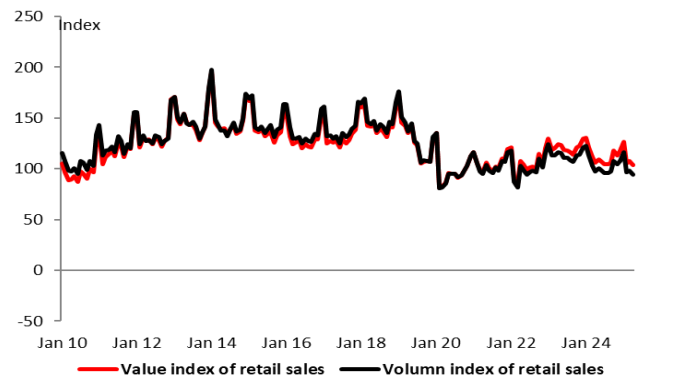


Chart 4: Retail sales still weak



Signs of cooling in labour market

HK's labour market showed signs of broad weakening, as unemployment rate before seasonal adjustment rose across sectors. The unemployment rate went up by 0.4 percentage point, from 3.0% in December 2024 to 3.4% in April 2025, while the total unemployed persons rose to the highest level since 4Q22 (at 129.4k) **(Chart 6)**. During the same period, the underemployment rate rose by a milder extent of 0.2 percentage point to 1.3%. Anecdotal evidence suggested that hiring sentiment continued to worsen. To reflect the cyclical pain ahead, we revised the full-year unemployment rate forecast higher to 3.4%, from the previous 3.1%, with weakness seen in accommodation services sector, food and beverage service activities sectors.

Chart 5: Decline in loan demand moderated

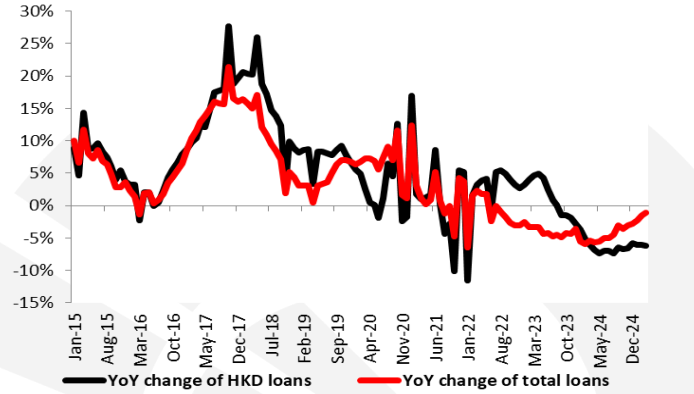
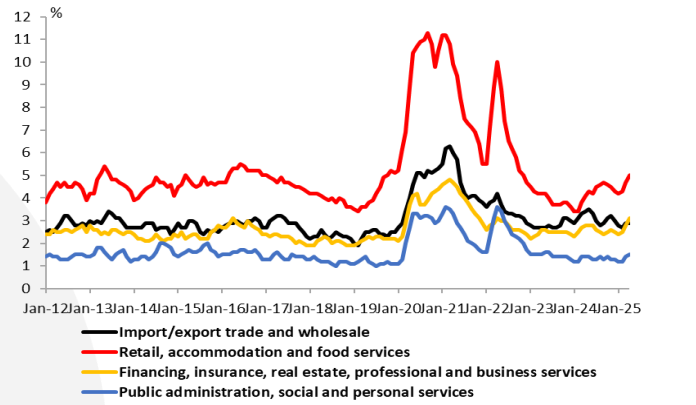


Chart 6: Signs of cooling in labour market



Hong Kong

Staying low now but normalization inevitable

The HKMA sold a total of HKD129.4 billion HKD to the market since 2 May, as the strong-side Convertibility Undertaking was repeatedly triggered. Correspondingly, the aggregate balance rose to HKD174.1bn, which offer liquidity buffer to IPOs, dividend payout activities, meanwhile the moderation of southbound inflow and the smaller-than-expected scale of IPO activities also left HKD liquidity at the loose side. HIBORs plunged across the board as a result, in particular for those at front-end.

While the wide USD-HKD rates differentials encourage carry trades, there is high uncertainty as to how long it takes to push spot USDHKD to 7.8500 level. That said, as and when it happens, any reversal in HKD rates move can be rapid and forceful. Apart from weak side convertibility undertaking being triggered, potential factors leading to higher HIBORs and short-end HKD rates include additional dividend payout activities, return of equity inflows, and recovery in HKD loan demand. We expect 3-month HIBOR can potentially normalise back to the 2.5-3.0% area, but the timing is highly uncertain.

The HKMA is rather reluctant to mop up the liquidity, though it has flagged the potential rebound in HKD interest rates. Separately, we expect the local banks to slash the prime rate further by 25bps in 3Q25, following the potential for Fed to resume rate cuts. This will likely bring the HKD prime rate cut cycle to an end, after returning to the long-term level before the 2022 Fed rate hike cycle.

From "investable" to "unmissable"?

The narrative surrounding the stock market shifted from "investable" to "unmissable" this year, as AI and technological breakthrough revived investors' interest, and the equity market recorded another quarter of stellar performance. Hang Seng Index's 18.6% (as of 6 June 2025) year-to-date gain outshined other major global indices **(Chart 7)**. Separately, issuers are capturing the window of opportunity, as policy setting turns more favourable and market sentiment improves alongside higher IPO subscription rate and better post-IPO performances. With a few blockbuster IPOs this year, a total of HKD78bn was raised by May this year, marking a sevenfold increase over 2024 figure. Listings are expected to grow further in coming quarters, given the solid pipeline.

Chart 7: IPO re-exuberance

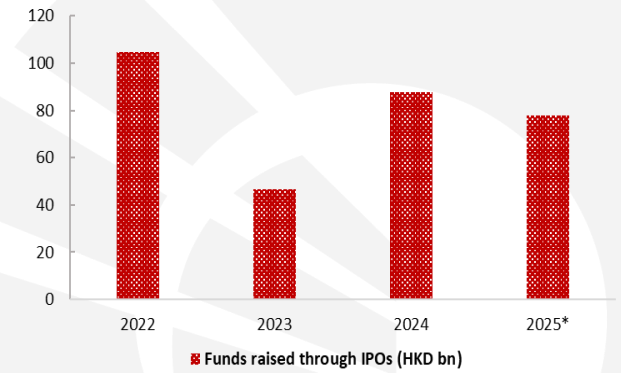
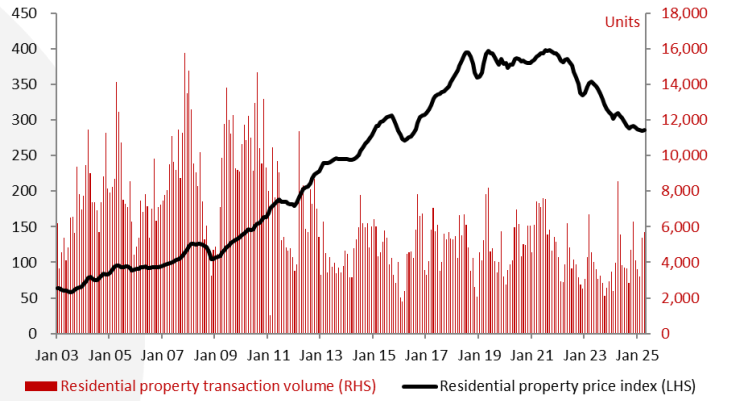


Chart 8: Housing market showed signs of stabilisation



Sources: HK Rating and Valuation Department, Land Registry, HKEX, Blomberg, OCBC.
(*) Data for the first five months of 2025.

Hong Kong

Narrowing buy-rent gap

The housing market is showing tentative signs of stabilisation. Housing prices ended the four-month losing streak in April (+0.4% MoM), narrowing the year-to-date loss to 1.2% **(Chart 8)**. Meanwhile, rents extended its recent rally and rose cumulatively by 0.6% in the first four months of 2025. The average rental yield rose to 2.94% in April 2025, and correspondingly our in-house estimate of buy-rent gap fell to 0.12% **(Chart 9)**. Judging by the current trend, it will soon cost less to own a residential property than renting one.

On the other hand, increased scrutiny over public housing tenants created extra end-user demand. We expect the residential property price index to stay largely flat in 2025, on the back of a narrowing buy-rent gap, likely further cut in the prime rate, together with increases in non-local and end-user demand. In view of the negative carry, we still hold on to a bearish view on the commercial real estate market. The property prices of retail spaces and office are expected to fall further by around 5%-10% this year.

There were no sparks on land and property market policies in this year's budget, after removing all demand-side measures last year. The Hong Kong government raised the maximum of properties chargeable to a nominal stamp duty of HK$100 from HK$3mn to HK$4mn, benefiting 15% of total property transactions. Since then, we have noticed a modest increase in trading activities in both primary and secondary markets, the former due to increase in launches of primary projects. Trading activities also increased to five-month high of 5,694 cases in April.

Inflationary pressure is still tamed

Price pressure is likely to stay tamed, with deflationary pressure from the Mainland China spreading to and manifesting in HK. Prices of basic food (majority of them sourced from Mainland) hovered at the lowest level since mid-2023. Meanwhile, housing inflation picked up somewhat to 1.9%, partly due to end of rate concession. In the first four months this year, composite CPI rose by an average 1.7% YoY, while underlying CPI (netting out the effect of government one-off relief measures) rose by a milder 1.3% YoY **(Chart 10)**. In view of the still-sluggish domestic demand, and limited impact from tariff imposition, we revised down the full-year inflation forecast to 1.7% YoY, from the earlier estimate of 2.0%.

Chart 9: Narrowing buy-rent gap

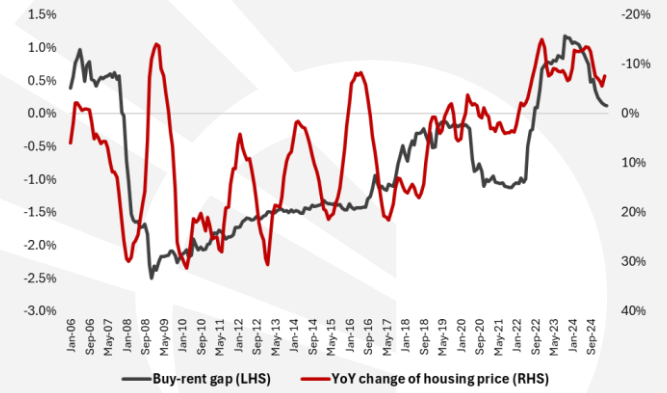
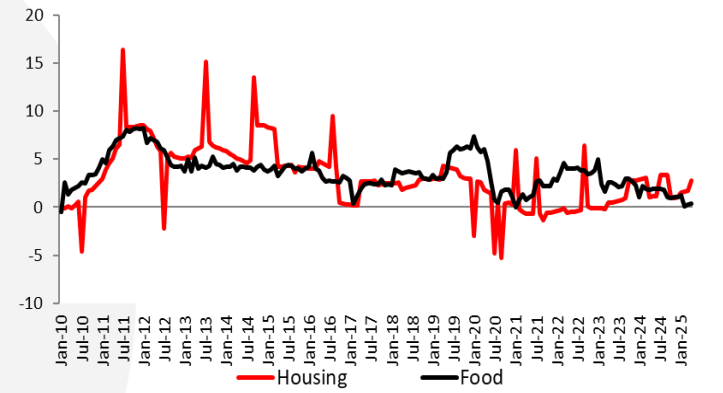


Chart 10: Inflationary pressure still tamed



India

India: Rising to the challenge

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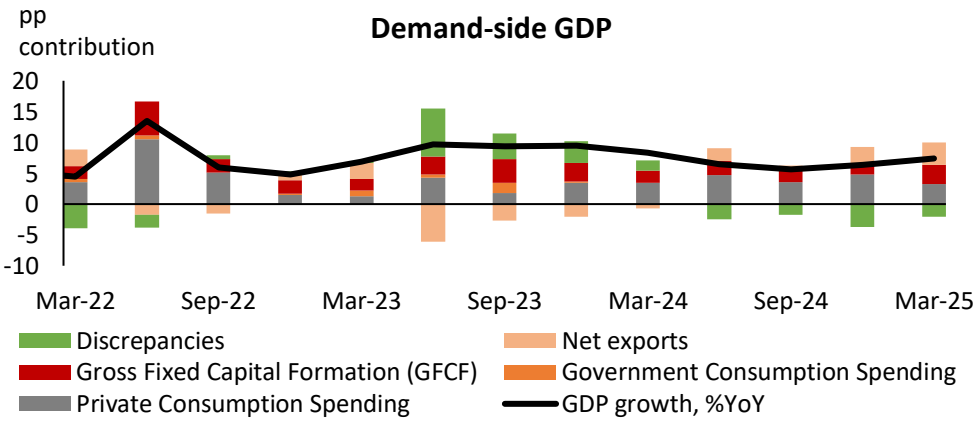
- We expect GDP growth of 6.0% in FY26 (i.e., April 2025 until March 2026) compared to 6.5% in FY25. Although India is more resilient to tariff troubles compared to most other economies in the region, it is not immune.
- The channels of impact to growth will likely be investment spending and exports, which we expect will moderate in FY26 compared to FY25. We, do, however, expect private consumption to stabilise into the second half of the FY as rate cuts allow for better credit growth.
- We expect the Reserve Bank of India (RBI) to cut its policy rate by an additional 50bps, taking the policy rate to 5.00% by December 2025. RBI delivered a cumulative 100bps in rate cuts from February to June 2025.

Growth stabilising

GDP growth slowed to 6.5%YoY in FY25 (i.e., year ending March 2025) from 9.2% in FY24. We had expected GDP growth to slow more sharply to 6.0%, however, the improvements in investment spending were backloaded to 4QFY25 allowing for the higher growth outcome. Specifically, GFCF grew by 9.4% YoY in the January to March quarter (i.e. 4QF25) from 5.2% in 3QFY25. This was mainly on account of still strong government capex spending growth of 33.4% YoY in 4QFY25 from 47.7% in 3QFY25, as reflected in the fiscal accounts.

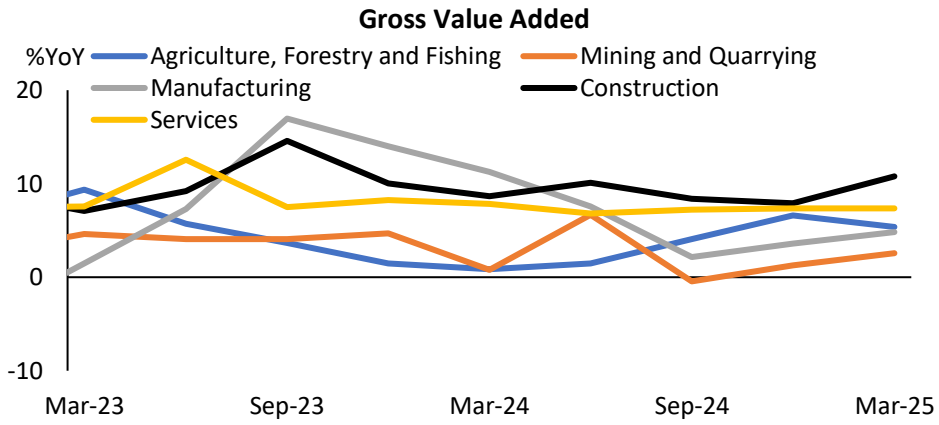


Source: CEIC; OCBC

The other drivers of growth in the final quarter of the fiscal year were relatively more subdued, with household spending (6.0% YoY versus 8.1% in 3QFY25) and government consumption (-1.8% YoY versus 9.3%) weaker compared to the previous quarter. The contribution of domestic final demand narrowed to 6.1 percentage points (pp) from 7.2pp. Mirroring this, import growth dropped to -12.7% YoY from -2.1%, with export growth slowing to 3.9% YoY from 10.8%; net exports added 3.7pp to GDP growth compared to 2.8pp in the previous quarter.

India

Net taxes (i.e., indirect taxes minus subsidies) were higher compared to 3QFY25. This led to more modest improvements in Gross Value Added (GVA) to 6.8% YoY in 4QFY25 from 6.5% in 3QFY25. The improvements were driven by the construction (10.8% YoY from 7.9%), corroborating details on the GDP side, manufacturing (4.8% from 3.6%) and mining (2.5% from 1.3%) sectors. Growth in the agriculture (5.4% versus 6.6%) and services (7.3% from 7.4%) were slower compared to the previous quarter.



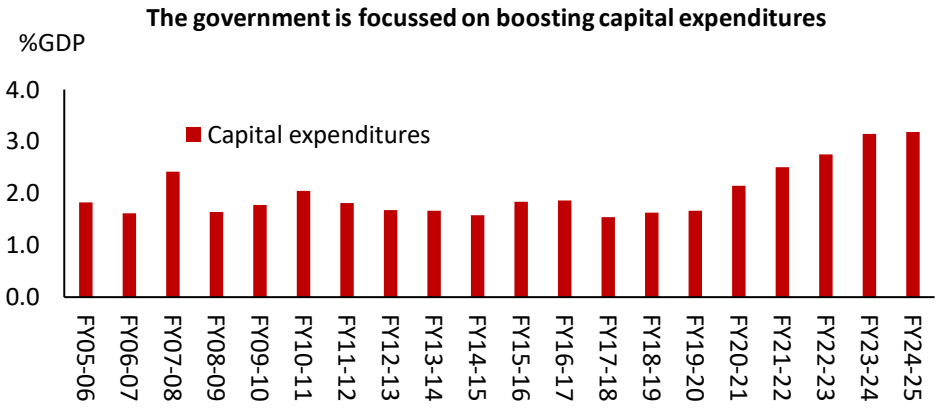
Source: CEIC; OCBC.

Looking ahead, we project FY26 (i.e., April 2025 until March 2026) GDP growth of 6.0% YoY. Our forecast, notwithstanding the statistical idiosyncrasies associated with net taxes, reflects a stabilisation in household consumption spending at 6% YoY in FY26 from 7.2% in FY25, as consumption spending remains subdued in the first half of the fiscal year before picking up in the second half as looser monetary policy conditions and better credit growth support spending.

Similarly, we expect fiscal consolidation to continue underpinned by strong prospects of GST revenue collections and the simplification of tariff structures (through the rationalisation of custom tariffs) while expenditures remain under check. Even if there is a need for some growth support on account of external factors, we expect it will be targeted to reduce the fiscal burden. This will likely keep government spending growth in check (3.5% YoY versus 2.3% in FY24).

Indeed, recent developments on the fiscal front have been encouraging. The government achieved its revised fiscal deficit target of 4.8% of GDP in FY25 and aims to further narrow the deficit to 4.4% of GDP in FY26. Revenues grew 11.3% YoY in FY25 from 14.5% in FY25 while expenditure growth slowed to 6.0% YoY from 10.5% in FY24. Importantly, capex growth was strong at 28.3% YoY from 24.8% in FY24.

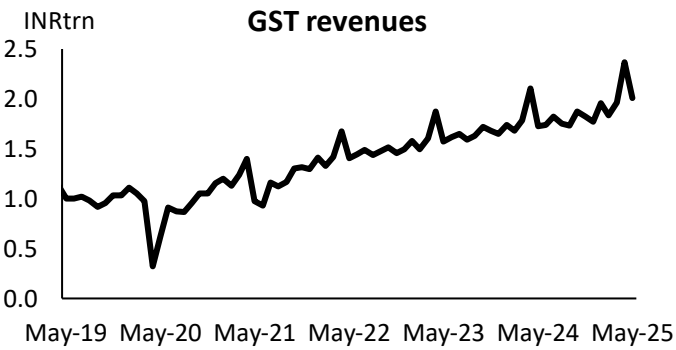
India



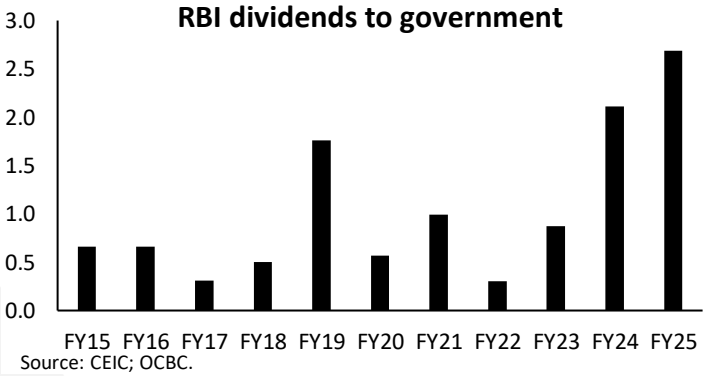
Source: CEIC; OCBC

Revenue collections in FY26 got off to a strong start, with GST collections grew 14.3% YoY in April-May from 9.4% in FY25. The collections in April of INR2.37trn is the highest on record since GST was implemented in July 2017. While May GST collections were lower at INR2.01trn, it still reflected an increase of 16.4% YoY. The annual budget shows that the government aims to collect INR11.78trn from GST in FY26. Non-tax revenues have also been boosted by higher-than-budgeted dividends from the Reserve Bank of India (RBI), which gives the government about 0.15% of GDP in additional revenues for FY26.

The government announced that it will borrow INR8trn in the first half (H1) of 2025-26 (FY26), accounting for ~54% of the total gross market borrowing target of INR14.82trn. The gross market borrowing of INR8trn will be completed through 26 weekly auctions.



Source: GST Council; OCBC.



Source: CEIC; OCBC.

While bolstering public sector capex is likely to remain a priority for the government, we forecast overall investment spending to slow to 6.3% from 7.1% as private sector businesses remain in wait-and-see mode given the external uncertainties related to US tariffs. While we have pegged as one of the more immune economies to the shockwaves emanating from US trade policies, it is not immune.

India

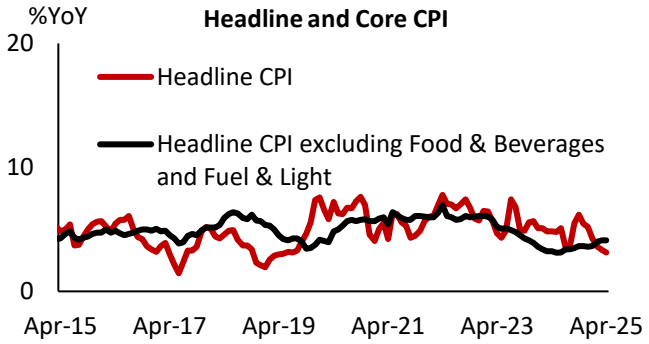
The Indian government is working to diversify trade and investment partnerships. India and the UK signed a bilateral trade agreement in May 2025, which is expected to increase bilateral trade between the two countries by USD34bn a year from 2040. The agreement will cut levies on 90% of British products sold in India, while 99% of India's exports to the UK will face no duties. The deal also contains a double contribution convention, which will exempt temporary Indian workers in Britain and their employers from making social security contributions in Britain for three years. In addition, UK businesses will have access to India's procurement market covering goods, services and construction.

The government is also working on other bilateral trade deals with the US while negotiating regarding reciprocal tariffs. The latest round of talks took place on 5 and 6 June to process with the BTA. The US has cited numerous concerns with India's trade policies as underscored in the USTR report. Indian and US officials note that talks are progressing in the right direction, it remains to be seen how much progress can be made ahead of the 9 July deadline for reciprocal tariffs.
As such, we do not see export growth collapsing into the second half of the fiscal year 2026 even if tariffs do come into effect. But we have pencilled in significantly slower growth in the exports of goods and services to 1.7% YoY from 6.3% in FY25. Concomitantly, we expect import growth to remain subdued at 0.8% YoY versus -3.7% in FY25.

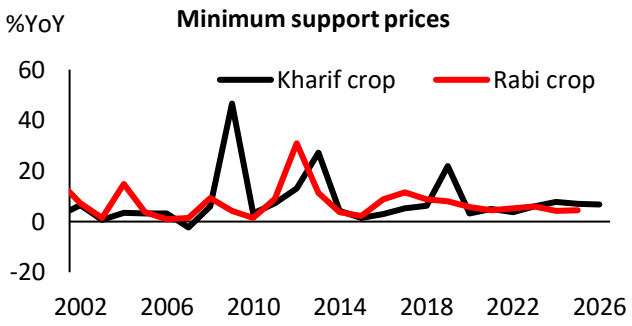
Inflationary pressures in check
Meanwhile, inflationary pressures have eased considerably over the past six months on account of lower food and transportation costs. Food inflation has eased from a peak of 10.9% YoY in October 2024 to 1.8% YoY in April 2025, driven mainly by pulses and vegetable prices. This more than offset increases in fuel inflation (-1.7% YoY to 2.9% in April) and core CPI (3.7% to 4.1%). Headline CPI averaged 4.6% in FY24-25 from 5.4% in FY23-24.

We reduce our FY25-26 headline CPI forecast to 3.8% YoY from 4.3%, previously. This is broadly consistent with RBI's revised forecast of 3.7%. The disinflation in food prices was more rapid that we had anticipated, and the outlook for food prices remains broadly comfortable. The India Meteorological Department forecasts that the monsoon rainfall will be 106+/-4% of the long period average (LPA, as of 29 May 2025) compared to its initial 105 +/- 5% of LPA, which will be supportive of the kharif (June-July) sowing season. In addition, minimum support price (MSP) increases for kharif crops at 6.9% YoY for FY25/26 is similar to 7.0% in FY24/25, preventing sharp spikes in overall price inflation.

India



Source: CEIC; OCBC



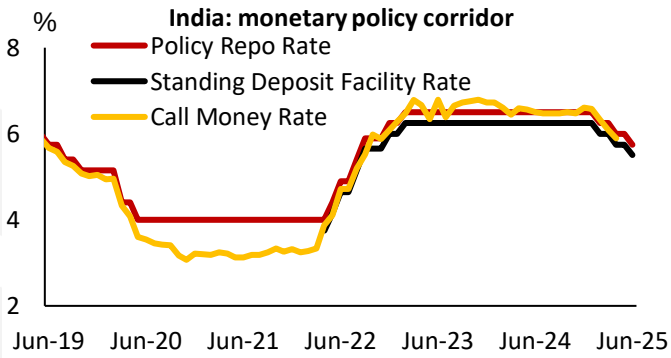
Source: CEIC; OCBC.

Reserve Bank of India has room to ease further

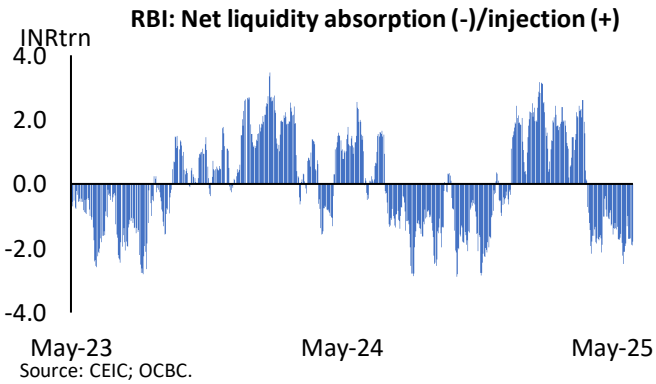
We expect RBI to cut by another cumulative 50bps through to end-2025, taking the repo rate to 5.00%. There are three more meetings left for the RBI in 2025 and one in 1Q26 to cover the remainder of the fiscal year (i.e., April 2025 until March 2026). We expect the rate cuts to be backloaded, i.e., likely in the 1 October and 5 December meetings, with the risk of delays to the 6 February 2026 meeting.

RBI cut its policy rate by a bigger than expected 50bps, taking the repo rate to 5.50% at its 6 June meeting and delivering a cumulative 100bps in rate cuts from February to June 2025. RBI reverted to a neutral stance after shifting to an accommodative one at its 9 April meeting.

The justification for the larger than expected rate cut was the inflation outlook. RBI cut its FY26 (i.e., April 2025 until March 2026) headline inflation forecast to 3.7% YoY from 4.0% previously, which is below the mid-point of RBI 2-6% target range. RBI Governor Sanjay Malhotra noted that the RBI is now confident that the inflation outlook is in "durable alignment…with the target of 4 per cent" but "is likely to undershoot the target at the margin." The confidence around the headline inflation forecasts come from food inflation remaining soft from "an early and promising start of the monsoon season" while core inflation "is expected to remain benign with easing of international commodity prices in line with the anticipated global growth slowdown."



Source: CEIC; OCBC



Source: CEIC; OCBC.

India

RBI also cut the CRR by 100bps to 3.00% and noted that the reduction will be carried out in four equal tranches of 25bps each with effect from the fortnights beginning 6 September, 4 October, 1 November and 29 November 2025. The cut in CRR would release primary liquidity of about INR2.5trn to the banking system by December 2025.

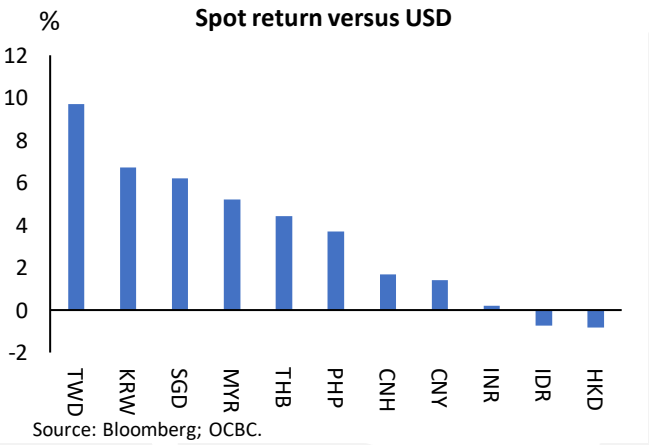
The motivation behind the CRR cut, apart from providing durable liquidity, is to "reduce the cost of funding of the banks, thereby helping in monetary policy transmission to the credit market." The timing of the cut is surprising considering net durable liquidity in the banking system had improved. Nonetheless, given the staggered nature of the announced CRR cut, we expect no further changes to CRR for this year.

The RBI has actively been managing liquidity conditions. From mid-December 2024 until end-March 2025, RBI was injecting liquidity into the banking system. It has also conducted a host of monetary operations including open market operation (OMO) purchases, USD/INR buy/sell swaps, and longer tenor variable rate repo (VRR) operations. The weighted average call money rate was below the repo policy rate in April and May but reflects a combination of looser liquidity conditions and lower transaction volumes.

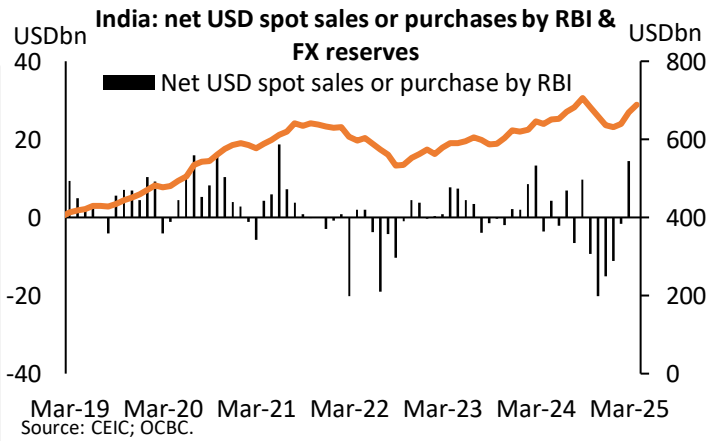
An eye in INR

INR was the worst performing currency versus USD in May and early June. This was in part driven by geopolitical tensions as cross-border relations with Pakistan deteriorated sharply following the terror attack on tourists in Kashmir in April 2025. Although tensions have since eased, the truce is a relatively uncomfortable one and this will remain a source of uncertainties in 2H25.

RBI Governor Sanjay Malhotra noted that the RBI will continue with two-sided intervention to mitigate against sharp currency moves. This the same playbook the RBI has adopted during past periods of volatility as well, intervening to prevent sharp appreciation and depreciation of the currency. This should, nonetheless, not deter the RBI from lowering its policy rate unless inflationary pressures take a sharp turn higher.



Source: Bloomberg; OCBC.



Source: CEIC; OCBC.

Indonesia

Indonesia: The perils of policy perception

- We expect growth to ease to 4.7% YoY in 2025 from 5.0% in 2024, with risks skewed to the downside.
- Fiscal policy is expected to remain supportive of growth through 2H25, anchored by President Prabowo's campaign priorities like the free nutritious meal program and increased social assistance.
- We expect at least one more 25bp of rate cut by Bank Indonesia in 2H25. The timing and size of future cuts will hinge on incoming inflation prints, rupiah stability, and the Fed's policy path

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Policy perception pains

The sharp drop in the local equity market on 18 March, rumoured personnel changes, the lack of clarity on fiscal outcomes, weaker 1Q25 GDP growth momentum, and sweeping policy changes such as Danantara (the new sovereign wealth fund) has kept investor sentiment toeing the line of trepidation through 1H25.

The authorities were fast to respond by clarifying the structure of Danantara, reaffirming crucial personnel appointments such as the finance minister and continuing with the timely release of monthly fiscal data. However, the more fundamental questions surrounding domestic policy priorities such as large fiscal expenditures for the 'free nutritious meal scheme' and the perceptions associated with broader policy direction becoming more populist will likely remain an overhang into 2H25.

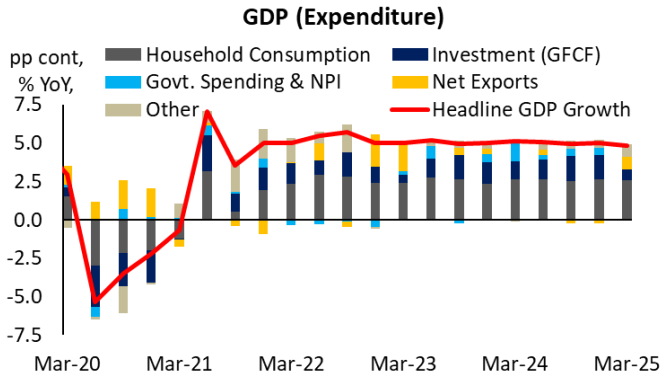
On the external front, Indonesia's team, led by Coordinating Minister of Economic Affairs Airlangga Hartarto, continued to negotiate with the US on reciprocal tariffs. Ongoing talks with the US aim to rebalance the trade surplus with the US, targeting up to USD19bn in redirected imports and addressing non-tariff barriers, including ICT-related restrictions. The government will likely aim to reduce the reciprocal tariffs to 10% from the 32% announced on 2 April. Should negotiations take time, the headwinds to export growth will be felt more immediately than other ASEAN neighbours. We estimate that less than 10% of US imports from Indonesia are exempt from tariffs compared to 59.7% in Singapore and 45.7% in Malaysia.

Economic impact starting to show

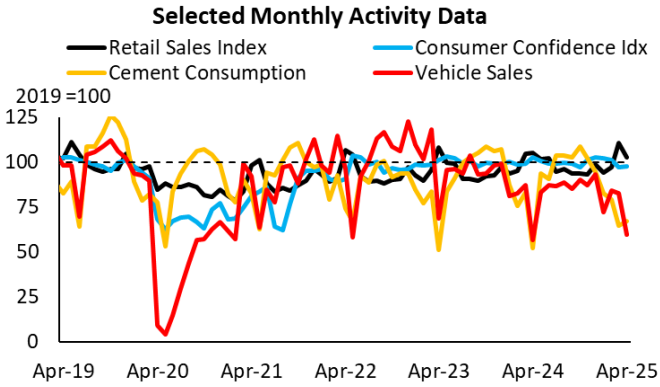
We forecast 2025 GDP growth slowing to 4.7% YoY from 5.0% in 2024 implying growth of 4.7% in 2Q-4Q25 from 4.9% YoY in 1Q25. The risks to our forecast are to the downside given heightened external uncertainties related to US trade policies but also limited signs of a clear turnaround in domestic policy direction.

Household consumption growth, which accounts for more than half of GDP, slowed to 4.9% YoY in 1Q25 from 5.0% in 4Q24, despite the seasonal festivities. The Ramadan-driven spending boost proved short-lived. High-frequency indicators continue to reflect weak underlying demand; real retail sales growth fell to -2.2% YoY in April from 5.5% growth in March while consumer confidence remains shaky, and both automotive and cement sales remained weak.

Indonesia



Note: Other refers to combined value of change in inventories and statistical discrepancies. Source: Statistics Indonesia (BPS), CEIC, OCBC.



Source: Bank Indonesia, GAIKINDO, Indonesia Cement Association, CEIC, OCBC.

We expect household consumption growth to remain soft, averaging 4.9% in 2Q–4Q25. Indeed, there is little evidence of a sustained recovery in 2Q25. Although the data suggests that employment conditions have been broadly stable, anecdotal evidence suggests that job losses are on the rise. According to Manpower Minister Yassierli, more than 24k workers in Indonesia have been laid off as of May 2025. The hardest hit regions were Central Java, Jakarta, and Riau. The hardest-hit sectors include manufacturing, wholesale and retail trade, and services[3].

The weakness in household consumption has prompted the government to implement measures aimed at bolstering demand. Specifically, the government plans to introduce new subsidies and incentives between June and July. These include discounts on public transportation and toll fees, expanded food and cash assistance, wage subsidies for low-income workers, and temporary relief from work accident insurance premiums. The announced stimulus package has cancelled the previously planned electricity discount; however, the funds will be redirected to significantly increase wage subsidies from IDR 150k per month to IDR 300k per month. Overall, the impact of these measures will more likely help mitigate further downside risks to household spending rather than boost growth in a meaningful manner.

[3] Over 24,000 Workers Laid Off in Indonesia So Far This Year. Jakarta Globe, 5 May 2025. Last accessed: 5 May 2025.

Indonesia

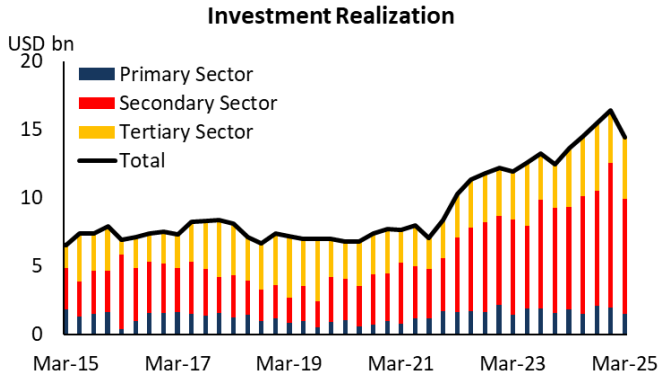
Announced stimulus to support purchasing power to be disbursed in June-July 2025			
Categories	**Items**	**Magnitude**	**Details**
Transportation (IDR0.94trn)	Discount on train fares	30%	A 30-percent discount will be offered on train tickets for 2.8mn passengers, budgeted at IDR0.3trn. Additionally, VAT for economy class airline tickets will be borne by the Government at a rate of 6 percent, with a budget of Rp0.43trn aimed at ~6mn passengers. Sea transportation tickets will be available at half price for 500k passengers, with a budget allocation of IDR0.21trn.
	Discount on plane tax (PPN DTP)	6%	
	Discount on sea transport	50%	
Toll fares (IDR0.65trn)	Toll road fares discount	20%	A 20% discount for 110mn toll road users under a partnership with the Toll Road Business Entity (BUJT), with the incentives will be carried out through non-state budget operations (non-APBN).
Social Assistance (IDR1193trn)	Staple food cards	IDR200k/ month	An additional fund of IDR200k/month will be given for two months to 18.3mn beneficiaries of the Basic Food Card (Kartu Sembako) program. Moreover, beneficiaries (KPM) will receive 10 kg of free rice per month, totalling 20 kg over two months.
	Rice supports	10kg	
Wage Subsidy (IDR10.72trn)	Wage Subsidy Assistance (BSU)	IDR300k/month	BSU of IDR300/month for two months, targeting 17.3mn workers with income below IDR3.5mn or below the provincial/regency/city minimum wage, as well as to 565k non-tenured teachers from the Ministry of Primary and Secondary Education and the Ministry of Religious Affairs.
Insurance premium (IDR0.2trn)	Occupational Accident Insurance premium discount	50%	Extend the period for 50% discount on occupational accident insurance (JKK) premium by 6 months for 2.7mn workers in labour-intensive industries. This incentive will be carried out through non-state budget operations (non-APBN).
Source: Cabinet Secretary, OCBC.			

Investment spending to remain on the sidelines

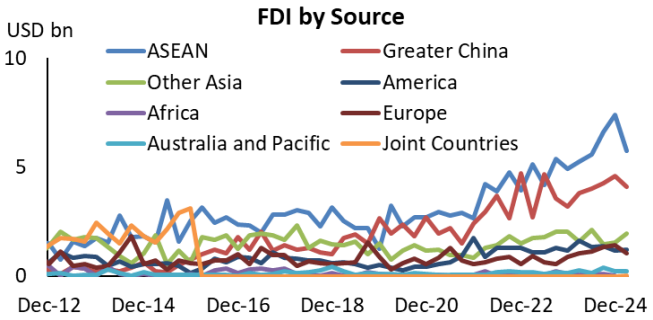
Investment spending, the other key driver of economic growth, slowed to 2.1% YoY in 1Q25 from 5.0% in 4Q24, likely reflecting slower construction activity and softer commodity prices. We expect gross fixed capital formation (GFCF) growth to remain muted for the rest of the year, averaging just 4.2% in 2025, down from 4.6% in 2024, as businesses remain cautious amid an uncertain policy landscape and tepid external demand.

Concerns over large-scale project viability emerged in 2Q25, following South Korea's LG Energy Solution's confirmation that it would no longer proceed with its previously announced EV battery joint venture valued at USD11bn with Indonesia Battery Corporation. While the group maintained its broader commitment to Indonesia's EV ecosystem, including plans for cell development and R&D, these cancellations/delays can be seen as a bellwether for future investments in the current backdrop.

Indonesia



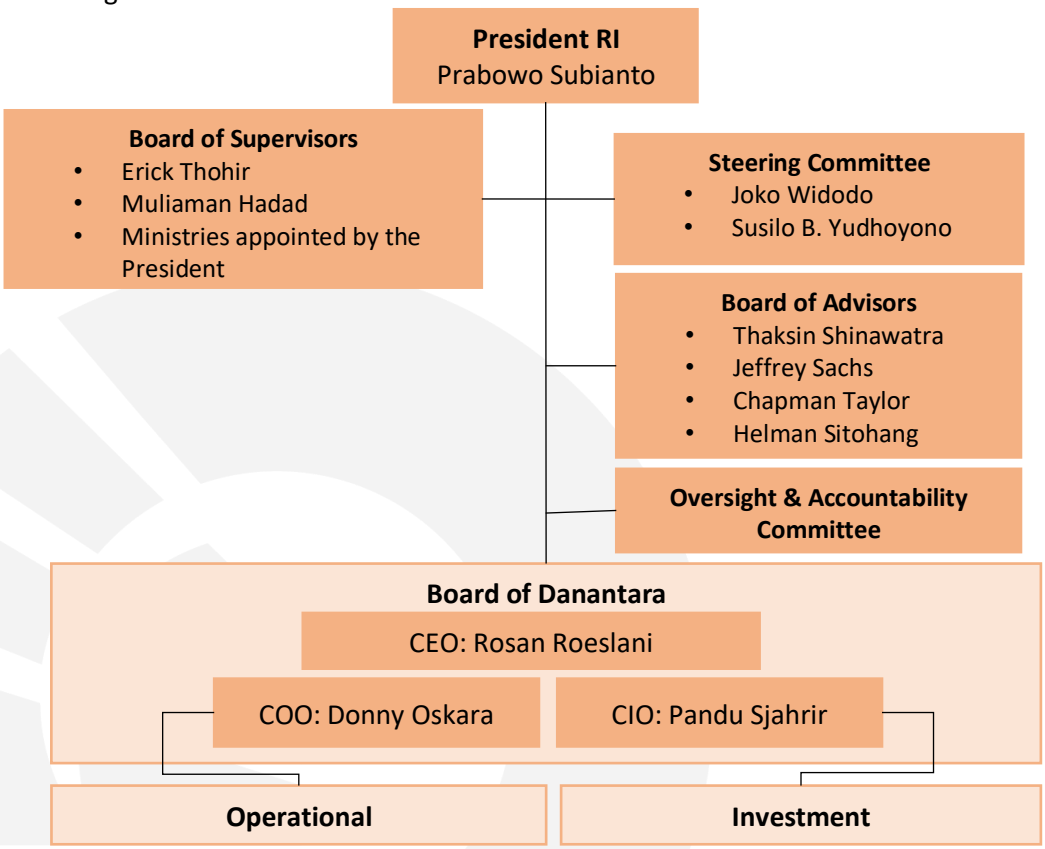
Source: BKPM, CEIC, OCBC.



Note: ASEAN values are comprised of Brunei Darussalam, Cambodia, Singapore, Malaysia, the Philippines, Thailand, and Vietnam. Greater China includes Mainland China, Hong Kong, Macau, and Taiwan. Source: BKPM, CEIC, OCBC.

Moreover, realized foreign direct investment (FDI), as reported by BKPM, slowed noticeably to 5.6% YoY to USD14.4bn in 1Q25 from 31.5% (USD16.4bn), with the slowdown more pronounced in the primary (-16.3% YoY in 1Q25 from 24.9% in 4Q24) rather than in the secondary (12.0% from 37.0%) and tertiary (3.9% from 21.4%) sectors.

The government plans to develop strategic investment projects backed by the new sovereign wealth fund, Danantara, over the medium-term. Danantara, launched in February 2025, aims to mobilize up to USD20bn in reinvested dividends and channel capital toward priority sectors such as digital infrastructure, healthcare, food security, and renewable energy, among others. The fund is expected to play a critical role in facilitating long-term investment and attracting co-financing from institutional and global investors.

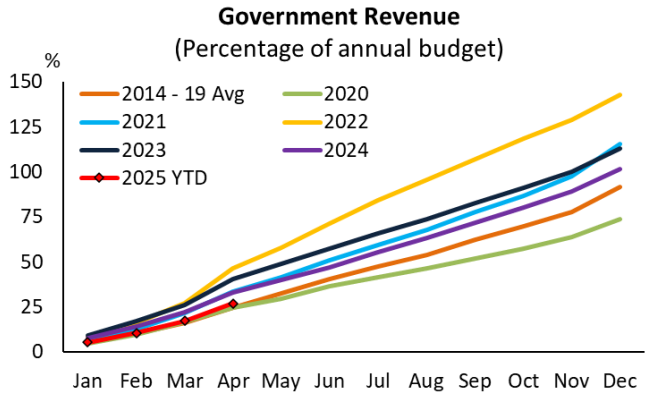


Indonesia

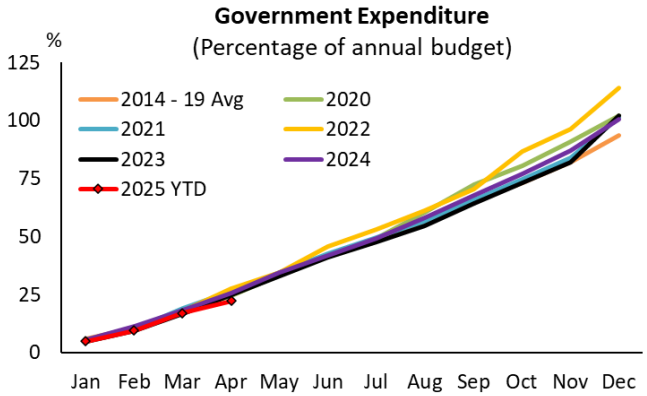
The launch of Danantara was met with trepidation and enthusiasm, and was cited as one of the key reasons for the sharp JCI drop on 18 March, which triggered the intra-day circuit breaker. With all the capital of the State-Owned Enterprises (SOEs) managed under Danantara, the capital concentration risk is non-negligible. The government did subsequently announce the structure of Danantara, which proved relatively credible. If managed well, the prospect for returns is promising.

Fiscal risks still remain

Fiscal policy is expected to remain supportive of growth through 2H25, anchored by President Prabowo's campaign priorities such as the free nutritious meal program and increased social assistance. While these commitments will keep spending elevated, the government still aims to keep the fiscal deficit at 2.5% of GDP this year, versus 2.3% of GDP in 2024.



Source: Indonesia Directorate General of Budget, CEIC, OCBC.



Source: Indonesia Directorate General of Budget, CEIC, OCBC.

The year-to-date fiscal balance is in a surplus of IDR4.3trn (0.02% of GDP) as of April 2025. The details are lacklustre, with revenues and expenditure growth dropping by 12.4% YoY and 7.6% year-to-April, respectively. The drop is revenues reflect both lower tax revenue (-8.7% YoY) and non-tax revenue (-24.6% YoY) amid subdued global commodity prices, and some tax administration teething issues. On the expenditure side, some social assistance spending was delayed due to data synchronization issues.

Looking ahead, we do believe that fiscal risks have not completely abated. President Prabowo's 'free nutritious meal scheme' is expensive, budgeted at IDR171trn in 2025. In addition, the government seems keen to bolster household spending (details in table above) which will also pressure the expenditure profile. Revenue collections are also likely to come under pressure. Slower growth momentum will weigh on tax revenue collections while lower commodity pressures could impact non-tax revenues.

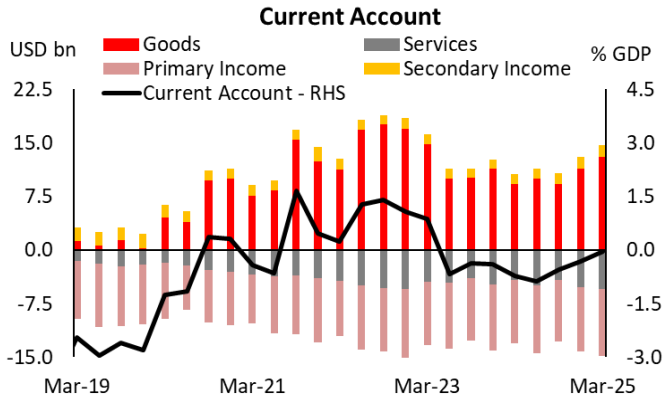
Our baseline is for the government to keep to its 2025 fiscal deficit forecast at 2.5% of GDP, below the statutory 3% ceiling. However, there remain risks of fiscal slippage, which could become more apparent in 4Q25 as the costs of the free meal scheme and revenue collection prospects become clearer. In addition, the degree of counter-cyclical fiscal policy requirements will also be better known.

Indonesia

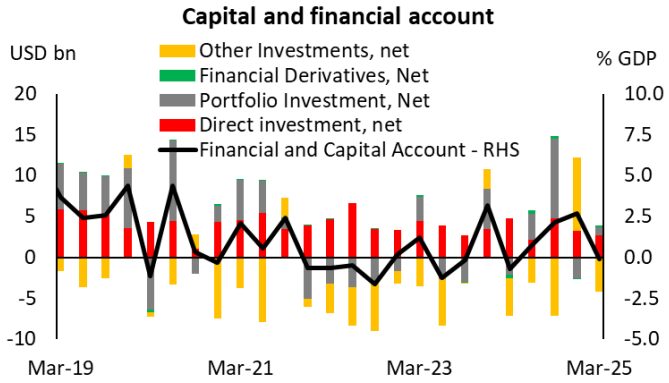
Cloudy external outlook

Meanwhile, the current account deficit narrowed to USD0.2bn (0.1% of GDP) from USD1.1bn (0.3% of GDP) in 4Q24, supported by a stronger non-oil and gas trade surplus. Frontloaded shipments ahead of the US tariff announcement likely boosted exports, with the goods surplus rising by 40.5% YoY to USD13.1bn in 1Q25.
We forecast the current account deficit to widen to 1.4% of GDP in 2025 from 0.6% in 2024, reflecting a softer goods trade balance and persistent deficits in services and primary income. Our forecast is slightly deeper than Bank Indonesia's 0.5%–1.3% range.

The overall balance of payments posted a deficit of USD0.8bn in 1Q25, a reversal from the USD7.9bn surplus in 4Q24. The capital and financial account shifted to a deficit of USD0.3bn from a surplus of USD9.7bn in 4Q24, as net outflows in the 'other investments' account outweighed portfolio inflows. Net portfolio investments recovered to a USD1.0bn surplus from a deficit of USD2.5bn, while net FDI inflows held relatively steady at USD2.6bn. As a result, the basic balance improved to USD2.5bn (0.7% of GDP) in 1Q25 from USD2.1bn (0.6% of GDP) in 4Q24.



Source: Bank Indonesia, CEIC, OCBC.



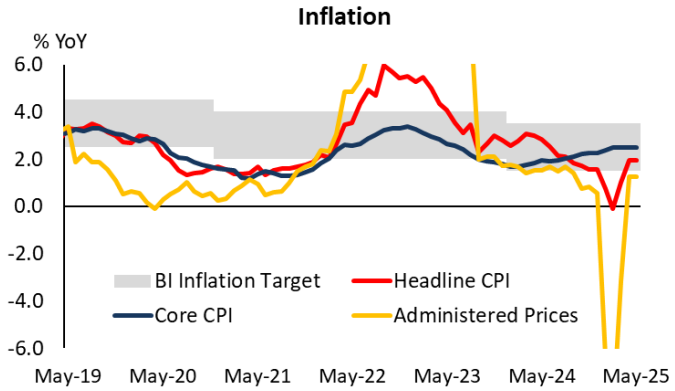
Source: Bank Indonesia, CEIC, OCBC.

Over the medium-term, Indonesia is actively deepening engagement through other trade avenues. It joined BRICS in January 2025, while its OECD accession is ongoing, alongside progress in various free trade agreement (FTA) negotiations. These include the I-EAEU FTA, efforts to facilitate deeper trade with Thailand, and deepening ties with China, evidenced by 12 MoUs signed during Premier Li Qiang's May 2025 visit.

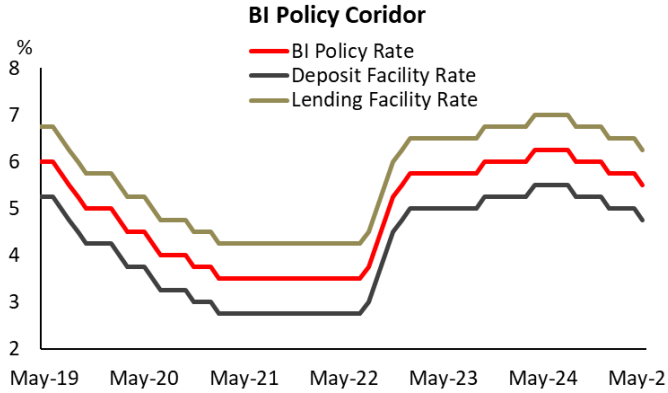
Benign inflation trajectory likely to sustain

The disinflation trend continued into 2Q25, with headline inflation averaging 2.0% ytd as of April - well below the midpoint of BI's 1.5–3.5% target band. We expect inflation to average 2.0% for full year 2025 from 2.3% in 2024, supported by stable food supply, subdued global commodity prices and delayed VAT hikes. Core inflation has remained soft, underscoring weak domestic demand conditions. There has, however, been some volatility in core inflation associated with elevated global gold prices. While risks around administered price adjustments and currency volatility remain, these are unlikely to meaningfully alter the current inflation outlook.

Indonesia



Source: Statistics Indonesia (BPS), Bloomberg, OCBC.



Source: Bank Indonesia, CEIC, OCBC

Bank Indonesia to remain opportunistic about rate cuts

The benign inflation backdrop has provided Bank Indonesia (BI) with room to recalibrate its monetary stance. Following two 25bp cuts in January and May 25 that brought the benchmark policy rate to 5.50%, we expect at least one more 25bp cut in 2H25. The bias for further easing is reinforced by soft growth momentum and relatively stable rupiah movement of late. BI has also complemented rate moves with macroprudential loosening, including relaxed reserve requirements and expanded foreign borrowing limits to encourage credit flows.

Looking ahead, we expect BI to maintain a data-dependent easing bias while closely monitoring external risks. The timing and size of future cuts will hinge on incoming inflation prints, rupiah stability, and the Fed's policy path. With inflation under control and growth still soft, we believe BI has room to reduce rates further without undermining external stability.

Notable macroprudential measures announced in 2025					
Measures	**Jan-25**	**Feb-25**	**Mar-25**	**Apr-25**	**May-25**
Macroprudential Liquidity Incentive Measures	400bp maximum. *No change from previous meeting.*	-	Raised to a maximum of 5% (500bps) from 4.0% previously.	-	-
Loan/Financing Ratio and Downpayment requirements	100% LTV/FTV, and 0% for down payment, effective 1 Jan 2025* *No change from previous meeting.*	-	-	-	-
Countercyclical Capital Buffer	0%. *No change from previous meeting.*	-	-	-	-
Macroprudential Liquidity Buffer/ Sharia Macroprudential Liquidity Buffer	5%. *No change from previous meeting.*	-	-	-	Lowered to 4.0% from 5.0% for conventional banks, and to 2.5% from 3.5% for syariah banks.
Bank Foreign Funding Ratio	30%. *No change from previous meeting.*	-	-	-	Raised to a maximum of 35% from 30%.
Source: Bank Indonesia, OCBC.					

Macau

Macau: Fading recovery

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- The economy contracted for the first time in real terms since the removal of border controls in 2022. Real GDP shrank by 1.3% YoY in 1Q25 (4Q24: 3.4% YoY; 2024: 8.8% YoY), dragged by sharp decline in tourism service exports and moderating gaming service exports. In tandem, a broad range of indicators are showing renewed weakness. Unemployment rate picked up again, loan demand stayed muted, while consumption sentiment remained tepid. All in all, recovery faded into early 2025, making the return to 2019 economic size an even longer and bumpier journey.
- With gross gaming revenue plateauing, and retails sales on downtrend, growth momentum was increasingly hard to gather. Moreover, the high-interest-rate environment and negative wealth effect stemming from property market downturn continued to pose drag on economic activities. We revise our full-year growth forecast down to 2.6% YoY, from the previous estimate of 4% YoY, taking into account the more challenging external environment and the slowing gaming sector recovery. Separately, the unemployment and inflation rates are pitched at 1.9% and 0.3% YoY respectively for 2025.
- Headwinds, such as fading economic recovery, low rental yields and stiff competition from neighbouring city Zhuhai, continued to plague the housing market. Meanwhile, housing supply remained abundant, even for the public sector. We tip the decline of housing prices at 6% YoY for 2025, following a decline of 11.7% YoY in 2024, with further prime rate cuts and mainland's increased housing support measures offsetting part of the headwinds.

From stalled recovery to fading recovery

Macau is confronted with a new reality, after the strong post-Covid comeback. While visitors continued to pour in, the once deep-pocketed gamblers and shoppers are now turning more price-sensitive and budget-conscious, amid increasing uncertain economic outlook. The gross gaming revenue and tourists' non-gaming spending essentially flatlined in early 2025, despite double-digit growth in visitor arrivals. The shift in consumption patterns spelled problems for the city's growth drivers and highlighted the fragility of the economy. Macau's economy shrank unexpectedly in 1Q25, ending the eight-quarter streak of growth. A broad range of indicators are also showing renewed weakness. Unemployment rate picked up again, loan demand stayed muted, while consumption sentiment remained tepid. All in all, recovery faded into early 2025, making the journey back to the economic size of 2019 even longer and bumpier.

Macau

Chart 1: Broad based weakening of growth momentum

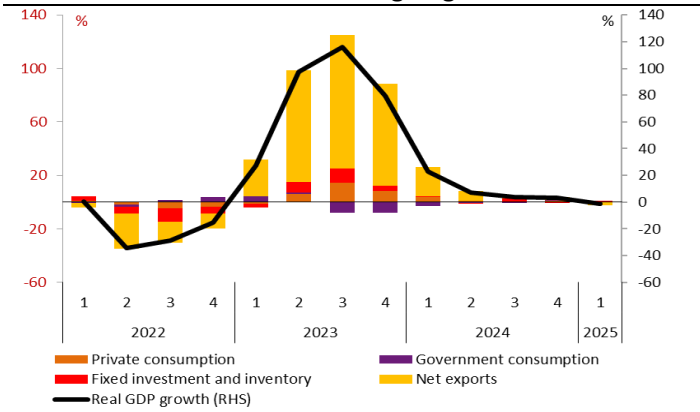
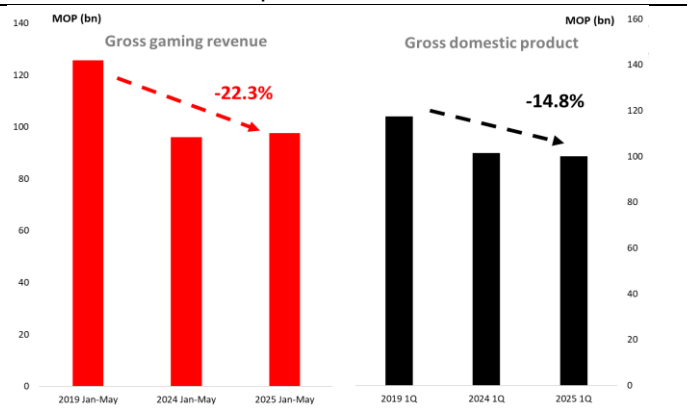


Chart 2: Still short of pre-covid size



Sources: DSEC, DICJ, OCBC.

First contraction since the removal of border control

Macau's economy contracted for the first time in real terms since the removal of border controls in 2022. Real GDP shrank by 1.3% YoY in 1Q25 (4Q24: 3.4% YoY; 2024: 8.8% YoY) **(Chart 1)**, dragged by a sharp decline in tourism service exports and moderating gaming service exports (1Q25: -11.7% YoY and 1.6% YoY). The government attributed the weaker-than-expected performance to the high base last year, as well as the changes in visitor consumption patterns, among other factors. Compared to the pre-Covid level in 2019, GDP was still down by 14.8% in 1Q25 **(Chart 2)**.

During the quarter, growth momentum weakened across the board, with growth of private and government consumption slowing to 0.3% YoY (4Q24: 2.9% YoY) and 1.1% YoY (4Q24: 6.3% YoY) respectively. Meanwhile, exports of services and total exports fell by 3.4% YoY (4Q24: 2.1% YoY) and 4.0% YoY (4Q24: 0.3% YoY) respectively in the first quarter. The only silver lining came from the investment front, which still stayed robust with strong presence from private sector. Gross fixed capital formation reverted to growth at 6.5% YoY (4Q24: -0.6% YoY), with private construction equipment investment expanding by 22.2% YoY (4Q24: 11.5% YoY).

Trends are pointing to a bleak outlook

With gross gaming revenue plateauing **(Chart 3)**, and retails sales on downtrend **(Chart 4)**, growth momentum was increasingly hard to gather. Moreover, the high-interest-rate environment and negative wealth effect stemming from property market downturn continued to pose drag on economic activities. We revised our full-year growth forecast down to 2.6% YoY, from the previous estimate of 4% YoY, taking into account the more challenging external environment and the slowing gaming sector recovery. We expect total gross gaming revenue to grow by a low-to-mid single digit figure in 2025, while full-year tourist arrivals to increase by 8-12%YoY. Export of services is likely to expand further, albeit at a moderated pace. Meanwhile, sectors with weak ties to tourism are likely to face persistent pressure. Separately, the unemployment and inflation rates are pitched at 1.9% and 0.3% YoY respectively for 2025. A sharper-than-expected slowdown in Mainland China's economy and further delays in Federal Reserve rate cuts represent the main short-term risks to the outlook.

Macau

Chart 3: Gross gaming revenue levelling off

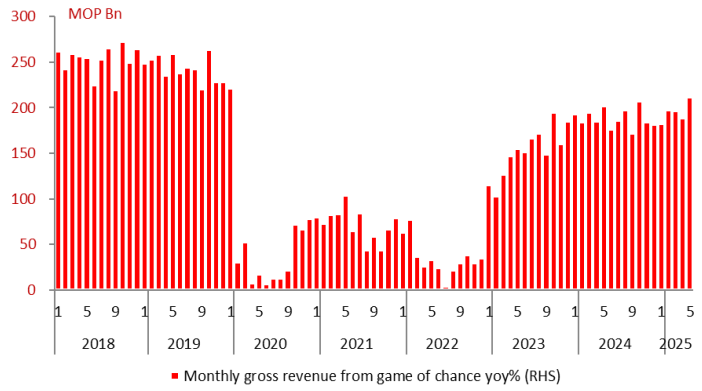
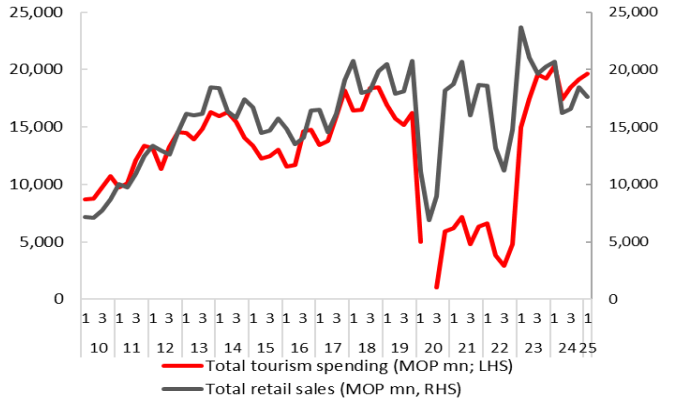


Chart 4: Retail sales on downtrend



Source: DSEC, Macau Tourism Office, OCBC.

"Quantity isn't quality"

On one hand, efforts to promote non-gaming tourism continued to yield results, attracting more leisure tourists, MICE travellers and concertgoers. In the first four months of 2025, total visitor arrival rose by 12.9% YoY **(Chart 5)**, returning to 93.9% of pre-Covid levels in 2019. Hotel occupancy rate averaged at 89.7% in the first quarter, just shy of 91.9% in the same period in 2019. On the other hand, shift in spending patterns invalidated the linear relationship between visitor arrivals and tourist spending. Macau's exports of services excluding gaming contracted by 3.7% YoY, despite the increase in visitor arrivals.

Chart 5: Visitor arrivals levelling off

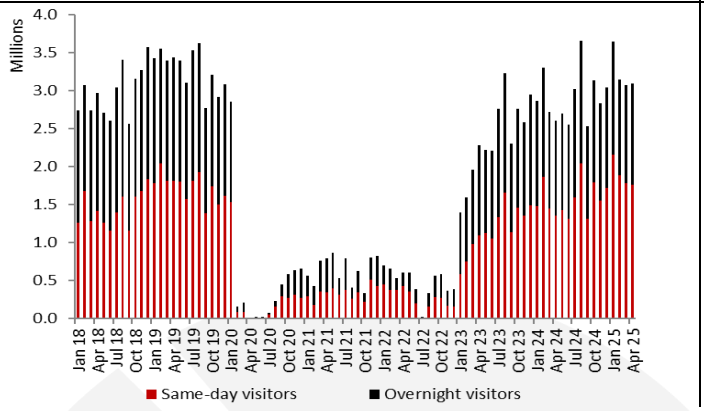
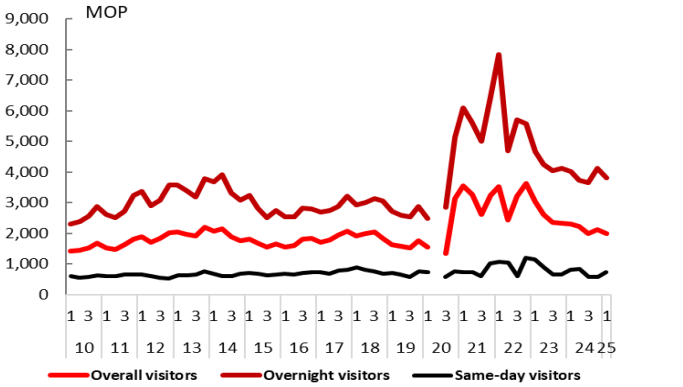


Chart 6*: Per capita spending declined further



*Excluding gaming

Source: DSEC, Macau Tourism Office, OCBC.

Concerns over a prolonged property downturn, job security and US-China trade tensions had dampened the willingness of Mainland visitors to spend. Additionally, the prevalence of "military-style travel", is reshaping and re-defining the post-Covid tourism. This new travel style emphasizes efficiency and packed experiences, and are often on tight budgets, sacrificing comfort and convenience. As a result, the share of same-day visitor rose to 58.5% in the first four months this year, above that of 53.9% in 2019. Per-capita spending (excluding gaming expenses) of tourists visiting Macau fell further to MOP1,989 in 1Q25, the lowest level since 2020 **(Chart 6)**. During the quarter, retail sales value fell by 15.0% YoY to MOP17,582mn. Sales of leather goods (-24.2% YoY), cosmetics and sanitary articles (-22.3% YoY),

Macau

department stores (-18.8% YoY) and watches, clocks and jewellery (-17.3%), which used to be tourists' top picks, recorded the most visible declines.

Chart 7: Slight pickup in the share of VIP segments

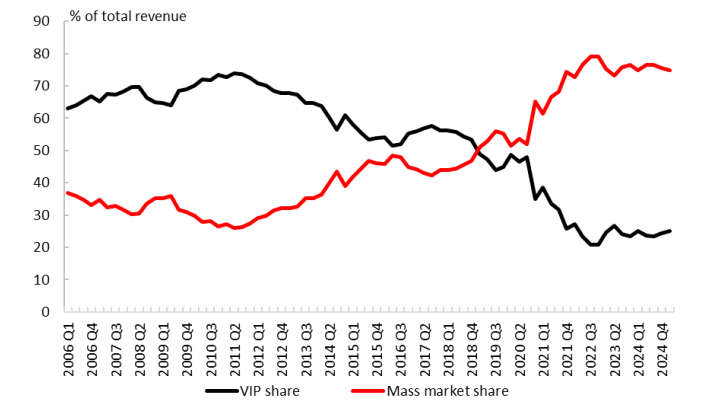
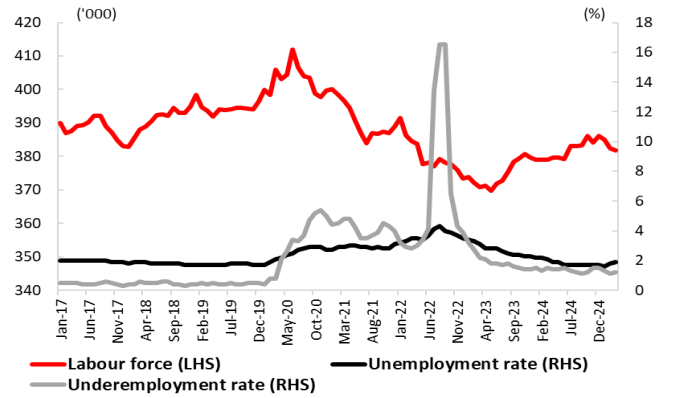


Chart 8: Unemployment rates bounced back



Sources: DSEC, DICJ, OCBC.

Shifting trends in gaming sector

Strict controls over the junket and gambling related activities, coupled with China's lagged economic recovery and intensified regional rivalries, stunted the city's gaming sector's recovery. Gross gaming revenue (averaging at MOP19.5bn per month) expanded at a meagre pace of 1.7% YoY in the first five months of the year, and is 2.3% below the official forecast. There appeared to be a slight pickup in the share of VIP segments, though still within recent range after the reset in regulatory environment **(Chart 7)**. Generally speaking, we expect share of the mass market to VIP segments to hold at roughly 75%-25%, with the landscape of latter permanently altered by the crackdown of junket activities. Gross total gaming revenue may still refresh post-Covid high in coming months. Yet, with the normalised base, year-on-year growth should fall to a low-to -mid single digit figure, i.e. 3%-6%, in 2025.

Slackening labour market

After achieving full employment status for the most part of 2024, the labour market softened again entering 2025, albeit only mildly. The overall unemployment rate and local resident unemployment rate inched back higher to 1.9% and 2.5% respectively in the first quarter **(Chart 8)**, up by 0.2 percentage points compared to the previous quarter. The rise in unemployment was most pronounced in "hotels and restaurants", "financial" and "real estate" industries. That said, salaries and remuneration packages remained competitive. The median employment income of total labour force and residents in the labour force reached all-time highs of MOP18,800/month and MOP21,500/month respectively in 1Q25 **(Chart 9)**.

Separately, the growth trend of labour force had been reversed, alongside a decline in local residents' labour force participation rate. The labour force fell back to early 2024 levels at 379.1k in the first quarter this year, while local residents' labour force participation rate edged down to a record low at 61.1% (from 62.1% in 4Q24). The loss in labour force was most evident among "25-34", "65 or above", and "below 25" age groups.

Macau

Chart 9: Employment earnings rose to record highs

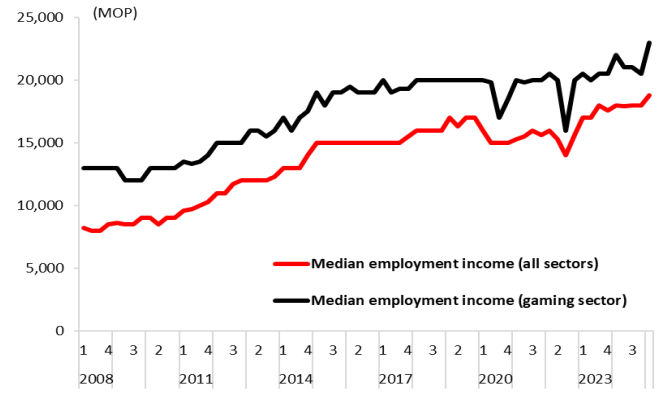
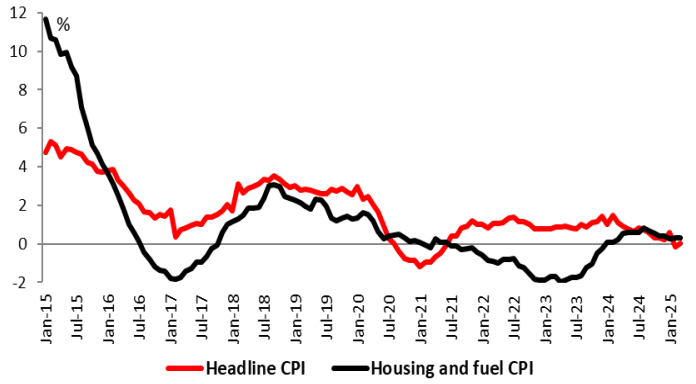


Chart 10: Subdued inflationary pressure



Inflationary pressures almost non-existent

In light of the weakening growth, the city's inflationary pressures cooled substantially to nearly non-existence. Headline inflation averaged at 0.15% YoY in the first quarter this year **(Chart 10)**, with the prices of "communication" (-2.9% YoY), "transport" (-2.7% YoY), "clothing and footwear" (-2.3% YoY) and "household furnishings and services" (-0.8% YoY) experiencing varied degrees of decline. Nonetheless, "housing and fuels" inflation (accounting for around 34% of the CPI basket) steadied at 0.3% YoY, providing some anchor to the overall price level. We expect inflationary pressures to remain fairly low in the remainder of the year, on the back of still-soft demand. The full-year headline inflation forecast was revised down to 0.3% YoY, from the earlier estimate of 0.8%, with risk titled to the downside.

Housing prices still in downtrend

The search for bottom for Macau housing prices continued, after four consecutive years of housing market downturn. Residential property price index fell further by 2.1% QoQ in the first quarter of 2025 (4Q24: -2.0% QoQ). Compared to the recent highs, the residential property price index declined cumulatively by 25.2% **(Chart 11)**. While average rent continued to trend higher, the pace of increase slowed to 0.4% QoQ (4Q24: 0.7% QoQ). Trading activities stayed subdued, at 251 cases/months in the first quarter, down from that of 295 cases/month in the previous quarter.

Headwinds, such as fading economic recovery, low rental yields and stiff competition from neighbouring city Zhuhai, continued to plague the housing market. Meanwhile, housing supply remained abundant, even in the public sector (public housing available for application exceeded that of qualifiable applications according to government record). We tip the decline of housing prices at 6% YoY for 2025, following a decline of 11.7% YoY in 2024, with further prime rate cuts and mainland's increased housing support measures offsetting part of the headwinds.

Challenging path ahead for SMEs

The newly appointed Chief Executive, Sam Hou Fai, delivered his first policy address on 14 April. Key changes include an increase in medical vouchers from MOP600 to MOP700, and increase in old-age allowance to MOP10,000 annually. Under the Wealth Partaking scheme, cash handout will be given to permanent resident

Macau

(MOP10,000) and non-permanent residents (MOP6,000), same as last year. An additional MOP7,000 will be credited to the non-mandatory central provident fund accounts of each eligible resident. Separately, a MOP10bn fund will be established to extend credit and liquidity support to SMEs.

The rollout of credit support highlighted the challenges faced by SMEs, in light of limited positive spillovers from gaming and tourism sector recovery. Domestic credit to private sector contracted further **(Chart 12)**, especially for the credit extended to the wholesales/ retail and other services sectors. Meanwhile, non-performing loan ratio reached 5.6% in January 2025, the highest since 2004. We expect the imbalanced economic recovery to persist, while credit quality may continue to worsen for selected sectors.

Chart 11: Ongoing correction in the housing prices

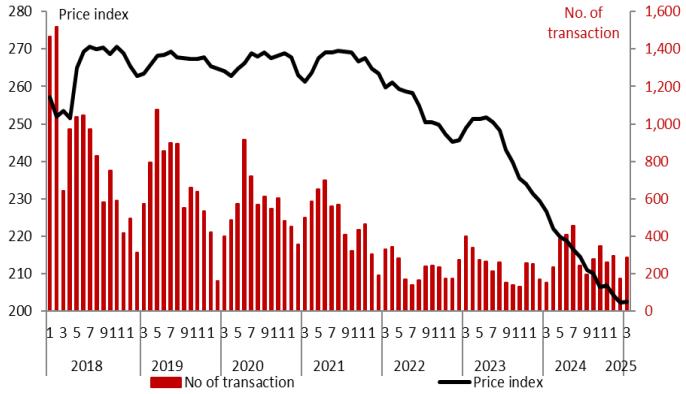
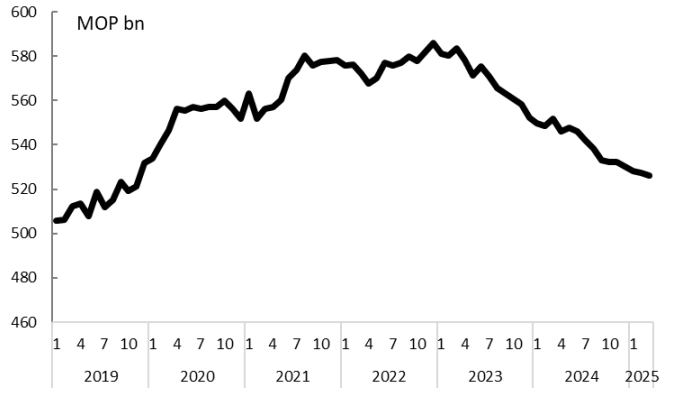


Chart 12: Weak loan demand



Sources: DSEC, AMCM, OCBC.

Malaysia

Malaysia: Focused on the fundamentals

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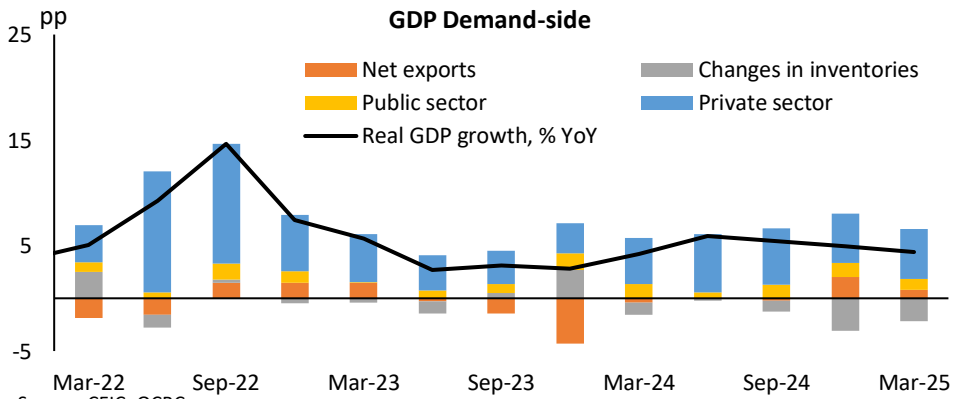
- We forecast GDP growth to slow to 4.3% YoY in 2025 from 5.1% in 2024, reflecting weaker external demand.
- We lower our headline inflation forecast to 3.0% from 3.7% in 2025, with RON95 rationalisation pushed to October from our previous baseline of June 2025.
- Our baseline is for Bank Negara Malaysia (BNM) to reduce its policy rate by a cumulative 50bps in 2H25, taking the policy rate to 2.50% by end 2025.

The economy entered this latest bout of volatility on strong footing. The economy grew by 5.1% YoY in 2024 driven by solid domestic and external demand. On the domestic demand front, the private sector contributed 5.0 percentage points to headline GDP growth last year from 3.5pp in 2023, while the public sector contributed 1.1pp from 0.8pp in 2023. Net exports contributed 0.4pp after shaving off 1.2pp in 2023 as electronics and electrical (E&E) exports lifted external sector prospects.



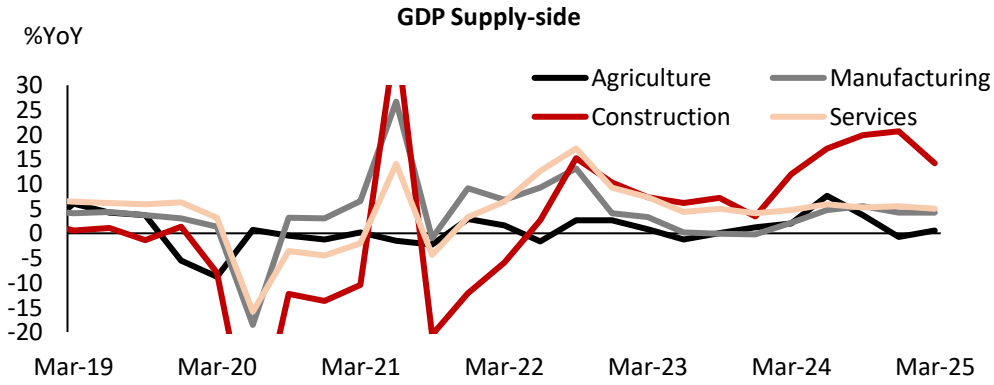
Source: CEIC; OCBC.

Corroborating this, growth in the manufacturing sector improved to 4.2% YoY from 0.2% in 2023 led by machinery & equipment, computers and peripheral equipment. Growth across other key sectors such as agriculture (3.1% YoY from 0.2% in 2023) and services (5.3% from 5.1% in 2023) also improved while growth in the construction sector jumped to 17.5% YoY in 2024 from 6.0% in 2023. This underscores the support from residential, non-residential and civil engineering projects.

Given the strong growth outturn in 2024, we had expected economic growth would slow in 2025. Our original 2025 GDP growth forecast of 4.5% YoY was downgraded to 4.3% following the 2 April reciprocal tariff announcements. 1Q25 GDP growth slowed to 4.4% YoY from 4.9% in 4Q24, driven by slower private consumption, investment spending and export growth.

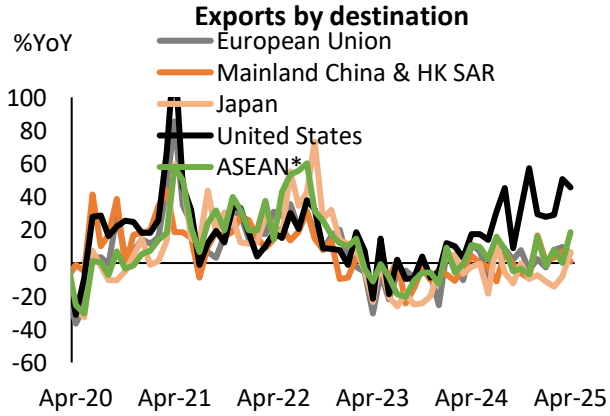
Malaysia

Nonetheless, the supply side points to some bright spots with construction sector growth still growing at double digits (14.2% from 20.7% in 4Q24) while growth in the manufacturing (4.1% from 4.2%) and services (5.0% from 5.5%) sectors were still resilient. Importantly, we estimate that 1Q25 GDP growth is close to our estimate of potential growth at 4.5% implying that the output gap is largely closed. BNM estimates that the output gap is still mildly positive based on potential growth estimates of 4-5%.

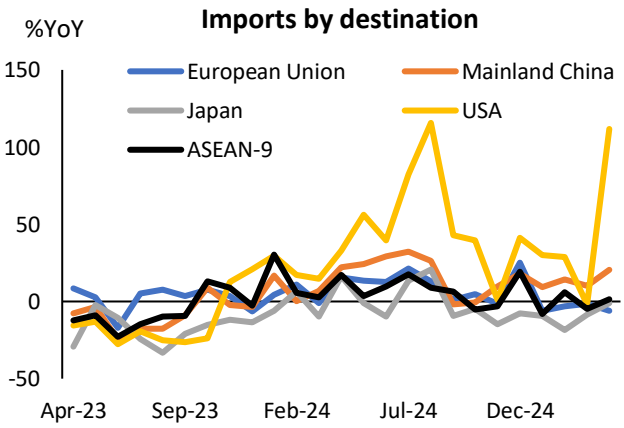


Source: CEIC; OCBC Bank

The growth outlook for the remaining three quarters is marred by heightened uncertainties on the external front. Malaysian authorities, led by Minister of Investment, Trade and Industry Tengku Zafrul Aziz, are negotiating with US counterparts to reduce the tariff from the reciprocal rate of 24%. The MITI minister said on 27 May that reducing the proposed tariff rate to 10% from 24% would be a good outcome. However, the extent of the negotiations and the outcome remain unclear ahead of the 9 July deadline. Moreover, a further extension of the tariff cannot be ruled out either.



*ASEAN includes Brunei, Indonesia, Philippines, Myanmar, Singapore, Thailand & Vietnam. Source CEIC; OCBC Bank

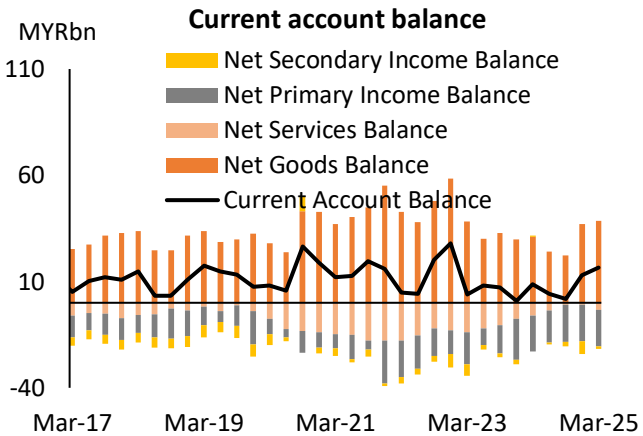


Source: CEIC; OCBC.

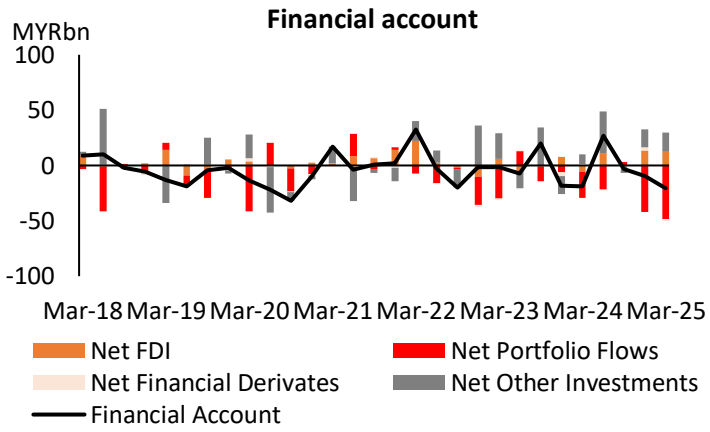
Malaysia

The growth outlook will be clearly demarcated by the imposition of tariffs and the rate of reciprocal tariffs. There will be some payback following the frontloading of exports to the US, which we estimate was MYR4.8bn from November 2024 to April 2025, once the tariffs are finalised. The trade balance, as a result, will likely become more volatile in 2H25. Although monthly deficits cannot be ruled out depending on the degree of export pull back, ultimately importation needs will be managed to keep the trade balance in check.

We do, however, expect the current account will remain in a surplus of 1.7% of GDP in 2025 from 1.4% in 2024. The current account surplus widened to MYR16.7bn (3.4% of GDP) in 1Q25 from MYR12.9bn (2.5% of GDP) in 4Q24. This was mainly driven by a wider goods surplus of MYR38.5bn (4Q24: MYR36.9bn) and narrower secondary income deficit (MYR1.2bn from MYR5.9bn in 4Q24). Although the services account deficit (MYR3.4bn from MYR1.0bn) widened in 1Q25, the outlook for tourist arrivals remains strong. The various events held under Malaysia's ASEAN Chairmanship and anecdotal evidence of solid tourist arrivals are signs of positive momentum.



Source: CEIC; OCBC.



Source: CEIC; OCBC.

Malaysian authorities have been reportedly negotiating on a broad range of criterion. These include addressing non-tariff barriers to reduce the impediments for American firms to do business in Malaysia, potentially increasing investments to the US through GLCs and GLICs, increasing safeguards for technology and tightening rules of origin. On 6 May, the government issued a statement that MITI will be sole issuer of non-preferential certificates of origin for exports to the US.

The National Geoeconomic Coordination Centre (NGCC) has been established to monitor and coordinate policies across the government. It is part of the wider government effort to monitor tariffs, sanctions, and supply chain risks across the globe to coordinate multi-ministry responses. The government has offered MYR1.5bn in additional loan guarantees and financing for Small and Medium Enterprises (SMEs) impacted by US tariffs. The government will also increase soft loans by MYR500mn through development financial institutions to support impacted SMEs.

Malaysia

While fiscal policy is more appropriate as a counter cyclical buffer to mitigate downside risks to growth, Malaysia's fiscal room will need to be used judiciously considering the government remains in fiscal consolidation mode. The government aims to narrow the fiscal deficit to 3.8% of GDP in 2025 from 4.1% in 2024. This rationalisation depends on raising additional revenues through broadening the tax base and rationalising RON95 prices.

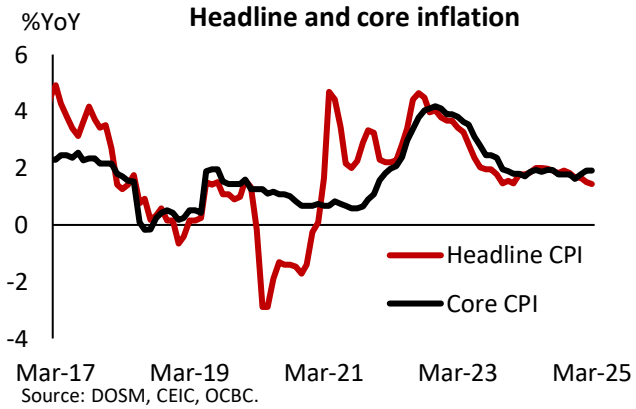
Tax changes regard sales and services taxes due on 1 May were postponed and the government had stated that these changes would yields MYR5bn in additional revenues for 2025. The sales and services tax will be broadened, effective 1 July, to include construction and financial services. Capital markets, foreign exchange and residential construction will remain exempt. There are new services taxes on private education and healthcare. The sales tax on premium items such as king crab, salmon, truffle, imported strawberries and silk, as well as industrial machinery will be taxed at 5% while racing bicycles and tungsten scraps will be taxed at 10%. The broadening of e-invoicing to all taxpayers was meant to come into effect in July 2025 but has been postponed to January 2026, for taxpayers with annual income/sales exceeding MYR1mn but not more than MYR5mn (phase 4). Phase 5 will cover the income group of up to MYR1mn and will commence on 1 July, 2026.

The timing and mechanism of RON95 rationalisation will be a more crucial lever of fiscal consolidation. Budget 2025 has accounted for a 14.4% YoY drop in 'subsidies and social assistance' expenditures. The assumption for Budget 2025 is that global oil prices will be lower at USD75-80/barrel compared to USD80-85/barrel in 2024. Year-to-date (13 June) WTI oil prices have averaged USD67.5/barrel, which could serve as a double-edged sword. On the one hand, lower prices could help the government by reducing the magnitude of the RON95 price hike given the reduced differential to RON97, which largely reflects changes in global oil prices. On the other hand, it reduces the fiscal burden by reducing the subsidy bill and allowing the government to kick the can down the road.

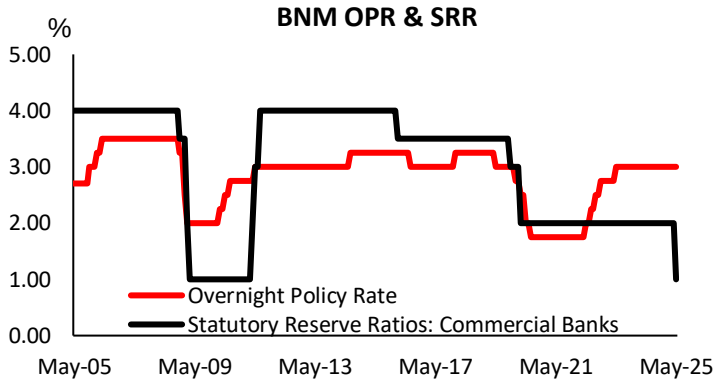
While officials have maintained that RON95 rationalisation will go through, the timeline has subtly moved from 'mid-2025' to 'second half 2025'. Our original assumption was that RON95 prices would be raised by 20-25% starting in June 2025. This did not materialise and now we are shifting our timeline to October 2025. The risk is that rationalisation is further delayed and/or the mechanism is adjusted to target smaller groups of the population with more measured price increases.

This change will result in subdued inflationary pressures in the near-term. We reduce our headline inflation forecast to 3.0% YoY from 3.7%, previously. This trajectory suggests that headline inflation will remain benign through to September, before it increases in 4Q25. BNM has a wider forecast range of 2.0-3.5%, likely accounting for some degree of RON95 rationalisation.

Malaysia



Source: DOSM, CEIC, OCBC.



Source: CEIC; OCBC Bank

Despite the uncertainty associated with the impending RON95 rationalisation, downside risks to growth are bigger policy priority. BNM sounded distinctly more dovish at its 8 May meeting, with comments from BNM Governor Abdul Rasheed Ghaffour in the following weeks confirming this shift in bias. We expect BNM to reduce its policy rate by a cumulative 50bps in 2H25.

The timing of the cut will depend on incoming activity data and progress on negotiations with the US. The pushing back of RON95 rationalisation to October from our previous assumption of June also opens up the possibility of a 25bp cut in July as inflationary pressures are likely to remain benign in the near-term. Meanwhile, further reductions to the Statutory Reserve Requirement (SRR) cannot be ruled out particularly if BNM assesses that liquidity conditions are constrained over a longer duration. BNM reduced the SRR to 1% effective 16 May 2025 and estimates that it will release MYR19bn worth of liquidity into the banking system.

Philippines

Philippines: Relative calm in a stormy ocean

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- Although we downwardly revise our 2025 GDP growth forecast to 5.5% YoY in 2025 from 5.9%, we forecast better GDP growth of 5.6% YoY in 2Q-4Q25, compared to 5.4% in 1Q25.
- We expect 2025 headline inflation to average 2.5% YoY, within BSP 2-4% target range, but widen our 2025 current account deficit forecast to 4.0% of GDP.
- We now expect a cumulative 50bps in rate cuts from Bangko Sentral ng Pilipinas (BSP) for the rest of 2025 from 25bps previously.

Policy continuity on the cards

The pivotal midterm election, a litmus test for President Ferdinand Marcos Jr. and the popularity of his administration, took place on 12 May. Twelve of the 24 Senate seats, all 317 House of Representative seats, as well as positions for governors, city mayors and municipal mayors were contested. Following the fallout between the Marcos and Duterte families, the twelve contested Senate seats were closely watched due to their implications on Vice President Sara Duterte upcoming impeachment proceedings in July.

Candidate	Affliated with	Percentage (%)
Bong Go	Duterte	6.33
Bam Aquino	Liberal Party	4.89
Ronald "Bato" dela Rosa	Duterte	4.85
Erwin Tulfo	Marcos Administration	4.00
Kiko Pangilinan	Liberal Party	3.58
Rodante Marcoleta	Duterte	3.56
Ping Lacson	Marcos Administration	3.53
Tito Sotto	Marcos Administration	3.46
Pia Cayetano	Marcos Administration	3.40
Camille Villar	Marcos Administration and Duterte	3.19
Lito Lapid	Marcos Administration	3.13
Imee Marcos	Duterte	3.11

Source: Commission on Elections, Various News Agencies, OCBC.

The opposition performed strongly in the contest for the 12 Senate seats – six winning senators are affiliated to the Marcos Administration while four winning senators are affiliated to the Duterte family. The other two winning senators are liberal opposition candidates. In response to the surprise gains, President Marcos issued a directive requesting for courtesy resignation from all his Cabinet secretaries, Head of Agencies of Cabinet rank, other Heads of Agencies, Presidential Advisers/Assistants[4]. He has retained his core economic team, implying policy continuity for economic and fiscal policies.

[4] Marcos quit call expanded to all government agency heads. Philstar, 24 May 2025.

Philippines

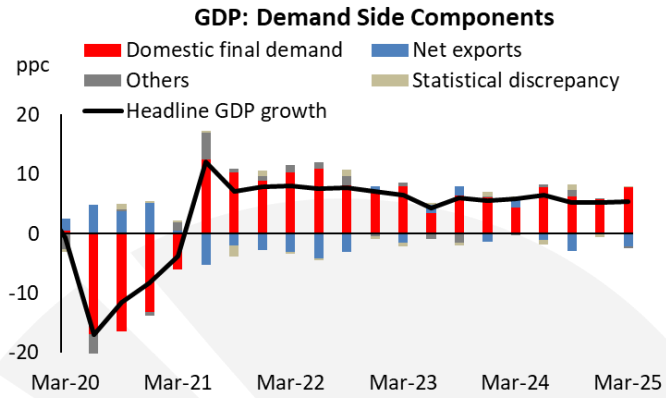
1Q25 GDP growth belies underlying improvements

The lower-than-expected 1Q25 GDP print belies signs of resilience in domestic demand. GDP growth barely improved to 5.4% YoY in 1Q25 versus 5.3% in 4Q24. However, the contribution of domestic final demand was higher at 7.9 percentage points (pp) in 1Q25 from 5.8pp in 4Q24. While government spending was turbocharged in the lead-up to the midterm elections on 12 May, household consumption, and investment spending improved in 1Q25. The improvements in household consumption are particularly encouraging considering the drag it posed to growth in 2024.

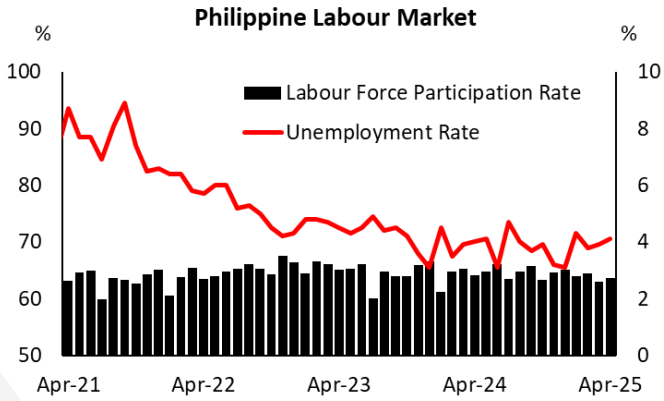
Corroborating the stronger domestic demand picture, imports of goods and services were up by 9.9% YoY in 1Q25 from 2.7% in 4Q24. Goods export growth picked up to 6.2% YoY versus 3.2% in 4Q24, mainly due to front-loading of some electronics exports to the US but services exports growth slowed to 7.2% YoY versus 13.2% in 4Q24. As a result, the negative contribution of net exports widened to 2.1pp in 1Q25 versus 0.1pp in 4Q24.

Downward revisions to 2025 GDP but path ahead is relatively stable

We downwardly revise our 2025 GDP growth forecast to 5.5% YoY in 2025 from 5.9%, previously. This implies slower growth momentum from 5.7% in 2024. We do, however, forecast better GDP growth momentum of 5.6% YoY in 2Q-4Q25, compared to 5.4% in 1Q25. This is unique to the Philippines, compared to other ASEAN economies, where we see lower growth momentum in the subsequent quarters. The government's official GDP growth target remains 6-8%, which we think will be hard to achieve this year, however, the Philippines will still likely remain one of the faster growing economies in this region.



Source: Philippine Statistics Authority, CEIC, OCBC.



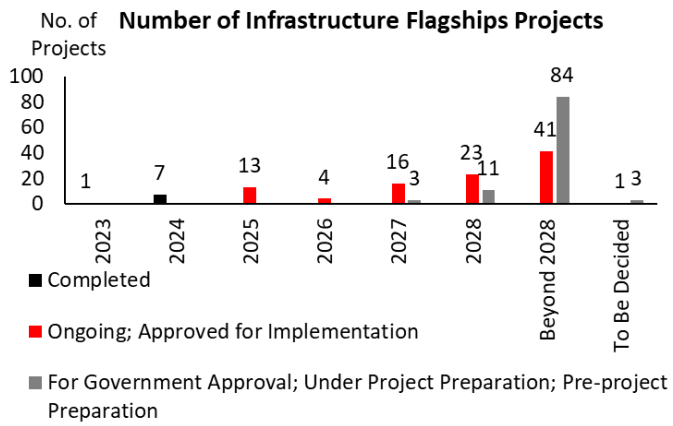
Source: Philippine Statistics Authority, CEIC, OCBC.

We see better domestic demand in the coming quarters helped by a normalisation of household spending, given the lagged impact of rate cuts and better credit growth. Private consumption spending is projected to remain robust at 5.6% YoY in 2Q-4Q25, up from 5.3% in 1Q25, underpinned by strong labour market conditions, low and stable inflation, and looser monetary policy settings. BSP has lowered its policy rate by a cumulative 100bps since August 2024, and we expect another 50bps in rate cuts for the remainder of the year.

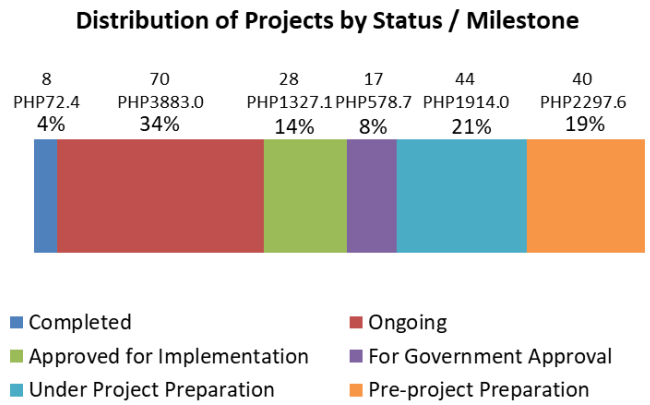
Philippines

Looser monetary policy settings will also benefit investment spending as the monetary transmission mechanism takes effect in the real economy. However, private sector investment spending will likely remain on the sidelines during this current period of external uncertainties. That said, there are signs that credit growth has remained strong. Consumer and investment related loans remained robust at 11.9% YoY in April from 12.4% in March.

We expect public sector capex to remain supportive of growth. The number of projects under the government's Infrastructure Flagship Projects have risen to 207, up from 185 projects (as of 31 March 2024), with an indicative cost of PHP10.1trn. We expect investment spending to accelerate by 7.1% YoY in 2Q-4Q25 versus 5.9% in 1Q25. These will more than offset the weakness in government consumption expenditures, following the sharp jump in 1Q25, as spending normalises following the elections. We expect government spending to normalise to 8.9% YoY in 2Q-4Q25, down from 18.7% in 1Q25.



Source: National Economic and Development Authority, OCBC.



Source: National Economic and Development Authority, OCBC.

This will also be supportive of continued fiscal consolidation efforts. The Development Budget Coordination Committee (DBCC) maintained the medium-term fiscal targets for FY25-28 at its 189th meeting on 2 December 2024. The fiscal deficit is budgeted to narrow to 5.3% of GDP in 2025, with reductions through to 3.7% by 2028, from 5.7% in 2024.

The consolidation in 2025 is expected to reflect past revenue increases from the introduction of new taxes and administrative measures. Tax revenues are budgeted to eased by 6.0% in 2025 from 15.6% in 2024, which is consistent with our nominal GDP growth forecast of 8% in 2025. Nevertheless, "these will be supported by recalibrated legislative measures that will provide a significant revenue boost to the government, such as the recently enacted VAT on Digital Services Act, and by tax administration reforms centred on digitalization.[5]" The Department of Finance even reaffirmed that the imposition of new taxes is not needed due to strong fiscal

[5] 189th DBCC Joint Statement on the Review of the Medium-Term Macroeconomic Assumptions and Fiscal Years. National Economic and Development Authority, 2 December 2024.

Philippines

position and withdrew the proposed Government Revenues Optimisation through Wealth Tax Harmonization (GROWTH) Bill[6].

The fiscal developments for the first four months of 2025 are mixed. Revenue growth slowed to 3.4% YoY in January-April 2025 from 15.6% in 2024. The moderation in revenue growth was mainly driven by lower non-tax revenues while tax revenue remained robust at 11.5% in January-April 2025. Expenditure increases were unusually high in 1Q25 owing to the pre-election boost but has since moderated in April, dropping by 8.0% YoY. We expect there will be continued normalisation of government consumption expenditures, with the priority given to capex. That said, counter cyclical fiscal policies, albeit targeted, cannot be ruled out.

Watchful of external risks

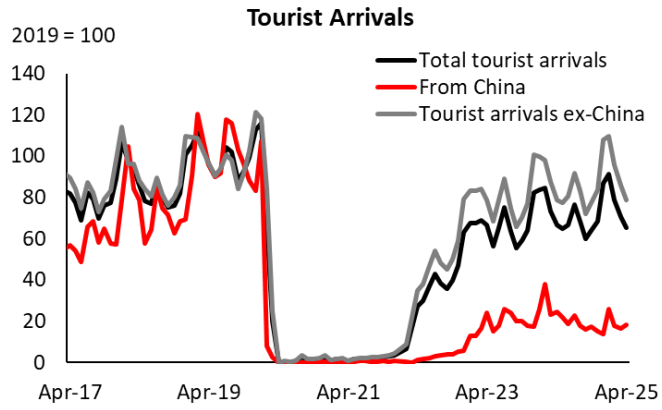
Although the reciprocal tariffs for the Philippines, set at 17%, is the lowest in the region, and the room for negotiation to a 10% baseline is the narrowest, the higher effective tariff rate for imports into the US from the Philippines will weigh on the Philippines export prospects. Moreover, sector specific tariffs could be more impactful since the Philippines' exports to the US are heavily weighted towards semiconductors. Bilateral tariff negotiations are underway, with the government having formed a technical working group that would continue discussions on the issue. Both sides will be working towards a framework during the 90-day moratorium period[7].

By contrast, tourism, services incomes and remittances flows are likely to remain well-supported, with growth in the Business Process Outsourcing (BPO) sector expected to remain resilient. According to the IT and Business Process Association of the Philippines (IBPAP), the BPO sector is projected to grow 5.2% YoY in 2025 versus 7% in 2024, generating USD40bn in revenue level[8].

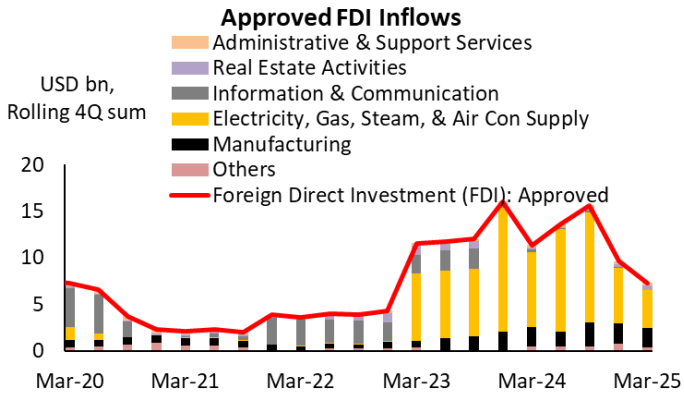
Visitors from South Korea, USA and Japan were the three largest source of tourist arrivals in the first four months to April. Year-to-April 2025, total tourist arrivals averaged 76.4% from 2019 levels. This is slightly lower compared to the same period last year, partly due to muted tourist arrivals from China (incl. HK SAR). Year-to-April 2025, Chinese tourist arrivals averaged 19.7% from 2019 levels, down from 28.0% in the same period last year.

[6] Bill hiking tax on capital gains 'not needed at this time' - DOF. GMA, 30 April 2025.
[7] Gov't forms TWG to continue negotiations on US reciprocal tariff. Philippine News Agency, 5 May 2025.
[8] More demand to fuel ITBPM sector to $40-B revenue in 2025. Philippine News Agency, 29 April 2025.

Philippines



Source: Department of Tourism, CEIC, OCBC.



Source: Philippine Statistics Authority, CEIC, OCBC.

Still a 'twin deficit' economy

We forecast that the current account deficit will widen to 4.0% of GDP in 2025 from 3.8% in 2024. The risk is that the current account deficit would be wider depending on the outcome from sector specific tariffs. As such, financing the current account deficit is crucial. Approved FDI inflows, on a rolling four quarter sum basis, have declined by 35.6% YoY to USD7.3bn in 1Q25, down from USD9.6bn in 4Q24. Nevertheless, the liberalisation of FDI rules and potentially strategic partnerships with the US could see the Philippines gaining further traction in terms of FDI over the medium-term.

Benign inflationary pressure

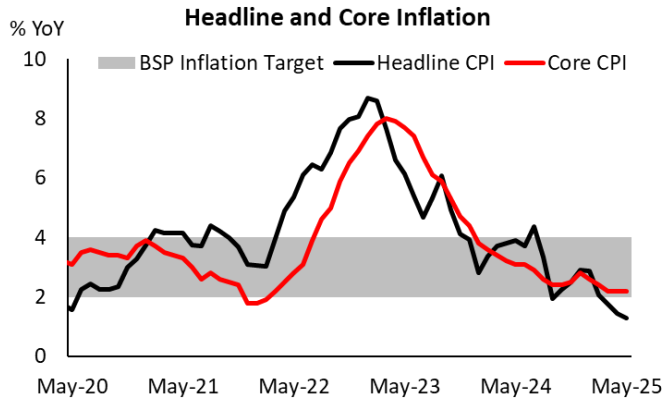
Meanwhile, inflationary pressures have subsided sharply driven by lower food and energy prices. Headline CPI has averaged 1.9% YoY in Jan-May 2025 versus 3.2% in 2024, sitting at the lower end of BSP's 2-4% target range. Similarly, core inflation (Jan-May 2025) slowed to an average of 2.3% YoY versus 3.0% in 2024.

We expect headline inflation to average 2.5% YoY in 2025, implying a pickup in headline CPI for the rest of the year but still within BSP 2-4% target range. Food inflation is expected to remain soft due to direct government policy measures such as the reduction of rice tariffs through Executive Order 62, and more broadly, moderating global food prices.

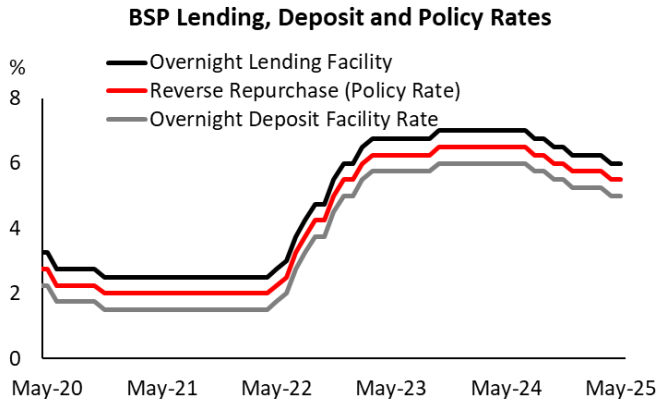
Lower global energy prices will also help keep inflationary pressures in check. Year-to-date, as of 13 June 2025, Brent crude has averaged USD70.7/bbl, representing a 14.6% YoY decline from the same period in 2024. Our house view is for Brent crude to average USD67/bbl in 2025, suggesting a decline of ~5.6% YoY in the coming months.

Philippines

BSP, at its 10 April meeting, forecasted risk-adjusted headline inflation[9] of 2.3 % YoY in 2025. According to the BSP, "the risk to the inflation have also eased and continue to be broadly balanced from 2025 to 2027. Upside pressures come from possible increases in transport charges, meat prices, and utility rates. Meanwhile, downside risks are linked to the continuing effects of lower tariffs on rice imports and the expected impact of weaker global demand."



Source: Philippine Statistics Authority, Bangko Sentral ng Pilipinas, CEIC, OCBC.



Source: Bangko Sentral ng Pilipinas, CEIC, OCBC.

Door for further rate cuts

Lower inflationary pressures will allow the BSP to continue its monetary policy easing cycle path. BSP Governor Eli Remolona has affirmed numerous times that there is room for at least two more 25bp rate cuts[10]. Nevertheless, he had warned against excessive reductions that could overstimulate demand. BSP has already delivered a 25bp in rate cut at its April meeting this year. Our baseline is now for a cumulative 50bps in rate cuts for the rest of 2025, taking the policy rate to 5.00% by end-2025. The balance of risks is skewed towards more rather than fewer cuts given the downside risks to growth stemming from global factors.

[9] At its 16 November meeting, BSP introduced a baseline and risk adjusted forecast. However, the decision to release both set of numbers after each MPC meeting is still under discussion. The risk-adjusted forecast is determined by adding the baseline inflation forecast to the probability weighted impact of the risks (both upside and downside risks) to inflation outlook. BSP Mulls Release of 2 Inflation Forecasts as Price Pressures Persist. Manila Bulletin, 17 November 2023.

[10] BSP sees 2 more rate cuts this year. Philstar, 24 May 2025.

Singapore

Singapore: From trade tailwinds in 1H25 to a slower throttle in 2H25?

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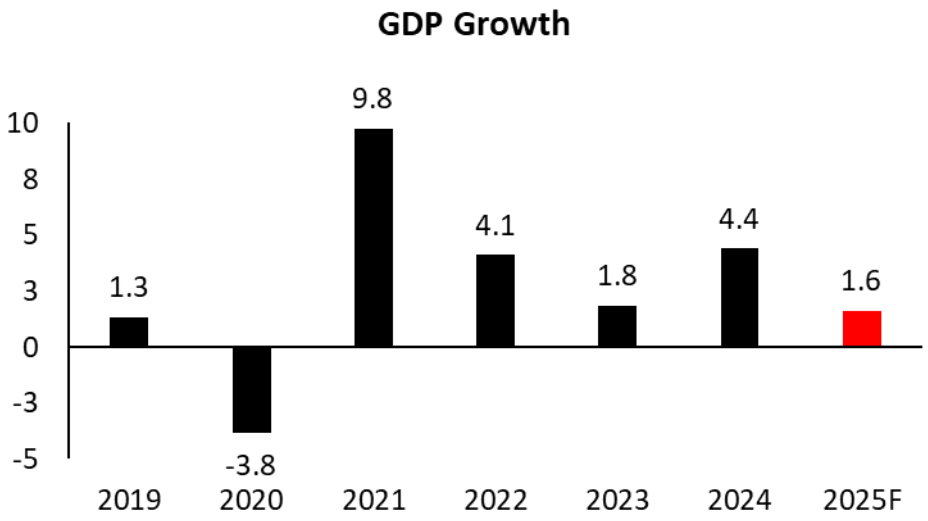
- Our 2025 GDP growth forecast is at 1.6% YoY compared to 4.4% in 2024. Economic growth was better than expected in 1Q25 but we do not rule out a technical recession for 2Q25. Front-loading of exports to the US, some resilience in services and construction likely bolstered growth in 1Q25 even as the outlook for the 2H25 is subject to a heightened degree of uncertainty. The outcome of tariff negotiations with the US for Singapore's key trading partners and potential sector specific tariffs on semiconductors and pharmaceuticals will be crucial for the 2H25 outlook.
- Core inflation has decelerated sharply over the past few months, notwithstanding the modest uptick in April. A cooling domestic labour market, strong S$NEER, limited price pressures from commodities and easing domestic demand will likely keep inflationary pressures in check. We forecast average core inflation at 1.2% YoY in 2025 from 2.8% in 2024, with average headline inflation at 0.9% in 2025 from 2.4% in 2024.
- The Monetary Authority of Singapore (MAS) reduced the rate of appreciation of the S$NEER policy band at its January and April meetings. The window for additional monetary policy easing is open, in our view, but the policy accommodation is likely to be supplemented by the fiscal side with potential assistance forthcoming from the Economic Resilience Taskforce. The Economic Resilience Taskforce has three main workstreams focused on communication, addressing immediate challenges and developing long-term strategies and responses.

The Singapore economy in 2025 is like a seasoned marathon runner, starting with a steady clip but acutely aware of the hurdles ahead. The first half of the year saw the Lion City navigating a global economic obstacle course, with slowing global growth momentum and shifting trade winds nipping at its heels. Yet, as the second half unfolds, the question is whether global trade will eventually hit the skids and in turn will Asian economies including Singapore also hit the "proverbial wall".

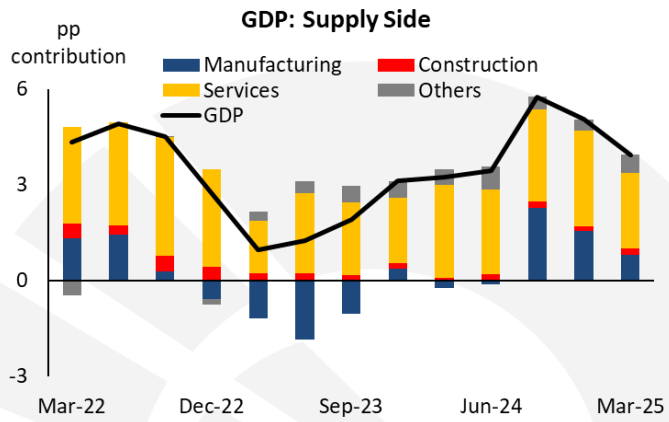
1Q25 GDP growth turned out to be better than expected, with the upward revision from advance estimates of 3.8% YoY (-0.8% QoQ sa) to 3.9% YoY (-0.6% QoQ sa). This was a surprise as manufacturing growth was to be revised down to 4.0% YoY due to the softer March industrial production data. However, the compensating factors were upward adjustments to the services (from 3.4% YoY to 3.6% YoY) and construction (from 4.65 YoY to 5.5% YoY) sectors. While the 1Q25 GDP growth is still a moderation from 4Q24 growth of 5.0% YoY (0.5% QoQ), it nevertheless marks a healthy start to the year, aided by wholesale trade, manufacturing and finance and insurance sectors.

Singapore

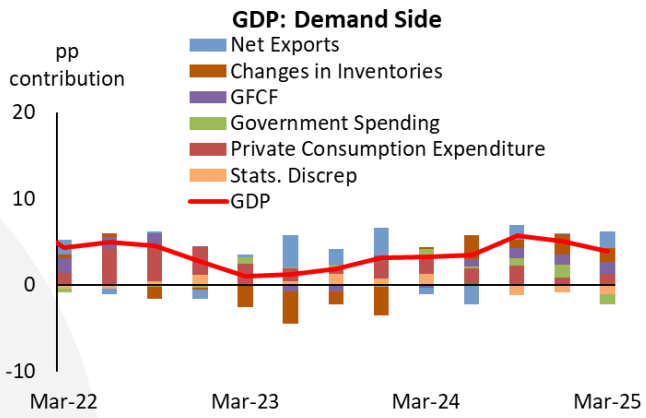


Source: Singstat, CEIC, OCBC.

By sectors, the manufacturing growth momentum eased from 7.4% YoY in 4Q24 to 4.0% YoY in Q25, despite higher output in electronics, precision engineering and transport engineering clusters. The construction sector maintained its healthy growth momentum at 5.5% YoY in 1Q25 as public infrastructure projects and private commercial developments kept cranes busy across the island. For the services sector, growth was buoyed by transportation & storage (5.2% YoY, mainly due to an increase in air passenger volumes and container throughput), finance & insurance (4.5% YoY due to robust net fees and commissions in the banking and fund management segments), information & communications (4.4% YoY), while real estate surprisingly accelerated to 7.1% YoY supported by a hike in private residential property and private commercial and industrial property activities.



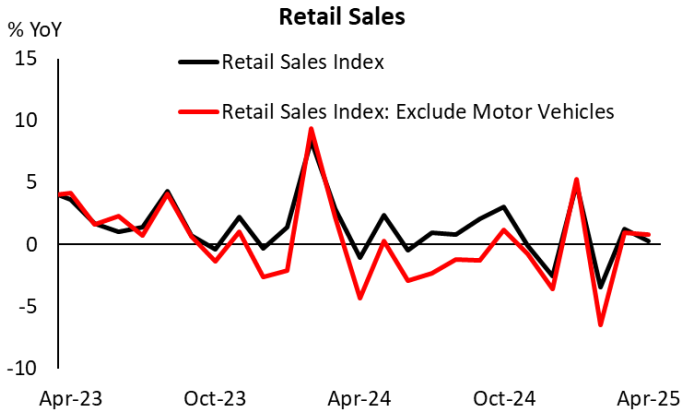
Source: MTI, Singstat, CEIC, OCBC.



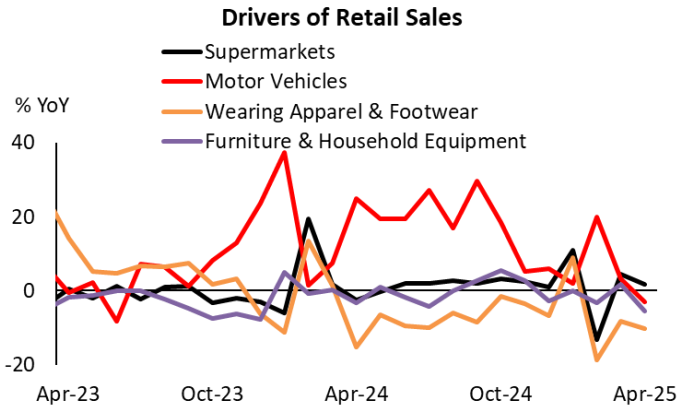
Source: MTI, Singstat, CEIC, OCBC.

Singapore

Even the retail trade segment stabilised at 0.1% YoY in 1Q25 after three consecutive quarters of contraction, albeit this was largely attributable to a pickup in motor vehicle sales. Meanwhile, the weakest services links were accommodation that reverted to contraction territory (-0.9% YoY versus 4.2% in 4Q24) due to a drop in total gross lettings, attributable to the upscale, luxury and economy hotel segments and food & beverages services which extended its losing streak for the fourth straight quarter at -0.2% YoY amidst lower sales volumes at café, food courts & other eating places, restaurants and fast-food segments. It appears that locals are opting for more affordable food choices.



Source: Singstat, CEIC, OCBC.



Source: Singstat, CEIC, OCBC.

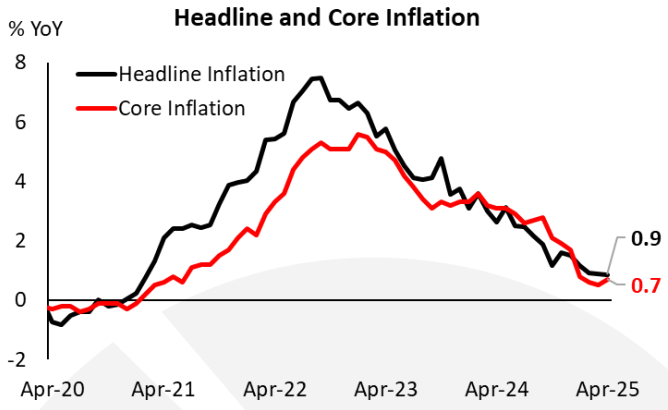
Despite the upbeat 1Q25 GDP growth revision, MTI held for to the official 2025 growth forecast of 0-2% YoY. More importantly, the rhetoric sounds distinctly dovish. MTI noted that outward-oriented sectors is tipped to slow over the year and a technical recession is possible. In addition, MTI said its growth forecast could be adjusted as necessary in the coming quarters. In particular, US tariffs will adversely impact the manufacturing sector through its export exposure to the US market as well as a slowdown in global end-markets including Eurozone and China. In turn, trade-related services will see some negative spillover effects – wholesale trade volumes may weaken after frontloading activities dissipates, especially in 2H25, which again will negatively affect the transportation & storage sector due to softer demand for shipping and air cargo services.

Moreover, finance & insurance sectors could also be weighed down by weaker trading activity and also payments activity as business and consumer spending moderates. With the cut back in discretionary spending, for example, IT and marketing, this will also dampen growth in the infocomms and professional services sectors. On the domestic front, the softening in labour market conditions is likely to mean lacklustre retail trade and food & beverage services, since Singaporeans continue to spend abroad to take advantage of the SGD strength. MTI cited downside risks in the elevated economic uncertainty contributing to a pullback in economic activity, a re-escalation in tariff actions, and disruptions to the global disinflation process and recession risks that could destabilise capital flows and cause banking and financial market indigestions.

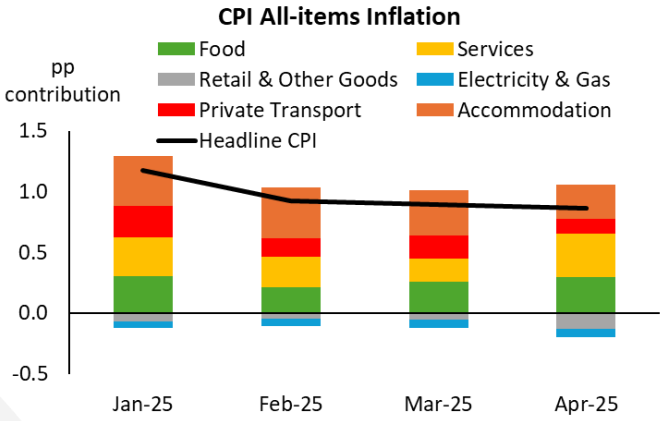
Singapore

Our 2025 GDP growth forecast remains at 1.6% YoY given the softer global growth prognosis and the tariff-related uncertainties. A technical recession remains on the cards with our forecast of a further deceleration in 2Q25 growth to 2.5% YoY (-0.3% QoQ sa). Recent developments include the 90-day stay on reciprocal tariffs, an initial US-UK trade deal as well as a 90-day US-China tariff truce (marking an important de-escalation to the earlier tit-for-tat retaliatory phase) and glimmer of a US-China deal, nevertheless, some damage to business and consumer confidence has already been done. Financial markets have been very volatile in April post-'Liberation Day' announcements on 2 April, and post-Moody's downgrade of the US sovereign credit rating and President Trump's tax-cut plans continue to cause market palpitations. In addition, sectoral tariffs such as on semiconductors and pharmaceuticals may still be on the cards.

MAS noted that the monetary policy stance remains appropriate for now. USDSGD had dropped below the 1.28 handle amidst the broad USD weakness. The S$NEER is trading closer to the stronger end of its parity band, notwithstanding that subsiding core inflation had led the MAS to flatten the S$NEER slope twice in January and April this year. While the official 2025 headline and core CPI forecasts are currently at 0.5-1.5% YoY, there are still potential downside risks to the inflation picture as demand softens. The softer-than-expected 1Q25 core CPI outturn suggests that domestic demand conditions are easing in line with the cooling domestic labour market. Commodity prices remain stable, reflecting the global growth demand conditions. Assuming some reciprocal tariffs resume in 2H25, even if they are lower than the initial levels announced on Liberation Day, the drag on global and regional growth will likely linger.



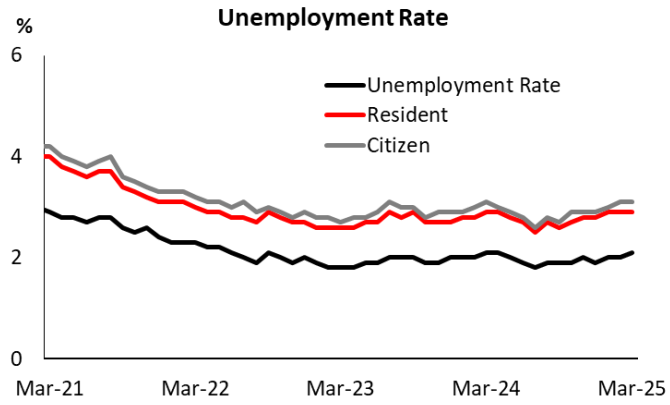
Source: Singstat, CEIC, OCBC.



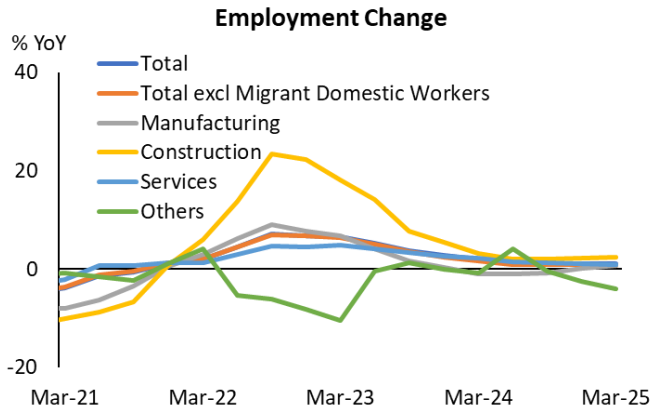
Source: Singstat, CEIC, OCBC.

At this juncture, the window for additional monetary policy easing is open, but the policy accommodation is likely to be supplemented by the fiscal side with potential assistance forthcoming from the Economic Resilience Taskforce. The previous instances of a neutral S$NEER slope was back in 2020 during Covid pandemic and from April 2016 – April 2018 during global growth slowdown. The overall unemployment rate has also risen from 1.9% in 4Q24 to 2.1% in 1Q25, albeit this is still relatively low by historical comparison.

Singapore

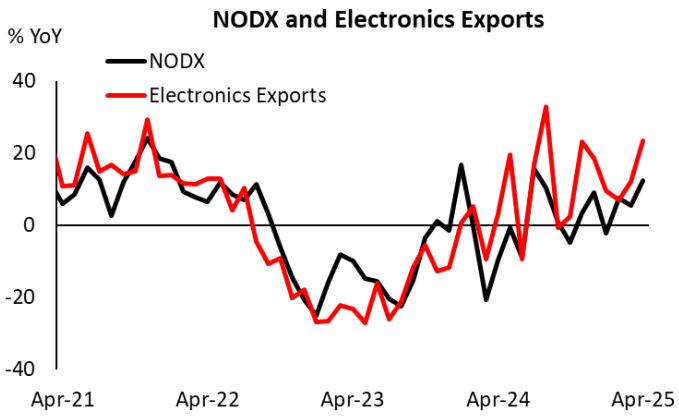


Source: MOM, CEIC, OCBC.

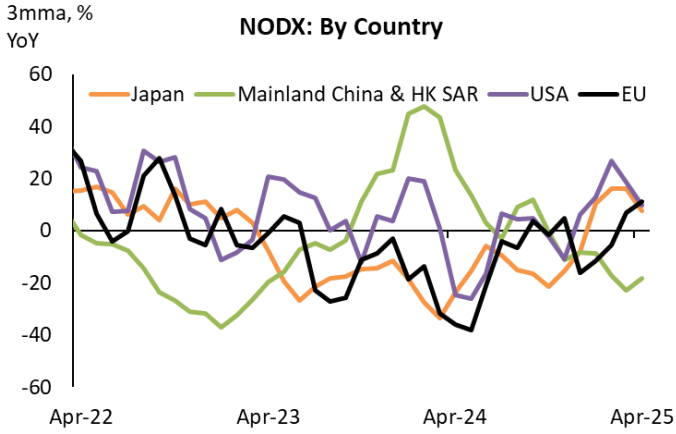


Source: MOM, CEIC, OCBC.

The better-than-expected 1Q non-oil domestic exports (NODX) growth of 3.3% YoY is likely attributable to front loading activities, driven by electronics exports (9.5% YoY). This was also reflected in the 19.2% YoY surge in NODX to the U.S., attributable to U.S. tariff concerns. In fact, Enterprise Singapore emphasized the weakening in external outlook and heightened trade policy uncertainties that focuses on the lower bound of their 1-3% full year NODX growth forecast.



Source: Enterprise Singapore, CEIC, OCBC.



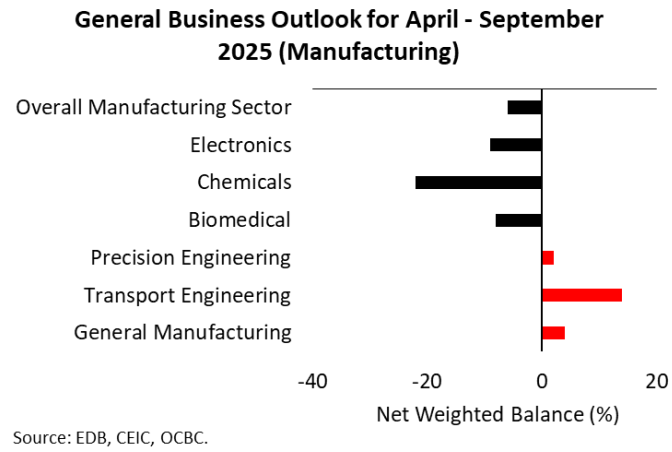
Source: Enterprise SG, CEIC, OCBC.

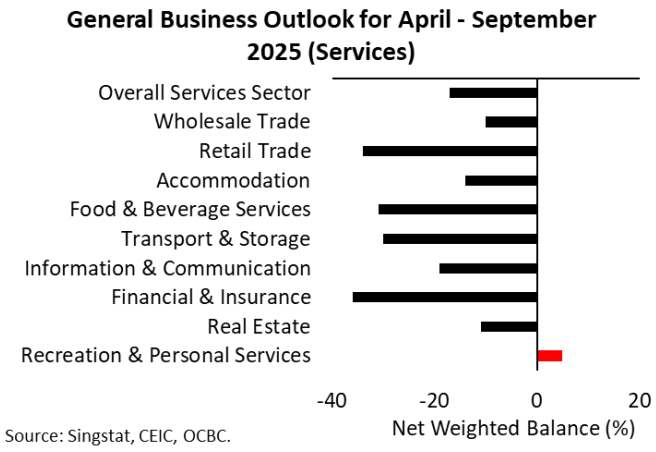
Our 2025 NODX growth forecast of -1 to 1% YoY essentially builds some buffer for softer global growth prospects and a potentially bumpy road ahead for tariff agreements, notwithstanding the initial market optimism about the U.S.-UK deal and the U.S.-China truce. It could well be a story of two halves with front loading in 1H25, followed by a deceleration in 2H25. In fact, NODX growth could contract YoY as early as 3Q25.

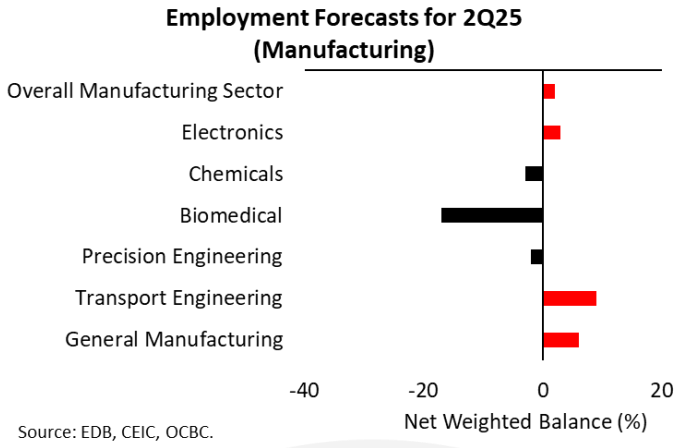
On the political scene, the general election was held on 3 May saw a resounding mandate for the incumbent with 87 out of 97 seats and 65.57% of the vote. This is the party's best performance since 2011 and assures market participants of substantial policy continuity amidst the 4G leadership renewal, notwithstanding the retirement of several long-serving senior ministers. The vote for stable hands amid the geopolitical volatility and rising trade tensions suggest that Singapore will also continue to play a neutral and pragmatic role in a fragmented world.

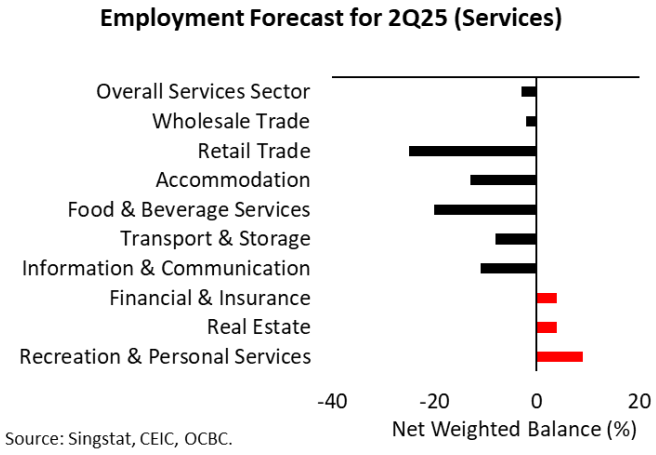
Singapore

The next lap should be one of cautious optimism. While the global economic headwinds persist, Singapore should be able to avoid an outright recession this year, even if it risks a technical recession. Business expectations have softened, with trade-related sectors bracing for the famine after the frontloading ahead of tariffs. Policymakers are actively engaging with the US administration to secure concessions on sectoral tariffs such as for semiconductors and pharmaceuticals.









The marathon isn't over, but Singapore knows how to strategically pace itself. The hurdles of 1H25 — global policy uncertainties, tariffs and China's slowdown remain intact for 2H25. For Singapore, the story is never about sprinting, but endurance to finish the race - to achieve that, it has to invest in AI, digital economy, green and sustainable leadership, skills training, building economic resilience. The Singapore Economic Resilience Taskforce (SERT) is aptly named as it is not just to help businesses and workers navigate the immediate uncertainties arising from the US tariffs and related global developments, but also to strengthen Singapore's resilience and position Singapore to thrive in the new economic landscape.

South Korea

South Korea: To avoid a recession

Tommy Xie
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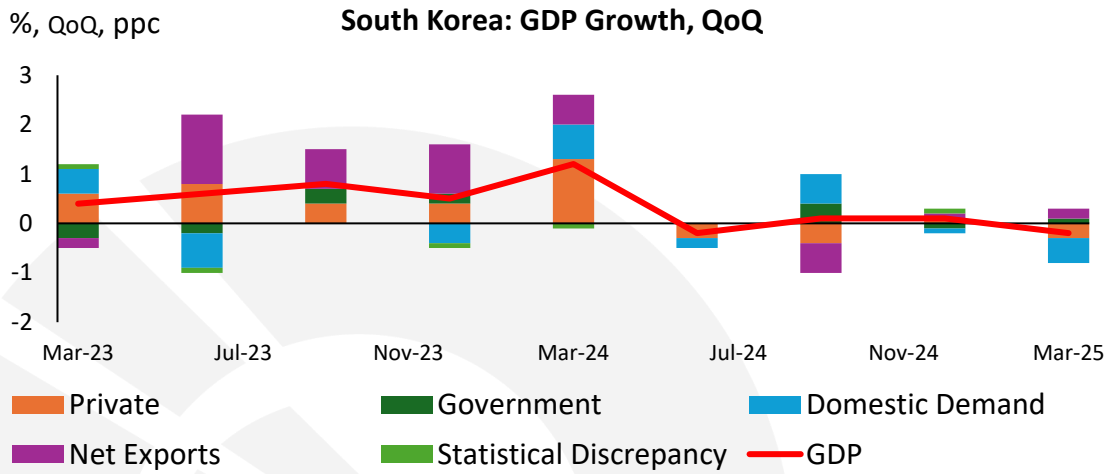
- A weak start due to delayed domestic demand recovery, a sharp correction in the construction sector, and faltering exports.
- The Bank of Korea (BoK) delivered 50bps of cumulative policy rate cuts year-to-date and maintained a dovish bias. We expect BOK to cut another 50bps this year to support the growth.
- Stabilizing political conditions, anticipated fiscal stimulus, and potential equity market-friendly measures under the new administration are likely to provide a backstop to growth.

The economy contracted by 0.2% QoQ sa in 1Q25, reversing the 0.2% expansion recorded in 4Q24. This marks the weakest quarterly performance since the pandemic-era shock, with YoY growth decelerating sharply to just 0.1% from 1.2% in the previous quarter. The downturn was broad-based, driven by simultaneous weakness in private consumption, investment, and trade.

Household consumption edged down 0.1% QoQ, reversing modest gains in the prior quarter, as consumer sentiment deteriorated in the aftermath of former President Yoon Suk-yeol's failed martial law declaration in December 2024 and his subsequent impeachment. Construction investment fell by 3.1% QoQ—its steepest drop since 2020—marking the fifth consecutive quarterly decline. The sector remains under pressure from falling property prices, rising default risks among mid-sized developers, and reduced public infrastructure spending, forming a negative feedback loop. Facility investment also contracted by 0.4% following a late-2024 surge in semiconductor-related equipment purchases.

Chart 1: Contribution to South Korea's growth



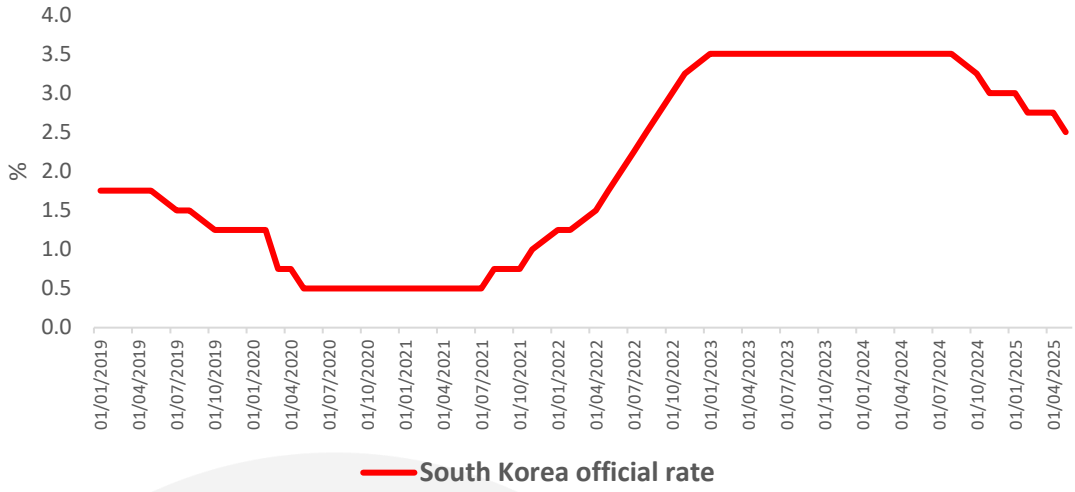
Source: BoK, Bloomberg, OCBC

South Korea

Net exports made a small positive contribution to growth in 1Q25, as imports declined more sharply than exports. However, the outlook for trade remains fragile. While the U.S. has temporarily paused its reciprocal tariff policy, the uncertainty surrounding future trade actions—particularly the Trump Administration's sectoral tariffs on autos—has already impacted sentiment and flows. South Korea's exports fell 3.7% MoM sa in May, with YoY growth sliding to -1.3% from +3.7% in April. The decline was broad-based across major export categories, excluding semiconductors.

In response to the slowdown, the BoK cut its 2025 GDP growth forecast to 0.8%, down from the previous estimate of 1.5%, citing delayed domestic demand recovery, a sharp correction in the construction sector, and faltering exports. The central bank has delivered 50bps of cumulative policy rate cuts year-to-date and maintained a dovish bias. Four out of six MPC members are open to an additional rate cut in the next three months. While Governor Rhee did not provide guidance beyond the near term, he acknowledged the need for sustained policy support—either fiscal or monetary—through 2025 and 2026, although he noted that rates below 2% are unlikely.

Chart 2: South Korea has delivered two rate cuts this year.



Headline inflation moderated further, with CPI easing to 1.9% YoY in May from 2.1% in April—the lowest since November 2024—driven entirely by lower agricultural goods prices. Core inflation (excluding food and energy) inched down to 2.0% YoY from 2.1%, while sequential momentum also slowed to 0.1% MoM sa from 0.3%. The disinflation trend reinforces the case for continued monetary easing.

The 3 June presidential elections brought an end to six months of political uncertainty. Lee Jae-myung of the Democratic Party (DP) secured a decisive victory, granting the DP control of both the executive and legislative branches until at least 2028. The DP had already secured an absolute majority in the National Assembly in the 2024 general elections.

South Korea

With the progressive bloc holding over 60% of parliamentary seats, cabinet formation is expected to proceed swiftly. Markets will closely monitor the nomination of the next finance minister, as the new administration sets its economic agenda.

The incoming government is expected to pursue more expansionary fiscal policy. Senior DP officials have hinted at a supplementary budget of at least KRW20trn, with President Lee suggesting the figure could exceed KRW35trn. Additionally, the administration must prepare the 2026 budget for submission by end-August, creating another opportunity for fiscal stimulus.

In terms of foreign policy, the new government is expected to maintain a strong alliance with the United States. At the same time, Mr. Lee's pragmatic approach to relations with China, Japan, and Russia may contribute to regional stability. Easing tensions with North Korea and broader diplomatic engagement could help reduce geopolitical risk premia.

On U.S.–Korea trade talks, technical progress has been reported by local media, and attention is turning toward a potential "July package." Trade-related developments are likely to dominate the policy narrative in the coming months.

Stabilizing political conditions, anticipated fiscal stimulus, and potential equity market-friendly measures under the new administration are likely to provide a backstop to growth. These developments may also reduce the need for aggressive monetary easing, though we still expect the BoK to deliver additional 50bps rate cuts in 2H25, given the subdued inflation backdrop and ongoing domestic demand weakness.

We maintain our 2025 GDP growth forecast at 1.0%, supported by coordinated fiscal and monetary policy. Risks remain tilted to the downside, particularly from the external environment, but policy normalization and improved confidence post-election offer a constructive path for recovery.

Taiwan

Taiwan: Risks may rise in 2H25

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- Real GDP grew by 5.48% YoY in the 1Q25. On quarter-on-quarter (qoq) seasonally adjusted basis, growth accelerated from 1.62% to 1.76%, marking the fourth consecutive quarter of economic expansion.
- Following the stronger-than-expected GDP expansion in Q125, we have revised our 2025 full-year GDP growth forecast upward 3.3% YoY, up from 2.7%. While a 90-day pause has been implemented on the "reciprocal" tariffs, a 32% of tariff rate applied to Taiwanese goods could still be considered "high" and this could put a significant downside pressure on the economic prospects, particularly in 2H25 if no trade deal is struck.
- Going forward, the momentum behind TWD strength may have legs if the broader de-escalation narrative holds, if tariff implication on growth proves more manageable than feared, and if broad-based USD weakness permeates. Our updated USD/TWD forecasts are at 29.60 by the end of this year.

1Q25 GDP surprised on the upside

Real GDP grew 5.48% YoY in 1Q25, above expectations (OCBC forecast: 3.80%; BBG consensus: 3.60%). On quarter-on-quarter (qoq) seasonally adjusted basis, growth accelerated from 1.62% to 1.76%, marking the fourth consecutive quarter of economic expansion.

The robust economic performance was driven by strong exports of electronic information and communication products, coupled with increased investments in machinery equipment, construction, and intellectual property products. Notably, exports of goods and services surged 20.29% YoY in 1Q25, up sharply from 8.89% YoY in 4Q24. Gross capital formation expanded by 15.98% YoY, maintaining four consecutive quarters of double-digit growth despite a moderation from 23.78% YoY in the prior quarter. However, growth in private consumption slowed to 1.36% YoY (down from 2.12% YoY in 4Q24), while government expenditure declined to 0.44% YoY (from 2.43% YoY in the previous quarter), reflecting relatively weaker domestic demand.

Analysing the contributions to the headline GDP growth, gross capital formation remained the primary driver, contributing 4.01 percentage points (pp) to GDP growth.Net exports added 0.77pp, underscoring the economy's reliance on external demand. Private consumption contributed 0.63 pp, while government consumption accounted for 0.06 pp.

Taiwan

Chart 1: Gross capital formation and net exports were the main contributors

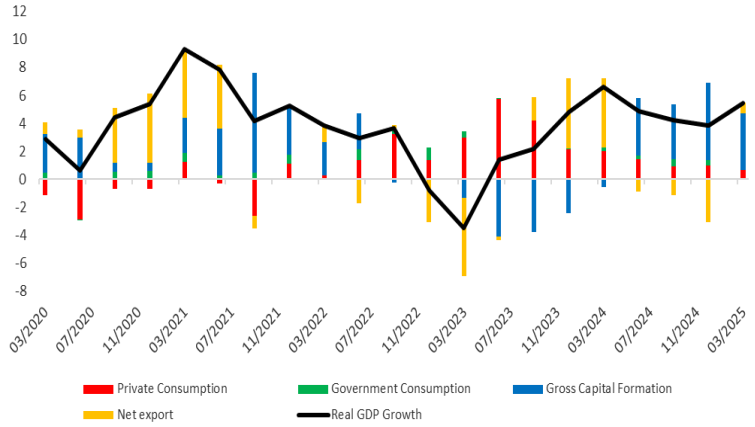


Table 1: Taiwan advance 1Q25 GDP (Percentage Contribution, by Expenditure)

Component	2023	2024	3Q24	4Q24	1Q25 (p)		2025F DGBAS	2025F CBC
Domestic Demand	1.17	5.48	6.30	8.11	5.46		2.15	
-Private Expenditure	8.32	2.81	1.84	2.12	1.36		1.64	
-Public Expenditure	0.88	2.46	4.03	2.43	0.44		2.39	
-Gross Capital Formuation	-10.30	12.45	17.06	23.78	15.98		5.6	
External Sector								
-Exports	-4.32	8.71	8.88	8.89	20.29		11.44	
-Imports	-5.73	11.41	13.88	18.32	24.43		11.98	
Real GDP	1.31	4.59	4.21	3.82	5.48		3.1	3.05

Source: DGBAS, OCBC Research

Revising our 2025 growth forecast but remain cautious in 2H25

Following the stronger-than-expected GDP expansion in 1Q25, we have revised our 2025 full-year GDP growth forecast upward to 3.3% YoY from 2.7%. While a 90-day pause has been implemented on the "reciprocal" tariffs, a 32% of tariff rate applied to Taiwanese goods would still be considered "high" and this could put a significant downside pressure on the economic prospects, particularly in the second half of the year if no trade deal is forthcoming.

In 2024, total exports to the U.S. reached USD111.4bn, accounting for 23% of total exports. Among the key export categories, information and communication products remain dominant, comprising 51% of exports. While shipments to the U.S. have remained strong ahead of the 90-day tariff pause expiration on July 9, markets await further data to assess the impact of reciprocal tariffs on Asia's economy and trade patterns. We believe the direct or indirect risks from these tariffs could still exert a drag on exports, particularly in 2H25.

On central bank, the Central Bank of the Republic of China (CBC) kept its benchmark rate unchanged at 2.0% at its 20 March meeting. In its Monetary Policy Committee (MPC) statement, the bank reiterated its commitment to "adjust monetary policy timely and appropriately to fulfil statutory duties of maintaining financial and price stability and fostering economic development within the scope of aforementioned objectives".

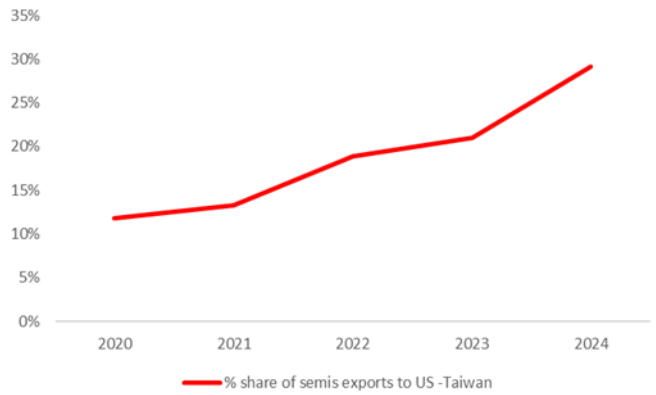
Taiwan

To curb housing speculation and channel credit non-homeowners seeking owner-occupied housing, the CBC has maintained selective credit controls and reserve requirement ratios (RRR) unchanged since implementing these measures in December 2020. Consequentially, housing transactions, real estate loans, and loan-to-value (LTV) ratios have turned lower since the bank implemented these controls since December 2020. We expect the benchmark rate to be 1.875% by the end of 2025, i.e. one 12.5bps cut by year end.

Chart 2: Taiwan stands for the 1st largest semis supplier to the US

Top 10 economies of semiconductors export to the US, 2024	Import value (In Acutal Dollars)	% of share
Taiwan	11,127,703,928.00	29.14%
Malaysia	8,917,218,121.00	23.35%
Israel	4,149,468,322.00	10.87%
South Korea	2,415,395,028.00	6.33%
Ireland	1,935,781,623.00	5.07%
Mexico	1,486,669,137.00	3.89%
Thailand	1,063,966,392.00	2.79%
Costa Rica	1,041,614,719.00	2.73%
Japan	993,919,240.00	2.60%
Philippines	955,758,410.00	2.50%

Chart 3: % share of semis exports going to the US



Source: US International Trade Commission, Bloomberg, OCBC Research

What's next after the recent spike in Taiwanese dollar?

On 2 May, the Taiwanese dollar (TWD) surged by over 4% in a single day, notching its largest gain since 1988. The massive gains have been catalysed by the prospects of a dialogue between US and China, thin market liquidity and the absence of FX intervention on that day. The faster-than-expected pace of TWD appreciation caught many market participants off guard, triggering a rapid rush to convert U.S. dollars (USD) into the local currency.

Following the wildest gains not seen since the 1980s, CBC moved to curb currency speculation and prioritize stability. This intervention reflects growing domestic concerns over the impact on importers, exporters, and overall economic equilibrium. More fundamentally, Taiwan remains on the US Treasury's currency monitoring list, and allowing the TWD to strengthen (in line with other FX) could help pre-empt any accusations of currency manipulation especially at a time where Taiwan's role in global chip supply chains is under the spotlight. A more market-determined exchange rate ahead of potential trade negotiations may also serve as a strategic buffer during diplomatic discussions. Should USD weakness persist, we anticipate more proactive adjustments to hedge ratios as market participants recalibrate risk exposures.

Going forward, the momentum behind TWD strength may have legs if the broader de-escalation narrative holds, if tariff implication on growth proves more manageable than feared, and if broad-based USD weakness permeates. Our updated USD/TWD forecasts are at 29.60 by the end of this year.

Taiwan

Table 2: OCBC's forecasts

OCBC's Forecast	Jun-25	Sep-25	Dec-25	Mar-26
USD-TWD	30.00	29.70	29.60	29.50
Taiwan Discount Rate	2.00%	2.00%	1.88%	1.88%

Source: Bloomberg, OCBC Research

Chart Taiwan net portfolio flows

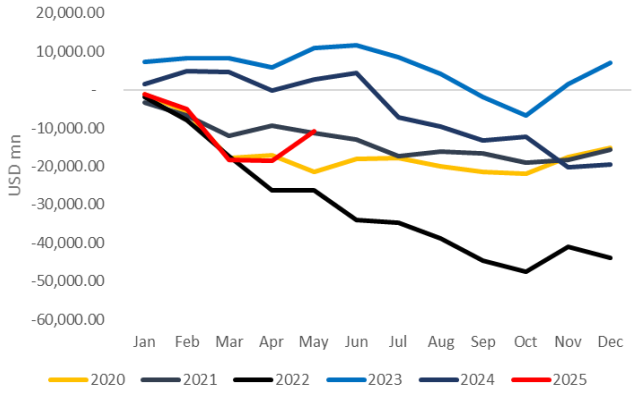
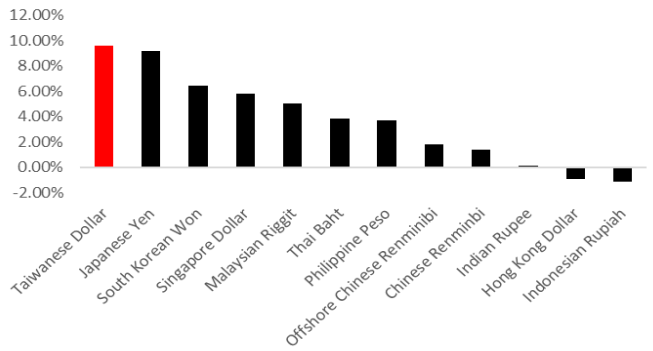


Chart 5: Asian currencies versus USD (YTD 2025, %)



Thailand

Thailand: Challenges all around

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- We expect GDP growth to slow to 2.0% YoY in 2025, down from 2.5% in 2024, on account of heightened external uncertainties and binding domestic demand constraints.
- Inflationary pressures have been low supported by fiscal and quasi-fiscal measures along with lower global oil prices.
- Our baseline is for one more 25bp cut from Bank of Thailand (BoT) this year as the room for further cuts are limited.

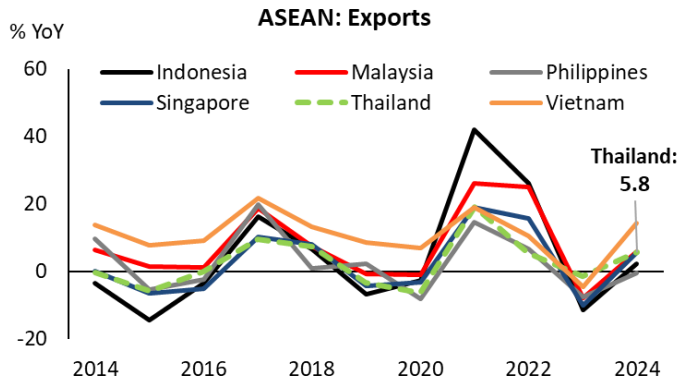
Thailand was the last amongst the ASEAN economies we cover to start bilateral trade negotiations with the US. Prime Minister Paetongtarn Shinawatra reaffirmed that her team will continue to work within the 90-day timeframe for the US to propose a formal negotiation date[11].

During this period, Thailand will be subject to the universal 10% tariff rate but would face a higher 36% tariff rate if discussions remain inconclusive. The Thai government has offered to ramp up imports from the US and revamping of its import duty structure and non-trade barriers. Our assumption is that reciprocal tariff rates will be introduced as announced on 2 April, leading to average growth of 2.0% YoY in 2025. As an open economy with exports of goods and services constituting 72.7% of GDP in 2024, Thailand is particularly vulnerable to external shocks, which tend to have ripple effects across all major drivers of growth. Investment spending, for example, will likely remain anaemic as businesses wait on the sidelines to weather the current tariff storm.

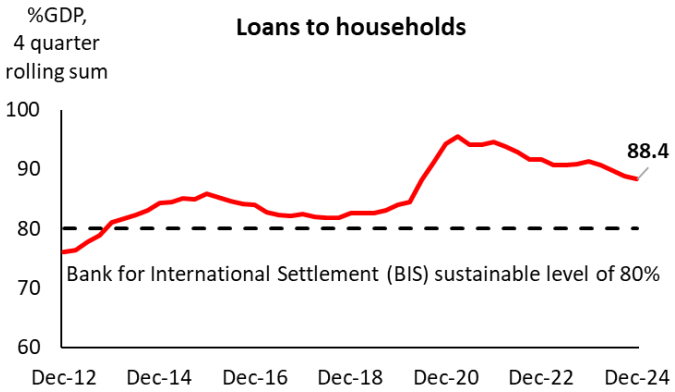
Thai exporters front-loaded exports to the US. Customs exports growth accelerated to 14.0% YoY in January-April 2025 from 5.4% in 2024, with exports to the US picking up to 25.0% YoY during the same period versus 13.7% in 2024. The frontloading of exports is likely to continue through 2Q25 and/or until the tariff rates are decided by the US. More fundamentally, Thailand's export competitiveness has deteriorated over the past decade with neighbouring economies such as Vietnam rapidly gaining share. The government is looking to diversify its export markets access through Free Trade Agreement (FTA) negotiations[12] [13] [14], however, the product mix will also need to be examined carefully.

[11] 'No pause' in Thai-US trade talks. Bangkok Post, 30 May 2025.
[12] Brics welcomes Thailand as newest partner nation. Bangkok Post, 1 January 2025.
[13] Thailand races to seal free trade deal with EU within 2025. The Nation, 14 March 2025.
[14] Free trade talks eyed with Gulf nations. Bangkok Post, 21 February 2025.

Thailand



Note: Local currencies for Malaysia and Singapore.
Source: CEIC, OCBC.



Source: Bank of Thailand, CEIC, OCBC.

Despite this frontloading of good exports, 1Q25 GDP growth slowed to 3.1% YoY in 1Q25, down from 3.3% in 4Q24. This points to underlying weakness in domestic demand and cracks in the tourist arrivals. The contribution of domestic final demand narrowing to 3.0 percentage points (pp) in 1Q25 from 3.9 in 4Q24. Private consumption, government spending and investment spending (i.e., GFCF) slowed in 1Q25 compared to 4Q24.

The persistent weakness in household spending is particularly worrisome given the government's efforts to bolster this driver of growth. The first and second phases of the digital wallet program provided THB145bn and THB30bn to people of the vulnerable group (i.e., welfare cardholders and people with disabilities), and senior citizens, respectively, in September 2024 and January 2025[15]. These did little to boost household spending. Thai households remain constrained by elevated levels of household debt, with debt servicing account for 88.4% of GDP, on a four-quarter rolling basis.

While BoT and the government have taken steps to address the household debt issues, BoT Governor Sethaput Suthiwartnarueput mentioned in an interview with Bloomberg that this issue will take time and concerted efforts to resolve[16]. The Thai government on 19 May 2025 announced the postponement of the third phase of the digital wallet programme, citing the need to wait for an improved economic climate[17].

With the postponement of the third phase of the digital wallet programme, the government has announced that THB157bn earmarked for the scheme will be made available to a new economic stimulus package that funds projects and support small businesses[18]. This counter cyclical fiscal policy stance will likely cushion against some downside risks to growth.

[15] Thailand's stalled cash handout scheme sours voters on ruling party. Reuters, 2 June 2025.
[16] Thai Central Bank Chief Warns Against Inflation Target Reset. Bloomberg, 18 June 2024.
[17] Thai Government Pulls Back on 10,000 Baht Digital Handout Scheme Amid Economic Headwinds. The Nation, 19 May 2025.
[18] Thai cabinet approves $4.7 bln funding to counter U.S. tariff impact. Reuters, 20 May 2025.

Thailand

Measures/Programmes	Details	Effective Period
Credit Card Debt Relief	1. Minimum instalment payment to hold stable at 8% until end-2025 (Previous: revert to 10% in January 2025). 2. Debtors paying 8% or more will receive cashback credits of 0.5% interest in 1H25 and 0.25% in 2H25.	Until end-2025.
Debt Consolidation	1. Financial Institutions are encouraged to offer debt consolidation services, combining mortgage and retail loans 2. LTV ratio restrictions will be relaxed for debt consolidation cases.	Until end-2025.
Assistance for Chronic Debtors	1. Debt closure period extended to 7 years for persistent debtors (Previous: 5 years), with interest rates capped at 15% per annum. 2. Additional information will be provided by service providers to encourage responsible borrowing.	From January 2025.
Jai Trong Kong Sup	A three-year interest moratorium aimed at easing the debt burden of eligible retail debtors and SMEs. Eligible debtors will be exempted from interest payments for three years, and their instalments will be reduced: Year 1 - 50% of original instalment amount Year 2 - 70% of original instalment amount Year 3 - 90% of original instalment amount	Until end-June 2025. The Ministry of Finance plans to revise the eligibility criteria for the programme and request for an extension to the programme's deadline.
Jai Pid Job	Under this measure, eligible borrowers are able to close their loan accounts by making a lump sum payment.	Until end-June 2025.The Ministry of Finance plans to revise the eligibility criteria for the programme and request for an extension to the programme's deadline.

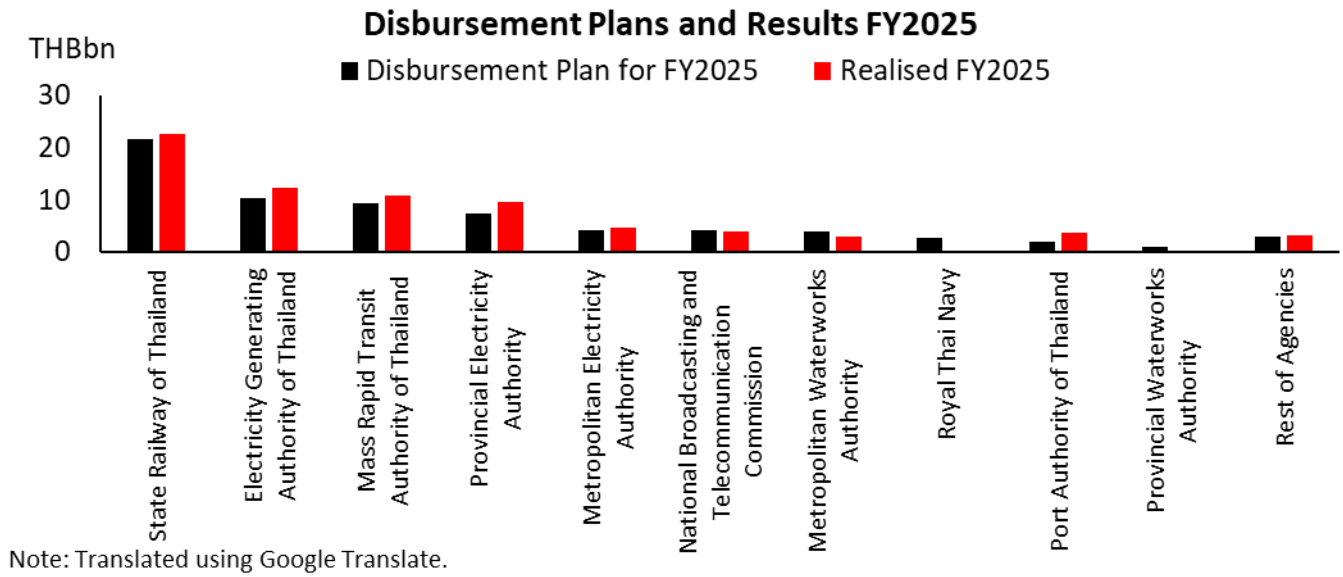
Source: Bank of Thailand, Ministry of Finance, The Nation.

The fiscal cash balance deficit has widened to 6.3% of GDP, on a 12-month sum basis until April 2025, from 4.1% of GDP for FY2024 (i.e., October 2023 to September 2024). The FY25 fiscal deficit target is 4.5% of GDP.

Expenditure growth rose by 25.9% YoY in October 2024 - April 2025, due to accelerated current and capital expenditure spending. The current and capital expenditure spending stood at 71.4% and 30.5% of the government budget, in the same period.

It is worth noting that slower capex disbursements persist, and this is another constraint for raising potential growth. The data from the Public Debt Management Office (PDMO) suggests that disbursement rates for government investment projects is also relatively low at 53% as of April 2025. The cabinet has approved 106 projects from 21 agencies for FY25.

Thailand



Note: Translated using Google Translate.
Source: Public Debt Management Office, OCBC.

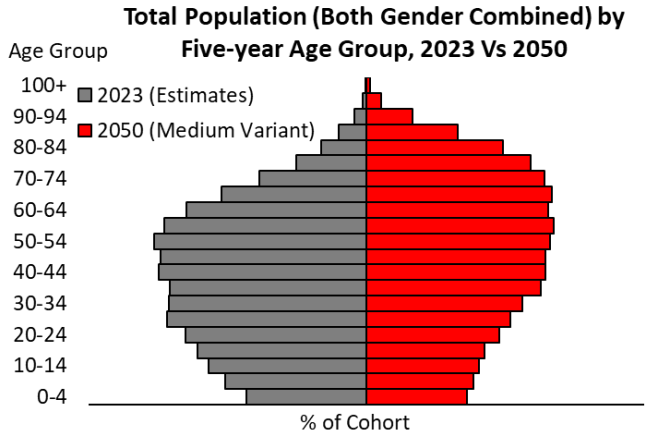
On the revenue front, revenue collection growth improved to 4.3% YoY for the period from October 2024 - April 2025, up from the flat revenue collection growth during the same period last year. The revenue collection rate stands at 49.3% of the FY2025 target.

The budget deficit for FY2026 (i.e., October 2025 to September 2026) is targeted at THB860bn, equivalent to 4.3% of GDP. The House of Representatives has passed the first reading of the FY2026 budget bill on 31 May[19]. The government aims to narrow the fiscal deficit to 3.1% of GDP by FY2029. Notably, the pace of fiscal consolidation has been adjusted to accommodate modestly wider deficits over the medium-term given the current economic conditions. The debt-to-GDP ratio is projected to grow to 69.3% in FY2029, up from 67.3% in FY2026, but still below the legal ceiling of 70%.

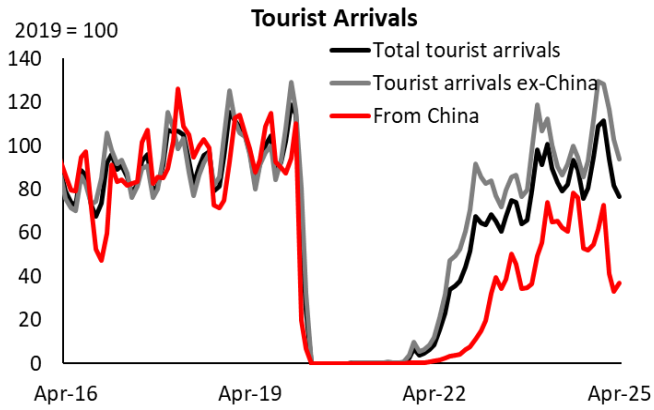
The burden on the government is set to increase over the coming years as the population ages rapidly. According to the UN Department of Economic and Social Affairs, the total dependency ratio is projected to increase to 60 (Median) per 100 persons in 2040, up from 42 (Median) per 100 persons in 2023. A higher total dependency ratio puts additional pressure on the authorities over the medium-term as greater burden will be placed on the working-age population.

[19] FY2026 Budget Bill clears first reading in 322–158 vote. The Nation, 31 May 2025.

Thailand



Source: United Nations Department of Economic and Social Affairs, OCBC.



Source: Bank of Thailand, Ministry of Tourism and Sports, CEIC, OCBC.

Economic growth in recent years has relied heavily on tourist arrivals. But the sentiment associated with tourism has dampened in 1Q25. This was partly due the earthquake in March as well as negative incidents associated with Chinese tourists. Additionally, the Chinese government's strong push for domestic tourism and greater intra-ASEAN competition for tourist dollars have weighed on tourism prospects.

The BoT reduced its projection for foreign arrivals for 2025 by 30% to 37.5mn, which they attributed it to the decline in Chinese visitors[20]. Year-to-April 2025, total tourist arrivals averaged 90.9% from 2019 levels. This is slightly lower compared to the same period last year, driven by sharp slowdown in tourist arrivals from China (incl. HK SAR). Year-to-April 2025, Chinese tourist arrivals averaged 46.1% from 2019 levels, down from 64.9% in the same period last year.

Weaker good exports and lower tourism will likely weigh on the current account surplus. We expect it to narrow to 1.1% of GDP in 2025 from 2.1% of GDP in 2024.

Inflation will remain subdued

Fiscal/quasi-fiscal policies and lower global oil prices kept inflationary pressures subdued in 1H25. Headline CPI averaged 0.5% YoY from January-May 2025 (2024: 0.4%) driven by government policies to reduce electricity tariffs for an extended period. At the same time, lower global oil prices have kept retail transportation fuel prices down, contributing further to the muted inflationary environment. Meanwhile, core CPI averaged at 0.9% from January-May 2025 versus 0.6% in 2024.

We expect headline inflation to average 0.9% YoY in 2025, implying a subdued headline inflation for the rest of the year. The government's energy measures as well as global oil prices will remain as key drivers to a subdued inflationary environment. The Energy Regulatory Commission has announced further reduction to the revised automatic tariff adjustment for the May to August 2025 period by 3.9% to THB3.99/unit[21].

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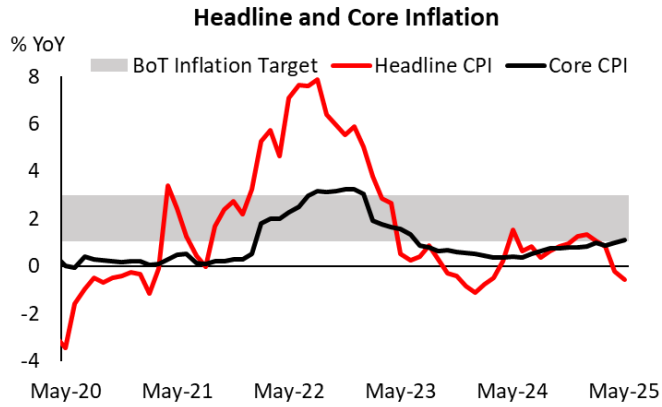
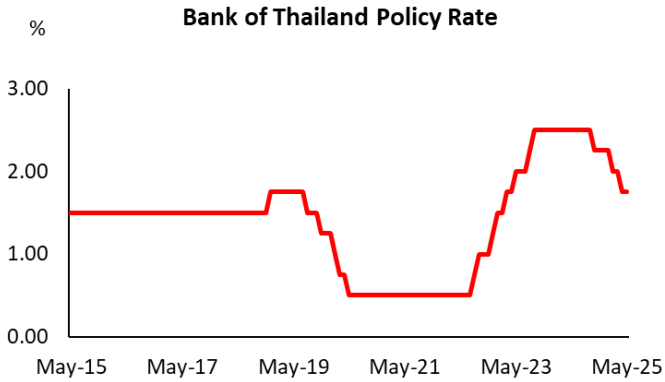
[20] Bank of Thailand slashes tourism forecast. Bangkok Post, 21 May 2025.
[21] NEPC sets electricity price cap at 3.99 baht per unit until end of 2025. The Nation, 6 May 2025.

Thailand

Compounding the effects, oil prices will remain low and would restrain any upward price pressures. Our house view is for Brent crude to average USD67/bbl in 2025, down from an average of USD79.9/bbl in 2024. The BoT, at its 30 April meeting, highlighted the need to closely monitor inflation trends as "global trade policies could result in heightened price competition and a greater influx of lower-priced imported goods, which might place additional pressure on domestically produced goods.[22]"



Source: Bureau of Trade and Economic Indices, CEIC, OCBC.



Source: Bank of Thailand, CEIC, OCBC.

Limited room for policy rate cuts

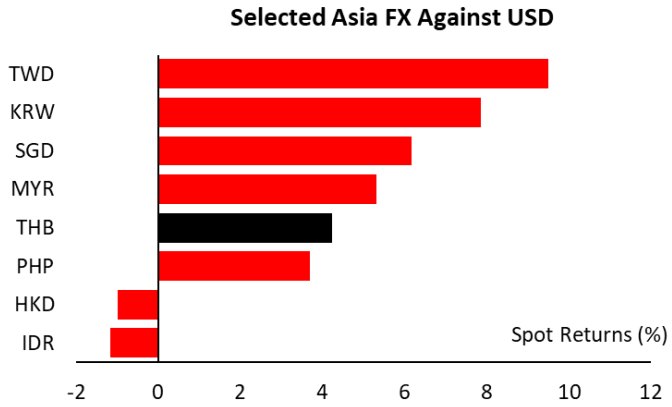
The BoT has delivered a cumulative 50bp in rate cut this year, characterising these rate cuts as an insurance against rising growth uncertainties. The most direct impact of lower rates is to support private investment spending, which is unlikely be motivated by rate cuts in the near-term given heightened uncertainties globally.

Our baseline is for one more 25bp cut from the BoT this year as the room for further cuts are limited. Indeed, the BoT highlighted the need to preserve policy space following rate cuts at its 26 February and 30 April meetings.

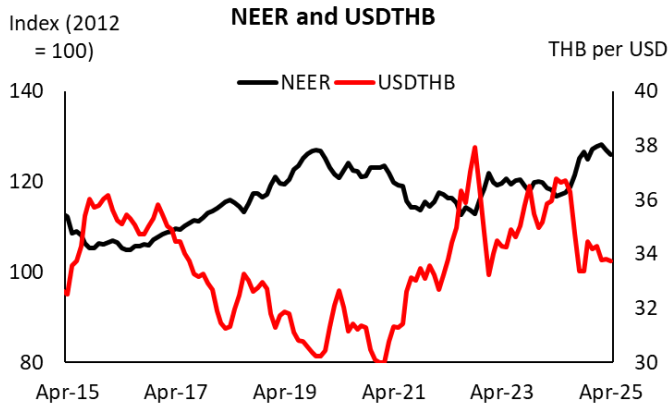
There will likely be some uncertainties associated with the impending transition to the new BoT governor. The term of the current governor ends on 30 September and the government expects to find a replacement in the coming months. It is unclear whether there could be a major shift in policy direction following the replacement of the governor since it will ultimately depend on the candidate. That said, BoT has traditionally been more conservative regards the use of monetary policy tools to support growth than the government would like. Notwithstanding, the relatively anaemic growth outlook the political pressure on the BOT for lower rates is likely to sustain.

[22] Edited Minutes of the Monetary Policy Committee Meeting (No. 2/2025) 25 and 30 April 2025. Bank of Thailand, 14 May 2025.

Thailand



Last updated: As of 4 June 2025.
Source: Bloomberg, OCBC.



Source: Bank of Thailand, CEIC, OCBC.

Should growth momentum deteriorate more rapidly than under our baseline and/or financial conditions tighten sharply, we do not rule out deeper rate cuts from BoT to support growth this year. Year-to-date, as of 4 June 2025, the currency (THB) appreciation has been relatively strong, gaining 4.2% versus the USD. At its 30 April MPC meeting, the committee assessed that "financial conditions remained tight, with a slight contraction in overall loan growth and a continued deterioration in loan quality, particularly for housing loans and business loans in sectors facing structural challenges." As such, it underscored the importance to "to closely monitor credit risk and macro-financial linkages going forward, particularly in business sectors adversely impacted by global trade policies."

Vietnam

Vietnam: Steering through the turbulance

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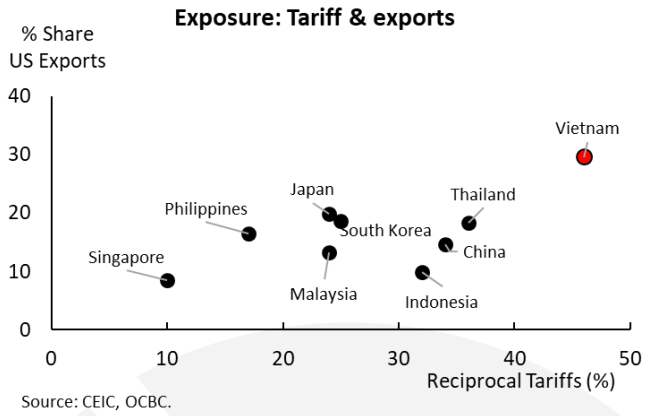
- Higher than expected frontloading in 1H25 has led us to revise higher our 2025 GDP growth to 5.5% in 2025 from 5.0% previously. This nonetheless implies a sharp slowdown to 4.4% in 2H25 assuming high reciprocal tariffs remain in place.
- Despite the external headwinds, the government remains focused on boosting domestic growth prospects through infrastructure spending and better governance.
- Although currency depreciation risks remain a concern, exacerbated by growth risks, inflationary pressures have been relatively well behaved. We maintain our forecast for a 50bp rate cut by SBV year end.

Heightened external risks

We have assessed Vietnam to be the most exposed to US protectionism (*see* 'Some of the hardest hit by reciprocal tariffs', published on 3 April 2025) given its large share of exports to the US (~30% of total exports) and a high reciprocal tariff rate of 46% as announced on 2 April. If the tariffs are not negotiated lower, it could have significant consequences for growth. We estimate that the current level, Vietnamese exports could be lower by ~50% in 2H25 compared to 1H25. That said, the risks to are to the upside if negotiations with the US yield lower tariff rates.



Recent signs point to some willingness from the US and Vietnam authorities to have proactive conversations. The second round of tariff negotiations took place from 19-22 May in Washington, reportedly making "significant progress" according to Industry and Trade Minister Nguyen Hong Dien, who also leads the trade delegation team from Vietnam.

The two countries are set to proceed with further technical and ministerial-level exchanges as the 9 July reciprocal tariff pause deadline approaches. While the non-disclosure agreements (NDAs) signed between the two governments have kept public details limited, we note that Vietnamese authorities have publicly committed to addressing both tariff and non-tariff barriers, including actions to combat illegal transshipment and even bringing tariff on imports from the US to zero.

Vietnam

Measures	Details
Increase imports of US goods	Prime Minister Pham Minh Chinh has, on several occasions, revealed plans to increase imports of various products from the US. On 14 March 2025, several US and Vietnamese companies signed cooperation agreements and purchase contracts totalling USD54.3bn for purchases of machinery, equipment, raw materials, aircraft procurement, aviation services, oil and gas extraction, as well as petrochemical products. Contract agreements worth USD36bn are also under discussion. PM Chinh has also urged for more imports of medical equipment, beef, and fruits from the US.
Addressing non-tariff barriers	In a document dated 15 April 2025, the Trade Ministry issued a directive aimed at combating the illegal transshipment of goods to the US and other trading partners to mitigate the risk of steep US tariffs. The directive emphasizes the need for enhanced supervision and inspection of imported goods, particularly raw materials used in production, to ascertain their origin and prevent trade fraud, which is expected to rise due to heightened tensions.
Other	In a call with US President Donald Trump on 4 April, General Secretary To Lam indicated that Vietnam is ready to cut all tariffs against US imports into the country to zero. PM Pham Minh Chinh has pledged to intensify efforts against trade fraud, smuggling, and counterfeit goods, particularly in light of ongoing US tariff negotiations. PM Chinh ordered the establishment of a task force to address the illegal export of counterfeit Vietnamese goods and to uphold intellectual property rights. Additionally, the government will review regulations to strengthen the legal framework against trade fraud, having already identified over 34,000 violations this year, including numerous cases of tax fraud and counterfeit goods, as reported by Bloomberg.
Source: Various news sources, OCBC.	

Higher than expected frontloading in 1H25 has led us to revise higher our 2025 GDP growth to 5.5% in 2025 from 5.0% previously. This nonetheless implies a sharp slowdown to 4.4% in 2H25 assuming high reciprocal tariffs remain in place

1Q25 GDP growth stood at 6.9% YoY from 7.6% in 4Q24, but the details suggest continued resilience in sectors such as manufacturing and services. On the demand side, retail sales were higher at 9.9% YoY in 1Q25 from 8.4% in 4Q24 while tourist arrivals were up by 29.6% YoY in 1Q25. In addition, average monthly income rose 9.5% YoY to VND8.3mn in 1Q25[23], comfortably outpacing inflation (3.2%) and supporting real purchasing power.

Incoming data for April and May suggest that growth momentum held up well in 2Q25, with our GDP estimate tracking 6.7% YoY for the quarter. Exports grew 18.3% YoY in April-May period from 10.5% in 1Q25, while imports stayed robust at 18.2%, up from 16.9%. Similarly, industrial production growth was resilient, averaging 9.5% YoY during the April–May period, close to the 8.7% recorded in 1Q25, with the manufacturing sector continuing to lead with double-digit growth, likely reflecting strong activity in export-oriented industries. Meanwhile, the steady recovery in tourism-related sectors has supported a pickup in retail sales, which averaged 10.7% YoY in April and May, up from 9.9% in 1Q25.

The outlook for 2H25 is heavily dependent on tariff negotiation outcomes, essentially demarcated by frontloading of exports to the US ahead of formal tariff implementation and a sharp drop once the front-loading impact abates. We err on the more cautious side assuming the worst case in 2H25.

[23] Workers' average monthly income increases to $320 in Q1, VnExpress, 14 April 2025. Last Accessed: 4 June 2025.

Vietnam

GDP Growth of Selected Sector (% YoY)	2020	2021	2022	2023	2024		2Q24	3Q24	4Q24	1Q25
GDP	**2.9**	**2.6**	**8.5**	**5.1**	**7.1**		**7.2**	**7.4**	**7.6**	**6.9**
Agriculture, Forestry and Fishery	**3.0**	**3.7**	**3.7**	**3.9**	**3.3**		**3.8**	**2.9**	**3.0**	**3.7**
Industry and Construction	**4.4**	**3.2**	**8.2**	**3.7**	**8.2**		**8.6**	**9.0**	**8.4**	**7.4**
Industry	3.8	4.1	8.5	3.0	8.3		8.7	9.3	8.4	7.3
Manufacturing	5.0	5.4	9.0	3.6	9.8		10.2	11.3	10.0	9.3
Construction	7.1	-0.6	6.6	7.3	7.9		8.0	7.4	8.3	8.0
Services	**2.0**	**1.7**	**10.7**	**6.9**	**7.4**		**7.4**	**7.5**	**8.2**	**7.7**
Wholesale, Retail Sales & Motor Vehicles	5.8	0.9	10.7	8.5	8.0		7.7	8.0	9.0	7.5
Transportation & Storage	1.1	-2.9	13.3	9.8	10.8		12.7	9.9	10.0	9.9
Accommodation & Food Services Activities	-21.1	-20.1	39.5	13.0	9.8		11.1	9.0	10.3	9.3
Information & Communication	6.5	4.6	8.8	5.0	5.8		5.4	6.4	6.7	6.7
Financial, Banking & Insurance Activities	7.5	9.8	10.2	5.8	7.1		6.1	7.7	9.3	6.8
Real Estate Activities	0.9	1.3	6.9	0.2	3.3		2.4	3.9	4.8	3.7

Source: General Statistics Office (GSO), CEIC, OCBC

Focused on the fundamentals

The authorities have also been active in broadening market access for its exports. In 2025 alone, it has upgraded bilateral ties with Indonesia, Singapore, and New Zealand to Comprehensive Strategic Partnerships, with key aims including deepening cooperation and increasing trade and investment among the countries involved, while also reduce reliance on a set of export markets. Meanwhile, the government has continued its free trade agreement (FTA) negotiations. The latest directive is to conclude or initiate talks with India, Brazil, Pakistan, Egypt, and other markets across the Middle East, Africa, Latin America, and Central Asia.[24]

Comprehensive Strategic Partnership relations		Free Trade Agreements			
Partner Country	Since	FTA	Effective date	FTA	Effective date
China	May-08	ASEAN Free Trade Area	1993	EU-Vietnam Free Trade Agreement	2020
Russia	Jul-12	ASEAN-China Comprehensive Economic Cooperation Agreement	2005	UK – Vietnam Free Trade Agreement	2010
India	Sep-16	ASEAN-South Korea Free Trade Agreement	2007	Regional Comprehensive Economic Partnership	2022
The Republic of Korea	Dec-22	ASEAN-Japan Comprehensive Economic Partnership	2008	Vietnam-Israel FTA	2024
The United States	Sep-23	Japan-Vietnam Economic Partnership Agreement	2009		
Japan	Nov-23	ASEAN-India Free Trade Agreement	2010		
Australia	Mar-24	ASEAN-Australia and New Zealand Free Trade Agreement	2010		

[24] 'Vietnam seeks more free trade deals to drive growth as Trump tariff looms', Reuters, 23 April 2025. Last accessed: 29 May 2025.

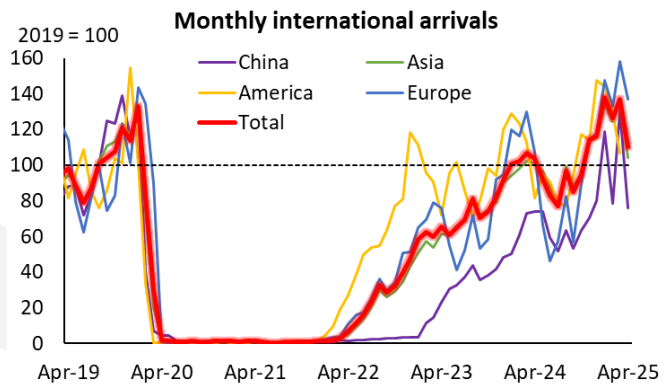
Vietnam

France	Oct-24		Vietnam-Chile Free Trade Agreement	2012	
Malaysia	Nov-24		South Korea-Vietnam Free Trade Agreement	2015	
New Zealand	Feb-25		Eurasian Economic Union-Vietnam Free Trade Agreement	2016	
Indonesia	Mar-25		Comprehensive and Progressive Agreement for Trans-Pacific Partnership	2019	
Singapore	Mar-25		ASEAN-Hong Kong, China Free Trade Agreement	2019	
Source: Vietnam Government News, Vietnam Briefing, OCBC.					

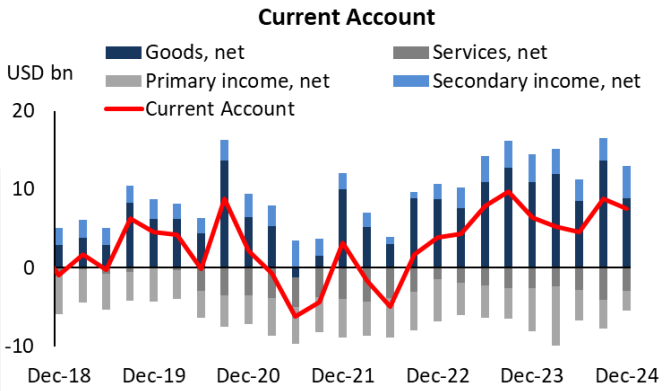
1. Tourism push remains strong

Tourist arrivals rose by 23.8% YoY to 7.7mn in the first four months of the year, supported by a sharp recovery in Chinese visitors (+119.7% YoY; 2.0mn arrivals), along with continued growth from the America (+41.6%; 1.0mn) and Europe (+57.0%; 1.0mn). The reduced number of Chinese tourists to Thailand could pose a unique opportunity for Vietnam to capitalize. Indeed, during the same period, the number of Chinese tourists to Thailand fell by 29.9% YoY to 1.6mn arrivals, with arrivals in April 2025 only equivalent to 36.9% of the monthly average in 2019. The recent reopening of the passenger train route connecting Hanoi and Nanning in China, along with the opening of Long Thanh International Airport, is poised to provide a further boost to the already surging tourism sector.

The government aims to attract 22–23mn visitors in 2025, up from 17.6mn in 2024. We believe this target is achievable, supported by ongoing targetter promotional campaigns and expanding e-visa eligibility. The Tourism Development Stimulus Program in 2025 with many activities, events, and attractive tourist packages will contribute to completing the target of receiving 22-23mn international visitors and 120-130 million domestic visitors this year.



Source: General Statistics Office (GSO), CEIC, OCBC.



Source: State Bank of Vietnam, CEIC, OCBC.

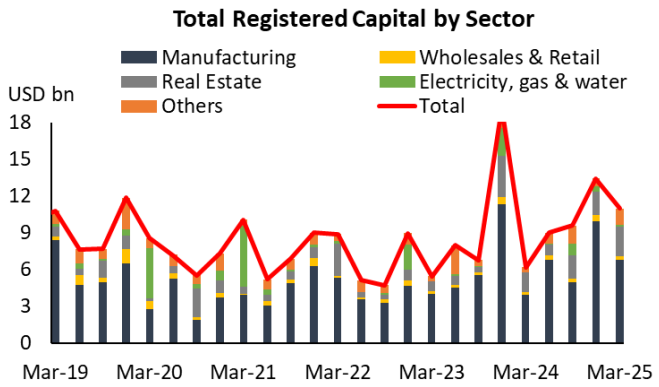
Despite the burgeoning tourism sector, we revise lower our current account surplus forecast to 3.2% of GDP in 2025 from 3.8% previously, given the ongoing volatilities on the goods trade accounts. This shows a steady decline in the current account surplus from 5.5% in 2024 and 6.5% in 2023.

Vietnam

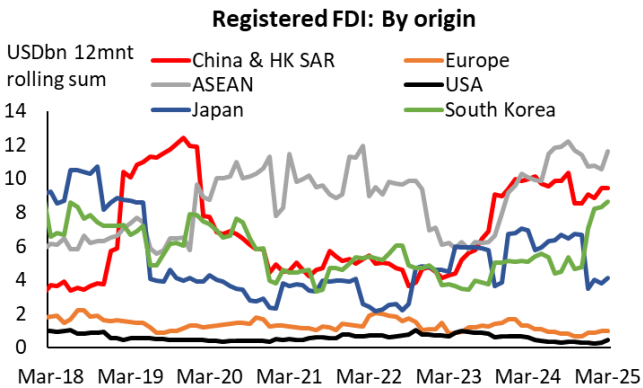
2. Still strong FDI Prospects

The near-term outlook for FDI is cloudy and investors are likely to stay on the sidelines. Vietnam's near-term FDI prospects could be impacted by this broader external sentiment but once the dust settles, we do not expect that Vietnam's prospects as an FDI destination will have lost too much of its shine.

Net FDI inflows were steady at USD19.5bn in 2024, even as net portfolio outflows increased to USD5.1bn in 2024 from USD1.2bn in 2023. Year-to-April FDI as registered capital increased to USD13.8bn compared to USD9.3bn for the same period in 2024, an increase of 49% YoY. Looking at a more detailed data as of March 2025, the manufacturing sector received bulk of the investment, reaching USD6.8bn or up 77.8% YoY in 1Q25, followed by real estate (USD2.4bn; 51.2%) and wholesale and retail (USD0.3bn; 21.2%). By origin, incoming FDI was led by ASEAN, China and Hong Kong, and South Korea, while Japanese investment slowed. Interestingly, despite the risk of facing higher tariffs, Vietnam has continued to attract large-scale investment commitments. For instance, Samsung Display pledged an additional USD1.2bn to expand its Bac Ninh operations, and SpaceX, through its Starlink unit, planned to invest up to USD1.5bn in the country. More recently, the Trump Organization held a groundbreaking ceremony on May 21, 2025, for a USD1.5bn luxury residential development with three 18-hole golf courses near Hanoi.



Source: Ministry of Planning and Investment, CEIC, OCBC.



Source: Ministry of Planning and Investment, CEIC, OCBC.

Inflationary pressures to remain contained

We have revised our full-year 2025 CPI forecast lower to 3.7%, from 4.0% previously, well within the government's 4.5% target. Against a backdrop of slower GDP growth, inflationary pressures have also largely remain well contained. Headline CPI averaged 3.2% YoY for the first four months of 2025, compared to 3.9% during the same period in 2024. Core inflation averaged modestly higher at 3.0% y-t-d, compared to 2.7% during the period in 2024. This nonetheless suggests relatively stable underlying demand-side pressures.

Specifically, the 'transportation' component recorded a negative print of -3.6% YoY in January–April period, reflecting the pullback in global oil prices. Our house view is for crude oil Brent price to continue easing into 2H25, averaging USD67/bbl in 2025 versus USD80/bbl in 2024, further supporting disinflation in the transportation component. Likewise, soft global commodity prices and the reversal of India's rice export ban have helped stabilize the 'food and foodstuff'

Vietnam

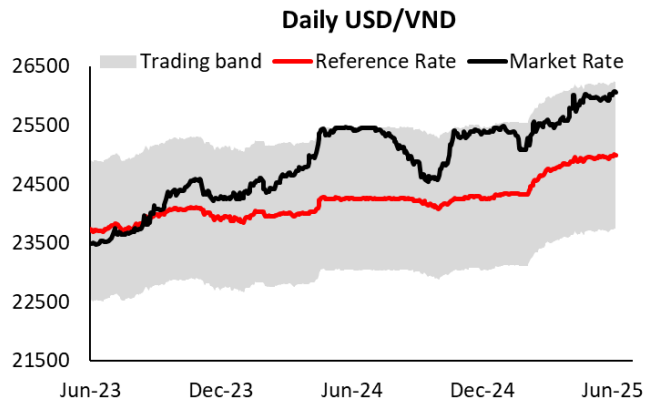
CPI at 3.9% ytd, slightly lower than the 4.0% recorded during the same period in 2024 .

A delicate balancing act

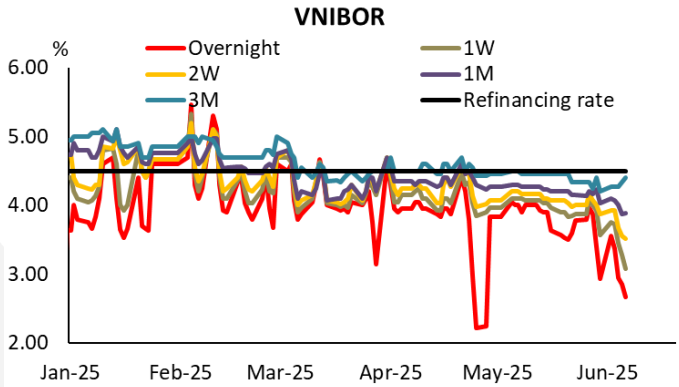
The challenge for the State Bank of Vietnam (SBV) is mitigating downside risks to growth while containing VND depreciation pressures. VND has depreciated by ~2.2% ytd versus USD, making it (one of) the worst performing currencies among regional peers. Even at the time of writing, VND traded near the weaker end of the official trading band. Officials have allowed the USD/VND daily reference rate to move higher since February 2025, signalling a willingness to tolerate a weaker VND. The extent of this tolerance remains to be tested, but it will likely cushion against some risks from weaker export growth.

We are keeping our forecast for SBV to deliver a cumulative 50bps in rate cut by year-end, which would bring the refinancing rate down to 4.0%. PM Chinh has repeatedly urged the SBV to lower interest rates and ease financial conditions to support economic growth. To that end, the shorter end of the interbank curve has moved meaningfully lower since the beginning of the year, signalling a more accommodative liquidity position and monetary stance by the SBV, and it aligns with the government's efforts to achieve its 2025 credit growth target of 16%.

The risk is that SBV does not deliver on rate cuts, however, allows for further easing through the banking system. According to the State Bank of Vietnam (SBV), 23 different commercial banks adjusted their interest rates between 25 February and 18 March and the adjustments ranged from 0.1-1%, depending on the term, with most cuts around 0.1% across various tenors. Lending rates have also decreased by 0.8 per cent since the beginning of the year[25].



Source: State Bank of Vietnam, Bloomberg, OCBC.



Source: Bloomberg, OCBC.

[25] Banks cut rates to boost business, Vietnam Investment Review, 21 March 2025. Last accessed: 6 June 2025.

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ASEAN-GCC: Opportunities and Challenges

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- The second summit between the Association of Southeast Asian Nations (ASEAN) and the Gulf Cooperation Council (GCC) concluded on 27 May in Malaysia. The two regions agreed to deepen cooperation across various aspects.
- The focus on inter-regional cooperation has increased in prominence following higher protectionist from the US.
- Given the relatively low starting points of economic cooperation between the two regions in terms of trade, investment and tourism, the scope to deepen and broaden ties across the various economies is large.

The ties between the ASEAN and GCC countries were formally established in 1990. The relationship has evolved since, with the second ASEAN-GCC summit culminating in promises of deeper economic and social partnerships across the regions. Regional cooperation has gained greater prominence following the sharp escalation of US tariff measures in 2025 and there is an increasingly greater collective understanding that these types of inter-regional agreements hold potential.

Overview of ASEAN-GCC relations	
1990	First formal contact
	ASEAN Foreign Ministers met with their counterparts from the GCC at the sidelines of the United Nations General Assembly (UNGA)
April 2007	Secretary-General of ASEAN, H.E. Ong Keng Yong, made an official visit to the GCC Secretariat and met with his GCC counterpart, H.E. Abdulrahman H Al Attiyah.
June 2009	Adopted the ASEAN-GCC Joint Vision and signed a Memorandum of Understanding (MOU) between the ASEAN Secretariat and the GCC Secretariat
	(i) a free trade area
	(ii) economic cooperation and development
	(iii) culture, education and information
June 2010	Second ASEAN-GCC ministerial meeting
	ASEAN-GCC Two-Year Action Plan (2010-2012) was developed
November 2010	ASEAN-GCC Consultative Meeting on Education in November 2010 in Bangkok
May 2011	ASEAN-GCC Working Group Meeting on Food Security and Agricultural Investment
June 2011	ASEAN-GCC Tourism Consultation
July 2011	ASEAN-GCC Senior Economic Officials
November 2013	Third ASEAN-GCC Ministerial Meeting
June 2014	First ASEAN-GCC Workshop
October 2023	First ASEAN and the GCC convened the Summit of ASEAN and GCC in Riyadh
May 2025	Second ASEAN-GCC Summit

Source: ASEAN Secretariat, OCBC.

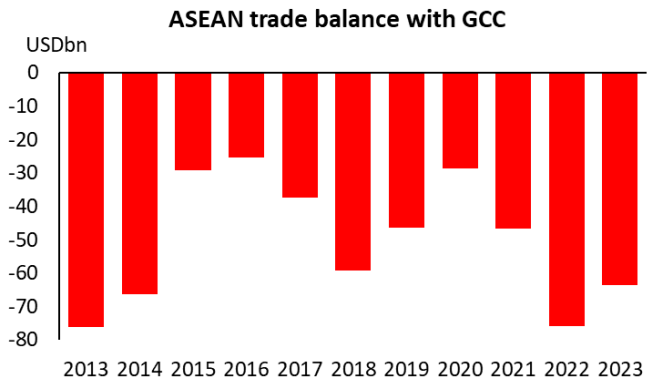
Thematic Report 1

The framework of cooperation between the ASEAN and GCC countries (2024-28) has identified the following areas for greater cooperation. These include security, trade and investment, agriculture and food security, energy, tourism, culture and information, education, capacity building and connectivity (sustainable infrastructure; digital innovation; seamless logistics; regulatory excellence; and people mobility).

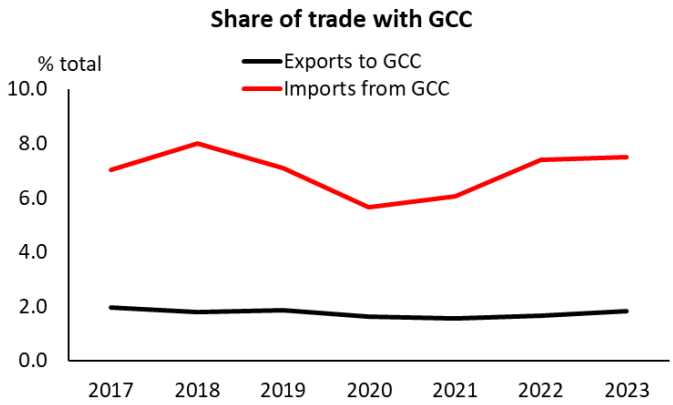
The outcome of the second ASEAN and GCC summit saw the two regions commit to enhancing trade and investment flows and conducting "a joint feasibility study on ASEAN-GCC Free Trade Agreement (FTA) and undertaking Free Trade discussions." It also sought to encourage public-private partnerships, promote greater involvement of the private sector, recognise the "growing role of sovereign wealth fund in advancing investment cooperation" amongst others.

Current state of play

The economic ties between ASEAN and GCC include trade, investments and tourism. The ASEAN region recorded net trade deficits with the GCC over the past decade. The deficit (in USDbn terms) has been volatile reflecting movements in global oil prices and economic downturns (for example, the pandemic 2020-22). More fundamentally, however, the share of ASEAN exports to GCC economies has remained low at 1.6-2.0% of total exports from 2017 until 2023. Similarly, imports as a share of total ASEAN imports accounted for 5-6% of total imports.



Source: ASEAN stats, OCBC.



Source: ASEANstats, OCBC.

Imports from GCC into ASEAN are largely focused on oil. Saudi Arabia and the UAE accounted for 49% of all crude oil imports from non-ASEAN countries. The dollar level of mineral fuel and oils imports[26] has increased sharply for Vietnam and Malaysia over the past decade but has declined for Indonesia while remaining relatively stable for the Philippines, Singapore and Thailand.

Notwithstanding, price effects (i.e., changes in global oil prices), the fuel trade deficit is projected to widen close to 600 million tonnes of oil equivalent (Mtoe)

[26] HS code two digit. The code is 27.

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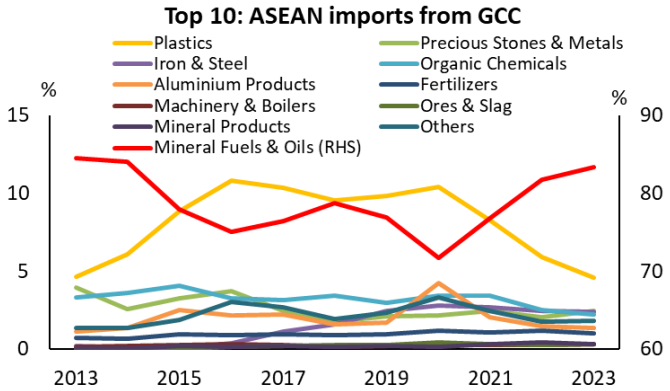
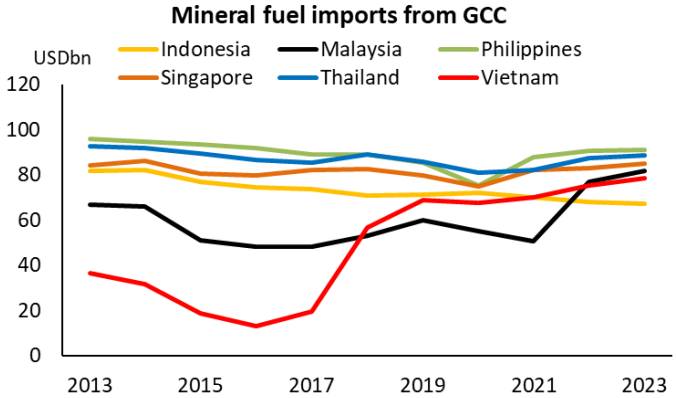
by 2050 under a baseline scenario, according to the 8th ASEAN Energy Outlook. Under the report's alternative more energy efficient scenario, the oil trade deficit will widen to less extent, below 400 MToe. This, nonetheless, implies that oil demand from the region's major supplies will remain a key pillar of the trading relationship.

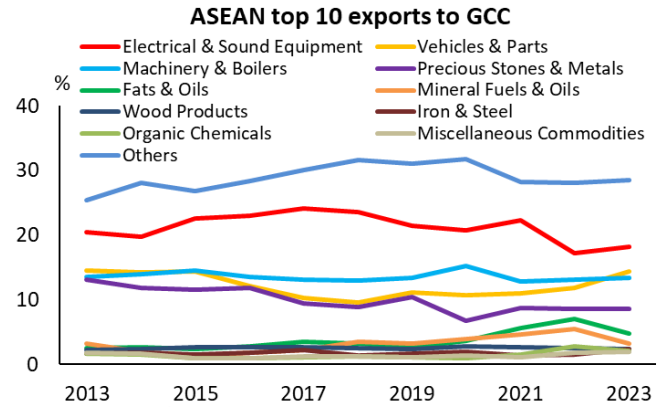


Source: UNComtrade, OCBC.

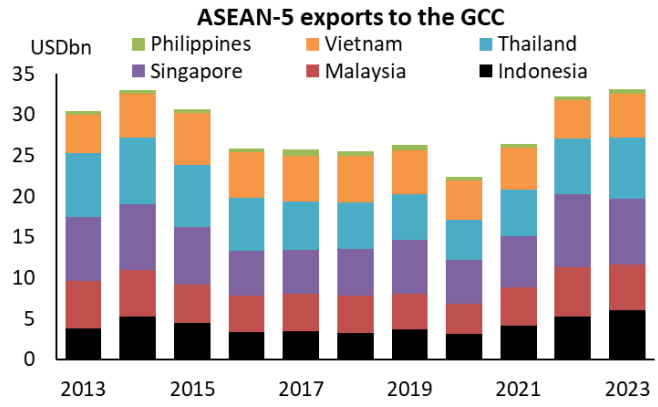


Source: ASEANstats, OCBC.

Exports from ASEAN to GCC economies are relatively more broad-based encompassing electronics, precious stones and metals, machinery and certain commodities such as palm oil and natural gas. By economy, exports from Indonesia, Malaysia, Singapore and Thailand to GCC are bigger compared to Vietnam or the Philippines exports to GCC.



Source: UNComtrade, OCBC.

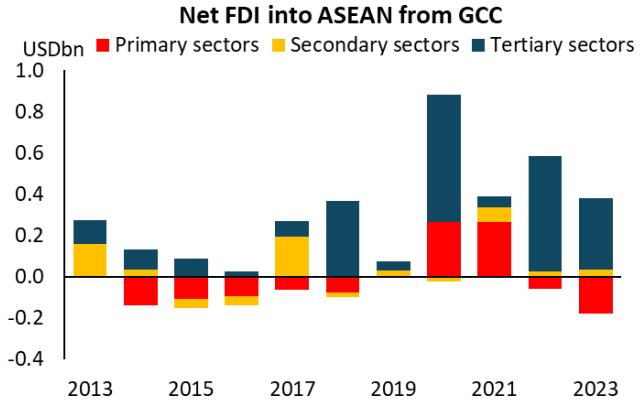


Source: UNComtrade, OCBC.

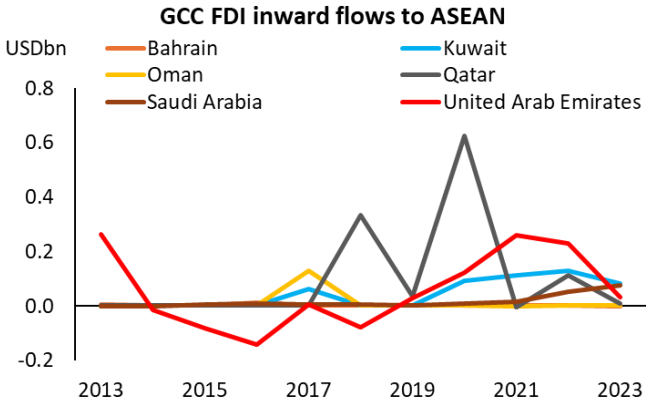
Given the relatively narrow scope of trade currently, there is room to significantly boost trade ties between the two regions. A free trade agreement between the two regions can help streamline regulatory requirements, trade licenses, and even identify sector and country specific collaboration efforts. Indeed, Singapore's FTA with the GCC economies, which came into force in September 2013, can form a blueprint for any forthcoming FTAs.

The picture is relatively similar for foreign direct investments. Net FDI inflows into the ASEAN from GCC is low and less than USD1bn and this has remained the case over the past decade. FDI, in recent years, has been directed towards key services industries such as wholesale and retail trade, financial services,

transportation and services. FDI inflows, while volatile, have come from Qatar, UAE and Kuwait within the GCC economies.

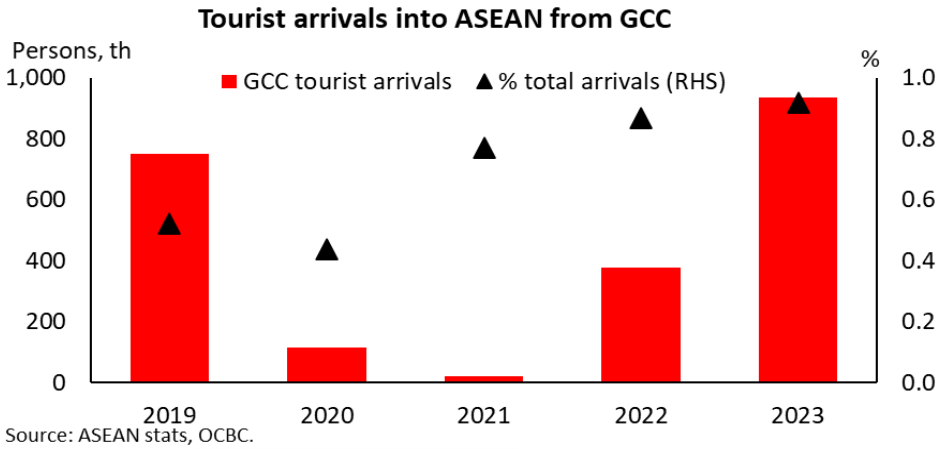


Source: ASEANStats, OCBC.



Source: ASEANStats, OCBC.

Similarly, tourist arrivals into ASEAN from GCC accounts for less than 1% of total tourist arrivals. While country specific breakdowns are harder to gauge given patchy data, it is clear that this route for greater inter-regional exposure has legs to go. Thailand seems the most popular destination spot for GCC tourists, followed by Indonesia and to a lesser extent Malaysia and the Philippines.



Source: ASEAN stats, OCBC.

Challenges and opportunities

With trade, investment and tourist arrivals at fairly low levels between ASEAN and the GCC economies, the room to build on the economic relationship is enormous. However, each of these regions is heterogenous and there will need to be a considerable effort made from both sides to identify sector and country specific synergies that can yield desired outcomes.

Indeed, the recent news flow just over the last few months suggests that the two regions are keen to broaden economic ties and potentially, even deepen three-way ties with China. Malaysia, as chairman of ASEAN in 2025, signed a Comprehensive Economic Partnership Agreement in January 2025. Indonesia's Danatara and the Qatar Investment Authority launched a USD4bn investment fund in April 2025 and Vietnam and Oman are signed to increase investments. Given the starting point, inter-regional cooperation could benefit from lower

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hanging fruits such as boosting tourism prospects through packages and visa-free travel opportunities.

Greater inter-regional cooperation holds crucial benefits in terms of greater trade, investment and tourism diversification against an increasingly protectionist global trade backdrop stemming from the US.

Participating Entities	News flows	Date
ASEAN, GCC, China	The ASEAN, GCC, and China summit concluded with a call to action for advancing a cross-regional framework to promote the digital economy, including AI, deepening regional economic ties, and adopting inclusive growth strategies	May-25
Malaysia, GCC	The GCC and Malaysia have officially launched negotiations for a Free Trade Agreement (FTA), with the agreement expected to cover a wide range of areas, including trade in goods and services, investment, trade facilitation, and broader economic cooperation	May-25
Malaysia, UAE	Malaysia and the United Arab Emirates (UAE) signed a Comprehensive Economic Partnership Agreement in January 2025, the first for Malaysia with a GCC country	Jan-25
Indonesia, GCC	The second round of FTA negotiations was held in February between Indonesia and the GCC, with the discussion focused on accelerating the agreement's completion, targeting a substantive deal by the end of 2025	Feb-25
Indonesia, Qatar	Indonesia's Sovereign Wealth Fund, Danantara, and the Qatar Investment Authority launched a USD4bn investment fund in April, with each agreeing to commit USD2bn	Apr-25
Indonesia, UAE	The UAE is reported to invest up to USD2bn in several Indonesian SOEs, with a pledge to invest up to USD20bn by 2030. Some of the agreed investments have already included the Abu Dhabi Investment Authority (ADIA) investment in the Java Trans Toll Road	Feb-25
Indonesia, Saudi Arabia	Indonesia and Saudi Arabia signed a preliminary agreement to enhance cooperation in the mining and minerals sector, including the exchange of expertise and knowledge transfers between the two countries	Apr-25
Thailand, GCC	Thailand is accelerating FTA negotiations with the GCC, with both sides agreeing on the opportunity to deepen collaboration in tourism, food security, and soft power	Feb-25
The Philippines, UAE	The Philippines' first FTA with a Middle Eastern country is set to be signed this year in June 2025 with the UAE	May-25
Vietnam, Oman	The Oman Investment Authority has signed an MoU with the State Capital Investment Corporation (SCIC) to increase its commitment from USD200mn to USD600mn, paving the way for a USD1bn investment	Jun-25

Source: Jakarta Globe, Jakarta Post, Arab News, Bloomberg, Reuters, OCBC.

Thematic Report 2

US push for deep-sea mining adds to global uncertainty

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- The US push for deep-sea mining, driven by the growing demand for critical minerals, aims to secure domestic supply chains and counter China's dominance in the industry.
- However, it poses significant environmental and social risks, bypasses international frameworks, and potentially increases geopolitical tensions and regulatory uncertainty.
- This move also risks fragmenting ocean governance frameworks and challenges international cooperation, increasingly reducing the role of the US in global environmental and climate action.

Deep-sea mining: Drivers and impacts

Deep-sea mining refers to the process of retrieving mineral deposits from the deep seabed at ocean depths greater than 200m. There is increasing interest in deep-sea mining due to depleting terrestrial deposits of metals including copper, nickel, aluminium, manganese, zinc, lithium and cobalt. There has also been greater demand for these metals due to their use in producing low-carbon technologies such as wind turbines, solar panels and EV batteries, as well as other advanced technologies such as smartphones.

Considering the projected rise in metals consumption through 2050 with global net-zero commitments, existing production levels of metals like cobalt and nickel fall short, with a shortfall of at least two-thirds compared to demand. Similarly, the supply of metals such as copper and lithium is also insufficient to meet future needs, with a gap of 30% - 40% relative to demand.

However, as the deep sea remains understudied and is not well understood, there are many gaps in knowledge of deep-sea biodiversity and ecosystems which are known to be highly sensitive and slow to recover. Recent studies highlight that deep-sea mining escalates environmental risks by 13% and social risks by 8% – 11%, compared to scenarios relying on land-based mining and other circular economy solutions. Deep-sea mining can cause the disturbance to or irreversible loss of deep-sea habitats, which may lead to the loss of species and critical ecosystem functions. Pollution may also arise from possible leaks and spills of fuel and other hazardous substances from mining equipment. In addition, the ocean floor acts as a carbon sink that, if disrupted, may release stored carbon dioxide into the atmosphere.

Trump administration's push for deep-sea mining

President Trump signed an executive order on 24 April in support of domestic and international seabed mineral resource exploration, extraction, processing and environmental monitoring. The move to boost deep-sea mining aims to strengthen a robust domestic supply chain for critical minerals derived from seabed resources, as well as to counter China's dominance in the industry. China currently produces around 70% of critical minerals and 90% of rare earths from land-based mining.

US authorities are expected to develop a plan to map priority areas of the seabed, engage with key partners for seabed mineral resource exploration, and expedite the process for reviewing and issuing seabed mineral exploration licenses and commercial recovery permits in areas beyond national jurisdiction under the Deep Seabed Hard Mineral Resources Act. Following the signing of the executive order, a deep-sea mining firm called The Metals Company sought the Trump administration's approval of its plans to mine the international seabed, potentially positioning itself as the first seabed mining firm to obtain a license to exploit minerals in international water.

This highlights the continued prioritisation of oil, gas and mining interests over climate change mitigation under the Trump administration. It aligns with the broader trend of rolling back climate policies from the Biden administration, increasingly reducing the role of the US in global environmental and climate action.

Regulatory challenges on top of environmental and social risks

The push for deep-sea mining also challenges the frameworks established under the United Nations Convention on the Law of the Sea (UNCLOS) and the International Seabed Authority (ISA), setting the stage for heightened geopolitical tensions, growing global uncertainty and escalating environmental concerns.

The ISA, established under the UNCLOS that the US has not ratified, has been developing regulations for deep-sea mining in international waters for years. These regulations, known as the Mining Code, are still under negotiation and have not been formalised due to the complexities of the industry. The ISA aims to finalise its regulations for commercial deep-sea mining in international waters by July 2025, which will be critical to shaping the future of the industry. Many countries, including China, have postponed the issuance of deep-sea mining permits until countries have agreed how such resources should be shared.

By bypassing the ISA, the US is risking the fragmentation of global ocean governance frameworks that may encourage other nations to pursue similar unilateral actions. This undermines the principle that seabed resources are designated as common heritage of mankind regulated under UNCLOS.

Rising tensions and global uncertainty

The US push for deep-sea mining may accelerate competition for seabed minerals, increase the risks of ecological collapse, heighten international conflicts and legal disputes, as well as enhance geopolitical risks.

US-China tensions are increasingly playing out in the deep-sea mining field, with both nations seeking to secure mineral resources essential for various technologies. China has also viewed the US push for deep-sea mining as a violation of international law.

In response to US actions, other countries may be encouraged to increase their own deep-sea mining objectives. The escalating tensions are likely to further fragment global ocean governance efforts and complicate international cooperation,

potentially increasing the risk of conflict over scarce resources. This threatens to destabilise global critical mineral markets and supply chains that can lead to price volatility, creating uncertainty for investors and related industries globally.

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Silver: A Silver Lining in Volatile Times

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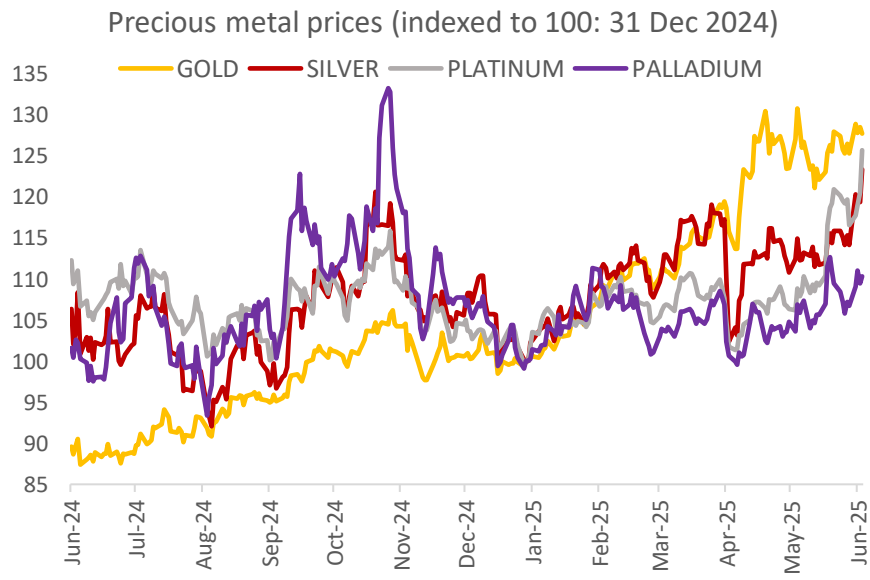
The outlook for silver remains positive. We modelled the relationship between several key drivers in attempt to find the "fair value", which appears to suggest that there is room for further upside. The potential for post-war reconstruction in Ukraine and Gaza, at some point could further boost demand for silver in infrastructure and technology applications. Additionally, silver's role in the low-carbon transition, alongside its traditional safe-haven appeal amid geopolitical uncertainties and inflationary pressures, enhances its attractiveness to investors. With ongoing challenges in global silver supply and positive spillover effects from gold's rally, silver is well-positioned as both a critical industrial metal and a reliable investment asset in the evolving economic landscape.

Recent silver rally and demand drivers

Prices of silver continue to rise alongside other precious metals, including gold, platinum and palladium this year. YTD as of 5 Jun, gold leads with 27% gain, followed by platinum at 25% and silver trailing at 23%. The surge in silver prices is attributed to a confluence of drivers, including geopolitical and economic policy uncertainties, such as Trump tariffs, industrial demand (solar panels), and diversification flows due to the de-dollarisation trend, which have boosted the appeal of precious metals.



Source: Bloomberg, OCBC Research

Historical context – Silver

Over the past 50 years, silver has experienced several significant price surges, typically driven by a combination of monetary factors, geopolitical tensions, and industrial demand shocks. By looking at historical silver prices and economic events, we attempt to better understand the primary drivers behind silver price surges.

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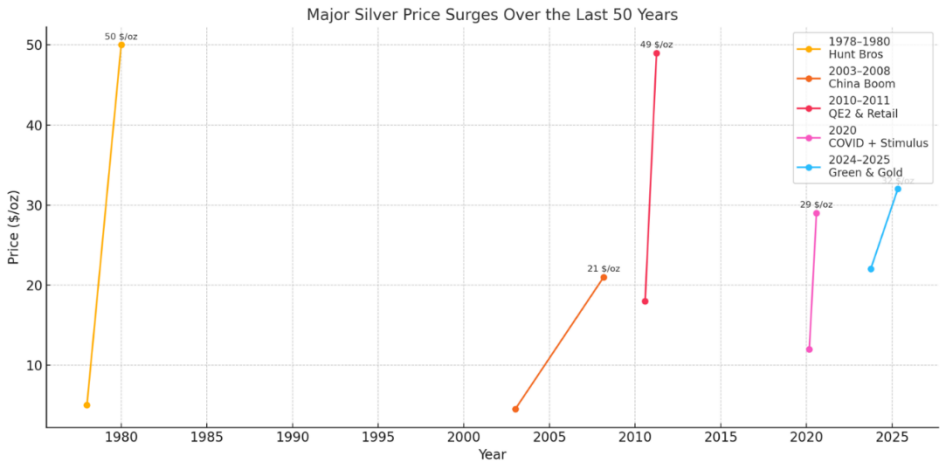

Source: Bloomberg, OCBC Research

Late 1970s – Early 1980s: During this period, silver prices soared to approximately $50/oz, marking a tenfold increase from around $5/oz. This surge, which lasted from 1978 to January 1980, was primarily driven by the Hunt Brothers' attempt to corner the silver market. The Texas oil tycoons aggressively purchased physical silver and futures, controlling over 100 million ounces of silver at one point. Additionally, high inflation and a weak U.S. dollar, compounded by geopolitical tensions such as the Iranian Revolution in 1979 and the Soviet invasion of Afghanistan, contributed to the rally. Investors sought hard assets like gold and silver as hedges against inflation, and prices were further fuelled by a speculative frenzy characterised by increased leverage and retail participation. However, this bull market ended abruptly in March 1980 when the COMEX changed margin rules, leading to a dramatic collapse in prices back to around $10/oz.

2003–2008 Commodity Supercycle: Silver experienced another significant surge from 2003 to March 2008, with prices rising from approximately $4.50 to $21/oz. This price movement was largely driven by a commodity boom led by China's rapid industrialisation, which significantly increased silver demand particularly in electronics and solar applications. The weak U.S. dollar and the Federal Reserve's monetary policy easing following the dot-com bubble and the September 11 attack also played a crucial role. The launch of silver exchange-traded funds (ETFs), such as SLV in 2006, provided investors with easier access to the market. Additionally, the rally in precious metals was supported by gold's rise from around $400/oz to $1,000/oz during this period. However, the 2008 Global Financial Crisis resulted in a sharp correction, with silver prices falling back to approximately $9/oz due to liquidity-driven selling.

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2010–2011 QE-Driven Rally: Another notable surge occurred between August 2010 and April 2011, when silver prices climbed from about $18/oz to nearly $49/oz. This rally was primarily fuelled by the implementation of Quantitative Easing (QE1 and QE2), which raised inflation fears in the aftermath of the Global Financial Crisis. Concerns over U.S. dollar debasement due to rising national debt and fears of fiat currency dilution also contributed to the surge. Retail and speculative mania played a significant role, as silver was perceived as a "poor man's gold," attracting substantial retail inflows. Additionally, the compression of the gold-to-silver ratio led investors to rotate into silver, believing it was undervalued compared to gold. However, this rally was short-lived, as the CME raised silver margins multiple times in May 2011, triggering a sharp correction that saw prices fall below $30/oz by the end of 2011.

2020–2021 COVID and Stimulus Rally: The most recent surge occurred between March and August 2020, with silver prices increasing from approximately $12/oz to $29/oz. This rally was driven by massive global stimulus measures, including trillions in fiscal and monetary support, and low real interest rates. Investors sought silver as an inflation hedge amid fears of future inflation stemming from extensive money printing. A retail frenzy, often referred to as the "silver squeeze," was fuelled by social media platforms like Reddit, temporarily pushing prices above $30/oz. Additionally, rising expectations for solar demand in the wake of the COVID-19 pandemic contributed to the surge. However, the lack of follow-through and eventual tightening by the Federal Reserve tempered the rally.

Since-2024 Green, Gold, De-dollarisation wave (Ongoing): Since early 2024, silver has experienced 2 waves of price increases, from $22/oz to a high of $34.80/oz in October 2024 before retracing lower. The second wave started at the start of 2025, with silver prices rising from $29/oz to $33-$34/oz. Current drivers of this rally include expectations of Federal Reserve rate cuts. Gold's recent rally to new all-time highs is also spilling over into silver markets. Strong industrial demand for silver, particularly in solar panels, electric vehicles, and green technology, is further supporting prices. Additionally, tight supply conditions, with global silver production remaining relatively flat and rising deficits, are contributing to the upward momentum. Finally, the de-dollarisation narrative, with emerging market central banks seeking to diversify their reserves, is adding to the bullish sentiment surrounding silver.

Silver price model and "fair value" assessment

Drawing on the last 50 years of silver price cycles — marked by sharp surges and corrections — we identify recurring macro drivers such as geopolitical tensions, inflation concerns, monetary policy shifts, investor sentiment, and industrial demand.

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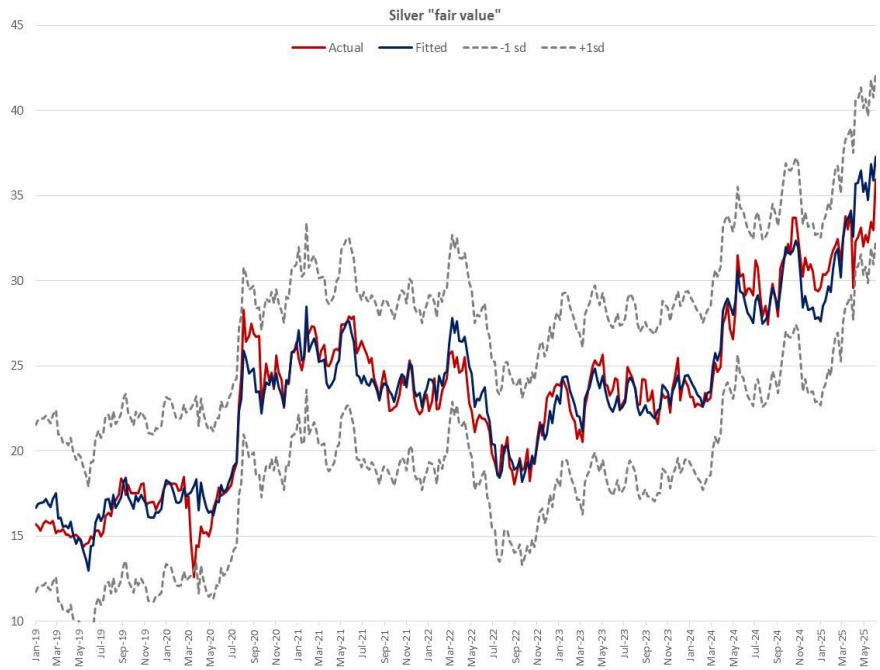
To quantify these dynamics, we employ a reduced-form econometric model that estimates silver's "fair value" based on key macro and market-based inputs. Specifically, the model incorporates: COMEX silver positioning (as a proxy for investor sentiment); 10-year breakeven inflation rates (proxy for inflation expectations, shifts in market expectations on monetary policy, economic conditions); Gold prices (proxy for safe-haven demand), US 10y real yields (opportunity cost of holding non-yielding assets); prices of copper (as proxy to industrial demand); and the DXY dollar index (USD trend).

Using current values for these inputs, the model suggests a fair value for silver around $37.40/oz, compared to the prevailing spot price of approximately $36/oz. This implies there is still some upside potential for silver, should macro conditions remain supportive, or sentiments strengthen further.



Notes: OLS regression on weekly frequency data starting 1 Jan 2019 till 4 June 2025
Source: Bloomberg, OCBC Estimates

Strong momentum behind low-carbon transition persists

The industrial applications of silver are diverse, spanning electronics, solar energy, automotive and medical technologies. The importance of silver's role in the low-carbon transition is evident in its various applications across Electric Vehicles (EVs) and renewable energy technologies. Silver possesses the highest electrical and thermal conductivity of all metals, a property that is especially important in technologies such as EV batteries and solar photovoltaic (PV) cells.

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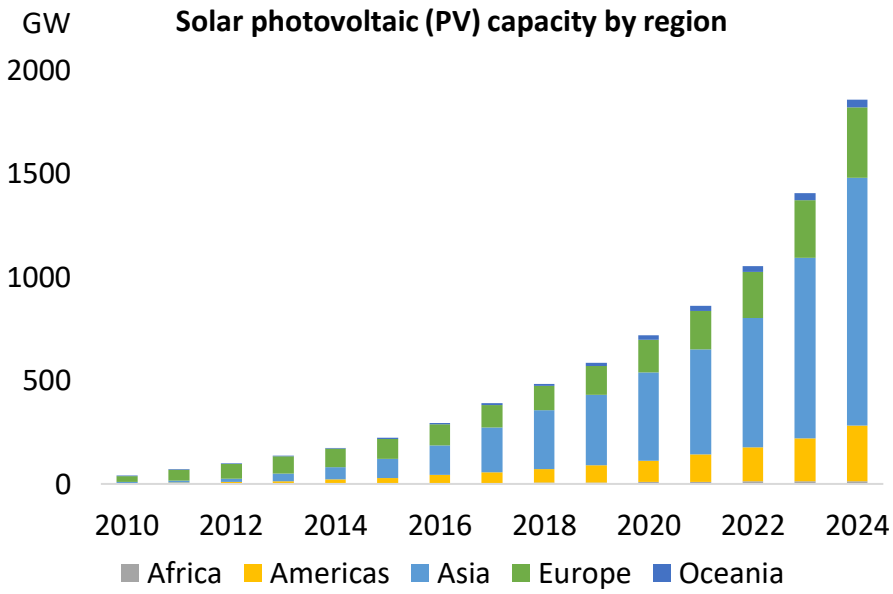
Robust growth in the solar sector is expected to remain a major factor in driving silver demand, with a significant portion of this growth projected to come from China as the global leader in solar PV installations. China broke its own records for new solar power installations in 2024, with installed solar capacity increasing by 45.2%, according to China's National Energy Administration. While China is facing solar panel oversupply issues, a more balanced supply-demand situation may be achieved by 2027 following continued policy tightening and industry consolidation. Many countries are also pushing for greater adoption of renewables as they strive towards reducing their reliance on fossil fuels, in efforts to achieve their climate targets.



Source: IRENA, OCBC Research

According to the IEA's Global Energy Review, 80% of the growth in global electricity generation was provided by renewable sources and nuclear power. Global new renewables installations hit record levels for the 22nd consecutive year, of which nearly 80% was solar PV. As the demand for solar energy continues to rise, silver's critical role in solar PV is likely to further support prices.

There are also important applications in other nascent low-carbon technologies such as carbon capture and storage (CCS) and nuclear. The stability of silver at high temperatures can enhance the cost-effectiveness of CCS technologies, in addition to its use as a material in nuclear reactors' control rods to control the rate of nuclear fission. This is due to the metals' high mechanical strength and corrosion-resistant properties, that allows it to absorb neutrons without undergoing nuclear fission itself. Nuclear power currently accounts for around 10% of global electricity supply and is experiencing renewed momentum, set to reach a new record in 2025 and bolster energy security as electricity demand accelerates. There is growing interest in harnessing nuclear power, because of advanced nuclear technologies that offer enhanced safety and suitability for urban environments e.g. small modular reactors. This interest reflects a broader trend towards exploring diverse energy sources to ensure enhanced energy resilience.

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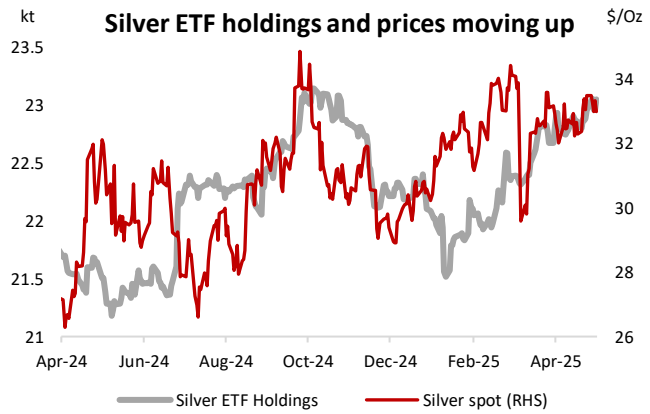
The Trump administration, despite halting support for many clean energy initiatives, has expressed support for nuclear energy. This can facilitate new opportunities for partnerships between the US and Southeast Asia in nuclear technology transfer and capacity building, particularly given the growing interest and renewed optimism for nuclear energy in Southeast Asia. For example, it was announced at Singapore Budget 2025 in February that Singapore will study the potential deployment of nuclear power in Singapore, with plans to develop related capabilities, including nuclear safety. Indonesia also aims to incorporate 10GW of nuclear power as part of its clean energy expansion plans by 2040.

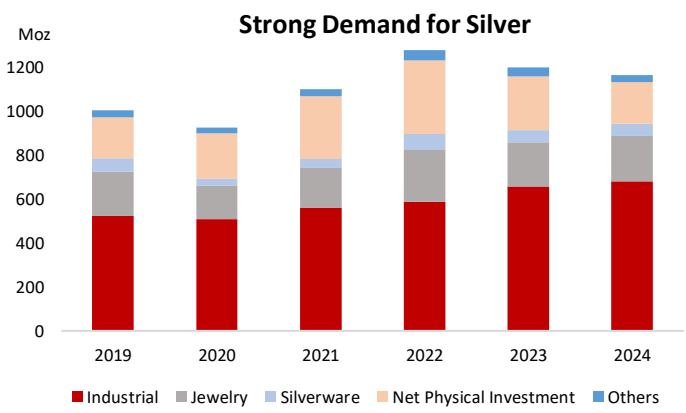
Therefore, the properties of silver allow it to play an important role in the ongoing low-carbon transition across various technologies. As demand from clean energy industries continues to rise, it is likely to further support silver prices.

Safe-haven appeal of silver

Beyond its industrial applications, silver has long been viewed as a safe-haven asset. When geopolitical risks, inflationary pressures, or financial instability rise, investors often turn to precious metals like gold and silver to preserve wealth.

1. **Geopolitical Risks and Market Volatility**: Even if conflicts in Ukraine and Gaza de-escalate, other geopolitical risks—such as tensions in the Taiwan Strait or global economic instability—could sustain demand for safe-haven assets.
2. **Monetary Policy and Inflation Hedge**: Historically, silver has served as an inflation hedge. With central banks navigating interest rate policy shifts, any dovish turn could support silver prices by making non-yielding assets more attractive.
3. **Retail and Institutional Investment Demand**: ETFs backed by physical silver, as well as growing retail interest in silver bullion and coins, highlight the metal's continued role as a wealth preservation asset. As macroeconomic uncertainty persists, silver's safe-haven status will likely continue to attract investor demand alongside its industrial applications.





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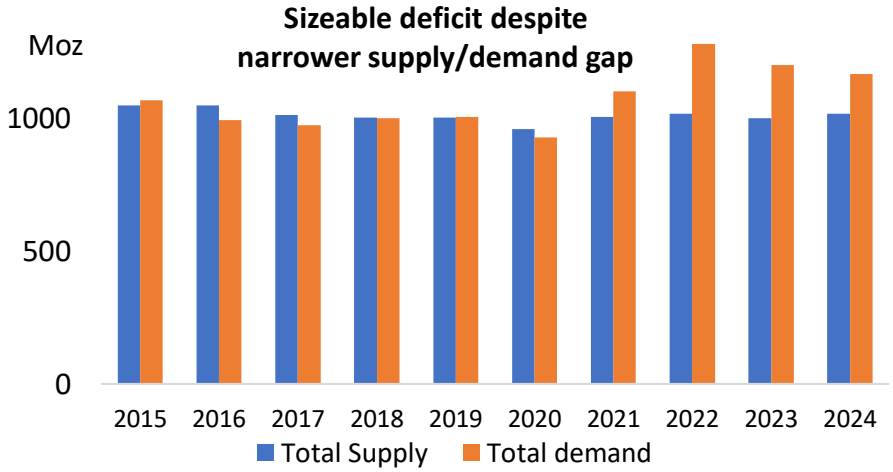
Potential demand for post-war reconstruction

The potential resolution of conflicts in Ukraine and Gaza, at some point could lead to significant reconstruction efforts, thereby increasing the demand for industrial metals, including silver.

1. **Infrastructure and Construction:** Post-war rebuilding efforts typically involve large-scale infrastructure development, including power grids, telecommunications, and transportation systems. Silver, with its superior conductivity and corrosion resistance, plays a crucial role in these areas.
2. **Electronics and 5G Expansion:** Silver is a critical material in electronic components and 5G technology. The push for modernisation post-conflict could drive additional demand in these areas, reinforcing silver's industrial importance. While industrial demand alone may not dictate silver's price, its dual role as a precious metal enhances its appeal, particularly in uncertain economic conditions.



Source: Metals Focus, OCBC Research

The outlook for silver remains constructive, driven by five key factors: strong momentum behind the low-carbon transition, safe-haven appeal, physical market undersupply, positive spillover effects from gold prices onto other "less expensive" precious metals and potential industrial demand for post-war reconstruction demand.

As global markets navigate evolving geopolitical and economic landscapes, silver remains well-positioned as both a critical industrial input and a reliable investment asset.

Technical momentum appears supportive

Silver (XAG) rose ~25% since start of the year. Last at 36.15 levels. Underlying momentum as seen on monthly and weekly charts remain bullish though RSI is approaching near-overbought conditions. Key resistance at 35.22 (61.8% fibo retracement of 2011 high to 2020 low). Sustained price action above this level should continue to see price momentum build up further. Next resistance at 40.80(76.4% fibo), 44 levels. Support at 33.60 (21 DMA), 30.72 (50% fibo).

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Source: Bloomberg, OCBC Research

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RMB Internationalization: New engines

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- Beyond trade finance, Renminbi (RMB) internationalization has entered a new phase, driven by strong growth in offshore CNH lending and onshore Panda bond issuance.
- Amid escalating geopolitical tensions, China has also redefined RMB internationalization as a tool to achieve financial autonomy and strategic control.
- Looking ahead, we believe the next chapter of RMB internationalization will be shaped by its new role as a funding currency and the accelerated buildout of cross-border payment infrastructure.

Since President Trump's announcement of the "Liberation Day" tariffs, the global conversation around de-dollarization has regained momentum. This renewed scrutiny of the USD's dominance is unfolding against a broader backdrop of shifting geopolitical alignments, trade frictions, and monetary fragmentation. Notably, these dynamics have reinforced the accelerating trend of RMB internationalization, which picked up pace following the outbreak of the Russia-Ukraine war in 2022. In this article, we examine the latest developments in the global use of the RMB and the evolving engines.

RMB Internationalization: A five-stage evolution

To recap, China's RMB internationalization has evolved through five distinct phases. The internationalization process began in 2004 when Hong Kong started accepting offshore RMB deposits. However, momentum remained limited until July 2009, when China formally permitted the use of RMB in cross-border trade settlements, laying the groundwork for broader international usage.

The launch of the offshore RMB market (CNH) in July 2010 marked a turning point, triggering rapid expansion in RMB usage. However, expectations of sustained RMB appreciation and opportunities for cross-border arbitrage based on interest rate and exchange rate differentials led to data distortions and inflated the apparent scale of internationalization.

Rising capital outflows and financial stability concerns in 2015 prompted Chinese authorities to tighten cross-border RMB usage. This policy shift caused a significant contraction in offshore RMB activity and a partial reversal of earlier gains in international adoption between 2015 and 2017.

Nevertheless, with financial risks largely contained, China gradually reopened its capital account from 2018 onward. This phase saw a marked increase in RMB usage under capital account transactions. For the first time since 2017, cross-border RMB flows related to capital transactions surpassed those under the current account, signalling a structural shift in international usage patterns.

The outbreak of the Russia-Ukraine war in 2022 and intensifying global geopolitical fragmentation prompted many Global South economies to diversify away from the USD. This trend, reinforced by the Trump administration's global trade tensions and

growing concerns over USD weaponization, has led to a renewed acceleration in RMB internationalization.

RMB's new role as global funding currency

We have witnessed a gradual but steady trend of decline of USD in global usage such as reserve currency and payment currency. Nevertheless, despite falling shares, USD has remained a dominant trade finance currency accounting for almost 82% share by end of 2024, according to the SWIFT.

Chart 1: Trend of decline of US dollar in global usage of trade finance currency

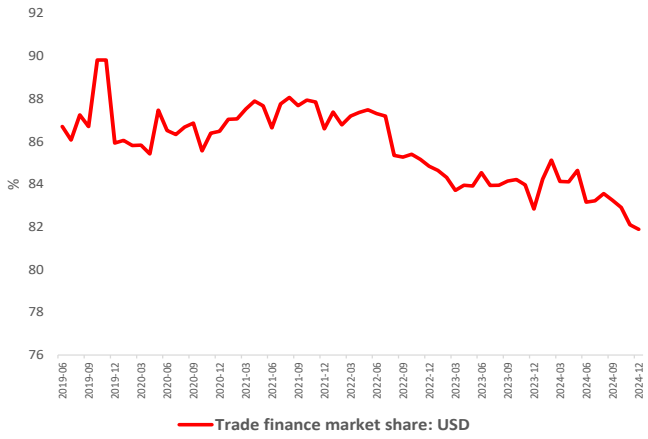
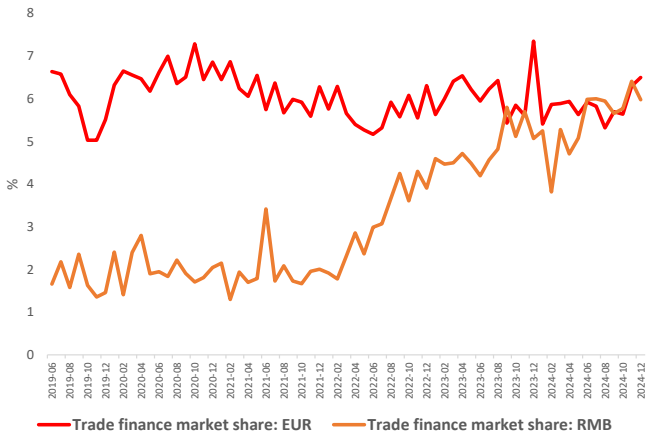


Chart 2: RMB's share in global trade finance has risen rapidly in the past few years



There are five reasons why USD has much higher share in trade finance than in global payments. Firstly, USD is the dominant invoicing currency in global trade given most global commodities and raw materials (oil, copper, soybeans) are priced in USD. Secondly, USD dominates the global trade finance infrastructure. For example, USD-based L/Cs [spell out Letters of Credit if using acronym for first time] are more widely accepted, operationally supported, and technologically integrated. Thirdly, there is legal and institutional trust in the USD system. USD-based instruments are backed by U.S. law, which is globally trusted for contract enforcement, arbitration, and dispute resolution. Fourthly, the global USD pool is vast — banks can easily access, borrow, and deploy USD for trade purposes. Fifthly, USD has the most extensive global clearing network including clearing system like CHIPS and major banks such as JPM and Citi.

That said, RMB's share in global trade finance has risen rapidly in the past few years, surpassing EUR to make it the second-most used currency for trade finance after the USD. RMB's adoption can be attributed to a few factors. First, there is policy push from China for RMB Internationalization on the back infrastructures building such as the bilateral currency swap lines and expansion of Cross-Border Interbank Payment System (CIPS), a RMB-based alternative to SWIFT. Second, China is increasingly pushing for RMB pricing in energy and bulk commodities. For example, the Shanghai crude oil futures contract (INE) provides a RMB-based benchmark. Third, the rising geopolitical risk and sanction hedging also lent the support to the use of RMB. Many firms — especially in countries like Russia, Iran, parts of Africa, and the Middle East — are deliberately shifting to RMB trade finance to reduce exposure to U.S. oversight. Even non-sanctioned countries are increasingly aware

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of the "weaponization of the dollar", prompting diversification. Lastly, China's falling interest rates amid global tightening in 2022 also make RMB more appealing to be a funding currency.

Beyond trade finance, RMB internationalization has entered a new phase, driven by strong growth in offshore CNH lending and onshore Panda bond issuance.

In Hong Kong, outstanding CNH loans have tripled over the past three years to exceed CNY600bn, up from just CNY200bn. Meanwhile, the outstanding volume of Panda bonds—RMB-denominated bonds issued by foreign entities in China—has doubled, with figures from the Shanghai Clearing House showing a rise from CNY150bn in 2021 to over CNY300bn as of early 2025. These developments reflect both rising demand for RMB funding and growing investor confidence in RMB assets.

Chart 3: CNH loan surged in Hong Kong

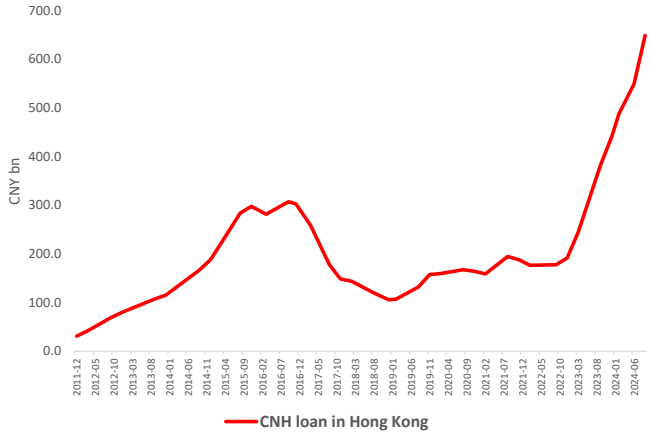
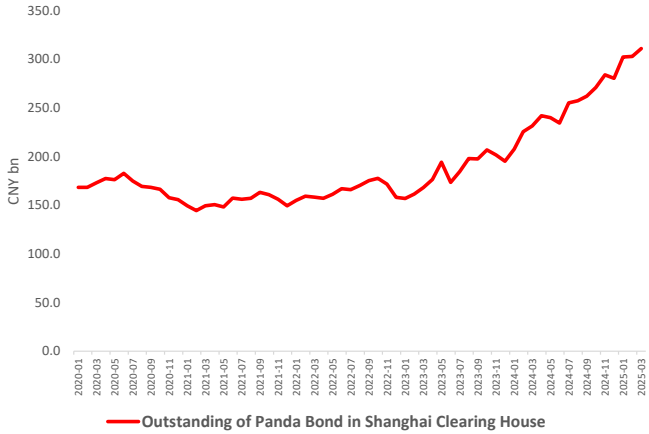


Chart 4: The issuance of panda bond also increased



Reshaping the landscape for cross border payment

Amid escalating geopolitical tensions, China has also redefined RMB internationalization as a tool to achieve financial autonomy and strategic control. This include expanding the global coverage of the Cross-Border Interbank Payment System (CIPS), actively developing the central bank digital currency (CBDC), and advancing decentralized cross-border payment systems such as the mBridge (Multi-CBDC Bridge) platform.

CIPS has seen rapid growth, with 8.22 million transactions totaling CNY175.49trn processed in 2024—up 42.6% YoY. As of end-March 2025, CIPS had 170 direct participants and 1,497 indirect participants, with a network spanning 186 countries and regions. CIPS is now a core pillar of China's cross-border financial infrastructure, increasingly seen as a viable alternative to SWIFT, especially for Belt and Road economies.

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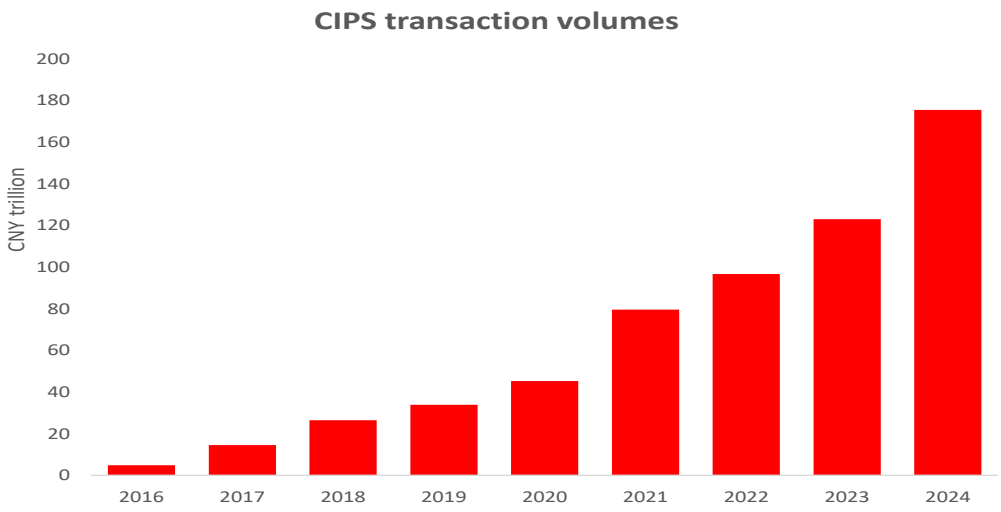
Chart 5: The increasing usage of CIPS.



China's e-CNY (digital yuan) initiative, together with its participation in mBridge, is reshaping cross-border payments. The mBridge platform, launched in 2021 in collaboration with the Hong Kong Monetary Authority, Bank of Thailand, and the UAE Central Bank, leverages distributed ledger technology (DLT) to enable real-time FX conversion, clearing, and settlement. Through "payment versus payment" protocols and peer-to-peer connections between participating banks, mBridge greatly reduces settlement risk and transaction cost, while enhancing transparency and regulatory oversight.

Together, CIPS and e-CNY form a "dual-engine" cross-border payment model that promotes greater resilience and autonomy for China's financial system. CIPS enhances the institutional and infrastructural reach of RMB, while e-CNY offers programmable, efficient, and secure digital settlement capabilities.

Looking ahead, we believe the next chapter of RMB internationalization will be shaped by its new role as a funding currency and the accelerated buildout of cross-border payment infrastructure. The convergence of market demand, policy push, and technological innovation sets the stage for the RMB to expand its global influence in a more multipolar financial world.

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US: The One Big Beautiful Bill (or not)

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- US President Trump's "One, Big, Beautiful Bill" was narrowly cleared at the House of Representatives on 22 May 2025, with a final vote tally of 215-214. The bill seeks to fulfil some of President Trump's campaign promises but is expected to cost USD3.8trn over the decade, according to estimates by the Congressional Budget Office (CBO).
- House Speaker Mike Johnson said 4 July would be the ideal deadline to clear both legislative chambers and get it to the president's desk.
- Bills that mature around late August/early September period traded at mildly higher yield levels, but the bill yield curve suggests that investors are not overly concerned about the debt ceiling.

The One Big Beautiful Bill

US President Trump's "One, Big, Beautiful Bill" was narrowly cleared at the House of Representatives on 22 May 2025, with a final vote tally of 215-214. The bill has been sent to the Senate for approval, where it will require only a simple majority. The bill seeks to fulfil some of President Trump's campaign promises but is expected to cost USD3.8trn over the decade, according to estimates by the Congressional Budget Office (CBO). For the bill in brief, we summarize the following and illustrate in detail below:

1. **Tax cut**. The bill aims to extend the tax provisions introduced during Trump's first term in 2017, with a goal of a $4.5trn tax reduction over the next decade according to calculations from the Tax Foundation.

   While the legislation leans heavily on prioritizing the continuity of the tax reform in 2017 over some new bold initiatives such as including tax reductions on permanent personal tax and expanding childcare credit, the bill's incremental additions and scale of expansion in term of tax cuts remain limited, likely constrained by the fiscal deficit pressures. For instance, personal and corporate income tax rates are not further reduced, but only extended. Meanwhile, most of the tax incentives are set with expiration dates (e.g. car loan interest tax exemption, standard deduction, and child tax credit are only temporarily effective until 2028 rather than made permanent).

2. **Spending reductions.** With the key goals to restore fiscal health and responsibility, the bill introduces substantial spending cuts, including approximately ~US1trn in reductions to Medicaid health coverage and the Supplemental Nutrition Assistance Program (SNAP). The change of the bill would result in stricter eligibility of these programs, applying additional requirements to U.S. citizens, green card holders, and designated refugee groups. In addition, there will be an early termination of the USD7,500 consumer tax credit for electric vehicles after 2025. Subsidies for households upgrading to energy-efficient home improvements will cease entirely by year-end.

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3. **Border security and defence funding.** The legislation earmarks nearly USD200bn for the national security initiatives and restarting the construction of US-Mexico border wall.

4. **Debt ceiling.** The plan will raise the nation's debt ceiling by USD4trn. Considering the U.S. government deficit in FY2024 was USD1.83trn, a rough calculation can show that raising the debt ceiling by $4 trillion can support approximately two years of fiscal spending needs. This could effectively push back the next round of debt ceiling negotiations after the midterm elections in 2026.

   The Congressional Budget Office (CBO) estimates the bill will add USD3.8trn to the total USD36.2trn in debt over the next decade and deficit may stretch to around 7% of GDP in coming years. While this may stimulate growth in the short term, it raises significant concerns about the rising trajectory of debt and deficits in the medium term, as well as the associated sovereign credit risk.

Table 1: The One Big Beautiful Bill in Brief

Provision	Details
Individual Tax	Makes permanent the modified federal income tax bracket schedule and lower tax rates created by the Tax Cuts and Jobs Act (SEC. 110001)
	Standard deduction enhancement of USD 1,000 for single filers, USD 1,500 for head of household filers, and USD 2,000 for joint filers (SEC. 110002)
	Above-the-line deduction for tips any overtime pay, excluding highly compensated employees (SEC. 110101, 110102)
	Imposes a five percent excise tax on remittance transfers (SEC. 112105)
Child Tax	Increase the maximum child tax credit by USD 500 to USD 2,500 for tax years 2025 through 2028 (SEC. 110004)
	Pilot program of one-time USD 1,000 credit deposited into "MAGA Accounts" for newborns (SEC. 110116)
Estate and Gift Tax	Extends the estate and lifetime gift tax exemption, increases the exemption amount to USD 15 mn for single filers (USD 30 mn for married filing joiuntly) in 2026, and indexes the exemption amount for inflation going forward (SEC. 110006)
Business Tax	Extension of deduction for qualified business income and permanent enhancement. For taxable years beginning after December 31, 2025, this provision also increases the deduction percentage from 20 percent to 23 percent (SEC. 110005)
	100 percent bonus depreciation allowance for short-lived property and certain structures (SEC. 111001)
	Business net interest deduction based on EBITDA (SEC. 111003)
Tariffs	Modifications to de minimis entry privilege for commercial shipments (SEC. 112031)
Medicare	Limiting Medicare coverage to lawful permanent residents, certain Cuban immigrants, and individuals living in the United States through a Compact of Free Association (SEC. 112104)
Others	No Tax on car loan interest (SEC. 110104)
	Termination of qualified bicycle commuting reimbursement exclusion (SEC. 110012)
	SALT cap increase to USD 20,000 for married individuals filing separately (USD 250,000 income limit) and USD 40,000 in the case of any other taxpayer (USD 500,000 income limit). (SEC. 112018)
	Implementing AI tools for purposes of reducing and recouping improper payments under Medicare (SEC. 112204)
	Increases the public debt limit by USD 4trn (SEC.113001)

Source: US House Committee, Tax Foundation, OCBC Research

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Table 2: Deficit effect of One Big Beautiful Bill

Provision	Deficit Increase (-) / Decrease (USD bn)
Extend & Expand Rate Cuts	-2,177
Extend AMT Repeal for Most Taxpayers	-1,414
Extend & Expand Standard Deduction Hike	-1,308
Repeal Personal/Dependent Exemption	1,870
Extend & Expand Child Tax Credit Increase	-797
Extend & Expand 199A Pass-Through Deduction	-820
Replace Pease w/ Itemized Deduction Limit	41
Cap SALT at $30k, phased down to $10k at Higher Incomes; Reduce Workarounds	916
Extend Other Deduction Changes	47
Extend & Expand Estate Tax Cut	-212
Subtotal, Extend & Expand TCJA Individual Provisions	**-3,855**

Source: Committee for a Responsible Federal Budget, Bloomberg, OCBC Research

What happens next?

The 'One Big Beautiful Bill' has been approved by the U.S. House of Representatives and now heads to the Senate for amendments before entering a reconciliation process via a conference between the two chambers. House Speaker Mike Johnson said 4 July would be the ideal deadline to clear both chambers and get it to the president's desk.

Given the bill act was passed by a narrow vote of 215-214, some disagreements are expected over the tax code, Medicaid and immigration, and this may complicate the progress of the legislative agenda despite the Republican majorities. According to the congressional calendar 2025, both chambers will be out for the traditional August recess, and if the senate fails to complete its deliberation in July, the bill's enactment timeline could be delayed to September.

Chart 1: Bill now moves on to the Senate

Source: Congress.gov, OCBC Research

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Table 3: 2025 Congressional Calendar

Source: Offices of House Majority Leader Steve Scalise and Senate Majority Leader John Thune, Roll Call, OCBC Research

The Debt Ceiling

Since the statutory limit was already hit at the start of January this year, the US Treasury has been using extraordinary measures, together with its cash balance (Treasury General Account balance) to fulfil federal obligations. The US national debt stands currently at USD36.2trn; interest payments alone amounts to a daily average of USD2.6bn (USD952bnin FY25, according to CBO). TGA balance stood at USD351bn on 30 May, while extraordinary measures left were at USD68bn as of 28 May.

The potential "X-date" is probably weeks away, as US Treasury Secretary Scott Bessent stated that the federal government's cash and extraordinary measure could be exhausted by August this year. If the legislation of the One Big Beautiful Bill/debt ceiling is not passed in time, it may result in a government shutdown.

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Chart 2: US Debt Limit

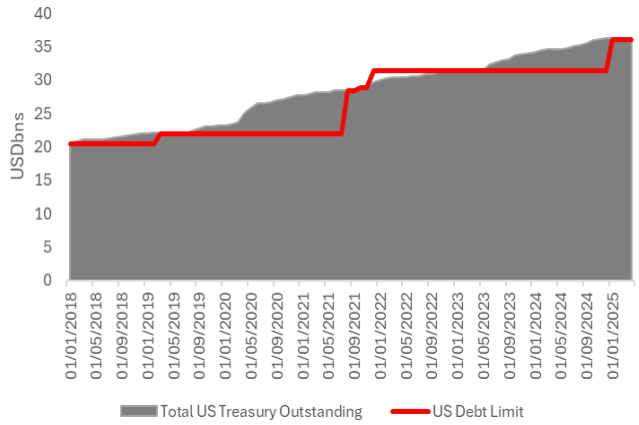
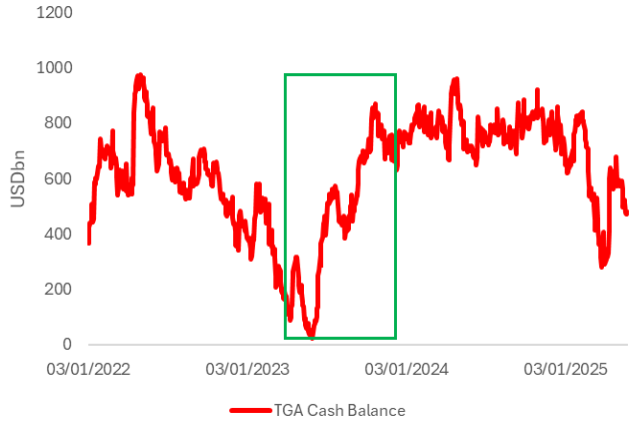


Chart 3: TGA Cash Balance



Nevertheless, our rates strategist noted that bill yield curve suggests that investors are not overly concerned about the debt ceiling. Bills that mature around late August/early September period traded at mildly higher yield levels, through this "yield premium" remained narrow, ranging within 5-10bps.

Chart 4: Following the U.S. debt ceiling crisis was resolved in 2023, USTs yields grinded higher in the 2H23

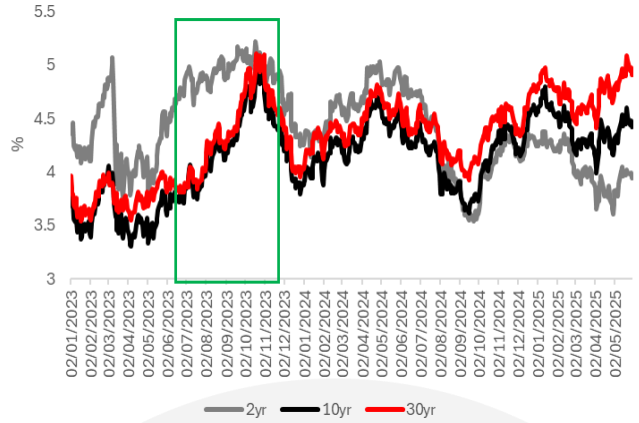
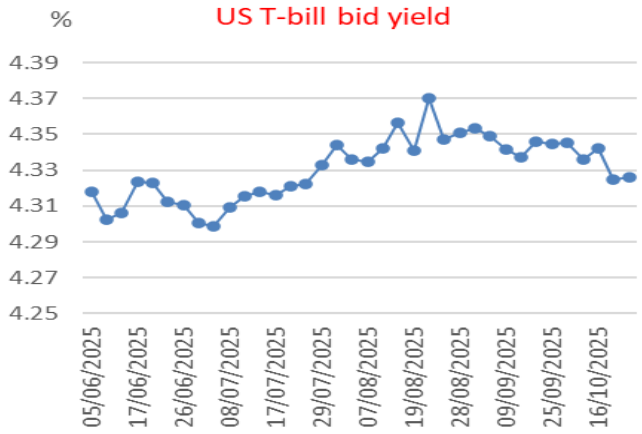


Chart 5: Yield premium remains low



Source: Bloomberg, OCBC Research

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Hong Kong: Why stick to the HKD peg?

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The Linked Exchange Rate System and de-peg debate

Hong Kong's Linked Exchange Rate System (LERS) has operated smoothly over past four decades, characterized by a high degree of transparency and credibility. In times of crisis, the Hong Kong Monetary Authority (HKMA) has demonstrated strong resolve and capability in defending the currency peg. Despite this impeccable track record, de-peg speculations still surface every now and then. Upon careful study of the rationales behind these de-peg debate, we found that the insecurity over the LERS stem from worries over its suitability—specifically, the local authorities' willingness to defend the peg—rather than its sustainability, which pertains to the actual ability to maintain the peg, and in some cases a potential misunderstanding of the underlying mechanism.

The debate over the sustainability of LERS arose from the following concerns. First, increasing economic structural divergence between HK and the US, and the resultant excessive economic adjustment costs; second, depleting fiscal reserves and; third, the diminishing status of US dollar as a global reserve and trading currency. Under these circumstances, importing monetary policy directly from the US became increasingly problematic for HK's economy, as well as its function as a global financial centre. That said, the daunting cost of quitting the peg and the outright lack of better alternatives eventually quelled these de-peg debate.

The operation of LERS and its goals

The Currency Board system mandates that Monetary Base (consisting of certificates of indebtedness, notes and coins in circulation, the aggregate balance, and outstanding Exchange Fund bills and notes) is backed by US dollar assets at the rate of HKD7.8 per USD. Additionally, the HKMA provides Convertibility Undertakings (CUs), under which it commits to selling HKD at 7.75 per USD (strong-side of CU) and buying HKD at 7.85 per USD (weak-side of CU) upon request by banks **(Chart 1)**.

The stability of HKD is maintained via an automatic adjustment mechanism that links capital inflows and outflows to the overall level of liquidity in the banking system, and in turn influences HKD interest rates. When there are capital inflows (or outflows) into HK, triggering strong-side (or weak-side) CU and requiring the HKMA to step in to sell (or buy) the HKD against the USD. As a result, the aggregate balance will then expand, leading to lower HKD interest rates and increases liquidity, which in turn moves the HKD away from the strong side of CU.

The LERS has been pivotal to HK's exchange rate and long-term financial stability, providing a conducive environment for the small and open economy to develop into international financial centre and trading hub. The simple and transparent system help installed market confidence and offered predictability in monetary policy. Furthermore, this currency arrangement also supported HK's role as China's gateway to the world, facilitating trade and capital flows with the rest of the world.

The cost and limitations of LERS

The LERS operates effectively only under a specific set of conditions and comes with considerable limitations and economic implications. First, the central bank is required to hold sufficient foreign exchange reserves to at least cover the entirety

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of narrow money supply. Also, having relinquished monetary policy autonomy, fiscal measures will have to do the heavy lifting in the progress of smoothening out business cycles, which speaks to the importance of fiscal prudence. Added to that, the banking sector will have to be robust and well-capitalised, as it bears the burden of adjustments. Any shortcomings in this regard can impede the process of interest rate convergence and interest rate arbitrage.

Economic adjustment in times of exogenous shock will have to come in forms of wage and asset price adjustments, which can be excruciatingly slow and painful. In cases of high price rigidity, the real economy may also have to undergo structural and durable adjustments. From 1997 to 2003, HK's economy was hit by Asian financial crisis and SARS epidemic, leading to a prolonged period of asset deflation, with residential property prices falling by a cumulative 66%. Nonetheless, this is in line with the design and expectation of the LERS, and any undesirable consequences of such system should be managed by macro-prudential tools and fiscal measures.

Chart 1: Spot USDHKD trading within the currency band

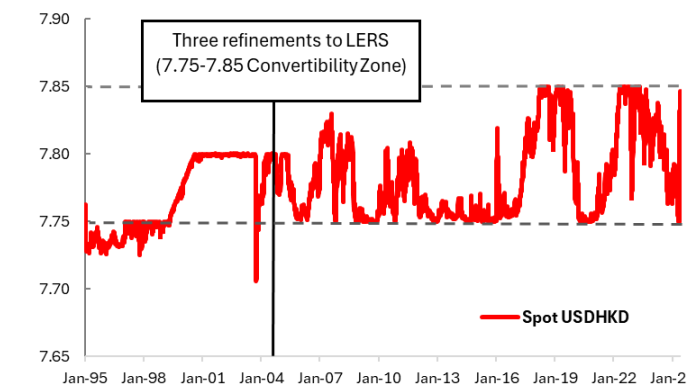
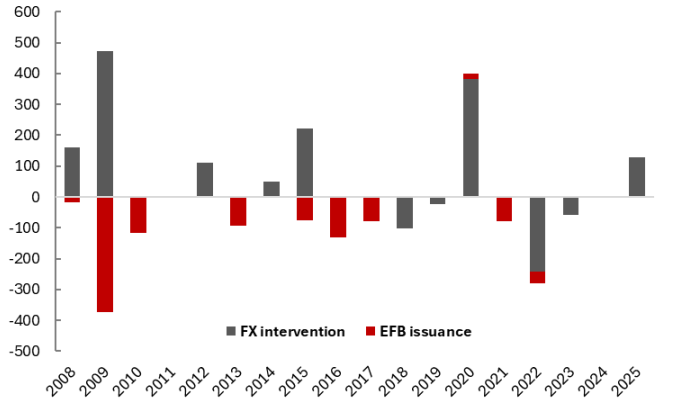


Chart 2: Change in aggregate balance



Debunking the myth of aggregate balance

It is important to clarify that some speculators have mistakenly equated the aggregate balance with the HKMA's foreign reserves, thereby misjudging the authorities' capacity to defend the peg. The aggregate balance is a clearing account commercial banks kept with the HKMA, for settling interbank payments and payments between banks and the HKMA. It is part of the monetary base and serve as a common indicator for gauging interbank liquidity. The HKMA can influence aggregate balance via three mechanisms: conducting FX intervention, Discount Window activities or by issuance of exchange fund bills (EFBs) **(Chart 2)**. Movements in aggregate balance have been fairly sporadic in the past, upon issuance of exchange fund bills or triggering of strong-side/ weak-side CUs. In the absence of these, aggregate balance barely moves except for some adjustments in interest payment on EFBs and Discount Window activities. Importantly, even if the aggregate balance were to drop to zero, it would not impact the operation of the LERS or the daily operations of commercial banks.

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Is the peg still safe?

To back HKD-USD peg and fend off speculation, the Exchange Fund holds USD408.7 billion foreign reserve as of April 2025 **(Chart 3)**, approximately five times the HKD currency in circulation, 1.6 times the monetary base and 36% of broad money supply M3. On the other hand, the HKMA is also required to maintain a backing portfolio within the Exchange Fund at 105-112.5% to the monetary base, known as the backing ratio. The backing portfolio ensures that the monetary base is fully backed by high-quality, highly liquid USD-denominated assets. As of end-April 2025, the backing ratio stood at 110.6%.

With the abundant foreign reserve, HK is more than capable to maintain its peg. Speculators have not amounted to any meaningful attack against the peg since the 1997-98 crisis period. In 1998, there was a net outflow of financial non-reserve assets of HKD65.6 billion (5.2% of GDP; 34% of the monetary base). Applying these ratios to 2024 nominal GDP (at HKD3.18 trillion) and end-May 2025 monetary base (HKD2.12 trillion) suggests a potential net outflow of between HKD165-722 billion – well covered by the official FX reserves at USD408.7 billion (HKD3.19 trillion) and the Exchange Fund's currency board account backing assets at HKD2.19 trillion as of end- April 2025.

The real question to consider

Under the LERS, HKD interest rates generally tracked the movements of their US counterparts **(Chart 4)**, despite being in different stages of business cycles. In the aftermath of 2008 global financial crisis, HK was forced to engage in quantitative easing and keep interest rate at zero, even when inflation reached as high as 5%. Currently, HK must endure the relatively high interest rates prescribed by the Federal Reserve, while the economy was trying to regain footing and inflationary pressure stayed subdued. The widening mismatch of economic fundamentals and interest rate levels — due to persistent desynchronisation of economic cycles between the US and HK, raises question on the appropriateness of the LERS.

However, given that the USD remained as the dominant reserve (58% of global FX reserves at of end-2024), financing and trading currency (60% international and foreign currency claims and liabilities), the peg continues to facilitate HK's function as an international financial centre, and Mainland China's gateway to the rest of the world. Therefore, when assessing the appropriateness of the LERS, the real question that needs to be considered is which is more important - to enable interest rate policy to achieve price stability and smoothen business cycles, or to serve the need of an international financial centre while maintaining financial and exchange rate stability.

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Chart 3: Foreign reserves and monetary base

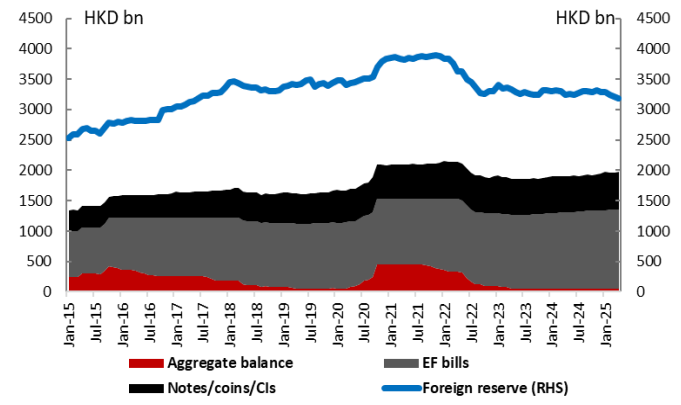
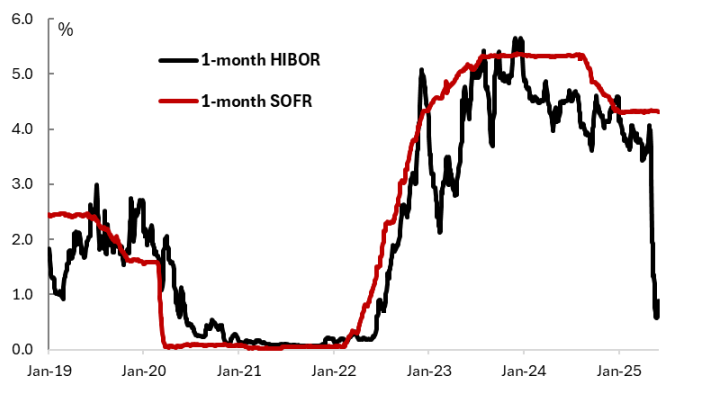


Chart 4: HKD rates tracked USD rates



Mitigating Economic Pain

While the societal consensus was that the latter is more important, the economic cost of adjustment was still deemed excessive, seeing the painful asset price correction and substantial drawdown of fiscal reserves in the past few years as the fiscal reserve has fallen by 47.5% from recent high at HKD1,211bn to HKD635 bn as of end-April 2025. The good news was that there are ongoing efforts to mitigate the economic cost due to the rigidity of currency board system, without having to change the HKD peg.

For one, the HK government had gradually increased the government bond issuance, to finance large infrastructure projects and manage the fiscal pressure. Most recently, the government offered 30-year multicurrency bonds, which had been well received by the market. This provides authorities with the ammunition to implement counter-cyclical measures, while enlarging the pool of investment tools and attracting capital inflows. Furthermore, there are also supports from central government of Mainland China, with the PBoC's governor Pan opting to increase allocation of foreign reserves to HK assets. These could lead into structural inflows and help keep the HKD interest rates low. Lastly, the economy is actively seeking productivity gains through AI adoption and innovation and technology development to align with US productivity growth.

Understanding the recent dynamic

The recent dynamic of spot USDHKD and HKD rates is perfect illustration of the LERS in action. As the spot USDHKD touched the strong-side CU in early May, the HKMA engaged in FX intervention and bought a total of HKD129.4bn. Correspondingly, aggregate balance rose to HKD174bn from HKD44.6bn before HKMA FX intervention, while HKD rates and forward points slid in the presence of flush HKD liquidity. In days following the FX intervention, the spot USDHKD staged an uninterrupted rally, from 7.75 to the upper bound of currency band at 7.85.

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At the moment, the USDHKD forward outright is trading below 7.75, outside of the currency band at 7.75-7.85. This however does not mean that the market is pricing in a de-peg scenario, but rather it reflects the HKD-USD interest rate differential (i.e. 12-month HKD IRS-USD OIS spread) **(Chart 5)**. To gauge market's expectation on future trajectory of spot USDHKD pair, we also take a look at the USDHKD option market pricing, in particular the three-month risk reversal (difference between implied volatility of similar call and put option) **(Chart 6)**. With the risk reversal value at deeply negative zone, it shows that market is pricing in a stronger HKD in the future.

Chart 5: Option pricing showed bullish HKD view

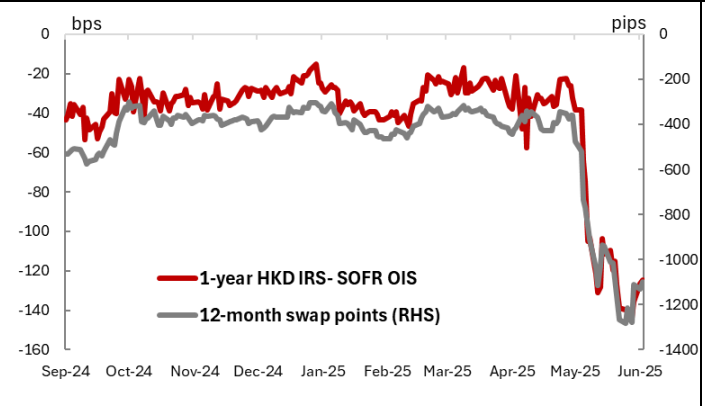
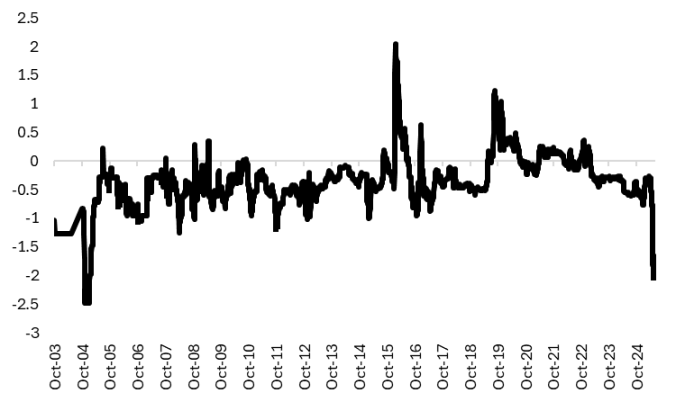


Chart 6: Option pricing showed bullish HKD view



Source: Bloomberg, HKMA, OCBC

Exploring other peg options

While we acknowledge the flaws and limitations of the current system, there is no other peg option that clearly suits HK better and hence justifies the cost of quitting the peg. Although pegging to a basket of currencies would have some clear advantage of less rigidity, it has the disadvantage of being less transparent, more complex and creating uncertainties for monetary policy. A RMB peg also entails an array of technical obstacles, such as capital controls, convertibility issues, and the lack of offshore RMB denominated assets. Not to mention that RMB has yet to compete with the USD for the status as a global reserve and trading currency. Moreover, Mainland China's monetary policies often serve the domestic agenda, which sometimes with little relevance to the HK economy.

Under the current set of circumstances, changes to the HKD peg do not appear to be in HK's best interest. Even minor adjustments to the LERS, such as widening the convertibility zone, can invite considerable market speculations and potentially undermine the credibility of the system. We continue to see strong resolve and capability from local authorities to maintain the LERS, even at the cost of economic pain. That said, circumstances can change, and LERS is not a one-size-fit-all exchange rate regime. As pointed out by the former HKMA Chief Joseph Yam, the legal, monetary and technical framework are there to support change, if change is considered desirable. But until then, the LERS remains the go-to option for HK.

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What are the alternatives to US Treasury Securities?

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Assisted by Miki Tan Wei Xi

- There has been gradual diversification of reserves – mostly away from the USD – by central banks over the years or decades. While reserves and private fund allocations are across asset classes, this report focuses on government bonds.
- As alternatives to USTs, investors look for government bonds that are relatively high-rated, or of significant outstanding amounts, or both.
- Under the criteria we set for ratings and sizes, our list includes the government bonds in the markets of Australia, Canada, Germany, Netherlands, Singapore, South Korea, France, UK, China and Japan. If we loosen slightly the criteria, then this list can be expanded to cover the markets of Spain, Belgium, Austria, Poland, and Malaysia. This list is not meant to suggest any relative value opportunities.

Re-allocation from USD assets

One of the key themes dominating the market across asset classes this year has been re-allocation away from USD assets. To be clear, there has been gradual diversification of reserves – mostly away from the USD – by central banks over the years or decades, as revealed by IMF's COFER (Currency Composition of Official Foreign Exchange Reserves). The percentage share of allocated reserves to the USD peaked at 72.7% at end 2Q01 and the share has since embarked on a mostly downward trend, with some interim pick-up in the 2015/2016 period. The USD's percentage share in allocated reserves was last at 57.8% at end-2024. The EUR's latest share at 19.8% was also below its peak of 28.3% at end 3Q09. The JPY's share rebounded from the trough of 2.79% to the latest 5.82% but was still short of its peak of 4.98%. Zooming into the more "recent" history over the past decade (end-2014 to end-2024), those which gained shares included the JPY, CNY, CAD, GBP, AUD, together with "others" – this "others" category included KRW, SEK and SGD etc. as per data at end-2020.

While reserves and private fund allocations are across asset classes, this report focuses on government bonds – mainly taking stock of available government bonds of higher or comparable credit ratings to US Treasury securities. According to US TIC (Treasury International Capital) data, foreign holdings of US Treasury securities (bills, notes and bonds) have been falling as a percentage share of total outstanding (amounts held have been mostly rising), to around 25% as of end 1Q25, from around 34% at end-2014. Within foreign holdings, holdings by the official sector (presumably mostly central banks) fell in shares, while the private sector took up the slack. In other words, some of the demand for USTs has been shifted to investors who are likely more price sensitive. Within the foreign holdings of USTs, Japan is the biggest holder, followed by UK and China with similar amounts held.

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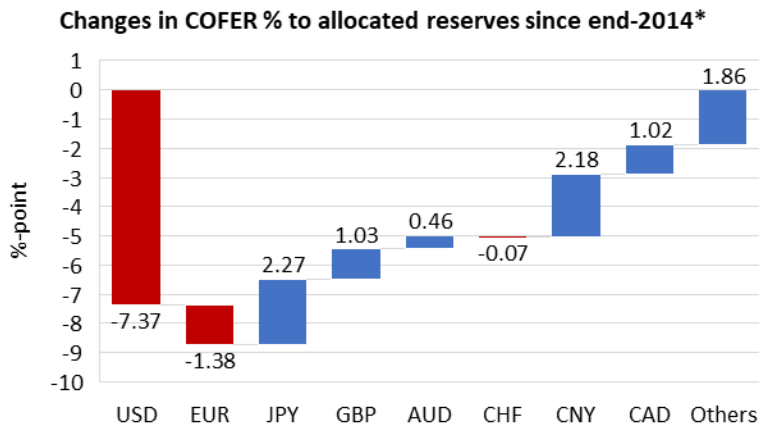
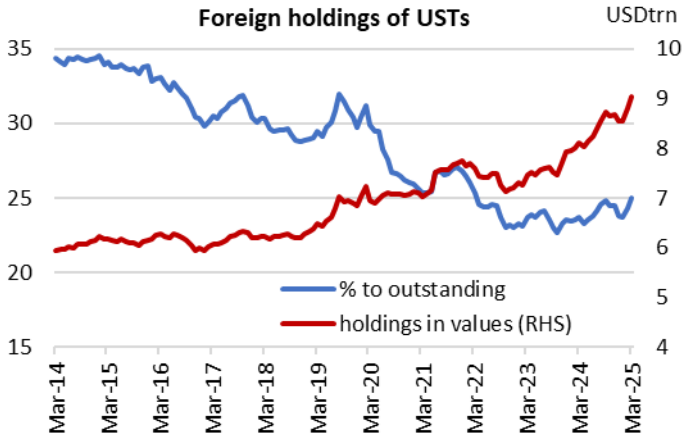
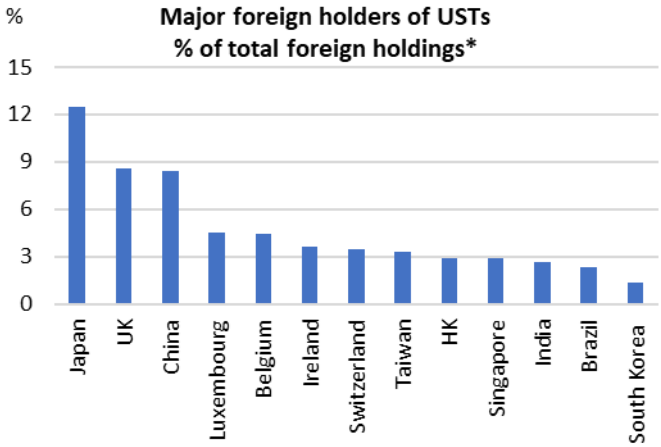


Source: Bloomberg (on IMF data), OCBC Research
*as of end-2024





Source: Bloomberg (on US TIC data), OCBC Research
*as of end Q1-2025

Outstanding government bonds in major markets

As investors diversify away from USTs, they will be in search for alternative government bonds. Viable government bonds presumably are relatively high-rated, or of significant outstanding amounts, or both. Major AAA-rated government bonds[27], which is one notch above the rating for the US, include ACGBs (Australia), Bunds (Germany), CAN (Canada), NETHER (Netherlands), and SGS (Singapore)[28]. Among these, outstanding amounts of Bunds and CAN are relatively big, followed by ACGBs. According to BIS, as of 3Q24, outstanding Bunds stood at USD2.6trn equivalent, outstanding CAN was at USD1.9trn equivalent, and outstanding ACGBs was at USD0.64trn equivalent. Each of these individual markets are still dwarfed by the size of the UST market.

Going down the sovereign credit curve by one or two notches (i.e. AA+/Aa1 or AA/Aa2), there are some more choices of government bonds. These include those in the markets of Austria, Belgium, South Korea, UK, among others. Within these

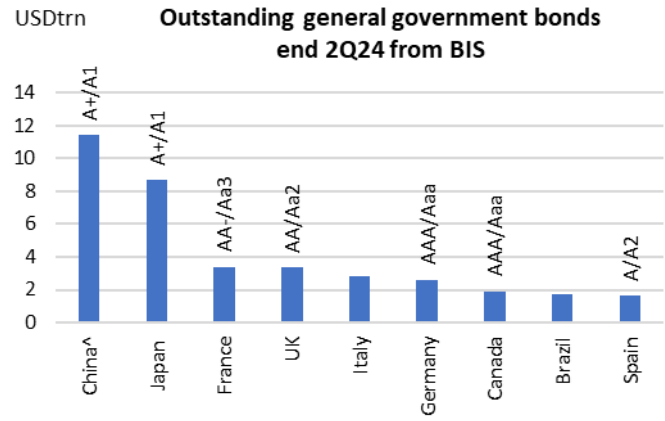
[27] Local currency rating; rated AAA by at least one of the three credit rating agencies – Moody's, S&P and Fitch.
[28] Non-exhaustive list

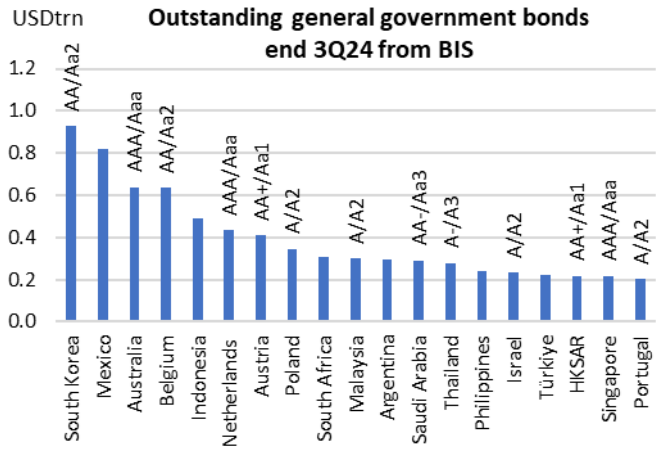
levels of ratings, government bonds in UK and South Korea stand out in terms of outstanding amounts.

Apart from sovereign credit ratings, some markets because of their sizes cannot be ignored given the supply of fixed income investment products. The UST market is by far the biggest government bond market. After USTs, biggest government bond markets are JGBs (Japan), CGBs (China), OATs (France) and Gilts (UK). Both JGBs and CGBs are rated at A+/A1, OATs are rated higher at AA-/Aa3, and Gilts are yet higher at AA/AA-/Aa3.

As a first attempt to look at potential investment alternative to USTs, our list of selection includes i) government bonds which are AAA-rated (top notch) and of size of at least USD200bn as per BIS data for Q3-2024, ii) government bonds which are rated A+/A1 and above (top 5 notches) and of sizes of at least USD800bn equivalent. These criteria try to include more AAA-rated bonds and not ignore big markets if their ratings are also relatively high. The list then includes the government bonds in Australia, Canada, Germany, Netherlands, Singapore, South Korea, France, UK, China and Japan.

If we loosen criterion ii) to include government bonds with ratings of A-/A3 or above, and with outstanding amounts of USD300bn or above, then the list will be expanded to cover the markets of Spain, Belgium, Austria, Poland, and Malaysia.





Source: BIS, OCBC Research

^BIS statistics appear to have included China Local Government Bonds (LGB); central government CGB (China Government Bond) outstanding was at around USD4.66trn as of end 3Q24.

Note: The chart indicates credit ratings for those government bonds with a rating of A-/A3 or above from at least one credit rating agency, and with above USD200bn outstanding amounts at end 3Q24 as per BIS statistics.

Yield levels and bond/swap spreads versus credit rating

Asset swap pick-up (fully hedged against FX risk when investing in a "local currency" market) is commonly used to compare yields in bond investment across markets. For example, from a USD-funded investor perspective, one usually looks at the yield spread above SOFR if the investor is to swap USD into the local currency in a way that the currency risk is hedged. However, under the grand scheme of diversification away from USD and USD assets, we focus on local currency yields here.

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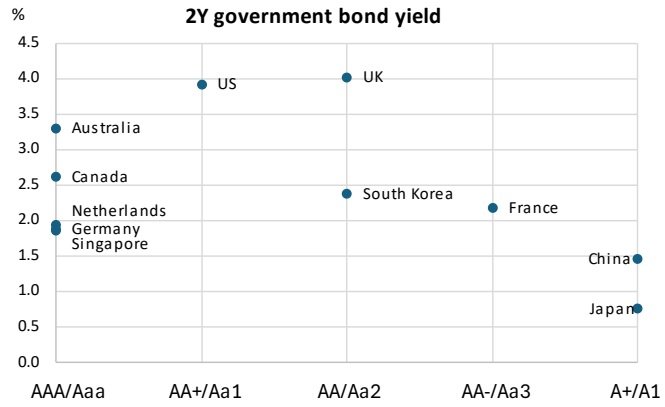
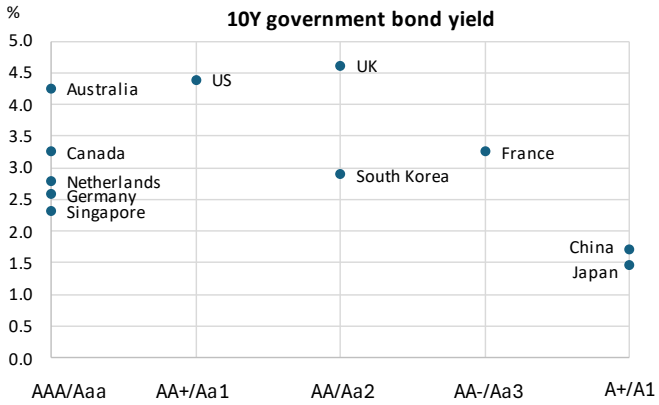
If we simply plot government bond yields (in local currency terms, not being translated into USD yield equivalent) against the respective credit ratings, then ACGBs and CANs appears to provide relatively high yields given their ratings, while CGBs and JGBs yields appear on the low side. Meanwhile, fiscal concerns in the US appear to have been partly compensated for by the high UST yields against its credit rating – or market perceived the rating to be lower than the current rating.

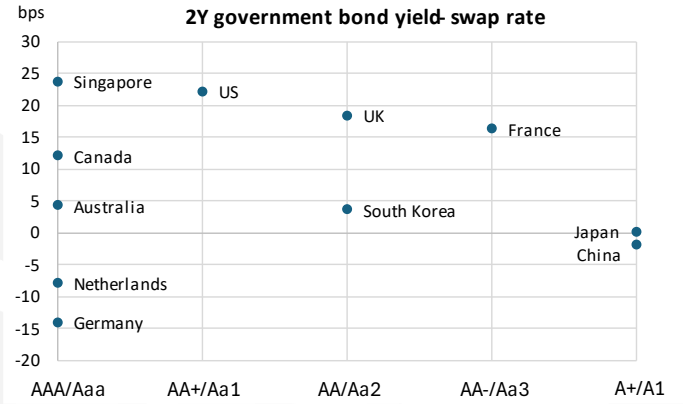


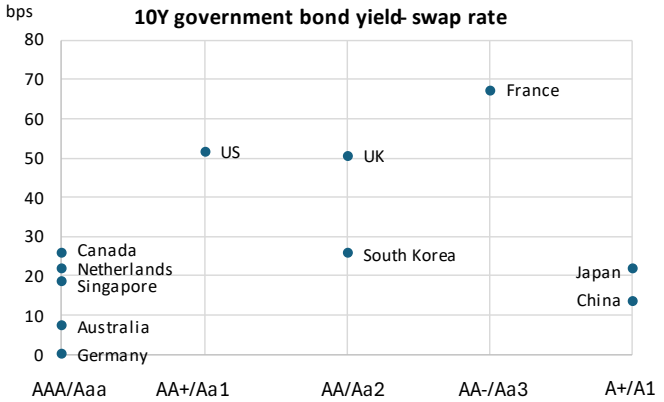


Source: Bloomberg, OCBC Research
Data on 5 June 2025

Local currency yield levels are affected to a large extent by domestic factors including the local currency liquidity situation, domestic investor demand, comparison to returns of other local currency assets etc. We next compare bond/swap spreads, which take into account local funding costs. For illustration purpose, the bond/swap spreads we use here are calculated as government bond yields minus swap rates. In terms of bond/swap spreads, short-end SGS, short-end CAN, long-end OATs, USTs and Gilts appear to be relatively wide against their respective credit rating. All these comparisons are before taxes and any other regulatory or transaction related costs.

These charts aim to provide an overview on yield and bond/swap spreads versus credit ratings. When investing in the respective bond market, bond supply/demand matrix and outlook, domestic macro environment, regulations, applicable taxes and capital requirement, among others, are factors to be considered.



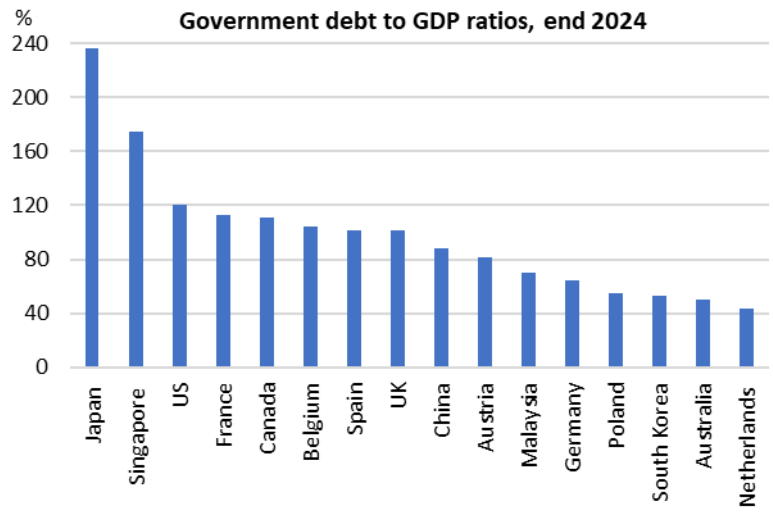


Source: Bloomberg, OCBC Research
Data on 5 June 2025

Thematic Report 7

Government debt to GDP ratios

While credit ratings presumably have incorporated a set of relevant indicators including government finances and debt levels, the current focus on US's debt sustainability is arguably one of the triggers for this thesis of diversification. Hence, we single out government debt to GDP ratios for comparison. Fiscal burden is not confined to the US but is present in many developed markets. For the ten markets under our list, we leave out Singapore for comparison, as Singapore has a distinct feature in that most of the government borrowings are not used to fund Singapore Government's expenditure but instead most issuances of SGS are for market development (to set up a benchmark yield curve). For the remaining nine markets on our list, Japan has the highest government debt to GDP ratio at above 230%. Next come France and Canada, which have government debt to GDP ratios that are not far away from that of the US. The rest have government debt to GDP ratios of around 100% or below 100%, which compare favourably with the US.



Source: IMF World Economic Outlook April 2025, OCBC Research

Asian government bond markets

CGBs, KTBs and SGS in Asian markets are on our list of viable alternatives, and MGS as well in our expanded list. According to IMF COFER data, 2.18% of allocated reserves was in CNY assets at end-2024. While there is no readily available time series breakdown for KRW and SGD, according to an IMF working paper[29] citing data at end-2020, KRW and SGD were among the "others" category for allocated reserves.

We see **SGS** (Singapore Government Securities) as standing out to benefit from diversion of flows including those away from the USD. Besides being AAA-rated, the Singapore Government operates a fiscally prudent and balanced budget policy and most of the government's borrowings are not used to fund its expenditure. This arrangement allows flexibility in the calibration of SGS auction sizes in reaction to prevailing market conditions. As such, the bond supply outlook tends to be

[29] "*The Stealth Erosion of Dollar Dominance: Active Diversifiers and the Rise of Nontraditional Reserve Currencies*", March 2022, IMF Working Papers WP/22/58

supportive of the domestic market. As at end May 2025, outstanding SGS amount to SGD298.9bn (circa. USD232bn), comprising SGD183.3bn of bonds and SGD115.6bn of bills. SGS have been FTSE WGBI since 2005 and the most recent weight of SGS in the index was about 0.4%.

In onshore China, excluding Local Government Bonds (LGBs), outstanding **CGBs** (China Government Bonds) stood at CNY35.57trn at end April 2025, or around USD4.9trn. Foreign holdings of CGBs as a % of outstanding has been largely edging down since it peaked at 11.14% in January 2022, and the share was last at 5.92% at end April 2025. CGBs were included in Bloomberg-Barclays Bond index in April 2019, and in FTSE Russell's WGBI in November 2021 with full weight reached in October 2024. After Korea's inclusion, weight for China is estimated at 10.0%. Cumulative flows into onshore CGBs since April 2019 was negative. Funds are probably underweight CGBs and there is potential for catch-up.

KTBs (Korea Treasury Bonds) will be included into FTSE Russell's WGBI starting April 2026 and the inclusion will be completed (reach full weight which is estimated at 2.05%) by November 2026. Depending on AUM assumption, cumulative passive inflows are estimated at USD40-50bn. Apart from KTBs, there are MBS (Monetary Stabilization Bonds) and NHBs (National Housing Bonds) in the KRW market.

MGS (Malaysia Government Securities) are also in FTSE Russell's WGBI with a weight of around 0.45%. Apart from the conventional Malaysia Government Securities, there are also the Islamic MGII (Malaysia Government Investment Issues). Outstanding MGS stood at MYR645.1bn and outstanding MGII at MYR604.8bn at end April 2025. MGS+MGII received inflows of MYR14.3bn during May 2025, the third monthly inflows in a row.

If concerns over US fiscal and debt positions linger, then the gradual diversification away from the USD and USTs is likely to continue. Selected Asian government bond markets are well positioned to benefit from inflows.

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