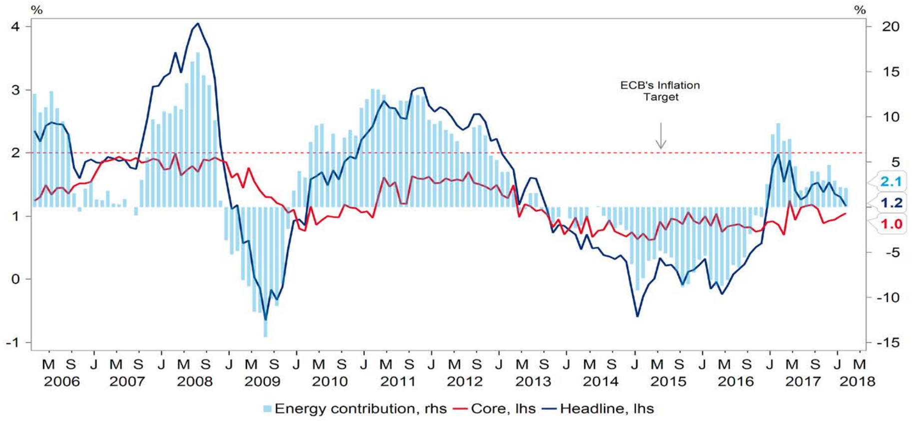
EUROZONE

FX & Rates	2Q18F	3Q18F	4Q18F	1Q19F
EUR/USD	1.25	1.27	1.29	1.29
EUR Refinancing Rate	0.00	0.00	0.00	0.00

Economic Indicators	2016	2017	2018F	2019F
GDP	1.8	2.3	2.3	1.9
CPI (average, y/y %)	0.2	1.5	1.5	1.6
Unemployment rate (%)	10.0	9.1	8.4	8.0
Current account (% of GDP)	3.3	3.1	3.1	3.0
Fiscal balance (% of GDP)	-1.5	-1.2	-1.0	-0.9

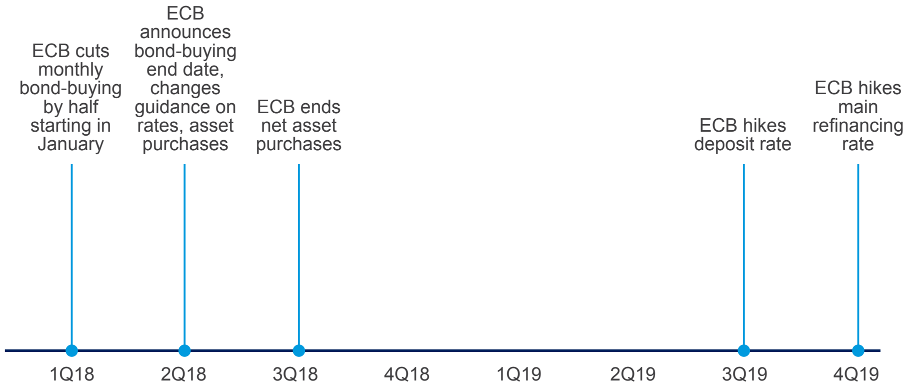
Eurozone Inflation At Weakest Level Since 2016

Source: Macrobond, UOB Global Economic Economics & Markets Research



Likely Exit Path By The ECB

Source: UOB Global Economic Economics & Markets Research



Economy Poised To Remain Positive

Seasonally adjusted GDP in the Eurozone rose by 0.6 q/q in the fourth quarter of 2017, compared to a revised 0.7% in the third quarter. Compared with the same quarter of the previous year, GDP rose by 2.7% in the fourth quarter of 2017, after 2.7% in the previous quarter. Overall, Eurozone growth for 2017 rose by 2.3% – stronger than many advanced markets, like the US and UK. During the fourth quarter of 2017, household final consumption expenditure rose by 0.2%. Gross fixed capital formation increased by 0.9%. Exports rose by 1.9% in the Euro area, whilst imports increased by 1.1%.

For months, the 19-country economy has been one of the bright spots in the global economy, with growth and job creation picking up steam. We think the positive momentum can remain in place, and anticipate a similar growth trend for 2018 – expecting GDP to expand by around 2.3% in 2018, higher than our previous estimate of 1.9%.

At the ECB, the latest economic projections showed growth and inflation broadly similar to the picture of solid economic momentum seen three months ago. Economic growth this year was seen at 2.4% versus an earlier 2.3% forecast. Inflation is seen at 1.4% this year and next year (2019's forecast was revised lower from 1.5% previously).

ECB Carefully Drops Easing Bias

In what ECB President Mario Draghi said was a unanimous decision, the March meeting culminated with the ECB reiterating that asset purchases will continue at the pace of EUR30bn until at least the end of September, but it crucially left out the so-called easing bias that the plan could be increased in "size and/or duration" if the inflation outlook deteriorates. The Governing Council also kept interest rates unchanged and repeated its expectation that borrowing costs will stay at present levels until well past the end of net purchases.

Overall, there is little implication to our view following the latest ECB meeting. The ECB needs to end asset purchases within the next 12-15 months to avoid a bond shortage problem. Yet we see little reason, at this juncture, for the ECB to make more fundamental changes to forward guidance before an announcement on the future of QE is made (likely in June). This should help to prevent a further strengthening of the EUR and "unwarranted tightening of monetary conditions". As for policy rates, we are not anticipating any rate increases until later in 2019.

EUR Outlook: Slow And Steady Appreciation As We Get Nearer To Eventual Stop In Asset Purchases

As a result of the ECB's deft balancing act, EUR/USD was sandwiched for now in-between the near term trading range of 1.22 to 1.25. Downside below 1.22 is firmly supported by strong and improving macroeconomic fundamentals in Eurozone. On the other hand, EUR/USD was prevented from staging a premature rally above 1.25. Overall, as we get nearer to the eventual stop in asset purchase towards the end of the year, we believe that EUR/USD will appreciate slowly from here on, in line with the gradual climb higher in various Eurozone and German bund yields.

It is worth nothing that 5 year German bund yields is now back above zero, from – 50 bps at the start of last year. Similarly, 10 year German bund yields have popped above 50 bps, after range trading around 30 bps for most part of last year. From 1.25 in 2Q18, we see EUR/USD climbing gradually to 1.27 in 3Q18 and 1.29 in 4Q18 and 1Q19. Any strength above 1.30 is unlikely for now, given that the US Federal Reserve is also in the process of monetary policy normalization.