FX Viewpoint

Monday, February 05, 2018

FX forecast refresh

- As we step into February 2018, investors may require a material shift in the current narrative to enable the dollar to pull out of its January 2018 dive. Despite last Friday's NFP numbers and the resultant jolt to dollar weakness, we think the community remains inherently positioned against the greenback (evidenced by CFTC positioning and the respective short term volatility surfaces), it may require a market pricing in a 4th Fed rate hike this year to materially to shakeout (or dent) dollar bearishness.

- As it stands, the market remains convinced that shifting monetary policy dynamics across the G10 central banks (set against a relatively static projected FOMC trajectory) will continue to channel bids into the major currencies at the expense of the dollar. To this end, ECB rhetoric in recent weeks has continued to fuel this scenario.

- Apart from the ECB however, we note that major global central banks (including those in Asia) have sought to dispel and defuse excessively hawkish intentions but thus far, this has largely fallen on deaf ears. **We look to the swath of central bank meetings at the beginning of the month for further cues on this front.**

- It remains to be seen therefore if the dollar can re-establish a meaningful link with aggregate rate differentials, or even the nominal 10y UST yields, both of which have continued to move in favor of the greenback for the past 3 months since November 2017 but ultimately failing miserably to grant the greenback any lasting traction in the same period. In the interim, dollar vulnerability may remain a path of least resistance.

- Meanwhile, outside of dollar space, pure FX carry (G10 as well as Asia) may remain on the back burner (given its disappointing performance in January 2018 and pretty much for 2017), perhaps an indication that investors have yet to commit to the global growth story, focusing instead on dollar vulnerability.

Potential caution in Asia

- For EM/Asia, note that our risk appetite indicator finally retraced back into Risk-Neutral territory in late January after dipping into Risk-On territory in late December 2017. This presents a potential caveat to the recent "Goldilocks' environment in Asia, especially if global/EM equities continue to stumble/consolidate in the coming weeks.

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- Note that actual net **portfolio inflows** in Asia started to taper at the end of January and early February following the initial rush of inflows in the initial weeks of the year. On a similar note, net implied fund flows have also begun to moderate in recent weeks. In aggregate, regional currencies may derive less of a tailwind if net portfolio capital inflows continue to moderate.

- Overall, we think directional risks for Asian FX may be more finely balanced with increasingly greater **room for differentiation**. To this end, idiosyncratic impediments may continue to put the INR and the PHP at a relative disadvantage compared to the likes of the CNY (or CNH) and the THB. Meanwhile, the KRW, TWD, and IDR may remain subject to further portfolio flow volatility.

- With the exception of the RBI and the BSP, **Asian central banks** are by and large still expected to remain on hand to discourage excessive domestic currency appreciation or excessively hawkish policy expectations. Note that in the year to date, only the NEERs of the CNY (CNH), THB, and the MYR have appreciated in response to the broad dollar slide, with the effective exchange rates of the KRW, PHP, INR, IDR, and SGD depreciating instead.

- Overall, if the current weak dollar environment persists into February and risk appetite levels manage to remain sanguine, expect USD-Asia to remain inherently top heavy. However, note that potential negative triggers ranging from a global equity rout (EM equities have stumbled since late January) to an abrupt re-pricing of global inflation risks may continue to accumulate and ultimately temper excessive Asian FX gains.

Renminbi complex

- Renminbi developments may come under greater scrutiny in the coming weeks (Lunar New Year considerations notwithstanding). In recent weeks, the accelerated appreciation (almost taking on convex proportions) of the **CFETS RMB Index** amidst the DXY's decline has resulted in the USD-CNY crashing to settle around the 6.3000 neighborhood. We look for a consolidation zone around 96.50-97.35 to kick in to forestall any untoward appreciation expectations.

SGD prospects

- Elsewhere, SGD appreciation remains constrained by NEER considerations and if the broad dollar continues to decay into February, expect the majors to continue to outperform the SGD (spot and total return basis).

Revised central tendency forecasts (as at 01 Feb 18)

	Spot	Mar-18	Jun-18	Sep-18	Dec-18
USD-JPY	109.51	108.40	109.22	111.06	112.89
EUR-USD	1.2425	1.2528	1.2644	1.2732	1.2821
GBP-USD	1.4237	1.4393	1.4487	1.4596	1.4704
AUD-USD	0.8024	0.8125	0.8213	0.8293	0.8373
NZD-USD	0.7363	0.7428	0.7538	0.7603	0.7668
USD-CAD	1.2306	1.2148	1.2033	1.1933	1.1833
USD-CHF	0.9326	0.9233	0.9167	0.9096	0.9024
USD-SGD	1.3124	1.3073	1.2971	1.2898	1.2824
USD-CNY	6.2983	6.2905	6.2645	6.2551	6.2455
USD-THB	31.349	31.12	30.93	30.74	30.56
USD-IDR	13422	13413	13343	13303	13263
USD-MYR	3.8985	3.8775	3.8333	3.7984	3.7636
USD-KRW	1071.84	1069.00	1053.22	1047.56	1041.89
USD-TWD	29.201	29.080	28.880	28.760	28.640
USD-HKD	7.8208	7.8238	7.8257	7.8275	7.8294
USD-PHP	51.589	51.93	51.68	51.19	50.71
USD-INR	63.69	63.58	62.96	62.68	62.39
EUR-JPY	136.07	135.80	138.10	141.40	144.73
EUR-GBP	0.8727	0.8705	0.8728	0.8723	0.8719
EUR-CHF	1.1588	1.1566	1.1591	1.1581	1.1569
EUR-SGD	1.6307	1.6377	1.6401	1.6422	1.6442
GBP-SGD	1.8685	1.8815	1.8792	1.8825	1.8857
AUD-SGD	1.0531	1.0621	1.0654	1.0697	1.0738
NZD-SGD	0.9663	0.9710	0.9778	0.9807	0.9834
CHF-SGD	1.4072	1.4159	1.4149	1.4180	1.4212
JPY-SG	1.1984	1.2060	1.1876	1.1614	1.1360
SGD-MYR	2.9705	2.9662	2.9552	2.9450	2.9347
SGD-CNY	4.7991	4.8120	4.8295	4.8497	4.8700

Source: OCBC Bank

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