



FX Outlook 2020: Waiting for the global recovery

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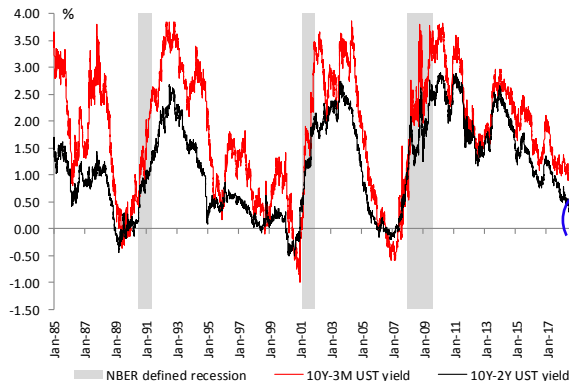
G10 FX Key Themes

- The broad USD has been weighed down **(1) in the near term by reduced tail-end geopolitical risks,** and **(2) structurally by US growth outlook converging lower to the global growth experience.**
- However, **it may be too early to call for a secular weak-USD trend just yet.** The pre-condition for that – a perceptible bottoming and recovery of the global growth outlook – has yet to materialize. Overall, the US macro outlook (albeit diminished in relative terms) is still the most favourable. Elsewhere, Sino-US tensions may be on the retreat, but the volatile nature of the issue should keep investors jittery. These factors continue to provide support for the USD, leaving a flat-to-firmer posture.
- **Thus, we reduce our outright long-USD bias into early 2020, taking a more neutral stance overall and expecting some USD divergence.** With the US macro outlook weaker, reserve currencies may prove to be more resilient against the USD. However, with global growth still anemic, the cyclicals may still underperform. Room for reassessment comes around 2Q to 3Q 2020, where global growth has a better chance of recovering. The USD prospects may turn heavier then, with the extent of USD negativity dependent on the nature of that recovery.

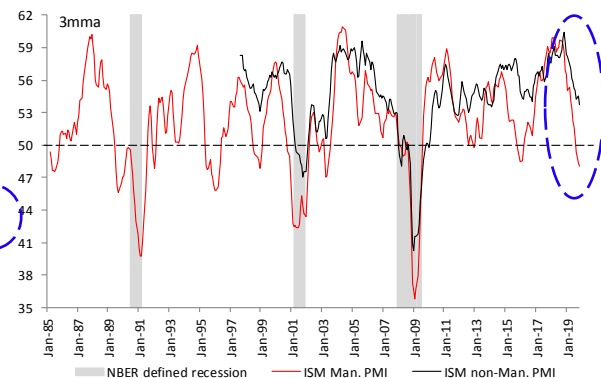
US growth outlook: Softer, but no imminent recession

- Yield curve inversion is not an unfailing indicator for US recessions. Macro indicators definitely highlight a slowdown compared to 2018, but remain at levels consistent with other periods of slowdown within the current expansion cycle. Signs of recession are not imminent.
- Soft US macro outlook less supportive of the USD, but not outright negative.**

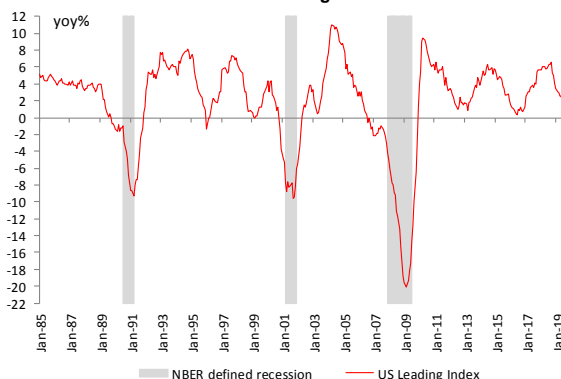
US Treasury yield curve



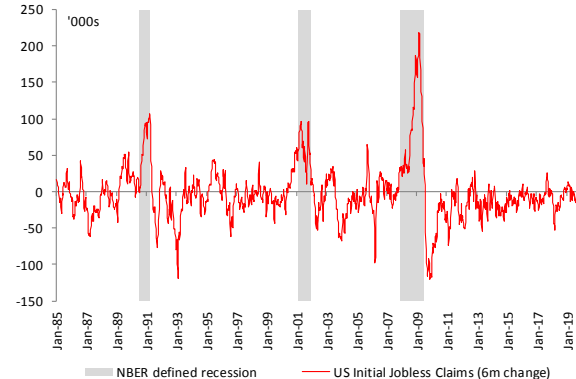
ISM Man. and non-Man PMI Indices



US Leading Index

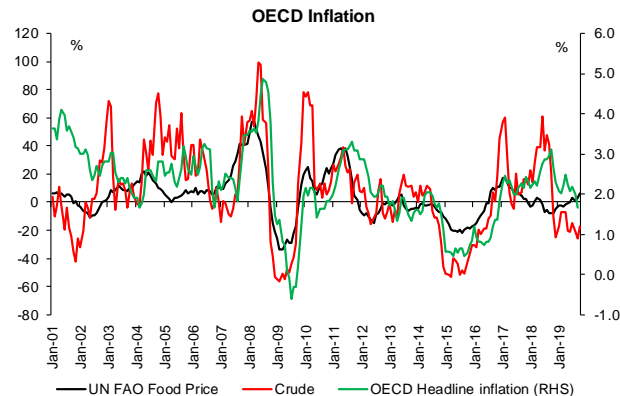
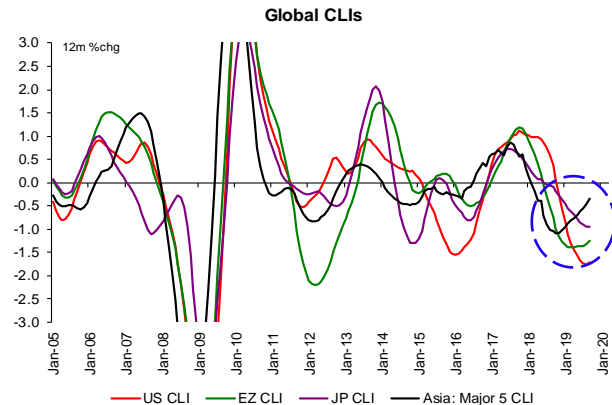
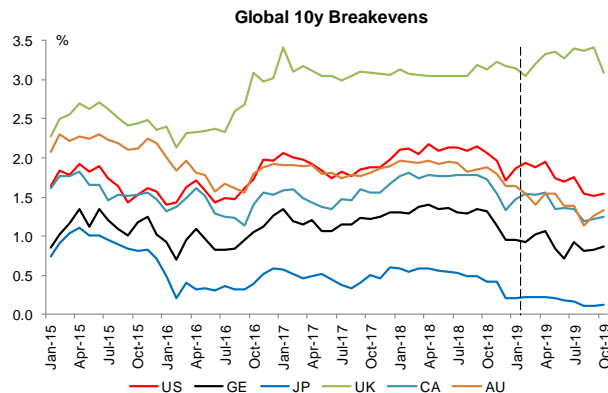
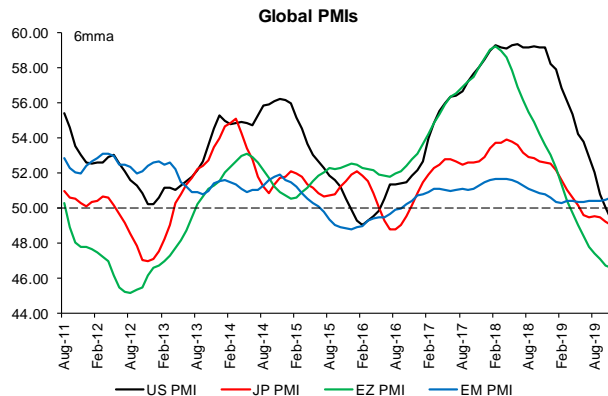


Initial Jobless Claims



Global growth concerns still persist

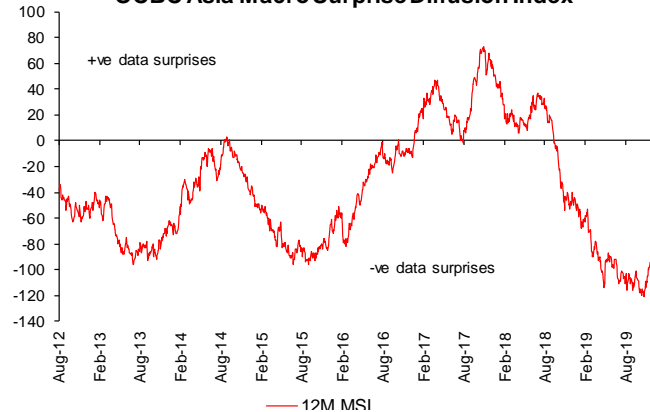
- Global coincident and leading economic indicators still paint a challenging picture. Price pressures continue to be muted, and long-end inflation expectations in developed markets are still depressed.
- Europe and Asia CLIs look to be showing very early signs of stabilization, with Asia more advanced in that regard.**



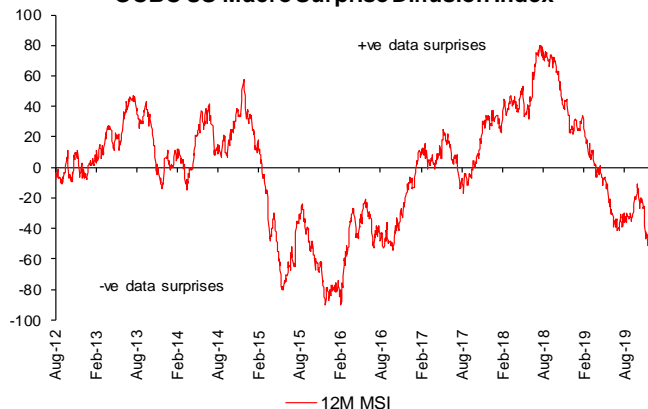
US growth converging lower, but still better

- However, looking across a wide range of higher frequency indicators through our Macro Surprises Index also shows the US holding out better relative to Asia and Europe. Data surprises in the US, on a rolling 12-month basis, is not plunging into depths seen in Asia and Europe.
- Index improvement in Asia and Europe is probably attributable more to downgrade in analyst expectations, rather than an advancement in underlying macro outcomes.

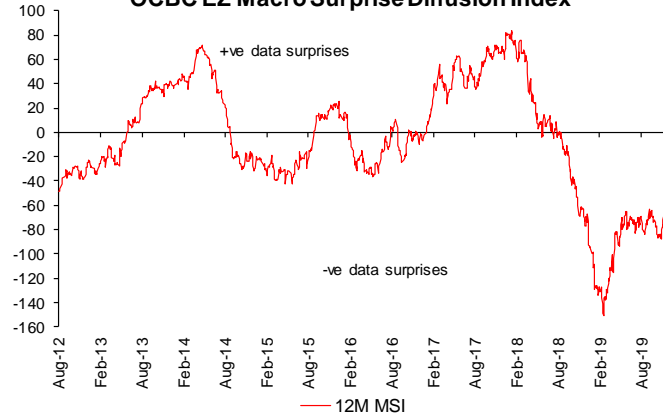
OCBC Asia Macro Surprise Diffusion Index



OCBC US Macro Surprise Diffusion Index

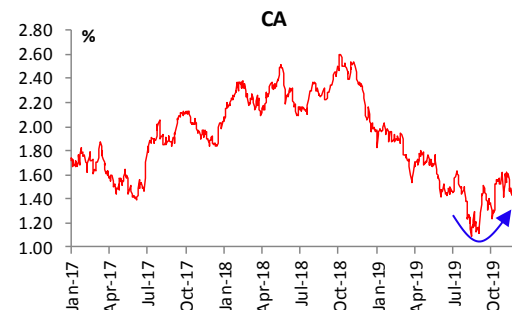
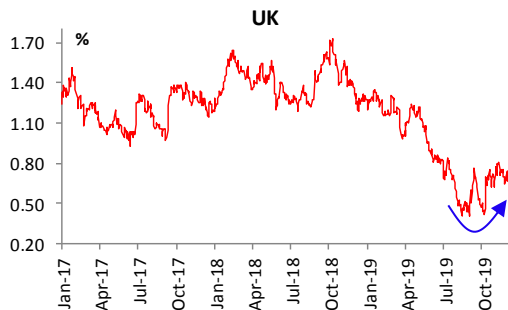
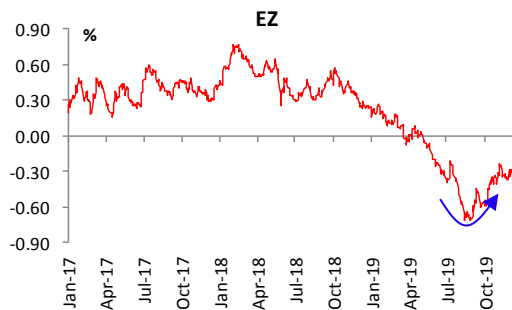
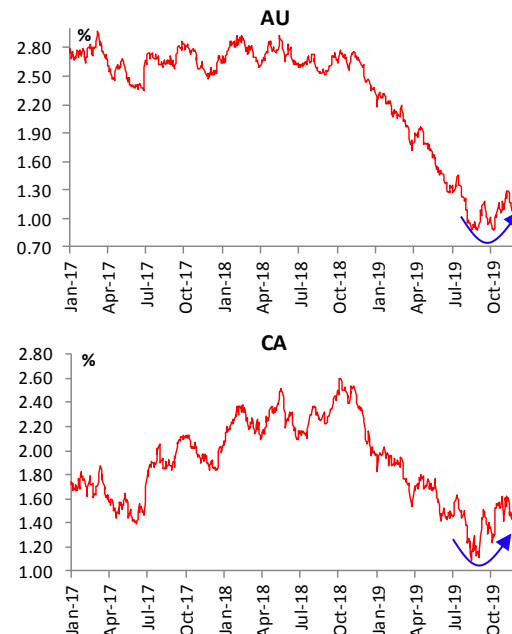
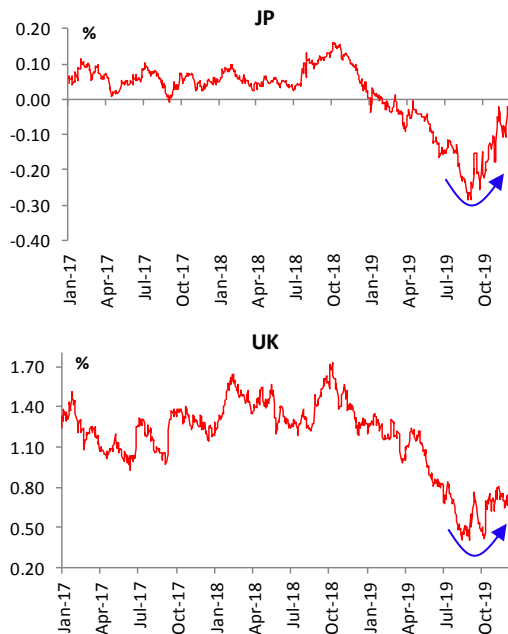
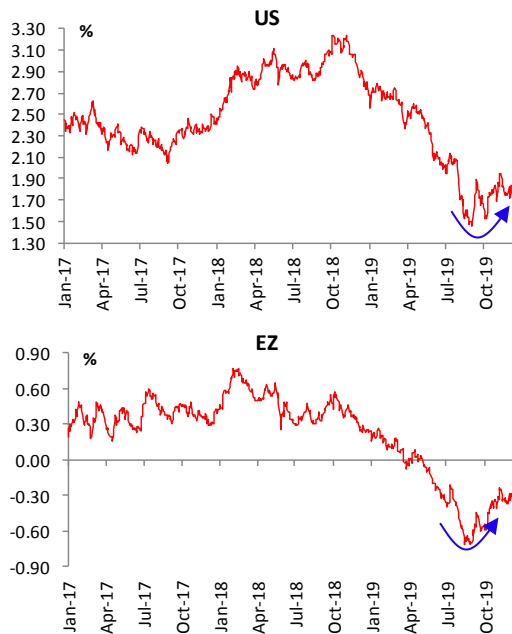


OCBC EZ Macro Surprise Diffusion Index



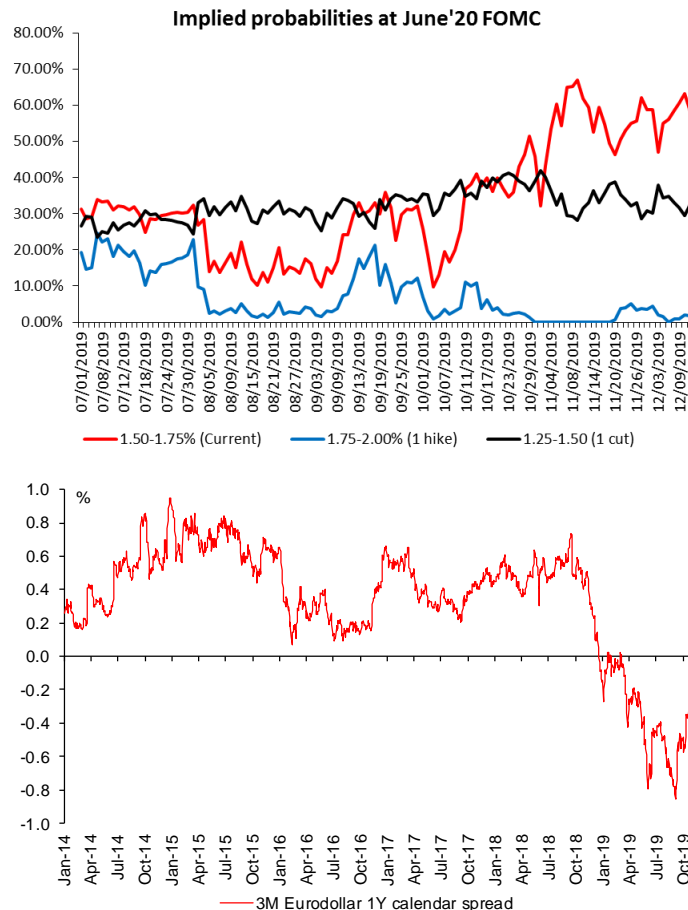
Global core 10y yields still soft...

- ..but note the attempt at bottoming out. Taken together with macro indicators, this suggests that the **macro outlook remains soggy, without strong signs of an imminent rebound. However, further downside macro risks in the near term may be contained.**



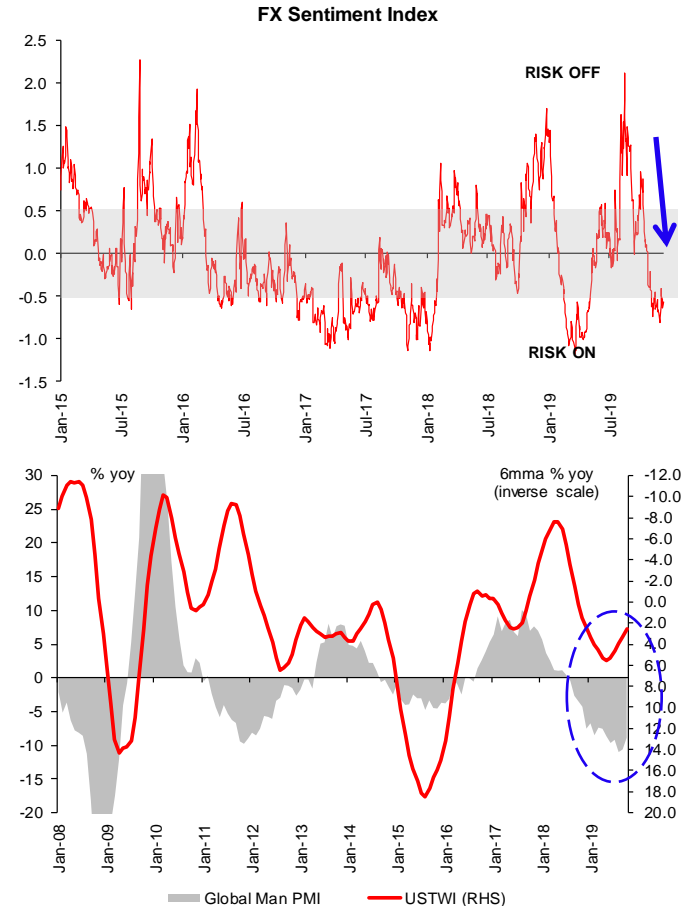
Fed and ECB likely in stasis in 2020

- **Fed** rate cut expectations in 2020 has been pared, although an easing bias still persists. The bar for any shift in Fed policy stance is set high. Most of the policy adjustment at the **ECB** may also have been completed in 3Q19, with attention now expected to shift to fiscal policy for further support. With market expectations very much aligned with the ECB and FOMC, expect market attention to shift away from these central banks for now.
- Meanwhile, expectations at the **RBA**, **RBNZ** and **BOC** may still be undergoing some flux. Expect their respective currencies to be more reactive to central cues.



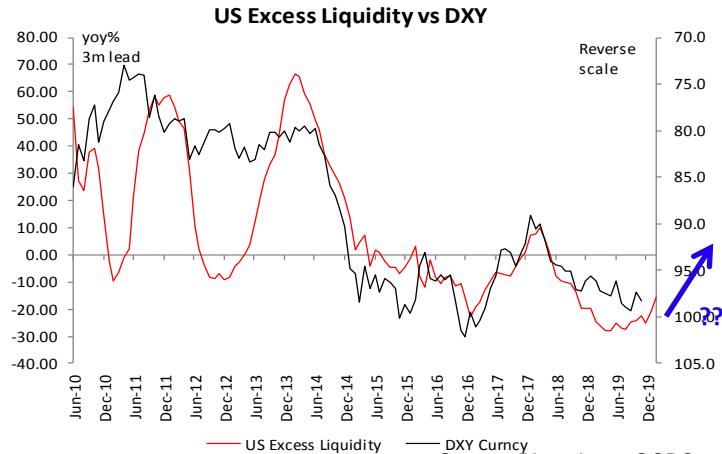
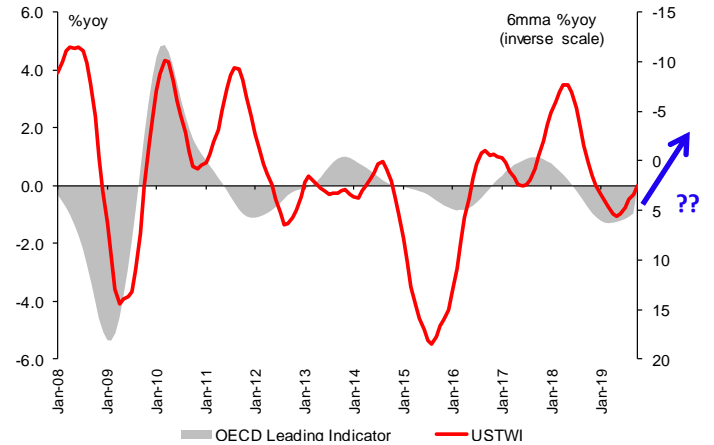
Less in favour of the USD, more divergence (1)

- Near term USD prospects have definitely been impinged by improving risk sentiment and softer US growth. However, the outlook in Europe is arguably still the worst of the lot, while Asia remains suspect. **The thesis that the US/Fed is in a relatively stronger position compared to the rest of the world is weakened, but not invalidated.**
- The current house-view posits USD heaviness coming in around 2Q 2020, as policy support fuels a bottoming of the global growth into 2020. However, the strength of the rebound (if it materializes) will be a big suspect. The late cycle situation that the global economy is currently in would likely preclude a strong V-shaped recovery, in favour of a wide trough. This may impart some implicit heaviness for the USD, but perhaps insufficient to initiate an aggressive multi-month USD down-cycle.



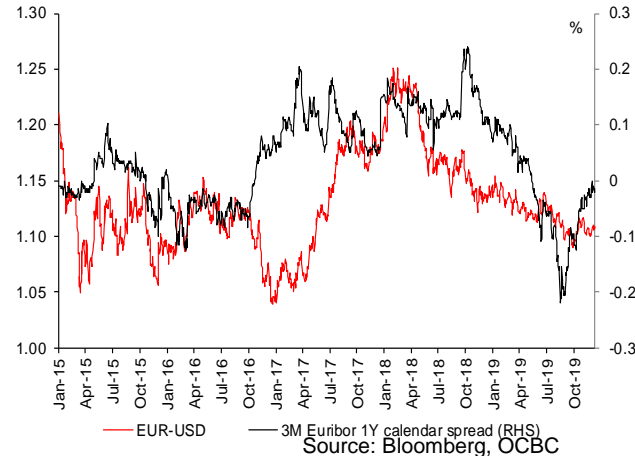
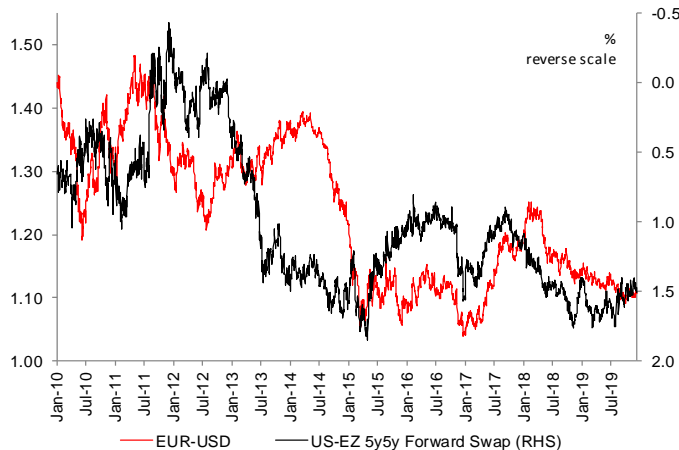
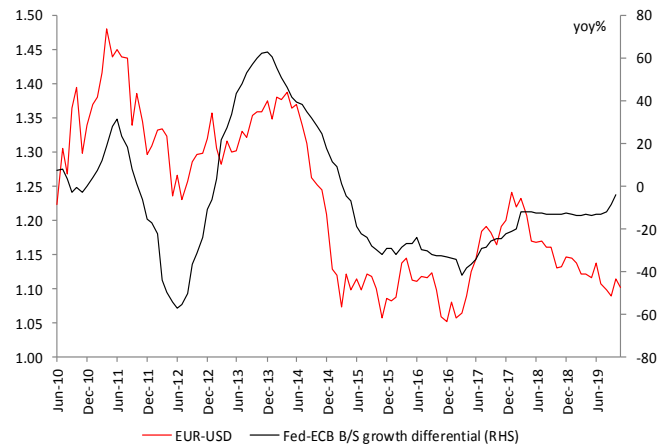
Less in favour of the USD, more divergence (2)

- It follows that **we reduce our long USD bias towards being more neutral, but not to the extent of taking an explicit short USD view.** The likes of EUR and JPY may still see structural downside, but the extent of the downside should be limited by a softening US outlook. Overall positioning is also less defensive, dialing back (but not reversing) our negative view on the cyclicals.
- The main risk to this baseline view is for the growth recovery to arrive sooner and stronger than expected. This would put the USD under stronger pressure earlier in the year. Elsewhere, domestic US issues may also present some concern, the primary of which is the Fed's expansion of repo facility and balance sheet, which may lead to a build-up in excess liquidity in the financial system in 2020, adding negative pressure on the broad USD.



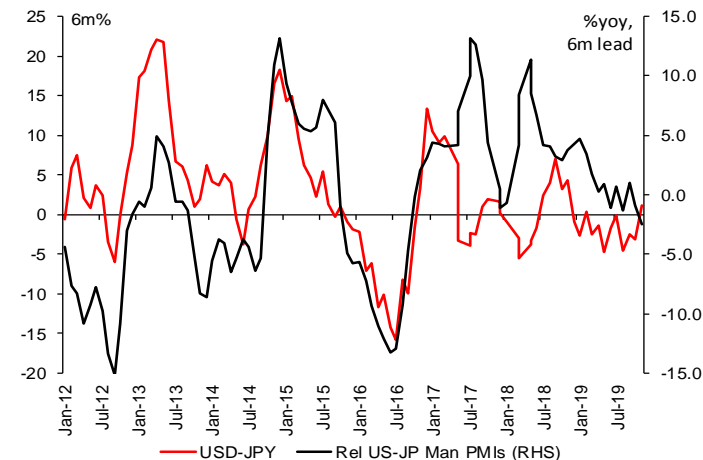
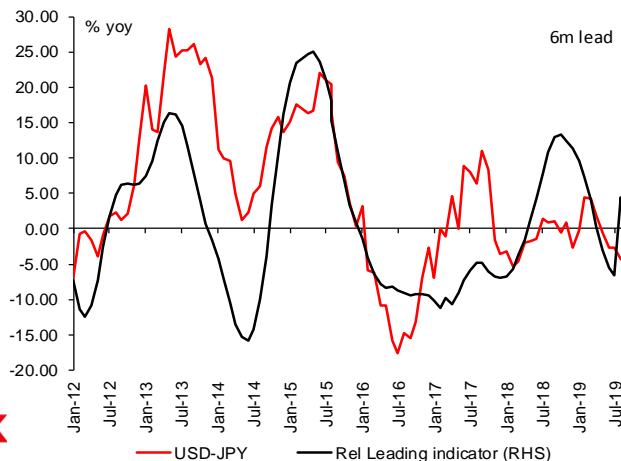
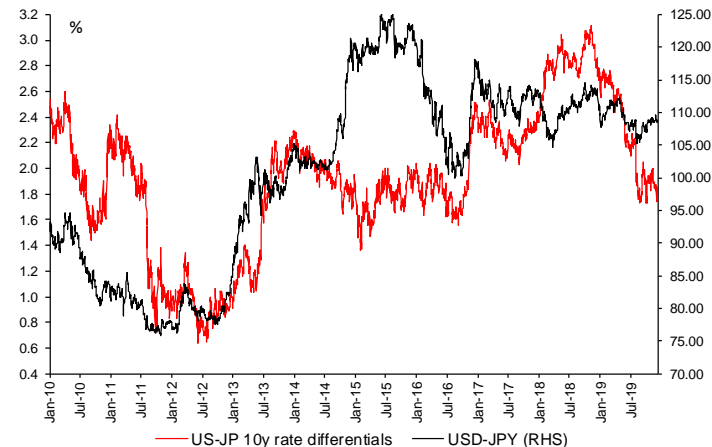
EUR: Disadvantaged by soft EU growth

- Recalibration of relative interest rate expectations, and the outpacing of Fed's balance sheet growth versus the ECB's, may limit excessive EUR downside. However, protracted growth weakness, persistence of downside risks and muted inflationary pressures remain a reality in Eurozone, and preclude a structural strong EUR thesis for now.
- Risk: Shift in policy mix towards greater fiscal support may spur an European growth turnaround faster than expected, alleviating the implicit negativity on the EUR.



JPY: Risk sentiment still the main driver in the near term

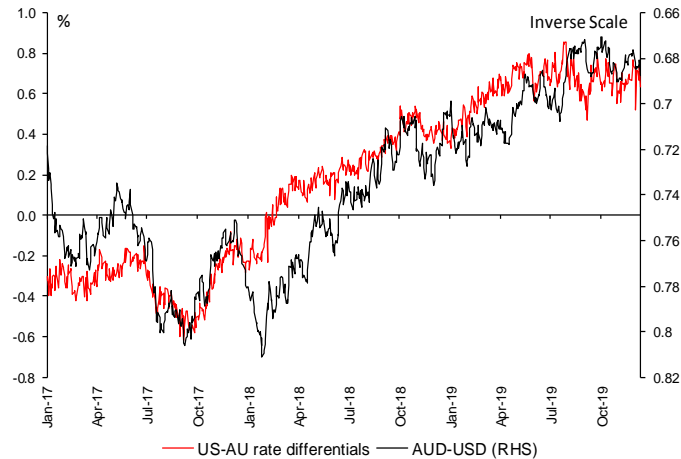
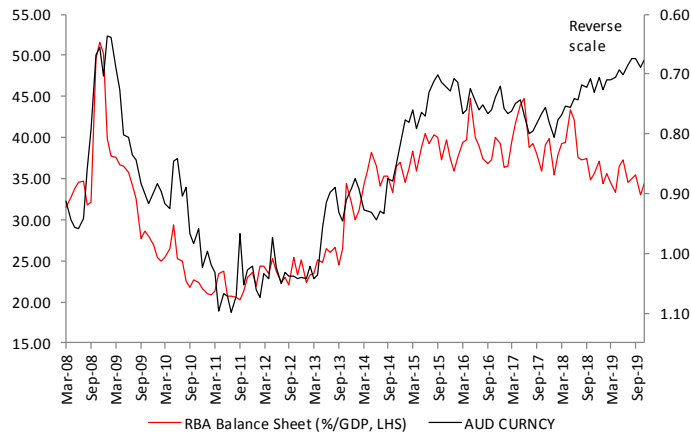
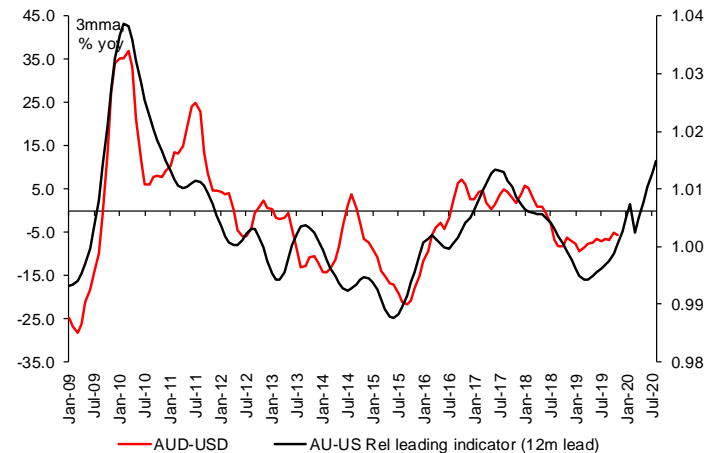
- Near term gyrations should be led by overall risk sentiments and US-JP rate differentials (with correlations strengthening). Sustained ceasefire on the Sino-US front may provide some buoyancy ahead.
- On a longer term perspective, watch **BOJ's** policy cues. Rate cut(s) with yield curve steepening may be supportive of the USD-JPY if it translates into a firmer equity market.



Source: Bloomberg, OECD, OCBC

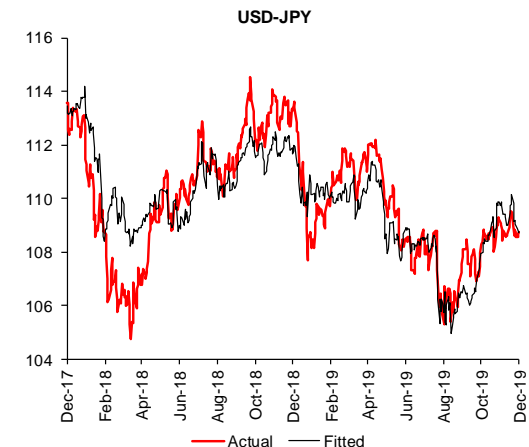
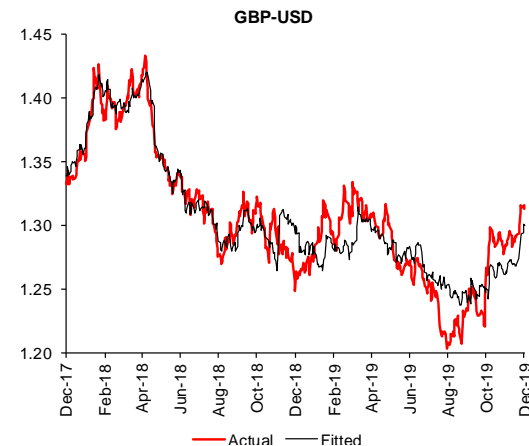
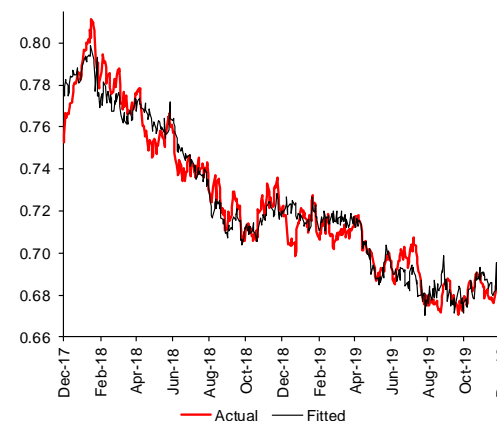
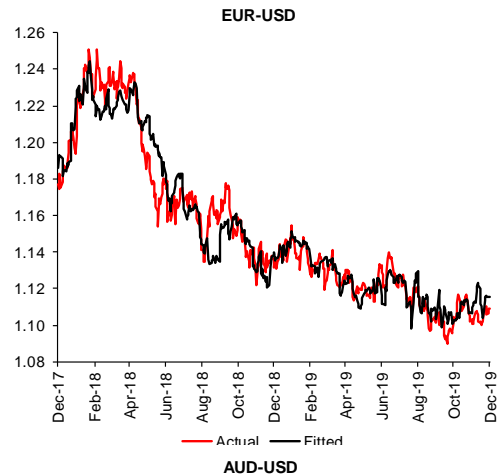
AUD: Dovish arguments fading; RBA's QE wildcard?

- Developments in the short term (positive risk sentiment on Sino-US rapprochement) and the long term (global/Asian growth uptick around 2Q 2020), should limit the downside for the AUD. Thus, we dial back on our AUD-negative bias.
- However, despite **RBA** Governor Lowe's push-back against quantitative easing, the market seems unable to shake off rate cut (1H 2020) and QE (late 2020 / early 2021) expectations. This jars against the pause at Fed/ECB, and may impart structural negativity on the AUD.



G10 summary

- Our short term implied valuation models show inclinations for a consolidation of USD prospects, but not outright USD weakness. **Overall, we think USD positivity may be curtailed in the near term, but not flip to USD weakness just yet.**
- Against the backdrop of positive risk appetite, expect the **AUD** to stay relatively resilient for now, while the **JPY** see negative pressure. The **EUR** should also retain a heavy stance beyond the immediate horizon on the back of ongoing macro weakness.

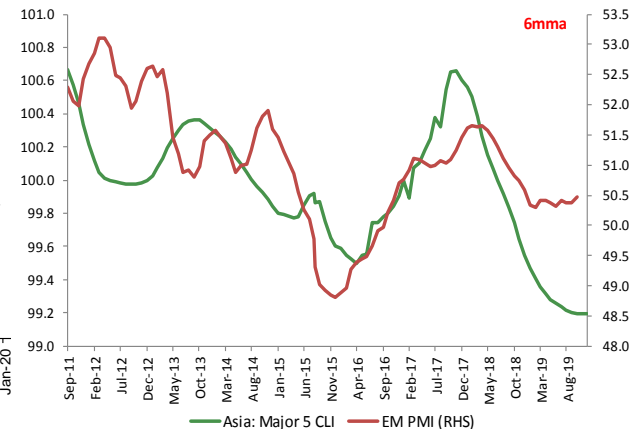
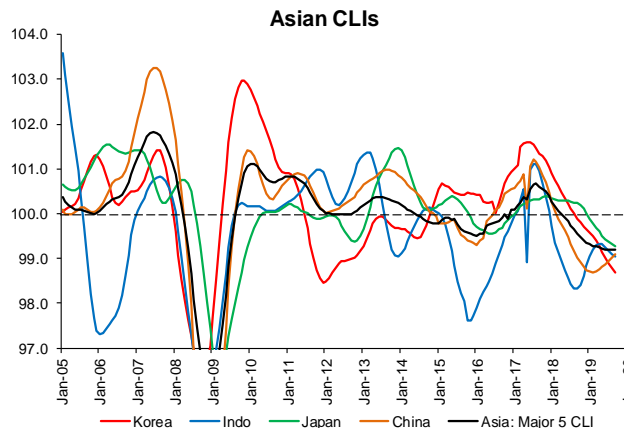
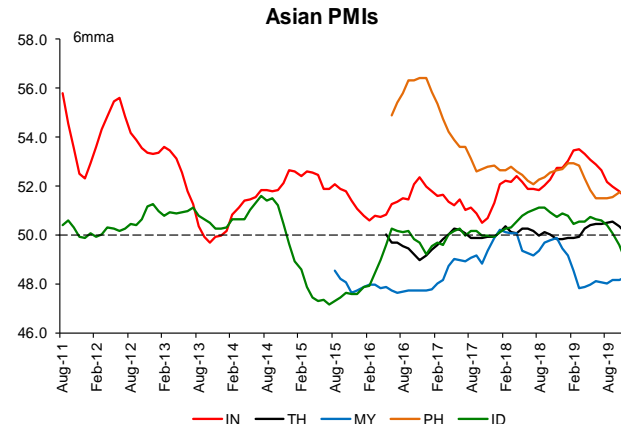
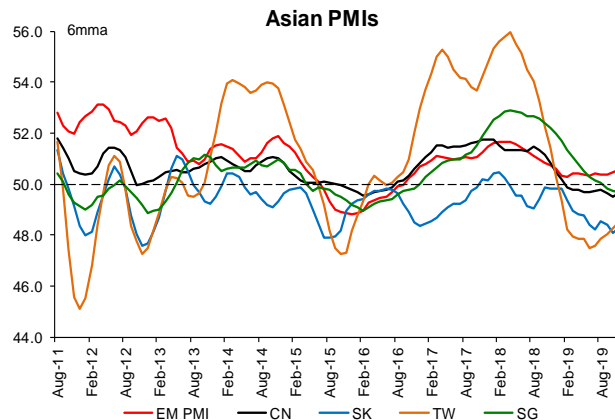


Asian FX Key Themes

- Asian FX have benefited significantly in 4Q19 from the pricing out of tail-end uncertainties and the ongoing risk-on sentiment. However, we may be at an inflexion point where further long term headway will require **(1) concrete Sino-US timeline beyond the Phase 1 deal**, or **(2) sustained macro improvement**, both of which may not be forthcoming.
- The Sino-US Phase 1 deal may have been achieved in principle, but we still lack a formal agreement to put the matter to rest. Further progress may be set aside due to the US Presidential elections. Thus, long term positioning based on Sino-US developments is next to impossible. On the growth front, we still lack concrete signs of sustained improvement. The question is when and how strong the recovery will be, if it actually arrives. The late-cycle dynamics may preclude a strong V-shaped recovery.
- Overall, **we prefer to remain tactical in Asian FX pending Sino-US developments, with the near term prospects looking positive, until we get more clarity in terms of a pick-up in macro outlook.** Pending the growth uptick, we still prefer to be underweight Asia as a whole, but to a reduced extent, in acknowledgement of the curtailment of downside risks.

Asian macro outlook remains soft (1)

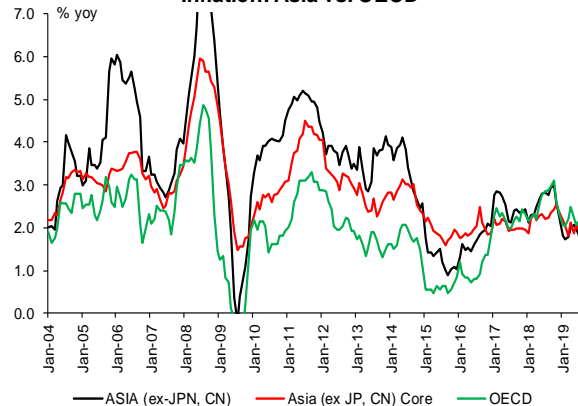
- Asia Major 5 CLIs bottoming out, especially in Indonesia and China. However, country-level high frequency data are still not showing strong signs of improvement.
- China manufacturing PMI has slipped into the contraction zone, while other Asian manufacturing PMIs reflect either a weakening bias, or outright contraction.



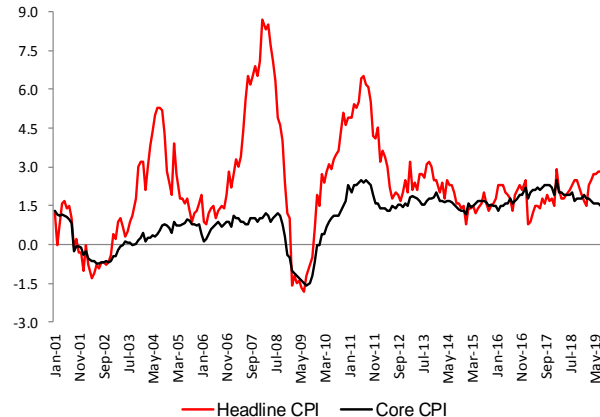
Asian macro outlook remains soft (2)

- Trade sector continues to be anaemic, hampering export-dependent Asian economies. Hope is placed on the Sino-US Phase 1 deal to set the stage for a trade rebound, but this is still speculative for now. Meanwhile, headline and core inflation continue to dip lower.
- **Still awaiting for the lagged effect of Asian central banks' monetary stimuli to be reflected in the data.** For now, expect more concrete signs of macro recovery between 2Q and 3Q 2020. **However, the recovery itself may not be a strong V-shaped bounce, given the late-cycle dynamics that we are now in.**

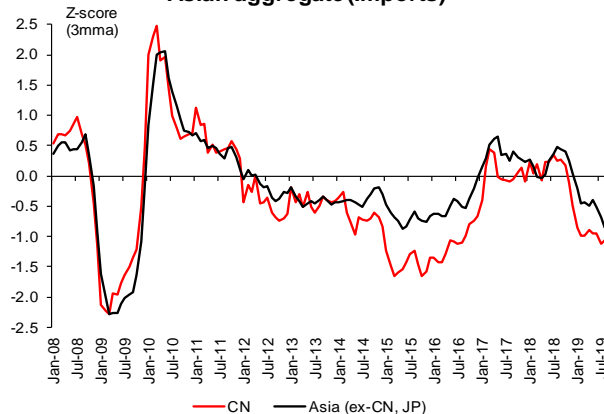
Inflation: Asia vs. OECD



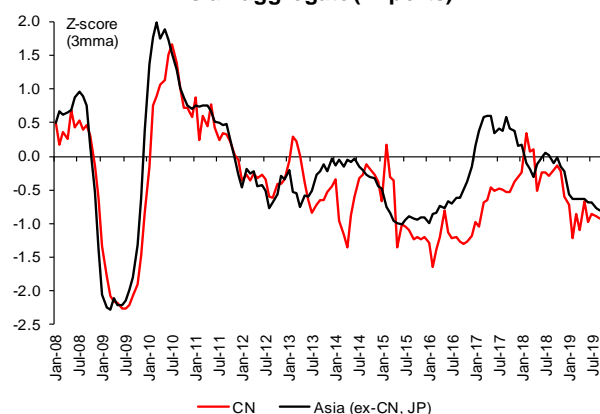
China inflation



Asian aggregate (Imports)

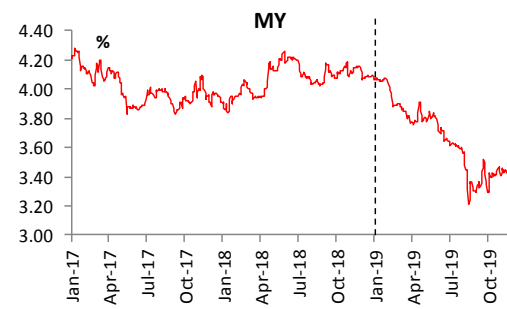
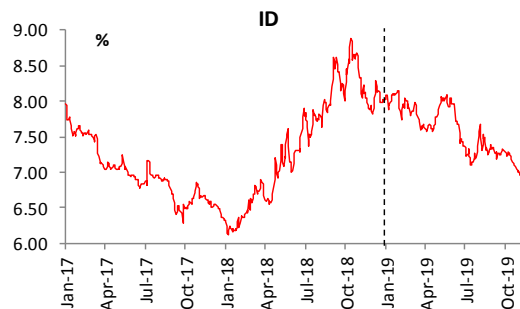
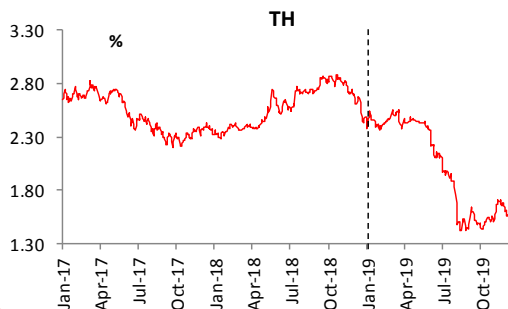
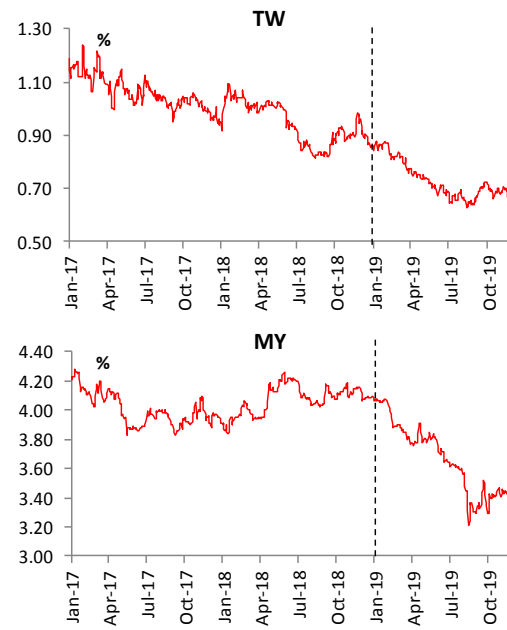
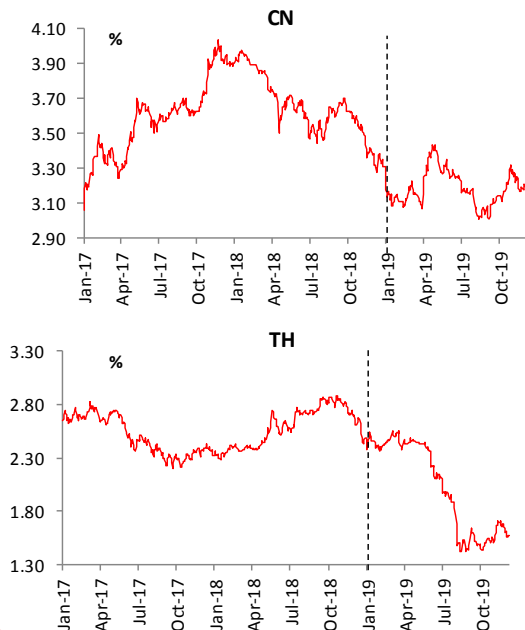


Asian aggregate (Exports)



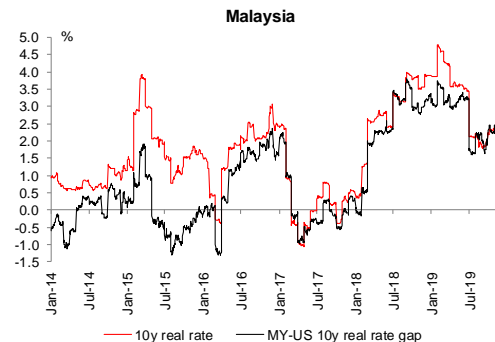
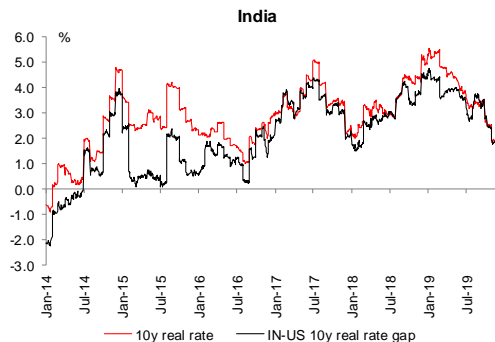
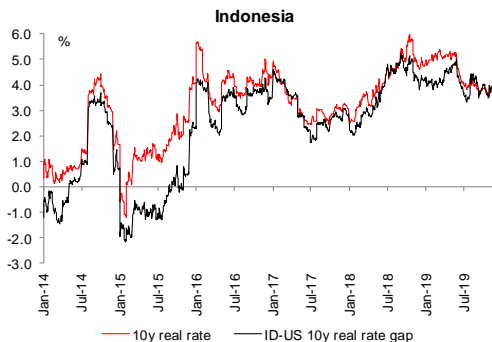
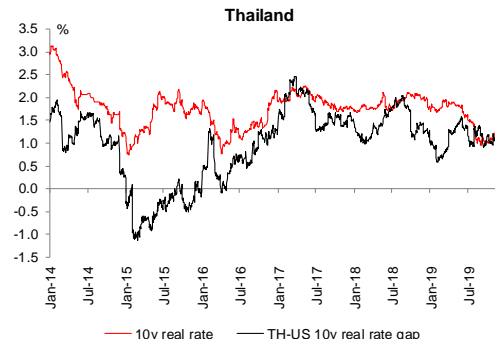
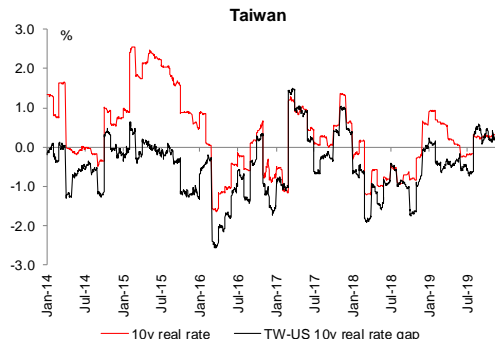
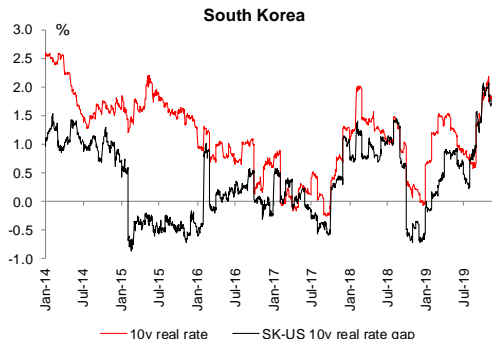
Asian 10y yields have mostly arrested declines

- Asian govt yields have been supported of late (Indonesia excepted) by improving risk sentiment. South Korean yields tracked G-10 yields higher. This reflects some short-term optimism that the macro outlook may not worsen significantly from here.



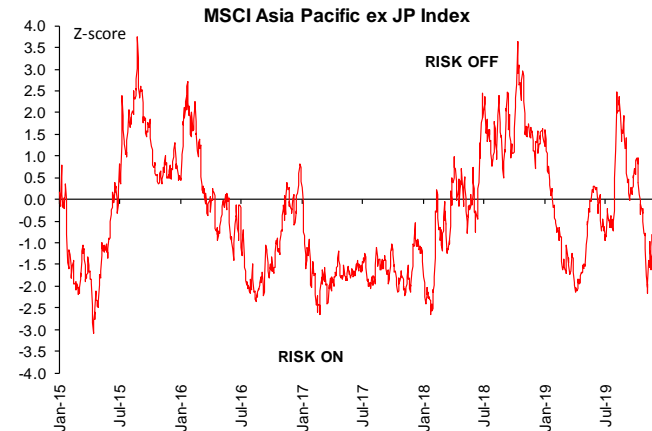
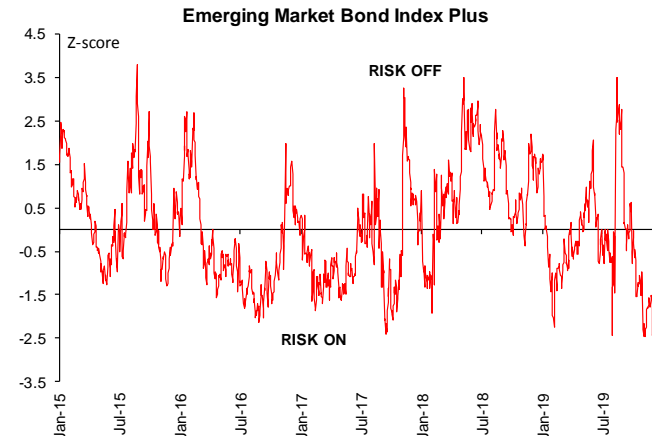
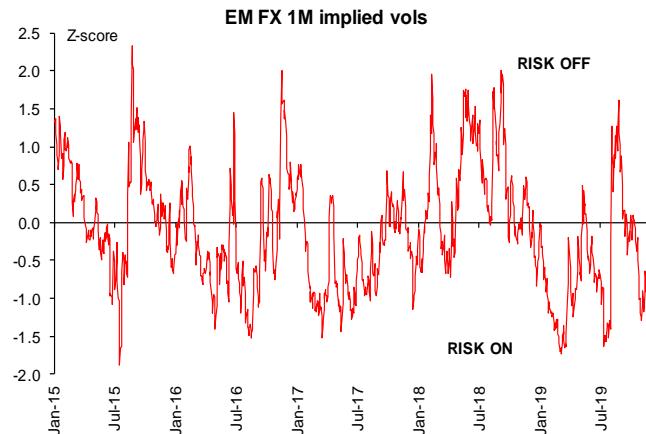
Long-end real yields have also normalized

- Real yields have also adjusted to the lower end of the recent historical range (South Korea excepted) – looser monetary conditions should fundamentally support growth going forward.



Sentiment in Asia positive, but not excessively

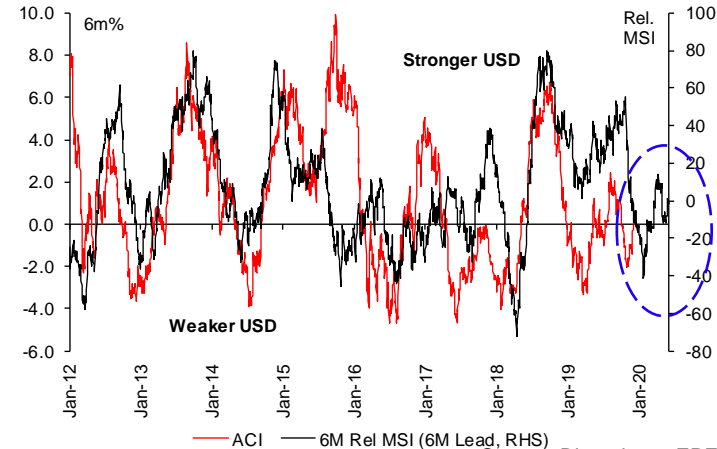
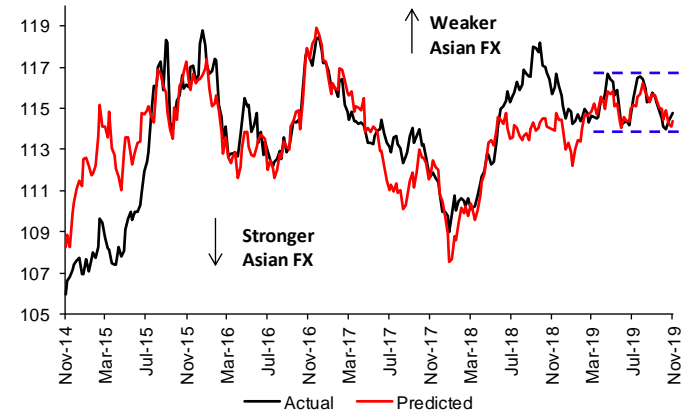
- Risk sentiment in Asia has turned positive across a number of asset classes, on the back of Sino-US rapprochement. However, the positive sentiment is not sufficiently stretched for now to risk a snap-back of asset price movement.
- Near term, how the Sino-US relationship progresses after the in-principle Phase 1 deal will still govern for investor sentiment. Any signs of break-down (this possibility probably should never be ruled out) should spark a swift reversal, taking Asian FX lower.



Structural drivers lacking; stay tactical on Asian FX

- Asian FX, as a whole, have performed in-line with their implied valuations. The recent run higher is largely sentiment-driven, with some support from a non-worsening macro outlook. However, with Sino-US developments inherently volatile, and the longer term lead from the macro outlook still negative for the Asian FX, we will not extrapolate recent strength too far into the future.
- **Our near term playbook remains decidedly short term, depending on the ebb and flow of Sino-US developments. Further out, the base case is for the macro outlook to stabilize around 2Q-3Q 2020, providing some support for Asian FX then. However, a strong V-shaped recovery may prove elusive, making a secular strong-Asian FX thesis difficult to construct.**

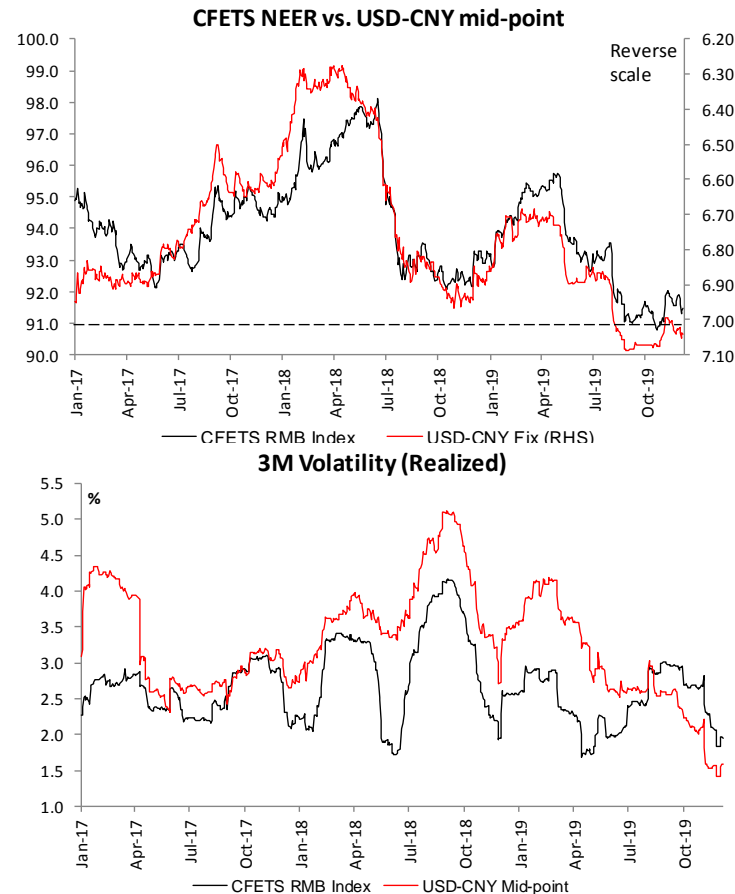
Asian Currency Index (ACI) implied valuation



Source: Bloomberg, EPFR, OCBC

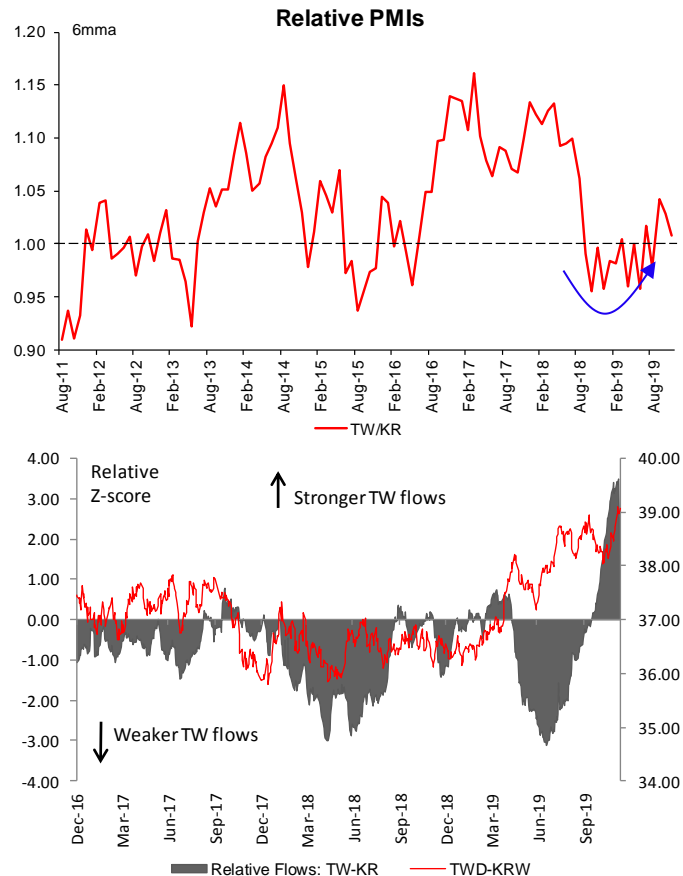
RMB: Headline-driven in the near term

- Initial positives for the RMB due to Sino-US rapprochement may be fully priced in for now. Any definitive positive outcome may yet drive the pairs lower to 6.8500. Any positives apart from that should have limited traction south of 6.9500. Overall, expect Sino-US talks to be the main near-term driver for RMB and North Asian currencies.
- Longer term, while the still-weak Chinese domestic economy weighs on the RMB, note that RMB depreciation is not regarded as a stimulatory tool. Thus, the risks of a sharp depreciation in the RMB is effectively curtailed.



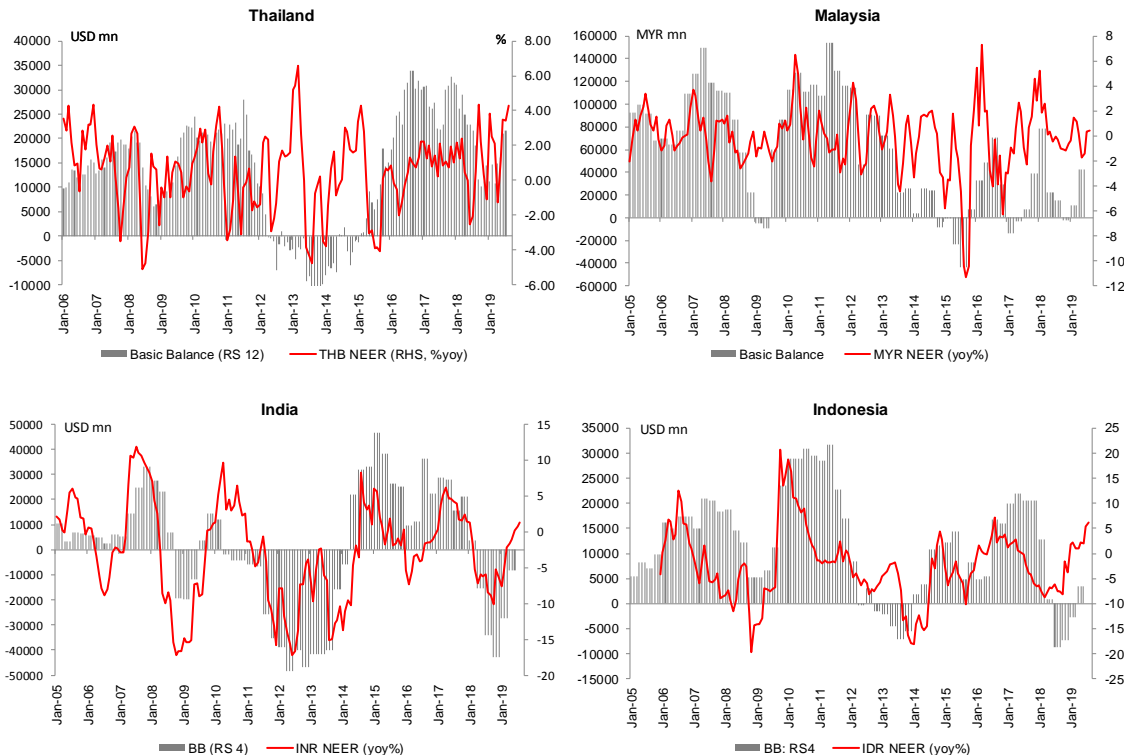
North Asia: TWD favoured over KRW

- The macro outlook for Taiwan has been better than South Korea this year. While, the export sector has been weak across Asia, the experience in Taiwan has been considerably more resilient compared to South Korea and Singapore. Similarly, on the PMI front, the Taiwanese gauge has outperformed relative to South Korea. The structural (rolling 60-day basis) inflow environment, has also moved consistently in favour of Taiwan relative to South Korea since 3Q19.
- **These ongoing factors drive us to favour TWD relative to KRW early in 2020.**
- The risk for this thesis is BOK's easing measures translating to a strong uptick in South Korea's macro outlook. However, there are limited signs of this recovery for now.



South Asia: Basic balance supports currencies

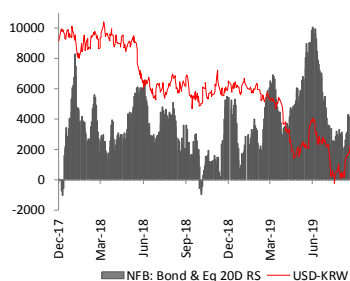
- South Asian currencies have been less reactive to Sino-US progress, but the underlying fundamentals are improving, or remain strong. This provides background support for the currencies.
- In particular, the THB has been undergirded by strong and improving basic balance – this should frustrate Bank of Thailand's ongoing attempts to weaken the THB.



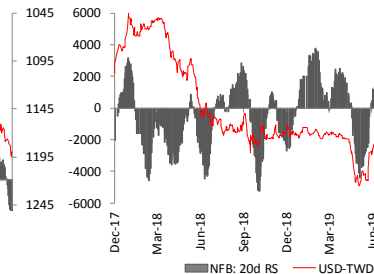
Portfolio flows into Asia faltering again

- A secular return of inflows into Asia may only materialize if growth improves sustainably – a 2Q/3Q 2020 story in our view. Under that environment, expect the high-yielders, **IDR** and **INR**, to outperform. Near term, the capitulation of inflows into Korea relative to Taiwan points to further **TWD-KRW** upside.

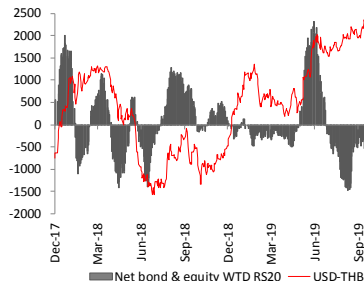
South Korea



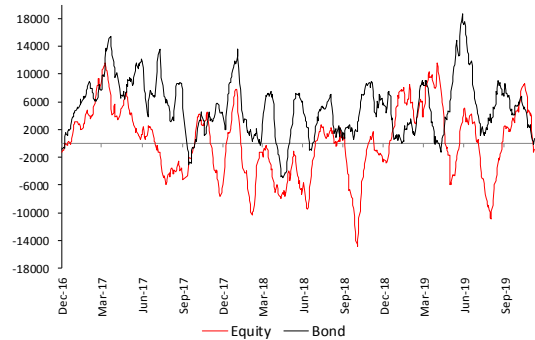
Taiwan



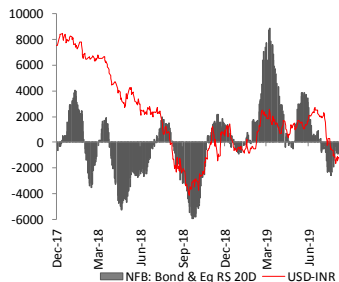
Thailand



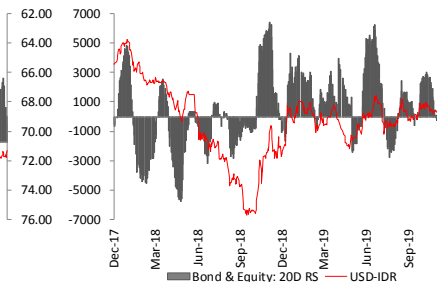
Asian aggregate portfolio flows (20D Rollsum)



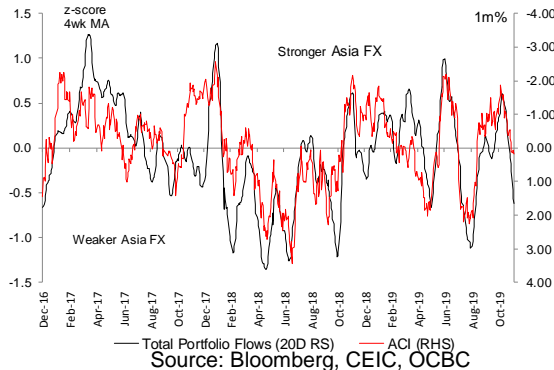
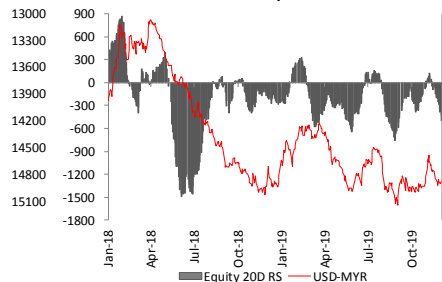
India



Indonesia

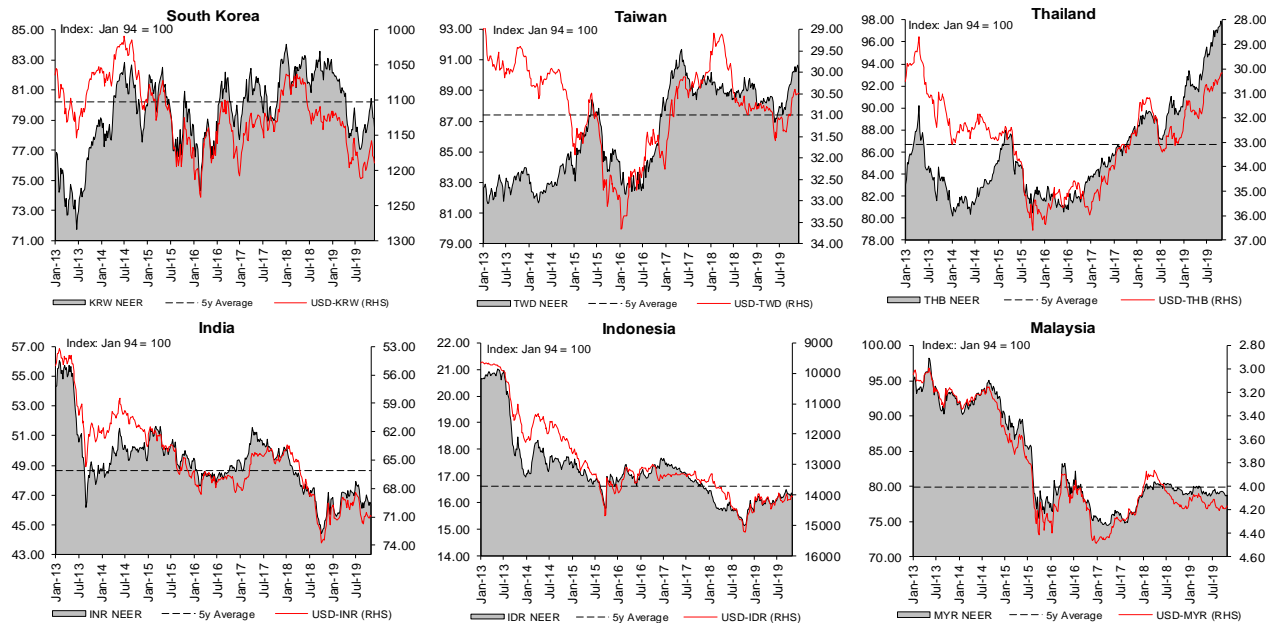


Malaysia

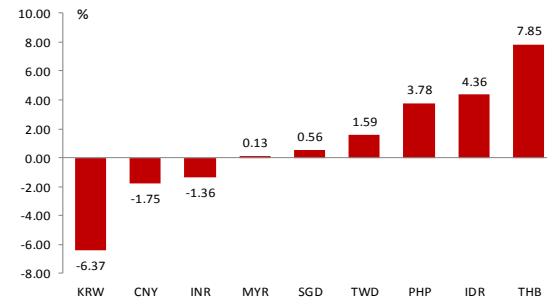


NEERs: THB strength year-to-date attracting attention

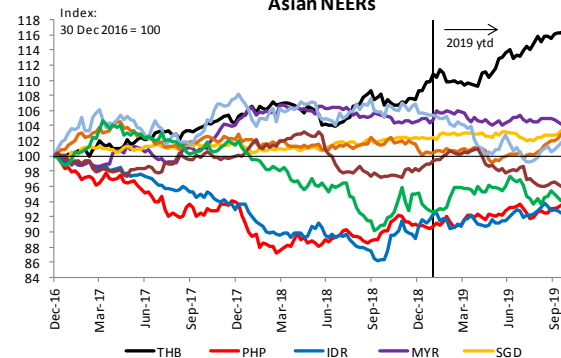
- Apart from the THB, most Asian currencies still are within familiar ranges in NEER terms. Nevertheless, BOT's attempts to rein in the THB may only be sufficient to cause the THB to lag relative to Asian peers, but not an outright turn in USD-THB trajectory.



Year-to-date Asian NEER performance



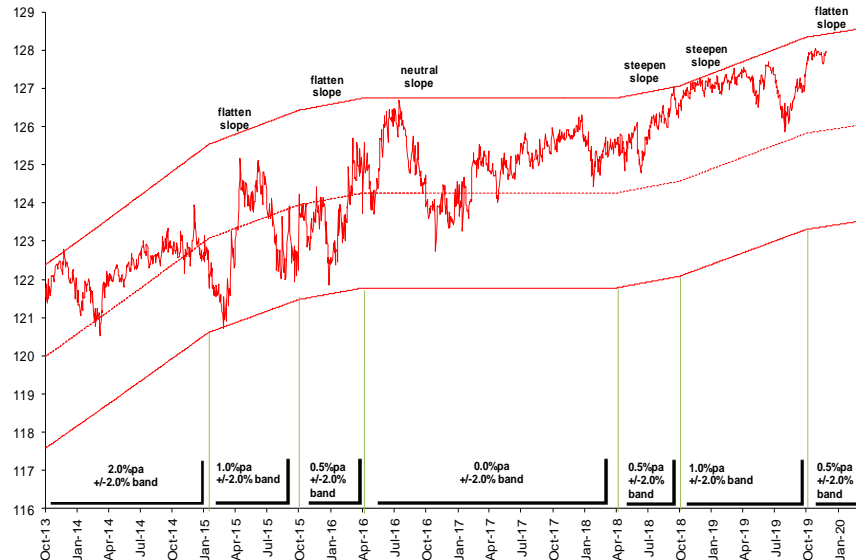
10/12/2019
Asian NEERs



Source: Bloomberg, OCBC

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- 129 flatten



FX Forecast (correct as of 4 Dec)

	Spot	Dec-19	Feb-20	May-20	Aug-20	Nov-20
USD-JPY	108.46	108.16	109.08	109.25	107.90	106.56
EUR-USD	1.1084	1.1107	1.1080	1.1080	1.1190	1.1300
GBP-USD	1.3044	1.3053	1.3191	1.3234	1.3280	1.3326
AUD-USD	0.6819	0.6831	0.6831	0.6881	0.6948	0.7015
NZD-USD	0.6504	0.6570	0.6563	0.6577	0.6637	0.6697
USD-CAD	1.3287	1.3361	1.3346	1.3358	1.3418	1.3478
USD-CHF	0.9859	0.9814	0.9871	0.9871	0.9801	0.9730
USD-SGD	1.3645	1.3672	1.3604	1.3597	1.3546	1.3494
USD-CNY	7.0689	7.1047	7.0379	7.0212	6.9625	6.9039
USD-THB	30.29	30.46	30.29	30.29	29.93	29.57
USD-IDR	14105	14,219	14,123	14,123	13,941	13758
USD-MYR	4.1777	4.1987	4.1805	4.1805	4.1477	4.1149
USD-KRW	1194.55	1202.82	1194.05	1194.05	1181.03	1168.01
USD-TWD	30.503	30.556	30.339	30.310	30.215	30.120
USD-HKD	7.8291	7.8350	7.8300	7.8150	7.7975	7.7800
USD-PHP	51.02	51.20	50.83	50.80	50.55	50.30
USD-INR	71.68	71.93	72.51	72.88	71.32	69.76
EUR-JPY	120.22	120.13	120.86	121.05	120.74	120.41
EUR-GBP	0.8497	0.8509	0.8399	0.8373	0.8426	0.8479
EUR-CHF	1.0928	1.0900	1.0937	1.0937	1.0967	1.0995
EUR-SGD	1.5124	1.5185	1.5073	1.5065	1.5157	1.5249
GBP-SGD	1.7800	1.7845	1.7946	1.7993	1.7989	1.7983
AUD-SGD	0.9304	0.9339	0.9293	0.9356	0.9411	0.9466
NZD-SGD	0.8875	0.8982	0.8928	0.8943	0.8990	0.9037
CHF-SGD	1.3840	1.3931	1.3782	1.3774	1.3821	1.3869
JPY-SGD	1.2580	1.2640	1.2472	1.2446	1.2554	1.2664
SGD-MYR	3.0617	3.0711	3.0730	3.0746	3.0620	3.0493
SGD-CNY	5.1804	5.1967	5.1734	5.1639	5.1401	5.1161

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