# Asia FX Update:

## Creeping divergence between USD-Asia pairs

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Treasury Research & Strategy
Global Treasury

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# Asian FX Key Themes

- A two-speed recovery in Asia continues to persist, with China looking on track but the rest of the Asia still soggy (p. 3-7). The latest data dump in China reinforced the status of its recovery, while countries like South Korea are grappling with a persistently weak export sector and Indonesia with renewed semi-lockdown arrangements. Moreover, risk sentiments are also looking increasingly choppy (p. 8). The interplay between the (1) weak USD, (2) resilient RMB and (3) idiosyncratic domestic factors should result in a sharper divergence between the USD-Asia pairs in the near term (p. 9-11).

- **Summary of research view**: Overall, we stay positive on the RMB front, expecting further room for strengthening before reaching levels of concern (p. 3, 9). However, how this translates to the rest of the Asian currencies is mixed. For now, downside for USD-North remains rather curtailed, not least because of a lack of official tolerance for a stronger local currency. MYR is the most reactive to the RMB, although it may face firmer resistance going forward from current levels. Meanwhile, continue to expect the IDR to move more on domestic imperatives. Meanwhile, the further worsening of the portfolio flows environment in Asia continues to be unsupportive of outsized Asian FX strength (p. 12-13). For the USD-SGD, the weak USD and firm RMB have opened up further downside room for the pair, even while keeping the SGD NEER anchored near parity. Expect further southbound drift if the 1.3600 floor fails to hold up (p. 14).

# Short term FX/bond market views and commentary

| | USD-Asia | 10y govie (%) | Commentary |
|---|---|---|---|
| **China** | ↓ | ↔/↑ | Macro recovery in China remains on track, weathering a slight blip in Jul. Aug industrial production back above expectations. A bigger confidence booster is retail sales, which had been the laggard in the recovery story. Aug prints were firmer than consensus, first time since the crisis. Aug official PMIs mixed, with the manufacturing print marginally weaker than expected, but the services print firmer. Both Caixin gauges are in expansionary territory, and better than expected. Aug exports also outperformed at 9.5% yoy, against expectations of 7.5% yoy. M2 growth marginally softer than expected, but aggregate financing expanded at a pace faster than expected. Overall, RMB positives remain broadly intact, with bulls likely to be boosted due to strong macro prints. **With 6.8000 breached, the next target will shift lower towards 6.7100/200 on a multi-session horizon. Persist with the strong RMB bias for now.** |
| **S. Korea** | ↔/↓ | ↔/↑ | A fourth extra budget this year, was announced and is pending Parliament approval. If approved, it will provide targeted support for the most vulnerable sectors. This spending is expected to be financed by government borrowings, and should raise debt-to-GDP ratio to 43.9%, from 43.5%. While this is not expected to be an issue, it will put pressure on the BOK to increase its bond purchases to stabilize the bond market that will face extra supply. The BOK held rates unchanged in Aug, but downgraded growth to -1.3% yoy for FY2020, from -0.2% yoy forecasted in May. Final print for 2Q GDP was shaded higher to -2.7% yoy, from -2.9% yoy. Aug man. PMI continued to recover, printing 48.5, compared to 46.9. Export contraction in Aug stands at -9.9% yoy, better than expected. With exports soft, expect little appetite for sustained KRW strength. **Expect the USD-KRW to stay range-bound between 1175.00 and 1195.00, with the domestic virus situation offsetting the soft USD.** |
| **Taiwan** | ↔/↓ | ↔/↓ | Macro conditions arguably more favourable compared to South Korea. Aug man. PMI continued to show uptick, printing 52.2, from 50.6 in July. Aug exports also showed a sharp rebound to 8.3% yoy, outstripping expectations handily. Aug headline CPI entered at -0.33% yoy, marginally better than expected. **The USD-TWD should be led lower by USD-CNH, but official tolerance seemed to be lacking.** |

# Short term FX/bond market views and commentary

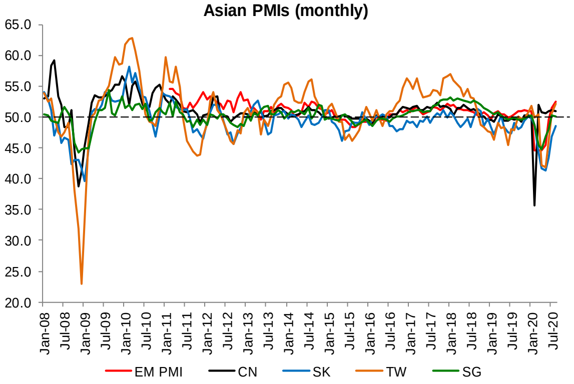
| | USD-Asia | 10y govie (%) | Commentary |
|---|---|---|---|
| **Singapore** | ↔/↓ | ↔/↑ | MOM's 2Q labour market report was a difficult read, with number of retrenchments spiking. Nevertheless, headline unemployment prints are still healthier than previous crises. NODX growth slowed in July relative to June, but remains stronger than expected. Jul headline and core CPI printed -0.4% yoy and -0.4% yoy, with the headline print improving from the previous month, but the core print slipped deeper into deflationary zone. Aug official PMI eased to 50.1, from 50.2 prior. The Markit reading, however, slipped lower to 43.6, from 45.6. **The combination of weak USD and firm RMB has opened up further room for USD-SGD. Expect the pair to flex against 1.3600, with a breach likely to see the pair ease towards 1.3450/00.** |
| **Thailand** | ↔ | ↔/↑ | Political issues persist, with the finance minister position still vacant. BOT unchanged at the Aug meeting as expected, with major moves likely only after the new governor takes over in Oct. 2Q GDP at -12.2% yoy, better than estimates. Thai finance ministry cut FY2020 GDP growth further to -8.5% yoy. Aug man. PMI continue to recover, printing 49.7, from 45.9 prior, but still in contractionary zone. July custom exports declined -11.37% yoy, a slower pace compared to Jun and better than expectations. Contraction in customs imports, however, accelerated to -26.38% yoy in Jul. Aug headline CPI printed -0.50% yoy, better than expected. Core CPI at 0.30% yoy. **USD-THB turned lower after USD weakness overrode domestic issues. However, expect the THB to underperform other Asian currencies for now.** |
| **Malaysia** | ↓ | ↔ | BNM held rates unchanged in its Sep meeting, inserting a new line in the statement that suggest that the rate cut cycle may be on hold for now. Nevertheless, the bar for further cuts are not high, especially if the macro recovery slumps further. 2Q GDP slumped -17.1% yoy (mkt consensus: -10.9% yoy), but the silver lining is that most economic activities have bounced back sharply by June. Jul CPI print in deflationary territory, but in line with expectations. Aug man. PMI slid back into contractionary zone at 49.3, from 50.0 prior. Jul exports again printed positive yoy, against market expectations of a contraction. Imports, however, continue to be cut lower fell -5.6% yoy, better than expected. **Downside momentum in USD-MYR remains intact, although the extension has gone on for quite an extent. Limited motivation to chase the pair lower from current levels.** |

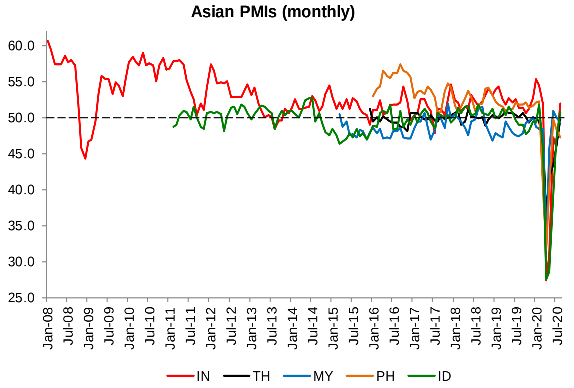
# Short term FX/bond market views and commentary

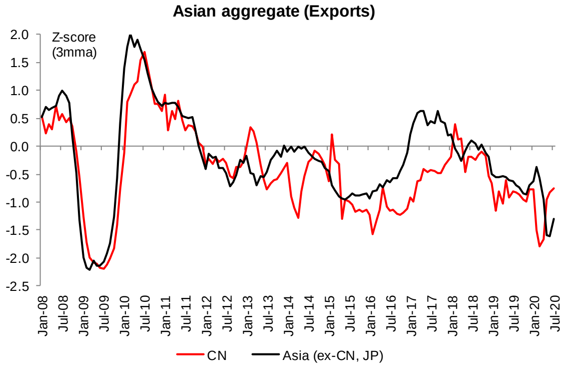
| | USD-Asia | 10y govie (%) | Commentary |
|---|---|---|---|
| **India** | ↔/↓ | ↑ | 2Q 2020 GDP print slumped -23.9% yoy, worse than an already weak -18.0% yoy. Such heavy prints are expected to prompt a rethink of fiscal conservatism in the government. Aug CPI prints at 6.69% yoy, marginally softer than expected but still beyond the RBI's tolerance band. RBI held policy rates unchanged in Aug, although the accommodative stance is retained. Measures also implemented to support the banking sector. Aug man. PMI rebounded higher to 52.0, from 46.0 prior. June exports shrank -12.4% yoy, while imports slumped -47.6%. USD-INR slipped lower towards 73.50, as selling pressure were not met with a supporting RBI. **RBI's tolerance level for the USD-INR may be lowered, but still some price discovery is needed to find the next support.** |
| **Indonesia** | ↔/↑ | ↔ | Renewed semi-lockdown arrangements in Jakarta and its surrounds. A draft law with new initiatives that may potentially undermine central bank independence will keep foreign investors on its toes. The BI held policy rates unchanged at 4.00% for its August meeting, as focus shifts towards the monetary channel for further accommodation and protecting currency stability and rate differentials. 2Q GDP contracted -5.32% yoy, against expectations of -4.72% yoy. Aug trade prints continue to show sharp declines for both the export and import sectors. Aug headline and core CPI at 1.32% and 2.03% yoy respectively, largely in line with expectation. Aug man. PMI recovered back into expansionary zone at 50.8, compared to 46.9 prior. **This overarching worry about BI independence and debt monetization won't go away easily, giving a background upward lift for the USD-IDR. However, a combination of reassurances from FM Sri Mulyani and BI intervention should keep a lid at 15,000 for now.** |
| **Philippines** | ↓ | NA | 2Q GDP contracted -16.5%, worse than the expected -9.4% yoy. The BSP held policy rates unchanged in its August meeting to allow the impact of previous cuts to flow through the economy. Aug CPI eased lower to 2.4%, below expectations. Aug man. PMI dipped for the second consecutive month at 47.3 versus 48.4 prior. Jul exports contracted -9.6% yoy and imports -24.4% yoy. Jun remittances unexpectedly grew 7.7% yoy, against expectations of a -7.2% yoy contraction. **No let-up in terms of USD-PHP downward trend, especially with 48.50 support breached.** |

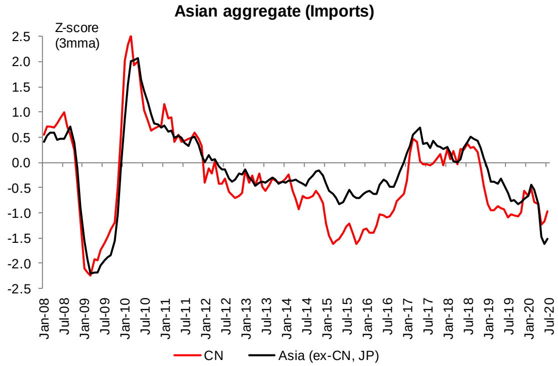
# Divergent prospects across Asia

- **Recent data prints in Asia reveal a two-speed recovery.** On one end, the August PMI prints in Malaysia and Philippines are back-sliding. PMI prints in Thailand and South Korea are recovering, but remains within contractionary zone. The most optimistic recoveries are in Taiwan and China, where PMIs are firmly within the expansionary territory.
- The export sector remains challenging for Asia (ex. China). Most economies' exports are still mired in contraction on a yoy basis. China and Malaysia are the exceptions. Traditionally export-reliant economies like South Korea and Singapore remains the worst hit.

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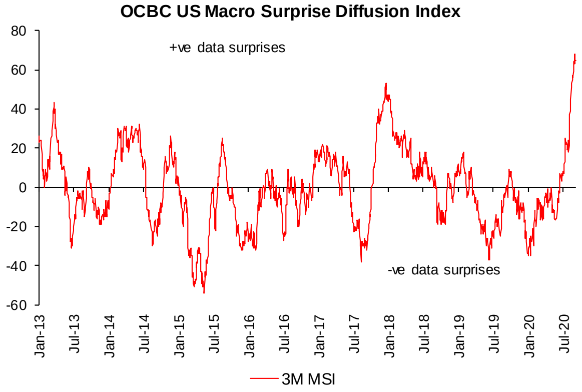
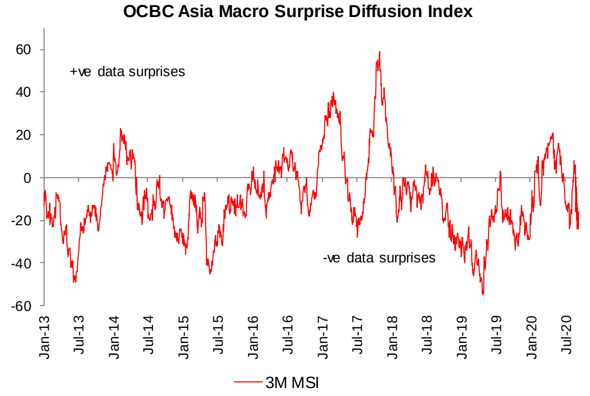
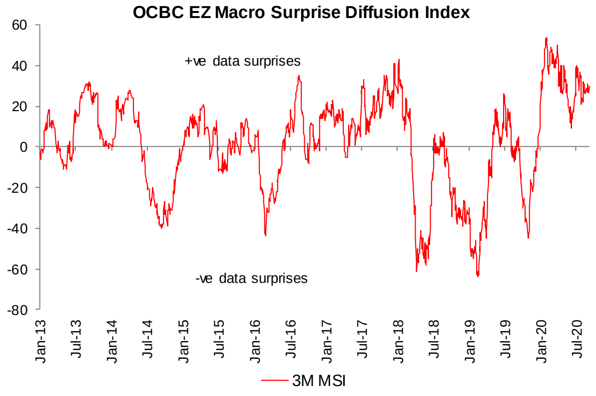
Source: Bloomberg, CEIC, OCBC

# Still not optimistic on Asia (ex. China) recovery

- **The Macro Surprises Index for Asia continued to show no upward momentum, suggesting that the macro outlook outside of China have yet to shake off the underlying challenges.** Note that the COVID-19 remains bad for a number of Asian economies, notably South Korea and Indonesia (which is heading back into a semi-lockdown arrangement). Thus, stay pessimistic regarding a strong, sustained macro recovery in Asia (ex. China). The situation in China is notably more upbeat (p. 10).
- In the US, the rolling-off of fiscal stimulus, and the subsequent impasse in the fiscal support talks weighs negatively. Market expectations for further fiscal support prior to the Nov elections seems low at this juncture. Meanwhile, the sense in Eurozone is rather more optimistic, with the ECB lifting the FY2020 forecast. Do note however, that second-wave virus cases looks to be hitting parts of Europe, with countries starting to tighten restrictions again.

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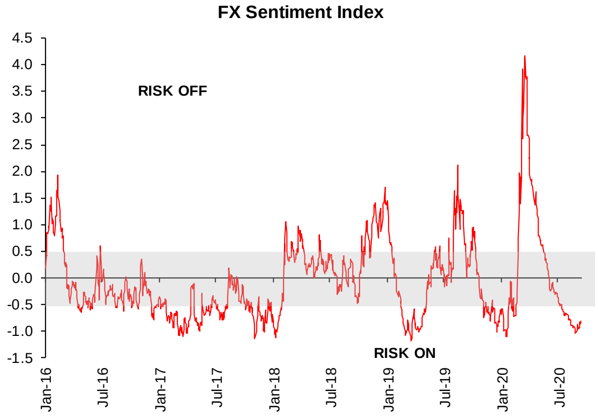
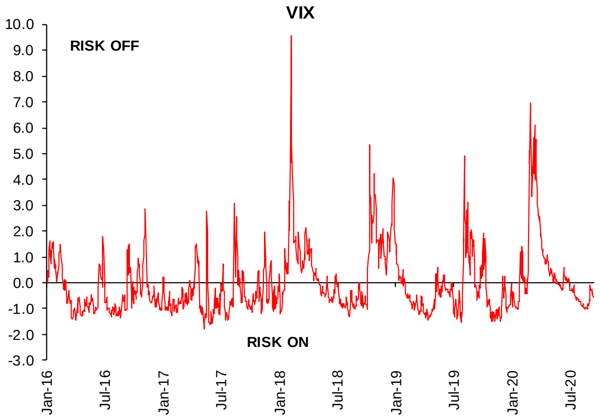
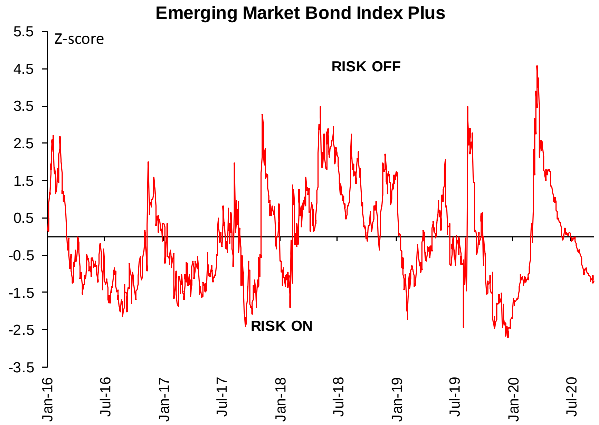
Source: Bloomberg, OCBC

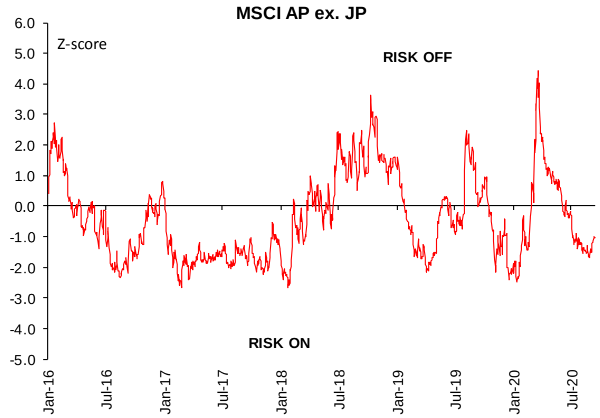
# Equity pullback forces a pause in the risk-on sentiment

- While still in the outright **Risk-On** zone, the **FX Sentiment Index (FXSI)** has started to pull higher this week, signaling a slight weakening of overall risk sentiment. Equity-related sub-indices in the FXSI are driving this move, while the bond market sub-indices still tilt risk-on for now.
- Major asset classes are mostly in a sideways posture, looking for clearer directionality. Such indecision is also reflected in the current choppy nature of risk sentiment. For now, **watch the equities space as a near term guide on overall sentiment**.

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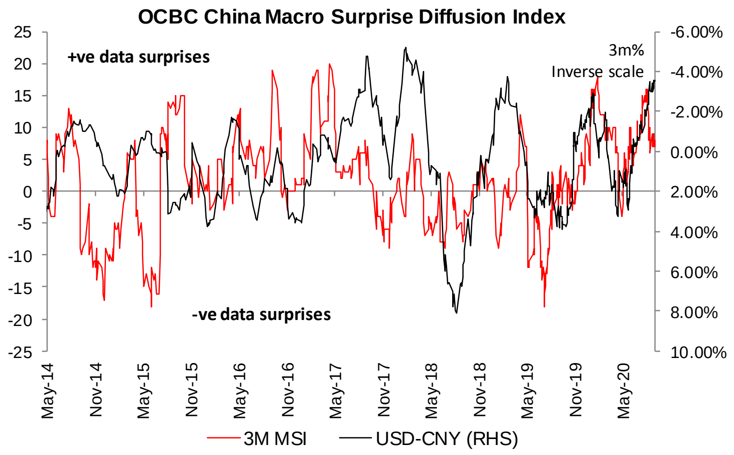
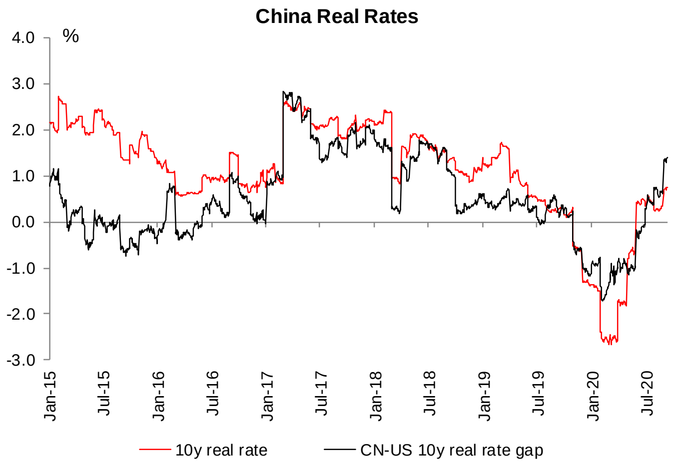
Source: Bloomberg, OCBC

# RMB: Latest data releases reinforce the Chinese recovery

- August industrial production and retail sales data suggest that China has weathered a slight dip in recovery momentum in July. The outperformance in retail sales is particularly encouraging, considering that it has been a laggard in the recovery story. This also underlies the pivot towards domestic consumption as a key driver for the Chinese economy.
- Overall, our RMB positive view has been strengthened. For now, we still see no pushback against the firming RMB through official jawboning or higher than expected USD-CNY morning fixes. On the CFETS RMB Index front, we are still a distance away from the peaks. **Thus, with the USD-CNH breaching the 6.8000 level, we expect the southbound target to shift lower to 6.7100/200 on a multisession horizon.**

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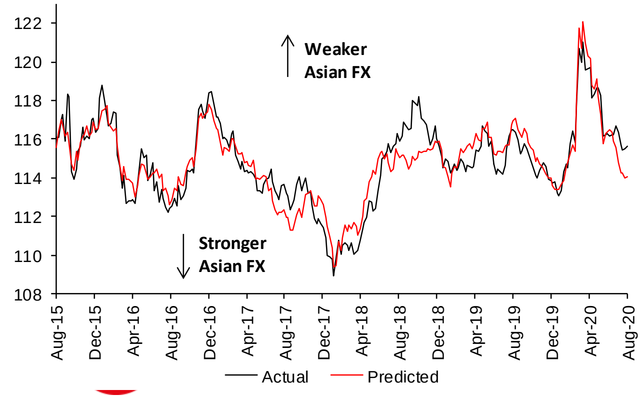
Source: Bloomberg, OCBC

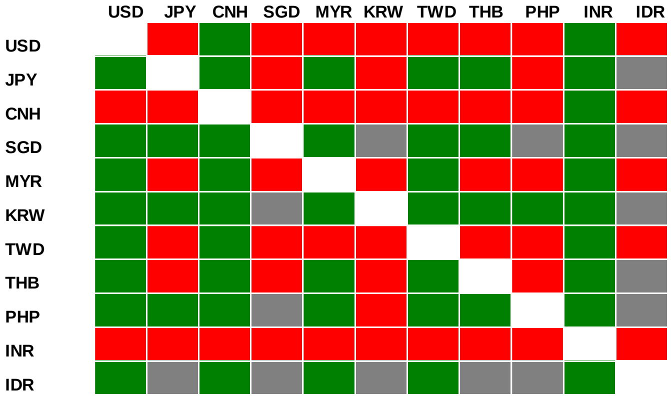
# RMB leads, but other Asian FX follows at their own pace

- A directionless USD and a resilient RMB imply that the broader environment is positive for Asian currencies. **However, after factoring in idiosyncratic domestic drivers, the sensitivity will differ across the USD-Asia pairs.** USD-North should be expected to react lower. However, the **USD-KRW** faces domestic macro issues and the 1175/80 may be a firm floor, while there are limited official tolerance for a lower **USD-TWD**. The **USD-MYR** has been reactive to the RMB, but its extension lower also start to hit firmer supports at current levels. The ability to breach the 4.1300/400 zone may see the 4.0500 implicitly attract, but we may not want to chase the pair lower for now.
- Domestic factors are still to dominate for the **USD-THB** and **USD-IDR**. Near term concerns of a spike in USD-IDR due to BI independence and debt monetization concerns have been alleviated through repeated reassurances and BI intervention. 15,000 may be a line in the sand for the USD-IDR in the near term. **Nevertheless, expect upward pressures to arise periodically, until the BI independence and debt monetization concerns are put to rest.**

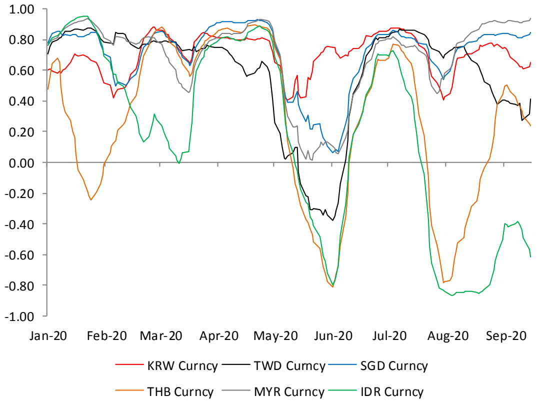
**Asian Currency Index (ACI) implied valuation**




**Asian FX Short-term Heat Map**



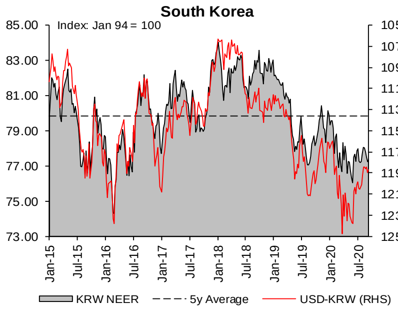

**40-day Correlation with RMB**

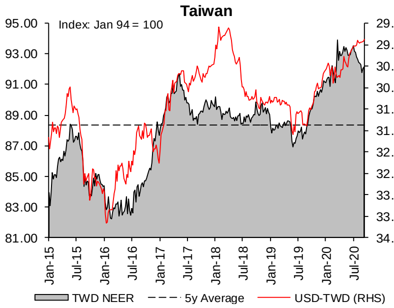


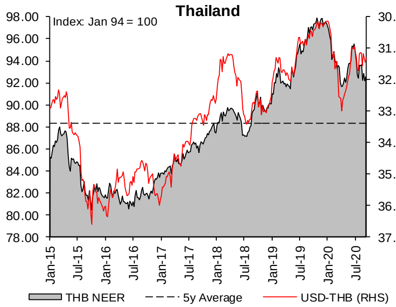

Source: Bloomberg, EPFR, OCBC

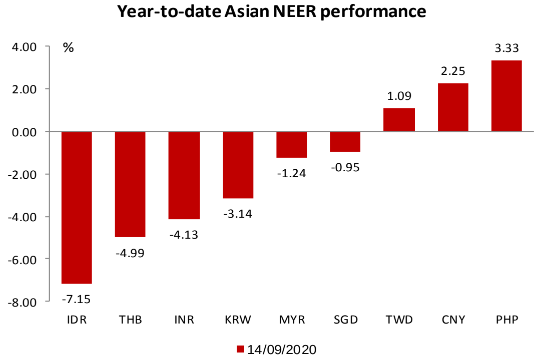
# NEERs: Increasing divergence across Asian currencies

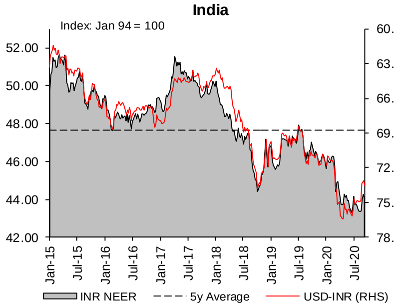
- The ranking of Asian NEERs have not changed this week, but a clear divergence has emerged. The underperformers (IDR, THB) in NEER basis have extended their declines, while the KRW was also one of the weakest compared to the previous update. On the flipside, focus on RMB strength

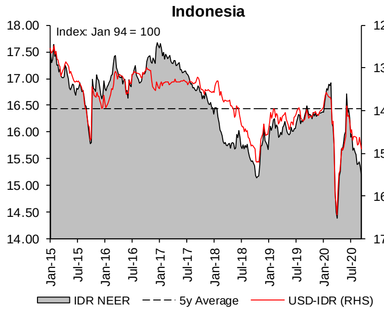


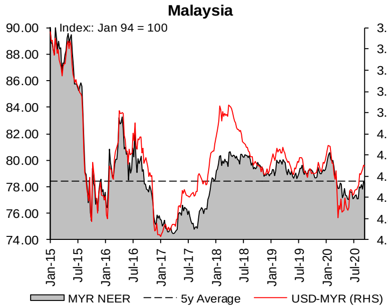



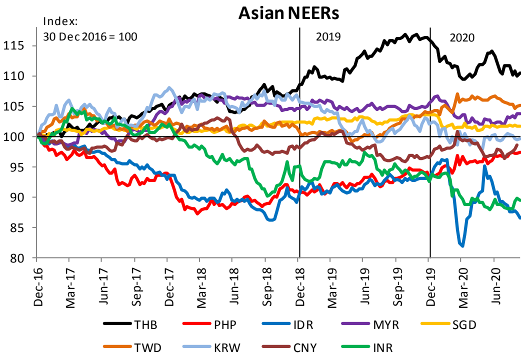

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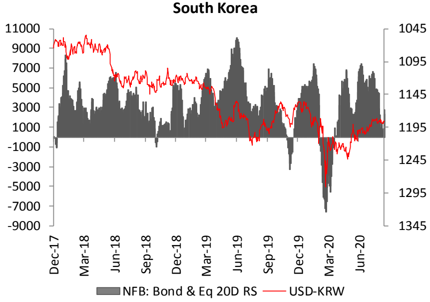
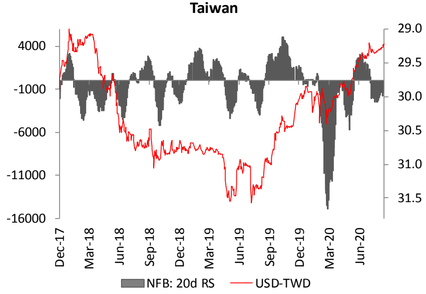
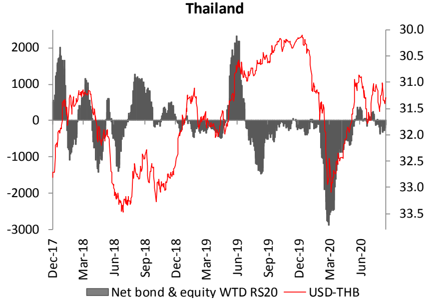
Source: Bloomberg, OCBC

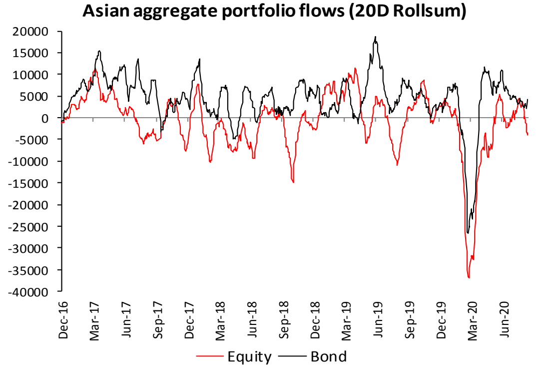
# Portfolio inflow momentum evaporating (1)

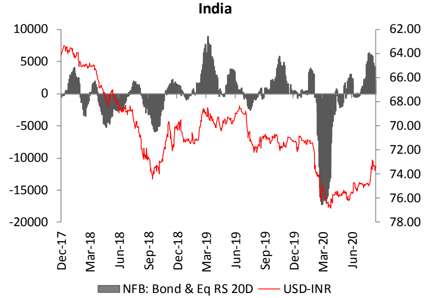
- Equity flows across Asia have dipped into a net outflow situation on aggregate terms. Even the previous poster boy for equity inflows, India, is seeing momentum moderate sharply lower. Only positive is in Malaysia, where equity outflow momentum is easing. Moderation of inflow momentum also noted on the bond front.

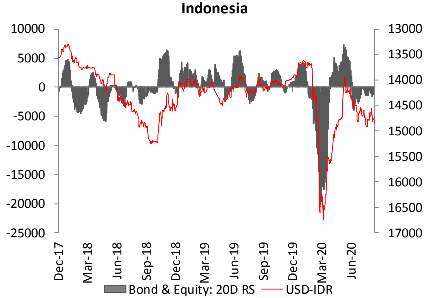


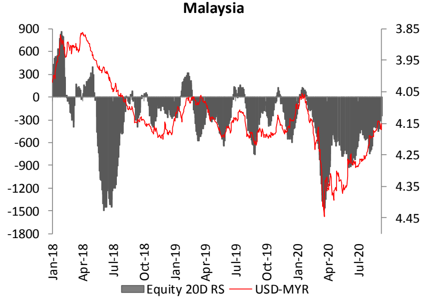



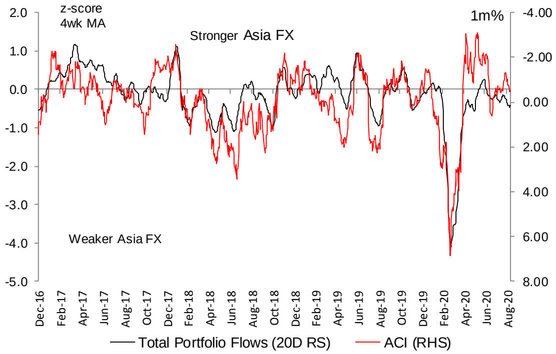

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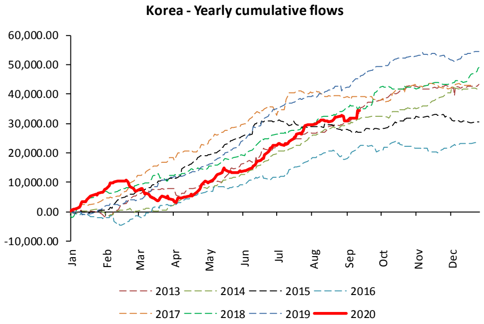
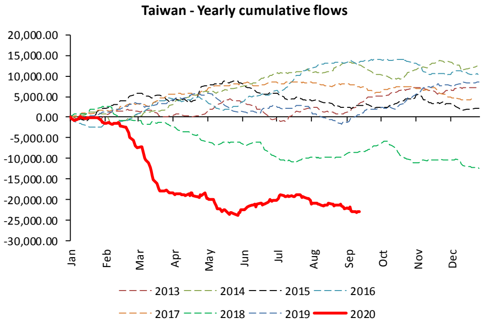
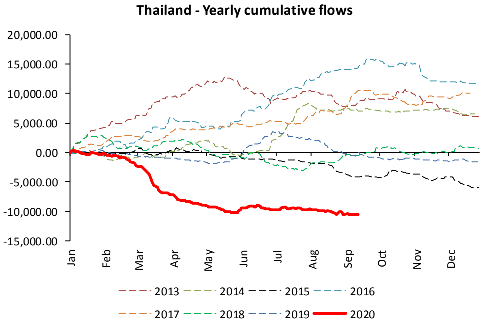
Source: Bloomberg, CEIC, OCBC

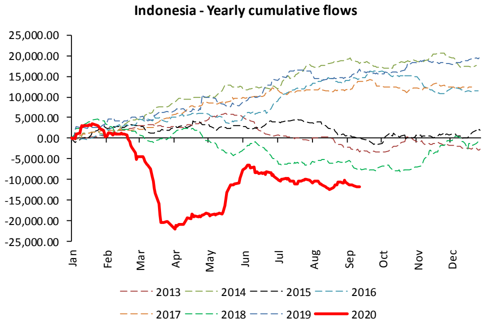
# Portfolio inflow momentum evaporating (2)

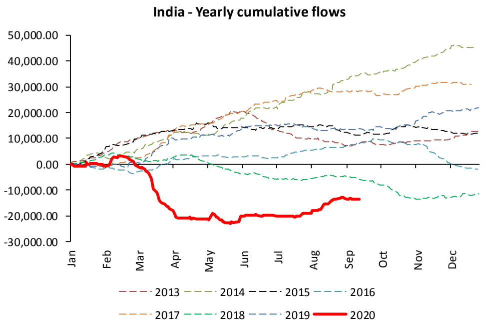
- Save for South Korea, all Asian economies have seen sharp net outflows year-to-date. More worryingly, there is no sign of the gap closing at all. **This keeps us from being outright bullish for Asian currencies. Instead, we see Asian FX resilience more of a function of broad USD malaise, and RMB resilience.**

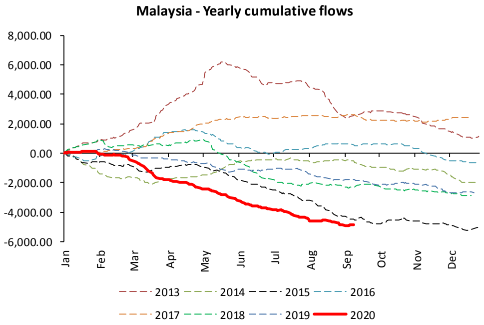
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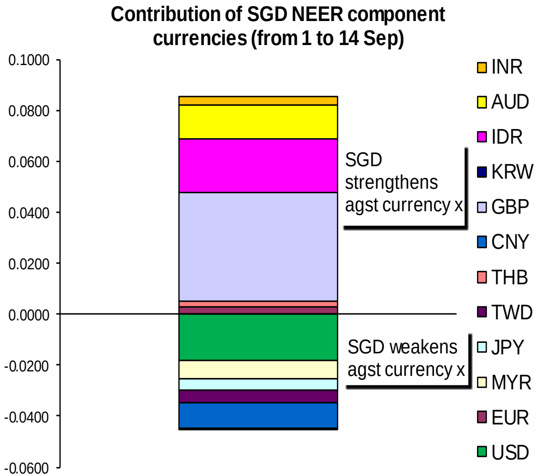
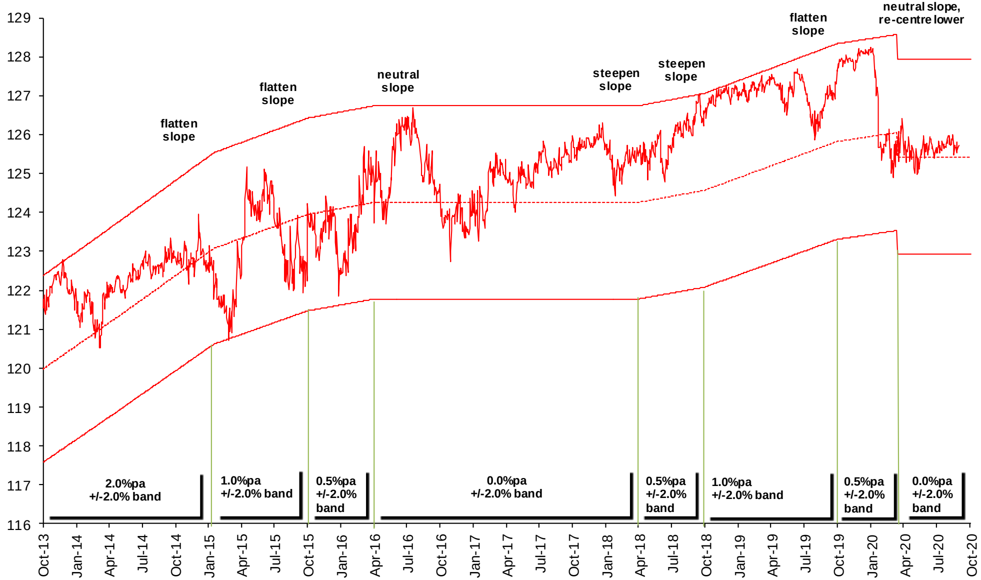
Source: Bloomberg, CEIC, OCBC

# SG: Labour market prints are a difficult read…

- … but does it impinge on MAS's deliberations for the upcoming Oct MPS? Our current sense is that the labour market issues are not yet sufficient to jolt the MAS into taking additional action. A degree of labour market slack would already have been factored in in April, and the current residents unemployment rate remains lower than previous crises. The wildcard here is whether significant further worsening is expected in the labour market into 2H 2020.
- Thus, we are not expecting a sea-change in terms of the SGD NEER stance. The weak USD and resilient RMB have opened up further the downside room for the USD-SGD. **Expect the pair to be flexing against the 1.3600 support. A breach of that level will open up a path lower towards 1.3450/00.**




Source: Bloomberg, OCBC

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