

FX Asia Fortnightly

Treading Cautiously

Treading Cautiously

ASEAN FX is likely to trade cautiously ahead as external events continue to serve as guide posts. Looming US tariffs on USD200bn of Chinese exports, ongoing market angst over EMs, and trade talks between US and its trading partners including Canada, EU and Japan continue to weigh on ASEAN FX. At the same time, markets will also be eyeing CPI data out of US for further clues on Fed rate hike trajectory. A less aggressive rate hike trajectory amid easing trade tensions and EM risks could see the USD drift lower and lift ASEAN FX higher ahead. A slew of China data including CPI, new yuan loans, etc. is also on tap sometime in the week of 10 Sep and data outperformance should be supportive of the yuan and provide some relief to ASEAN FX as well. Escalating EM stresses though could weigh further on the IDR with an overshoot towards 15000-levels cannot be ruled out.

BOJ and BoT meets on 12 Sep and there is little to indicate that either central bank will change direction. BOJ is still a ways from its 2% inflation target, making it unlikely for any policy tightening in the foreseeable horizon. Meanwhile, BoT has the policy space to be patient before beginning the process of normalising policy. BOT is expected to normalise policy only in 4Q.

Our in-house model implies that SGD NEER is trading 0.72% above the implied midpoint of 1.3851, suggesting it is on the stronger side of the SGD vs. other trading partner currencies.

IDR Weakness Could Persist For A While Longer

ASEAN FX was put under pressure by contagion concerns from EM stresses in the past week triggered by crises in Turkey, Argentina and South Africa. Concerns that more EMs could blow-up could lead to further pullback in funds and exacerbate the outflows from EMs. In particular, the IDR was the worst hit in ASEAN, falling around 2.1% since 28 Aug. The IDR's vulnerability was due to the country's twin deficits, large foreign holding of its domestic assets and dependence on external sources for funding. Aside from macro-fundamentals, various market indicators also suggest that the IDR remains under pressure. The rise in Indonesian CDS by about 30bp since Aug that reflects increase concerns over spillover effects from EM contagion risks, though a credit default event by Indonesia seems unlikely at this point. USDIDR forward points suggest that market is looking for further IDR weakness ahead as reflected in the spike in the forward points since end-Aug. While the spike in the forward points has eased from its recent high (of 339) to 200 at the point of writing, it remains elevated and suggests that downside pressure on the IDR could remain for now. USDIDR 3-month at the money option volatility has spiked to a two-year high of 13.26 on 5 Sep as concerns over spillover from EM risks escalated. When compared to its 5-year average of around 9.5, the contrast is even starker. The USDIDR vols were mostly below its 5-year average for the past year or so. It has now spiked beyond its 5-year average and this signals that the USDIDR could remain supported ahead. Technical chart suggests that risks are still to the upside, though there is a potential for a pullback given overstretched conditions. Resistance is around the 15000-levels. Support around 14650-levels.

Analysts

Saktiandi Supaat
(65) 6320 1379
saktiandi@maybank.com.sg

Leslie Tang
(65) 6320 1378
leslietang@maybank.com.sg

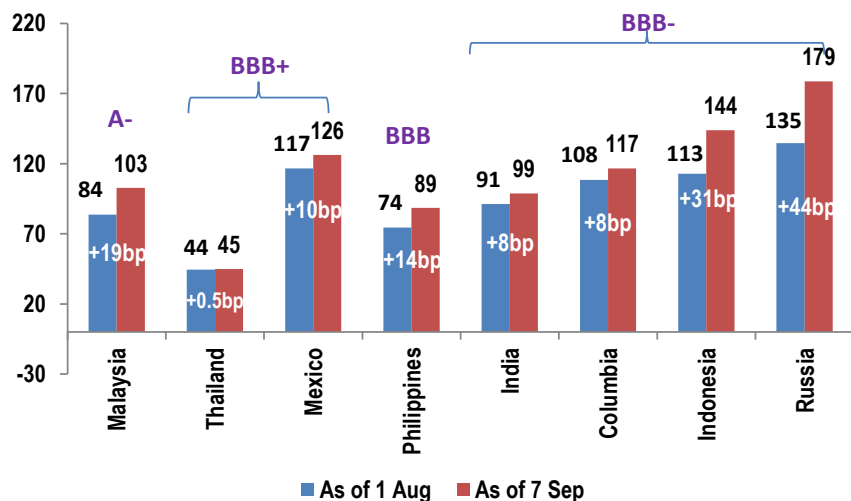
Fiona Lim
(65) 6320 1374
fionalim@maybank.com.sg

Christopher Wong
(65) 6320 1347
wongkl@maybank.com.sg

Flavour of the Week: IDR Weakness Could Persist For A While Longer

- ASEAN FX was put under pressure by contagion concerns from EM stresses in the past week that spurred portfolio outflows. These EM stresses had been triggered first by the crisis in Turkey, followed by Argentina and then South Africa. Concerns that more EMs could blow-up could lead to further pullback in funds and exacerbate the outflows from EMs.
- In particular, the IDR was the worst hit in ASEAN, falling around 2.1% since 28 Aug. The IDR’s vulnerability was due to the country’s twin deficits (2Q current account deficit: 3.04%; 2018 estimate for fiscal deficit: -2.12%), large foreign holding of its domestic assets (around 40%) and dependence on external sources for funding. Aside from macro-fundamentals, various market indicators also suggest that the IDR remains under pressure.
- Risks that contagion fears from EM risks have risen as reflected in rising CDS for Indonesia. But there does not appear to be an imminent risk of a meltdown in Indonesia. The rise in Indonesian CDS by about 30bp since Aug that reflects increase concerns over spillover effects from EM contagion risks (Chart 1). Nevertheless, the rise in CDS though does not appear excessive as compared to the taper tantrum period in 2013 when the premiums had jumped 80bp. A credit default event by Indonesia seems unlikely at this point. At the same time, Indonesia’s CDS may have risen more markedly than its peers in the BBB- credit rating space but is not the worst. Russia’s CDS has risen by even more.

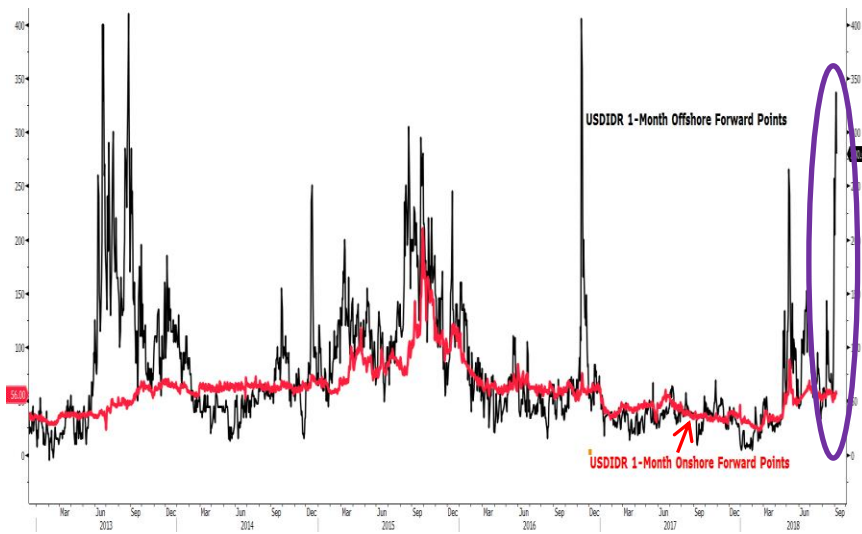
Chart 1: ID 5-Yr CDS Has Climbed Higher Since Aug



Note: (1) Countries are grouped by S&P credit ratings
 (2) Change in CDS between 1 Aug and 7 Sep show within bars
 Source: Bloomberg, Maybank FX Research & Strategy

- USDIDR forward points suggest that market is looking for further IDR weakness ahead as reflected in the spike in the forward points since end-Aug (Chart 2). While the spike in the forward points has eased from its recent high (of 339) to 200 at the point of writing, it remains elevated and suggests that downside pressure on the IDR could remain for now. At the same time, onshore forward points have remained relatively stable around the 56-levels. This divergence between onshore and offshore forward points could reflect ample liquidity onshore and also intervention by the BI to curb IDR volatility.

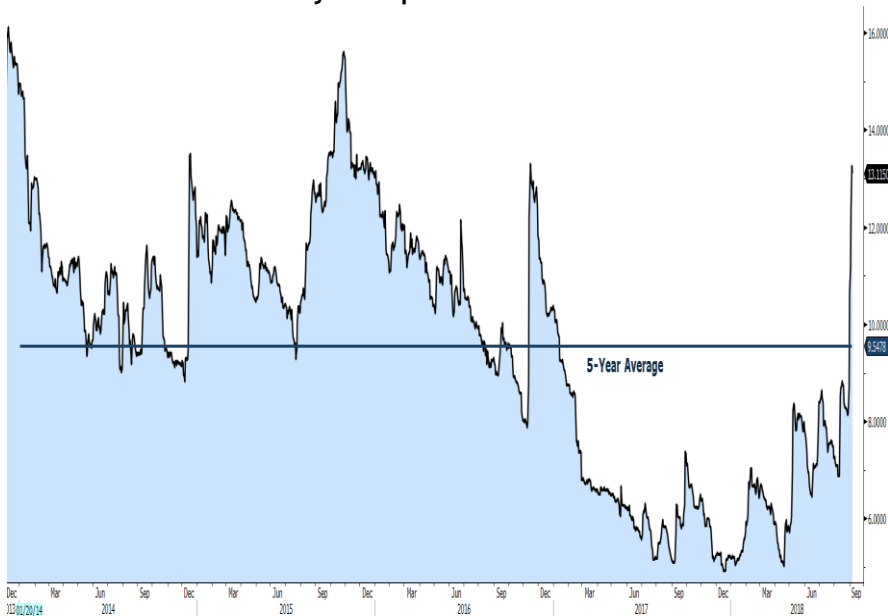
Chart 2: Offshore Forward Point Premium Has Risen



Source: Bloomberg, Maybank FX Research & Strategy

- USDIDR 3-month at the money option volatility has spiked to a two-year high of 13.26 on 5 Sep as concerns over spill-over from EM risks escalated (Chart 3). When compared to its 5-year average of around 9.5, the contrast is even starker. The USDIDR vols were mostly below its 5-year average for the past year or so. It has now spiked beyond its 5-year average and this signals that the USDIDR could remain supported around current levels for now.

Chart 3: USDIDR Volatility Has Spiked



Note: USDIDR volatility is proxied by USDIDR 3 Month at the money option volatility

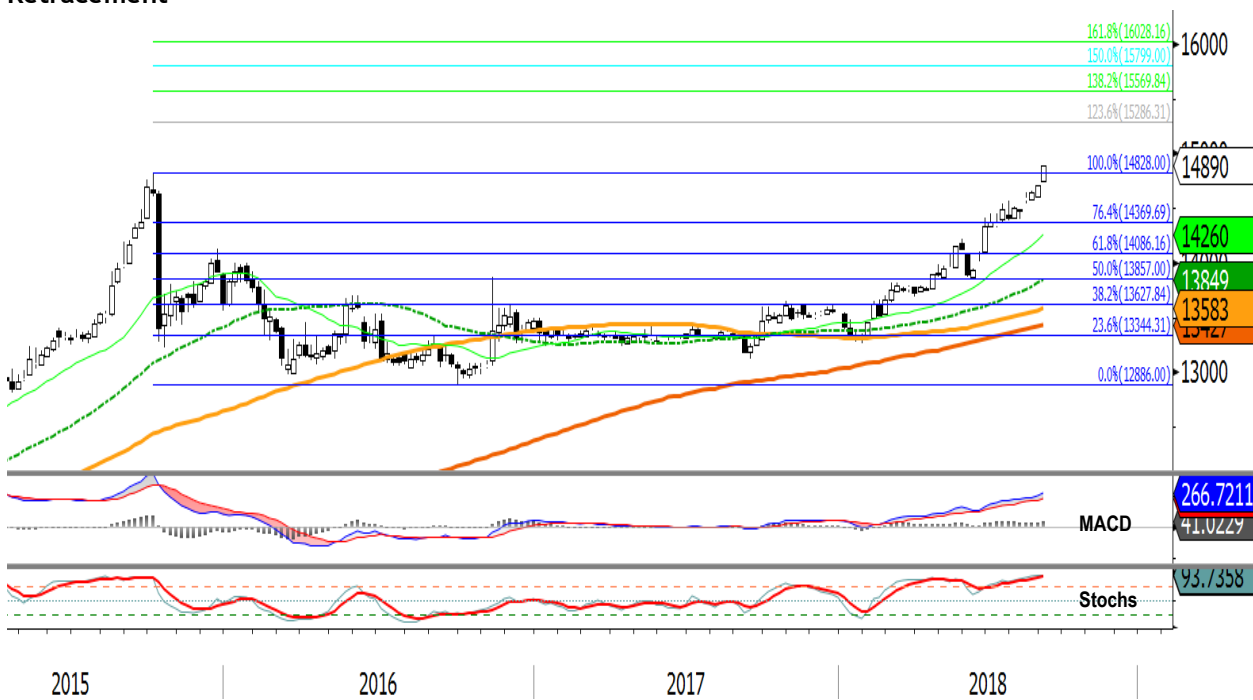
Source: Bloomberg, Maybank FX Research & Strategy

Despite all the concerns over the vulnerability of the IDR, we believe that the measures introduced by the government as well as BI, including a policy of import substitution, the use of biodiesel as an alternative to crude oil, and introduction of overnight index swaps and interest-rate

swaps for hedging by corporates, should help with the current account deficit and temper the sell-off in the IDR. At the same time, expectations that BI could move again on its policy rate, possibly through another unscheduled meeting, should also be supportive of the IDR. Continued intervention in both the FX and bond markets by BI should also help to curb volatility in the IDR and yields given ample foreign exchange reserves. Already we are seeing the forward points coming off and the gap between onshore-offshore forward points could narrow, suggesting that contagion fears from EM stresses have tapered amid softer USD.

Clarity on further risks from EM stresses remains cloudy. Much will depend on policy responses of the central banks and governments of the vulnerable economies. Failure to introduce credible policies could cause further market angst and put EMs under further pressure.

Chart 4: USDIDR Weekly Chart - Upside Bias But Potential For Retracement



Source: Bloomberg, Maybank FX Research & Strategy

Last seen around 14890. USDIDR has risen to levels not seen since the Asian Financial Crisis in 1998. Momentum indicators remain bullish bias on the weekly chart, and stochastics remains in overbought. This suggests risks are still to the upside, though there is a potential for a pullback given overstretched conditions. Resistance is around the 15000-levels. Support around 14650-levels.

Key Data and Events Ahead

	10-16 Sep	17-23 Sep			
Japan	<ul style="list-style-type: none"> Mon: GDP (2Q F), Current Account (Jul) Tue: Tertiary Industry Index (Jul), Machine Tool Orders (Aug F) Wed: - Nil - Thu: PPI (Aug), Core Machine Orders (Jul) Fri: Capacity Utilisation, Industrial Production (Jul) 	<ul style="list-style-type: none"> Mon: Public Holiday Tue: - Nil - Wed: BOJ Policy Balance Rate, Trade (Aug) Thu: LDP Presidency Election Fri: CPI (Aug), Nikkei PMI Mfg (Sep P), All Industry Activity Index (Jul) 			
	China	<ul style="list-style-type: none"> Mon: PPI, CPI (Aug), Money Supply, Aggregate Financing, New Yuan Loans (Aug - due 10-15 Sep) Tue: - Nil - Wed: - Nil - Thu: - Nil - Fri: Retail Sales, Industrial Production, FAI Urban (Aug) 	<ul style="list-style-type: none"> Mon: - Nil - Tue: - Nil - Wed: - Nil - Thu: - Nil - Fri: - Nil - 		
		South Korea	<ul style="list-style-type: none"> Mon: - Nil - Tue: - Nil - Wed: Unemployment Rate (Aug) Thu: - Nil - Fri: - Nil - 	<ul style="list-style-type: none"> Mon: - Nil - Tue: - Nil - Wed: - Nil - Thu: - Nil - Fri: PPI (Aug) 	
			Singapore	<ul style="list-style-type: none"> Mon: - Nil - Tue: - Nil - Wed: Retail Sales (Jul) Thu: - Nil - Fri: - Nil - 	<ul style="list-style-type: none"> Mon: NODX (Aug) Tue: - Nil - Wed: - Nil - Thu: - Nil - Fri: - Nil -
				Malaysia	<ul style="list-style-type: none"> Mon: Public Holiday Tue: Public Holiday Wed: - Nil - Thu: - Nil - Fri: - Nil -
Indonesia					<ul style="list-style-type: none"> Mon: - Nil - Tue: Public Holiday Wed: - Nil - Thu: - Nil - Fri: - Nil -
	Philippines				<ul style="list-style-type: none"> Mon: - Nil - Tue: Trade (Jul) Wed: - Nil - Thu: - Nil - Fri: - Nil -
		Thailand			<ul style="list-style-type: none"> Mon: - Nil - Tue: - Nil - Wed: - Nil - Thu: - Nil - Fri: Foreign Reserves (7 Sep)
			India		<ul style="list-style-type: none"> Mon: - Nil - Tue: - Nil - Wed: CPI (Aug), Industrial Production (Jul), Trade (Aug - due 12-15 Sep) Thu: - Nil - Fri: Wholesale Prices (Aug), Public Holiday
				Vietnam	<ul style="list-style-type: none"> Mon: - Nil - Tue: - Nil - Wed: - Nil - Thu: - Nil - Fri: - Nil -

DISCLAIMER

This report is for information purposes only and under no circumstances is it to be considered or intended as an offer to sell or a solicitation of an offer to buy the securities or financial instruments referred to herein, or an offer or solicitation to any person to enter into any transaction or adopt any investment strategy. Investors should note that income from such securities or financial instruments, if any, may fluctuate and that each security's or financial instrument's price or value may rise or fall. Accordingly, investors may receive back less than originally invested. Past performance is not necessarily a guide to future performance. This report is not intended to provide personal investment advice and does not take into account the specific investment objectives, the financial situation and the particular needs of persons who may receive or read this report. Investors should therefore seek financial, legal and other advice regarding the appropriateness of investing in any securities and/or financial instruments or the investment strategies discussed or recommended in this report.

The information contained herein has been obtained from sources believed to be reliable but such sources have not been independently verified by Malayan Banking Berhad and/or its affiliates and related corporations (collectively, "Maybank") and consequently no representation is made as to the accuracy or completeness of this report by Maybank and it should not be relied upon as such. Accordingly, no liability can be accepted for any direct, indirect or consequential losses or damages that may arise from the use or reliance of this report. Maybank and its officers, directors, associates, connected parties and/or employees may from time to time have positions or be materially interested in the securities and/or financial instruments referred to herein and may further act as market maker or have assumed an underwriting commitment or deal with such securities and/or financial instruments and may also perform or seek to perform investment banking, advisory and other services for or relating to those companies whose securities are mentioned in this report. Any information or opinions or recommendations contained herein are subject to change at any time, without prior notice.

This report may contain forward looking statements which are often but not always identified by the use of words such as "anticipate", "believe", "estimate", "intend", "plan", "expect", "forecast", "predict" and "project" and statements that an event or result "may", "will", "can", "should", "could" or "might" occur or be achieved and other similar expressions. Such forward looking statements are based on assumptions made and information currently available to us and are subject to certain risks and uncertainties that could cause the actual results to differ materially from those expressed in any forward looking statements. Readers are cautioned not to place undue relevance on these forward looking statements. Maybank expressly disclaims any obligation to update or revise any such forward looking statements to reflect new information, events or circumstances after the date of this publication or to reflect the occurrence of unanticipated events.

This report is prepared for the use of Maybank's clients and may not be reproduced, altered in any way, transmitted to, copied or distributed to any other party in whole or in part in any form or manner without the prior express written consent of Maybank. Maybank accepts no liability whatsoever for the actions of third parties in this respect.

This report is not directed to or intended for distribution to or use by any person or entity who is a citizen or resident of or located in any locality, state, country or other jurisdiction where such distribution, publication, availability or use would be contrary to law or regulation.

Published by:



Malayan Banking Berhad
(Incorporated in Malaysia)

Saktiandi Supaat
Head, FX Research
saktiandi@maybank.com.sg
(+65) 63201379

Christopher Wong
Senior FX Strategist
wongkl@maybank.com.sg
(+65) 63201347

Fiona Lim
Senior FX Strategist
Fionalim@maybank.com.sg
(+65) 63201374

Leslie Tang
Senior FX Strategist
leslietang@maybank.com.sg
(+65) 63201378