FX Flash

MYR - Political Uncertainty Still In the Price

Confluence of Covid and Domestic Political Concerns

MYR has softened by more than 3% since week of 20 Jan, before Covid-19 concerns took over global headlines. In the past week, some domestic political uncertainty—resignation of Dr Mahathir as PM, overturning of the Pakatan Harapan (PH) coalition government—may have added to Covid worries as well.

Downward Retracement (USDMYR) Due to US Rate Expectations

A comparison with the 2018 GE episode shows that softness in MYR came in a lot faster last week as developments were unexpected, but subsequent recovery vs. USD also set in very quickly from mid last week. Nonetheless, a large part of the "recovery" could be due to softness in USD strength as markets priced in higher likelihoods of more Fed rate cuts this year.

These moves further highlight the complexity of the current situation for MYR, as the shifting geographical impact of Covid (AxJ vs DM) interacts with monetary policy expectations (Fed being key driver) as well as domestic political uncertainty to drive outturns.

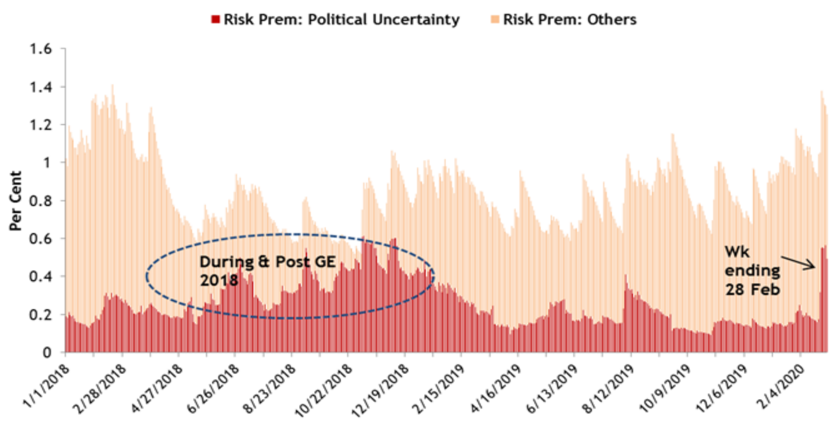
MYR Political Uncertainty Risk Premium Rose Last Week

We note that despite some broad moderation of the drag in Asian FX risk sentiments due to Covid last week (i.e., AxJ broadly performed better), estimated MYR risk premium was higher, and mainly on a spike in political uncertainty risk premium. This component was back near highs seen sporadically during and post GE 2018, and accounted for slightly less than half of the total risk premium last week.

We refrain from second-guessing how events might play out from here, but postulate that further, sharp spikes in USDMYR due to political uncertainty alone might be less likely. End-Q1 and end-Q4 forecasts for USDMYR are at 4.16 and 4.12.

Looking at technicals, daily momentum and RSI are showing a downward bias and a move lower to close the runaway gap in USDMYR is not ruled out. Immediate support at 4.1980, before 4.1705 and 4.1560. Resistance at 4.23, 4.2435 levels.

<u>MYR Risk Premium Stepped Up in Week of 24-28 Feb</u>



Source: Bloomberg, Maybank FX Research & Strategy Estimates

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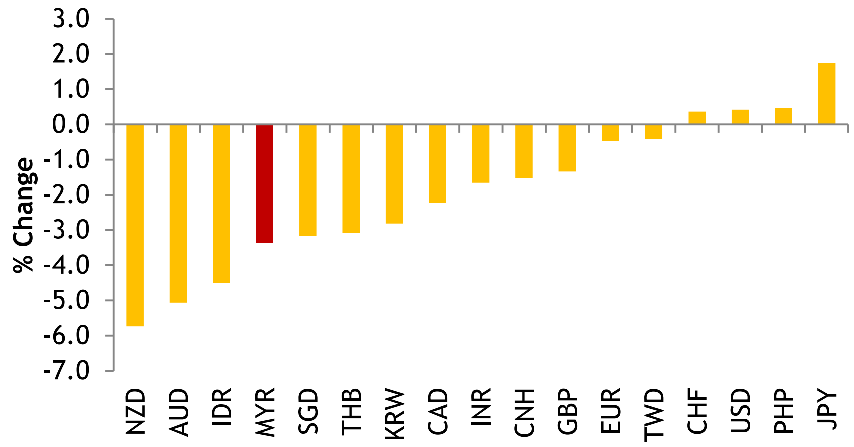
MYR Softness on Covid, Political Uncertainty

MYR has softened by more than 3% since week of 20 Jan, before Covid-19 concerns took over global headlines. In the past week, some domestic political uncertainty—resignation of Dr Mahathir as PM, overturning of the Pakatan Harapan (PH) coalition government—may have added to Covid worries as well.

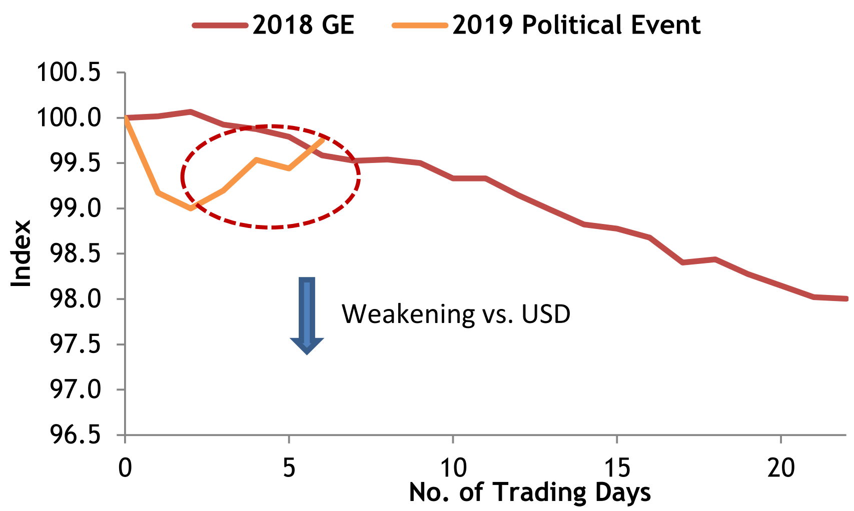
Change in FX (vs. USD) From 20 Jan to 2 Mar



Source: *Bloomberg, Maybank FX Research & Strategy Estimates*

A comparison with the 2018 GE shows that softness in MYR came in a lot faster over 24-25 Feb as developments were unexpected, but subsequent recovery vs. USD also set in very quickly.

MYR Strength: 2018 GE vs. 2019 Political Event



Source: *Bloomberg, Maybank FX Research & Strategy Estimates*
Note: “Day 0” for 2018 GE is on 6 Apr, (announcement of intention to dissolve the Malaysian Parliament), while that for 2019 political event is on 21 Feb, the last trading day before signs of political uncertainty emerged over the 22-23 Feb weekend.

Nonetheless, a large part of the “recovery” (dotted lines) was likely **due to broad softness in USD strength as markets priced in higher likelihoods of more Fed rate cuts this year**. Futures markets are now pricing in 3 Fed cuts by the end of the year, vs. less than 2 cuts indicated by pricing in early Feb.

These moves further highlight the complexity of the current situation for MYR, when the asymmetric geographical impact of Covid (AxJ vs DM) interacts with monetary policy expectations (Fed being key driver) as well as domestic political uncertainty to drive outturns.

Quick GARCH-M Model to Assess Shifts in Risk Premium

To estimate the extent of recent changes in MYR risk premium, we estimate a quick GARCH-M model of the form:

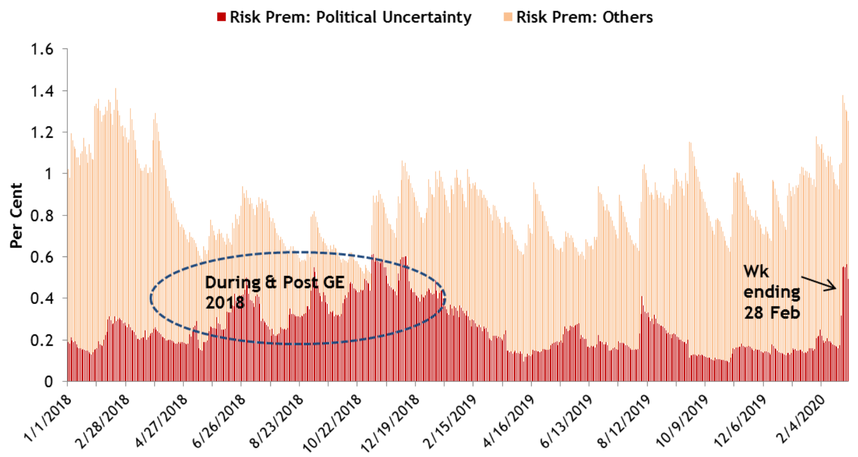
$$MYR_t = f(SQRT(GARCH), DXY_t),$$

where error term ~ GARCH (1,1).

Model uses daily data and is estimated in changes. MYR refers to the USDMYR pair. DXY refers to broad dollar index and is taken as a control variable. Risk premium for MYR is extracted from the time-varying GARCH term in the estimated model and converted to standard deviation (in % returns) form below.

We also proceed to estimate the risk premium component attributable to political uncertainty. This is achieved by including Malaysian 5 Yr CSD spreads as a proxy control for political risks in the GARCH-M model above.

MYR Risk Premium (Pol. Uncertainty) Stepped Up in Week of 24-28 Feb



Source: *Bloomberg, Maybank FX Research & Strategy Estimates*

We note that despite some broad moderation of the drag in Asian FX risk sentiments due to Covid last week (i.e., AxJ broadly performed better), estimated MYR risk premium was higher, and mainly on a spike in political uncertainty risk. This component was back near highs seen sporadically during and post GE 2018, and accounted for slightly less than half of overall risk premium last week.

We refrain from second-guessing how events might play out from here, but postulate that further, sharp spikes in USDMYR due to political uncertainty alone might be less likely.

Summary of Outlook

Forecast	1Q 2020	2Q 2020	3Q 2020	4Q 2020
USDMYR	4.1600	4.1500	4.1200	4.1200
SGDMYR	3.0145	3.0292	3.0294	3.0519

MYR could see some downside pressures in the interim on the back of Covid-19 concerns and political uncertainty, but we note that political developments remain fluid at this point.

We had shifted our USDMYR 1Q forecast higher from 4.12 to 4.16 during our monthly review end-Feb (see report here), but broadly still look for some recovery in MYR vs. USD given mixed US growth data and increasing calls for Fed rate cuts going forward.

A MYR20bn stimulus package was also unveiled to deal with the clear and present downsides associated with the Covid-19 outbreak, consisting of three strategies and almost 40 specific measures mostly w.e.f. Mar/Apr 2020. These are targeted at mitigating cash flow concerns for corporates in tourism, travel and retail sectors, and stimulating demand for travel and tourism. Disposable income will also be boosted by up to MYR10bn by cutting employees' minimum monthly contribution to the Employees Provident Fund. Lastly, there is a focus to promote both public and private investments by accelerating development projects and capex. (For more details, refer to our Chief Economist's Suhaimi's piece here.) This could support sentiments to some extent in the interim.

Our house view expects BNM to stand pat at 2.75% at its MPC later today. Monetary conditions have eased considerably as weaker MYR adds to the monetary stimulus: (1) 50bps cut in OPR (in Jan 2020 and May 2019) and (2) 50bps cut to SRR in Nov 2019 while economic package announced last Thu should help to deal with COVID-19. Our Economists however do not rule out another 25bps OPR cut if COVID-19 outbreak is prolonged and worsened, leading to longer and larger negative economic impact, hence the revised official 2020 real GDP growth forecast range of 3.2%-4.2%. Key to BNM's OPR decision are updates on COVID-19 and economic indicators over the next few weeks/months to give more clarity on the outbreak's duration and its economic impact. MPC meeting on 4-5 May 2020 is the one to watch.

For 2020 as a whole, MYR fundamentals also remain well anchored by sustained current account surplus, stable FX reserves to retained imports & short-term debt. We expect the monetary and fiscal support from OPR cuts and government development & infrastructure projects, as well as growth supportive Budget 2020 measures to structurally revive capex and boost private consumption as Covid-19 and political concerns ease.

Technicals

USDMYR: Weekly chart - Chance For Pullback

Source: Bloomberg

USDMYR eased off recent highs starting this week but remains near multi-month highs. Pair was last seen at 4.2030 levels. Bullish momentum on weekly chart remains intact while RSI is showing signs of turning lower. Daily momentum and RSI (not shown here) are showing a downward bias.

A move lower to close the runaway gap is not ruled out. Immediate support at 4.1980 (23.6% fibo retracement of 2020 low to high) before 4.1705 (38.2% fibo) and 4.1560 (200 DMA). Resistance at 4.23, 4.2435 levels.

SGDMYR: Daily chart - Consolidate

Source: Bloomberg

SGDMYR rebounded over the past week, consistent with our call for rebound play. Cross was last seen at 3.0220 levels.

Bullish momentum on daily chart shows signs of pause while RSI has eased. A temporary pause in recent run-up is likely. Support at 3.0140 (50 DMA), 3 levels and 2.9970 (21 DMA). Resistance at 3.0250 levels (50% fibo retracement of Dec high to 2020 low) before 3.0360 levels (100, 200 DMAs). We look for 3.0120 – 3.0350 range this week, within wider perimeter of 3 – 3.05 range.

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