FX Flash

IDR - Firing on All Cylinders

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Sharp Shifts in Global Risk Aversion Tanked IDR in Late Feb

IDR has seen sharp moves recently in the last one and a-half weeks. One factor leading to the sharp IDR softness in late Feb was the shift in global risk sentiments on Covid contagion, especially as the number of confirmed cases accelerated in DM countries. The resulting withdrawal of funds from riskier markets in favour of safe haven assets dented sentiments in EM markets, including Indonesia.

At one point, USDIDR touched above 14,400, before coming back down towards 14,100. On a NEER basis, IDR is estimated to have fallen by around -3.3% during Feb, before recovering by around 0.8% in the first few days of March.

BI's 5 Measures; 2 Tranches of Fiscal Stimulus

To curb the volatility in financial markets, BI introduced a series of 5 measures on 2 Mar (detailed in main report). We think that intensifying triple intervention policy shows BI's determination in managing any IDR weakness deemed not in line with underlying macro fundamentals. Lowering FX reserve requirements for commercial banks from 8% to 4% could aid in ensuring sufficient liquidity in the economy, especially in preventing shortage of USD.

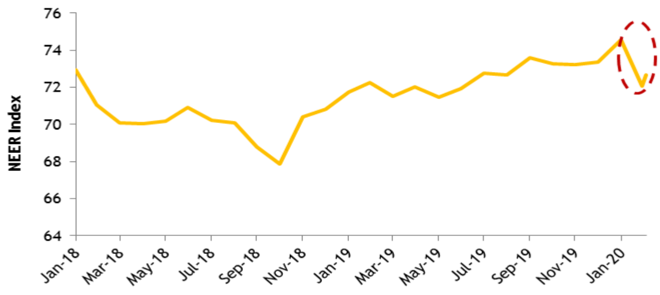
A US$742mn stimulus package was also introduced last week, consisting of subsidies, tax cuts, accelerated cash-transfers and unemployment benefit programs in Indonesia's major tourist destinations. Further, it was just announced that a new tranche of fiscal measures which would be "sizable" and "bigger" than the first, is currently in the works.

Maintain Forecasts for Now, But Flag Risks

Forecasts are kept unchanged from Jan for now (end-2020 USDIDR at 13,400), given the tendency for volatile swings in IDR amid bout of Covid-led uncertainty, and as Indonesian authorities fire on all cylinders to calm markets. Nonetheless, we are cautious of possibility of Covid contagion accelerating in Indonesia and its impact on sentiments.

Technical analysis suggests that while momentum on USDIDR pair is still bullish, there are signs of turning from overbought conditions. Recent high of 14400 could be a key resistance level. Support at 14,000, before 13,800-13,860 (50, 21 DMAs).

<u>IDR NEER Slipped in Late Feb But Is Showing Signs of Recovering</u>



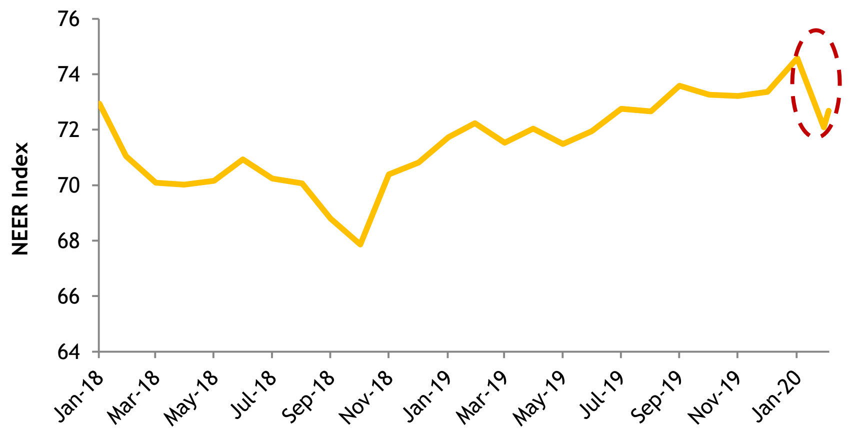
Source: Bloomberg, Maybank FX Research & Strategy Estimates

IDR Volatile on Sharp Shifts in Global Risk Aversion

IDR has seen sharp moves recently in the last one and a-half weeks. At one point, USDIDR touched above 14,400, before coming back down rapidly towards 14,100.

Currencies have been generally quite volatile since concerns of Covid-19 took over global headlines. In this instance, it would be more useful to look at FX moves on a trade-weighted basis, i.e., nominal effective exchange rate (NEER) basis.

Nominal Effective Exchange Rate (NEER) for IDR

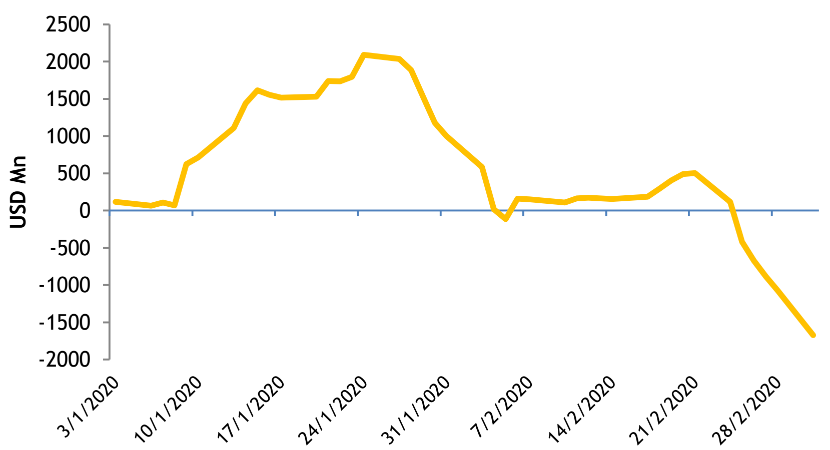


Source: BIS, Maybank FX Research & Strategy Estimates
Note: Data from BIS has last monthly data point at 31 Jan 2020. Figures afterwards are estimated.

We note that IDR NEER has fallen by around -3.3% during Feb (mostly in late Feb), before recovering by around 0.8% in the first few days of March.

One factor leading to the sharp decline in late Feb was the shift in global risk sentiments on Covid contagion, especially as the number of confirmed cases accelerated in DM countries. The resulting withdrawal of funds from riskier markets in favour of safe haven assets such as USTs, gold and yen, dented sentiments in EM markets, including Indonesia.

Flows in Indonesian Government Securities (Cumulative From 3 Jan 2020)



Source: Bloomberg, Maybank FX Research & Strategy Estimates

As seen in the above chart, despite relatively resilient outcomes in early Feb, outflows from Indonesian government bonds accelerated from week of 24 Feb, as flight-to-quality behavior materialized. As a result net outflow in Feb alone (mtd) was slightly more than US$2bn.

Indonesian 10 year government bond yields reached near 7.0% at one point before slipping back towards the 6.5% mark.

Indonesia Authorities Firing on All Cylinders

To curb the volatility in financial markets, BI introduced a series of 5 measures on 2 Mar.

Table of BI Measures Introduced on 2 Mar 2020

	Measures
1	**Intensify triple intervention policy** to ensure IDR exchange rates move in line with the currency's fundamental value and market mechanisms. To that end, Bank Indonesia will optimise its intervention strategy in the DNDF market, spot market and SBN market in order to minimise the risk of increasing rupiah exchange rate volatility.
2	**Lower the FX reserve requirements for commercial banks from 8% to 4%**, effective 16th March 2020, which will increase FX liquidity in the banking industry by around USD3.2 billion and simultaneously alleviate foreign exchange market pressures.
3	**Lower the IDR reserve requirements by 50bps for banks financing export-import activity** in coordination with the Government. Effective from 1st April 2020 for a period of nine months before a further review, this policy is expected to facilitate export-import activity through lower costs/fees.
4	Expand the range of underlying transactions available to foreign investors in order to provide alternative hedging instruments against IDR holdings.
5	Reaffirm that global investors can utilise global and domestic custodian banks to conduct investment activity in Indonesia.

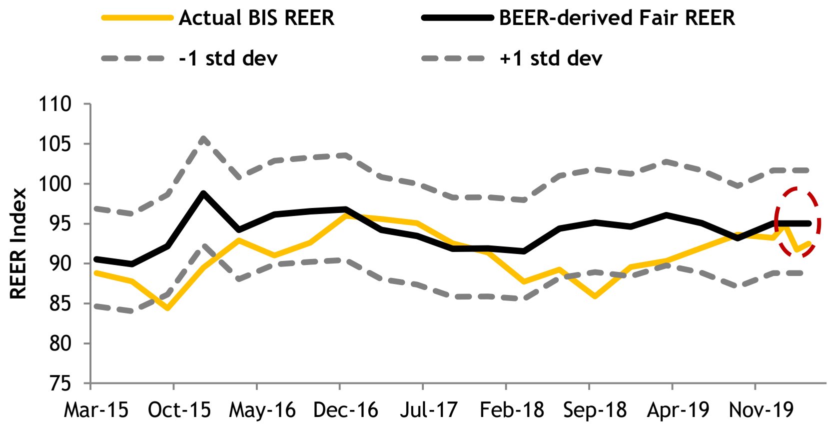
Source: Bank Indonesia

We think that measure 1) shows BI's determination in capping any IDR weakness deemed not in line with underlying macro fundamentals. Among the 5 measures, this could be the most effective in serving to sooth interim market sentiments.

Measures 2) and 3) are important in ensuring sufficient liquidity in the economy, especially in preventing shortage of USD.

Measures 4) and 5) will work broadly to improve financial intermediation efficiency and are part of structural improvements to financial market operations.

IDR REER Fair Value Monitor



Source: BIS, CEIC, Bloomberg, Maybank FX Research & Strategy Estimates
Note: BEER-derived fair value is from panel dynamic ordinary least squares estimation (panel DOLS), incorporating variables such as net foreign assets, trade exposure, productivity differentials with trading partners and real interest rate differentials with trading partners.

A quick look at fair value estimates show that actual REER was moving away from estimated fair value (with the extent of mis-alignment at around -3.5% end-Feb), before starting to correct in Mar as BI rolled out the above measures.

On net, the quick and well-communicated responses of BI recently seem to imply that they are still on top of the current situation. Closer policy coordination is also key and in this context, it's a good sign that Indonesia is firing on the fiscal cylinders as well.

A US$742mn stimulus package introduced last week will consist of subsidies, tax cuts, accelerated cash-transfers and unemployment benefit programs in Indonesia's major tourist destinations.

Further, it was just announced that a new tranche of fiscal measures which would be “sizable” and “bigger” than the first, is currently in the works. These will consist of 8 packages in total, 4 stimulus packages related to fiscal policy and 4 packages related to trade procedures to combat the Covid-19 drag on the economy. There also appear to be discussions on potential easing of corporate tax and import duty requirements to ensure sufficient supply of raw materials.

Summary of Outlook

Forecast	1Q 2020	2Q 2020	3Q 2020	4Q 2020
USDIDR	13,700	13,600	13,500	13,400

Forecasts are kept unchanged from Jan for now, given the tendency for volatile swings in IDR amid bout of Covid-led uncertainty, but we flag clear upside risks to the USDIDR pair (i.e., IDR weakening). Covid-19 impact would include modest short-term disruptions to domestic production due to drying up of raw materials and intermediate goods from China, and delays to various infrastructure projects. With confirmed patients (now at 2) in Indonesia, any escalation in contagion, especially if domestic health security measures are deemed to be ill-prepared, would likely also dent sentiments.

Nonetheless, support from above financial and fiscal measures should work to mitigate drags. If Covid-19 fears ease subsequently in 2H, optimism on domestic omnibus bills on tax and job creation would also be helpful for IDR confidence.

We expect monetary easing by BI to continue as both domestic and global economic outturns would likely be more subdued this year. After the previous rate cut on 20 Feb (by 25bps to 4.75%), another rate cut could be on the table before end 1H. Overall magnitude of cuts this year will depend on eventual extent of damage wrought by Covid-19, but is still expected to be more modest than the 100bps of rate cuts last year. This could help to maintain attractive yield differentials vs. DMs, especially with signs of aggressive rate cuts in the US (emergency 50bps cut in Fed Funds Rate on 3 Mar) and carry appeal may still be intact.

Technicals

USDIDR: Bullish But Overbought

Source: Bloomberg

USDIDR pair last seen at 14160. Pair has seen significant upward gains recently, breaking past the 100 and 200 DMAs, before paring gains. It remains above the 200-DMA for now.

Bullish momentum on daily chart is intact but stochastics are showing signs of turning from overbought conditions. Support at 14,000, before 13,800-13,860 (50, 21 DMAs). We look to recent high of 14400 to be a potentially firm resistance level.

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Published by:

Malayan Banking Berhad
(Incorporated in Malaysia)

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