FX Insight

(AXJ) Phoenix from the Ashes

Positioning for Eventual Recovery

Equities and other risk assets have seen a near 30% rally from their March-lows as infection rates show signs of peaking in key epi-centers. Within Asia Pacific, Taiwan, Australia, New Zealand, China and South Korea seem to have gotten their respective outbreaks well under control, but the outbreak situations in other countries such as India and Indonesia are less certain. In Singapore, foreign workers' dormitories became the weakest link and saw a multi-fold surge in new cases while local cases stabilize.

While regional countries are on different parts of their epidemic curves and equity valuations may look a bit stretched vs. the incoming COVID toll on activity and jobs in 2Q, we think that it may be timely to consider positioning for an eventual market recovery.

2-Pronged Approach on Which FX to Ride the Recovery

In this report, we adopt a composite approach in setting up a framework to assess which FX could benefit more in the event of a more decisive recovery from COVID-19 pandemic, taking into account:

(1) Market parameters to assess current state of Value, Sovereign Risk and Carry in individual FX;

(2) A relook at underlying and emerging trends that proxy FX could ride on in the "new normal" post-COVID-19.

Our FX Bias - Long North Asian FX - KRW, TWD, CNH

Looking at aggregate table below, our bias is for KRW, TWD and CNY to outperform riding on resumption of tech recovery trend and China rebound. One point to note is that the value metric (using REER relative to its historical as a proxy) suggests that KRW and SGD may see more room for gains. TW handled COVID-19 crisis well and TWD is well positioned to fully take advantage of resumption of the tech rebound.

IDR and MYR could regain appeal if carry and value pans out well over the next 3 months. For THB, the timing of tourism recovery is key, as re-emergence of tourist flows may take longer compared to the SARS episode.

	Market Parameters (Percentiles)			Trend Proxy (Betas)	
	Value	Risk	Carry	Resumption of Tech Recovery	China Activity Rebound
CNY	71%	11%	98%	0.012	0.156
KRW	5%	14%	98%	0.167	-0.117
TWD	95%	-	100%	0.023	0.079
SGD	2%	-	90%	0.018	0.143
MYR	30%	48%	98%	-0.161	-0.221
IDR	21%	87%	98%	-0.280	-0.265
THB	76%	56%	94%	0.017	0.075
PHP	86%	59%	92%	-0.081	-0.082

Note: "Value" is based on REER, "Risk" is based on CDS Spreads and "Carry" is based on 10Y Bond Yield Differentials vs. the US. Interpretation of the table: For market parameters, we utilize the concept of percentile rankings. A lower percentile would indicate that the current value is relatively "low" as compared to its "norm", which we used a 5-year history. For example in the case of value, the current SGD REER is perceived to be low vs. its own 5-year history. We see attractiveness in currencies perceived to have lower percentile (blue) for value and risk and higher percentile for carry (coded blue). For Beta sensitivity on trend proxy, higher beta means the AXJ is more sensitive to the trend proxy and is shaded in blue while negative beta means the AXJ's sensitivity is inversely correlated to the trend proxy and is shaded in red. We prefer shades of blue to capture the trend.
Source: Maybank FX Research & Strategy Estimates

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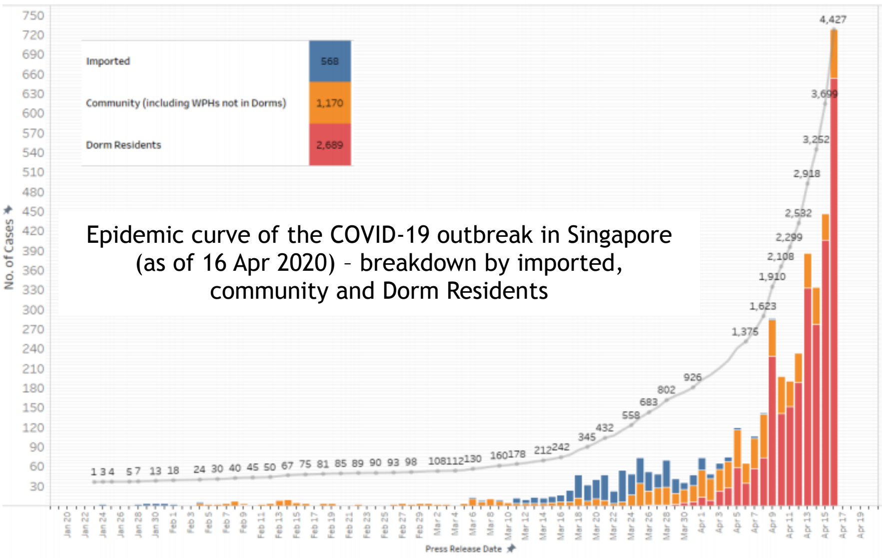
COVID-19 Epidemic Curve Peaking at Differing Pace

We see new cases peaking globally but still at elevated levels and at differing pace. Within Asia Pacific, Taiwan, Australia, New Zealand, China and South Korea seems to have gotten their respective outbreaks well under control, but the outbreak situations in other countries such as India and Indonesia are less certain. In Singapore, foreign workers' dormitories became the weakest link and saw a multi-fold surge in new cases while local cases stabilize.

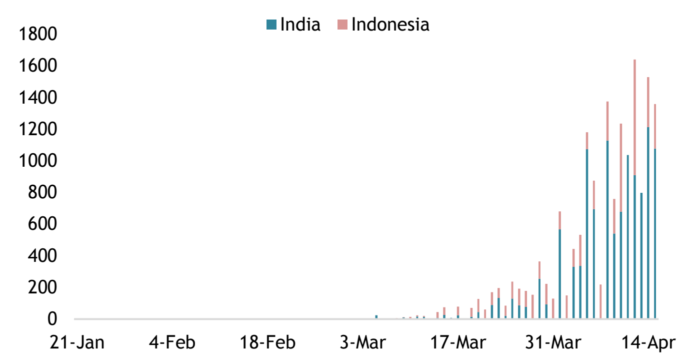
SG: Surge in Cases within Foreign Worker Dormitories while Community Infections Stabilize



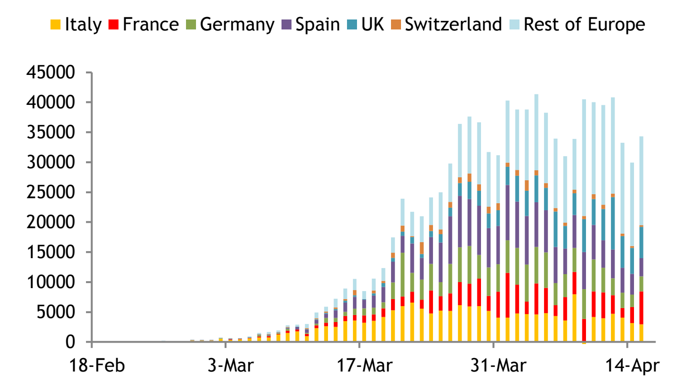
Source: Ministry of Health Singapore *Situation Report 16 Apr 2020*

For India, despite the lockdown, hundreds of thousands of migrant workers left the cities on foot back to their villages due to a lack of work in the cities, likely spreading the virus across the country. For Indonesia, the government has not curbed the yearly *Mudik* and millions of homebound people might bring Covid-19 with them. The low number of tests conducted so far (last check at 99/mn of population as of 15 Apr) suggests that there are still likely significant numbers of undetected Covid cases in the community. These developments underscore the multi-speed nature of the COVID-19 containment globally.

Daily New Infections Are Still Elevated in India, Indonesia



Infections in Europe Seem to Have Slowed in Europe



Source: WHO, Maybank FX Research & Strategy

Policy Measures - Evaluating Effectiveness

1) Lockdowns, Social Distancing in Attempt to Contain

Economic Pain for Mortality Gain

Since COVID-19 went global, countries dealt with the crisis at hand in variants. What was common amongst sovereigns was the multi-pronged approach - i) enforcing social distancing measures, ii) ramping up diagnostic testing capability and iii) gargantuan fiscal support to tide companies and households over, and unprecedented central bank policies to ensure normal market functioning and lower financing rates. Dramatic central bank and government actions are stop-gap measures to ensure most stay afloat in this crisis period, while being able to test and diagnose COVID-19 readily and ensuring physical distancing are key factors to limiting the spread and mortality rate. This would eventually lower the adverse impact via supply and demand channels that could linger beyond the pandemic crisis.

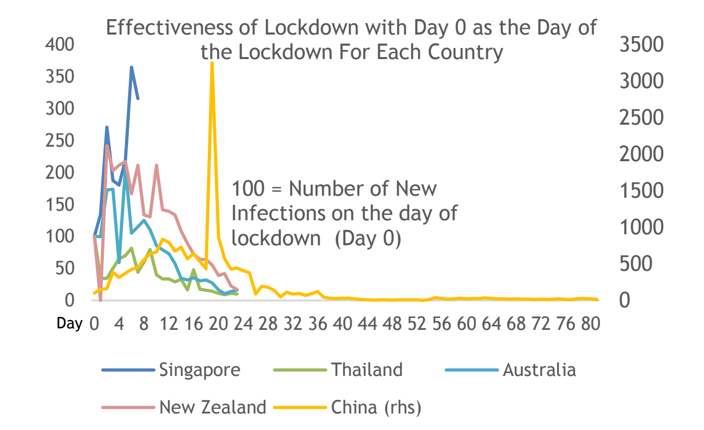
Lockdowns - The More Extreme Form of Social Distancing

Being the first to be hit, China set an example by locking down Wuhan on 23 Jan—the epicenter and supposed origin of COVID-19. China also proceeded to lock down at least 48 cities and 4 provinces, effectively freezing the movements of an estimated 500-800mn people in China.

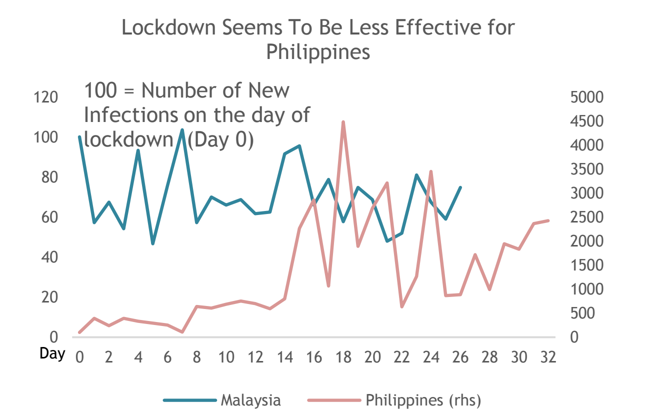
Other countries that also implemented mass quarantines are Denmark, EL Salvador, France, Ireland, Italy, New Zealand, Poland, Spain, the UK and the US. Nearer to home, Singapore is in the midst of its "circuit breaker" (a partial lockdown where non-essential services are halted), Malaysia is already into its 5th week of the Movement Control Order. In Philippines, President Duterte put Luzon under Enhanced Community Quarantine. In Thailand, Bangkok is in partial shutdown with only supermarkets, pharmacies and takeaway restaurants allowed to remain open.

Movement restrictions are aggressive and have been rather effective for certain countries including Australia, New Zealand, China and to some extent, Thailand. The impact is less certain for Malaysia and apparently yet to show effectiveness for Philippines.

Daily Infections Typically Peak Within the First Two Weeks



The Luzon Quarantine in Philippines Show Less Favourable Outcome



Source: WHO, Maybank FX Research & Strategy

Exemplary Countries Which Did Not Require Severe Movement Restrictions

However, there are also countries which did not seem to require lockdowns and yet managed to get COVID-19 under control. These exemplary countries are Taiwan and South Korea. While Taiwan enjoyed the luxury of being able to produce enough masks for their own residents (albeit not without rationing), another key reason for their success is their speedy social distancing recommendation as well as quick surveillance.

South Korea had a sudden spike in cases due to an infamous "Patient 31" who participated in gatherings at the Shincheonji Church of Jesus in Daegu. However, due to their aggressive contact tracing using credit cards, CCTV footages as well as the use of apps that alert users of any Covid-19 patient within a 100m radius, the country was also able to get a grip on the outbreak. A key defining ability is its capability to diagnose widely. Tests were almost freely available for anyone (subsidized depending on the eligibility of the person) and allowed rapid detections and isolation of confirmed cases, limiting the spread.

2) Bazooka Policy Responses Calmed Nerves

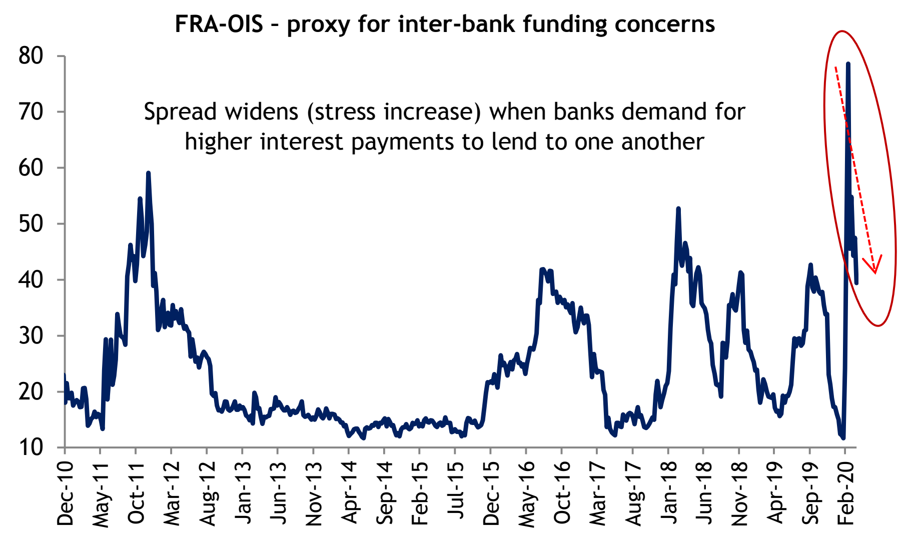
Looking back, policymakers' rapid and multiple responses via fiscal stimulus, monetary easing and credit support have been effective in alleviating financial market stresses and to some extent, the fiscal support is targeted at relieving household/corporate financial distress, saving jobs and protecting livelihoods. We briefly discussed some of the recent monetary responses below.

Central bankers around the world have unprecedentedly doubled down on their stimulus in an attempt to calm markets. For instance, RBA and RBNZ cut rates to historical low and launched bond purchase program for the first time, ECB unleashed 2 sets of stimulus measures including EUR750bn bond purchase program, more favorable terms on TLTROs while Fed cut interest rate by 150bps in a space of less than 2 weeks and relaunched asset purchase program of US$700bn and thereafter announced unlimited QE, as well as unprecedented support for US corporate bond markets. **And even with bazooka stimulus announced, policymakers continue to show a willingness to do more**.

Just before the Easter long weekend, the Fed announced decisions to (1) **purchase debt from sub-investment-grade or "junk" rated companies**, including ETFs holding such debt; (2) expand another facility to begin to buy highly rated new issues of CLOs and commercial MBS; (3) purchase $500bn of short term notes directly from states, counties and cities; (4) $600bn "Main Street Lending Fund" to offer support for SMEs who will have to pay between 2.5% - 4% above SOFR (currently at zero). Banks will make loans to such SMEs for a 4-year period. Principal and interests will be deferred for the first year. Banks can sell up to 95% of the loan to Fed's new SPV. On point 1, Fed had earlier announced plans (23 Mar) to purchase IG corporate bonds in secondary markets including ETFs but had now expanded to include HY debt. Fed's intent is to expand the pool of credit due to "fallen angels" as about $560bn of IG corporate bonds have been downgraded in the past month. (See here for earlier report on policy responses).

On net, the steps taken by central bankers to alleviate funding and liquidity stresses and to rein in both short term borrowing costs and long term yields have somewhat achieved positive results so far. Inter-bank funding stresses have eased, though still higher than "normal" levels while USD shortage issues were somewhat addressed.

Inter-bank Funding Stress Eases but Still Remains Elevated



Source: Bloomberg, Maybank FX Research & Strategy

2-Pronged Approach on Which FX to Ride the Recovery

In this report, we adopt a 2-pronged approach in setting up a framework to assess which FX could benefit more in the event of a more decisive recovery from COVID-19 pandemic, taking into account the following factors:

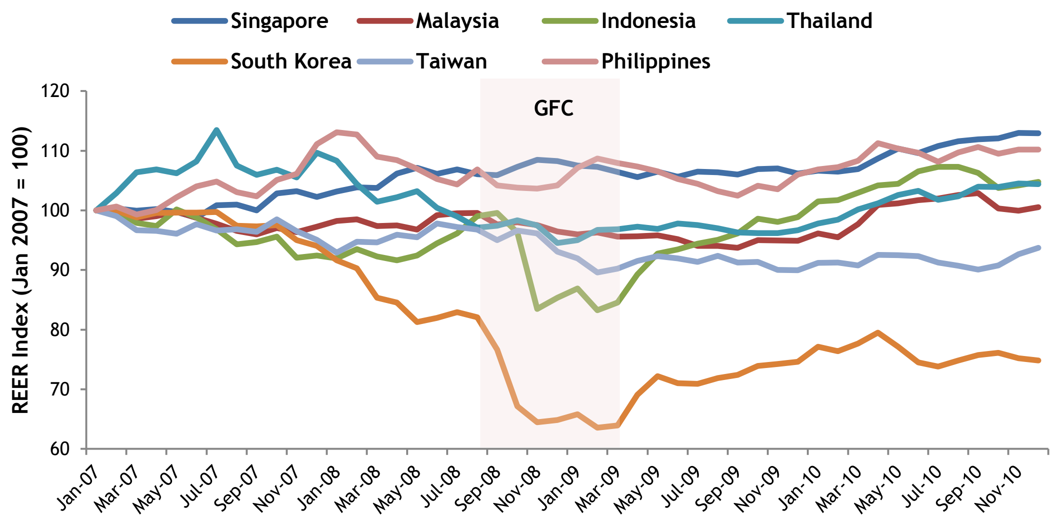
1. Market parameters to assess current state of Value, Sovereign Risk and Carry in individual FX; and
2. A relook at underlying and emerging trends that proxy FX could ride on in the “new normal” post-COVID-19.

Given how volatile recent FX moves have been, we need a sense of the “current state” of currencies at each point in time. To that end, we pick three key indicators representing value, sovereign risk and carry, respectively, and present them in percentile form (to be elaborated below).

Value Indicator: Real Effective Exchange Rate (REER)

The real effective exchange rate (REER) is used to measure the value of a specific currency in relation to the currencies of its trading partners, taking into account inflation. REER moves can be caused by both long-term fundamental changes within an economy as well as shorter-term factors. In the case of Covid, REERs of regional currencies have recently been impacted by concerns over loss of tourism and export revenues. Assuming that some of these flows in people and goods & services reverse when lockdowns gradually ease, and demand conditions on the ground recover, we could see a concomitant retracement in REER weakness as well. All else equal, a lower REER also suggests that a country’s goods are becoming cheaper, and further support any rebound in exports in an economy’s recovery phase.

Most Regional REERs Fell During GFC and Recovered Swiftly



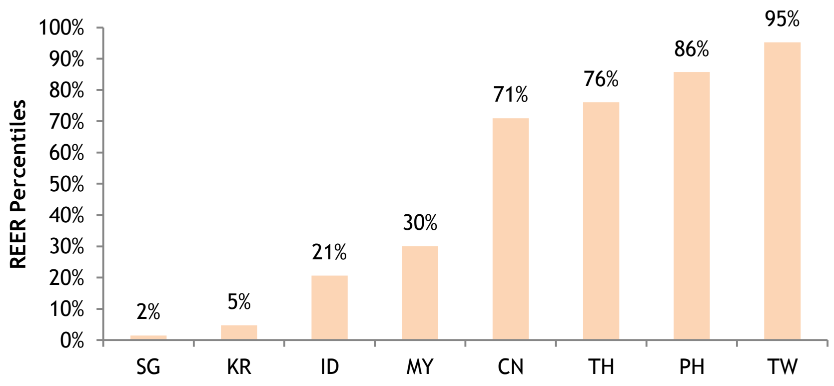
Source: Bloomberg, CEIC, Maybank FX Research & Strategy Estimates

Looking at the chart above, we see that most regional REERs did decline heading into the Global Financial Crisis (GFC), and saw troughs at the peak of the crisis in late 2008, before paring losses afterwards in a matter of months.

The notable exceptions were Singapore and Philippines. Singapore utilizes an exchange rate-based monetary policy (keeping SGD stable within a band), which could have prevented sharp declines in the SGD vs. peers at the time. Philippines, on the other hand, has a relatively closed economy, and PHP's sensitivity to externally-drivers could be lower vs. peers.

To better capture how elevated/depressed current regional REERs are for regional FX, we utilize the concept of **percentile rankings**. We choose 5-year comparison periods to proxy for the "norm" over recent history. A higher percentile ranking would indicate that the current value of the REER is relatively high vs. **its own recent 5-year history**. A value of 0% or 100% would mean that the current REER is at its minimum or maximum point vs. its 5-year history, respectively.

SGD, KRW REERs Most Depressed Relative to Own 5-Year History



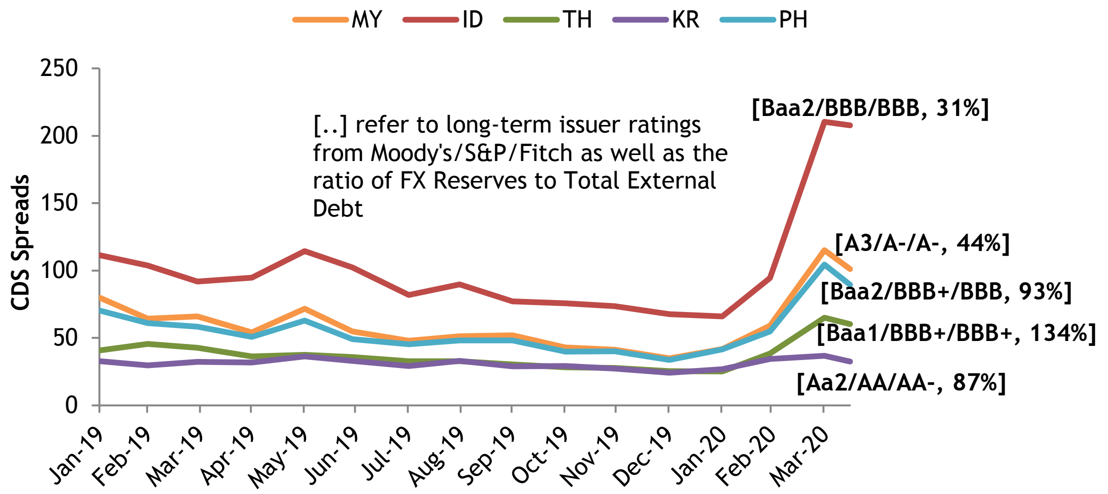
Note: BIS Broad REERs are used (last data point at Feb 2020) and updated to latest levels using internal estimates.
Source: Bloomberg, BIS, Maybank FX Research & Strategy Estimates

From our calculations, KRW and SGD REERs are significantly softer now compared to their own recent norms. Such "stretched" levels of weakness could see these currencies recover more/quicker once global sentiments turn decisively.

Risk Indicator: CDS 5-Year Spreads

We turn to credit default swap (CDS) spreads as a generic "risk premium" indicator. Views on credit risks are influenced by many factors, including issuer ratings from rating agencies as well as sufficiency in FX reserves (vs. external debt). The differential moves in CDS spreads at the onset of Covid are telling.

Wide Differentiation in CDS Spread Spikes Among AxJ Amid Covid



Note: CSD Spreads unavailable for Sg and TW, but long-term issuer ratings are robust at Aaa/AAAu/AAA and Aa3/AA-u/AA- respectively.

Source: Bloomberg, Maybank FX Research & Strategy Estimates

Twin deficit countries such as Indonesia had to quickly revise legislation to allow for the rise in fiscal spending (removing legal cap in deficit of 3% of GDP for 3 years). With an estimated US$25 billion allocated to fight Covid for now, budget deficit is pushed to 5.07% of GDP. Concerns are on whether a more protracted Covid episode (and accompanying expansions/extensions of lockdowns) will lead to calls for even greater stimulus and greater fiscal strain ahead.

Spreads for Malaysia was also elevated in late March. Besides Covid pressures, softer oil prices also likely led to worries over oil-related revenues. Our Chief Economist Suhaimi notes that every US$10/bbl decline in oil price will reduce fiscal revenues by MYR7bn and raise the budget deficit to GDP ratio by 45bps. Meanwhile, perceived sovereign credit risks for Korea hardly budged despite a US$82bn (5% of GDP) stimulus package, alongside a global search for quality assets.

Given the nature of the pandemic-led crisis (huge stimulus plans leading to issuance of longer-term fiscal debt, cash crunch among firms), sovereign or corporate credit risks may take longer to fade than in previous crises. In this instance, the differentiated levels of CDS spreads would be useful for monitoring the perceived risks for each economy. We similarly compute percentile rankings for current CDS spreads and include them in a table at the end of this section.

Carry Indicator: 10 Year Bond Yield Differentials (vs. US)

In US, recent Fed rate cuts (even to near-zero) were accompanied by strong demand for USTs. Search for yields clearly matter less in the rush for quality/liquidity. Alongside heightened market volatility and bouts of risk aversion, unwinding of carry in some Asian markets was observed over Feb-Mar, alongside portfolio outflows. For instance, higher yield differentials (domestic vs. US) were not sufficiently appealing to support regional FX against bouts of softening then.

Unwinding of Carry Seen in ID, and to a Lesser Extent, MY in Feb-Mar

	Indonesia				Malaysia			
	Period	Local Currency Bond Flows	IDR vs. USD	ID 10Y Vs. US 10Y Differential (Change)	Period	Local Currency Bond Flows	MYR vs. USD	MY 10Y Vs. US 10Y Differential (Change)
GFC	Aug 08 to Mar 09	-US$4.9bn (-42%)	-21.8%	+2.2% pt	Apr 08 to Mar 09	-US$8.6bn (-54%)	-13.5%	+0.9% pt
Covid	Mid-Jan to 31 Mar 2020	-US$17.4bn (-22%)	-15.9%	+2.3% pt	Mid-Jan to 31 Mar 2020	-US$6.6bn (-16%)	-5.7%	+1.2% pt

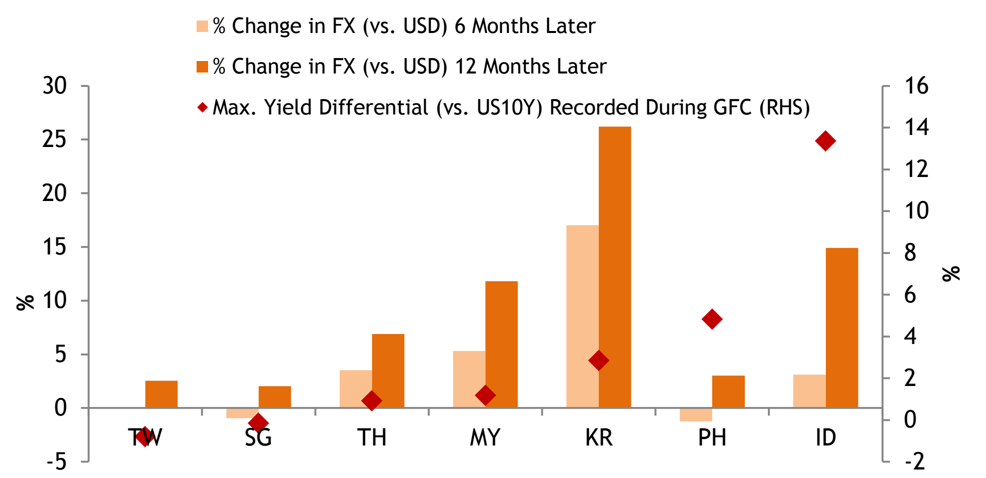
Source: Bloomberg, CEIC, Maybank FX Research & Strategy Estimates

In the recovery period however, as the initial risk trigger (e.g., Covid) fades and market volatility eases, yield differentials can matter again. For instance, BI says that despite some volatility in 2Q and 3Q, it expects foreign capital inflows to recover more strongly by 4Q this year. Higher frequency sovereign bond outflows from Bloomberg show that MTD outflow by mid-April is at a negligible -US$71mn, compared to -US$7.5bn in March.

In the chart below, we look at the maximum yield differentials (domestic 10Y vs. US 10Y) recorded during the GFC period (during the peak of the crisis in late 2008), and the % change in the respective currencies 6 and 12 months after.

With the exception of PHP, we note that currencies with higher carry vs. the dollar then recorded broadly significant recoveries post-crisis. While admittedly a whole host of other factors including the ones we discussed above are at play, **the return of carry appeal in a lower-for-longer DM rates environment could contribute to strength in regional currencies in a recovery phase**.

FX with High/Positive Carry Saw Swift Recoveries Post-GFC



Source: Bloomberg, Maybank FX Research & Strategy Estimates

Similarly, we compute percentile rankings for yield differentials (relative to their recent 5-year norms) and include them in a table below alongside the other indicators above.

Prefer Low REER, Low CDS Spread, High Yield Differentials (Blue Cells)

	Market Parameters (Percentiles)		
	Value	Risk	Carry
CNY	71%	11%	98%
KRW	5%	14%	98%
TWD	95%	-	100%
SGD	2%	-	90%
MYR	30%	48%	98%
IDR	21%	87%	98%
THB	76%	56%	94%
PHP	86%	59%	92%

Note: CSD Spreads unavailable for SG and TW, but long-term issuer ratings are robust at Aaa/AAAu/AAA and Aa3/AA-u/AA- respectively. We assess sovereign credit risks to be low (i.e., blue).

Source: Maybank FX Research & Strategy Estimates

Trends and Proxy Plays

As we turn the page on COVID-19 looking for a recovery, we also explore what underlying trends and emerging trends there may be for tactical FX plays. We consider various trends including a (i) general risk-on where the markets buy the story that we are out of the woods and is in a clear hunky-dory V-shape recovery; (ii) a resumption of the tech-trend that was previously disrupted; (iii) an oil rebound given OPEC+ cuts; (iv) China activity rebound as the economy reopens after lockdown.

We identify proxies to the above trends and establish the general behavior of FX to those trends, in terms of magnitudes and direction. We run OLS regressions between AXJ/FX (as dependent Y-variable) with proxy identifiers (as independent X variable). Our 4 proxy identifiers are MSCI world equities to proxy for risk-on sentiment; Philadelphia Stock exchange semiconductor index (SOX) to proxy for tech trend; brent prices to proxy for oil rebound; and china electricity energy consumption to proxy for China activity rebound. The sample period is 15 years on weekly frequency data on log values and we extract their respective historical betas to characterize the potential FX behavior. Higher beta (or sensitivity) to trend is shaded in blue while negative beta (inverse correlation) to trend is shaded in red.

Extracted Currency Betas on Trend Proxies

	Risk-On market sentiment	Tech Recovery	Oil Rebound	China Activity Rebound
CNY	0.059	0.012	0.085	0.156
KRW	0.074	0.167	0.080	-0.117
TWD	0.061	0.023	0.077	0.079
SGD	0.080	0.018	0.141	0.143
MYR	-0.277	-0.161	0.296	-0.221
IDR	-0.551	-0.280	0.317	-0.265
THB	0.078	0.017	0.135	0.075
PHP	-0.099	-0.081	0.160	-0.082

Note: Betas shown here are meant as a general indication of average currency (XXX/USD) sensitivity to changes in market variables/economic indicators over 15-year sample period from Apr 2005 to Apr 2020. (log values; weekly freq data except for China activity rebound where China electricity consumption used are of monthly frequency). Sensitivities can increase or decrease when defined sample period changes.

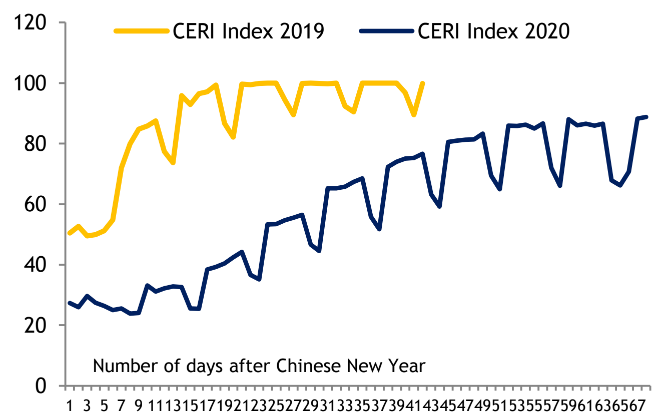
Source: Maybank FX Research & Strategy Estimates

For the purpose of the aggregate framework introduced above, we singled out 2 trends—a **resumption of tech recovery and China-led rebound**—we believe should play out more strongly in the event of a recovery from current COVID pandemic environment.

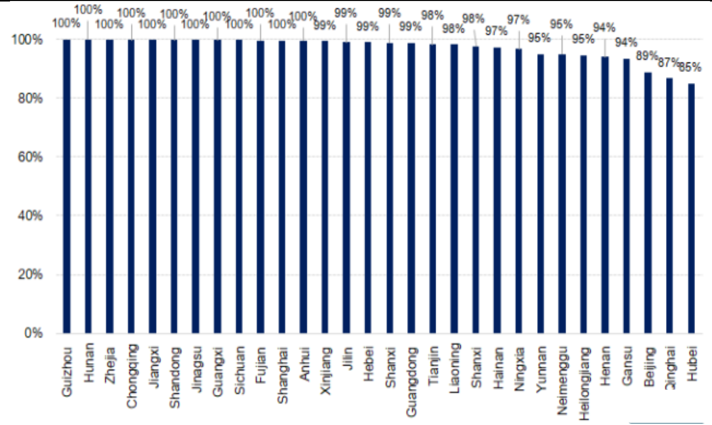
True that China's output and domestic demand took a massive hit owing to COVID-19 pandemic outbreak and lockdown measures. Retail sales and industrial production fell 20.5% y/y and 13.5% y/y in Feb (latest available data at time of writing; next set of data to be released on 17 Apr) while Caixin services PMI remains in contractionary territories (43.0) in Mar. China 1Q GDP is also likely to show a huge contraction, with Bloomberg consensus estimates showing a 12% sequential contraction for 1Q.

But China has moved on from COVID-19. It is no longer the epicenter and the economy has gradually reopened after being on lockdown for nearly 60 days. China economic recovery index (or CERI – an aggregated mobility data) is signaling a >80% recovery in business activities (includes manufacturing and consumption but not capturing online shopping and working from home), according to data as of 9 Apr. Other proxy data for economic activity such as work resumption rate of provinces and cities have indicated that work resumption rate have returned to above 85% for most provinces while traffic congestion has returned to 90% of pre-Lunar New Year levels and China railway daily passenger volume has risen back to pre-lockdown levels in mid-Jan 2020. These proxy data for activity suggest that the economy is making progress to resuming economic activities after lockdown measures were lifted gradually since Mar. Latest China data (published 17 Apr) showed a weaker 1Q GDP print (-6.8% y/y) and weaker retail sales for Mar (-15.8% y/y) while industrial production was less weak than expected (-1.1% y/y for Mar vs. expectations of -6.2%). This reinforced the proxy data above that work, business resumption was faster while resumption in consumer activities were somewhat still restricted and cautious at this point.

More than 80% Recovery in Business Activities



Work Resumption Have Returned to above 85%



Source: iFAST research, Bloomberg, Maybank FX Research & Strategy

Pent-up consumer demand is likely to return faster if there are clearer signs of medical breakthrough in terms of vaccination or more evidence to confirm that the risk of second wave of infections is low. Anecdotal evidence suggests that Chinese spending powers should not be underestimated—it was reported that Luxury French retailer Hermes posted $2.7m sales on the day its flagship store reopened in Guangzhou while property giant Capitaland sold all 288 units of its new La Botanica township development in Xi'an, within 4 days of launch on 24 Mar.

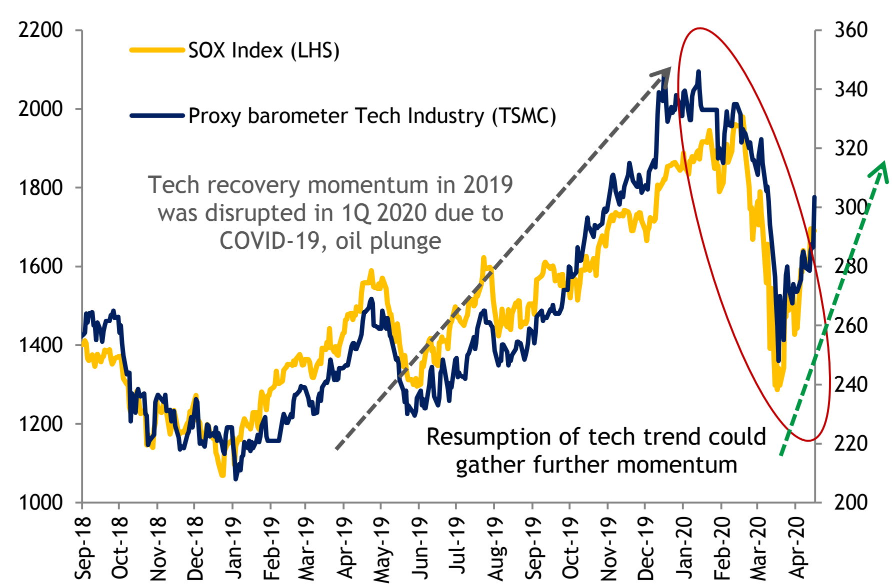
- As a word of caution, there were some concerns of second wave infections due to imported cases. Heilongjiang province which borders Russia reported a spike in imported cases (49 Chinese nationals entered

China via Heilongjiang borders from Russia tested positive). The respectable Lancet medical journal also warned that premature relaxation[1] of measures such as social distancing, contact tracing, etc. could result in adverse consequences (i.e. second wave of infections).

Taken together, resumption in economic activities, pent-up consumer demand could lead a strong rebound (but not full) for China. **Our FX sensitivity study suggests that RMB, SGD and TWD could stand to benefit.**

We also single out the **resumption of the tech trend** that is likely to come into attention once again. COVID-19 pandemic saw a surge in demand for video conference, cloud computing, IT supplies, including laptops, printers and some corporates were under-invested in such infrastructure and is urgently looking to fill the gaps.

Resumption in Tech trend as seen in proxy barometers



Source: Bloomberg, Maybank FX Research & Strategy

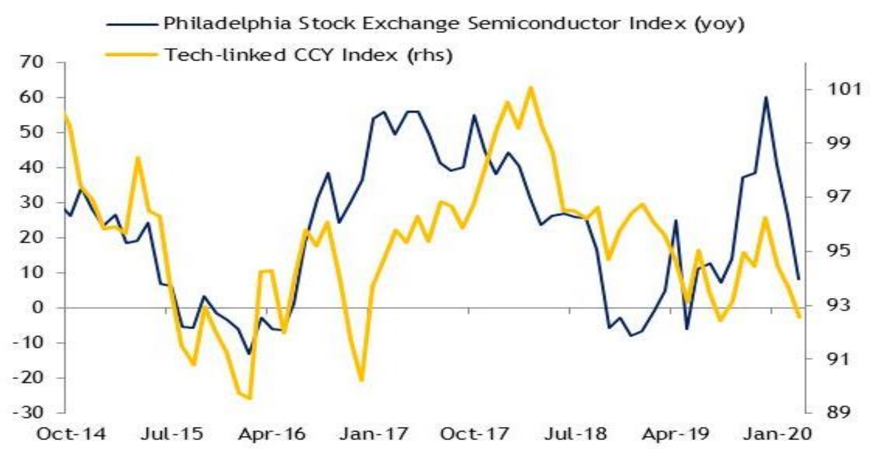
Prior to COVID-19 outbreak, the tech recovery was already gaining traction but overshadowed by oil price plunge and COVID-19 pandemic. We drew reference to the report published by World Semiconductor trade statistics (WSTS) in which it expects the global semiconductor market to recover 5.4% in 2020, following a projected decline of 12.1% in 2019. All subsectors are forecasted to grow with Memory contributing the highest growth, followed by Optoelectronics and Logic. The global semiconductor down cycle bottomed in 3Q 2019, after 4 consecutive down quarters (Typically, a semiconductor downcycle involve about 4 – 5 down quarters before a turnaround takes place). Inventory drawdowns (after chip producers cut production in response to the down-cycle and decline in memory prices in late-2018 to 1H 2019) as well as an improving demand environment led by increase in orders for 5G network deployment, cloud providers and Internet of Things (IOT) supports a cyclical recovery story. Tech giant, TSMC said it is sticking with plans for aggressive capital investments this year by about $15 – 16bn, an increase from $14.9bn in 2019 and is forecasting revenue growth of about 30% this quarter. This is a sign from the bellwether of resilience demand despite COVID-19 pandemic and large downgrade to global growth.

Taiwan, Korea and China are key players in the global semiconductor industry. According to Worldwide Semiconductor Equipment Market statistics, Taiwan claimed the largest market for new semiconductor equipment in 2019 with a 29% share of the global sales of $59.8bn, China took second spot with 22% share while

[1] Xu Sq, Li Yy. Beware of the second wave of COVID-19. Lancet 2020. Published online 8 Apr 2020. https://doi.org/10.1016/S0140-6736(20)30845-X

Korea slipped to 3rd spot with 17% share. **Our FX sensitivity study suggests that KRW, TWD and SGD could stand to benefit in the event of resumption in tech rebound.**

Positive Correlation between SOX and Tech-linked Currencies



Note: Tech-linked currency index consists of equally weighted SGD, KRW, TWD vs. the USD (index 100 = Jan 2011)
Source: Bloomberg, Maybank FX Research & Strategy

We see lesser likelihood of trends (i) general risk-on where the markets buy the story that we are out of the woods and is in a clear hunky-dory V-shape recovery; and (iii) an oil rebound given OPEC+ cuts materializing in the near term.

- A broad risk-on at this stage maybe premature as economic growth risks are skewed to the downside. IMF projected global growth to be -3%. This is a 6.3ppt downward adjustment from Jan-2020 forecast making the great lockdown the worst recession since the Great Depression and far worse than the Global Financial Crisis. At the same time corporates have seen negative impact on their earnings and some have refused to offer forward guidance for the quarters ahead. According to ICE BofAML corporate index, about $560bn of IG corporate bonds have been downgraded in the past month. Clearly there are downside risks ahead as lockdowns in certain parts of the world could be extended and countries that have lifted lockdowns will not hesitate to lockdown again on any signs of second wave infections. Sentiment can be whippy and dragged lower especially after the 30% rebound (in S&P 500) from Mar-2020 lows faces a reality check. We are however hopeful of a broad recovery eventually when there are clearer signs of vaccine development or flattening of epidemic curve. A more broad based lifting of lockdown measures could see a sharper recovery in demand, exports and this could result broad risk on play at some stage in the future (likely in 3Q 2020).
- We also think an oil price recovery is unlikely in the near term (1-3month horizon) despite OPEC+ members committing to 9.7mbpd cut to oil production. IEA's recent report is a reminder that current oil supply-demand imbalance remains unresolved as demand loss owing to COVID-19 pandemic could result in oil inventory build of 12mbpd in 1H 2020 and global storage capacity may be overwhelmed by the supply glut. We do think an eventual recovery could take place sometime in 2H 2020 when demand picks up, especially if travel restrictions can be lifted alongside country lockdowns and social distancing measures. MYR and IDR would be optimal FX proxies to position for oil rebound then.

FX Playbook - Our Bias Based On Derived Framework

From a markets point of view, the first 3 months of 2020 has been one of the most challenging, with vols rose rising all asset classes including FX, equities, bonds and oil to levels not seen since GFC 2008-09 levels. And this was largely due to black swan COVID-19 pandemic and its consequential remedial actions including lockdowns, travel restrictions to contain the spread of COVID-19, compounded by the >60% plunge in oil prices (sparked off by Saudi-Russia disagreement). The IMF had made one of the most bearish economic assessment - projecting global growth to be -3%. This is a 6.3ppt downward adjustment from Jan-2020 forecast making the great lockdown the worst recession since the Great Depression and far worse than the Global Financial Crisis.

Since mid-Mar, vols have eased from its highs and equity markets have even rallied about 30%, from its Mar lows. Upbeat sentiment suggests tentative optimism as some parts of the world are looking to gradually reopen their economies after multi-week lockdowns—a testament that lockdowns have been effective to flatten the epidemic curves. At the same time policy responses from central bankers have managed to alleviate funding/liquidity stresses and keeps the flow of credit functioning while fiscal support is helping to ease the burden on households and corporates. This helps to support market sentiment and we would describe the recent boost in sentiment as a cheer to containment efforts.

But looking on, a reality check on the rally may be due given the economic damage, corporate downgrades and massive job losses globally COVID-19 pandemic has caused. We are certainly not out of the woods as COVID-19 epidemic curve has yet to flatten meaningfully across the world; lockdowns, travel restrictions and social distancing are still in place and there is not yet ready a medical breakthrough in terms of vaccine development. While **a V-shape recovery for markets maybe ruled out at this point, a bottoming in risk appetite could still be in place for an eventual U-shape recovery** especially if COVID-19 containment remains and if COVID-19 drug/vaccine development gathers traction. And we thought it would be **timely at this point to assess how optimal we can position for a recovery via FX plays.**

Aggregate View of Our Framework Results ("Blue" Preferred)

	Market Parameters (Percentiles)			Trend Proxy (Betas)	
	Value	Risk	Carry	Resumption of Tech Recovery	China Activity Rebound
CNY	71%	11%	98%	0.012	0.156
KRW	5%	14%	98%	0.167	-0.117
TWD	95%	-	100%	0.023	0.079
SGD	2%	-	90%	0.018	0.143
MYR	30%	48%	98%	-0.161	-0.221
IDR	21%	87%	98%	-0.280	-0.265
THB	76%	56%	94%	0.017	0.075
PHP	86%	59%	92%	-0.081	-0.082

Note: "Value" is based on REER, "Risk" is based on CDS Spreads and "Carry" is based on 10Y Bond Yield Differentials vs. the US. Interpretation of the table: For market parameters, we utilize the concept of percentile rankings. A lower percentile would indicate that the current value is relatively "low" as compared to its "norm", which we define as its 5-year history. For example in the case of value, the current SGD REER is perceived to be low vs. its own recent 5-year history. We see attractiveness in currencies perceived to have lower percentile (coded blue) for value and risk and higher percentile for carry (coded blue). For Beta sensitivity on trend proxy, higher beta means the AXJ is more sensitive to the trend proxy and is shaded in blue while negative beta means the AXJ's sensitivity is inversely correlated to the trend proxy and is shaded in red. We prefer shades of blue to capture the trend.

Source: Maybank FX Research & Strategy Estimates

Overall, we see chance for a **recovery led by China** as the economy reopens after nearly 60 days of lockdown—resumption in economic activities, pent-up consumer demand there could lead a strong rebound for China (though we do note that minimal inter-province travel and zero tourism as a result of travel restrictions are likely to limit economic rebound) as well as one that is led by **a resumption of an underlying tech trend**. We remain skeptical of a meaningful oil rebound in the near term (1 – 3 month horizon) as supply-demand imbalance will weigh on oil prices for longer.

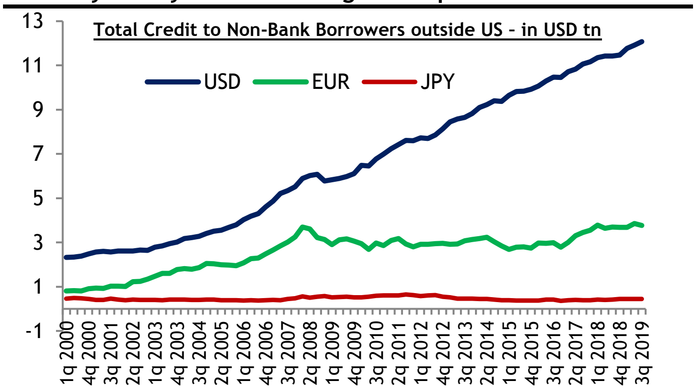
Given the above scenario, our bias is for KRW, TWD and CNY to outperform riding on resumption of tech recovery trend and China rebound. One point to note is that the value metric (proxied by REER relative to its historical) suggests that KRW and SGD may see more room for gains amongst the North Asian FX. TW handled COVID-19 crisis well and TWD is well positioned to fully take advantage of resumption of the tech rebound.

Results for MYR, THB and IDR are more mixed, reflecting in part the confluence of multiple factors impacting each now. For THB, the timing of tourism recovery is key, as re-emergence of tourist flows may take longer compared to the SARS episode. The THB REER is also a tad elevated even after recent dampening in the currency. IDR and MYR could regain appeal if value and carry pans out well over the next 3 months.

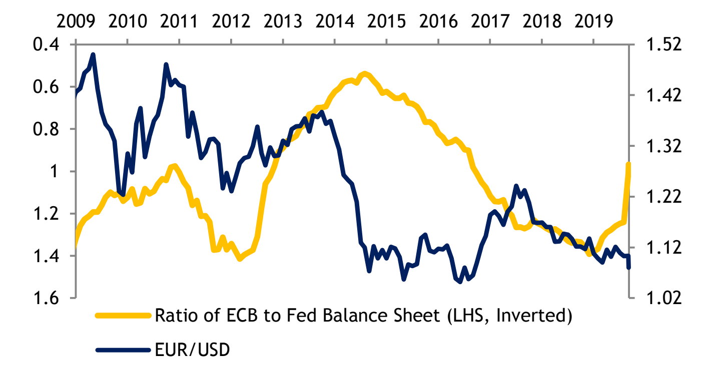
PHP has been relatively resilient since the onset of the COVID-19 crisis, which could potentially also constrain gains during recovery. A scan across the metrics in the table above adds weight to this possibility.

Finally a word on the greenback. We are biased for USD downside play but this is not a one way bet. The USD has 2 key aspects – an "international" role due to US being the world's reserve and payment currency (for a lack of better alternative) and as a proxy of its domestic factors. So in a risk-off pandemic environment, there will be demand for USD for funding/liquidity purposes and this will keep USD supported. But the USD cannot escape unscathed given unprecedented trillions of "money printing", massive surge in job losses in US (about 16mio in jobless claims over the past 3 weeks) and more economic pains ahead owing to COVID-19 (as US remains the epicentre as death tolls surpassed Italy and the US public health system cannot cope with the outbreak). It is likely Fed and the US government may have to do more (i.e. further easing, fiscal stimulus) to prevent the US economy from deeper fallout. USD "glut" amid Fed liquidity pumping will dent UST yield advantage and USD appeal when COVID-19 crisis fades.

USD Plays a Key role in funding of companies outside US



Expansion of Fed balance can Depress USD Appeal



Note: Total credit refers to bank loans and debt securities; EUR and JPY debt converted to USD using respective qtr-end FX rate
Source: BIS, Bloomberg, Maybank FX Research & Strategy

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