Macro | FX Research and Strategy

Global

FX Insight

ASEAN FX Gains - More To Go?

Recovery Priced but More Could Come After a Temporary Phase of Consolidation

ASEAN FX have made a "swooshed" recovery from their respective COVID-19 troughs and we attempt to explore if the recovery has jumped the gun, or if there is room for further gains. The past 5 crises over the last 32 years show that ASEAN FX, as a broad basket, typically recovered by about 50-60% from their respective sell-offs within 50 days. If history is a guide, the current recovery post COVID-19 trough has been adequately been priced in, as of now. There could be room for further gains, but this could come after a temporary phase of consolidation—as near-term concerns (second wave contagion, drag on global jobs markets) play out. Structurally, the simultaneous use of twin stimulus on such a global scale is unprecedented, and combined with low-for-longer US rates, softer USD environment, a more durable global economic recovery could kick in gradually. Cyclical proxy-FX including ASEAN FX could stand to benefit further while USD stays back-footed. Our bias at this point is to sell USD-ASEAN pairs on rallies.

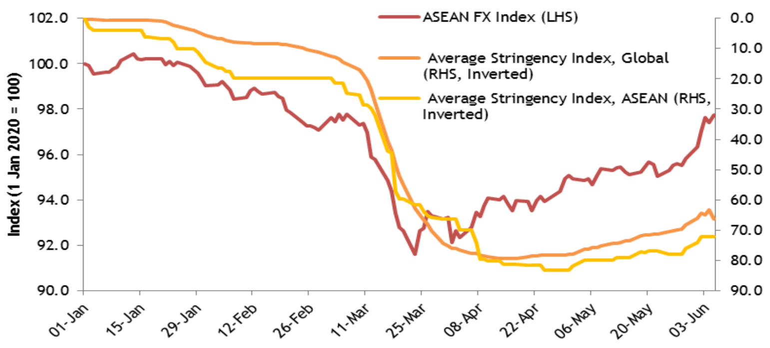
Certain Aspects of this Recovery Differ Discernibly from Past Episodes

1) On the unique boost that "reopenings" are giving to ASEAN FX, using Google Trends data as a proxy of sentiments, we found that SGD and MYR were more reactive to this aspect vs. peers. There is likely room for more support to FX on this front, as more than two-thirds of restrictions remained in place in early June (as proxied by the Stringency Index, Oxford Covid-19 Govt Response Tracker). Nonetheless, gains ahead could be more modest, as some front-loading of positivity has likely occurred.

2) Unconventional monetary policy is also a somewhat new phenomenon for regional central banks. We used a panel VAR model to gauge initial FX reactions to the announcements of bond purchase programs and found near-term FX impact to be mildly positive, suggesting that concerns over debt monetization etc. have yet to weigh on sentiments.

3) US-China tensions admittedly complicate the current recovery. Examining sensitivities of ASEAN FX to CNY over bouts of negative CNY shocks, we found that sensitivities vary depending on the channel of sentiment shocks. While the potential for escalation is intact, without a breakdown of the Phase 1 trade deal, there could be a lack of a clear channel for pessimism to entrench more aggressively.

ASEAN FX Moves May Have Front-loaded Lockdown Easings



Source: OxCGRT, Bloomberg, Maybank FX Research & Strategy

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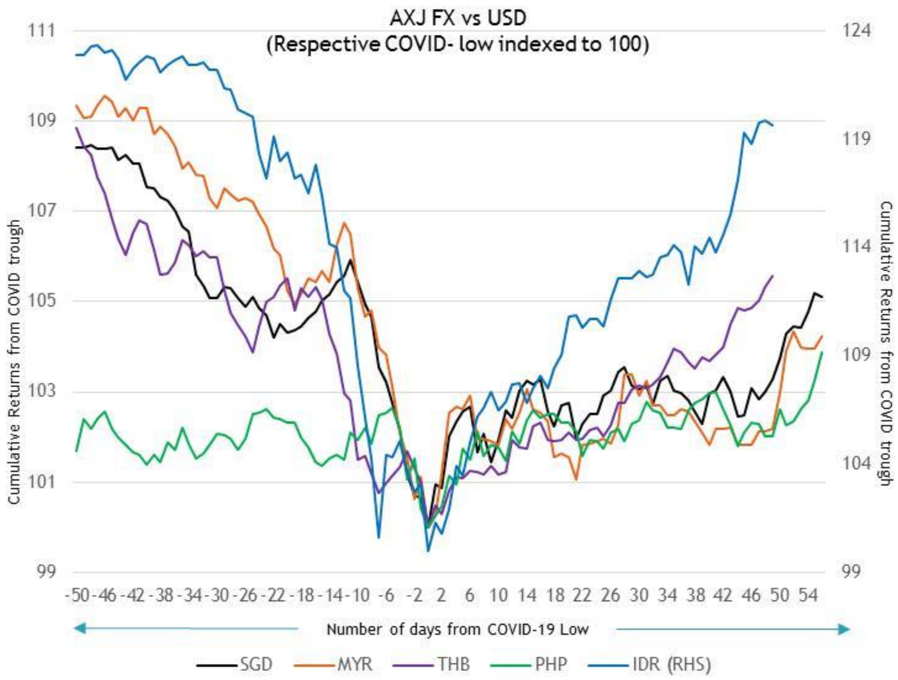
ASEAN FX Rebounded from COVID trough but Yet to Return to Pre-COVID Levels

As of 9 Jun, most ASEAN FX, including SGD, MYR, THB and PHP have risen between 2% and 5% (vs. USD) while IDR has risen about 19% (vs. USD) from respective COVID-19 trough. The rebound was in line with our call for an *opportune time to consider positioning for eventual recovery*, as shared in our last report (AXJ) Phoenix from Ashes, sent on April 17.

"Nike"-Swooshed Recovery for most ASEAN FX



Source: Bloomberg, Maybank FX Research & Strategy
Note: Each ASEAN low in COVID sell-off differs

At first glance, IDR after appreciating nearly 19% from Mar-2020 low, is the big winner amongst ASEAN FX. But prior to its low point, IDR plunged nearly 24%, 50-days prior to COVID-low.

In the same period, SGD, MYR and THB fell about 10% to its respective COVID-19 low. THB has strengthened by about 6% while MYR and SGD have strengthened between 4% and 5% (marginal laggards in terms of recovery momentum compared to other ASEAN FX).

PHP, on the other hand has been resilient, depreciated the least (<3%) and has more than recovered to pre-covid levels.

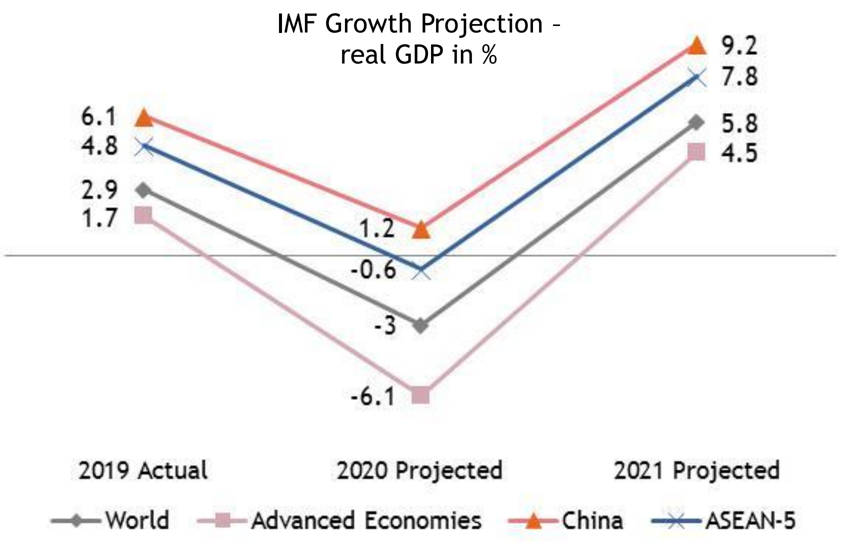
Relative to their respective levels at T-50day, IDR has recovered nearly 80% of its losses while THB, SGD and MYR have recovered by about 60%, 50% and 40%, respectively. This can be subjective due to where the start point of comparison is, but essentially, the performance so far illustrates that IDR and PHP shine more relative to its ASEAN peers.

We explore further – if this uneven ASEAN FX recovery has room for some to play catch up, if a recovery is already fully priced and/or there is further legs to more gains.

Markets Pricing in Forward Expectations Instead of an Over-Emphasis on the Severity of Incoming Data

The swooshed recovery for most ASEAN FX can be attributed to rapid and somewhat coordinated policy responses - both monetary and fiscal, globally including ASEAN central banks and governments, hopes of vaccine development/ drug discovery as well as guidance by central banks and IMF of a V-shape economic recovery in 2021.

V-Shape Economic Recovery for 2021 Guided by IMF



Source: World Economic Outlook (Apr 2020), Maybank FX Research & Strategy

Thanks to IMF's guidance for 2021, markets' re-pricing for post-covid global growth rebound is also intensifying especially when more countries, including, Singapore, Indonesia, Philippines, Malaysia gradually ease lockdown restrictions, social distancing measures and re-open their economies this month, joining Australia, NZ, and some European countries etc. last month. Yes, activities may still see a slow start (as social distancing guidelines remain in place) but at least economic activities are no longer at a halt.

There are also ongoing talks of countries lifting travel restrictions via creation of "travel bubbles" (or green lanes – basically allowing for quarantine-free flow of people). To name a few, Singapore-China fast lane is in operation since 8 Jun, otherwise known as a "travel bubble" enabling essential business and official travelers to cross borders with minimal or no quarantine. And this looks set to be expanded to Canada and South Korea. Singapore is also in talks with Malaysia to resume travel soon. Indonesia is lifting its ban on air travel, allowing planes to carry up to 70% of their passenger capacity staring 10 Jun. Australia and NZ are planning a Trans-Tasman travel bubble while some Baltic countries including Estonia, Latvia and Lithuania have formed "travel bubbles" lifting restrictions for each other citizens; Greece is looking to welcome international tourists from selected countries from 1 Jul while "travel bubbles" between Germany-Austria-France-Switzerland are potentially forming. We explore the link between economies reopening and impact on FX later in this report.

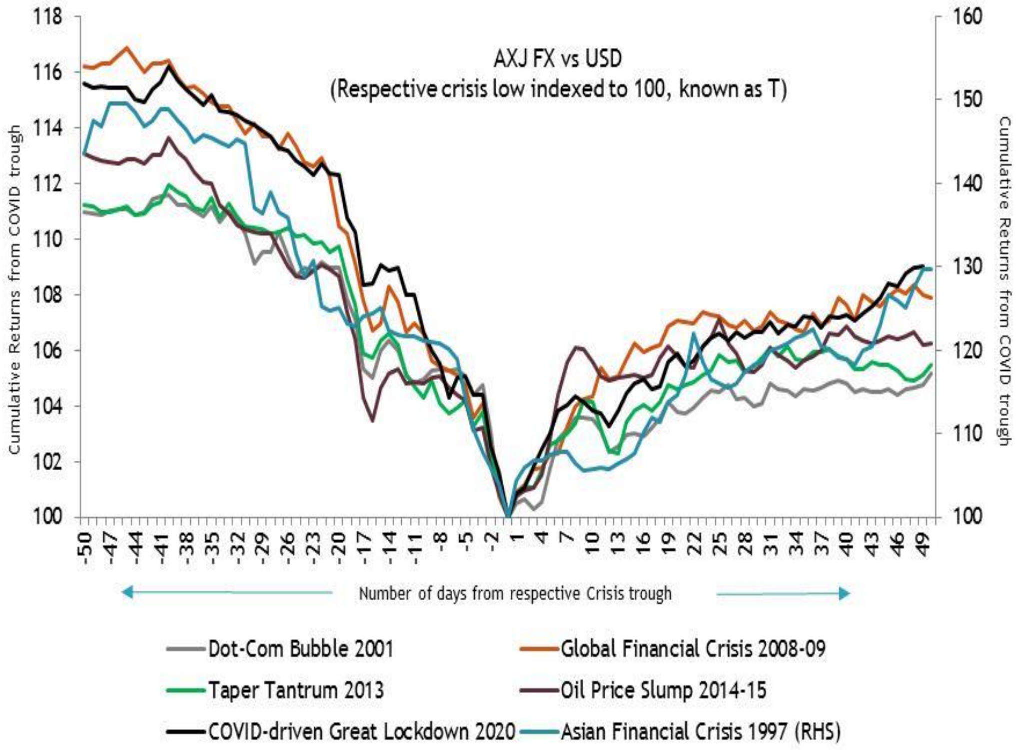
Restarting of travel and tourism in due course is a positive (though marginal for a start) for investor sentiment, business confidence and risk assets. So as the world economy picks up, cyclical proxy FX such as the ASEAN currencies strengthen while USD weakens.

How Swift is the Ongoing Recovery?

To get a sense of the current ASEAN FX recovery post-COVID slump, we look back at the past 5 exogenous shocks in the last 30 years or so, including the Asian Financial crisis in 1997-98, Dot-Com bubble in 2001, Global financial crisis in 2008-09, Taper tantrum in 2013 and oil price slump in 2014-15.

For this exercise we created an ASEAN-5 basket FX (equally-weighted) of SGD, MYR, IDR, THB and PHP and indexed its respective crisis low to 100 for each episode to get a sense of the magnitude and swiftness of decline and recovery as well as to sieve out similar recovery trajectories to the current one.

A Comparison with the Past



Source: Bloomberg, Maybank FX Research & Strategy

On a T-50 to T+50 timeframe, some findings include:

(1) ASEAN FX as a whole, did not fully recover in any of its past 6 sell-offs relating to exogenous factors, including the current COVID-19 episode;

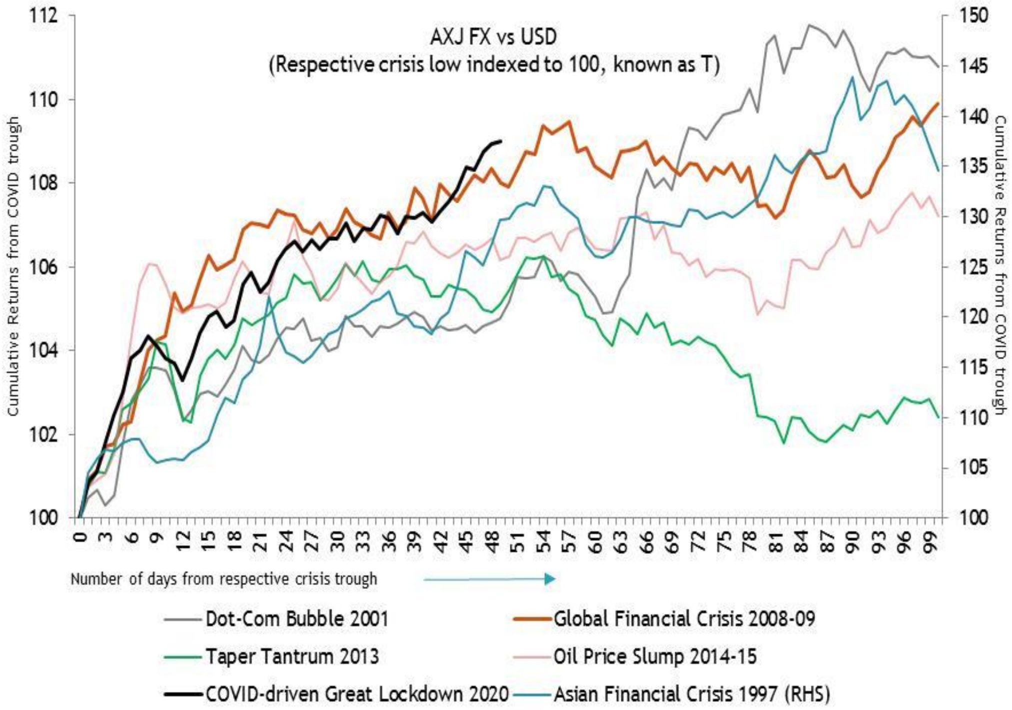
(2) ASEAN FX fall between 10% and 16% from T-50 to respective crisis troughs except for AFC 1997-98 episode when ASEAN FX fell by around 50%;

(3) ASEAN FX typically recovered by about 50-60% from its prior sell-off;

(4) Post-crisis recovery momentum is weakest in dot-com bubble 2001, taper tantrum 2013 and oil price slump 2014-15 relative to recoveries seen in AFC 1997-98, GFC 2008-09 and COVID-driven great lockdown in 2020. The difference could be due to the use of stimulus response.

Note that the above findings are on a broad-based, currency index perspective. Individual ASEAN currencies performance can vary.

Current Recovery Trajectory Similar to Post-GFC Recovery



Source: Bloomberg, Maybank FX Research & Strategy

Focusing on recovery trajectories for ASEAN FX from respective crisis lows, the **current rebound mirrors that of post-GFC 2008-09 episode, in terms of trajectory and magnitude** so far.

The triggers, market conditions and macro landscapes are somewhat different for the 2 episodes. During the GFC, the downturn of the US housing market was the trigger for a financial crisis contagion that started from US to the rest of the world via linkages in the global financial system. The current sell-off was caused by COVID-19 becoming a global pandemic. Drastic but necessary actions to contain the spread of COVID-19 (via country lockdowns, travel restrictions and social distancing measures) severely impacted economic activities. IMF made one of its most bearish economic assessment - projecting global growth to be -3% for 2020, 6.3ppts 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.

But to some extent, there are also some similarities in both episodes. Massive monetary policy responses were very quickly put in place in 2008 and 2020. Fed's deployment of substantial quantitative easing was instrumental in both episodes' rebound.

For the current episode, apart from easing policies via rate cuts, ASEAN central banks also stepped up to explore unconventional policy tools as a mean of shoring up its policy toolkit if crisis worsens. Our Economists had earlier shared on the start of ASEAN QE (see here for note). We will also discuss this in more detail later in this report.

Rapid policy responses also came via fiscal stimulus in size and speed. For instance, Singapore and Malaysia's fiscal response came in at nearly 20% and 17% of GDP. These policy responses designed to save jobs and protect livelihoods somewhat supported sentiment and should help to secure a strong recovery.

If history is a guide, the current recovery in ASEAN FX is likely to have been adequately priced in for now. However, any interim consolidation in FX may be temporary. ASEAN gains have the potential to extend further as we take into consideration the current state of market environment and other factors.

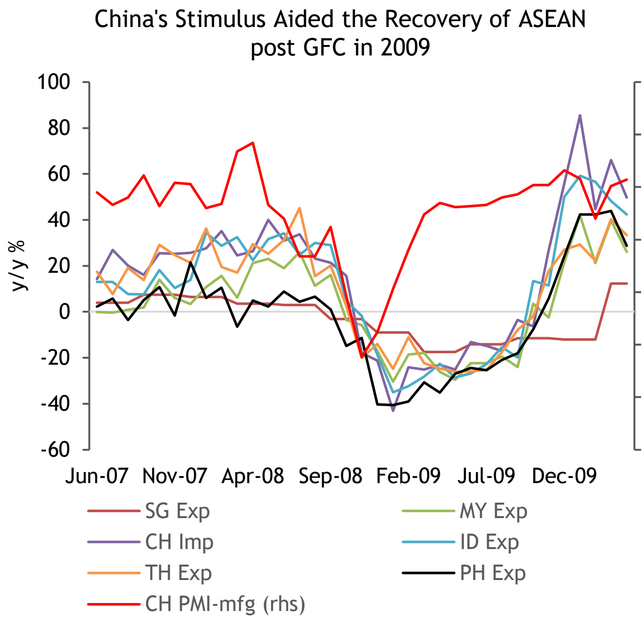
After Production Resumption, China's Recovery May Lift ASEAN

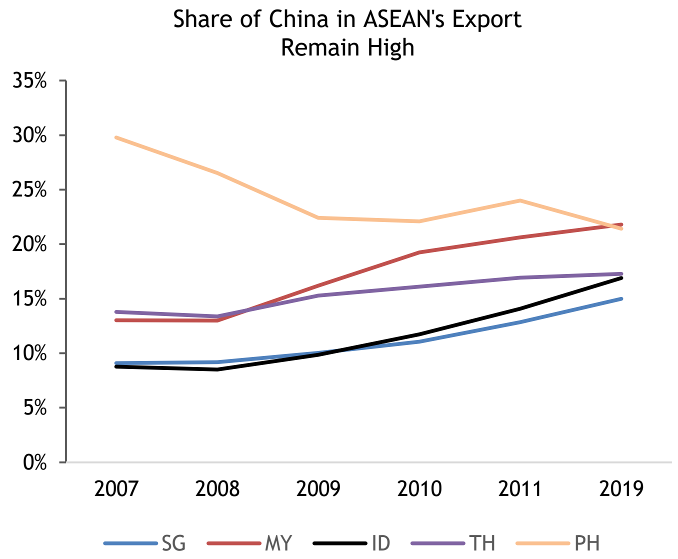
For one, it should be acknowledged that China's ongoing recovery may have the potential to lift ASEAN too.

Looking back at the GFC, it brought about massive global central banks supports as well as an unprecedented size of fiscal stimulus from China. The infrastructure investment thrust there spurred a strong rebound in growth (along with gargantuan credit expansion, unlikely to be repeated). Its domestic demand recovery then lifted the region.

The portion of exports from China rose for ASEAN countries (except Philippines) thereafter and remained elevated as of 2019. In fact, ASEAN overtook US to be China's largest trading partner. Although the experience in 2008-2009 suggests that trade resumption would be U-shaped, the potential for ASEAN to benefit from China's recovery is still one of ASEAN's strength for this crisis episode (much like post GFC in 2009) and the planned completion of the RCEP (ASEAN, New Zealand, Australia, South Korea, Japan and China) negotiations by 2020 may even help to spur the trade recovery within the Asia Pacific.

China Made Quick Recovery Due to Unprecedented Scale of Stimulus in 2008/9 and Lifted The Region





Source: CEIC, Bloomberg, Maybank FX Research & Strategy

What Happened in 2009?

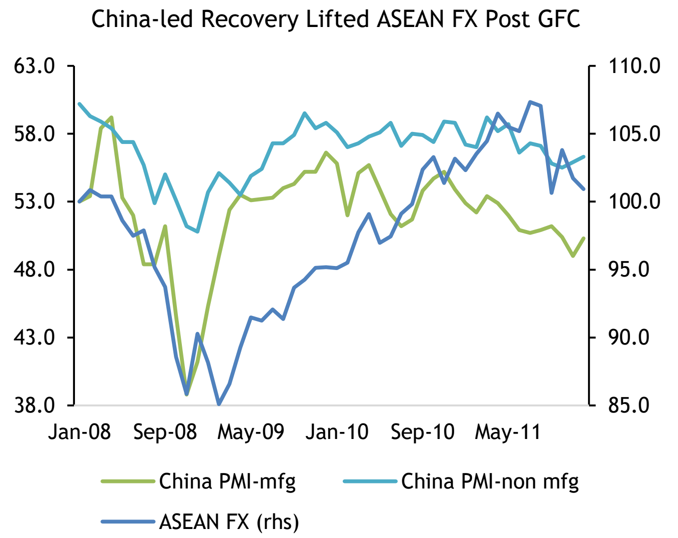
Former China Premier Wen introduced the infamous CNY4trn program "of investments" in Nov 2008. Public infrastructure took up 38% of the total package (CNY1.5trn), followed by reconstruction works (CNY1trn) on areas affected by the Sichuan earthquake. A special CNY200bn treasury bond was issued by MoF on behalf of local governments. As the local governments had to undertake much of the burden of infrastructure provision, the local government financial platforms (LGFPs also known as LGFVs) were created by PBoC and CBRC for local governments to raise funds to finance public investments. (While short-term demand and employment were created successfully in 2009-2010, the stimulus became problematic thereafter as the investment thrust drove China into overcapacity and significant debt accumulation.)

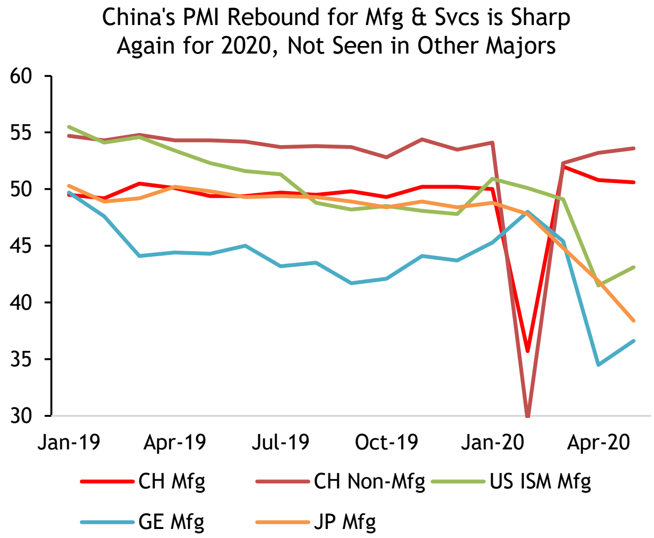
Some Tools Reused for 2020 to Stimulate Demand - Investment

More than a decade later, China is keen not to repeat the mistake of massive fiscal stimulus together with the significant credit easing, especially after having strived to deleverage in recent years.

Notably, the crises response by China to lockdown cities and getting COVID-19 under control was key and also set the economy for an earlier recovery ahead of its peers. As a result, the PMI prints for China recorded sharp rebounds, not unlike what was seen in 2009. In fact, similar to 2009, China faces a weakened external demand, although China is no longer as export-reliant as before.

GFC Recovery Lifted ASEAN FX Well Into 2011; China's PMI Have Recorded a Sharp Rebound This Time As Well



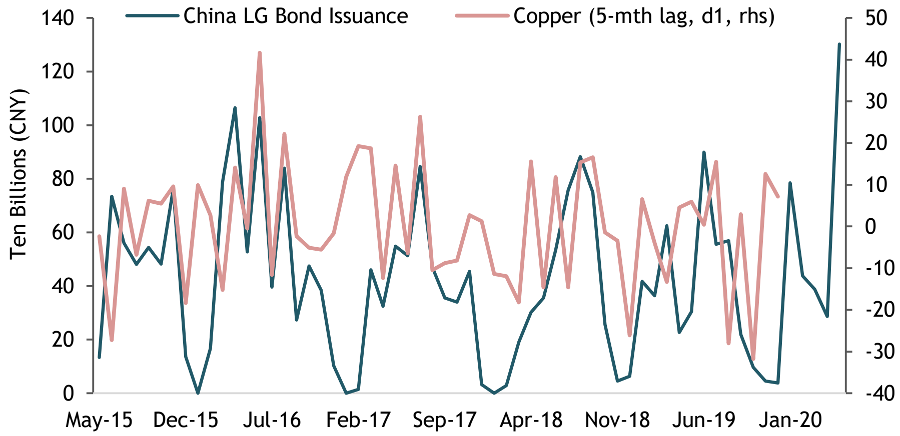


Source: NBS, Bloomberg, Maybank FX Research & Strategy
Note: Left Chart - ASEAN FX Index is a simple average of the ASEAN FX-USD pairs with 31st Jan 2008 = 100

So stimulating domestic demand is again required. However, it is apparent that China desired to be a lot more prudent this time compared to 2009. At the NPC in May, the growth target for 2020 was abandoned (unlike 2009 where the growth target was maintained at 8%) and emphasis was on social targets (maintaining employment levels, living standards, etc). Nonetheless, some parts of the 2009 playbook were re-used such as the rare issuance of the special treasury bond in light of the extraordinary circumstance. Most importantly, infrastructure investment is again a key thrust to stabilize the economy. CNY3.75trn of special local government bonds will be issued to spend on infrastructure and major projects including the "new infrastructure" such as 5G networks, electric-vehicle charging stations.

This resulted in the sharp rise in the local government bond issuance seen in May. For the past few years, the issuance of local government bonds in China tend to lift copper prices with an approximate lag of 5 months, a sign of the boost they give to commodity demand. China consumes half of global copper consumption as of 2019. The recent spike in local government bond issuance underscores the drive for infrastructure investment. China has also drawn down its copper inventory from its highs in Mar and copper prices have been on the up-move.

A Surge in LG bond issuance is Typically Followed by A Rise in Copper Price

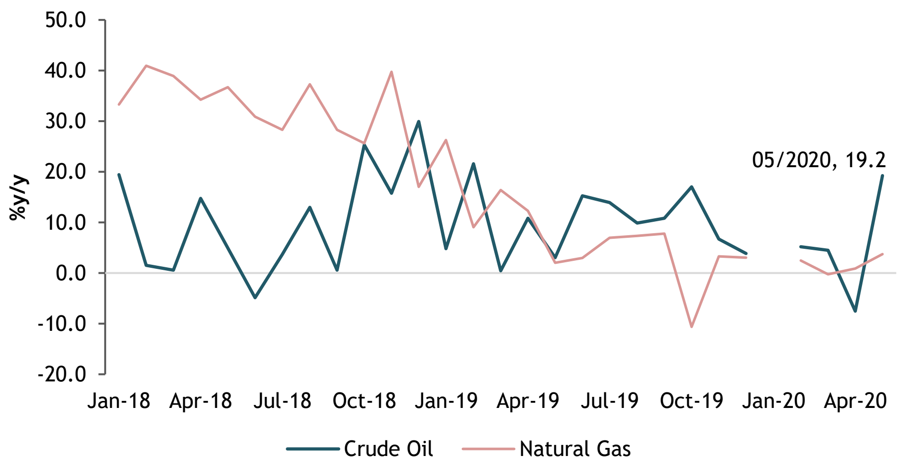


Source: Bloomberg, ChinaBond, Maybank FX Research & Strategy

Note: Copper Prices Are adjusted for a 5-month lag and first differenced to de-trend.

The Shanghai copper futures show a rather sharp increase in copper prices and the evidence in China's growing demand is also in the rebound of its import volume of oil and gas recently.

China's Volume of Oil and Gas Import Rebounds



Source: CEIC, General Administration of Customs, Maybank FX Research & Strategy

Along with the rise in China's domestic demand that could once again be at least partially investment-driven, ASEAN FX could once again benefit from export recovery of its commodities and food that China typically purchases from the bloc. While the upcoming infrastructure investment is not likely to be as significant as what was seen in 2009, ASEAN exports may still find support from the leading recovery in China and thatshould translate to more support for the ASEAN currencies in the medium term.

Differentiating Factors This Time Round

While part of the playbook this time round might resemble the recovery phase in earlier crises, we are also cognizant that there are several differentiating factors this time round (vs. past episodes) which could complicate the recovery.

We touched on them earlier, but will now look at them in greater detail.

- "Reopening", a development unique to the current pandemic, has been a major market theme underpinning recent market optimism. Is there room for it to drive further gains in regional FX?
- Unconventional monetary policy in the region is slowly beginning to attract attention. How has regional FX reacted to central bank bond purchase programmes and what is sentiment pricing in?
- One key risk factor that is more pertinent to the current recovery is the fragile state of the US-China relations. We examine how the relationship between ASEAN FX and CNY has evolved in recent years.

A mix of approaches (panel VAR analysis, conditional sensitivities) and alternative data (Google Trends, Oxford Covid-19 Government Response Stringency Index) will be utilized to value-add to the discussions.

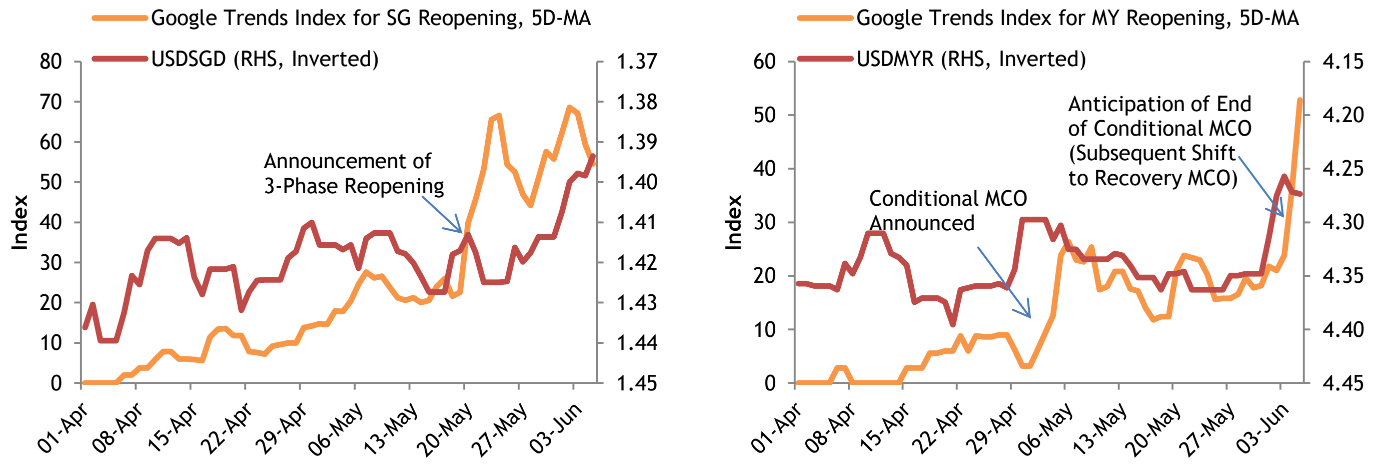
(i) Reopenings—Some Gains Likely Frontloaded, But Room for Modest Positivity

Sentiments are prone to swing when external conditions invert sharply. Arguably, the psychological impact of moving from "lockdown" to "reopening" is a highly significant shift in "narrative" for financial markets. We attempt to use Google Trends data to see if interest in opening up of regional economies has partly driven, or is associated discernibly with moves in regional currencies.

Google Trends data indicates the extent of interest in a particular topic based on what people are searching for online at a particular time. The data is expressed as an index—the date with the highest frequency of relevant searches will receive an index value of 100.

To gauge sentiments relating to the easing of lockdown restrictions in ASEAN, we extract Google Trends series associated with key phrases such as "Singapore reopening", "Malaysia reopening" etc. and smooth them using a 5-day moving average. This is then compared with FX moves.

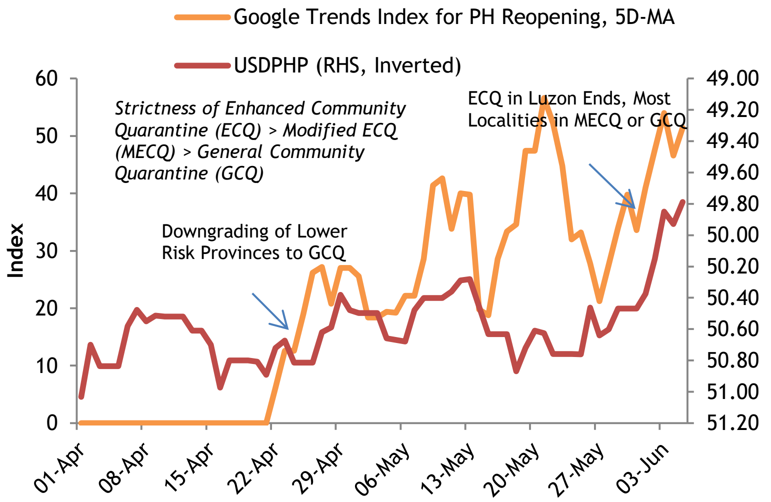
SG and MY: Reopening-related Announcements & FX Moves Largely in Lockstep



Source: Google Trends, Bloomberg, Maybank FX Research & Strategy

For Singapore and Malaysia, we note that reopening related announcements coincided with or slightly preceded episodes of recovery in currencies. For Singapore, it was announced in the third week of May that a three-phased recovery plan would be implemented from 2 June. In the first phase, an estimated three-quarter of economic activities would resume normal operations. In Malaysia, the Conditional MCO allowed most economic sectors to gradually re-open while observing enhanced social distancing procedures, and the Recovery MCO subsequently allowed interstate travel as well, except for areas placed under enhanced MCO.

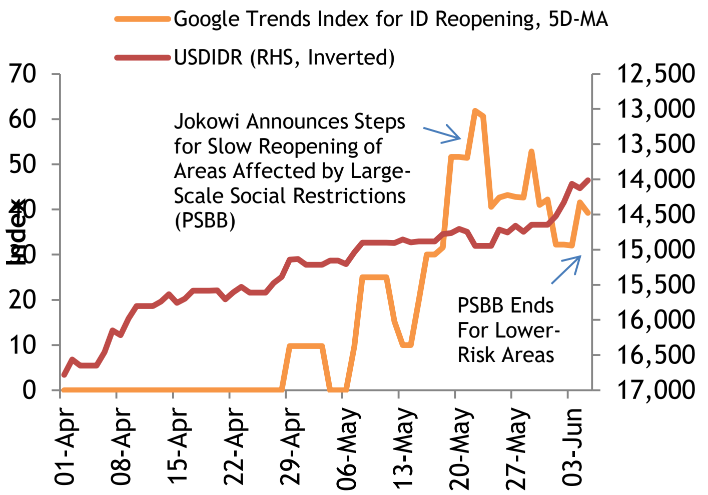
PH: Reopening Impact Positive, But Dispersed

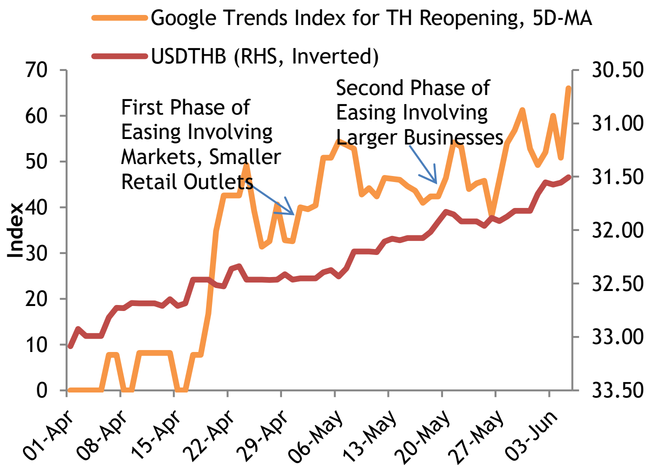


Source: Google Trends, Bloomberg, Maybank FX Research & Strategy

For Philippines, the impact of reopening was likely positive on sentiments, but appears somewhat "dispersed" over time. Differentiated levels of restrictions/easing across provinces, with differing timelines according to contagion considerations, likely contributed to this effect.

ID and TH: Reopening Announcements Mitigate Negativity But Not A Major Driver of FX

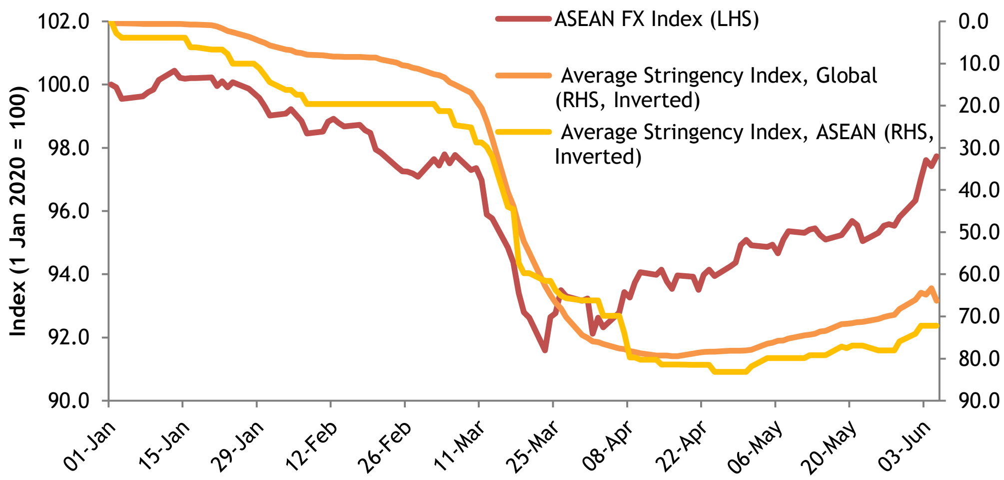




Source: Google Trends, Bloomberg, Maybank FX Research & Strategy

For Indonesia and Thailand, reopening announcements/policies do not appear to be a major driver of day-to-day FX moves, even as they likely helped to mitigate negative macro sentiments overall. Other considerations could be more pertinent for IDR (e.g., portfolio flows/carry) and THB (e.g., effective control of Covid-19 contagion, gold trading, signs of global easing in travel restrictions) over this period.

ASEAN FX Moves May Have Front-loaded Some Easing of Lockdown Restrictions



Source: ourworldindata.org, Oxford Covid-19 Government Response Tracker (OxCGRT), Bloomberg, Maybank FX Research & Strategy

Note: ASEAN FX Index is a simple average of the ASEAN FX-USD pairs.

For a broad sense of the pace of ASEAN FX recovery vs. easing in lockdown restrictions, we turn to the Stringency Index from the Oxford Covid-19 Government Response Tracker (OxCGRT) database. The index measures the variation in governments' Covid-19 containment and closure responses using a simple additive score of various indicators (school closures, workplace closures, travel bans, restrictions on gathering etc.) measured on an ordinal scale, rescaled to vary from 0 (least strict) to 100 (strictest).

We note that the trough of ASEAN FX weakness in late March largely coincided with the point when stringency of government responses tapered. Since then, as stringency (global average and ASEAN average) slowly loosened, ASEAN FX strength has recovered at a comparatively quicker pace.

We think that (i) given significant room for the stringency index to ease further, there is room for further gains in ASEAN FX as well, but that (ii) these gains could be more modest compared to the recovery over April to early June, as some front-loading of positivity on this front has likely occurred.

(ii) Unconventional Monetary Policy—Initial FX Reaction Mildly Positive, Long-Term Debt Monetization Concerns Not Priced In

Broad market consensus already sees public debt ballooning in 2020. As global lockdowns dent corporate earnings and add to job losses, governments around the world are responding with increasing levels of fiscal stimulus, largely with the intent of avoiding corporate closures and downward spirals in jobs and demand.

In part to help stabilize markets and provide much-needed financing for domestic stimulus, some regional central banks have embarked on bond purchase programmes, steps considered contentious in the pre-Covid era.

Within ASEAN, Malaysia was already allowed to purchase government bonds, limited to 10% of the issue size. Indonesia has started to make government purchases in the primary market, limited to 25% to 30% per auction. Thailand established a THB$400bn fund earlier, which enables the BoT to purchase high-quality corporate bonds. Philippines has purchased PHP300bn of government bonds directly from the Treasury under a three month repurchase agreement, which can be extended for another three months, and was also allowed to purchase government securities on the Secondary Market.

The following table (*extracted from a longer table compiled by the BIS*) shows a quick list of announcements relating to central bank bond purchase programmes in the region. India and Korea are included for comparison.

Announcements of Central Bank Bond Purchase Programmes In Mar & Apr

Country	Announcement Dates	Market	Type
Indonesia	01/4	Gov. Bonds	Outright
Philippines	10/4	Gov. Bonds	Outright
Thailand	19/3, 22/3, 07/4	Gov., Corp. Bonds	Outright
India	18/3, 20/3, 23/4	Gov. Bonds	Outright, Swap
Korea	19/3, 09/4	Gov. Bonds	Outright

Source: BIS
Note: Outright: Direct purchases by the central bank. Swap: Bond purchases financed through sales of short-term paper.

Broadly speaking, there may be two sets of sentiments effects associated with such announcements:

- Positive sentiments associated with more resilient investor confidence and greater ammunition to combat the Covid-19 macro drag on the economy.
- Negative sentiments associated with concerns over deteriorating fiscal discipline, market distortion, debt monetization.

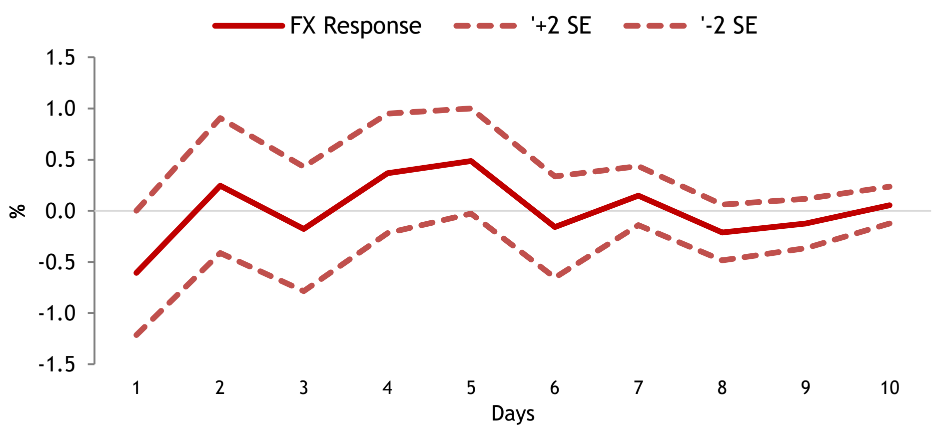
To investigate which of these effects have been priced in, we utilize a panel VAR model to gauge reactions to the announcements of these programmes. As per the table above, we include data for Indonesia, Philippines, Thailand, India, Korea. Daily data from March to April 2020 was utilized as the investigation focuses on announcements of bond purchase programmes concentrated over this period.

The model takes the form:

FX Change$_{i,t}$ = f(Policy Rates$_{i,t}$, Announcement Date Dummies$_{i,t}$)

A panel VAR allows us to extract the response of the "announcement" shock while taking into account the endogenous relationships between variables. Simply put, **we look at the average impact the announcements of bond purchase programmes had on FX,** while controlling for policy rates.

Mild Positive Impact on FX From Announcements In First Week



Source: Maybank FX Research & Strategy
Note: We look at the average FX impact for the first 10 (trading) days after policy announcements. A rising exchange rate denotes appreciation vs. USD.

On net, FX of countries introducing these programmes appreciated vs. USD by around 0.3% on average within 5 trading days. This effect then gradually dissipated towards the second week.

Interpretation: The sentiment impact of these programmes was mildly positive initially, and investor confidence in the "structural integrity" of the currencies was not visibly dampened. However, this may also imply that longer-term concerns over monetary/fiscal discipline, debt monetization have yet to be priced in.

One likely reason why market reaction has not been as adverse could be because central banks conducting such operations often emphasize their role as buyer of last resort. If this covenant were to be breached, the impact on sentiments could be severe. Furthermore, such actions by regional central banks are occurring at a time when other major global central banks are "throwing the kitchen sinks" at markets too. The level of concern could be quite different later on if major central banks begin to unwind their unconventional monetary policy before the Asian central banks do.

More broadly, we think that eventual concerns over such actions by regional central banks could also be part of broader worries over funding stresses, depending on whether post-Covid recoveries proceed smoothly. We had looked at this in more detail in an earlier report (*Risks To Be Mindful Of*).

(iii) US-China Relations—ASEAN FX Sensitivity to CNY Depends on Channel of Shock; Still More "Bark" Than "Bite"?

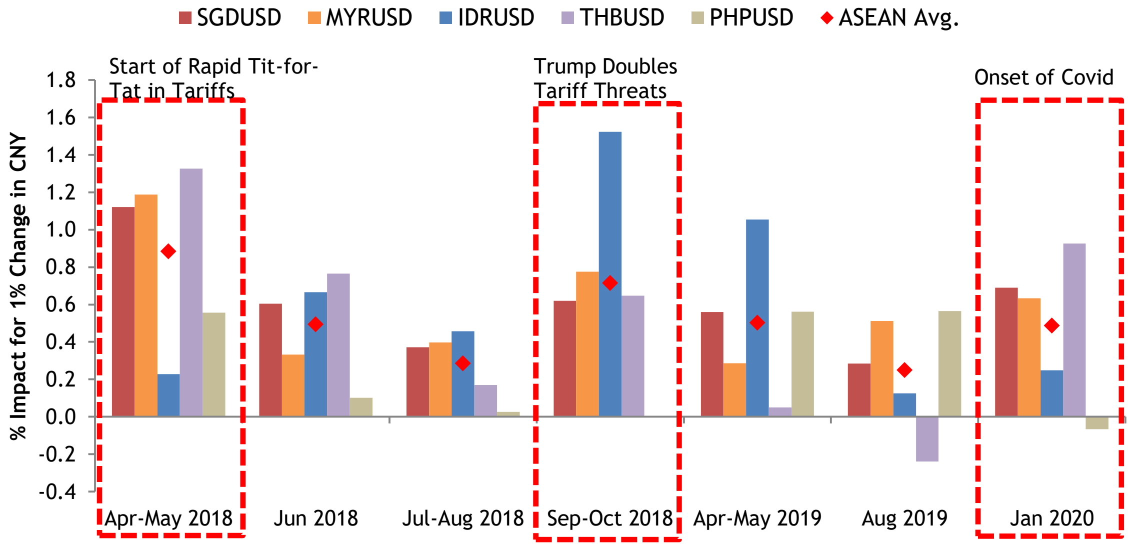
One key difference from past crises in the current recovery phase is the finger-pointing and fragile relations between US and China. USDCNH has retreated significantly from the recent high of 7.1965 observed in late May, but remains above the psychological 7-level. This is still somewhat higher than the recent low of near-6.90 in early March, after China successfully brought the Covid-19 contagion under control.

At this point, we think that markets seem to be pricing in a certain degree of continued spat between the two major powers, through verbal accusations or minor sanctions on officials/entities, but largely view severe derailment of the Phase 1 trade deal as less likely.

Here, we investigate how the influence of CNY on ASEAN currencies has evolved over time using conditional sensitivities. We do this by extracting episodes of relatively sharp CNY weakness over 2018 to early 2020, defined as CNY declining by around 2% or more vs. USD over a relatively short time, before computing the sensitivity of individual ASEAN FX to CNY in each episode. I.e., how much did regional FX decline for a 1% decline in CNY?

We avoid deriving the sensitivities for Mar-May 2020 given that figures are likely to be immensely skewed—CNY was relatively stable over this period aside from the occasional reaction to US threats, while ASEAN FX saw sharp V-shape moves.

Impact on ASEAN FX is Larger when there is a Shock to Expectations



Source: Bloomberg, Maybank FX Research & Strategy

Note: Sensitivities are measured for exact periods in between local-peaks and troughs for CNH. Labelling in chart is simplified; e.g., Jun 2018 actually refers to 16 Jun to 2 Jul 2018.

Broadly, the extent of shock to expectations and the channel of shock matters in influencing the sensitivity of ASEAN FX to CNY. The highlighted episodes (red dotted lines) with larger sensitivities on net were arguably periods of sharp shifts in market expectations.

Apr-May 2018: Rapid Tit-for-tat Escalation in Tariff Action with Signs of Conflict Broadening to Tech Sphere

Date	Events
Apr 2, 2018	China imposes tariffs (ranging 15-25 percent) on 128 products (worth US$3 billion) in retaliation to earlier US' steel and aluminium tariffs.
Apr 3, 2018	The USTR releases an initial list of 1,334 proposed products (worth US$50 billion) subject to a potential 25 percent tariff.
Apr 4, 2018	China reacts to USTR's initial list, and proposes 25 percent tariffs to be applied on 106 products (worth US$50 billion).
Apr 16, 2018	US Dept of Comm. concludes Chinese telco ZTE violated US sanctions. US companies banned from doing business with ZTE for seven years.
May 3-7, 2018	US-China engage in trade talks in Beijing, where the US demands that China reduce the trade gap by US$200 billion within two years.
May 29, 2018	US reinstates tariff plans after brief truce.

Source: china-briefing.com

Sep-Oct 2018: Trump Doubles Tariff Threats, China Cancels Talks

Date	Events
Sep 7, 2018	Trump threatens to impose tariffs on US$267 billion more, which would bring total tariffs threatened or imposed by the US on China to US$517 billion, accounting for essentially all Chinese exports to the US.
Sep 17, 2018	The USTR announces the finalized list of tariffs on US$200 billion worth of Chinese goods, to go into effect on Sep 24 at an initial rate of 10 percent, then increased to 25 percent by Jan 1, 2019.
Sep 18, 2018	China announces that it will implement tariffs on US$60 billion worth of US goods.
Sep 22, 2018	China cancels trade talks with US.
Oct 30, 2018	Reiteration of US threat to impose tariffs on all remaining Chinese products by early Dec if talks between Trump and Xi at the G20 are not successful.

Source: china-briefing.com

The third highlighted episode, onset of Covid from mid-Jan 2020, highlights in particular how the channel of sentiment shock matters for FX sensitivities. At the start of Covid, major concerns were different from those pertinent to tariff threats. Markets could have been looking at asset exposure to factors such as (i) tourism flows and (ii) China's domestic demand.

FX Sensitivity At Covid Onset Influenced by Tourism, China Demand Concerns

	Tourism China Visitors' Share	Tourism Receipts as % of GDP	Exposure to China's Domestic Demand (% of GDP)	Sensitivity to CNY at Onset of Covid	Avg. Sensitivity to CNY (2018-Jan 20)
SGD	15%	6%	8%	0.7%	0.6%
MYR	15%	6%	9%	0.6%	0.7%
IDR	14%	2%	3%	0.2%	0.6%
THB	28%	12%	7%	0.9%	0.4%
PHP	18%	2%	4%	0%	0.2%

Source: CEIC, Bloomberg, OECD-TiVA Database, Maybank FX Research & Strategy

Note: Deeper shade of red indicates higher exposure to highlighted channels or higher sensitivity to CNY. "Covid onset" refers to period from 17 Jan to 3 Feb 2020, i.e., local peak to trough in CNYUSD. *Computed by OECD by decomposing the actual input of each country in the production of goods & services consumed worldwide. Latest data point is 2015 due to complexity of calculations.

While the shock did start off via CNY, fears of a sudden stop in the flows of tourism demand for THB had disproportionately dampened THB demand. Thailand's dependence on tourism receipts is the highest among regional peers (at more than one-tenth of its GDP) and more than a quarter of tourist arrivals are from China. As a result, the sensitivity coefficient for THB in this episode (0.9%) was around double that its average sensitivity to CNY for past episodes (0.4%). In contrast, the initial sensitivities of IDR and PHP to CNY shocks in Jan 2020 were lower than average of past episodes due to their perceived lower tourism and domestic demand linkages with China. These underscore the point that the channel of sentiment shocks has a significant influence on ASEAN FX sensitivities.

Moving to the present, over the past couple of months, we witnessed a host of hostile exchanges and actions that included 1) a bill passed by the US Senate that could see Chinese companies delist in the US stock exchanges and drove JD.com and Netease to apply to list on HKEX, 2) a bill passed by the Congress to impose sanctions on Chinese officials involved in the repression of Uighurs in Xinjiang and 3) curbing Huawei's ability to use US technology and equipment made overseas to manufacture semiconductors for their products; 4) the cancellation of plans (under the pressure of the White House) for the Federal Retirement Thrift Investment Board to invest in index funds that include Chinese shares; 5) threats of sanctions on officials, entities that enforce the new national security law enacted for Hong Kong by China along and above all 6) blaming China for the COVID-19 pandemic. On these, the Huawei risk factor is not a new threat, while reactions in sentiments to the rest of the piece-meal announcements were also largely modest.

It was also apparent that the US and China are still eager to keep phase 1 of the Trade Deal. The two nations' trade negotiators were quick to have a phone call on 8 May (Asia morning) and came to the consensus that "both countries fully expect to meet their obligations under the agreement in a timely manner". China also reiterated its pledge to implement the phase 1 of the trade deal at the Two Sessions. In addition, USTR Lighthizer told Fox News on 4 Jun that he is satisfied with the progress of the phase 1 deal and China has done a "pretty good job" at keeping to their commitments.

Without a breakdown of the Phase 1 trade deal, there may be a lack of a clear channel for pessimism to entrench more aggressively.

Conclusion

Drawing on lessons from the past, looking at the known positives being taken into consideration and the sharp rebound in equity markets (S&P 500 rallied more than 40% from Mar-2020 troughs), it may appear that the current recovery in ASEAN FX so far may have been adequately priced for now. There could be room for further gains, but this could come after a temporary phase of consolidation—as near-term concerns (second wave contagion, drag on global jobs markets) play out.

Structurally, the simultaneous use of twin stimulus on such a global scale is unprecedented, and combined with low-for-longer US rates, softer USD environment, a more durable global economic recovery could kick in. Cyclical proxy-FX including ASEAN FX could stand to benefit further. In particular, China's focus on infrastructure investment as a way to stimulate demand could help in part to boost ASEAN's exports, not unlike what we have seen in post-GFC 2009-2011 (albeit on a smaller scale without the aggressive credit easing seen then).

Interestingly, there are certain aspects of the current recovery which differ discernibly from earlier episodes.

- On the unique boost that "reopenings" are giving to ASEAN FX, there is likely room for more support to currencies on this front, as we have yet to cross the half-way mark (around two-thirds of restrictions remain in place for ASEAN on average). Nonetheless, gains ahead could be more modest compared to the pace seen in April to early June, as some front-loading of positivity on this front has likely occurred.

- Unconventional monetary policy is also a somewhat new phenomenon for regional central banks. On these, we find that the initial impact of bond purchase programmes on the currencies of these countries was actually mildly positive. I.e., investor confidence in the "structural integrity" of the currencies has yet to be visibly dampened by concerns over monetary/fiscal discipline, debt monetization etc.

- The current recovery phase is complicated by constant headlines on the US-China spat. We look at episodes of CNY weakness over 2018-20 and find that reactions of ASEAN FX vary significantly depending on the sentiment channel in play. While the potential for escalation is intact, without a breakdown of the Phase 1 trade deal, there may be a lack of a clear channel for pessimism to entrench more aggressively.

On net, while ASEAN FX could consolidate in the interim, it still has the potential to take another leg higher, barring any risk of second wave covid infection and sino-US tensions taking an unexpected turn. Our bias at this point is to sell USD-ASEAN pairs on rallies.

Lastly, given that recent volatility in USD-ASEAN pairs has been driven partly by broad dollar moves, it would be remiss of us not to mention developments on the US front. Broadly, we retain our bias for weaker USD on the back of multitude of reasons—US is still a covid-19 epicentre, now with risks of second wave infection, potential political risks in the lead up to US Presidential elections in Nov 2020, massive and increasing Fed's balance sheet amid QE, deteriorating twin deficits, chatters of reserve diversification or reallocation away from USD, as well as USD counter-cyclical factor kicking in. But also noting that USD lower is not a one way bet, as 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 environment, where there are risks of second wave infection, sino-US tensions re-escalating, etc., there will still be demand for USD for funding/liquidity purposes and this could still serve to mitigate USD downside pressure.

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