Ringgit Outlook

Further downside seen following US Treasury decision to include Malaysia in currency manipulators' watch list

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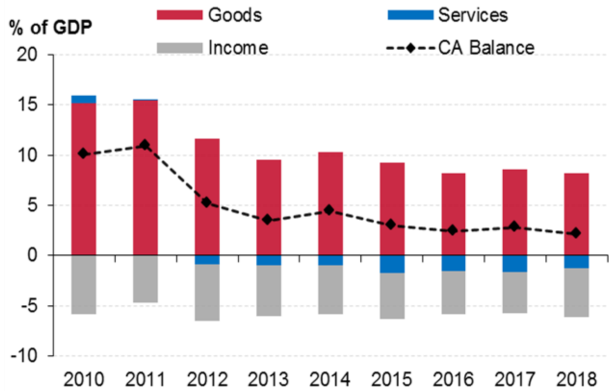
OVERVIEW

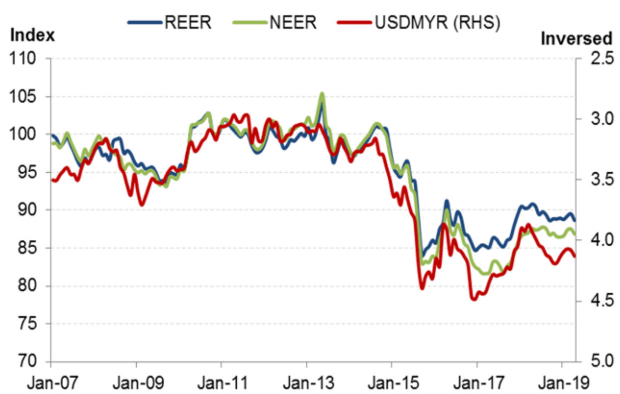
- **Another knock on effect**. The US Treasury's decision to include Malaysia in the Monitoring List of Potential Currency Manipulator would weigh on the Ringgit in the short to medium term. The move has compounded the impact brought about by the decision to potentially exclude Malaysia from the FTSE Russell World Government Bond Index announced last month. The decision hastens the USDMYR to reach a six-month low of 4.20 after months lingering in the 4.00-4.19 range. Ringgit has depreciated by about 2.0% against the USD since it passed the 4.10-mark on 10th April.
- The much-anticipated decision came as **no big surprise** as the US, under Donald Trump's presidency, is determined to exert its protectionist stance on trade. Furthermore, Trump has been using the foreign-exchange policy as a tool to rewrite global trade rules in the pretext of protecting US businesses and jobs in a bid to win support for his re-election in 2020. The US, however, spared China the currency manipulator label but it remains in the watch list. This may have been to avoid further escalation in the on-going protracted US-China trade negotiation.
- **Expanded list**. In the semi-annual foreign-exchange report to Congress, the US Department of Treasury Office of International Affairs expanded the potential currency manipulator to nine from five while none was named a manipulator. No major trading partners were labelled a manipulator since 1994. Malaysia is among the five new entrants, including Ireland, Italy, Vietnam and Singapore. The incumbents were China, Japan, South Korea and Germany while India and Switzerland were removed. The rise in the number of countries in the list mainly reflects the Treasury Secretary Steven Mnuchin's decision to expand the number of major trading partners covered in the report, as well as to revise thresholds for the three eligibility criteria (refer to Table 1). Of note, a minimum of two of the three criteria has to be met in order for a country to be included into the list. A country will remain on the list for a minimum of two consecutive reports, before it stands the chance to be removed, in ensuring sustained improvement in performance with regards to the said criteria.
- **Ensuing the revision of thresholds, 21 economies, including Malaysia has fallen under the major trading partner coverage,** given that its goods trade with the US registered at USD 52.2b in 2018, above the threshold of USD 40.0b. As extracted from the official report, Malaysia met two of the three criteria, specifically a goods surplus exceeding USD 20.0b (Malaysia: USD 26.5b) and a current account balance surpassing 2.0% of GDP (Malaysia: 2.1%), rendering its inclusion into the Monitoring List. Of significance, technically, Malaysia was not perceived as a currency manipulator, premising on the fact that though BNM intervened in the currency market, it was executed in a two-sided manner, curbing both appreciatory and depreciatory pressures to the Ringgit, as opposed to a persistent one-sided intervention, an act heavily detested by the US. With net sales of foreign exchange amounting to 3.1% of GDP in 2018, Malaysia did not meet the criteria of having net foreign exchange purchases of 2.0% of GDP.
- **BNM's defence**. In response to US Treasury's decision, Bank Negara stressed that it "does not practice unfair currency practices." Though it somewhat admitted the part on intervention in the forex market, BNM, however, explained that it has been in both directions over the last few years, concurring the US Treasury report, and "is limited to ensuring an orderly market and avoiding excessive volatility".
- **Ringgit Outlook.** While there is a chance that Malaysia might be taken off the list in a year or so, it still needs to contend with the unfavourable perception of investors in the next three to six months. Coupled with the uncertainty over the impact of the protracted US-China trade negotiation as well as an increasingly dovish US Federal Reserve, we expect the USDMYR to hover between 4.15 and 4.25 in the short term. Though we still believe the Ringgit is relatively undervalued, the challenge is for the Government to restore confidence and ensure a clearer policy direction going forward. Nonetheless, we reckon the US Treasury decision to see the Ringgit as a potential threat does not change its underlying fundamental support. Hence, we are maintaining our USDMYR year-end forecast of 4.10.

Graph 1: Current Account Balance



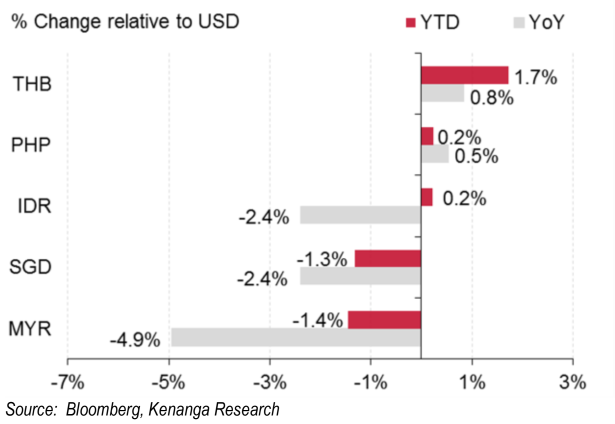
Source: Dept. of Statistics, CEIC, Kenanga Research

Graph 2: Malaysia Exchange Rates



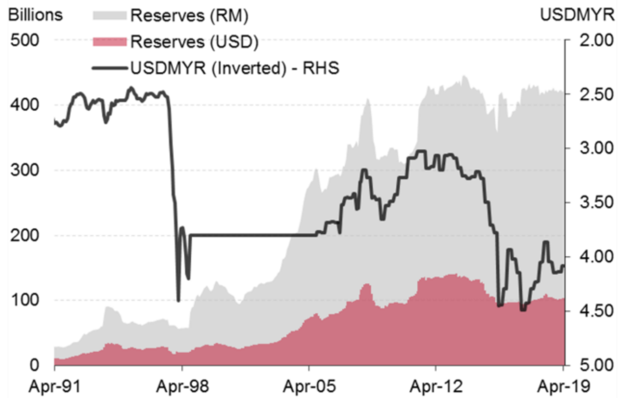
Source: BIS, Kenanga Research

Graph 3: Currency Performance



Source: Bloomberg, Kenanga Research

Graph 4: BNM Forex Reserves



Source: BNM, Bloomberg, Kenanga Research

Table 1: New Treasury Thresholds under the 2015 Act

Criteria	Benchmark	Previous Threshold	New Threshold	Malaysia's Position as of 2018
Major trading partner coverage	Total bilateral goods trade (imports plus exports)	12 largest trading partners	USD 40.0b	USD 52.2b
1) Significant bilateral trade surplus with the US	Goods surplus with the US	USD 20.0b	USD 20.0b	USD 26.5b
2) Material current account surplus	Current account balance	3.0% of GDP	2.0% of GDP	2.1% of GDP
3) Persistent, one-sided intervention in foreign exchange markets	Net FX purchases	2.0% of GDP	2.0% of GDP	Net FX sales of 3.1% of GDP
	Persistence of net FX purchases	8 of 12 months	6 of 12 months	n.a.

Source: US Department of the Treasury Office of International Affairs, Office of the US Trade Representatives

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