Asia FX Monthly Outlook

China zero-COVID policy and interest rate divergence to weigh on Asia FX

CNY (7.092) ▼

- CNY strengthened for the first time in nine months against the USD, appreciating by almost 3.0%, mainly due to the DXY's descent from peak 114.1 (Sep 26) to as low as 106.0 (Nov 30) amid Fed's dovish signal and China's reopening optimism. However, the ongoing China's COVID-19 protests has been hurting risk sentiment, weighing on the yuan.
- The growing public unrest in China, coupled with the People's Bank of China's easing monetary policy stance may continue to induce capital flows out of China and hurt the yuan. Hence, we expect the CNY to hover around the 7.10 – 7.30 level in December. However, the narrative will completely shift if President Xi Jinping puts an end to his zero-COVID policy.

JPY (138.840) ▼

- JPY appreciated to its strongest level since August 2022, primarily due to a broadly weak USD. The yen was also lifted by a significantly higher Japanese core inflation print of 3.6% in October (Sep: 3.0%), its highest in 40 years, although Bank of Japan (BoJ) governor Kuroda stressed that rates would remain accommodative going forward.
- JPY may weaken slightly in December as the monetary policy divergence between the BoJ and US Fed widens as the latter is broadly expected to raise rates by another 50 basis points (bps). However, the yen may still find some support from renewed safe-haven demand as investors turn cautious on positions in China amid its worsening COVID-19 condition and civil unrest.

MYR (4.446) ▼

- The depreciation of the USD index by 5.0% due to dovish Fed signals has helped the ringgit to reverse most of its losses against the greenback. Domestically, the ringgit was partly supported by the appointment of Datuk Seri Anwar Ibrahim as Malaysia's 10th prime minister, after five days of election stalemate.
- The ongoing nationwide social unrest in China, coupled with global market uncertainty may reduce investors' risk appetite and push the ringgit to trade around the 4.45 - 4.55 level against the USD in December. However, the ringgit may benefit from Fed's Powell recent dovish remarks, USD seasonal weakness and Malaysia's façade of political stability.

IDR (15,732) ▲

- IDR depreciated marginally in November, mainly due to risk-off sentiment surrounding the resurgence of COVID-19 cases in China and a protest over its zero-COVID policy. Nonetheless, the weakness was partially mitigated earlier by Bank Indonesia's (BI) rate hikes decision while partly supported by the less hawkish US Fed following the release of its minutes.
- We still expect IDR to rebound in December, as the US Fed is expected to pivot towards slower rate hikes going forward. Nonetheless, the upside bias may likely be limited given the increase in rates differentials and growing fears of China's economic slowdown amid its prolonged zero-COVID policy.

THB (35.268) ▼

- THB strengthened in November on broad USD weakness as markets continued to expect a less hawkish US Fed. The baht was also driven by Thailand's strong growth momentum, with 3Q22 GDP advancing to 4.5% YoY (2Q22: 2.5%), underpinned by sustained tourism recovery and robust domestic demand.
- THB may weaken slightly in December, dragged by a weaker CNY amid China's surge in COVID-19 cases, and by the US Fed's likely 50 bps rate hike. With that said, baht weakness should be tempered by the Bank of Thailand's own 25 bps rate hike and Thailand's sustained growth momentum.

Table 1: Currencies Outlook

	Long Term*					
	Q3-22	Q4-22F	Q1-23F	Q2-23F	Q3-23F	OUTLOOK
USDCNY	7.116	7.216	7.391	7.154	6.837	▲
USDJPY	144.740	138.743	138.897	136.334	136.502	▼
USDMYR	4.638	4.542	4.643	4.510	4.357	▼
USDIDR	15227	15664	15430	15200	14973	▲
USDTHB	37.847	35.257	34.278	33.514	33.421	▼
USDPHP	58.650	56.596	52.879	51.837	51.832	▼

	Short Term (Technical)					
	EMA (21)	R1	R2	S1	S2	OUTLOOK
USDCNY	7.159	7.247	7.402	6.991	6.890	▲
USDJPY	141.374	145.487	152.133	134.997	131.153	▲
USDMYR	4.573	4.647	4.848	4.345	4.245	▲
USDIDR	15649	15818	15905	15570	15409	▼
USDTHB	36.224	37.101	38.933	34.352	33.435	▲
USDPHP	57.341	58.082	59.572	55.847	55.102	▲

Signal for USD Trend = ▲ Bullish — Neutral ▼ Bearish
**F=Forecasts for end of period*
Source: Kenanga Research, Bloomberg

EMA (21): 21-day Exponential Moving Average
EMA gives more weight to the most recent periods, places more emphasis on what has been happening lately. Old data points retain a multiplier even if they are outside of the selected data series length.

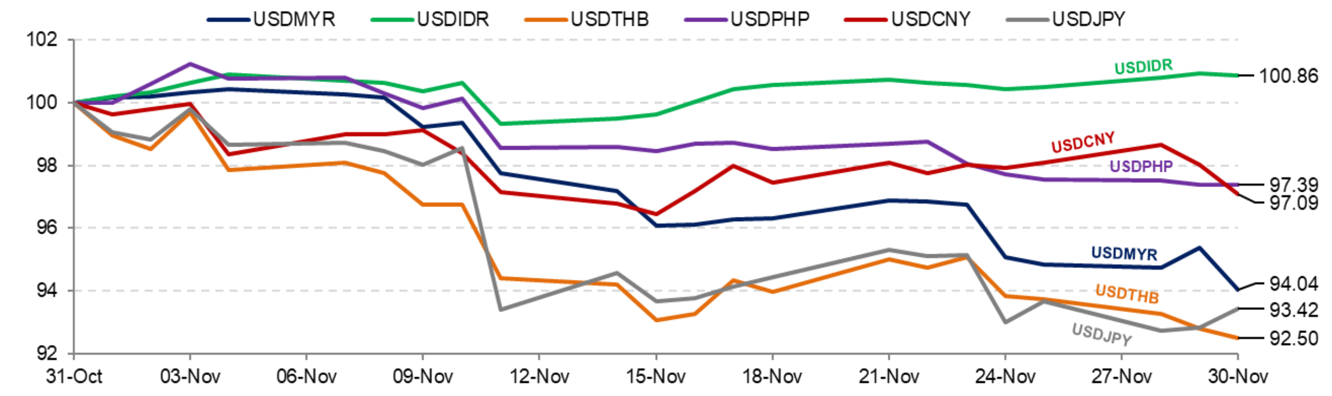
$$EMA = (P \times \alpha) + [Previous\ EMA\ \times (1 - \alpha)]$$

Table 2: Upcoming Major Data Release

Date	Currency	Indicator
01/12/2022	MYR	PMI (NOV)
01/12/2022	THB	PMI (NOV)
01/12/2022	IDR	PMI (NOV)
01/12/2022	IDR	Inflation (NOV)
06/12/2022	THB	Inflation (NOV)
07/12/2022	CNY	Trade (NOV)
08/12/2022	JPY	GDP (Q3)
09/12/2022	CNY	Inflation (NOV)
09/12/2022	MYR	Retail Sales (OCT)
09/12/2022	MYR	Industrial Production (OCT)
09/12/2022	IDR	Retail Sales (OCT)
12/12/2022	IDR	Unemployment (OCT)
15/12/2022	JPY	Trade (NOV)
15/12/2022	CNY	Industrial Production (NOV)
15/12/2022	CNY	Unemployment (NOV)
15/12/2022	IDR	Trade (NOV)
19/12/2022	MYR	Trade (NOV)
20/12/2022	JPY	Interest Rate Decision
22/12/2022	THB	Trade (NOV)
22/12/2022	IDR	Interest Rate Decision
23/12/2022	JPY	Inflation (NOV)
23/12/2022	MYR	Inflation (NOV)
27/12/2022	JPY	Unemployment (NOV)
27/12/2022	JPY	Retail Sales (NOV)
28/12/2022	THB	Industrial Production (NOV)
30/12/2022	MYR	Money Supply (NOV)
30/12/2022	THB	Retail Sales (OCT)

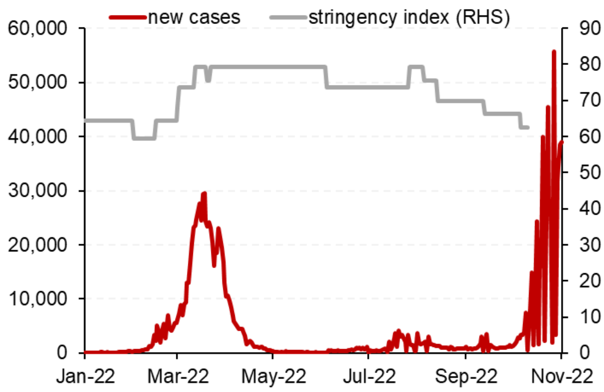
Source: Kenanga Research, Trading Economics

Graph 1: Monthly Asia FX Indices Trend



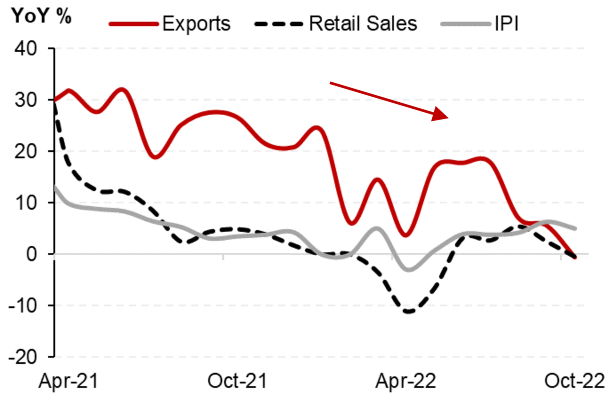
Source: Kenanga Research, Bloomberg

Graph 2: China COVID-19 cases and stringency index



Source: Kenanga Research, Our World in Data

Graph 3: China's Key Macroeconomic Indicators



Source: Kenanga Research, CEIC

Surging COVID-19 cases, lockdown protests, and monetary policy divergence in China to weigh on Asian currencies

- China continues to record an increase in COVID-19 infection amid nationwide zero-COVID policy protests following a deadly fire in an apartment building in Xinjiang blamed on strict lockdown measures. The latest data showed local infections totalled around 39.0k on Monday, 28th November, slightly lower than the previous day of 38.5k. The recent surge in infections have prompted tighter security and lockdown measures to contain the outbreak, which is likely to result in weaker GDP growth going forward.
- On 25th November, the People's Bank of China reduced the reserve requirement ratio for most banks by 25 bps, injecting CNY500.0b (USD70.b) of liquidity into the economy. This is the second time the central bank slashed reserve requirements to support the domestic economy hit by surging COVID-19 cases and a prolonged property market slump. Of reference, China's latest key macroeconomic indicators are pointing to a slowdown at the start of 4Q22, with IPI slowed to 5.0% YoY in October (Sep: 6.3%), exports contracted by 0.6% (Sep: 5.6%), its lowest in 29 months, while retail sales declined by 0.5% (Sep: 2.5%). The near-term outlook is likely to remain weak, as reflected by the official manufacturing PMI, which fell to 48.0 in November (Oct: 49.2).
- Given the bleak economic outlook amid sustained economic pressures and the global economic slowdown narrative, we believe there is room for China to further loosen its monetary policy in 2023 by slashing its key loan prime rate. This, in turn, would further weakened the yuan due to the divergence in the monetary policy with the US, raising fears of an economic slowdown amid the uncertainty of its zero-COVID policy. This may trigger further capital outflows and create a domino effect on other Asian currencies.

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