



## **Asia monthly update January**

**Is there any currency manipulator in Asia?**

Amy Y. Zhuang, Chief Asia Analyst  
20 February 2017

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## Executive summary

- In early February, Donald Trump accused China and Japan of currency manipulation. Associated with his campaign promise to brand China a currency manipulator on his first day in office, the market remains deeply worried that Trump could use this as a justification for introducing punitive trade actions against China.
- In the next two pages we discover that China does not qualify as a currency manipulator, using the US' own criteria. In fact, no country in Asia can be justifiably called that.
- Nonetheless, the fact will not necessarily stop Trump in carrying out protectionist policies. Economic nationalism is set to rise in the US. It continues to pose a large growth risk to the export-dependent economies in Asia. Thus, we remain cautious on these currencies.
- We also look pessimistically at the MYR due to the country's large and rising external funding need and the sensitivity to the USD strength.
- Our relatively bearish picks : SGD, KRW, TWD and MYR
- Our relatively bullish picks: INR and THB

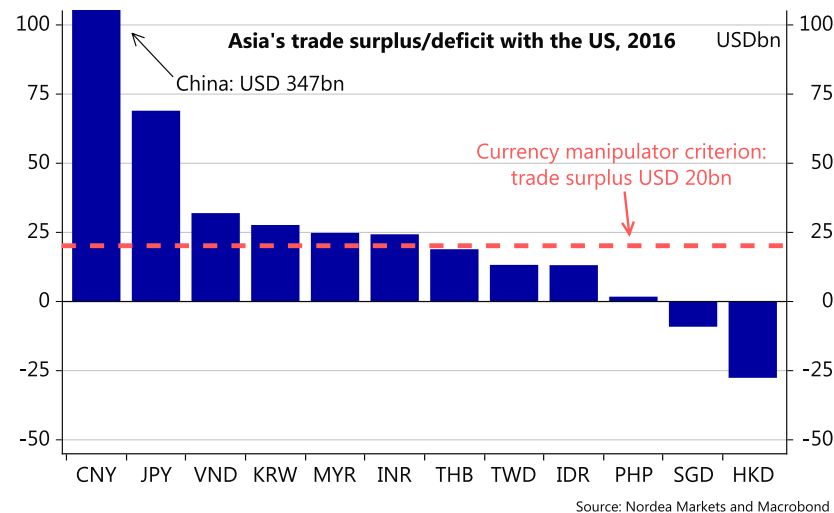
## Asia: Is there any currency manipulator in Asia?

- In early February, Trump accused China and Japan for currency manipulation. We use the three criteria made by the US Treasury:

- 1) Bilateral trade surplus with the US,  $\geq$  USD 20bn within the past year
- 2) Current account surplus  $\geq$  3% of GDP
- 3) One-sided FX intervention by net purchasing FX for more than 2% of GDP during the past year

- No country in Asia fulfills all three criteria and five (out of 12) satisfy two criteria: HKD, KRW, JPY, THB and VND.

- So even if Trump decides to label some Asian country a currency manipulator, it should not be China. In fact, Beijing has spent billions of dollar during the past year preventing the currency from falling too much.

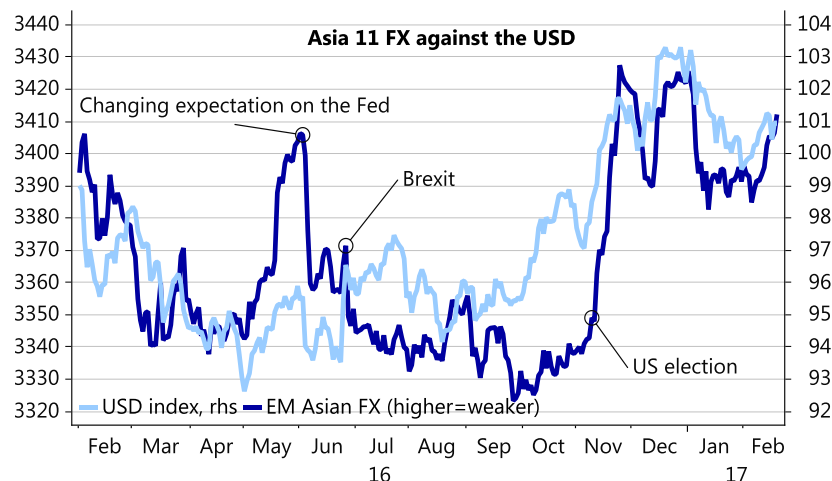


Currency	Criterion 1 Trade surplus $\geq$ USD 20bn	Criterion 2 C/A surplus $\geq$ 3% of GDP	Criterion 3 FX purchases $\geq$ 2% of GDP
CNY	x		
HKD		x	x
IDR			
INR	x		
JPY	x	x	
KRW	x	x	
MYR	x		
PHP			
SGD		x	
THB		x	x
TWD		x	
VND	x		x

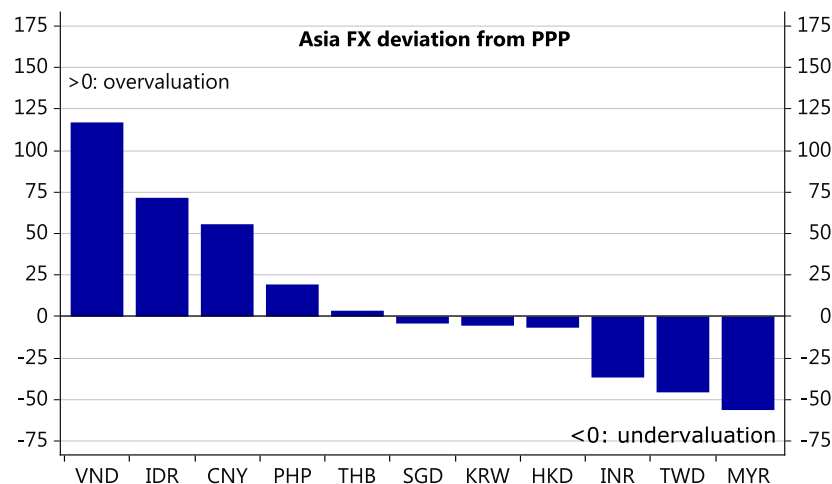
\*Source: Nordea

## Asia FX: Tracking the USD

- So far in February, the Asian FX has not performed well as a whole. This was a result of the USD's renewed strength after losing steam in January.
- We do not see much upsides for Asian FX this year as market sentiment could turn to risk off due to uncertainty. Elections in core Euro area, such as Germany and France, add more political uncertainty to the one already in the US.
- Trump has attacked China as currency manipulators, a statement that could not be supported by the US Treasury's own criteria (see previous page). In fact, the CNY is overvalued by our calculation.
- The MYR, TWD and INR are undervalued but there has been no sign that it was a result of government intervention.



Source: Nordea Markets and Macrobond



Source: Nordea Markets and Macrobond

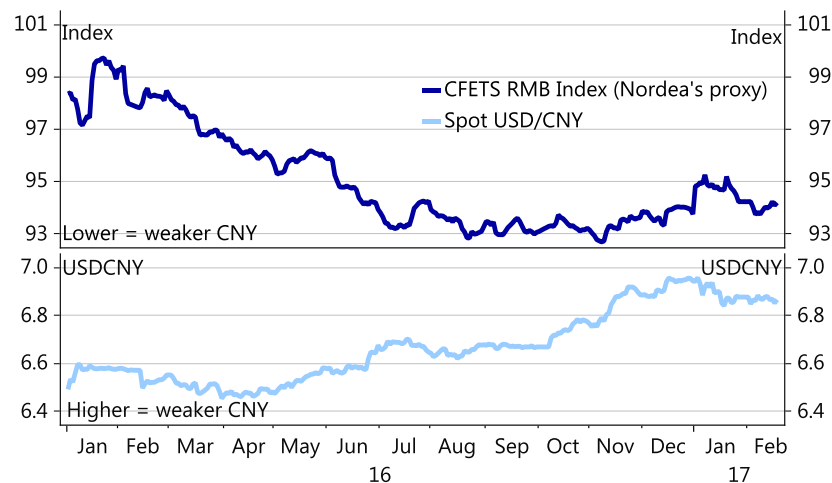
## China: Growth to face renewed pressure this year

- The current growth momentum is strong and likely the best in years. This is confirmed by the PMI for manufacturing, which is close to a three-year high.
- Annual GDP growth suggested that the recovery happened in Q4, as growth was 6.8% and higher than previous quarters. But quarterly growth of 1.3%, 1.9%, 1.8 and 1.7% indicates that the economy started bounce up already in Q2.
- The 2017 growth target will most likely be 6.5% again. At the same time, we expect the economy to face renewed downward pressure this year as the housing market is cooling down. It implies that Beijing will have to stimulate the economy even harder this year to achieve the growth target. This could worsen the existing credit-fuelled investment bubble.

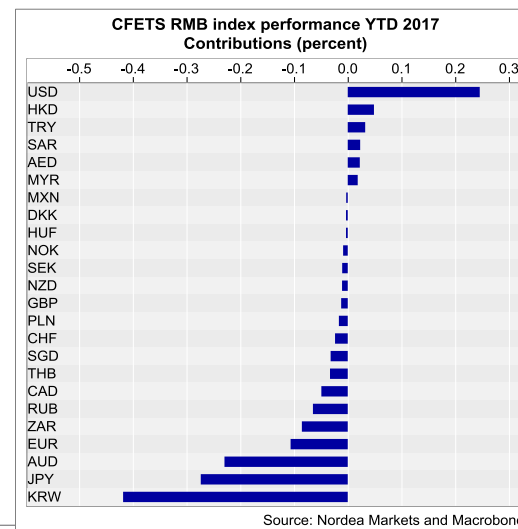


## CNY: No competitive devaluation

- In January and the first week of February, the CFETS RMB index, i.e. the CNY against a basket of 24 currencies, has weakened, raising concerns about Beijing starting a currency war.
- We do not think it was the case. A weaker USD pushed most currencies higher in January. Although the CNY has gained 1.5% versus the USD, other currencies have gained more, such as the KRW (4.9%) and AUD (5.2%). It implies a broad-based weaker CNY.
- We maintain the view that China has no interest in a currency war as it would undermine China's efforts in promoting itself as free trade supporter. On the other side, Beijing does not want lose competitiveness. Thus, the CFETS RMB index will likely remain at 94-95.



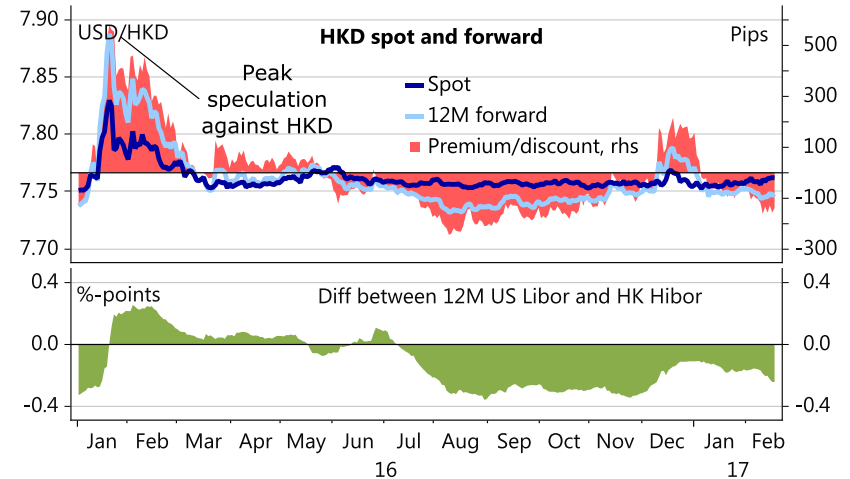
Source: Nordea Markets and Macrobond



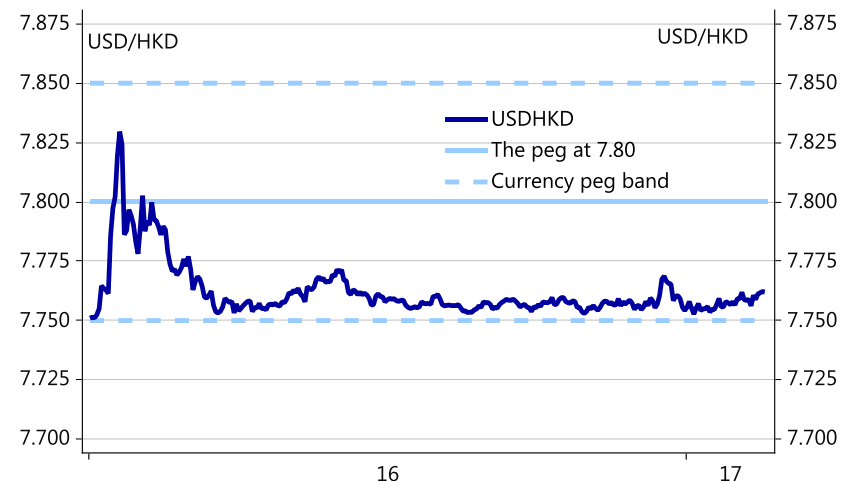
Source: Nordea Markets and Macrobond

## HKD: Continued interest rate dilemma

- Hong Kong continues to face a dilemma with the island's interest rate. On the one hand, if rates stay low relative to the US it would trigger more capital outflows. It also implies persistent HKD forward discount, as it has been the case since August 2016, except for in December.
- On the other hand, higher rates in Hong Kong raise concerns about the island's overheated stock and property markets.
- Since the Chinese New Year in late January, stock market inflows from mainland China via the Shanghai- and Shenzhen-Hong Kong Stock Connect have helped improving liquidity in Hong Kong and lowered the Hibor rates.
- The HKD is still trading close to the lower side of the pegged band to the USD.



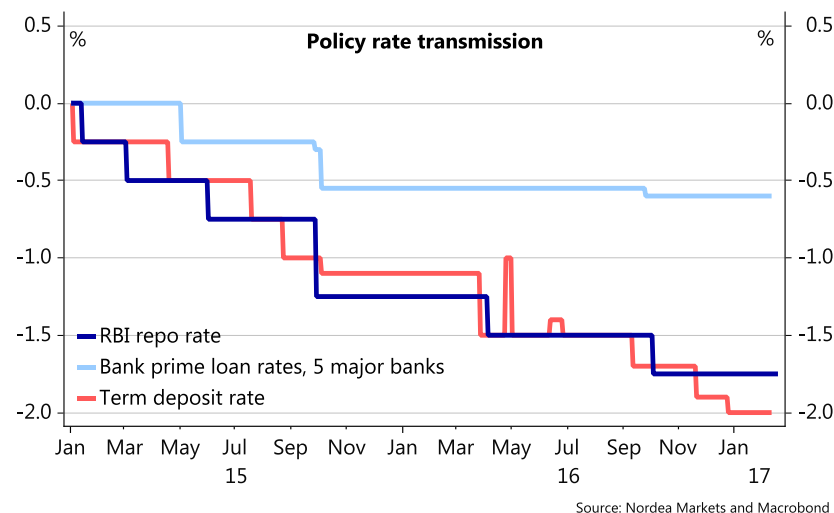
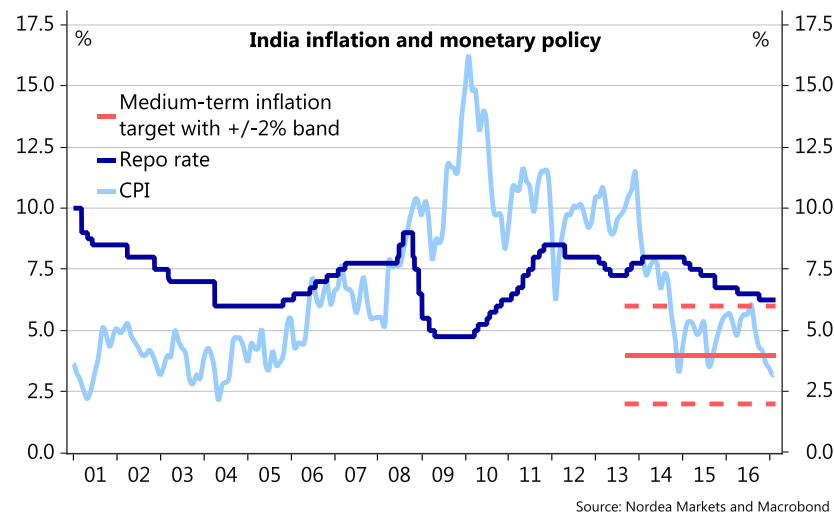
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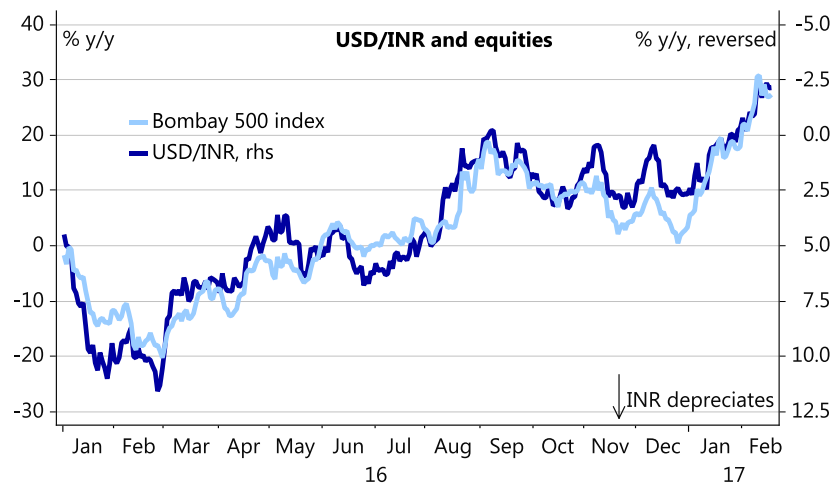
## India: No rate cut on the near horizon

- The RBI kept rates unchanged at 6.25% at the February meeting, because it expects the currently weakening growth and falling inflation as a temporary result of the demonetisation.
- We see a likelihood for a rate cut in H2 2017 as inflation will be a more sustainable downward trend. Swaps trading is pricing in a very low probability of a rate cut in H1 2017.
- The demonetisation has effectively improved the transmission between the policy rate and the lending rates, a long-standing concern for the RBI. The demonetisation caused bank deposits to surge and several state-owned banks to cut lending rates to the lowest level in six years. Governor Patel said recently the lending rates could come down further.

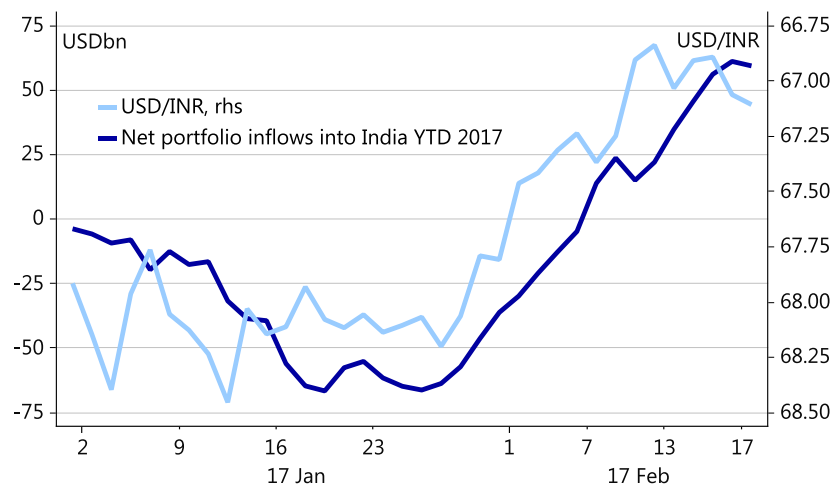


## INR: Protected from Trump

- The INR has been one of the best performers in Asia since Trump's inauguration on 20 February, gaining nearly 2% versus the USD.
- Elevated political uncertainty in the US (or in Europe) is generally bad for EM FX. For this reason, we see downside risks to the INR in the near term. But we still expect the INR to outperform its regional peers this year.
- The INR is likely protected from India's limited trade exposure, which makes it less vulnerable to Trump's potential protectionist policies.
- Moreover, the relatively high carry attracts foreign investors to INR assets. Nearly USD 1bn has flown into the local bond market in the second week of February.



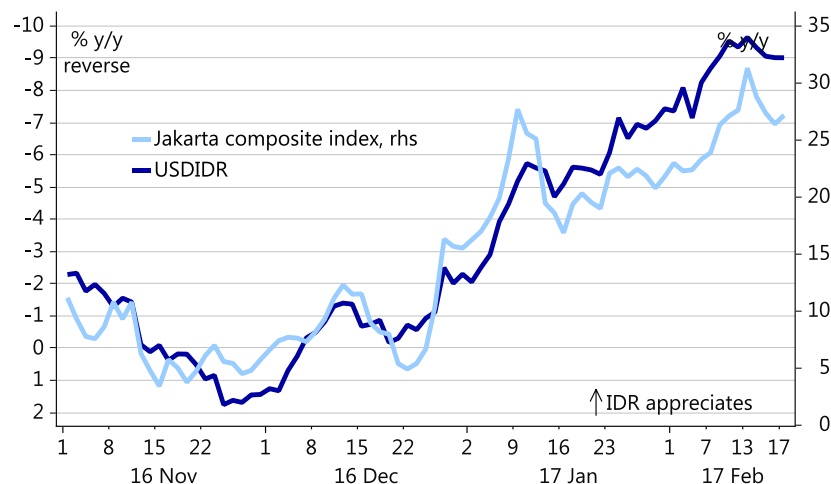
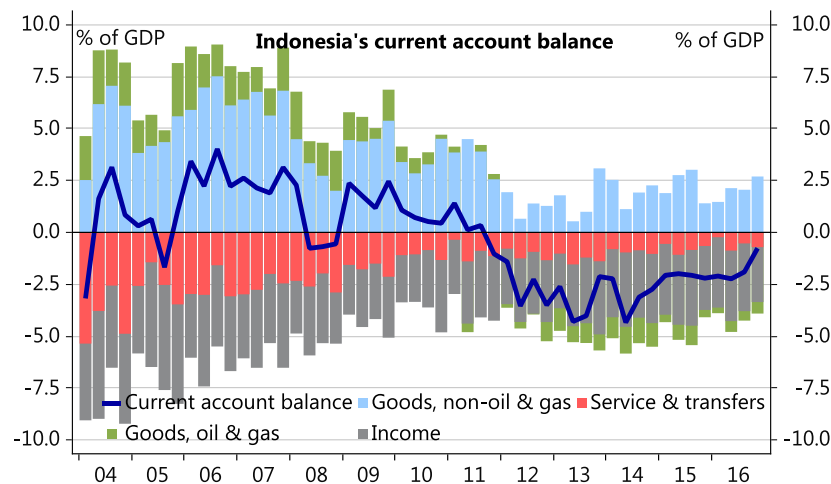
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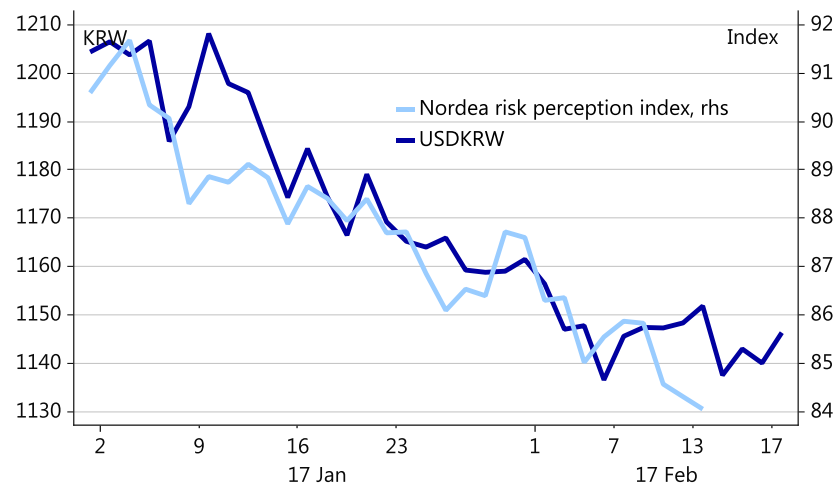
## IDR: Fundamental improvement

- Although Indonesia's growth, at 5% in Q4, is far below what it used to be, there are improvements in fundamentals.
- In Q4, Indonesia's current account deficit shrank to a five-year low of 0.7% of GDP. Its external financing need (short-term foreign debt and c/a deficit) fell to 55% of FX reserves, a remarkable improvement since 2013, when the IDR was labelled one of the most fragile EM currencies.
- The S&P is expected to upgrade Indonesia and help attracting foreign portfolio inflows and supporting the IDR.
- However, risks remain on the IDR, with still relatively high external debt and the recent news about the financial authorities considering to increase capital controls to ensure IDR stability.

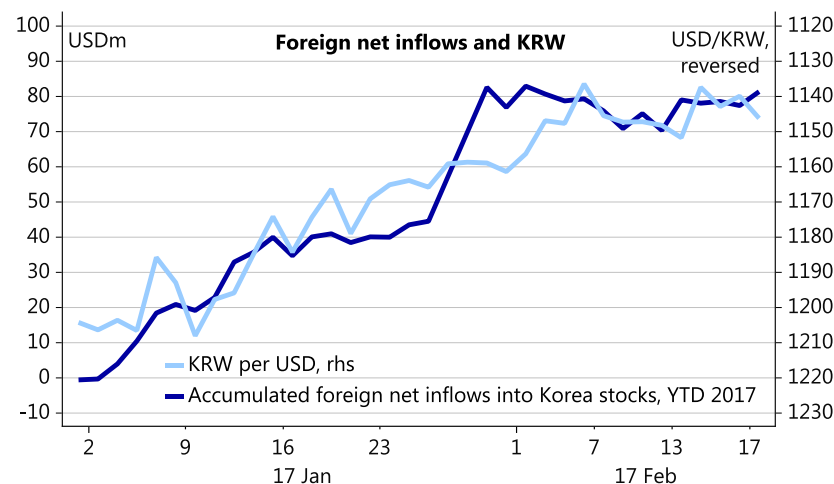


## KRW: A possible reversal of risk sentiment

- The KRW's gain so far in 2017 was driven by risk-on stock inflows into South Korea's stock market.
- We do not see the strength to last long. Trump's trade policy remains clear. As a large supplier to China, Korea could be hurt by any potential trade tensions between the US and China.
- Moreover, if Trump plans to officially label China as a currency manipulator, South Korea may well suffer the same fate, as it fulfills more of US Treasury's criteria for manipulation (see p. 5).
- Finally, the lingering political drama poses downside risks for the KRW. Samsung Group's de facto head, Jay Y. Lee, was formally arrested on allegations of bribery, perjury and embezzlement.



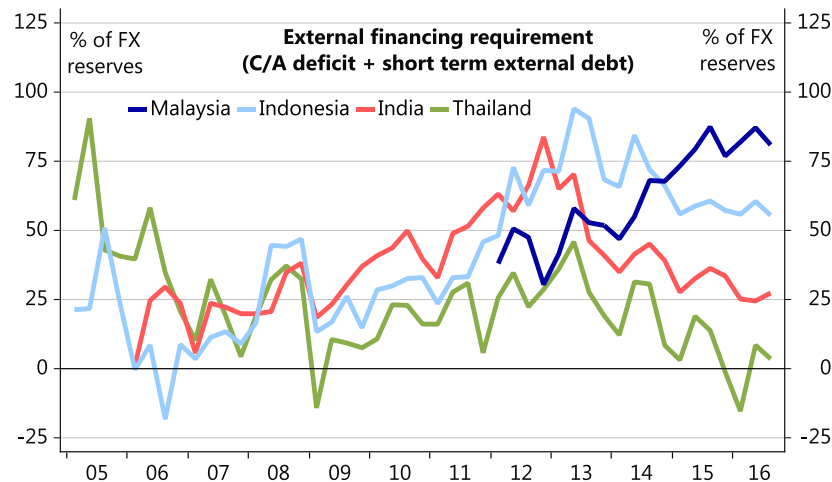
Source: Nordea Markets and Macrobond



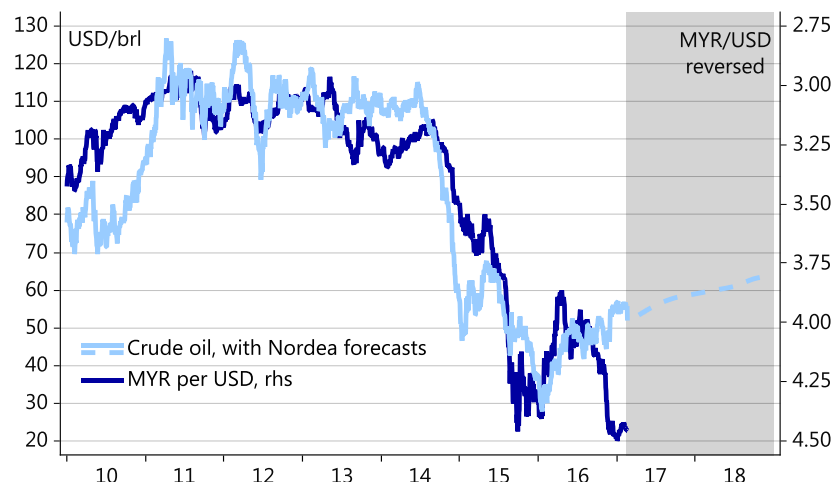
Source: Nordea Markets and Macrobond

## MYR: Most vulnerable to a hawkish Fed

- Yellen's reassurance of higher rates in the US this year regardless of Trump's fiscal policy is bad news for the MYR.
- Malaysia has the largest external funding need in Asia. Its short-term foreign debt is about 80% of the FX reserves, after accounting for the current account surplus. To raise alarm, this funding need has increased during the past four years and surpassed Indonesia.
- The deteriorating external balance is the reason for the latest tightening of capital controls. Now, 75% of all goods export proceeds are required to be converted to MYR instead of held in foreign currency.
- The decoupling from oil prices show that despite expected rebounding oil prices, the MYR faces downsides.



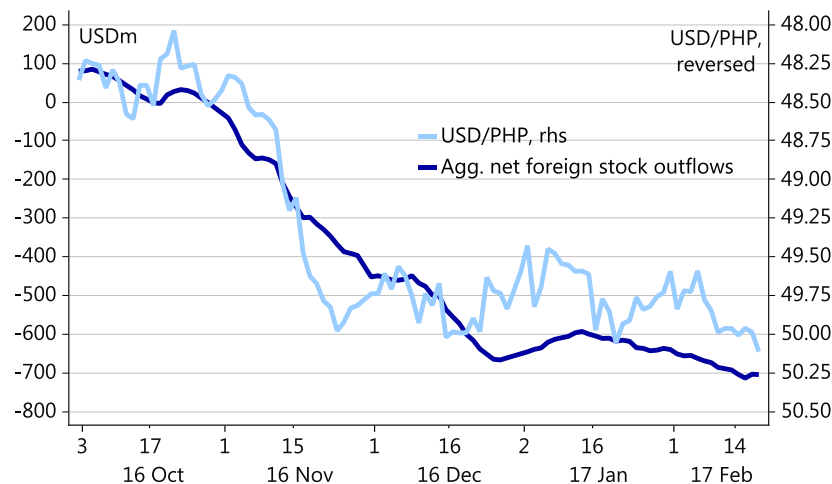
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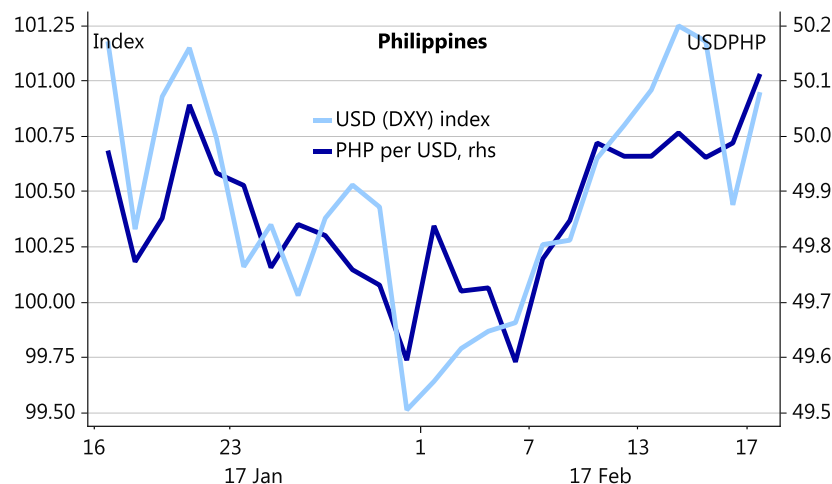
Source: Nordea Markets and Macrobond

## PHP: Investor flight

- The PHP is the worst-performing Asian currency year-to-date, losing about 1% versus the USD.
- In mid-February, the peso broke the psychological level of 50 and is now trading at the weakest level since 2006, despite strong fundamentals, including a consumer-led economy, stable remittance inflows and favourable demographics.
- We think the uncertain political development has dragged down investor confidence and caused foreign capital leaving the local stock market.
- On a longer horizon, we remain fairly positive on the PHP, because of its bright growth outlook and little external funding dependence, which makes the PHP less sensitive to USD strengthening.



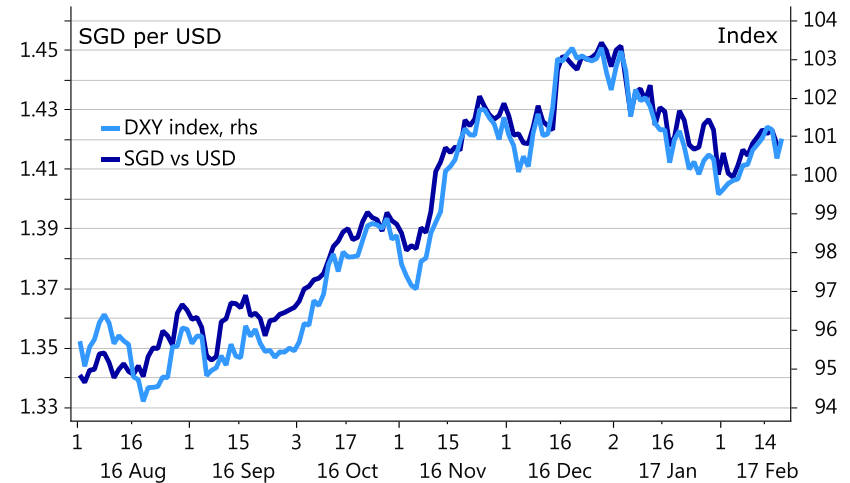
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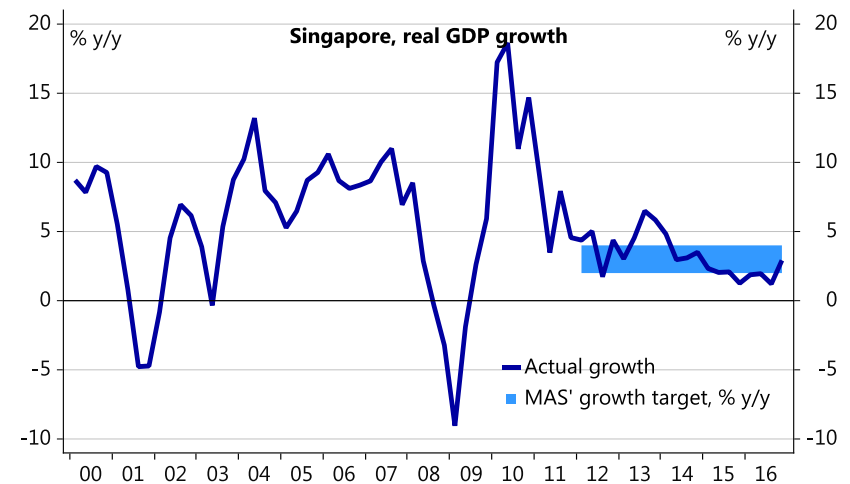
Source: Nordea Markets and Macrobond

## SGD: USD-driven

- The SGD is the Asian currency that has the highest correlation with the USD index, around 75% currently.
- Despite domestic developments, such as unexpectedly high GDP growth in Q4 and fiscal easing, which are expected to support the SGD in the near term, the SGD will largely depend on the USD.
- We look less optimistically at Singapore's macro outlook than the market. The recent growth rebound was helped China's temporary recovery and hence not sustainable.
- In mid-February, a government panel, led by Finance Minister Heng, published a report to reform the economy, including deregulation, digitalisation and changes to the tax system.



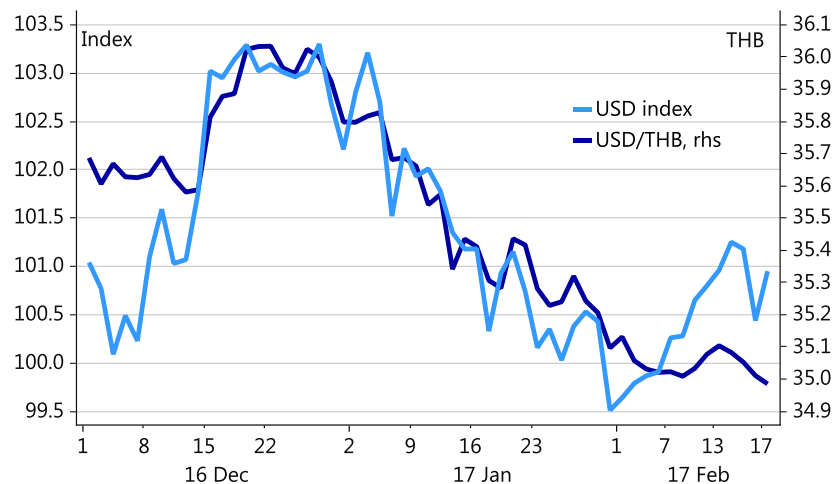
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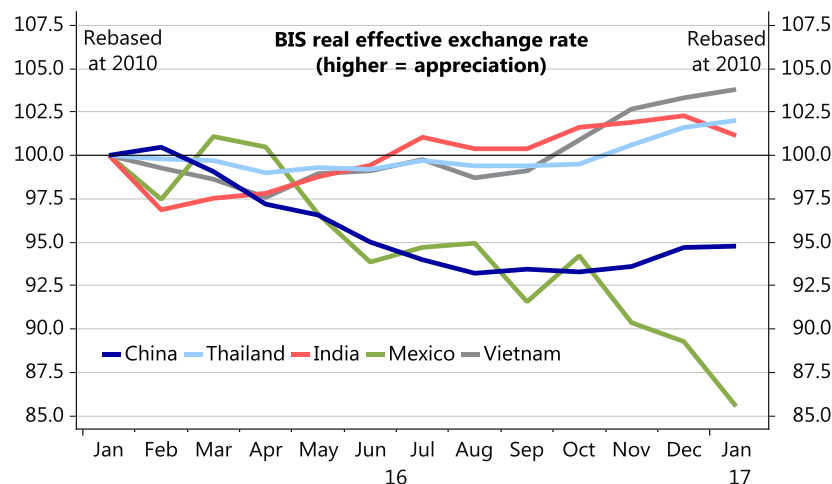
Source: Nordea Markets and Macrobond

## THB: Intervention

- The THB has gained nearly 3% against the USD so far this year. Investors have been bullish due to the expansive fiscal policy. The government recently passed an additional budget for transport infrastructure investment.
- Bank of Thailand is wary about the THB strength, especially against its major trading partners. It has been intervening with all measures, verbally, encouraging outflows by liberalising capital rules and by holding a net long position in FX forward and futures, shown by the central bank data.
- Continued intervention is a risk for Thailand to be added on the US' monitoring list. Thailand already fulfills two of three criteria to be labelled a currency manipulator (p. 4)



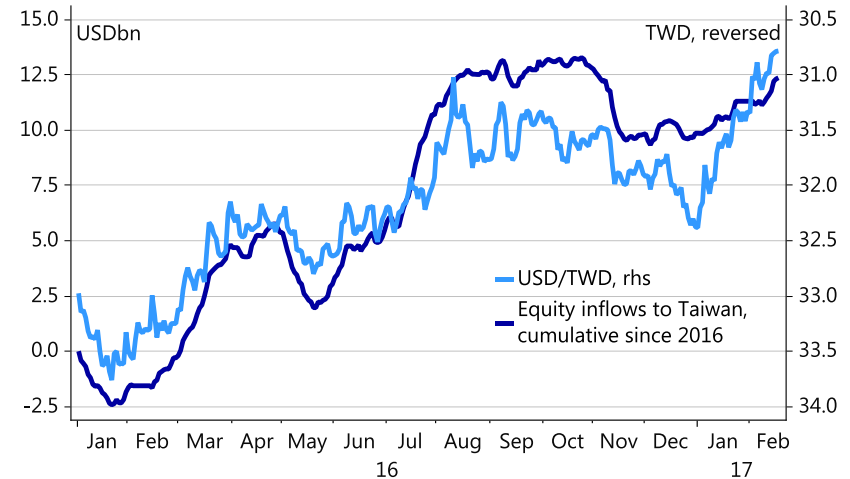
Source: Nordea Markets and Macrobond



Source: Nordea Markets and Macrobond

## TWD: Sentiment lifted by China

- The TWD is the second-best performing currency in Asia so far this year. The strength was due to a combination of a weaker dollar and strong capital inflows.
- Sentiment is high in Taiwan thanks to China's growth recovery. Q4 GDP surprised positively at 2.9% y/y. In addition, Apple's strong earnings report gave a positive spill-over to Taiwanese stocks, of which many companies are supplier to Apple.
- Nonetheless, we remain cautious on the TWD in the medium term. The risk of rising trade tensions between the US and China is still fairly large. Under such circumstances, Taiwan will take a large hit as a crucial supplier to Chinese production.



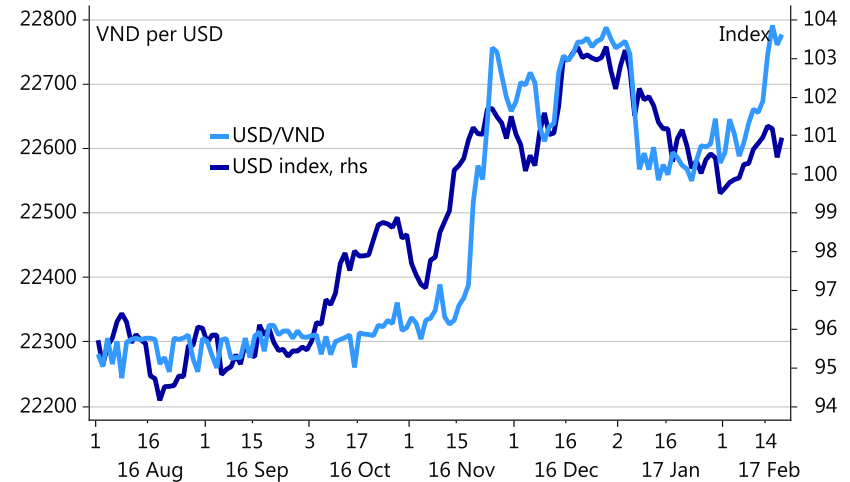
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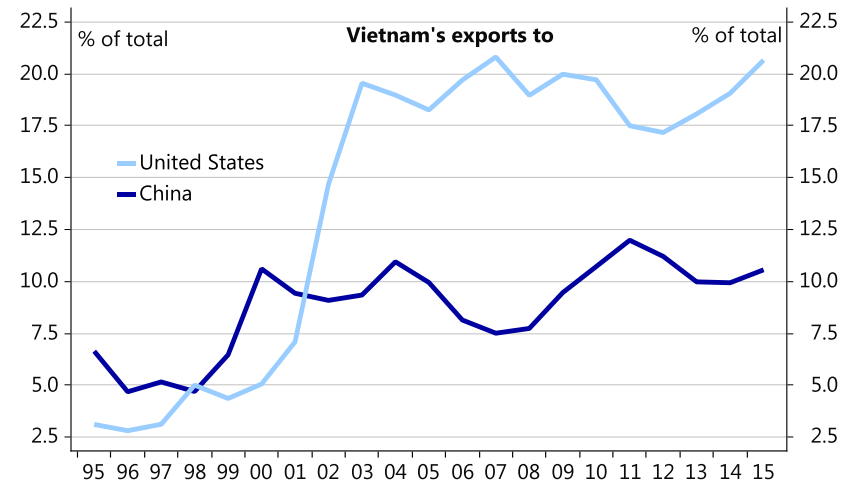
Source: Nordea Markets and Macrobond

## VND: External headwinds

- We remain bearish on the VND's outlook for this year and see more weakening against the USD due to several reasons.
- A hawkish Fed and expansive fiscal policy in the US would likely underpin the USD's strength and weaken most EM FX.
- Moreover, Vietnam faces growth headwinds in the short term, as global trade could remain subdued on rising protectionism. Vietnam is already hurt by losing the US as a part of the TPP.
- Finally, the VND is one of the most overvalued currencies in the region, so fundamentals support a weaker VND.
- Several years ahead, the VND faces upside potential as growth will benefit from reforms and relatively high growth in ASEAN.



Source: Nordea Markets and Macrobond



Source: Nordea Markets and Macrobond

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## Financial forecasts – FX rates

Exchange rates vs. EUR

	20/02/2017	3M	30/06/2017	31/12/2017	31/12/2018
EUR/USD	1.06	1.05	1.10	1.10	1.15
EUR/JPY	120.00	114.40	113.40	121.00	128.80
EUR/DKK	7.43	7.45	7.45	7.45	7.45
EUR/SEK	9.45	9.60	9.40	9.00	8.80
EUR/NOK	8.86	8.90	8.70	8.50	8.50
EUR/GBP	0.85	0.83	0.82	0.82	0.80
EUR/CHF	1.06	1.10	1.12	1.13	1.15
EUR/PLN	4.33	4.40	4.30	4.20	4.10
EUR/CZK	27.02	27.00	27.00	26.75	26.50
EUR/HUF	308.11	310.00	310.00	305.00	300.00
EUR/TRY	3.85	3.50	3.30	3.10	3.00
EUR/RUB	61.95	63.00	66.00	69.30	63.25
EUR/ZAR	13.86	13.91	14.58	14.30	13.80
EUR/CNY	7.29	7.25	7.59	7.54	7.82
EUR/INR	71.14	72.45	74.80	74.80	75.90
EUR/BRL	3.29	3.47	3.63	3.58	3.57
EUR/MXN	21.71	21.00	20.90	19.80	18.40

Exchange rates vs. USD

	20/02/2017	3M	30/06/2017	31/12/2017	31/12/2018
USD/JPY	113.04	108.00	110.00	112.00	114.00
USD/DKK	7.00	7.09	6.77	6.77	6.48
USD/SEK	8.90	8.95	8.46	8.18	7.65
USD/NOK	8.34	8.48	7.91	7.73	7.39
USD/GBP	0.81	0.80	0.75	0.75	0.74
USD/CHF	1.00	1.03	1.00	1.00	0.97
USD/PLN	4.08	4.19	3.91	3.82	3.57
USD/CZK	25.45	25.71	24.55	24.32	23.04
USD/HUF	290.23	293.33	277.27	272.73	252.17
USD/TRY	3.62	3.62	3.27	3.09	2.61
USD/RUB	58.36	60.00	60.00	63.00	55.00
USD/ZAR	13.06	13.25	13.25	13.00	12.00
USD/CNY	6.87	6.90	6.90	6.85	6.80
USD/INR	67.01	69.00	68.00	68.00	66.00
USD/BRL	3.10	3.30	3.30	3.25	3.10
USD/MXN	20.45	20.00	19.00	18.00	16.00

# Financial forecasts – rates

## Monetary policy rates

Country	Spot	3M	30Jun17	31Dec17	31Dec18
United States	0.75	0.75	1.00	1.25	2.00
Japan	-0.10	-0.10	-0.10	-0.10	-0.10
Euro Area	-0.40	-0.40	-0.40	-0.40	-0.40
Denmark	-0.65	-0.65	-0.65	-0.65	-0.65
Sweden	-0.50	-0.50	-0.50	-0.50	0.00
Norway	0.50	0.50	0.50	0.50	0.50
United Kingdom	0.25	0.25	0.25	0.25	0.25
Switzerland	-0.75	-0.75	-0.75	-0.75	-0.75
Poland	1.50	1.50	1.50	1.50	2.00
Russia	10.00	9.50	9.50	8.00	7.00
China	4.35	4.35	4.35	4.35	4.35
India	6.25	6.25	6.25	6.00	6.00
Brazil	13.00	11.00	11.00	10.00	10.00
Czech Republic	0.05	0.05	0.05	0.05	0.05
Hungary	0.90	0.90	0.90	1.00	1.50
Turkey	8.00	8.50	8.50	8.00	7.50

## 3-month rates

Country	Spot	3M	30.06.17	31.12.17	31.12.18
United States	1.05	1.00	1.15	1.40	2.10
Euro Area	-0.33	-0.30	-0.30	-0.30	-0.30
Denmark	-0.23	-0.20	-0.20	-0.20	-0.20
Sweden	-0.50	-0.50	-0.50	-0.50	0.00
Norway	1.01	1.00	1.00	0.90	0.90
United Kingdom	0.36	0.40	0.40	0.40	0.40
Poland	1.63	1.70	1.70	1.70	2.25
Russia	10.50	10.30	9.70	8.35	8.00

## 10-year government

Country	Spot	3M	30.06.17	31.12.17	31.12.18
United States	2.41	2.60	2.70	2.75	3.20
Euro Area	0.30	0.40	0.50	0.70	0.90
Denmark	0.63	0.40	0.50	0.70	0.90
Sweden	0.68	0.70	0.85	1.35	1.50
Norway	1.72	1.65	1.60	2.00	2.25
United Kingdom	1.21	1.45	1.50	1.60	1.80
Poland	3.83	3.90	4.00	3.75	3.50

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