APAC Economic Perspectives
ASEAN: Are the SGD and MYR overshooting?

Economics

Asia Pacific

Edward Teather
Economist
edward.teather@ubs.com
+65-6495 5965

Alice Fulwood
Associate Economist
alice.fulwood@ubs.com
+65-6495 3085

Maximillian Lin
Strategist
maximillian.lin@ubs.com
+65-6495 8429

MYR may be in the process of overshooting, further SGD weakness ahead

We have been looking for ASEAN and Indian currencies, to varying degrees, to fall versus a stronger US dollar. However, the ringgit and Singapore dollar have softened further than we expected. We think the ringgit could be on the verge of overshooting, but doubt this is the case for the SGD. We extend our projections to look for USDSGD 1.35 by end 2015 and our USDMYR projection to 3.50 by end 2015 (Figure 8).

Ringgit weakness linked to oil and liquidity

The 11% decline in the Malaysian ringgit from its highs against the US dollar in August 2014 to recent lows can be broken into two periods. Firstly, from 27 August to 27 November, when the ringgit weakened a little over 6% against 2.5-4.5% declines in the other SE Asian currencies against a stronger US dollar. Secondly, the sharp 4.1% decline since 27 November, which coincided with the drop in the oil price post the OPEC meeting and a set of unfavourable Malaysian trade data. The lower oil price promises to adversely impact Malaysian income growth given the country's position as a net oil and gas exporter, while the lower October trade surplus implies a diminished margin of surplus savings with which to manage the income shock. The weakness in the ringgit is likely based on a combination of the stronger US dollar and the lower oil price on top of already slowing growth momentum – implying weak growth and lower policy interest rates (see Malaysia: oil prices – adding fuel to the fire; 3 Dec 2014). These fundamentals probably drove asset sales by foreign investors (both the bond and equity market sold off since 27 November) which in turn depressed the currency.

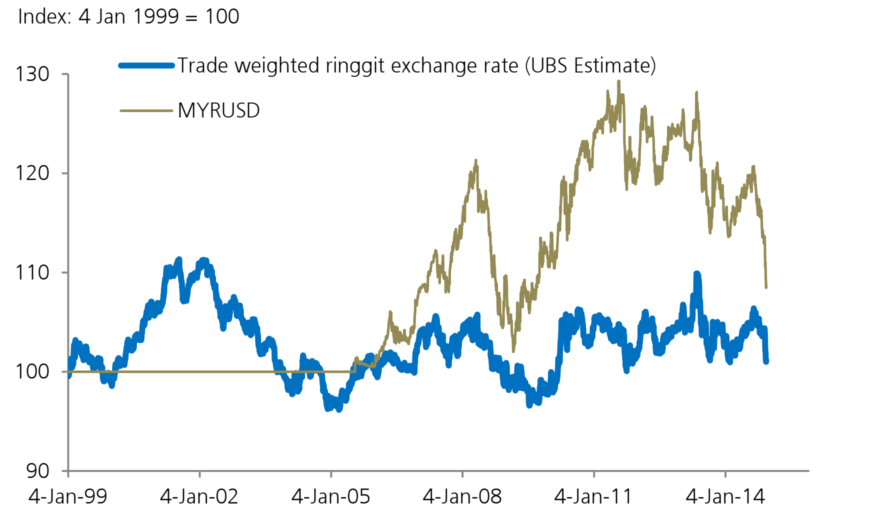
Ringgit to recover its poise

While things may well get worse before they get better, oil and capital flows could become more ringgit positive later in 2015. UBS' oil team expect the oil market to remain oversupplied into early 2015, which could mean further declines in the oil price. However, lower oil prices are already incentivising oil companies to reduce capital expenditure on extraction – indeed this was part of the reason we lowered our Malaysian growth forecast on 3 December. Ultimately that should help deliver a stabilisation and recovery in the oil price – although, according to UBS' oil team, not until late in 2015. At some point, this should support faith in the ringgit. We also expect better support from the balance of trade and capital flows. Lower domestic demand should mitigate the downward impact of commodity prices on the Malaysian current account balance. Meanwhile, the adverse impact of near term foreign portfolio outflows should be overcome by i) a combination of the recent FX and asset price adjustment (which should attract foreign funds) and ii) the return of Malaysian funds invested overseas driven by home bias and liquidity preference in a more uncertain domestic economic environment. Against this, UBS expects the US dollar to continue appreciating in 2015 towards EURUSD 1.15 and Malaysia's domestic credit cycle to further mature alongside that of Asia. As such, we forecast the ringgit to regain some of its poise, but not to reverse recent losses. We project USDMYR 3.50 for end 2015.

Singapore dollar to keep falling against US dollar

Analysis by UBS currency strategist Max Lin shows much of the decline in the Singapore dollar against the US dollar was driven by the rise in the USD against Singapore's trading partner currencies. We expect i) continued US dollar strength, though at a reduced pace, ii) pressure on the Singapore economy from higher US yields and iii) the MAS to ease currency policy during 2015. We reckon that will put the SGD Nominal Effective Exchange Rate (NEER) in the lower half of the MAS' policy band at end 2015. Consistent with this, we project USDSGD 1.35 by end 2015.

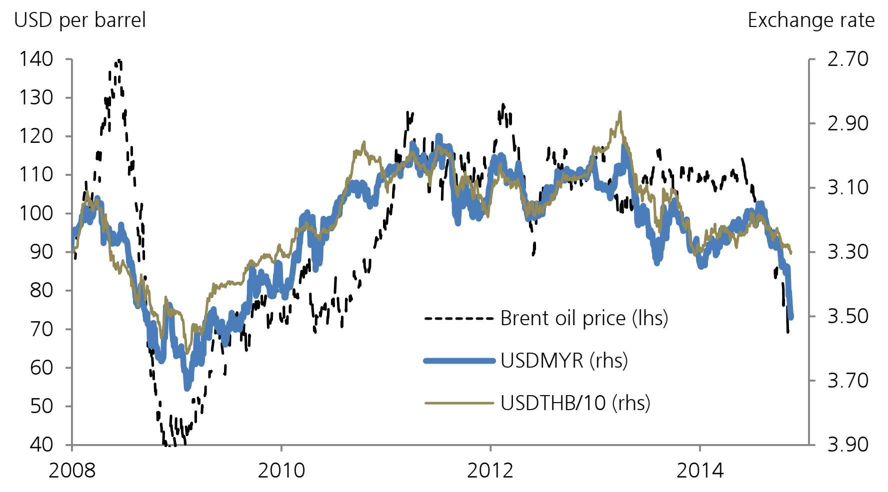
Figure 1: Ringgit exchange rate against US dollar and trade weighted peers



Source: UBS Estimates, Haver, CIEC

The ringgit has weakened against peers and the US dollar

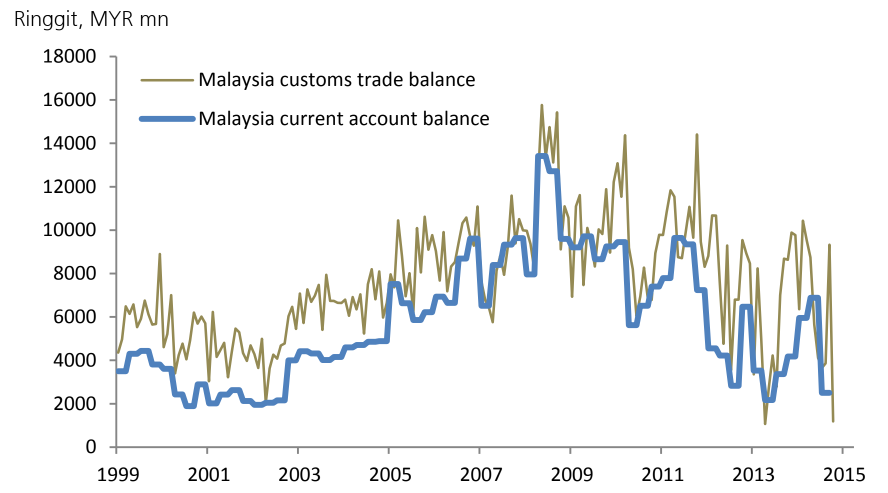
Figure 2: Oil prices appear to added to idiosyncratic MYR weakness



Source: UBS Estimates, Haver, CIEC

Oil prices appear to explain some of the ringgit's weakness against close peers. That makes sense; Malaysia is an oil and gas exporter. The economy can expect to see reduced national income levels and growth as a result of the sharp decline in oil prices.

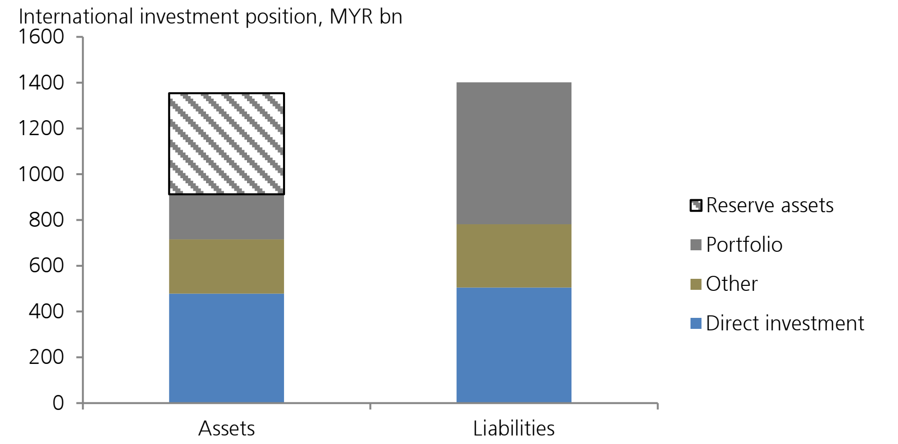
Figure 3: Deterioration in trade balance implies less current account cushion



Source: UBS Estimates, Haver, CIEC

Weak October trade data may also have played a role. The reduced trade surplus implies a narrower cushion to adsorb income losses as a result of lower commodity prices. The dip in October's trade balance was caused by higher imports – specifically capital goods imports – rather than lower oil-linked export revenue. We expect imports to weaken with domestic demand next year, providing some offset to a reduced oil and gas balance of trade.

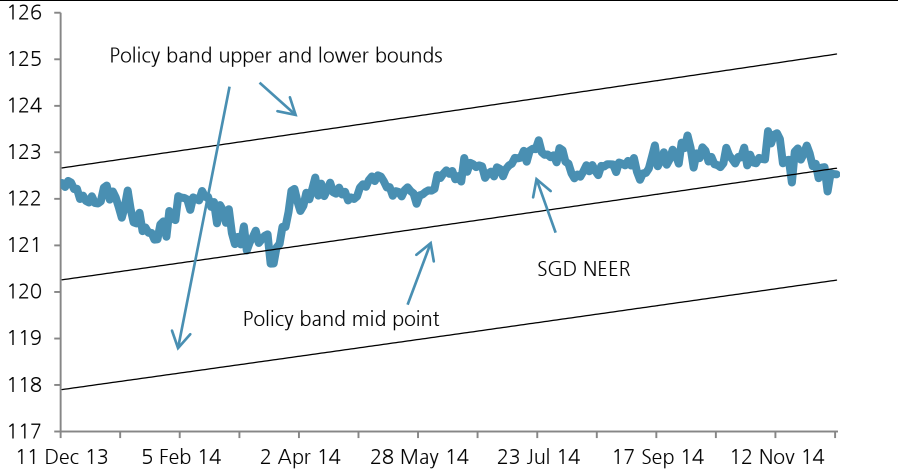
Figure 4: Malaysia's strong international asset position could imply reserve of support for ringgit in fullness of time



Source: UBS Estimates, Haver, CIEC

Malaysia's substantial external liabilities (including external debt) at 142% of GDP are often highlighted as a cause for concern. However, Malaysia's external assets are of a similar magnitude (137% of GDP). Foreign portfolio outflows may have been dominant in the recent past, but it is quite possible the flows may become more balanced or favourable for the MYR if home bias and liquidity preference take hold amongst Malaysian investors.

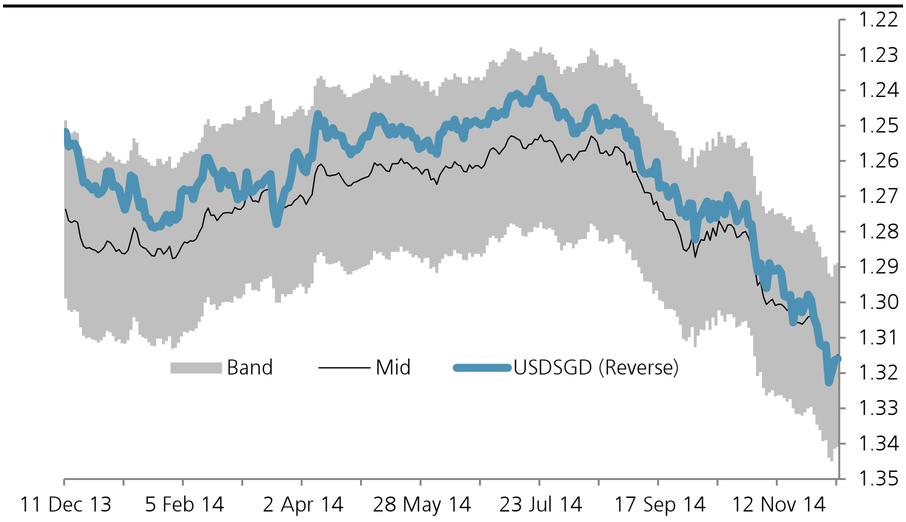
Figure 5: MAS Nominal Effective Exchange Rate and policy band (UBS Estimate)



Source:

The Singapore dollar has weakened modestly within the Monetary Authority of Singapore's policy band, consistent with a growing expectation of easier policy at one of the MAS meetings in 2015.

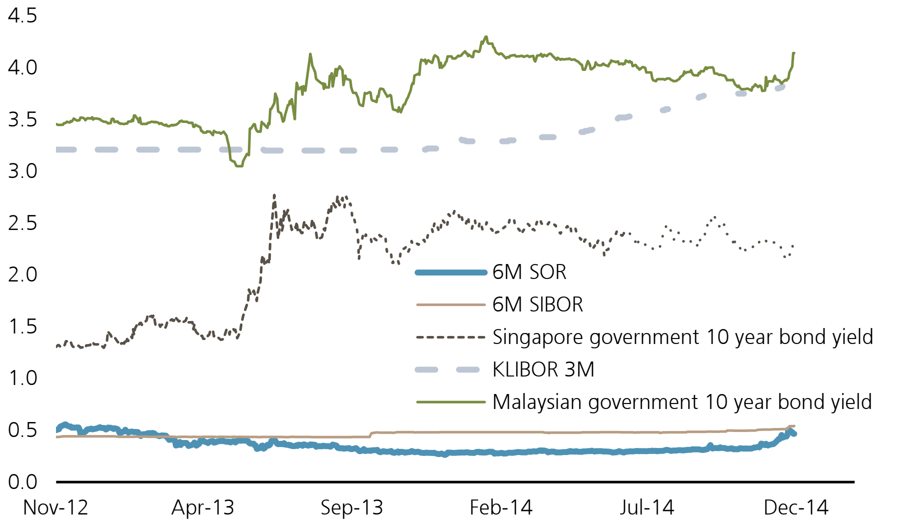
Figure 6: Implied MAS policy band in USDSGD Terms & USDSGD Spot



Source: UBS Estimates, Haver, CIEC

But the majority of weakness in SGD against USD has been the due to US dollar strength against the Singapore dollar and its peers. There is still plenty of room for the SGD to fall within the policy band and hence against trading partner currencies and the USD.

Figure 7: Higher Malaysian yields should draw capital home, Singapore yields may need to rise to achieve the same effect during 2015



Source: UBS Estimates, Haver, CIEC

Malaysian government bond yields jumped modestly in recent days, consistent with the market finding a new equilibrium in the face of capital outflow pressure. Capital outflow pressure may force Singapore yields higher if US interest rates begin to rise in line with UBS projections later in 2015.

Figure 8: UBS currency forecasts

	Current	End 2015 E (Old)	End 2016 E (old)	% chg between current and End 2015
USDINR	61.8	63.0	65.0	+2.0%
USDIDR	12340	12800	13250	+3.7%
USDMYR	3.49	3.50(3.40)	3.55(3.45)	+0.3%
USDPHP	44.6	47	49	+5.5%
USDSGD	1.317	1.350(1.320)	1.360 (1.330)	+2.5%
USDTHB	32.9	34.0	35.0	+3.4%

Source: UBS estimates

Recent publications relevant to MYR, SGD and oil

Singapore Banks: SOR soars – points to FX and liquidity shifts (8 Dec 2014)

APAC Econ Comment - Malaysia: Oil prices - adding fuel to the fire (3 Dec 2014)

APAC Econ Perspectives - ASEAN and India: Lower oil, lower rates (3 Dec 2014)

Asian Economic Perspectives – Outlook 2015-16 (11 Nov 2014)

EM Cross Asset Strategy: Outlook 2015 (10 Nov 2014)

Asian Focus – Malaysia: Budget 2015 – a better mix (13 Oct 2014)

Asian Focus - Singapore: Ready for a rough ride? (11 Aug 2014)

Recent Issues of the APAC Economic Perspectives/Asian Focus:

Recent Issues of the Asian Economic Perspectives:

Required Disclosures

This report has been prepared by UBS Securities Pte. Ltd., an affiliate of UBS AG. UBS AG, its subsidiaries, branches and affiliates are referred to herein as UBS.

For information on the ways in which UBS manages conflicts and maintains independence of its research product; historical performance information; and certain additional disclosures concerning UBS research recommendations, please visit www.ubs.com/disclosures. The figures contained in performance charts refer to the past; past performance is not a reliable indicator of future results. Additional information will be made available upon request. UBS Securities Co. Limited is licensed to conduct securities investment consultancy businesses by the China Securities Regulatory Commission.

Analyst Certification: Each research analyst primarily responsible for the content of this research report, in whole or in part, certifies that with respect to each security or issuer that the analyst covered in this report: (1) all of the views expressed accurately reflect his or her personal views about those securities or issuers and were prepared in an independent manner, including with respect to UBS, and (2) no part of his or her compensation was, is, or will be, directly or indirectly, related to the specific recommendations or views expressed by that research analyst in the research report.

UBS Global Credit Strategy and Research: Rating Definitions
UBS ranks potential investment opportunities within non-government fixed income markets and sectors. Issuers are rated on one or both criteria shown below, and specific securities may be recommended as well.

	UBS Terminology	Time Horizon	Definition
Issuer Ratings			
Credit Rating	AAA, AA, A, BBB, BB, B, CCC, CC, C (+/-)	Up to 12 months	UBS' assessment of a company's creditworthiness
Outlook	Positive; Stable; Negative	Up to 6 months	UBS' expected trend in a company's creditworthiness
Security Recommendations			
Bond Recommendation	Outperform; Marketperform; Underperform	Up to 3 months	A corporate bond's expected relative performance versus a defined reference
CDS Recommendation	Buy Protection; Sell Protection	Up to 3 months	Recommendation to hedge a company's creditworthiness

Note: Recommendations for periods under 3 months are defined as 'Tactical', as in Tactical Outperform or Tactical Underperform. The UBS credit rating may be modified by the addition of a plus (+) or minus (-) sign where applicable to show relative standing within the major categories.
Source: UBS

Company Disclosures

Issuer Name	Credit Rating	Outlook
Government of Indonesia	-	-
India (Republic Of)	-	-
Malaysia	-	-
Philippines (Republic of)	-	-
Singapore	-	-
Thailand (Kingdom of)	-	-

Source: UBS. Ratings in this table are the most current published ratings prior to this report.

Global Disclaimer

This document has been prepared by UBS Securities Pte. Ltd., an affiliate of UBS AG. UBS AG, its subsidiaries, branches and affiliates are referred to herein as UBS.

This document is for distribution only as may be permitted by law. It is not directed to, or intended for distribution to or use by, any person or entity who is a citizen or resident of or located in any locality, state, country or other jurisdiction where such distribution, publication, availability or use would be contrary to law or regulation or would subject UBS to any registration or licensing requirement within such jurisdiction. It is published solely for information purposes; it is not an advertisement nor is it a solicitation or an offer to buy or sell any financial instruments or to participate in any particular trading strategy. No representation or warranty, either express or implied, is provided in relation to the accuracy, completeness or reliability of the information contained in this document ('the Information'), except with respect to Information concerning UBS. The Information is not intended to be a complete statement or summary of the securities, markets or developments referred to in the document. UBS does not undertake to update or keep current the Information. Any opinions expressed in this document may change without notice and may differ or be contrary to opinions expressed by other business areas or groups of UBS. Any statements contained in this report attributed to a third party represent UBS's interpretation of the data, information and/or opinions provided by that third party either publicly or through a subscription service, and such use and interpretation have not been reviewed by the third party.

Nothing in this document constitutes a representation that any investment strategy or recommendation is suitable or appropriate to an investor's individual circumstances or otherwise constitutes a personal recommendation. Investments involve risks, and investors should exercise prudence and their own judgement in making their investment decisions. The financial instruments described in the document may not be eligible for sale in all jurisdictions or to certain categories of investors. Options, derivative products and futures are not suitable for all investors, and trading in these instruments is considered risky. Mortgage and asset-backed securities may involve a high degree of risk and may be highly volatile in response to fluctuations in interest rates or other market conditions. Foreign currency rates of exchange may adversely affect the value, price or income of any security or related instrument referred to in the document. For investment advice, trade execution or other enquiries, clients should contact their local sales representative.

The value of any investment or income may go down as well as up, and investors may not get back the full (or any) amount invested. Past performance is not necessarily a guide to future performance. Neither UBS nor any of its directors, employees or agents accepts any liability for any loss (including investment loss) or damage arising out of the use of all or any of the Information.

Any prices stated in this document are for information purposes only and do not represent valuations for individual securities or other financial instruments. There is no representation that any transaction can or could have been effected at those prices, and any prices do not necessarily reflect UBS's internal books and records or theoretical model-based valuations and may be based on certain assumptions. Different assumptions by UBS or any other source may yield substantially different results.

This document and the Information are produced by UBS as part of its research function and are provided to you solely for general background information. UBS has no regard to the specific investment objectives, financial situation or particular needs of any specific recipient. In no circumstances may this document or any of the Information be used for any of the following purposes:

(i) valuation or accounting purposes;

(ii) to determine the amounts due or payable, the price or the value of any financial instrument or financial contract; or

(iii) to measure the performance of any financial instrument.

By receiving this document and the Information you will be deemed to represent and warrant to UBS that you will not use this document or any of the Information for any of the above purposes or otherwise rely upon this document or any of the Information.

Research will initiate, update and cease coverage solely at the discretion of UBS Investment Bank Research Management. The analysis contained in this document is based on numerous assumptions. Different assumptions could result in materially different results. The analyst(s) responsible for the preparation of this document may interact with trading desk personnel, sales personnel and other parties for the purpose of gathering, applying and interpreting market information. UBS relies on information barriers to control the flow of information contained in one or more areas within UBS into other areas, units, groups or affiliates of UBS. The compensation of the analyst who prepared this document is determined exclusively by research management and senior management (not including investment banking). Analyst compensation is not based on investment banking revenues; however, compensation may relate to the revenues of UBS Investment Bank as a whole, of which investment banking, sales and trading are a part.

For financial instruments admitted to trading on an EU regulated market: UBS AG, its affiliates or subsidiaries (excluding UBS Securities LLC) acts as a market maker or liquidity provider (in accordance with the interpretation of these terms in the UK) in the financial instruments of the issuer save that where the activity of liquidity provider is carried out in accordance with the definition given to it by the laws and regulations of any other EU jurisdictions, such information is separately disclosed in this document. For financial instruments admitted to trading on a non-EU regulated market: UBS may act as a market maker save that where this activity is carried out in the US in accordance with the definition given to it by the relevant laws and regulations, such activity will be specifically disclosed in this document. UBS may have issued a warrant the value of which is based on one or more of the financial instruments referred to in the document. UBS and its affiliates and employees may have long or short positions, trade as principal and buy and sell in instruments or derivatives identified herein; such transactions or positions may be inconsistent with the opinions expressed in this document.

UBS