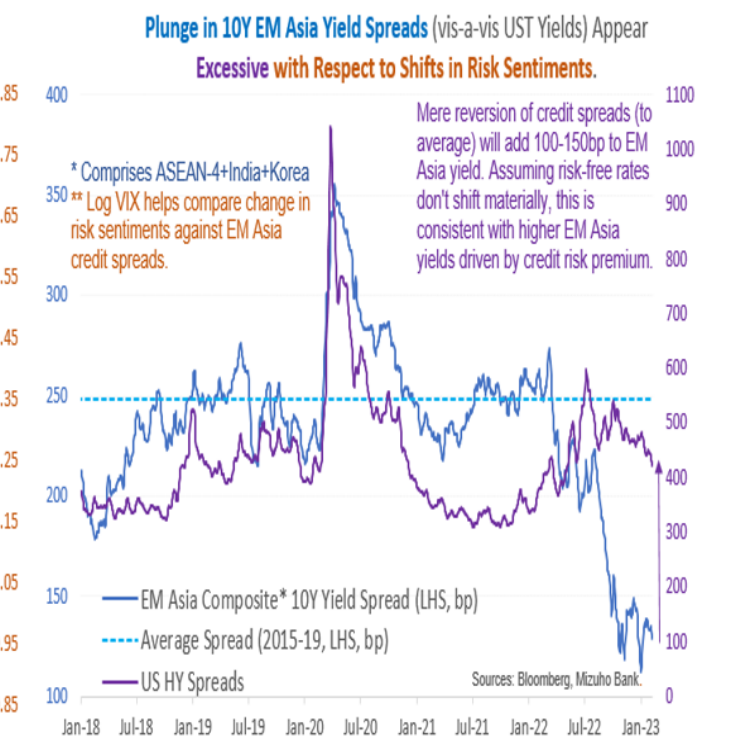
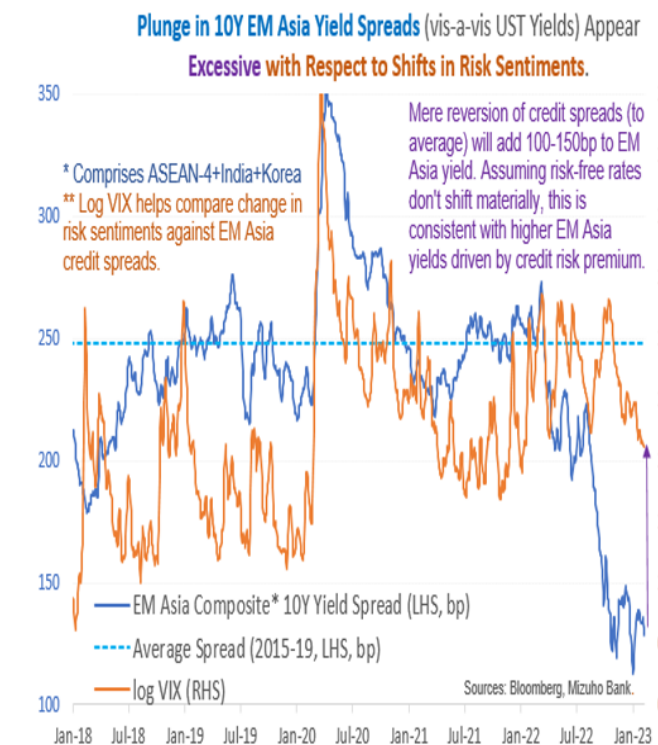
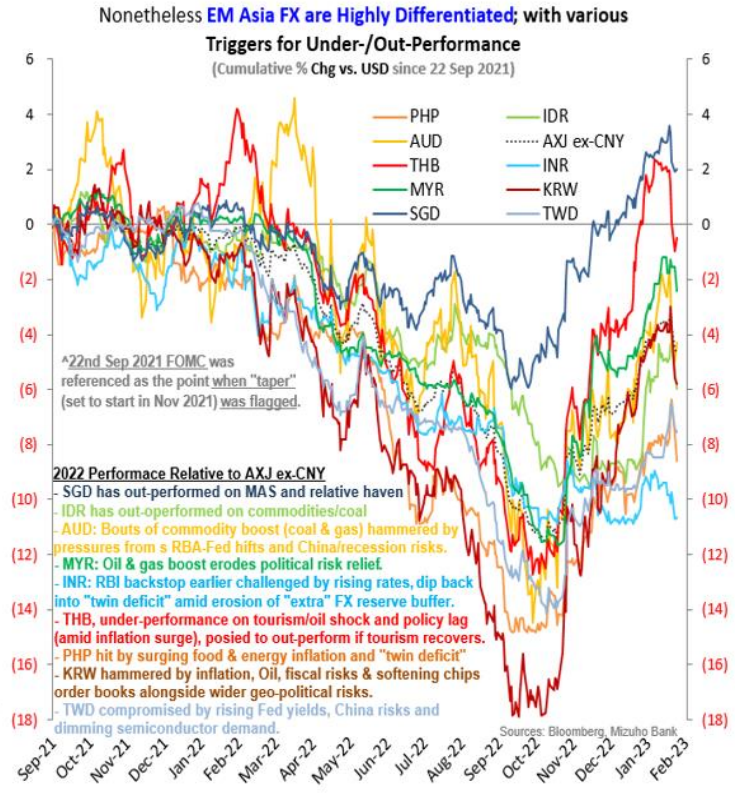
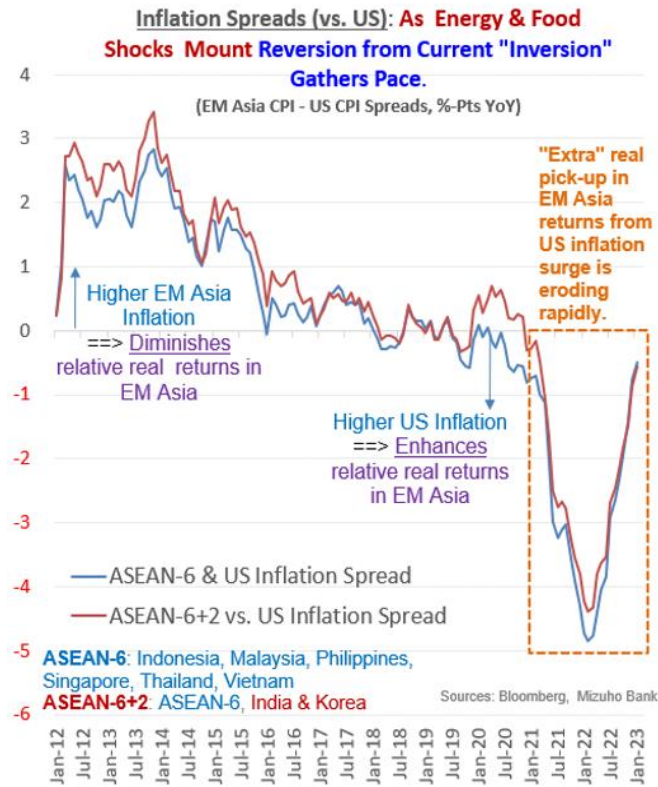
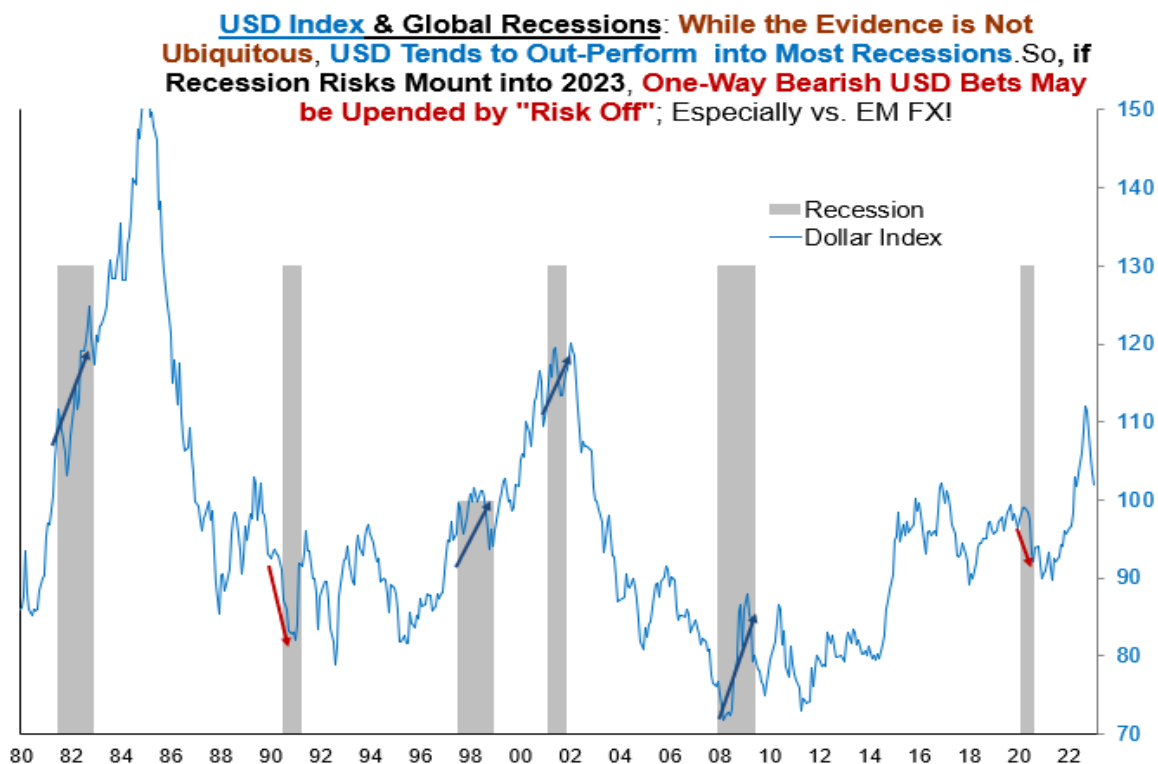


Beware (Bull) Traps & Turbulence





“Be careful not to choke on your aspirations.” – Darth Vader, *Star Wars*

In a Nutshell: Warnings of bull traps and turbulence, and not cavalier doubling down of bullish bets, ought to dominate the narrative around EM Asia FX (AXJ) in coming months. Admittedly, AXJ appear constructive on a medium- to longer-term basis but face significant turbulence near-term; as scope for risk re-pricing, diminishing real returns and gathering global demand headwinds conspire

For one, in the broadest of strokes, EM Asia FX gains will be checked by the resistance that the USD puts up; even as it relinquishes its crown. Simply because Fed hawks, while less aggressive, are not done as yet; and could revive outbursts of USD rebound as Fed pivot bets are disappointed.

Crucially, EM Asia risk premium exceptionally diminished. The laws of (at least partial) reversion must apply as overdone China cheer and post COVID relief wane; especially if global downturn risks mount. And that suggests moderation in the rapid EM Asia FX gains since Q4 last year. More so as US disinflation outpacing sticker inflation in EM Asia diminishes AXJ's real carry. Finally, growing US-China tensions could also take some wind out of EM Asia assets/FX (in aggregate).

High inflation regimes with twin deficit risks will be most vulnerable to bouts of risk re-pricing that tends to correspond to strong USD rebound. So, tourism buffer of THB and the capital inflow/quasi-haven status of a MAS bolstered SGD are preferred to the twin deficit-high inflation risks of PHP and INR; the latter also being buffeted by the Adani crisis. KRW and TWD may initially struggle on soft chip order books requiring cyclical tailwinds from further out to stage a strong rebound (on a relative basis).

Pitching AXJ Allure on Peak USD

Arguably, it is tempting to exploit 'Peak USD' narrative as an opportunity for long EM Asia FX bets. And admittedly, there are reasons to be fundamentally constructive on EM Asia currencies (AXJ) too; from the cyclical tailwinds of (lagged) post-COVID recovery to the structural geological forces of demographics and productivity gains alongside capacity enhancements from investments.

Flawed Amid Overarching Risks

But **confusing peak USD for AXJ propulsion is fatally flawed**. More so if AXJ support premised on **medium- to longer-term fundamentals** support. Whereas **AXJ will not be absolved of overarching global policy and geo-political upheavals**; which are inclined to **keep downside AXJ risks in play**.

Significant Risks of AXJ Turbulence

In fact, the **broader macro and geo-political backdrop** is bristling with **significant risks of AXJ turbulence**. In particular, given the **build-up of inherent and growing AXJ vulnerabilities** associated with *risk re-pricing*, *diminishing real returns* and *gathering global demand headwinds*. And so, despite the strong rebound in AXJ since Q4 last year, it would be **cavalier to double down on unbridled bullish AXJ bets**. Instead, a **far wiser approach would be to be respectful of the danger of bull traps and episodic turbulence**; for wide-ranging, but not exhaustive, reasons elucidated here:

Dollar to Contest: For a start, and in the broadest of strokes, **EM Asia FX gains are likely to be checked by the proclivity of the USD to contest demands to relinquish its crown**. Simply *because Fed hawks, while less aggressive, are far from done; and certainly not turning doves in a rush*. Point being, the Fed may continue to disappoint bets on proximate rate cuts in H2. In turn, this *demonstration of “keeping at it”* ought to squeeze overdone USD selling; with **attendant convulsions in (and against) AXJ**.

Rich EM Asia Valuations: Especially given that **EM Asia’s risks appear to be severely mis-priced**. Specifically, *EM Asia’s risk premium appear exceptionally diminished* (under-priced); which implies **precariously rich valuations** that are **vulnerable to sharp corrections**. So apart from episodes of broad-based USD rebound, **AXJ are inherently inclined to sharp corrections**; assuming at least partial reversion to historically consistent risk premium. A process that may be *hastened by more elevated rates and mounting geo-political uncertainty*.

Moderating Economic Cheer: Overdone China cheer and post COVID relief waning under the circumspection of binding economic and geo-political realities also suggests that front-loaded AXJ gains may be saturated. Especially if a global demand destruction risks grow, warning of diminished hard currency flow to most EM Asia exporters. And that suggests **moderation in the rapid EM Asia FX gains since Q4 last year**.

Diminished Real Carry: What’s more, *as US disinflation outpaces stickier inflation in EM Asia*, the **real carry** in EM Asia (and AXJ) is **materially diminished**. And as this inflation dynamic, disadvantageous to AXJ plays out further, *accentuated by a relatively more hawkish Fed* (in terms of combined hikes and QT) the **allure of AXJ is liable to erode**.

US-China Risks: Finally, **growing US-China tension** could also take some wind out of EM Asia assets/FX as spillover economic/financial risks mount. Specifically, prospects of devastation of both real economic damage inflicted indirectly via trade channels as well as adverse financial risks.

Dampened & Differentiated

Despite broad-based drag forces, any **AXJ shake-down** is more **likely** than not **to entail a greater degree of differentiation**; as **uneven exposures** to; i) *sectors* (e.g. manufacturing, hospitality), which are themselves to hospitality) prospects; ii), twin deficit risks; iii) commodity/shipping reliance and; iv) geopolitical-headline exposures discriminate. While far from comprehensive, some broad thoughts are as follow:

- As such **high inflation regimes with twin deficit risks will be most vulnerable to bouts of risk re-pricing** that tends to correspond to strong USD rebound; which raise *red flags for PHP and INR vulnerabilities* most noticeably. Adani headline risks amplifying rupee risks.
- While sweeping insulation is not a luxury any EM Asia FX may declare, the *tourism buffer of THB* and the *capital inflow/quasi-haven status of a MAS bolstered SGD* render these as relative outperformers in the region.
- KRW and TWD may initially struggle on soft chip order books requiring cyclical tailwinds from further out to stage a strong rebound (on a relative basis). So a case of front-loaded pro-cyclical risks linked to global downturn risks. KRW may have a greater degree of weakness given Current Account-driven positive correlation to shipping cycle as well.
- Despite the commonality of commodity theme for AUD, IDR and MYR, the performance between these currencies could also materially diverge. MYR has near-term pick-up from faded political risks premium, but IDR faces continued policy divergence risks. RBA-debt tensions hold back AUD.

FX Forecasts	Mar 23	Jun 23	Sep 23	Dec 23	Mar 24	Jun 24
USD/CNY	6.50 - 6.96 (6.78)	6.49 - 6.94 (6.68)	6.63 - 7.32 (7.02)	6.63 - 7.12 (6.85)	6.57 - 7.06 (6.79)	6.56 - 6.96 (6.78)
USD/INR	79.5 - 84.6 (83.2)	79.6 - 84.4 (81.6)	80.7 - 87.1 (84.6)	77.8 - 86.3 (82.0)	76.3 - 83.0 (80.4)	75.5 - 82.3 (79.6)
USD/KRW	1170 - 1320 (1250)	1130 - 1320 (1230)	1210 - 1390 (1320)	1180 - 1350 (1280)	1220 - 1340 (1270)	1210 - 1370 (1265)
USD/SGD	1.279 - 1.351 (1.323)	1.253 - 1.347 (1.298)	1.282 - 1.436 (1.370)	1.284 - 1.410 (1.358)	1.306 - 1.388 (1.342)	1.289 - 1.365 (1.325)
USD/TWD	28.9 - 30.8 (30.2)	27.8 - 31.2 (29.3)	29.1 - 33.2 (31.6)	28.5 - 32.2 (30.3)	29.1 - 31.6 (30.0)	28.5 - 30.6 (29.4)
USD/IDR	14420 - 15910 (15350)	14470 - 15800 (15120)	14710 - 16640 (15960)	15120 - 16540 (15780)	15000 - 16300 (15500)	14570 - 15810 (15050)
USD/MYR	4.05 - 4.43 (4.35)	3.98 - 4.40 (4.20)	4.13 - 4.63 (4.48)	4.23 - 4.58 (4.43)	4.18 - 4.51 (4.36)	4.14 - 4.50 (4.32)
USD/PHP	53.5 - 57.7 (56.3)	51.0 - 61.5 (54.2)	53.7 - 61.8 (57.2)	53.7 - 57.9 (56.2)	51.7 - 57.0 (54.3)	52.4 - 57.2 (54.0)
USD/THB	31.9 - 34.6 (33.3)	30.7 - 33.8 (32.6)	32.3 - 35.2 (34.2)	31.6 - 35.1 (33.9)	32.7 - 35.3 (33.6)	32.4 - 34.6 (33.3)
USD/VND	22900 - 23900 (23550)	22500 - 24100 (23600)	23500 - 25200 (24500)	23700 - 24800 (23800)	23600 - 24500 (23700)	23400 - 24000 (23600)
AUD/USD	0.666 - 0.755 (0.708)	0.700 - 0.800 (0.746)	0.621 - 0.762 (0.670)	0.650 - 0.781 (0.685)	0.641 - 0.728 (0.695)	0.682 - 0.746 (0.710)

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