



Philequity Corner (September 21, 2020)
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Upward pressure on the peso

The Philippine peso strengthened 0.3% last week to close at 48.395 vs. the US dollar. This is the highest level for the peso since November 2016. Last week's move was the result of the strong upward pressure caused by the Chinese yuan on the peso. The Chinese yuan surged 0.96% to close at 6.7675 last Friday, its highest level in 16 months.

Peso's inherent strength

In previous articles, we cited the domestic and external reasons why the peso is strong. Among these are the prudent and proactive management of our country's finances, resulting in a robust fiscal position, record gross international reserves (GIR) and strong external balances, benign inflation and a healthy banking system. We also discussed the US dollar's general weakness and the global dearth of yield that boosts the peso's demand.

OFW remittances continue to recover

OFW remittances continue to defy expectations, recovering with back-to-back 7.6% growth in June and July. Remittances from land-based workers grew 12.6% in July. This growth more than made up for the 9.2% decline in remittances from sea-based workers. The improved remittance figures brought the seven-month total to \$18.66 billion, or 2.4% lower than the \$19.12 billion registered over a similar period last year. OFW remittances have traditionally kept the country's current account balance contained despite the huge trade deficits. This has contributed greatly to the strength of the peso.

Yuan rises on robust economic data

More recently, it is the strong yuan that is driving the peso higher. The yuan rose on news that Chinese industrial production accelerated the most in eight months, accompanied by strong retail sales growth. Note that China's second quarter's GDP expanded 3.2%, suggesting that economic recovery is gathering pace. According to a new report by the Asian Development Bank (ADB), China is the only country in the region to register growth this year, expanding by 1.8% in 2020. For 2021, ADB forecasts a 7.7% GDP growth for the region's largest economy.

Yuan may strengthen to 6.48 over the next 12 months

Since hitting 7.18 last June, the Chinese yuan has strengthened by 5.7%. A technical analysis of the USDCNY rate shows support at 6.67. If the yuan breaks this level, it can further strengthen to 6.48, which is the "measured move" target from 6.83.

USDCNY Weekly Chart



Correlation with yuan tightened in recent months

In the past 3-month and 6-month periods, the correlation between the Chinese yuan and Asian EM currencies has never been tighter. This was the period when the US dollar started to display broad-based weakness. In the past, the peso and the yuan had a weak correlation, equivalent to -0.26 during the past 5-year period.

But recently, the peso's 3-month correlation with the yuan strengthened to 0.93. Note that a correlation with an absolute value of 0.9 or greater represents a very strong relationship. Thus, the peso was closely mirroring the movement of the Chinese yuan in the past 3-month and 6-month periods. The same can be said of the other Asian EM currencies as shown in the table below.

CNY Correlation table	SGD	PHP	INR	TWD	MYR	KRW
3-month	0.88	0.93	0.90	0.83	0.94	0.81
6-month	0.80	0.87	0.85	0.74	0.88	0.77
1-year	0.55	0.61	0.23	0.53	0.62	0.54
5-year	0.42	(0.26)	0.28	(0.53)	0.19	0.05

Source: Wealth Securities Research

USDPHP support is seen at 48

If indeed the Chinese yuan is going to 6.48 longer term, we may continue to expect upward pressure to the Asian EM currencies, including the Philippine peso. But shorter term, significant technical support for the peso is seen at 48, where it is expected to hold and shift to a broader trading range.

USDPHP Weekly Chart



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