AUGUST 26, 2024

PHILEQUITY CORNER

By Wilson Sy

Philippine peso strengthens

The Philippine peso strengthened 1.19% to 56.415 last week as the currency touched its strongest level in five months against the US dollar. The peso's rebound defied earlier expectations, which had predicted weakness on bets that the Bangko Sentral ng Pilipinas (BSP) would cut rates before the Federal Reserve.

The peso's strength is caused by US dollar weakness against most currencies. Lower US inflation and slower economic growth suggests that interest rates have to start coming down. Additionally, the unwinding of carry trades and broadening of stock market gains to other sectors and other countries have further contributed to the dollar weakness.

Source: Tradingview.com

BSP cuts rates amid lower inflation risks

The Bangko Sentral ng Pilipinas (BSP) lowered its benchmark interest rate by 25 basis points to 6.25% at its August 2024 policy meeting, a move that had long been signaled by the central bank. Governor Remolona emphasized that the inflation outlook was skewed to the downside for 2024 and 2025, prompting the rate cut. This decision aligns with Remolona's statements in recent months, which had been preparing markets for potential easing.

Dollar weakness fuels peso's strength

A key driver of the peso's strength is the broad weakening of the US dollar against most currencies. Cooling U.S. inflation, which have decelerated for four straight months, and lower US interest rates have diminished the dollar's appeal. This has narrowed interest rate differentials against the major currencies like the yen and the euro triggered a significant rebalancing in the forex markets.

Carry trade unwinding propels Yen, Euro gains

Market anticipation of the Fed's first rate cut has triggered a significant unwinding of carry trades. One popular carry trade involves shorting the Japanese yen while buying US Treasuries and US stocks. This shift has led to notable appreciation in the Japanese yen, Swiss franc, British pound, the euro, and other major currencies over the past two months.

Asian currencies have also benefitted from this broad weakening of the US dollar, with the Malaysian ringgit and Thai baht leading the gains. The Philippine peso has likewise strengthened, rallying 4.35% from its low this year.

Major Currencies	% rally from 2024 Low
Japanese Yen	12.00%
Swiss Franc	8.43%
British Pound	6.99%
Norwegian Krone	6.25%
Australian Dollar	6.14%
Euro	5.40%
Canadian Dollar	2.70%
	% pullback from High
US Dollar Index (DXY)	-5.21%

Asian Currencies	% rally from 2024 Low
Malaysian Ringgit	9.69%
Thai Baht	9.56%
Indonesian Rupiah	6.18%
Korean Won	5.08%
Singaporean Dollar	4.94%
Philippine Peso	4.35%
Taiwanese Dollar	2.86%
Chinese Yuan	2.18%
Indian Rupee	0.08%

Source: Bloomberg, Wealth Sec. Research

PSEi rallies on broadening bull market

While the peso has strengthened alongside Asian peers, the Philippine Stock Exchange Index (PSEi) has surged 13% from its June low. The PSEi closed at 6,961.96 last week - near the upper end of its two-year range. This reflects a broadening global bull market that is extending to diverse sectors and emerging markets like the Philippines. The broadening has resulted in flows coming to other sectors and countries, with the Philippine peso and stock market being clear beneficiaries.

Powell: “The time has come”

Last Friday, Fed Chair Jerome Powell affirmed expectations of upcoming rate cuts in his Jackson Hole speech, stating "the time has come for policy to adjust." This statement has made a September rate cut a certainty with markets now pricing in a 1/3 chance of a 50bp cut and a 2/3 chance of a 25bp cut . Notably, officials from the ECB and Bank of England also signaled they’re set to lower rates in coming months, heralding the end of a high-interest rate era.

Peso stability gives BSP policy flexibility

The peso’s newfound stability provides the BSP increased policy flexibility, allowing it to focus on economic growth without the constant concern of currency volatility. While challenges remain, the shift marks a turning point. Investors are now watching how the central bank leverages this improved landscape, with its next moves potentially setting the tone for both domestic policy and foreign investment flows.