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MACRO MORNING BRIEFING

October 31, 2024

Excessive ATM Volatility in APAC FX

October has been extremely volatile, driven by a number of factors, including uncertainty related to the elections in the US and Japan, ongoing debate regarding the pace and magnitude of near-term US interest rate expectations, and, finally, the prospect of macro and sentiment stabilization and recovery in China.

For example, market pricing of near-term US federal funds rates has shifted from pricing in more than 75bp in cuts to less than 50bp by the end of the year, with an SOFR December 2024 implied yield of around 4.40%. The 10yr US Treasury yield, a benchmark for global funding costs, has risen by more than 50bp on the month to 4.30%. And the US dollar has surged by more than 3% on the month and is now back to levels last seen at the end of July, while USDJPY marches toward 155.

For a full discussion of US Treasury dynamics, see our Short Thoughts report from earlier this week.

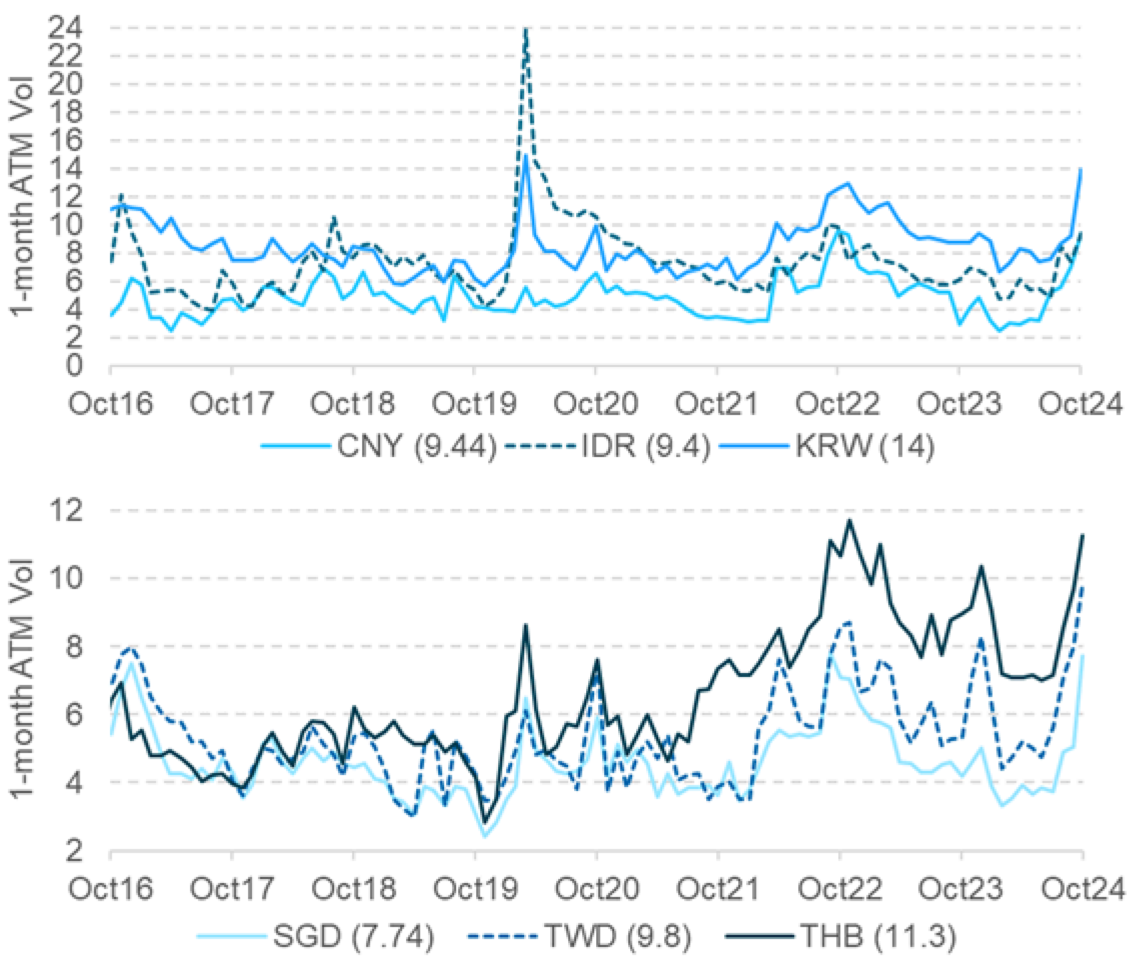
Emerging market currencies underperformed on the back of higher global bond yields and a stronger US dollar. We have observed an indiscriminate increase in volatility across APAC currencies, using short-dated 1-month at-the-money (ATM) as a proxy, compared with a target currencies like the Mexican peso in LatAm.

APAC 1-month at-the-money volatility is near multiyear highs. As shown in Exhibit #1, at 9.8 USDTWD 1-month ATM is at its highest level since September 2011, while USDSGD 1-month ATM has more than doubled from 3.7% in July to 7.74% in October and USDCNH 1-month

ATM is at 9.14, just shy of its high of 10.68 in October 2022.

While the higher 1-month ATM volatility was accompanied by weaker currencies, there has been little sign of foreign capital pressure in local markets. Foreign equity outflows have been relatively stable and contained, except in India, which has posted accelerated outflows over the past few weeks. As a result, the current extreme pricing observed in options markets is not viewed as sustainable. Risk-reward favors a reversal strategy rather than chasing at the top.

Exhibit #1: Heightened Volatility Across APAC Currencies

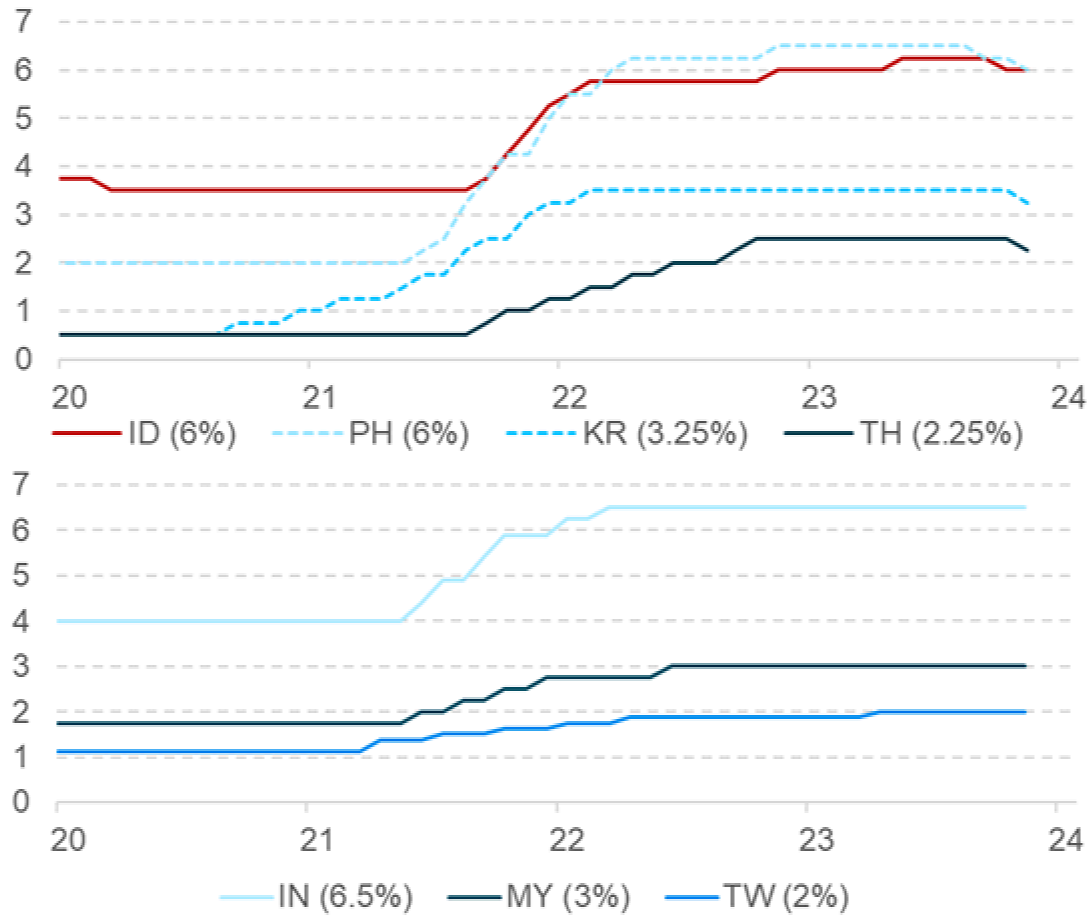


Source: BNY, Bloomberg L.P.

Rising uncertainty and the currency depreciation momentum in Asian FX is likely to impact monetary policy in a hawkish or less dovish manner. Indeed, responding to the recent surge by USDKRW toward 1,390, an rise of more than 5% on the month, the Bank of Korea noted in an unusual comment that “the exchange rate has become a factor to consider in monetary policy.”

Overall, heightened market volatility may delay but will not alter the near-term policy easing path. Rate normalization intended to make interest rates less restrictive is here to stay. This is true for Bank Indonesia where real positive interest rates are at historically high levels.

Exhibit #2: Policy Rates Across the APAC Region

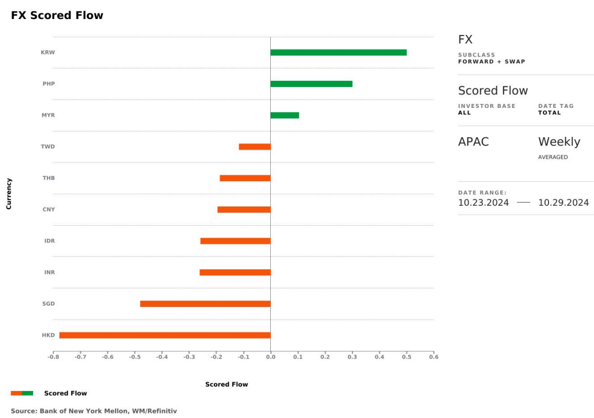


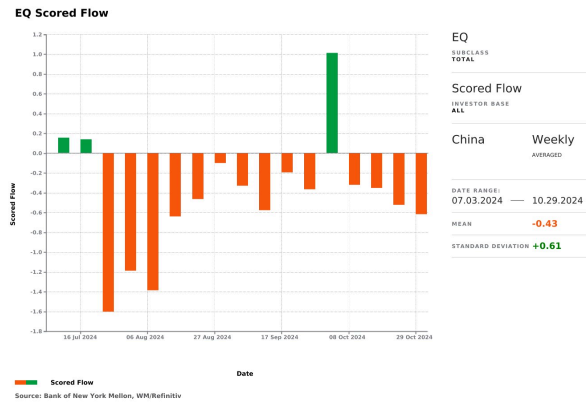
Source: BNY, Bloomberg L.P.

Over the past week, ongoing US dollar strength has led to outflow pressure in EM APAC. HKD and SGD were the most sold while demand was observed in KRW. The pickup of outflow momentum has led aggregate APAC scored holdings to drop back into negative, or underheld territory, after having reached the neutral zone at the beginning of the month. INR was the most significant currency, with weekly average scored holdings of 2.45 compared with over 4 the week before.

In equities, investor appetite for Chinese shares remains low with continued outflows, while Indian equities posted accelerated outflows. With respect to bonds, Chinese sovereign bond outflow momentum continued for the 12th consecutive week, while demand for Indian sovereign bonds continues after a brief period of outflows the week before.

Exhibit #3: HKD, SGD Most Sold / China Equity Outflows Continues





Source: BNY, Bloomberg L.P.

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Please direct questions or comments to: iFlow@BNY.com

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