The KRW - No Respite

- The KRW is one of worst performers in Asia in 2019
- Significance of Powell testimonies can't be overstated
- Exports under pressure as tensions with Japan rise

Deteriorating fundamentals and a developing trade spat suggest that the odds on the KRW’s protracted, regional under-performance being curtailed are somewhat lengthy.

The KRW has been one of the worst performers in Asia in 2019: since the turn of the year, the KRW has ceded 5.9% to the USD whilst the INR, the IDR and the PHP, for example, have gained an average 2.8%. The region’s star performer, the THB, has gained an impressive 5%.

Long-term cross-correlations for the KRW with its peers – which stand well north of 90% - only serve to emphasise the significance of this markedly divergent performance. And it is a performance that can be explained to a large extent by South Korea’s status as a technology and export hub caught up in an international trade war.

Compounded by the end of a two-year super-cycle in the demand for semiconductors, slowing global growth has been anathema to an export-led economy. And the KRW’s slide got underway on April 18 when US/China trade uncertainty finally got the better of foreign investors (the Kospi has since lost 9%).

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2. Chinese producer price inflation falls to zero for June >
3. 
Slowing global growth has been anathema to an export-led economy

However, the more recent gyrations in USD/KRW and South Korean stocks can be placed at the door of Fed policy and speculation thereof and hence, the significance of the Powell testimonies cannot be overstated.

Certainly, a stronger USD could feasibly rekindle speculation over the sanctity of the CNY 7 to the USD level and potentially unleash renewed instability into the region’s currencies.

Uncertainty surrounding China’s economic outlook has been keenly felt in South Korea in particular – we note that five of the top ten daily moves in the KRW this year have been instigated by China-related news.

And as such, even were USD/KRW to recoil post-Powell, the move could well prove fleeting given that the South Korean economy is showing particular signs of fatigue and to the point where the odds on easier money from the Bank of Korea are shortening appreciably.

Indeed, the country’s worst set of GDP data since 2008 prompted the BoK into a hasty retreat from hawkish territory and data in the interim has prompted the Bank to lower its growth and inflation forecasts.

The prospects of easier money from the Bank of Korea are shortening accordingly

The country’s inflation rate – one of the lowest in the OECD – has been below 1% for six months now; PMI data point to contracting manufacturing activity; and exports are under growing pressure just as tensions with Japan over trade look to be on the rise.

The two countries have engaged in a “tit-for-tat” exchange of retaliatory measures for several months now but tensions rose last Friday when Japan imposed new
restrictions on South Korea’s technology exports.

Were USD/KRW to remain on its present, northerly course, however, we might then consider the possibility of a staunch defence of the KRW 1,200 to the USD level.

Certainly, in the seven times that the pair has traded north of 1,190 in the past ten years, only twice has it failed to go on to challenge the 1,200 level.

Intriguingly, however, the last such occasion was in May.

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