ASEAN New Finance

Crypto Opportunities & Hurdles

Saktiandi Supaat
Regional Head of FX Research,
Maybank Group

Lai Gene Lih
Analyst, Technology, Research

In Focus:

Network effects is a key driver for cyptocurrency adoption, and the current adoption rate appears already outpacing that of early stages of the internet.

Institutional interest is rising – Bitcoin is seen a diversifier in asset allocation. Banks and other institutions are also exploring blockchain based methods to make payments and cross-border transfers more efficient.

Given the disruptive potential and rapid gain in mindshare among retail, institutional and regulatory players, developments in this blockchain and cryptocurrencies can no longer be dismissed.

Fidelity launched its inaugural Bitcoin-only fund.

MicroStrategy announced adding Bitcoin to its treasury.

PayPal announced that its users in US can buy, sell and hold key cryptocurrencies.

Tesla revealed it bought USD1.5bn worth of Bitcoin.

BlackRock added Bitcoin futures as an eligible investment.

Morgan Stanley became the first big US bank to offer Bitcoin funds to its wealthier clients.

2020 is widely recognized as the year Bitcoin went institutional. Institutional interest in cryptocurrencies picked up discernibly. Fidelity launched its inaugural Bitcoin-only fund while MicroStrategy announced adding Bitcoin to its treasury. PayPal announced that its users in US can buy, sell and hold key cryptocurrencies. Fast forward to 2021 and Tesla revealed it bought USD1.5bn worth of Bitcoin. BlackRock added Bitcoin futures as an eligible investment to two funds, while Morgan Stanley became the first big US bank to offer Bitcoin funds to its wealthier clients.

Over the past year, accommodative monetary and fiscal policy globally has likely resulted in an abundance of liquidity which could have spilled over to the cryptocurrency space. Even as Bitcoin prices tanked in May 2021, blockchain data shows signs of institutional buying on-the-dip.

Growing engagement in cryptocurrencies by institutions as a new asset class could lead crypto asset moves to be more intricately linked with broader market swings, even as negative spillovers from sporadic crypto market crashes to other assets clearly remain limited for now.

Going forward, ESG will likely become an important lens via which market participants—blockchain developers, miners, investors—view crypto assets. Elon Musk's concerns over Bitcoin's impact on climate change was likely one of the news drivers contributing to the May 2021 cryptocurrency slump.

Mitigation efforts are already underway. For instance, segments of the Bitcoin mining industry have moved to invest in renewable energy projects to push for reduction in carbon emissions caused by cryptocurrency mining. Transitions to more energy-efficient approaches (e.g., Ethereum's switch to proof-of-stake from proof-of-work) in blockchain are also closely monitored.

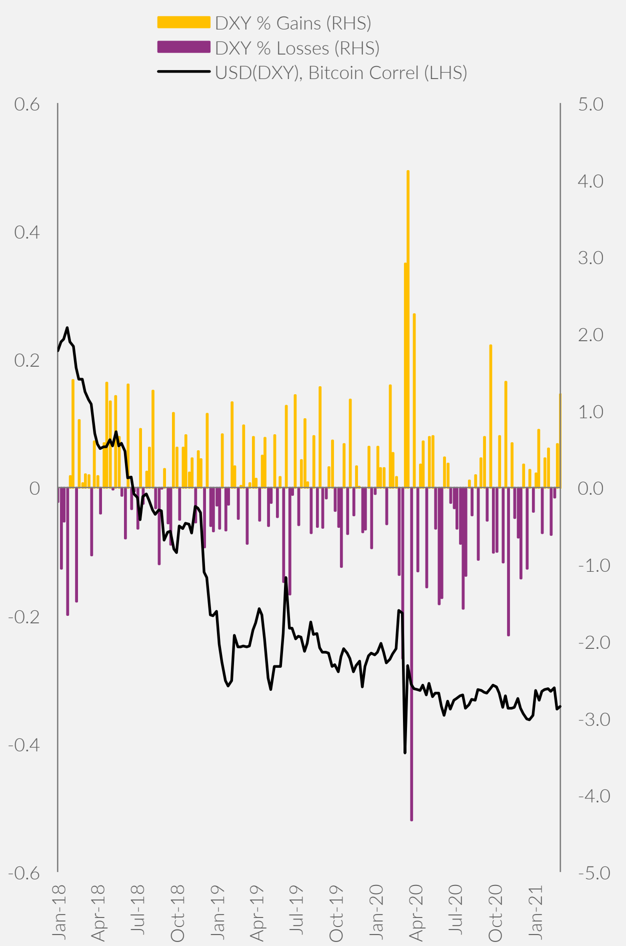
How does Bitcoin move with FX?

On the relationship between Bitcoin and FX, we also notice some interesting trends. Bitcoin's negative correlation with USD started emerging in 2019, and rose in magnitude in 2020.

One possible reason could be that with Bitcoin prices commonly denominated in USD, periods of decline in the dollar (versus other FX) leads Bitcoin to look cheaper in local currency terms for global investors, and this might encourage incremental bitcoin demand at the margin.

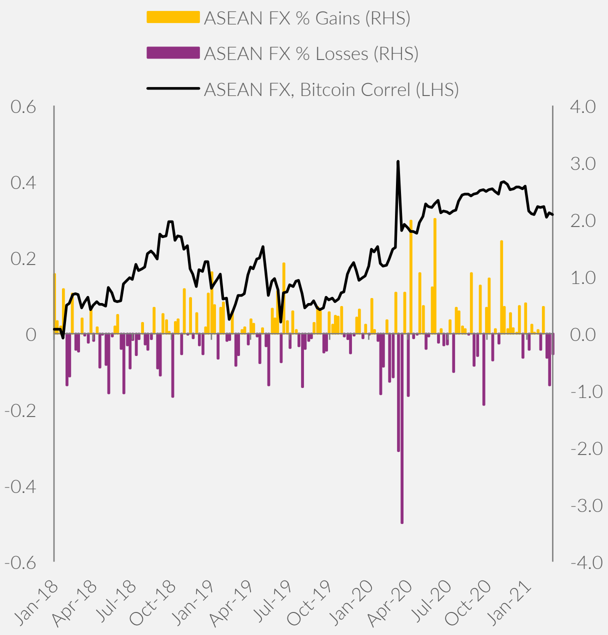
> "Segments of the Bitcoin mining industry have moved to invest in renewable energy projects to push for reduction in carbon emissions caused by cryptocurrency mining."

52-week rolling correlation between bitcoin returns and USD (DXY) % changes



Source: Bloomberg, Maybank FX Research & Strategy Estimates

52-week rolling correlation between bitcoin returns & ASEAN FX % changes



Source: Bloomberg, Maybank FX Research & Strategy Estimates

To some extent, this is corroborated by rising positive correlation between Bitcoin returns and ASEAN FX over the past one-and-a-half years.

These effects may also be more pronounced when trading volumes are larger—since 2019, Bitcoin trading volumes have spiked due to the introduction of leveraged trading in Bitcoin products as well as aforementioned growing institutional interest.

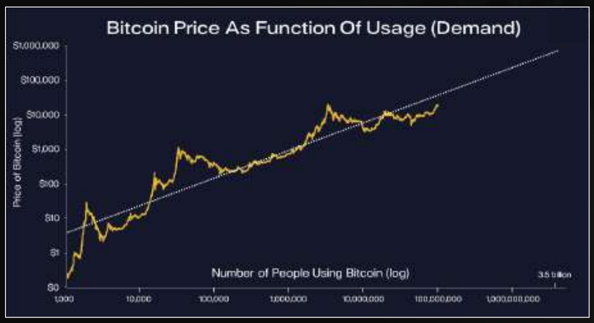
Of course, a softer USD, rising ASEAN FX environment post Mar-2020 is usually also synonymous with a global growth recovery outlook, so rising Bitcoin prices over the past few quarters could be pricing in some procyclical elements in market sentiments as well.

Network effects

Network effects is a key driver of cryptocurrency prices and adoption. This is suggested by the relationship of bitcoin price versus user adoption.

Bitcoin price appears to be driven by network effects

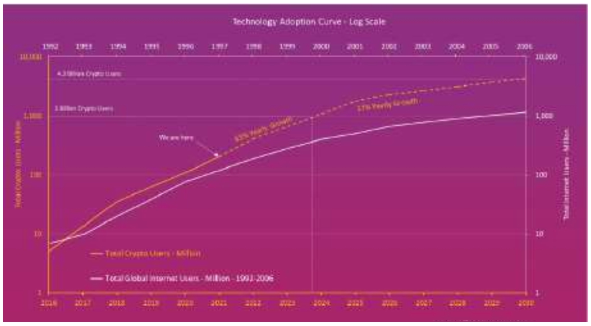
(as seen by the log scale used in the axes below)



Source: Pantera Capital

> “The blockchain technology market is expected to enjoy a 2018-25 CAGR of 65% to USD39.7b.”

Cryptocurrency adoption is already outpacing internet adoption in the 90s



Source: Crypto.com - World Bank

In terms of user adoption, cryptocurrencies appears to already be outpacing the adoption of the internet, and it is a trend that we believe investors should pay attention to.

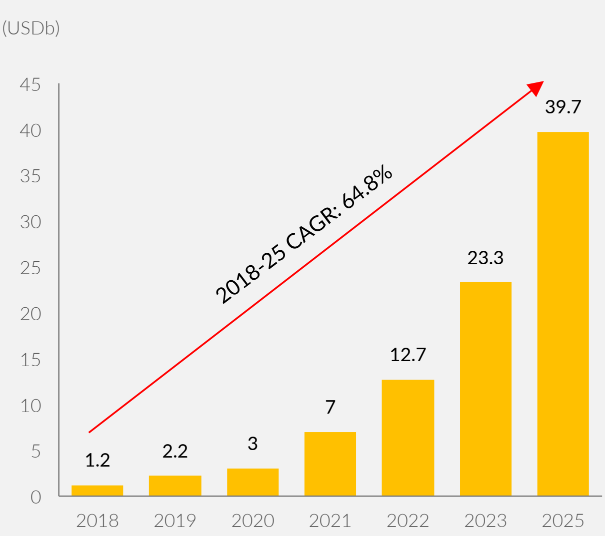
The blockchain marketplace

The blockchain technology market is expected to enjoy a 2018-25 CAGR of 65% to USD39.7b, according to Statista. In 2020, the top 3 applications were:

- Digital currency (33%)
- Data access/ sharing (32%)
- Data reconciliation (31%)

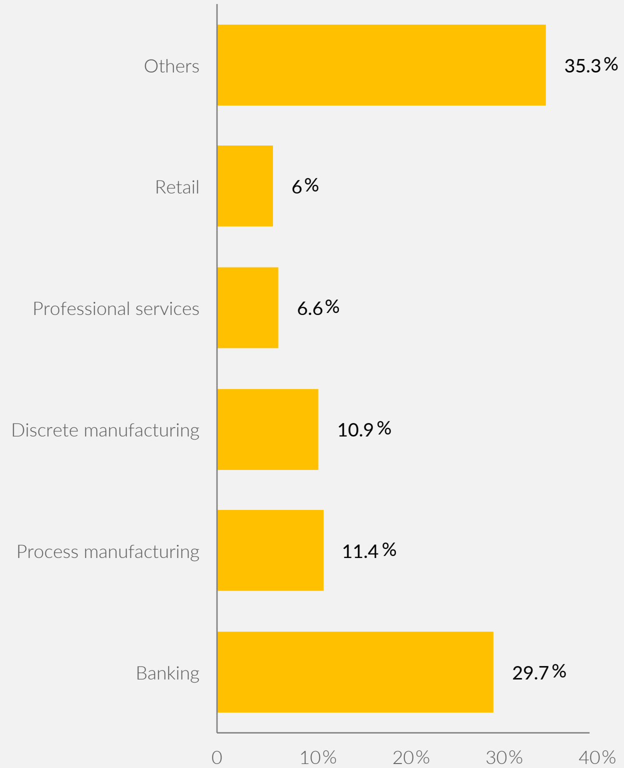
From a perspective of distribution by vertical in 2020, the banking sector accounted for the highest share, at 29.7%, followed by process manufacturing (11.4%) and discrete manufacturing (10.9%).

The blockchain market is expected to enjoy a 2018-25 CAGR of 65%



Source: Statista

Distribution of blockchain market value worldwide in 2020, by vertical



Source: Statista

Within the financial services sector, three of the highest impact and highest feasibility areas for blockchain are in:

- Cross border P2P payments
- Repurchase agreements and cross border B2B payments
- Trade and supply chain finance

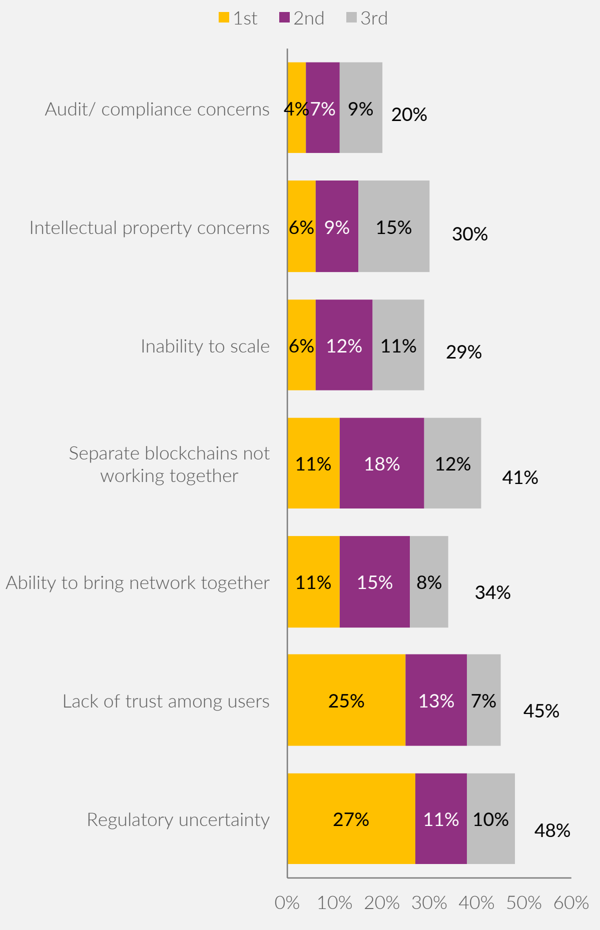
According to PwC, some of the big shifts that blockchain is altering in the business landscape include

- Tokenization (representation of assets on a blockchain)
- Initial coin offerings (ICOs) – companies that raise capital by selling a predefined number of digital tokens to the public; and
- Enterprise software platforms – e.g. Microsoft, Oracle, SAP and Salesforce have all announced blockchain initiatives, and in the future, many core business processes will run on/interoperate with blockchain based systems

While this emerging technology appears promising, adoption hurdles exist as well. In a 2018 PwC survey, 600 respondents were asked to rank the top 3 barriers to blockchain adoption. They were:

- Regulatory uncertainty (48%)
- Lack of trust among users (45%)
- The ability to bring networks together (44%)

Top 3 adoption hurdles in PwC's survey of 600 respondents in 2018



Source: PwC

New finance is here to stay

In Singapore, banks and other financial institutions have launched crypto and blockchain initiatives. In early 2021, DBS became the first traditional bank in ASEAN to launch its own digital exchange. In Apr-21, DBS, JP Morgan, and Temasek announced their new platform Partior, which leverages on blockchain to overcome the inefficiencies of the traditional "hub and spoke" cross-border payments model.

To conclude, a marked contrast in the current crypto rally as compared to 2017 is the exponential rise in institutional interest.

This comes on the back of:

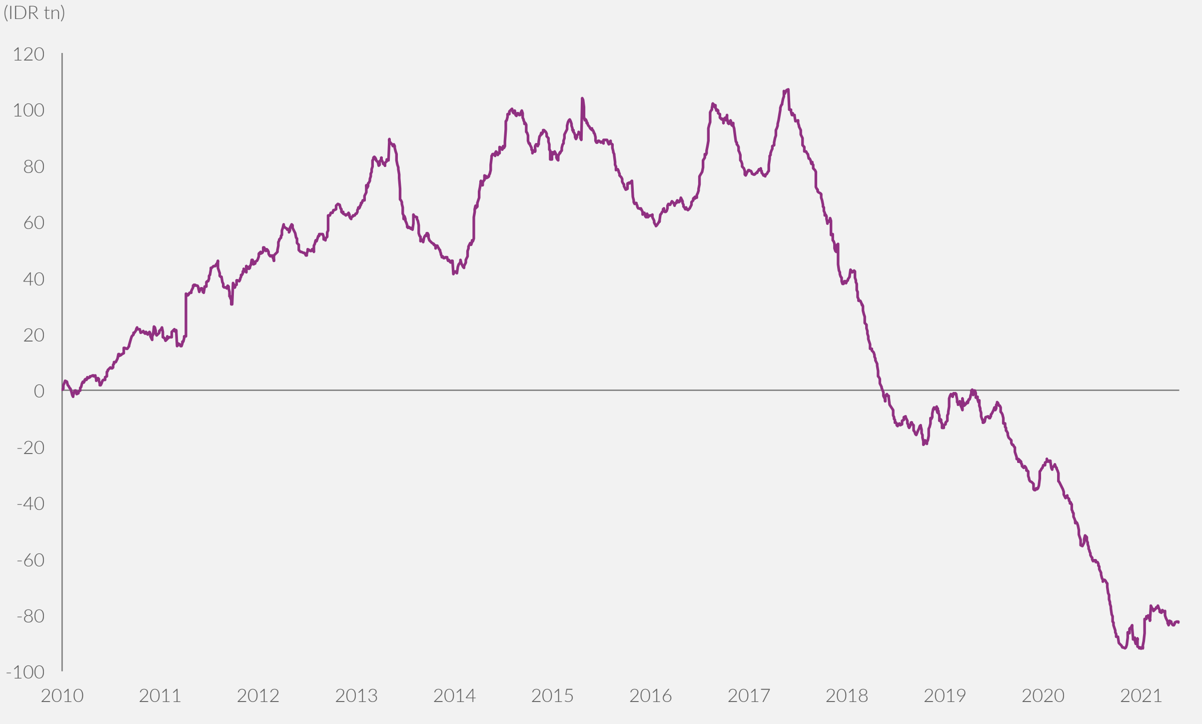
- Bitcoin being seen as a diversifier in asset allocation
- Regulators exploring the potential of central bank digital currencies
- Other financial institutions researching and leveraging blockchain to disrupt traditional methods of payments and cross-border transfers to remain relevant among its users

Given the disruptive potential and rapid gain in mindshare among retail, institutional and regulatory players alike, we believe developments in blockchain and cryptocurrencies can no longer be dismissed.

Indonesia

Entering a New Chapter

Cumulative Foreign Net Buy/Sell in Equity



Source: IDX, Maybank Kim Eng

Foreign fund flows have been on a declining trend since the middle of 2017 with net outflows of c. IDR200t. Foreign inflows started to emerge at the end of 2020 totaling c.15t. However, this trend has been reversed since mid-1Q21.

We attribute the net outflows to a couple of factors, such as increasing Covid cases, slower-than-expected economic and earnings recovery and the lack of tech stocks in ASEAN.

We think whether foreign investors will return to the market in near term will depend on the progress of the vaccination, which YTD has reached only c.6% of the population.

Other factors that could drive foreign inflows into the Indonesia market in the medium to long term include potential IPO of some technology companies and improving FDI due structural changes in the economy driven by the Omnibus law and industrialization in the mining sector.

The potential IPO of GoTo (Gojek Tokopedia), Bukalapak, and other technology companies in 2H21, will make Indonesia's market look attractive within ASEAN. This is not to mention that the weighting of the technology sector in the market could be substantial (we estimate 5-10%).

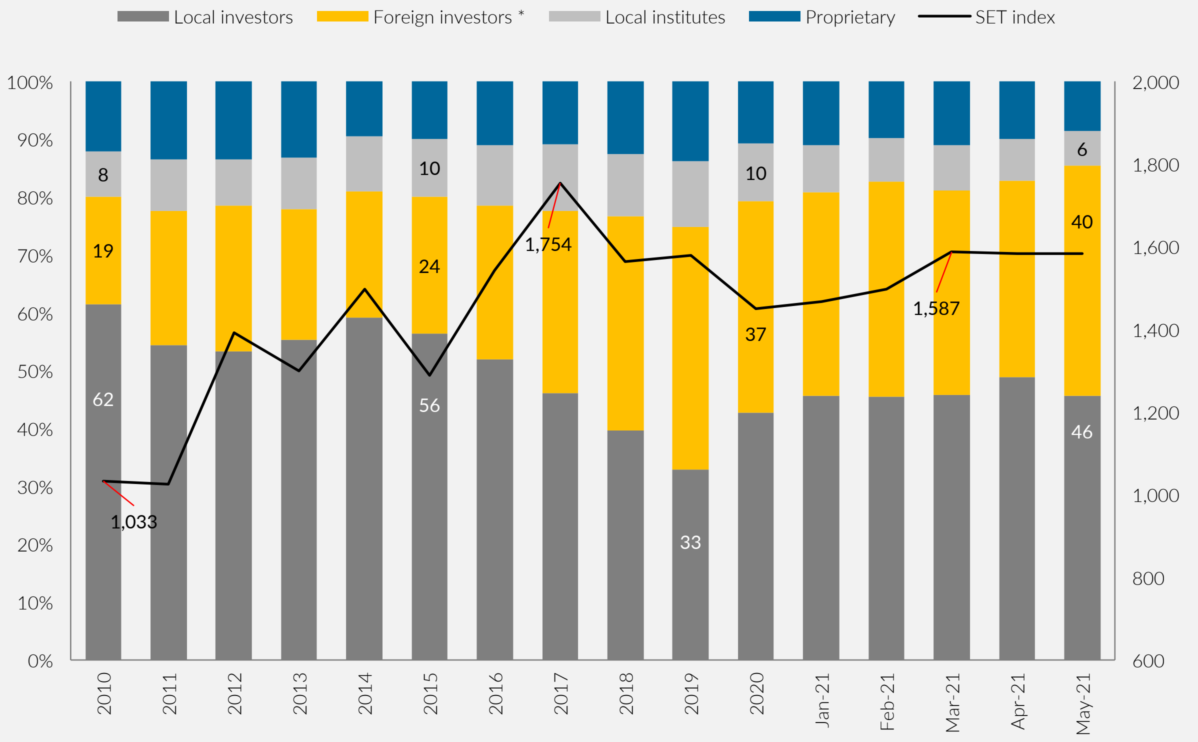
Meanwhile, we expect the Omnibus law will make the country more competitive in attracting FDI. The success of the law will structurally change the economy, which has not been factored in by the market.

Industrialization in the mining sector will be positive to both increasing volume and improving the quality of exports. Improvement in the trade balance should reduce foreign investors' concerns about the country's twin-deficit situation.

Thailand

Against All Odds

SET Trading Profile



* About half are passive funds
Source: SET, Maybank Kim Eng

Thailand's current account surplus has been diminishing and it has been in a slight deficit since Nov-20, and this is one reflection of the weaker economic conditions. However, this limitation on liquidity has had no impact on the stock market as funds from the government's stimulus programmes filled in the gap. The next round of stimulus programmes, worth THB300b, will serve the same function.

Retail investors have again become the most important driver of market turnover, at 46%, clawing back from the 2019 low of 33%, although still far below the 2010 high of 62%. Foreign investors also add to the dynamism of the SET, now accounting for 40% of daily turnover, the 2nd largest investor group. We estimate about half of these trades are passive funds.

With retail investors and passive funds in play, holding periods are shorter and market turnover higher. YTD, the average daily turnover was THB90b (c.USD3b), up 43% YoY. Internet trading has fast become an important platform within such a short period of time. In 1Q21 this was 40% of the total turnover, up from the 2020 average of 34.5%.

Retail investors and passive funds focus on growth and are largely story-driven. This is reflected in the 40% surge in the SmallCap index compared to the pre-Covid levels whereas big capitalization indexes are still below the pre-Covid levels.

The prevailing market features imply that, any market correction not linked to liquidity flows will not be deep, and that momentum and growth trumps value. The SET is trading at close to 3x SD>10-year average and it can stay at these lofty multiples for some time.