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FX Flash

SGD NEER, Nearer to Home

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Proxy Basket Trade in the Money; SGD NEER Could Fall Further

With the recent up-move in the USDSGD pair, and continued tame Singapore inflation figures earlier this week removing any potential obstructions to policy easing by the MAS in Oct, we re-look at the factors which could influence the trajectory of SGD NEER over the next few months.

We note that our call on 3 Jul to short SGD NEER via a proxy basket (weighted "basket" approach where we Long USD, CNH, MYR, IDR, PHP in 30%/35%/20%/10%/5% shares vs. Short SGD; see here) is in the money, with unleveraged gains of around 0.9% (as of market close yesterday), even before carry returns. We see a fair chance of further upsides from the trade with weakening momentum setting in for the SGD NEER.

The SGD NEER has fallen from around 1.8% above mid-point at end-Jun, to around 1.1%, as at yesterday's market close. After looking at outcomes from previous easing cycles stretching back to the GFC (2008), we think that a possible policy move by MAS in Oct could be a 1.0% reduction in policy slope (to neutral). This could potentially be consistent with an actual 1.0-1.5% falloff in SGD NEER heading into, and shortly after, the policy announcement, even as a softer USD in 2H remains a risk for this view.

We also take the chance to append some technical chart picks for USDSGD and SGD-crosses.

USDSGD - Bias to Sell Rallies.
Support at 1.3630; Resistance at 1.3690.

EURSGD - Bullish Divergence.
Support at 1.5150; Resistance at 1.5230.

AUDSGD - Break Out Higher.
Support at 0.9500; Resistance at 0.9550.

NZDSGD - Bullish Momentum Waning.
Support at 0.9080; Resistance at 0.9170.

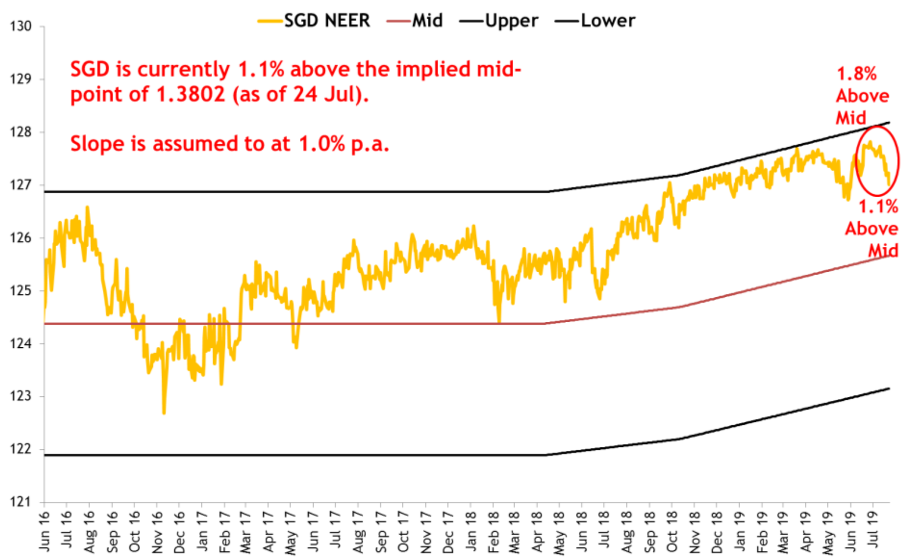
SGDMYR - Bias to Sell Rallies.
Support at 3.0140; Resistance at 3.0220.

CNHSGD - Upside Bias.
Support at 0.1977; Resistance at 0.1995.

SGD NEER - How Much Easing; When will it be Priced in?

As mentioned, SGD-NEER has fallen to around 1.1% above mid-point as of yesterday, compared to 1.8% as at end-Jun. USDSGD 3M forward points have narrowed to around -18.1 as at writing, from a recent trough of -24.4 on 10 Jul. It is likely that the weaker-than-expected 2Q Advanced sequential growth figure (-3.4% qoq saar, vs. expected 0.5%) released on 12 Jul led markets to price in a greater likelihood of potential MAS easing in the next policy meeting in Oct.

Chart 1: SGD NEER and Policy Band



Source: *Maybank FX Research & Strategy Estimates*

Conditional on 3Q macro outturns, we think that a move to neutral slope (from an estimated 1% appreciation path now) in the SGD NEER could be likely in Oct, consistent with our Economist team's views (see here).

Table 1: Policy Slopes (Estimates) and Macro Indicators during MAS Easing

				Macro Indicators (Avg. in Prior 2 Quarters Before Policy)				
	Slope Before Easing	New Policy Slope	Reduction in Slope Easing*	Headline Inflation	Core Inflation	Sg GDP (%yoy)	Sg GDP (%qoq saar)	World GDP (%y/y)
10-Oct-08	2.5%	0.0%	-2.5%	7.2	6.1	1.6	-6.4	2.5
14-Oct-11	2.5%	1.5%	-1.0%	5.4	2.2	5.4	4.5**	4.3
28-Jan-15	2.0%	1.0%	-1.0%	0.3	1.7	4.0	4.8	3.3
14-Oct-15	1.0%	0.5%	-0.5%	-0.5	0.4	3.3	5.0	3.2
14-Apr-16	0.5%	0.0%	-0.5%	-0.8	0.5	2.6	1.3	3.1

Source: *Bloomberg, Maybank FX Research & Strategy Estimates*
* All policy slopes and slope reductions are our estimates.
** 4.5% is the currently available final revised figure. Initial figures available to Authorities in 2011 (extracted from Policy Statement) showed a -2.5% qoq saar average over 2Q and 3Q 2011.

MAS is relatively forward-looking (i.e., considers medium-term inflation and growth outlook in setting policy), and a quick scan of the macro conditions at the time of easing is unlikely to give us a conclusive reading of their full policy considerations. Nonetheless, there are clues.

Larger reductions in slope (e.g., Oct 2008) seem to be reserved for GFC-type recessions. In any case, the current policy slope is estimated at 1%, and barring a re-centring downwards (which is not possible for now given that SGD NEER is still in the upper half of the band), a 1.0% slope reduction appears to be the most aggressive easing stance that MAS can adopt. The MAS has never adopted a negative policy slope.

0.50% reductions in slopes (Oct 2015, Apr 2016) seem to be associated with circumstances where (i) inflationary pressures were soft but picking up, and (ii) softer external demand led to modest drags on domestic growth, but full-year growth was still resilient, i.e., expected to average 2.0% or higher.

The 1.0% reduction in slope in Jan 2015 (off-cycle policy) was due to a down-shift in inflationary expectations led by the fall-off in oil prices in late-2014.

That leaves us with the Oct 2011 easing. At that time, supply-side disruptions from the earthquake in Japan and faltering global demand due in part to the sovereign debt crisis in Eurozone had led Sg GDP growth to average -2.5% qoq saar in 2Q and 3Q 2011 (figures available to Authorities at that point in time, as opposed to revised figures today).

On balance, we think a situation where average growth momentum in 2Q and 3Q this year comes in negative, expected annual growth falls to 1% or lower, and inflationary pressures continue to be tame (i.e., core inflation at 1-1.5% for 2019 and 2020), could see increased likelihood of a 1.0% reduction in slope (to neutral) at the next MAS policy meeting. Hence, policy decision would hinge on 3Q outturns.

Understanding the considerations behind MAS' policy decision is one thing. The actual movement in the SGD NEER pre- and post-policy decision is another.

Table 2: SGD NEER Level (Relative to Policy Mid-Point) Before/After Easing

		Positions of SGD NEER Relative to Policy Mid-Point (+ve = above)					
	Estimated Reduction in Slope	3 Months Before	1 Month Before	1 Day before	Policy Announce-ment Day	1 Month Later	Cumulative Change (3M prior to 1M post)
10-Oct-08	**-2.5%**	1.7	-0.4	-1.5	-1.5	-1.1	**-2.8**
14-Oct-11	**-1.0%**	2.5	0.9	-1.1	-0.4	-1.6	**-4.1**
28-Jan-15	**-1.0%**	0.2	0.1	-0.3	-1.1	-1.5	**-1.7**
14-Oct-15	**-0.5%**	-0.1	-0.7	-1.5	-0.1	-1.2	**-1.1**
14-Apr-16	**-0.5%**	-1.5	-0.1	0.3	-0.5	-0.3	**1.2**

Source: *Bloomberg, Maybank FX Research & Strategy Estimates*

From Table 2, we note that a large part of the softening in SGD NEER actually occurs before the actual policy announcement. Movement on the day of policy announcement itself would depend on market expectations at the time. On Jan 2015, the off-cycle policy caught markets off-guard, and the intra-day movement was almost equivalent to the extent of the easing.

More importantly, we look at the cumulative change in the levels of the SGD NEER (relative to policy mid-point) from three months prior to 1 month post policy announcement.

For the Oct 2011 easing, the three months leading up to the policy meeting had coincided with a period of significant pullback in investor risk appetite on concerns over a deepening Eurozone debt crisis and softer growth prospects for Asia; hence the "magnified" downward pressure on SGD NEER.

For the Apr 2016 easing, the SGD NEER strengthened just before the policy meeting as financial markets revised downwards their expectations of the Fed's normalisation pace, and the USD saw broad-based weakness. SGD NEER actually weakened by 0.6%, if we compare the day before policy announcement and 1 month after.

We discount the two instances above due to the unique set of macro-conditions then, and look instead at the other easing exercises (Oct 2008, Jan 2015, Oct 2015). For these, the resulting easing effect was estimated to be modestly greater than the policy slope change, by around 0.3% to 0.7%.

In this case, if the MAS policy in Oct is indeed a 1% reduction in slope (to neutral), we think that SGD NEER could potentially fall by around 1-1.5% in the coming months. Compared to its position today (1.1% above mid-point), it could be closer to, or modestly below the policy mid-point post-Oct.

Nonetheless, we note that one risk to this view is the extent of softening in the USD in 2H this year, especially with the first Fed policy cut (for more than a decade) expected to be delivered next Wed. A broadly softer USD could weigh on the USDSGD pair to some extent and mitigate the extent of SGD NEER's fall.

Technical Charts for USDSGD and SGD-Crosses

USDSGD Daily Chart - Bias to Sell Rallies

Easing expectations have begun to set in; the SGD NEER is estimated to have come off from 1.8% above mid-point during end-Jun to 1.1% above mid-point today. We look for SGD NEER to stay in the 0.75-1.25% above mid-point range in the interim, which translates to around 1.3630-1.3700 range for SGD. Momentum on the daily chart is bullish, but stochastics are in overbought conditions. Bias to sell rallies. Levels last seen at 1.3647. Previous resistances at 1.3630 (200 DMA), 1.3610 (100 DMA, 61.8% Fibonacci retracement from 2019 low to high) have turned support. Resistance at 1.3690 (38.2% fibo), 1.3750 (23.6% fibo).

EURSGD Daily Chart - Bullish Divergence

Momentum indicators are mildly bearish, but we note that potential bullish divergence may be forming on daily chart, and the pair is inching towards near-oversold conditions. This could be indicative of a potential reversal upwards. This is also consistent with our longer-term view of a constructive bias for the EUR—premised on slowing Fed-ECB policy divergence (coming from more dovish Fed), even as SGD could see some weakness as easing expectations set in. Levels last seen at 1.5201. Support at 1.5150 (2019 low). Resistances at 1.5230 (76.4% fibo retracement from 2019 low to Jun high), 1.5300 (100 DMA).

AUDSGD Daily Chart – Break Out Higher

This cross tapered off and hovered around 0.9522. Daily momentum loses bullish bias while stochastics is in overbought conditions. This cross is retracing towards the 0.95-figure, and interim EUR down-move in the face of ECB meeting could also be negative for this cross. But we see chance of break out higher post-ECB policy meeting. Resistance at 0.9550 (100 DMA), 0.9640 (23.6% fibo retracement of 2017 high to 2019 flash crash low). Support at 0.95 (50 DMA), 0.9460 (21 DMA).

NZDSGD Daily Chart – Bullish Momentum Dissipating

NZD backed off from recent highs, weighed by RBNZ's comments that it could revisit its strategy for unconventional monetary policy, encouraging speculation that rates could remain low for an extended period of time. Levels last seen at 0.9135. Bullish momentum shows signs of waning while stochastics is showing signs of turning from overbought conditions. Near term risks skewed to the downside. Support at 0.9080 (100 DMA), before 0.9030 (50 DMA) levels. Resistance at 0.9170 (200 DMA).

SGDMYR Daily Chart - Bias to Sell Rallies

Levels last seen at 3.0176. Bearish momentum on daily chart remains intact while stochastics is in oversold conditions. We remain cautious of rebound risks given oversold conditions, but prefer to sell rallies given bearish momentum. Resistance at 3.0220, 3.0340 levels (200 DMAs, 23.6% fibo retracement of 2018 low to 2019 high). Immediate support at 3.0140 (38.2% fibo), 2.9980 (50% fibo).

CNHSGD Daily Chart – Upside Bias

This cross strengthened towards 0.1983 and MACD maintains an upside bias. Momentum on the daily chart is modestly bullish. Next resistance is seen at 0.1995 (100, 200 DMA). Support at 0.1977 (50-dma) before 0.1974 (21-dma).

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