FX Insight

SGD Preview: Can SGD Outperformance Continue?

MAS is Likely to Stand Pat and See Stance as Appropriate

Our view is for MAS to maintain the prevailing monetary policy parameters at the upcoming Jan policy meeting. The economic recovery continues as the latest 4Q GDP print showed an acceleration in growth to 2.8%, with rebounds in both manufacturing and construction. Core inflation remains above MAS' comfort levels and is forecasted to remain sticky above historical norms in 2024 at 2.8%. MAS is thus likely to stand pat at the Jan meeting and could continue to see the current stance as "sufficiently tight". **We think that SGDNEER is likely to stay supported although outperformance of SGDNEER could taper.**

SGDNEER Outperformance Could Taper

Back in Oct-23 (see here), we maintained a bullish bias on the SGDNEER and suggested that the SGDNEER could outperform, suggesting to buy the SGDNEER basket on dips. We saw continued outperformance of the SGDNEER from "haven" characteristics versus its peers in a period of elevated uncertainty and our Taylor Rule implied SGDNEER model continued to suggest upward pressures on the SGDNEER. Indeed, in the wake of MAS' Oct stand pat, the SGDNEER has been extremely strong (average: +2.10%) as the USDSGD also traded lower (from 1.37 levels to 1.32 levels) over the same period. Singapore's robust macro fundamentals and unique exchange rate policy, which results in SG rates being highly correlated with US rates, underpinned the outperformance of the SGDNEER against a narrative that US rates would remain higher for longer. As we approach a time where potential rate cuts are being discussed, we think that the expectation of Fed rate cuts could lead to a tapering off in SGDNEER strength - specifically if basket constituents start to outperform the SGD i.e. appreciate by more against the USD than the SGD as the Fed cuts rates.

USDSGD to Come Off Gradually

We also maintain our forecasts for USDSGD to come off gradually, i.e. for SGD to strengthen against the USD gradually through 2024. This is based on the belief that SGD will continue to stay resilient as MAS stands pat on policy and the Fed cuts rates. The current pace of SGDNEER appreciation (assumed to be 1.5%) should continue to be supportive of the SGD. Fed rate cuts should also be supportive of SGD strength, although cuts could benefit other constituents more than the SGD. Rate cuts narrow interest rate differentials between the US and other countries, which should result in a weaker USD and could lead to outperformance of constituents which have their own explicit interest rate policy. While the SGD should strengthen against the USD, it could then underperform basket constituents given that Singapore does not have an explicit interest rate policy and is a price taker for interest rates.

Analysts

Saktiandi Supaat
(65) 6320 1379
saktiandi@maybank.com.sg

Shaun Lim
(65) 6320 1371
shaunlim@maybank.com

Fiona Lim
(65) 6320 1374
fionalim@maybank.com.sg

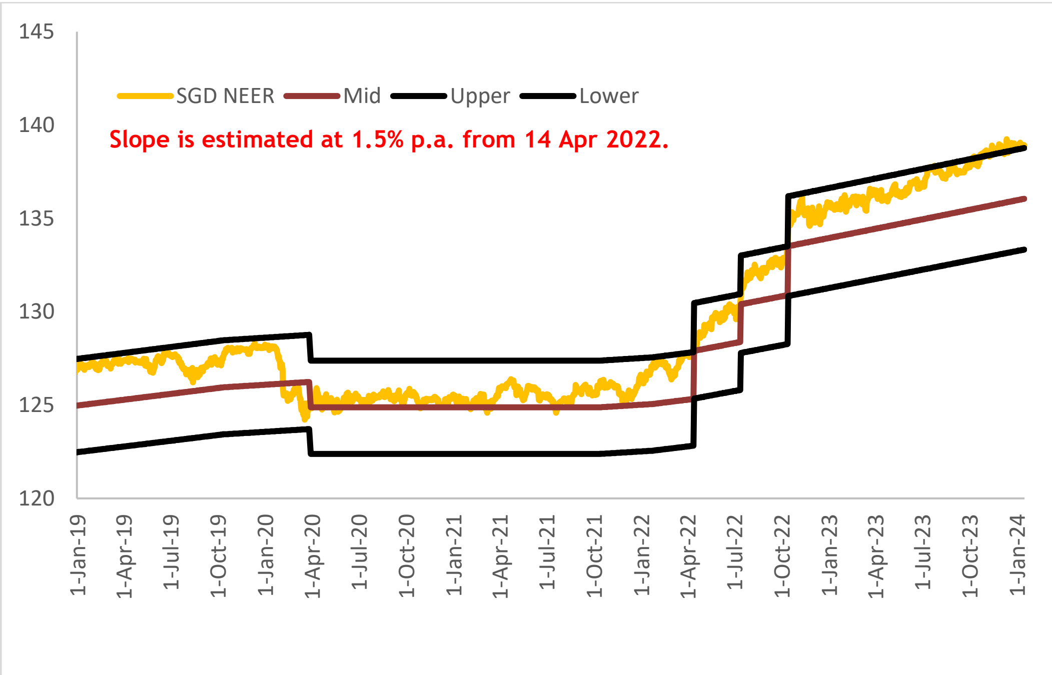
Alan Lau
(65) 6320 1378
alanlau@maybank.com

SGDNEER Outperformed since Oct Stand Pat

In Oct, MAS stood pat as policy was assessed to be sufficiently tight against a backdrop of gradually improving growth and slowing inflation. While inflation has come off and growth has gradually improved in line with the outlook, core inflation remains above MAS' comfort zone. SGDNEER has remained firmly in the upper half of the band and has even exceeded the upper end of the band in our model in the wake of the Oct decision (Chart 1). We believe that MAS will stand pat once again at the Jan meeting given that core inflation remains elevated and on the belief that the gradual economic recovery can continue.

Following MAS' stand pat stance, we suggested buying SGDNEER on dips (see here) and here) as upward pressures on the SGDNEER would remain and that the SGD would outperform. Since then, USDSGD has traded lower (from 1.37 levels to 1.32 levels) and the SGDNEER has remained firm with the average deviation from the mid-point at +2.10% since Oct. We think that SGDNEER could remain supported going forward, although outperformance could eventually taper off - especially if SGDNEER basket constituents start to do better against the USD (than the SGD) in an environment of rate cuts, which could happen.

Chart 1: SGDNEER at Elevated Levels since Oct



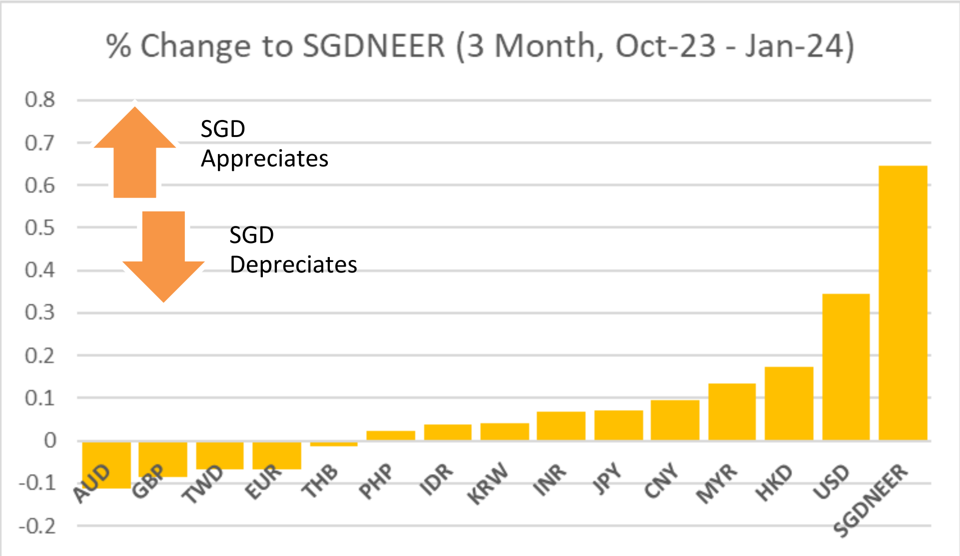
Source: Bloomberg, Maybank FX Research & Strategy

The "safe-haven" qualities of the SGD - its resilience both in bilateral and trade-weighted contexts against most other currencies continues to hold. The SGDNEER demonstrated remarkable resilience primarily because the SGD served as a notably steadfast store of value compared to most other basket currencies amidst market fluctuations (Chat 2a, 2b and 2c). This durability can be attributed to Singapore's robust macro fundamentals, including fiscal resilience, and the credibility of MAS' unique monetary policy, which is based on the exchange rate. In contrast to numerous other currencies impacted by widening yield differentials due to a more hawkish Fed, Singapore remains shielded thanks to the absence of an explicit interest rate policy and a robust correlation (estimated at 97%) between SG rates and US rates (Chart 4). Additionally, the SGD derived support from a positive crawl rate (presumed to be +1.5%) against its peers in the

SGDNEER basket. Notably, this crawl rate has consistently stayed above 0%, further instilling investor confidence in the SGD and fortifying the credibility of MAS' policy.

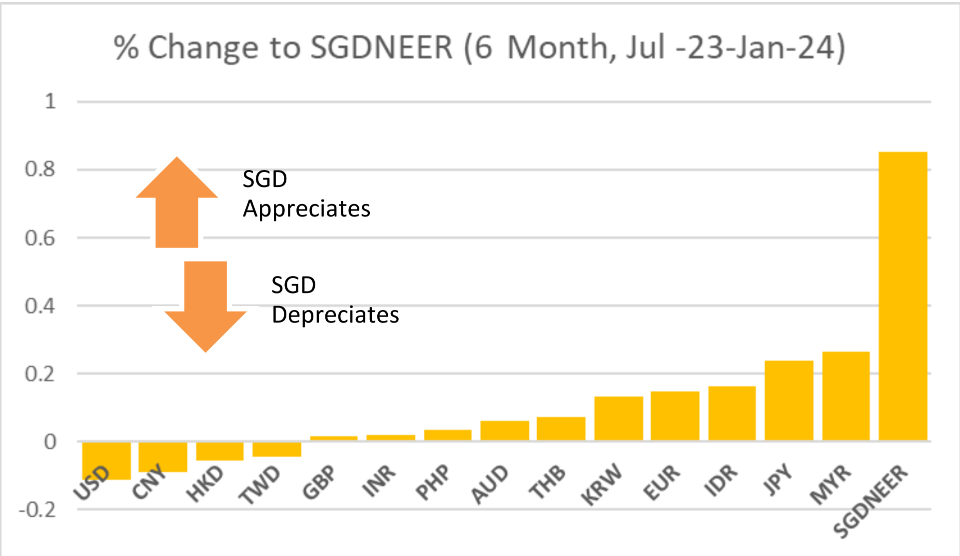
SGDNEER has remained elevated and gained about 2.21% over a 12-month period (Chart 2c). While Asean FX volatility remained relatively stable, SGDNEER has continued to edge up and remained at elevated levels (Chart 3). Over a 6-month and 12-month horizon, the USD bloc (USD and HKD) had been a moderator of SGDNEER strength. However, this has changed over the 3-month horizon, with the USD bloc actually being the main contributor to SGDNEER strength amid rate cut expectations. We think that given these developments, other constituents could actually moderate the strength in the SGDNEER when rate cuts finally happen, and this should allow SGDNEER outperformance to taper.

Chart 2a: 3-Month SGDNEER Strength Largely Due to Dollar Bloc



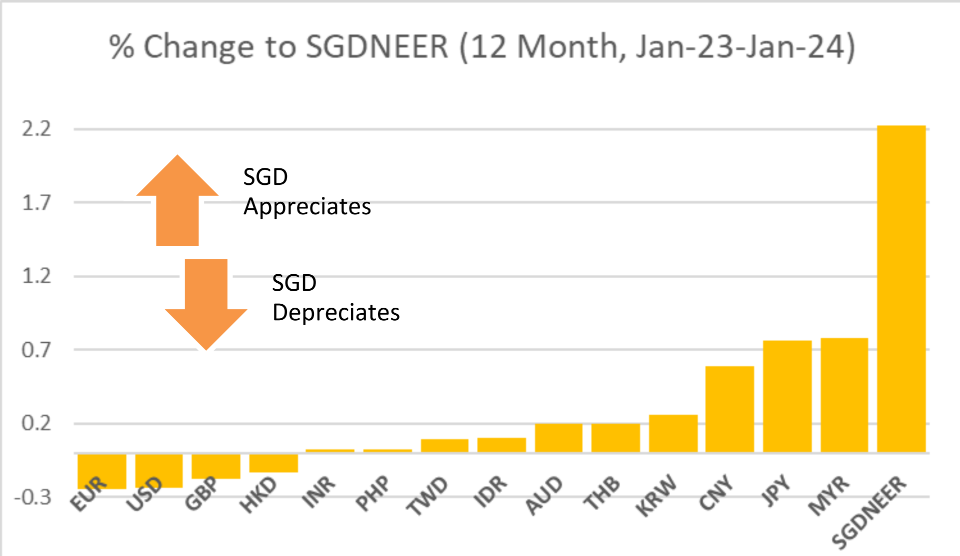
Source: Bloomberg, Maybank FX Research & Strategy

Chart 2b: 6-Month SGDNEER Strength More Broad-Based



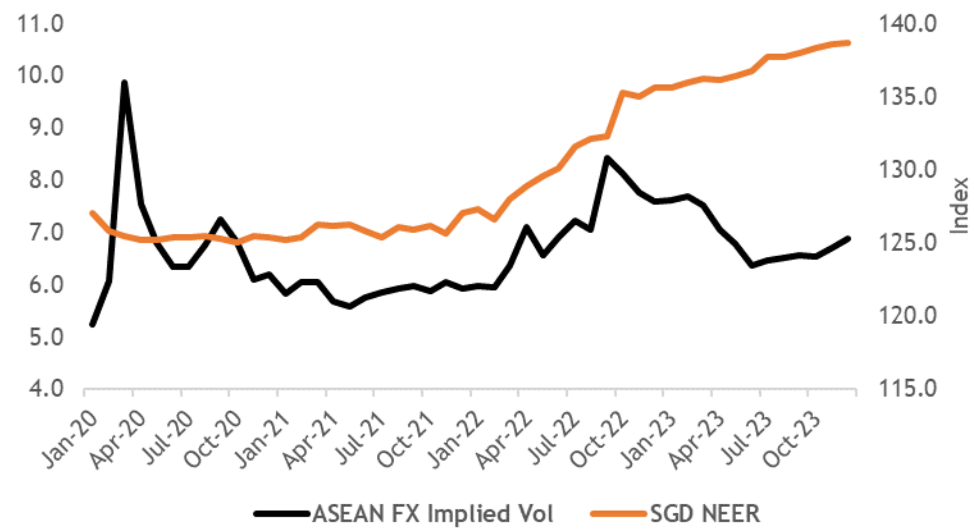
Source: Bloomberg, Maybank FX Research & Strategy

Chart 2c: 12-Month SGDNEER Strength from MYR, JPY and CNY offset by EUR, USD Block and GBP



Source: Bloomberg, Maybank FX Research & Strategy

Chart 3: SGDNEER (RHS) Elevated Amid Relatively Stable Volatility



Source: Bloomberg, Maybank FX Research & Strategy

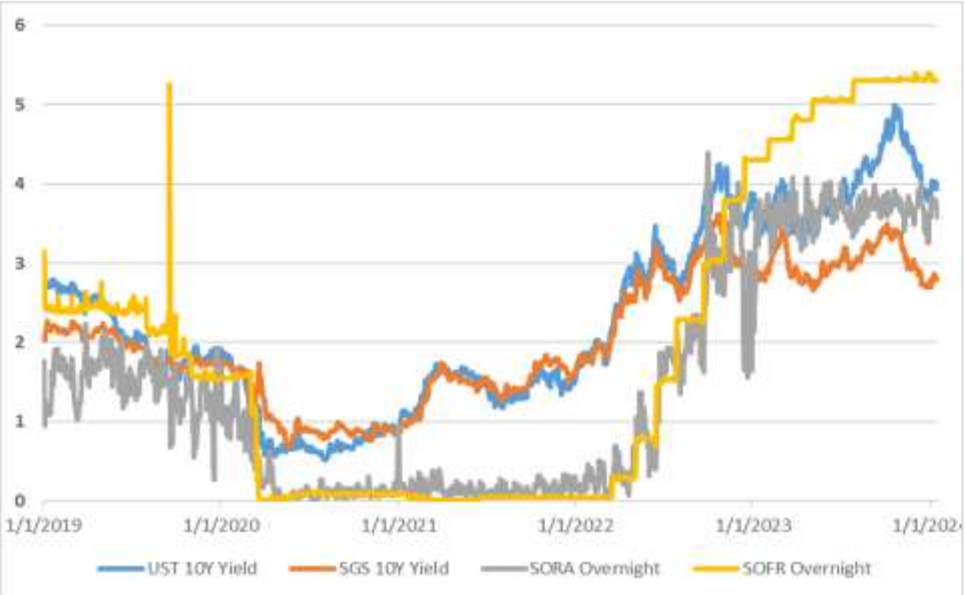
Since the Oct MAS policy decision, SGDNEER appreciation has been due to the SGD appreciating against the USD bloc, MYR and CNY. Over the same period, SGDNEER strength was moderated by gains in the AUD, GBP, and TWD. We see that this is in line with the soft-landing narrative as pairs that tend to do well with improvement in risk sentiment outperformed. Should this trend continue, it could further support our thesis that SGDNEER outperformance could taper as growth improves later in 2024 and inflationary pressures recede.

However, we do maintain that the SGDNEER should remain resilient amid market fluctuations, given that the Singapore's strong macroeconomic fundamentals such as persistent current account and fiscal surpluses. So while SGDNEER outperformance could taper, we do not expect SGDNEER strength to turn to weakness as long as MAS maintains its appreciating crawl of the SGDNEER. Our economists currently expect MAS to stand pat for the first three meetings of 2024 and ease the slope slightly at the Oct meeting.

Global and domestic interests rates have come off in the last quarter of 2023 (Chart 4). Our fixed income analysts are expecting US rates to decline in 2024 which should continue to weigh on the USD in 2024. Alongside this, financial conditions have become less restrictive (Chart 6), while growth and inflation are broadly in line with MAS' forecasts (Chart 5).

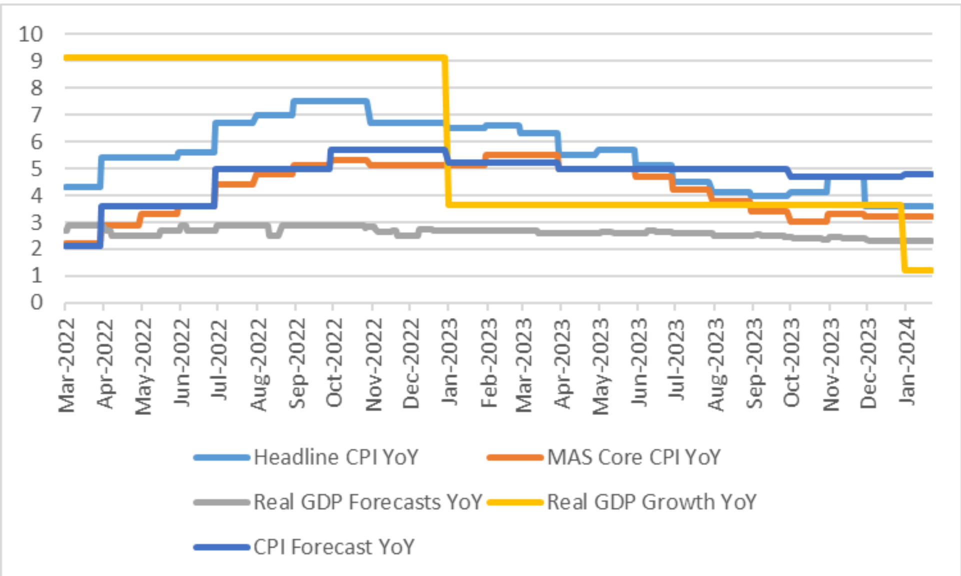
Therefore, it is likely MAS will stand pat in Jan, and the continued appreciating stance (assumed to be +1.5% p.a.) in the SGDNEER should continue to provide support for the SGD.

Chart 4: USD Rates and SGD Rates Remain Highly Correlated



Source: Bloomberg, Maybank FX Research & Strategy

Chart 5: Singapore Growth and Inflation Broadly in Line with MAS Forecasts



Source: Bloomberg, Maybank FX Research & Strategy

Chart 6: Financial Conditions Are Less Restrictive

Source: Macrobond, Maybank FX Research & Strategy

MAS is Likely to Stand Pat (29 Jan 2024)

Although upside risks to inflation still exist and while there are downside risks to growth as well, MAS is unlikely to prematurely switch to a growth supporting mode. MAS previously referred to the policy stance as "sufficiently tight" and "appropriate". **Actual growth and inflation prints have largely come in line with MAS' forecasts and we think that they will continue to view the current appreciating stance as appropriate given current balance of risks.**

Full-year GDP growth came in at +1.2% in 2023, a shade above our economists' +1.1% forecast. Growth should be stronger and more balanced and our economists forecast economic growth of +2.2% in 2024, as manufacturing recovers while revenge spending in services moderates. Trade-related and outward-oriented services sectors, including wholesale trade and financial services, will return to growth in 2024 with the global demand pickup and easing domestic interest rates. Our economists' 2024 GDP forecast of +2.2% stands at the higher end of MTI's 1%-3% forecast range. This is predicated on a rebound in manufacturing seen in 2023, which our economists think could herald a brighter outlook for exports and manufacturing in 2024. MAS' forward looking policy stance therefore suggests there is no need to prematurely shift to a growth supporting stance (i.e. easing bias) and should continue to see the current stance as appropriate.

Core inflation was at +3.2% in Nov-23, and our economists see a likely uptick in early 2024 given hikes in GST, carbon taxes and other administrative prices including water and public transport. Core inflation will remain sticky and above historical norms in 2024 (Maybank forecast: +2.8%), given that labor costs could stay elevated due to the tight job market and stricter manpower measures. Higher wage costs from the expansion and scheduled increases in the Progressive Wage Model scheme, stricter dependency ratio ceiling, and recent hikes to qualifying work pass salaries will likely keep wage cost pressures elevated.

Market consensus based on the MAS survey (Table 1) is also overwhelmingly in favour of a stand pat in Jan, with a minority expecting easing via a slope reduction from the Apr meeting onwards. Our economists see MAS standing pat for three meetings and easing in Oct 2024.

Table 1: MAS Survey of Professional Forecasters (% of respondents)

MAS Actions	Sep Survey		Dec Survey			
	2023 Oct	2024 Apr	2024 Jan	2024 Apr	2024 Jul	2024 Oct
Increase slope	0.0	5.6	0.0	0.0	0.0	0.0
Reduce slope	0.0	27.8	0.0	13.0	21.7	18.2
Flatten slope	0.0	0.0	0.0	0.0	0.0	4.5
Unchanged	100.0	66.7	100.0	87.0	78.3	77.3
Re-center higher	0.0	0.0	0.0	0.0	0.0	0.0
Re-center lower	0.0	5.6	0.0	0.0	0.0	4.8
Unchanged	100.0	94.4	100.0	100.0	100.0	95.2
Widen band	0.0	0.0	0.0	0.0	0.0	0.0
Narrow band	0.0	0.0	0.0	0.0	0.0	0.0
Unchanged	100.0	100.0	100.0	100.0	100.0	100.0

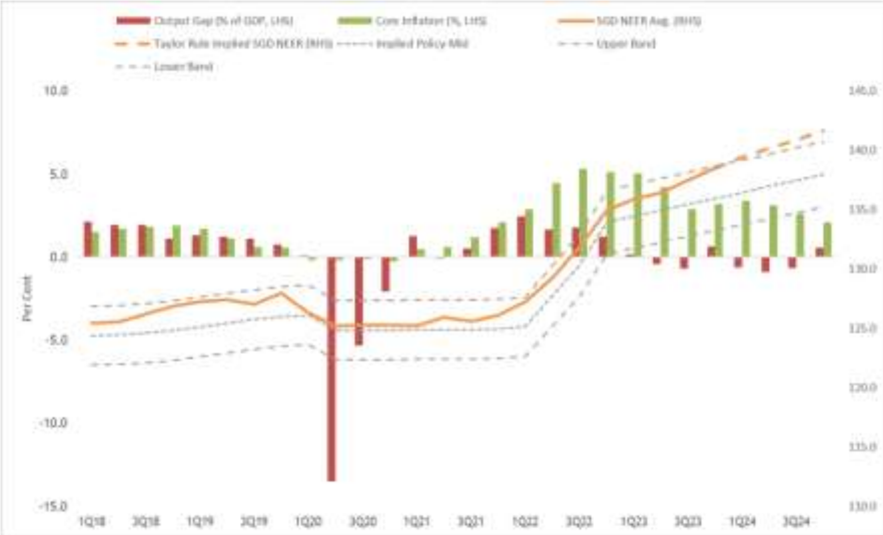
Source: MAS, Maybank FX Research & Strategy

SGDNEER Likely to Outperform

For a check on the potential trajectory for SGDNEER going forward, we turn to our Taylor rule model to derive an implied SGDNEER (Chart 7). Core inflation (green bars) has exceeded 2% since Dec 2021 and looks to remain sticky above 2% through 2024. Our economist team's latest forecasts for core inflation and headline inflation in 2024 are 2.8% and 3.0%, respectively. Based on our estimates and our economists' growth forecasts, the small negative output gaps (red bars) should turn mildly positive by the end of 2024.

Given these macroeconomic conditions, our Taylor rule implied SGDNEER estimates (dotted orange line in Chart 7 below) suggest that SGDNEER is likely to continue seeing upward pressures in the coming quarters. Notably, our estimates imply that the SGDNEER could continue to see upward pressures into 2024. This is largely due to inflation remaining high for longer which in turn implies that the central bank should maintain a sufficiently restrictive monetary policy stance.

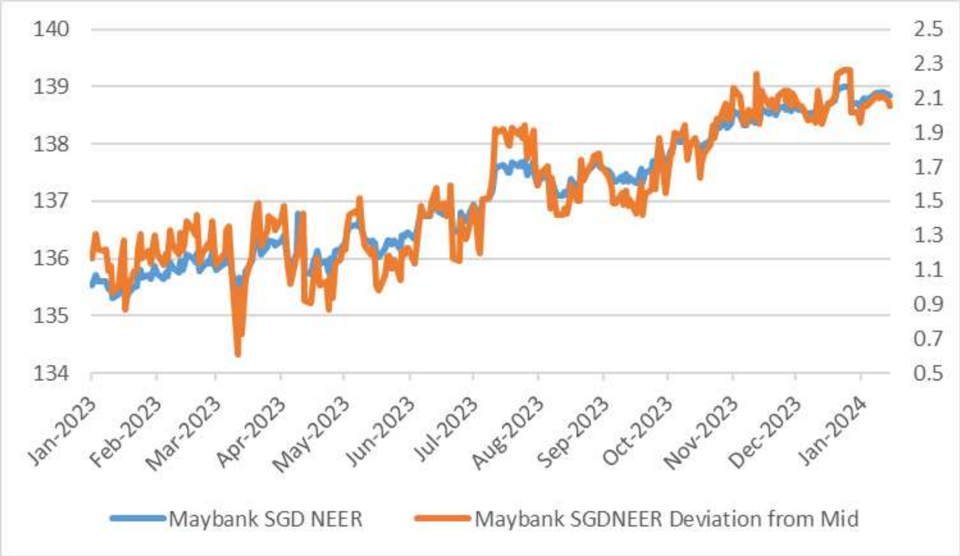
Chart 7: Upward Pressures on SGDNEER Persist (Taylor Rule Estimates)



Source: Bloomberg, Maybank FX Research & Strategy Estimates

As mentioned earlier, the SGD has outperformed on a trade-weighted basis, reflected in SGDNEER moving higher (Chart 8). Year-to-date, the SGDNEER has continued to remain strong and hovers around the 2% deviation from the mid-point. Our assessment that MAS is likely to stand pat in Jan, and the continued appreciating stance (assumed to be +1.5% p.a.) in the SGDNEER should provide plenty of support for the SGD and result over time in a lower USDSGD. We do see rate cut expectations perhaps enabling other basket constituents to outperform the SGD and we could see the SGDNEER outperformance taper. Rate cuts narrow interest rate differentials between the US and other countries, which should result in a weaker USD and could lead to outperformance of constituents which have their own explicit interest rate policy. While the SGD should strengthen against the USD, it could then underperform basket constituents given that Singapore does not have an explicit interest rate policy and is a price taker for interest rates. However, we also do not foresee a complete capitulation of SGDNEER strength and think that SGDNEER should remain supported on dips.

Chart 8: SGDNEER Performance (%, LHS) and Deviation from Mid (%, RHS)



Source: Bloomberg, Maybank FX Research & Strategy

USDSGD to Come Off Gradually

Against the backdrop of a soft-landing where growth improves and inflation remains on a downward trajectory, we suggest that the USD should gradually weaken. This is reflected in a gradual easing in the USDSGD through 2024 as suggested in our latest annual forecasts (Table 2). Several themes, such as the export/manufacturing recovery, AI exuberance and bottoming of the chip cycle mentioned in our annual outlook are further supportive of the SGD.

Table 2: Quarterly USDSGD Forecasts

Forecast	1Q 2024	2Q 2024	3Q 2024	4Q 2024
USDSGD	1.3500	1.3450	1.3400	1.3350

Source: Maybank FX Research & Strategy Estimates

What is Next for MAS?

We lay out the past policy moves since Apr 2016 (Table 3). Over the course of the next 3 policy announcements by MAS, the possible moves will reflect a change in the balance of risks if inflationary pressures ease and growth prospects worsen. While not our base case, we do not rule out a low probability scenario of a MAS "double" easing i.e. a re-centre downwards with a slope reduction. This last happened in Mar 2020 in response to Covid and could occur if there is a drastic improvement in the inflation outlook (6 to 9 months ahead) and/or a significantly worse growth outlook. As a starting point, we would look out for inflation/growth outturns that deviate significantly from MAS' forecasts. Risks such as geopolitical tensions in the Middle East and the Red Sea blockade could exacerbate and precipitate such a scenario and affect the 6-12 month outlook which affects the policy deliberations. To recap, MAS can adjust the slope of the band, the level at which the band is centred or the width of the band. The latter is usually done to accommodate volatility, while adjustments to the slope or level at which the band is centred are to ease/tighten policy as appropriate. So at this juncture, the most likely move in Oct 2024 is a slight reduction to the slope if the inflation and growth trajectory pans out over the next few quarters as our economists expect.

Table 3: Recent MAS Actions and *Possible Future Actions*

Date	Slope of Band	Width of Band	Level at Which Band is Centred	Comments
Oct 2024	*Economists see Slope Reduction*			
Jul 2024	*Likely Stand Pat*			
Apr 2024	*Likely Stand Pat*			
29 Jan 2024	*Likely Stand Pat*			
13 Oct 2023	-	-	-	-
14 Apr 2023	-	-	-	-
14 Oct 2022	-	-	Re-centre upwards at prevailing level	-
14 Jul 2022	-	-	Re-centre upwards at prevailing level	Off-cycle decision
14 Apr 2022	Increase slightly	-	Re-centre upwards at prevailing level	1.5% slope
25 Jan 2022	Increase slightly	-	-	Off-cycle decision 1% slope
14 Oct 2021	Increase slightly	-	-	0.5% slope
14 Apr 2021	-	-	-	-
14 Oct 2021	-	-	-	-
30 Mar 2020	Set at 0%	-	Re-centre downwards at prevailing level	Covid Period easing
14 Oct 2019	Reduce slightly	-	-	0.5% slope
12 Apr 2019	-	-	-	-
12 Oct 2018	Increase slightly	-	-	1% slope
13 Apr 2018	Increase	-	-	0.5% slope

	slightly			
13 Oct 2017	-	-	-	-
13 Apr 2017	-	-	-	-
14 Oct 2016	-	-	-	-
14 Apr 2016	Set at 0%	-	-	-

Source: MAS, Maybank FX Research & Strategy

'-' denotes no change to the policy parameters

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Published by:

Malayan Banking Berhad
(Incorporated In Malaysia)

Foreign Exchange

Singapore
Saktiandi Supaat
Head, FX Research
saktiandi@maybank.com.sg
(+65) 6320 1379

Fiona Lim
Senior FX Strategist
Fionalim@maybank.com.sg
(+65) 6320 1374

Alan Lau
FX Strategist
alanlau@maybank.com
(+65) 6320 1378

Shaun Lim
FX Strategist
shaunlim@maybank.com
(+65) 6320 1371

Indonesia
Juniman
Chief Economist, Indonesia
juniman@maybank.co.id
(+62) 21 2922 8888 ext 29682

Myrdal Gunarto
Industry Analyst
MGunarto@maybank.co.id
(+62) 21 2922 8888 ext 29695

Fixed Income

Malaysia
Winson Phoon
Head, Fixed Income
winsonphoon@maybank.com
(+65) 6340 1079

Se Tho Mun Yi
Fixed Income Analyst
munyi.st@maybank-ib.com
(+60) 3 2074 7606

Sales

Malaysia
Zarina Zainal Abidin
Head, Sales-Malaysia, Global Markets
zarina.za@maybank.com
(+60) 03- 2786 9188

Singapore
Janice Loh Ai Lin
Head of Sales, Singapore
jloh@maybank.com.sg
(+65) 6536 1336

Indonesia
Endang Yulianti Rahayu
Head of Sales, Indonesia
EYRahayu@maybank.co.id
(+62) 21 29936318 or
(+62) 2922 8888 ext 29611

Shanghai
Joyce Ha
Treasury Sales Manager
Joyce.ha@maybank.com
(+86) 21 28932588

Hong Kong
Joanne Lam Sum Sum
Head of Corporate Sales Hong Kong
Joanne.lam@maybank.com
(852) 3518 8790

Philippines
Angela R. Ofrecio
Head, Global Markets Sales
Arofrecio@maybank.com
(+632 7739 1739)