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Global

# FX Flash

# SGD NEER Steady Even as Rates Soften

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## Quick Recap of SGD NEER Trajectory

SGD NEER had declined over Feb-Mar before the MAS policy decision on 30 Mar. MAS flattened the policy slope and re-centred the mid-point of the policy band downwards, on concerns that the Singapore economy will contract and core inflation is likely to remain below its historical average in the near and medium term. Since then, we estimate that the SGD NEER has been largely hugging the policy mid-point or trading modestly to the stronger side of band. As we write, SGD NEER is estimated to be around +0.4% above the implied policy mid-point. We note that moves over the past few months were largely aligned with our "guesses" in our previous SGD NEER reports.

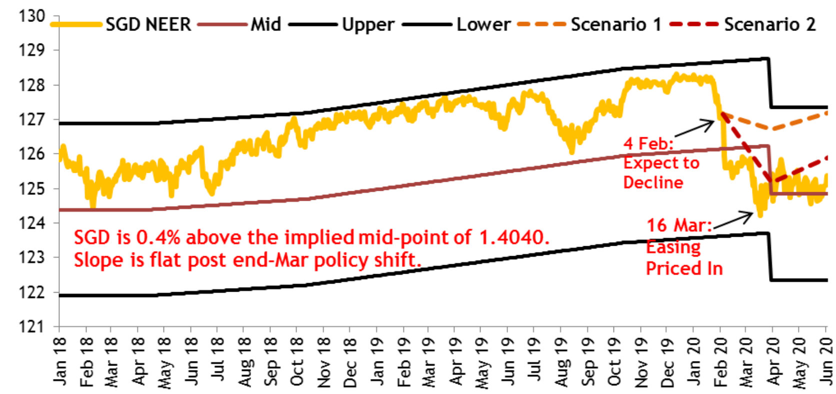
## SGD NEER May Remain on Stronger Side of Band

Broadly, the burden of the recovery has been aptly laid on fiscal, rather than monetary policy. With soft inflation and economic activity slowly on the mend, **it is likely that MAS will maintain accommodative monetary policy by keeping a neutral bias in policy slope in October.**

Meanwhile, even as escalation in US-China tensions remains a discernible risk, recent experience suggests that sentiments in AxJ currencies, including SGD, could be less sensitive (but not immune) to US-China sparring this time round, as both US and China seems reluctant to utilize broad tariff threats given the fragile states of their economies. As long as the global recovery in activity and aggregate demand continues apace, **we expect SGD NEER to remain on the stronger side of the policy band in the interim**. Our USDSGD forecast range for end-2020 to early 2021 is around 1.36-1.38.

Alongside our expectations of (i) a continued flat policy slope and (ii) benign performance for SGD NEER, the 3M USDSGD FX Swap—which also represents the differential between 3M SG-US rates—is unlikely to see upward pressures in the short run, i.e., **no discernible SG rate premiums over US rates**. Given consensus expectations for lower-for-longer US rates, **SG short-term rates are unlikely to move significantly upwards in the interim as well**. House view of 3M SIBOR for end-2020 and end-2021 is at 0.4%.

**SGD NEER Moves Largely Aligned With Our Recent Views**




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

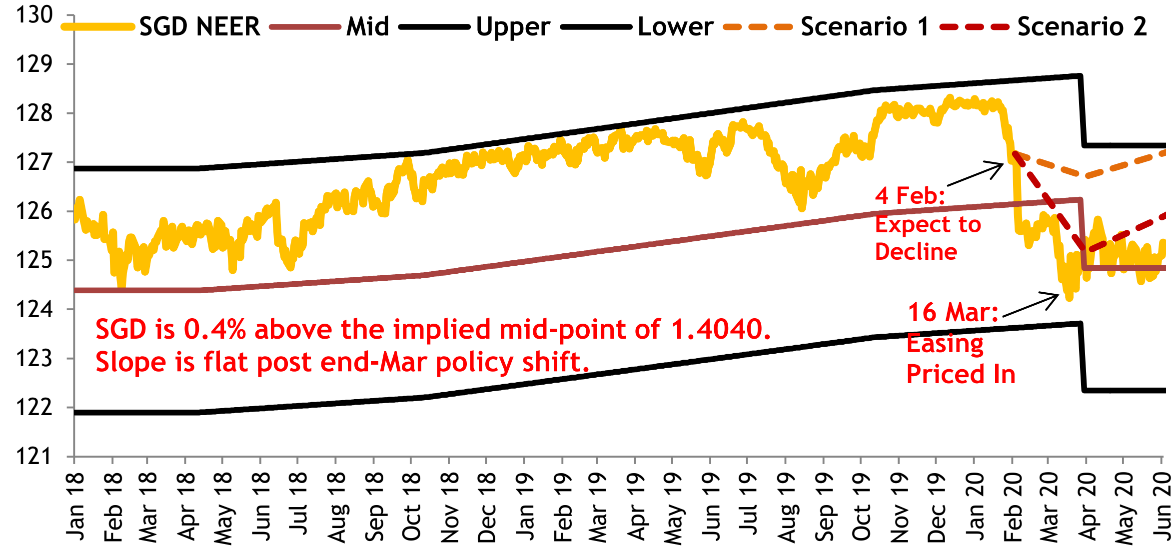
### SGD NEER Stable After Tanking in Feb-Mar (As Cautioned)

4 months ago on 4th Feb, just as Covid impact was starting to be felt in the region, we had discussed two possible scenarios in a piece titled *SGD NEER - More Room to Fall?*

**Scenario 1 (mild) was for Covid damage to be contained largely within 1Q**, and where GDP growth forecast for Singapore could potentially be maintained above 1% in 2020. On the other hand, **Scenario 2 (serious) was for a larger and more protracted Covid impact roiling global economies and financial markets**, and where Singapore's GDP was expected to contract for the year.

Developments since then have been rather in line with Scenario 2, and arguably the trough in economic activity has been even deeper than our initial expectations of a downside scenario. Our economist team expects a 20% contraction in 2Q GDP, led by a plunge in services. **Actual SGD NEER (yellow line) had tanked earlier as we expected**, with the extent of decline not too far from our earlier projection (red dotted line) for a dire scenario.

**Chart From 4 Feb Updated with Actual SGD NEER Developments**

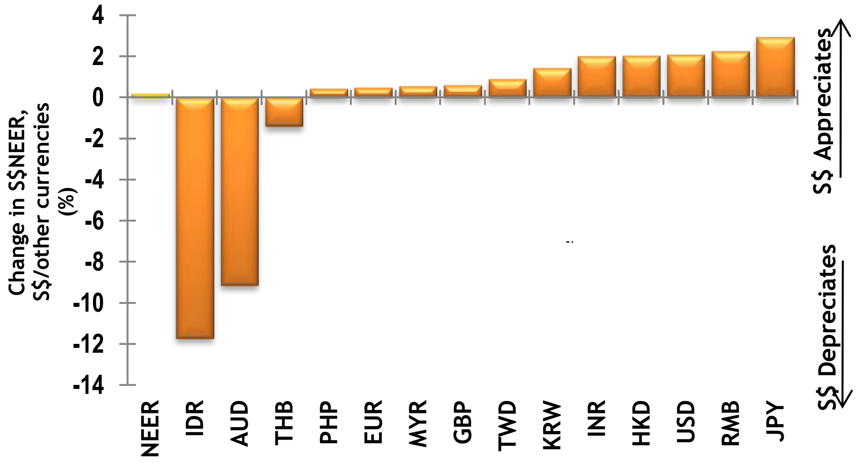



*Source: Bloomberg, Maybank FX Research & Strategy Estimates*

Subsequently on 16 Mar (*SGD NEER - MAS Easing Partly Priced In*), we had argued that MAS could potentially have an inter-policy meeting before mid-Apr (this was later confirmed to be on 30 Mar) to mitigate the Covid hit on market sentiments, and that **easing expectations were usually priced in prior to actual policy announcements**, **leaving less room for SGD NEER to fall further**. This largely came to pass as well.

On 30 Mar, MAS officially flattened the policy slope and re-centred the mid-point downwards (to prevailing level). Since then the SGD NEER has been largely hugging the policy mid-point or trading modestly to the stronger side of band. As we write, SGD NEER is estimated to be around +0.4% above the implied policy mid-point.

<u>Since End-Mar, NEER Stable Despite Recovery Rally in IDR and AUD</u>




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

Despite a huge recovery rally in IDR and AUD over the past two months, SGD NEER has been relatively stable, partly because IDR and AUD only hold modest weights in the NEER basket. SGD had also outperformed most other FX, including USD, RMB, JPY over the past 2 months.

**MAS Oct Policy, SGD NEER & FX Swaps**

Going forward, price pressures in Singapore are expected to remain soft alongside lower energy costs and likely weaker wage outcomes. But 2Q could be the trough of the current crisis with the economy entering a 3-Phase reopening from early June. Pharma is also turning out to be a bright spot in exports. Broadly, the burden of the recovery has been aptly laid on fiscal, rather than monetary policy. **On net, it is likely that MAS will maintain accommodative monetary policy by keeping a neutral bias in policy slope in October.**

Meanwhile, SGD NEER has been trading on the stronger side of the policy band, albeit modestly (i.e., 0% to +0.5% above implied policy mid-point mostly). Even as escalation in US-China tensions remains a discernible risk factor, recent experience suggests that sentiments in AxJ currencies, including SGD, could be less sensitive (but not immune) to US-China sparring this time round. Up till this point, US' words have been louder than its actions, with the occasional mention of corporate/entity sanctions. Broad-based tariff, which was the key threat in 2018-19, have been largely avoided for now, and the all-important Phase 1 deal is still somewhat intact. Under such circumstances, recovery of SGD (especially vs. USD) could be intermittently disrupted but is unlikely to be derailed.

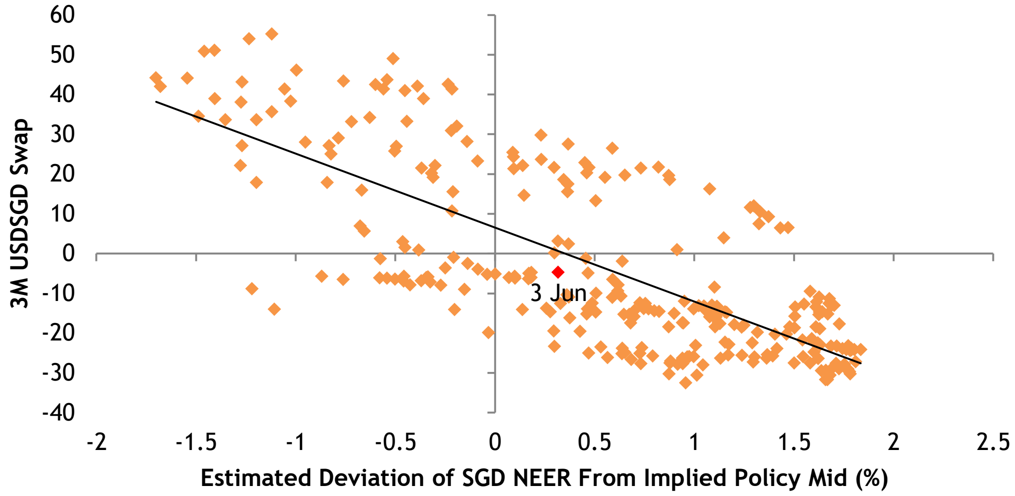
The multiple rounds of recent Covid-fighting fiscal stimulus (amounting to S$93bn, 20% of GDP) have also reminded markets of Singapore's deep fiscal buffers, which is a huge positive when other major economies and regional peers are aggressively adding on to debt and will arguably have a tougher time managing fiscal dynamics over the next several years.

**We hence expect SGD NEER to remain on the stronger side of the policy band in the interim**. Our USDSGD forecast range for end-2020 to early 2021 is around 1.36-1.38.

Given our expectations of (i) a continued flat policy slope and (ii) benign performance for SGD NEER, the 3M USDSGD FX Swap—which also represents the differential between 3M SG-US rates—is unlikely to see upward pressures in the short run, i.e., **no discernible SG rate premiums over US rates**. (See broad negative relationship between SGD NEER & rate differentials in chart below).

In this case, if US rates remain low—consensus forecasts for Fed policy rate (upper bound) expects it to remain at current 0.25% for end-2020 before ticking up slightly to 0.4% in 2021—**SG short-term rates are unlikely to move upwards in the interim as well**. House view of 3M SIBOR for end-2020 and end-2021 is at 0.4%.

**3M USDSGD FX Swap Unlikely to See Significant Upsides in Interim**




*Source: Bloomberg, Maybank FX Research & Strategy Estimates*
Note: Data is from 2015 till latest, in weekly frequency.

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