

FX Insight

SGD - MAS Can Be Patient

MAS To Pause Policy Normalisation

We expect the MAS to maintain its current “slight appreciation bias” for the SGD NEER at its 12 Apr meeting. Our call is premised on moderate growth in the latter half of 2019 amid concerns over the outlook of the global environment. At the same time, core inflation (headline inflation less private transport & accommodation) shows no signs of accelerating in 2019 unless oil prices climbs more aggressively. The SGD NEER is currently around 1.20% above the mid-point of its policy band, highlighting the SGD is on the stronger side vs. its other trading partners’ currencies. However, there is room for the SGD to depreciate within the current policy parameters in the next 6-months or so with the SGD NEER expected to slide lower below the mid-point by 3Q-2019.

Market Conditions Suggest Little Need For Any MAS Moves

Our Taylor Rule estimates highlight that the SGD NEER remains on the upward trajectory and should remain within the policy band in the forecast horizon. In addition, the policy band still allows for some fluctuation in the SGD NEER. The appropriate policy response from the MAS under these conditions is to hit the pause button on its policy normalisation and maintain the current “modest and gradual appreciation” policy stance. The breakdown of the change in currency movements in the SGD basket in the six months ahead showed that the SGD could weaken against a majority of its major trading partners’ currencies, including the IDR and JPY, based on our house projections. Thus, from a markets perspective, further moves to normalise policy further by steepening the policy band would be unnecessary as this could lead to an undershoot resulting in a sub-optimal outcome in the economy on balance.

Maintain Our USDSGD Outlook & Trajectory

We have kept our USDSGD outlook and trajectory unchanged in the forecast horizon. The USDSGD should end 2Q and 3Q around 1.34- and 1.33-levels underpinned by trade optimism and fading USD strength. Thereafter, concerns over a potential slowdown in global growth could see USD strength re-emerge somewhat and lift the USDSGD higher to 1.35- and 1.36-levels by year-end and into 1Q of 2020.

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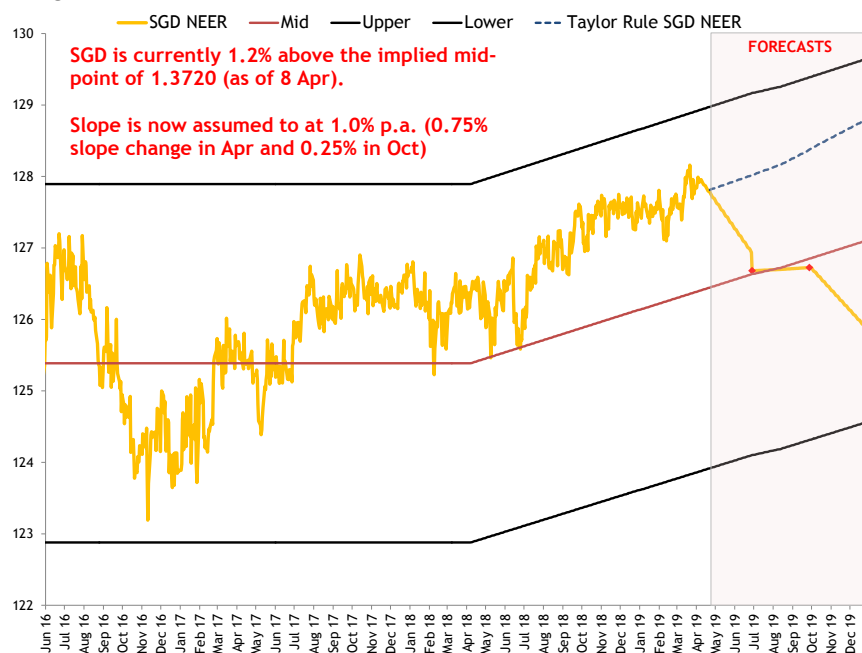
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Policy Normalisation On Hold For Now

We expect the MAS to maintain its current “slight appreciation bias” for the SGD NEER at its 12 Apr meeting. Our call is premised on moderate growth in the latter half of 2019 amid concerns over the outlook of the global environment. At the same time, core inflation (headline inflation less private transport & accommodation) shows no signs of accelerating in 2019 unless oil prices climbs more aggressively.

Recall that the MAS had moved twice in Apr and Oct 2018 to steepen the slope of the policy band of the SGD NEER by about 1% (Maybank estimates) from zero percent prior to 2018 to accommodate expected stronger inflationary pressures then. The SGD NEER is currently around 1.20% above the mid-point of its policy band, highlighting the SGD is on the stronger side vs. its other trading partners’ currencies (Chart 1). However, there is room for the SGD to depreciate within the current policy parameters in the next 6-months or so with the SGD NEER expected to slide lower below the mid-point by 3Q-2019.

Chart 1: Our Taylor Rule Estimates* For The SGD NEER Point To Stronger SGD



Note that the yellow line is Maybank estimates of the SGD NEER, while the blue dotted line is our Taylor Rule-SGD NEER estimates.

*Estimated using GMM Model using an augmented Taylor Rule Framework

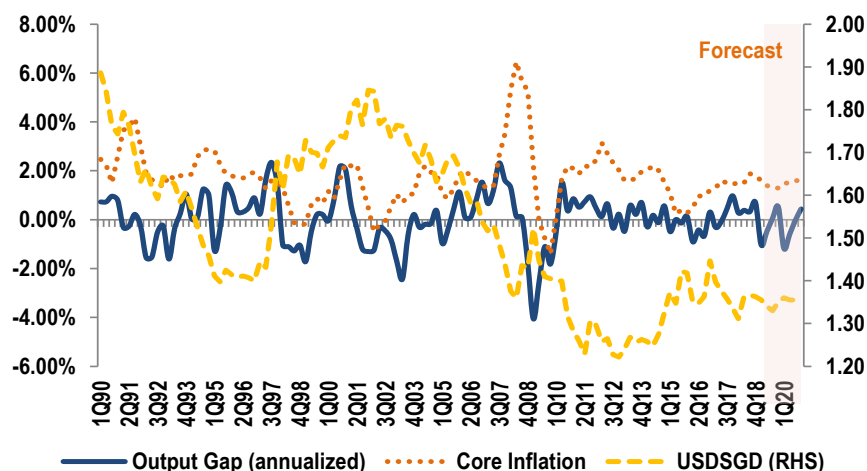
Source: Bloomberg, Maybank FX Research & Strategy

Our economic team is not expecting any significant shifts in the current goldilocks environment. Domestic economic growth is not expected to outperform and core inflation should ease. The team is looking for economic growth of just +1.8% in 2019 before bouncing mildly higher to +2.1% in 2020, well below the +3.2% in 2018. Core inflation should be contained, averaging +1.4% in 2019 (vs. +1.7% in 2018) amid softer electricity prices.

We expect the negative output gap in 1H 2019 to dissipate going into 2H 2019 as the economy picks on expectations that a Sino-US trade deal will be signed that should spur an exports and investment recovery (Chart 2). A similar pattern should emerge in 2020 where a negative output gap

expected in the first three quarters of 2020 gives way to a mild positive gap by 4Q as the recovery in the electronics cycle takes hold. These should help to mitigate any upside pressure on prices.

Chart 2: Mildly Positive Output Gap Unlikely To Spur Significant Inflationary Pressures



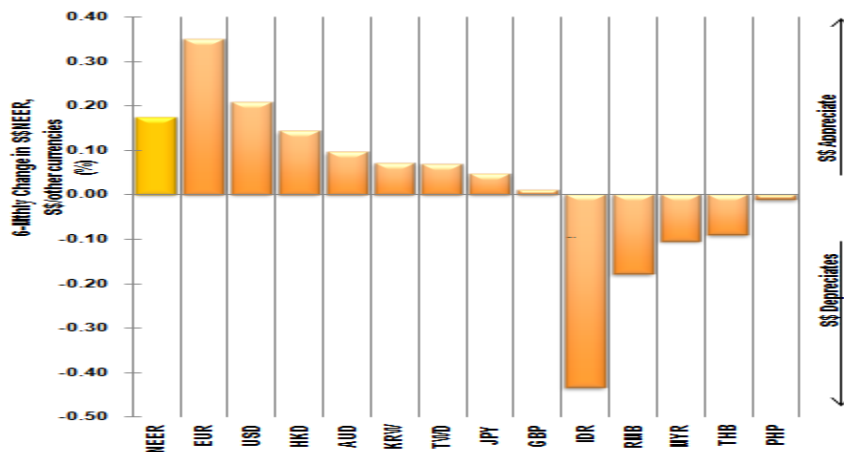
Source: Bloomberg, CEIC, Maybank FX Research & Strategy

Our SGD NEER estimates using the Taylor Rule (growth and inflation trade-offs) suggest that the SGD NEER should strengthen ahead. The SGD NEER ended 1Q 2019 around 127.61, and the Taylor Rule-SGD NEER is estimated to climb higher to 127.71 (2Q 2019), 128.00 (3Q 2019) before ending 2019 around 128.41. For 2020, the Taylor Rule estimates for the SGD NEER is 129.00 (1Q 2020), 129.05 (2Q 2020), 129.30 (3Q 2020) and then to 129.71 by end-2020. The implied USDSGD forecasts corresponding to the 2019 estimates are 1.3559 (2Q 2019), 1.3530 (3Q 2019) and 1.3485 (4Q 2019). The corresponding implied USDSGD forecasts for 2020 are 1.3425 (1Q 2020), 1.3419 (2Q 2020), 1.3395 (3Q 2020) and 1.3552 (4Q 2020).

Our Taylor Rule estimates for the SGD NEER highlight that the SGD NEER remains on the upward trajectory and should remain within the policy band in the forecast horizon (Chart 1). This suggests that the MAS can afford to be patient and maintain the status quo of “a slight appreciation bias” until its next meeting in Oct 2019. In addition, the policy band still allows for some fluctuation in the SGD NEER. Thus, the appropriate policy response from the MAS under these conditions is to hit the pause button on its policy normalisation and maintain the current “modest and gradual appreciation” policy stance.

Our examination of the breakdown of the change in currency movements in the SGD basket in the past six months showed that the SGD has appreciated against the EUR, USD, HKD, AUD, TWD, JPY and GBP (Chart 3). Weighing on the SGD NEER was the appreciation of the IDR, RMB, MYR, THB and PHP against the SGD. This suggests that there is some room for the SGD to appreciate further in the near-term.

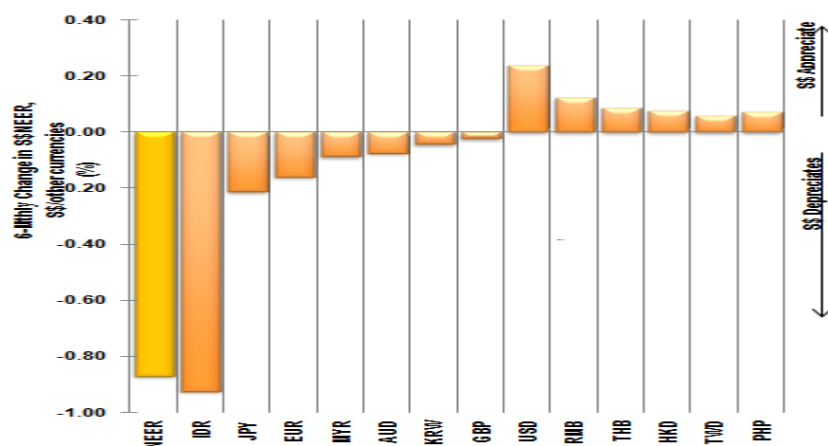
Chart 3: Relative Weakness In The EUR, USD, HKD, AUD, TWD, JPY & GBP Supports The SGD NEER Higher The Past Six-Months



Source: Bloomberg, CEIC, Maybank FX Research & Strategy

In the six-months ahead though, we could see the SGD weakened against a majority of its major trading partners' currencies (Chart 4). Based on our house projections, the SGD should depreciate against the IDR, JPY, EUR, MYR, AUD, KRW and GBP. On the flip-side, the SGD should appreciate against the USD, RMB, THB, HKD, TWD and PHP. Thus, from a markets perspective, further moves to normalise policy further by steepening the policy band would be unnecessary as this could lead to an undershoot resulting in a sub-optimal outcome in the economy on balance.

Chart 4: Relative Strength In The IDR, JPY, EUR, MYR, AUD, KRW & GBP To Weigh On The SGD NEER In The Six-Months Ahead



Source: Bloomberg, CEIC, Maybank FX Research & Strategy

Consequently, we have kept our USDSGD outlook and trajectory unchanged in the forecast horizon. The USDSGD should end 2Q and 3Q around 1.34- and 1.33-levels underpinned by trade optimism and fading USD strength. Thereafter, concerns over a potential slowdown in global growth could see USD strength re-emerge somewhat and lift the USDSGD higher to 1.35- and 1.36-levels by year-end and into 1Q of 2020.

Maybank's USDSGD Forecast Changes

Forecast	2Q 2019	3Q 2019	4Q 2019	1Q 2020
USDSGD	1.3400 (--)	1.3300 (--)	1.3500 (--)	1.3600 (--)

No Change To Previous Forecast

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