

FX Insight

SGD - Buoyed By Favorable Risk Environment

Positive External Environment Weighs On The USDSGD

We have revised lower our 2019 USDSGD forecast for several reasons. First, the escalation in Sino-US trade war failed to materialise but instead has dissipated. Second, a soft-landing for China is anticipated following moves by Chinese policymakers to support the economy. These have led to the slippage in the USDCNH 12-month forward, which points to downside pressure on the rise in the USDSGD given that the USDSGD tracks the 12-month forward very closely. Third, rising expectations of a pause in Fed rate hike and slower US growth because of the government shut-down has weighed on the USD, which in turn dragged the USDSGD lower. The question is if this rising expectations of a pause is overdone. Consensus is still around 1-2 rate hikes this year with a high probability that we will have more clarity by mid-2019. The SGD NEER is currently trading around 1.0% above the implied mid-point of 1.3675. This suggests that the SGD NEER is on the stronger side vs. its trading partners, though it is expected to slip lower below the mid-point by end-2019. The SGDMYR is expected to end-2019 around the 3.04-levels due to some expected oil prices softness before stabilising. This is likely to keep the MYR muted and see the SGDMYR pressured higher by year-end.

Domestic Factors Should Also Be Supportive Of The SGD

We no longer expect the MAS to move again on policy this year unless growth comes out more resilient for the next few quarters and inflationary pressures pick up. Instead, given our base view that growth will decant lower, we expect the MAS to maintain its current slightly appreciation bias given that growth is expected to moderate and inflation to remain muted this year and into 2020. In addition, anecdotal evidence suggests some leaning against the wind activity to slow the USDSGD decline lately. Overall, these should keep the USDSGD from slipping aggressively lower in 2019. Meanwhile, healthy domestic economic fundamentals, including healthy fiscal space, triple-A status, and persistently higher balance of payments surpluses, continue to provide support a backstop for the SGD in 2019.

USDSGD Outlook Upgraded; Trajectory Maintained

We have made changes to our USDSGD outlook for 2019 but maintain the currency's trajectory. We now expect the USDSGD to come in around the 1.36-levels by end-1Q. In a plausible environment of eventual recovery in optimism that a trade deal between China and US is within reach and fading USD strength, we look for the pair to slide lower to 1.34 and 1.33 in 2Q and 3Q respectively. Thereafter, concerns over a possible global economic slowdown in 2020-2021 could see USD strength re-emerge somewhat and lift the pair higher to 1.35-levels at end the year.

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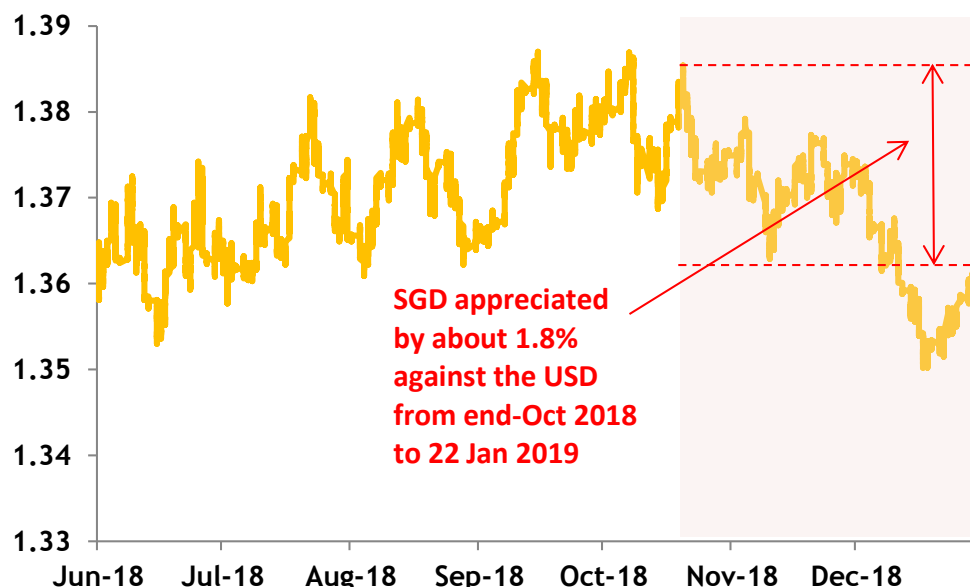
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SGD Outperforms Expectations

The SGD had a good run towards the end of 2018. Upside pressure on the SGD against the USD was triggered by the Fed's dovish tone on further fund rate increases and rising optimism over Sino-US trade talks. The USDSGD, which had been hovering around the 1.3870-levels at end-Oct 2018, bounced lower past the 1.35-handle before settling around the 1.36-levels currently (Chart 1).

Chart 1: SGD Strengthened Towards The End Of 2018

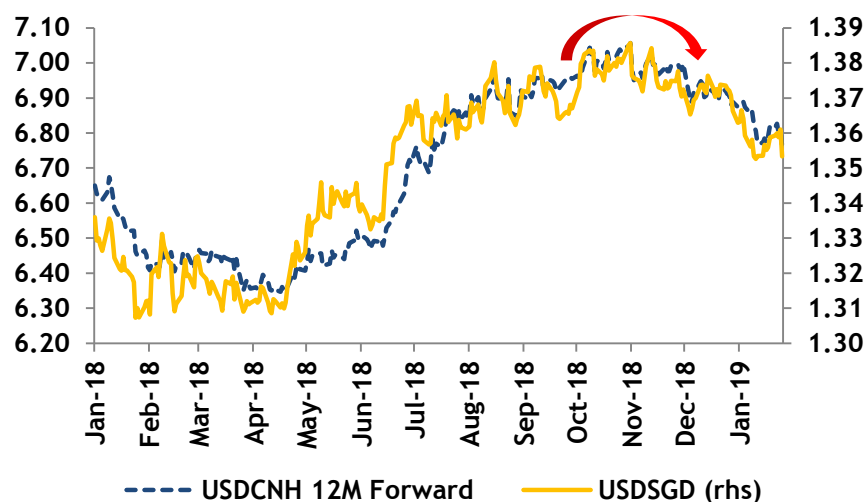


Source: Bloomberg, Maybank FX Research & Strategy

The USDSGD failure to drift higher towards the end of 2019 can be attributed to several factors. First, the concerns that the Sino-US trade war could escalate failed to materialise. The world was brought back from the brink of an all-out trade war between the two world-largest economies when the two sides agreed to trade talks and delay any punitive trade actions till 1 Mar 2019. At the same time, China's policymakers' support of SME via RRR and corporate tax cuts, boosting the fiscal deficit for 2019, and more targeted monetary tools, has lifted optimism that it will orchestrate a soft-landing.

The optimism generated by dissipating trade war concerns and China's pump-priming has led to the collapse in the USDCNH premium over its 12-month forward. This suggests that the yuan might not be under much depreciation pressure as before. The resulting optimism should bolstered risk appetite and hence demand for EM Asia risk assets and concomitantly, EM Asia currencies. The slippage in the USDCNH 12-month forward, suggests risks to the USDCNH are to the downside in 12-month ahead. The expected softness in the USDCNH has in turn has dragged the SGD higher and capped the rise in the USDSGD, given that the pair tracks the USDCNH 12-month forward closely (Chart 2).

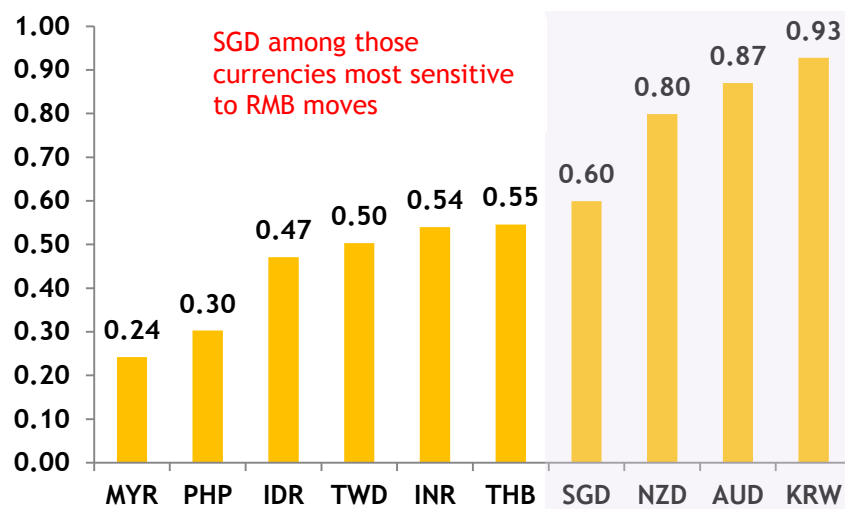
Chart 2: The Fall In USDCNH Forwards Have Weighed On The USDSGD



Source: Bloomberg, Maybank FX Research & Strategy

Just as important, the USDSGD is among the few currencies in the region that are very closely correlated to the USDCNH (Chart 3). Our regression analysis with the SGDUSD as the dependent variable and CNHUSD as the independent variable showed that the SGD is among the most sensitive to moves in the CNH with a sensitivity of 0.60%. Thus, as concerns over China (trade war, hard-landing etc.) moderates, the SGD should be among the currencies to benefit.

Chart 3: The SGD Should Benefit From Re-Emerging CNH Strength



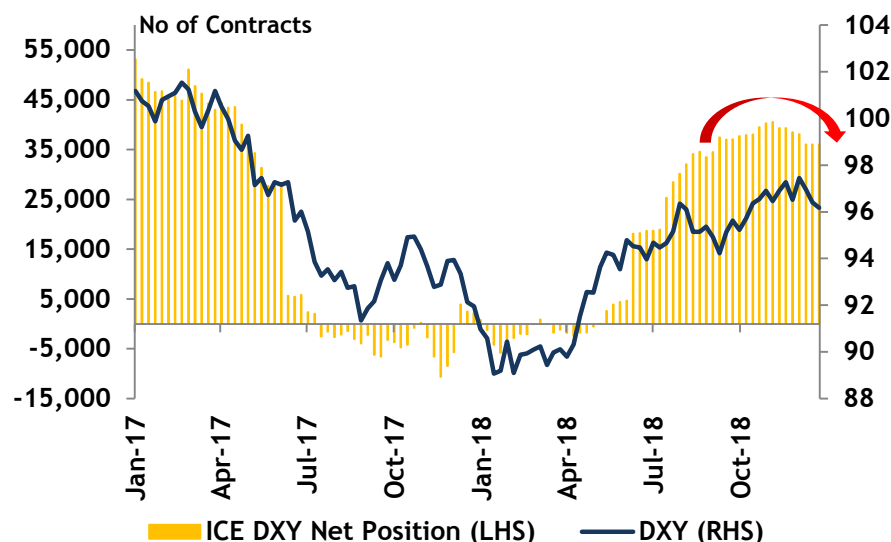
Note: Regression analysis - % change in respective currencies (dependent variables) to CNH as independent variable based on daily change data (17 Jan 2017 - 17 Jan 2019).

Source: Bloomberg, Maybank FX Research & Strategy

Next, the absence of a strong acceleration in USD strength as we had anticipated also weighed on the USDSGD. Aside from rising optimism over Sino-US trade talks that had led to more risk-taking activities, we also had a shift in tone by the US Fed at the end of 2019. The lowering of the Fed's median dot plot projection to 2 hikes in 2019 from 3 hikes previously, while not a game-changer by itself, did trigger a re-think of further Fed rate hikes. The expectations that the Fed could slow its rate

hikes and possibly even pause in 2019 set-off an unwinding of stale long USD positions against its G10 peers and even the AXJs (Chart 4). This weighed on the USD and provided the AXJs including the SGD a lift.

Chart 4: Unwinding Of Stale Long USD Positions Exerted Downside Pressure On DXY



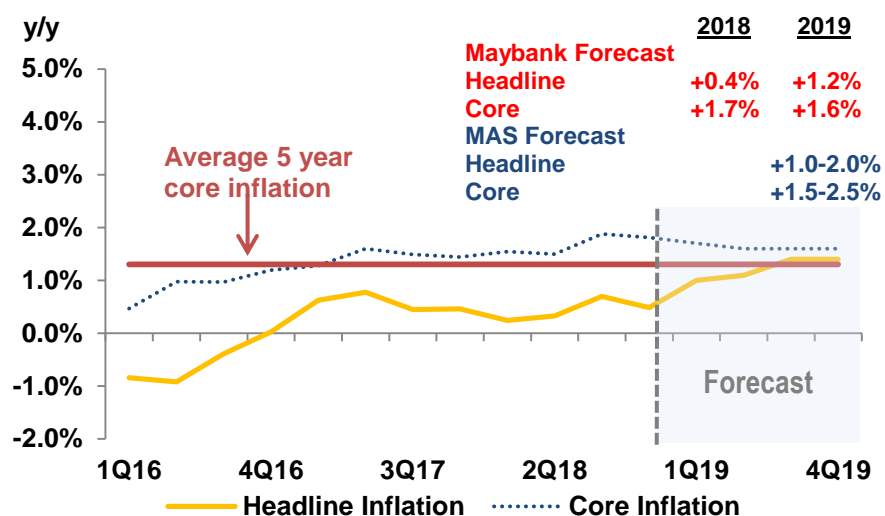
Source: Bloomberg, Maybank FX Research & Strategy

The comments by Fed Chair Powell that the Fed “will be patient” with monetary policy and adjustment of the balance sheet and that of other Fed officials appear to re-affirm that the Fed could slow its rate hike trajectory and possibly even hit the pause as growth in the US moderates. Given the recent shut-down in the US government is likely to drag 1Q 2019 GDP lower, a Fed move in Mar is unlikely. The re-pricing of Fed expectations should put downside pressure on the USD and drag the USDSGD lower.

Beyond 1Q 2019, a combination of factors is likely to support a softer USD in 2Q and 3Q, namely the nearing the end of the Fed’s tightening cycle, the peaking of the US economy, and US twin deficits that could see a surge in borrowing. This should keep the USDSGD on a downward trajectory for 2Q and 3Q. Thereafter, there could be some intensification of global growth concerns in 4Q, triggering global risk off and supporting the USD somewhat. This in turn could lift the USDSGD higher in the quarter.

Still, we do not expect the USDSGD to slip aggressively lower in 2019 back to around the 1.30-levels as a consequence of the more optimistic external environment. This is because we no longer expect the MAS to move again on policy after tightening moves at its Apr and Oct meetings last year. Instead, we expect the MAS to maintain its current slightly appreciation bias given that growth is expected to moderate and inflation to remain muted this year. Our economic team is expecting core inflation to average +1.6% in 2019, moderating from 2018’s +1.7% and economic growth to slow to +2.2% in 2019 vs. +3.2% in 2018.

Chart 5: Moderating Core Inflation Provides Little Impetus For MAS To Tighten Policy Again in 2019

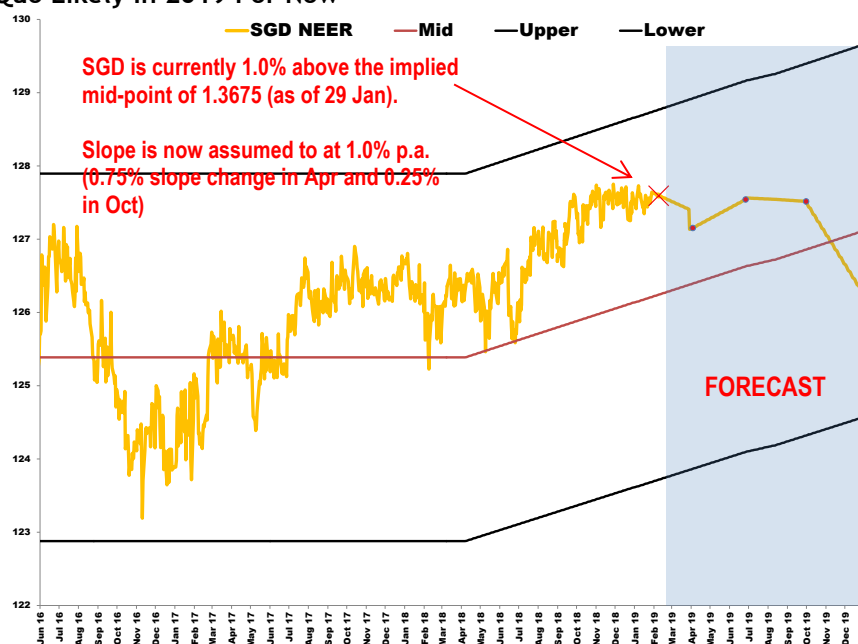


Source: CEIC, Maybank FX Research & Strategy

As we had previously written, still healthy domestic economic fundamentals provide support for the SGD. The healthy budget surpluses of the past few years provide fiscal space for the government to accelerate its infrastructure programme, including development of Changi Airport Terminal 5 and the redevelopment and rejuvenation of the Jurong Lake District if necessary. The upcoming Budget speech on 18 Feb will likely see the government put forward policies to stimulate the economy and mitigate any economic slowdown. Also ensuring that the SGD remains supported is its triple-A status and persistent high balance of payments surpluses. These fundamentals should provide the backstop to the SGD in 2019.

The two moves in Apr and Oct 2018 saw the MAS steepen the slope of the policy band of the SGD NEER to around 1% (Maybank estimates) from zero percent prior to 2018 to accommodate expected stronger inflationary pressures (chart 6). This has allowed the SGD NEER to trade around 1.0% above the implied mid-point of 1.3675 currently. This suggests that the SGD NEER trades on the stronger side vs. its trading partners. However, this could change in the coming quarters with the SGD NEER expected to slide lower below the mid-point by end-2019.

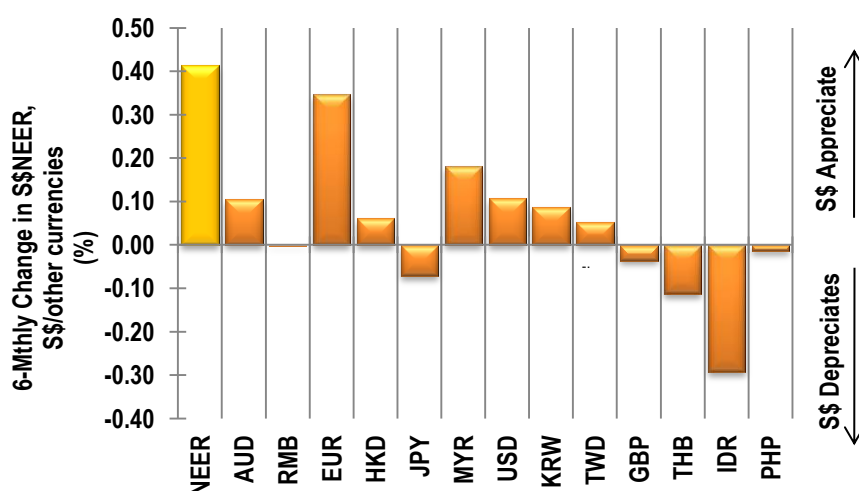
Chart 6: SGD NEER Policy Slope Steepened Twice In 2018, But Status Quo Likely In 2019 For Now



Source: Bloomberg, Maybank FX Research & Strategy

We examined the breakdown of the change in currency movements in our basket on a six-monthly basis (chart 7). It shows that the appreciation impetus for the SGD NEER came largely from the depreciation of the AUD, EUR, HKD, MYR, USD, KRW and TWD against the SGD. Weighing on the SGD NEER though was the appreciation of the RMB, JPY, GBP, THB, IDR and PHP against the SGD.

Chart 7: SGD Appreciation Against Most Currencies In The Basket Kept The SGD NEER Elevated Above The Mid-Point (6-month changes in SGD NEER)



Source: Bloomberg, Maybank FX Research & Strategy

Consequently, we have made changes to our USDSGD outlook for 2019, though we have maintained the currency's trajectory. We now expect the USDSGD to come in around the 1.36-levels by end-1Q. In an environment of trade optimism and fading USD strength, we look for the pair to slide lower to 1.34 and 1.33 in 2Q and 3Q respectively.

Thereafter, concerns over a possible global economic slowdown could see USD strength re-emerge somewhat and lift the pair higher to 1.35-levels to end the year.

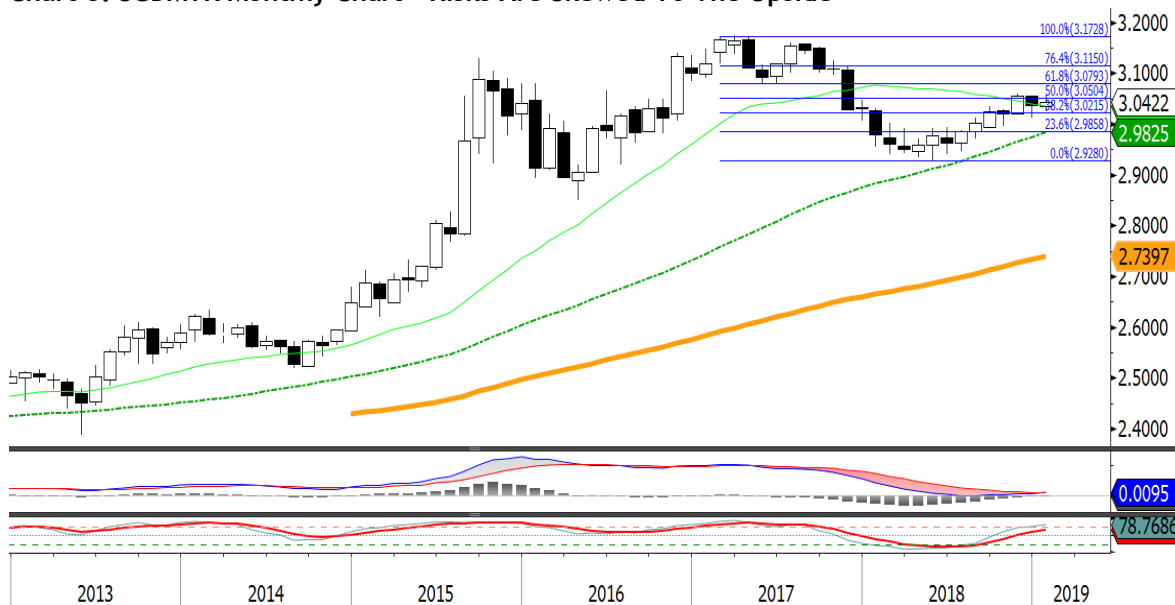
Maybank's USDSGD Forecast Changes

Forecast	1Q 2019	2Q 2019	3Q 2019	4Q 2019
USDSGD	1.3600 (1.4000)	1.3400 (1.3900)	1.3300 (1.3800)	1.3500 (1.3800)

Previous Forecasts in Parenthesis

The SGDMYR cross looks to climb higher in 2019 on the back of the relative outperformance of the SGD. The SGDMYR is expected to end 2019 around 3.04-levels. Aside from relative SGD strength, the MYR is also under-pressure from softer oil prices. Oil prices are likely to remain soft on the back of soggy overall global growth this year, though it should stabilise in 2H 2019 as the supply glut dissipates, and which suggests that the trajectory of the SGDMYR should remain to the upside.

Chart 8: SGDMYR Monthly Chart - Risks Are Skewed To The Upside



Source: Bloomberg, Maybank FX Research & Strategy

Last seen around 3.0392-levels, the SGDMYR cross has lost most of its bearish bias on the monthly chart, and stochastics is fast approaching overbought conditions. This suggests that risks are tilting to the upside in the medium term. Resistance is around 3.08-levels (61.8% fibo retracement of the 2017 high to 2018 low). Support at 2.9860 (23.6% fibo).

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