OCBC TREASURY RESEARCH

FX Viewpoint

14 October 2019

October MAS MPS Post-view

- This morning, the MAS reduced slightly the rate of appreciation of the SGD NEER. There are no changes to the width and centre of the policy band. This is in-line with our house view. **With this move, we estimate the current rate of appreciation to be +0.50% pa, compared to +1.0% pa previously.**

- From a macro perspective, the latest MPS makes for a difficult read. In comparison with the April statement, the October statement was noticeably more dovish in terms of the domestic growth/inflation prognosis.

    - On the **growth** front, pressures on the local manufacturing sector was thought to have “intensified”, and the output gap “has turned slightly negative” (as opposed to positive output gap in April MPS). The impact of Sino-US trade uncertainties also got slightly more air-time in the statement.

    - Meanwhile, domestic **inflationary pressures** are expected to be “muted”, and the labour market conditions are thought to be “softening” (as opposed to firm in April MPS). Previous comments about higher unit labour costs were also absent this time.

- Meanwhile, the global macro narrative continues to be challenging. As seen from the latest data prints, the previously more supported US economy is also converging lower towards the weaker global experience, putting yet another negative to the overall picture. Against this backdrop, the Sino-US trade tensions, although in temporary remission, will continue to feature heavily in the central bankers’ minds. One suspects that had last week’s Sino-US trade talks concluded acrimoniously, the message this morning would have been more ominous.

- At the risk of stating the obvious, the MAS added for good measure that it “is prepared to recalibrate monetary policy should prospects for inflation and growth weaken significantly”. We think this is telling of its intentions. **Further policy easing measures may be on the cards, and we do not rule out a further reduction of slope to zero appreciation in the next meeting.**

USD-SGD and SGD NEER: Domestic imperatives vs. global drivers

- In the near term, the impact of this announcement on the USD-SGD should be limited, as the decision was broadly in line with consensus. We expect the pair to ease lower in response to the positive risk sentiments and a lower USD-CNH for now.

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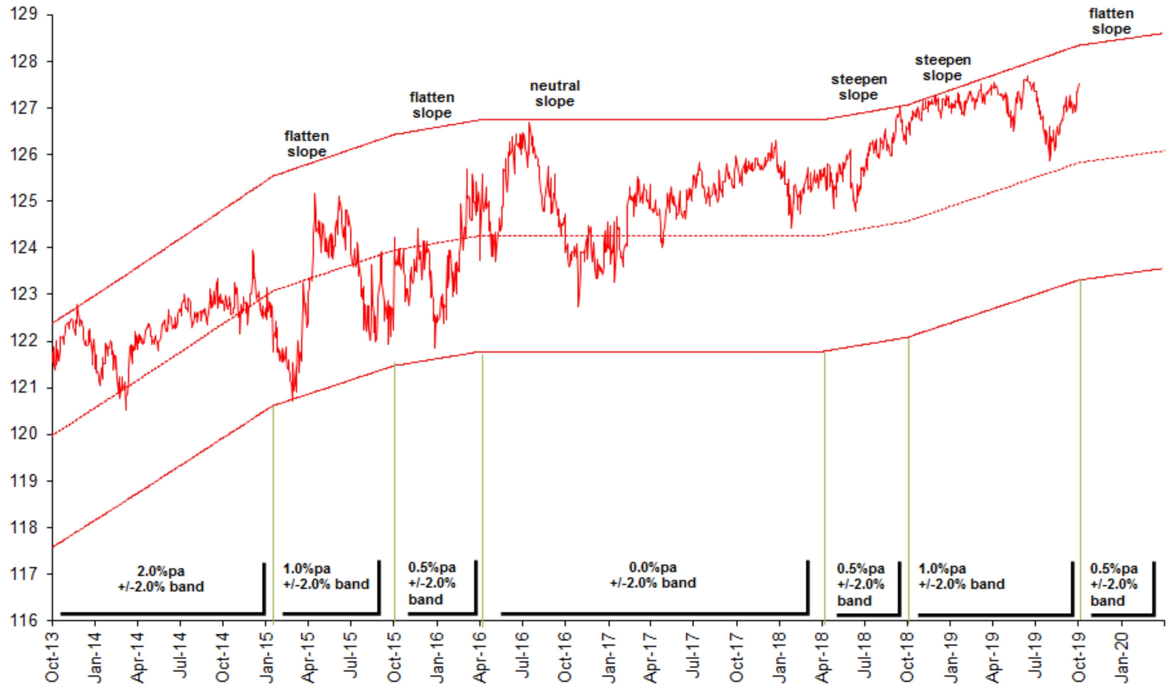
- **Further out, while domestic economic imperatives and policy signals call for a lower SGD NEER basket, we think this may be offset by a global environment that implicitly transmits an upward pressure on the basket.** Since May 2019, the RMB has been underperforming the rest of the Asian currencies (SGD included), although this depreciation was at a measured pace (CFETS RMB Index finding a floor at 91.00). Some unpacking suggests:

    - RMB underperforming against the SGD imparts upside pressure on the SGD NEER given the RMB's considerable weightage in the basket.

    - The measured depreciation for RMB implies that it still provides some sheltering effect on Asian currencies against the likes of the USD. This suggests the floor will not be falling off for the Asian currencies, SGD included. Again, this lends at least some support for the SGD against the USD and other G10 currencies, keeping the SGD NEER supported.

- Therefore, **with global drivers flexing against the domestic imperatives, SGD NEER downside from current levels may be limited. Instead, we expect the basket to stay relatively supported. Similarly, excessive upside expectations on the USD-SGD into the year-end may be disappointed.** At this juncture, we retain our year-end forecast for USD-SGD at 1.3940.



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