Singapore Outlook

OCBC Bank

Singapore added to US watch list for US' FX monitoring report and implications

Wednesday, May 29, 2019

Highlights

- **Market may understandably be a bit jittery,** but the de-risking due to the recent escalation of the US-China trade war had already contributed to USD strengthening against many Asian currencies and heightened market volatility. Hence, the S$NEER had already retreated from the stronger end of its parity band to now trading below +1% of its parity band. While this move may have limited structural impact on the USD-SGD trajectory, nevertheless, there may be some market uncertainties about the potential impact on the Singapore economy and monetary policy stance in the medium term. The tricky part is that MAS's monetary policy framework is centered on the exchange rate and intervention in the FX market is par for the game to manage the SGD within the S$NEER band. However, the critical difference is that MAS monetary policy is targeted at ensuing medium-term price stability given Singapore is a small open economy and a price-taker, rather than trying to boost export competitiveness per se. Singapore's monetary policy framework is unlikely to fundamentally change as a result of this report, but the nuancing may become increasingly important to address the US perception of currency intervention going forward.

- **Being on the watchlist is subjective to a certain extent**. As the US had expanded the coverage from its 12 largest trading partners to those who trade more than US$40 billion with the US, and lowered the bar for the definition of "material" current account surplus from 3% of GDP to 2% of GDP and also the definition of persistence of net FX purchases from 8 out of 12 months to 6 out of 12 months. In addition, the US administration will add and retain on the Monitoring List any major trading partner that accounts for a large and disproportionate share of the overall U.S. trade deficit even if that economy has not met two of the three criteria from the 2015 Act. Hence another 9 countries including Singapore, Ireland, Italy, Malaysia and Vietnam were consequently included in the watchlist.

- **Once added to the monitoring list, it does imply greater scrutiny from the US.** The report also stated that any economy added to the monitoring list will remain there for at least two consecutive reports to ensure any improvement is durable and not due to temporary factors. This means that Singapore, like the other new additions to the list, will probably stay there until the next report due later this year. The worst case scenario if a country is labelled a currency manipulator is

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that the US Commerce Department may consider imposing anti-subsidy duties on products from countries that have undervalued currencies. Obviously, the current ongoing US-China trade and tech tensions appear to have raised the potential stakes (feared and otherwise). At this juncture, the assessed economic impact on the Singapore economy may be limited in the short-term, apart from the immediate financial market gyrations on increased uncertainty.

- **If history is any guide, the US had labelled three countries as currency manipulators in the past**: Japan in 1988, Taiwan in 1988 and again in 1992, and China from 1992 until 1994. According to a report by the Government Accountability Office, all three countries made "substantial reforms to their foreign exchange regimes" after the negotiations, and were removed from the list after their "currencies appreciated and external trade balances declined significantly." This suggests that being added to the monitoring list is not a permanent sentence.

- **What can Singapore do?** The large current account surplus that amounted to 17.9% of GDP in 2018 (criteria 2) is unlikely to be reduced drastically even with a cyclical slowdown amid the global economic headwinds. Our high savings rate is also unlikely to unwind quickly, but the ageing population may mean that consumption will rise over time and the current account surplus may normalise somewhat. In addition, the saving grace is that Singapore runs a steady bilateral goods deficit with the US (criteria 1). For criteria 3, MAS already announced on 8 May that it will start disclosing the net FX purchases on a six-month aggregated basis with a six-month lag from end of 2H19. This would contribute to greater transparency of the actual intervention amounts. If the released data is hypothetically less than 2% of GDP (compared to the US estimates of around 4.6% of GDP), this may help to address the third criteria of persistent, one-sided intervention in FX markets. This probably is the most realistic criteria improvement that can be achieved over the next 6-12 months. If you look back in early 2015, the S$NEER did trade at the weaker side of its parity, so any intervention would have been on the other side, so it may also not be true that the FX intervention is one-sided.

Box 1. New Treasury Thresholds Under the 2015 Act

Criteria	Benchmark	Previous threshold	New threshold
Major Trading Partner Coverage	Total Bilateral Goods Trade (Imports plus Exports)	12 largest trading partners	$40 billion[1]
(1) Significant Bilateral Trade Surplus with the United States	Goods Surplus with the United States	$20 billion	$20 billion
(2) Material Current Account Surplus	Current Account Balance	3% of GDP	2% of GDP
(3) Persistent, One-Sided Intervention in Foreign Exchange Markets	Net FX Purchases	2% of GDP	2% of GDP
	Persistence of Net FX Purchases (months)	8 of 12 months	6 of 12 months

[1] As of 2018, 21 trading partners exceeded this threshold.

Source: US Department of the Treasury

Table 2. Major Foreign Trading Partners Evaluation Criteria

	Bilateral Trade	Current Account			FX Intervention			
	Goods Surplus with United States (USD Bil., Trailing 4Q) (1)	Balance (% of GDP, Trailing 4Q) (2a)	3 Year Change in Balance (% of GDP) (2b)	Balance (USD Bil., Trailing 4Q) (2c)	Net Purchases (% of GDP, Trailing 4Q) (3a)	Net Purchases (USD Bil., Trailing 4Q) (3b)	Net Purchases (USD Bil., Trailing 2Q) (3c)	Net Purchases 6 of 12 Months† (3d)
China	419	0.4	-2.4	49	-0.2	-32	-38	Yes
Mexico	82	-1.8	0.8	-22	0.0	0	0	No
Germany	68	7.4	-1.1	298	..	..	..	..
Japan	68	3.5	0.4	176	0.0	0	0	No
Ireland	47	9.2	4.8	35	..	..	..	..
Vietnam*	40	5.4	3.0	12	1.7	4	-7	No
Italy	32	2.5	1.2	52	..	..	..	..
Malaysia	27	2.1	-0.9	8	-3.1	-11	-8	No
India	21	-2.4	-1.3	-65	-1.7	-47	-25	No
Canada	20	-2.7	0.9	-45	0.0	0	..	No
Thailand	19	7.0	-1.0	35	0.0	0	-1	No
Switzerland	19	10.2	-1.0	72	0.3	2	1	No
Korea	18	4.7	-2.9	76	-0.2	-3	-2	No
France	16	-0.3	0.1	-9	..	..	..	..
Taiwan	16	12.2	-1.7	72	0.4	2	0	Yes
United Kingdom	-5	-3.8	1.1	-109	0.0	0	..	No
Singapore	-6	17.9	0.7	65	4.6	17	6	Yes
Brazil	-8	-0.8	2.2	-15	-2.6	-49	-11	No
Belgium	-14	-1.3	-0.3	-7	..	..	..	..
Netherlands	-25	10.8	4.3	99	..	..	..	..
Hong Kong	-31	4.3	1.0	16	-1.4	-5	-14	No
Memo: Euro Area	152	2.9	0.2	398	0.0	0	0	No

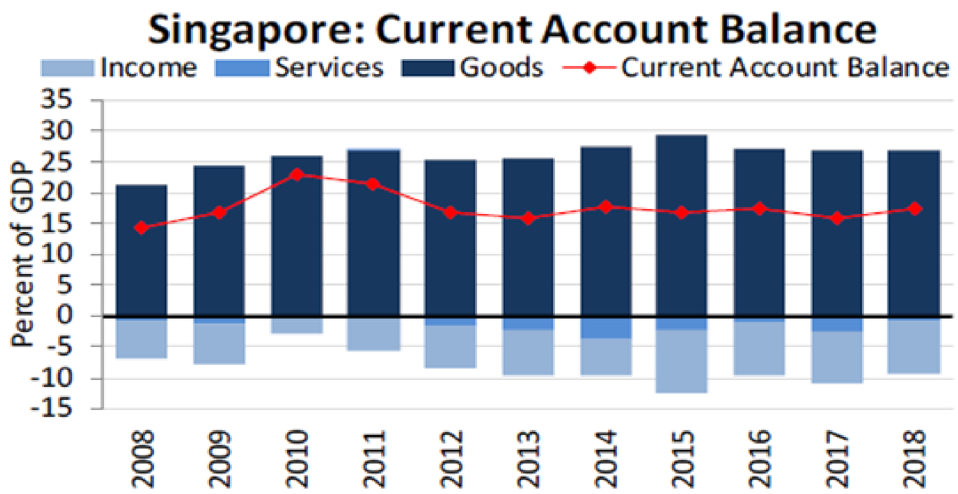
Note: Current account balance measured using BOP data, recorded in U.S. dollars, from national authorities.

Sources: Haver Analytics; National Authorities; U.S. Census Bureau; and U.S. Department of the Treasury Staff Estimates

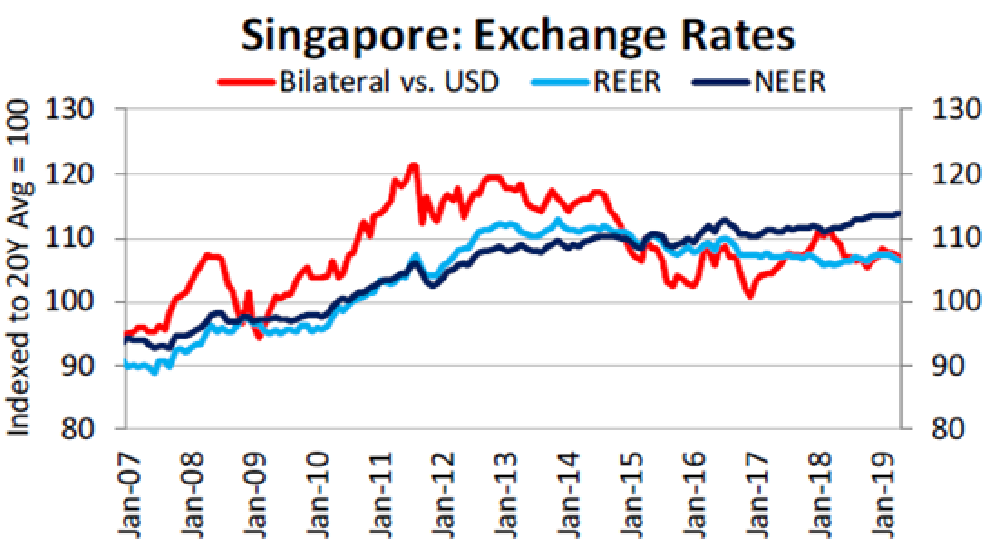
† In assessing the persistence of intervention, Treasury will consider an economy that is judged to have purchased foreign exchange on net for 6 of the 12 months to have met the threshold.

* Current account data for Vietnam are only available through 2018Q2.

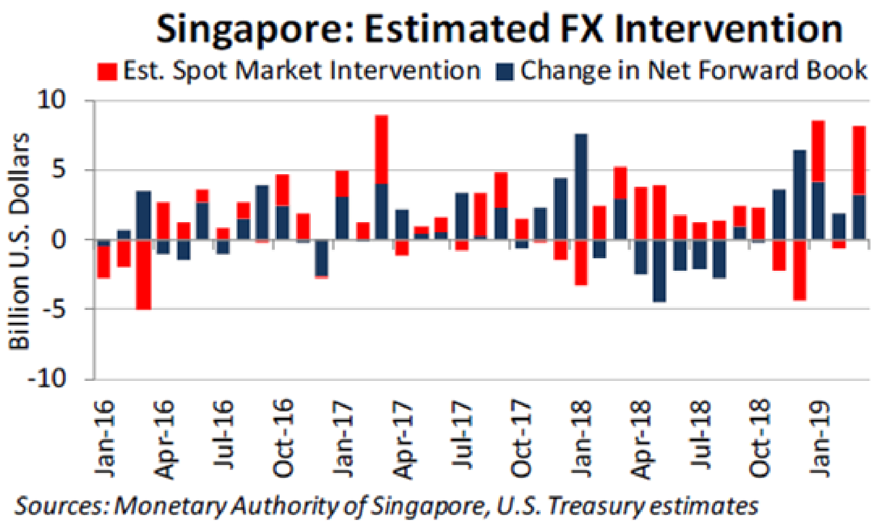
Source: US Department of the Treasury



Sources: Monetary Authority of Singapore, Department of Statistics



Sources: FRB, Bank for International Settlements



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