FX Viewpoint

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SGD NEER and the April 2021 MAS MPS Preview

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- In the October 2020 MAS MPS meeting, the MAS expectedly kept the slope, width and centre of the SGD NEER policy band unchanged in its Monetary Policy Statement (MPS). This kept the SGD NEER on the zero-appreciation path that was first set on the 30 March 2020 MPS. **In the upcoming April 2021 MPS, we expect the MAS to retain the current policy parameters, but the bias may be for the statement rhetoric to sound more positive in terms of the economic recovery.**

- Despite the improved growth outlook, the still-negative output gap leaves us to think that it is premature for the MAS to revert to an upward sloping SGD NEER at the upcoming meeting. While the official policy parameters are unlikely to change, **the improved macro outlook perhaps suggest that there is room for SGD NEER dynamics to shift somewhat. Going forward, we expect the SGD NEER to populate a new range between +0.50% and +1.00% above the perceived parity level.**

Domestic macro outlook: Looking better now

- On the growth front, a low base effect from the 1H 2021 should contribute to strong yoy data prints. However, that should not overly undermine the improved macroeconomic outlook. The latest forecasts by our macroeconomists have FY2021 growth at 6.0%, an upgrade from the 5.0% from earlier in the year. The negative output gap, while contracting, should continue to persist at least for 1H 2021.

- Price pressures seem to be on a consistent uptick since hitting trough in 2Q 2020 (headline inflation) and 3Q 2020 (core inflation). The Feb 2021 core CPI print is the first yoy positive since Jan 2020, and the uptick in headline inflation is also accelerating in 2021. For now, the MAS is expected to keep core inflation forecasts unchanged, but has already signaled for a revised forecast range for headline inflation in the upcoming MPS. We think this revision may form the basis of a less-dovish-than-expected messaging. Yet, without an upward shift in core inflation forecasts, overly-hawkish expectations will need to be tampered.

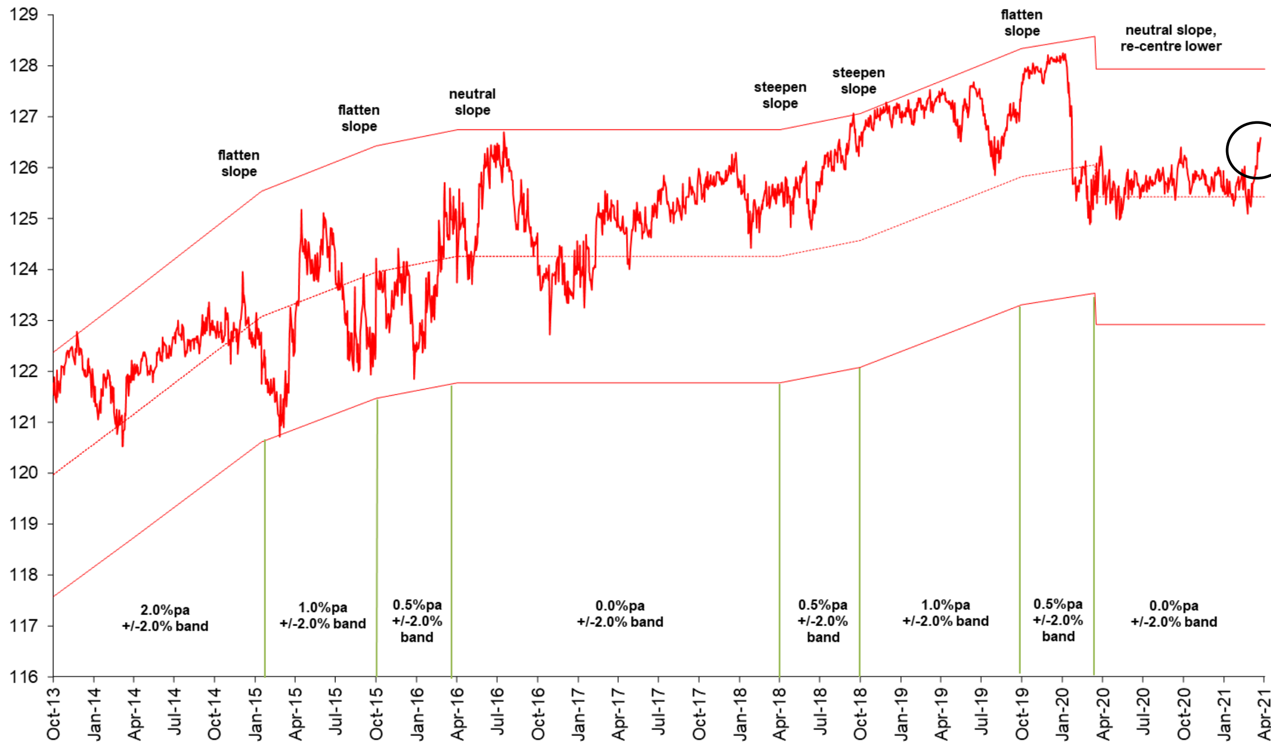
SGD NEER: Trudging into new range?

- In the post-view of the October 2020 MPS meeting (see FX Viewpoint: Oct MAS MPS Post-view, 14 October 2020), we called for the SGD NEER to continue its path just above the estimated parity level (the parity to +0.50% above parity range). The SGD NEER has largely evolved as expected (barring temporary overshoots on either side), until a clear breach occurred on 30 March 2021. Since then, the SGD NEER touched a high at +0.97% above parity on our estimated model. There are no signs of it returning to the previous parity to +0.50% above parity range.

- **The still-negative output gap and core inflation dynamics preclude a tightening move by the MAS in the upcoming meeting.** The time-path of the SGD NEER also does not point in that direction. The October 2021 MPS, is more of a toss-up for now, depending on the progress and effectiveness of the global vaccination effort, and its impact on the growth recovery. **Our current bias is that the return to an upward sloping SGD NEER will only arrive in 2022.**

- However, unchanged policy parameters do not mean that the SGD NEER dynamics will remain static. If anything, the improved fundamentals should see the market comfortable with the SGD NEER on a higher plane. Signs of this may already be seen since 30 March 2021, when the SGD NEER breached the +0.50% above parity top-end of the recent range. This leaves **the question of whether there is scope for the market to bring the SGD NEER to even loftier levels, perhaps closer to the top-end of the official tolerance band? For now, we think that may be stretching the optimism too much** – there is still much uncertainty in the pandemic situation ahead, and there is limited justification for too much tightening to jeopardize the economic recovery.

- **On balance, we expect the SGD NEER to populate a new range between +0.50% and +1.00% above the perceived parity level, in response to the better macro prospects.** This may be a step towards the SGD NEER moving more decisively towards the +1.50% above parity range in late-2021/early-2022 when the macro recovery is more entrenched.



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