

MAS Watch: Sweet Spot

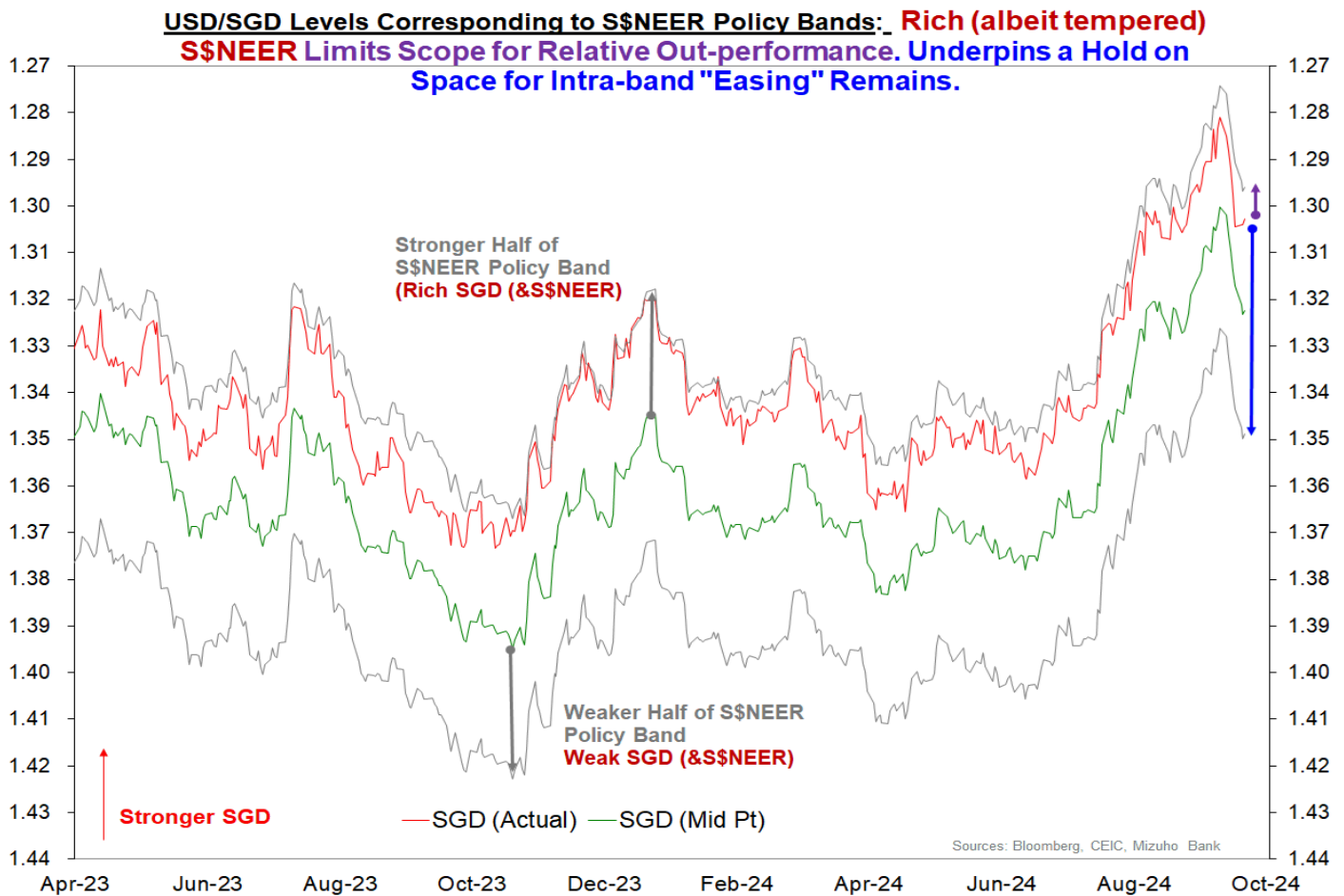
Economics & Strategy | Asia ex-Japan

10 Oct, 2024 | Vishnu Varathan | Head Macro Research, Asia ex-Japan

MAS Watch: Sweet Spot

"People say nothing is impossible. But I do nothing every day." - Winnie the Pooh

In a Nutshell: The **MAS** is set to **stay on hold**, defying the global easing wave, but arguably still **in a policy sweet spot**. This certainly **derives from balanced growth-inflation risks**. Specifically, *disinflation that is insufficient despite being encouraging* and arguably *sticky price pressures* by some measures. On the other, *growth remains resilient even as the dispersion of two-way risks mount*. But not just that. The **unique self-acclimatizing characteristics of the MAS' exchange rate policy**, articulated *via managed appreciation bias and volatility bounds of a trade-weighted SGD (S\$NEER)*, inherently **mitigate the need for over-calibration**. Finally, a **"rich" S\$NEER (at the hawkish extreme of the policy bands)** **simultaneously** constitutes **emphatic restraint** (to anchor inflation expectations) and **scope for defacto easing within the policy bands** to initially "absorb" demand shocks. **SGD impact** from MAS-specific cues is **likely to be limited**, with **USD-, JPY- and/or CNY-induced volatility the far greater risk**.

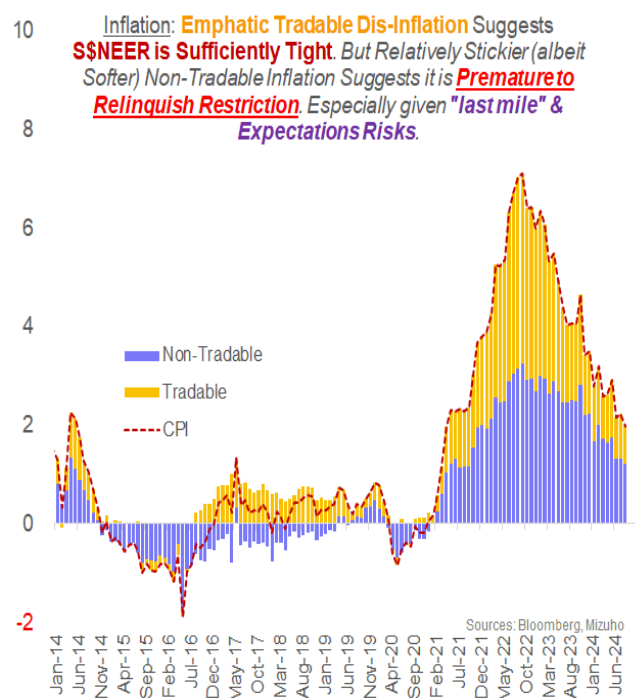
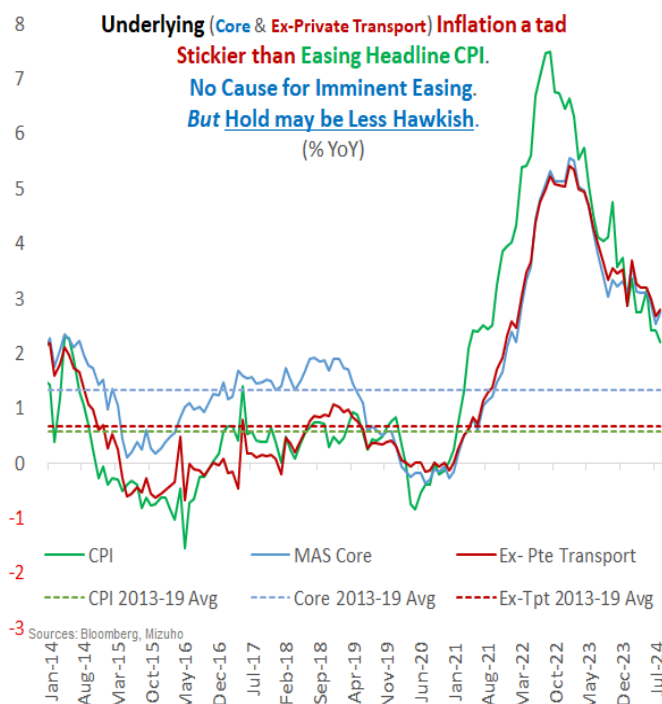


MAS Not Jumping on the Global Easing Bandwagon

- **Despite the wave of global policy easing**, underscored by an aggressive start to the Fed rate cuts in September (with a 50bp cut), **the MAS is not set to ease**. Not just yet.
- In fact, the MAS is *not even likely to concede* a distinct shift *to an unambiguously dovish hold*.
- Instead, the **MAS is likely to convey a neutral hold**, *citing finely balanced risks to the upside* (China stimulus, Fed easing, etc.) *as well as downside* (lagged demand headwinds from policy tightening, brewing trade conflicts and adversarial geo-politics).
- But this isn't necessarily a **precarious policy "tight rope"** imposed by conflicting risks from **two-way uncertainty**. *Instead, it is arguably still a policy sweet spot to simultaneously better anchor inflation expectations and insure against downside risks to the economy.*

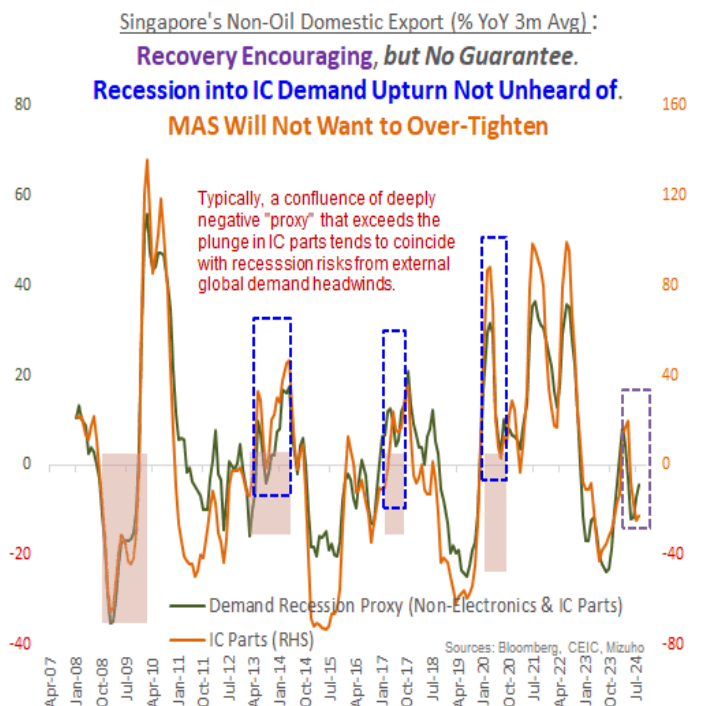
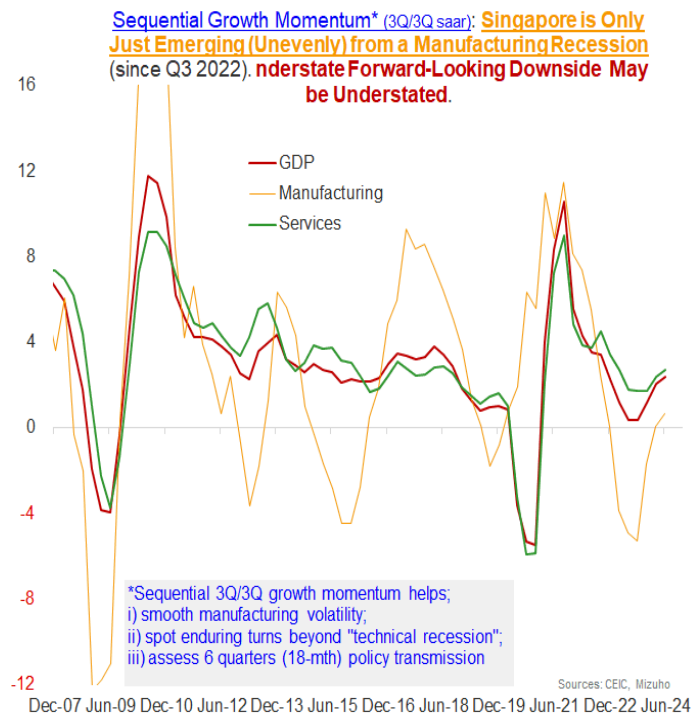
1. Inflation to Concede Neutral Hold, Not Condone Easing

- For a start, while **inflation risks** have **further receded**, it has *not* been **resolutely contained**.
- Admittedly, the **path of sustained disinflation** has been **encouraging**.
- In particular, signs of fairly **broad-based reduction in price pressures**, backed by *meaningfully diminished tradable* (imported) inflation suggest further S\$NEER tightening is not required.
- In fact, the **MAS can afford to drop overtly hawkish bias** in stance.
- **But** inflation risks are not vanquished. First, insofar that the drop in **inflation** is **disproportionately led by COE price base effects**, the *rate of underlying dis-inflation may be overstated*.
- What's more, *non-tradable* inflation, including some *spots of "sticky" services inflation*, may **warrant residual policy restraint** to remain in **both the settings** (S\$NEER slope) and **signals**.
- And **diminished, but perhaps not "dead-and-buried"**, **wage-price spiral risks** (*as wage inflation cools in tandem with CPI, but with both still above longer-term trend rates*), square with **policy posture shift to neutral, albeit with inherited restraint intact**.



2. Growth Risks: (Fatter) Tail(s), Not Head(ed Off)

- With regards to economic growth, **two-way risks constituting fatter tails**, and not risk extremities headed off, is **what the MAS must contend with**.
- By most accounts, **Singapore's growth momentum appears reasonably healthy**, with **encouraging signs of nascent recovery from the underlying manufacturing recession** coming through, *accentuated by positive spillovers from the global demand for semiconductors*.



- And even amidst signs of normalizing from post-pandemic surge, the service sector remains robust.
- **But** with the **uncertainty of US elections** that features, but is not limited to, an *escalation in US-China trade antagonism*, unwelcome **disruption from on-going conflicts** (Middle East and Ukraine) the **lingering threat of demand dent from lagged policy tightening** (not necessarily extinguished with global policy easing) underscore the *litany of downside risks hidden in plain sight*.
- And to be fair, it is **not as if the risks are clearly tilted to one side either**.
- Fact is, a **frenzy of global policy stimulus**, from *emphatic rate cutting cycles by global central bankers* (with the exception of the BoJ) to *China's "big bang" stimulus*, could unwittingly conspire with the "AI-mania" to set off larger-than-expected demand out-run.
- But the permutations are (far too) many, and the potential dispersion of outcomes exceptionally wide.
- Accordingly, **confidence around policy setting** based on demand projections, already a fraught exercise to begin with, *is rendered even more precarious*.
- And so, the **sweet spot** might be to be on an **"active hold"**.
- More so not only does the **unique nature of the (S\$NEER) policy tool** favour a hold, but a **rich S\$NEER underscore the desirability of maintaining prevailing policy balance** (between current restraint and potential for defacto easing as and when required).

3. S\$NEER as a Dynamic Policy Tool Require Fewer (than Rate) Calibration

- To be sure, the MAS’s approach to “**gradual and modest appreciation**” of the trade-weighted SGD (S\$NEER) as a policy tool, guided *within undisclosed volatility bands*, is not directly comparable to rate setting policy. And it certainly does not have one-for-one mapping.
- Point being, this dynamic policy tool has **unique self-acclimatizing characteristics**.
- And so, *managed S\$NEER appreciation bias subject to policy trading bands* inherently **do not require active intervention** that commensurate with rate (hike/cut) policy
- And a MAS hold is far more “active” on two counts. First, the trade-weighted S\$NEER means that exchange rate strength dynamically adjusts for relative FX moves elsewhere.
- Second, **dynamic, market-driven, adjustments** within the (presumed +/-2%) trading bands (**intra-band**) **allow for a more continuous policy calibrations** as inflation and growth conditions evolve.

4. Rich S\$NEER Validates a Dynamic Hold:

- **As an extension the “intra-band” adjustment** alluded to above, a “**rich**” S\$NEER (*at the hawkish extreme of the policy bands*) further **validate the policy hold amid uncertainty** and *rapidly evolving global economic conditions*.
- The upshot is that a **rich S\$NEER simultaneously** constitutes **emphatic restraint** (to anchor inflation expectations) and **disproportionate scope for defacto easing within the policy bands** to initially “absorb” demand shocks **should adverse demand conditions play out**.
- In essence, a rich S\$NEER is more suited as a “dynamic hold” under conditions of lingering inflation that may be juxtaposed against greater uncertainty downside tail risks.

Appropriately Muted SGD Impact

- In our view, proximate MAS impact on *SGD will probably be muted, in the absence of large and unexpected swings from expectations of a predominantly neutral policy stance* (with a tint of remnant rather than intended hawkish bias).
- This is primarily as **relative (rich) S\$NEER levels are consistent with inflation** still above MAS’ desired levels. And crucially, with no compelling case (and certainly no near-term commitment) to either adjust the slope or shift the mid-point* of the S\$NEER policy bands.
- But **lack of SGD response to MAS policy** is *not* the same as the **absence of volatility**.
- Instead, we expect **SGD volatility to remain heightened** as the trade-basket influence renders SGD sensitive to not only **broad-based USD swings** (amid rapidly and constantly evolving Fed expectations) but also **sympathetic sway from pronounced and persistent CNY and JPY volatility**.

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