Mizuho Brief: MAS Watch

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MAS Watch: Suspend (Slope Appreciation)

"Your focus determines your reality." **– Star Wars, Qui-Gon Jinn**

In a Nutshell:

- **Gathering trade war storm clouds** and initial external headwinds suggest that the **MAS calculus ought to turn emphatically more dovish** to guard against adverse demand shocks.
- Admittedly, **both the slope** and shifting the **re-centring tools** (for the S$NEER policy band) feature as options to ease.
- But the **focus** on the prevailing, *exceptionally adversarial global trade threats* ought to **determine** the **reality** of policy trade-offs.
- Accordingly, the **optimal policy choice** is arguably for **flattening of the S$NEER slope** (the strongest viable iteration of slope easing).
- And to the ***conspicuous exclusion of re-centring lower*** ("step depreciation of S$NEER that front-loads easing)., despite this being the more aggressive easing.
- For one, a **suspended slope guards against two-sided, conflicting (price and demand)** shocks rather than being wrong-footed.
- More importantly, **re-centring the S$NEER policy bands lower away from prevailing S$NEER** (at the strong side of the policy band) is **unprecedente**d, **awkward**, and **risks being misperceived as arbitrary devaluation,** *to the detriment of credibility and confidence.*
- Crucially, **abstaining from re-centring lower will mitigate unfounded allegations of mercantilist FX polici**es in the current adversarial global trade environment. And ***averting such geo-political landmines is critical***.
- While ***suspending S$NEER appreciation bias does not automatically dampen the S$NEER***, augmented S$NEER appreciation (and possible future "step depreciation") expectations could *knock 25-50bp off $NEER; especially accompanied by dovish MAS guidance*.

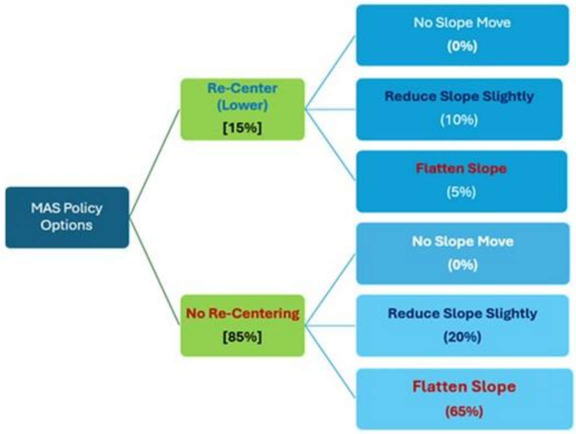
- Distinctly Dovish: Our earlier view of S**$NEER slope easing** being the **optimal policy stands**, *but now takes on a* ***distinctly more dovish form of S$NEER slope flattening***.
- Amid Risks of Amplified Demand Shocks: Point being, the **precarious turn of global events** featuring **amplified second-order China shocks amid heightened uncertainty**, arguably calls for **appreciably** (no pun intended) **more dovish MAS response**.
- Sooner as "Insurance" Insufficient: The case for **imminent and more emphatic easing is compelling** a the **"insurance" easing** (via "slight S$NEER slope reduction) in January increasingly **appears insufficient in the face of unprecedented global turmoil**.

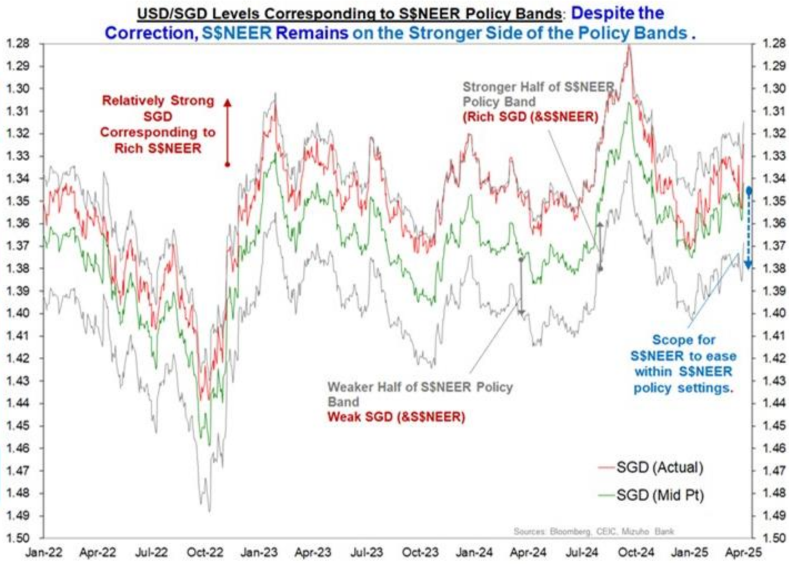
- Slope Suspension Warranted: So, **flattening the S$NEER slope** (*the strongest iteration of slope easing**) is **arguably warranted**.
- Most Optimal: In fact, the **focus** on, *exceptionally adversarial global trade threats* **determine** the **reality** of **suspended S$NEER appreciation bias**, *especially given the rich (elevated) S$NEER,* being the **most optimal move for the MAS***.*
- To the Exclusion of Step (Depreciation): Specifically, **to the exclusion of so-called "step depreciation"** (re-centring the S$NEER policy bands lower) ***despite the benefit of more aggressive, front-loaded easing****.*
- To Avoid Wider Mis-Steps: So as to **risks being a mis-step** (pun not intended) amid *two-way risks, geo-political sensitivities* and *policy confidence;* all of ***which slope suspension avoids****.*
- Accounts for Opposing (Price & Demand) Risks: For one, just **suspending the S$NEER slope best mitigates the policy dilemma** and **most effectively manages heightened risks of opposing, two-way** (price and demand) **shocks** *amid exceptionally heightened uncertainty.*
- Without Sabotaging Credibility/Confidence: Moreover, the **MAS can avert pitfalls of inadvertently sabotaging** (policy) **credibility** or **confidence** (in SGD policy).
- Amid Unprecedented Re-Centring Dynamics: Especially should a **highly unusual, if not unprecedented, "step depreciation" *away* from prevailing S$NEER levels** (which is higher vis-à-vis S$NEER mid-point) **is misconstrued as arbitrary devaluation**.
- Or Inadvertently Inflaming Geo-Political Threats: Above all, the **non-negligible risk** that **a "step depreciation" in an adversarial global trade environment** ***unnecessarily agitates*** *(misguided)* ***accusations of overtly mercantilist FX policy^****.*
- "Step Depreciation" Still a Key Tool: To be sure **as threats of second-order China shocks mount** amid **exceptional global trade uncertainty** there will be **ample scope for a mid-point shift lower** *beyond the slope flattening*.
- But Subject to Deferred & Conditional Application: ***But*** only as a **deferred policy option**, *depending on the pace and path of global trade/geo-political events. October MAS or inter-meeting Q3 on watch for such a move.*
- Slope Flattening Has No Mechanical S$NEER Impact: In theory, a **S$NEER slope suspension is not expected to have a strong influence on the prevailing relative S$NEER levels** (within the policy bands).
- But Expectations May Bias S$NEER Lower Trigger: *Nonetheless,* there could be some **marginal downside pressures on the S$NEER**, all else equal as markets price; i) *impaired appreciation bias*, and; ii) *pipeline "step depreciation".*
- Especially on Dovish Guidance: And so, this could potentially **prompt some degree of front-running in tempering relative S$NEER strength** *given relatively rich levels* (in the upper half of the band). And ***especially with dovish MAS guidance****.*
- Measured 25-50bp S$NEER Downside: All else equal, **slope suspension alongside a dovish statement** *could prompt a 25-50bp slip in S$NEER*.
- Attendant USD/SGD Lift Contingent on Wider USD Moves: Based on today's levels, his is **consistent with USD/SGD lift to above sub-1.33 to mid-1.33** (from current mid-1.32 levels). *Caveat being, broader USD moves will overrule.*

*Theoretically one could argue that a negative slope (i.e. S$NEER depreciation bias) is in fact the more

** Typically entails shifting the $NEER mid-point lower (higher in the case of “step appreciation”), which effectively front-loads aggressive easing (tightening).

^Averting a confrontation is way better than trying to resolve one with a counterpart that has suspended economic reason and logic in favour of geo-political aggression/dominance.





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