Mizuho Brief: MAS

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MIZUHO

MAS Watch: Calibrated & Coupled

"Always two there are." – **Master Yoda**

In a Nutshell: Admittedly, the **mainstream MAS bets for October** move may favour either a **policy hold** – *given two successive slope increments have arguably removed accommodation appreciably* – **or** to **"very slightly" increase the slope** to build on July's cautiously calibrated tightening. **But** we beg to differ. Point being, a **calibrated coupling** of both slope increment (*"very slightly"*) *and* mid-point shift (*"higher but below prevailing S$NEER"*). So as to **better effectively target** and *insidious conspiracy of upfront price shocks* alongside *longer-term inflation uncertainty*. **Appropriately apportioning tightening** for the **asymmetries and uncertainties** associated with *acute distributional challenges* (exacerbated by both Middle East crisis and A.I.) and *time-varying nature of inflation risks.* Thereby, **insulating** against (imminent price shocks) and **insuring** against longer-term inflation uncertainties. If executed, this combination may inspire a 50-80bp lift to S$NEER and SGD to reflect partial "step appreciation towards prevailing S$NEER, which is 100-150bp above the S$NEER policy mid-point).

- A Dampened Double: Our out-of-consensus view is for the **MAS to do a calibrated coupling** of both slope increment (*"very slightly"*) *and* mid-point shift (*"higher but below prevailing S$NEER*"), whereby the "**double-barelled" move** is **adequately dampened**, and crucially, ***appropriately directed*** – such that policy finesses, and not force alone, is the objective.

- Accommodation Removed Appreciably: Admittedly, under normal circumstances, there may be **justifiable cause to suggest** that the MAS may be in **a comfortable** position to keep policy on **hold *after the two/three slope increments***, which have arguably removed accommodation appreciably (pun intended).

- Extraordinary Times: But the **circumstances confronting the MAS** are **anything but "normal"**. In fact, this **extraordinary juxtaposition of "war-flation"** - which is simultaneously an inflationary price shock as well as threat of demand destruction - **and "A.I.-nflation"*** warn of ***exceptionally adverse distributional*** and ***time-varying challenges for policy*** to confront.

- Distributional: Point being, both "A.I.-nflation" and "war-flation" *impose disproportionately adverse impact on lower-income households* as **upfront price shocks** - cascading through energy, food and consumer goods - **largely unfiltered** (given the amplitude of shocks), and woefully ***unmitigated by wage gains*** or ***asset market rallies*** (especially, vis-a-vis more affluent households). Inevitably, **threatening to** acutely exacerbate inequality.

- Time-varying & Uncertain: Moreover, the **risks shift starkly with the passage of time**. To be sure, unprecedented **supply disruptions from the Middle East crisis** and **insatiable A.I. capex demand**, ***while wildly different in the "usual" supply vs. demand nature***, are ***nevertheless* both initially present as acute upfront price shocks**. Whereas, *with the passage of time*, both **could invariably flip to become (demand) deflationary forces****, which may be ***starkly at odds with prevailing risks of inflation expectations being***

lifted**.** The wider point being, **current policy calculus is vulnerable inadequately accounting for heightened uncertainty further out**.

- Appropriately Apportioning Tightening: In which case, the **policy response ought to** be structured so as to **apportion tightening appropriately** across upfront impact to effectively tame outsized price shocks such that it would allow for more longer-term inflation expectations anchoring (via S$NEER slope increment) to be sufficiently measured.

- To Insure Against Acute Uncertainty: Which is particularly **important policy fine-tuning to insure against acute two-way risks** around inflation further out.

- Measured Appreciation Bias: If we are right about the "calibrated coupling" – the **controlled mid-point shift higher** (**step appreciation**) being enable by s "rich S$NEER" now ~100-150bp above the presumed +/-2% policy bands – the shift up in the S$NEER mid-point to "higher but below the prevailing" (the precise quantum, which is undisclosed) ought to trigger a reflexive 50-80bp lift in the S$NEER (and SGD all else being equal).

- Similar to (Our) Preferred Alternative: **Admittedly**, we may be wrong, and the **MAS may not go for a "double"**. But ***even then,*** we prefer the **calibrated "step appreciation"** that partially catches up to the prevailing S$NEER as **the preferred *and more effective* tool to address upfront price shocks** that dominate. Hence more **effectively nipping price shocks and inflation expectations in the bud**. And this too will likely give rise to S$NEER/SGD pick-up as described above.

* A.I.-nflation is broader version of "chip-flation"(higher prices of semiconductors/chips driving up wider consumer good prices) expressing demand-driven inflation from AI-related capex build-out, which, for all its element of demand-pull risks nevertheless also have a dimension of demand borrowed from the future (hence, susceptible to a subsequent softening).
**"War-flation" due to its value destruction and discretionary income suppression. And "AI-nflation" due to overhang from over-investment/mis-allocation - possibly even financial shocks from Schumpeterian destruction.

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