FX Monthly Report- Singapore Dollar

July 2024

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FX Monthly Report

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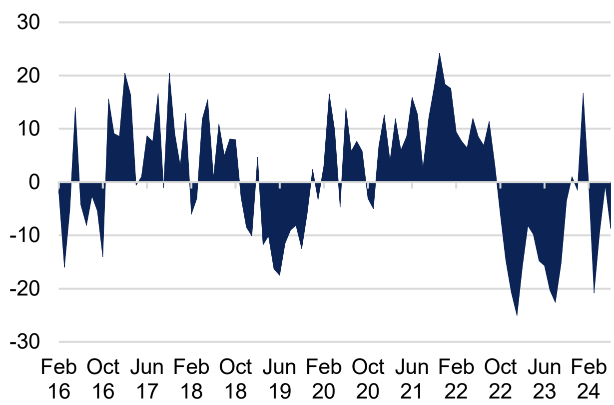
Singapore Dollar Focus

Singapore Economy

Singapore has a small and trade-reliant economy, with gross exports and imports of goods and services exceeding three times its GDP. In this setting, the exchange rate has a stronger influence on inflation than domestic interest rates. Therefore, it is crucial that we pay attention to the trade relations between Singapore and its trading partners to assess the path that the MAS will take going forward. These changes impact the USDSGD pair.

Singapore Non-Oil Domestic Exports YoY

Key export metric has been deteriorating since the start of this year.



Source: Enterprise Singapore

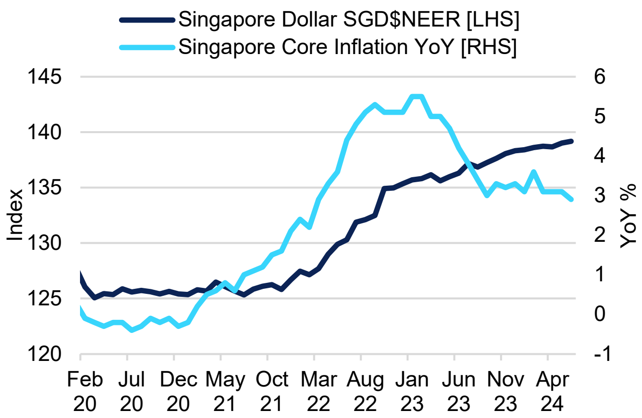
The non-oil domestic exports (NODX) contracted 8.7% YoY in June, extending previous months' declines. NODX to Singapore's top markets fell in June as a whole, with the largest contributors to the decline being the US, HK and the Chinese mainland. While electronics shipments declined 9.5% in June after the 19.6% expansion in the previous month, other factors also contributed to the drop. In particular, port congestions have plagued Singapore's ports in recent months, with ship arrivals falling to the lowest level in more than a year, given the rerouting of ships away from the Red Sea. However, we expect the pressures on trading routes to soften in the coming months, bringing export/import flows in balance.

Singapore Monetary Policy

Singapore's central bank has a unique method of conducting monetary policy. Instead of changing domestic interest rates like other economies, the Monetary Authority of Singapore (MAS) adjusts the exchange rate of its dollar. MAS sets the path of the policy band of the S$NEER (Singapore Dollar Nominal Effective Exchange Rate), which involves adjusting the local currency against those of its main trading partners. The S$NEER is an index that combines bilateral exchange rates between Singapore and its major trading partners, with weights assigned to the importance of its respective trading partners.

SGD$NEER vs Singapore Core Inflation

In response to higher inflation, MAS tightened its monetary policy.



Source: Monetary Authority of Singapore

During its latest meeting in July, the MAS kept its policy rate unchanged. Specifically, MAS re-centred the mid-point of the S$NEER policy band to its prevailing level but did not change the slope or width of the band. This marks the fifth consecutive meeting with no changes despite a softening inflation narrative. The decision has been made after several years of tighter monetary policy to enable a faster pace of SGD appreciation, which was necessary for addressing inflation. Singapore's inflation has been persistently sticky this year but is starting to show signs of easing. In June, core inflation decelerated by more than expected, posting 2.9% y/y – the lowest point in over two years. The headline followed suit, landing at 2.4% y/y after posting 3.1% in May. As a result, the MAS expects overall inflation to average between 2% and 3% for the year, down from a previous forecast of 2.5% to 3.5%.

USDSGD

Despite growing SGD$NEER, USDSGD has kept within a tight range.

Source: Bloomberg

This opens the path for MAS to begin the cutting cycle by the end of this year. Given the expectation of the Fed monetary policy cutting cycle starting in September, the narrowing interest rate differential with the US should alleviate any need for a premature cut from the MAS. For now, inflationary pressures continue to be a concern worldwide. Major central banks may opt for gradual rate cuts instead of aggressive ones. A cut later on in 2024 or in Q1 2025 will give MAS more room to assess the domestic situation before implementing monetary policy changes.

Desk Comments

GBP

GBP has continued to strengthen this year. It is the best-performing currency in the G10 space. The UK is benefiting primarily from relative political stability following the recent general election, in comparison to neighbouring France's political turmoil over recent months and the ever-changing US electoral landscape as we approach the November election.

The BoE cut interest rates for the first time since the pandemic and ahead of the FED. This was priced in as a 65% chance of a cut and additionally fully priced in for next month if they had kept on hold so the reaction was muted. The vote split was 5-4. The biggest concern for the BOE will be the upside surprise in services. Accommodation price rises were attributed to be the largest contributor to price growth. The market is now pricing a further 42bp of cuts by year end.

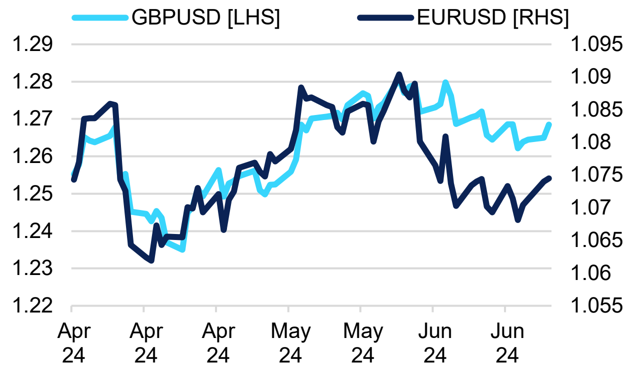
Recent PMI releases also show the UK outperforming France, Germany, and Spain, supporting GBP's strength within the G10 space, especially against the EUR. UK July Manufacturing PMI rose from 50.9 to 51.8, and services increased from 52.1 to 52.4, meaning the composite PMI rose 0.5 compared to the Eurozone composite 0.1 growth. We continue to favour selling into EURGBP rallies as PMIs diverge and the yield differential is set to widen further.

EUR

Following last month's French elections, the country is set to be left in some political limbo as President Macron announced the outgoing government will remain in place while France hosts the Olympics. While this will provide domestic stability for the games, it also leaves France's fiscal policy uncertain as the new government is formed, raising questions about the policies the expected super-coalition will propose. The formation of the government may take up to a year, after which a re-election could be called. Therefore, Frances's political uncertainty will not be resolved anytime soon, so volatility could remain in the EUR and could hinder the EUR's performance against other G10s for the foreseeable future.

GBP and EUR vs the Dollar

EURUSD has been gaining momentum following the outcome of French Elections.



Source: Bloomberg

France and Germany's Manufacturing PMIs came in below survey levels, dragging the July composite number down to 50.1 from 50.9 in June. Eurozone PMIs across the board are almost returning to stagnation levels. From a forward-looking perspective, after Lagarde mentioned that growth figures are important to the ECB in terms of making future decisions, these worsening PMIs are sure to dampen the ECB's previously dovish position.

We remain cautious about trading the EUR; technically and fundamentally, the near-term outlook is bearish. In addition, the ECB is looking to cut further, making it an attractive funding currency. However, any political stability will give it a much-needed boost.

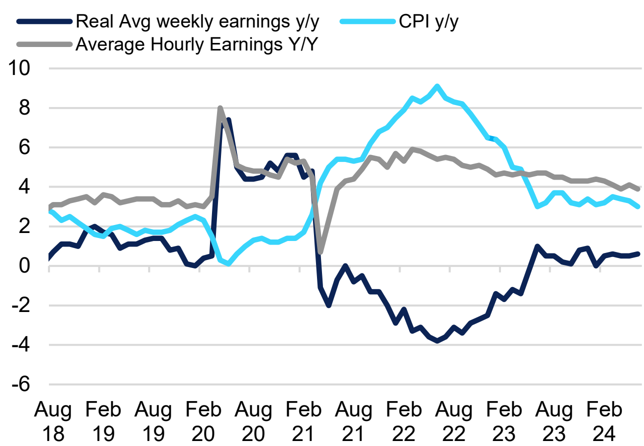
USD

The Fed maintained its policy at 5.5%. The expectation for a cut this month was down to 6.5%. The focus is on upcoming rate cuts, which are expected to begin in September.

US PMIs were mixed, with manufacturing underperforming (49.5 vs. the expected 51.6) while both services and composites beat forecasts. The latest CPI prints have given the Fed confidence that inflation is on course to reach the target. At the same time, US growth remains strong, potentially due to the increased likelihood of Trump's re-election and Trump's America-first attitude towards world economics.

US Wages vs CPI

Inflation, and in turn, real average income remains sticky.



Source: Bureau of Labour Statistics

US unemployment continues to tick higher, currently at 4.1%, which is half a percentage point above its low point in the past year. According to the Sahm Rule, this is an early indication of growing recessionary risks. However, we believe this is more due to a rebounding labour supply. On the other hand, the number of layoffs remains historically low, and as long as firms retain their existing workforce, the chance of a recession remains slim.

The medium-term outlook of the USD is dependent on the US elections. Historically, markets begin to trade elections from late August into September, so while the macro outlook is likely to drive the market over the next few weeks, the focus will change to elections. The current pricing of a Trump victory is at 63%. In this scenario, we expect USD to trade positively as the likely impact of a Trump victory will have on trade and geopolitics. The MXN and CNH will likely weaken due to potential tariffs imposed on the flow of imports. Safe haven assets will also benefit, with the added risk premium associated with the election.

Our Outlook

Our View: Our expectation is for a gradual strengthening of the SGD until the end of this year and the beginning of next year. The MAS is likely to continue keeping the S$NEER unchanged in an effort to uphold the appreciation of the local dollar. This will help to dampen imported inflation, calm the markets, and reassure investors who might be wary of sudden policy changes. With stabilizing inflation in Singapore and a softening monetary policy narrative in the US, we anticipate the USDSGD to weaken to 1.33-1.34 by the end of this year and continue to fall to 1.32 by the second half of 2025.

Technical Analysis

GBPUSD

GBPUSD has been trading within a symmetrical triangle pattern. Price broke above the 1.2800 – 1.2890 resistance that had served as strong resistance this year. If these levels hold, we expect a test of the upper triangle 1.30 – 1.3035 area. A break back below may open up 1.2613 (previous low) -1.2652 (200dma). Our expectation over the summer months is for the pair to continue to trade within the range.

EURUSD

EURUSD price action continues to trade within a range. The wedge formation still holds. On the topside a break of 1.09 – 1.0940 confirms a break of the wedge and further momentum could see EURUSD test 1.1140 (Dec 2023 highs) and even 1.1276 (Jul 2024 highs). On the downside a break of 1.0670 opens up 1.0460 (Oct 2023 lows) and an extended move lower would target 50% fibo at 1.0406.

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