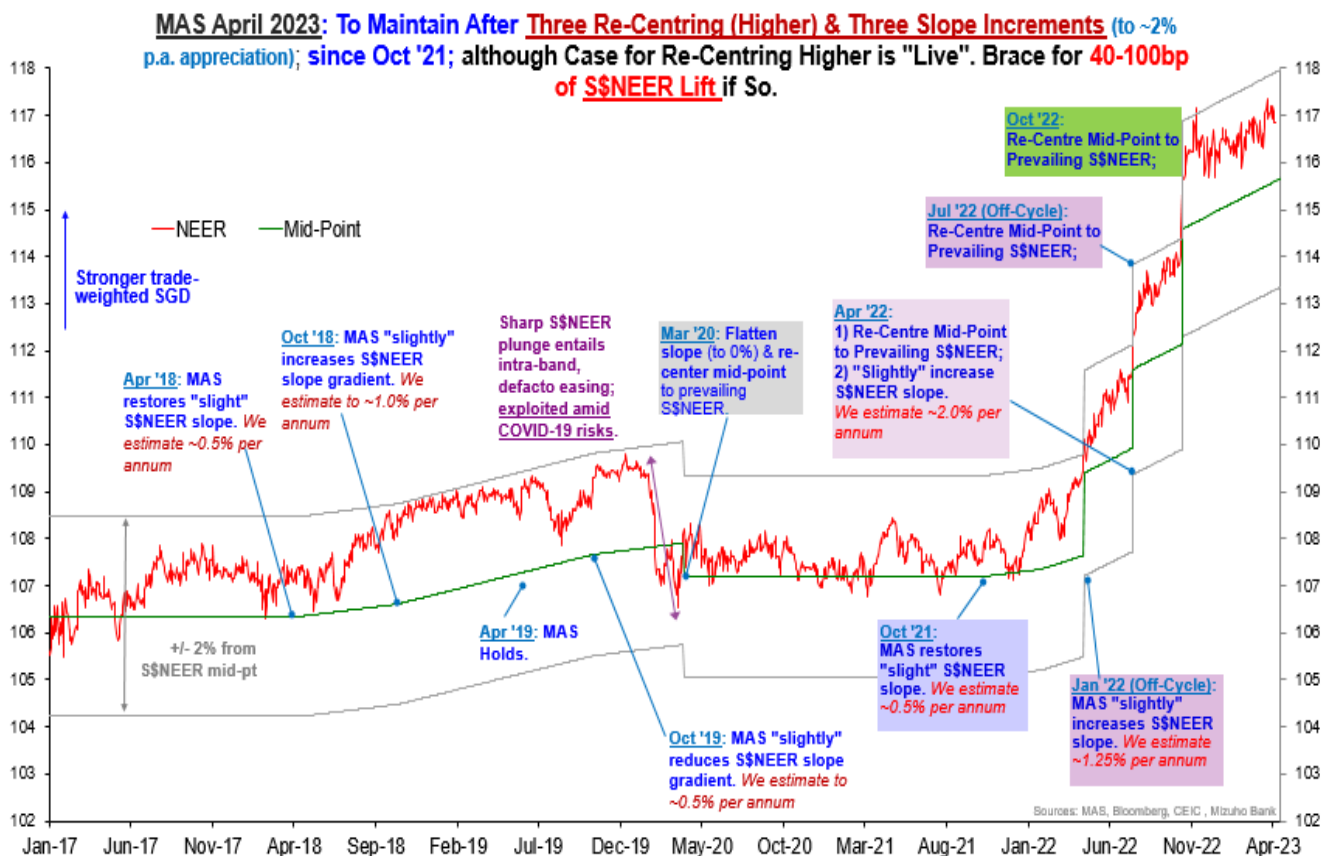


MAS: Constrained Options & Compromised Outcomes

	Option 1	Option 2	Option 3	Option 4
MAS Move	Hold (Formerly unambiguous base case)	Re-centre <i>Higher but Below</i> Prevailing S\$NEER	Re-centre <i>Higher to</i> Prevailing S\$NEER	Widen the Policy Band
Nature of Move	Neutral	Mildly Hawkish	Hawkish	Neutral (Defacto Mildly Hawkish)
Probability	40%	25%	20%	15%
S\$NEER Impact	Declines 10-40bp	Rises 30-50bp	Rises 80-120bp	Rises 20-60bp



“No longer certain that one ever does win a war, I am.” – **Master Yoda, Star Wars**

Base Case Hold Challenged; But Without Clarity

Our previous (pre-banking turmoil) **base case for MAS to hold** is now **seriously challenged, albeit with little clarity**, as **conflicting externalities** (inflationary shocks amid growing risks of adverse external demand shocks). **More complex calculus of various discrete policy options** suggest **potential for greater S\$NEER/SGD volatility on MAS policy** decision.

Up-Front Tightening Down-Plays Inflation Trigger

To be clear, unnervingly elevated inflation is not the reason; at least not directly so Reason being, aggressively front-loaded tightening from October 2021 through October 2022, comprising an unprecedented three rounds each of re-centring (S\$NEER mid-point) higher and steepening (S\$NEER slope) ought to have set up policy to absorb most of the pipeline inflation risks.

But Diametrically Opposed Banking-Oil Shock Risks Frustrate

Instead, our comfort with a hold for is compromised by a frustrating juxtaposition of (potentially deflationary) global banking sector risks and (latent inflationary threat from) steep OPEC+ production cuts. What's more, these diametrically opposed risks cannot simply negate one another; as triggers and nature of impact differ substantially.

Compromised Action from Constrained Options

Nor can monetary policy address inflationary and deflationary risks at simultaneously. Which necessarily means that there needs to be a compromise policy action, derived from four constrained policy options, that minimizes risks associated with the inherent and accentuated policy dilemma:

Option 1 - Stoic Hold: The first is to stick with the policy hold. This deliberate inaction will be most effective in checking downside economic risks without undoing prior inflation anchor. Nevertheless, it entails letting the guard down on fresh cost shocks.

Option 2 - Calibrated, Incomplete Re-Centring: Re-centring the S\$NEER higher, but below, the prevailing S\$NEER level provides the benefits of additional inflation buffer, while being relatively less aggressive (than re-centring to prevailing S\$NEER levels) and having precedent (in April 2011).

Option 3 - Unrestrained Re-Centring: Re-centring the S\$NEER to the prevailing S\$NEER level provides maximum inflation buffer, but at the highest cost to growth; especially in the event of adverse shocks.

Option 4 – Wider Bands: Admittedly the most controversial tool. This is theoretically meant to temporarily accommodate higher volatility, not impose a durable policy hawkish/dovish slant. But this is precisely why this left-field tool may deliver. For a start, pre-existing upside S\$NEER tendencies render this technically neutral move to an effectively hawkish one (of more S\$NEER upside). And revoking wider bands (upside in S\$NEER) when external headwinds mount will inflict the least damage to credibility (i.e. won't be seen as a hasty reversal of excessive tightening).

Communication Challenge Argues for Status Quo (Hold) ...

The pity though is that challenges in communicating policy intent significantly affect the viability of 'Option 4 - Widening Bands'. Hence we "only" ascribe a 15% probability to this while retaining a hold (Option 1: 40%) as the most likely discrete outcome given growing headwinds to growth.

... Although Non-Negligible Re-centring Speaks to S\$NEER/SGD Upside

But that said, the likelihood of measured tightening via mid-point re-centring higher simply cannot be dismissed (combined 45% in the partial and unreserved iterations). This suggests potential for pronounced S\$NEER (SGD) volatility; as more dispersed policy expectations are forced to converge on MAS policy announcement. Ironically our preference for a hold (as a discrete outcome) is at odds with a greater combined probability of measured S\$NEER (and SGD) appreciation bias. In any case binary SGD outcomes are a distinct likelihood; and unfortunately "winning" outcomes are precious few.

Important Information

This publication has been prepared by Mizuho Bank, Ltd. (“Mizuho”) and represents the views of the author. It has not been prepared by an independent research department and it has not been prepared in accordance with legal requirements in any country or jurisdiction designed to promote the independence of investment research and is not subject to any prohibition on dealing ahead of the dissemination of investment research.

Disclaimer

Unless otherwise stated, all views or opinions herein are solely those of the author(s) as of the date of this publication and are not to be relied upon as authoritative or taken in substitution for the exercise of judgement by any recipient, and are subject to change without notice. This publication has been prepared by Mizuho solely from publicly available information. Information contained herein and the data underlying it have been obtained from, or based upon, sources believed by us to be reliable, but no assurance can be given that the information, data or any computations based thereon are accurate or complete. This publication provides general background information only. It is information in summary form and does not purport to be complete. This publication has been prepared for information purposes only and is not intended by Mizuho or its affiliates to constitute investment, legal, accounting, tax or other advice of any kind and all recipients of this publication are advised to contact independent advisors in order to evaluate the publication, including, without limitation, the suitability of any security, commodity, futures contract or instrument or related derivative (hereinafter, a “financial instrument”), product or strategy herein described. This publication is not intended to be relied upon as advice to investors or potential investors and does not take into account investment objectives, financial situation or needs of any particular investor. It is not intended for persons who are Retail Clients within the meaning of the United Kingdom’s Financial Conduct Authority rules nor for persons who are restricted in accordance with US, Japanese, Singapore or any other applicable securities laws.

This publication has been prepared for information purposes only and is not intended by Mizuho to market any financial instrument, product or service or serve as a recommendation to take or refrain from taking any particular course of action or participate in any trading or other strategy. This publication is not an offer to buy or sell or a solicitation of any offer to buy or sell any security or any of the assets, businesses or undertakings described herein, or any other financial instrument, nor is it an offer to participate in any trading or other strategy, nor a disclosure document under applicable laws, rules, regulations or guidelines. Nothing contained herein is in any way intended by Mizuho or its affiliates to offer, solicit and/or market any financial instrument, product or service, or to act as any inducement to enter into any contract or commitment whatsoever. Neither the author, Mizuho nor any affiliate accepts any liability whatsoever with respect to the use of this publication or its contents or for any errors or omissions herein.

Mizuho and its affiliates, connected companies, employees or clients may take the other side of any order by you, enter into transactions contrary to any recommendations contained herein or have positions or make markets or act as principal or agent in transactions in any securities mentioned herein or derivative transactions relating thereto or perform or seek financial or advisory services for the issuers of those securities or financial instruments.

All of the information contained in this publication is subject to further modification without prior notice and any and all opinions, forecasts, projections or forward-looking statements contained herein shall not be relied upon as facts nor relied upon as any indication of future results. Opinions stated in this publication are subject to change without notice. Future results may materially vary from such opinions, forecasts, projections or forward-looking statements. The information contained in this publication may not be current due to, among other things, changes in the financial markets or economic environment. Mizuho has no obligation to update any information contained in this publication. Past performance is not indicative of future performance.

This is a strictly privileged and confidential publication. This publication contains information addressed only to a specific individual and is not intended for distribution to, or use by, any person other than the named addressee or any person or entity in any jurisdiction or country where such distribution or use would be contrary to law or regulation. Save with Mizuho’s prior written consent, you may not disclose, divulge, reproduce or furnish any information contained herein to any other party. Please notify the sender immediately if you have mistakenly received this publication.

Singapore: Mizuho is licensed as a bank under the Banking Act (Chapter 19) of Singapore, and is regulated by the Monetary Authority of Singapore.

Japan: Mizuho is authorised and regulated by the Financial Services Agency of Japan.

United Kingdom / European Economic Area: In the UK, Mizuho is authorised by the Prudential Regulation Authority and subject to regulation by the Financial Conduct Authority and limited regulation by the Prudential Regulation Authority. Details about the extent of MHBK’s regulation by the Prudential Regulation Authority are available upon request. This publication may also be distributed by Mizuho International plc (“MHI”). MHI is authorised by the Prudential Regulation Authority and regulated by the Financial Conduct Authority and the Prudential Regulation Authority.

United States: This publication is not a “research report” as defined in Commodity Futures Trading Commission (“CFTC”) Regulations 1.71 and 23.605. The content of publications distributed by Mizuho Securities USA Inc. (“MSUSA”) is the responsibility of MSUSA. The content of publications distributed directly to US customers by Mizuho is the responsibility of Mizuho. US investors must effect any order for a security that is the subject of this report through MSUSA.

© 2014 Mizuho Bank Ltd