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Singapore: Monetary Policy Tightened Aggressively

- In a surprise move, MAS tightened the monetary policy more aggressively by re-centring the policy band at the prevailing level of the S$NEER, and further shifted the band to one of modest and gradual appreciation, from a zero appreciation path, with the policy bandwidth unchanged.

- The combination of strong 1Q10 GDP growth, a possible revaluation in the RMB, the development in asset prices, as well as the need to anchor future inflation expectations, probably led MAS to deliver a double dose of policy tightening.

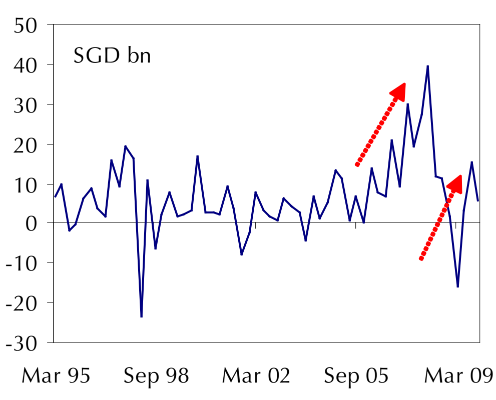
- The monetary policy decision came on the back of strong 1Q growth in the Singapore economy. Advance estimates show Singapore's 1Q GDP surged 13.1% y/y, and 32.1% q/q saar. We are upgrading our full year forecast to 7.5% from 5.8% on the strong 1Q data and the upswing in electronics and pharmaceutical output, as well as significant growth in tourist-related sectors in the coming months ahead. MAS has revised its forecast upwards to between 7.0-9.0% from 4.5-6.5%.

- We're revising our forecast for a stronger SGD of about 1.5% of our earlier forecast. Our call is now for USD/SGD to reach 1.36 at the end of 2Q and 3Q, before touching 1.33 at the end of the year.

In a surprise move, MAS tightened the monetary policy more aggressively by re-centring the policy band at the prevailing level of the S$NEER, and further shifted the band to one of modest and gradual appreciation, from a zero appreciation path, with the policy bandwidth unchanged. This is the first time the central bank has undertaken two tightening measures in one meeting. While we had expected MAS to recentre the band upwards, we had not expected 2 tightening measures, especially when the global recovery story in the later half of the year is not certain. But the combination of strong 1Q10 GDP growth, a possible revaluation in the RMB, the development in asset prices, as well as the need to anchor future inflation expectations, probably led MAS to deliver a double dose of policy tightening.

While debatable, over time though, it's generally accepted that a stronger SGD could impact foreigners' participation in Singapore's assets market (particularly real estate). Capital inflow, as shown by Singapore's Balance of Payments in financial assets has been on the uptrend since 2006, which coincided with a gradual and modest appreciation in the policy stance. This reached a peak of SGD 39.5 bn in Mar 2008. After plunging last year, it started surging upwards in Mar 09, to reach SGD 15.3 bn in Sep 09.

Balance of Payments: Financial Asset - Liabilities



Source: CEIC

A move up on the policy band would relieve pressure on the trade-weighted index and also allow further flexibility for the SGD NEER to move within the band. The SGD NEER on our model had been hovering at about 2% above the midpoint, very close to the upper limit of the policy band, for the past few weeks. MAS' current move unwinds the 2 prior policy decisions since Oct 08, which saw MAS shift to a zero appreciation neutral stance, from a previous policy of modest and gradual appreciation, and then a one-off re-centring of the policy band downwards in Apr 09.

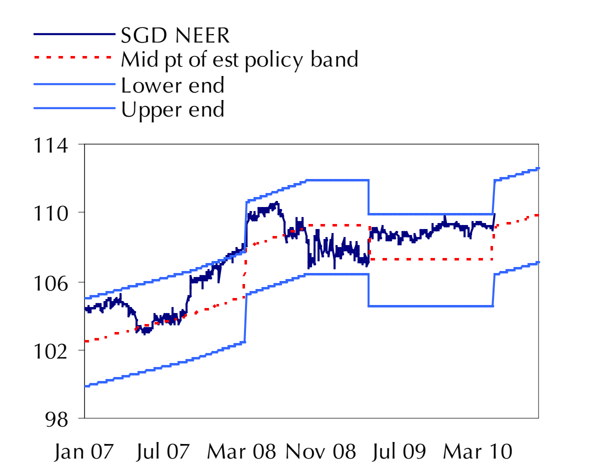
Immediately following MAS' hawkish move, the SGD NEER jumped 0.6% to 2.4% above the mid point of the policy band on our model, from the 1.8% level prior to the policy announcement. After adjustment on our model, the SGD NEER is now about 0.8% above the midpoint. USD/SGD has appreciated nearly 1.0% post-announcement to 1.3782, and with the gradual appreciation path set, we're revising our forecast for a stronger SGD of about 1.5% of our earlier forecast. Our call is now for USD/SGD to reach 1.36 at the end of 2Q and 3Q, before touching 1.33 at the end of the year.

Clearly, one of the key factors leading MAS to tighten is price increases. Headline inflation for this year should be trending higher as a result of higher commodity and COE prices, and a tight labour market. MAS now expects CPI inflation to rate to trend higher, revising their forecast upwards to around 2.5-3.5% this year from 2.0-3.0% this year. We are maintaining our CPI inflation forecast of 3.0%. Tightening policy at the next meeting in October would probably have been behind the curve, especially with Singapore's exchange rate policy, which would take longer to filter down to the economy, as compared to an interest rate policy. We are thus expecting MAS to stand pat at Oct's meeting.

The monetary policy decision came on the back of strong 1Q growth in the Singapore economy. Advance estimates show Singapore's 1Q GDP surged 13.1% y/y, and 32.1% q/q saar, higher than our own (UOB:12% y/y, 24.8% q/q saar) and consensus estimates (11.0% y/y, 18.4% q/q saar). Manufacturing was a huge boost to GDP growth, expanding 30.0% y/y and 139% q/q saar, as electronics and biomedical output rose. The data implies Mar industrial production figures to grow 32.9% y/y and -8% m/m s/adj. Services also grew more than expected, at 8.4% y/y compared to 4.1% y/y in 4Q09, as wholesale trade and tourism-related services recovered. On the back of the robust 1Q growth, we are upgrading our full year forecast to 7.5% from 5.8% on the strong 1Q data and the upswing in electronics and pharmaceutical output, as well as significant growth in tourist-related sectors in the coming months ahead. MAS has revised its forecast upwards to between 7.0-9.0% from 4.5-6.5%.

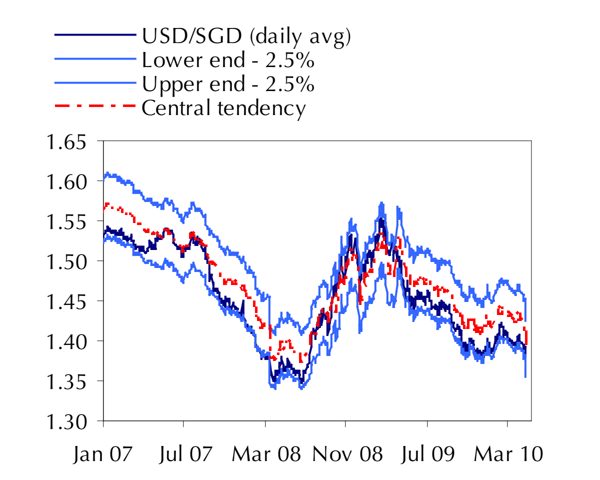
USD/SGD	2Q10	3Q10	4Q10
New Forecasts	1.36	1.36	1.33
Previous Forecasts	1.38	1.38	1.37
Source: UOB Forecast			

SGD NEER Now at 0.8% Above the Mid-Point



Source: UOB's Estimation of SGD NEER

USD/SGD to Weaken



Source: UOB's Estimation of SGD NEER

Announced MAS Monetary Policy Statements/Actions Since 2003

Date	Scheduled Meeting ?	Decision			Factors / Outlook Affecting Decision					
		Bias	Pivot Point	Width	External Econ	Global Electronics	Domestic Econ	Imported Inflation	Domestic Inflation	Labour Mkt
10 Jul 03	yes	neutral stance, 0% app	at Jul 03 level		signs of pickup, but downside risks	tentative improvement	modest H2 recovery	muted	muted	significant slack
10 Oct 03	yes	neutral stance, 0% app	at Jul 03 level		clearer signs of upturn	continued improvement	outlook improved, modest recovery	benign	subdued into next year	slack
12 Apr 04	yes	modest & gradual app	from Jul 03 level		synchronised upturn,	pickup in global IT demand,	outlook improved, likely to exceed official forecast	risk of rising inflation pressure	subdued, but could intensify	strengthen (output gap turn positive by yr-end)
11 Oct 04	yes	modest & gradual app	from Jul 03 level		greater uncertainty	greater uncertainty	growth momentum easing	risk of rising inflation pressure	subdued, but could intensify	continued improvement
12 Apr 05	yes	modest & gradual app	from Jul 03 level		growing at healthy pace	modest recovery in H2	slowing to potential growth rate	risk of rising inflation pressure	subdued, but could intensify	continued improvement
11 Oct 05	yes	modest & gradual app	from Jul 03 level		growing at steady pace	modest expansion	potential growth in 2005 & 2006	risk of rising inflation pressure	subdued, but expected to pick up in 2006	continued improvement
11 Apr 06	yes	modest & gradual app	from Jul 03 level		holding up, downside risk in 2H	steady pace of expansion	positive outlook	risk of second round inflationary pressure	some upward pressure but well-contained	remains strong
10 Oct 06	yes	modest & gradual app	from Jul 03 level		healthy 1H, moderation in 2H	peaked, 2H demand moderation	strong 1H, moderation in 2H	benign	subdued	record job gains, some wage pressures
10 Apr 07	yes	modest & gradual app	from Jul 03 level		holding up but US-realted risks emerging	easing in 1H, recovering by 2H	slower growth but outlook still positive	benign	higher by 0.5% point on GST	tight market, wage pressures in some sectors
10 Oct 07	yes	modest & gradual app, slightly steeper slope of S$NEER policy band	from Jul 03 level		downside risk has increased with fallout in US subprime housing	remained weak	strong 2007	upside risk	higher. GST rate hiked by 2ppt in July, higher asset prices	tight market, wage pressures in some sectors
10 Apr 08	yes	modest & gradual app	recentre at current level		downside risk	remained weak	stronger-than-expected 1Q08, moderation ahead	upside risk	remains high	tight market but wage growth easing
10 Oct 08	yes	neutral stance 0% app	from Apr 08 level		deteriorated sharply	expected to weaken	technical recession in 3Q08, growth to to remain below potential over the next few quarters	oil prices ease	peaked but remains high	expected to ease
14 Apr 09	yes	neutral stance 0% app	recentre at current level		sustained weakness	could weaken further	growth downgraded sharply	muted	full-year deflation expected	job losses
12 Oct 09	yes	neutral stance 0% app	from Apr 09 level		signs of recovery, but downside risks remain	continued improvement	out of technical recession, outlook improved, growth in 2010	upside risk	eased, but picking up	jobs remained fairly resilient
14 Apr 10	yes	modest & gradual app	recentre at current level		recovery in place, some downside risks remain	continued improvement	outlook for 2010 good, expected 7.5% growth rate	risk of rising inflation pressure	MAS revised forecast to 2.5-3.5% from 2.0-3.0%	tight labour market: rising wage growth