Daily Market Outlook

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Central Bank Week

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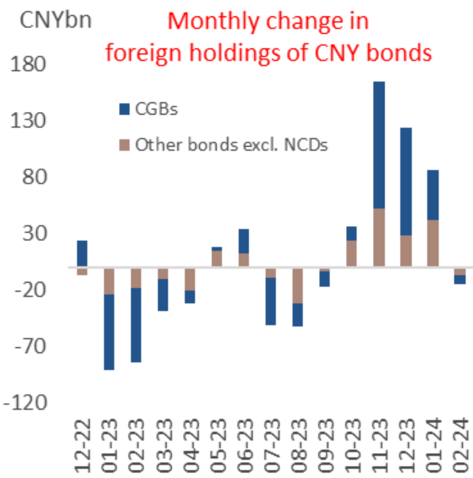
- **USD rates**. UST yields rose across the 2Y to 5Y segment on Friday as investors trimmed positions ahead of March FOMC meeting seeing risk of a hawkish tilt. Market rate cuts expectation was further pared back; Fed funds futures price a total of 72bps of cuts for this year. With the FOMC widely expected to keep Fed funds rate unchanged at its March meeting, one of the key focuses is the updated dot-plot. The December dot-plot is skewed to the upside, in that two dots moving higher would be enough to move the median dot higher. History suggests these "dots" have not been particularly accurate in predicting what would be delivered ultimately, but should the median dot move up, it would move the market given current pricing of 72bps. In the scenario where the median dot does not move, investors would likely reload bond positions. On QT, while our view remains that on aggregate, liquidity is enough to allow QT to continue at the current pace through most of this year, the last FOMC minutes revealed that members prefer to taper QT to help smooth the transition to an ample level of reserves when reserves are still more than ample, as it is difficult to gauge what is considered as ample. Investors are likely sidelined for now.

- **JPY rates and USDJPY**. JGBs were supported after BoJ announced unscheduled bond purchase operations this morning. On Friday, Rengo said in its initial results that an average 5.28% wage hike has been won, exceeding last year's 3.8%. Robust wage growth shall give the BoJ the greenlight to start normalizing monetary policy. There are a few parts of BoJ monetary policy: 1/ Short-term interest rate. We expect a 10bp hike in the policy-rate balance rate from -10bps to zero percent. 2/ Long-term interest rate: it is a close call as to whether the BoJ will remove the guidance of "10-year JGB yields will remain at around zero percent" at this upcoming meeting. We do however note the 1% is now a soft target after all. 3/ Conduct of YCC: the BoJ is likely to continue with JGB purchases even if they decide to remove YCC (2/ above); this part may just need to be renamed as "JGB purchases" if there is no longer YCC. 4/ Asset purchases. The BoJ may well stop/reduce asset purchase other than JGBs. Despite the rate hike prospect, we have a steepening bias on the JGB curve across the 2s10s segment, as the YCC may also be removed and even if not, market will likely contemplate the likelihood of a removal down the road, while the BoJ is unlikely to hike policy rates aggressively. While the yen experienced a slight uptick following the release of the Rengo results, USDJPY closed around 149.04 on Friday as UST yields rose and the dollar strengthened broadly. We expect USDJPY should continue to trade within range of 145.00-150.00 in the near term, as yield differentials are likely to play a bigger role in USDJPY's direction. On the technical chart, support is at 146.40 (200 DMA), followed by 145.00; resistance is at 149.30/40 and 150.00.

- **AUD rates.** The RBA has not pivoted yet. The February MPC statement has even left the door open for further tightening, saying "a further increase in interest rates cannot be ruled out". The RBA minutes further revealed that the Board debated rate hike at the February policy meeting. The market is however not convinced that there is a material risk of additional rate hikes. Cash Rate Futures are pricing in around 41bps of rate cuts for this year. We remain of the view that the next move is likely to be a cut rather than a hike; but the RBA will probably be among the last major central banks to start the easing cycle. Current market pricing looks roughly fair compared to our base-case for a total of 50bps of cuts this year likely starting at the August or September MPC meeting. Market watch as to whether the RBA will tweak the monetary policy guidance.

- **CNY rates.** Onshore bonds (excluding NCDs) registered a net outflow of RMB15.4bn in February. Positioning was probably heavy after four months of inflows and hence some investors might have chosen to take some profits given yields had fallen rapidly. Inflows into NCDs stayed heavy, at RMB95.8bn; Asset swap pick-up for USD-funded investors into NCDs remained appealing in the month. As long as implied CNY rates stay low, asset swap flows are likely to continue, mostly at the short end. Further out the curve, for the hefty inflows that we have seen in earlier months to repeat, CGB-UST yield differentials have to turn more favourable. We earlier cautioned against chasing long-end CGB yields lower. Yields have since rebounded; still, at current levels, we are at best neutral long-end CGBs on supply and reflation efforts. China's fixed asset investment and industrial production rose by 4.2% YoY and 7.0% YoY in the first two months respectively this year, surprising market to the upside, while retail sales went up by 5.5% YoY roughly in line with expectation. The stimulus measures put forward by the government shall contribute to growth in the later part of the year. February FX settlement data point to roughly balanced inflows versus outflows pressure, with a small outflow of USD6bn in settlement but a small positive USD4bn in forward contract. Inflows via the goods account were offset by outflows via the services account; net flows in securities were flat. The willingness to convert foreign currency proceeds into RMB was lower at 61.1%, versus above 65% in the previous two months, but still within range.



Source: CEIC, OCBC Research

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