Prepared by Treasury Research & Strategy

SGS Review & Strategy

January 2018

Your monthly guide on trend and outlook for Singapore government securities

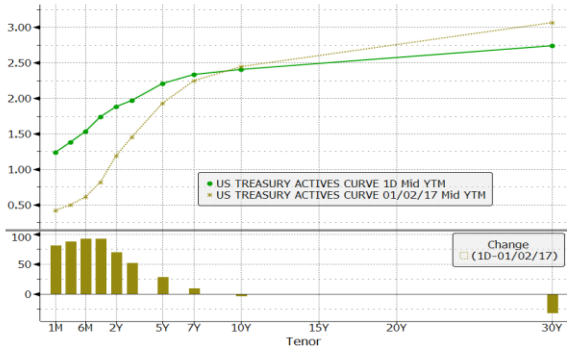
Fundamental Highlights

A benign 2018 outlook may not fully shield financial markets from bouts of volatility and profit-taking.
The passage of the US tax reform package before Christmas, including a corporate income tax cut from 35% to 21%, fueled hopes that the US economy would continue to chug along in 2018 notwithstanding the FOMC's intention persist with its monetary policy normalization after delivering its third rate hike of 25bps in December 2017 and the median dot plot still suggest three hikes in 2018. Note the PBoC shadowed the Fed in raising its key money market rates, including reverse repo rate, SLF rate and MLF rate, by 5bps on 14 December. Elsewhere, the ECB also upgraded its growth and inflation forecasts but ECB president Draghi still sounded accommodative. Key would be the September 2018 when the asset purchase program could fully wind down. For now, the other major central banks like RBA, BOE and BOJ are content to tread water and remain reluctant to follow in the FOMC's footsteps, whereas BOK and BNM in Asia have turned more hawkish in their rhetoric. Fitch also recently upgraded Indonesia's sovereign credit rating to BBB with a stable outlook, making the second upgrade in 2017 following S&P earlier, and a similar upgrade from Moody's could be on the cards as well. Asian growth prospects remain benign this year, but FX and rates may recalibrate after a strong 2017.

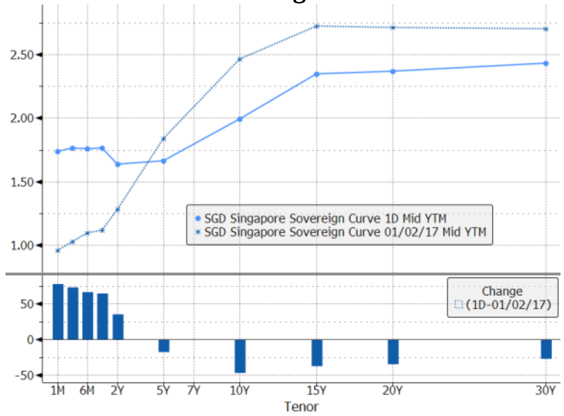
SGS Review and Outlook

2017 GDP growth hit 3.5% yoy, up from 2016's 2% and was also the fastest pace since 2014.
4Q17 GDP growth of 3.1% yoy (2.8% qoq saar) marked a slowdown from 3Q17 GDP growth, as manufacturing momentum slowed to 6.2% yoy (-11.5% qoq saar), but services sectors picked up speed to 3.0% yoy (7.5% qoq saar) on the back of finance & insurance, wholesale & retail trade and transportation & storage sectors. Unsurprisingly, construction remained the laggard at -8.5% yoy (-3.6% qoq saar) in 4Q17, dragged down by private sector construction activity weakness. Both 2Q and 3Q17 growth estimates were also revised higher. We remain sanguine on 2018 growth outlook at 2-4% yoy for now, but watch for potential policy tightening risks. The FY18 Budget, which will be announced on 19 February, is likely to focus on familiar issues of economic restructuring, education, healthcare, environment and infrastructure, but possibly also herald some tax changes. Crude oil prices topped US$60 per barrel at end-2017 and our end-2018 forecast is for US$65 per barrel for WTI. Property market sentiments have also turned more upbeat. The URA private residential property price index rose by 0.7% qoq for the second straight quarter in 4Q17 to bring the whole of 2017 increase to 1% yoy (2016: -3.1% yoy). A stronger domestic growth outlook, coupled with a possible GST hike, may accelerate inflationary expectations. MAS could potentially tweak its current neutral monetary policy stance to a slightly appreciation bias this year. The 3-month SIBOR surged to 1.50171%, with SOR at 1.11071%, and this implies some upside risks to our end-2018 forecasts of 1.55% and 1.60%.

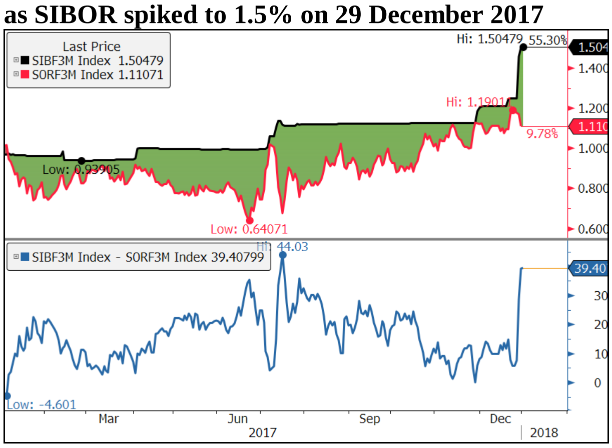
The UST curve flattened in 2017 even though the 10-year yield was virtually unchanged at 2.4%



The SGS yield curve also flattened amid strong demand for longer-dated bonds



The 3-month SOR-SIBOR spread spiked to 39bps as SIBOR spiked to 1.5% on 29 December 2017



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