Prepared by Treasury Research & Strategy

SGS REVIEW & STRATEGY

January 2017

Your monthly guide on trend and outlook for Singapore government securities

Fundamental Highlights

Trumponomics to trump the markets in 1Q17.

As US president-elect Trump's inauguration draws closer, markets are trading on a combination of hope and fear – hope that his promised tax cuts and fiscal stimulus plans would boost growth and lift corporates, but fear that China and Mexico would be at the losing end of his anti-globalisation/trade/ Immigration policies. This is clearly illustrated in the sustained uptrend in the Dow Jones since November 2016, whereas the broad USD index and the 10-year UST bond yield have begun to take a breather in January. Will this be a case of "buy the rumour, sell the fact"? At this juncture, financial markets appear to be giving Trump and the FOMC the benefit of the doubt. Whilst wage inflation has ticked higher in the December payrolls data, the futures market is still largely discounting up to two rather than three 25bp rate hikes. The FOMC is also unlikely to rock the boat by lifting interest rates at the 2 February or the 16 March meetings, albeit March will give Yellen an opportunity to set the stage for 4 May or 15 June. Elsewhere, foreign reserve erosion in many parts of Asia reflect a more proactive effort by the central banks to stabilize their currency markets, notwithstanding that economic indicators have seen more green shoots of late, especially the cyclical rebound for the manufacturing PMIs. If the reflationary theme gains further momentum, bond yields may still be biased on the upside.

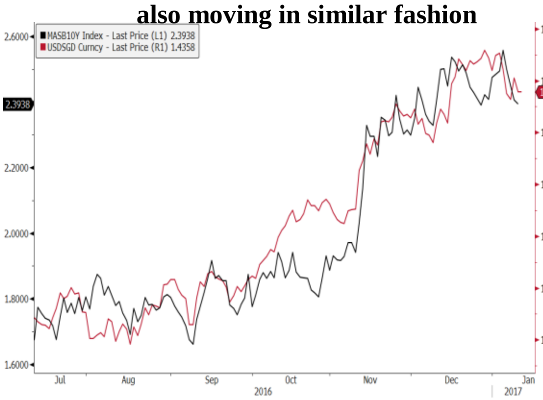
SGS Review and Outlook

4Q16 GDP surprise does not alter 2017 outlook.

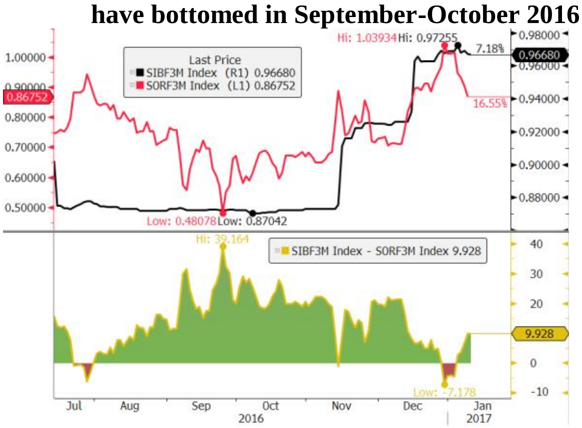
The Singapore economy saw 4Q16 GDP growth surprising on the upside at 1.8% yoy (+9.1% qoq saar) based on flash estimates, which was an improvement from 3Q's 1.2% yoy (-1.9% qoq saar) and brought the full-year growth to 1.8% as well. The uptick in manufacturing offset the contraction in construction, but services continued to be resilient. So far, both the manufacturing and Nikkei S'pore PMIs are holding above the 50 expansion level, suggesting that economic activity should sustain even though the business outlook has turned more cautious for domestic companies. Looking ahead, domestic demand is likely to soften in line with the domestic labour market, but fiscal measures at the upcoming FY17 Budget (where a modest fiscal deficit plan may not look out of place) may offset some of the consumption slowdown if greater assistance is extended to the lower-income households, elderly and unemployed. Moreover the stage has been set for a coordinated effort to build new capabilities and tackle the more challenging global economy ahead, with the Committee for Future Economy due to release its recommendations later in January. At this juncture, the clarion call of an anticipated higher US interest rate trajectory coupled with a stronger USD path may continue to hold sway in 2017. That said, a lighter 2016 SGS bond auction calendar, with the 2-year re-opening ahead, may partially offset the steepening curve bias. The 10-year SGS bond yield has shied away from the 2.60% handle so far, but a decisive break could open the way to the 2.88% high seen in September 2015. There is a 10-year SGS bond re-opening on 1 March.

Higher USD and 10-year UST bond yields - January breather ahead of Trump?

10-year SGS bond yield and USDSGD also moving in similar fashion



The 3-month SIBOR and SOR appear to have bottomed in September-October 2016



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