

**Upcoming 20-year SGS bond auction:
Fair value seen around 2.45%****Tuesday, June 25, 2019****Highlights:**

- **Tomorrow, MAS will auction \$1.9b (with MAS taking \$200m) new 20-year SGS bond maturing on 1 July 2039.** Note that this will be the last long-dated scheduled SGS bond issue this year, so demand from lifers should be decent. The scheduled SGS bond issuance calendar for the remainder of 2019 comprises of a 5-year re-opening on 1 August, a 10-year re-opening on 2 September, a 2-year re-opening on 1 October and a 7-year re-opening on 1 November, as well as an optional mini-auction on 1 October. In terms of upcoming SGS bond maturities, there is \$7.1 billion of 5-year SGS bonds maturing on 1 October this year.
- **However, the post-FOMC bond rally on the back of a dovish US Federal Reserve has left SGS yields richer than initially expected.** The existing 20-year SGS benchmark bond which matures on 1 August 2036 is currently yielding just 2.37% , down from 2.57% on 9 January – on an absolute yield level, this is at the low end of the 2.24-2.57% range seen year-to-date, and also below the five-year average yield of 2.61%. However, compared to where the 10-year UST bond yield is currently yielding at 2.01%, it offers a pick-up of 35bps (a level last seen in November 2016).
- **The SGS yield curve has actually bull-steepened since the start of 2019.** The 2-20-year SGS bond yield curve has steepened to 70bps, which while slightly wider than the 43bps seen at end-2018, but is still near the historical tightness last seen back in 2007. In particular, the 20-30-year SGS bond yield spread has also widened to 20bps (widest since June 2013), after averaging below 12bps since the start of 2018.
- **In an environment where the Fed is preparing to trim its Fed Funds policy rates and the futures market has priced in up to 75bps of Fed rate cuts this year, the SGS curve is likely to lag any US bond market moves.** This implies there is limited upside for any prospective SGS bond rallies, barring an outright recession story which is not a mainstream domestic scenario yet even though the street has marked down 2019 GDP growth expectations to around 2% and our house forecast is for 1.8% yoy growth this year. That said, pending the Trump-Xi meeting this weekend on the sidelines of the G20 summit, there is potential for global bond market to be whipsawed further.

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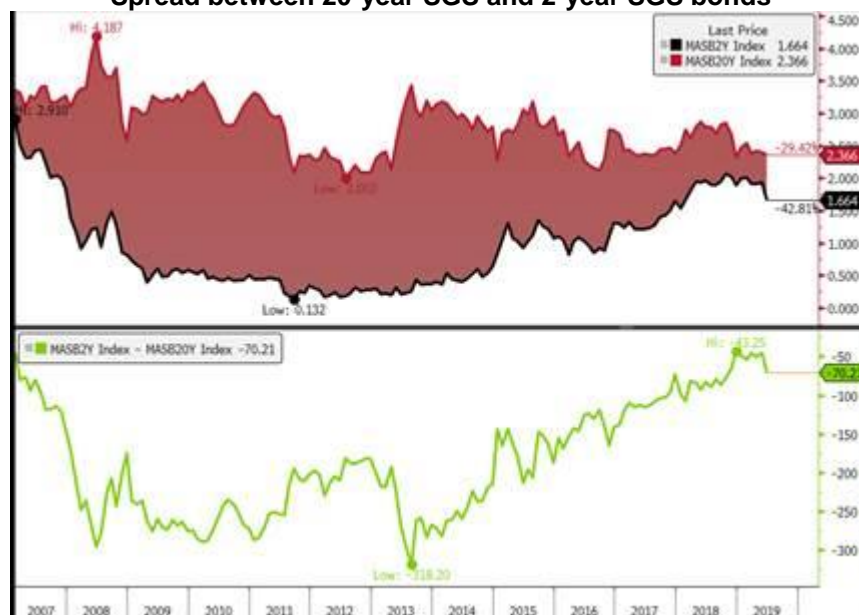
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- **We see fair value for the new 20-year SGS bond yield around 2.45% region.** Note that the 20-year bond-swap spread has widened to 16bps (last seen in March 2010), suggesting that market players have been making room for the upcoming new 20-year SGS bond issue. The 20-year swap rate has fallen precipitously to a low of 2.17% on 14 June and is currently hugging the 2.2% handle, but the existing 20-year SGS bond yield has already climbed from the recent low of 2.24% on 14 June to its current 2.37%.
 - **The previous 20-year SGS bond auction history** suggest that when yields are trading below 2.4% handle such as for the May 2017 and August 2016 auctions, the bid-cover ratio may be between 1.8-2.2x, albeit those auctions were for smaller auction sizes of \$800m-\$1.5b. Moreover, the net issue size of \$1.7 billion for the new 20-year SGS bond is on the larger end of the spectrum, so it will boil down to competing corporate issues (such as perpetuals) and the yield differential pickup they offer that could lure some potential demand away.

Historical 20-year SGS bond auctions

Issue size (\$m)	Issue Date	Amount Applied (\$\$M)	Bid-to-Cover Ratio	Cut-off Yield (%)	Median Yield (%)	Average Yield (%)
2,000	01/09/2010	4,118.3	2.06	2.91	2.85	2.81
1,100	01/03/2011	2,095.4	1.90	3.35	3.28	3.26
1,700	02/09/2013	2,533.2	1.49	3.40	3.25	3.23
1,400	02/05/2014	3,156.0	2.25	3.04	3.00	2.97
1,500	01/08/2016	2,759.4	1.84	2.25	2.21	2.19
800	02/05/2017	1,726.8	2.16	2.39	2.37	2.36
1,500	02/07/2018	3,565.2	2.38	2.86	2.82	2.73

Source: MAS, OCBC

Spread between 20-year SGS and 2-year SGS bonds



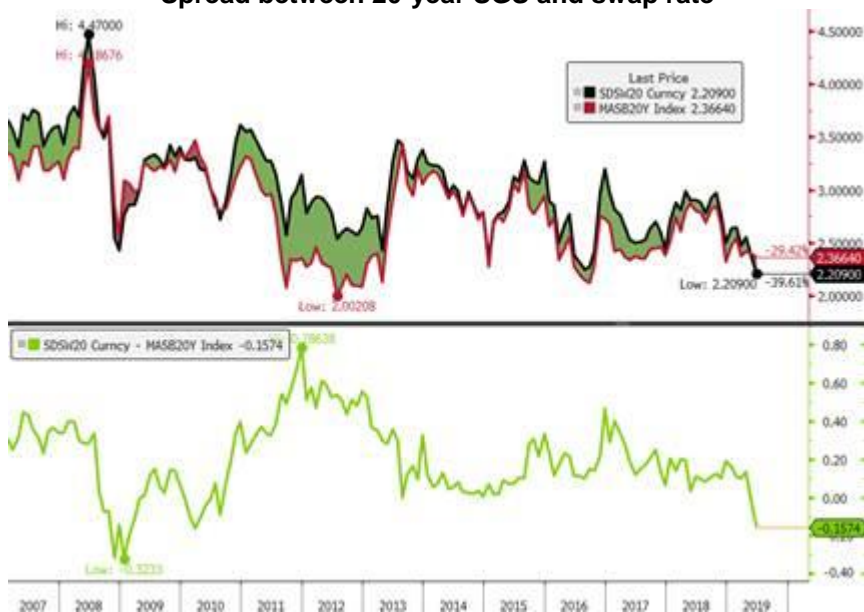
Source: Bloomberg, OCBC

Spread between 20-year SGS and 10-year UST bond



Source: Bloomberg, OCBC

Spread between 20-year SGS and swap rate



Source: Bloomberg, OCBC

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