SGS REVIEW & STRATEGY

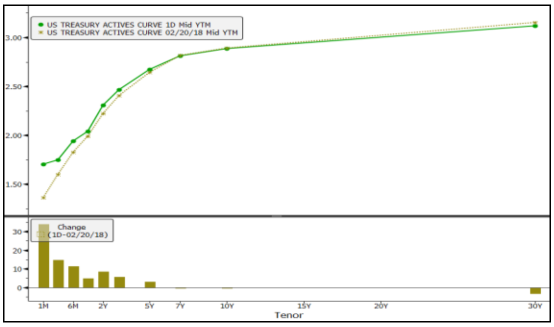
March 2018

Your monthly guide on trend and outlook for Singapore government securities

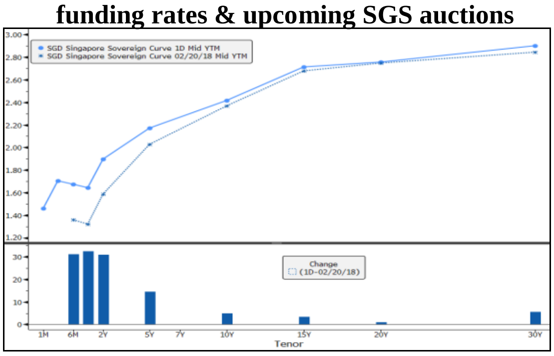
Fundamental Highlights

Fed is dovish for 2018 and too hawkish for 2019-2020?
The FOMC hiked 25bps as widely expected, and sounded more upbeat in its growth and unemployment forecasts. The FOMC statement noted that "economic outlook has strengthened in recent months". However, as we had warned market anticipation was excessively hawkish pre-FOMC and prone to disappointment. For the dots plot, 7 members are now looking at 4 or more rate hikes this year, while 8 still tip 3 or less rate hikes, leaving the median unchanged for now. Nevertheless, the 2019-2020 dots trajectory had also been lifted higher (from 2 to 3 hikes in 2019, and 2 more hikes in 2020) in anticipation of the core PCE breaching 2% during that period. This implied a median fed funds rate of 2.1% (end-2018), 2.9% (end-2019) and 3.4% (end-2020), but with the caveat that "if the outlook changes, we will adjust monetary policy appropriately". FOMC now tips growth at 2.7% (2018), 2.4% (2019) and 2% (2020), with unemployment at 3.8% (4Q18) and 3.6% (2019-2020), but median inflation is only slightly higher at 1.9% (2018), 2% (2019) and 2.1% (2020). Fed chair Powell reiterated the need for further gradual policy normalisation, highlighting that "there is no sense in the data that we are on the cusp of an acceleration of inflation". Looking forward, watch for the next US trade salvo on China's IP violation which could trigger the next bout of market volatility.

The UST curve flattened over the past month, pressured by the rising LIBOR



The SGS yield curve also flattened, amid higher funding rates & upcoming SGS auctions



SGS Review and Outlook

Watch the upcoming April monetary policy meeting.
The MAS survey of professional forecasters (SPF) tip 3.2% growth (previously 3% in Dec17) in 2018, with 2019 at 2.8%. Interestingly, SPF respondents cited the following key downside risks as trade protectionism (88% versus 40% a quarter ago), China slowdown (cut from 67% to 53%) and financial sector uncertainty rose (up from 7% to 18%). Inflationary pressures remain muted on mildly higher imported inflation and restrained domestic price pressures, especially for accommodation. MAS tips headline and core CPI at 0-1% and 1-2% for 2018, with medium-term core inflation trending towards but averaging slightly below 2%. We tip 2018 growth forecast around 3-4%, with headline and core inflation forecasts at 0.8% and 1.5% this year, and 1.5% and 2.0% in 2019. While the labour market conditions improved in 2017, driven by local employment, wage pressures remain nascent for now. Given the current headwinds of heightened trade war tensions, it's probably a finely balanced call between pre-emptive tightening and keeping the accommodative policy buffer to wait and see first as far as MAS is concerned for the upcoming MPS in mid-April. There is a $2.7b re-opening (with MAS taking 4300m) of a 2-year SGS bond maturing 1 July 2020, and $800m of a 5-year non-benchmark SGS bond maturing 1 April 2022. With the approaching month/quarter-end, liquidity conditions have tightened, especially for USD. Whilst the 3-month SIBOR is relatively stable around 1.38%, the 3-month SOR has spiked to 1.59% (highest since January 2016) but may stabilise. Our 3-month SIBOR and SOR forecasts are 1.58% and 1.63% respectively for end-2018.

The 3-month SIBOR & SOR lagging as LIBOR takes flight

Group Treasury
Treasury Research & Strategy
Selena Ling ***(65) 6530 4887***
Lingsssselena@ocbc.com.sg