SGS REVIEW & STRATEGY

Prepared by Treasury Research & Strategy

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Your monthly guide on trend and outlook for Singapore government securities

Fundamental Highlights

Crunch time for Emerging Markets (EM) amid a hawkish Trump and FOMC and a scrutiny of idiosyncratic risks.

A more volatile September appears to be a no-brainer as US president Trump threatens that the next US$200b of tariffs on Chinese imports will "take place very soon depending on what happens" and "behind that there is another US$267b ready to go on short notice if I want". In 2017, the US imported US$505b of China products. Trump had hinted that Japan will have a "big problem" if it doesn't conclude a new trade deal with the US. Fund outflows reinforce the view that the tide has turned for the many EM markets, particularly for the Fragile Five (namely Turkey, Argentina, South Africa, India and Indonesia) and may be extending to other bedfellows like Russia and the Philippines. The stronger than expected acceleration in US average hourly earnings growth has also cemented market expectations for a 25bp rate hike at the upcoming September FOMC and raising the probability pricing for another December hike to 66.9%. We don't see any light at the end of the tunnel in the near-term, with key risk events being the levying of additional US tariffs on Chinese imports, the upcoming US Treasury semi-annual FX report on currency manipulators, and the US mid-term elections likely to dominate 4Q18.

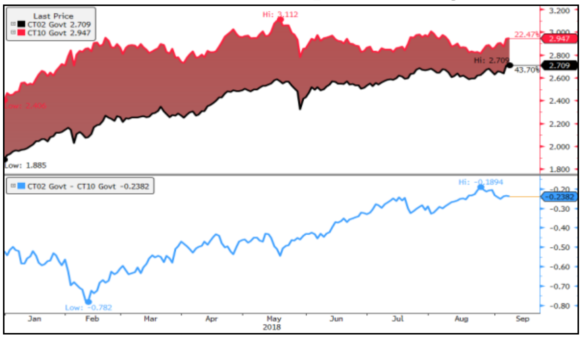
SGS Review and Outlook

Domestic resilience amid growing external headwinds

S'pore's manufacturing and electronics PMIs both improved in August to 52.6 (+0.3 points) and 52.0 (+0.4 points), which suggests our full-year manufacturing growth forecast of 7.0% yoy is still achievable. However, the Singapore Nikkei PMI pulled back to 51.1 (weakest since mid-2017) in August, down significantly from 53.0 in July, amid slower output and new orders increases and employment stagnated with wage inflation slowing further. Notably, export sales fell again and purchasing activity also dipped sharply in August, as global trade tensions begun to bite. We anticipate topline GDP growth is tipped to ease from the 3.9% yoy seen in 2Q18 to around 2.3% yoy in 3Q18. That said, the business confidence gauge for output over the next year which improved to the best in a year and suggests non-permanent damage should the trade concerns subside. The latest MAS professional forecasters survey also continue to tip 2018-2019 GDP growth at 3.2% and 2.7% yoy respectively, unchanged from three months ago. Some domestic economic resilience in the face of a deteriorating external environment should keep the odds for a further gradual S$NEER tightening at the October MPS warm for now. The 2-year SGS bond re-opening on 3 September saw healthy a bid-cover ratio of 2.19x with a cut-off yield of 1.92%. There is a 15-year SGS bond re-opening on 1 October, with the issue size announcement and auction on 19 and 26 September. There may be a mini SGS bond auction on 1 November.

The US 5y5y forward breakeven rate has crept higher post-NFP, but remains below 2014 prints.

The flattening 2-10year UST yield curve may have bottomed at 19bps on 24 August.



The 3-month SIBOR and SOR remain gradually biased higher.

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