OCBC TREASURY RESEARCH

Daily Market Outlook

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FX Themes/Strategy

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- Initial jobless claims entered marginally better than expected. Global equities edged positive, although core yield curves were softer overnight. The dovish-Fed / risk-on dynamic still persisting, at least within the FX space. The **FX Sentiment Index (FXSI)** making noticeable moves towards the Risk-On zone again over the past two sessions.

- The **USD** is still heavily weighed down ahead of the NFP print (1230 GMT). The **cyclicals** and **GBP** outperformed, with the **AUD** flexing at the 0.7400 handle and GBP clear of 1.3800. The **EUR** moved clear of 1.1850 towards the next key resistance at 1.1900/10. Overall, the DXY Index now stands near 92.00/20, where we view as a critical support below which a deeper extension of USD weakness may materialize.

- The USD's reaction to the NFP may be asymmetric to the downside – an in-line reading may still see the USD grind lower towards the Sep FOMC (22 Sep) as the market await information on the pace of tapering. A large positive surprise may be needed to reverse the USD momentum. Although the DXY Index is near a key support (92.00/20), the broad USD is not out of the woods just yet.

- Market has run on Fed- and US-driven drivers effectively since the June FOMC. Should we enter a wait-and-see mode ahead of the Sep FOMC, other central bank decisions may get more attention. RBA, ECB and BOC decisions are scheduled next week. Market chatter is for the RBA to delay the reduction of asset purchases in light of the uptick in pandemic cases. Prefer to stay negative on the AUD against the NZD. Also, the hawkish camp within the ECB is stirring again this week, with a potential slowdown in PEPP on the books at the ECB decision next week. While EUR-centric factors have not been dominant, note that EZ-US yield differentials are moving in favour of the EUR from both on the front- and back-end.

- **USD-Asia**: USD-China pairs closed below their recent range lows (USD-CNY below 6.4600; USD-CNH below 6.4500) overnight. Next key support at 6.4000 – cannot rule out a grind towards that level. This also gives the go-ahead for further downside for other USD-Asia pairs. Stay negative, pending NFP risk event, for now.

- **USD-SGD:** The SGD NEER consolidated between +0.80% and +0.90% above the perceived parity (1.3544) on Thu, and stands at +0.84% this morning. The SGD NEER's decline from +1.20% levels have been consistent, and there may still be room to extend towards +0.50%. USD-SGD nears support at 1.3420, but 1.3400 will be the key level to watch.

Rates Themes/Strategy

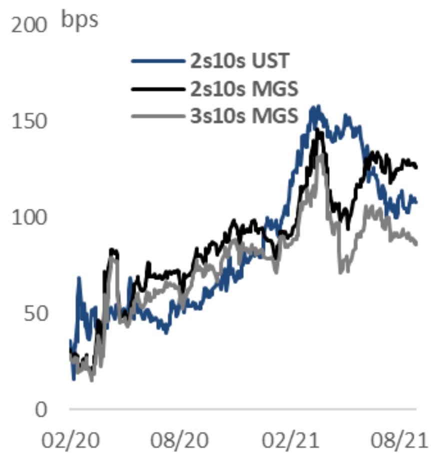
- There was limited price action in the UST market on Thursday as investors awaited the August NFP. With the perceived timing of the start of taper being sensitive to the labour report, market braces for volatility around the release. We look for an initial reaction range of 1.20%-1.33% in the 10Y yield, while a wider range is at 1.14%-1.45% which is a less likely scenario. In case of a soft payroll print, we tend to believe that any dovish market reaction will not have much follow-through, as investors may quickly realize the Fed's taper plan is unlikely to be derailed by a single month's data print – although the timing may be affected as nevertheless this is an important data point.

- The 4W bill auction continued to garner solid demand, awarded at 3.5bp, being 1.5bp lower than the o/n reverse repo rate and IOER, as the Treasury is paying down USD55bn of bills this week. Meanwhile, the 8W bill auction yield picked up to 6.5bp from 6bp at a prior auction. The relative demand between these two tenors reflects market expectation surrounding a resolution – or the absence of it - of the debt ceiling. Usage at the o/n reverse repo facility stayed high at above USD1trn.

- The recent hawkish remarks from a couple of ECB officials have sparked debate on the potential scaling back of pandemic era stimulus. The run-rate for the PEPP to end in March 2022 is around EUR20bn per week, higher than the average net weekly purchases of EUR17bn so far in Q3. The net purchased amounts in August were smaller than those in July. The ECB may probably end up not fully utilizing the existing envelope.

- IndoGBs were trading in ranges on Thursday amid a better risk sentiment but some profit-taking flows, ahead of NPF release in the US. Supportive factors for the domestic bonds remain, including flows capping USD/IDR, availability of DNDF and well-behaved onshore swap points for hedging, and a favourable supply outlook. That said, after the fairly rapid downward move in yields over the past couple of weeks, it is more likely to be a period of consolidation rather than another leg lower for yields.

- The 20Y MGII auction went well at a bid/cover of 2.687x, and with bid yields a tad lower than WI levels. We remain of the view the MGS curve is biased to steepening mildly, on dovish monetary expectations and a mild supply risk. The MGS curve has flattened more than most Asian peers in z-score term over the past three months, with the 3s10s segment 1.4 standard deviations narrower than its three-month average.



Source: Bloomberg, OCBC

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