Daily Market Outlook

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FX Themes/Strategy

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- Some Nikkei/Topix weakness in the Asian session flowed through into EZ equities also coming in soft. However, US equities firmed into the close, leaving the overall risk gauge still leaning positive. Overall, the **FX Sentiment Index (FXSI)** has reflected a consistent improvement in risk sentiment over the past 7 sessions or so, leaving it closer to Risk-On zone rather than Risk-Off.

- The **broad USD** bounced higher against most G-10 counterparts after the DXY Index touched the 93.50 support level. The **JPY** was the sole gainer against the USD, with the USD-JPY back below the 114.00 support. The **EUR-USD** retreated from highs towards 1.1600/20 levels. The **antipodeans** were the sharpest decliners, led by the **AUD**. This could potentially be the start of a deeper pull-back by the antipodeans from their over-extended technical levels.

- Overall, the USD's consolidation lower appeared to have paused for breath. We have reiterated the case that the USD's underlying fundamentals are bullish, and it's a matter of being patient for the USD bulls. They can look to two potential catalysts:

- (1) The full suite of major central bank decisions coming up over the next two weeks – BOC, BOJ and ECB next week, then the RBA, FOMC and BOE the following week – may be cue for relative central bank dynamics to impose on the FX market again, after running on risk and commodities over the past 7-10 sessions. This could be a USD positive as hawkish Fed remains the central assumption within the central bank space. It may also imply toppish action for the EUR and AUD should their central reiterate dovishness. (2) Front-end yield differentials have a good correlation with EUR-USD and USD-JPY movements this year. There has been some disconnection of late, but do not rule out a re-engagement soon. Should these two factors start to pull over the next two weeks, we may see the USD regain traction against the EUR and JPY.

- **USD-Asia**: The USD-CNH has partially retraced this week's dip to return to the 6.4000 handle. Clearly, the pace of RMB appreciation remains a concern for the authorities. Nevertheless, so long as the services deficit on the BOP does not return, we may not see the RMB come under sustained pressure. One view onshore is that international travel may still be restricted until the Beijing Winter Olympics in Feb 2022 – this implies another 3-4m before the return of the main source of services deficit for China – the outgoing tourists. Still time for RMB strength to persist.

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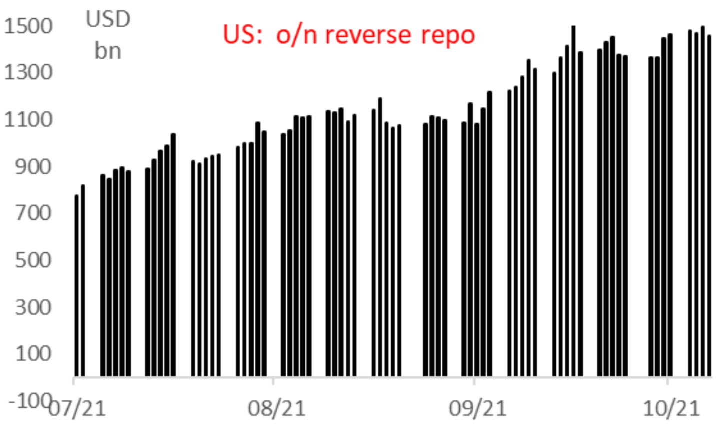
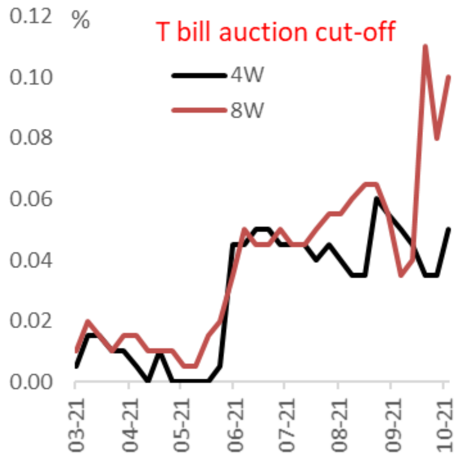
- The UST curve bearish flattened as investors geared up inflation expectations while maintaining hawkish rate hike pricing. The supply of USD19bn of 5Y TIPS was absorbed readily, with the 5Y breakeven rising by 10bp overnight to 2.9128%, almost matching the highest in March 2005. After the recent upticks, the 2Y UST yield still lags the movement in Eurodollar futures or Fed fund futures surrounding late 2023 contracts. In other words, front-end yields may stay at the current high levels as long as market maintains rate hike expectations.

- The yield at the 8W bill auction rose back to 10bp, widening the gap with the 4W bill yield, reflecting that the pressure point regarding the debt ceiling resurfaces as we get nearer December. Yields on bills that mature in December have already been trading slightly higher than the rest of the curve in the secondary market in recent sessions. Meanwhile, usage at the Fed's o/n reverse repo facilities stayed high at USD1.459trn on Thursday despite the pick-up in bill supply.

- BoE's chief economist Pill said the November MPC meeting is "live" and the debate on whether to raise interest rate is "finely balanced" within the MPC. The "finely balanced" comment suggests a rate hike is not a done deal; SONIA pricing eased somewhat but still reflects an expectation of two hikes by the end of this year and for the Bank Rate to peak above 1% with rate hikes expected to be done by end-2022. These pricings look overly hawkish to us and the front-end is poised for some dovish correction.



Source: Bloomberg, OCBC



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IDR:

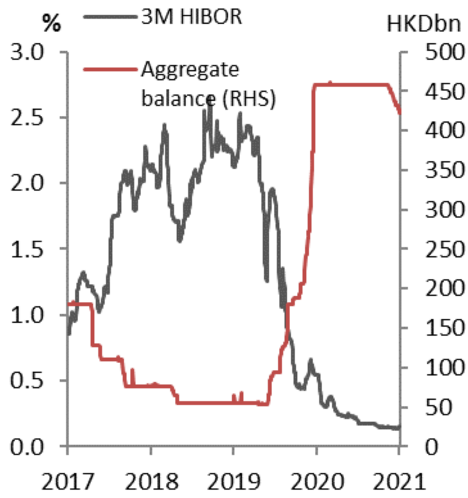
IndoGBs were trading mildly weaker on Thursday taking cue from the UST market, and also amid the weaker Rupiah. The long-end underperformed, while the mid- to front-end still saw support by domestic liquidity. The upcoming conventional bond auction on 26 October has been announced at the reduced size of IDR8trn. Supply is light but nevertheless may still trigger some re-positioning ahead of the auction. Assuming it is IDR8trn for the rest of conventional bond auctions this year, then total supply will be at IDR74trn in the quarter, lower the initially announced target of IDR81trnr which looks likely given narrower budget deficit estimates. While supply and liquidity are both supportive of IndoGBs, it may be a slightly different story for foreign investors where global yield movement remains the swing factor. There has been some comeback of foreign inflow but a trend is yet to be established. On balance, the 6% level is not easy to be broken for the 10Y.

MYR:

The 5Y MGS auction garnered a relatively high bid/cover ratio of 2.04x, but it was after some concession with yields marginally higher than WI levels which themselves already reflected the recent upticks. On balance, there was a relief rally post auction, as 3.2% appear to be the peak for the 5Y yield for now. The rally however may not be sustained given overnight movement in global yields. Tourism Minister said Malaysia aims to reopen its border to international tourists in November; and that travelers from Singapore could be some of the first to be let in.

HKD:

HKD IRS have been paid up this morning so far following USD rates. HKD rates underperformed their USD counterparts in the recent uptrend, as USD liquidity stayed exceptionally flush. This situation shall gradually change as and when there is a longer-term resolution to the US debt ceiling issue and when Fed taper starts, which is mostly a story for 2022 though. The aggregate balance (interbank liquidity) fell by HKD5bn upon the additional bill issuances on Wednesday, which was as planned; HIBOR shall be fairly insensitive to the changes (planned for further reductions in November and December) in the aggregate balance as the level will still be high.



Source: Bloomberg, OCBC

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