Rates and FX Themes/Strategy

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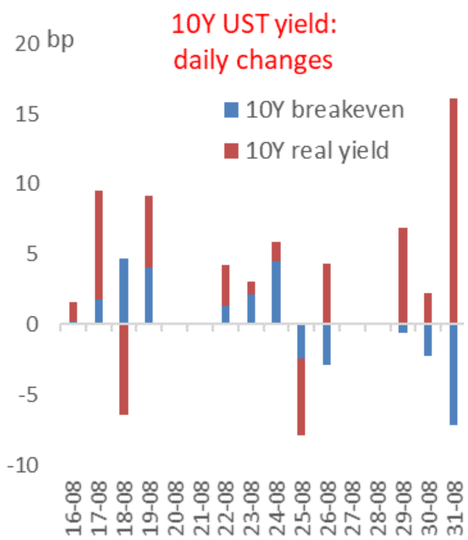
- The **UST** curve bearish steepened overnight. TIPS underperformed upon the falls in commodity – mostly energy – prices, with the 10Y breakeven down by 6bp. Front-end rates were pushed further higher at Asia open, with USD OIS now fully pricing a 75bp hike at the September FOMC. The 2Y UST yield appears to choose to put itself much ahead of the curve again, returning to the pattern seen in earlier months of the year. Comments coming through from Fed officials stayed on the hawkish side, with Mester – an extreme hawk – reiterating that "even if the economy were to go into a recession", the Fed must get inflation down and that the Fed needs to raise the policy rate to above 4% by early 2023. On the data front, the ADP report was largely shrugged off by the market, while payroll tonight is closely watched. To recap, the earlier released JOLT US job report underpinned the tightness in the labour market.



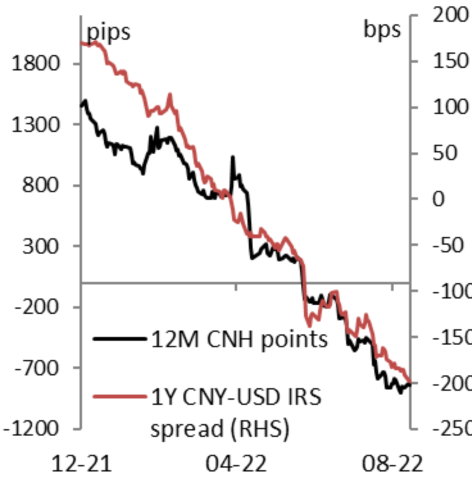
Source: Bloomberg, OCBC

- **DXY. ISM manufacturing Report in Focus.** Broad USD strength seen overnight as equities slipped and UST yields continued to inch higher. Fed speaks this week post-Jackson Hole remains consistent with Fed Chair Powell's rhetoric. Mester reiterated that she doesn't expect the Fed to cut rates in 2023 and her view is that "it will be necessary to move Fed funds rate up to somewhat above 4% by early-2023 and hold it there". We also keep a look out on UST yields as 2y is coming close to 3.5% - a level not seen since 2007. Decisive break above 3.5% could trigger more USD buying. The ISM manufacturing report to be released later is key. A stronger than expected print on ISM prices paid and ISM mfg may see UST yields, USD trade higher while slower prints could point to a temporary pause in USD strength. DXY was last at 108.96 levels. Bullish momentum on daily chart remains intact though there are signs of it waning while RSI is near overbought conditions. Resistance at 109.3 (interim double top) before 110 levels. Support at 107.30(21 DMA), 106.70 (50 DMA). Day ahead brings ISM manufacturing, construction spending.

- **EURUSD. Range.** EUR continued to trade higher, following a hotter than expected CPI print (headline at 9.1% vs. 9% expected while core printed 4.3% vs. 4.1% expected) and gas prices falling by >9% overnight. Recent ECB speaks have taken a more hawkish tilt with hawks preparing the ground for a possible 75bps hike at next week's ECB meeting. Earlier comments from EU policymaker to reform electricity market and reports of France and Germany's gas storage facilities filling up faster than planned are helping to drive down European gas futures and keeping EUR supported. We also keep in view the extraordinary meeting of EU energy ministers (9 Sep) and Ursula's state of the union address to EU parliament (14 Sep) on potential structural reform of the electricity market as Ursula said that an "emergency intervention" is required to bring down rising energy prices. A favourable outcome can help to ease price pressures overall and could mitigate recession fears in Euro-area. This can be supportive of EUR. Pair was last at 1.0025 levels. Bearish momentum on daily chart waned but rise in RSI waned. Resistance at 1.0080 (38.2% fibo) and 1.0140 levels. Support at 1.0010 (23.6% fibo retracement of Aug high to low), 0.9960 and 0.99 levels. 0.9980 – 1.0050 range likely intra-day. Day ahead brings Eurozone manufacturing PMI, unemployment rate.

- **USD/SGD. Upside Risks**. USDSGD continued to trade higher this morning amid upticks in broad USD, UST yield as hawkish Fed speaks reverberates. Fed's Mester said "it will be necessary to move Fed funds rate up to somewhat above 4% by early-2023 and hold it there". SGD NEER was trading at 0.9930% above mid-point this morning. Pair was last at 1.40 levels. Bullish momentum remains intact while RSI rose. Risks to the upside. Immediate resistance at 1.4010, 1.4060 and 1.41 levels (Jul high). Support at 1.3935 (23.6% fibo retracement of 2022 low to high), 1.3890 (50DMA) and 1.3835 (38.2% fibo).

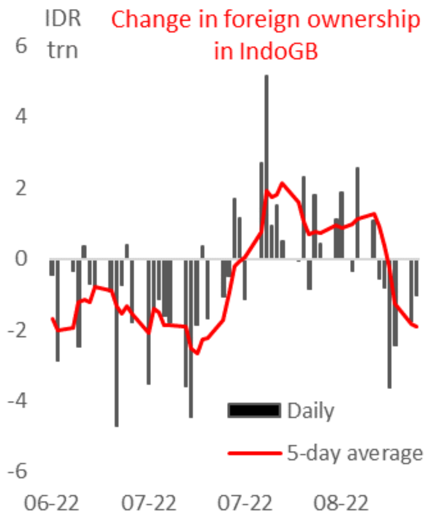
- Overnight, back-end **CNH points** rose despite the higher US yields, driven by FX and policy risk. With pressure on USD/CNY staying on the upside, investors watch out for any further policy actions to smooth the RMB move if the fixings and verbal intervention fail to do so. One of the policy tools may be the reserve requirement on foreign currency deposits; the liquidity released will not be huge with each 100bp cut translating into around USD9.5bn, but still, given the extended fall in back-end points investors might want to lighten positions in view of any possible alleviation of downward pressure brought about by a policy action. A more drastic policy action – not that we see a high chance of such - would be to re-impose the forward reserve requirement; depending on the USD funding cost, a 20% requirement would add a few hundred pips to the onshore curve at the back end. Otherwise, implied CNY rates are not as depressed as just days ago compared to repo (12M implied at 2.07% vs 1Y CNY IRS at 1.92%); and pressure is to the downside for Asian basis in general. In addition, the still wide on-offshore gap (almost 300 pips at the 12M) is a buffer for the offshore DF curve.



Source: Bloomberg, OCBC

- **USDCNH. Measured Pace of CNH Depreciation.** USDCNH was a touch firmer this morning but still off its recent highs, thanks to CNY fix coming in stronger for 7 consecutive sessions. That said, slump in China PMI into contractionary territory of 49.5 in Aug (vs. 50.4 in Jul vs, 50 expected), news of US government restricting NVIDIA chip exports to China and fresh lockdowns in many cities in China could still undermine CNH. Pair was last 6.9110 levels. Bullish momentum on daily chart intact but RSI eased from near overbought conditions. Support at 6.90, 6.8560 levels (61.8% fibo). Resistance at 6.95, 6.9860 levels (76.4% fibo retracement of 2020 high to 2022 low). Looking on, we expect CNH to take cues from broader USD moves, CNY daily fixing and China's macro outlook. Bias may still be skewed towards gradual softening in CNH.

- Some profit-taking flows were seen at **IndoGBs** on Wednesday, with yields ending the day little changed amid a tight range in USD/IDR. August CPI is due out today, where consensus is looking for a level similar to the July reading, which is still above BI's target range of 2-4%. Nevertheless, core inflation is likely to be emphasised as the preferred measure, and as such we do not expect market to react meaningfully to the CPI outcome. The 10Y IndoGB yield is likely to trade in a 7.0-7.20% range near-term. IndoGBs saw six days of outflows amid the jumps in global yields, with foreign holdings down to IDR762trn as of 30 August.



Source: Bloomberg, OCBC

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