OCBC TREASURY RESEARCH

Daily Market Outlook

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FX Themes/Strategy

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- Market focus overnight was on the sustained rise in the UST yields. The 2Y and 10Y yields opened above 1.00% and 1.80%, and basically never looked back. This further extended the yield differential advantage USTs have over bunds and JGBs. Global equities sold off in response, with the US tech sector hardest hit. The **FX Sentiment Index (FXSI)** is still within the Risk-Neutral zone but moved perceptibly the Risk-Off direction.

- The broad **USD** marked the largest one-day gain against G-10 counterparts yesterday. The European complex led losses, with the **EUR** losing more than 0.70% against the greenback. **Antipodeans** were heavy as both the AUD and NZD lost their support levels at 0.7200 and 0.6800. The **JPY** and **CAD** were more resilient against the USD, supported by risk-off and surge in crude oil prices respectively.

- The BoJ tweaked its inflation outlook to balanced in its policy decision yesterday, but market focus was on the exceptionally strong push-back from Kuroda regarding any hawkish market chatter. He was explicit in stating that policy rates will “remain at current low levels or fall even lower” and that rate hikes are “unthinkable”. This crystal-clear messaging should put any expectations of a hawkish BOJ to rest.

- In the near term, front-end yield differentials moved another leg in favour of the USD after the overnight UST yield extension. The positive correlation between the yield differentials and the USD may belatedly start to re-engage. Couple this with technical that are now turning in favour of the USD, the near-term trough for the USD may have been seen. The view that the underlying environment is not supportive of sustained USD downside is also reinforced with the latest move. Going forward, the compressed timeline of the Fed’s tightening action (tapering, rate hikes, QT) will spur more volatility in the broad USD. Prefer to stay tactical for now.

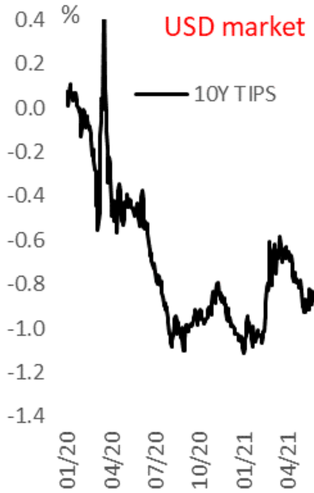
- **USD-Asia:** With US equity weakness looking to spillover into Asia, and the USD firm overnight, expect Asian currencies to come under pressure today. The PBoC followed up the rate cut with more dovish rhetoric, pledging to use the full range of tools to support the economy. The USD-CNH bounced off 6.3400 lows to stand around the 6.3600 handle. Should the USD rebound persist, expect the USD-CNH to see reduced downside impetus, and re-enter a range-trade mode.

- **USD-SGD:** The SGD NEER trudged range between +1.40% and +1.60% on Tue, settling this morning at +1.50% above the perceived parity (1.3711). The USD-SGD tracked the broad USD higher overnight, retaking the 1.3500 handle. Stay positive on the pair.

Rates Themes/Strategy

- Treasury yields jumped further across the curve, with the 5-7Y sector underperforming. The move in the 10Y yield was again brought about by higher real yield which is approaching the high seen in March 2021. Near-term fluctuations aside, our medium-term bias remains for real yield to move further higher and long-term inflation expectation to be sustained around/mildly above the current level. These may push the 10Y nominal yield to 2.20% by end-2022. The next focus is the auction of USD20bn of 20Y coupon bond tonight; market also awaits the US Treasury's next quarterly funding update.

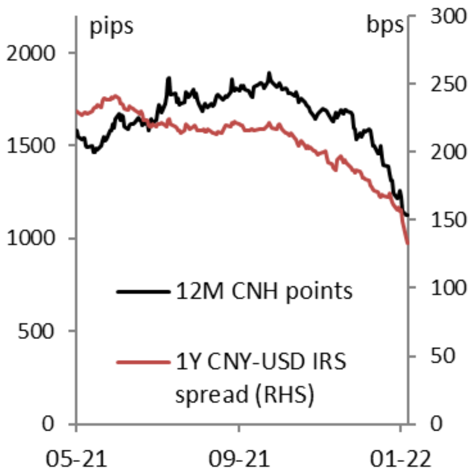
- At the front-end, market has increased pricing of rate hikes, with Fed funds futures pricing in four hikes this year. Fed officials have also been vocal in supporting the notion that rate liftoff can come right upon the conclusion of asset purchases; the last round of Fed asset buying shall happen in the mid-February/mid-March period. With the risk of rate hike coming sooner rather than later, we now expect four Fed rate hikes this year. If these expected rate hikes are to be paced out as one hike each quarter, then the schedule is still not a packed one.



Source: Bloomberg, OCBC

- **IndoGBs** stayed resilient with yields mildly higher on Tuesday, while the Rupiah outperformed some of the regional peers. The MoF issued bonds as targeted at IDR25trn against the strong incoming bids of IDR84.84trn. Sentiment may turn more subdued today given overnight fall in equities while the dollar strengthened; the next support for the 10Y bond is at 6.43%.

- The divergence in rates moves in **China** versus US has become more obvious, with the latest comments coming from PBoC deputy governor Liu who said the central bank would open the monetary policy toolbox wider. The policy outlook is a dovish one, with potential cuts in the RRR and/or MLF rate again, while investors also focus on the quantity of easing. Next to watch is the LPR on Thursday. CNY rates are trading further lower this morning. Back-end CNH points have fallen rapidly since early December, mainly on the back of narrowing CNY-USD rates differentials; recently most of the price actions happened during Asian hours while the points were relatively stable/firmer during London hours. It appears difficult to fight against the momentum given the divergence in monetary policies.



Source: Bloomberg, OCBC

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