OCBC TREASURY RESEARCH

Daily Market Outlook

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Budget and Election in Focus

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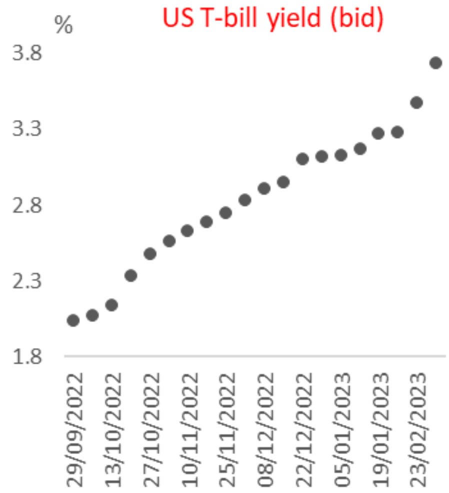
- **DXY. Hanging Man Pattern.** USD's run-up post-FOMC paused, albeit still at elevated levels above 111-handle. Part of the reason could be due to BoJ intervention yesterday to prop up the JPY that may have distorted price action. Nonetheless, higher UST yields, soggy risk sentiments may still keep USD bid on dips. We also keep an eye on geopolitical developments between Russia and Ukraine as partial mobilisation and planned referendums are expected to be held today. Another round of re-escalation in tensions could further dampen risk appetite. DXY was last at 111.16 levels. Mild bullish momentum on daily chart intact while RSI shows tentative signs of turning from near-overbought conditions. A hanging man pattern appears to have formed on yesterday's candlestick. Typically, this is associated with trend reversal. We watch price action for further confirmation. Support at 110.10, 109.67 (21DMA). Resistance at 111.80, 112.40 levels. Day ahead, watch US preliminary PMIs.

- **UST** yields continued to jump across the curve, in a steepening manner overnight. The 10Y yield was driven by higher real yield which rose to 1.30% versus pre-COVID peak of 1.16%. Usage at the Fed's o/n reverse repo facility, which now pays in interest rate of 3.05%, rose to a record high of USD2.359trn on Thursday; bill supply is on the light side – a small net cash paydown again next week, when short-end instrument is likely preferred in view of Fed rate hike prospects and market volatility.

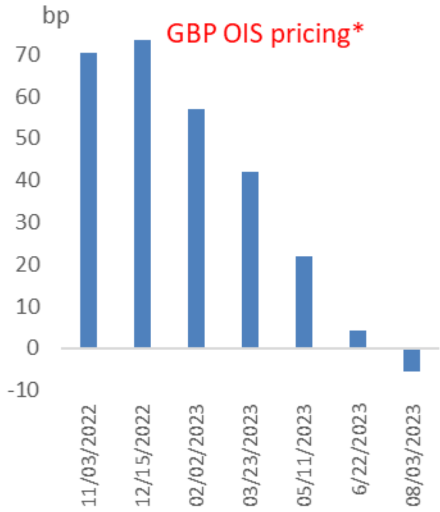


Source: Bloomberg, OCBC

- The **Bank of England** raised the policy Bank Rate by 50bp in line with expectation; the vote was not unanimous - five MPC members voted for the 50bp hike, three for a 75bp hike, and one for a 25bp hike. The MPC sounded less hawkish on the inflation front, primarily because of the energy bill. The central bank opined the Energy Price Guarantee is "likely to limit significantly further increases in CPI inflation", "will lower and bring forward the expected peak of CPI inflation", and it may reduce the risk that external inflation leads to more persistent domestic price and wage pressures. The MPC said it would make a full assessment of the impact from the Energy Price Guarantee and Growth Plan as part of its November MPC exercise. The market is not convinced that the energy bill would mean a lower pace of rate hike; instead, GBP OIS is pricing in a 75bp hike at the next MPC meeting in November. The split votes yesterday, on balance, also means a jumbo rate hike at the next MPC meeting cannot be ruled out. Still, the OIS pricing of a terminal rate at 5% looks overly hawkish.

- On QT, the BoE MPC voted unanimously to reduce the stock of Gilts by GBP80bn over the next 12 months, in line with the plan set out at the August MPC meeting. To be clear, QT has already started via run-off, and Gilt holdings under APF have fallen from a peak of GBP875bn to the latest 838bn. Yesterday's QT decision was on the active selling part. Gilt holdings will fall further to GBP758bn over the next 12 months, via around GBP40bn of run-off and GBP40bn of active selling.

- **GBPUSD. Mini Budget in Focus.** GBP is still trading around levels last seen in 1980s. Yesterday's BoE meeting saw a 3-way vote, with 1 member Swati voting for 25bps hike as she is worried about demand outlook. Accompanying statement noted that extra government spending will lead to higher medium-term inflation but government's planned energy price cap should reduce the risk of inflation expectations becoming de-anchored. Headline CPI will be around 5 percentage point lower by Jan, compared to a scenario without the energy price cap. This puts focus on the emergency mini-budget today. No details are known except on the earlier announced energy price cap of GBP2,500 annually for 2 years, effective 1 Oct. The Institute for Fiscal Studies think-tank estimated that the energy price support could cost more than GBP100bn but price tag hinges on international energy prices. There are also expectations of permanent tax cuts worth about GBP30bn a year as well as a review on fiscal rules to allow the government to borrow more. The new Chancellor has insisted that tax cuts will boost growth and help lower debt burden. But question remains how is the mini-budget funded. The Chancellor has refused to let the government watchdog, Office of Budget Responsibility assess the economic impact of planned tax cuts or release forecasts with the mini budget. Private sector estimates suggest that public sector borrowing could be at least GBP100bn and majority of it could be funded by Treasury sales of GILTs. Bear in mind BoE is engaged in QT and will begin active sales of GILTs next month. This means the BoE and Treasury will be competing for investor demand. We wait for further details though we are slightly cautious on how UK sovereign rating may be affected. GBP was last at 1.1255 levels. Mild bearish momentum on daily chart intact while RSI fell towards oversold conditions. Risks are skewed to the downside. Next support at 1.12, 1.10 levels. Previous key support at 1.1351 (recent low) now turns resistance before 1.14. Sell rallies preferred. UK preliminary PMIs are due for release today.



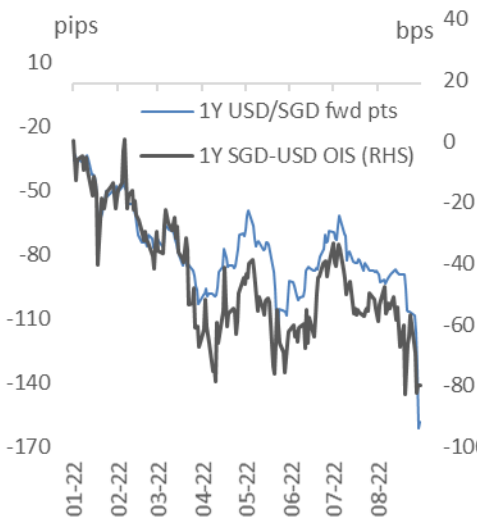
Source: Bloomberg, OCBC

- **EURUSD. Italy Election on Sunday.** EUR continued to trade with a heavy bias but short of breaking below 0.98-handle. Russian's partial mobilisation of 300,000 reserves troops and referendums planned from today to next Tue on the 4 Russian-occupied Ukrainian regions of Luhansk, Kherson, Donetsk and Zaporizhzhia may suggest that the conflict could drag on for longer, posing risks to further inflationary pressures and raises risk of economic hard-landing. EUR was last at 0.9845 levels. Mild bearish momentum on daily chart intact while decline in RSI shows signs of moderation. Key support at 0.98. A decisive break could risk a decline towards 0.9670 levels. Resistance at 0.9910, 0.9980 levels. Looking on, we still expect EUR to still take cues from (1) ECB speaks; (2) natural gas prices and how recent EU's 5-point plan to tackle energy crisis pans out; (3) Russian-Ukraine conflict, if there is further escalation. To a smaller extent, we also keep in view Italy general election (Sunday). Opinion polls suggest that a right-wing coalition led by leader Meloni is expected to win. A negative surprise outcome would undermine EUR but it appears political uncertainty in Italy is relatively contained for now. Today brings preliminary PMIs.

- **USDJPY. Wide Range May Persist.** USDJPY trades were choppy yesterday with post-FOMC USD strength and subsequent BoJ intervention, but JPY volatility appeared to have somewhat subsided overnight. This is the first time BoJ intervened to buy JPY for the first time in >20years. Previous intervention in 2011 was to sell JPY. Nonetheless our historical observation of BoJ intervention in the last 20+ years shows that JPY typically moves between 3% and 5% in the direction of intervention and the impact is typically more pronounced within the first 48 hours though the overall effect may last up to 5 days before reversing over 2 weeks. Intervention may slow the pace of JPY depreciation but the move alone is not likely to alter the underlying trend unless USD/ UST yields turn lower or BoJ changes policy stance. Yesterday's BoJ policy inaction suggests that dovish policy may continue for as long as Kuroda's term last. Looking ahead, we won't rule out stealth JPY intervention if magnitude of JPY decline increases again especially when it breaches 146 levels. Pair was last at 142.10 levels. Daily momentum turned mild bearish while RSI fell. Risks skewed to the downside. Resistance at 145 levels. Support at 141.5 levels (23.6% fibo retracement of Jul low to Sep high), 140.40 levels. Trades in 140 – 145 range could still suffice for now. Onshore markets are closed today and we caution that thin market liquidity can exaggerate abrupt FX movements.

- **IndoGBs** fell across the 2Y to 5Y segment in response to Bank Indonesia's decision to hike its policy 7-day reverse repo rate by 50bp against consensus for a 25bp hike. The policy tightening underpins our view for the curve to stay flat, with bonds at front-end up to the 5Y staying under selling pressure from some local investors and BI's operation twist. Next week's conventional bond auction has the usual indicative target of IDR19trn; if the market environment is not conducive then MoF may not issue the full amount. Foreign holdings of IndoGBs fell further to IDR743trn, or 14.72% of total outstanding, as of 21 September. On the policy rate front, we now expect a 25bp hike at each of the remaining three meetings of the year, which will bring the 7-day reverse repo to 5% by year-end.

- **SGD rates**. SGD rates had outperformed USD rates in recent sessions until yesterday, as the forward points were under downward pressure probably as market tried to incorporate some MAS tightening expectation. Further outperformance hinges on MAS policy and the broad dollar direction. Singapore releases inflation data later today. The CPI, in particular the core CPI, is a key input into the expectation



Source: Bloomberg, OCBC

for the upcoming MAS policy. If core CPI surprises to the upside, then we may see some further SGD rates outperformance over USD rates.

- **USD/SGD. Sideways at Elevated Levels.** USDSGD remains bid, tracking USD strength post-FOMC, continued weakening in RMB and recent escalation in geopolitical tensions stoking risk-off sentiment. Pair was last at 1.4190 levels. Bullish momentum on daily chart intact while RSI rose near-overbought conditions. Risks to the upside. Resistance at 1.4230, 1.4295 (76.4% fibo retracement of 2020 high to 2021 low). Support at 1.4160, 1.4110/20 levels. S$NEER is trading ~1.4% above mid-point. SG CPI in focus today.

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