OCBC TREASURY RESEARCH

Daily Market Outlook

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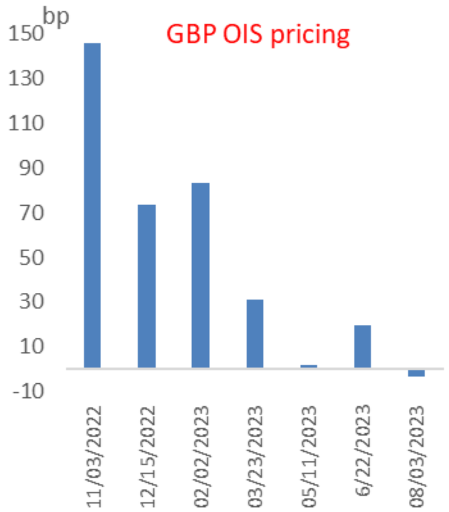
Relative calm

- The **UST** curve bearish steepened overnight with yields closing at near intra-day highs. Yields softened back mildly upon Asia open this morning. The 10Y real yield rose to 1.62% at NY close, well above the pre-covid peak of 1.16%, while the 10Y breakeven edged lower. The upticks in the 10Y real yield over the past sessions may be better seen as a residual of the relative performances of TIPS versus nominal bonds, rather than being a driver for market movement. Still, real yield is also a proxy for the growth outlook, and we see upside being capped until investors see additional, strong US economic data. Meanwhile, the 2Y UST yield shall move nearer the expected peak (effective) Fed funds rate over time; our target is 4.60%.

- **Gilts** underwent another sell-off session on Monday as investors continued to digest the fiscal news. Upon much expectation for some emergency actions from the BoE, the central bank came up with a short statement which failed to impress the market. BoE re-iterated that it would "make a full assessment at its next scheduled meeting of the impact on demand and inflation from the Government's announcements" including the Energy Price Guarantee and the Growth Plan. The BoE said it would not hesitate "to change interest rates by as much as needed" to return inflation to target. The strongest wordings being "as much as needed", without an immediate policy action, appears not enough to revive confidence in GBP assets at this juncture. GBP OIS pared back pricing of rate hikes upon the BoE statement, to 146bp of hike at the November MPC. Market waits for some calm coming back to the market but risk-reward does not justify positioning for Gilt rally at the moment.

- **DXY. Slowing Pace of Gains.** DXY continues to trade near 2-decade high amid elevated uncertainty in markets but there are signs that the pace of gains appeared to have slowed, at least for now. We believe **regional authorities are keeping a close watch on markets and as such, may potentially engage in *leaning against the wind* activities or impose further stabilisation measures, etc if market volatility heightens**. For instance, PBoC imposed a 20% risk reserve requirement (up from zero) on FX forward sales, BoJ ramped up its operations yesterday (to buy JPY550bn of JGBs maturing in 5 -10y vs JPY150bn in previous operation) and again did another unscheduled bond purchase operation this morning while BoK is also preparing several measures to stabilise financial markets. Overnight, White House said it is monitoring markets amid volatility, SNB governor signalled openness to intervene in CHF if needed and this morning, Taiwan central said it may adopt FX controls in case of severe foreign outflows but so far outflows are under control. Stabilisation measures can help to restore market confidence. That said the yield appeal and haven characteristics of the dollar may still keep it supported. DXY was last



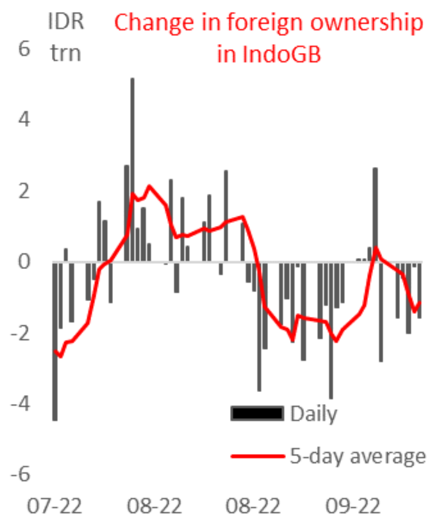
Source: Bloomberg, OCBC

at 113.82 levels. Bullish momentum on daily chart intact while RSI shows signs of turning from overbought conditions. This may indicate that the pace of gains may slow. Support at 113.20, 112.40 levels. Resistance at 114.20, 114.50 levels. Day ahead, watch durable goods order, conference board consumer confidence, Richmond fed mfg, new home sales.

- **EURUSD. Bearish but Oversold.** EUR's decline paused near 20-y lows as markets re-assess dynamics. Apart from USD strength, geopolitical tension in Russia and lingering uncertainty out of Italy election outcome were some factors behind EUR's softness. Last at 0.9630 levels. Bearish momentum on daily chart intact while RSI dips into oversold conditions. Support at 0.9555 levels (intra-day low), 0.95. Resistance at 0.97, 0.9865 levels. Elsewhere we also watch if Russia dials up geopolitical tensions again. There were warnings from Russian officials that Moscow could use nuclear weapons to defend illegally annexed regions in Ukraine. A case of conflict could drag on for longer poses risks to further inflationary pressures and raises risk of economic hard-landing. 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.

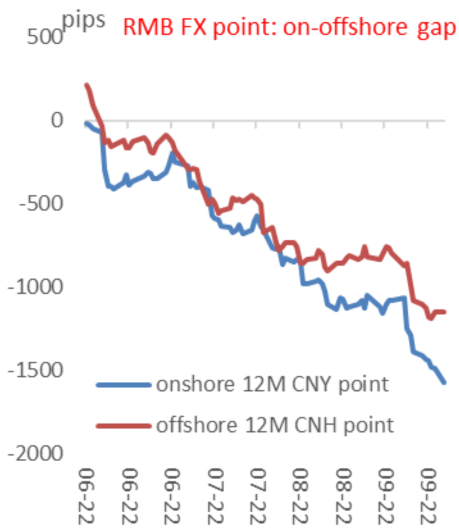
- **GBPUSD. Rebound Not Ruled Out in Near Term.** GBP's yo-yo session somewhat stabilised a little after Treasury issued a statement to say that the fiscal plan will set out further details of government's fiscal rules including ensuring that debt falls as a share of GDP in the medium term. But uncertainty remains elevated, judging from 1m vols which has spiked above 20-levels. These are levels seen around Brexit-2016 and pandemic sell-off in 2020. We remain cautious on GBP outlook. Short GBP has been one of market's favourite trade this year to proxy for stagflation play but increasingly, there is now another motivation to short GBP as it is becoming a confidence issue. In Lawrence Summers' words, the *UK is behaving a bit like an emerging market turning itself into a submerging market*. Sky news reported that some former minister had claimed that letters of no confidence already being submitted against the PM and there are calls for Chancellor Kwarteng to resign if pound breaks parity. Elsewhere we also remain cautious on potential downgrade to UK's sovereign rating/ outlook. S&P and Moody's will conclude their rating review by 21 Oct while Fitch will conclude by 9 Dec. A downgrade to outlook/rating will undermine GBP. Pair was last at 1.0750 levels. Bearish momentum on daily chart intact while RSI shows signs of turning from near oversold conditions. Technical rebound risks not ruled out though bias remains for sell rallies. Support at 1.0350 (low intra-day), parity levels. Resistance at 1.08, 1.10 levels.

- **IndoGBs** stabilised in the afternoon from the morning sell-off on Monday; the 10Y yield (FR91) was up by around 8bp on the day, with the domestic bond outperforming the 10Y UST. Today's conventional bond auction has an indicative target of IDR19trn and a maximum target of IDR28.5trn; upsize is unlikely unless demand comes in exceptionally strong, although funding raising appears to be slightly behind schedule. We expect the 10Y IndoGB to hold up with yield in the range of 7.30-7.40% near-term. Foreign holdings of IndoGBs fell to IDR741.66trn or 14.67% of outstanding as of 23 September, after six days of consecutive outflows.



Source: Bloomberg, OCBC

- **CNY and CNH points.** Onshore CNY FX points fell while offshore CNH DF points edged up upon the reimposition of the 20% FX risk reserve requirement. The gap between the 12M CNY and CNH points widened to around 430pips from 300pips before the announcement, with the adjustment falling mostly on the onshore curve. The 20% FX risk reserve requirement would add a few hundred pips to the cost of forward positions which mean a higher effective onshore FX swap curve; for example, at a 1Y USD rate of 4% the cost of 12M forward position would be 570pips higher. The off-onshore gap shall reflect such additional costs and hence we see room for further widening. This widening can be engineered via a combination of lower onshore points – because of reduced demand for RHS positions, and probably smaller drops (rather than further increases) in offshore points – to better align with the "effective" onshore curve, as after all, the bias on the points remain to the downside on CNY-USD rates differentials. In rates terms, the offshore 12M CNH implied rate was at 2.73% and onshore 12M CNY implied rate at 2.16% at the time of writing; these were against onshore 1Y repo-IRS at 2.02%.



Source: Bloomberg, OCBC

- **USD/SGD. Potential Pullback.** USDSGD remains well bid, tracking USD strength and UST yield higher. Pair was last at 1.4350 levels. Bullish momentum on daily chart intact while RSI shows signs of turning from overbought conditions. Not ruling out technical pullback intra-day. Support at 1.4295 (76.4% fibo retracement of 2020 high to 2021 low), 1.4220 levels. Resistance at 1.4360/70 levels (around intra-day high). S$NEER is trading ~1.5% above mid-point.

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