OCBC TREASURY RESEARCH

Daily Market Outlook

12 January 2023

US CPI matters

- The **UST** curve bullish flattened upon a solid 10Y coupon auction. The 10Y bond cut off at 3.575%, 0.5bps below WI level, with the bid/cover ratio edging higher to 2.53x and indirect award higher to 67%. More supply (of bills and coupon) is lining up, with net new cash/issuance planned at USD37.5bn for next week, which will push the debt level nearer the debt ceiling – total public debt subject to limit stood at USD31.32trn as of 9 January versus ceiling at USD31.38trn. Market watch when the US Treasury's extraordinary measures will be triggered. Meanwhile, liquidity will be tightened as the US Treasury rebuilds TGA. Nearer to us is apparently US CPI tonight. Consensus looks for a marked deceleration in the headline to 6.5% YoY, primarily based on easing goods price inflation which should have been in part due to lower energy prices; there might also have been a further stabilization in core services inflation. Risk for the rates market surrounding the CPI print appears balanced, as a deceleration in inflation is already expected. Fed Funds futures pricing of 50bps of hikes in Q1 also looks fair – our base case is a 25bps hike each at the February and the March FOMC meetings.

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- **DXY. Waiting for Cues**. The US CPI report tonight (930pm SG time) remains the highlight. Consensus expects headline CPI to slow to 6.5% YoY, down from 7.1% and core CPI to slow to 5.7% YoY, down from 6%. Another deceleration in price pressures would add to speculations that the Fed could again cut back on its pace of hike to 25bps (from 50bps hike at December FoMC) at the upcoming FoMC (1 Feb). This can support risk sentiment while the USD could come under renewed pressure. A decisive break below 103-support for DXY could trigger more USD decline against Asian FX. However, the risk of any unexpected uptick in CPI may un-nerve sentiments and temporarily lend support to the USD. On Fed speaks, Collins said she leans towards supporting 25bps hike at upcoming FoMC as smaller move gives Fed more time to assess data. DXY traded a touch softer overnight; last at 103.20 levels. Mild bullish momentum on daily chart faded while RSI turned lower. Risks remain skewed to the downside. Next support comes in at 103, 102.15 (50% fibo retracement of 2021 low to 2022 high). Resistance at 104.15 (21 DMA), 105.1 and 106.20 levels (50, 200DMAs death cross). Beyond US CPI, the University of Michigan consumer sentiment data on Friday will also be closely watched. Consensus is looking for a 3rd straight improvement (expectations at 60.5 vs. 59.7 in December). Consumption has held up relatively well as the strong labor market continues to boost sentiment and incomes. Both 1- and 5-year inflation expectations are also seen steady at 4.4% and 2.9%, respectively.

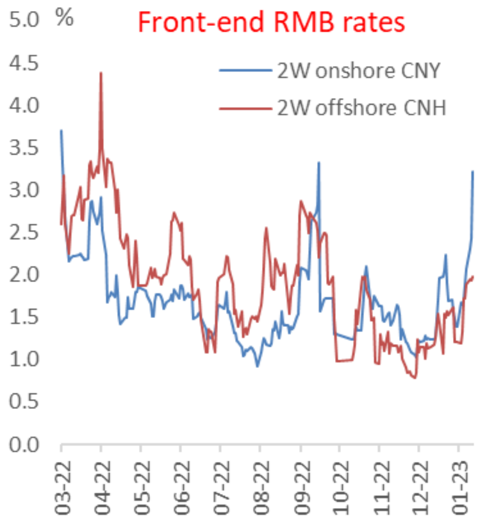
Source: Bloomberg, OCBC Research

- **EURUSD. Further Moves Hinge on US CPI.** EUR inched higher amid hawkish ECB speaks, that seem to suggest no let-up in tightening to arrest inflationary expectations. Rehn said increases in interest rates must still rise significantly to reach levels restrictive to ensure a return to 2% medium term target while De Cos said the ECB will deliver big increases in borrowing cost at next meetings. Earlier this week, Centeno said that increases in borrowing costs must persist until inflation is on a sustainable path to 2% target. He said there is no alternative that to carry out the process of normalisation and increasing interest rates that started at end-2021. Schnabel said that rates will still have to rise significantly at a steady pace to reach levels that are sufficiently restrictive to ensure a timely return of inflation to ECB's 2% medium-term target. EUR was last at 1.0760 levels. Daily momentum is not showing a clear bias while RSI is rising. Sideways trade likely with risks skewed to upside. US CPI tonight a key event risk for USD and would have impact on other FX, including the EUR. Resistance at 1.0750 levels (61.8% fibo retracement of 2022 high to low, trend upper bound). Decisive break-out of 1.0750 should see EUR gather traction. Next resistance at 1.0850, 1.0940 levels. Support at 1.0640 (21 DMA), 1.0520/40 (50% fibo) and 1.0480 (50 DMA).

- **GBPUSD. Golden Cross.** GBP traded a subdued range overnight as markets await outcome of US CPI report tonight. GBP was last at 1.2160 levels. Daily momentum shows signs of turning bullish while RSI rose. Golden cross formed, with 50DMA cutting 200DMA to the upside. Risk modestly skewed to the upside. Resistance at 1.2220 levels. Support at 1.2085 (21 DMA), 1.2050 (50% fibo retracement of 2022 high to low), 1.2020 (50, 200 DMAs). Earlier this week, BoE Chief Economist Huw Pill said that inflationary pressures in UK may be easing as labor market weakens and the economy heads into recession. He added that "should economic slack emerge, and unemployment rise as latest MPC projected, that will weigh against domestic inflationary pressure and ease the threat of inflation persistence.

- **USDJPY. 21DMA Caps Advance.** USDJPY fell in response to Yomiuri report that BoJ will review the side effects of its recent policy changes at its next BoJ MPC (18 Jan). The report also mentioned that they will consider adjusting its bond purchases and make further policy tweaks if it believes they are necessary. The report made no attribution. Basically, the risk of another BoJ move drove demand for JPY. Yesterday we noted that Uniqlo operator Fast Retailing was said to raise Japan salary by up to 40% from March. Similar moves were seen across corporate Japan: Nippon Life Insurance plans to increase salaries of sales reps by ~7% while Suntory will raise wages by 6%. On data release earlier this week, Tokyo CPI was seen inching higher to 4% YoY, up from 3.8%. This ties in with the view of rising likelihood of policy shift if trend inflation overshoots expectations and stay above its 2% target. Japan's "shunto" wage negotiations between labor unions and employers between March and April should provide further information of wage increases. Potentially, some options that the BoJ may consider could be a removal of YCC regime and/or even exit from NIRP. Anticipation of further BoJ moves could see a return of JPY strength at some stage. But in the near term, US CPI data is a key event risk. An unexpected uptick on data point could pose upward risk for USDJPY. Pair was last at 131.70 levels. Mild bullish momentum remains intact while RSI fell. Sideways trade. Resistance at 133.05 (21 DMA) should cap advances while bigger resistance comes in at 134.80 (23.6% fibo retracement of Oct high to Jan low). Support at 131, 130.60 and 129.50. On the weekly chart, bearish momentum remains intact. Price action exhibits a head and shoulders pattern – bearish reversal. A break below 130 support could see losses accelerate towards 127.30 (50% fibo).

- **CNY rates**. The PBoC injected CNY65bn of liquidity via 7-day reverse repos and CNY52bn via 14-day reverse repos this morning. More support is likely in the days ahead, as liquidity appears tight – 1W and 2W implied CNY rates are elevated. As the CNY700bn of MLF maturity comes ahead of the Chinese New Year, a full coverage of the liquidity as a minimum is probably needed – but it is a matter of the use of instruments; if part of the liquidity is compensated for by short-term reverse repos, it would be a disappointment to the market. Back-end CNH points went higher upon the lower US yields; we prefer to stay on the sidelines in view of potential volatility in USD rates around CPI release, with medium term strategy staying as buy-on-dips.



Source: Bloomberg, OCBC Research

- **IndoGBs** continued to fare well on Wednesday, alongside the move lower in USD/IDR. There were some profit-taking flows on bonds in the afternoon ahead of US CPI print. Risk is to the upside for IndoGB yields after the recent bullish sessions while supply is front-loaded in Q1 and MoF appears happy to issue up to target. Next supply is on Tuesday with an expected indicative target of IDR23trn. Foreign inflows slowed on 10 January, with foreign holdings of IndoGBs at IDR774trn, or 14.5% of outstanding.

- **MGS** on the other hand were traded soft on Wednesday with investors waiting for US CPI. The size of the 15Y MGS (reopening) came in on the high side at MYR3bn with additional private placement of MYR2.5bn. We have a steepening bias to the MGS curve amid supply risk, while front-end yields are likely better anchored given they are already ahead of the policy curve.

- **USDSGD. Consolidate.** USDSGD continued to trade with a heavy bias near its recent lows. US CPI tonight (930pm SG time) is a key event risk. Expect some volatility around the release of data. Pair was last at 1.3302 levels. Daily momentum and RSI indicators are flat. Bias still for downside play. Support here at 1.33 levels. Decisive break puts next support at 1.3270, 1.3220 levels. Resistance at 1.3480 (21 DMA, 76.4% fibo), 1.3670 (50 DMA, 61.8% fibo retracement of 2020 low to 2022 high). S$NEER is 1.19% above model-implied mid.

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