OCBC TREASURY RESEARCH

Daily Market Outlook

9 January 2023

Gains in AxJs Accelerate

- **DXY. Volatility to Pick Up**. USD extended losses this morning in early trade. Bullish momentum seems to be picking up pace for KRW, THB, PHP and MYR this morning. Softer US data last Fri triggered a sharp turnaround in the USD. In particular, average hourly earnings decelerated (0.3% MoM in Dec vs. 0.6% prior), ISM services fell into contractionary territories (49.6 in Dec vs. 55 expected), factory orders slumped (-1.8% in Nov vs. -1% expected) while NFP gains of +223k was the smallest since Dec-2020. Softer data suggests that Fed's cumulative tightening in 2022 is starting to have its effects felt on the economy. That said, US labor market remains solid despite a slowdown in hiring. This somewhat supports Fed's hopes for economic soft-landing. This week's CPI data (Thu) would be key for near term USD directional cues. 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 Dec FoMC) at the upcoming FoMC (1 Feb). And this could boost appetite for risk assets while the USD could come under renewed pressure. However, an unexpected uptick may un-nerve sentiments and lend support to the USD. In any case, we should expect volatility to pick up and more 2-way swings on the USD this week ahead of CPI release. DXY last at 103.8 levels. Mild bullish momentum on daily chart intact while RSI turned lower. Sideway trade near recent lows are likely. Key support at 103.40 (recent low). A clean break below this support is required for USD to move another leg down. Next support comes in at 102.15 (50% fibo retracement of 2021 low to 2022 high). Resistance at 104.40 (21 DMA), 105.1 and 106.20/40 (50, 200DMAs).

- **USTs** rallied upon a slew of soft US economic data, in particular the softer-than-expected ISM services index across sub-components. As for the labour market report, hourly earnings growth slowed but payroll came in higher than expected. Market pared back rate hike expectations mildly, seeing the Fed funds rate (upper end) at 4.68% at year-end. Our expected peak Fed funds rate is 5.00%, a tad lower than market pricing and the Fed's dot-plot; but our base-case is for no rate cut this year. As investors pay more attention to the data than Fed's comments, Dec CPI releases on Thursday will be the next driver for bonds and rates.

- Although futures positionings again varied across investors in the week ended 3 January, overall investors were more bullish at the 2Y than the 10Y. Speculators added to net short positions at 10Y Treasury futures but trimmed net short positions at the 2Y; asset managers cut net long positions at the 10Y but added to net long positions at the 2Y. On a multi-month horizon, we have a steepening bias on the yield

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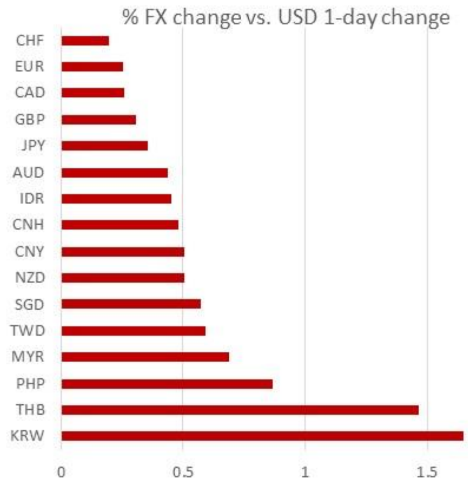
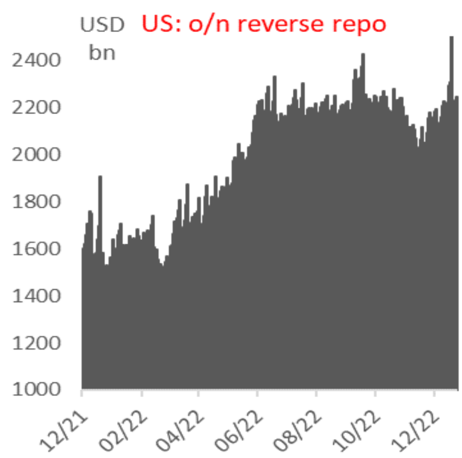
AxJs Gains Power On



Source: Bloomberg, OCBC Research



Source: Bloomberg, OCBC Research

curve. On the liquidity front, USD2.208trn of funds still parked at the Fed's o/n reverse repo facility which gives an interest of 4.3%; the amount is likely to stay around this level in the coming days. US Treasury has planned to pay down a small USD1bn of bills this week. There is unlikely to be a material change in the liquidity situation near-term.

- **EURUSD. Rebound Underway.** EUR reclaimed 1.06-handle on the back of softer set of US data last Fri. Continued decline (down nearly 9% YTD) in European gas prices to pre-invasion levels due to mild weather conditions suggests that inflationary pressures may not be as bad as feared and this could help business to cope better. Pair was last at 1.0660 levels. Mild bearish momentum on daily chart shows tentative signs of fading while RSI rose. Bullish trend channel (formed since Nov) still holds. Golden cross formed (50DMA cuts 200 DMA to the upside). Resistance at 1.0675, 1.0750 levels (61.8% fibo retracement of 2022 high to low, trend upper bound). Break-out of 1.0750 is needed for EUR bulls to follow through. Support at 1.0520/40 (50% fibo) and 1.0410 (50 DMA).

- **GBPUSD. Firmer Footing; Eyes 21 DMA.** GBP reversed losses to trade flat for the week. This comes amid broad USD softness on disappointing US data. Pair was last at 1.2110 levels. Bearish momentum on daily chart shows signs of waning while RSI rose. A bullish engulfing was observed on Fri session while weekly chart suggests potential of rebound. The initial near-term caution that we had been calling for may have ran its course with support at 1.1850 met (low traded on Fri at 1.1842). Immediate resistance at 1.2120 (21 DMA). Decisive break above that could bring back buying momentum. Next resistance at 1.2150, 1.2220 levels. Failure to recapture price action above 21DMA could see GBP re-attempt downside. Support at 1.2050 (50% fibo retracement of 2022 high to low), 1.1960 (50 DMA) and 1.1840 levels (recent low).

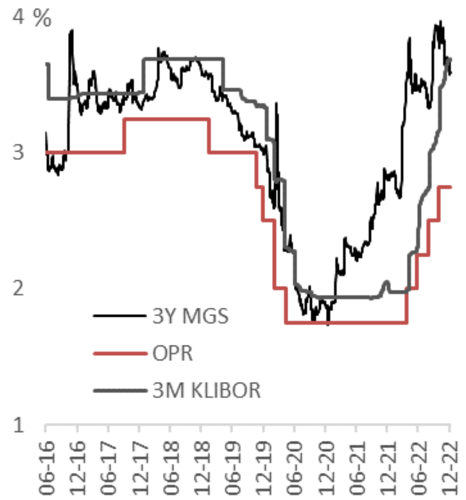
- **USDJPY. 2-Way Trades but Bias to Sell Rallies.** USDJPY traded a high of 134.77 levels last Fri before reversing earlier gains into losses. Softer US data was the main driver fuelling the selloff in USD. Pair was last at 132 levels. Mild bullish momentum remains intact, but RSI fell. 2-way trades likely. Resistance at 133.60 (21 DMA), 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). Last week a Reuters report indicated that BoJ is putting more emphasis on core CPI and will likely raise its projections soon. Report also highlighted that price increases are broadening more than initially expected. This reconciles with earlier observation that recent comments from other BoJ officials seem to suggest rising likelihood of policy shift especially if trend inflation overshoots expectations and stay above its 2% target. We believe Dec's surprise YCC tweak signals the beginning of more to come. Question is on the timing. Some options that the BoJ may consider could be a removal of YCC regime and/or even exit from NIRP. A potential policy shift will lead to JPY strength.

- **AUDUSD. Long Bias.** AUD managed to trade higher for the 3rd consecutive week. Softer US data (raising hopes for Fed policy calibration) and positive development out of China are still the key drivers fuelling AUD upside. AUD was last at 0.69 levels. Bullish momentum on weekly chart intact while RSI rose. A potential cup and handle pattern is observed on weekly chart, and this is typically a bullish formation. Completion of pattern puts textbook objective at around 0.75/0.76 levels. On the daily chart, daily momentum is showing tentative signs of turning mild bullish while RSI rose. We continue to favour a long bias. Next resistance at 0.6920 (76.4% fibo), 0.7020 before 0.7150 (Aug high). Support at 0.6840 (200 DMA), 0.6760/70 levels (21 DMA, 61.8% fibo retracement of Aug high to Oct low) and 0.6680 (50 DMA).

- **USDSGD. Heavy.** USDSGD continued to trade with a heavy bias, taking cues from the decline in USDCNY (breaking below 6.80-handle), USDJPY and softer USD. Pair was last at 1.3320 levels. Daily momentum is mild bullish while RSI is flat. Bias still for downside play but the move down from here could be a slow grind, given the sharp pullback of ~8% since Oct peak. Support at 1.3320/40 levels (recent low). Decisive break puts next support at 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 1.32% above model-implied mid.

- **CNY rates.** The daily OMO amount stayed at CNY2bn, resulting in a net drainage of liquidity of CNY41bn upon maturity. According to this pattern, Tuesday's drainage is likely at CNY62bn. Thereafter, we expect some liquidity provisions towards the latter part of the week or the start of next week. Mid to back-end CNH points rose on lower US yields. While our medium-term strategy for back-end CNH points is buy-on-dips, in view of the potential volatility in US rates ahead of the Dec's CPI print – the falls in yields could mean any reversal can potentially be forceful, we prefer to stay away from CNH points for now. Northbound Stock Connect flows have been relatively heavy in recent days; CNH liquidity is still not a major driver for the points yet, but over the course of the year potential asset swap flows are likely to support our buy-on-dip strategy at the points.

- **MGS** pared back some losses on Fri post MGII auction, with yields ending the day 1-3bp higher. The 10Y MGII (reopening) cut off at 4.147% which was mildly above WI level which already represented some concession into the auction; nevertheless, after cheapening, the bond garnered a decent bid/cover ratio of 2.09x which appeared to be a relief to the market. We remain of the view that front-end MGS shall be better anchored as short end yields and rates are already running ahead of the policy rate curve. 3M MGS yield at 3.6% and 3M KLIBOR at 3.69% are high enough compared to the current OPR at 2.75% and our expectation for the OPR to reach 3.25%. There is unlikely to be a matching increase in KLIBOR upon further BNM rate hikes; we see limited upside to KLIBOR from here.



Source: Bloomberg, OCBC

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