Daily Market Outlook

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Solid 10Y UST auction; BoK on hold

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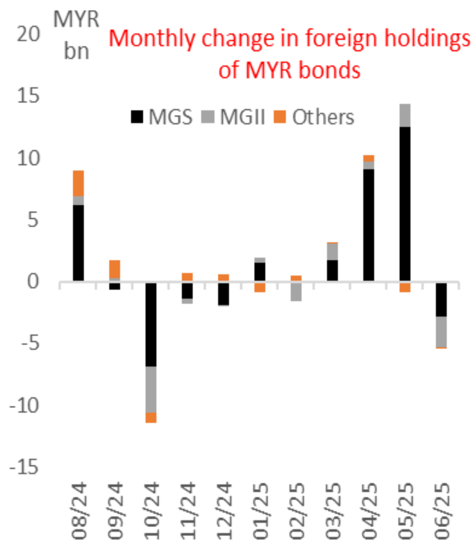
- **USD rates**. USTs rallied overnight with the curve mildly flatter as the 10Y coupon bond auction went well, while the FOMC minutes reinforced expectations for some rate cuts this year. The 10Y bond sales garnered a bid/cover ratio of 2.61x higher versus 2.52x prior and stopped through to cut off at 4.362% despite the richening into the auction, although indirect accepted edged lower to 65.4% which was still decent. The next is the 30Y coupon bond auction tonight. Upon maturity of USD87.6bn, net coupon bond settlement next week is at USD31.4bn which is not a high level. Net bills settlement is at USD15bn next Tuesday and we expect more to come, as US Treasury rebuild its cash position which has been well anticipated given the increase in the debt ceiling. TGA balance was at USD332bn as of 7 July, while the target is USD850bn for end Q3 and end Q4. TGA balance was USD510bn below the peak on 11 February; the falls have been "matched" by overall balance sheet shrinkage, increase in reverse repos (all tenor) usage, increase in note & coins, and increase in bank reserves. As US Treasury replenishes its cash position, we expect bank reserves to fall but to an above-ample level.

- On **FOMC minutes**, while it reflected a divided committee as expected, key quotes include : 1/ "most participants assessed that some reduction in the target range for the federal funds rate this year would likely be appropriate, noting that upward pressure on inflation from tariffs may be temporary or modest, that medium and longer-term inflation expectations had remained well anchored, or that some weakening of economic activity and labour market conditions could occur."; 2/ "a couple of participants noted that, if the data evolve in line with their expectations, they would be open to considering a reduction in the target range for the policy rate as soon as at the next meeting". While these are not fresh pieces of information – we have understood/heard from the June dot plot and subsequent official comments, wordings in the minutes itself appear enough to reinforce current market pricing of two 25bp Fed funds rate cuts while we still see room for a total of 75bps of cuts before year end.

- **MYR rates**. BNM cut OPR by 25bps to 2.75% on Wednesday in line with expectations. MPC statement commented "while the domestic economy is on a strong footing, uncertainties surrounding external developments could affect Malaysia's growth prospects. The reduction in the OPR is, therefore, a pre-emptive measure aimed at preserving Malaysia's steady growth path amid moderate inflation prospects". A rate cut had been in the price, but market had not fully priced in another rate cut after yesterday's one; as such, MYR IRS did react to the dovish MPC statement. 1Y MYR IRS ended Wednesday 6bps lower while longer tenor IRS were mostly 1-2bps lower. 3Y and 5Y MGS yields were 2-3bps lower on the day, as the spreads between yields and OPR had already been compressed. 3M KLIBOR was fixed lower by 24bps at 3.23% this morning; 3M KLIBOR-OPR spread was last at 48bps. OCBC economists maintain expectation for one more 25bp cut in the OPR before year-end. MGS/MGII saw outflows of MYR5.3bn in June: 1/ after the hefty inflows of MYR14.3bn in May and of MYR9.7bn in April, there might have been some profit-taking; 2/ asset swap pick-up narrowed; 3/ the sell USD theme subsided somewhat in June. Malaysia has a local currency credit rating of A (S&P)/ A3 (Moody's), while MGS are included in key bond indices including FTSE Russell's WGBI and GBI-EM. Despite some daily/monthly fluctuations in flows, MGS stands to benefit from inflows including those diverted from USD assets.



Source: CEIC, OCBC Research

- **KRW rates**. Bank of Korea kept its policy Base Rate unchanged at 2.50% this morning in line with expectations. The decision was unanimous. The policy guidance at the MPC statement has remained similar to that at the last statement noting "the Board will maintain its rate cut stance to mitigate downside risks to economic growth" and "adjust the timing and pace of any further Base Rate cuts". Today's Statement opined that "as risks associated with the housing market in Seoul and its surrounding areas and with household debt have increased, it is necessary to assess the effect of the macroprudential policies". This had been precisely seen as the reason for today's status quo decision. Four out of the 6 members are open to rate cut in the next three months, while the other two see "great chance" of hold in the next three months. Rhee opined there is a need to maintain easing policy. We keep two additional 25bp cuts this year in our forecast profile, but the BoK would likely want to see some impact of recent macroprudential policy. KRW IRS were offered down 1-5bps thus far this morning, taking cue from the USD rates market and as BoK maintains easing stance.

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