Daily Market Outlook

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USTs in consolidation mode

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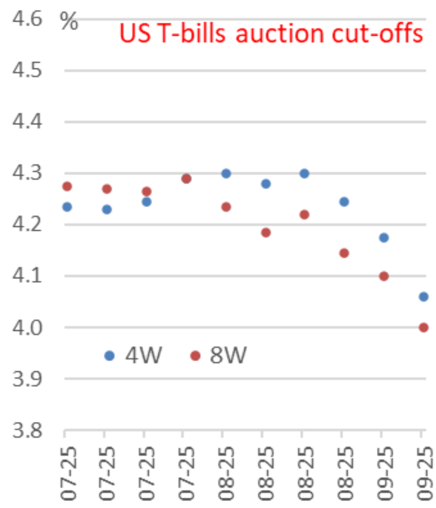
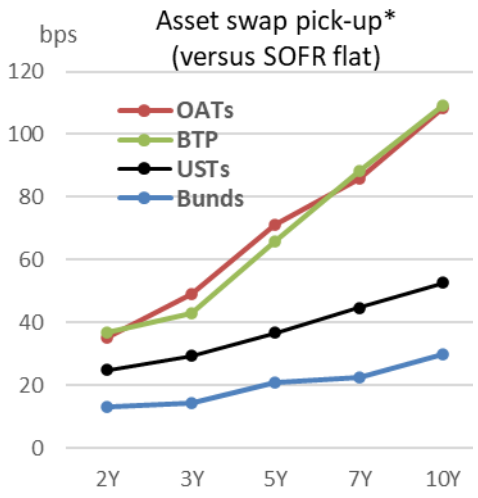
- **USD rates**. UST yields initially dipped upon CPI and jobless claims releases, before rebounding to end the day little changed. A confluence of factors suggest USTs are supported around current yield levels. August CPI came in mostly as expected, labour market data point to a continued softening, and demand at this week's coupon bond auctions was solid. Headline CPI MoM printed a tad higher than expected, mainly driven by the index of shelter, while the food index in particular the food at home index showed larger increases than in the previous months. Nevertheless, core CPI inflation at 0.3%MoM was in line with expectation, and the core services indices showed some marginal easing in price pressure. Overall, the outcome reinforces market expectation for the Fed to resume rate cuts next week. Fed funds futures continued to price 28bps of cut at the September FOMC meeting, and a total of 72bps of cuts for this year. Bond market instead reacted to the jump in initial jobless claims, with the 10Y yield dipping below the 4% market briefly for multiple times driven by real yield, and the yield was last at 4.028%. Overnight's 30Y coupon bond auction was well received, garnering a bid/cover ratio of 2.38x versus 2.27x prior, with indirect accepted slightly higher at 62.0% versus 59.5% prior. At bills auctions, the 8W bill sales drew bid/cover of 2.81x, with cut-off 10bps lower compared to previous auction, at 4.00% as investors tried to lock in such yield. Now given August CPI is out of the way, 2Y UST is likely to consolidate around the yield level of 3.50-3.60%, while range for the 10Y is seen at 4.00-4.15%, as investors await FOMC decision next week together with the updated dot-plot.



Source: Bloomberg, OCBC Research

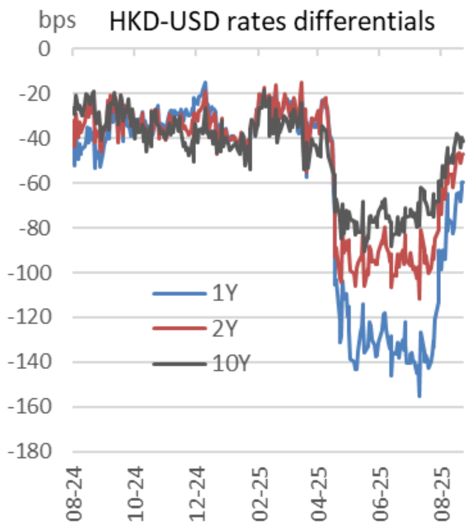
- **EUR rates and EUR**. ECB kept the three key ECB interest rates unchanged as widely expected. The central bank revised upward GDP growth and inflation forecasts for 2025 and 2026. Lagarde, while remaining non-committal, elaborated on what she meant by "in a good shape". She said, "we continue to be in a good place, but we are not on a predetermined path and we will take stock, meeting-by-meeting, to look at all the data – the outlook, the projections – that we receive in order to make sure that we stay in a good place." At the margin, we interpret it as Lagarde not ruling out another rate cut, but it does not look like to be the central bank's base-case. We still have one final 25bp cut in our forecast profile, which is a close call. Regardless, the ECB is seen at or nearing the end of the easing cycle. Relative value in EUR remains attractive against the dollar especially under our views that the USD is likely to trade softer in the remainder of the year. Resistance for the pair is at 1.1750, 1.1830 levels; support sits at 1.1650/60 levels and 1.1570. On bond side, Bunds appear to be lacking impetus to rally especially when OATS have stabilised of late. In terms of asset swap, pick-up was last at around SOFR+30bps at 10Y Bunds, at around SOFR+108bps at both 10Y OATS and 10Y BTP. ASW pick-up at 5Y OATS at around SOFR+73bps is wider than that at 5Y BTP at around SOFR+65bps. Investors may start to see some relative value at OATS especially if sentiment continues to stabilise.

- **HKD and CNH rates**. HKD IRS continued to underperform USD OIS, which pushed HKD-USD rates spreads higher (less negative), in line with our directional view. At current spread levels, however, we prefer to turn neutral. First, a fair amount of dovishness is already reflected in USD OIS. Second, with spot t/t at current level and the softer USD bias, any further liquidity drainage is seen as not being near, while the risk of liquidity injection does not appear imminent either. Third, on the other hand, inflows into HKD assets will prevent liquidity from loosening materially. There have been relatively big amounts of net-buy under Southbound Stock Connect – a whopping HKD19bn on Thursday, bringing month-to-date amount to HKD87bn, versus HKD112bn for the whole of August. These inflows are keeping CNH rates anchored at the same time, but we see limited downside to short-end CNH implied rates and CCS as onshore short-end CNY rates appear floored at 1.50% level for now before the next outright interest rate cut, while there is no yield premium in offshore CNH rates.



Source: Bloomberg, OCBC Research

*10 September



Source: Bloomberg, OCBC Research

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