GLOBAL MARKETS RESEARCH

Daily Market Outlook

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FOMC Likely Remains Divided Post-CPI

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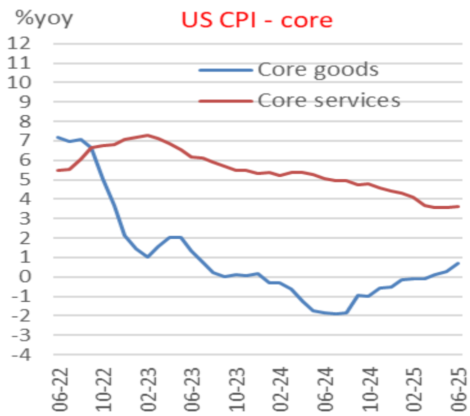
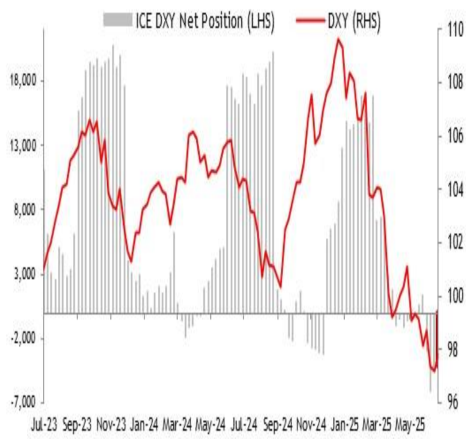
Global Markets Research and Strategy

- **USD rates**. UST yields rose on the CPI report, which showed core goods price inflation accelerated. Yields initially dipped as core CPI MoM printed a tad below consensus, but that reaction was brief. Yields rebounded as breakdown suggested there was some passthrough from tariff, with core goods inflation picking up to 0.70%YoY, after having emerged from deflation since April. Subsequently, Fed funds futures pared back rate cut expectation to 43bps for this year, with the chance of a 25bp cut by the September FOMC meeting now seen at 56%. On a month-on-month, seasonally adjusted basis, the CPI report was more mixed: indexes for used cars, trucks, new vehicles, and airline fares were among the major indexes that decreased in June; price of shelter was relatively tame at 0.2%MoM versus 0.3% in May. The latest CPI prints support the wait-and-see camp within the Committee but are unlikely to shift the stance of the dovish camp much, i.e. the FOMC is likely to remain divided. Our base-case has been for three cuts (25bp each) this year and one cut in 2026, versus market pricing of roughly two plus two cuts – hence the difference in views is essentially on the timing of expected cuts. Terminal rate is commonly seen at 3.25-3.50% level. The reaction in USTs to the CPI prints is likely done. With impact of tariff generally seen as one-off, 10Y breakeven at 2.4% appears on the high side. Near-term range for 10Y UST yield stays at 4.34-4.52%.

- **DXY. *PPI in Focus***. USD extended its bullish run higher, with JPY, EUR, CHF and PHP the main underperformers. US CPI report was a trigger as USD shorts bailed. While the June core CPI print was slightly softer than estimates, the devil was in the details – which explained why the USD fell at first on data release but subsequently rebounded sharply after scrutinising the details. Several tariff-sensitive categories within core CPI – apparel, housing furnishings, auto parts, recreation goods – saw higher prints. This stoked the first signs that tariffs may be starting to show up in consumer prices, especially for goods. Markets will continue to question whether the disinflation trend in US is stalling, especially when considering the likely positive passthrough into core PCE. Adding to the mix, the Empire Manufacturing survey surprised to the upside (5.5 vs. -9.2 expected) with broad-based strength, further reducing the urgency for rate cuts. Markets now implied



Source: CEIC, OCBC Research



Source: Bloomberg, OCBC Research

about 43bps of cut for the year (vs. about 48bps cut before CPI was released), lending support to the USD and bear in mind, we still have PPI data tonight, retail sales tomorrow and Uni. of Michigan data on Fri. Hotter print may well see USD short facing another round of squeeze. DXY was last at 98.55 levels. Bullish momentum on daily chart intact while RSI rose closer to overbought conditions. Resistance at 98.80 (50 DMA), 99.60 levels (23.6% fibo retracement of 2025 high to low). Support at 97.60/80 (21 DMA), 97.20 levels.

- **EURUSD.** ***Another French Political Risk?*** EUR fell amid broad USD strength, as US core goods CPI rose. This is despite European data coming in firmer than expected – ZEW survey, industrial production. EUR was last at 1.1610. Bearish momentum on daily chart intact while the decline in RSI continued to slow. Risks somewhat skewed to the downside. Next support at 1.1540, 1.1490 levels (50 DMA). Resistance at 1.1670 (21 DMA), 1.1830 levels. French PM Bayrou outlined his first budget yesterday, proposing to freeze most public spending, scrapping 2 public holidays (Easter Monday and end of WW2 in Europe) but defence spending will increase. French budget deficit was 5.8% of GDP (almost double EU's official limit of 3%). The proposal met with disagreement from the left-wing parties and far-right party. Detailed budget bill is likely to go to parliament in October and failure to convince opposition parties to support his proposal is more likely than not to see PM Bayrou face a no-confidence motion then. To recap, a similar no-confidence motion saw the exit of former PM Barnier last year. This is one risk to watch for implication on EUR.

- **USDJPY.** ***Near Term Election Risks.*** USDJPY continued to trade higher, driven by higher UST yields (due to US CPI report) and Upper House election uncertainty. Recent poll by Nikkei, Kyodo, Asahi shows LDP-Komeito coalition is at risk of losing Upper House election. A total of 125 seats are up for grabs in the July 20 election. These include half of the seats in the Diet chamber and one for the Tokyo electoral district that has become vacant. The coalition held 141 Upper House seats before the campaign started, and 66 are being contested. Securing 50 seats will give the coalition a majority of 125 in the Upper House (i.e. they can afford to lose 16 seats). Nevertheless, seats lost in the Upper House can affect Ishiba administration. On the contrary, if PM Ishiba manages to get past this election, then it will be another 3 years before the next major election in Japan (excluding the election for LDP President in 2027). For now, the struggle in the Upper House has resulted in pledges of spending hikes and tax cuts in attempt to shore up votes. Moody's has earlier warned that election results may impact fiscal health and ratings. This temporarily weighs on JPY. USDJPY was last at 148.90 levels. Bullish momentum on daily chart intact while rise in RSI shows tentative signs of turning lower near overbought conditions. Next resistance at 149.40/70 levels (200 DMA, 50% fibo retracement of 2025 high to low). Support at 147.15 (38.2% fibo), 146.20 levels.

- **USDSGD. *Consolidation.*** USDSGD continued to drift higher amid broad USD bounce. Last at 1.2850 levels. Daily momentum is mild bullish while RSI rose. Consolidation still likely. Resistance at 1.2860 (50 DMA), 1.2910 levels. Support at 1.28, 1.2750 levels. S$NEER was steady near upper bound; last at ~1.94% above our model-implied mid. From a trade weighted point of view, there may be limited room for SGD to appreciate against trade peers, but due to SGD's safe haven characteristics, S$NEER may still stay near upper bound for now. On upcoming MAS MPC in July, we reiterate our view that we believe MAS can afford to wait and monitor, rather than ease for a 3rd consecutive time after 2 back-to-back easing in first half this year. The last time in the last 10y when MAS did back-to-back easing to reduce to zero appreciation was during COVID in Mar-2020 and Apr-2016 global growth slowdown. But this time SG growth had surprised to the upside. That said, there may still be room for further easing at later MPCs in Oct or Jan-2026 should growth and inflation dynamics worsen more materially. Taking stock, YTD core inflation averaged 0.65%. Vs. MAS projection for 0.5-1.5%. MAS-MTI joint statement noted that imported inflation should remain moderate. Domestically, enhanced government subsidies for essential services are likely to dampen services inflation.

- **CNY rates**. PBoC continued to inject liquidity to the market amid tax payment seasons. Net injections via daily OMOs amounted to CNY737.bn from Monday to Wednesday. Although MLF maturity drained CNY100bn, net injection via outright reverse repo is at CNY200bn thus far this month (CNY1.4trn gross injections versus CNY1.2trn maturity). CGB yields and repo-IRS continue to trade in narrow ranges, showing little reaction to economic data yesterday. Our China Economist noted that "the room for more aggressive rate cuts may be limited given the bottleneck faced by the economy". For the market, while PBoC stays supportive of liquidity, it is still in reaction to market liquidity need. Room for further rallies in rates and bonds appears limited, with the 1.4% OMO reverse repo rate setting an interim floor for now. In offshore, short-end CNH CCS traded a tad higher on Tuesday, while long-end CNH CCS traded softer on expectation on some issuance-related flows. We suspect near-term issuance-related flows may not be as big as thought, while front-end CNH rates are still likely to stayed anchor supported by Connect flows. Bias is for the CNH CCS curve to steepen back.

- **HKD rates**. FX intervention was triggered overnight/early Asia morning. HKMA bought HKD14.829bn worth of HKD from the market, thereby draining the same amount of liquidity from the interbank market. Aggregate Balance will fall to HKD86.4bn on 17 July. HKD IRS were paid up by 3-6bps at open this morning, mostly following USD rates thus far. Front-end HKD rates may be more responsive to the latest round of FX intervention, as Aggregate Balance adjusts to a lower level. Market is also pricing in higher HKD rates ahead. T/N was trading a tad higher at -8pips versus -9pips prior but the carry is still appealing. We continue to see chances of repeated FX interventions pushing HKD rates higher and expect benchmark 3M HIBOR to normalise back to 2.0-2.5% area as the first target. We maintain an upward bias to HKD-USD interest rates differentials.

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