Daily Market Outlook

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September FOMC is Live

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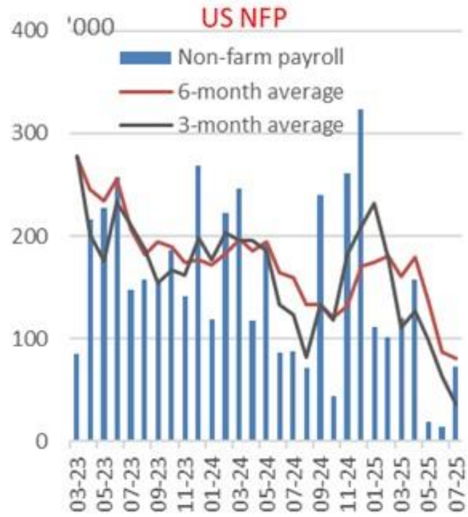
- **USD rates**. UST yields plunged on the payroll report, in a steepening manner as market added back to rate cut expectations. Fed funds futures last priced an 82% chance of a 25bp cut at September FOMC meeting, a total of 58bps of cuts this year and 72bps of cuts in 2026. July payroll came in weak at 73K, while the figures for the previous two months were revised downward substantially, to 14K for June and 19K for May; these leave three-month average at 35K and six-month average at 81K, well below those for most of the months in the 2013-2019 period to which we like to make comparison when the Fed funds rates were at or below 2.5% then. Under the separate household survey, unemployment rate edged back up to 4.2% which itself was the highest since October 2021; underemployment rate was higher at 7.9% versus 7.7% prior. July ISM manufacturing printed weak at 48 points, with employment particularly weak at 43.4 point while prices paid and new orders also printed a tad lower than expected. We mentioned last Thursday that Powell said if the risks to the two mandates (inflation and employment) were more in balance, that would imply that policy shouldn't be restrictive – and our take was "the bar for a rate cut is not necessarily high". Now the risk appears at least in balance, if not skewed to the downside risk in the labour market. Our base-case remains for a total of 75bps of cuts this year, followed by one 25bp cut in Q1-2026, versus market pricing of a total of slightly more than five cuts (assuming 25bps each) between now and end-2026. 2Y UST yield at 3.69% appears mostly in line with current market pricing of rate cuts – although this is slightly more dovish than our base-case, the valuation does not look overly stretched. We expect consolidation for 2Y UST yield. On the other hand, the fall in the 10Y UST yield was driven by both lower breakeven and real yield; we see a small downside room to both components on a multi-month horizon.



Source: Bloomberg, OCBC Research

- **DXY. *In Consolidation Following the Sharp Drop.*** USD turned sharply lower on release of payrolls report last Fri. Most USD/Asean FX was also trading lower this morning, catching up on the USD pullback. THB, PHP and MYR gained over 1% vs. USD. US NFP headline print of 73k missed expectations (104k) while downward revisions for the last 2 months (-258k) caught markets by surprise. Nevertheless, this alongside the slump in ISM employment (43.4) point to softening labour market. Markets were just positioning for a potential return of US exceptionalism trade, but the soft labour market print suggests that the return of US exceptionalism trade may well be a back burner. Fed fund futures are now suggesting that a Sept rate cut should not be ruled out. Focus this week on ISM services data (Tue); initial jobless claims (Thu) and Fedspeaks. DXY was last at 98.80 levels. Bullish momentum shows signs of fading while RSI fell. Risks skewed to the downside. Support at 98.30 (21, 50 DMAs), 97.20 levels. Resistance at 100 (100 DMA), 100.50 levels.

- **GBP rates**. We expect the Bank of England to cut its Bank Rate by 25bps this week, notwithstanding the pick-up in June inflation as the Bank is likely to put more focus on the cooling labour market. Bailey recently opined pay rises are possibly less than they would have been if the NICs change hadn't happened – this has been our view as we earlier wrote "the increase in employer NICs may lead firms to contain pay increase to partly offset the impact on their costs." We expect the central bank to stick with a gradual and careful approach, in view of upside risk to inflation and inflation expectations, before signs showing that the labour market weakens at a more rapid pace. After this week's expected rate cut, we have one more 25bp cut for Q4-2025 in our forecast profile. GBP OIS fully price in this week's expected cut, and price a total of 54bps of cuts for the rest of the year (including this week's), which looks fair to us. We continue to see the 10Y Gilt being supported at current bond/swap spread level.

- **USDJPY. *Sell Rally Intact.*** USDJPY turned sharply lower as US payrolls underwhelmed while Finance Minister also commented on FX moves after the pair rose above 150-levels. Specifically, he said "the government is deeply concerned about trends in the currency market, including speculative movements" and that "it's important for exchange rates to remain stable, reflecting economic fundamentals". Earlier on Fri, USDJPY had traded a high of 150.92 after BoJ Governor Ueda's press conference lacked hint on timing of next rate hike. "Right now I don't see us being behind the curve. Neither do I think there's a high risk we'll fall behind... We don't see the fog suddenly lifting over trade, despite progress made through the US-Japan deal". Pair was last at 147.70. Mild bullish momentum on daily chart is fading while RSI fell. Near term consolidation; bias still to sell rallies. Support at 147.10/40 levels (21 DMA, 38.2% fibo), 145.60/80 levels (50, 100 DMAs). Resistance at 149.40/70 levels (200 DMA, 50% fibo retracement of 2025 high to low), 151 levels (recent high). We continue to look for BoJ to hike rate at some point later this year. Political uncertainty (referring to PM Ishiba's political career/ LDP leadership), credit rating concerns (dependent on fiscal health) and carry allure may still be somewhat supportive of USDJPY but "sell USD" trade momentum can negate.

- **USDSGD. *Continue to Track USD Closely.*** USDSGD turned lower, after hitting 1.30 briefly on Fri. Decline in USDSGD took cues from decline in USD. This is consistent with our view that USDSGD will revert to tracking USD, given significant correlation between USDSGD and DXY (30d rolling correlation significant at ~0.97) and other external/macro events. Pair was last at 1.2870 levels. Bullish momentum on daily chart shows sign of fading while RSI turned lower from near overbought conditions. Support at 1.2830 (21, 50 DMAs), 1.2760 levels. Resistance comes in at 1.30 (100 DMA). S$NEER was steady at around +1.9% above our model-implied midpoint.

- **CNY rates**: OMO reverse repo maturity continues to be heavy, as PBoC rolled over liquidity provisions in recent weeks. Separately, NCD maturities amount to more than CNY3trn each this month and next, which needs to be digested when foreign interests may stay subdued at current pick-up levels. PBoC is likely to stay supportive of liquidity. This morning, it did CNY544.8bn of daily OMO reverse repos, thereby net injecting CNY49bn of liquidity. That said, short-end repo-IRS may still be floored at around 1.5% level for now, given the 1.4% OMO reverse repo rate. As OCBC China Economist pointed out, "in contrast to the April 25 Politburo meeting, which explicitly referenced timely RRR and interest rate cuts, the latest communiqué made no mention of further outright rate cuts. While this does not preclude future rate cuts, it suggests that the sense of urgency has eased". CGBs may undergo a period of consolidation, before signs of a stronger economic recovery, but a sustained rally in long end bonds appears unlikely. Data to watch this week include exports-imports trade, and PPI and CPI for July.

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