Daily Market Outlook

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FOMC decision this week

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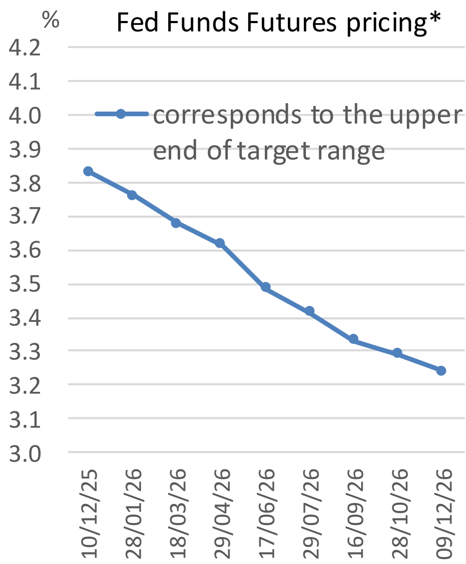
- **USD rates**. UST yields rose for a second day on Friday, as investors adjusted positions ahead of FOMC decision this week. September PCE price indices were in line with expectations, with headline ticking up to 2.8%YoY vs 2.7% prior and core easing slightly to 2.8%YoY vs 2.9% prior. There are a few things to watch on FOMC decision day.

  First, the rate decision itself (and the vote split). Our base-case is the target range for the Fed funds rate will be cut by 25bps to 3.50-3.75%, as data and survey have continued to point to a cooling labour market. Fed funds futures last priced an 95% chance of a 25bp cut this week. While there have been both dovish and hawkish comments from Fed officials, the balance appears to suggest enough votes for a 25bp cut decision.

  Second, the updated dot-plot. Investors may look beyond the December FOMC meeting and forward to 2026. We have been of the view that 2026 market pricings of Fed funds rate cuts were overly dovish; market has pared back 2026 expectations over recent days, to the latest 59bps, versus 67bps priced last Wednesday. This is still more dovish than our base-case of 25bps. The updated dot-plot will shed more light on the Fed funds rate path ahead. If there is any further pushback on 2026 rate cut pricings, then 2Y UST yield may test 3.60%.

  Third, balance sheet policy. We expect an announcement on asset purchase some time in Q1-2026, instead of as imminent as at this week's meeting. First, bank reserves are expected to rise upon liquidity released from TGA. Second, there is room for SRF usage to pick up further – facility limit of USD500bn versus usage at below USD50.35bn thus far, which will then mitigate the upward pressure on funding rates. Further out, there is very likely to be a resumption of asset purchases (expected to be mainly T-bills) to ensure an ample level of reserves as other liabilities on the Fed's balance sheet may grow (thereby "displacing" bank reserves) and/or underlying demand for reserves may increase over time.

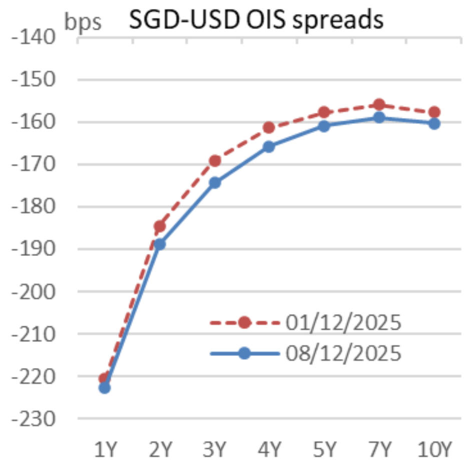
- **AUD rates.** RBA is widely expected to keep its Cash Rate on hold at 3.6% this week, extending the pause after the August policy rate cut. The notion that the next move from the RBA is a hike rather



Source: Bloomberg, OCBC Research
*8 December

than a cut has gained traction. RBA Governor Bullock commented last week that "projections still see inflation coming back down…but obviously we're alert to the possibility that there might be inflation pressures building, and the board would respond accordingly". Cash rate futures priced more than an even chance for a 25bp hike by mid-2026, and a hike is fully priced by August 2026. Key to watch is policy guidance in the RBA statement. Interest rate assumptions under RBA's economic forecasts are based on market pricings. With market pricing having turned more hawkish, that may feed back onto the central bank's GDP and inflation forecasts – there will not be forecast updates at this week's meeting though. As of now, RBA projections still see inflation coming back down. It looks premature to price in rate hikes at this juncture.

- **SGD rates**. SGD OIS movements over the past week broadly tracked USD OIS, with a mild outperformance. SGD OIS traded on the firm side this morning, but with SORA fixing last at 1.1351% on Friday, and implied O/N SGD rate at below 1% level, the upward momentum in short-end SGD OIS may not get stronger near-term. Our forecasts have assumed an upward normalisation in SGD interest rates over time and this view has mostly panned out, but at a more rapid pace than expected. 2Y OIS at 1.46% is around our target level for H1-2026, while 1Y OIS at 1.3% still appears overly stimulus. The liquidity situation and short-end SORA rates fluctuates a lot. Some interim retracements in short-end SGD rates cannot be ruled out. That said, our expectation remains for short-end rates to revert towards the 1.40-1.55% area after dips – if any. There are auctions of 4W, 12W and 36W MAS bills tomorrow. 4W MAS bills cut-off may ease back, with the last cut-off particularly high due to the maturity date – but only partially, as the 4W bills still cross year-end. 12W MAS bills cut-off is expected at 1.40-1.45% as per this morning's market level.



Source: Bloomberg, OCBC Research

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