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Interest Rates Thoughts

Mixed bond performances

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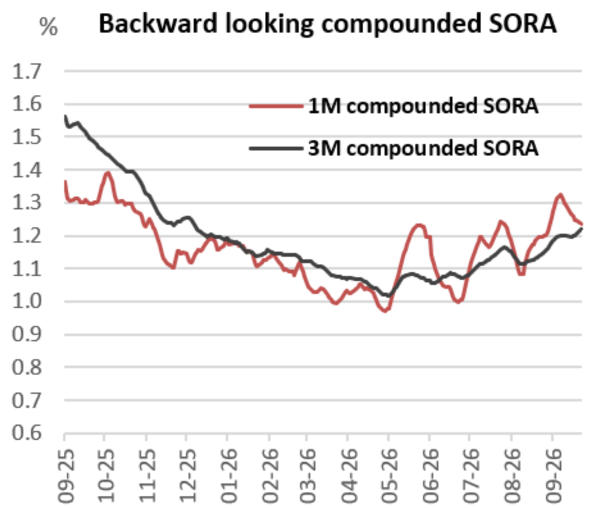
- **DM rates**. Global bonds rallied on lower oil prices, but with different curve dynamics. The gilt curve steepened as market mildly pared back BoE rate hike pricings while the long-end reaction to the QT plan may be done for now with 30Y bond/swap spread at -67bps which was not far away from the high observed in January. As the BoE thus far still see limited second round inflation effect, their monetary policy reaction function, compared to some other major central banks, may be more sensitive to ongoing oil prices developments. The UST curve, on the other hand, flattened further, as market held onto hawkish Fed pricings, while long-end bonds showed some signs of stabilization. Tonight's auction of USD69bn of 2Y UST coupon bond would provide a gauge on investor demand at a 2Y yield which is around 87bps above effective fed funds rate.

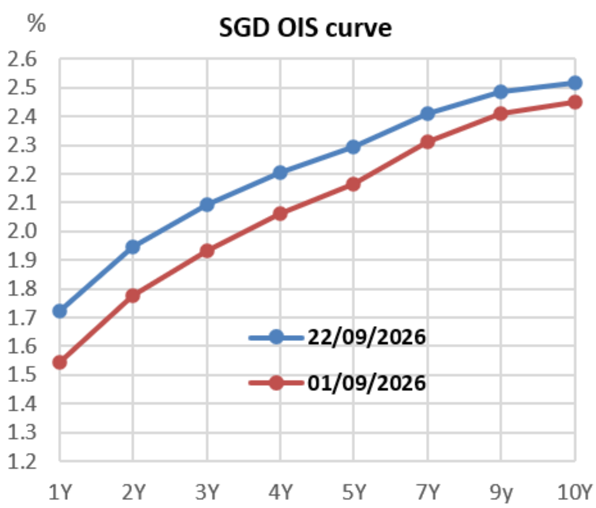
- **SGD rates**. We have recently revised upward SGD rates and SGS yields forecasts higher, to maintain an upward trajectory given our long-held view for upward normalization in SGD interest rates. That said, we are not overly bearish rates, while some interim retracement cannot be ruled out. First, we maintain a downward trajectory in our USD rates forecasts, as market pricing of the Fed funds rate path are already more hawkish than the latest dot-plot suggests. Second, before SORA move up at a more rapid pace, further upward moves in SGD OIS from here may be more gradual compared to the moves which started in July. Third, there is an absence of fiscal concern in Singapore which maintains a triple A rating, while supply is always neutral or supportive as there is room to calibrate supply in accordance with demand.

- On supply, the size of the upcoming 15Y SGS (Infra) will be announced later today. We expect a modest size of around SGD1bn as year-to-date issuances have already been on the high side. Our view of SGS outperformance against swaps, based on expected light supply for the remainder of the year, has mostly panned out. At current bond/swap spread levels, room for further SGS outperformance against swaps has become smaller.

- On SORA, as the overnight rate fluctuates over the days, compounded SORA, albeit being lagging, would provide a clearer picture of the trend. 3M compounded SORA has been trending higher, in line with our upward normalization view. 1M compounded SORA has seen higher lows and higher highs, in line with our expectation for non-linear move. SORA was last fixed at

1.2327% on 21 September, while averaging 1.18% this month thus far. We maintain our expectation for SORA to edge higher to 1.4% level by year-end – still with two-way volatilities. Implied SGD rates, meanwhile, has been on a steadier uptrend, which has driven up MAS bills and T-bills yields. But again, the upward move in bill yields is unlikely to be a one-way train.

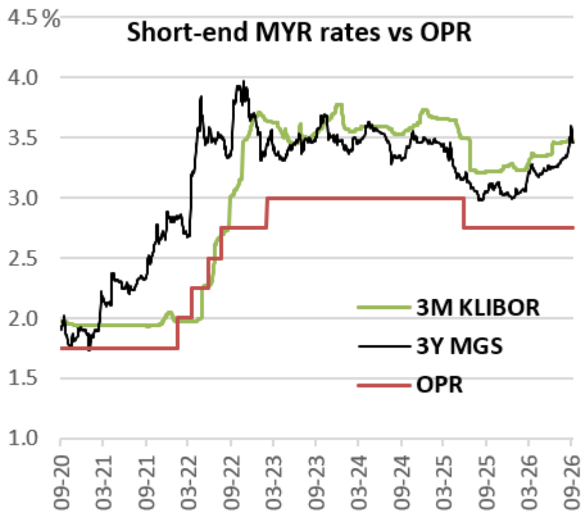


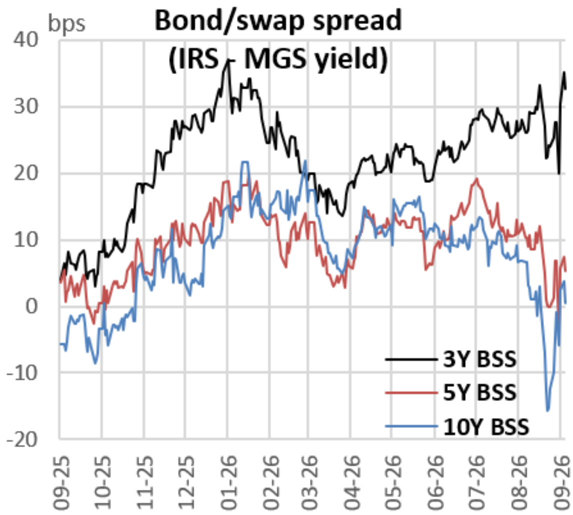


Source: Bloomberg, OCBC Group Research

- **MYR rates**. MGS staged a relief rally last Thursday and Friday, before giving back some of the gains on Monday. From the high levels attained on 15 September, MGS yields have fallen by cumulative 14-24bps across 3-20Y tenors (as of 21 September). Long-end MGS outperformed swaps, as we last opined on 9 September that "the bond/swap valuation starts to look attractive" although we remained cautious. Monday's 7Y MGS auction garnered a bid/cover ratio of 2.17X, with cut-off at 3.999% and the tail mildly wider at 1.6bps. Considering the increases in US yields in the prior trading day, and the intraday volatility in the domestic bonds, the auction result was seen as fair.

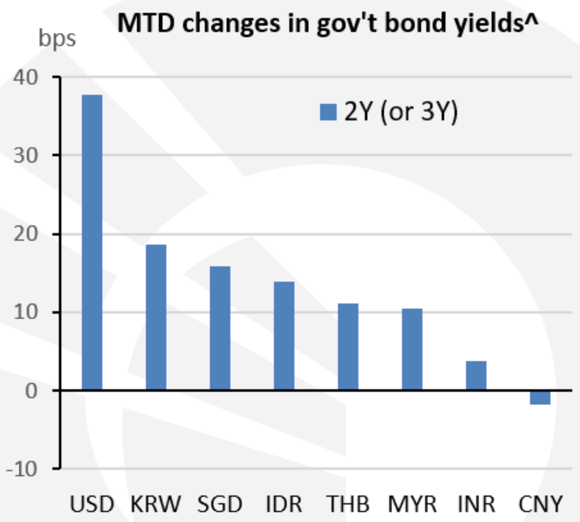
- While MGS may potentially manage to consolidate around current levels, room for rally in MGS is likely small. At the short end, the spread between 3Y MGS yield and OPR at around 70bps is wider than multi-year average; but with a 25bp hike in the OPR being priced on a 3-month horizon, there may not be too much room for the 3Y yield – OPR spread to narrow at current OPR level, i.e. before the hike is delivered. At the longer end, given recent bond outperformances, bond/swap spreads are back up to nearer one-year averages.

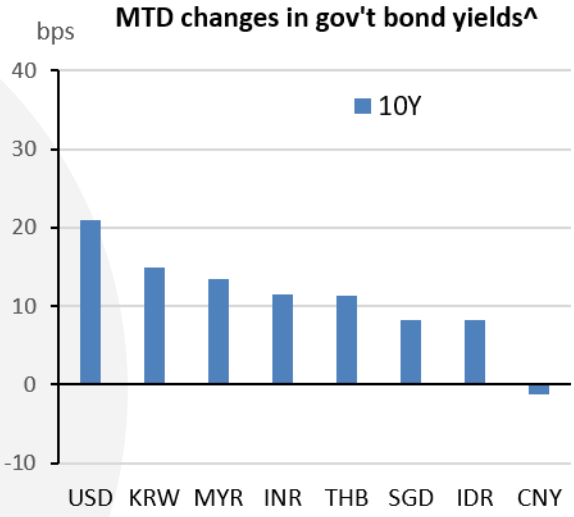




Source: Bloomberg, OCBC Group Research

- **Asian rates**. Month-to-date most Asian local currency government bonds outperformed USTs, especially at the short end, as USD rates rose on hawkish repricing of the Fed policy outlook while idiosyncratic factors have been at play in Asia local markets. At the 2Y or 3Y tenors, the "pass-through" was higher for KTBs, followed by SGS and IndoGBs – still, these yields rose by less than half of the increases in UST yields month-to-date. On the other hand, CGBs even saw yields a tad lower thus far this month, retaining their low corrections with global yields. Looking ahead, if the moves in US yields remain orderly, domestic factors may continue to be the main driver for short end rates in Asia markets. At the longer end, the spillover has been bigger than that at the short end, which is worth monitoring.





Source: Bloomberg, OCBC Group Research
^as of 21 September Asia afternoon; 3Y for KTB and MGS

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