Daily Market Outlook

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Politburo Optimism

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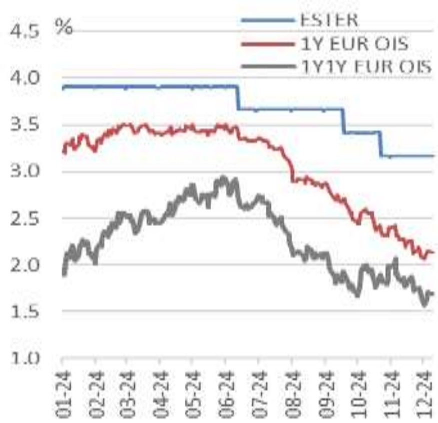
- **USD rates**. The UST curve bearish steepened as market corrected from Friday's reaction to the labour market report. 3M and 6M bill auctions cut off at 4.3% and 4.2% respectively, 10bps and 10.5bps lower than previous cut-offs with the 3/6M spread little changed. Fed funds futures last price an 86% chance of a December 25bp cut. NY Fed 1Y inflation expectation edged up from 2.87% to 2.97% as expected which was not market moving. And precisely, we opined the "uptick in 2Y breakeven suggest that at least part of the potential inflation impact is in the price" of the 2Y bond. We maintain a downward bias to short-end yields. Room for long-end UST yields to fall appears more limited; 10Y breakeven at 2.26% and 10Y real yield at 1.93% are not particularly elevated. Regarding November CPI, headline may have ticked up partly because of base effect; we look for a steady core CPI or ideally some mild disinflation in core services to give the greenlight for a rate cut next week. Further ahead, recent Fed commentaries point to an intention to slow the pace of rate cuts comes 2025, while we have been expecting a slower pace starting 2Q2025. As such, the risk is a pause may come earlier than our base-case – as early as January; we will review the Fed funds rate outlook upon the December FOMC outcome together with SEP and updated dot-plot.

- **EUR rates**. While market has trimmed pricing of a 50bp cut at December MPC meeting, now seeing mostly a 25bp cut – in line with our base-case, overall EUR OIS pricing remains dovish. The EUR OIS curve is very inverted across 1M to 2Y with market looking for a terminal rate well below 2%. Such pricing reflects more of a weak growth/recession driven rate-cutting cycle rather than monetary policy normalization. Our base-case is for a further 100bps of rate cuts between now and end-2025. But risk is for more or quicker rate cuts should the economy weaken by more than expected and should the ECB judge that much lower rates are required to help channel savings into spending and investments. ECB and Lagarde's commentaries will again be scrutinized. Any further market dovishness may be more reflected in the 1Y rate as the 2-3Y rates are more depressed.

- **CNY rates**. Repo-IRS fell by 4bps upon the politburo statement yesterday. Most notably, the monetary policy stance has been

Source: Bloomberg, OCBC Research



Source: Bloomberg, OCBC Research

changed to "moderately loose". Even when the stance was "prudent", there was some monetary easing and hence, the explicit change in the wordings gives high hope for more monetary support to come including outright interest rate cuts. 2Y repo-IRS fell below the 1.5% level that we watched, as we opined "materialization of interest rate cuts is a potential trigger for short-end repo-IRS to break lower". Now, the change in monetary policy stance was dovish enough as a trigger. After initial reaction, market will monitor as to whether fiscal policy is effective in reviving consumption. Fiscal policy is "more proactive" instead of "proactive", reinforcing expectation for more supply to come in 2025. And there will be "extraordinary" counter cyclical adjustments. Against such monetary and fiscal policy backdrop, we have a mild steepening bias to the CGB curve on a multi-month horizon. Market awaits outcome of CEWC. Another focus is on the CNY1.45trn of MLF that matures on 16 December. Chance remains for a near-term RRR cut.

- **USDCNH. *Will China Walk the Talk?*** USDCNH continued to drift lower, thanks to recent news from politburo about ramping up support and also taking cues from daily fixing guidance. Policymakers continue to manage the daily fix, setting it below 7.20 and at times, even lower, when USD was even trading stronger. Fixing pattern suggests that PBoC is doing whatever it takes to not only restraint the RMB from over-weakening but also to guide its bias and direction. Tariff may hurt RMB when it happens but that may be a story for 2025 after Trump inauguration. In the interim, we would keep a look out for the China's CEWC meeting on 11-12 Dec. Expectations are building up for stimulus support after politburo vowed to stabilise property and stock markets. Officials also pledged to ramp up 'extraordinary counter-cyclical policy adjustment' to support the economy and it also announced that it will embrace a "moderately loose" strategy for monetary policy in 2025. Follow-up policy action is crucial, and bear in mind markets are impatient. We caution that any delay in concrete policy action may setup a case for disappointment (again). For now, we remain cautiously hopeful. And that would imply some support for Asian FX, including CNH, KRW, TWD, SGD and MYR. USDCNH was last at 7.2550 levels. Daily momentum turned bearish while RSI fell. Risks are skewed to the downside. Support at 7.2340 (23.6% fibo retracement of Sep low to Dec high), 7.2040 9200 DMA), 7.18 levels (38.2% fibo, 50 DMA). Resistance at 7.27 levels.

- **DXY. *Consolidation.*** USD traded a subdued range overnight in absence of key catalyst. Fedspeaks go into blackout so that puts the focus on data before FOMC next Thu (19 Dec). This week, we have CPI on Wed and PPI on Thu. A 25bp cut is more or less a done deal for Dec meeting unless US CPI unexpectedly surprises a lot to the upside. We would be keen to see the dot plot guidance for

2025. Fed fund futures are implying about 3 cuts for 2025, slightly less than the previous dot plot of 4 cuts that was penciled in for 2025. DXY was last at 106.14. Daily momentum is mild bearish while RSI is flat. Head and shoulders pattern appears to have formed with DXY testing the neckline (which was respected last Fri). This is typically a bearish setup. A decisive break below neckline should see bears gather momentum. Support at 105 levels (38.2% fibo retracement of Sep low to Nov high), 104.60 (50 DMA) and 104.10 (200 DMA, 50% fibo). Resistance at 106.20/30 levels (23.6% fibo, 21 DMA), 106.70 (second shoulder).

- **USDJPY. *Sell Rallies.*** USDJPY traded higher this week after PM Ishiba told parliament that the government is not considering revising a long-standing agreement between BoJ and the government as Japan has not escaped deflation yet. He also added that BoJ's monetary policy doesn't aim to move FX. USDJPY rose to a high of 151.55. Last seen at 151.20 levels. Bearish momentum on daily chart intact but shows signs of fading but rise in RSI slowed. Bias remains to sell rallies. Resistance at 151.30 (50 DMA), 152 levels (200 DMA) and 152.70/80 levels (21 DMA, 23.6% fibo). Support at 150.20 (38.2% fibo), 148.70 levels (100 DMA) and 148.20 (38.2% fibo retracement of Sep low to Nov high). In terms of data releases, there is a few to keep a look out for this week, including PPI on Wed and Tankan survey on Fri before BoJ MPC (19 Dec). But largely, we are looking for BoJ to carry on with policy normalization with a hike next week and into 2025. Recent uptick in base pay supports the view about positive development in labour market, alongside still elevated services inflation, better 3Q GDP (that was released yesterday morning) and expectations for 5-6% wage increases for 2025. The risk is a slowdown in pace of respective policy normalisation, especially if Fed slows pace on return of US exceptionalism. Then USDJPY moves may even face intermittent upward pressure.

- **AUDUSD. *RBA Today (1130am SGT).*** This is the last meeting for the year and the next meeting is not due until 18 Feb. We expect cash rate to remain on hold at 4.35% as services inflation remains sticky and labour market is fairly tight. The risk is an earlier than expected dovish pivot as softer than expected 3Q GDP print last week saw markets shifted expectations to fully price in a cut at Apr's meeting. There were also light chatters if RBA may even need to cut earlier at the Feb meeting. Broadly speaking, tariff worries, slowing growth momentum and anticipation for earlier RBA cuts are some factors that may continue to undermine AUD. However, there may be some factors that could see AUD shorts getting unwound. One of them is 1/ RBA shows little to no change from its hawkish rhetoric, then AUD shorts may be shaken out; 2/ China's CEWC (11-12 Dec) – if fresh stimulus support is announced; 3/ a hotter than expected Aussie labour market report on Thu; 4/ USD reverses lower. AUD was last at 0.6425 levels. AUD was last at 0.6450. Daily momentum is flat while RSI slipped. Near term risks skewed to the downside. Support at 0.6370/80 levels, 0.6350 (2024 low). Resistance at 0.6490 (21 DMA), 0.6560 levels.

- **EURUSD. *Short Squeeze Not Ruled Out as ECB Pricing Aggressive.*** EUR traded little changed. Last at 1.0560 levels. Daily momentum is mild bullish but rise in RSI slowed. Price pattern shows a classic formation of an inverted head & shoulders pattern, which is typically associated with a bullish reversal. Neckline comes in at 1.0610/20 levels. Break-out puts 1.0670 (38.2% fibo) within reach before next resistance comes in at 1.0750/75 levels (50 DMA, 50% fibo). Support at 1.0540/50 levels (23.6% fibo, 21 DMA), 1.0460 levels. This week, EUR may continue to see more volatility. On Wed, German Chancellor Scholz is expected to call for a vote of confidence and the Bundestag will vote next Monday on 16 Dec. To survive the vote, Scholz would need to receive the support of an absolute majority of 367 votes. But in the event, he fails, then Germany is likely to make way for elections on 23 Feb 2025. Far-right AfD is calling for Germany to leave the European Union, the EUR and Paris climate deal as the party prepares for early elections in Feb-2025. The concern here is the explicit language to quit EU unlike its manifesto ahead of the European parliament elections previously in Jun-2024. On Thu, ECB meeting takes centre stage. Markets have already reduced bets for 50bp cut and is now pricing just a 25bp cut. OIS-implied has also priced in back-to-back cuts for 1H next year, taking rates to below 2% in Jun 2025, or even 1.75% in July. This may have been overdone. While political risks in Europe may still weigh on EUR, but we had also flagged that many EUR negatives, such as slowing growth momentum, political fallout, aggressive ECB cut expectations, etc. are already in the price. We still do not rule out the risk of EUR short squeeze in the short term.

- **USDSGD. *Consolidation with Slight Bias to Downside.*** USDSGD traded a touch softer, tracking moves in RMB on politburo optimism. Pair was last seen at 1.3400. Mild bearish momentum on daily chart intact while RSI fell. Consolidation likely with slight bias to the downside. Support at 1.3340 (200 DMA, 23.6% fibo), 1.33, 1.3240 (32.8% fibo retracement of Sep low to Nov high). Resistance at 1.3420 (21 DMA), 1.3490 levels. Pair should continue to take directional cues from USD and CNY fix in absence of key data. Next set of SG data is NODX (17 Dec) and CPI (23 Dec). S$NEER strengthened; last at 1.1% above model-implied mid.

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