Daily Market Outlook

8 July 2024

China Interest Rate Corridor; Cooling Labor Market in US

- **USD rates**. UST yields fell upon the nonfarm payroll and the labour market report, after a very transient confusion. June nonfarm payroll printed 206K which was a tad higher than consensus but the change in private payroll was on the low side while previous figures were revised downward. Separately, the employment rate edged higher to 4.1% in June from 4.0% prior, while hourly earnings growth slowed. The latest statistics add to the notion that the labour market has been cooling. the Six-month average of non-farm payroll change was last at 222K (as of May 2024) which was similar to the 200K+ levels in the years 2013-2019. In comparison, Fed funds target rate ranged between 0.25% and 2.50% in those years. Furthermore, if FOMC members perceive the equilibrium level of employment is higher now due to immigration, then the labour market may already be in equilibrium and the current rate levels are probably overly restrictive. Fed funds futures added marginally to rate cuts expectation, pricing a total of 50bps of cuts by year-end, in line with our base-case. While rate cuts are already in the price, we continue to have a downward bias to short-end UST yields. The 2Y UST yield has been moving consistently with market pricing of Fed funds rates, plus a (varying) term premium. As time goes by, even without a further dovish adjustment in the market pricing of Fed funds rate trajectory, the 2Y yield shall trend lower as the rate cuts priced will be increasingly factored into the valuation of short-end bond yields. Trading range for the 2Y yield is seen at 4.50-4.65%.

- **DXY. *Softer NFP Should Weigh on USD.*** DXY fell last week on softer US data and Fedspeaks. While recent headline NFP may have surprised to the upside at +206k vs 190k, the print is now dipping back below the 6month moving average of +222k. 2month payroll downward net revision was also large at -111k while unemployment rate rose to 4.1% (vs. 4% prior). Job vacancy rate is also on a decline. On net, tightness in labour market is easing. This week, we are keeping a close watch on US CPI report (Thu) and Fed Chair Powell's semi-annual testimony to Banking senate panel (Tue) and House Financial Services Committee (Wed). If there is no change in tune to Powell's recent remarks and CPI continues to print softer, then the USD slippage may have room to run. DXY was last seen at Last seen at 104.92. Daily momentum turned bearish while RSI fell. Evening star pattern observed on weekly chart. On net, the bearish setup may have room to run.

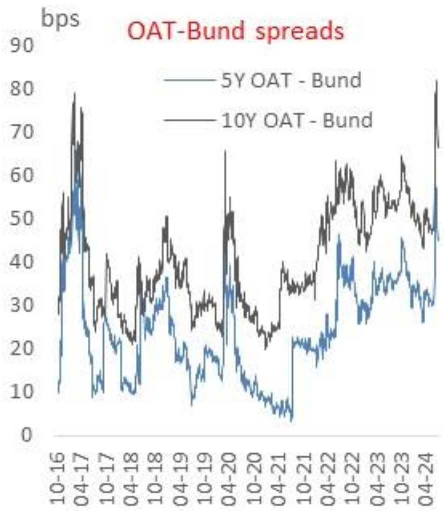
Frances Cheung, CFA
Rates Strategist
FrancesCheung@ocbc.com

Christopher Wong
FX Strategist
ChristopherWong@ocbc.com

Global Markets Research
Tel: 6530 8384

Source: Bloomberg, OCBC Research

Support at 104.80 (61.8% fibo retracement of Oct high to 2024 low, 100 DMA), 104.50 (200 DMA) and 103.98 (50% fibo). Resistance at 105.10 (50 DMA), 105.80 (76.4% fibo) and 106.20.

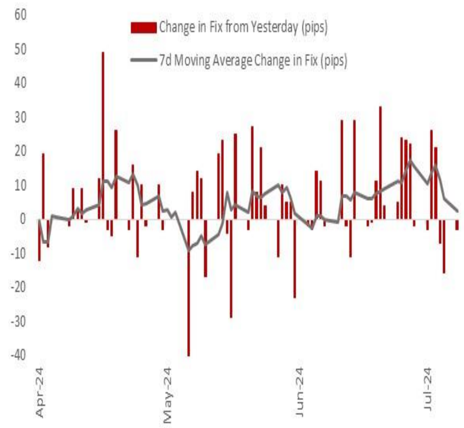


- **EUR rates**. With risk of fiscal slippage in France being perceived as higher now, market is eying early 2017 levels for OAT-Bund yield spreads when the spreads were as wide as 79bps at the 10Y and 66bps at the 5Y. Bunds had benefitted from additional safe-haven flows as investors positioned for risk surrounding the French election, with widened OAT-Bund yield spreads and EUR OIS – Bund yield spreads. OAT-Bund yield spreads narrowed back mildly in recent days in hope for a market-friendly outcome. Starting from such positions, near-term reaction may see a re-widening of these spreads. The 2Y EUR OIS-Bund yield spread at 10bps, for example, is not wide compared to historical levels and regardless of the election outcome, we do not expect further narrowing.

- **EURUSD. *Hung Parliament but With Surprise Twist.*** EUR started the week on a slightly softer footing after 2nd round election results produced a somewhat surprise outcome. Leftwing NFP alliance is tops on 182, Macron's centrists on 163 and the far-right RN and its allies on 143. The outcome shows how elections can be fluid and unpredictable as markets were so fixated on a far-right win. It also shows how tactical dropouts in round 2 elections can affect far-right and swing final outcome. A leftist-dominated government was least expected and most feared as public spending may rise, further putting financial strains on public finance. The only consolation here is that the outcome is a hung parliament, and the left is short of an absolute majority. They will need to find other parties to form a government. Markets are expected to digest the results further as government formation may take some time in the interim. Though neither the left nor right scored an absolute majority, a leftist leaning government may be a mild negative for EUR in the interim. EUR was last seen at 1.0830 levels. Mild bullish momentum on daily chart intact but rise in RSI slowed. 2-way risks look more likely. Resistance at 1.0870 (50% fibo). Support at 1.0810 (38.2% fibo retracement of 2024 high to low, 100 DMA). 1.0730/50 levels (23.6% fibo, 21 DMA), 1.0660/ 70 levels (recent low).

- **USDSGD. *Watching NFP.*** USDSGD continued to trade with a heavy bias, owing to broad pullback in USD, UST yields while depreciation pressure seen in JPY, RMB eased. This week, expect the pair to take cues from USD, and near-term fate for the USD is dependent on Powell's testimony (Tue, Wed) and CPI report (Thu). Softer print and a less hawkish rhetoric are needed for USD to continue its slippage. Meanwhile, we continue to watch moves in JPY and RMB. Pair was last at 1.3495 levels. Daily momentum turned bearish while decline in RSI moderated. Consolidation likely. Support at 1.3460/80 levels (200 DMA, 50% fibo), 1.3410 levels. Resistance at 1.3520/30levels (21, 50 DMAs, 61.8% fibo retracement of Oct high to Jan low), 1.36. Our estimates show S$NEER was last at 1.86% above model-implied midpoint.

- **USDCNH. *Fixing Normalises.*** USDCNH traded briefly above 7.31 before turning lower into the week's close. Move lower tracked broad USD pullback while daily fixing reverted to +5pips/ day last week (vs. +15 pips/day during 19 – 28 Jun). Today's fixing came in at -3pips at 7.1286 (vs. 7.1289 on Fri). That said, recent USDCNY fixings continued to follow a pattern that reinforced our view that authorities are pursuing a measured pace of RMB depreciation, in attempt to let out some depreciation pressure. We believe the Intent is not to pursue a big bang approach so as not to undermine sentiments (for fear of accelerating outflows) – we continue to monitor. But overall, higher USDCNY fix, wider CNH-CNY spread and worries of escalation in US-China trade tensions may imply some concerns on RMB in the immediate horizon. USDCNH was last at 7.29 levels. Mild bullish on daily chart eased but decline in RSI moderated. 2-way risks. Resistance at 7.31, 7.3440 (previous high in Oct 2023). Support at 7.28, 7.2770 (21 DMA) and 7.26 (50 DMA).



Source: Bloomberg, OCBC Research

- **CNY rates**. PBoC announced this morning that it will conduct temporary repo or reverse repo depending on market conditions on working days at 1600-1620 local time. We wrote earlier on 1 July that *OMO reverse repo rate (and decade back, OMO repo rate) has been effectively serving as a policy rate. PBoC injects liquidity via reverse repos and as such the OMO reverse repo rate acts as the cap of an interest rate corridor. If OMO repos were to be conducted, then OMO repo rate could serve as the floor as this would be the rate the PBoC pays to absorb excess liquidity from the market. Being conducted regularly, daily OMOs can be effective in guiding market interest rates within a range*. While market demand for OMO repo may be on the low side, re-starting the program can be seen as part of the effort to build the interest rate corridor. PBoC discloses more details, that temporary overnight OMO repos will be conducted at a fixed rate which is the 7-day OMO reverse repo rate minus 20bps, while the overnight OMO reverse repos will be conducted at the 7-day OMO reverse repo rate plus 50bps, effectively a width of 70bps. 2Y CGB yield rose by 5bps this morning, as the yield is very near the 1.6% rate at which PBoC intends to conduct OMO repo. Near-term steepening momentum may not be strong across the 2s10s part of the curve since it has steepened by a fair bit; more potential may be across the 5s30s segment.

Macro Research

Selena Ling
Head of Research & Strategy
lingssselena@ocbc.com

Tommy Xie Dongming
Head of Asia Macro Research
xied@ocbc.com

Keung Ching (Cindy)
Hong Kong & Macau Economist
cindyckeung@ocbc.com

Herbert Wong
Hong Kong & Taiwan Economist
herberthtwong@ocbc.com

Lavanya Venkateswaran
Senior ASEAN Economist
lavanyavenkateswaran@ocbc.com

Ahmad A Enver
ASEAN Economist
ahmad.enver@ocbc.com

Jonathan Ng
ASEAN Economist
jonathanng4@ocbc.com

Ong Shu Yi
ESG Analyst
shuyiong1@ocbc.com

FX/Rates Strategy

Frances Cheung, CFA
Head of FX & Rates Strategy
francescheung@ocbc.com

Christopher Wong
FX Strategist
christopherwong@ocbc.com

Credit Research

Andrew Wong
Head of Credit Research
wongvkam@ocbc.com

Ezien Hoo
Credit Research Analyst
ezienhoo@ocbc.com

Wong Hong Wei
Credit Research Analyst
wonghongwei@ocbc.com

Chin Meng Tee
Credit Research Analyst
mengteechin@ocbc.com