

Interest Rates Monthly

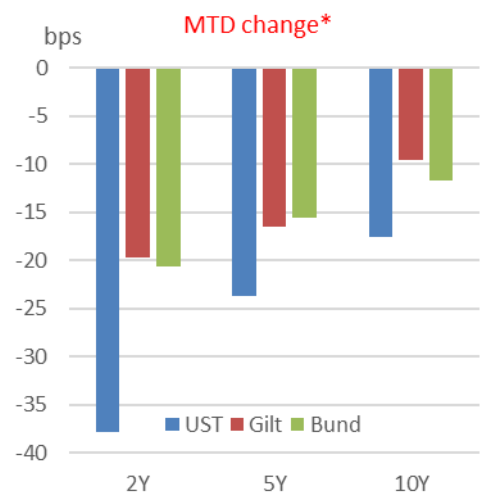
25 September 2024

Aggressive rate cuts in the price

- USD rates.** As and when additional Fed rate cuts materialise, there will still be downside to short-end yields, as the prevailing rate and expected rate trajectory will be increasingly factored into the valuation at the short-end. For yields at the belly to the longer end, we see less room for further downward move from here premised on our soft-landing scenario. The 2% level has proved to be sticky downward for the 10Y breakeven in line with our view, while additional weak US economic data are probably need for the 10Y real yield to break decisively below the 1.5-1.7% range.
- GBP rates.** We expect another 25bp Bank Rate cut before year-end, likely to be delivered at the November MPC. GBP OIS pricing is more dovish than our base-case. Meanwhile, heavier APF gilt maturity for the next 12-month period will be a buffer to active gilt sales amid ongoing QT. This backdrop may help slow the gilt underperformance against swaps at the long end.
- JPY rates.** Additional interest rate hikes are on the table based on domestic fundamentals. Obstacles to any delay in the timing of rate hikes are probably external. We maintain our expectation for another 10bp hike before year-end.
- IndoGBs.** As IndoGB-UST yield differentials have already improved, a domestic rate-cutting cycle shall be supportive of short to mid-end IndoGBs and shall render the domestic bonds more appealing to foreign investors.
- SGD rates.** Our medium-term view remains that room for short-end SGD rates to fall shall be less than that for USD rates to fall, leading to some further normalization in short-end SGD-USD rates spreads. But this spread normalization may lose some momentum near-term. On the SGD OIS curve itself, the front part of the curve is very inverted. We do not expect much further downside to rates at 2Y and beyond over our forecast horizon.
- CNY rates.** Officials announced a slew of support measures including cuts in the RRR, 7-day OMO reverse repo rate and MLF rate. While it takes time for the impact on the economy to show up, the recovery in the overall risk sentiment can come earlier. We maintain a steepening bias on the curve. At the short-end, our view has been for short-end repo-IRS to partially catch up with CGB yields.

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Global Markets Research and Strategy



Source: Bloomberg, OCBC Research

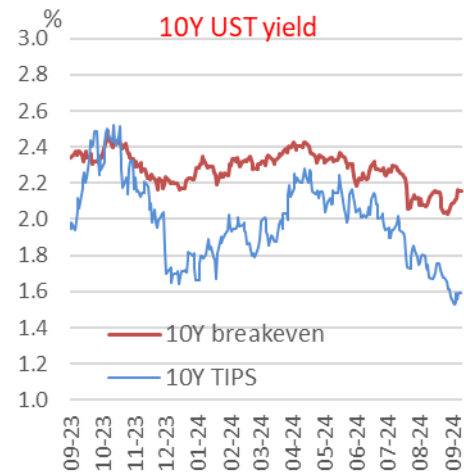
*as of 24 September

USD:

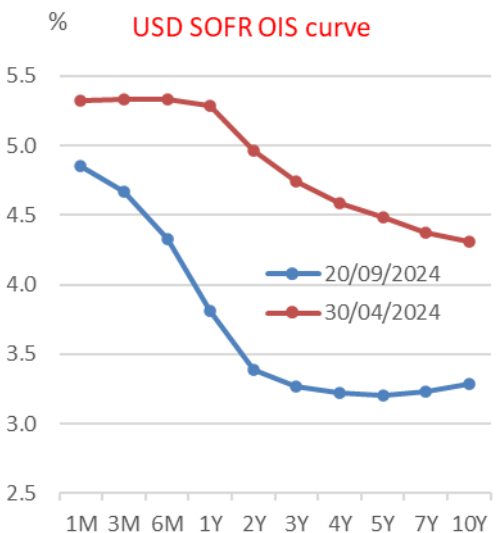
The UST curve bearish steepened on the day of the FOMC decision to lower the target range for the Fed funds rate by 50bps. The 50bp cut did not disappoint market expectation and it outsized economist consensus, but there were a few elements which could explain the initial market reaction of higher yields (and firmer dollar). First, market pricing was dovish enough and investors were already seen trimming positions running into the FOMC meeting. Second, Powell's tone was not particularly dovish. Third, the 2025 median dot shows 100bps of cuts versus market pricing of 125bps or more. Fourth, the rate cut that was delivered and prospects of more cuts were probably seen as adding to the likelihood of a soft-landing scenario. All being said, short-end yields have since fallen further as market doubled down on rate cuts bets.

After the September rate cut, **we expect another 50bps of Fed funds rate cuts for the rest of the year, and we maintain our view for a total of 125bps of cuts in 2025. As and when additional Fed rate cuts materialise, there will still be downside to short-end yields and rates**, as the prevailing rate and expected rate trajectory will be increasingly factored into the valuation at the short-end. For rates at the belly to the longer end, premised on our soft-landing scenario. The 2% level has proved to be sticky downward for the 10Y breakeven in line with our view, while additional weak US economic data is probably needed for the 10Y real yield to break decisive below the 1.5-1.7% range. We maintain our expectation for the 10Y UST yield at 3.7% at year end. The USD OIS curve is very inverted at the front part; we expect more limited downside to rates at 2Y tenor and beyond compared to the shorter end.

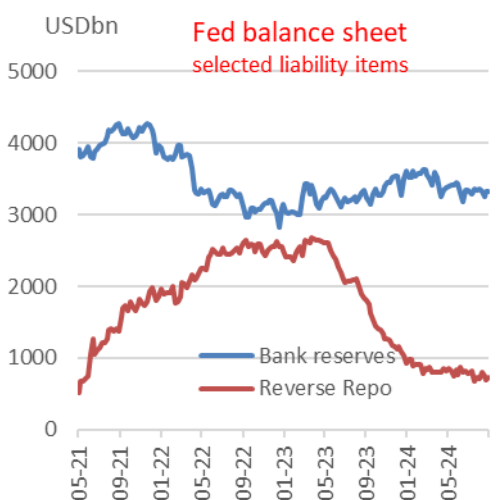
USD liquidity. Usage at the Fed's o/n reverse repo has risen back up to above the USD300bn level, similar to end-August level after some ups and downs over the past month. This usage may not fall much in the coming quarter. US Treasury has planned for small net bills issuances for the October-December period, ahead of the reinstatement of the federal debt ceiling on 2 January 2025. Taking the broader measure of liquidity, bank reserves stood at USD3.3trn and total reverse repos at USD723bn as of 18 September, which shall allow QT to run through to at least year-end before the next decision is made. Reduction in reverse repos have been absorbing the majority of the liquidity tightening from QT thus far, leaving bank reserves relatively more stable. It would then be natural to see lower bank reserves when usage at reverse repos falls to and stay stable at a low level. By then, front-end rates may become a bit more sensitive to changes in bank reserves.



Source: Bloomberg, OCBC Research



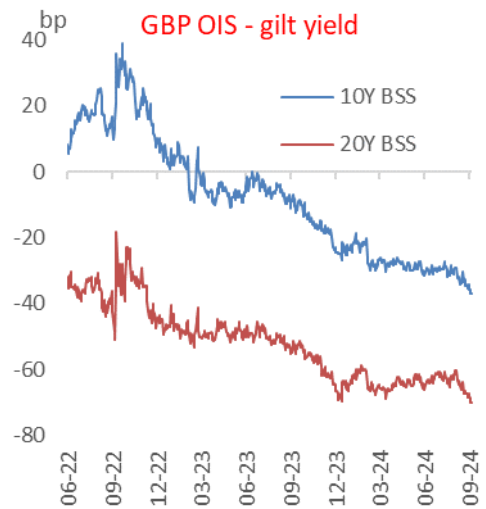
Source: Bloomberg, OCBC Research



Source: Bloomberg, OCBC Research

GBP:

Bank of England kept its Bank Rate unchanged at 5%, as widely expected. The vote was 8-1 with one member preferring a 25bp cut. The MPS did not shed much light on the central bank’s latest thoughts on the economic outlook, as “there has generally been limited news in UK economic indicators”, but the summary added “in the absence of material developments, a gradual approach to removing policy restraint remains appropriate”. **Our expectation remains for a 25bp Bank Rate cut before year-end**, likely to be delivered at the November MPC. GBP OIS pricing is still more dovish than our base-case, last at 43bps of cuts before year end. Meanwhile, QT pace for the next 12-month starting October has been planned at GBP100bn, the same as that in the previous 12-month period. Our view has been that “even if BoE maintains this annual GBP100bn pace, **heavier APF gilt maturity will be a buffer to active gilt sales**”. With GBP87bn maturing over the coming 12 months, APF gilt sales shall be on the low side. Still, the Q4 schedule looks particularly light, which includes three auctions, all in October, totalling GBP2.15bn when no APF gilts mature. This may help slow the gilt underperformance against swaps at the long end.



Source: Bloomberg, OCBC Research

Interest rates forecasts	Q424	Q125	Q225	Q325	Q425
BoE Base Rate	4.75	4.50	4.25	4.00	3.75
GBP SONIA	4.70	4.45	4.20	3.95	3.70
3M GBP OIS SONIA	4.70	4.45	4.20	3.95	3.75

JPY:

The Bank of Japan kept its policy rate unchanged at 0.25% at the September MPM. The statement opined that “with firms’ behaviour shifting more toward raising wages and prices recently, exchange rate developments are, compared to the past, more likely to affect prices”. In the press conference, Governor Ueda elaborated on that, opining that the risk of inflation overshooting from rising import prices has subsided, after recent FX movements. Meanwhile, he reiterated if the central bank’s economic and price forecasts are achieved, then it will raise interest rates further. Earlier in the month, Board Member Nakagawa in a prepared speech commented “possible upswings in the CPI, led by higher import prices, require attention”. Another Board Member Tamura opined in a prepared speech that he was “concerned that risks [for prices] are possibly becoming more skewed to the upside”. On this he cited Q2 Tankan suggesting labour shortages. The September Tankan is due out on 1 October which will be closely watched.



Source: Bloomberg, OCBC Research

Additional interest rate hikes are on the table based on domestic fundamentals – mainly, the virtuous cycle between wages and prices. Obstacles to any delay in the timing of rate hikes are

probably external in nature. On balance, we maintain our expectation for another 10bp hike before year-end; and given real rates are still very low in Japan, we expect three 10bp hikes in 2025, likely to be delivered in a gradual manner.

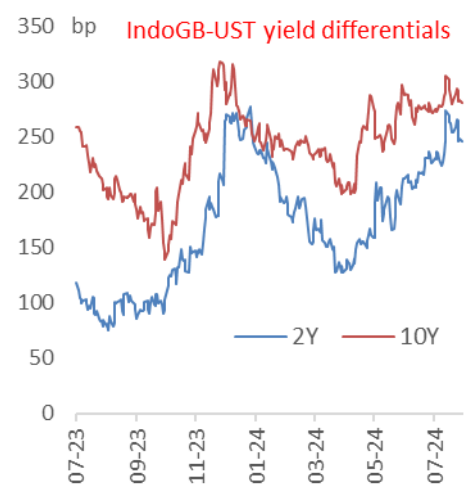
Interest rates forecasts	Q424	Q125	Q225	Q325	Q425
BoJ Policy Target Rate	0.35	0.45	0.55	0.65	0.65
1M JPY TIBOR	0.45	0.55	0.65	0.75	0.75
3M JPY TIBOR	0.48	0.58	0.68	0.78	0.78

IDR:

IndoGB-UST yield differentials widened further during the past month, but in a milder manner than the movements in previous months. Bank Indonesia cut its policy BI rate by 25bps at its September meeting; economist consensus was a hold, but it was a close call. OCBC economists expect an additional 25bp rate cut before year end to be followed by a total of 75bps of rate cuts in 2025.

As IndoGB-UST yield differentials have already improved, a domestic rate-cutting cycle shall be supportive of short to mid-end IndoGBs and shall render the domestic bonds more appealing to foreign investors. The 2Y IndoGB-UST yield spread is at around 1.7 standard deviations wider than 6-month average, while the 6-month z-score for the 5Y spread is around 1.2 and for the 10Y spread is around 1.0. In the four weeks to 19 September, foreign inflows amounted to IDR15trn with foreign holdings standing at IDR863trn or 14.66% of outstanding on 19 September. During these four weeks, banks increased holdings of IndoGBs (including bills) while BI reduced holdings.

On domestic auctions, demand at the last conventional bond auction on 17 September was strong, with incoming bids of IDR63.7trn while IDR22trn of bonds were awarded. Cut-offs were mostly near the lowest incoming bid yield levels.



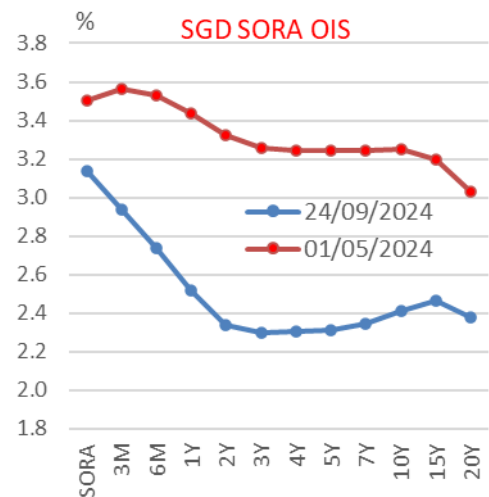
Source: Bank Indonesia, OCBC Research

SGD:

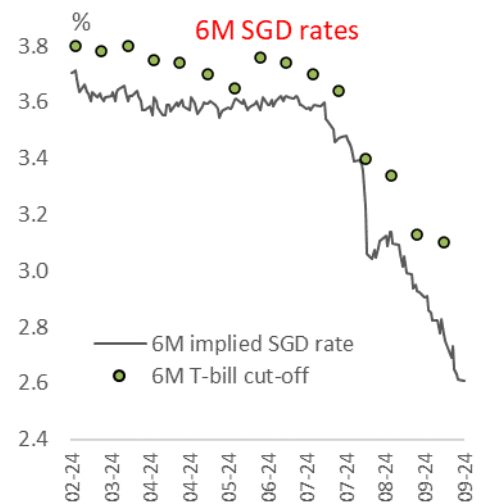
Short-end SGD OIS further underperformed USD OIS in the past month, more so at the 1Y followed by the 2Y. This was in line with historical pattern and our medium-term view. SGD-USD OIS spreads became less negative as a result. This underperformance may be extended as rates fall further and when MAS eases S\$NEER policy in terms of a slope reduction. In this regard, **this spread normalization may lose some momentum near-term**, as the latest CPI prints suggest that MAS may keep S\$NEER parameters unchanged at the upcoming meeting in October. Our **medium-term view remains that room for short-end SGD rates to fall shall be less than that for short-end USD rates to fall**, leading to some further normalization in SGD-USD rates spreads. On the SGD OIS curve itself, rates have adjusted materially lower since the highs in late April; the front part of the curve is very inverted. We do not expect much further downside to rates at 2Y and beyond over our forecast horizon.

The size of the 50Y Green SGS (Infra) reopening auction has been announced at SGD1.5bn, in line with expectations for long-end bond supply. Full year gross SGS issuance will be at SGD27.3bn which is on the low side. We expect demand at this auction to be fair, with most of the demand likely coming from domestic investors. First, the 20s50s part of the SGS curve is flat and therefore there may be some pre-positioning ahead of auction leading to a mild steepening in that part of the curve. Second, there is no same-tenor swap reference, which may mean there will not be much asset swap demand.

6M T-bills cut-offs have been falling alongside market interest rates. One interesting observation, however, is the recent falls in cut-offs were somewhat smaller than the falls in implied SGD rates, which may suggest that investors demand may not keep up entirely if the absolute levels of rates/yields are lower. At the last 6M T-bills auction on 12 September, the 3.10% cut-off was only 3bps below the 3.13% cut-off at the 29 August auction while during this period the 6M implied SGD rate had fallen by more than 10bps.



Source: Bloomberg, OCBC Research



Source: MAS, Bloomberg, OCBC Research

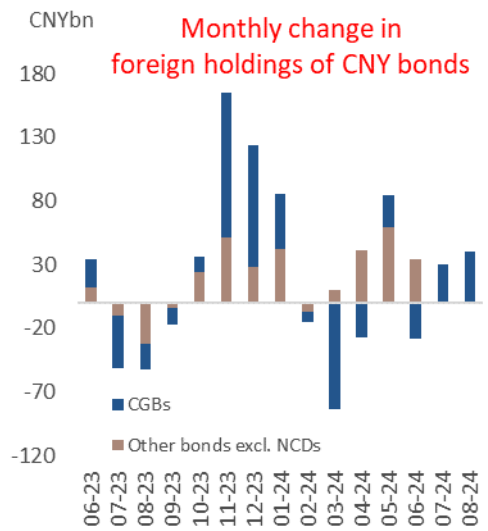
CNY:

At a briefing held jointly by PBoC, CSRC and NFRA on 24 September, officials announced a slew of support measures. Among other measures, the RRR will soon be cut by 50bps, releasing CNY1trn of liquidity; depending on market conditions, official said the RRR may be cut by a further 25-50bps before year end. The rate on the 7-day OMO reverse repo will be cut by 20bps from 1.7% to 1.5%. Initial reactions saw CGB yields lower across the curve, as market probably focused on the softer growth outlook instead of the stimulus impact at this juncture. While it takes time for the impact on the economy to show up, the recovery in the overall risk sentiment can come earlier. We expect a fair bit of consolidation in the 10Y yield at the 2.00% level after initial adjustment; and we maintain a steepening bias on the curve. At the short-end, our view has been for short-end repo-IRS to partially catch up with CGB yields as they had lagged in the downward move. 1Y repo-IRS has fallen by 8bps since the policy announcement; we see some further downside from here.

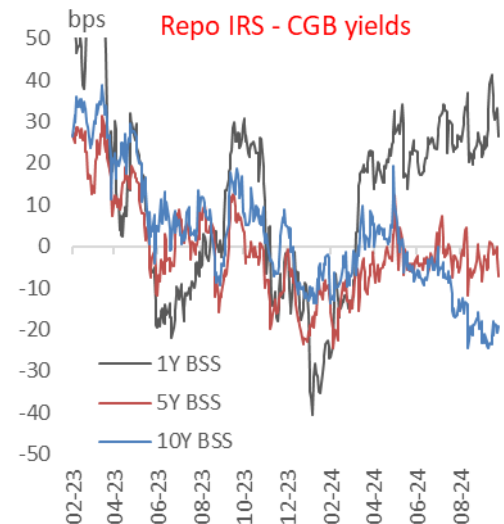
PBoC conducted CNY300bn of MLF in the month, against CNY591bn that matured, i.e. a partial rollover. This did not come as a surprise especially with the planned RRR cut. Looking ahead, the window of opportunity is there for another RRR cut before year end, given heavy MLF maturity – CNY789bn in October, CNY1.45trn in November and another CNY1.45trn in December. Meanwhile, the 30bp cut in MLF rate renders the facility more aligned with the funding costs under other channels such as via NCDs. The highest and lowest incoming bids of MLF were also disclosed, reflecting the intention to make this facility more driven by demand and to fade the role of the MLF rate as a policy guidance

Bond flows. CGBs saw another month of inflows of RMB40.3bn in August after July's RMB30.5bn, as yield differentials improved upon the more rapid falls in UST yields. Inflows into NCDs had been hefty for months but fell to RMB28bn in August; in that month, implied RMB rates went higher as onshore forward points were paid up rapidly, narrowing potential asset swap pick-up, while investors positionings and credit exposure might have been other constraints as well.

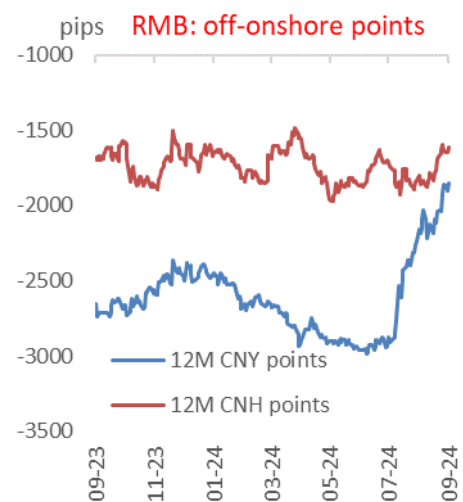
The spreads between back-end CNH points and CNY points have narrowed rapidly as onshore points were paid up. As USD rates fall, off-onshore spreads in the point shall tend to narrow as impact of onshore 20% risk reserve requirement becomes less; for example, the full impact of the 20% requirement at the 12M is roughly 600pips versus more than 800pips two months ago. Not all entities are subject to the 20% requirement, which help explain the much narrower spread of 230pips currently. Still, at current levels, room for further narrowing is more limited.



Source: CEIC, OCBC Research



Source: Bloomberg, OCBC Research



Source: Bloomberg, OCBC Research

Rates Forecast

USD Interest Rates	Q424	Q125	Q225	Q325	Q425
FFTR upper	4.50	4.00	3.75	3.50	3.25
SOFR	4.32	3.82	3.57	3.32	3.09
3M SOFR OIS	4.25	3.80	3.65	3.40	3.20
6M SOFR OIS	4.05	3.70	3.65	3.40	3.20
1Y SOFR OIS	3.62	3.32	3.17	3.02	3.00
2Y SOFR OIS	3.27	3.12	3.09	3.02	3.00
5Y SOFR OIS	3.17	3.04	3.04	3.00	3.00
10Y SOFR OIS	3.25	3.09	3.09	3.05	3.05
15Y SOFR OIS	3.30	3.14	3.14	3.10	3.10
20Y SOFR OIS	3.32	3.19	3.19	3.17	3.12
30Y SOFR OIS	3.32	3.22	3.22	3.20	3.15
SGD Interest Rates	Q424	Q125	Q225	Q325	Q425
SORA	3.15	2.90	2.78	2.65	2.50
3M compounded SORA	3.30	3.05	2.85	2.70	2.58
3M SGD OIS	2.75	2.65	2.50	2.40	2.40
6M SGD OIS	2.65	2.60	2.50	2.35	2.35
1Y SGD OIS	2.45	2.40	2.35	2.30	2.30
2Y SGD OIS	2.30	2.25	2.20	2.20	2.20
3Y SGD OIS	2.25	2.25	2.25	2.25	2.30
5Y SGD OIS	2.25	2.25	2.25	2.30	2.30
10Y SGD OIS	2.35	2.35	2.35	2.40	2.40
15Y SGD OIS	2.35	2.35	2.35	2.40	2.40
20Y SGD OIS	2.35	2.35	2.35	2.40	2.40
UST yields	Q424	Q125	Q225	Q325	Q425
2Y UST	3.55	3.40	3.35	3.35	3.10
5Y UST	3.50	3.50	3.45	3.40	3.15
10Y UST	3.70	3.65	3.60	3.55	3.55
30Y UST	4.00	3.95	3.90	3.90	3.90
SGS yields	Q424	Q125	Q225	Q325	Q425
2Y SGS	2.35	2.30	2.25	2.20	2.15
5Y SGS	2.35	2.30	2.30	2.25	2.25
10Y SGS	2.50	2.50	2.45	2.40	2.30
15Y SGS	2.55	2.55	2.55	2.50	2.40
20Y SGS	2.55	2.55	2.50	2.50	2.45
30Y SGS	2.60	2.60	2.60	2.55	2.55

Source: OCBC Research (Latest Forecast Update: 25th September 2024)

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