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Macro Insights Weekly

Economic implication of shifting yield curves

Group Research **March 18, 2024**

Taimur Baig
Chief Economist
taimurbaig@dbs.com

Chua Han Teng
Economist
hantengchua@dbs.com

For Alliance Bank clients, please direct your enquiries to Malaysia Research +603 2604 3915 general@alliancedbs.com

- *Resilient demand and price data have pushed global fixed income markets to a point of capitulation. As rate cut expectations are pared back, investors need to watch for potential fault lines.*
- *Bond selloff has caused no consternation in global markets yet.*
- *The lack of panic reflects healthy wages, earnings, and capital gains.*
- *Balance sheets can absorb rates that reflect healthy returns on capital.*
- *There could however be a point when high rates affect a sensitive part of the financial markets.*
- *Market complacency could be upturned by continued inflation surprises.*

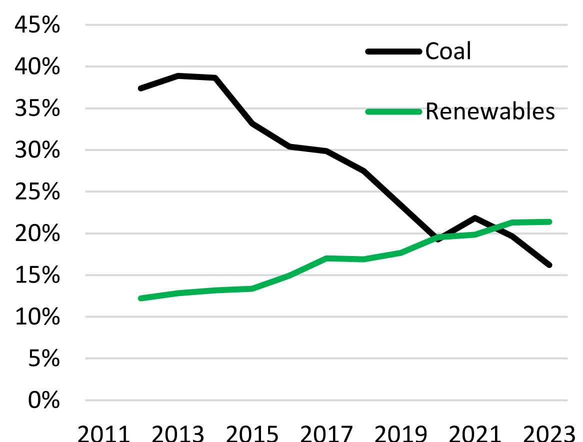
Key data release and events this week:

- *We expect the BOJ to terminate the negative interest rate policy at this week's meeting.*
- *The US Fed is set to provide new clues on future rate cuts.*
- *Central banks in Indonesia and Taiwan are likely to keep policy rates steady.*

Chart of the Week: Rise of renewables

In the span of a decade, renewable energy production in the US has more than doubled, just as coal production has halved. Soaring natural gas production, combined with the surge in renewables, have pushed coal from the largest contributor to US energy production to a laggard, with numerous coal plants due for retirement in the near term. Within renewables, wind (10.2%) commands the top post in contribution to total energy production, followed by hydro (5.7%) and then solar (3.9%).

US electricity generation by fuel type
% of total



Source: IEA, DBS

Refer to important disclosures at the end of this report.

Commentary: Economic implication of shifting yield curves

There is an element of capitulation in the global fixed income markets. The narrative of 2024 being a year of sizeable interest rate cuts, so prevalent just a few months ago, has been upended rather dramatically. A few of months of sticky inflation data and growing evidence of demand resiliency have pushed up yield curves around the world. The markets are not giving up on rate cuts, rather expecting them to take place later and to be fewer.

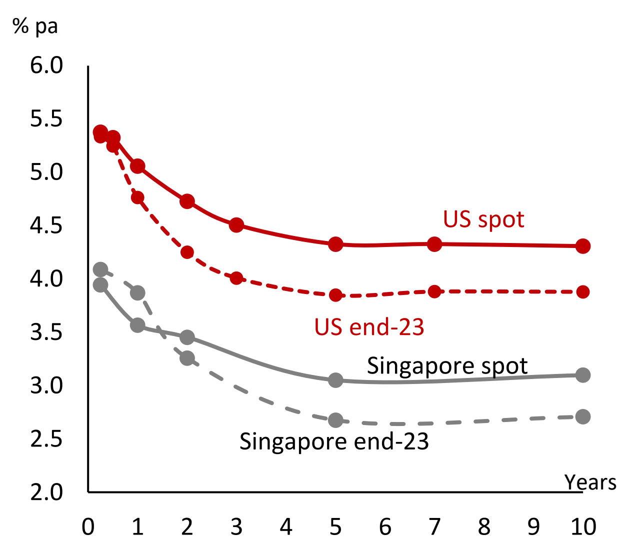
There is little apparent consternation in financial markets owing to these developments. Public and corporate debt Issuances and refinancing are progressing without a hitch, stock markets are in rally-or-stable mode, volatility markers are at 5-year lows, financial conditions are on the easy side, and currency markets are largely gyration-free.

The key reason for fixed income market repricing causing barely a ripple in wider markets stems from economic data. The inflation surprises so far don't reveal any supply side distortions or demand shocks. Labour markets in the US are tight, keeping services inflation high, but goods and energy prices are well-behaved, reflecting soft demand in China and ample supply/production.

Even China and Europe, a laggard on the demand side relative to the US, have stopped from yielding negative dataflow. Exports have bottomed out, tourism and travel continue to thrive, and shocks from various wars and inclement weather have been absorbed remarkably well.

As long as high rates are a reflection of strong underlying demand, which in turn reflects higher rate of return on capital, the fixed income market capitulation should be seen in a constructive light. Typically, a higher-than-expected interest rate horizon would bode ill for debt holders, but if their incomes, wages, and profits are growing at the same time, then a higher debt service cost need not be a net negative. There is a delicate balance in place in this context—climbing rates, as long as they are countered by healthy outturns in other items in the balance sheet, can be readily absorbable.

US and Singapore Treasury yield curves



Source: Bloomberg, DBS

This cannot sustain indefinitely though. Eventually, some parts of the economy will succumb to duration mismatch, balance sheet quality deterioration, or a negative feedback loop from a poorly performing, widely held financial product. Could it be residential mortgages, commercial real estate, or high yield bonds in some other sector? Time will tell, but for now, the ongoing treasury selloff is leaving global markets remarkably unruffled.

Taimur Baig

Key forecasts for the week

Event	DBS	Previous
Mar 18 (Mon)		
China: industrial production (Jan-Feb)	6.0% y/y	6.8% y/y
- retail sales	7.0% y/y	7.4% y/y
- fixed asset investment	3.2% y/y	3.0% y/y
Malaysia: exports (Feb)	-2.0% y/y	8.7% y/y
- imports	7.8% y/y	18.8% y/y
- trade balance	MYR10.1bn	MYR10.1bn
Mar 19 (Tue)		
BOJ: policy balance rate	0%	-0.1%
Mar 20 (Wed)		
China: 1Y loan prime rate	3.45%	3.45%
Indonesia: 7D reverse repo	6.00%	6.00%
Taiwan: export orders (Feb)	1.3% y/y	1.9% y/y
Mar 21 (Thu)		
US: FOMC rate decision	5.50%	5.50%
Hong Kong: CPI (Feb)	1.9% y/y	1.7% y/y
Taiwan: CBC benchmark rate	1.875%	1.875%
Japan: exports (Feb)	1.8% y/y	11.9% y/y
- imports	0.6% y/y	-9.6% y/y
- trade balance	-JPY844bn	-JPY1760bn
Mar 22 (Fri)		
Japan: CPI (Feb)	3.0% y/y	2.2% y/y

Central bank policy meetings

Bank of Japan (March 19): With the Shunto talks showing encouraging results, we now expect the BOJ to terminate the negative interest rate policy at this week's meeting. Last Friday, Japan's largest labour union RENGO announced a significant 5.28% hike in total wages, including a 3.7% rise in base wages, which notably exceeds last year's increases of 3.8% and 2.3%. This suggests that this year's macro wages will likely increase by around 2.5%, nearing the threshold necessary for achieving 2% inflation. The termination of NIRP, involving the hike in the policy balance rate from -0.1% to 0% or 0.1%, is deemed an essential step toward policy normalisation. Meanwhile, the possibility of terminating yield curve control is also being considered, yet the BOJ might defer such action to 2H24, when the global interest rate environment becomes more conducive due to anticipated Fed easing. Additionally, the BOJ is expected to continue quantitative and qualitative easing, committing to substantial JGB purchases and an expansion in the monetary base, until inflation achieves 2% in a sustainable and stable manner.

Reserve Bank of Australia (March 19): We expect the cash rate target to remain unchanged at 4.35% for the third meeting. The RBA should feel vindicated for its decision to resist a rate hike at its meeting on February 6. After the surprise hike last November, CPI inflation fell from 4.3% YoY in November to 3.4% in January, near the RBA's 2-3% target and 3.3% forecast for 1H24. The unemployment rate also increased from 3.9% in December to 4.1% in January, above the RBA's projected 4% for 1H24. Although addressing inflation remained the primary concern, Treasurer Jim Chalmers noted that the balance of risks was shifting from inflation to growth. GDP growth slowed to 1.5% YoY in 4Q23, its worst growth since 2020. Interest rate futures see a 49% chance of a rate cut in June.

People's Bank of China (March 20): The 1Y LPR is expected to remain unchanged this week. The policymaker aims at stabilising the exchange rate to forestall further capital outflow. Stabilising economic data also leaves room for a delayed rate cut decision. In Feb 2024, the Consumer Price Index returned to positive territory for the first time since Sep 2023. Encouraging Lunar New Year domestic travel data suggests that retail sales growth is expected to remain steady at 7.0% YoY despite the high base reopening boost in Jan-Feb 2023. Similarly, industrial production is projected to have grown by 6.0% YoY in Jan-Feb 2024, reflecting stabilising domestic demand. External demand is also improving, with regional electronics exports showing signs of bottoming out. Fixed asset investment is

forecasted to accelerate from 3.0% YoY YTD in Dec 2023 to 3.2%. The narrowing gap between M1 and M2 growth suggests increasing liquidity needs for investment purposes.

Taiwan's central bank (March 21): The central bank is likely to maintain the benchmark discount rate at 1.875% during the upcoming meeting. Inflation stood at 1.8% YoY in January and 3.1% in February, resulting in an average of 2.4% for the first two months of the year. On a sequential basis, inflation momentum held steady at 2.2% 3M/3M saar. Notably, the government is contemplating a 10-15% hike in electricity prices in April, potentially contributing 0.1-0.2ppt to CPI inflation. Given the persistent elevation of inflation above the policy rate, the central bank's room to cut rates is limited. We continue to expect that policy rate will remain at 1.875% throughout the year, and we acknowledge potential upward risks to our full-year inflation forecast of 1.7%.

Bank of England (March 21): We expect the bank rate to remain at 5.25% for a fifth meeting. On March 20, UK's CPI inflation will remain above the 2% target despite the consensus for headline inflation to drop to 3.5% YoY in February from 4% in January, and core inflation to 4.6% from 5.1%. With the UK economy in a mild technical recession in 2H23, the BOE may start to balance its inflation priority with growth risks. Last week, BOE Governor Andrew Bailey became less wary about second-round effects, i.e., the need for a higher unemployment rate to curb inflation. Last month, Bailey told the Treasury Select Committee that CPI inflation would hit the 2% target in spring before rising again in the rest of the year, emphasizing that the BOE did not need headline inflation at 2% before cutting rates. As of last Friday, interest rate futures see three rate cuts this year in June, September, and December.

Swiss National Bank (March 21): We cannot rule out an easing at this week's meeting, which interest rate futures see a 28% chance of happening. A fortnight ago, SNB President Thomas Jordan declared that "monetary policy has been reached" when he announced his surprise decision to step down this September. When the SNB delivered its final hike to 1.75% in June and kept it below the 2% neutral rate, inflation had returned to the 0-2% target range. CPI and core inflation continued falling to 1.2% YoY and 1.1% in February, below the 1.8% level the SNB forecasted in December for 1Q24. In December, SNB said it was no longer focused on selling foreign currencies, acknowledging that more CHF appreciation was not needed to rein in inflation. Following through in January, SNB noted that the CHF's real appreciation was hurting domestic companies. That said, futures think the odds are higher at 76% for a rate cut in June. If so, SNB will likely pave the way for a summer hike at this week's meeting.

Bank Indonesia (March 20): BI is expected to extend its pause into March, in line with its focus on maintaining stability in the FX markets. Despite benign headline and core inflation, sequential pressures have risen on higher food and stronger demand in midst of religious festivities. Additionally, there is considerable uncertainty in the pipeline with regards to the direction of global interest rates, particularly the US Fed as markets continue to delay expectations of a start to the rate easing cycle. The resultant volatility in the US dollar and rates is likely to swing the Indonesian markets, necessitating the central bank to keep an adequate ID-US differential for the time being.

Forthcoming data releases

Hong Kong SAR: Consumer price growth is forecasted to increase from 1.7% YoY in Jan to 2.1% YoY in Feb 2024. Hong Kong registered 2.08mn Mainland visitor arrivals in Feb, reaching 2018 level on a daily average basis. Total local resident departures narrowed to 1.6x of the total visitor arrivals during the Chinese New Year Holiday, returned to the average level of 2017-2019. Rising rental cost will keep consumer price moderated.

Japan: Both headline and core CPI are likely to rebound to approximately 3% YoY in February, up from the 2.2-2.3% range observed in January. Excluding fresh food and energy, core-core CPI is expected to settle at 3.3%, a marginal slowdown from the 3.5% recorded in January. The expected volatility is attributed to seasonal factors influencing goods prices, while services inflation is projected to remain stable at around 2%. With full-year inflation progressing towards the 2% target, the path is clear for the Bank of Japan to terminate negative interest rates and normalize monetary policy.

Taiwan: February export orders are expected to exhibit a modest single-digit growth of approximately 1% YoY. Earlier data reported a 1.3% YoY increase in exports for the month. Adjusting for the impact of the Chinese New Year, exports showed a 4.2% 3M/3M saar growth in February. This aligns with our projection of a gradual recovery in external trade during 1Q. The recovery, however, displays an uneven pattern, driven primarily by G3 and ASEAN markets, particularly in the electronics sector. Conversely, China and non-electronics goods continue to act as dragging factors on overall growth.

Malaysia: Malaysia's goods exports likely pulled back to 2.0% YoY contraction in February 2024 from January 2024's strong 8.7% YoY expansion. Notwithstanding the near-term fluctuations, exports are turning around, and should benefit from an ongoing improvement in the global electronics cycle. Yet, the recovery would be gradual, given ongoing global uncertainties from high interest rates in advanced economies, bumpy conditions in China, and lingering geopolitical tensions that could still disrupt supply chains.

Economics Team

India announces election dates

In the world's largest democratic voting exercise, an estimated 969mn are due to vote this year, marking a more than 70mn increase from five-year back at the 2019 election. The Election Commission announced the 2024 general election poll dates over the weekend. **Polling is scheduled to take place over seven phases between 19 April and 1 June 2024, with the official results out on 4 June.** Ahead of the final count, private sector surveys/ exit polls will begin to trickle in from 1 June onwards, provided an early peek into the direction of the voting.

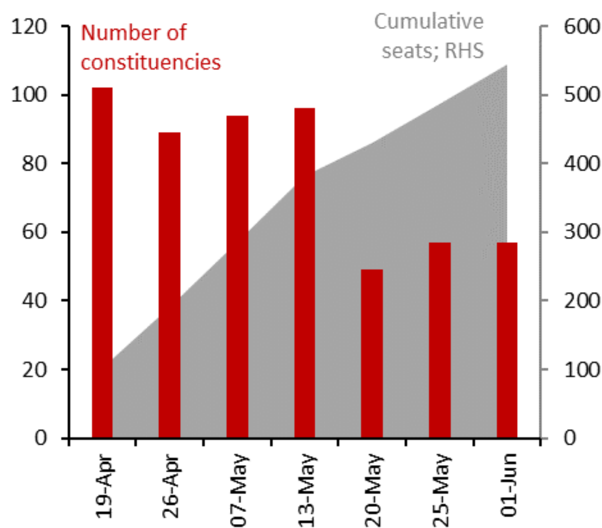
The official mode of conduct kicks in immediately, limiting the scope of additional big-ticket policy announcements by the ruling government until the new team takes office in 2H24. Of the 543 parliamentary seats, the next government will be required a win a simple majority of more than 270 seats. Key parties this year include -

a) ruling coalition National Democratic Alliance (NDA) led the by main party Bharatiya Janata Party (BJP) and its allies.
b) The Indian National Congress and a mix of regional/ opposition parties under the INDIA (Indian National Development Inclusive Alliance) umbrella
c) Regional parties might also fight on their accord in their own strongholds.

Private opinion polls suggest that the ruling coalition party will return with even a stronger mandate than the 2019 polls, led by Prime Minister Narendra Modi. The latest News 18 opinion poll on Thursday projected that the NDA might be on course for a hattrick win, with the ruling political party BJP expected to corner 411 seats in the Lower House of parliament/ Lok Sabha, in essence win an absolute majority singlehandedly. The last time a win of this magnitude (of a party winning more than 400 seats) was in 1984, when the Congress Party bagged 411 seats out of 542 available. The survey pegs NDA's vote share at 48% in the upcoming General Elections.

As the elections draw near, markets will be focused on political stability and a continuation of economic reforms in midst of a rising manufacturing footprint. The incumbent government has also focused on higher capex spending, which is expected to draw in more private sector participation after the polls. We maintain our growth forecast of 7.6% for FY24 with an upward bias towards 8%.

Polling schedule - results due on 4 June 2024



Source: Local press, DBS

Radhika Rao

FX: Fed and BOJ to set the tone this week

Fed Chair **Jerome Powell should feel vindicated about a rate cut not being the "base scenario" at the FOMC** meeting on March 19-20. During his semi-annual congressional testimonies on March 6-7, Powell **said the Fed was "not far" from having the confidence** that inflation was moving sustainably to the 2% target **to dial back the level of restriction and avert an economic recession.** However, less than a week later, US CPI and core inflation came in stronger-than-expected at 0.4% MoM in February. Minneapolis Fed President Neel Kashkari, a non-voting FOMC member, saw only 1-2 cuts this year vs. the 3-4 cuts in the Summary of Economic Projections.

Premature to get overly worried about US inflation

	Headline, % MoM			Core, % MoM			Fed Funds Rate, bps ch		
	2022	2023	2024	2022	2023	2024	2022	2023	2024
Jan	**0.6**	**0.5**	0.3	**0.6**	0.4	0.4			
Feb	**0.8**	0.4	0.4	**0.5**	**0.5**	0.4		+25	Pause
Mar	**1.1**	0.1		0.3	0.3		+25	+25	
Apr	0.4	0.4		**0.5**	**0.5**				
May	**0.9**	0.1		**0.5**	0.4		+50	+25	
Jun	**1.2**	0.2		**0.7**	0.2		+75	Pause	
Jul	0.0	0.2		0.4	0.2		+75	+25	
Aug	0.1	**0.5**		**0.5**	0.2				
Sep	0.4	0.4		**0.6**	0.3		+75	Pause	
Oct	**0.5**	0.1		0.4	0.2				
Nov	0.3	0.2		0.3	0.3		+75	Pause	
Dec	0.1	0.2		0.4	0.3		+50	Pause	

Bold: ≥0.5% MoM increase
Blue/Red/Black: Slow/Accelerate/Unchanged vs. same month year ago.
Sources: DBS Research, Bloomberg data

We doubt Powell will sound hawkish at the post-meeting press conference. Like other central banks, Powell will likely see the Fed's policy outlook becoming more balanced between inflation and growth. Inflation tends to be seasonally strong at the start of the year. More importantly, this year's readings had been stable and lower than those a year ago. New York Fed President John **Williams**, a permanent FOMC member, **said rate cuts would not be on a specific fixed schedule but depend on economic conditions, not just inflation**. Looking beyond the increase in nonfarm payrolls to 275k in February from 229k in January, the Fed will probably pay more attention to the unemployment rate rising to 3.9% from 3.7% and average hourly earnings growth declining to 0.1% MoM (4.3% YoY) from 0.5% MoM (4.4% YoY).

Hence, **DXY can resume its decline after its best weekly rebound** (0.7%) in eight weeks. DXY faces stiff resistances at 103.4-103.7, where multiple moving averages have converged.

The **Bank of Japan** meeting on March 19 **could** lead **USD/JPY to fall again after the squeeze** to 149 from 146.50 last week. Last Friday, the country's largest trade union federation, Rengo, reported that **companies agreed to increase wages** by a preliminary weighted average of 5.8% this year, the **largest since 2013**. The tone set by the major companies **should cascade into the next stage of wage talks at the small and midsized enterprises** that account for 70% of all employment. More so now that Japan averted a technical recession after final GDP growth in 4Q23 was revised to an annualized 0.4% QoQ sa expansion from a preliminary 0.4% contraction earlier. Hence, many believe it will be **a question of "not if, but when" Japan ends the world's final negative interest rate policy**. According to Reuters last Friday, 12 of the 34 economists polled favoured a move tomorrow, with 21 keeping to their call for a shift in April.

Apart from these two crucial meetings, **three other central banks will also hold meetings** to assess their monetary policies. The Reserve Bank of Australia and the Bank of England will likely lean towards the Fed's more balanced stance between inflation and growth. The Swiss National Bank could join the BOJ in setting or providing guidance on interest rates in the opposite direction.

Philip Wee

Group Research

Economics & Strategy

Taimur BAIG, Ph.D.
Chief Economist
Global
taimurbaig@dbs.com

Wei Liang CHANG
FX & Credit Strategist
Global
weiliangchang@dbs.com

Tracy Li Jun LIM
Credit Analyst
USD Credit
tracylimt@dbs.com

Amanda SEAH
Credit Analyst
SGD Credit
amandaseah@dbs.com

Nathan CHOW
Senior Economist
China/HK SAR
nathanchow@dbs.com

Eugene LEOW
Senior Rates Strategist
G3 & Asia
eugeneleow@dbs.com

Daisy SHARMA
Analyst
Data Analytics
daisy@dbs.com

Han Teng CHUA, CFA
Economist
Asean
hantengchua@dbs.com

Teng Chong LIM
Credit Analyst
SGD Credit
tengchonglim@dbs.com

Joel SIEW, CFA
Credit Analyst
SGD Credit
joelsiew@dbs.com

Mo JI, Ph.D.
Chief Economist
China/HK SAR
mojim@dbs.com

Tieying MA, CFA
Senior Economist
Japan, South Korea, Taiwan
matieying@dbs.com

Mervyn TEO
Credit Strategist
USD Credit
mervynteo@dbs.com

Byron LAM
Economist
China/HK SAR
byronlamfc@dbs.com

Radhika RAO
Senior Economist
Eurozone, India, Indonesia
radhikarao@dbs.com

Samuel TSE
Economist/Strategist
China/HK SAR
samueltse@dbs.com

Violet LEE
Associate
Publications
violetleeyh@dbs.com

Philip WEE
Senior FX Strategist
Global
philipwee@dbs.com

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DBS Bank Ltd., 12 Marina Boulevard, Marina Bay Financial Centre Tower 3, Singapore 018982. Tel: 65-6878-8888. Company Registration No. 196800306E.

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DBS Bank (Hong Kong) Limited, a company incorporated in Hong Kong with limited liability. 13th Floor One Island East, 18 Westlands Road, Quarry Bay, Hong Kong SAR

AllianceDBS Research Sdn Bhd (128540 U), 19th Floor, Menara Multi-Purpose, Capital Square, 8 Jalan Munshi Abdullah, 50100 Kuala Lumpur, Malaysia. Tel.: +603 2604 3915.

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