



# FROM THE FIXED INCOME DESK

## Monthly Outlook

### Summary

- USTs ended September mixed. While the Federal Reserve (Fed) left interest rates unchanged and the Bank of Japan reinforced commitment to monetary easing, the ECB's lack of new stimulus disappointed the market. 10-year UST yields rose by about 1 basis point (bp) to end at 1.6%.
- China delivered better than expected economic results for the month of August. Money supply and RMB loans registered gains while industrial production and retail sales also printed better than forecast.
- In India, headline CPI inflation moderated more than consensus expectations on the back of lower food prices. Conversely, industrial production weakened as manufacturing output dropped, disappointing the market.
- Bank Indonesia cut its benchmark interest rate by 25bps. In addition, the country's tax amnesty programme witnessed a significant pick-up in revenue proceeds. Meanwhile, Standard & Poor's (S&P) maintained the Philippines' credit rating, citing caution against possible political uncertainty.
- Asian credits registered gains in September, amid mixed signals from global central banks which sparked volatility. Towards the end of the month, concern regarding Deutsche Bank and a pick-up in supply of new issues weighed on risk assets, resulting in wider credit spreads.
- New deals in the primary market picked up momentum as compared to August. The high-grade space issued a total of 29 new bonds worth USD 16.45bn while 20 new issues amounting to USD 10bn were issued in the high-yield segment.
- We continue to favour Indian, Malaysian and Indonesian bonds as domestic growth could be buoyed by more monetary easing from the respective central banks. The Philippines, on the other hand, is expected to underperform as no further stimulus is expected from the Bangko Sentral ng Pilipinas in the foreseeable future.
- Demand for the Indonesian Rupiah and Indian Rupee are likely to be supported by the tax amnesty programme and lower trend in inflation respectively. Conversely, trade-reliant economies of Singapore and Korea are expected to remain vulnerable against tepid global growth.
- Ongoing macro uncertainties regarding Deutsche Bank, BREXIT and the expected path of Fed rates are expected to be key highlights in October. In the upcoming month, the supply of new issues in high-grade and high-yield is expected to remain robust, resulting in further widening of secondary spreads.

### Asian Rates and FX

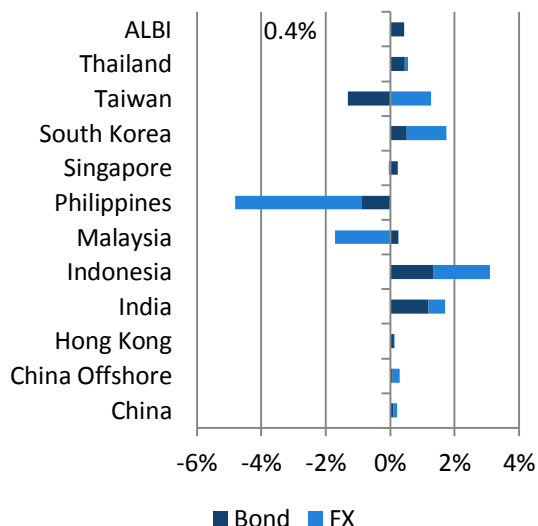
#### Market Review

- USTs ended mixed  
USTs ended in mixed trading. Short-to-mid dated notes registered gains, while long-dated bonds ended lower. Volatility heightened, sparked by mixed messages on the course of global central bank policy. At start of the month, disappointment over the lack of new stimulus from the European Central Bank (ECB) pushed markets to ask if major central banks could be reconsidering a shift in current loose monetary policies. Subsequent hawkish comments from US Fed officials, together with the steepening of the JGB yield curve, fueled a further push higher in yields. Towards the end of the month, yields plunged, as the Fed left interest rates unchanged and revised the interest rate path lower for the

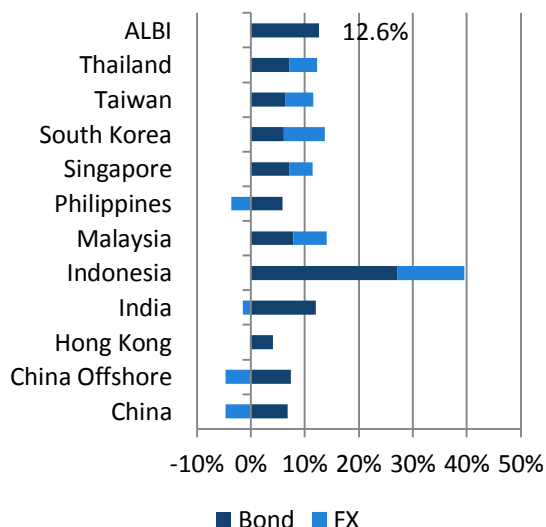
coming years. Meanwhile, the Bank of Japan affirmed its commitment to monetary easing, soothing concerns that it may be looking to remove policy support. Overall, the 10-year point on the UST yield curve rose by about 1 basis point (bp), to end at 1.6%.

### Markit iBoxx Asian Local Bond Index (ALBI)

For the month ending 30 September 2016



For the year ending 30 September 2016



Note: Bond returns are in local currencies while FX and ALBI returns are in USD. Past performance is not necessarily indicative of future performance. Source: Markit iBoxx Asian Local Currency Bond Indices, Bloomberg, 30 September 2016

- **Economic indicators in China surprised on the upside**

China delivered better than expected economic numbers in August. Money supply growth in China rose by a much higher than expected 11.4% year-on-year (YoY) in August, up from 10.2% in July. New RMB loans increased by RMB 948.7bn, and aggregate financing staged a significant rebound in the same month. Credit expansion was driven largely by a jump in household loans. Industrial output and retail sales accelerated

in August. Both the 6.3% YoY rise in industrial production and the 10.6% increase in retail sales also printed ahead of expectations. Meanwhile, fixed asset investment – a gauge of infrastructure spending – was up 8.1% in the first eight months of 2016.

- **Indian CPI inflation moderated more than expected in August; industrial production weakened**

Headline CPI inflation in August registered 5.0% YoY, significantly lower compared to July's 6.1% reading. Lower prices of vegetables, pulses, meat and fish, and eggs drove overall food inflation to ease to 5.8% in the month, from 8.0% in July. In contrast to the positive outturn in CPI relative to expectations, industrial production in July disappointed. The latter posted a 2.4% YoY decline, against expectations of a 1.4% increase. Details reveal that manufacturing output dropped 3.4%, while mining and electricity output expanded.

- **Bank Indonesia cut interest rates by 25bps**

Bank Indonesia (BI) cut its benchmark interest rate by 25 basis points (bps) to 5.0% in September, reducing borrowing costs by a total of 125bps so far this year. According to BI Governor Agus Martowardojo, the central bank thinks that "various measures are still needed to help prop up domestic demand." Earlier in the month, a report indicated that headline CPI registered 2.8% YoY in August, below BI's headline inflation target of 3-5%. The sharp drop in price pressures was driven mainly by significantly lower food price inflation.

- **Indonesia reported a marked pick-up in revenue raised from the tax amnesty programme**

During the month, Indonesia's Ministry of Finance reported a meaningful acceleration of revenue proceeds from the tax amnesty programme. Latest data revealed that penalties paid by participants in the amnesty programme have exceeded 50% of the government's IDR 165tr target, three months into the 9-month programme. Notably, the penalty rate increases starting October.

### Market Outlook

- **Overweight Indian, Malaysian and Indonesian bonds; cautious on Philippine bonds**

We expect global liquidity to sustain the demand for carry the rest of the year. Within the region, we expect Indian, Indonesian and Malaysian bonds to outperform. Despite lowering rates further this month, Bank Indonesia has left the door open for additional easing. Meanwhile, against a backdrop of benign inflation, we believe that monetary authorities in India and Malaysia have room to cut interest rates to spur domestic growth. In contrast, we expect Philippine bonds to underperform, as we see the Bangko Sentral ng Pilipinas remaining on the sidelines for the foreseeable future.

- Prefer IDR and INR; cautious on PHP

We are cautious on the Philippine Peso as we see it underperforming regional currencies in the near-term, prompted in part by greater political uncertainty. Meanwhile in Indonesia, the repatriation of these funds should benefit demand for the Indonesian Rupiah. Similarly, demand for the Indian Rupee is likely to be sustained by the lower trend in inflation. In contrast, against a backdrop of sluggish global growth, the trade-reliant economies of Singapore and Korea are likely to be vulnerable.

## Asian Credits

### Market Review

- Asian credits ended higher despite wider credit spreads

Asian credits registered gains in September. Asian high-grade returned 0.11% and Asian high-yield returned 0.68%, as heavy primary supply capped bond performance in the secondary market.

- Primary market picked up momentum

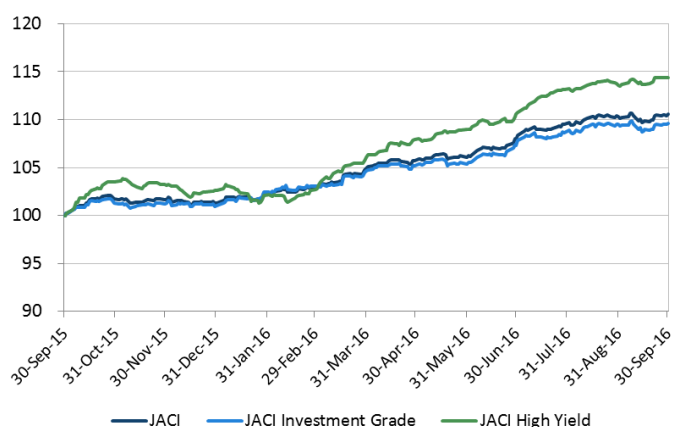
The month saw a lower number of new deals of investment-grade credits. There were a total of nine new issues – amounting to USD 4.65bn – in the high-grade space. Meanwhile, primary activity for high-yield segment picked up with 17 issues (including taps of existing issues) amounting to USD 5.1bn.

- S&P reaffirmed Philippines' credit rating but flagged uncertainties amid diminished policy stability

Credit rating agency Standard & Poor's (S&P) kept the Philippines' credit rating unchanged, but cited concern about "rising uncertainties surrounding the stability, predictability, and accountability of its new government." S&P explicitly said that an upgrade was unlikely in the next two years. Currently, the Philippines is rated 'investment-grade' by S&P, Moody's and Fitch Ratings.

### JP Morgan Asia Credit Index (JACI)

Daily returns for the period from 30 September 2015 to 30 September 2016



Note: Returns in USD. Past performance is not necessarily indicative of future performance. Source: JP Morgan, 30 September 2016

### Market Outlook

- Ongoing macro uncertainties and expected path of monetary policy to drive returns

Ongoing concerns surrounding Deutsche Bank, BREXIT by the UK government and the expected path of interest rates from the economic data releases in the US even as the Fed stayed on hold in September should remain on the center stage in October. Asian credit spreads have widened given these uncertainties and a sizeable uptick in new issuance volumes. High-grade spreads and high-yield corporate spreads are 12 basis points (bps) and 15bps wider over the month but are still below their historical averages.

- Expect supply to remain robust pressuring secondary levels

The supply of new issues is expected to remain high in the coming month. The recent pick-up of new issues in high-grade and high-yield has eroded technicals. Secondary spreads have begun to widen in face of this pick-up in supply. The uncertain macro backdrop and a sharply higher supply pipeline forecasted suggest a more cautious stance although the demand backdrop seems to remain intact for Asian credit.

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