Interest Rate Outlook & Strategy

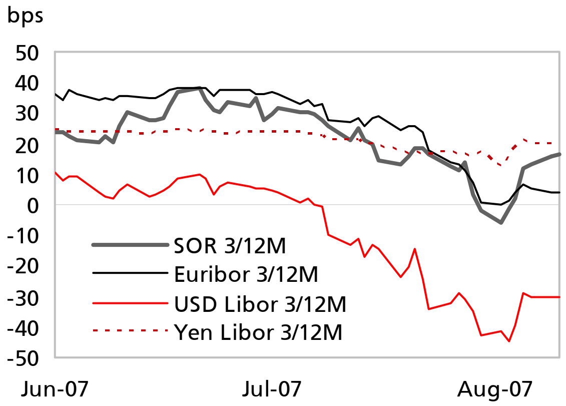
Short-term View

DBS Group Research **29 August 2007**

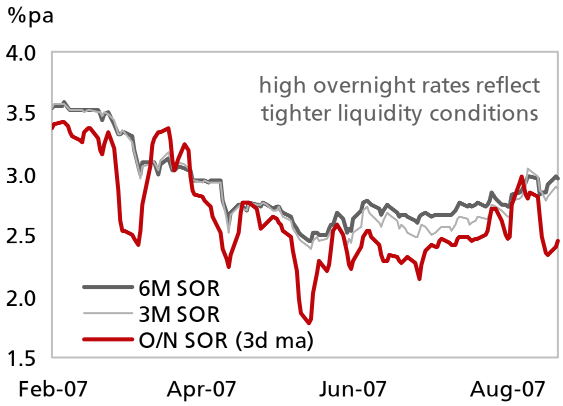
Trade: Pay 2Y SGD IRS vs Rec 10Y SGD IRS

We expect SGD money market rates to continue to rise in the coming weeks, putting upward pressure on the front end of the SGD swap curve. A re-steepening of G3 money market curves should be the main driver of this but SORs also stand to rise if credit market conditions and the US economic outlook deteriorate.

G3 & SGD Money Market Curve Spreads

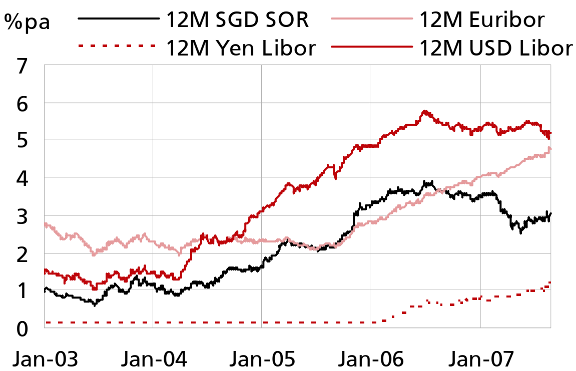


SGD money market yield trends

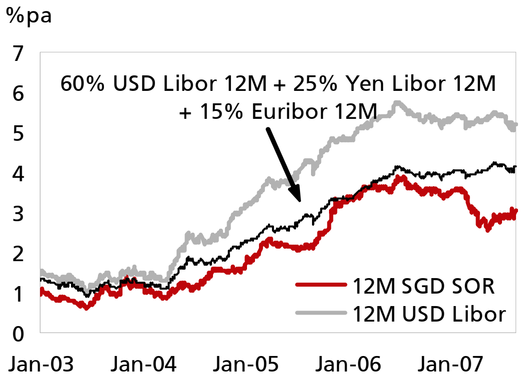


This is in line with our longer-term call for a narrowing of spreads between SGD money market rates and the weighted average of G3 money market rates (TWIBOR), which we use as a reference rate. We expect spreads to narrow although the MAS looks set to keep its tightening stance on the SGD NEER in September after both money supply and loan growth have been growing at a rapid pace of 22.4% and 8.7% respectively over the last twelve months and CPI inflation has risen to 2.6% YoY in July.

12M G3 & SGD money market rates



12M SGD SOR vs weighted average of 12M G3 interbank rates & 12M USD Libor



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With money market rates rising, shorter-term SGD swap rates are unlikely to fall further; even if the Fed cuts rates in September and USD swap rates move lower.

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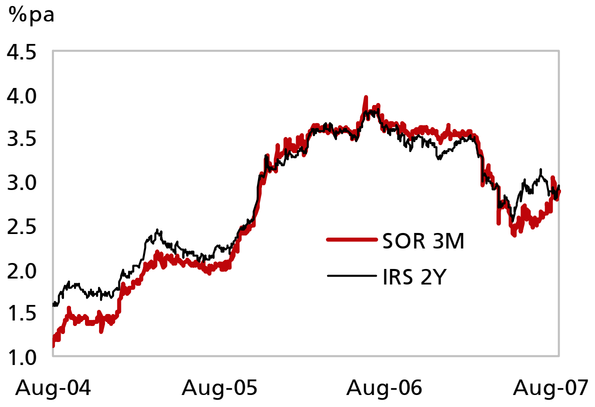
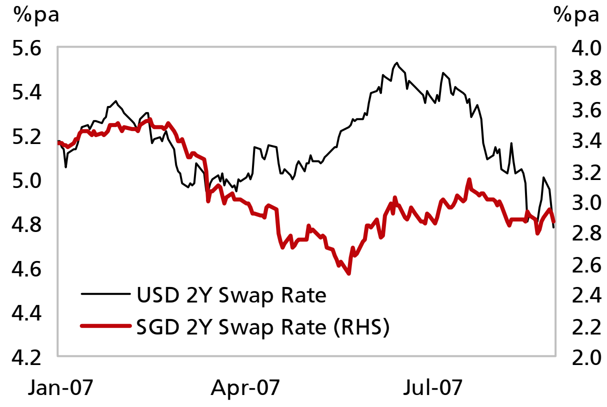
SOR 3M vs SGD IRS 2Y

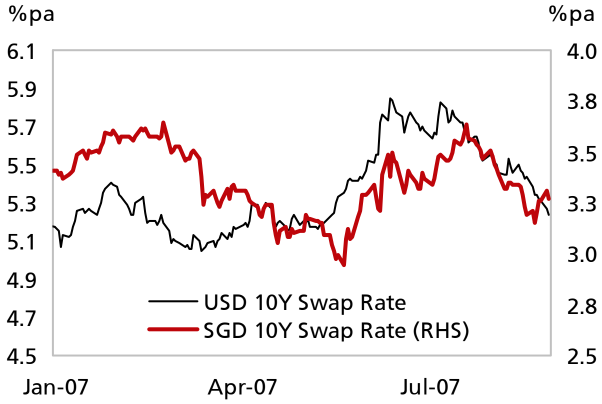


SGD IRS 2Y vs USD IRS 2Y

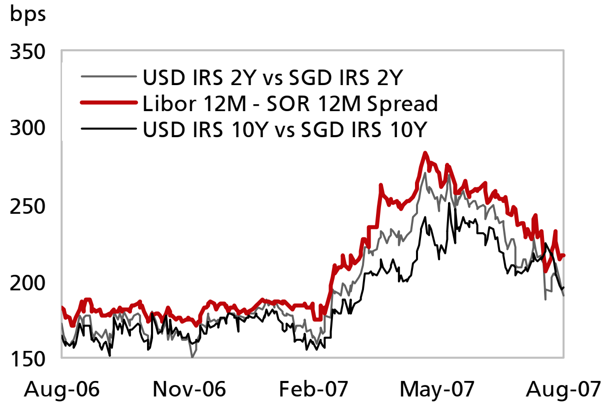


At the long end, the 10Y SGD swap rate should remain under downward pressure as USD swap rates move lower. We expect the US swap curve to bull-steepen somewhat further in the weeks ahead as expectations for Fed easing remain aggressive.

SGD IRS 10Y vs USD IRS 10Y



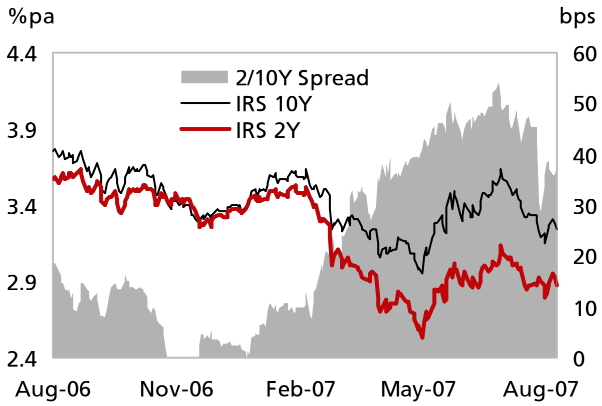
USD/SGD IRS 2Y & 10Y vs Libor12M-SOR 12M



For the SGD 2Y/10Y swap curve all this means we are likely to see a neutral flattening and narrower spreads between SGD and USD swap rates. We recommend a 2Y/10Y flattener in SGD swaps, expecting the spread to narrow to 25bps from 36bps currently (stop loss 42bps).

Position					
2s/10s		Amount	Yield	Risk	DV01
Pay	2s	1,000,000	2.90%	1.93	193
Rec	10s	225,995	3.26%	8.54	193

SGD2Y IRS vs 10Y IRS



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