

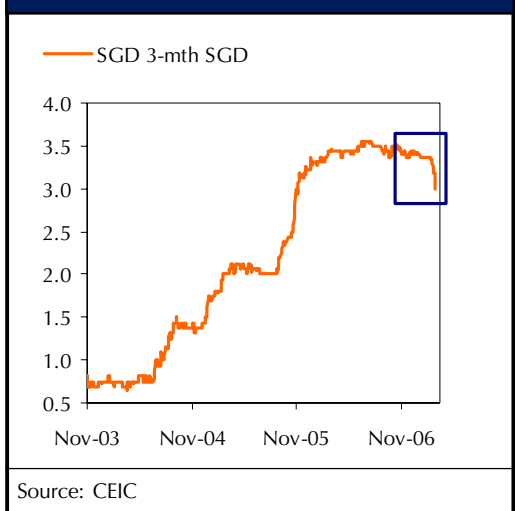
Singapore: After The Recent Sharp Drop In SGD Interest Rates

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After hovering around 3.3-3.5% since Mar 2006, the 3-mth SGD SIBOR fell to 2.93% in Mar 2007, before stabilising around 3% of late. More significantly, the drop was over a mere 2-week period, amounting to 50bps. While unwinding of global risk taking was clearly the trigger, the magnitude was probably related to the flush liquidity condition and increasingly fewer safe haven assets globally.

However, our view remains that global fundamentals have yet been eroded, and risk taking activities should eventually return. While not a perfect parallel, the unwinding of risks in May-Jun 2006 indicated the adjustment process could stretch 15-17%, and over a period of 5-6 weeks. Once the dust settles, we expect the improving domestic growth prospects, and a return of lending activities to play a more prominent role in determining SGD rates. Indeed, a more reasonable range for the 3-mth SGD SIBOR is probably around 3.2-3.5%.

Sudden Drop in SGD Interest Rates in Mar 2007



SGD Interest Rates:
Recent Moves Appears to be Exaggerated

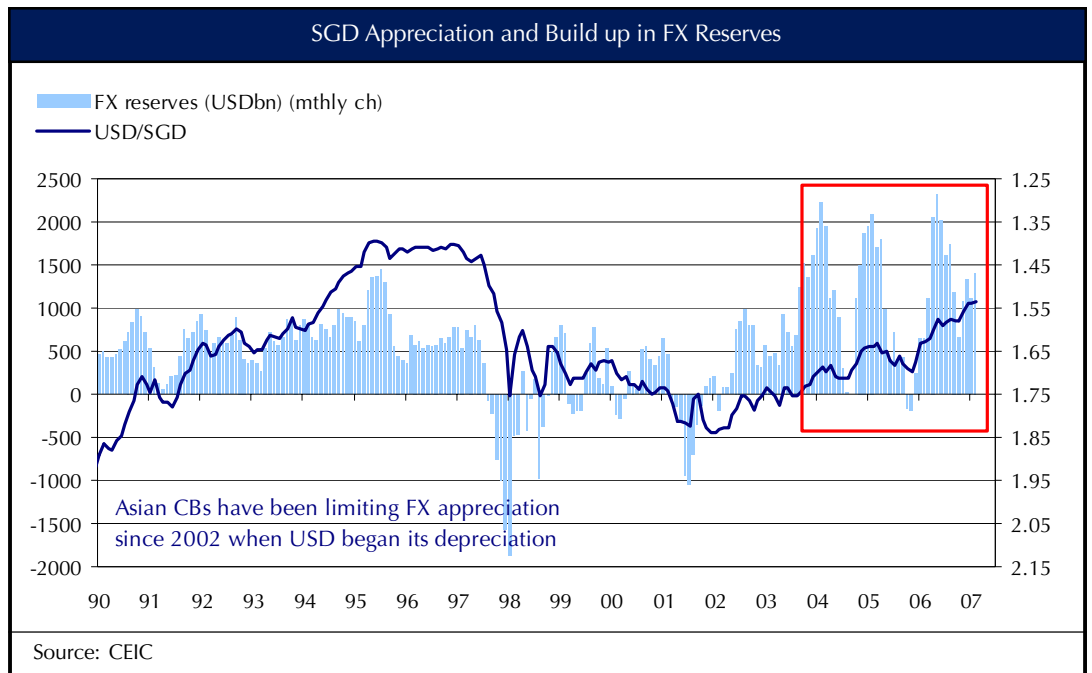


SGD Interest Rates:
Recent Moves Appears to be Exaggerated



Global liquidity and asset prices

As previously highlighted, the global system is still flush with liquidity. While inflating asset prices, it is important to note that any downside adjustment will be equally exaggerated. Also, there appears to be fewer safe-haven assets globally, as the usual risk adverse assets such as silver, gold and platinum, are now positively correlated with equities. This, we believe, could explain the extended adjustment on bond yields.

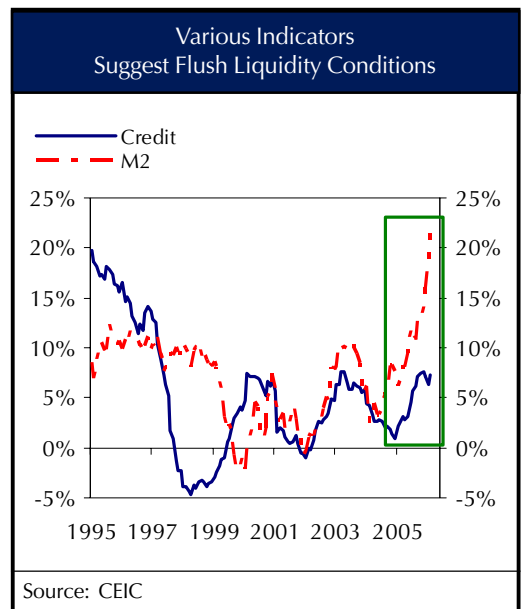
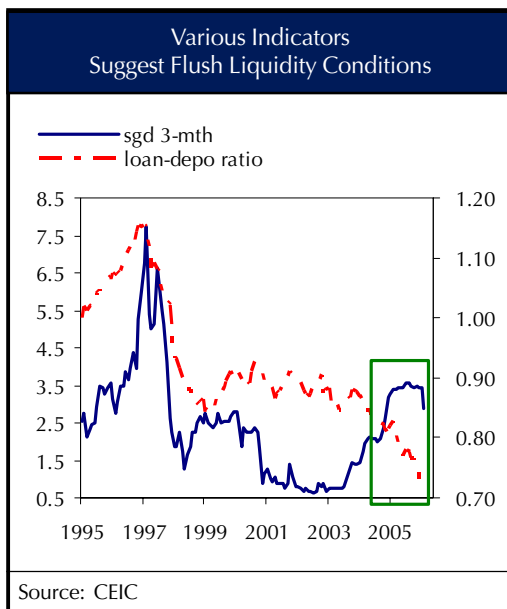
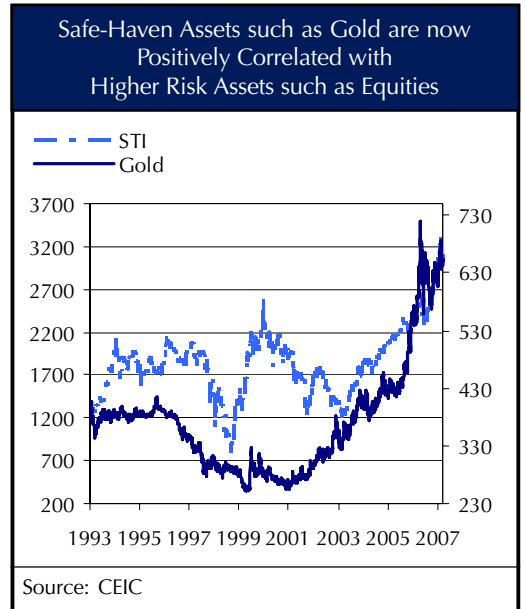


A liquid domestic system

Ample liquidity remains a dominant story in the domestic system, as reflected on common indicators such as M2 growth and loan-to-deposit ratio. SGD strength, as well as the build up in FX reserves certainly added more funds to the already liquid system. Some also suggested the transfer of funds from 'developers' to 'individuals' as a result of the massive S\$7.4bn in en-bloc activities last year. Indeed, if not for the out-performance in higher risk assets (such as equities and properties) absorbing this liquidity, SGD rates could have taken a tumble much earlier.

From here...Watch the equity markets

Our view remains that risk taking activities will eventually return, as fundamentals have yet been eroded. While there is now greater concern over



the health of the US housing, particularly the sub-prime sector, it is far from the clear its impact upon the broader economy. And, no one is really pricing in the Fed would move anytime soon. Indeed, unless it becomes clear that the Fed will move in the near future, our view is that we could be nearing the bottom on short-term yields - both US and SGD.

As for firmer rates going forward, however, it would depend very much on the extent and the duration of the on-going equities markets correction. While not exactly the best parallel, the correction in May-June 2006 could provide some indications. Then, the equity market corrected approximately 15-17%, over a period of 5-6 weeks (10 May to 26 June). The on-going correction is only into its fourth week, while the extent is about 10%. Certainly, there appears to be further downside risk, which is also reflected on the still fragile sentiment - including equities, commodities and interests in carry-trades.

However, the prospect remains positive for Singapore, in particular its assets markets. Adding in renewed life in bank lending activities, a more reasonable range for SGD 3-mth rates are probably around 3.2-3.5%. As for longer-dated yields, unless there is clear indication that the Fed would move anytime soon, we should see the 2-yr SGD IRS back towards 3.5%, and the 10-yr SGD IRS around 3.6%.

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