MARKET COMMENTARY

Fixed income market review and outlook

December 2023

Review

- The U.S. economic data released in December 2023 appears mixed. The Federal Open Market Committee ("**FOMC**") unanimously decided to maintain the target range for the federal funds rate at 5.25-5.50%, as recent indicators suggest that "growth of economic activity has slowed" from its strong pace in the third quarter. Both U.S. Personal Consumption Expenditure ("**PCE**") and Core PCE price index continued to cool to 2.6% and 3.2% respectively in November (October revised: 2.9%; 3.4%). However, the University of Michigan Consumer Sentiment index for December rebounded to 69.7 from 61.3 in the previous month. The U.S. Flash Composite Purchasing Managers' Index ("**PMI**") increased marginally to 51.0 in December from 50.7 in November, as the rise in Services PMI to 51.3 was partially offset by the decline in Manufacturing PMI to 48.2. The U.S. economy added 199,000 jobs based on Nonfarm Payroll ("**NFP**") for November, an increase compared to 150,000 in October. Unemployment rate declined to 3.7% in November compared to 3.9% recorded in the month before.

- The Bank of England ("**BOE**") in its Monetary Policy Committee ("**MPC**") meeting in December kept its bank rate unchanged at 5.25% for a third consecutive meeting, citing that "monetary policy will need to be restrictive for sufficiently long to return inflation to the 2% target". The U.K.'s inflation rate continued its downward trajectory in November to 3.9% (October: 4.6%), while its composite PMI stayed above 50 points for the second month since July 2023 at 51.7 in December (November revised: 50.7) as Services PMI increased to 52.7 despite Manufacturing PMI declining to 46.4 (November revised: 50.9; 47.2).

- The European Central Bank ("**ECB**") decided to keep its three key interest rates on the main refinancing operations, marginal lending facility and the deposit facility unchanged at 4.50%, 4.75% and 4.00% respectively. ECB stated that while inflation has dropped in recent months, it is likely to pick up again temporarily in the near term. Eurozone's composite PMI had declined to 47.0 in December from the upwardly revised 47.6 in the previous month, as both Services PMI remained flattish at 44.2 but Manufacturing PMI decreased to 48.1 from the revised figure of 48.7 in the prior month.

- The Reserve Bank of Australia ("**RBA**") in its December meeting maintained the cash rate target at 4.35%, as its members agreed that "inflation expectations remained consistent with the inflation target". In Asia, the central banks of Indonesia and the Philippines both decided to maintain their policy interest rates at 6.00% and 6.50% respectively in December. Meanwhile, Bank of Thailand and Bank Negara Malaysia ("**BNM**") did not hold any monetary policy committee meeting in December.

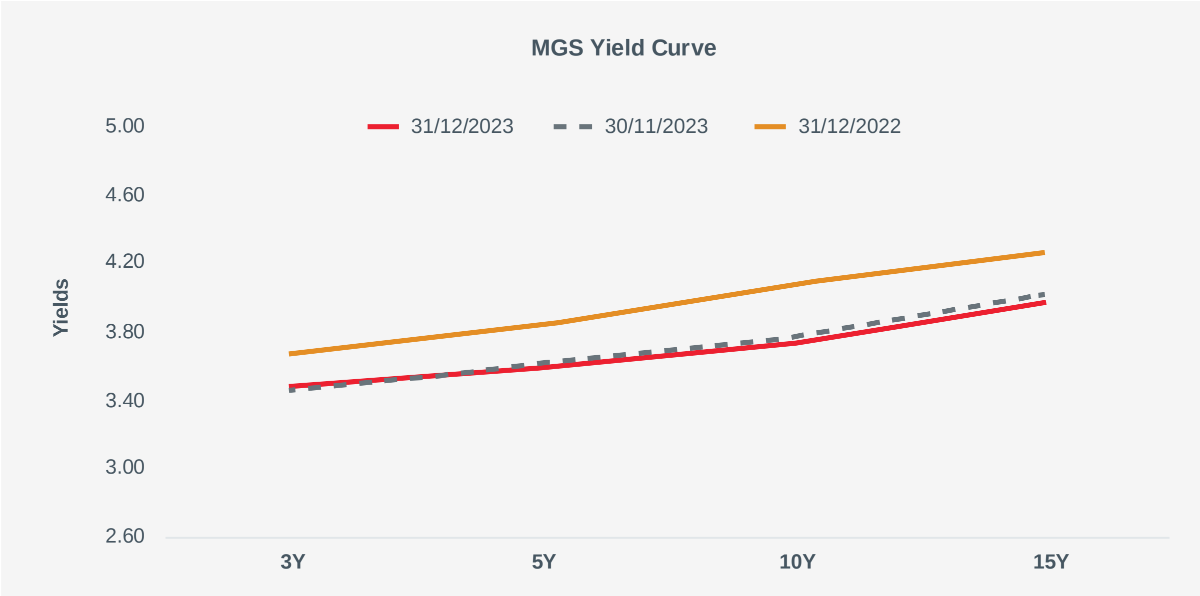
- The People's Bank of China ("**PBoC**") maintained its key lending rate, 1-year and 5-year loan prime rate ("**LPR**") at 3.45% and 4.20% respectively in December. Economic activity data from China continued to show some improvement compared to the past few months, although its economic recovery is perceived to still be fragile. China's imports declined by 0.6% YoY in November after growing by 3.0% YoY in the previous month. However, exports growth turned positive at 0.5% YoY in November compared to the revised -6.6% in October. Its retail sales grew at a stronger pace of 10.1% in November compared to 7.6% in October while the industrial production growth was also higher at 6.6% (October: 4.6%). China's fixed asset investments recorded flattish growth rate of 2.9% YoY for 11M2023 (10M2023: 2.9% YoY). Moody's reaffirmed China's A1 long-term rating on the country's sovereign bonds, but downgraded its outlook to negative from stable. The outlook change is mainly due to rising evidence of financial support by the government for distressed local governments and state-owned enterprises which could diminish China's fiscal, economic and institutional strength; as well as increased risks related to structurally and persistently lower medium-term economic growth and the ongoing downsizing of the property sector.

- Malaysia's CPI and core CPI continued to decline to 1.5% and 2.0% YoY respectively in November (October: 1.8%; 2.4%). Unemployment rate remained unchanged at 3.4% from June to October 2023. BNM international reserves increased to US$112.8bn as of mid-December (mid-Nov: US$110.5bn). The reserves position is sufficient to finance 5.5 months of imports and is 1.0x of the total short-term external debt.

- Two auctions were held in December, the re-opening 5Y MGS 04/28 and the re-opening of 10Y MGS 11/33. The auctions received an average bid-to-cover ratio of 2.471x.
  - RM5.0b re-opening 5-year MGS averaging 3.592% at a bid-to-cover ratio of 2.736x; and
  - RM4.0b re-opening 10-year MGS averaging 3.713% at a bid-to-cover ratio of 2.206x.
- Malaysia's MGS curve flattened in the month of December. The yield of 3-year MGS increased by 3 bps to 3.48% while the yields of the 5-, 10- and 15-year MGS declined by 2 bps, 7 bps and 5 bps to close the month at 3.58%, 3.74% and 3.97% respectively. The yields of MGII shifted downwards with the 3-, 5-, 10- and 15-year MGII decreasing by 7 bps, 6 bps, 9 bps and 10 bps to end the month at 3.49%, 3.61%, 3.78% and 3.93% respectively.

BENCHMARK	Dec 2022 Yield	Nov 2023 Yield	Dec 2023 Yield	MOM Change	YTD Change
3-year MGS	3.67%	3.45%	3.48%	+3 bps	-19 bps
5-year MGS	3.84%	3.61%	3.58%	-2 bps	-26 bps
10-year MGS	4.07%	3.81%	3.74%	-7 bps	-33 bps
15-year MGS	4.26%	4.02%	3.97%	-5 bps	-29 bps

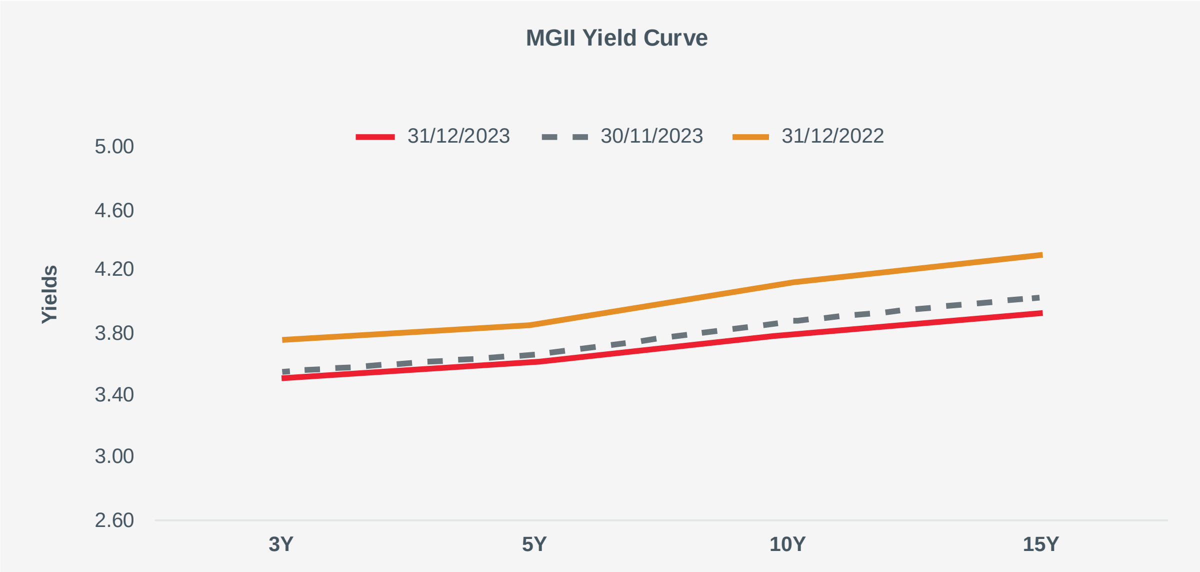
Source: Bloomberg



Source: Bloomberg

BENCHMARK	Dec 2022 Yield	Nov 2023 Yield	Dec 2023 Yield	MOM Change	YTD Change
3-year MGII	3.76%	3.56%	3.49%	-7 bps	-27 bps
5-year MGII	3.85%	3.67%	3.61%	-6 bps	-25 bps
10-year MGII	4.13%	3.87%	3.78%	-9 bps	-35 bps
15-year MGII	4.31%	4.02%	3.93%	-10 bps	-38 bps

Source: Bloomberg



Source: Bloomberg

Outlook

- After months of aggressive interest rate hikes by the central banks in developed countries, future monetary decisions will be dependent on economic data. Inflation rates seemed to have peaked in the U.S., U.K. and the Eurozone, and are declining towards the target of 2%. Heightened geopolitical risks continues with the Israel-Hamas war, on top of the ongoing Russia-Ukraine war and the tensions between U.S. and China. 2024 will also be a year of elections, with countries such as Taiwan, Indonesia and the U.S. going to the polls to vote. Although China's GDP growth may meet its government target of 5% in 2023, OECD forecasts a lower growth rate for China in 2024 of 4.7% on the back of ongoing stresses in the real estate sector and continued high household saving rates.

- For Malaysia, BNM's decision on the OPR will also be data dependent as the central bank assesses the sustainability of the domestic growth momentum, upside risks to inflation with potential subsidies rationalisation, global economic growth in developed economies and China, as well as the performance of the Ringgit. With the roll out of the targeted subsidy programme for RON95 petrol expected in the second half of 2024, inflation is expected to come in higher in 2024. Malaysia's growth momentum in the next few years will depend on the execution of the policy blueprints such as MADANI Economy, National Energy Transition Roadmap ("NETR") and New Industrial Master Plan ("NIMP").

- Based on the recently released auction calendar for 2024, there will be 37 auctions in 2024, same as in 2023. However, total MGS and GII supply is expected to be less at ~RM178 billion compared to RM185 billion in 2023 (auction and private placement). There seems to be no more new issuance of Sustainability GII planned in 2024. There will be three auctions in the month of January 2024, with the re-opening 10Y MGII 08/33, the re-opening of 30Y MGS 03/53 and the re-opening of 5Y MGII 07/28. While there is still ample liquidity in the system, the outcome of these auctions is likely to be influenced by prevailing market sentiment both from local and foreign investors. On the corporate front, we expect mixed demand for corporate bonds as investors continue to be selective in their investments.

Table 1: Indicative Rates (%)

	31-Dec-23
MBB O/N*	1.30
MBB 1-Week*	1.40
MBB 1-Mth FD*	2.70
MBB 6-Mth FD*	3.05
MBB 1-Year FD*	3.10
1-mth BNM MN	3.18
3-mth BNM MN	3.23
3-mth KLIBOR	3.77
CP	
1-mth (P1)	3.75
3-mth (P1)	3.93

Source: Bloomberg/Bondstream
* Maybank2u.com.my

Table 2: Indicative Bond Yields (%)

	3yr	5yr	7yr	10yr	15yr
MGS	3.53	3.65	3.74	3.73	3.99
GII	3.51	3.64	3.79	3.80	3.96
Swap rate*	3.49	3.58	3.71	3.82	4.05
AAA	3.83	3.90	3.97	4.05	4.25
AA1	3.92	3.99	4.09	4.17	4.41
AA2	4.00	4.08	4.20	4.30	4.56
AA3	4.08	4.17	4.30	4.43	4.73
A1	4.83	5.19	5.43	5.67	6.03
A2	5.44	5.88	6.21	6.61	7.09
A3	6.03	6.57	6.99	7.54	8.15

Source: Bloomberg*/Bondstream