MARKET COMMENTARY

FIXED INCOME MARKET REVIEW AND OUTLOOK

September 2019

REVIEW

- Bank Negara Malaysia ("BNM") in its Monetary Policy Committee ("MPC") meeting in September maintained the Overnight Policy Rate ("OPR") at 3.00%, comforted by the stronger economic growth performance in the second quarter which was underpinned by resilient private spending amid broad-based expansion in key economic sectors alongside stable labor market and wage growth. While the baseline growth projection remains at 4.3% - 4.8%, BNM acknowledged the lingering downside risks from the ongoing trade tensions and the resulting uncertainties in global and domestic environment. The overall tone of the policy statement was still neutral and the assessment on the stance of monetary policy at the point of meeting was still "accommodative and supportive of economic activity" which could suggest that BNM's future monetary policy decisions are likely to be data-dependent.

- Headline inflation in August 2019 remained relatively stable at +1.50% YoY (July: +1.4% YoY) driven by Furnishings, Household Equipment & Routine Household Maintenance (+3.2%), Food & Non-Alcoholic Beverages (+2.6%), Alcoholic Beverages & Tobacco (+2.5%), Miscellaneous Goods & Services (+2.5%), Recreation Services & Culture (+2.3%) and Communication (+2.2%). Similarly, core inflation for the month remained stable at +2.0% YoY (July: +2.0% YoY). In the short-term, direction of headline inflation is contingent on the timing of the fuel subsidy rationalization by the Government. For the full year, BNM maintains its inflation forecast at 0.70% - 1.70%.

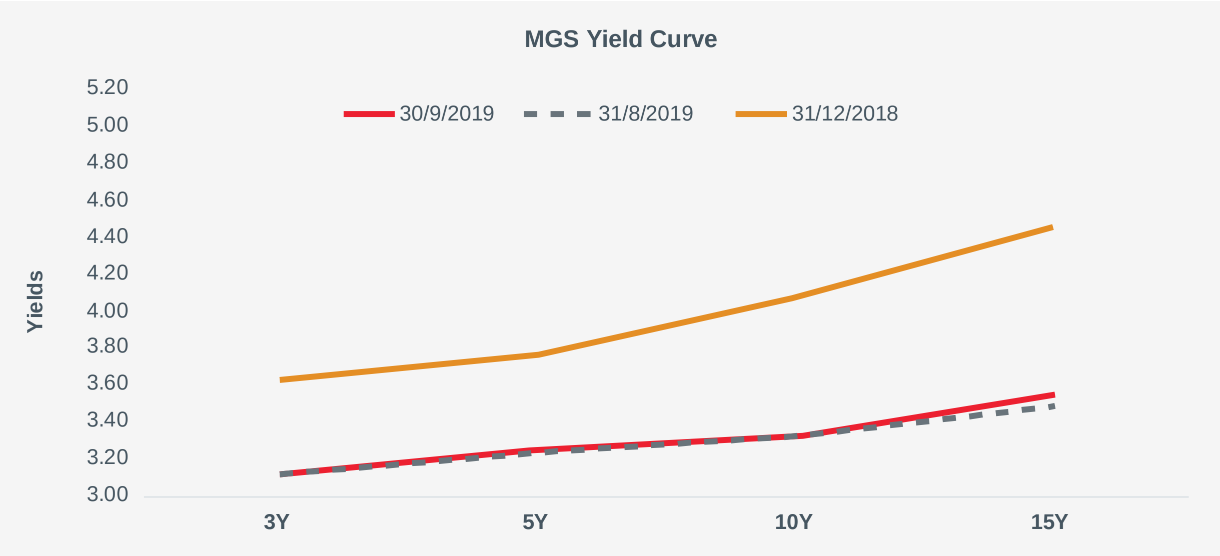
- Malaysia sovereign bond curve bear-steepened in September with yields for 5- and 15-years MGS moved higher by 1-7 bps to close higher at 3.24% and 3.55%, respectively. Yields on the 3- and 10-years on the other hand remained unchanged at 3.12% and 3.32%, respectively, resulting in a steeper curve. In September, the steepening of sovereign bond curve was consistent with the movement in US Treasury ("UST") curve, on the back of news on the restart of US-China talk which led to global risk-on mode and the unwinding of expectation on Federal Reserve's ("Fed") aggressive monetary easing following its September meeting where the forward guidance was less dovish than the market expected. MGII yield curve also steepened in the month and ended mixed, with 3-year moved 1bp lower to 3.12% and 5-years moved 4bps lower to 3.21% while the 10- and 15-years moved higher by 4 and 13bps to close at 3.40% and 3.64% respectively.

- There were three government bond auctions in September:
  - RM3.0b re-opening of the 7-year MGS averaging 3.392% at a bid-to-cover ratio of 1.26x.
  - RM2.0b re-opening of the 15-year MGII averaging 3.632% at a bid-to-cover ratio of 3.195x.

- Meanwhile, trading in corporate bonds for the month of September mostly concentrated in selected quasi-government and AAA rated bonds.

BENCHMARK	31/12/2018 Yield	30/8/2019 Yield	30/9/2019 Yield	MOM Change	YTD Change
3-year MGS	3.62%	3.12%	3.12%	-	- 50 bps
5-year MGS	3.76%	3.23%	3.24%	+ 1 bps	- 52 bps
10-year MGS	4.07%	3.32%	3.32%	-	- 75 bps
15-year MGS	4.44%	3.48%	3.55%	+ 7 bps	- 89 bps

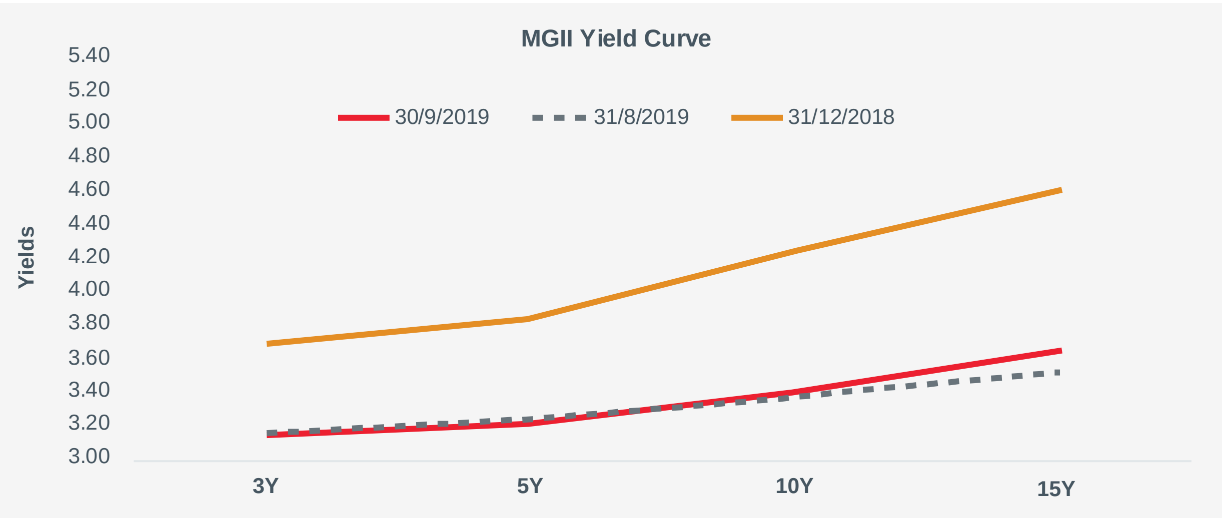
Source: Bloomberg



Source: Bloomberg

BENCHMARK	31/12/2018 Yield	30/8/2019 Yield	30/9/2019 Yield	MOM Change	YTD Change
3-year MGII	3.68%	3.13%	3.12%	- 1 bps	- 56 bps
5-year MGII	3.83%	3.25%	3.21%	- 4 bps	- 62 bps
10-year MGII	4.24%	3.36%	3.40%	+ 4 bps	- 84 bps
15-year MGII	4.61%	3.51%	3.64%	+ 13 bps	- 97 bps

Source: Bloomberg



Source: Bloomberg

OUTLOOK

- In the US, FOMC delivered its consequential second interest rate cut in the September meeting. The cut was attributed to “implications of global developments for the economic outlook as well as muted inflationary pressures”. However, the policy statement is counterbalanced by “sustained expansion of economic activity, strong labor market conditions, and inflation near the Committee's symmetric 2 percent objective”. In the accompanying press conference, Chairman Powell described the rate cut as a modest adjustment as compared to "mid-cycle adjustment" back in July. Powell also stressed that moving forward the Federal Reserve will be “highly” data dependent, despite the market’s expectation for an aggressive easing cycle.

- On the trade war front, the markets cheered on the news of US and China restarting the trade discussion. In a phone call between the countries’ two high officials in early September, a new round of high-level talks in early October has been agreed between the two. Should it take place, the meeting will be the first in-person, high-level discussion since the failed US-China trade meeting in July which prompted the August announcement of new tariffs by President Trump. While the news has renewed hope of a trade resolution between the two economies, investors remained skeptical due to the US and China deep differences over the former’s demands for sweeping changes to China’s practice on intellectual property protections, transfers of US technology to Chinese companies and curbs on subsidies to China’s state-owned enterprises. Market will be following the progress of the talk closely and given that little clarity in sight at the moment, the lingering uncertainties will continue to weigh on global sentiments and add volatilities to the market.

- In the immediate future, sentiment in the domestic fixed income will be determined by the details in Budget 2020 which will be tabled on 11 October 2019. Economists predict the government to table an expansionary budget, pump-priming the domestic economy to counter the already weak external environment going into year 2020. The government is widely expected to deviate from the 3% fiscal deficit target in 2020 as set in the Medium-Term Fiscal Framework 2019-2021. Nonetheless, Budget 2020 is anticipated to strike a balance between maintaining fiscal discipline and being pro-growth.

- In October, there will be three MYR government bond auctions, re-opening of 5- and 10-year MGS and re-opening of 20-year MGII against a RM11.8 billion MGS maturity. The trend of healthy bid-to-cover ratio from the previous government bond auctions is expected to continue on the back of ample domestic liquidity.

- On the corporate bond front, the pickup in new issuances is expected to be sustained in October from refinancing activities on the back of upcoming corporate bond maturities, and the relatively low-interest rate environment which is favorable for issuers. We expect demand for corporate bonds to remain strong due to 1) scarcity of quality corporate bond supply and 2) ample domestic liquidity.

Table 1: Indicative Rates	
	30-Sep-19
MBB O/N*	1.60%
MBB1-Week*	1.70%
MBB 1-Mth FD*	2.90%
MBB 6-Mth FD*	3.05%
MBB 1-Year FD*	3.10%
1-mth BNM MN	3.05%
3-mth BNM MN	3.07%
3-mth KLIBOR	3.38%
CP	
1-mth (P1)	3.43%
3-mth (P1)	3.67%

Source: Bloomberg/Bondstream
* Maybank2u.com.my

Table 2: Indicative Bond Yields (%)

	3 yr	5yr	7yr	10yr	15yr
MGS	3.14	3.25	3.34	3.36	3.55
GII	3.14	3.22	3.39	3.40	3.64
Swap rate*	3.27	3.31	3.34	3.37	3.48
AAA	3.52	3.62	3.71	3.79	4.02
AA1	3.68	3.78	3.89	4.02	4.28
AA2	3.82	3.92	4.03	4.16	4.42
AA3	3.94	4.05	4.15	4.28	4.54
A1	4.45	4.79	5.08	5.51	6.13
A2	5.14	5.70	6.09	6.68	7.49
A3	5.84	6.54	7.01	7.70	8.58

Source: Bloomberg*/Bondstream