A member of Prudential plc (UK)

# MARKET COMMENTARY

## FIXED INCOME MARKET REVIEW AND OUTLOOK

March 2019

# REVIEW

- On the domestic front, the second Monetary Policy Committee ("MPC") meeting for 2019 held on 5 March saw Bank Negara Malaysia ("BNM") maintained the Overnight Policy Rate ("OPR") at 3.25%. Bank Negara believes that the current level of the OPR is consistent with its intended policy stance. Bank Negara expects domestic growth to be sustained in 2019 but materialization of downside risk from unresolved trade tension could weigh on growth.

- According to Bank Negara's Annual Report 2018, the central bank has revised lower the country's real Gross Domestic Production ("GDP") growth target for FY2019 to be in the range of between 4.3% to 4.8% (4.7% in 2018), as compared to the government's earlier projection of 4.9% for 2019. This is in line with the lower International Monetary Fund's ('IMF") global growth expectation of +3.5% in 2019, lower than +3.7% in 2018, but still within the long-term average range of 3.5%. BNM also lowered its inflation target to a range of between 0.7%-1.7% in 2019, as compared to the earlier government's forecast of 2.5-3.5%. BNM lowered its forecast on the back of its expectation of lower global oil prices as well as recent implementation on the cap on prices of RON95 and diesel until the middle of 2019.

- Separately, February'19 headline inflation moderated higher to -0.4% YoY compared with -0.7% YoY January. The increase in inflation was mainly due to smaller decrease in transportation costs (Feb: -6.8%, Jan: -7.8% YoY) while Housing, Water, Electricity, Gas & Other Fuels continued to increase at +2.0% YoY (Jan: +2.0% YoY) and Food & Non-Alcoholic Beverages increased by +1.0% YoY (Jan: +1.0% YoY). On the other hand, core inflation increased to +0.3% YoY in February from +0.2% YoY in January.

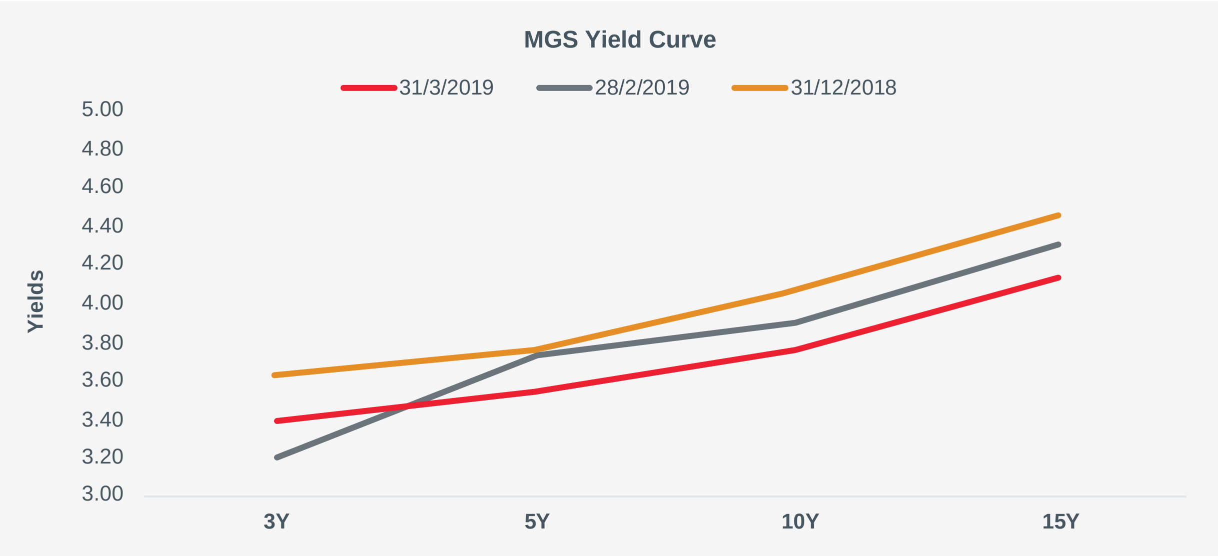
- Malaysia sovereign bonds yields for 5-, 10- and 15-years MGS continued to decrease by 12-19bps in March to close lower at 3.53%, 3.77% and 4.12% respectively while the 3-year MGS yield increased by 19bps to close at 3.38%. In March, sovereign bonds yields moved due to continued buying interest from local investors. Similarly, MGII yields 3-, 5-, 10- and 15-years moved lower by 15-26bps respectively to close at 3.49%, 3.60%, 3.81% and 4.11% respectively.

- There were three government bond auctions in March:
  - RM3.0b re-opening of the 3-year MGS averaging 3.483% at a bid-to-cover ratio of 3.132x.
  - RM2.5b new issue of the 20.5-year MGII averaging 4.467% at a bid-to-cover ratio of 2.758x.
  - RM2.0b re-opening of the 30-year MGS averaging 4.591% at a bid-to-cover ratio of 1.718x.
  - RM4.0b new issue of the 7-year MGII averaging 3.726% at a bid-to-cover ratio of 2.330x

- Meanwhile, trading in corporate bonds increased in the month of March with most trades concentrated in selected quasi-government and AAs rated bonds.

| BENCHMARK | 31/12/2018 Yield | 28/2/2019 Yield | 29/3/2019 Yield | MOM Change | YTD Change |
|---|---|---|---|---|---|
| 3-year MGS | 3.62% | 3.19% | 3.38% | +19 bps | -24 bps |
| 5-year MGS | 3.76% | 3.72% | 3.53% | -19 bps | -23 bps |
| 10-year MGS | 4.07% | 3.89% | 3.77% | -12 bps | -30 bps |
| 15-year MGS | 4.44% | 4.29% | 4.12% | -17 bps | -32 bps |

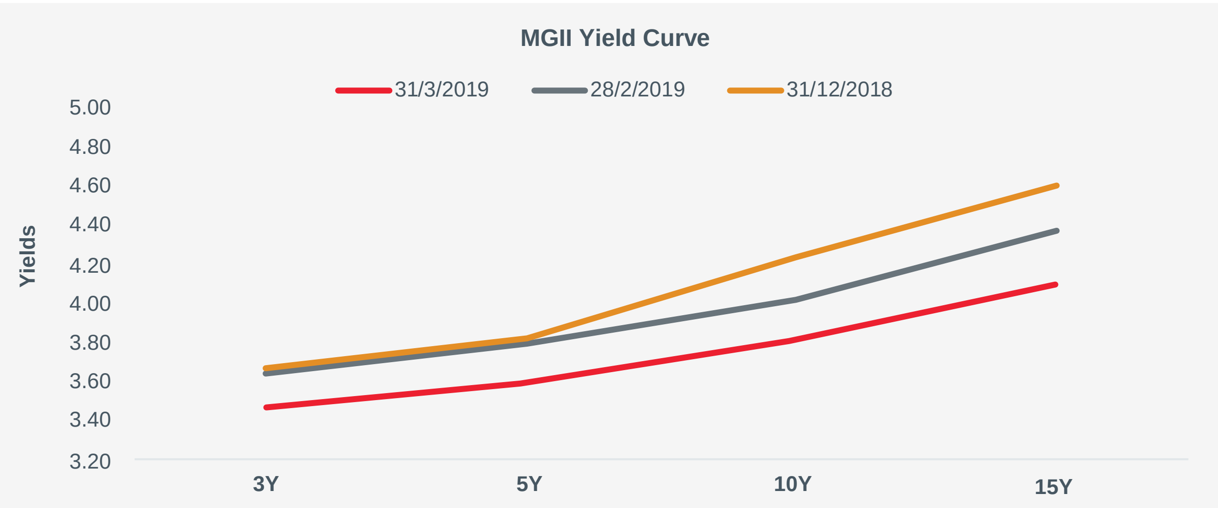
Source: Bloomberg




Source: Bloomberg

| BENCHMARK | 31/12/2018 Yield | 28/2/2019 Yield | 29/3/2019 Yield | MOM Change | YTD Change |
|---|---|---|---|---|---|
| 3-year MGII | 3.68% | 3.64% | 3.49% | -15 bps | -19 bps |
| 5-year MGII | 3.83% | 3.81% | 3.60% | -21 bps | -23 bps |
| 10-year MGII | 4.24% | 4.03% | 3.81% | -22 bps | -43 bps |
| 15-year MGII | 4.61% | 4.37% | 4.11% | -26 bps | -50 bps |

Source: Bloomberg




Source: Bloomberg

# OUTLOOK

- In the US, the Federal Open Market Committee (“FOMC”) kept rates unchanged in the range of 2.25%-2.50% during March’s as expected. However, the US Federal Reserve (“Fed”) turned more dovish as the Fed lowered its median assessment on the Federal Fund Rate to no hike in FY2019 from two hikes previously. The Fed acknowledged that the labor market remains strong, but that growth of economic activity has slowed from its solid rate in the fourth quarter. In light of global economic and financial developments and muted inflation pressures, the Committee will continue to be patient as it determines what future adjustments to the target range for the federal funds rate may be appropriate to support these outcomes.

- Separately, the Committee also discussed on the possibility to scale back its balance sheet reduction plan. The Committee indicated that it will stop the unwinding at the end of September 2019. The Fed has set an unwinding schedule of USD50billion in April and then USD35billion for each of the next five months through September. As a result, the Fed is expected to reduce its balance sheet down to USD3.7trillion from USD4.5trillion when the central bank began its balance sheet reduction plan two years ago.

- On the domestic front, the third Monetary Policy Committee (“MPC”) meeting for 2019 will be held on 7 May. In March, Bank Negara left the OPR unchanged at 3.25% but caution on the unresolved global trade tension which may impact domestic growth. We expect BNM to monitor the domestic and global economy further before making any changes to its monetary policy stance. Bank Negara’s will need to assess its monetary policy stance going forward to ensure its monetary policy remains supportive for sustainable economic growth amid the subdued inflation outlook.

- In April, there will be three MYR government bond auctions, a re-opening of a 15-year MGS, a new issue of 5.5y MGII and a re-opening of 7-year MGS. There will also be a maturity of around RM10billion of MGII during the month. Sovereign bonds yields are expected to remain volatile given the global economic uncertainties while investors continue their search for yields. Nevertheless, we expect domestic sovereign bond market to remain supported by ample liquidity and strong investor demand.

- On the corporate bond front, the market is expected to see a continuous supply in the April as yields have decreased over the past three months which is favorable for issuers. We expect demand for corporate bonds to remain strong due to scarcity of quality corporate bond supply.

| Table 1: Indicative Rates | | |
|---|---|---|
| | | **31-Mar-19** |
| MBB O/N* | | 1.90% |
| MBB1-Week* | | 2.00% |
| MBB 1-Mth FD* | | 3.15% |
| MBB 6-Mth FD* | | 3.30% |
| MBB 1-Year FD* | | 3.35% |
| | | |
| 1-mth BNM MN | | 3.26% |
| 3-mth BNM MN | | 3.28% |
| 3-mth KLIBOR | | 3.69% |
| | | |
| **CP** | | |
| 1-mth (P1) | | n/a |
| 3-mth (P1) | | n/a |

Source: Bloomberg/Bondstream
* Maybank2u.com.my

| Table 2: Indicative Bond Yields (%) | | | | | |
|---|---|---|---|---|---|
| | **3 yr** | **5yr** | **7yr** | **10yr** | **15yr** |
| MGS | 3.39 | 3.59 | 3.71 | 3.76 | 4.13 |
| GII | 3.49 | 3.66 | 3.73 | 3.81 | 4.14 |
| Swap rate* | 3.54 | 3.63 | 3.74 | 3.92 | 4.10 |
| AAA | 4.13 | 4.22 | 4.29 | 4.37 | 4.64 |
| AA1 | 4.24 | 4.34 | 4.41 | 4.49 | 4.77 |
| AA2 | 4.34 | 4.44 | 4.51 | 4.59 | 4.89 |
| AA3 | 4.46 | 4.55 | 4.62 | 4.70 | 4.99 |
| A1 | 5.17 | 5.52 | 5.84 | 6.18 | 6.83 |
| A2 | 6.00 | 6.54 | 6.92 | 7.45 | 8.25 |
| A3 | 6.82 | 7.45 | 7.91 | 8.56 | 9.42 |

Source: Bloomberg*/Bondstream